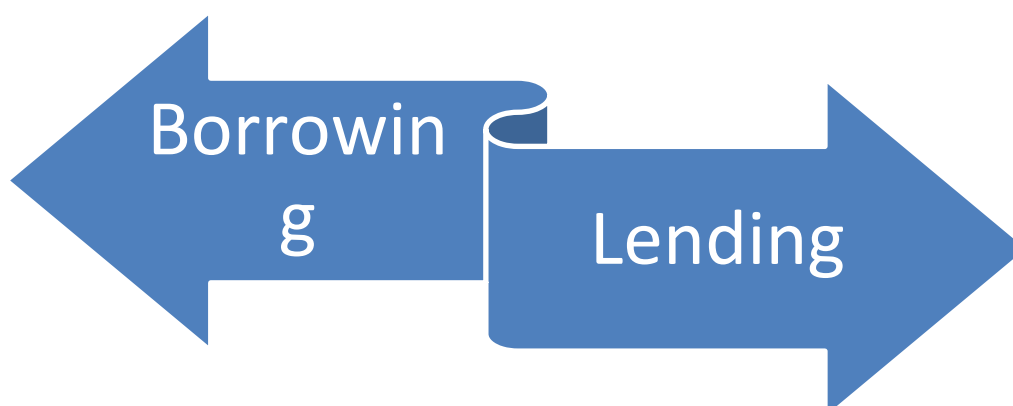


FAREHAM
BOROUGH COUNCIL

**TREASURY MANAGEMENT
STRATEGY
AND
INVESTMENT STRATEGY
2025/26**



INTRODUCTION

WHAT IS TREASURY MANAGEMENT?

1. Treasury Management is defined as:

The management of the organisation's cash flows, its banking, money market and capital market transactions;

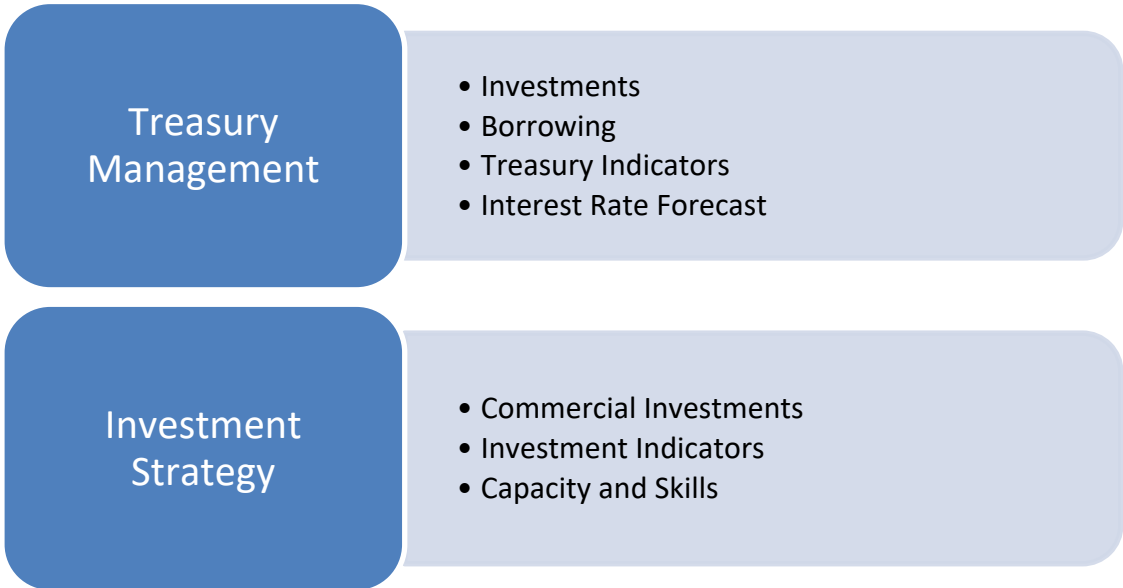
the effective control of the risks associated with those activities and the pursuit of optimum performance consistent with those risks.

2. The Council operates a balanced budget, which broadly means cash raised during the year will meet its cash expenditure. There are two aspects to the treasury management service:

- a) To ensure the 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 Council's low risk appetite, providing adequate liquidity initially before considering investment return.
- b) To ensure the cash flow meets the Council's **capital plans**. These capital plans provide a guide to the **borrowing need** of the Council. Essentially this is the longer term cash flow planning to ensure that the Council can meet its capital spending requirements. The management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses. On occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

CONTENT OF THE TREASURY MANAGEMENT AND INVESTMENT STRATEGIES

3. These strategies set out the expected approach to treasury management and investment activities for 2025/26. It covers two main areas:



4. The content of the Strategies is designed to cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, the CIPFA Treasury Management Code and the MHCLG Investment Guidance.

REPORTING REQUIREMENTS

5. The Council receives and approves three main reports each year in relation to Treasury Management, which incorporate a variety of policies, estimates and actuals. The three reports are:



6. The Executive Committee is responsible for the implementation and monitoring of these reports whilst the Audit and Governance Committee is responsible for the effective scrutiny of the treasury management strategy and policies.

