Treasury Management Strategy

Medway Council

2025-26

Contents

1. Introduction

1.1 The Authority is required to operate a balanced revenue budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low-risk counterparties or instruments commensurate with the Authority's low risk appetite, providing adequate liquidity initially before considering investment return

1.2 The second main function of the treasury management service is the funding of the Authority's capital plans. These capital plans provide a guide to the borrowing need of the Authority, essentially the longer-term cash flow planning, to ensure that it can meet its capital spending obligations. This management of longer-term cash may involve arranging long or short-term loans or using longer-term cash flow surpluses. On occasion, when it is prudent and economic, any debt previously drawn may be restructured to meet risk or cost objectives.

1.3 The contribution the treasury management function makes to the Authority is critical, as the balance of debt and investment operations ensure liquidity or the ability to meet spending commitments as they fall due, either on day-to-day revenue or for larger capital projects. The treasury operations will see a balance of the interest costs of debt and the investment income arising from cash deposits affecting the available budget. Since cash balances generally result from reserves and balances, it is paramount to ensure adequate security of the sums invested, as a loss of principal will in effect result in a loss to the General Fund Balance.

1.4 CIPFA defines treasury management as: *"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."*

2. Reporting requirements

2.1 Capital Strategy

2.1.1 The CIPFA 2021 Prudential and Treasury Management Codes require all local authorities to prepare a capital strategy report, which will provide the following:

- a high-level long-term overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services
- an overview of how the associated risk is managed
- the implications for future financial sustainability

2.1.2 The aim of this capital strategy is to ensure that all elected members fully understand the overall long-term policy objectives and resulting capital strategy requirements, governance procedures and risk appetite.

2.2 Treasury Management Reporting

2.2.1 The Council is required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of policies, estimates and actuals.

2.2.2 **Prudential and treasury indicators and treasury strategy** (this report): The first, and most important report is forward looking and covers:

- the capital plans (including prudential indicators).
- a minimum revenue provision (MRP) policy (how residual capital expenditure is charged to revenue over time).

- the Treasury Management Strategy (how the investments and borrowings are to be organised) including treasury indicators; and
- an Annual Investment Strategy (the parameters on how investments are to be managed).

2.2.3 **A mid-year treasury management report**: This is primarily a progress report and will update members on the capital position, amending prudential indicators as necessary, and whether any policies require revision. In addition, this Authority will receive quarterly update reports.

2.2.4 **An annual treasury report**: This backwards looking review provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

2.2.5 The above reports are required to be adequately scrutinised before being recommended to the Cabinet and finally to Council. This role is undertaken by the Audit Committee.

2.2.6 Quarterly reports – In addition to the three major reports detailed above, quarterly reporting (end of June/end of December) is also required. However, these additional reports do not have to be reported to Full Council but do require to be adequately scrutinised. This role is undertaken by the Audit Committee and Cabinet. (The reports, specifically, should comprise updated Treasury/Prudential Indicators.)

3. Treasury Management Strategy for 2025/26

3.1 The strategy for 2025/26 covers two main areas:

3.2 Capital issues

- the capital expenditure plans and the associated prudential indicators.
- the minimum revenue provision (MRP) policy.

3.3 Treasury management issues

- the current treasury position.
- treasury indicators which limit the treasury risk and activities of the Council.
- prospects for interest rates.
- the borrowing strategy.
- policy on borrowing in advance of need.
- debt rescheduling.
- the investment strategy.
- creditworthiness policy; and
- policy on use of external service providers.

3.4 These elements cover the requirements of the Local Government Act 2003, MHCLG Investment Guidance, MHCLG MRP Guidance, the CIPFA Prudential Code and the CIPFA Treasury Management Code.

3.5 Training

3.5.1 The CIPFA Treasury Management Code requires the responsible officer to ensure that members with responsibility for treasury management receive adequate training in treasury management. This especially applies to Members responsible for scrutiny. The training needs of Members and of treasury management officers are periodically reviewed. Members received a presentation by our treasury advisors, MUFG (previously Link), on 29th November 2023.

3.5.2 Furthermore, pages 47 and 48 of the Code state that they expect “all organisations to have a formal and comprehensive knowledge and skills or training policy for the effective acquisition and retention of treasury management knowledge and skills for those responsible for management, delivery, governance and decision making”.

3.5.3 The scale and nature of this will depend on the size and complexity of the organisation’s treasury management needs. Organisations should consider how to assess whether treasury management staff and council members have the required knowledge and skills to undertake their roles and whether they have been able to maintain those skills and keep them up to date.

As a minimum, authorities should carry out the following to monitor and review knowledge and skills:

- Record attendance at training and ensure action is taken where poor attendance is identified.
- Prepare tailored learning plans for treasury management officers and board/council members.
- Require treasury management officers and board/council members to undertake self-assessment against the required competencies (as set out in the schedule that may be adopted by the organisation).
- Have regular communication with officers and board/council members, encouraging them to highlight training needs on an ongoing basis.”

3.5.4 In further support of the revised training requirements, CIPFA’s Better Governance Forum and Treasury Management Network have produced a ‘self-assessment by members responsible for the scrutiny of treasury management’, which is available from the CIPFA website to download.

3.6 Treasury management consultants

3.6.1 The Council uses MUFG (Link) Treasury Services Limited as its external treasury management advisors.

3.6.2 The Council recognises that responsibility for treasury management decisions remains with the with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers. All decisions will be undertaken with regards to all available information including, but not solely, our treasury advisors.

3.6.3 It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented and subjected to regular review.

3.7 The Capital Prudential Indicators 2025/26 – 2027/28

3.7.1 The Council’s capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in prudential indicators, which are designed to assist Members’ overview and confirm capital expenditure plans.

3.7.2 The capital prudential indicator is a summary of the Council’s capital expenditure plans, both those agreed previously, and those forming part of this budget cycle. Due to uncertainties over future funding the Capital expenditure it is likely that these indicators will evolve as the budget setting process progresses. The table below summarises the current capital expenditure plans and how these plans are being financed by capital or revenue resources. Any shortfall of resources results in a funding borrowing need.

