Manchester City Council
Report for Resolution

Report to:	Executive – 15 February 2023 Resources and Governance Scrutiny Committee – 27 February 2023
Subject:	Treasury Management Strategy Statement 2022/23, including Borrowing Limits and Annual Investment Strategy
Report of:	Deputy Chief Executive and City Treasurer

Summary

To set out the proposed Treasury Management Strategy Statement and Borrowing Limits for 2023/24 and Prudential Indicators for 2023/24 to 2025/26.

Recommendations

The Executive is requested to:

(1) Recommend the report to Council.
(2) Delegate authority to the Deputy Chief Executive and City Treasurer, in consultation with the Executive Member for Finance and Human Resources, to:
- approve changes to the borrowing figures as a result of changes to the Council's Capital or Revenue budget; and
- submit these changes to Council.

The Resource and Governance Scrutiny Committee is requested to recommend the report to Council.

The Council is requested to:

(1) Approve the proposed Treasury Management Strategy Statement, and in doing so approve the following:

- Borrowing Requirements listed in Section 7 of this report;
- Borrowing Strategy outlined in Section 10;
- Annual Investment Strategy detailed in Section 11;
- Prudential and Treasury Indicators listed in Appendix A;
- MRP Strategy outlined in Appendix B;
- Treasury Management Policy Statement at Appendix C; and
- Treasury Management Scheme of Delegation at Appendix D

(2) Delegate to the Deputy Chief Executive and City Treasurer, in consultation with the Executive Member for Finance and Human Resources, the power to pursue any restructuring, rescheduling or redemption opportunities available, including amendments to the Treasury Management Strategy if the changes require it. Any changes required to the Strategy will be reported to members at the earliest opportunity.

Wards Affected - All

Environmental Impact Assessment - the impact of the decisions proposed in this report on achieving the zero-carbon target for the city
Treasury Management activity underpins the Council’s finances, and therefore supports projects and initiatives which seek to achieve the Council’s zero carbon target.

<table>
<tr><th>Our Manchester Strategy outcomes</th><th>Contribution to the strategy</th></tr>
<tr><td>A thriving and sustainable city: supporting a diverse and distinctive economy that creates jobs and opportunities</td><td rowspan="5">The Treasury Management function supports the whole Council by seeking to ensure that funding is available when required, to fund all the work that the Council undertakes. Therefore, whilst not directly contributing to the strategic aims, the Council’s treasury management activity underpins the work taking place elsewhere to achieve the outcomes.</td></tr>
<tr><td>A highly skilled city: world class and home-grown talent sustaining the city’s economic success</td></tr>
<tr><td>A progressive and equitable city: making a positive contribution by unlocking the potential of our communities</td></tr>
<tr><td>A liveable and low carbon city: a destination of choice to live, visit, work</td></tr>
<tr><td>A connected city: world class infrastructure and connectivity to drive growth</td></tr>
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Full details are in the body of the report, along with any implications for

- Equal Opportunities Policy
- Risk Management
- Legal Considerations

Financial Consequences – Revenue

The capital financing budget forms a key part of the Council’s revenue budget. The activity forecast in this report is affordable within the existing and future capital financing budget, including use of the capital financing reserve.

Financial Consequences – Capital

None – the Council’s treasury management activity is not capital expenditure.

Contact Officers:

Name: Carol Culley
Position: Deputy Chief Executive and City Treasurer
Telephone: 0161 234 3406
E-mail: carol.culley@manchester.gov.uk

Name: Tom Wilkinson
Position: Deputy City Treasurer
Telephone: 0161 234 1017
E-mail: tom.wilkinson@manchester.gov.uk

Name: Tim Seagrave
Position: Commercial Finance Lead
Telephone: 0161 234 3445
E-mail: timothy.seagrave@manchester.gov.uk

Name: Kate Stonehouse
Position: Group Finance Lead – Capital and Treasury Management
Telephone: 0161 245 7853
E-mail: kate.stonehouse@manchester.gov.uk

Name: Charlotte Arrowsmith Jones
Position: Treasury Manager
Telephone: 0161 277 1887
E-mail: charlotte.arrowsmithjones@manchester.gov.uk

Background documents (available for public inspection):

The following documents disclose important facts on which the report is based and have been relied upon in preparing the report.

- Capital Strategy and Budget 2022/23 - 2025/26 report to Executive 15 February 2023
- CIPFA Prudential Code 2021
- CIPFA Treasury Management Code of Practice 2021

Copies of the background documents are available up to 4 years after the date of the meeting. If you would like a copy, please contact one of the contact officers above.

1. **Introduction**

1.1 The Treasury Management Strategy Statement sets out the risk framework under which the Council's treasury management function will operate. By detailing the investment and debt instruments to be used during the year the Strategy details the risk appetite of the Authority and how those risks will be managed.

1.2 The Treasury Management Strategy Statement is linked to the Capital Strategy, in that both documents detail the risks that the Council face, but critically the Treasury Management Strategy Statement is focussed on the risks associated with the management of the Council's cash flow and debt, whereas the Capital Strategy looks at capital investment and expenditure decisions.

1.3 The capital budget contains significant priorities for the Council, such as the refurbishment of the Town Hall, which are to be funded from borrowing. This strategy details how decisions will be taken regarding new borrowing and that the over-arching principle is that the borrowing provides value for money for the Council in whatever form it takes. Capital investment decisions are made in line with the economic and regeneration objectives for the city and to support delivery of the agreed capital strategy.

1.4 For treasury management investments the Council holds security and liquidity as paramount. This strategy proposes the use of investment types aimed at ensuring that funds are kept secure and that the Council has access to funds when they are required.

1.5 The work of the Council's treasury management function is impacted by market conditions and significant economic changes, such as the cost-of-living crisis, which create uncertainty in the market. The strategy has been drafted to provide flexibility to manage the risks associated with uncertainties such as interest rate or liquidity challenges.

Treasury Management Strategy for 2023/24

1.6 The suggested strategy for 2023/24 is based upon the treasury officers' views on interest rates, supplemented with market forecasts provided by the Council's treasury advisor, Link Asset Services.

The strategy covers:

Section 1:	Introduction
Section 2:	CIPFA Definition of Treasury Management
Section 3:	Statutory and other Requirements
Section 4:	Prudential and Treasury Indicators for 2022/23 to 2024/25
Section 5:	Impact of 2012 HRA reform
Section 6:	Current Portfolio Position
Section 7:	Prospects for Interest Rates
Section 8:	Borrowing Requirement
Section 9:	Borrowing Strategy
Section 10:	Annual Investment Strategy
Section 11:	Non-Treasury Investments and Liabilities
Section 12:	Skills and Knowledge
Section 13:	Scheme of Delegation

Section 14: Role of the Section 151 Officer
Section 15: Minimum Revenue Provision (MRP) Strategy
Section 16: Recommendations

Appendix A: Prudential and Treasury Indicators for approval
Appendix B: MRP Strategy
Appendix C: Treasury Management Policy Statement
Appendix D: Treasury Management Scheme of Delegation
Appendix E: The Treasury Management Role of the Section 151 Officer
Appendix F: Economic Background – Link Asset Services
Appendix G: Prospects for Interest Rates
Appendix H: Glossary of Terms
Appendix I: Treasury Management Implications of HRA Reform

2 CIPFA Definition of Treasury Management

2.1 Treasury management is defined by CIPFA as:
'The management of the organisation'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.'

3 Statutory and other requirements

Statutory requirements

3.1 The Local Government Act 2003 (the Act) and supporting regulations require the Council to 'have regard to' the Chartered Institute of Public Finance and Accountancy's (CIPFA) Prudential Code and the CIPFA Treasury Management Code of Practice to set Prudential and Treasury Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable.

3.2 The Act therefore requires the Council to set out its treasury strategy for borrowing and to prepare an Annual Investment Strategy (as required by Investment Guidance subsequent to the Act and included as section 11 of this report); the Strategy sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments.

3.3 The Department for Housing, Communities and Local Government (DHCLG) issued revised investment guidance which came into effect from the 1 April 2010. In 2017 the Department, now the Ministry of Housing Communities and Local Government (MHCLG) further updated its guidance on local government investments. CIPFA responded to these revisions by issuing an updated Code of Practice on Treasury Management and the Prudential Code in 2021.

CIPFA requirements

3.4 The CIPFA Code of Practice on Treasury Management has been adopted by the Council. This strategy has been prepared in accordance with the revised December 2021 Code.

3.5 The primary requirements of the Code are as follows:

a) Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities;
b) Creation and maintenance of Treasury Management Practices which set out the way the Council will seek to achieve those policies and objectives;
c) Receipt by the full Council of an annual Treasury Management Strategy Statement, including the Annual Investment Strategy and Minimum Revenue Provision Policy for the year ahead, a Mid-year Review Report and an Annual Report covering activities during the previous year;
d) Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions;
e) Delegation by the Council of the role of responsible body for treasury management strategy and practices, budget consideration and approval, monitoring and selection of external service providers to a specific named body. For this Council the delegated body is the Audit Committee.
f) Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body. For this Council the delegated body is the Resource and Governance Scrutiny Committee.

3.6 The Council's adherence to the Prudential Code is monitored through the series of Prudential Indicators defined by CIPFA. Adherence to the CIPFA Prudential Code is a factor which informs the Council's investment policy. The legal status of the Treasury Management Code is derived in England and Wales from regulations issued under the Local Government Act 2003. This includes statutory guidance on Local Government investments issued under section 15(1) (a) of the Act.

Balanced Budget Requirement

3.7 It is a statutory requirement under Section 33 of the Local Government Finance Act 1992, revised under Section 31 of the Localism Bill 2011, for the Council to produce a balanced budget. Section 31 requires a local authority to calculate its budget requirement for each financial year to include the revenue costs that flow from capital financing decisions. This means that increases in capital expenditure must be limited to a level whereby increases in charges to revenue from:

- increases in interest charges caused by increased borrowing to finance additional capital expenditure;
- increases to the minimum revenue provision; and
- increases in running costs from new capital projects are limited to a level which is affordable within the projected income of the Council for the foreseeable future.

4 Prudential and Treasury Indicators for 2023/24 to 2025/26

4.1 It is a statutory duty under Section 3 of the Act and supporting regulations that the Council determines and keeps under review how much it can afford to borrow. This amount is termed the 'Affordable Borrowing Limit'. In England this Authorised Limit represents the legislative limit specified in the Act and is one of the key Prudential Indicators identified by the CIPFA Code.

4.2 The Council must have regard to the Prudential Code when setting the Authorised Limit which requires it to ensure that total capital investment remains within sustainable limits.

4.3 Whilst termed an Affordable Borrowing Limit, the capital plans incorporate financing by both external borrowing and other forms of liability such as credit arrangements. The Authorised Limit is to be set on a rolling basis for the forthcoming financial year and two successive financial years.

4.4 The full set of Treasury limits and Prudential Indicators recommended by the Code and used by the Council, together with their suggested levels for 2023/24 is noted in Appendix A of this report.

4.5 Under the revised Prudential and Treasury Management Codes, there are two new indicators introduced this year. They are:

- Net income from commercial and service investments to net revenue stream; and
- Liability benchmark.

4.6 The first new indicator is an indicator of affordability and proportionality, reflecting the scale of the revenue budget which is supported by income generated from non-treasury management investments, and which could be affected by changes to the economy and the financial environment.

