Appendix 1

# MERTHYR TYDFIL COUNTY BOROUGH COUNCIL

Cyngor Bwrdeistref Sirol
MERTHYR TUDFUL
MERTHYR TYDFIL
County Borough Council

# MEDIUM TERM FINANCIAL PLAN

# 2024/25 - 2026/27

**April 2024**

## 1.0 Introduction

1.1 Local Government is faced with significant demanding future challenges in marrying corporate and service expenditure plans and priorities to scarce available financial resources. It is imperative that Merthyr Tydfil County Borough Council (MTCBC) recognizes these challenges and aligns budgets and spending plans to corporate priorities through the implementation of a robust rolling programme Medium Term Financial Plan (MTFP) continuously updated to consider changing circumstances, future demands, priorities and initiatives. Consequently, regular reporting to Corporate Management Team, Cabinet, Governance and Audit Committee, Scrutiny Committees and Council is both desirable and essential.

1.2 A meaningful, continuously updated MTFP has the following advantages:

- Informs the budget process.
- Allows timely recognition of future budget pressures, minimising unforeseen demands.
- Allows budget decisions to be based on priorities rather than the requirement to arbitrarily reduce costs.
- Supports earlier budget setting since financial decisions are being recommended earlier in the year.
- Supports integration of Council plans and policies.

1.3 To ensure ownership of the MTFP by all stakeholders, for example members, senior management, service managers and finance professionals', the MTFP must be a meaningful tool in informing effective decision making and financial planning.

1.4 A meaningful MTFP should be fully integrated to aid financial planning and corporate decision making. The following are considered within the Council's MTFP for 2024/25 to 2026/27:

- Section 2 – Corporate Wellbeing Objectives
- Section 3 – Asset Management Plan
- Section 4 – Healthy Organisation Plan
- Section 5 – Financial Context
- Section 6 – Revenue Budget
- Section 7 – Capital Programme / Capital Strategy
- Section 8 – Reserves Strategy
- Section 9 – Treasury Management

## 2.0 Financial Context

### Introduction

2.1 This MTFP has been prepared against a backdrop of increasing concerns about the financial sustainability of Welsh local authorities, with unprecedented increases in Council Tax and significant use of Earmarked Reserves across Wales required to set balanced budgets for 2024/25.

2.2 Meanwhile, the Welsh Government has described its budgetary position as "the most difficult financial situation since the dawn of devolution". Spending pressures have outstripped the growth in local government revenues in the last two years despite significant nominal terms increases in funding from Welsh Government. A key driver has been substantial pay increases for local government staff and teachers, despite many workers still seeing real terms pay cuts.

2.3 Based on current, indicative UK government spending plans, the Welsh Government's resource budget is set to increase by just 0.8% per year on average between 2024-25 and 2027-28 (in real terms). Beyond increasing health, schools, and childcare spending, we estimate the Welsh Government will need to find cuts of over £300 million in cash terms by 2027-28 in all other spending areas.

2.4 While the economic and fiscal context could radically change, projections of spending pressures and funding suggest there could be significant reductions in local services over coming years. With the current UK government and opposition Labour party refusing to commit to additional spending on public services, the Welsh Government and local authorities must now weigh up the difficult choices that may lie ahead.

### The Challenge Ahead

2.5 Based on the projections determining the MTFP, the Council is faced with significant challenges in addressing the projected budget deficits over the term of the MTFP. Transformation initiatives are critical in ensuring the financial sustainability of the Council and providing assurance to all stakeholders (including Welsh Government and Audit Wales) that the Council can confidently respond to both current and future financial challenges.

2.6 The Transformation Programme will build upon the principles of the Council's Recovery, Transformation and Improvement (RTI) Plan in identifying sustainable efficiency savings whilst recognising the priorities within the RTI Plan. In addition, it is recognised that up-front investment may also be required to drive change providing both quantitative and qualitative opportunities as follows:

- Quantitative – efficiency savings and cost avoidance opportunities through investment in preventative initiatives
- Qualitative – increased performance, service improvement and risk mitigation

## 3.0 Revenue Medium-Term Financial Plan

3.1 A recap of the 2024/25 budget approved at the Special Council meeting on March 6th is included below.

| Area | 2024/25 Budget £'000 (Agreed) |
|---|---|
| Education | 62,877 |
| Social Services | 48,191 |
| Economy & Public Protection | 9,626 |
| Neighbourhood Services | 12,110 |
| Governance & Resources | 8,724 |
| Corporate Authority | 24,065 |
| Non-General Fund Allocations | -935 |
| Discretionary NDR Relief | 44 |
| Collection Fund Surplus | -700 |
| Corporate Vacancy Factor | -1,000 |
| In-Year Savings | -71 |
| Use of Reserves | -2,032 |
| **Net Expenditure** | **160,899** |
| | |
| Revenue Settlement | -123,492 |
| Council Tax | -37,407 |
| | |
| **Net Income** | **-160,899** |
| | |
| **Budget Deficit** | **0** |

3.2 Given the amount of savings proposals proposed to achieve a balanced budget for 2024/25, it was not possible to produce a Medium-Term Financial Plan in the timeframes required for setting Council Tax.

3.3 That work has now been carried out for the remaining period of the Medium-Term Financial Plan, and a summary of that information is included in the table below:

| **Area** | **2025/26 Budget £'000** | **2026/27 Budget £'000** |
|---|---|---|
| Education | 66,145 | 67,469 |
| Social Services | 52,539 | 55,394 |
| Economy & Public Protection | 11,264 | 11,493 |
| Neighbourhood Services | 12,807 | 13,258 |
| Governance & Resources | 9,230 | 9,511 |
| Corporate Authority | 25,520 | 26,726 |
| Non-General Fund Allocations | -935 | -935 |
| Discretionary NDR Relief | 44 | 44 |
| Collection Fund Surplus | -850 | -850 |
| Corporate Vacancy Factor | -1,500 | -1,500 |
| Pension Strain | 247 | 247 |
| **Net Expenditure** | **174,511** | **180,854** |
| | | |
| Revenue Settlement | -126,456 | -129,491 |
| Council Tax | -39,277 | -41,241 |
| | | |
| **Net Income** | **-165,733** | **-170,732** |
| | | |
| **Budget Deficit** | **8,778** | **10,122** |

3.4 The table above indicates that a budget deficit of £8.778 million is projected for 2025/26 and a cumulative budget deficit of £18.900 million is projected for the period of the MTFP. A further breakdown of directorate budgets is included as Appendix A.

