Report

Governance & Audit Committee

Part 1

Date:

Subject **Treasury Management Outturn Report - 2023/24**

Purpose This report is to inform Governance & Audit Committee of treasury activities undertaken within the financial year 2023/24 and confirms that all treasury and prudential indicators have been adhered to. The Committee is asked to make any comments or observations, as needed, which will be included in this report when subsequently sent to Cabinet / Council.

Author Assistant Head of Finance / Chief Accountant

Ward All

Summary In line with the agreed Treasury Management Strategy, the Council continues to be both a short-term investor of cash and borrower to manage day-to-day cash flows. Current forecasts indicate that, in the future, temporary borrowing may be required to fund normal day-to-day cash flow activities and longer-term borrowing will increase to fund commitments in the current capital programme, as well as the impact of reduced capacity for 'internal borrowing'. In addition, the Council has a large refinancing requirement for external borrowing during 2024/25.

During the year, the Council's total borrowing reduced from £138.6m to £137.7m and total investments reduced from £47.2m to £13.9m, as anticipated, meaning overall the Council net borrowing increased by £32.3m to £123.7m as at 31st March 2024.

The report confirms that all prudential indicators were complied with during 2023/24.

Proposal To note the report on treasury management activities for the period 2023/24 and provide comments to Cabinet/Council.

Action by Head of Finance / Assistant Head of Finance

Timetable Immediate

This report was prepared after consultation with:

- Treasury Advisors
- Head of Finance

Signed

Background

1. Treasury risk management within Newport City 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). The revised edition had a number of key changes which the Authority has adopted in the 2023/24 financial year. The key changes are;
    - It particularly highlights the requirement that local authorities must not borrow to invest primarily for financial return.
    - The forward-looking prudential indicators must be monitored and reported to members at least quarterly (currently half-yearly) as part of the normal budget monitoring reports.
    - The Authority will also have to explicitly document a formal and comprehensive knowledge and skills schedule to ensure the effective acquisition and retention of treasury management skills for those responsible for the management, delivery, governance, decision-making and compliance with legislative requirements.

2. CIPFA defines Treasury Management as

   The management of the organisation'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.

   The successful identification, monitoring and control of risk are therefore central to the Authority's treasury management strategy.

3. The 2023/24 Treasury Management Strategy was approved by the Council as part of the Capital Strategy in February 2023 and can be viewed at the following location.

   https://democracy.newport.gov.uk/documents/s25059/05%20Council%20Report%20-%20Capital%20Strategy%20Treasury%20Strategy%202023-24.pdf?LLL=0

4. This report presents the following information:

    - details of capital financing, borrowing, any debt rescheduling and investment transactions
    - reports on the risk implications of treasury decisions and transactions
    - details the monitoring position on treasury management transactions
    - compliance with treasury limits set and Prudential Code

BORROWING STRATEGY / ACTIVITY

Short and Long Term Borrowing

5. Whilst the Council has significant long-term borrowing requirements, the Council's current strategy of funding capital expenditure is through the concept of 'internal borrowing', where the Council seeks to use its existing cash balances to afford its capital expenditure prior to taking out external borrowing i.e. deferring taking out new long term borrowing and funding capital expenditure from the Council's own cash resources for as long as is possible, which it has because of its 'cash-backed' reserves and, to a lesser extent, day to day positive cash-flows. The Council may undertake borrowing early if there is a clear underlying need for future borrowing and it feels it can minimise the risk of future interest rate rises while providing value for money. Any such action will be in line with advice from our treasury advisors.

6. By using an internal borrowing strategy, the Council can also minimise cash holding at a time when counterparty risk remains relatively high, especially within the current economic climate. However, the capacity to internally borrow is planned to reduce over the short to medium term as the level of reserves are being utilised as intended. In addition, some existing sizeable loans are due to mature

within the next year. These two factors will mean that some new borrowing will be required simply to replace existing borrowing, before considering any overall increase in the capital financing requirement as a result of the Council's capital programme.

7. Interest rates have seen substantial rises over the last two years, although these rises have now begun to plateau. Having begun the financial year at 4.25%, the Bank of England's Monetary Policy Committee (MPC) increased Bank Rate to 5.25% in August 2023. Following this MPC meeting, Arlingclose, the authority's treasury adviser, maintained its central view that 5.25% remains the peak in Bank Rate and that interest rates will most likely start to be cut in the latter half of 2024. The risks in the short-term are deemed to be to the downside as a rate cut may come sooner than expected, but then more broadly balanced over the medium term. Bank Rate was maintained at 5.25% through to March 2024.

8. The following table compares the borrowing levels at the end 2023/24 with the equivalent from March 2023. The increase in interest free borrowing was from Salix and included 6 new loans totalling £1.9m, which were linked to specific energy efficiency projects. Even though the Authority took out some new borrowing, there was a small overall reduction in the level of borrowing in the 2023/24 financial year. This was due to the redemption of two small PWLB loans at the end of September, which have not been refinanced, plus there are a number of loans which are Equal Instalments of Principal (EIP) loans, which pays back principal over the life of the loan, so the borrowing levels decline naturally over the life of the loan as an alternative to maturity based loans where the amount borrowed is only repaid when the loan period expires.

