Treasury Management Strategy
2024 to 2025

CHELTENHAM
BOROUGH COUNCIL

cheltenham.gov.uk

1. Introduction

1.1 Treasury management is the management of the Council's cash flows, borrowing and investments, and the associated risks. Treasury risk 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.

1.2 The Council's Treasury Management Strategy forms a key part of our overall Corporate Planning Framework. It provides a mechanism by which our treasury management decisions can be aligned with our over-arching corporate priorities and objectives over a medium-term planning horizon.

1.3 The Strategy has direct links to the Council's Asset Management Strategy, Commercial Strategy, Capital Strategy and Investment Strategy and forms a key part of the Council's Medium Term Financial Strategy (MTFS) as presented below:

2. Purpose of this strategy

2.1 Our 2024/25 Treasury Management Strategy has been developed, with a focus on working with our partner organisations to lead in future place shaping, investment and regeneration in Cheltenham.

2.2 The key aims of this document are:

- To outline how we invest our money to ensure we have the financial resources to support the key priorities outlined in the 2023-2027 Corporate Plan.
- To set out the key principles on which our borrowing and investment decisions are made, including how security and risk have been assessed in the development of our investments (See Section 5, page XX).
- To present the arrangements for managing and monitoring our treasury management decisions, including assessment of outcomes and the continual alignment to our Corporate Plan (See Section 6, page XX).

3. Why we invest our money

2.1 The Council invests its money for three broad purposes:

- because it has surplus cash as a result of its day-to-day activities, for example when income is received in advance of expenditure (known as treasury management investments)
- to directly support local public services by lending to other organisations (service investments), and
- to invest in community led and sustainable place shaping, regeneration and economic development of our town (known as growth investments).

Our Investment Strategy outlines the principles and arrangements in place for the second two categories of investment. This strategy focuses on our approach to the first category.

4. How we borrow money

Our Borrowing

4.1 The council currently holds debt of £184.497m as at 31st January 2024. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while balance sheet resources are the underlying sums available for investment. The Council has an increasing CFR due to the capital programme especially within the HRA capital programme to deliver on our affordable housing target. With minimal investments the council will therefore be required to borrow up to £75m over the forecast period

4.2 CIPFA's Prudential Code for Capital Finance in Local Authorities recommends that the Council's external borrowing should be lower than its highest forecast CFR over the following three years. The table below shows that the Council expects to comply with this recommendation during 2024/25.

4.3 To compare the Council's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing. This assumes that cash and investment balances are kept to a minimum level of £10m at each year-end to maintain sufficient liquidity but minimise credit risk.

4.4 The liability benchmark is an important tool to help establish whether the Council is likely to be a long-term borrower or long-term investor in the future, and so shape its strategic focus and decision making. The liability benchmark itself represents an estimate of the cumulative amount of external borrowing the Council must hold to fund its current capital and revenue plans while keeping treasury investments at the minimum level required to manage day-to-day cash flow. The total forecast net borrowing against the CFR and liability benchmark is set out in the table below for the period of the Medium-Term Financial Strategy.

Table: 1

	31.3.23 Actual £m	31.3.24 Estimate £m	31.3.25 Forecast £m	31.3.26 Forecast £m	31.3.27 Forecast £m
General Fund CFR	109.598	110.189	113.942	116.175	113.908
Housing (HRA) CFR	82.584	98.249	118.526	130.452	158.971
TOTAL CFR	**192.182**	**208.438**	**232.468**	**246.627**	**272.879**
Less: External Borrowing	179.111	193.276	214.864	239.641	268.160
Internal (over) Borrowing	**13.071**	**15.162**	**17.604**	**6.986**	**4.719**
Less: Useable reserves	(4.062)	(2.890)	(3.052)	(2.993)	(2.797)
Less: Working Capital	(21.788)	(27.198)	(29.703)	(19.993)	(18.922)
Investments/ (New Borrowing)	**12.779**	**14.926**	**15.151**	**16.000**	**17.000**
Net Borrowing Requirement	166.332	178.350	199.713	223.641	251.160
Preferred year-end position (Invest)	10.000	10.000	10.000	10.000	10.000
Liability Benchmark (year-end)	**176.332**	**188.350**	**209.713**	**233.641**	**261.160**

Our Borrowing Strategy

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

4.6 Given the significant cuts to public expenditure and in particular to local government funding, the Council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. With short-term interest rates currently lower than long-term rates, it is likely to be more cost effective in the short-term to either use internal resources, or to borrow short-term loans instead. However, if long term rates prove more attractive, then the Council will switch to using the Public Works Loan Board (PWLB) or another lender in the market to fund past and future debt.