3.5 The key data underpinning the 2025/26 and 2026/27 aspects of the MTFP are summarised below:

- A Revenue Settlement of +2.4%
- A Pay Award of +2.3
- A Council Tax increase of 5% per annum
- No utilisation of Reserves from 2025/26 onwards

3.6 It is clear that the Council continues to face significant financial challenges over the course of the medium-term and an ongoing programme of transformation will be required to achieve the levels of saving required. Further reports will be brought to Council in due course.

## 4.0 Capital Programme / Capital Strategy

4.1 The Capital Programme for 2024/25 to 2027/28 was agreed at Council in February 2024 and is summarised in the table below.

| Description | 2024/25 £'000 | 2025/26 £'000 | 2026/27 £'000 | 2027/28 £'000 | Total £'000 |
|---|---|---|---|---|---|
| **Capital Expenditure** | | | | | |
| Education | 5,602 | 15,487 | 2,998 | 3,119 | 27,206 |
| Physical Regeneration | 1,050 | 900 | 900 | 900 | 3,750 |
| Transport Infrastructure | 4,719 | 3,881 | 3,881 | 3,881 | 16,362 |
| Land and Buildings | 2,807 | 1,346 | 450 | 450 | 5,053 |
| Miscellaneous | 3,180 | 3,205 | 2,170 | 2,170 | 10,725 |
| **Total** | **17,358** | **24,819** | **10,399** | **10,520** | **63,096** |
| **Financed By** | | | | | |
| Borrowing | 15,258 | 22,719 | 8,299 | 8,420 | 54,696 |
| Capital Grants | 1,600 | 1,600 | 1,600 | 1,600 | 6,400 |
| Capital Receipts | 500 | 500 | 500 | 500 | 2,000 |
| **Total** | **17,358** | **24,819** | **10,399** | **10,520** | **63,096** |

4.2 A significant amount of additional capital investment is supported by external providers such as Welsh Government, and Heritage Lottery Fund demonstrating the Council's ability to attract and successfully bid for external capital funding.

4.3 The Council currently has a number of medium to long term capital commitments linked to its Corporate Priorities and Corporate Risk Register and supported by its Asset Management Plans. It is evident that the Council is faced with challenging capital finance constraints but is innovative and effective in securing external funding and working with partners to support its capital investment ambitions.

4.4 It is recognised that owing to funding restrictions there are a number of potential significant projects currently not included within the proposed Capital Programme which may result in further urgent requests for capital funding during 2024/25.

4.5 Capital investment decisions will significantly impact on the net revenue expenditure of the Council especially in terms of capital financing costs (repayment of borrowing to finance expenditure on capital projects) and future running and maintenance costs of new fixed assets. Capital expenditure financed by unsupported borrowing through the Prudential Code framework for Capital Finance included in the period of the Capital Programme equates to £40.468 million.

4.6 Unlike supported borrowing through General Capital Funding, the capital financing costs associated with unsupported borrowing is not included within the Council's Revenue Support Grant received from Welsh Government. Instead through Prudential Indicators the Council is required to ensure the capital spending plans are affordable, prudent and sustainable.

4.7 Capital option appraisals are required to be formally adopted to assist with decisions involving the allocation of scarce resources to competing projects and/or priorities in establishing the full-life costs of the proposals. Once a capital project is approved the Council is also making a commitment towards the ongoing revenue running costs associated with the asset. The appraisal will take account of both quantitative and qualitative criteria and links to the Council's Asset Management Plan.

4.8 The Capital Strategy is a new report introduced by the 2017 edition of the Prudential Code which is intended to give a high level, concise and comprehensible overview to all elected members of how capital expenditure, capital financing and treasury management activity contribute to the provision of the Authority's services. This report should also provide an overview of the associated risk, its management and the implications for future financial sustainability.

The areas to be covered in this strategy are:

- Capital Expenditure and Financing
- Treasury Management
- Investments for Service Purposes
- Commercial Activities
- Liabilities
- Revenue Budget Implications
- Knowledge and skills

The Capital Strategy Report for 2024/25 is appended as Appendix B.

## 5.0 Treasury Management

5.1 The Council's Treasury Management Strategy Statement for 2024/25 is appended as Appendix C. The Prudential Indicators included within the Policy, ensure that the Council's borrowing and investment plans included within the MTFP are affordable, prudent and sustainable.

5.2 Appendix C reflects the proposed Minimum Revenue Provision Statement for 2024/25.

5.3 A Treasury Outturn Statement for 2023/24 and a Mid-Year Treasury Statement for 2024/25 will be reported to Council during the 2024/25 financial year.

5.4 If appropriate, revised Prudential Indicators may be reported to Council during 2024/25 in the event of unforeseen circumstances such as greater than projected borrowing or potential breach of borrowing limits.

**Appendix A**

## Medium Term Financial Plan 2025/25 & 2026/27

## Corporate Summary

| Description | 2025/26 £'000 | 2026/27 £'000 |
|---|---|---|
| **Education** | | |
| Individual Schools Budget | 52,086 | 53,238 |
| Strategic Management & Support | 312 | 319 |
| School Planning Support & Resources | 5,934 | 5,936 |
| Additional Learning Needs & Inclusion | 7,456 | 7,615 |
| Achievement & Wellbeing | 357 | 361 |
| **Total** | **66,145** | **67,469** |
| **Social Services** | | |
| Business Support | 404 | 418 |
| Early Intervention & Assistance | 216 | 217 |
| Collaborative Partnerships | 1,260 | 1,303 |
| Adult Social Care | 485 | 514 |
| Assessment & Care Management | 1,523 | 1,566 |
| Initial Support Services | 2,093 | 2,307 |
| Supported & Accommodation Services | 3,379 | 3,483 |
| Day Care Services | 1,813 | 1,862 |
| Independent External Care Provision | 22,763 | 24,657 |
| Children's Social Care | 507 | 523 |
| Children with Disabilities | 792 | 796 |
| Children Looked After | 11,933 | 11,962 |
| Intake & Family Support Services | 4,012 | 4,133 |
| Safeguarding | 705 | 722 |
| Social Services Grant | -502 | -255 |
| Early Years & Youth Management | 1,091 | 1,117 |
| Adult Community Learning | 65 | 69 |
| **Total** | **52,539** | **55,394** |