TREASURY MANAGEMENT STRATEGY

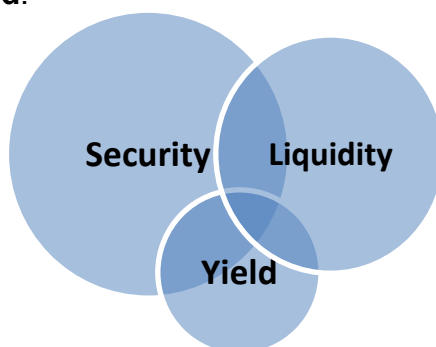
INVESTMENTS

Current Portfolio Position

7. The Council holds invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Council's investment balance has ranged between £13 million and £32 million, lower levels are expected in the forthcoming year due to capital programme expenditure.

Treasury Investment Strategy

8. The CIPFA Code requires the Council to invest its funds prudently, and to have regard to the **security** and **liquidity** of its investments before seeking the highest rate of return, or **yield**.



9. The Council's objective when investing money is to strike an appropriate balance between **risk and return**, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income. Where balances are expected to be invested for more than one year, the Council will aim to achieve a total return that is equal or higher than the prevailing rate of inflation, in order to maintain the spending power of the sum invested.
10. The Council aims to be a responsible investor and will consider environmental, social and governance (ESG) issues when investing.
11. The Council expects to be a long-term borrower and new treasury investments will therefore be made primarily to manage day-to-day cash flows using short-term low risk instruments. The existing portfolio of strategic pooled funds will be maintained to diversify risk into different sectors and boost investment income.
12. Under the new IFRS 9 standard, the accounting for certain investments depends on the Council's **business model** for managing them. The Council aims to achieve value from its treasury investments by a business model of collecting the contractual cash flows and therefore, where other criteria are also met, these investments will continue to be accounted for at amortised cost.

Approved Counterparties

13. The Council may invest its surplus funds with any of the counterparty types in the

table below, subject to the limits shown.

Sector	Time Limit	Counterparty Limit	Sector Limit
UK Government	50 years	Unlimited	n/a
Local authorities and other government entities	25 years	£4m	Unlimited
Secured investments*	25 years	£4m	Unlimited
Banks (unsecured)*	13 months	£2m	Unlimited
Building Societies (unsecured)*	13 months	£2m	£4m
Money market funds*	n/a	£4m	Unlimited
Strategic pooled funds	n/a	£5m	£20m

14. Treasury investments in the sectors marked with an asterisk will only be made with entities whose lowest published **long-term credit rating is no lower than A-**. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used. However, investment decisions are never made solely based on credit ratings, and all other relevant factors including external advice will be taken into account.
15. For entities without published credit ratings, investments may be either (a) where external advice indicates the entity to be of similar credit quality; or (b) to a maximum of £2 million per counterparty as part of a diversified pool.
16. Summary of counterparty types:
 - a) **UK Government:** Sterling-denominated investments with or explicitly guaranteed by the UK Government, including the Debt Management Account Deposit Facility, treasury bills and gilts. These are deemed to be zero credit risk due to the government's ability to create additional currency and therefore may be made in unlimited amounts for up to 50 years.
 - b) **Local Authorities and other government entities:** Loans to, and bonds and bills issued or guaranteed by, other national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is generally a lower risk of insolvency, although they are not zero risk.
 - c) **Secured investments:** Investments secured on the borrower's assets, which limits the potential losses in the event of insolvency. The amount and quality of the security will be a key factor in the investment decision. Covered bonds, secured deposits and reverse repurchase agreements with banks and building societies are exempt from bail-in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the higher of the collateral credit rating and the counterparty credit rating will be used. The combined secured and unsecured investments in any one bank will not exceed the cash limit for secured investments.
 - d) **Banks and Building Societies (unsecured):** Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than

multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail. See below for arrangements relating to operational bank accounts.

- e) **Money Market Funds:** Pooled funds that offer same-day or short notice liquidity and very low or no price volatility by investing in short-term money markets. They have the advantage over bank accounts of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a small fee. Although no sector limit applies to money market funds, the Council will take care to diversify its liquid investments over a variety of providers to ensure access to cash at all times.
 - f) **Strategic Pooled Funds:** Bond, equity and property funds, including exchange traded funds, that offer enhanced returns over the longer term but are more volatile in the short term. These allow the Council to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date, but can be either withdrawn after a short notice period or sold on an exchange, their performance and continued suitability in meeting the Council's investment objectives will be monitored regularly.
17. The Council may also invest its surplus funds in corporates (loans, bonds and commercial paper issued by companies other than banks), registered providers (loans to, and bonds issued or guaranteed by, registered providers of social housing or registered social landlords, formerly known as housing associations) and real estate investment trusts, subject to meeting the minimum credit rating criteria and time limits recommended by the Council's treasury advisers.

Operational Bank Accounts

18. The Council may incur operational exposures, for example through current accounts, collection accounts and merchant acquiring services, to any UK bank with credit ratings no lower than BBB- and with assets greater than £25 billion. These are not classed as investments but are still subject to the risk of a bank bail-in, and balances will therefore be kept below £4 million per bank. The Bank of England has stated that in the event of failure, banks with assets greater than £25 billion are more likely to be bailed-in than made insolvent, increasing the chance of the Council maintaining operational continuity.

