Report to: Full Council – 17 December 2024

Relevant Committee Chair: Councillor Peter Harris, Audit & Governance Committee

Director Lead: Sanjiv Kohli, Director – Resources and S151 Officer

Lead Officer: Andrew Snape, Assistant Business Manager Financial Services, Ext. 5323

| Report Summary | |
|---|---|
| **Report Title** | Treasury Management Mid-Year Report 2024/25 |
| **Purpose of Report** | This report provides an update on the Council's treasury activity and prudential indicators for the first half of 2024/25. This was reported to the Audit & Governance Committee on 11 December 2024. |
| **Recommendations** | That the Council note:<br>(a) the treasury management activity; and<br>(b) the Prudential Indicators detailed in Section 6 & 7 of the report. |
| **Reason for Recommendation** | To allow Full Council to note the Treasury Management Activity and Prudential Indicators. |

## 1.0 Background Information

1.1 This report has been written in accordance with the requirements of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised 2017). The primary requirements of the Code are as follows:

1.2 Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.

1.3 Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.

1.4 Receipt by the full council of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead, a Mid-year Review Report and an Annual Report, (stewardship report), covering activities during the previous year.

1.5 Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

1.6 Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body. For this Council the delegated body is the Audit and Governance Committee.

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

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

1.8 Treasury Management is defined as: "The management of the local authority's borrowing, investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks".

1.9 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 the Council can meet its capital spending operations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses, and on occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

## 2.0 <u>Summary of Treasury Balances as at 30 September 2024</u>

2.1 Below is a summary of the Councils borrowing position as at 30 September 2024, further information is available at section 4.

| **Balance on 01/04/2024 £m** | | **Balance on 30/09/2024 £m** |
|---|---|---|
| 85.463 | Total Borrowings | 94.922 |
| 4.864 | Total Other Long Term Liabilities | 4.789 |
| **90.327** | **TOTAL EXTERNAL DEBT** | **99.711** |

2.2 Below is a summary of the Council's investment position as at 30 September 2024, further information is available at section 5.

| **Balance on 01/04/2024 £m** | | **Balance on 30/09/2024 £m** |
|---|---|---|

| | | |
|---|---|---|
| 21.910 | Total Short Term Investments | 30.020 |
| 12.500 | Total Long Term Investments | 12.500 |
| **34.410** | **TOTAL INVESTMENTS** | **42.520** |

2.3 Below is a summary of the Councils capital expenditure position as at 30 September 2024, further information is available at section 3.

| Capital Expenditure | 2024/25 Initial Capital Budget £m | 2024/25 Revised Estimate £m | 2024/25 Current Expenditure £m |
|---|---|---|---|
| General Fund Expenditure | 25.599 | 28.442 | 5.012 |
| HRA Expenditure | 25.808 | 21.025 | 8.459 |
| **Total Capital Expenditure** | **51.407** | **49.467** | **13.471** |

2.4 **Prudential Indicators**, during the first half of the financial year there was no breach in the prudential indicators.

**Treasury Management Strategy Statement (TMSS) and Annual Investment Strategy update**

2.5 The Treasury Management Strategy Statement (TMSS) for 2024/25 was approved by Full Council on 7 March 2024. There are no suggested policy changes to the TMSS within this report; the details in this report update the position in the light of the updated economic position and capital budget changes approved throughout the year.

**3.0 The Council's Capital Position**

3.1 This part of the report is structured to update:

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

3.2 The table below shows the revised estimates for capital expenditure and the changes since the Capital Programme was agreed within the Capital budget on 7 March 2024.

| Capital Expenditure | 2024/25 Original Budget Approved 7 March 2024 £m | 2024/25 Revised Budget as at 30 September 2024 £m | Actual Spend as at 30 September 2024 £m |
|---|---|---|---|
| General Fund Expenditure | 25.599 | 28.442 | 5.012 |
| HRA Expenditure | 25.808 | 21.025 | 8.459 |
| **Total Capital Expenditure** | **51.407** | **49.467** | **13.471** |

| | | | |
|---|---|---|---|
| Financed By: | | | |
| Capital Receipts | 1.667 | 2.579 | |
| Capital Grants & CIL | 4.907 | 11.082 | |
| Capital Reserves | 0.756 | 0.076 | |
| Revenue | 13.719 | 15.267 | |
| **Total Financing** | **21.049** | **29.004** | |
| **Borrowing Requirement** | **30.358** | **20.463** | |

3.3 The financing of the Capital Programme will be determined by the S151 Officer at the year-end based on best use of resources.