Comparison	2023-24	2022-23
Public Works Loan Board	104,531,704	93,089,897
Interest Free Borrowing	11,263,988	9,905,757
LOBOs	15,000,000	30,000,000
Ex LOBO	5,000,000	5,000,000
Accrued Interest	1,856,838	606,212
	137,652,530	138,601,866

9. As well as traditional external borrowing via the Public Works Loans Board (PWLB), the Council has LOBO (Lender Option / Borrower Option) borrowing. One of the more unusual features of a LOBO is that the lender can volunteer a change in rate at certain intervals, and this is more probable in an environment of rising interest rates, as recently experienced. Within 2023/24 three of the six LOBOs that the Authority held gave notice that they were intending to increase the interest rate, therefore the Council decided to repay the loan at no additional cost as accepting the revised terms would mean the Authority would still have refinancing risk for those loans in later years. Therefore, the authority took out £15m of new long term borrowing in PWLB loans to repay the LOBOs loans, which has had no impact on the Council's overall borrowing.

   The other three LOBOs also have call dates within the next 12 months. Again, if the option is exercised and an increased rate proposed, a decision on how to proceed considering other financing options would be made in conjunction with our treasury advisors.

   The accrued interest is substantially higher than in previous years due to the fact that 31st March was a non-working day, as it was then followed by a bank holiday interest payments were not completed until 2nd April, in the new financial year.

INVESTMENTS ACTIVITY / POSITION

10. The Council's strategies in this area of Treasury Management are:

- to be a short term and relatively low value investor, consistent with the pursuit of an 'internal borrowing strategy' and

- investment priorities should follow the priorities of security, liquidity and yield, in that order.

11. The following table compares the investment levels at the end of March 2024 with the equivalent from the end of March 2023. This indicates a net decrease in investment activity of £33.3m since March 2023. As demonstrated by the liability benchmark in this report, the Authority expects to be a long-term borrower and new treasury investments are therefore primarily made to manage day-to-day cash flows using short-term low risk instruments.

Comparison	2023-24	2022-23
Investment	- 13,944,735	- 47,231,574
	- 13,944,735	- 47,231,574

12. The January 2018 saw the implementation in the UK of the second Markets in Financial Instruments Directive (MiFID II), where treasury consulting firms were obliged to treat all local authorities as retail clients unless they opted up to professional client status and met certain criteria. Those criteria included holding a minimum of £10m investment balance and employing knowledgeable and experienced staff to carry out investment transactions. In February 2023, the Council invested in three covered bonds to satisfy this requirement; Santander (£3.5m), Lloyds (£4m) and Cie de Financement Foncier (£2.5m). These are longer term investments, which form part of the balance in the table above and help to diversify our investment portfolio and provide a high level of investment security.

NON-TREASURY INVESTMENTS

13. The definition of investments in CIPFA's revised Treasury Management Code now covers all the financial assets of the Authority as well as other non-financial assets which the Authority holds primarily for financial return. This is replicated in the Investment Guidance issued by Ministry of Housing, Communities and Local Government's (MHCLG) and Welsh Government, in which the definition of investments is further broadened to also include all such assets held partially for financial return.

14. The Authority held such investments in:

    - directly owned property such as office and commercial units of £9.6m
    - loans to developers £10.3m
    - shareholding in subsidiaries £0.3m (Newport Transport)

15. Directly held property is subject to annual valuation review which can change the value of the holding.

16. The developer loans activity reflects those regenerative partnership projects that are included within the capital programme to assist developers with cash flow loans on particular projects and which are required to be repaid plus interest.

OTHER TREASURY CONSIDERATIONS FOR 2023-24

Economic background and Counter Party Update

17. Appendix A outlines the underlying economic environment as provided by the Council's Treasury Management Advisors, Arlingclose. This is very useful context in informing annual strategy and assisting in effective treasury decisions.

18. UK inflation continued to decline from the 8.7% rate seen at the start of 2023/24. By the last quarter of the financial year headline consumer price inflation (CPI) had fallen to 3.4% in February but was still above the Bank of England's 2% target at the end of the period.

