Crawley Borough Council

Report to Overview & Scrutiny Commission
29 January 2024

Report to Cabinet
31 January 2024

Treasury Management Strategy 2024/2025

Report of the Head of Corporate Finance– **FIN/644**

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1. Purpose

1.1 The Strategy for 2024/25 covers two main areas:

Capital
- the capital plans and the associated prudential indicators;
- the Minimum Revenue Provision (MRP) policy.

Treasury Management
- 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.

2. Recommendations

2.1 To the Overview and Scrutiny Commission:

That the Commission considers the report and decides what comments, if any, it wishes to submit to the Cabinet.

2.2 To the Cabinet

The Cabinet is requested to recommend to Full Council the approval of:-

a) the Treasury Prudential Indicators and the Minimum Revenue Provision (MRP) Statement contained within Section 5.4;
b) the Treasury Management Strategy contained within Section 6;
c) the Investment Strategy contained within Section 7;

3. Reasons for the Recommendations

3.1 The Council's financial regulations, in accordance with the CIPFA Code of Practice for Treasury Management, requires a Treasury Management Strategy to be approved for the forthcoming financial year. This report complies with those requirements.

4. Background

4.1 The Council is required to operate balanced General Fund and Housing Revenue Account (HRA) revenue budgets, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low-risk counterparties or instruments commensurate with the Council's low risk appetite, providing adequate liquidity initially before considering investment return.

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

4.3 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 those balances.

4.4 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.

4.5 CIPFA defines treasury management as:

"The management of the local authority's borrowing, investments and cash flows, including 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."

4.6 This report takes into account the revenue and capital implications arising in the 2024/25 Budget and Council Tax report (FIN/642).

5. The Capital Prudential Indicators 2024/25 – 2026/27

5.1 The Capital Expenditure Plans

5.1.1 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.

Capital Expenditure

5.1.2 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.

Capital Expenditure £'000	2022/23 Actual *	2023/24 Estimate	2024/25 Forecast	2025/26 Forecast	2026/27 Forecast
Joint responsibility inc. New Town Hall	7,442	2,012	3,565	0	0
Cabinet	428	333	339	300	0
Environment Services & Sustainability	489	3,521	365	210	85
Housing General Fund	1,353	4,799	6,505	15	15
Planning & Economic Development	1,225	6,690	14,479	15,724	1,955
Resources	141	626	1,809	0	0
Wellbeing	615	1,658	490	0	0
General Fund	**11,695**	**19,639**	**27,552**	**16,249**	**2,055**
HRA	**19,871**	**27,665**	**38,656**	**35,504**	**20,677**
Non-treasury investments **	0	0	0	0	0
Total	**31,566**	**47,304**	**66,208**	**51,753**	**22,732**

* £44k of capital expenditure in 2022/23 arises from a change in the accounting for leases and does not represent cash expenditure

** Non-treasury investments relate to areas such as capital expenditure on investment properties, loans to third parties, etc.

5.1.3 The table below shows how the above capital expenditure plans are being financed. Any shortfall of resources results in a borrowing need.

Financing of Capital Expenditure £'000	2022/23 Actual	2023/24 Estimate	2024/25 Forecast	2025/26 Forecast	2026/27 Forecast
Capital receipts	8,038	5,046	6,826	4,910	352
Capital reserves	0	1,577	252	0	0
1-4-1 receipts	2,627	2,603	7,321	8,097	8,271
Revenue	1,447	4,860	544	315	15
Capital grants	2,369	8,852	18,904	11,024	1,688
Major Repairs Reserve	8,387	19,568	20,409	27,407	12,406
Net financing need for the year	**8,698**	**4,798**	**11,952**	**0**	**0**

5.2 Capital Financing Requirement (The Council's borrowing need)

5.2.1 The Council's Capital Financing Requirement (CFR) is 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 it's underlying need to borrow. Any capital expenditure which has not been financed through a revenue or capital resource will increase the CFR.

5.2.2 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 assets life, and so charges the economic consumption of capital assets as they are used.

5.2.3 The Council is asked to approve the CFR projections below:

£'000	2022/23 Actual	2023/24 Estimate	2024/25 Forecast	2025/26 Forecast	2026/27 Forecast
Capital Financing Requirement					
CFR – General Fund	18,029	19,730	25,053	24,344	23,621
CFR - HRA	249,325	240,410	233,925	220,925	205,925
CFR – Non-financial investments	0	0	0	0	0
Total CFR	**267,354**	**260,140**	**258,978**	**245,269**	**229,546**
Movement in CFR	**7,029**	**(7,214)**	**(1,162)**	**(13,709)**	**(15,723)**

Movement in CFR represented by					
Net financing need for the year (above)	0	4,798	11,952		
IFRS16 Leases	44				
Less MRP/VRP and other financing movements - GF	(791)	(12)	(114)	(709)	(723)
Less MRP/VRP and other financing movements - HRA	(11,000)	(12,000)	(13,000)	(13,000)	(15,000)
Movement in CFR	**(11,747)**	**(7,214)**	**(1,162)**	**(13,709)**	**(15,723)**

5.3 Core funds and expected investment balances

5.3.1 The application of resources (capital receipts, reserves etc.) to either finance capital expenditure or support the revenue budget will have an ongoing impact on investments unless resources are supplemented each year from new sources (asset sales etc.).

Detailed below are estimates of the year end balances for each resource stream which form the anticipated day to day cash flow balances. The external borrowing relates to the PWLB loans taken out for the HRA self-financing. The downward forecast reflects the repayment of those loans in line with the repayment schedule.

