Agenda item 8

Cabinet – 4 February 2009

Annual Treasury Management and Investment Strategy - Prudential Indicators 2009/10 onwards

Portfolio: Councillor A Griffiths – Finance and Personnel

Service: Corporate Finance

Wards: All

Key decisions: Yes

Forward Plan: Yes

1. Summary of report

1.1. This report sets out treasury management and investment strategies as required by the CIPFA Code of Practice and the council's investment and treasury management policy statement for 2009/10 onwards (**Appendix A**).

1.2. It also provides details on the Prudential Code Indicators (PCIs) for the next three years (**Appendix B**) and asks cabinet to recommend adoption of these to full Council. The report both complies with the Local Government Act 2003 and also provides an additional framework over and above the statutory minimum for monitoring performance.

1.3. The treasury management and investment strategies support the capital programme and revenue budgets, which in turn are key to the delivery of the council's vision. **Appendix C** provides details on the required borrowing and resources needed.

1.4. The treasury management function participates in a local and national benchmarking group, which compares Walsall council's treasury management performance with those of other councils. As previously reported Walsall continues to have a low average rate of borrowing compared to other councils. This has enabled the council to take out additional unsupported borrowing to support capital investment.

2. Recommendations

2.1. That the 2009/10 treasury management and investment strategy document set out in **Appendix A** and the adoption of the prudential indicators set out in **Appendix B** be approved and recommended to full Council.

2.2. That decisions to effect movements between conventional borrowing and other long term liabilities, such as leases, be delegated to the Chief Finance Officer.

2.3. That decisions to use capital receipts or unsupported borrowing within the framework of approved prudential indicators be delegated to the Chief Finance Officer.

3. Background information

3.1. Members consider treasury management and investment strategies each year as a requirement of the CIPFA Code of Practice on Treasury Management in the Public Services; the updated version of which cabinet formally adopted on 22 March 2002. Capital Financing regulations issued in February 2008 require that a Statement on the council's policy for its annual minimum revenue provision (MRP) i.e. the amount set-aside for the repayment of debt, should be submitted to the full Council for approval before the start of the financial year to which the provision will relate. Thus a MRP statement to be used for the set-aside each year for the repayment of debt is included in the treasury management strategy (See **Appendix A**).

3.2. The 2003 Prudential Code for Capital Finance in Local Authorities (the Code) introduced new requirements for the way in which capital investment plans are considered and approved and introduced more integration with councils' treasury management strategies and the council's medium term financial planning activities.

3.3. The draft budget contains prudential indicators and borrowing limits for treasury management activities in 2009/10. This provides a framework through which the authority's treasury management and investment strategy is monitored.

3.4. The Code requires the council to set a number of prudential indicators (PCIs) (See **Appendix B**). These set limits on maximum total borrowing, temporary borrowing and on the proportion of borrowing at variable interest rates. The PCIs cover a period of three years from 2009/10 to 2011/12.

3.5. The ability to contain costs and make savings in this activity directly impacts on the level of resources available for the development of council strategies. Treasury management activity is delegated to the Chief Finance Officer (CFO) and Deputy CFO. Relevant activities take place within the framework of the council's treasury policy statement, which sets out the type of activities that may be undertaken and by whom. It also specifies formal reporting requirements. The specific elements of the MTFS relating to treasury management are as follows:

TREASURY MANAGEMENT

CONTEXT: We have a successful track record of effective treasury management, securing low cost borrowing to fund capital investment. Our aim is to continue to do so within the requirements of the prevailing policies and codes of practice.

G1 All borrowing and/or investment activity will be carried out in accordance with the approved treasury management strategy and treasury policy statements and within approved prudential indicators, having the highest regard for prudence, affordability and sustainability in the longer term.

G2 Appropriate use will be made of the prudential Code for capital investment within approved prudential indicators and subject to medium term affordability.

Source: extract from the MTFS, Nov 2008

3.6 The local target for the average rate for external debt remains at less than 4.7% for internally managed debt and less than 4.85% for total debt. To beat this target the rescheduling of debt would be required, opportunities for this are continually assessed.

