Policy Committee

19 February 2024

Reading Borough Council
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Title	Treasury Management Strategy Statement 2024/25
Purpose of the report	To make a recommendation to Council
Report status	Public report
Report author	Stuart Donnelly, Financial Planning & Strategy Manager
Lead Councillor	Councillor Brock, Leader of the Council
Corporate priority	Not applicable, but still requires a decision
Recommendations	**That Policy Committee endorse and recommend that Council approve:** 1. The Treasury Management Strategy Statement for 2024/25 as set out in Appendix 1 Section 2; 2. The Capital Prudential Indicators as set out in Appendix 1 Section 3; 3. The Minimum Revenue Provision (MRP) Policy for 2024/25 as set out in Appendix 1 Section 4 (noting the potential requirement for a revised MRP Policy to be brought forward once the outcome of the current MRP Consultation has been announced); 4. The Borrowing Strategy for 2024/25 as set out in Appendix 1 Section 5; 5. The Annual Investment Strategy for 2024/25 as set out in Appendix 1 Section 6; 6. The Prudential and Treasury Management Indicators as set out in Appendix 1 Annex 1.

1. Executive Summary

1.1. The Council's Treasury Management Strategy Statement (TMSS), attached at Appendix 1, sets out the parameters for the Council's planned treasury activity during 2024/25 under which the Council's Treasury Team will manage day to day activity. The TMSS reflects the Council's Draft Capital Programme 2024/25 – 2026/27.

1.2. The successful identification, monitoring and control of financial risk are central to the Strategy.

1.3. The CIPFA 2021 Prudential Code also requires the Council to prepare a Capital Strategy report which sets out the Council's capital requirements arising from policy objectives, as well as the associated governance procedures and risk appetite.

1.4. The Capital Strategy is reported separately from the Treasury Management Strategy Statement and includes non-treasury investments. The CIPFA Treasury Management Code 2021 further breaks down non-treasury investment into:

- Investments for service purposes – taken or held primarily for the provision and for the provision and for the purposes of delivering public services (including housing, regeneration, and local infrastructure), or in support of joint working with others to deliver such services.

- Investment for commercial purposes - taken or held primarily for financial return and are not linked to treasury management activity or directly part of delivering services.

1.5. In December 2023, the Government launched a further consultation on proposed changes to the capital framework for Minimum Revenue Provision (MRP) and a new consultation relating to additional flexibilities to use capitalisation without the requirement to approach Government (further details are set out in Sections 7 and 8 respectively). As the outcome of these consultations have not yet been announced, the MRP Policy, set out within Appendix 1 to this report, and the Council's use of capitalisation and capital receipts have all been based on the existing guidance and legislation. Depending on the outcome of these consultations, and any proposed implementation dates of any new guidance, there may be a requirement for amended policies to be brought back to Council for approval in advance of February 2025.

2. Policy Context

2.1. In accordance with the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2021 and the CIPFA Prudential Code for capital finance in local authorities (2021), the Council is required to approve a Treasury Management Strategy before the start of each financial year. This report fulfils that obligation.

3. Economic Background

3.1. Following the Bank of England Monetary Policy Committee (MPC) meeting on 1st February 2024, the Bank Rate was retained at 5.25%, where it has sat since August 2023. The Council's Treasury Management advisors, Link Group, are currently forecasting that Bank Rate will begin to gradually reduce from Quarter 2 of 2024/25 and ultimately levelling out at 3.00% from Quarter 3 of 2025/26.

3.2. The annual inflation rate in the United Kingdom as measured by the Consumer Prices Index (CPI) stands at 4.0% as at December 2023, down from 10.5% in December 2022. The Consumer Prices Index including owner occupiers' housing cost (CPIH) stands at 4.2% as at December 2023, down from 9.2% in December 2022.

4. Borrowing

4.1. Under the Prudential Code, the Council can borrow to fund capital expenditure if such borrowings are sustainable, affordable, and prudent. In order to comply with the Prudential Code, an authority must not borrow to invest primarily for financial return.

4.2. The underlying need to borrow (the net borrowing requirement) for capital purposes is measured by the Capital Financing Requirement (CFR). Usable reserves and working capital are the underlying resources available for investment.

4.3. Historically the Council has borrowed to pay for new assets including schools, roads, housing and community facilities etc. The value of the Council's assets is circa £1.2bn. As at 31st December 2023, the Council had £402.670m of loans outstanding in respect of General Fund and Housing Revenue Account (HRA) assets.

