Agenda Item No. 5

South Ayrshire Council

Report by Head of Finance, ICT and Procurement to South Ayrshire Council of 6 March 2024

Subject: Treasury Management and Investment Strategy 2024/25

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1. Purpose

1.1 The purpose of this report is to request that Members consider the proposed Treasury Management and Investment Strategy for financial year 2024/25.

2. Recommendation

2.1 **It is recommended that the Council approves the draft Treasury Management and Investment Strategy for 2024/25 (attached as Appendix 1).**

3. Background

3.1 The Treasury Management service undertakes two main roles wiithin the Council:

3.1.1 The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's low risk investment appetite, whilst providing adequate liquidity initially before considering investment return.

3.1.2 The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer-term cash flow planning, to ensure that the Council can meet its capital spending obligations. This management of longer-term cash may involve arranging long or short-term loans or using longer-term cash flow surpluses. On occasion, when it is prudent and economic, any debt previously drawn may be restructured to meet Council risk or cost objectives.

3.2 The contribution the treasury management function makes to the authority is critical, as the balance of debt and investment operations ensure liquidity and the ability to meet spending commitments as they fall due, either on day-to-day revenue or for larger capital projects.

3.3 The treasury operations will see a balance of the interest costs of debt and the investment income arising from cash deposits affecting the available budget. Since cash balances generally result from reserves and balances, it is paramount to ensure adequate security of the sums invested, as a loss of principal will in effect result in a loss to the General Fund Balance.

3.4 Whilst any loans to third parties, commercial investment initiatives or other non-financial investments will impact on the treasury function, these activities are generally classed as non-treasury activities, (arising usually from capital expenditure),and are separate from the day to day treasury management activities.

3.5 CIPFA defines treasury management as:

> ‘The management of the local authority’s borrowing, investments and cashflows, 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.’

4. Proposals

4.1 The purpose of the Treasury Management and Investment Strategy is to detail the planned activities for the treasury service in the forthcoming financial year. The draft proposed Strategy for 2024/25 is attached at Appendix 1.

4.2 The Strategy sets out the basis for decision making in relation to managing the Council’s cash flow position to ensure appropriate investment returns are achieved and ensuring that appropriate funding for budgeted capital investment plans during 2024/25 are in place and to ensure the relevant borrowings are in line with loan charge budgets.

4.3 The overall objectives for the Council’s Treasury Management and Investment Strategy are:

4.3.1 ***For Borrowings the objective is:***

- to minimise the revenue cost of borrowings;
- to manage the Council’s cash flow;
- to manage the borrowing repayment profile;
- to assess interest rate movements, and borrow/invest accordingly;
- to monitor and review the level of variable rate loans held to take advantage of interest rate movements; and
- to identify and evaluate opportunities for debt rescheduling.

4.3.2 ***For Temporary Investments the objective is:***

- to protect capital security of the invested funds; and
- to obtain the best market return available commensurate with protection of security and liquidity.

Temporary investments will continue to be managed using the following priorities in order of importance:

- security of capital;
- liquidity; and
- yield.

4.4 ***Reporting Requirements*** - The reporting of Treasury Management to Members in 2024/25 is proposed to be as follows:

4.4.1 **A Treasury Management and Investment Strategy Report (this report)** - This first, and most important, report covers:

- the capital plans (including prudential indicators);
- the Treasury Management Strategy (how the investments and borrowings are to be managed) including treasury indicators; and
- an Investment Strategy (the parameters on how investments are to be managed).

This report is presented to full Council for approval.

4.4.2 **A Quarter 1 Treasury Report** – This provides details of the actual prudential and treasury indicators for the first quarter of 2024-25.

4.4.3 **A Mid-Year Treasury Management Report** – This will update Members on the progress of the strategy, including loan charges, prudential indicators, and any proposed change to the strategy or whether any policies require revision.

4.4.4 **A Quarter 3 Treasury Report** – This provides details of the actual prudential and treasury indicators for the third quarter of 2024-25.

4.4.5 **An Annual Treasury Report** – This provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

Above 4 reports are presented to the Audit and Governance Panel for scrutiny and then to Cabinetl for approval.

5. Legal and Procurement Implications

5.1 There are no legal implications arising from this report.

5.2 There are no procurement implications arising from this report.

6. Financial Implications

6.1 There are no resources implications arising from this report other than those resulting from the delivery of the proposed Strategy as contained in Appendix 1.

7. Human Resources Implications

7.1 Not applicable.

8. Risk

8.1 ***Risk Implications of Adopting the Recommendations***

8.1.1 There are no risks associated with adopting the recommendations.

8.2 ***Risk Implications of Rejecting the Recommendations***

8.2.1 The Council would not be compliant with the requirements of the CIPFA Treasury Management Code of Practice.

9. Equalities

9.1 The proposals in this report have been assessed through the Equality Impact Assessment Scoping process. There are no significant potential positive or negative equality impacts of agreeing the recommendations and therefore an Equalities Impact Assessment is not required. A copy of the Equalities Scoping Assessment is attached as Appendix 2.

10. Sustainable Development Implications

10.1 ***Considering Strategic Environmental Assessment (SEA)* -** This report does not propose or seek approval for a plan, policy, programme or strategy or document otherwise described which could be considered to constitute a plan, programme, policy or strategy.

11. Options Appraisal

11.1 An options appraisal has not been carried out in relation to the subject matter of this report.

12. Link to Council Plan

12.1 The matters referred to in this report contribute to Priority 4 of the Council Plan: Efficient and effective enabling services.

13. Results of Consultation

13.1 There has been no public consultation on the contents of this report.

13.2 Consultation has taken place with Councillor Ian Davis, Portfolio Holder for Finance, Human Resources and ICT, and the contents of this report reflect any feedback provided.

14. Next Steps for Decision Tracking Purposes

14.1 If the recommendations above are approved by Members, the Head of Finance, ICT and Procurement will ensure that all necessary steps are taken to ensure full implementation of the decision within the following timescales, with the completion status reported to the Cabinet in the ‘Council and Cabinet Decision Log’ at each of its meetings until such time as the decision is fully implemented:

Implementation	***Due date***	***Managed by***
The approved strategy will be incorporated into the 2024/25 treasury and investment planning and management process	1 April 2024	Head of Finance, ICT and Procurement

Background Papers	**2021 revised CIPFA Treasury Management Code and Prudential Code** **CIPFA Code of Practice for Treasury Management in the Public Services** **CIPFA The Prudential Code for Capital Finance in Local Authorities** **The Local Government Investments (Scotland) Regulations 2010** **The Local Authority (Capital Finance and Accounting) (Scotland) Regulations 2016**
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Date: 27 February 2024

south AYRSHIRE COUNCIL
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Appendix 1

Treasury Management And Investment Strategy 2024/25

March 2024

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Index

Introduction

2021 revised CIPFA (Chartered Institute of Public Finance and Accountancy) Treasury Management Code and Prudential Code – changes which will impact on future TMSS/AIS reports and the risk management framework

CIPFA published the revised Codes on 20th December 2021 and has stated that revisions needed to be included in the reporting framework from the 2023/24 financial year onwards. This Authority, therefore, has to have regard to these Codes of Practice when it prepares the Treasury Management Strategy Statement and Annual Investment Strategy, and related reports during the financial year, which are taken to Full Council for approval.

The revised Treasury Management Code requires all investments and investment income to be attributed to one of the following three purposes: -

Treasury management

Arising from the organisation's cash flows or treasury risk management activity, this type of investment represents balances which are only held until the cash is required for use. Treasury investments may also arise from other treasury risk management activity which seeks to prudently manage the risks, costs or income relating to existing or forecast debt or treasury investments.

Service delivery

Investments held primarily and directly for the delivery of public services including housing, regeneration and local infrastructure. Returns on this category of investment which are funded by borrowing are permitted only in cases where the income is "either related to the financial viability of the project in question or otherwise incidental to the primary purpose."

Commercial return

Investments held primarily for financial return with no treasury management or direct service provision purpose. Risks on such investments should be proportionate to an authority's financial capacity – i.e., that 'plausible losses' could be absorbed in budgets or reserves without unmanageable detriment to local services. An authority must not borrow to invest primarily for financial return.

The revised Treasury Management Code requires the following: -

1. **A liability benchmark treasury indicator** to support the financing risk management of the capital financing requirement; this is to be shown in chart form for a minimum of ten years, with material differences between the liability benchmark and actual loans to be explained;

2. **Long-term treasury investments**, (including pooled funds), are to be classed as commercial investments unless justified by a cash flow business case;

3. **Pooled funds** are to be included in the indicator for principal sums maturing in years beyond the initial budget year;

4. A **knowledge and skills register** for officers and members involved in the treasury management function - to be proportionate to the size and complexity of the treasury management.

5. **Reporting to members is to be undertaken quarterly**. Specifically, the Chief Finance Officer (CFO) is required to establish procedures to monitor and report performance against

all forward-looking prudential indicators at least quarterly. The CFO is expected to establish a measurement and reporting process that highlights significant actual or forecast deviations from the approved indicators. However, monitoring of prudential indicators, including forecast debt and investments, is not required to be taken to Full Council and should be reported to Audit and Governance Panel.

6. **Environmental, social and governance (ESG)** issues to be addressed within the authority's treasury management policies and practices (TMP1).

The main requirements of the Prudential Code relating to service and commercial investments are: -

1. The risks associated with service and commercial investments should be proportionate to their financial capacity – i.e. that plausible losses could be absorbed in budgets or reserves without unmanageable detriment to local services;

2. An authority must not borrow to invest for the primary purpose of commercial return;

3. It is not prudent for local authorities to make any investment or spending decision that will increase the CFR, and so may lead to new borrowing, unless directly and primarily related to the functions of the authority, and where any commercial returns are either related to the financial viability of the project in question or otherwise incidental to the primary purpose;

4. An annual review should be conducted to evaluate whether commercial investments should be sold to release funds to finance new capital expenditure or refinance maturing debt;

5. A prudential indicator is required for the net income from commercial and service investments as a proportion of the net revenue stream;

6. Create new Investment Management Practices to manage risks associated with non-treasury investments, (like the current Treasury Management Practices).

The Annual Investment Strategy should include: -

1. The authority's approach to investments for service or commercial purposes (together referred to as non-treasury investments), including defining the authority's objectives, risk appetite and risk management in respect of these investments, and processes ensuring effective due diligence;

2. An assessment of affordability, prudence, and proportionality in respect of the authority's overall financial capacity (i.e. whether plausible losses could be absorbed in budgets or reserves without unmanageable detriment to local services);

3. Details of financial and other risks of undertaking investments for service or commercial purposes and how these are managed;

4. Limits on total investments for service purposes and for commercial purposes respectively (consistent with any limits required by other statutory guidance on investments);

5. Requirements for independent and expert advice and scrutiny arrangements (while business cases may provide some of this material, the information contained in them will need to be periodically re-evaluated to inform the authority's overall strategy);

6. State compliance with paragraph 51 of the Prudential Code in relation to investments for commercial purposes, in particular the requirement that an authority must not borrow to invest primarily for financial return;

As this Treasury Management Strategy Statement and Annual Investment Strategy deals solely with treasury management investments, the categories of service delivery and commercial investments will be dealt with as part of the Capital Strategy report. South Ayrshire Council do not now have any commercial investments and do not plan to do so within the next 3 years of this report.

CIPFA defines treasury management as:

'The management of the local authority's borrowing, 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. '

The background for the requirements strategy is set out in the in the undernoted legislation:

All treasury management reports written during the financial year of 2024/25 will need to consider the under-noted:

1. CIPFA (Chartered Institute of Public Finance and Accountancy) Treasury Management Codes of Practice and Guidance notes 2023/24;
2. 2021 revised CIPFA Treasury Management Code and Prudential Code
3. CIPFA Prudential Code for Capital Finance in Local Authorities revised 2017;
4. CIPFA Prudential Code for Capital Finance in Local Authorities - Guidance Notes for practitioners 2018;
5. Finance Circular 7/2016, which covered Loans Fund Accounting and the revised requirements around loans fund repayments;
6. Statutory investment regulations; and
7. Statutory guidance for annual loan repayments.

South Ayrshire Council's Treasury Management and Investment Strategy for 2024/25 is set out in the following Sections 1 to 4 plus Annex A and B.

