

**Treasury Management Strategy  
Statement**

Minimum Revenue Provision Policy Statement  
and Annual Investment Strategy

2024/25

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## INDEX

1.1	Background .....	3
1.2	Reporting Requirements .....	3
1.3	Treasury Management Strategy for 2024/25 .....	5
1.4	Training.....	5
1.5	Treasury Management Consultants .....	6
2.	<b>THE CAPITAL PRUDENTIAL INDICATORS 2024/25 – 2026/27 .....</b>	<b>7</b>
2.1	Capital Expenditure and Financing .....	7
2.2	The Authority’s Borrowing Need (the Capital Financing Requirement).....	7
2.3	Liability Benchmark.....	8
2.4	Core Funds and Expected Investment Balances .....	9
2.5	Minimum Revenue Provision (MRP) Policy Statement .....	10
3.	<b>BORROWING .....</b>	<b>12</b>
3.1	Current Portfolio Position .....	12
3.2	Treasury Indicators: Limits to Borrowing Activity.....	13
3.3	Prospects for Interest Rates .....	16
3.4	Borrowing Strategy .....	19
3.5	Policy on Borrowing in Advance of Need.....	19
3.6	Rescheduling.....	19
3.7	New Financial Institutions as a Source of Borrowing and / or Types of Borrowing (if applicable).....	20
3.8	Approved Sources of Long and Short-term Borrowing.....	20
4	<b>ANNUAL INVESTMENT STRATEGY.....</b>	<b>21</b>
4.1	Investment Policy – Management of Risk .....	21
4.2	Creditworthiness Policy .....	23
4.3	Limits .....	Error! Bookmark not defined.
4.4	Investment Strategy .....	25
4.5	Investment Performance / Risk Benchmarking .....	26
4.6	End of Year Investment Report .....	27
4.7	External Fund Managers .....	27
5	<b>APPENDICES .....</b>	<b>28</b>
5.1	<b>THE CAPITAL PRUDENTIAL AND TREASURY INDICATORS 2024/25 – 2026/27 ...</b>	<b>29</b>
5.2	<b>INTEREST RATE FORECASTS 2023-2026 .....</b>	<b>30</b>
5.3	<b>ECONOMIC BACKGROUND .....</b>	<b>31</b>
5.4	<b>TREASURY MANAGEMENT PRACTICE (TMP1) – CREDIT AND COUNTERPARTY RISK MANAGEMENT OPTION 1 .....</b>	<b>36</b>
5.5	<b>TREASURY MANAGEMENT PRACTICE (TMP1) – CREDIT AND COUNTERPARTY RISK MANAGEMENT OPTION 2 .....</b>	<b>Error! Bookmark not defined.</b>
5.6	<b>APPROVED COUNTRIES FOR INVESTMENTS .....</b>	<b>38</b>
5.7	<b>TREASURY MANAGEMENT SCHEME OF DELEGATION.....</b>	<b>39</b>
5.8	<b>THE TREASURY MANAGEMENT ROLE OF THE SECTION 151 OFFICER .....</b>	<b>40</b>

## 1.1 Background

The Authority is required to operate a balanced revenue budget, 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 Authority'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 Authority's capital plans. These capital plans provide a guide to the borrowing need of the Authority, essentially the longer-term cash flow planning, to ensure that it 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 risk or cost objectives.

The contribution the treasury management function makes to the Authority is critical, as the balance of debt and investment operations ensure liquidity or the ability to meet spending commitments as they fall due, either on day-to-day revenue or for larger capital projects. The treasury operations will see a balance of the interest costs of debt and the investment income arising from cash deposits affecting the available budget. Since cash balances generally result from reserves and balances, it is paramount to ensure adequate security of the sums invested, as a loss of principal will in effect result in a loss to the General Fund Balance.

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.”*

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 strategy is to ensure that all the Authority's elected members fully understand the overall long-term policy objectives and resulting Capital Strategy requirements, governance procedures and risk appetite.

### 1.2.2 Treasury Management Reporting

The Authority 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 Annual Investment Strategy, (the parameters on how 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. In addition, this Authority will receive quarterly update reports.
  
- 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.

#### Scrutiny

The above reports are required to be adequately scrutinised before being recommended to the Full Council. This role is undertaken by the Cabinet.

**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 but do require to be adequately scrutinised. This role is undertaken by the Cabinet. (The reports, specifically, should comprise updated Treasury/Prudential Indicators.)

### **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 Authority
- 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, DLUHC Investment Guidance, DLUHC MRP Guidance, the CIPFA Prudential Code and the CIPFA Treasury Management Code.

### **1.4 Training**

The CIPFA Treasury Management Code requires the responsible officer to ensure that members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsible for scrutiny.

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

The scale and nature of this will depend on the size and complexity of the organisation’s treasury management needs. Organisations should consider how to assess whether treasury management staff and board/ council members have the required knowledge and skills to undertake their roles and whether they have been able to maintain those skills and keep them up to date.

As a minimum, authorities should carry out the following to monitor and review knowledge and skills:

- Record attendance at training and ensure action is taken where poor attendance is identified.
- Prepare tailored learning plans for treasury management officers and board/council members.
- Require treasury management officers and board/council members to undertake self-assessment against the required competencies (as set out in the schedule that may be adopted by the organisation).
- Have regular communication with officers and board/council members, encouraging them to highlight training needs on an ongoing basis.”

In further support of the revised training requirements, CIPFA's Better Governance Forum and Treasury Management Network have produced a 'self-assessment by members responsible for the scrutiny of treasury management', which is available from the CIPFA website to download.

In November 2023 the Council's Treasury Consultants provided training to all Members

The training needs of treasury management officers are periodically reviewed with officers regularly attending seminars and conferences to keep informed of current issues and new starters receiving introductory training as required.

During the year treasury officers have attended LINK's treasury management training sessions to keep up to date with latest developments and regulations.

### **1.5 Treasury Management Consultants**

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

The Authority recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon 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 Authority will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented and subjected to regular review.

## 2. THE CAPITAL PRUDENTIAL INDICATORS 2024/25 – 2026/27

The Authority'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 are prudent, affordable and sustainable.

