ISLE OF ANGLESEY COUNTY COUNCIL

COMMITTEE :	**COUNTY COUNCIL**
DATE :	**5 MARCH 2013**
TITLE OF REPORT :	**BUDGET 2013-14**
PURPOSE OF REPORT :	**TO DEAL WITH STATUTORY MATTERS**
REPORT BY :	**HEAD OF FUNCTION (RESOURCES)**
ACTION :	**ADOPT RESOLUTION**

1. INTRODUCTION

The Executive have formulated their proposals to the Council in respect of the 2013-14 budget and the medium term strategy. These are outlined in a separate report in the name of the Executive.

In order to adopt its budget for the year 2013-14 and to determine the level of Council Tax for the year, the County Council is required to adopt a formal resolution which deals in some detail with all connected matters.

This report is my formal advice to the Council as a whole concerning the budget. It deals with statutory matters and other matters required to complete the advice on the budget. The draft budget resolution is intended to give effect to the Executive proposals and take account of this advice.

This report is based on the Executive's final budget proposals on the assumption that these will be carried by the Council. If there is any amendment to these proposals, I may need to reconsider this report. To assist me to do so, the Budget Procedure Rules in the Council Constitution 4.3.2.2.6 provide that three working days' notice of an amendment should be given.

2. ROBUSTNESS OF ESTIMATES

I am required under section 25 (1) (a) of the Local Government Act 2003 to report to the Council on the robustness of estimates made in the course of drawing up the budget. In this year's more challenging situation facing local authorities, CIPFA's Chief Executive has this year again reminded Chief Finance Officers of their duties in this respect. This assessment summarises my report to the Executive, in which I referred to the following risks potentially affecting the robustness of estimates:

Inflation risk;
Interest rate risk;
Grants risk;
Income risk;
Optimism risk;
Over-caution risk;
Salary and grading risk;
Risk of slippage on achievement of savings;
Specific significant risks against identified items of income and expenditure.

I concluded that optimism risk and salary and grading risk were the greatest. Looking at the financial position estimated for the 2012-13 outturn and the contribution of non-achievement of savings to this, there is a further significant risk of slippage in the delivery of the savings programme.

I also drew attention to the risk that, having not completed its salary and grading review, and already having a number of equal pay claims lodged at the Employment Tribunal, the Council may be required to pay compensation claims to staff because of alleged unfairness of its pay arrangements. The revised proposals implemented in 2012-13 are expected to reduce staff costs but may risk more claims, although the risks to the Authority in all scenarios have been carefully evaluated by the Pay and Grading Panel. The Panel has met regularly throughout 2012-13 and it has been recommended that Job Evaluation and Equal Pay considerations should be dealt with together. A timetable has now been agreed for implementation of Job Evaluation which will finalise matters in April 2014. Job Evaluation is a long-standing risk which is now coming to fruition, and challenges the robustness of the budget as in previous years. In mitigation, there remains an annual contingency budget (reduced to £450k in 2013-14) towards the cost of the new pay structure and an accumulated reserve which, by March 2013, is projected at about £2.5m. The Medium Term Revenue Budget Plan has been amended to cover projected costs of implementation.

Looking to the medium term, there is a risk to the Authority from national economic conditions. Inflation affecting pay and prices may affect what can be afforded within the indicative funding totals announced by WG. Further decline in the economy may threaten those spending totals. There is also a risk that adverse demographic changes, or lower than average increases compared to the rest of Wales, will reduce this Authority's share of the national total. In a situation where the budget gap has not yet been bridged for 2014-15 and 2015-16, the prospect of deterioration means a need to over-plan and over-achieve savings.

3. ADEQUACY OF RESERVES

Under section 25(1)(b) of the Local Government Act 2003, I am required to report to the Council on the adequacy of financial reserves. Formally this relates to the reserves at the start and at the end of the financial year of the budget. Again, CIPFA's Chief Executive has commented on this requirement, and also specifically commented on the need for the level of balances to be based on local decisions.

Earmarked reserves have been established to deal with known commitments, plans or risks. In assessing the level of reserves, I have assumed that commitments will be honoured, that plans, if still planned, will be delivered, and the provision for risk is reasonable given its amount and likelihood. The assessment of general balances considers risks and uncertainty not provided for as earmarked reserves or contingency budget.

The level of reserves is reviewed regularly. This assessment draws on the report to the Executive in December 2012 and updated in the report to the Executive on 18 February, which took account of the third quarter budget monitoring report for 2012-13.

In these reports, we referred to:

- A projected level of balances of £4.4m by year end - £0.5m lower than planned;
- Earmarked reserves being generally appropriate, although low in comparison with other councils, with £0.1m identified as no longer being required;
- Schools reserves becoming more variable and a greater number in deficit.

The projected financial position for 2012-13 leads to the general balances being below the level I would judge “adequate”, in view of the current economic situation and the risks for future years, £500k has been set aside in 2013-14 for ‘the cost of change’ which will enable some of the main services to transform the way those services are delivered. Inevitably, with the level of reductions in expenditure deemed necessary, based on the projections in the three year strategy, staffing levels may need to reduce or change. In consequence, I am proposing to set aside £1m in the budget to finance severance costs and other related one off costs.

The projected level of general balances of £4.4m is too low in the context of the continuing economic pressures and as a result, I am recommending that a sum of £500k is used to replenish general balances in 2013-14. It is vital that a system is in place to monitor the achievement of this year’s savings and bring forward a programme of additional cuts for 2014-15 and future years. Achievement of these savings will be closely monitored by the programme management through the Transformation Plan. Continuing slippage and non- achievement of previous year savings programmes continue to pose a challenge and both addressing these, and ensuring the timely achievement of the latest proposals is vital to maintaining the robustness of the Council’s financial position.

4. ACHIEVING THE BUDGET

Once the 2013-14 budget is agreed there will be a further efficiency programme to develop the service efficiencies for the next three years. There are also areas remaining from the APP to be explored. This will provide an opportunity to review the whole savings programme and ensure that robust arrangements are in place to support these so that the budget next year and in future years is achievable. Key to achieving delivery of all budgets will be bringing under control those budgets which are in deficit, including schools. As well as focusing on efficiencies, there is clearly a risk relating to funding streams and general income. Work has been done in 2012-13 on a number of areas which should have been identified to support the funding and income:

- A project to optimise numbers registered as eligible for school meals;
- Closer monitoring of specific grants;
- Programme of Council Tax discount and exemption reviews;
- Closer monitoring of fees and charges.

As in 2012-13, the 2013-14 programme of savings and efficiencies is more significant than in previous years, and brings with it additional risks. It is clear that these savings programmes need to be managed as a fundamental part of the corporate budget monitoring arrangements and risk assessed. The key areas identified as a risk to the Council in terms of delivering both the savings programme and the base budget will need both strong project management and financial support to assist in achieving delivery of the overall budget. This will be done through the programme management arrangements set out in the new Transformation Plan. These will be put in place shortly to maximise the use of project and financial management skills and resources to manage the whole Council budget.

5. THE PRUDENTIAL CODE AND TREASURY MANAGEMENT

The legislative framework introduced by the Local Government Act 2003 requires the Council to have regard to The Prudential Code for Capital Finance in Local Authorities. The Executive has already affirmed this. The primary requirements of the Prudential Code are that authorities should have regard to affordability and prudence.

Affordability

The Executive's budget proposals have regard to affordability. As always, the capital budget is financed by a combination of external grants, capital receipts, revenue funds and borrowing. Anticipated funding from grants is linked to what is approved or realistically achievable; some spending proposals are to be included in the capital budget but subject to confirmation of grants: if the grants are not confirmed, the schemes will fail. Capital receipts are based on sales made or in progress or included in the agreed Outcome Agreements with WG; amounts expected but not yet confirmed as definite have been discounted, with any surplus or shortfall being carried forward to future years' budgets. Revenue funding is in place, consistent with the revenue budget.

Unsupported Borrowing

The Treasury Management report deals with the circumstances in which unsupported borrowing is used. This year, the contingent use of unsupported borrowing by the Council Fund to support spend-to-save schemes continues, but larger projects are deferred.

The Treasury Management Strategy includes the Local Government Borrowing Initiative funding for the three years from 2012-13. Borrowing projections have been increased by the Authority's estimated share of £170m for Wales (up to £5.25m). Although specific revenue grant was received to cover the modelled cost of debt repayment in 2012-13, this now becomes part of RSG.

