Appendix I - Draft Treasury Management Strategy Statement 2025/26

To note information highlighted will be updated after 31/12/2024

Introduction

1.0 Treasury management is the management of the Council's cash flows, borrowing and investments, and the associated risks. The Council has borrowed and 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 financial risk are therefore central to the Council's prudent financial management.

2.0 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.

3.0 Investments held for service purposes are considered separately within the Investment Strategy.

External Context

4.0 UK headline consumer price inflation remained around the Bank of England (BoE) target later in the period, falling from an annual rate of 3.2% in March to 2.0% in May and then rebounding marginally to June to 2.2% in July and August, as was expected, due to base effects from energy prices. Core and services price inflation remained higher at 3.6% and 5.6% respectively in August.

5.0 The UK economy continued to expand over the period, albeit slowing from the 0.7% gain in the first calendar quarter to 0.5% (downwardly revised from 0.6%) in the second. Of the monthly figures, the economy was estimated to have registered no growth in July.

6.0 Labour market data was slightly better from a policymaker perspective, showing an easing in the tightness of the job market, with inactivity rates and vacancies declining. However, a degree of uncertainty remains given ongoing issues around the data collected for the labour force survey by the Office for National Statistics. Figures for the three months to July showed the unemployment rate fell to 4.1% (3mth/year) from 4.4% in the previous three-month period while the employment rate rose to 74.8% from 74.3%.

7.0 With headline inflation lower, the BoE cut Bank Rate from 5.25% to 5.00% at the August Monetary Policy Committee (MPC) meeting. The decision was finely balanced, voted by a 5-4 majority with four members preferring to hold at 5.25%. At the September MPC meeting, committee members voted 8-1 for no change at 5.00%, with the lone dissenter preferring Bank Rate to be cut again to 4.75%. The meeting minutes and vote suggested a reasonably hawkish tilt to rates, with sticky inflation remaining a concern among policymakers.

8.0 The latest BoE Monetary Policy Report, published in August, showed policymakers expected GDP growth to continue expanding during 2024 before falling back and moderating from 2025 to 2027. Unemployment was forecast to stay around 4.5% while inflation was shown picking up in the latter part of 2024 as the previous years' energy price declines fell out of the figures before slipping below the 2% target in 2025 and remaining there until early 2027. Arlingclose, the authority's treasury adviser, maintained its central view that Bank Rate would steadily fall from the 5.25% peak, with the first cut in August being followed by a series of further cuts, with November 2024 the likely next one, taking Bank Rate down to around 3% by the end of 2025.

9.0 The US Federal Reserve (the Fed) also cut interest rates during the period, reducing the Federal Funds Rate by 0.50% to a range of 4.75%-5.00% at its policy meeting in September. The forecasts released at the same time by the central bank suggested a further 1.00% of easing is expected by the end of the calendar year, followed by the same amount in 2025 and then a final 0.50% of cuts during 2026.

10.0 Having first reduced interest rates in June, the European Central Bank (ECB) held steady in July before cutting again in September, reducing its main refinancing rate to 3.65% and its deposit rate to 3.50%. Unlike the Fed, the ECB has not outlined a likely future path of rates, but inflation projections remain in line with the central bank's previous forecasts where it will remain above its 2% target until 2026 on an annual basis.

Credit outlook

11.0 Credit default swap prices were generally lower at the end of the period compared to the beginning for the vast majority of the names on UK and non-UK lists. Price volatility over the period was also generally more muted compared to previous periods.

12.0 Financial 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.

Interest rate forecast (November 2024)

13.0 the Council's treasury management adviser, Arlingclose, forecasts that Bank Rate will continue to decrease albeit at slower pace and less frequent than initially thought. Arlingclose forecast the Bank of England's Monetary Policy Committee will cut Bank Rate in February 2025 and then every quarter to 3.75% by December 2025. The Rate is expected to remain at 3.75% over the medium term.

14.0 Arlingclose expects long-term gilt yields to rise to reflect the change in the UK and US Government Administrations.. Yields will remain volatile as the market digests the impact of policy changes caused by monetary and fiscal changes passed by the new Administrations. As ever, there will undoubtedly be short-term volatility due to economic and political uncertainty and events.

15.0 For the purpose of setting the budget, it has been assumed that new treasury investments will be made at an average rate of 3.9%, and that new long-term loans will be borrowed at an average rate of 5.2% in 2025/26.

Local Context

16.0 At 31 December 2024, the Council held £x.xm of borrowing (£x.xm long term and £x.xm short term) and £x.xm of cash investments. This is set out in further detail at ***Appendix 2***. Forecast changes in these sums are shown in the balance sheet analysis in table 1 below.

