AUD038
FOR DECISION
WARD(S): GENERAL

AUDIT COMMITTEE

25 September 2012

TREASURY MANAGEMENT STEWARDSHIP REPORT FOR 2011/12

REPORT OF HEAD OF FINANCE

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RECENT REFERENCES:

CAB2117 – Treasury Management Strategy 2011/12, 9 February 2011

AUD011 – Treasury Management Stewardship Report 2010/11, 26 Sept. 2011

AUD015 – Treasury Management Mid-year review 2011-12, 5 December 2011

AUD020 – Treasury Management Strategy 2011/12 – Implications of Housing Finance Reform, 5 December 2011

CAB2284 – Treasury Management Strategy 2012/13 and 2011/12 Revision, 8 February 2012

EXECUTIVE SUMMARY:

The Treasury Management Strategy for 2011/12 (CAB2117) has been underpinned by the adoption of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management 2009, which includes the requirement for determining a treasury strategy on the likely financing and investment activity for the forthcoming financial year.

The Code also recommends that members are informed of treasury management activities at least twice a year. This report therefore ensures that the Council is embracing Best Practice in accordance with CIPFA's recommendations.

Treasury management is defined 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."

RECOMMENDATIONS:

That the Audit Committee:

Approves the Treasury Management Stewardship Report for 2011/12 and the actual Prudential Indicators provided at Appendix A.

AUDIT COMMITTEE

25 September 2012

TREASURY MANAGEMENT STEWARDSHIP REPORT 2011/12

1 Introduction

1.1 The Treasury Management Strategy for 2011/12 (CAB2117) has been underpinned by the adoption of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management, which includes the requirement for determining a treasury strategy on the likely financing and investment activity for the forthcoming financial year.

1.2 The Code also recommends that members are informed of Treasury Management activities at least twice a year. This report therefore ensures the Council is embracing Best Practice in accordance with CIPFA's recommendations.

1.3 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."

1.4 Arlingclose commenced as the Council's treasury management advisers on 1 April 2011 following a request for quotations exercise.

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 Economic Background

2.1 At the time of determining the 2011/12 strategy in Jan/Feb 2011, there were tentative signs that the UK was emerging from recession with the worst of the financial crisis behind it. Recovery in growth was expected to be slow and uneven as the austerity measures announced in the 2010 Comprehensive Spending Review were implemented in order to bring down the budget deficit and government borrowing and rebalance the economy and public sector finances. Inflation measured by the Consumer Price Index (CPI) had remained stubbornly above 3%. Unemployment was at a 16-year high at 2.5 million and was expected to rise further as the public and private sector contracted. There was a also high degree of uncertainty surrounding Eurozone sovereign debt sustainability.

2.2 Inflation: During 2011-12 inflation remained high with CPI (the official measure) and RPI rising in September to 5.2% and 5.6% respectively primarily due to escalating utility prices and the January 2011 increase in VAT to 20%. Inflation eased slowly as reductions in transport costs, food prices, intensifying competition amongst retailers and supermarkets and the VAT effect falling out in 2012, pushed February 2012's CPI down to 3.4% and RPI to 3.7%. This, however, was not enough to offset low wage growth and, as a result, Britons suffered the biggest drop in disposable income in more than three decades.

2.3 Growth, Employment, House Prices : Growth, on the other hand, remained elusive. The Bank's Quarterly Inflation Reports painted a bleak picture as the outlook was downgraded to around 1% in 2011 and 2012 alongside. The unresolved problems in the Eurozone weighed negatively on global economic prospects. UK GDP was positive in only the first and third calendar quarters of 2011; annual GDP to December 2011 registered just 0.5%. Unemployment rose to 2.68 million and, worryingly, youth unemployment broke through the 1 million barrier. House prices struggled to show sustained growth and consumer confidence remained fragile.

2.4 Monetary Policy : It was not surprising that the Bank of England's Monetary Policy Committee maintained the status quo on the Bank Rate which has now been held at 0.5% since March 2009, but increased asset purchases by £75bn in October 2011, £50bn in February 2012 and another £50m in July 2012 taking the Quantitative Easing (QE) total to £375bn.

2.5 The policy measures announced in the March 2012 Budget statement were judged to be neutral. The Government stuck broadly to its austerity plans as the economy was rebalancing slowly. The opinion of independent Office for Budget Responsibility (OBR) was that the Government was on track to meet its fiscal targets; the OBR identified oil price shocks and a further deterioration in Europe as the main risks to the outlook for growth and in meeting the fiscal target.

