

TREASURY MANAGEMENT STRATEGY INTERIM REPORT

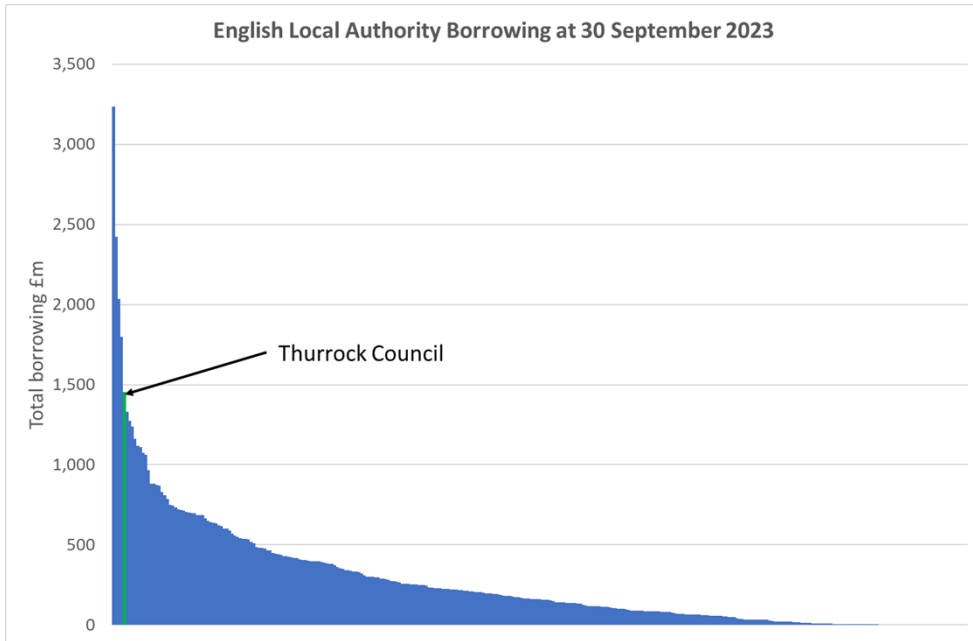
Debt Position at 30 September 2023

1. Table 1 below sets out the Council's debt position and changes between 1 April 2023 and 30 September 2023.

Table 1

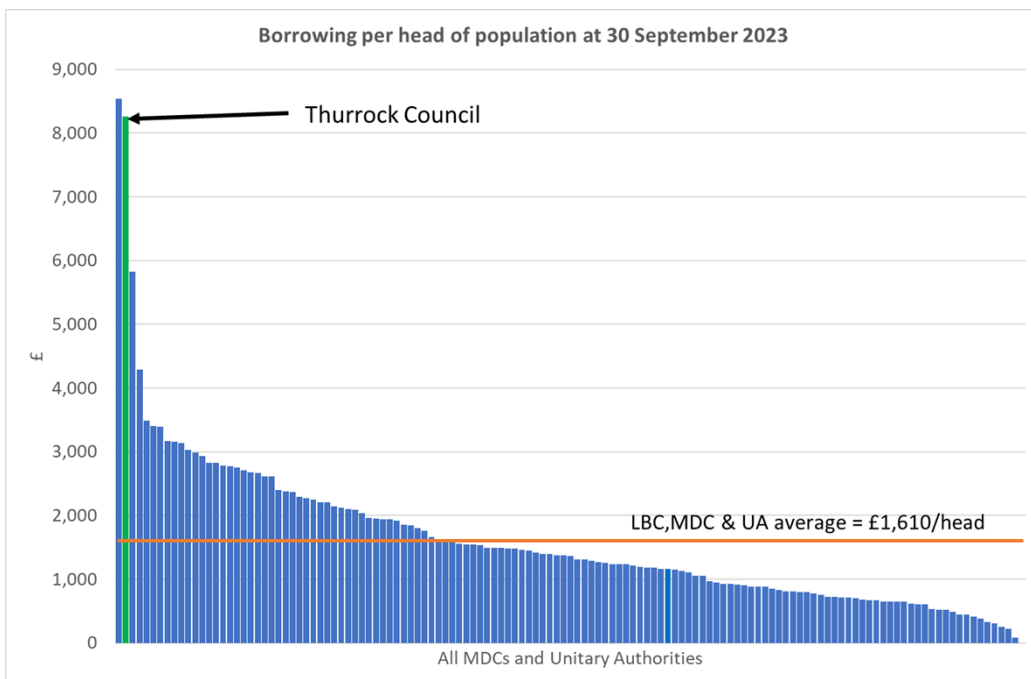
	Opening Balance 01-Apr £m	Repayments 30-Sep £m	New Borrowing 30-Sep £m	Mid-Year Balance 30-Sep £m
Long-Term PWLB	376	-	-	376
Market Loans	56	(2)	-	54
Local to Local Temporary Borrowing	200	(188)	-	12
Short-Term PWLB	921	(200)	290	1,011
Total	1,553	(390)	290	1,453