3.7 In response to the sharp falls in the bank interest rate. The rate to be gained from investment returns (income to the council) has been decreased from 5.25% to 3.5%. A commentary on the current economic climate provided by the council's treasury advisors is included in **Appendix D.** It includes a summary of economic forecasts for 2009/10 and beyond. The recent world banking crisis has made the environment for investments more unstable and returns have reduced. The UK's bank base rate has reduced from 5.25% to 1.75% in the last 12 months. The council's investment return target will need particular attention, monitoring and potentially review during the year.

4. Resource considerations

4.1 Financial

- The council is expected to end 2008/9 with a net borrowing portfolio of £264m (£257m 2007/8) against an asset base of £859m and short term investments of between £80m and £90m. These will be proactively managed to minimise borrowing costs and maximise investment returns within a robust risk management environment. In 2009/10 estimated annual interest payments are c£11.6m and investment interest income c£2.4m. The net budget for capital financing in 2009/10 is £16.8m. The challenge for the capital financing budget once again this year has been to manage the loss of commutation grant and discounts of £0.800m from 2007/8 whilst also generating additional borrowing capacity to support the capital programme.

- All financial activities by the council are covered by the strategies. Funds managed on behalf of schools and street lighting receive the benefit from interest gained (c£0.800m).

4.2 Legal

- The Local Government Act 2003 and supporting Regulations require the council to 'have regard to' the Prudential Code and to set prudential indicators for the next three years to ensure that the council's capital investment plans are affordable, prudent and sustainable.

- The Act requires the council to set out its treasury strategy for borrowing and to prepare an annual investment strategy (as required by investment guidance issued subsequent to the Act); this sets out the council's policies for managing it's investments and for giving priority to the security and liquidity of those investments.

4.3 **Staffing**

None directly related to the report.

5. Citizen impact

None directly related to the report.

6. Community safety

None directly associated with this report.

7. Environmental impact

None directly related to the report.

8. Performance and risk management issues

8.1 **Risk**

- Treasury management activity takes place within a robust risk management environment, which enables the council to effectively maximise investment income and minimise interest payments without undue or inappropriate exposure to financial risk. A risk assessment has been undertaken in determining the 2009/10 policy and this is contained within the council's corporate risk register.

- In response to the banking crisis in 2008 culminating in the failure of the Icelandic banks and the loss by some other council's of their deposits. additional controls and monitoring have been added to the council's process for making deposits with Banks and Building Societies to ensure that the security of Walsall's cash reserves is maintained as of paramount importance, although this cannot be guaranteed.

8.2 **Performance**

- Performance is regularly reviewed by the treasury management panel. Activities are planned in 2009/10 to further improve the service and performance through the evaluation of rescheduling options and cash flow management. To enhance the performance monitoring of treasury activities, local indicators have also been set and are used.

9. Equality implications

None directly relating to this report.

10. Consultation

The strategy has been approved by the finance treasury management panel, an internal governance arrangement comprising the CFO, Deputy CFO and Corporate Financial Systems and Treasury Manager.

Background papers

Various financial working papers.
Draft Corporate Revenue Budget and Capital Programme 2009/10 to 2011/12 - Cabinet 14.01.09 and annual review of treasury management policy statement and annual report on treasury management activity for 2007/8 – Cabinet 17.09.08.

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APPENDIX A

TREASURY MANAGEMENT AND INVESTMENT STRATEGIES 2009/10 ONWARDS

Walsall Council has a successful track record of effective treasury management, securing low cost borrowing to fund capital investment. Our aim is to continue to do so within the requirements of the prevailing policies and codes of practice.

In order to achieve our aim:

1. All borrowing and/or investment activity will be carried out in accordance with the approved treasury management strategy and treasury policy statements and within approved prudential indicators, having the highest regard for prudence, affordability and sustainability in the longer term.

2. Appropriate use will be made of the Code for capital investment within approved prudential indicators and subject to medium term affordability.