Table 1: Capital Programme 2024/25 to 2027/28 (based on Round 2 monitoring)

Expenditure	2024/25 £000s	2025/26 £000s	2026/27 £000s	2027/28 onwards £000s	Total £000s
Children and Adults (including Public Health)	19,734	11,537	535	0	31,806
Regeneration, Culture and Environment	64,017	89,084	50,490	14,221	217,811
Housing Revenue Account	22,080	19,127	17,474	8.954	67,636
Business Support Department	386	44	0	0	430
Total Expenditure	**106,217**	**119,792**	**68,499**	**23,175**	**317,683**
Prudential Borrowing	40,908	74,921	41,050	8,954	165,833
Borrowing in lieu of Future Business Rates	4,893	5,695	6,232	0	16,820
Borrowing in lieu of Future Rent	0	3,805	3,805	3,805	11,415
Borrowing in lieu of Capital Receipts	683	1,246	8,716	10,076	20,721
Borrowing in lieu of Future S106	59	0	0	0	59
Borrowing in lieu of Future NHS Grant	7,000	4,764	0	0	11,764
Capital Grants	43,128	19,347	2,038	0	64,513
Developer Contributions	1,461	2,149	1,100	340	5,050
Capital Receipts	822	1,657	0	0	2,479
Right-to-Buy Receipts	0	0	0	0	0
Revenue/ Reserves	7,263	6,208	5,558	0	19,029
Total Funding	**106,217**	**119,792**	**68,499**	**23,175**	**317,683**

4. Borrowing

4.1 The Council's borrowing need (the Capital Financing Requirement)

4.1.1 The second prudential indicator is the Council's Capital Financing Requirement (CFR). The CFR is simply the total historic outstanding capital expenditure which has not been paid for from either revenue or capital resources. It is essentially a measure of the Council's indebtedness and so its underlying borrowing need. Any capital expenditure above, which has not immediately been paid for through a revenue of capital resource, will increase the CFR.

4.1.2 The CFR does not increase indefinitely, as the minimum revenue provision or MRP (a statutory annual revenue charge) broadly reduces the indebtedness in line with each asset's life, and so charges the economic consumption of capital assets as they are used.

4.1.3 The CFR includes any other long-term liabilities (e.g. embedded leases and finance leases). Whilst these increase the CFR, and therefore the Council's borrowing requirement, these types of schemes include a borrowing facility by the lease provider and so the Council is not required to separately borrow for these schemes. The Council had £0.699m, of such liabilities within the CFR at 31 March 2024.

4.1.4 Members are asked to approve the CFR projections:

	2023/24 Actual	2024/25 Estimate £000s	2025/26 Estimate £000s	2026/27 Estimate £000s	2027/28 Estimate £000s
CFR – non housing	456,902	510,469	619,916	667,204	655,938
CFR – housing	42,829	47,363	55,219	56,574	56,193
Total CFR	499,731	557,832	675,135	723,777	712,131
Movement in CFR		58,101	117,303	48,642	(11,646)

4.1.5 Movement in CFR represented by:

	2024/25 Estimate £000s	2025/26 Estimate £000s	2026/27 Estimate £000s	2027/28 Estimate £000s
Prudential Borrowing (Capital Programme)	28,605	89,141	34,251	1,780
Prudential Borrowing (Exceptional financial Support)	26,000	18,500	0	0
Borrowing in lieu of capital receipts	139	1,609	18,537	0
Borrowing in lieu of future business rates	4,632	5,576	6,232	0
Borrowing in lieu of future rents	0	3,805	3,805	3,805
Borrowing in lieu of future S.106 Contributions	53	0	0	0
Borrowing in lieu of future NHS grant	5,247	6,517	0	0
Less MRP/VRP (net of offset) and other financing movements	(5,350)	(6,780)	(7,774)	(8,124)
Less KCC debt repayment	(1,110)	(1,065)	(1,023)	(982)
Less capital receipts repaying borrowing (2-year lag assumed)	0	0	(139)	(1,609)
Less repayment from S106 (2-year lag assumed)	(115)	0	0	0
Less repayment from NHS grant (2-year lag assumed)	0	0	(5,247)	(6,517)
Movement in CFR	58,101	117,303	48,642	(11,646)

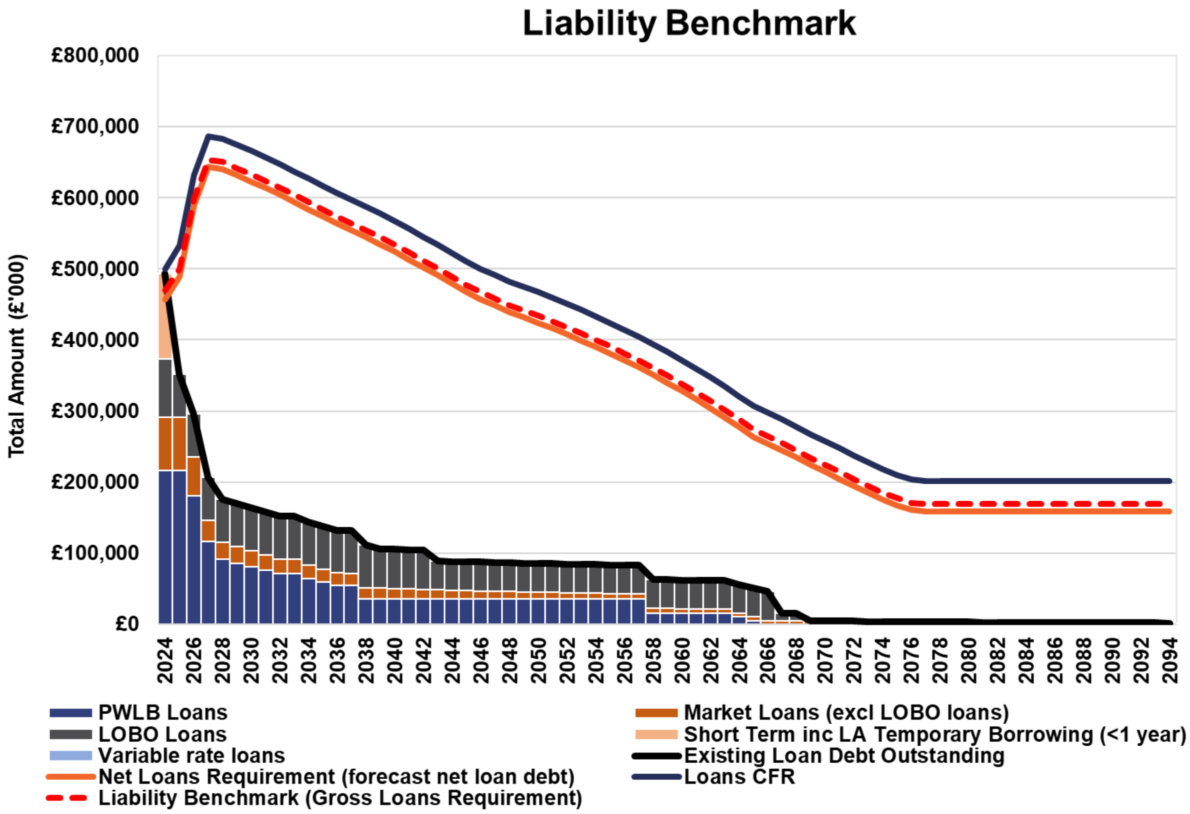
4.1.6 It is envisaged, subject to revisions in the capital programme and the estimated borrowing as a result of Exceptional Financial Support (EFS), that external borrowing will have increased by £58.1m over the course of 2024/25, £117.3m in 2025/26, and £48.6m in 2026/27 but reduce by £11.6m in 2027/28.

