

REPORT TO: **AUDIT AND GOVERNANCE COMMITTEE**

MEETING DATE: 17 December 2024

BY: Executive Director for Council Resources

SUBJECT: Treasury Management – Mid Year Review 2024-25

1 PURPOSE

- 1.1 An update to the Committee on Treasury Management activity during the first six months of 2024-25.

2 RECOMMENDATIONS

- 2.1 The Committee is asked to note the content of the report.

3 BACKGROUND

- 3.1 A main function of treasury management operations is to ensure that the cash flow is adequately planned, with cash being available when it is required. Surplus monies are invested in low-risk counterparties, providing adequate liquidity initially before considering optimising investment return.
- 3.2 In addition, the treasury management service manages the accounting and funding of the Council's capital plans. The approved capital plans provide a guide to the borrowing need of the Council, including setting out the longer-term cash flow planning to ensure the Council can meet its capital spending obligations in future years. This management of longer-term cash may involve arranging long or short-term loans or using longer-term cash flow surpluses. On occasion, any debt previously incurred may be restructured to meet wider risk or cost objectives.
- 3.3 Treasury management is therefore defined as being the management of the local authority's borrowing, investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum

performance consistent with those risks. This mid-year report is reviewed against the current Treasury Management Strategy that was approved by Council on 20 February 2024.

- 3.4 This mid-year report has been prepared in compliance with CIPFA's Code of Practice on Treasury Management, and covers the following:
- A. An economic update for the first part of the 2024-25 financial year;
 - B. A review of the Treasury Management Strategy Statement and Annual Investment Strategy;
 - C. The Council's capital position (prudential indicators);
 - D. A review of the Council's investment portfolio for 2024-25.
 - E. A review of the Council's borrowing strategy for 2024-25.
 - F. A review of any debt rescheduling undertaken during 2024-25.

Part A – Economic Update

- 3.5 The Monetary Policy Committee (MPC) decreased interest rates by 0.25%, taking Bank rate from 5.25% in March to 5.00% in August as inflation fell closer to the Bank of England's target.
- 3.6 Interest rates are thought to continue to decrease but a slower rate than predicted previously, with the rate expected to hold at 4.75% until the end of 2024, in line with the Bank of England strategy to for managing inflation, which they predict will rise to at least 2.5% by the end of 2024 and will continue to fluctuate until at least 2026.
- 3.7 The MPC's thoughts and the economic conditions have informed our Treasury advisors forecast for the period December 2024 to December 2027 as shown in Table 3.1. It shows Bank Rate at 4.75% with an expectation that it will continue to decrease by 0.25% quarterly with a pause at the end of 2025, remaining almost constant at 3.75% for 2026, a drop of 0.25% then holding steady at 3.50% for 2027.

Table 3.1

Link Group Interest Rate View	11.11.24												
	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27	Jun-27	Sep-27	Dec-27
BANK RATE	4.75	4.50	4.25	4.00	4.00	3.75	3.75	3.75	3.50	3.50	3.50	3.50	3.50
3 month ave earnings	4.70	4.50	4.30	4.00	4.00	4.00	3.80	3.80	3.80	3.50	3.50	3.50	3.50
6 month ave earnings	4.70	4.40	4.20	3.90	3.90	3.90	3.80	3.80	3.80	3.50	3.50	3.50	3.50
12 month ave earnings	4.70	4.40	4.20	3.90	3.90	3.90	3.80	3.80	3.80	3.50	3.50	3.50	3.50
5 yr PWLB	5.00	4.90	4.80	4.60	4.50	4.50	4.40	4.30	4.20	4.10	4.00	4.00	3.90
10 yr PWLB	5.30	5.10	5.00	4.80	4.80	4.70	4.50	4.50	4.40	4.30	4.20	4.20	4.10
25 yr PWLB	5.60	5.50	5.40	5.30	5.20	5.10	5.00	4.90	4.80	4.70	4.60	4.50	4.50
50 yr PWLB	5.40	5.30	5.20	5.10	5.00	4.90	4.80	4.70	4.60	4.50	4.40	4.30	4.30

Part B – Review of Treasury Management Strategy Statement and Annual Investment Strategy

- 3.8 The Treasury Management Strategy Statement (TMSS) sets out the wider Treasury and Investment Strategy and was approved by Council on 20 February 2024. The Strategy includes several key treasury management indicators. This report provides an update on the Treasury Management activity undertaken by the Council relative to the approved strategy taking account of the updated economic position and budgetary changes already approved.
- 3.9 Table 3.2 below provides a summary of the current position relative to approved indicators, with more details around the position on each indicator set out in the remainder of this report.

