BARNSLEY METROPOLITAN BOROUGH COUNCIL

REPORT OF:	**Executive Director – Core Services & Director of Finance (Section 151 Officer)**
TITLE:	**ANNUAL REPORT ON TREASURY MANAGEMENT ACTIVITIES 2023/24**

REPORT TO:	**Cabinet**
Date of Meeting	
Cabinet Member Portfolio	**Cllr Frost – Core Services**
Key Decision	**Yes**
Public or Private	**Public**

Purpose of report

This report reviews the treasury management activities carried out by the Council during 2023/24, in accordance with statutory guidance. The Council is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2023/24. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management, (the Code), and the CIPFA Prudential Code for Capital Finance in Local Authorities, (the Prudential Code).

In broad terms this report covers:

- The overarching treasury management strategy for 2023/24;
- An economic summary for the year;
- An update on the Council's borrowing and investment activities; and
- The Council's Prudential and Treasury Indicators.

Council Plan priority

All

Recommendations

It is recommended that Cabinet:

1. Note the latest expectations for interest rates (as outlined at paragraph 2.4);
2. Note the activities undertaken during the year to support the Council's borrowing and investment strategies, and;
3. Note the Prudential and Treasury Indicators set out in Appendix 1.

1. INTRODUCTION

1.1 The Treasury Management Strategy Statement (TMSS) for 2023/24 was approved by full Council on 23rd February 2023. It identifies the key risks associated with the Council's borrowing and investment activities and sets out how those risks will be managed.

1.2 The Council operates within a Treasury Framework which facilitates flexibility for treasury strategy. The need to adopt an agile approach to Treasury Management has never been as important following volatility within the UK economy and major global events impacting on economies worldwide.

1.3 Due to elevated long-term borrowing costs, the current borrowing strategy is to maintain a minimum proportion of fixed rate borrowing to limit the Council's exposure to interest rate risk, whilst managing an appropriate level of internal borrowing in order to reduce the Council's financing costs. As paragraph 2.4 refers, interest rate forecasts are closely monitored by treasury officers to achieve optimum value and manage risk exposure in the long-term in relation to the Authority's external borrowing requirement.

1.4 The current investment strategy seeks to minimise credit risk and maintain a suitable balance of liquid funds to ensure that sufficient cash is available when needed and as such the pursuit of higher investment returns is a secondary objective. Throughout the financial year, officers ensured that the Council's investments remained both secure and liquid.

2. PROPOSAL

<u>Economic Summary</u>

Highlights:

