

# TREASURY MANAGEMENT STRATEGY UPDATE 2024/25



## REPORT OF THE TREASURER

**For Approval**

### 1. PURPOSE OF REPORT

1.1 The purposes of the report are to:

- i) Provide a review of Treasury Management activity for 2023/24 including the 2023/24 outturn Prudential Indicators; and
- ii) Provide the second quarter update of the 2024/25 Treasury Management activity.

### 2. RECOMMENDATIONS

It is recommended that Members note the following:

- i) Note the 2023/24 Treasury Management outturn detailed in Section 4 and Appendix A.
- ii) Note the 2024/25 Treasury Management mid-year position detailed in section 5.
- iii) Note the Investment Strategy in Section 3 and Appendix B.

### 3. BACKGROUND

3.1 The Treasury Management Strategy covers:

- The strategy for the Authority's borrowing requirement arising from historic capital expenditure and the element of the approved Asset Management Plan funded from Prudential Borrowing; and
- The Annual Investment Strategy relating to the Authority's cash flow.

3.2 The Local Government Act 2003 requires the Authority to 'have regard to' the CIPFA (Chartered Institute of Public Finance and Accountancy) Prudential Code and to set prudential indicators for the next three years to ensure that the Authority's capital investment plans are affordable, prudent and sustainable.

- 3.3 The Act requires the Authority to set out a Treasury Management Strategy for borrowing and to prepare an Annual Investment Strategy, which sets out the policies for managing investments and for giving priority to the security and liquidity of those investments. The Secretary of State has issued Guidance on Local Government Investments which came into force on 1<sup>st</sup> April, 2004, and has subsequently been updated, most recently in 2021.
- 3.4 The Authority is required to nominate a body to be responsible for ensuring effective scrutiny of the Treasury Management Strategy and policies, before making recommendations to the full Authority. This responsibility has been allocated to the Audit and Governance Committee.
- 3.5 This report covers the following areas:
- Economic background and outlook for interest rates;
  - Treasury Management outturn position for 2023/24; and
  - Treasury Management Strategy 2024/25 second quarter review.

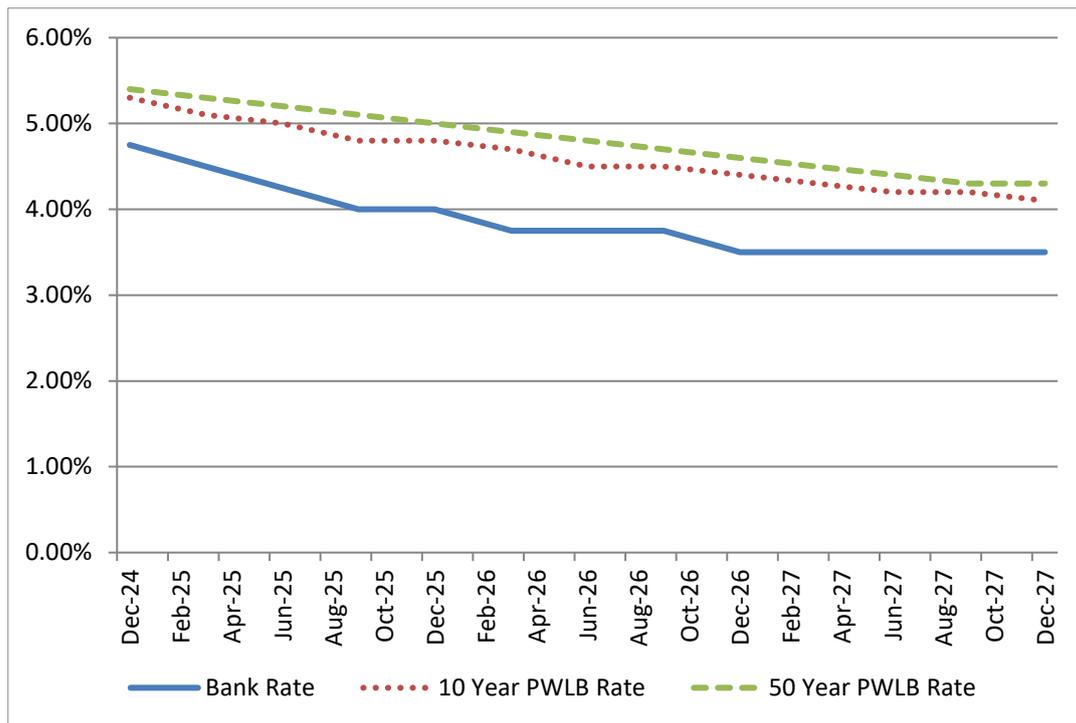
### 3.6 Economic Background and Outlook For Interest Rates