Table 3.2

Prudential Indicators 2024-25	Approved £m	Current Estimated Prudential Indicator £m
Capital Financing Requirement	685	688
Operational Boundary	685	688
Authorised Limit	756	756

Includes long term liabilities for PPP arrangements and finance leases

Part C - The Council's Capital Position (Prudential Indicators)

- 3.10 The current projections set against the approved indicators are set out below.

Capital Expenditure and Financing of the Capital Programme

- 3.11 Table 3.3 below sets out the current projected outturns for the Council's capital investment programmes for 2024-25 relative to the approved budget set on 20 February 2024.

The table sets out how the programme is financed, highlighting the supported and unsupported elements and the expected financing arrangements.

The borrowing requirement increases the underlying indebtedness of the Council by way of the Capital Financing Requirement (CFR). This in part will be offset by any revenue charges for the repayment of debt.

Table 3.3

Capital Expenditure	2024-25 Approved Budget £m	2024-25 Projected Outturn * £m
General Services	117	113
HRA	32	29
Total capital expenditure	149	142
Financed by:		
Capital receipts	15	13
Capital Grants	52	51
CFCR	2	2
Total financing	69	66
Borrowing requirement	80	76

** Projected outturn is based on the position to be reported in the December Council update and remains subject to change*

Impact on Prudential Indicators

- 3.12 The Capital Financing Requirement (CFR) measures the Council's underlying need to borrow for a capital purpose. Table 3.4 below, sets out the CFR and the expected debt position over the period, which is termed the Operational Boundary.
- 3.13 Overall, the Council is currently projecting to be marginally over the approved limits for both CFR and Operational Boundary. This is due to the reprofiling of the PPP arrangements to match asset lives as per guidance issued by the Scottish Government and implemented at the end of the 2023-24 financial year.

This increased the CFR by £14 million and has therefore cancelled out any reduction which would have been seen from any reduction or reprofiling of budgeted spend and the increase in capital receipts in 2023-24 in General Services of close to £10 million on the opening position to budget.

Table 3.4

Prudential Indicators	2024-25 Approved Limits £m	2024-25 Projected Outturn £m
Capital Financing Requirement		
CFR – General Services	394	402
CFR – HRA	291	286
Total CFR	685	688
Operational Boundary for external debt		
Borrowing	656	659
Other long term liabilities*	29	29
Total debt (year-end position)	685	618

** PPP arrangements and finance leases*

The impact of capital investment decisions on the ratio of financing costs to net revenue streams and the debt per Band D equivalent and per HRA dwelling are shown in the table below.

Table 3.5

Prudential Indicators	2024-25 Approved Budget	2024-25 Projected Outturn
Ratio of financing costs to net revenue stream		
General Services	5.57%	5.24%
HRA	36.24%	35.20%
Impact of Capital Investment Decisions		
General Services – Debt per Band D equivalent	£5,940	£5,807
HRA – Debt per dwelling	£31,112	£30,312

Limits to Borrowing Activity

- 3.14 One of the main key controls over the treasury activity is to ensure that over the medium term, net borrowing (borrowing less investments) will only be for a capital purpose. Gross external borrowing should not, (except in the short term), exceed the total of CFR in the previous year plus the estimates of any additional CFR for 2024-25 and next two financial years. This allows some flexibility for limited early borrowing for future years should the need arise.
- 3.15 Table 3.5 below sets out that the Council is currently managing to operate within this limit and continue to maintain an under-borrowed position. The table below shows that at the end of this financial year the Council is currently forecasting to have external borrowings of £596 million and to utilise £92 million of cash flow funds (under-borrowing) in lieu of borrowing. This is the most prudent and cost effective approach in the current economic climate and remains consistent with the approved Treasury Management Strategy.

