Agenda Item No. 7

Note:

It is important to note that the Treasury Strategy Statement is adopted by the Council, based upon advice from its external treasury advisors, and accordingly the Strategy is tailored to meet the specific and unique needs of the Council. All financial information contained within this Report and Statement should not be used by any individual or organisation as a basis for making investment or borrowing decisions. The Council and its treasury advisors will not accept any liability on behalf of any individual or organisation that seeks to act on the financial information contained within this Report and Statement.

Meeting of the Audit and Standards Committee – 27th January 2025

Report of the Interim Director of Finance (Section 151 Officer)

Treasury Management

Purpose

1. The purpose of this report is:

   - To outline treasury activity in the year 2024/25 up to 31st December 2024.
   - To set out the Treasury Strategy Statement 2025/26.

Recommendations

2. It is recommended:

   - That the Committee notes the treasury activities in 2024/25 outlined in this report.

- That the Committee approves the Treasury Strategy 2025/26 attached as Appendix 2 for subsequent submission to Cabinet and Full Council.
- That the Committee authorises the Interim Director of Finance (S151 Officer) to effect such borrowings, repayments and investments as are appropriate and consistent with the approved Treasury Strategy and relevant guidance.
- That the Committee refers all the above for approval by full Council at its meeting on 24th February 2025.

Background

3. Treasury Management entails the management of the Council's cash flows, its borrowings and investments, the management of the associated risks and the pursuit of the optimum performance or return consistent with those risks.

4. The Council undertakes treasury management activity on its own behalf and as administering authority for the West Midlands Debt Administration Fund (WMDAF). The Council is responsible for administering capital funding of £736m on the Council's account and another £43m on behalf of other West Midlands councils in respect of the WMDAF. The treasury function is governed by the Council's Treasury Policy Statement and Treasury Management Practices.

5. The Bank of England Base Rate reported in the previous Treasury Management report that was taken to this Committee was 5.25%. This rate has been cut twice since that report and is now at 4.75% (see Appendix 2 for more information).

6. Appendix 2 contains some detailed economic commentary but in summary the Monetary Policy Committee is expected to decrease interest rates slowly through 2025 and 2026.

7. In November 2020 HM Treasury prohibited access to Public Works Loans Board loans for the purpose of funding investments purely for commercial income, and the revised code prohibits local authorities any new commercial investments altogether with immediate effect. The revised code requirements on commercial investments do not impact on Dudley MBC as the Council already has a long-standing policy to refrain from investing in assets purely for revenue income or other financial return (see Section 7 of the Treasury Management Strategy).

Treasury Activity 2024/25 - Dudley Fund

8. Treasury activities in the current year have been undertaken in the context of the Treasury Strategy Statement 2024/25 approved by Audit and Standards Committee and Full Council in February 2024. In that document the Council anticipated that long term borrowing would be required in the next 12 months due to cashflow need.

9. The Council's investments up to 31st December 2024 have averaged £45.2m. The average return on these investments since the start of the year was 4.51% and the interest received was £1.7m. All investments were placed with institutions that satisfied the criteria for credit-worthiness set out in the Treasury Strategy Statement 2024/25. The performance of the Council's investments is largely dependent on movements in short-term (up to one year) rates. The Council's investment activity for 2024/25 (to 31st December 2024) is set out in more detail in Appendix 1.

10. The returns outlined above have been achieved without compromising on the security of the Council's investments. The Council have maintained and continue to maintain an approved investment list that sets the highest rating standards. The Council have an account with the Government's Debt Management Office (DMO) which provides maximum security and reasonable returns. The Council use this account extensively due the fact that it has strict credit criteria in the Investment Strategy for non-government counterparties.

11. The average value of long-term borrowings up to the 31st December 2024 was £649.9 million. The average rate of interest on these borrowings was 3.99% and interest paid was £19.6m and they were due to mature on dates ranging from the current year to 2072. To date no new long term loans have been taken out in 2024/25.

12. The Council has also taken 2 short-term loans in the year to date to manage daily cash flow; the first with a duration of 4 days and the other with a duration of 3 days. The first was for £8.5m and the other was for £2.5m; both at a rate of 5.40%. These were both with other local authorities and have now been repaid.

13. The Council is monitoring cash flows and interest rates closely and anticipate that, due to the Council's capital programme, planned use of reserves and loan maturities, further borrowing is likely to be taken by the end of the 2024/25 financial year; the current estimate is a further approximately £40m before the end of the year which is driven by cashflow needs. This borrowing is driven by current capital

spending, it will be replacement of internal borrowing by external loans.

Treasury activity 2024/25 - WMDAF

14. The Council has taken 5 short term loans in the year to date to manage daily cash flow for the WMDAF. The average value of the borrowing has been £4.2m at an average rate of 5.13% for an average duration of 126 days. The latest estimate of interest payable by members of the WMDAF in 2024/25 is 5.4%.

