Scottish Borders Council

TREASURY MANAGEMENT STRATEGY STATEMENT

Policy on the Statutory Repayment of Loans Fund Advances and Annual Investment Strategy

2025/26

CONTENTS

1. Purpose and Scope

The Council is required to operate a balanced revenue budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this 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.

The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer-term cash flow planning, to ensure that it can meet its capital spending obligations. This management of longer-term cash may involve arranging long or short-term loans or using longer-term cash flow surpluses. On occasion, when it is prudent and economic, any debt previously drawn may be restructured to meet risk or cost objectives.

The Prudential and Treasury Indicators (summarised in Annex A) consider the affordability and impact of capital expenditure decisions and set out the Council's overall capital framework. These Indicators have been developed in line with both the Prudential and Treasury Codes. The treasury service considers the effective funding of these decisions. Together they form part of the process which ensures the Council meets its balanced budget requirement under the Local Government Finance Act 1992. The Treasury Management Strategy therefore forms an integral part of the Council's overall Financial Strategy covering both its revenue and capital budgets.

The contribution the treasury management function makes to the Council is critical, as the balance of debt and investment operations ensure liquidity or the ability to meet spending commitments as they fall due, either on day-to-day revenue or for larger capital projects. The treasury operations will see a balance of the interest costs of debt and the investment income arising from cash deposits affecting the available budget. Since cash balances generally result from reserves and balances, it is paramount to ensure adequate security of the sums invested, as a loss of principal will in effect result in a loss to the General Fund Balance.

CIPFA defines treasury management as:

"The management of the local authority's borrowing, investments and cash flows, including 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."

Whilst any commercial initiatives or loans to third parties will impact on the treasury function, these activities are generally classed as non-treasury activities, (arising usually from capital expenditure), and are separate from the day-to-day treasury management activities.

1.1 Reporting Requirements

1.1.1 Capital Strategy

The CIPFA 2021 Prudential and Treasury Management Codes require all local authorities to prepare a Capital Strategy report which will provide the following: -

- a high-level long-term overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services
- an overview of how the associated risk is managed
- the implications for future financial sustainability

The aim of the strategy is to ensure that all the Council's elected members fully understand the overall long-term policy objectives and resulting Capital Strategy requirements, governance procedures and risk appetite.

1.1.2 Treasury Management Reporting

The Council is currently required to receive and approve, as a minimum, three main treasury reports each year, which incorporate a variety of policies, estimates and actuals.

a. **Prudential and treasury indicators and treasury strategy** (this report) - The first, and most important report is forward looking and covers: -
   - the capital plans, (including prudential indicators)
   - a policy on statutory repayment of loans fund advances, (how residual capital expenditure is charged to revenue over time)
   - the Treasury Management Strategy, (how the investments and borrowings are to be organised), including treasury indicators; and
   - an Annual Investment Strategy, (the parameters on how investments are to be managed).

b. **A mid-year treasury management report** – This is primarily a progress report and will update members on the capital position, amending prudential indicators as necessary, and whether any policies require revision.

c. **An annual treasury report** – This is a backward-looking review document and provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

Scrutiny
The above reports are required to be adequately scrutinised before being recommended to the Full Council. This role is undertaken by the Audit Committee.

Quarterly reports – In addition to the three major reports detailed above, from 2023/24 quarterly reporting (end of June/end of December) has also been required. However, these additional reports do not have to be reported to Full Council/Board but do require to be adequately scrutinised. This role is undertaken by the Executive Committee. and the information is contained within the quarterly Capital Report. (The reports, specifically, comprise updated Treasury/Prudential Indicators).

1.2 Treasury Management Strategy for 2025/26

The strategy for 2025/26 covers two main areas:

Capital issues

- the capital expenditure plans and the associated prudential indicators
- the policy for statutory repayment of loans fund advances

Treasury management issues

- the current treasury position
- treasury indicators which limit the treasury risk and activities of the Authority
- prospects for interest rates
- the borrowing strategy
- policy on borrowing in advance of need
- debt rescheduling
- the investment strategy
- creditworthiness policy; and
- the policy on use of external service providers

These elements cover the requirements of the Local Government in Scotland Act 2003, the CIPFA Prudential Code, the CIPFA Treasury Management Code and Scottish Government loans fund repayment regulations and investment regulations, particularly Finance Circulars 5/2010 and 7/2024.

1.3 Training

The CIPFA Treasury Management 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.

Furthermore, pages 47 and 48 of the Code state that they expect "all organisations to have a formal and comprehensive knowledge and skills or training policy for the effective acquisition and retention of treasury management knowledge and skills for those responsible for management, delivery, governance and decision making."

This Council ensures that this important issue is addressed by:

Elected Members

- Working with members of the Audit Committee to identify their training needs
- Working with MUFG Corporate Markets to identify appropriate training provision for elected members

Officers dealing with treasury management matters will have the option of various levels of training, depending on need, including:

- Treasury courses run by the Council's advisers
- Attendance at CIPFA treasury management training events
- Attendance at the CIPFA Scottish Treasury Management Forum and information exchanged via the Treasury Management Forum network
- On the job training in line with the approved Treasury Management Practices (TMPs).

In further support of the revised training requirements, CIPFA's updated guidance note for Audit Committees includes the Good Practice Principles Checklist and Evaluation of Impact and Effectiveness Toolkit. This requires self assessment by members responsible for the scrutiny of treasury management and identifies any development needs.

Treasury Management Consultants

The Council uses MUFG Pension & Market Services, MUFG Corporate Markets as its external treasury management advisors. Link Group was acquired by Mitsubishi UFJ Trust & Banking Corporation (the Trust Bank), a consolidated subsidiary of Mitsubishi UFJ Financial Group, Inc (MUFG) on 16 May 2024. As a result, Link Group is now known as MUFG Pension & Market Services and Link Treasury Services is now known as MUFG Corporate Markets.

The Council recognises that responsibility for treasury management decisions always remains with the organisation and will ensure that undue reliance is not placed upon the services of our external service providers. All decisions will be undertaken with regards to all available information, including, but not solely, our treasury advisers.

It also recognises that there is value in employing external providers of treasury management services 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.

The Treasury Management Strategy covers the treasury management activities for the Council (including any subsidiary organisations) and the cash managed by the Council on behalf of the Scottish Borders Council Pension, Common Good and Trust Funds.

1.4 International Financial Reporting Standard (IFRS) 16 – Leasing

The CIPFA LAASAC Local Authority Accounting Code Board deferred implementation of IFRS16 until 1st April 2024, the 2024/25 financial year. From this date, most leases which were previously off balance sheet and funded via revenue, will now be included as part of the other long term liabilities and the associated assets will now be included under a new classification called 'Right of Use Assets' within the annual accounts. The full impact of this change will be reflected in the Financial Statements for the year to 31 March 2025.

There will be adjustments to the Capital Financing Requirement, external debt (other long-term liabilities), the Authorised Limit and Operational Boundary, to allow for those leases which were previously off-balance sheet, being brought onto the balance sheet at 1 April 2024.

It is not currently possible to be precise about such adjustment figures until detailed data gathering has been substantially completed at the end of the 2024/25 financial year. The limits may need to be amended mid-year once the detailed impact is known.

In summary, IFRS16 is expected to impact the following treasury management and prudential indicators:

Authorised Limit: as this includes borrowing and long-term liabilities (the lease liability)
Operational Boundary: as this includes borrowing and long-term liabilities (the lease liability)
Actual external debt at year end: as this includes borrowing and long-term liabilities (the lease liability)
Capital expenditure: will need to include the right of use asset additions
Capital Financing Requirement: includes the right of use asset addition less statutory repayment of loans fund advances
Gross debt and the Capital Financing Requirement: gross borrowing will include long-term liabilities (the lease liability), and the CFR will include the right of use asset additions less statutory repayment of loans fund advances
Financing costs to net revenue stream: interest payable element of the lease rental and statutory repayment of loans fund advances will be impacted

2. Background

2021 revised CIPFA Treasury Management Code and Prudential Code – changes which impact on future reports and the risk management framework

CIPFA published the revised Codes on 20th December 2021 and stated that revisions need to be included in the reporting framework from the 2023/24 financial year. This Council, therefore, must have regard to these Codes of Practice when it prepares the Treasury Management Strategy Statement (TMSS) and Annual Investment Strategy (AIS), and also related reports during the financial year, which are taken to Full Council for approval.

The revised Treasury Management Code required all investments and investment income to be attributed to one of the following three purposes: -

Treasury management
Arising from the organisation's cash flows or treasury risk management activity, this type of investment represents balances which are only held until the cash is required for use. Treasury investments may also arise from other treasury risk management activity which seeks to prudently manage the risks, costs or income relating to existing or forecast debt or treasury investments.

Service delivery
Investments held primarily and directly for the delivery of public services including housing, regeneration and local infrastructure. Returns on this category of investment which are funded by borrowing are permitted only in cases where the income is "either related to the financial viability of the project in question or otherwise incidental to the primary purpose".

Commercial return
Investments held primarily for financial return with no treasury management or direct service provision purpose. Risks on such investments should be proportionate to an authority's financial capacity – i.e., that 'plausible losses' could be absorbed in budgets or reserves without unmanageable detriment to local services. An authority must not borrow to invest primarily for financial return.

The revised Treasury Management Code requires an authority to implement the following: -

- **Adopt a liability benchmark treasury indicator** to support the financing risk management of the capital financing requirement; this is to be shown in chart form for a minimum of ten years, with material differences between the liability benchmark and actual loans to be explained;

- **Long-term treasury investments**, (including pooled funds), are to be classed as commercial investments unless justified by a cash flow business case;

- **Pooled funds** are to be included in the indicator for principal sums maturing in years beyond the initial budget year;

- Amendment to the **knowledge and skills register** for officers and members involved in the treasury management function - to be proportionate to the size and complexity of the treasury management conducted by each authority;

- **Reporting to members is to be done quarterly.** Specifically, the Director of Finance is required to establish procedures to monitor and report performance against all forward-looking prudential indicators at least quarterly. The Director is expected to establish a measurement and reporting process that highlights significant actual or forecast deviations from the approved indicators. However, monitoring of prudential indicators, including forecast debt and investments, is not required to be taken to Full Council and should be reported as part of the authority's integrated revenue, capital and balance sheet monitoring;

- **Environmental, social and governance (ESG)** issues to be addressed within an authority's treasury management policies and practices (TMP1).

The main requirements of the Prudential Code relating to service and commercial investments are: -

- The risks associated with service and commercial investments should be proportionate to their financial capacity – i.e. that plausible losses could be absorbed in budgets or reserves without unmanageable detriment to local services;

- An authority must not borrow to invest for the primary purpose of commercial return;

- It is not prudent for local authorities to make any investment or spending decision that will increase the CFR, and so may lead to new borrowing, unless directly and primarily related to the functions of the authority, and where any commercial returns are either related to the financial viability of the project in question or otherwise incidental to the primary purpose;

- An annual review should be conducted to evaluate whether commercial investments should be sold to release funds to finance new capital expenditure or refinance maturing debt;

- A prudential indicator is required for the net income from commercial and service investments as a proportion of the net revenue stream;

- Create new Investment Management Practices to manage risks associated with non-treasury investments, (similar to the current Treasury Management Practices).

An authority's Annual Investment Strategy should include: -

- The authority's approach to investments for service or commercial purposes (together referred to as non-treasury investments), including defining the authority's objectives, risk appetite and risk management in respect of these investments, and processes ensuring effective due diligence;

- An assessment of affordability, prudence and proportionality in respect of the authority's overall financial capacity (i.e., whether plausible losses could be absorbed in budgets or reserves without unmanageable detriment to local services);

- Details of financial and other risks of undertaking investments for service or commercial purposes and how these are managed;

- Limits on total investments for service purposes and for commercial purposes respectively (consistent with any limits required by other statutory guidance on investments);

- Requirements for independent and expert advice and scrutiny arrangements (while business cases may provide some of this material, the information contained in them will need to be periodically re-evaluated to inform the authority's overall strategy);

- State compliance with paragraph 51 of the Prudential Code in relation to investments for commercial purposes, in particular the requirement that an authority must not borrow to invest primarily for financial return.

As this TMSS and AIS deals solely with treasury management investments, the categories of service delivery and commercial investments should be addressed as part of the Capital Strategy report.

However, as investments in commercial property have implications for cash balances managed by the treasury team, it will be for each authority to determine whether to add a high level summary of the impact that commercial investments have, or may have, if it is planned to liquidate such investments within the three year time horizon of this report, (or a longer time horizon if that is felt appropriate).

3. The Capital Prudential Indicators 2025/26 – 2029/30

The Council's Financial Strategy sets out financial resource and management parameters within which it will deliver its Council Plan. The Financial Strategy brings together various elements, including the Treasury Management Strategy, and establishes the financial planning framework for the Council in terms of Revenue Expenditure and Capital Investment. The output from this framework is the Council's Financial Plan, approved annually in February, presenting the proposals for delivering its services and objectives.

The Financial Strategy establishes that the Financial Principles underpinning the planning for the Council's future service delivery are to:

(i) Raise the funds required by the Council to meet approved service levels in the most effective manner;

(ii) Manage the effective deployment of those funds in line with the Council's corporate objectives and priorities; and

(iii) Provide stability in resource planning and service delivery as expressed through Corporate and Business Plans and the Revenue and Capital Financial Plan.

