MID-YEAR TREASURY MANAGEMENT STRATEGY REVIEW 2024/25

1 Original Strategy for 2024/25

1.1 The Treasury Management Strategy for 2024/25 was approved by Executive Board on 7th March 2024.

The broad strategy continued the approach of looking to minimise borrowing costs, in the context of the Council's long-term debt being considerably lower than its accumulated Capital Financing Requirement (CFR), with the difference being covered by the use of any available balances.

When the strategy was written, it was expected that both short and long-term interest rates would fall throughout the financial year. However, given that rates were still expected to remain high overall despite the anticipated downward trend, it was likely to be more cost effective to maximise the use of internal resources in order to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk.

1.2 The original 2024/25 Investment Limits were set by reference to amount, duration and credit rating – and distinguished between Unsecured Deposits, which would be subject to greater risk of credit loss, and Secured Deposits, in which there was less risk. The limits set were largely comparable to those applying in previous years.

2 Economic Review 2024/25

The current economic background, particularly covering the latest quarter from July 2024 to September 2024, is summarised below. Key issues are as follows:

2.1 The Bank of England (BoE) Bank Rate decreased from 5.25% at the start of the financial year to 5.00% by the end of the September 2024.

2.2 The UK 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.

2.3 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.

2.4 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%.

3 Treasury Performance to date

3.1 Thus far, investment balances have ranged between £83M and £137M (with an average balance of £115m), continuing to be higher than in previous years as a result of grants received in advance from central government, including in respect of the Darwen Town Deal and Levelling-Up schemes and limited progress with the delivery of schemes within the capital programme. There has been no short-term borrowing during the period and no further long-term borrowing has been taken..

Analysis of Debt Outstanding	31st March 2024 £m		30th September 2024 £m	
Short-Term Debt		-		-
Longer-Term Debt:				
Public Works Loan Board (PWLB)	116.6		110.0	
Market Loans	13.0		10.0	
		129.6		120.0
Lancashire County Council (LCC) Debt		12.0		11.7
Debt re PFI Arrangements		55.2		53.8
Gross Borrowings		**196.8**		**185.5**
This was offset by investments of:		79.5		111.7
Net Borrowing (gross borrowing less investments)		**117.3**		**73.8**
Net Borrowing (if LCC and PFI debt are excluded)		**50.1**		**8.3**

3.2 Investments have continued to be made with a limited range of banks and Money Market Funds, along with other local authorities and the Government's Debt Management Office (DMO). Interest rates have fallen slightly over the first half of this year (driven largely by the Bank Rate changes referred to above), however, the average interest earned on investment balances has remained high at around 5.39%. It is likely that investment returns will remain at relatively high levels during the second half of the year (despite the fact that additional cuts to Bank Rate are forecast).

3.3 Decreased net interest costs have been reported through corporate monitoring, reflecting the higher interest rates achieved on investments and lower levels of short-term borrowings taken this year.

4 Investment and Borrowing Strategy for the rest of the year

Investment

4.1 Both the CIPFA Code and government guidance require that funds be invested prudently, and with regard to security and liquidity, before seeking the optimum rate of return or yield. The Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

4.2 The Council's Investment Criteria allow investment in a range of other organisations and structures, but as there are limited opportunities for straightforward trading in Secured Deposits, and as priority is given to maintaining liquidity, short-dated and simpler options are mainly used. Investments are made in: fixed term deposits and instant access accounts with banks and building societies; instant access Money Market Funds; and fixed term deposits with local authorities and the UK Government's Debt Management Office. It is expected that these will continue to be the main investment options taken up across the remainder of the year.

4.3 It is proposed that there be no changes to the existing Investment Criteria and Investment Counterparty Limits.

Borrowing

4.4 The Council's key objective when borrowing has been to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required. The flexibility to renegotiate loans, should long-term plans change is a further, secondary objective.

4.5 In keeping with these objectives, no new borrowing was undertaken in the first half of the year. This strategy enabled the Authority to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk.

4.6 It is proposed that the Borrowing Strategy remain unchanged, with the Council looking to take new borrowing as determined by cash flow requirements and by reference to movements in actual and projected long-term interest rates.

5 Risk Management

5.1 The Council's main objective for the management of its investments is to give priority to the security and liquidity of its funds before seeking the best rate of return. Therefore, most surplus cash is held in short-term investments with government bodies, and with highly rated banks and pooled funds. In addition, the Council can hold investments that entail a slightly higher level of risk, but such risks are mitigated by limiting the amount and duration of exposure.

5.2 The Council's main objective for the management of its debt is to ensure its long-term affordability. The largest portion of its loans are from the PWLB at long-term fixed rates of interest.

5.3 Another significant element of the Council's long-term debt is £10M of loans from banks and other institutions. £5M of this relates to a "lender's option, borrower's option" (LOBO) loan, under which the Lender can, at pre-determined times, exercise an Option to increase the rate payable on the debt, and the Borrower has the Option to either accept the proposed increase or repay the whole loan. These loans tend to have interest rates fixed at levels that were relatively low when they began, but if the Lender Option is exercised, the Borrower would have to deal with whatever interest rates are at the call date.

At the beginning of the year the Council had £8M in LOBO loans. However, in August 2024, FMS Wertmanagement exercised the option to increase the interest rate on a £3m LOBO from 4.75% to 7.82%. Following a review of the financial implications, and supported by advice from our treasury management advisors, Arlingclose, the Council subsequently exercised the option to repay the loan on the 6th August 2024.

The remaining loan exposes the Council to some risk of rising long-term interest rates, but that is mitigated by the fact that the debt can only be "called" once in every five years, with the next call date not falling until August 2029.

5.4 A combination of short duration investments and long duration debt exposes the Council to the risk of falling investment income during periods of low interest rates. This is not a concern in the current financial year because interest rates remain high, however, even if interest rates were to fall, the risk of low investment returns is viewed as lower priority compared to the benefits of optimising the security and liquidity of investments, and the savings made on borrowing costs.

6 Indicators

6.1 The previously approved Indicators were set at cautious levels and can remain unchanged.

6.2 The Council has complied with the Limits and Indicators it has set, and expects to do so over the remainder of the year.

7 Codes of Practice and MRP – Consultation and Proposed Changes

7.1 CIPFA published its revised Prudential Code for Capital Finance and Treasury Management Code on 20th December 2021. The key changes in the two codes were around permitted reasons to borrow, knowledge and skills, and the management of non-treasury investments.

7.2 To comply with the Prudential Code, authorities must not borrow to invest primarily for financial return. This Code also states that it is not prudent for local authorities to make investment or spending decision that will increase the Capital Financing Requirement (CFR) unless directly and primarily related to the functions of the authority.

7.3 Borrowing is permitted for cash flow management, interest rate risk management, to refinance current borrowing and to adjust levels of internal borrowing. Borrowing to refinance capital expenditure primarily related to the delivery of a local authority's function but where a financial return is also expected is allowed, provided that financial return is not the primary reason for the expenditure. These changes aligned the CIPFA Prudential Code with the PWLB lending rules.

7.4 The Authority has not invested in assets primarily for financial return or that are not primarily related to the functions of the Authority, and has no plans to do so in future.