Report Title:	**Treasury Management Position to September 2024**
Date of meeting:	Wednesday 11 December 2024
Report to:	Audit & Governance Committee
Report of:	Executive Director of Corporate Services and Commercial
Portfolio:	Corporate Services
Wards affected:	All wards
Is this a key decision:	Yes · Included in Forward Plan: Yes
Exempt/confidential report:	No

Summary:

This report provides Members with a review of the Treasury Management activities undertaken to 30th September 2024. This document is the second 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 30th September 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.

The Rationale and Evidence for the Recommendations

To ensure that Members are fully appraised of the treasury activity undertaken to 30th September 2024 and to meet the reporting requirements set out in Sefton's Treasury Management Practices and those recommended by the CIPFA code.

1. Introduction

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 2024/25 (approved by Council on 29th February 2024) included a requirement for regular updates to be provided on the investment activity of the Authority. This report is the second of such reports for the year and presents relevant Treasury Management information for the period ending 30th September 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 30/09/2024 comprise the following:

Institution	Deposit £m	Rate %	Maturity	Rating
Money Market Funds:				
Aberdeen	2.58	4.96	01.10.24	AAA
Aviva	2.58	5.01	01.10.24	AAA
Blackrock	0.20	4.90	01.10.24	AAA
BNP Paribas	2.58	4.96	01.10.24	AAA
Goldman-Sachs	2.58	4.92	01.10.24	AAA
Invesco	2.58	5.00	01.10.24	AAA
Morgan Stanley	2.58	4.94	01.10.24	AAA
Federated	2.58	5.03	01.10.24	AAA
Insight	2.58	5.01	01.10.24	AAA
Total	20.84			
Property Fund:				
CCLA	5.00	5.21	n/a	n/a
Total	5.00			
TOTAL INVESTMENTS	**25.84**			

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 2024/25. The balance of investments is therefore expected to fall over the coming months as the income is fully expended.

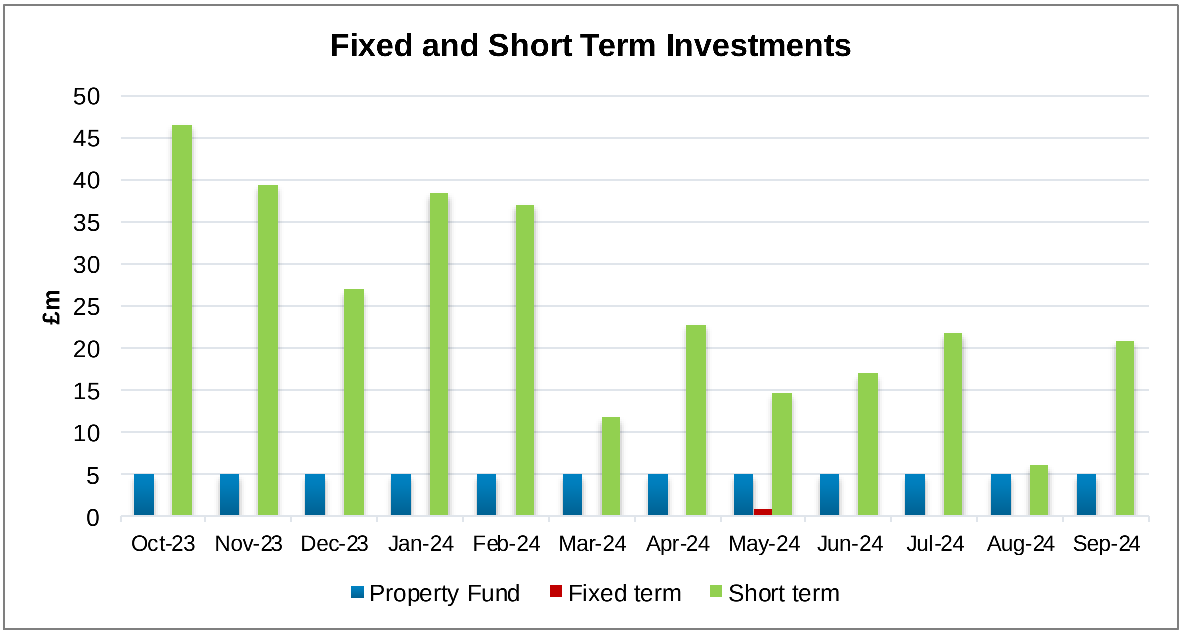
2.3. All of the investments made since April 2024 have been with organisations on the current counterparty list. The maximum level of investment permitted in the Treasury Management Strategy in any one institution, or banking group, is currently £15m. Whilst the maximum should be retained, in light of 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).