To adhere to these Principles, the Financial Strategy states that the Council will adopt Financial Objectives to:

"ensure capital borrowing is within prudential borrowing limits and sustainable in the longer term. In this regard it is important to recognise the capital investment decisions taken now have long term borrowing implications and these have the potential to place a significant burden on future tax payers".

The draft revenue budget sets loans charges associated with capital borrowing over the next 5 years at £23.6m in 2025/26, rising to £32.7m in 2029/30.

The Council's Capital Financial Plan is the key driver of treasury management activity. The output of the capital expenditure plans is reflected in the prudential indicators, which are designed to assist members' overview and confirm capital expenditure plans.

3.1 Capital Expenditure (Prudential Indicator PI-1)

This prudential indicator is a summary of the Council's capital expenditure plans, both those agreed previously, and those forming part of this planning cycle. The Capital Financial Plan for 2025/26 – 2034/35 includes the following capital expenditure forecasts for the first five years. 2024/25 projected outturn figures are also shown for information:

Capital Expenditure (PI-1)	Forecast					
£m	2024/25	2025/26	2026/27	2027/28	2028/29	2029/30
Assets & Infrastructure	30.7	19.3	14.2	14.1	12.2	11.9
Other Corporate Services	6.9	0.8	0.5	0.2	0.2	0.1
Children & Young People	74.6	39.3	38.9	23.8	3.1	1.8
Culture & Sport	0.5	2.0	0.7	0.7	0.7	0.7
Economic Regeneration	5.4	23.7	12.0	12.8	5.7	6.4
Housing Strategy & Services	1.0	0.5	0.5	0.5	0.5	0.5
Social Care Infrastructure	1.2	13.2	5.5	13.2	-	-
Emergency & Unplanned & Planned programme adjustments	(7.0)	-	0.1	0.2	5.2	5.2
Total	113.2	98.8	72.4	65.5	27.6	26.6

3.2 Capital Financing Assumptions

The table below summarises the above capital expenditure plans and how these plans are being financed by capital or revenue resources. Any shortfall of resources results in a financing need.

Capital Expenditure	Forecast					
£m	2024/25	2025/26	2026/27	2027/28	2028/29	2029/30
Capital Expenditure – per plan	113.2	98.8	72.4	65.5	27.6	26.6
Total Expenditure	**113.2**	**98.8**	**72.4**	**65.5**	**27.6**	**26.6**
Financed by:						
Capital receipts	4.5	1.5	1.5	1.5	-	-
CFCR	1.2	1.8	-	-	-	-
Developer Contributions	6.2	0.1	0.1	0.1	0.1	0.1
Govt. General Capital Grants	11.8	12.3	11.2	11.2	11.3	11.0
Govt. Specific Capital Grants	0.7	1.2	-	-	-	0.2
Other Grants & Contributions	8.1	22.2	12.5	12.7	5.6	6.3
Plant & Vehicle / Infrastructure Fund	3.5	3.5	3.5	3.5	2.0	2.0
Synthetic Pitch Replacement Fund	-	1.1	0.5	0.5	0.5	0.5
Net financing need for the year met by borrowing	77.2	55.1	43.1	36.0	8.1	6.5

3.3 The Council's Borrowing Need (the Capital Financing Requirement – Prudential Indicator PI-2)

a) The second prudential indicator is the Council's Capital Financing Requirement (CFR).

The CFR measures the Council's underlying need to borrow to finance its capital investment. It is calculated for a particular year with reference to the outstanding amount from the previous year, the Council's borrowing requirement for the year in question less the amount which the Council sets aside from revenue to repay debt. It is not the same amount as the Council actually borrows which is determined by the capital plan, interest rate and cash flow considerations.

The CFR does not increase indefinitely, as prudent annual repayments from revenue need to be made which reflect the useful life of capital assets financed by borrowing. From 1 April 2016, authorities have been able to choose whether to use scheduled debt amortisation (loans pool charges), or another suitable method of calculation to repay borrowing. The Council calculates repayment of loans fund advances with reference to the life of an asset using the annuity method (option 3) – further details at 3.5 below.

b) The CFR also includes any other long term liabilities (e.g. PPP schemes, finance leases). Whilst these increase the CFR, and therefore the Council's borrowing requirement, these types of schemes include a borrowing facility by the PPP lease provider and so the Council is not required to separately borrow for these schemes. The Council has £75.2m of liabilities relating to such schemes within the 2024/25 long term liabilities figure.

These liabilities will be remeasured for the year end Financial Statements to comply with IFRS16 and so the CFR will increase as a direct result.

Capital Financing Requirement (PI-2) £m	Actual	Estimate					
	23/24	24/25	25/26	26/27	27/28	28/29	29/30
Total CFR (PI-2) *	411.9	479.4	522.2	551.1	571.3	562.0	550.7
Movement in CFR represented by:							
Net financing need for the year (above)		77.2	55.1	43.1	36.0	8.1	6.5
Less scheduled debt amortisation and other financing movements		(9.7)	(12.3)	(14.2)	(15.8)	(17.4)	(17.8)
Movement in CFR		67.5	42.8	28.9	20.2	(9.3)	(11.3)

* *The CFR for this calculation includes projected capital expenditure to 31 March of each financial year.*

c) A key aspect of the regulatory and professional guidance is that elected members are aware of the size and scope of any commercial activity in relation to the authority's overall financial position. This Council does not currently have any commercial activity.

3.4 Liability Benchmark

The Council is required to estimate and measure the Liability Benchmark (LB) for the forthcoming financial year and the following two financial years, as a minimum however CIPFA strongly recommends that the LB is produced for at least ten years. The Council has measured the LB for a ten year period in line with the Capital Plan as shown in the graph below.

There are four components to the LB: -

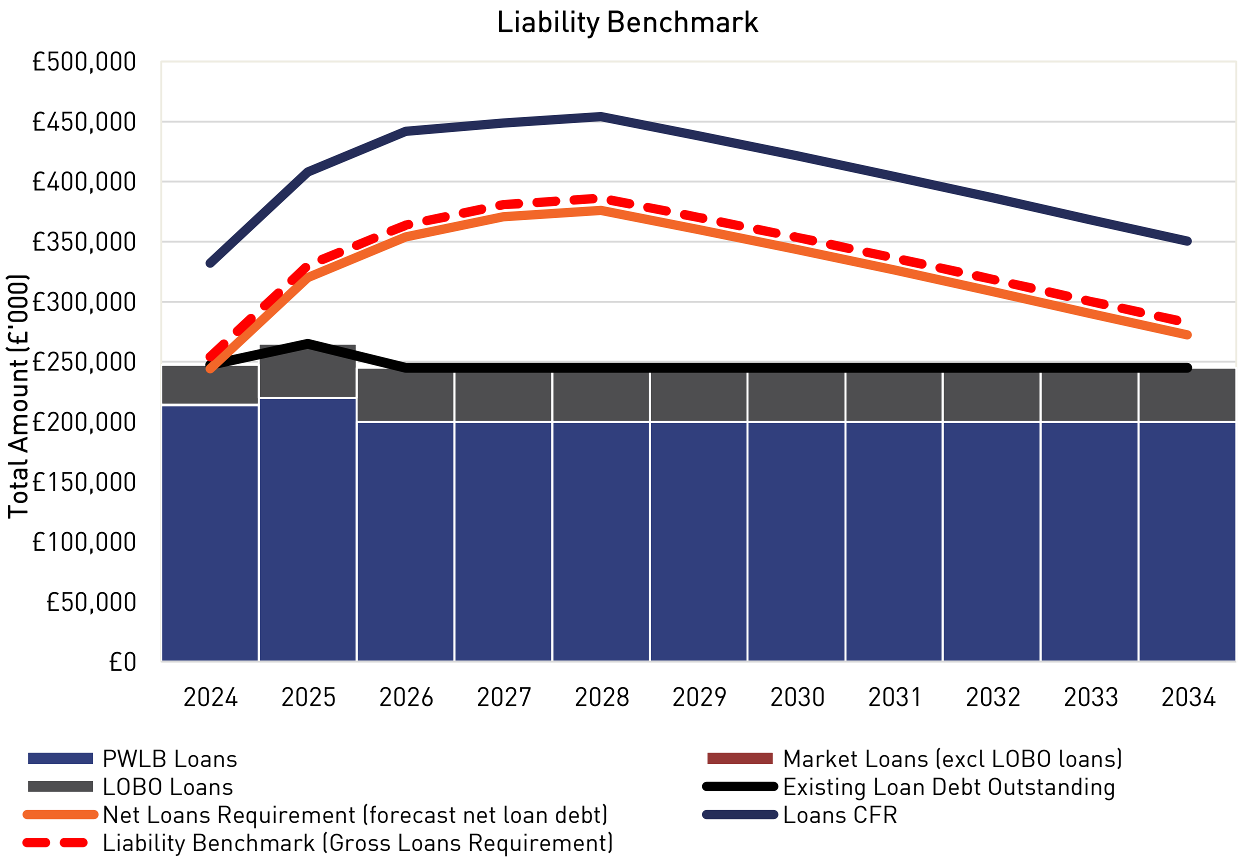
1 Existing loan debt outstanding: the Authority's existing loans that are still outstanding in future years, with no new borrowing added.

2 Loans CFR: this is calculated in accordance with the loans CFR definition in the Prudential Code and projected into the future based on approved prudential borrowing and planned Loans Fund advances/Loans Fund principal repayments. As only approved prudential borrowing is included, the Loans CFR peaks after four years.

3 Net loans requirement: this will show the Authority's gross loan debt less treasury management investments at the last financial year-end, projected into the future and based on its approved prudential borrowing, planned Loans Fund principal repayments and any other major cash flows forecast.

4 Liability benchmark (or gross loans requirement): this equals net loans requirement plus short-term liquidity allowance.

The graph below shows the Council to be in an under-borrowed position with a requirement for further borrowing in future years. The Council will actively monitor the progress of the Capital Plan and align forecast spend to the most efficient borrowing options available at that time.



3.5 Statutory Repayment of Loans Fund Advances

a) The Council is required to set out its policy for the statutory repayment of loans fund advances prior to the start of the financial year. The repayment of loans fund advances ensures that the Council makes a prudent provision each year to pay off an element of the accumulated loans fund advances made in previous financial years.

b) A variety of options are provided to Councils so long as a prudent provision is made each year. The Council is recommended to approve the following policy on the repayment of loans fund advances:-

- For loans fund advances made before 1 April 2016, the policy will be to maintain the practice of previous years and apply the **Statutory Method (option 1)**, with all loans fund advances being repaid by the annuity method.
- For loans fund advances made after 1 April 2016, the policy for the repayment of loans advances will be the:-

  1. **Asset life method** – loans fund advances will be repaid with reference to the life of an asset using either the equal instalment or **annuity method (option 3)**.

The annuity rate applied to the loans fund repayments was based on historic interest rates and is currently 2.02%. However, as required, under paragraph 86 of the Finance Circular 7/2024, the Authority has reviewed and re-assessed the historic annuity rate to ensure that it is a prudent application, which it is.

4 Treasury Management Strategy

The capital expenditure plans set out in Section 3 provide details of the service activity of the Council. The treasury management function ensures that the Council's cash is organised in accordance with the relevant professional Codes, so that sufficient cash is available to meet this service activity and the Council's capital strategy. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of appropriate borrowing facilities. The strategy covers the relevant treasury / prudential indicators, the current and projected debt positions and the annual investment strategy.

4.1 Current Portfolio Position

a) The overall treasury management portfolio as at 31 March 2024 and for the position as at 31 December 2024 are shown below for both borrowing and investments. The increase in external borrowing relates to approved investment in the school estate as approved within the Council's Financial Plan.

TREASURY PORTFOLIO				
Treasury investments	actual 31.3.24 £000	actual 31.3.24 %	current 31.12.24 £000	current 31.12.24 %
Banks	2,736	84.5%	4,494	19.5%
DMADF (HM Treasury)	-	-	-	-
Money Market Funds	500	15.5%	18,500	80.5%
Total managed in house	3,236	100%	22,994	100%
Total managed externally	-	-	-	-
Total treasury investments	3,236	100%	22,994	100%
Treasury external borrowing				
Third party loans	600	0.2%	600	0.2%
PWLB	213,737	86.4%	309,355	93.2%
LOBOs	33,000	13.4%	22,000	6.6%
Total external borrowing	247,337	100%	331,955	100%
Net treasury investments / (borrowing)	(244,101)	-	(308,961)	-

b) The Council's forward projections for borrowing are summarised below. The Prudential Code provides that over the medium term the Council should ensure that net external borrowing does not exceed the total of the CFR in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years. This provides assurance that borrowing will only be incurred for capital purposes.

as at 31 March £m	Forecast					
	2024/25	2025/26	2026/27	2027/28	2028/29	2029/30
Borrowing	335.8	380.8	410.8	430.8	423.8	408.8
Other Long Term Liabilities (Finance Leases)	75.2	70.9	66.6	62.4	58.2	54.0
Total Gross Borrowing (Prudential Indicator PI-5)	411.0	451.6	477.4	493.2	482.0	462.8
Capital Financing Requirement*	551.1	571.3	562.0	550.7	538.5	525.8
(Under) / Over Borrowing (Prudential Indicator PI-6)	(140.1)	(119.7)	(84.6)	(57.5)	(56.5)	(63.0)

** The CFR for this calculation includes the current and two future years projected capital expenditure see 4.1b)*

c) The Council has complied with this prudential indicator in the current year and no difficulties are currently envisaged for the long term future. This view takes into account current commitments, existing plans, and the proposals in the Financial Plans for 2025/26.