4.4. The Council has not taken out any long-term borrowing in 2023/24 to 31st December 2023 but has utilised the temporary borrowing market when required in line with the 2023/24 Borrowing Strategy. As at 31st December 2023, the Council had an outstanding temporary borrowing portfolio of £39.000m as set out in Appendix 1 Annex 3.

4.5. Market projections, per Table 11 in Appendix 1, indicate that long-term borrowing costs will begin to reduce in line with the forecast decreases to the Bank of England Bank Rate as set out above. Consequently, the Council intends to continue with the strategy of utilising lower cost temporary borrowing in the coming year where required. This strategy will be kept under review with the Council's Treasury Management Advisors. Longer term borrowing will not be taken out until necessary, thereby avoiding the "cost of carry" (the difference between the cost of borrowing and return on investing the funds until such time as the borrowing is required to fund the capital expenditure incurred).

4.6. The Capital Programme 2024/25-2026/27 totals £290.956m (£170.737m General Fund and £120.219m HRA) as set out in Table 1 of Appendix 1. The Programme aims to improve the infrastructure, asset base and effectiveness of service provision for the residents of Reading.

4.7. After accounting for specific grants, s106 contributions and capital receipts, the total borrowing requirement is £100.867m per Table 2 of Appendix 1 (£61.496m General Fund and £39.371m HRA). The cost of borrowing together with any associated revenue savings is included within the Council's Medium-Term Financial Strategy 2024/25 – 2026/27.

4.8. After reducing the borrowing requirement by a total Minimum Revenue Provision charge of £38.382m across the period, the Council has a projected increase in its CFR of £62.485m, as set out in Table 3 of Appendix 1.

4.9. The Director of Finance has delegated responsibility for borrowing and works closely with the Council's Treasury Management Team and advisors, Link Group, on borrowing decisions taking into account several factors including:

- The cost of borrowing short or long-term;
- Anticipated changes in the cost of borrowing;
- The level of cash balances held under investment;
- The return on invested balances.

4.10. The Council's long-term borrowing (loans over 12 months in length) is from two sources: The Public Works Loans Board (PWLB) and private banks for debt relating to Lender Option Borrower Option loans (LOBO loans currently stand at £15m). For short term borrowing the Council will continue to use other sources of finance, e.g. loans from other local authorities that it can borrow from at lower rates of interest than PWLB.

4.11. The framework for taking borrowing decisions in the coming year is set out in the Council's TMSS, attached at Appendix 1 Section 5. The Council may increase its longer term borrowing to cover new capital project expenditure in advance of need to minimise the risk of interest rate fluctuations. Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates and will be considered carefully to ensure that value for money can be demonstrated, that the costs of borrowing can be met and that the Council can ensure the security of such funds.

4.12. The Council's self-imposed limits on sustainable, affordable and prudent borrowing and investment, the Prudential and Treasury Management Indicators that need to be approved by Council are set out in Appendix 1.

5. Investments

5.1. The Council's investments for Treasury Management purposes seek to manage fluctuations in cash-flow. Treasury investments can be called on at short-notice and in the main are held in Money Market Funds or short-term fixed term deposits. These are low-risk investments and give higher rates of interest compared to leaving balances in the Council's bank account. The long-term treasury investment held by the Council is in the CCLA property fund.

5.2. The level of investments fluctuates throughout the year dependent on cash balances. The balance of treasury investments was £52.918m at the end of December 2023 (per Table 6 in Appendix 1). The average interest was 5.29% and the average weighted rate of return 3.34%.

5.3. The Council can legally invest in the following funds and instruments:

- Fixed Term Deposits (Government, public sector bodies, Banks and Building Societies)
- Callable deposits (Banks and Building Societies)
- Money Market Funds
- Certificates of Deposit (tradable term deposits)
- Governments Gilts and Treasury Bills
- Corporate Bonds
- Derivatives (where used for risk management)

5.4. The Department for Levelling Up, Housing and Communities (DLUHC) published updated guidance on investments in February 2018. The previous edition covered treasury investments only, but the latest edition focuses on non-treasury investments. These are commercial investments such as the purchase of investment properties, investments in subsidiaries or investments for service objectives including regeneration.

