TREASURY MANAGEMENT ACTIVITY DURING 2024/25

BORROWING REQUIREMENT AND DEBT MANAGEMENT

1. The council has a forecast net borrowing requirement of £190.7M by the 31st March 2025, arising from its revenue and capital income and expenditure. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while useable reserves and working capital are the underlying resources available for investments. These are the core drivers of Treasury Management (TM) Activity, and the year-on-year change is summarised in table 1.

   Included within this figure is the total EFS (£121.6M) that is available to the council during 2024/25 to allow the council time to develop savings and transformation plans to reduce the structural budget deficits in future years, this figure is likely change as EFS plans are further developed, including the level of requirement and its funding

2. The current strategy, given the increasing borrowing requirement, is to minimise both external borrowing and investments and to only borrow to the level of the net borrowing requirement. The reasons for this are to reduce credit risk, take pressure off the Council's lending list and to avoid the cost of carry (i.e. borrowing cash and paying interest on it before it is needed) in the current interest rate environment.

Table 1 – Balance Sheet Summary

	31-Mar-24 Actual £M	31-Mar-25 Outturn £M	31-Mar-25 Forecast £M	31-Mar-25 Forecast Movement in year £M
General Fund CFR	345.36	469.27	464.63	119.27
Housing CFR	182.05	198.25	210.41	28.36
Total CFR	**527.41**	**667.52**	**675.04**	**147.63**
Less Other Debt Liabilities*	(53.45)	(49.12)	(49.12)	4.33
Loans CFR	**473.96**	**618.40**	**625.92**	**151.96**
Less External Borrowing**	(312.59)	(281.99)	(282.00)	30.59
Internal (over) Borrowing	**161.37**	**336.41**	**343.92**	**182.55**
Balance sheet Resources	(197.23)	(193.76)	(193.76)	3.47
Treasury Investments	35.86	48.00	48.00	12.14
New Borrowing or (Investments)	**0.00**	**190.65**	**198.16**	**198.16**

** finance leases, PFI liabilities and Transferred debt that form part of the council 's total debt*
*** See Table 3 below*

3. The forecast movement in coming years is one of the Prudential Indicators (PIs) and measures the cumulative outstanding amount of debt, this increases with new debt-financed capital expenditure and reduces with MRP repayments and capital receipts used to replace debt. Movement since the last reported position is shown below.

Table 2 – Capital Financing Requirement Movement in year

Capital Financing Requirement	31/03/2024 Actual £M	31/03/2024 Last Reported (Outturn) £M	31/03/2025 Forecast £M	Movement since last reported position £M
Balance Brought forward	342.57	345.36	345.36	0.00
New Borrowing	15.14	143.78	133.07	(10.71)
MRP	(8.69)	(15.53)	(9.46)	6.07
Appropriations (to) from HRA	0.00	0.00	0.00	0.00
Movement in Other Liabilities	(3.66)	(4.34)	(4.34)	0.00
Total General Fund Debt	**345.36**	**469.27**	**464.63**	**(4.64)**
HRA	182.05	198.25	210.41	12.16
Total CFR	**527.41**	**667.52**	**675.04**	**7.52**
Estimated Debt (*see below for breakdown*)	366.05	509.62	516.12	6.50
Under / (Over) Borrowed	**161.36**	**157.90**	**158.92**	**1.02**

4. The treasury management position at 30th September and the change over the six months is shown in tables 3 and 4 below together with activity in the year.

