

## Treasury Management Strategy for 2023/24

The strategy for 2023/24 covers two main areas:

### **Capital Issues**

- the capital expenditure plans and the associated prudential indicators;
- the Minimum Revenue Policy (MRP) in Appendix 4

### **Treasury Management Issues**

- the current treasury position;
- treasury indicators which will limit the treasury risk and activities of the Council;
- prospects for interest rates;
- the borrowing strategy;
- policy on borrowing in advance of need;
- debt rescheduling;
- the investment strategy;
- creditworthiness policy; and
- policy on the use of external service providers.

These elements cover the requirements of the Local Government Act 2003, DLUHC Investment Guidance, DLUHC MRP Guidance, the CIPFA Prudential Code and the CIPFA Treasury Management Code.

### **Capital issues**

#### **The Capital Prudential Indicators 2023/24 – 2025/26 (See Table 1 in Appendix 2)**

The Council's capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in the prudential indicators, which are designed to assist members' overview and confirm capital expenditure plans.

**Capital Expenditure.** This prudential indicator is a summary of the Council's capital expenditure plans, both those agreed previously, and those forming part of this budget cycle.

The table below summarises the capital expenditure plans and how these plans are being financed by capital or revenue resources. Any shortfall of resources results in a funding need (borrowing).

<b>Table 1 Capital Expenditure</b>	<b>2021/22 Actual £000</b>	<b>2022/23 Revised Estimate £000</b>	<b>2023/24 Estimate £000</b>	<b>2024/25 Estimate £000</b>	<b>2025/26 Estimate £000</b>
Programmed Spend	33,504	19,956	41,535	18,066	7,133
<b>Financed by:</b>					
Capital receipts	1,218	2,305	2,547	1,607	1,462
3rd Party Contributions	159	512	5,007	544	715
Capital grants	8,674	10,923	17,518	9,799	2,954
Revenue	191	1,855	1,062	282	198
<b>Net borrowing need for the year</b>	<b>23,262</b>	<b>4,361</b>	<b>15,401</b>	<b>5,834</b>	<b>1,804</b>

## Ratio of Financing Costs to Net Revenue Streams

This indicator shows the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) expressed as a percentage against the net revenue stream. Table 1 in Appendix 2 shows there is a general trend that financing costs are taking up a higher percentage of the revenue budget. This is due to forecast reductions in future aggregate external funding based on 'revenue spending power' for the Council through reduced Government grant, together with increased borrowing costs to fund the council's capital programme.

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

This prudential indicator is the Council's Capital Financing Requirement (CFR). The CFR is simply the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's underlying borrowing need. Any capital expenditure above, which has not immediately been paid for, will increase the CFR and is represented by the net financing need for the year line. The Council's CFR is shown in Table 1 of Appendix 2 and below.

The CFR does not increase indefinitely, as the MRP is a statutory annual revenue charge which broadly reduces the borrowing need in line with each assets life, and so charges the economic consumption of capital assets as they are used.

<b>Table 2</b>	<b>2021/22 Actual £000</b>	<b>2022/23 Revised Estimate £000</b>	<b>2023/24 Estimate £000</b>	<b>2024/25 Estimate £000</b>	<b>2025/26 Estimate £000</b>
<b>Capital Financing Requirement</b>					
Total CFR at 31 <sup>st</sup> March	63,913	66,506	80,097	84,073	83,840
<b>Net financing need for the year</b>	<b>23,239</b>	<b>2,593</b>	<b>13,591</b>	<b>3,976</b>	<b>(233)</b>

<b>£m</b>	<b>2021/22 Actual £000</b>	<b>2022/23 Revised Estimate £000</b>	<b>2023/24 Estimate £000</b>	<b>2024/25 Estimate £000</b>	<b>2025/26 Estimate £000</b>
<b>Movement in CFR represented by</b>					
Net borrowing need for the year (Table 1 above)	23,262	4,361	15,401	5,834	1,804
Less MRP and other financing movements	(1,023)	(1,768)	(1,810)	(1,858)	(2,037)
<b>Movement in CFR in Year</b>	<b>22,239</b>	<b>2,593</b>	<b>13,591</b>	<b>3,976</b>	<b>(233)</b>

## Liability Benchmark

A new prudential indicator for 2023/24 is the Liability Benchmark (LB). The council is required to estimate and measure the LB for the forthcoming financial year and the following two financial years, as a minimum.