2.6 Markets sentiment oscillated between 'risk on'/'risk off' modes, this swing becoming the norm for much of 2011/12 as investors shifted between riskier assets and the relative safety of higher quality Government bonds. Gilts, however, were a principal beneficiary of the 'risk-off' theme which helped push yields lower. There was little market reaction to or impact on gilts by the decision by Fitch and Moody's to change the outlook on the UK's triple-A rating from stable to negative. Over the 12-month period from April 2011 to March 2012, 5-year gilt yields more than halved from 2.40% to 1.06%; 10-year gilt yields fell from 3.67% to 2.25%; 20-year yields fell from 4.30% to 3.20% and 50-year yields from 4.20% to 3.35%. PWLB borrowing rates fell commensurately (see table 2 in appendix 2), but the cost of carry associated with borrowing longer-term loans whilst investing the monies temporarily until required for capital financing remained high, in excess of 4.1 % for 20-year PWLB Maturity borrowing.

3 Reform of Council Housing Finance

3.1 The Localism Act passed into law in November 2011 which enabled the reform of council housing finance. The Housing Revenue Account subsidy system has now been abolished and replaced with self-financing whereby authorities support their own housing stock from their own income. This reform required the Council to take on housing-related debt based on a valuation of its council housing stock. The CLG issued the final Settlement Payment Determination in February 2012. Settlement date for the Self Financing transaction was Wednesday 28th March 2012.

3.2 As the Council's debt level generated by the housing reform model was higher than the Subsidy Capital Financing Requirement (SCFR), the Council was required to pay the CLG the difference between the two, which was £156.722m.

3.3 A preferential set of PWLB rates at 13bps above the equivalent gilt yield were available for this transaction on 26 March only, for settlement on 28 March. Given the one-off nature of the PWLB funding window and the advantages offered in terms of rate, loan structure and administration, the Council took the decision to fund all the £156.722m through new borrowing from the PWLB.

3.4 Loan structures and maturities were discussed and analysed with the Council's Treasury Advisors to fit in with the Council's HRA business plan and strategy, funding costs, as well as the Council's existing treasury management position and risk profile. Details of the loans borrowed are in section 4, below. The Council will continue to work with its Treasury Advisors and Housing Consultants to manage the HRA Business Plan and accounting implications going forward.

3.5 The Council approved the adoption of a "two pool" approach in relation to the allocation of debt between the General Fund and the HRA.

4 The Borrowing Requirement and Debt Management

4.1

	Balance on 01/04/2011 £m	New Borrowing £m	Debt Maturing £m	Debt Prematurely Repaid £m	Balance on 31/03/2012 £m	Avg Rate %/ Avg Life (yrs)
CFR	4.2				164.5	
Short Term Borrowing	0.0	0.0	0.0	0.0	0.0	
Long Term Borrowing	0.0	156.7	0.0	0.0	156.7	25 years @ 3.30%
TOTAL BORROWING	0.0	156.7	0.0	0.0	156.7	
Other Long Term Liabilities	0.0	2.6	(0.2)	0.0	2.4	8 years @ 2.16%
TOTAL EXTERNAL DEBT	0.0	159.3	(0.2)	0.0	159.1	

The Council's underlying need to borrow as measured by the Capital Financing Requirement (CFR) as at 31/3/2012 was estimated at £164.5m. The Council's borrowing requirement during the year was £159.1m.

The Council funded £1.3m of its capital expenditure through the use of its internal resources. No new external borrowing was required for that purpose.

