Agenda Item No: **7**

Wolverhampton City Council

# Cabinet (Resources) Panel

9 December 2014

| | |
|---|---|
| **Report title** | Treasury Management Activity Monitoring - Mid Year Review 2014/15 |
| **Decision designation** | RED |
| **Cabinet member with lead responsibility** | Councillor Andrew Johnson<br>Resources |
| **Key decision** | Yes |
| **In forward plan** | Yes |
| **Wards affected** | All |
| **Accountable director** | Keith Ireland, Managing Director<br>Sarah Norman, Community<br>Tim Johnson, Education and Enterprise |
| **Originating service** | Strategic Finance |
| **Accountable employee(s)** | Mark Taylor — Assistant Director Finance<br>Tel — 01902 556609<br>Email — Mark.Taylor@wolverhampton.gov.uk |
| **Report to be/has been considered by** | Strategic Executive Board — 6 November 2014 |

**Recommendations for approval:**

That Cabinet (Resources) Panel recommends to Council:

1. That it approves:

    (a) The revised upper limits for treasury management indicator (TMI) 2 - upper and lower limits to the maturity structure of its borrowing (paragraph 3.4).

    (b) The revised Annual Minimum Revenue Provision (MRP) Statement for 2014/15, the new method of calculating MRP being on an annuity basis set out in appendix G.

2. That it notes the contents of the report, and particularly that:

   (a) A mid-year review of the Treasury Management Strategy Statement has been undertaken and the Council has operated within the limits and requirements approved in March 2014 except for temporarily exceeding TMI 2 - upper and lower limits to the maturity structure of its borrowing until revised limits are approved by Council (recommendation one of this report) in order to generate savings by taking advantage of exceptionally low short term interest rates.

   (b) Savings of £4.4 million for the General Fund and £6.0 million for the Housing Revenue Account are forecast from treasury management activities in 2014/15.

   (c) Some of the credit ratings currently used in the Council's Annual Investment Strategy approved by Council in March 2014 will need to be amended in light of regulatory changes in the financial sector.

## 1.0 Purpose

1.1 This report provides a monitoring and progress report on Treasury Management Activity for the second quarter of 2014/15 as part of the mid-year review, in line with the Prudential Indicators approved by Council in March 2014.

## 2.0 Background

2.1 The treasury management activities of the Council are underpinned by The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management 2011. The primary requirements of the Code are the:

- Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the council's treasury management activities.

- Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.

- Receipt by Cabinet / Council of an annual strategy report for the year ahead, a mid-year review report and an annual review report of the previous year.

- Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

- Nomination of the Confident, Capable Council Scrutiny Panel to be responsible for ensuring effective scrutiny of the treasury management strategy and policies.

2.2 Treasury management in this context is defined as:

"The management of the local authority's 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."

2.3 The system of controls on local authority capital investment has been in place since 1 April 2004. This replaced the previous complex regulatory framework governing local authority capital expenditure. The current system is one based largely on self-regulation by local authorities themselves. At its heart is CIPFA's Prudential Code for Capital Finance.

2.4 Cabinet (Resources) Panel receives quarterly reports throughout the year to monitor performance against the strategy and Prudential Indicators that have previously been approved by Council.

2.5 The Council continues to use Capita Asset Services, previously known as Sector Treasury Services Limited, as its treasury management advisors throughout 2014/15. Capita provides market data and intelligence on which the Council can make decisions regarding all aspects of treasury management activities and in particular, managing the risks associated with investing surplus cash. This service contract expires 31 December 2014 and is therefore undergoing a re-tendering exercise.

## 3.0 2014/15 Forecast Outturn

3.1 The forecast outturn for treasury management activities in 2014/15 compared to budget is shown in Table 1 below.

**Table 1 – Treasury Management Budget and Forecast Outturn 2014/15**

| | Approved Budget £000 | Forecast Outturn £000 | Variance £000 |
|---|---|---|---|
| General Fund | 23,480 | 19,080 | (4,400) |
| Housing Revenue Account | 16,975 | 10,953 | (6,022) |
| Total | 40,455 | 30,033 | (10,422) |

3.2 At its meeting of 16 July 2014, Council approved a reduction in the treasury management General Fund budget of £1.0 million; this has been reflected in Table 1. Overall savings of £4.4 million for the General Fund and £6.0 million for the HRA are projected for the year 2014/15. The Council's strategy is to continue to use cash balances to finance capital expenditure rather than external borrowing. Borrowings are actively managed to achieve savings wherever possible. The General Fund forecast is based on the revised MRP policy attached in Appendix G which was included in the Medium Term Financial Strategy as approved by Cabinet on 22 October 2014 and for which approval is sought in paragraph 4.9 of this report.

3.3 Appendix A shows a comparison of the latest estimates of Prudential and Treasury Management Indicators over the medium term period with the equivalent figures which were approved by Council in March 2014.

3.4 It has been identified that the Council's current approved maturity structure of fixed rate debt (TMI 2 - upper and lower limits to the maturity structure of its borrowing) unduly restricts the ability to take advantage of available interest rate savings in comparison with other local authorities. By increasing the approved upper limits the Council would be able to take advantage of lower interest rates for borrowing over a shorter term. Borrowing rates for 25 years are in the region of 4% whereas rates for 1 to 3 years are between 0.8% and 2%. To generate savings, TMI 2 has been temporarily exceeded until the revised rates are approved by Council. Table 2 identifies the current approved upper limit and the new proposed levels. The proposed increased upper limits are still assessed as prudent by the Section 151 Officer.

**Table 2 – Upper Limits to the Maturity Structure of Fixed Rate Debt**

| | Approved Upper Limit | Proposed Upper Limit |
|---|---|---|
| Under 12 months | 10% | 25% |
| 12 months and within 24 months | 15% | 25% |
| 24 months and within 5 years | 20% | 40% |
| 5 years and within 10 years | 20% | 50% |
| 10 years and above | 90% | 90% |

## 4.0 Borrowing Forecast for 2014/15

4.1 The Council's need to borrow and the rates available continue to be monitored in order to achieve optimum results. The Council's medium term forecast is regularly updated to reflect actual borrowing that takes place along with any revisions to future anticipated borrowing.