In January 2024, the Council replaced £20m of temporary borrowing with a fixed 10 ½ year PWLB Annuity loan at a rate of 4.32%. This will reduce borrowing costs of approximately £200k for 2024/25.

4.7 As a net borrower, the speed of the rise in interest rates has created a budget pressure for the Council during 2023/24 and into 2024/25. It is forecast that the net impact of interest rate rises will require an additional £193k of revenue funding in 2024/25 which is included in the budget proposals. This is a decrease when compared to the 2023/24 budget where £587k of additional cost has had to be funded to cover the borrowings. The 2023/24 forecast is based on the Bank of England rate increasing to 4.25% and remaining there for the full twelve months which was obviously surpassed early in the Summer of 2023.

Ongoing monitoring may determine whether the Council borrows additional sums at long-term fixed rates in 2024/25 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.

4.8 Alternatively, the Council may arrange forward starting loans during 2024/25, where the interest rate is fixed in advance, but the cash is received in later years. This would enable certainty of cost to be achieved without suffering a cost of carry in the intervening period. The Council may also borrow short-term loans to cover unplanned cash flow shortages.

4.9 The main sources of approved long-term and short-term borrowing for Cheltenham Borough Council are:

Sources of borrowing

HM Treasury's PWLB lending facility (formally the Public Works Loan Board):
The Council has previously raised the majority of its long-term borrowing from the PWLB (currently £121.1m) but will consider long-term loans from other sources including banks, pensions and local authorities, and will investigate the possibility of issuing bonds and similar instruments, in order to lower interest costs and reduce over-reliance on one source of funding in line with the CIPFA Code. PWLB loans are no longer available to local authorities planning to buy investment assets primarily for yield; the Council will avoid this activity in order to retain its access to PWLB loans.

Municipal Bonds Agency:
UK Municipal Bonds Agency plc was established in 2014 by the Local Government Association as an alternative to the PWLB. It issues bonds on the capital markets and lends the proceeds to local authorities. This is a more complicated source of finance than the PWLB for two reasons: borrowing authorities will be required to provide bond investors with a guarantee to refund their investment in the event that the agency is unable to for any reason; and there will be a lead time of several months between committing to borrow and knowing the interest rate payable. Any decision to borrow from the Agency will therefore be the subject of a separate report to Cabinet. The Council currently holds no loans from the MBA.

UK Infrastructure Bank Limited:
UK Infrastructure Bank is a government-owned policy bank, launched in 2021 looking to provide £6bn of infrastructure finance to local government over the next 5 years to finance regional and local economic growth, support tackling climate change and the investment in infrastructure assets or in new infrastructure technology. The Council holds no loans with the UK Infrastructure Bank.

LOBOs:
The Council holds £5m of LOBO (Lender's Option Borrower's Option) loans where the lender has the option to propose an increase in the interest rate at set dates, following which the Council has the option to either accept the new rate or to repay the loan at no additional cost. The Council will take the option to repay LOBO loans at no cost if it has the opportunity to do so.

Short-term and variable rate loans:
These loans leave the Council exposed to the risk of short-term interest rate rises and are therefore subject to the limit on the net exposure to variable interest rates in the treasury management indicators. However, the use of short-term loans is currently favourable as borrowing costs are still lower compared with long term rates. Arlingclose forecast a slow decrease in rates in 2024/25. The Council as at end of February 2024 holds £55.5m of these loans.

Debt rescheduling:
The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. Other lenders may also be prepared to negotiate premature redemption terms. The 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 or a reduction in risk.

5. How we invest money

Our Treasury Management investments

5.1 The Council holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Council's investment balance has averaged from as high as £25m and as low as £14.5m. On 31 January 2024, we held £22.039m of treasury investments which are outlined in the table 2 below.