4.2 Borrowing during 2011/12

PWLB Loans taken out 28 March 2012

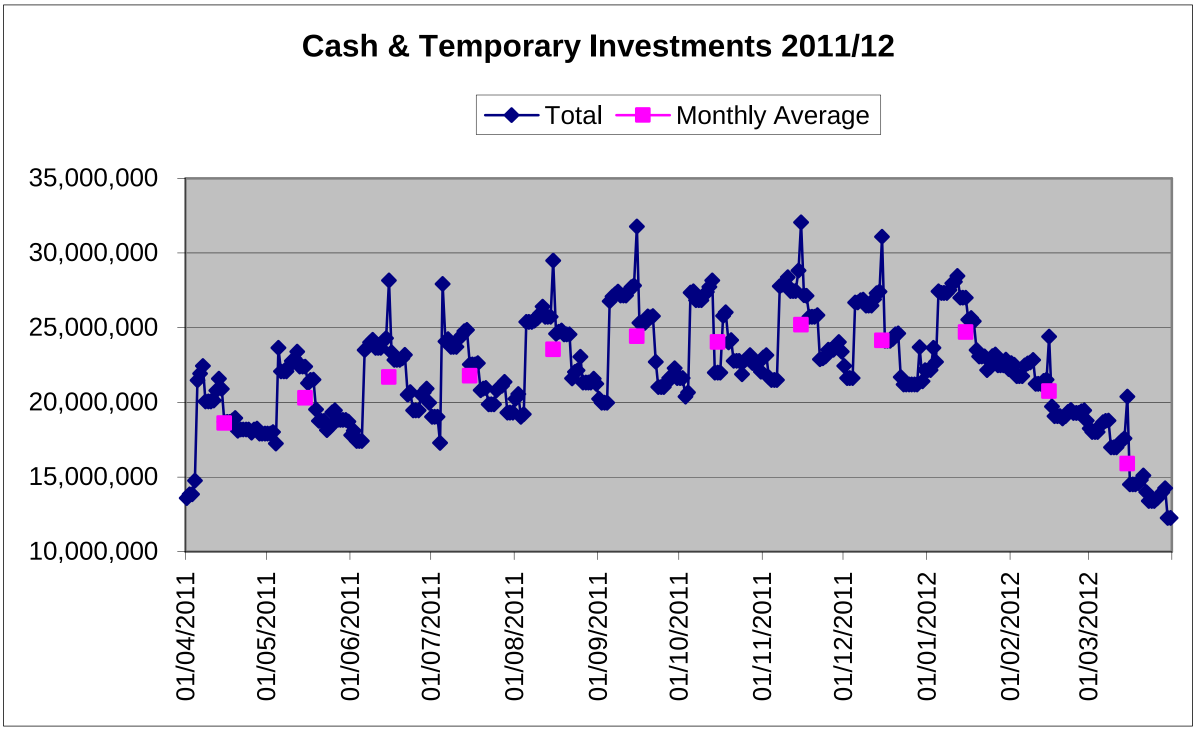
Years	PWLB	Rate
11	5,000,000	2.56
12	5,000,000	2.70
13	5,000,000	2.82
14	5,000,000	2.92
15	10,000,000	3.01
16	10,000,000	3.08
19	10,000,000	3.26
20	15,000,000	3.30
23	15,000,000	3.40
25	10,000,000	3.44
30	10,000,000	3.50
35	10,000,000	3.52
40	10,000,000	3.52
45	10,000,000	3.50
50	26,722,000	3.48
Total	156,722,000	3.30

Additionally, the Joint Environmental Services Contract with east Hampshire District Council that commenced on the 1 October 2011, included embedded finance leases of £2.6m.

The Council continued with its policy of financing capital schemes that can generate a return and used £1.3m in 2011/12, which it funded out of internal resources.

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 2011/12 are shown below:



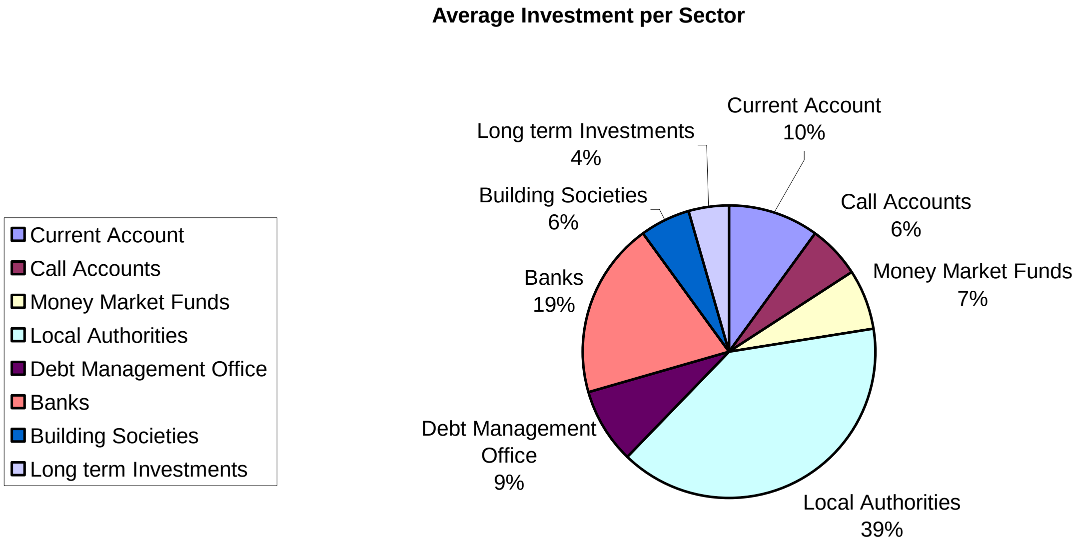
5.2 Investment activity was as follows:

