ARGYLL AND BUTE COUNCIL **COUNCIL**

FINANCIAL SERVICES **27 FEBRUARY 2025**

TREASURY MANAGEMENT STRATEGY AND ANNUAL INVESTMENT STRATEGY 2025-26

1.0 EXECUTIVE SUMMARY

1.1 The Local Government in Scotland Act 2003 requires the council to have regard to the CIPFA Code of Practice on Treasury Management (revised 2021), the Code. The Treasury Management Strategy, including prudential and treasury Indicators, and the Annual Investment Strategy is a key reporting requirement, providing a comprehensive statement of treasury management policies and planned activity for the financial year ahead.

1.2 This report, prepared in compliance with the Code, covers the following:

- Capital Expenditure and Financing;
- An economic and interest rate update;
- Borrowing Strategy;
- Investment Strategy; and
- Prudential and Treasury Indicators 2025-28.

1.3 The report concludes that:

a) The Treasury Management Strategy provides a comprehensive statement of treasury management policies and planned activities, covering the relevant treasury and prudential indicators, the current and projected debt positions, and the Annual Investment Strategy for 2025-26.

b) A key driver of treasury management activity is the council's capital investment plans. Prudential indicators reflect the output from these plans and are designed to ensure that the council's capital investment plans are affordable, prudent and sustainable. Within the range of prudential indicators, there are several key indicators to ensure that the authority operates its activities within well defined limits.

c) Whilst the Capital Financing Requirement represents an underlying need to borrow, the council is currently maintaining an under-borrowed position. This strategy is prudent while medium and longer dated borrowing rates are expected to fall from their current levels, albeit that considerable uncertainty remains around interest rate forecasts.

d) The council's revenue budget includes appropriate provision for financing costs of capital expenditure. The key principles of the borrowing strategy will be to minimise debt interest costs over the medium term and to achieve a more even spread in the debt maturity profile.

e) The council's investment priorities will be security, liquidity and yield (return). A prudent approach to managing investment risk has been adopted. Exposure to credit risk will be limited by ensuring that all investments are placed with the higher rated bodies. A balanced view of risk against return will be taken in respect of all investments. It is anticipated that return on investments will be limited in 2025-26, as a result of Bank Rate forecasts and the over-riding principle of risk aversion.

1.4 This report has been considered by the Policy and Resources Committee and referred to full Council for approval. Council is requested to:

a) Approve the Treasury Management Strategy and Annual Investment Strategy for 2025-26, and the Prudential and Treasury Indicators for 2025-26 to 2027-28; and

b) Note that the strategy will be further scrutinised by the Audit and Scrutiny Committee at its meeting of 13 March 2025, with any recommendations requiring Council approval brought back to full Council at the earliest opportunity.

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TREASURY MANAGEMENT STRATEGY AND ANNUAL INVESTMENT STRATEGY 2025-26

2. INTRODUCTION

2.1 Background

2.1.1 The Chartered Institute of Public Finance and Accountancy (CIPFA) defines treasury management as 'The management of the local authority's borrowing, investments and cash flows, including its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks.'

2.1.2 The authority is required to operate a balanced revenue budget, which broadly means that cash raised during the year will meet cash expenditure. In addition, the authority's capital plans indicate the borrowing and longer term cash flow planning, required to meet its capital spending obligations. The treasury management operation ensures that cash flow is adequately planned, with cash being available when it is needed.

2.1.3 Surplus monies are invested in low risk counterparties or instruments commensurate with the council's low risk appetite, providing adequate liquidity initially before considering investment return. The management of longer term cash flow 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 risk or cost objectives.

2.1.4 The contribution the treasury management function makes to the authority is critical, as the balance of debt and investment operations ensure liquidity or the ability to meet spending commitments as they fall due, either on day to day revenue or for larger capital projects. The treasury operations will see a balance of the interest costs of debt and the investment income arising from cash deposits, impacting available resources. 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.

2.2 Reporting Requirements

2.2.1 The authority is required to receive and approve, as a minimum, three main treasury reports each year:

1) The Treasury Management Strategy, including prudential and treasury Indicators, and the Annual Investment Strategy (this report) – A forward looking report for the financial year ahead.
2) A Mid-year Treasury Management report – To update members on the capital and treasury position, amending prudential and treasury indicators, as necessary; and any required policy revisions.
3) An Annual Treasury Management report – A backward looking review, providing details of actual treasury activity, and prudential and treasury indicators, compared to the approved estimates.