Table: 2

	31 January 2024 Actual Portfolio £m	31 January 2024 Actual Rate %
Treasury investments:		
Glos Airport – Revolving credit facility	1.700	7.25%
Glos Airport – Sub Station/ Radar loans	0.123	2.00%
Glos Airport – Working Capital Loan	5.827	6.25%
Cheltenham Borough Homes (St Georges Place)	1.530	2.40%
Money Market Funds	5.250	5.31%
Cheltenham Borough Homes (St Georges Place) Equity	0.535	1.10%
The Trustees of St. Margaret's Hall	0.034	3.00%
Cheltenham Town FC – Capital Loan	0.040	3.50%
Other Pooled Funds		
CCLA Property Investment Management	3.000	4.60%
CCLA Diversified Income	2.000	2.57%
Schroders Unit Trusts Ltd	2.000	5.04%
Total Treasury investments	**22.039**	**5.06%**

5.2 By the end of the 2023/24 financial year, it is forecast that our investment balance will have reduced as the use of cash liquid accounts i.e., Money Market Funds to reduce the need to borrow at year end. The table below shows the forecast between short- and longer-term holdings. Future capital receipts are not factored in until they are received.

	31.3.2023 Actual £m	31.03.2024 Forecast £m	31.03.2025 Budget £m	31.03.2026 Budget £m	31.03.2027 Budget £m
Near-term investments	6.130	1.000	1.000	1.000	1.000
Longer-term investments	14.625	16.789	16.500	16.500	16.500
Total	**23.267**	**13.942**	**14.756**	**15.710**	**16.663**

Our Treasury Management investments

5.3 The Council's policy on treasury investments, in line with the CIPFA Code, is to prioritise security and liquidity over yield; that is to focus on minimising risk rather than maximising returns. Cash that is likely to be spent in the near term is invested securely, for example with the government, other local authorities or selected high-quality banks, to minimise the risk of loss. Money that will be held for longer terms is invested more widely, including in bonds, shares and property, to balance the risk of loss against the risk of receiving returns below inflation. Both near-term and longer-term investments may be held in pooled funds, where an external fund manager makes decisions on which particular investments to buy, and the Council may request its money back at short notice. Where balances are expected to be invested for more than one year, the Council will aim to achieve a total return that is equal or higher than the prevailing rate of inflation, in order to maintain the spending power of the sum invested. The council aims to be a responsible investor and will consider environmental, social and governance (ESG) issues when investing.

5.4 ESG policy: Environmental, social and governance (ESG) considerations are increasingly a factor in global investors' decision making, but the framework for evaluating investment opportunities is still developing and therefore the Council's ESG policy does not currently include ESG scoring or other real-time ESG criteria at an individual investment level. When investing in banks and funds, the council will prioritise banks that are signatories to the UN Principles for Responsible Banking and funds operated by managers that are signatories to the UN Principles for Responsible Investment, the Net Zero Asset Managers Alliance and/or the UK Stewardship Code.

5.5 Under the new IFRS 9 standard, the accounting for certain investments depends on the Council's "business model" for managing them. The Council aims to achieve value from its treasury investments by a business model of collecting the contractual cash flows and therefore, where other criteria are also met, these investments will continue to be accounted for at amortised cost.

5.6 The Council may invest its surplus funds with any of the counterparty types in table 3 below, subject to the cash limits (per counterparty) and the time limits shown.

5.7 The Gloucestershire Airport and Cheltenham Borough Homes loans limits will be recalculated during 2024, when a full review will be carried out.

Table: 3

Sector	Time limit	Counterparty limit	Sector limit
The UK Government	50 years	Unlimited	n/a
Local authorities & other government entities	25 years	£4m	Unlimited
Secured investments *	20 years	£4m	Unlimited
Banks (unsecured) *	13 months	£1m	Unlimited
Building societies (unsecured) *	13 months	£1m	£10m
Registered providers (unsecured) *	5 years	£2m	£5m
Money market funds *	n/a	£5m	Unlimited
Strategic pooled funds	n/a	£5m	£10m

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

Bank & Building Society unsecured

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

Bank & Building Societies secured

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

Government

Loans, bonds, and bills issued or guaranteed by national governments, regional and local authorities and multilateral development banks. Investments with the UK Government are deemed to be zero credit risk due to its ability to create additional currency and therefore may be made in unlimited amounts for up to 50 years.

