Report to Council

Date: 21 February 2024

Title: **Treasury Management Strategy 2024-25 to 2026-27**

Cabinet Member(s): Cllr John Chilver - Cabinet Member for Accessible Housing and Resources and Cllr Tim Butcher - Deputy Cabinet Member for Resources and Human Resources

Contact officer: Hasina Shah

Ward(s) affected: Not Applicable

Recommendations: **Council approves the Council's Treasury Management Strategy Statement (TMSS) for 2024/25 including**

1. The Treasury Management Strategy Statement (TMSS);
2. The Borrowing Strategy as set out in Section 4;
3. The Prudential Indicators (PI) set out in Sections 3, 4 and 5;
4. The Annual Investment Strategy set out in Appendix 1; and
5. The Minimum Revenue Provision Policy set out in Appendix 2.

Reason for recommendation: To ensure that the Council's borrowing and investment plans are prudent, affordable and sustainable and comply with statutory requirements.

1. Executive summary

1.1 The Local Government Act 2003 ("the Act") and the Regulations made under the Act require the Council to have regard to the Prudential Code for Capital Finance in Local Authorities and to set Prudential Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable.

1.2 The Act also requires the Council to set out a statement of its treasury management strategy for borrowing and to prepare an Annual Investment Strategy (AIS) (as shown in Appendix 1). This sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments. The Treasury Management Strategy Statement and Annual Investment Strategy must both have regard to guidance issued by the Department for Levelling Up, Housing and Communities (DLUHC) and must be agreed by Full Council.

1.3 Treasury management at the Council 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 Council to approve a treasury management strategy before the start of each financial year. This report fulfils the Council's legal obligation under the Local Government Act 2003 to have regard to the CIPFA Code.

1.4 The Investment Strategy is considered separately within the Capital Investment Strategy. The TMSS and AIS form part of the Council's overall budget setting and financial framework.

2. Background Information

2.1 The Council is required to operate a balanced budget, which broadly means that monies received during the year will meet payments expenditure. The function of treasury management is to ensure that the Council's capital programme and corporate investment plans are adequately funded, and the cashflow is adequately planned, with cash being available when it is needed to discharge the Council's legal obligations and deliver Council services. Surplus monies are invested to obtain an optimal return, while ensuring security of capital and liquidity.

2.2 The CIPFA code defines treasury management as "the management of the local authority's borrowing, investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

2.3 The primary requirements of the Treasury Management Code are summarised below:-

- Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.
- Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.
- Receipt by the full Council of an annual **TMS** (this report) - including the AIS and Minimum Revenue Provision Policy - for the year ahead, a Mid-year Review

Report and an Annual Report (stewardship report) covering activities during the previous year.

- Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions. At Buckinghamshire, this responsibility is delegated to the Director of Finance (S151 Officer).
- Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body. In Buckinghamshire, the delegated body is the Audit and Governance Committee.
- Day to day treasury investment and borrowing activity in undertaken by the Treasury Team in accordance with strategy, policy, practices and procedures.
- **Training** - The S151 officer has the responsibility to ensure that Officers executing treasury function and Members with responsibility for making treasury management decisions and for scrutinising treasury functions receive adequate training. These training needs are met through: -
    - Annual training session delivered by Link (advisor) for both Members and Officers; and
    - Officers training needs are reviewed periodically as part of the Learning and Development programme and attend various seminars, training sessions and conferences organised by CIPFA and Local Authority Treasurers Investment Forum.

2.4 The TMSS covers three main areas summarised below:-

Capital

- Capital spending plans (Prudential Indicator 1)
- Capital Finance Requirement (CFR) (Prudential Indicator 2 & 3)
- Affordability (Prudential Indicator 4)
- Minimum Revenue Provision (MRP)

Borrowing

- Borrowing strategy
- Sources of Borrowing
- Liability benchmark
- Limits on Borrowing Activity
- Maturity structure of borrowing
- Policy on borrowing in advance of need
- Debt rescheduling
- Investing primarily for yield

Managing cash balances

- The current cash position and cash flow forecast
- Prospects for investment returns
- Balancing short and long term investments

2.5 The AIS at Appendix 1 provides more detail on how the Council’s surplus cash investments are to be managed in 2024/25.

3. Capital

Capital Spending Plans (Prudential Indicator 1)

3.1 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. Table 1 summarises the Council's capital expenditure plans, both in terms of those projects agreed previously, and those forming part of the current budget cycle.

Table 1 - PI 1 Capital Expenditure £m	2022/23 Actual	2023/24 Forecast	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate
Total Capital Expnditure	**107.4**	**118.3**	**248.7**	**187.7**	**139.3**
Funding £m					
Capital receipts	24.2	3.0	29.1	24.1	28.0
Capital grants	80.5	94.4	177.1	133.3	93.1
Capital reserves	0.2	8.2	13.9	6.2	11.5
Revenue		8.7	3.7	4.5	5.6
Net financing need	**2.5**	**4.0**	**24.9**	**19.6**	**1.1**

Capital Financing Requirements (CFR) (Prudential Indicator 2 & 3)

3.2 The CFR measures the extent to which capital expenditure has not yet been financed from either Revenue or Capital resources. This indicator is essentially a measure of indebtedness and therefore a guide as to the Council's underlying borrowing needs. Any capital expenditure which has not been immediately financed or paid for will increase the CFR.

3.3 The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual revenue charge which broadly reduces the indebtedness in line with each asset's life, and so charges the economic consumption of capital assets as they are used.

3.4 **Table 2** shows that the CFR will increase when the borrowing increases to fund the capital programme. Consequently, the capital financing charge to revenue will increase, reflecting the capital spending plans.

