



# **FLINTSHIRE COUNTY COUNCIL**

**TREASURY MANAGEMENT**

**MID YEAR REPORT 2024/25**

## **1.00 PURPOSE OF REPORT**

- 1.01 To provide Members with a mid-year update on matters relating to the Council's Treasury Management function.

## **2.00 BACKGROUND**

- 2.01 Treasury management comprises the management of the Council's cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks.
- 2.02 The Council's primary objectives for the investment of its surplus funds are to protect the principal sums invested from loss, and to ensure adequate liquidity so that funds are available for expenditure when needed. The generation of investment income to support the provision of local authority services is an important, but secondary, objective.
- 2.03 The Council's policy is to appoint external consultants to provide advice on its treasury management function. In September 2021 Arlingclose Ltd were reappointed as the Council's advisors for a period of 3 years, following a competitive tendering exercise. This period has been extended a further 2 years as per the contract terms to September 2026.
- 2.04 The Council has adopted the 2021 edition of the CIPFA Treasury Management in the Public Services: Code of Practice, which requires the Council to approve a treasury management strategy before the start of each financial year, a mid-year report, and an annual report after the end of each financial year.

This report includes the new requirement in the 2021 Code, mandatory from 1st April 2023, of quarterly reporting of the treasury management prudential indicators and non-treasury prudential indicators.

- 2.05 In addition, the Welsh Government (WG) issues guidance on local authority investments that requires the Council to approve an investment strategy before the start of each financial year.
- 2.06 This report fulfils the Council's legal obligation under the Local Government Act 2003 to have regard to both the CIPFA Code and the WG Guidance.
- 2.07 The Council approved the 2024/25 Treasury Management Strategy at its meeting on 20<sup>th</sup> February 2024.

### **3.00 ECONOMIC & INTEREST RATE REVIEW APRIL – OCTOBER 2024.**

*Provided by Arlingclose Ltd, the Council's treasury management advisors.*

**Economic background:** UK headline consumer price inflation remained around the Bank of England (BoE) target later in the period, falling from an annual rate of 3.2% in March to 2.0% in May and then rebounding marginally to June to 2.2% in July and August, as was expected, due to base effects from energy prices. Core and services price inflation remained higher at 3.6% and 5.6% respectively in August.

The UK economy continued to expand over the period, albeit slowing from the 0.7% gain in the first calendar quarter to 0.5% (downwardly revised from 0.6%) in the second. Of the monthly figures, the economy was estimated to have registered no growth in July.

Labour market data was slightly better from a policymaker perspective, showing an easing in the tightness of the job market, with inactivity rates and vacancies declining. However, a degree of uncertainty remains given ongoing issues around the data collected for the labour force survey by the Office for National Statistics. Figures for the three months to July showed the unemployment rate fell to 4.1% (3mth/year) from 4.4% in the previous three-month period while the employment rate rose to 74.8% from 74.3%.

Over the same period average regular earnings (excluding bonuses) was 5.1%, down from 5.4% in the earlier period, and total earnings (including bonuses) was 4.0% (this figure was impacted by one-off payments made to NHS staff and civil servants in June and July 2023). Adjusting for inflation, real regular pay rose by 2.2% in May to July and total pay by 1.1%.

With headline inflation lower, the BoE cut Bank Rate from 5.25% to 5.00% at the August Monetary Policy Committee (MPC) meeting. The decision was finely balanced, voted by a 5-4 majority with four members preferring to hold at 5.25%. At the September MPC meeting, committee members voted 8-1 for no change at 5.00%, with the lone dissenter preferring Bank Rate to be cut again to 4.75%. The meeting minutes and vote suggested a reasonably hawkish tilt to rates, with sticky inflation remaining a concern among policymakers.

The latest BoE Monetary Policy Report, published in August, showed policymakers expected GDP growth to continue expanding during 2024 before falling back and moderating from 2025 to 2027. Unemployment was forecast to stay around 4.5% while inflation was shown picking up in the latter part of 2024 as the previous years' energy price declines fell out of the figures before slipping below the 2% target in 2025 and remaining there until early 2027.

Arlingclose, the Council's treasury adviser, maintained its central view that Bank Rate would steadily fall from the 5.25% peak, with the first cut in August being followed by a series of further cuts, with November 2024 the likely next one, taking Bank Rate down to around 3% by the end of 2025.