2. During this period the Council's overall borrowing reduced by £100m. This reduction is mainly due to a combination of three factors:
 - the Council now manages its day-to-day treasury function with lower cash balances than previously, the limit on the Council's bank account having been reduced from an average of £80m to £40m as part of the 2023/24 Treasury Management Strategy
 - the Council has received investment distributions from some capital investments, which have bolstered available cash balances, and
 - the significant reduction in borrowing to fund capital spending (see below).
3. Debt is forecast to reduce further in the second half of the year, as the Council is expecting to receive capital receipts from the sale of assets and investments, all of which will be used to repay outstanding debt balances.
4. Current expectations are that the Council's revised expectation is that external borrowing will reduce to £872m by 31 March 2024 – a £637m reduction in the original forecast of £1,509m for 31 March 2024.
5. At £1.453 billion, the Council had the fifth highest level of external borrowing amongst all English local authorities at 30 September 2023, as shown below:



Source: www.gov.uk/government/statistical-data-sets/live-tables-on-local-government-finance.

6. The chart above does not reflect the relative size of the authority to the borrowing. Expressed as borrowing per head of population shows that The Council's borrowing was the second highest at £8,255 per head of population at 30 September 2023.



Source: www.gov.uk/government/statistical-data-sets/live-tables-on-local-government-finance.

7. A significant reduction in external borrowing is a key requirement of the intervention measures currently in place with DLUHC and is necessary to ensure that the Council moves towards a more sustainable financial position. Reducing debt is important from a financial perspective for two reasons:

- Once a loan is repaid, the Council no longer has to set aside a Minimum Revenue Provision (MRP), which is a revenue saving (although not a cash saving) against the General Fund, and
- The Council will also save the interest cost in respect of any loan which is has been repaid.

Future Borrowing needs

8. Reductions to the Council's capital programme should significantly reduce future borrowing need. Proposals will be presented in a separate report to Members with the potential to further reduce the capital programme by up to £122.8m through a combination of removing non-essential projects from the programme altogether, and reprofiling HRA expenditure into 2026/27 and future years.
9. This has the potential to reduce the Council's requirement for new borrowing over the same 3-year period from £152m to £58.7m, leading to expected annual revenue savings of c£14.7m pa.

Liability Benchmark

10. This is a new Prudential Indicator for 2023/24, representing a projection of the amount of loan debt outstanding that the authority needs in the future to fund its existing debt liabilities, planned prudential borrowing and other cash flows. The Council is required to estimate and measure the benchmark for the forthcoming financial year and the following two financial years, as a minimum. Table 2 below sets out the expected position separately for the General Fund and the HRA:

Table 2 – Liability Benchmarks (General Fund and HRA)

Liability Benchmark (General Fund)		2023/24	2024/25	2025/25	2026/27	2027/28
Revised liability benchmark at 30/9/2023		£m	£m	£m	£m	£m
Existing Loan Debt Outstanding	A	244	244	29	29	29
Loans CFR	B	738	739	703	670	671
New loans Requirement	C	738	740	704	671	672
Liability Benchmark (Gross Loans Requirement)	D	758	760	724	691	692
(Over)/Under Liability Benchmark	E=D-A	514	516	695	662	663

