**Appendix 1**

# TREASURY MANAGEMENT POLICY AND STRATEGY 2024/25

East Sussex County Council

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# 1. INTRODUCTION

## *1.1 Background*

The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in counterparties or instruments commensurate with the Council's risk appetite, providing adequate liquidity initially before considering investment return.

The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer-term cash flow planning, to ensure that the Council can meet its capital spending obligations. This management of longer-term cash may involve arranging long or short-term loans or using longer-term cash flow surpluses. On occasion, when it is prudent and economic, any debt previously drawn may be restructured to meet Council risk or cost objectives.

The contribution the treasury management function makes to the authority is critical, as the balance of debt and investment operations ensure liquidity or the ability to meet spending commitments as they fall due, either on day-to-day revenue or for larger capital projects. The treasury operations will see a balance of the interest costs of debt and the investment income arising from cash deposits affecting the available budget. Since cash balances generally result from reserves and balances, it is paramount to ensure adequate security of the sums invested, as a loss of principal will in effect result in a loss to the General Fund Balance.

CIPFA defines treasury management as:

*"The management of the local authority's borrowing, investments and 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."*

## *1.2 Reporting Requirements*

### *1.2.1 Capital Strategy*

The CIPFA 2021 Prudential and Treasury Management Codes require all local authorities to prepare a capital strategy report, to provide the following:

- a high-level long-term overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services
- an overview of how the associated risk is managed
- the implications for future financial sustainability

The aim of the capital strategy is to ensure that all elected members on the Council fully understand the overall long-term policy objectives and resulting capital strategy requirements, governance procedures and risk appetite.

This capital strategy is reported separately from the Treasury Management Strategy Statement; non-treasury investments will be reported through the former. This ensures the separation of the core treasury function under security, liquidity and yield principles, and the policy and commercialism investments usually driven by expenditure on an asset.

### *1.2.2 Treasury Management reporting*

The Council is currently required to receive and approve, as a minimum, three main treasury reports each year, which incorporate a variety of policies, estimates and actuals.

a. **Prudential and treasury indicators and treasury strategy** (this report) - The first, and most important report is forward looking and covers:

- the capital plans, (including prudential indicators);
- a minimum revenue provision (MRP) policy, (how residual capital expenditure is charged to revenue over time);
- the treasury management strategy, (how the investments and borrowings are to be organised), including treasury indicators; and
- an investment strategy, (the parameters on how investments are to be managed).

b. **A mid-year treasury management report** – This is primarily a progress report and will update members on the capital position, amending prudential indicators as necessary, and whether any policies require revision.

c. **An annual treasury report** – This is a backward looking review document and provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

*This Council delegates responsibility for implementation and monitoring treasury management to Cabinet and responsibility for the execution and administration of treasury management decisions to the Section 151 Officer. Cabinet therefore receives the Mid-Year and Annual treasury reports in December each year.*

The above reports are required to be adequately scrutinised before being recommended to the Council. This role is undertaken by the Audit Committee.

d. **Quarterly reports** – In addition to the three major reports detailed above, from 2023/24 quarterly reporting is incorporated into the quarterly Council Monitoring process.

### *1.3 Treasury Management Strategy for 2024/25*

The strategy for 2024/25 covers two main areas:

**Capital issues**

- the capital expenditure plans (section 2) and the associated prudential indicators (Annex C);
- the minimum revenue provision (MRP) policy (Section 3).

**Treasury management issues**

- the current treasury position (section 1.5);
- treasury indicators which limit the treasury risk and activities of the Council (Annex C);
- prospects for interest rates (Annex B);
- the borrowing strategy (section 2);
- policy on borrowing in advance of need (section 2.2);
- debt rescheduling (section 2.3);
- the investment strategy (section 4);
- creditworthiness policy (section 4.4); and
- the policy on use of external service provider (section 5.3).

These elements cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, DLUHC MRP Guidance, the CIPFA Treasury Management Code and DLUHC Investment Guidance.

### *1.4 Treasury Management Policy Statement*

The policies and objectives of the Council's treasury management activities are as follows:

i) This Council defines its treasury management activities as:

*'The management of the authority's investments and 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'.*

ii) This Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the Council, and any financial instruments entered into to manage these risks.

iii) This Council acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance management techniques, within the context of effective risk management.

### *1.5 Current Treasury Position*

A summary of the Council's borrowing & investment portfolios as at 30 November 2023 and forecast at the end of the financial year is shown in **Table 1** below:

| Table 1 | Actual at 30 November 2023 | | | Forecast to 31 March 2024 | | |
|---|---|---|---|---|---|---|
| | £'000 | % of portfolio | Average Rate | £'000 | % of portfolio | Average Rate |
| **Investments** | | | | | | |
| Banks | 129,000 | 48% | 5.39% | 130,000 | 54% | 5.40% |
| Local Authorities | 66,000 | 24% | 5.06% | 80,000 | 33% | 5.40% |
| Money Market Funds | 69,400 | 26% | 5.48% | 25,000 | 11% | 5.25% |
| CCLA Pooled Property Fund | 5,000* | 2% | 4.60% | 5,000 | 2% | 4.60% |
| **Total Investments** | **269,400** | **100%** | **5.32%** | **240,000** | **100%** | **5.37%** |
| | | | | | | |
| **Borrowing** | | | | | | |
| PWLB loans | 210,142 | 97% | 4.53% | 210,142 | 97% | 4.53% |
| Market loans | 6,450 | 3% | 4.25% | 6,450 | 3% | 4.25% |
| **Total external Borrowing** | **216,592** | **100%** | **4.52%** | **216,592** | **100%** | **4.52%** |

*£4,284,479 capital valuation 30 November 2023

## 2. BORROWING STRATEGY

The capital expenditure plans of the Council are set out in the Capital Strategy Report being considered by Full Council on 6 February 2024. 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 this service activity and Capital Strategy. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of appropriate borrowing facilities. The strategy covers the relevant treasury / prudential indicators, the current and projected debt positions, and the Annual Investment Strategy.

Any capital investment that is not funded from these new and/or existing resources (e.g. capital grants, receipts from asset sales, revenue contributions or earmarked reserves) increases the Council's need to borrow, represented by the Capital Financing Requirement (CFR). However, external borrowing does not have to take place immediately to finance its related capital expenditure: the Council can utilise cash being held for other purposes (such as earmarked reserves and working capital balances) to temporarily defer the need for external borrowing. This is known as 'internal borrowing'.

The Council's primary objective is to strike an appropriate balance between securing cost certainty, securing low interest rates.

### *2.1 Capital Prudential Indicators*

The Authority's capital expenditure plans are a key driver for Treasury Management activity. The output of the capital expenditure plans is reflected in the prudential indicators, which are designed to assist members' overview and confirm capital expenditure plans.

Tables 2 and 3 show the capital expenditure plans of the Authority, and the implications of these on the Capital Financing Requirement over the 3 year period to 2025/26.

The liability benchmark shown in section 2.3 measures the authority's external debt levels net of the external investments, with the inclusion of a liquidity buffer against the Authority's CFR projection. This measure assumes that the authority will internally borrow almost all its available cash balances held in reserves and balances, with an allowance ensure it is able to meet is cash obligations.

There are four components to the Liability Benchmark: -

1. **Existing loan debt outstanding**: the Authority's existing loans that are still outstanding in future years.
2. **Loans CFR**: this is calculated in accordance with the loans CFR definition in the Prudential Code and projected into the future based on approved prudential borrowing and planned MRP.
3. **Net loans requirement:** this will show the Authority's gross loan debt less treasury management investments at the last financial year-end, projected into the future and based on its approved prudential borrowing, planned MRP and any other major cash flows forecast.
4. **Liability benchmark (or gross loans requirement)**: this equals net loans requirement plus short-term liquidity allowance.

The Liability Benchmark has been produced below in section 2.3 and notes included to explain each element and the Authority's assumptions and forward view.

### *2.2 Borrowing Strategy for 2024/25*

The Council has been carrying an internal borrowing position since 2019/20, a policy which reduces cost and reduces investment counterparty risk as the Council are using cash from its own reserves to fund its borrowing requirement as opposed to entering into external borrowing.

There is £17m expected to be funded via borrowing in the 2023/24 Capital Programme. No new external borrowing is expected to be undertaken to fund this, and this will be funded through cash balances. This is expected to increase the Council's under-borrowed position compared to its CFR from £51m at 31 March 2023 to £64m by 31 March 2024.

