AUD101
FOR DECISION
WARD(S): GENERAL

AUDIT COMMITTEE

25 September 2014

TREASURY MANAGEMENT STEWARDSHIP REPORT FOR 2013/14

REPORT OF CHIEF FINANCE OFFICER

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RECENT REFERENCES:

CAB2455 – Treasury Management Strategy 2013/14, 13 February 2013

AUD055 – Treasury Management Policy & Practices, 12 March 2013

AUD073 – Treasury Management Mid-year Review 2013/14, 3 December 2013

CAB2599 – Treasury Management Service, 2 July 2014

EXECUTIVE SUMMARY:

In accordance with the requirements of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management 2009, this report provides detail of the performance of the treasury management function, on the effects of the decisions taken and the transactions executed in the past year, and confirmation that there were no instances of non-compliance with the Council's Treasury Management Policy Statement and Treasury Management Practices, for the year 2013/14.

RECOMMENDATIONS:

That the Audit Committee:

1. Approves the Treasury Management Stewardship Report for 2013/14 and the actual Prudential Indicators provided at Appendix A, and
2. Notes that the Treasury Management Service partnership working with Hampshire County Council was implemented on 15 September 2014.

AUDIT COMMITTEE

25 September 2014

TREASURY MANAGEMENT STEWARDSHIP REPORT FOR 2013/14

1 Introduction

1.1 The Council's Treasury Management Strategy for 2013/14 (CAB2455 refers) is underpinned by the adoption of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management ("the Code"), which requires local authorities to produce annually Prudential Indicators and a Treasury Management Strategy Statement on the likely financing and investment activity for the forthcoming financial year.

1.2 The Code also states the following minimum requirements:

The organisation will receive:

- An annual report on the strategy and plan to be pursued in the coming year;
- A mid-year review;
- An annual report on the performance of the treasury management function, on the effects of the decisions taken and the transactions executed in the past year, and on any circumstances of non-compliance with the organisation's treasury management policy statement and TMPs.

1.3 The full Council approves the Strategy and Plan annually and consideration of the mid-year review and stewardship report is delegated to the Audit Committee.

1.4 Treasury management is defined by the CIPFA Code of Practice on Treasury Management as:

> "The management of the local 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."

1.5 Overall responsibility for treasury management remains with the Council. No treasury management activity is without risk; the effective identification and management of risk are integral to the Council's treasury management objectives.

2 Treasury Management Service

2.1 In July, Cabinet approved the recommendations set out in CAB2599, for the Council to progress proposals for partnership working with Hampshire County Council (HCC) whereby the HCC Investments and Borrowing team would manage the Council's cash balance and undertake investment of surplus cash or sourcing of short term borrowing in accordance with Winchester City Council's agreed Treasury Management Strategy.

2.2 In August, members of the Audit Committee were circulated with the Chief Finance Officer's report recommending the final decision to implement changes to the operation of the Treasury Management Service.

2.3 Following the agreement of the Portfolio Holder for Business Services and the Chairman of the Audit Committee the change in service provision was implemented on 15 September 2014.

3 External Context

3.1 Economic background: At the beginning of the 2013-14 financial year markets were concerned about lacklustre growth in the Eurozone, the UK and Japan. Lack of growth in the UK economy, the threat of a 'triple-dip' alongside falling real wages (i.e. after inflation) and the paucity of business investment were a concern for the Bank of England's Monetary Policy Committee. Only two major economies – the US and Germany – had growth above pre financial crisis levels, albeit these were still below trend. The Eurozone had navigated through a turbulent period for its disparate sovereigns and the likelihood of a near-term disorderly collapse had significantly diminished. The US government had just managed to avoid the fiscal cliff and a technical default in early 2013, only for the problem to re-emerge later in the year.

3.2 With new Governor Mark Carney at the helm, the Bank of England unveiled forward guidance in August pledging to not consider raising interest rates until the ILO unemployment rate fell below the 7% threshold. In the Bank's initial forecast, this level was only expected to be reached in 2016. Although the Bank stressed that this level was a threshold for consideration of rate increase rather an automatic trigger, markets began pricing in a much earlier rise than was warranted and, as a result, gilt yields rose aggressively.

3.3 The recovery in the UK surprised with strong economic activity and growth. Q4 2014 GDP showed year-on-year growth of 2.7%. Much of the improvement was down to the dominant service sector, and an increase in household consumption buoyed by the pick-up in housing transactions which were driven by higher consumer confidence, greater availability of credit and strengthening house prices which were partly boosted by government initiatives such as Help-to-buy. However, business investment had yet to recover convincingly and the recovery was not accompanied by meaningful productivity growth. Worries of a housing bubble were tempered by evidence that net mortgage lending was up by only around 1% annually.

3.4 CPI fell from 2.8% in March 2013 to 1.7% in February 2014, the lowest rate since October 2009, helped largely by the easing commodity prices and discounting by retailers, reducing the pressure on the Bank to raise rates. Although the fall in unemployment (down from 7.8% in March 2013 to 7.2% in January 2014) was faster than the Bank of England or indeed many analysts had forecast, it hid a stubbornly high level of underemployment. Importantly, average earnings growth remained muted and real wage growth (i.e. after inflation) was negative. In February the Bank stepped back from forward guidance relying on a single indicator – the unemployment rate – to more complex measures which included spare capacity within the economy. The Bank also implied that when official interest rates were raised, the increases would be gradual – this helped underpin the 'low for longer' interest rate outlook despite the momentum in the economy.

3.5 The Office of Budget Responsibility's 2.7% forecast for economic growth in 2014 forecast a quicker fall in public borrowing over the next few years. However, the Chancellor resisted the temptation to spend some of the proceeds of higher economic growth. In his 2013 Autumn Statement and the 2014 Budget, apart from the rise in the personal tax allowance and pension changes, there were no significant giveaways and the coalition's austerity measures remained on track.