Specific objectives have been developed to measure and guide borrowing and investment activities. These being:

BORROWING OBJECTIVES

Our borrowing objectives are:

- To minimise the revenue costs of debt whilst maintaining a balanced loan portfolio
- To manage the council's debt maturity profile, ensuring no single future year has a disproportionate level of repayments
- To maintain a view on current and possible future interest rate movements and borrow accordingly
- To monitor and review the balance between fixed and variable rate loans against the background of interest rate levels and prudential indicators.

Specific Borrowing Objectives

- Full compliance with the Prudential Code
- Actual debt as a proportion of operational debt range is maintained at between 80%- 95%
- Average interest rate for internally managed debt will be less than 4.7%
- Average interest rate for total debt (including other local authority debt) will be less than 4.85%
- Average maturity date between 20 and 25 years
- Capital financing costs as a percentage of the government's assumed level of Walsall's capital financing costs < 90%
- The gearing effect on capital financing estimates of 1% increase in interest rates increase must not be greater than 5%.

KEY OBJECTIVES FOR INVESTMENT

- The general policy objective for this council is the prudent investment of its treasury balances
- The council's investment priorities are:
    - The security of capital and
    - Liquidity of its investments.
- All investments will be in sterling
- The council will aim to achieve the optimum return on its investments commensurate with the proper levels of security and liquidity.

Specific Investment Objectives

- Average interest rate received on short term investment to be > 2.5 %
- Average interest rate received on STI Versus 7 day Libid rate – 0.1%
- Average rate on all investments >3.5%
- % daily bank balances within a target range of 98%
- A maximum of £25m is invested over a period over 365 days.

Counter Party Principles

Approved Organisations for Investments

Only organisations that are eligible to receive investments from local authorities may be used.

The maximum limit for investment with any single organisation shall be no more than £15 million, with the exact amount in accordance with each individual institution's credibility and Credit Rating:

- Only invest in organisations we are familiar with
- Only invest in products we understand.

Banks and Institutions with a national credit rating of 1 will only be used.

Unrated Building Societies may be used providing reference to and analysis of their Size, Profitability and Proportion of free capital is undertaken and proves satisfactory.
Specified and non specified investments may be undertaken, specified investments being deposits for time periods less than 365 days and non specified being over 365 days.

ANNUAL MRP STATEMENT 2009/10

Under the Draft Local Authorities (Capital Finance and Accounting)(Amendment)(England) Regulations 2008, local authorities have a duty to produce an annual statement on its policy for making a minimum revenue provision (MRP).

For 2009/10 financial year the authority will be adopting the following policies in determining the MRP:

- For any capital expenditure carried out after 1 April 2008 being financed by supported borrowing the authority will again be adopting the regulatory method.

- For any capital expenditure carried out after 1 April 2008 being financed by unsupported borrowing the authority will be adopting the asset life method. This is where MRP will be based on the capital expenditure divided by a determined asset life to give equal annual instalments. It must be noted that once the asset life has been determined for this capital expenditure it cannot be altered in future years for this repayment.

The Regulatory Method is the calculation of MRP under the previous regulations. When MRP was set at a uniform rate of 4% of the adjusted Capital Financing Requirement. (CFR) on a reducing balance method (which in effect meant that MRP charges would stretch into infinity. This historic approach must continue for all capital expenditure incurred in years before the start of this capital financing regulations 2008.

APPENDIX B

PRUDENTIAL INDICATORS FOR 2009/10, 2010/11 & 2011/12

National and local indicators that will be monitored are detailed below. Their aim is to ensure the three principles contained within the prudential code are complied with, i.e.: affordability, prudence and sustainability.

National Prudential Indicators

Table 1 details the proposed national prudential indicators for Walsall council from 2009/10 to 2011/12. More details on prudential indicators 11 and 12 are shown in table 2.