# Medium Term Financial Plan 2025/26 & 2026/27

## Corporate Summary

| Description | 2025/26 £'000 | 2026/27 £'000 |
|---|---|---|
| **Neighbourhood Services** | | |
| Bereavement Services | 191 | 198 |
| Grounds Maintenance | 1,805 | 1,854 |
| Street Cleansing | 1,363 | 1,413 |
| Fleet Management | 161 | 173 |
| Waste Management | 5,519 | 5,727 |
| Highways & Engineering | 3,210 | 3,307 |
| Planning | 558 | 586 |
| **Total** | **12,807** | **13,258** |
| **Economy and Public Protection** | | |
| Community Regeneration | 376 | 410 |
| Creditors | 163 | 167 |
| Procurement | 389 | 402 |
| Employability & worklessness | 176 | 181 |
| Public Protection | 5,206 | 5,317 |
| Emergency Planning | 129 | 132 |
| Leisure | 2,546 | 2,548 |
| Corporate Property & Estates | 2,279 | 2,336 |
| **Total** | **11,264** | **11,493** |
| **Governance and Resources** | | |
| Corporate Services | 721 | 740 |
| Finance | 5,202 | 5,380 |
| Legal | 1,913 | 1,950 |
| Human Resources | 1,015 | 1,050 |
| Corporate Communications | 379 | 391 |
| **Total** | **9,230** | **9,511** |

## Medium Term Financial Plan 2025/26 & 2026/27

## Corporate Summary

| Description | 2025/26 £'000 | 2026/27 £'000 |
|---|---|---|
| **Corporate Costs** | | |
| Corporate Management | 1,125 | 1,159 |
| Capital Financing Costs | 10,333 | 10,446 |
| Council Tax Reduction Scheme | 7,763 | 8,349 |
| Levies | 4,051 | 4,132 |
| Contribution to Pensions | 442 | 442 |
| External Audit Fees | 343 | 343 |
| Insurances | 936 | 1,315 |
| Apprenticeship Levy | 365 | 376 |
| Other | 162 | 164 |
| **Total** | **25,520** | **26,726** |
| **Other** | | |
| Contributions / Recharges | -3,241 | 3,241 |
| Pension Strain | 247 | 247 |
| **Total** | **2,994** | **2,994** |
| | | |
| **Net Expenditure** | **178,646** | **180,854** |
| Revenue Settlement | -126,456 | -129,491 |
| Council Tax Levy | -39,277 | -41,241 |
| **Projected Budget Deficit** | **8,778** | **10,122** |

**Appendix B**

## Merthyr Tydfil County Borough Council

## Capital Strategy Report 2024/25

### 1.0 Introduction

1.1 This capital strategy report gives a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of local public services along with an overview of how associated risk is managed and the implications for future financial sustainability. It has been written in an accessible style to enhance members' understanding of these sometimes technical areas.

1.2 Decisions made this year on capital and treasury management will have financial consequences for the Authority for many years into the future. They are therefore subject to both a national regulatory framework and to local policy framework, summarised in this report.

### 2.0 Capital Expenditure and Financing

2.1 Capital expenditure is where the Authority spends money on assets, such as property or vehicles that will be used for more than one year. In local government this includes spending on assets owned by other bodies, and loans and grants to other bodies enabling them to buy assets. The Authority has some limited discretion on what counts as capital expenditure, for example assets costing below £10,000 are not capitalised and are charged to revenue in year.

2.2 In 2024/25, the Authority is planning capital expenditure of £69.425 million as summarised below:

Table 1: Prudential Indicator Estimates of Capital Expenditure

| | 2022/23 Actual £'000 | 2023/24 Forecast £'000 | 2024/25 Budget £'000 | 2025/26 Budget £'000 | 2026/27 Budget £'000 |
|---|---|---|---|---|---|
| **General Fund Services** | 38,478 | 62,726 | 69,425 | 49,016 | 15,452 |
| **TOTAL** | **38,478** | **62,726** | **69,425** | **49,016** | **15,452** |

* £6.155m of capital expenditure in 2024/25 arises from a change in the accounting for leases and does not represent cash expenditure.

2.3 The main General Fund capital projects include:

- The Sustainable Communities for Learning (SCfL) Programme - The Current programme totals £96 million over the four years of the Capital Medium Term Financial plan, with a total contribution of £21 million as match from the Council.
- The Authority’s Physical Regeneration Programme for the Council requires a financial commitment of £1.050 million from the Authority in 2024/25. This also provides the opportunity for the Authority to secure external funding to deliver projects.
- Transport and Infrastructure costs of £4.719 million have been included in the 2024/25 financial year.
- Expenditure on Land, Buildings and Miscellaneous Schemes of £4.787 million have been included for the 2024/25 financial year.

2.4 Service managers bid annually to include projects in the Authority’s capital programme. However, due to pressures on revenue budgets, the capital programme has been reviewed and only projects deemed critical by services managers have been included. Some projects have been removed from the Capital Programme for or re-profiled into future years. The capital programme was considered at Cabinet in February 2024 and is then presented to Council in February/March each year.

  - The Authority’s capital programme was reported to both Cabinet and Council on 21st February 2024.

2.5 All capital expenditure must be financed, either from external sources (government grants and other contributions), the Authority’s own resources (revenue, reserves and capital receipts) or debt (borrowing and leasing). The planned financing of the above expenditure is as follows:

Table 2: Capital Financing

| | 2022/23 Actual £'000 | 2023/24 Forecast £'000 | 2024/25 Budget £'000 | 2025/26 Budget £'000 | 2026/27 Budget £'000 |
|---|---|---|---|---|---|
| **External Sources** | 21,796 | 37,387 | 53,667 | 25,797 | 6,653 |
| **Own Resources** | 490 | 665 | 500 | 500 | 500 |
| **Debt** | 16,192 | 24,674 | 15,258 | 22,719 | 8,299 |
| **TOTAL** | **38,478** | **62,726** | **69,425** | **49,016** | **15,452** |

* £6.155 m of debt financing in 2024/25 arises from a change in the accounting for leases and does not represent cash expenditure.

2.6 Debt is only a temporary source of finance, since loans and leases must be repaid, and this is therefore replaced over time by other financing, usually from revenue which is known as the minimum revenue provision (MRP). Alternatively, proceeds from selling capital assets (known as capital receipts) may be used to replace debt finance. Planned MRP and use of capital receipts are as follows:

Table 3: Replacement of debt finance

| | 2022/23 Actual £'000 | 2023/24 Forecast £'000 | 2024/25 Budget £'000 | 2025/26 Budget £'000 | 2026/27 Budget £'000 |
|---|---|---|---|---|---|
| **Own Resources** | 2,291 | 2,598 | 4,025 | 4,379 | 4,646 |
| **TOTAL** | **2,291** | **2,598** | **4,025** | **4,379** | **4,646** |

- The Authority's full minimum revenue provision statement will be reported to Council on 6th March 2024.

