AG133
AUDIT & GOVERNANCE COMMITTEE

REPORT TITLE: TREASURY MANAGEMENT OUTTURN REPORT 2023/24

18 JULY 2024

REPORT OF CABINET MEMBER: Cllr Margot Power, Cabinet Member for Finance and Value

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WARD(S): ALL WARDS

## PURPOSE

In accordance with the requirements of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management, this report provides details of the performance of the treasury management function, on the effects of the decisions taken and the transactions executed in the past year, and confirmation that there were no instances of non-compliance with the council's Treasury Management Policy Statement and Treasury Management Practices, for the year 2023/24.

## RECOMMENDATIONS:

1. Note the Annual Treasury Outturn Report 2023/24.

IMPLICATIONS:

1 COUNCIL PLAN OUTCOME

Treasury management is an integral part of helping to deliver the council Strategy and all of its outcomes. Of key importance is ensuring the security and sufficient liquidity of the council's cash and investment balances whilst, where possible, optimising the yield from those investments. The income from investments is available to be used by the council in achieving its objectives.

2 FINANCIAL IMPLICATIONS

Effective treasury management ensures both the financial security and liquidity of the council. The 2023/24 outturn shows £1.7m of income achieved against a budget of £1.5m delivering an additional £0.2m of income above budget. This was a consequence of higher average cash and investment balances than forecast due to slippage in significant one-off budgets and in the capital programme.

3 LEGAL AND PROCUREMENT IMPLICATIONS

The Council's Treasury Management Strategy Statement follows the latest codes of practice and the MHCLG and CIPFA guidance.

With effect from September 2014 Hampshire County Council (HCC) and Winchester City Council (WCC) established arrangements for the joint discharge of functions under Section (101)(1) and (5) of the Local Government Act 1972 and Section 9EA and 9EB Local Government Act 2000. Under this arrangement, HCC's Investments and Borrowing Team provide a Treasury Service which includes the management of WCC's cash balances and investment of surplus cash or sourcing of short-term borrowing in accordance with the agreed Treasury Management Strategy Statement.

4 WORKFORCE IMPLICATIONS

HCC's Investments and Borrowing Team carry out the day-to-day management of the council's cash balances and investments. The council's in-house finance team undertake the accounting and retain responsibility for long-term borrowing decisions.

5 PROPERTY AND ASSET IMPLICATIONS

None

6 CONSULTATION AND COMMUNICATION

This report has been produced in consultation with HCC's Investments & Borrowing team.

7 ENVIRONMENTAL CONSIDERATIONS

Following the council's declaration of a Climate Emergency in June 2019 and in line with the ethical stances in its investment policy, the council has no direct or indirect equity investments in companies directly involved in the fossil fuel industry.

8 EQUALITY IMPACT ASSESSEMENT

There are no actions which arise directly from this report.

9 DATA PROTECTION IMPACT ASSESSMENT

None required

10 RISK MANAGEMENT

| **Risk** | **Mitigation** | **Opportunities** |
|---|---|---|
| *Returns from investments are too low* | A diversified strategy that attempts to manage the balance between liquidity risk, credit risk and yield within the council's risk appetite. | Returns above budgeted levels |
| *A counterparty fails* | A diversified strategy that has relatively low levels of counter-party risk | |
| *Cash is not available* | A balanced portfolio of liquid and long-term funds are held to ensure cash is available to utilise. The council also mitigates this risk through cashflow forecasting | More accurate and immediate cashflow forecasting can help improve the return on investments through more active treasury management activity |

11 SUPPORTING INFORMATION:

Introduction

11.1 The council has adopted the key recommendations of the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice (the CIPFA Code), last updated in 2021. The CIPFA Code requires the council to approve a treasury management strategy before the start of the year, a mid-year report, and annual treasury outturn report. The purpose of this report is therefore to meet this obligation by providing an update on the performance of the treasury management function during 2023/24.

12 Summary

12.1 The report fulfils the council's legal obligation under the Local Government Act 2003 to have regard to the CIPFA Code and provides an update on the performance of the treasury management function during 2023/24.