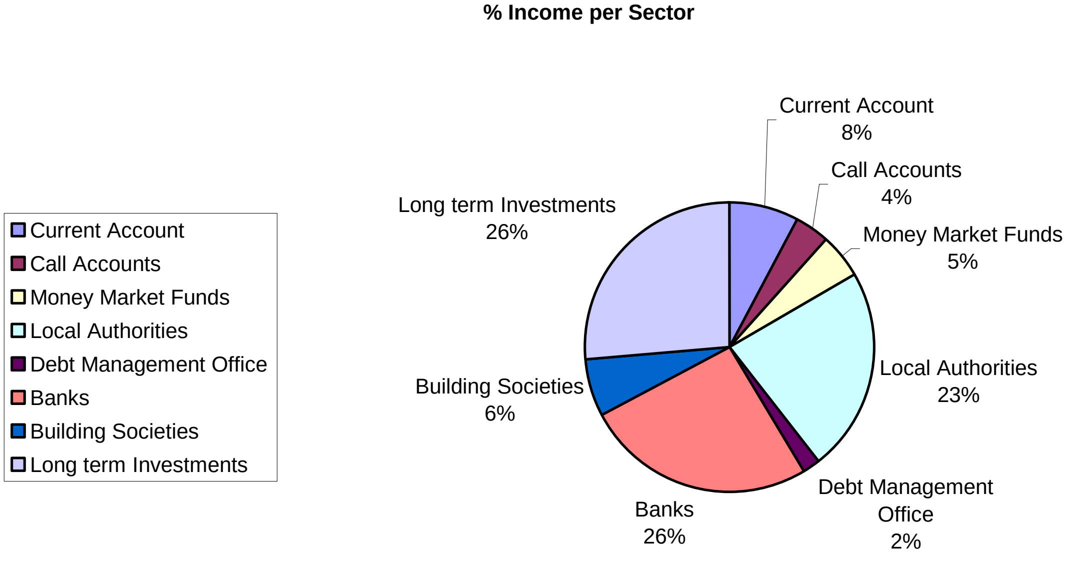
	Balance on 01/04/2011 £000s	Investments Made £000s	Investments Repaid £000s	Balance on 31/03/2012 £000's	Increase/ (decrease) in Investments £000's
Short Term Investments					
Call Accounts	3,000	22,344	25,344	0	(3,000)
Pooled Funds	0	22,150	20,400	1,750	1,750
Term Deposits					
Local Authorities	4,000	31,225	26,225	9,000	5,000
Debt Management Office	0	81,600	81,100	500	500
Banks	3,000	6,000	9,000	0	(3,000)
Building Societies	1,000	3,000	4,000	0	(1,000)
Long Term Investments	1,000	0	0	1,000	0
TOTAL INVESTMENTS	12,000	166,319	166,069	12,250	250

Other Interest Bearing	Balance on 01/04/2011 £000s	Cash Received £000s	Cash Paid £000s	Balance on 31/03/2012 £000's	Increase/ (decrease) in Balance £000's
Current Account	2,531	504,944	506,451	1,024	(1,507)
Total External Balances *	14,531	338,875	340,132	13,274	(1,257)