15. The Council has made no short term investments with the DMO in the year to date for the WMDAF.

Treasury Strategy Statement 2025/26

16. The Treasury Strategy Statement covers the Council's latest capital funding requirements, the view of interest rate movements and the strategy for borrowing and investment in the light of that view. As such, it needs to be reviewed annually. The proposed Treasury Strategy Statement for 2025/26 is attached as Appendix 2.

17. The Council's expectations for interest rates advised by the treasury advisors Link Group, which will be subject to continuous review with the treasury advisors, are as follows:

- **Short-term rates**. The Bank Rate is expected to remain at 4.75% during early 2025 but drop steadily through the year to 4% by December 2025.
- **Medium-term rates**. 5-year PWLB certainty rate is expected to be 4.90% in March 2025 and drop slightly to 4.50% by March 2026.
- **Long- term rates**. 50-year PWLB certainty rate is expected to be 5.30% in March 2025 and drop to 4.90% by March 2026.

18. The Local Government Act 2003 introduced a system of "prudential borrowing" allowing councils to set their own borrowing limits subject to criteria of prudence and affordability. These criteria are set out in more detail in the Chartered Institute of Public Finance & Accountancy (CIPFA) Prudential Code which specifically requires us to set a number of prudential indicators. The proposed indicators that relate to treasury management are set out in the Treasury Strategy Statement.

19. In order to protect the Council's position if an individual or organisation were to act upon the views expressed in this report, the Council have deemed it necessary to produce a disclaimer which is shown as a note at the head of the report and Appendix 2.

Finance

20. Forecasts of performance against budget for treasury management activities are sensitive to movements in cash flow and interest rates. The revenue impact of any variances are reported regularly to Cabinet as part of the wider Financial Monitoring Regime (FMR).

Law

21. The Council has adopted CIPFA's Treasury Management in the Public Services: Code of Practice 2021 which requires the Council to approve a treasury management strategy before the start of the financial year and provide a mid-year update on treasury management activity. In addition, the Ministry for Housing, Communities and Local Government (MHCLG) issued revised Guidance on Local Authority Investments in 2010 that required the Council to approve an investment strategy before the start of each financial year. This report fulfils the legal obligation under the Local Government Act 2003 to have regard to both the CIPFA code and the MHCLG guidance.

Risk Management

22. Treasury Management, by its nature entails the management of financial risks, specifically credit risk for investments which is mitigated by limiting acceptable counterparties to those of the highest credit quality and imposing counterparty limits for non-government institutions; and interest rate risk which is mitigated by prudential indicators detailed in Appendix 2.

Equality Impact

23. The treasury management activities considered in this report have no direct impact on issues of equality.

Human Resources / Organisational Development

24. There are no Human Resources / Organisational Development implications associated with this report.

Commercial / Procurement

25. The over-riding purpose of the Council's Treasury Strategy is day to day cash management and not income generation. The strategy prioritises security and liquidity of cash investments over yield. Once those are met, the Council aims to secure the maximum yield from the investments held with the small number of counterparties that meet the strict criteria laid out in the Annual Investment Strategy.

Environment / Climate Change

26. The Council is required to consider environmental, social and governance considerations when making investments. It will not invest in fossil fuel companies.

Council Plan

27. Treasury Management supports the Council's capital investment priorities as set out in the approved Capital Strategy.

Brendan Arnold
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List of Background Papers

- Treasury Policy Statement, Treasury Management Practices and Schedules to the Treasury Management Practices.
- The Local Government Act 2003
- The Prudential Code for Capital Finance in Local Authorities (CIPFA)
- Guidance on Local Government Investments Issued by the Secretary of State under section 15(1)(a) of the Local Government Act 2003
- Code of Practice for Treasury Management in the Public Services (CIPFA)

Appendix 1

Investment Activity 2024/25 to 31st December 2024

Counterparties	Number of investments	Average value £ million	Average rate %	Average duration (days)
Debt Management Office	354	40.19	4.97	14
Lloyds Call Account	n/a	2.43	5.01	Call
Santander Call Account	n/a	1.42	3.23	Call
Santander Notice Account	n/a	0.02	4.70	35 day notice
Barclays Call Account	n/a	1.14	4.65	Call

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DUDLEY METROPOLITAN BOROUGH COUNCIL
TREASURY STRATEGY STATEMENT 2025/26

1.0 Introduction

2.1 This Treasury Strategy Statement details the expected activities of the treasury function in the financial year 2025/26. The suggested strategy is based upon officers' views of interest rates as advised by external advisors, supplemented with leading market forecasts. It should be noted that the use of expert external advisors does not remove the responsibility of members and officers for treasury management functions and that those functions cannot be delegated to any outside organisation. The strategy covers:

- the current portfolio position
- prudential and treasury indicators
- prospects for interest rates
- temporary investment strategy
- requirements and strategy for long-term borrowing
- debt rescheduling and premature repayment opportunities
- treasury implications for the Housing Revenue Account (HRA)

2.0 Current Portfolio Position

2.2 The Council's estimated debt position as at 1st April 2025 is as follows:

	£m
Long-term debt:	
- PWLB fixed rate	660.7
- PWLB variable rate	0.0
- Market fixed rate	0.0
- Market LOBO*	10.0
Short-term debt	10.0
Total debt	680.7

*Lenders Option Borrowers Option (LOBO). This loan was at a fixed rate of 4.6% until February 2009 after which the rate may be varied at the lender's option. If the lender exercises this option to vary the rate then the Council, as the borrower, have the option to repay the loan.