2.7 The Authority's cumulative outstanding amount of debt finance is measured by the capital financing requirement (CFR). This increases with new debt-financed capital expenditure and reduces with MRP and capital receipts used to replace debt. The CFR is expected to increase by £17 million during 2024/25. Based on the above figures for expenditure and financing, the Council's estimated CFR is as follows:

Table 4: Prudential Indicator Estimates of Capital Financing Requirement

| | 2022/23 Actual £'000 | 2023/24 Forecast £'000 | 2024/25 Budget £'000 | 2025/26 Budget £'000 | 2026/27 Budget £'000 |
|---|---|---|---|---|---|
| **General Fund Services** | 129,829 | 152,454 | 169,842 | 188,285 | 192,041 |
| **TOTAL CFR** | **129,829** | **152,454** | **169,842** | **188,285** | **192,041** |

2.8 **Asset management:** To ensure that capital assets continue to be of long-term use, the Council has an asset management plan in place. The plan sets out the vision for asset management where the property portfolio is aligned to corporate priorities and service requirements, appropriate investment is made in capital projects and the portfolio is efficiently maintained, is fit for purpose and meets health and safety requirements.

**Asset disposals:** When a capital asset is no longer needed, it may be sold so that the proceeds, known as capital receipts, can be spent on new assets or to repay debt. The Authority is currently also permitted to spend capital receipts "flexibly" on service transformation projects until 2024/25. Repayments of capital grants, loans and investments also generate capital receipts. The Authority plans to receive £500,000 of capital receipts in the coming financial year as follows:

Table 5: Capital Receipts

| | 2022/23 Actual £'000 | 2023/24 Forecast £'000 | 2024/25 Budget £'000 | 2025/26 Budget £'000 | 2026/27 Budget £'000 |
|---|---|---|---|---|---|
| **Asset sales** | 0 | 500 | 500 | 500 | 500 |
| **TOTAL** | **0** | **500** | **500** | **500** | **500** |

## 3.0 Treasury Management

3.1 Treasury management is concerned with keeping sufficient but not excessive cash available to meet the Authority's spending needs, while managing the risks involved. Surplus cash is invested until required, while a shortage of cash will be met by borrowing, to avoid excessive credit balances or overdrafts in the bank current account. The Authority is typically cash rich in the short-term as revenue income is received before it is spent, but cash poor in the long-term as capital expenditure is incurred before being financed. The revenue cash surpluses are offset against capital cash shortfalls to reduce overall borrowing.

Due to decisions taken in the past, the Authority currently has £129 million borrowing at an average interest rate of 4.57% and £13 m treasury investments at an average rate of 4.50% (as at December 2023).

3.2 **Borrowing strategy:** The Authority's main objectives when borrowing are to achieve a low but certain cost of finance while retaining flexibility should plans change in future. These objectives are often conflicting, and the Authority therefore seeks to strike a balance between cheap short-term loans and long-term fixed rate loans where the future cost is known but higher.

The Authority does not borrow to invest for the primary purpose of financial return and therefore retains full access to the Public Works Loans Board.

Projected levels of the Authority's total outstanding debt (which comprises borrowing and leases) are shown below, compared with the capital financing requirement (see above).

Table 6: Prudential Indicator: Gross Debt and the Capital Financing Requirement

| | 2022/23 Actual £'000 | 2023/24 Forecast £'000 | 2024/25 Budget £'000 | 2025/26 Budget £'000 | 2026/27 Budget £'000 |
|---|---|---|---|---|---|
| **Debt** | 126,542 | 138,597 | 157,736 | 177,305 | 181,992 |
| **Capital Financing Requirement** | 129,829 | 152,454 | 169,842 | 188,285 | 192,041 |

Statutory guidance is that debt should remain below the capital financing requirement, except in the short-term. As can be seen from table 6, the Authority expects to comply with.

3.3 **Liability benchmark:** To compare the Authority's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing. This assumes that cash and investment balances are kept to a minimum level of £10 m at each year-end. This benchmark is currently projected at £140 m and is forecast to rise to £181 m over the next three years.

Table 7: Borrowing and the Liability Benchmark

| | 2022/23 Actual £'000 | 2023/24 Forecast £'000 | 2024/25 Budget £'000 | 2025/26 Budget £'000 | 2026/27 Budget £'000 |
|---|---|---|---|---|---|
| **Forecast Borrowing** | 126,542 | 138,597 | 157,736 | 177,305 | 181,992 |
| **Liability Benchmark** | 107,806 | 140,643 | 158,804 | 177,429 | 181,185 |

3.4 **Affordable borrowing limit:** The Authority is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt) each year. In line with statutory guidance, a lower “operational boundary” is also set as a warning level should debt approach the limit.

| | 2023/24 Limit £'000 | 2024/25 Limit £'000 | 2025/26 Limit £'000 | 2026/27 Limit £'000 |
|---|---|---|---|---|
| **Authorised Limit** | 221,828 | 264,594 | 285,283 | 289,715 |
| **Operational Boundary** | 201,681 | 241,002 | 259,734 | 263,697 |

- Further details on borrowing are included within the treasury management strategy statement to be reported to Council on 20th March 2024.

3.5 **Treasury investment strategy:** Treasury investments arise from receiving cash before it is paid out again. Investments made for service reasons or for pure financial gain are not generally considered to be part of treasury management.

The Authority’s policy on treasury investments is to prioritise security and liquidity over yield that is to focus on minimising risk rather than maximising returns. Cash that is likely to be spent in the near term is invested securely, for example with the government, other local authorities or selected high-quality banks and building societies, to minimise the risk of loss.

Table 9: Treasury management investments

| | 2022/23 Actual £'000 | 2023/24 Forecast £'000 | 2024/25 Budget £'000 | 2025/26 Budget £'000 | 2026/27 Budget £'000 |
|---|---|---|---|---|---|
| **Investments** | 28,736 | 10,000 | 10,000 | 10,000 | 10,000 |

- Further details on investments are included within the treasury management strategy statement to be reported to Council on 20th March 2024.

**Risk management:** The effective management and control of risk are prime objectives of the Authority's treasury management activities. The treasury management strategy therefore sets out various indicators and limits to constrain the risk of unexpected losses.

- The treasury management Prudential indicators are included within the treasury management strategy statement to be reported to Council on 20th March 2024.

**Governance:** Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Chief Finance Officer and staff, who must act in line with the treasury management strategy approved by Council. Half yearly reports on treasury management activity are presented to Council.

