City of
BRADFORD
METROPOLITAN DISTRICT COUNCIL

Report of the Director of Finance to the meeting of the Governance and Audit Committee to be held on 21st March 2024

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Subject:

Treasury Management Strategy 2024-25

Summary statement:

This report shows the Council's 2024-25 Treasury Strategy and Prudential Indicators

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Portfolio:
Corporate Services

Overview & Scrutiny Area:
Corporate Services

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. With Government support provided in the form of Capitalisation Directions the Council will meet this requirement. The Council has concluded that the revenue expenditure it is anticipated to incur in each year of the period 2024-28 is likely to exceed the financial resources available and that reaching financial and operational sustainability without further government assistance will not be possible. In 2023-24 the Council has requested a capitalisation directive of £80m, and £140m has been requested to balance the budget in 2024-25.

A capitalisation directive allows the Council to use capital funding sources (borrowing and receipts from asset disposals) to fund revenue costs for an agreed period. It needs to be noted that capitalisation of revenue spend increases the cost of borrowing in following years. Each additional £10m borrowed through capitalisation directions would however add an estimated £0.9m per annum to future borrowing costs for 20 years.

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 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, 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 Council 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.

The Chartered Institute of Public Finance and Accountancy (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."*

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.

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 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 the 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. This capital strategy is reported separately from the Treasury Management Strategy Statement; non-treasury investments will be reported through the former.

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 treasury 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.

1.2.3 Scrutiny

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

1.2.4 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 the Executive Committee as part of the Quarterly Finance Reports.

1.3 Treasury Management Strategy for 2024-25

The strategy for 2024-25 covers two main areas:

Capital issues

- the capital expenditure plans and the associated 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
- the policy on use of external service providers.

These elements cover the requirements of the Local Government Act 2003, Department of Levelling Up Housing and Communities (DLUHC) Investment Guidance, DLUHC MRP Guidance, the CIPFA Prudential Code and the CIPFA Treasury Management Code.

Treasury Management Practices (TMPs)

The Council is currently updating its TMPs, and these will be presented to Full Council for approval during 2024-25.

1.4 Training

The CIPFA Treasury Management Code requires the responsible officer (in Bradford the Director of Finance) to ensure that Members with responsibility for treasury management receive adequate training in treasury management. This especially applies to Members responsible for scrutiny. Annual treasury management training is provided by the Council's treasury management adviser, Link Group Treasury Services Ltd. The most recent training was undertaken by Members on the 23rd November 2023. This training helps elected members to develop their skills and knowledge by defining the role of officers and elected members in treasury management decisions and highlighting the risks and opportunities in treasury management.

The training needs of treasury management officers are periodically reviewed. Most of this training is provided by Link Group, Treasury Services Ltd. however, staff are also encouraged to undertake other relevant training as it becomes available.

A formal record of the training received by officers central to the Treasury function will be maintained. Similarly, a formal record of the treasury management/capital finance training received by Members will also be maintained.

1.5 Treasury management consultants

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

The Council recognises that responsibility for treasury management decisions always remains with the organisation and will ensure that undue reliance is not placed upon the services of our 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 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

The Council's capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in the capital prudential indicators, which are designed to assist members' overview of the Council's Capital Investment Plan (CIP) to ensure that the capital expenditure plans are affordable, sustainable and prudent.

2.1 Capital expenditure and financing

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 proposed CIP includes £772m of capital investment in the District (£736m General Fund and £36m Housing Revenue Account). The HRA is a ring-fenced account which ensures that council housing does not subsidise, or is itself subsidised, by other local services paid for from the general fund. HRA capital expenditure is therefore recorded separately.

Table 1: Capital Expenditure

Capital expenditure	2022-23 Actual £m	2023-24 Estimate £m	2024-25 Estimate £m	2025-26 Estimate £m	2026-27 Estimate £m	2027-28 Estimate £m
General Fund	-	216	234	122	60	104
HRA*	-	3	15	10	8	-
Total CIP	**154**	**219**	**249**	**132**	**68**	**104**
Capitalisation direction (EFS)	-	80	140	106	88	52
TOTAL CAPITAL SPEND	**154**	**299**	**389**	**238**	**156**	**156**

*Separate HRA applies from 01-04-2023

Table 1 also includes an annual amount for capitalisation directions and these contribute significantly to the Capital Programme. From 2025-26 onwards these are included based on estimates for the ongoing support required by the Council.

Against the Council financial backdrop the Council's Capital Programme is significantly impacted. The Council is projecting to spend £299m in 2023-24 and total planned expenditure of £1,238m (including capitalisation directions) across the five remaining years of the Capital Programme.

The Council's high level of short-term borrowing and cost pressures from increased interest rates means the Council will be undertaking a full review of all capital spending projects as part of its plan to ensure the Council returns to financially sustainability starting in March 2024. The CIP will be reviewed to reflect a reduction in scale and cost, it will comprise only core programmes and schemes that i) the Council are committed to commercially, ii) meet statutory obligations, iii) deliver savings in management and maintenance costs, and iv) avoid future cost increases.

The capital expenditure shown above excludes other long-term liabilities, such as Private Finance Initiative (PFI) and leasing arrangements which already include borrowing instruments.

Table 2 over summarises the above capital expenditure plans and how these plans are being financed by capital or revenue resources. Any shortfall of resources results in a funding borrowing need.

Table 2: Capital funding

	2022-23 Actual £m	2023-24 Estimate £m	2024-25 Estimate £m	2025-26 Estimate £m	2026-27 Estimate £m	2027-28 Estimate £m
Total Capital Spend	**154**	**299**	**389**	**238**	**156**	**156**
Capital Spend not funded from borrowing	76.6	110	145	87	52	66
Capitalisation direction (EFS) not funded by borrowing (estimated capital receipts)	-	-	18.0	18.0	15.0	15.0
Capital spend funded from borrowing	77.4	109	104	45	16	39
Capitalisation direction (EFS) funded by borrowing	-	80.0	122	88	73	36
Total spend funded from borrowing	**77.4**	**189**	**226**	**133**	**89**	**75**

The borrowing need for capital expenditure in 2024-25 is currently expected to be £104m for the Capital Investment Pan and £122m for the capitalisation direction. This will however change if there is a revision to the spending profile of the capital plan following the full review.

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 historic outstanding capital expenditure which 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 borrowing need. Any capital expenditure above, which has not immediately been paid for through a revenue or capital resource, will increase the CFR.

The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual revenue charge which broadly reduces the indebtedness in line with each asset's life, and so charges the economic consumption of capital assets as they are used.

The CFR includes any other long-term liabilities (e.g., PFI schemes, finance leases currently). Whilst these increase the CFR, and therefore the Council's borrowing requirement, these types of schemes include a borrowing facility by the PFI, PPP lease provider and so the Council is not required to separately borrow for these schemes. The Council currently has £139m of such schemes within the CFR.