Corporates

Loans, bonds and commercial paper issued by companies other than banks and registered providers. These investments are not subject to bail-in but are exposed to the risk of the company going insolvent. Loans to unrated companies will only be made either following an external credit assessment as part of a diversified pool in order to spread the risk widely.

Registered providers

Loans and bonds issued by, guaranteed by or secured on the assets of registered providers of social housing, formerly known as housing associations. These bodies are tightly regulated by the Regulator of Social Housing (in England) and, as providers of public services; they retain the likelihood of receiving government support if needed.

Money Market funds

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

Strategic pooled funds

Bond, equity and property funds that offer enhanced returns over the longer term but are more volatile in the short term. These allow the Council to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Council's investment objectives will be monitored regularly.

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

Operational bank accounts

The Council banks with Lloyds (Lloyds Banking Group). On adoption of this Strategy, it will meet the minimum credit criteria of A- (or equivalent) long term. It is the Councils intention that even if the credit rating of Lloyds Bank falls below the minimum criteria A- the bank will continue to be used for short term liquidity requirements (overnight and weekend investments) and business continuity arrangements.

Policy investments
Loans, bonds and commercial paper issued by companies other than banks and registered providers. These investments are not subject to bail-in but are exposed to the risk of the company going insolvent. Loans to unrated companies will only be made either following an external credit assessment as part of a diversified pool in order to spread the risk widely.

- Gloucestershire Everyman Theatre £100k up to one year duration
- Gloucestershire Everyman Theatre £286k Non-specified duration
- Ubico Limited £500k up to one year duration
- Workshop Cheltenham £6.1m Non-Specified
- Cheltenham Town Football Club £40k Non-Specified
- Cheltenham BID £100k up to one year duration
- The Cheltenham Trust £100k up to one year duration
- Publica Group £100k up to one year duration
- Cheltenham Borough Homes £97m Non-specified duration[1]
- Cheltenham Borough Homes £10m Equity Non- Specified duration[2]
- Cheltenham Borough Homes £500k up to one year
- Gloucestershire Airport Limited £9m up to one year
- Gloucestershire Airport Limited £7.250m Non-specified duration
- Folk2Folk (Peer to Peer lending) £575k Non-specified duration[3]

[1] Cheltenham Borough Homes is looking to borrow £90m and a further

[2] £10m Equity Investment from the council to assist in three areas over the coming years to provide substantial new housing in the town by providing Private Rented Sector (PRS) housing, purchasing 106 sites and building new homes. The drawdown of the loans will be over a period of 40 years.

[3] Folk2Folk is a peer to peer lending platform in which the council can lend to support local, rural and entrepre¬neurial businesses £575,000 with a capped limit of £100,000 per loan application, up to a maximum of 5 years. Interest rates earned can be between 4.5% and up to 9% per annum.

Renewable Energy investments

Over recent years significant investments from Local Authorities in the Renewable Energy markets have occurred by way of investing in an energy bond. Currently the council has approved the use of Corporate Bonds and has used them on a regular basis but only for a maximum of two years previously. To be able to potentially invest in Green Renewable energy recommendation was made following consultation with members of the Treasury Management Panel on the 5 June 2017 and approved by Council on 24 July 2017 that up to £2m in relation to Green Investment bonds can be invested up to five years.

Within our treasury management investments, it is critical to get the right balance between social, environmental and financial factors when assessing the investment, we make. Full Council noted in December 2023 that our exposure to gas and oil investments currently stands at £120K down from £173k this time last year. This is part of the Schroder Income Maximiser Fund and makes up 1.71% (2.5% in 2023) of the £7m we have invested in Pooled Funds. However, the current capital value of the fund is valued £493k less than the original £2m invested. Given our current climate priorities, assurance was provided to Council that we are looking to take steps to ensure our investments are contributing to these goals. We are committed in the longer term to divesting from oil and gas but need to balance these priorities with ensuring we are making the right financial decisions to safeguard our residents, businesses and communities. We will continue to closely monitor the performance of this fund and when it is financially prudent to do so, will consider the climate implications of how we invest this money in the future.

Monitoring our Treasury Management Investments

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

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

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

5.10 The Council understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations, in which it invests, including credit default swap prices, financial statements, information on potential government support and reports in the quality financial press. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may meet the credit rating criteria.

