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Audit Committee

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Treasury Management Strategy Mid-Year Review Report 2024/25

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Summary

This report gives an overview of treasury management activity since 1 April 2024 and presents a review of the Treasury Strategy approved by Council on 29 February 2024.

The key indicators are set out in the table below:

Indicator	**2024/25**	**2025/26**	**2026/27**	**2027/28**
	£000	**£000**	**£000**	**£000**
Capital Expenditure	106,217	119,792	68,499	23,175
General Fund (GF) Capital Financing Requirement (CFR) at year end	520,442	614,721	654,913	660,907
Housing Revenue Account (HRA) Capital Financing Requirement (CFR) at year end	59,598	72,336	83,995	92,682
Total Capital Financing Requirement at year end	580,039	687,057	738,909	753,589
External Borrowing	547,152	654,170	706,022	720,702
Underborrowing	32,887	32,887	32,887	32,887

The movement in the capital financing requirement is shown below:

GF Capital Financing Requirement	**2024/25**	**2025/26**	**2026/27**	**2027/28**
	£000	**£000**	**£000**	**£000**
Opening Balance	453,632	520,442	614,721	654,913
Add Unfinanced Capital Expenditure	39,267	77,212	47,888	13,882
Add Long Term Debtors (Capital Loans)	97,216	24,612	0	0
Less Minimum Revenue Provision (MRP)	(6,343)	(6,166)	(6,343)	(6,558)
Less KCC Debt Repayment	(1,110)	(1,065)	(1,023)	(982)
Less Repayment of Capital Loans	(62,220)	(313)	(330)	(348)
Closing CFR	**520,442**	**614,721**	**654,913**	**660,907**

HRA Capital Financing Requirement	2024/25	2025/26	2026/27	2027/28
	£000	£000	£000	£000
Opening Balance	45,844	59,598	72,336	83,995
Add Unfinanced Capital Expenditure	14,215	13,219	11,916	8,954
Less Voluntary Revenue Provision (VRP)	(461)	(481)	(256)	(267)
Closing CFR	**59,598**	**72,336**	**83,995**	**92,682**

1. Recommendations

1.1. The Committee is requested to consider this report, note its contents and note that the report will also be referred to Cabinet and Full Council.

2. Budget and Policy Framework

2.1. Audit Committee is responsible for the scrutiny of the Council's Treasury Management, Investment Strategy and Minimum Revenue Provision Policy Statement along with Treasury Management Practices and associated Schedules.

2.2. There needs to be, as a minimum, a mid-year review of treasury management strategy and performance. This is intended to highlight any areas of concern that have arisen since the original strategy was approved.

2.3. This report is also scheduled for consideration by Cabinet on 17 December 2024 and full Council on 23 January 2025.

3. Background

3.1. In December 2021 the Chartered Institute of Public Finance and Accountancy (CIPFA) issued revised Prudential and Treasury Management Codes. These require all local authorities to prepare a Capital Strategy which is to provide the following:

- A high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of service
- An overview of how the associated risk is managed
- The implications for future financial sustainability

3.2. The Council operates a balanced budget, which broadly means cash raised during the year will meet its cash expenditure. Part of the treasury management operations ensures this cash flow is adequately planned, with surplus monies being invested in low-risk counterparties, providing adequate liquidity initially, before optimising investment return.

3.3. The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing requirements of the Council, essentially the longer-term cash flow planning to ensure the Council can meet its capital spending liabilities. This management of longer-term cash may involve arranging long or short-term loans, or using long-term cash flow surpluses, and on occasion, debt previously incurred may be restructured to meet Council risk or cost objectives.

3.4. As a consequence, treasury management is defined as:

3.5. "The management of the local authority's 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."

3.6. The principal requirements of the Treasury Management In The Public Services Code of Practice (Treasury Management Code) are as follows:

(i) Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities;

(ii) Creation and maintenance of Treasury Management Practices (TMP's) which set out the manner in which the Council will seek to achieve those policies and objectives.

(iii) Receipt by full Council of an annual Treasury Management Strategy Statement - including as a minimum, the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead, a Mid-year Review Report and an Annual Report (stewardship report) covering activities undertaken during the previous reporting period;

(iv) Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

(v) Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific committee.

