AUDIT COMMITTEE
4 NOVEMBER 2024

MID YEAR PRUDENTIAL INDICATORS AND TREASURY MANAGEMENT MONITORING REPORT 2024/25

SUMMARY REPORT

Purpose of the Report

1. This report seeks approval of the revised Treasury Management Strategy, Prudential Indicators and provides a mid–yearly review of the Council's borrowing and investment activities. Audit Committee are requested to forward the revised Strategy and indicators to Cabinet and Council for their approval and note any changes to the MTFP with regard to the Treasury Management Budget (Financing Costs).

Summary

2. The mandatory Prudential Code, which governs Council's borrowing, requires Council approval of controls, called Prudential Indicators, relating to capital spending and borrowing. Prudential Indicators are set in three statutory annual reports, a forward looking annual treasury management strategy, a backward looking annual treasury management report and this mid-year update. The mid-year update follows Council's approval in February 2024 of the 2024/25 Prudential Indicators and Treasury Management Strategy.

3. The key objectives of the three annual reports are:

    (a) to ensure the governance of the large amounts of public money under the Council's Treasury Management activities:

    (i) Complies with legislation.
    (ii) Meets high standards set out in codes of practice

    (b) To ensure that borrowing is affordable,
    (c) To report performance of the key activities of borrowing and investments.

4. The key proposed revisions to Prudential Indicators relate to the Operational Boundary will reduce to £179.323m and the Authorised Limit to £259.628m which will allow for any additional cashflow requirement.

Recommendations

5. It is recommended that:

    (a) The revised prudential indicators and limits within the report in Tables 1 to 6, 8, 10 and 12 to 17 are examined.

(b) The Treasury Management Budget (Financing Costs) projected outturn shown in Table 11 is noted.

(c) That this report is forwarded to Council via Cabinet with comments from this committee, in order for the updated prudential indicators to be approved.

Reasons

6. The recommendations are supported by the following reasons :-

(a) In order to comply with the Prudential Code for Capital Finance in Local Authorities;

(b) To inform Members of the performance of the Treasury Management function;

(c) To comply with the Local Government Act 2003;

(d) To enable further improvements to be made in the Council's Treasury Management function.

Elizabeth Davison
Executive Director - Resources and Governance

Background Papers

(i) Capital Medium Term Financial Plan 2024/25
(ii) Prudential Indicators & Treasury Management Strategy 2024/25
(iii) Accounting records
(iv) The Prudential Code for Capital Finance in Local Authorities

Judith Murray: Extension 5204

Council Plan	The Council's treasury management contributes to all priorities outlined within the Council Plan.
Addressing inequalities	This report is providing an update on prudential indicators and the monitoring of the Council's treasury management. There is therefore no impact as a result of this report.
Tackling Climate Change	This report is providing an update on prudential indicators and the monitoring of the Council's treasury management. There is therefore no impact as a result of this report.
Efficient and effective use of resources	This report contains updated information regarding the Council's treasury management position
Health and Wellbeing	This report is providing an update on prudential indicators and the monitoring of treasury management therefore there is no impact as a result of this report.
S17 Crime and Disorder	This report has no implications for crime and disorder
Wards Affected	No specific impact on an individual area as a result of this report
Groups Affected	No specific impact on an individual area as a result of this report
Budget and Policy Framework	This report does not recommend a change to the Council's budget or policy framework
Key Decision	This is not a key decision
Urgent Decision	This is not an urgent decision
Impact on Looked After Children and Care Leavers	This report has no impact on Looked After Children or Care Leavers

MAIN REPORT

Information and Analysis

7. This mid-year review report meets the regulatory framework requirement of treasury management. It also incorporates the needs of the Prudential Code to ensure monitoring of the capital expenditure plans and the Council's prudential indicators (PIs). The Treasury Strategy and the PIs were previously reported to Council on 15 February 2024.

8. This report concentrates on the revised positions for 2024/25. Future year's indicators will be revised when the impact of the MTFP 2025/26 onwards is known.