Risk Assessment and Credit Ratings

19. Credit ratings are obtained and monitored by the Council's treasury advisers, who will notify changes in ratings as they occur. The credit rating agencies in current use are listed in the Treasury Management Practices document. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:
- no new investments will be made,
 - any existing investments that can be recalled or sold at no cost will be, and
 - full consideration will be given to the recall or sale of all other existing investments with the affected counterparty.

20. Where a credit rating agency announces that a credit rating is on review for possible downgrade (also known as “rating watch negative” or “credit watch negative”) so that it may fall below the approved rating criteria, then only investments that can be withdrawn on the next working day will be made with that organisation until the outcome of the review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.

Other Information on the Security of Investments

21. 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 and analysis and advice from the Council treasury management adviser. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may otherwise meet the above credit rating criteria.
22. Reputational aspects: The Council is aware that investment with certain counterparties, while considered secure from a purely financial perspective, may leave it open to criticism, valid or otherwise, that may affect its public reputation, and this risk will therefore be taken into account when making investment decisions.
23. When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2008, 2020 and 2022, this is not generally reflected in credit ratings, but can be seen in other market measures. In these circumstances, the Council 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 Council’s cash balances, then the surplus will be deposited with the UK Government, or with other local authorities. This will cause investment returns to fall but will protect the principal sum invested.
24. The following **internal measures** are also in place:
- Investment and borrowing decisions formally recorded and endorsed using a Counterparty Decision Document.
 - Monthly officer reviews of the investment and borrowing portfolio and quarterly reviews with the Chief Executive Officer.

Investment Limits

25. The Council’s revenue reserves available to cover investment losses are forecast to be £4 million on 31st March 2025. In order to minimise risk, in the case of a single default, the maximum that will be lent to any one organisation (other than the UK Government) will be **£5 million**. A group of entities under the same ownership will be treated as a single organisation for limit purposes.
26. Limits are also placed on fund managers, investments in brokers’ nominee

accounts and foreign countries as in the table below. Investments in pooled funds and multilateral development banks do not count against the limit for any single foreign country, since the risk is diversified over many countries.

	Cash limit
Any group of pooled funds under the same management	£10m per manager
Investments held in a broker's nominee account	£10m per broker
Foreign countries	£4m per country

Liquidity Management

27. The Council uses a purpose-built cash flow forecasting spreadsheet to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a prudent basis to minimise the risk of the Council being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Council's medium-term financial plan and cash flow forecast.
28. The Council will spread its liquid cash over at least **four providers** (e.g. bank accounts and money market funds) to ensure that access to cash is maintained in the event of operational difficulties at any one provider.

Environmental, Social and Governance Policy

29. Environmental, social and governance (ESG) considerations are increasingly a factor in global investors' decision making, but the framework for evaluating investment opportunities is still developing and therefore the Council's ESG policy does not currently include ESG scoring or other real-time ESG criteria at an individual investment level.
30. The Council will seek to move towards investments that improve the environment, bring wider social benefits, and are with organisations with good governance.
31. The Council will give weight to the environmental, social and governance elements of credit ratings in making investment decisions, provided that the overall risk profile of the investment portfolio (including liquidity risk) is not compromised, and that decisions remain consistent with responsible financial management and stewardship.

BORROWING

Current Portfolio Position

32. The Council's borrowing position at 31 March 2024, with forward projections are summarised below.

£'000	2024/25 Revised	2025/26 Estimate	2026/27 Estimate	2027/28 Estimate	2028/29 Estimate
Debt at 1 April	64,589	66,900	71,300	70,600	69,900
Expected change in debt	2,311	4,400	(700)	(700)	(600)
Gross Debt at 31 March	66,900	71,300	70,600	69,900	69,300

33. Debt at 31 March 2025 is projected to be higher than originally estimated due to borrowing short-term externally to fund the capital programme.

Borrowing Strategy

34. The Council's main objective when borrowing money is to strike an appropriately low risk balance between **securing low interest costs** and achieving **certainty of those costs** over the period for which funds are required. The flexibility to renegotiate loans should the Council's long-term plans change is a secondary objective.
35. Given the significant cuts to public expenditure and in particular to local government funding, the Council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio.
36. Short-term interest rates are currently higher than in the recent past but are expected to fall in the coming year and it is therefore likely to be more cost effective over the medium term to either **use internal resources**, or to **borrow short-term** loans instead.
37. By doing so, the Council can reduce net borrowing costs (despite foregone investment income) and **reduce overall treasury risk**. The benefits of internal borrowing or short-term borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise modestly.
38. Our treasury advisers will assist the Council with this '**cost of carry**' and breakeven analysis. Its output may determine whether the Council borrows additional sums at long-term fixed rates in 2025/26 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.
39. The Council has previously raised all of its long-term borrowing from the PWLB but will consider long-term loans from other sources including banks, pensions and local authorities, and will investigate the possibility of issuing bonds and similar instruments, in order to lower interest costs and reduce over-reliance on one source of funding in line with the CIPFA Code.
40. PWLB loans are no longer available to local authorities planning to buy investment assets primarily for yield.
41. Alternatively, the Council may arrange forward starting loans, where the interest rate is fixed in advance, but the cash is received in later years. This would enable certainty of cost to be achieved without suffering a cost of carry in the intervening period.
42. In addition, the Council may borrow further short-term loans to cover unexpected cash flow shortages.