2.2.2 The above reports require to be adequately scrutinised before being recommended to full Council for approval. This role will be undertaken by the Policy and Resources and Audit and Scrutiny Committees. In addition to the three major reports detailed above, quarterly reporting (end of June/end of December) is also required. These additional reports do not have to be reported to full Council but do require to be adequately scrutinised. This role will be undertaken by the Audit and Scrutiny Committee.

3. RECOMMENDATIONS

3.1 This report has been considered by the Policy and Resources Committee and referred to full Council for approval. Council is requested to:

a) Approve the Treasury Management Strategy and Annual Investment Strategy for 2025-26, and the Prudential and Treasury Indicators for 2025-26 to 2027-28; and

b) Note that the strategy will be further scrutinised by the Audit and Scrutiny Committee at its meeting of 13 March 2025, with any recommendations requiring Council approval brought back to full Council at the earliest opportunity.

4. TREASURY MANAGEMENT STRATEGY 2025-26

4.1 Capital Expenditure and Financing

4.1.1 The authority’s capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in the prudential indicators, which are designed to assist members’ overview and confirm capital expenditure plans are prudent, affordable and sustainable.

4.1.2 The Capital Expenditure prudential indicator is a summary of the authority’s capital expenditure plans, both those agreed previously, and those forming part of this budget cycle. The following table summarises the capital expenditure plans, as outlined within the proposed capital plan 2025-28.

	2025-26 Estimate £m	2026-27 Estimate £m	2027-28 Estimate £m
Executive Directorate (Douglas Hendry)			
Education	2.946	1.988	1.988
Facility Services - Shared Offices	3.681	0.667	0.382
Major Projects/CHORD	10.865	10.018	0.000
Executive Directorate (Kirsty Flanagan)			
ICT	1.352	0.820	0.688
Roads and Infrastructure	48.500	39.110	33.979
Development and Economic Growth	1.104	0.000	0.000
Health and Social Care Partnership	2.084	0.000	0.382
Live Argyll	0.474	0.468	0.382
Total	**71.006**	**53.071**	**37.801**

Note: The above financing need excludes other long-term liabilities, such as PFI and leasing arrangements that already include borrowing instruments.

4.1.3 The table below summarises the above capital expenditure plans and how these plans are being financed by capital or revenue resources. Any shortfall of resources results in a funding borrowing need.

	2025-26 £m	2026-27 £m	2027-28 £m
Gross Capital Expenditure	**71.006**	**53.071**	**37.801**
Financing:			
Specific Project Income	8.302	5.000	0.000
General Capital Grant	11.178	8.633	8.633
Asset Sales	0.750	0.500	0.500
Earmarked Reserves/Revenue	5.577	5.030	0.000
Total	**25.807**	**19.163**	**9.133**
Net Financing Need	**45.199**	**33.908**	**28.668**

4.2 The Authority's Borrowing Need (the Capital Financing Requirement)

4.2.1 The second prudential indicator is the authority'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 essentially a measure of the authority's indebtedness and so its underlying borrowing need. Any capital expenditure, which has not immediately been paid for through a revenue or capital resource, will increase the CFR.

4.2.2 The CFR does not increase indefinitely, as prudent annual repayments from revenue need to be made, which reflect the useful life of capital assets financed by borrowing. This authority has chosen to make debt repayments through scheduled debt amortisation (loans fund charges).

4.2.3 The CFR includes any other long term liabilities (e.g., PPP schemes, finance leases). Whilst these increase the CFR, and therefore the authority's borrowing requirement, these types of schemes include a borrowing facility by the PPP or lease provider and so the authority is not required to separately borrow for these schemes. The council hold long term liabilities within its CFR in this respect totalling an estimated £106.346m as at 31 March 2025.