The Council's Capital Programme 2024/25 to 2026/27 forecasts £262m of capital investment over the next three years with £168m met from existing or new resources. The increase in the Council's borrowing need over this period is therefore £94m as shown in **Table 2** below. Please note, this has been prepared using the programme **before** the corporate slippage risk factor has been applied.

| 2023/24 Projected £m | Table 2 | 2024/25 Estimate £m | 2025/26 Estimate £m | 2026/27 Estimate £m | Total £m |
|---|---|---|---|---|---|
| 80 | Capital Expenditure | 97 | 98 | 67 | 262 |
| (63) | **Financed by:** New & existing resources | (65) | (66) | (37) | (168) |
| **17** | **Borrowing Need** | **32** | **32** | **30** | **94** |

**Table 3** below shows the actual expected external borrowing against the capital financing requirement, identifying any under or over borrowing.

| 2023/24 Estimate £m | Table 3 | 2024/25 Estimate £m | 2025/26 Estimate £m | 2026/27 Estimate £m |
|---|---|---|---|---|
| 221 | External Debt at 1 April | 217 | 230 | 278 |
| (4) | Expected change in Debt | 13 | 48 | 20 |
| **217** | **External Debt at 31 March** | **230** | **278** | **298** |
| 272 | CFR* at 1 April | 281 | 305 | 328 |
| 17 | Borrowing need (Table 2) | 32 | 32 | 30 |
| (8) | MRP | (8) | (9) | (10) |
| **281** | **CFR* at 31 March** | **305** | **328** | **348** |
| **64** | **Under / (Over) borrowing** | **75** | **50** | **50** |

**CFR in Table 3 is the underlying need to borrow and excludes PFI and lease arrangements, which are included in the CFR figure in the Prudential Indicators in Annex C*

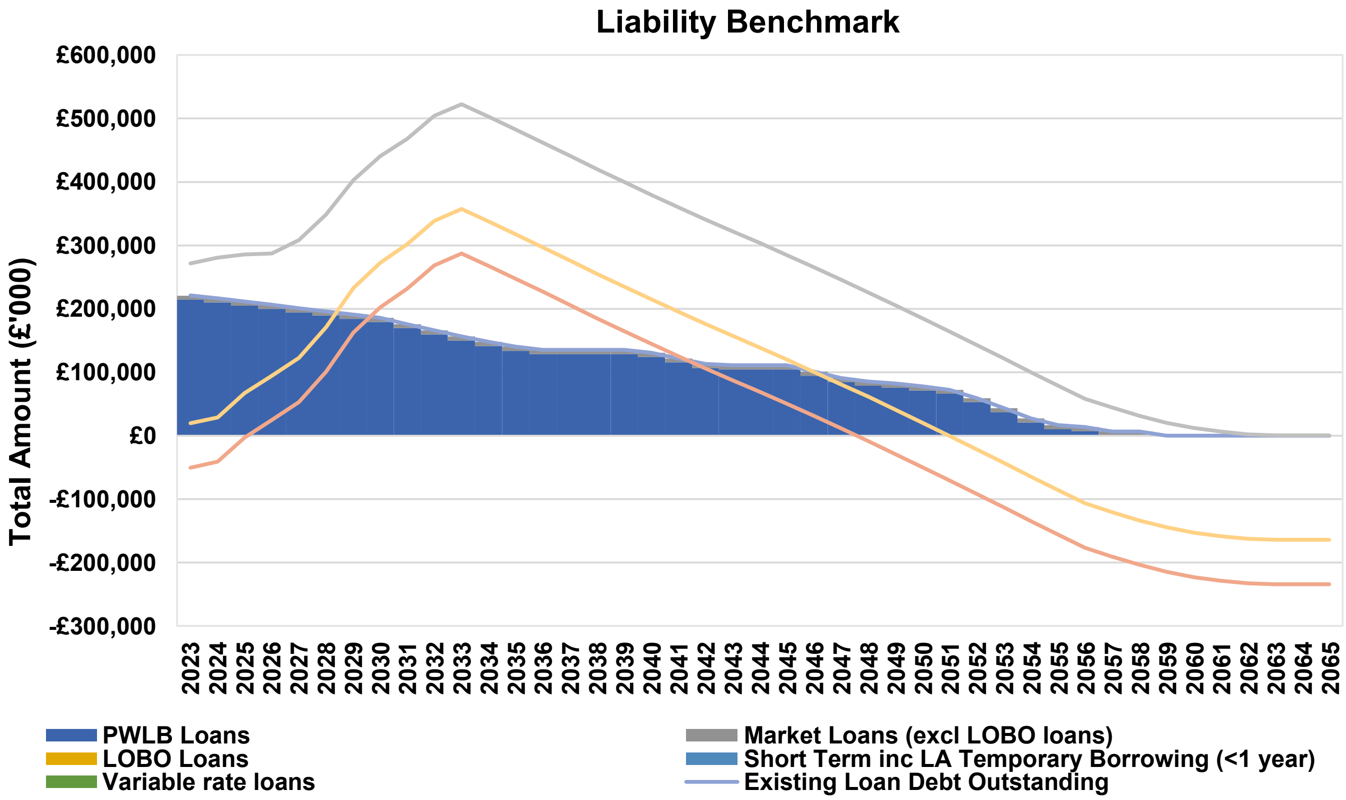
**Table 2** demonstrates that the Council has a borrowing need of £94m over the next three years. The strategy will initially focus on meeting this borrowing need from internal borrowing; avoiding external borrowing by utilising the Council's own surplus funds. Modelling of the movement of reserves and the Council's capital expenditure plans demonstrates that the Council's long-term reserves can support a level of at least £75m of internal borrowing across 2024/25, and £50m thereafter. This will mitigate the increase in the cost of borrowing and reduce counterparty risk within the Council's investment portfolio by reducing the portfolio size. The strategy and budget have been prepared based on this assumption. The Liability Benchmark, in section 2.3 below, demonstrates that if the Council were to utilise its cash-backed reserves and balances as far as possible, external borrowing can be avoided until 2028.

The Council's priority is to strike a balance between cost and certainty, and therefore the internal borrowing position will be carefully monitored to avoid incurring higher borrowing costs in the future at a time when the authority may not be able to avoid new borrowing to finance capital expenditure or refinance maturing debt.

### *2.3 Liability Benchmark*

The Liability Benchmark is a measure of the Council's borrowing need were it to fully utilise its cash-backed reserves and balances to avoid external borrowing. It assumes a liquidity buffer is maintained to ensure the Council's obligations are able to be met.

The Council's liability benchmark is shown below:




1) ***External Debt –*** *The maturity profile of the current portfolio of external debt is shown by the bars. The debt has a very gradual maturity profile which means that there are no requirements to pay back large amounts of debt in any one year.*

2) ***Loans CFR –*** *This is the projections of the Council's underlying borrowing requirement (or CFR) based on the Council's capital plans, and is shown by the top, grey line. The 2023/24 opening Loans CFR was £272m, and it is expected to peak at £517m in 2032/33. This only shows the Loans CFR projection based on the current capital programme of the Council, therefore if ongoing borrowing is required beyond 2032/33 then the CFR would rise further and for longer.*

3) ***Net Loans Requirement –*** *The expected net treasury position is shown by the bottom orange line. This shows a projection of the loans requirements measured by opening external debt for 2023/24 (£221m) less the opening external investments for 2023/24 (£272m). The projections are then based on the expected borrowing within the capital programme and the expected movement in reserves and balances, and shows the borrowing requirement if the Council were to utilise all of its reserves and balances for internal borrowing. This shows that the Council had more external investments than external debt as at 31/03/23, which is expected to change from 2024/25 as reserves reduce and borrowing is required in the capital programme. The Net Loans Requirement also peaks in 2032/33 as a result of the end of current capital planning period.*

4) ***Liability Benchmark –*** *The liability benchmark shows the Net Loan Requirement, but with a buffer of £70m incorporated to ensure the Council has sufficient cash to meet its cash obligations. This measure shows the level to which the Council can internally borrow based on the projection of the capital programme, movement of reserves and allowing for a liquidity buffer. Where the liability benchmark rises above the current debt portfolio, this shows a need for external borrowing, and where the benchmark reduces back below the current portfolio, it shows that the Council will be over-borrowed based on current plans.*

*This graph demonstrates that the Council may not need to externally borrowing until 2027/28, and that the external borrowing requirement will peak at £352m in 2032/33, before falling. The graph also shows that based on current plans, new borrowing will be required until 2040/41, so a shorter period than the Council historically borrows for.*

*Whilst the Liability Benchmark is a good indicator of the Council's direction of travel in terms of borrowing need, it assumes that capital borrowing stops after the current capital planning period, and ignores future borrowing beyond the planning period. Therefore it should not be used in isolation when making long term decisions, but as part of a range of factors.*

### *2.4 Policy on Borrowing in Advance of Need*

The Council will not borrow purely in order to profit from investment of extra sums borrowed. Any decision to borrow in advance will be within approved Capital Financing Requirement estimates and will be considered carefully to ensure that value for money can be demonstrated and that the Council can ensure the security of such funds. Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting.

### *2.5 Debt Rescheduling*

Officers continue to regularly review opportunities for debt rescheduling, but there has been a considerable widening of the difference between new borrowing and repayment rates, which has resulted in much fewer opportunities to realise any savings or benefits from rescheduling PWLB debt.

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).