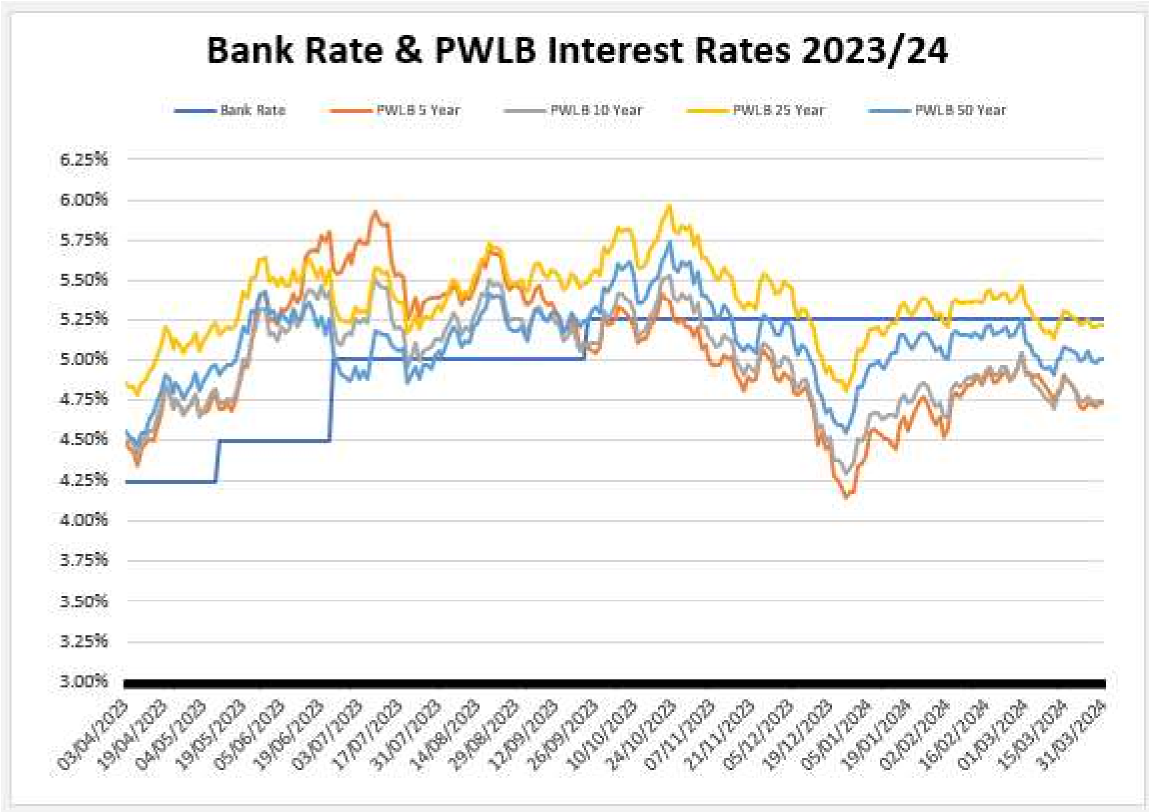
- *Starting April 2023 at 4.25%, the UK Bank Rate moved up in stepped increases of either 0.25% or 0.5%, reaching 5.25% by August 2023;*
- *5.25% is forecast to be the peak of the interest rate cycle;*
- *Long-term borrowing costs remained elevated during 2023/24;*
- *Consumer Price Index (CPI) inflation rate was 3.2% in March 2024, down from 3.4% in February 2024.*

2.1 The UK staged an early recovery from a technical recession in the second half of 2023, with real GDP growth expected to be 0.3% in 2024, accelerating to 0.9% in 2025. Although growth is weak, economists expect improving incomes to bolster consumer spending and help the UK economy to emerge from a period of stagnation.

2.2 UK interest rates have been volatile throughout 2023/24 against a backdrop of continuing inflationary pressures and global events, including the wars in the

Ukraine and the Middle East. The Bank of England left the Bank Rate at 5.25% at the meeting in March 2024 and the underlying message from the Monetary Policy Committee was confidence that inflation will fall sustainably back to the 2.0% target in the first half of 2024.

2.3 Interest rates are a key driver of the Council's treasury management activities and are closely monitored by officers. As illustrated in the graph, PWLB rates fell during the latter part of 2023, based on signs of improvement within domestic and international economies, before moving slightly upwards during the beginning of 2024. Economists are currently forecasting PWLB rates to fall over the next one to two years in-line with forecast cuts to the Bank Rate and as inflation moves towards the Bank of England's 2% target.



2.4 The Council has appointed Link Group as its Treasury Management advisors and part of their service is to formulate a view on interest rates. For comparison purposes, the Council reviews forecasts published by other leading economists (Capital Economics) in addition to those provided by Link Group. The UK Base Rate and PWLB 50 Year Certainty Rate forecasts are shown below, and these are closely monitored in order to mitigate the risk of movements which could adversely impact on Council finances.

Latest Interest Rate Projections (provided by Link Group & Capital Economics as at 05.02.24)

	Latest	Sep-24	Mar-25	Sep-25	Mar-26	Sep-26	Mar-27
UK Base Rate ~ Link Group	*5.25%*	4.75%	3.75%	3.00%	3.00%	3.00%	3.00%
UK Base Rate ~ Capital Economics	*5.25%*	4.50%	3.50%	3.00%	3.00%	3.00%	-
PWLB Certainty 50 Years ~ Link Group	*5.16%*	4.70%	4.40%	4.10%	4.00%	3.90%	3.90%
PWLB Certainty 50 Years ~ Capital Economics	*5.16%*	4.60%	4.40%	4.30%	4.30%	4.10%	-

2.5 As shown above, the latest forecast by Link Group (as at 5th February 2024) is that the Bank Rate has reached its peak of 5.25%, with a first rate cut to 4.75% in Q3 2024, to be followed by further rate cuts through 2024 and 2025. The low point of the interest rate cycle is expected to be 3%.