## Appendix 1

There are four components to the LB: -

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

The table below summarises the council's Liability Benchmark as at the end of the last financial year and estimates for the current and next three years, and shows that the council is consistently under its liability benchmark. This means that the council is maintaining an underborrowed position, which is prudent whilst interest rates for borrowing are high, but also indicates that future borrowing may be required in order to fund the council's capital programme or to repay debt.

<b>Table 3 Liability Benchmark</b>	<b>2021/22 Actual £000</b>	<b>2022/23 Revised Estimate £000</b>	<b>2023/24 Estimate £000</b>	<b>2024/25 Estimate £000</b>	<b>2025/26 Estimate £000</b>
Existing Loan Debt Outstanding	61,146	59,525	56,118	53,522	52,906
Loans CFR	63,913	66,506	80,097	84,073	83,840
Net Loans Required	20,930	31,067	45,214	49,759	50,106
Liability Benchmark	61,146	64,067	78,214	82,759	83,106
<b>(Over)/Under Liability Benchmark</b>	<b>0</b>	<b>4,542</b>	<b>22,096</b>	<b>29,237</b>	<b>30,200</b>

### Treasury Management Issues

The capital expenditure plans set out above, provide details of the activity of the Council. The treasury management function ensures that the Council's cash is organised within the relevant professional codes, so that sufficient cash is available to meet these activities. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of appropriate borrowing facilities. The strategy covers the relevant treasury/prudential indicators, the current and projected debt positions and the annual investment strategy.

### The Council's Current Portfolio Position

Within the prudential indicators in Appendix 2 there are a number of key indicators to ensure that the Council operates its activities within well-defined limits. One of these is that the Council needs to ensure that its gross debt does not, except in the short term, exceed the

## Appendix 1

total of the CFR in the preceding year plus the estimates of any additional CFR for 2023/24 and the following two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue or speculative purposes. In the Council's case, the estimated external debt at 31<sup>st</sup> March 2023 of £65m is less than the CFR which ranges from £66.5m to £84.1m and means that the Council 'borrows internally' (using reserves and balances) to finance past capital spending as this tends to be cheaper than external debt.

### **Treasury Limits for 2023/24 to 2025/26**

It is a statutory duty under Section 3 of the Act and supporting regulations, for the Council to determine and keep under review how much it can afford to borrow. The amount so determined is termed the "Authorised Borrowing Limit".

The Council must have regard to the Prudential Code when setting the Authorised Limit, which essentially requires it to ensure that total capital investment remains within sustainable limits and, in particular, that the impact upon its future council tax levels is 'acceptable'.

Whilst termed an "Affordable Borrowing Limit", the capital plans to be considered for inclusion incorporate financing by both external borrowing and other forms of liability, such as credit arrangements. The Authorised Limit is to be set, on a rolling basis, for the forthcoming financial year and two successive financial years, details of the Authorised Limit can be found in Table 2 in Appendix 2 of this report outlining the prudential and treasury indicators for 2023/24 – 2025/26.

**The Operational Boundary** is the limit beyond which external debt is not normally expected to exceed and is normally similar to the CFR. It is proposed to set this at 10% above the CFR.

**The Authorised Limit** is a further key indicator representing a control on the maximum level of borrowing, beyond which external debt is prohibited, and this limit needs to be set or revised by the Full Council. It reflects the level of external debt which, whilst not desired, could be afforded in the short term, but is not sustainable in the longer term. It is proposed to set this at 10% above the operational boundary and includes provision for 'unusual cash movements'.