Table 2 - PI 2 - CFR £m	2022/23 Actual	2023/24 Forecast	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate
CFR as at 01 April	571	562	554	566	573
Net financing need	2	4	25	20	1
Less MRP	-11	-12	-13	-13	-14
CFR as at 31 March	**562**	**554**	**566**	**573**	**560**

3.5 CIPFA's Prudential Code for Capital Finance in Local Authorities recommends that the Council's total debt should be lower than its highest forecast CFR over the next three years. Table 3 on the next page shows that the Council expects to comply with this recommendation during 2024/25 and the next two years. The under-borrowing

position allows some flexibility for limited early borrowing for future years to take advantage of potential favourable interest rates and it evidences that borrowing is not undertaken for revenue purposes.

Table 3 - PI 3 - Debt Vs CFR £m	2022/23	2023/24	2024/25	2025/26	2026/27
	Actual	Forecast	Estimate	Estimate	Estimate
Debt as at March	293	286	264	256	259
Externalisation of internal borrowing and ref	0	0	0	25	20
Borrowing	293	286	264	281	279
Finance Lease	4	4	4	4	4
Total Borrowing	297	290	268	285	283
Capital Financing Requirement	562	554	566	573	560
Under/(Over) borrowing	**265**	**264**	**298**	**288**	**277**

Affordability (Prudential Indicator 4)

3.6 The objective of the affordability indicator is to ensure that the level of investment in capital assets remains within sustainable limits and to ensure the impact on the Council's "bottom line" is manageable. This indicator identifies the trend in the cost of capital, (borrowing and other long-term obligation costs net of investment income), against the net revenue stream. The estimates of financing costs include current commitments and the proposals in the Council's budget report. Table 4 below sets out the expected ratio of capital financing costs to income for General Fund activities.

Table 4 - PI 4 - Affordability	2022/23	2023/24	2024/25	2025/26	2026/27
	Actual	Forecast	Estimate	Estimate	Estimate
Ratio of capital financing cost to income	3.16%	2.85%	3.91%	4.35%	4.82%

Minimum Revenue Provision (MRP) Policy Statement

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

3.8 The Council is required to calculate a prudent provision of MRP which ensures that the outstanding debt liability is repaid over a period that is reasonably commensurate with that over which the capital expenditure provides benefits. The MRP policy statement for the Council is specified at Appendix 2.

4. Borrowing

Borrowing Strategy

4.1 One of the main functions of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council and help ensure that the Council can meet its capital spending

obligations. This management of longer-term cash may involve arranging long or short-term loans or using medium-term cash flow surpluses. On occasion, when it is prudent and economic, any debt previously drawn may be restructured to meet Council risk or cost objectives.

4.2 The Council's main objective when borrowing money is to strike an appropriate balance between securing low interest costs and achieving cost certainty over the period for which funds are required. Given the significant cuts to public expenditure and particularly, to local government funding, the Council's borrowing strategy continues to address the key issue of affordability without compromising the long-term stability of the debt portfolio. The key factors influencing the 2024/25 strategy are:

- forecast borrowing requirements
- the current economic and market environment
- interest rate forecasts.

4.3 The Council's treasury advisor Link group has provided the following forecasts on 08 January 2024. These are forecasts for Bank Rate, average earnings and PWLB certainty rates, gilt yields plus 80 bps.

Table 5

Link Group Interest Rate View	08.01.24												
	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27
BANK RATE	5.25	5.25	4.75	4.25	3.75	3.25	3.00	3.00	3.00	3.00	3.00	3.00	3.00
3 month ave earnings	5.30	5.30	5.00	4.50	4.00	3.50	3.30	3.00	3.00	3.00	3.00	3.00	3.00
6 month ave earnings	5.20	5.10	4.80	4.30	3.80	3.30	3.20	3.10	3.10	3.10	3.10	3.10	3.10
12 month ave earnings	5.00	4.90	4.60	4.10	3.70	3.20	3.20	3.10	3.10	3.10	3.10	3.20	3.20
5 yr PWLB	4.50	4.40	4.30	4.20	4.10	4.00	3.80	3.70	3.60	3.60	3.50	3.50	3.50
10 yr PWLB	4.70	4.50	4.40	4.30	4.20	4.10	4.00	3.90	3.80	3.70	3.70	3.70	3.70
25 yr PWLB	5.20	5.10	4.90	4.80	4.60	4.40	4.30	4.20	4.20	4.10	4.10	4.10	4.10
50 yr PWLB	5.00	4.90	4.70	4.60	4.40	4.20	4.10	4.00	4.00	3.90	3.90	3.90	3.90

4.4 The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement) was not fully funded with loan debt, as cash supporting the Council's reserves and balances was used as an interim funding measure. This strategy was prudent as investment returns have only recently begun to rise and counterparty risk has been minimised. It has also saved a considerable amount of interest payable, known as the 'cost of carry'.

4.5 The Council will continue with this prudent strategy of maintaining an under-borrowed position for the financial year 2024/25, however after that it will need to consider external borrowing taking account of reserves and balances. This strategy aligns with the interest rates forecast (in the table above) which shows longer dated borrowing rates are expected to fall from their current levels once prevailing inflation concerns are addressed by tighter near-term monetary policy.

4.6 Against this background and the risks within the economic forecast, continued caution will be adopted with the 2024/25 treasury operations. The Director of

Finance will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

- if it was felt that there was a significant risk of a sharp FALL in borrowing rates, then borrowing will be postponed.
- if it was felt that there was a significant risk of a much sharper RISE in borrowing rates than that currently forecast, fixed rate funding may be drawn whilst interest rates are lower than they are projected to be in the next few years.

4.7 Any decisions will be reported to the Treasury Management Group and Audit & Governance Committee at the next available opportunity.

