Appendix A

CHESHIRE EAST TREASURY MANAGEMENT STRATEGY 2009/10

1. INTRODUCTION

1.1 The Local Government Act 2003 requires the Council to have regard to the Prudential Code and to set Prudential Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable.

1.2 The Act therefore requires the Council to set out its Treasury Strategy for borrowing and to prepare an Annual Investment Strategy; this sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments.

2. BACKGROUND

2.1 The Chartered Institute of Public Finance and Accountancy's Code of Practice for Treasury Management in Public Services (the "CIPFA TM Code") requires local authorities to set the Treasury Management Strategy Statement (TMSS) for borrowing each financial year.

2.2 CIPFA has defined Treasury Management as:

"the management of the organisation's 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."

2.3 It is a statutory requirement, under Section 33 of the Local Government Finance Act 1992, for the Council to produce a balanced budget. In particular, Section 32 requires a local authority to calculate its budget requirement for each financial year to include the revenue costs that flow from capital financing decisions. This means that increases in capital expenditure must be limited to a level whereby increases in charges to revenue from:

- increases in interest charges caused by increased borrowing to finance additional capital expenditure, and
- any increases in running costs from new capital projects are affordable within the projected income of the Council for the foreseeable future.

2.4 Members' involvement in the process is essential in order that the Council can demonstrate that its capital expenditure plans are affordable, external borrowing is prudent and sustainable and treasury decisions are taken in accordance with good practice.

2.5 The Council 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. Treasury management risks are identified in the Council's approved Treasury Management Practices; the main risks to the Council's treasury activities are:

- Liquidity Risk (Inadequate cash resources)

- Market or Interest Rate Risk (Fluctuations in interest rate levels and thereby in the value of investments).

- Inflation Risks (Exposure to inflation)

- Credit and Counterparty Risk (Security of Investments)

- Refinancing Risks (Impact of debt maturing in future years).

- Legal & Regulatory Risk (i.e. non-compliance with statutory and regulatory requirements, risk of fraud).

3. LOCAL GOVERNMENT REVIEW

3.1 As Members and Officers are aware the merger of the three District Councils within East Cheshire and the disaggregated share of Cheshire County Council's investment and borrowing portfolio's will come under the ownership of the New Unitary Authority, Cheshire East.

3.2 As such some of the key areas of the new treasury management function have yet to be decided for the 2009/10 financial year and work is still continuing in the shape of the joint Treasury Management Group to work out a cutover strategy from 1st April 2009. Two key areas where decisions are still to be made are as follows:

- The final disaggregation of Cheshire County Council's balance sheet commitments for loans and investments as at 31st March 2009.

- Whether the new Authority will use the specialist services of an external cash manager.

3.3 New Treasury advisors are to be appointed for Cheshire East, a panel of Treasury Officers interviewed prospective advisors and Arlingclose were chosen as the preferred candidate for Cheshire East and the contract is due to commence shortly.

4. CURRENT POSITION

The Council's treasury portfolio position as at 9th January 2009 comprises of the three existing District portfolio positions and the County Council's share that has been disaggregated to the East.

Investments	Principal £m
Macclesfield Borough Council	39.5m
Congleton Borough Council	16.0m
Crewe & Nantwich Borough Council	35.9m
Cheshire County Council (disaggregated East)	51.3m
Total Investments	**142.7m**
Debt	**Principal £m**
Cheshire County Council (disaggregated East	135.6m
Total Debt	**135.6m**

5. RISK MANAGEMENT

5.1 The identification, understanding and management of risk are, by necessity, a major part of an organisation's treasury management activities. It is therefore no surprise to learn that risk management is, and has been for a number of years, well embedded in the area of treasury management.

5.2 The consequences of making a wrong treasury management decision can be significant and long lasting. eg were the Council to invest monies with a lender who ultimately cannot repay the amount lent to them (ie defaults on repayment) then the whole of the amount not repaid will fall as a charge on the I&E account in the year in which the default occurs.

5.3 To avoid the Council suffering loss as a result of its treasury management activities a number of risk management procedures have been put in place. These are listed below. These procedures are based on the concept that firstly security of principal is paramount, secondly that there is a need to maintain liquidity and finally earning a rate of return commensurate with the first two concepts.