3.4 The movement from the Budget approved 7 March 2024 relates to approved capital carry forward requests and approved variations to the capital programme as shown in the table below.

| | |
|---|---|
| **Original Capital Budget Approved 2024/25** | **£51.407m** |
| Capital Slippages Carried Forward | £13.588m |
| Cabinet Approvals 10 September 24 | (£1.763m) |
| Cabinet Variations requested 3 December 24 | (£13.765m) |
| **New Revised Budget** | **£49.467m** |

## 4.0 <u>Borrowing Strategy</u>

4.1 At 30 September 2024 the Council held £94.922m of loans, as part of its strategy for funding previous years' borrowing within those capital programmes.

4.2 **Borrowing Activity in 2024/25**

| | **General Fund** | | **HRA** | |
|---|---|---|---|---|
| | **Balance on 01/04/2024 £m** | **Balance on 30/09/2024 £m** | **Balance on 01/04/2024 £m** | **Balance on 30/09/2024 £m** |
| Short Term Borrowing | 0.528 | 1.006 | 6.532 | 15.513 |
| Long Term Borrowing | 3.500 | 3.500 | 74.903 | 74.903 |
| **Total Borrowing** | **4.028** | **4.506** | **81.435** | **90.416** |
| Other Long Term Liabilities | 4.864 | 4.789 | 0.000 | 0.000 |
| **Total External Debt** | **8.892** | **9.295** | **81.435** | **90.416** |
| CFR | 34.591 | 45.216 | 101.067 | 113.030 |
| **Under / (over) borrowing** | **25.699** | **35.921** | **19.632** | **22.613** |

4.3 As the Council is in a significant under borrowed position, as per the table in 4.2, there may be a requirement during the remainder of the financial year where new borrowing is required. Any new borrowing will be within the approved Treasury Management Borrowing Strategy framework and will have been reviewed by the S151 Officer for cost effectiveness as whether to borrow shorter term or long term in relation to interest rate forecasts.

4.4 **LOBOs**: The Council holds £3.5m of LOBO (Lender's Option Borrower's Option) loans where the lender has the option to propose an increase in the interest rate at set dates, following which the Council has the option to either accept the new rate or to repay the loan at no additional cost. All of the £3.5m of LOBOS had options during the last 6 months, none of which were exercised by the lender. The Council acknowledges there is an element of refinancing risk even though in the current interest rate environment lenders are unlikely to exercise their options.

4.5 **Internal borrowing*:*** For the Council, the use of internal resources in lieu of borrowing has continued to be the most cost-effective means of funding of capital expenditure that has not been funded from grants and other resources. This has lowered overall treasury risk by reducing both external debt and temporary investments. However, this position will not be sustainable over the medium to longer term as the Council needs to use reserves for the purpose they were set aside for, and external borrowing may need to be undertaken.

4.6 **Debt rescheduling*:*** The premium charge for early repayment of PWLB debt remains relatively expensive for the loans in the Council's portfolio and therefore unattractive for debt rescheduling activity. No rescheduling activity was undertaken or is proposed during the rest of the financial year as a consequence.

## 5.0 Investment Activity

5.1 The Guidance on Local Government Investments in England gives priority to security and liquidity and the Council's aim is to achieve a return commensurate with these principles.

