Appendix C

Treasury Management Strategy

2025/26

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Contents

Introduction

1. Treasury management is the management of the Authority’s cash flows, borrowing and investments, and the associated risks. The Authority 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 financial risk are therefore central to the Authority’s prudent financial management.

2. Treasury risk management at the Authority is conducted within the framework of the Chartered Institute of Public Finance and Accountancy’s Treasury Management in the Public Services: Code of Practice 2021 Edition (the CIPFA Code) which requires the Authority to approve a treasury management strategy before the start of each financial year. This report fulfils the Authority’s legal obligation under the Local Government Act 2003 to have regard to the CIPFA Code.

Economic Background

3. The impact on the UK from the government’s Autumn Budget, slower interest rate cuts, modestly weaker economic growth over the medium term, together with the impact from President-elect Trump’s second term in office and uncertainties around US domestic and foreign policy, will be major influences on the Authority’s treasury management strategy for 2025/26.

4. The Bank of England’s (BoE) Monetary Policy Committee (MPC) reduced Bank Rate to 4.75% at its meeting in November 2024, having previously cut by 25bp from the 5.25% peak at the August MPC meeting. At the November meeting, eight Committee members voted for the cut while one member preferred to keep Bank Rate on hold at 5%.

5. The November quarterly Monetary Policy Report (MPR) is forecasting Gross Domestic Product (GDP) growth to pick up to around 1.75% (four-quarter GDP) in the early period of the BoE’s forecast horizon before falling back. The impact from the Budget pushes GDP higher in 2025 than was expected in the previous MPR, before becoming weaker. Current GDP growth was shown to be 0.5% between April and June 2024, a downward revision from the 0.6% rate previously reported by the Office for National Statistics (ONS).

6. Office for National Statistics (ONS) figures reported the annual Consumer Price Index (CPI) inflation rate at 1.7% in September 2024, down from 2.2% in the previous month and lower than the 1.9% expected. Core CPI also declined further than expected to 3.2% against a forecast of 3.4% and the previous month's 3.6%. The outlook for CPI inflation in the November MPR showed it rising above the MPC's 2% target from 2024 into 2025 and reaching around 2.75% by the middle of calendar 2025. This represents a modest near-term increase due to the ongoing impacts from higher interest rates, the Autumn Budget, and a projected margin of economic slack. Over the medium-term, once these pressures ease, inflation is expected to stabilise around the 2% target.

7. The labour market appears to be easing slowly however, but the data still requires treating with some caution. The latest figures reported the unemployment rate fell to 4.0% in the three months to August 2024, while economic inactivity also declined. Pay growth for the same period was reported at 4.9% for regular earnings (excluding bonuses) and 3.8% for total earnings. Looking ahead, the BoE MPR showed the unemployment rate is expected to increase modestly, rising to around 4.5%, the assumed medium-term equilibrium unemployment rate, by the end of the forecast horizon.

8. The US Federal Reserve has also been cutting interest rates, bringing down the Fed Funds Rate by 0.25% at its November 2024 monetary policy meeting to a range of 4.5%-4.75%. Further interest rate cuts are expected, but uncertainties around the potential inflationary impact of incoming President 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, rising at an annual rate of 2.8% in the third quarter of 2024, and inflation remains elevated suggesting that monetary policy may need to remain more restrictive in the coming months than had previously been anticipated.

9. Euro zone inflation fell below the European Central Bank (ECB) 2% target in September 2024, the first time in over three years. This allowed the ECB to continue its rate cutting cycle and reduce its three key policy rates by 0.25% in October. Inflation is expected to rise again 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.

Credit Outlook

10. Credit Default Swap (CDS) prices have typically followed a general trend downwards during 2024, reflecting a relatively more stable financial period compared to the previous year. Improved credit conditions in 2024 have also led to greater convergence in CDS prices between ringfenced (retail) and non-ringfenced (investment) banking entities again. On an annual basis, CDS price volatility has so far been lower in 2023 compared to 2022, but this year has seen more of a divergence in prices between ringfenced (retail) and non-ringfenced (investment) banking entities once again.