## 4.0 Investments for Service Purposes

The Authority has an investment (Gellideg Housing Co-operative) made for service purposes which is currently valued at £349,800 (as at 31st March 2023), the terms of the investment are that it is cost neutral for the Authority. A full Council report on the Gellideg Housing Co-operative project was reported on the 25th February 2015. The Council also participates in various Loan schemes including the Empty Homes and Vibrant and Viable Places Loans schemes funded by the Welsh Government.

**Governance:** Decisions on service investments are made by the relevant service manager in consultation with the Chief Finance Officer and are reported to Council.

## 5.0 Commercial Activities

In light of the uncertainty surrounding future Government support through financial settlements, the Authority may look to identify other sources of income for future financial sustainability. At present, the Authority has not invested in any commercial activities.

## 6.0 Liabilities

In addition to debt as at 31st March 2023 of £126.542 m as detailed above, the Authority is committed to making future payments to cover its pension fund deficit (valued at £64.910m). It has also set aside £1.693 m to cover risks of provisions. The Authority is also at risk of having to pay for contingent liabilities however the Authority is not required to set aside any money for these liabilities

- Further details on liabilities and guarantees are on pages 72 and 100 of the 2022/23 statement of accounts, reported to Council on 27th November 2023.

**Governance:** Decisions on incurring new discretional liabilities are taken by service managers/Corporate Management Team in consultation with Chief Finance Officer. The risk of liabilities crystallising and requiring payment is monitored by the finance section.

## 7.0 Revenue Budget Implications

Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP are charged to revenue. The net annual charge is known as financing costs; this is compared to the net revenue stream i.e. the amount funded from Council Tax, business rates and general government grants.

| | 2022/23 Actual £'000 | 2023/24 Forecast £'000 | 2024/25 Budget £'000 | 2025/26 Budget £'000 | 2026/27 Budget £'000 |
|---|---|---|---|---|---|
| **Financing Costs (£'000)** | 6,188 | 7,356 | 10,793 | 11,360 | 11,340 |
| **Proportion of net revenue stream** | **4.3%** | **4.8%** | **6.7%** | **6.9%** | **6.6%** |

- Further details on the revenue implications of capital expenditure are included within the 2024/25 revenue budget reported to Council on 6th March 2024.

**Sustainability:** Due to the very long-term nature of capital expenditure and financing, the revenue budget implications of expenditure incurred in the next few years will extend for up to 50 years plus into the future. The Chief

Finance Officer is satisfied that the proposed capital programme is prudent, affordable and sustainable.

## 8.0 Knowledge and Skills

The Authority employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. For example, the Chief Finance Officer is a qualified accountant with over 10 years' post qualification experience. The Council pays for junior staff to study towards relevant professional qualifications including CIPFA.

Where Authority staff do not have the knowledge and skills required, use is made of external advisers and consultants that are specialists in their field. The Council currently employs Arlingclose Limited as treasury management advisers. This approach is more cost effective than employing such staff directly, and ensures that the Authority has access to knowledge and skills commensurate with its risk appetite.

**Appendix C**
**Merthyr Tydfil County Borough Council**

## Treasury Management Strategy Statement 2024/25

### 1.0 Introduction

1.1 Treasury management is the management of the Authority's cash flows, borrowing and investments, and the associated risks. The Authority has borrowed and invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of financial risk are therefore central to the Authority's prudent financial management.

1.2 Treasury risk management at the Authority is conducted within the framework of the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice 2021 Edition* (the CIPFA Code) which requires the Authority to approve a treasury management strategy before the start of each financial year. In addition, the Welsh Government (WG) issued revised Guidance on Local Authority Investments in November 2019 that requires the Authority to approve an investment strategy before the start of each financial year. This report fulfils the Authority's legal obligation under the *Local Government Act 2003* to have regard to both the CIPFA Code and the WG Guidance.

1.3 **Revised strategy:** In accordance with the WG Guidance, the Authority will be asked to approve a revised Treasury Management Strategy Statement should the assumptions on which this report is based change significantly. Such circumstances would include, for example, a large unexpected change in interest rates, in the Authority's capital programme or in the level of its investment balance, or a material loss in the fair value of a non-financial investment identified as part of the year end accounts preparation and audit process.

### 2.0 External Context

Appendix 1 outlines an Economic Commentary.

## 3.0 Local Context

3.1 On 31st December 2023, the Authority held £129 m of borrowing and £13 m of investments. This is set out in further detail at Appendix 2. Forecast changes in these sums are shown in the balance sheet analysis in table 1 below.

Table 1: Balance sheet summary and forecast

| | 2022/23 Actual £'000 | 2023/24 Forecast £'000 | 2024/25 Budget £'000 | 2025/26 Budget £'000 | 2026/27 Budget £'000 |
|---|---|---|---|---|---|
| **Capital Financing Requirement** | **129,829** | **152,454** | **169,842** | **188,285** | **192,041** |
| Less External Borrowing** | (126,542) | (138,597) | (119,781) | (115,347) | (111,531) |
| Less usable reserves | (38,538) | (28,326) | (27,553) | (27,371) | (27,371) |
| Plus working capital | 14,787 | 14,787 | 14,787 | 14,787 | 14,787 |
| Financial Instruments Adjustment | (8,272) | (8,272) | (8,272) | (8,272) | (8,272) |
| **Investments (or New Borrowing)** | **28,736** | **7,954** | **(29,023)** | **(52,082)** | **(59,654)** |

* leases that form part of the Authority's total debt

** shows only loans to which the Authority is committed and excludes optional refinancing.

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 Authority's current strategy is to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing.

The Authority has an increasing CFR due to the capital programme, but minimal investments and will therefore be required to borrow up to £68 m over the forecast period.

CIPFA's *Prudential Code for Capital Finance in Local Authorities* recommends that the Authority's total debt should be lower than its highest forecast CFR over the next three years. Table 1 shows that the Authority expects to comply with this recommendation.

3.2 **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 same forecasts as table

1 above, but that cash and investment balances are kept to a minimum level of £10m at each year-end to maintain sufficient liquidity but minimise credit risk.