- 3.7 **UK** – The Bank of England’s (BoE) Monetary Policy Committee (MPC) opted to hold rates at 5.0% in its September meeting. At the November meeting it implemented a 0.25% interest reduction, lowering rates from 5.0% to 4.75%. The BoE Monetary policy stated interest rates will need to continue to remain restrictive for sufficiently long until the risks to inflation returning sustainably to the 2% target in the medium term have dissipated further. The BoE will closely monitor the risks of inflation persistence and will decide the appropriate degree of monetary policy restrictiveness at each meeting.
- 3.8 The latest Consumer Price Index (CPI) data shows that the UK CPI measure of inflation reduced to 1.7% in September (2.2% in August), but services inflation remained at 5.6% (5.9% August), significantly above its long-run average of 3.5%. CPI inflation is expected to rise in the coming months, with the October Budget forecasts rate for 2024/25 of 2.3%, 2025/26 – 2.6, before declining to around 2.0% by 2026/7. The increasing uncertainties of the Middle East may also exert an upward pressure on inflation, with oil prices rising in the aftermath of Iran’s missile attack on Israel on 1<sup>st</sup> October 2024.
- 3.9 The Office for Budget Responsibility’s revised growth forecasts up to 2028 are set out in the following table:

Year	March 2023 Growth Forecast	March 2024 Growth Forecast
2024	1.8%	0.8%
2025	2.5%	1.9%
2026	2.1%	2.0%
2027	1.9%	1.8%
2028		1.7%

- 3.10 **European Union (EU)** – Annual inflation rates in the Eurozone fell to 1.8% in September, the lowest since April 2001, compared to 2.2% in August. The annual core inflation rate in the Eurozone, excluding volatile items such as energy, food, alcohol and tobacco, decreased to a 5-month low of 2.7% in September from 2.8% in August, below expectations of 2.8%. The unemployment rate in the Eurozone was unchanged from the prior month at 6.4% in August, holding at its lowest on record, and in line with market expectations.
- 3.11 **Other Economies** – The Federal Reserve cut the target range in September by 0.5% to 4.75%-5.00%, the first reduction in borrowing costs since March 2020. While the decision to cut rates was anticipated, there was speculation about whether the central bank would choose a more conservative 0.25% reduction instead. The People’s Bank of China lowered its one-year medium term lending facility by 0.3% to 2.0% from 2.3% on 25<sup>th</sup> September 2024. The central bank introduced its most comprehensive economic stimulus measures since 2015 to revive the economy and restore market confidence and ongoing economic headwinds, including weak domestic demands and deflation risks.
- 3.12 **Interest Rate Forecasts**
- 3.13 Link Group (the Authority’s Treasury Management advisors) continue to update their interest rate forecasts to reflect statements made by the Governor of the Bank of England and changes in the economy.
- 3.14 In September the MPC reduced the Base Rate by 25bps to 4.75%, voting 8-1 in favour.
- 3.15 Link Group forecast is now 50bps-75bps higher than was previously the case, with the next Bank Rate cut in March 2025, with further cuts likely throughout 2025.
- 3.16 Economic and interest rate forecasting remains difficult with so many influences impacting on the economy. UK gilt yields (i.e. Government borrowing) and PWLB rates forecasts made by Link Group may be liable to further amendment depending on how the political and economic developments transpire over the next year.

