AUDIT COMMITTEE	AGENDA ITEM No. 8
25 NOVEMBER 2024	PUBLIC REPORT

Report of:	Cecilie Booth, Executive Director of Corporate Services and Section 151 Officer	
Cabinet Member(s) responsible:	Councillor Mohammed Jamil, Deputy Leader and Cabinet Member for Finance and Governance	
Contact Officer(s):	Cecilie Booth, Executive Director of Corporate Services and Section 151 Officer	Tel. 07970 325557

TREASURY MANAGEMENT MID YEAR UPDATE

RECOMMENDATIONS	
FROM: Cecilie Booth, Executive Director of Corporate Services and S151 Officer	**Deadline date:** N/A
It is recommended that Audit Committee: 1. Reads the update on the economic background and implications for the Treasury Management Strategy in 2024-25. 2. Reviews the Treasury Management Strategy Statement (TMSS) Mid-year position and performance against the Prudential Indicators.	

1. ORIGIN OF REPORT

1.1 This report has been written in accordance with the requirements of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised 2021), which recommends that Members receive reports on its treasury management policies, practices, and activities, including an annual strategy and plan in advance of the year, a mid-year review and an annual report after its close.

Treasury management is defined 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."

This mid-year report has been prepared in compliance with CIPFA's Code of Practice on Treasury Management, and covers the following:

- An economic update for the first half of the 2024/25 financial year;
- A review of the Treasury Management Strategy Statement and Annual Investment Strategy;
- The Authority's capital expenditure, as set out in the Capital Strategy, and prudential indicators;
- A review of the Authority's investment portfolio for 2024/25;
- A review of the Authority's borrowing strategy for 2024/25;
- A review of compliance with Treasury and Prudential Limits for 2024/25.

2. CORPORATE PRIORITIES

The report contains no proposals for changes to service delivery and therefore there is no decision to take which may impact carbon emissions of the council or the city.

3. LEGAL IMPLICATIONS

Treasury Management activities have to conform to the Local Government Act 2003, the Local Authorities (Capital; Finance and Accounting) (England) Regulations 2003 (SI 2003/3146), which specifies that the Council is required to have regard to the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice and also the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2022 and 2024, which clarifies the requirements of the Minimum Revenue Provision guidance.

This report takes into the account the impact of the CIPFA Prudential Code and CIPFA Treasury Management Code of practice issued in 2021.

4. ECONOMICS AND INTEREST RATES

4.1 Economic Update

- The third quarter of calendar year 2024 (July to September) saw:
  - GDP growth stagnating in July following downwardly revised Q2 figures
  - CPI inflation hitting its target in June before edging above it to 2.2% in July and August
  - Core CPI inflation increasing from 3.3% in July to 3.6% in August
  - The Bank of England initiating its easing cycle by lowering interest rates from 5.25% to 5.0% in August and holding them steady in its September meeting
  - 10-year gilt yields falling to 4.0% in September.

- The economy's stagnation in June and July points more to a mild slowdown in GDP growth than a sudden drop back into a recession. Moreover, the drop in September's composite activity Purchasing Managers Index, from 53.8 in August to 52.9, was still consistent with GDP growth of 0.3%-0.4% for the summer months. This is in line with the Bank of England's view.

- The government's plans to raise public spending by around £16bn a year (0.6% GDP) have caused concerns that a big rise in taxes will be announced in the Budget, which could weaken GDP growth in the medium-term. However, if taxes are raised in line with spending (i.e., by £16bn) that would mean the overall stance of fiscal policy would be similar to the previous government's plan to reduce the budget deficit. Additionally, rises in public spending tend to boost GDP by more than increases in taxes reduce it.

- The further easing in wage growth will be welcomed by the Bank of England as a sign that labour market conditions are continuing to cool. On three-month annual basis, the average earnings fell from 4.6% in June to 4.0% in July. Other labour market indicators also point to a further loosening in the labour market. Nonetheless, the Bank of England is still more concerned about the inflationary influence of the labour market rather than the risk of a major slowdown in labour market activity.