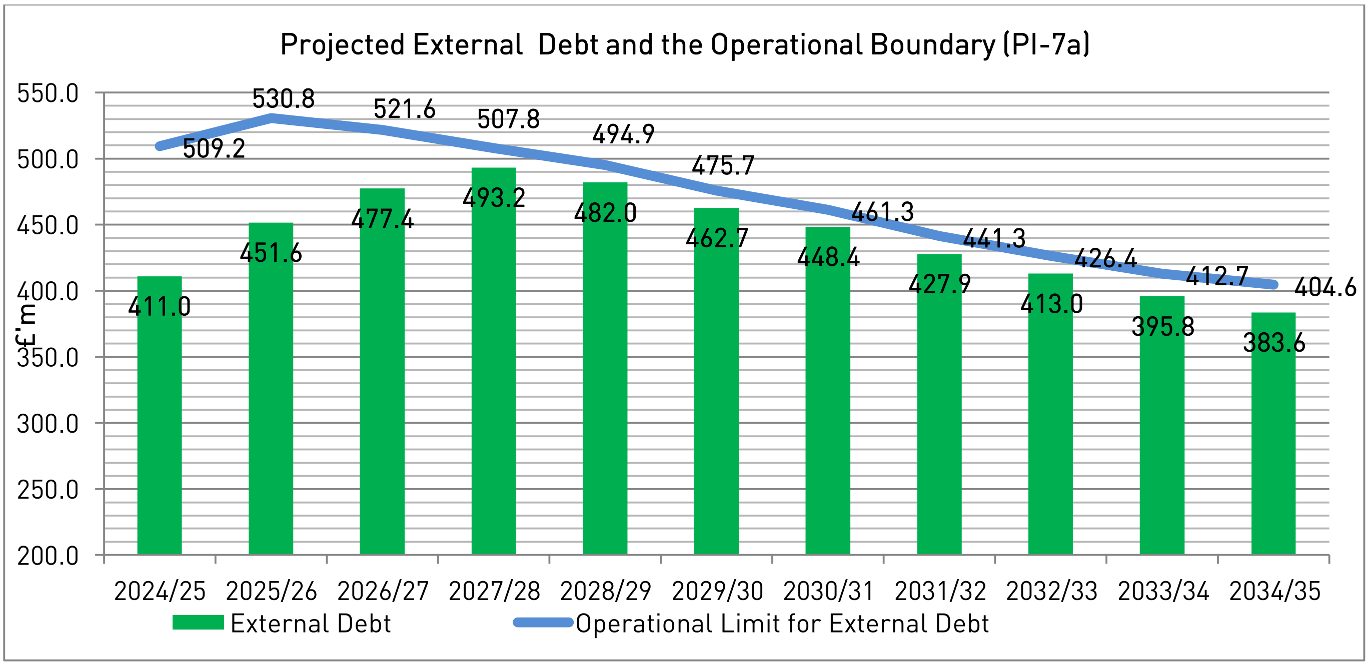
4.2 Treasury Indicators: Limits to Borrowing Activity

The Operational Boundary (Prudential Indicator PI-7)

a) This is the limit beyond which external borrowing is not normally expected to exceed. In most cases, this would be a similar figure to the CFR but may be lower or higher depending on the levels of actual debt and the ability to fund under-borrowing by other cash resources.

Operational boundary £m	Estimate					
	2024/25	2025/26	2026/27	2027/28	2028/29	2029/30
Total Operational Boundary (PI-7a)	509.2	530.8	521.5	507.9	494.9	475.7
Less: Other long term liabilities	(75.2)	(70.9)	(66.6)	(62.4)	(58.2)	(54.0)
Operational Boundary exc. Other Long Term Liabilities (PI-7b)	434.0	459.9	454.9	445.5	436.7	421.7

b) The following chart shows how the current and projected Operational Borrowing limit compare with the anticipated levels of gross external debt **(PI-5)**.



The Authorised Limit for External Debt (Prudential Indicator PI-8)

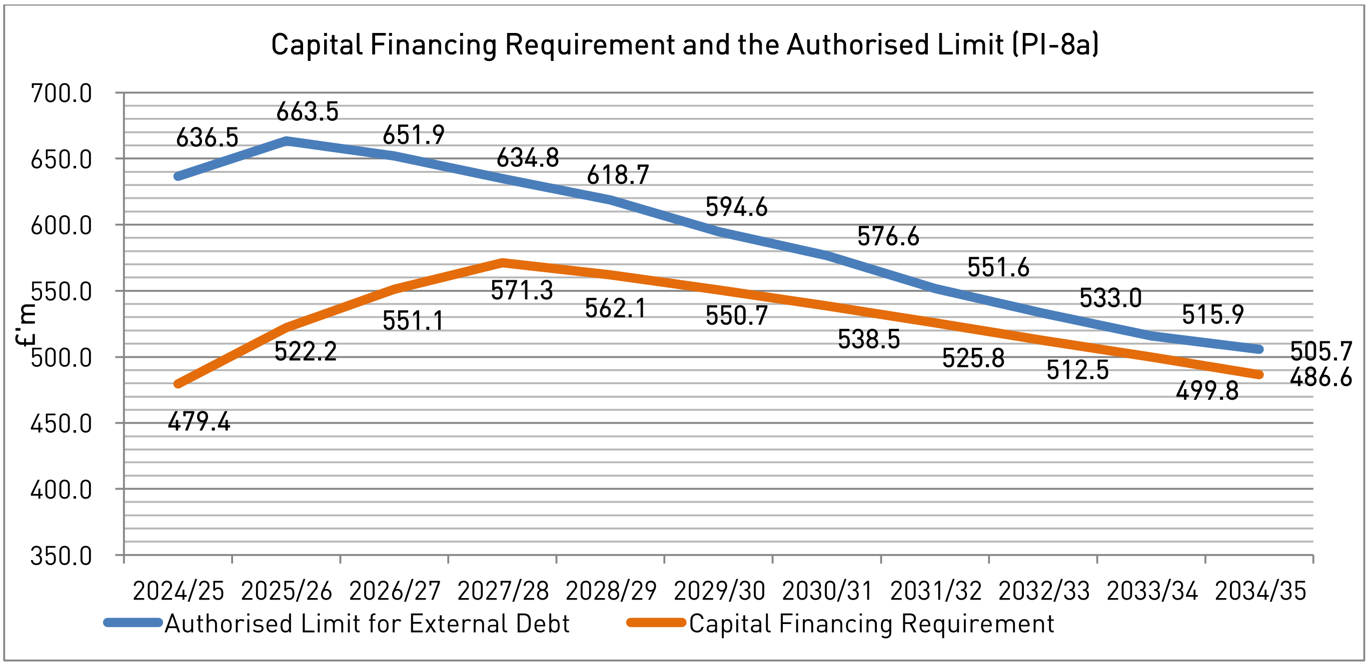
c) A further key prudential indicator is the Authorised Limited for external debt which represents a control on the maximum level of borrowing. This represents the limit set by Council beyond which external debt is prohibited, and this limit needs to be set or revised by full Council. It reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

d) The authorised limits for external debt for the current year and two subsequent years are required to be set by Council under Regulation 6(1) of the Local Authority (Capital Finance and Accounting) (Scotland) Regulations 2016.

e) The Authorised Limit is shown below, being the Operational Boundary **(PI-7a)** plus 25% margin: This will require to be updated following the application of IFRS16.

Authorised Limit £m	Estimate					
	2024/25	2025/26	2026/27	2027/28	2028/29	2029/30
Total Authorised Limit (PI-8a)	636.5	663.5	651.9	634.8	618.7	594.6
Less: Other long term liabilities	(75.2)	(70.9)	(66.6)	(62.4)	(58.2)	(54.0)
Authorised Limit exc. Other Long-Term Liabilities (PI-8b)	561.3	592.6	585.3	572.4	560.5	540.6

f) The chart below shows how the current and projected Capital Financing Requirement **(PI-2)** compares to the Authorised Limit for External Debt **(PI–8a)**.



4.3 Prospects for Interest Rates

a) The Council has appointed MUFG Corporate Markets as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates.

MUFG Corporate Markets provided the following forecasts and associated commentary on 12th December 2024.

These are forecasts for certainty rates (gilt yields plus 80bps):

Link Group Interest Rate View	11.11.24												
	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27	Jun-27	Sep-27	Dec-27
BANK RATE	4.75	4.50	4.25	4.00	4.00	3.75	3.75	3.75	3.50	3.50	3.50	3.50	3.50
3 month ave earnings	4.70	4.50	4.30	4.00	4.00	4.00	3.80	3.80	3.80	3.50	3.50	3.50	3.50
6 month ave earnings	4.70	4.40	4.20	3.90	3.90	3.90	3.80	3.80	3.80	3.50	3.50	3.50	3.50
12 month ave earnings	4.70	4.40	4.20	3.90	3.90	3.90	3.80	3.80	3.80	3.50	3.50	3.50	3.50
5 yr PWLB	5.00	4.90	4.80	4.60	4.50	4.50	4.40	4.30	4.20	4.10	4.00	4.00	3.90
10 yr PWLB	5.30	5.10	5.00	4.80	4.80	4.70	4.50	4.50	4.40	4.30	4.20	4.20	4.10
25 yr PWLB	5.60	5.50	5.40	5.30	5.20	5.10	5.00	4.90	4.80	4.70	4.60	4.50	4.50
50 yr PWLB	5.40	5.30	5.20	5.10	5.00	4.90	4.80	4.70	4.60	4.50	4.40	4.30	4.30

Additional notes by MUFG Corporate Markets on this forecast table: -

Following the 30 October Budget, the outcome of the US Presidential election on 6 November, and the 25bps Bank Rate cut undertaken by the Monetary Policy Committee (MPC) on 7 November, we have significantly revised our central forecasts for the first time since May. In summary, our Bank Rate forecast is now 50bps – 75bps higher than was previously the case, whilst our PWLB forecasts have been materially lifted to not only reflect our increased concerns around the future path of inflation, but also the increased level of Government borrowing over the term of the current Parliament.

If we reflect on the 30 October Budget, our central case is that those policy announcements will be inflationary, at least in the near-term. The Office for Budgetary Responsibility and the Bank of England concur with that view. The latter have the CPI measure of inflation hitting 2.5% y/y by the end of 2024 and staying sticky until at least 2026. The Bank forecasts CPI to be 2.7% y/y (Q4 2025) and 2.2% (Q4 2026) before dropping back in 2027 to 1.8% y/y.

The anticipated major investment in the public sector, according to the Bank, is expected to lift UK real GDP to 1.7% in 2025 before growth moderates in 2026 and 2027. The debate around whether the Government's policies lead to a material uptick in growth primarily focus on the logistics of fast-tracking planning permissions, identifying sufficient skilled labour to undertake a resurgence in building, and an increase in the employee participation rate within the economy.

There are inherent risks to all the above. The worst-case scenario would see systemic blockages of planning permissions and the inability to identify and resource the additional workforce required to deliver large-scale IT, housing and infrastructure projects. This would lead to upside risks to inflation, an increased prospect of further Government borrowing & tax rises, and a tepid GDP performance.

Our central view is that monetary policy is sufficiently tight at present to cater for some further moderate loosening, the extent of which, however, will continue to be data dependent. We forecast the next reduction in Bank Rate to be made in February and for a pattern to evolve whereby rate cuts are made quarterly and in keeping with the release of the Bank's Quarterly Monetary Policy Reports (February, May, August and November).

Any movement below a 4% Bank Rate will, nonetheless, be very much dependent on inflation data in the second half of 2025. The fact that the November MPC rate cut decision saw a split vote of 8-1 confirms that there are already some concerns around inflation's stickiness, and with recent public sector wage increases beginning to funnel their way into headline average earnings data, the market will be looking very closely at those releases.

Regarding our PWLB forecast, the short to medium part of the curve is forecast to remain elevated over the course of the next year, and the degree to which rates moderate will be tied to the arguments for further Bank Rate loosening or otherwise. The longer part of the curve will also be impacted by inflation factors, but there is also the additional concern that with other major developed economies such as the US and France looking to run large budget deficits there could be a glut of government debt issuance that investors will only agree to digest if the interest rates paid provide sufficient reward for that scenario.

So far, we have made little mention of the US President election. Nonetheless, Donald Trump's victory paves the way for the introduction/extension of tariffs that could prove inflationary whilst the same could be said of further tax cuts and an expansion of the current US budget deficit. Invariably the direction of US Treasury yields in reaction to his core policies will, in all probability, impact UK gilt yields. So, there are domestic and international factors that could impact PWLB rates whilst, as a general comment, geo-political risks abound in Europe, the Middle East and Asia.

Our revised PWLB rate forecasts below are based on the Certainty Rate (the standard rate minus 20 bps) which has been accessible to most authorities since 1 November 2012. Please note, the lower Housing Revenue Account (HRA) PWLB rate started on 15 June 2023 for those authorities with an HRA (standard rate minus 60 bps).