12.2 The council's treasury management strategy was most recently updated and approved at a meeting of Full Council in February 2024. The council has borrowed and invested sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to the council's treasury management strategy.

12.3 Treasury management in the context of this report is defined as: "the management of the organisation's 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."

12.4 This annual report sets out the performance of the treasury management function during 2023/24, to include the effects of the decisions taken and the transactions executed in the past year.

12.5 Hampshire County Council's Investments & Borrowing Team has been contracted to manage the council's treasury management balances since September 2014 but overall responsibility for treasury management remains with Winchester City Council. No treasury management activity is without risk and as such the effective identification and management of risk are integral to the council's treasury management objectives.

12.6 A breach of the council's Treasury Management Strategy and Investment Strategy for 2023/24 did occur on an overnight basis in August 2023, and this was explained in detail in the 2023/24 Quarter 1 Report (AG118). No other breaches of the TMSS have occurred during 2023/24. Advice in undertaking treasury management activities has been provided by the council's treasury advisers, Arlingclose.

12.7 The Prudential Code includes a requirement for local authorities to provide a Capital Strategy, a summary document approved by Full Council covering capital expenditure and financing, treasury management and non-treasury investments. The latest iteration of the council's Capital and Investment Strategy, complying with CIPFA's requirement, was approved by Full Council in February 2024.

13 External Context

13.1 The following sections outline the key economic themes in the UK against which investment and borrowing decisions were made in 2023/24.

Economic commentary

13.2 UK inflation continued to decline from the 8.7% rate seen at the start of 2023/24. By the last quarter of the financial year headline consumer price inflation (CPI) had fallen to 3.4% in February 2024, but was still above the Bank of England's (BoE) 2% target at the end of the period.

13.3 The UK economy entered a technical recession in the second half of 2023. Over the 2023 calendar year GDP (gross domestic product) growth only expanded by 0.1% compared to 2022. Of the recent monthly data, the Office for National Statistics reported a rebound in activity with economy expanding 0.2% in January 2024. While the economy may somewhat recover in Quarter 1 2024, the data suggests that prior increases in interest rates and higher price levels are depressing growth, which will continue to bear down on inflation throughout 2024.

13.4 Having begun the financial year at 4.25%, the BoE's Monetary Policy Committee (MPC) increased Bank Rate to 5.25% in August 2023 and this remained the rate at the end of the financial year.

13.5 In the February 2024 Monetary Policy Report the BoE's expectations for the UK economy were positive for the first half of 2024, with a recovery from the mild recession in the second half of 2023 being gradual. Headline CPI was forecast to dip below the 2% target quicker than previously thought due to declining energy prices; these effects would hold inflation slightly above target for much of the forecast horizon.

13.6 Following this MPC meeting, the Council's treasury adviser, Arlingclose, maintained its central view that 5.25% remains the peak in Bank Rate and that interest rates will most likely start to be cut later in the second half of 2024. The risks in the short-term are deemed to be to the downside as a rate cut may come sooner than expected, but then more broadly balanced over the medium term.

Financial markets

13.7 Sentiment in financial markets remained uncertain and bond yields continued to be volatile over the year. During the first half of the year, yields rose as interest rates continued to be pushed up in response to rising inflation. From October 2023 they started declining again before falling sharply in December 2023 as falling inflation and central bank attitudes caused financial markets to expect cuts in interest rates in 2024. When it emerged in January 2024 that inflation was stickier than expected and the BoE and the Federal Reserve were data dependent and not inclined to cut rates soon, yields rose once again, ending the period some 0.5%+ higher than when it started.

Credit review

13.8 In response to an improving outlook for credit markets, in January 2024 Arlingclose moved away from its previous temporary stance of a 35-day maximum duration and increased its advised recommended maximum unsecured duration limit on all banks on its counterparty list to 100 days.

13.9 Credit default swap (CDS) prices are used as an indicator of credit risk, where higher premiums indicate higher perceived risks. CDS prices began the financial year at elevated levels following the fallout from Silicon Valley Bank and collapse/takeover of other lenders. From then the general trend was one of falling prices and UK lenders' CDS ended the period at similar levels to those seen in early 2023.

