COMMITTEE:	**CABINET**	
DATE:	**13th FEBRUARY 2003**	
SUBJECT:	**BORROWING LIMIT AND TREASURY MANAGEMENT STRATEGY FOR 2003-2004**	
REPORT OF:	**DIRECTOR OF FINANCE AND CORPORATE SERVICES**	
Ward(s):	All	
Purpose:	To determine the Council's borrowing limit for 2003-2004. To adopt a treasury management strategy for 2003-2004.	
Contact:	Sue McHugh, Telephone 01323 415104 or Bruce Bird, Telephone 01323 415146.	
Recommendations:	Cabinet is recommended that for 2003-2004:	
	1. an overall Borrowing Limit of £39 million is determined;	
	2. the short term borrowing limit is set at 15% of the overall Borrowing Limit;	
	3. the proportion of the total amount of interest payable by the Council which may be at variable rates is up to 25%;	

		4. the treasury management strategy as set out in Paragraph 3 is adopted.	
1.0	**Introduction**		
1.1	The Local Government and Housing Act 1989 requires that before the beginning of each financial year a local authority must determine:		
	a) an overall borrowing limit.		
	a) a short term borrowing limit which, within the overall borrowing limit, is the maximum amount which may be outstanding by way of short term borrowing; and		
	c) a limit on the proportion of the total amount of interest payable by the authority which is at a rate or rates which can be varied by the lender or by references to external factors.		
	The determination may be varied at any time by the Council.		
1.2.	In addition to the determinations required by statute, the CIPFA Code of Practice on Treasury Management in the Public Services, which the Council adopted at its meeting on 27th February 2002, requires the setting of an annual strategy for treasury management.		
2.0	**Borrowing Limit**		
2.1	The borrowing limit needs to be set at a level to cover the sum of the following - the existing loan debt outstanding, capital expenditure financed by credit approvals, capital expenditure incurred while awaiting receipt of grants and contributions, and revenue expenditure incurred before the collection of income due.		

2.2.	For 2003-2004 it is estimated that the borrowing limit should be determined as:-			
		2003-2004		**2002-2003**
		£ million		**£ million**
	Credit Ceiling (net capital indebtedness) at 1st April	33	36	
	New advances during year (credit approvals used)	2	1	
	Normal loan repayments and set aside capital receipts	(4)	(3)	
	Total Credit Ceiling	31	34	
	Temporary Capital Borrowing Limit (pending receipt of capital grants and contributions)	-	-	
	Temporary Revenue Borrowing Limit (pending collection of income due)	2	2	
	Approved Investments and cash less usable capital receipts	6		6
	Total Borrowing Limit	**39**	42	

	2002 -2003 figures are shown for comparative purposes.

2.3.	Existing long term borrowing currently totals £35 million, equivalent to 90% of the overall borrowing limit, all of which is fixed. The remaining £4 million (10%) is, therefore, the maximum short term borrowing that would be permitted within an overall borrowing limit of £39 million for 2003-2004.	
	However, to continue to give our current portfolio of loans the flexibility which may be needed to achieve debt restructuring savings in the present (and forecast) interest rate environment, the officers recommend that the short term borrowing limit for 2003-2004 be set at 15%. This is at the same level as approved by Cabinet for the current financial year, and will allow the officers to act decisively, following consultation with Butlers our treasury advisors, if and when market conditions exist to deliver beneficial savings to the Council through further debt restructuring opportunities. Members may be assured that, as now, any restructuring will only be carried out where it accords with the Council's approved treasury management policy statement.	
2.4	Cabinet approved a maximum limit of 25% for interest payable at variable rates on 6th February 2002 and it is recommended that this be continued for 2003-2004 to retain the necessary flexibility for our portfolio.	
3.0.	**Treasury Management Strategy for 2003-2004**	
3.1.	**Underlying Strategy**	
	The main feature of the Council's Treasury Management Strategy since 1999-2000 has been to use set aside receipts for debt repayment wherever possible, rather than for investment.	
	This is in order to align our borrowing more closely with the Housing Revenue Account (HRA) element of our Credit Ceiling. The term “Credit Ceiling” refers to the total long-term capital indebtedness of the Council.	
	The interest paid on the HRA element of the Credit Ceiling is reimbursed through the Housing Subsidy mechanism. Interest on any debt above that level is borne by the General Fund.	