3.6 The Federal Reserve's then Chairman Ben Bernanke's announcement in May that the Fed's quantitative easing (QE) programme may be 'tapered' caught markets by surprise. Investors began to factor in not just an end to QE but also rapid rises in interest rates. 'Tapering' (a slowing in the rate of QE) began in December 2013. By March 2014, asset purchases had been cut from $75bn to $55bn per month with expectation that QE would end by October 2014. This had particular implications for global markets which had hitherto benefited from, and got very accustomed to, the high levels of global liquidity afforded by QE. The impact went further than a rise in the dollar and higher US treasury bond yields. Gilt yields also rose as a consequence and emerging markets, which had previously benefited as investors searched for yield through riskier asset, suffered large capital outflows in December and January.

3.7 With the Eurozone struggling to show sustainable growth, the European Central Bank cut main policy interest rates by 0.25% to 0.25% and the deposit rate to zero. Markets were disappointed by the lack of action by the ECB despite CPI inflation below 1% and a looming threat of deflation. Data pointed to an economic slowdown in China which, alongside a weakening property market and a highly leveraged shadow banking sector, could prove challenging for its authorities.

3.8 Russia's annexation of the Ukraine in March heightened geopolitical tensions and risk. The response from the West which began with sanctions against Russia which is the second largest gas producer in the world and which supplies nearly 30% of European natural gas needs and is also a significant supplier of crude oil – any major disruption to their supply would have serious ramifications for energy prices.

3.9 Gilt yields ended the year higher than the start in April. The peak in yields was during autumn 2013. The biggest increase was in 5-year gilt yields which increased by nearly 1.3% from 0.70% to 1.97%. 10-year gilt yields rose by nearly 1% ending the year at 2.73%. The increase was less pronounced for longer dated gilts; 20-year yields rose from 2.74% to 3.37% and 50-year yields rose from 3.23% to 3.44%. 3-month, 6-month and 12-month Libid rates remained at levels below 1% through the year.

4 The Borrowing Requirement and Debt Management

4.1 ***Borrowing during 2013/14 & PWLB Certainty Rate*** - the Certainty Rate was introduced by the PWLB in November 2012, allowing the Council to borrow at a reduction of 20bps on the Standard Rate. However, there was no new borrowing during the year and the Council's overdraft facility was not used.

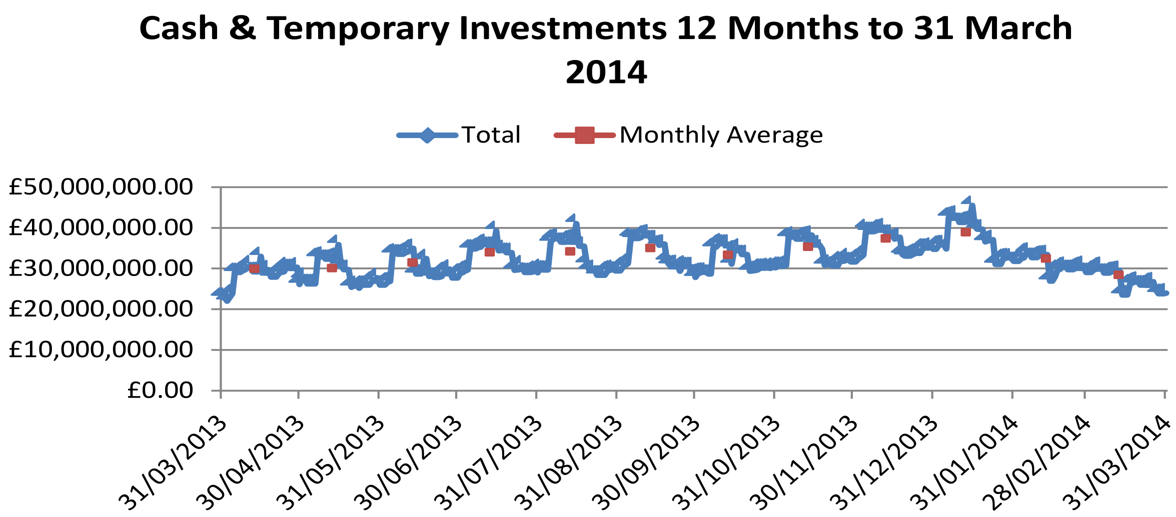
4.2 The Council's underlying need to borrow as measured by the Capital Financing Requirement (CFR) as at 31/3/2014 was £165.7m. The Council's borrowing requirement at the year end was £158.5m. £6.6m of capital expenditure was funded from internal resources in 2013/14.

4.3 The use of internal resources in lieu of borrowing has continued to be the most cost effective means of funding new unfinanced capital expenditure. This has lowered overall treasury risk by reducing both external debt and temporary investments. However, the Council recognises that this will not be sustainable in the medium term and continues to keep borrowing options under review, in consultation with the Council's treasury advisers.