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

## 14 Local Context

14.1 The council's Balance Sheet is presented once a year as part of the annual Statement of Accounts. The Balance Sheet represents the council's assets, liabilities, and reserves at the end of the financial year. Table 1 summarises the Balance Sheet for Treasury Management purposes.

14.2 The Capital Financing Requirement (CFR) is the underlying need to borrow for capital purposes. It is the amount of capital spending that has not yet been financed by capital receipts, capital grants or contributions from revenue income. The table shows a mixture of internal and external borrowing has been utilised, which is explained in more detail later in this report.

| **Table 1: Balance sheet summary** | **31/03/23 Balance £m** | **Movement £m** | **31/03/24 Balance £m** |
|---|---:|---:|---:|
| General Fund CFR | (71.6) | 1.4 | (70.2) |
| Housing Revenue Account CFR | (199.8) | (12.7) | (212.5) |
| **Borrowing CFR** | **(271.4)** | **(11.3)** | **(282.7)** |
| | | | |
| External borrowing* | (161.7) | 2.0 | (159.7) |
| Internal borrowing | (109.7) | (13.3) | (123.0) |
| **Total funding of the CFR** | **(271.4)** | **(11.3)** | **(282.7)** |
| | | | |
| **Total investments** | **23.6** | **(11.2)** | **12.4** |

* shows only loans to which the council is committed and excludes optional refinancing.

14.3 Table 1 shows that during 2023/24 the council's Borrowing CFR increased by £11.3m because an increase in the Housing Revenue Account's (HRA) underlying need to borrow due to unfinanced capital expenditure such as the HRA new build programme. The Borrowing CFR is financed by external and internal borrowing. External borrowing is made up of external loans such as loans secured via the market or Public Works Loan Board (PWLB), whilst internal borrowing is where the council borrows from its own cash balances. During 2023/24 the council's external borrowing reduced by £2.0m due to the combination of the repayment of £5.0m of Treasury Management borrowing on maturity, and the securing of £3.0m of new Treasury Management borrowing at the end of the year. These changes to the external borrowing balanced in combination with the increase in Borrowing CFR led to internal borrowing increasing by £13.3m in 2023/24.

14.4 The council's strategy was to maintain borrowing and investments below their underlying levels, referred to as internal borrowing, to reduce risk and keep interest costs low. This has meant that internal funds have been utilised in lieu of taking on external borrowing debt. The treasury management position as at 31 March 2024 and the change during the year are shown in Table 2.

| **Table 2: Treasury management summary** | **31/03/23 Balance £m** | **Movement £m** | **31/03/24 Balance £m** | **31/03/24 Rate %** |
|---|---|---|---|---|
| Long-term borrowing | (156.7) | 2.0 | (154.7) | 3.30 |
| Short-term borrowing | (5.0) | 0.0 | (5.0) | 2.82 |
| **Total borrowing** | **(161.7)** | **2.0** | **(159.7)** | **3.28** |
| Long-term investments | 5.0 | 0.0 | 5.0 | 5.02 |
| Short-term investments | 7.0 | (3.0) | 4.0 | 5.22 |
| Cash and cash equivalents | 11.6 | (8.2) | 3.4 | 5.01 |
| **Total investments** | **23.6** | **(11.2)** | **12.4** | **5.08** |
| **Net borrowing** | **(138.1)** | **(9.2)** | **(147.3)** | |

Note: the figures in Table 2 are from the balance sheet in the council's statement of accounts but adjusted to exclude operational cash, accrued interest and other accounting adjustments.

14.5 The increase in net borrowing of £9.2m shown in Table 2 occurred due to a net reduction in total borrowing of £2.0m coupled with a decrease in total investments of £11.2m. This reduction in investment balances was anticipated and is primarily a result of financing expenditure on the council's capital programme. Further details are provided in the Borrowing Strategy and Activity and Treasury Investments Activity sections of this report.

15 Borrowing Update

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

15.2 The council has not invested in assets primarily for financial return or that are primarily related to the functions of the council. It has no plans to borrow to invest primarily for commercial return and so is unaffected by the changes to the Prudential Code.

