BROMSGROVE DISTRICT COUNCIL

Cabinet **11th September 2024**

Treasury Management Strategy Outturn Report 2023/24

Relevant Portfolio Holder	Councillor Colella – Portfolio Holder for Finance and Governance
Portfolio Holder Consulted	Yes
Relevant Head of Service	Debra Goodall
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Wards Affected	All Wards
Ward Councillor(s) consulted	No
Relevant Strategic Purpose(s)	All
Key Decision	
If you have any questions about this report, please contact the report author in advance of the meeting.	

1. SUMMARY

The purpose of this report is to set out the annual outturn for 2023/24 on the Council's Capital and Treasury Management Strategies, including all prudential indicators.

2. RECOMMENDATIONS

Cabinet are asked to RESOLVED to NOTE:

1. **The Council's Treasury performance for the financial year 23/24.**
2. **The position in relation to the Council's Prudential indicators.**

3. BACKGROUND

Introduction

3.1 The Authority has adopted the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice* (the CIPFA Code) which requires the Authority to approve, as a minimum, treasury management semi-annual and annual outturn reports.

3.2 This report includes the requirement in the 2021 Code, mandatory from 1st April 2023, of reporting the treasury management prudential indicators. The non-treasury prudential indicators are incorporated in the Authority's normal quarterly revenue report.

3.3 The Authority's treasury management strategy for 2023/24 was approved in February

2023. The Authority has invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk remains central to the Authority's treasury management strategy.

External Context

3.4 **Economic background:** 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 but was still above the Bank of England's 2% target at the end of the period. The core measure of CPI, i.e. excluding food and energy, also slowed in February to 4.5% from 5.1% in January, a rate that had stubbornly persisted for three consecutive months.

3.5 The UK economy entered a technical recession in the second half of 2023, as growth rates of -0.1% and -0.3% respectively were recorded for Q3 and Q4. Over the 2023 calendar year GDP 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 Q1 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.

3.6 Labour market data provided a mixed message for policymakers. Employment and vacancies declined, and unemployment rose to 4.3% (3mth/year) in July 2023. The same month saw the highest annual growth rate of 8.5% for total pay (i.e. including bonuses) and 7.8% for regular pay growth (i.e. excluding bonuses). Thereafter, unemployment began to decline, falling to 3.9% (3mth/year) in January and pay growth also edged lower to 5.6% for total pay and 6.1% for regular pay, but remained above the Bank of England's forecast.

3.7 Having begun the financial year at 4.25%, the Bank of England's Monetary Policy Committee (MPC) increased Bank Rate to 5.25% in August 2023 with a 3-way split in the Committee's voting as the UK economy appeared resilient in the face of the dual headwinds of higher inflation and interest rates. Bank Rate was maintained at 5.25% through to March 2024. The vote at the March was 8-1 in favour of maintaining rates at this level, with the single dissenter preferring to cut rates immediately by 0.25%. Although financial markets shifted their interest rate expectations downwards with expectations of a cut in June, the MPC's focus remained on assessing how long interest rates would need to be restrictive in order to control inflation over the medium term.

3.8 In the Bank's quarterly Monetary Policy Report (MPR) released in August 2023 the near-term projection for services price inflation was revised upwards, goods price inflation widespread across products, indicating stronger domestic inflationary pressure with second-round effects in domestic prices and wages likely taking longer to unwind than they did to emerge. In the February 2024 MPR the Bank's expectations for the UK economy were positive for the first half of 2024, with a recovery from the mild recession in calendar H2 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.

3.9 Following this MPC meeting, Arlingclose, the authority's treasury adviser, 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 H2 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.

3.10 The US Federal Reserve also pushed up rates over the period, reaching a peak range of between 5.25-5.50% in August 2023, where it has stayed since. US policymakers have maintained the relatively dovish stance from the December FOMC meeting and at the meeting in March, economic projections pointed to interest rates being cut by a total of 0.75% in 2024.

3.11 Following a similarly sharp upward trajectory, the European Central Bank hiked rates to historically high levels over period, pushing its main refinancing rate to 4.5% in September 2023, where it has remained. Economic growth in the region remains weak, with a potential recession on the cards, but inflation remains sticky and above the ECB's target, putting pressure on policymakers on how to balance these factors.