Treasury Management and Investment Strategy 2024/25

Section 1 - Capital Plans and Prudential Indicators 2022/23 to 2026/27

The Council's capital expenditure plans and delivery are the key drivers of treasury management activity. The capital expenditure plans are reflected in prudential indicators, which are designed to assist in providing Members with an overview of the Council's capital plans.

1.1 ***Capital Expenditure*** **-** This prudential indicator is a summary of the Council's capital expenditure plans, both those agreed previously, and those forming part of the budget cycle.

Members are asked to approve the capital expenditure forecasts:

Capital Expenditure	***2022/23 Actual £'000***	***2023/24 Projected £'000***	***2024/25 Estimate £'000***	***2025/26 Estimate £'000***	***2026/27 Estimate £'000***
General Services	90,749	61,671	102,570	94,223	81,358
HRA	28,315	46,550	95,619	42,997	26,741
Total	**119,064**	**108,221**	**198,189**	**137,220**	**108,099**
Financed by:					
Government Grant/Other	(22,818)	(22,368)	(16,939)	(11,757)	(10,503)
Capital Receipts/Other	(23,369)	(16,435)	(39,760)	(35,976)	(8,412)
Net financing need for the year – (Borrowing)	**72,877**	**69,418**	**141,490**	**89,487**	**89,184**

The table above takes in to account the 2022/23 actual and 2023/24 projections for spend and any programme decisions that impact on future years. The table also summarises the capital expenditure plans and how these plans are being financed by capital or revenue resources.

Any shortfall of resources results in a funding requirement (borrowing).

Other Long-Term Liabilities **(OLTL) -** The above summarised capital plan excludes other long-term liabilities, such as PFI and leasing arrangements which already include borrowing instruments.

The CIPFA LAASAC Local Authority Accounting Code Board has deferred implementation of IFRS16 until 1st April 2024, the 2024/25 financial year.

This template has no alterations to deal with bringing currently off-balance sheet leased assets onto the balance sheet: this will, though, be a requirement for closing of the accounts for 2024/25.

1.2 ***Borrowing and Capital Financing Requirement***

The second prudential indicator is the Council's Capital Financing Requirement (CFR). The CFR is simply the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is a measure of the Authority's indebtedness and so its underlying borrowing need.

Any capital expenditure, which has not immediately been paid for, will increase the CFR.

The CFR does not increase indefinitely, as prudent annual repayments from revenue need to be made which reflect the useful life of capital assets that are financed by borrowing.

The CFR includes any other long-term liabilities (e.g. PFI schemes and finance leases). Whilst these schemes increase the CFR and therefore the Council's borrowing requirement, these types of schemes include a borrowing facility and so the Council does not require borrowing separately for these schemes.

Full Council agreed a report in meeting of 15th December 2022 on PPP Service Concession Arrangement Flexibilities. The reprofiling of the debt liability repayments increased the Capital Financing Requirement (CFR) by £21.718m as of 1 April 2022. The Council made this adjustment in financial year 2022/23.

The increase in the CFR will continue to be reduced by the revised repayments after each SAC (South Ayrshire Council) contract has expired until the end of the revised period. This has now been incorporated into the revised Prudential indicators as appropriate. Based on above the Council has £85.9m of such schemes within the CFR as of 31 March 2024.

The table below shows the projected and estimated movement in the CFR based on current capital expenditure plans.

Capital Financing Requirement	***2022/23 Actual £'000***	***2023/24 Projected £'000***	***2024/25 Estimate £'000***	***2025/26 Estimate £'000***	***2026/27 Estimate £'000***
General Services	407,333	436,059	481,816	524,885	579,648
HRA	77,275	104,710	171,136	210,055	231,877
CFR	**484,608**	**540,769**	**652,952**	**734,940**	**811,525**
Other Long-Term Liabilities	(91,951)	(88,023)	(84,047)	(79,996)	(75,933)
Underlying Borrowing Need	**392,657**	**452,746**	**568,905**	**654,944**	**735,592**

Movement in underlying borrowing need	**89,428**	**60,089**	**116,159**	**86,039**	**80,648**
Movement in underlying borrowing need represented by					
Net financing need for the year	72,877	69,418	141,490	89,485	89,184
PPP Adjustment	23,789	2,077	2,026	1,994	1,895
In Year Slippage	0	(3,471)	(18,273)	5,059	806
Less scheduled debt amortisation	(7,238)	(7,935)	(9,084)	(10,499)	(11,237)
Movement in underlying borrowing need.	**89,428**	**60,089**	**116,159**	**86,039**	**80,648**

A key aspect of the regulatory and professional guidance is that elected members are aware of the size and scope of any commercial activity in relation to the authority's overall financial position. The capital expenditure figures shown in 1.1 and the details above demonstrate the scope of this activity and, by approving these figures; consider the scale proportionate to the Authority's remaining activity.

1.3 ***Liability Benchmark***

The Authority is required to estimate and measure the Liability Benchmark (LB) for the forthcoming financial year and the following two financial years, as a minimum.

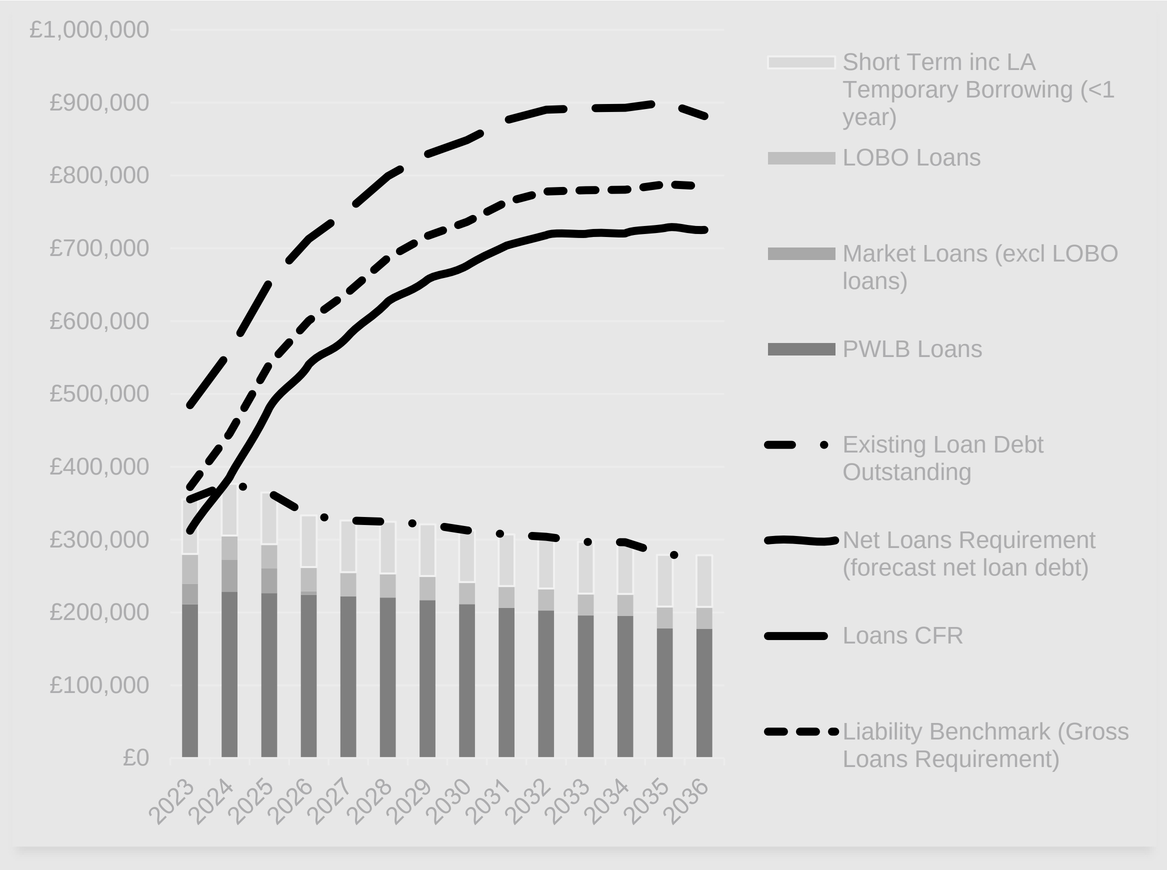
CIPFA notes on page 13 of the 2021 TM Code: "The liability benchmark should be analysed as part of the annual treasury management strategy, and any substantial mismatches between actual loan debt outstanding and the liability benchmark should be explained. Any years where actual loans are less than the benchmark indicate a future borrowing requirement; any years where actual loans outstanding exceed the benchmark represent an overborrowed position, which will result in excess cash requiring investment (unless any currently unknown future borrowing plans increase the benchmark loan debt requirement). The treasury strategy should explain how the treasury risks inherent in these mismatched positions will be managed."

There are four components to the LB:-

1. **Existing loan debt outstanding**: the Authority's existing loans that are still outstanding in future years.
2. **Loans CFR**: this is calculated in accordance with the loans CFR definition in the Prudential Code and projected into the future based on approved prudential borrowing and planned Loans Fund advances/Loans Fund principal repayments. (Note only approved prudential borrowing is included).

3. **Net loans requirement:** this will show the Authority's gross loan debt less treasury management investments at the last financial year-end, projected into the future and based on its approved prudential borrowing, planned Loans Fund principal repayments and any other major cash flows forecast.

4. **Liability benchmark** (or gross loans requirement): this equals net loans requirement plus short-term liquidity allowance. The graph below shows the projected movement in the liability benchmark.



This chart shows that South Ayrshire have a significant borrowing requirement over the coming years, as highlighted by the middle-dashed line, which is a risk. However, this borrowing is being monitored to determine timescales and interest rate risk factors and borrowing will only be taken if required.

1.4 *Capital Affordability Indicators*

The previous section covers the overall capital and borrowing prudential indicators, but within this framework prudential indicators are required to assess the affordability of the capital investment plans. These provide an indication of the impact of the capital investment plans on the Council's overall finances.

1.4.1 **Actual and Estimates of the Ratio of Financing Costs to Net Revenue Stream**

This indicator identifies the trend in the cost of capital (borrowing and other long-term obligation costs net of investment income) against the net revenue stream of the Council.

	2022/23 Actual %	2023/24 Projected %	2024/25 Estimate %	2025/26 Estimate %	2026/27 Estimate %
General Services	5.43	5.85	6.04	6.57	7.03
HRA	10.69	12.26	19.86	26.69	29.45
Total Net Revenue Stream to Total Financing Costs	6.03	6.54	7.35	8.41	9.05

1.4.2 **HRA Debt Ratios**

£'000	2022/23 Actual £'000	2023/24 Projected £'000	2024/25 Estimate £'000	2025/26 Estimate £'000	2026/27 Estimate £'000
HRA debt	76,839	104,274	170,699	209,618	231,441
HRA revenues	34,147	33,522	33,635	34,995	37,363
Ratio of debt to revenues	2.25	3.11	5.08	5.99	6.19

£'000	2022/23 Actual £'000	2023/24 Projected £'000	2024/25 Estimate £'000	2025/26 Estimate £'000	2026/27 Estimate £'000
HRA debt	76,839	104,274	170,699	209,618	231,441
Number of HRA dwellings	8,055	8,122	8,251	8,484	8,647
Debt per dwelling	£9,539	£12,838	£20,688	£20,707	£26,765

1.4.3 Significant investment is planned in the next few years in the HRA major component replacement programme and the new build programme which has increased the debt per dwelling figure in the table above.

1.4.4 All of the above indicators at 1.4 are designed to indicate the financing costs of the Council's investment plans against its revenues and that of the HRA. The Code does not provide target figures and states that these indicators are not comparable between authorities given the wide-ranging variations in Council's historic debt and borrowing and investment plans.

Section 2 - Treasury Management

The capital expenditure plans set out in Section 1 provide details of the service activity of the Council. The treasury management function ensures that the Council's cash is organised in accordance with the the relevant professional codes, so that sufficient cash is available to meet this service activity. This will involve both the management of the cash flow and, where capital plans require, the arrangement of appropriate borrowing facilities. The strategy covers the relevant treasury / prudential indicators, the current and projected debt positions and the annual investment strategy.

2.1 *Current Portfolio Position*

The Council's treasury portfolio position as at 31 March 2023, with forward projections are summarised below. The table shows the actual external debt (the treasury management operations), against the underlying capital borrowing need (the Capital Financing Requirement - CFR), highlighting any over or under borrowing.