15.3 Further, the council has invested in a pooled property fund as part of its Treasury Management strategy. This is not a policy to primarily generate yield but a part of the implementation of the wider Treasury Management strategy to invest the council's surplus cash and reserves ensuring it is investing its funds prudently, having regard to the security and liquidity of its treasury investments before seeking the optimum rate of return, or yield. By investing a diversified portfolio in respect of yield this meets the council's aim of protecting reserves from high inflation.

15.4 The council is a net borrower and as stated in the Treasury Management Strategy 2024/25, the council expects a positive liability benchmark across the forecast period, which generally means an authority is required to take external borrowing to fund the gap between its resources and the CFR. Although the council currently has taken external borrowing, this is not predicted to be sufficient to meet the CFR and, depending on the internal borrowing position, further borrowing will be considered by the Section 151 Officer as required.

15.5 The Section 151 Officer will review the current pooled fund investment prior to making any external borrowing decisions.

16 Borrowing Strategy and Activity

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

16.2 Interest rates have seen substantial rises over the last two years, although these rises have now begun to plateau. Gilt yields fell in late 2023, by December 2023 they had returned to the lows previously see in April earlier that year before rebounding to an extent in the first three months of 2024. Gilt yields have remained volatile, seeing upward pressure from perceived stickier inflation at times and downward pressure from falling inflation and a struggling economy at other times.

16.3 The cost of short-term borrowing from other local authorities has generally risen with Base Rate over the year. Interest rates peaked at around 7% towards the later part of March 2024 as many authorities required cash at the same time. These rates fell back to more normal market levels in April 2024.

16.4 At 31 March 2024 the council held £159.7m of loans, all of which relates to the HRA including the financing settlement in 2012. The year-end treasury management borrowing position and year-on-year change are summarised in Table 3.

| **Table 3: Borrowing position** | **31/03/23 Balance £m** | **Net movement £m** | **31/03/24 Balance £m** | **31/03/24 Weighted average rate %** | **31/03/24 Weighted average maturity (years)** |
|---|---|---|---|---|---|
| Public Works Loan Board | (161.7) | 2.0 | (159.7) | 3.28 | 19.5 |
| **Total borrowing** | **(161.7)** | **2.0** | **(159.7)** | **3.28** | **19.5** |

Note: The figures in the table above are from the balance sheet in the council's statement of accounts but adjusted to exclude accrued interest.

16.5 The council has seen steadily decreasing investment balances over the course of the financial year, which had been used in part to fund internal borrowing. The decrease in balances has been, in large part, due to increased expenditure on the capital programme. To meet cash flow requirements and maintain sufficient liquidity, the decision was made in March 2024 to borrow £3m from the PWLB at an average interest cost of 4.84%, with the borrowing maturing in March of 2037. This external borrowing replaces the internal borrowing the council was previously able to fund with its higher cash balances. This is in keeping with the council's borrowing strategy and the maturity profile of the existing portfolio of loans.

16.6 This also meant that £5m of existing PWLB loans with an average interest cost of 2.70% which was repaid at maturity earlier during the year was effectively part-refinanced, albeit at a higher rate. Because this additional borrowing related to the HRA, these new loans were secured using the PWLB's HRA Rate which offers a discount of 60 basis points to loans at the Standard Rate. This borrowing strategy has been monitored with the assistance of Arlingclose and has enabled the council to keep long-term borrowing costs low and mitigates against future interest rate increases.

17 <u>Treasury Investment Activity</u>

17.1 The CIPFA Treasury Management Code now defines treasury management investments as investments that arise from the authority's cash flows or treasury risk management activity that ultimately represents balances that need to be invested until the cash is required for use in the course of business.