3.7. This mid-year report has been prepared in compliance with CIPFA's Code of Practice on Treasury Management, and covers the following:

- A review of the Treasury Management Strategy Statement and Annual Investment Strategy (Section 3);
- A review of the Council's borrowing strategy for 2024/25 (Section 4);
- A review of the Council's investment portfolio for 2024/25 (Section 5);
- A review of any debt rescheduling undertaken during 2024/25 (Section 6);
- A review of compliance with Treasury and Prudential Limits for 2024/25. (Section 7);
- An economic update for the first part of 2024/25 (Appendix).

4. Treasury Management Strategy Statement and Annual Investment Strategy Update

4.1. Full Council approved the 2024/25 Treasury Management Annual Investment Strategy on the 29 February 2024.

4.2. The Strategy stated that in the long-term aim of officers is to smooth out the maturity profile and reduce reliance on short-term borrowing but whilst holding some short-term debt to manage cash flow. However, as and a significant amount of capital receipts are expected in the next few years, a higher level of short to medium-term loans from other local authorities will be held in the immediate term. At 31 March 2024 short-term borrowing stood at £114million, short-term borrowing was £119million as at 30 September 2024. This figure includes £79million due for repayment before 31 March 2025. The aim over the next few months will be to avoid increasing the overall amount due for repayment in 2025/26 and concentrate new borrowing for repayment in 2026/27 to 2028/29 with ideally no more than £10m maturing each month.2026/27 onwards. Many of the new loans are likely to be taken from the Public Works Loans Board (PWLB). Any further smoothing would require the use of longer-term funding from PWLB and although still high, interest rates are on a downward trajectory meaning this option will become less expensive. The current position is shown in the graph at 5.8.

5. Borrowing & Borrowing Limits

5.1. The purpose of the Capital Financing Requirement (CFR) is to demonstrate that Council borrowing is undertaken to fund capital expenditure only. The CFR represents the long-term assets of the Council that have not been funded from sources other than borrowing, such as grants and external contributions, capital receipts or revenue funding. External borrowing should not exceed the CFR over the medium term. This allows some flexibility for limited early borrowing for future years. The Council has approved a policy for borrowing in advance of need which will be adhered to if this proves prudent.

5.2. An updated estimate of the CFR and borrowing position compared with the estimate included in the Treasury Strategy is shown in the table below:

CFR & Borrowing	Per 2024/25 Strategy £000	Revised Estimate £000
CFR 31 March 2025	573,924	580,039
External Debt	527,382	547,152
Under-borrowing	46,542	32,887
Estimated In Year Borrowing Required	56,004	76,564

5.3. The revision compared with the estimates arise from the evolution of the capital programme including changes to profiling and funding since the Strategy was formulated in late 2023.

5.4. The Chief Operating Officer (S.151 Officer) reports that no difficulties are envisaged for the current or future years in ensuring that borrowing does not exceed CFR.

5.5. A further prudential indicator controls the overall level of borrowing. This is the Authorised Limit, which represents the limit beyond which borrowing is prohibited, and needs to be set and revised by Members. It reflects the level of borrowing which, while not desired, could be afforded in the short term, but is not sustainable in a longer-term scenario. It is a forecast of maximum borrowing requirement with some capacity for unexpected movements. This is the statutory limit determined under section 3(1) of the Local Government Act 2003. The Council's authorised borrowing limit for 2024/25 is £713.516 million and it will not exceed this limit.

5.6. One of the risks inherent within Treasury management is "Interest rate risk". This risk is high where a large proportion of an organisation's borrowing portfolio reach termination point at the same time. The organisation has then to re-finance a large proportion of their portfolio at a set point in time with the risk that interest rates may not be favourable. The recent strategy has been to reduce interest rate risk and smooth the borrowing repayment profile by taking out new borrowing for longer repayment terms. Progress towards this aim has been limited by the factors noted above.