External Debt	***2022/23 Actual £'000***	***2023/24 Projected £'000***	***2024/25 Estimate £'000***	***2025/26 Estimate £'000***	***2026/27 Estimate £'000***
Opening Debt on 1 April	289,434	355,385	404,160	513,174	602,255
Long Term Debt Maturities	(83,049)	(78,725)	(11,986)	(31,419)	(6,919)
New External Debt	149,000	127,500	121,000	120,500	93,000
External Debt	**355,385**	**404,160**	**513,174**	**602,255**	**688,336**
Other long-term liabilities (PPP + Finance Leases)	91,951	88,023	84,047	79,996	75,933
Actual Debt on 31 March	**447,336**	**492,183**	**597,221**	**682,251**	**764,269**
The Capital Financing Requirement	**484,608**	**540,769**	**652,952**	**734,940**	**811,525**
Under / (Over) Borrowing	**37,272**	**48,586**	**55,731**	**52,689**	**47,256**

External Debt	**355,385**	**404,160**	**513,174**	**602,255**	**688,336**
Cash Investments	(43,155)	(35,000)	(35,000)	(35,000)	(35,000)
Net External Debt	**312,230**	**369,160**	**478,174**	**567,255**	**653,336**

Within the prudential indicators, there are several key indicators to ensure that the Council operates its activities within well-defined limits. One of these is that the Council needs to ensure that its gross debt does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2023/24 and the following two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes.

The Head of Finance, ICT and Procurement reports that the Council complied with this prudential indicator in the current year. This view considers current commitments, existing plans, and the proposals in the budget report.

2.2 ***Treasury Indicators: Limits to Borrowing Activity***

2.2.1 **The Operational Boundary** - this is the limit beyond which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt and the Council's under/over borrowed position.

Operational Boundary	***2023/24 £'000***	***2024/25 £'000***	***2025/26 £'000***	***2026/27 £'000***
Debt	405,000	515,000	605,000	690,000
Other long-term liabilities	140,000	145,000	140,000	135,000
Total	**545,000**	**660,000**	**745,000**	**825,000**

2.2.2 **The Authorised Limit for External Borrowing** - a further key prudential indicator represents a control on the maximum level of external debt. This represents a limit beyond which external debt is prohibited, and this limit needs to be set or revised by the full Council. It reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

This is the statutory limit (Affordable Capital Expenditure Limit) determined under section 35(1) of the Local Government in Scotland Act 2003. The Government retains an option to control either the total of all Councils' plans, or those of a specific Council, although this power has not yet been exercised.

Authorised limit	***2023/24 £'000***	***2024/25 £'000***	***2025/26 £'000***	***2026/27 £'000***
Debt	460,000	560,000	670,000	710,000
Other long-term liabilities	140,000	145,000	140,000	135,000
Total	**600,000**	**705,000**	**810,000**	**845,000**

2.2.3 The under-noted graph shows the relationship between the 4 main components of capital financing:

a) Authorised Limit (Debt);

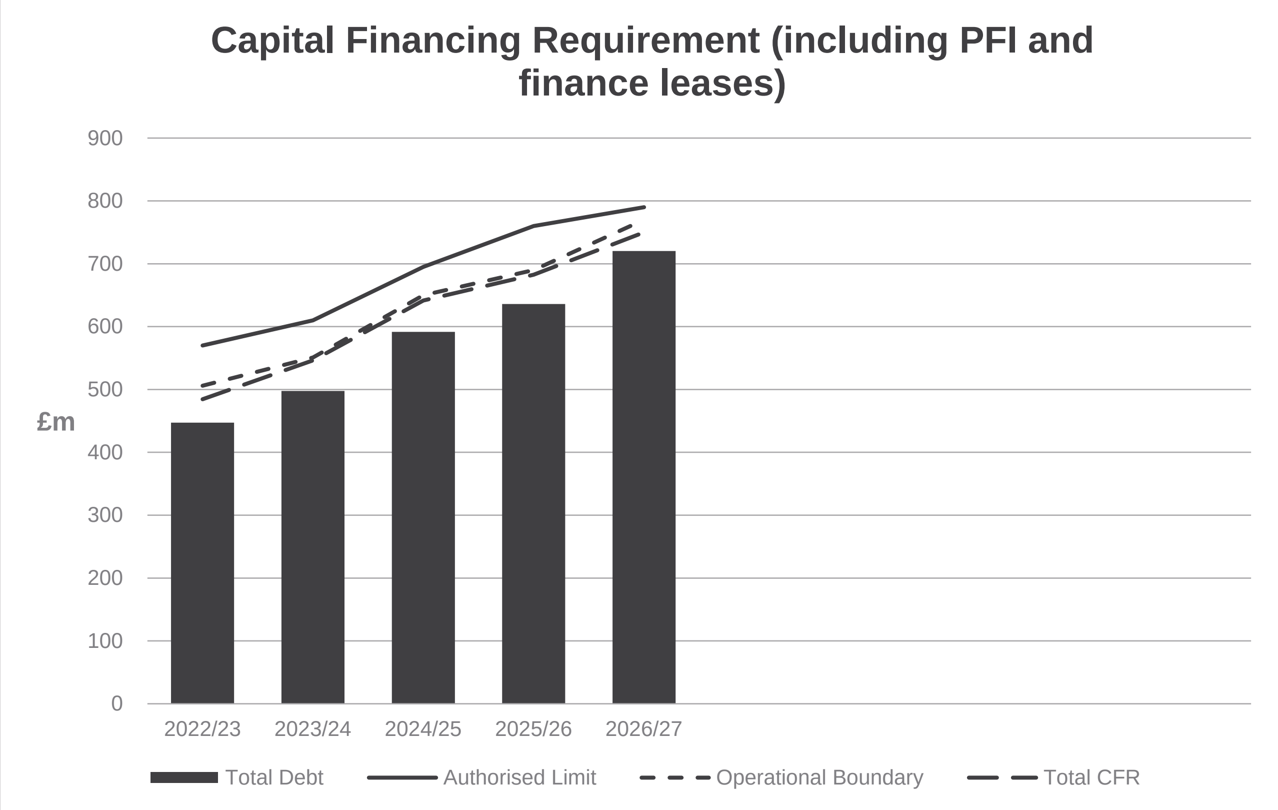
b) Operational Boundary (Debt);

c) Capital Financing Requirement; and

d) Actual External Debt

The graph below shows the increasing trend in the substantial capital investment plans of the Council in the medium term, and therefore increasing debt and capital financing requirements going forward.

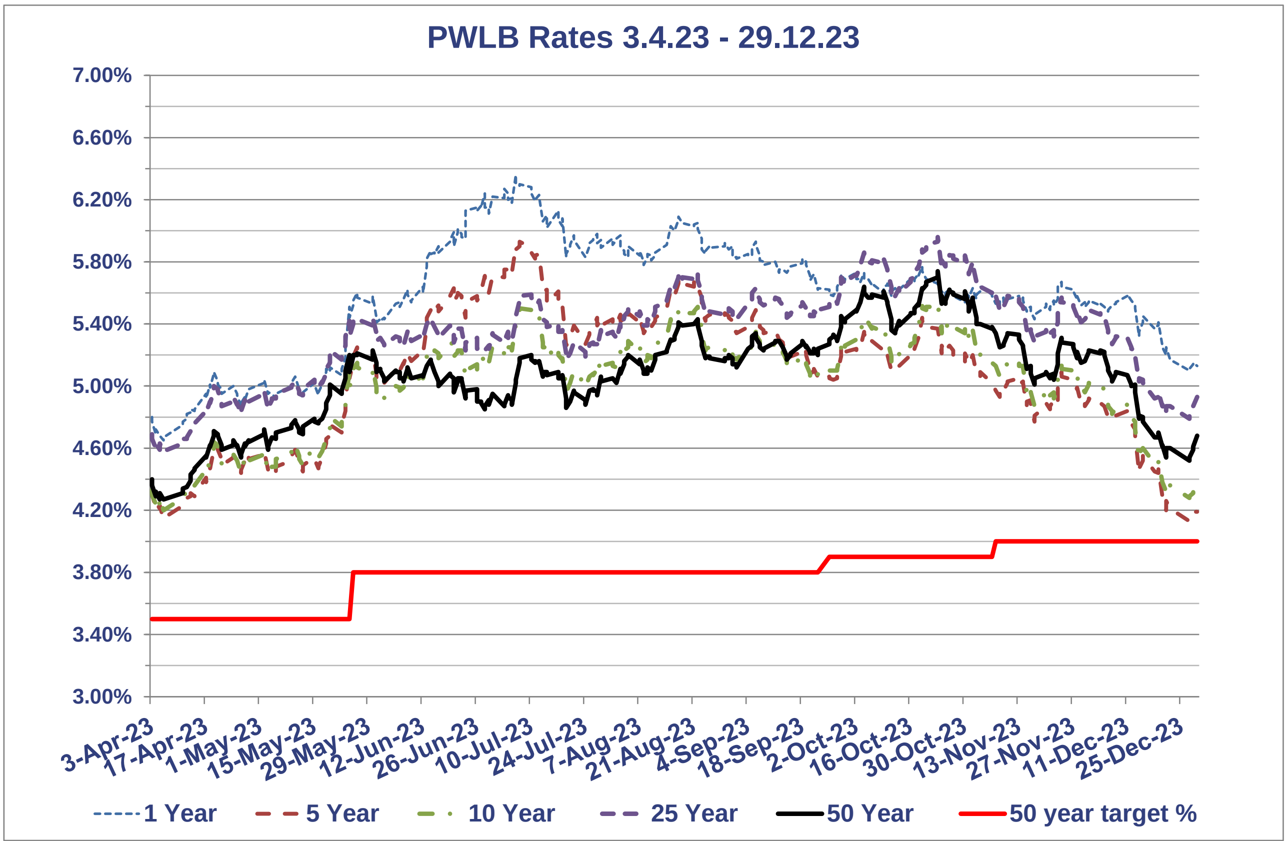
Both the authorised debt and operational boundary indicators include a margin for the balance of other financing arrangements such as PPP schemes.



2.3 ***Economic Commentary***

- The third quarter of 2023/24 saw:
  - A 0.3% m/m decline in real Gross Domestic Product (GDP) in October, potentially partly due to unseasonably wet weather, but also due to the ongoing effect from higher interest rates. Growth for the second quarter, ending 30th September, was revised downwards to -0.1% and growth on an annual basis was also revised downwards, to 0.3%;
  - A sharp fall in wage growth, with the headline 3myy rate declining from 8.0% in September to 7.2% in October, although the ONS (Office for National Statistics) rate of unemployment has remained low at 4.2%;
  - Consumer Price Index (CPI) inflation continuing a downward trajectory, from 8.7% in April to 4.6% in October, then again to 3.9% in November, with a slight increase to 4.0% for months of December and January.
  - Core CPI inflation decreasing from April and May's 31 years' high of 7.1% to 5.1% in January 2024, which was the lowest rate since January 2022.
  - The Bank of England holding Bank Rate at 5.25% from November 2023 to January 2024.
  - A steady fall in 10-year gilt yields as investors revised their interest rate expectations lower.
- The 0.3% m/m fall in retail sales volumes in October means that after contracting by 1.0% q/q (which was downwardly revised from -0.8% q/q) in Q2, retail activity remained weak at the start of Q3. That suggests higher interest rates are taking a bigger toll on real consumer spending.