### **IFRS16 – Leased Assets**

The CIPFA LASAAC, Local Authority Accounting Code Board has deferred the implementation of IFRS16 until the 2024/25 financial year.

A requirement for closing of the council's accounts for 2023/24 is therefore to bring operational leased assets onto the balance sheet. This will have the effect of increasing the council's CFR, External Debt, Authorised Limit and Operational Boundary. The Authorised Limit and Operational Boundary may therefore need to be amended mid-year, once the detailed impact is known.

### **Prospects for Interest Rates (Provided by Link Asset Services)**

Part of the service provided by Link Asset Services is to assist the Council to formulate a view on interest rates and the table below gives Link Asset Services forecast.

## Appendix 1

Link Group Interest Rate View	19.12.22												
	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25
BANK RATE	3.50	4.25	4.50	4.50	4.50	4.00	3.75	3.50	3.25	3.00	2.75	2.50	2.50
3 month ave earnings	3.60	4.30	4.50	4.50	4.50	4.00	3.80	3.30	3.00	3.00	2.80	2.50	2.50
6 month ave earnings	4.20	4.50	4.60	4.50	4.20	4.10	3.90	3.40	3.10	3.00	2.90	2.60	2.60
12 month ave earnings	4.70	4.70	4.70	4.50	4.30	4.20	4.00	3.50	3.20	3.10	3.00	2.70	2.70
5 yr PWLB	4.20	4.20	4.20	4.10	4.00	3.90	3.80	3.60	3.50	3.40	3.30	3.20	3.10
10 yr PWLB	4.30	4.40	4.40	4.30	4.10	4.00	3.90	3.80	3.60	3.50	3.40	3.30	3.30
25 yr PWLB	4.60	4.60	4.60	4.50	4.40	4.20	4.10	4.00	3.90	3.70	3.60	3.50	3.50
50 yr PWLB	4.30	4.30	4.30	4.20	4.10	3.90	3.80	3.70	3.60	3.50	3.30	3.20	3.20

Our central forecast for interest rates was updated on 19 December and reflected a view that the MPC would be keen to further demonstrate its anti-inflation credentials by delivering a succession of rate increases. Bank Rate stands at 3.5% currently but is expected to reach a peak of 4.5% in Q1 2023.

Further down the road, we anticipate the Bank of England will be keen to loosen monetary policy when the worst of the inflationary pressures are behind us – but that timing will be one of fine judgment: cut too soon, and inflationary pressures may well build up further; cut too late and any downturn or recession may be prolonged.

The CPI measure of inflation looks to have peaked at 11.1% in Q4 2022 (currently 10.7%). Despite the cost-of-living squeeze that is still taking shape, the Bank will want to see evidence that wages are not spiralling upwards in what is evidently a very tight labour market. Regarding the plan to sell £10bn of gilts back into the market each quarter (Quantitative Tightening), this has started and will focus on the short, medium and longer end of the curve in equal measure, now that the short-lived effects of the Truss/Kwarteng unfunded dash for growth policy are behind us.

In the upcoming months, our forecasts will be guided not only by economic data releases and clarifications from the MPC over its monetary policies and the Government over its fiscal policies, but the on-going conflict between Russia and Ukraine. (More recently, the heightened tensions between China/Taiwan/US also have the potential to have a wider and negative economic impact.)

On the positive side, consumers are still estimated to be sitting on over £160bn of excess savings left over from the pandemic so that will cushion some of the impact of the above challenges. However, most of those are held by more affluent people whereas lower income families already spend nearly all their income on essentials such as food, energy and rent/mortgage payments.

### PWLB RATES

- The yield curve movements have become less volatile of late and PWLB 5 to 50 years Certainty Rates are, generally, in the range of 4.10% to 4.80%.
- We view the markets as having built in, already, nearly all the effects on gilt yields of the likely increases in Bank Rate and the elevated inflation outlook.