Table 3.5

	2023-24 Estimate £m	2023-24 Actual £m	2024-25 Original Estimate £m	2024-25 Revised Estimate £m
External borrowing	573	494	559	567
Other long term liabilities*	31	31	29	29
Total external debt	604	525	588	596
CFR* (year end position)	669	625	685	688
Under-borrowing	65	100	97	92

* Includes PPP arrangements and finance leases etc.

3.16 The Authorised Limit is a statutory requirement that represents the limit beyond which borrowing is prohibited and sets an overall control on the level of borrowing. This limit reflects the level of borrowing which while not desired, could be afforded in the short term, but is not sustainable in the longer term. The approved Authorised Limit for 2024-25 is £756 million and as highlighted in Table 3.2 above, the Council continues to operate well within approved limits, and therefore there is no change to the overall strategy required.

Part D - Investment Portfolio 2024-25

3.17 In accordance with the Code, it is the Council's priority to ensure security of capital and liquidity, and to obtain an appropriate level of return consistent with the Council's risk appetite. Wider loan interest rates remain in line with the latest Bank Rate. Bank interest rates are forecast remain at 4.75% for the remainder of the financial year and given this, investment returns will be lower than in 2023-24.

3.18 The Council's investment decisions are made in accordance with the approved strategy. Fifty-two short term investments were placed during the first 6 months of the financial year as shown in Table 3.6. Seven of the investments placed are due to mature in the next financial quarter of the year.

Ethical, Sustainable, Governance (ESG) investments are sought where interest rates are comparable with other bodies and the criteria for risk exposure are also met and 2 investments of this type were placed in the period. Any other surplus cash balances are held in the Council's bank account.

These short term investments are aligned to the overall strategic direction to take opportunities to maximise income while maintaining overall liquidity and remaining in alignment with TMP1 (Treasury Management Practices) as per the Annual Investment Strategy within the approved 2024/25 Treasury Strategy.

Table 3.6

Counterparty	Date	Principle £m	Maturity	Interest rate
DMO (UK Govt. Debt Management Office)	08/05/2024	5	10/05/2024	5.19%
DMO	08/05/2024	10	13/05/2024	5.19%
Lloyds Bank	08/05/2024	5	10/06/2024	5.28%
Standard Chartered Sustainable	08/05/2024	5	08/08/2024	5.15%
Central Bedfordshire	24/05/2024	5	22/08/2024	5.15%

DMO	11/06/2024	10	12/06/2024	5.19%
Lloyds Bank	11/06/2024	5	11/07/2024	5.28%
DMO	12/06/2024	10	21/06/2024	5.19%
Monmouthshire County Council	19/06/2024	5	19/09/2024	5.24%
Central Bedfordshire Council	24/06/2024	5	08/07/2024	5.25%
DMO	26/06/2024	10	27/06/2024	5.19%
DMO	01/07/2024	5	15/07/2024	5.20%
DMO	03/07/2024	5	05/07/2024	5.19%
DMO	09/07/2024	10	10/07/2024	5.19%
DMO	10/07/2024	10	12/07/2024	5.19%
Lloyds Bank	11/07/2024	5	12/08/2024	5.25%
DMO	12/07/2024	10	19/07/2024	5.19%
DMO	15/07/2024	4	19/07/2024	5.19%
DMO	15/07/2024	5	29/07/2024	5.19%
DMO	17/07/2024	5	18/07/2024	5.19%
DMO	18/07/2024	5	22/07/2024	5.19%
DMO	22/07/2024	5	29/07/2024	5.19%
DMO	24/07/2024	5	30/07/2024	5.19%
DMO	30/07/2024	20	31/07/2024	5.19%
DMO	31/07/2024	20	01/08/2024	5.19%
DMO	01/08/2024	10	12/08/2024	5.03%
DMO	02/08/2024	6.5	08/08/2024	4.94%
DMO	08/08/2024	8	12/08/2024	4.94%
Standard Chartered Sustainable	08/08/2024	5	08/11/2024	4.89%
DMO	12/08/2024	10	16/08/2024	4.94%
Lloyds Bank	12/08/2024	5	12/09/2024	4.94%
DMO	13/08/2024	7	20/08/2024	4.94%
DMO	16/08/2024	8	19/08/2024	4.94%
DMO	21/08/2024	10	30/08/2024	4.94%
DMO	21/08/2024	5	27/08/2024	4.94%
DMO	27/08/2024	5	29/08/2024	4.94%
DMO	28/08/2024	6	29/08/2024	4.94%
DMO	30/08/2024	10	06/09/2024	4.94%
DMO	04/09/2024	4	06/09/2024	4.94%
DMO	05/09/2024	3	13/09/2024	4.94%
DMO	06/09/2024	7	12/09/2024	4.94%
DMO	11/09/2024	3	12/09/2024	4.94%
DMO	12/09/2024	1.5	12/09/2024	4.94%
DMO	12/09/2024	8	20/09/2024	4.94%