2.2 The average rate of interest on the above debt is expected to be 4.05%.

2.3 The average level of investments held by the Council during 2024/25 to December 2024 was £45.2m. Cashflow monitoring indicates that long term borrowing is likely to be required in the next 12 months.

2.4 The Council also administers the debt of the former West Midlands County Council on behalf of the West Midlands districts. The estimated debt position at 1st April 2025 is as follows:

	£m
Long-term debt: - PWLB fixed rate	24.7
Short-term debt	0.0
Total debt	**24.7**

2.5 The average rate of interest charged to the West Midlands fund is expected to be 5.84%.

3.0 Prudential & Treasury Indicators

3.1 Under the Local Government Act 2003 and the Prudential Code for Capital Finance in Local Authorities, local authority capital spending and its borrowing to fund that spending is limited by what is affordable, prudent and sustainable. The Prudential Code sets out a number of indicators that enable the authority to assess affordability and prudence. The following indicators are relevant for the purposes of setting an integrated treasury management strategy.

3.2 Treasury Indicators in the Prudential Code

The Prudential Code requires that the total external debt does not exceed the Authorised Limit for external debt and only exceeds the Operational Boundary for external debt temporarily on occasions due to variation in cash flow.

These external debt indicators are intended to ensure that levels of external borrowing are affordable, prudent and sustainable. The authorised limit for external debt is a statutory limit (section 3 of the Local Government Act 2003) that should not be breached under any circumstances. It has been calculated to take account of the Council's capital expenditure and financing plans and allowing for the possibility of unusual cash movements. The operational boundary for external debt has also been calculated with regard to the Council's capital expenditure and financing plans allowing for the most likely, prudent, but not worst-case scenario for cash flow. Temporary breaches of the operational boundary, due to variations in cash flow, will not be regarded as significant. Actual external debt represents the closing balance for borrowing and other long-term liabilities.

	2023/24 **£m**	**2024/25 Revised** **£m**	**2025/26 Revised** **£m**	**2026/27 Revised** **£m**	**2027/28 Revised** **£m**	**2028/29** **£m**
Authorised limit for external debt : Borrowing	n/a	779	794	822	843	845
Other long term liabilities	n/a	11	10	9	8	6
Total	**n/a**	**790**	**804**	**831**	**851**	**851**
Operational Boundary*						
Borrowing	n/a	741	777	805	816	816
other long term liabilities	n/a	11	10	9	8	6
Total	**n/a**	**752**	**787**	**814**	**824**	**822**
Actual External Debt: Borrowing	701.7	n/a	n/a	n/a	n/a	n/a
Other long term liabilities	11.1	n/a	n/a	n/a	n/a	n/a
Total	**712.8**	n/a	n/a	n/a	n/a	n/a

3.3 Gross Debt and the Capital Financing Requirement

This is a key indicator of prudence. In order to ensure that over the medium-term debt will only be for a capital purpose, the local authority should ensure that debt does not, except in the short term, exceed the total of capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years.

