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DATE OF MEETING:	18 FEBRUARY 2003	CATEGORY: DELEGATED
REPORT FROM:	CHIEF FINANCE OFFICER	OPEN PARAGRAPH NO: N/A
MEMBERS' CONTACT POINT:	PAUL CULLEN (EXT 5872)	DOC: s:\cent_serv\committee reports\finance and management\18 feb 2003\treas man strategy 2003 - 4.doc
SUBJECT:	TREASURY MANAGEMENT STRATEGY	REF: PAC/JHM
WARD(S) AFFECTED:	ALL	TERMS OF REFERENCE: FM08

1.0 Recommendations

1.1 That the Council be recommended to set the following limits for 2003/2004:

Overall Borrowing Limit	£18 million
Short-Term Borrowing Limit	£8 million
Proportion of interest at Variable Rates	20%

1.2 That the Committee approve the Strategy for 2003/2004.

1.3 To approve an increase in the current limit on investments allowed with the UK Debt Management Office (DMO) from £5 million to £10 million.

2.0 Purpose of Report

2.1 Under Section 45 of the Local Government and Housing Act 1989 the full Council has to make a number of determinations relating to the Council's borrowing. In addition the Council's Treasury Management Policy requires a strategy to be approved for the coming year.

2.2 To ratify an amendment, agreed with the Chair of the Finance and Management Committee on 16 January 2003, to the List of Approved Counterparties and Limits for Investments.

3.0 Detail

3.1 Determinations

The Council has to make determinations in respect of:

- The Overall Borrowing Limit.
- The Short-Term Borrowing Limit.
- The proportion of interest payable where the interest rate is variable.

3.2 Short-Term Borrowing Limit

The current short-term borrowing limit, set for 2002/3, is £10 million.

It was estimated that 50% of the £5.8 million proceeds received from two large land sales in March 2002 would be used in 2002/3. However, only a £1 million payment into the Superannuation Fund actually took place, with the result that the Council has maintained a surplus throughout 2002/3.
Even though another £2 million is expected to be used in 2003/4, the normal level of borrowing in deficit periods will be around £1 million, with peaks unlikely to exceed £4 million during the year.

3.3 Members are therefore asked to recommend a limit on the total amount to be outstanding for short-term borrowing for next year of £8 million. This will still allow for some flexibility as the limit can only be varied by full Council.

3.4 Overall Borrowing Limit

The Council's borrowing is made up of:

- Long-term fixed rate loans from the Public Works Loan Board (PWLB).
- Other long-term loans.
- Short-term loans.

Short-term loans are defined as loans taken out for less than 12 months.

3.5 A schedule of the Council's existing long-term loans is shown at Annex A. The amount currently outstanding is approximately £9.07 million (£8.07 million from the PWLB and £1 million from other lenders) which is inline with the 2002/03 Treasury Management Strategy.

3.6 An abnormally high NNDR3 adjustment payment for 2002/3 of approximately £3.6 million is due from the Government in 2003/4, although not until at least August 2003.

3.7 However, apart from certain periods prior to receipt of this settlement, cashflow is forecast to remain in surplus during 2003/4 even after taking account of the proposed use of £2 million of land sale income and credit approvals of £546,000. As a consequence it is proposed not to borrow from the PWLB next year.

3.8 If circumstances change in the future and the Council needs to replace short term borrowing with a PWLB loan over and above a normal years quota, then there is an option available to apply for additional quota.

3.9 The normal level of overall borrowing for 2003/4 will therefore be around £9.07 million. However, at the end of the year this could rise to around £13.07 million. Members are therefore asked to recommend an Overall Borrowing Limit of £18 million, again to allow flexibility.

3.10 <u>Proportion of Variable Rate Borrowing</u>

The estimated interest payable on the Council's loans next year is as follows:

	£	%
PWLB Loans	628,033	92.0
Other Long-Term Loans	48,750	7.1
Short-Term Loans	5,876	0.9
	682,659	100.0

3.11 The interest on the Other Long-Term Loans and on Short-Term Loans is variable. Members are therefore asked to recommend 20% as the proportion of interest at variable rates, thus leaving room for some flexibility.