* Cash Received excludes investments repaid, Cash Paid excludes investments made

5.3 Analyses of average balances & interest receivable for the 12 months to 31 March 2012





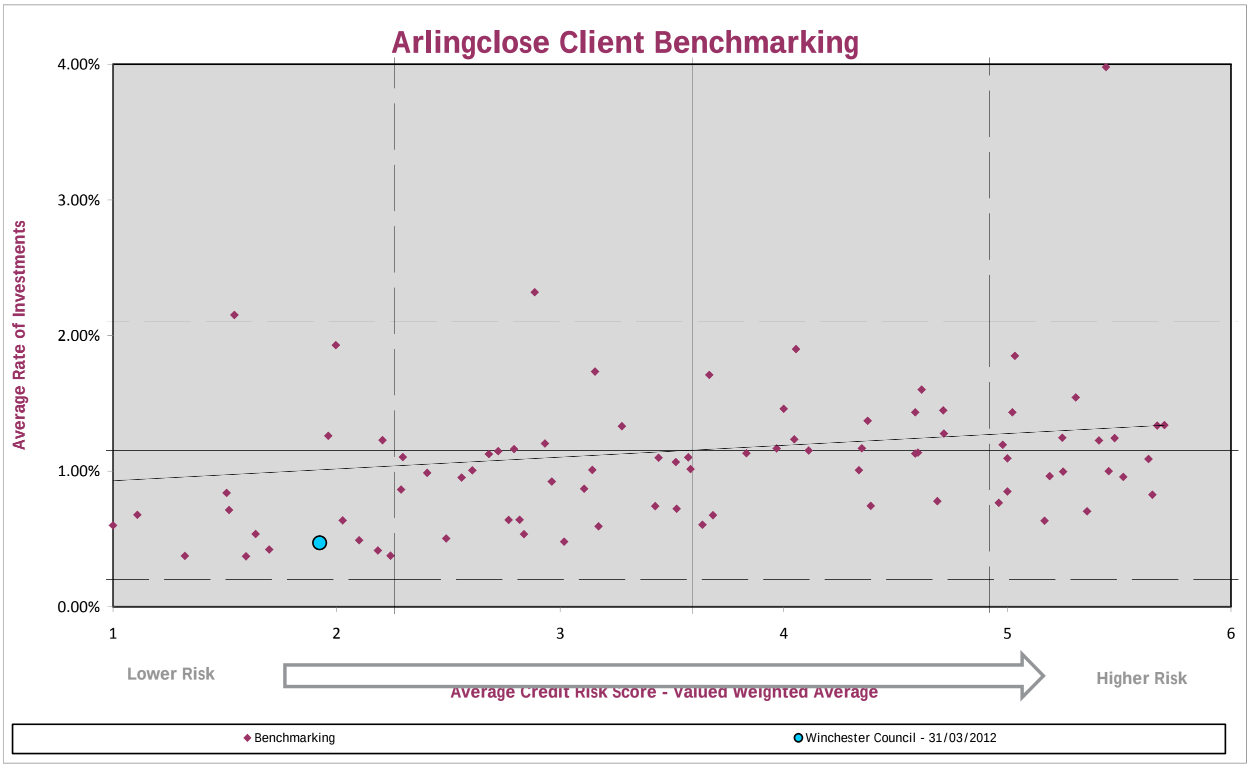
5.4 Security of capital has remained the Council's main investment objective. This has been maintained by following the Council's counterparty policy as set out in its Treasury Management Strategy Statement for 2011/12 (per CAB2117). New investments can be made with the institutions/instruments as set down on the approved counterparty list in Appendix B.

5.5 Credit Risk, Counterparty credit quality was progressively strengthened 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
31/03/2011	4.11	AA-	4.69	A+
30/06/2011	3.77	AA-	3.06	AA
30/09/2011	2.96	AA	2.81	AA
30/12/2011	3.02	AA	3.12	AA
31/03/2012	1.92	AA+	1.69	AA+

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

5.6 The Council's average credit risk score at 31 March 2011 is relatively low when compared with other Arlingclose - local authority clients



5.7 The Head of Finance can report that the investment portfolio has been managed within the counterparty limits, with the exception of one occasion on 5 July 2011 when funds received into the current account were not transferred into other investments until the following day. This resulted in £10,420,103 being held in the current account exceeding the £4,000,000 limit. The Portfolio Holder was notified and the cost implications were minimal. This was already reported in the mid year review (AUD015).

5.8 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 / current account bearing interest/ the use of call accounts.

5.9 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. The Council considered an appropriate risk management response to uncertain and deteriorating credit conditions in Europe was to shorten maturities for new investments. Short term money market rates also remained at very low levels which had a significant impact on investment income.

a) Budgeted Interest Income and performance in the year.

(i) The Council's budgeted investment income for the year was set at £150,000. The average cash balances representing the Council's reserves and working balances were £23.1m during the period.

(ii) The UK Bank Base Rate has been maintained at 0.5% since March 2009 and is not expected to rise within the next 3 years. Short-term money market rates have remained at very low levels. The Council has an investment income outturn of £239,000 / 1.03% for the whole year. This was due to larger than budgeted average balances being held by the Council as capital projects that were to be funded by internal resources slipped

6 Other Holdings

6.1 Local Authorities Mutual Investment Trust (LAMIT)

a) The Council currently holds 422,654 property fund units in LAMIT which were purchased in 1989/90 at a cost price of £1 million. The value of LAMIT has been subject to market fluctuations.

Valuation date	Value*	Gain / (Loss) on investment (unrealised)
31st March 2008	1,335,000	335,000
31st March 2009	821,000	(179,000)
31st March 2010	913,000	(87,000)
31st March 2011	962,000	(38,000)
31st March 2012	963,000	(37,000)

b) In accordance with the accounting requirements an impairment was reflected in the Annual Accounts to 31 March 2012. The effect of the improved valuation as at 31 March 2012 was a reversal of £1k of this charge to the Comprehensive Income & Expenditure Statement in 2011/12.

c) Dividends received on this investment amounted to £63,030.