4.2.4 Council is asked to approve the CFR projections outlined in the table below.

	2025/26 Estimate £m	2026/27 Estimate £m	2027/28 Estimate £m
Opening CFR	360	394	415
Movement in CFR	34	21	16
Closing CFR	**394**	**415**	**431**

Net financing need for the year (above)	45	34	29
Less Loans Fund principal repayments and other financing movements including new PPP/ finance lease arrangements and principal repayments	11	13	13
Movement in CFR	**34**	**21**	**16**

4.2.5 In addition to the CFR, there will be a refinancing requirement in respect of the repayment of PWLB loan principal of £1.680m each year. These repayments of principal relate to a 10 year PWLB loan (original principal £21m), which was taken on a fixed Equal Instalments of Principal (EIP) basis. All other PWLB loans will be repayable on maturity, with no maturity loans due to mature in the period to 31 March 2028.

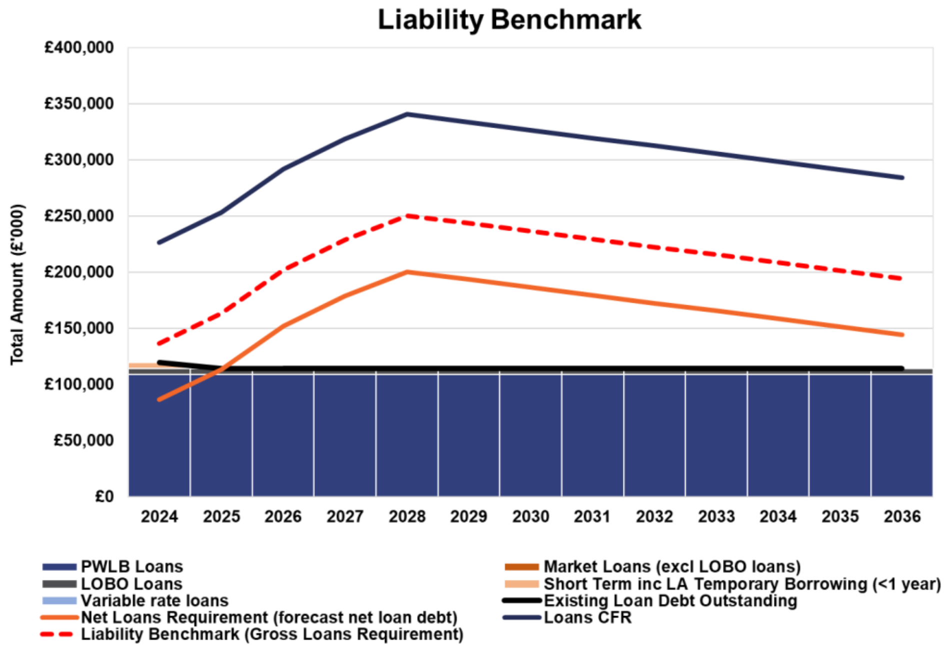
4.2.6 There is also a potential for market loans to be recalled. The council has one outstanding market or LOBO loan for £5.255m, maturing 2048, with call dates every 6 months. This loan could potentially be recalled at the 22 June or 22 December call dates in any year.

4.2.7 Any PWLB or LOBO loans maturing during the year will ultimately require replacement borrowing to maintain the council's cashflow position. In addition, the council will continue to actively monitor potential restructuring opportunities, in order to generate cash savings, at a minimum risk, and improve the balance of the loan debt maturity profile.

4.3 Liability Benchmark

4.3.1 The authority is required to estimate and measure the Liability Benchmark for the forthcoming financial year and the following two financial years, as a minimum. There are four components to the Liability Benchmark, also reflected in the graph below:

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.
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. *4.* **Liability benchmark** (or gross loans requirement): this equals net loans requirement plus short-term liquidity allowance. 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.



4.4 Core Funds and Expected Investment Balances

4.4.1 The application of resources to either finance capital expenditure or to support the revenue budget will have an ongoing impact on cash balances available for investment. It is anticipated that treasury investments will be held to manage day to day cashflow requirements, with balances expected to fluctuate throughout the year. Whilst the council holds significant usable reserve balances, due to the strategy of internal borrowing, as outlined within the Borrowing Strategy section, investment balances are expected to be low throughout the year.

4.5 Statutory Repayment of Loans Fund Advances

4.5.1 The authority 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

4.5.2 A variety of options are provided to councils, so long as a prudent provision is made each year. A review of the council's loan fund advances was undertaken during 2019-20 to ensure the council continues to make a prudent provision each year for the repayment of loans fund advances.