3.12 **Financial markets:** 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 they started declining again before falling sharply in December as falling inflation and dovish central bank attitudes caused financial markets to expect cuts in interest rates in 2024. When it emerged in January 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 50+ bps higher than when it started.

3.13 Over the financial year, the 10-year UK benchmark gilt yield rose from 3.44% to peak at 4.75% in August, before then dropping to 3.44% in late December 2023 and rising again to 3.92% (28th March 2024). The Sterling Overnight Rate (SONIA) averaged 4.96% over the period to 31st March.

3.14 **Credit review:** 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.

3.15 Earlier in the period, S&P revised the UK sovereign outlook to stable and upgraded Barclays Bank to A+. Moody's also revised the UK outlook to stable, Handelsbanken's outlook to negative, downgraded five local authorities, and affirmed HSBC's outlook at stable while upgrading its Baseline Credit Assessment. Fitch revised UOB's and BMO's outlooks to stable.

3.16 In the final quarter of the financial year, Fitch revised the outlook on the UK sovereign rating to stable from negative based on their assessment that the risks to the UK's public finances had decreased since its previous review in October 2022, the time of the mini-budget.

3.17 Moody's, meanwhile, upgraded the long-term ratings of German lenders Helaba, Bayern LB and LBBW on better solvency and capital positions, despite challenges from a slowing German economy and exposure to the commercial real estate sector. Moody's also upgraded or placed on review for an upgrade, Australian banks including ANZ, CBA NAB and Westpac on the back of the introduction of a new bank resolution regime.

3.18 Credit default swap 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. Earlier in the year some Canadian lenders saw their CDS prices rise due to concerns over a slowing domestic economy and housing market, while some German lenders were impacted by similar economic concerns and exposure to commercial real estate towards the end of the period, with LBBW remaining the most elevated.

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

Local Context

3.20 On 31st March 2024, the Authority had net borrowing of £10.09m arising from its revenue and capital income and expenditure. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while balance sheet resources are the underlying resources available for investment. These factors are summarised in Table 1 below.

Table 1: Balance Sheet Summary

	31.3.23 Actual £m	31.3.24 Actual £m
General Fund & Regeneration CFR	20.08	32.65
Total CFR	**20.08**	**32.65**
External borrowing**	-0.15	-7.50
Internal borrowing	19.93	25.15
Less: Usable reserves	-13.49	-11.96
Less: Working capital	-3.10	-3.10
Net borrowing	**3.34**	**10.09**

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

3.21 The treasury management position at 31st March and the change during the year is shown in Table 2 below.

Table 2: Treasury Management Summary

	31.3.23 Balance £m	Movement £m	31.3.24 Balance £m	31.3.24 Rate %
Long-term borrowing				
- PWLB				
- LOBOs				
- Other				
Short-term borrowing	3.75	3.75	7.50	
Total borrowing	**3.75**	**3.75**	**7.50**	**5.51%**
Long-term investments				
Short-term investments	1.00	-1.00	0.00	5.00%
Cash and cash equivalents				
Total investments	**1.00**	**-1.00**	**0.00**	
Net borrowing	**2.75**	**4.75**	**7.50**	

Borrowing Strategy and Activity

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

3.23 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, reaching April 2023 lows in December 2023 before rebounding to an extent in the first three months of 2024. Gilt yields have remained volatile, seeing upward pressure from perceived sticker inflation at times and downward pressure from falling inflation and a struggling economy at other times.

3.24 On 31st December, the PWLB certainty rates for maturity loans were 4.74% for 10-year loans, 5.18% for 20-year loans and 5.01% for 50-year loans. Their equivalents on 31st March 2023 were 4.33%, 4.70% and 4.41% respectively.

3.25 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 are expected to fall back to more normal market levels in April 2024.

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

3.27 **Loans Portfolio:** At 31st March the Authority held £7.5m of loans, as part of its strategy for funding previous and current years' capital programmes. Outstanding loans on 31st March 2024 are summarised in Table 3 below.

