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| **Report to:** | Audit and Governance Committee | **Date of Meeting:** | Wednesday 20 March 2024 |
| **Subject:** | Treasury Management Position to January 2024 | | |
| **Report of:** | Executive Director of Corporate Resources and Customer Services | **Wards Affected:** | All Wards |
| **Portfolio:** | Cabinet Member - Regulatory, Compliance and Corporate Services | | |
| **Is this a Key Decision:** | No | **Included in Forward Plan:** | No |
| **Exempt / Confidential Report:** | No | | |

**Summary:**

This report provides Members with a review of the Treasury Management activities undertaken to 31st January 2024. This document is the third report of the ongoing quarterly monitoring provided to Audit & Governance Committee whose role it is to carry out scrutiny of treasury management policies and practices.

**Recommendation(s):**

Members are requested to note the Treasury Management update to 31st January 2024, to review the effects of decisions taken in pursuit of the Treasury Management Strategy and to consider the implications of changes resulting from regulatory, economic and market factors affecting the Council's treasury management activities.

**Reasons for the Recommendation(s):**

To ensure that Members are fully appraised of the treasury activity undertaken to 31st January 2024 and to meet the reporting requirements set out in Sefton's Treasury Management Practices and those recommended by the CIPFA code.

**Alternative Options Considered and Rejected:** (including any Risk Implications)

N/A

**What will it cost and how will it be financed?**

**(A) Revenue Costs**

The financial position on the external investment budget to the end of January indicates a surplus to the end of the period. The forecast to the end of the financial year also shows that investment income will exceed the level set in the budget.

### (B) Capital Costs

None.

### Implications of the Proposals:

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| **Resource Implications (Financial, IT, Staffing and Assets):**<br>A surplus in investment income has been forecast for 2023/24 financial year due to prevailing market conditions. |
| **Legal Implications:**<br>The Council has a statutory duty under the Local Government Act 2003 to review its Prudential Indicators and Treasury Management Activities. |
| **Equality Implications:**<br>There are no equality implications. |
| **Impact on Children and Young People:** No |
| **Climate Emergency Implications:** |

The recommendations within this report will

| | |
|---|---|
| Have a positive impact | N |
| Have a neutral impact | Y |
| Have a negative impact | N |
| The Author has undertaken the Climate Emergency training for report authors | N |

The Council has during 2023/24, invested its reserves and balances overnight with either banks or money market funds in order to maintain high security and liquidity of such balances. It has not had the opportunity to invest in longer term financial instruments or investment funds for which there may be a chance to consider the impact on the Council's Climate Emergency motion.

In the event that the Council has more surplus balances available in future that may lead to longer term investing, the Council will take account of the climate emergency when discussing the options available with the Treasury Management Advisors.

### Contribution to the Council's Core Purpose:

| |
|---|
| Protect the most vulnerable: n/a |
| Facilitate confident and resilient communities: n/a |
| Commission, broker and provide core services: n/a |
| Place – leadership and influencer: Support strategic planning and promote innovative, affordable and sustainable capital investment projects through application of the CIPFA Prudential Code. |

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|---|
| Drivers of change and reform: The Treasury Management function ensures that cash flow is adequately planned, and cash is available when needed by the Council for improvements to the borough through its service provision and the Capital Programme. |
| Facilitate sustainable economic prosperity: Pursuit of optimum performance on investments activities and minimising the cost of borrowing and the effective management of the associated risk continues to contribute to a balanced budget for the Council. |
| Greater income for social investment: n/a |
| Cleaner Greener: n/a |

**What consultations have taken place on the proposals and when?**

**(A) Internal Consultations**

The Executive Director of Corporate Resources and Customer Services (FD5700/24) is the author of the report.
The Chief Legal and Democratic Officer (LD7600/24) have been consulted and any comments have been incorporated into the report.

**(B) External Consultations**

N/A

**Implementation Date for the Decision**

With immediate effect.

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**Appendices:**

There are no appendices to this report

**Background Papers:**

There are no background papers available for inspection.

## 1. Background to the Report

1.1. As recommended under CIPFA's revised 2021 Code of Practice on Treasury Management in Public Services, the Council's Treasury Management Policy and Strategy document for 2023/24 (approved by Council on 2nd March 2023) included a requirement for regular updates to be provided on the investment activity of the Authority. This report is the third of such reports for the year and presents relevant Treasury Management information for the period ending 31st January 2024.

1.2. The report includes information on the investments held / entered into during the period and the interest rates obtained (with a comparison of performance against a standard benchmark figure). In addition, the report highlights whether there has been any variance from the Treasury Management Policy and Strategy and the Council's approved Prudential Indicators (the operational boundaries within which the Council aims to work).