The medium term revenue budget strategy had allowed for capital financing costs of up to an additional £5 million a year of unsupported borrowing in order to compensate for loss of WG capital and to help fund the asset rationalisation programme. This helps to demonstrate that such borrowing would be affordable. This has been deferred to 2014-15. However, the interim capital budget and the proposed Treasury Management policy do not assume this borrowing will take place, and the Council has not yet been asked to authorise this additional level of borrowing. Only when specific capital expenditure plans are in place that requires this borrowing will the Council be asked to authorise this.

Local Authority Mortgage Scheme

The Housing Service is working on a proposal to take part in a national initiative to support the provision of mortgages by the banking sector for first time buyers. Effectively, the Authority uses the strength of its balance sheet to guarantee the loans. Again, the proposed Treasury Management Policy does not assume this initiative will be adopted locally, and the Council is not yet asked to authorise implementation. Only when specific proposals are in place will the Council be asked to authorise them.

Treasury Management Strategy

The necessary Treasury Management policies are included this year in Appendix 4 to this report. I recommend that these should be adopted.

6. COUNCIL RESOLUTION

The draft Council resolution covers all matters on which a decision is required arising out of the Executive's proposals and this report.

The Council's draft budget requirement includes formal levies by the following bodies:-

£	2013-14	2012-13 COMPARISON
North Wales Fire Authority	3,219,270	3,236,550
Malltraeth Marsh Internal Drainage Board	1,870	1,870
Board of Conservators of Towyn Trewan	1,500	1,500

and the draft resolution includes precepts by the Police and Crime Commissioner, North Wales the 40 community councils as separate items at 6 dd and 7.

7. OVERALL POSITION

Having regard to the Budget Strategy, to economic projections and to the reported position on robustness of estimates and adequacy of reserves, my recommendation is that the increase in council tax for 2013-14 should be no lower than 5% and that the target level of general balances should be no lower than £5m.

CLARE WILLIAMS **21 FEBRUARY 2013**
HEAD OF FUNCTION (RESOURCES)

TABLE

TREASURY MANAGEMENT STRATEGY STATEMENT

ANNUAL INVESTMENT STRATEGY, MINIMUM REVENUE PROVISION POLICY STATEMENT AND TREASURY MANAGEMENT POLICY STATEMENT 2013/14

1. Introduction

1.1 Background

The Council is required to operate a balanced budget, meaning that total revenue due during the financial year must be sufficient to meet expenditure, and also that actual cash inflows must be adequate to cover cash outflows. A key part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's low risk approach, ensuring adequate liquidity before considering investment return.

The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer term cash flow planning to ensure that the Council can meet its capital spending obligations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses. On occasion, debt previously drawn may be restructured to meet Council risk or cost objectives.

A particular point is that a local authority must calculate its budget requirement for each financial year to include the revenue costs that flow from capital financing decisions. This means that:-

- increases in revenue costs resulting from increases in interest charges, incurred to finance additional borrowing to finance capital expenditure; and
- any increases in running costs from new capital projects, must be limited to a level which is affordable within the Council's projected income.

The Treasury Management Policy Statement defines the policies and objectives of the treasury management activities. See Appendix 9.

1.2 Reporting Requirements

The Council is required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of polices, estimates and actuals. These reports are required to be adequately scrutinised by committee before being recommended to the Council. This role is undertaken by the Audit Committee.

Prudential and Treasury Indicators and Treasury Strategy - The first and most important report, covers:-

- the Treasury Management Strategy (how the investments and borrowings are to be organised) including treasury indicators;
- an investment strategy (the parameters on how investments are to be managed);
- a Minimum Revenue Provision (MRP) Policy (how residual capital expenditure is charged to revenue over time); and
- a Treasury Management Policy Statement (definition of the policies and objectives of the treasury management function).

Reporting is also required on the capital plans (including the associated prudential and treasury indicators).

A Mid Year Treasury Management Report - This will update members with the progress of the capital position, amending prudential indicators as necessary, and whether the treasury strategy is meeting its objectives or whether any policies require revision. Rather than this minimum requirement, these reports will be produced quarterly (with quarters one and three being reported only to the Audit Committee).

An Annual Treasury Report - This provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

1.3 Treasury Management Strategy for 2013/14

The suggested strategy for 2013/14 in respect of the following aspects of the treasury management function is based upon the treasury officers' views on interest rates, supplemented with leading market forecasts provided by the Council's treasury advisor, Sector Treasury Services.

The strategy for 2013/14 covers two main areas:-

Capital Issues

- the capital plans and the prudential indicators; and
- the minimum revenue provision (MRP) strategy.

Treasury management Issues

- the current treasury position;
- treasury indicators which will limit the treasury risk and activities of the Council;
- prospects for interest rates;
- the borrowing strategy;
- policy on borrowing in advance of need;
- debt rescheduling;
- the investment strategy;
- creditworthiness policy; and
- policy on use of external service providers.

These elements cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, the WG MRP Guidance, the CIPFA Treasury Management Code and the WG Investment Guidance.

1.4 Training

The CIPFA Code requires the responsible officer to ensure that Members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsible for scrutiny. In October 2012 Member training on treasury management issues was undertaken in order to support the scrutiny role of members of the Audit Committee. Further training will be arranged as required.

The training needs of treasury management officers are periodically reviewed.

1.5 Adoption of the Code

The Council is required to indicate if it has adopted the CIPFA Code of Practice on Treasury Management. This original, 2001 Code, was adopted on 5 March 2002 by the full Council, a revised Code was adopted on 4 March 2010 and the current, 2011, Code now requires adoption.

2. Capital Considerations

The Council's current capital expenditure projection for 2013/14 is set out below. In respect of the years after 2012/13, the amounts shown are limited to existing commitments associated with ongoing schemes, but also account for the assumption that 'annual budgets' will continue, at their 2013/14 level, that an annual unsupported borrowing contingency of £1m is utilised in full in each year, that in 2014/15 and 2015/16 £5m per annum is spent on asset rationalisation, and that the HRA expenditure follows the current 30 year plan.

The key points to note are:

- the overall programmes will be limited to what is affordable, both in terms of actual capital spend and in terms of the revenue implications (see 1.1 above);
- the programmes for future years will be significantly reduced, compared to current levels, due, in part, to the HRA Welsh Housing Quality Standard Programme being completed in 2012.

£m	2011/12 Actual £m	2012/13 Projected £m	2013/14 Estimate £m	2014/15 Estimate £m	2015/16 Estimate £m
TOTAL	21.6	25.6	23.9	27.2	16.2

3. Borrowing

The capital expenditure plans, set to be out in a separate report to the Executive Committee, provide details of the service activity of the Council. The treasury management function ensures that the Council's cash is organised in accordance with the relevant professional codes, so that sufficient cash is available to meet this service activity. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of appropriate borrowing facilities. The strategy covers the relevant treasury/prudential indicators, the current and projected debt positions and the annual investment strategy.

3.1 Current Portfolio Position

The Council's treasury portfolio position at 16 January 2013 comprised:-

		Principal (£m)	Average Rate (%)
Fixed Rate Funding	PWLB	96.1	5.53
Variable Rate Funding	n/a	0.0	n/a
Total Debt		**96.1**	**5.53**

PWLB: Public Works Loans Board

A more detailed breakdown of external debt is shown at Appendix 1.

3.2 Treasury Indicators: Limits to Borrowing Activity

It is a statutory duty under Section 3 of the Act and supporting regulations, for the Council to determine and keep under review how much it can afford to borrow. The amount so determined is termed the "Affordable Borrowing Limit". The Prudential Code refers to this as the Authorised Limit.

The Council must have regard to the Prudential Code when setting the Authorised Limit, which essentially requires it to ensure that total capital investment remains within sustainable limits and, in particular, that the impact upon its future council tax and council rent levels is 'acceptable'.

Whilst termed an "Affordable Borrowing Limit", the capital plans to be considered for inclusion incorporate financing by both external borrowing and other forms of liability, such as credit arrangements. The Authorised Limit is to be set, on a rolling basis, for the forthcoming financial year and two successive financial years.