### The Borrowing Strategy

The Council is currently maintaining an under-borrowed position which means that the capital borrowing need (the CFR), has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary

## Appendix 1

measure. This strategy is prudent as medium and longer dated borrowing rates are expected to fall from their current levels once prevailing inflation concerns are addressed by tighter near-term monetary policy. That is, Bank Rate increases over the remainder of 2022 and the first half of 2023.

The Head of Finance & Property will monitor interest rates and adopt a pragmatic approach to changing circumstances:

- if it was felt that there was a significant risk of a sharp fall in borrowing rates, then long term borrowings will be postponed,
- if it was felt that there was a significant risk of a much sharper rise than that currently forecast, then the portfolio will be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.
- will take a view on prevailing and perceived future interest rates and take decisions on whether to borrow longer-term or short-term accordingly whenever a borrowing requirement arises. As well as taking a view on the appropriate mix of fixed and variable interest rate exposure in the light of prevailing and perceived future market conditions.
- undertake a constant review of the Council's total external debt portfolio to determine the scope for any restructuring possibilities and make recommendations to Full Council accordingly.

### **The Borrowing Policy and Borrowing Requirement**

The Council will not borrow more than or in advance of its need purely in order to profit from the investment of the extra sums borrowed.

The Council's maximum borrowing requirement (Authorised Limit for external debt) is £96.918m next year. This is limited to 10% above the operational boundary of £88.107m, which has been set at 10% above the CFR.

Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through the mid-year or annual reporting mechanism.

### **Debt Rescheduling**

Rescheduling of current borrowing in our debt portfolio is unlikely to occur as there is still a very large difference between premature redemption rates and new borrowing rates.

The reasons for any rescheduling to take place will include: -

- the generation of cash savings and / or discounted cash flow savings
- helping to fulfil the treasury strategy;
- enhance the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

Consideration will also be given to identify if there is any residual potential left for making savings by running down investment balances to repay debt prematurely as short term rates on investments are likely to be lower than rates paid on current debt.

All rescheduling will be reported to the Council at the earliest meeting following its action.

### **New Financial Institutions as a source of borrowing**

Currently the PWLB Certainty Rate is set at gilts plus 80 basis points. However, consideration may still need to be given to sourcing funding from the following sources:

- Local Authorities (primarily shorter date maturities)
- Financial Institutions (primarily insurance companies and pension funds but also some banks, out of forward dates where the objective is to avoid a cost of carry or to achieve refinancing certainty over the next few years)
- Municipal Bonds Agency (possibly still a viable alternative depending on market circumstances prevailing at the time)

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

### **Annual Investment Strategy**

#### **Investment Policy – management of risk**

The Council's investment policy has regard to the following;

- DLUHC's Guidance on Local Government Investments ("The Guidance")
- CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2021 ("The Code")
- CIPFA Treasury Management Guidance Notes 2021

The Council's deposit priorities focus on;

- Security of Capital
- Liquidity, and
- Yield

The Council will aim to achieve optimum return [yield] on deposits commensurate with proper levels of security and liquidity.

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

The above guidance from the DLUHC and CIPFA places a high priority on the management of risk. This council has adopted a prudent approach to managing risk and defines its risk appetite by the following means: -

1. Minimum acceptable credit criteria are applied in order to generate a list of highly creditworthy counterparties. This also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the short-term and long-term ratings.

2. Other information: ratings will not be the sole determinant of the quality of an institution; it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of

## Appendix 1

the markets. To achieve this consideration the Authority will engage with its advisors to maintain a monitor on market pricing such as “credit default swaps” and overlay that information on top of the credit ratings.

3. Other information sources used will include the financial press, share price and other such information pertaining to the financial sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.

4. The council has defined the list of types of investment instruments that the treasury management team are authorised to use, together with lending and transaction limits. These are set out in appendix 3 to this report.

The council will also pursue value for money in treasury and will monitor yield from investment income against appropriate benchmarks for investment performance. Regular monitoring of investment performance will be carried out during the year.