## 2. Investments Held

2.1. Investments held at the 31/01/2024 comprise the following:

| Institution | Deposit £m | Rate % | Maturity | Rating |
|---|---|---|---|---|
| **Money Market Funds:** | | | | |
| Aberdeen | 4.34 | 5.22 | 01.02.24 | AAA |
| Aviva | 4.34 | 5.32 | 01.02.24 | AAA |
| Blackrock | 4.34 | 5.24 | 01.02.24 | AAA |
| BNP Paribas | 4.34 | 5.31 | 01.02.24 | AAA |
| Goldman-Sachs | 3.20 | 5.21 | 01.02.24 | AAA |
| HSBC | 0.49 | 5.20 | 01.02.24 | AAA |
| Invesco | 4.34 | 5.31 | 01.02.24 | AAA |
| Morgan Stanley | 4.34 | 5.27 | 01.02.24 | AAA |
| Federated | 4.34 | 5.34 | 01.02.24 | AAA |
| Insight | 4.34 | 5.29 | 01.02.24 | AAA |
| Total | 38.41 | | | |
| **Property Fund:** | | | | |
| CCLA | 5.00 | 4.94 | n/a | n/a |
| Total | 5.00 | | | |
| **TOTAL INVESTMENTS** | **43.41** | | | |

2.2. The Authority holds significant invested funds, representing grant income received in advance of expenditure plus balances and reserves held. The cash is initially held in a number of highly liquid Money Market Funds to ensure security of the funds until they are required to be paid out. This approach is consistent with the Council's approved Treasury Management Policy and Strategy for 2023/24. The balance of investments is therefore expected to fall over the coming months as the income is fully expended.

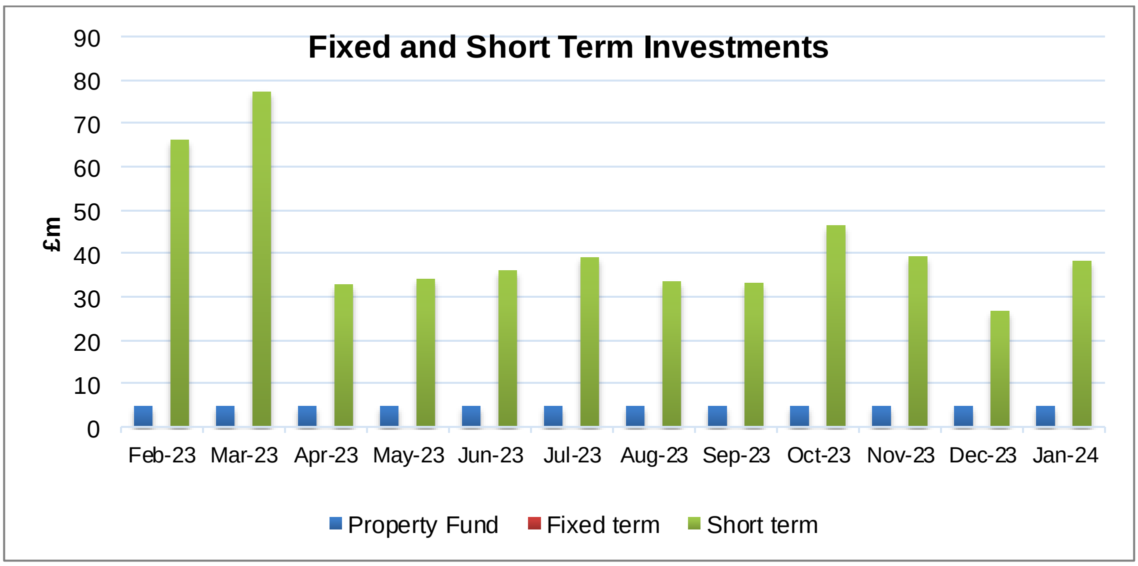
2.3. All of the investments made since April 2023 have been with organisations on the current counterparty list. The maximum level of investment permitted in the Treasury Management Strategy in any one institution, or banking group, is currently £15m. Whilst the maximum should be retained, in light of current economic conditions, a day-to-day operational maximum of 10% of the total portfolio is currently being imposed for investments. This will spread the risk for the Council but will have a small detrimental impact on the returns the Council will receive in the future. The Council has remained within that boundary during the year. At present, it is not expected that there will be any need to review this limit.

2.4. The Council will only invest in institutions that hold a minimum Fitch rating of A- for banking institutions, or AAA for money market funds. The ratings applied to investment grade institutions, and the much riskier speculative grade institutions, as defined by Fitch, have been placed into a risk matrix (paragraph 2.8).