3.3 Prospects for Interest Rates

The Council's appointed treasury advisor is Sector Treasury Services and part of their service is to assist the Council to formulate a view on interest rates. Appendix 3 draws together a number of current City forecasts for short term (Bank Rate) and longer fixed interest rates. The following table gives the Sector central view.

Annual Average (%)	Bank Rate (%)	PWLB Borrowing Rates (including certainty rate adjustment)		
		5 year	25 year	50 year
Dec 2012	0.50	1.50	3.70	3.90
March 2013	0.50	1.50	3.80	4.00
June 2013	0.50	1.50	3.80	4.00
Sept 2013	0.50	1.60	3.80	4.00
Dec 2013	0.50	1.60	3.80	4.00
March 2014	0.50	1.70	3.90	4.10
June 2014	0.50	1.70	3.90	4.10
Sept 2014	0.50	1.80	4.00	4.20
Dec 2014	0.50	2.00	4.10	4.30
March 2015	0.75	2.20	4.30	4.50
June 2015	1.00	2.30	4.40	4.60
Sept 2015	1.25	2.50	4.60	4.80
Dec 2015	1.50	2.70	4.80	5.00
March 2016	1.75	2.90	5.00	5.20

The economic recovery in the UK since 2008 has been the worst and slowest recovery in recent history, although the economy returned to positive growth in the third quarter of 2012. Growth prospects are weak and consumer spending, the usual driving force of recovery, is likely to remain under pressure due to consumers focusing on repayment of personal debt, inflation eroding disposable income, general malaise about the economy and employment fears.

The primary drivers of the UK economy are likely to remain external. 40% of UK exports go to the Eurozone so the difficulties in this area are likely to continue to hinder UK growth. The US, the main world economy, faces similar debt problems to the UK, but urgently needs to resolve the fiscal cliff now that the Presidential elections are out of the way. The resulting US fiscal tightening and continuing Eurozone problems will depress UK growth and is likely to see the UK deficit reduction plans slip.

This challenging and uncertain economic outlook has several key treasury management implications:-

- The Eurozone sovereign debt difficulties provide a clear indication of high counterparty risk. This continues to suggest the use of higher quality counterparties for shorter time periods;
- Investment returns are likely to remain relatively low during 2013/14 and beyond;
- Borrowing interest rates continue to be attractive and may remain relatively low for some time. The timing of any borrowing will need to be monitored carefully; and
- There will remain a cost of carry - any borrowing undertaken that results in an increase in investments will incur a revenue loss between borrowing costs and investment returns.

A detailed review of the current economic background is contained within Appendix 4 to this report.

3.4 Borrowing Requirement

The forecast movements in the Council's capital financing requirement (CFR) are:-

ESTIMATED MOVEMENTS IN THE CAPITAL FINANCING REQUIREMENT AND REPLACEMENT BORROWING 2012/13 TO 2015/16				
	2012/13 Projected £'000	**2013/14 Estimate £'000**	**2014/15 Estimate £'000**	**2015/16 Estimate £'000**
Movement in the CFR				
New borrowing to support capital expenditure				
Supported Borrowing	*3,758*	*4,820*	*2,140*	*2,140*
Unsupported Borrowing	*5,720*	*6,308*	*6,850*	*6,000*
Total	**9,478**	**11,128**	**8,990**	**8,140**
Reduce by: Minimum Revenue Provision and set aside capital receipts	(4,380)	(4,618)	(5,120)	(5,167)
Net movement in the CFR	**5,098**	**6,510**	**3,870**	**2,973**
Potential movements in actual borrowing				
Movement in the CFR (above)	5,098	6,510	3,870	2,973
Externalisation of pre 2012/13 internal borrowing	4,564	-	**-**	**-**
Replacement Borrowing	6	6,507	7	8
Total potential new borrowing	**9,668**	**13,017**	**3,877**	**2,981**

This incorporates the full impact of the draft Capital Programme for 2013/14. For the following financial years, the amounts of new borrowing are limited to the notified (indicative) allocations for supported borrowing, plus an annual amount of £1m of additional unsupported borrowing, plus cover for delayed capital receipts and the effect of the Local Government Borrowing Initiative. It also assumes the capital receipt from the sale of the current Ysgol y Bont site will be as budgeted and will arise in 2014/15, reducing the requirement for unsupported borrowing in that year.

The likelihood is that not all of this requirement will be met by external borrowing (see 3.4.1 below).

3.5 Borrowing Strategy

The Council is currently in an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This approach is prudent as investment returns are low and counterparty risk is high, and will continue to be followed where appropriate (see 3.5.1 below for a more detailed consideration of internal and external borrowing).

Against this background and the risks within the economic forecast, caution will be adopted with the 2013/14 treasury operations. The S151 Officer will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:-

- if it was felt that there was a significant risk of a sharp FALL in long and short term rates, e.g. due to a marked increase of risks around relapse into recession or of risks of deflation, then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.

- if it was felt that there was a significant risk of a much sharper RISE in long and short term rates than that currently forecast, perhaps arising from a greater than expected increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates were still relatively cheap.

Any decisions will be reported to the appropriate decision making body at the next available opportunity.

In view of the above, the Council's borrowing strategy will be based upon the following sources providing value:-

- Temporary borrowing from the money markets or other local authorities;
- PWLB variable rate loans for up to 10 years;
- Short dated borrowing from non PWLB sources;
- There will be a flexible approach to the mix of internal and external borrowing (see 3.5.1 below);
- Long term fixed rate market loans, where rates are significantly below PWLB rates for the equivalent maturity period, and to maintain an appropriate balance between PWLB and market debt in the debt portfolio;
- PWLB borrowing for periods under ten years where rates are expected to be significantly lower than rates for longer periods. This offers a range of options for new borrowing which will spread debt maturities away from a concentration in longer dated debt.

The S151 Officer will also keep under review potential opportunities to join in bond issues or other collaborative borrowing arrangements.

3.5.1 External v. internal borrowing

The comparison of gross and net debt positions as at year end is as follows (this is on the basis of being fully funded):-

NET BORROWING 2011/12 TO 2015/16					
	2011/12 Actual £'000	**2012/13 Projected £'000**	**2013/14 Estimate £'000**	**2014/15 Estimate £'000**	**2015/16 Estimate £'000**
Total Borrowing	96,103	105,764	112,274	116,347	119,367
Total Investments	16,151	20,967	20,000	20,000	20,000
Net Borrowing	**79,952**	**84,797**	**92,274**	**96,347**	**99,367**

Current conditions indicate a need for a flexible approach to the choice between internal and external borrowing. Many of the factors which lay behind the previous policy to externalise all borrowing remain valid, e.g.:

- To protect the council tax payer from losses caused by the method of calculation of Housing Revenue Account Subsidy in the current system;
- To mitigate any liquidity issues caused by the implementation in the future of the long stop provisions to limit unsupported borrowing;
- With a continuing historically abnormally low Bank Rate, there remains an unique opportunity for local authorities to actively manage their strategy of undertaking new external borrowing.

However, it remains the case that there are certain limitations to this approach, as previously noted, e.g.:-

- The policy can cause exposure to credit risk, so this aspect must be very carefully managed;
- Careful on going consideration needs to be given to the difference between borrowing rates and investment rates to ensure the Council obtains value for money once an appropriate level of risk management has been attained to ensure the security of its investments.

In favour of internalisation, over the next three years investment rates are expected to be below long term borrowing rates. This means that value for money considerations would indicate that value could best be obtained by avoiding new external borrowing and by using internal cash balances to finance new capital expenditure, or to replace maturing external debt (this is referred to as internal borrowing). This would maximise short term savings.

However, short term savings by avoiding new long term external borrowing in 2013/14 must also be weighed against the potential for incurring additional long term extra costs, by delaying unavoidable new external borrowing until later years when PWLB long term rates are forecast to be significantly higher.

Potential changes to Housing Subsidy will have a bearing on the balance of the internalisation/externalisation, but further information on this is awaited from WG.

The Council has examined the potential for undertaking early repayment of some external debt to the PWLB in order to reduce the difference between its gross and net debt positions. However, the introduction by the PWLB of significantly lower repayment rates than new borrowing rates in November 2007, compounded by a considerable further widening of the difference between new borrowing and repayment rates in October 2010, has potentially meant that large premiums would be incurred by such action; such levels of premiums are unlikely to be justifiable on value for money grounds. This situation will be monitored in case these differentials are narrowed by the PWLB at some future date.

