APPENDIX 1

Appendix 1

Treasury Management Report - Quarter 3 2024/25

Introduction

In January 2023, the Council adopted the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice* (the CIPFA Code) which requires the Council to approve treasury management semi-annual and annual reports. This quarterly report provides an additional update.

This report includes the new requirement in the 2021 code, mandatory from 1st April 2023, of quarterly reporting of the treasury management prudential indicators.

The Council's treasury management strategy for 2024/25 was approved at a meeting on 29th January 2024. The Council has borrowed and invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk remains central to the Council's treasury management strategy.

External Context

Economic background: The Chancellor of the Exchequer delivered her Autumn Budget at the end of October. Based on the plans announced, the Office for Budget Responsibility reported they would provide a short-term boost to GDP growth before weakening it further out and push inflation higher over the medium-term. This change to the economic and inflation outlook caused financial markets to readjust expectations of Bank of England (BoE) Bank Rate and gilt yields higher. The council's treasury management advisor, Arlingclose, also revised its interest rate forecast upwards in November, with Bank Rate expected to eventually fall to 3.75%.

UK annual Consumer Price Index (CPI) inflation remained above the Bank of England (BoE) 2% target in the later part of the period. The Office for National Statistics (ONS) reported headline consumer prices rose 2.6% in November 2024, up from 2.3% in the previous month and in line with expectations. Core CPI also rose, but by more than expected, and remained elevated at 3.6% in November against a forecast of 3.5% and compared to 3.3% in the previous month.

UK economy GDP registered no growth (0.0%) between July and September 2024 and 0.4% between April and June 2024, a further downward revision from the 0.5% rate previously reported by the ONS. Of the monthly GDP figures, the economy was estimated to have contracted by 0.1% in October, following the same size decline in September.

The labour market continued to loosen, but the ONS data still require treating with some caution. Recent figures reported the unemployment rate rose to 4.3% (3mth/year) in the three months to October 2024 and economic inactivity fell to

21.7%. The ONS reported pay growth over the same three-month period at 5.2% for both regular earnings (excluding bonuses) and for total earnings.

The BoE's Monetary Policy Committee (MPC) held Bank Rate at 4.75% at its December 2024 meeting, having reduced it to that level in November and following a previous 25bp cut from the 5.25% peak at the August MPC meeting (5-4 vote to cut). At the December meeting, six Committee members voted to maintain Bank Rate at 4.75% while three members preferred to reduce it to 4.50%. The meeting minutes suggested a reasonably dovish tilt to rates with the outlook for economic growth a concern among policymakers as the Bank downgraded its Q4 GDP forecast from 0.3% to 0.0%.

The November Monetary Policy Report (MPR) showed the BoE expected GDP growth to pick up to around 1.75% (four-quarter GDP) in the early period of the forecast horizon before falling back. The impact from the government's Autumn Budget pushed GDP higher in 2025 than was expected in the August MPR, before becoming weaker. The outlook for CPI inflation showed it rising above the MPC's 2% target from 2024 into 2025 and reaching around 2.75% by the middle of calendar 2025. Over the medium-term, once the near-term pressures eased, inflation was expected to stabilise around the 2% target. The unemployment rate was expected to increase modestly, rising to around 4.5%, the assumed medium-term equilibrium unemployment rate, by the end of the forecast horizon.

Arlingclose, the Council's treasury adviser, maintained its central view that Bank Rate would continue to fall from the 5.25% peak. From the first cut in August 2024, followed by the next in November which took Bank Rate to 4.75%, February 2025 is deemed the likely month for the next reduction, with other cuts following steadily in line with MPR months to take Bank Rate down to around 3.75% by the end of 2025.

The US Federal Reserve continued cutting interest rates during the period, reducing the Fed Funds Rate by 0.25% at its December 2024 monetary policy meeting to a range of 4.25%-4.50%, marking the third consecutive reduction. Further interest rate cuts are expected into 2025, but uncertainties around the potential inflationary impact of President-elect Trump's policies may muddy the waters in terms of the pace and magnitude of further rate reductions. Moreover, the US economy continues to expand at a decent pace, suggesting that monetary policy may need to remain more restrictive in the coming months than had previously been anticipated.