Year End Resources £'000	2022/23 Actual	2023/24 Estimate	2024/25 Forecast	2025/26 Forecast	2026/27 Forecast
Total CFR	**267,354**	**260,140**	**258,978**	**245,269**	**229,546**
Less: External borrowing*	(249,356)	(237,344)	(227,338)	(220,331)	(208,325)
Under/over borrowing	**17,998**	**22,796**	**31,640**	**24,938**	**21,221**
Less: Usable reserves	(86,244)	(53,971)	(28,059)	(13,078)	(10,951)
Less: Working Capital**	(29,779)	(20,000)	(20,000)	(20,000)	(20,000)
Expected investments	**(98,025)**	**(51,175)**	**(16,419)**	**(8,140)**	**(9,730)**

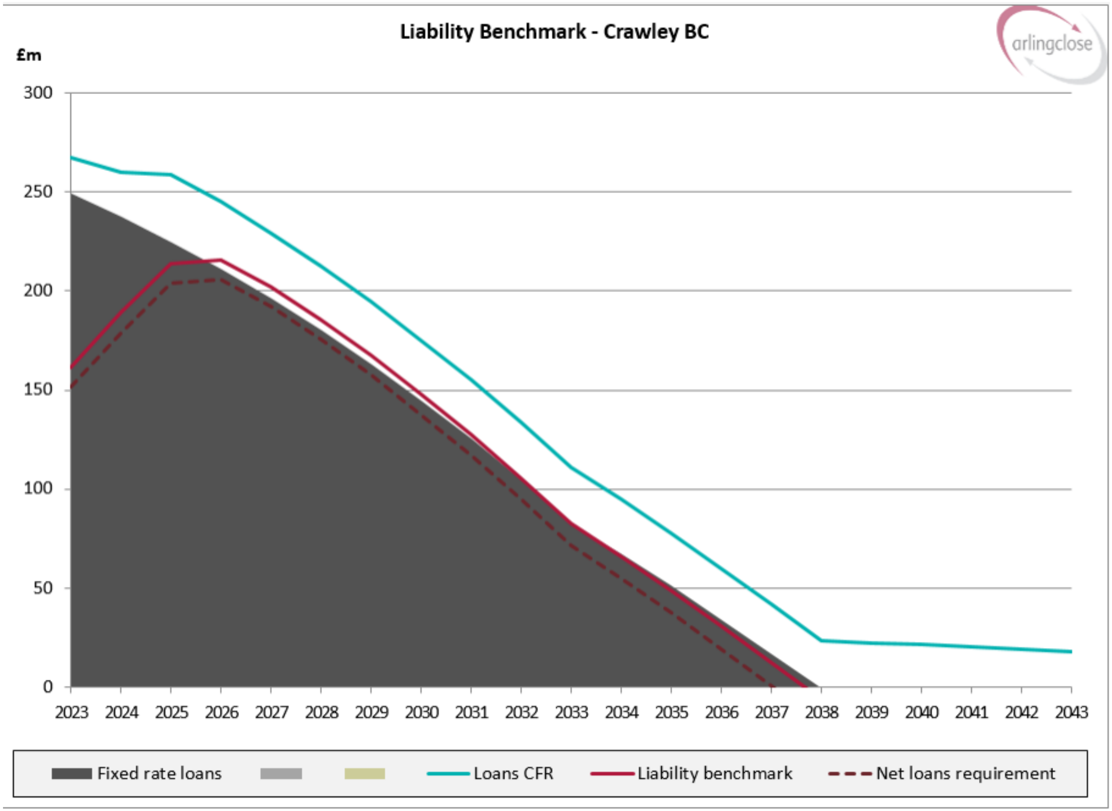
* shows only loans to which the Council is committed and excludes optional refinancing
** Working capital balances shown are estimated year-end; these may be higher mid-year

5.3.2 Liability benchmark: To compare the Council's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing. This assumes the same forecasts as table in 5.3.1 above but that cash and investment balances are kept to a minimum level of £10m at each year-end to maintain sufficient liquidity but minimise credit risk.

5.3.3 The liability benchmark is an important tool to help establish whether the Council is likely to be a long-term borrower or long-term investor in the future, and so shape its strategic focus and decision making. The liability benchmark itself represents an estimate of the cumulative amount of external borrowing the Council must hold to fund its current capital and revenue plans while keeping treasury investments at the minimum level required to manage day-to-day cash flow.

£'000	2022/23 Actual	2023/24 Estimate	2024/25 Forecast	2025/26 Forecast	2026/27 Forecast
Total CFR	**267,354**	**260,140**	**258,978**	**245,269**	**229,546**
Less: Usable reserves	(86,244)	(53,971)	(28,059)	(13,078)	(10,951)
Less: Working Capital	(29,779)	(20,000)	(20,000)	(20,000)	(20,000)
Net loans requirement	**151,331**	**186,169**	**210,919**	**212,191**	**198,595**
Plus: Liquidity allowance	10,000	10,000	10,000	10,000	10,000
Liability benchmark	**161,331**	**196,169**	**220,919**	**222,191**	**208,595**

5.3.4 Following on from the medium-term forecasts in the table above, the long-term liability benchmark assumes capital expenditure funded by borrowing of £12m in 2024/25, minimum revenue provision on new capital expenditure based on a 40-year asset life and income, expenditure and reserves all increasing by inflation of 4.0% a year. This is shown in the chart below:



5.4 Minimum Revenue Provision (MRP) Policy Statement

5.4.1 Where the Council finances capital expenditure by debt it must put aside resources to repay that debt in later years. The amount charged to the revenue budget for the repayment of debt is known as MRP.

5.4.2 The MHCLG Guidance requires the Council to approve a MRP Policy Statement each year and recommends a number of options for calculating a prudent amount of MRP. The following statement only incorporates options recommended in the Guidance.

5.4.3 The broad aim of the MHCLG Guidance is to ensure that capital expenditure is financed over a period that is either reasonably commensurate with that over which the capital expenditure provides benefits, or, in the case of borrowing supported by Government Revenue Support Grant, reasonably commensurate with the period implicit in the determination of that grant.

5.4.4 The Council is recommended to approve the following MRP Statements in 5.4.5 to 5.4.8.

5.4.5 MRP will be determined by charging the expenditure over the expected useful life of the relevant asset by either:

- equal instalments
- annuity method where the income stream of the asset increases over time

starting in the year after the asset becomes operational.

MRP will be charged as follows:

- purchases of freehold land will be charged over 50 years.

