Annex 5.2

TREASURY MANAGEMENT OUTTURN 2023/24

1. Introduction

The Council has adopted the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice* (the CIPFA Code) which requires the Council to approve, as a minimum, treasury management semi-annual and annual outturn reports.

This report satisfies the requirement in the 2021 Code, mandatory from 1 April 2023, of quarterly reporting of the treasury management prudential indicators.

The non-treasury prudential indicators are incorporated in the quarterly revenue and capital monitoring update.

The Treasury Management Strategy for 2023/24 was approved by Council on 20 July 2023.

The Council has invested significant sums and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates.

The successful identification, monitoring and control of risk therefore remains central to the Council's treasury management strategy.

2. External Context

(Source: Arlingclose)

Economic background: *UK inflation continued to decline from the 8.7% rate seen at the start of 2023/24. By the last quarter of the financial year headline consumer price inflation (CPI) had fallen to 3.4% in February but was still above the Bank of England's 2% target at the end of the period. The core measure of CPI, i.e., excluding food and energy, also slowed in February to 4.5% from 5.1% in January, a rate that had stubbornly persisted for three consecutive months.*

The UK economy entered a technical recession in the second half of 2023, as growth rates of -0.1% and -0.3% respectively were recorded for Q3 and Q4. Over the 2023 calendar year GDP growth only expanded by 0.1% compared to 2022. Of the recent monthly data, the Office for National Statistics reported a rebound in activity with *economy expanding 0.2% in January 2024. While the economy may somewhat recover in Q1 2024, the data suggests that prior increases in interest rates and higher price levels are depressing growth, which will continue to bear down on inflation throughout 2024.*

Labour market data provided a mixed message for policymakers. Employment and vacancies declined, and unemployment rose to 4.3% (3mth/year) in July 2023. The same month saw the highest annual growth rate of 8.5% for total pay (i.e. including bonuses) and 7.8% for regular pay growth (i.e. excluding bonuses). Thereafter, unemployment began to decline, falling to 3.9% (3mth/year) in January and pay growth also edged lower to 5.6% for total pay and 6.1% for regular pay, but remained above the Bank of England's forecast.

Having begun the financial year at 4.25%, the Bank of England's Monetary Policy Committee (MPC) increased Bank Rate to 5.25% in August 2023 with a 3-way split in the Committee's voting as the UK economy appeared resilient in the face of the dual headwinds of higher inflation and interest rates. Bank Rate was maintained at 5.25% through to March 2024. The vote at the March was 8-1 in favour of maintaining rates at this level, with the single dissenter preferring to cut rates immediately by 0.25%. Although financial markets shifted their interest rate expectations downwards with expectations of a cut in June, the MPC's focus remained on assessing how long interest rates would need to be restrictive in order to control inflation over the medium term.

In the Bank's quarterly Monetary Policy Report (MPR) released in August 2023 the near-term projection for services price inflation was revised upwards, goods price inflation widespread across products, indicating stronger domestic inflationary pressure with second-round effects in domestic prices and wages likely taking longer to unwind than they did to emerge. In the February 2024 MPR the Bank's expectations for the UK economy were positive for the first half of 2024, with a recovery from the mild recession in calendar H2 2023 being gradual. Headline CPI was forecast to dip below the 2% target quicker than previously thought due to declining energy prices, these effects would hold inflation slightly above target for much of the forecast horizon.

Following this MPC meeting, Arlingclose, the authority's treasury adviser, maintained its central view that 5.25% remains the peak in Bank Rate and that interest rates will most likely start to be cut later in H2 2024. The risks in the short-term are deemed to be to the downside as a rate cut may come sooner than expected, but then more broadly balanced over the medium term.

The US Federal Reserve also pushed up rates over the period, reaching a peak range of between 5.25-5.50% in August 2023, where it has stayed since. US policymakers have maintained the relatively dovish stance from the December

FOMC meeting and at the meeting in March, economic projections pointed to interest rates being cut by a total of 0.75% in 2024.

Following a similarly sharp upward trajectory, the European Central Bank hiked rates to historically high levels over period, pushing its main refinancing rate to 4.5% in September 2023, where it has remained. Economic growth in the region remains weak, with a potential recession on the cards, but inflation remains sticky and above the ECB's target, putting pressure on policymakers on how to balance these factors.