Table 1: National Prudential Indicators 2009/10 to 2011/12

No.	Indicator	2009/10	2010/11	2011/12
PCI 1	**Total capital expenditure**	60,812	56,404	18,526
Reduces in later years due to uncertainty on the level of future grants and other resources.				
PCI 2	**Estimates of the ratio of financing costs to the net revenue stream**	9.9%	9.9%	9.7%
Compared to other councils Walsall's is very low, most financing costs will continue to be funded from central Government. The local indicator of comparison of the unsupported financing costs to revenue stream (L3) provides more appropriate information on the level of costs funded from council's own resources.				
PCI 3	**Estimates of the council tax that would result from the expenditure plans.**	£14.73	£4.99	£2.01
This is a notional amount indicating the amount of council tax band D that is affected by unsupported borrowing (USB).				
PCI 4	**Estimates of capital financing requirement.**	274,537	287,793	286,620
This represents the underlying level of borrowing needed to finance historic and future capital expenditure. To ensure that net borrowing will only fund capital, except in the short term, net external borrowing should not exceed the total capital financing requirement (CFR) in the preceding year plus estimated capital financing needs for the current and next two years.				
PCI 5	**Authorised limit for external debt.**	301,991	316,572	315,282
The council may not breach the limit it sets, so it is important to allow prudent room for uncertain cash flow movements and borrowing in advance of future need.				
PCI 6	**Operational boundary for external debt.**	274,537	287,793	286,620
This has been set at the level of the capital financing requirement.				
PCI 7	**Net Borrowing exceeds Capital Financing Requirement**	**No**	**No**	**No**
The CFR represents the underlying level of borrowing needed to finance historic capital expenditure. Actual net borrowing should be lower than this because of strong positive				

cash flow and balances. It would be a cause for concern if net borrowing exceeded CFR.				
PCI 8	**Compliance with CIPFA Code of Practice for TM in the Public Services.**	**Yes**	**Yes**	**Yes**
To ensure that treasury management activity is carried out within best professional practice**.**				
PCI 9	**Upper limits on fixed interest rate exposures.**	**95%**	**95%**	**95%**
The council cannot control interest rates, but a relatively high degree of interest cost stability can be achieved by limiting its exposure to variable rates and by managing the long-term debt maturity profile so that not too much fixed rate debt will mature in any year.				
PCI 10	**Upper limits on variable interest rate exposures. 3.**	**45%**	**45%**	**45%**
See comment under PCI 9.				
PCI 11	**Lower limits for the maturity structure of borrowings: 4.**		**See Table 2**	
Stability can also be managed by the long-term debt maturity profile so that not too much fixed rate debt will mature in any year.				
PCI 12	**Upper limits for the maturity structure of borrowings:**		**See Table 2**	
See comment under PCI 9.				
PCI 13	**Upper limit for principal sums invested for periods longer than 364 days.**	**£25,000,000**	**£25,000,000**	**£25,000,000**
The council is at risk when lending temporarily surplus cash. The risk is limited by investing surplus cash in specified investments and by applying lending limits and high credit worthiness. These are kept under constant review.				

Table 2 Prudential Indicators: Additional Information	**2009/10**	**2010/11**	**2011/12**
PCI 11. Lower limits for the maturity structure of borrowings:			
- Under 12 Months	0%	0%	0%
- 12 months and within 24 months	0%	0%	0%
- 24 months and within 5 years	0%	0%	0%
- 5 years and within 10 years	10%	10%	10%
- 10 years and above	40%	40%	40%
PCI 12. Upper limits for the maturity structure of borrowings:			
- Under 12 Months	15%	15%	15%
- 12 months and within 24 months	20%	20%	20%
- 24 months and within 5 years	25%	25%	25%
- 5 years and within 10 years	50%	50%	50%
- 10 years and above	85%	85%	85%

Local Prudential Indicators: Table 3 sets out local prudential indicators proposed for 2009/10 to 2011/12.