Liability Benchmark (HRA)		2023/24	2024/25	2025/25	2026/27	2027/28
Revised liability benchmark at 30/9/2023		£m	£m	£m	£m	£m
Existing Loan Debt Outstanding	A	161	161	161	161	161
Loans CFR	B	262	283	292	313	329
New loans Requirement	C	266	283	292	313	329
Liability Benchmark (Gross Loans Requirement)	D	271	288	297	318	334
(Over)/Under Liability Benchmark	E=D-A	110	127	136	157	173

11. The liability benchmarks for the General Fund and HRA have changed since the beginning of the financial year as follows:
- The General Fund liability benchmark has reduced significantly as shown in Table 3 below:

Table 3 – Liability benchmark – General Fund movement

Liability Benchmark (General Fund)		2023/24			2024/25		
		Original	Revised	Variance	Original	Revised	Variance
		£m	£m	£m	£m	£m	£m
Existing loan debt outstanding	A	244	244	0	244	244	0
Loans CFR	B	1,282	738	(544)	746	739	(7)
Net Loans Requirement	C	1,297	463	(834)	684	375	(309)
Liability Benchmark (Gross Loans Requirement)	D	1,337	483	(854)	724	395	(329)
(Over)/Under Liability Benchmark	E=D-A	1,093	239	(854)	480	151	(329)

This reflects approved changes to the capital programme, timing, and levels of income from disinvestments and timing of other asset disposals.

- However, the HRA liability benchmark has increased as shown in Table 4 below, reflecting a slight increase in the capital programme:

Table 4 – Liability benchmark – HRA movement

Liability Benchmark (HRA)		2023/24			2024/25		
		Original	Revised	Variance	Original	Revised	Variance
		£m	£m	£m	£m	£m	£m
Existing loan debt outstanding	A	161	161	0	161	161	0
Loans CFR	B	254	262	8	309	283	(26)
Net Loans Requirement	C	173	266	93	228	283	55
Liability Benchmark (Gross Loans Requirement)	D	173	271	98	228	288	60
(Over)/Under Liability Benchmark	E=D-A	12	110	98	67	127	60

12. Notwithstanding the increase in the HRA liability benchmark, review of the capital programme has kept the need for borrowing at the level originally forecast.

Capital Financing Requirement

13. The Capital Financing Requirement (CFR) is a key financial indicator established in line with the requirements of The Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 and CIPFA's Prudential Code. It represents the amount of capital spending that has not yet been financed by capital receipts, capital grants or contributions from revenue income. Applying the general principle that borrowing should only be for capital purposes and not support revenue spending, the CFR is therefore a proxy, under normal

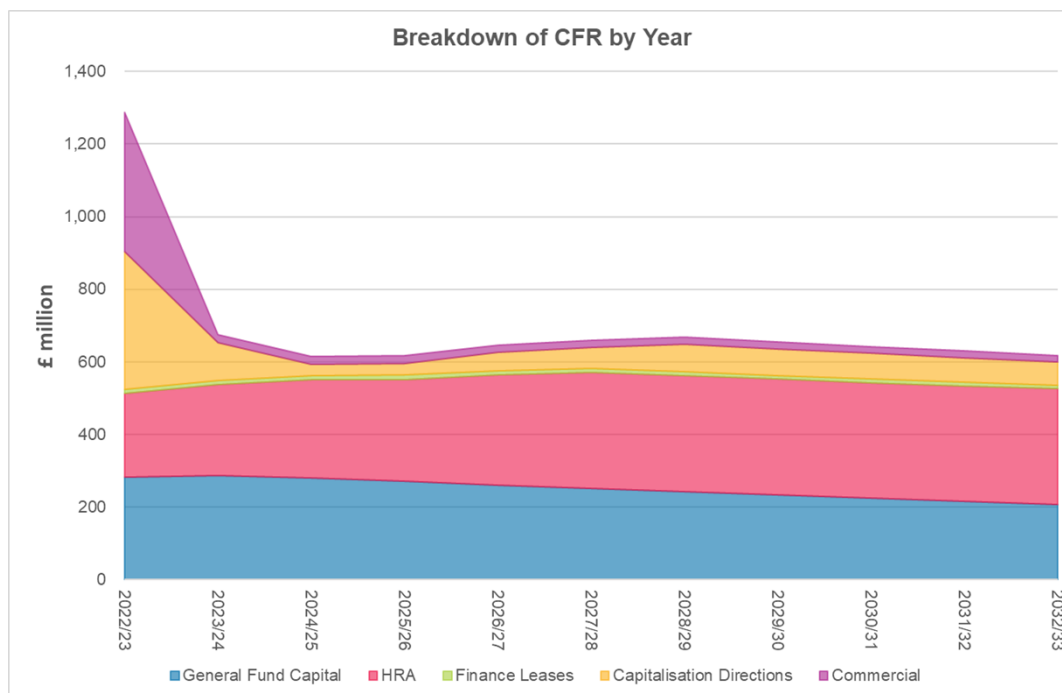
circumstances, for the limit of external borrowing which the Council should not exceed.