Table 1: Balance sheet summary and forecast

£m	31/03/2024 Actual	31/03/2025 Forecast	31/03/2026 Estimated	31/03/2027 Estimated	31/03/2028 Estimated	31/03/2029 Estimated
Capital Financing Requirement	1,236.6	1,377.7	1,610.8	1,647.2	1,649.3	1,626.2
Other debt liabilities*	32.5	28.5	24.7	22.7	20.4	17.0
Loans CFR	**1,269.1**	**1,406.2**	**1,635.5**	**1,669.9**	**1,669.6**	**1,643.2**
(less) External borrowing**	(814.3)	(800.0)	(681.3)	(658.1)	(634.3)	(620.6)
Internal (Over) Borrowing	**422.3**	**577.7**	**929.5**	**989.1**	**1,014.9**	**1,005.6**
(less) Balance Sheet Resources	(517.6)	(486.0)	(560.8)	(511.4)	(459.4)	(451.5)
New borrowing (or Treasury Investments)	**(95.3)**	**91.7**	**368.8**	**477.7**	**555.6**	**554.1**

* Leases and PFI liabilities that form part of the Council's total debt
** shows only loans to which the Council is committed and excludes optional refinancing and new loans

17.0 The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The Council's strategy has been to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing. This means the Council has minimised its interest costs by utilising internal resources over the short term instead of undertaking more expensive external borrowing. As our internal resources continue to be depleted, there is an increasing need for the Council to undertake new external borrowing to fund the capital programme. However, whilst deferring external borrowing and using internal resources minimises debt interest costs, internal resources will need to be replenished at a later date. This could expose the Council to interest rate risk whereby interest rates could be higher (or lower) than the present day.

18.0 CIPFA's *Prudential Code for Capital Finance in Local Authorities* recommends that the Council's total debt should be lower than its highest forecast CFR over the next three years. Table 1 shows that the Council expects to comply with this recommendation during 2025/26.

19.0 The Council will need to borrow up to £554.1m over the forecast period to support the financing of the capital programme. Table 2 sets out the Councils current and future years capital programme and capital financing based on Period 6 data from Programme Managers.

Table 2: Capital Programme

Capital Expenditure & Financing (£m)	2024/25 Forecast	2025/26 Estimated	2026/27 Estimated	2027/28 Estimated	2028/29 Estimated	Total 2024/25-2028/29
Corporate Landlord	14.9	21.8	13.5	28.2	0.5	**78.9**
Housing GF	79.3	75.7	30.7	3.6	0.0	**189.3**
Schools	20.7	21.8	26.1	3.5	0.0	**72.1**
Regeneration	64.3	117.2	7.3	0.0	0.0	**188.8**
Public Realm	25.4	12.1	1.1	1.0	6.0	**45.6**
South Kilburn	33.6	3.9	3.9	0.0	0.0	**41.4**
St Raphael's	0.5	3.2	3.9	12.5	0.0	**20.1**
HRA	48.2	51.1	19.7	0.0	0.0	**119.0**
Total Capital Expenditure	**286.9**	**306.8**	**106.2**	**48.8**	**6.5**	**755.2**
Grants	44.5	28.3	25.8	3.2	0.0	**101.8**
Section 106	25.5	16.4	0.0	0.0	0.0	**41.9**
Capital Receipts	1.8	28.2	11.2	0.0	0.0	**41.2**
Earmarked Reserves	1.9	1.3	1.4	0.0	0.0	**4.6**
Major Repairs Reserve	18.9	21.1	2.3	0.0	0.0	**42.3**
Revenue Contributions	10.3	0.5	7.7	0.5	0.5	**19.5**
Borrowing	184.0	211.0	57.8	45.1	6.0	**503.9**
Total Capital Financing	**286.9**	**306.8**	**106.2**	**48.8**	**6.5**	**755.2**

20.0 Table 3 details the cost of delivering the Council's proposed capital programme as well as servicing existing debt relating to past capital programmes.

Table 3: Capital financing costs

Capital Financing Costs (£m)	2024/25 Forecast	2025/26 Estimated	2026/27 Estimated	2027/28 Estimated	2028/29 Estimated
Total Gross External Debt Interest (Current and New Debt)	**34.8**	**44.6**	**46.8**	**50.3**	**51.4**

Total Interest Payable & Expenses	**36.6**	**45.9**	**47.9**	**51.4**	**52.5**
Total Interest Receivable	**(25.0)**	**(28.6)**	**(29.8)**	**(31.7)**	**(32.7)**
Net Interest	**11.6**	**17.4**	**18.1**	**19.7**	**19.7**
MRP (Excluding PFI)	15.1	17.3	18.7	21.0	23.2
Total Interest & MRP	**26.8**	**34.7**	**36.8**	**40.7**	**43.0**
Revenue Contributions to Capital Programme	**8.5**	**9.0**	**3.5**	**3.5**	**4.5**
Total Capital Financing Costs	**35.3**	**43.7**	**40.3**	**44.2**	**46.5**