Against this background, caution will be adopted with the 2013/14 treasury operations. The S151 Officer will monitor the interest rate market and adopt a pragmatic approach to changing circumstances, reporting any decisions to the appropriate decision making body at the next available opportunity.

3.6 Policy on borrowing in advance of need

The Council will not borrow more than, or in advance of, its needs, solely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates, and will be considered carefully to ensure that value for money can be demonstrated and that the Council can ensure the security of such funds.

In determining whether borrowing will be undertaken in advance of need the Council will:-

- ensure that there is a clear link between the capital programme and maturity profile of the existing debt portfolio which supports the need to take funding in advance of need;
- ensure the ongoing revenue liabilities created, and the implications for the future plans and budgets, have been considered;
- evaluate the economic and market factors that might influence the manner and timing of any decision to borrow;
- consider the advantages and disadvantages of alternative forms of funding;

- consider the alternative interest rate bases available, the most appropriate periods to fund and repayment profiles to use; and
- consider the impact of borrowing in advance on temporarily (until required to finance capital expenditure) increasing investment cash balances and the consequent increase in exposure to counterparty risk, and other risks, and the level of such risks given the controls in place to minimise them.

Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through the mid-year or annual reporting mechanism.

3.7 Debt Rescheduling

The introduction by the PWLB in 2007 of a spread between the rates applied to new borrowing and repayment of debt, which was compounded on 20 October 2010 by a considerable further widening of the difference between new borrowing and repayment rates, has meant that PWLB to PWLB debt restructuring is now much less attractive than it was before these events. In particular, consideration would have to be given to the large premiums which would be incurred by prematurely repaying existing PWLB loans and it is very unlikely that these could be justified on value for money grounds if using replacement PWLB refinancing. However, some interest savings might still be achievable through using LOBO (Lenders Option Borrowers Option) loans, and other market loans, in rescheduling exercises rather than using PWLB borrowing as the source of replacement financing.

As short term borrowing rates will be considerably cheaper than longer term fixed interest rates, there may be potential opportunities to generate savings by switching from long term debt to short term debt. However, these savings will need to be considered in the light of the current treasury position and the size of the cost of debt repayment (i.e. premiums incurred).

The reasons for any rescheduling to take place will include:-

- the generation of cash savings and/or discounted cash flow savings;
- helping to fulfil the treasury strategy;
- enhance the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

Consideration will also be given to identify if there is any residual potential for making savings by running down investment balances to repay debt prematurely as short term rates on investments are likely to be lower than rates paid on current debt.

All rescheduling will be reported to the Audit Committee, at the earliest practicable meeting following its action.

4. Annual Investment Strategy

4.1 Current Portfolio Position

The Council's treasury portfolio position at 16 January 2013 comprised:-

	Principal (£m)	Average Rate (%)
Deposits – Call to 30 days	14.4	0.74
Deposits – Fixed Term < 1 year	10.0	1.63
Deposits – Fixed Term 1 year +	-	-
Total Deposits	**24.4**	**1.11**

4.2 Investment Policy

The Council's investment policy has regard to the WG's Guidance on Local Government Investments ("the Guidance") and the 2011 revised CIPFA Treasury Management in Public Services Code of Practice for Local Authorities and Cross-Sectorial Guidance Notes ("the CIPFA TM Code"). The Council's investment priorities will be security first, liquidity second, and then return.

In accordance with the above, and in order to minimise the risk to investments, the Council has clearly stipulated the minimum acceptable credit quality of counterparties for inclusion on the lending list (see Appendix 5). The creditworthiness methodology used to create the counterparty list fully accounts for the ratings, watches and outlooks published by all three ratings agencies with a full understanding of what these reflect in the eyes of each agency. Using the Sector ratings, service banks' ratings are monitored on a real time basis with knowledge of any changes notified electronically as the agencies notify modifications.

Furthermore, the Council's officers recognise that ratings should not be the sole determinant of the quality of an institution and that it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To this end, the Council will engage with its advisors to maintain a monitor on market pricing such as "Credit Default Swaps" and overlay that information on top of the credit ratings. This is fully integrated into the credit methodology provided by the Council's advisors, Sector, in producing its colour codings which show the varying degrees of creditworthiness.

Other information sources used will include the financial press, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.

The aim of the strategy is to generate a list of highly creditworthy counterparties which will also enable diversification and thus avoidance of concentration risk.

The intention of the strategy is to provide security of investment and minimisation of risk.

Investment instruments identified for use in the financial year are listed in Appendix 5 under the 'Specified' and 'Non-Specified' Investments categories.

The Council will also from time to time, make loans, deposits and investments 'for the purpose of delivery of its Service'. These transactions will require the authority of the County Council for amounts over £100k. All transactions will be subject to adequate credit quality and the approval of the Section 151 Officer in consultation with the Portfolio Holder for Finance.

4.3 Creditworthiness policy

The Chief Finance Officer will maintain a counterparty list in compliance with the criteria set out in Appendix 5 and will revise the criteria and submit them to Council for approval as necessary.

The minimum rating criteria uses the lowest common denominator method of selecting counterparties and applying limits. This means that the application of the Council's minimum criteria will apply to the lowest available rating for any institution. For instance, if an institution is rated by two agencies, one meets the Council's criteria, the other does not, the institution, on the basis of credit rating, will fall outside the lending criteria. Credit rating information is supplied by Sector, our treasury consultants, on all active counterparties that comply with the criteria below. Any counterparty failing to meet the criteria could be omitted from the counterparty list. Any rating changes, rating watches (notification of a likely change), rating outlooks (notification of a possible longer term change) are provided to officers almost immediately after they occur and this information is considered before dealing.

As an additional layer to the minimum credit rating criteria described above, this Council also employs the creditworthiness service provided by Sector. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies - Fitch, Moody's and Standard and Poor's. The credit ratings of counterparties are supplemented with the following overlays:-

- credit watches and credit outlooks from credit rating agencies;
- Credit Default Swaps (CDS) spreads to give early warning of likely changes in credit ratings;
- Sovereign ratings to select counterparties from only the most creditworthy countries.

This modelling approach combines credit ratings, credit watches and credit outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads from which the end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Council to assist in determining the duration for investments. The Council will, therefore, normally use counterparties within the following durational bands:-

- Yellow 5 years
- Purple 2 years
- Blue 1 year (only applies to nationalised or semi nationalised UK Banks)
- Orange 1 year
- Red 6 months
- Green 3 months
- No Colour not to be used without specific approval by S151 Officer

The Sector creditworthiness service uses a wider array of information than just primary ratings and, by using a risk weighted scoring system, does not give undue preponderance to just one agency's ratings.

All credit ratings will be monitored weekly. The Council is alerted to changes to ratings of all three agencies through its use of the Sector creditworthiness service.

- if a downgrade results in the counterparty/investment scheme no longer meeting the Council's minimum credit rating criteria, its further use for new investment will cease immediately, unless otherwise authorised; and
- in addition to the use of credit ratings, the Council will be advised of information in movements in Credit Default Swap spreads against the iTraxx benchmark and other market data on a weekly basis. Extreme market movements may result in downgrade of an institution or removal from the Council's lending list.

Reference will also be made to market data and market information, information on government support for banks and the credit ratings of that supporting government.

4.4 Country limits

The Council has determined that it will only use approved counterparties from countries with a minimum sovereign credit rating of AA- from Fitch Ratings (or equivalent from other agencies if Fitch does not provide). The list of countries that qualify using this credit criteria as at the date of this report are shown in Appendix 6. This list will be added to or deducted from by officers should ratings change in accordance with this policy.

4.5 Investment Strategy

In-house funds*:* Based on cash flow forecasts, the S151 Officer anticipates that the available cash balances in 2013/14 will be up to £30m on average and will range between £15m and £35m. This estimate is based on available cash balances, on a fully funded basis, of £30m on average this year to date (with a range of £16m to £34m). There is a core balance of up to £15m available for investment over a 2-3 year period. Investments will accordingly be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (i.e. rates for investments up to 12 months).

As at the date of this report the Council holds no investments with a maturity of more than one year.