Sources of Borrowing

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

- HM Treasury's PWLB lending facility (formerly the Public Works Loan Board).
 - National Wealth Fund Ltd (formerly UK Infrastructure Bank Ltd)
 - Any institution approved for investments.
 - Any other bank or building society authorised to operate in the UK.
 - Any other UK public sector body.
 - UK public and private sector pension funds (except the Hampshire County Council Pension Fund).
 - Capital market bond investors.
 - UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues.
44. In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:
- Leasing
 - Hire purchase
 - Private Finance Initiative
 - Sale and leaseback
 - Similar asset based finance
45. **Municipal Bonds Agency:** UK Municipal Bonds Agency plc was established in 2014 by the Local Government Association as an alternative to the PWLB. It issues bonds on the capital markets and lends the proceeds to local authorities. This is a more complicated source of finance than the PWLB for two reasons: borrowing authorities will be required to provide bond investors with a guarantee to refund their investment in the event that the agency is unable to for any reason; and there will be a lead time of several months between committing to borrow and knowing the interest rate payable. Any decision to borrow from the Agency will therefore be the subject of a separate report to full Council.
46. **Short-Term and Variable Rate Loans:** These loans leave the Council exposed to the risk of short-term interest rate rises and are therefore subject to the interest rate exposure limits in the treasury management indicators below.
47. **Debt Rescheduling:** The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. The Council may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall cost saving or a reduction in risk.

TREASURY MANAGEMENT PRUDENTIAL INDICATORS

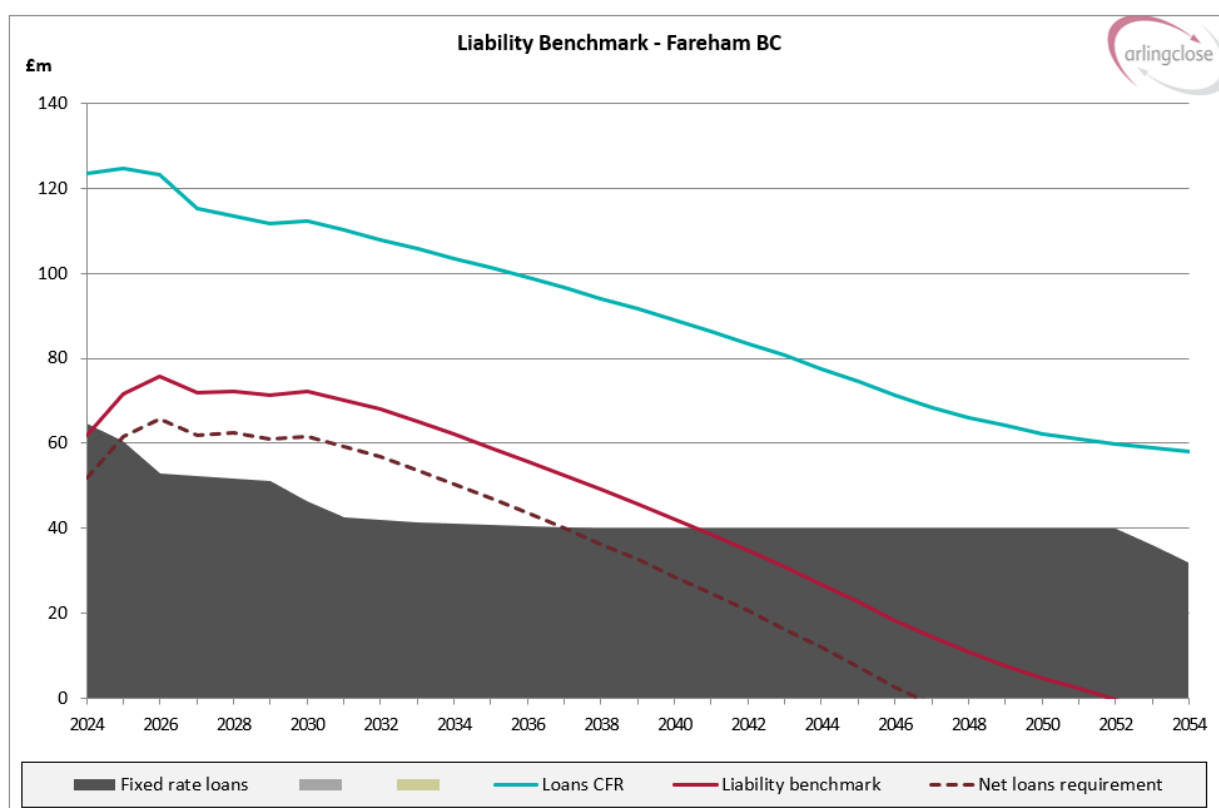
48. The Council measures and manages its exposures to treasury management risks using the following three treasury management indicators.
49. *Treasury Management Prudential Indicator 1 – Liability Benchmark:* To compare the Council's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing. This assumes the cash and investment balances are kept to a minimum level of £10m at each year-

end to maintain sufficient liquidity but minimise credit risk.