- Other property (buildings, equipment etc) between 20 and 50 years as appropriate
- expenditure which has been capitalised by regulation or direction will be charged over 20 years.

5.4.6 Where former operating leases have been brought onto the balance sheet on 1 April 2022 due to the adoption of the *IFRS 16 Leases* accounting standard, and the asset values have been adjusted for accruals, prepayments, premiums and/or discounts, then the annual MRP charges will be adjusted so that the total charge to revenue remains unaffected by the new standard.

5.4.7 For capital expenditure loans to third parties, the Council will make nil MRP unless (a) the loan is an investment for commercial purposes and no repayment was received in year or (b) an expected credit loss was recognised or increased in-year, but will instead apply the capital receipts arising from principal repayments to reduce the capital financing requirement instead. In years where there is no principal repayment on loans that are investments for commercial purposes, MRP will be charged in accordance with the MRP policy for the assets funded by the loan, including where appropriate, delaying MRP until the year after the assets become operational. Sufficient MRP will be charged to ensure that the outstanding capital financing requirement (CFR) on the loan is no higher than the principal amount outstanding less the expected credit loss. This option was proposed by the government in its recent MRP consultation and in the Council's view is consistent with the current regulations.

5.4.8 No MRP will be charged in respect of assets held within the Housing Revenue Account.

5.4.9 Based on the Council's latest estimate of its CFR on 31 March 2024, the budget for MRP has been set as follows:

	31.03.2023 Estimated CFR £'000	**2023/24 Estimated MRP £'000**
Unsupported capital expenditure after 31.03.2008	0	(546)
Leases and Private Finance Initiative	19,711	(6)
Voluntary overpayment (or use of prior year overpayments)	19	**438**
Total General Fund	**0**	**(114)**
Assets in the Housing Revenue Account	0	0
HRA subsidy reform payment	**19,730**	**(13,000)**
Total Housing Revenue Account	**0**	**(13,000)**
Total	**240,410**	**(13,114)**

5.4.8 Overpayments: In earlier years, the Council has made a voluntary overpayment of MRP to the value of £922k which is available to reduce the revenue charges in later years. It is planned to use some of this 2024/25.

MRP Overpayments	£’000
Actual balance 31.03.2023	922
Approved drawdown 2023/24	-484
Expected balance 31.03.2024	438
Planned drawdown 2024/25	-438
Forecast balance 31.03.2025	0

6. Treasury Management Strategy

6.1 The capital expenditure plans set out in Section 5 provide details of the service activity of the Council. The Council’s main objectives when borrowing are to achieve a low but certain cost of finance while retaining flexibility should plans change in future. These objectives are often conflicting, and the Council therefore seeks to strike a balance between cheap short-term loans (currently available at around 5.40%) and long-term fixed rate loans where the future cost is known but higher (currently 4.71% to 5.53%).

6.2 Current portfolio position

6.2.1 The Council’s treasury portfolio position at 31 March 2024, with forward projections are summarised below. The table shows the actual external debt against the underlying capital borrowing need (the CFR), highlighting any over or under borrowing.

£’000	2022/23 Actual	2023/24 Estimate	2024/25 Forecast	2025/26 Forecast	2026/27 Forecast
External Debt					
Debt at 1 April	260,325	249,325	237,325	227,325	220,325
Expected change in Debt	(11,000)	(12,000)	(10,000)	(7,000)	(12,000)
Other long-term liabilities (OLTL)	44	31	19	13	6
Expected change in OLTL	(13)	(12)	(6)	(7)	(6)
Actual gross debt at 31 March	**249,356**	**237,344**	**227,338**	**220,331**	**208,325**
The Capital Financing Requirement	267,354	260,140	258,978	245,269	229,546
(Under) / over borrowing	17,998	22,796	31,640	24,938	21,221

6.2.2 Within the above figures there is no debt relating to commercial activities/non-financial investment as shown below:

	2022/23 Actual	2023/24 Estimate	2024/25 Forecast	2025/26 Forecast	2026/27 Forecast
External Debt for commercial activities / non-financial investments					
Actual debt at 31 March £m	0	0	0	0	0
Percentage of total external debt %	0	0	0	0	0

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

6.3 Treasury Indicators

6.3.1 The Council measures and manages its exposures to treasury management risks using the following indicators.

6.3.1 Affordable borrowing limit

The Council is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt) each year. In line with statutory guidance, a lower “operational boundary” is also set as a warning level should debt approach the limit.

Operational boundary £’000	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate
Debt	249,325	237,325	227,325	220,325
Other long term liabilities	19	13	6	0
Total	249,344	237,338	227,331	220,325

6.3.2 The Council is asked to approve the following Authorised Limit:

Authorised limit £’000	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate
Debt	269,325	257,325	247,325	240,325
Other long term liabilities	19	13	6	0
Total	269,344	257,338	247,331	240,325

6.3.3 **Security**

The Council has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average credit rating of its investment portfolio. This is calculated by applying a score to each investment (AAA=1, AA+=2, etc.) and taking the arithmetic average, weighted by the size of each investment. Unrated investments are assigned a score based on their perceived risk.

Credit risk indicator	Target
Portfolio average credit rating	A

6.3.4 **Liquidity**

The Council has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments within a one week period, without additional borrowing.

Liquidity risk indicator	Target
Total cash available within 1 week	£3m

6.3.5 **Interest rate exposures**: This indicator is set to control the Council's exposure to interest rate risk. The upper limits on the one-year revenue impact of a 1% rise or fall in interest rates will be:

Interest rate risk indicator	Limit
Upper limit on one-year revenue impact of a 1% rise in interest rates	£1,200,000
Upper limit on one-year revenue impact of a 1% fall in interest rates	£1,200,000

The impact of a change in interest rates is calculated on the assumption that maturing loans and investments will be replaced at new market rates.

6.3.6 **Maturity structure of borrowing**

This indicator is set to control the Council's exposure to refinancing risk. The upper and lower limits on the maturity structure of borrowing will be:

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%	30%
5 years to 10 years	0%	50%
10 years to 20 years	0%	40%
20 years to 30 years	0%	10%
30 years to 40 years	0%	10%
40 years to 50 years	0%	10%

Time periods start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment.