The strategy is to continue to seek opportunity to reduce the overall level of Council's debt where prudent to do so, thus providing in future years cost reduction in terms of lower debt repayments costs, and 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 agreed by the Chief Finance Officer.

### *2.5 Interest Rate Risk & Continual Review*

The total borrowing need in **Table 2,** as well as the debt at risk of maturity shown in **Table 4** is the extent to which the Council is subject to interest rate risk.

| Table 4 | 2024/25 | 2025/26 | 2026/27 |
|---|---|---|---|
| | £m | £m | £m |
| Maturing Debt | 5 | 5 | 6 |
| Debt Subject to early repayments options | 0 | 0 | 0 |
| **Total debt at risk of maturity** | **5** | **5** | **6** |

Officers continue to review the need to borrow taking into consideration the potential increases in borrrowing costs, the need to finance new capital expenditure, refinancing maturing debt, and the cost of carry that might incur a revenue loss between borrowing costs and investment returns.

Against this background and the risks within the economic forecast, caution will be adopted with the 2024/25 treasury operations. The Chief Finance Officer will continue to monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

- if it was felt that there was a significant risk of a sharp FALL in borrowing rates, then borrowing will be postponed.

- if it was felt that there was a significant risk of a much sharper RISE in borrowing rates than that currently forecast, fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.

## 3. MINIMUM REVENUE PROVISION POLICY STATEMENT

The Council is required to pay off an element of the accumulated General Fund capital spend each year (the Capital Financing Requirement - CFR) through a revenue charge (the Minimum Revenue Provision - MRP). The Department for Levelling Up, Housing and Communities (DLUHC) regulations require the full Council to approve an MRP Statement in advance of each year. A variety of options are available to Councils, so long as the principle of any option selected ensures a prudent provision to redeem its debt liability over a period which is commensurate with that over which the capital expenditure is estimated to provide benefits (i.e. estimated useful life of the asset being financed).

The Council is recommended to approve the following MRP Statement for 2023/24 onwards:

**For borrowing incurred before 1 April 2008, the MRP policy will be:**

- Annuity basis over a maximum of 40 years.

**From borrowing incurred after 1 April 2008, the MRP policy will be:**

- Asset Life Method (annuity method) – MRP will be based on the estimated life of the assets, in accordance with the proposed regulations. A maximum useful economic life of 50 years for land and 40 years for other assets. This option will also be applied for any expenditure capitalised under a capitalisation directive.

**For PFI schemes, leases and closed landfill sites that come onto the Balance Sheet, the MRP policy will be:**

- Asset Life Method (annuity method) - The MRP will be calculated according to the flow of benefits from the asset, and where the principal repayments increase over the life of the asset. Any related MRP will be equivalent to the “capital repayment element” of the annual charge payable.

There is the option to charge more than the prudent provision of MRP each year through a Voluntary Revenue Provision (VRP).

For loans to third parties that are being used to fund expenditure that is classed as capital in nature, the policy will be to charge an MRP over the life of the loan.

In view of the variety of different types of capital expenditure incurred by the Council, which is not in all cases capable of being related to an individual asset, asset lives will be assessed on a basis which most reasonably reflects the anticipated period of benefit that arises from the expenditure. Also, whatever type of expenditure is involved, it will be grouped together in a manner which reflects the nature of the main component of expenditure. This approach also allows the Council to defer the introduction of an MRP charge for new capital projects/land purchases until the year after the new asset becomes operational rather than in the year borrowing is required to finance the capital spending.

## 4. ANNUAL INVESTMENT STRATEGY

The DLUHC and CIPFA have extended the meaning of 'investments' to include both financial and non-financial investments. This report deals with financial investments. Non-financial investments are covered in the Capital Strategy.

The Council's investment policy has regard to the following:

- DLUHC's Guidance on Local Government Investments (the "Guidance")
- CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2021 (the "Code")
- CIPFA Treasury Management Guidance Notes 2021

***The Council's investment priorities will be the security of capital first, portfolio liquidity second and then yield (return).*** *The Authority will aim to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity and with regard to the Authority's risk appetite.*

### *4.1 Annual Investment Strategy for 2024/25*

Investments will be made with reference to the core balance and cash flow requirements and the outlook for interest rates.

Greater returns are usually obtainable by investing for longer periods. However, based on the forecast of Bank Rate below, it is recommended that an "agile" investment strategy is recommended as an appropriate way of optimising returns.

While most cash balances are required in order to manage the ups and downs of cash flow, where cash sums can be identified that could be invested for longer periods, the value to be obtained from longer term investments will be carefully assessed.

- If it is predicted that Bank Rate is likely to rise significantly within the time horizon being considered, then consideration will be given to keeping most investments on short term or variable terms.
- Conversely, if it is predicted that Bank Rate is likely to fall within that time period, consideration will be given to locking in the higher rates currently obtainable, for longer periods.

It is currently expected that the Bank Rate will remain at the current level (expected to be the peak) during the remainder of 2023/24, with the prospect for Bank Rate to fall in the second half of 2024/25, and gradually reducing into 2025/26. Link Asset Service's (LAS) Bank Rate forecasts for financial year ends (March) are:

| Year | 2023/24 | 2024/25 | 2025/26 | 2026/27 |
|---|---|---|---|---|
| Bank Rate | 5.25% | 3.75% | 3.00% | 3.00% |

LAS's view on the prospect for interest rates, including their forecast for short term investment rates is appended at Annex B.

The primary principle governing the Council's investment criteria is the security of its investments, although the return on the investment is also a key consideration. After this main principle, the Council will ensure that:

- It maintains a policy covering both the categories of investment types it will invest in and the criteria for choosing investment counterparties with adequate security, and monitoring their security;
- It has sufficient liquidity in its investments;
- It receives a yield that is aligned with the level of security and liquidity of its investments;
- Where possible, it actively seeks to support Environmental, Social and Governance (ESG) investment products and institutions that meet all of the above requirements.

The preservation of capital is the Council's principal and overriding priority.

### *4.1.1 Changes from 2023/24 Strategy*

No new changes to the strategy are proposed.

### *4.2 Investment Policy – Management of risk*

The guidance from the DLUHC and CIPFA place a high priority on the management of risk. This authority has adopted a prudent approach to managing risk and defines its risk appetite by the following means: -

i) Minimum acceptable credit criteria are applied in order to generate a list of highly creditworthy counterparties. This also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the short term and long-term ratings.

ii) Other information: ratings will not be the sole determinant of the quality of an institution; it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To achieve this consideration the Council will engage with its advisors to maintain a monitor on market pricing such as “credit default swaps” and overlay that information on top of the credit ratings.

iii) Other information sources used will include the financial press, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.

iv) This authority has defined the list of types of investment instruments that the treasury management team are authorised to use.

    a. **Specified investments** are those with a high level of credit quality and subject to a maturity limit of one year. The limits and permitted instruments for specified investments are listed within Table 7.

    b. **Non-specified investments** are those with less high credit quality, may be for periods in excess of one year, and/or are more complex instruments which require greater consideration by members and officers before being authorised for use. The limits and permitted instruments for non-specified investments are listed within Table 8.

v) Lending limits (amounts and maturity) for each counterparty will be set through applying the credit criteria matrix (within Table 7).

vi) This authority will set a limit for the amount of its investments which are invested for longer than 365 days, detailed in the Treasury Indicators in Annex C.

vii) Investments will only be placed with counterparties from countries with a specified minimum sovereign rating of AA- (see paragraph 4.3).

viii) This authority has engaged external consultants, (see paragraph 5.3), to provide expert advice on how to optimise an appropriate balance of security, liquidity and yield, given the risk appetite of this authority in the context of the expected level of cash balances and need for liquidity throughout the year.

ix) All investments will be denominated in sterling.

x) As a result of the change in accounting standards for 2022/23 under IFRS 9, this Authority will consider the implications of investment instruments which could result in an adverse movement in the value of the amount invested and resultant charges at the end of the year to the General Fund. (In November 2018, the MHCLG, concluded a consultation for a temporary override to allow English local authorities time to adjust their portfolio of all pooled investments by announcing a statutory override to delay implementation of IFRS 9 for five years ending 31.3.23. At the current juncture it has not been determined whether a further extension to the over-ride will be agreed by Government.

However, this authority will also pursue value for money in treasury management and will monitor the yield from investment income against appropriate benchmarks for investment performance. Regular monitoring of investment performance will be carried out during the year and included within the quarterly reporting.

### *4.3 Sovereign Credit Ratings*

The current approved strategy of lending to sovereign nations and their banks which hold a minimum of AA- remains in place. The proposed Maximum investment limits and duration periods will remain the same as in the previous strategy at £60 million and one year respectively. The list of countries that qualify using this credit criteria (as at the date of this report) are shown below:

**AAA** Germany, Netherlands, Singapore, Sweden
**AA+** Canada, Finland, USA
**AA** Abu Dhabi (UAE)
**AA-** **United Kingdom**

### *4.4 Creditworthiness Policy*

The Council applies the creditworthiness service provided by the Link Group. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies which is then supplemented with the following overlays:

- credit watches and credit outlooks from credit rating agencies;
- credit default swap (CDS) spreads to give early warning of likely changes in credit ratings;
- sovereign ratings to select counterparties from only the most creditworthy countries.