Gilt yields and PWLB rates

The overall longer-run trend is for gilt yields and PWLB rates to fall back over the timeline of our forecasts, but the risks to our forecasts are to the upsides. Our target borrowing rates are set **two years forward** (as we expect rates to fall back) and the current PWLB (certainty) borrowing rates are set out below: -

PWLB debt	Current borrowing rate as at 11.11.24 p.m.	Target borrowing rate now (end of Q3 2026)	Target borrowing rate previous (end of Q3 2026)
5 years	5.02%	4.30%	3.90%
10 years	5.23%	4.50%	4.10%
25 years	5.66%	4.90%	4.40%
50 years	5.42%	4.70%	4.20%

Borrowing advice: Our long-term (beyond 10 years) forecast for Bank Rate has been increased to 3.25% (from 3%). As all PWLB certainty rates are currently significantly above this level, borrowing strategies will need to be reviewed in that context. Overall, better value can be obtained at the shorter end of the curve and short-dated fixed LA to LA monies should also be considered. Temporary borrowing rates will, generally, fall in line with Bank Rate cuts.

Our suggested budgeted earnings rates for investments up to about three months' duration in each financial year are set out below.

Average earnings in each year	Now	Previously
2024/25 (residual)	4.60%	4.25%
2025/26	4.10%	3.35%
2026/27	3.70%	3.10%
2027/28	3.50%	3.25%
2028/29	3.50%	3.25%
Years 6 to 10	3.50%	3.25%
Years 10+	3.50%	3.50%

We will continue to monitor economic and market developments as they unfold. Typically, we formally review our forecasts following the quarterly release of the Bank of England's Monetary Policy Report but will consider our position on an ad hoc basis as required.

Our interest rate forecast for Bank Rate is in steps of 25 bps, whereas PWLB forecasts have been rounded to the nearest 10 bps and are central forecasts within bands of + / - 25 bps. Naturally, we continue to monitor events and will update our forecasts as and when appropriate.

4.4 Borrowing Strategy

a) The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need, (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as medium and longer dated borrowing rates are expected to fall from their current levels once prevailing inflation concerns are addressed by tighter near-term monetary policy. Additional borrowing has been taken this year reducing the under-borrowed position. That is, Bank Rate remains relatively elevated in 2025 even if some rate cuts arise.

b) Against this background and the risks within the economic forecast, caution will be adopted with the 2025/26 treasury operations. The Director of Finance will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

• *if it was felt that there was a significant risk of a sharp FALL in borrowing rates,* then borrowing will be postponed where possible.

• *if it was felt that there was a significant risk of a much sharper RISE in borrowing rates than that currently forecast,* fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the future.

c) Any decisions will be reported to Council or the Executive Committee, as appropriate, at the earliest meeting.

4.5 Policy on borrowing in advance of need

a) Borrowing in advance of need is defined as any borrowing undertaken by the Council which will result in the total external debt exceeding the capital financing requirement (CFR) of the Council for the following twelve month period. This twelve month period is on a rolling twelve month basis.

b) The Council will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed.

c) Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates and will be considered carefully to ensure that value for money can be demonstrated and that the Council can ensure the security of such funds.

d) The Director of Finance has the authority to borrow in advance of need under delegated power where, for instance, a sharp rise in interest rates is expected, and so borrowing early at fixed interest rates will be economically beneficial or meet budgetary constraints. The Director of Finance will adopt a cautious approach to any such borrowing and a business case to support the decision making process must consider:

- the benefits of borrowing in advance,
- the risks created by additional levels of borrowing and investment, and
- how far in advance it is reasonable to borrow considering the risks identified

e) Any such advance borrowing will be reported through the mid-year or annual Treasury Management reporting mechanism.

4.6 Debt Rescheduling

a) All rescheduling will be reported to Council or the Executive Committee, as appropriate, at the earliest meeting following its action.

4.7 New financial institutions as a source of borrowing and/or types of borrowing

a) Currently the PWLB Certainty Rate is set at gilts + 80 basis points for non-Housing Revenue Account borrowing. However, consideration may still need to be given to sourcing funding from the following sources for the following reasons:

- Local authorities (primarily shorter dated maturities out to 3 years or so – still cheaper than the Certainty Rate).
- Financial institutions (primarily insurance companies and pension funds but also some banks, out of forward dates where the objective is to avoid a "cost of carry" or to achieve refinancing certainty over the next few years).
- Municipal Bonds Agency (possibly still a viable alternative depending on market circumstances prevailing at the time).

b) Our advisors will keep us informed as to the relative merits of each of these alternative funding sources.

5 Annual Investment Strategy

5.1 Investment Objectives and Policy

a) The Council's investment policy implements the requirements of the following:-

- Local Government Investments (Scotland) Regulations 2010, (and accompanying Finance Circular 5/2010);
- CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2021, ("the Code");
- CIPFA Treasury Management Guidance Notes 2021.

b) The Council's primary investment objectives are as follows, in order of importance:

(i) The safeguarding or **security** of the re-payment of principal and interest of investments on a timely basis;
(ii) The **liquidity** of its investments;
(iii) The **returns on investments** that can be realised.

The Council will therefore aim to achieve the optimum return on its investments corresponding with proper levels of security and liquidity. The risk appetite of this Council is low in order to give priority to security of its investments. In the current economic climate it is considered appropriate to keep investments short term to cover cash flow needs, but also to seek out value available in periods up to 12 months with high credit rated financial institutions.

c) Minimum acceptable **credit criteria** are applied to generate a list of highly creditworthy counterparties. This also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the short term and long-term ratings (**Annex I**).

d) **Other information**: ratings will not be the sole determinant of the quality of an institution; it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To achieve this consideration the Council will engage with its advisors to maintain a monitor on market pricing such as "**credit default swaps**" and overlay that information on top of the credit ratings.

e) **Other information sources** used will include the financial press, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.

f) The Council has defined the list of **types of investment instruments** that are permitted investments authorised for use expanding on the risks involved in each type of investment and the mitigating controls in **Annex D and** Annex **E.**

g) **Lending limits**, (amounts and maturity), for each counterparty will be set through applying the matrix table in paragraph 5.3.

h) The Council has engaged **external consultants** to provide expert advice on how to optimise an appropriate balance of security, liquidity and yield, given the risk appetite of this authority in the context of the expected level of cash balances and need for liquidity throughout the year.

i) All investments will be denominated in **sterling.**

j) The Council will also pursue **value for money** in treasury management and will monitor the yield from investment income against appropriate benchmarks for investment performance. Regular monitoring of investment performance will be carried out during the year.

k) The above criteria are unchanged from last year.

5.2 Council Permitted Investments

The proposed criteria for permitted investments are shown in **Annex D** for approval.

5.3 Creditworthiness Policy

a) The Council applies the creditworthiness service provided by the MUFG Corporate Services. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies - Fitch, Moody's and Standard and Poor's. The credit ratings of counterparties are supplemented with the following overlays:

- credit watches and credit outlooks from credit rating agencies;
- Credit Default Swaps (CDS) spreads to give early warning of likely changes in credit ratings;
- sovereign ratings to select counterparties from only the most creditworthy countries.

b) This modelling approach combines credit ratings, and any assigned Watches and Outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads. The end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Council to determine the suggested duration for investments. The Council will therefore use counterparties within the following durational bands:

Creditworthiness Colour Banding	Maximum Investment Duration
Yellow	5 years*
Dark pink	5 years for Ultra short dated bond funds with a credit score of 1.25
Light pink	5 years for Ultra short dated bond funds with a credit score of 1.5
Purple	2 years
Blue	1 year (only applies to nationalised or semi-nationalised UK Banks)
Orange	1 year
Red	6 months
Green	100 days
No colour	not to be used (ie don't invest)

Y	Pi1	Pi2	P	B	O	R	G	N/C
1	1.25	1.5	2	3	4	5	6	7
Up to 5yrs	Up to 5yrs	Up to 5yrs	Up to 2yrs	Up to 1yr	Up to 1yr	Up to 6mths	Up to 100days	No Colour

c) The MUFG Corporate Services creditworthiness service uses a wider array of information than just primary ratings. Furthermore, by using a risk weighted scoring system, it does not give undue preponderance to just one agency's ratings.

d) Typically the minimum credit ratings criteria the Council use will be a Short Term rating (Fitch or equivalents) of F1 and a Long Term rating of A- which is considered to be a strong grade but still susceptible to market conditions. There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances consideration will be given to the whole range of ratings available, or other topical market information, to support their use. More detail is seen in **Annex I**.

e) All credit ratings will be monitored on a real time basis. The Council is alerted to changes to ratings of all three agencies through its use of a creditworthiness service provided by the MUFG Corporate Services.

- if a downgrade results in the counterparty / investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.
- in addition to the use of credit ratings the Council will be advised of information in movements in credit default swap spreads against the iTraxx benchmark and other market data on a daily basis via its Passport website, provided exclusively to it by MUFG Corporate Services Extreme market movements may result in downgrade of an institution or removal from the Council's lending list.

f) Sole reliance will not be placed on the use of this external service. In addition, the Council will also use market data and market information, as well as information on any external support for banks to help support its decision-making process.

g) Significant levels of downgrades to Short and Long-Term credit ratings have not materialised since the crisis in March 2020. In the main, where they did change, any alterations were limited to Outlooks. Nonetheless, when setting minimum sovereign debt ratings, the Council will not set a minimum rating for the UK.

h) Although bank CDS prices, (these are market indicators of credit risk), spiked upwards during the autumn of 2022, they have returned to more average levels since then. However, sentiment can easily shift, so it will remain important to undertake continual monitoring of all aspects of risk and return in the current circumstances. MUFG Corporate Services monitor CDS prices as part of their creditworthiness service to local authorities and the Authority has access to this information via its Link-provided Passport portal.

5.4 Country and Sector Considerations

a) Due care will be taken to consider the country and sector exposure of the Council's investments.

Country Limits

b) The Council has determined that it will only use approved counterparties from the UK and from countries with a minimum sovereign credit rating of AA- from Fitch (or equivalent). The list of countries that qualify using this credit criteria as at the date of this report are shown in Annex F. This list will be added to, or deducted from, by officers should ratings change in accordance with this policy.

c) No more than 10% of the Council's investments will be placed with any non-UK country at any time.

Institutional Sector Limits

d) These institutions must either be UK Local Authorities or UK Incorporated Institutions, UK Banks and Building Societies incorporated in the European Economic Area entitled to accept deposits through a branch in the UK. The Council may also use the UK Government including in the form of gilts and the Debt Management Account Deposit Facility (DMADF).

e) Limits will be applied to the overall amount lent out to any one sector at any one time in order to limit sector specific exposure risk, as follows:

UK Building Societies	£25 m
Banks	£35 m
UK Local Authorities	£40 m
UK Government Debt Management Office	£unlimited
UK Gilts and Treasury Bills	£20 m
Institutions covered by Government Guarantee	£10 m
Part Nationalised Banks	£35 m
Money Market Funds (AAA)	£25 m

These limits will be monitored regularly for appropriateness.

5.5 Individual Institution Monetary Limits

a) The monetary limits for individual institutions on the Council's Counterparty List are as follows:

	Money Limit
UK Building Societies	£5m
Banks	£5m
UK Local Authorities (i)	£40m
UK Government Debt Management Office	Unlimited
UK Gilts & Treasury Bills	£20m
Government Guaranteed Institutions	£2m
AAA rated Money Market Funds	£5m
Council's Own Banker (ii)	£5m

(i) No individual limit will be applied on lending to a UK local authority, other than it must not exceed the relevant sector limit of £40m.

(ii) Further to Sections 5.4 and 5.5, if the rating of the Council's own banker falls below the criteria, the time limit on money deposited with the bank will be reduced to an overnight basis.

b) As mentioned earlier, the treasury function manages the funds of the Council, any subsidiary organisations and the Common Good and Trust Funds. When applying the limits set out in the table above, these limits will apply to the cumulative investment with an institution from the Council and the Common Good Funds and Trust Funds.

Group Limits

c) Limits will be applied to the overall amount lent out to institutions within the same group at any one time in order to limit group specific exposure risk, as follows, and subject to the parent company appearing on Link Groups' creditworthiness list:

Group of Banks	£10m

Council's Own Banker

d) The Council's own banker (currently Royal Bank of Scotland) will be maintained on the Council's counterparty list in situations where rating changes may mean this is below the above criteria. This is to allow the Council to continue to operate normal current account banking facilities and overnight and short-term investment facilities. However, if the rating does change below the criteria, officers will review the situation carefully and identify any appropriate action required to manage the risk that this change creates for the Council.

5.6 Types of Investments

a) For institutions on the approved counterparty list, investments will be restricted to safer instruments (such as deposits). Currently this involves the use of money market funds, the Debt Management Account Deposit Facility (DMADF) and institutions with higher credit ratings than the minimum permissible rating outlined in the investment strategy, as well as the Council's own bank.

b) Where appropriate, investments will be made through approved brokers. The current list of approved brokers comprises:

- BGC Brokers L.P.
- ICAP Securities Limited
- Tradition (UK) Limited

5.7 Investment Strategy and bank rate projections

In-house funds

a) Investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (i.e. rates for investments up to 12 months). Greater returns are usually obtainable by investing for longer periods. The current shape of the yield curve suggests that the risks are relatively balanced between the Bank Rate staying higher for longer, if inflation picks up markedly through 2025 post the 30 October 2024 Budget, or it may be cut quicker than expected if the economy stagnates. The economy only grew 0.1% in Q3 2024, but the CPI measure of inflation is now markedly above the 2% target rate set by the Bank of England's Monetary Policy Committee two to three years forward. Accordingly, while most cash balances are required in order to manage the ups and downs of cash flow , where cash sums can be identified that could be invested for longer periods, the value to be obtained from longer-term investments will be carefully assessed.