9. A summary of the revised headline indicators for 2024/25 is presented in Table 1 below. More detailed explanations of each indicator and any proposed changes are contained in the report. The revised indicators reflect the movement in the Capital MTFP since its approval in February 2024 and the means by which it is financed.

Table 1 Headline Indicators

	2024/25 Original Estimate	2024/25 Revised Estimate
	£m	£m
Capital Expenditure (Tables 2 and 3)	70.088	69.646
Capital Financing Requirement (Table 4)	260.106	247.265
Operational Boundary for External Debt (Table 4)	183.973	179.323
Authorised Limit for External Debt (Table 6)	273.111	259.628
Ratio of Financing Costs to net revenue stream- General Fund (Table 14)	4.16%	4.10%
Ratio of Financing Costs to net revenue stream- Housing Revenue Account (HRA)(Table 14)	12.42%	12.49%

10. The capital expenditure plans and prudential indicators for capital expenditure are set out initially, as these provide the framework for the subsequent treasury management activity. The actual treasury management activity follows the capital framework and the position against the treasury management indicators is shown at the end.

11. The purpose of the report supports the objective in the revised CIPFA Code of Practice on Treasury Management and the Ministry of Housing, Communities and Local Government Investment Guidance which state that Members receive and adequately scrutinise the treasury service.

12. The underlying economic environment remains difficult for Councils. It is essential that the Council continues to monitor its cashflow in these times of high interest rates. Borrowing rates are higher than investment returns and this background encourages the Council to continue investing over the shorter term and with high quality counterparties but also limit any borrowing to only that which is essential and for the shorter term where possible until interest rates start to fall.

Key Prudential Indicators

13. This part of the report is structured to update:

    (a) The Council's capital expenditure plans
    (b) How these plans are financed
    (c) The impact of the changes in the capital expenditure plans on the PI's and the underlying need to borrow
    (d) Compliance and limits in place for borrowing activity
    (e) Changes to the Annual Investment Strategy
    (f) The revised financing costs budget for 2024/25

Capital Expenditure PI

14. Table 2 shows the revised estimates for capital expenditure and the changes since the capital programme was agreed at the budget.

Table 2

Capital Expenditure by Service	2024/25 Original Estimate	2024/25 Revised Estimate
	£m	£m
General Fund	31.038	20.876
HRA	27.270	43.032
Total Estimated Capital Expenditure	**58.308**	**63.908**
Loans to Joint Ventures	11.780	5.738
Total	**70.088**	**69.646**

15. The changes to the 2024/25 capital expenditure estimates have been notified to Cabinet as part of the Capital Budget monitoring process (Quarterly Project Position Statement Report).

16. The current capital programme that has not already been financed now stands at £151.869m but this includes a number of schemes that will be spent over a number of years not just in 2024/25. A reduction of £82.223m has been allowed for schemes which are known will be finalised in future years, but it is likely that other schemes will also slip into future years.

Impact of Capital Expenditure Plans

Changes to the financing of the Capital Programme

17. Table 3 draws together the main strategy elements of the capital expenditure plans shown above, highlighting the original elements of the capital programme, and the expected financing arrangements of this capital expenditure. The borrowing element (Borrowing Need) increases the underlying indebtedness of the Council by way of the Capital Financing Requirement (CFR). Borrowing need is estimated to increase slightly for 2024/25 mainly

due to rising costs and additional schemes being approved. This direct borrowing need may also be supplemented by maturing debt and other treasury requirements.