This weighted scoring system then produces an end product of a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Council to determine the suggested duration for investments. The Council (in addition to other due diligence consideration) will use counterparties within the following durational bands provided they have a minimum A- (UK Banks) and AA- (Non-UK Banks) credit rating:

| ***Y*** | ***P*** | ***B*** | ***O*** | ***R*** | ***G*** | ***N/C*** |
|---|---|---|---|---|---|---|
| *Up to 5yrs* | *Up to 2yrs* | *Up to 1yr* | *Up to 1yrs* | *Up to 6 months* | *Up to 100 days* | *Not to be used* |

Typically the minimum credit ratings criteria the Council use will be a Short Term rating (Fitch or equivalents) of F1 and a Long Term rating of A- for UK Banks. There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances consideration will be given to the whole range of ratings available, or other topical market information, to support their use.

The primary principle governing the Council's investment criteria is the security of its investments, although the return on the investment is also a key consideration. After this main principle, the Council will ensure that:

- It maintains a policy covering both the categories of investment types it will invest in and the criteria for choosing investment counterparties with adequate security, and monitoring their security;
- It has sufficient liquidity in its investments.

All credit ratings are monitored daily. The Council is alerted to changes to ratings of all three agencies through its use of the LAS credit worthiness service. If a downgrade results in the counterparty or investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.

In addition to the use of credit ratings, the Council is advised of information re movements in Credit Default Swap against the iTraxx benchmark and other market data on a weekly basis. Extreme market movements may result in downgrade of an institution or removal from the Council's lending list. The counterparties in which the Council will invest its cash surpluses is based on officer's assessment of investment security, risk factors, market intelligence, a diverse but manageable portfolio and their participation in the local authority market.

**Table 7** below summarises the types of specified investment counterparties available to the Council, and the maximum amount and maturity periods placed on each of these. A full list of the Council's counterparties and the current limits for 2024/25 are appended at Annex A.

**Criteria for Specified Investments**

| Table 7 | Country/ Domicile | Instrument | Min. Credit Criteria/LAS colour band | Max. Amount | Max. maturity period |
|---|---|---|---|---|---|
| Debt Management and Deposit Facilities (DMADF) | UK | Term Deposits (TDs) | N/A | unlimited | 12 Months |
| Government Treasury bills | UK | TDs | UK Sovereign Rating | unlimited | 12 Months |
| UK Local Authorities* | UK | TDs | UK Sovereign Rating | £60m | 12 Months |
| Banks – part nationalised | UK | ▪ TDs<br>▪ Deposits on Notice<br>▪ Certificates of Deposit (CDs) | N/A | £60m | 12 Months |
| Banks | UK | ▪ TDs<br>▪ Deposits on Notice<br>▪ CDs | Blue | £60m | 12 Months |
| | | | Orange | £60m | 12 Months |
| | | | Red | £60m | 6 Months |
| | | | Green | £60m | 100 Days |
| Building Societies | UK | ▪ TDs<br>▪ Deposits on Notice<br>▪ CDs | Blue | £60m | 12 Months |
| | | | Orange | £60m | 12 Months |
| | | | Red | £60m | 6 Months |
| | | | Green | £60m | 100 Days |
| Individual Money Market Funds (MMF) CNAV and LVNAV | UK/Ireland/ EU domiciled | AAA Rated Money Market Fund Rating | N/A | £60m | Liqiuid |
| VNAV MMF's and Ultra Short Dated Bond Funds | UK/Ireland/EU domiciled | AAA Rated Bond Fund Fund Rating | N/A | £60m | Liquid |
| Banks – Non-UK | Those with sovereign rating of at least AA-** | ▪ TDs<br>▪ Deposits on Notice<br>▪ CDs | Blue | £60m | 12 Months |
| | | | Orange | £60m | 12 Months |
| | | | Red | £60m | 6 Months |
| | | | Green | £60m | 100 Days |

** Local Authorities appear on both Specified and Non-specified investment list – an investment with a LA for up to a year is Specified, and between 1-2 years is Non-specified. The maximum amount that can be lent to any single Local Authority is £60m across both specified and Unspecified Investments*

***See Paragraph 4.3 for full list of countries that meet these criteria*

**Non-Specified investments** are any other types of investment that are not defined as specified. The identification and rationale supporting the selection of these other investments and the maximum limits to be applied are set out in **Table 8** below:

| Table 8 | Minimum credit criteria | Maximum investments | Period |
|---|---|---|---|
| UK Local Authorities** | Government Backed | £60m | 2 years |
| Corporate Bond Fund(s) | Investment Grade | £30m | 2 - 5 years |
| Pooled Property Fund(s) | N/A | £30m | 5+ years |
| Mixed Asset Fund(s) | N/A | £30m | 2 - 5 years |
| Short Dated Bond Fund(s) | N/A | £30m | 2 – 5 years |

*** Local Authorities appear on both Specified and Non-specified investment list – an investment with a LA for up to a year is Specified, and between 1-2 years is Non-specified. The maximum amount that can be lent to any single Local Authority is £60m across both specified and Unspecified Investments*

The maximum amount that can be invested will be monitored in relation to the Council's surplus monies and the level of reserves. The approved counterparty list will be maintained by referring to an up-to-date credit rating agency reports, and the Council will liaise regularly with brokers for updates. Where Externally Managed Funds are not rated, a selection process will evaluate relative risks & returns. Security of the Council's money and fund volatility will be key measures of suitability. Counterparties may be added to or removed from the list only with the approval of the Chief Finance Officer. A full list of the Council's counterparties and the current limits for 2024/25 are appended at Annex A.

### *4.5 Investment Risk Benchmarking*

The weighted average benchmark risk factor for 2024/25 is recommended to be 0.05%. This is unchanged from 2023/24. This is a measure of the percentage of the portfolio deemed to be at risk of loss by reference to the maturity date, value of investment, and credit rating of the individual investments within the portfolio compared to the historic default data for those credit ratings.

This benchmark is a simple target (not limit) to measure investment risk and so may be breached from time to time, depending on movements in interest rates and counterparty criteria. The purpose of the benchmark is that the in-house treasury team can monitor the current and trend position and amend the operational strategy depending on any changes. Any breach of the benchmarks will be reported with supporting reasons in the mid-year or end of year reviews.

This matrix will only cover internally managed investments, excluding externally managed cash that has been subject to an individual selection process. It also excludes funds lend to other Local Authorities, consistent with the CIPFA Accounting Code.

### *4.6 Investment Performance Benchmarking*

The performance of the Council's investment portfolio will be measured against the overnight SONIA Rate.

## 5. OTHER TREASURY ISSUES

### *5.1 Banking Services*

NatWest, which is part Government owned, currently provides banking services for the Council.

### *5.2 Training*

The CIPFA Treasury Management Code requires the responsible officer to ensure that members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsible for scrutiny.

The scale and nature of this will depend on the size and complexity of the organisation's treasury management needs. Organisations should consider how to assess whether treasury management staff and board/ Council members have the required knowledge and skills to undertake their roles and whether they have been able to maintain those skills and keep them up to date.

As a minimum, authorities should carry out the following to monitor and review knowledge and skills:

- Record attendance at training and ensure action is taken where poor attendance is identified.
- Prepare tailored learning plans for treasury management officers and board/Council members.
- Require treasury management officers and board/Council members to undertake self-assessment against the required competencies (as set out in the schedule that may be adopted by the organisation).
- Have regular communication with officers and board/Council members, encouraging them to highlight training needs on an ongoing basis."

In further support of the revised training requirements, CIPFA's Better Governance Forum and Treasury Management Network have produced a 'self-assessment by members responsible for the scrutiny of treasury management', which is available from the CIPFA website to download.

Training was last provided for members of the Audit Committee (and expended to all Councillors online) on 24 November 2023 and further training will be arranged for November 2024.

The training needs of treasury management officers are periodically reviewed.

A formal record of the training received by officers central to the Treasury function and members who are responsible for decision making and scrutiny of the Treasury function will be maintained by the Principal Accountant (Treasury).

### *5.3 Policy on the use of External Service Providers*

The Council uses Link Asset Services as its external treasury management advisors.

The Council recognises that responsibility for treasury management decisions remains with the Council at all times and will ensure that undue reliance is not placed upon our external service providers. It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed, documented and subject to regular review.

### *5.4 Lending to Third Parties*

The Council has the power to lend monies to third parties subject to a number of criteria. These are not treasury type investments rather they are policy investments. Any activity will only take place after relevant due diligence has been undertaken.

