

# Treasury Management Strategy 2024/25 to 2028/29

For Consideration by Cabinet 6 February 2024

## 1 INTRODUCTION

### 1.1 Background

The Council is required to operate a balanced budget, which means broadly that income to be raised during the year will meet expenditure to be incurred, after allowing for any changes in reserves and balances. Part of the treasury management operation is to ensure that the associated cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's low 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 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.

Whilst any commercial initiatives or loans to third parties will impact on the treasury function, these activities are generally classed as non-treasury activities, (arising usually from capital expenditure) and are separate from the day to day treasury management activities.

The Chartered Institute of Public Finance and Accountancy (CIPFA) defines treasury management as:

*“The management of the local 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.”*

## 1.2 Reporting Requirements

### Capital Strategy

The CIPFA 2021 Prudential and Treasury Management Codes require, all local authorities to prepare an additional report, a capital strategy report, which will 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 this capital strategy is to ensure that all elected members on the full council fully understand the overall long-term policy objectives and resulting capital strategy requirements, governance procedures and risk appetite.

### Treasury Management Reporting

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

**Prudential and treasury indicators and treasury strategy** (this report) - The first, and most important report 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 Annual Investment Strategy (the parameters on how investments are to be managed).

**A mid-year treasury management report** – This will update Members with the progress of the treasury position, amending prudential indicators as necessary, and whether any policies require revision. In addition the Authority will receive quarterly update reports.

**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.

**Scrutiny** - The above reports are required to be adequately considered and scrutinised before being presented to Council. This is undertaken by Cabinet and the Budget and Performance Panel.

**Quarterly reports** - In addition to the three major reports detailed above, from 2023/24 quarterly reporting (end of June/end of December) is also required. However, these additional reports do not have to be reported to Full Council/Board but do require to be adequately scrutinised. This role is undertaken by Budget & Performance Panel.

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

The strategy for 2024/25 covers two main areas:

#### **Capital Issues**

- the capital plans and the prudential indicators;
- the minimum revenue provision (MRP) policy.

#### **Treasury Management Issues**

- the current treasury position;
- treasury indicators which limit the treasury risk and activities of the Council;
- prospects for interest rates;
- the borrowing strategy;
- policy on borrowing in advance of need;
- debt rescheduling;
- the investment strategy;
- creditworthiness policy; and
- policy on use of external service providers.

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

### **1.4 Training**

The CIPFA Code requires the responsible officer to ensure that Members with responsibility for treasury management receive adequate associated training. This especially applies to Members responsible for scrutiny.

Furthermore, pages 47 and 48 of the Code state that they expect “all organisations to have a formal and comprehensive knowledge and skills or training policy for the effective acquisition and retention of treasury management knowledge and skills for those responsible for management, delivery, governance and decision making.

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.

A member training session has been arranged prior to Budget & Performance Panel on 14 February and further training will be arranged during the forthcoming year as required.

A formal record of the training received by officers central to the Treasury function will be maintained by the Accountancy Services Manager. Similarly, a formal record of the treasury management/capital finance training received by members will also be maintained by the Chief Resources & S151 Officer.

The training needs of treasury management Officers are periodically reviewed.

### **1.5 Treasury Management Consultants**

The Council uses Link Group, Treasury solutions as its external treasury management advisors.

The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon external service providers. All decisions will be undertaken with regards to all available information, including, but not solely, our treasury advisers.

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 and documented, and subjected to regular review.

## **2 CAPITAL PRUDENTIAL INDICATORS 2023/24 – 2028/29**

The Council's capital expenditure plans are the key driver of treasury management activity. The plans are reflected in various prudential indicators which are designed to assist members' overview and confirm capital expenditure plans are prudent, affordable and sustainable.

### **2.1 Capital Expenditure**

This prudential indicator is a summary of the Council's capital expenditure plans, both those agreed previously, and those forming part of this budget cycle.

The table below provides that summary, showing how the plans are being financed by capital or revenue resources. Any shortfall of resources results in an underlying borrowing or financing need.

<b>Capital expenditure</b>	<b>2022/23 Actual £m</b>	<b>2023/24 Estimate £m</b>	<b>2024/25 Estimate £m</b>	<b>2025/26 Estimate £m</b>	<b>2026/27 Estimate £m</b>	<b>2027/28 Estimate £m</b>	<b>2028/29 Estimate £m</b>
General Fund	10.44	10.62	17.01	18.09	4.34	4.09	4.81
Housing Revenue Account (HRA)	5.31	8.33	4.77	3.93	3.90	4.19	4.35
<b>Total</b>	<b>15.75</b>	<b>18.95</b>	<b>21.78</b>	<b>22.02</b>	<b>8.24</b>	<b>8.28</b>	<b>9.16</b>
<b>Financed by:</b>							
Capital receipts	-0.22	-1.82	-0.16	-0.00	-0.00	-0.00	-0.00
Capital grants	-5.15	-4.92	-10.73	-4.83	-2.42	-2.34	-2.33
Capital reserves	-4.94	-3.72	-4.32	-3.93	-3.90	-4.19	-4.35
Revenue	-0.83	-2.47	-0.04	-0.00	-0.00	-0.00	-0.00
<b>Net financing need for the year</b>	<b>4.61</b>	<b>6.02</b>	<b>6.53</b>	<b>13.26</b>	<b>1.92</b>	<b>1.75</b>	<b>2.48</b>

## 2.2 The Council's Borrowing Need (the Capital Financing Requirement)

The second prudential indicator is the Council's Capital Financing Requirement (CFR). The CFR is simply the total amount of capital expenditure (including that from prior years) that has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's indebtedness and so its underlying need to borrow. Any capital expenditure, which has not immediately been paid for through a revenue or capital resource, will increase the CFR.