Sources of Borrowing

4.8 All new loans are subject to the relevant gilt yields +0.8% (known as the PWLB certainty rate). A prohibition is in place to deny access to borrowing to any local authority which plans to purchase assets primarily for yield in its capital programme.

4.9 Consideration will be given to other sources of funding as summarised below:-

- Local authorities (primarily shorter dated maturities out to 3 years or so – generally still cheaper than the Certainty Rate).
- Financial institutions (primarily insurance companies and pension funds but also some banks, out of forward dates where the objective is to avoid a "cost of carry" or to achieve refinancing certainty over the next few years).
- UK Municipal Bond Agency Plc and any other special purpose companies created to enable Local Authority bonds issues.

4.10 Our advisors will keep us informed as to the relative merits of each of these approved alternative funding sources detailed on following page.

- HM Treasury's PWLB lending facility
- UK Municipal Bonds Agency
- Local Authorities
- Market - Any bank or building society authorised to operate in the UK
- UK public and private sector pension funds
- Insurance companies
- UK Infrastructure Bank
- Stock issues
- Negotiable Bonds
- Other special purpose companies created to enable local authority bond issues
- Finance Leases
- Commercial Paper
- Overdraft
- Local Authority Bills

Limits on Borrowing Activity (Prudential Indicator 5)

4.11 The Prudential Code requires the Council to set two limits on its total external debt, as set out in Table 6 below:

- **Authorised Limit for External Debt** (Prudential Indicator 5a) – This is the limit prescribed by section 3(1) of the Local Government Act 2003 representing the maximum level of borrowing which the Council may incur. It reflects the level of external debt which, while not desired, could be afforded in the short term, but may not be sustainable in the longer term.
- **Operational Boundary (Prudential Indicator 5b)** – This is the limit which external debt is not normally expected to exceed. The boundary is based on current debt plus anticipated net financing need for future years.

4.12 The Director of Finance reports that the Council complied with these prudential indicators in the current year and does not envisage difficulties for the future. This view considers current commitments, existing plans and the proposals in this report.

Table 6 - PI 5 - Borrowing Limits £m	2022/23	2023/24	2024/25	2025/26	2026/27
	Actual	Forecast	Estimate	Estimate	Estimate
Authorised Limit	**622**	**594**	**606**	**613**	**600**
Borrowing	293	286	264	281	279
Finance Lease	4	4	4	4	4
Operational Boundary	**297**	**290**	**268**	**285**	**283**

Maturity structure of borrowing (Prudential Indicator 8)

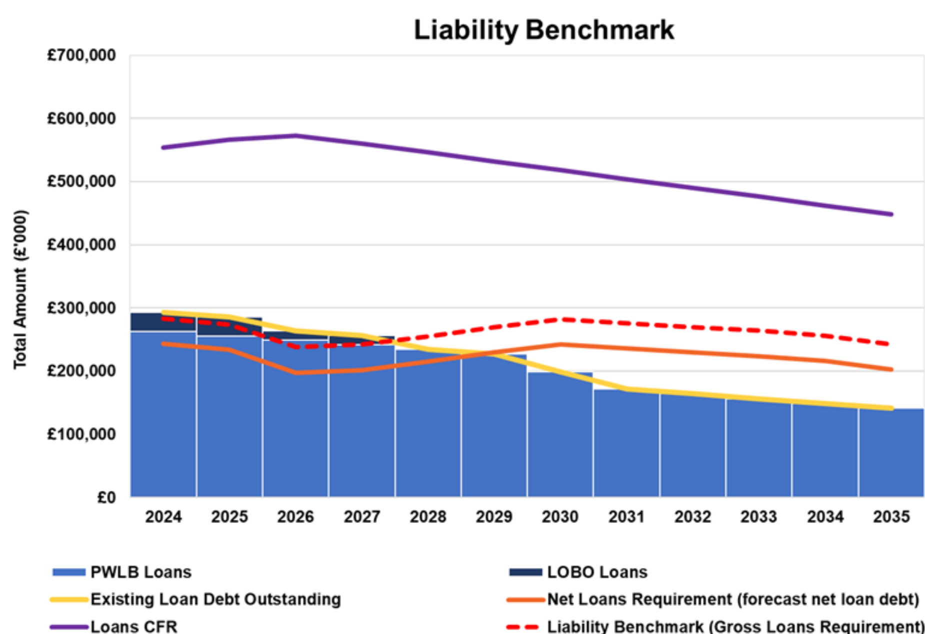
4.13 Managing the maturity profile of debt is essential for reducing the Council's exposure to large, fixed rate sums falling due for refinancing within a short period, and thus potentially exposing the Council to additional cost. Table 7 below sets out current upper and lower limits for debt maturity for approval.

Table 7 - Prudential Indicator 8	Upper Limit	Actual	
		£m	%
Under 12 Months	18%	22.09	7.7%
12 Months to 2 Years	20%	7.19	2.5%
2 Years to 5 Years	17%	37.17	13.0%
5 Years to 10 Years	36%	77.44	27.1%
10 Years to 20 Years	34%	59.19	20.7%
20 Years to 30 Years	34%	21.17	7.4%
30 Years to 40 Years	32%	31.47	11.0%
40 Years to 50 Years	20%	30.00	10.5%
More than 50 Years	12%	0.00	0.0%

Liability Benchmark (Prudential Indicator 9)

4.14 The Council is required to estimate and measure the Liability Benchmark (LB) of at least 10 years as recommended by CIPFA's Prudential Code. Liability benchmark looks at net management of treasury position and aims to minimise refinancing, interest rate and credit risk.

4.15 The Liability Benchmark is calculated by deducting the amount of cash available from external debt and then adding minimum level of working capital required to manage day-to-day cash flows. This shows the minimum level of external borrowing necessary based on available internal borrowing.