Table 3: Capital Financing Requirement

	2022-23 Actual £m	2023-24 Estimate £m	2024-25 Estimate £m	2025-26 Estimate £m	2026-27 Estimate £m	2027-28 Estimate £m
General Fund	-	904	1,099	1,195	1,242	1,277
HRA*	-	33	39	44	49	49
Capital Financing Requirement	**769**	**937**	**1,138**	**1,239**	**1,291**	**1,326**
Movement in CFR		**168**	**201**	**101**	**52**	**35**

Movement in CFR represented by

Net financing need for the year (above)		189	226	133	89	75
Less MRP/VRP and other financing movements		-21	-25	-32	-37	-40
Movement in CFR		**168**	**201**	**101**	**52**	**35**

*Separate HRA applies from 01-04-2023

Table 3 shows:

- The actual CFR at 31 March 2023 was £769m. This figure is also shown in the Council's draft statement of accounts and is being externally audited.
- The CFR is projected to increase, peaking at £1,326m at 31 March 28. There is an increase when borrowing in year for a capital purpose is more than the amounts set aside to fund the principal repayments. It also reflects the additional borrowing for capitalisation direction.

2.3 Liability Benchmark

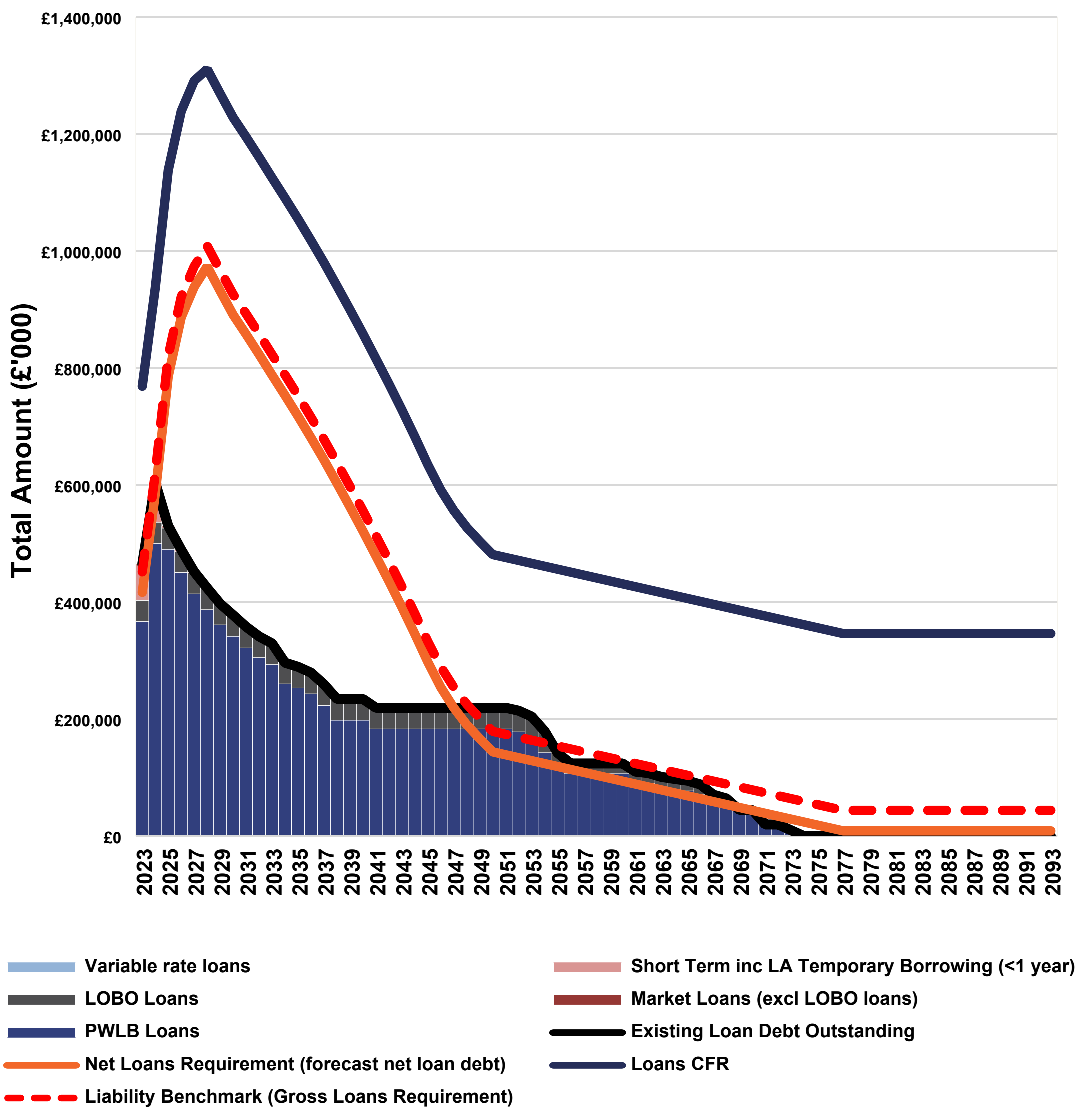
The Council is required to estimate and measure the Liability Benchmark (LB) for the forthcoming financial year and the following two financial years, as a minimum. The Liability Benchmark, based on current capital plans and cash flow assumptions, therefore gives the Council an indication of how much it needs to borrow, when it is likely to need to borrow, and where to match maturities to its planned borrowing needs. The liability benchmark makes no assumption about the level of future prudential borrowing in unknown capital budgets.

There are four components to the LB: -

1. **Existing loan debt outstanding**: the Council'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 Council'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 purpose of this prudential indicator is to compare the Council's existing loans outstanding against its future need for loan debt; the liability benchmark (the red dotted line). If the loans outstanding are below the liability benchmark (the red dotted line), the existing debt outstanding is less than the loan debt required, and the Council will need to borrow in the future to meet the shortfall. If the loans outstanding are above the liability benchmark (the red dotted line), the Council will have more debt than it needs based on current plans and the excess will have to be invested.

Graph 1 Liability Benchmark



As can be seen from the Council's liability benchmark graph, the loans outstanding, CFR, liability benchmark and net loans requirement broadly follow the same trend lines. Based on the CFR position and loans outstanding at 29th February 2024 we see the Council's current under borrowed position. In the next 5 years the CFR increases in line with prudential borrowing expectations to fund increases to the capital programme before gradually starting to decrease. The liability benchmark and net loans requirement also increase to indicate the additional borrowing need before gradually starting to decrease. Existing loans start to decrease as maturities occur and loans are paid back.

Considering the current under borrowed position and with no assumptions on future borrowing requirements beyond the current capital programme, the gap between the CFR and loans outstanding remain broadly similar over the term indicted on the liability benchmark graph. When considering the liability benchmark and net loans requirement this gives an indication of how much future loan debt may need be taken and on what maturity term to assist with long term planning and reduce risk.

Actual future debt taken may not exactly follow the liability benchmark as this is only a guide at a specific point in time, and one of several considerations when drawing down long term debt, to be determined by the S.151 Officer.

2.4 Minimum revenue provision (MRP) policy statement

In accordance with the Local Government Act 2003 the Council is required to pay off an element of the accumulated General Fund capital spend each year (the CFR) through a revenue charge (the minimum revenue provision - MRP), although it is also allowed to undertake additional voluntary payments if required (voluntary revenue provision - VRP).

DLUHC regulations have been issued which require the Full Council to approve an MRP Statement in advance of each year. A variety of options are provided to councils, so long as there is a prudent provision. The policy, as approved by Executive 05 March 2024 and Full Council 07 March 2024, is set out in Appendix 2.