14. However, this comparison comes with three important caveats:
- although any unfinanced capital expenditure incurred will increase the CFR, if the Council has cash resources available to it, these could be used as an alternative to external borrowing. Therefore the CFR increases, but not the level of external debt,
 - the CFR mechanism assumes that all expenditure financed from borrowing is capital in nature, but the Council has made several investments that were subsequently found not to meet the definition of capital expenditure but nonetheless had been borrowed for. In this situation the Council's borrowing increases, but not the CFR.
 - MRP set aside requirements (see below) do not correspond to actual repayments of borrowing.
15. All three situations create a mismatch between the CFR and borrowing levels. At 31 March 2023, the Council's CFR was £1,454m and external borrowing was £1,553m, mainly as a result of the reclassification of investments from capital to revenue.
16. By implementing the debt reduction strategies outlined above, the CFR at 31 March 2024 is expected to fall from the original forecast of £1,548m to the revised forecast of £725m (as at 30 September 2023), as shown in Table 5 below. The £823m reduction in the CFR reflects the impact of the anticipated capital receipts from the Council's divestment programme and a change to accounting for previous years' understatement of MRP from being a retrospective adjustment to a prospective adjustment from 1 April 2023.

Table 5 – Forecast General Fund and HRA CFR at 31 March 2024

	Original forecast			Revised forecast			Variance £m
	General Fund	HRA	Total	General Fund	HRA	Total	
	£m	£m	£m	£m	£m	£m	
General Fund	648		648	341		341	(307)
HRA		255	255		250	250	(5)
Finance Leases		12	12		12	12	0
Capitalisation Direction	610		610	273		273	(337)
Commercial	23		23	124		124	101
Total	1,281	267	1,548	738	262	1,000	(548)

17. The Council's longer-term aim is to reduce the CFR to below £900m by 2032/33, as shown below:



Source: Council Treasury Management Model

Interest Rates

18. Interest rates remain a key risk to the Council, particularly as most of the debt is short-term and needs to be refinanced regularly, leaving the Council exposed to changes in interest rates.
19. All new borrowing taken out by the Council is from PWLB and the interest rates charged are based on Gilt prices. At present, the Council's borrowing is priced at Gilts + 0.8% and these rates fluctuate daily. While not directly connected to Bank of England base rates, any change in the base rate will usually have an impact on Gilt prices.
20. At the beginning of April 2022 the Bank of England base rate stood at 0.75% but by March 2023 this had risen to 4.25%. Currently the base rate stands at 5.25%, although there is a general expectation from the Council's advisors that this will begin to reduce towards the end of the current financial year and fall to 3% by 2026, although it should be noted that other agencies may be predicting different levels to this.
21. The Government has set a medium-term target of 2% for annual inflation however it is well known that inflation is at a much higher level than this currently, and, more importantly, is not coming down as quickly as had been hoped. Consumer Price Inflation at the beginning of September 2023 stood at

6.7%¹, a significant improvement from the high point of 11.1% in October 2022, but the pace and extent of any future reductions remain uncertain.