### 2.1 Capital Expenditure and Financing

This prudential indicator is a summary of the Authority's capital expenditure plans, both those agreed previously, and those forming part of this budget cycle. Members are asked to approve the capital expenditure forecasts: -

Capital expenditure £'000	2022/23 Actual	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate
Great Council	132	179	210	0	0
People	66	15	2,909	345	345
Place	667	15,395	237	398	50
<b>Total General Expenses</b>	<b>865</b>	<b>15,589</b>	<b>3,356</b>	<b>743</b>	<b>395</b>
Special	0	0	10	0	0
HRA	3,888	5,514	3,805	4,268	2,935
<b>Total</b>	<b>4,753</b>	<b>21,103</b>	<b>7,171</b>	<b>5,011</b>	<b>3,330</b>

Other long-term liabilities - the above financing need excludes other long-term liabilities, such as PFI and leasing arrangements that already include borrowing instruments.

The table below 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.

Financing of capital expenditure £'000	2022/23 Actual	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate
Capital receipts	1,316	3,514	1,143	530	350
Capital grants	827	13,874	2,909	345	345
Reserves	12	1,167	858	0	0
Repairs & Renewals Fund	132	399	92	162	0
Third party contributions	523	376	0	0	0
Revenue	1,943	1,773	2,169	3,974	2,635
<b>Net financing need for the year</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>

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

The second prudential indicator is the Authority'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 Authority'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). Whilst these increase the CFR, and therefore the Authority's borrowing requirement, these types of schemes include a borrowing facility by the PFI, PPP lease provider and so the Authority is not required to separately borrow for these schemes. The Authority currently has £43k of such schemes within the CFR.

The Authority is asked to approve the CFR projections below:

£'000	2022/23 Actual	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate
<b>Capital Financing Requirement</b>					
Non-HRA	54	43	32	21	10
Housing	31,484	31,484	31,484	31,484	31,484
<b>Total CFR</b>	<b>31,538</b>	<b>31,527</b>	<b>31,516</b>	<b>31,505</b>	<b>31,494</b>
<b>Movement in CFR</b>	<b>-12</b>	<b>-11</b>	<b>-11</b>	<b>-11</b>	<b>-11</b>

<b>Movement in CFR represented by</b>					
Net financing need for the year (above)	0	0	0	0	0
Less MRP/VRP and other financing movements	-11	-11	-11	-11	-11
<b>Movement in CFR</b>	<b>-11</b>	<b>-11</b>	<b>-11</b>	<b>-11</b>	<b>-11</b>

### 2.3 Liability Benchmark

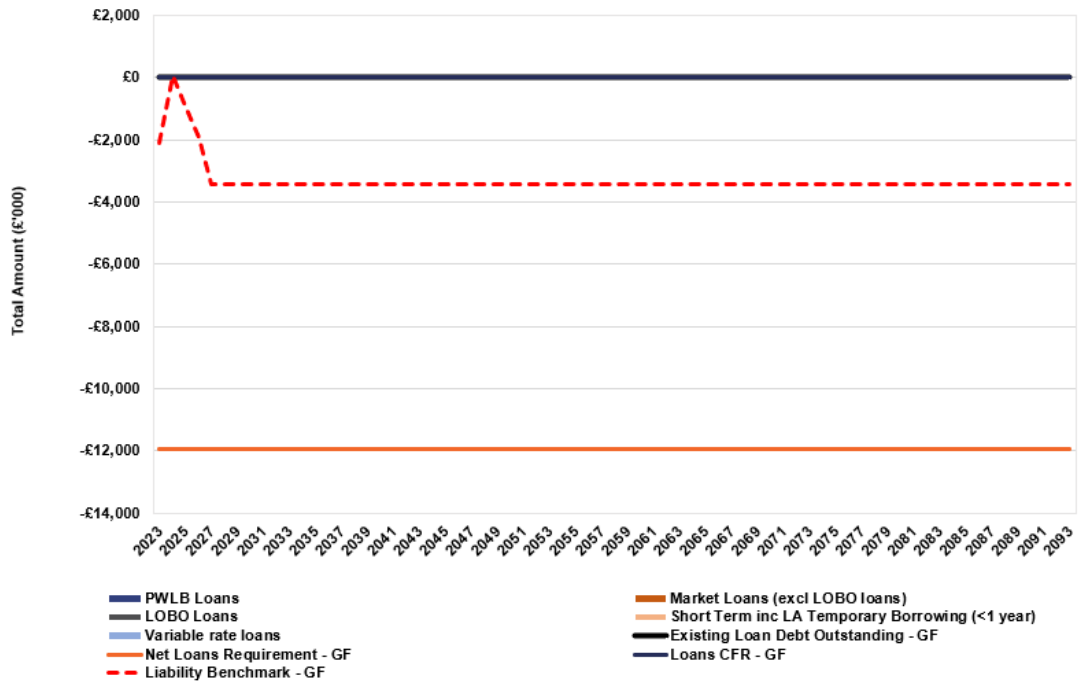
The Authority is required to estimate and measure the Liability Benchmark (LB) for the forthcoming financial year and the following two financial years, as a minimum.