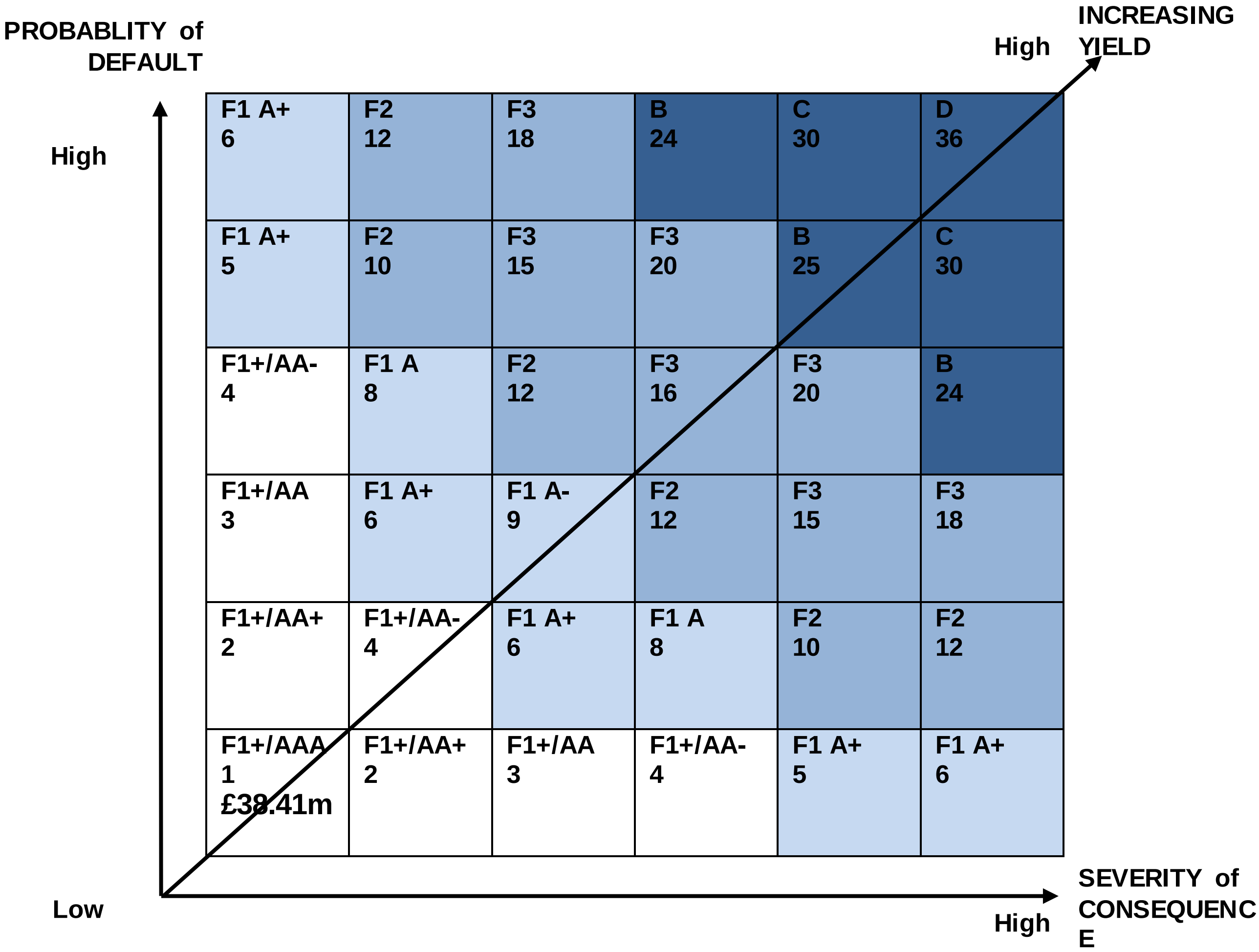
2.5. An investment has been made with the Church, Charities and Local Authority Investment Fund (CCLA) in June 2014. CCLA invest in commercial property which is rented out to enterprises such as retail units, warehousing, and offices. The majority of properties owned are in the south of the country where the market is often more buoyant than the north. The Council has in effect bought a share of the property portfolio and returns paid are in the region of 4%. This is seen as a long-term investment with the potential for the capital value of the investment to vary as property prices fluctuate.

2.6. The Net Asset Value (NAV) of the Property Fund has decreased over a 12-month period to January 2024 from 289.43p per unit to 277.86p per unit, a decrease of 4%. The fund is considered to be a long-term investment and fluctuations in value are to be expected with this type of asset. The situation will continue to be monitored closely however, and advice taken from the Council's treasury advisers should its position in the fund need to be reviewed. The income yield on the Property fund at the end of January 2024 was 4.94% which is above the level of returns received in the past.

