Appendix 3

Borrowing Strategy and Indicators 2016/17

The capital expenditure plans of the council are set out in the Capital Programme Report approved by Policy & Resources Committee on 11 February 2016 and full Council on 25 February 2016. The treasury management function ensures that the Council's cash is organised in accordance with the relevant professional codes so that sufficient cash is available to meet the capital expenditure plans. This involves both the organisation of the cash flow and where required, the organisation of appropriate borrowing facilities.

As a response to the economic climate, the Council had previously been following a strategy of repaying debt and funding its borrowing requirement through utilising cash balances which were supporting the Council's reserves and balances (known as under borrowing). This was a prudent strategy which has allowed the council to minimise the cost of carry on its borrowing, and reduce its counterparty exposure risk.

This strategy was amended in 2015/16; Table 1 below shows the net borrowing requirement (i.e. after allowing for provision to repay debt) and the level of reserves that is funding the borrowing requirement (under borrowing) over the next three years. The table demonstrates that the Council is currently funding its borrowing requirement with approximately £53.0m of reserves and balances and cash flows but this figure will decline in subsequent years. The 2016/17 budget uses certain reserves to meet one off costs, and this will reduce the availability of cash backed resources to fund the borrowing requirement. Additionally, the Capital Investment Plans set out in the Capital Programme Report presented to Policy & Resources Committee on 11 February 2016 shows an expectation of large capital borrowing requirement over the next 3 years. These factors increase the need to borrow externally to ensure the availability of cash to meet these commitments.

Subsequently, officers, in consultation with the council's treasury advisors, set some trigger points for taking on new borrowing during 2015/16. Both trigger rates set have been met, which has led to the council undertaking two tranches of £5.000m borrowing at very attractive rates. To further reduce the under borrowing position, the Financing budget has been prepared to allow for a further £10.000m of borrowing to be undertaken over the next two years with the first £5.000m forecast for 2016/17. As a result of rates falling to historical lows again in February 2016, the £5.000m within 2016/17 budget was bought forward into 2015/16 to secure borrowing at very low cost. Officers will consider bringing forward the 2017/18 tranche of £5.000m if it is considered that the long term benefits of doing so will outweigh any short term cost of carrying the debt for an additional year.

Table 1 – Projected borrowing requirement (excluding PFIs and other long term liabilities) and under borrowing position

	2015/16 £'m	**2016/17 £'m**	**2017/18 £'m**	**2018/19 £'m**
General Fund				
Borrowing Requirement - start of the year	162.7	180.9	188.7	213.4
Increase in borrowing requirement	25.2	15.9	33.2	44.2
Provision to repay debt	(7.0)	(8.1)	(8.5)	(10.4)
Borrowing Requirement - end of the year	180.9	188.7	213.4	247.2
	127.9	140.4	179.4	222.0

Actual Borrowing Under/(over) borrowing position	**53.0**	**48.3**	**34.0**	**25.2**

Housing Revenue Account				
Borrowing Requirement - start of the year	115.9	117.4	140.5	150.7
Increase in borrowing requirement	4.5	26.1	10.7	
Provision to repay debt	(3.0)	(3.0)	(0.5)	(0.9)
Borrowing Requirement - end of the year	117.4	140.5	150.7	149.8
Actual Borrowing	117.4	140.5	150.7	149.8
Under/(over) borrowing position	**(0.0)**	**(0.0)**	**(0.0)**	**(0.0)**

Interest rate risk

The under borrowing position illustrated in Table 1 above demonstrates the extent to which the council is exposed to interest rate risk. As Appendix 2 outlines, borrowing rates have been historically low, and expected to rise in the medium term.

Officers will monitor market interest rates and adopt a pragmatic approach to changing circumstances in order to minimise the financial impact any adverse movement on interest rates on the Council's debt and investment portfolios;

- Long term borrowing will be postponed where it was felt there was a significant risk of a sharp fall in long term interest rates
- The borrowing position will be re-appraised and considered where it was felt that there was a significant risk of a sharp rise in long term interest rates with the likely action that new long term borrowing will be raised whilst interest rates are expected to be lower than in subsequent years.

Consideration will be given to the following borrowing options, which will be assessed appraised to seek the most appropriate option at the time:

- Short term borrowing (i.e. repayable for less than a year)
- PWLB variable rate loans for up to 10 years
- PWLB fixed rate loans up to 50 years
- Market loans that offer comparable or better terms to that set out above
- Bond issues by the Municipal Bonds Agency where they offer comparable or better terms than the other options outlined above.

The length and type of borrowing will depend upon factors including prevailing interest rates, interest rate expectations and the maturity profile of the council's existing portfolio.