21.0 Delivering a capital programme in environment of rising construction costs, high interest rates relative to pre-Ukraine period means that capital financing costs are expected to increase over the capital investment period as new loans are raised to fund the capital programme's borrowing requirement as set out in Table 2. The cost of new loans is based on an interest rate of 5.2%. The Council also has an ongoing obligation to service existing long dated fixed rate debt that has been raised secured to fund capital programmes of the past. The increase in capital financing costs is also attributable to Minimum Revenue Provision (MRP), a Statutory charge to the Revenue Account for the repayment of debt. MRP is increasing due to new capital spend that is being financing through borrowing, as well as existing borrowing associated with past capital programmes that requires to be repaid over the life of the assets that have enhanced or constructed. The Council uses the annuity method to determine the MRP charge, which results in a lower charge in the earlier period of the repayment schedule but increases over time.

22.0 To ensure financial resilience and sustainability, these emerging pressures are being built into the Council's Medium-Term Financial Strategy. Through this proactive approach, the Council aims to maintain a balanced budget while continuing to invest in essential infrastructure and services for the community through the capital programme.

Liability Benchmark

23.0 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 to maintain sufficient liquidity but minimise credit risk.

24.0 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.

Table 4: Prudential Indicator: Liability benchmark

Liability Benchmark (£m)	2024/25	2025/26	2026/27	2027/28	2028/29
	Forecast	Estimated	Estimated	Estimated	Estimated

Loans CFR	1,377.7	1,610.8	1,647.2	1,649.3	1,626.2
Less Balance Sheet Resources	(470.5)	(470.5)	(470.5)	(470.5)	(470.5)
Net Loan Requirement	**907.3**	**1,140.4**	**1,176.7**	**1,178.8**	**1,155.7**
Plus Liquidity Allowance	20.0	20.0	20.0	20.0	20.0
Liability Benchmark	**927.3**	**1,160.4**	**1,196.7**	**1,198.8**	**1,175.7**

25.0 Following on from the medium-term forecasts in Table 3, the long-term liability benchmark assumes Minimum Revenue Provision (MRP) on new capital expenditure based on a 5–50-year asset life and income, expenditure and reserves remaining static. A higher asset life will be used where a professional opinion has been obtained. The chart below shows the profile of the Capital Financing Requirement (CFR) reducing by the MRP together with the maturity profile of the Council's existing borrowing.

26.0 The Loan CFR (Blue lines) represents the need to fund capital expenditure through borrowing. The Liability benchmark (Green Line) represents the level of borrowing requirement once reserves and working capital has been considered. Where the liability benchmark exceeds the Council's current borrowing levels (Grey area), this indicates the real need to borrow.

Borrowing Strategy

27.0 As of 31 December 2024, the Council held £x.xm of loans, an decrease of £x.xm compared to balances held at the start of the financial year (£814.3m). The balance sheet forecast in Table 1 shows that the Council expects to borrow up to £554.1m by 2028/29, however, this is largely dependent on how the capital programme progresses. The Council may also borrow additional sums to pre-fund future years' requirements as well as replenish the internal borrowing position, providing this does not exceed the authorised limit for borrowing of £1.8 billion.

28.0 **Objectives:** The Council's main 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.

29.0 **Strategy:** Given the significant cuts to public expenditure and 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. Interest rates have increased across the yield curve over the past year. The Council will continue to work closely with our Treasury advisors Arlingclose to ensure borrowing occurs at optimal points avoiding the worst of the market volatility. Short-term interest rates are currently at a 15-year high but are expected to fall in the coming years and it is therefore likely to be more cost effective over the medium-term to either use internal resources, or to borrow short-term loans instead. The Council's Borrowing Strategy is to maintain its debt portfolio Pool Rate within this range of 4% to 4.5%. As at 31 Deecember 2024 the average Debt Pool Rate (excluding PFI) was x.x%.

30.0 To ensure long term stability of the debt portfolio, a proportion of the portfolio will be funded by long term borrowing using a little and often approach. Where it is affordable, this can help provide certainty to ensure the ongoing viability for capital programme schemes in these volatile markets.

31.0 **Sources of borrowing:** The approved sources of long-term and short-term borrowing are:

- HM Treasury's PWLB lending facility (formerly the Public Works Loan Board)
- UK Infrastructure Bank Ltd
- Any institution approved for investments (see below)
- Any other bank or building society authorised to operate in the UK
- Any other UK public sector body including the Greater London Authority
- UK public and private sector pension funds (except the local Brent Pension Fund)
- Capital market bond investors
- Retail investors via a regulated peer-to-peer platform
- UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues

32.0 **Other sources of debt finance:** In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:

- Leasing
- Hire purchase
- Private Finance Initiative
- Sale and leaseback
- Similar asset-based finance

33.0 **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 if 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 by the Corporate Director for Finance and Resources in consultation with the Lead Member for Finance.