### Monitoring Performance:

The council has retained HSBC UK Bank plc as the provider for administering the Council’s banking facilities [contract renewed in December 2021 for a three-year term]. The Council continues to have a ‘sweep’ facility for our current account. This means that if we do not deposit monies with other counterparties but leave the balance with HSBC, they will automatically transfer the money into an interest earning deposit account. This account is effectively a call account whereby we can get the money back instantly if required. The current rate the Council is achieving on these deposits is in line with that achieved with other counterparties.

### Approved list of Counterparties for Deposits

There are strict limits in terms of the type of institution with which funds may be deposited and the length of time funds can be invested for.

As part of the Treasury Policy Statement, as a minimum, the approved list of counterparties is reviewed annually and reported to Council. The current list was approved by Full Council on 23 February 2022 and there are no proposed changes for 2023/24. Any changes arising during the year requiring approval will be reported as appropriate.

It is proposed that the maximum amount that can be deposited with other counterparties for a period exceeding 364 days and up to 2 years remains limited to £4m which is shown in Appendix 3.

### Creditworthiness Policy

This Council uses the creditworthiness service provided by Link Asset Services. This service uses a sophisticated modelling approach with credit ratings from all three rating agencies – Fitch, Moodys and Standard and Poors, forming the core element. However, it does not rely solely on the current credit ratings of counterparties but also uses the following as overlays: -

- credit watches and credit outlooks from credit rating agencies
- Credit Default Swaps (CDS) spreads to give early warning of likely changes in credit ratings



## Appendix 1

- sovereign ratings to select counterparties from only the most creditworthy countries

This modelling approach combines credit ratings, credit watches, credit outlooks and CDS spreads in a weighted scoring system for which the end product is a series of colour code bands which indicate the relative creditworthiness of counterparties. These colour codes are also used by the Council to determine the duration for investments and are therefore referred to as durational bands. The Council is satisfied that this service gives a much improved level of security for its investments. It is also a service which the Council would not be able to replicate using in house resources.

The Council is alerted to changes to ratings of all three agencies through its use of the Link Asset Services' creditworthiness service.

- If a downgrade results in the counterparty/investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.

In addition to the use of Credit Ratings the Council will be advised of information on:

- movements in CDS against the iTraxx benchmark and other market data on a daily basis via its Passport website, provided exclusively to it by Link Asset Services. Extreme market movements may result in downgrade of an institution or removal from the Councils lending list.

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

### **Creditworthiness**

Significant levels of downgrades to Short and Long-Term credit ratings have not materialised since the crisis in March 2020. In the main, where they did change, any alterations were limited to Outlooks. However, more recently the UK sovereign debt rating has been placed on Negative Outlook by the three major rating agencies in the wake of the Truss/Kwarteng unfunded tax-cuts policy. Although the Sunak/Hunt government has calmed markets, the outcome of the rating agency reviews is unknown at present, but it is possible the UK sovereign debt rating will be downgraded. Accordingly, when setting minimum sovereign debt ratings, this council will not set a minimum rating for the UK.

### **Investment Strategy**

**In-house funds.** Investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (i.e., rates for investments up to 12 months). Greater returns are usually obtainable by investing for longer periods. The current shape of the yield curve suggests that is the case at present, but there is the prospect of Bank Rate peaking in the first half of 2023 and possibly reducing as early as the latter part of 2023 so an agile investment strategy would be appropriate to optimise returns.

Accordingly, while most cash balances are required in order to manage the day to day cash flow requirements, where cash sums can be identified that could be invested for longer periods, the value to be obtained from longer-term investments will be carefully assessed.

### **Investment Performance**

The council will use an investment benchmark to assess the investment performance of its investment portfolio.

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

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

### **Policy on the use of treasury management consultants**

The Council uses Link Asset Services, Treasury Solutions as its external treasury management advisors.

The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers.

It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Head of Finance & Property through recommendations to Full Council, will ensure that the terms of their appointment and the methods by which their value will be assessed, are properly agreed and documented, and will be subject to regular review.