

## Appendix 2 – Treasury Management Strategy – Prudential Indicators – 2016/17

1. The Prudential Code for Capital Finance in Local Authorities provides a framework for local authority capital finance to ensure that:
  - (a) capital expenditure plans are affordable,
  - (b) all external borrowing and other long term liabilities are within prudent and sustainable levels;
  - (c) treasury management decisions are taken in accordance with professional good practice.
2. In taking decisions in relation to (a) and (c) above, the local authority is accountable by providing a clear and transparent framework.
3. The Code requires the Council to set a range of Prudential Indicators for the next financial year and at least the following two financial years. The Council has set out indicators for the next 10 financial years in line with setting a 10 year budget. The indicators include the Invest to save scheme however the costs of borrowing associated with the scheme will be offset by the income generated by these projects.
4. During 2016/17 the Council has operated within the treasury limits and Prudential Indicators set out in the Council's Annual Treasury Management Strategy.
5. The Council's outturn performance position against the 2016/17 Prudential Indicators are shown below.

### Indicator 1: Capital Expenditure

This indicator is the actual capital expenditure for the year based on the Capital Programme in 2016/17.

| Capital Expenditure | 2016/17<br>Indicator<br>£m | 2016/17<br>Actual<br>£m |
|---------------------|----------------------------|-------------------------|
| Capital Expenditure | 100.0                      | 57.7                    |
| Invest to Save      | 56.6                       | 19.1                    |
| <b>Total</b>        | <b>156.6</b>               | <b>76.8</b>             |

### Indicator 2: Capital Financing Requirement (CFR)

The CFR measures the Council's underlying need to borrow money in the long term for capital purposes. Any capital expenditure which has not immediately been paid for will increase the CFR.

| Capital Financing Requirement              | 2016/17<br>Indicator<br>£m | 2016/17<br>Actual<br>£m |
|--|----------------------------|-------------------------|
| CFR b/fwd                                  | 546.0                      | 480.9                   |
| Underlying Need to Borrow                  | 52.3                       | 9.8                     |
| Underlying Need to Borrow - Invest to Save | 60.0                       | 19.1                    |
| <b>Total CFR C/fwd</b>                     | <b>658.3</b>               | <b>509.8</b>            |

### Indicator 3: Actuals and estimates of the ratio of financing costs to net revenue budget

The Council must estimate the proportion of the revenue budget, which is taken up in financing capital expenditure i.e. the net interest cost and to make provision to repay debt.

| <b>Ratio of net financing costs to net revenue stream</b> | <b>2016/17 Indicator</b> | <b>2016/17 Actual</b> |
|---|--------------------------|-----------------------|
| Total Ratio   | 6.1%                     | 6.1%                  |

The difference between the Indicator and final ratio percentage is largely the result of the revised Minimum Revenue Provision (MRP) policy that was approved by Council as part of the 2016/17 Medium Term Financial Strategy (MTFS) process where debt repayment was rephased.

#### **Indicator 4: Actuals and estimates of the incremental impact of capital investment on Council Tax**

This indicator is intended to show the impact of the Council's decisions about capital investment on the level of Council Tax required to support those decisions over the medium term.

The calculation of this indicator has been done on the basis of the amount of the capital programme that is financed from borrowing and the interest assumption for borrowing that was included in the capital financing budget for the MTFS. The revenue costs are divided by the estimated Council Tax base for the year, and the actual performance is shown in the table below.

| <b>Incremental impact on capital investment decisions on Council Tax</b> | <b>2016/17 Indicator<br/>£m</b> | <b>2016/17 Actual<br/>£m</b> |
|--|---------------------------------|------------------------------|
| A – Cap Fin Budget -Previous MTFS  | 28,889                          | 28,889                       |
| B – Cap Fin Budget - Current   | 18,193                          | 17,551                       |
| C - Incremental change (B-A)   | (10,695)                        | (11,338)                     |
| D - Council Tax Base (1,000's)   | 54.10                           | 54.10                        |
| <b>Total Incremental Impact (C/D)</b>                                    | <b>(197.70)</b>                 | <b>(209.75)</b>              |

The incremental change of £15.5m shown in the table is largely the result of the 2016/17 MTFS where the Council agreed to revise the 2015/16 MRP policy.