6.3.6 **Principal sums invested for periods longer than a year.**

The purpose of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments. The prudential limits on the long-term principal sum invested to final maturities greater than one year will be:

Price risk indicator	**2024/25**	**2025/26**	**2026/27**	**No fixed date**
Limit on principal invested greater than 1 year	£20m	£15m	£10m	£10m

6.3.7 Long-term investments with no fixed maturity date include strategic pooled funds and real estate investment trusts but exclude money market funds and bank accounts with no fixed maturity date as these are considered short-term.

6.4 Prospects for Interest Rates

6.4.1 The Council has appointed Arlingclose Limited as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. A more detailed economic and interest rate forecast table provided by Arlingclose is attached below with assumptions and forecast detail at Appendix 1.

	Current	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26
Official Bank Rate													
Upside risk	0.00	0.25	0.50	0.50	0.75	0.75	0.75	0.75	0.75	0.75	0.75	1.00	1.00
Central Case	5.25	5.25	5.25	5.25	5.00	4.75	4.25	4.00	3.75	3.50	3.25	3.00	3.00
Downside risk	0.00	0.00	-0.25	-0.50	-0.75	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
3-month money market rate													
Upside risk	0.00	0.25	0.50	0.50	0.75	0.75	0.75	0.75	0.75	0.75	0.75	1.00	1.00
Central Case	5.40	5.40	5.40	5.30	5.15	4.80	4.30	4.10	3.80	3.50	3.25	3.05	3.05
Downside risk	0.00	0.00	-0.25	-0.50	-0.75	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
5yr gilt yield													
Upside risk	0.00	0.50	0.70	0.70	0.85	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Central Case	4.28	4.35	4.30	4.25	4.10	4.00	3.75	3.50	3.40	3.30	3.30	3.30	3.35
Downside risk	0.00	-0.55	-0.75	-0.85	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
10yr gilt yield													
Upside risk	0.00	0.50	0.70	0.70	0.80	0.90	1.00	1.10	1.20	1.20	1.20	1.20	1.20
Central Case	4.32	4.40	4.35	4.30	4.25	4.15	4.00	3.80	3.75	3.65	3.60	3.65	3.70
Downside risk	0.00	-0.55	-0.75	-0.85	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
20yr gilt yield													
Upside risk	0.00	0.50	0.70	0.70	0.80	0.90	1.00	1.10	1.20	1.20	1.20	1.20	1.20
Central Case	4.78	4.70	4.65	4.55	4.45	4.35	4.25	4.25	4.25	4.25	4.25	4.25	4.25
Downside risk	0.00	-0.55	-0.75	-0.85	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
50yr gilt yield													
Upside risk	0.00	0.50	0.70	0.70	0.80	0.90	1.00	1.10	1.20	1.20	1.20	1.20	1.20
Central Case	4.38	4.30	4.25	4.20	4.15	4.15	4.10	4.10	4.10	4.10	4.10	4.10	4.10
Downside risk	0.00	-0.55	-0.75	-0.85	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00

PWLB Standard Rate = Gilt yield + 1.00%
PWLB Certainty Rate = Gilt yield + 0.80%
PWLB HRA Rate = Gilt yield + 0.40%
UK Infrastructure Bank Rate = Gilt yield + 0.40%

6.4.2 Arlingclose forecasts that Bank Rate will start to reduce in 2024 as the Bank of England attempts to prevent recession whilst reducing inflation which is significantly above its 2% target. Although UK inflation and wage growth remain elevated, they forecasts that Bank Rate has peaked at 5.25%. The Bank of England's Monetary Policy Committee will start reducing rates in 2024 to stimulate the UK economy but will be reluctant to do so until it is sure there will be no lingering second-round effects. Arlingclose predicts rate cuts from Q3 2024 to a low of around 3% by early-mid 2026.

6.4.3 Arlingclose expects long-term gilt yields to be broadly stable at current levels (amid continued volatility), following the decline in yields towards the end of 2023, which reflects the expected lower medium-term path for Bank Rate. Yields will remain relatively higher than in the past, due to quantitative tightening and significant bond supply. As ever, there will undoubtedly be short-term volatility due to economic and political uncertainty and events. Arlingclose sees rate cuts from Q3 2024 to a low of around 3% by early-mid 2026.

6.4.4 For the purpose of setting the budget, it has been assumed that new treasury investments will be made at an average rate/yield of 4.89%, and that new long-term loans will be borrowed at an average rate of 4.77%.

6.5 Borrowing Strategy

6.5.1 The Council currently holds £249.325 million of loans, a decrease of £11m on the previous year, as part of HRA self-financing. The table in 5.1.3 shows that the Council expects to borrow up to £4.8m in 2024/25. The Council may also borrow additional sums to pre-fund future years' requirements, providing this does not exceed the authorised limit for borrowing of £257.338 million. 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. This strategy is prudent as investment returns are low and counterparty risk is still an issue that needs to be considered.

6.5.2 The Council's chief objective when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving certainty of those costs over the period for which funds are required. The flexibility to renegotiate loans should the Council's long-term plans change is a secondary objective.

6.5.3 Given the significant cuts to public expenditure, and in particular to local government funding, the Council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. Short-term interest rates are currently at a 15-year high but are expected to fall in the coming years and it is therefore likely to be more cost effective over the medium-term to either use internal resources, or to borrow short-term loans instead.

6.5.4 By doing so, the Council is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of internal borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise modestly. Arlingclose will assist the Council with this 'cost of carry' and breakeven analysis. Its output may determine whether the Council borrows additional sums at long-term fixed rates in

2024/25 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.

6.5.6 The Council has previously raised all of its long-term borrowing from the PWLB but will consider long-term loans from other sources including banks, pensions and local authorities, and will investigate the possibility of issuing bonds and similar instruments, in order to lower interest costs and reduce over-reliance on one source of funding in line with the CIPFA Code. PWLB loans are no longer available to local authorities planning to buy investment assets primarily for yield; the Council intends to avoid this activity in order to retain its access to PWLB loans.