Investment returns expectations: Bank Rate has been unchanged at 0.50% since March 2009. Bank Rate is forecast to commence rising in quarter 4 of 2014. Bank Rate forecasts for financial year ends (March) are: -

- **2012/2013** 0.50%
- **2013/2014** 0.50%
- **2014/2015** 0.75%
- **2015/2016** 1.75%

There are downside risks to these forecasts (i.e. start of increases in Bank Rate is delayed even further) if economic growth remains weaker for longer than expected. However, should the pace of growth pick up more sharply than expected there could be upside risk, particularly if Bank of England inflation forecasts for two years ahead exceed the Bank of England's 2% target rate.

The Council will avoid locking into longer term deals while investment rates are down at historically low levels unless exceptionally attractive rates are available which make longer term deals worthwhile.

The suggested budgeted investment earnings rates for returns on investments placed for periods up to three months during each financial year for the next four years are as follows:-

2012/13	0.50%
2013/14	0.50%
2014/15	0.60%
2015/16	1.50%

For its cash flow generated balances, the Council will seek to utilise its business reserve instant access and reserve accounts, and short-dated deposits (overnight to three months) in order to benefit from the compounding of interest.

4.6 End of year investment report

At the end of the financial year, the Council will report on its investment activity as part of its Annual Treasury Report.

4.7 External fund managers

The Council has not appointed external fund managers. The need for this will be kept under review and a report will be made to the Executive before such an appointment is made.

4.8 Policy on the use of external service providers

In order to acquire access to specialist skills and resources, the Council uses Sector Treasury Services as its external treasury management advisors. The terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review.

Final responsibility for treasury management decisions remains with the Council.

4.9 Delegation

The Treasury Management scheme of delegation and the role of the Section 151 Officer are outlined in Appendix 7.

APPENDICES

1. Loan maturity profile
2. MRP Policy Statement
3. Interest rate forecasts
4. Economic background
5. Specified and non specified investments / Approved Lending List
6. Approved countries for investments
7. Treasury management scheme of delegation and the role of the section 151 officer.
8. Treasury Management Key Principles
9. Treasury Management Policy Statement
10. Prudential and Treasury Indicators **– TO BE CONFIRMED BY THE COUNCIL**

ATODIAD 1/APPENDIX 1

DADANSODDIAD BENTHYCIADAU YN AEDDFEDU 2012/13 YMLAEN/ LOANS MATURITY ANALYSIS 2012/13 ONWARDS						
	PWLB Aeddefedu/ PWLB Maturity £'000	**PWLB EIP/ Annuity/ PWLB EIP/ Annuity £'000**	**Benthyciadau Marchnad/ Market Loans £'000**	**PWLB Amrywiol/ PWLB Variable £'000**	**Cyfanswm yn Aeddfedu/ Total Maturing £'000**	**%YN Aeddfedu o'r Cyfran yn sefyll/ Maturing of Total Outstanding %**
2012/13	0	6	0	0	6	0.0
2013/14	6,500	7	0	0	6,507	6.8
2014/15	0	7	0	0	7	0.0
2015/16	0	8	0	0	8	0.0
2016/17	0	9	0	0	9	0.0
2017/18	5,500	9	0	0	5,509	5.7
2018/19	5,000	10	0	0	5,010	5.2
2019/20	5,000	11	0	0	5,011	5.2
2020/21	4,500	12	0	0	4,512	4.7
2021/22	0	14	0	0	14	0.0
2022/23	2,285	15	0	0	2,300	2.4
2023/24	1,854	16	0	0	1,870	1.9
2024/25	0	18	0	0	18	0.0
2025/26	0	20	0	0	20	0.0
2026/27	854	22	0	0	876	0.9
2027/28	1,675	24	0	0	1,698	1.8
2028/29	0	26	0	0	26	0.0
2029/30	854	21	0	0	875	0.9
2030/31	0	15	0	0	15	0.0
2031/32	1,281	9	0	0	1,290	1.3
2032/33	0	8	0	0	8	0.0
2033/34	0	0	0	0	0	0.0
2034/35	0	0	0	0	0	0.0
2035/36	0	0	0	0	0	0.0
2037/38	0	0	0	0	0	0.0
2039/40	5, 000	0	0	0	5,000	5.2
2040/41	3,500	0	0	0	3,500	3.6
2045/46	0	0	0	0	0	0.0
2047/48	0	0	0	0	0	0.0
2050/51	2,000	0	0	0	2,000	2.1
2052/53	28,238	0	0	0	28,238	29.4
2054/55	3,000	0	0	0	3,000	3.1
2055/56	3,500	0	0	0	3,500	3.6
2056/57	5,000	0	0	0	5,000	5.2
2057/58	8,513	0	0	0	8,513	8.9
2059/60	1,763	0	0	0	1,763	1.8
	95,816	**287**	**0**	**0**	**96,102**	**100.0**
Cyfartaledd bywyd (blynyddoedd)/ Average life(years)	25.64	11.84	0.00	0.00	25.60	
Cyfartaledd graddfa (%)/ Average rate (%)	5.52	9.41	0.00	0.00	5.53	

APPENDIX 2

Minimum Revenue Provision Policy Statement 2013/14

The Council implemented the new Minimum Revenue Provision (MRP) guidance in 2008/09*,* and will assess the MRP for 2013/14 having regard to the main recommendations contained within the guidance issued by Welsh Ministers under section 21(1A) of the Local Government Act 2003. This relates to Council Fund only, not to HRA.

The major proportion of the MRP for 2013/14 will relate to the more historic debt liability that will continue to be charged at the rate of 4% of Capital Financing Requirement (in accordance with *option 2* of the guidance). Certain expenditure, generally that funded from unsupported borrowing, reflected within the debt liability at 31st March 2007 will be subject to MRP (under *option 3),* in accordance with the asset life method as below.

Although the regulations give discretion to charge MRP on new expenditure either at 4% as previously, or according to estimated asset life, MRP will normally be charged at 4%. However, expenditure financed by unsupported borrowing will be charged in accordance with the asset life method. This distinction will be kept under review.

Under the Asset Life method, MRP is charged over a period which is reasonably commensurate with the estimated useful life applicable to the nature of expenditure, using the equal annual instalment method*.* For example, capital expenditure on a new building, or on the refurbishment or enhancement of a building, will be related to the estimated life of that building.

Estimated life periods will be determined by the S151 Officer. To the extent that expenditure is not on the creation of an asset and is of a type that is subject to estimated life periods that are referred to in the guidance, these periods will generally be adopted by the Council. However, the Council reserves the right to determine useful life periods and prudent MRP in exceptional circumstances where the recommendations of the guidance would not be appropriate.

The S151 Officer will determine the appropriate and prudent use of the paragraph 13 exception to defer charging MRP until the year following the one in which the asset became operational.

As some types of capital expenditure incurred by the Council are not capable of being related to an individual asset, asset lives will be assessed on a basis which most reasonably reflects the anticipated period of benefit that arises from the expenditure. Also, whatever type of expenditure is involved, it will be grouped together in a manner which reflects the nature of the main component of expenditure and will only be divided up in cases where there are two or more major components with substantially different useful economic lives.

The Housing Revenue Account share of the Capital Financing Requirement is generally subject to a 2% MRP charge; however, unsupported borrowing will be charged to HRA revenue over a shorter period according to the approved 30 year business plan.