4.2 Table 3 shows the average rate of interest payable in 2013/14 and forecast for 2014/15.

**Table 3 - Average Interest Rate Payable in 2013/14 and 2014/15**

| | 2013/14 Actual | 2014/15 Forecast |
|---|---|---|
| Average Interest Rate Payable | 3.97% | 3.74% |

4.3 The average rate of interest payable by the Council is estimated to fall from 3.97% to 3.74% for 2014/15.

4.4 Each year it is necessary to raise new loans to finance capital expenditure and to replace existing maturing debt. The Council's policy is to prioritise the use of capital receipts to finance capital expenditure. Balances which are set aside to meet credit liabilities (i.e. to repay debt) are used to reduce the external borrowing requirement. Decisions to take borrowing will be made by the Assistant Director Finance when it is judged that rates are likely to be at their lowest levels, and probably about to rise according to market indications, and only when an inflow of funds is required to meet imminent cash flow commitments. This will keep overall surplus cash balances to a minimum, in line with the current strategy. Appendix B shows the maturity profile of external borrowing.

4.5 Any short term savings made by avoiding new long term external borrowing in 2014/15 and thereafter, will also need to be weighed against the potential for incurring additional long term extra costs by delaying unavoidable new external borrowing until later years, when Public Works Loan Board (PWLB) long term rates are forecast to be significantly higher. Appendix C includes the Capita commentary for quarter two 2014/15 and forecasts that interest rates for both short and long term borrowing will increase up to March 2015. The Assistant Director Finance will continue to keep actual and forecast rates under close review.

4.6 In March 2014, Council approved a net borrowing requirement for 2014/15 of £168.3 million. The forecast net borrowing requirement for 2014/15 is £153.2 million, as shown in appendix F. PWLB borrowing of £23.0 million has been taken out during quarter two, and £10.0 million of temporary borrowing was repaid. £30.0 million of existing borrowing is due to be repaid in quarter four. Appendix D shows a detailed breakdown of new loans and repayments made throughout the year.

4.7 Appendix E shows a graphical summary of current borrowing by type; fixed and variable as at 30 September 2014.

4.8 Appendix F shows details for the disclosure for certainty rate, which will enable the Council to submit a return for 2014/15 and thereby secure access to discounted borrowing at 0.20% below normal PWLB rates.

4.9 In March 2014 Council approved the Annual Minimum Revenue Provision (MRP) Statement setting out the method used to calculate MRP for 2014/15 onwards. A review of this statement has identified potential savings that could be generated by switching to an annuity method. This was reported to Councillors at Cabinet on 22 October 2014 as part of the Budget and Medium Term Financial Strategy report. Appendix G shows the proposed new statement requiring approval. In the opinion of the Assistant Director Finance (Section 151 Officer) the methodology set out in the statement will generate an amount of MRP that is prudent; this has been agreed by the Council's external auditors.

## 5.0 Investment Forecast for 2014/15

5.1 The approach during the year is to continue to use cash balances to finance capital expenditure so as to keep cash balances low.

5.2 Table 4 shows the total amount of surplus funds invested as at 30 June 2014 and 30 September 2014.

**Table 4 – Total Amounts Invested 2014/15**

| | 30 June 2014<br>£000 | 30 September 2014<br>£000 |
|---|---:|---:|
| Business Reserve Accounts<br>Money Market Funds | 19,994<br>34,820 | 7<br>15,815 |
| | **54,814** | **15,822** |
| Average cash balance for the year to date | 59,979 | 46,301 |

5.3 Money Market Funds and Business Reserve Accounts are the main investments used as these have high credit ratings and instant access. This is based on the Council's low appetite for risk.

5.4 The Council's cash flow balances have reduced during the second quarter of the current financial year, moving between a low of £12.9 million up to a maximum of £50.0 million and have averaged £31.6 million for the quarter.

5.5 Table 5 shows the budgeted average rate of interest receivable in 2014/15 and the forecast for the year.

**Table 5 – Average Interest Rate Receivable in 2014/15**

| | 2014/15 Budget | 2014/15 Forecast |
|---|---|---|
| Average Interest Rate Receivable | 0.50% | 0.43% |

5.6 This reduction is due to the significantly reduced interest rates currently available and anticipated throughout the year.

5.7 The Council will avoid locking into longer term deals while investment rates are at historically low levels. Investment rates are expected to continue to be below long term borrowing rates, in which case, the Council can minimise its overall net treasury costs in the short term by continuing to avoid new external borrowing and by using internal cash balances to finance new capital expenditure or to replace maturing external debt (this is referred to as internal borrowing).

5.8 The Council manages its investments in-house and invests only in the institutions listed in the Council's approved lending list, which is reviewed each time a counterparty is subject to a credit rating amendment. The Council's strategy allows for investments for a range of periods from overnight to five years, depending on the Council's cash flows, its interest rate view and the interest rates on offer. However, in order to maintain sufficient liquidity whilst total investment levels are relatively low, most investments have been placed for shorter durations.

5.9 The approved Treasury Management Code of Practice sets out the criteria to be used for creating and managing approved counterparty lists and limits. As a result of any changes to credit criteria, the Assistant Director Finance is authorised to make changes to the list of approved counterparties. In the event that any of these counterparties fall below the council's minimum lending criteria, activity in that account will temporarily cease and any balance withdrawn immediately. Appendix H shows the Council's current specified investments lending list

5.10 In quarter two 2014/2015 the Assistant Director Finance has not been required to use his discretion to temporarily exceed any upper limits with approved counter-parties.

5.11 The Annual Investment Strategy (AIS) approved by Council in March 2014 details the criteria the Council will use when making investment decisions. Data provided by Capita as part of its credit methodology supports the AIS. Due to regulatory changes ratings information will be changed and therefore Capita will be revising the ratings information supplied to the Council. This will have no direct impact upon the risk of individual investments however as the previous ratings information was utilised in the Council's AIS this will have to be revised to incorporate the new ratings information. There is some uncertainty when these changes will come into force; however, when they do the Council's AIS will be amended by Assistant Director Finance under delegations approved in March 2014; it is not expected to impact on the Council's investments.

## 6.0 Financial Implications

6.1 The financial implications are discussed in the body of this report.

[SH/31102014/F]

## 7.0 Legal implications

7.1 Treasury Management relates to the management of the Council's cash flow, borrowing and cash investments. This involves seeking the best rates of interest for borrowing, earning interest on investments, whilst managing risk in making financial decisions and adopting proper accounting practice.