Borrowing Activity

Highlights:

- *No new long-term borrowing undertaken during the year;*
- *A closing Capital Financing Requirement (CFR) of £828.8 Million*
- *The Council repaid £55 Million of LOBO loans during the year, generating in the region of £10 Million in long-term savings over the remaining lifetime of the loans (32 years);*
- *An underlying need to borrow of up to £88.8 Million over the period to 2025/26 (up £30.3 Million from the original estimate partly as a result of the LOBO repayment);*
- *Fixed rate borrowing targets to be reviewed throughout the new financial year in line with interest rate forecasts and monitoring of capital expenditure over the planning period.*

2.6 The Council's underlying need to borrow for capital expenditure is termed the Capital Financing Requirement (CFR). This figure is a gauge of the Council's indebtedness. The CFR results from the capital activity of the Council and resources used to pay for capital spend. It represents the 2023/24 unfinanced capital expenditure, and prior years' net or unfinanced capital expenditure which has not yet been paid for by revenue or other resources.

2.7 Part of the Council's treasury management activities is to address the funding requirements for this borrowing need. The treasury management service organises the Council's cash position to ensure that sufficient cash is available to meet the capital plans and daily cash flow requirements. This may be sourced through borrowing from external bodies, or by utilising temporary cash resources within the Council.

2.8 **Reducing the CFR** - the Council's CFR for the year is shown in the following table and represents a key prudential indicator (refer to Appendix 1 for further details). The Council's (non HRA) underlying borrowing need (CFR) is not allowed to rise indefinitely. Statutory controls are in place to ensure that capital assets are broadly charged to revenue over the life of the asset. The Council is required to make an annual revenue charge, called the Minimum Revenue Provision (MRP), to reduce the CFR each year in line with the MRP Policy, which is effectively a repayment of the non-HRA borrowing need. The MRP charge is represented in the table at 2.9 as the 'Amounts set aside to repay debt'. The Council's 2023/24 MRP Policy, (as required by DLUHC Guidance), was approved as part of the TMSS 2023/24 on 23rd February 2023.

2.9 In accordance with the approved TMSS 2023/24, the Council's borrowing strategy is to reduce its exposure to interest rate risk, whilst maintaining an under-borrowed* position to keep its financing costs to a minimum. The table below shows the Council's under-borrowed position of £250.7M as at 31st March 2024, and how this compares to the original estimate.

	2023/24 Estimate (£M)	2023/24 Actual (£M)	Variance (£M)
Opening CFR (exc. PFI Schemes / finance leases)**	**823.154**	**823.154**	**0.000**
Increase from in-year capital investment	34.953	10.834	(24.119)
Amounts set aside to repay debt (MRP)	(4.632)	(5.219)	(0.587)
Closing CFR (exc. PFI Schemes / finance leases)**	**853.475**	**828.769**	**(24.706)**
External borrowing	(633.072)	(578.072)	55.000
Under-borrowed position	**220.403**	**250.697**	**30.294**

** Refers to the temporary use of internal cash resources (e.g. earmarked reserves or grants received in advance of expenditure) to support its borrowing requirement.*

*** Excluded on the basis that each arrangement contains its own borrowing facility and therefore the Council is not required to borrow separately.*

Debt Rescheduling

2.10 The Council entered into 'Lender Option Borrower Option' (LOBO) loan agreements in 2003 and 2004, like many other local authorities at that time as they were a cheaper option than borrowing from the Public Works Loans Board (PWLB). LOBOs provide the option for both parties to reconsider the loan at pre-defined periods. If the interest rate is increased, the borrower (the Council) has the option to continue at the new rate or repay the loan.

2.11 The use of LOBOs by local authorities has been criticised in the past due to the variable rate structure and the risk that the loans could tie the borrower into higher rates in future. Despite this negative reputation Councils have so far benefited from LOBO deals as, until recently, interest rates have only fallen. However, as the Council's borrowing strategy is to limit exposure to interest rate risk, opportunities to exit this type of loan have been explored but have not proven cost effective until recently.