4.7 The second indicator is a projection of the amount of loan debt outstanding that the authority needs each year and shows the gap between existing debt and future borrowing needs. It highlights the maturities of future debt needed so that future debt matches future liabilities.

4.8 It should be noted that the Prudential and Treasury Indicators in this report may be subject to change dependent on decisions taken on the Capital and Revenue budgets which are reported elsewhere on this agenda.

5 The Housing Revenue Account – Impact of 2012 HRA Reform

5.1 The Local Government Finance and Housing Act 1989 requires Councils who own housing they rent out to tenants to separate all the financial activities relating to the Council acting as landlord into a ring-fenced account known as the Housing Revenue Account (HRA). Due to the ring-fence, it is illegal for the Council to subsidise any General Fund (GF) activity from its HRA and vice versa.

5.2 The Treasury Management Strategy for 2013/14 was the first to incorporate the split of the Council's debt portfolio following the HRA debt settlement of March 2012 which ended the subsidy arrangement. Details of how the split was calculated and the corresponding effect on treasury management activities are at Appendix I.

5.3 The treasury position of the Council will continue to be monitored at a Council level alongside the separate positions for the GF and the HRA. The HRA is also limited in terms of the treasury activity it can undertake as any temporary borrowing or investing it requires or long-term borrowing will be through the GF. This ensures that the overall Council position is managed as effectively and efficiently as possible.

5.4 To reflect the fact that the HRA now has its own treasury position this report will mention where the HRA treasury strategy may be different to that of the GF. Where the Council strategy is mentioned, this applies to both the GF and the HRA.

6 Current Portfolio Position

6.1 The forecast portfolio position for the end of the current financial year is shown below. The short-term borrowing taken during the pandemic has been refinanced with long term debt from the PWLB, with further PWLB taken to fund the capital programme.

6.2 The Council's forecast treasury portfolio position at 31st March 2023 is:

Table 1	Principal			Av Rate
	GF £'m	HRA £'m	**Total £'m**	%
Long Term Borrowing				
PWLB	500.0	0.0	**500.0**	2.33
Market	330.0	60.7	**390.7**	4.44
Stock	0.9	0.0	**0.9**	4.00
SALIX	6.8	0.0	**6.8**	0.00
HCA	8.5	0.0	**8.5**	0.00
	846.1	60.7	**906.8**	
Short Term Borrowing				
Other	141.3	0	**141.3**	3.51
Gross Debt	987.4	60.7	**1,048.1**	
External Investments	0.0	0.0	**0.0**	0.0
Internal Balances (GF/HRA)	52.9	(52.9)	0	0.0
Net Debt	1,040.3	7.8	**1,048.1**	

6.3 The Capital Financing Requirement measures an Authority's underlying need to borrow or finance by other long-term liabilities for a capital purpose. It represents the amount of capital expenditure that has not yet been resourced absolutely, whether at the point of spend (by capital receipts, capital grants/contributions or from revenue income), or over the longer term by prudent Minimum Revenue Provision (MRP) or voluntary application of capital receipts for debt repayment etc. Alternatively, it provides a figure for the capital expenditure incurred by the Council but not yet provided for.

6.4 The Council's debt is comparatively high compared to other local authorities, due to both the relative size of the authority and the relatively high levels of capital expenditure funded by borrowing in recent years, for example the Our Town Hall refurbishment and the highways maintenance programme. A key element of the treasury management strategy is that debt should be both proportional and affordable, so that the debt costs associated with it are contained within existing revenue resources. To achieve this, the Council's balance sheet is monitored throughout the year, with debt management scenarios reviewed to understand the risks to the Council of changes in interest rates, for example. Decisions taken on new debt seek to balance market conditions with long term affordability.

6.5 The long-term forecast for external debt in comparison to the Capital Financing Requirement, known as the Liability Benchmark, is shown at Appendix 1. This highlights the level of internal borrowing, where the council is using its own cashflow and cash backed reserves in lieu of external debt. However, with the planned use of reserves to support the revenue and capital budgets means this position will change and further external borrowing will be required. External debt peaks as the forecast capital programme for approved schemes ends and will change as further projects are approved and the level of internal borrowing reduced.

6.6 The forecast profile for the Capital Financing Requirement is shown in the table below:

	2022/23	2023/24	2024/25	2025/26	2026/27
	£'m				
Opening CFR	1,768.3	1,988.4	2,176.5	2,216.2	2,172.6
New Borrowing	255.8	208.6	84.0	3.3	
Additional long-term liabilities [1]	0.9	20.8	0.7	1.3	1.6
MRP	(36.6)	(41.3)	(45.0)	(48.2)	(47.6)
Closing CFR	**1,988.4**	**2,176.5**	**2,216.2**	**2,172.6**	**2,126.6**

6.7 The Capital Financing Requirement of the City Council as at 31st March 2023 is forecast to be c. £1.99bn. The difference between this and the actual gross debt of the Council is c. £0.9bn which is the amount of funding that the Council has internally borrowed or has been funded through credit arrangements. This reflects the Council's ongoing treasury strategy of using internal cash to reduce the amount of borrowing required rather than holding this cash as investments.

6.8 This strategy reflects the current environment where the rate of interest on investments is significantly lower than that on borrowing and there are substantial counterparty risks, this has been a prudent approach and has provided value for money for the Council. Internal cash refers to cash surpluses which arise from holding of reserves and timing of receipts and payments.

6.9 As part of the reform of the HRA, on the 28th March 2012 the then DHCLG repaid all the Council's Public Works Loan Board (PWLB) debt which had been gradually reduced over recent years by various housing stock transfers. Subsequently the HRA debt portfolio consists almost exclusively of market debt, the majority of which are Lender Option Borrower Option (LOBO) loans which have long-term maturity dates. Whilst this provides some stability for the Council as LOBOs are unlikely to be called in the near future due to the current and forecast market environment, it does mean that when seeking to take new debt the Council should consider diversifying the portfolio, not least to ensure a wider range of maturity dates.

6.10 The portfolio at 31st March 2023 includes Council Stock with a value of £0.9m. This Stock debt is attributable to the irredeemable class of stock where stockholders have not taken up the Council's redemption offer made in 2017/18.

[1] The additional long term liabilities are likely to increase following the introduction of international Financial Reporting Standard 16, due in April 2024. Work is underway to identify the impact of this, and it will be reported to members in due course, the estimate included in these figures is a c. £20m increase.

7 Prospects for Interest Rates

7.1 The Council has appointed Link Asset Services as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. Appendix G draws together several current City forecasts for short term (Bank Rate) and longer fixed interest rates. The following gives Link's central view for interest rates at financial year ends (March):

- 2023: 4.25%
- 2024: 4.00%
- 2025: 3.00%

7.2 There is no certainty to these forecasts. A detailed view of the current economic background prepared by Link Asset Services is at Appendix F to this report.

7.3 The Council seeks to maintain a portfolio of debt and investments that is a mix of fixed and variable interest rates. Whilst fixed interest rates give the Council certainty, there is also a risk that prevailing market rates change and there are then opportunities to either increase the rate of return on investments or reduce the rate of interest on debt which could not be taken if the whole portfolio was fixed.

7.4 The Council's treasury management investments are classed as variable as the Council invests short term to enable the cash flow to be managed. In terms of debt, the Council has a significant portfolio of fixed rate debt, but as noted above a significant element of this is LOBO debt which means that there are risks that the interest rate on that debt could change. The Council monitors this position, including the likely use of the Lender Options, and will make future borrowing decisions with a view to keeping the debt portfolio balanced between fixed and variable debt.

8 Borrowing Requirement

8.1 The potential long-term borrowing requirements over the next three years are:

Table 2	**2023/24**	**2024/25**	**2025/26**
	£'m	**£'m**	**£'m**
	estimate	**estimate**	**estimate**
Planned Capital Expenditure funded by Borrowing	208.6	84.0	3.3
Change in Grants & Contributions	26.1	31.0	0.0
Change in Capital Receipts	(23.4)	(11.1)	(2.4)
Change in Reserves	69.5	70.7	45.0
MRP Provision	(37.2)	(40.6)	(43.6)
Refinancing of maturing debt (GF)	93.7	11.5	0.0
Refinancing of maturing debt (HRA)	0.0	0.0	0.0
Movement in Working Capital	80.0	0.0	0.0
Estimated Borrowing Requirement	**417.3**	**145.5**	**2.3**
Funded by:			
GF	417.3	145.5	2.3
HRA	0.0	0.0	0.0

9 Borrowing Strategy

General Fund

9.1 Following the HRA debt settlement in 2012 the Council's debt position is one of significant internal borrowing meaning cash backed reserves and provisions are being used in lieu of external debt. The external debt held is predominantly long term in nature.

9.2 The proposed Capital Budget, submitted to Executive in February and Council in March, contains significant capital investment across the city. The scale of the investment will mean that the Council will need to undertake external borrowing in the future and will not be able on to rely on internal borrowing alone. Where possible, internal borrowing will remain the first option due to the interest savings generated.

9.3 Under the Prudential Code, the Council must make an annual revenue provision for the repayment of debt, called the minimum revenue provision (MRP). This spreads the cost of repaying the debt for an asset over the useful economic life of the asset. It is a real cost and will impact the revenue budget position. The MHCLG MRP guidance is followed and principles applied. The following asset lives are used when calculating MRP, unless there are asset-specific reasons for deviating from them – such deviation will be guided by qualified valuers recommendations on maximum useful lives:

- Land: 50 years
- Property: 50 years
- Highways: 25 years
- ICT: 5 years

9.4 The Council's borrowing strategy will utilise the annual provision it is required to make to reduce debt, in the form of its Minimum Revenue Provision (MRP). If MRP is not used to reduce external debt it is held as cash, so the most efficient arrangement is for MRP to be used to reduce the new long-term debt expected to be required. This ensures that MRP is utilised and does not accumulate as cash on the Balance Sheet. Alternatively, MRP could be used to repay existing debt early but this would be at considerable cost in the current interest rate environment.

9.5 Beyond the forecast period for capital investment and matching to the same principles as above, a prudent strategy is to seek to borrow in the medium term with maturities to match the estimated MRP that is generated in the same period. This avoids an accumulation of cash on the Balance Sheet that would need to be invested at a potential net cost and investment risk to the Council.

9.6 The overall strategy is therefore for the Council to continue to use reserves and provisions to maximise internal borrowing whilst seeking to rebalance the portfolio with more medium-term debt when there is a need to externally borrow. This must be done with a strong focus on achieving value for money on interest costs and balancing the risks to the overall debt portfolio over the long term.

HRA

9.7 The Council's proposed capital budget for 2023/24 and beyond does not contain any requirement for the HRA to borrow additional sums. It is expected that proposals may be brought forward that require funding via borrowing, which would create a borrowing requirement for 2023/24 or future years. The level of borrowing affordable is restrained by the statutory requirement for the HRA Business Plan to avoid going into a deficit, and as such any long-term borrowing that is taken to invest in capital assets would have to generate sufficient income to cover the costs of financing the debt and be supported by a sufficiently robust business case.

9.8 The impact of any required further long-term borrowing on the Business Plan will be reviewed which will inform the borrowing options pursued. Any temporary borrowing required will be sought from the General Fund, as per the pooled funding approach which is discussed further in Appendix I.

9.9 Note, if some of the current debt is required to be repaid, for example if one of the LOBO loans was called, the refinancing arrangements would need to be considered.