50. The liability benchmark is an important tool to help establish whether the Council is likely to be a long-term borrower or long-term investor in the future, and so shape its strategic focus and decision making. The liability benchmark itself represents an estimate of the cumulative amount of external borrowing the Council must hold to fund its current capital and revenue plans while keeping treasury investments at the minimum level required to manage day-to-day cash flow.

£'000	31/03/24 Actual	31/03/25 Estimate	31/03/26 Estimate	31/03/27 Estimate	31/03/28 Estimate
Capital Financing Requirement	123,444	124,558	123,238	115,172	113,622
Less: Balance sheet resources	(71,600)	(62,900)	(57,500)	(53,200)	(51,300)
Net loans requirement	51,844	61,658	65,738	61,972	62,322
Plus: Liquidity allowance	10,000	10,000	10,000	10,000	10,000
Liability benchmark	61,844	71,658	75,738	71,972	72,322

51. The long-term liability benchmark is shown in the chart below together with the maturity profile of the Council's existing borrowing:



52. If cash flows occur as forecast, the Council's level of existing borrowing remains below the liability benchmark for the next 16-17 years. This indicates a need for further external borrowing over this period, peaking at approximately an additional £26m by 2031 and then reducing over time.

53. *Treasury Management Prudential Indicator 2 – Long-term treasury management investments:* The purpose of this indicator is to control the Council's exposure to

the risk of incurring losses by seeking early repayment of its investments. The prudential limits on the long-term treasury management investments will be:

£'000	2024/25 Revised	2025/26 Estimate	2026/27 Estimate	2027/28 Estimate	2028/29 Estimate
Limit on principal invested beyond year end	12,000	12,000	12,000	12,000	12,000

54. *Treasury Management Prudential Indicator 3 - Maturity structure of borrowing*: This indicator is set to control the Council's exposure to refinancing risk. The upper and lower limits on the maturity structure of borrowing will be:

Maturity structure of borrowing	Upper Limit %	Lower Limit %
- Loans maturing within 1 year	50	0
- Loans maturing within 1 - 2 years	50	0
- Loans maturing within 2 - 5 years	50	0
- Loans maturing within 5 - 10 years	50	0
- Loans maturing in over 10 years	100	100

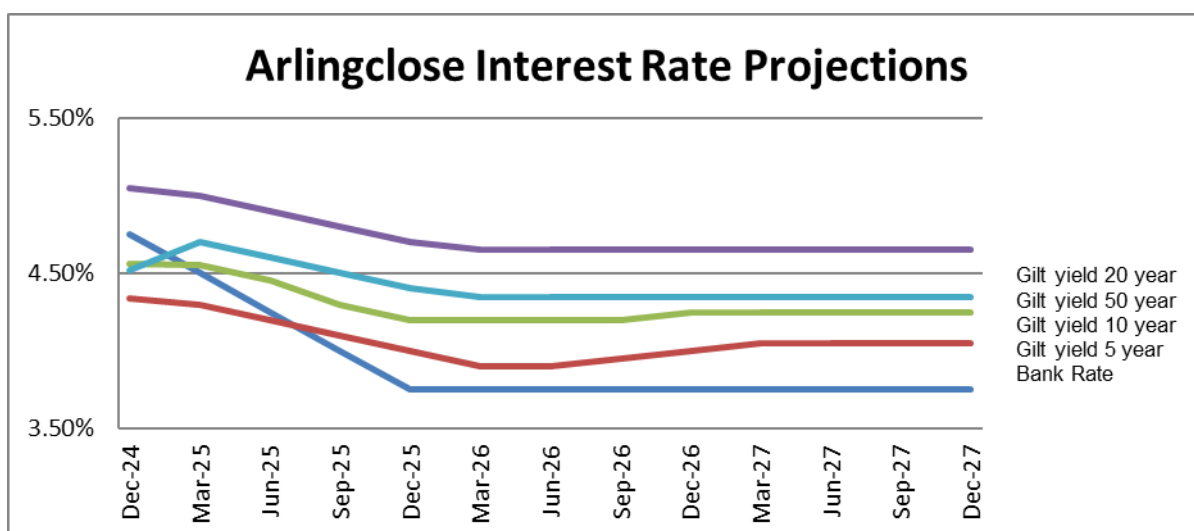
55. Time periods start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment.
56. *Treasury Management Prudential Indicator 4 - Housing Revenue Account (HRA) ratios*: As a result of the HRA Reforms in 2012, the Council moved from a subsidy system to self-financing and was required to take on **£49.3 million** of debt. The table below shows additional local indicators relating to the HRA in respect of this debt.

	2024/25 Revised	2025/26 Estimate	2026/27 Estimate	2027/28 Estimate	2028/29 Estimate
HRA debt £'000	58,268	65,500	55,100	51,600	51,400
HRA revenues £'000	15,606	15,836	16,681	17,500	17,859
Number of HRA dwellings	2,379	2,398	2,468	2,463	2,458
Ratio of debt to revenues	3.73:1	3.55:1	2.82:1	2.69:1	2.63:1
Debt per dwelling £	24,495	27,317	22,328	20,952	20,913
Debt repayment fund £'000	6,840	6,840	0	0	0

57. The HRA is due to repay borrowing from the General Fund of £9.268 million in 2026/27. It is assumed that the debt repayment fund balance of £6.84 million will be used and the balance refinanced.