### 3.17 Interest Rate Forecast up to December 2027



## 4. TREASURY MANAGEMENT OUTTURN POSITION 2023/24

### 4.1 **Capital Expenditure and Financing 2023/24**

4.2 The Authority's approved capital programme was funded from a combination of borrowing, the Capital Investment Programme Reserve, revenue contributions and capital receipts.

4.3 Actual capital expenditure forms one of the required prudential indicators. As shown at Appendix A, the total amount of capital expenditure for the year was £1.809m, funded by a mix of the Capital Investment Programme Reserve, revenue contributions, capital receipts and borrowing.

4.4 The Authority's underlying need to borrow is called the Capital Financing Requirement (CFR). This figure is the accumulated value of capital expenditure which is not funded from revenue or capital resources. Each year the Authority is required to apply revenue resources to reduce this outstanding balance termed the Minimum Revenue Provision.

4.5 Whilst the Authority's CFR sets a limit on the level of borrowing, the Authority can manage the actual borrowing position by either:

- borrowing externally to the level of the CFR; or
- choosing to use temporary internal cash flow funds instead of borrowing; or
- a combination of the two.

4.6 The Authority's CFR for the year was £9.680m as shown at Appendix A.

- 4.7 The Authority can also borrow for future planned increases in the CFR up to 3 years in advance, when this is deemed to be appropriate. As previously reported, in line with the approved Treasury Management Strategy, long term borrowing secured low interest rates to fund the business case for the Asset Management Plan.
- 4.8 The Authority's total long term external borrowing as at 31<sup>st</sup> March, 2024 was £8.796m, which funds 91% of the CFR up to 2024/25. The total borrowing remains below the CFR and there continues to be an element of netting down investments and borrowing (i.e. using cash backed reserves to delay borrowing). This is appropriate whilst interest rates remain at current levels and the Authority needs to carefully manage the timing of new borrowing to fund forecast capital expenditure to secure affordable interest rates.
- 4.9 **Prudential Indicators and Compliance Issues 2023/2024**
- 4.10 Details of each Prudential Indicator are shown at Appendix A. Some of the Prudential Indicators provide either an overview or specific limits on treasury activity. The key Prudential Indicators to report at outturn are described below.
- 4.11 The **Authorised Limit** is the "Affordable Borrowing Limit" required by Section 3 of the Local Government Act 2003. The Authority does not have the power to borrow above this level. Appendix A demonstrates that during 2023/2024 the Authority has maintained gross borrowing within the Authorised Limit.
- 4.12 **Gross Borrowing and the CFR** – In order to ensure that borrowing levels are prudent, over the medium term the Authority's external borrowing, must only be for a capital purpose. Gross borrowing should not exceed the CFR for 2023/24 plus the expected changes to the CFR over 2024/25 and 2025/26. The Authority has complied with this Prudential Indicator.
- 4.13 **The Treasury position at 31<sup>st</sup> March 2024**
- 4.14 The table below shows the Treasury position for the Authority as at the 31<sup>st</sup> March, 2024 compared with the previous year:

Treasury position	31st March 2023		31st March 2024	
	Principal	Average Rate	Principal	Average Rate
<b>Fixed Interest Rate Debt</b>				
- PWLB	£6.90	2.92%	£6.8m	2.92%
- Market Loans (LOBOs)	£2.0m	3.95%	£2.0m	3.95%
<b>Total Long Term Debt</b>	<b>£8.9m</b>	<b>3.15%</b>	<b>£8.8m</b>	<b>3.15%</b>
<b>Temporary Borrowing</b>	£3.00	4.20%	£0.8m	4.20%
<b>Total Investments</b>	<b>(£13.2m)</b>	<b>0.17%</b>	<b>(£12.1m)</b>	<b>5.60%</b>
<b>Net Debt / (Investment) Position</b>	<b>(£1.3m)</b>		<b>(£2.5m)</b>	

# A LOBO (Lender Option, Borrower Option) loan was taken out in March 2007 at which time interest rates for comparative PWLB loans were 4.3%.