DMO	20/09/2024	9	23/09/2024	4.94%
Lloyds Bank	20/09/2024	5	21/10/2024	4.95%
DMO	26/09/2024	9	27/09/2024	4.94%
DMO	26/09/2024	10	04/10/2024	4.94%
Wrexham Council	27/09/2024	2	11/10/2024	5.00%
LB Haringey Council	30/09/2024	5	30/10/2024	5.00%
NE Lincolnshire Council	30/09/2024	5	28/11/2024	4.90%
LB Barking & Dagenham Council	30/09/2024	5	28/11/2024	5.05%

3.19 An external investment management company, Rathbones (previously with Investec which has been incorporated into Rathbones) manages East Lothian Council Common Good funds and Charitable Trust funds in two separate portfolios. The returns on these investments continue to be closely monitored during the year. As of 30 September 2024:

- The Common Good portfolio was valued at £3.946 million, an increase of £0.096 million over the 6 month period. Although the performance of this portfolio over the first 6 months was slightly lower than the benchmark by 0.28% it was higher than benchmark by 0.11% in the first 3 months of the financial year.
- The East Lothian Charitable Trust portfolio was valued at £3.894 million, an increase of £0.087 million over the 6 month period. The performance of this portfolio over the first 6 months was below the benchmark by 0.40% although it was higher than benchmark by 0.17% in the first 3 months of the financial year.

Part E – Borrowing Strategy 2024-25

3.20 In recent years, the Council has predominately used PWLB as its main source of funding partly due to the level of risk and interest rates available. Consideration is given to both the maturity profile and interest rates to manage cost and refinancing risk. With regard to the interest rate forecast discussed in Part A, while increases in interest rates were included within the current approved capital investment and borrowing plans, that forecast was much lower than the actual increases in rates. The subsequent estimated reduction in interest rates were in an earlier timeframe than now forecast and has had an impact on interest on new borrowing undertaken and due to be taken in the current financial year.

Looking forward, the Council will need to consider further both the affordability of capital investment plans and potentially seek alternative sources and/or methods of borrowing in order to achieve the best rates and terms. Whilst it remains unclear as to the extent of any further increase in borrowing rates or the duration of any peak, the Council's treasury advisor, Link Asset Services provides regular forecasting of

PWLB rates so that an informed decision can be made on the timing of the borrowing for the capital programme.

- 3.21 Five long term external loans were taken in the first 6 months of the financial year. Due to the overall financial position and the underlying need to borrow for capital purposes (the capital financing requirement – CFR, currently £688 million) it is currently estimated that further new external borrowing of £30 million will be required during the second half of this financial year.

4 Table 3.7

Loan	Date	Principal £m	Maturity (Years)	Interest rate
PWLB – EIP (equal instalments of principal)	02/04/2024	10	11	4.19%
PWLB - Maturity	02/04/2024	5	6	4.19%
PWLB - EIP	25/09/2024	15	11	4.37%
PWLB - EIP	25/09/2024	10	11	3.97%
PWLB - Maturity	25/09/2024	15	2.5	4.83%