### *5.5 Updates to Accounting Requirements*

- **IFRS9 – local authority override – English local authorities**

  The MHCLG (DLUHC) enacted a statutory over-ride from 1.4.18 for a five-year period until 31.3.23 following the introduction of IFRS 9 in respect of the requirement for any unrealised capital gains or losses on marketable pooled funds to be chargeable in year. This has been extended to 31.3.25 and the effect of allowing any unrealised capital gains or losses arising from qualifying investments to be held on the balance sheet until 31.3.25: this is intended to allow authorities to initiate an orderly withdrawal of funds if required. In addition, IFRS9 impacts the write-down in the valuation of impaired loans.

- **IFRS 16 – Leasing**

  The CIPFA LAASAC Local Authority Accounting Code Board has deferred implementation of IFRS16 until 1.4.24, the 2024/25 financial year. Once implemented, this has the following impact to the Treasury Management Strategy:

  - The MRP Policy sets out how MRP will be applied for leases bought onto the balance sheet;
  - The Council's Capital Financing Requirement authorised limit and operational boundary expectations for 2024/25 onwards have been increased to reflect the estimated effect of this change.

## Counterparty List 2024/25

**ANNEX A**

| Bank with duration colour | Country | Fitch Ratings | | | | Moody's Ratings | | S & P Ratings | | CDS Price | ESCC Duration | Link Duration Limit | Money Limit |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Specified Investments:** | | L Term | S Term | Viab. | Supp. | L Term | S Term | L Term | S Term | | (Months) | (Months) | (£m) |
| **UK Counterparties:** | | | | | | | | | | | | | |
| Lloyds Bank PLC (RFB) | UK | A+ | F1 | a | WD | A1 | P-1 | A+ | A-1 | 53.22 | 6 | 6 | 60 |
| Lloyds Bank Corporate Markets Plc (NRFB) | UK | A+ | F1 | - | WD | A1 | P-1 | A | A-1 | - | 6 | 6 | |
| Bank of Scotland PLC (RFB) | UK | A+ | F1 | a | WD | A1 | P-1 | A+ | A-1 | 53.22 | 6 | 6 | |
| NatWest Bank (RFB) | UK | A+ | F1 | a | WD | A1 | P-1 | A+ | A-1 | - | 12 | 12 | 60 |
| NatWest Markets Plc (NRFB) | UK | A+ | F1 | WD | WD | A1 | P-1 | A | A-1 | 84.12 | 6 | 6 | |
| Royal Bank of Scotland (RFB) | UK | A+ | F1 | a | WD | A1 | P-1 | A+ | A-1 | - | 12 | 12 | |
| HSBC UK Bank (RFB) | UK | AA- | F1+ | a | WD | A1 | P-1 | A+ | A-1 | - | 12 | 12 | 60 |
| HSBC Bank (NRFB) | UK | AA- | F1+ | a | WD | A1 | P-1 | A+ | A-1 | 52.88 | 12 | 12 | |
| Barclays Bank UK (RFB) | UK | A+ | F1 | a | WD | A1 | P-1 | A+ | A-1 | - | 6 | 6 | 60 |
| Barclays Bank (NRFB) | UK | A+ | F1 | a | WD | A1 | P-1 | A+ | A-1 | 100.00 | 6 | 6 | |
| Santander UK | UK | A+ | F1 | a | WD | A1 | P-1 | A | A-1 | - | 6 | 6 | 60 |
| Santander Financial Services (NRFB) | UK | A+ | F1 | - | WD | A1 | P-1 | A- | A-2 | - | 6 | 6 | |
| Goldman Sachs International Bank | UK | A+ | F1 | - | WD | A1 | P-1 | A+ | A-1 | 79.25 | 6 | 6 | 60 |
| Handlesbanken PLC | UK | AA | F1+ | - | WD | - | - | AA- | A-1+ | - | 12 | 12 | 60 |
| SMBC Bank International Plc | UK | A- | F1 | - | WD | A- | P-1 | A | A-1 | 35.27 | 6 | 6 | 60 |
| Standard Chartered Bank | UK | A+ | F1 | a | WD | A1 | P-1 | A+ | A-1 | 52.68 | 6 | 6 | 60 |
| Close Brothers Ltd | UK | A- | F2 | a- | WD | Aa3 | P-1 | - | - | - | 6 | 6 | 60 |
| Clydesdale Bank PLC | UK | A- | F2 | bbb+ | WD | A3 | P-2 | A- | A-2 | - | 3 | 3 | 60 |
| Nationwide Building Society | UK | A | F1 | a | WD | A1 | P-1 | A+ | A-1 | - | 6 | 6 | 60 |
| **Non UK Counterparties:** | | | | | | | | | | | | | |
| Royal Bank of Canada | Canada | AA- | F1+ | aa- | WD | Aa1 | P-1 | AA- | A-1+ | - | 12 | 12 | 60 |
| Toronto-Dominion Bank | Canada | AA- | F1+ | aa- | WD | Aa1 | P-1 | AA- | A-1+ | - | 12 | 12 | 60 |
| Nordea Bank Abp | Finland | AA- | F1+ | aa- | WD | Aa3 | P-1 | AA- | A-1+ | - | 12 | 12 | 60 |
| Landwirtschaftliche Rentenbank | Germany | AAA | F1+ | - | WD | Aaa | P-1 | AAA | A-1+ | - | 12 | 24 | 60 |

| Continued Counterparty list Bank with duration colour | Country | Fitch Ratings | | | | Moody's Ratings | | S & P Ratings | | CDS Price | ESCC Duration | Link Duration Limit | Money Limit |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | L Term | S Term | Viab. | Supp. | L Term | S Term | L Term | S Term | | (Months) | (Months) | (£m) |
| NRW.BANK | Germany | AAA | F1+ | - | WD | Aa1 | P-1 | AA | A-1+ | - | 12 | 24 | 60 |
| Bank Nederlandse Gemeenten N.V. | Netherlands | AAA | F1+ | - | WD | Aaa | P-1 | AAA | A-1+ | - | 12 | 24 | 60 |
| DBS Bank Ltd. | Singapore | AA- | F1+ | aa- | WD | Aa1 | P-1 | AA- | A-1+ | - | 12 | 12 | 60 |
| Oversea-Chinese Banking Corp. Ltd. | Singapore | AA- | F1+ | aa- | WD | Aa1 | P-1 | AA- | A-1+ | - | 12 | 12 | 60 |
| United Overseas Bank Ltd. | Singapore | AA- | F1+ | aa- | WD | Aa1 | P-1 | AA- | A-1+ | - | 12 | 12 | 60 |
| Svenska Handelsbanken AB | Sweden | AA | F1+ | aa | WD | Aa2 | P-1 | AA- | A-1+ | - | 12 | 12 | 60 |
| First Abu Dhabi Bank PJSC | UAE | AA- | F1+ | a- | WD | Aa3 | P-1 | AA- | A-1+ | - | 12 | 12 | 60 |
| Bank of New York Mellon | USA | AA | F1+ | aa- | WD | Aa1 | P-1 | AA- | A-1+ | - | 12 | 12 | 60 |

| *Yellow* | *Purple* | *Blue* | *Orange* | *Red* | *Green* | *No Colour* |
|---|---|---|---|---|---|---|
| | | | | | | |
| *Up to 5yrs* | *Up to 2yrs* | *Up to 1yr (semi nationalised UK banks)* | *Up to 1yr* | *Up to 6 months* | *Up to 100 days* | *Not to be used* |

| **Non-Specified Investments:** | | | |
|---|---|---|---|
| | **Minimum credit Criteria** | **Maximum Investments** | **Period** |
| UK Local Authorities | Government Backed | £60m | 2 years |
| Corporate Bond Fund(s) | Investment Grade | £30m | 2 – 5 years |
| Pooled Property Fund(s) | N/A | £30m | 5+ years |
| Mixed Asset Fund(s) | N/A | £30m | 2 - 5 years |
| Short Dated Bond Fund(s) | N/A | £30m | 2 - 5 years |