Full Council approved the MRP statement. There are no proposed changes to the Council's MRP policy for 2024-25. The main elements of the policy are set out below.

- For supported borrowing MRP will be calculated using an Asset Life annuity basis on the remaining average life of the overall asset base. This is considered to be more prudent than other available methods.
- For all unsupported borrowing MRP will be calculated using an Asset Life annuity basis. Estimated asset life periods will be determined under delegated powers.
- Capital expenditure incurred during 2024-25 will not be subject to an MRP charge until 2025-26, or in the year after the asset becomes operational.
- The Council will apply the asset life method for any expenditure capitalised under a Capitalisation Direction.
- For MRP in respect of PFI contracts the charge to the revenue account is over the life of the school building assets. As per the main borrowing this is on an annuity asset life basis.
- MRP in respect of finance leases will equal the repayment amount for the year.
- There is no requirement on the HRA to make a minimum revenue provision but there is a requirement for a charge for depreciation to be made.

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 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 overall treasury management portfolio as at 31st March 2023 and as at 31st January 2024 are shown below for both borrowing and investments.

Table 4: Treasury Portfolio

	Actual 31 March 2023 £m	Actual 31 March 2023 %	Current 31 January 2024 £m	Current 31 January 2024 %
Treasury Investments				
Banks	0	0	0	0
Building Societies	0	0	0	0
DMADF (H M Treasury)	0	0	0	0
Money Market funds	48.3	100	7.1	100
Total Treasury Investments	**48.3**	**100**	**7.1**	**100**
Treasury External Borrowing				
Other	12.1	3	14.5	2
PWLB	366.8	78	445.3	80
LOBOs	36.2	8	36.2	7
Short term borrowing	50.0	11	60.0	11
Total external borrowing	**465.1**	**100**	**556.0**	**100**
Net Treasury Investments / (borrowing)	**416.8**		**548.9**	

At 31 January 2024 the Council had £556m of fixed interest rate debt. The cash balance available for investment was £7.1m. Over the long term as the Capital Programme progresses the level of cash available for investment is gradually decreasing as expected as the Council is using previously held balances to fund the programme.

The level of cash balances available is largely dependent on the timing of the Council's cash flow because of precept payments, receipt of grants, receipt of developers contributions, borrowing for capital purposes, payments to its suppliers of goods and services and spend progress on the Capital Plan. Cash held compared with this time last year has decreased due to the timing of these cash flows and the cash balances are therefore only available on a temporary basis.

The Council's forward projections for borrowing are summarised over. The table shows the actual external debt, against the underlying capital borrowing need, (the Capital Financing

Requirement - CFR), highlighting any over or under borrowing. The Council is currently maintaining an under-borrowed position in relation to the Capital Financing Requirement.

The Council is forecast to hold around £668 million of external borrowing and £130m other long-term liabilities as at 31 March 2024. This is analysed in Table 5.

Table 5: Borrowing Projection

	31/03/23 Actual £m	31/03/24 Estimate £m	31/03/25 Estimate £m	31/03/26 Estimate £m	31/03/27 Estimate £m	31/03/28 Estimate £m
Capital Financing Requirement	**769**	**937**	**1,138**	**1,239**	**1,291**	**1,326**
General Fund - Private Finance Initiative	-139	-130	-121	-111	-101	-90
External Borrowing	**-465**	**-668**	**-885**	**-995**	**-1,115**	**-1,137**
Under / (over) borrowing	165	139	132	133	75	99

Table 5 shows that, based on the capital programme (paragraph 2.1), additional borrowing from PWLB will be required if capital programme expenditure matches the anticipated spending profile. The borrowing requirement is a key driver of the borrowing strategy. The timing of any additional borrowing given the amounts indicated in the table above will be closely monitored. Members will recall that capital spending plans have been reprofiled year on year and it is likely that the trend could be repeated in 2024-25 and future years.

The relative mix of future internal and external borrowing will be considered in conjunction with advice from the Council's external treasury management advisor, noting that provision has been made in the updated Council budget plan revenue resource assumptions to accommodate a continued future mix of internal and external borrowing.

Within the range of prudential indicators there are several 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 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 this budget report.

The Council should include within the forecast gross borrowing figures in Table 5, any debt that relates to commercial activities / non-financial investments. The Council has no external debt for commercial activities/non-financial investments included in the gross borrowing figures in Table 5.

Salix Finance Limited provides interest free Government funding to the public sector to improve their energy efficiency, reduce carbon emissions and lower energy bills. The Council has taken the opportunity to secure £19.1 million interest free loans to part fund the £45 million approved street lighting replacement scheme in the Council's approved capital plan. To date, the Council has received £17.9m from Salix and repaid £2.8m.

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.

The authorised limit for external debt. This is a key prudential indicator and 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. The Council is asked to approve the following authorised limit.

Table 6: Operational Boundary and Authorised Limit

	2023-24 Estimate £m	2024-25 Estimate £m	2025-26 Estimate £m	2026-27 Estimate £m
Operational boundary	860	1,140	1,250	1,300
Authorised limit	880	1,160	1,270	1,320

3.3 Interest Rate Forecast

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 the following forecasts on 5th February 2024. These are forecasts for certainty rates, gilt yields plus 80 bps.

Table 7: Interest rate Forecast

Link Group Interest Rate View	05.02.24												
	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

- Link Group's 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 H2 2024. 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 (although most recent GDP releases have surprised with their on-going robustness).
- 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 recovery in China as well as the on-going 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 Euro-zone. At the time of writing there is 0.7% 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.

Downward pressure to current forecasts for UK gilt yields and PWLB rates include:-

- Labour and supply shortages prove more enduring and disruptive and depress economic activity.
- 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.
- 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.

Upward pressures to current forecasts for UK gilt yields and PWLB rates: -

- Despite the move 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 the sale of the Bank's QE programme**,** could be too much for the markets to comfortably digest without higher yields compensating.

Borrowing advice from our advisors: The Link 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 (although this is currently not a realistic option for CBMDC due to our budget overspend). 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.

3.5 Borrowing strategy

The factors that influence the 2024-25 strategy are:

- The movement in CFR (set out in Table 3);
- The interest rate forecasts (set out in Table 7);

- Aiming to minimise revenue costs to reduce the impact on the Council Tax Requirement;
- The impact of the Council's Capital Programme; and
- The capitalisation direction – EFS.

The Council is forecast to hold around £798 million of external borrowing and long-term liabilities at 31 March 2024, an increase of £194 million on the previous year, as part of its strategy for funding the capital programme and the additional borrowing for the Capitalisation direction.

The Council is currently maintaining an under-borrowed position (Table 5). 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 reserves, balances and cash flow has been used as a temporary measure. The Council has a significant borrowing need due to the increasing CFR and depleting reserves; the internal borrowing used to fund the CFR will be converted to external borrowing. The Council needs to lock in the costs to minimise risks of fluctuating interest rates and provide certainty on costs for the treasury budget. 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.

In addition the Council may borrow short-term loans to cover unplanned cash flow shortages.

Against this background and the risks within the economic forecast, caution will be adopted with the 2024-25 treasury operations. The Director of Finance 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 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, perhaps arising from an acceleration in the rate of increase in central rates in the USA and UK, an increase in world economic activity, or a sudden increase in inflation risks, then the portfolio position will be re-appraised. Most likely, fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.