Table 3

Capital Expenditure	2024/25 Original Estimate	2024/25 Revised Estimate
	£m	£m
General Fund	31.038	20.876
HRA	27.270	43.032
Loans to Joint Ventures	11.780	5.738
Total Capital expenditure	70.088	69.646
Financed By:		
Capital Receipts – Housing	0.303	0.000
Capital Receipts –General Fund	4.840	0.887
Capital grants	26.198	16.319
JV Repayments	1.799	1.000
HRA Revenue Contributions	13.455	25.007
GF Revenue Contributions	0.000	0.651
Total Financing	46.595	43.864
Borrowing Need	**23.493**	**25.782**

The Capital Financing Requirement (PI), External Debt (PI) and the Operational Boundary

18. Table 4 shows the Capital Financing Requirement (CFR), which is the underlying external need to borrow for capital purposes. It shows the expected actual debt position over the period. This is called the Operational Boundary. The increase in Borrowing Need (Table 3) is around £2.3m and currently actual borrowing for the Council is £158.411m. It is proposed to set an actual borrowing figure of £171.411m this will accommodate the additional borrowing need and any debt requirements for cash flow purposes. Other Long-term liabilities (the PFI scheme) will be added to give the revised operational boundary for 2024/25.

Prudential Indicator- External Debt/ Operational Boundary

Table 4

	2024/25 Original Estimate	2024/25 Revised Estimate
	£m	£m
Prudential Indicator- Capital Financing Requirement		
Opening CFR- Post Audit of Accounts	**241.020**	**233.973**
CFR General Fund	148.208	151.371
CFR General Fund PFI/Leasing IFRS	5.912	5.912
CFR – Housing	85.871	76.371
CFR – Loans to Joint Ventures	20.115	13.611
Total Closing CFR	**260.106**	**247.265**
Net Movement in CFR	19.086	13.292
Borrowing	176.061	171.411
Other long-Term Liabilities	5.912	5.912
Total Debt 31 March- Operational Boundary	**181.973**	**177.323**

Limits to Borrowing Activity

19. The first key control over the treasury activity is a PI to ensure that over the medium term gross borrowing should not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2024/25 and the next two financial years. As shown in **Table 5** below.

Table 5

	2024/25 Original Estimate £m	2024/25 Revised Estimate £m	2025/26 Revised Estimate £m	2026/27 Revised Estimate £m
Gross borrowing	176.061	171.411	188.411	205.411
Plus Prudential Borrowing Leases	2.000	2.000	2.000	2.000
Plus Other Long Term Liabilities	5.912	5.912	4.817	3.722
Total Gross Borrowing	**183.973**	**179.323**	**195.228**	**211.133**
CFR* (year-end position)	260.106	247.265	254.758	261.448

* includes on balance sheet PFI schemes and finance leases

20. The Executive Director - Resources and Governance reports that no difficulties are envisaged for the current and future years in complying with this PI.

21. A further PI controls the overall level of borrowing, this is the Authorised Limit which 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 desirable, could be afforded in the short term, but is not sustainable in the longer term. The Authorised Limit is currently set 5% above the Capital Financing Requirement to allow for any additional cashflow needs,

the revised figure for 2024/25 has been raised by 5% of the new CFR total. Whilst it is not expected that borrowing would be at these levels this would allow additional borrowing to take place should market conditions change suddenly and swift action was required. This is a Statutory limit determined under section 3 (1) of the Local Government Act 2003.

22. It is proposed to move the Authorised Limit in **Table 6** in line with the movement in the overall Capital Financing Requirement.

Table 6

Authorised Limit for External Debt	2024/25 Original Indicator £m	2024/25 Revised Indicator £m
Capital Financing Requirement	260.106	247.265
Additional headroom to Capital Financing Requirement	13.005	12.363
Total Authorised Limit for External Debt	**273.111**	**259.628**

Interest Rate Forecasts Provided by Link Asset Services (as at 30th September 2024)

Table 7

	Bank Rate	**PWLB rates for borrowing purposes***			
		5 year	10 year	25 year	50 year
	%	%	%	%	%
2024/25					
Dec 2024	4.50	4.50	4.60	5.00	4.80
March 2025	4.00	4.30	4.40	4.80	4.60
2024/25					
June 2025	3.50	4.10	4.30	4.70	4.50
Sept 2025	3.25	4.00	4.10	4.50	4.30
Dec 2025	3.25	3.90	4.10	4.50	4.30
March 2026	3.25	3.90	4.10	4.40	4.20
2025/26					
June 2026	3.25	3.90	4.00	4.40	4.20
Sept 2026	3.00	3.90	4.00	4.40	4.20
Dec 2026	3.00	3.90	4.00	4.30	4.10
March 2027	3.00	3.80	3.90	4.30	4.10