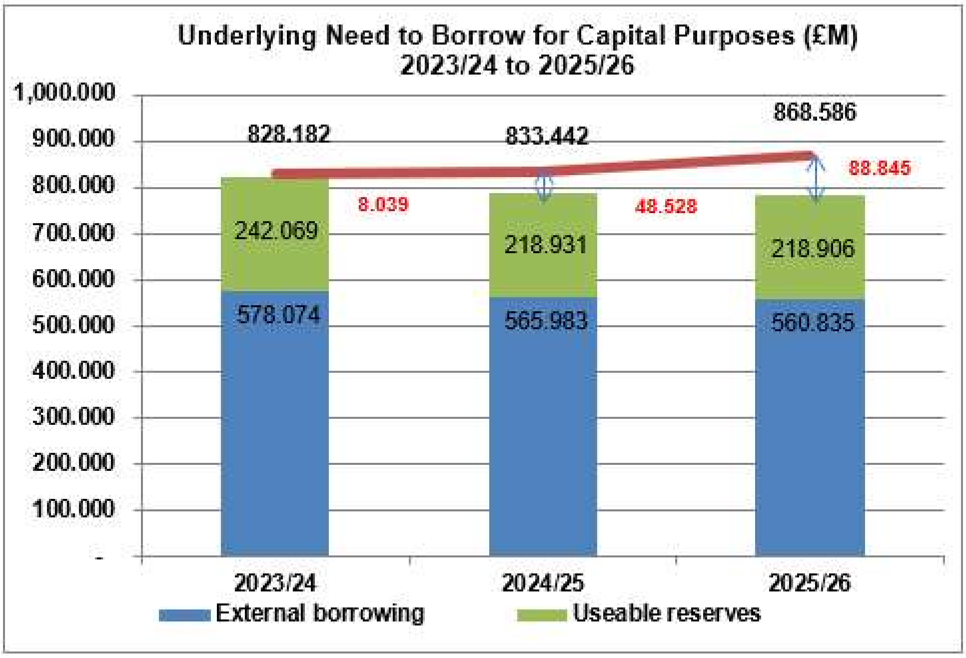
2.12 During 2023/24 debt rescheduling opportunities increased due to market conditions and the rising interest rate environment. The Council took a pro-active approach and explored a number of options, including the repayment of the LOBO loans, to rebalance the debt portfolio and provide more certainty. Exiting these loans early would also help to de-risk the investment portfolio by reducing cash balances, thereby reducing exposure to credit and counterparty risk.

2.13 Options were discussed and approved at Treasury Management Panel and officers worked with its Treasury Management Advisers, LINK Group, to negotiate the repayment of £55M of outstanding LOBO loans in November 2023. This repayment was on the basis of using existing cash balances and delaying further long-term borrowing. The repayment has generated in the region of £10M in long-term savings over the remaining lifetime of the LOBO loans (32 years).

Latest Borrowing Position

2.14 There was a £73.4M decrease in total external debt during the year, with the final balance as at 31st March 2024 being £578.1M (£651.5M as at 31/03/23). This includes the £55M LOBO repayment as detailed previously. A breakdown of the net movement in borrowing is provided at Appendix 2. During 2023/24, the Council has followed advice from our Treasury Management Advisors, Link Group, and focused on a policy of internal and temporary borrowing, utilising cash balances and reserves in lieu of long-term external borrowing. This borrowing strategy is being continually reviewed to avoid incurring higher costs in the future when the Authority may not be able to avoid new borrowing to finance capital expenditure and/or the refinancing of maturing debt.

2.15 As illustrated by the following chart, the Council's underlying need to borrow for capital purposes (represented by the blue arrows) is £88.8M over the period to 2025/26. This is an updated position as at 31st March 2024, based on the latest capital spend projections and the temporary use of available reserves:



Projected external borrowing requirement 2023/24 - 2025/26	**£M**
Planned capital investment	85.414
Maturing loans / reduced support from useable reserves	27.618
Amounts set aside to repay debt	(24.187)
Total	**88.845**

2.16 The Director of Finance has previously advised that a target of 70% fixed rate borrowing be maintained in order to manage risk and provide cost certainty, and the Authority has been working to this target over several years whilst interest rates have remained low.