5.7. Link's latest forecast of interest rates issued on 16 October 2024 is as follows:

UK Interest Rate Forecast — LINK Group

Bank Rate	NOW	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27
Link Group	5.00%	4.50%	4.00%	3.50%	3.25%	3.25%	3.25%	3.25%	3.00%	3.00%	3.00%
Capital Economics	5.00%	4.75%	4.50%	4.25%	3.75%	3.25%	3.00%	3.00%	3.00%	3.00%	-

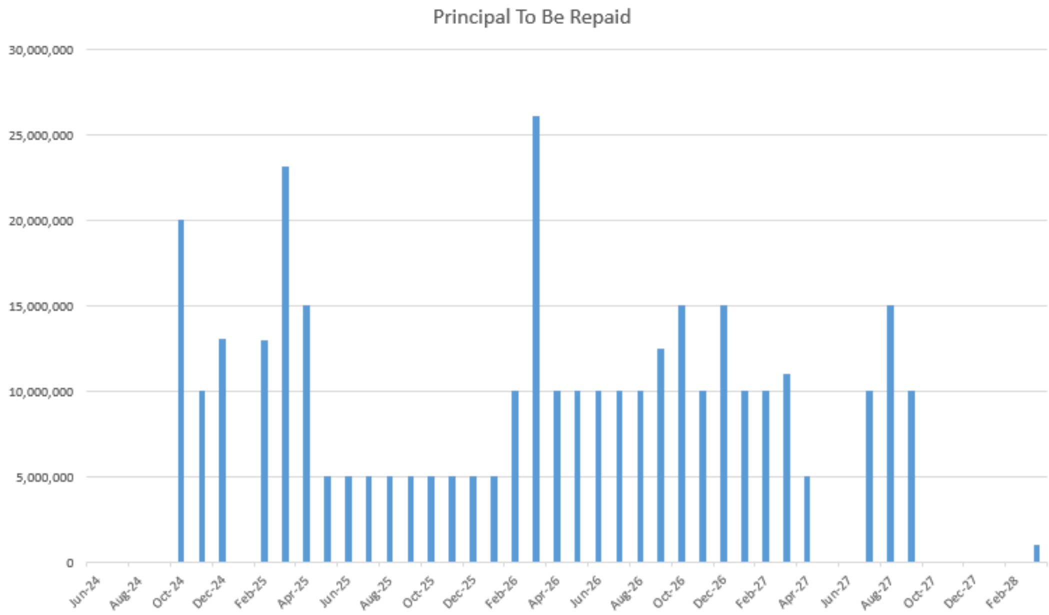
5yr PWLB Rate	NOW	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27
Link Group	4.80%	4.50%	4.30%	4.10%	4.00%	3.90%	3.90%	3.90%	3.90%	3.90%	3.80%
Capital Economics	4.80%	4.70%	4.60%	4.40%	4.30%	4.10%	4.10%	4.00%	4.00%	4.00%	-

10yr PWLB Rate	NOW	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27
Link Group	5.04%	4.60%	4.40%	4.30%	4.10%	4.10%	4.10%	4.00%	4.00%	4.00%	3.90%
Capital Economics	5.04%	4.80%	4.70%	4.60%	4.50%	4.30%	4.30%	4.20%	4.10%	4.10%	-

25yr PWLB Rate	NOW	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27
Link Group	5.53%	5.00%	4.80%	4.70%	4.50%	4.50%	4.40%	4.40%	4.40%	4.30%	4.30%
Capital Economics	5.53%	5.10%	4.90%	4.80%	4.70%	4.50%	4.50%	4.40%	4.30%	4.20%	-

50yr PWLB Rate	NOW	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27
Link Group	5.31%	4.80%	4.60%	4.50%	4.30%	4.30%	4.20%	4.20%	4.20%	4.10%	4.10%
Capital Economics	5.31%	5.10%	5.00%	4.80%	4.70%	4.60%	4.50%	4.40%	4.40%	4.30%	-

5.8. The graph in below shows the debt portfolio repayment profile as at 30 September. All debts are being shown as repayable at term, although the LOBO's (Lender Option Borrower Option) have a variety of "call" periods of between 6 months and every 5 years. The risk of a call occurring is higher than before due to the rise in interest but at the time of writing no approaches have been made by the lenders. As previously reported in Quarter One, a LOBO of £20m was repaid on a call date in April 24 following notice of an increase in the interest rate payable.



6. Investment Portfolio 2024/25

6.1. 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 which is consistent with the Council's risk appetite.