2.7. The ratio of overnight deposits (short term) to fixed term investments and the property fund is shown below:



2.8. The matrix below shows how the Council has set its risk appetite by being risk averse and putting security and liquidity before yield when investing:




**SEFTON RISK TOLERANCE:**

| Risk Level | Score | Grade | Amount Invested |
|---|---|---|---|
| LOW | 1 - 4 | Investment Grade | £38.41m |
| LOW - MEDIUM | 5 - 9 | Investment Grade | £0 |
| MEDIUM | 10 - 20 | Investment Grade | £0 |
| HIGH | 21 - 36 | Speculative Grade | £0 |

2.9. The Council will continue to maximise any investment opportunities as they arise but given that the Council's cash balances are typically lower towards the end of the financial year is not envisaged that any substantial increase in returns can be achieved during the final quarter. Cash balances available for investment will be held in overnight deposits to allow the council to respond to any exceptional demands for cash as they arise. The possibility for making long term deposits at potentially improved rates will be reviewed in the first quarter of 2024/25 as new grant allocations begin to be paid to the Council and cash increases.

## 3. Interest Earned

3.1. The actual performance of investments against the profiled budget to the end of January 2024 and the forecast performance of investments against total budget at year end is shown below:

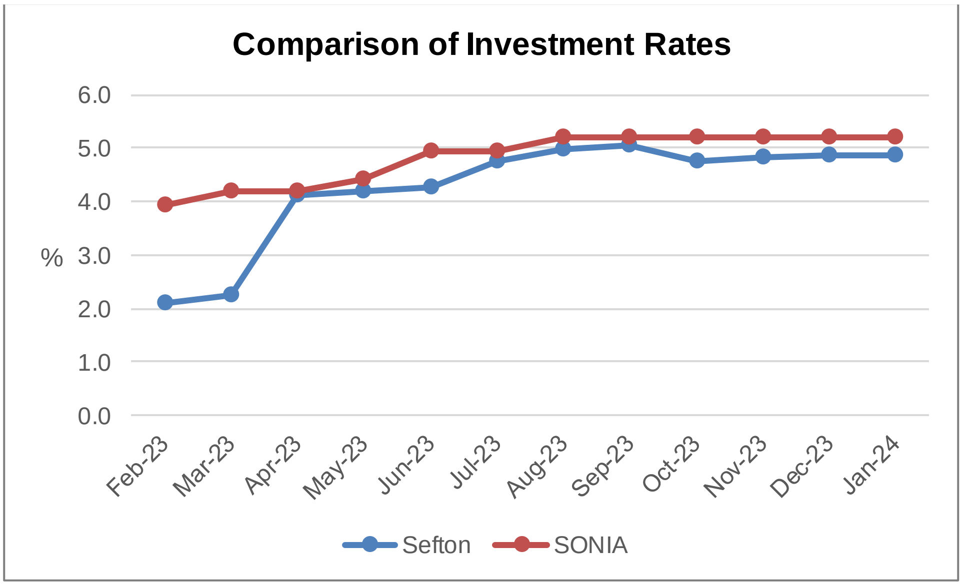
| | Budget £m | Actual £m | Variance £m |
|---|---|---|---|
| **January-24** | 1.079 | 1.957 | 0.879 |

| | Budget £m | Forecast £m | Variance £m |
|---|---|---|---|
| **Outturn 2023/24** | 1.317 | 2.217 | 0.900 |

3.2. The forecast outturn for investment income shows the level of income to be above target against the budget for 2023/24. Investment rates have increased in the past 12 months (see 3.4. below) largely in response to rises in interest rates. The forecast income for 2023/24 has therefore been set at a higher level when compared to previous financial years.

3.3. As mentioned in paragraph 2.9, it is not envisaged that increased rates will lead to a significant improvement in the forecast income from investments for the remainder of 2023/24 as cash balances are diminishing and held in short term deposits. A prudent approach has therefore been taken when forecasting returns for the rest of the year.

3.4. The Council has achieved an average rate of return on its investments of 4.89%. The chart below shows the average rate of return plotted against the SONIA benchmark.



3.5. As can be seen from the chart above, Sefton's investments have slightly underperformed (by 0.3%) compared to SONIA to the end of January 2024, although the investment income received is above target as per the 2023/24 budget as shown in paragraph 3.1 (above).