Policy on Borrowing in advance of need

The council will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. With long term fixed interest rates at risk of being higher over the next few years (see Table A, Appendix 2) officers will consider the borrowing in advance of need in order to minimise the expected cost of borrowing. Any decision to borrow in advance will be within the forward approved Capital Financing Requirement estimates, and will be considered carefully to ensure value for money can be demonstrated and that the Council can ensure the security of such funds.

Risks associated with any borrowing in advance of activity will be subject to prior appraisal and subsequent reporting through the Treasury Management reporting process.

Debt Rescheduling

Table 2 shows the level of maturing debt over the next three years. The council has a number of loans where the lender may vary the interest rate, after which the council would have the right to repay. Based on the latest interest rate projections (Table A, Appendix 2), it is considered very unlikely that these loans would be repaid early – however, debt that is repaid early will have implications on both the GF and HRA debt portfolios.

	2016/17	2017/18	2018/19
Maturing Debt	£3.7m	£1.7m	£2.4m
Debt subject to early repayment options	£55.0m	£5.0m	£0.0m
Total debt at risk of maturity	£58.7m	£6.7m	£2.4m

As short term borrowing rates will be considerably cheaper than longer term fixed interest rates, there may be potential opportunities to generate savings by switching from long term debt to short term debt. However, these savings will need to be considered in the light of the current treasury position and the size of the cost of debt repayment (premiums incurred).

The reasons for any rescheduling to take place will include:

- the generation of cash savings and / or discounted cash flow savings;
- helping to fulfil the treasury strategy;
- enhance the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

Consideration will also be given to identify if there is any residual potential for making savings by running down investment balances to repay debt prematurely as short term rates on investments are likely to be lower than rates paid on current debt.

All rescheduling will be reported to Policy & Resources Committee within the normal Treasury Management reporting process and/or Target Budget Management process following its action.

Municipal Bonds Agency

It is likely that the Municipal Bond Agency, currently in the process of being set up, will be offering loans to local authorities in the near future. It is also hoped that the borrowing rates will be lower than those offered by the Public Works Loan Board (PWLB). The council will consider borrowing from the agency if the terms offered are in line with the council's borrowing needs.

Borrowing prudential Indicators

The following borrowing indicators were approved as part of the budget report at full Council on 25 February 2016.

Limits to borrow activity

Prudential Indicators D1, D2 and D3 set the limits of external borrowing

The operational boundary is the point at which external debt is not expected to be exceeded. The Authorised Limits is a control on the maximum level of borrowing, defined as the statutory limit under Section 3 (1) of the Local Government Act 2003. External debt is prohibited beyond the Authorised Limit and any revision to the limit would need approval by full Council.

Prudential indicators (D1) "Authorised limit" and (D2) "Operational boundary" 2016/17 to 2018/19

	2016/17 Estimate		2017/18 Estimate		2018/19 Estimate	
Authorised limit						
- Borrowing	£350m		£385m		£420m	
- Other l/term liabilities	£54m	£404m	£52m	£437m	£50m	£470m
Operational boundary						
- Borrowing	£338m		£373m		£407m	
- Other l/term liabilities	£54m	£392m	£52m	£425m	£50m	£457m

Separately, the Council is also limited to a maximum HRA CFR through the HRA self financing regime. This limit is currently:

Prudential indicators (D3) HRA Limit on indebtedness 2016/17 to 2018/19

	2016/17 Estimate	2017/18 Estimate	2018/19 Estimate
HRA limit on indebtedness	£156.8m	£156.8m	£156.8m
HRA Debt	£139.2m	£149.3m	£148.4m
Headroom	£17.6m	£7.5m	£8.4m

Treasury management Indicators

Prudential Indicators E2, E2a and E3 below are intended to manage the risk of adverse movement in interest rates and risk associated with refinancing maturing debt.

Prudential indicator (E2) – Upper limits on net debt interest rate exposure 2016/17 to 2018/19

	2016/17	2017/18	2018/19
Upper limit on fixed interest rate exposure	108%	108%	107%

Upper limit on variable interest rate exposure	43%	43%	43%

The percentages in Indicator E2 are calculated on the net outstanding principal sums (i.e. net of investments). The upper limit of 109% is a consequence of the council maintaining an investment portfolio. Indicator E2a exemplifies the indicator over borrowing and investment.

Prudential indicator (E2a) (supplemental) – Upper limits on interest rate exposure 2016/17 to 2018/19

	2016/17	2017/18	2018/19
Upper limit on borrowing – fixed rate exposure	100%	100%	100%
Upper limit on borrowing – variable rate exposure	40%	40%	40%
Upper limit on investments – fixed rate exposure	100%	100%	100%
Upper limit on investments – variable rate exposure	100%	100%	100%

Prudential indicator (E3) – Upper and lower limits on the maturity structure of borrowing 2016/17

	Upper limit	Lower limit
under 12 months	40%	0%
12 months and within 24 months	40%	0%
24 months and within 5 years	50%	0%
5 years and within 10 years	75%	0%
10 years and above	100%	40%