The CFR does not increase indefinitely. This is because the Minimum Revenue Provision (MRP), which is a statutory annual charge to revenue, broadly reduces the indebtedness in line with each asset's life.

The CFR includes any other long term liabilities (e.g. finance leases). Whilst these increase the CFR, and therefore the Council's borrowing requirement, these types of schemes include a borrowing facility and so the Council is not required to separately borrow for these schemes. The Council currently has no leases within the CFR.

Members are asked to approve the CFR projections below:

£m	2022/23 Actual £m	2023/24 Estimate £m	2024/25 Estimate £m	2025/26 Estimate £m	2026/27 Estimate £m	2027/28 Estimate £m	2028/29 Estimate £m
<b>Capital Financing Requirement</b>							
CFR – Non Housing	63.56	66.95	70.47	80.54	77.81	74.99	73.00
CFR – Housing	35.13	34.09	33.05	32.00	30.96	29.92	28.88
<b>Total CFR</b>	<b>98.69</b>	<b>101.04</b>	<b>103.52</b>	<b>112.54</b>	<b>108.77</b>	<b>104.91</b>	<b>101.88</b>
<b>Movement in CFR</b>							
Non Housing	4.50	3.38	3.52	10.07	-2.73	-2.82	-1.99
Housing	-1.04	-1.04	-1.04	-1.04	-1.04	-1.04	-1.04
<b>Net Movement in CFR</b>	<b>3.46</b>	<b>2.34</b>	<b>2.48</b>	<b>9.03</b>	<b>-3.77</b>	<b>-3.86</b>	<b>-3.03</b>

<b>Movement in CFR represented by</b>							
Net financing need for the year (above) re Non Housing	4.61	6.02	6.53	13.26	1.92	1.75	2.48
Less MRP/VRP and other financing movements	-1.15	-3.68	-4.05	-4.23	-5.69	-5.61	-5.51
<b>Net Movement in CFR</b>	<b>3.46</b>	<b>2.34</b>	<b>2.48</b>	<b>-9.03</b>	<b>-3.77</b>	<b>-3.86</b>	<b>-3.03</b>

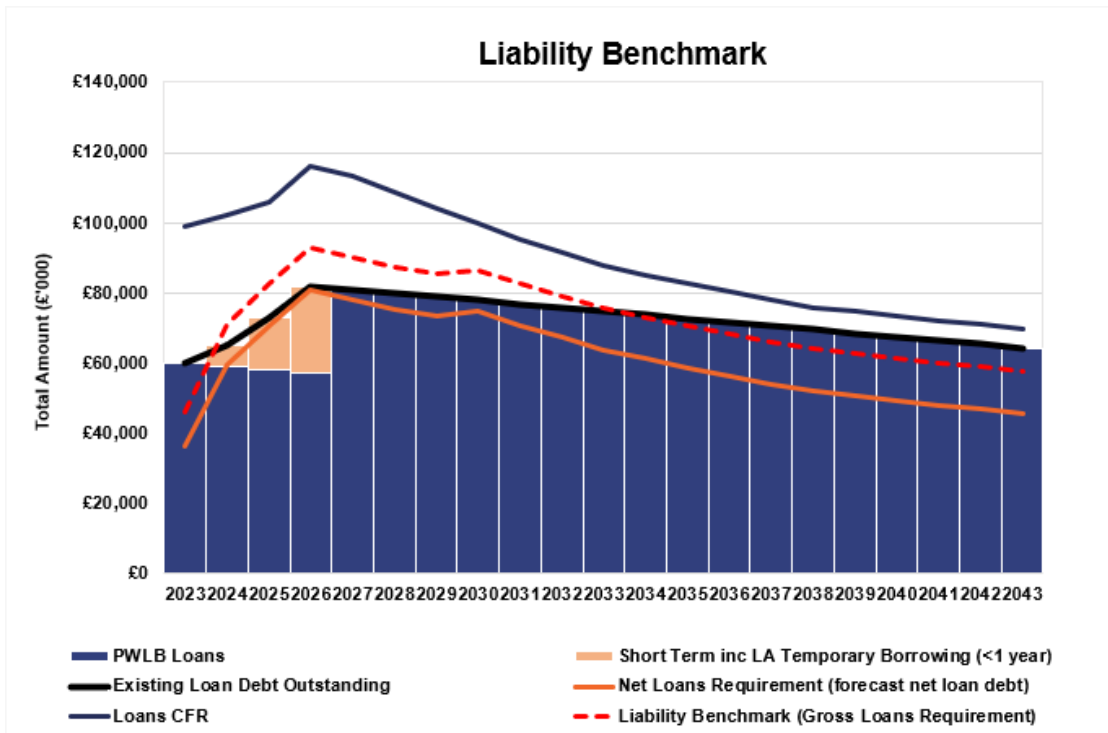
### 2.3 Liability Benchmark

The Council is required to estimate and measure the Liability Benchmark (LB) for the forthcoming financial year and the following two financial years, as a minimum.