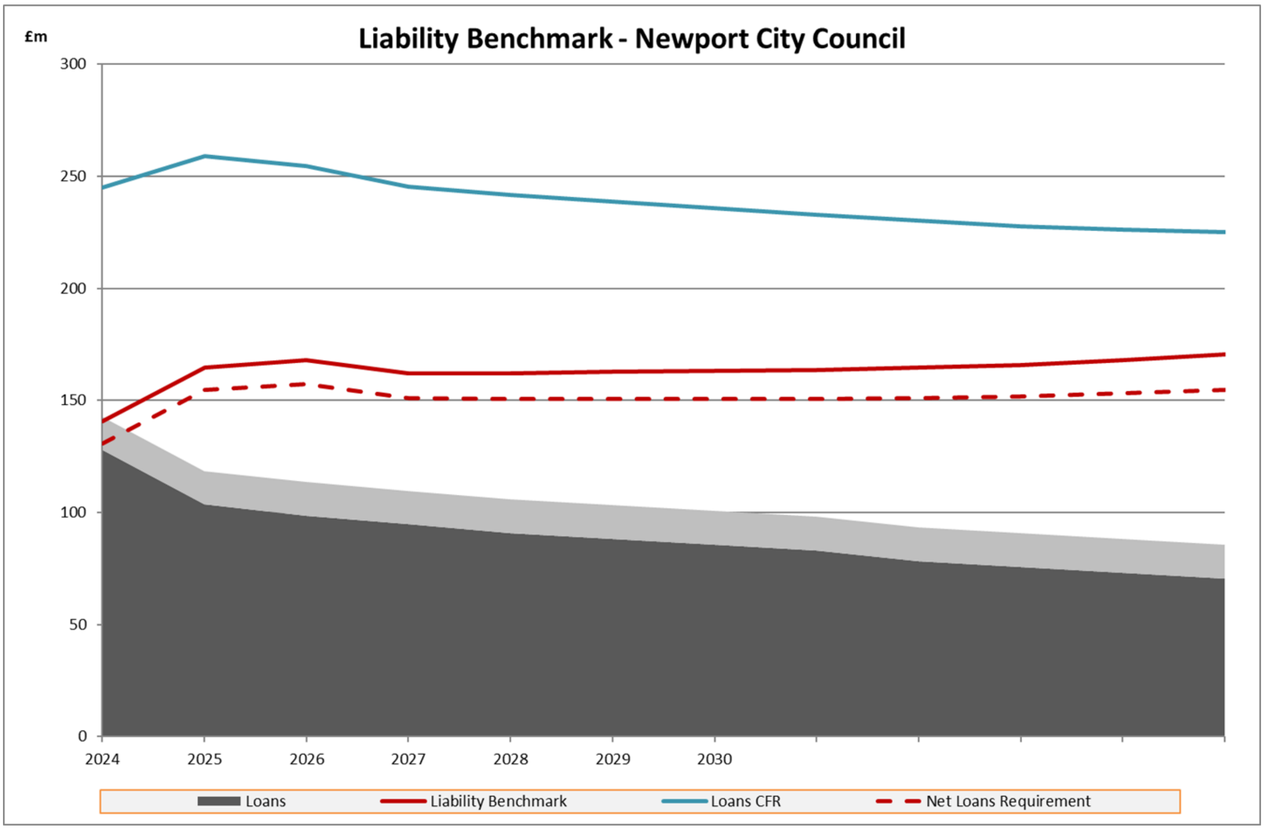
Compliance with Prudential Indicators approved by Council

19. The Authority measures and manages its exposures to treasury management risks using various indicators which can be found in Appendix B. The Authority has complied with the Prudential Indicators for 2023/24, set in February 2023 as part of the Treasury Management Strategy.

Liability Benchmark Indicator

20. CIPFA recommends that the optimum position for external borrowing should be at the level of the Liability Benchmark (i.e. all balance sheet resources should be used to maximise internal borrowing). If the outputs show future periods where external loans are less than the Liability Benchmark, then this indicates a borrowing requirement thus identifying where the authority is exposed to interest rate, liquidity and refinancing risks. Conversely, where external loans exceed the Liability Benchmark then this will highlight an over borrowed position which will result in excess cash in the organisation requiring investment thus exposing the authority to credit and reinvestment risks and a potential cost of carry. The treasury strategy should explain how the treasury risks identified by the Liability Benchmark are to be managed over the coming years.

21. The Liability Benchmark is effectively the Net Borrowing Requirement of a local authority plus a liquidity allowance. In its simplest form, it is calculated by deducting the amount of investable resources available on the balance sheet (reserves, cash flow balances) from the amount of outstanding external debt and then adding the minimum level of investments required to manage day-to-day cash flow. It is often denoted in pictorial form using the following graph:



22. In the chart above, the blue line reflects the accumulated value of historic, and future, unfunded capital expenditure – i.e. expenditure initially funded by borrowing and then funded via the revenue budget, over time, in the form of MRP (Minimum Revenue Provision). In effect, this line represents the gross amount of borrowing required.

The solid red line is the calculated actual/real level of borrowing required, taking into account the Council's internal borrowing capacity (i.e. the value of balance sheet resources at any point in time). The gap between the blue and red lines represents the internal borrowing capacity.

The grey shaded areas represent the actual borrowing undertaken by the Council as of 31st March 2024 and shows how these loans are set to reduce as they are scheduled for repayment.

The white gap between the solid red line and the grey shaded areas represents the estimated amount of new borrowing required over the next ten years. A large proportion of this new borrowing would be to replenish existing maturing borrowing, with the remainder being required as a result of the Council's capital expenditure plans.

Outlook for short to medium term

23. As outlined in the Liability Benchmark graph, and elsewhere in the report, the Council has a longer term underlying need to borrow. This is driven by the increasing expenditure on the Capital Programme, as well as the need to refinance existing borrowing. It is anticipated that the need to borrow will crystallise towards the second half of the 2024/25 financial year. In the intervening period, the Council should be able to manage its cashflow requirements through its internal borrowing strategy and gradually reducing the level of investments held. If there are any short term cashflow needs, these can be addressed via short term borrowing.