	Balance at 01/04/2013 £m	New Borrowing £m	Debt Maturing £m	Debt Prematurely Repaid £m	Balance at 31/03/2014 £m	Avg Rate %/ Avg Life (yrs)
Capital Financing Requirement (CFR)	162.4				165.7	
Short Term Borrowing	0.0	0.0	0.0	0.0	0.0	
Long Term Borrowing	156.7	0.0	0.0	0.0	156.7	23 years @ 3.30%
TOTAL BORROWING	156.7	0.0	0.0	0.0	156.7	
Other Long Term Liabilities	2.1	0.0	(0.3)	0.0	1.8	6 years @ 2.16%
TOTAL EXTERNAL DEBT	158.8	0.0	(0.3)	0.0	158.5	

5 Investment Activity

5.1 The Guidance on Local Government Investments gives priority to security and liquidity and the Council's aim is to achieve a yield commensurate with these principles. The average daily balances that were held during 2013/14 are shown below:



5.2 Investment activity was as follows:

	Balance at 01/04/2013 £000s	Investments Made £000s	Maturities £000s	Balance at 31/03/2014 £000's	Increase/ (decrease) in Investments £000's
Short Term Investments					
Call Accounts	7,000	7,000	4,000	10,000	3,000
Pooled Funds	4,300	97,700	97,300	4,700	400
Certificates of Deposit	1,000	13,000	10,000	4,000	3,000
Term Deposits					
Local Authorities	3,000	6,500	8,500	1,000	(2,000)
Debt Management Office	0	0	0	0	0
Banks	3,000	11,000	12,000	2,000	(1,000)
Building Societies	2,000	6,500	7,500	1,000	(1,000)
Long Term Investments	1,000	1,000	0	2,000	1,000
TOTAL INVESTMENTS	21,300	142,700	139,300	24,700	3,400

Other Interest Bearing	Balance at 01/04/2013 £000s	Cash Received * £000s	Cash Paid * £000s	Balance at 31/03/2014 £000's	Increase/ (decrease) in Balance £000's
Current Account	2,630	138,676	140,011	1,295	(1,335)
Total External Balances	23,930	(624)	(2,689)	25,995	2,065

5.3 Analysis of average balances & interest receivable for the 12 months to 31 March 2014

Chart 1
Average Investment per Sector

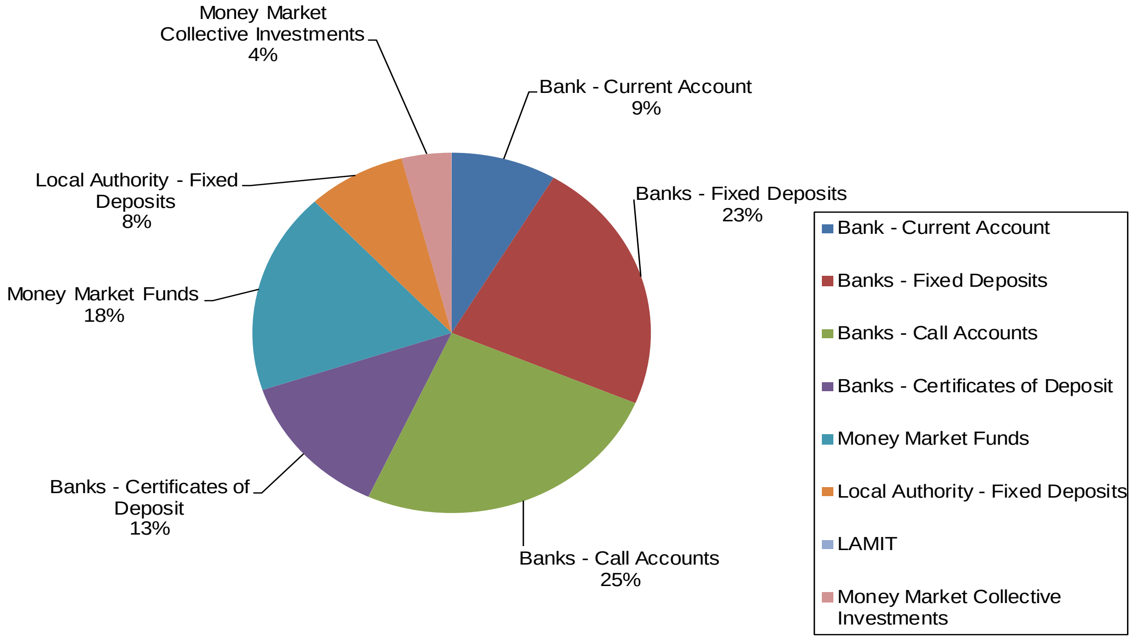
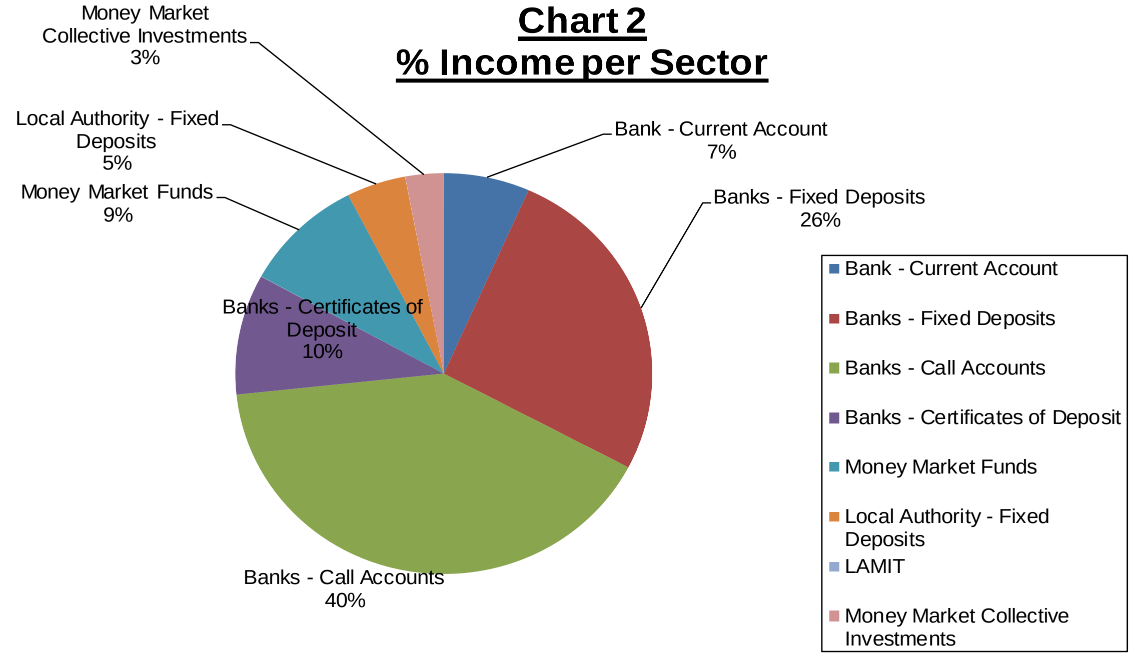