There are four components to the LB: -

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 Council's liability benchmark presented as a chart of the above four balances is shown below:



Any years where actual loans are less than the benchmark indicate a future borrowing requirement.

During 23/24 forecast levels of funds available for treasury investments is falling in line with cash flow forecasts and as overall levels of General Fund and HRA reserves decrease.

There is, therefore, a need to borrow to cover the net loans requirement. Given PWLB interest rates at present, temporary borrowing from other local authorities will be utilised until PWLB rates reduce.

It is intended that the gap between the net loans requirement and the liability benchmark (gross loans requirement) will be covered by day-to-day working cashflow surpluses.

## 2.4 Core Funds and Expected Investment Balances

The application of resources (capital receipts, reserves etc.) to either finance capital expenditure or other budget decisions to support the revenue budget will have an ongoing impact on investments, unless resources are supplemented each year from new sources (e.g. asset sales). The following table provides estimates of the year end balances for each resource and anticipated year end cash flow balances from other day to day activities:

Year End Resources	2022/23 Actual £m	2023/24 Estimate £m	2024/25 Estimate £m	2025/26 Estimate £m	2026/27 Estimate £m	2027/28 Estimate £m	2028/29 Estimate £m
Fund balances / reserves	33.85	24.78	25.20	26.91	27.69	27.84	27.76
Capital receipts	2.39	0.00	0.00	0.00	0.00	0.00	0.00
Provisions	4.74	5.00	5.00	5.00	5.00	5.00	5.00
<b>Total core funds</b>	<b>40.98</b>	<b>29.78</b>	<b>30.20</b>	<b>31.91</b>	<b>32.69</b>	<b>32.84</b>	<b>32.76</b>
Working capital*	19.02	15.00	15.00	15.00	15.00	15.00	15.00
Under borrowing	-39.69	-37.07	-31.59	-31.66	-28.93	-26.11	-24.12
<b>Expected investments</b>	<b>20.31</b>	<b>7.71</b>	<b>13.61</b>	<b>15.25</b>	<b>18.76</b>	<b>21.73</b>	<b>23.64</b>

\*Working capital balances shown are estimated year end; these may be higher mid-year

## 2.5 Minimum Revenue Provision (MRP) Policy Statement

Under Regulation 27 of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, where the Authority has financed capital expenditure by borrowing it is required to make a provision each year through a revenue charge (MRP).

Regulation 28 of the Local Authorities (Capital Finance and Accounting) (England) (Amendment) regulations 2008 require the Authority to calculate a prudent provision of MRP whilst having regard to the current MRP Guidance (2018). The broad aim of prudent provision is to ensure that the outstanding debt liability is repaid over a period that is reasonably commensurate with that over which the capital expenditure provides benefits. The Guidance gives four ready-made options for calculating MRP but the Authority can use any other reasonable basis that it can justify as prudent.

The MRP policy statement requires full Council approval in advance of each financial year.

It is recommended that Council approves the following MRP Policy Statement.

- Supported borrowing incurred before 1st April 2008 will apply the Asset Life Method using an annuity method over 60 years.
- Unsupported borrowing will be subject to MRP using the Asset Life Method, which will be charged over a period which is reasonably commensurate with the average estimated useful life of the assets. An annuity method will be applied for the MRP calculation.
- Unsupported borrowing on vehicles will be subject to MRP using the Asset Life Method, which will be charged over a period which is reasonably commensurate with the estimated useful life of the vehicles. An annuity method will be applied for the MRP calculation.



- The interest rate applied to the annuity calculations will reflect the market conditions at the time. For the current financial year the interest rate used will be the Authority's weighted average borrowing rate.
- MRP will commence in the financial year following the one in which the expenditure was incurred, or in the year after the asset becomes operational.
- MRP in respect of unsupported borrowing taken to meet expenditure, which is treated as capital expenditure by virtue of either a capitalisation direction or regulations, will be determined in accordance with the asset life method as recommended by the MRP guidance.
- MRP in respect of assets acquired under PFI or Finance Leases will be charged at a rate equal to the principal element of the annual lease rental for the year in question.
- MRP Overpayments - The MRP Guidance allows that any charges made in excess of the statutory MRP, i.e. voluntary revenue provision (VRP) or overpayments, can be reclaimed in later years if deemed necessary or prudent. In order for these sums to be reclaimed for use in the budget, this policy must disclose the cumulative overpayment made each year. The VRP overpayments up to 31st March 2022 are £11.45m.
- On an annual basis the Section 151 officer shall review the level of MRP to be charged, to determine if this is at a level which is considered prudent based on the Authority's circumstances at that time, taking into account medium / long term financial plans, current budgetary pressures, current and future capital expenditure plans. Dependant on this review the Section 151 officer will adjust the annual MRP charge by making VRP or reclaiming previous VRP. The amount of MRP charged shall not be less than zero in any financial year.