24. Aside from LOBOs, which could potentially see interest rate rises, all of the external borrowing is on a fixed rate basis. Therefore, and in line with advice from the treasury advisors, the intention is to hold off undertaking any borrowing until absolutely necessary, in anticipation that rates will reduce, even if not to the levels available in recent years. However, this position will be reviewed on a regular basis in conjunction with the treasury advisors, and a decision could be taken to undertake borrowing in advance of need where it was felt to be appropriate, and affordable, in order to mitigate against future interest rate rises.

Risks

Risk	Impact of Risk if it occurs* (H/M/L)	Probability of risk occurring (H/M/L)	What is the Council doing or what has it done to avoid the risk or reduce its effect	Who is responsible for dealing with the risk?
Investment counterparty not repaying investments	High, but depending on investment value.	Low	The Council only invests with institutions with very high credit scores. It employs advisors to monitor money market movements and changes to credit scores and acts immediately should things change adversely. The lower levels of funds available for investment will also alleviate the risk. Colleagues also monitor financial circulars and Treasury consultants advice to be able to respond in a timely fashion, and withdrew its investment from one local authority recently.	Members, Head of Finance, Treasury staff, based on advice from treasury advisors
Interest Rates moving adversely	Medium	Medium	Interest rates remain high, although are more stable than in recent times. However, the	Head of Finance, Treasury

against expectations			Council's external borrowing is based on fixed interest rates, although there is a degree of risk in relation to LOBOs. The Council will continue to monitor interest rates in anticipation of a medium term need to borrow and will work with its treasury advisors to identify the optimum time to undertake any new borrowing.	staff, treasury advisors

* Taking account of proposed mitigation measures

Links to Council Policies and Priorities

It is the Council's policy to ensure that the security of the capital sums invested is fully recognised and has absolute priority. The Council follows the advice of the Welsh Government that any investment decisions take account of security, liquidity and yield in that order.

Options Available and considered

The Prudential Code and statute requires that, during and at the end of each financial year, reports on these matters are presented to Council for approval.

Preferred Option and Why

The approach required by statute is quite prescriptive, such that there aren't many choices/options. This report is a regular half yearly event. The Governance and Audit Committee acts as the main scrutiny mechanism before a similar report is received by Cabinet/Council. The approach remains unchanged in advocating that the Committee notes the contents of the report in relation to treasury activities and indicators and provides endorsement or feedback pertinent to add to the Cabinet/Council report.

Comments of Chief Financial Officer

Decisions made on treasury matters will be made with a view to comply with the Treasury Management Strategy, Prudential Indicators, taking advice, where needed, from our treasury advisors.

The report reflects a slightly more active period, from a treasury management perspective, than in recent periods. Although borrowing levels have reduced slightly, as expected, due to the redemption of some small maturity loans and EIP loan repayments, the need to refinance three £5m LOBO loans required the Council to access new external borrowing via the PWLB. This is the first time new long term borrowing has been required for a number of years. Also, investment balances have significantly reduced during the second half of the year. This was expected to happen, in line with the intended use of reserves and consequent reduction in internal borrowing capacity, coupled with the continuation of the capital programme delivery. As highlighted in previous reports, and confirmed by the Liability Benchmark indicator, there remains an underlying, short to medium-term, need to borrow, which is currently anticipated to crystallise during 2024/25. The lower level of investment balances, compared to previous years, is a clear indication of this borrowing need starting to crystallise.

The indications are that interest rate volatility has now calmed, with our treasury advisors forecasting that rates will remain broadly in line with current levels, before starting to steadily reduce. Because of this, there is not an intention to undertake new long-term external borrowing until absolutely necessary, unless there are financial advantages of doing so. Rates will be more closely monitored on a regular basis, to identify any change in circumstances. This is especially important, considering there is a certain need to undertake new borrowing of circa £20m towards the end of the financial year, due to some large loans maturing in

March 2025, plus the impact of the reducing internal borrowing capacity, as well as the possibility that the remaining LOBOs could be called during the year.

Because of the reduction in investment balances, it means that cashflow management will be more challenging, particularly towards the end of each month. As a result, it is likely that some short-term borrowing will need to be undertaken to assist with managing day to day cashflow requirements. As and when that is required, the Head of Finance has the necessary delegated authority to undertake this.

Comments of Monitoring Officer

There are no legal implications. The in year and annual treasury management report is consistent with relevant Chartered Institute of Public Finance and Accountancy Guidance, Treasury Management principles and the Council's investment Strategy.

Comments of Head of People, Policy and Transformation

The Wellbeing of Future Generations Act requires public bodies to balance immediate financial pressures with the need to act sustainably over the longer-term. This is reflected in the Council's treasury management strategy, which includes regular reporting and monitoring arrangements.

There are no direct HR implications contained within the report.

Comments of Cabinet Member

N/A

Local issues

N/A

Scrutiny Committees

N/A

Fairness and Equality Impact Assessment:

- **Wellbeing of Future Generation (Wales) Act**
- **Equality Act 2010**
- **Socio-economic Duty**
- **Welsh Language (Wales) Measure 2011**

For this report, a full Fairness and Equality Impact Assessment has not been undertaken. This is because this report is not seeking any strategic decisions or policy changes, with its purpose being to update on the treasury management activities for the year retrospectively. However, fairness and equality are considered as part of service delivery and will feature in annual finance reports, such as the Treasury and Capital Strategy.