Financial markets: *Sentiment in financial markets remained uncertain and bond yields continued to be volatile over the year. During the first half of the year, yields rose as interest rates continued to be pushed up in response to rising inflation. From October they started declining again before falling sharply in December as falling inflation and dovish central bank attitudes caused financial markets to expect cuts in interest rates in 2024. When it emerged in January that inflation was stickier than expected and the BoE and the Federal Reserve were data dependent and not inclined to cut rates soon, yields rose once again, ending the period some 50+ bps higher than when it started.*

Over the financial year, the 10-year UK benchmark gilt yield rose from 3.44% to peak at 4.75% in August, before then dropping to 3.44% in late December 2023 and rising again to 3.92% (28th March 2024). The Sterling Overnight Rate (SONIA) averaged 4.96% over the period to 31st March.

Credit review: *In response to an improving outlook for credit markets, in January 2024 Arlingclose moved away from its previous temporary stance of a 35-day maximum duration and increased its advised recommended maximum unsecured duration limit on all banks on its counterparty list to 100 days.*

Earlier in the period, S&P revised the UK sovereign outlook to stable and upgraded Barclays Bank to A+. Moody's also revised the UK outlook to stable, Handelsbanken's outlook to negative, downgraded five local authorities, and affirmed HSBC's outlook at stable while upgrading its Baseline Credit Assessment. Fitch revised UOB's and BMO's outlooks to stable.

In the final quarter of the financial year, Fitch revised the outlook on the UK sovereign rating to stable from negative based on their assessment that the risks to the UK's public finances had decreased since its previous review in October 2022, the time of the mini- budget.

Moody's, meanwhile, upgraded the long-term ratings of German lenders Helaba, Bayern LB and LBBW on better solvency and capital positions, despite challenges from a slowing German economy and exposure to the commercial real estate sector. Moody's also upgraded or placed on review for an upgrade, Australian banks *including ANZ, CBA NAB and Westpac on the back of the introduction of a new bank resolution regime.*

Credit default swap prices began the financial year at elevated levels following the fallout from Silicon Valley Bank and collapse/takeover of other lenders. From then the general trend was one of falling prices and UK lenders' CDS ended the period at similar levels to those seen in early 2023. Earlier in the year some Canadian lenders saw their CDS prices rise due to concerns over a slowing domestic economy and housing market, while some German lenders were impacted by similar economic concerns and exposure to commercial real estate towards the end of the period, with LBBW remaining the most elevated.

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

3. Local Context

On 31 March 2024, the Council had net investments of £16.0million arising from its revenue and capital income and expenditure.

The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while balance sheet resources are the underlying resources available for investment.

These factors are summarised in the table below.

Table 1: Balance Sheet Summary	**31/03/2023 Actual £000**	**31/03/2024 Actual £000**
General Fund CFR	90,200	72,100
External borrowing[1]	(7,000)	-
Internal borrowing	**83,200**	**72,100**
Less: Balance sheet resources	99,194	88,110
Investments/ (borrowing)	**15,994**	**16,010**

NOTE 1: Council loans during 2022/23 were repaid in 2023/24.

The treasury management position at 31 March and the change since 1 April is set out in the table below.

Table 2: Treasury Management Summary	31/03/2023 Balance £000	Movement £000	31/03/2024 Balance £000	31/03/2024 Rate %
Short term Borrowing	(7,000)	7,000	-	-
Cash and cash equivalents	15,994	16	16,010	4.87%
Net investments	**8,994**	**7,016**	**16,010**	**4.87%**

Borrowing

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

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

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

Borrowing Strategy and Activity

As at 31 March 2024 the Council held no loans.

The Council has historically been largely debt free and has borrowed on a temporary basis to fund short term cash flow shortfalls. This strategy is likely to remain the most effective in future.

The chief objective when borrowing has been to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required, with flexibility to renegotiate loans should long-term plans change being a secondary objective.

The borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio.