The European Central Bank (ECB) also continued its rate cutting cycle, reducing its three key policy rates by 0.25% in December. Euro zone inflation rose above the ECB 2% target in November 2024, hitting 2.2% as was widely expected and a further increase from 2% in the previous month. Inflation is expected to rise further in the short term, but then fall back towards the 2% target during 2025, with the ECB remaining committed to maintaining rates at levels consistent with bringing inflation to target, but without suggesting a specific path.

Financial markets: Financial market sentiment was generally positive over the period, but economic, financial and geopolitical issues meant the ongoing trend of bond yield volatility very much remained. In the last few months of the period, there was a general rising trend in yields due to upwardly revised interest rate and inflation expectations, causing gilt yields to end the period at substantially higher levels to where they began.

Over the period, the 10-year UK benchmark gilt yield started at 3.94% and ended at a high of 4.57%, having reached a low of 3.76% in mid-September. While the 20-year gilt started at 4.40%, ended at a high of at 5.08% and hit a low of 4.27% in mid-September. The Sterling Overnight Rate (SONIA) averaged 5.01% over the period to 31st December.

Credit review: In October, Arlingclose revised its advised recommended maximum unsecured duration limit on most banks on its counterparty list to six months. Duration advice for the remaining five institutions, including the newly added Lloyds Bank Corporate Markets, was kept to a maximum of 100 days.

Fitch revised the outlooks on Royal Bank of Scotland, NatWest Markets PLC, and National Westminster Bank to positive from stable, while affirming their long-term ratings at A+.

Moody's upgraded the ratings on National Bank of Canada to Aa2 from Aa3, having previously had the entity on Rating Watch for a possible upgrade. Moody's also upgraded the ratings on The Co-operative Bank to A3 (from Baa3) and downgraded the ratings on Coventry Building Society to A3 (from A2) and Canada's Toronto-Dominion Bank to Aa2 (from Aa1).

S&P also downgraded Toronto-Dominion Bank, to A+ from AA-, but kept the outlook at stable.

Credit default swap prices were generally lower at the end of the period compared to the beginning for the vast majority of the names on UK and non-UK lists. Price volatility over the period also remained generally more muted compared to previous periods.

Financial market volatility is expected to remain a feature, at least in the near term and, credit default swap levels will be monitored for signs of ongoing credit stress. As ever, the institutions and durations on the Council's counterparty list recommended by Arlingclose remain under constant review.

Local Context

On 31st March 2024, the Council had net borrowing of £127.4m arising from its revenue and capital income and expenditure. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while balance sheet resources are the underlying resources available for investment. These factors are summarised in Table 1 below.

Table 1: Balance Sheet Summary

	31.3.24 Actual £m	**31.3.25 Forecast £m**
General Fund CFR	21.7	40.1
HRA CFR	177.3	189.1
Total CFR	**199.0**	**229.2**
Less: *Other debt liabilities	0	(0.8)
Borrowing CFR	**199.0**	**228.4**
External borrowing**	(142.8)	(157.0)
Internal borrowing	56.2	71.4
Less: Balance sheet resources	(70.2)	(81.4)
Net	**14.0**	**10.0**

* finance leases, PFI liabilities and transferred debt that form part of the Council's total debt
** shows only loans to which the Council is committed and excludes optional refinancing

The treasury management position at 31st December and the change over the quarter is shown in Table 2 below.

Table 2: Treasury Management Summary

	31.3.24 Balance £m	**Movement £m**	**31.12.24 Balance £m**	**31.12.24 Rate %**
Long Term Borrowing – PWLB	142.8	7.7	150.5	3.91
Total Borrowing	**142.8**	**7.7**	**150.5**	**3.91**
Short-Term Investments	(14.0)	(4.0)	(18.0)	(4.77)
Cash and cash Equivalents	(1.4)	(3.3)	(4.7)	(4.65)
Total Investments	**(15.4)**	**(7.3)**	**(22.7)**	**(4.74)**
Net Borrowing	**127.4**	**0.4**	**127.80**	

Borrowing strategy and activity

As outlined in the treasury strategy, the Council's chief objective when borrowing has been to strike an appropriately risk balance between securing lower interest costs and achieving cost certainty over the period for which funds are required, with flexibility to renegotiate loans should the Council's long-term plans change being a secondary objective. The Council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. During the period short term interest rates have been higher than long term interest rates.