17.2 The council holds invested funds, representing income received in advance of expenditure plus balances and reserves held. During the year the council's investment balances have ranged between £12.4m and £46.2m due to timing differences between income and expenditure. The year-end investment position and the year-on-year change are shown in Table 4.

| **Table 4: Treasury investment position** | **31/03/23 Balance £m** | **Movement £m** | **31/03/24 Balance £m** | **31/03/24 Income return %** | **31/03/23 Weighted average maturity (years)** |
|---|---|---|---|---|---|
| **Short term investments:** | | | | | |
| Banks and building societies: | | | | | |
| - Unsecured | 3.3 | (2.3) | 1.1 | 4.48 | 0.01 |
| Money market funds | 7.8 | (5.5) | 2.3 | 5.24 | 0.01 |
| Government: | | | | | |
| - Local authorities | - | 3.0 | 3.0 | 5.60 | 0.22 |
| - UK treasury bills | 6.5 | (6.5) | 0.0 | N/A | N/A |
| Cash plus funds | 1.0 | 0.0 | 1.0 | 4.09 | 0.01 |
| **Total** | **18.6** | **(11.2)** | **7.4** | **5.13** | **0.09** |
| **Long term investments** | | | | | |
| - Pooled property fund* | 5.0 | 0.0 | 5.0 | 5.02 | N/A |
| **Total** | **5.0** | **0.0** | **5.0** | **5.02** | **N/A** |
| **Total investments** | **23.6** | **(11.2)** | **12.4** | **5.08** | **0.06** |

* The rate provided for the pooled property fund investment is reflective of annualised income returns over the year to 31 March 2024.

Note: the figures in Table 4 are from the balance sheet in the council's statement of accounts but adjusted to exclude operational cash, accrued interest and other accounting adjustments.

17.3 The CIPFA Treasury Code and government guidance both require the council to invest its funds prudently, and to have regard to the security and liquidity of its treasury investments before seeking the optimum rate of return, or yield. The council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income. The council's Treasury Management Strategy Statement (TMSS) sets out how it will manage and mitigate these risks.

17.4 Bank Rate increased by 1% over the period, from 4.25% at the beginning of April 2023 to 5.25% by the end of March 2024. Short term rates peaked at 5.7% for 3-month rates and 6.7% for 12-month rates during the period, although these rates subsequently began to decline towards the end of the period. Money Market Rates also rose and were between 4.5% and 5.3% by the end of March 2024.

17.5 £5m that is currently available for longer-term investments is invested in a pooled property fund.

17.6 The security of investments has been maintained by following the counterparty policy and investment limits within the TMSS, taking advice from Arlingclose on changes in counterparty credit worthiness. The council invests in liquid investments to ensure money is available when required to meet its financial obligations, spreading these investments across a number of counterparties to mitigate operational risk.

17.7 The council benchmarks the performance of its internally managed investments against that of other Arlingclose clients. Internally managed investments include all investments except externally managed pooled funds but do include Money Market Funds. The performance of these investments against relevant measures of security, liquidity and yield are shown in Table 5, providing data for the quarter ended 31 March 2024 and at the same date in 2023 for comparison.

| **Table 5: Investment benchmarking (excluding pooled funds)** | **Credit rating** | **Bail-in exposure %** | **Weighted average maturity (days)** | **Rate of return %** |
|---|---|---|---|---|
| 31.03.2023 | AA- | 63 | 27 | 3.95 |
| 31.03.2024 | A+ | 53 | 38 | 5.29 |
| Similar LAs | A+ | 61 | 50 | 5.20 |
| All LAs | A+ | 61 | 9 | 5.17 |

17.8 Over the 12 months to 31 March 2024, cash balances have significantly reduced to the extent that they are now predominately used to fund liabilities. Of the cash and equivalents held at 31 March 2024, a sizeable percentage is invested in unsecured bank deposits which has impacted the average credit rating of the portfolio, reducing from AA- to A+. Despite this, the credit rating is now comparative with other authorities in the benchmarking exercise. Bail-in risk exposure has reduced when compared to the same point in 2023, owing to a proportion of investment balances being allocated to lending to other local authorities which have no bail-in risk. This allocation to local authority lending also provides the reason why the average maturity of the portfolio has increased. Despite the changes in 2023/24, the council's investment portfolio compares favourably to other Arlingclose clients, particularly when considering the average rate of return.