There are four components to the LB: -

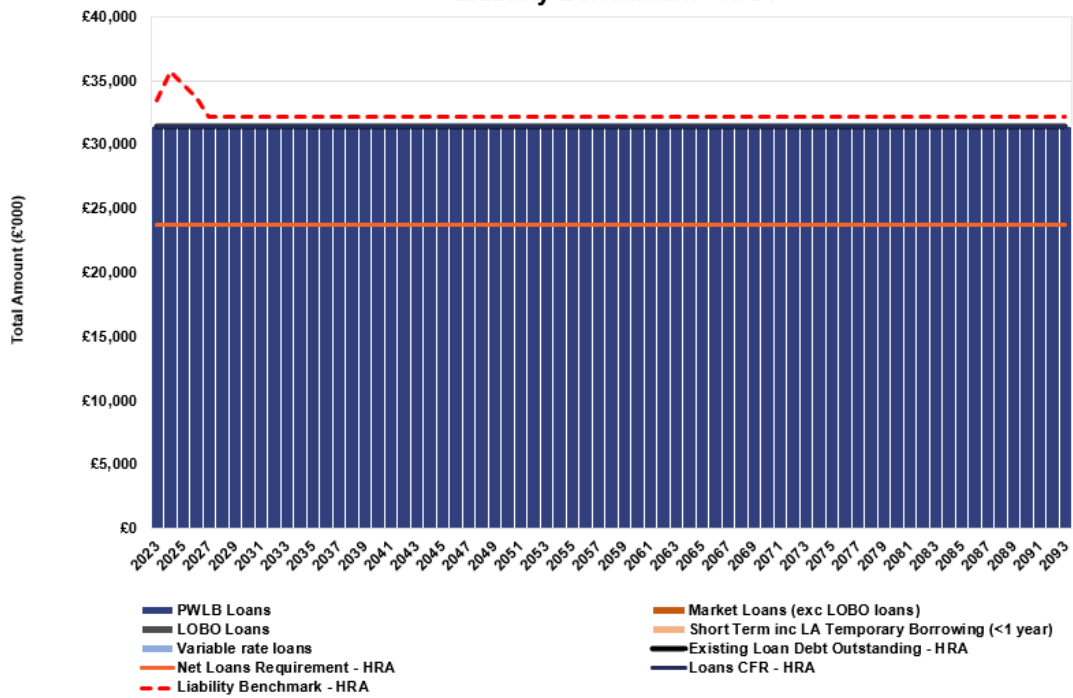
1. **Existing loan debt outstanding:** the Authority's existing loans that are still outstanding in future years.
2. **Loans CFR:** this is calculated in accordance with the loans CFR definition in the Prudential Code and projected into the future based on approved prudential borrowing and planned MRP.
3. **Net loans requirement:** this will show the Authority's gross loan debt less treasury management investments at the last financial year-end, projected into the future and based on its approved prudential borrowing, planned MRP and any other major cash flows forecast.
4. **Liability benchmark (or gross loans requirement):** this equals net loans requirement plus short-term liquidity allowance.



### Liability Benchmark - General Fund



### Liability Benchmark - HRA



## 2.4 Core Funds and Expected Investment Balances

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

<b>Year End Resources £'000</b>	<b>2022/23 Actual</b>	<b>2023/24 Estimate</b>	<b>2024/25 Estimate</b>	<b>2025/26 Estimate</b>	<b>2026/27 Estimate</b>
Fund balances / reserves	14,405	11,873	9,810	9,018	7,918
Capital receipts	4,279	2,811	1,842	1,312	962
Provisions	317	317	317	317	317
<b>Total core funds</b>	<b>19,001</b>	<b>15,001</b>	<b>11,969</b>	<b>10,647</b>	<b>9,197</b>
Working capital*	<b>548</b>	<b>8,928</b>	<b>9,960</b>	<b>9,282</b>	<b>7,732</b>
Under/over borrowing**	71	71	71	71	71
<b>Expected investments</b>	<b>19,620</b>	<b>24,000</b>	<b>22,000</b>	<b>20,000</b>	<b>17,000</b>

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

## 2.5 Minimum Revenue Provision (MRP) Policy Statement

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

The Authority is required to calculate a prudent provision of MRP which ensures that the outstanding debt liability is repaid over a period that is reasonably commensurate with that over which the capital expenditure provides benefits. The MRP Guidance (2018) gives four ready-made options for calculating MRP, but the Authority can use any other reasonable basis that it can justify as prudent.

The MRP policy statement requires full Council approval (or closest equivalent level) in advance of each financial year.

The Authority is recommended to approve the following MRP Statement

From 1 April 2008 for all unsupported borrowing the MRP policy will be:

- **Asset life method (straight line)** – MRP will be based on the estimated life of the assets;

Capital expenditure incurred during 2023/24 will not be subject to an MRP charge until 2024/25, or in the year after the asset becomes operational

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

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.

MRP in respect of assets acquired under Finance Leases or PFI will be charged at an amount equal to the principal element of the annual repayment.

For capital expenditure on loans to third parties 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.

**MRP Overpayments** - Under the MRP guidance, any charges made in excess of the statutory MRP can be made, known as voluntary revenue provision (VRP).

VRP can be reclaimed in later years if deemed necessary or prudent. In order for these amounts to be reclaimed for use in the budget, this policy must disclose the cumulative overpayment made each year. The Council has not made any VRP overpayments to date.

### 3. BORROWING

The capital expenditure plans set out in Section 2 provide details of the service activity of the Authority. The treasury management function ensures that the Authority's cash is organised in accordance with the relevant professional codes, so that sufficient cash is available to meet this service activity and the Authority'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 31.3.23 and for the position as at 31.12.23 are shown below for both borrowing and investments.

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

<b>TREASURY PORTFOLIO</b>				
	<b>actual</b>	<b>actual</b>	<b>current</b>	<b>current</b>
	<b>31.3.23</b>	<b>31.3.23</b>	<b>31.12.23</b>	<b>31.12.23</b>
	<b>£000</b>	<b>%</b>	<b>£000</b>	<b>%</b>
<b>Treasury investments</b>				
banks	15,500	79%	20,000	71%
money market funds	2,120	11%	6,100	22%
<b>Total managed in house</b>	<b>17,620</b>	<b>90%</b>	<b>26,100</b>	<b>93%</b>
property funds	2,000	10%	2,000	7%
<b>Total managed externally</b>	<b>2,000</b>	<b>10%</b>	<b>2,000</b>	<b>7%</b>
<b>Total treasury investments</b>	<b>19,620</b>	<b>100%</b>	<b>28,100</b>	<b>100%</b>
<b>Treasury external borrowing</b>				
PWLB	31,413	100%	31,413	100%
<b>Total external borrowing</b>	<b>31,413</b>	<b>100%</b>	<b>31,413</b>	<b>100%</b>
<b>Net treasury investments / (borrowing)</b>	<b>-11,793</b>	<b>0</b>	<b>-3,313</b>	<b>0</b>

£'000	2022/23 Actual	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate
<b>External Debt</b>					
Debt at 1 April	31,413	31,413	31,413	31,413	31,413
Expected change in Debt	0	0	0	0	0
Other long-term liabilities (OLTL)	66	54	43	32	21
Expected change in OLTL	-11	-11	-11	-11	-11
<b>Actual gross debt at 31 March</b>	<b>31,468</b>	<b>31,456</b>	<b>31,445</b>	<b>31,434</b>	<b>31,423</b>
<b>The Capital Financing Requirement</b>	<b>31,539</b>	<b>31,527</b>	<b>31,516</b>	<b>31,505</b>	<b>31,494</b>
<b>Under / (over) borrowing</b>	<b>71</b>	<b>71</b>	<b>71</b>	<b>71</b>	<b>71</b>

Within the range of prudential indicators there are several key indicators to ensure that the Authority operates its activities within well-defined limits. One of these is that the Authority 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 Director of Corporate Services reports that the Authority complied with this prudential indicator in the current year and does not envisage difficulties for the future. This view takes account of current commitments, existing plans and the proposals in this budget report.