11. Higher interest rates can lead to a deterioration in banks' asset quality through increased loan defaults and volatility in the value of capital investments. Fortunately, the rapid interest rate hikes during this monetary tightening cycle, while putting some strain on households and corporate borrowers, has not caused a rise in defaults, and banks have fared better than expected to date, buoyed by strong capital positions. Low unemployment and robust wage growth have also limited the number of problem loans, all of which are positive in terms of creditworthiness.

12. Moreover, while a potential easing of US financial regulations under a Donald Trump Presidency may aid their banks' competitiveness compared to institutions in the UK and other regions, it is unlikely there will be any material impact on the underlying creditworthiness of the institutions on the counterparty list maintained by Arlingclose, the authority's treasury adviser.

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

Interest rate forecast (November 2024)

14. The Authority's treasury management adviser Arlingclose forecasts that The Bank of England's Monetary Policy Committee will continue reducing rates during 2024 and through 2025, taking Bank Rate to around 3.75% by the end of the 2025/26 financial year. The effect from the Autumn Budget on economic growth and inflation has reduced previous expectations in terms of the pace of rate cuts as well as pushing up the rate at the end of the loosening cycle.

15. Arlingclose expects long-term gilt yields to remain broadly at current levels on average (amid continued volatility), but to end the forecast period modestly lower compared to now. Yields will continue remain relatively higher than in the past, due to quantitative tightening and significant bond supply. As ever, there will be short-term volatility due to economic and (geo)political uncertainty and events.

16. A more detailed economic and interest rate forecast provided by Arlingclose is in **Appendix A**.

17. Like the BoE, the Federal Reserve and other central banks see persistently high policy rates through 2023 and 2024 as key to dampening domestic inflationary pressure. Bond markets will need to absorb significant new supply, particularly from the US government.

18. A more detailed economic and interest rate forecast provided by Arlingclose is in Appendix A.

19. For the purpose of setting the budget, it has been assumed that new treasury investments will be made at an average rate/yield of 4.25% and that new long-term loans will be borrowed at an average rate of 5.0%.

Local context

20. On 30th November 2024, the Authority held £46.5m of borrowing and £28.3m of treasury investments. This is set out in further detail at **Appendix B**. Forecast changes in these sums are shown in the balance sheet analysis in table 1 below.

Table 1: Balance sheet summary and forecast.
CFR and Balance Sheet resources figures are under review and this table will change once the figures have been received.

	31.3.24 Actual £(000)	**31.3.25 Estimate £(000)**	**31.3.26 Forecast £(000)**	**31.3.27 Forecast £(000)**	**31.3.28 Forecast £(000)**
Capital financing requirement	**60,522**	**62,899**	**69,163**	**63,231**	**59,445**
Less: Other debt liabilities *	-	-	-	-	-
Loans CFR	**60,522**	**62,899**	**69,163**	**63,231**	**59,445**
Less: External borrowing **	(46,500)	(60,500)	(66,000)	(60,000)	(53,500)
Internal borrowing	**14,022**	**2,399**	**3,163**	**3,231**	**5,945**
Less: Balance sheet resources	(21,144)	(18,204)	(18,968)	(9,231)	(11,345)
Treasury investments	**7,122**	**15,805**	**15,805**	**6,000**	**5,400**

* Leases and PFI liabilities that form part of the Authority's total debt
** shows only loans to which the Authority is committed and excludes optional refinancing

21. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while balance sheet resources are the underlying sums available for investment. The Authority's current strategy is to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing.

22. The Authority has an increasing CFR due to the capital programme, but with minimal investments and will therefore be required to borrow up to £66.0m over the forecast period.

23. CIPFA's Prudential Code for Capital Finance in Local Authorities recommends that the Authority's total debt should be lower than its highest forecast CFR over the next three years. Table 1 shows that the Authority expects to comply with this recommendation during 2024/25.

Liability Benchmark

24. To compare the Council's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing. This assumes the same forecasts as table 1 above, but that cash and investment balances are kept to a minimum level of £5m at each year-end to maintain sufficient liquidity but minimise credit risk.