4.5.3 For all new loans fund advances the policy for repayment will be in accordance with the following methodology, as appropriate:

1. **Asset life method** – loans fund advances will be repaid with reference to the life of an asset using a 5.1% annuity rate;
2. **Funding / Income profile method** – loans fund advances will be repaid by reference to an associated income stream.

4.5.4 Using the asset life method, the council is required to ensure that the debt is repaid over a period that is reasonably commensurate with that over which the capital expenditure provides benefits. The following table details the repayment period applicable to each asset type.

Asset Type	Repayment Period (Years)
Land (including cemeteries)	100
Road Structures - Bridges, Retaining Walls, Sea Walls, Flood Defences	60
Piers and Harbours - Major Structural Work	60
Piers and Harbours - Medium Term Works e.g painting/cathodic protection	20
Piers and Harbours - Limited Lifespan Improvements	10
Roads and Footways	20
Street Lighting	30
Vehicles & Plant	7
IT Equipment	5
Major Regeneration Works (Public Realm etc)	60
New Builds including Schools	60
Buildings - Electrical	40
Buildings - Plant	20
Buildings - Roofing	35
Buildings - Windows & External Doors	20
Buildings - Structural	25

4.6 Current Treasury Portfolio Position

4.6.1 The overall treasury management portfolio as at 31.3.24 and for the position as at 31 December 2024 are shown below for both borrowing and investments.

TREASURY PORTFOLIO				
	Actual 31 March 2024		Actual 31 December 2024	
Treasury investments	**£m**	**%**	**£m**	**%**
Banks	18.133	55%	10.016	30%
Local Authorities	10.000	30%	0.000	0%
Money Market Funds	1.400	4%	20.000	60%
Third Party Loans (RSLs)	3.543	11%	3.408	10%
Total treasury investments	**33.076**	**100%**	**33.424**	**100%**
Treasury external borrowing				
PWLB	108.877	92%	107.197	95%
Market Loans (LOBO)	5.255	4%	5.255	5%
Temporary Borrowing*	5.256	4%	0.297	0%
Local Bonds	0.018	0%	0.018	0%
Total external borrowing	**119.406**	**100%**	**112.767**	**100%**

**Note: This represents short term borrowing from various institutions.*

4.6.2 The council’s forward projections for borrowing are summarised in the following table. This table shows the actual external debt, against the underlying capital borrowing need, (the Capital Financing Requirement), highlighting any over or under borrowing.

	2025/26 Estimate £m	2026/27 Estimate £m	2027/28 Estimate £m
Debt at 1 April	153	220	275
Expected change in Debt	67	55	37
Other long-term liabilities (OLTL)	106	101	95
Expected change in OLTL	(5)	(6)	(6)
Actual Gross Debt at 31 March	**321**	**370**	**401**
The Capital Financing Requirement	**394**	**415**	**431**
Under / (over) borrowing	**73**	**45**	**30**

4.6.3 Within the range of prudential indicators there are several key indicators to ensure that the authority operates its activities within well defined limits. One of these is that the authority 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 2025/26 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 or speculative purposes.

4.6.4 The council's Section 95 Officer reports that the council has complied with this prudential indicator in the current year and does not envisage difficulties for the future. This view takes account of current commitments, existing plans and the proposals in the 2025-26 Budget Pack in respect of the Capital Plan 2025-28.

4.7 Treasury Indicators: Limits to Borrowing Activity

4.7.1 **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 ability to fund under-borrowing by other cash resources.

Operational Boundary	2025/26 Estimate £m	2026/27 Estimate £m	2027/28 Estimate £m
Debt	293	320	341
Other long-term liabilities	101	95	90
Total	**394**	**415**	**431**

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

- This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total of all local authority plans, or those of a specific authority, although this power has not yet been exercised.

- Council is asked to approve the following Authorised Limit:

Authorised Limit	2025/26 Estimate £m	2026/27 Estimate £m	2027/28 Estimate £m
Debt	298	325	346
Other long-term liabilities	104	98	93
Total	**402**	**423**	**439**

4.8 Prospects for Interest Rates

4.8.1 The council's treasury advisor has provided an update on the current economic position, given within Appendix 1. Part of this advisory service is also to assist the authority to formulate a view on interest rates. The following forecasts have been provided for short term (Bank Rate) and long term (PWLB certainty rates) borrowing.