There are four components to the Liability Benchmark:

- **Existing loan debt outstanding (Yellow)**: the Council's existing loans portfolio based on current borrowing and repayment terms of the loans, split by loan type.
- **Loans CFR (Purple)**: this measures the extent to which the capital expenditure is financed from borrowing and a guide to the Council's underlying borrowing needs. This is reduced by an annual revenue (MRP) charge which represents the economic consumption of capital assets as they are used. For the Council, comparing this line graph with the existing loan debt outstanding line graph demonstrates we have not borrowed in advance of need through the under borrowed position of approximately £265m rising to £300m as demonstrated in prudential indicator 3 in paragraph 3.5 above.
- **Net loans requirement (Orange)**: This is an overview of Council's forecast cashflow position, which shows the Council's gross loan debt less treasury management investments at the last financial year-end, projected into the future mainly impacted by the cashflows (timing of income and expenditure).

Comparing this line graph with the existing loan debt outstanding line graph demonstrates the cash balance position over the medium term is in the range of £50m to £165m as demonstrated in prudential indicator 6 in paragraph 5.3. For the Council this means we have not borrowed in advance of need and evidence that our strategy of using internal borrowing to fund the capital programme has worked.

- **Liability benchmark (or gross loans requirement) (Red)**: this equals net loans requirement plus short-term working cash balance allowance.

4.16 The Liability Benchmark aids in evaluating the amount, timing and maturities structure of new borrowing and avoids borrowing too much, too little, too long or too short. Both the Net loans requirements and the Liability Benchmark is projected to exceed the outstanding loans from 2027 as significant amount of debt is maturing as demonstrated in prudential indicator 8 in paragraph 4.13.

4.17 The borrowing strategy has used the liability benchmark for the planned borrowing requirement in 2025 and 2026, by which time the cost of borrowing is projected to reduce to levels approaching 4%.

4.18 The Council is currently in an under borrowed position, where it is financing current capital schemes through the temporary use of its own cash reserves. The use of these reserves is expected to remain part of the Council's balance sheet throughout 2024/25.

Policy on borrowing in advance of need

4.19 The Council has the power to borrow in advance of need in line with its future borrowing requirements under the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, as amended.

4.20 The Council will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates and will be considered carefully to ensure that value for money can be demonstrated and that can ensure the security of such funds.

Debt Rescheduling

4.21 The Council can repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. The Council 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, helping to fulfil the treasury strategy or enhancing the balance of the portfolio by amending the maturity profile and/or the balance of volatility.

International Financial Reporting Standard 16 (IFRS16)

4.22 Although not classed as borrowing, the Council has capital finance liabilities (i.e. commitments to make payments) in the form of finance leases. With effect from 1 April 2024, local authorities are required to implement a new accounting standard known as IFRS 16. This standard requires that assets previously recognised as operating leases will, in many cases, need to be accounted for on the balance sheet. Authorities will need to recognise an asset corresponding to their 'right to use' assets held under operating leases and a liability corresponding to the payments due under the relevant leases to secure use of the leased assets.

4.23 The application of IFRS16 will impact on statutory reporting requirements, however there will be net nil impact on the Council's revenue budget. Work is progressing on the identification of all current arrangements covered by the Codes new definition of a lease. This analysis will be completed over the coming year and the detailed impact on the Council's balance sheet, CFR and Prudential Indicators will be reported in the treasury management report at a future date.

Investing primarily for yield

4.24 PWLB loans are not available to local authorities planning to buy investment assets primarily for yield. The Council has not undertaken such borrowing and has no plans to in future, which ensures continuing access to PWLB borrowing facilities.

4.25 On transacting a PWLB loan, the S151 officer is required to confirm that the Council is not borrowing in advance of need and does not intend to buy investment assets primarily for yield.

5. Managing Cash Balances

The current cash position and cash flow forecast (Prudential Indicator 6)

5.1 Investments will be made with reference to the core balance, cash flow requirements and the outlook for short term interest rates (i.e., rates for investments up to 12 months).

5.2 Table 8 below shows that cash balances have increased by £63m since 31 March 2023 to 31st December 2023 which is mainly due to the forecast pattern of the Council's cashflows and is mainly dependant on the timing of precept payments, receipt of grants, council tax and business rates, and progress on the capital expenditure programme.

Table 8 Cash Position as at December 23 £m	31 Dec 2023	March 2023
Borrowing		
PWLB	257	263
LOBO	30	30
Total	**287**	**293**
Investments		
Specified Investments (up to one year)	152	95
Non-Specified Investments (longer than one year)		
CCLA Property Pooled Fund	19	19
Total Investments	**171**	**114**
Net Cash Invested	**-116**	**-179**

5.3 The medium-term cash flow forecast below demonstrates that the Council currently has a positive cash flow position with the average cash position expected to decrease each subsequent year with a projected requirement to take further financing in 2025/26. Treasury officers will work closely with the capital finance team to monitor slippage within the capital program.

Table 9 - PI 6 - Medium-term Cashflow forecast £m	2023/24	2024/25	2025/26	2026/27
	Forecast	Estimate	Estimate	Estimate
Balance as at 1 April	**114**	**50**	**63**	**124**
Movement in Cash				
Capital Receipt	0	29	24	28
Grants & Contributions	67	168	133	93
Cash In	**67**	**197**	**157**	**121**
Capital Programme	-77	-162	-122	-91
Other Cash Movement	-59	-13	-5	-1
Cash Out	**-136**	**-175**	**-127**	**-92**
Net repayment of Debt (MRP & Borrowing)	5	-9	6	-8
Borrowing	0	0	25	20
Forecast balance 31 March	**50**	**63**	**124**	**165**

Prospects for investment returns

5.4 The suggested budgeted investment earnings rates for returns on investments placed for periods up to about three months during each financial year as shown in the table below.