At the point of acquiring longer term funding consideration will be given to:

- Whether the forecast capital borrowing requirement has reduced or slipped into the following year.
- The forecast changes to levels of reserves/balances, including whether the Council has received funding in advance of spending for capital schemes.

The strategy is to take longer term fixed rate borrowing when opportunities arise in combination with the temporary use of short-term borrowing as required.

The HRA strategy for borrowing will be the same as the borrowing strategy described above for the whole Council. The HRA Business Plan will guide and influence the overall HRA borrowing strategy.

Any decisions will be reported to the appropriate decision-making body at the earliest opportunity.

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.

Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through the mid-year or annual reporting mechanism.

3.7 Debt rescheduling

Rescheduling of current borrowing in our debt portfolio is unlikely to occur as there is still a large difference between premature redemption rates and new borrowing rates.

3.8 New financial institutions as a source of borrowing and / or types of borrowing

Currently the PWLB Certainty Rate is set at gilts + 80 basis points for both HRA and non-HRA borrowing. However, consideration may still need to be given to sourcing funding from the following sources for the following reasons:

- Local authorities (primarily shorter dated maturities out to 3 years or so – still cheaper than the Certainty Rate).
- Financial institutions (primarily insurance companies and pension funds but also some banks, out of forward dates where the objective is to avoid a "cost of carry" or to achieve refinancing certainty over the next few years).
- Municipal Bonds Agency.
- UK Infrastructure Bank.

Our advisors will keep us informed as to the relative merits of each of these alternative funding sources.

Approved Sources of Long and Short-term Borrowing
Table 8 shows sources of borrowing that the Council may use and whether the related interest rates are fixed or variable.

Table 8: Approved sources of long and short term borrowing

On Balance Sheet	Fixed	Variable
PWLB	●	●
UK Municipal Bond Agency	●	●
Local Authorities	●	●
Banks	●	●
Pension Funds	●	●
Insurance Companies	●	●
UK Infrastructure Bank	●	●
Market (long-term)	●	●
Market (temporary)	●	●
Market (LOBOs)	●	●

Stock Issues	●	●
Local Temporary	●	●
Local Bonds	●	
Local Authority Bills	●	●
Overdraft		●
Negotiable Bonds	●	●
Internal (capital receipts & revenue balances)	●	●
Commercial Paper	●	
Medium Term Notes	●	
Finance Leases	●	●

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 treasury (financial) investments, (as managed by the treasury management team). Non-financial investments, essentially the purchase of income yielding assets, are covered in the Capital and Investment Strategies (separate reports that went to full Council 7th March 2024).

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 security first, portfolio liquidity second and then yield, (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.

The Council expects to be a long-term borrower and new treasury investments will therefore be made primarily to manage day-to-day cashflows using short-term low risk instruments.

In the current economic climate, it is considered appropriate to keep investments short term to cover cash flow needs. However, where appropriate (from an internal as well as external perspective), the Council will also consider the value available in periods up to 12 months with high credit rated financial institutions, as well as wider range fund options.

The guidance from the DLUHC and CIPFA places 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 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.

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

4. This Council has defined the list of types of investment instruments that the treasury management team are authorised to use.

- 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 more than one year, and/or are more complex instruments which require greater consideration by members and officers before being authorised for use.

5. Non-specified and loan investment limits. The Council has determined that it will set a limit to the maximum exposure of the total treasury management investment portfolio to non-specified treasury management investments of £20m.

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. This Council will set a limit for 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. This 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 Council 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.

However, this Council will also pursue value for money in treasury management and will monitor the yield from investment income against appropriate benchmarks for investment performance, (see paragraph 4.5). 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

The primary principle governing the Council's investment criteria is the security of its investments, although the yield or 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, criteria for choosing investment counterparties with adequate security, and monitoring their security. This is set out in the specified and non-specified investment sections below; and
- It has sufficient liquidity in its investments. For this purpose, it will set out procedures for determining the maximum periods for which funds may prudently be committed. These procedures also apply to the Council's prudential indicators covering the maximum principal sums invested.

The Director of Finance will maintain a counterparty list in compliance with the following criteria and will revise the criteria and submit them to Council for approval as necessary. These criteria are separate to that which determines which types of investment instrument are either specified or non-specified as it provides an overall pool of counterparties considered high quality which the Council may use, rather than defining what types of investment instruments are to be used.

The criteria for providing a pool of high-quality investment counterparties, (both specified and non-specified investments) are:

Table 9: Investment Counterparties

Institution	Amount	Time limit	To qualify as a "specified investment"	Non-UK Country	Short term Investment rating	Long Term investment rating
Bank /Building Society	£30m	2yrs	Less than 1 year	AA-	Requires if available Fitch F1 S & P A-1 Moody's P-1	Moody's Aa3 or Fitch AA- if not available.
Bank /Building Society	£20m	1yr	Less than 1 year	AA-	Requires if available Fitch F1 S&P A_1 Moody's P_1w	Moody's A1 or Fitch A1 if not available
Bank/Building Society	£7m	100 days	Less than 1 year	AA-	Either F1 or S&P A_1	Either Moody's A1
Nat West Bank	£20m	1yr	Less than 1 year	AA-	Council bank/part Government owned	A1* for Moodys or Fitch A+
Treasury Bill/DMO	No limit	1yr	Less than 1 year		n/a	UK Gov. rating
Money Market Fund	£20m	Instant access	Less than 1 year		n/a	Either Moody's AAA Fitch AAA or S&P AAA
Local Authority	£20m	1yr	Less than 1 year	AA-	n/a	n/a

Use of additional information other than credit ratings - Additional requirements under the Code require the Council to supplement credit rating information. Whilst the above criteria rely primarily on the application of credit ratings to provide a pool of appropriate counterparties for officers to use, additional operational market information will be applied before making any specific investment decision from the agreed pool of counterparties. This additional market information (for example Credit Default Swaps, rating Watches/Outlooks) will be applied to compare the relative security of differing investment opportunities.

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. However, as economies are beginning to reopen, there have been some instances of previous lowering of Outlooks being reversed.

CDS prices - Although bank CDS prices, (these are market indicators of credit risk), spiked upwards at the end of March / early April 2020 due to the heightened market uncertainty and ensuing liquidity crisis that affected financial markets, 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 Other 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 treasury management investment limit.** The Council has determined that it will limit the maximum total exposure of treasury management investments to non-specified treasury management investments as being £20m of the total treasury management investment portfolio.

b) **Country limit.** The Council has determined that it will only use approved counterparties from the UK and from countries with a minimum sovereign credit rating of A1 for the UK and AA- for the rest of the world from Fitch or equivalent. The list of countries that qualify using these credit criteria as at the date of this report are shown in Appendix 4. 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 (i.e., rates for investments up to 12 months). Greater returns are usually obtainable by investing for longer periods. 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 thought that Bank Rate is likely to rise significantly within the time horizon being considered, then consideration will be given to keeping most investments as being short term or variable.

- Conversely, if it is thought that Bank Rate is likely to fall within that period, consideration will be given to locking in higher rates currently obtainable, for longer periods.