Borrowing Options

9.10 The overall forecast for long-term borrowing rates is that they are expected to rise gradually during 2023/24 and will continue to increase in future years from their historically low levels. In terms of the Council's borrowing strategy there are three options:

i. Internal borrowing
ii. Short to medium term borrowing
iii. Long term borrowing

The Treasury Management team will continue to monitor and manage the risk of each of the above borrowing options. At such time the Council will need to borrow, the debt market will be actively monitored and the borrowing strategy which delivers the optimum value for money will be chosen. The short-term advantage of internal and short-term borrowing will be weighed against the potential cost if long term borrowing is delayed.

9.11 Some of the expected options for new borrowing are noted below. All options will be evaluated alongside their availability, and which provides best value for money. The options below are not presented in a hierarchical order.

- **Public Works Loan Board (PWLB)**

In February 2020 Parliament reformed the statutory basis of the PWLB, transferring lending powers to HM Treasury. In March 2020 the government consulted on revising the PWLB's lending terms to reflect the new governance arrangements as well as to end the situation in which a minority of local authorities used PWLB loans to fund debt for yield activity via commercial investments. The government published its response to this consultation and implemented these reforms in November 2020.
Additional requirements to borrow from PWLB were introduced. Each local authority that wishes to borrow from the PWLB will need to submit a high-level description of their capital spending and financing plans for the following three years, including their expected use of the PWLB. Any investment assets bought primarily for yield will not be supported by PWLB.

Local Authorities will be asked to:

i. Categorise Capital Spending into: Service Spending, Housing, Regeneration, Preventative Action, Treasury Management, and Debt for Yield activity.
ii. Provide a short description covering at least 75% of the spending in each category.
iii. Provide assurance from the section 151 officer or equivalent that the local authority is not borrowing in advance of need and does not intend to buy investment assets primarily for yield.

PWLB borrowing is available between 1- and 50-year maturities on various bases. This offers a range of options for new borrowing which could spread debt maturities away from a concentration in longer dated debt and allow the Council to align maturities to MRP.

In June 2021, the UK Infrastructure Bank launched. It is independent of HM Treasury, and aims to lend to local authorities for strategic and high value projects alongside the private sector. One of the access routes to the bank is through the PWLB, and the Council would evaluate this option if it were available.

The Link forecast for the PWLB Certainty Rate is as follows:

Table 3	**Mar 23**	**Jun 23**	**Sep 23**	**Dec 23**	**Mar 24**	**Dec 24**	**Mar 25**	**Dec 25**
	%							
Bank Rate	4.25	4.50	4.50	4.50	4.00	3.25	3.00	2.50
5 yr PWLB rate	4.20	4.20	4.10	4.00	3.90	3.50	3.40	3.10
10 yr PWLB rate	4.40	4.40	4.30	4.10	4.00	3.60	3.50	3.30
25 yr PWLB rate	4.60	4.60	4.50	4.00	4.20	3.90	3.70	3.50
50 yr PWLB rate	4.30	4.30	4.20	4.10	3.90	3.60	3.50	3.20

A more detailed Link forecast is included in Appendix G to this report.

- **European Investment Bank (EIB)**

Historically, the EIB rates for borrowing were generally favourable compared to PWLB although the margin of benefit has now reduced as a result of the U.K. withdrawing from the EU and the reversal of PWLB rates as described above. The Council still has access to EIB along with the option to forward fix rates for borrowing and this option will be considered if the conditions can be met and it offers better value for money. The EIB appraises its funding plans against individual schemes, particularly around growth and employment and energy efficiency, and any monies borrowed are part of the Council's overall pooled borrowing.

- **Third Party Loans**

These are loans from third parties that are offered at lower than market rates, for example Salix Finance Ltd is offering loans to the public sector at 0% to be used specifically to improve their energy efficiency and reduce carbon emissions.

- **Inter-Local Authority advances**

Both short- and medium-term loans are often available in the inter Local Authority market.

- **Market Loans**

Following the reversal of the PWLB rates noted above, there has been a decrease in market activity relating to local authority debt as the debt pricing and structure offer less value for money compared to PWLB.

Market loans offer forward fixing, which is not an option with PWLB, however as rates are forecast to remain relatively low over the next few years forward fixing brings marginal advantage.

- **Local Authority Bond Agency**

The UK Municipal Bonds Agency was established in June 2014 with the primary purpose of reducing local authority financing costs by:

- Issuing bonds in the capital markets and on-lending to councils.
- Lending between councils.
- Sourcing funding from 3rd party sources, and on-lending to councils.

The Agency's aim is to raise finance for Local Authorities by issuing municipal bonds to capital markets. The Agency has successfully issued a small number of bonds for local authorities, and the Council will continue to monitor the Agency's development and whether it can offer a competitive option for future borrowing.

9.12 These types of borrowing will need to be evaluated alongside their availability, particularly whilst there is a very limited availability of traditional market loans. The traditional market loans available tend to be Lender Option Borrower Option (LOBO) loans and they are not currently offered at competitive rates of interest. LOBOs provide the lender with future options to increase the interest rate whilst the local authority has the option to repay if the increase in the rate is unacceptable to them.

9.13 Following HRA reform the vast majority of the Council's existing debt portfolio consists of LOBOs and the Authority continues to need to consider diversifying its loan book to reduce the impact of any volatility that may cause these loans to be called It should be noted that the Council's current LOBO loans are considered unlikely to be called in the medium term, despite the interest rises across the last year. However, should long term interest rates increase further, this risk of call will also increase.

Sensitivity of the forecast

9.14 In normal circumstances the main sensitivities are likely to be the two scenarios noted below. Council officers in conjunction with the treasury advisors will continually monitor the prevailing interest rates and the market forecast, adopting the following responses to a change of sentiment:

- ***If it were felt that there was a significant risk of a sharp FALL in long- and short-term rates***, e.g. due to a marked increase of risks around relapse into recession or of risks of deflation then long-term borrowings will be postponed.

- ***If it were felt that there was a significant risk of a much sharper RISE in long and short term rates than that current forecast***, perhaps arising from a greater than expected increase in world economic activity or a sudden increase in inflation risks, the portfolio position will be re-appraised. The likely action will be that fixed rate funding will be drawn whilst interest rates remain relatively cheap.

External v. Internal borrowing

9.15 The current borrowing position reflects the historic strong Balance Sheet of the Council as highlighted in Section 6. The policy remains to keep cash as low as possible and minimise temporary investments.

9.16 The next financial year is again expected to be one of rates continuing to rise as the Bank of England looks to tackle inflation, with the expectation that rates will fall back in the medium term albeit not to the recent historic lows. At Appendix F there is an in-depth analysis of economic conditions provided by Link Asset Services, the Council's independent treasury advisors.

9.17 Over the next three years, investment rates are expected to be continue to be below long-term borrowing rates. This would indicate that value could best be obtained by limiting new external borrowing and by using internal cash balances to finance new capital expenditure or to replace maturing external debt.

9.18 This will be weighed against the potential for incurring additional long-term costs by delaying new external borrowing until later years when longer term rates could be marginally higher. Consideration will also be given to forward fixing rates whilst rates are favourable.

9.19 Against this background caution will be adopted within 2022/23 treasury operations. The Deputy Chief Executive and City Treasurer will monitor the interest rate market and adopt a pragmatic approach to changing circumstances, reporting any decisions to the appropriate decision-making body at the next available opportunity.

Policy on borrowing in advance of need

9.20 From a statutory point of view a Local Authority has the power to invest for 'any purpose relevant to its functions under any enactment, or for the purposes of the prudent management of its financial affairs.' DLUCH takes an informal view that local authorities should not borrow purely to invest at a profit. This does not prevent the Council temporarily investing funds borrowed for the purpose of expenditure in the reasonable near future.

9.21 This Council will not borrow in advance of need to on-lend and profit from the difference in interest rate. Any decision to borrow in advance in support of strategic and service delivery objectives will be in the context of achieving the best overall value for money, for example to minimise the risk of borrowing costs increasing in the future and that the Council can ensure the security of such funds. In determining whether borrowing is undertaken in advance of need the Council will:

- ensure that there is a clear link between the capital programme and maturity profile of the existing debt profile which supports the need to take funding in advance of need;
- ensure the ongoing revenue liabilities created and implications for future and budget have been considered;

- evaluate the economic and market factors that might influence the manner and timing of any decision to borrow;
- consider the merits and demerits of alternative forms of funding;
- consider the alternative interest rate bases available, the most appropriate periods to fund and repayment profiles to use; and
- consider the impact of borrowing in advance temporarily (until required to finance capital expenditure) increasing investment cash balances and the consequent increase in exposure to counterparty risk, and other risks, and the level of such risks given the controls in place to minimise them.

Forward Fixing

9.22 As noted above, the Council will consider forward fixing debt, whereby the Council agrees to borrow at a point in the future at a rate based on current implied market interest rate forecasts. There is a risk that the interest rates proposed would be higher than current rates; however, it can be beneficial as it avoids the need to borrow in advance of need and suffer cost of carry. It can also play an important role in providing certainty of rates as part of the overall portfolio of debt. It may also represent a saving if rates were to rise in the future. Any decision to forward fix will be reviewed for value for money and will be reported to Members as part of the standard treasury management reporting.

Debt Rescheduling

9.23 It is likely that opportunities to reschedule debt in the 2023/24 financial year will be limited due to prevailing debt interest rates being relatively similar to existing debt.

9.24 As short-term borrowing rates are expected to be cheaper than longer term rates, there may be some opportunity to generate savings by switching from long term debt to short term debt. These savings will need to be considered in the light of the premiums incurred and the likely cost of refinancing those short-term loans once they mature, and the risk of sudden changes in the short-term debt markets, compared to the current rates of longer-term debt in the existing portfolio.

9.25 The debt portfolio following HRA reform consists mainly of LOBOs, and the premia for rescheduling these make it unlikely there will be a cost-effective opportunity to reschedule. The premia relate to the future interest payments associated with the loan and compensation for the lender for the buy-back of the interest rate options the loan has embedded in it.

9.26 The Council will continue to monitor the LOBO market and opportunities to reschedule, redeem or alter the profile of existing LOBO debt. The reasons for any rescheduling to take place will include:

- the generation of cash savings and / or discounted cash flow savings;
- helping to fulfil the strategy outlined above in this section;
- enhancing the balance of the portfolio (amending the maturity profile and/or the balance of volatility)

9.27 Any restructuring of LOBOs will only be progressed if it provides value for money and reduces the overall treasury risk the Council faces. The Council’s Constitution delegates to the Deputy Chief Executive and City Treasurer the authority to pursue any restructuring, rescheduling or redemption opportunities available.

9.28 Consideration will also be given to the potential for making savings by running down investment balances to repay debt prematurely. It is likely short-term rates on investments will be lower than rates paid on current debt.

9.29 All rescheduling will be reported to the Executive as part of the normal treasury management activity. If rescheduling requires amendments to the Treasury Management Strategy the Deputy Chief Executive and City Treasurer will be asked to approve them in accordance with the delegated powers accorded to the position and the changes will be reported to Members.

10 Annual Investment Strategy

HRA

10.1 In order to maintain efficient, effective and economic treasury management for the Council as a whole, the HRA will only be able to invest with the General Fund. This is discussed further in Appendix I.