4.2 Liability Benchmark

4.2.1 The Authority is required to estimate and measure the Liability Benchmark (LB) for the forthcoming financial year and the following two financial years, as a minimum.

4.2.2 There are four components to the liability benchmark:

- **Existing loan debt outstanding**: the Authority's existing loans that are still outstanding in future years (shaded areas at the bottom of the graph below)
- **Loans CFR**: this is calculated in accordance with loans CFR definition in the Prudential Code and projected into the future based on approved prudential borrowing and planned MRP (dark blue line at the top of the graph)
- Net loans requirement: this will show the Authority's gross loan debt less treasury management investments at the last financial year end, projected into the future based on its approved prudential borrowing, planned MRP and other major cash flows forecast (orange line below the red dotted line)
- **Liability benchmark** (or gross loans requirement): this equals net loans requirement plus short-term liquidity allowance (red dotted line)



The graph shows that under current capital plans the Council will need to take out new loans in future as shown by the gap between the orange line and the shaded areas. The loan requirement is close to the liability benchmark as it is assumed that the Council needs only £10m as a day to day (liquidity) cash balance. At no point does the loan requirement exceed the CFR.

4.3 Borrowing strategy

4.3.1 The capital expenditure plans set out in Table 1 (Paragraph 3.7.2 above) provide details of the service activity of the Council. The treasury management function ensures that the Council's cash is organized in accordance with the relevant professional codes, so that sufficient cash is available to meet this service activity and the Council's capital strategy. This will involve both the organization of the cash flow and, where capital plans require the organization of appropriate borrowing facilities. The strategy covers the relevant treasury/prudential indicators, the current and projected debt positions and the annual investment strategy.

4.3.2 Current portfolio position – The overall treasury management portfolio as at 31 March 2024 and the position as at 15 January 2025 (including November 2024 valuation for Property Funds) is shown below for both borrowing and investment.

TREASURY PORTFOLIO				
	31 Mar 24 Actual £000	31 Mar 24 Actual %	15 Jan 25 Current £000	15 Jan 25 Current %
Treasury Investments				
Banks	10,515	8.43	23,743	13.64
Medway Council Subsidiaries	87,258	69.93	109,861	63.11
Total Managed In House	97,773	78.35	133,604	76.75
Externally Managed – Property Funds (at current value)	22,999	18.43	20,583	11.82
Money Market Funds	4,015	3.22	19,900	11.43
Total Treasury Investments	124,787	100.00	174,088	100.00
Treasury External Borrowing				
Long Term Borrowing	268,974	57.86	363,874	69.39
Short Term Borrowing	114,100	24.54	100,000	19.07
LOBOs	81,800	17.60	60,500	11.54
Total External Borrowing	464,874	100.00	524,374	100.00
Net Borrowing	340,087		350,286	

4.3.3 The Council's forward projections for borrowing are summarized below. The table shows the actual external debt against the underlying capital borrowing need, (the Capital Financing Requirement – CFR), highlighting any over or under borrowing.

	2024/25 Estimate £000s	2024/25 Estimate £000s	2025/26 Estimate £000s	2026/27 Estimate £000s
Debt at 1 April	498,332	556,434	673,736	722,379
Expected Change in Debt	58,101	117,303	48,642	(11,646)
Expected Gross Debt at 31 March	556,434	673,736	722,379	710,733
Capital Financing Requirement 31 March	557,832	675,135	723,777	712,131
Under/ (over) borrowing	1,398	1,399	1,398	1,398