(a) Long term PWLB rates:

PWLB rates	Dec 2024 %	March 2025 %	March 2026 %	March 2027 %	Dec 2027 %
5 year	5.0	4.9	4.5	4.1	3.9
10 year	5.3	5.1	4.7	4.3	4.1
25 year	5.6	5.5	5.1	4.7	4.5
50 year	5.4	5.3	4.9	4.5	4.3

The current and expected interest rates for long term borrowing from the PWLB highlight a gradual decrease from the current position. The PWLB rates quoted (gilt yields plus 80 bps) take account of the application of a 0.2% certainty rate reduction, introduced by the government in return for council's providing their borrowing forecast information. Argyll and Bute Council is able to access the certainty rate reduction.

(b) Short term borrowing rates:

Bank Rate	Dec 2024 %	March 2025 %	March 2026 %	March 2027 %	Dec 2027 %
	4.75	4.50	3.75	3.50	3.50

The 'Bank Rate' is the official Bank of England rate paid on commercial bank reserves. The current and Bank Rate forecasts also highlight an expected gradual decrease from the current position. Short term borrowing rates will generally fall in line with Bank Rate cuts.

4.8.2 Considerable uncertainty remains around interest rate forecasts. As all PWLB certainty rates are currently significantly above the longer term Bank Rate forecast (10 years 3.25%), borrowing strategies will need to be reviewed in that context. Overall, better value can be obtained at the shorter end. MUFG will continue to monitor economic and market developments as they unfold and advise the authority accordingly. Typically, forecasts are reviewed following the quarterly release of the Bank of England's Monetary Policy Report but will be considered on an ad hoc basis, as required.

4.9 Borrowing Strategy

4.9.1 The council is currently maintaining an under borrowed position. This means that the capital borrowing need, (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the authority's reserve balances and cash flow has been used as a temporary measure (internal borrowing). This strategy is prudent while medium and longer dated borrowing rates are expected to fall from their current levels, albeit only once prevailing inflation concerns are addressed by restrictive near term monetary policy.

4.9.2 Short term borrowing from money markets or other local authorities is currently expected to be cheaper than long term borrowing and will therefore be attractive throughout the financial year. However, as with internal borrowing, short term savings by delaying new long term external borrowing requires to be balanced with potential additional long term costs.

4.9.3 Current PWLB rates are forecast to gradually decrease over the next couple of years. As a result, consideration will be given to the timing of any new fixed rate long term borrowing. Although more expensive in the short term, this may be more cost effective over the longer term and also provides an element of budget certainty in respect of future years.

4.9.4 The council's annual revenue estimates include appropriate provision for financing costs of capital expenditure. The key principles of the strategy will be to minimise debt interest costs over the medium term and to achieve a more even spread in the debt maturity profile. It is anticipated that a range of solutions will be employed in order to mitigate against interest rate risk, and to provide longer term cost certainty, as outlined above.

4.9.5 Against the economic background and the risks within interest rate forecasts, caution will be adopted with the 2025-26 treasury operations. The Section 95 Officer, in conjunction with the treasury advisors, will monitor interest rate forecasts and adopt a pragmatic approach to changing circumstances, with any new borrowing reported to committee at the next available opportunity.

4.10 Policy on Borrowing in Advance of Need

4.10.1 The authority will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums 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 authority can ensure the security of such funds. Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through the mid-year or annual reporting mechanism.

4.11 Rescheduling

4.11.1 The principle reasons for debt rescheduling include:

- The generation of cash savings; and
- To enhance the balance of the debt maturity profile, mitigating the risk of refinancing at a higher rate of interest in any year in the future.

4.11.2 Opportunities for debt rescheduling within the current debt portfolio will be monitored on an ongoing basis throughout the year. There may be potential opportunities to generate savings and enhance the balance of the debt maturity profile by switching from long term debt to short term debt. However, these options would need careful consideration in light of the short term nature of potential savings and the likely cost of re-financing those short term loans on maturity, if required, together with any debt repayment premiums that may be incurred. Whilst premature redemption rates remain elevated, rescheduling opportunities to generate savings are not expected to be available. This would only expect to be undertaken, where a rebalancing of the portfolio, to provide more certainty, is considered appropriate. Any rescheduling undertaken will be reported to Council, at the earliest opportunity.