Table 10 - Average earnings in each year	
2023/24 (residual)	5.30%
2024/25	4.55%
2025/26	3.10%
2026/27	3.00%
2027/28	3.25%
Years 5 to 10	3.25%
Years 10+	3.25%

5.5 **Country Rating –** The UK sovereign rating is currently AA-. To align with this rating, it is recommended to lower the sovereign rating of counter parties from AAA to AA-. This rating level is in line with the suggested minimum rating advised by Link Treasury Services Ltd. This will allow investments with financial entities domiciled in the following countries:

- AAA : Australia, Denmark, Germany, Netherlands, Norway, Singapore, Sweden, Switzerland;
- AA+ : Canada, Finland, USA
- AA : Abu Dhabi (UAE)
- AA- : Belgium, France, Qatar, UK

5.6 **Country Limits** - The current aggregate investment limit for treasury deposits placed across all non-UK domiciled banks is £40m. It is recommended to increase this by a further £40m to £80m.

5.7 The above two recommendations are designed to increase the flexibility of the Council's investment strategy and maximise its effectiveness. In a changing interest rate environment, it is important to consider each investment counterparty and where their funding "sweet spots" are. Currently the average yield for 3 months from UK Building Societies is 5.04%; UK Bank 5.20%; foreign bank with AAA rating 5.27% and foreign bank with AA+ to AA- rating 5.41%. The aim here is not only to maximise the use of each counterparty but to enable diversification and avoidance of concentration risk. The Council will continue to focus on achieving the optimum return on its investments commensurate with proper levels of security and liquidity.

Balancing short and long term investments (Prudential Indicator 7)

5.8 Greater returns are usually obtainable by investing for longer periods. While most cash balances are required to manage the ups and downs of cash flow where cash sums can be identified that could be invested for longer periods, the value to be obtained from longer term investments will be carefully assessed.

Table 11 - PI 7 - Investment Limits £m	2022/23	2023/24	2024/25	2025/26	2026/27
	Actual	Estimate	Estimate	Estimate	Estimate
Upper Limit for principal sums invested for more than 364 days	0	25	25	25	25

6. Other Matters

6.1 **International Financial Reporting Standards (IFRS) 9** – The change in accounting standards for 2023/24 under IFRS 9 and the statutory override to delay implementation with further extension to 31st March 2025 and its impact of investment instruments, such as the pooled Local Authority Property Fund administered by CCLA, which could result in an adverse movement in the value of the amount invested and resultant charges at the end of the year to the General Fund. Any potential mitigation will be considered as part of the outturn position at year end.

- The Council has £19m invested in this fund and in the past it has provided a good return compared to cash investment portfolio along with diversification. As at the end of December 23 it is generating a return of 4.92%. The portfolio is managed actively with the aim of providing a high income and long-term capital appreciation.

6.2 **Treasury Management Consultants** - The Council uses Link Group, Link Treasury Services Limited as its external treasury management advisors. The Council recognises that the responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon the services of the external service providers.

7. Economic update

7.1 The impact on the UK from higher interest rates and inflation, a weakening economic outlook, an uncertain political climate due to an upcoming general election, together with war in Ukraine and the Middle East, will be major influences on the Council's treasury management strategy for 2024/25.

7.2 The Bank of England (BoE) increased Bank Rate to 5.25% in August 2023, before maintaining this level for the period September to December. Members of the BoE's

Monetary Policy Committee voted 6-3 in favour of keeping Bank Rate at 5.25% at its December meeting. The three dissenters wanted to increase rates by another 0.25%.

7.3 UK GDP was estimated to have fallen 0.2% in 2023 Q3, falling by another 0.3% in October before recovering by 0.3% in November. Based on the latest official and survey data, Bank staff expect GDP growth to be broadly flat in Q4 and over coming quarters. The Committee continues to consider a wide range of data on developments in labour market activity. Employment growth is likely to have softened, and there has been further evidence of some loosening in the labour market.

7.4 Twelve-month CPI inflation fell sharply from 6.7% in September to 3.9% in November. Services price inflation declined to 6.6%, although much of the downside news relative to the November Report reflected movements in components that may not provide a good signal of underlying trends in services prices and of persistence in headline inflation.

7.5 Further information on the economic background is provided by our Treasury advisor Link Group which is attached at appendix 3. This will be updated with the latest commentary for the full Council.

8. Other options considered

8.1 Not applicable

9. Legal and financial implications

9.1 **Finance** : Financial Implications are contained in the body of this report.

9.2 **Legal** : The Local Government Act 2003 (“the Act”) provides that a local authority has the power both to borrow and invest money for any purpose relevant to its functions and for the prudent management of its financial affairs. The Act requires the Council to determine and to keep under review how much money it can afford to borrow. The Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, provide that, in complying with this duty, the Council must have regard to the Prudential Code for Capital Finance in Local Authorities published by CIPFA. The Council is also required to have regard to the CIPFA Treasury Management Code of Practice.

10. Corporate implications

10.1 Treasury Management activities play a significant role in supporting the delivery of the Council’s Capital Programme and Corporate Priorities

11. Communication, engagement & further consultation

11.1 Not applicable

12. Next steps and review

12.1 Full Council to approve the Treasury Management Strategy Statement.

13. Background papers

13.1 Section 3 Local Government Act 2003.

13.2 Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, as amended.