34.0 The Council has previously raised the majority of its long-term borrowing from the PWLB but will consider long-terms loans from other sources including banks, pensions and local authorities, and will review the appropriateness 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 not available to local authorities planning to buy investment assets primarily for yield. The Council has not undertaken such borrowing and has no plans to in future, which ensures continuing access to PWLB borrowing facilities.

35.0 In addition to the above, the Council may borrow short-term loans to cover temporary cash flow pressures from other Local Authorities or public sector bodies and banks.

36.0 The Council may arrange forward starting loans, 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.

37.0 **LOBOs:** As at 19 November 2024 the Council held £59.5m 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. It is expected that £35.0m of LOBO loans (5 loans) will undergo a rate review in 2025/26 resulting in a potential change in the loan rate. Due to higher market rates, there is now an elevated risk that existing LOBO's may require refinancing at higher rates or will require repaying upon future break dates. The Council will assess the financial implications of the best approach and either repay the LOBO loan using existing cash resources (where applicable) or raise new loans.

38.0 **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 interest rate exposure limits in the treasury management indicators below. Financial derivatives may be used to manage this interest rate risk (see section 71 below).

39.0 **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. Current high interest rate environment gives rise to favourable rescheduling opportunities. Such opportunities will be kept under review by Officers. Any decision to undertake debt rescheduling be the subject of a separate report by the Corporate Director for Finance and Resources in consultation with the Lead Member for Finance.

Treasury Investment Strategy

40.0 The Council holds invested funds, representing income received in advance of expenditure plus balances and reserves held. When cash balances are high the Council will defer the decision to borrow for the capital programme until such time cash balances deplete. Cash balances are forecasted to reduce over time as the Council is a net borrower.

41.0 **Objectives:** The CIPFA Code requires the Council to invest its treasury funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest 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. 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. The ESG Policy is discussed below.

42.0 **Strategy:** As demonstrated by the liability benchmark above, the Council expects to be a long-term borrower and new treasury investments will therefore be made primarily to manage day-to-day cash flows using short-term low risk instruments such as Local Authority deposits or Money-Market Funds. Cash invested beyond the liquidity duration will be in accordance with the investment instruments set out in Table 5. However, it is anticipated that the Council will not have significant cash balances to invest into long durations. The Council will maintain a minimum investment balance of £10m to ensure the Council complies with the requirements to be a professional client under MIFID II regulations.

43.0 **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 for greater than a year, 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.

44.0 Currently, the majority of the Council's surplus cash remains invested in short-term money market funds. The average rate of interest received on short-term investments during the year to 19 November 2024 was 5.2% with an average duration of 1 day and an average weighted risk rating of A+. Due to the Council's borrowing requirement, there is unlikely to be scope to improve the short-term investment returns achieved as liquidity of the surplus funds will play a key role.

45.0 **Business models:** 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.

46.0 **Approved counterparties:** The Council may invest its surplus funds with any of the counterparty types in table 5, subject to the limits shown.

Table 5: Investment Limits

	Credit Quality	Cash limit	Time Limit
Any single organisation, except a Government entity	A- Or equivalent	£20m	n/a
UK Government	Any	Unlimited	50 years
Local Authorities & other government entities	Any	Unlimited	25 years
Banks (unsecured)*	A- Or equivalent	£20m	13 months
Building Societies (unsecured)*	A- Or equivalent	£20m	13 months
Registered providers and registered social landlords*	A- Or equivalent	£20m	5 years
Secured investments*	A- Or equivalent	£20m	5 years
Money market funds*	A- Or equivalent	Lower of 5% of total net assets of the fund or £20m	n/a

Strategic pooled funds*	A- Or equivalent	£20m	n/a
Real estate investment trusts*	A- Or equivalent	£20m	n/a
Other Investments*	A- Or equivalent	£50m	5 years

47.0 **Minimum Credit Rating:** Treasury investments in the sectors marked with an asterisk will only be made with entities whose long-term credit rating is no lower than A-. The Council uses the lowest rating quoted by the main rating agencies, as recommended by CIPFA. 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. Within these criteria the Corporate Director for Finance and Resources will have discretion to accept or reject individual institutions as counterparties based on any information which may become available.

48.0 **Government:** Loans to, and bonds and bills issued or guaranteed by, national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is generally a lower risk of insolvency, although they are not zero risk. 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.

49.0 **Banks and building societies (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. There is no upper limit to the maximum credit loss that the Council could suffer in the event of a bail-in scenario. See section 61 below for arrangements relating to operational bank accounts. Investments in unsecured deposits will be limited to £20m.