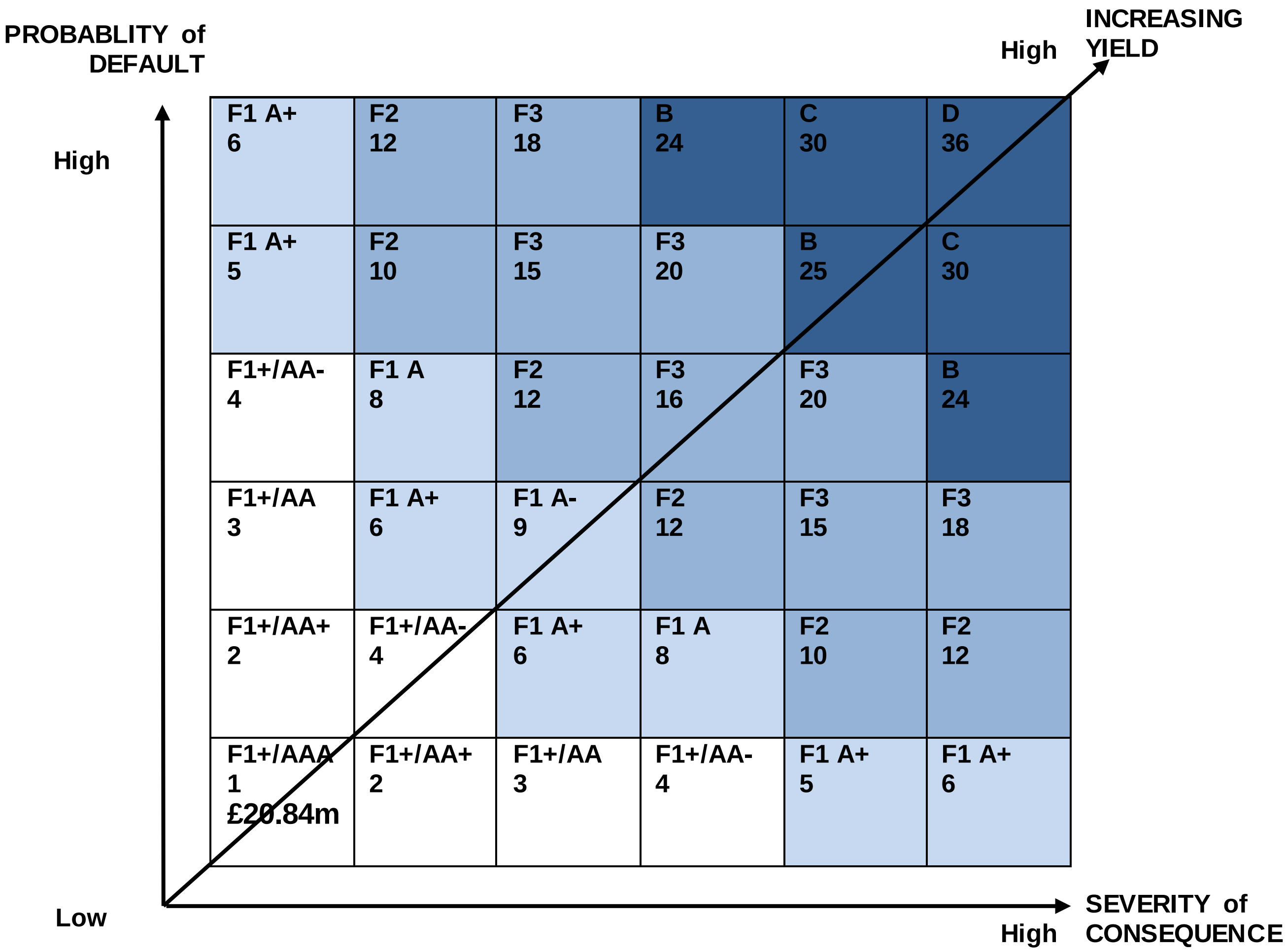
2.5. An investment has been made with the Church, Charities and Local Authority Investment Fund (CCLA) in June 2014. CCLA invest in commercial property which is rented out to enterprises such as retail units, warehousing, and offices. The majority of properties owned are in the south of the country where 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 September 2024 from 282.48p per unit to 276.04p per unit, a decrease of 2.3%. 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 September 2024 was 5.21% which, is higher than returns received in the past and represents a reasonable return on the Council's investment.