6.5.7 Alternatively, the Council may arrange forward starting loans, where the interest rate is fixed in advance, but the cash is received in later years. This would enable certainty of cost to be achieved without suffering a cost of carry in the intervening period.

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

6.6 Related Matters

6.6.1 **Housing Revenue Account (HRA)**

On 1st April 2012, the Council notionally split each of its existing long-term loans into General Fund and HRA pools. In the future, new long-term loans borrowed will be assigned in their entirety to one pool or the other. Interest payable and other costs/income arising from long-term loans (e.g. premiums and discounts on early redemption) will be charged/ credited to the respective revenue account. Differences between the value of the HRA loans pool and the HRA's underlying need to borrow (adjusted for HRA balance sheet resources available for investment) will result in a notional cash balance which may be positive or negative. This balance will be measured as an average over year and interest transferred between the General Fund and HRA at the Council's average interest rate on investments, adjusted for credit risk

6.6.3 **Markets in Financial Instruments Directive**

The Council has opted up to professional client status with its providers of financial services, including advisers, banks, brokers and fund managers, allowing it access to a greater range of services but without the greater regulatory protections afforded to individuals and small companies. Given the size and range of the Council's treasury management activities, the Head of Corporate Finance (S151 officer and Chief Executive believe this to be the most appropriate status.

6.7 Debt rescheduling

6.7.1 The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. Other lenders may also be prepared to negotiate premature redemption terms. The Council may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall cost saving or a reduction in risk. The recent rise in interest rates means that more favourable debt rescheduling opportunities should arise than in previous years.

6.7.2 Any rescheduling will be reported to the Cabinet.

6.8 Other sources of debt finance

6.8.1 In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:
- leasing
- hire purchase
- Private Finance Initiative
- sale and leaseback

6.9 Municipal Bonds Agency

UK Municipal Bonds Agency plc was established in 2014 by the Local Government Association as an alternative to the PWLB. It issues bonds on the capital markets and lends the proceeds to local authorities. This is a more complicated source of finance than the PWLB for two reasons: borrowing authorities will be required to provide bond investors with a guarantee to refund their investment in the event that the agency is unable to for any reason; and there will be a lead time of several months between committing to borrow and knowing the interest rate payable. Any decision to borrow from the Agency will therefore be the subject of a separate report to Full Council.

6.10 Approved Sources of Long and Short Term Borrowing

- HM Treasury's PWLB lending facility (formerly the Public Works Loan Board)
- UK Infrastructure Bank Ltd
- any institution approved for investments (see below)
- any other bank or building society authorised to operate in the UK
- any other UK public sector body
- UK public and private sector pension funds (except West Sussex Pension Fund)
- capital market bond investors
- retail investors via a regulated peer-to-peer platform
- UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues

7. Treasury Investment Strategy

7.1 The Council holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Council's treasury investment balance has ranged between £97.408 and £153.281 million, and lower levels are expected in the forthcoming year due to planned expenditure in the capital programme.

7.1.1 **Objectives**

The CIPFA Code requires the Council to invest its treasury funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income. Where balances are expected to be invested for more than one year, the Council will aim to achieve a total return that is equal or higher than the prevailing rate of inflation, in order to maintain the spending power of the sum invested.

7.1.2 **Strategy**

The Council currently has £10m invested with Royal London's Short Term Fixed Income Enhanced Fund to provide an improved yield: there are no plans to change this investment. The Council plans to keep investments short-term whilst interest rates rise. Available cash reserves will continue to reduce with the ongoing Capital Programme expenditure.

7.1.3 **Environmental, social and governance (ESG)**

ESG considerations are increasingly a factor in global investors' decision making, but the framework for evaluating investment opportunities is still developing and therefore the Authority's ESG policy does not currently include ESG scoring or other real-time ESG criteria at an individual investment level. When investing in banks and funds, the Council will prioritise banks that are signatories to the UN Principles for Responsible Banking and funds operated by managers that are signatories to the UN Principles for Responsible Investment, the Net Zero Asset Managers Alliance and/or the UK Stewardship Code.

7.1.4 **Approved counterparties**

The Council may invest its surplus funds with any of the counterparty types in the table below, subject to the limits shown.

Sector	**Time limit**	**Counterparty limit**	**Sector limit**
The UK Government	50 years	Unlimited	n/a
Local authorities & other government entities	25 years	£15m	Unlimited
Secured investments *	25 years	£10m	Unlimited
Banks (unsecured) *	13 months	£10m	Unlimited
Building societies (unsecured) *	13 months	£5m	£10m
Registered providers (unsecured) *	5 years	£5m	£10m
Money market funds *	n/a	£10m	Unlimited
Strategic pooled funds	n/a	£10m	£20m
Real estate investment trusts	n/a	£10m	£20m
Other investments *	5 years	£5m	£10m

*** Minimum credit rating:** Treasury investments in the sectors marked with an asterisk will only be made with entities whose lowest published long-term credit rating is no lower than A-. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used. However, investment decisions are never made solely based on credit ratings, and all other relevant factors including external advice will be taken into account.

For entities without published credit ratings, investments may be made where external advice indicates the entity to be of similar credit quality.

7.1.6 Government

Loans to, and bonds and bills issued or guaranteed by, national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is generally a lower risk of insolvency, although they are not zero risk. Investments with the UK Government are deemed to be zero credit risk due to its ability to create additional currency and therefore may be made in unlimited amounts for up to 50 years.

7.1.7 Secured investments

Investments secured on the borrower's assets, which limits the potential losses in the event of insolvency. The amount and quality of the security will be a key factor in the investment decision. Covered bonds and reverse repurchase agreements with banks and building societies are exempt from bail-in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the higher of the collateral credit rating and the counterparty credit rating will be used. The combined secured and unsecured investments with any one counterparty will not exceed the cash limit for secured investments.