7.2 The area is heavily regulated. The Local Government and Housing Act 1989 regulates the operation of the Housing Revenue Account. The 'CIPFA Code of Practice for Treasury Management in the Public Services', contains Treasury Management indicators and advice on Treasury Management Strategy. Investment strategy is regulated by 'DCLG Guidance on Local Government Investments' issued initially in 2004 and re-issued in 2010. Part 2 of this Guidance is statutory guidance.

[TS/12112014/I]

## 8.0 Equalities implications

8.1 This report has no equality implications.

## 9.0 Environmental implications

9.1 This report has no environmental implications.

## 10.0 Human resources implications

10.1 This report has no human resources implications.

## 11.0 Corporate landlord implications

11.1 This report has no corporate landlord implications.

## 12.0 Schedule of background papers

Treasury Management Strategy 2014/15, Report to Cabinet, 25 February 2014

Treasury Management – Annual Report 2013/14 and Activity Monitoring Quarter One 2014/15, Report to Cabinet, 23 July 2014

2015/16 Budget and Medium Term Financial Strategy 2015/16 – 2018/19, Report to Cabinet, 22 October 2014

## 13.0 Schedule of Appendices

**APPENDIX A**

**Debt and Treasury Management - Prudential and Treasury Management Indicators**

**Prudential Indicators (PI)**

**PI for Affordability -** These indicators are used to ensure the total capital investment of the council is within a sustainable limit and the impact of these decisions are considered with regard to acceptable council tax and housing rent levels.

**PI 1 - Estimates and Actual ratio of financing costs to net revenue stream.**
This represents the cost of financing capital expenditure as a % of net revenue for both the General Fund and HR/

| | Approved by Council 5 March 2014 | | | As at 30 September 2014 | | |
|---|---|---|---|---|---|---|
| | 2014/15 Forecast | 2015/16 Forecast | 2016/17 Forecast | 2014/15 Forecast | 2015/16 Forecast | 2016/17 Forecast |
| General Fund | 10.3% | 14.0% | 15.6% | 8.0% | 11.6% | 14.4% |
| HRA | 12.3% | 12.1% | 12.6% | 11.1% | 10.6% | 12.6% |

**PI 2 - Estimates of the incremental impact of capital investment decisions on the council tax and housin**
The council could consider different options for its capital investment programme in relation to their different impact on the council tax and housing rents. Negatives reflect a reduction in total capital expenditure.

| | Approved by Council 5 March 2014 | | | As at 30 September 2014 | | |
|---|---|---|---|---|---|---|
| | 2014/15 Forecast £ | 2015/16 Forecast £ | 2016/17 Forecast £ | 2014/15 Forecast £ | 2015/16 Forecast £ | 2016/17 Forecast £ |
| For Band D council tax | | | | | | |
| Implications of the Capital Programme for Year | 201.41 | 236.60 | 243.92 | 157.70 | 228.25 | 248.59 |
| Financial Year Impact | 201.41 | 236.60 | 243.92 | 157.70 | 228.25 | 248.59 |
| For average weekly housing rents | | | | | | |
| Implications of the Capital Programme for Year | 4.65 | 5.34 | 6.13 | 3.28 | 6.32 | 7.52 |
| Financial Year Impact | 4.65 | 5.34 | 6.13 | 3.28 | 6.32 | 7.52 |
| For Band D council tax | | | | | | |
| Implications of the Capital Programme for Year | 2.02 | (7.64) | (15.44) | (6.36) | 7.14 | 23.11 |
| Marginal Impact to Quarter One | 2.02 | (7.64) | (15.44) | (6.36) | 7.14 | 23.11 |
| For average weekly housing rents | | | | | | |
| Implications of the Capital Programme for Year | - | - | - | (0.82) | (0.04) | (0.04) |
| Marginal Impact to Quarter One | - | - | - | (0.82) | (0.04) | (0.04) |

**PI 3 - Estimates and actual capital expenditure.**
Full details of capital expenditure plans and funding can be found in the Capital Quarter Two Monitoring 2014/15 report.

| | Approved by Council 5 March 2014 | | | As at 30 September 2014 | | |
|---|---|---|---|---|---|---|
| | 2014/15 Forecast £000 | 2015/16 Forecast £000 | 2016/17 Forecast £000 | 2014/15 Forecast £000 | 2015/16 Forecast £000 | 2016/17 Forecast £000 |
| General Fund | 111,799 | 36,889 | 18,290 | 122,692 | 57,035 | 29,195 |
| HRA | 57,928 | 30,477 | 33,228 | 74,935 | 62,040 | 38,233 |
| | 169,727 | 67,366 | 51,518 | 197,627 | 119,075 | 67,428 |

**APPENDIX A**

**Debt and Treasury Management - Prudential and Treasury Management Indicators**

**PI 4 - Estimates and actual capital financing requirement General Fund and HRA.**
The capital financing requirement measures the authority's underlying need to borrow for a capital purpose.

| | Approved by Council 5 March 2014 | | | As at 30 September 2014 | | |
|---|---|---|---|---|---|---|
| | 2014/15 Forecast £000 | 2015/16 Forecast £000 | 2016/17 Forecast £000 | 2014/15 Forecast £000 | 2015/16 Forecast £000 | 2016/17 Forecast £000 |
| General Fund | 570,638 | 573,285 | 556,896 | 558,031 | 589,136 | 586,333 |
| HRA | 352,603 | 347,163 | 340,438 | 328,864 | 352,234 | 349,975 |
| | 923,241 | 920,448 | 897,334 | 886,895 | 941,370 | 936,308 |

**PI 5 - Authorised limit for external debt.**
These limits apply to the total external debt gross of investments and separately identify borrowing from other long term liabilities such as finance leases including Private Finance Initiatives (PFI).

| | Approved by Council 5 March 2014 | | |
|---|---|---|---|
| | 2014/15 Limit £000 | 2015/16 Limit £000 | 2016/17 Limit £000 |
| Borrowing | 896,862 | 909,345 | 919,984 |
| Other Long Term Liabilities | 109,740 | 98,092 | 96,145 |
| Total Authorised Limit | 1,006,602 | 1,007,437 | 1,016,129 |
| Forecast External Debt As at 30 September 2014 | 766,062 | 847,005 | 873,068 |
| Variance (Under) / Over Authorised Limit | (240,540) | (160,432) | (143,061) |