The US Federal Reserve (the Fed) also cut interest rates during the period, reducing the Federal Funds Rate by 0.50% to a range of 4.75%-5.00% at its policy meeting in September. The forecasts released at the same time by the central bank suggested a further 1.00% of easing is expected by the end of the calendar year, followed by the same amount in 2025 and then a final 0.50% of cuts during 2026.

Having first reduced interest rates in June, the European Central Bank (ECB) held steady in July before cutting again in September, reducing its main refinancing rate to 3.65% and its deposit rate to 3.50%. Unlike the Fed, the ECB has not outlined a likely future path of rates, but inflation projections remain in line with the central bank's previous forecasts where it will remain above its 2% target until 2026 on an annual basis.

**Financial markets:** Sentiment in financial markets continued to mostly improve over the period, but the ongoing trend of bond yield volatility remained. The general upward trend in yields in the early part of the period was reversed in the later part, and yields ended the half-year not too far from where they started. However, the volatility in response to economic, financial and geopolitical issues meant it was a bumpy ride for bond investors during that time.

Over the period, the 10-year UK benchmark gilt yield started at 3.94% and ended at 4.00% but hit a high of 4.41% in May and a low of 3.76% in mid-September. While the 20-year gilt started at 4.40% and ended at 4.51% but hit a high of 4.82% in May and a low of 4.27% in mid-September. The Sterling Overnight Rate (SONIA) averaged 5.12% over the period to 30th September.

**Credit review:** Arlingclose maintained its advised recommended maximum unsecured duration limit on all banks on its counterparty list at 100 days.

Having had its outlook increased by Fitch and ratings by S&P earlier in the period, Moody's upgraded Transport for London's rating to A2 from A3 in July.

Moody's also placed National Bank of Canada on Rating Watch for a possible upgrade, revising the outlook on Standard Chartered to Positive, the outlook to Negative on Toronto Dominion Bank, and downgrading the rating on Close Brothers to A1 from Aa3.

S&P upgraded the rating on National Bank of Canada to A+ from A, and together with Fitch, the two rating agencies assigned Lancashire County Council with a rating of AA- and A+ respectively.

Credit default swap prices were generally lower at the end of the period compared to the beginning for the vast majority of the names on UK and non-UK lists. Price volatility over the period was also generally more muted compared to previous periods.

Financial market volatility is expected to remain a feature, at least in the near term and, credit default swap levels will be monitored for signs of ongoing credit stress. As ever, the institutions and durations on the Council’s counterparty list recommended by Arlingclose remain under constant review.

### **Outlook for the remainder of 2024/25**

The MPC held Bank Rate at 5.00% in September. It will continue to cut rates to stimulate the UK economy but will initially be cautious given lingering domestic inflationary pressure. Arlingclose see another rate cut in 2024 (Q4), but more significant monetary easing in 2025, with Bank Rate falling to a low of around 3%.

The upside risks to inflation remain, which could limit the extent of monetary easing.

Long term gilt yields have fallen alongside US monetary policy expectations. Arlingclose’s central case id for yields to be volatile around a relatively narrow range, reflecting the likelihood for monetary policy loosening in the Eurozone, UK and US.

	Current	Dec 24	Mar 25	Jun 25	Sept 25	Dec 25	Mar 26	Jun 26	Sept 26	Dec 26	Mar 27	Jun 27	Sept 27
Upside Risk (%)	0.00	0.25	0.50	0.75	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Interest Rate (%)	5.00	4.75	4.25	3.75	3.25	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00
Downside Risk (%)	0.00	-0.25	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50

## **4.00 BORROWING**

4.01 CIPFA’s 2021 Prudential Code is clear that local authorities must not borrow to invest primarily for financial return and that it is not prudent for local authorities to make any investment or spending decision that will increase the capital financing requirement and so may lead to new borrowing, unless directly and primarily

related to the functions of the Council. PWLB loans are no longer available to local authorities planning to buy investment assets primarily for yield unless these loans are for refinancing purposes.

The Council has not invested in assets primarily for financial return or that are not primarily related to the functions of the Council. It has no plans to do so in future.

## **BORROWING STRATEGY & ACTIVITY**

### 4.02 Borrowing Strategy

As outlined in the treasury strategy, the Council's chief objective when borrowing has been to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required, with flexibility to renegotiate loans should the Council's long-term plans change being a secondary objective. The Council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. At the present time, short term interest rates are higher than long-term.