Table 3: Local Prudential Indicators 2009/10 to 2011/12				
No.	**Indicator**	**2009/10**	**2010/11**	**2011/12**
L.1	**Full compliance with Prudential Code**	**Yes**	**Yes**	**Yes**
L.2	**Average length of debt**	**20 to 25 years**	**20 to 25 years**	**20 to 25 years**
This is a maturity measure and ideally should relate to the average lifespan of assets.				
L.3	**Ratio of unsupported financing costs to revenue stream**	1.9%	2.5%	2.5%
Provides an indication of the significance of USB in relation to the total net budget. A low % means that the council is using low level of own resources to fund USB.				
L.4	**Actual debt versus operational debt**	94.1%	92.0%	93.0%
This assists the monitoring of the authority's debt position.				
L.5	**Average interest rate of debt excluding OLA** **Average interest rate of debt including OLA**	**4.70%** **4.85%**	**4.70%** **4.85%**	**4.70%** **4.85%**
This is a recognised measure of debt management performance. The measure should be as low as possible. Other Local Authority debt (OLA) is managed on our behalf by Dudley council				
L.6	**Gearing effect on capital financing costs of 1% increase in interest rate**	**5%**	**5%**	**5%**
This relates risk management principles to the monitoring of the TM strategy. It measures the effect of a change in national interest rates and the effect it may have on the capital financing costs.				
L.7	**Average interest rate received on short term investment**	**2.5%**	**3.0%**	**3.25%**
A recognised PI for measuring the performance of return on investments.				
L.8	**Average interest rate received on STI Versus 7 day LIBID rate**	**0.10%**	**0.10%**	**0.10%**
The council aims to be gain interest on surplus funds higher than the 7 day LIBID rate. This measuring performance in a changing economic context. .				
L.9	**Average rate on all investments**	**3.5%**	**3.1%**	**3.3%**
As L6. but includes investments longer than 364 days.				
L.10	**% daily bank balances within target range**	**98%**	**98%**	**98%**
This measures how good our daily cash flow prediction is. A figure of 98% indicates high level of accuracy.				

The monitoring of the indicators supports budget monitoring and will be undertaken monthly and considered quarterly by the finance treasury management panel that reports to the finance service's senior management team including the Chief Finance Officer.

APPENDIX C

TREASURY LIMITS AND BORROWING LIMITS

It is a statutory duty under S.3 of the Local Government Act 2003 and supporting regulations, for the council to determine and keep under review how much it can afford to borrow. The amount so determined is termed the "affordable borrowing limit". In England and Wales the Authorised Limit represents the legislative limit specified in section 3 of the Local Government Act 2003.

The council's long term borrowing position at 31.12.08 comprised:

Table 1 – Summary of Borrowing Portfolio as 31.12.08				
		£ m	£ m	Average rate %
Fixed rate funding	PWLB	125,282		4.77%
	Market	107,000	232,282	4.63%
Variable rate funding	PWLB	-		
	Market	15,000	15,000	4.95%
Other Long term Liabilities	OLA	27,254		6.70%
	Waste disposal	- 10,289	16,965	6.70%
			264,247	4.83%

The council must have regard to the Prudential Code when setting the authorised limit, which essentially requires it to ensure that total capital investment remains within sustainable and affordable limits and, in particular, that the impact upon its future council tax is 'acceptable'.

Whilst termed an "affordable borrowing limit", the capital plans to be considered for inclusion incorporate financing by both external borrowing and other forms of liability, such as credit arrangements. The authorised limit is to be set on a rolling basis for the forthcoming financial year and two indicative successive financial years.

Table 2 shows the estimate of mainstream resources from 2009/10 to 2011/12 to support the capital programme. It shows a borrowing requirement of £36.4m over the next 3 years. During this period the authority plans to set aside for £37.7m debt repayment so there is not currently expected to be any net increase in borrowing.

Table 2 – Estimate of Mainstream Resources 2008/9 to 2012/2013 (£M)			
Capital Resources	**2009/10**	**2010/11**	**2011/12**
Supported borrowing	6.588	5.104	2.762
Unsupported borrowing	16.928	4.515	1.941
Total borrowing	**23.516**	**9.619**	**4.703**
Capital receipts	1.137	-	-
Other one off resources	0.700	0.700	0.500
Total	**25.353**	**10.319**	**5.203**

USE OF UNSUPPORTED BORROWING

The Prudential Code allows councils to raise finance for capital expenditure without Government consent where they can afford to service the costs of the additional debt without government support. Prior to this local authorities' capital expenditure was constrained by government borrowing approvals. Shortfalls in government funding for capital schemes were often made up by the use of capital receipts, which in some circumstances could be lost if not used. Walsall council has had a more planned use of capital receipts over the medium term and analyses whether it is more appropriate to use unsupported borrowing for capital programme shortfalls.