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

Table 2: Prudential Indicator: Liability benchmark

	31.3.24 Actual £(000)	**31.3.25 Estimate £(000)**	**31.3.26 Forecast £(000)**	**31.3.27 Forecast £(000)**	**31.3.28 Forecast £(000)**
Loans CFR	**60,522**	**62,899**	**69,163**	**63,231**	**58,857**
Less: Balance sheet resources	(21,144)	(18,204)	(18,968)	(9,231)	(11,345)
Net loans requirement	39,378	44,695	50,195	54,000	47,512
Plus: Liquidity allowance	10,000	5,000	5,000	5,000	5,000
Liability benchmark	**49,378**	**49,695**	**55,195**	**59,000**	**52,512**

CFR and Balance Sheet resources figures are under review and this table will change once the figures have been received.

Following on from the medium-term forecasts in table 2 above, the long-term liability benchmark assumes capital expenditure funded by borrowing of a maximum £51.9m, minimum revenue provision on new capital expenditure based on the Useful Economic Lives of the individual assets ranging from 3 years to 50 years with income, expenditure reserves all increasing by inflation of 2.5% a year.

Borrowing Strategy

26. The Authority currently holds £46.5 million of loans, an increase of £15 million on the previous year, as part of its strategy for funding previous years' capital programmes. The balance sheet forecast in table 1 shows that the Authority expects to borrow up to £60.5m in 2024/25. The Authority may also borrow additional sums to pre-fund future years' requirements, providing this does not exceed the authorised limit for borrowing of £100 million.

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

28. **Strategy:** Given the significant cuts to public expenditure and to local government funding, the Authority's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. With short-term interest rates currently much lower than long-term rates, it is likely to be more cost effective in the short-term to either use internal resources, or to borrow short-term loans instead.

29. By doing so, the Authority is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of short-term borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise modestly. Arlingclose will assist the Authority with this 'cost of carry' and breakeven analysis. Its output may determine whether the Authority borrows additional sums at long-term fixed rates in 2024/25 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.

30. The Authority has previously raised all of its long-term borrowing from the HM Treasury PWLB Lending Facility (PWLB) (formerly the Public

Works Loans Board) but will consider long-term loans from other sources including banks, pension funds and local authorities, and will investigate the possibility of issuing bonds and similar instruments, in order to lower interest costs and reduce over-reliance on one source of funding in line with the CIPFA Code. PWLB loans are no longer available to local authorities planning to buy investment assets primarily for yield; the Authority intends to avoid this activity in order to retain its access to PWLB loans.

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

32. In addition, the Authority may borrow further short-term loans to cover unplanned cash flow shortages.

33. **Sources of borrowing:** The approved sources of long-term and short-term borrowing are:

a. HM Treasury's PWLB Lending Facility (formerly the Public Works Loan Board)
b. National Wealth Fund Ltd (formerly UK Infrastructure Bank Ltd)
c. any institution approved for investments (see below).
d. any other bank or building society authorised to operate in the UK.
e. any other UK public sector body.
f. UK public and private sector pension funds (except the Hertfordshire Local Government Pension Scheme).
g. capital market bond investors.
h. UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues.

34. **Other sources of debt finance:** In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:

a. Leasing.
b. Hire purchase.
c. Private Finance Initiative.
d. Sale and leaseback.
e. Similar asset based finance.

35. **Municipal Bonds Agency:** UK Municipal Bonds Agency plc was established in 2014 by the Local Government Association as an alternative to the PWLB. It issues bonds on the capital markets and lends

the proceeds to local authorities. This is a more complicated source of finance than the PWLB for two reasons: borrowing authorities will be required to provide bond investors with a guarantee to refund their investment in the event that the agency is unable to for any reason; and there will be a lead time of several months between committing to borrow and knowing the interest rate payable. Any decision to borrow from the Agency will therefore be the subject of a separate report to Full Council.

36. **LOBOs:** The Authority holds no 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 Authority has the option to either accept the new rate or to repay the loan at no additional cost. Borrowing via LOBO loans will not be undertaken unless a separate report requesting authority is approved by Full Council.

37. **Short-term and variable rate loans:** These loans leave the Authority exposed to the risk of short-term interest rate rises and are therefore subject to the interest rate exposure limits in the treasury management indicators below. Financial derivatives may be used to manage this interest rate risk (see section below).