2.17 As borrowing costs are at their highest since 2008, it has not been considered prudent to undertake additional borrowing during 2023/24. The recommended approach has been to hold off further long-term borrowing and closely monitor the profile of capital spend and funding requirements over the planning period. Temporary reserves and balances have been utilised in lieu of external borrowing until a time when rates begin to fall from their current high levels as forecast in the table at 2.4. This prudent approach allows the Authority the flexibility to use the under borrowed position to minimise costs and defer long-term borrowing until it becomes less expensive.

2.18 If the Council were to continue to meet the 70% fixed rate borrowing target, this would require in the region of £50M of debt to be secured in additional fixed rate loans over the period to 2025/26. Based on current long-term borrowing rates this would cost the Authority approximately £2.5M in additional interest payments per year. Updates in relation to the Council's TM policy and the impact on the capital financing requirement will be provided to Members throughout 2024/25.

2.19 In light of the above requirement, officers continue to monitor rates and assess borrowing options and opportunities as set out in the Council's borrowing strategy:

- **Deferred loans** - the Council may be able to access long-term, fixed rate funding from financial institutions such as banks, insurance companies and pension funds on a deferred drawdown basis. Whilst there is a small premium above PWLB rates, deferred loans help to protect the Council from interest rate risk without the additional cost of carry and credit risk.
- **Municipal Bonds Agency (MBA)** - the MBA was established in 2014 with the intention of providing an alternative source of funding to the PWLB. The MBA has made two bond issues for Lancashire CC and are aiming to launch a pooled bond issue. Barnsley has been a leading authority in promoting the MBA and has already committed to the next bond issue subject to 'due diligence' tests. The MBA also offer a flexible range of short and long-term loans, and forward loans.
- **PWLB borrowing** - the Council has access to long-term PWLB funding at the 'Certainty Rate' (providing loans at 0.2% below the usual rate). The latest forecasts (at paragraph 2.4) show a gradual decline in PWLB rates during the forecast period to March 2027. There is likely to be unpredictable volatility during this period, and officers will continue to closely monitor long-term PWLB rates and assess opportunities for securing long-term funding at attractive rates.
- **Local authority loans** - the Council may be able to borrow from other local authorities for periods of up to 5 years, which would provide additional budget certainty over the medium-term whilst providing a saving against current long-term PWLB rates. Opportunities for inter-authority lending have been assessed by treasury officers on an ongoing basis throughout the year.
- **Market loans** - as with deferred loans the Council may be able to access long-term, fixed rate funding from financial institutions on a spot basis (i.e. immediate drawdown). However, this is currently a more expensive option than borrowing from the PWLB, and therefore has not been utilised during 2023/24.

- **Internal Borrowing** - while borrowing rates remain elevated, the Council could continue with the temporary use of internal cash resources (e.g. earmarked reserves or grants received in advance of expenditure) in lieu of external borrowing. This is a temporary measure and should be considered in line with the reserves strategy and capital spend projections over the planning period**.**

Investment Activity

Highlights:

- *Total investment balance of £55.7M as at 31 March 2024;*
- *A net decrease in investment balances of £98.2 Million during the year, primarily due to the repayment of LOBO loans;*
- *Investment activity during the year conformed to the approved strategy, and the Council had no liquidity difficulties;*
- *Security and liquidity remained the key priorities, with the majority of new investments placed in secure Money Market Funds and instant access accounts.*

2.20 The TMSS for 2023/24, which includes the Annual Investment Strategy, was approved by the Council in February 2023. In accordance with the CIPFA Treasury Management Code of Practice, it sets out the Council's investment priorities as being:

- Security of capital
- Liquidity
- Yield

2.21 The Council aims to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity and with the Council's risk appetite. 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, using the Link suggested creditworthiness approach.

2.22 The majority of transactions during the financial year related to short-term deposits. However, to maintain sufficient liquidity, an appropriate balance of cash was deposited in the Council's Money Market Funds and instant access accounts (see Appendix 3 for further details). In addition, officers continued to take advantage of the competitive rates offered on short-term local authority deposits.