- If it is thought that Bank Rate is likely to rise significantly within the time horizon being considered, then consideration will be given to keeping most investments as being short term or variable.
- Conversely, if it is thought that Bank Rate is likely to fall within that time period, consideration will be given to locking in higher rates currently obtainable, for longer periods.

Investment returns expectations

b) The current forecast shown in paragraph 4.3, includes a forecast for Bank Rate to fall to a low of 3.5% by December 2026.

c) The suggested budgeted investment earnings rates for returns on investments placed for periods up to about three months during each financial year are as follows:

Average earnings in each year	Now	Previously
2024/25 (residual)	4.60%	4.25%
2025/26	4.10%	3.35%
2026/27	3.70%	3.10%
2027/28	3.50%	3.25%
2028/29	3.50%	3.25%
Years 6 to 10	3.50%	3.25%
Years 10+	3.50%	3.50%

Investment Treasury Indicator and Limit (Treasury Indicator TI-5)

d) This indicator is concerned with total principal funds invested with a maturity date of greater than 365 days. These limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment, and are based on the availability of funds after each year end.

The Council is asked to approve the treasury indicator and limit:

Maximum principal sums invested for longer than 365 days (TI-5)						
£m	2024/25	2025/26	2026/27	2027/28	2028/29	2029/30
Principal sums invested for longer than 365 days	20%	20%	20%	20%	20%	20%

e) For positive cash balances and in order to maintain liquidity, the Council will use overnight investment accounts, short term (← 1 month) notice accounts, money market funds and short-dated deposits (overnight to three months).

5.8 Investment Risk Benchmarking

These benchmarks are simple guides to maximum risk, so they may be breached from time to time, depending on movements in interest rates and counterparty criteria. The purpose of the benchmark is for officers to monitor the current and trend position and amend the operational strategy to manage risk as conditions change. Any breach of the benchmarks will be reported, with supporting reasons in the mid-year or Annual Report.

a) Security

Historic Risk of Default is a proxy for the average % risk for each investment based on over 30 years of data provided by Fitch, Moody's and S&P.
The Council's **maximum** security risk for the current portfolio, when compared to historic default tables, is:
0.002% historic risk of default when compared to the whole portfolio.

b) Liquidity

In respect of this area the Council seeks to maintain:

- Bank Overdraft: £250,000
- Liquid short term deposits of at least £1,500,000 available with a week's notice.
- Weighted Average Life is **expected to be 0.5 years** (equivalent to a weighted average life of 6 months), with a **maximum of 1.00 years**

c) Yield

Local measures of yield are:

Investments – **Internal returns above the 365 day backward looking SONIA (Sterling Overnight Index Average) uncompounded rate**

At the end of the financial year, the Council will report on its investment activity as part of the Annual Treasury Report.

6 Performance Indicators

6.1 The CIPFA Code requires the Council to set performance indicators to assess the adequacy of the treasury function over the year. These are distinct historic indicators, as opposed to the prudential indicators, which are predominantly forward looking.

6.2 Investment Risk Benchmark Indicators for Security, Liquidity and Yield, as set out in paragraph 5.8.

6.3 Loans Charges

a) Loans Charges for 2024/25 are expected to be at or below the Revenue Budget estimate contained in the Council's Financial Plans to be approved in February 2025, which are estimated as follows:

£m	2024/25	2025/26	2026/27	2027/28	2028/29	2029/30
Total Loan Charges *	18.3	23.4	27.1	30.3	32.5	34.1

**Total Loan Charges exclude the capital element of PPP repayments.*

b) The expected outturn for 2024/25 reflects the continuing higher interest rates.

6.4 The indicators, based on actual performance for the year, will be included in the Treasury Management Annual Report for 2025/26.

ANNEXES

ANNEX A
SUMMARY OF PRUDENTIAL AND TREASURY INDICATORS

Indicator ref	Indicator	Page Ref.	2024/25	2025/26	2026/27	2027/28	2028/29	2029/30
PRUDENTIAL INDICATORS								
Capital Expenditure Indicator								
PI-1	Capital Expenditure Limits (£m)	10	113.2	98.8	72.4	65.5	27.6	26.6
PI-2	Capital Financing Requirement (CFR) (£m)	12	479.4	522.2	551.1	571.3	562.0	550.7
Affordability Indicator								
PI-3	Ratio of Financing Costs to Net Revenue (inc. capital PPP repayment costs)	32	7.0%	8.0%	8.8%	9.6%	9.8%	9.7%
PI-4	Incremental movement of Capital Investment Decisions on Council Tax		£(0.01)	£0.01	£0.02	£0.03	£0.02	£0.01
External Debt Indicators								
PI-5	Actual Debt (£m)	14	411.0	451.6	477.4	493.2	482.0	462.8
PI-7a	Operational Boundary (inc. Other Long Term Liabilities) (£m)	15	509.2	530.8	521.5	507.9	494.9	475.7
PI-7b	Operational Boundary (exc. Other Long Term Liabilities) (£m)	15	434.0	459.9	454.9	445.5	436.7	421.7
PI-8a	Authorised Limit (inc. Other Long Term Liabilities) (£m)	16	636.5	663.5	651.9	634.8	618.7	594.6
PI-8b	Authorised Limit (exc. Other Long Term Liabilities) (£m)	16	561.3	592.6	585.3	572.4	560.5	540.6
Indicators of Prudence								
PI-6	(Under)/Over Gross Borrowing against the CFR (£m)	14	(140.1)	(119.7)	(84.6)	(57.5)	(56.5)	(63.0)
TREASURY INDICATORS								
TI-1	Upper Limit to Fixed Interest Rates based on Net Debt (£m)	33	509.2	530.8	521.5	507.8	494.9	475.7
TI-2	Upper Limit to Variable Interest Rates based on Net Debt (£m)	33	178.2	185.8	182.5	177.7	173.2	166.5
TI-3	Maturity Structure of Fixed Interest Rate Borrowing 2023/24	33	Lower		Upper			
	Under 12 months		0%		20%			
	12 months to 2 years		0%		20%			
	2 years to 5 years		0%		20%			
	5 years to 10 years		0%		20%			
	10 years and above		20%		100%			
TI-5	Maximum Principal Sum invested greater than 365 days	27	20%	20%	20%	20%	20%	20%

Further prudential indicators are required to assess the affordability of the capital investment plans. These provide an indication of the impact of the capital investment plans on the Council's overall finances. The updated indicators are as follows:

Ratio of financing costs to net revenue stream (Prudential Indicator PI-3)

This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs, net of investment income) against the net revenue stream.

%	Actual	Estimate					
	23/24	24/25	25/26	26/27	27/28	28/29	29/30
Ratio of Financing Costs to Net Revenue Stream (PI-3) *(inc. capital PPP repayment costs)*	7.9%	7.0%	8.0%	8.8%	9.6%	9.8%	9.7%

The estimates of financing costs include current commitments, the revisions due to the rebasing of the service concession arrangements and the proposals in the 2025/26 Financial Plan. The movements in the above ratio from 2024/25 onwards reflect an increasing proportion of the Council's revenue budget being directed to loans charges.

Treasury Management Limits on Activity

There are three debt related treasury activity limits. The purpose of these are to restrain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of any adverse movement in interest rates. However, if these are set to be too restrictive, they will impair the opportunities to reduce costs / improve performance. The indicators are:

(i) **Upper limits on fixed interest rate exposure (Treasury Indicator TI-1)**

This identifies a maximum limit for borrowing exposure to fixed interest rates, based on the debt position net of investments. This is set with reference to the Operational Boundary (PI-7a).

(ii) **Upper limits on variable interest rate exposure (Treasury Indicator TI-2)**

This identifies a maximum limit for borrowing exposure to variable interest rates based upon the debt position net of investments. This is set with reference to 35% of the Operational Boundary (PI-7a)

(iii) **Maturity structure of borrowing (Treasury Indicator TI-3)**

These gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing, and are required for upper and lower limits.

(iv) The following table highlights the proposed treasury indicators and limits:

£m	2024/25	2025/26	2026/27	2027/28	2028/29	2029/30
Interest rate exposures						
	Upper	Upper	Upper	Upper	Upper	Upper
Limits on fixed interest rates based on net debt (TI-1)	509.2	530.8	521.5	507.8	494.9	475.7
Limits on variable interest rates based on net debt (TI-2)	178.2	185.8	182.5	177.7	173.2	166.5

Maturity Structure of fixed interest rate borrowing 2024/25 (TI-3)		
	Lower	Upper
Under 12 months	0%	20%
12 months to 2 years	0%	20%
2 years to 5 years	0%	20%
5 years to 10 years	0%	20%
10 years and above	20%	100%

ANNEX B: INTEREST RATE FORECASTS 2024-27

[PWLB rates and forecast shown below have taken into account the 20 basis point certainty rate reduction effective as of the 1st November 2012.] There are no changes to these forecasts as at 30.01.25.

Link Group Interest Rate View	11.11.24												
	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27	Jun-27	Sep-27	Dec-27
BANK RATE	4.75	4.50	4.25	4.00	4.00	3.75	3.75	3.75	3.50	3.50	3.50	3.50	3.50
3 month ave earnings	4.70	4.50	4.30	4.00	4.00	4.00	3.80	3.80	3.80	3.50	3.50	3.50	3.50
6 month ave earnings	4.70	4.40	4.20	3.90	3.90	3.90	3.80	3.80	3.80	3.50	3.50	3.50	3.50
12 month ave earnings	4.70	4.40	4.20	3.90	3.90	3.90	3.80	3.80	3.80	3.50	3.50	3.50	3.50
5 yr PWLB	5.00	4.90	4.80	4.60	4.50	4.50	4.40	4.30	4.20	4.10	4.00	4.00	3.90
10 yr PWLB	5.30	5.10	5.00	4.80	4.80	4.70	4.50	4.50	4.40	4.30	4.20	4.20	4.10
25 yr PWLB	5.60	5.50	5.40	5.30	5.20	5.10	5.00	4.90	4.80	4.70	4.60	4.50	4.50
50 yr PWLB	5.40	5.30	5.20	5.10	5.00	4.90	4.80	4.70	4.60	4.50	4.40	4.30	4.30

Interest Rate Forecasts								
Bank Rate	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26
MUFG CM	4.50%	4.25%	4.00%	4.00%	3.75%	3.75%	3.75%	3.50%
Cap Econ	4.50%	4.25%	4.00%	3.75%	3.50%	3.50%	3.50%	3.50%
5Y PWLB RATE								
MUFG CM	4.90%	4.80%	4.60%	4.50%	4.50%	4.40%	4.30%	4.20%
Cap Econ	5.10%	4.90%	4.80%	4.60%	4.60%	4.50%	4.50%	4.40%
10Y PWLB RATE								
MUFG CM	5.10%	5.00%	4.80%	4.80%	4.70%	4.50%	4.50%	4.40%
Cap Econ	5.30%	5.10%	5.00%	4.80%	4.80%	4.70%	4.60%	4.60%
25Y PWLB RATE								
MUFG CM	5.50%	5.40%	5.30%	5.20%	5.10%	5.00%	4.90%	4.80%
Cap Econ	5.70%	5.50%	5.30%	5.00%	4.90%	4.90%	4.80%	4.70%
50Y PWLB RATE								
MUFG CM	5.30%	5.20%	5.10%	5.00%	4.90%	4.80%	4.70%	4.60%
Cap Econ	5.30%	5.20%	5.20%	5.10%	5.00%	4.90%	4.80%	4.80%

Source: MUFG Corporate Markets January 2025

ANNEX C: ECONOMIC BACKGROUND – supplied by MUFG Corporate Markets

The third quarter of 2024/25 (October to December) saw:

- GDP growth contracting by 0.1% m/m in October following no growth in the quarter ending September;
- The 3myy rate of average earnings growth increase from 4.4% in September to 5.2% in October;
- CPI inflation increase to 2.6% in November;
- Core CPI inflation increase from 3.3% in October to 3.5% in November;
- The Bank of England cut interest rates from 5.0% to 4.75% in November and held them steady in December.
- 10-year gilt yields starting October at 3.94% before finishing up at 4.57% at the end of December (peaking at 4.64%).

The 0.1% m/m fall in GDP in October was the second such decline in a row and meant that GDP would need to rise by 0.1% m/m or more in November and December, for the economy to grow in Q4 as a whole rather than contract. With on-going concern over the impact of the October budget and drags from higher interest rates and weak activity in the euro zone, our colleagues at Capital Economics have revised down their forecast for GDP growth in 2025 to 1.3% (it was initially 1.8% in the immediate wake of the Budget.)