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

Treasury Investment Strategy

39. The Authority holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Authority's treasury investment balance has ranged between £28 and £38 million (including long term property investments), these levels are expected to reduce by year end and the forthcoming year, due to the redemptions of the property funds.

40. **Objectives:** The CIPFA Code requires the Authority to invest its treasury funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The

Authority's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income. Where balances are expected to be invested for more than one year, the Authority will aim to achieve a total return that is equal or higher than the prevailing rate of inflation, in order to maintain the spending power of the sum invested. The Authority aims to be a responsible investor and will consider environmental, social and governance (ESG) issues when investing.

41. **Strategy:** As demonstrated by the liability benchmark above, the Authority expects to be a long-term borrower and new treasury investments will therefore be made primarily 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 sectors and boost investment income.

42. The CIPFA Code does not permit local authorities to both borrow and invest long-term for cash flow management. But the Authority may make long-term investments for treasury risk management purposes, including to manage interest rate risk by investing sums borrowed in advance for the capital programme for up to three years; to manage inflation risk by investing usable reserves in instruments whose value rises with inflation; and to manage price risk by adding diversification to the strategic pooled fund portfolio. As a result we are in the process of ending a long term investment of £10 million in the Lothbury Property Fund. The £10 million in the Hermes Property Fund will be held until the redemption restrictions on the fund are lifted in the next few years.

43. **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 Authority's ESG policy does not currently include ESG scoring or other real-time ESG criteria at an individual investment level. When investing in banks and funds, the Authority 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.

44. **Business models:** Under the IFRS 9 standard, the accounting for certain investments depends on the Authority's "business model" for managing them. The Authority aims to achieve value from its treasury investments by a business model of collecting the contractual cash flows and

therefore, where other criteria are also met, these investments will continue to be accounted for at amortised cost.

45. **Approved counterparties:** The Authority may invest its surplus funds with any of the counterparty types in table 3 below, subject to the limits shown.

Table 3: Treasury investment counterparties and limits

Sector	Time limit	Counterparty limit	Sector limit
The UK Government	50 years	Unlimited	n/a
Local authorities & other government entities	3 years	£20m	Unlimited
Secured investments *	3 years	£20m	Unlimited
Banks (unsecured) *	13 months	£20m	Unlimited
Building societies (unsecured) *	13 months	£20m	£60m
Registered providers (unsecured) *	3 years	£5m	£30m
Money market funds *	n/a	£20m	Unlimited
Strategic pooled funds	n/a	£20m	£20m
Real estate investment trusts	n/a	£20m	£20m
Other investments *	3 years	£1m	£5m

This table must be read in conjunction with the notes below.

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

47. For entities without published credit ratings, investments may be made either (a) where external advice indicates the entity to be of similar credit quality; or (b) to a maximum of £500,000 per counterparty as part of a diversified pool e.g. via a peer-to-peer platform.

48. **UK Government:** Sterling-denominated investments with or explicitly guaranteed by the UK Government, including the Debt Management Account Deposit Facility, treasury bills and gilts. These are deemed to be zero credit risk due to the government’s ability to create additional

currency and therefore may be made in unlimited amounts for up to 50 years.

49. **Local Authorities and other Government entities:** Loans to, and bonds and bills issued or guaranteed by, national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is generally a lower risk of insolvency, although they are not zero risk.

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

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

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

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

54. **Strategic pooled funds:** Bond, equity and property funds including exchange traded funds, that offer enhanced returns over the longer term but are more volatile in the short term. These allow the Authority to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date, but can be either withdrawn after a notice period or sold on an exchange, their performance and continued suitability in meeting the Authority's investment objectives will be monitored regularly.

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

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

57. **Operational bank accounts:** The Authority may incur operational exposures, for example though current accounts, collection accounts and merchant acquiring services, to any UK bank with credit ratings no lower than BBB- and with assets greater than £25 billion. These are not classed as investments but are still subject to the risk of a bank bail-in, and balances will therefore be kept below £1 million per bank except the council's banker, Nat West, where the balance will be kept below £20 million. The Bank of England has stated that in the event of failure, banks with assets greater than £25 billion are more likely to be bailed-in than made insolvent, increasing the chance of the Authority maintaining operational continuity.