22. Table 6 below shows the assumptions on interest rates which were used in the original strategy and the revised rates currently being factored in, based on information provided by the Council's Treasury Management advisors (Link Treasury Services Ltd), and represent an average rate for the year:

Table 6 – Interest rate assumptions 2023/24 and 2024/25

	Original		Revised	
	2023/24	2024/25	2023/24	2024/25
Bank Rate	4.50%	3.50%	5.50%	5.00%
Temporary Loans	5.00%	4.00%	5.80%	4.80%
Investment Rate	4.50%	3.30%	5.00%	4.50%
Overdraft	5.50%	4.50%	6.50%	6.00%
1 year PWLB	4.50%	4.00%	5.80%	4.80%
5 year PWLB	4.10%	3.60%	5.60%	4.60%
10 year PWLB	4.30%	3.80%	5.40%	4.40%
25 year PWLB	4.50%	4.00%	5.20%	4.20%
50 year PWLB	4.20%	3.70%	5.00%	4.00%

23. Looking at the PWLB rates specifically, the rate (one year certainty rate for new maturity loan) that was applicable at the beginning of the year was 4.80%. Rates during the first half of the year peaked at 6.36% before falling to 5.69% at the end of September. Current projections from the Council's advisors suggests that 12-month PWLB borrowing will reduce to around 5.00% by the end of the financial year.
24. The Council's interest costs will continue to be monitored closely and will be reported as part of the quarterly budget monitoring financial reporting.

Investments

25. This section of the report deals with the Council's management of surplus cash balances not needed for immediate use. The Statutory Guidance on Local Government Investments (3rd edition) published by DLUHC explains that financial investments can fall into one of three categories:
- Specified investments;
 - Loans; and
 - Non-specified investments.
26. Specified investments are:
- denominated in sterling;
 - held for less than 12 months maturity;

¹ Source: Office for National Statistics

- not statutorily defined capital expenditure under Regulation 25(1)(d) of the Local Authorities (Capital Finance and Accounting)(England) Regulations 2003, as amended; and
 - invested in high quality schemes as defined in the Statutory Investment Guidance.
27. The Council has a substantial investment portfolio with a nominal value in excess of £1 billion. The portfolio has experienced a fall in value to date of around £283m as shown in the table below.

Table 7 - Value of investment portfolio

Asset Class	Nominal value £m	Change in value £m	Estimated carrying value £m
Specified investments Cash			
On call	20	0	20
Short-term notice	40	0	40
Total specified investments	60	0	60
Loans	39	0	39
Non-specified investments:			
Equity	104	(21)	83
Corporate Bonds	804	(252)	552
Pooled Funds	104	(10)	94
Total non-specified investments	1,012	(283)	729
Total	1,111	(283)	828

Investment performance monitoring

28. At over £1 billion, the value of investments is on the same level as for smaller local authority pension funds. The performance of local authority pension funds is heavily regulated to safeguard members' investments. Regulation includes:
- Setting performance benchmarks for assets classes over different time periods;
 - Quarterly monitoring of investment performance for each investment;
 - Provision of investment advice independent from the fund manager;
 - Safeguarding of the assets by holding them through a custodian.
29. The Statutory Guidance on Local Government Investments does not explicitly specify an equivalent form of regulation, but nonetheless requires that authorities investing on non-specified investments should appropriate capacity, skills and information to enable both members and officers to make informed decisions about entering into and monitoring investments.

30. Although independent investment advice is provided by Camdor Global Advisors, several of the key measures that would be expected of a local authority pension fund were not in place:
- no performance benchmarks have been set;
 - there has been no regular quarterly monitoring information obtained;
 - only about half of the assets were securely held via a custodian provider;
31. Action is now being taken to ensure that appropriate investment performance information is obtained for all investments and performance reported quarterly to Members.