- Core inflation crept up from 3.3% to 3.6%. CPI inflation is also expected to rise in the coming months, potentially reaching 2.9% in November, before declining to around 2.0% by mid-2025.

- The Bank initiated its loosening cycle in August with a 25bps rate cut, lowering rates from 5.25% to 5.0%. In its September meeting, the Bank, resembling the ECB more than the Fed, opted to hold rates steady at 5.0%, signalling a preference for a more gradual approach to rate cuts.

- Gilt yield declined from 4.32% in May to 4.02% in August as the Bank's August rate cut signalled the start of its loosening cycle. Following the decision to hold the Bank Rate at 5.0% in September, the market response was muted, with the 10-year yield rising by only 5bps after the announcement. There is a possibility that gilt yields will rise near-term as UK policymakers remain cautious due to persistent inflation concerns, before declining in the longer term as rates fall to 3.0%.

- In August 2024, the Bank of England's Monetary Policy Committee (MPC) decided to cut the rates by 25bps to 5%. However, subsequent speeches from MPC members have supported Governor Bailey's tone with its emphasis on "gradual" reductions over time. MPC decide to hold the rate in its September Meeting.

- Nonetheless, November still looks most likely to be the next month to see a rate cut to 4.75% but, thereafter, inflation and employment data releases, as well as geo-political events, are likely to be the determinant for what happens in the remainder of 2024/25 and into 2025/26.

4.2 Interest Rate Forecasts

The Council has appointed Link Group as its treasury advisors and part of their service is to assist the Council to formulate a view on interest rates.

Link Group's latest forecast on 28th May 2024 sets out a view that short, medium and long-dated interest rates will fall back over the next year or two, although there are upside risks in respect of the stickiness of inflation and a continuing tight labour market, as well as the size of gilt issuance.

Link Group Interest Rate View	28.05.24									
	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27
BANK RATE	4.50	4.00	3.50	3.25	3.25	3.25	3.25	3.00	3.00	3.00
3 month ave earnings	4.50	4.00	3.50	3.30	3.30	3.30	3.30	3.00	3.00	3.00
6 month ave earnings	4.40	3.90	3.50	3.30	3.30	3.30	3.30	3.10	3.10	3.20
12 month ave earnings	4.30	3.80	3.50	3.40	3.40	3.40	3.40	3.20	3.30	3.40
5 yr PWLB	4.50	4.30	4.10	4.00	3.90	3.90	3.90	3.90	3.90	3.80
10 yr PWLB	4.60	4.40	4.30	4.10	4.10	4.10	4.00	4.00	4.00	3.90
25 yr PWLB	5.00	4.80	4.70	4.50	4.50	4.40	4.40	4.40	4.30	4.30
50 yr PWLB	4.80	4.60	4.50	4.30	4.30	4.20	4.20	4.20	4.10	4.10

The PWLB rate forecasts above are based on the Certainty Rate (the standard rate minus 20 bps) which has been accessible to most authorities since 1st November 2012, i.e those that provide information as required on their long term borrowing ad associated capital spending.

4.3 The Treasury Management Strategy Statement, (TMSS), for 2024/25 was approved by Cabinet on 12 February 2024.

There are no policy changes to the TMSS; the details in this report update the position in the light of the updated economic position and budgetary changes already approved.

5. APPENDICES

5.1 Appendix A - Treasury Management Strategy – Prudential Indicators – Forecast Outturn as at 30 September 2024
Appendix B – Borrowing strategy as at 30 September 2024
Appendix C - Investment Portfolio as at 30 September 2024
Appendix D - CFR, Debt Liability Benchmark and Borrowing

Appendix A - Treasury Management Strategy – Prudential Indicators – Forecast Outturn as at September 2024

The Council operates a balanced budget, which broadly means cash raised during the year will meet its cash expenditure. Part of the treasury management operations ensure this cash flow is adequately planned, with surplus monies being invested in low-risk counterparties, providing adequate liquidity initially before considering optimising investment return.

The second main function of the treasury management service is the funding of the Council's capital plans. The Capital Plans identify the borrowing need of the Council and the longer-term cash flow planning to ensure the Council can meet its capital spending requirements. Cashflow management may involve long or short-term loans and investments, using longer term cash flow surpluses for investment purposes, and / or restructuring of the Council's debt portfolio.