	Therefore the General Fund bears a lower proportion of the interest charge if the total debt outstanding is closely aligned to the HRA Credit Ceiling.
	It is proposed to continue this policy in 2003-2004, as far as market conditions allow.
3.2.	**Interest Rates**
	The Treasury Management Strategy for 2003-2004 will be determined by movements in both short and long-term interest rates.
	Short-Term Rates
	The repo (base) rate is currently 4% and has not been varied by the Bank of England since it fell to this level in November 2001. Market consensus remains that this is probably at or near the bottom of the interest rate cycle, with perhaps a further short-term reduction of 0.25% if there is one at all. Other than this forecasters are predicting base rate remaining at or near to 4% for the whole of calendar year 2003, with perhaps a modest rise to 4.25% by the end of March 2004. **Longer Term Rates**
	Long term interest rates are likely to reflect market concerns about the effect that deterioration in public sector finances will have on the demand for and supply of gilt-edged stock. Forecasters suggest that this will come about because of the combination of Government's ambitious spending plans, as announced in the comprehensive spending review, coupled with the effect that slower economic growth will have on public expenditure and revenues. The outcome may well be increased borrowing by Government - that is, an increase beyond what it already plans to borrow - leading to long term interest rate rises.
	By way of example, the twenty year gilt yield is currently around 4.75% but is forecast to rise to 5.4% by March 2004.
	As a consequence of this, interest rates offered by the Public Works Loans Board are likely to increase across all maturity spreads during the course of 2003-2004.
3.3.	**Borrowing**

	Total borrowing at 1st April 2003 will be £35.3million. This exceeds our forecast credit ceiling at 31st March 2004 of £31 million. It is unlikely that we will be able to easily reduce our outstanding borrowing because the low level of interest rates compared with our existing debt portfolio make the premia for early repayment prohibitive.
	Our PWLB Quota for 2003-2004 is expected to be £2 million, being £1.8 million of Credit Approvals and £0.2 million of maturing loans. We will not be taking any new loans to finance our capital strategy because our debt outstanding already exceeds our Credit Ceiling. Rather we will continue our policy of financing credit approvals from set aside capital receipts.
	New loans will only be taken as part of a debt restructuring programme, if and when opportunities arise. This may be possible in 2003-2004 as long term rates start to rise. However, such a decision will only be taken as part of the Council's approved treasury management policy statement, and where it is demonstrably in the long term interests of the Council.
	We will continue to consult with Butlers, our Treasury Advisors, on any early repayments or new borrowing which beneficially re-profile our debt portfolio.
3.4.	**Investments**
	Investments will be kept short in the expectation of an increase in rates. Following a reduction in the current financial year when we used £3,500,000 of set aside receipts to repay a high coupon fixed rate loan - approved by Cabinet on 5th September 2002 - our core level of investment is likely to grow during 2003-2004 as we set aside further capital receipts. This will only change if we are able to utilise set aside receipts to repay debt.
	Other than our core funds, all other investments will be largely governed by the management of the Council's working capital and the consequent cash flow requirements.
3.5	**Monitoring**
	The Director of Finance and Corporate Services, assisted by her staff and our treasury management advisors Butlers, will monitor the interest rate market and adopt a pragmatic approach to changing circumstances. Any decisions taken and implemented under delegated powers will be reported through the monthly Finance Briefing in the Members Newsletter, and through the bi-monthly budget monitoring report to Cabinet.

4.0.	**Treasury Management Budget**	
4.1	**Borrowing**	
	Borrowing costs for 2003-2004 are estimated as:	
	Source	£'000
	Public Works Loans Board (PWLB)	2,169
	Stock	659
	Temporary Loans	1
	Bank Overdraft	1
		2,830
	The estimate is based on a no change basis to our current portfolio at an average rate for 2002-2003 of 8.03%. Given that all of the PWLB loans and the Stock Issue carry interest at fixed rates, the only change of substance would come from a debt restructuring exercise.	
4.2	**Investments**	
	Investment returns for 2003-2004 are estimated as:	
	Source	£'000
	Set-aside capital receipts	176
	Revenue cash	179
	Other investments	45

			400
	Investments are estimated to return an average of 3.95% for 2003-2004.		

4.3	**Management expenses**	
	Management expenses for 2003-2004 are estimated as:	
	Source	£'000
	In-house staff and systems	45
	External advice, consultancy and training	12
	Other expenses	3
		60
	Management expenses are estimated to represent less than 2% of the value of all treasury management revenue transactions for 2003-2004.	
4.4	**Financing the budget**	
	The budget for treasury management is shared between the General Fund and the Housing Revenue Account.	
	Borrowing costs are shared on the basis of the Housing Revenue Account element being directly proportionate to its credit ceiling, and the General Fund being charged with the balance.	

	Investment income falls substantially to the General Fund. The Housing Revenue Account does however benefit from interest on its working balance and on the balance of any unspent Major Repairs Allowance.
	Management expenses are shared in proportion to borrowing costs.
	The figures detailed within paragraphs 4.1, 4.2 and 4.3 above have been factored into the General Fund and Housing Revenue Account budgets as set out in the separate 2003-2004 budget report elsewhere on today's agenda.
5.0	**Consultations**
5.1.	The report has been discussed with Butlers, our treasury advisors.
6.0	**Implications**
6.1.	These have been included within the report where appropriate.

Sue McHugh

Director of Finance and Corporate Services

Background Papers:

The Background Papers used in compiling this report were as follows:

Local Government and Housing Act 1989.

CIPFA Code of Practice 2001 – Treasury Management in the Public Services.

To inspect or obtain copies of background papers please refer to the contact officers listed above.

Ref: openlinkCFOreports/cabinet/Cabinet 13/2/03 BorrowingLimitTreasury statement