**ANNEX B**

**ECONOMIC OVERVIEW**

**Provided by Link Asset Services, January 2024**

- The third quarter of 2023/24 saw:
  - A 0.3% m/m decline in real GDP in October, potentially partly due to unseasonably wet weather, but also due to the ongoing drag from higher interest rates. Growth for the second quarter, ending 30th September, was revised downwards to -0.1% and growth on an annual basis was also revised downwards, to 0.3%;
  - A sharp fall in wage growth, with the headline 3myy rate declining from 8.0% in September to 7.2% in October, although the ONS "experimental" rate of unemployment has remained low at 4.2%;
  - CPI inflation continuing on its downward trajectory, from 8.7% in April to 4.6% in October, then again to 3.9% in November;
  - Core CPI inflation decreasing from April and May's 31 years' high of 7.1% to 5.1% in November, the lowest rate since January 2022;
  - The Bank of England holding Bank Rate at 5.25% in November and December;
  - A steady fall in 10-year gilt yields as investors revised their interest rate expectations lower.
- The revision of GDP data in Q2 to a 0.1% q/q fall may mean the mildest of mild recessions has begun. Indeed, real GDP in October fell 0.3% m/m which does suggest that the economy may stagnate again in Q3. The weakness in October may partly be due to the unseasonably wet weather. That said, as the weakness was broad based it may also be the case that the ongoing drag from higher interest rates is more than offsetting any boost from the rise in real wages.
- However, the rise in the flash composite activity Purchasing Managers Index, from 50.7 in November to 51.7 in December, did increase the chances of the economy avoiding a contraction in Q3. The improvement was entirely driven by the increase in the services activity balance from 50.9 to 52.7. (Scores above 50 point to expansion in the economy, although only tepid in this instance.) The press release noted that this was primarily driven by a revival in consumer demand in the technological and financial services sectors. This chimes with the further improvement in the GfK measure of consumer confidence in December, from -24 to -22. The services PMI is now consistent with non-retail services output growing by 0.5% q/q in Q3, but this is in stark contrast to the manufacturing sector where the output balance slumped from 49.2 to 45.9 and, at face value, the output balance is consistent with a 1.5% q/q fall in manufacturing output in Q3.
- The 0.3% m/m fall in retail sales volumes in October means that after contracting by 1.0% q/q (which was downwardly revised from -0.8% q/q) in Q2, retail activity remained weak at the start of Q3. That suggests higher interest rates are taking a bigger toll on real consumer spending.
- Higher interest rates have filtered through the financial channels and weakened the housing market but, overall, it remains surprisingly resilient with the Halifax house price index recently pointing to a 1.7% year on year increase whilst Nationwide's December data pointed to a -1.8% year on year decrease. However, the full weakness in real consumer spending and real business investment has yet to come as currently it is estimated that

around two thirds to a half of the impact of higher interest rates on household interest payments has yet to be felt.

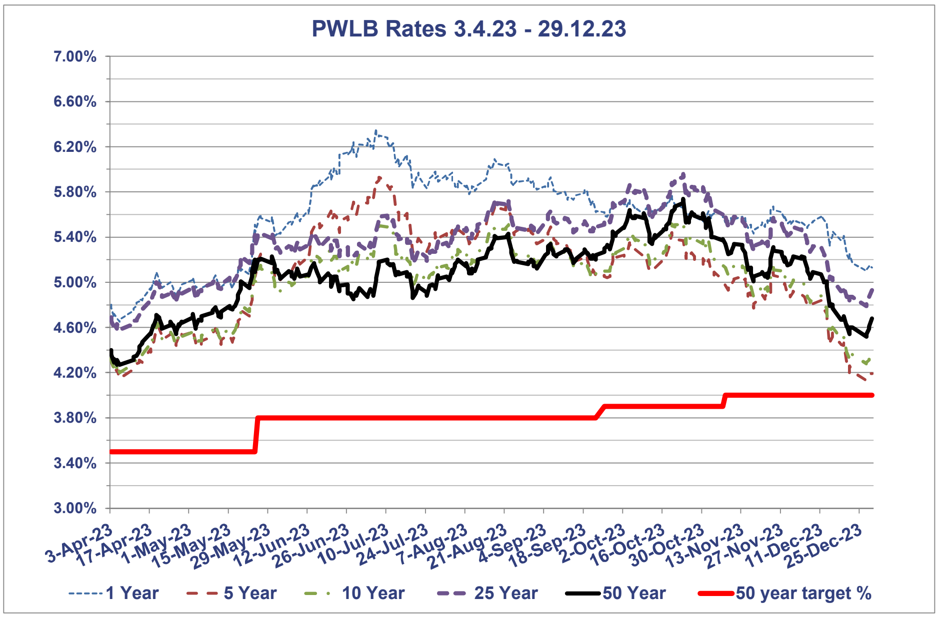
- Overall, we expect real GDP growth to remain subdued throughout 2024 as the drag from higher interest rates is protracted but a fading of the cost-of-living crisis and interest rate cuts in the second half of 2024 will support a recovery in GDP growth in 2025.
- The labour market remains tight by historical standards, but the sharp fall in wage growth seen in October will reinforce the growing belief in markets that interest rates will be cut mid-2024. Wage growth eased in October much faster than the consensus expected. Total earnings fell by 1.6% m/m, which meant the headline 3myy rate eased from 8.0% in September to 7.2% in October. This news will be welcomed by the Bank of England. Indeed, the timelier three-month annualised rate of average earnings growth fell from +2.4% to -1.2%. Excluding bonuses, it fell from 5.3% to 2.0%. Furthermore, one of the Bank's key barometers of inflation persistence, regular private sector pay growth, dropped from 7.9% 3myy to 7.3%, which leaves it comfortably on track to fall to 7.2% by December, as predicted by the Bank in November.
- The fall in wage growth occurred despite labour demand being stronger in October than expected. The three-month change in employment eased only a touch from +52,000 in September to +50,000 in October. But resilient labour demand was offset by a further 63,000 rise in the supply of workers in the three months to October. That meant labour supply exceeded its pre-pandemic level for the first time, and the unemployment rate remained at 4.2% in October. In the three months to November, the number of job vacancies fell for the 17th month in a row, from around 959,000 in October to around 949,000. That has reduced the vacancy to unemployment ratio as demand for labour eases relative to supply, which may support a further easing in wage growth in the coming months.
- CPI inflation fell from 6.7% in September to 4.6% in October, and then again to 3.9% in November. Both these falls were bigger than expected and there are clear signs of easing in domestic inflationary pressures. The fall in core CPI inflation from 5.7% to 5.1% in November was bigger than expected (consensus forecast 5.6%). That's the lowest rate since January 2022. Some of the decline in core inflation was due to the global influence of core goods inflation, which slowed from 4.3% to 3.3%. But some of it was due to services inflation falling from 6.6% to 6.3%. The Bank views the latter as a key barometer of the persistence of inflation and it came in further below the Bank's forecast of 6.9% in its November Monetary Policy Report. This will give the Bank more confidence that services inflation is now on a firmly downward path.
- The Bank of England sprung no surprises with its December monetary policy committee (MPC) meeting, leaving interest rates at 5.25% for the third time in a row and pushing back against the prospect of near-term interest rate cuts. The Bank continued to sound hawkish, with the MPC maintaining its tightening bias saying that "further tightening in monetary policy would be required if there were evidence of more persistent inflationary pressures". And it stuck to the familiar script, saying that policy will be "sufficiently restrictive for sufficiently long" and that "monetary policy is likely to need to be restrictive for an extended period of time". In other words, the message is that the MPC is not yet willing to endorse investors' expectations that rates will be cut as soon as May 2024.
- Looking ahead, our colleagues at Capital Economics forecast that the recent downward trends in CPI and core inflation will stall over the next few months before starting to decline

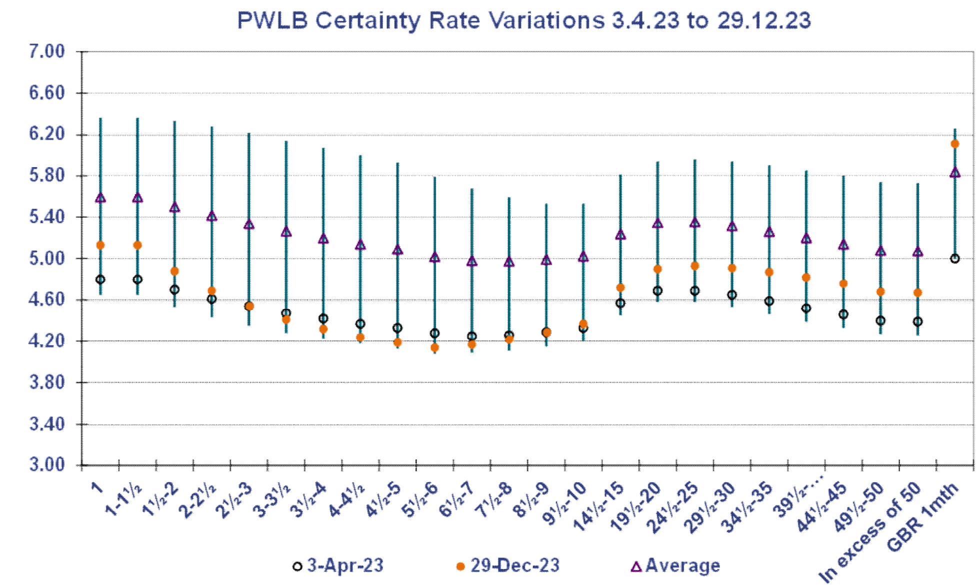
more decisively again in February. That explains why we think the Bank of England won't feel comfortable cutting interest rates until H2 2024.