## **2.6 Affordability Prudential Indicators**

The previous sections cover the overall capital and control of borrowing prudential indicators, but within this framework prudential indicators are required to assess the affordability of the capital investment plans. These provide an indication of the impact of the capital investment plans on the Council's overall finances. Members are asked to approve the following indicators:

## **2.7 Ratio of Financing Costs to Net Revenue Stream**

This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

	2022/23 Actual £m	2023/24 Estimate £m	2024/25 Estimate £m	2025/26 Estimate £m	2026/27 Estimate £m	2027/28 Estimate £m	2028/29 Estimate £m
General Fund	5.90	19.94	18.20	20.20	24.65	23.79	22.30
HRA	18.79	17.00	16.22	16.25	15.99	15.75	15.75

The estimates of financing costs include current commitments and the proposals in this budget report.

### 3 BORROWING

The capital expenditure plans set out in Section 2 provide details of the service activity of the Council. The treasury management function ensures that the Council's cash is organised in accordance with the the relevant professional codes, so that sufficient cash is available to meet this service activity and the Council's 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.

#### 3.1 Current Portfolio Position

The Council's forward projections for borrowing are summarised below. The table shows the actual external debt, against the underlying capital borrowing need (the Capital Financing Requirement or CFR), highlighting any over or under borrowing.

	2022/23 Actual £m	2023/24 Estimate £m	2024/25 Estimate £m	2025/26 Estimate £m	2026/27 Estimate £m	2027/28 Estimate £m	2028/29 Estimate £m
<b>External Debt</b>							
Debt at 1 April	60.05	59.01	63.97	71.93	80.88	79.84	78.80
Expected change in Debt	-1.04	4.96	7.96	8.95	-1.04	-1.04	-1.04
Other long-term liabilities (OLTL)	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Expected change in OLTL	0.00	0.00	0.00	0.00	0.00	0.00	0.00
<b>Actual gross debt at 31 March</b>	<b>59.01</b>	<b>63.97</b>	<b>71.93</b>	<b>80.88</b>	<b>79.84</b>	<b>78.80</b>	<b>77.76</b>
<b>The Capital Financing Requirement</b>	98.69	101.04	103.52	112.54	108.77	104.91	101.88
<b>Under Borrowing</b>	<b>-39.69</b>	<b>-37.07</b>	<b>-31.59</b>	<b>-31.66</b>	<b>-28.93</b>	<b>-26.11</b>	<b>-24.12</b>

There are a number of key indicators to ensure that the Council operates its activities within well defined limits. One of these is that the Council needs to ensure that its gross debt does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2024/25 and the following two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue or speculative purposes.

The Chief Resources & Section 151 Officer reports that the Council complied with this prudential indicator in the current year and does not envisage difficulties for the future. This view takes into account current commitments, existing plans, and the proposals in the budget report.

### 3.2 Treasury Indicators: Limits to Borrowing Activity

#### The Operational Boundary

This is the limit beyond which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt and the ability to fund under-borrowing by other cash resources.

Operational boundary	2023/24 Estimate £m	2024/25 Estimate £m	2025/26 Estimate £m	2026/27 Estimate £m	2027/28 Estimate £m	2028/29 Estimate £m
Debt*	101.04	103.52	112.54	108.77	104.91	101.88
Other long term liabilities	1.00	1.00	1.00	1.00	1.00	1.00
<b>Total</b>	<b>102.04</b>	<b>104.52</b>	<b>113.54</b>	<b>109.77</b>	<b>105.91</b>	<b>102.88</b>

#### The Authorised Limit for External Debt

A further key prudential indicator represents a control on the maximum level of borrowing. This represents a legal limit beyond which external debt is prohibited,

and this limit needs to be set or revised by the full Council. It reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

1. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total of all councils' plans, or those of a specific council, although this power has not yet been exercised.
2. Council is asked to approve the following authorised limit:

<b>Authorised Limit</b>	<b>2023/24 Estimate £m</b>	<b>2024/25 Estimate £m</b>	<b>2025/26 Estimate £m</b>	<b>2026/27 Estimate £m</b>	<b>2027/28 Estimate £m</b>	<b>2028/29 Estimate £m</b>
Debt	116.00	119.00	128.00	124.00	120.00	117.00
Other long-term liabilities	1.00	1.00	1.00	1.00	1.00	1.00
<b>Total</b>	<b>117.00</b>	<b>120.00</b>	<b>129.00</b>	<b>125.00</b>	<b>121.00</b>	<b>118.00</b>

### 3.3 Prospects for Interest Rates

The Council has appointed Link Group as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. Link provided forecasts on 08.01.2024. These are forecasts for certainty rates, gilt yields plus 80 bps:

	<b>Mar-24</b>	<b>Mar-25</b>	<b>Mar-26</b>	<b>Mar-27</b>
Bank Rate	5.25	3.75	3.00	3.00
3 Month average earnings	5.30	3.80	3.00	3.00
6 Month average earnings	5.20	3.70	3.10	3.10
12 Month average earnings	5.00	3.60	3.10	3.20
5yr PWLB rate	4.50	4.10	3.60	3.50
10yr PWLB rate	4.70	4.20	3.80	3.70
25yr PWLB rate	5.20	4.60	4.20	4.10
50yr PWLB rate	5.00	4.40	4.00	3.90

*Further commentary by Link on this forecast table: -*

*Our central forecast for interest rates was previously updated on 7 November and reflected a view that the MPC would be keen to further demonstrate its anti-inflation credentials by keeping Bank Rate at 5.25% until at least the second half of 20-24. We expect rate cuts to start when both the CPI inflation and wage/employment data are supportive of such a move, and when there is*

*a likelihood of the overall economy enduring at least a slowdown or mild recession over the coming months.*

*Naturally, timing on this matter will remain one of fine judgment: cut too soon, and inflationary pressures may well build up further; cut too late and any downturn or recession may be prolonged.*

*In the upcoming months, our forecasts will be guided not only by economic data releases and clarifications from the MPC over its monetary policies and the Government over its fiscal policies, but also international factors such as policy development in the US and Europe, the provision of fresh support packages to support the faltering recover in China as well as the ongoing conflict between Russia and Ukraine, and Gaza and Israel.*

## **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 Eurozone. At the time of writing there is circa 70 basis points difference between the 5 and 50 year parts of the curve.*

***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 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.*

*As there are so many variables at this time, caution must be exercised in respect of all interest rate forecasts. Naturally, we continue to monitor events and will update our forecasts as and when appropriate.*

### **3.4 Borrowing Strategy**

The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the Council's provisions, reserves, balances and working capital has been used as a temporary measure. This strategy is prudent as medium and longer dated borrowing rates are expected to fall from their current levels once prevailing inflation concerns are addressed by tighter near-term monetary policy. That is, Bank Rate remains elevated through to the second half of 2024.

Against this background and the risks within the economic forecast, caution will be adopted with the 2024/25 treasury operations. The Section 151 Officer, under delegated powers will 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 would be postponed.*

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

Any decisions will be reported to Cabinet at the next available opportunity.

### 3.5 Maturity Structure of Borrowing

These gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing and are required for upper and lower limits.

The Council is asked to approve the following indicators and limits:

<b>Maturity structure of fixed interest rate borrowing 2022/23</b>	<b>£m</b>	<b>Current %</b>	<b>Lower %</b>	<b>Upper %</b>
Under 12 months	1.04	1.63	0	100
12 months and within 24 months	7.04	11.01	0	100
24 months and within 5 years	3.12	4.88	0	100
5 years and within 10 years	5.21	8.14	0	100
10 years and within 20 years	8.33	13.02	0	100
20 years and within 30 years	0.00	0.00	0	100
30 years and within 40 years	39.22	61.32	0	100
40 years and within 50 years	0.00	0.00	0	100

### 3.6 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. Any decision to borrow in advance will be within forward 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.

### 3.7 Debt Rescheduling

Rescheduling of current borrowing in our debt portfolio may be considered whilst premature redemption rates remain elevated but only if there is surplus cash available to facilitate any repayment, or rebalancing of the portfolio to provide more certainty is considered appropriate.

If rescheduling was done it would be reported to Cabinet at the earliest meeting following its action.

## 4 ANNUAL INVESTMENT STRATEGY

### 4.1 Investment Policy – Management of Risk

The Department of Levelling Up, Housing and Communities (DLUHC) and CIPFA have extended the meaning of ‘investments’ to include both financial and non-financial investments. This report deals solely with financial investments, (as managed by the treasury management team). Non-financial investments, essentially the purchase of income yielding assets, are covered in the Capital Strategy (a separate report).

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 security first, liquidity second, then return.

The Council will aim to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity and with the Council’s risk appetite.

In the current economic climate, it is considered appropriate to maintain a degree of liquidity to cover cash flow needs but also to consider “laddering” investments for periods up to 12 months with high credit rated financial institutions, whilst investment rates remain elevated, as well as wider range fund options.

The above 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:

1. 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.
2. **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 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.
3. **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.
4. The authority has defined the list of types of investment instruments that the treasury management team are authorised to use. There are two lists in **annex B2** under the categories of ‘specified’ and ‘non-specified’ investments.