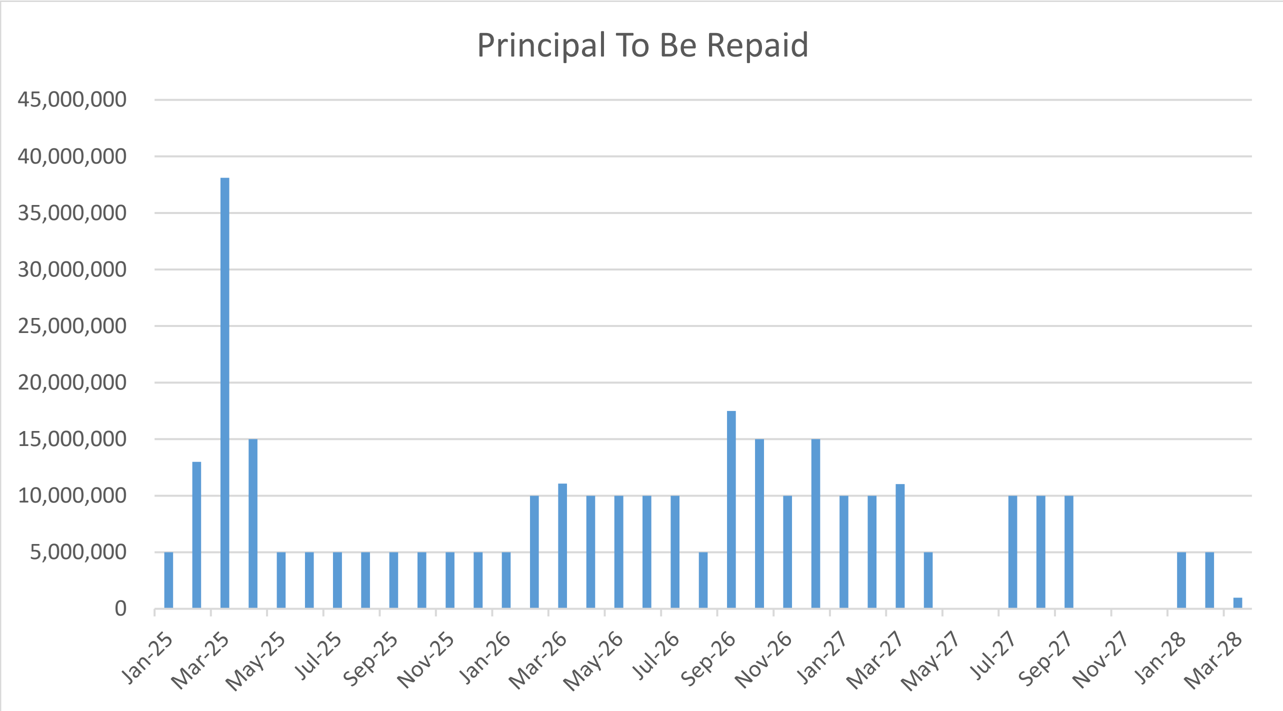
4.3.4 The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as medium and longer dated borrowing rates are expected to fall from their current levels during 2025/26 from 4.5% in April 2025 to 3.75% by March 2026.

Against this background and the risks within the economic forecast, caution will be adopted with the 2025/26 treasury operations. The Chief Operating Officer will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

- *if it was felt that there was a significant risk of a sharp FALL in borrowing rates,* then borrowing would be postponed.
- *if it was felt that there was a significant risk of a much sharper RISE in borrowing rates than that currently forecast,* fixed rate funding would be drawn whilst interest rates are lower than they are projected to be in the next few years.

Any decisions will be reports at the next available opportunity.

4.3.5 The repayment dated for maturity loans is shown below:



4.3.6 The long-term aim of officers is to smooth out the maturity profile and reduce reliance on short-term borrowing but will seek to hold 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.

4.4 New financial institutions as a source of borrowing and / or types of borrowing

4.4.1 As an alternative to PWLB consideration will be given to the following sources:

- Local authorities (primarily shorter dated maturities)
- Financial institutions (primarily insurance companies and pension funds but also some banks, out of spot or forward dates)
- Municipal Bonds Agency (no issuance at present but there is potential)

4.4.2 Before any of these sources is used for long term funding officers will consult with our treasury advisors, MUFG (Link).

4.5 Treasury Indicators: limits to borrowing activities

4.5.1 The CIPFA LAASAC Local Authority Accounting Code Board deferred implementation of IFRS16 until 1 April 2024, the 2024/25 financial year. Where off-balance sheet leased assets have been brought onto the balance sheet in 2024/25, their inclusion will have an impact on the Operational Boundary and Authorised Limit for External Debt for 2025/26. At this point the data isn't yet available to make an estimate on the likely impact. When the data is available changes will be made to these two indicators and reported if significant.

4.6 The Operational Boundary

4.6.1 This is the limit beyond which external debt is not normally expected to exceed. In most cases this would be a similar figure to the CFR but may be lower or higher depending on the levels of actual debt and the ability to fund under-borrowing by other cash resources. (Table below)

Operational Boundary	2024/25 Estimate £000s	2025/26 Estimate £000s	2026/27 Estimate £000s	2027/28 Estimate £000s
Debt	657,832	775,135	823,777	812,131
Other long-term liabilities	2,000	2,000	2,000	2,000
Total	659,832	777,135	825,777	814,131

4.7 The authorised limit for external debt.

4.7.1 This is a key prudential indicator and represents a control on the maximum level of borrowing. It is a legal limit, determined under S3(1) of the Local Government Act 2003, beyond which external borrowing is prohibited, and this limit needs to be set or revised by full Council. The Government retains an option to control either the total of all councils' plans, or those of a specific council, although this power has not yet been exercised.

Authorised Limit	2024/25 Estimate £000s	2025/26 Estimate £000s	2026/27 Estimate £000s	2027/28 Estimate £000s
Debt	723,615	852,649	906,155	893,344
Other long-term liabilities	2,200	2,200	2,200	2,200
Total	725,815	854,849	908,355	895,544

Upper Limit for Fixed Interest Rate Exposure	2024/25 £000s	2025/26 £000s	2026/27 £000s	2027/28 £000s
Net principal fixed rate borrowing	725,815	854,849	908,355	895,544
Net principal fixed rate investment (excluding subsidiaries)	50,000	50,000	50,000	50,000
Net principal fixed rate loans to subsidiaries of Medway Council	125,000	125,000	125,000	125,000

Upper Limit for Variable Rate Exposure	2024/25 £000s	2025/26 £000s	2026/27 £000s	2027/28 £000s
Net principal investment/borrowing (excluding LOBOs) at variable rate	150,000	150000	150,000	150,000
LOBO limit	102,000	102,000	102,000	102,000

Maturity Structure of Fixed rate Borrowing during 2024/25	Upper Limit	Lower Limit
under 12 months	50%	0%
12 months and within 24 months	50%	0%
24 months and within 5 years	50%	0%
5 years and within 10 years	50%	0%
10 years and above	100%	0%

4.7.2 A limit of £125m applies for fixed rate loans to subsidiaries. The interest rate set on such loans will take account of market rates, the security offered, the risk of default, and the requirements to comply with subsidy rules.