- 4.15 A key performance indicator shown in the above table is the low average interest rate for external long term debt of 3.15% for debt held as at 31<sup>st</sup> March, 2024.
- 4.16 The Authority's investment policy is governed by Ministry of Housing, Communities and Local Government (MHCLG) guidance, which has been implemented in the annual investment strategy approved by Authority.
- 4.17 The Authority continues to keep under review the most opportune approach to borrowing. Given the increase in interest rates experienced during 2022, no long term borrowing has been entered into. However, during financial year end a short term loan was taken out for 1 week at a rate of 4.2% to manage the cash balances being used to manage the capital programme in the short -term.
- 4.18 As at the 30<sup>th</sup> September, the funds managed by the Authority amounted to £23.063m. All investments complied with the Annual Investment Strategy and are shown in the table below.

Borrower	Duration	Value of Investment (£m)	Rate (%)	Start Date	Maturity Date
<b>Call Accounts*</b>					
Svenska Handelsbanken	On Call	0.001	2.100		Call
NatWest Bank	On Call	0.002	1.150		Call
		<b>0.003</b>	<b>1.568</b>		
<b>Fixed term Deposits</b>					
CFB Risk Management	1 year	0.072	2.740		
Lloyds	1 year	5.000	5.910	06/10/23	04/10/24
Standard Charter	1 year	2.000	5.170	26/02/24	25/02/25
Goldman Sachs	1 year	2.000	5.230	15/04/24	15/04/25
Goldman Sachs	1 year	3.000	5.140	05/07/24	04/07/25
Natwest Markets Plc	1 year	5.000	5.000	26/07/24	25/07/25
Standard Chartered Bank	3 months	3.000	5.070	26/07/24	25/10/24
Debt Management Office	<1 month	1.127	4.905	19/09/24	15/10/24
Debt Management Office	<1 month	0.289	4.940	20/09/24	07/10/24
Debt Management Office	<1 month	1.000	4.940	30/09/24	01/10/24
		<b>22.488</b>	<b>5.251</b>		
<b>Money Market Funds</b>					
Blackrock	On Call	0.572	4.94		Call
<b>Total Deposits</b>		<b>23.063</b>	<b>5.242</b>		

- 4.19 The principals and hierarchy of security / liquidity / rate of return continue to be closely adhered to.
- 4.20 Investment benchmarking information for the year-ending March 2024 covering 249 authorities (provided by Link Group, our Treasury Management advisors), which measures the "weighted average rate of return" was 5.67%. This is in the upper quartile of performance. Further comparative information and an overview of the Investment Strategy is provided in **Appendix B**. These investments are providing one-off income to support the MTFs and further details will be reported to the Full Authority on 6<sup>th</sup> December 2024.

#### 4.21 **Regulatory Framework, Risk and Performance 2023/24**

4.22 The Authority's Treasury Management activities are regulated by a variety of professional codes, statutes and guidance:

- The Local Government Act 2003 (the Act), which provides the powers to borrow and invest as well as providing controls and limits on this activity;
- The Act permits the Secretary of State to set limits either on the Authority or nationally on all local authorities restricting the amount of borrowing which may be undertaken (although no restrictions have been made since this power was introduced);
- Statutory Instrument (SI) 3146 2003, as amended, develops the controls and powers within the Act, and requires the Authority to undertake any borrowing activity with regard to the CIPFA Prudential Code for Capital Finance in Local Authorities;
- The SI also requires the Authority to operate the overall treasury function with regard to the CIPFA Code of Practice for Treasury Management in the Public Services;
- Under the Act the DLUCH has issued Investment Guidance to structure and regulate the Authority's investment activities;
- Under section 238(2) of the Local Government and Public Involvement in Health Act 2007 the Secretary of State has taken powers to issue guidance on accounting practices. Guidance on Minimum Revenue Provision was issued under this section on 8<sup>th</sup> November, 2007.