After substantial rises in interest rates since 2021 many central banks have now begun to reduce rates, albeit slowly. Gilt yields were volatile over the 6-month period and have reduced slightly between April and September 2024. Much of the downward pressure from lower inflation figures was counteracted by upward pressure from positive economic data. Data from the US continues to impact global bond markets including UK gilt yields.

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

Whilst the cost of short-term borrowing from other local authorities spiked to around 7% in late March 2024, primarily due a dearth of LA-LA lending/borrowing activity during the month, as expected shorter-term rates reverted to a more normal range and were generally around 5.00% - 5.25%.

The PWLB HRA rate which is 0.4% below the certainty rate is available up to June 2025. This discounted rate is to support local authorities borrowing for the Housing Revenue Account and for refinancing existing HRA loans, providing a window of opportunity for HRA-related borrowing. The Council borrowed £5m using this lower rate in August 2024.

The Council submitted its application for access to PWLB lending 2024/25

(including access to HRA and certainty rates) in April 2024.

During the period April – September 2024, the following loans were taken out –

Start Date	Maturity Date	Amount	Rate	Loan Type
20 June 2024	20 June 2064	£0.118m	5.42%	Annuity
05 Aug 2024	05 Aug 2064	£0.743m	5.63%	Annuity
14 Aug 2024	14 Aug 2035	£5m	4.15%	EIP
23 Sept 2024	23 Sept 2034	£10m	4.32%	EIP

The annuity loans have been lent on to New Homes, the Council's wholly-owned subsidiary, to fund the building of affordable homes in Flintshire.

Existing loans of £0.696m were allowed to mature without replacement. This strategy enabled the Council to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk.

4.03 The long-term borrowing outstanding at 30<sup>th</sup> September 2024 totalled £315.63m.

4.04 Loans with the Public Works Loans Board are in the form of fixed rate (£292.58m). £18.95m is variable in the form of LOBOs (Lender's Option, Borrower's Option) and £4.1m are interest free loans from government. The Council's average long-term borrowing rate is currently 4.49%.

	Balance 01/04/2024 £m	Debt Maturing £m	New Debt £m	Balance 30/09/2024 £m
Long Term Borrowing	297.97	(2.30)	15.86	311.53
Government Loans	4.34	(0.24)	0.00	4.10
<b>TOTAL BORROWING</b>	<b>302.31</b>	<b>(2.54)</b>	<b>15.86</b>	<b>315.63</b>
Other Long Term Liabilities *	2.43	0.00	0.00	2.4313
<b>TOTAL EXTERNAL DEBT</b>	<b>304.74</b>	<b>(2.54)</b>	<b>15.86</b>	<b>318.067</b>
Increase/ (Decrease) in Borrowing £m				13.32

\* relates to finance leases in respect of Deeside Leisure Centre and Jade Jones Pavilion

4.05 Short-term borrowing was undertaken as necessary. The total short-term borrowing as at 30<sup>th</sup> September 2024 was £10m, with an average rate of 4.63%

4.06 On 1st April 2024 the Council held £18.95m of LOBO (Lender's Option Borrower's Option) loans where the lender has the option to propose an increase in the interest rate at set dates, following which the Council has the option to either accept the new rate and terms or to repay the loan at no additional cost.

As market interest rates rose, it increased the probability of call options on the LOBOs being exercised by lenders. All of LOBO loans had semi-annual call option dates during the six-month period to September 2024, no LOBO loans were called.

The LOBO loans have call dates within the next 12 months. The Council has liaised with treasury management advisors Arlingclose over the likelihood of the options being exercised. If the option is exercised and an increased rate proposed, the Council plans to repay the loan at no additional cost as accepting the revised terms would mean the Council would still have refinancing risk in later years. If required, the Council will repay the LOBO loans with available cash or by borrowing from other local authorities or the PWLB.

#### 4.07 Debt Rescheduling

The continuing rise in gilt yields since early 2022 resulted in some of the Council's PWLB loans being in or close to a discount position if repaid early. However, as the prepaid loans would need to be replaced by new loans at higher interest rates, this was not a cost-effective option for the Council.

The Corporate Finance Manager, in conjunction with the Council's treasury advisors, will continue to review any potential opportunities for restructuring the Council's debt in order to take advantage of potential savings as interest rates change and to enhance the balance of the long-term portfolio (amend the maturity profile and/or the balance of volatility).