7.1.8 Banks and building societies (unsecured)

Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail. See below for arrangements relating to operational bank accounts.

7.1.9 Registered providers (unsecured)

Loans to, and bonds issued or guaranteed by, registered providers of social housing or registered social landlords, formerly known as housing associations. These bodies are regulated by the Regulator of Social Housing (in England), the Scottish Housing Regulator, the Welsh Government and the Department for Communities (in Northern Ireland). As providers of public services, they retain the likelihood of receiving government support if needed.

7.1.10 Money market funds

Pooled funds that offer same-day or short notice liquidity and very low or no price volatility by investing in short-term money markets. They have the advantage over bank accounts of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a small fee. Although no sector limit applies to money market funds, the Council will take care to diversify its liquid investments over a variety of providers to ensure access to cash at all times.

7.1.11 **Strategic pooled funds**

Bond, equity and property funds that offer enhanced returns over the longer term but are more volatile in the short term. These allow the Council to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Council's investment objectives will be monitored regularly.

7.1.12 **Real estate investment trusts** (REIT's)

Shares in companies that invest mainly in real estate and pay the majority of their rental income to investors in a similar manner to pooled property funds. As with property funds, REITs offer enhanced returns over the longer term, but are more volatile especially as the share price reflects changing demand for the shares as well as changes in the value of the underlying properties.

7.1.13 **Other investments**

This category covers treasury investments not listed above, for example unsecured corporate bonds and company loans. Non-bank companies cannot be bailed-in but can become insolvent placing the Council's investment at risk.

7.1.14 **Operational bank accounts**

The Council may incur operational exposures, for example though current accounts, collection accounts and merchant acquiring services, to any UK bank with credit ratings no lower than BBB- and with assets greater than £25 billion. These are not classed as investments but are still subject to the risk of a bank bail-in, and balances will therefore aimed to be kept below £1,000,000 per bank. The Bank of England has stated that in the event of failure, banks with assets greater than £25 billion are more likely to be bailed-in than made insolvent, increasing the chance of the Council maintaining operational continuity.

7.1.15 **Risk assessment and credit ratings**

Credit ratings are obtained and monitored by the Council's treasury advisers, who will notify changes in ratings as they occur. The credit rating agencies in current use are listed in the Treasury Management Practices document. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:

- no new investments will be made,
- any existing investments that can be recalled or sold at no cost will be, and
- full consideration will be given to the recall or sale of all other existing investments with the affected counterparty.

Where a credit rating agency announces that a credit rating is on review for possible downgrade (also known as “negative watch”) so that it may fall below the approved rating criteria, then only investments that can be withdrawn will be made with that organisation until the outcome of the review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.

7.1.16 **Other information on the security of investments**

The Council understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support, reports in the quality financial press and analysis and advice from the Council’s treasury management adviser. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may otherwise meet the above criteria.

When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2008 and 2020, this is not generally reflected in credit ratings, but can be seen in other market measures. In these circumstances, the Council will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the Council’s cash balances, then the surplus will be deposited with the UK Government, or with other local authorities. This will cause investment returns to fall but will protect the principal sum invested.

7.1.17 **Reputational aspects**

The Authority is aware that investment with certain counterparties, while considered secure from a purely financial perspective, may leave it open to criticism, valid or otherwise, that may affect its public reputation, and this risk will therefore be taken into account when making investment decisions.

7.1.17 **Investment limits**

The Council’s revenue reserves available to cover investment losses are forecast to be £10.5 million on 31st March 2024 and £5.8 million on 31st March 2025. In order that no more than 45% of available reserves will be put at risk in the case of a single default, the maximum that will be lent to any one organisation (other than the UK Government) will be £10 million. A group of entities under the same ownership will be treated as a single organisation for limit purposes.

Credit risk exposures arising from non-treasury investments and balances greater than £1,000,000 in operational bank accounts count against the relevant investment limits.

Limits are also placed on fund managers, investments in brokers’ nominee accounts and foreign countries as below. Investments in pooled funds and multilateral development banks do not count against the limit for any single foreign country, since the risk is diversified over many countries.

Additional investment limits

	Cash limit
Any group of pooled funds under the same management	£25 m per manager
Negotiable instruments held in a broker's nominee account	£25m per broker
Foreign countries	£10m per country

7.1.18 **Liquidity management**

The Council uses purpose-built cash flow forecasting software to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a prudent basis to minimise the risk of the Council being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Council's medium-term financial plan and cash flow forecast.

The Council will spread its liquid cash over at least two providers (e.g. bank accounts and money market funds) to ensure that access to cash is maintained in the event of operational difficulties at any one provider.

7.2 Ethical Investment Policy

7.2.1 The Council will not undertake direct investment or borrowing activities with organisations whose core activities include:

- Armaments – weapon systems
- Gambling
- Pornography
- Tobacco
- Pay-day loans
- Companies that generate more than 10% of their revenue from the extraction of coal, oil or gas.

7.2.2 In order to comply with treasury management guidance, the Council's investments will prioritise security, liquidity and yield in that order. The Ethical Investment Policy thereby becomes a fourth consideration in the decision making process.

7.2.3 The core activities in the Ethical Investment Policy have been chosen after careful consideration of the Policy direction of the administration, the officer time in implementing the policy, the cost of external resources, and the timeliness of investment decisions.

7.3 Non-treasury Investment strategy

7.3.1 The Council invests its money for three broad purposes:

- because it has surplus cash as a result of its day-to-day activities, for example when income is received in advance of expenditure (known as treasury management investments),
- to support local public services by lending to or buying shares in other organisations (service investments), and

- to earn investment income (known as commercial investments where this is the main purpose).

The statutory guidance defines investments as “all of the financial assets of a local authority as well as other non-financial assets that the organisation holds primarily or partially to generate a profit; for example, investment property portfolios.” The Council interprets this to exclude (a) trade receivables which meet the accounting definition of financial assets but are not investments in the everyday sense of the word and (b) property held partially to generate a profit but primarily for the provision of local public services. This aligns the Council’s definition of an investment with that in the CIPFA Prudential Code.