7 Heritable Bank in Administration

7.1 The Council had an investment of £1m with Heritable Bank Ltd which was placed into administration in October 2008. Whilst in Administration, the Administrators will be seeking to find purchasers for, and will continue to manage, the remainder of Heritable's business and loan book to maximise recovery for creditors. At 31 March 2012 the Council had received dividends of £681,562 and a further £66,632 has been received in 2012/13 to date. The next receipt of c.3.5% is expected in January 2013. It is currently forecast that 86p-90p/£ will be recovered overall.

8 Compliance with Prudential Indicators

8.1 The Head of Finance can confirm that the Council has complied with its Prudential Indicators for 2011/12, which were approved as part of the Council's Treasury Management Strategy Statement CAB2117 and revised because of HRA Housing Finance Reform (AUD015). Details can be found in Appendix A.

8.2 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 2011/12. 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:

9 SUSTAINABLE COMMUNITY STRATEGY AND CHANGE PLANS (RELEVANCE TO):

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

10 RESOURCE IMPLICATIONS:

10.1 Investment income amounted to £239K in 2011-12 (£245k in 2010/11).

11 RISK MANAGEMENT ISSUES

11.1 These are considered within the report.

BACKGROUND DOCUMENTS:

Operational and financial records held in the Financial Services

APPENDICES:

Appendix A Prudential Indicators

Appendix B Investments at 31 March 2012

Appendix C Glossary of Terms

PRUDENTIAL INDICATORS

Capital Financing Requirement

The Council's external borrowing requirement for 2011/12 compared to budget is shown in the table below:

	31/03/2011 Actual £000s	31/03/2012 Original Estimate £000s	31/03/2012 Revised Estimate £000s	31/03/2012 Actual £000s
Capital Financing Requirement	4,154	13,900	166,300	164,508
Less: Existing Profile of Borrowing	0	0	157,400	156,722
Less: Other Long Term Liabilities	0	0	0	2,418
Cumulative Maximum External Borrowing Requirement	**4,154**	**13,900**	**8,900**	**5,368**

Balances and Reserves

The Council's level of Balances and Reserves for 2011/12 were as follows:

	31/03/2011 Actual £000s	31/03/2012 Original Estimate £000s	31/03/2012 Revised Estimate £000s	31/03/2012 Actual £000s
Balances and Reserves	18,805	10,200	13,300	19,254

Prudential Indicator Compliance

a) Authorised Limit and Operational Boundary for External Debt

* The Local Government Act 2003 requires the Council to set an Affordable Borrowing Limit, irrespective of their indebted status. This is a statutory limit which should not be breached.

* The Council's Affordable Borrowing Limit was originally set at £13.9m and revised for HRA Financing reform to £172.3m for 2011/12.

* The Operational Boundary is based on the same estimates as the Authorised Limit but reflects the most likely, prudent but not worst case scenario without the additional headroom included within the Authorised Limit.

* The Operational Boundary for 2011/12 was originally set at £8.9m and revised for HRA financing reform to £175.3m

* The Head of Finance confirms that there were no breaches to the Authorised Limit or the Operational Boundary during the year. Borrowing at its peak was £159.1m and the bank overdraft facility was not used during the year.

PRUDENTIAL INDICATORS

(b) Upper Limits for Fixed Interest Rate Exposure and Variable Interest Rate Exposure

* These indicators allow the Council to manage the extent to which it is exposed to changes in interest rates.

* The upper limit for variable rate exposure allows for the use of variable rate debt to offset exposure to changes in short-term rates on our portfolio of investments.

	Original Limits for 2011/12 £/%	**Revised Limits for 2011/12 £/%**	**Maximum during 2011/12 £/%**
Upper Limit for Fixed Rate Exposure	100%	100%	100%
Compliance with Limits:	Yes	Yes	Yes
Upper Limit for Variable Rate Exposure	100%	39%	0%
Compliance with Limits:	Yes	Yes	Yes

c) 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.

Orginal PI to 13 February 2012 Maturity Structure of Fixed Rate Borrowing	**Upper Limit** £/%	**Lower Limit** £/%	**Actual Fixed Rate Borrowing at 31 March 2012**	**% Fixed Rate Borrowing at 31 March 2012**	**Compliance with Set Limits?**
Under 12 months	100%	0	0	0	Yes
12 months and within 24 months	£5m	0	0	0	Yes
24 months and within 5 years	£5m	0	0	0	Yes
5 years and within 10 years	£5m	0	0	0	Yes
10 years and above	£5m	0	0	0	Yes