Liquidity risk

5.4 The risk that cash will not be available when it is needed to meet the Council's obligations.

5.5 The Council prepares an annual cash flow forecast each year that identifies, by month, the anticipated cash inflows and outflows over the year. The purpose of preparing such a forecast is to identify the timing, duration and magnitude of any cash surpluses and shortfalls.

5.6 A daily cash flow spreadsheet is also maintained that lists all the monthly major cash inflows and outflows. This spreadsheet is a key input when deciding how long any surplus cash balances should be invested for. The first priority when investing surplus cash balances is to cover known cash outflows i.e. to retain liquidity.

Credit (or counter-party) risk

5.7 The risk that an amount deposited by the authority will not be repaid in full on the day it is due.

5.8 When selecting counter-parties (ie banks and building societies) with which the Council will deposit monies the avoidance of loss of principal is regarded as paramount. This is achieved by having in place formal policies and procedures that ensure that the risk of a potential loss of principal through the default of a counter-party is reduced to a suitably agreed and acceptable level.

5.9 These policies and procedures include setting minimum requirements on the independently assessed financial standing of the counterparties with which monies are deposited. In addition an upper limit is placed on the amount that can be deposited with an individual counterparty or with a group of related counterparties.

Refinancing risk

5.10 The risk that the Council will be unable to renew its maturing funding arrangements / reinvest deposits on reasonable terms.

5.11 This risk is managed to an acceptable level by ensuring that the maturity profile of the Council's long term loans portfolio remains fairly smooth. The Council also tries to avoid having too large an amount of loans maturing on a particular day or in a particular financial year.

Legal and regulatory risk

5.12 The risk that one of the parties to an agreement will be unable to honour its legal obligations to the other party.

5.13 When investing its cash balances the Council ensures that it adheres to the guidance on the investment of surplus cash balances by local authorities that was issued by the Secretary of State at the Office of the Deputy Prime Minister (ODPM) in March 2004.

Prevention of fraud, error and collusion

5.14 A set of comprehensive procedures exist that detail the procedures and processes that need to be undertaken before, during and after entering into a money market deal.

5.15 The purpose of these procedures and processes is to ensure that a clear segregation of duties is in place. This segregation of duties ensures that at least two members of staff have checked and agreed the details of the money market transaction before any monies are paid over.

6. OUTLOOK FOR INTEREST RATES

The economic interest rate outlook provided by the Council's treasury advisor, Arlingclose Ltd, is summarised below. See Annex B for further details.

(a) Background

Central bankers acted decisively in October 2008 as the effective breakdown of financial systems threatened to destabilise the global economy. It included government sponsored recapitalisations, interventions through the provision of liquidity and guarantees for lending; in some instances nationalisation of private sector financial institutions; the removal of compromised assets from banks' balance sheets through special finance mechanisms; and co-ordinated emergency interest rates cuts. The UK, Eurozone and US economies contracted in the third and fourth quarters of 2008.

(b) Outlook

- **Availability of credit** is likely expected to remain restricted and credit conditions challenging, particularly as banks change their lending behaviour and lower their lending risk. The poorly functioning transmission mechanism for lower rates to be passed to consumers could cause governments to intervene directly between banks and corporates/individuals.

- **Inflation:** The elevated levels of commodity, food and energy inflation which exerted a powerful squeeze on real incomes in 2008 are expected to fade in 2009. CPI, which had risen to 5.2% in 2008, is now expected to fall below the MPC's lower boundary of 1%. Whilst this will provide consumers some relief, lower inflation erodes debt burdens more slowly.

- **Labour market:** Unemployment, already at 6%, is expected to rise further. The fear of unemployment will keep wage bargaining and wage inflation to a minimum.

- **Housing / Consumer Confidence:** The prospect of negative housing equity, and/or rising unemployment and depressed asset values could culminate in a further negative loop-back for confidence. Consumers and businesses will scale back spending to conserve or repair their balance sheets.