4.23 The Authority has complied with all of the above relevant statutory and regulatory requirements which limit the levels of risk associated with Treasury Management activities.

### **5. TREASURY MANAGEMENT STRATEGY 2024/25 2<sup>nd</sup> QUARTER REVIEW**

5.1 The 2024/25 Treasury Management Strategy was approved on the 23<sup>rd</sup> February 2024. The Authority's borrowing and investment position as at 30<sup>th</sup> September 2024 is summarised as follows:

	<b>£m</b>	<b>Average Rate</b>
LOBO Loan #	2.0	3.95%
PWLB Loans	6.8	2.92%
<b>Gross Long Term Debt</b>	<b>8.8</b>	<b>3.15%</b>
Investments	23.1	5.24%
<b>Net Investment</b>	<b>14.3</b>	

# A LOBO (Lender Option, Borrower Option) loan was taken out in March 2007 at which time interest rates for comparative PWLB loans were 4.3%.

5.2 As part of the Treasury Management Strategy for 2024/25 the Authority set a number of Prudential Indicators. Compliance against these indicators is monitored on a regular basis and there are no breaches to report.

- 5.3 The CFR and Capital Expenditure Financed by Borrowing will vary from the original estimate approved by the Fire Authority in February 2024 owing to planned capital expenditure being re-phased between financial years.
- 5.4 **Investment Strategy** - there are no changes to the counterparty investment limits as agreed as part of the Investment strategy and set out in the table below.

Category	Fitch	Moody's	Standard & Poor's	Proposed Counterparty Limit	Proposed Time Limit
A	F1+/AA-	P-1/Aa3	A-1+/AA-	£7m	1 year
B	F1/A-	P-1/A3	A-1/A-	£5m	1 year
C	Debt Management Office/Treasury Bills/Gilts			£14m	1 year
D	Nationalised Banks			£5m	2 years
E	Other Local Authorities Individual Limits per Authority: - £3m County, Metropolitan or Unitary Councils - £1.5 District Councils, Police or Fire Authorities			£15m	2 years
F	Three Money Market Funds (AAA) with maximum investment of £1.5m per fund			£4.5m	Liquid (instant access)

- 5.5 **Borrowing Strategy** - In relation to the Authority's borrowing requirement for approved capital expenditure in 2024/25 it is not recommended that any new borrowing is undertaken during the current year as interest rates are expected to fall in future years. Therefore, by deferring borrowing decisions the Authority will not lock into these high interest rates.
- 5.6 It is recognised that there is a potential risk that current interest rates may prevail longer than currently anticipated. However, it is expected these rates will fall once the MPC is satisfied inflation is under control, although interest rates are unlikely to fall to the previously historical low level of recent years.
- 5.7 In the short-term any borrowing requirement for the approved 2024/25 capital programme will be funded from a combination of netting down investments and borrowing (in a similar way to an individual having an offset mortgage), or temporary borrowing for a short period if this is necessary. This approach will minimise the net overall costs of the Authority's investments and borrowing requirement.
- 5.8 **CIPFA Treasury Management Code of Practice**
- 5.9 The Authority has adopted the updated CIPFA Treasury Management Code of Practice published 20<sup>th</sup> December 2021.
- 5.10 **Treasury Management Advisors**
- 5.11 The Authority uses Link Group as its external treasury management advisors.

- 5.12 The Authority recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers.
- 5.13 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 Authority 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.