Table 3: Borrowing Position

	31.3.23 Balance £m	**Net Movement £m**	**31.3.24 Balance £m**	**31.3.24 Weighted Average Rate %**	**31.4.24 Weighted Average Maturity (years)**
Public Works Loan Board					
Banks (LOBO)					
Banks (fixed-term)					
Local authorities (long-term)					
Local authorities (short-term)	3.75	3.75	7.50	5.51%	0.5
Total borrowing	**3.75**	**3.75**	**7.50**		

Treasury Investment Activity

3.28 The CIPFA Treasury Management in the Public Services Code of Practice and Cross-Sectoral Guidance Notes (revised in 2021) defines treasury management investments as investments that arise from the organisation'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.

3.29 The Authority does not hold any invested funds, representing income received in advance of expenditure plus balances and reserves held. During the period, the Authority's investment balances ranged between £1.0 and £6.5 million due to timing differences between income and expenditure. The investment position is shown in table 4 below.

Table 4: Treasury Investment Position

	31.3.23	Net	31.3.24	31.3.24	31.3.24
	Balance	Movement	Balance	Income Return	Weighted Average Maturity
	£'000	£'000	£'000	%	days
Banks & building societies (unsecured)					
Banks & building societies (secured deposits)					
Covered bonds (secured)					
Government	1.00	-1.00	0.00		6 days
Local authorities and other govt entities					
Corporate bonds and loans					
Money Market Funds					
Total investments	**1.00**	**-1.00**	**0.00**		

3.30 Both the CIPFA Code and government guidance require the Authority 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 Authority's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

3.31 As demonstrated by the liability benchmark in this report, the Authority expects to be a long-term investor and treasury investments therefore include both short-term low risk instruments to manage day-to-day cash flows and longer-term instruments where limited additional risk is accepted in return for higher investment income to support local public services.

3.32 Bank Rate increased by 1% over the period, from 4.25% at the beginning of April 2023 to

5.25% by the end 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.

Non-Treasury Investments

3.33 The definition of investments in the Treasury Management Code now covers all the financial assets of the Authority as well as other non-financial assets which the Authority 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).

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

Treasury Performance

3.35 The Authority measures the financial performance of its treasury management activities both in terms of its impact on the revenue budget and its relationship to benchmark interest rates, as shown in table 5 below.

Table 5: Performance

	Actual £m	**Budget £m**	**Over/ under**
Government (incl. local authorities)	**7.50**	**10.00**	**2.50**
Total borrowing	**7.50**	**10.00**	**2.50**
Short-term Investments	0.00	0.00	0.00
Total treasury borrowing	**7.50**	**10.00**	2.50

MRP Regulations

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

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

Compliance

3.38 The Director of Resources and Section 151 officer reports that some treasury management activities undertaken during the year complied fully with the principles in the Treasury Management Code, while lending to Bromsgrove District Council didn't comply, and the Authority's approved Treasury Management Strategy. Compliance with specific investment limits is demonstrated in table 6 below.

Table 6: Investment Limits

	2023/24 Maximum	**31.3.24 Actual**	**2023/24 Limit**	**Complied?** Yes/No
Any single organisation, except the UK Government	£4m each			
UK Central Government	Unlimited			
Unsecured investments with banks and building societies	**£2.5m in total**			
Loans to unrated corporates	**£1m in total**			
Money Market Funds	**£20m in total**			
Foreign countries	**£5m per country**			
Real Estate Investment Trusts	**£2.5m in total**			

3.39 Compliance with the Authorised Limit and Operational Boundary for external debt is demonstrated in table 7 below.

Table 7: Debt and the Authorised Limit and Operational Boundary

	2023/24 Maximum	31.3.24 Actual	2023/24 Operational Boundary	2023/24 Authorised Limit	Complied? Yes/No
Borrowing	50.00	7.50	50.00	55.00	Yes
PFI and Finance Leases	1.50	0	1.50	1.50	Yes
Total debt	**51.50**	**7.50**	**51.50**	**56.50**	

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

Treasury Management Prudential Indicators

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

Liability Benchmark

3.42 This indicator compares the Authority’s actual existing borrowing against a liability benchmark that has been calculated to show the lowest risk level of borrowing. The liability benchmark is an important tool to help establish whether the Council is likely to be a long-term borrower or long-term investor in the future, and so shape its strategic focus and decision making. It represents an estimate of the cumulative amount of external borrowing the Council must hold to fund its current capital and revenue plans while keeping treasury investments at the minimum level of £2m required to manage day-to-day cash flow.