2.23 The key investment issues managed by the Council during 2023/24 have included:

- **Security of Investments** – The Council continues to take a cautious approach to investing, whilst also recognising that there have been changes to regulatory requirements for financial institutions in terms of additional capital and liquidity that were introduced following the Financial Crisis in

2008/09. These requirements have provided a far stronger basis for financial institutions, with annual stress tests by regulators evidencing how institutions are now far more able to cope with extreme stressed market and economic conditions. The Director of Finance confirms that all investments as at 31st March 2024 are placed with low-risk, high credit rated counterparties in accordance with the approved TMSS 2023/24.

- **Local Authority Creditworthiness / Reputation Management** – this remains an ongoing issue for local authorities particularly in light of the current economic climate. Whilst there are no issues foreseen from a credit perspective (there are regulations in place to avoid local authorities going bankrupt), officers recognise the reputational risk associated with such investments and will take this into consideration when deciding where to invest the Council's surplus cash.

Performance Measurement / Compliance with Prudential and Treasury Limits

2.24 The Council's capital financing budget underspent during the year by £1.7M. The underspend is due to a combination of maintaining an appropriate level of internal borrowing, increased investment returns due to higher interest rates and the repayment of long-term LOBO loans. This underspend is expected to reduce in future years as reserves are utilised and the Council considers further external borrowing when economic conditions are more favourable.

2.25 It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. During the year to 31st March 2024, the Council has operated within the prudential and treasury indicators set out in the agreed TMSS 2023/24. The Director of Finance reports that no difficulties are envisaged for the current or future years in complying with these indicators (see Appendix 1 for more details). All treasury management operations have been conducted in full compliance with the Council's Treasury Management Practices.

Regulatory Framework & Risk Assessment

2.26 The Council has adopted the statutory guidance issued by the Chartered Institute of Public Finance and Accountancy (CIPFA) and the Department for Levelling Up, Housing and Communities (DLUHC), which seeks to ensure that its capital expenditure and borrowing are prudent, affordable and sustainable, and its treasury practices demonstrate a low-risk approach.

2.27 Members are asked to note that the implementation of International Financial Reporting Standard 16 (IFRS16) bringing currently off-balance sheet leased assets onto the balance sheet, has been delayed until 2024/25. Further details will be provided in Treasury Management updates prepared in the new financial year, 2024/25.

2.28 The Council is aware of the risks of passive management of the treasury portfolio and, with the support of its Treasury Management advisers, Link Group, has proactively managed the debt and investments over the past year.

2.29 Treasury Management activities are scrutinised as part of the Council's External Auditors annual accounts and VfM opinion process with any recommendations to be included as part of their 2023/24 Annual Reports. As a result, the Council will continue to closely monitor treasury management activities and the associated risks.

3. IMPLICATIONS OF THE DECISION

3.1 Financial and Risk

The financial and risk implications arising from the treasury management activities for the year are reported to Cabinet separately as part of the Council's revenue outturn report for 2023/24.

3.2 Legal

Not applicable.

3.3 Equality

Not applicable – Equality Impact Assessments are undertaken for key Treasury Management decisions where appropriate.

3.4 Sustainability

Decision-making wheel not completed – where appropriate individual decision-making wheels would be completed for key Treasury Management decisions.

3.5 Employee

None arising from this report.

3.6 Communications

No specific requirements.

4. CONSULTATION

4.1 This report has been prepared in consultation with Link Asset Services and approved by the Treasury Management Panel.

5. ALTERNATIVE OPTIONS CONSIDERED

5.1 Not applicable as reporting year-end position.

6. REASONS FOR RECOMMENDATIONS

6.1 Recommendations made in-line with the approved Treasury Management Strategy.

7. GLOSSARY

Not applicable.

8. LIST OF APPENDICES

Appendix 1: Actual Prudential and Treasury Indicators for 2023/24
Appendix 2: BMBC Borrowing 2023/24
Appendix 3: BMBC Investments 2023/24

9. BACKGROUND PAPERS

Various Financial Services working papers.

If you would like to inspect background papers for this report, please email governance@barnsley.gov.uk so that appropriate arrangements can be made.

10. REPORT SIGN OFF

Financial consultation & sign off	Report prepared by Director of Finance

Report Author: Neil Copley
Post: Director of Finance
Date: 22/04/2024