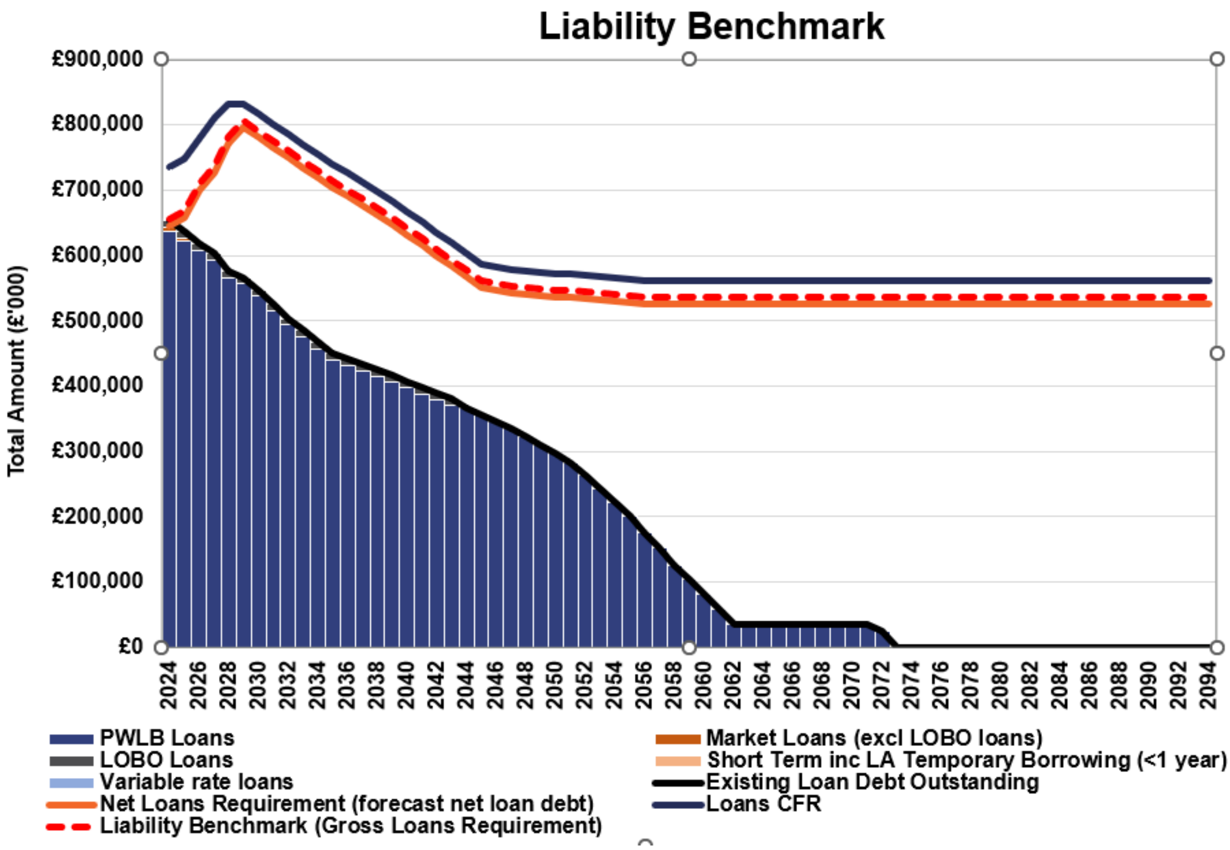
The Council has met this requirement so far in 2024/25 and expects to do so in future years. This view takes into account current commitments, existing plans and the proposals in the approved budget.

3.4 Liability Benchmark

The revised Prudential Code introduced a new prudential indicator called the Liability Benchmark (LB). The Council is required to estimate and measure the LB for the forthcoming financial year and the following two financial years, as a minimum. There are four components to the LB:-

- Existing loan debt outstanding – the Council's existing loans that are still outstanding in future years,
- Loans capital financing requirement (CFR) – this will include only approved prudential borrowing
- Net loans requirement – this is the Council's gross loan debt less treasury management investments at the last financial year end projected into the future
- Liability benchmark – (also known as the gross loans requirement) which is the net loans requirement plus short-term liquidity allowance.

As the chart shows there is currently a gap between the existing loan debt outstanding and liability benchmark this indicates that further borrowing is likely to be required in the next few years.



3.5 Capital Expenditure

The Authority's capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in the prudential indicators, which are designed to assist members' overview and confirm capital expenditure plans. The detail behind the Capital Programme is being taken to Cabinet on 17th January along with the Council's Capital Strategy.

Capital expenditure £m	2023/24 Actual	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate	2027/28 Estimate	2028/29 Estimate
Non-HRA	**46.52**	**72.21**	**63.56**	**36.91**	**26.14**	**9.65**
HRA	**52.18**	**46.06**	**78.54**	**70.78**	**70.78**	**70.78**
Total	**98.70**	**118.27**	**142.10**	**107.69**	**96.92**	**80.43**

A further indicator to assess the affordability of the Capital Programme is the ratio of financing costs to net revenue stream.

%	2023/24 Actual	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate	2027/28 Estimate	2028/29 Estimate
Non-HRA	**8.7**	**9.0**	**9.8**	**10.1**	**10.5**	**10.8**
HRA	**42.9**	**43.3**	**41.4**	**41.8**	**41.9**	**42.2**

3.6 Interest rate exposures

These indicators allow the Council to manage the extent to which it is exposed to changes in interest rates. The upper limit for fixed interest reflects the fact that it is possible to construct a prudent treasury strategy on the basis of using only fixed rate debt and investments, so long as the maturity dates of these debts and investments are reasonably spread. The same does not apply to variable rates where a 100% exposure could lead to significant year on year fluctuations in the cost of debt. The upper limit for variable rate exposure allows for the use of variable rate debt to offset the exposure to changes in short-term rates on the Council's portfolio of investments. This limit reduces over time as the strategy is to gradually reduce the level of investments.

	2023/24*	**2024/25**	**2025/26**	**2026/27**	**2027/28**	**2028/29**
Upper limit for fixed interest rate exposure	99.99	100	100	100	100	100
Upper limit for variable rate exposure	0.01	10	10	10	10	10

* 2023/24 figures are the actual percentages of debt held in these categories.

3.7 Maturity structure of borrowing and investments

The maturity structure of fixed rate borrowing is designed to protect against excessive exposures to interest rate changes in any one period, in particular over the course of the next ten years.