**PI 6 - Operational boundary for external debt.**
This is based on the same estimates as the authorised limit but directly reflects the Assistant Director Finance's estimate of the most likely, prudent but not worst case scenario, without the additional headroom included.

| | Approved by Council 5 March 2014 | | |
|---|---|---|---|
| | 2014/15 Limit £000 | 2015/16 Limit £000 | 2016/17 Limit £000 |
| Borrowing | 870,926 | 901,661 | 916,319 |
| Other Long Term Liabilities | 100,057 | 98,092 | 96,145 |
| Total | 970,983 | 999,753 | 1,012,464 |
| Forecast External Debt As at 30 September 2014 | 766,062 | 847,005 | 873,068 |
| Variance (Under) / Over Operational Boundary Limit | (204,921) | (152,748) | (139,396) |

**APPENDIX A**

**Debt and Treasury Management - Prudential and Treasury Management Indicators**

**PI 7 - HRA limit on indebtedness.**
This maximum debt limit has been set by Government as part of the self-financing regime and is compared to the HRA capital financing requirement.

| | Approved by Council 5 March 2014 | | | As at 30 September 2014 | | |
|---|---|---|---|---|---|---|
| | 2014/15 Forecast £000 | 2015/16 Forecast £000 | 2016/17 Forecast £000 | 2014/15 Forecast £000 | 2015/16 Forecast £000 | 2016/17 Forecast £000 |
| HRA Debt Limit | 356,770 | 356,770 | 356,770 | 356,770 | 356,770 | 356,770 |
| HRA Capital Financing Requirement | 352,603 | 347,163 | 340,438 | 328,864 | 352,234 | 349,975 |
| Headroom | 4,167 | 9,607 | 16,332 | 27,906 | 4,536 | 6,795 |

**PI for Prudence -** Ensuring that external debt is sustainable and compliance with good professional practice are essential features of prudence.

**PI 8a - Gross debt and the capital financing requirement.**
"In order to ensure that over the medium term debt will only be for a capital purpose, the local authority should ensure that debt does not, except in the short term, exceed the total of capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years". This replaced PI 8 net debt and the capital financing requirement from 2013/14 onwards.

| | Approved by Council 5 March 2014 | | | As at 30 September 2014 | | |
|---|---|---|---|---|---|---|
| | 2014/15 Forecast £000 | 2015/16 Forecast £000 | 2016/17 Forecast £000 | 2014/15 Forecast £000 | 2015/16 Forecast £000 | 2016/17 Forecast £000 |
| Forecast Capital Financing Requirement at end of Second Year | 920,448 | 923,241 | 920,448 | 941,371 | 941,371 | 941,371 |
| Gross Debt | 804,343 | 833,112 | 845,824 | 766,062 | 847,005 | 873,068 |
| Capital Financing Requirement Greater than Gross Debt | Yes | Yes | Yes | Yes | Yes | Yes |

**PI 9 - Has the local authority adopted the CIPFA Treasury Management in the Public Services: Code of Practice. Yes**

**APPENDIX A**

**Debt and Treasury Management - Prudential and Treasury Management Indicators**

**Treasury Management Indicators (TMI)**

**TMI 1 - Upper limits on fixed interest and variable interest exposures.**
These relate to the levels of net outstanding principal sums exposed to fixed and variable interest rates.

| | Approved by Council 5 March 2014 | | | As at 30 September 2014 | | |
|---|---|---|---|---|---|---|
| | 2014/15 Limit | 2015/16 Limit | 2016/17 Limit | 2014/15 Forecast | 2015/16 Forecast | 2016/17 Forecast |
| Upper limit for fixed rate | 100% | 100% | 100% | 84% | 86% | 87% |
| Upper limit for variable rate | 20% | 20% | 20% | 16% | 14% | 13% |

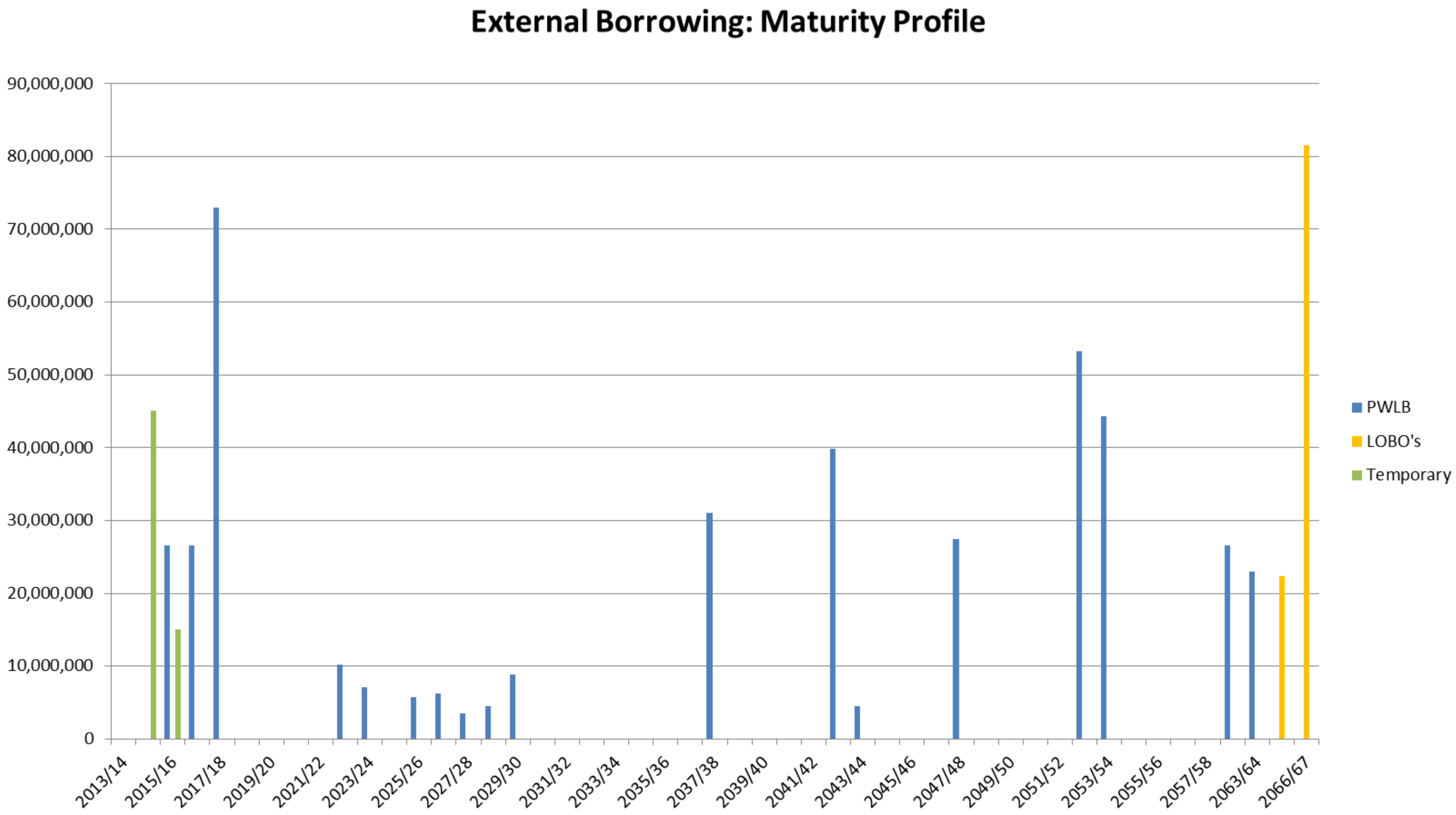
**TMI 2 - Upper and lower limits to the maturity structure of its borrowing.**
These limits relate to the % of fixed rate debt maturing.