After substantial rises in interest rates since 2021 many central banks have now begun to reduce their policy rates, albeit slowly. Gilt yields were volatile but have increased overall during the period. Much of the increase has been in response to market concerns that policies introduced by the Labour government will be inflationary and lead to higher levels of government borrowing. The election of Donald Trump in the US in November is also expected to lead to inflationary trade policies.

The PWLB certainty rate for 10-year maturity loans was 4.80% at the beginning of the period and 5.40% at the end. The lowest available 10-year maturity rate was 4.52% and the highest was 5.44%. Rates for 20-year maturity loans ranged from 5.01% to 5.87% during the period, and 50-year maturity loans from 4.88% to 5.69%.

Whilst the cost of short-term borrowing from other local authorities spiked to around 7% in late March 2024, primarily due a dearth of LA-LA lending/borrowing activity during that month, as expected shorter-term rates reverted to a more market-consistent range and were generally around 5.00% - 5.5%. Rising rates were seen towards the end of the period in the LA-LA market.

CIPFA's 2021 Prudential Code is clear that local authorities must not borrow to invest primarily for financial return and that it is not prudent for local authorities to make any investment or spending decision that will increase the capital financing requirement and so may lead to new borrowing, unless directly and primarily related to the functions of the Authority. PWLB loans are no longer available to local authorities planning to buy investment assets primarily for yield unless these loans are for refinancing purposes. The Authority has no new plans to borrow to invest primarily for financial return.

On 31st December the Council held £150.5m of loans, an increase of £7.7m since 31st March 2024, as part of its strategy for funding previous and current years' capital programmes. Outstanding loans on 31st December are summarised in Table 3A below.

Table 3A: Borrowing Position

PWLB Borrowing **Term**	**Maturity Profile 31 March 2024 £'000**	**Net Movement £'000**	**Maturity Profile 31 December 2024 £'000**
12 Months	6,109	(5,906)	203
1 - 2 years	9,000	800	9,800
2 - 5 years	10,284	2,400	12,684
5 - 10 years	28,326	4,000	32,326
10 - 15 years	42,000	400	42,400
Over 15 years	47,090	6,000	53,090
Total PWLB Debt	**142,809**	**7,694**	**150,503**

The Council's borrowing decisions are not predicated on any one outcome for interest rates and a balanced portfolio of short-term and long-term borrowing was maintained.

There remains a strong argument for diversifying funding sources, particularly if rates can be achieved on alternatives which are below gilt yields + 0.80%. The Council will evaluate and pursue these lower cost solutions and opportunities with its advisor Arlingclose.

The National Wealth Fund (formerly the UK Infrastructure Bank) is one alternative source of funding which offers funding at gilt yields + 0.40% (0.40% below the PWLB certainty rate) and the possibility of more flexible funding structures than the PWLB. Funding from the National Wealth Fund is generally only available for certain types of projects that meet its criteria of green energy, transport, digital, water and waste. The minimum loan size is £5 million.

Treasury Management Investment Activity

CIPFA revised TM Code defines treasury management investments as those which arise from the Council's cash flows or treasury risk management activity that ultimately represents balances which need to be invested until the cash is required for use in the course of business.

The Council holds invested funds, representing income received in advance of expenditure plus balances and reserves held. During the year, the Council's investment balances ranged between £10.0 and £29.0 million due to timing differences between income and expenditure. The investment position is shown in table 4 below.

Table 4: Treasury Investment Position

Bank Name	Duration of Loan	B/Fwd 01/04/24 £000's	Amount Invested 2024/25 £000's	Amount Returned 2024/25 £000's	Balance Invested 31/12/24 £000's	Interest Received 31/12/24 £000's
Federated Fund 3	Call	3,000	20,604	(18,604)	5,000	(104)
Aberdeen Standard	Call	0	7,007	(7,007)	0	(7)
CCLA Public Sector Deposit Fund	1 Day Call	0	11,524	(8,524)	3,000	(24)
Aviva	Call	0	28,122	(23,122)	5,000	(122)
Invesco	Call	1,000	5,016	(1,016)	5,000	(16)
JP Morgan	Call	0	0	(0)	0	(0)
Goldman Sachs	Call	0	0	(0)	0	(0)
SSGA	Call	0	5,007	(5,007)	0	(7)
Lancashire County Council	12 Months	5,000	163	(5,163)	0	(163)
Aberdeen County Council	12 Months	5,000	197	(5,197)	0	(197)
Total		**14,000**	**77,640**	**(73,640)**	**18,000**	**(640)**

Overnight Investments

The balance of the daily surplus funds can be placed as overnight investments with the Councils bank which is Lloyds. The maximum amount invested with Lloyds in the first three quarters of the financial year was £4.788m. There has been no breach of the £5m limit set in the Treasury Management Strategy. For clarity, this limit relates to the amount invested and doesn't include interest accruing as a result. The interest earned from daily balances up to 31 December 2024 is £77,420.44.