### 3.2 Treasury Indicators: Limits to Borrowing Activity

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

Operational Boundary £'000	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate
Debt	31,413	31,413	31,413	31,413
Other long-term liabilities	43	32	21	10
Headroom	2,544	2,555	2,566	2,577
Total	34,000	34,000	34,000	34,000

**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.

- 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 local authority plans, or those of a specific authority, although this power has not yet been exercised.

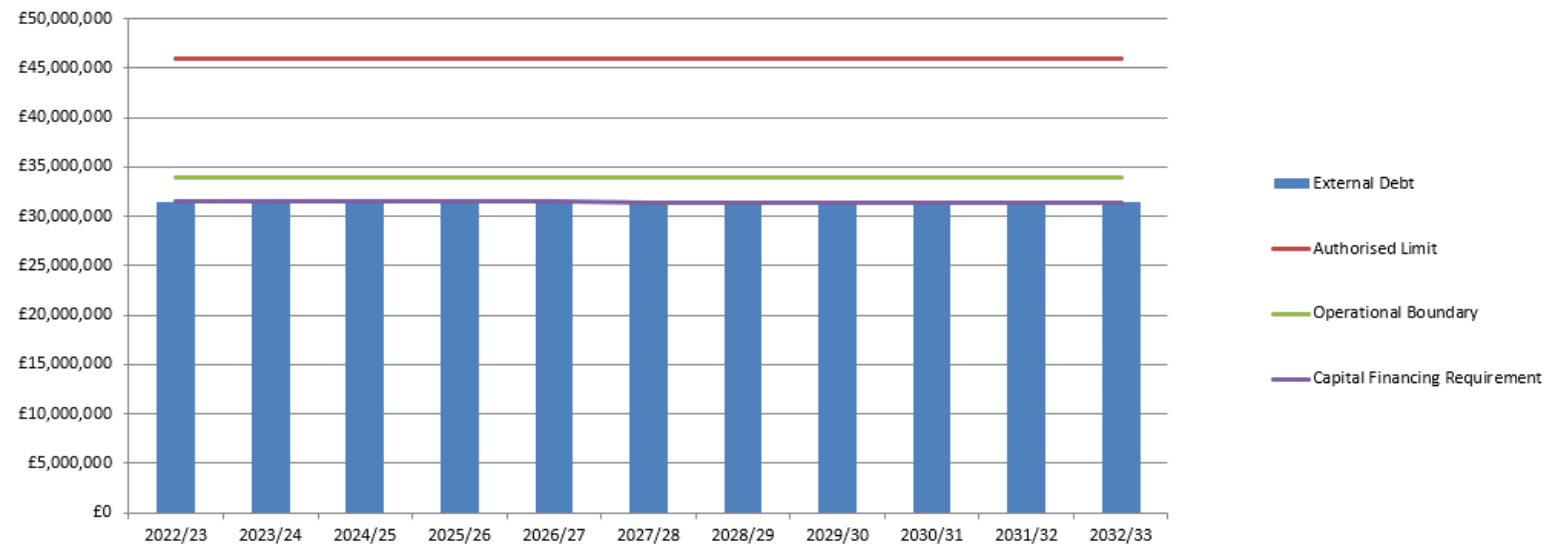
- The Authority is asked to approve the following Authorised Limit:

<b>Authorised Limit £'000</b>	<b>2023/24 Estimate</b>	<b>2024/25 Estimate</b>	<b>2025/26 Estimate</b>	<b>2026/27 Estimate</b>
Debt	45,960	45,970	45,980	45,990
Other long-term liabilities	40	30	20	10
<b>Total</b>	<b>46,000</b>	<b>46,000</b>	<b>46,000</b>	<b>46,000</b>

The table and graph below provides a summary of information above

The table and graph below provides a summary of information above in sections 2 and 3

<b>CAPITAL FINANCING REQUIREMENTS</b>											
	Actual 2022/23	Estimated 2023/24	Estimated 2024/25	Estimated 2025/26	Estimated 2026/27	Estimated 2027/28	Estimated 2028/29	Estimated 2029/30	Estimated 2030/31	Estimated 2031/32	Estimated 2032/33
<b>CFR (including PFI and finance leases)</b>											
HRACFR	£31,484,000	£31,484,000	£31,484,000	£31,484,000	£31,484,000	£31,484,000	£31,484,000	£31,484,000	£31,484,000	£31,484,000	£31,484,000
GFCFR	£55,000	£43,000	£32,000	£21,000	£10,000	£0	£0	£0	£0	£0	£0
<b>Capital Financing Requirement</b>	<b>£31,539,000</b>	<b>£31,527,000</b>	<b>£31,516,000</b>	<b>£31,505,000</b>	<b>£31,494,000</b>	<b>£31,484,000</b>	<b>£31,484,000</b>	<b>£31,484,000</b>	<b>£31,484,000</b>	<b>£31,484,000</b>	<b>£31,484,000</b>
<b>External Borrowing</b>	<b>£31,413,000</b>	<b>£31,413,000</b>	<b>£31,413,000</b>	<b>£31,413,000</b>	<b>£31,413,000</b>	<b>£31,413,000</b>	<b>£31,413,000</b>	<b>£31,413,000</b>	<b>£31,413,000</b>	<b>£31,413,000</b>	<b>£31,413,000</b>
Deferred Liabilities	£55,000	£43,000	£32,000	£21,000	£10,000	£0	£0	£0	£0	£0	£0
<b>External Debt</b>	<b>£31,468,000</b>	<b>£31,456,000</b>	<b>£31,445,000</b>	<b>£31,434,000</b>	<b>£31,423,000</b>	<b>£31,413,000</b>	<b>£31,413,000</b>	<b>£31,413,000</b>	<b>£31,413,000</b>	<b>£31,413,000</b>	<b>£31,413,000</b>
Authorised Limit	£46,000,000	£46,000,000	£46,000,000	£46,000,000	£46,000,000	£46,000,000	£46,000,000	£46,000,000	£46,000,000	£46,000,000	£46,000,000
Operational Boundary	£34,000,000	£34,000,000	£34,000,000	£34,000,000	£34,000,000	£34,000,000	£34,000,000	£34,000,000	£34,000,000	£34,000,000	£34,000,000



### 3.3 Prospects for Interest Rates

The Authority has appointed Link Group as its treasury advisor and part of their service is to assist the Authority to formulate a view on interest rates. Link provided the following forecasts on 08 January 2024. These are forecasts for Bank Rate, average earnings and PWLB certainty rates, gilt yields plus 80 bps.