| | Approved by Council 5 March 2014 | | As at 30 September 2014 | |
|---|---|---|---|---|
| | Upper Limit | Lower Limit | Proposed Upper Limit | 2014/15 Forecast Borrowing |
| Under 12 months | 10% | 0% | 25% | 20.56% |
| 12 months and within 24 months | 15% | 0% | 25% | 4.77% |
| 24 months and within 5 years | 20% | 0% | 40% | 13.10% |
| 5 years and within 10 years | 20% | 0% | 50% | 3.10% |
| 10 years and above | 90% | 50% | 90% | 58.46% |

**TMI 3 - Upper limits to the total of principal sums invested longer than 364 days.**
This details the maximum amount which can be invested for up to 5 years (as per paragraph 1.5 of the Annual Investment Strategy).

| | Approved by Council 5 March 2014 | | | As at 30 September 2014 | | |
|---|---|---|---|---|---|---|
| | 2014/15 Limit £000 | 2015/16 Limit £000 | 2016/17 Limit £000 | 2014/15 Forecast £000 | 2015/16 Forecast £000 | 2016/17 Forecast £000 |
| Upper limit for more than 364 days | 35,000 | 35,000 | 35,000 | 35,000 | 35,000 | 35,000 |

**APPENDIX B**


External Borrowing: Maturity Profile
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PWLB
LOBO's
Temporary

**APPENDIX C**

## Economic Background

The following economic background has been provided by the Council's Treasury Advisors, Capita.

### U.K.

After strong UK GDP quarterly growth of 0.7%, 0.8% and 0.7% in quarters 2, 3 and 4 respectively in 2013, (2013 annual rate 2.7%), and 0.7% in Q1, 0.9% in Q2 and a first estimate of 0.7% in Q3 2014 (annual rate 3.1% in Q3), it appears very likely that strong growth will continue through 2014 and into 2015 as forward surveys for the services and construction sectors, are very encouraging and business investment is also strongly recovering. The manufacturing sector has also been encouraging though the latest figures indicate a weakening in the future trend rate of growth. However, for this recovery to become more balanced and sustainable in the longer term, the recovery needs to move away from dependence on consumer expenditure and the housing market to exporting, and particularly of manufactured goods, both of which need to substantially improve on their recent lacklustre performance. This overall strong growth has resulted in unemployment falling much faster through the initial threshold of 7%, set by the Monetary Policy Committee (MPC) last August, before it said it would consider any increases in Bank Rate. The MPC has, therefore, subsequently broadened its forward guidance by adopting five qualitative principles and looking at a much wider range of about eighteen indicators in order to form a view on how much slack there is in the economy and how quickly slack is being used up. The MPC is particularly concerned that the current squeeze on the disposable incomes of consumers should be reversed by wage inflation rising back above the level of inflation in order to ensure that the recovery will be sustainable. There also needs to be a major improvement in labour productivity, which has languished at dismal levels since 2008, to support increases in pay rates. Most economic forecasters are expecting growth to peak in 2014 and then to ease off a little, though still remaining strong, in 2015 and 2016. Unemployment is therefore expected to keep on its downward trend and this is likely to eventually feed through into a return to significant increases in pay rates at some point during the next three years. However, just how much those future increases in pay rates will counteract the depressive effect of increases in Bank Rate on consumer confidence, the rate of growth in consumer expenditure and the buoyancy of the housing market, are areas that will need to be kept under regular review.

Also encouraging has been the sharp fall in inflation (CPI), reaching 1.2% in September, the lowest rate since 2009. Forward indications are that inflation is likely to fall further in 2014 to possibly 1%. Overall, markets are expecting that the MPC will be cautious in raising Bank Rate as it will want to protect heavily indebted consumers from too early an increase in Bank Rate at a time when inflationary pressures are also weak. A first increase in Bank Rate is therefore expected in Q2 2015 and they expect increases after that to be at a slow pace to lower levels than prevailed before 2008 as increases in Bank Rate will have a much bigger effect on heavily indebted consumers than they did before 2008.

The return to strong growth has also helped lower forecasts for the increase in Government debt by £73bn over the next five years, as announced in the 2013 Autumn Statement, and by

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an additional £24bn, as announced in the March 2014 Budget - which also forecast a return to a significant budget surplus, (of £5bn), in 2018-19. However, monthly public sector deficit figures have disappointed so far in 2014/15.

**U.S.**

In September, the Federal Reserve continued with its monthly $10bn reductions in asset purchases, which started in December 2013. Asset purchases have now fallen from $85bn to $15bn and are expected to stop on 29th October 2014, providing the economic outlook remains strong. First quarter GDP figures for the US were depressed by exceptionally bad winter weather, but growth rebounded very strongly in Q2 to 4.6% (annualised).

The U.S. faces similar debt problems to those of the UK, but thanks to reasonable growth, cuts in government expenditure and tax rises, the annual government deficit has been halved from its peak without appearing to do too much damage to growth, although the weak labour force participation rate remains a matter of key concern for the Federal Reserve when considering the amount of slack in the economy and monetary policy decisions.