Investment returns expectations.
The current forecast shown in paragraph 3.3, 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 as follows:

Table 10: Investment earnings rates

Average earnings in each year	Now
2023-24 (remainder)	5.3%
2024-25	4.55%
2025-26	3.1%
2026-27	3.0%
2027-28	3.25%
Years 6 to 10	3.25%
Years 10+	3.25%

For its cash flow generated balances, the Council will seek to utilise its business reserve instant access and notice accounts, money market funds and short-dated deposits, (overnight to 100 days), in order to benefit from the compounding of interest.

Investment treasury indicator and limit - total principal funds 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.

The Council is asked to approve the following treasury indicator and limit:

Table 11: Upper limit for principle sums invested for longer than 365 days

	2024-25 £m	2025-26 £m	2026-27 £m
Principal sums invested for longer than 365 days	£20m	£20m	£20m
Current investments as at 31-01-2024 in excess of 1 year maturing in each year	£0m	£0m	£0m

4.5 Investment performance / risk benchmarking

This Council will use an investment benchmark to assess the investment performance of its investment portfolio of overnight, 7 day, compounded/ SONIA. The investment average return up to the end of January was 5.28% with average investment balance of £22m.

4.6 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.

5. Other considerations

5.1 Environmental, Social & Governance (ESG) Considerations

ESG considerations are becoming an increasingly important topic within the investment community. The 2021 changes to the CIPFA Treasury Management Code sees ESG incorporated into Treasury Management Practice (TMP) 1, with the inclusion of the wording, 'the organisation's credit and counterparty policies should set out its policy and practices relating to environmental, social and governance (ESG) investment considerations. This is a developing area, and it is not implied that the organisation's ESG policy will currently include ESG scoring or other real-time ESG criteria at individual investment level".

The Council with advice from its treasury advisor, is looking into the impact of including ESG in TMP 1 and must ensure that there is a clear understanding of what "environmental, social and governance (ESG)" investment considerations mean, understanding the ESG "risks" that the Council is exposed to and evaluating how well the Council can manage these risks. Members must note that ESG is not the same as Socially Responsible Investing and not the same as Sustainable Investing (investing in products / companies based on expected sustainable and beneficial societal impact, alongside a financial return).

6. Financial and Resources Appraisal

6.1 The financial implications are set out in section 1,2,3 and 4 of this report

7. Risk Management and Governance Issues

7.1 The principal risks associated with treasury management are:

Risk: Loss of investments as a result of failure of counterparties.
Mitigation: Limiting the types of investment instruments used, setting lending criteria for counterparties, and limiting the extent of exposure to individual counterparties.

Risk: That the Council will commit too much of its investments in fixed term investments and might have to recall investments prematurely resulting in possible additional costs or new borrowing (Liquidity risk).
Mitigation: Ensuring that a minimum proportion of investments are held in short term investments for cash flow purposes.

Risk: Increase in the net financing costs of the Council due to borrowing at high rates of interest.
Mitigation: Planning and undertaking borrowing and lending in light of assessments of future interest rate movements, and by undertaking mostly long term borrowing at fixed rates of interest (to reduce the volatility of capital financing costs).

Risk: Higher interest rates increase borrowing making it more difficult to self-finance capital schemes. Debt servicing becomes less affordable and less sustainable and crowds out revenue spend.
Mitigation: To pause, delay or defer capital schemes. Also review opportunities to borrow in the future at current interest rates.

Risk: Return on non-treasury investments lower than expected.
Mitigation: Review and analysis of risk prior to undertaking non-treasury investments.

Risk: The Council's Minimum Revenue Policy charges an insufficient amount to the Revenue Estimates to repay debt.
Mitigation: Align the Minimum Revenue Policy to the service benefit derived from the Council's assets.

Risk: Associated with cash management, legal requirements and fraud.
Mitigation: These risks are managed through:

- Treasury Management Practices covering all aspects of Treasury management procedures including cash flow forecasting, documentation, monitoring, reporting and division of duties.
- All Treasury management procedures and transactions are subject to inspection by internal and external auditors. The council also employs external financial advisors to provide information on market trends, credit rating alerts, lending criteria advice and investment opportunities.

Risk: Anticipated borrowing is lower / higher than expected because the 2024-25 capital programme forecast is incorrect. This is explained in more detail below, together with the actions being taken to reduce these risks:
Mitigation: The Council is required to set a balanced budget for its revenue estimates; so in broad terms, income received will match expenditure over the 2024-25 financial year. The 2024-25 revenue estimates cause only temporary cash flow differences, for example when income is received in a different month to when the expenditure is incurred.

However, the 2024-25 capital budget will cause a cash flow shortfall in the long term, which generates a borrowing requirement. While some of the capital budget is funded immediately, mainly with Government grants, other elements are not funded initially, leading to the cash flow deficit that requires borrowing.

Managing borrowing is part of the Treasury Management role. To help in its management, the Treasury Strategy identifies the element within the capital budget that is not funded straightaway, to anticipate the Council's borrowing requirement.

However, when the capital budget is under / overspent, the Council has a lower / higher borrowing requirement than anticipated. This risk is managed in practice because the Council only borrows when there is an actual cash flow shortage. The uncertainty around spend against the capital budget makes cash flow management more difficult. For example, it is less likely that the Council would take advantage of a short-term fall in interest rates, without more certainty around the timing of any borrowing need. Actions that have taken place to manage the risks relating to this uncertainty in the timing of capital spend are Councillor and Officer challenge sessions on the capital budget; increased scrutiny of the capital forecasts in the quarterly monitoring, and the collection of additional documentation around the critical paths of individual schemes.

<u>Risk: Failure to deliver planned reduction in the Capital Investment Plan or additional capital receipts means a higher-than-expected borrowing requirement</u>
Mitigation: The 2024-25 Budget Report by the Section 151 Officer sets out the actions required by the Council to deliver overall financial sustainability for the Council. This includes a review of the Capital Investment Plan to reduce capital spend funded by borrowing. Delivery of the overall programme will be reviewed as part of improvement and transformation process.

8. Legal Appraisal

8.1 Any relevant legal considerations are set out in the report.

9. Other Implications

9.1 Equality & Diversity – no direct implications
9.2 Sustainability implications – no direct implications
9.3 Green house Gas Emissions Impact – no direct implications
9.4 Community safety implications – no direct implications
9.5 Human Rights Act – no direct implications
9.6 Trade Unions – no direct implications
9.7 Ward Implications – no direct implications
9.8 Implication for Corporate Parenting – no direct implications
9.9 Issues arising from Privacy Impact Assessment– no direct implications

10. Not for publications documents
10.1 None

11. Options
11.1 None

12. Recommendations
12.1 That the report be noted by the Governance and Audit Committee and passed to full Council for adoption.

13. Appendices

Appendix 1 Prudential and Treasury Indicators
Appendix 2 Minimun Revenue Provision (MRP) Policy
Appendix 3 Economic Background
Appendix 4 Approved countries for investments
Appendix 5 Treasury Management scheme of delegation
Appendix 6 Treasury Management role of the Statutory Chief Finance Officer (Director of Finance)

Appendix 1

THE CAPITAL PRUDENTIAL AND TREASURY INDICATORS 2024-25 – 2027-28

To facilitate the decision making process and support capital investment decisions, the Prudential Code requires the Council to approve and monitor a minimum number of prudential indicators. These indicators are mandatory and cover affordability, prudence, capital expenditure, external debt and treasury management.