5.5. The revised PWLB borrowing terms announced in November 2020, prevent Local Authorities from borrowing from the PWLB for any purpose should their ongoing Capital Programme contain commercial schemes that are primarily investments to generate a financial yield. Consequently, Policy Committee approved the removal of the Capital budget for the Purchase of Commercial Property from its Capital Programme at its meeting in December 2020.

6. Approved Investments and Counterparties

6.1. The counterparty criteria are kept under regular review and are detailed in Annex X of the appendix to this report. The criteria set out the value and duration limits which are applied in the day to day investment of the Council's cash balances.

6.2. The value and duration limits as well as the minimum credit ratings required of individual institutions seek to minimise the Council's exposure to counterparty risk, i.e. limit any potential loss due to the failure of any single institution or group.

6.3. The credit ratings agencies' criteria are relative measures of financial strength, any changes are notified to the Council's Treasury Team on the same day by our treasury advisor, Link Group. Over recent years the agencies have downgraded many financial institutions by removing the implied sovereign support. However, financial institutions have responded by improving their capital ratios to meet new regulatory standards to enable them to withstand market shocks like that experienced during the financial crisis in 2008. This requirement for increased resilience is designed to give higher assurance that institutions will be going concerns in the medium to long term.

6.4. In addition, central banks such as the Bank of England and European Central Bank provide financial support to financial institutions through Term Funding Schemes (TFS) that ensures they have access to enough liquidity at low rates. The TFS was launched in 2016 and provides funding to banks and building societies at rates close to Base Rate.

6.5. CIPFA's Treasury Management Code (2021) requires the Council to set out its policies and practices relating to environmental, social and governance (ESG) investment considerations within its credit and counterparty policies. The framework for taking investment decisions in the coming year is set out in the Council's TMSS, attached at Appendix 1 Section 6 and includes the use of credit rating agencies' criteria, which incorporate Environmental, Social & Governance (ESG) risks alongside more traditional financial risk metrics, and the application of the Freedom House Global Freedom rating system.

6.6. The Freedom House Global Freedom rating system is a scored assessment of people's access to political rights and civil liberties in 210 countries and territories. In its annual Freedom in the World report, Freedom House assigns a numerical score and a Free/Partly Free/Not Free status to each country. The Council will only invest in organisations from countries with a 'Free' rating. Ratings will be regularly monitored to determine if ratings have changed.

7. Minimum Revenue Provision (MRP) Consultation

7.1. On 30th November 2021, the Department for Levelling Up, Housing & Communities published a consultation about proposed changes to the capital framework for Minimum Revenue Provision (MRP). MRP is the amount that has to be set aside from the revenue budget for the financing of capital expenditure.

7.2. The consultation responses highlighted concerns raised by a number of authorities that the changes, as revised, could have unintended consequences that could adversely affect the delivery of priorities such as housing where councils were providing capital loans to finance delivery. In response to sector concerns, the proposals were amended to offer more flexibility regarding capital loans, balancing the need for MRP with the risk of non-repayment. The consultation on these changes ran from June to July 2022.

7.3. A further consultation, seeking views on the proposed changes to the Statutory MRP Guidance and Regulations, in line with changes proposed in the June to July 2022 consultation (with some minor changes to reflect consultation responses), was launched on 21st December 2023. This consultation will close on 16th February 2024 with the Government response expected on 15th March 2024.

7.4. One of these proposals would, if implemented, require councils to provide MRP on any commercial loans given to third parties and wholly owned companies. MRP would not need to be provided for non-commercial loans as long as the loan was being re-paid. The Council's current MRP Policy, as well as repayment schedules of the loans to the Council's wholly owned companies would therefore need to be reviewed and any required additional budgetary provision made within the Council's revenue budget in order to comply with this change, should it materialise.

7.5. The latest information we have is that any changes will take effect from 2024/25 at the earliest; it is not the Government's intention that these changes are applied retrospectively.

7.6. As the outcome of this consultation is still outstanding, the 2024/25 MRP Policy, contained within the 2024/25 Treasury Management Strategy has been prepared in line with the current guidance and regulations.

8. Local Authority Capital Flexibilities Consultation

8.1. The current Flexible Capital Receipts Directive issued by Central Government, which allows Local Authorities to use Capital Receipts to fund revenue expenditure which generates future and ongoing savings and service transformation, is currently due to end on 31st December 2025.

8.2. On 19th December 2023, the Government launched a consultation seeking to engage with councils to identify and develop options for the use of capital resources and borrowing to support and encourage invest-to-save activity, and more flexibilities to use capitalisation without the requirement to approach Government.