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

5.12 In order to monitor this, we have set cash limits on the credit quality of the investments.

	Cash limit
Total long-term investments	**£20m**
Total investments without credit ratings or rated below A- (except UK Government and local authorities)	**£10m**
Total investments (except pooled funds) with institutions domiciled in foreign countries rated below AA+	**£10m**

Investment Limits

5.13 The Council's revenue reserves available to cover investment losses are forecast to be £3.8 million on 31st March 2024. In order that no more than the available reserves will be put at risk in the case of a single default, the maximum that will be lent to any one organisation (other than the UK Government) will be £4 million. A group of banks under the same ownership will be treated as a single organisation for limit purposes. Limits will also be placed on fund managers, investments in brokers' nominee accounts, foreign countries and industry sectors as below. Investments in pooled funds and multilateral development banks do not count against the limit for any single foreign country, since the risk is diversified over many countries.

Table 4: Investment limits

	Cash limit
Any single organisation, except the UK Central Government	£1m each
UK Central Government	unlimited
Any group of organisations under the same ownership	£1m per group
Any group of pooled funds under the same management	£5m per manager
Foreign countries	£1m per country
Registered providers	£2m in total
Unsecured investments with building societies	£1m in total
Loans to unrated corporates – Renewable Energy	£4m in total- £2m max in each
Money Market Funds	£5m per MMF

5.14 The Council uses purpose-built cash flow forecasting to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a prudent basis to minimise the risk of the Council being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Council's medium term financial plan and cash flow forecast.

6. Treasury Management Indicators

6.1 The Council measures and manages its exposures to treasury management risks using the following indicators.

Security

The Council 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.

	Target
Portfolio average credit rating	**A -**

Interest rate exposures

This indicator is set to control the Council's exposure to interest rate risk. The upper limits on fixed and variable rate interest exposures, expressed as the proportion of net principal borrowed will be:

	2022/23	2023/24	2024/25
Upper limit on fixed interest rate exposure	**100%**	**100%**	**100%**
Upper limit on variable interest rate exposure	**75%**	**75%**	**75%**

Fixed rate investments and borrowings are those where the rate of interest is fixed for at least 12 months, measured from the start of the financial year or the transaction date if later. All other instruments are classed as variable rate.

Maturity structure of borrowing

This indicator is set to control the Council's exposure to refinancing risk. The upper and lower limits on the maturity structure of fixed rate borrowing will be:

	Upper	Lower
Under 12 months	**50%**	**0%**
12 months and within 24 months	**50%**	**0%**
24 months and within 5 years	**100%**	**0%**
5 years and within 10 years	**100%**	**0%**
10 years and within 20 years	**100%**	**0%**
20 years and within 30 years	**100%**	**0%**
30 years and within 40 years	**100%**	**0%**
40 years and above	**100%**	**0%**

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.

Principal sums invested for periods longer than 364 days

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 will be:

	2023/24	2024/25	2025/26
Limit on principal invested beyond one year	**£20m**	**£20m**	**£20m**

7. Related Matters

7.1 There are a number of additional items that the Council is obliged by CIPFA or DLUHC to include in its Treasury Management Strategy.

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

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

Policy on apportioning interest to the HRA
On 1st April 2012, the Council notionally split each of its existing long-term loans into General Fund and HRA pools. In the future, new long-term loans borrowed will be assigned in their entirety to one pool or the other. Interest payable and other costs/ income arising from long-term loans (e.g., premiums and discounts on early redemption) will be charged/ credited to the respective revenue account. Differences between the value of the HRA loans pool and the HRA's underlying need to borrow (adjusted for HRA balance sheet resources available for investment) will result in a notional cash balance which may be positive or negative. This balance will be measured each year and interest transferred between the General Fund and HRA at the Council's average interest rate on treasury investments excluding strategic pooled funds, adjusted for credit risk.

Markets in Financial Instruments Directive
The Council has opted up to professional client status with its providers of financial services, including advisers, banks, brokers and fund managers, allowing it access to a greater range of services but without the greater regulatory protections afforded to individuals and small companies. Given the size and range of the Council's treasury management activities, the Chief Financial Officer believes this to be the most appropriate status.

Investment advisers
The Council recently re-appointed Arlingclose Limited as treasury management advisers for three years plus the option for a further two years after a full joint tender with Cotswold District Council, Forest of Dean District Council and West Oxfordshire District Council. The new contract commenced from 1st March 2023 and will run to at least 28th February 2026.