The Council typically receives its income in cash (e.g. from taxes and grants) before it pays for its expenditure in cash (e.g. through payroll and invoices). It also holds reserves for future expenditure and collects local taxes on behalf of other local authorities and central government. These activities, plus the timing of borrowing decisions, lead to a cash surplus which is invested in accordance with guidance from the Chartered Institute of Public Finance and Accountancy.

The contribution that these investments make to the objectives of the Council is to support effective treasury management activities.

7.3.2 Commercial Investments: Property

The Council has invested in local commercial property with the intention of making a profit that will be spent on local public services.

CURRENT INVESTMENT PROPERTIES

Investment property	Actual	31/03/2023 actual		31.03.2024
	Purchase cost £000	Gains or (losses) £000	Fair value £000	Forecast £000
Ashdown House	7,915	170	8,085	8,085
49-51 High Street	1,576	(431)	1,145	1,145
Atlantic House	4,633	(1,059)	3,574	3,574
The Create Building	29,582	(2,441)	27,141	27,141
Voluntary Organisations	1,033	220	1,253	1,253
Other	966	391	1,357	1,357
Total	**45,705**	**(3,150)**	**42,555**	**42,555**

7.3.3 **Security:** In accordance with government guidance, the Council considers a property investment to be secure if its accounting valuation, fair value, is at or higher than its purchase cost including taxes and transaction costs.

A fair value assessment of the Council’s investment property portfolio is undertaken annually. Where the fair value of an investment property is no longer sufficient to provide security against loss, the Council will consider mitigating actions to protect the capital invested.

7.3.4 **Risk assessment:** The Council does not intend to acquire any new investment properties in order to retain its access to PWLB loans. The Council may invest in its current portfolio subject to the investment securing best value for the asset.

A key aspect of the regulatory and professional guidance is that commercial activity is proportionate to the Council's other activity and in relation to the Council's overall financial position.

7.3.5 **Liquidity:** Compared with other investment types, property is relatively difficult to convert to cash at short notice.

7.3.6 **Investment Indicators**

The Council has set quantitative indicators to show the Council's total risk exposure as a result of its investment decisions.

7.3.7 **Total risk exposure**

The first indicator shows the Council's total exposure to potential investment losses. This includes amounts the Council is contractually committed to lend but have yet to be drawn down and guarantees the Council has issued over third party loans.

Total investment exposure	**31.03.2023 Actual £000**	**31.03.2024 Forecast £000**	**31.03.2025 Forecast £000**
Treasury management investments	98,025	51,175	16,419
Commercial investments: Property*	42,555	42,555	42,555
TOTAL INVESTMENTS	140,580	93,730	58,974
Commitments to lend	0	0	0
TOTAL EXPOSURE	140,580	93,730	58,974

7.3.8 **How investments are funded**

The Council does not normally associate particular assets with particular liabilities but funds its investments in total from usable reserves and income received in advance of expenditure. No investments are being funded by borrowing.

7.3.9 **Rate of return received**

This indicator shows the investment income received less the associated costs, including the cost of borrowing where appropriate, as a proportion of the sum initially invested.

Investment rate of return (net of all costs)

Investments net rate of return	**2022/23 Actual**	**2023/24 Forecast**	**2024/25 Forecast**
Treasury management investments	1.85%	4.84%	4.92%
Commercial investments: Property	1.12%	2.71%	3.39%
ALL INVESTMENTS	1.92%	4.16%	4.27%

8. Implications

8.1 The budget for investment income in 2024/25 is £2.856m (£1.878m General Fund; £0.978m HRA), based on an average investment portfolio of £58 million at an interest rate of 4.92%. The budget for debt interest to be paid in 2024/25 is £7.7 million, based on an average debt portfolio of £237.325 million at an average interest rate of 3.19%. These are forecasts and actual performance will be reported during 2024/25.

8.2 There are no significant legal implications as a result of the recommendations in this report. Compliance with the CIPFA Code of Practice for Treasury Management in the public services, the Local Government Investment Guidance provides that the council's investments are and will continue to be, within its legal powers conferred under the Local Government Act 2003.

9. Background Papers

Treasury Management Strategy for 2023/2024 – Cabinet, 1 February 2023 [report FIN/608 refers].
Treasury Management Mid-Year Review 2023/2024 – Cabinet, 29 November 2023 [report FIN/637 refers].
2024/2025 Budget and Council Tax – Cabinet, 31 January 2024 [report FIN/642 refers].
"Treasury Management in the Public Services – Code of Practice and Cross-Sectoral Guidance Notes", 2021 Edition – Chartered Institute of Public Finance and Accountancy.
"The Prudential Code for Capital Finance in Local Authorities", 2021 Edition – Chartered Institute of Public Finance and Accountancy.

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APPENDIX 1

Interest Rate Forecasts December 2023

Underlying assumptions:

- UK inflation and wage growth remain elevated but have eased over the past two months fuelling rate cuts expectations. Near-term rate cuts remain unlikely, although downside risks will increase as the UK economy likely slides into recession.
- The MPC's message remains unchanged as the Committee seeks to maintain tighter financial conditions. Monetary policy will remain tight as inflation is expected to moderate to target slowly, although some wage and inflation measures are below the Bank's last forecasts.
- Despite some deterioration in activity data, the UK economy remains resilient in the face of tighter monetary policy. Recent data has been soft but mixed; the more timely PMI figures suggest that the services sector is recovering from a weak Q3. Tighter policy will however bear down on domestic and external activity as interest rates bite.
- Employment demand is easing. Anecdotal evidence suggests slowing recruitment and pay growth, and we expect unemployment to rise further. As unemployment rises and interest rates remain high, consumer sentiment will deteriorate. Household and business spending will therefore be weak.
- Inflation will fall over the next 12 months. The path to the target will not be smooth, with higher energy prices and base effects interrupting the downtrend at times. The MPC's attention will remain on underlying inflation measures and wage data. We believe policy rates will remain at the peak for another 10 months, or until the MPC is comfortable the risk of further 'second-round' effects has diminished.
- Maintaining monetary policy in restrictive territory for so long, when the economy is already struggling, will require significant loosening in the future to boost activity.
- Global bond yields will remain volatile. Markets are currently running with expectations of near-term US rate cuts, fuelled somewhat unexpectedly by US policymakers themselves. Term premia and bond yields have experienced a marked decline. It would not be a surprise to see a reversal if data points do not support the narrative, but the current 10-year yield appears broadly reflective of a lower medium- term level for Bank Rate.