Treasury Investment Activity

The CIPFA Treasury Management Code defines treasury management investments as those investments which arise from the authority's cash flows or treasury risk management activity that ultimately represents balances that are invested until the cash is required for use in the course of business.

The Council holds invested funds, representing income received in advance of expenditure, plus balances and reserves.

During the year, investment balances ranged between £11.8 million and £65.9 million due to timing differences between income and expenditure.

The investment position is set out in the table below:

Table 4: Treasury Investment Position	**31/03/2023 Balance £000**	**Net Movement £000**	**31/03/2024 Balance £000**	**31/03/2024 Income Return %**	**31/03/2024 Weighted Average Maturity (Days)**
Banks & building societies (unsecured)	8,994	(6,984)	2,010	2.12%	1
Money Market Funds	7,000	7,000	14,000	2.05%	1
Total investments	**15,994**	**16**	**16,010**	**4.87%**[1]	**1**[1]

NOTE 1: Weighted Average

Both the CIPFA Code and government guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its treasury investments before seeking the optimum rate of return, or yield.

The objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

Other factors taken into account after considering security, liquidity and yield include the counter-party's Environmental, Social & Governance (ESG) status. This is determined by reference to whether they are members of the Net Zero Asset Managers Initiative and a signatory to the UN Principles for Responsible Investment

Bank Rate was maintained at 5.25% from December to the end of March 2024.

Performance against risk and return metrics are set out in the extract from Arlingclose's quarterly investment benchmarking below.

Table 5: Investment Benchmarking – Treasury investments managed in-house	**Credit Score**	**Credit Rating**	**Bail-in Exposure**	**Weighted Average Maturity (days)**	**Rate of Return %**
Reigate & Banstead Borough Council					
31/03/2023	4.90	A+	100%	1	4.01%
30/09/2024	4.29	AA-	66%	25	4.65%
30/12/2023	4.62	AA-	80%	9	5.02%
31/03/2024	4.92	A+	100%	1	4.87%
Similar Local Authorities	4.90	A+	61%	50	5.20%
All Local Authorities	4.82	A+	61%	9	5.17%

Non-Treasury Investments

The definition of investments in the Treasury Management Code covers all financial assets of the Council as well as other non-financial assets which the Council holds primarily for financial return.

Investments that do not meet the definition of treasury management investments (i.e., management of surplus cash) are categorised as either for service purposes (made explicitly to further service objectives) and or for commercial purposes (made primarily for financial return).

Investment Guidance issued by the Department for Levelling Up Housing and Communities (DLUHC) and Welsh Government also includes, within the definition of investments, all such assets held partially or wholly for financial return.

During 2023/24 the Council held:

- £1.1m shares in Pathway For Care Limited;
- £0.652m shares in Greensand Holdings Limited; and
- Loans of £13.258m advanced to Greensand Holdings Limited

Note: the above excludes funds previously provided to Horley Business Park Development LLP which has been liquidated.

Compliance

All treasury management activities undertaken during 2023/24 complied fully with the CIPFA Code of Practice and the Council’s approved Treasury Management Strategy. Compliance with specific investment limits, is demonstrated in the table below.

Table 6: Investment Limits	**2023/24 Maximum £000**	**31/03/2024 Actual £000**	**2023/24 Limit £000**	**Complied?**
Any single organisation, except the UK Government	10,000	2,010	10,000	Yes
Any group of pooled funds under the same management	-	-	10,000	Yes
Negotiable instruments held in a broker’s nominee account	-	-	13,000	Yes
Limit per non-UK country	-	-	5,000	Yes
The UK Government	25,000	-	n/a	Yes
Local authorities & other government entities	-	-	Unlimited	Yes
Secured investments	-	-	Unlimited	Yes
Banks (unsecured) (Excluding the Councils Operational bank accounts)	10	10	Unlimited	Yes
Building societies (unsecured)	-	-	10,000	Yes
Registered providers (unsecured)	-	-	13,000	Yes
Money market funds	£41m sector (£10m per counterparty)	£14m sector (£3m per counterparty)	Unlimited (£10m per counterparty)	Yes
Strategic pooled funds	-	-	25,000	Yes
Real estate investment trusts	-	-	13,000	Yes
Other investments	-	-	5,000	Yes