The Prudential Code for Capital Finance in Local Authorities provides a framework for local authority capital finance to ensure that:

(a) capital expenditure plans are affordable
(b) all external borrowing and other long-term liabilities are within prudent and sustainable levels
(c) treasury management decisions are taken in accordance with professional good practice

In taking decisions in relation to (a) and (c) above, the local authority is accountable by providing a clear and transparent framework.

The Code requires the Council to set a range of Prudential Indicators for the forthcoming financial year and at least the following two financial years.

The actual and forecast outturn, compared to those contained in the MTFS for the Prudential Indicators for this financial year are detailed below. The indicators include the Invest to Save schemes however the costs of borrowing associated with these schemes will be offset by the income generated by these projects.

The Councils Capital Position

This part of the report is structured to update:

a) The Council's capital expenditure plans;
b) How these plans are being financed;
c) The impact of the changes in the capital expenditure plans on the prudential indicators and the underlying need to borrow; and
d) Compliance with the limits in place for borrowing activity.

Indicator 1: Capital Expenditure

This indicator is the estimated capital expenditure for the year based on the Capital Programme for that period.

Capital Expenditure	2024/25 Indicator £m	2024/25 Actual at 30.09.2024 £m	2024/25 Forecast Outturn £m
Capital Bids	120.4	24.4	75.8
Transformation/Invest to Save	0.0	0.0	0.0
Total	**120.4**	**24.4**	**75.8**

The capital expenditure forecast outturn is now reduced to £75.8m as a result of the capital expenditure moratorium introduced in June 2024 to manage borrowing costs. It applies to all capital schemes apart from those that are:

- externally funded (i.e. by grant),
- absolutely required for Health and Safety, or
- Invest to Save (cashable revenue savings above the cost of borrowing).

Financed By	2024/25 Indicator £m	2024/25 Actual at 30.09.2024 £m	2024/25 Forecast Outturn £m
Capital receipts to be used to fund capital programme	0	6.0	6.0
Capital grants & contributions	60.4	18.0	48.7
Revenue contributions	0.8	0	0.0
Transformation/invest to Save	22.2	0	0.0
Net Financing Requirement	36.9	0.4	21.1
Total	**120.4**	**24.4**	**75.8**

The table above draws together the main strategy elements of the capital expenditure plans, highlighting the original supported and unsupported elements of the capital programme, and the expected financing arrangements of this capital expenditure. The borrowing element of the table increases the underlying indebtedness of the Council by way of the Capital Financing Requirement (CFR), although this will be reduced in part by revenue charges for the repayment of debt (the Minimum Revenue Provision). This direct borrowing need may also be supplemented by maturing debt and other treasury requirements.

Capital receipts of c£6m received beginning of this financial the year will be used to fund the qualifying capital schemes to reduce the capital financing requirements (CFR). Any forecast capital receipts are assumed to be used in the next financial year due to the receipts may not be available until end of this financial year.

Indicator 2: Capital Financing Requirement (CFR)
The CFR measures the Council's underlying need to borrow money in the long term for capital purposes. Any capital expenditure which has not immediately been paid for will increase the CFR.

Capital Financing Requirement	2024/25 Indicator £m	2024/25 Forecast Outturn £m
CFR B/fwd 31/3/24	635.1	633.8
Net financing requirement	36.9	21.1
Less MRP & other financing	(18.1)	(18.9)
CFR C/fwd	**653.8**	**636.0**

Indicator 3: Actuals and Estimates of the Ratio of Financing Costs to Net Revenue Budget
The Council must estimate the proportion of the revenue budget, which is taken up in financing capital expenditure i.e. the net interest cost and to make provision to repay debt.

Ratio of Gross Financing Costs to Net Revenue Budget	2024/25 Indicator	2024/25 Forecast Outturn
Total Ratio	16.4%	17.0%

Increased forecast outturn in the above ratio is linked to overspend in capital financing cost. The latest BCR forecast that £2.3m will be overspend in finance cost. This is mainly due to the higher interest rate faced by the current economic climate to refinance the existing borrowings. Bank of England rate cuts are taking longer than expected during the budget setting process.