Investment of money borrowed in advance of need

The Council may, from time to time, borrow in advance of need, where this is expected to provide the best long-term value for money. Since amounts borrowed will be invested until spent, the Council is aware that it will be exposed to the risk of loss of the borrowed sums, and the risk that investment and borrowing interest rates may change in the intervening period. These risks will be managed as part of the Council's overall management of its treasury risks.

The total amount borrowed will not exceed the authorised borrowing limit of £300m. The maximum period between borrowing and expenditure is expected to be three years, although the Council is not required to link particular loans with particular items of expenditure.

Financial Implications

The budget for investment income in 2024/25 is forecast to be £920,422 based on an average investment portfolio of £18.178 million at an interest rate of 5.06%. For the purpose of setting the budget, it has been assumed that new treasury investments will be made at an average rate of 5% to 5.5%. On top of this interest received on third parties' loans amounts to £279k.

The estimated budget for debt interest to be paid in 2024/25 is forecast to be £6.884 million, based on an average debt portfolio of £177.1m at an average interest rate of 3.86% (3.15% 23/24). The HRA will reimburse the General Fund £3.319m for its share of the debt it holds as of 1 April 2024. If actual levels of investments and borrowing, and actual interest rates differ from those forecast, performance against budget will be correspondingly different.

8. Alternative options

The CIPFA Code does not prescribe any particular treasury management strategy for local authorities to adopt. The S151 Officer, having consulted the Cabinet Member for Finance and Assets, believes that the above strategy represents an appropriate balance between risk management and cost effectiveness. Some alternative strategies, with their financial and risk management implications, are listed below.

Alternative	Impact on income and expenditure	Impact on risk management
Invest in a narrower range of counterparties and/or for shorter times	Interest income will be lower	Lower chance of losses from credit related defaults, but any such losses may be greater
Invest in a wider range of counterparties and/or for longer times	Interest income will be higher	Increased risk of losses from credit related defaults, but any such losses may be smaller
Borrow additional sums at long-term fixed interest rates	Debt interest costs will rise; this is unlikely to be offset by higher investment income	Higher investment balance leading to a higher impact in the event of a default; however long-term interest costs may be more certain
Borrow short-term or variable loans instead of long-term fixed rates	Debt interest costs will initially be lower	Increases in debt interest costs will be broadly offset by rising investment income in the medium term, but long-term costs may be less certain
Reduce level of borrowing	Saving on debt interest is likely to exceed lost investment income	Reduced investment balance leading to a lower impact in the event of a default; however long-term interest costs may be less certain

Appendix 1 - Arlingclose Limited Economic & Interest Rate Forecast February 2024

Economic background:

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.

The Bank of England (BoE) increased Bank Rate to 5.25% in August 2023, before maintaining this level for the rest of 2023 and also in February 2024. In February 2024, members of the BoE's Monetary Policy Committee voted 6-3 in favour of keeping Bank Rate at 5.25%. Two dissenters wanted to increase rates by another 0.25% and one wanted to see a reduction of 0.25%.

Recent reports showed lower-than-expected CPI inflation, due to decreases in fuel, core goods, and services prices. Despite this, inflation for services prices is still notably high. Twelve-month CPI inflation fell to 4.0% in December 2023, falling below the forecasts made in the November Report. CPI inflation is predicted to hit the 2% target briefly in Q2 of 2024, then rise in the latter half of the year due to diminishing declines in direct energy prices. Based on predictions tied to a lower expected Bank Rate, CPI inflation is seen at about 2.75% by year's end, staying above the target for most of the forecast period. This trend suggests ongoing domestic inflation pressures, even as the economy starts to show more slack. Inflation is estimated at 2.3% in two years and 1.9% in three, reflecting these sustained pressures.

ONS figures showed the UK economy contracted by 0.1% between July and September 2023. The BoE forecasts GDP will likely stagnate through 2024. The BoE forecasts that higher interest rates will constrain GDP growth, which will remain weak over the entire forecast horizon.