- Higher interest rates have filtered through the financial channels and weakened the housing market but, overall, it remains resilient with the Halifax house price index recently pointing to a 1.7% year on year increase whilst Nationwide's December data pointed to a -1.8% year on year decrease. However, the full weakness in real consumer spending and real business investment has yet to come as currently it is estimated that around two thirds to a half of the impact of higher interest rates on household interest payments has yet to be felt.
- Overall, we expect real GDP growth to remain subdued throughout 2024 as the effect from higher interest rates is protracted but a fading of the cost-of-living crisis and interest rate cuts in the second half of 2024 will support a recovery in GDP growth in 2025.
- The labour market remains tight by historical standards, but the sharp fall in wage growth seen in October will reinforce the growing belief in markets that interest rates will be cut mid-2024.
- CPI inflation fell from 6.7% in September to 4.6% in October, and then again to 3.9% in November. Both these falls were bigger than expected and there are clear signs of easing in domestic inflationary pressures.
- The Bank of England monetary policy committee (MPC) meeting in December, left interest rates at 5.25% for the third time in a row and pushed back against the prospect of near-term interest rate cuts. The MPC maintained its tightening bias saying that "further tightening in monetary policy would be required if there were evidence of more persistent inflationary pressures." And it continued by, saying that policy will be "sufficiently restrictive for sufficiently long" and that "monetary policy is likely to need to be restrictive for an extended period of time." Meaning that the MPC is not yet willing to endorse investors' expectations that rates will be cut as soon as May 2024.
- Looking ahead, Capital Economics forecast that the recent downward trends in CPI and core inflation will pause over the next few months before starting to decline more decisively again in February. This is the reasoning that the Bank of England will not feel comfortable cutting interest rates until the second half of 2024.
- The fall in UK (United Kingdom) market interest rate expectations in December has driven most of the decline in 10-year gilt yields, which have fallen in line with 10-year US (United States) Treasury and euro-zone yields. 10-year gilt yields have fallen from 4.68% in October 2023 to around 3.70% at the time of writing, with further declines if falling inflation is maintained.
- Investors' growing expectations that the Federal Reserve will cut interest rates soon has led to an improvement in risk sentiment, which has boosted the pound and other risky assets. In addition, the rise in the pound, from $1.21 in November to $1.27 now, has also been supported by the recent relative decline in UK wholesale gas prices.



HIGH/LOW/AVERAGE PWLB RATES FOR 3.4.23 – 29.12.23

	1 Year	5 Year	10 Year	25 Year	50 Year
Low	4.65%	4.13%	4.20%	4.58%	4.27%
Date	06/04/2023	27/12/2023	06/04/2023	06/04/2023	05/04/2023
High	6.36%	5.93%	5.53%	5.96%	5.74%
Date	06/07/2023	07/07/2023	23/10/2023	23/10/2023	23/10/2023
Average	5.60%	5.09%	5.03%	5.35%	5.08%
Spread	1.71%	1.80%	1.33%	1.38%	1.47%

MPC meetings 2nd November, 14th December 2023 and 1st February 2024

- On 2nd November, the Bank of England's Monetary Policy Committee (MPC) voted to keep Bank Rate on hold at 5.25%, and on 14th December reiterated that view. Both increases reflected a split vote, the latter by 6 votes to 3, with the minority grouping voting for an increase of 0.25% as concerns about inflation remained in place.
- The MPC meeting held on 1st February kept rates on hold for the fourth time in a row, pushing back against the prospect of near-term interest rate cuts. The vote in favour of keeping rates on hold was 6-3. There were six members that voted for rates to stay on hold, two that voted for a 25bps hike and one that voted for a 25bps cut.
- The Bank of England stated the policy will remain sufficiently restrictive for an extended period. It continues to place weight on services inflation and wage growth, assessing it won't fall as fast as CPI inflation. Moreover, the forecast is that inflation would fall to the 2% target in Q2 2024 (compared to Q4 2025 previously) and that the upside risks from domestic drivers have lessened, however it expects inflation to rebound in Q3 2024 and to be above the 2% target for the bulk of the next three years.
- Estimates are now that the first Bank Rate cut will not happen till the August 2024 MPC.

- In addition, what happens outside of the UK is also critical to movement in gilt yields. The US Federal Open Market Committee (FOMC) has kept short-term rates in the range of 5.25%-5.50%, whilst the European Central Bank (ECB) has moved its Deposit rate to a probable peak of 4%. Markets currently expect both central banks to start cutting rates in 2024.

2.4 Prospects for Interest Rates

The Council has appointed Link Group as its treasury advisor and part of their service is to assist the Authority to formulate a view on interest rates. Link provided the following forecasts on 08 January 2024. These are forecasts for Bank Rate, average earnings and PWLB certainty rates, gilt yields plus 80 bps.

Link Group Interest Rate View 08.01.24													
	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27
BANK RATE	5.25	5.25	4.75	4.25	3.75	3.25	3.00	3.00	3.00	3.00	3.00	3.00	3.00
3 month ave earnings	5.30	5.30	4.80	4.30	3.80	3.30	3.00	3.00	3.00	3.00	3.00	3.00	3.00
6 month ave earnings	5.20	5.10	4.60	4.10	3.70	3.30	3.10	3.10	3.10	3.10	3.10	3.10	3.10
12 month ave earnings	5.00	4.90	4.40	3.90	3.60	3.20	3.10	3.10	3.10	3.10	3.10	3.20	3.20
5 yr PWLB	4.50	4.40	4.30	4.20	4.10	4.00	3.80	3.70	3.60	3.60	3.50	3.50	3.50
10 yr PWLB	4.70	4.50	4.40	4.30	4.20	4.10	4.00	3.90	3.80	3.70	3.70	3.70	3.70
25 yr PWLB	5.20	5.10	4.90	4.80	4.60	4.40	4.30	4.20	4.20	4.10	4.10	4.10	4.10
50 yr PWLB	5.00	4.90	4.70	4.60	4.40	4.20	4.10	4.00	4.00	3.90	3.90	3.90	3.90

- Our central forecast for interest rates was updated on 8 January and reflected a view that the MPC would be keen to further demonstrate its anti-inflation credentials by keeping Bank Rate at 5.25% until at least H2 2024. The expectation is rate cuts to start when both the CPI inflation and wage/employment data are supportive of such a move, and when there is a likelihood of the overall economy enduring at least a slowdown or mild recession over the coming months (although most recent GDP releases have surprised with their on-going robustness).
- Timing on this matter will remain one of fine judgment: cut too soon, and inflationary pressures may well build up further; cut too late and any downturn or recession may be prolonged.
- In the upcoming months, forecasts will be guided not only by economic data releases and clarifications from the MPC over its monetary policies and the Government over its fiscal policies, but also international factors such as policy development in the US and Europe, the provision of fresh support packages to support the recovery in China as well as the on-going conflict between Russia and Ukraine, and Gaza and Israel.

PWLB RATES

- The short and medium part of the gilt curve has rallied since the start of November as markets price in a quicker reduction in Bank Rate through 2024 and 2025. This reflects market confidence in inflation falling back in a similar manner to that already seen in the US and the Euro-zone. At the time of writing there is c70 basis points difference between the 5- and 50-year parts of the curve.

The balance of risks to the UK economy: -

- The overall balance of risks to economic growth in the UK is even.

Downside risks to current forecasts for UK (United Kingdom) gilt yields and PWLB rates include: -

- Labour and supply shortages prove more enduring and disruptive and depress economic activity (accepting that in the near-term this is also an upside risk to inflation and, thus, could keep gilt yields high for longer).

- The Bank of England has increased Bank Rate too fast and too far over recent months, and subsequently brings about a deeper and longer UK recession than we currently anticipate.

- Geopolitical risks, for example in Ukraine/Russia, the Middle East, China/Taiwan/US, Iran, and North Korea, which could lead to increasing safe-haven flows.

Upside risks to current forecasts for UK gilt yields and PWLB rates: -

- Despite the tightening in Bank Rate to 5.25%, the Bank of England allows inflationary pressures to remain elevated for a prolonged period within the UK economy, which then necessitates Bank Rate staying higher for longer than we currently project.

- The pound weakens because of a lack of confidence in the UK Government's pre-election fiscal policies, which may prove inflationary, resulting in investors pricing in a risk premium for holding UK sovereign debt.

- Projected gilt issuance, inclusive of natural maturities and QT, could be too much for the markets to comfortably digest without higher yields compensating.

The suggested budgeted earnings rates for investments up to about three months' duration in each financial year are set out below.

Average earnings in each year	Now	Previously
2023/24 (residual)	5.30%	5.30%
2024/25	4.55%	4.70%
2025/26	3.10%	3.20%
2026/27	3.00%	3.00%
2027/28	3.25%	3.25%
2028/29	3.25%	3.25%
Years 6 to 10	3.25%	3.25%
Years 10+	3.25%	3.25%

As there are so many variables at this time, caution must be exercised in respect of all interest rate forecasts. The interest rate forecast for Bank Rate is in steps of 25 bps, whereas PWLB forecasts have been rounded to the nearest 10 bps and are central forecasts within bands of + / - 25 bps.

2.5 *Borrowing Strategy*

At the time of writing this report, the Council is estimated to have an under-borrowed position at the end of 2023/24 of £48,586m, (around 10.7% of the total underlying borrowing requirement). This would mean that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with external loan debt and means that an element of internal resources, cash and revenue surpluses have been used to finance capital expenditure. This strategy is prudent even although investment returns are on the increase, counterparty risk is still an issue that needs to be considered. Given the under-borrowed position is 10.7% of the borrowing requirement it removes an element of interest rate risk.

During **2024/25** it is estimated that the Council and HRA will have additional borrowing requirements of **£140,839m**.

The strategy is to fund most of this requirement from long term external borrowing of **£121m** whilst reducing the under-borrowed position to around 9.7% of the borrowing requirement. Although a reduction on the current year position, this remains a prudent strategy in the current interest rate environment and also allows flexibility in taking a pragmatic approach in terms of the pace of the major capital spend in 2024/25.

The treasury team are monitoring longer term interest rate forecasts on a regular basis to assess timing of longer term borrowing; whilst still minimising the cost of carrying any new borrowing prior to the loans actually being required.

Whilst the under-borrowed position remains a minimal risk, the significant borrowing requirements in 2024/25 and the level of temporary borrowing will require close monitoring.

Against this background and the risks within the economic forecast, caution will be adopted with the 2024/25 treasury operations. The Head of Finance, ICT and Procurement will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

The estimates of borrowing required are set out in the under-noted table:

New Borrowing (Year)	***General Services £'000***	***HRA £'000***	***Total £'000***
2024/25	61,134	79,705	140,839
2025/26	51,452	38,035	89,487
2026/27	66,845	22,989	89,834
2027/28	13,867	31,621	45,488
2028/27	4,324	25,069	29,393
Total 5 Yr Borrowing	**197,622**	**197,419**	**395,041**

It is emphasised that a pragmatic approach will be taken when considering the timing of this borrowing externally in the light of prevailing interest rates, the overall treasury strategy, cost of carry, and in particular the out-turn of capital expenditure as the projects are delivered in 2024/25 and 2025/26:

- Iif it was felt that there was a significant risk of a sharp FALL in borrowing rates, then borrowing will be postponed.

- if it was felt that there was a significant risk of a much sharper RISE in borrowing rates than that currently forecast, fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.

Any decisions on new borrowing will be reported to Members within the mid-year Treasury Report or the end of year out-turn report.

2.5.1 **Treasury Management Limits on Activity**

Maturity structure of borrowing. These gross limits are set to reduce the Council's exposure to large, fixed rate sums falling due for refinancing.

Maturity Structure of Fixed Interest Rate Borrowing		
	Lower	**Upper**
Under 12 months	0.00%	25%
1 – 2 years	0.00%	25%
2 – 5 years	0.00%	50%
5 – 10 years	0.00%	75%
10 years and above	0.00%	90%

2.6 ***Statutory Repayment of Loans Fund Advances***

The Council is required to set out its policy for the statutory repayment of loans fund advances prior to the start of the financial year. The repayment of loans fund advances ensures that the Council makes a prudent provision each year to pay off an element of the accumulated loans fund advances made in previous financial years.

A variety of options are provided to Councils and method C below will be the prudent repayment option adopted by the Council.

- **Statutory method**

- **Depreciation method** – annual repayment of loans fund advances will follow standard depreciation accounting procedures;

- **Asset life method** – loans fund advances will be repaid with reference to the life of an asset using either the equal instalment or annuity method;

- **Funding / Income profile method** – loans fund advances will be repaid by reference to an associated income stream.

2.6.1 Finance Circular 7/2016 suggests Councils set out additional disclosures on loans fund account information, so the proposed disclosure note below has been provided to assist. Paragraph 89 of the Finance Circular also states, 'a local authority should set out their policy on the interest rate selected for the annuity calculation'.

The annuity rate applied to the loans fund repayments was based on historic interest rates and is currently 5%. However, under regulation 14 (2) of SSI 2016 No 123, the Council has reviewed and re-assessed the historic annuity rate to ensure that it is a prudent application.

The result of this review suggests that an annuity rate of 5% would remain a prudent approach and provides for principal repayments closely associated with the use of the assets.