- **Growth:** The effort to reduce erstwhile ballooning debt will hit economic activity and growth in the UK, US and in Europe. The prospects for growth remains uniformly poor in for much of 2009. Asset values are forecast to drop further, particularly those which are commodities and housing-related.

- **Interest Rates:** To avoid deflation and to mitigate the severity of the economic slowdown, there will be a growing willingness by Central Bankers to countenance abnormally low interest rates and/or some form of quantitative easing (i.e. using more unconventional methods such as expanding the central bank's balance sheet and injecting cash into the economy), sooner rather than later.

- **Market conditions and volatility:** Market volatility remains high, risk appetite at a low ebb; markets are expected to continue in 'capital preservation mode' into early 2009. Although Libor is falling, the gap between official and market interest rates is likely to remain relatively wide for some months to come.

The deterioration in public finances – both via the cost of shoring up the financial system and also as recession hits the government's revenue streams – and the burgeoning budget deficit will require significant new gilt issuance in 2009. This excess supply is expected to push longer dated yields higher although not aggressively so. Short-dated gilt yields are however expected to fall with the gathering momentum of a fall in official policy rates.

The price destruction in equities will keep stock markets subdued and, even though there may be tentative signs of stability, it would be too early to say if a bottom has been reached.

The Arlingclose forecast for the UK Bank Rate (December 2008) is:

	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10	Mar-11
Official Bank Rate									
Upside risk							+0.25	+0.25	+0.25
Central case	**1.00**	**1.00**	**1.00**	**1.00**	**1.00**	**1.50**	**2.00**	**2.50**	**2.50**
Downside risk	-0.50	-0.75	-0.75	-0.75	-0.75	-0.50	-0.50	-0.50	-0.50

The probability or zero or near zero interest rates – unthinkable just a few months ago – is now very high. The economic outlook provides both opportunities and challenges for the Council's treasury strategy in 2009-10.

7. BORROWING REQUIREMENT & STRATEGY

7.1 The Council's underlying need to borrow for capital purposes is measured by reference to its Capital Financing Requirement (CFR) – see Annex A. The change, year on year will be influenced by the capital expenditure in the year and the means available to finance it. The CFR will determine the Council's requirement to make a Minimum Revenue Provision for Debt Redemption (MRP) from within its Revenue budget. Physical borrowing may be greater or less than the CFR.

7.2 In accordance with the Prudential Code, the Council will ensure that net external borrowing does not, except in the short term, exceed the CFR in the preceding year plus the estimates of any additional CFR for the current and next two financial years.

7.3 Capital expenditure not financed from internal resources (i.e. Capital Receipts, Capital Grants and Contributions, Revenue or Reserves) will produce an increase in the CFR (the underlying need to borrow) and may in turn produce an increased requirement to charge MRP in the Revenue Account.

7.4 The Council prefers to maintain maximum control over its borrowing activities as well as flexibility on its loans portfolio. Capital expenditure levels, market conditions and interest rate levels will be monitored during the year in order to minimise borrowing costs over the medium to longer term. A prudent and pragmatic approach to borrowing will be maintained to minimise borrowing costs without compromising the longer-term stability of the portfolio, consistent with the Council's Prudential Indicators.

7.5 In conjunction with advice from its treasury advisor, Arlingclose Ltd, the Council will keep under review the options it has in borrowing from the PWLB, the market and other sources identified in the Treasury Management Practices Schedules up to the available capacity within its CFR and Affordable Borrowing Limit (defined by CIPFA as the Authorised Limit).

7.6 Short-dated gilt yields are forecast to be considerably lower than medium- and long-dated gilt yields during the financial year. Despite additional gilt issuance to fund the UK government's support to the banking industry, short-dated gilts are expected to benefit from expectations of lower interest rates as the economy struggles through a recession. Yields for these maturities will fall as expectations for lower interest rates mount.

The Outlook for Borrowing Rates:

7.7 Variable Rate borrowing : The shocks in the financial markets in the second half of 2008 leaves the UK in a different era in respect of official interest rates which are forecast to fall below 1.5%. By December 2008 the rates for PWLB variable-rate borrowing had fallen substantially and are forecast to fall to altogether very low levels as the Bank Rate is cut further.