Link Group Interest Rate View 08.01.24													
	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
<b>BANK RATE</b>	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

*Additional notes by Link on this forecast table: -*

- Our central forecast for interest rates was previously updated on 7 November and reflected a view that the MPC would be keen to further demonstrate its anti-inflation credentials by keeping Bank Rate at 5.25% until at least 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 c70 basis points 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.

### Downside risks to current forecasts for UK gilt yields and PWLB rates include: -

- **Labour and supply shortages** prove more enduring and disruptive and depress economic activity (accepting that in the near-term this is also an upside risk to inflation and, thus, could keep gilt yields high for longer).
- **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.

### Upside risks to current forecasts for UK gilt yields and PWLB rates: -

- Despite the tightening 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 QT**, could be too much for the markets to comfortably digest without higher yields compensating.

## LINK GROUP FORECASTS

We expect the MPC will keep Bank Rate at 5.25% until the second half of 2024, to combat on-going inflationary and wage pressures, even if they have dampened somewhat of late. We do not think that the MPC will increase Bank Rate above 5.25%.

### Gilt yields and PWLB rates

The overall longer-run trend is for gilt yields and PWLB rates to fall back over the timeline of our forecasts, as inflation continues to fall through 2024.

Our target borrowing rates are set **two years forward** (as we expect rates to fall back) and the current PWLB (certainty) borrowing rates are set out below: -

PWLB debt	Current borrowing rate as at 08.01.24 p.m.	Target borrowing rate now (end of Q4 2025)	Target borrowing rate previous (end of Q3 2025)
5 years	4.53%	3.70%	3.80%
10 years	4.67%	3.90%	3.80%
25 years	5.19%	4.20%	4.20%
50 years	4.97%	4.00%	4.00%

**Borrowing advice:** Our long-term (beyond 10 years) forecast for Bank Rate remains at 3% and reflects Capital Economics' research that suggests AI and general improvements in productivity will be supportive of a higher neutral interest rate. As all PWLB certainty rates are currently 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. 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.

Our suggested budgeted earnings rates for investments up to about three months' duration in each financial year are set out below.

Average earnings in each year	Now	Previously
2023/24 (residual)	5.30%	5.30%
2024/25	4.55%	4.70%
2025/26	3.10%	3.20%
2026/27	3.00%	3.00%
2027/28	3.25%	3.25%
2028/29	3.25%	3.25%
Years 6 to 10	3.25%	3.25%
Years 10+	3.25%	3.25%

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

Our interest rate forecast for Bank Rate is in steps of 25 bps, whereas PWLB forecasts have been rounded to the nearest 10 bps and are central forecasts within bands of + / - 25 bps. Naturally, we continue to monitor events and will update our forecasts as and when appropriate.

### **3.4 Borrowing Strategy**

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

Against this background and the risks within the economic forecast, caution will be adopted with the 2024/25 treasury operations. The Director of Corporate Services 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, fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.*

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

The Council would only borrow to fund capital investment which has a clearly defined business case and rational with associated repayment and MRP provision calculated. The Council's preference would be to use PWLB. We do not envisage any borrowing requirement and can use internal resources for 2024/25 where required.

### **3.5 Policy on Borrowing in Advance of Need**

The Authority 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 Authority can ensure the security of such funds.

### **3.6 Rescheduling**

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

If rescheduling is to be undertaken, it will be reported to the Cabinet, at the earliest meeting following its action.

### 3.7 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. 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 – generally 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).

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

### 3.8 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 - this was formerly the Ministry of Housing, Communities and Local Government (MHCLG)) 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 and service investments, are covered in the Capital Strategy, (a separate report).

The Authority’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 Authority’s investment priorities will be security first, portfolio liquidity second and then yield (return). The Authority will aim to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity and with regard to the Authority’s risk appetite.

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

The above guidance from the DLUHC and CIPFA 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 Authority 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 Authority has defined the list of **types of investment instruments** that the treasury management team are authorised to use. There are two lists in Appendix 5.4 under the categories of 'specified' and 'non-specified' investments.

**Specified investments** are those with a high level of credit quality and subject to a maturity limit of one year or have less than a year left to run to maturity, if originally they were classified as being non-specified investments solely due to the maturity period exceeding one year.

**Non-specified investments** are those with less high credit quality, may be for periods in excess of one year, and/or 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 Authority 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 £10m.
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 Authority 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 Authority has engaged **external consultants**, (see paragraph 1.5), to provide expert advice on how to optimise an appropriate balance of security, liquidity and yield, given the risk appetite of this Authority in the context of the expected level of cash balances and need for liquidity throughout the year.
11. All investments will be denominated in **sterling**.
12. As a result of the change in accounting standards for 2023/24 under IFRS 9, this Authority will consider the implications of investment instruments which could result in an adverse movement in the value of the amount invested and resultant charges at the end of the year to the General Fund. (In November 2018, the MHCLG, concluded a consultation for a temporary override to allow English local authorities time to adjust their portfolio of all pooled investments by announcing a statutory override to delay implementation of IFRS 9 for five years ending

31.3.23. More recently, a further extension to the over-ride to 31.3.25 has been agreed by Government.

However, this Authority 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**

This Authority applies the creditworthiness service provided by the Link Group. However we take the approach that where there is colour banding we are comfortable that we can invest up to one year in duration due to the low risk profile and maximising returns. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies - Fitch, Moody's and Standard & Poor's. The credit ratings of counterparties are supplemented with the following overlays: -

1. "watches" and "outlooks" from credit rating agencies;
2. CDS spreads that may give early warning of changes in credit ratings;
3. sovereign ratings to select counterparties from only the most creditworthy countries.