Dudley MBC Maturity Indicator	**Upper Limit %**	**Lower Limit %**
Under 12 months	15	0
12 months and within 24 months	15	0
24 months and within 5 years	20	0
5 years and within 10 years	25	0
10 years and above	100	50

The WMADF will close in March 2026 so no new long term loans will be required. With that in mind no new indicators for upper and lower limits have been proposed for this debt as all debt will be maturing within 12 months by the end of 2025/26.

3.8 Upper Limit for total principal sums invested over 365 days

The purpose of the limits for principal sums invested for periods longer than 365 days is to contain the Council's exposure to the possibility of loss that might arise as a result of having to seek early repayment of principal sums invested. On the basis of prudent treasury management the proposed upper limit on principal maturing in any one year for sums invested for over 365 days is £10m.

3.9 MRP Policy Statement

3.10 Regulation 27 of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 ('the 2003 Regulations') requires local authorities to 'charge to a revenue account a minimum revenue provision (MRP) for that year'. The minimum revenue provision is an annual amount set aside from the General Fund to meet the cost of capital expenditure that has not been financed from available resources, namely: grants, developer contributions (e.g. s.106 and community infrastructure levy) revenue contributions, earmarked reserves or capital receipts.

3.11 MRP is sometimes referred to as the mechanism for setting aside monies to repay external borrowing. In fact, the requirement for MRP set aside applies even if the capital expenditure is being financed from the Council's own cash resources and no new external borrowing or other credit arrangement has been entered into.

3.12 Regulation 27 of the 2003 Regulations sets out a duty for local authorities to make a Minimum Revenue Provision (MRP) and Regulation 28 requires full Council to approve a Minimum Revenue Provision (MRP) Statement setting out the policy for making MRP and the amount of MRP to be calculated which the Council considers to be prudent. This statement is designed to meet that requirement.

3.13 Regulation 27 (the Duty to make revenue provision) was amended in April 2024 and takes effect from 7 May 2024, following a number of consultations. Key changes address some common practices used to underpay MRP, namely;

- Using proceeds from asset sales to replace the revenue charge; and
- Not making MRP on debt associated with investments

3.14 In addition, the amendments to regulation 27 include provisions for making MRP where a local authority borrows to lend the money onto a third party as a capital loan.

3.15 In setting a prudent level of MRP local authorities must "have regard" to guidance issued from time to time by the Secretary of State for Housing, Communities and Local Government. The latest version of this guidance (version five) was issued by Ministry of Housing, Communities and Local Government in April 2024.

3.16 In setting a level which the Council considers to be prudent, the Guidance states that the broad aim is to ensure that debt is repaid over a period reasonably commensurate with that over which the capital expenditure provides benefits to the Council.

3.17 The Guidance sets out four “possible” options for calculating MRP, as set out below.

Option	**Calculation Method**	**Application**
1: Regulatory Method	Formulae set out in 2003 Regulations (later revoked)	Can only be applied to expenditure incurred before 1 April 2008
2: CFR Method	4% of Capital Financing Requirement	Can only be applied to expenditure incurred before 1 April 2008
3: Asset Life Method	Amortises MRP over the expected lift of the asset	Expenditure incurred after 1 April 2008
4: Depreciation Method	Charge MRP on the same basis as depreciation	Expenditure incurred after 1 April 2008

3.18 Two main variants of Option 3 were set out in the fifth edition of the 2024 Guidance: (i) the equal instalment method and (ii) the annuity method. The annuity method weights the MRP charge towards the later part of the asset’s expected useful life and is increasingly becoming the most common MRP option for local authorities.

3.19 The 2024 Guidance also included specific recommendations for setting MRP in respect of finance leases, investment properties and revenue expenditure which is statutorily defines as capital expenditure under the 2003 Regulations (also referred to as revenue expenditure funded by capital under statute or REFCUS). Examples of REFCUS include capitalised redundancy costs, loans or grants to third parties for capital purposes, and the purchase of shares in limited companies.

3.20 With effect from 1 April 2024, MRP set aside requirements will also apply to “right of use” leased assets, following the introduction of IFRS16.

3.21 Other approaches are not ruled out however they must meet the statutory duty to make prudent MRP provision each financial year.

3.22 Minimum Revenue Provision (MRP) Policy Statement for 2025/26

3.23 Having regard to the current 2024 Guidance on MRP issued by DLUHC and the "options" outlined in that Guidance (the MRP Guidance), the Council is recommended to approve the following MRP Statement to take effect from 1 April 2025, on the basis that this represents "a prudent provision" in line with Regulation 28.