8.3. The Government has not committed to any of the options set out in the consultation but at a high level these can be categorised as:

a. **Supporting invest-to-save activity**. Increasing the flexibilities to use capital receipts and borrowing to finance the costs of transformation and efficiency projects;

b. **Local management of budget pressures.** Providing greater flexibilities on the use of capital receipts, including the scope to meet general budget pressures, and potential additional flexibilities where the proceeds relate to the sale of investment properties.

8.4. The options are not intended to be mutually exclusive, and local authorities that use any new flexibilities provided by the Government will be expected to put in place plans to reduce costs and improve efficiency in a way that reduces future risk.

8.5. The Government has not announced an expected response date in respect of this consultation. The 2024/25 Budget and Medium Term Financial Strategy 2024/25, the Capital Strategy 2024/25 (including the Flexible Capital Receipts Strategy) and the Treasury Management Strategy Statement have all therefore been prepared in alignment with the current guidance relating to the flexible use of capital receipts.

9. Risk Controls

Investment Risk

9.1. The main risk of investing is that the borrower or counterparty defaults on the loan and cannot repay it.

9.2. The main controls on investment risk are the application of counterparty criteria which limit the amount and duration of investments with both individual and groups of related counterparties. The criteria are generally based on rating agency evaluations as detailed in Appendix 1 Section 6.

Borrowing Risk

9.3. The main risks when deciding to borrow is around the timing of the decision and ensuring affordability. There is a risk that interest rates will increase before any planned borrowing is taken. The Council receives regular interest rate forecasts which are used to inform decisions on the timing of external borrowing.

9.4. The latest guidance requires the use of other information as well as rating agency evaluations. When ratings change, the Treasury Team are notified on the same day by our treasury advisors. There are regular internal and external meetings the Treasury Team attend to keep abreast of latest topics. The monthly updates from Link Group include other market sources of information, such as the prices of financial instruments and shares. In addition, professional publications and sector specific reports are reviewed by the Team to ensure that any decision to borrow is based a broad array of available information.

9.5. The Treasury Management Policies deal with risk controls, decision making and reporting processes, along with high level administration of the Treasury Management activities.

10. Contribution to Strategic Aims

10.1. Full details of the Council's Corporate Plan and the projects which will deliver these priorities are published on the Council's website. These priorities and the Corporate Plan demonstrate how the Council meets its legal obligation to be efficient, effective, and economical. An updated Corporate Plan will be presented to Council in February 2024.

10.2. Delivery of the Council's revenue and capital budgets is essential to ensuring the Council meets its strategic aims and remains financially sustainable going forward. The treasury management functions are crucial in ensuring that the Council has access to funds when required and in investing surplus funds in secure investments.

11. Environmental and Climate Implications

11.1. There are no environmental implications arising directly from this report.

11.2. As set out in the Council's Annual Investment Strategy (Appendix 1 paragraph 6.18), the Council will not knowingly invest directly in businesses whose activities and practices pose a risk of serious harm to individuals or groups, or whose activities are inconsistent with the Council's Corporate Plan and values. This would include institutions with material links to environmentally harmful activities (e.g. pollution, destruction of habitat, fossil fuels).

12. Community Engagement

12.1. Budget-related communications and consultations will continue to be a priority over the next three years as we work to identify savings.

13. Equality Implications

13.1. Under the Equality Act 2010, Section 149, a public authority must, in the exercise of its functions, have due regard to the need to:

- eliminate discrimination, harassment, victimisation and any other conduct that is prohibited by or under this Act;
- advance equality of opportunity between persons who share a relevant protected characteristic and persons who do not share it;
- foster good relations between persons who share a relevant protected characteristic and persons who do not share it.

13.2. There are no equality implications arising directly from this report.

14. Other Relevant Considerations

14.1. There are none.

15. Legal Implications

15.1. This report assists the Council in fulfilling its statutory obligation to set out its Treasury Strategy for borrowing and to prepare an Annual Investment Strategy for the coming year setting out the Council's policies for managing its borrowing and investments and giving priority to the security and liquidity of those investments.

16. Financial Implications

16.1. The financial implications are set out within the main body of this report and Appendix 1.

17. Timetable for Implementation

17.1. Not applicable.

18. Background Papers

18.1. There are none.

Appendices

1. Treasury Management Strategy Statement 2024/25