50.0 **Registered providers (unsecured):** Loans to, and bonds issued or guaranteed by, registered providers of social housing or registered social landlords, formerly known as housing associations. These bodies are regulated by the Regulator of Social Housing (in England), the Scottish Housing Regulator, the Welsh Government and the Department for Communities (in Northern Ireland). As providers of public services, they retain the likelihood of receiving government support if needed. Investments with registered providers will be limited to £20m in 2025/26.

51.0 **Secured investments:** 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. The Council and its advisors remain alert for signs of credit or market distress that might adversely affect the Council. Investments in secured deposits will be limited to £20m.

52.0 **Money market funds (MMFs):** 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. 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. Deposits will not exceed 0.5% of the net asset value of the MMF. In addition, each Fund will be limited to a maximum deposit of £20m.

53.0 The investment strategy will provide flexibility to invest cash for longer periods in order to access higher investment returns. The upper limit for lending beyond a year is £50m. In practice, lending for more than one year will be only to institutions of the highest credit quality and at rates which justify the liquidity risk involved. Marketable instruments may have longer maturities, though the maturity will be considered in conjunction with the likely liquidity of the market and credit quality of the institution. Other than UK Central Government the Council may invest its surplus funds subject to a maximum duration of 25 years.

Alternative investment options will include:

54.0 **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. Although considered as pooled funds, MMF's are discussed separately in section 56. The Council currently has no investments in Pooled Funds (other than MMFs) at present but may make prudent use of them in the future. Investments in pooled funds will be limited to £20m in 2025/26. A Statutory Override is in place until 31 March 2025 to mitigate the accounting valuation risk impacting on the Comprehensive Income & Expenditure Account. Once the Override expires any fair value gains/losses will need to be recognised in the Comprehensive Income & Expenditure Account thus impacting on the Councils reserve balances.

55.0 **Real estate investment trusts (REITs):** 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. The risk with any investments in REITs is that shares cannot be withdrawn but can be sold on the stock market to another investor which leaves the Council open to market risk. Investments in REITs will be limited to £20m in 2025/26.

56.0 **Other investments:** This category covers treasury investments not listed above, for example unsecured corporate bonds and company loans. Non-bank companies cannot be bailed-in but can become insolvent placing the Council's investment at risk.

57.0 **Operational bank accounts:** The Council may incur operational exposures, for example though current accounts, collection accounts and merchant acquiring services, to any UK bank with credit ratings no lower than BBB- and with assets greater than £25 billion. These are not classed as investments but are still subject to the risk of a bank bail-in. The Bank of England has stated that in the event of failure, banks with assets greater than £25 billion are more likely to be bailed-in than made insolvent, increasing the chance of the Council maintaining operational continuity. The Council banks with National Westminster Bank (NatWest) who meet the Council's minimum credit criteria. Should Natwest's creditworthiness deteriorate below the Council's minimum credit criteria, then as far as is consistent with operational efficiency, no money will be placed with NatWest and credit balances in the various Council accounts will be kept to a minimum level.

58.0 **Unrated Counterparties**: For entities without published credit ratings, investments may be made either (a) where external advice indicates the entity to be of similar credit quality; or (b) to a maximum of £200,000 per counterparty as part of a diversified pool e.g., via a peer-to-peer platform.

59.0 **Risk Assessment:** Credit ratings are obtained and monitored by the Council's treasury advisers, who will notify changes in ratings as they occur. Any institution will be suspended or removed should any factors give rise to concern, and caution will be paramount in reaching any investment decision regardless of the counterparty or the circumstances. Should an entity's credit rating be downgraded so that it does not meet the Council's approved criteria then:

- No new investments will be made.
- Full consideration will be made to the recall or sale of existing investments with the affected counterparty.

60.0 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.

61.0 **Other information on the security of investments:** 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, reports in the quality financial press and analysis and advice from the Council's treasury management adviser. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may otherwise meet the above criteria.

62.0 Having an appropriate lending list of counterparties, remains critically important to protecting Brent's cash investments. A list of extremely secure counterparties would be very small, and the limits with each would be correspondingly high. This would expose the Council to a risk of an unlikely but potentially large loss. This arises because the arrangements for dealing with banks in difficulty now require a loss to be imposed on various categories of liabilities of the banks to allow the bank to recapitalise itself and continue in business (sometimes referred to as bail in).

63.0 When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2022; 2008 and 2020, 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. This will cause a reduction in the level of investment income earned but will protect the principal sum invested.

64.0 **Reputational Risk:** The Council is aware that investment with certain counterparties, while considered secure from a purely financial perspective, may leave it open to criticism, valid or otherwise, that may affect its public reputation, and this risk will therefore be considered when making investment decisions.