13.3 DLUHC Guidance on Minimum Revenue Provision (fourth edition) February 2018.

13.4 DLUHC Capital Finance Guidance on Local Government Investments February 2018.

13.5 CIPFA Prudential Code for Capital Finance in Local Authorities and Treasury Management Code of Practice.

14. Appendices

14.1 Appendix 1 – Annual Investment Strategy

14.2 Appendix 2 – Minimum Revenue Provision Policy

14.3 Appendix 3 – Economic Background

Appendix 1

Annual Investment Strategy

1. The Council holds significant invested funds, representing income received in advance of expenditure, balances and reserves. Investments are made with reference to the core balance, future cash flow requirements and the outlook for interest rates.

2. The Department of Levelling Up, Housing and Communities (DLUHC - this was formerly the Ministry of Housing, Communities and Local Government (MHCLG)) and CIPFA have extended the meaning of 'investments' to include both financial and non-financial investments. This report deals solely with treasury (financial) investments, (as managed by the treasury management team). Non-financial investments, essentially the purchase of income yielding assets and service investments, are covered in the Capital Strategy, (a separate report).

3. 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")

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

5. This Council has adopted a prudent approach to managing risk and defines its risk appetite by the following means: -

   - 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.

   - **Credit Default Swaps:** ratings will not be the sole determinant of the quality of an institution; it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To achieve this consideration the Council will engage with its advisors to maintain and monitor on market pricing such as **"credit default swaps"** and overlay that information on top of the credit ratings.

   - **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.

- The DLUHC Guidance on Local Government Investments made under section 15(1) of the Local Government Act 2003, places restrictions on local authorities around the use of specified and non-specified investments.
  - **Specified investments** are those with a high level of credit quality and subject to a maturity limit of one year or have less than a year left to run to maturity, if originally they were classified as being non-specified investments solely due to the maturity period exceeding one year.
  - **Non-specified investments** are those with less high credit quality, may be for periods in excess of one year, and/or are more complex instruments which require greater consideration by members and officers before being authorised for use.
- **Non-specified and loan investment limits.** The Council has determined that it will set a limit to the maximum exposure of the total treasury management investment portfolio to non-specified treasury investments of £100m.
- This Council has engaged **external consultants** to provide expert advice on how to optimise an appropriate balance of security, liquidity and yield, given the risk appetite in the context of the expected level of cash balances and need for liquidity throughout the year.
- The Council will set a limit for its investments which are invested for longer than 364 days. For the year 2024/25, the proposed limit is £25m as set out in table 11 of the TMSS.
- All investments will be denominated in **sterling**.

6. **Investment Strategy**

- In the current economic climate, it is considered appropriate to maintain a degree of liquidity to cover cash flow needs but to also consider investments for periods up to 12 months with high credit rated financial institutions whilst investment rates remain elevated.
- 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 and possibly reducing as early as the second half of 2024 so an agile investment strategy would be appropriate to optimise returns.
- While most cash balances are required in order to manage the ups and downs of cash flow, where cash sums can be identified that could be invested for longer periods, the value to be obtained from longer-term investments will be carefully assessed.

7. **Creditworthiness Policy**

- This Council applies the creditworthiness service provided by the Link Group. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies - Fitch, Moody's and Standard & Poor's. The credit ratings of counterparties are supplemented with the following overlays: -

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

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

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

- Typically, the minimum credit ratings criteria the Council uses will be a short-term rating (Fitch or equivalents) of F1 and a long-term rating of A-. There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances, consideration will be given to the whole range of ratings available, or other topical market information, to support their use.

- **Local Authority Investments -** The investment with Local Authority can only be placed with the prior approval of the Council Leader, the Chief Executive and the Director of Finance (Section 151 Officer) or deputies in the case of leave. If a deposit is placed with a local authority that subsequently issues a Section 114 notice, is given a capitalisation directive or experiences any other untoward financial event then the incident will be reported to the Audit & Governance Committee at the earliest opportunity.

- **Buckinghamshire Council's Bank -** The Council frequently receives cash without prior notification from the sender. There is a possibility that a large receipt or several

smaller receipts could be received once the daily treasury dealing process is complete resulting in overnight cash at the Council's bank exceeding the counterparty limit as defined in the treasury management strategy. If this occurs, the cash will be invested with other counterparties in line with the strategy on the following working day.

- **Limits** - Due care will be taken to consider the exposure of the Council's total investment portfolio to non-specified investments, countries, groups and sectors
  - **Country limit -** minimum sovereign credit rating of AA- from Fitch (or equivalent). This rating level is in line with the suggested minimum rating advised by Link Treasury Services Ltd. This will allow investments with financial entities domiciled in the following countries:
    - AAA : Australia, Denmark, Germany, Netherlands, Norway, Singapore, Sweden, Switzerland;
    - AA+ : Canada, Finland, USA
    - AA : Abu Dhabi (UAE)
    - AA- : Belgium, France, Qatar, UK
  - This list will be kept under review and any proposed changes to the policy reported to the next meeting.
  - no more than £20m will be placed with any non-UK country at any time.
  - the aggregate investment limit for treasury deposits placed across all non-UK domiciled banks is £80m.
- Changes to the credit rating will be monitored and, in the event, that a counterparty is downgraded and does not meet the minimum criteria, the following action will be taken immediately:
  - no new investments will be made;
  - existing investments will be recalled if there are no penalties; and
  - full consideration will be given to recall or sell existing investments which would be liable to penalty clause.