## 4. Borrowing Strategy

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

4.2. There has been a substantial rise in the cost of taking out new loans, both short- and long-term, over the last 18 months. The Bank Rate rose by 1% from 4.25% at the beginning of April to 5.25% at the end of September 2023. The Bank Rate was 2% higher than at the end of September 2022.

4.3. The Council has PWLB loan maturities of £11.9m scheduled during 2023/24 comprising several historic loans. The Council pursues a strategy of internal borrowing as per the Treasury Management Strategy approved by Council. Cash balances have therefore been reduced to replace maturing loans where possible and when interest rates on deposits remain lower than PWLB borrowing rates.

4.4. The Council may opt to reverse its internal borrowing position at any time by taking out additional borrowing from the PWLB. This option has been exercised in February 2024 and an additional £15m in borrowing from the PWLB was undertaken on a fixed term basis following consultation with the Council's treasury advisers. The new loans are fully affordable within the existing planned budget provision.

## 5. Interest Rate Forecast

5.1. Arlingclose, the Council's treasury advisors, have provide the following economic and interest rate view as at February 2024:

| | Current | Mar-24 | Jun-24 | Sep-24 | Dec-24 | Mar-25 | Jun-25 | Sep-25 | Dec-25 | Mar-26 | Jun-26 | Sep-26 | Dec-26 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Official Bank Rate | | | | | | | | | | | | | |
| Upside risk | 0.00 | 0.25 | 0.25 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.75 | 0.75 | 1.00 | 1.00 | 1.00 |
| Central Case | 5.25 | 5.25 | 5.25 | 5.00 | 4.75 | 4.25 | 3.75 | 3.25 | 3.00 | 3.00 | 3.00 | 3.00 | 3.00 |
| Downside risk | 0.00 | -0.25 | -0.50 | -0.75 | -1.00 | -1.00 | -1.00 | -1.00 | -1.00 | -1.00 | -1.00 | -1.00 | -1.00 |

**Underlying assumptions:**

- UK inflation and wage growth remains elevated, although on a likely downward trend over the first half of 2024. Core and services inflation is likely to remain in excess of target throughout this period, so policymakers will be cautious when it comes to easing monetary policy, despite growing downside risks. UK growth rates will remain low as increasingly restrictive monetary policy dampens activity.

- In February, the language in the MPC minutes moved to a more neutral position, despite two members continuing to vote for a further rise in Bank Rate. The focus is now on assessing how long Bank Rate needs to remain at 5.25% before reducing, with the projections in the Monetary Policy Report suggesting that market expectations for rate cuts are not far from the mark.
- UK activity data remains relatively weak, although there has been some evidence of recovery in the services sector and housing market. Consumer confidence is low but on an improving trend; household spending on goods, though, remains under pressure.
- Employment demand continues to ease, although remaining relatively resilient given the soft economic backdrop. Anecdotal evidence suggests lower pay growth, and we expect unemployment to rise, which will lead to some deterioration in consumer sentiment. Household and business spending will therefore remain weak.
- Inflation rates will move lower over the next 12 months. By April, the headline CPI rate will likely be at or below the 2% target, but with upside risks from geo-political issues. With policymaker fears around the persistence of underlying inflationary pressure, we believe Bank Rate will remain unchanged until August and initially reduce slowly.
- Maintaining monetary policy in restrictive territory for so long, when the economy is already struggling, will require substantial loosening in 2025 to boost activity.
- Global bond yields will remain volatile. Investors' expectations of near-term US rate cuts have been dealt a severe blow by the continued strength of the US economy, particularly labour markets. Investors' positioning for the timing of US monetary loosening will continue to influence movements in gilt yields.
- Moreover, there is a heightened risk of fiscal policy, credit events and/or geo-political events causing substantial volatility in yields.

**Forecast:**

- The MPC held Bank Rate at 5.25% in February.
- The MPC will cut rates in the medium term to stimulate the UK economy but will be reluctant to do so until it is sure there will be no lingering second-round effects. We see rate cuts from Q3 2024 to a low of around 3% by late 2025.
- The risks around Bank Rate are initially balanced before shifting to the downside due to on-going soft UK economic activity and the resulting dampening effects on inflation. Upside risks to inflation remain, but the likelihood of further rises in Bank Rate are low.
- Long-term gilt yields have moved higher since the start of the year, largely due to stronger US data. Arlingclose's central case is for yields to be volatile around a relatively narrow range, reflecting the likelihood for monetary loosening in the Eurozone, UK and US.

## 6. Compliance with Treasury and Prudential Limits

6.1. As at the end of January 2024, the Council has operated within the treasury and prudential indicators set out in the Council's Treasury Management Strategy Statement and in compliance with the Council's Treasury Management Practices.