5.2 **Investment Activity in 2024/25**

| Type of Investment | Balance on 01/04/2024 £m | Balance on 30/09/2024 £m | Average Interest Rate |
|---|---|---|---|
| **Short term Investments** | | | |
| *Fixed Term Deposits:* | | | |
| Santander | 5.000 | 5.000 | 4.81% |
| Lloyds 95 Day Notice | 5.000 | 5.000 | 4.99% |
| Close Brothers | 2.000 | 0 | 0% |
| Standard Chartered Sustainable Deposit | 0 | 3.000 | 5.10% |
| *Money Market Funds:* | | | |
| Goldman Sachs | 0.310 | 0.310 | 4.92% |
| Deutsche Bank | 0.050 | 1.905 | 4.94% |
| Invesco | 4.710 | 6.870 | 5.02% |
| Northern Trust | 2.600 | 5.695 | 5.00% |
| CCLA | 2.240 | 2.240 | 4.92% |
| **Total Short Term Investments** | **21.910** | **30.020** | |
| Long term Investments | | | |
| CCLA Property Fund | 7.000 | 7.000 | 4.83% |
| CCLA Diversified Income Fund | 5.500 | 5.500 | 4.05% |
| **Total Long Term Investments** | **12.500** | **12.500** | |
| **TOTAL INVESTMENTS** | **34.410** | **42.520** | |
| Increase/ (Decrease) in Investments | | 8.110 | |

5.3 Both the CIPFA Code and government guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its treasury investments before seeking the optimum 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.

## 6.0 Non-Treasury Investments

6.1 The definition of investments in CIPFA's revised Treasury Management Code now covers all the financial assets of the Council as well as other non-financial assets which the Council holds primarily for financial return or regeneration purposes. This is replicated in MLUHC's Investment Guidance, in which the definition of investments is further broadened to also include all such assets held partially for financial return or regeneration purposes.

Breakdown below of current Non-Treasury Investments held;

| **Counterpart** | **Balance at 30/09/2024 £m** |
|---|---|
| Loans to Housing Associations | 0.011 |
| Loans to Parish Councils | 0.009 |

6.2 These investments are due to generate £0.001m of investment income for the Council after taking account of direct costs, representing a rate of return of 6.31%.

**6.3 Maturity Structure of Fixed Rate Borrowing.** This indicator is to limit large concentrations of fixed rate debt needing to be replaced at times of uncertainty over interest rates.

| | **Upper Limit %** | **Actual at 30/9/24 £m** | **Actual at 30/9/24 £m** | **Compliance** |
|---|---|---|---|---|
| Under 12 Months | 15% | 12.987 | 13.68% | Yes |
| 12-24 Months | 15% | 5.000 | 5.27% | Yes |
| 2-5 Years | 30% | 18.031 | 19.00% | Yes |
| 5-10 Years | 100% | 8.039 | 8.47% | Yes |
| Over 10 Years | 100% | 50.865 | 53.59% | Yes |

### Limits to Investing Activity

**6.4 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 | Actual | Compliance |
|---|---|---|---|
| Portfolio average credit rating | A | AA | Yes |

**6.5** **Liquidity Risk Indicator**. 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 banding period, without additional borrowing.

| Total Cash Available within; | Limit | Actual 30/09/24 | Compliance |
|---|---|---|---|
| 3 Months | 100% | 59% | Yes |
| 3-12 Months | 80% | 12% | Yes |
| Over 12 Months | 60% | 29% | Yes |

**6.6** **Principal Sums Invested for over 364 Days.** 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.

| Price risk indicator | Limit | Actual 30/09/24 | Compliance |
|---|---|---|---|
| Limit on principal invested beyond year end | £15m | £12.5m | Yes |

## 7.0 Limits to Capital Activity

**7.1** **Capital Financing Requirement.** The table below shows the CFR, which is the underlying external need to incur borrowing for a capital purpose.

| | 2024/25 Original Estimate £m | 2024/25 Revised Estimate £m |
|---|---|---|
| CFR – non housing | 45.216 | 43.412 |
| CFR – housing | 113.030 | 109.095 |
| **Total CFR** | **158.246** | **152.507** |
| **Estimated Net Movements in CFR** | | **-5.739** |

**7.2** **Capital Financing Costs to Net Revenue Stream.** Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP are charged to revenue, offset by any investment income receivable. The net annual charge is known as financing costs; this is compared to the net revenue stream i.e. the amount funded from Council Tax, business rates and general government grants.

| | 2024/25 Original Estimate £m | 2024/25 Revised Estimate £m |
|---|---|---|
| ***General Fund*** | | |
| Financing Costs | -1.379 | -1.480 |
| Proportion of net revenue stream | -5.61% | -6.02% |

| | | |
|---|---|---|
| ***Housing Revenue Account*** | | |
| Financing Costs | 13.924 | 13.924 |
| Proportion of net rental stream | 47.09% | 47.05% |

## 8.0 Economic Background/Interest Rate Forecast

8.1 **Appendix A and Appendix B** gives a summarised outlook for the economic background and interest rate forecast from our Treasury Consultants, Link.