## 5.0 **INTERIM INVESTMENT AND PERFORMANCE REPORT**

5.01 The definition of investments in the Treasury Management Code now covers all the financial assets of the Council as well as other non-financial assets which the Council holds primarily for financial return. Investments that do not meet the definition of treasury management investments (i.e. management of surplus cash) are categorised as either for service purposes (made explicitly to further service objectives) and or for commercial purposes (made primarily for financial return).

Investment Guidance issued by the Welsh Government also includes within the definition of investments all such assets held partially or wholly for financial return.

Non-treasury investments, including loans to subsidiaries and purchases of investment property, are not normally considered to be treasury investments, and these are therefore covered separately in Appendix A.

5.02 The maximum investments the Council had on deposit at any one time totalled £66.7m. The average investment balance for the period was £41.9m and the



average rate of return was 5.15%, generating investment income of £1.09m.

- 5.03 Both the CIPFA Code and government guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its treasury investments before seeking the optimum rate of return, or yield. The Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

As demonstrated by the liability benchmark in this report (paragraph 6.01), the Council expects to be a long-term borrower and new treasury investments are therefore primarily made to manage day-to-day cash flows using short-term low risk instruments. The existing portfolio of strategic pooled funds will be maintained to diversify risk into different asset classes and boost investment income.

- 5.04 Up to 30<sup>th</sup> September, investments were made in the Debt Management Office Deposit Account, banks, other local authorities and money market funds.
- 5.05 The average of long-term borrowing was £302.92m generating interest payable of £6.784m, in line with budget forecasts to date.

	Investments		Long Term Borrowing		Short Term Borrowing	
	Interest received £k	Interest rate %	Interest paid £k	Interest rate %	Interest paid £k	Interest rate %
2024/25 Apr - Sept	1,089	5.15	6,784	4.49	580	4.63
2023/24 Apr - Sept	1,112	4.58	6,659	4.51	0	n/a
Difference	(23)		125		580	

Year-end projections are as follows:

	Investments		Long Term Borrowing		Short Term Borrowing	
	Interest received £k	Interest rate %	Interest paid £k	Interest rate %	Interest paid £k	Interest rate %
2024/25 est.	1,890	4.80	13,773	4.49	1,245	4.75
2023/24 act	2,180	4.87	13,461	4.49	425	5.46
Difference	(290)		312		820	

- 5.06 Credit Risk (security)

Counterparty credit quality was assessed and monitored with reference to credit ratings (the Council's minimum long-term counterparty rating for institutions defined as having "high credit quality" is A- across rating agencies Fitch, S&P and Moody's);

credit default swap prices, financial statements, information on potential government support and reports in the quality financial press.

#### 5.07 Liquidity

In keeping with the WG's Guidance on Investments, the Council maintained a sufficient level of liquidity through the use of money market funds.