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.

As demonstrated by the liability benchmark in this report, the Authority expects to be a long-term borrower and new treasury investments are therefore primarily made to manage day-to-day cash flows using short-term low risk instruments. The existing portfolio of strategic pooled funds will be maintained to diversify risk into different asset classes and boost investment income.

Bank Rate reduced from 5.25% to 5.00% in August 2024 and again to 4.75% in November 2024 with short term interest rates largely being around these levels. Money Market Rates ranged between 5.25% and 5.25%.

The progression of risk and return metrics are shown in the extracts from Arlingclose's quarterly investment benchmarking in Table 5 below.

Table 5: Investment Benchmarking – Treasury investments managed in-house

	Credit Score	Credit Rating	Bail-in Exposure	Weighted Average Maturity (days)	Rate of Return %
31.03.2024 31.03.2024	5.35	A+	25%	34	5.58
Similar Las/All LAs	4.62	A+	60%	52	4.92

*Weighted average maturity

Statutory override: In April 2023 the Ministry for Housing, Communities and Local Government (MHCLG) published the full outcome of the consultation on the extension of the statutory override on accounting for gains and losses on pooled investment funds. A further consultation on the override was included in MHCLG's annual consultation on the provisional local government finance settlement published in December 2024: the consultation closes on 15th January 2025 with the outcome expecting to be published in February 2025. So far the override has been extended until 31st March 2025; whether the override will be extended beyond this date is unknown but commentary from both consultations suggests an extension is unlikely. The Council has set up a reserve of £0 to mitigate the impact of the statutory override not being extended and unrealised losses on pooled investment funds are required to be recognised.

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

Non-Treasury Investments

The definition of investments in CIPFA's revised 2021 Treasury Management Code covers all the financial assets of the Authority as well as other non-financial assets which the Council holds primarily for financial return. Investments that do not meet the definition of treasury management investments (i.e. management of surplus cash) are categorised as either for service purposes (made explicitly to further service objectives) and or for commercial purposes (made primarily for financial return).

Investment Guidance issued by the Ministry of Housing, Communities and Local Government (MHCLG) and Welsh Government also includes within the definition of investments all such assets held partially or wholly for financial return.

The Council also held £15.853m of such investments in

- Loans to Rykneld Homes Ltd £6.501m
- Loans to Mypad £9.352m

The Council held £21.8m of investments made for commercial purposes

- Directly owned property £21.8m

These investments generated £0.449m of investment income for the Council after taking account of direct costs, representing a rate of return of 2.06% as at 31st December 2024.

Treasury Performance

The Council measures the financial performance of its treasury management activities both in terms of its impact on the revenue budget and its relationship to benchmark interest rates, as shown in table 6 below.

Table 6: Performance

	Actual £m	**Budget £m**	**Over/ under**	**Actual %**	**Benchmark %**	**Over/ under**
PWLB Borrowing	150.5	157.0	Under	3.91	5.69	Under
Total borrowing	150.5	157.0	Under	3.91	5.69	Under
Total debt	150.5	157.0	Under	3.91	5.69	Under
Investments (see table 4)	18.0	10.0	Over	4.74	4.25	Over
Total treasury investments	18.0	10.0	Over	4.74	4.25	Over

MRP Regulations

On 10th April 2024 amended legislation and revised statutory guidance were published on Minimum Revenue Provision (MRP). The majority of the changes take effect from the 2025/26 financial year, although there is a requirement that for capital loans given on or after 7th May 2024 sufficient MRP must be charged so that the outstanding Capital Financing Requirement (CFR) in respect of the loan is no higher than the principal outstanding less the Expected Credit Loss (ECL) charge for that loan.

The regulations also require that local authorities cannot exclude any amount of their CFR from their MRP calculation unless by an exception set out in law. Capital receipts cannot be used to directly replace, in whole or part, the prudent charge to revenue for MRP (there are specific exceptions for capital loans and leased assets).