7.8 Fixed rate borrowing: Gilts across all maturities will initially benefit from their status of safe haven assets in uncertain economic times. As yields fall initially, fixed PWLB rates across most maturities could challenge historic lows. As the UK Bank Rate falls to 1% or lower, short-dated yields and PWLB rates should provide some attractive fixed rate borrowing opportunities.

7.9 The Council will evaluate the relative merits of a strategic exposure to variable rate debt. Decisions to borrow at low, variable rates of interest will be taken after considering the absolute level of longer term interest rate equivalents and the extent of variable rate earnings on the Council's investment balances. Should longer term rates move below the cost of variable rate borrowing any strategic exposure to variable interest rates will be reviewed and, if appropriate, reduced.

7.10 Actual borrowing undertaken and the timing will depend on capital expenditure levels, interest rate forecasts and market conditions during the year, in order to minimise borrowing costs. The Council will consult their advisors Arlingclose on the specific timing of borrowing. This may include borrowing in advance of future years' requirements provided that overall borrowing is maintained within the Council's projected CFR and its approved Affordable Borrowing Limit.

7.11 The Council will undertake a financial options appraisal process to establish how it has arrived at its 'value for money' judgement in the use of resources.

8. Debt Rescheduling

8.1 The Council will continue to maintain a flexible policy for debt rescheduling. Market volatility may provide opportunities for rescheduling debt from time to time. The rationale for rescheduling would be one or more of the following:

- Savings in interest costs with minimal risk.
- Balancing the volatility profile (i.e. the ratio of fixed to variable rate debt) of the debt portfolio.
- Amending the profile of maturing debt to reduce any inherent refinancing risks.

8.2 The rescheduling of PWLB debt since the introduction of its repayment rates on 1st November 2007 has not ceased, but has become undoubtedly harder and places greater emphasis on the timing and type of new borrowing. PWLB rates exhibited a fair degree of volatility in 2008-09; should a similar pattern emerge in 2009-10, this could provide the Council with some rescheduling opportunities.

8.3 Any rescheduling activity will be undertaken within the Council's treasury management policy and strategy. Thereafter the Council's debt portfolio will be monitored against equivalent interest rates and available refinancing options on a regular basis.

8.4 All rescheduling activity will comply with the accounting requirements of the local authority SORP and regulatory requirements of the Capital Finance and Accounting Regulations (SI 2007 No 573 as amended by SI 2008/414).

9. Investment Policy and Strategy

Background

9.1 Guidance from the then ODPM (now DCLG) on Local Government Investments in England requires, similarly, that an Annual Investment Strategy (AIS) be set. The Guidance permits the TMSS and the AIS to be combined into one document.

Investment Policy

9.2 The Council's general policy objective is to invest its surplus funds prudently. The Council's investment priorities are:

- security of the invested capital;
- liquidity of the invested capital;
- an optimum yield which is commensurate with security and liquidity.

9.3 Investments are categorised as 'Specified' or 'Non Specified' investments based on the criteria in the ODPM Guidance. Potential instruments for the Council's use within its investment strategy are contained in Annex C.

9.4 The credit crisis has refocused attention on the treasury management priority of security of capital monies invested. The Council will continue to maintain a counterparty list based on its criteria and will monitor and update the credit standing of the institutions on a regular basis. This assessment will include credit ratings and other alternative assessments of credit strength (for example, statements of potential government support). The Council will also take into account information on corporate developments of and market sentiment towards investment counterparties.

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Investment Strategy

9.5 The global financial market storm in 2008 has forced investors of public money to reappraise the question of risk versus yield. Income from investments is a key support in the Council's budget.

9.6 By January 2009 the UK Bank Rate had fallen to 1.5%, its lowest level since the 1950s. It is expected that the Bank Rate will fall to near zero in 2009/10, short-term money market rates will continue to fall to very low levels which will have a significant impact on investment income. The Council's strategy must however be geared towards this development whilst adhering to the principal objective of security of invested monies. All investments will be in sterling.