Revised PI post 13 February 2012 Maturity structure of fixed rate borrowing	**Upper Limit** **£m**	**Lower Limit** **£m**	**Actual Fixed Rate Borrowing at 31 March 2012** **£m**	**% Fixed Rate Borrowing at 31 March 2012** **%**	**Compliance with Set Limits?**
12 months and within 24 months	20.0	0.0	0.0	0.0	Yes
24 months and within 5 years	40.0	0.0	0.0	0.0	Yes
5 years and within 10 years	60.0	0.0	0.0	0.0	Yes
10 years and within 20 years	120.0	0.0	65.0	41.5	Yes
20 years and within 30 years	177.3	0.0	35.0	22.3	Yes
30 years and within 40 years	177.3	0.0	20.0	12.8	Yes
40 years and within 50 years	177.3	0.0	36.7	23.4	Yes
50 years and above	177.3	0.0	0.0	0.0	Yes

PRUDENTIAL INDICATORS

d) Actual External Debt

* This indicator is obtained directly from the Authority's balance sheet. It is the closing balance for actual gross borrowing (short and long-term) plus other deferred liabilities.

* The indicator is measured in a manner consistent for comparison with the Operational Boundary and Authorised Limit.

Actual External Debt as at 31/03/2012	**£m**
Borrowing	156.7
Other Long-term Liabilities	2.4
Total	**159.1**

e) Total principal sums invested for periods longer than 364 days

* This indicator allows the Council to manage the risk inherent in investments longer than 364 days.

* The limit for 2011/12 was set at £2m.

* Local Authorities Mutual Investment Trust (LAMIT) £1m is the only investment that the Council holds on a long term basis. No further investment of over 364 days have been made in the period to 31 March 2012

f) 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.

PRUDENTIAL INDICATORS

	2010/11 Actual £million	2011/12 Original Estimate £million	2011/12 Revised Estimate £million	2011/12 Actual £million
Capital Expenditure				
Non-HRA	5.6	14.1	9.0	6.0
HRA	4.2	6.5	161.6	161.4
Financed by:				
Non - HRA				
Government grants	0.4	0.4	0.4	0.4
External contributions	0.8	0.8	1.1	0.6
Earmarked reserves	1.1	0.4	0.8	0.4
Major Investment reserve	0.7	0.8	0.9	0.4
Capital receipts	1.0	2.1	1.2	0.3
HRA				
Major repairs allowance	3.5	3.9	4.3	3.4
Revenue Reserves	0.6	0.1	0.3	0.5
Capital Receipts	0.1	2.5	0.3	0.7
External Contributions	0.0	0.0	0.0	0.1
Capital Financing Requirement	**1.6**	**9.6**	**161.3**	**160.6**
CFR Financed by				
PWLB Loan	0.0	0.0	157.4	156.7
Embedded Lease	0.0	0.0	0.0	2.6
Internal Resources	1.6	9.6	3.9	1.3
Total	1.6	9.6	161.3	160.6

The table shows that the capital expenditure plans of the Authority could not be funded entirely from sources other than external borrowing.

g) Ratio of Financing Costs to Net Revenue Stream

* 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 financing costs.

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

Affordability Indicator	2010/11 Actual %	2011/12 Original %	2011/12 Revised %	2011/12 Actual %
Non-HRA	0.2	0.5	(1.1)	(0.0)
HRA	0.3	0.3	0.5	0.4

h) Adoption of the CIPFA Treasury Management Code

PRUDENTIAL INDICATORS

* 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)

i) Gross and Net Debt

* the purpose of this treasury indicator is to highlight a situation where the Authority has borrowed in advance of need.

Upper Limit on Net Debt compared to Gross Debt	**2010/11 Actual**	**2011/12 Original Estimate**	**2011/12 Revised Estimate**	**2011/12 Actual**
	£m	**£m**	**£m**	**£m**
Outstanding Borrowing (at nominal value)	0.0	8.9	172.3	156.7
Other Long-term Liabilities (at nominal value)	0.0	0.0	5.0	2.4
Gross Debt	0.0	8.9	177.3	159.1
Less: Investments	14.5	0.0	4.7	13.3
Net Debt	**0.0**	**8.9**	**172.6**	**145.8**
Net Debt as % of Gross Debt	N/A	100.0%	97.3%	91.6%

j) 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	**2010/11 Actual**	**2011/12 Orginal Estimate**	**2011/12 Revised Estimate**	**2011/12 Actual**
	£m	**£m**	**£m**	**£m**
	1.0	2.0	2.0	1.0

PRUDENTIAL INDICATORS

k) HRA Limit on indebtedness

HRA Limit on Indebtedness	2010/11 Actual	2011/12 Approved	2011/12 Revised	2011/12 Actual
	£m	£m	£m	£m
HRA CFR	10.1	10.1	10.1	166.9
HRA Debt Cap (as prescribed by DCLG)	N/A	N/A	N/A	166.9
Difference				0.0

Treasury Management Performance Indicators

Debt- Borrowing – Average rate of borrowing for the year compared to average available.