## 9.0 Implications

In writing this report and in putting forward recommendations, officers have considered the following implications: Data Protection; Digital & Cyber Security; Equality & Diversity; Financial; Human Resources; Human Rights; Legal; Safeguarding & Sustainability and where appropriate they have made reference to these implications and added suitable expert comment where appropriate.

**Background Papers and Published Documents**

Except for previously published documents, which will be available elsewhere, the documents listed here will be available for inspection in accordance with Section 100D of the Local Government Act 1972.

None.

**APPENDIX A**

**Economics Update**

- The third quarter of 2024 (July to September) saw:
  - GDP growth stagnating in July following downwardly revised Q2 figures (0.5% q/q)
  - A further easing in wage growth as the headline 3myy rate (including bonuses) fell from 4.6% in June to 4.0% in July;
  - CPI inflation hitting its target in June before edging above it to 2.2% in July and August;
  - Core CPI inflation increasing from 3.3% in July to 3.6% in August;
  - The Bank of England initiating its easing cycle by lowering interest rates from 5.25% to 5.0% in August and holding them steady in its September meeting;
  - 10-year gilt yields falling to 4.0% in September.
- The economy's stagnation in June and July points more to a mild slowdown in GDP growth than a sudden drop back into a recession. Moreover, the drop in September's composite activity Purchasing Managers Index, from 53.8 in August to 52.9, was still consistent with GDP growth of 0.3%-0.4% for the summer months. This is in line with the Bank of England's view, and it was encouraging that an improvement in manufacturing output growth could be detected, whilst the services PMI balance suggests non-retail services output grew by 0.5% q/q in Q3. Additionally, the services PMI future activity balance showed an uptick in September, although readings after the Chancellor's announcements at the Budget on 30th October will be more meaningful.
- The 1.0% m/m jump in retail sales in August was stronger than the consensus forecast for a 0.4% m/m increase. The rise was reasonably broad based, with six of the seven main sub sectors recording monthly increases, though the biggest gains came from clothing stores and supermarkets, which the ONS reported was driven by the warmer-than-usual weather and end of season sales. As a result, some of that strength is probably temporary.
- The government's plans to raise public spending by around £16bn a year (0.6% GDP) have caused concerns that a big rise in taxes will be announced in the Budget, which could weaken GDP growth in the medium-term. However, if taxes are raised in line with spending (i.e., by £16bn) that would mean the overall stance of fiscal policy would be similar to the previous government's plan to reduce the budget deficit. Additionally, rises in public spending tend to boost GDP by more than increases in taxes reduce it. Our colleagues at Capital Economics suggest GDP growth will hit 1.2% in 2024 before reaching 1.5% for both 2025 and 2026.
- The further easing in wage growth will be welcomed by the Bank of England as a sign that labour market conditions are continuing to cool. The 3myy growth rate of average earnings fell from 4.6% in June to 4.0% in July. On a three-month annualised basis, average earnings growth eased from 3.0% to 1.8%, its lowest rate since December 2023. Excluding bonuses, the 3myy rate fell from 5.4% to 5.1%.
- Other labour market indicators also point to a further loosening in the labour market. The 59,000 fall in the alternative PAYE measure of the number of employees in August marked the fourth fall in the past five months. And the 77,000 decline in the three months to August was the biggest drop since November 2020. Moreover, the number of workforce jobs fell by 28,000 in Q2. The downward trend in job vacancies continued too. The number of job vacancies fell from 872,000 in the three months to July to 857,000 in the three months to August. That leaves it 34% below its peak in May 2022, and just 5% above its pre-pandemic level. Nonetheless, the Bank of England is still more concerned about the inflationary influence of the labour market rather than the risk of a major slowdown in labour market activity.