**Eurozone**

The Eurozone is facing an increasing threat from weak or negative growth and from deflation. In September, the inflation rate fell further, to reach a low of 0.3%. However, this is an average for all EZ countries and includes some countries with negative rates of inflation. Accordingly, the ECB took some rather limited action in June to loosen monetary policy in order to promote growth. In September it took further action to cut its benchmark rate to only 0.05%, its deposit rate to -0.2% and to start a programme of purchases of corporate debt. However, it has not embarked yet on full quantitative easing (purchase of sovereign debt).

Concern in financial markets for the Eurozone subsided considerably during 2013. However, sovereign debt difficulties have not gone away and major issues could return in respect of any countries that do not dynamically address fundamental issues of low growth, international uncompetitiveness and the need for overdue reforms of the economy, (as Ireland has done). It is, therefore, possible over the next few years that levels of government debt to GDP ratios could continue to rise for some countries. This could mean that sovereign debt concerns have not disappeared but, rather, have only been postponed.

**China and Japan**

Japan is causing considerable concern as the increase in sales tax in April has suppressed consumer expenditure and growth. In Q2 growth was -1.8% q/q and -7.1% over the previous year. The Government is hoping that this is a temporary blip.

As for China, Government action in 2014 to stimulate the economy appeared to be putting the target of 7.5% growth within achievable reach but recent data has raised fresh concerns. There are also major concerns as to the creditworthiness of much bank lending to corporates and local government during the post 2008 credit expansion period and whether the bursting of a bubble in housing prices is drawing nearer.

**APPENDIX C**

**Interest Rate Forecast**

The Council's treasury advisor, Capita Asset Services, has provided the following forecast:

| | Dec-14 | Mar-15 | Jun-15 | Sep-15 | Dec-15 | Mar-16 | Jun-16 | Sep-16 | Dec-16 | Mar-17 | Jun-17 | Sep-17 | Dec-17 | Mar-18 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Bank rate | 0.50% | 0.50% | 0.75% | 0.75% | 1.00% | 1.00% | 1.25% | 1.25% | 1.50% | 1.50% | 1.75% | 2.00% | 2.25% | 2.50% |
| 5yr PWLB rate | 2.50% | 2.70% | 2.70% | 2.80% | 2.90% | 3.00% | 3.10% | 3.20% | 3.30% | 3.40% | 3.50% | 3.50% | 3.50% | 3.50% |
| 10yr PWLB rate | 3.20% | 3.40% | 3.50% | 3.60% | 3.70% | 3.80% | 3.90% | 4.00% | 4.10% | 4.10% | 4.20% | 4.20% | 4.30% | 4.30% |
| 25yr PWLB rate | 3.90% | 4.00% | 4.10% | 4.30% | 4.40% | 4.50% | 4.60% | 4.70% | 4.70% | 4.80% | 4.80% | 4.90% | 4.90% | 5.00% |
| 50yr PWLB rate | 3.90% | 4.00% | 4.10% | 4.30% | 4.40% | 4.50% | 4.60% | 4.70% | 4.70% | 4.80% | 4.80% | 4.90% | 4.90% | 5.00% |

Capita Asset Services undertook a review of its interest rate forecasts on 24 October. During September and October, a further rise in geopolitical concerns, principally over Ukraine but also over the Middle East, plus fears around Ebola and an accumulation of dismal growth news in most of the ten largest economies of the world and also on the growing risk of deflation in the Eurozone, had sparked a flight from equities into safe havens like gilts and depressed PWLB rates. However, there is much volatility in rates as news ebbs and flows in negative or positive ways. This latest forecast includes a first increase in Bank Rate in quarter 2 of 2015.

Our PWLB forecasts are based around a balance of risks. However, there are potential upside risks, especially for longer term PWLB rates, as follows: -

- A further surge in investor confidence that robust world economic growth is firmly expected, causing a flow of funds out of bonds and into equities.

- UK inflation being significantly higher than in the wider EU and US, causing an increase in the inflation premium inherent to gilt yields.

Downside risks currently include:

- The situation over Ukraine poses a major threat to EZ and world growth if it was to deteriorate into economic warfare between the West and Russia where Russia resorted to using its control over gas supplies to Europe.

- Fears generated by the potential impact of Ebola around the world

- UK strong economic growth is currently mainly dependent on consumer spending and the potentially unsustainable boom in the housing market. The boost from these sources is likely to fade after 2014.

**APPENDIX C**

- A weak rebalancing of UK growth to exporting and business investment causing a weakening of overall economic growth beyond 2014.

- Weak growth or recession in the UK's main trading partner - the EU, inhibiting economic recovery in the UK.

- A return to weak economic growth in the US, UK and China causing major disappointment in investor and market expectations.

- A resurgence of the Eurozone sovereign debt crisis caused by ongoing deterioration in government debt to GDP ratios to the point where financial markets lose confidence in the financial viability of one or more countries and in the ability of the ECB and Eurozone governments to deal with the potential size of the crisis.

- Recapitalisation of European banks requiring more government financial support.

- Lack of support by populaces in Eurozone countries for austerity programmes, especially in countries with very high unemployment rates e.g. Greece and Spain, which face huge challenges in engineering economic growth to correct their budget deficits on a sustainable basis.

- Italy: the political situation has improved but it remains to be seen whether the new government is able to deliver the austerity programme required and a programme of overdue reforms. Italy has the third highest government debt mountain in the world.

- France: after being elected on an anti austerity platform, President Hollande has embraced a €50bn programme of public sector cuts over the next three years. However, there could be major obstacles in implementing this programme. Major overdue reforms of employment practices and an increase in competiveness are also urgently required to lift the economy out of stagnation.

- Monetary policy action failing to stimulate sustainable growth in western economies, especially the Eurozone and Japan.

- Heightened political risks in the Middle East and East Asia could trigger safe haven flows back into bonds.

- There are also increasing concerns at the reluctance of western central banks to raise interest rates significantly for some years, plus the huge QE measures which remain in place (and may be added to by the ECB in the near future). This has created potentially unstable flows of liquidity searching for yield and, therefore, heightened the potential for an increase in risks in order to get higher returns. This is a return to a similar environment to the one which led to the 2008 financial crisis.