4.7.3 Against this background and the risks within the economic forecast, caution will be adopted with the 2025/26 treasury operations. The Chief Operating Officer will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

- *if it was felt that there was a significant risk of a sharp FALL in long and short term rates,* e.g. due to a marked increase of risks around relapse into recession or of risks of deflation, then long term borrowings would be postponed, and potential rescheduling from fixed rate funding into short term borrowing would be considered.
- *if it was felt that there was a significant risk of a much sharper RISE in long and short term rates than that currently forecast,* perhaps arising from an acceleration in the start date and in the rate of increase in central rates in the USA and UK, an increase in world economic activity or a sudden increase in inflation risks, then the portfolio position would be re-appraised with the likely action that fixed rate funding would be drawn whilst interest rates are still lower than they will be in the next few years.

4.8 Policy on borrowing in advance of need

4.8.1 The Council will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. 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 and that the Council can ensure the security of such funds.

4.8.2 Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through the mid-year or annual reporting mechanism.

4.9 Prospects for Interest Rates

4.9.1 The Authority has appointed MUFG (Link) as its treasury advisor and part of their service is to assist the Authority to formulate a view on interest rates. MUFG (Link) provided the following forecasts on 11 November 2024. These are forecasts for Bank Rate, average earnings and PWLB certainty rates (gilt yields plus 80 bps).

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

4.9.2

Additional notes by MUFG (Link) on this forecast table: -

- Our central forecast for interest rates was previously updated on 25 September and reflected a view that the MPC would be keen to further demonstrate its anti-inflation credentials by keeping Bank Rate at 5.25% until at least H2 2024. We expect rate cuts to start when both the CPI inflation and wage/employment data are supportive of such a move, and that there is a likelihood of the overall economy enduring at least a mild recession over the coming months, although most recent GDP releases have surprised with their on-going robustness.
- Naturally, timing on this matter will remain one of fine judgment: cut too soon, and inflationary pressures may well build up further; cut too late and any downturn or recession may be prolonged.
- In the upcoming months, our forecasts will be guided not only by economic data releases and clarifications from the MPC over its monetary policies and the Government over its fiscal policies, but also international factors such as policy development in the US and Europe, the provision of fresh support packages to support the faltering recovery in China as well as the on-going conflict between Russia and Ukraine, and Gaza and Israel.
- On the positive side, consumers are still anticipated to be sitting on some excess savings left over from the pandemic, which could cushion some of the impact of the above challenges and may be the reason why the economy is performing somewhat better at this stage of the economic cycle than may have been expected. However, as noted previously, most of those excess savings are held by more affluent households whereas lower income families already spend nearly all their income on essentials such as food, energy and rent/mortgage payments.

PWLB RATES

- Gilt yield curve movements have broadened since our last Newsflash. The short part of the curve has not moved far but the longer-end continues to reflect inflation concerns. At the time of writing there is 60 basis points difference between the 5- and 50-year parts of the curve.

4.9.3

The balance of risks to the UK economy: -

- The overall balance of risks to economic growth in the UK is to the downside.

4.9.4 **Downside Risks to current forecasts for UK gilt yields and PWLB rates include**:

- **Labour and supply shortages** prove more enduring and disruptive and depress economic activity (accepting that in the near-term this is also an upside risk to inflation and, thus, could keep gilt yields high for longer).

- **The Bank of England** acts too quickly, or too far, over the next two years to raise Bank Rate and causes UK economic growth, and increases in inflation, to be weaker than we currently anticipate.

- **UK / EU trade arrangements** – if there was a major impact on trade flows and financial services due to complications or lack of co-operation in sorting out significant remaining issues.
- **Geopolitical risks,** for example in Ukraine/Russia, China/Taiwan/US, Iran, North Korea and Middle Eastern countries, which could lead to increasing safe-haven flows.

4.9.5 Upside risks to current forecasts for UK gilt yields and PWLB rates include:

- Despite the recent tightening to 5.25%, the **Bank of England proves too timid** in its pace and strength of increases in Bank Rate and, therefore, allows inflationary pressures to remain elevated for a longer period within the UK economy, which then necessitates Bank Rate staying higher for longer than we currently project.

- **The pound weakens** because of a lack of confidence in the UK Government's pre-election fiscal policies, resulting in investors pricing in a risk premium for holding UK sovereign debt.

- Longer-term **US treasury yields** rise strongly if inflation remains more stubborn there than the market currently anticipates, consequently pulling gilt yields up higher.

- Projected **gilt issuance, inclusive of natural maturities and QT,** could be too much for the markets to comfortably digest without higher yields compensating.

4.10 Investment and borrowing rates

4.10.1 MUFG's (Link) long-term (beyond 10 years) forecast for Bank Rate has increased from 2.75% to 3% and reflects Capital Economics' research that suggests AI and general improvements in productivity will be supportive of a higher neutral interest rate. As all PWLB certainty rates are currently significantly above this level, borrowing strategies will need to be reviewed in that context. Overall, better value can generally be obtained at the shorter end of the curve and short-dated fixed LA to LA monies should be considered. Temporary borrowing rates will remain elevated for some time to come but may prove the best option whilst the market continues to wait for inflation, and therein gilt yields, to drop back later in 2024.

4.10.2 Suggested budgeted earnings rates for investments up to about three months' duration in each financial year are rounded to the nearest 10bps and set out below. You will note that investment earnings have been revised somewhat higher for all years from 2025/26 as Bank Rate remains higher for longer.

Average earnings in each year	Now	Previously
2023/24 (residual)	5.30%	5.30%
2024/25	4.70%	4.70%
2025/26	3.20%	3.00%
2026/27	2.25%	3.05%
2027/28	3.25%	3.05%
Years 6 to 10	3.25%	3.05%
Years 10+	3.25%	3.05%

4.10.3 As there are so many variables at this time, caution must be exercised in respect of all interest rate forecasts.

4.10.4 MUFG's (Link) interest rate forecast for Bank Rate is in steps of 25 bps, whereas PWLB forecasts have been rounded to the nearest 10 bps and are central forecasts within bands of + / - 25 bps. Naturally, they continue to monitor events and will update our forecasts as and when appropriate.

4.10.5 While this authority will not be able to avoid borrowing to finance new capital expenditure, to replace maturing debt, there will be a cost of carry, (the difference between higher borrowing costs and lower investment returns), to any new borrowing that causes a temporary increase in cash balances as this position will, most likely, incur a revenue cost.

4.11 Debt Rescheduling

4.11.1 Rescheduling of current borrowing in our debt portfolio is unlikely to occur as PWLB rates for premature repayments are unattractive.