Compliance

The S151 Officer reports that all treasury management activities undertaken during the quarter complied fully with the principles in the Treasury Management Code and the Council's approved Treasury Management Strategy. Compliance with specific investment limits is demonstrated in table 7 below.

Table 7: Investment Limits

	2024/25 Maximum per counterparty	**31.12.24 Actual**	**2024/25 Limit**	**Complied?**
The UK Government	Unlimited	£0m	n/a	Yes
Local authorities & other government entities	£5m	£0m	Unlimited	Yes
Secured investments	£5m	£0m	Unlimited	Yes
Banks (unsecured)	£5m	£0m	Unlimited	Yes
Building societies (unsecured)	£5m	£0m	£20m	Yes
Registered providers (unsecured)	£5m	£0m	£20m	Yes
Money market funds	£5m	£18.0m	Unlimited	Yes
Strategic pooled funds	£5m	£0m	£20m	Yes
Real Estate Investment Trusts	£5m	£0m	£20m	Yes
Other investments	£5m	£0m	£20m	Yes

Compliance with the Authorised Limit and Operational Boundary for external debt is demonstrated in table 8 below.

Table 8: Debt and the Authorised Limit and Operational Boundary

	Q1 2024/25 Maximum £m	31.12.24 Actual £m	2024/25 Operational Boundary £m	2024/25 Authorised Limit £m	Complied?
Borrowing	157.0	150.5	234.2	239.2	Yes
Total debt	**157.0**	**150.5**	**234.2**	**239.2**	Yes

Since the operational boundary is a management tool for in-year monitoring it is not significant if the operational boundary is breached on occasions due to variations in cash flow, and this is not counted as a compliance failure.

Treasury Management Prudential Indicators

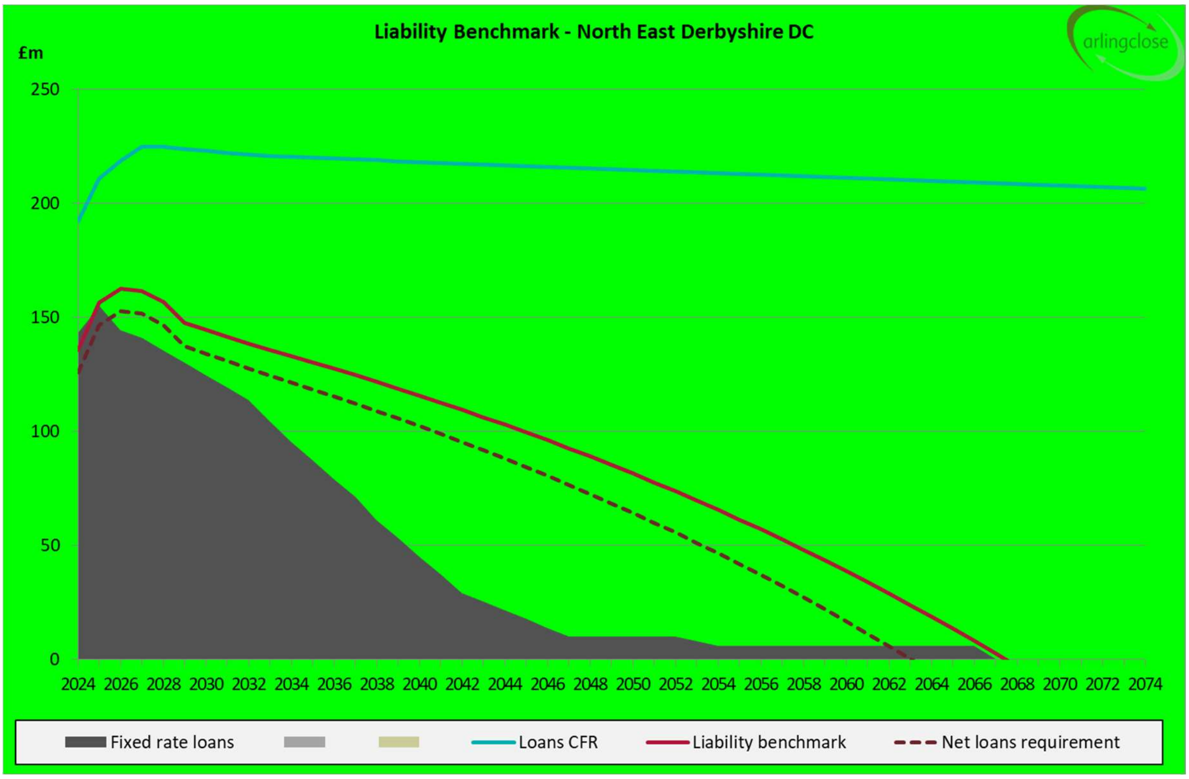
As required by the 2021 CIPFA Treasury Management Code, the Council monitors and measures the following treasury management prudential indicators.