- The fall in UK market interest rate expectations in December has driven most of the decline in 10-year gilt yields, which have fallen in line with 10-year US Treasury and euro-zone yields. 10-year gilt yields have fallen from 4.68% in October 2023 to around 3.70% in early January, with further declines likely if the falling inflation story is maintained.
- Investors' growing expectations that the Fed will cut interest rates soon has led to an improvement in risk sentiment, which has boosted the pound and other risky assets. In addition, the rise in the pound, from $1.21 in November to $1.27 now, has also been supported by the recent relative decline in UK wholesale gas prices.
- The further fall in 10-year real gilt yields in December has supported the recent rise in the FTSE 100. That said, the index remains 5% below its record high in February 2023. This modest rise in equities appears to have been mostly driven by strong performances in the industrials and rate-sensitive technology sectors. But UK equities have continued to underperform US and euro-zone equities. The FTSE 100 has risen by 2.2% in December, while the S&P 500 has risen by 3.8%. This is partly due to lower energy prices, which have been a relatively bigger drag on the FTSE 100, due to the index's high concentration of energy companies.

In the table below, the rise in gilt yields across the curve as a whole in 2023/24, and therein PWLB rates, is clear to see.

**PWLB RATES 03.04.23 - 29.12.23**






**HIGH/LOW/AVERAGE PWLB RATES FOR 01.04.23 – 29.12.23**

| | 1 Year | 5 Year | 10 Year | 25 Year | 50 Year |
|---|---|---|---|---|---|
| **Low** | 4.65% | 4.13% | 4.20% | 4.58% | 4.27% |
| **Date** | 06/04/2023 | 27/12/2023 | 06/04/2023 | 06/04/2023 | 05/04/2023 |
| **High** | 6.36% | 5.93% | 5.53% | 5.96% | 5.74% |
| **Date** | 06/07/2023 | 07/07/2023 | 23/10/2023 | 23/10/2023 | 23/10/2023 |
| **Average** | 5.60% | 5.09% | 5.03% | 5.35% | 5.08% |
| **Spread** | 1.71% | 1.80% | 1.33% | 1.38% | 1.47% |

The peak in medium to longer dated rates has generally arisen in August and September and has been primarily driven by continuing high UK inflation, concerns that gilt issuance may be too much for the market to absorb comfortably, and unfavourable movements in US Treasuries.

The S&P 500 and FTSE 100 have struggled to make much ground through 2023.

### Prospects for Interest Rates

The Council has appointed Link Group as its treasury advisor and part of their service is to assist the Authority to formulate a view on interest rates. Link provided the following forecasts on 08 January 2024. These are forecasts for Bank Rate, average earnings and PWLB certainty rates, gilt yields plus 80 bps.

| Link Group Interest Rate View 08.01.24 | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Mar-24 | Jun-24 | Sep-24 | Dec-24 | Mar-25 | Jun-25 | Sep-25 | Dec-25 | Mar-26 | Jun-26 | Sep-26 | Dec-26 | Mar-27 |
| BANK RATE | 5.25 | 5.25 | 4.75 | 4.25 | 3.75 | 3.25 | 3.00 | 3.00 | 3.00 | 3.00 | 3.00 | 3.00 | 3.00 |
| 3 month ave earnings | 5.30 | 5.30 | 4.80 | 4.30 | 3.80 | 3.30 | 3.00 | 3.00 | 3.00 | 3.00 | 3.00 | 3.00 | 3.00 |
| 6 month ave earnings | 5.20 | 5.10 | 4.60 | 4.10 | 3.70 | 3.30 | 3.10 | 3.10 | 3.10 | 3.10 | 3.10 | 3.10 | 3.10 |
| 12 month ave earnings | 5.00 | 4.90 | 4.40 | 3.90 | 3.60 | 3.20 | 3.10 | 3.10 | 3.10 | 3.10 | 3.10 | 3.20 | 3.20 |
| 5 yr PWLB | 4.50 | 4.40 | 4.30 | 4.20 | 4.10 | 4.00 | 3.80 | 3.70 | 3.60 | 3.60 | 3.50 | 3.50 | 3.50 |
| 10 yr PWLB | 4.70 | 4.50 | 4.40 | 4.30 | 4.20 | 4.10 | 4.00 | 3.90 | 3.80 | 3.70 | 3.70 | 3.70 | 3.70 |
| 25 yr PWLB | 5.20 | 5.10 | 4.90 | 4.80 | 4.60 | 4.40 | 4.30 | 4.20 | 4.20 | 4.10 | 4.10 | 4.10 | 4.10 |
| 50 yr PWLB | 5.00 | 4.90 | 4.70 | 4.60 | 4.40 | 4.20 | 4.10 | 4.00 | 4.00 | 3.90 | 3.90 | 3.90 | 3.90 |

**PWLB Rates**

- The short and medium part of the gilt curve has rallied since the start of November as markets price in a quicker reduction in Bank Rate through 2024 and 2025 than held sway back then. This reflects market confidence in inflation falling back in a similar manner to that already seen in the US and the Euro-zone. At the time of writing there is c70 basis points difference between the 5 and 50 year parts of the curve.

The balance of risks to the UK economy: -

- The overall balance of risks to economic growth in the UK is even.

Downside risks to current forecasts for UK gilt yields and PWLB rates include: -

- Labour and supply shortages prove more enduring and disruptive and depress economic activity (accepting that in the near-term this is also an upside risk to inflation and, thus, could keep gilt yields high for longer).

- The Bank of England has increased Bank Rate too fast and too far over recent months, and subsequently brings about a deeper and longer UK recession than we currently anticipate.

- UK / EU trade arrangements – if there was a major impact on trade flows and financial services due to complications or lack of co-operation in sorting out significant remaining issues.

- Geopolitical risks, for example in Ukraine/Russia, the Middle East, China/Taiwan/US, Iran and North Korea, which could lead to increasing safe-haven flows.

Upside risks to current forecasts for UK gilt yields and PWLB rates: -

- Despite the tightening in Bank Rate to 5.25%, the Bank of England allows inflationary pressures to remain elevated for a long period within the UK economy, which then necessitates Bank Rate staying higher for longer than we currently project.

- The pound weakens because of a lack of confidence in the UK Government's pre-election fiscal policies, which may prove inflationary, resulting in investors pricing in a risk premium for holding UK sovereign debt.

- Projected gilt issuance, inclusive of natural maturities and QT, could be too much for the markets to comfortably digest without higher yields compensating.

Gilt yields and PWLB rates

The overall longer-run trend is for gilt yields and PWLB rates to fall back over the timeline of our forecasts, as inflation starts to fall through the remainder of 2023 and into 2024.

Our target borrowing rates are set two years forward (as we expect rates to fall back) and the current PWLB (certainty) borrowing rates are set out below: -

| PWLB debt | Current borrowing rate as at 08.01.24 p.m. | Target borrowing rate now (end of Q4 2025) | Target borrowing rate previous (end of Q3 2025) |
|---|---|---|---|
| 5 years | 4.53% | 3.70% | 3.80% |
| 10 years | 4.67% | 3.90% | 3.80% |
| 25 years | 5.19% | 4.20% | 4.20% |
| 50 years | 4.97% | 4.00% | 4.00% |

Borrowing advice: Our long-term (beyond 10 years) forecast for Bank Rate remains at 3% and reflects Capital Economics' research that suggests AI and general improvements in productivity will be supportive of a higher neutral interest rate. As all PWLB certainty rates are currently significantly above this level, borrowing strategies will need to be reviewed in that context. Overall, better value can be obtained at the shorter end of the curve and short-dated fixed LA to LA monies should be considered. Temporary borrowing rates will remain elevated for some time to come but may prove the best option whilst the market continues to factor in Bank Rate reductions for 2024 and later.

Our suggested budgeted earnings rates for investments up to about three months' duration in each financial year are set out below.

| Average earnings in each year | Now | Previously |
|---|---|---|
| 2023/24 (residual) | 5.30% | 5.30% |
| 2024/25 | 4.55% | 4.70% |
| 2025/26 | 3.10% | 3.20% |
| 2026/27 | 3.00% | 3.00% |
| 2027/28 | 3.25% | 3.25% |
| 2028/29 | 3.25% | 3.25% |
| Years 6 to 10 | 3.25% | 3.25% |
| Years 10+ | 3.25% | 3.25% |

As there are so many variables at this time, caution must be exercised in respect of all interest rate forecasts.

Our interest rate forecast for Bank Rate is in steps of 25 bps, whereas PWLB forecasts have been rounded to the nearest 10 bps and are central forecasts within bands of + / - 25 bps. Naturally, we continue to monitor events and will update our forecasts as and when appropriate.

**ANNEX C**

**PRUDENTIAL AND TREASURY INDICATORS 2024/25 to 2026/27**

The Council's capital expenditure plans are a key driver of treasury management activities. The output of the capital expenditure plans is reflected in prudential indicators. Local Authorities are required 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 Code sets out the indicators that must be used but does not suggest limits or ratios as these are for the authority to set itself.