Externally managed pooled property fund

17.9 £5m of the council's investments are invested in an externally managed strategic pooled and property fund where short-term security and liquidity are lesser considerations, and the objectives instead are regular revenue income and long-term price stability. In 2023/24 these funds generated an average total return of 1.13%, comprising a 5.02% income return which is used to support services in year, and 3.89% of unrealised capital loss. Over the holding period, the council's investments in pooled funds have contributed 4.25% income per year on average, which compares favourably in a period where base rates have generally been low.

17.10 The market background for commercial property improved marginally in 2023 and was more stable, in contrast to the very challenging backdrop of 2022. Low transactional volumes were a constraint on valuations and made prospective sellers and buyers more cautious. Although many sectors lacked momentum, there was growing confidence in the longer-term outlook as occupier demand and rental markets held up. Industrial and retail warehousing sectors remained strong, but the retail and offices sectors remained weak, the latter continuing to be hindered by low occupancy from hybrid working practices.

17.11 Because this fund has no defined maturity date but is available for withdrawal after a notice period, the performance and continued suitability in meeting the council's medium-to long-term investment objectives are both regularly reviewed. Strategic fund investments are made in the knowledge that capital values will move both up and down on months, quarters and even years and with the expectation that over a three- to five-year period total returns should exceed cash interest rates.

17.12 In April 2023 the Department for Levelling Up, Housing and Communities (DLUHC) published the full outcome of the consultation on the extension of the statutory override on accounting for gains and losses on pooled investment funds. The override has been extended until 31 March 2025, but no other changes have been made; whether the override will be extended beyond this date is unknown but commentary to the consultation outcome suggests it will not. The council will discuss with Arlingclose the implications for the investment strategy and what action may need to be taken.

Financial Implications

17.13 The outturn for debt interest paid in 2023/24 was £5.2m on an average debt portfolio of £161.7m at an average interest rate of 3.28%.

17.14 The outturn for investment income received in 2023/24 was £1.7m on an average investment portfolio of £33.8m, therefore giving a yield of 5%, against a budgeted £1.5m. In comparison in 2022/23 investment income received was £1.08m on an average investment portfolio of £52.6m, therefore giving a yield of 2.05%.

18 Non-Treasury Investments

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

18.2 Investment Guidance issued by the Department for Levelling Up Housing and Communities (DLUHC) and Welsh Government also broadens the definition of investments to include all such assets held partially or wholly for financial return.

18.3 This could include loans made to local businesses or the direct purchase of land or property and such loans and investments will be subject to the council's normal approval process for revenue and capital expenditure and need not comply with the treasury management strategy.

18.4 Further information on the council's non-Treasury investments will be included in CAB3464 General Fund Outturn 23-24 which will be presented to Cabinet on 11 September 2024.

19 Consultations

19.1 Following three rounds of consultation, the Department for Levelling Up, Housing and Communities (DLUHC) has published its final consultation response, amendment regulations and revised statutory guidance on Minimum Revenue Provision (MRP). The statutory guidance also incorporates an informal commentary. There are three main changes:

- Local authorities cannot exclude any amount of their Capital Financing Requirement (CFR) from their MRP calculation, unless by an exception set out in law.

- Capital receipts cannot be used to directly replace, in whole or part, the prudent charge to revenue for MRP, with specific exceptions for capital loans and leased assets.

- For capital loans given on or after 7 May 2024, sufficient MRP must be charged so that the outstanding CFR in respect of the loan is no higher than the principal outstanding minus any expected credit loss.

19.2 Changes will take effect from the 2025/26 financial year, except in respect of expected credit losses which take effect from the current 2024/25 year.

19.3 The changes are not expected to impact the council's forecast MRP as its policy is already consistent with the changes in statutory guidance.

20 Compliance Report

20.1 As previously detailed in the Q1 Treasury Management Report presented to Audit Committee on 11 October 2023, during Quarter 2 an overnight breach of the Treasury Management Strategy and Investment Strategy occurred. No other breaches of the TMSS have occurred during 2023/24.