## **6. CONCLUSIONS**

- 6.1 The invasion of Ukraine by Russia resulted in significant inflation increase across the world, which lasted longer than forecast by central banks, despite there being a significant increase in interest rates. Within the UK the BoE increased to a peak of 5.5% (August 2023). This was from a low of 0.25% in January 2022.
- 6.2 The BoE commenced reducing interest rates in August 2024 with a 0.25% and further reduction are forecast over the remainder of 2024 and into 2025. The scale of these reductions will depend on the BoE assessment of inflation risks, which remain uncertain owing to international events.
- 6.3 The current economic environment makes Treasury Management significantly more challenging than it has been for over a decade. Against this background the recommended strategy is designed to manage these risks, minimise costs to the Authority of long term borrowing to fund the approved Asset Management Plan, and secure temporary investment income to support the Medium Term Financial Strategy. The Investment Strategy will continue to prioritise security of monies invested over interest return.
- 6.4 The report sets out how the Authority will comply with the regulatory framework to ensure the Council achieves the lowest borrowing costs and security for any temporary cash investments. Within this framework and the more uncertain / volatile financial environment officers will continue to actively manage borrowing and investments to support the overall financial position of the Authority.

**CHRIS LITTLE**  
**TREASURER**

**APPENDIX A****Prudential Indicators 2023/24 Outturn**1. Ratio of Financing Costs to Net Revenue Stream

This indicator shows the proportion of the total annual revenue budget that is funded by the local tax payer and Central Government, which is spent on servicing debt.

2023/24 Estimate £'000		2023/24 Outturn £'000
2.51%	Ratio of Financing costs to net revenue stream	2.56%

2. Capital Expenditure

This indicator shows the total capital expenditure for the year and the outturn reflects the actual phasing of capital expenditure.

2023/24 Estimate £'000		2023/24 Outturn £'000
3,342	Capital Expenditure	1,809

3. Capital Expenditure Financed from Borrowing

This shows the borrowing required to finance the capital expenditure programme.

2023/24 Estimate £'000		2023/24 Outturn £'000
1,835	Capital Expenditure Financed by Borrowing	1,314

The actual is lower than estimated owing to the phasing of capital expenditure between years.

4. Capital Financing Requirement (CFR)

CFR is used to determine the minimum annual revenue charge for capital expenditure repayments (net of interest). It is calculated from the Authority's Balance Sheet and is shown below. Forecasts for future years are directly influenced by the capital expenditure decisions taken and the actual amount of revenue that is set aside to repay debt.

2023/24 Estimate £'000		2023/24 Outturn £'000
10,860	Capital Financing Requirement	9,680

The capital financing requirement is lower than estimated owing to the phasing of capital expenditure.

#### 5. Authorised Limit for External Debt

The authorised limit determines the maximum amount the Authority may borrow at any one time. The authorised limit covers both long term borrowing for capital purposes and borrowing for short term cash flow requirements. The authorised limit is set above the operational boundary to provide sufficient headroom for operational management and unusual cash movements. In line with the Prudential Code, the level has been set to give the authority flexibility to borrow up to three years in advance of need if more favourable interest rates can be obtained.

2023/24 Limit £'000		2023/24 Peak £'000
14,000	Authorised limit for external debt	12,875

#### 6. Operational Boundary for External Debt

The operational boundary is the most likely prudent, but not worst case scenario, level of borrowing without the additional headroom included within the authorised limit. The level is set so that any sustained breaches serve as an early warning that the Authority is in danger of overspending or failing to achieve income targets and gives sufficient time to take appropriate corrective action. The external debt figure below includes temporary borrowing of £4.0m.

2023/24 Limit £'000		2023/24 Peak £'000
12,000	Operational boundary for external debt	12,875

#### 7. Interest Rate Exposures

This indicator is designed to reflect the risk associated with both fixed and variable rates of interest, but must be flexible enough to allow the Authority to make best use of any borrowing opportunities.