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	**£20.84m**
LOW - MEDIUM	5 - 9	Investment Grade	-
MEDIUM	10 - 20	Investment Grade	-
HIGH	21 - 36	Speculative Grade	-

2.9. The Council will continue to maximise any investment opportunities as they arise although it is not envisaged that any substantial increase in returns can be achieved for the remainder of the current financial year as balances available for investment will be held in short term deposits to allow the council to respond to any exceptional demands for cash as they arise. The security and availability of cash will be prioritised over improved yields as per the agreed Treasury Management Strategy and advice received from Sefton's treasury management advisors.

3. <u>Interest Earned</u>

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

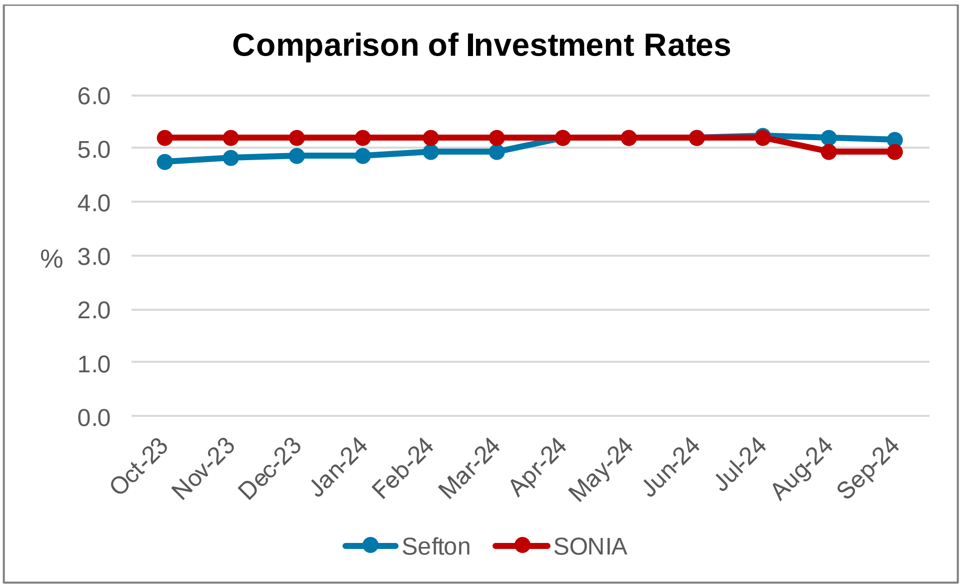
	Budget £m	Actual £m	Variance £m
Sep-24	0.605	0.680	0.075

	Budget £m	Forecast £m	Variance £m
Outturn 2024/25	1.343	1.537	0.194

3.2. The forecast outturn for investment income shows the level of income to be above target against the budget for 2024/25. Investment rates had remained at a higher level over the past twelve months (see 3.4. below) when compared to previous years largely in response to previous rises in interest rates. The budgeted income for 2024/25 was therefore set at a higher level when compared to prior financial years.

3.3. As mentioned in paragraph 2.9, it is not envisaged that improved rates will lead to a significant increase over and above the current forecast income from investments during 2024/25. Investment rates have begun decreasing as central banks have cut rates towards the second half of 2024. Sefton expects to be a net borrower in future years and therefore cash balances are diminishing and will be held in short term deposits which are low risk but return a lower level of investment income.

3.4. The Council has achieved an average rate of return on its investments of 5.2%. 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 performed in line with the SONIA to the end of September 2024.

4. Borrowing Strategy

4.1. As outlined in the Treasury Management Strategy approved by Council in February 2024, 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. After substantial rises in interest rates since 2021 many central banks have now begun to reduce rates, albeit slowly. Gilt yields were volatile over the 6-month period and have reduced slightly between April and September 2024. Much of the downward pressure from lower inflation figures was counteracted by upward pressure from positive economic data.

4.3. The PWLB certainty rate for 10-year maturity loans was 4.80% at the beginning of the half year period to September and 4.79% at the end. The lowest available 10-year maturity rate was 4.52% and the highest was 5.18%. Rates for 20-year maturity loans ranged from 5.01% to 5.57% during the half year, and 50-year maturity loans from 4.88% to 5.40%.

4.4. The Council has PWLB loan maturities of £8.846m scheduled during 2024/25 comprising several historic loans. The Council has pursued a strategy of internal borrowing in recent years 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. This position is however, considered temporary and may be reversed at any time in response to the ongoing liquidity needs of the Authority or when exceptional demands for cash may arise.

Impact of the High Needs Deficit:

4.5. Cabinet receives regular reports on the Council's High Needs Budget and the current deficit position that has been increasing over a number of years due to rising demand for provision coupled with a shortfall in funding made available from central government. The deficit position reported to Cabinet on 25 July 2024 was £38m as at the end of 2023/24 financial year. Due to the increased pressure the High Needs Deficit has placed on the availability of cash balances the Council has taken additional short-term borrowing of £15m and one longer term loan of £5m during the period to September 2024. These loans were taken in the Local Authority to Local Authority market at below PWLB rates.