General Fund

Introduction

10.2 The Council will have regard to the MHCLG’s Guidance on Local Government Investments (the Guidance) and the 2011 and 2021 revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes (the CIPFA TM Code). The Council’s investment priorities are:

- The security of capital; and
- The liquidity of its investments.

10.3 The risk appetite of the Council is low in order to give priority to the security of its investments. The Council will aim to achieve the optimum return on its investments commensurate with desired levels of security and liquidity.

10.4 The borrowing of monies by an Authority purely to invest or on-lend and make a return is unlawful and this Council will not engage in such activity. However, the Council may provide loan finance funded from borrowing if this supports the achievement of the Council’s strategies and service objectives.

10.5 The Council’s TMSS focusses solely on treasury management investments. The Council does not hold any commercial investments and details of strategic capital investments can be found in the Capital Strategy and Budget Report to the Executive.

Investment Policy

10.6 The Council’s investment policy is to manage the Council’s cash flow through investments in high credit quality.

10.7 As in previous years, the Council will not just utilise ratings as 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. The Council will engage with its advisors to maintain a monitor on market pricing such as 'credit default swaps'[2] and overlay that information on top of the credit ratings.

10.8 In line with the policy adopted in this strategy in previous years, options to diversify the investment portfolio have been reviewed and adopted. The Council now actively uses money market funds alongside deposits with banks, other local authorities and the Debt Management Agency.

10.9 For 2023/24 the Council will continue to consider investing in Treasury Bills, Certificates of Deposit and Covered Bonds. In addition to diversification each of these options offer the Council benefits which are noted in more detail below. These instruments require the Council to have specific custodian and broker facilities which have been opened. Officers are working to monitor these markets to prompt participation in the instruments when rates are favourable, and to identify and resolve any governance challenges arising from investing in instruments which have an active secondary market. Work is continuing to open further access points to markets and to identify opportunities for benefit which are new to the Council.

10.10 It should be noted that, whilst seeking to broaden the investment base officers will seek to limit the level of risk taken. It is not expected that the measures considered above will have a significant impact on the rates of return the Council currently achieves.

Specified and Non-Specified Investments

10.11 Investment instruments identified for use in the financial year are listed below and are all specified investments. Any proposals to use other non-specified investments will be reported to Members for approval.

10.12 Specified investments are sterling denominated, with maturities up to a maximum of one year and meet the minimum 'high' rating criteria where applicable. Further details about some of the specified investments below can be found in later paragraphs in this Section.

Table 4	Minimum 'High' Credit Criteria	Use
Term deposits – banks and building societies[3]	See Creditworthiness Policy.	In-house
Term deposits – other Local Authorities	High security. Only few local authorities' credit-rated	In-house
Debt Management Agency Deposit Facility	UK Government backed	In-house

[2] A credit default swap is a financial instrument that effectively provides the holder insurance against a loan defaulting. The CDS spread is the difference between the price at which providers are willing to sell the swap, and the price at which buyers are willing to buy. A relatively high spread may suggest that the loan is more likely to default.

[3] Banks & Building Societies

The Council will keep the investment balance below or at the maximum limit based on the institutions credit rating as detailed in paragraph 10.21-10.22. If this limit is breached, for example due to significant late receipts, the Deputy Chief Executive and City Treasurer will be notified as soon as possible after the breach, along with the reasons for it. Please note this relates to specific investments and not balances held within the Council's bank accounts, including the general bank account.

Certificates of deposit issued by banks and building societies covered by UK Government guarantees	UK Government explicit guarantee	In-house
Money Market Funds (MMFs)	AAA	In-house
Treasury Bills	UK Government backed	In-house
Covered Bonds	AAA	In-house

Creditworthiness Policy

10.13 The Council applies the creditworthiness service provided by Link Asset Services. This service employs a sophisticated modelling approach utilising credit rating from the three main credit rating agencies; Fitch, Moody's and Standard & Poor's. Link supplement the credit ratings of counterparties with the following overlays:

- Credit Watches and Credit Outlooks from credit rating agencies
- Credit Default Swap spreads to provide early warning of likely changes in credit ratings
- Sovereign Ratings to select counterparties from only the most creditworthy countries

10.14 The above are combined in a weighted scoring system which is then combined with an overlay of CDS spreads. The product is a series of colour coded bands which indicate the relative creditworthiness of counterparties.

10.15 The Council has regard to Link's approach to assessing creditworthiness when selecting counterparties as it uses a wider array of information than just primary ratings and by using a risk weighted scoring system does not give undue prominence to just one agency's ratings.

10.16 In summary the Council will approach assessment of creditworthiness by using the Link counterparty list and then applying its own counterparty limits and durations. All credit ratings will be monitored daily and re-assessed weekly. The Council is alerted to changes to ratings of all three agencies through its use of the Link creditworthiness service.

- 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 Credit Default Swap against the iTraxx benchmark[4] and other market data on a weekly basis. Extreme market movements may result in the downgrade of an institution or removal from the Council's lending list.

10.17 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, information on government support for banks and the credit ratings of that government support.

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[4] The Markit iTraxx Senior Financials Index is a composite of the 25 most liquid financial entities in Europe. The index is calculated through an averaging process by the Markit Group and is used as the benchmark level of CDS spreads on Link Asset Services' Credit List.

Investment Limits

10.18 In applying the creditworthiness policy, the Council holds the security of investments as the key consideration and will only seek to make treasury investments with counterparties of high credit quality.

10.19 The financial investment limits of financial institutions will be linked to their short and long-term ratings (Fitch or equivalent) as follows:

<u>Long Term</u>	<u>Amount</u>
Fitch AA+ and above	£20 million
Fitch AA/AA-	£15 million
Fitch A+/A	£15 million
Fitch A-	£10 million
Fitch BBB+	£10 million

The Council will only utilise those institutions that have a short-term rating of F2 or higher, (Fitch or equivalent).

UK Government (including the Debt Management Office)	£200 million
Greater Manchester Combined Authority	£200 million
Other Local Authorities (inc. pension funds)	£20 million

10.20 In seeking to diversify the Council will utilise other investment types which are described in more detail below and ensure that the investment portfolio is mixed to help mitigate credit risk. The following limits will apply to each asset type:

Total Deposit	**Amount**
Local Authorities	£250 million
UK Government - Debt Management Office - Treasury Bills	£200 million
Money Market Funds	£75 million
Certificates of Deposit	£25 million
Covered Bonds	£25 million

10.21 It may be prudent to temporarily increase the limits shown above, if the prevailing economic environment means that it becomes difficult for officers to place funds. If this is the case officers will seek approval from the Deputy Chief Executive and City Treasurer and any increase in the limits will be reported to Members through the normal treasury management reporting process.

Durational Limits

10.22 Operationally the Council has in recent years not invested cash for more than three months, which was a product of security concerns following the financial crisis of 2008/09 and the relatively volatile nature of the Council's cash flow.

10.23 The financial markets have changed significantly since 2008/09, and the transparency of creditworthiness has improved. It is therefore proposed that the Council formally states, as part of the Investment Strategy, that it will invest for up to 364 days provided that such investments form part of the management of the cash flow and not for increased yield. On this basis, such investments will only be made if the cash flow forecast at the time indicates a level of "core" cash which will not be required for the investment period.

Environmental, Social and Governance Investment Policy

10.24 The investment classes detailed in this Strategy are almost exclusively short term in nature, and therefore establishing investment criteria for environmental, social and governance (ESG) factors is challenging.

10.25 There are several approaches to ESG investing, but they all focus on investments which will have a positive return and a long-term impact in people, the environment, and how business is conducted. This is particularly important when the investment takes the form of equity, and therefore the investor can use their influence in corporate matters.

10.26 None of the investment classes contained within this Strategy provide that level of influence. Instead, the treasury management team will continue to screen potential investments to make sure that institutions demonstrate a significant level of commitment to ESG matters, are aligned to the Council's corporate objectives and approaches, and will not invest if there are concerns.

Money Market Funds

10.27 The removal of the implied levels of sovereign support that were built into ratings throughout the financial crisis has impacted on bank and building society ratings across the world. Rating downgrades can limit the number of counterparties available and to provide flexibility the Council will use MMFs when appropriate as an alternative specified investment.

10.28 MMFs are investment instruments that invest in a variety of institutions therefore diversifying the investment risk. The funds are managed by a fund manager and have objectives to preserve capital, provide daily liquidity and a competitive yield. Most money market funds invest both inside and outside the UK. MMFs also provide flexibility as investments and withdrawals can be made daily.

10.29 MMFs are rated through a separate process to bank deposits. This looks at the average maturity of the underlying investments in the Fund as well as the credit quality of those investments. The Council will only use MMFs where the institutions hold the highest AAA credit rating and those which are UK or European based.

10.30 As with all investments there is some risk with MMFs in terms of the capital value of the investment. European legislation has required existing and new Constant Net Asset Value MMFs to convert to a Low Volatility Net Asset Value (LVNAV) basis by January 2019. This basis allows movements in capital value, but there is a restriction that the deviation cannot be more than 20 basis points, e.g. on a deposit of £100 the Fund must ensure withdrawal proceeds are no greater than +/- 20p.

Treasury Bills

10.31 Treasury Bills are marketable securities issued by the UK Government and counterparty and liquidity risk is relatively low although there is potential risk to value arising from an adverse movement in interest rates unless they are held to maturity.

Certificates of Deposit

10.32 Certificates of Deposit are short dated marketable securities issued by financial institutions, so the counterparty risk is low. The instruments have flexible maturity dates, so it is possible to trade them in early although there is a potential risk to capital if they are traded ahead of maturity and there is an adverse movement in interest rates. Certificates of Deposit are subject to bail-in risk as they are given the same priority as fixed deposits if a bank was to default. The Council will only deal with Certificates of Deposit that are issued by banks and meet the credit criteria.

Covered Bonds

10.33 Covered Bonds are debt instruments secured by assets such as mortgage loans. They are issued by banks and other non-financial institutions. The loans remain on the issuing institutions' Balance Sheet and investors have a preferential claim in the event of the issuing institution defaulting. All issuing institutions are required to hold enough assets to cover the claims of all covered bondholders. The Council would only deal with bonds that are issued by banks which meet the credit criteria, or AAA rated institutions, (e.g. insurance companies).

Liquidity

10.34 Based on cash flow forecasts, the level of cash balances in 2023/24 is estimated to range between £0m and £300m. The higher level can arise where for instance large Government grants are received or long-term borrowing has recently been undertaken.

Investment Strategy to be followed in-house

10.35 Link's view of the forecast Bank Rate is noted at Section 9. Link's view is that the Bank Rate will increase during 2023, given the high inflation outlook.

10.36 There will remain a cost of carry to any new borrowing which causes an increase in investments as this will incur a revenue loss between borrowing costs and investment returns.

10.37 The Council will avoid locking into longer term deals while investment rates are at historically low levels unless attractive rates are available with counterparties of particularly high creditworthiness which make longer term deals worthwhile and within the risk parameters set by the Council.

10.38 The Council uses the Sterling Overnight Index Average (SONIA) as a benchmark rate for investments and temporary borrowing following the phasing out of LIBOR by the Bank of England and the Financial Conduct Authority (FCA). SONIA represents the overnight rate of interest banks pay to borrow sterling overnight, unsecured, from other financial institutions.

10.39 This change means that the benchmark rate is now based on observable data, whereas LIBOR/ID was based on information provided by major banks. The impact on SONIA of changes in the Bank of England bank rate is far more immediate, particularly when compared to the investment instruments that the Council uses where there is a time lag between bank rate changing and the rate offered for the instrument reflecting that change.