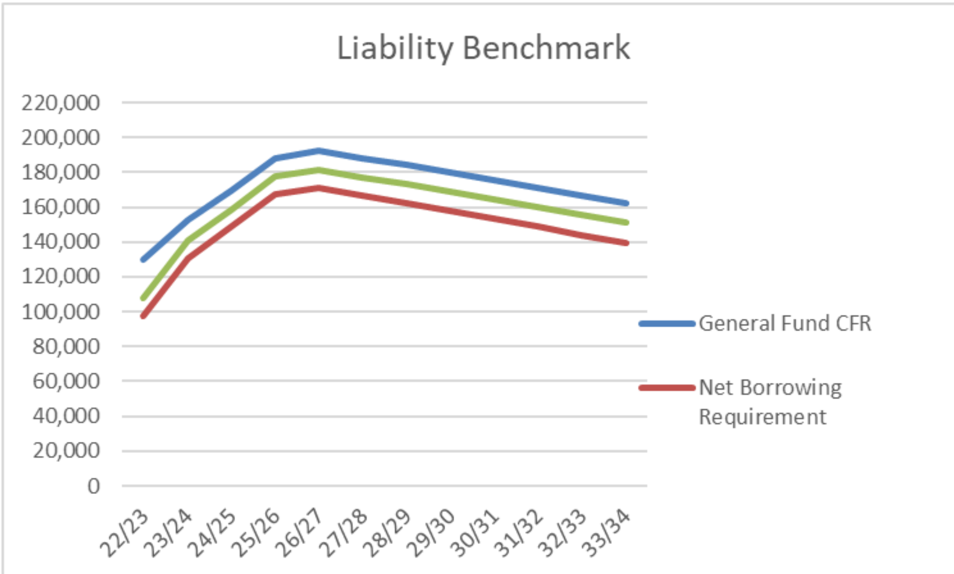
The liability benchmark is an important tool to help establish whether the Council is likely to be a long-term borrower or long-term investor in the future, and so shape its strategic focus and decision making. The liability benchmark itself represents an estimate of the cumulative amount of external 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.

Table 2: Liability benchmark

| | 2022/23 Actual £'000 | 2023/24 Forecast £'000 | 2024/25 Budget £'000 | 2025/26 Budget £'000 | 2026/27 Budget £'000 |
|---|---|---|---|---|---|
| **Capital Financing Requirement** | **129,829** | **152,454** | **169,842** | **188,285** | **192,041** |
| Less usable reserves | (38,538) | (28,326) | (27,553) | (27,371) | (27,371) |
| Plus working capital | 14,787 | 14,787 | 14,787 | 14,787 | 14,787 |
| Plus Minimum Investments | 10,000 | 10,000 | 10,000 | 10,000 | 10,000 |
| Financial Instruments Adjustment | (8,272) | (8,272) | (8,272) | (8,272) | (8,272) |
| **Liability Benchmark** | **107,806** | **140,643** | **158,804** | **177,429** | **181,185** |

Following on from the medium-term forecasts in table 2 above, the long-term liability benchmark assumes capital expenditure funded by borrowing, the minimum revenue provision on new capital expenditure is based on asset life and changes in reserves in line with planned utilisation. This is shown in the chart below together with the maturity profile of the Authority's existing borrowing:

Table 3: Liability Benchmark Chart




## 4.0 **Borrowing Strategy**

4.1 The Authority currently holds £129 million of loans (as at 31st December 2023), a decrease of £13m to the previous year, as part of its strategy for funding previous years' capital programmes. The balance sheet forecast in table 1 shows that the Authority is expected to hold £148 million of loans at the end of 2024/25. The Authority may also borrow additional sums to pre-fund future years' requirements, providing this does not exceed the authorised limit for borrowing of £265 million.

4.2 The Authority's chief 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 Authority's long-term plans change is a secondary objective.

4.3 Given the significant cuts to public expenditure and in particular to local government funding, the Authority's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. Short-term interest rates are currently at a 15-year high but are expected to fall in the coming years 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.

By doing so, the Authority is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of internal / 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. Arlingclose will assist the Authority with this ‘cost of carry’ and breakeven analysis. Its output may determine whether the Authority borrows additional sums at long-term fixed rates in 2024/25 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.

The Authority has previously raised the majority of its long-term borrowing from the PWLB but will consider long-term loans from other sources including banks, pensions and local authorities. PWLB loans are no longer available to local authorities planning to buy investment assets primarily for yield; the Authority intends to avoid this activity in order to retain its access to PWLB loans.

Alternatively, the Authority 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.

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

- HM Treasury’s PWLB lending facility (formerly the Public Works Loan Board)
- any institution approved for investments (see below)
- any other bank or building society authorised to operate in the UK
- any other UK public sector body

4.5 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

4.6 **Short-term and variable rate loans**: These loans leave the Authority 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.

4.7 **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. Other lenders may also be prepared to negotiate premature redemption terms. The Authority 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. The recent rise in interest rates means that more favourable debt rescheduling opportunities should arise than in previous years.

## 5.0 Treasury Investment Strategy

5.1 The Authority holds invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Authority's investment balance has ranged between £10 million and £28 million, and similar levels are expected to be maintained in the forthcoming year.

5.2 Both the CIPFA Code and the WG Guidance require the Authority to invest its treasury funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Authority'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 Authority 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. The Authority aims to be a responsible investor and will consider environmental, social and governance (ESG) issues when investing.

5.3 As demonstrated by the liability benchmark above, the Authority 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.

5.4 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 Authority's ESG policy does not currently include ESG scoring or other real-time ESG criteria at an individual investment level. When investing in banks and funds, the Authority will prioritise banks that are signatories to the UN Principles for Responsible Banking and funds operated by managers that are signatories to the UN Principles for Responsible Investment, the Net Zero Asset Managers Alliance and/or the UK Stewardship Code.

5.5 Under the new IFRS 9 standard, the accounting for certain investments depends on the Authority's "business model" for managing them. The Authority aims to achieve value from its internally managed 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.

5.6 The Authority may invest its surplus funds with any of the counterparty types in table 3 below, subject to the cash limits (per counterparty) and the time limits shown.

Table 4: Approved investment counterparties and limits

| Institution | Maximum Loan £'000 |
|---|---|
| UK Local Authorities | 10,000 |
| UK Bank or UK Rated Building Society | 5,000 |
| Barclays Bank (The Authorities Banker) | 5,000 |
| Money Market Funds | 5,000 per fund or trust |
| Debt Management Account (UK Government) | As required |

| Investment | Security | Use | Maximum Investment Period |
|---|---|---|---|
| Debt Management Agency Deposit Facility | High | In-house | 365 days |
| Term deposits - UK Local Authorities | High although LA's not credit rated | In-house | 365 days |
| Term Deposits - UK Banks and Rated Building Societies | All UK Banks and Rated UK Building Societies | In-house | 365 days |

5.7 **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.

5.8 **Government:** Loans, bonds and bills issued or guaranteed by 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. Investments with the UK Government are deemed to be zero credit risk due to its ability to create additional currency and therefore may be made in unlimited amounts.