4.6. The High Needs Deficit is fundamentally impacting the Council’s treasury management activity and budget activity. It is forecast that the Council could be servicing a deficit that will be around £59m at the end of the financial year that will arise from the cumulative effect of High Needs expenditure incurred in excess of Dedicated School Grant (DSG) funding from central government over several years. It is anticipated that further external borrowing will therefore be required in 2024/25 to further reverse the Council’s internal borrowing position and maintain prudent levels of liquidity.

4.7. Officers have sought clarification from MHCLG on the application of DSG debt costs and have been advised that this must be charged to the General Fund. The estimated revenue account impact of the High Needs Deficit over the next three years could therefore be £1.5m in 2024/25, £3.2m in 2025/26, and £4.0m in 2026/27. Funding diverted to servicing these additional costs will reduce the amount of funding available for core services.

4.8. Officers will continue to take advice from the Council’s external treasury advisers when undertaking new borrowing in order to ensure borrowing remains prudent and affordable and to minimise the financial impact to the Council.

5. Interest Rate Forecast

5.1. Arlingclose, the Council’s treasury advisors, have provide the following interest rate view as at November 2024:

	Current	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27	Jun-27	Sep-27
Official Bank Rate													
Upside risk	0.00	0.00	0.25	0.50	0.50	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75
Central Case	4.75	4.75	4.50	4.25	4.00	3.75	3.75	3.75	3.75	3.75	3.75	3.75	3.75
Downside risk	0.00	0.00	-0.25	-0.25	-0.50	-0.50	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75

Underlying assumptions:

- As expected, the Bank of England Monetary Policy Committee (MPC) cut Bank Rate to 4.75% in November in an 8-1 vote. However, the outlook for monetary policy has changed following the new government's fiscal plans, as delivered in the recent Budget.
- The Budget contained measures that will boost demand, in a constrained supply environment, while pushing up direct costs for employers. The short to medium-term inflationary effects of the Budget require a change to our Interest Rate Forecast.
- UK GDP recovered well in H1 2024 from technical recession, but underlying growth appears relatively subdued. However, the Budget will significantly boost government spending over the short-term, with few offsetting measures to subdue household demand, so GDP growth is likely to rise relatively steeply.
- Private sector wage growth has eased to 4.8% yet remains high, while services inflation continues to hold above pre-pandemic levels. The increase in employers' NICs, minimum and public sector wage levels could have wide ranging impacts on private sector employment demand and costs, but the near-term impact will likely be inflationary as these additional costs get passed to consumers.
- CPI inflation was below the 2% target in September but will rise a little by year-end as energy price declines from the previous year fall out of the annual comparison. The Bank of England (BoE) estimates the Budget impact will see the CPI rate at 2.7% by year end 2025 and remain over target in 2026, as opposed to the prior projection of inflation easing back to and then below target by this point.
- The MPC re-emphasised the gradual move to easing monetary policy, and we now believe the Budget measures have both reduced the pace of Bank Rate cuts and increased the low for this loosening cycle (although downside risks remain in the medium term).
- The increase in borrowing, rise in inflation and shallower path for Bank Rate projected by the Office for Budget Responsibility (OBR) raised gilt yields. The material change in rate expectations means that yields will be generally higher in the post-Budget world.
- US government yields have risen following Donald Trump's and Republican victories in the US elections. Trump has run on a platform of policies that appear inflationary, calling into question the extent of policy loosening required from the Federal Reserve (which was already uncertain given continued solid US growth data). Higher US yields could also support higher UK yields.

Forecast:

- In line with our forecast, Bank Rate was cut to 4.75% in November 2024.
- The MPC will continue to lower Bank Rate to reduce the restrictiveness of monetary policy, but more slowly and to a higher level. We see another rate cut in February 2025, followed by one cut per quarter, in line with Monetary Policy Report publication, to a low of 3.75%.
- Long-term gilt yields have risen to reflect both UK and US economic, monetary and fiscal policy expectations, and increases in bond supply. Volatility is likely to remain elevated as the market digests incoming data for clues around the impact of policy changes.
- This uncertainty may also necessitate more frequent changes to our forecast than has been the case recently.
- Upside risks to inflation over the next 12 months could limit the extent of monetary easing, but we see the risks as broadly balanced over the medium term.

6. <u>Compliance with Treasury Management Limits</u>

6.1. As at the end of September 2024, the Council has operated within the treasury limits for borrowing and investments set out in the Council's Treasury Management Strategy Statement and in compliance with the Council's Treasury Management Practices.