#### **Indicator 5: Proportion of Gross Debt to the CFR**

This indicator shows the proportion of the Council's external borrowings (Gross Debt) against the CFR.

| <b>Proportion of Gross Debt to the CFR</b> | <b>2016/17 Indicator<br/>£m</b> | <b>2016/17 Actual<br/>£m</b> |
|--|---------------------------------|------------------------------|
| CFR  | 658.4                           | 509.8                        |
| Gross Debt                                 | 584.1                           | 430.9                        |
| <b>% of Gross Debt to CFR</b>              | <b>88.7%</b>                    | <b>84.5%</b>                 |

#### **Indicator 6: The Operational Boundary**

The Operational Boundary is a measure of the day to day likely borrowing for the Council. The code recognises that circumstances might arise when the boundary might be exceeded temporarily, but if this continues for a lengthy period then it ought to be investigated.

This indicator takes into consideration the capital programme over the life of the MTFS and the ability to phase the borrowing over this period. The indicator provides flexibility for the Council to take advantage of favourable interest rates in advance of the timing of the actual capital expenditure.

| <b>Operational Boundary</b> | <b>2016/17 Indicator</b> | <b>2016/17 Actual</b> |
|-----------------------------|--------------------------|-----------------------|
|-----------------------------|--------------------------|-----------------------|

|                                   | £m           | £m           |
|-----------------------------------|--------------|--------------|
| Borrowing                         | 690.9        | 395.3        |
| Other Long Term Liabilities       | 38.6         | 35.6         |
| <b>Total Operational Boundary</b> | <b>729.5</b> | <b>430.9</b> |

### Indicator 7: The Authorised Limit

The Authorised Limit represents the maximum amount the Council may borrow at any point in time in the year. It is set at a level the Council considers is “prudent”.

The indicator takes account of the capital financing requirement estimated at the start of each year, plus the expected net borrowing requirement for the year. This makes allowance for the possibility that the optimum time to do all borrowing may be early in the year.

The limits also incorporated margins to allow for exceptional short-term movements in the Council’s cash flow, bids from service departments to finance efficiencies, changes to the timing of capital payments and fluctuations in the realisation of capital receipts.

| <b>Authorised Limit</b>       | <b>2016/17<br/>Indicator<br/>£m</b> | <b>2016/17<br/>Actual<br/>£m</b> |
|-------------------------------|-------------------------------------|----------------------------------|
| Borrowing                     | 796.6                               | 395.3                            |
| Other Long Term Liabilities   | 38.6                                | 35.6                             |
| <b>Total Authorised Limit</b> | <b>835.2</b>                        | <b>430.9</b>                     |

It is ultra vires to exceed the Authorised Limit so this should be set to avoid circumstances in which the Council would need to borrow more money than this limit. However, the Council can revise the limit during the course of the year. The actual outturn is lower than the indicator as the Council did not need to borrow in advance of need during 2015/16.

### Indicator 8: Fixed Interest rate exposure

This indicator places an upper limit on the total amount of net borrowing which is at fixed rates secured against future interest rate movements. The upper limit allows flexibility in applying a proportion of the investment portfolio to finance new capital expenditure. It also reflects a position where the majority of borrowing is at fixed rate which provides budget certainty with 100% of borrowing being at fixed rate. The upper limit for fixed interest rate exposure was set to allow for flexibility in applying a proportion of the investment portfolio to finance new capital expenditure. It also reflected a position where the majority of borrowing was at fixed rates to provide budget certainty.

| <b>Upper limit for fixed rate exposure</b> | <b>2016/17<br/>Indicator<br/>£m</b> | <b>2016/17<br/>Actual<br/>£m</b> |
|--|-------------------------------------|----------------------------------|
| Upper Limit - Borrowing                    | 796.6                               | 430.9                            |
| % of fixed interest rate exposure          | 100%                                | 100%                             |

**Indicator 9: Variable interest rate exposure**

This indicator places an upper limit on the total amount of net borrowing (borrowing less investment) which is at variable rates subject to interest rate movements. The intention is to keep the variable rate borrowing below 25% of the total gross borrowing (CFR).

The limit is expressed as the value of total borrowing less investments

| <b>Upper limit for variable rate exposure</b> | <b>2016/17<br/>Indicator<br/>£m</b> | <b>2016/17<br/>Actual<br/>£m</b> |
|---|-------------------------------------|----------------------------------|
| Upper Limit                                   | 199.2                               | -                                |
| % of variable interest rate exposure          | 25%                                 | 25%                              |

The indicator for actual outturn is zero due to the current borrowing strategy of borrowing only at a fixed interest rate in the current economic climate of volatile interest rates and also provides budget certainty for the Council.