#### 5.08 Yield

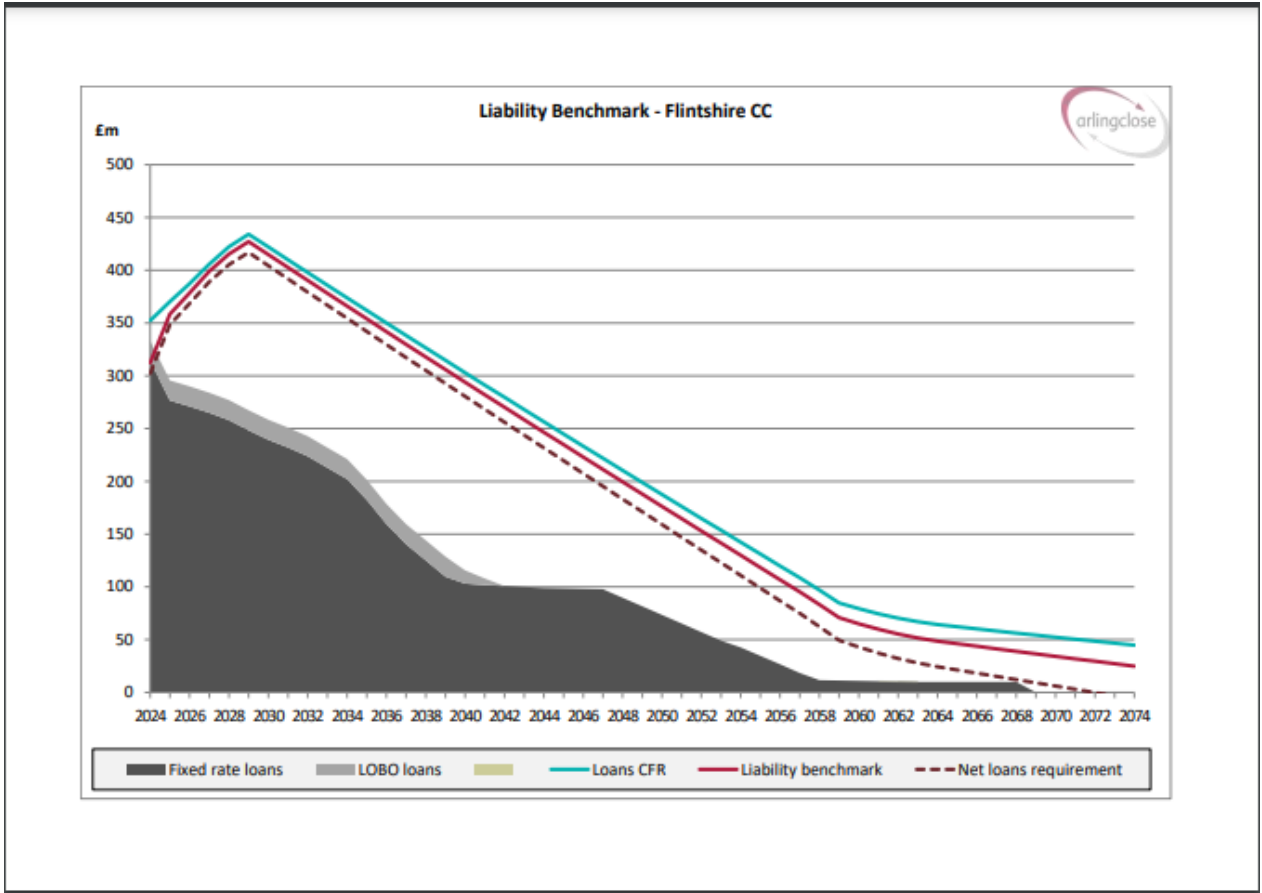
The Council sought to optimise returns commensurate with its objectives of security and liquidity. The Council's investment yield is outlined in paragraph 5.0.2.

### **6.00 TREASURY MANAGEMENT PRUDENTIAL INDICATORS**

As required by the 2021 CIPFA Treasury Management Code, the Council monitors and measures the following treasury management prudential indicators.

#### 6.01 Liability Benchmark

This indicator compares the Council's actual existing borrowing against a liability benchmark that has been calculated to show the lowest risk level of borrowing. The liability benchmark is an important tool to help establish whether the Council is likely to be a long-term borrower or long-term investor in the future, and so shape its strategic focus and decision making. It represents an estimate of the cumulative amount of external borrowing the Council must hold to fund its current capital and revenue plans while keeping treasury investments at the minimum level required to manage day-to-day cash flow.



6.02 Interest rate exposures

This indicator is set to control the Council’s exposure to interest rate risk.

<b>Interest rate risk indicator</b>	<b>30.06.24 £'000</b>	<b>30.09.24 £'000</b>
Upper limit on one-year revenue impact of a 1% <u>rise</u> in interest rates	(48)	(60.0)
Upper limit on one-year revenue impact of a 1% <u>fall</u> in interest rates	177	206.0

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

Fixed rate investments and borrowings are those where the rate of interest is fixed for at least 12 months, measured from the start of the financial year or the transaction date if later. All other instruments are classed as variable rate.

6.03 Maturity structure of borrowing

This indicator is set to control the Council's exposure to refinancing risk. The upper and lower limits on the maturity structure of fixed rate borrowing will be:

	Lower	Upper	Actual as at 30.09.24
Under 12 months	0%	20%	2.76%
12 months and within 24 months	0%	20%	3.39%
24 months and within five years	0%	30%	7.99%
Five years and within 10 years	0%	50%	17.76%
10 years and above	0%	100%	68.10%

Time periods start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment.

6.04 Long-term treasury management investments:

The purpose of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments. The prudential limits on the long-term treasury management investments will be:

Price risk indicator	2024/25 Limit	30.09.24 Actual
Limit on total principal invested beyond year end	£5m	£0m

Any long-term investments carried forward from previous years will be included in each year's limit.

6.05 Borrowing Limits

These limits are reported as part of the quarterly monitoring of the capital programme, however, they are repeated here for completeness.