*PWLB rates above are for certainty rates (which are provided for those authorities that have disclosed their borrowing/capital plans to the government. Darlington Borough Council will be able to access these certainty rates which are 0.2% below PWLB's normal borrowing rates.

23. The latest Bank Rate increase was reviewed in September with no change from 5.00% being implemented. The next review will be in November with a cut to 4.75% anticipated, however, what happens for the remainder of 2024/25 and into 2025/26 will most likely depend on inflation and employment data releases as well as geo-political events.

24. The government's plans to raise public spending by around £16bn a year (0.6% GDP) have caused concerns that a big rise in taxes will be announced which could weaken GDP growth in the medium-term. However, raises in public spending tend to boost GDP by more than increases in taxes reduce it.

25. CPI inflation decreased to 1.7% in September with falls in transportation costs, furniture and household energy costs, however CPI inflation is expected to rise in the next couple of months, potentially reaching 2.9% in November before declining to around 2.0% by mid 2025.

26. The increasing uncertainties of the Middle East may also exert an upward pressure on inflation with oil prices rising in the aftermath of Iran's missile attack on Israel. China's recent outpouring of new fiscal support measures has also added to the upshift in broader commodity prices which in turn may impact on global inflation levels and thus monetary policy. The forecast is however for the bank rate to fall to 4.5% by the end of November with further cuts in 2025. In the second half of 2025 a more marked easing in inflation will prompt the Bank to speed up rate cuts eventually potentially reaching 3.0% by 2026.

Treasury Management Strategy 2024/25 and Annual Investment Strategy Update

27. The Treasury Management Strategy Statement, (TMSS), for 2024/25 was approved by Council on 15 February 2024.

28. There are no policy changes to the TMSS.

29. The details in this report update the position in the light of the updated economic position and budgetary changes already approved.

Debt Activity during 2024/25

30. The expected net borrowing need is set out in **Table 8**

Table 8

	2024/25 Original Estimate £m	**2024/25 Revised Estimate £m**
CFR (year-end position) from Table 4	254.194	241.353
Less other long term liabilities PFI and finance leases	5.912	5.912
Net adjusted CFR (net year end position)	**260.106**	**247.265**
Expected Borrowing	181.973	177.333
(Under)/ Over borrowing	**(78.135)**	**(69.932)**

31. The Council has taken on £27m of new short debt in the current year to date which will either be replaced or will be repaid using short term maturing investments and any surplus cash.

32. The amount borrowed by the Council now stands at £158.411m, this excludes any additional cashflow loans which may be required. An additional £13.000m has been included in Table 8 above for estimated cashflow loans which may be required.

33. There will still be an element of under-borrowing by the Council at the end of March 2024.

Property Funds

34. The Annual Investment Strategy highlighted the situation regarding the Lothbury Property Fund and it was confirmed in the 2023/24 Treasury Management Outturn report that unfortunately the Lothbury Property Fund was terminated in the first quarter of 2024/25 (30th May 2024).

35. The process of winding up the Lothbury Property Fund will take some time, as assets need to be sold and the distributions of funds can only be made once completed. This process is expected to be finalised by the end of March 2025, but this will depend upon how asset sales progress.

36. To date the Council has received three distributions from the sale of Lothbury assets. These have been invested in the UBS Triton Property Fund.

37. UBS Triton is a 5 star rated fund which offers returns of around 3.1% over 5 yrs, that is projected to increase to 5-8% per annum from 2025 to 2029.