INTEREST RATE FORECAST

58. The Council's treasury management adviser, Arlingclose, assist the Council to formulate a view on interest rates. The latest detailed economic and interest rate forecast provided by Arlingclose is attached at Annex 1.
59. The following graph and commentary gives the Arlingclose's central view on interest rates.



60. Arlingclose expects the Bank of England's MPC will continue reducing Bank Rate through 2025, taking it to around 3.75% by the end of the 2025/26 financial year. The effect from the Autumn Budget on economic growth and inflation has reduced previous expectations in terms of the pace of rate cuts as well as pushing up the rate at the end of the loosening cycle.
61. Arlingclose expects long-term gilt yields to remain broadly at current levels on average (amid continued volatility), but to end the forecast period modestly lower compared to now. Yields will continue remain relatively higher than in the past, due to quantitative tightening and significant bond supply. As ever, there will be short-term volatility due to economic and (geo)political uncertainty and events.

Other Items

62. The CIPFA Code requires the Council to include the following in its Treasury Management Strategy.
63. **Policy on Apportioning Interest to the HRA:** On 28 March 2012, the Council borrowed £40 million from the Public Works Loan Board (PWLB) to buy itself out of the HRA subsidy System. The monies were borrowed by the General Fund on behalf of the HRA. The interest on these loans is charged to the HRA on a half-yearly basis at the rate charged by PWLB. A further £9.268 million was lent by the General Fund to the HRA to complete the buyout. Interest on this element is charged at the average weighted rate of the PWLB loans.
64. The unfunded HRA capital financing requirement is also charged to the HRA at the average weighted rate of the PWLB loans.
65. The General Fund credits the HRA with interest earned on HRA credit balances calculated on the reserve balances at year end. The rate used is the weighted interest rate on General Fund investments and cash balances.
66. **Markets in Financial Instruments Directive:** The Council has opted up to professional client status with its providers of financial services, including advisers, banks, brokers and fund managers, allowing it access to a greater range of services but without the greater regulatory protections afforded to individuals and small companies. Given the size and range of the Council's treasury management

activities, the Chief Financial Officer believes this to be the most appropriate status.

Financial Implications

67. The budget for net interest received in 2025/26 for the General Fund is £357,300 and the budget for net interest paid in 2025/26 for the HRA is £2,203,000. If actual levels of investments and borrowing, and actual interest rates differ from that forecast, performance against budget will be correspondingly different.
68. **Statutory Override:** In April 2023 the Ministry for Housing, Communities and Local Government (MHCLG) published the full outcome of the consultation on the extension of the statutory override on accounting for **gains and losses on pooled investment funds**. A further consultation on the override was included in MHCLG's annual consultation on the provisional local government finance settlement published in December 2024.
69. The consultation closed on 15th January 2025 with the outcome expecting to be published in February 2025. So far, the override has been extended until 31st March 2025. Whether the override will be extended beyond this date is unknown but commentary from both consultations suggests an extension is unlikely.
70. The Council has invested £12 million in pooled investment funds and has set up a **reserve of £500,000** to mitigate the impact of the statutory override not being extended, as unrealised losses on pooled investment funds are required to be recognised in the General Fund. The actual impact will be based on the valuations of the Council's long term pooled funds on 31 March 2026.

Other Options Considered

71. The CIPFA Code does not prescribe any particular treasury management strategy for local authorities to adopt. The Chief Financial Officer believes that the above strategy represents an appropriate balance between risk management and cost effectiveness. Some alternative strategies, with their financial and risk management implications, are listed below.

Alternative	Impact on income and expenditure	Impact on risk management
Invest in a narrower range of counterparties and/or for shorter times	Interest income will be lower	Lower chance of losses from credit related defaults, but any such losses may be greater
Invest in a wider range of counterparties and/or for longer times	Interest income will be higher	Increased risk of losses from credit related defaults, but any such losses may be smaller
Borrow additional sums at long-term fixed interest rates	Debt interest costs will rise; this is unlikely to be offset by higher investment income	Higher investment balance leading to a higher impact in the event of a default; however long-term interest costs may be more certain
Borrow short-term or variable loans instead of long-term fixed rates	Debt interest costs will initially be lower	Increases in debt interest costs will be broadly offset by rising investment

		income in the medium term, but long-term costs may be less certain
Reduce level of borrowing	Saving on debt interest is likely to exceed lost investment income	Reduced investment balance leading to a lower impact in the event of a default; however long-term interest costs may be less certain

INVESTMENT STRATEGY

- 72. The Council invests its money for three broad purposes:
 - because it has surplus cash as a result of its day-to-day activities, for example when income is received in advance of expenditure (known as **treasury management investments**),
 - to support local public services by lending to or buying shares in other organisations (**service investments**), and
 - to earn investment income (known as **commercial investments** where this is the main purpose).
- 73. This investment strategy meets the requirements of statutory guidance issued by the Government in January 2018 and focuses on the third of these categories.
- 74. The Council does not currently have any service investments.

COMMERCIAL INVESTMENTS

- 75. The Council invests in local and some regional UK commercial property with the intention of making a profit that will be spent on local public services.
- 76. Since the Executive approval of a Commercial Property Investment Acquisition Strategy in January 2013, the Council has purchased commercial investment properties currently valued at **£33.6 million** and expected to generate rental income of £2.6 million during 2025/26.