9.7 The Borough Treasurer, under delegated powers, will undertake the most appropriate form of investments in keeping with the investment objectives, income and risk management requirements and

Investments Managed In-house :

9.8 The Council's shorter term cashflow investments are made with reference to the outlook for the UK Bank Rate and money market rates. For these monies, the Council will mainly invest in

- The Debt Management Agency Deposit Facility (The rates of interest from the DMADF are below equivalent money market rates. However, the returns are an acceptable trade-off for the guarantee that the Council's capital is secure.)
- AAA-rated Money Market Funds with a Constant Net Asset Value (Constant NAV) investing predominantly in government securities
- AAA-rated Money Market Funds with a Constant Net Asset Value (Constant NAV) investing in instruments issued primarily by financial institutions;
- Deposits with other local authorities
- Business reserve accounts
- Term deposits
- Certificates of deposit.

Investments managed externally

9.9 The Council's funds are also managed on a discretionary basis by Investec, The fund's remit allows the managers scope to add value through the use of investments contained in Annex C and within the parameters and guidelines set for the Council's fund. Performance is monitored and measured against the benchmark set for the fund, prevailing economic conditions and investment opportunities. A further decision on whether this arrangement will continue in 2009/10 is still to be made.

10 REPORTING

10.1 The Borough Treasurer will report to the Cheshire East Cabinet on treasury management activity / performance as follows:

(a) annually against the strategy approved for the year.

(b) The Council will produce an outturn report on its treasury activity no later than 30th September after the financial year end.

Reporting on the Treasury Activity during 2009/10 will be in accordance with the following timetable:

	Date	**Meeting**	**Responsibility**
Strategy Report	February 2009	Cabinet/Council	Borough Treasurer
Quarterly Reports	Month after Quarter End	Cabinet	Borough Treasurer
Annual Treasury Report	August 2010	Cabinet	Borough Treasurer

Annex A

Prudential Indicators FY 2009-10 to FY 2011-12

1 Background

There is a requirement under the Local Government Act 2003 for local authorities to have regard to CIPFA's Prudential Code for Capital Finance in Local Authorities (the "CIPFA Prudential Code") when setting and reviewing their Prudential Indicators. It should be noted that CIPFA undertook a review of the Code in early 2008. The outcome from that review has yet to be published.

2. Estimates of Capital Expenditure

2.1 This indicator is set to ensure that the level of proposed capital expenditure remains within sustainable limits and, in particular, to consider the impact on Council Tax levels.

No. 1	**Capital Expenditure**	2008-09	2008-09	2009-10	2010-11	2011-12
		Approved £m	Revised £m	Estimate £m	Estimate £m	Estimate £m
	Total	**90**	**87**	**97**	**67**	**53**

2.2 Capital expenditure will be financed as follows:

Capital Financing	2008-09	2008-09	2009-10	2010-11	2011-12
	Approved £m	Revised £m	Estimate £m	Estimate £m	Estimate £m
Capital receipts	19	18	13	5	4
Capital Reserve	5	4	2	3	3
Government Grants	30	29	44	42	31
External Contributions	5	4	6	0	0
Revenue contributions	3	3	3	1	1
Supported borrowing	19	17	13	13	13
Unsupported borrowing	9	12	16	3	1
Total	**90**	**87**	**97**	**67**	**53**

3. Ratio of Financing Costs to Net Revenue Stream

3.1 This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet borrowing costs. The definition of financing costs is set out at paragraph 87 of the Prudential Code.

3.2 The ratio is based on costs net of investment income.

No. 2	Ratio of Financing Costs to Net Revenue Stream	2009-10	2010-11	2011-12
		Estimate	Estimate	Estimate
		%	%	%
	Total	**5.26**	**6.28**	**5.95**

4. Capital Financing Requirement

4.1 The Capital Financing Requirement (CFR) measures the Council's underlying need to borrow for a capital purpose. The calculation of the CFR is taken from the amounts held in the Balance Sheet relating to capital expenditure and it's financing. It is an aggregation of the amounts shown for Fixed and Intangible assets, the Revaluation Reserve, the Capital Adjustment Account, Government Grants Deferred and any other balances treated as capital expenditure.