65.0 **Investment limits:** The Council's revenue reserves available to cover investment losses are forecast to be £513.3m on 31st March 2025. In order that no more than 10% of 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 and Council subsidiaries) will be £20 million. A group of banks under the same ownership will be treated as a single organisation for limit purposes.

Liquidity management: The Council uses internal purpose-built cash flow modelling tools 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. The Council aims to spread its liquid cash over at least two providers (e.g., bank accounts and money market funds) to ensure that access to cash is maintained in the event of operational difficulties at any one provider.

TREASURY MANAGEMENT PRUDENTIAL INDICATORS

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

67.0 **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.

Table 6: Credit risk indicator

Credit risk indicator	**Target**
Portfolio average credit rating	A

68.0 **Liquidity:** The Council 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.

Table 7: Liquidity risk indicator

Liquidity risk indicator	**Target**
Total cash available within 3 months	£20m

69.0 **Interest rate exposures:** This indicator is set to control the Council's exposure to interest rate risk. The upper limits on the one-year revenue impact of a 1% rise or fall in interest rates will be:

Table 8: Interest rate risk indicator

Interest rate risk indicator	Limit
Upper limit on one-year revenue impact of a 1% rise in interest rates	£5m
Upper limit on one-year revenue impact of a 1% fall in interest rates	£5m

The impact of a change in interest rates is calculated on the assumption that maturing loans and investments will be replaced at current rates.

70.0 **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 borrowing will be:

Table 9: Refinancing rate risk indicator

Refinancing rate risk indicator	Upper limit	Lower limit
Under 12 months	40%	0%
12 months and within 24 months	40%	0%
24 months and within 5 years	40%	0%
5 years and within 10 years	60%	0%
10 years and within 20 years	75%	0%
20 years and within 30 years	75%	0%
30 years and within 40 years	75%	0%
Over 40 years	75%	0%

Time periods start on the first day of each financial year. LOBOs are classified as maturing on the next call date i.e., the earliest date that the lender can require repayment.

71.0 **Principal sums invested for periods longer than a year:** 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:

Table 10: Price risk indicator

Price risk indicator	2024/25	2025/26	2026/27	2027/28	2028/29
Limit on principal invested beyond year end	£50m	£50m	£50m	£50m	£50m

Related Matters

72.0 The CIPFA Code requires the Council to include the following in its treasury management strategy.

73.0 **Financial Derivatives:** A Derivative is a contract between two or more parties to hedge against the risk associated with the performance of an underlying asset.

74.0 Local authorities have previously made use of financial derivatives embedded into its loans and investments both to reduce interest rate risk and to reduce costs or increase income at the expense of greater risk. Brent Council has not previously used such instruments.

75.0 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).

76.0 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 considered 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.

77.0 Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria. The current value of any amount due from a derivative counterparty will count against the counterparty credit limit and the relevant foreign country limit.

78.0 In line with the CIPFA Code, the Council will seek external advice and consult with Members before entering into financial derivatives to ensure that it fully understands the implications however there are no current plans to enter this type of arrangement. This will include analysis of the impact on interest rate, refinancing, counterparty, market, regulatory and legal risks, together with an assessment on the effectiveness of the derivative.

79.0 **Housing Revenue Account:** 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 month and interest transferred between the General Fund and HRA at the Council's average interest rate on investments, adjusted for credit risk.

80.0 The Council is eligible for the PWLB HRA rate, which is 0.4% below the Standard Rate, and is available up to June 2025. This discounted rate can be used to support local authorities borrowing for the Housing Revenue Account's capital programme and for refinancing existing HRA loans. The Council may choose to raise PWLB loans for the HRA in 2025/26 under the HRA concessionary rate subject to HRA affordability.

81.0 **Markets in Financial Instruments Directive:** The MiFID II regulations took effect from January 2018 which saw the council reclassified as a retail client with the opportunity to opt up to professional client status. Retail clients have access increased protection however this would be balanced against potentially higher fees and access to a more limited range of products. The Council has opted up to professional client status with its providers of financial services, including advisors, banks, brokers and fund managers. Given the size and range of the Council's treasury management activities, the Corporate Director for Finance and Resources believes this to be the appropriate status for the Council's treasury management activities.

82.0 **Financial Implications:** The draft capital financing budget of £35.2m for 2025/26 has been determined to enable the Council to service its debt in a timely manner; to ensure it complies with the Statutory MRP Guidance and to allow the Council to continue with the delivery of its proposed capital programme in a prudent and affordable manner.

83.0 **Other Options Considered:** The CIPFA Code does not prescribe any particular treasury management strategy for local authorities to adopt. The Council 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.

Table 11: Alternative Strategies

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 Economic & Interest Rate Forecast – 19th November 2024

Interest Rate Updates

- The Monetary Policy Committee (MPC) cutbank Rate to 4.75% in November 2024.