Rhagolygon Graddfeydd Llog 2013-2016/
Interest Rate Forecasts 2013 – 2016

Sector's Interest Rate View														
	Now	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14	Jun-14	Sep-14	Dec-14	Mar-15	Jun-15	Sep-15	Dec-15	Mar-16
Sector's Bank Rate View	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.75%	1.00%	1.25%	1.50%	1.75%
3 Month LIBID	0.39%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.60%	0.60%	0.70%	0.80%	1.10%	1.40%	1.70%
6 Month LIBID	0.54%	0.70%	0.70%	0.70%	0.70%	0.70%	0.70%	0.80%	0.90%	1.00%	1.10%	1.30%	1.60%	1.90%
12 Month LIBID	0.88%	1.00%	1.00%	1.00%	1.00%	1.00%	1.10%	1.10%	1.20%	1.30%	1.30%	1.50%	1.80%	2.10%
5yr PWLB Rate	1.85%	1.50%	1.50%	1.60%	1.60%	1.70%	1.70%	1.80%	2.00%	2.20%	2.30%	2.50%	2.70%	2.90%
10yr PWLB Rate	2.87%	2.50%	2.50%	2.60%	2.60%	2.70%	2.70%	2.80%	3.00%	3.20%	3.30%	3.50%	3.70%	3.90%
25yr PWLB Rate	4.02%	3.80%	3.80%	3.80%	3.80%	3.90%	3.90%	4.00%	4.10%	4.30%	4.40%	4.60%	4.80%	5.00%
50yr PWLB Rate	4.15%	4.00%	4.00%	4.00%	4.00%	4.10%	4.10%	4.20%	4.30%	4.50%	4.60%	4.80%	5.00%	5.20%
Bank Rate														
Sector's View	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.75%	1.00%	1.25%	1.50%	1.75%
UBS	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	-	-	-	-	-
Capital Economics	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	-	-	-	-	-
5yr PWLB Rate														
Sector's View	1.85%	1.50%	1.50%	1.60%	1.60%	1.70%	1.70%	1.80%	2.00%	2.20%	2.30%	2.50%	2.70%	2.90%
UBS	1.85%	-	-	-	-	-	-	-	-	-	-	-	-	-
Capital Economics	1.85%	1.55%	1.30%	1.30%	1.30%	1.30%	1.30%	1.50%	1.60%	-	-	-	-	-
10yr PWLB Rate														
Sector's View	2.87%	2.50%	2.50%	2.60%	2.60%	2.70%	2.70%	2.80%	3.00%	3.20%	3.30%	3.50%	3.70%	3.90%
UBS	2.87%	3.00%	3.10%	3.20%	3.40%	3.50%	3.60%	3.70%	3.80%	-	-	-	-	-
Capital Economics	2.87%	2.55%	2.30%	2.30%	2.30%	2.30%	2.30%	2.30%	2.30%	-	-	-	-	-
25yr PWLB Rate														
Sector's View	4.02%	3.80%	3.80%	3.80%	3.80%	3.90%	3.90%	4.00%	4.10%	4.30%	4.40%	4.60%	4.80%	5.00%
UBS	4.02%	4.20%	4.30%	4.40%	4.50%	4.50%	4.50%	4.50%	4.50%	-	-	-	-	-
Capital Economics	4.02%	3.70%	3.50%	3.50%	3.50%	3.50%	3.50%	3.50%	3.50%	-	-	-	-	-
50yr PWLB Rate														
Sector's View	4.15%	4.00%	4.00%	4.00%	4.00%	4.10%	4.10%	4.20%	4.30%	4.50%	4.60%	4.80%	5.00%	5.20%
UBS	4.15%	4.30%	4.40%	4.50%	4.60%	4.60%	4.60%	4.60%	4.60%	-	-	-	-	-
Capital Economics	4.15%	4.00%	3.80%	3.80%	3.80%	3.80%	3.80%	3.80%	3.80%	-	-	-	-	-

Rhan o gyngor dderbyniwyd gan SECTOR Cyf/
An extract from advice received from SECTOR Ltd

Economic Background
The Global economy

The Eurozone debt crisis has continued to cast a pall over the world economy and has depressed growth in most countries. This has impacted the UK economy which is unlikely to have grown significantly in 2012 and is creating a major headwind for recovery in 2013. Quarter 2 of 2012 was the third quarter of contraction in the economy; this recession is the worst and slowest recovery of any of the five recessions since 1930. A return to growth @ 0.9% in quarter 3 is unlikely to prove anything more than a washing out of the dip in the previous quarter before a probable return to negative growth in quarter 4; this would leave overall growth in 2012 close to zero and could then lead into negative growth in quarter 1 of 2013, which would then mean that the UK was in its first triple dip recession since records began in 1955.

The **Eurozone sovereign debt crisis** abated following the ECB's commitment to a programme of Outright Monetary Transactions i.e. a pledge to buy unlimited amounts of bonds of countries which ask for a bailout. The immediate target for this statement was Spain which continues to prevaricate on making such a request, (for a national bailout), and so surrendering its national sovereignty to IMF supervision. However, the crisis in Greece has subsided, for the time being, as a result of the Eurozone agreement to provide a further €50bn financial support package in December. Many commentators, though, still view a Greek exit from the Euro as being likely in the longer term as successive rounds of austerity packages could make it more difficult to bring down the annual deficit and total debt as ratios of GDP due to the effect they have on shrinking the economy and reducing employment and tax revenues. However, another possible way out would be a major write down of total Greek debt; this has now been raised by the German Chancellor as a possible course of action, but not until 2014-15, and provided the Greek annual budget is in balance.

Sentiment in financial markets has improved considerably since this ECB action and additional financial support for Greece to ensure that the Eurozone remained intact during 2012. However, the foundations to this "solution" to the Eurozone debt crisis are still weak and do not address the huge obstacle of unemployment rates of over 25% in Greece and Spain. It is also possible that the situations in Portugal and Cyprus could deteriorate further in 2013 and, although they are minor economies, such developments could unnerve financial markets. There are also general elections coming up in Italy and Germany which could potentially produce some upsets on the political scene. It is, therefore, quite possible that sentiment in financial markets could turn during 2013 after the initial burst of optimism at the start of the year. While equity prices have enjoyed a strong start to 2013, the foundations for this stock market recovery are shallow given the economic fundamentals in western economies. In addition, QE has to come to an end at some point in time and there is a distinct increase in doubt in the central banks of the US and UK as to the effectiveness of any further QE in stimulating economic growth. An end to central purchases of bonds may lead to a fall in bond prices.

The US economy has only been able to manage weak growth in 2012 despite huge efforts by the Federal Reserve to stimulate the economy by liberal amounts of quantitative easing (QE) combined with a commitment to a continuation of ultra low interest rates into 2015. Unemployment levels have been slowly reducing but against a background of a fall in the numbers of those available for work. The fiscal cliff facing the President at the start of 2013 has been a major dampener discouraging business from spending on investment and increasing employment more significantly in case there is a sharp contraction in the economy in the pipeline. The fiscal cliffs, and raising the total debt ceiling, still await final resolution by the end of February. The housing market, though, does look as if it has, at long last, reached the bottom and house prices are now on the up.

Hopes for a broad based recovery have, therefore, focused on the **emerging markets**. Recent news from China appears to indicate that the economy has returned to a healthier rate of growth. However, there are still concerns around the unbalanced nature of the economy which is heavily dependent on new investment expenditure. The potential for the bubble in the property sector to burst, as it did in Japan in the 1990s, could have a material impact on the economy as a whole.

The UK economy

The Government's austerity measures, aimed at getting the public sector deficit into order, have now had to be extended, in the autumn statement, over a longer period than the original four years. Achieving this new extended timeframe will still be dependent on the UK economy returning to a reasonable pace of growth towards the end of this period.

Currently, the UK is enjoying a major financial benefit from some of the lowest sovereign borrowing costs in the world as the UK is seen as a safe haven from Eurozone debt. However, the subsiding of market concerns over the Eurozone has unwound some of the attractiveness of gilts as a safe haven and led to a significant rise in gilt yields. There is little evidence that UK consumer confidence levels are recovering, nor that the manufacturing sector is picking up. The dominant services sector disappointed in December with the PMI survey indicating the first fall in activity in two years. On the positive side, banks have made huge progress since 2008 in shrinking their balance sheets to more manageable levels and also in reducing their dependency on wholesale funding. However, availability of credit remains tight in the economy and the Funding for Lending scheme, which started in August 2012, has not yet had time to make a significant impact in respect of materially increasing overall borrowing in the economy. Finally, the housing market remains tepid and the outlook is for house prices to be little changed for a prolonged period.

Economic Growth. Economic growth has basically flat lined since the election of 2010 and, worryingly, the economic forecasts for 2012 and beyond were revised substantially lower in the Bank of England Inflation quarterly report for August 2012 and were then further lowered in the November Report. Quantitative Easing (QE) increased by £50bn in July 2012 to a total of £375bn. Many forecasters are expecting the MPC to vote for a further round of QE in early 2013 to try to stimulate economic activity. The announcement in November 2012 that £35bn will be transferred from the Bank of England's Asset Purchase Facility to the Treasury (representing coupon payments to the Bank by the Treasury on gilts held by the Bank) was also effectively a further addition of QE.