No. 3	Capital Financing Requirement	31/3/09	31/3/09	31/3/10	31/3/11	31/3/12
		Approved	Revised	Estimate	Estimate	Estimate
		£m	£m	£m	£m	£m
	Total CFR	**153**	**153**	**175**	**181**	**186**

4.2 In order to ensure that over the medium term net borrowing will only be for a capital purpose, the Council should make sure that net external borrowing does not, except in the short term, exceed the Capital Financing Requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years.

4.3 The Borough Treasurer reports that this Council does not envisage difficulties in meeting this requirement if future financial years.

5 Actual External Debt

5.1 This indicator is obtained directly from the Council's balance sheet. It is the closing balance for actual gross borrowing plus other long-term liabilities. This Indicator is measured in a manner consistent for comparison with the Operational Boundary and Authorised Limit.

No. 4	Actual External Debt as at 31/3/2008	£m
	Borrowing	136
	Other Long-term Liabilities	0
	Total	**136**

6. Incremental Impact of Capital Investment Decisions

6.1 This is an indicator of affordability that shows the impact of capital investment decisions on Council Tax and Housing Rent levels. The incremental impact is calculated by comparing the total revenue budget requirement of the current approved capital programme with an equivalent calculation of the revenue budget requirement arising from the proposed capital programme.

No. 5	**Incremental Impact of Capital Investment Decisions**	2009-10	2010-11	2011-12
		Estimate £	Estimate £	Estimate £
	Increase in Band D Council Tax	3.10	9.76	8.39

The increase in Band D council tax in 2009/10 reflects the increases in the provision for Capital Financing Charges of £0.45m to undertake borrowing of £31m arising from the proposed capital programme.

7 Authorised Limit and Operational Boundary for External Debt

7.1 The Council has an integrated treasury management strategy and manages its treasury position in accordance with its approved strategy and practice. Overall borrowing will therefore arise as a consequence of all the financial transactions of the Council and not just those arising from capital spending reflected in the CFR.

7.2 The **Authorised Limit** sets the maximum level of external borrowing on a gross basis (i.e. not net of investments) for the Council. It is measured on a daily basis against all external borrowing items on the Balance Sheet (i.e. long and short term borrowing, overdrawn bank balances and long term liabilities. This Prudential Indicator separately identifies borrowing from other long term liabilities such as finance leases. It is consistent with the Council's existing commitments, its proposals for capital expenditure and financing and its approved treasury management policy statement and practices.

7.3 The Authorised Limit has been set on the estimate of the most likely, prudent but not worst case scenario with sufficient headroom over and above this to allow for unusual cash movements.

7.4 The Authorised Limit is the statutory limit determined under Section 3(1) of the Local Government Act 2003 (referred to in the legislation as the Affordable Limit).

No. 6	Authorised Limit for External Debt	2008-09	2008-09	2009-10	2010-11	2011-12
		Approved £m	Revised £m	Estimate £m	Estimate £m	Estimate £m
	Borrowing	149	149	218	222	226
	Other Long-term Liabilities	0	0	0	0	0
	Total	**149**	**149**	**218**	**222**	**226**

7.5 The **Operational Boundary** links directly to the Council's estimates of the CFR and estimates of other cash flow requirements. This indicator is based on the same estimates as the Authorised Limit reflecting the most likely, prudent but not worst case scenario but without the additional headroom included within the Authorised Limit.

7.6 The Borough Treasurer has delegated authority, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long-term liabilities. Decisions will be based on the outcome of financial option appraisals and best value considerations.

No. 7	Operational Boundary for External Debt	2008-09	2008-09	2009-10	2010-11	2011-12
		Approved £m	Revised £m	Estimate £m	Estimate £m	Estimate £m
	Borrowing	**149**	**149**	**210**	**216**	**220**
	Other Long-term Liabilities	0	0	**0**	0	0
	Total	**149**	**149**	**210**	**216**	**220**

8. Adoption of the CIPFA Treasury Management Code

8.1 This indicator demonstrates that the Council has adopted the principles of best practice.

No. 8	Adoption of the CIPFA Code of Practice in Treasury Management
	The Council will consider the adoption of the CIPFA Treasury Management Code at its Shadow Council meeting on 24 February 2009

9. Upper Limits for Fixed Interest Rate Exposure and Variable Interest Rate Exposure

9.1 These indicators allow the Council to manage the extent to which it is exposed to changes in interest rates. This Council calculates these limits on net principal outstanding sums, (i.e. fixed rate debt net of fixed rate investments).

