

Cabinet - 5 December 2013

## Report of the County Treasurer

Electoral Division affected: All
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### Treasury Management Indicators for Interest Rate Exposure (Appendix A refers)

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#### Executive Summary

The CIPFA Treasury Management Code of Practice obliges local authorities to set, monitor and report on several treasury management indicators, including the setting of upper limits on the level of exposure to both fixed and variable interest rates. This is an important tool in managing the financial affairs of the County Council as it is intended to limit the risks the Council is exposed to through by short term borrowing and long-term investments i.e. the risk that changes in interest rates will create an unexpected or unbudgeted burden on the Council's finances.

This report sets out the issues regarding the current indicator, and proposes changes which will enable the indicator to support the County Treasurer in her assessment of the County Council's financial health (including exposure to financial risk) and enable a greater level of assurance to be provided to Cabinet in relation to treasury management activity.

Following advice received from the County Council's treasury management advisers, Arlingclose Ltd, on the way that the Council's bond portfolio should be reflected in the calculation of the indicator, in relation to the Council's exposure to fixed and variable interest rates, the indicator is no longer fit for purpose.

There are a number of options available, but Arlingclose Ltd recommends the use of an indicator which sets an upper limit on interest rate exposure based on the net interest payable by the County Council – which takes into account interest received on investments and paid on borrowing. The indicator would provide assurance on the Council's Treasury Management activities as it will allow more short-term borrowing while interest rates are low, but force the Council to move progressively to borrowing at fixed rates as rates rise, which is in underlying principle behind the Council's approach to treasury management.

## **Recommendation**

That Cabinet recommends to Full Council that the Treasury Management Strategy be amended to:

- (i) Adopt the 'amount of net interest payable' indicator, option C set out at Appendix 'A', in replacement of the current indicator;
- (ii) In line with Arlingclose's advice, an upper limit of £5m net interest should be set for variable rate exposure and a limit of £37.6m net interest set for the fixed rate indicator;
- (iii) Incorporate the local indicator 'impact of an immediate interest rate rise of 1%' with a maximum limit of £25m.

## **Background and Advice**

Treasury management is the management of the County Council's investments and cash flows, its banking, money market and capital market transactions; it also includes the effective control and management of the risks associated with these activities, ensuring that the Council gets the best performance for the least risk.

The Treasury Management Strategy sets out the Council's policies for ensuring the security and liquidity of its investments, whilst having regard to investment returns in order to protect the value of the funds. It also outlines the Council's strategy for financing existing borrowing and future capital borrowing requirements, with the aim of securing the required funds at the lowest possible rate.

The strategy also includes a set of indicators known as Treasury Management Indicators which set boundaries on treasury management activities for risk management purposes. This report recommends a change to the fixed and variable interest rate indicators, with detailed information set out in Appendix A to this report.

## **Consultations**

Arlingclose Ltd. Treasury Management Consultants

## **Implications:**

This item has the following implications, as indicated:

## **Risk management**

Legal

The County Council must adhere to the "Prudential Code for Treasury Management in Local Authorities".

## Financial

The Treasury Management Indicators ensure the County Council operates within the agreed Treasury Management Strategy. The objective of the Treasury Management Strategy is to ensure the security and liquidity of the County Council's debt and investment portfolios, and to improve investment returns and reduce borrowing costs while reducing the financial risks to which the Council is exposed. The forecast impact of these strategic decisions is reflected in the Medium Term Financial Strategy.

### List of Background Papers

Paper	Date	Contact/Directorate/Tel
Treasury Management Strategy 2013/14	February 2013	Andy Ormerod, County Treasurer's Directorate, (01772) 534740

Reason for inclusion in Part II, if appropriate

N/A