6.2. The investment portfolio yield on cash investments at 30 September 2024 ranges from 0.0% to 4.99%.

6.3. A full list of in house investments held as at 30 September is shown below:

Investments: Core Investments	**Principal £**	**Interest %**
CCLA Property Fund (September 2024 market value)	11,554,441	n/a
Patriza Hannover Property UT (September 2024 market value)	4,979,717	n/a
Lothbury Property Trust (April 2024 market value less redistributions to 08/11/24)*	1,216,371	n/a
Total Core Investments	**17,750,529**	n/a
Investments: Liquid investments	**Principal 30 September £**	**Interest %**
Svenska Handelsbanken	1,152	0.00%
Lloyds	4,129,739	4.88%
Barclays	4,546	1.00%
Santander	0	3.43%
CCLA Public Sector Deposit Fund	19,931,145	4.99%
Total Liquid Investment	**24,066,582**	n/a
Total In house Investments	**41,817,111**	**n/a**

6.4. Members may like to note the overall performance of the investment in property funds in the current financial year as shown below.

	CCLA	Patriza	Total		Lothbury*
	£000	£000	£000		£000
Opening Value 31 March	11,566	4,890	16,455	Value as at 30 April	3,632
Revaluation	(11)	90	79	Redistribution	(2,416)
Closing Value 30 September	11,554	4,980	16,534	Awaiting Redistribution	1,216
Dividend Received	307	98	405		
Overall Gain/ (Loss)	296	188	484		

* Lothbury Property Fund ceased on 31 May 2024. The trustees of the fund are redistributing the final fund valuations (30 April 2024) in Tranches as properties are sold. The Council has received 4 tranches to date with a total value of £2.416million, leaving a balance of £1.216million still to be received. The fund gives monthly statements as to the projected value of assets still to be sold, and based upon the latest statement, officers are confident that the Council will receive the remaining value of monies as soon as the properties the fund holds are sold.

6.5. The Council's finance and interest net expenditure for 2024/25 is estimated to result in a £1.8m underspend as at Round 2 as set out below:

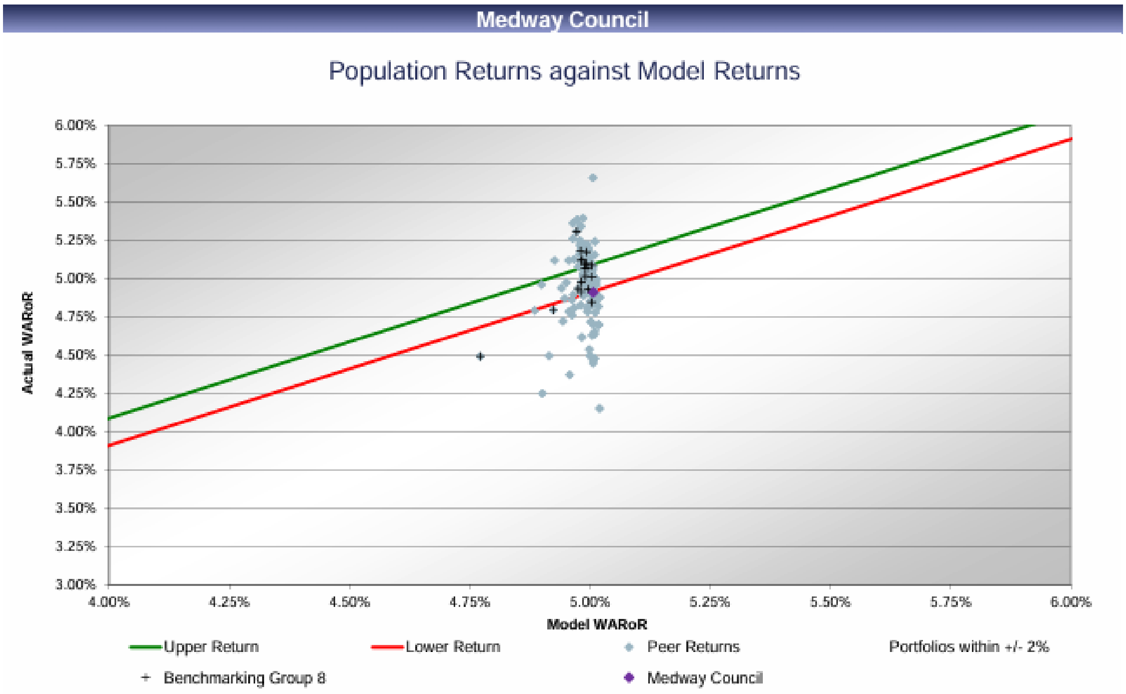
	2023/24 Outturn	Budget 2024/25	Round 2 Forecast	Round 2 Variance
	£000	£000	£000	£000
Interest Earned	(8,764)	(5,842)	(11,931)	(6,089)
Interest Paid	15,328	17,342	22,346	5,005
KCC Principal	1,156	1,204	1,110	(94)
MRP	6,077	6,442	5,792	(649)
Treasury Costs	145	65	91	26
TOTAL INTEREST & FINANCING	**13,943**	**19,211**	**17,409**	**(1,802)**

6.6. Investment Counterparty Criteria

6.6.1. The current investment counterparty criteria selection approved in the Treasury Strategy is meeting the requirement of the treasury management function.