3.12 <u>Strategy</u>

The base rate was lowered on 6th February to 3.75%, having remained unchanged at 4% since November 2001. Whilst a cut in the rate had been thought possible, particularly if global risks worsened, it was becoming increasingly unlikely – given the concern over the housing market boom, higher Government borrowing and the rise in inflation above target.

This also appeared to be supported by the majority's view at the Bank of England's Monetary Policy Committee (MPC) meeting in December ie. that the threat of instability arising from the housing boom must be given greater weight than the global uncertainties.

However, since December the house market seems to have been stagnating. Consequently, the latest forecast is that from now onwards there will be distinct cooling signs in the housing market.

Also, the CBI's most recent surveys have shown that around 72% of firms are operating below capacity and that investment intentions are at a 15 year low, which will make workers nervous and more likely to hold back on spending.

It is therefore believed that, given the changes now beginning to happen and the many conflicting pressures that are likely to continue to face the MPC for most of this year, this will force base rates down to 3.5%. However, things should calm down in the fourth quarter which may see them edging back towards 4%.

3.13 Cash Flow Management and Investment of Surplus Funds

Based on forecasts of base rate movement, it is proposed to avoid investing surplus funds for longer than 6 months at the beginning of the year unless there is a change in outlook. The situation will then be reviewed again if and when base rates begin to rise.

Money Market Funds are a new form of investment tool now available to local authorities. Investigation of this method of short-term investment will take place during 2003/4 to determine if it would be of benefit to the Council.

However, the Council's surplus funds will continue to be invested with the minimum of risk, at the same time aiming to achieve maximum returns whilst fulfilling short-term cash flow requirements.

3.14 Short Term Borrowing

For the following 12 months period the Council will borrow short term if this becomes necessary for the purposes of cash flow (in accordance with the limit to be set by this Committee).

3.15 Long Term Borrowing

No allowance has been made during 2003/04 for long-term borrowing.
However, in line with the Finance Services Division Action Plan, it is proposed to continually review the feasibility of rescheduling long-term debt in order to reduce overall borrowing costs. The implications of carrying out such an exercise is currently being explored with the Public Works Loans Board.

3.16 <u>Amendment of The List Of Approved Counterparties And Limits For Investments.</u>

In accordance with item 11.2 of the Council's Treasury Management Policy Statement 2002/3, the Finance and Management Committee may revise the Statement in exceptional circumstances during the year, but only if necessary to avoid incurring a loss or cost to the Council.

3.17 Members may recall that the original limit, set by the Finance and Management Committee on 18 April 2002 (minute FM/114) for investments with the Debt Management Office (DMO), was £5 million. This limit was set when the Council first joined a six month pilot scheme run by the Government's Debt Management Office which commenced on 2 April 2002.
Due to the success of the scheme the facility was moved to a longer term basis in October 2002.

3.18 The consistently competitive rates offered by the DMO has resulted in an increasing amount of the Council's short-term investments being placed with them. Consequently, on occasions when a surplus of more than £5 million has been available for investment, the excess has had to be placed with another institution sometimes at a lower rate of interest.
Members are therefore asked to approve an increase in the DMO's investment limit to £10 million.

3.19 The UK Debt Management Office is guaranteed by the Government and has the equivalent of a sovereign triple-A credit rating. A higher investment limit can therefore be justified than that set for other financial institutions.

4.0 Financial Implications

4.1 As contained in the report.

5.0 <u>Background Papers</u>

5.1 Treasury Management Policy Statement 2002 / 2003.
5.2 RSM Robson Rhodes: Prospects for the UK Economy – Dec 2002.
5.3 Sterling International Brokers Ltd: Monthly Newsletter 29/1/03.