20.2 Compliance with the authorised limit and operational boundary for external debt is demonstrated in Table 6.

| **Table 6: Debt limits** | **2023/24 Maximum £m** | **31/03/24 Actual £m** | **2023/24 Operational Boundary £m** | **2023/24 Authorised Limit £m** | **Complied?** |
|---|---|---|---|---|---|
| Borrowing | (162.4) | (159.7) | (310.9) | (324.2) | ✓ |
| Finance leases | - | - | (2.2) | (2.7) | ✓ |
| **Total debt** | **(162.4)** | **(159.7)** | **(313.1)** | **(326.9)** | ✓ |

21 Treasury Management Indicators

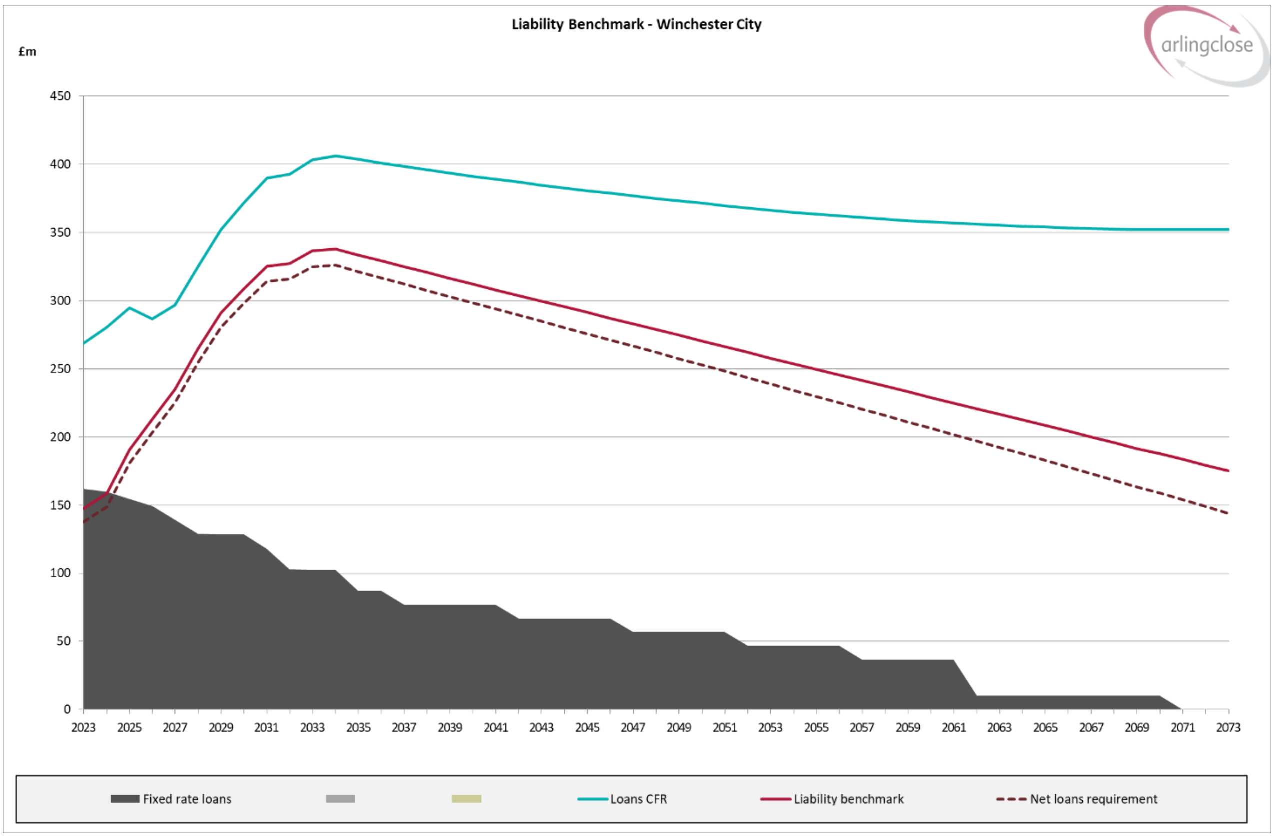
21.1 The council measures and manages its exposures to treasury management risks using the following indicators.