- **Specified investments** are those with a high level of credit quality and subject to a maturity limit of one year or have less than a year left to run to maturity, if originally they were classified as being non-specified investments solely due to the maturity period exceeding one year.
  - **Non-specified investments** are those with less high credit quality, may be for periods in excess of one year, and/or more complex instruments which require greater consideration by members and officers before being authorised for use.
5. **Non-specified investments limit.** The Council has determined that it will limit the maximum total exposure to non-specified investments as being 20% of the total investment portfolio. (see paragraph 4.3)
  6. **Lending limits** (amounts and maturity), for each counterparty will be set through applying the matrix table in paragraph 4.2
  7. **Transaction limits** are set for each type of investment in 4.2
  8. The Council will set a limit for the amount of its investments which are invested for **longer than 365 days** (see paragraph 4.4)
  9. Investments will only be placed with counterparties from countries with a specified minimum **sovereign rating** (see paragraph 4.3)
  10. The Council has engaged **external consultants** (see paragraph 1.5), 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.
  11. All investments will be denominated in **sterling**.
  12. As a result of the change in accounting standards for 2023/24 under IFRS9, the 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.

The Council 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.

#### **Changes in risk management policy from last year.**

The above criteria are unchanged from last year

#### **4.2 Creditworthiness Policy**

This Council will apply the creditworthiness service provided by Link Asset Services. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies - Fitch, Moody's and Standard and Poor's. The credit ratings of counterparties are 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 modelling approach combines credit ratings, credit watches and credit outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads for which the end product is 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 will therefore use counterparties within the following durational bands:

- **Yellow (Y)** up to but less than 1 year
- **Dark pink (Pi1)** liquid - Ultra-Short Dated Bond Funds with a credit score of 1.25
- **Light pink (Pi2)** liquid – Ultra-Short Dated Bond Funds with a credit score of 1.5
- **Purple (P)** up to but less than 1 year
- **Blue (B)** up to but less than 1 year (only applies to nationalised or part- nationalised UK Banks)
- **Orange (O)** up to but less than 1 year
- **Red (R)** 6 months
- **Green (G)** 100 days
- **No colour (N/C)** not to be used

Y	Pi1	Pi2	P	B	O	R	G	N/C
1	1.25	1.5	2	3	4	5	6	7

	Colour (and long term rating where applicable)	Money Limit	Time Limit
Banks /UK Govt. backed instruments*	yellow	£12m	≤1 year
Banks	purple	£6m	≤1 year
Banks	orange	£6m	≤1 year
Banks – part nationalised	blue	£12m	≤1 year
Banks	red	£6m	≤6 mths
Banks	green	£3m	≤100 days
Banks	No colour	Not to be used	
Limit 3 category – Council's banker (for non-specified investments)	n/a	£1.5m	1 day
DMADF	UK sovereign rating	unlimited	≤6 months
Local authorities	n/a	£12m	≤1 year
	Fund rating**	Money and/or % Limit	Time Limit

Money Market Funds CNAV	AAA	£6m	liquid
Money Market Funds LVNAV	AAA	£6m	liquid
Money Market Funds VNAV	AAA	£6m	liquid
Ultra-Short Dated Bond Funds with a credit score of 1.25	Dark pink / AAA	£6m	liquid
Ultra-Short Dated Bond Funds with a credit score of 1.5	Light pink / AAA	£6m	liquid

\* the yellow colour category includes UK Government debt, or its equivalent, money market funds and collateralised deposits where the collateral is UK Government debt – see Annex B2.

\*\* “fund” ratings are different to individual counterparty ratings, coming under either specific “MMF” or “Bond Fund” rating criteria.

The creditworthiness service uses a wider array of information other than just primary ratings and by using a risk weighted scoring system, does not give undue preponderance to just one agency’s ratings.

Typically the minimum credit ratings criteria (built in) that the Council use will be a Short Term rating of F1 and a Long Term rating of A- (Fitch, or equivalents). 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.

All credit ratings will be monitored daily. The Council is alerted to changes to ratings of all three agencies through its use of the creditworthiness service.

- If a downgrade results in the counterparty / 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 will be advised of information in movements in credit default swap spreads against the iTraxx European Senior financials benchmark and other market data on a daily basis via its Passport website, provided exclusively to it by Link. Extreme market movements may result in downgrade of an institution or removal from the Council’s lending list.

Sole reliance will not be placed on the use of this external service. In addition, the Council will also use to some limited extent market data and market information, information on sovereign support for banks and the credit ratings of that supporting government to help support its decision making process.

### **Creditworthiness**

Significant levels of downgrades to Short- and Long-Term credit ratings have not materialised since the crisis in March 2020. In the main, where they did change, any alterations were limited to Outlooks. Nonetheless, when setting minimum sovereign debt ratings, the Council will not set a minimum rating for the UK.

## CDS prices

Although bank CDS prices, (these are market indicators of credit risk), spiked upwards during the days of the Truss/Kwarteng government, they have returned to more average levels since then. However, sentiment can easily shift, so it will remain important to undertake continual monitoring of all aspects of risk and return in the current circumstances. Link monitor CDS prices as part of their creditworthiness service to local authorities and the Council has access to this information via its Link-provided Passport portal.

### 4.3 Country Limits

Due care will be taken to consider the exposure of the Council's total investment portfolio to non-specified investments, countries, groups and sectors

- a) **Non-specified investment limit.** The Council has determined that it will limit the maximum total exposure to non-specified investments as being 20% of the total investment portfolio.
- b) **Country limit.** The Council has determined that it will only use approved counterparties from other countries with a minimum sovereign credit rating of AAA (Fitch) or equivalent from each of the credit rating agencies. This list will be added to, or deducted from, by Officers should ratings change in accordance with this policy.