We are in a favourable position to take advantage of unsupported borrowing as:

- Compared to other councils, Walsall Council has a very low average rate on its debt - 4.69%,
- Yet the revenue settlement assumes an average borrowing rate of around 5.5% in the calculation of formula grant, and

Therefore, once again it is proposed to adopt a flexible approach to funding of the 2009/10 capital programme by using unsupported borrowing (USB) of up to £16.2. This will secure the best value for money option and optimize use of resources. For 2009/10 onwards, the use of USB is projected and included in the capital programme (see **Table 3).**

Table 3 – Unsupported Borrowing 2009/10 to 2011/12			
	2009/10 £m	**2010/11 £m**	**2011/12 £m**
ICT transformation	4.665	0.358	0.268
Debt capacity – general support	12.263	4.157	1.673
Total	16.928	4.515	1.941

In addition to the USB allocated to specific schemes, a further £1m will be earmarked for projects that may come along throughout the year that can demonstrate with thorough option appraisal that they are self funding. Prudential Indicator **PCI 3** estimates the annual effect on council tax of the use of USB for general support. The ICT transformation is a project that is to be funded by savings streams generated and therefore has no additional pressure on council tax.

APPENDIX D

Economic Outlook and Interest Rate Forecast

The council has appointed Sector Treasury Services as treasury adviser to the council and part of their service is to assist the council to formulate a view on interest rates. Below draws together a number of current City forecasts for short term (Bank Rate) and longer fixed interest rates.

Sector interest rate forecast –

	Q/E1 2009	Q/E2 2009	Q/E3 2009	Q/E4 2009	Q/E1 2010	Q/E2 2010	Q/E3 2010	Q/E4 2010	Q/E1 2011	Q/E2 2011	Q/E3 2011	Q/E4 2011	Q/E1 2012
Bank rate	0.50%	0.50%	0.50%	0.50%	0.50%	0.75%	1.00%	1.25%	1.75%	2.50%	3.25%	3.75%	4.00%
5yr PWLB rate	2.50%	2.25%	2.15%	2.15%	2.15%	2.45%	2.80%	3.15%	3.65%	3.95%	4.20%	4.45%	4.60%
10yr PWLB rate	3.10%	2.75%	2.55%	2.55%	2.55%	2.85%	3.25%	3.65%	4.15%	4.40%	4.70%	4.75%	4.85%
25yr PWLB rate	4.00%	3.95%	3.95%	3.95%	4.00%	4.15%	4.35%	4.45%	4.60%	4.85%	4.95%	5.00%	5.05%
50yr PWLB rate	3.85%	3.80%	3.80%	3.80%	3.85%	3.90%	4.00%	4.25%	4.40%	4.70%	4.80%	4.95%	5.00%

Sector's current interest rate view is that Bank Rates:

- **Will fall from current levels because of the intensifying global recession**
- **Will be 2.50% at financial year end 2008 and will reach a low point of 1.75% in Q1 2009**
- **It will then stay unchanged at 1.75% before edging up to 2.00% in Q2 2010**
- **It will then rise by 0.25% in the next quarter and then by 0.50% per quarter until it ends the forecast period in Q3 2011 at 4.25%**
- **Even at these levels there is downside risk in 2009 to the forecast while there is upside risk in 2010 should the lower interest rates turn the economy around more quickly than currently anticipated.**

ECONOMIC BACKGROUND

Introduction

- The sub prime crisis of early 2008 was supplanted by the banking crisis of autumn 2008. The world banking system came near to collapse and governments around the world were forced to recapitalise and rescue their major banks. The resulting dearth of lending from banks anxious to preserve capital led to economic forecasts being sharply reduced and recession priced into markets. This in turn led to sharp falls in oil and other commodity prices with the result that inflation, which in the UK was running at over 5%, became yesterday's story and recession fears drove interest rate sentiment and policy. A co-ordinated global interest rate cut of 50bp took place on 8th October 2008. Forecasts in the UK were for further sharp cuts in interest rates as recession hove into view.