The indicators are purely for internal use by the Council and are not intended to be used as comparators between councils. In addition to this in-year indication, the benefit from monitoring arises from following the movement in indicators over time and the year-on-year changes.

Capital expenditure

The Council's capital expenditure plans are the key driver of 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.

Capital expenditure	2022-23 Actual £m	2023-24 Estimate £m	2024-25 Estimate £m	2025-26 Estimate £m	2026-27 Estimate £m	2027-28 Estimate £m
General Fund	-	216	234	122	60	104
HRA*	-	3	15	10	8	-
Total	**154**	**219**	**249**	**132**	**68**	**104**
Capitalisation direction (EFS)	-	80.0	140	106	88	52
TOTAL CAPITAL SPEND	**154**	**299**	**389**	**238**	**156**	**156**

*Separate HRA applies from 01-04-2023

Estimates of Capital Financing Requirement

	2022-23 Actual £m	2023-24 Estimate £m	2024-25 Estimate £m	2025-26 Estimate £m	2026-27 Estimate £m	2027-28 Estimate £m
Opening Capital Financing Requirement	**712**	**769**	**937**	**1,138**	**1,239**	**1,291**
Increase in borrowing	77	189	226	133	89	75
Less MRP and other financing movements	-20	-21	-25	-32	-37	-40
Closing Capital Financing Requirement	**769**	**937**	**1,138**	**1,239**	**1,291**	**1,326**

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. The Council is asked to approve the following indicators:

a. 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), against the net revenue stream.

General Fund	2023-24 £m	2024-25 £m	2025-26 £m	2026-27 £m	2027-28 £m
MRP, excluding PFI**	17.8	22.4	25.1	27.0	27.3
MRP PFI, finance lease	3.3	3.3	3.4	3.4	3.5
Old West Yorkshire Waste debt	0.1	0.1	0.1	0.1	0.1
Interest on external borrowing	22.4	28.4	28.7	28.8	28.6
Interest on PFI	15.3	14.6	14.0	13.2	12.4
Premium on debt repayment	0.3	0.3	0.3	0.3	0.3
Capitalisation Direction (MRP / Interest) *	-	3.7	12.7	19.3	23.9
Total Capital Financing Costs	**59.2**	**72.8**	**84.3**	**92.1**	**96.1**
Projected Net Revenue Stream	453	435	459	492	513
Ratio to Net Revenue Stream	**13.1%**	**16.8%**	**18.4%**	**18.7%**	**18.7%**

*2024-25 onwards - Year of EFS includes half year interest, years afterwards include MRP and interest over a 20-year timeframe
**2024-25 onwards includes MRP on 2023-24 £80m EFS

HRA	2023-24 £m	2024-25 £m	2025-26 £m	2026-27 £m	2027-28 £m
Total Capital Financing Costs	1.1	1.1	1.1	1.1	1.1
HRA Rental Income	2.7	2.9	3.0	3.1	3.2
Ratio to Net Revenue Stream	**41.7%**	**38.8%**	**37.5%**	**36.3%**	**35.2%**

Prudence indicators

- Gross debt and the capital financing requirement

The Prudential Code requires the calculation of the capital financing requirement (CFR). This figure represents the Council's underlying need to borrow for a capital purpose and the change year-on-year will be influenced by the capital expenditure in the year.

In order to ensure that over the medium-term gross debt will only be for capital purposes, the Council must ensure that 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 the current and next two financial years. In cases where the CFR is reducing over the period, the Code allows the CFR at its highest point to be used in this calculation.

The Council had no difficulty meeting the previous calculation in 2023-24, nor are any difficulties envisaged for the current or future years. This view considers current commitments, existing plans, and the proposals in this budget report and is shown in the table over.

	31/03/23 Actual £m	31/03/24 Estimate £m	31/03/25 Estimate £m	31/03/26 Estimate £m	31/03/27 Estimate £m	31/03/28 Estimate £m
Capital Financing Requirement	**769**	**937**	**1,138**	**1,239**	**1,291**	**1,326**
General Fund - Private Finance Initiative	-139	-130	-121	-111	-101	-90
External Borrowing	**-465**	**-668**	**-885**	**-995**	**-1,115**	**-1,137**
Under-borrowing	165	139	132	133	75	99

External debt indicators
Operational boundary

	2023-24 Estimate £m	2024-25 Estimate £m	2025-26 Estimate £m	2026-27 Estimate £m	2027-28 Estimate £m
Total	860	1,140	1,250	1,300	1,330

Authorised limit

	2023-24 Estimate £m	2024-25 Estimate £m	2025-26 Estimate £m	2026-27 Estimate £m	2027-28 Estimate £m
Total	880	1,160	1,270	1,320	1,350

Actual external debt as at 31st March - this will be reported within the outturn report on treasury management.

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 treasury indicators and limits:

Maturity structure of fixed interest rate borrowing 2024-25		
	Lower	**Upper**
Under 12 months	0%	20%
12 months to 2 years	0%	20%
2 years to 5 years	0%	50%
5 years to 10 years	0%	50%
10 years to 20 years	0%	90%
20 years to 30 years	20%	90%
30 years to 40 years	20%	90%
40 years to 50 years	20%	90%

Maturity structure of variable interest rate borrowing 2024-25		
	Lower	**Upper**
Under 12 months	0%	20%
12 months to 2 years	0%	20%
2 years to 5 years	0%	20%
5 years to 10 years	0%	20%
10 years and over	0%	20%

Upper limit for principle sums invested

Total principal sums invested for periods longer than 365 days – if the Council invests or plans to invest for longer than 365 days it must set an upper limit for each financial year for the maturing of such investments.

£m	2024-25 £m	2025-26 £m	2026-27 £m
Principal sums invested for longer than 365 days	£20m	£20m	£20m

Control of interest rate exposure

Members are advised that indicators for interest rate exposure are no longer a requirement under the new Treasury Management Code. However, as interest rate exposure risk is an important issue, officers will continue to monitor the balance between fixed and variable interest rates for borrowing and investments. This will aim to ensure the Council is not exposed to adverse fluctuations in fixed or variable rate interest rate movements.

This is likely to reflect higher fixed interest rate borrowing if the borrowing need is high or fixed interest rates are likely to increase, or a higher variable rate exposure if fixed interest rates are expected to fall. Conversely if shorter term interest rates are likely to fall, investments may be fixed earlier, or kept shorter if short term investments are expected to rise.

The balance between variable rate debt and variable rate investments will be monitored as part of the overall treasury function in the context of the overall financial instruments structure and any under or over borrowing positions.

Appendix 2 Minimum Revenue Provision Policy 2024-25

1.1 The Local Government Act 2003 requires the Council to make a provision for the repayment of borrowing used to finance its capital expenditure, known as the Minimum Revenue Provision (MRP).

1.2 The MRP is the amount of principal capital repayment that is set aside each year in order to repay the Capital Financing Requirement (CFR) based on the requirement of statutory regulation and the Council's own accounting policies.

1.3 DLUHC regulations require full Council to approve an MRP statement in advance of each year. The Policy may be revised during the year by full Council, or the appropriate body of Members where required.