MRP Stream	**Policy**	**Explanation**	**Changes from Previous Policy**
Capital Expenditure incurred before 1st April 2008	MRP will be calculated on a 4% reducing balance.	This complies with Option 2 of the MRP guidance.	Previous policies charged MRP on an annuity basis
All General Fund operational capital expenditure after 1st April 2008	MRP will be calculated on an amortised basis using the expected asset lives of the assets (Option 3 asset life), subject to a maximum useful asset life of 50 years. The discount rate to be applied will be the PWLB annuity rate applicable on 1 April in the year of expenditure.	This complies with Option 3 as set out in para 35(b) of the MRP Guidance. The MRP Guidance does not suggest which discount rate(s) to use. By specifying the PWLB new loan annuity rate at 1 April of year of expenditure provides a clearly evidenced trail to the discount rate to be used.	No change

MRP Stream	Policy	Explanation	Changes from Previous Policy
MRP for service concession contracts	The amount of MRP charge will be equal to the amount by which the balance sheet liability is written down by the unitary charge (i.e. the principal element of the unitary charge)	This complies with para 43 of the MRP Guidance.	Previous policies charged MRP on an annuity basis
Loans to third parties	MRP will be calculated on an annuity basis over the expected useful life for which the loan is to be used and adjusted by any loan principal repayments by the third party. Any residual balance will be charged to the General Fund Revenue Account, subject to the amount not being less than nil (i.e. a credit to the revenue account). The discount rate to be applied will be the PWLB annuity rate applicable on 1 April in the year the loan was issued.	This approach complies with Option 3 of the MRP Guidance and the useful life is that set out in para 47 of the MRP Guidance.	Previous policies would have charged MRP on an annuity basis but no capital loans identified so no MRP charged

3.24 Asset Lives used for MRP calculations will be determined by the Council's capital team and will be consistent with the depreciation policies set out in the Council's annual Statement of Accounts. If no life can be reasonably attributed to an asset, such as freehold land, the estimated useful life will be taken to be a maximum of 50 years. This complies with the MRP Guidance.

3.25 MRP commencement – MRP should normally begin in the financial year following the one in which the expenditure was incurred. However, in accordance with the statutory MRP Guidance, commencement of MRP may be deferred until the financial year following the one in which the asset becomes operational. This approach complies with the MRP Guidance.

3.26 The above MRP Policy statement is considered to represent a prudent charge to the General Fund for the provision of repayment of unfinanced capital expenditure and will ensure that all unfinanced capital expenditure is funded through the MRP charge in line with the life expectancies of the assets underpinning the CFR balance.

3.27 A provision of £2m has been set aside to receive the additional charges which are mandatory.

3.28 There is no requirement on the HRA to make an MRP charge, but there is a requirement for a charge to be made for depreciation.

4.0 Economic Background

4.1 The Monetary Policy Committee (MPC) has decreased the Bank of England Base Rate twice since the last time a change in rate was reported to this Committee (the current rate is now 4.75%). The market expects the rate to fall again throughout 2025 and 2026.

4.2 The CPI inflation figure has stayed low since the last report but is currently above the target of 2% but is expected to return to this level in 2025.

5.0 Prospects for Interest Rates

5.1 The Council’s Treasury Advisor, Link Asset Services, has provided the following forecast (with the PWLB rates reflecting the certainty rates available to the Council at 0.2% below the published rates):

	December 2024 (Actuals)	**December 2025 (Forecasts)**	**December 2026 (Forecasts)**	**December 2027 (Forecasts)**
Bank Rate	4.75%	4.00%	3.50%	3.50%
5yr PWLB rate	5.00%	4.50%	4.20%	3.90%
10yr PWLB rate	5.30%	4.80%	4.40%	4.10%
25yr PWLB rate	5.60%	5.20%	4.80%	4.50%
50yr PWLB rate	5.40%	5.00%	4.60%	4.30%

5.3 Link Asset Services will continue to monitor economic data releases and information released by the Monetary Policy Committee (MPC) who set the Bank Rate.

5.4 The Council's overall strategy will be based on the projections above. However, the Council will maintain flexibility to take account of unexpected variations from the forecast.

6.0 Annual Investment Strategy

6.1 The Council's investment activities are subject to government guidance issued under Section 15(1) (a) of the Local Government Act 2003. This section of the Treasury Strategy Statement constitutes an "Annual Investment Strategy" produced in accordance with the guidance.

6.2 The Council holds invested funds, representing income received in advance of expenditure plus balances and reserves held. The Council have a policy of keeping cash balances at minimum levels by maximising the use of internal borrowing to finance capital expenditure.

6.3 Both the CIPFA Code and the Ministry for Housing, Communities and Local Government (MHCLG) require the Council to invests its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return or yield. The Council's primary objective in relation to the investment of public funds remains the security of capital. The liquidity or accessibility of the Council's investments followed by the yields earned on investments is important but are secondary considerations.

6.4 *Strategy for "specified investments"*

6.4.1 The Council will make use of specified investments (as defined within the terms of the government guidance). These are investments that satisfy the following conditions:

a) The investment is denominated in sterling and any payments or repayments in respect of the investment are payable only in sterling.
b) The Council may require that the investment be repaid or redeemed within 12 months of the date on which the investment was made.
c) The making of the investment is not defined as capital expenditure by legislation.

d) The investment satisfies either of the following conditions:

I. The investment is made with the UK government, a local authority, a parish council or a community council, or
II. The investment is made with a body or in an investment scheme of high credit quality.