There was a recent consultation undertaken by the Scottish Government on proposed amendments to The Local Authority (Capital Finance and Accounting) (Scotland) Regulations 2016 (the 2016 Regulations) which set out the statutory requirements for the borrowing and lending of money and for loans fund accounting, and Local Government Finance Circular 7/2016 which sets out proper accounting practices for loans fund accounting.

The statutory framework differentiates between those advances before 1 April 2023 (covered by Regulation 14 of the 2016 Regulations) and those after 1 April 2023 (covered by the statutory guidance). There are also additional proposals related to capital projects approved after that date. It is therefore helpful to consider the how the proposals apply to three categories of loans fund advances, i.e. advances made:

• before 1 April 2023
• from 1 April 2023 relating to capital projects approved before that date.

• from 1 April 2023 relating to capital projects approved after that date.

Proposals: -

Loans fund advances made before 1 April 2023

Any variation to a loans fund repayment may only be

- calculated on the balance of the loans fund advance in the financial year of variation
- applied to the remaining loans fund repayments from the financial year of variation.

- The repayment period cannot extend beyond the earlier of the remaining useful life of an asset or 50 years from the date of the advance. The decision to vary a loans fund repayment must be taken by the full council and cannot be delegated.

Loans fund advances made from 1 April 2023 relating to capital projects approved before that date

- clarify that where a loans fund advance relates to an asset, the prudent repayment period should usually align to the asset life but may not exceed 50 years.
- confirm that, where an asset life cannot reasonably be attributed to an asset, the loans fund repayment period should align to the period over

which benefit of the expenditure will be provided to the community but may not exceed 50 years and may not subsequently be varied.

- require that any variation to loans fund repayments may only be calculated on the balance of the loans fund advance outstanding in the financial year of variation and may only be applied prospectively.

Loans fund advances made from 1 April 2023 relating to capital projects approved after that date

- Annuity calculation - The use of an annuity calculation (as part of the asset life method of calculating the repayment of the advance) is permitted only where the local authority can evidence that either the flow of benefits of the capital investment or a directly attributable revenue stream will increase over the asset life. Where an annuity is used, the interest rate applied should not exceed the weighted average PWLB borrowing rate of the authority.
- Capital receipts - The use of capital receipts to fund the repayment of advances should be minimised.
- Identification against a specific asset Advances and repayments must be readily identified against a specific asset.
- Repayment on derecognition Advances must be repaid in full on derecognition of the related asset. In the case of obsolescence, a local authority may spread the repayment of the remaining loans fund advance over a maximum period of 5 years to smooth the effect on the General Fund.
- Investment properties A local authority should fully provide for debt taken on to acquire an investment property over the lifetime of the debt.

2.6.2 It is felt these proposals would cause an undue administrative burden to the Council.

This consultation has been responded to by both the council's consultants Link Group, Councils and by the CIPFA Treasury Management Forum.

Any changes that may arise due to this consultation will be reported to Elected members.

Loans Fund Advances to General Fund

Loans Fund	Actual 2022/23 £'000	Est 2023/24 £'000	Est 2024/25 £'000	Est 2025/26 £'000	Est 2026/27£ '000
Opening Balance	226,125	289,526	320,103	367,810	412,938
Add advances	69,290	36,838	54,164	51,858	64,045
Less repayments	(5,889)	(6,261)	(6,457)	(6,730)	(7,115)
Closing Balance	**289,526**	**320,103**	**367,810**	**412,938**	**469,868**

Loans Fund Advances to HRA

Loans Fund	Actual 2022/23 £'000	Est 2023/24 £'000	Est 2024/25 £'000	Est 2025/26 £'000	Est 2026/27 £'000
Opening Balance	74,601	76,839	104,274	170,699	209,618
Add advances	3,587	29,109	69,052	42,688	25,944
Less repayments	(1,349)	(1,674)	(2,627)	(3,769)	(4,121)
Closing Balance	**76,839**	**104,274**	**170,699**	**209,618**	**231,441**

2.7 ***Policy on Borrowing in Advance of Need***

The Council will not borrow more than, or in advance of its needs, purely to profit from the investment of the extra sum borrowed. Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates and will be considered carefully to ensure that value for money can be demonstrated and that the Council can ensure the security of such funds.

Borrowing in advance will be made within the constraints that:

- It will be limited to no more than 20% of the expected increase in borrowing need (CFR) over the three-year planning period; and
- Would not look to borrow more than 12 months in advance of need.

Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through the mid-year or annual reporting arrangements.

2.8 ***Debt Rescheduling***

Rescheduling of current borrowing in our debt portfolio is unlikely to occur as there is still a significant difference between premature redemption rates and new borrowing rates.

The reasons for any rescheduling to take place will include:

1. the generation of cash savings and / or discounted cash flow savings;
2. helping to fulfil the treasury strategy; and
3. enhance the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

If rescheduling is to be undertaken, it will be reported to the Cabinet at the earliest meeting following its action.

2.8.1 **New financial institutions as a source of borrowing and / or types of borrowing**

Currently the PWLB Certainty Rate is set at gilts + 80 basis points for both HRA and non-HRA borrowing. However, consideration may still need to be given to sourcing funding from the following sources for the following reasons:

1. Local authorities (primarily shorter dated maturities out to 3 years or so – still cheaper than the Certainty Rate).
2. Financial institutions (primarily insurance companies and pension funds but also some banks, out of forward dates where the objective is to avoid a ‘cost of carry’ or to achieve refinancing certainty over the next few years).
3. Municipal Bonds Agency (still a viable alternative depending on market circumstances prevailing at the time).

Our advisors Link Group will keep us informed as to the relative merits of each of these alternative funding sources. All rescheduling will be reported to Members in the mid-year or year-end treasury reports.

2.8.2 Approved Sources of Long and Short-term Borrowing

On Balance Sheet	**Fixed**	**Variable**
PWLB	•	•
Municipal Bond Agency	•	•
Local Authorities	•	•
Banks	•	•
Pension Funds	•	•
Insurance Companies	•	•
UK (United Kingdom) Infrastructure Bank	•	•
Market (long-term)	•	•
Market (temporary)	•	•
Market (LOBOs)	•	•
Stock Issues	•	•
Local Temporary	•	•
Local Bonds	•	
Local Authority Bills	•	•
Overdraft		•
Negotiable Bonds	•	•
Internal (capital receipts & revenue balances)	•	•
Commercial Paper	•	
Medium Term Notes	•	
Finance Leases	•	•

Section 3 – Annual Investment Strategy

3.1 *Investment Policy*

The Council's investment policy implements the requirements of the following: -

- Local Government Investments (Scotland) Regulations 2010, (and accompanying Finance Circular 5/2010),
- CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2021 ("the Code")
- CIPFA Treasury Management Guidance Notes 2021

The Council's investment priorities will be security first, portfolio liquidity second and then yield, (return). The Council will aim to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity and with the Council's risk appetite. In the current economic climate, it is considered appropriate maintain a degree of liquidity to cover cash flow needs. However, where appropriate (from an internal as well as external perspective), the Council will also consider the value available in periods up to 12 months with high credit rated financial institutions, as well as wider range fund options

The above regulations and guidance place a high priority on the management of risk. The Council has adopted a prudent approach to managing risk and defines its risk appetite by the following means: -

1. Minimum acceptable credit criteria are applied to generate a list of highly creditworthy counterparties. This also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the short term and long-term ratings.

2. **Other information**: ratings will not be 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. To achieve this consideration the Council will engage with its advisors to maintain a monitor on market pricing such as 'credit default swaps' and overlay that information on top of the credit ratings.

3. **Other information sources** used will include the financial press, share price and other such information pertaining to the banking sector to establish the most robust scrutiny process on the suitability of potential investment counterparties.

4. The Council has defined the list of types of investment instruments that are permitted investments authorised for use in Annex A. Annex B expands on the risks involved in each type of investment and the mitigating controls.

   Specified investments are those with a high level of credit quality and subject to a maturity limit of one year or have less than a year left to run to maturity, if originally, they were classified as being non-specified investments solely due to the maturity period exceeding one year.

Non-specified investments are those with less high credit quality, may be for periods more than one year, and/or are more complex instruments which require greater consideration by members and officers before being authorised for use.

5. Lending limits, (amounts and maturity), for each counterparty will be set through applying the matrix table in paragraph 3.2.

6. Transaction limits are set for each type of investment in appendix 3.2.

7. The Council will set a limit for its investments which are invested for longer than 365 days, (see paragraph 3.4).

8. Investments will only be placed with counterparties from countries with a specified minimum sovereign rating, (see paragraph 3.3).

9. The Council has engaged external consultants, (see paragraph 4.3), to provide expert advice on how to optimise an appropriate balance of security, liquidity, and yield, given the risk appetite of this authority in the context of the expected level of cash balances and need for liquidity throughout the year.

10. All investments will be denominated in sterling.

As a result of the change in accounting standards for 2022/23 under IFRS 9, the council will consider the implications of investment instruments which could result in an adverse movement in the value of the amount invested and resultant charges at the end of the year to the General Fund.

The Council will pursue value for money in treasury management and will monitor the yield from investment income against appropriate benchmarks for investment performance, Regular monitoring of investment performance will be carried out during the year.

3.2 *Credit Worthiness Policy*

3.2.1 The Council applies the credit worthiness service provided by Link Group. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies - Fitch, Moodys and Standard and Poors. The credit ratings of counterparties are supplemented with the following overlays:

- credit watches and credit outlooks from credit rating agencies;
- Credit Default Swaps (CDS) spreads to give early warning of changes in credit ratings; and
- sovereign ratings to select counterparties from only the most creditworthy countries.

This modelling approach combines credit ratings, credit watches and credit outlooks in a weighted scoring system which is then combined with an overlay of Credit Default Swap (CDS) spreads for which the product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Council to determine the duration for investments.

The Council will therefore use counterparties within the following durational bands:

- Yellow 5 years
- Dark Pink 5 years for Ultra short, dated bond funds with a credit score of 1.25
- Light Pink 5 years for Ultra short, dated bond funds with a credit score of 1.5
- Purple 2 years
- Blue 1 year (UK (United Kingdom) part nationalised banks)
- Orange 1 year
- Red 6 months
- Green 100 days
- No Colour not used

3.2.2 The under-noted table sets out the monetary limits that will be applied to each counterparty within each colour on the creditworthiness matrix.

Applying the criteria in the under-noted table has been derived from the Council's current investment activities in terms of funds available for investment, and cash flow requirements. This policy also provides a clearly defined policy on investment activity limits.

	Colour Code (Based on credit information)	***Limit per Counterparty***	***Maximum Maturity Period***
Banks/ Building Societies	Yellow	£25m	5 Years
Banks – (UK Part Nationalised)	Blue	£25m	1 Year
Banks/ Building Societies	Purple	£20m	2 Years
Banks/ Building Societies	Orange	£15m	1 Years
Banks/ Building Societies	Red	£10m	6 months
Banks/ Building Societies	Green	£5m	100 days
Banks/ Building Societies	No Colour	£0	0 days
Council's Corporate Bankers	Orange	£50m	1 Year
Debt Management Account – UK Treasury	AA+	unlimited	6 months
Local / Public Authorities	N/A	£10m	2 Years
Housing Associations	Colour Bands	£5m	As per colour band
Money Market Funds CNAV	AAA	£20m	Liquid
Money Market Funds LVNAV	AAA	£10m	Liquid
Money Market Funds VNAV	AAA	£10m	Liquid
Ultra-short, dated bond funds with a credit score of 1.25	Dark Pink/ AAA	£10m	Liquid
Ultra-short, dated bond funds with a credit score of 1.25	Light Pink/ AAA	£10m	Liquid

The Link creditworthiness service uses a wider array of information other than just primary ratings. Furthermore, by using a risk weighted scoring system, it does not give undue preponderance to just one agency's ratings.

Typically, the minimum credit ratings criteria South Ayrshire uses will be a short-term rating (Fitch or equivalents) of F1 and a long-term rating of A-. There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances, consideration will be given to the complete range of ratings available, or other topical market information, to support their use.