5.9 **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.

## 6.0 Treasury Management Prudential Indicators

6.1 The Authority measures and manages its exposures to treasury management risks using the following indicators.

6.2 **Interest rate exposures**: This indicator is set to provide an indication of the Authority's exposure to interest rate risk. The upper limits on the one-year revenue impact of a 1% rise or fall in interest rates will be:

| Interest rate risk indicator | Limit £'000 |
|---|---|
| Upper limit on one year revenue impact of a 1% rise in interest rates | **871** |

The impact of a change in interest rates is calculated on the assumption that maturing loans and investments will be replaced at current rates.

6.3 **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 will be:

| Refinancing rate risk indicator | Upper Limit | Lower Limit |
|---|---|---|
| Under 12 Months | 95% | 0% |
| 12 months and within 24 months | 35% | 0% |
| 24 months and within 5 years | 35% | 0% |
| 5 years and within 10 years | 50% | 0% |
| 10 years and above | 40% | 0% |

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.

6.4 **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 investments will be:

| | 2024/25 £'000 | 2025/26 £'000 | 2026/27 £'000 |
|---|---|---|---|
| Principal Sums Invested for Periods longer than 365 days | 0 | 0 | 0 |

## 7.0 Related Matters

7.1 The CIPFA Code requires the Authority to include the following in its treasury management strategy.

7.2 **Financial derivatives:** Local authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk (e.g. interest rate collars and forward deals) and to reduce costs or increase income at the expense of greater risk (e.g. LOBO loans and callable deposits). The general power of competence in section 24 of the *Local Government and Elections (Wales) Act 2021* 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 Authority will only use standalone financial derivatives (such as swaps, forwards, futures and options) where they can be clearly demonstrated to reduce the overall level of the financial risks that the Authority is exposed to. Additional risks presented, such as credit exposure to derivative counterparties, will be taken into account when determining the overall level of risk. Embedded derivatives, including those present in pooled funds and forward starting transactions, will not be subject to this policy, although the risks they present will be managed in line with the overall treasury risk management strategy.

Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria, assessed using the appropriate credit rating for derivative exposures. An allowance for credit risk calculated using the methodology in the Treasury Management Practices document will count against the counterparty credit limit and the relevant foreign country limit.

In line with the CIPFA Code, the Authority will seek external advice and will consider that advice before entering into financial derivatives to ensure that it fully understands the implications.

7.3 **Markets in Financial Instruments Directive**: The Authority has opted up to professional client status with its providers of financial services, including advisers, banks and brokers, 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 Authority's treasury management activities, the Chief Finance Officer believes this to be the most appropriate status.

7.4 **Government Guidance:** Further matters required by the WG Guidance are included in Appendix 3.

## 8.0 Financial Implications

The budget for investment income in 2024/25 is £489,000. The budget for debt interest paid in 2024/25 is £6.995 million. If actual levels of investments and borrowing, or actual interest rates, differ from those forecast, performance against budget will be correspondingly different.

## 9.0 Other Options Considered

9.1 The WG Guidance and the CIPFA Code do not prescribe any particular treasury management strategy for local authorities to adopt. The Chief Finance 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 |

**Appendix 1**

## Economic Commentary *(January 2024)*

**Economic background:** The impact on the UK from higher interest rates and inflation, a weakening economic outlook, an uncertain political climate due to an upcoming general election, together with war in Ukraine and the Middle East, will be major influences on the Authority's treasury management strategy for 2024/25.

The Bank of England (BoE) increased Bank Rate to 5.25% in August 2023, before maintaining this level for the rest of 2023. In December 2023, members of the BoE's Monetary Policy Committee voted 6-3 in favour of keeping Bank Rate at 5.25%. The three dissenters wanted to increase rates by another 0.25%.

The November quarterly Monetary Policy Report (MPR) forecast a prolonged period of weak Gross Domestic Product (GDP) growth with the potential for a mild contraction due to ongoing weak economic activity. The outlook for CPI inflation was deemed to be highly uncertain, with upside risks to CPI falling to the 2% target coming from potential energy price increases, strong domestic wage growth and persistence in price-setting.

Office for National Statistics (ONS) figures showed CPI inflation was 3.9% in November 2023, down from a 4.6% rate in the previous month and, in line with the recent trend, lower than expected. The core CPI inflation rate declined to 5.1% from the previous month's 5.7%, again lower than predictions. Looking ahead, using the interest rate path implied by financial markets the BoE expects CPI inflation to continue falling slowly, but taking until early 2025 to reach the 2% target before dropping below target during the second half 2025 and into 2026.

ONS figures showed the UK economy contracted by 0.1% between July and September 2023. The BoE forecasts GDP will likely stagnate through 2024. The BoE forecasts that higher interest rates will constrain GDP growth, which will remain weak over the entire forecast horizon.

The labour market appears to be loosening, but only very slowly. The unemployment rate rose slightly to 4.2% between June and August 2023, from 4.0% in the previous 3-month period, but the lack of consistency in the data between the two periods made comparisons difficult. Earnings growth has remained strong, but has showed some signs of easing; regular pay (excluding bonuses) was up 7.3% over the period and total pay (including bonuses) up 7.2%. Adjusted for inflation, regular pay was 1.4% and total pay 1.3%. Looking forward, the MPR showed the unemployment rate is expected to be around 4.25% in the second half of calendar 2023, but then rising steadily over the forecast horizon to around 5% in late 2025/early 2026.

Having increased its key interest rate to a target range of 5.25-5.50% in August 2023, the US Federal Reserve appears now to have concluded the hiking cycle. It is likely this level represents the peak in US rates following a more dovish meeting outcome in December

2023. US GDP grew at an annualised rate of 4.9% between July and September 2023, ahead of expectations for a 4.3% expansion and the 2.1% reading for Q2. But the impact from higher rates has started to feed into economic activity and growth will weaken in 2024. Annual CPI inflation was 3.1% in November.

Eurozone inflation has declined steadily since the start of 2023, falling to an annual rate of 2.4% in November 2023. Economic growth has been weak and GDP contracted by 0.1% in the three months to September 2023. In line with other central banks, the European Central Bank has increased rates, taking its deposit facility, fixed rate tender, and marginal lending rates to 3.75%, 4.25% and 4.50% respectively.

**Credit outlook:** Credit Default Swap (CDS) prices were volatile during 2023, spiking in March on the back of banking sector contagion concerns following the major events of Silicon Valley Bank becoming insolvent and the takeover of Credit Suisse by UBS. After then falling back in Q2 of calendar 2023, in the second half of the year, higher interest rates and inflation, the ongoing war in Ukraine, and now the Middle East, have led to CDS prices increasing steadily.