In terms of the Wellbeing of Future Generations (Wales) Act, and the five ways of working contained within it, this report highlights examples of these being supported. This report is a backwards looking report of the treasury management activities of the Council. It shows that we followed the treasury management strategy and the compliance with prudential code and treasury management indicators. This links into the long-term objectives of the authorities and ensures that the Councils' activities are carried out in an affordable, prudent and sustainable manner.

In the case of the Welsh Language, the service will continue to ensure that, wherever possible, services or information is available in the medium of Welsh.

The Equality Act 2010 contains a Public Sector Equality Duty, which came into force on 06 April 2011. The Act identifies a number of 'protected characteristics', namely age; disability; gender reassignment; pregnancy and maternity; race; religion or belief; sex; sexual orientation; marriage and civil partnership. The new single duty aims to integrate consideration of equality and good relations into the regular business of public authorities. Compliance with the duty is a legal obligation and is intended to result in better-informed decision-making and policy development and services that are more effective for users. Nothing in this report is considered to have a direct equality impact.

Consultation

N/A

Background Papers

Report to Council February 2023: Capital Strategy and Treasury Strategy.

Dated: 15th May 2024

APPENDIX A

Introduction

The Authority's treasury management strategy for 2023/24 was approved at a meeting on 28th February 2023. The Authority 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 risk remains central to the Authority's treasury management strategy.

External Context (Provided by the Council's Treasury Management Advisors

Economic background: UK inflation continued to decline from the 8.7% rate seen at the start of 2023/24. By the last quarter of the financial year headline consumer price inflation (CPI) had fallen to 3.4% in February, but was still above the Bank of England's 2% target at the end of the period. The core measure of CPI, i.e. excluding food and energy, also slowed in February to 4.5% from 5.1% in January, a rate that had stubbornly persisted for three consecutive months.

The UK economy entered a technical recession in the second half of 2023, as growth rates of -0.1% and -0.3% respectively were recorded for Q3 and Q4. Over the 2023 calendar year GDP growth only expanded by 0.1% compared to 2022. Of the recent monthly data, the Office for National Statistics reported a rebound in activity with economy expanding 0.2% in January 2024. While the economy may somewhat recover in Q1 2024, the data suggests that prior increases in interest rates and higher price levels are depressing growth, which will continue to bear down on inflation throughout 2024.

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

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

In the Bank's quarterly Monetary Policy Report (MPR) released in August 2023 the near-term projection for services price inflation was revised upwards, goods price inflation widespread across products, indicating stronger domestic inflationary pressure with second-round effects in domestic prices and wages likely taking longer to unwind than they did to emerge. In the February 2024 MPR the Bank's expectations for the UK economy were positive for the first half of 2024, with a recovery from the mild recession in calendar H2 2023 being gradual. Headline CPI was forecast to dip below the 2% target quicker than previously thought due to declining energy prices, these effects would hold inflation slightly above target for much of the forecast horizon.

Following this MPC meeting, Arlingclose, the authority's treasury adviser, maintained its central view that 5.25% remains the peak in Bank Rate and that interest rates will most likely start to be cut later in H2 2024. The risks in the short-term are deemed to be to the downside as a rate cut may come sooner than expected, but then more broadly balanced over the medium term.

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

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

Financial markets: Sentiment in financial markets remained uncertain and bond yields continued to be volatile over the year. During the first half of the year, yields rose as interest rates continued to be pushed up in response to rising inflation. From October they started declining again before falling sharply in December as falling inflation and dovish central bank attitudes caused financial markets to expect cuts in interest rates in 2024. When it emerged in January that inflation was stickier than expected and the BoE and the Federal Reserve were data dependent and not inclined to cut rates soon, yields rose once again, ending the period some 50+ bps higher than when it started.

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

Credit review: In response to an improving outlook for credit markets, in January 2024 Arlingclose moved away from its previous temporary stance of a 35-day maximum duration and increased its advised recommended maximum unsecured duration limit on all banks on its counterparty list to 100 days.

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

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

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

Credit default swap prices began the financial year at elevated levels following the fallout from Silicon Valley Bank and collapse/takeover of other lenders. From then the general trend was one of falling prices and UK lenders' CDS ended the period at similar levels to those seen in early 2023. Earlier in the year some Canadian lenders saw their CDS prices rise due to concerns over a slowing domestic economy and housing market, while some German lenders were impacted by similar economic concerns and exposure to commercial real estate towards the end of the period, with LBBW remaining the most elevated.

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

APPENDIX B

<u>Local Context</u>

On 31st March 2024, the Authority had net borrowing of £123.7m arising from its revenue and capital income and expenditure. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while balance sheet resources are the underlying resources available for investment. Whilst work on the

2023-24 Statement of Accounts remains a work in progress, a comparative draft illustration is provided in Table 1 below. These factors are summarised in Table 1 below.

Table 1: Balance Sheet Summary

	31.03.23 Actual £m	31.03.24 Actual £m
General Fund CFR	270.9	282.0
Less: *Other debt liabilities	38.5	36.1
Borrowing CFR	**232.4**	**245.9**
Less: Usable reserves	-139	-127
Less: Working capital	-2	4.7
Net borrowing	**91.4**	**123.7**

* finance leases, PFI liabilities and transferred debt that form part of the Authority's total debt

The figures included in the table above are currently draft until the work on the statement of accounts is completed.