Indicator 4: Liability benchmark – Please see appendix D

Indicator 5: The council's treasury position
The Council's treasury position as at 30 September 2024 is summarised below. The table below shows the actual external borrowing (Gross debt) against the CFR.

Gross debt & capital financing requirement	2024/25 Indicator £m	2024/25 Actual at 30.09.2024 £m	2024/25 Forecast Outturn £m
External Borrowing			
Borrowing	500.0	512.5	512.5
Repayment of borrowing	-33.0	-94.5	-94.5
Expected change in borrowing	51.7	60.0	120.1
Other long-term liabilities	27.2	27.2	27.2
Gross Debt on 30 September 2024	**545.9**	**505.2**	**565.2**
CFR	**653.8**		**636.0**
% Of Gross Debt to CFR	**83.5%**		**88.9%**

Indicator 6: The Operational Boundary
The Operational Boundary is a measure of the day to day likely borrowing for the Council. The code recognises that circumstances might arise when the boundary might be exceeded temporarily, but if this continues for a lengthy period then it ought to be investigated.

This indicator takes into consideration the capital programme over the life of the MTFS and the ability to phase the borrowing over this period. The indicator provides flexibility for the Council to take advantage of favourable interest rates in advance of the timing of the actual capital expenditure.

Operational Boundary	**2024/25 Indicator £m**	**2024/25 Forecast Outturn £m**
Borrowing	653.8	636.0
Other long-term liabilities	27.2	27.2
Total	**681.1**	**663.2**

Indicator 7: The Authorised Limit for external borrowing
The Authorised Limit represents the maximum amount the Council may borrow at any point in time in the year. It is set at a level the Council considers is "prudent".

The indicator takes account of the capital financing requirement estimated at the start of each year, plus the expected net borrowing requirement for the year. This makes allowance for the possibility that the optimum time to do all borrowing may be early in the year. It reflects the level of borrowing which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

Authorised Limit	**2024/25 Indicator £m**	**2024/25 Forecast Outturn £m**
Borrowing*	663.8	636.0
Other Liabilities	27.2	27.2
Total Authorised Limit	**691.1**	**663.2**