9.2 The upper limit for variable rate exposure has been set to ensure that the Council is not exposed to interest rate rises which could adversely impact on the revenue budget. The limit allows for the use of variable rate debt to offset exposure to changes in short-term rates on investments

		2008-09 Approved	2008-09 Revised	2009-10 Revised	2010-11 Revised	2011-12 Revised
		%	%	%	%	%
No. 9	**Upper Limit for Fixed Interest Rate Exposure**	100	100	100	100	100
No. 10	**Upper Limit for Variable Rate Exposure**	100	100	100	100	100

9.3 The limits above are set at 100% for fixed and 100% for variable to allow the Council the necessary flexibility within which decisions will be made for drawing down new loans on a fixed or variable rate basis; the decisions will ultimately be determined by expectations of anticipated interest rate movements as set out in the Council's treasury management strategy.

10 Maturity Structure of Fixed Rate Borrowing

10.1 This indicator highlights the existence of any large concentrations of fixed rate debt needing to be replaced at times of uncertainty over interest rates and is designed to protect against excessive exposures to interest rate changes in any one period, in particular in the course of the next ten years.

10.2 It is calculated as the amount of projected borrowing that is fixed rate maturing in each period as a percentage of total projected borrowing that is fixed rate. The maturity of borrowing is determined by reference to the earliest date on which the lender can require payment.

No. 11	**Maturity structure of fixed rate borrowing**	**Lower Limit %**	**Upper Limit %**
	under 12 months	Nil	25%
	12 months and within 24 months	Nil	25%
	24 months and within 5 years	Nil	35%
	5 years and within 10 years	Nil	35%
	10 years and above	Nil	100%

11. Upper Limit for total principal sums invested over 364 days

11.1 The purpose of this limit is to contain exposure to the possibility of loss that may arise as a result of the Council having to seek early repayment of the sums invested.

No. 12	**Upper Limit for total principal sums invested over 364 days shown as a % of the portfolio**	Maturing beyond 1 year	Maturing beyond 2 years	Maturing beyond 3 years
		40%	40%	40%

Annex B

Arlingclose's Forecast for Interest Rates (December 2008)

	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10	Mar-11
Official Bank Rate									
Upside risk							+0.25	+0.25	+0.25
Central case	**1.00**	**1.00**	**1.00**	**1.00**	**1.00**	**1.50**	**2.00**	**2.50**	**2.50**
Downside risk	-0.50	-0.75	-0.75	-0.75	-0.75	-0.50	-0.50	-0.50	-0.50
1-yr LIBID									
Upside risk									
Central case	**2.50**	**1.75**	**1.50**	**1.50**	**1.50**	**1.75**	**2.00**	**2.75**	**3.00**
Downside risk	-0.25	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50
5-yr gilt									
Upside risk									
Central case	**3.00**	**2.75**	**2.50**	**2.00**	**2.00**	**2.50**	**2.75**	**3.00**	**4.00**
Downside risk		-0.50	-0.50	-0.50	-0.50	-0.50			
10-yr gilt									
Upside risk									
Central case	**3.40**	**3.10**	**3.00**	**3.00**	**3.00**	**3.50**	**3.75**	**4.00**	**4.50**
Downside risk	-0.25	-0.25	-0.50	-0.50	-0.50	-0.50			
20-yr gilt									
Upside risk		+0.10	+0.10	+0.10	+0.10	+0.10			
Central case	**4.00**	**4.00**	**4.00**	**4.25**	**4.25**	**4.50**	**4.75**	**4.75**	**4.75**
Downside risk		-0.10	-0.10	-0.10	-0.10	-0.10			
50-yr gilt									
Upside risk	+0.10	+0.10	+0.10	+0.10	+0.10	+0.10	+0.10	+0.10	+0.10
Central case	**3.90**	**3.90**	**4.00**	**4.00**	**4.25**	**4.50**	**4.50**	**4.50**	**4.50**
Downside risk	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10

- The inflationary threats of 2008 turn into the deflationary reality of 2009. Central Banks under pressure to reduce rates decisively – even to zero or near-zero – to avoid the perils of a destructive and prolonged recession.