**Indicator 10: Maturity structure of borrowing**

The prudential limits have been set with regard to the maturity structure of the Council's borrowing, and reflects the beneficial long term rates that are available to the Council.

| <b>Period</b>                   | <b>Upper Limit<br/>Indicator</b> | <b>Actual<br/>Borrowing</b> | <b>Actual<br/>Borrowing<br/>£m</b> |
|---------------------------------|----------------------------------|-----------------------------|------------------------------------|
| Under 12 months*                | 40%                              | 4.8%                        | 18.8                               |
| 1 – 2 years                     | 40%                              | 2.2%                        | 8.9                                |
| 2 – 5 years                     | 80%                              | 6.3%                        | 25.0                               |
| 5 – 10 years                    | 80%                              | 4.1%                        | 16.1                               |
| Over 10 years                   | 100%                             | 82.6%                       | 326.4                              |
| <b>Total 'Market' Borrowing</b> |                                  |                             | <b>395.3</b>                       |

\* The borrowing for under 12 months includes £17.5m of Lenders Option Borrowers Option (LOBO) loans. Although the loans are due to mature in 30-40 years' time, they are classified as loans repayable within the financial year due to LOBO's having a call-in date every 6 months.

Although this table is not a Prudential Indicator it gives a breakdown of the types of borrowing held by the Council and the average interest rates for each:

| <b>Borrowing</b>                   | <b>31 March 2016</b> |                                      | <b>31 March 2017</b> |                                      |
|------------------------------------|----------------------|--------------------------------------|----------------------|--------------------------------------|
|                                    | <b>Amount<br/>£m</b> | <b>Average<br/>Interest<br/>Rate</b> | <b>Amount<br/>£m</b> | <b>Average<br/>Interest<br/>Rate</b> |
| <b>Long Term:</b>                  |                      |                                      |                      |                                      |
| Public Works Loan Board            | 282.4                | 3.90%                                | 329.5                | 3.68%                                |
| Market Loans                       | 17.5                 | 4.53%                                | 17.5                 | 4.53%                                |
| <b>Short Term:</b>                 |                      |                                      |                      |                                      |
| Local Authorities                  | 59.5                 | 1.44%                                | 44.5                 | 1.63%                                |
| <b>Other Borrowing:</b>            |                      |                                      |                      |                                      |
| Local Enterprise Partnership       | 3.8                  | 0.00%                                | 3.8                  | 0.00%                                |
| <b>Total 'Market' Borrowing</b>    | <b>363.2</b>         |                                      | <b>395.3</b>         |                                      |
| Public Finance Initiative & Leases | 38.9                 |                                      | 35.6                 |                                      |
| <b>Total Borrowing</b>             | <b>402.1</b>         |                                      | <b>430.9</b>         |                                      |

**Indicator 11: Total Investments for periods longer than 364 days**

Authorities are able to invest for longer than 364 days; this can be advantageous if higher rates are available. However it would be unwise to lend a disproportionate amount of cash for too long a period particularly as the Council must maintain sufficient working capital for its operational needs.

| <b>Interest Rate Exposure (Upper Limits)</b> | <b>2016/17<br/>Indicator<br/>£m</b> | <b>2016/17<br/>Actual<br/>£m</b> |
|--|-------------------------------------|----------------------------------|
| Principal sums invested >364 days            | 10.0                                | -                                |

This indicator reflects the Council's current lending policy of keeping investments short term for liquidity purposes. Also the Council has run down its cash balances over the last three financial years as an alternative to new borrowing and does not have the available cash balances to invest for long periods.

The indicator was set at £6m to allow for the accounting treatment of the Local Authority Mortgage Scheme (LAMS). At present the Council has £2m deposited in the LAMS scheme with Lloyds TSB and this is treated as capital expenditure, as a loan to a third party, (see section 3.5 of the TMS). There is currently no plan to extend this initiative. The Council's external auditors highlighted in a previous Statement of Accounts report that there was some debate about the accounting treatment for LAMS. Whilst the Council is confident of its accounting treatment as a capital loan, if the accounting treatment changed for this deposit for to be classed as an investment then this indicator would cover this investment.

This page is intentionally left blank