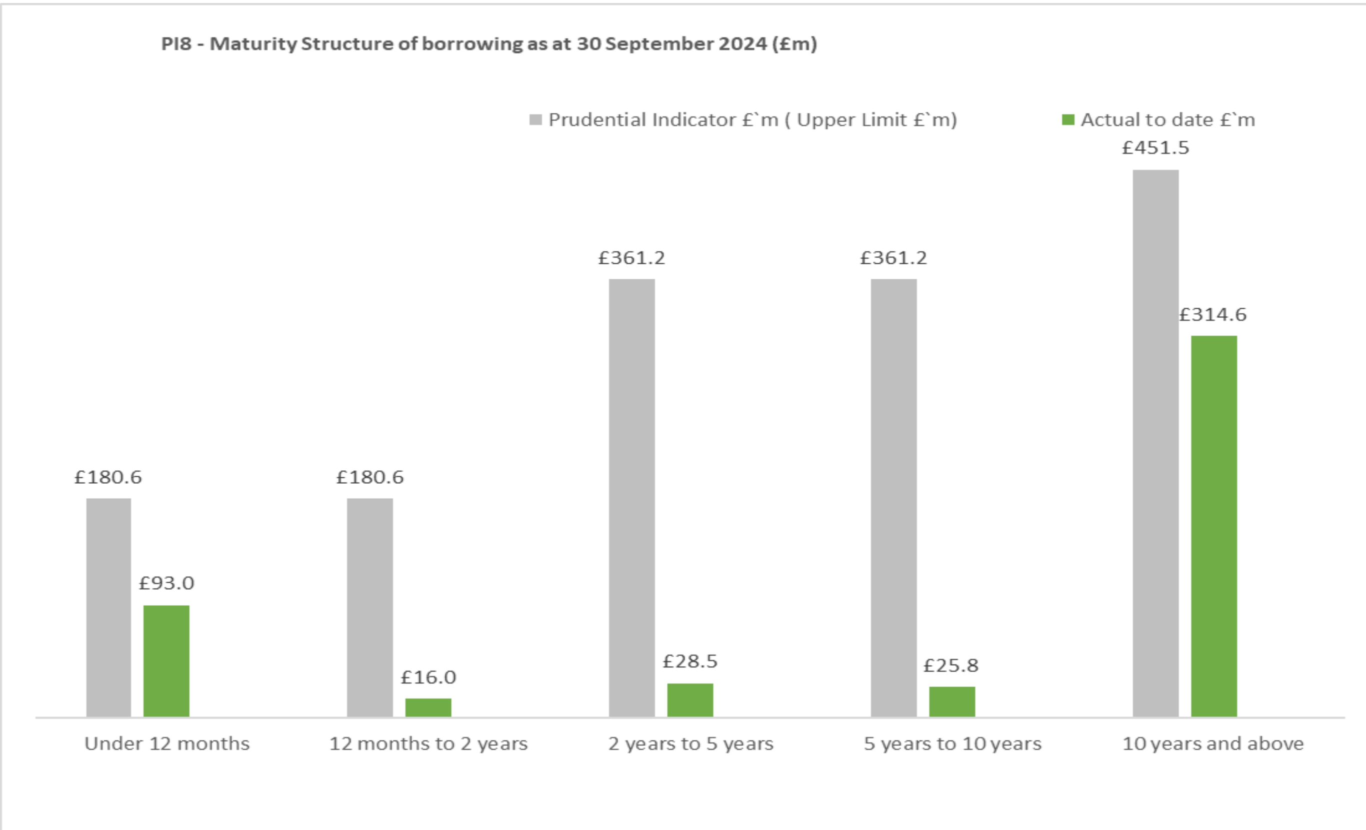
*This limit also incorporates a margin to allow for exceptional short-term movements in the Council's cash flow, bids from service departments to finance efficiencies, changes to the timing of capital payments and fluctuations in the realisation of capital receipts.

It is ultra vires (beyond the powers) to exceed the Authorised Limit so this should be set to avoid circumstances in which the Council would need to borrow more money than this limit. However, the Council can revise the limit during the course of the year. The forecast outturn is lower than the indicator as the Council does not currently anticipate any exceptional cashflow movements or borrowing in advance of need.

Indicator 8: Maturity structure of borrowing
The prudential limits have been set with regard to the maturity structure of the Council's borrowing and reflected the relatively beneficial long-term rates that were expected to be available over the next few years. The borrowing that the Council has taken up to the end of September 2024 is £478m shown in the indicator below.

Maturity Structure of borrowing	Upper Limit	As of 30 September 2024	As of 30 September 2024
		£m	%
Under 12 months *	40%	93.0	20%
12 months to 2 years	20%	16.0	3%
2 years to 5 years	30%	28.5	6%
5 years to 10 years	80%	25.8	5%
10 years and above	100%	314.6	66%

**The borrowing for under 12 months includes £5m of Lenders Option Borrowers Option (LOBO) loans. Although the loans are due to mature in 2054, they are classed as loans repayable within the financial year due to LOBO's having a call-in-date every 6 months.*



Indicator 11: Total Investments for periods longer than 365 days

Authorities are able to invest for longer than 365 days excluding loans. It would be unwise to invest a disproportionate amount of cash for too long a period particularly as the Council must maintain sufficient working capital for its operational needs, however, if higher rates are available, it may be advantageous to consider other types of financial instruments to invest in.

	2024/25 Indicator £m	2024/25 Actual at 30.09.2024 £m	2024/25 Forecast Outturn £m
Principal sums invested >365 days	10	**0**	**0**

This indicator reflects the Council's current lending policy of keeping investments short term for liquidity purposes. Also, the Council has minimised its available cash balances as an alternative to external borrowing and currently has an internally borrowed position. This is in line with the current strategy for revenue savings and avoids the 'cost of carry' associated with borrowing in advance of need.