This modelling approach combines credit ratings, and any assigned Watches and Outlooks, in a weighted scoring system which is then combined with an overlay of CDS spreads. The end-product of this is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Authority to determine the suggested duration for investments. The Authority will, therefore, use counterparties within the following durational bands:

- Yellow 5 years \*
- Dark pink 5 years for Ultra-Short Dated Bond Funds with a credit score of 1.25
- Light pink 5 years for Ultra-Short Dated Bond Funds with a credit score of 1.5
- Purple 2 years
- Blue 1 year (only applies to nationalised or semi nationalised UK Banks)
- Orange 1 year
- Red 6 months
- Green 100 days
- No colour not to be used

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

Typically, the minimum credit ratings criteria the Authority uses will be a short-term rating (Fitch or equivalents) of F1 and a long-term rating of A-. There may be

occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances, consideration will be given to the whole range of ratings available, or other topical market information, to support their use.

All credit ratings will be monitored on a regular basis. The Authority is alerted to changes to ratings of all three agencies through its use of the Link creditworthiness service.

- if a downgrade results in the counterparty / investment scheme no longer meeting the Authority's minimum criteria, its further use as a new investment will be withdrawn immediately.
- in addition to the use of credit ratings the Authority will be advised of information in movements in Credit Default Swap spreads against the iTraxx European Senior Financials benchmark and other market data on a daily basis via its Passport website, provided exclusively to it by Link. Extreme market movements may result in downgrade of an institution or removal from the Authority's lending list.

Sole reliance will not be placed on the use of this external service. In addition, this Authority will also use market data and market information, as well as information on any external support for banks to help support its decision-making process.

Y	Pi1	Pi2	P	B	O	R	G	N/C
1	1.25	1.5	2	3	4	5	6	7
Up to 5yrs	Up to 5yrs	Up to 5yrs	Up to 2yrs	Up to 1yr	Up to 1yr	Up to 6mths	Up to 100days	No Colour

At Melton we have taken the decision to apply the approach where an institution with any colour coding from blue or orange (up to 1year) to green (up to 100 days) can be used for fixed term investments for up to 1 year in duration.

### **Creditworthiness.**

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

### **CDS prices**

Although bank CDS prices, (these are market indicators of credit risk), spiked upwards during the days of the Truss/Kwarteng government in the autumn of 2022, 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 Authority has access to this information via its Link-provided Passport portal.



## Limits

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

- a. **Non-specified treasury management investment limit.** The Authority has determined that it will limit the maximum total exposure of treasury management investments to non-specified treasury management investments as being 25% of the total treasury management investment portfolio.
- b. **Country limit.** The Authority has determined that it will only use approved counterparties from the UK and from countries with a **minimum sovereign credit rating of AA-** from Fitch (or equivalent). The list of countries that qualify using this credit criteria as at the date of this report are shown in Appendix 5.6. This list will be added to, or deducted from, by officers should ratings change in accordance with this policy.

**Other limits.** In addition: -

- no more than 50% will be placed with any one country outside of the UK at any time;
- limits in place above will apply to a group of companies/institutions;
- sector limits will be monitored regularly for appropriateness.

## 4.3 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. The current shape of the yield curve suggests that is the case at present, but there is the prospect of Bank Rate having peaked in the second half of 2023 and possibly reducing as early as the second half of 2024 so an agile investment strategy would be appropriate to optimise returns.

Accordingly, 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.

### **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: -

Average earnings in each year	
2023/24 (residual)	5.30%
2024/25	4.25%
2025/26	3.50%
2026/27	3.00%
2027/28	3.25%
Years 6 to 10	3.25%
Years 10+	3.25%

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

For its cash flow generated balances, the Authority 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 Authority'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 Authority is asked to approve the following treasury indicator and limit: -

<b>Upper limit for principal sums invested for longer than 365 days</b>			
	<b>2024/25</b>	<b>2025/26</b>	<b>2026/27</b>
Principal sums invested for longer than 365 days	£10m	£10m	£10m
Current investments as at 31.12.2023 in excess of 1 year maturing in each year	£0m	£0m	£0m

#### **4.4 Investment Performance / Risk Benchmarking**

This Authority will use an investment benchmark to assess the investment performance of its investment portfolio of overnight 7 day SONIA.

#### **4.5 End of Year Investment Report**

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

#### **4.6 External Fund Managers**

£2m of the Authority's funds is externally managed on a discretionary / pooled basis by CCLA. In addition to this, the Council uses Money Market Funds of which there was £6.1m invested as at 31<sup>st</sup> December 2023.

The Authority's external fund manager(s) will comply with the Annual Investment Strategy. The agreement(s) between the Authority and the fund manager(s) additionally stipulate guidelines on duration and other limits in order to contain and control risk.

## **5 APPENDICES**

(These can be appended to the report or omitted as required)

1. Prudential and treasury indicators
2. Interest rate forecasts
3. Economic background
4. Treasury management practice 1 – credit and counterparty risk management (option 1)
5. Treasury management practice 1 – credit and counterparty risk management (option 2)
6. Approved countries for investments
7. Treasury management scheme of delegation
8. The treasury management role of the section 151 officer

## 5.1 THE CAPITAL PRUDENTIAL AND TREASURY INDICATORS 2024/25 – 2026/27

The Authority'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.

### 5.1.1 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 Authority's overall finances. The Authority is asked to approve the following indicators: -

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

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

%	2022/23 Actual	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate
Non-HRA	-6.63	-14.2	-10.5	-8.8	-6.42
HRA	31.01	26.49	27.04	28.55	27.50

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

#### HRA Ratios

	2022/23 Actual	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate
HRA Debt (£'000)	31,413	31,413	31,413	31,413	31,413
HRA Revenues (£'000)	8,079	8,804	9,457	9,586	9,852
Ratio of Debt to Revenues (%)	26%	28%	30%	31%	31%
Interest Cover (Ideally over 1.10)	0.04	0.73	1.26	1.15	1.33

	2022/23 Actual	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate
HRA Debt (£'000)	31,413	31,413	31,413	31,413	31,413
Number of HRA Dwellings	1,788	1,783	1,778	1,773	1,768
Debt per Dwelling (£)	17.57	17.62	17.67	17.72	17.77

### 5.1.3 Maturity Structure of Borrowing

Maturity structure of borrowing. These gross limits are set to reduce the Authority's exposure to large, fixed rate sums falling due for refinancing, and are required for upper and lower limits.