Chart 2
% Income per Sector



Type of Deposit	Average Holding £000's	Interest £000's	Interest %	Share of Total Investment	Share of Total Income
Bank - Current Account	2,607	15	0.52%	8%	4.53%
Banks - Fixed Deposits	6,975	59	0.27%	21%	17.72%
Banks - Call Accounts	7,786	92	0.91%	24%	27.58%
Banks - Certificates of Deposit	3,981	22	0.18%	12%	6.61%
Money Market Funds	5,527	21	0.27%	17%	6.39%
Local Authority - Fixed Deposits	2,437	10	0.15%	8%	3.12%
LAMIT	1,921	107	5.29%	6%	32.03%
Money Market Collective Investments	1,240	7	0.51%	4%	2.02%
	32,473	334	0.73%		

5.4 Security of capital has remained the Council's main investment objective. This has been maintained by following the Council's counterparty policy as set out in its Treasury Management Strategy Statement for 2013/14 (per CAB2455).

<u>Credit developments and credit risk management</u>

5.5 The Council assessed and monitored counterparty credit quality with reference to credit ratings; credit default swaps; GDP of the country in which the institution operates; the country's net debt as a percentage of GDP and share price. The minimum long-term counterparty credit rating determined by the Authority for the 2013/14 treasury strategy was A- across rating agencies Fitch, S&P and Moody's.

5.6 The debt crisis in Cyprus was resolved by its government enforcing a 'haircut' on unsecured investments and bank deposits over €100,000. This resolution mechanism, in stark contrast to the bail-outs during the 2008/2009 financial crisis, sent shockwaves through Europe but allowed banking regulators to progress reform which would in future force losses on investors through a 'bail-in' before taxpayers were asked to support failing banks.

5.7 The Financial Services (Banking Reform) Act 2013 gained Royal Assent in December, legislating for the separation of retail and investment banks and for the introduction of mandatory bail-in in the UK to wind up or restructure failing financial institutions. EU finance ministers agreed further steps towards banking union, and the Single Resolution Mechanism (SRM) for resolving problems with troubled large banks which will shift the burden of future restructurings/rescues to the institution's shareholders, bondholders and unsecured investors.

5.8 Proposals were also announced for EU regulatory reforms to Money Market Funds which may result in these funds moving to a VNAV (variable net asset value) basis and losing their 'triple-A' credit rating wrapper in the future.

5.9 The material changes to UK banks' creditworthiness were (a) the strong progress made by the Lloyds Banking Group in strengthening its balance sheet, profitability and funding positions and the government reducing its shareholding in the Group to under 25%, (b) the announcement by Royal Bank of Scotland of the creation of an internal bad bank to house its riskiest assets (this amounted to a material extension of RBS' long-running restructuring, further delaying the bank's return to profitability) and (c) substantial losses at Co-op Bank which forced the bank to undertake a liability management exercise to raise further capital and a debt restructure which entailed junior bondholders being bailed-in as part of the restructuring.

5.10 In July Moody's placed the A3 long-term ratings of Royal Bank of Scotland and NatWest Bank and the D+ standalone financial strength rating of RBS on review for downgrade amid concerns about the impact of any potential breakup of the bank on creditors. As a precautionary measure the Council reduced its duration to overnight for new investments with the bank(s). In March Moody's downgraded the long-term ratings of both banks to Baa1. As this rating is below the Authority's minimum credit criterion of A-, the banks were withdrawn from the counterparty list for further investment. However, in line with the Treasury Management Strategy, as NatWest is the Council's banker it will continue to be used for operational and liquidity purposes. The Co-op's long-term ratings were downgraded by Moody's and Fitch to Caa1 and B respectively, both sub-investment grade ratings.