This quarter saw the composite activity Purchasing Manager Index (PMI) dip below the level of 50 that separates expansion from contraction for the first time since October 2023. Although December's composite PMI came in above this level, at 50.5, this was still consistent with the 0% rise in real GDP in Q3 being followed by a flat-lining, or potential contraction, in the final quarter of 2024. However, the economy is unlikely to be quite as weak as that given that the PMIs do not capture rises in government spending, but the data does underline the continued divergence in trends between the manufacturing and services sectors. The manufacturing PMI fell for its fourth consecutive month in December, from 48.0 in November to 47.3. That's consistent with manufacturing output falling by 1.5% q/q in the final quarter of 2024 after flatlining through the summer months. This weakness in the manufacturing sector was offset by a rebound in the services sector. The services PMI rose from 50.8 in November to 51.4 in December, which is consistent with non-retail services output growth increasing from +0.1% q/q to +0.3% for October - December. This suggests that more of the recent slowdown in GDP is being driven by the weakness in activity overseas rather than just domestic factors. Additionally, the services output prices balance rose for the third consecutive month, from 55.4 in November to 56.9, showing signs that price pressures are reaccelerating.

After rising by 1.4% q/q in July - September, the retail sector had a difficult final quarter of the year. Indeed, the bigger-than-expected 0.7% m/m fall in retail sales in October (consensus forecast -0.3% m/m) suggested that households' concerns about expected tax rises announced in the Budget on 30th October contributed to weaker retail spending at the start of the quarter. The monthly decline in retail sales volumes in October was reasonably broad based, with sales in five of the seven main sub sectors slipping. However, the potential for seasonally adjusted sales to rise in November - if October's figures were impacted by the timing of the school half term – combined with a rebound in consumer confidence and rising real incomes, points to some promise to the final quarter of 2024.

The Government's October budget outlined plans for a significant £41.5bn (1.2% of GDP) increase in taxes by 2029/30, with £25bn derived from a 1.2% rise in employers' national insurance contributions. The taxes are more than offset by a £47bn (1.4% of GDP) rise in current (day-to-day) spending by 2029/30 and a £24.6bn (0.7% of GDP) rise in public investment, with the latter being more than funded by a £32.5bn (1.0% of GDP) rise in public borrowing. The result is that the Budget loosens fiscal policy relative to the previous government's plans - although fiscal policy is still being tightened over the next five years – and that GDP growth is somewhat stronger over the coming years than had previously been forecasted. By way of comparison, the Bank of England forecasts four-quarter GDP growth to pick up to almost 1¾% through 2025 (previously forecast to be 0.9%) before falling back to just over 1% in 2026.

December's pay data showed a rebound in wage growth that will likely add to the Bank of England's inflationary concerns. The 3myy rate of average earnings growth increased from 4.4% in September (revised up from 4.3%) to 5.2% in October (consensus forecast 4.6%) and was mainly due to a rebound in private sector pay growth from 4.6% to 5.4%. Excluding bonuses, public sector pay stagnated in October and the 3myy rate fell from 4.7% to 4.3%.

The number of job vacancies also fell again from 828,000 in the three months to October to 818,000 in the three months to November. This marks the first time it has dropped below its pre-pandemic February 2020 level of 819,000 since May 2021. Despite this, the Bank of England remains concerned about the inflationary influence of high wage settlements as well as the risk of a major slowdown in labour market activity.

CPI inflation has been on the rise this quarter, with the annual growth rate increasing from 1.7% in September to 2.3% in October, before rising further to 2.6% in November. Although services CPI inflation stayed at 5.0% in November, the Bank had expected a dip to 4.9%, while the timelier three-month annualised rate of services CPI rose from 5.0% to 5.1%. That shows that there currently isn't much downward momentum. Moreover, the wider measure of core CPI inflation rose from 3.3% to 3.5% in November. Both services and core inflation are currently at rates well above those consistent with the 2.0% target and are moving in the wrong direction. Capital Economics forecast that after dipping to 2.5% in December, CPI inflation will rise further in January, perhaps to 2.8%. Although CPI inflation is expected to be back at close to the 2.0% target by the end of 2025, given that a lot of the rise in inflation in the coming months will be due to base effects that won't persist, the potential for a broader set of tariffs to arise from the US as well as the constant threat of geo-political factors to impact energy and food prices suggest risks remain very much to the upside.

Throughout the quarter gilt yields have risen. The 10-year gilt yield increased from 3.94% at the start of October to 4.57% by the year end (and has subsequently risen to 4.64% early in 2025). As recently as mid-September 10-year gilt yields were at their low for the financial year, but since then, and specifically after the Budget at the end of October, yields have soared. Overall, the reaction to the UK Budget highlights how bond markets are both fragile and highly attentive to news about the fiscal outlook.

The FTSE 100 started off this quarter at 8,276, before finishing up at 8,121. In particular, UK markets have continued to fall further behind US equities, a trend which has accelerated since Trump's election victory in November, partly due to the UK stock market being less exposed to AI hype, and it being weighed down by its relatively large exposure to the energy and materials sectors.

MPC meetings: 9 May, 20 June, 1 August, 19 September 7th November & 18th December 2024

- On 9 May, the Bank of England's Monetary Policy Committee (MPC) voted 7-2 to keep Bank Rate at 5.25%. This outcome was repeated on 20th June.
- However, by the time of the August meeting, there was a 5-4 vote in place for rates to be cut by 25bps to 5%. However, subsequent speeches from MPC members have supported Governor Bailey's tone with its emphasis on "gradual" reductions over time.
- Markets thought there may be an outside chance of a further Bank Rate reduction in September, following the 50bps cut by the FOMC, but this came to nothing.
- On 7 November, Bank Rate was cut by 0.25% to 4.75%. The vote was 8-1 in favour of the cut but the language used by the MPC emphasised "gradual" reductions would be the way ahead with an emphasis on the inflation and employment data releases, as well as geo-political events.
- At the 18 December meeting, another split vote arose. Members voted 6-3 to keep Bank Rate on hold at 4.75%, but dissenters (Dhingra, Ramsden and Taylor) were keen for rates to be cut further as concerns over the slowing down of the UK economy took root, despite near-term inflation fears remaining.
- The MPC again stated that "a gradual approach" to rate cuts "remains appropriate" and that policy will "remain restrictive for sufficiently long".

PWLB maturity Certainty Rates 1st April to 31st December 2024

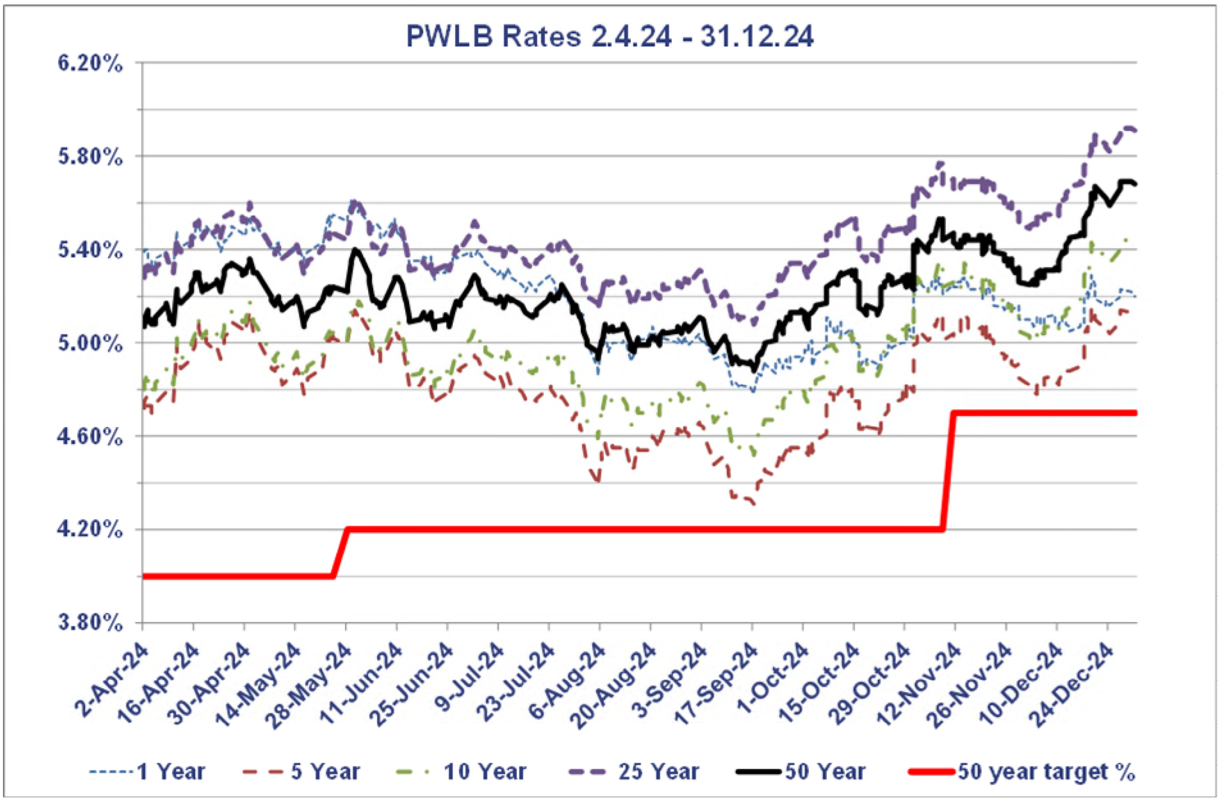
Medium and longer-dated gilt yields, and therein PWLB rates, have moved significantly higher over the course of the financial year, culminating in long-term rates approaching levels last seen in 1998. The rise in medium to long-term yields has arisen because of several factors. Namely, the inflation outlook has become stickier than the market anticipated earlier in the year, with wages remaining somewhat elevated (currently increases are c5% y/y) and the labour market tight (unemployment a little above 4% and job vacancies more than 800,000).

Moreover, the Government has not fully convinced the markets that the UK economy is about to undergo a material increase in productivity and growth. The quarter ending 30th September saw UK GDP stagnate and the prospects for 2025 are somewhat opaque at present. With the UK public finances seemingly under pressure too (as of 7th January, it is estimated that the Chancellor's October Budget contingency is less than £1bn following the recent rise in gilt yields), and historic buyers of longer-dated gilts – pension funds and insurance companies – targeting shorter-dated maturities of late, it is not that great a surprise that yields have risen in the longer dates even as the Debt Management Office has sought to issue debt with shorter durations than might normally have been the case.

There is also anecdotal evidence that hedge funds, who are not long-term holders of long-dated debt issuance, as a rule, may be more active in this part of the market than has normally been the case. Their presence, arguably, adds volatility to the equation. Consequently, and pulling all these factors together, and it is clear that any signs of public finance weakness could lead to elevated yields from time to time.

Additionally, US Treasury yields have also risen prior to Donald Trump's inauguration as US President on 20th January. Markets are nervous as to what the effect of deportation, tariff and tax-cutting policies will have on inflation. Given the impact US markets have globally, this is another contributing factor to the near-term rise in UK yields. The hope is that when the "unknowns" become known, markets will behave in a calmer fashion and yields fall back. But that is not certain.

In the chart below, PWLB rates, have moved significantly higher over the course of the financial year, culminating in long-term rates approaching levels last seen in 1998.



HIGH/LOW/AVERAGE PWLB RATES FOR 02.04.24 – 31.12.24

	1 Year	5 Year	10 Year	25 Year	50 Year
02/04/2024	5.39%	4.72%	4.80%	5.28%	5.07%
31/12/2024	5.20%	5.12%	5.43%	5.91%	5.68%
Low	4.78%	4.31%	4.52%	5.08%	4.88%
Low date	17/09/2024	17/09/2024	17/09/2024	17/09/2024	17/09/2024
High	5.61%	5.16%	5.44%	5.92%	5.69%
High date	29/05/2024	19/12/2024	19/12/2024	19/12/2024	27/12/2024
Average	5.22%	4.80%	4.96%	5.43%	5.21%
Spread	0.83%	0.85%	0.92%	0.84%	0.81%

ANNEX D: TREASURY MANAGEMENT PRACTICE (TMP1)

PERMITTED INVESTMENTS, ASSOCIATED CONTROLS AND LIMITS

This Council approves the forms of investment instrument detailed in **Annex E** for use as permitted investments

Treasury risks

All the investment instruments are subject to the following risks: -

1. **Credit and counter-party risk:** this is the risk of failure by a counterparty (bank or building society) to meet its contractual obligations to the organisation particularly because of the counterparty's diminished creditworthiness, and the resulting detrimental effect on the organisation's capital or current (revenue) resources. There are no counterparties where this risk is zero although AAA rated organisations have the highest, relative, level of creditworthiness.

2. **Liquidity risk:** this is the risk that cash will not be available when it is needed. While it could be said that all counterparties are subject to at least a very small level of liquidity risk as credit risk can never be zero, in this document, liquidity risk has been treated as whether or not instant access to cash can be obtained from each form of investment instrument. However, it has to be pointed out that while some forms of investment e.g. gilts, CDs, corporate bonds can usually be sold immediately if the need arises, there are two caveats: - a. cash may not be available until a settlement date up to three days after the sale b. there is an implied assumption that markets will not freeze up and so the instrument in question will find a ready buyer.

3. **Market risk:** this is the risk that, through adverse market fluctuations in the value of the principal sums an organisation borrows and invests, its stated treasury management policies and objectives are compromised, against which effects it has failed to protect itself adequately. However, some cash rich local authorities may positively want exposure to market risk e.g. those investing in investment instruments with a view to obtaining a long term increase in value.