6.4.2 The Council will be prepared to lend to the West Midlands Combined Authority. Such lending will be as part of arrangements agreed with the Combined Authority and other constituent authorities.

6.4.3 For the purpose of this strategy a body or investment scheme is deemed to be of high credit quality if it has minimum short-term ratings of F1 (Fitch), P2 (Moody's), and A1 (Standard and Poors).

6.4.4 The Council will also limit risks by applying lending limits and criteria for "high credit quality" as shown below:

Specified Investments Counterparty	**Minimum Short-term Credit Rating***	**Maximum %s Investment per Counterparty*** **	**Time Limit**
Banks	F1/P2/A1	50%	12 months
UK Local Authorities	n/a	No maximum	12 months
UK Government	n/a	No maximum	none
Money Market Funds (MMF)	AAA**	50%	3 months

*Fitch / Moody's / S&P rating agencies respectively. Institutions must have the requisite rating at 2 of the 3 agencies.
** MMFs only have long term credit ratings so AAA would be the minimum long-term credit rating for these funds.
***N.B. If a number of banks are part of one banking group all banks within that group would fall into one counterparty.

6.4.5 Since the financial crisis of 2008, the Council has not allowed investments in non-UK institutions. This strategy has been based on the implicit assumption that the UK Government would support a failing UK bank. This factor has been less relevant since the Financial Services (Banking Reform) Act 2013 and proposed regulations. The table above now expands the list of banks to include non UK banks. In practice the Council's strategy will still be limited by the low level of investments and cashflow, but the changes should marginally improve return.

6.4.6 The Council understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support and reports in the quality financial press. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may meet the credit rating criteria.

6.4.7 When deteriorating financial market conditions affect the creditworthiness of all organisations, this is not generally reflected in credit ratings, but can be seen in other market measures. In these circumstances, the Authority will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the Authority's cash balances, then the surplus will be deposited with the UK Government, via the Debt Management Office for example, or with other local authorities. This will cause a reduction in the level of investment income earned, but will protect the principal sum invested.

6.4.8 The only indicators with prescriptive values remain to be credit ratings. Other indicators of creditworthiness are considered in relative rather than absolute terms.

6.4.9 If conditions in the financial markets worsen during 2025/26 or other factors indicate that increased security of Council funds is required, the Director of Finance may impose tighter restrictions on the type of investments and institutions used by the Council, than those detailed in this strategy.

6.4.10 The Council currently banks with Lloyds Plc. At the present time Lloyds Plc meets the minimum credit criteria. Even if the credit rating of the Council's main bank falls below the Council's minimum criteria the main bank will continue to be used for short term liquidity requirements (overnight and weekend investments) and business continuity arrangements.

6.5 *Strategy for "non-specified investments"*

6.5.1 Non-specified investments are those that do not meet the criteria for a specified investment detailed in 6.4.1 above. The Council does not intend to make any investments denominated in foreign currencies, or any that are defined as capital expenditure by legislation such as company shares. Neither is there an intention to make new long term investments, especially in the light of maximising the length of any non-government investment to 3 months irrespective of its credit quality. Therefore the Council will not place its funds with non-specified investments.

6.6 *Liquidity of investments*

6.6.1 In determining the maximum period for which investments may be held, the Council will have regard to the most recent cash-flow forecast. The Council will not enter into an investment where the cash-flow forecast indicates that, as a result of that investment, it would be forced to borrow money at a later date that the Council would not otherwise have had to borrow.

6.7 *Environmental, Social & Governance (ESG) Considerations*

6.7.1 The Council is required to consider environmental, social and governance considerations when making investments. It will not invest in fossil fuel companies.

7.0 Policy on Non-Financial Investments

7.1 Investment in non-financial assets including property is not part of the Council's Treasury Management Strategy**.** The Council will incur capital expenditure on acquisition or development of property only where the primary purpose is regeneration and/or service delivery, and then only where a development would not happen without Council involvement, and the potential regeneration gain justifies any financial or other risks. It will not invest in property for the sole or primary purpose of revenue income or other financial return.

7.2 The only non-treasury investments currently held by the Council are shares held with Birmingham Airport which were valued at £35.3m at 31st March 2024. These are held as a service type investment as they were not purchased in order to generate a financial return; rather they are for regeneration purposes only. There are no current plans to make any further non-treasury investments.

8.0 Policy on the Use of Financial Derivatives

8.1 A financial derivative is a contract whose value is based on, or "derived" from, an underlying financial instrument such as a loan. Local authorities have previously been able to make use of financial derivatives embedded into loans and investments, both to reduce interest rate risk (e.g. forward deals) and to reduce costs or increase income at the expense of greater risk (e.g. LOBO loans).

8.2 The general power of competence in Section 1 of the Localism Act 2011 removes much of the uncertainty over local authorities' use of standalone financial derivatives (i.e. those that are not embedded into a loan or investment). The CIPFA Code requires authorities to clearly detail their policy on the use of derivatives in the annual strategy.