38. Given these forecasts, and after extensive engagement and discussions with UBS Triton and with our advisors regarding alternative investment options, the Council have invested the funds received to date into UBS Triton. However investment decisions regarding future distributions will be made on receipt, in consideration of the best investment options and the Council's financial position at that point.

39. The latest projection is that future distributions from the Lothbury Fund will be a further £2.9m based upon the current value of their asset portfolio.

40. Maximising returns for the Council is key, so monitoring of the performance of all the property funds and other investments will continue to be a high priority.

Debt Rescheduling

41. Debt rescheduling opportunities have been very limited in the current economic climate given the consequent structure of interest rates and following the increase in the margin added to gilt yields which has impacted PWLB new borrowing rates since October 2010. No debt rescheduling has therefore been undertaken to date in the current financial year.

Annual Investment Strategy 2024/25

Investment Portfolio

42. In accordance with the Code, it is the Council's priority to ensure security of Capital and liquidity, and to obtain an appropriate level of return which is consistent with the Council's risk appetite. Successive interest rises over the past year have meant that current investment returns are much

higher than we have seen in previous years and in line with the current bank rate of 5.00%. During this period of greater returns the Council are actively investing where possible.

Treasury Management Activity from 1 April 2024 to 30 September 2024

43. Current investment position – The Council held £40.749m of investments at 30/09/2024 and this is made up of the following types of investment.

Table 9

Sector	Country	Amount
		£m
AAA Money Market Funds	Sterling Funds	13.530
Property Funds* - CCLA	UK	10.000
Hermes	UK	10.000
Lothbury	UK	2.908
UBS Triton		4.311
Total		**40.749**

* dividends are received from property funds

Short Term Cashflow Investments

44. Cash balances are invested on a daily basis to maximise the benefit of temporary surplus funds. These include investments in Money Market Funds, the Government's Debt Management Office and bank short term notice accounts. A total of 85 investments were made in the period 1 April 2024 to 30 September 2024 totalling c£148m these were for short periods of up to 180 days and earned interest of £0.501m on an average balance of £19.877m which equated to an annual average interest rate of 5.03%.

Investment returns measured against the Service Performance Indicators

45. The target for our investment returns is to better or at least match a number of external comparators, this performance indicator is also known as yield benchmarking. As can be seen from Table 10, the short term investment achievements (up to 6 months) are above market expectations.

Table 10

	Cashflow Investments %
Darlington Borough Council - Actual	**5.03%**
External Comparators	
Sterling Overnight Index Average (SONIA) – 6 months	4.96%

Treasury Management Budget

46. There are three main elements within the Treasury Management Budget:-

    (a) Longer term capital investments interest earned – a cash amount of which earns interest and represents the Councils revenue balances, unused capital receipts, reserves and provisions, this will now include Property Funds.

    (b) Cash flow interest earned – the authority has consistently had a positive cash flow. Unlike long term capital investments it does not represent any particular sum but it is the consequence of many different influences such as receipt of grants, the relationship between debtors and creditors, cashing of cheques and payments to suppliers.

    (c) Debt serving costs – this is the principal and interest costs on the Council's long term debt to finance the capital programme.

Table 11 - Changes to the Financing Costs Budget 2024/25

	£m	£m
Original Financing Costs Budget 2024/25		**3.547**
Add Increased debt costs	0.085	
Less Increased returns on Investments	(0.235)	
Less decreased returns on Property Funds	0.150	
Total adjustments		**0.000**
Revised Treasury Management Budget 2024/25		**3.547**

47. This statement concludes that the Treasury Management budget is forecast to Outturn on budget in 2024/25, this will be reflected in the current MTFP projections.

Risk Benchmarking

48. A regulatory development is the consideration and approval of security and liquidity benchmarks. Yield benchmarks are currently widely used to assess investment performance and these are shown in Table 12. Discrete security and liquidity benchmarks are also requirements of member reporting.