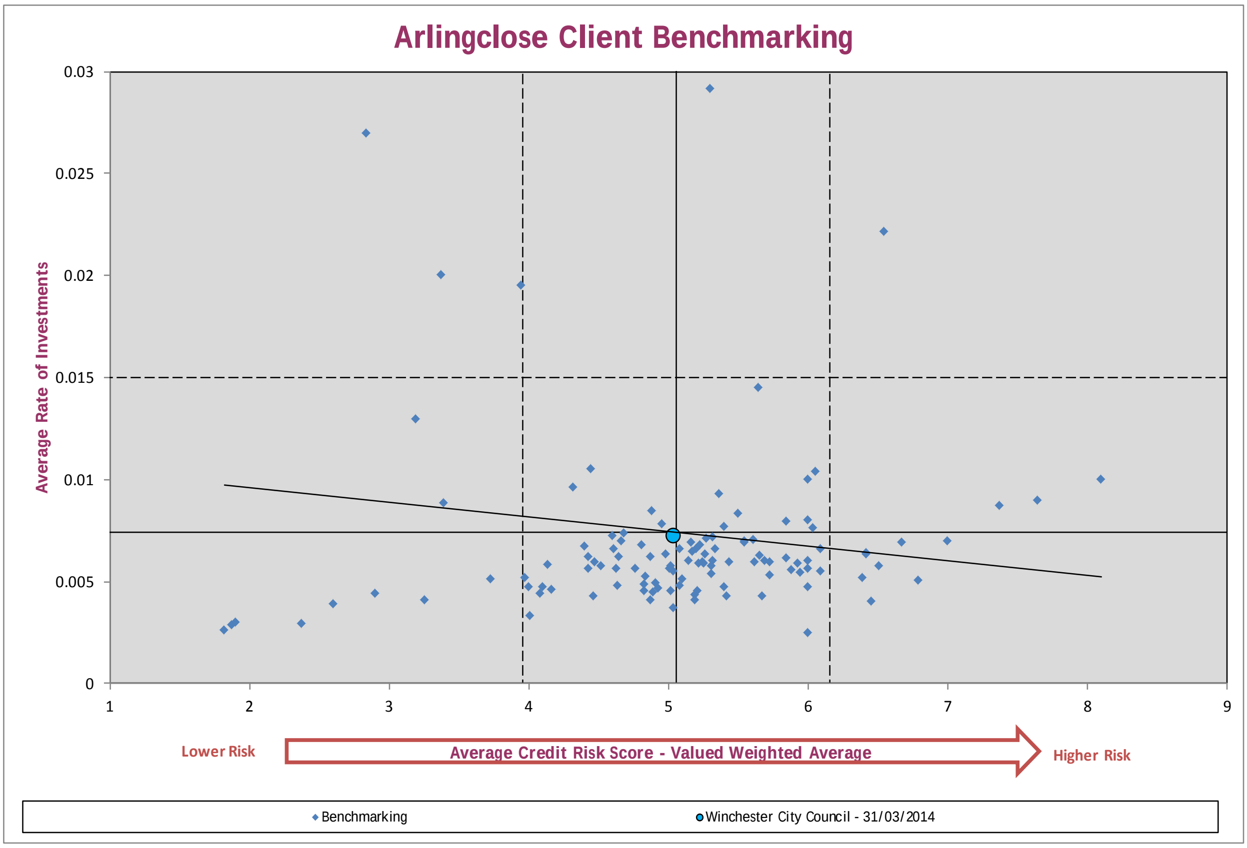
5.11 Counterparty credit quality has weakened through the year, as can be demonstrated by the Credit Score Analysis summarised below.

Date	Value Weighted Average – Credit Risk Score	Value Weighted Average – Credit Rating	Time Weighted Average – Credit Risk Score	Time Weighted Average – Credit Rating
31/03/2013	4.94	A+	4.61	A+
30/06/2013	5.21	A+	5.14	A+
30/09/2013	5.32	A+	5.66	A+
31/12/2013	5.14	A+	5.19	A+
31/03/2014	5.03	A+	5.06	A+

Scoring:

-Value weighted average reflects the credit quality of investments according to the size of the deposit
-Time weighted average reflects the credit quality of investments according to the maturity of the deposit
-AAA = highest credit quality = 1
- D = lowest credit quality = 15
-Aim = A+ or higher credit rating, with a score of 5 or lower, to reflect current investment approach with main focus on security

5.12 The Council's value weighted average credit risk score at 31 March 2014, represented by the blue circle on the chart below, is slightly below mean risk and return for Arlingclose's English Non Metropolitan District Council clients short term investments.



5.13 The Chief Finance Officer can report that the investment portfolio has been managed within the counterparty limits.

5.14 Liquidity: in keeping with the DCLG's Guidance on Investments, the Council maintained a sufficient level of liquidity through the use of Money Market Funds, a current account bearing interest, and the use of call accounts.

5.15 Yield: the Council sought to optimise returns commensurate with its objectives of security and liquidity. The UK Bank Rate remained at 0.5% through the year. Short term money market rates also remained at very low levels which had a significant impact on investment income.

Budgeted Interest Income and performance in the year.

(i) The Council's budgeted investment income for the year was set at £74,000 based on 0.5% interest rate on average cash balances representing the Council's reserves and working balances of £19.8m during the period.

(ii) The UK Bank Base Rate has been maintained at 0.5% since March 2009 and is expected to rise within the next 3 years per Arlingclose forecasts. Short-term money market rates have remained at very low levels. The Council has an investment income outturn of £334,000 / 0.73% for the whole year on average balances of £33m.

6 <u>Other Holdings</u>

6.1 Local Authorities Mutual Investment Trust (LAMIT)

a) At 31 March 2014, the Council held 870,161 property fund units in LAMIT. 422,654 units were purchased in 1989/90 at a cost price of £1 million and 447,507 units were purchased on the 30/04/2014. The value of LAMIT has been subject to market fluctuations.

Valuation date	Value*	Gain / (Loss) on investment (unrealised)
31st March 2010	£913,000	(87,000)
31st March 2011	£962,000	(38,000)
31st March 2012	£963,000	(37,000)
31st March 2013	£945,000	(55,000)
31st March 2014	£2,115,000	115,000

b) Dividends receivable on this investment amounted to £106,543 for the year to 31 March 2014.

6.2 <u>Heritable Bank in Administration</u>

The Council had an investment of £1m with Heritable Bank Ltd which was placed into Administration in October 2008. The Council has now recovered 94% of its investment. It is likely that further distributions will be received, although the administrators have not made any further estimate of final recoveries yet.

7 Compliance with Prudential Indicators

7.1 The Chief Finance Officer can confirm that the Council has complied with its Prudential Indicators for 2013/14, which were approved as part of the Council's Treasury Management Strategy Statement (CAB2455). Details can be found in Appendix A.

7.2 In compliance with the requirements of the CIPFA Code of Practice this report provides members with a summary report of the treasury management activity during 2013/14. None of the Prudential Indicators have been breached and a prudent approach has been taking in relation to investment activity with priority being given to security and liquidity over yield.