Property Type	Current Value £'000
Retail	20,570
Commercial (Industrial)	11,160
Other (Healthcare)	1,830
Total	33,560

- 77. The Council’s total Commercial property portfolio, shown below, is valued at **£66.5 million** and includes Faretec and industrial estates at Palmerston Business Park and Newgate Lane. The Council purchased the leasehold of Fareham Shopping Centre at the end of September 2023. The table includes the freehold value only.

Property Type	Current Value £'000
Retail	32,025
Commercial	23,756
Other	4,217
Office	4,925
Leisure	1,536
Total	66,459

78. A fair value assessment of the Council's more recent commercial property purchases has been made within the past twelve months, and the underlying assets provide security for capital investment.
79. The Council assesses the risk of loss before entering into and whilst holding property investments. These risks are managed by ensuring:
- funds available for new purchases are disaggregated to limit the overall impact that any single investment would have on the Council's finances;
 - there is a mix of property types in the portfolio e.g. retail, industrial, etc.;
 - new purchases are only considered with existing tenants of "high quality" and sufficiently long tenancy term;
 - appropriate checks are carried out to ascertain the tenant's reliability;
 - other "due diligence" is undertaken to protect the Council's investment as far as possible such as checks on planning conditions, land contamination issues and planning policy issues.

Proportionality

80. The Council is dependent on profit generating investment activity to achieve a balanced revenue budget. The table below shows the extent to which the expenditure planned to meet the service delivery objectives is dependent on achieving the expected net profit from investments over the lifecycle of the Medium-Term Financial Strategy.

£'000	2023/24 Actual	2024/25 Revised	2025/26 Estimate	2026/27 Estimate	2027/28 Estimate	2028/29 Estimate
Gross service expenditure	47,815	49,482	49,207	49,352	49,680	49,787
Investment income	5,263	5,052	5,002	5,002	5,002	5,002
Proportion	11.0%	10.2%	10.2%	10.1%	10.1%	10.0%

INVESTMENT INDICATORS

81. The Council has set the following three investment indicators to assess the Council's total risk exposure as a result of its investment decisions.
82. *Investment Indicator 1 - Total risk exposure:* The first indicator shows the Council's total exposure to potential investment losses.

£'000	2023/24 Actual	2024/25 Estimate	2025/26 Estimate
Treasury Management Investments	13,588	15,000	15,000
Commercial Investments	66,459	66,459	66,459
Total	80,047	81,459	81,459

83. *Investment Indicator 2 - How investments are funded:* Government guidance is that these indicators should include how investments are funded. Since the Council does not normally associate particular assets with particular liabilities, this guidance is difficult to comply with. However, the following investments could be described as being funded by borrowing. The remainder of the Council's investments are funded by usable reserves and income received in advance of expenditure.

£'000	2023/24 Actual	2024/25 Estimate	2025/26 Estimate
Treasury Management Investments	0	0	0
Commercial Investments	28,663	27,823	26,958
Total	29,479	27,823	26,958

84. *Investment Indicator 3 - Rate of return received:* This indicator shows the investment income received less the associated costs, including the cost of borrowing where appropriate, as a proportion of the sum initially invested.

	2023/24 Actual	2024/25 Estimate	2025/26 Estimate
Treasury Management Investments	3.9%	1.7%	1.8%
Commercial Investments	3.8%	4.0%	3.8%
Total	3.8%	3.5%	3.4%

CAPACITY AND SKILLS

Training

85. The CIPFA 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.
86. Treasury management officers regularly attend training courses, seminars and conferences provided by the Council's treasury management advisers and CIPFA.
87. Property services officers also regularly attend training courses, seminars and conferences provided RICS (Royal Institution of Chartered Surveyors) accredited/approved providers.

Use of Treasury Management Consultants

88. The Council has appointed Arlingclose as treasury management advisers and receives specific advice on investment, debt and capital finance issues.
89. 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 our external service providers.
90. 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.

ARLINGCLOSE ECONOMIC AND INTEREST RATE FORECAST

Economic Background – January 2025

The impact on the UK from the government's Autumn Budget, slower expected interest rate cuts, a short-term boost to but modestly weaker economic growth over the medium term, together with the impact from President-elect Trump's second term in office and uncertainties around US domestic and foreign policy, will be major influences on the Authority's treasury management strategy for 2025/26.

The Bank of England's (BoE) Monetary Policy Committee (MPC) held Bank Rate at 4.75% at its December 2024 meeting, having reduced it to that level in November and following a previous 25bp cut from the 5.25% peak at the August MPC meeting. At the December meeting, six Committee members voted to maintain Bank Rate at 4.75% while three members preferred to reduce it to 4.50%.

The November quarterly Monetary Policy Report (MPR) expected Gross Domestic Product (GDP) growth to pick up to around 1.75% (four-quarter GDP) in the early period of the BoE's forecast horizon before falling back. The impact from the Budget pushes GDP higher in 2025 than was expected in the previous MPR, before becoming weaker. Current GDP growth was shown to be zero (0.0%) between July and September 2024 and 0.4% between April and June 2024, a further downward revision from the 0.5% rate previously reported by the Office for National Statistics (ONS).