- The outlook for monetary policy has changed following the new government's fiscal plans, as delivered in the recent Budget. The Budget measures will boost demand in a constrained supply environment, while pushing up direct costs for employers.

- UK GDP recovered well in H12024 from technical recession, but underlying growth appears relatively subdued. The Budget will significantly boost government spending over the short-term, with few off setting measures to subdue household demand, so GDP growth is likely to rise relatively steeply.

- Private sector wage growth and services inflation remain elevated. The increase in employers' NICs, minimum and public sector wage levels could have wide ranging impact on private sector employment demand and costs, but the near-term impact will likely be inflationary as these additional costs get passed to consumers.

- CPI inflation rates will rise a little by year-end due to higher energy prices and less favourable base effects. The Bank of England (BoE) estimates the Budget impact will see t he CPI rate at 2.7% by year end 2025 and remain over target in 2026, as opposed to the prior projection of inflation easing back to and then below target.

- The MPC re-emphasised that monetary policy will be eased gradually, and we now believe the Budget measures have both reduced the pace of Bank Rate cuts and raised the low point for this loosening cycle (although downside risks develop ater).

- The Office for Budget Responsibility's (OBR) projections for increased borrowing, higher inflation and a shallower path for Bank Rate raised gilt yields. The material change in expectations means that yields will be generally higher in the post-Budget world.

- US government bond yields have risen following Donald Trump's and the Republican party victories in the US elections. Trump ran on a platform of policies that appear inflationary, calling in to question the extent of policy loosening required from the Federal Reserve (which was already uncertain given continued solid US growth data). Higher US yields could also support higher UK yields.

    - Bank Rate was cut to 4.75% in November 2024. The MPC will continue to reduce Bank Rate, but more slowly and by less. We see another rate c ut in February 2025, followed by a cut alongside every Monetary Policy Report publication, to a low of 3.75%.

- Long-term gilt yields have risen to reflect both UK and US economic, monetary and fiscal policy expectations, and increases in bond supply. Volatility will remain elevated as the market digests incoming data for clues around the impact of policy changes.

- The risks around the forecasts lie to the upside over the next 12 months but are broadly balanced in the medium term.