IFRS 16 - Implementation impacts

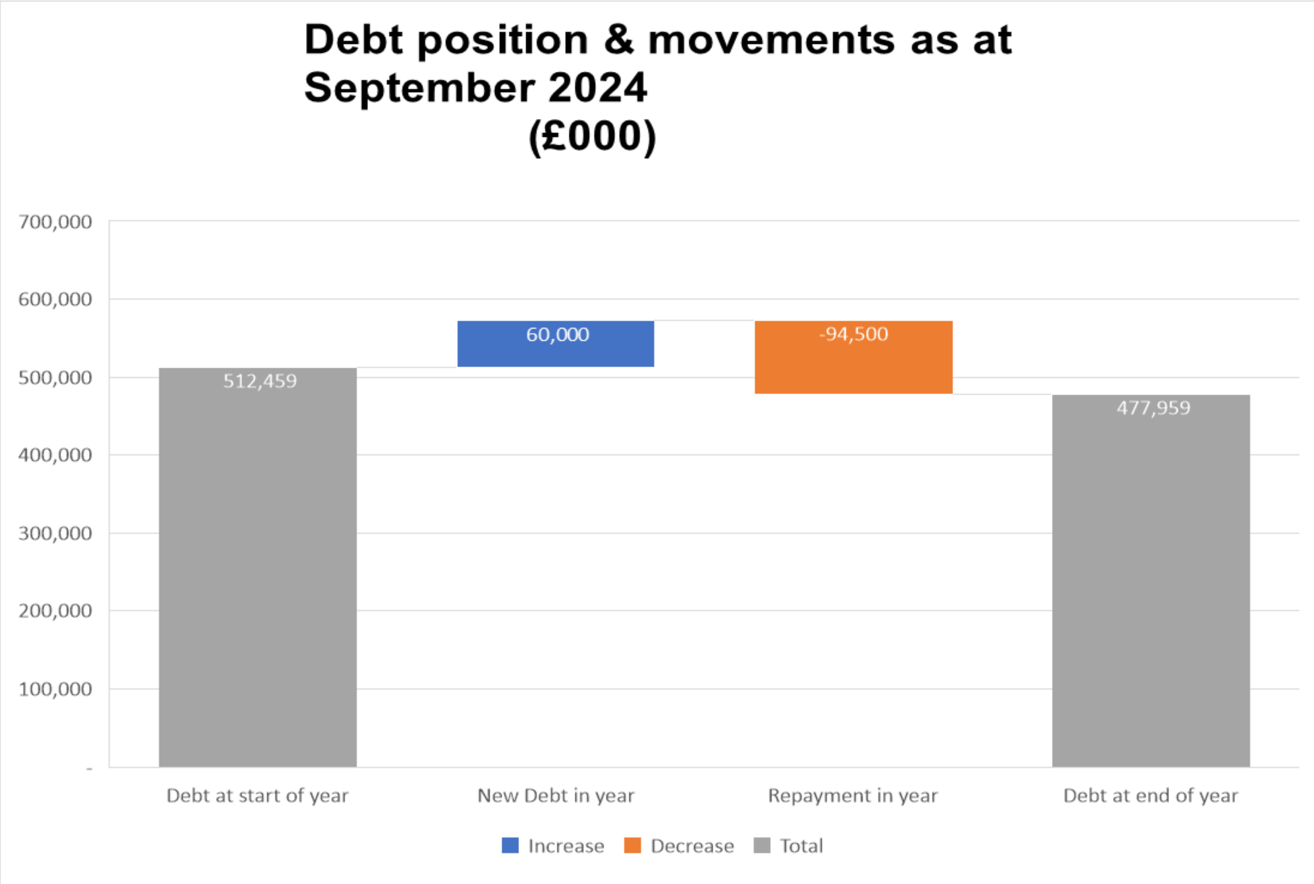
The Treasury Management Strategy and this Mid-year update does not reflect any changes to accounting for leases under IFRS 16 which came into effect on 1 April 2024. These changes require that certain leased assets not currently reported as part of the PCC's balance sheet may need to be brought on balance sheet. Should this be the case it will increase the value of Other Long-Term Liabilities. Officers are currently evaluating the impact of these changes and will bring back the results of this exercise in due course.