1. Liability Benchmark**:**

This new indicator compares the Council's actual existing borrowing against a liability benchmark that has been calculated to show the lowest risk level of borrowing. The liability benchmark is an important tool to help establish whether the Council is likely to be a long-term borrower or long-term investor in the future, and so shape its strategic focus and decision making. It represents an estimate of the cumulative amount of external borrowing the Council must hold to fund its current capital and revenue plans while keeping treasury investments at the minimum level of £10m required to manage day-to-day cash flow.

	31.3.24 Actual	31.3.25 Forecast	31.3.26 Forecast	31.3.27 Forecast
Loans CFR	199.0	229.2	233.8	236.6
Less: Balance sheet resources	(73.7)	(81.4)	(87.2)	(90.3)
Net loans requirement	**125.3**	**147.8**	**146.6**	**146.3**
Plus: Liquidity allowance	10.0	10.0	10.0	10.0
Liability benchmark	**135.3**	**157.8**	**156.7**	**156.3**
Existing borrowing	**142.8**	**157.0**	**156.0**	**155.9**

Following on from the medium-term forecast above, the long-term liability benchmark assumes capital expenditure funded by borrowing of £18.5m in 2024/25, minimum revenue provision on new capital expenditure based on a 50-year asset life. This is shown in the chart below together with the maturity profile of the Council's existing borrowing.



Whilst borrowing may be above the liability benchmark, strategies involving borrowing which is significantly above the liability benchmark carry higher risk.

2. Maturity Structure of Borrowing**:** This indicator is set to control the Council's exposure to refinancing risk. The upper and lower limits on the maturity structure of all borrowing were:

	Upper Limit	Lower Limit	31.12.24 Actual	Complied?
Under 12 months	20%	0%	0.13%	Yes
12 months and within 24 months	20%	0%	6.51%	Yes
24 months and within 5 years	40%	0%	8.43%	Yes
5 years and within 10 years	40%	0%	21.48%	Yes
10 years and above	90%	0%	63.45%	Yes

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

3. Long-term Treasury Management Investments**:** The purpose of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments. The prudential limits on the long-term treasury management limits are:

	2024/25	2025/26	2026/27	No fixed date
Limit on principal invested beyond year end	£20m	£20m	£20m	£20m
Actual principal invested beyond year end	£0m	£0m	£0m	£0m
Complied?	Yes	Yes	Yes	Yes

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

Additional indicators

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.

	2024/25 Target	31.12.24 Actual	Complied?
Portfolio average credit rating	<3.0	1.00	Yes

Liquidity**:** The Council has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments within a rolling three-month period, without additional borrowing / it can borrow each period without giving prior notice.

	2024/25 Target £m	31.12.24 Actual £m	Complied?
Total cash available within 3 months	10.0	18.0	Yes

Interest Rate Exposures: This indicator is set to control the Council's exposure to interest rate risk.

Interest rate risk indicator	2024/25 Target	31.12.24 Actual	Complied
Upper limit on one-year revenue impact of a 1% rise in interest rates	£1.5m	£0.0m	Yes
Upper limit on one-year revenue impact of a 1% fall in interest rates	(£1.5m)	(£0.0m)	Yes

For context, the changes in interest rates during the half year were:

	31/03/24	31/12/24
Bank Rate	5.25%	4.75%
1-year PWLB certainty rate, maturity loans	5.36%	5.19%
5-year PWLB certainty rate, maturity loans	4.68%	5.10%
10-year PWLB certainty rate, maturity loans	4.74%	5.40%
20-year PWLB certainty rate, maturity loans	5.18%	5.84%
50-year PWLB certainty rate, maturity loans	5.01%	5.66%

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