10.40 For 2022/23 it is suggested the Council should target an investment return on investments placed during the financial year that is close to the SONIA. This reflects the ongoing market uncertainty, and the short term nature of any cash that the Council holds. For cash flow generated balances, the Council will seek to utilise its business reserve accounts and short-dated deposits (overnight to six months) in order to benefit from the compounding of interest.

10.41 The SONIA rate will also be applied to any transfer rates between the General Fund and the HRA, further details are outlined in Appendix I. Treasury Management will apply mitigating changes to the transfer rates if the benchmark rates were to go into negative territory

End of year Investment Report

10.42 At the end of the financial year, the Council will receive a report on investment activity as part of the Annual Treasury Management Report.

Policy on the use of External Service Providers

10.43 The Council uses Link Asset Services as external treasury management advisors and has access to another provider who is an approved supplier should a second opinion or additional work be required. The Council recognises that responsibility for treasury management decisions always remains with the organisation and will ensure that undue reliance is not placed upon its external service providers.

10.44 The Council recognises there is value in employing external providers of treasury management services to acquire access to specialist skills and resources. It will ensure the terms of the Advisor's appointment and the methods by which their value is assessed are properly agreed and documented and subjected to regular review.

11 Non-Treasury Investments and Liabilities

11.1 CIPFA's revised Prudential and Treasury Management Codes acknowledge that authorities may hold non-treasury investments. These are investments held for service purposes, such as housing or regeneration, or commercial purposes. They are non-treasury because they are not related to the management of the authority's cash flows. Non-treasury investments are classed as capital expenditure.

11.2 The Council has a portfolio of non-treasury investments, including investment property, as outlined below. Such capital investments are regularly reviewed to ensure they continue to perform as expected. Whilst these investments are held for fundamentally different reasons compared to treasury management investments, it is important to set out how they will be managed, and the Council's overall approach.

Approach, Due Diligence and Risk Appetite

11.3 Council investments are managed in line with the Department for Levelling Up, Homes and Communities (DLUHC) investment guidance principles of security, liquidity and yield. The application of these principles will differ when considering capital investment rather than treasury management investment. The risk appetite for these two distinct types of investment may also differ as capital investments also consider the broader strategic and regeneration objectives and benefits.

11.4 Capital investments are considered in line with the Checkpoint process. Schemes could include lending to organisations with low credit ratings if the appropriate security over the organisations assets or guarantees from parent companies or organisations can be given. A key consideration is that income received from the investment covers the capital financing costs incurred.

Summary of material investments, guarantees and liabilities

11.5 The Council has the current historic investments on the balance sheet as at 31st March 2022:

	Value as at 31/3/22
	£m
Long-term debtors	486.2
Long-term investments	141.5
Investment Property	493.7
Total	**1,121.4**

11.6 Long-term debtors are loan finance provided by the Council, including the loans to Manchester Airport (£313.9m), Public Finance Initiative prepayments (£20.9m), and Manchester College (£19.0m), for which repayments have begun. These loans are regularly reviewed and would be impaired if there was a risk of default.

11.7 Long-term investments are equity investments held including Manchester Airport (£112.4m), a car park at Manchester Airport (£4.8m), Destination Manchester (£10.2m) which is the Council's investment in Manchester Central, Manchester Science Park (£6.2m) and Matrix Homes (£5.6m). Investments are valued on an annual basis.

11.8 Investment property is held on the basis that it will generate a revenue return, for example land at Manchester Airport and at Eastlands. Some of the properties are held for regeneration purposes but as they provide a return they have to be shown as investment property. Investment properties are independently valued on an annual basis.

11.9 The capital programme contains the following which will create either long-term debtors, investments or investment properties:

- Waste Contract - providing a loan to the contractor to upgrade vehicles.
- Civic Quarter Heat Network - creation of a heat network through a Council-owned company.
- Private Sector Housing Equity Loans - loans to residents to provide housing support
- This City – debt and equity to create a housing company providing affordable housing; and
- Victoria North – loans to support the Victoria North joint venture in acquiring land.

11.10 There may be other projects which become capital investments, such as to support the Eastern Gateway and Victoria North.

11.11 All investments are scrutinised via the capital approval process, including to Executive and Council as required, with independent financial, legal and other relevant advice sought.

11.12 Where investments provide a return through interest or dividends this can be used to support the revenue budget. For example, in 2022/23 c. £24.9m of dividends will be used within the revenue budget. Where investments are funded by borrowing the income received is used to fund the capital financing costs, for example the Airport Strategic Loan.

11.13 All investments are monitored regularly with the frequency based on risk, and any material changes are reported to the Deputy Chief Executive and City Treasurer at the earliest opportunity.

Commercial Investments

11.14 Capital investments are made for strategic or regeneration purposes. The Council will not invest in capital schemes purely for yield, although some schemes will be financed all or in part from returns on investment. Usually, investment will be within the local authority area, although there may be exceptions if it is within the relevant economic area and meets a key regeneration or zero carbon objective.

11.15 It is worth noting that investment property is considered, under CIPFA's Prudential Code, as a commercial investment, and so the Council does have assets of a commercial nature on the balance sheet.

11.16 Following the consultation on the future of the PWLB and the introduction of new terms for accessing PWLB loans, local authorities are actively discouraged from investing in assets primarily for yield. All proposed capital investments will have to be reviewed against PWLB guidance to assess whether they are:

- Service spending;
- Investment in housing;
- Regeneration;
- Investment as preventative action; or
- Investment in assets primarily for yield.

11.17 The decision over whether a project complies with the terms of the PWLB is for the Council's Section 151 officer but may be reviewed by Treasury and external auditors. Where local authorities do invest in assets primarily for yield, irrespective of how such assets are financed, access to the PWLB for new debt will be removed apart from for refinancing existing debt.

11.18 The outcome of the consultation also requires local authorities to only invest within their economic area.

12 Skills and Knowledge

12.1 Information, advice and training on the capital checkpoint processes is available for officers and members. The Capital Programme team use their experience to evaluate new capital investment proposals. All proposals are reviewed by the Senior Management Team, including the Deputy Chief Executive and City Treasurer. Capital investments are reviewed under the same approval process with input from appropriately qualified and skilled Finance professionals and external advisors where required.

12.2 Since January 2018 the Markets in Financial Instruments Directive II (MiFID II) regulations are in force. For the Council to continue to invest as before it is required to opt up to become a “Professional Status” counterparty. Those with responsibility for the delivery of the treasury management function must be able to demonstrate that they have significant skills and experience of working in a market environment. The existing team fulfils this requirement, and the Council currently holds “Professional Status”.

13 Scheme of Delegation

13.1 Appendix D describes the responsibilities of Member groups and officers in relation to treasury management.

14 Role of the Section 151 Officer

14.1 Appendix E notes the definition of the role of the Deputy Chief Executive and City Treasurer in relation to treasury management.

15 Minimum Revenue Provision (MRP) Strategy

15.1 Appendix B contains the Council’s policy for spreading capital expenditure charges to revenue through the annual MRP charge.

16 Recommendations

16.1 Please see the start of the report for the list of recommendations.

17 Contributing to a Zero-Carbon City

17.1 Treasury Management activity underpins the Council’s finances, and therefore supports projects and initiatives which seek to achieve the Council’s zero carbon target.

18 Contributing to the Our Manchester Strategy

18.1 The Treasury Management function supports the whole Council by seeking to ensure that funding is available when required, to fund all the work that the Council undertakes. Therefore, whilst not directly contributing to the strategic aims, the Council’s treasury management activity underpins the work taking place elsewhere to achieve the outcomes.

19 Key Policies and Considerations

(a) Equal Opportunities

19.1 None.

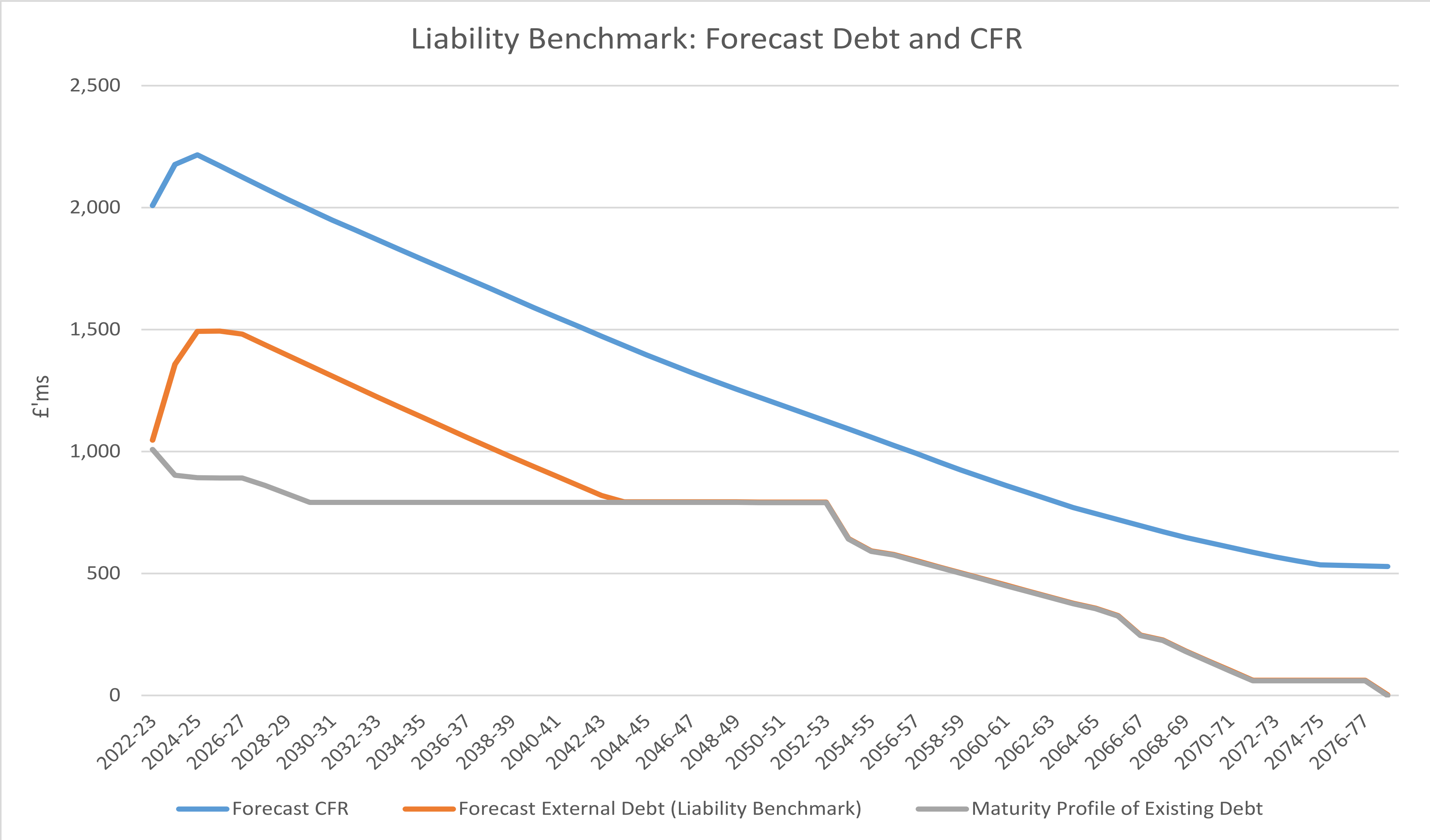
(b) Risk Management

19.2 CIPFA’s Prudential and Treasury Management Codes provide the risk management framework within which the treasury management activities of the Council operate. The Strategy should be the Council’s approach to this framework.