All credit ratings will be monitored daily. South Ayrshire 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 South Ayrshire's minimum criteria, its further use as a new investment will be withdrawn immediately.
- in addition to the use of credit ratings South Ayrshire will be advised of information in movements in Credit Default Swap spreads against the iTraxx European Senior Financials benchmark and other market data daily via its Passport website, provided exclusively to it by Link. Extreme market movements may result in downgrade of an institution or removal from the South Ayrshire's lending list.

Sole reliance will not be placed on the use of this external service. In addition, South Ayrshire will also use market data and market information, as well as information on any external support for banks to help support its decision-making process.

3.3 *Country Limits – Credit Worthiness*

Significant levels of downgrades to Short and Long-Term credit ratings have not materialised since the crisis in March 2020. In the main, where they did change, any alterations were limited to Outlooks. However, more recently the UK sovereign debt rating has been placed on Negative Outlook by the three major rating agencies in the wake of the Truss/Kwarteng unfunded tax-cuts policy. Although the Sunak/Hunt government has calmed markets, the outcome of the rating agency reviews is unknown at present, but it is possible the UK sovereign debt rating will be downgraded. Accordingly, when setting minimum sovereign debt ratings, this Authority will not set a minimum rating for the UK.

CDS prices

Although bank CDS prices, (these are market indicators of credit risk), spiked upwards during the days of the Truss/Kwarteng government, they have returned to more average levels since then. However, sentiment can easily shift, so it will remain important to undertake continual monitoring of all aspects of risk and return in the current circumstances. Link monitor CDS prices as part of their creditworthiness service to local authorities and South Ayrshire has access to this information via its Link-provided Passport portal.

Other limits

Due care will be taken to consider the exposure of South Ayrshire's total investment portfolio to non-financial investments, countries, groups, and sectors.

1. **Non-financial investment limit.** South Ayrshire has determined that it will limit the maximum total exposure to non-financial investments, (e.g. property and third-party loans).

2. **Country limit.** South Ayrshire has determined that it will only use approved counterparties from the UK and from countries with a **minimum sovereign credit rating of *AA-.*** The list of countries that qualify using this credit criteria as at the date of this report are shown below. This list will be added to, or deducted from, by officers should ratings change in accordance with this policy.

APPROVED COUNTRIES FOR INVESTMENTS

This list is based on those countries which have sovereign ratings of AA- or higher, (shown is the lowest rating from Fitch, Moody's and S&P) and also, (except - at the time of writing - for Hong Kong, Norway and Luxembourg), have banks operating in sterling markets which have credit ratings of green or above in the Link credit worthiness service.

Based on lowest available rating

AAA

- Australia
- Denmark
- Germany
- Luxembourg
- Netherlands
- Norway
- Singapore
- Sweden
- Switzerland

AA+

- Canada
- Finland
- U.S.A.

AA

- Abu Dhabi (UAE)
- France

AA-

- Belgium
- Hong Kong
- Qatar
- U.K.

3.4 ***Investment Strategy***

In-house funds. Investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (i.e., rates for investments up to 12 months). Greater returns are usually obtainable by investing for longer periods. The current shape of the yield curve suggests that is the case at present, but there is the prospect of Bank Rate having peaked in the second half of 2023 and possibly reducing as early as the second half of 2024 so an agile investment strategy would be appropriate to optimise returns.

Accordingly, while most cash balances are required to manage the downs of cash flow where cash sums can be identified that could be invested for longer periods, the value to be obtained from longer-term investments will be carefully assessed.

Bank Rate and Investment Returns Expectations -

The current forecast shown in paragraph 3.3, includes a forecast for Bank Rate to have peaked at 5.25% in Q4 2023.

The suggested budgeted investment earnings rates for returns on investments placed for periods up to about three months during each financial year are as follows:

Average earnings in each year	
2023/24 (residual)	5.30%
2024/25	4.55%
2025/26	3.10%
2026/27	3.00%
2027/28	3.25%
Years 6 to 10	3.25%
Years 10+	3.25%

As there are so many variables now, caution must be exercised in respect of all interest rate forecasts.

Invesment Treasury Indicator and Limit - total principal funds invested for greater than 365 days. These limits are set regarding the Council's liquidity requirements and to reduce the need for early sale of an investment, and are based on the availability of funds after each year-end.

Maximum principal sums invested > 365 days (about 12 months)			
	2023/24 £m	***2024/25 £m***	***2025/26 £m***
Principal sums invested > 365 days (about 12 months)	£10m	£10m	£10m

For its cash flow generated balances, the Council will seek to utilise its business reserve accounts, notice accounts, money market funds and short-dated deposits to benefit from the compounding of interest.

3.5 *Investment – Cash Liquidity*

A key responsibility of the Treasury function is to ensure the Council maintains adequate liquidity of cash to ensure its payment obligations can be fully always met. This liquidity of cash is required on a daily basis to meet the cash flow requirements of payments to employees, suppliers, agencies, re-payment of loan interest and benefits etc.

The Council does not currently utilise an overdraft facility from its bankers, Bank of Scotland as liquidity cash is available using investment accounts. Additionally, the Council has access to short term loan funding from the money markets when required.

Liquidity - in respect of this area the Council seeks to maintain:

- Bank overdraft **-** £0.00m; and
- Liquidity cash available of £15m.

3.6 *End of Year Investment Report*

At the end of the financial year, the Council will report on its investment activity as part of its Annual Treasury Report. This report will be submitted to the Council's Audit and Governance Panel and South Ayrshire Council Leadership Panel prior to 30 September following the end of each financial year (or as soon as practicable depending on Council meeting dates).

Section 4 – Governance Arrangements

4.1 *Financial Regulations*

The Financial Regulations set out the responsibilities of the Council and the Audit and Governance Panel in respect of treasury matters as follows:

4.1.1 Council

1. Approval of treasury strategy report.

Cabinet

1. budget consideration and approval
2. approval of the division of responsibilities
3. approval of the quarterly performance indicators
4. approval of mid-year and annual report; and
5. Approving the selection of external service providers and agreeing terms of appointment.

Audit and Governance Panel

1. Reviewing the treasury management policy and procedures and making recommendations to the responsible body; and
2. Scrutiny of the mid-year and annual report.
3. Scrutiny or the quarterly performance indicators

4.2 *Role of the Section 95 Officer – Head of Finance ICT and Procurement*

The S95 (responsible) officer has authority through the Scheme of Delegation and the Financial Regulations for the day-to-day execution and administration of treasury management decisions in line with the Council's Strategy and Treasury Management Practices. This includes:

- recommending clauses, treasury management policy 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;

- preparation of a capital strategy to include capital expenditure, capital financing, non-financial investments and treasury management, with a longer-term timeframe;
- 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;
- ensure 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; and
- creation of Treasury Management Practices which specifically deal with how non-treasury investments will be carried out and managed, to include the following:

    1. *Risk management (TMP1 and schedules), including investment and risk management criteria for any material non-treasury investment portfolios;*

    2. *Performance measurement and management (TMP2 and schedules), including methodology and criteria for assessing the performance and success of non-treasury investments;*

    3. *Decision making, governance and organisation (TMP5 and schedules), 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;*

    4. *Reporting and management information (TMP6 and schedules), including where and how often monitoring reports are taken;*

    5. *Training and qualifications (TMP10 and schedules), including how the relevant knowledge and skills in relation to non-treasury investments will be arranged.*

4.3 ***Policy on the Use of External Service Providers***

South Ayrshire uses Link Group, Treasury solutions as its external treasury management advisors.

South Ayrshire recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon the services of our external service providers. All decisions will be undertaken with regards to all available information, including, but not solely, our treasury advisers.

It also recognises that there is value in employing external providers of treasury management services to acquire access to specialist skills and resources. South Ayrshire will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented and subjected to regular review.

4.4 ***Training***

The CIPFA Treasury Management Code requires the responsible officer to ensure that members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsible for scrutiny.

Furthermore, pages 47 and 48 of the Code state that they expect “all organisations to have a formal and comprehensive knowledge and skills or training policy for the effective acquisition and retention of treasury management knowledge and skills for those responsible for management, delivery, governance, and decision making.

As a minimum, South Ayrshire will carry out the following to monitor and review knowledge and skills:

- Record attendance at training and ensure action is taken where poor attendance is identified.
- Prepare tailored learning plans for treasury management officers and board/council members.
- Require treasury management officers and board/council members to undertake self-assessment against the required competencies (as set out in the schedule that may be adopted by the organisation).
- Have regular communication with officers and board/council members, encouraging them to highlight training needs on an ongoing basis.”

In further support of the revised training requirements, CIPFA’s Better Governance Forum and Treasury Management Network have produced a ‘self-assessment by members responsible for the scrutiny of treasury management,’ which is available from the CIPFA website to download.

The training needs of treasury management officers are periodically reviewed.

A formal record of the training received by officers central to the Treasury function will be maintained by Senior Finance Officer. Similarly, a formal record of the treasury management/capital finance training received by members will also be maintained by Senior Finance Officer.

Permitted Investments

The Council approves the following forms of investment instrument for use as permitted investments as set out in **Table 1-6** (page 36 to 38).

Treasury risks

All the investment instruments in Table 1 are subject to the following risks:

- **Credit and counter-party risk:** this is the risk of failure by counterparty (bank or building society) to meet its contractual obligations to the organisation particularly because of the counterparty's diminished creditworthiness, and the resulting detrimental effect on the organisation's capital or current (revenue) resources. There are no counterparties where this risk is zero although AAA rated organisations have the highest, relative, level of creditworthiness.

- **Liquidity risk:** this is the risk that cash will not be available when it is needed. While it could be said that all counterparties are subject to at least a very small level of liquidity risk as credit risk can never be zero, in this document, liquidity risk has been treated as whether instant access to cash can be obtained from each form of investment instrument. However, it must be pointed out that while some forms of investment e.g., Gilts, CDs, corporate bonds can usually be sold immediately if the need arises, there are two caveats: a. Cash may not be available until a settlement date up to three days after the sale b. there is an implied assumption that markets will not freeze up and so the instrument in question will find a ready buyer. The column in tables 1 / 2 headed as 'market risk' will show each investment instrument as being instant access, sale T+3 = transaction date plus 3 business days before you get cash, or term – i.e., money is locked in until an agreed maturity date.

- **Market risk**: this is the risk that, through adverse market fluctuations in the value of the principal sums an organisation borrows and invests, its stated treasury management policies and objectives are compromised, against which effects it has failed to protect itself adequately. However, some cash-rich local authorities may want exposure to market risk, e.g., those investing in investment instruments to obtain a long-term increase in value.

- **Interest rate risk:** this is the risk that fluctuations in the levels of interest rates create an unexpected or unbudgeted burden on the organisation's finances, against which the organisation has failed to protect itself adequately. This authority has set limits for its fixed and variable rate exposure in its Treasury Indicators in this report. All types of investment instrument have interest rate risk except for the following forms of instrument which are at variable rate of interest (and the linkage for variations is also shown):

- **Legal and regulatory risk:** this is the risk that the organisation itself, or an organisation powers or regulatory requirements, and that the organisation suffers losses accordingly.

Controls on treasury risks

- o **Credit and counter-party risk**: this authority has set minimum credit criteria to determine which counterparties and countries are of sufficiently high creditworthiness to be considered for investment purposes.

- o **Liquidity risk:** the Council has a cash flow forecasting model to enable it to determine how long investments can be made for and how much can be invested.

- o **Market risk:** this Council does not purchase investment instruments which are subject to market risk in terms of fluctuation in their value.

- o **Interest rate risk:** the Council manages this risk by having a view of the future course of interest rates and then formulating a treasury management strategy accordingly which aims to maximize investment earnings consistent with control of risk or alternatively, seeks to minimise expenditure on interest costs on borrowing.

- o Legal and regulatory risk: the Council will not undertake any investment until it has ensured it has all necessary powers and complied with all regulations.

Unlimited investments

Regulation 24 states that an investment can be shown as being 'unlimited' in terms of the maximum amount or percentage of the total portfolio that can be put into that type of investment.

The Council has given the following types of investment an unlimited category:

- o **Debt Management Agency Deposit Facility.** This is considered the lowest risk investment form available to local authorities as it is operated by the Debt Management Office, part of H.M. Treasury, i.e., the UK Government's sovereign rating stands behind the DMADF. It is also a deposit account and avoids the complications of buying and holding Government issued treasury bills or gilts.