Treasury Management Prudential Indicators

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

1. Liability Benchmark

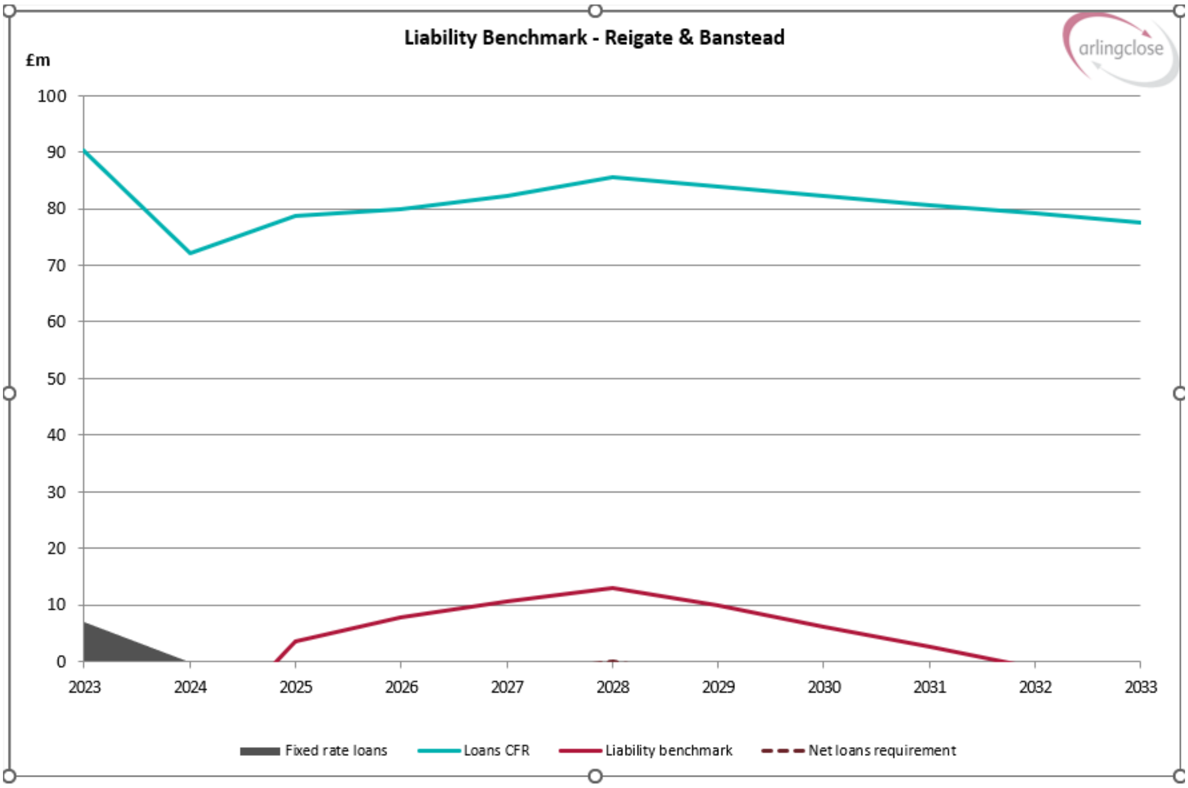
This indicator compares the Council’s actual current borrowing against a liability benchmark that has been calculated to show the lowest risk level of borrowing.

The liability benchmark is an important tool to help establish whether the Council is likely to be a long-term borrower or long-term investor in the future, and so shape its strategic focus and decision making.

It represents an estimate of the cumulative amount of external borrowing the Council must hold to fund its current capital and revenue plans while keeping treasury investments at the minimum level of £15.0 million required to manage day-to-day cash flow.

Table 7: Liability Benchmark	**31/03/2023 Actual £000**	**31/03/2024 actual £000**	**31/03/2025 Forecast £000**	**31/03/2026 Forecast £000**
Loans CFR	90,200	72,100	78,700	80,000
Less: Balance sheet resources	99,194	88,110	88,100	85,000
Net loans requirement	**8,994**	**16,010**	**9,400**	**5,000**
Plus: Liquidity allowance	-	-	13,000	13,000
Liability benchmark	**-**	**-**	**3,600**	**8,000**
Current borrowing	**(7,000)**	**-**	**-**	**-**

Following on from the medium-term forecast in the table above, the long-term liability benchmark assumes no capital expenditure will be funded by borrowing after 2027/28 and that reserves will increase by 2.5%. This is illustrated in the chart below:



The net loans requirement represents external borrowing required to keep investment balances just above nil. This is below zero and therefore does not appear on the graph.