The Prudential Indicators for 2024/25 to 2026/27 are set out in **Table A** below:

| Table A | 2024/25 Estimate | 2025/26 Estimate | 2026/27 Estimate |
|---|---|---|---|
| **Capital Expenditure £m (gross)**<br>Council's capital expenditure plans | £97m | £98m | £67m |
| **Capital Financing Requirement £m***<br>Measures the underlying need to borrow for capital purposes (including PFI & Leases) | £383m | £399m | £413m |
| **Ratio of financing costs to net revenue stream****<br>Identifies the trend in the cost of capital (borrowing and other long term obligation costs) against net revenue stream | 3.81% | 3.87% | 4.25% |

** From 2024/25, the CFR includes an estimate for leases that will be bought onto the balance sheet under a change in leasing accounting regulations.*

*** the ratio of financing costs to net revenue stream illustrates the percentage of the Council's net revenue budget being used to finance the Council's borrowing. This includes interest costs relating to the Council's borrowing portfolio and MRP. This was previously reported net of the investment income from the Council's investment portfolio, but this is no longer allowable under the 2021 Code, and therefore the ratio is higher than previously reported.*

The Treasury Management Code requires that Local Authorities set a number of indicators for treasury performance in addition to the Prudential Indicators which fall under the Prudential Code. The Treasury Indicators for 2024/25 to 2026/27 are set out in **Tables B & C** below. These have been calculated and determined by Officers in compliance with the Treasury Management Code of Practice.:

| Table B | 2024/25 Estimate | 2025/26 Estimate | 2026/27 Estimate |
|---|---|---|---|
| **Authorised Limit for External Debt £m***<br>The Council is expected to set a maximum authorised limit for external debt. This represents a limit beyond which external debt is prohibited, and this limit needs to be set or revised by Full Council. | £413m | £429m | £443m |
| **Operational boundary for external debt £m***<br>The Council is required to set an operational boundary for external debt. This is the limit which external debt is not normally expected to exceed. This indicator may be breached temporarily for operational reasons. | £393m | £409m | £423m |
| **Principal Sums invested for longer than 365 days** | £60m | £60m | £60m |

| | | | |
|---|---|---|---|
| **Control on interest rate exposure:**<br>**Upper limit for fixed interest rate exposure**<br>Identifies a maximum limit for fixed interest rates for borrowing and investments. | 100% | 100% | 100% |
| **Control on interest rate exposure:**<br>**Upper limit for variable interest rate exposure**<br>Identifies a maximum limit for variable interest rates for borrowing and investments. | 15% | 15% | 15% |

**From 2024/25 The Authorised Limit and Operational Boundary includes an estimate for leases that will be bought onto the balance sheet under a change in leasing accounting regulations.*

| **Table C** | | |
|---|---|---|
| **Maturity Structure of fixed interest rate borrowing**<br>The Council needs to set upper and lower limits with respect to the maturity structure of its borrowing. | | |
| | Lower | Upper |
| Under 12 months | 0% | 25% |
| 12 months to 2 years | 0% | 40% |
| 2 years to 5 years | 0% | 60% |
| 5 years to 10 years | 0% | 70% |
| Over 10 years | 0% | 90% |

**ANNEX D**

**SCHEME OF DELEGATION**

## 1. Full Council

In line with best practice, Full Council is required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of polices, estimates and actuals. These reports are:

**i. Treasury Management Policy and Strategy Report**

The report covers:

- the capital plans (including prudential indicators);
- the Capital Strategy;
- a Minimum Revenue Provision Policy (how residual capital expenditure is charged to revenue over time);
- the Treasury Management Strategy (how the investments and borrowings are to be organised) including treasury indicators; and
- an investment strategy (the parameters on how investments are to be managed).

**ii. A Mid-Year Review Report and a Year End Stewardship Report**

These will update members with the progress of the capital position, amending prudential indicators as necessary, and indicating whether the treasury strategy is meeting the strategy or whether any policies require revision. The report also provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

## 2. Cabinet

- Recommendation of the Treasury Management Strategy to Full Council
- Approval of the Treasury Management quarterly update reports;
- Approval of the Treasury Management mid-year and outturn reports.

## 3. Audit Committee

- Scrutiny of performance against the strategy.

## 4. Role of the Section 151 Officer

The Section 151 (responsible) Officer:

- recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance;
- submitting regular treasury management policy reports;
- submitting budgets and budget variations;
- receiving and reviewing management information reports;
- reviewing the performance of the treasury management function;
- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function;
- ensuring the adequacy of internal audit, and liaising with external audit;
- recommending the appointment of external service providers.

There are further responsibilities for the S151 Officer identified within the 2017 Code in respect of non-financial investments. They are identified and listed in the Capital Strategy where relevant.

## ANNEX E
## INVESTMENT PRODUCT GLOSSARY

**Bank / Building Society**: Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail.

**Bank / Building Society Secured (Covered Bonds):** These investments are secured on the bank's assets, which limit the potential losses in the unlikely event of insolvency, and means that they are exempt from bail-in.

**Corporate Bonds:** Bonds issued by companies other than banks and registered providers. These investments are not subject to bail-in but are exposed to the risk of the company going insolvent.

**Enhanced Cash / Ultra Short Dated Bond Funds:** Funds designed to produce an enhanced return over and above a Money Market Fund. The manager may use a wider range of alternative options to try and generate excess performance. These could include different counterparties, instruments as well as longer dated investments.

**Equity Fund:** Equity funds are pooled investment vehicles that will focus investments primarily in UK equities.

**Government:** Loans, bonds and bills issued or guaranteed by UK government, local authorities and supranational banks. These investments are not subject to bail-in, and there is a minimal risk of insolvency.

**Money Market Funds:** An open ended fund that invests in short term debt securities, offers same-day liquidity and very low volatility.

**Mixed Asset Funds:** Rather than focus on a particular asset class, these funds will look to invest across a broader range of classes in an effort to provide investors with a smoother performance on a year-to-year basis. Primarily, the asset classes will be equities and fixed income, but the latter will include both corporate and government-level investments.

**Pooled Property Funds:** Shares in diversified property investment vehicles. Property funds offer enhanced returns over the longer term but are more volatile in the short term. The funds have no defined maturity date, but are available for withdrawal after a notice period

**Short Dated Bond Funds:** Funds designed to produce an enhanced return over and above an Ultra Short Dated Fund. The manager may use a wider range of alternative options to try and generate excess performance. These could include different counterparties, instruments as well as longer dated and a proportion of lower rated investments. The return on the funds are typically much higher but can be more volatile than Ultra-Short Dated bond funds, so a longer investment time horizon is recommended.

**ANNEX F**
**LOCAL GOVERNMENT OUTLOOK**

The Chancellor announced the Autumn Budget Statement on 22 November, accompanied by new national economic forecasts from The Office for Budget Responsibility (OBR). The OBR judged that overall growth would be 0.7% in 2024, rising to 1.4% in 2025, and then an average of 1.9% between 2026 and 2028. Debt and borrowing forecasts were lower than at the March 2023 Budget, with debt expected to hit a peak of 93.2% of Gross Domestic Product (GDP) in 2026/27 before falling to 92.8% in 2028/29. The unemployment rate was predicted to peak at 4.6%, later than expected, in 2025 before falling to 4.1%.

The OBR forecasted that headline inflation will remain higher for longer than previously predicted, falling to 2.8% by the end of 2024 and not reaching the 2% target rate until 2025 – this revised projection has impacts for our ongoing operating costs. The Bank of England held interest rates at 5.25% in December in support of its ongoing strategy to curb inflation, with some analysts predicting rates may begin to fall during 2024 as inflation reduces further.

The increased cost of living has continued to impact on households, although inflation, as measured by the Consumer Prices Index (CPI), reduced to 3.9% in the 12 months to November (down from 4.6% in October), a larger than expected reduction. The falls in recent months have been driven by a significant drop in the cost of energy from the peak in autumn 2022 and slower growth in the cost of food and fuel. However, the ongoing high rate, on top of previous price increases, continues to create significant pressures on households, particularly those on low incomes.

Children's Services have continued to experience significant pressures from rising demand and increased complexity of need, coupled with workforce shortages and a lack of specialist placements, all of which has led to escalating costs and operational challenges over the past year. Overspends in Children's Services are significant and commonplace across Local Government, reflecting a national issue.

The provisional Local Government Finance Settlement, received on 18 December, provided the detailed funding picture for local government and was again for one year only. It indicated that Core Spending Power would increase by an average 6.5% for local authorities in England, based on the presumption that all councils will levy the maximum increase in Council Tax. The Council Tax referendum limit was maintained at 3% and the Adult Social Care precept at 2%. The continuation of a range of short-term grants was confirmed, including grant funding for social care, but crucially, there was no additional funding over and above the funding announcement in the 2022 Settlement.

In response to cost pressures on councils the Department for Levelling Up, Housing and Communities (DLUHC) instead advised the use of reserves to maintain services and for investment to be made in preventative approaches in children's services where possible to improve the sustainability of children's social care.

For Local Government, there is a continued reliance on raising funding through council tax, which is unrelated to need, with remaining budget gaps mitigated through use of one-off reserves. This is unsustainable, and the sector continues to lobby for a sustainable funding settlement to enable councils to continue to set balanced budgets.