For future years, the authorised and operational boundaries may have to be increased to accommodate the additional long-term liabilities arising from any new leases identified as part of this exercise.

Appendix B - Borrowing Position

The Council's forecast capital financing requirement (CFR) for 2024/25 is £636m. The CFR denotes the Council's underlying need to borrow for capital purposes. As the CFR is positive the Council may borrow from the PWLB or the market (external borrowing), or from internal balances on a temporary basis (internal borrowing). The balance of external and internal borrowing is generally driven by market conditions.

The Council's external borrowing has reduced by a net £34.5m in year to date:



Due to the overall financial position and the underlying need to borrow for capital purposes (the CFR), external borrowing of £60m was undertaken to refinance maturing debt and to manage the cashflow requirements. The capital programme is being kept under regular review to assess the effects of inflationary and increased capital financing cost pressures. Our borrowing strategy will, therefore, also be regularly reviewed and then revised, in order to achieve optimum value and risk exposure in the long-term.

It is anticipated that some replacement borrowing will be required during this financial year.

PWLB maturity certainty rates (gilts plus 80bps) year to date to 30 September 2024

Gilt yields and PWLB certainty rates were less volatile than at this time last year. Overall, the 10, 25 and 50-year part of the curve endured a little volatility but finished September very much as it started in April.

At the beginning of April, the 5-year certainty rate was the cheapest part of the curve at 4.72% whilst the 25-year rate was relatively expensive at 5.28%. May saw yields at their highest across the whole curve.

Conversely, 17 September saw the low point for the whole curve, with the 5-year certainty rate falling to 4.31% before rebounding to 4.55% by the end of the month. Similarly, the 50-year certainty rate fell to 4.88% but finished the month at 5.13%, slightly higher than at the start of April.

Appendix C - Investment Portfolio

The Treasury Management Strategy Statement (TMSS) for 2024/25 to 2026/27, which includes the Annual Investment Strategy, was approved by the Council on 12 February 2024. In accordance with the CIPFA Treasury Management Code of Practice, it sets out the Council's investment priorities as being:

- Underlying Security of capital
- Liquidity
- Yield

The Council will aim to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity and with the Council's risk appetite. In the current economic climate, it is considered appropriate to keep the majority of investments short term to cover cash flow needs, but also to seek out value available in periods up to 12 months with high credit rated financial institutions, using the Link suggested creditworthiness approach. In addition, the Council is also seeking approval to explore the options to invest longer term in non-specified investments.

Investment Counterparty
The Council has begun to invest in a wider range of institutions to take advantage of rising interest rates. Surplus cash is invested for short periods with Barclays, the Churches, Charities and Local Authorities (CCLA) money market fund, Federated Hermes, AVIVA Investors, Aberdeen GBP Liquidity, JP Morgan and LGIM Short Term Sterling Prime money market fund. The Council also uses Standard Chartered, SMBC Bank International, Lloyds, Goldman Sachs, Handelsbanken banks and with other local authorities for its short-term investments.

Investment balances
The Council held £16.365m of investments as at 30th September 2024. These funds were available on a temporary basis, and the level of funds available was mainly dependent on the timing of grants, and progress on the capital programme.

Estimated interest earned on investments as at 30th September 2024 is £1.0m.