4.11.2 Decisions related to rescheduling will be reported in reviews of this strategy.

5. Investment

5.1 Annual Investment Strategy

5.1.1 Investment policy – management of risk

5.1.2 The Department of Levelling Up, Housing and Communities (DLUHC - this was formerly the Ministry of Housing, Communities and Local Government (MHCLG)) and CIPFA have extended the meaning of 'investments' to include both financial and non-financial investments. This report deals solely with treasury (financial) investments, (as managed by the treasury management team). Non-financial investments, essentially the purchase of income yielding assets and service investments, are covered in the Capital Strategy, (a separate report).

5.1.3 The Council's investment policy has regard to the following: -

- DLUHS's Guidance on Local Government Investments ("the Guidance")
- CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2021 ("the Code")
- CIPFA Treasury Management Guidance Notes 2021

5.1.4 The Authority's investment priorities will be security first, portfolio liquidity second and then yield (return). The Authority will aim to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity and with regard to the Authority's risk appetite.

5.1.5 Minimum acceptable credit criteria are applied in order to generate a list of highly creditworthy counterparties. This also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the short term and long-term ratings.

5.1.6 Other information: ratings will not be the sole determinant of the quality of an institution; it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To achieve this consideration the Council will engage with its advisors to maintain a monitor on market pricing such as "credit default swaps" and overlay that information on top of the credit ratings.

5.1.7 Other information sources used will include the financial press, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.

5.1.8 This authority has defined the list of types of investment instruments that the treasury management team are authorised to use. There are two lists in appendix 4 under the categories of ‘specified’ and ‘non-specified’ investments.

5.1.9 Specified investments are those with a high level of credit quality and subject to a maturity limit of one year.

5.1.10 Non- specified investments are those with less high credit quality, may be for periods in excess of one year, and/or are more complex instruments which require greater consideration by members and officers before being authorised for use. Once an investment is classed as non-specified, it remains non-specified all the way through to maturity i.e. an 18-month deposit would still be non-specified even if it has only 11 months left until maturity.

5.1.11 Lending limits, (amounts and maturity), for each counterparty will be set through applying Treasury Management Practice 1.

5.1.12 Transaction limits are set for each type of investment in appendix 4.

5.1.13 This authority will set a limit for the amount of its investments which are invested for longer than 365 days, (see appendix 4).

5.1.14 Investments will only be placed with counterparties from countries with a specified minimum sovereign rating, (see appendix 5).

5.1.15 This authority has engaged external consultants, (see paragraph 3.6), to provide expert advice on how to optimise an appropriate balance of security, liquidity, and yield, given the risk appetite of this authority in the context of the expected level of cash balances and need for liquidity throughout the year.

5.1.16 All investments will be denominated in sterling.

5.1.17 As a result of the change in accounting standards in 2023/24 under IFRS 9, this authority will consider the implications of investment instruments which could result in an adverse movement in the value of the amount invested and resultant charges at the end of the year to the General Fund. (In November 2018, the Ministry of Housing, Communities and Local Government, [MHCLG], concluded a consultation for a temporary override to allow English local authorities time to adjust their portfolio of all pooled investments by announcing a statutory override to delay implementation of IFRS 9 for five years ending 31 March 2023.) More recently, a further extension to the over-ride to 31 March 2025 has been agreed by Government.

5.1.18 However, this authority will also pursue value for money in treasury management and will monitor the yield from investment income against appropriate benchmarks for investment performance. Regular monitoring of investment performance will be carried out during the year.

5.2 Creditworthiness policy

5.2.1 This Council applies the creditworthiness service provided by MUFG (Link). This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies – Fitch, Moody’s and Standard & Poor’s. The credit ratings of counterparties are supplemented with the following overlays:

5.2.2 credit watches and credit outlooks from credit rating agencies;

5.2.3 CDS spreads to give early warning of likely changes in credit ratings;

5.2.4 Sovereign ratings to select counterparties from only the most creditworthy countries.

5.2.5 This modelling approach combines credit ratings, credit watches and credit outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads for which the end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Council to determine the duration for investments. The Council will therefore use counterparties within the following durational bands:

- Yellow 5 years *
- Dark pink 5 years for Ultra-Short Dated Bond Funds with a credit score of 1.25
- Light pink 5 years for Ultra-Short Dated Bond Funds with a credit score of 1.5
- Purple 2 years
- Blue 1 year (only applies to nationalised or semi nationalised UK Banks)
- Orange 1 year
- Red 6 months
- Green 100 days
- No colour not to be used

5.2.6 The MUFG (Link) creditworthiness service uses a wider array of information than just primary. Furthermore, by using a risk weighted scoring system, it does not give undue preponderance to just one agency's ratings.

5.2.7 Typically, the minimum credit ratings criteria the Council use will be a short-term rating (Fitch or equivalents) of F1, a Long-Term rating A-. There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances, consideration will be given to the whole range of ratings available, or other topical market information, to support their use.

5.2.8 All credit ratings will be monitored, primarily via MUFG (Link) updates, by Officers on a continuous basis. The Council is alerted to changes to ratings of all three agencies through its use of the MUFG (Link) creditworthiness service.

5.2.9 If a downgrade results in the counterparty / investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.

5.2.10 In addition to the use of credit ratings the Council will be advised of information in movements in Credit Default Swap against the iTraxx benchmark and other market data on a weekly basis via its Passport website, provided exclusively to it by MUFG (Link). Extreme market movements may result in downgrade of an institution or removal from the Council's lending list.

5.2.11 Sole reliance will not be placed on the use of this external service. In addition, the Council will also use market data and market information, information on any external support for banks to help support its decision-making process.

5.3 Counterparty Limits

5.3.1 The current counterparty limits are set as;

- In-house team £20 million limit per counterparty and £25 million for counterparties with a MUFG (Link) Asset Services duration rating of 12 months or above.

5.3.2 No amendments are requested to these counterparty limits.

5.4 Country limits

5.4.1 The Council has determined that it will only use approved counterparties from countries with a minimum sovereign credit rating of AA- from Fitch (or equivalent). The list of countries that qualify using this credit criteria as at the date of this report are shown in Appendix 5. This list will be added to or deducted from by officers should ratings change in accordance with this policy.