OTHER CONSIDERATIONS:

8 COMMUNITY STRATEGY AND PORTFOLIO PLANS (RELEVANCE TO):

8.1 The Treasury Management Strategy supports all tenets of the Sustainable Community Strategy including the core value of being efficient and ensuring value for money.

9 RESOURCE IMPLICATIONS:

9.1 Investment income amounted to £334K in 2013/14 (£213k in 2012/13).

9.2 Interest payable

a) As a consequence of the HRA finance reform settlement £5.168m interest was payable on the £156.722m loans taken out to finance the reform.

b) An embedded lease within the Joint Environmental Services Contract cost £349k; comprising £307k capital repayment, and £43k interest.

10 RISK MANAGEMENT ISSUES

10.1 These are considered within the report. The Council's Treasury Management Practices provide a detailed consideration of the management of treasury risks.

BACKGROUND DOCUMENTS:

None

APPENDICES:

Appendix A Prudential Indicators

Appendix B Glossary of Terms

PRUDENTIAL INDICATORS

Debt and Investment Portfolio position at 31/3/14

	Actual Portfolio 31/03/2014 £m	Average Rate %
Total External Borrowing - (PWLB – Fixed Rate)	156.7	**3.3**
Other Long Term Liabilities: Finance Leases	1.8	2.2
Total Gross External Debt	**158.5**	
Investments (*Managed in-house)* Short-term investments	24.0	
Pooled Funds *(Local Authority Mutual Investment Trust)*	2.0	
Total Investments	**26**	
Net Debt	**132.5**	

Capital Financing Requirement Estimates of the Council's cumulative maximum external borrowing requirement for 2013/14 to 2015/16 are shown in the table below:

Capital Financing Requirement	31/03/2014 Approved £m	31/03/2014 Revised £m	31/03/2014 Actual £m	31/03/2015 Estimate £m	31/03/2016 Estimate £m
General Fund	13.5	7.4	5.4	31.6	31.5
HRA	163.4	163.3	160.3	165.2	165.8
	176.9	170.7	165.7	196.8	197.3

Gross Debt and the Capital Financing Requirement: In order to ensure that over the medium term debt will only be for a capital purpose, the Authority should ensure that debt does not, except in the short term, exceed the total of capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years. This is a key indicator of prudence.

Debt	31/03/2014 Approved £m	31/03/2014 Revised £m	31/03/2014 Actual £m	31/03/2015 Estimate £m	31/03/2016 Estimate £m
Borrowing	176.9	170.7	156.7	196.8	197.3
Finance Leases	1.8	1.8	1.8	1.5	1.2
Total Debt	178.7	172.5	158.5	198.3	198.5
Borrowing in excess of CFR	N	N	N	N	N

PRUDENTIAL INDICATORS

Authorised Limit and Operational Boundary for External Debt

The Operational Boundary for External Debt is based on the Authority's estimate of most likely, i.e. prudent, but not worst case scenario for external debt. It links directly to the Authority's estimates of capital expenditure, the capital financing requirement and cash flow requirements and is a key management tool for in-year monitoring. Other long-term liabilities comprise finance lease, Private Finance Initiative and other liabilities that are not borrowing but form part of the Authority's debt.

The Authorised Limit for External Debt is the affordable borrowing limit determined in compliance with the Local Government Act 2003. It is the maximum amount of debt that the Authority can legally owe. The authorised limit provides headroom over and above the operational boundary for unusual cash movements.

The Chief Finance Officer confirms that there were no breaches to the Authorised Limit and the Operational Boundary during 2013/14; borrowing remained at £156.7m throughout.

£000's	Approved Authorised Limt	Approved Operational Boundary	Actual External Debt at 31/03/2014
Borrowing	176.9	171.9	156.7
Other Long-term Liabilities	6.0	4.0	1.8
	182.9	**175.9**	**158.5**

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

This indicator is set to control the Authority's exposure to interest rate risk. The upper limits on fixed and variable rate interest rate exposures is provided in the table below.

	Original Limits for 2013/14 £m	**Revised Estimate for 2013/14 £m**	**Maximum during 2013/14 £m**
Upper Limit for Fixed Rate	176.9	176.0	156.7
Compliance with Limits:	Yes	Yes	Yes
Upper Limit for Variable Rate	15	0.0	0.0
Compliance with Limits:	Yes	Yes	Yes

Maturity Structure of Fixed Rate Borrowing

This indicator is to limit large concentrations of fixed rate debt needing to be replaced at times of uncertainty on interest rates.

PRUDENTIAL INDICATORS

PI Maturity structure of fixed rate borrowing	Lower Limit	Upper Limit	Actual Fixed Rate Borrowing at 31 March 2014	% Fixed Rate Borrowing at 31 March 2014	Compliance with Set Limits?
	£m	£m	£m	%	
Under 12 months	0.0	15.0	0.0	0.0	Yes
12 months and within 24 months	0.0	20.2	0.0	0.0	Yes
24 months and within 5 years	0.0	20.2	0.0	0.0	Yes
5 years and within 10 years	0.0	20.2	10.0	6.4	Yes
10 years and within 20 years	0.0	85.2	55.0	35.1	Yes
20 years and within 30 years	0.0	55.2	35.0	22.3	Yes
30 years and within 40 years	0.0	40.2	20.0	12.8	Yes
40 years and within 50 years	0.0	56.9	36.7	23.4	Yes
50 years and above	0.0	20.2	0.0	0.0	Yes
Total	0.0		156.7	100.0	Yes

Capital expenditure

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 and in the case of the HRA, housing rent levels.