4. **Interest rate risk**: this is the risk that fluctuations in the levels of interest rates create an unexpected or unbudgeted burden on the organisation's finances, against which the organisation has failed to protect itself adequately. This authority has set limits for its fixed and variable rate exposure in its Treasury Indicators in this report.

5. **Legal and regulatory risk:** this is the risk that the organisation itself, or an organisation with which it is dealing in its treasury management activities, fails to act in accordance with its legal powers or regulatory requirements, and that the organisation suffers losses accordingly.

Controls on treasury risks

1. **Credit and counter-party risk:** this authority has set minimum credit criteria to determine which counterparties and countries are of sufficiently high creditworthiness to be considered for investment purposes. See paragraphs 5.3 and 5.4.

2. **Liquidity risk:** this authority has a cash flow forecasting model to enable it to determine how long investments can be made for and how much can be invested.

3. **Market risk:** this authority does not purchase investment instruments which are subject to market risk in terms of fluctuation in their value.

4. **Interest rate risk**: this authority manages this risk by having a view of the future course of interest rates and then formulating a treasury management strategy accordingly which aims to maximise investment earnings consistent with control of risk or alternatively, seeks to minimise expenditure on interest costs on borrowing. See paragraph 5.7.

5. **Legal and regulatory risk:** this authority will not undertake any form of investing until it has ensured that it has all necessary powers and also complied with all regulations. All types of investment instruments

Unlimited investments

Regulation 24 under the Investment Regulations states that an investment can be shown as being 'unlimited' in terms of the maximum amount or percentage of the total portfolio that can be put into that type of investment. However, it also requires that an explanation must be given for using that category. The authority has given the following types of investment an unlimited category: -

1. **Debt Management Agency Deposit Facility (DMADF).** This offers the lowest risk form of investment available to local authorities as it is effectively an investment placed with the Government. It is also easy to use as it is a deposit account and avoids the complications of buying and holding Government issued treasury bills or gilts. As it is low risk it also earns low rates of interest. However, it is very useful for authorities whose overriding priority is the avoidance of risk. The longest period for a term deposit with the DMADF is 6 months.

Environmental, Social & Governance (ESG) Considerations

This topic is becoming a more commonplace discussion within the wider investment community, including Local Authorities. While around two thirds of councils have declared a "climate emergency" to date, this has not translated into the incorporation of something more formal within their treasury-related Annual Investment Strategy. Changes to the CIPFA TM Code 2021 will see ESG incorporated into Treasury Management Practice 1. The following wording (page 18 of the Treasury Management Code) suggests the scope of what is included: "The organisation's credit and counterparty policies should set out its policy and practices relating to environmental, social and governance (ESG) investment considerations. This is a developing area, and it is not implied that the organisation's ESG policy will currently include ESG scoring or other real-time ESG criteria at individual investment level."

Furthermore, page 50 of the Treasury Management Code states "ESG issues are increasingly significant for investors and investment managers. This is better developed in equity and bond markets than for short-term cash deposits, and there is a diversity of market approaches to ESG classification and analysis. This means that a consistent and developed approach to ESG for public service organisations is currently difficult. Organisations are therefore recommended to consider their credit and counterparty policies in light of ESG information and develop their own ESG investment policies and treasury management practices consistent with their organisation's own relevant policies, such as environmental and climate change policies."

From MUFG Corporate Services perspective, the most important issue is ensuring that there is a clear understanding of what "environmental, social and governance (ESG)" investment considerations means. It is about understanding the ESG "risks" that an entity is exposed to and evaluating how well it manages these risks, (all entities will be subject to these to one extent or other). It is NOT the same as Socially Responsible Investing, (typically where you apply negative screens), and equally, it is NOT the same as Sustainable Investing, (investing in products / companies based on expected sustainable and beneficial societal impact, alongside a financial return).

There is such a huge potential for misunderstanding which could have material unintended consequence i.e., limiting of potential counterparty options, thus decreasing diversification. The above could then lead to authorities widening credit criteria to take on more names, or those with a stronger "ESG" performance, which could then increase credit risk…which would place the cornerstone of prudent investing at risk.

The other factor, i.e., what local authorities can or already do to take this into account, is credit ratings. All the main agencies are now extoling how they incorporate ESG risks alongside more traditional financial risk metrics when assessing counterparty ratings. As such, you could argue that their incorporation is already being done, to an extent, by the use of mainstream rating agencies.

Also, a final note to point out is that given ESG risks are all about potential impact on entity enterprise value; the "G" (governance) is by far the most important one when considering treasury investments, the majority of which will be shorter-term in nature. This is because poor governance can have a more immediate impact on the financial circumstances of an entity and the potential for a default event that would impact the amount the local authorities receive back from their investments. Those financial institutions that are viewed as having poor/weak corporate governance are generally less well rated in the first instance or have a higher propensity for being subject to negative rating action. So, this element of ESG is of high importance to an investor that is following investment guidance with the security, liquidity and yield (SLY) principle at its core. Environmental & Social factors are also important, but more for the long-term impact, unless you are specifically going down the "impact" / "sustainable" type investment route…and there are not many options for that in respect of short-term investments.

Naturally, MUFG Corporate Services continues to look at ways in which we can incorporate these factors into our creditworthiness assessment service. However, the lack of consistency, as well as uncertainty as to how the Treasury Management Code may develop TMP1, means that although we continue to review the options and will update clients as progress is made, it is not practicable to expand broadly upon ESG matters at the current time.

ANNEX E: CREDIT AND COUNTERPARTY RISK MANAGEMENT (TMP 1 continued)

Permitted Investments, Associated Controls and Limits for Scottish Borders Council, Common Good and Trust Funds and In-house Managed Pension Fund

Type of Investment	Treasury Risks	Mitigating Controls	Council Limits	Common Good & Trust Funds Limits	Pension Fund In-house Limits
Cash type instruments					
a. Deposits with the Debt Management Account Facility (UK Government) (Very low risk)	This is a deposit with the UK Government and as such counterparty and liquidity risk is very low, and there is no risk to value. Deposits can be between overnight and 6 months.	Little mitigating controls required. As this is a UK Government investment the monetary limit is unlimited to allow for a safe haven for investments.	£unlimited, maximum 6 months	£unlimited, maximum 6 months	£unlimited, maximum 6 months
b. Deposits with other local authorities or public bodies (Very low risk)	These are considered quasi-UK Government debt and as such counterparty risk is very low, and there is no risk to value. Liquidity may present a problem as deposits can only be broken with the agreement of the counterparty, and penalties can apply. Deposits with other non-local authority bodies will be restricted to the overall credit rating criteria.	Little mitigating controls required for local authority deposits, as this is a quasi-UK Government investment. Non-local authority deposits will follow the approved credit rating criteria.	£40m and maximum 1 year	£5m and maximum 1 year	£40m and maximum 1 year
c. Money Market Funds (MMFs) (very low risk)	Pooled cash investment vehicle which provides very low counterparty, liquidity and market risk. These will primarily be used as liquidity instruments.	Funds will only be used where the MMFs has a “AAA” rated status from either Fitch, Moody’s or Standard and Poor’s.	£5m per fund/£25m total	£5m per fund/£25m total	£5m per fund/£25m total

Type of Investment	Treasury Risks	Mitigating Controls	Council Limits	Common Good & Trust Funds Limits	Pension Fund In-house Limits
d. Ultra-short dated bond funds **(low risk)**	Pooled cash investment vehicle which provides very low counterparty, liquidity and market risk. These will primarily be used as liquidity instruments.	Funds will only be used where they have a "AAA" rated status from either Fitch, Moody's or Standard and Poor's.	N/A	N/A	N/A
e. Call account deposit accounts with financial institutions (banks and building societies) **(Low risk depending on credit rating)**	These tend to be low risk investments but will exhibit higher risks than categories (a), (b) and (c) above. Whilst there is no risk to value with these types of investments, liquidity is high and investments can be returned at short notice.	The counterparty selection criteria approved above restricts lending only to high quality counterparties, measured primarily by credit ratings from Fitch, Moody's and Standard and Poor's. Day to day investment dealing with these criteria will be further strengthened by use of additional market intelligence.	As shown in the counterparty section criteria above	As shown in the counterparty section criteria above	As shown in the counterparty section criteria above
f. Term deposits with financial institutions (banks and building societies) **(Low to medium risk depending on period & credit rating)**	These tend to be low risk investments but will exhibit higher risks than categories (a), (b) and (c) above. Whilst there is no risk to value with these types of investments, liquidity is low and term deposits can only be broken with the agreement of the counterparty, and penalties may apply.	The counterparty selection criteria approved above restricts lending only to high quality counterparties, measured primarily by credit ratings from Fitch, Moody's and Standard and Poor's. Day to day investment dealing with these criteria will be further strengthened by use of additional market intelligence.	As shown in the counterparty section criteria above	As shown in the counterparty section criteria above	As shown in the counterparty section criteria above

Type of Investment	Treasury Risks	Mitigating Controls	Council Limits	Common Good & Trust Funds Limits	Pension Fund In-house Limits
g. Government Gilts and Treasury Bills (Very low risk)	These are marketable securities issued by the UK Government and as such counterparty and liquidity risk is very low, although there is potential risk to value arising from an adverse movement in interest rates (no loss if these are held to maturity.	Little counterparty mitigating controls are required, as this is a UK Government investment. The potential for capital loss will be reduced by limiting the maximum monetary and time exposures.	£20m, maximum 1 year	£5m, maximum 1 year	£20m, maximum 1 year
Other types of investments					
a. Investment properties	These are non-service properties which are being held pending disposal or for a longer term rental income stream. These are highly illiquid assets with high risk to value (the potential for property prices to fall or for rental voids).	In larger investment portfolios some small allocation of property-based investment may counterbalance/compliment the wider cash portfolio. Property holding will be revalued regularly and reported annually with gross and net rental streams	£30m	£25m	N/A
b. Loans to third parties, including soft loans	These are service investments either at market rates of interest or below market rates (soft loans). These types of investments may exhibit credit risk and are likely to be highly illiquid.	Each third party loan requires Member approval and each application is supported by the service rational behind the loan and the likelihood of partial or full default.	£25m	£1m	N/A

Type of Investment	Treasury Risks	Mitigating Controls	Council Limits	Common Good & Trust Fund Limits	Pension Fund In-house Limits
c. Loans to a local authority company	These are service investments either at market rates of interest or below market rates (soft loans). These types of investments may exhibit credit risk and are likely to be highly illiquid.	Each loan to a local authority company requires Member approval and each application is supported by the service rational behind the loan and the likelihood of partial or full default.	£25m	N/A	N/A
d. National Housing Trust (Very Low Risk due to Scottish Government Underwriting Shareholdings in a local authority company	These are loans to a Special Purpose Vehicle to allow it to purchase new homes under the NHT umbrella. These loans represent either 65% or 70% of the purchase price, the remainder being funded by the developer. The loan is redeemed after a 5 to 10 year period when the properties are sold. These are service investments which may exhibit market risk and are likely to be highly illiquid.	Loan redemption arises when the homes are sold. Interest payments are made to the Council by the SPV from rental payments in the intervening period. Both the loan amount and associated interest payments are underwritten by Scottish Government.	£8m	N/A.	N/A
e. Shareholdings in a local authority company	These are service investments which may exhibit market risk and are likely to be highly illiquid.	Each equity investment in a local authority company requires Member approval and each application will be supported by the service rational behind the investment and the likelihood of loss.	£1m	N/A	N/A

Type of Investment	Treasury Risks	Mitigating Controls	Council Limits	Common Good & Trust Fund Limits	Pension Fund In-house Limits
f. Investment in the Subordinated Debt of projects delivered via the ‘HubCo’ model **(Very Low Risk)**	These are investments that are exposed to the success or failure of individual projects and are highly illiquid.	The Council and Scottish Government (via the SFT) are participants in and party to the governance and controls within the project structure. As such they are well placed to influence and ensure the successful completion of the project’s term. These projects are based on robust business cases with a cashflow from public sector organisations (i.e. low credit risk)	£600,000	N/A	N/A

The Monitoring of Investment Counterparties

The status of counterparties will be monitored regularly. The Council receives credit rating and market information from MUFG Corporate Services, including when ratings change, and counterparties are checked promptly. On occasion ratings may be downgraded when an investment has already been made. The criteria used are such that a minor downgrading should not affect the full receipt of the principal and interest. Any counterparty failing to meet the criteria will be removed from the list immediately by the Director of Finance, and if required new counterparties which meet the criteria will be added to the list.

Use of External Fund Managers

It is the Council’s policy to use external fund managers to manage the investment portfolios of the Scottish Borders Council Pension Fund and the pooled investment fund of the Common Good and Trust Funds. This Annex reflects the approved policies around the Common Good and Trust Fund Investment Strategy but specifically excludes, as allowed by regulations, the work undertaken by External Fund Managers in relation to the Scottish Borders Council Pension Fund.

ANNEX F: APPROVED COUNTRIES FOR INVESTMENTS

This list is based on those countries which have sovereign ratings of AA- or higher, (we show the lowest rating from Fitch, Moody's and S&P) and have banks operating in sterling markets which have credit ratings of green or above in the MUFG Corporate Services creditworthiness service.

Based on lowest available rating

AAA

a) Australia
b) Denmark
c) Germany
d) Netherlands
e) Norway
f) Singapore
g) Sweden
h) Switzerland

AA+

i) Canada
j) Finland
k) U.S.A.