International

- Early in 2008 the US economy was being badly affected by the housing market slump. Interest rates were at 2% and inflation was being dragged higher by the inexorable rise in commodity prices. The ECB was very concerned about rising inflation and less about the state of the economy.
- The second quarter of 2008/9 was torn between inflation worries on the one hand, with oil rising towards $150 per barrel, and the deteriorating economic outlook on the other.
- In the second and third quarters of the year the financial crisis erupted and escalated as the world became aware of the extent of the sub-prime fiasco and the impact it was having on institutions that had invested in these issues.
- In September Fannie Mae/Freddie Mac (the mortgage banks) and AIG, the insurance giant, had to be bailed out by the US Federal Government.
- Then in mid September, Lehman Bros., the investment bank, was allowed to fail. This triggered a domino effect with other banks and financial institutions having to be rescued or supported by governments around the world.
- After the collapse into receivership of the Icelandic banks in early October, other countries then started to feel the strain and a number had to approach the IMF for support.
- Eventually even the Asian 'Tiger' economies were affected, including India and China, and it became clear that the crisis had become a global one and no country was insulated from it.
- The financial crisis had therefore precipitated an economic crisis and there was a co-ordinated global interest rate cut with the Fed, ECB and MPC all cutting rates by 50bp on 8th October. The Fed subsequently cut rates again by 50bp to 1% on 29th October and again on 16 December to a band of 0.0% to 0.25% in an attempt to stave off the oncoming recession. Inflation was yesterday's problem.
- On 4th November the USA elected Barack Obama as President with little immediate financial impact.
- The ECB reduced rates again on 6th November by 50bp and by its biggest ever cut of 75bp on 4 December to reach 2.5%.

UK

- GDP: growth was already slowing in 2008 from 2007 before the full impact of the credit crunch was felt. Earlier in 2008 GDP was 2.3% whereas in the autumn the figure fell back to -0.3% and was then expected to continue to be negative going into 2009.
- Wage inflation remained relatively subdued as the Government kept a firm lid on public sector pay. Private sector wage growth was kept in check by the slowing economy.
- Growth slowed across the economy and unemployment rose throughout the year with forecasts of 2 million unemployed by the end of the financial year and continuing to increase thereafter through 2010.
- Notwithstanding the pressures on household finances consumer spending still continued at a reasonable clip although the trend was slowing as the year progressed.
- Bank lending came to a virtual standstill in the autumn as the credit crunch tightened its grip and various banks internationally had to be rescued, or supported, by their governments.
- The Government and Bank of England supplied massive amounts of liquidity to the banking market in an attempt to reignite longer interbank lending.