6.2. <u>Liability Benchmark:</u> the Council monitors its levels of external debt (excluding long term liabilities) against a prudential indicator for the liability benchmark. The benchmark for 2024/25 and the following two financial years is shown below compared to the Council's forecast level of borrowing:

Liability Benchmark	**31.03.25 Estimate £m**	**31.03.26 Estimate £m**	**31.03.27 Estimate £m**

Loans CFR *	236.4	229.8	242.1
Less: Balance sheet resources	-57.0	-31.7	-28.5
Net loans requirement	179.4	198.1	213.5
Plus: Liquidity allowance	10.0	10.0	10.0
Liability benchmark	**189.4**	**208.1**	**223.5**
Forecast Borrowing	173.8	194.5	213.0

** CFR excluding other long-term debt liabilities*

6.3. The Council's forecast borrowing has remained broadly in line with the benchmark although this may be exceeded from time to time due to temporary liquidity requirements and where there is a need to reverse the Council's internal borrowing position. As mentioned in 4.5 above, additional borrowing has been required due to exceptional demands from the High Needs deficit and a prudent estimate of this demand has been included above. The level of forecast borrowing will not exceed the Authorised Limit and Operational Boundary for 2024/25 agreed by Council in February.

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

Maturity structure of fixed rate borrowing:	Upper Limit %	Lower Limit %	Actual %
Under 12 months	20	0	14
12 months to 24 months	20	0	7
24 months to 5 years	20	0	10
5 years to 10 years	30	10	22
10 years to 15 years	50	10	14
15 years +	50	30	33

6.5. External Debt: This indicator shows the levels of actual debt compared to the authorised limit and operational boundary set for the current financial year:

External Debt:	**2024/25 £m**
Authorised limit for external debt	200
Operational boundary for external debt	175
Actual external debt 30.09.24	157

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

Long-term Treasury Management Investments:	**2024/25 £m**	**2025/26 £m**	**2026/27 £m**	**No fixed date £m**
Limit on principal invested beyond year end	15	10	5	15
Actual principal invested beyond year end	0	0	0	5

6.7. Long-term investments with no fixed maturity date include strategic pooled funds, real estate investment trusts and directly held equity but exclude money market funds and bank accounts with no fixed maturity date as these are considered short-term. As at the end of September 2024, Sefton holds £5m with the CCLA Property Fund as a strategic investment with no fixed maturity date.

6.8. Interest Rate Risk Indicator: This indicator is set to control the Authority's exposure to interest rate risk. A target is set for the one-year impact of a 1% rise and a 1% fall in interest rates on the revenue account. This is measured by examining the parallel shifts in yield curves on borrowing net of treasury investments. The impact of a change in interest rates is calculated on the assumption that maturing loans and investments will be replaced at new market rates.

Interest Rate Risk Indicator	**Limit £m**	**Forecast £m**
Upper limit on one-year revenue impact of a 1% **rise** in interest rates	1.0	0.4
Upper limit on one-year revenue impact of a 1% **fall** in interest rates	1.0	0.4

Financial Implications

A surplus in investment income has been experienced for 2024/25.

Legal Implications

The Council has a statutory duty under the Local Government Act 2003 to review its Prudential Indicators and Treasury Management Activities.

Corporate Risk Implications

Treasury management risks are assessed and managed under the Treasury Management Policy and Strategy and the Treasury Management Practices. Having operated with the limits and parameters set at the beginning of the year, the Council has remained within its agreed risk appetite and there are no additional risk implications to be considered.

Staffing HR Implications

None

Conclusion

The Council has acted in accordance with the CIPFA Prudential Code for Capital Finance in Local Authorities and has reviewed its Prudential Indicators to comply with legislation and is acting prudently in that its capital expenditure proposals remain affordable.

Alternative Options Considered and Rejected

None.

Equality Implications: There are no equality implications.
Impact on Children and Young People: None.
Climate Emergency Implications: The recommendations within this report will have a neutral impact. The Council has during 2024/25, 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.

What consultations have taken place on the proposals and when?

(A) Internal Consultations

The Executive Director of Corporate Services and Commercial (FD7868/24) and the Chief Legal and Democratic Officer (LD5968/24) have been consulted and any comments have been incorporated into the report.

(B) External Consultations

The Council's external Treasury Management Advisors: Arlingclose have provided advice with regards to Treasury Management activities undertaken during the financial year.

Implementation Date for the Decision:

Immediately following the meeting.

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Appendices:

There are no appendices to this report.

Background Papers:

There are no background papers to this report.