On an annual basis, CDS price volatility has so far been lower in 2023 compared to 2022, but this year has seen more of a divergence in prices between ringfenced (retail) and non-ringfenced (investment) banking entities once again.

Moody's revised its outlook on the UK sovereign to stable from negative to reflect its view of restored political predictability following the volatility after the 2022 mini-budget. Moody's also affirmed the Aa3 rating in recognition of the UK's economic resilience and strong institutional framework.

Following its rating action on the UK sovereign, Moody's revised the outlook on five UK banks to stable from negative and then followed this by the same action on five rated local authorities. However, within the same update the long-term ratings of those five local authorities were downgraded.

There remain competing tensions in the banking sector, on one side from higher interest rates boosting net income and profitability against another of a weakening economic outlook and likely recessions that increase the possibility of a deterioration in the quality of banks' assets.

However, 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.

**Interest rate forecast (December 2023):** Although UK inflation and wage growth remain elevated, the Authority's treasury management adviser Arlingclose forecasts that Bank Rate has peaked at 5.25%. The Bank of England's Monetary Policy Committee will start reducing rates in 2024 to stimulate the UK economy but will be reluctant to do so until it is sure there will be no lingering second-round effects. Arlingclose sees rate cuts from Q3 2024 to a low of around 3% by early-mid 2026.

Arlingclose expects long-term gilt yields to be broadly stable at current levels (amid continued volatility), following the decline in yields towards the end of 2023, which reflects the expected lower medium-term path for Bank Rate. Yields will remain relatively higher than in the past, due to quantitative tightening and significant bond supply. As ever, there will undoubtedly be short-term volatility due to economic and political uncertainty and events.

Appendix 2

## Existing Investment & Debt Portfolio Position

| Description | 31.12.23 Actual Debt Portfolio £000 | 31.12.23 Average Rate % |
|---|---|---|
| **External Borrowing** | | |
| Public Works Loan Board Loans | 83,335 | 5.17 |
| Local Authorities | 29,000 | 5.40 |
| LOBO Loans | 0 | 0.00 |
| Banks and Building Societies | 0 | 0.00 |
| Other Loans | 16,181 | 0.00 |
| **Total Gross External Debt** | **128,516** | **4.57** |
| **Treasury Investments** | | |
| Banks and Building Societies | 0 | 0.00 |
| Cash and Bank Equivalents | 3,438 | 4.95 |
| DMO | 4,500 | 5.18 |
| Local Authorities | 5,000 | 5.40 |
| **Total Treasury Investments** | **12,938** | **5.20** |
| **Net Debt** | **115,578** | **4.50** |

**Appendix 3**

**Additional requirements of Welsh Government Guidance**

1.0 The Welsh Government (WG) published revised Investment Guidance in November 2019 which places additional reporting requirements upon local authorities that are not integral to this Authority's treasury management processes. The guidance also covers investments that are not part of treasury management, for example investment property and loans to local organisations.

2.0 The Authority's investments contribute to its service delivery objectives and/or to promote wellbeing as follows:

- treasury management investments support effective treasury management activities,
- loans to local organisations provide financial support to those organisations to enable them to deliver local public services that would otherwise be provided directly by the Authority, and
- investment property provides a net financial surplus that is reinvested into local public services.

3.0 **Climate change:** The Authority's Carbon Management Plan was reported to Council on the 23rd October 2019, with regular reports to Scrutiny Committee, the latest in January 2022.

4.0 **Specified investments**: The WG Guidance defines specified investments as those:

- denominated in pound sterling,
- due to be repaid within 12 months of arrangement unless the counterparty is a local authority,
- not defined as capital expenditure by legislation, and
- invested with one of:
    - the UK Government,
    - a UK local authority, parish council or community council, or
    - a body or investment scheme of "high credit quality".

The Authority defines “high credit quality” organisations and securities as those having a credit rating of [A-] or higher that are domiciled in the UK or a foreign country with a sovereign rating of [AA+] or higher. For money market funds and other pooled funds “high credit quality” is defined as those having a credit rating of [A-] or higher.

5.0 **Loans:** The WG Guidance defines a loan as a written or oral agreement where the authority temporarily transfers cash to a third party, joint venture, subsidiary or associate who agrees a return according to the terms and conditions of receiving the loan, except where the third party is another local authority.

The Authority has one service investment at a value of £349,800 (as at 31st March 2023) for the Gellideg Housing Co-operative. The Council also participates in various Loans schemes including the Empty Homes and Vibrant and Viable Places Loans schemes funded by the Welsh Government. The Authority’s financial exposure to loans to local enterprises, local charities, wholly owned companies and joint ventures is to be determined and will be subject to a further report if necessary.

The Authority uses an allowed ‘expected credit loss’ model for loans and receivables as set out in *International Financial Reporting Standard 9 Financial Instruments* as adopted by proper practices to measure the credit risk of its loan portfolio. Appropriate consideration is given to state aid rules and competition law. The Authority has appropriate credit control arrangements to recover overdue repayments in place.

**Non-specified investments**: Any financial investment not meeting the definition of a specified investment or a loan is classed as non-specified. Given the wide definition of a loan, this category only applies to units in pooled funds and shares in companies. The Authority does not currently have any non-specified investments, limits are to be determined and will be subject to a further report if necessary.

**Non-financial investments:** This category covers non-financial assets held primarily or partially to generate a profit, primarily investment property. Security is determined by comparing each asset’s purchase price to its fair value using the model in International Accounting Standard 40: Investment Property as adapted by proper practices. The Authority does not currently have any Investment Properties.

**Investment advisers:** The Authority has appointed Arlingclose Limited as treasury management advisers. The quality of these services is controlled by client meetings and the contract is reviewed every three to five years.

**Borrowing in advance of need:** Welsh Government guidance is that local authorities must not borrow more than or in advance of their needs purely in order to profit from the investment of the extra sums borrowed.

**Capacity and skills:** The Council employs professionally qualified and experienced staff in senior positions with responsibility for making investment decisions.

Staff attend training courses, seminars, meetings and conferences provided by Arlingclose and CIPFA. Relevant staff are also encouraged to study professional qualifications from CIPFA, and other appropriate organisations.

**Commercial deals:** The Authority does not currently have any commercial investments, if this occurs in the future it will be in consultation with the Chief Finance Officer to ensure the core principles of the prudential framework and of the regulatory regime within which local authorities operate is considered.