The Authority is asked to approve the following treasury indicators and limits: -

<b>Maturity structure of fixed interest rate borrowing 2024/25</b>		
	<b>Lower</b>	<b>Upper</b>
Under 12 months	0%	50%
12 months to 2 years	0%	50%
2 years to 5 years	0%	50%
5 years to 10 years	0%	50%
10 years to 20 years	0%	50%
20 years to 30 years	0%	50%
30 years to 40 years	0%	50%
40 years to 50 years	0%	50%
<b>Maturity structure of variable interest rate borrowing 2024/25</b>		
	<b>Lower</b>	<b>Upper</b>
Under 12 months	0%	50%
12 months to 2 years	0%	50%
2 years to 5 years	0%	50%
5 years to 10 years	0%	50%
10 years to 20 years	0%	50%
20 years to 30 years	0%	50%
30 years to 40 years	0%	50%
40 years to 50 years	0%	50%

### 5.1.4. Control of Interest Rate Exposure

Please see paragraphs 3.3, 3.4 and 4.4.

## 5.2 INTEREST RATE FORECASTS 2023-2026

Link Group Interest Rate View 08.01.24													
	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
<b>BANK RATE</b>	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

PWLB forecasts are based on PWLB certainty rates.

### 5.3 ECONOMIC BACKGROUND (commentary provided by LINK)

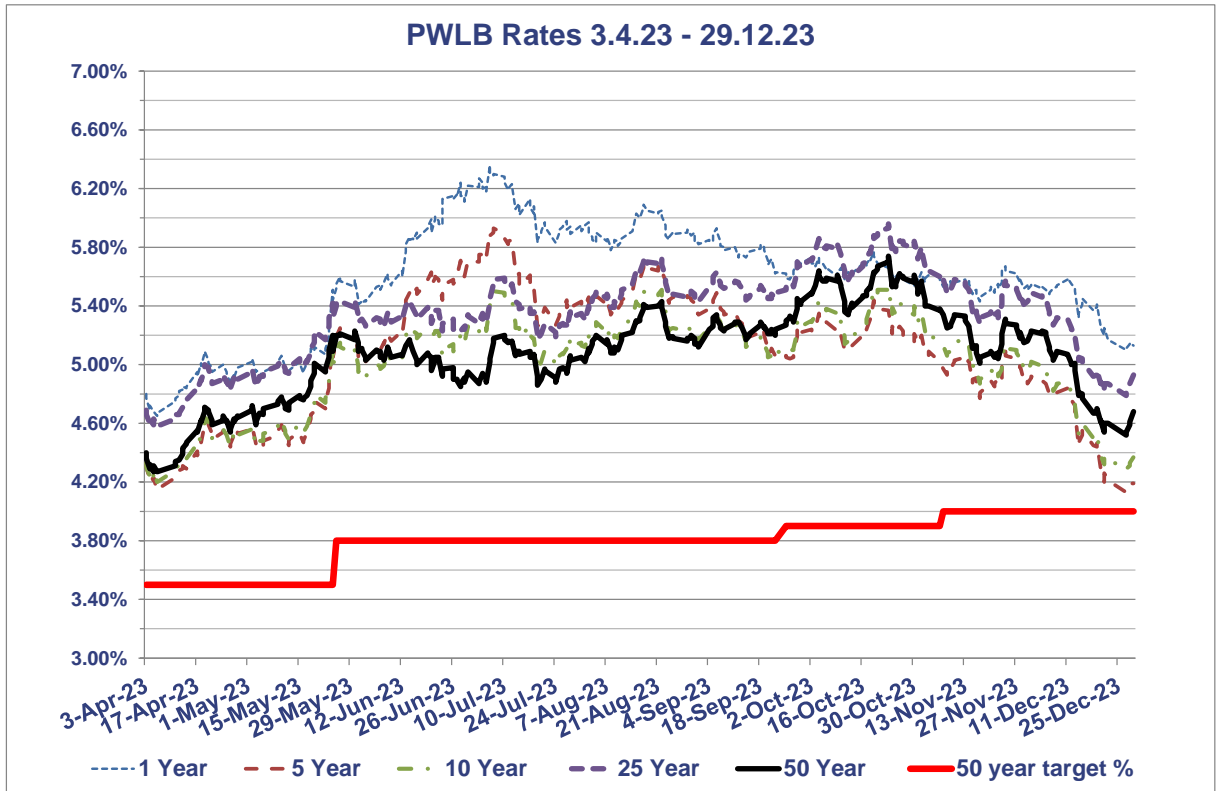
- The third quarter of 2023/24 saw:
  - A 0.3% m/m decline in real GDP in October, potentially partly due to unseasonably wet weather, but also due to the ongoing drag from higher interest rates. Growth for the second quarter, ending 30<sup>th</sup> September, was revised downwards to -0.1% and growth 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 ONS “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% q/q fall may mean the mildest of mild recessions has begun. Indeed, real GDP in October fell 0.3% m/m 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% q/q 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% q/q fall in manufacturing output in Q3.
- The 0.3% m/m fall in retail sales volumes in October means that after contracting by 1.0% q/q (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% m/m, which meant the headline 3myy 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 17<sup>th</sup> 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.