**APPENDIX D**

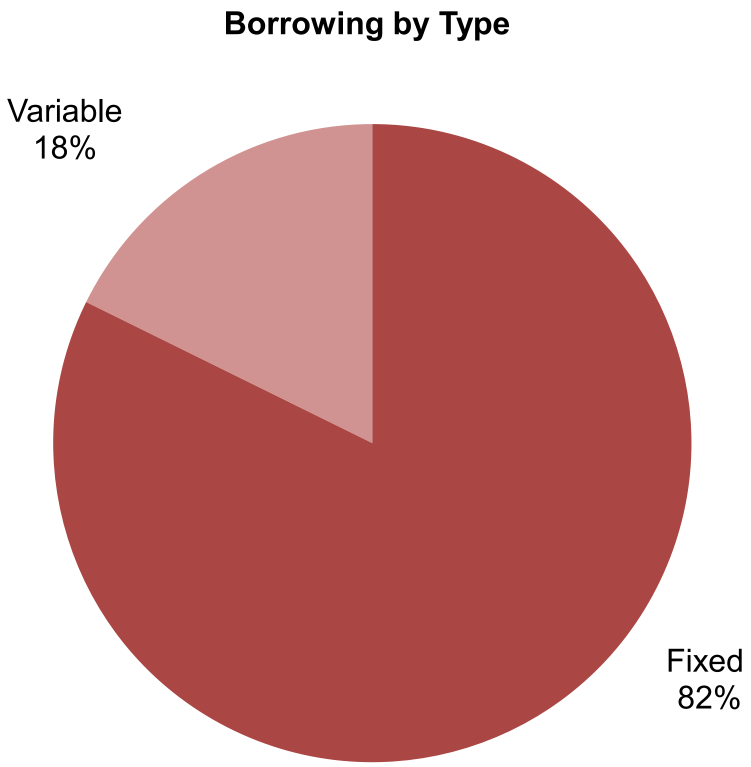
**Borrowing and Repayments in 2014/15**

| | Maturity Date | Amount £000 | Length | Interest Rate | Full Year Interest £000 |
|---|---|---|---|---|---|
| **2014/15 Borrowing** | | | | | |
| PWLB Fixed Maturity | | | years | | |
| 503341 | 30/09/2017 | 23,000 | 3 | 2.05% | 472 |
| | | **23,000** | | **2.05%** | **472** |
| **2014/15 Repayments** | | | | | |
| Temporary Loans | | | days | | |
| Caerphilly BC | 02/05/2014 | 5,000 | 86 | 0.35% | 4 |
| Portsmouth City Council | 29/08/2014 | 6,000 | 182 | 0.43% | 13 |
| Derbyshire CC Super. Fund | 29/08/2014 | 4,000 | 182 | 0.45% | 9 |
| | | **15,000** | | **0.41%** | **26** |

**APPENDIX E**

## Borrowing: Graphical Summary

## As at 30 September 2014



**APPENDIX F**

## Disclosure for Certainty Rate

**Certainty Rate**
This table details the information that is required to enable the Council to submit a return for 2014/15.

| | As at 25 February 2014 | | | As at 30 September 2014 | | |
|---|---|---|---|---|---|---|
| | 2014/15 Forecast £000 | 2015/16 Forecast £000 | 2016/17 Forecast £000 | 2014/15 Forecast £000 | 2015/16 Forecast £000 | 2016/17 Forecast £000 |
| **Net Borrowing Requirement:** | | | | | | |
| Borrowing to Finance approved Capital Expenditure | 103,742 | 30,735 | 14,658 | 104,440 | 82,851 | 27,949 |
| Existing Maturity Loans to be Replaced During the Year | 90,000 | 76,605 | 86,605 | 70,200 | 114,605 | 76,605 |
| Less: | | | | | | |
| Minimum Revenue Provision for Debt Repayment | (13,646) | (17,394) | (19,020) | (7,690) | (11,125) | (13,637) |
| Voluntary Debt Repayment | (11,804) | (14,169) | (16,805) | (13,711) | (15,343) | (17,488) |
| | (25,450) | (31,563) | (35,825) | (21,401) | (26,468) | (31,125) |
| Loans Replaced Less Debt Repayment | 64,550 | 45,042 | 50,780 | 48,799 | 88,137 | 45,480 |
| Net Advance Requirement | 168,292 | 75,777 | 65,438 | 153,239 | 170,988 | 73,429 |

**APPENDIX G**

## Annual MRP Statement 2014/15

### Minimum Revenue Provision – an introduction

### 1. What is Minimum Revenue Provision?

Capital expenditure is generally expenditure on assets which have a life expectancy of more than one year e.g. buildings, vehicles, machinery etc. In accordance with proper practice, the financing of such expenditure is spread over several years in order to try to match the years over which such assets benefit the local community through their useful life. The manner of spreading these costs is through an annual charge known as Minimum Revenue Provision (MRP), which is determined by the Council under guidance.

### 2. Statutory duty

The Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 (as amended by Statutory Instrument 2008 no. 414 s4) lay down that:

"A local authority shall determine for the current financial year an amount of minimum revenue provision that it considers to be prudent."

### 3. Government guidance

Along with the above duty, the Government issued guidance which came into force on 31 March 2008 which requires that a Statement on the Council's policy for its annual MRP should be submitted to the full Council for approval before the start of the financial year to which the provision will relate.

The Council is legally obliged to "have regard" to the guidance, which is intended to enable a more flexible approach to assessing the amount of annual provision than was required under the previous statutory requirements. Although it is up to each Council to determine for itself how to calculate its MRP, the guidance suggests four methodologies, with an overriding recommendation that the Council should make prudent provision to redeem its debt liability over a period which is reasonably commensurate with that over which the capital expenditure is estimated to provide benefits. The requirement to 'have regard' to the guidance therefore means that:

1. Although four main options are recommended in the guidance, there is no intention to be prescriptive by making these the only methods of charge under which a local authority may consider its MRP to be prudent.

2. It is the responsibility of each authority to decide upon the most appropriate method of making a prudent provision, after having had regard to the guidance.

**APPENDIX G**

## 4. Timing

This statement shall take effect from 1 April 2014 and shall take precedence over any statements previously approved.

## 5. Calculation

MRP shall be calculated by adding together the amount calculated using the method as stated below and any amount calculated under adjustment 1 below.