	2024/25 Limit	30.09.24 Actual
Operational Boundary	£485m	£397m
Authorised Limit	£520m	£397m

## **7.00 OTHER ITEMS**

7.01 Other treasury management related activities that took place during April – September 2024 included:

- Statutory override: In April 2023 the Ministry for Housing, Communities and Local Government published the full outcome of the consultation on the extension of the statutory override on accounting for gains and losses on pooled investment funds. The override has been extended for 2 years until 31st March 2025 but no other changes have been made; whether the override will be extended beyond the new date is unknown but commentary to the consultation outcome suggests not.
- The Treasury Management Annual Report 2023/24 was reported to Governance and Audit Committee on 24<sup>th</sup> July 2024, Cabinet on 25<sup>th</sup> September 2024 and will be reported to Council on 21<sup>st</sup> November 2024.
- The Quarter 1 Treasury Management update was reported to the Governance and Audit Committee.

## **8.00 COMPLIANCE**

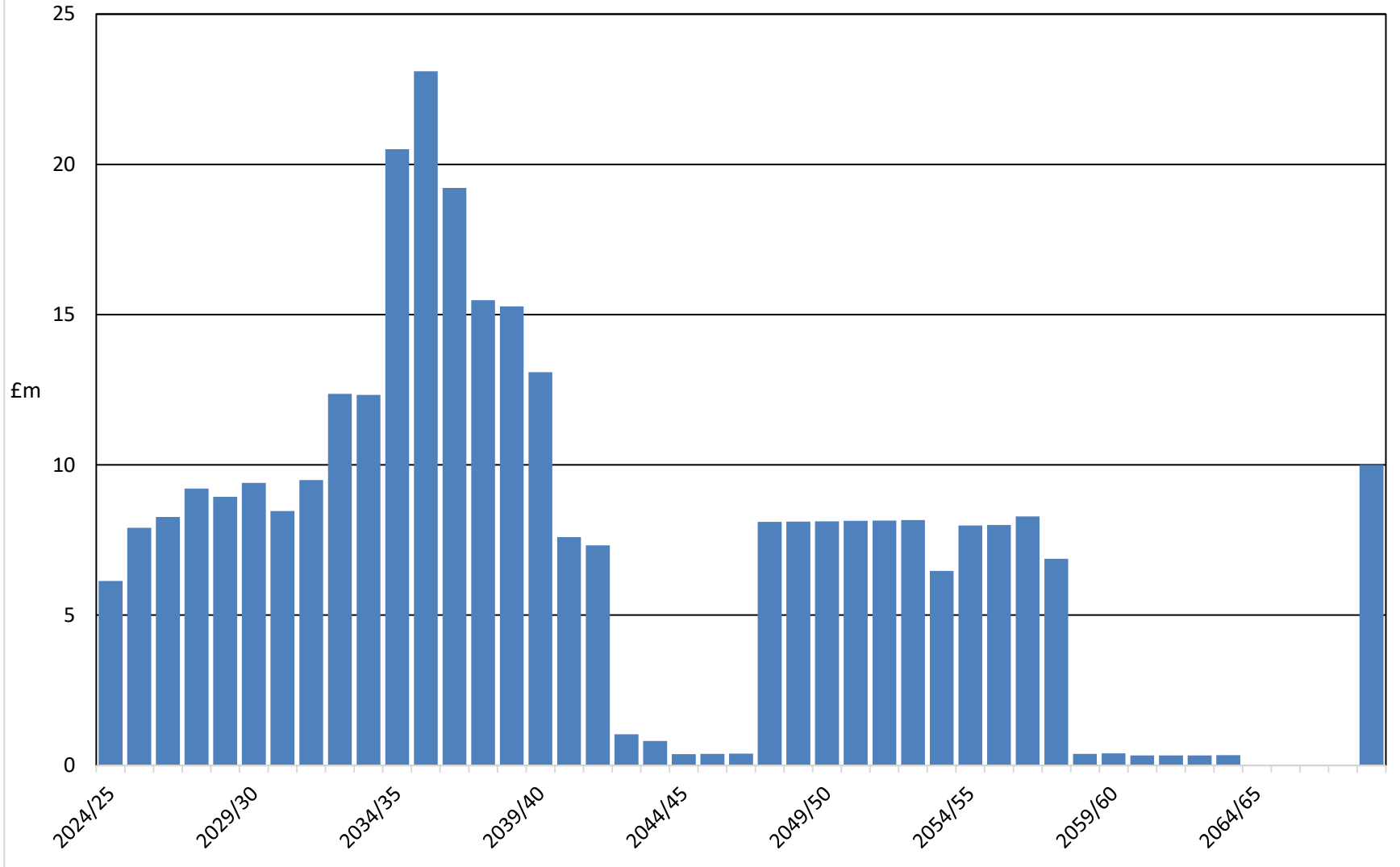
8.01 The Corporate Finance Manager reports that all treasury management activities undertaken during the quarter complied fully with the principles in the Treasury Management Code and the Council's approved Treasury Management Strategy. Compliance with specific investment limits is demonstrated in Section 6.00.