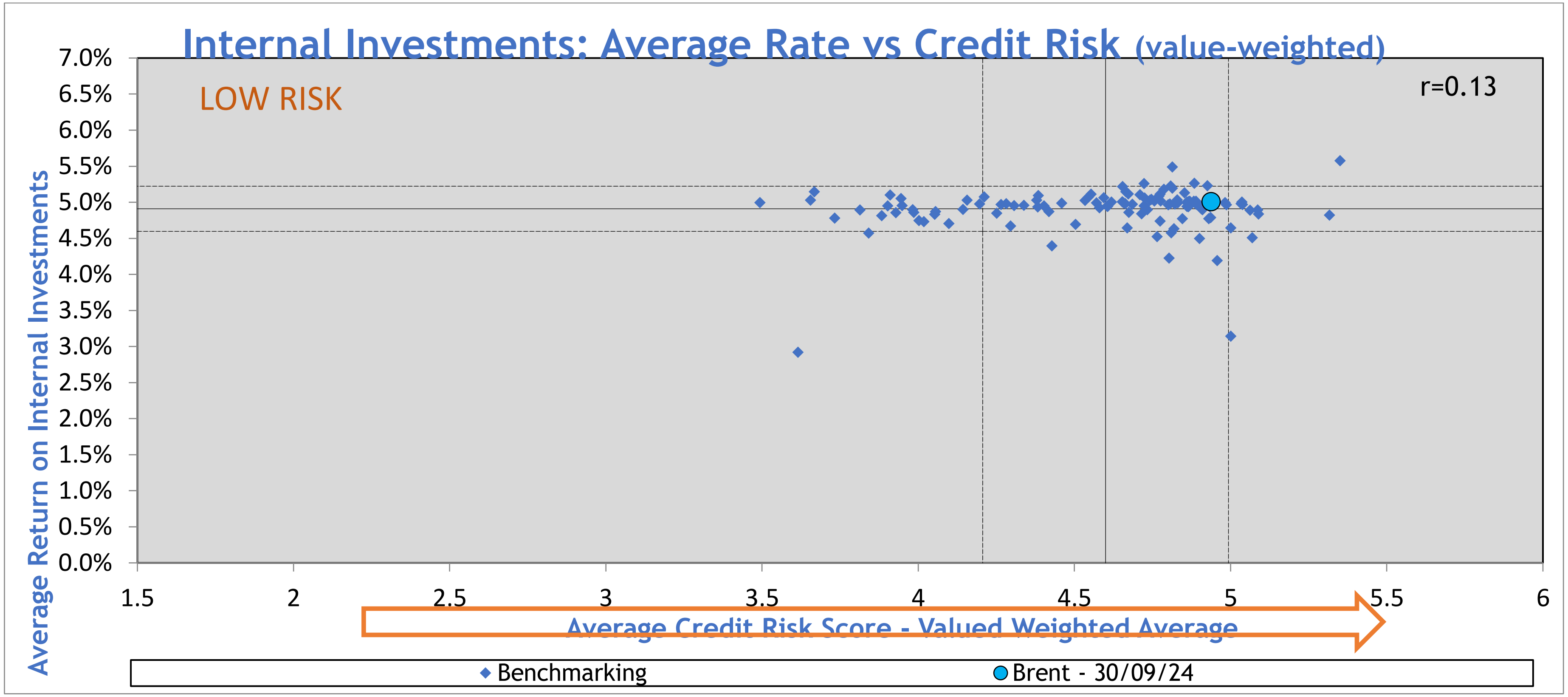
	Current	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27	Jun-27	Sep-27
Official Bank Rate													
Upside risk	0.00	0.00	0.25	0.50	0.50	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75
Central Case	4.75	4.75	4.50	4.25	4.00	3.75	3.75	3.75	3.75	3.75	3.75	3.75	3.75
Downside risk	0.00	0.00	-0.25	-0.25	-0.50	-0.50	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75
3-month money market rate													
Upside risk	0.00	0.00	0.25	0.50	0.50	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75
Central Case	4.95	4.80	4.60	4.35	4.10	3.90	3.85	3.85	3.85	3.85	3.85	3.85	3.85
Downside risk	0.00	0.00	-0.25	-0.25	-0.50	-0.50	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75
5yr gilt yield													
Upside risk	0.00	0.60	0.70	0.80	0.90	0.90	0.90	0.90	0.90	0.90	0.90	0.90	0.90
Central Case	4.30	4.20	4.10	4.05	3.95	3.90	3.90	3.90	3.95	4.00	4.05	4.05	4.05
Downside risk	0.00	-0.40	-0.50	-0.60	-0.65	-0.65	-0.70	-0.70	-0.75	-0.75	-0.80	-0.80	-0.80
10yr gilt yield													
Upside risk	0.00	0.60	0.70	0.80	0.90	0.90	0.90	0.90	0.90	0.90	0.90	0.90	0.90
Central Case	4.41	4.40	4.30	4.30	4.25	4.20	4.20	4.20	4.20	4.25	4.25	4.25	4.25
Downside risk	0.00	-0.40	-0.50	-0.60	-0.65	-0.65	-0.70	-0.70	-0.75	-0.75	-0.80	-0.80	-0.80
20yr gilt yield													
Upside risk	0.00	0.60	0.70	0.80	0.90	0.90	0.90	0.90	0.90	0.90	0.90	0.90	0.90
Central Case	4.84	4.80	4.75	4.70	4.65	4.65	4.65	4.65	4.65	4.65	4.65	4.65	4.65
Downside risk	0.00	-0.40	-0.50	-0.60	-0.65	-0.65	-0.70	-0.70	-0.75	-0.75	-0.80	-0.80	-0.80
50yr gilt yield													
Upside risk	0.00	0.60	0.70	0.80	0.90	0.90	0.90	0.90	0.90	0.90	0.90	0.90	0.90
Central Case	4.35	4.50	4.45	4.40	4.35	4.35	4.35	4.35	4.35	4.35	4.35	4.35	4.35
Downside risk	0.00	-0.40	-0.50	-0.60	-0.65	-0.65	-0.70	-0.70	-0.75	-0.75	-0.80	-0.80	-0.80

PWLB Standard Rate (Maturity Loans) = Gilt yield + 1.00%
PWLB Certainty Rate (Maturity Loans) = Gilt yield + 0.80%
PWLB HRA Rate (Maturity Loans) = Gilt yield + 0.40%
UKIB Rate (Maturity Loans) = Gilt yield + 0.40%

Appendix 2 – Existing Investment & Debt Portfolio Position

	31/12/2024 Actual Portfolio £m	31/12/2024 Average Rate %
Long-term borrowing		
Public Works Loan Board		
LOBO's		
Other loans		
Short-term borrowing		
Local Authorities		
Total External Borrowing		
Other long-term liabilities:		
Private Finance Initiative		
Finance Leases		
Total other long-term liabilities		
Total gross external debt		
Treasury investments:		
Money Market Funds		
Total treasury investments		
Net debt		

Appendix 3 – Internal Investments: Average Rate vs Credit Risk (September 2024)



A credit rating of 4 is equivalent to credit score of AA-. The Council has a target rating of A which is a rating of 6. The current portfolio has a credit rating of A+ (Credit score 5) which exceeds our target rating.