The treasury management position on 31st March 2024 and the change over the 12 months is shown in Table 2 below.

Table 2: Treasury Management Summary

	31.3.23 Balance £m	Movement £m	31.03.24 Balance £m	31.03.24 Rate %
Long-term borrowing	128.7	(2.3)	126.4	3.5
Long term interest free borrowing	9.9	1.4	11.3	-
Short-term borrowing	0.0	-	-	-
Total borrowing	**138.6**	**(0.9)**	**137.7**	**3.5**
Long-term investments	(10.0)	0.0	(10.0)	3.5
Short-term investments	(30.2)	26.3	(3.9)	1.4
Cash and cash equivalents	(7.0)	7.0	-	-
Total investments	**(47.2)**	**33.3**	**(13.9)**	**4.9**
Net borrowing	91.4	32.3	123.7	8.4

The authority took out £15m of new long term borrowing in PWLB loans and £1.4m of new long-term interest free borrowing in 2023/24. The £15m from PWLB was to repay the three LOBO loans that had been recalled, so these loans just replaced existing funding and had no impact on the Council's overall total borrowing. The interest free borrowing was from Salix and included 6 new loans totalling £1.9m, which were linked to specific energy efficiency projects. The Council has redeemed two small PWLB loans at the end of September, which have not been refinanced, plus we have a number of loans with PWLB and Salix which are Equal Instalments of Principal (EIP) loans.

Short term investments have increased during the period, but this is part of the normal day to day treasury management activity of managing cashflows.

Borrowing

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

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

Borrowing strategy and activity

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

Interest rates have seen substantial rises over the last two years, although these rises have now begun to plateau. Gilt yields fell in late 2023, reaching April 2023 lows in December 2023 before rebounding to an extent in the first three months of 2024. Gilt yields have remained volatile, seeing upward pressure from perceived sticker inflation at times and downward pressure from falling inflation and a struggling economy at other times.

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

The cost of short term borrowing from other local authorities has generally risen with Base Rate over the year. Interest rates peaked at around 7% towards the later part of March 2024 as many authorities required cash at the same time. These rates are expected to fall back to more normal market levels in April 2024.

At 31st March 2024 the Authority held £137.7m of loans, decrease of £0.9m /similar position to 31st March 2023, as part of its strategy for funding previous [and current] years' capital programmes. Outstanding loans on 31st March are summarised in Table 3A below.

Table 3A: Borrowing Position

	31.3.23 Balance £m	Net Movement £m	31.03.24 Balance £m	31.03.24 Weighted Average Rate %	31.03.24 Weighted Average Maturity (years)
Public Works Loan Board	93.1	11.4	104.5	3.8	16.8
Banks (LOBO)	30.0	(15.0)	15.0	4.4	34.0
Banks (fixed-term)	5.0	-	5.0	3.8	53.9
Local authorities (long-term)	-	-	-	-	-
Local authorities (short-term)	-	-	-	-	-
Other inc. WG loans	9.9	1.4	11.3	-	0.5
Accrued interest	0.6	1.3	1.9	-	-
Total borrowing	**138.6**	**(0.9)**	**137.7**	**3.5**	**18.9**

The Authority's borrowing decisions are not predicated on any one outcome for interest rates.

LOBO loans: On 1st April 2023 the Authority held £30m 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 Authority has the option to either accept the new rate and terms or to repay the loan at no additional cost.

As market interest rates rose, there was increased probability of call options on the LOBOs being exercised by lenders. £30m of LOBO loans had annual/semi-annual call option dates during the year to 31st March 2024, lenders exercised options on the following of the Authority's loans:

	Amount £m	Rate %	Final Maturity	New rate proposed	Action taken by Authority
Loan 1	**5,000,000**	**5.05**	07/05/2042	**6.80%**	Repaid at no cost and refinanced by PWLB loan @ 4.8% for 17 years
Loan 2	**5,000,000**	**4.3**	29/04/2043	**5.20%**	e.g. repaid at no cost and refinanced by PWLB loan @ 4.82% for 12 years
Loan 3	**5,000,000**	**4.01**	22/05/2066	**5.85%**	e.g. repaid at no cost and refinanced by PWLB loan @ 4.61% for 15 years
Total	**15,000,000**				

The Authority has £15m LOBO loans with call dates within the next 12 months. The Authority has liaised with treasury management advisors Arlingclose over the likelihood of the options being exercised. If the option is exercised and an increased rate proposed, the Authority plans to repay the loan at no additional cost as accepting the revised terms would mean the Authority would still have refinancing risk in later years. If required, the Authority will repay the LOBO loans with available cash or by borrowing from other local authorities or the PWLB.

Other Debt Activity

Although not classed as borrowing, the Authority previously raised capital finance to afford Glan Usk School and the Southern Distributor Road. The Accounts for 2023-24 an outstanding liability of £36.1m to pay to the operator.

Treasury Investment Activity

The CIPFA Treasury Management Code now defines treasury management investments as those investments which arise from the Authority's cash flows or treasury risk management activity that ultimately represents balances that need to be invested until the cash is required for use in the course of business.