Capital Expenditure	31/03/2014 Approved £m	31/03/2014 Revised £m	31/03/2014 Actual £m	31/03/2015 Estimate £m	31/03/2016 Estimate £m
Non-HRA	18.0	10.1	8.0	18.0	1.1
HRA	12.3	10.7	10.0	13.6	13.1
Total	**30.3**	**20.8**	**18.0**	**31.6**	**14.2**

Capital Financing	31/03/2014 Approved £m	31/03/2014 Revised £m	31/03/2014 Actual £m	31/03/2015 Estimate £m	31/03/2016 Estimate £m
Capital Receipts	1.2	2.1	1.6	0.4	0.2
Government Grants & contributions	1.9	0.4	0.4	0.4	0.5
Reserves	7.1	7.6	6.7	6.1	6.2
Revenue Contributions	6.2	3.27	2.57	6.1	6.6
Total Financing	**16.4**	**13.4**	**11.3**	**13.0**	**13.5**
Supported Borrowing	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Unsupported Borrowing	**13.9**	**7.4**	**6.7**	**18.6**	**0.7**
Total Funding	**13.9**	**7.4**	**6.7**	**18.6**	**0.7**
Total Financing and Funding	30.3	20.8	18.0	31.6	14.2

PRUDENTIAL INDICATORS

Ratio of Financing Costs to Net Revenue Stream

This is an indicator of affordability and highlights the revenue implications of existing capital expenditure by identifying the proportion of the revenue budget required to meet financing costs, net of investment income.

Affordability Indicator	2013/14 Approved %	2013/14 Revised %	2013/14 Actual %	2014/15 Estimate %	2015/16 Estimate %
Non-HRA	(1.0)	(1.4)	(2.3)	0.5	3.8
HRA	20.5	20.2	20.1	19.5	18.6

Adoption of the CIPFA Treasury Management Code

This indicator demonstrates that the Authority adopted the principles of best practice.

The Council has adopted the CIPFA Treasury Management code under the Constitution, Financial Procedure Rule 5.4 (CAB313, 13 February 2002 refers)

Upper limit for Total Principal Sums Invested over 364 Days

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

Upper Limit for total principal sums invested over 364 days	31/03/2014 Approved	31/03/2014 Actual	31/03/2015 Estimate	31/3/16 Estimate
	£m	£m	£m	£m
	15.0	2.0	15.0	15.0

HRA Limit on indebtedness

HRA Limit on Indebtedness	31/3/14 Approved	31/3/14 Actual	31/3/15 Estimate	31/3/15 Estimate
	£m	£m	£m	£m
HRA CFR	163.4	160.3	163.4	166.9
HRA Debt Cap (as prescribed by DCLG)	166.9	166.9	166.9	166.9
Difference	3.5	6.6	3.5	0.0

Glossary

AAA-rating The best *credit rating* that can be given to a borrower's debts, indicating that the risk of borrowing *defaulting* is minuscule.

Base rate The key interest rate set by the Bank of England. It is the overnight interest rate that it charges to banks for lending to them. The base rate - and expectations about how the base rate will change in the future - directly affect the interest rates at which banks are willing to lend money in sterling.

Basis point One hundred basis points make up a percentage point, so an interest rate cut of 25 basis points might take the rate, for example, from 3% to 2.75%.

Bill A debt *security* - or more simply an IOU. It is very similar to a *bond*, but has a maturity of less than one year when first issued.

Bond A debt *security*, or more simply, an IOU. The bond states when a loan must be repaid and what interest the borrower (issuer) must pay to the holder. They can be issued by companies, banks or governments to raise money. Banks and investors buy and trade bonds.

Commercial paper Unsecured, short-term loans taken out by companies. The funds are typically used for working capital, rather than fixed assets such as a new building. The loans take the form of IOUs that can be bought and traded by banks and investors, similar to bonds.

CPI The Consumer Prices Index is a measure of the price of a bundle of goods and services from across the economy. It is the most common measure used to identify inflation in a country. CPI is used as the target measure of inflation by the Bank of England and the *ECB*.

Credit default swap (CDS) A financial contract that provides insurance-like protection against the risk of a third-party borrower defaulting on its debts. For example, a bank that has made a loan to Greece may choose to hedge the loan by buying CDS protection on Greece. The bank makes periodic payments to the CDS seller. If Greece *defaults* on its debts, the CDS seller must buy the loans from the bank at their full face value. CDSs are not just used for hedging - they are used by investors to speculate on whether a borrower such as Greece will default.

Credit rating The assessment given to debts and borrowers by a *ratings agency* according to their safety from an investment standpoint - based on their creditworthiness, or the ability of the company or government that is borrowing to repay. Ratings range from *AAA*, the safest, down to D, a company that has already *defaulted*. Ratings of BBB- or higher are considered "investment grade". Below that level, they are considered "speculative grade" or more colloquially as *junk*.

Deflation Negative inflation - that is, when the prices of goods and services across the whole economy are falling on average.

Derivative A financial contract which provides a way of investing in a particular product without having to own it directly. For example, a stock market *futures* contract allows investors to make bets on the value of a stock market index such as the FTSE 100 without having to buy or sell any shares. The value of a derivative can depend on anything from the price of coffee to interest rates or what the weather is like. Credit derivatives such as *credit default swaps* depend on the ability of a borrower to repay its debts. Derivatives allow investors and banks to hedge their risks, or to speculate on markets. *Futures*, *forwards*, *swaps* and *options* are all types of derivatives.

Fiscal policy The government's borrowing, spending and taxation decisions. If a government is worried that it is borrowing too much, it can engage in austerity - raising taxes and cutting spending. Alternatively, if a government is afraid that the economy is going into recession it can engage in fiscal stimulus - cutting taxes, raising spending and raising borrowing.