(c) Legal Considerations

19.3 None.

Appendix A - Prudential and Treasury Indicators for approval



Please note last years approved figures are shown in brackets.

Treasury Management Indicators	2023-24		2024-25		2025-26
	%		%		%
Estimated Financing Costs to Net Revenue Stream[5]	5.49		5.37		5.34
Estimated Net Income from Commercial and Service Investments to Net Revenue Stream	10.8		10.6		10.4
	£m		£m		£m
Authorised Limit - external debt					
Borrowing	1,825.1	(1,816.1)	1,811.9	(1,816.1)	1,811.9
Other long-term liabilities	190.0	(190.0)	190.0	(190.0)	190.0
TOTAL	2,015.1	(2,006.1)	2,001.9	(2,006.1)	2,001.9
Operational Boundary - external debt					
Borrowing	1,620.5	(1,698.5)	1,726.3	(1,724.0)	1,728.1
Other long-term liabilities	190.0	(190.0)	190.0	(190.0)	190.0
TOTAL	1,810.5	(1,888.5)	1,916.3	(1,914.0)	1,918.1
Estimated external debt	1,465.5	(1,572.0)	1,611.0	(1,606.0)	1,613.3
Upper limit for total principal sums invested for over 364 days	0	(0)	0	(0)	0
Estimated Capital Expenditure					
Non - HRA	377.4	(223.2)	155.7	(51.3)	22.5
HRA	49.0	(31.9)	43.7	(14.6)	11.6
TOTAL	426.4	(255.1)	199.4	(65.9)	34.1
Estimated Capital Financing Requirement (as at 31 March)					
Non – HRA	1854,7	(1,895.8)	1893.7	(1,898.6)	1845.4
HRA	321.8	(321.8)	322.5	(322.6)	323.9
TOTAL	2,176.5	(2,220.6)	2,216.2	(2,221.2)	2,169.3

Maturity structure of borrowing during 2023-24	Upper Limit		Lower limit	

[5] Note that for 2024-25 onward these are based on estimated net revenue budgets.

under 12 months 12 months and within 24 months 24 months and within 5 years 5 years and within 10 years 10 years and above	70% 60% 40% 50% 80%	(70%) (70%) (60%) (60%) (90%)	0% 0% 0% 0% 30%	(0%) (0%) (0%) (0%) (30%)
Has the Authority adopted the CIPFA Treasury Management Code?				Yes

The status of the indicators will be included in Treasury Management reporting during 2023/24. They will also be included in the Council's Capital Budget monitoring reports during 2023/24.

Definitions and Purpose of the Treasury Management Indicators noted above (Indicators are as recommended by the CIPFA Prudential Code last revised in 2017)

Estimated Financing Costs to Net Revenue Stream

The authority will set for the forthcoming year and the following financial years an estimate of financing costs to net revenue stream. The indicator recognises that ultimately all debts of a local authority fall on the taxpayer, and that therefore when considering affordability, it is important to review the scale of financing costs to net revenue.

Estimated Net Income from Commercial and Service Investments to Net Revenue Stream

The authority will set for the forthcoming year and the following financial years an estimate of new income from commercial and service investments to net revenue stream. The indicator is intended to show the financial exposure of the authority to the loss of income, and therefore the proportionality of commercial and service investment income to the authority's overall budget.

Estimated Capital Expenditure

The authority sets a capital budget for each financial year, which includes an estimate of the capital expenditure which might be incurred. The figures here also include changes to other long-term liabilities.

Estimates Capital Financing Requirement

The capital financing requirement reflects the authority's underlying need to finance capital expenditure and is based on all capital expenditure including that incurred in previous years.

Authorised Limit - external debt

The local authority will set for the forthcoming financial year and the following two financial years an authorised limit for its total external debt, excluding investments, separately identifying borrowing from other long-term liabilities. Other long-term liabilities include PFI's, service concessions and finance leases. Due to the introduction of IFRS16 (Leasing) on the 1st of April 2022, more of the Council's lessee leases will be classed as finance leases and will become other long-term liabilities, therefore the value will increase from previous years.

Work is underway to determine the value of this change in accounting standards, but £20.0m has been added to the indicator at this stage and will be reviewed once this work is complete. This prudential indicator is referred to as the Authorised Limit.

Operational Boundary - external debt

The local authority will also set for the forthcoming financial year and the following two financial years an operational boundary for its total external debt, excluding investments, separately identifying borrowing from other long-term liabilities. This prudential indicator is referred to as the Operational Boundary.

Both the Authorised Limit and the Operational Boundary need to be consistent with the authority's plans for capital expenditure and financing; and with its treasury management policy statement and practices. The Operational Boundary should be based on the authority's estimate of most likely, i.e. prudent, but not worst-case scenario. Risk analysis and risk management strategies should be considered.

The Operational Boundary should equate to the maximum level of external debt projected by this estimate. Thus, the Operational Boundary links directly to the Authority's plans for capital expenditure; its estimates of capital financing requirement; and its estimate of cash flow requirements for the year for all purposes. The Operational Boundary is a key management tool for in-year monitoring.

It will probably not be significant if the Operational Boundary is breached temporarily on occasions due to variations in cash flow. However, a sustained or regular trend above the Operational Boundary would be significant and should lead to further investigation and action as appropriate. Thus, both the Operational Boundary and the Authorised Limit will be based on the authority's plans. The authority will need to assure itself that these plans are affordable and prudent. The Authorised Limit will in addition need to provide headroom over and above the Operational Boundary enough for example for unusual cash movements.

Estimated external debt

After the year end, the closing balance for actual gross borrowing plus (separately), other long-term liabilities are obtained directly from the local authority's Balance Sheet.

The prudential indicator for Estimated External Debt considers a single point in time and hence is only directly comparable to the Authorised Limit and Operational Boundary at that point in time. Actual external debt during the year can be compared.

Upper limit for total principal sums invested for over 364 days

The authority will set an upper limit for each forward financial year period for the maturing of investments made for a period longer than 364 days. This indicator is referred to as the prudential limit for Principal Sums Invested for periods longer than 364 days.

The purpose of this indicator is so the authority can contain its exposure to the possibility of loss that might arise as a result of it having to seek early repayment or redemption of principal sums invested.

Maturity structure of new borrowing

The authority will set for the forthcoming financial year both upper and lower limits with respect to the maturity structure of its borrowing. These indicators are referred to as the Upper and Lower limits respectively for the Maturity Structure of Borrowing.

Liability Benchmark

The liability benchmark is a projection of the amount of loan debt outstanding that the authority needs each year into the future to fund its existing debt liabilities, planned prudential borrowing and other cash flows. The benchmark shows the gap between the authority's outstanding loans at future points in time and the authority's need to for borrowing (the benchmark). It can be used to identify the debt maturities needed for new borrowing in order to match to future liabilities.

Local Prudential Indicators

The Council has not yet introduced Local Prudential Indicators to reflect local circumstances but will review on a regular basis the need for these in the future.

Appendix B - Minimum Revenue Provision Strategy

The Council implemented the new Minimum Revenue Provision (MRP) guidance in 2011/12 and has assessed its MRP for 2023/24 in accordance with the main recommendations contained within the guidance issued by the Secretary of State under section 21(1A) of the Local Government Act 2003.
The Council is required to make provision for repayment of an element of the accumulated General Fund capital spend each year through a revenue charge (the Minimum Revenue Provision - MRP).
MHCLG Regulations require full Council to approve an MRP Statement, in advance of each year. If the Council wishes to amend its policy during the year this would need to be approved by full Council. A variety of options are available to councils to replace the previous Regulations, so long as there is a prudent provision. The options are:

- ***Option 1:*** Regulatory Method – can only be applied to capital expenditure incurred prior to April 2008 or Supported Capital Expenditure. This is calculated as 4% of the non-housing CFR at the end of the preceding financial year, less some transitional factors relating to the movement to the new Prudential Code in 2003.

- ***Option 2:*** CFR Method – a provision equal to 4% of the non-housing CFR at the end of the preceding financial year.

- ***Option 3:*** Asset Life Method – MRP is calculated based on the life of the asset, on either an equal instalment or an annuity basis.

- ***Option 4:*** Depreciation Method – MRP is calculated in accordance with the depreciation accounting required for the asset.

Options 1 and 2 may be used only for supported expenditure, which is capital expenditure for which the Council has been notified by Government that the costs of that expenditure will be considered in the calculation of Government funding due to the Council.

It is important to note that the Council can deviate from these options provided that the approach taken ensures that there is a prudent provision. The Council has historically followed option 1 for supported expenditure based on the level of support provided by Government through Revenue Support Grant (RSG).

The assets created or acquired under Supported Capital Expenditure predominantly had long asset lives of c. 50 years, such as land or buildings, and an MRP of 4% suggests a significantly shorter asset life. As the level of notional RSG the Council receives has reduced in recent years, it was considered prudent to review the approach to MRP on supported borrowing to reflect the Government support received.

It was therefore agreed that from 2017/18 a provision of 2% of the non-housing CFR as at the end of the preceding financial year is to be made. This is in line with many other local authorities who have reviewed the basis for their MRP and have applied similarly revised policies.

It is the Council's policy that MRP relating to an asset will start to be incurred in the year after the capital expenditure on the asset is incurred or, in the case of new assets, in the year following the asset coming into use, in accordance with MHCLG's guidance.

The Council recognises that there are different categories of capital expenditure, for which it will incur MRP as follows:

- For non HRA Supported Capital Expenditure: MRP policy will be charged at a rate of 2% on a similar basis to option 1 of the guidance (the regulatory method) but at a lower rate, better reflecting the asset lives of the assets funded through Supported Borrowing.

- For non HRA unsupported capital expenditure incurred the MRP policy will be:
  - Asset Life Method – MRP will be based on a straight-line basis or annuity method so linking the MRP to the future flow of benefits from the asset, dependant on the nature of the capital expenditure, in accordance with option 3 of the guidance.

  - If the expenditure is capital by virtue of a Ministerial direction, has been capitalised under a Capitalisation Directive, or does not create a council asset, MRP will be provided in accordance with option 3 of the guidance with asset lives calculated as per the table below:

Expenditure type	**Maximum period over which MRP to be made**
Expenditure capitalised by virtue of a direction under s16 (2) (b).	20 years.
Regulation 25(1) (a). Expenditure on computer programs.	Same period as for computer hardware.
Regulation 25(1) (b). Loans and grants towards capital expenditure by third parties.	The estimated life of the assets in relation to which the third-party expenditure is incurred.
Regulation 25(1) (c). Repayment of grants and loans for capital expenditure.	25 years or the period of the loan if longer.
Regulation 25(1) (d). Acquisition of share or loan capital.	20 years, or the estimated life of the asset acquired.
Regulation 25(1) (e). Expenditure on works to assets not owned by the authority.	The estimated life of the assets.
Regulation 25(1) (ea). Expenditure on assets for use by others.	The estimated life of the assets.
Regulation 25(1) (f). Payment of levy on Large Scale Voluntary Transfers (LSVTs) of dwellings.	25 years.