6.7. Benchmarking

6.7.1. The in-house Treasury team, contribute to the Link Asset Services benchmarking club which produces quarterly reports. Shown below is a graph showing Medway's performance to September.



Medway Council	Actual WARoR	Model WARoR	Difference	Lower Bound	Upper Bound	Performance
	4.91%	5.01%	-0.09%	4.92%	5.10%	Below

6.7.2. The “x” axis of the graph shows the “Model Weighted Average Rate of Return”, this is easiest interpreted as the level of return we should expect for the level of risk that we are taking with our investment portfolio. This is then plotted against the “Actual Weighted Average Rate of Return” on the “y” scale, running diagonally upwards across the graph are two parallel lines, if a Council performance falls between these lines, then they are deemed to be receiving a return as would be expected for their level of risk, below these two lines and performance is considered below that expected and above then the return being received is above that expected. As can be seen Medway’s return fell just slightly below expectations for our level of risk. However, the data includes only at cash deposits and excludes property funds.

6.7.3. In assessing the risk inherent in an Investment Portfolio for the benchmarking, three factors are taken into account:

(i) The number of days to maturity of an investment. With a larger the number of days left to maturity the greater the risk that an adverse event could occur
(ii) The total number of days that the investment was originally invested for, again the longer an authority is comfortable to invest for the greater the risk it is willing to take.
(iii) The creditworthiness of the counterparties in which the authority invests.

6.7.4. The table below shows some detail from the September 2024 benchmarking data comparing Medway in-house performance against all participants of the benchmarking group: unitary authorities and other local councils.

Authority/Group	Model Weighted Average Rate of Return	Risk: Weighted Average Maturity (Days)	Risk: Weighted Average Total Time (Days)	Risk: Weighted Average Credit Risk	Weighted Average Rate of Return
Medway	**5.01%**	**0**	**0**	**1.69**	**4.91%**
Average English Unitaries (24)	n/a	58	134	1.82	4.95%
Average Total Population (229)	n/a	70	134	2.3	4.99%
Average Local Benchmarking Group (20)	n/a	93	225	2.37	5.01%
Brighton & Hove CC	4.77%	330	1307	2.96	4.77%
East Sussex CC	4.97%	85	235	2.34	4.97%
Sevenoaks DC	5.00%	12	14	1.21	5.00%
Tonbridge and Malling BC	4.98%	87	201	3.24	4.98%

7. Debt Rescheduling

7.1. Following the interest rate cut to 5% in August (4.75% in November) and the advice of Link Asset Services, loans that have matured have been re-borrowed with a medium-term maturity of 2-5 years. This enables there to be a better spread of maturities across the next 5 years. We will continue to monitor the situation and opportunities will be carefully considered.

8. Compliance with Treasury and Prudential Limits

8.1. It is a statutory duty for the Council to determine and keep under review the “Affordable Borrowing Limits”. Council’s approved Treasury and Prudential Indicators (affordability limits) are outlined in the approved Treasury Management Strategy Statement.

8.2. As reported at quarter one, the short-term Council’s short term borrowing limit was breached temporarily. There have been no breaches during quarter two of limits and indicators contained within the Treasury Management Strategy Statement and in compliance with the Council’s Treasury Management Practices.

9. Risk management

9.1. Risk and the management thereof is a feature throughout the Strategy and in detail within the Treasury Management Practices 1 published alongside the Treasury Management Strategy at the start of 2024.

10. Financial and legal implications

10.1. The finance and legal implications are highlighted throughout this report. The Council has delegated responsibility for the execution and administration of treasury management decisions to the Chief Operating Officer, who will act in accordance with the Council’s policy statement and Treasury Management Practices.

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Appendices

Appendix 1 – View of economic conditions

Background Papers

None