Investment performance as at 30th September 2024

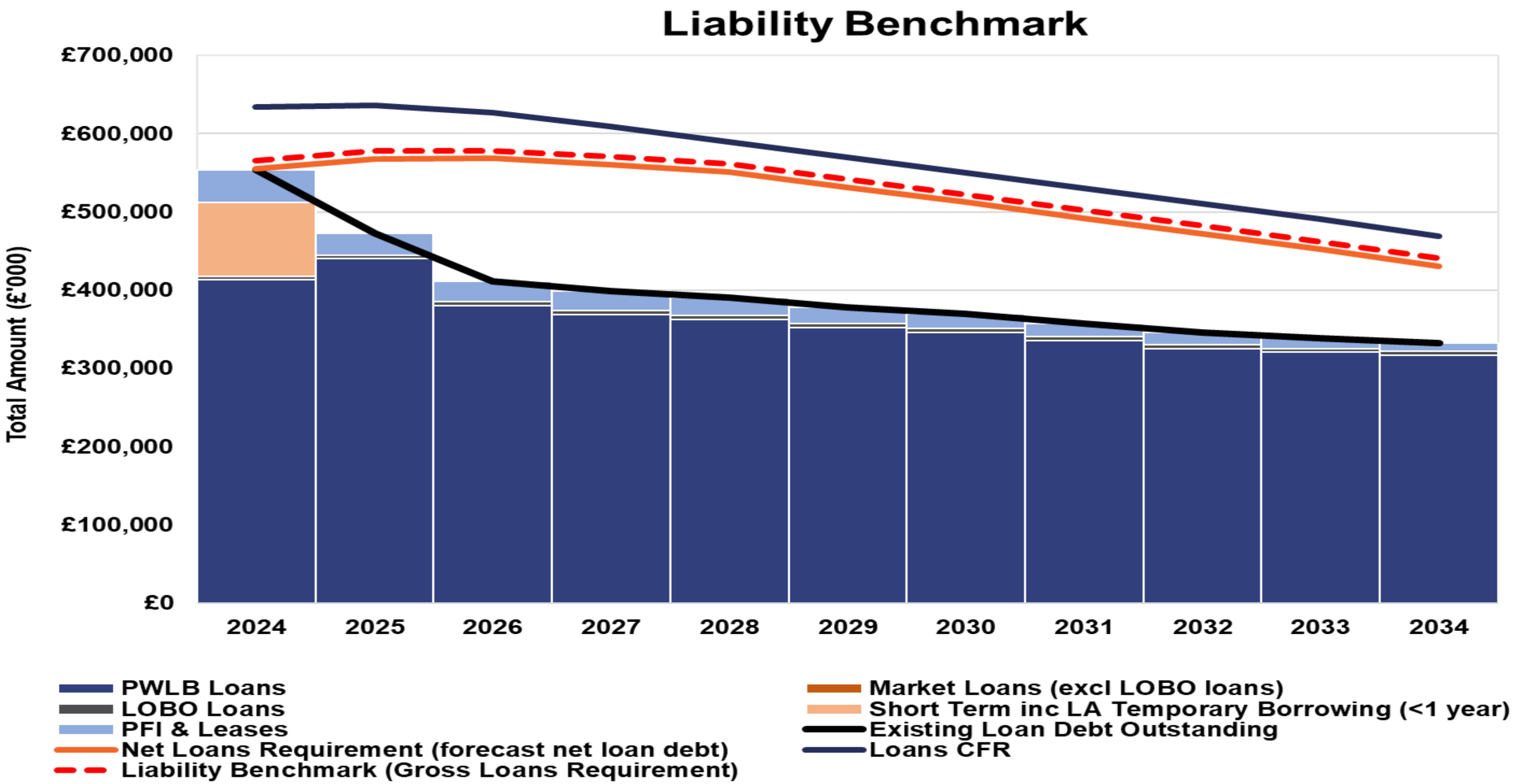
Investment Portfolio '000	**30 September 2024**		
	Principal	Average Rate (%)	Average Life (days)
MMFs	16,365	5.01%	1
Banks	0	0.00%	0
Local Authorities	0	0.00%	0
Total Investments	**16,365**	5.01%	0

Investment balances are mainlybeing kept liquid by placing with money market funds to manage the daily cashflow requirments. The council is very much committed to its Environmental, Social and Governance (ESG) policy. In support of the the ESG commitments the council will look into placing its investment with ESG related investments. In the last 6 months to September 2024, the Council has had £8.5m one month green deposit with Lloyds plc and £10m two month green deposit with SMBC and generated a total investment income of c£127k.

Appendix D

CFR, Debt Liability Benchmark and borrowing.

Comparison of borrowing parameters to actual external borrowing:



The liability benchmark is effectively the net borrowing requirement plus a liquidity allowance. It is calculated by deducting the amount of investable resources available on the balance sheet (reserves, cash flow balances) from the amount of outstanding external debt and then adding the minimum level of investments required to manage day-to-day cash flow