- o **High credit worthiness banks and building societies**. See Section 3.2 relating to creditworthiness. While an unlimited amount of the investment portfolio may be put into banks and building societies with high credit worthiness, the Council will ensure diversification of its portfolio ensuring that no more than 50% of the total portfolio can be placed with any one institution or group at any one time.

Objectives of each type of investment instrument

Regulation 25 requires an explanation of the objectives of every type of investment instrument which an authority approves as being 'permitted'. (Part 1 section 17 also requires authorities to explain any special circumstances that have led them to a particular approach.

1. Deposits

The following forms of 'investments' are more accurately called deposits as cash is deposited in an account until an agreed maturity date or is held at call.

1. **Debt Management Agency Deposit Facility -** This offers the lowest risk form of investment available to local authorities as it is effectively an investment placed with the Government. It is also easy to use as it is a deposit account and

avoids the complications of buying and holding Government issued treasury bills or gilts. As it is low risk it also earns low rates of interest. However, it is very useful for authorities whose overriding priority is the avoidance of risk. The longest period for a term deposit with the DMADF is 6 months.

2. **Term deposits with high credit worthiness banks and building societies -** See paragraph 3.2 for an explanation of this authority's definition of high credit worthiness. This is the most widely used form of investing used by local authorities. It offers a much higher rate of return than the DMADF (dependent on term). The Council will ensure diversification of its portfolio of deposits, ensuring that no more than 50% of the total portfolio can be placed with any one institution or group. In addition, longer-term deposits offer an opportunity to increase investment returns by locking in high rates ahead of an expected fall in the level of interest rates. At other times, longer-term rates can offer good value when the markets incorrectly assess the speed and timing of interest rate increases. This form of investing therefore, offers a lot of flexibility and higher earnings than the DMADF. Where it is restricted is that once a longer-term investment is made, that cash is locked in until the maturity date.

3. **Call accounts with high credit worthiness banks and building societies**. The objectives are as for 1b. But there is instant access to recalling cash deposited. This generally means accepting a lower rate of interest than that which could be earned from the same institution by making a term deposit. Some use of call accounts is highly desirable to ensure that the authority has ready access to cash when needed to pay bills.

4. **Fixed term deposits with variable rate and variable maturities (structured deposits).** This line encompasses ALL types of structured deposits. There has been considerable change in the types of structured deposits brought to the market over the last few years, some of which are no longer available. In view of this area's fluidity, this is a generic title for all structured deposits to provide Councils greater flexibility to adopt new instruments as and when they are brought to the market.

5. **Collateralised deposits.** These are deposits placed with a bank which offers collateral backing based on specific assets. Examples seen in the past have included local authority LOBOs, where such deposits are effectively lending to a local authority as that is the ultimate security.

- **Deposits with Counterparties currently in receipt of Government Support/ Ownership**

These banks offer another dimension of creditworthiness in terms of Government backing through either partial or full direct ownership. The view of the Council is that such backing makes these banks attractive institutions with whom to place deposits, and that will remain our view if the UK sovereign rating were to be downgraded in the coming year.

1. **Term deposits with high credit worthiness banks which are fully or semi nationalised.** As for 1b. but Government full, (or substantial partial), ownership, implies that the Government stands behind this bank and will be deeply committed to providing whatever support that may be required to ensure the continuity of that bank. This authority considers that this indicates a low and acceptable level of residual risk.

2. **Fixed term deposits with variable rate and variable maturities (structured deposits).** This line encompasses ALL types of structured deposits. There has been considerable change in the types of structured deposits brought to the market over the last few years, some of which are no longer available. In view of this area's fluidity, this is a generic title for all structured deposits to provide Councils greater flexibility to adopt new instruments as and when they are brought to the market.

- **Collective Investment Schemes structured as Open-Ended Investment Companies (OEICs)**

1. **Government liquidity funds**. These are the same as money market funds (see below) but only invest in government debt issuance with highly rated governments. Due to the higher quality of underlying investments, they offer a lower rate of return than MMFs. However, their net return is typically on a par with the DMADF, but with instant access.

2. **Money Market Funds (MMFs).** MMFs are AAA rated and are widely diversified, using many forms of money market securities including types which this authority does not currently have the expertise or capabilities to hold directly. However, due to the high level of expertise of the fund managers and the huge amounts of money invested in MMFs, and the fact that the weighted average maturity (WAM) cannot exceed 60 days (about 2 months), MMFs offer a combination of high security, instant access to funds, high diversification and good rates of return compared to equivalent instant access facilities. They are particularly advantageous in falling interest rate environments as their 60-day WAM means they have locked in investments earning higher rates of interest than are currently available in the market. MMFs also help an authority to diversify its own portfolio as e.g., a £2m investment placed directly with HSBC is a 100% risk exposure to HSBC whereas £2m invested in an MMF may end up with say £10,000 being invested with HSBC through the MMF. For authorities particularly concerned with risk exposure to banks, MMFs offer an effective way of minimising risk exposure while still getting much better rates of return than available through the DMADF.

3. **Ultra-short, dated bond funds.** These funds are like MMFs, can still be AAA rated but have variable net asset values (VNAV) as opposed to a traditional MMF which has a Constant Net Asset Value (CNAV). They aim to achieve a higher yield and to do this either take more credit risk or invest out for longer periods of time, which means they are more volatile. These funds can have WAM's and Weighted Average Life (WAL's) of 90 – 365 days (about 12 months) or even longer. Their primary objective is yield and capital preservation is second. They therefore have a higher risk than MMFs and correspondingly have the potential to earn higher returns than MMFs.

4. **Gilt funds.** These are funds which invest only in U.K (United Kingdom). Government gilts. They offer a lower rate of return than bond funds but are highly rated both as a fund and through investing only in highly rated government securities. They offer a higher rate of return than investing in the DMADF, but they do have exposure to movements in the market prices of assets held.

5. **Bond funds**. These can invest in both government and corporate bonds. This therefore entails a higher level of risk exposure than gilt funds and the aim is to achieve a higher rate of return than normally available from gilt funds by trading in non-government bonds.

4. Securities Issued or Guaranteed by Governments

The following types of investments are where an authority directly purchases a particular investment instrument, a security – i.e., it has a market price when purchased and that value can change during the period the instrument is held until it matures or is sold. The annual earnings on a security are called a yield – i.e., it is normally the interest paid by the issuer divided by the price you paid to purchase the security unless a security is initially issued at a discount – for example, treasury bills.

1. **Treasury bills.** These are short term bills (up to 18 months (about 1 and a half years) but usually 9 months or less, although none have ever been issued for this maturity) issued by the Government and so are backed by the sovereign rating of the UK. The yield is higher than the rate of interest paid by the DMADF, and another advantage compared to a time deposit in the DMADF is that they can be sold if there is a need for access to cash at any point in time. However, there is a spread between purchase and sale prices so early sales could incur a net cost during the period of ownership.

2. **Gilts.** These are longer term debt issuance by the UK Government and are backed by the sovereign rating of the UK. The yield is higher than the rate of interest paid by the DMADF, and another advantage compared to a time deposit in the DMADF is that they can be sold if there is a need for access to cash at any point in time. However, there is a spread between purchase and sale prices so early sales may incur a net cost. Market movements between purchase and sale may also adversely impact proceeds. The advantage over Treasury bills is that they generally offer higher yields the longer it is to maturity (for most periods) if the yield curve is positive.

3. **Bond issuance issued by a financial institution which is explicitly guaranteed by the UK Government** e.g., National Rail. This is like gilt due to the explicit Government guarantee.

4. **Sovereign bond issues (other than the UK govt) denominated in Sterling.** As for gilts but issued by other nations. Use limited to issues of nations with at least the same sovereign rating as for the UK.

5. **Bonds issued by Multi-Lateral Development Banks (MLDBs).** These are like c. and d. above but are issued by MLDBs which are typically guaranteed by a group of sovereign states e.g. European Bank for Reconstruction and Development.

5 Securities issued by Corporate Organisations

The following types of investments are where an authority directly purchases a particular investment instrument, a security – i.e., it has a market price when purchased and that value can change during the period the instrument is held until it is sold. The annual earnings on a security are called a yield – i.e., is the interest paid by the issuer divided by the price you paid to purchase the security. These are like the previous category but corporate organisation's can have a wide variety of credit worthiness so it is essential for local authorities to only select the organisation's with the highest levels of credit worthiness. Corporate securities are generally a higher risk than government debt issuance and so earn higher yields.

1. **Certificates of deposit (CDs).** These are shorter term securities issued by deposit taking institutions (mainly financial institutions). They are negotiable instruments, so can be sold ahead of maturity and purchased after being issued. However, that liquidity can come at a price where the yield could be marginally less than placing a deposit with the same bank as the issuing bank.

2. **Commercial paper.** This is like CDs but is issued by commercial organisations or other entities. Maturity periods are up to 365 days (about 12 months) but commonly 90 days (about 3 months).

3. **Corporate bonds.** These are (long term) bonds (usually bearing a fixed interest rate) issued by a financial institution, company, or other non-government issuer to raise capital for the institution as an alternative to issuing shares or borrowing from banks. They are generally seen to be of a lower creditworthiness than government issued debt and so usually offer higher rates of yield.

4. **Floating rate notes.** These are bonds on which the rate of interest is established periodically with reference to short-term interest rates.

6. Other

Property Fund - This is a collective investment fund specialising in property. Rather than owning a single property with all the risk exposure that means to one property in one location rising or falling in value, maintenance costs, tenants paying their rent / lease etc., a collective fund offers the advantage of diversified investment over a wide portfolio of different properties. This can be attractive for authorities who want exposure to the potential for the property sector to rise in value. However, timing is critical to entering or leaving this sector at the optimum times of the property cycle of rising and falling values. Typically, the minimum investment time horizon for considering such funds is 3-5 years.

Deposits

Table 1	***Liquidity risk***	***Market risk***	***Max % of total investment***	***Max. maturity***
Debt Management Agency Deposit Facility	Term	no	100%	6 months
Term deposits – local / public authorities	Term	no	100%	2 years
Call accounts – banks and building societies	Instant	no	100%	N/A
Term deposits – banks and building societies	Term	no	100%	See Credit Policy (colour code)
Fixed term deposits with variable rate and variable maturities: Structured deposits.	Term	no	10%	See Credit Policy (colour code)

Deposits with Counterparties Currently in Receipt of Government Support/ Ownership

Table 2	*Liquidity risk*	*Market risk*	*Max % of total investment*	*Max. maturity period*
UK Part Nationalised Banks	Term	no	100%	See Credit Policy (colour code)
Banks nationalised by high credit rated (sovereign rating) countries – non-UK	Term	no	100%	See Credit Policy (colour code)
Fixed term deposits with variable rate and variable maturities: Structured deposits	Term	Yes	10%	See Credit Policy (colour code)

Collective Investment schemes structured as Open-Ended Investment Companies (OEIC's)

Table 3	Liquidity risk	Market risk	Max % of total investment	Max. maturity period
Government Liquidity Funds	Instant	See Section 3	20%	See credit policy
Money Market Funds (CNAV)	Instant	See Section 3	100%	See credit policy
Money Market Funds LVNAV	Instant	See Section 3	50%	See credit policy
Money Market Funds VNAV	Instant	See Section 3	50%	See credit policy
Ultra-short, dated bond funds with a credit score of 1.25	T+1 – T+5	See Section 3	50%	See credit policy
Ultra-short, dated bond funds with a credit score of 1.50	T+1 – T+5	See Section 3	50%	See credit policy
Bond Funds	Min T+2	See Section 3	50%	See credit policy
Gilt Funds	Min T+2	See Section 3	50%	See credit policy

Securities issued or guaranteed by governments

Table 4	***Minimum Credit Criteria***	***Liquidity risk***	***Market Risk***
Treasury Bills	UK sovereign	Sale T+1	Yes
UK Government Gilts	UK Sovereign	Sale T+1	Yes
Bond issuance issued by a financial institution which is guaranteed by UK Government e.g. Network Rail	UK Sovereign	Sale T+3	Yes
Sovereign Bond issues (other than UK Government)	AAA	Sale T+1	Yes
Bonds issued by multi-lateral development banks	AAA	Sale T+1	Yes

Securities issued by corporate organisations

Table 5	***Liquidity risk***	***Market risk***	***Max % of total investmen t***
Certificates of deposit issued by banks and building societies	Sale T+1	yes	20%
Commercial Paper	Sale T+1	yes	20%
Floating Rate Notes	Sale T+0	yes	20%
Corporate bonds	T +3	Yes	20%

Other

Table 6	***Liquidity risk***	***Market risk***	***Max % of total investment***	***Max. maturity period***
Property Funds	Variable	Yes	20%	3-5 Yrs.