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

a. no new investments will be made,

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

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

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

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

62. When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2008, 2020 and 2022, this is not generally reflected in credit ratings, but can be seen in other market measures. In these circumstances, the Authority will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the Authority's cash balances, then the surplus will be deposited with the UK Government, or with other local authorities. This will cause investment returns to fall but will protect the principal sum invested.

63. **Investment limits:** The Authority's revenue reserves available to cover investment losses are forecast to be £18 million on 31st March 2025 and £18 million on 31st March 2026. In order that no more than 60% of available reserves will be put at risk in the case of a single default, the maximum that will be lent to any one organisation (other than the UK Government) will be £10 million. A group of entities under the same ownership will be treated as a single organisation for limit purposes.

64. Credit risk exposures arising from non-treasury investments, financial derivatives and balances greater than £10k in operational bank accounts count against the relevant investment limits.

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

Table 4: Additional investment limits

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

66. **Liquidity management:** The Authority uses a spreadsheet-based cash flow forecasting model to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a prudent basis to minimise the risk of the Authority being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Authority's medium-term financial plan and cash flow forecast.

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

Treasury Management Prudential Indicators

68. The Authority measures and manages its exposures to treasury management risks using the following indicators.

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

Credit risk indicator	**Target**
Portfolio average credit score	6.0

70. **Liquidity:** The Authority 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.

Liquidity risk indicator	**Target**
Total cash available within 3 months	£5m

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

Interest rate risk indicator	**Limit**
Upper limit on one-year revenue impact of a 1% <u>rise</u> in interest rates	£640,000
Upper limit on one-year revenue impact of a 1% <u>fall</u> in interest rates	£640,000

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

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

Refinancing rate risk indicator	**Upper limit**	**Lower limit**
Under 12 months	100%	0%
12 months and within 24 months	100%	0%
24 months and within 5 years	50%	0%
5 years and within 10 years	50%	0%

10 years and within 20 years	75%	0%
20 years and within 30 years	75%	0%

74. **Long-term treasury management investments:** The purpose of this indicator is to control the Authority's exposure to the risk of incurring losses by seeking early repayment of its investments. The prudential limits on the long-term treasury management investments will be:

Price risk indicator	**2024/25**	**2025/26**	**2026/27**	**No fixed date**
Limit on principal invested beyond year end	£0m	£0m	£0m	£10m

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

Related Matters

76. The CIPFA Code requires the Authority to include the following in its treasury management strategy.

77. **Financial derivatives:** Local authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk (e.g. interest rate collars and forward deals) and to reduce costs or increase income at the expense of greater risk (e.g. LOBO loans and callable deposits). The general power of competence in section 1 of the Localism Act 2011 removes much of the uncertainty over local authorities' use of standalone financial derivatives (i.e. those that are not embedded into a loan or investment).

78. The Authority will only use standalone financial derivatives (such as swaps, forwards, futures and options) where they can be clearly demonstrated to reduce the overall level of the financial risks that the Authority is exposed to. Additional risks presented, such as credit exposure to derivative counterparties, will be taken into account when determining the overall level of risk. Embedded derivatives, including those present in pooled funds and forward starting transactions, will not be subject to this policy, although the risks they present will be managed in line with the overall treasury risk management strategy.

79. Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria, assessed using the appropriate credit rating for derivative exposures. An allowance for credit risk calculated using the methodology in the Treasury Management Practices document will count against the counterparty credit limit and the relevant foreign country limit.

80. In line with the CIPFA Code, the Authority will seek external advice and will consider that advice before entering into financial derivatives to ensure that it fully understands the implications.

81. **Markets in Financial Instruments Directive (MFID):** The Authority has opted up to professional client status with its providers of financial services, including advisers, banks, brokers and fund managers, allowing it access to a greater range of services but without the greater regulatory protections afforded to individuals and small companies. Given the size and range of the Authority's treasury management activities, the Head of Strategic Finance and Property believes this to be the most appropriate status.

Financial Implications

82. The budget for investment income in 2025/26 is £1.0 million, based on an average investment portfolio of £24.0 million at an interest rate of 4.25%. The budget for debt interest paid in 2025/26 is £3.3 million, based on an average debt portfolio of £65.0 million at an average interest rate of 5.0%. If actual levels of investments and borrowing, or actual interest rates, differ from those forecasts, performance against budget will be correspondingly different.