The Council only borrowed once on the 26 March at a weighted average rate of 3.30% for a weighted average of 28.6 years. The weighted average PWLB during the year for the same debt profile was 4.49%. The low rate achieved reflects both the fall in PWLB rates during the year and the special rate that was available as a one off to fund the HRA Housing Finance reform.

Debt – Average rate movement during the year

At normal PWLB rates the loans at the 1 April 2011 would have cost 5.27%, at the 31 March 2012 that had fallen to 4.17% a fall of 1.10%

Investments – Internal returns above base rate

Base rate was maintained at 0.50% throughout the year. The Council achieved returns of 1.03% which equals an additional £123,000 of investment income received.

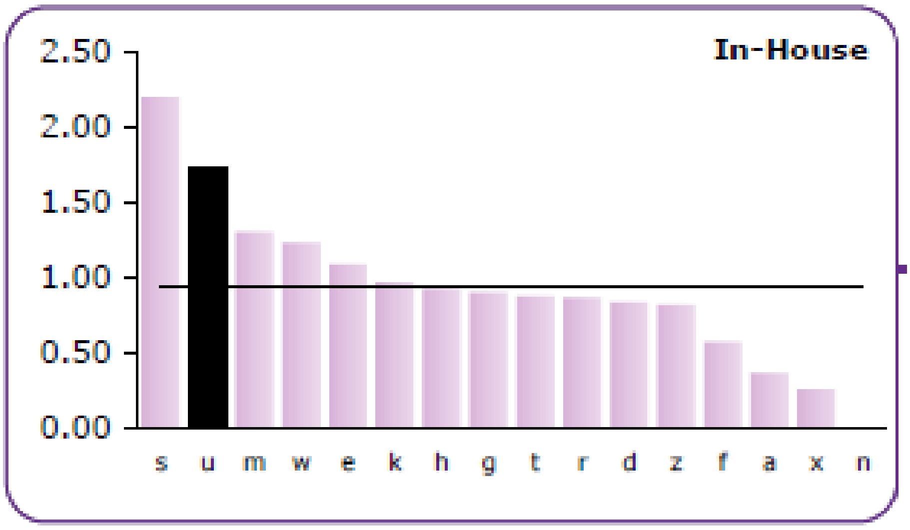
Investments- External fund managers. The Council did not use external fund managers during 2011/12.

PRUDENTIAL INDICATORS

Cost Benchmarking

The Council has benchmarked itself against 15 other district councils from CIPFA's Treasury Benchmarking Club

The table below shows the costs £'k per £'m Invested. Winchester is the black line.



This is a function of having the 4th lowest investment portfolio and being debt free for the majority of the year therefore not being able to offset the costs against debt maintenance rather than staff time / costs allocated against treasury management.

Investments & Bank as at

	31 March 2012					
Tier 1 UK Government	**£**	**Maturity Date**	**Term (days)**	**Weighted Ave Rates %**	**Approved TM Strategy Limits**	**Limit remaining**
Debt Management Office	500,000	05/04/2012	14	0.25	unlimited	0
Local Authorities: Salford City Council	2,000,000	25/05/2012	91	0.43	2,000,000	0
Local Authorities: Mid Lothian Council	2,000,000	15/06/2012	92	0.45	2,000,000	0
Local Authorities: Blaenau Gwent	2,000,000	16/04/2012	31	0.30	2,000,000	0
Local Authorities: Dumfries & Galloway Council	2,000,000	03/05/2012	34	0.35	2,000,000	0
Local Authorities: Leeds City Council	1,000,000	22/06/2012	93	0.40	2,000,000	1,000,000
AAA Money Market Funds	-					
Prime Rate MMF	1,250,000			0.83	2,000,000	750,000
CCLA Public Sector Deposit Fund	500,000			0.69	500,000	0
Total Tier 1	**11,250,000**			**0.44**		
Tier 2 UK Banks with significant Government Shareholdings						
National Westminster Bank Current Account	1,024,455			0.80	3,000,000	1,975,545
Total Tier 2	**1,024,455**			**0.80**	**9,000,000**	**7,975,545**
All Short Term Funds	**12,274,455**			**0.47**		
Long Term Investments						
Local Authorities Mutual Investment Trust	1,000,000			6.30		
Total Bank & Investments	**13,274,455**			**0.91**		

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.

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.

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*.