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

	Colour (and long-term rating where applicable)	Money and/or % limit	Transaction limit	Time limit
Banks *	**Yellow**	**£20m**	**£10m**	**5yrs**
Banks	**Purple**	**£20m**	**£10m**	**2yrs**
Banks	**Orange**	**£20m**	**£10m**	**1yr**
Banks – part nationalised	**Blue**	**£20m**	**£10m**	**1yr**
Banks	**Red**	**£10m**	**£5m**	**6 mths**
Banks	**Green**	**£10m**	**£5m**	**100 days**
Banks	**No Colour**	**Not to be used**	**-**	**-**
Limit 3 category – Authority's banker (where "No Colour")	**-**	**Minimal balances**	**Minimal balances**	**1 day**
Debt Management Agency Deposit Facility (UK Govt.)	**UK sovereign rating**	**Unlimited**	**£100m**	**6 months** (max. duration offered)
Local authorities (sector limit £150m)	**n/a**	**£10m**	**£10m**	**5yrs**

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

Housing associations **(sector limit £25m)**	**Colour bands**	**£5m**	**£5m**	**As per colour band**
	Fund rating**	**Money and/or % Limit**		**Time Limit**
Money Market Funds CNAV	**AAA**	**£30m**	**-**	**liquid**
Money Market Funds LVNAV	**AAA**	**£30m**	**-**	**liquid**
Money Market Funds VNAV	**AAA**	**£30m**	**-**	**liquid**
Ultra-Short Dated Bond Funds with a credit score of 1.25	**Dark Pink / AAA**	**£30m**	**-**	**liquid**
Ultra-Short Dated Bond Funds with a credit score of 1.50	**Light Pink / AAA**	**£30m**	**-**	**liquid**

** The yellow colour category is for UK Government debt.*

*** "fund" ratings are different to individual counterparty ratings*

8. **Investment performance** - This Council will benchmark against 1-month SONIA (Sterling Overnight Index Average) rate to assess the performance of portfolio.

9. **External Fund Managers** - £19m of the Council's funds are externally managed in a pooled local authority property fund by CCLA (Churches, Charities and Local Authorities). The Council meets with representatives of the fund manager on an annual basis. These meetings allow for additional scrutiny of the manager's activity as well as discussions on the outlook for the fund as well as wider markets.

Appendix 2

Minimum Revenue Provision Policy

1. Minimum Revenue Provision (MRP) is the charge to revenue made in respect of paying off the principal sum of the borrowing undertaken to finance the capital programme. MRP, which is largely defined by regulation, is aimed at ensuring that the council does not have time expired/fully depreciated assets, but still has associated outstanding debt.
2. Where capital expenditure was incurred before 1 April 2008 MRP will be charged on a straight-line basis over 50 years (from 1 April 2016) in line with previous budget approvals. For capital expenditure incurred on or after 1 April 2008 and funded through borrowing, the Council will calculate MRP using the asset life annuity method. Using this method MRP is calculated in a similar way as calculating the capital repayment element of a fixed rate repayment mortgage. Where borrowing relates to historic balances from the former County and District Councils, the calculation is based on the outstanding balances on 1 April 2020 and the remaining asset lives.
3. In accordance with provisions in the guidance, MRP will be first charged in the year following the date that an asset becomes operational.
4. The asset life annuity method calculation requires estimated useful lives of assets to be input into the calculations. These life periods will be determined under delegated powers to the Service Director Finance, with regard to the statutory guidance. However, the Council reserves the right to determine useful life periods and prudent MRP in exceptional circumstances where the asset life annuity method would not be appropriate.
5. As some types of capital expenditure incurred by the Council are not capable of being related to an individual asset, asset lives will be assessed on a basis which most reasonably reflects the anticipated period of benefit that arises from the expenditure. Also, whatever type of expenditure is involved, it will be grouped together in a manner which reflects the nature of the main component of expenditure and will only be divided up in cases where there are two or more major components with substantially different useful economic lives.

Appendix 3

Economic Background *(This is the view from our Treasury advisor)*

1. The third quarter of 2023/24 saw:
   - A 0.3% m/m decline in real GDP in October, potentially partly due to unseasonably wet weather, but also due to the ongoing drag from higher interest rates. Growth for the second quarter, ending 30th September, was revised downwards to -0.1% and growth on an annual basis was also revised downwards, to 0.3%.
   - A sharp fall in wage growth, with the headline 3myy rate declining from 8.0% in September to 7.2% in October, although the ONS "experimental" rate of unemployment has remained low at 4.2%.
   - CPI inflation continuing its downward trajectory, from 8.7% in April to 4.6% in October, then again to 3.9% in November.
   - Core CPI inflation decreasing from April and May's 31 years' high of 7.1% to 5.1% in November, the lowest rate since January 2022.
   - The Bank of England holding Bank Rate at 5.25% in November and December.
   - A steady fall in 10-year gilt yields as investors revised their interest rate expectations lower.
2. The revision of GDP data in Q2 to a 0.1% q/q fall may mean the mildest of mild recessions has begun. Indeed, real GDP in October fell 0.3% m/m which does suggest that the economy may stagnate again in Q3. The weakness in October may partly be due to the unseasonably wet weather. That said, as the weakness was broad based it may also be the case that the ongoing drag from higher interest rates is more than offsetting any boost from the rise in real wages.
3. However, the rise in the flash composite activity Purchasing Managers Index, from 50.7 in November to 51.7 in December, did increase the chances of the economy avoiding a contraction in Q3. The improvement was entirely driven by the increase in the services activity balance from 50.9 to 52.7. (Scores above 50 point to expansion in the economy, although only tepid in this instance.) The press release noted that this was primarily driven by a revival in consumer demand in the technological and financial services sectors. This chimes with the further improvement in the GfK measure of consumer confidence in December, from -24 to -22. The services PMI is now consistent with non-retail services output growing by 0.5% q/q in Q3, but this is in stark contrast to the manufacturing sector where the output balance slumped from 49.2 to 45.9 and, at face value, the output balance is consistent with a 1.5% q/q fall in manufacturing output in Q3.
4. The 0.3% m/m fall in retail sales volumes in October means that after contracting by 1.0% q/q (which was downwardly revised from -0.8% q/q) in Q2, retail activity remained weak at the start of Q3. That suggests higher interest rates are taking a bigger toll on real consumer spending.