The Authority holds a level of invested funds, representing income received in advance of expenditure plus balances and reserves held. During the year, the Authority's investment balances ranged between £80.9 and £13.7 million due to timing differences between income and expenditure. The investment position is shown in Table 4 below.

Table 4: Treasury Investment Position

	31.3.23 Balance £m	Movement £m	31.03.24 Balance £m	31.03.24 Income Return %	31.03.24 Weighted average maturity Years
Banks & building societies (unsecured)	-	-	-	-	-
Government (incl. local authorities)	(30.2)	26.5	(3.7)	1.9	-
Money Market Funds	(7.0)	7.0	-	-	-

Covered Bonds	(10.0)	0.0	(10.0)	4.3	3.5
Accrued Interest	-	(0.3)	(0.3)	-	-
Total investments	**(47.2)**	**33.3**	**(13.9)**	**6.2**	**3.5**

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

As demonstrated by the liability benchmark in this report, the Authority expects to be a long-term borrower and new treasury investments are therefore primarily made to manage day-to-day cash flows using short-term low risk instruments.

Bank Rate increased by 1% over the period, from 4.25% at the beginning of April 2023 to 5.25% by the end March 2024. Short term rates peaked at 5.7% for 3-month rates and 6.7% for 12-month rates during the period, although these rates subsequently began to decline towards the end of the period.

The £10m that is available for longer-term investment is invested in covered bonds, which has been maintained since the last report and no change is expected in the medium term.

Non-Treasury Investments

The definition of investments in the Treasury Management Code now covers all the financial assets of the Authority as well as other non-financial assets which the Authority holds primarily for financial return. Investments that do not meet the definition of treasury management investments (i.e. management of surplus cash) are categorised as either for service purposes (made explicitly to further service objectives) and or for commercial purposes (made primarily for financial return).

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

The Authority also held investments in

- directly owned property such as office and commercial units of £9.6m
- loans to developers £10.3m
- shareholding in subsidiaries £0.3m

These investments generated £1.02m in 2023/24 of investment income for the Authority after taking account of direct costs.

Compliance

The Head of Finance reports that all treasury management activities undertaken during the quarter complied fully with the principles in the Treasury Management Code and the Authority's approved Treasury Management Strategy. Compliance with specific investment limits is demonstrated in Table 7 below.

Table 7: Investment Limits

Sector	Time limit	Counterparty limit	Sector limit	31.03.24 Actual	Complied? Yes / No
The UK Government	50 years	Unlimited	n/a		✓

Local authorities & other government entities	25 years	£10m	Unlimited	3.7	✓
Secured investments *	25 years	£10m	Unlimited	10.0	✓
Banks (unsecured) *	13 months	£10m	Unlimited	-	✓
Building societies (unsecured) *	13 months	£10m	£10m		✓
Registered providers (unsecured) *	5 years	£10m	£25m		✓
Money market funds *	n/a	£10m	Unlimited	-	✓
Strategic pooled funds	n/a	£10m	£25m		✓
Real estate investment trusts	n/a	£10m	£25m		✓
Other investments *	5 years	£10m	£5m		✓

Compliance with the Authorised Limit and Operational Boundary for external debt is demonstrated in Table 8 below.

Table 8: Debt and the Authorised Limit and Operational Boundary

	2023/24 Maximum	31.03.24 Actual	2023/24 Operational Boundary	2023/24 Authorised Limit	Complied? Yes / No
Borrowing	138	137.7	150	246	✓
PFI and Finance Leases	36.1	36.1	39	39	✓
Total debt	**174.1**	**173.7**	**189**	**285**	✓