Liability benchmark

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

| **Table 7 – Liability Benchmark** | **31/03/2023 Actual** | **31/03/2024 Actual** | **31/03/2025 Forecast** | **31/03/2026 Forecast** |
|---|---|---|---|---|
| Loans CFR | 268.9 | 280.5 | 294.7 | 286.7 |
| Less: Balance sheet resources | (131.4) | (132.0) | (114.1) | (83.7) |
| **Net loans requirement** | **137.5** | **148.5** | **180.6** | **203.0** |
| Plus: Liquidity allowance | 10.0 | 10.0 | 10.0 | 10.0 |
| **Liability benchmark** | **147.5** | **158.5** | **190.6** | **213.0** |

**Chart 1: Liability Benchmark**




21.3 Table 7 and Graph 1 illustrate the council expects a positive liability benchmark across the forecast period, which generally means an authority is required to take external borrowing to fund the gap between its resources and the CFR. The chart shows that if it is to deliver its capital programme as planned, the council will need to take out additional external borrowing as reflected in the gap between the liability benchmark (the red line) and the existing borrowing (the grey area). This requirement will be considered by the Section 151 Officer in consultation with Arlingclose and the Investments & Borrowing team at Hampshire County Council to ensure borrowing is undertaken at the most appropriate time.

<u>Interest rate exposures</u>

21.4 The following indicator shows the sensitivity of the council's current investments and borrowing to a change in interest rates:

| **Table 8 – Interest rate risk indicator** | **31/03/24 Actual** | **Impact of +/-1% interest rate change** |
|---|---|---|
| Sums subject to variable interest rates: | | |
| Investments | £6.39m | +/-£0.06m |
| Borrowing | (£0.11m) | +/-0.00m |

21.5 Fixed rate investments and borrowings are those where the rate of interest is fixed for the whole financial year. Instruments that mature during the financial year are classed as variable rate.

Maturity structure of borrowing

21.6 This indicator is set to control the council's exposure to refinancing risk. The upper and lower limits show the maximum and minimum maturity exposure to fixed rate borrowing as agreed in the TMSS:

| Table 9: Maturity structure of borrowing | 31/03/24 Actual | Upper Limit | Lower Limit | Complied |
|---|---|---|---|---|
| Under 12 months | 3% | 25% | 0% | ✓ |
| 12 months and within 24 months | 3% | 25% | 0% | ✓ |
| 24 months and within 5 years | 13% | 25% | 0% | ✓ |
| 5 years and within 10 years | 16% | 30% | 0% | ✓ |
| 10 years and within 20 years | 22% | 50% | 0% | ✓ |
| 20 years and within 30 years | 13% | 50% | 0% | ✓ |
| 30 years and within 40 years | 23% | 75% | 0% | ✓ |
| 40 years and within 50 years | 6% | 100% | 0% | ✓ |

Long-term Treasury Management Investments

21.7 The purpose of this indicator is to control the council's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the long-term principal sum invested to final maturities beyond the period end were:

| Table 10: Long-term Treasury Management Investments | 2023/24 | 2024/25 | 2025/26 | No fixed date |
|---|---|---|---|---|
| Actual principal invested beyond year end | £5m | £5m | £5m | £5m |
| Limit on principal invested beyond year end | £20m | £20m | £20m | £5m |
| Complied | ✓ | ✓ | ✓ | ✓ |

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

## 22 OTHER OPTIONS CONSIDERED AND REJECTED

22.1 The council could elect to bring all treasury management activity back in-house. This option has been rejected as the arrangement with Hampshire County Council's Investments and Borrowing team provides significant resilience and economies of scale.

22.2 The council could make more risky investments than those proposed in the Strategy to increase its yield. This has been rejected as priority is given to ensuring security and liquidity in line with the key principles of the CIPFA Treasury Management Code.

## BACKGROUND DOCUMENTS:-

Previous Committee Reports:-

AUD119: Treasury Management Practices, 22 June 2015

CAB3390: Treasury Management Strategy 2023/24, 23 February 2023

AG109: Treasury Management Outturn 2022/23, 20 July 2023

AG119: Treasury Management Mid-Year Monitoring Report 2023/24, 09 November 2023

CAB3446: Treasury Management Strategy 2024/25, 22 February 2024

Other Background Documents:-

None

## APPENDICES:

None