## **8.00 CONCLUSION**

8.01 In compliance with the requirements of the CIPFA Code of Practice this report provides Members with a summary report of the treasury management activity during the first half of 2024/25.

8.02 As indicated in this report none of the prudential indicators have been breached and a prudent approach has been taken in relation to investment activity with priority being given to security and liquidity over yield.

Debt Maturity Profile - September 2024



## APPENDIX A NON-TREASURY INVESTMENTS

- 1.01 The definition of investments in the Treasury Management Code now covers all the financial assets of the Council as well as other non-financial assets which the Council holds primarily for financial return. Investments that do not meet the definition of treasury management investments (i.e. management of surplus cash) are categorised as either for service purposes (made explicitly to further service objectives) and or for commercial purposes (made primarily for financial return).

Investment Guidance issued by the Welsh Government also includes within the definition of investments all such assets held partially or wholly for financial return.

The Council has given loans to wholly owned companies for service purposes and has historical non-financial investments in property defined as Investment Properties within the Council's Statement of Accounts. The Council considers both to be non-treasury investments.

### 1.02 Wholly Owned Companies

The Council's investments in the form of loans to wholly owned companies contribute to its service delivery objectives and/or to promote wellbeing as follows:

- The Council has embarked on an ambitious house building programme as part of its Strategic Housing and Regeneration Programme (SHARP). Over a 5-year period 500 new homes will be built at a range of sites across the county, a mixture of new council houses and affordable homes, alongside commissioning a range of linked regeneration initiatives and community benefits.
- Affordable homes are being developed through the Council's wholly owned subsidiary North East Wales Homes Limited (NEW Homes) in partnership with the Council. Affordable homes for rent are built or purchased by NEW Homes funded by loans from the Council. New affordable homes for rent have been built in Flint, Penyffordd (Holywell), Dobshell, Bryn-y-Baal, Northop and Saltney.

The Council considers that its financial exposure to loans to wholly owned companies is proportionate and has set the limits in the table below. The Council's loan book is currently within these self-assessed limits.

<b>Borrower</b>	<b>Cash Limit</b>
Wholly owned companies	£40m
Treasury management investments meeting the definition of a loan	Unlimited

#### Yield (net profit)

The loans generate a small income for the Council as there is a margin of approx. 0.25% charged to NEW Homes on the Council's borrowing rate from the PWLB. The income makes a very small contribution to achieving a balanced revenue budget.

### 1.03 Investment Properties

The Welsh Government guidance includes an investment category covering non-financial assets held primarily or partially to generate a profit, primarily investment property. Proper accounting practice defines an investment property as those that are held solely to earn rent and / or for capital appreciation.

The Council has a portfolio of investment properties, in the form of agricultural property and industrial units. Although these are classified as investment properties, they are legacy assets, and the Council is managing down its agricultural portfolio and is reviewing its position regarding industrial units.

#### **Fair Value of Investment Properties**

	31.03.2024 £m	31.03.2023 £m	31.3.2022 £m	31.3.2021 £m	31.3.2020 £m
Fair Value Inv. Properties	29.3	29.1	27.6	25.2	25.0

#### Yield (net profit)

The profit generated by investment activity makes a small contribution to achieving a balanced revenue budget. The table below details the extent to which funding expenditure to meet the service delivery objectives and or promote wellbeing in the Council is dependent on achieving the expected yield over the life cycle of the Medium-Term Financial Plan.



### Proportionality of Investment Properties

	2023/24 Actual £m	2024/25 Budget £m	2025/26 Budget £m
Net Revenue Budget	352.121	368.106	368.106
Net Investment income	1.71	1.67	1.67
Proportion	0.49%	0.45%	0.45%