Forecast:

- The MPC held Bank Rate at 5.25% in December. We believe this is the peak for Bank Rate.
- The MPC will cut rates in the medium term to stimulate the UK economy but will be reluctant to do so until it is sure there will be no lingering second-round effects. We see rate cuts from Q3 2024 to a low of around 3% by early-mid 2026.
- The immediate risks around Bank Rate have become more balanced, due to the weakening UK economy and dampening effects on inflation. This shifts to the downside in the short term as the economy weakens.
- Long-term gilt yields are now substantially lower. Arlingclose expects yields to be flat from here over the short-term reflecting medium term Bank Rate forecasts. Periodic volatility is likely.

APPENDIX 2

Economic Background

The impact on the UK from higher interest rates and inflation, a weakening economic outlook, together with war in Ukraine and the Middle East, will be major influences on the Authority's treasury management strategy for 2024/25.

The Bank of England (BoE) increased Bank Rate to 5.25% in August 2023, before maintaining this level for the rest of 2023. In December 2023, members of the BoE's Monetary Policy Committee voted 6-3 in favour of keeping Bank Rate at 5.25%. The three dissenters wanted to increase rates by another 0.25%.

The November quarterly Monetary Policy Report (MPR) forecast a prolonged period of weak Gross Domestic Product (GDP) growth with the potential for a mild contraction due to ongoing weak economic activity. The outlook for CPI inflation was deemed to be highly uncertain, with upside risks to CPI falling to the 2% target coming from potential energy price increases, strong domestic wage growth and persistence in price-setting.

Office for National Statistics (ONS) figures showed CPI inflation was 3.9% in November 2023, down from a 4.6% rate in the previous month and, in line with the recent trend, lower than expected. The core CPI inflation rate declined to 5.1% from the previous month's 5.7%, again lower than predictions. Looking ahead, using the interest rate path implied by financial markets the BoE expects CPI inflation to continue falling slowly, but taking until early 2025 to reach the 2% target before dropping below target during the second half 2025 and into 2026.

ONS figures showed the UK economy contracted by 0.1% between July and September 2023. The BoE forecasts GDP will likely stagnate through 2024. The BoE forecasts that higher interest rates will constrain GDP growth, which will remain weak over the entire forecast horizon.

The labour market appears to be loosening, but only very slowly. The unemployment rate rose slightly to 4.2% between June and August 2023, from 4.0% in the previous 3-month period, but the lack of consistency in the data between the two periods made comparisons difficult. Earnings growth has remained strong, but has showed some signs of easing; regular pay (excluding bonuses) was up 7.3% over the period and total pay (including bonuses) up 7.2%. Adjusted for inflation, regular pay was 1.4% and total pay 1.3%. Looking forward, the MPR showed the unemployment rate is expected to be around 4.25% in the second half of calendar 2023, but then rising steadily over the forecast horizon to around 5% in late 2025/early 2026.

Having increased its key interest rate to a target range of 5.25-5.50% in August 2023, the US Federal Reserve appears now to have concluded the hiking cycle. It is likely this level represents the peak in US rates following a more dovish meeting outcome in December 2023. US GDP grew at an annualised rate of 4.9% between July and September 2023, ahead of expectations for a 4.3% expansion and the 2.1% reading for Q2. But the impact from higher rates has started to feed into economic activity and growth will weaken in 2024. Annual CPI inflation was 3.1% in November.

Eurozone inflation has declined steadily since the start of 2023, falling to an annual rate of 2.4% in November 2023. Economic growth has been weak and GDP contracted by 0.1% in the three months to September 2023. In line with other central banks, the European Central Bank has increased rates, taking its deposit facility, fixed rate tender, and marginal lending rates to 3.75%, 4.25% and 4.50% respectively..

Credit outlook

Credit Default Swap (CDS) prices were volatile during 2023, spiking in March on the back of banking sector contagion concerns following the major events of Silicon Valley Bank becoming insolvent and the takeover of Credit Suisse by UBS. After then falling back in Q2 of calendar 2023, in the second half of the year, higher interest rates and inflation, the ongoing war in Ukraine, and now the Middle East, have led to CDS prices increasing steadily.

On an annual basis, CDS price volatility has so far been lower in 2023 compared to 2022, but this year has seen more of a divergence in prices between ringfenced (retail) and non-ringfenced (investment) banking entities once again.

Moody's revised its outlook on the UK sovereign to stable from negative to reflect its view of restored political predictability following the volatility after the 2022 mini-budget. Moody's also affirmed the Aa3 rating in recognition of the UK's economic resilience and strong institutional framework.

Following its rating action on the UK sovereign, Moody's revised the outlook on five UK banks to stable from negative and then followed this by the same action on five rated local authorities. However, within the same update the long-term ratings of those five local authorities were downgraded.

There remain competing tensions in the banking sector, on one side from higher interest rates boosting net income and profitability against another of a weakening economic outlook and likely recessions that increase the possibility of a deterioration in the quality of banks' assets.

However, the institutions on our adviser Arlingclose's counterparty list remain well-capitalised and their counterparty advice on both recommended institutions and maximum duration remain under constant review and will continue to reflect economic conditions and the credit outlook.

APPENDIX 3

Treasury Management Scheme of Delegation

(i) Full Council

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

(ii) Cabinet

- 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) Overview and Scrutiny Commission

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

APPENDIX 4

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.
- 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 Council has appropriate legal powers to undertake expenditure on non-financial assets and their financing
- ensuring the proportionality of all investments so that the Council 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 Council 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.*