83. Where investment income exceeds budget, e.g. from higher risk investments including pooled funds, or debt interest paid falls below budget, e.g. from cheap short-term borrowing, then [50%] of the revenue savings will be transferred to a treasury management reserve to cover the risk of capital losses or higher interest rates payable in future years.

Appendix A - Arlingclose Economic & Interest Rate Forecast

Underlying assumptions:

- As expected, the Bank of England Monetary Policy Committee (MPC) cut Bank Rate to 4.75% in November in an 8-1 vote. However, the outlook for monetary policy has changed following the new government's fiscal plans, as delivered in the recent Budget.
- The Budget contained measures that will boost demand, in a constrained supply environment, while pushing up direct costs for employers. The short to medium-term inflationary effects of the Budget require a change to our Interest Rate Forecast.
- UK GDP recovered well in H1 2024 from technical recession, but underlying growth appears relatively subdued. However, the Budget will significantly boost government spending over the short-term, with few offsetting measures to subdue household demand, so GDP growth is likely to rise relatively steeply.
- Private sector wage growth has eased to 4.8% yet remains high, while services inflation continues to hold above pre-pandemic levels. The increase in employers' NICs, minimum and public sector wage levels could have wide ranging impacts on private sector employment demand and costs, but the near-term impact will likely be inflationary as these additional costs get passed to consumers.
- CPI inflation was below the 2% target in September but will rise a little by year-end as energy price declines from the previous year fall out of the annual comparison. The Bank of England (BoE) estimates the Budget impact will see the CPI rate at 2.7% by year end 2025 and remain over target in 2026, as opposed to the prior projection of inflation easing back to and then below target by this point.
- The MPC re-emphasised the gradual move to easing monetary policy, and we now believe the Budget measures have both reduced the pace of Bank Rate cuts and increased the low for this loosening cycle (although downside risks remain in the medium term).
- The increase in borrowing, rise in inflation and shallower path for Bank Rate projected by the Office for Budget Responsibility (OBR) raised gilt yields. The material change in rate expectations means that yields will be generally higher in the post-Budget world.

- US government yields have risen following Donald Trump's and Republican victories in the US elections. Trump has run on a platform of policies that appear inflationary, calling into question the extent of policy loosening required from the Federal Reserve (which was already uncertain given continued solid US growth data). Higher US yields could also support higher UK yields.

Forecast:

- In line with our forecast, Bank Rate was cut to 4.75% in November 2024.
- The MPC will continue to lower Bank Rate to reduce the restrictiveness of monetary policy, but more slowly and to a higher level. We see another rate cut in February 2025, followed by one cut per quarter, in line with Monetary Policy Report publication, to a low of 3.75%.
- Long-term gilt yields have risen to reflect both UK and US economic, monetary and fiscal policy expectations, and increases in bond supply. Volatility is likely to remain elevated as the market digests incoming data for clues around the impact of policy changes.
- This uncertainty may also necessitate more frequent changes to our forecast than has been the case recently.
- Upside risks to inflation over the next 12 months could limit the extent of monetary easing, but we see the risks as broadly balanced over the medium term.

	Current	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27	Jun-27	Sep-27
Official Bank Rate													
Upside risk	0.00	0.00	0.25	0.50	0.50	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75
Central Case	4.75	4.75	4.50	4.25	4.00	3.75	3.75	3.75	3.75	3.75	3.75	3.75	3.75
Downside risk	0.00	0.00	-0.25	-0.25	-0.50	-0.50	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75
3-month money market rate													
Upside risk	0.00	0.00	0.25	0.50	0.50	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75
Central Case	4.95	4.80	4.60	4.35	4.10	3.90	3.85	3.85	3.85	3.85	3.85	3.85	3.85
Downside risk	0.00	0.00	-0.25	-0.25	-0.50	-0.50	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75
5yr gilt yield													
Upside risk	0.00	0.60	0.70	0.80	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Central Case	4.30	4.20	4.10	4.05	3.95	3.90	3.90	3.90	3.95	4.00	4.05	4.05	4.05
Downside risk	0.00	-0.40	-0.50	-0.60	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65
10yr gilt yield													
Upside risk	0.00	0.60	0.70	0.80	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Central Case	4.41	4.40	4.35	4.35	4.35	4.30	4.30	4.30	4.35	4.35	4.35	4.35	4.35
Downside risk	0.00	-0.40	-0.50	-0.60	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65
20yr gilt yield													
Upside risk	0.00	0.60	0.70	0.80	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Central Case	4.84	4.80	4.75	4.70	4.65	4.65	4.65	4.65	4.65	4.65	4.65	4.65	4.65
Downside risk	0.00	-0.40	-0.50	-0.60	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65
50yr gilt yield													
Upside risk	0.00	0.60	0.70	0.80	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Central Case	4.35	4.50	4.45	4.40	4.35	4.35	4.35	4.35	4.35	4.35	4.35	4.35	4.35
Downside risk	0.00	-0.40	-0.50	-0.60	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65