- The Government took action in September to either supply finance itself to recapitalise some of the major clearing banks or to require the others to strengthen their capital ratios by their own capital raising efforts. This was so that these banks would be seen to have sufficient reserves to last through the coming recession with its inevitable increase in bad loans etc.
- The housing market also came to a virtual standstill as lenders demanded larger deposits and higher fees. House sales and prices both dropped sharply.
- Government finances deteriorated as income from taxation dropped as the economy slowed and the cost of the bailout of the banks was added to the deficit.
- U.K. equity prices declined sharply in the 3rd and 4th quarters as the impending recession was priced into the markets. Prices hit five year lows and volatility was extremely high.
- The story of 2008 has been the credit crunch, the banking crisis and the change in economic outlook from slow growth to outright recession. After the initial concerns about the impact of the credit crunch in the earlier part of 2008 it appeared as though the storm had been weathered. The MPC had been very concerned about CPI inflation, which had been rising sharply on the back of higher commodity and food prices. Bank Rate reached a peak of 5.75% in July 2007 after which cuts of 0.25% occurred in December 2007 and February and April 2008 before the major cuts in the autumn. The economic data had been indicating a slowing economy for some while but it was not sufficiently weak to force the MPC into another cut. It was the strength of the banking crisis, pre-empted by the collapse of Lehmans in New York that eventually drove the MPC to cut interest rates by 50bp on October 8th in concert with the Federal Reserve, the ECB and other central banks. It was then appreciated that the economic downturn would be much more severe than previously thought and interest rates were subsequently slashed by 150bps on 6 November, 100bps on 4 December and 50 bps on 8 January 2009.
- The LIBOR spread over Bank Rate has also been a feature, and a concern, of 2008/9. Because of the credit fears and the reluctance of lenders to place cash for long periods 3 month LIBOR (this is the London Inter Bank Offer Rate – the rate at which banks will lend to one another) has been substantially higher than Bank Rate. This has meant that the MPC's power over monetary policy has been eroded by the widening of this spread between LIBOR and Bank Rate and it has therefore had a limited ability to bring relief to hard pressed borrowers through lower interest rates. However, the power of the Government over the semi nationalised clearing banks had considerable impact in enforcing pro rata reductions to the 150 bps Bank Rate cut in November on some borrowing rates.
- The Government has abandoned its 'golden rule'. The pre Budget Report on 14 November revealed the Government's plans for a huge increase in Government borrowing over coming years as a result of falling tax revenues and also due to tax cuts and increases in Government expenditure in the short term designed to help stimulate economic growth to counter the recession.

APPENDIX E

EXPLANATION OF TECHNICAL TERMS USED IN THIS REPORT AND ITS APPENDICES

TERM	DEFINITION
Authorised Limit	Level of debt set by the council that must not be exceeded.
Bond	A government or public company's document undertaking to repay borrowed money usually with a fixed rate of interest.
Borrowing	Obtaining money for temporary use that has to be repaid.
Capital receipts	The proceeds from the disposal of land or other assets. Capital receipts can be used to fund new capital expenditure but cannot be used to finance revenue expenditure
Cash flow Management	The management of the authority's receipts and payments to ensure the authority can meet its financial obligations.
Counter party limits	Maximum amount that the council may lend to other institutions will vary according to size and credit rating of other intuitions.
Dividends	Sum to be payable as interest on loan.
ECB	European Central Bank
Investments	The employment of money with the aim of receiving a return.
LIBID	London Interbank Bid Rate (the rate that banks are willing to borrow from other banks)
LIBOR	London Interbank Offered Rate (the rate that banks offer to lend to other banks)
Liquidity	How easily an asset including investments may be converted to cash.
Long Term Borrowing	Borrowing of money for a term greater than one year.
Long Term Liabilities	Amounts owed by the council greater than 12 months old.
Market convention	The rules and regulations by which all brokers and dealers should abide by. It includes standards of practice and calculation convention for interest. They are defined in the London Code of Conduct ("The London Code") published by the Bank of England.
MPC	Monetary Policy Committee – group that sets the bank base rate for the Bank of England
Non specified investments	Investments with a maturity exceeding a year
Operational Boundary	An indicator of the level day the authority expects during day to day treasury management activities
Other Local Authority Debt	Debt that is owed by one local authority to another local authority.
Prudential Code	A framework of policies and working practices to ensure that loc authorities' capital investment plans are affordable, prudent ar sustainable.
Regulator Method	Principle of calculating the amount of money to be set aside for the repayment of debt as defined by the government.
Short Term Borrowing	Borrowing of money for a term of up to 364 days.
Stock	Subscribed capital of trading company, or public debt of nation, municipal corporation etc regarded as transferable property
Temporary borrowing	Borrowing of money for a term of up to 364 days.
Treasury management	The management of the local authority's cash flows, its borrowings an its investments, the management of associated risks, and the pursuit the optimum performance or return consistent with those risks.

Treasury Policy Statement	A statement of key policies that an organisation follows in pursuit of effective treasury management, including borrowing limits and strateg
Variable debt	This is money that has been borrowed at a variable interest rate, and as such is subject to interest rate changes.
Unsupported borrowing	Borrowing taken through the remit of the Prudential Code for which th council will not receive any government funding and will fund from own resources.