4.12 New Financial Institutions as a Source of Borrowing

4.12.1 Currently the PWLB Certainty Rate is set at gilts + 80 basis points. However, consideration may still need to be given to sourcing funding from the following sources:

- Local authorities (primarily shorter dated maturities out to 3 years or so – generally still cheaper than the Certainty Rate).
- 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).

Our advisors will keep us informed as to the relative merits of each of these alternative funding sources.

4.13 Approved Sources of Long and Short Term Borrowing

4.13.1 A summary of the council's approved sources and types of borrowing are set out within Appendix 2.

4.14 Treasury and Prudential Indicators 2025-28

4.14.1 A key driver of treasury management activity is the council's capital investment plans. The treasury management function ensures that sufficient cash is available to meet capital spending commitments. Prudential indicators reflect the output from these plans and are designed to ensure that the council's capital investment plans are affordable, prudent and sustainable. Required updates to the prudential and treasury indicators for 2024-25 were outlined within the Treasury Management Strategy Mid-year Review Report, approved by Council on 20 December 2024. The prudential and treasury indicators for 2025-26 to 2027-28 are outlined in Appendix 3 and reflect the proposed Capital Plan 2025-28. These indicators are relevant for the purpose of setting an integrated treasury management strategy.

5. ANNUAL INVESTMENT STRATEGY

5.1 Investment Policy

5.1.1 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")

5.1.2 The council's investment priorities, in order of importance, will be security, minimising the risk of any loss on the principal sum invested; portfolio liquidity, ensuring that cash is available when required; and yield (return), the rate of interest earned from the investment. The authority will aim to achieve the optimum return on its investments, commensurate with proper levels of security and liquidity, and with regard to the authority's risk appetite. The risk appetite of the council will be low, with security of investments the key priority.

5.1.3 In the current economic climate, it is considered appropriate to maintain a degree of liquidity to cover cash flow needs but to also consider opportunities for 'laddering' investments for periods up to 12 months with high credit rated financial institutions, whilst investment rates remain elevated.

5.1.4 The borrowing of monies purely to invest or on-lend and make a return is not permitted and the council will not engage in such activity. The limit of investments will reflect the level of available council reserve fund balances and borrowing in advance to meet capital financing requirements, in line with the borrowing strategy, together with provision for managing the council's day to day cash flow requirements.

5.1.5 The guidance from the Scottish Government and CIPFA places a high priority on the management of risk. This authority has adopted a prudent approach to managing risk and defines its risk appetite by the following means:

1. Minimum acceptable credit criteria are applied in order 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’ (CDS) 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 financial sector, in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.
4. This council has defined the list of types of investment instruments that the treasury management team are authorised to use and lending limits (amounts and maturity). A limit for the amount of its investments which are invested for longer than 365 days has also been set.
5. Investments will only be placed with counterparties from countries with a specified minimum sovereign rating and all investments will be denominated in sterling.

However, the council will also pursue value for money in treasury management and will monitor the yield from investment income against appropriate benchmarks for investment performance throughout the year.

5.1.6 Investment instruments identified for potential use during the year, together with associated treasury risk mitigations and monetary limits, are outlined in Appendix 4. Information on Environmental, Social and Governance (ESG) considerations is also provided. Within the constraints of the policy, due consideration will be given to the diversification of investments**,** in order to limit a concentration of investments with too few counterparties or countries, and to ESG factors**.**

5.1.7 There has been considerable change in the types of investment instrument brought to the market in recent years. Given the fluidity of this area, members will be kept informed and requested to approve the use of any new instruments, as appropriate, in order to allow maximum flexibility.

5.2 Creditworthiness Policy

5.2.1 The council applies the creditworthiness service provided by MUFG (formerly Link Group). This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies - Fitch, Moody’s and Standard & Poor’s. The credit ratings of counterparties are supplemented with the following overlays: -

1. “watches” and “outlooks” from credit rating agencies;
2. CDS spreads that may give early warning of changes in credit ratings;
3. sovereign ratings to select counterparties from only the most creditworthy countries.