- The downturn in the UK gathers pace and the economy contracts for much of 2009. Prospects for Bank of England "Quantitative easing" increasingly likely**.**

- Pension, hedge and insurance fund values struggle and lead to enhanced demand for longer dated gilts.

Underlying assumptions

- Despite central bank intervention to raise bank capital and improve liquidity, conditions in money and credit markets remain very difficult as banks' lending behaviour changes fundamentally.
- Consumer spending and business investment stall, hampered by the credit drought.
- Falling house prices compel households to review savings levels and repair balance sheets (where possible).
- Commodity prices continue to fall. CPI is projected to fall below the MPC's 1% lower threshold in 2009, providing some relief for the overstretched consumer, but eroding debt burdens more slowly.
- Fear of rising unemployment dampens confidence and any prospect of sizeable wage demands.
- UK public finances are in horrid shape and will worsen as the recession bites, resulting in a slew of gilt issuance in 2009. This will ultimately push gilt yields higher, although not aggressively so.
- Global growth and activity continue to weaken. The Federal Reserve has already cut rates to a range between 0% and 0.25% and has engaged in 'quantitative easing'. The ECB could bring rates down to 2% as European economies struggle with falling domestic and international demand.

Annex C

Specified Investments

(All such investments will be sterling denominated, with **maturities up to maximum of 1 year**, meeting the minimum 'high' rating criteria where applicable)

	Minimum 'High' Credit Criteria	**Use**
UK Government Gilts	Long term AAA	Fund Managers
Treasury Bills	Long term AAA	Fund Managers
Debt Management Agency Deposit Facility	--	In-house
Term deposits – local authorities	--	In-house
Term deposits – banks and building societies **	Short-term F1, Long-term A, Individual C, Support 3	In-house and fund managers
Certificates of Deposits (CDs) – banks and building societies **	Short-term F1, Long-term A, Individual C, Support 3	Fund managers

Non-Specified Investments

Such investments are defined as all investments not meeting the definition of a specified investment. They comprise of the following investments

Fixed term deposits with variable rate and variable maturities: -	**Minimum 'High' Credit Criteria**	**Use**	**Maximum Limit Internally Managed £**	**Maximum Limit Externally Managed £m**
1. Structured deposits including callable deposits, range trades and snowballs.	Short-term F1, Long-term A, Individual C, Support 3	In-house and fund managers	£25 million	£25 million
Certificates of deposits issued by banks and building societies with a maturity of more than one year but less than three years	Short-term F1, Long-term AA-, Individual C, Support 3	Fund Managers		£25 million
Certificates of deposits issued by banks and building	Short-term F1, Long-term AA-, Individual C,	Fund Managers		£25 million

societies with a maturity of more than one year but less than three years	Support 3			
UK Government Gilts	Long term AAA	Fund Managers		£25 million
Bonds issued by multilateral development banks	Long term AAA and listed on either the London or Luxembourg stock exchange	Fund Managers. Also on a 'buy-and-hold' basis in-house.	£25 million	
Bonds issued by a financial institution which is guaranteed by the UK government	Long term AAA and listed on either the London or Luxembourg stock exchange	Fund Managers. Also on a 'buy-and-hold' basis in-house.	£25 million	£7 million
Sovereign bond issues (ie other than the UK govt)	Long Term AA and listed on a recognised stock exchange	Fund Managers		£7 million

Monitoring of credit ratings:

All credit ratings will be monitored ***monthly***. If a counterparty or investment scheme is downgraded with the result that it no longer meets the Council's minimum credit criteria, the use of that counterparty / investment scheme will be withdrawn.
Any intra-month credit rating downgrade which the Council has identified that affects the Council's pre-set criteria will also be similarly dealt with.