The labour market appears to be loosening, but only very slowly. The unemployment rate rose slightly to 4.2% between June and August 2023, from 4.0% in the previous 3-month period, but the lack of consistency in the data between the two periods made comparisons difficult. Earnings growth has remained strong but has showed some signs of easing; regular pay (excluding bonuses) was up 7.3% over the period and total pay (including bonuses) up 7.2%. Adjusted for inflation, regular pay was 1.4% and total pay 1.3%. Looking forward, the MPR showed the unemployment rate is expected to be around 4.25% in the second half of calendar 2023, but then rising steadily over the forecast horizon to around 5% in late 2025/early 2026.

Credit outlook:

Credit Default Swap (CDS) prices were volatile during 2023, spiking in March on the back of banking sector contagion concerns following the major events of Silicon Valley Bank becoming insolvent and the takeover of Credit Suisse by UBS. After then falling back in Q2 of calendar 2023, in the second half of the year, higher interest rates and inflation, the ongoing war in Ukraine, and now the Middle East, have led to CDS prices increasing steadily.

On an annual basis, CDS price volatility has so far been lower in 2023 compared to 2022, but this year has seen more of a divergence in prices between ringfenced (retail) and non-ringfenced (investment) banking entities once again.

Moody's revised its outlook on the UK sovereign to stable from negative to reflect its view of restored political predictability following the volatility after the 2022 mini-budget. Moody's also affirmed the Aa3 rating in recognition of the UK's economic resilience and strong institutional framework.

Following its rating action on the UK sovereign, Moody's revised the outlook on five UK banks to stable from negative and then followed this by the same action on five rated local authorities. However, within the same update the long-term ratings of those five local authorities were downgraded.

There remain competing tensions in the banking sector, on one side from higher interest rates boosting net income and profitability against another of a weakening economic outlook and likely recessions that increase the possibility of a deterioration in the quality of banks' assets.

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

Interest rate forecast (February 2023):

The Council's treasury management adviser Arlingclose forecasts that Bank Rate will remain at 5.25% until around August/September 2024, as the MPC seeks to maintain tighter financial conditions. Monetary policy will remain tight as inflation is expected to moderate to target slowly, although some wage and inflation measures are below the Bank's last forecasts.

Please see Arlingclose's interest rate forecasts over the next two years

	Current	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26
Official Bank Rate													
Upside risk	0.00	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.75	0.75	1.00	1.00	1.00
Central Case	5.25	5.25	5.25	5.00	4.75	4.25	3.75	3.25	3.00	3.00	3.00	3.00	3.00
Downside risk	0.00	-0.25	-0.50	-0.75	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
3-month money market rate													
Upside risk	0.00	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.75	0.75	1.00	1.00	1.00
Central Case	5.40	5.40	5.30	5.15	4.80	4.30	4.10	3.80	3.50	3.25	3.15	3.10	3.10
Downside risk	0.00	-0.25	-0.50	-0.75	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
1yr money market rate													
Upside risk	0.10	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30
Central Case	0.30	0.75	0.70	0.70	0.70	0.70	0.70	0.70	0.70	0.70	0.70	0.70	0.70
Downside risk	-0.05	-0.15	-0.15	-0.15	-0.15	-0.15	-0.15	-0.15	-0.15	-0.15	-0.15	-0.15	-0.15
5yr gilt yield													
Upside risk	0.00	0.75	0.85	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Central Case	4.14	3.75	3.70	3.65	3.60	3.50	3.40	3.30	3.30	3.30	3.30	3.35	3.40
Downside risk	0.00	-0.75	-0.85	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
10yr gilt yield													
Upside risk	0.00	0.75	0.85	0.85	0.90	0.90	0.90	0.90	1.00	1.00	1.00	1.00	1.00
Central Case	3.96	3.80	3.80	3.80	3.75	3.70	3.65	3.65	3.65	3.65	3.65	3.70	3.75
Downside risk	0.00	-0.75	-0.85	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
20yr gilt yield													
Upside risk	0.00	0.75	0.85	0.85	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Central Case	4.00	4.40	4.30	4.25	4.25	4.20	4.20	4.20	4.20	4.20	4.20	4.25	4.25
Downside risk	0.00	-0.75	-0.85	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
50yr gilt yield													
Upside risk	0.00	0.75	0.85	0.85	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Central Case	3.94	3.90	3.90	3.90	3.90	3.90	3.90	3.90	3.90	3.95	3.95	3.95	3.95
Downside risk	0.00	-0.75	-0.85	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00

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