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

Treasury Management Prudential Indicators

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

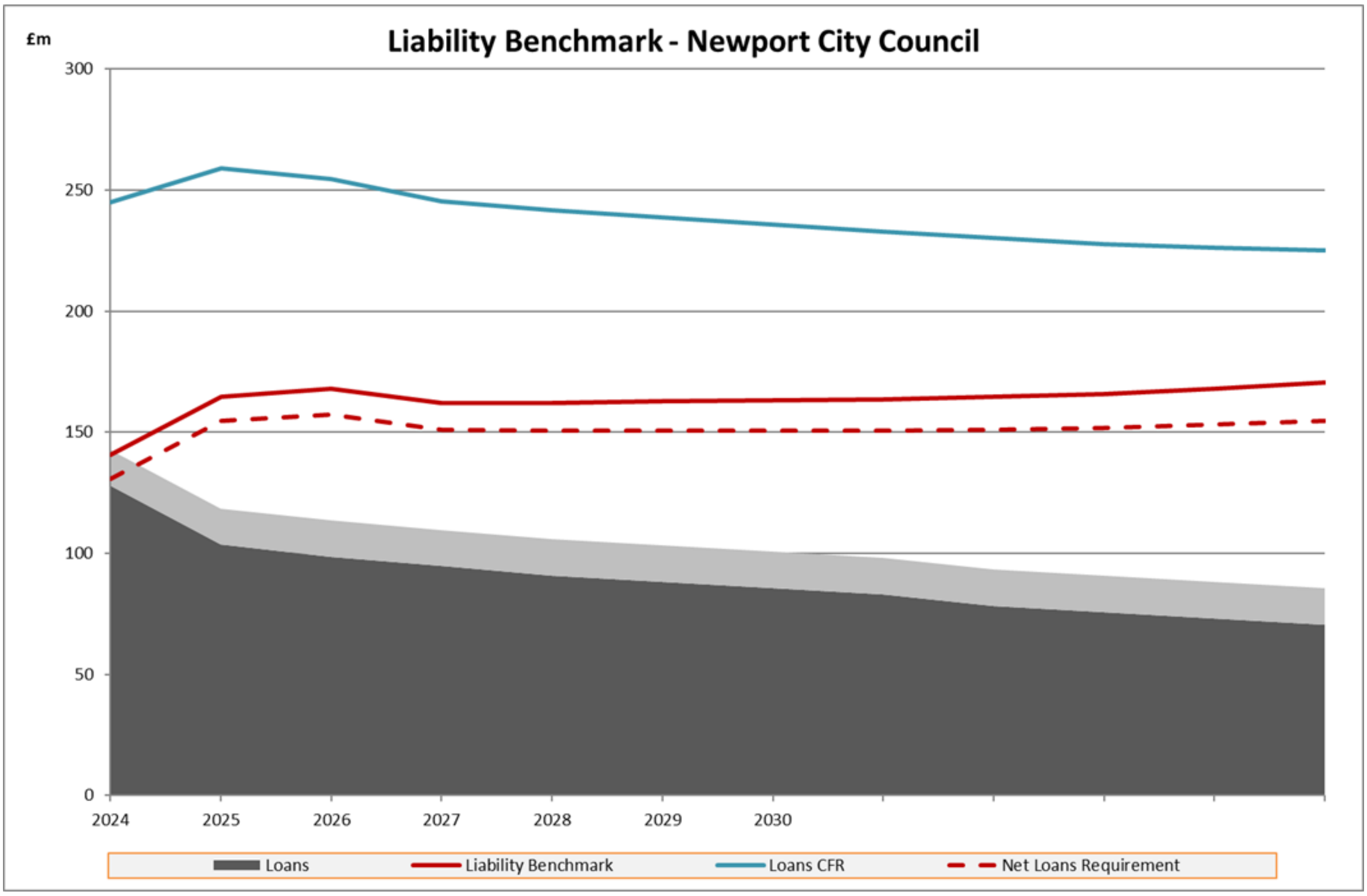
1. Liability Benchmark:

This new indicator compares the Authority's actual existing borrowing against a liability benchmark that has been calculated to show the lowest risk level of borrowing. The liability benchmark is an important tool to help establish whether the Council is likely to be a long-term borrower or long-term investor in the future, and so shape its strategic focus and decision making. It represents an estimate of the cumulative amount of external borrowing the Council must hold to fund its current capital and revenue plans while keeping treasury investments at the minimum level of £10m required to manage day-to-day cash flow.

	31.3.23 Actual	31.3.24 Actual	31.3.25 Forecast	31.3.26 Forecast
Loans CFR	232.2	245.9	258.7	254.5
Less: Balance sheet resources	-125.3	-127	-103.8	-96.8
Net loans requirement	106.9	118.9	154.9	157.7
Plus: Liquidity allowance	10	10	10	10
Liability benchmark	**116.9**	**128.9**	**164.9**	**167.7**
Existing borrowing	**-137.2**	**-137.7**	**-135.4**	**-130.9**

The figures included in the table above are currently draft until the work on the statement of accounts is completed.

Following on from the medium-term forecast above, the long-term liability benchmark assumes no new capital expenditure funded by borrowing until 2027/28 (other than that already approved as part of the Capital Programme or contained within the existing capital headroom), minimum revenue provision on new capital expenditure based on a 25 year asset life and income, expenditure and reserves all increasing by inflation of 2.5% p.a. This is shown in the chart below together with the maturity profile of the Authority's existing borrowing.



Whilst borrowing may be above the liability benchmark, strategies involving borrowing which is significantly above the liability benchmark carry higher risk.

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

	31.03.24 Actual	Upper limit	Lower limit	Complied
Under 12 months	32%	60%	0%	✓
12 months and within 24 months	4%	40%	0%	✓
24 months and within 5 years	9%	40%	0%	✓
5 years and within 10 years	14%	40%	0%	✓
10 years and within 20 years	18%	30%	0%	✓
20 years and within 30 years	3%	20%	0%	✓
30 years and within 40 years	15%	20%	0%	✓
40 years and within 50 years	4%	20%	0%	✓

50 years and above	0%	20%	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.

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

	2023/24	**2024/25**	**2025/26**	**No fixed date**
Actual principal invested beyond year end	10	10	10	10
Limit on principal invested beyond year end	£10m	£10m	£10m	£10m
Complied	✓	✓	✓	✓

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

Interest Rate Exposures: This indicator is set to control the Authority's exposure to interest rate risk. Bank Rate rose by 1.00% from 4.25% on 1st April 2023 to 5.25% by 31st March 2024.

Interest rate risk indicator	**Limit**	**31.03.24 Actual**	**Complied**
Upper limit on one-year revenue impact of a 1% rise in interest rates	£200,000	183,813	✓
Upper limit on one-year revenue impact of a 1% fall in interest rates	£100,000	36,750	✓

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

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

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