1.4 The regulations allow the Council to review its policy every year and set a policy that it considers prudent at that time. The impact of a revised MRP policy will be kept under regular review to ensure that the annual provision is prudent.

1.5 The method for calculating the MRP on each category of debt is outlined below:

a) For supported borrowing MRP will be calculated using an Asset Life annuity basis on the annuity asset life method over the remaining 36 years. This is more prudent than other available methods.

b) Unsupported or prudential borrowing MRP is based on the Asset Life method – that is, the expenditure financed from borrowing is divided by the expected asset life. From 1 April 2022 the MRP is calculated on the annuity basis.

c) Since 2009-10 the appropriate financing costs for the Council's Building Schools for the Future (BSF) Private Finance Initiative (PFI) schemes have been included in MRP calculations. In 2018-19 the MRP policy for PFI assets was brought into line with the main MRP Policy and the charge of the principal to the revenue account is now over the life of the school building assets. As per the main borrowing from the 1 April 2022 this is on an annuity asset life basis.

d) Finance lease MRP is equal to the principal repayment.

e) The Council will apply the asset life method for any expenditure capitalised under a Capitalisation Direction.

f) There is no requirement on the HRA to make a minimum revenue provision but there is a requirement for a charge for depreciation to be made.

g) Asset lives are reviewed on an ongoing basis to match the MRP charge to the Revenue Estimates with the service benefit derived from the asset. The Council reserves the right to determine useful life periods and prudent MRP in exceptional circumstances where the recommendations of the guidance would not be appropriate.

h) MRP will generally commence in the financial year following the one in which the expenditure was incurred. However, for long life assets, the authority will postpone the commencement of MRP until the financial year following the one in which the asset becomes operational.

i) MRP overpayments – DLUHC MRP Guidance makes allowance for any charges made over the statutory MRP, VRP or overpayments, can, if needed, be reclaimed in later years if deemed necessary or prudent. For these sums to be reclaimed for use in the budget, this policy must disclose the cumulative overpayment made each year. There are no plans for VRP to be made in 2024-25. However, VRP will be kept under review, and should it be deemed prudent to make any VRP this will be the decision of the S.151 Officer and reported to Executive and Governance & Audit Committee at the next available opportunity.

j) Where capital expenditure involves repayable loans to third parties no MRP is charged where the principal element of the loan is being repaid in annual instalments. The capital receipts arising from the principal loan repayments will be used to reduce the CFR instead of MRP. Where no principal repayment is made in a given year, MRP will be charged at a rate in line with the life of the assets funded by the loan.

Appendix 3 Economic Background (provided by Link Group)

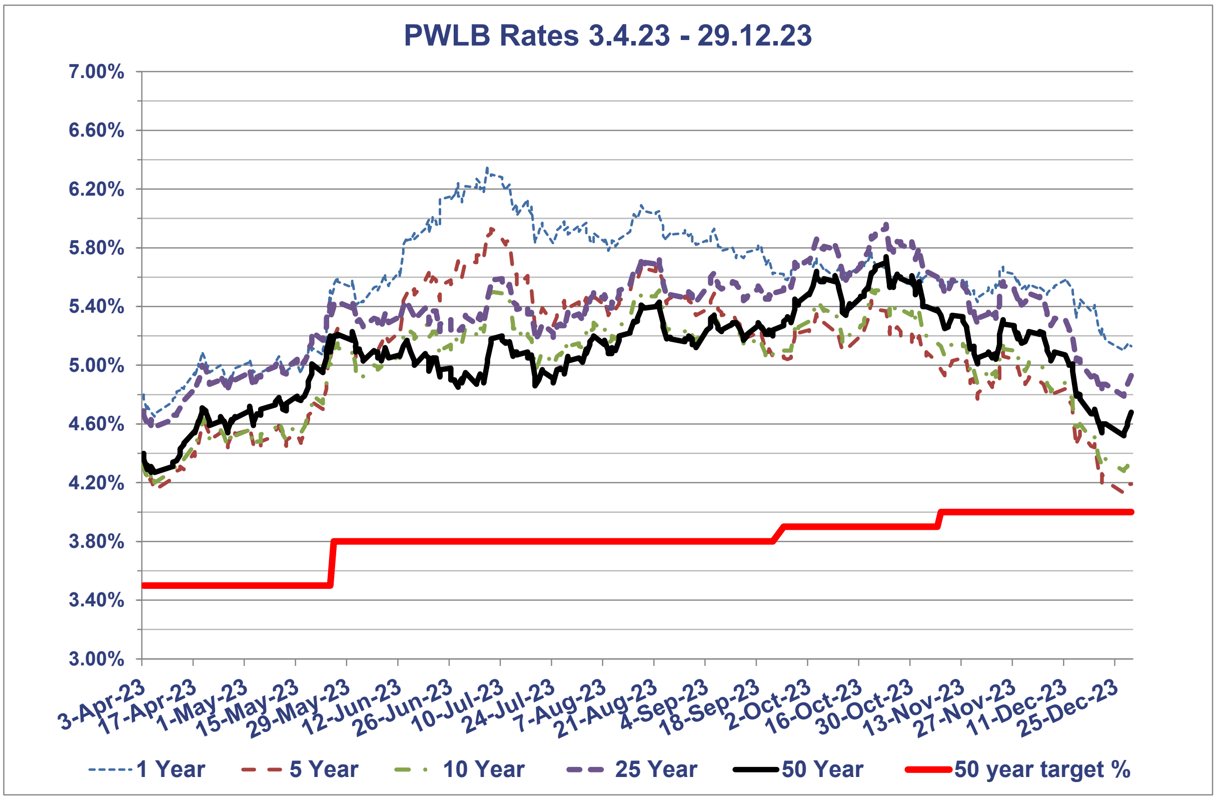
- The third quarter of 2023-24 saw:
  - A 0.3% month on month decline in real GDP in October, potentially partly due to unseasonably wet weather, but also due to the ongoing drag from higher interest rates. Growth for the second quarter, ending 30th September, was revised downwards to -0.1% and growth 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 Office of National Stats "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% quarter on quarter fall may mean the mildest of mild recessions has begun. Indeed, real GDP in October fell 0.3% month on month 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% quarter on quarter 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% quarter on quarter fall in manufacturing output in Q3.
- The 0.3% month on month fall in retail sales volumes in October means that after contracting by 1.0% quarter on quarter (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.