AA

l) Abu Dhabi (UAE)
m) Qatar

AA-

n) Belgium
o) France
p) U.K.

[Ratings provided by MUFG Corporate Services as at 31 December 2024]

ANNEX G: SCHEME OF DELEGATION

Full Council

- receiving and reviewing reports on treasury management policies, practices and activities;
- approval of annual strategy.

Full Council or Executive Committee, as appropriate

approval of/amendments to the organisation's adopted clauses, treasury management policy statement and treasury management practices;

- budget consideration and approval;
- approval of the division of responsibilities;
- receiving and reviewing regular monitoring reports and acting on recommendations;
- approving the selection of external service providers and agreeing terms of appointment.

Audit Committee

- reviewing the treasury management policy and procedures and making recommendations to the responsible body.

THE TREASURY MANAGEMENT ROLE OF THE SECTION 95 OFFICER

The S95 (responsible) officer

- Take and/or authorise all operational decisions regarding the Council's investments and borrowing, in accordance with approved Treasury Management Strategy.
- Responsible for execution and administration of treasury management decisions in accordance with the Council's Treasury Management Strategy, and if (s)he is a CIPFA member, CIPFA's Standard of Professional Practice on Treasury Management.
- In terms of Treasury Management, from time to time, formulate suitable criteria for assessing and monitoring the credit risk of investment counterparties and construct a lending list defining appropriate limits.
- Borrow, in advance of need, where, for instance, a sharp rise in interest rates is expected, and so borrowing early at fixed interest rates will be economically beneficial or meet budgetary constraints. Adopt a cautious approach to any such borrowing, and a business case to support the decision-making process must consider:
    - the benefits of borrowing in advance,
    - the investment risks created by the existence of investments at the same time as additional borrowing being outstanding; and
    - how far in advance it is reasonable to borrow, considering the risks identified. Any such advance borrowing shall be reported through the mid-year or annual Treasury Management reporting mechanism.
- Take the most appropriate form of borrowing depending on the prevailing interest rates at the time, taking into account the risks shown in the forecast contained in the Treasury Management Strategy.
- Maintain a counterparty list consistent with the Investment Counterparty Selection Criteria and revise the criteria and submit them to Committee for approval as necessary, and in addition, set out the types of investment to be made (Permitted Investments).

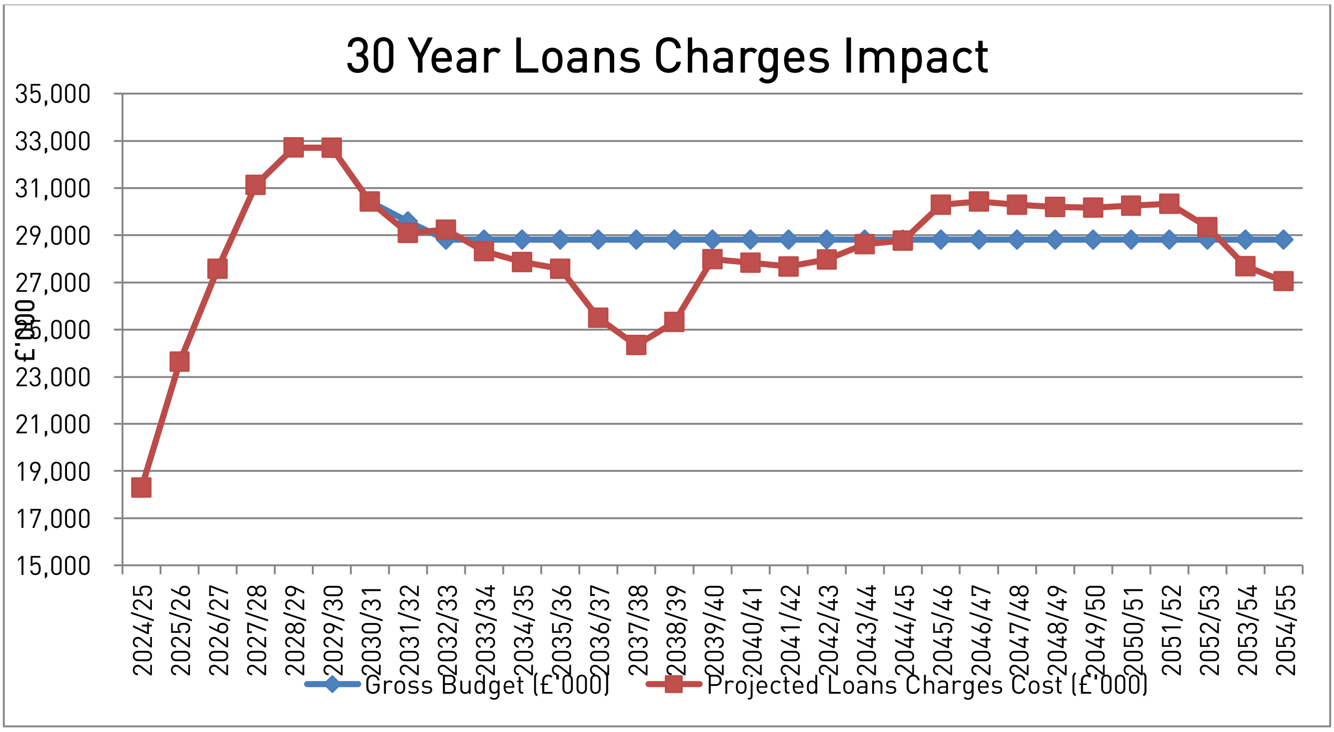
- Preparation of a capital strategy to include capital expenditure, capital financing, non-financial investments and treasury management, with a long-term timeframe
- Ensuring that the capital strategy is prudent, sustainable, affordable and prudent in the long term and provides value for money.
- Ensuring that due diligence has been carried out on all treasury and non-financial investments and is in accordance with the risk appetite of the Council.
- Ensure that the Council has appropriate legal powers to undertake expenditure on non-financial assets and their financing.
- Ensuring the proportionality of all investments so that the Council does not undertake a level of investing which exposes the authority to an excessive level of risk compared to its financial resources.
- Ensuring that an adequate governance process is in place for the approval, monitoring and ongoing risk management of all non-financial investments and long term liabilities.
- Provision to members of a schedule of all non-treasury investments including material investments in subsidiaries, joint ventures, loans and financial guarantees ensuring that members are adequately informed and understand the risk exposures taken on by the Council.
- Ensuring that the Council has adequate expertise, either in house or externally provided, to carry out the above.
- Creation of Treasury Management Practices which specifically deal with how non-treasury investments will be carried out and managed, to include the following ***(TM Code p54):*** -
    - *Risk management (TMP1 and schedules), including investment and risk management criteria for any material non-treasury investment portfolios;*
    - *Performance measurement and management (TMP2 and schedules), including methodology and criteria for assessing the performance and success of non-treasury investments;*
    - *Decision making, governance and organisation (TMP5 and schedules), including a statement of the governance requirements for decision making in relation to non-treasury investments; and arrangements to ensure that appropriate professional due diligence is carried out to support decision making;*
    - *Reporting and management information (TMP6 and schedules), including where and how often monitoring reports are taken;*
    - *Training and qualifications (TMP10 and schedules), including how the relevant knowledge and skills in relation to non-treasury investments will be arranged.*

ANNEX H

Long Term (30 Year) Loans Charges Analysis

Current capital and revenue plans have been extrapolated over a 30 year period in order to assess the impact on the revenue Loans Charges budget. In line with assumptions made when assessing external debt and associated limits, long term capital planning will create an increasing charge which will require to be addressed through the revenue financial planning process. Movements in notional loans charges associated with internal borrowing also impact on these figures.

It should be noted that from 2035-36, the first year outwith the current 10 year Capital Plan, a 10 year average capital expenditure, and annual borrowing requirement of £10.5m, has been assumed and the gross budget remains at the 2032-33 amount.



ANNEX I: CREDIT RATINGS

Long and Short Term Credit Ratings

Audit Commission Grading#	Fitch		Moody's		Standard and Poor's	
	Long Term	Short Term	Long Term	Short Term	Long Term	Short Term
Extremely strong grade	AAA	F1+	Aaa	P-1	AAA	A-1+
Very strong grade	AA+ AA AA-	F1+ F1+ F1+	Aa1 Aa2 Aa3	P-1 P-1 P-1	AA+ AA AA-	A-1+ A-1+ A-1+
Strong grade But susceptible to adverse conditions	A+ A A-	F1+ / F1 F1 F1	A1 A2 A3	P-1 P-1 / P-2 P-1 / P-2	A+ A A	A-1+ / A-1 A-1 A-1 / A-2
Adequate Grade	BBB+ BBB BBB-	F2 F2 / F3 F3	Baa1 Baa2 Baa3	P-2 P-2 / P-3 P-3	BBB+ BBB BBB-	A-2 A-2 / A-3 A-2
Speculative Grade	BB+ BB BB-	B B B	Ba1 Ba2 Ba3	NP * NP NP	BB+ BB BB-	B-1 B-2 B-3
Very Speculative Grade	B+ B B-	B B B	Ba1 Ba2 Ba3	NP NP NP	B+ B B-	- - -
Vulnerable Grade	CCC CCC CCC CC C	C C C C C	Caa1 Caa2 Caa3 - Ca	NP NP NP NP NP	CCC+ CCC CCC- CC C	C C C C C
Defaulting Grade	D	D	C	NP	D	D

for the purpose of standardisation based on Standard and Poor's credit rating definitions.
* NP – Not Prime

Source: Audit Commission adaptation of information from Fitch, Moody's and Standard & Poor's

ANNEX J: INVESTMENT PERFORMANCE/RISK BENCHMARKING

The consideration and approval of security and liquidity benchmarks are also part of Member reporting. These benchmarks are targets and so may be breached from time to time. Any breach will be reported, with supporting reasons, in the Annual Treasury Report.

Yield

These benchmarks are currently widely used to assess investment performance. Local measures of yield benchmarks are:

> Investments – Internal returns above the 365 day backward looking SONIA (Sterling Overnight Index Average) uncompounded rate

Security and liquidity benchmarks are already intrinsic to the approved Treasury Strategy through the counterparty selection criteria and some of the prudential indicators. Benchmarks for the cash type investments are below. In the other investment categories, appropriate benchmarks will be used where available.

Liquidity

This is defined as an organisation "having adequate, though not excessive, cash resources, borrowing arrangements, overdrafts or standby facilities to enable it at all times to have the level of funds available to it which are necessary for the achievement of its business/service objectives" (CIPFA Treasury Management Code of Practice). In respect of liquidity, the Council seeks to maintain:

> Bank overdraft - £250,000
> Liquid short term deposits of at least £1,500,000 available with a week's notice

The availability of liquidity in the portfolio can be benchmarked by the monitoring of the Weighted Average Life (WAL) of the portfolio – shorter WAL would generally embody less risk. In this respect, the proposed benchmark to be used is:

> WAL benchmark is expected to be 0.5 years, with a maximum of 1.00 years.

Security of the investments

In the context of benchmarking, assessing security is a much more subjective area to assess. Security is currently evidenced by the application of minimum credit quality criteria to investment counterparties, primarily using the Creditworthiness service provided by Link Group. Whilst this approach embodies security considerations, benchmarking levels of risk is more problematic. One method to benchmark security risk is to assess the historic level of default against the minimum criteria used in the Council's investment strategy.

The Council's maximum security risk benchmark for the whole portfolio, when compared to these historic default tables, is:

> 0.002% historic risk of default when compared to the whole portfolio.

These benchmarks are embodied in the criteria for selecting cash investment counterparties and these will be monitored and reported to Members in the Annual Treasury Management Report. As this data is collated, trends and analysis will be collected and reported.

GLOSSARY OF TERMS

CIPFA	Chartered Institute of Public Finance and Accountancy
CIPFA Code	Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes
CFR	Capital Financing Requirement is the estimated level of borrowing or financing needed to fund capital expenditure.
Consent to Borrow	Para 1 (1) of Schedule 3 of the Local Government (Scotland) Act 1975 (the 1975 Act) effectively restricts local authorities to borrowing only for capital expenditure. Under the legislation Scottish Ministers may provide consent for local authorities to borrow for expenditure not covered by this paragraph, where they are satisfied that the expenditure should be met by borrowing.
Gilts	A gilt is a UK Government liability in sterling, issued by HM Treasury and listed on the London Stock Exchange. The term "gilt" or "gilt-edged security" is a reference to the primary characteristic of gilts as an investment: their security. This reflects the fact that the British Government has never failed to make interest or principal payments on gilts as they fall due.
MPC	Monetary Policy Committee
NHT	National Housing Trust initiative undertaken in partnership with the Scottish Futures Trust.
Other Long-Term Liabilities	Balance sheet items such as Public Private Partnership (PPP), and leasing arrangements which already include borrowing instruments.
PPP	Public-Private Partnership.
Prudential Indicators	The Prudential Code sets out a basket of indicators (the Prudential Indicators) that must be prepared and used to demonstrate that local authorities have fulfilled the objectives of the Prudential Code.
SONIA	SONIA (Sterling Overnight Index Average), is the risk-free rate for sterling markets administered by the Bank of England.
Treasury Indicators	These consist of a number of Treasury Management Indicators that local authorities are expected to 'have regard' to, to demonstrate compliance with the Treasury Management Code of Practice.

You can get this document on tape, in Braille, large print and various computer formats by contacting the address below.

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