Unemployment. The Government's austerity strategy has resulted in a substantial reduction in employment in the public sector. Despite this, total employment has increased to the highest level for four years as over one million jobs have been created in the private sector in the last two years.
Inflation and Bank Rate. Inflation has fallen sharply during 2012 from a peak of 5.2% in September 2011 to 2.2% in September 2012. However, inflation increased back to 2.7% by the end of the year, though it is expected to fall back to reach the 2% target level within the two year horizon.

AAA rating. The UK continues to enjoy an AAA sovereign rating. However, the three main credit rating agencies have stated that they will be reviewing this rating in early 2013; they will, thereafter, also be carefully monitoring the rate of growth in the economy as a disappointing performance in that area could lead to a major derailment of the plans to contain the growth in the total amount of Government debt over the next few years.

Sector's forward view

Economic forecasting remains difficult with so many external influences weighing on the UK. There does, however, appear to be consensus among analysts that the economy remains relatively fragile and whilst there is still a broad range of views as to potential performance, expectations have all been downgraded during 2012. Key areas of uncertainty include:

- the potential for the Eurozone to withdraw support for Greece at some point if the Greek government was unable to eliminate the annual budget deficit and the costs of further support were to be viewed as being prohibitive, so causing a worsening of the Eurozone debt crisis and heightened risk of the breakdown of the bloc or even of the currency itself. The same considerations could also apply to Spain;
- inter government agreement on how to deal with the overall Eurozone debt crisis could fragment;
- the impact of the Eurozone crisis on financial markets and the banking sector;

- the impact of the Government's austerity plan on confidence and growth and the need to rebalance the economy from services to manufactured goods;
- the under-performance of the UK economy which could undermine the Government's policies that have been based upon levels of growth that are unlikely to be achieved;
- the risk of the UK's main trading partners, in particular the EU and US, falling into recession;
- stimulus packages failing to stimulate growth;
- elections due in Italy and Germany in 2013;
- potential for protectionism i.e. an escalation of the currency war/trade dispute between the US and China;
- the potential for action to curtail the Iranian nuclear programme;
- the situation in Syria deteriorating and impacting other countries in the Middle East.

The focus of so many consumers, corporates and banks on reducing their borrowings, rather than spending, will continue to act as a major headwind to a return to robust growth in western economies.

Given the weak outlook for economic growth, Sector sees the prospects for any changes in Bank Rate before 2015 as very limited. There is potential for the start of Bank Rate increases to be even further delayed if growth disappoints.

Sector believes that the longer run trend is for gilt yields and PWLB rates to rise due to the high volume of gilt issuance in the UK, and the high volume of debt issuance in other major western countries. The interest rate forecast in this report represents a balance of downside and upside risks. The downside risks have already been commented on. However, there are specific identifiable upside risks as follows to PWLB rates and gilt yields, and especially to longer term rates and yields:-

- UK inflation being significantly higher than in the wider EU and US causing an increase in the inflation premium in gilt yields;
- Reversal of QE; this could initially be allowing gilts held by the Bank to mature without reinvesting in new purchases, followed later by outright sale of gilts currently held;
- Reversal of Sterling's safe haven status on an improvement in financial stresses in the Eurozone;
- Investors reverse de-risking by moving money from government bonds into shares in anticipation of a return to worldwide economic growth;
- The possibility of a UK credit rating downgrade.

Rhan o gyngor dderbyniwyd gan SECTOR Cyf/
An extract from advice received from SECTOR Ltd

Buddsoddiadau Penodedig ac Amhenodedig/Rhestr Benthyca Cymeradwyedig/ Specified and Non-Specified Investments/Approved Lending List

Rheolau/Criteria

BUDDSODDIADAU PENODEDIG	**SPECIFIED INVESTMENTS**
Adneuon y Trysorlys	Treasury Deposits
Adneuon gydag awdurdodau lleol y DU hyd at 364 diwrnod.	Deposits with UK local authorities for up to 364 days.
Adneuon gyda banciau a chymdeithasau adeiladu sydd wedi derbyn cyfradd credyd uchel, am gyfnodau o hyd at 364 diwrnod (gweler 4.1).	Deposits with banks and building societies which have been awarded a high credit rating, for up to 364 days (see 4.1).
BUDDSODDIADAU AMHENODEDIG *Mwyafswm ar unrhyw bryd £30m*.	**NON-SPECIFIED INVESTMENTS** *Overall limit at any time £30m.*
Grŵp 1 *(wedi eu cymeradwyo)* Adneuon gyda banciau am gyfnodau o hyd at 5 mlynedd (gweler 4.2).	**Group 1** *(approved for use)* Deposits with banks for up to 5 years (see 4.2).
Mwyafswm ar unrhyw bryd £15m.	Overall limit at any time £15m.
Adneuon gyda banciau a chymdeithasau adeiladu nad ydynt wedi derbyn cyfradd credyd uchel, am gyfnodau o hyd at 364 diwrnod (gweler 4.2).	Deposits with banks and building societies which have not been awarded a high credit rating, for up to 364 days (see 4.2).
Mwyafswm ar unrhyw bryd £5m.	Overall limit at any time £5m.
Banciau'r DU sydd wedi eu gwladoli	Nationalised Banks in the UK
Banciau a ddaw dan Becyn Cefnogi System Bancio'r DU	Banks covered by UK Banking System Support Package
Giltiau	Gilts
Biliau'r Trysorlys	Treasury Bills
Cronfeydd Marchnad Arian a raddiwyd AAA	Triple A Rated Money Market Funds
Gwarant Ddiamwys y Llywodraeth ar faterion dyled penodol (e.e. tystysgrifau adneuon, bondiau, a.y.b.) gan fanciau sy'n cael diogelwch dan y pecyn cefnogi system bancio.	UK Government Explicit Guarantee on specific debt issues (e.g. certificates of deposits, bonds, etc.) by banks covered by the banking system support package.
Grŵp 2 *(angen cymeradwyaeth y Pwyllgor Gwaith)*	**Group 2** *(requires Executive approval)*
Dyroddiadau Euro-Sterling gan rai cyrff rhyngwladol a restrir ar Gyfnewidfeydd Stoc gwledydd cymwys yr AEE.	Euro-Sterling issues by certain Supranational bodies listed on the Stock Exchanges of qualifying EAA states.
Mwyafswm ar unrhyw bryd £10m.	Overall limit at any time £10m.
Grŵp 3 *(angen cymeradwyaeth y Cyngor)*	**Group 3** *(requires the Council's approval)*
Pob math arall o fuddsoddiad i bwrpas Rheoli'r Trysorlys.	All other types of investment for Treasury Management purposes.
Dim ond gwrthbartïon a gymeradwywyd o wledydd sydd â chyfradd credyd isaf o AA- trwy Fitch Ratings (neu gyfatebol trwy asiantaethau eraill os nad yw Fitch yn eu darparu) fydd y Cyngor yn eu defnyddio.	The Council will only use approved counterparties from countries with a minimum sovereign credit rating of AA- from Fitch Ratings (or equivalent from other agencies if Fitch does not provide).
Bydd y Cyngor hefyd yn gwneud benthyciadau i bwrpas cyflwyno ei wasanaethau lle mae cyllideb benodol wedi ei gytuno i'r pwrpas e.e. tai fforddiadwy. **Bydd hefyd yn gwneud adneuon a buddsoddiadau yn sefydliadau ariannol i bwrpas darparu ei wasanaethau.**	The Council will also make loans for the purposes of the delivery of its services where there is an approved budget for that specific purpose e.g. affordable housing. **It will also make deposits and investments in financial institutions for the purposes of the delivery of its services.**

CYNGOR SIR YNYS MÔN – ISLE OF ANGLESEY COUNTY COUNCIL
CYRFF Y GELLIR RHOI ARIAN AR FENTHYG IDDYNT YN ÔL Y GYFRADD CREDYD - ADNEUON
Rheolau diwygiedig - Mawrth 2013
APPROVED LENDING LIST BY CREDIT RATING – DEPOSITS
Revised Criteria – March 2013