- For PFI service concessions and some lessee interests: Following the move to International Accounting Standards arrangements under private finance initiatives (PFIs) service concessions and some lessee interests (including embedded leases) are accounted for on the Council's Balance Sheet, and with the introduction of IFRS16 (Leasing) from the 1st of April 2022 more lessee leases will be classified in a similar way. Where this occurs, a part of the contract charge or rent payable will be taken to reduce the Balance Sheet liability rather than being charged as revenue expenditure. The MRP element of these schemes will be the amount of contract charge or rental payment charged against the Balance Sheet liability. This approach will produce an MRP charge comparable to that under option 3 in that it will run over the life of the lease or PFI scheme.

In some exceptional cases, the Council will deviate from the policy laid out above provided such exceptions remain prudent. Any exceptions are listed below:

- Where capital expenditure is incurred through providing loans to organisations, and where those loans are indemnified or have financial guarantees protecting against loss from a third party of high credit quality, no MRP will be charged in relation to the capital expenditure. Similarly, loans given by the Council where any losses incurred on the investment will impact solely on a third party, such as those provided under the City Deal arrangement with the HCA, will not require an MRP charge.

Appendix C - Treasury Management Policy Statement

1. This organisation defines its treasury management activities as:
   The management of the organisation's investments and 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. This organisation regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation, and any financial instruments entered to manage these risks.

3. This organisation acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

The Council will invest its monies prudently, considering security first, liquidity second, and yield last, carefully considering its investment counterparties. It will similarly borrow monies prudently and consistent with the Council's service objectives.

Appendix D =- Treasury Management Scheme of Delegation

i **Full Council**

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

ii **Responsible body – Audit Committee**

- 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

iii **Body with responsibility for scrutiny** - Resource and Governance Scrutiny Committee

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

iv **Deputy Chief Executive and City Treasurer**

- delivery of the function

Appendix E

The Treasury Management role of the Section 151 Officer
The S151 (responsible) Officer

- recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance
- submitting regular treasury management policy reports
- submitting budgets and budget variations
- receiving and reviewing management information reports
- reviewing the performance of the treasury management function
- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function
- ensuring the adequacy of internal audit, and liaising with external audit
- recommending the appointment of external service providers

The points noted above reflect the specific responsibilities of the S151 Officer prior to the 2017 CIPFA Treasury Management Code revisions. The CIPFA Prudential Code revision which followed the MHCLG revised guidance on local government investments represents a major extension of the functions of the S151 Officer role, especially in respect of non-financial investments which CIPFA define as being part of treasury management.
The additional functions of the S151 Officer role are:

- preparation of a capital strategy with a long-term timeframe to include capital expenditure, capital financing, non-financial investments and treasury management
- 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 authority
- ensuring that the authority has appropriate legal powers to undertake expenditure on non-financial assets and their financing
- ensuring the proportionality of all investments so that the authority 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 an authority
- ensuring that the authority 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:
    - Risk management including investment and risk management criteria for any material non-treasury investment portfolios;
    - Performance measurement and management including methodology and criteria for assessing the performance and success of non-treasury investments;
    - Decision making, governance and organisation 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 including where and how often monitoring reports are taken;
- Training and qualifications including how the relevant knowledge and skills in relation to non-treasury investments will be arranged.

Appendix F

Economic Background January 2023 – Link Asset Services

This section has been prepared by the Council's Treasury Advisors, Link Asset Services, for the Treasury Management Strategy Statement 2023/24.

Against a backdrop of stubborn inflationary pressures, the easing of Covid restrictions in most developed economies, the Russian invasion of Ukraine, and a range of different UK Government policies, it is no surprise that UK interest rates have been volatile right across the curve, from Bank Rate through to 50-year gilt yields, for all of 2022.
Market commentators' misplaced optimism around inflation has been the root cause of the rout in the bond markets with, for example, UK, EZ and US 10-year yields all rising by over 200bps since the turn of the year. The table below provides a snapshot of the conundrum facing central banks: inflation is elevated but labour markets are extra-ordinarily tight, making it an issue of fine judgment as to how far monetary policy needs to tighten.

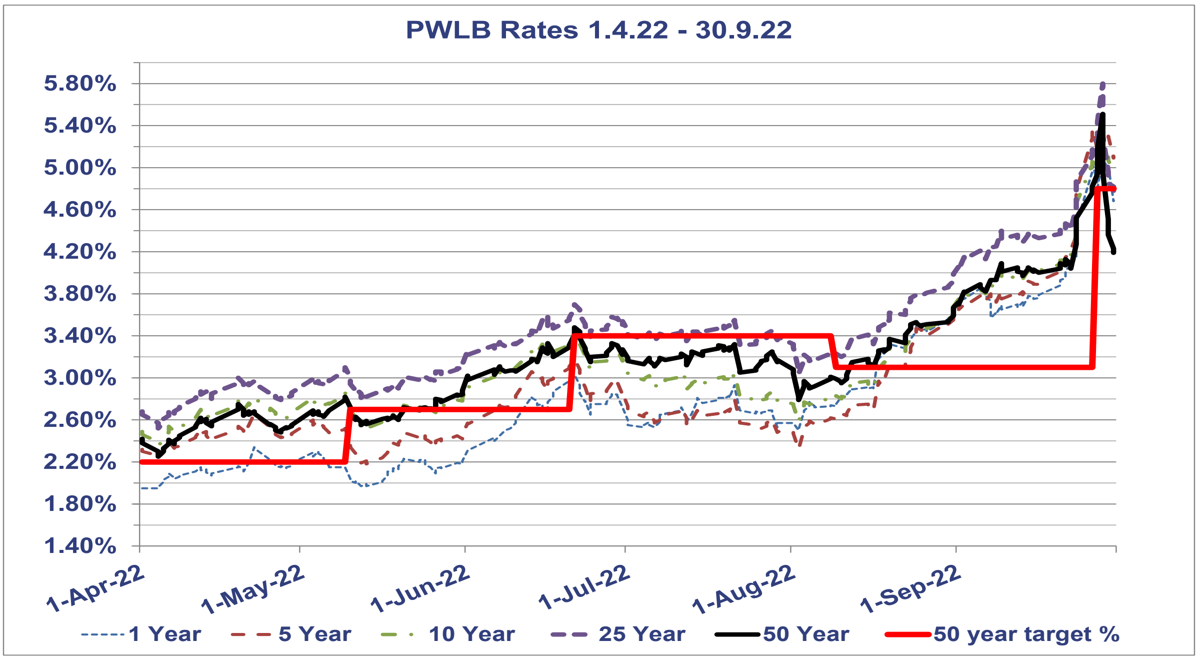
	UK	**Eurozone**	**US**
Bank Rate	3.5%	2.0%	4.25%-4.50%
GDP	-0.2%q/q Q3 (2.4%y/y)	+0.2%q/q Q3 (2.1%y/y)	2.6% Q3 Annualised
Inflation	10.7%y/y (Nov)	10.1%y/y (Nov)	7.1%y/y (Nov)
Unemployment Rate	3.7% (Oct)	6.5% (Oct)	3.7% (Nov)

Q2 of 2022 saw UK GDP revised upwards to +0.2% q/q, but this was quickly reversed in the third quarter, albeit some of the fall in GDP can be placed at the foot of the extra Bank Holiday in the wake of the Queen's passing. Nevertheless, CPI inflation has picked up to what should be a peak reading of 11.1% in October, although with further increases in the gas and electricity price caps pencilled in for April 2023, and the cap potentially rising from an average of £2,500 to £3,000 per household, there is still a possibility that inflation will spike higher again before dropping back slowly through 2023.
The UK unemployment rate fell to a 48-year low of 3.6%, and this despite a net migration increase of c500k. The fact is that with many economic participants registered as long-term sick, the UK labour force actually shrunk by c500k in the year to June. Without an increase in the labour force participation rate, it is hard to see how the UK economy will be able to grow its way to prosperity, and with average wage increases running at over 6% the MPC will be concerned that wage inflation will prove just as sticky as major supply-side shocks to food and energy that have endured since Russia's invasion of Ukraine on 22nd February 2022.
Throughout Q3 Bank Rate increased, finishing the quarter at 2.25% (an increase of 1%). Q4 has seen rates rise to 3.5% in December and the market expects Bank Rate to hit 4.5% by May 2023.
Following a Conservative Party leadership contest, Liz Truss became Prime Minister for a tumultuous seven weeks that ran through September and October. Put simply, the markets did not like the unfunded tax-cutting and heavy spending policies put forward by her Chancellor, Kwasi Kwarteng, and their reign lasted barely seven weeks before being replaced by Prime Minister Rishi Sunak and Chancellor Jeremy Hunt. Their Autumn Statement of 17th November gave rise to a net £55bn fiscal tightening, although much of the "heavy lifting" has been left for the next Parliament to deliver. However, the markets liked what they heard, and UK gilt yields have almost completely reversed the increases seen under the previous tenants of No10/11 Downing Street.

Globally, though, all the major economies are expected to struggle in the near term. The fall below 50 in the composite Purchasing Manager Indices for the UK, US, EZ and China all point to at least one, if not more, quarters of GDP contraction. In November, the MPC projected eight quarters of negative growth for the UK lasting throughout 2023 and 2024, but with Bank Rate set to peak at lower levels than previously priced in by the markets and the fiscal tightening deferred to some extent, it is not clear that things will be as bad as first anticipated by the Bank.

The £ has strengthened of late, recovering from a record low of $1.035, on the Monday following the Truss government's "fiscal event", to $1.22. Notwithstanding the £'s better run of late, 2023 is likely to see a housing correction of some magnitude as fixed-rate mortgages have moved above 5% and affordability has been squeezed despite proposed Stamp Duty cuts remaining in place.

In the table below, the rise in gilt yields, and therein PWLB rates, through the first half of 2022/23 is clear to see.



However, the peak in rates on 28th September as illustrated in the table covering April to September 2022 below, has been followed by the whole curve shifting lower. PWLB rates at the front end of the curve are generally over 1% lower now whilst the 50 years is over 1.75% lower.

	1 Year	5 Year	10 Year	25 Year	50 Year
Low	1.95%	2.18%	2.36%	2.52%	2.25%
Date	01/04/2022	13/05/2022	04/04/2022	04/04/2022	04/04/2022
High	5.11%	5.44%	5.35%	5.80%	5.51%
Date	28/09/2022	28/09/2022	28/09/2022	28/09/2022	28/09/2022
Average	2.81%	2.92%	3.13%	3.44%	3.17%
Spread	3.16%	3.26%	2.99%	3.28%	3.26%

After a shaky start to the year, the S&P 500 and FTSE 100 have climbed in recent weeks, albeit the former is still 17% down and the FTSE 2% up. The German DAX is 9% down for the year.

CENTRAL BANK CONCERNS – DECEMBER 2022

In December, the Fed decided to push up US rates by 0.5% to a range of 4.25% to 4.5%, whilst the MPC followed by raising Bank Rate from 3% to 3.5%, in line with market expectations. EZ rates have also increased to 2% with further tightening in the pipeline.

Having said that, the sentiment expressed in the press conferences in the US and the UK were very different. In the US, Fed Chair, Jerome Powell, stated that rates will be elevated and stay higher for longer than markets had expected. Governor Bailey, here in the UK, said the opposite and explained that the two economies are positioned very differently so you should not, therefore, expect the same policy or messaging.