- CPI inflation stayed at 2.2% in August, but services inflation rose from a two-year low of 5.2% in July to 5.6%, significantly above its long-run average of 3.5%. Food and fuel price inflation exerted some downward pressure on CPI inflation, but these were offset by the upward effects from rising furniture/household equipment inflation, recreation/culture inflation and a surprisingly large rise in airfares inflation from -10.4% in July to +11.9% in August. As a result, core inflation crept back up from 3.3% to 3.6%. CPI inflation is also expected to rise in the coming months, potentially reaching 2.9% in November, before declining to around 2.0% by mid-2025.
- The Bank initiated its loosening cycle in August with a 25bps rate cut, lowering rates from 5.25% to 5.0%. In its September meeting, the Bank, resembling the ECB more than the Fed, opted to hold rates steady at 5.0%, signalling a preference for a more gradual approach to rate cuts. Notably, one Monetary Policy Committee (MPC) member (Swati Dhingra) voted for a consecutive 25bps cut, while four members swung back to voting to leave rates unchanged. That meant the slim 5-4 vote in favour of a cut in August shifted to a solid 8-1 vote in favour of no change.
- Looking ahead, CPI inflation will likely rise in the coming months before it falls back to its target of 2.0% in mid-2025. The increasing uncertainties of the Middle East may also exert an upward pressure on inflation, with oil prices rising in the aftermath of Iran's missile attack on Israel on 1 October. China's recent outpouring of new fiscal support measures in the latter stages of September has also added to the upshift in broader commodity prices, which, in turn, may impact on global inflation levels and thus monetary policy decisions. Despite these recent developments, our central forecast is still for rates to fall to 4.5% by the end of 2024 with further cuts likely throughout 2025. This is in line with market expectations, however, although a November rate cut still looks likely, December may be more problematic for the Bank if CPI inflation spikes towards 3%. In the second half of 2025, though, we think a more marked easing in inflation will prompt the Bank to speed up, resulting in rates eventually reaching 3.0%, rather than the 3.25-3.50% currently priced in by financial markets.
- Our forecast is next due to be updated around mid-November following the 30 October Budget, 5 November US presidential election and the 7 November MPC meeting and the release of the Bank of England Quarterly Monetary Policy Report.
- Looking at gilt movements in the first half of 2024/25, and you will note the 10-year gilt yield declined from 4.32% in May to 4.02% in August as the Bank's August rate cut signalled the start of its loosening cycle. Following the decision to hold the Bank Rate at 5.0% in September, the market response was muted, with the 10-year yield rising by only 5bps after the announcement. This likely reflected the fact that money markets had priced in a 25% chance of a rate cut prior to the meeting. The yield had already increased by about 10bps in the days leading up to the meeting, driven in part by the Fed's "hawkish cut" on 18 September. There is a possibility that gilt yields will rise near-term as UK policymakers remain cautious due to persistent inflation concerns, before declining in the longer term as rates fall to 3.0%.
- The FTSE 100 reached a peak of 8,380 in the third quarter of 2024, but its performance is firmly in the shade of the US S&P500, which has breached the 5,700 threshold on several occasions recently. Its progress, however, may pause for the time being whilst investors wait to see who is elected the next US President, and how events in the Middle East (and Ukraine) unfold. The catalyst for any further rally (or not) is likely to be the degree of investors' faith in AI.

**Interest rate forecasts** **APPENDIX B**

The Council has appointed Link Group as its treasury advisors and part of their service is to assist the Council to formulate a view on interest rates. The PWLB rate forecasts below are based on the Certainty Rate (the standard rate minus 20 bps) which has been accessible to most authorities since 1st November 2012.

Our latest forecast on 28 May sets out a view that short, medium and long-dated interest rates will fall back over the next year or two, although there are upside risks in respect of the stickiness of inflation and a continuing tight labour market, as well as the size of gilt issuance. Our PWLB rate forecasts below are based on the Certainty Rate (the standard rate minus 20 bps, calculated as gilts plus 80bps) which has been accessible to most authorities since 1st November 2012.

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