### 4.4 Investment Strategy

**In-house Funds:** Investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (up to 12 months). Greater returns are usually obtainable by investing for longer periods. The current shape of the yield curve suggests that is the case at present, but there is the prospect of Bank Rate having peaked in the second half of 2023 and possibly reducing as early as the second half of 2024 so an agile investment strategy would be appropriate to maximise returns.

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

**Investment Returns Expectations:** The current forecast includes a forecast for Bank Rate to have peaked at 5.25%.

The suggested budgeted investment earnings rates for returns on investments placed for periods up to about three months during each financial year are:

- 2023/24 5.30%
- 2024/25 4.55%
- 2025/26 3.10%
- 2026/27 3.00%
- 2027/28 3.25%

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

**Investment treasury indicator and limit** - the total principal funds that can be invested for greater than 365 days. These limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment, and are based on the availability of funds after each year-end. Council is asked to approve the following treasury indicator and limit:

<b>Maximum principal sums invested &gt; 365 days</b>						
	<b>2023/24</b>	<b>2024/25</b>	<b>2025/26</b>	<b>2026/27</b>	<b>2027/28</b>	<b>2028/29</b>
Principal sums invested > 365 days	Nil	Nil	Nil	Nil	Nil	Nil

#### **4.5 End of year investment report**

At the end of the financial year, the Council will report on its investment activity as part of its Annual Treasury Report.

## Treasury Management Glossary of Terms

- **Annuity** – method of repaying a loan where the payment amount remains uniform throughout the life of the loan, therefore the split varies such that the proportion of the payment relating to the principal increases as the amount of interest decreases.
- **CIPFA** – the Chartered Institute of Public Finance and Accountancy, is the professional body for accountants working in Local Government and other public sector organisations, also the standard setting organisation for Local Government Finance.
- **Call account** – instant access deposit account.
- **Counterparty** – an institution (e.g. a bank) with whom a borrowing or investment transaction is made.
- **Credit Rating** – is an opinion on the credit-worthiness of an institution, based on judgements about the future status of that institution. It is based on any information available regarding the institution: published results, Shareholders' reports, reports from trading partners, and also an analysis of the environment in which the institution operates (e.g. its home economy, and its market sector). The main rating agencies are Fitch, Standard and Poor's, and Moody's. They currently analyse credit worthiness under four headings (but see changes referred to in the strategy):
  - **Short Term Rating** – the perceived ability of the organisation to meet its obligations in the short term, this will be based on measures of liquidity.
  - **Long Term Rating** – the ability of the organisation to repay its debts in the long term, based on opinions regarding future stability, e.g. its exposure to 'risky' markets.
  - **Individual/Financial Strength Rating** – a measure of an institution's soundness on a stand-alone basis based on its structure, past performance and credit profile.
  - **Legal Support Rating** – a view of the likelihood, in the case of a financial institution failing, that its obligations would be met, in whole or part, by its shareholders, central bank, or national government.

The rating agencies constantly monitor information received regarding financial institutions, and will amend the credit ratings assigned as necessary.

- **DMADF and the DMO** – The DMADF is the 'Debt Management Account Deposit Facility'; this is highly secure fixed term deposit account with the Debt Management Office (DMO), part of Her Majesty's Treasury.
- **EIP** – Equal Instalments of Principal, a type of loan where each payment includes an equal amount in respect of loan principal, therefore the interest due with each payment reduces as the principal is eroded, and so the total amount reduces with each instalment.
- **Gilts** – the name given to bonds issued by the U K Government. Gilts are issued bearing interest at a specified rate, however they are then traded on the markets like

shares and their value rises or falls accordingly. The Yield on a gilt is the interest paid divided by the Market Value of that gilt.

E.g. a 30 year gilt is issued in 1994 at £1, bearing interest of 8%. In 1999 the market value of the gilt is £1.45. The yield on that gilt is calculated as  $8\%/1.45 = 5.5\%$ .

See also PWLB.

- **Liquidity** – Relates to the amount of readily available or short term investment money which can be used for either day to day or unforeseen expenses. For example Call Accounts allow instant daily access to invested funds.
- **Maturity** – Type of loan where only payments of interest are made during the life of the loan, with the total amount of principal falling due at the end of the loan period.
- **Money Market Fund (MMF)** – Type of investment where the Council purchases a share of a cash fund that makes short term deposits with a broad range of high quality counterparties. These are highly regulated in terms of average length of deposit and counterparty quality, to ensure AAA rated status. As from 21 July 2018 there will be three structural options for existing money market funds – Public Debt Constant Net Asset Value (CNAV), Low Volatility Net Asset Value (LVNAV) and Variable Net Asset Value (VNAV)
- **Policy and Strategy Documents** – documents required by the CIPFA Code of Practice on Treasury Management in Local Authorities. These set out the framework for treasury management operations during the year.
- **Public Works Loans Board (PWLB)** – a central government agency providing long and short term loans to Local Authorities. Rates are set daily at a margin over the Gilt yield (see Gilts above). Loans may be taken at fixed or variable rates and as Annuity, Maturity, or EIP loans (see separate definitions) over periods of up to fifty years. Financing is also available from the money markets, however because of its nature the PWLB is generally able to offer better terms.
- **Link Asset Services** – Link Asset Services are the City Council's Treasury Management advisors. They provide advice on borrowing strategy, investment strategy, and vetting of investment counterparties, in addition to ad hoc guidance throughout the year.
- **SONIA** (Sterling Overnight Index Average) – this reflects the average of the interest rates that banks pay to borrow sterling overnight from other financial institutions and other institutional investors. It is used as a replacement for LIBOR (and LIBID calculations), the publication of which ceased at the close of 2021.
- **Yield** – see Gilts