Regarding UK market expectations, although they now expect Bank Rate to peak within a lower range of 4.5% - 4.75%, caution is advised as the Bank of England Quarterly Monetary Policy Reports have carried a dovish message over the course of the last year, only for the Bank to have to play catch-up as the inflationary data has proven stronger than expected.

In addition, the Bank's central message that GDP will fall for eight quarters starting with Q3 2022 may prove to be a little pessimistic. Will the £160bn excess savings accumulated by households through the Covid lockdowns provide a spending buffer for the economy – at least to a degree? Ultimately, however, it will not only be inflation data but also employment data that will mostly impact the decision-making process, although any softening in the interest rate outlook in the US may also have an effect (just as, conversely, greater tightening may also).

<u>Appendix G</u>

Interest Rate Forecasts 2022 – 2025

PWLB forecasts shown below have taken into account the 20 basis point certainty rate reduction effective as of the 1st November 2012.

	MAR-23	**Jun-23**	**Sep-23**	**Dec-23**	**Mar-24**	**Dec-24**	**Mar-25**	**Dec-2**
Bank Rate	4.25	4.50	4.50	4.50	4.00	3.25	3.00	2.50
5yr PWLB	4.20	4.20	4.10	4.00	3.90	3.50	3.40	3.10
10yr PWLB	4.40	4.40	4.30	4.10	4.00	3.60	3.50	3.30
25yr PWLB	4.60	4.60	4.50	4.00	4.20	3.90	3.70	3.50
50yr PWLB	4.30	4.30	4.20	4.10	3.90	3.60	3.50	3.20

The Link forecasts are as at 19.12.22.

Appendix H

Glossary of Terms

Authorised Limit - This Prudential Indicator represents the limit beyond which borrowing is prohibited and needs to be set and revised by Members. It reflects the level of borrowing which, while not desired, could be afforded in the short term, but is not sustainable. It is the expected maximum borrowing need, with some headroom for unexpected movements.

Bank Rate - the rate at which the Bank of England offers loans to the wholesale banks, thereby controlling general interest rates in the economy.

Counterparty - one of the opposing parties involved in a borrowing or investment transaction.

Covered Bonds - Debt instruments secured by assets such as mortgage loans. These loans remain on the issuer's balance sheet and investors have a preferential claim in the event of the issuing institution defaulting.

Credit Rating - A qualified assessment and formal evaluation of an institution's (bank or building society) credit history and capability of repaying obligations. It measures the probability of the borrower defaulting on its financial obligations, and its ability to repay these fully and on time.

Discount - Where the prevailing interest rate is higher than the fixed rate of a long-term loan, which is being repaid early, the lender can refund the borrower a discount, the calculation being based on the difference between the two interest rates over the remaining years of the loan, discounted back to present value. The lender can offer the discount, as their investment will now earn more than when the original loan was taken out.

Fixed Rate Funding - A fixed rate of interest throughout the time of the loan. The rate is fixed at the start of the loan and therefore does not affect the volatility of the portfolio, until the debt matures and requires replacing at the interest rates relevant at that time.

Gilts - The loan instruments by which the Government borrows. Interest rates will reflect the level of demand shown by investors when the Government auctions Gilts.

High/Low Coupon - High/Low interest rate

LIBID (London Interbank Bid Rate) - This is an average rate, calculated from the rates at which individual major banks in London are willing to borrow from other banks for a time period. For example, 6-month LIBID is the average rate at which banks are willing to pay to borrow for 6 months.

LIBOR (London Interbank Offer Rate) - This is an average rate, calculated from the rates which major banks in London estimate they would be charged if they borrowed from other banks for a time period. For example, 6-month LIBOR is the average rate which banks believe they will be charged for borrowing for 6 months.

Liquidity - The ability of an asset to be converted into cash quickly and without any price discount. The more liquid a business is, the better able it is to meet short-term financial obligations.

LOBO (Lender Option Borrower Option) - This is a type of loan where, at various periods known as call dates, the lender has the option to alter the interest rate on the loan. Should the lender exercise this option, the borrower has a corresponding option to repay the loan in full without penalty.

Market -The private sector institutions - Banks, Building Societies etc.

Maturity Profile/Structure - an illustration of when debts are due to mature, and either must be renewed or money found to pay off the debt. A high concentration in one year will make the Council vulnerable to current interest rates in that year.

Monetary Policy Committee - the independent body that determines Bank Rate.

Money Market Funds - Investment instruments that invest in a variety of institutions, therefore diversifying the investment risk.

Operational Boundary – This Prudential Indicator is based on the probable external debt during the year. It is not a limit and actual borrowing could vary around this boundary for short times during the year. It should act as an indicator to ensure the Authorised Limit is not breached.

Premium - Where the prevailing current interest rate is lower than the fixed rate of a long-term loan, which is being repaid early, the lender can charge the borrower a premium, the calculation being based on the difference between the two interest rates over the remaining years of the loan, discounted back to present value. The lender may charge the premium, as their investment will now earn less than when the original loan was taken out.

Prudential Code - The Local Government Act 2003 requires the Council to 'have regard to Prudential Code and to set Prudential Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable.

PWLB - Public Works Loan Board. Part of the Government's Debt Management Office, which provides loans to public bodies at rates reflecting those at which the Government can sell Gilts.

SONIA – Sterling Overnight Index Average (SONIA) is an interest rate benchmark which is based on actual transactions and reflects the average of the interest rates that banks pay to borrow sterling overnight from other financial institutions and other institutional investors.

Specified Investments - Sterling investments of not more than one-year maturity. These are considered low risk assets, where the possibility of loss of principal or investment income is very low.

Non-specified investments - Investments not in the above, specified category, e.g., foreign currency, exceeding one year or outside our minimum credit rating criteria.

Treasury Bills - These are marketable securities issued by the UK Government and as such counterparty and liquidity risk is very low.

Variable Rate Funding - The rate of interest either continually moves reflecting interest rates of the day; or can be tied to specific dates during the loan period. Rates may be updated on a monthly, quarterly or annual basis.

Volatility - The degree to which the debt portfolio is affected by current interest rate movements. The more debt maturing within the coming year and needing replacement, and the more debt subject to variable interest rates, the greater the volatility.

Yield Curve - A graph of the relationship of interest rates to the length of the loan. A normal yield curve will show interest rates relatively low for short-term loans compared to long-term loans. An inverted Yield Curve is the opposite of this.

Appendix I

Treasury Management Implications of HRA Reform

As discussed in Section 5 of the report, the reform of the HRA finance system has consequences for the treasury management of the Council. As part of the reform, the HRA's debt portfolio needs to be separately identifiable to that of the General Fund, and the HRA will hold some autonomy over the management of its debt portfolio. However, in order to ensure that the treasury management function of the Council remains effective and provides value for money, and given that the Section 151 officer for both the General Fund and the HRA is the Deputy Chief Executive and City Treasurer, the HRA's treasury portfolio must be run in the context of the overall Council portfolio.

This appendix seeks to explain how the debt portfolio of the Council has been split between the General Fund and the HRA, and how the HRA treasury position will be managed going forward.

The Portfolio Split

One of the principles behind the reform of HRA finance was to provide some level of treasury autonomy for the HRA, separating its debt from the Council's so that its treasury position could be managed separately. To achieve this, the debt portfolio was to be split at the point that the debt settlement was made.

On the 28 March 2012, the Council received c. £294m which was to be used to reduce the debt held by the Council. The table below shows the Council's treasury portfolio before and after the settlement:

	Pre reform		Post reform
	£'000		*£'000*
PWLB	199,966		0
Market	549,640		480,215
Stock	8,159		8,159
Gross Debt	**757,765**		**488,374**
Deposits	-17,954		-42,839
Net Debt	**739,811**		**445,535**

At this point, the debt was to be split according to the relative capital financing requirements (CFRs) of both the General Fund and the HRA. The cash remainder of the settlement could not be used to redeem further market debt so, to ensure that the HRA CFR fell by the full level of the settlement, a notional transaction took place. An amount of debt equivalent to the cash remainder was transferred from the HRA to the General Fund, alongside the cash. This had a neutral effect on the General Fund's net debt.

The table below shows the CFRs before and after the debt settlement, with the HRA CFR falling by the settlement:

CFRs	Pre reform		Post reform	% of total
	£'000		*£'000*	
General Fund	675,454		675,454	84.47%
HRA	418,463		124,187	15.53%
Total	**1,093,917**		**799,641**	**100.00%**
		Of which financed:	*488,374*	
		Of which unfinanced:	*311,267*	

As can be seen from the tables below, the debt was to split in a ratio of 84.47:15.53 between the General Fund and the HRA, including the unfinanced CFR element. This is the level of internal borrowing undertaken in lieu of external borrowing, through the use of cash balances to fund expenditure rather than external borrowing. It was decided, for administrative reasons, that all of the Council's remaining stock debt should be held by the General Fund, which increased the relative level of unfinanced CFR held by the HRA.

The final split of the debt portfolio is shown in the table below:

	General Fund	HRA	Total
	£'000	*£'000*	*£'000*
Market	405,636	74,579	480,215
% of total market	*84.47%*	*15.53%*	
Stock	8,159	0	8,159
% of stock	*100.00%*	*0.00%*	
Total Loans	**413,795**	**74,579**	**488,374**
% of total loans	*84.73%*	*15.27%*	
Unfinanced CFR	261,659	49,608	311,267
% of unfinanced CFR	*84.06%*	*15.94%*	
Total CFR	**675,454**	**124,187**	**799,641**
% of total CFR	*84.47%*	*15.53%*	

Future HRA borrowing

Following the split of the portfolio, the HRA can make borrowing decisions according to the needs of their business plan, provided those decisions are aligned with their treasury strategy and are agreed by the Section 151 officer. The amounts and maturity periods of any future loans will be determined by the HRA, in conjunction with the Treasury Management team and the Deputy Chief Executive and City Treasurer. Any future borrowing made by the Council will be for either the General Fund or the HRA and not for the Council in general.

Use of Temporary Cash Balances and Temporary Borrowing

Although the HRA’s treasury position is now independent of the General Fund, both are managed in the name of the Council as a whole. As such, the day to day treasury position of the Council, whilst having regard to the impact on the HRA and the General Fund, will be run on a Council basis – this simplifies the risk management of the treasury position, and should help to ensure that the treasury function is providing value for money.

To achieve this, the General Fund will deposit and temporarily borrow externally, but the HRA will only be able to deposit with the General Fund and, should it be required, will only be able to access temporary borrowing through the General Fund. In order to ensure that this is fair, interest rates will be applied to any such internal transfers, as summarised below:

- If the General Fund has temporary investments, HRA investments with the General Fund will earn – ***average portfolio temporary investment rate***

- If the General Fund does not have temporary investments, HRA investments with the General Fund will earn – ***SONIA***

- If the General Fund has temporary borrowing, HRA temporary borrowing from the General Fund will be charged – ***average portfolio temporary borrowing rate***

- If the General fund does not have temporary borrowing, HRA temporary borrowing from the General Fund will be charged – ***SONIA***

The Bank of England and the Financial Conduct Authority (FCA) are committed to phasing out LIBOR before the end of 2021. Therefore, the market rates used are SONIA which the Council will use for benchmarking investments and temporary borrowing.

Future Reporting

The intention is to continue to report to Members the overall treasury position of the Council, including both the General Fund and the HRA. Separate reports will be provided on the General Fund and the HRA, when required.