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

Appendix B – Existing Investment & Debt Portfolio Position

	30/12/2024 **Actual portfolio** **£m**	30/12/2024 **Average rate %**
External borrowing:		
Public Works Loan Board	**1.5**	**8.875%**
Local authorities	**45.0**	**4.020%**
LOBO loans from banks	**-**	**-**
Other loans	**-**	**-**
Total external borrowing	**46.5**	
Other long-term liabilities:		
Private Finance Initiative	-	-
Leases	-	-
Transferred Debt	-	-
Total other long-term liabilities	-	
Total gross external debt	**46.5**	
Treasury investments:		
The UK Government		
Local authorities		
Other government entities		
Secured investments		
Banks (unsecured)	7.0	5.140%
Building societies (unsecured)		
Registered providers (unsecured)		
Money market funds	5.6	5.240%
Strategic pooled funds		
Real estate investment trusts		
Other investments	17.8	3.405%
Total treasury investments		
Net debt	**16.1**	

Appendix C – Treasury Management Scheme of Delegation

Full Council

1. Receiving and reviewing reports on treasury management policies, practices and activities.
2. Approval of annual strategy.

Executive

1. Approval of/amendments to the organisation's adopted clauses, treasury management policy statement and treasury management practices.
2. Budget consideration and approval.
3. Approval of the division of responsibilities.
4. Receiving and reviewing regular monitoring reports and acting on recommendations.
5. Approving the selection of external service providers and agreeing terms of appointment.

Audit & Governance Committee

1. Reviewing the treasury management policy and procedures and making recommendations to the responsible body.
2. Receiving and reviewing reports on treasury management policies, practices and activities

Appendix D – The Treasury Management Role of the Section 151 Officer

1. Recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance.
2. Submitting regular treasury management policy reports.
3. Submitting budgets and budget variations.
4. Receiving and reviewing management information reports.
5. Reviewing the performance of the treasury management function.
6. Ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function.
7. Ensuring the adequacy of internal audit, and liaising with external audit.
8. Recommending the appointment of external service providers.
9. Preparation of a Capital Strategy to include capital expenditure, capital financing, non-financial investments and treasury management, with a long-term timeframe.
10. Ensuring that the Capital Strategy is prudent, sustainable, affordable and prudent in the long term and provides value for money.
11. 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.
12. Ensure that the Authority has appropriate legal powers to undertake expenditure on non-financial assets and their financing.
13. 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.
14. 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.

15. Provision to members of a schedule of all non-treasury investments including material investments in subsidiaries, joint ventures, loans and financial guarantees.

16. Ensuring that members are adequately informed and understand the risk exposures taken on by the Authority.

17. Ensuring that the Authority has adequate expertise, either in house or externally provided, to carry out the above

18. Creation of Treasury Management Practices which specifically deal with how non treasury investments will be carried out and managed, to include the following (TM Code p54): -

    a. Risk management (TMP1 and schedules), including investment and risk management criteria for any material non-treasury investment portfolios.

    b. Performance measurement and management (TMP2 and schedules), including methodology and criteria for assessing the performance and success of non-treasury investments.

    c. 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.

    d. Reporting and management information (TMP6 and schedules), including where and how often monitoring reports are taken.

    e. Training and qualifications (TMP10 and schedules), including how the relevant knowledge and skills in relation to non-treasury investments will be arranged.