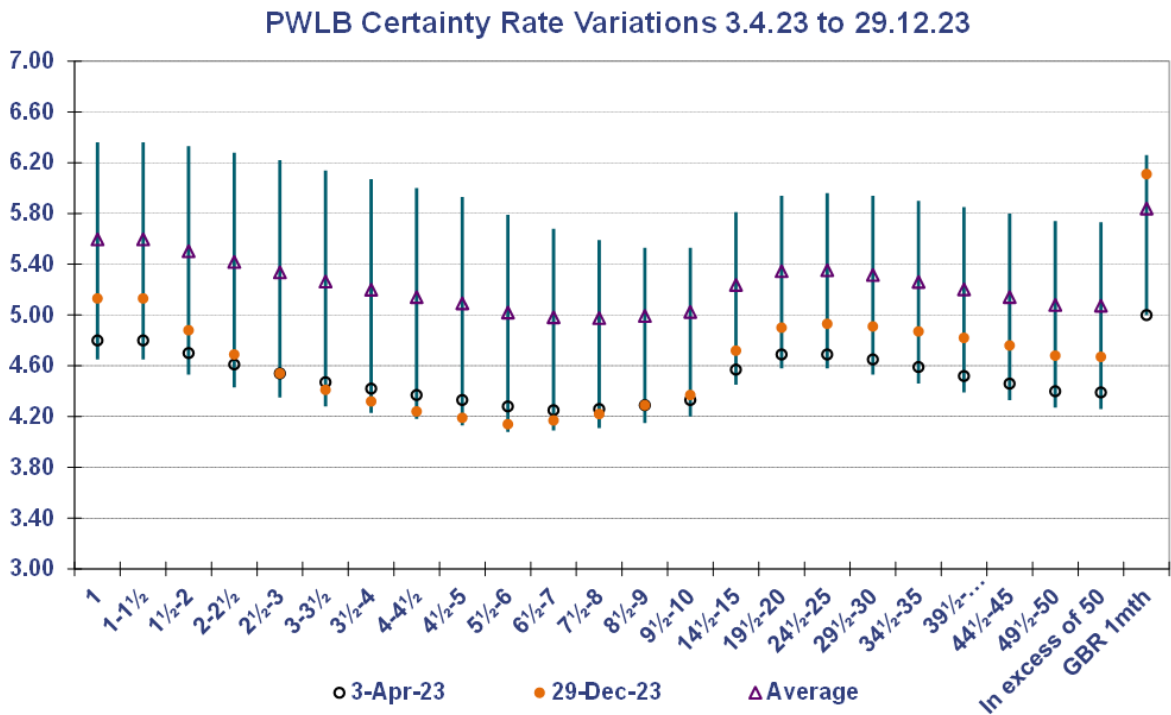


- The Bank of England sprung no surprises with its December monetary policy committee (MPC) meeting, leaving interest rates at 5.25% for the third time in a row and pushing back against the prospect of near-term interest rate cuts. The Bank continued to sound hawkish, with the MPC maintaining its tightening 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 investors’ 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.
- Investors’ growing expectations that the Fed will cut interest rates soon has led to an improvement in risk sentiment, which has boosted the pound and other risky assets. In addition, the rise in the pound, from \$1.21 in November to \$1.27 now, has also been supported by the recent relative decline in UK wholesale gas prices.
- 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
<b>Low</b>	4.65%	4.13%	4.20%	4.58%	4.27%
<b>Date</b>	06/04/2023	27/12/2023	06/04/2023	06/04/2023	05/04/2023
<b>High</b>	6.36%	5.93%	5.53%	5.96%	5.74%
<b>Date</b>	06/07/2023	07/07/2023	23/10/2023	23/10/2023	23/10/2023
<b>Average</b>	5.60%	5.09%	5.03%	5.35%	5.08%
<b>Spread</b>	1.71%	1.80%	1.33%	1.38%	1.47%

### MPC meetings 2<sup>nd</sup> November and 14<sup>th</sup> December 2023

- On 2<sup>nd</sup> November, the Bank of England’s Monetary Policy Committee (MPC) voted to keep Bank Rate on hold at 5.25%, and on 14<sup>th</sup> December reiterated that view. Both increases 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.

## 5.4 TREASURY MANAGEMENT PRACTICE (TMP1) – CREDIT AND COUNTERPARTY RISK MANAGEMENT OPTION 1

**SPECIFIED INVESTMENTS:** All such investments will be sterling denominated, with **maturities up to a maximum of 1 year**, meeting the minimum ‘high’ quality criteria where applicable. (Non-specified investments which would be specified investments apart from originally being for a period longer than 12 months, will be classified as being specified once the remaining period to maturity falls to under twelve months.)

**NON-SPECIFIED INVESTMENTS:** These are any investments which do not meet the specified investment criteria. A maximum of £10m\*\* will be held in aggregate in non-specified investment.

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

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

	Minimum credit criteria / colour band	** Max % of total investments / £ limit per institution	Max. maturity period
DMADF – UK Government	Yellow	100%	6 months (max. is set by the DMO*)
UK Gilts	Yellow	£2m	5 years
UK Treasury Bills	Yellow	£2m	364 days (max. is set by the DMO*)
Bonds issued by multilateral development banks	Yellow	£2m	5 years
Money Market Funds CNAV	AAA	£3m per fund	Liquid
Money Market Funds LNAV	AAA	£3m per fund	Liquid
Money Market Funds VNAV	AAA	£3m per fund	Liquid

Ultra-Short Dated Bond Funds with a credit score of 1.25	AAA	100%	Liquid
Ultra-Short Dated Bond Funds with a credit score of 1.5	AAA	100%	Liquid
Local Authorities	N/A	100%	12 Months
	N/A	£2m – non specified	5 Years
Term Deposits with Housing Associations	Blue Orange Red Green No Colour	£3m per fund	12 months 12 months 6 months 100 days Not for use
Term Deposits with Banks and Building Societies	Blue Orange Red Green No Colour	£6m per institution £9m per banking group	12 months 12 months 6 months 100 days Not for use
	Blue Orange Red Green No Colour	£3m per institution	3 years
CDs or Corporate Bonds with Banks and Building Societies	Blue Orange Red Green No Colour	£3m- non specified per banking group	12 months 12 months 6 months 100 days Not for use
Property Funds (longer term investment option)	N/A	£5m	Minimum 5 years
Gilt Funds	UK sovereign rating		
Council's own bank	N/A	Unlimited	Overnight

\* DMO – is the Debt Management Office of HM Treasury

**Accounting treatment of investments.** The accounting treatment may differ from the underlying cash transactions arising from investment decisions made by this Authority. To ensure that the Authority is protected from any adverse revenue

impact, which may arise from these differences, we will review the accounting implications of new transactions before they are undertaken.

### **5.5 APPROVED COUNTRIES FOR INVESTMENTS**

The Council can invest in 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.

## **5.6 TREASURY MANAGEMENT SCHEME OF DELEGATION**

### **(i) 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 recommendations to council;
- receiving and reviewing regular monitoring reports and acting on recommendations;
- approving the selection of external service providers and agreeing terms of appointment.

### **(iii) Director for Corporate Services**

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

## 5.7 THE TREASURY MANAGEMENT ROLE OF THE SECTION 151 OFFICER

### The S151 (responsible) officer – Director for Corporate Services

- 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 authority
- 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 Authority 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 the 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.*