49. The following reports the current position against the benchmarks originally approved.

50. **Security** – The Council's maximum security risk benchmarks for the current portfolio of investments, when compared to historic default tables were set as follows;

    0.077% historic risk of default when compared to the whole portfolio

Table 12

Maximum	**Benchmark 2024/25**	**Actual May**	**Actual July**
Year 1	0.077%	0.000%	0.002%

N.B. this excludes Property Funds

51. The counterparties that we use are all high rated therefore our actual risk of default based on ratings attached to counterparties is very low.

52. The reason that there is no risk of default in May is due to the fact that all investments were in Money Market Funds which could be recalled at any time and carry no risk of default.

53. **Liquidity** – In respect of this area the Council set liquidity facilities/ benchmark to maintain

(a) Bank overdraft - £0.100M
(b) Liquid short term deposits of a least £3.000M available within a weeks notice
(c) Weighted Average Life benchmark is expected to be 0.4 years with a maximum of 1 year

54. The Group Director of Operations can report that liquidity arrangements have been adequate for the year to date as shown in Table 13

Table 13

	Benchmark 2024/25	**Actual May**	**Actual July**
Weighted Average Life	0.4 – 1 year	0.00 years	0.52 years

55. The figures are for the whole portfolio of cash flow investments deposited with Money Market funds on a call basis (i.e. can be drawn on without notice) as well as call accounts that include a certain amount of notice required to recall the funds.

Treasury Management Indicators

56. **Actual and estimates of the ratio of financing costs to net revenue stream** – This indicator identifies the trend in the cost of capital (financing costs net of interest and investment income) against the net revenue stream.

Table 14

	2024/25 Original Indicator	**2024/25 Revised Indicator**
General Fund	**4.16%**	**4.10%**
HRA	**12.42%**	**12.49%**

Treasury Management Prudential indicators

57. **Upper Limits on Variable Rate Exposure –** This indicator identifies a maximum limit for variable interest rates based upon the debt position net of investments.

58. **Upper Limits on Fixed Rate Exposure –** Similar to the previous indicator this cover a maximum limit on fixed interest rates

59. Historically for a number of years this Council has used these percentages; together they give flexibility to the treasury management strategy allowing the Council to take advantage of both fixed and variable rates in its portfolio whilst ensuring that its exposure to variable rates is limited.

Table 15

	2024/25 Original Indicator	2024/25 Revised Indicator
Limits on fixed interest rates	100%	100%
Limits on variable interest rates	40%	40%

60. **Maturity Structures of Borrowing -** These gross limits are set to reduce the Council's exposure to large fixed rate loans (those instruments which carry a fixed interest for the duration of the instrument) falling due for refinancing. The higher limits for longer periods reflect the fact that longer maturity periods give more stability to the debt portfolio.

Table 16 - **Maturity Structures of Borrowing**

	2024/25 Original indicator	2024/25 Actual to Date	2024/25 Revised Indicator
Under 12 months	40%	26%	40%
12 months to 2 years	50%	0%	50%
2 years to 5 years	60%	36%	60%
5 years to 10 years	80%	37%	80%
10 years and above	100%	100%	100%

61. **Total Principal Funds Invested –** These limits are set having regard to the amount of reserves available for longer term investment and show the limits to be placed on investments with final maturities beyond 1 year. This limit allows the authority to invest for longer periods if they give better rates than shorter periods. It also allows some stability in the interest returned to the Authority.

Table 17 - Principal Funds Invested

	2024/25 Original Indicator	2024/25 Revised Indicator
Maximum principal sums invested greater than 1 year	£50m	£50m

Conclusion

62. The prudential indicators have been produced to take account of the Council's borrowing position. The key borrowing indicator (the Operational Boundary) is £179.323m. The Council's return on investments has been good, exceeding both of the targets. Based on the

first six months of 2024/25 the Council's borrowing and investments is forecast to be on target on the approved 2024/25 budget.

63. The Council's treasury management activities comply with the required legislation and meet the high standards set out in the relevant codes of practice.

Outcome of Consultation

64. No consultation was undertaken in the production of this report.