8.3 The Council does not intend to use standalone financial derivatives (such as swaps, forwards, futures and options). Should this position change, the Council may seek to develop a detailed and robust risk management framework governing the use of derivatives, but no change in strategy will be made without full Council approval.

9.0 Requirements and Strategy for Long-Term Borrowing

9.1 The primary factor in determining whether the Council undertake new long-term borrowing will be cash flow need. The Council will seek to minimise the time between borrowing and anticipated cash flow need, subject to the need to maintain day to day liquidity.

9.2 The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The Council's strategy is to maintain borrowing and investments at a minimum (well below their underlying levels) thereby maximising the use of internal borrowing. This keeps borrowing costs lower than they would otherwise be and keeping cash balances low reduces credit risk.

9.3 The balance sheet forecast indicates a requirement to increase the level of external borrowing in the medium and long term. The Council's interest rate expectations (outlined in 5.1) provide a variety of options on the type of borrowing the Council will undertake:

- That short-term variable rates will be good value compared to long-term rates and are likely to remain so for potentially at least the next couple of years. Best value will therefore be achieved by borrowing short term at variable rates in order to minimise borrowing costs in the short term.

- That the risks intrinsic in the shorter term variable rates are such, when compared to historically relatively low long term fixed funding, which may be achievable in 2025/26, that the Council will maintain a stable, longer term portfolio by drawing longer term fixed rate funding at a marginally higher rate than short term rates.

9.4 Against this background caution will be adopted with the 2025/26 treasury operations. The Director of Finance will monitor the interest rate market and adopt a pragmatic approach to changing circumstances.

Sensitivity of the forecast - The main sensitivities of the forecast are likely to be the two scenarios below. In conjunction with the treasury advisers, the Council will continually monitor both the prevailing interest rates and the market forecasts, adopting the following responses to a change of sentiment:

- If it were felt that there was a significant risk of a sharp rise in long and short term rates, perhaps arising from a greater than expected increase in world economic activity, then the portfolio position will be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates are still relatively cheap.

- If it were felt that there was a significant risk of a sharp fall in long and short term rates, due to growth rates remaining low or weakening, then long term borrowings will be postponed.

9.5 With respect to the West Midlands Debt, variances due to timing differences between the maturity profile of the debt and repayments from authorities can be managed by short term borrowing in 2025/26.

9.6 The approved sources of long-term and short-term borrowing are:

- Public Works Loans Board
- Any institution approved for investments (above)
- Any other bank or building society authorised to operate in the UK
- UK public and private sector pension funds (except the West Midlands Pension Fund)

In addition, capital finance may be raised by finance leases and similar arrangements which may be classed as debt liabilities.

10.0 Debt Rescheduling and Premature Repayment Opportunities

10.1 The Council may consider rescheduling or premature repayment with the following aims:

- the generation of cash savings at minimum risk
- in order to help fulfil the strategy outlined in 9 above
- in order to enhance the balance of the long-term portfolio (by amending the maturity profile and/or the balance of volatility)

10.2 Any rescheduling or premature repayment will be reported to an appropriate committee at the meeting following its implementation.

11.0 HRA Self Financing

11.1 On 1st April 2012, the Council notionally split each of its existing long-term loans into General Fund and HRA pools. In the future, new long-term loans borrowed will be assigned in their entirety to one pool or the other. Interest payable and other costs/income arising from long-term loans (e.g. premiums and discounts on early redemption) will be charged/ credited to the respective revenue account.

11.2 Differences between the value of the HRA loans pool and the HRA's underlying need to borrow (adjusted for HRA balance sheet resources available for investment) will result in a notional cash balance which may be positive or negative. An average of this notional balance will be calculated annually and interest transferred between the General Fund and HRA at an internally determined rate of interest, adjusted for risk.

12.0 Training

12.1 CIPFA's Code of Practice requires the Chief Financial Officer to ensure that all members tasked with treasury management responsibilities, including scrutiny of the treasury management function, receive appropriate training relevant to their needs and understand fully their roles and responsibilities. Relevant training is provided by Link Asset Services to the members of the Audit & Standards Committee and other members of the Council.

12.2 The Council recognises the importance of ensuring that all staff involved in the treasury management function are fully equipped to undertake the duties and responsibilities allocated to them. It will therefore seek to appoint individuals who are both capable and experienced and will provide training for staff to enable them to acquire and maintain an appropriate level of expertise, knowledge and skills. The Director of Finance will recommend and implement the necessary arrangements.

13.0 Treasury Management Advisors

13.1 The Council uses Link Asset Services as its external treasury management advisers. The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon the external service providers.

13.2 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 maintains the quality of the service with its advisors by holding regular meetings and tendering periodically for the provision of treasury management advice.

13.3 The Council receives the following services from Link Asset Services:

a. Credit advice
b. Investment advice
c. Technical advice
d. Economic & interest rate forecasts
e. Workshops and training events for officers and members