	31.3.23 Actual	31.3.24 Actual	31.3.25 Forecast	31.3.26 Forecast
Loans CFR	20.08	32.65	33.77	34.54
Less: Usable Reserves	-13.49	-11.96	-11.72	-11.14
Less: Working Capital	-3.10	-3.10	-3.10	-3.10
Net loans requirement	3.49	17.59	18.95	20.30
Plus: Liquidity allowance	0.20	0.20	0.20	0.20
Liability benchmark	**3.69**	**17.79**	**19.15**	**20.50**
Existing borrowing	**0.15**	**7.50**	**10.20**	**12.54**

3.43 Following on from the medium-term forecast above, the long-term liability benchmark assumes capital expenditure funded by borrowing of £12.54m, minimum revenue provision on new capital expenditure based on a 40 year asset life and income, expenditure and reserves all increasing by inflation of 2% p.a. This is shown in the chart below together with the maturity profile of the Authority's existing borrowing.

Maturity Structure of Borrowing

3.44 This indicator is set to control the Authority's exposure to refinancing risk. The upper and lower limits on the maturity structure of all borrowing were:

	Upper Limit	Lower Limit	31.3.24 Actual	Complied?
Under 12 months	100%	0%	100%	Yes
12 months and within 24 months	100%	0%	0%	Yes
24 months and within 5 years	100%	0%	0%	Yes
5 years and within 10 years	100%	0%	0%	Yes
10 years and above	100%	0%	0%	Yes

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

Long-term Treasury Management Investments

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

	2023/24	2024/25	2025/26	No fixed date
Limit on principal invested beyond year end	£1.5m	£1.0m	£0.5m	
Actual principal invested beyond year end	0	0	0	
Complied?	Yes	Yes	Yes	

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

Additional indicators

Security**:**

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

	2023/24 Target	31.3.24 Actual	Complied?
Portfolio average credit rating	A	-	Yes

Liquidity**:**

3.49 The Authority has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments within a rolling three-month period, without additional borrowing.

	2023/24 Target	31.3.24 Actual	Complied?
Total cash available within 3 months	£2.5m	£2.5m	Yes
Total sum borrowed in past 3 months without prior notice	Nil	£4.0m	Yes

Interest Rate Exposures:

3.50 This indicator is set to control the Authority's exposure to interest rate risk.

Interest rate risk indicator	2023/24 Target	31.3.24 Actual	Complied?
Upper limit on one-year revenue impact of a 1% rise in interest rates	500,000	0	Yes
Upper limit on one-year revenue impact of a 1% fall in interest rates	500,000	0	Yes

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

	31/3/23	31/3/24
Bank Rate	4.25%	5.25%
1-year PWLB certainty rate, maturity loans	4.78%	5.36%
5-year PWLB certainty rate, maturity loans	4.31%	4.68%
10-year PWLB certainty rate, maturity loans	4.33%	4.74%
20-year PWLB certainty rate, maturity loans	4.70%	5.18%
50-year PWLB certainty rate, maturity loans	4.41%	5.01%

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

4. IMPLICATIONS

Legal Implications

4.1 A number of statutes governing the provision of services covered by this report contain express powers or duties to charge for services. Where an express power to charge does not exist the Council has the power under Section 111 of the Local Government Act 1972 to charge where the activity is incidental or conducive to or calculated to facilitate the Councils statutory function.

Service / Operational Implications

4.2 Monitoring is undertaken to ensure that income targets are achieved, with Treasury Management activities taking place on a daily basis.

Customer / Equalities and Diversity Implications

4.3 The only impact of treasury transactions is in respect of ethical investment linked to the Councils investment counterparties. Presently the Council has a limited counterparty list based on financial risk to the Authority.

5. RISK MANAGEMENT

5.1 There is always significant risk in relation to treasury transactions, this is why Councils appoint Treasury advisors, which in the case of Bromsgrove is Arlingclose. In addition, there is the requirement in this area to provide an Annual Strategy report containing indicators/limits that must be met, a quarterly update and closure report all of which must be reported to full Council.

6. APPENDICES

None

7. BACKGROUND PAPERS

MTFP 2023/24 – February 2023 which contains the years Capital Strategy, Treasury Management Strategy and MRP Policy.

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