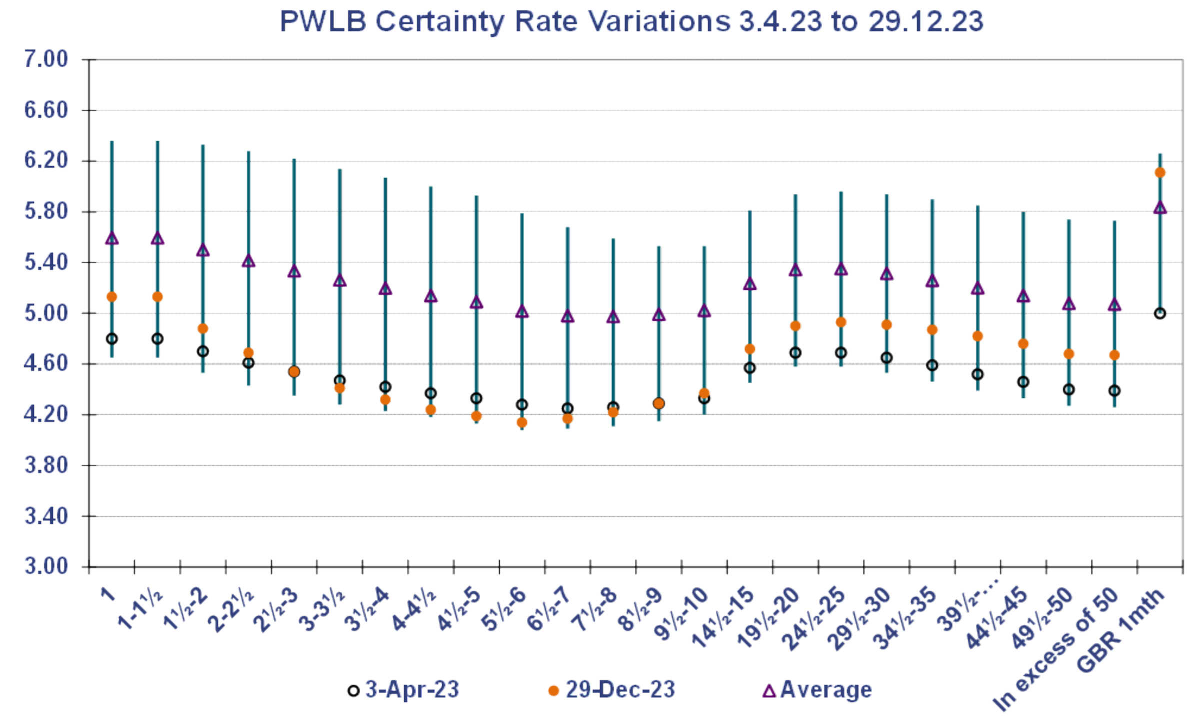
- Overall, we expect real GDP growth to remain subdued throughout 2024 as the drag from higher interest rates is protracted but a fading of the cost-of-living crisis and interest rate cuts in the second half of 2024 will support a recovery in GDP growth in 2025.
- The labour market remains tight by historical 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% month on month, which meant the headline 3 month year on year 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 positive on higher rates, with the MPC maintaining its higher rate 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 market 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.
- At the time of writing (Feb 24) yields are back to the November 23 levels of around 4.20%.
- 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 chart below, the rise in gilt yields across the curve in the first half of 2023-24, and therein PWLB rates, is clear to see, prior to the end of year rally based on a mix of supportive domestic and international factors.

PWLB RATES 3.4.23 - 29.12.23





HIGH/LOW/AVERAGE PWLB RATES FOR 3.4.23 – 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%

MPC meetings 2nd November and 14th December 2023

- On 2nd November, the Bank of England's Monetary Policy Committee (MPC) voted to keep Bank Rate on hold at 5.25%, and on 14th December reiterated that view. Both meetings reflected a split vote, the latter by 6 votes to 3, with the minority grouping voting for an increase of 0.25% as concerns about "sticky" inflation remained in place.
- Nonetheless, with UK CPI inflation now at 3.9%, and core inflating beginning to moderate (5.1%), markets are voicing a view that rate cuts should begin in Q1 2024/25, some way ahead of the indications from MPC members. Of course, the data will be the ultimate determinant, so upcoming publications of employment, wages and inflation numbers will be of particular importance, and on-going volatility in Bank Rate expectations and the gilt yield curve can be expected.
- In addition, what happens outside of the UK is also critical to movement in gilt yields. The US FOMC has kept short-term rates in the range of 5.25%-5.50%, whilst the ECB has moved its Deposit rate to a probable peak of 4%. Markets currently expect both central banks to start cutting rates in 2024.

Appendix 4

APPROVED COUNTRIES FOR INVESTMENTS

This list is based on those countries which have sovereign ratings of AA- or higher, (we show the lowest rating from Fitch, Moody's and S&P) and also, (except - at the time of writing - for Hong Kong and Luxembourg), have banks operating in sterling markets which have credit ratings of green or above in the Link creditworthiness service.

Based on lowest available rating

AAA

- Australia
- Denmark
- Germany
- Netherlands
- Norway
- Singapore
- Sweden
- Switzerland

AA+

- Canada
- Finland
- U.S.A.

AA

- Abu Dhabi (UAE)

AA-

- Belgium
- France
- Qatar
- **U.K.**

Appendix 5 TREASURY MANAGEMENT SCHEME OF DELEGATION

(i) Full Council

- receiving and reviewing reports on treasury management policies, practices and activities;
- approval of annual strategy.

(ii) Governance and Audit Committee

- approval of/amendments to the organisation’s adopted clauses, treasury management policy statement and treasury management practices;
- budget consideration and approval;
- approval of the division of responsibilities;
- receiving and reviewing regular monitoring reports and acting on recommendations;
- approving the selection of external service providers and agreeing terms of appointment.

(iii) Corporate Overview and Scrutiny Committee

- reviewing the treasury management policy and procedures and making recommendations to the responsible body.

Appendix 6 THE TREASURY MANAGEMENT ROLE OF THE SECTION 151 OFFICER

The S151 (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.

The above list of specific responsibilities of the S151 officer in the 2021 Treasury Management Code has not changed. However, implicit in the changes in both codes, is a major extension of the functions of this role, especially in respect of non-financial investments, (which CIPFA has defined as being part of treasury management). These include:

- preparation of a capital strategy to include capital expenditure, capital financing, non-financial investments and treasury management, with a long-term timeframe.
- ensuring that the capital strategy is prudent, sustainable, affordable and prudent in the long term and provides value for money.
- ensuring that due diligence has been carried out on all treasury and non-financial investments and is in accordance with the risk appetite of the Council.
- ensure that the authority has appropriate legal powers to undertake expenditure on non-financial assets and their financing.
- ensuring the proportionality of all investments so that the authority does not undertake a level of investing which exposes the Council to an excessive level of risk compared to its financial resources.
- ensuring that an adequate governance process is in place for the approval, monitoring and ongoing risk management of all non-financial investments and long term liabilities.
- provision to members of a schedule of all non-treasury investments including material investments in subsidiaries, joint ventures, loans and financial guarantees.
- ensuring that members are adequately informed and understand the risk exposures taken on by an authority.
- ensuring that the authority has adequate expertise, either in house or externally provided, to carry out the above.
- creation of Treasury Management Practices which specifically deal with how non treasury investments will be carried out and managed, to include the following -
    - Risk management (TMP1 and schedules), including investment and risk management criteria for any material non-treasury investment portfolios;
    - Performance measurement and management (TMP2 and schedules), including methodology and criteria for assessing the performance and success of non-treasury investments;

- Decision making, governance and organisation (TMP5 and schedules), including a statement of the governance requirements for decision making in relation to non-treasury investments; and arrangements to ensure that appropriate professional due diligence is carried out to support decision making;

- Reporting and management information (TMP6 and schedules), including where and how often monitoring reports are taken;

- Training and qualifications (TMP10 and schedules), including how the relevant knowledge and skills in relation to non-treasury investments will be arranged.