Accounting Treatment of Investments

The accounting treatment may differ from the underlying cash transactions arising from investment decisions made by this Council. To ensure that the Council is protected from any adverse revenue impact, which may arise from these differences, we will review the accounting implications of new transactions before they are undertaken.

Treasury Management Practice – Credit and Counterparty Risk Management
South Ayrshire Council and Common Good Funds Permitted Investments, Associated Controls

Type of Investment	***Treasury Risks***	***Mitigating Controls***	***Council Limits***	***Common Good Limits***
Cash type instruments				
• Deposits with the Debt Management Account Facility (UK Government) (**Very low risk)**	This is a deposit with the UK Government and as such counterparty and liquidity risk is very low, and there is no risk to value. Deposits can be between overnight and 6 months.	Little mitigating controls required. As this is a UK Government investment the monetary limit is unlimited to allow for a safe haven for investments.	Unlimited (maximum 6 months)	Unlimited (maximum 6 months)
• Deposits with other local authorities or public bodies **(Very low risk)**	These are considered quasi–UK Government debt and as such counterparty risk is very low, and there is no risk to value. Liquidity may present a problem as deposits can only be broken with the agreement of the counterparty, and penalties can apply. Deposits with other non-local authority bodies will be restricted to the overall credit rating criteria.	Little mitigating controls required for local authority deposits, as this is a quasi-UK Government investment. Non- local authority deposits will follow the approved credit rating criteria.	£20m per counterparty – 2 Years	£20m per counterparty – 2 Years
• Money Market Funds (MMFs) **(Low to Very low risk)**	Pooled cash investment vehicle which provides very low counterparty, liquidity, and market	Funds will only be used where the MMFs have an 'AAA' rated status from Fitch, Moody's or Standard and Poor's.	£20m	£20m

Type of Investment	*Treasury Risks*	*Mitigating Controls*	*Council Limits*	*Common Good Limits*
	risk. These will primarily be used as liquidity instruments.			
• Ultra-short, dated bond funds **(low risk)**	Pooled cash investment vehicle which provides very low counterparty, liquidity, and market risk. These will primarily be used as liquidity instruments.	Funds will only be used where the MMFs have an 'AAA' rated status from Fitch, Moody's or Standard and Poor's.	£10m	£10m
• Call account deposit accounts with financial institutions (banks and building societies) **(Low risk depending on credit rating)**	These tend to be low risk investments but will exhibit higher risks than categories (a), (b) and (c) above. Whilst there is no risk to value with these types of investments, liquidity is high, and investments can be returned at short notice.	The counterparty selection criteria approved above restricts lending only to high quality counterparties, measured primarily by credit ratings from Fitch, Moody's and Standard and Poor's. The selection defaults to the lowest available credit rating to provide additional risk control measures. On daily investment dealing with these criteria will be further strengthened by additional market intelligence.	See credit policy	See credit policy
• Term deposits with financial institutions (banks and building societies) **(Low to medium risk depending on period and credit rating)**	These tend to be low risk investments but will exhibit higher risks than categories (a), (b) and (c) above. Whilst there is no risk to value with these types of investments, liquidity is low and term deposits can only be broken with the	The counterparty selection criteria approved above restricts lending only to high quality counterparties, measured primarily by credit ratings from Fitch, Moody's and Standard and Poor's. The selection defaults to the lowest available credit rating to provide additional risk control measures.	See credit policy	See credit policy

Type of Investment	*Treasury Risks*	*Mitigating Controls*	*Council Limits*	*Common Good Limits*
	agreement of the counterparty, and penalties may apply.	On daily investment dealing with these criteria will be further strengthened by additional market intelligence.		
• Government Gilts and Treasury Bills **(Very low risk)**	These are marketable securities issued by the UK Government and as such counterparty and liquidity risk is very low, although there is potential risk to value arising from an adverse movement in interest rates (no loss if these are held to maturity.	Little counterparty mitigating controls are required, as this is a UK Government investment. The potential for capital loss will be reduced by limiting the maximum monetary and time exposures.	See credit policy	See credit policy
• Certificates of deposits with financial institutions **(Low risk)**	These are short dated marketable securities issued by financial institutions and as such counterparty risk is low but will exhibit higher risks than categories (a), (b) and (c) above. There is a risk to value of capital loss arising from selling ahead of maturity if combined with an adverse movement in interest rates. Liquidity risk will normally be low.	The counterparty selection criteria approved above restricts lending only to high quality counterparties, measured primarily by credit ratings from Fitch, Moody's and Standard and Poor's. The selection defaults to the lowest available credit rating to provide additional risk control measures. On daily investment dealing with these criteria will be further strengthened by additional market intelligence.	See credit policy	See credit policy
• Structured deposit facilities with banks and building societies (escalating rates, de-escalating rates etc.)	These tend to be medium to low risk investments but will exhibit higher risks than categories (a), (b) and (c) above. Whilst there is no risk to value with these types	The counterparty selection criteria approved above restricts lending only to high quality counterparties, measured primarily by credit ratings from Fitch, Moody's and Standard and	See credit policy	See credit policy

Type of Investment	*Treasury Risks*	*Mitigating Controls*	*Council Limits*	*Common Good Limits*
(Low to medium risk depending on period and credit rating)	of investments, liquidity is very low, and investments can only be broken with the agreement of the counterparty (penalties may apply).	Poor's. The selection defaults to the lowest available credit rating to provide additional risk control measures. On daily investment dealing with these criteria will be further strengthened by additional market intelligence.		
• Corporate bonds **(Medium to high risk depending on period and credit rating)**	These are marketable securities issued by financial and corporate institutions. Counterparty risk will vary and there is risk of the value of capital loss arising from selling ahead of maturity if combined with an adverse movement in interest rates. Liquidity risk will be low.	The counterparty selection criteria approved above restricts lending only to high quality counterparties, measured primarily by credit ratings from Fitch, Moody's and Standard and Poor's. Corporate bonds will be restricted to those meeting the base criteria. Day-to-day investment dealing with these criteria will be further strengthened using additional market intelligence.	See credit policy	See credit policy

Other types of Investment

Type of Investment	*Credit Criteria*	*Liquidity Risk*	*Market Risk*	*Mitigating Controls*	*Council Limits*
Common Good	Not applicable	Not applicable	No	Any Common Good, loan or investment would be subject to a separate panel report and the approval of Members before progressing. Each loan would therefore be assessed on a case-by-case basis and be supported by the rationale behind the investment and likelihood of any loss.	Term – 20 years - unlimited

Type of Investment	***Credit Criteria***	***Liquidity Risk***	***Market Risk***	***Mitigating Controls***	***Council Limits***
Registered Social Landlord	Not applicable	Not applicable	No	Any RSL loan or investment would be subject to a separate panel report and the approval of Members before progressing. Each loan would therefore be assessed on a case-by-case basis and be supported by the rationale behind the investment and likelihood of any loss.	Term – 20 years - unlimited
Third Party	Not applicable	Not applicable	No	Any third-party loan or investment would be subject to a separate panel report and the approval of Members before progressing. Each loan would therefore be assessed on a case-by-case basis and be supported by the rationale behind the investment and likelihood of any loss.	Term – 5 years - £1m
Third Party (Soft Loans)	Not applicable	Not applicable	No	Any third-party loan or investment on a soft loan basis (below market rates) would be subject to a separate panel report and the approval of Members before progressing. Each loan would therefore be assessed on a case-by-case basis and be supported by the rationale behind the investment and likelihood of any loss.	Term – 5 years - £1m
hub SW/ SFT Project Investment	Not applicable	Minimum 25 years term	No	Investment is subject to a separate panel report and the approval of Members before progressing. The investment would therefore be assessed on a case basis and be supported by the rationale behind the investment and the likelihood of any loss.	Term – 25 years - £1m

The Monitoring of Investment Counterparties - The status of counterparties will be monitored regularly. The Council receives credit rating and market information from Link Asset Services, including when ratings change, and counterparties are checked promptly.

On occasion ratings may be downgraded when an investment has already been made. The criteria used are such that a minor downgrading should not affect the full receipt of the principal and interest. Any counterparty failing to meet the criteria will be removed from the list immediately by the Head of Finance and ICT, and if required new counterparties which meet the criteria will be added to the list.

Appendix 2

South Ayrshire Council
Equality Impact Assessment
Scoping Template

Equality Impact Assessment is a legal requirement under the Public Sector Duty to promote equality of the Equality Act 2010. Separate guidance has been developed on Equality Impact Assessment's which will guide you through the process and is available to view here: [Equality Impact Assessment including Fairer Scotland Duty](#)

Further guidance is available here: [Assessing impact and the Public Sector Equality Duty: a guide for public authorities (Scotland)](#)

The Fairer Scotland Duty ('the Duty'), Part 1 of the Equality Act 2010, came into force in Scotland from 1 April 2018. It places a legal responsibility on Councils to actively consider ('pay due regard to') how we can reduce inequalities of outcome caused by socio-economic disadvantage, when making strategic decisions. See information here: [Interim Guidance for Public Bodies](#) in respect of the Duty, was published by the Scottish Government in March 2018.

1. Policy details

Policy Title	Treasury Management and Investment Strategy 2024-25
Lead Officer (Name/Position/Email)	Kate Copland, Senior Finance Officer, Treasury/ Capital – kate.copland@south-ayrshire.gov.uk

2. Which communities, groups of people, employees or thematic groups do you think will be, or potentially could be, impacted upon by the implementation of this policy? Please indicate whether these would be positive or negative impacts

Community or Groups of People	Negative Impacts	Positive impacts
Age – men and women, girls & boys	-	-
Disability	-	-
Gender Reassignment (Trans/Transgender Identity)	-	-
Marriage or Civil Partnership	-	-
Pregnancy and Maternity	-	-
Race – people from different racial groups, (BME) ethnic minorities and Gypsy/Travellers	-	-
Religion or Belief (including lack of belief)	-	-
Sex – gender identity (issues specific to women & men or girls & boys)	-	-
Sexual Orientation – person's sexual orientation i.e. LGBT+, lesbian, gay, bi-sexual, heterosexual/straight	-	-
Thematic Groups: Health, Human Rights & Children's Rights	-	-

3. What likely impact will this policy have on people experiencing different kinds of social disadvantage? (Fairer Scotland Duty). Consideration must be given particularly to children and families.

Socio-Economic Disadvantage	Negative Impacts	Positive impacts
Low Income/Income Poverty – cannot afford to maintain regular payments such as bills, food, clothing	-	-
Low and/or no wealth – enough money to meet Basic living costs and pay bills but have no savings to deal with any unexpected spends and no provision for the future	-	-
Material Deprivation – being unable to access basic goods and services i.e. financial products like life insurance, repair/replace broken electrical goods, warm home, leisure/hobbies	-	-
Area Deprivation – where you live (rural areas), where you work (accessibility of transport)	-	-
Socio-economic Background – social class i.e. parent's education, employment and income	-	-

4. Do you have evidence or reason to believe that the policy will support the Council to:

General Duty and other Equality Themes Consider the 'Three Key Needs' of the Equality Duty	Level of Negative and/or Positive Impact (High, Medium or Low)
Eliminate unlawful discrimination, harassment and victimisation	Low
Advance equality of opportunity between people who share a protected characteristic and those who do not	Low
Foster good relations between people who share a protected characteristic and those who do not. (Does it tackle prejudice and promote a better understanding of equality issues?)	Low
Increase participation of particular communities or groups in public life	Low
Improve the health and wellbeing of particular communities or groups	Low
Promote the human rights of particular communities or groups	Low
Tackle deprivation faced by particular communities or groups	Low

5. Summary Assessment

Is a full Equality Impact Assessment required? (A full Equality Impact Assessment must be carried out if impacts identified as **Medium and/or High**)	~~**YES**~~ **NO**

Rationale for decision:

The strategy outlines the approach to be taken in managing the Council's cash flow and capital funding arrangements and is a mechanism for ensuring that budget targets are achieved: a full EQIA is, therefore, not required

Signed : Tim Baulk **Head of Service**

Date: 20 February 2024