**Method**

To be used for all capital expenditure taking into account only capital expenditure and financing decisions, and the classification of fixed assets, reflected in the Council's accounts for the preceding year.

With the variations set out below, MRP will be calculated, on an individual fixed asset basis (unless they are land or community assets (no depreciation) or where it is capitalised under statute/direction (equal pay, refcus etc.) when one grouped "asset" is created for MRP calculation purposes for each category for individual years), in accordance with the annuity method whereby MRP for each year will be the amount presumed to be the principal element of the equal amounts that would be payable each year in respect of a loan at the specified rate of interest that would reduce the outstanding principal amount to zero at the end of the estimated useful life.

The specified rate of interest will be the average interest rate of the Council's debt as at the end of the year preceding the first year in which the annuity rate is to be applied. Where the interest rate on debt is variable the rate to be used in calculating the average shall be the interest rate on the debt at 31 March of the year for which the average is being calculated.

MRP will thus be calculated in accordance with the following formula:

PPMT (A,B,C,D-E) + F

Where

PPMT is the PPMT financial function in Microsoft Excel 2010
A is the specified interest rate
B is the number of years (including the current year) for which MRP has been charged on an annuity basis
C is the useful economic life of the asset as at the start of the year for which MRP is first charged on an annuity basis
D is the total need to borrow for capital purposes (resulting from capital expenditure)
E is the aggregate value of any anticipated future capital receipts that are an integral part of the capital scheme in question.
F is an amount determined by Cabinet (Resources) Panel.

**APPENDIX G**

C shall be equal to the useful life of the fixed asset in question, as estimated by the Council. For assets with a useful life of more than 99 years, C shall equal 99. C shall not be varied for changes in the useful life of the asset unless the Council considers that special circumstances apply that would mean that a change would result in MRP being more reasonably calculated on a prudent basis; for example the useful life of a particular asset (as assessed for depreciation purposes) could change so dramatically that continued use of the option would no longer be supportable as prudent. For example, a property could be sold only a short time into its originally estimated useful life.

E shall be reviewed each year on performing the calculation, and amended if necessary.

The cumulative total of F, taken across all past and current years, shall never be less than zero.

**The Method shall be varied in the following circumstances:**

(a) For non-operational assets, for which no charge will be made.

(b) For expenditure on fixed assets that are not or would not be classed as fixed assets of the Council in accordance with proper accounting practice, for which C shall initially be equal to the estimated remaining useful life of the fixed asset in question.

(c) For expenditure capitalised under direction, for which C shall initially equal 20, and shall not be reviewed or amended.

**APPENDIX H**

## Wolverhampton City Council
## 2014/15 Specified Investments Lending List as at 30 September 2014

| Institution | Country (Sovereign Rating) | Limit £000 | Term Limit |
|---|---|---|---|
| Australia & New Zealand Banking Group Ltd | Australia (AAA) | 10,000 | 6 mths |
| Bank Netherlandse Gemeenten | Netherlands (AAA) | 20,000 | 12 mths |
| Bank of Montreal | Canada (AAA) | 10,000 | 6 mths |
| Bank of New York Mellon, The | USA (AAA) | 10,000 | 6 mths |
| Bank of Nova Scotia | Canada (AAA) | 10,000 | 6 mths |
| Canadian Imperial Bank of Commerce | Canada (AAA) | 10,000 | 6 mths |
| Clearstream Banking | Luxembourg (AAA) | 20,000 | 12 mths |
| Commonwealth Bank of Australia | Australia (AAA) | 10,000 | 6 mths |
| Cooperatieve Centrale Raiffeisen - Boerenleenbank BA | Netherlands (AAA) | 5,000 | 3 mths |
| DBS Bank Ltd | Singapore (AAA) | 10,000 | 6 mths |
| Hong Kong and Shanghai Banking Corporation Ltd | Hong Kong (AA+) | 10,000 | 6 mths |
| HSBC Bank plc | UK (AA+) | 10,000 | 6 mths |
| HSBC Bank USA | USA (AAA) | 10,000 | 6 mths |
| National Australia Bank Ltd | Australia (AAA) | 10,000 | 6 mths |
| Nordea Bank AB | Sweden (AAA) | 10,000 | 6 mths |
| Nordea Bank Finland plc | Finland (AAA) | 10,000 | 6 mths |
| Oversea Chinese Banking Corporation Ltd | Singapore (AAA) | 10,000 | 6 mths |
| Royal Bank of Canada | Canada (AAA) | 10,000 | 6 mths |
| Standard Chartered Bank | UK (AA+) | 10,000 | 6 mths |
| Svenska Handelsbanken AB | Sweden (AAA) | 10,000 | 6 mths |
| Toronto Dominion Bank | Canada (AAA) | 10,000 | 6 mths |
| United Overseas Bank Ltd | Singapore (AAA) | 10,000 | 6 mths |
| Wells Fargo Bank NA | USA (AAA) | 10,000 | 6 mths |
| Westpac Banking Corporation | Australia (AAA) | 10,000 | 6 mths |
| **Nationalised Banks** | | | |
| **Lloyds Banking Group plc** | | | |
| Bank of Scotland plc | UK (AA+) | 10,000 | 3 mths |
| Lloyds Bank plc | UK (AA+) | 10,000 | 3 mths |
| **Royal Bank of Scotland Group plc** | | | |
| National Westminster Bank plc | UK (AA+) | 10,000 | 3 mths |
| The Royal Bank of Scotland plc | UK (AA+) | 10,000 | 3 mths |
| **Money Market Funds** | **Fund Rating** | | |
| Invesco STIC Account | Fitch AAAmmf | 20,000 | Instant Access |
| Ignis Sterling Liquidity Fund | Fitch AAAmmf | 20,000 | Instant Access |
| Federated Short-Term Sterling Prime Fund | Fitch AAAmmf | 20,000 | Instant Access |
| Black Rock Sterling Liquidity Fund | Moody's Aaa-mf | 20,000 | Instant Access |
| Scottish Widows Sterling Liquidity Fund | Moody's Aaa-mf | 20,000 | Instant Access |

**Non-rated Institutions**

County Councils, London Boroughs, Metropolitan Districts and Unitary Authorities - limits £6m and 12 months. Shire District Councils, Fire and Civil Defence Authorities, Passenger Transport Authorities and Police Authorities - limits £3m and 12 months.