5.2.2 This modelling approach combines credit ratings, and any assigned Watches and Outlooks, in a weighted scoring system, which is then combined with an overlay of CDS spreads. The end product of this is a series of colour coded bands, which indicate the relative creditworthiness of counterparties. These colour codes are used by the authority to determine the suggested duration for investments.

5.2.3 All credit ratings will be monitored on an ongoing basis throughout the year. Through its use of the MUFG creditworthiness service, the council is alerted to changes to ratings of all three agencies and will also be advised of information in movements in Credit Default Swap spreads and other market data on a daily basis. If a downgrade results in the counterparty / investment scheme no longer meeting the authority's minimum criteria, its further use as a new investment will be withdrawn immediately. Sole reliance will not be placed on the use of this external service. All available information will be considered when making investment decisions.

5.2.4 The council will continue to limit exposure to credit risk by ensuring that all investments are placed with the higher rated bodies from a weekly credit list of worldwide potential counterparties. For illustration purposes, a snapshot of this counterparty list as at 7 February 2025 is provided in Appendix 5.

5.2.5 The council essentially adopts a hybrid approach in formulating its creditworthiness policy. In addition to the MUFG creditworthiness service, which provides details of the most highly credit rated institutions (counterparties) and suggested investment durations, the council also places a monetary limit on each type of investment or counterparty, as outlined within Appendix 4. These investment criteria will be kept under review throughout the year and amended, if required, to ensure that they continue to be fit for purpose.

5.3 Investment Strategy

5.3.1 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. Accordingly, while most cash balances are required in order to manage the ups and 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.

5.3.2 The current forecast shown in paragraph 4.8.1 includes a forecast for Bank Rate to fall to a low of 3.5%. However, as there are so many variables at this time, caution must be exercised in respect of all interest rate forecasts. 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	%
2025/26	4.10%
2026/27	3.70%
2027/28	3.50%

5.3.3 For its cash flow generated balances, the authority will seek to utilise its business reserve instant access accounts, Money Market Funds and short-dated deposits, (overnight to 100 days), in order to benefit from the compounding of interest.

5.3.4 An investment treasury indicator and limit requires to be set in respect of total principal funds invested for greater than 365 days. These limits are set with regard to the authority'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. The council is asked to approve the following Treasury Indicator and limit:

Upper limit for principal sums invested for longer than 365 days			
	2025/26 £m	**2026/27 £m**	**2027/28 £m**
Principal sums invested for longer than 365 days	20	20	20
Current investments in excess of 1 year maturing in each year	0	0	0

5.4 Investment Performance / Risk Benchmarking

5.4.1 The Section 95 Officer will continue to monitor the economic environment and adopt a pragmatic approach to changing circumstances. A balanced view of risk against return will be taken in respect of all investments. The authority may use an investment benchmark to assess the investment performance of its investment portfolio of overnight, 7 day, 1, 3, 6 or 12 month compounded SONIA (Sterling Overnight Index Average), as appropriate. However, it is anticipated that return on investments will be limited in 2025-26, as a result of Bank Rate forecasts and the over-riding principal of risk aversion. Investment activity will be reported at the end of the financial year, as part of the Annual Treasury Report.

5.5 Non-treasury investments

5.5.1 Non-treasury investments are defined as the following categories:

- All shareholding, unit holding and bond holding, including those in a local authority owned company;
- Loans to a local authority company or other entity formed by a local authority to deliver services;
- Loans made to third parties; and
- Investment property.

5.5.2 Any such finance arrangements or loans would be subject to specific committee approval. The authority may make loans to third parties, where this is consistent with meeting the service objectives of the council and for which, specific statutory provision exists. For service reasons, loans to third parties may be offered at an interest rate below the market rate. Where the loan is advanced at less than a market interest rate, there is an associated loss of investment return, which would otherwise have been earned on these resources. Any cost to the council in this respect will be reflected in the authority's annual accounts. All loans to third parties will be recognised as investments and detailed within the Annual Investment Report.