5.4.2 In addition:

- no more than £40m will be placed with any non-UK country at any time;
- limits in place will apply to a group of companies;
- sector limits will be monitored regularly for appropriateness.

5.5 Investment Strategy

5.5.1 In-house funds. Investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (i.e. rates for investments up to 12 months).

5.5.2 Officers will aim to minimise net cash balances by appropriate uses of short-term borrowing such that as cash balances surplus to immediate needs arise they are quickly matched by the opportunity to repay maturing debt.

5.6 Investment in Property Funds

5.6.1 Property Funds are a form of investment, comprising a portfolio of commercial properties to achieve investment returns through rental income and capital growth. However, the value of such investments may fall as well as rise. There may also be restrictions on redemption of the investment. This type of investment is regarded as a 5-to-7-year minimum timeframe.

5.6.2 Due diligence was undertaken before the Council invested in Property Fund and the CFO would carefully consider the Council's cash balances and cashflow projections before investing further amounts.

5.7 Loans to Social Enterprises and Similar Organisations

5.7.1 Medway will consider advancing funds to organisations where the purpose of such loans advances Council priorities.

5.7.2 The Council may also make loans or rolling credit facilities to its subsidiary companies.

5.8 Investment in Money Market Funds

5.8.1 Money Market Funds (MMFs) often offer enhanced returns compared with bank call accounts while reducing bail- in risk through diversification. Investment has been made in a MMF operated by CCLA and officers with consider making similar investments in other MMFs.

5.8.2 Investment treasury indicator and limit – total principal funds invested for greater than 365 days. These limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment and are based on the availability of funds after each year-end.

Upper limit for principal sums invested for longer than 365 days			
	2024/25 £m	2025/26 £m	2026/27 £m
Principal sums invested for longer than 365 days	150	150	150
Current Investments as at 30.11.21 in excess of 1 year maturing each year	0	0	0

5.9 End of year investment report

5.9.1 At the end of the financial year, the Council will report on its investment activity as part of its Annual Treasury Report.

6. Kent County Council (KCC) Local Government Reorganisation (LGR) Debt

6.1 The charge for the share of KCC debt for which Medway Council was responsible on local government reorganisation is based on the current average cost of debt for the County Council as a whole. The County estimated the rate at 4.409% for 2024/25 however the final payment each year is adjusted to reflect actual interest. Early redemption may incur a penalty. The outstanding principal at 1 April 2025 will be £26.635million.

7. Minimum Revenue Provision (MRP)

7.1 The Minimum Revenue Provision is explained and the Policy Statement for 2025/26 is set out at Appendix 1.

Appendix 1 – Minimum Revenue Provision Policy Statement 2025/26

Under Regulation 27 of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, where the Authority has financed capital expenditure by borrowing it is required to make a provision each year through a revenue charge (MRP).

The Authority is required to calculate a prudent provision of MRP which ensures that the outstanding debt liability is repaid over a period that is reasonably commensurate with that over which the capital expenditure provides benefits. The MRP Guidance (2024) gives four ready-made options for calculating MRP, but the Authority can use any other reasonable basis that it can justify as prudent.

The MRP policy statement requires full council approval in advance of each financial year.

The Authority is recommended to approve the following MRP Statement:

MRP is calculated on an annuity basis over the estimated lives of assets funded from debt. The period over which provision is made for all expenditure after 1 April 2018 is subject to an upper limit of 50 years in line with the latest DLUHC guidance. MRP on expenditure prior to 1 April 2018 is provided over the remaining life previously estimated.

The Council will treat all expenditures as not ranking for MRP until the year after the scheme or asset to which they relate is completed and/or brought into use.

Estimated life periods will be determined under delegated powers.

As some types of capital expenditure incurred by the Council are not capable of being related to an individual asset, asset lives will be assessed on a basis which most reasonably reflects the anticipated period of benefit that arises from the expenditure. Also, whatever type of expenditure is involved, it will be grouped together in a manner which reflects the nature of the main component of expenditure and will only be divided up in cases where there are two or more major components with substantially different useful economic lives.

In the case of long-term debtors arising from loans to subsidiaries, the MRP guidance requires the Council to determine whether loans are either performing (commercial) or non-performing (non-commercial) in nature. The Government definition of a commercial loan is: "defined in regulation 27(5) as a loan from the authority to another entity for a purpose which, if the authority were to undertake itself, would be primarily for financial return; or, where the loan is itself capital expenditure undertaken primarily for financial return." The Council has determined that the loans are not primarily for financial return and therefor Non-Performing and therefore under the MRP guidance, the Council is not required to set aside MRP for loans of this type.

Other types of capital expenditure made by the Council which will be repaid under separate arrangements (such as long-term investments), or where borrowing has occurred but will be repaid by future Capital Receipts or agreed income from other source, there will be no Minimum Revenue Provision made.

There is no requirement on the HRA to make a minimum revenue provision, though in the interests of prudence the council has opted to do so.

Appendix 2 – Interest Rate Forecasts 2024-27

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

Appendix 3 – Prudential and Treasury Indicators

PRUDENTIAL INDICATORS	2024/2025	2025/2026	2026/2027	2027/2028
	Estimate	Estimate	Estimate	Estimate
	£'000	£'000	£'000	£'000
Capital Expenditure				
Non - HRA	84,137	100,665	51,025	14,221
HRA	22,080	19,127	17,474	9
TOTAL	106,217	119,792	68,499	14,230
Ratio of financing costs to net revenue stream				
Non - HRA	4.51%	5.00%	4.81%	4.25%
HRA	11.65%	11.59%	11.59%	11.59%
Gross borrowing requirement				
brought forward 1 April	498,332	556,434	673,736	722,379
carried forward 31 March	556,434	673,736	722,379	710,733
in year borrowing requirement	58,101	117,303	48,642	(11,646)
Capital Financing Requirement as at 31 March				
Non – HRA	510,469	619,916	667,204	655,938
HRA	47,363	55,219	56,574	56,193
TOTAL	557,832	675,135	723,777	712,131
Annual change in Cap. Financing Requirement				
Non- HRA	53,567	109,447	47,288	(11,266)
HRA	4,534	7,856	1,354	(381)
TOTAL	58,101	117,303	48,642	(11,646)