4.1	**BUDDSODDIADAU PENODEDIG/SPECIFIED INVESTMENTS***	**Rheolau/Criteria**
Si) aiii	Cymdeithasau Adeiladu; Banciau'r DU a thramor- £10m am 12 mis (364 diwrnod) Building Societies; UK & Foreign Banks - £10m for 12 months (364 days)	AA- & A1 + /P1/F1+
Si) aiii	Banciau'r DU sydd wedi eu gwladoli/eu gwladoli'n rhannol - £10m am 12 mis (364 diwrnod) Nationalised/Semi Nationalised UK Banks - £10m for 12 months (364 days)	Pob un /All : CC neu PGC/ HoF(R) or HoS(F)
Si) b	Cymdeithasau Adeiladu; Banciau'r DU a thramor - £7.5m am 6 mis Building Societies; UK & Foreign Banks - £7.5m for 6 months	A & A1 + /P1/F1
Si) c	Cymdeithasau Adeiladu; Banciau'r DU a thramor - £5m am 3 mis Building Societies; UK & Foreign Banks - £5m for 3 months	A & A1 + /P1/F1
Si)d	Banciau'r DU a thramor - £10m am 1 mis UK & Foreign Banks - £10m for 1 month	A & A1 + /P1/F1
Sv)	Trysorlys y DU – dim mwyafswm UK Treasury – no maximum	
Svi)	Awdurdodau Lleol y DU - £5m am 12 mis UK Local Authorities - £5m for 12 months	Pob un /All : CC neu PGC/HoF(R) or HoS(F)
4.2	**BUDDSODDIADAU AMHENODEDIG/NON-SPECIFIED INVESTMENTS***	
Ni) ai	Banciau'r DU a thramor - £10m am 5 mlynedd UK & Foreign Banks - £10m for 5 years	AA & A1 + /P1/F1 + Cefnogaeth/Support ½ CC neu PGC/ HoF(R) or HoS(F)
Ni) ai	Banciau'r DU a thramor - £10m am 3 blynedd UK & Foreign Banks - £10m for 3 years	AA & A1 + /P1/F1 + Cefnogaeth/Support ½ CC neu PGC/ HoF(R) or HoS(F)
N ii)	Is-gwmnïau Prif Fanciau'r DU - £1m am 1 mis Subsidiaries Major UK Banks - £1m for 1 month	Pob un /All : CC neu PGC/ HoF(R) or HoS(F)
N iii)	Banciau Clirio Eraill y DU - £1m am 1 mis Other UK Clearing Banks - £1m for 1 month	Pob un /All : CC neu PGC/ HoF(R) or HoS(F)
N iv) c	Cymdeithasau Adeiladu'r DU - £2m am 2 fis UK Building Societies - £2m for 2 months	Graddfa unigol/ Cefnogaeth dda Good individual/ Support Ratings
N iv) ch	Cymdeithasau Adeiladu'r DU - £1m am 1 mis UK Building Societies - £1m for 1 months	Pob un /All : CC neu PGC/ HoF(R) or HoS(F)
	* Yn amodol ar uchafswm fesul gwrth barti a fesul grŵp. * Subject to limits by counterparty and by group. * Yn amodol hefyd ar raddfa credyd y wlad y mae'r banc yn perthyn iddo. * Subject also to the sovereign credit rating of the country the bank is from.	

Approved countries for investments

Based upon lowest available rating

AAA
- Australia
- Canada
- Denmark
- Finland
- Germany
- Luxembourg
- Netherlands
- Norway
- Singapore
- Sweden
- Switzerland

AA+
- France
- Hong Kong
- U.S.A.
- U.K.

AA
- Abu Dhabi
- Qatar
- UAE

AA-
- Belgium
- Japan
- Saudi Arabia

Treasury management scheme of delegation

(i) County Council

- receiving and reviewing reports on treasury management policies, practices and activities; and
- approval of annual strategy.

(ii) County Council or Executive

- approval of/amendments to the organisation's adopted clauses, treasury management policy statement and treasury management practices;
- budget consideration and approval;
- approval of the division of responsibilities; and
- approving the selection of external service providers and agreeing terms of appointment.

(iii) Audit Committee

- reviewing the treasury management policy and procedures and making recommendations to the responsible body; and
- receiving and reviewing regular monitoring reports and acting on recommendations.

The treasury management role of the section 151 officer

The S151 (responsible) officer's role includes:

- recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance;
- submitting regular treasury management policy reports;
- submitting budgets and budget variations;
- receiving and reviewing management information reports;
- reviewing the performance of the treasury management function;
- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function;
- ensuring the adequacy of internal audit, and liaising with external audit; and
- recommending the appointment of external service providers.

Capital Issues

- the capital plans and the prudential indicators; and
- the MRP strategy.

The CIPFA Treasury Management in the Public Services: Code of Practice

This Authority adopts the key principles of CIPFA's ***Treasury Management in the Public Services: Code of Practice (2011 Edition)***, as described in Section 4 of that Code as follows:-

Key Principle 1:
Public service organisations should put in place formal and comprehensive objectives, policies and practices, strategies and reporting arrangements for the effective management and control of their treasury management activities.

Key Principle 2:
Their policies and practices should make clear that the effective management and control of risks are prime objectives of their treasury management activities and that responsibility for these lies clearly within their organisations. Their appetite for risk should form part of their annual strategy, including any use of financial instruments for the prudent management of those risks, and should ensure that priority is given to security and liquidity when investing funds.

Key Principle 3:
They should acknowledge that the pursuit of value for money in treasury management and the use of suitable performance measures are valid and important tools for responsible organisations to employ in support of their business and service objectives; and that, within the context of effective risk management, their treasury management policies and practices should reflect this.

The Code then goes on to say that:

"In framing these recommendations, CIPFA acknowledges the difficulties of striving for effective risk management and control, whilst at the same time pursuing value for money. This code does not seek to be prescriptive about how this issue should be handled, particularly since it covers such a wide variety of organisations. However, where appropriate, the sector specific guidance notes give suitable advice. CIPFA recognises that no two organisations in the public services are likely to tackle this issue in precisely the same manner but success in this area of treasury management is likely to be viewed, especially in value for money terms, as an indicator of a strongly performing treasury management function."

"Even though it dates back to 1991, CIPFA considers that the report by the Treasury and Civil Service Committee of the House of Commons on the BCCI closure is still pertinent, wherein it was stated that:"

"In balancing risk against return, local authorities should be more concerned to avoid risks than to maximise returns."

"Indeed this view was supported by the Communities and Local Government Select Committee report into local authority investments in 2009."

"It is CIPFA's view that throughout the public services the priority is to protect capital rather than to maximise return. The avoidance of all risk is neither appropriate nor possible. However, a balance must be struck with a keen responsibility for public money."

Accordingly the Authority will adopt, as part of the standing orders, the following four clauses;

1. The Authority will create and maintain, as the cornerstones for effective treasury management:

- a treasury management policy statement, stating the policies, objectives and approach to risk management of its treasury management activities; and

- Suitable treasury management practices (TMPs) setting out the manner in which the Authority will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities.

The content of the Policy Statement and TMPs will follow the recommendations contained in Sections 6 and 7 of the Code, subject only to amendment where necessary to reflect the particular circumstances of the Authority. Such amendments will not result in the Authority materially deviating from the Code's key principles.

2. The Authority will also have regard for the Guidance on Local Government Investments issued by the Welsh Assembly Government and effective from 1st April 2010.

3. Full Council will receive reports on its treasury management policies, practices and activities, specifically; an annual strategy and plan in advance of the year, a mid year review and an annual report after its close, in the form prescribed in the TMPs. In addition to this the Audit Committee will receive quarterly review reports for first and third quarters.

4. The Authority delegates responsibility for the implementation and regular monitoring of its treasury management policies and practices to the Audit Committee, and for the execution and administration of treasury management decisions to the Chief Financial Officer, who will act in accordance with the Authority's policy statement and TMPs and, if he/she is a CIPFA member, CIPFA's Standard of Professional Practice on Treasury Management.

5. The Authority nominates Audit Committee to be responsible for ensuring effective scrutiny of treasury management policies, practices and performance.

APPENDIX 9

Treasury Management Policy Statement

1. The Authority defines its treasury management activities as: “The management of the authority’s investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks’’.

2. This organisation regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation, and any financial instruments entered into to manage these risks.

3. This organisation acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.”

APPENDIX 10

Prudential and Treasury Indicators

TO BE CONFIRMED BY THE COUNCIL