6. Capital Strategy

6.1 The CIPFA 2021 Prudential and Treasury Management Codes places a requirement on local authorities to prepare a Capital Strategy. The Capital Strategy demonstrates how capital expenditure, capital financing and treasury management activity contribute to the provision of services and longer term policy objectives of the council. It also provides an overview of how associated risk is managed and the implications for future financial sustainability. An updated Capital Investment Strategy was approved by Policy and Resources Committee in August 2023. This will be reviewed and updated, as appropriate, as part of a planned review of capital arrangements, to be undertaken during the 2025-26.

7. Training

7.1 The CIPFA Code requires the proper officer to ensure that members with responsibility for treasury management receive adequate training. This especially applies to Members responsible for scrutiny. Members of the Audit and Scutiny Committee received training from the council's treasury advisors, Link Group in October 2024, to assist with this scrutiny role. Members are advised to notify Financial Services as/when they feel further training sessions would be beneficial. Furthermore, the training needs of treasury management officers are periodically reviewed to ensure appropriate treasury management knowledge and skills for those responsible for management, delivery, governance and decision making.

8. Policy on Use of External Service Providers

8.1 The authority uses MUFG (formerly Link Group), as its external treasury management advisors, to acquire access to specialist skills and resources. However, it is recognised that responsibility for treasury management decisions remains with the council. All decisions will be undertaken with due regard to all available information, including from our treasury advisers. For short term market borrowing and investments, the council utilises a number of brokers to access sterling cash markets. This ensures that the council ensures best value in daily cash flow management.

9. Scheme of Delegation and Role of the Section 95 Officer

9.1 The treasury management scheme of delegation, together with the treasury management role of the Section 95 officer and nominated Member, are outlined in Appendix 6.

10. CONCLUSION

10.1 The Treasury Management Strategy provides a comprehensive statement of treasury management policies and planned activities, covering the relevant treasury and prudential indicators, the current and projected debt positions, and the Annual Investment Strategy for 2025-26.

10.2 A key driver of treasury management activity is the council's capital investment plans. Prudential indicators reflect the output from these plans and are designed to ensure that the council's capital investment plans are affordable, prudent and sustainable. Within the range of prudential indicators, there are several key indicators to ensure that the authority operates its activities within well defined limits.

10.3 Whilst the Capital Financing Requirement represents an underlying need to borrow, the council is currently maintaining an under-borrowed position. This strategy is prudent while medium and longer dated borrowing rates are expected to fall from their current levels, albeit that considerable uncertainty remains around interest rate forecasts.

10.4 The council's revenue budget includes appropriate provision for financing costs of capital expenditure. The key principles of the borrowing strategy will be to minimise debt interest costs over the medium term and to achieve a more even spread in the debt maturity profile.

10.5 The council's investment priorities will be security, liquidity and yield (return). A prudent approach to managing investment risk has been adopted. Exposure to credit risk will be limited by ensuring that all investments are placed with the higher rated bodies. A balanced view of risk against return will be taken in respect of all investments. It is anticipated that return on investments will be limited in 2025-26, as a result of Bank Rate forecasts and the over-riding principal of risk aversion.

11. IMPLICATIONS

11.1	Policy		Sets the policy for borrowing and investment decisions.
11.2	Financial		Provides the Treasury Management Strategy for 2025-26, including the Annual Investment Strategy.
11.3	Legal		None
11.4	HR		None
11.5	Fairer Duty Scotland:		
	10.5.1	Equalities – protected characteristics	None
	10.5.2	Socio-economic Duty	None
	10.5.3	Islands	None
11.6	Climate Change		None
11.7	Risk		Provides an overview of treasury management and investment risk, and how these risks are managed.
11.8	Customer Service - None		None
11.9	The Rights of the Child (UNCRC)		None

Kirsty Flanagan
Executive Director/S95 Officer
10 February 2025

Councillor Ross Moreland, Policy Lead for Finance and Commercial Services

APPENDICES:
Appendix 1 – Economic Background
Appendix 2 - Approved Sources and Types of Borrowing
Appendix 3 – Treasury and Prudential Indicators 2025-28
Appendix 4 – Permitted Investments
Appendix 5 – Example Weekly Counterparty List
Appendix 6 – Scheme of Delegation; Section 95 Officer and Nominated Member Roles

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