TREASURY MANAGEMENT INDICATORS	2024/2025	2025/2026	2026/2027	2027/2028
	Estimate	Estimate	Estimate	Estimate
	£'000	£'000	£'000	£'000
Authorised Limit for external debt -				
Borrowing	723,615	852,649	906,155	893,344
Other Long-term liabilities	2,200	2,200	2,200	2,200
TOTAL	725,815	854,849	908,355	895,544
Operational Boundary for external debt -				
Borrowing	657,832	775,135	823,777	812,131
Other long-term liabilities	2,000	2,000	2,000	2,000
TOTAL	659,832	777,135	825,777	814,131
Estimated actual external debt (31 March)	556,434	673,736	722,379	710,733
Upper limit for fixed interest rate exposure				
Net principal re fixed rate borrowing	725,815	854,849	908,355	895,544
Net principal fixed rate investment (exc. Subsidiaries)	50,000	50,000	50,000	50,000
Net principal fixed rate loans to subsidiaries of Medway Council	125,000	125,000	125,000	125,000
Upper limit for variable rate exposure				
Net principal re variable rate borrowing / investments (excluding LOBOs) LOBO Limit	150,000	150,000	150,000	150,000
Upper limit for total principal sums invested for over 1 year				
(per maturity date)	150,000	150,000	150,000	150,000

TABLE 5: Maturity structure of fixed rate borrowing during 2025/2026	**upper limit**		**lower limit**
under 12 months	50%		0%
12 months and within 24 months	50%		0%
24 months and within 5 years	50%		0%
5 years and within 10 years	50%		0%
10 years and above	100%		0%

Appendix 4 – Specified and Non-specified Investments

SPECIFIED INVESTMENTS: (All such investments will be sterling denominated, with **maturities up to maximum of 1 year**, meeting the minimum 'high' rating criteria where applicable)

	*** Minimum 'High' Credit Criteria**	**Use**
Debt Management Agency Deposit Facility	--	In-house and Fund Manager
Term deposits – local authorities	--	In-house and Fund Manager
Term deposits – banks and building societies	See note 1	In-house and Fund Manager
Collateralised deposit (see note 3)	UK sovereign rating	In-house and Fund Manager
Certificates of deposit issued by banks and building societies	See note 1	In-house and Fund Manager
UK Government Gilts	UK sovereign rating	In-house buy and hold and Fund Manager
Bonds issued by multilateral development banks	AAA	In-house buy and hold and Fund Manager
Bond issuance issued by a financial institution which is explicitly guaranteed by the UK Government (refers solely to GEFCO - Guaranteed Export Finance Corporation)	UK sovereign rating	In-house buy and hold and Fund Manager
Sovereign bond issues (other than the UK govt)	AAA	In-house buy and hold and Fund Manager
Treasury Bills	UK sovereign rating	In house and Fund Manager
Government Liquidity Funds	* Long-term AAA volatility rating V1+	In-house and Fund Managers
Money Market Funds CNAV, LVNAV or VNAV	* Long-term AAA volatility rating V1+	In-house and Fund Managers

Note 1. Award of "Creditworthiness" Colour by MUFG (Link) as detailed in paragraph 1.55.2.

Accounting treatment of investments. The accounting treatment may differ from the underlying cash transactions arising from investment decisions made by this Council. To ensure that the Council is protected from any adverse revenue impact, which may arise from these differences, we will review the accounting implications of new transactions before they are undertaken.

NON-SPECIFIED INVESTMENTS: These are any investments which do not meet the Specified Investment criteria. A maximum of 70% ** will be held in aggregate in non-specified investment

1. Maturities of ANY period

	*** Minimum Credit Criteria**	**Use**	**** Max total investments**	**Max. maturity period**
Fixed term deposits with variable rate and variable maturities: - Structured deposits	See note 1	In-house	£10m	Lower of 5 years or MUFG duration rating
Property Funds	See note 2 and 3	In-house	£25m (original cost of investment)	N/A

2. Maturities in excess of 1 year

	*** Minimum Credit Criteria**	**Use**	**** Max total investments**	**Max. maturity period**
Term deposits – local authorities	--	In-house	£25m	5 Years
Term deposits – banks and building societies	See note 1	In-house	£25m	As per MUFG duration rating
Certificates of deposit issued by banks and building societies covered by UK Government (explicit) guarantee	See note 1 and 2	In-house	£25m	As per MUFG duration rating and see note 3
Certificates of deposit issued by banks and building societies	See note 1 and 2	In-house	£25m	As per MUFG duration rating and see note 3
UK Government Gilts	UK sovereign rating	In-house	£25m	see note 1
Bonds issued by multilateral development banks	AAA	In-house	£10m	see note 1
Sovereign bond issues (other than the UK govt)	AAA	In-house	£10m	see note 1
Social Enterprises	See note 4	In House	£5m	25 years

Note 1. Award of "Creditworthiness" Colour by MUFG (Link) Treasury services as detailed in paragraph 1.55.2

Note 2. Property Funds are not credit rated.

Note 3. Property Funds: up to an aggregate of £25m may be invested in collective property Funds (based on original cost of investment)

Note 4. Social Enterprises may not be credit rated

** If forward deposits are to be made, the forward period plus the deal period should not exceed one year in aggregate.

N.B. buy and hold may also include sale at a financial year end and repurchase the following day in order to accommodate the requirements of SORP.

Appendix 5 – Approved countries for investments

Based on lowest available rating (as at 25.11.24)

AAA

- Australia
- Denmark
- Germany
- Netherlands
- Norway
- Singapore
- Sweden
- Switzerland

AA+

- Canada
- Finland
- U.S.A.

AA

- Abu Dhabi (UAE)
- Qatar

AA-

- Belgium
- France
- **U.K.**

Appendix 6 – Amendments to the Treasury Management Practices

The following principal changes have been made to the TMPs compared with those published in January 2024:

Treasury Management Practice 1: Treasury Risk Management paragraphs

- 1.61 list of Guidance and Codes of Practice updated

Treasury Management Practice 10: Training and qualifications

- 10.9 list of staff and qualifications updated