ONS figures reported the annual Consumer Price Index (CPI) inflation rate at 2.6% in November 2024, up from 2.3% in the previous month and in line with expectations. Core CPI also rose, but by more than expected, to 3.6% against a forecast of 3.5% and 3.3% in the previous month. The outlook for CPI inflation in the November MPR showed it rising above the MPC's 2% target from 2024 into 2025 and reaching around 2.75% by the middle of calendar 2025. This represents a modest near-term increase due to the ongoing impacts from higher interest rates, the Autumn Budget, and a projected margin of economic slack. Over the medium-term, once these pressures ease, inflation is expected to stabilise around the 2% target.

The labour market appears to be easing slowly, but the data still require treating with some caution. The latest figures reported the unemployment rate rose to 4.3% in the three months to October 2024 and economic inactivity fell to 21.7%. Pay growth for the same period was reported at 5.2% for both regular earnings (excluding bonuses) and for total earnings. Looking ahead, the BoE MPR showed the unemployment rate is expected to increase modestly, rising to around 4.5%, the assumed medium-term equilibrium unemployment rate, by the end of the forecast horizon.

The US Federal Reserve has continued cutting interest rates, bringing down the Fed Funds Rate by 0.25% at its December 2024 monetary policy meeting to a range of 4.25%-4.50%, marking the third consecutive reduction. Further interest rate cuts are expected, but uncertainties around the potential inflationary impact of incoming President Trump's policies may muddy the waters in terms of the pace and magnitude of further rate reductions. Moreover, the US economy continues to expand at a decent pace, rising at an (upwardly revised) annual rate of 3.1% in the third quarter of 2024, and inflation remains elevated suggesting that monetary policy may need to remain more restrictive in the coming months than had previously been anticipated.

Euro zone inflation rose above the European Central Bank (ECB) 2% target in November 2024, hitting 2.2% as was widely expected and a further increase from 2% in the previous month. Despite the rise, the ECB continued its rate cutting cycle and reduced its three key policy rates by 0.25% in December. Inflation is expected to rise further in the short term, but then fall back towards the 2% target during 2025, with the ECB remaining committed to maintaining rates at levels consistent with bringing inflation to target, but without suggesting a specific path.

Credit outlook:

Credit Default Swap (CDS) prices have typically followed a general trend downwards during 2024, reflecting a relatively more stable financial period compared to the previous year. Improved credit conditions in 2024 have also led to greater convergence in CDS prices between ringfenced (retail) and non-ringfenced (investment) banking entities again.

Higher interest rates can lead to a deterioration in banks' asset quality through increased loan defaults and volatility in the value of capital investments. Fortunately, the rapid interest rate hikes during this monetary tightening cycle, while putting some strain on households and corporate borrowers, has not caused a rise in defaults, and banks have fared better than expected to date, buoyed by strong capital positions. Low unemployment and robust wage growth have also limited the number of problem loans, all of which are positive in terms of creditworthiness.

Moreover, while a potential easing of US financial regulations under a Donald Trump Presidency may aid their banks' competitiveness compared to institutions in the UK and other regions, it is unlikely there will be any material impact on the underlying creditworthiness of the institutions on the counterparty list maintained by Arlingclose, the authority's treasury adviser.

Overall, the institutions on our adviser Arlingclose's counterparty list remain well-capitalised and their counterparty advice on both recommended institutions and maximum duration remain under constant review and will continue to reflect economic conditions and the credit outlook.

Underlying assumptions:

- As expected, the Monetary Policy Committee (MPC) held Bank Rate at 4.75% in December, although, with a 6-3 voting split and obvious concerns about economic growth, presented a much more dovish stance than had been expected given recent inflationary data.
- The Budget measures remain a concern for policymakers, for both growth and inflation. Additional government spending will boost demand in a constrained supply environment, while pushing up direct costs for employers. The short to medium-term inflationary effects will promote caution amongst policymakers.
- UK GDP recovered well in H1 2024 from technical recession, but underlying growth has petered out as the year has progressed. While government spending should

boost GDP growth in 2025, private sector activity appears to be waning, partly due to Budget measures.

- Private sector wage growth and services inflation remain elevated; wage growth picked up sharply in October. 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 rates have risen due to higher energy prices and less favourable base effects. The current CPI rate of 2.6% could rise further in Q1 2025. The Bank of England (BoE) estimates the CPI rate at 2.7% by year end 2025 and to remain over target in 2026.
- The MPC re-emphasised that monetary policy will be eased gradually. Despite recent inflation-related data moving upwards or surprising to the upside, the minutes suggested a significant minority of policymakers are at least as worried about the flatlining UK economy.
- US government bond yields have risen following strong US data and uncertainty about the effects of Donald Trump's policies on the US economy, particularly in terms of inflation and monetary policy. The Federal Reserve pared back its expectations for rate cuts in light of these issues. Higher US yields are also pushing up UK gilt yields, a relationship that will be maintained unless monetary policy in the UK and US diverges.

Forecast:

- In line with our forecast, Bank Rate was held at 4.75% in December.
- The MPC will reduce Bank Rate in a gradual manner. We see a rate cut in February 2025, followed by a cut alongside every 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 will 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.
- The risks around the forecasts lie to the upside over the next 12 months but are broadly balanced in the medium term.