Specified investments

32. The value of specified investments (i.e. cash-based investment balances) at 30 September 2023 of £60m was £7m higher than at the beginning of the year, although it should be noted that the equivalent balance at 1 April 2022 was £68.7m.
33. To reduce borrowing for capital purposes, the Council is now operating with lower cash balances and is increasingly using cash 'on call' (can be returned to the Council on the same day) and short-term notice (one week notice required for return of funds) investments. This ensures that the Council maintains sufficient funds for day-to-day liquidity requirements before any fixed term investments are considered.
34. During the period to 30 September the Council earned just over £1.53m in interest income and this is expected to rise to £2.89m by year-end. This compares favourably against the budgeted income £1.5m for 2023/24. The increased income is the result of investing surplus cash balances arising from realising receipts from selling investments as part of the Council's accelerated Asset Disposal Strategy. All cash-based investments in 2023/24 to date have complied with the strategy approved by Members prior to the start of the year.

Loans

35. The Council has advanced £39m of loans to three entities. £32.4m (i.e. 83%) of the lending is to the Council's subsidiary company Thurrock Regeneration Ltd. To date there has been no experience of default on any of the loans advanced.

Non-specified Investments

36. As noted above, the Council has experienced a loss of approximately 28% in the value of its non-specified investment portfolio. Investment performance is the total of any investment returns less any operating costs and finance costs incurred in holding the assets plus or minus any change in market value of the assets. As the entire portfolio was financed from borrowing, even after taking

after taking account of borrowing costs, the portfolio is generating a negative return of 37.8% summarised below:

Table 8 - Performance of non-specified investments

Non-specified investment	Nominal value	Return
	£m	%
Equity	104	-20.3
Corporate Bonds	804	-44.1
Pooled Funds	104	-5.9
Total	1,012	-37.8

37. The Council has approved a Disinvestment Strategy and all proceeds from the sale of investments will be used to reduce external debt. Work is continuing with advisors to maximise the return from these investments, the position remains fluid and is affected to some extent by disposals and disinvestment, this will continue to be updated during the year.

Minimum Revenue Provision (MRP)

38. As well as new capital expenditure increasing the CFR, when capital expenditure has not been financed by grant funding, capital receipts or third-party contributions, the Council is required to make a provision annually for the repayment of debt. This non-cash adjustment, which represents a charge against General Fund balances each year, is known as the Minimum Revenue Provision or MRP. When MRP is applied, the CFR is reduced, but this does not represent actual repayment of borrowing. However, the use of capital receipts from the sale of assets and investments to reduce debt can also reduce the requirement for MRP.
39. As part of the Council's process of engagement with DLUHC, the current MRP policy and underlying calculations have been subject to detailed external review. Although the relevant legislation and statutory Guidance provides some discretion as to how MRP should be calculated, the review highlighted that the Council has not set aside adequate levels of MRP in previous years.

MRP Policy Statement

40. The MRP Policy Statement forms part of the annual budget setting framework. Paragraph 10 of Annex B to the 2018 Statutory MRP Guidance explains that the purpose of preparing a MRP Statement "is to give elected Members the opportunity to scrutinise the proposed use of the additional freedoms conferred under the new arrangements".
41. When reporting its proposed MRP policy for the forthcoming year, the Council must therefore both demonstrate that the authority has had regard to the Statutory MRP Guidance and also provide sufficient detailed information to allow elected members to make an informed decision. About whether or not to approve the proposed policy. Therefore, the proposed policy should explain:

- What the four suggested calculation options are under the Statutory MRP Guidance;
 - Whether there are any proposed deviations from these four options; and
 - Where any deviations are proposed, an explanation of how, and confirmation that, the proposed policy still provides a “prudent” level of MRP.
42. Prior to 2023/24, none of the MRP Policy Statements provided the above information to elected Members, so provided insufficient information for Members to make an informed decision.
43. The following changes were made to the Council’s MRP calculations:
- In 2016/17 the MRP policy was amended in respect of supported capital expenditure to charge MRP on a straight-line over a 50 year period and was backdated to 1 April 2008. There was no mention that this was a deviation from the Statutory MRP Guidance which only permits the use of Options 1 or 2 to be used to calculate MRP for supported capital expenditure.
 - In 2017/18, the calculation of the MRP on supported capital expenditure was further amended to an annuity method. The impact of using an annuity approach was to shift the incidence of the MRP charge into future years which is in direct opposition to the reducing balance method of Options 1 and 2. The change in method was not reported to Members.
44. Discussions with DLUHC and CIPFA have confirmed that only Options 1 and 2 are permissible methods for calculating MRP on supported capital expenditure.
45. Notwithstanding that the MRP policies which the Council had approved in previous years did not follow the statutory MRP Guidance, legal advice obtained confirms that the MRP policies in those years were properly approved in line with the Council’s decision-making processes and thus lawfully set. Accordingly to bring the MRP Policy in line with the MRP Guidance, the changes will be effected from 1 April 2023. This means that the change in MRP policy will be executed over the residual CFR for each element of the CFR at 31 March 2023 and MRP amortised over the remaining asset lives at 31 March 2023.
46. For example, an investment asset acquired in 2019/20 with a ten year asset life would have a remaining asset life at 31 March 2023 of 7 years. Therefore MRP would be charged over 7 years rather than the original 10 years.
47. The impact of the above is to reduce the CD in 2022/23 by £425m to £28m, and thus the MRP on the CD in 2023/24 is reduced to £0.9m, but increases the MRP on the investment portfolio to £155m in 2023/24. However the accelerated asset disposal programme means that the capital receipts generated in 2023/24 (rather 2024/25 as originally forecast) can be apply to fully finance the CD at 31 March 2024. This results in a reduction in the MRP on the CD over the period 2022/23 to 2028/29 from £71m to £4m.

48. Accordingly, it is recommended that:
- the MRP policy for 2023/24 in respect of MRP on supported capital expenditure should revert to Option 1 of the MRP Guidance, namely, that MRP should be set at 4% of the closing balance of the previous year's capital financing requirement (CFR) in respect of supported capital expenditure;
 - the change in MRP Policy to take effect from 1 April 2023.

Other Elements of the Strategy

49. Other aspects of the strategy approved for 2023/24 are commented on below and include comments on the outcomes for the year:
- The Treasury Management Strategy operates in a 'two pool' model, meaning that the debt and related costs are kept separate for the General Fund and HRA. This has been observed for the year to date, with new loans allocated to the appropriate fund. Adjustments will be made at year end to ensure that costs are allocated fairly to each of the funds and that separate CFR calculations are maintained for both the General Fund and the HRA.
 - Within the strategy the Council is required to operate within the overall debt and investment position and will be managed having regard to the Prudential Indicators set by the Council and the treasury indicators set. In this regard, the maximum gross external debt (including finance leases) during the first half of the year was £1,565 million, meaning that neither the operational boundary (£1,576 million) nor the authorised limit (£1,733 million) for external debt was breached during the period. A detailed comparison of other Prudential Indicators is provided in Appendix 2.
 - In line with the MHCLG Statutory Guidance on Local Government Investments (2018 edition), all monies are invested prudently considering security first, liquidity second and yield last. In the first half of 2023/24, no long-term investments have been made, and any surplus cash has been placed in short-term (on call) accounts.
50. During 2023/24, the limit on deposits with the Debt Management Office (DMO) was breached 52 times. In addition, the Council is likely to be in a position over the coming months when large cash deposits are received from sales and disinvestments and this change in policy will allow for officers to ensure that cash received is kept securely until such time as it is required for the repayment of debt.
51. The DMO is part of central government and is highly secure does not place limits on the sums taken and is often used as an alternative if cash cannot be placed with any other counterparty.
52. Consequently, it is recommended that the limit on deposits with the Debt Management Office (DMO) is removed.

53. There have been some changes to the assumptions underpinning expected levels of debt, new borrowing requirements, CFR calculations and interest costs and these have been set out in this report. However, the fundamental elements that made up the original strategy for 2023/24 remain unchanged, namely:
- A Debt Reduction Strategy is now in place,
 - Going forward, new borrowing will be minimised,
 - A Disinvestment Strategy is now in place to dispose of all non-cash investments and any assets held for operational purposes which are no longer required, and
 - All proceeds of sale will be applied to reduce external debt.

This page is intentionally left blank