Members may also wish to make reference to *The Councillor's Guide to Local Government Finance*.

## ANNEX B2

A variety of investment instruments will be used, subject to the credit quality of the institution, and depending on the type of investment made it will fall into one of the above categories.

The criteria, time limits and monetary limits applying to institutions or investment vehicles are:

	Minimum credit criteria / colour band	Max % of counterparty limit - *Specified	Max % of counterparty limit – **Non - Specified	Max. maturity period
<b>DMADF – UK Government</b>	N/A	<b>100%</b>	<b>N/A</b>	<b>6 months</b>
UK Government gilts	UK sovereign rating	100%	<b>N/A</b>	1 year
UK Government Treasury bills	UK sovereign rating	100%	<b>N/A</b>	1 year
Bonds issued by multilateral development banks	AAA	100%	<b>N/A</b>	6 months
Money Market Funds CNAV	AAA	100%	<b>N/A</b>	Liquid
Money Market Funds LVNAV	AAA	100%	<b>N/A</b>	Liquid
Money Market Funds VNAV	AAA	100%	<b>N/A</b>	Liquid
Ultra-Short Dated Bond Funds with a credit score of 1.25	AAA	100%	<b>N/A</b>	Liquid
Ultra-Short Dated Bond Funds with a credit score of 1.5	AAA	100%	<b>N/A</b>	Liquid
Local authorities	N/A	100%	<b>N/A</b>	1 year
Term deposits with banks and building societies	Yellow	100%	20%	Up to 1 year
	Purple	100%	20%	Up to 1 year
	Blue	100%	N/A	Up to 1 year
	Orange	100%	20%	Up to 1 year
	Red	100%	20%	Up to 6 Months
	Green	100%	20%	Up to 100 days
	No Colour	0%	0%	Not for use
Certificates of Deposit and corporate bonds with banks and building societies	Yellow	20%	0%	Up to 1 year
	Purple	20%	0%	Up to 1 year
	Blue	20%	0%	Up to 1 year
	Orange	20%	0%	Up to 1 year
	Red	0%	0%	Up to 6 Months
	Green	0%	0%	Up to 100 days
	No Colour	0%	0%	Not for use

**\*SPECIFIED INVESTMENTS:** All such investments will be sterling denominated, with maturities up to maximum of 1 year, meeting the quality criteria as applicable.

**\*\*NON-SPECIFIED INVESTMENTS:** These are any investments which do not meet the specified investment criteria. A maximum of up to 20% \*\* will be held in aggregate in relevant non-specified investments (as at the trade date of investing).

## Background information on credit ratings

Credit ratings are an important part of the Authority's investment strategy. The information below summarises some of the key features of credit ratings and why they are important.

### What is a Credit Rating?

A credit rating is:

- An independent assessment of an organisation;
- It gauges the likelihood of getting money back on the terms it was invested;
- It is a statement of opinion, not statement of fact;
- They help to measure the risk associated with investing with a counterparty;

### Who Provides / Uses Credit Ratings?

There are three main ratings agencies, all of which are used in the Authority's treasury strategy.

- Fitch
- Moody's Investor Services
- Standard & Poor's

The ratings supplied by these agencies are used by a broad range of institutions to help with investment decisions, these include:

- Local Authorities;
- Other non-financial institutional investors;
- Financial institutions;
- Regulators;
- Central Banks;

### Rating Criteria

There are many different types of rating supplied by the agencies. The key ones used by the Authority are ratings to indicate the likelihood of getting money back on terms invested. These can be split into two main categories:

- 'Short Term' ratings for time horizons of 12 months or less. These may be considered as the most important for local authorities.
- 'Long Term' ratings for time horizons of over 12 months. These may be considered as less important in the current climate.

In addition, the agencies issue sovereign, individual and support ratings which will also feed into the investment strategy.

### Rating Scales (Fitch, Moody's and Standard & Poor's)

The table below shows how some of the higher graded short and long term ratings compare across the agencies; the top line represents the highest grade possible. (There are other ratings that go much lower than those shown below, and ratings for other elements).

Short Term			Long Term		
Fitch	Moody's	S&P	Fitch	Moody's	S&P
F1+	P-1	A-1+	AAA	Aaa	AAA
F1	P-1	A-1	AA	Aa2	AA
F2	P-2	A-2	A	A2	A