Hedging Making an investment to reduce the risk of price fluctuations to the value of an asset. Airlines often hedge against rising oil prices by agreeing in advance to buy their fuel at a set price. In this case, a rise in price would not harm them - but nor would they benefit from any falls.

ILO International Labour Organisation

Impairment charge The amount written off by a company when it realises that it has valued an asset more highly than it is actually worth.

Inflation The upward price movement of goods and services.

Junk bond A *bond* with a *credit rating* of BB+ or lower. These debts are considered very risky by the *ratings agencies*. Typically the bonds are traded in markets at a price that offers a very high *yield* (return to investors) as compensation for the higher risk of *default*.

LAMIT Local Authorities Mutal Investment Trust, a property fund exclusively for local authorities to invest in commercial and industrial property. Its objective is to provide a satisfactory total capital and income return over the long term

Leverage Leverage, or gearing, means using debt to supplement investment. The more you borrow on top of the funds (or *equity*) you already have, the more highly leveraged you are. Leverage can increase both gains and losses. *Deleveraging* means reducing the amount you are borrowing.

Libid London Inter Bank Bid Rate. The average rate at which banks in London borrow money to each other for the short-term in a particular currency. A new Libid rate is set every morning by the *British Bankers Association*.

Libor London Inter Bank Offered Rate. The rate at which banks in London lend money to each other for the short-term in a particular currency. A new Libor rate is set every morning by the *British Bankers Association*.

Liquidity How easy something is to convert into cash. Your current account, for example, is more liquid than your house. If you needed to sell your house quickly to pay bills you would have to drop the price substantially to get a sale.

Monetary policy The policies of the central bank. A central bank has an unlimited ability to create new money. This allows it to control the short-term interest rate, as well as to engage in unorthodox policies such as *quantitative easing* - printing money to buy up government debts and other *assets*. Monetary policy can be used to control inflation and to support economic growth.

Money markets Global markets dealing in borrowing and lending on a short-term basis.

PWLB Public Works Loan Board, the function of the board, derived chiefly from the Public Works Loan Act 1875 and the National Loans Act 1968, is to consider loan applications from local authorities and other prescribed bodies and to collect repayments

Quantitative easing Central banks increase the supply of money by "printing" more. In practice, this may mean purchasing government bonds or other categories of assets, using the new money. Rather than physically printing more notes, the new money is typically issued in the form of a deposit at the central bank. The idea is to add more money into the system, which depresses the value of the currency, and to push up the value of the assets being bought and to lower longer-term interest rates, which encourages more borrowing and investment. Some economists fear that quantitative easing can lead to very high inflation in the long term.

Rating The assessment given to debts and borrowers by a *ratings agency* according to their safety from an investment standpoint - based on their creditworthiness, or the ability of the company or government that is borrowing to repay. Ratings range from *AAA*, the safest, down to D, a company that has already *defaulted*. Ratings of BBB- or higher are considered "investment grade". Below that level, they are considered "speculative grade" or more colloquially as *junk*.

Rating agency A company responsible for issuing *credit ratings*. The major three rating agencies are Moody's, Standard & Poor's and Fitch.

Recapitalisation To inject fresh *equity* into a firm or a bank, which can be used to absorb future losses and reduce the risk of *insolvency*. Typically this will happen via the firm issuing new shares. The cash raised can also be used to repay debts. In the case of a government recapitalising a bank, it results in the government owning a stake in the bank. In an extreme case, such as Royal Bank of Scotland, it can lead to *nationalisation*, where the government owns a majority of the bank.

Recession A period of negative economic growth. In most parts of the world a recession is technically defined as two consecutive quarters of negative economic growth - when real output falls. In the United States, a larger number of factors are taken into account, such as job creation and manufacturing activity. However, this means that a US recession can usually only be defined when it is already over.

Securities lending When one broker or dealer lends a security (such as a bond or a share) to another for a fee. This is the process that allows *short selling*.

Securitisation Turning something into a *security*. For example, taking the debt from a number of mortgages and combining them to make a financial product, which can then be traded (see *mortgage backed securities*). Investors who buy these securities receive income when the original home-buyers make their mortgage payments.

Security A contract that can be assigned a value and traded. It could be a share, a bond or a mortgage-backed security.

Separately, the term "security" is also used to mean something that is pledged by a borrower when taking out a loan. For example, mortgages in the UK are usually secured on the borrower's home. This means that if the borrower cannot repay, the lender can seize the security - the home - and sell it in order to help repay the outstanding debt.

Spread (yield) The difference in the *yield* of two different *bonds* of approximately the same maturity, usually in the same currency. The spread is used as a measure of the market's perception of the difference in creditworthiness of two borrowers.

Swap A *derivative* that involves an exchange of cashflows between two parties. For example, a bank may swap out of a fixed long-term interest rate into a variable short-term interest rate, or a company may swap a flow of income out of a foreign currency into their own currency.

Warrants A document entitling the bearer to receive shares, usually at a stated price.

Working capital A measure of a company's ability to make payments falling due in the next 12 months. It is calculated as the difference between the company's current assets (unsold inventories plus any cash expected to be received over the coming year) minus its current liabilities (what the company owes over the same period). A healthy company should have a positive working capital. A company with negative working capital can experience cashflow problems.

Yield The return to an investor from buying a *bond* implied by the bond's current market price. It also indicates the current cost of borrowing in the market for the bond issuer. As a bond's market price falls, its yield goes up, and vice versa. Yields can increase for a number of reasons. Yields for all bonds in a particular currency will rise if markets think that the central bank in that currency will raise short-term interest rates due to stronger growth or higher inflation. Yields for a particular borrower's bonds will rise if markets think there is a greater risk that the borrower will *default*.