2023/24 Limit £'000	Upper limits on fixed and variable interest rate exposure	2023/24 Peak £'000
100% 75%	Fixed Rates Variable Rates	77% 23%

#### 8. Maturity Structure of Borrowing

This indicator is designed to reflect and minimise the situation whereby the Authority has a large repayment of debt needing to be replaced at a time of uncertainty over interest rates, but as with the indicator above, it must also be flexible enough to allow the Authority to take advantage of any borrowing opportunities.

	Upper Limit	Lower Limit	Actual by Maturity Date	Actual by soonest call date
	£'000	£'000	£'000	£'000
Under 12 months	8,000	0	102	2,102
12 month to 2 years	10,000	0	105	105
2 years to 5 years	10,000	0	334	334
5 years to 10 years	10,000	0	626	626
10 years to 20 years	10,000	0	1,559	1,559
20 years to 30 years	10,000	0	2,085	2,085
30 years to 40 years	10,000	0	1,986	1,986
40 years to 50 years	10,000	0	0	0
50 years to 60 years	10,000	0	2,000	0

The Authority's current outstanding borrowing includes a LOBO (Lender Option Buyer Option) loan which provide fixed interest rates for defined periods and also defined dates for reviewing interest rates, known as 'call dates'. A change to the Prudential Code requires that the call date is reflected in the Maturity Structure indicator above rather than maturity date. However the likelihood of a LOBO being 'called' at present is very low and both methods are presented above for completeness.

#### 9. Investments over Maturing over One Year

This sets an upper limit for amounts invested for periods longer than 364 days. The limit was not exceeded as a prudent approach to investment has been taken owing to uncertainties in the economy. This is in line with the Treasury Management Strategy. Consequently all investments made during the year were limited to a maximum of one year.

	1 year £000	2 year £000	3 year £000
Maximum Limit	5,000	0	0
Actual	0	0	0

**APPENDIX B****INVESTMENT STRATEGY UPDATE**

The Bank of England set the Base Rate at historically low levels (i.e. below 1%) over the period February 2009 to June 2022. This included significant periods at 0.1% or 0.25%. The Bank of England increased the base rate to 1.25% on 16<sup>th</sup> June 2022, there-after increasing rates on a regular basis to a peak of 5.25% in August 2024.

Against the background of low interest rates up to June 2022 the Authority's previous Treasury Management strategy netted down investments and borrowings as this position provided the lowest cost option.

In response to the sudden increase in market interest rates following the Liz Truss mini budget on 22<sup>nd</sup> September 2022 the investment strategy was reviewed to lock investments into these higher interest rates, as it was not expected this position would continue. The initial strategy aimed to achieve fixed rate investments for two years. However, the financial investments available to the Authority only provided one-year investments, as the markets also thought the position would be temporary.

Benchmarking information for year ending March 2024 covering 249 authorities (provided by the Link Group, our Treasury Management advisors), which measures the "weighted average rate of return" was 5.67%. This put us in the upper quartile of performance. To provide some context benchmarking for 11 other public sector organisations in the North East, Cumbria and Yorkshire is summarised below:

Weighted average rate of return year end 31.03.24

<b>Authority Ranking</b>	<b>Weighted average rate of return year end 31.03.24</b>
1	5.68%
<b>2 (Cleveland)</b>	<b>5.67%</b>
3	5.64%
4	5.53%
5 and 6	5.28%
7, 8, 9 and 10	5.26%
11	5.19%
12	4.77%

The selection of the investment counterparties has continued to prioritise security of the funds invested over the interest return.

In anticipation of continuing reductions in interest rates by the Bank of England later this year and continuing into 2025, the re-investments of temporary resources has been phased with maturity dates spread from February 2025 to October 2025. This approach ensures the Authority has the funds available to meet expenditure commitments and avoids all investments maturing at a time when it is expected interest rates will have fallen further from the 5.25% peak.