5. Higher interest rates have filtered through the financial channels and weakened the housing market but, overall, it remains surprisingly resilient with the Halifax house price index recently pointing to a 1.7% year on year increase whilst Nationwide's December data pointed to a -1.8% year on year decrease. However, the full weakness in real consumer spending and real business investment has yet to come as currently it is estimated that around two thirds to a half of the impact of higher interest rates on household interest payments has yet to be felt.
6. Overall, we expect real GDP growth to remain subdued throughout 2024 as the drag from higher interest rates is protracted but a fading of the cost-of-living crisis and interest rate cuts in the second half of 2024 will support a recovery in GDP growth in 2025.
7. The labour market remains tight by historical standards, but the sharp fall in wage growth seen in October will reinforce the growing belief in markets that interest rates will be cut mid-2024. Wage growth eased in October much faster than the consensus expected. Total earnings fell by 1.6% m/m, which meant the headline 3myy rate eased from 8.0% in September to 7.2% in October. This news will be welcomed by the Bank of England. Indeed, the timelier three-month annualised rate of average earnings growth fell from +2.4% to -1.2%. Excluding bonuses, it fell from 5.3% to 2.0%. Furthermore, one of the Bank's key barometers of inflation persistence, regular private sector pay growth, dropped from 7.9% 3myy to 7.3%, which leaves it comfortably on track to fall to 7.2% by December, as predicted by the Bank in November.
8. The fall in wage growth occurred despite labour demand being stronger in October than expected. The three-month change in employment eased only a touch from +52,000 in September to +50,000 in October. But resilient labour demand was offset by a further 63,000 rise in the supply of workers in the three months to October. That meant labour supply exceeded its pre-pandemic level for the first time, and the unemployment rate remained at 4.2% in October. In the three months to November, the number of job vacancies fell for the 17th month in a row, from around 959,000 in October to around 949,000. That has reduced the vacancy to unemployment ratio as demand for labour eases relative to supply, which may support a further easing in wage growth in the coming months.
9. CPI inflation fell from 6.7% in September to 4.6% in October, and then again to 3.9% in November. Both these falls were bigger than expected and there are clear signs of easing in domestic inflationary pressures. The fall in core CPI inflation from 5.7% to 5.1% in November was bigger than expected (consensus forecast 5.6%). That's the lowest rate since January 2022. Some of the decline in core inflation was due to the global influence of core goods inflation, which slowed from 4.3% to 3.3%. But some of it was due to services inflation falling from 6.6% to 6.3%. The Bank views the latter as a key barometer of the persistence of inflation and it came in further below the Bank's forecast of 6.9% in its November Monetary Policy Report. This will give the Bank more confidence that services inflation is now on a firmly downward path.
10. The Bank of England sprung no surprises with its December monetary policy committee (MPC) meeting, leaving interest rates at 5.25% for the third time in a row and pushing back against the prospect of near-term interest rate cuts. The Bank

continued to sound hawkish, with the MPC maintaining its tightening bias saying that "further tightening in monetary policy would be required if there were evidence of more persistent inflationary pressures". And it stuck to the familiar script, saying that policy will be "sufficiently restrictive for sufficiently long" and that "monetary policy is likely to need to be restrictive for an extended period of time". In other words, the message is that the MPC is not yet willing to endorse investors' expectations that rates will be cut as soon as May 2024.

11. Looking ahead, our colleagues at Capital Economics forecast that the recent downward trends in CPI and core inflation will stall over the next few months before starting to decline more decisively again in February. That explains why we think the Bank of England won't feel comfortable cutting interest rates until H2 2024.
12. The fall in UK market interest rate expectations in December has driven most of the decline in 10-year gilt yields, which have fallen in line with 10-year US Treasury and euro-zone yields. 10-year gilt yields have fallen from 4.68% in October 2023 to around 3.70% in early January, with further declines likely if the falling inflation story is maintained.
13. Investors' growing expectations that the Fed will cut interest rates soon has led to an improvement in risk sentiment, which has boosted the pound and other risky assets. In addition, the rise in the pound, from $1.21 in November to $1.27 now, has also been supported by the recent relative decline in UK wholesale gas prices.
14. The further fall in 10-year real gilt yields in December has supported the recent rise in the FTSE 100. That said, the index remains 5% below its record high in February 2023. This modest rise in equities appears to have been mostly driven by strong performances in the industrials and rate-sensitive technology sectors. But UK equities have continued to underperform US and euro-zone equities. The FTSE 100 has risen by 2.2% in December, while the S&P 500 has risen by 3.8%. This is partly due to lower energy prices, which have been a relatively bigger drag on the FTSE 100, due to the index's high concentration of energy companies.
15. On 2nd November, the Bank of England's Monetary Policy Committee (MPC) voted to keep Bank Rate on hold at 5.25%, and on 14th December reiterated that view. Both increases reflected a split vote, the latter by 6 votes to 3, with the minority grouping voting for an increase of 0.25% as concerns about "sticky" inflation remained in place.
16. Nonetheless, with UK CPI inflation now at 3.9%, and core inflating beginning to moderate (5.1%), markets are voicing a view that rate cuts should begin in Q1 2024/25, some way ahead of the indications from MPC members. Of course, the data will be the ultimate determinant, so upcoming publications of employment, wages and inflation numbers will be of particular importance, and on-going volatility in Bank Rate expectations and the gilt yield curve can be expected.
17. In addition, what happens outside of the UK is also critical to movement in gilt yields. The US FOMC has kept short-term rates in the range of 5.25%-5.50%, whilst the ECB has moved its Deposit rate to a probable peak of 4%. Markets currently expect both central banks to start cutting rates in 2024.