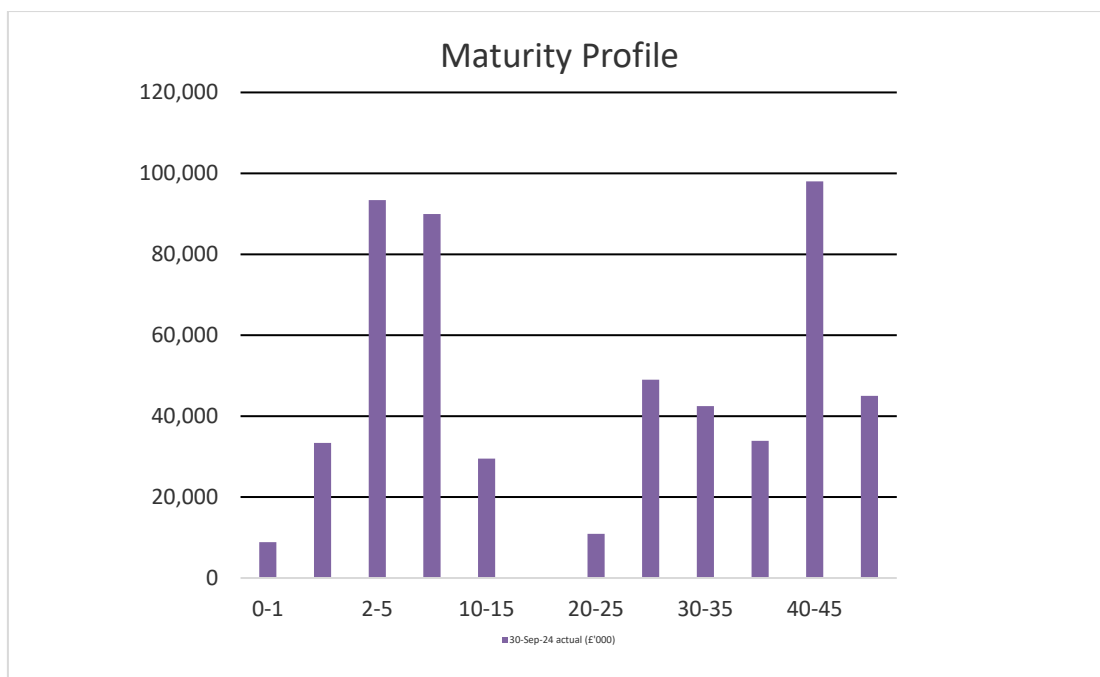
- 4.1 Three PWLB loans matured during the first six months and was repaid as set out in Table 3.8 below

Table 3.8

Loan	Date repaid	Principal £m	Maturity (Years)	Interest rate
PWLB	21/09/2024	3.5	12	3.09%
PWLB	24/09/2024	3.5	12	3.04%
PWLB	28/09/2024	0.639	29	8.25%

Current Loan Maturity Profile

- 4.2 The graph below sets out the current external borrowing maturity profile for the Council.



Part F – Debt Rescheduling

- 4.3 Debt rescheduling opportunities have increased over the course of the past six months and will be considered if giving rise to long-term savings. However, no debt repayments or rescheduling have been undertaken to date in the current financial year.

Part G - Introduction of Reporting Standard IFRS16

- 4.4 International Financial Reporting Standard 16 – Leases came into operation from 1 April 2024. The standard brings the value of assets where the Council has the right of use including lease agreements onto the Council’s balance sheet. The standard also requires that these values are reflected in both capital and debt calculations. This standard has implications on treasury prudential indicators, particularly the Capital Financing Requirement as well as the Operational Boundary and Authorised Limit.
- 4.5 Work is progressing on the implementation of the new standard and an update of the implications will be incorporated into future reporting and in future Treasury Strategies.

5 POLICY IMPLICATIONS

- 5.1 There are no direct policy implications associated with this report, however the Council’s treasury management activity is determined by the policy framework set out in the approved Treasury Management Strategy. No

changes to the current strategy are recommended on the basis of this mid-year review.

6 INTEGRATED IMPACT ASSESSMENT

- 6.1 The subject of this report has been considered and given there is no change in policy direction, there is no requirement to undertake any further impact assessment.

7 RESOURCE IMPLICATIONS

- 7.1 Financial - There are no direct financial implications associated with this report however the Council's Treasury Management and Capital activity clearly has a significant impact on the management of the Council's financial resources.
- 7.2 Personnel - none
- 7.3 Other – none

8 BACKGROUND PAPERS

- 8.1 Treasury Management Strategy 2024-25 to 2027-28 – East Lothian Council 20 February 2024

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