What this means is that no external borrowing would be required solely to maintain a positive investment balance. However, borrowing is required, as shown by the liability benchmark line, to maintain investment balances at the desired £15m minimum level.

The net loans requirement on the graph is a lower figure and represents the borrowing that would be required if investment balances were kept at nil.

The graph represents only a snapshot in time at year end when balances are typically at their lowest and borrowing needs are highest. In year balances are expected to fluctuate to up to £65.9 million.

Borrowing is therefore in practice only likely to be required in the short term for some parts of the year.

2. Maturity Structure of Borrowing

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

Table 8: Maturity Structure of Borrowing	Upper Limit	Lower Limit	31/03/2024 Actual Borrowing	Complied?
Under 12 months	100%	0%	-	Yes
12 months and within 24 months	100%	0%	-	Yes
24 months and within 5 years	100%	0%	-	Yes
5 years and within 10 years	100%	0%	-	Yes
10 years and above	100%	0%	-	Yes

Time periods start on the first day of each financial year.

The maturity date of borrowing is the earliest date on which the lender can demand repayment.

As the Council has a relatively modest, and short term, overall borrowing requirement there is no significant refinancing risk associated with having all loans maturating within the timescales shown above.

At present the Council would wish to retain maximum flexibility as to the periods in which it borrows over. If the debt portfolio becomes more extensive, then the indicator will be reviewed to ensure that it remains suitable.

3. Long-term Treasury Management Investments

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

Table 9: Long Term Investments	2023/24	2024/25	2025/26	No fixed date
Limit on principal invested beyond year end	£10.0m	£10.0m	£10.0m	£10.0m
Actual principal invested beyond year end	£0m	£0m	£0m	£0m
Complied?	Yes	Yes	Yes	Yes

Long-term investments with no fixed maturity date include strategic pooled funds, real estate investment trusts and directly held equity, but exclude money market funds and bank accounts with no fixed maturity date as these are considered short-term.

Additional indicators

Security: The Council has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average rating / credit score of its investment portfolio.

This is calculated by applying a score to each investment (AAA=1, AA+=2, etc.) and taking the arithmetic average, weighted by the size of each investment. Unrated investments are assigned a score based on their perceived risk.

Table 10: Credit Risk	2023/24 Target	31/03/2024 Actual	Complied?
Portfolio average credit	A	A+	Yes

Liquidity: The Council has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments within a rolling three-month period.

Table 11: Liquidity Risk	2023/24 Target	31/03/2024 Actual	Complied?
Total cash available within 3 months	£5.0m	£14.0m	Yes

Interest Rate Exposures: This indicator is set to control the Council's exposure to interest rate risk. The Bank Rate was maintained at 5.25% since December 2023.

Table 12: Interest rate risk indicator	2023/24 Target	31/03/2024 Actual	Complied?
Revenue impact of a 1% change in interest rates	£0.078m (net income, per annum)	£0.144m (net income, per annum)	Exceeded indicator.

The target figure was set at a time when the authority had both short-term investments and short-term debt, mitigating the overall impact of a change of interest rates. At 31 March 2024 the authority had no short-term debt, thus increasing the impact of a change in interest rates on investments held. This target will be reviewed for the next financial year.

For context, the changes in interest rates during the year were:

Interest Rates	31/3/23	31/03/24
Bank Rate	4.25%	5.25%
1-year PWLB certainty rate, maturity loans	4.78%	5.56%
5-year PWLB certainty rate, maturity loans	4.31%	4.98%
10-year PWLB certainty rate, maturity loans	4.33%	5.10%
20-year PWLB certainty rate, maturity loans	4.70%	5.49%
50-year PWLB certainty rate, maturity loans	4.41%	5.30%

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