5. ***Table 3: Borrowing and Investment Position***

	31-Mar-24 Actual £M	31-Mar-24 Average %	30-Sep-24 Actual £M	30-Sep-24 Average %	31-Mar-25 Forecast £M	31-Mar-25 Forecast %
Long Term Borrowing						
Public Works Loan	288.59	3.47	283.29	3.47	463.00	2.96
LOBO Loans from Banks	4.00	4.86	4.00	4.86	4.00	4.85
	292.59	**3.58**	**287.29**	**3.58**	**467.00**	**3.00**
Short Term Borrowing						
Other Local Authorities	20.00	5.79	29.00	5.29	0.00	5.79
Total External Borrowing	**312.59**	**2.98**	**316.29**	**3.62**	**467.00**	**3.11**
Other Long Term Liabilities						
PFI Schemes	41.08	9.82	41.08	9.56	37.11	9.82
Deferred Debt Charges (HCC)	12.37	4.99	12.37	3.27	12.01	4.99
Total Gross External Debt	**366.04**	**3.97**	**369.74**	**4.08**	**516.12**	**3.97**
Investments:						
Managed In-House						
Cash (Instant access)	(7.83)	5.27	(16.78)	5.01	(20.00)	5.40
Long Term Bonds	(1.03)	5.27	(1.02)	5.27	(1.00)	5.27
Managed Externally						
Pooled Funds (CCLA) & Shares	(27.00)	4.76	(27.00)	4.76	(27.00)	3.00
Total Investments	**(35.86)**	**4.78**	**(44.80)**	**4.78**	**(48.00)**	**4.05**
Net Debt	**330.18**		**324.94**		**468.12**	

6. *Table 4: Movement in Borrowing during the year*

Movement during the year	2023/24 Actual £M	2024/25 Movement in year £M	30-Sep-24 £M	Average Life
Long-term borrowing Carried Forward	298.19		292.59	
Maturities in year	(15.60)		(5.30)	
New borrowing taken in year	10.00		0.00	
Net Long Term Borrowing	**292.59**	**(5.30)**	**287.29**	**24 Years**
Short-term borrowing Carried Forward	5.00		20.00	
Maturities in year	(5.00)		(20.00)	
New borrowing taken in year	20.00		29.00	
Net Short Term Borrowing	**20.00**	**9.00**	**29.00**	**1.4 Months**
Total Borrowing	**312.59**	**3.70**	**316.29**	

Please note that these figures do not reflect the accounting convention of moving loans maturing in the year from long term to short term so will differ from the maturity analysis.

7. The maturity analysis of the Council's long-term debt at 30th September 2024 is further analysed below, in table 5. LOBO loans are shown as uncertain as although they are within the call option, and given the current interest environment there is a possibility they could be called in.

8. *Table 5: Maturity Structure of Long Term Borrowing*

Analysis of Loans by Maturity	Lower Limit	Upper Limit	Compliance with Limit	Outstanding 30/09/2024 £M	% of Debt
Less than 1 Year	0	50	Yes	5.30	2
Between 1 and 2 years	0	50	Yes	10.60	4
Between 2 and 5 years	0	50	Yes	31.80	11
Between 5 and 10 years	0	55	Yes	60.50	21
Between 10 and 20 years	0	60	Yes	30.25	11
Between 20 and 40 years	0	60	Yes	144.84	50
Over 40	0	75	Yes	0.00	0
Uncertain Date**	0	5	Yes	4.00	1
				287.29	**100**

Borrowing Update

9. CIPFA's Prudential Code is clear that local authorities must not borrow to invest primarily for financial return and that it is not prudent for local authorities to make any investment or spending decision that will increase the capital financing requirement, and so may lead to new borrowing, unless directly and primarily related to the functions of the Authority. PWLB loans are no longer available to local authorities planning to buy investment assets primarily for yield unless these loans are for refinancing purposes.

	Currently £27M is held in commercial investments that were purchased prior to the change in the CIPFA Prudential Code. Before undertaking further additional borrowing the council will review the benefits of retaining these investments against cost of future borrowing.
Borrowing Strategy	
10.	At 30th September the council held £316.29M of loans, (an increase of £3.70M since 31st March 2024), as part of its strategy for funding previous and current years' capital programmes and the need to externalise borrowing as a result of falling reserves. Outstanding loans are summarised in Table 4 and 5 above.
11.	We have remained under our CFR limit and had internal borrowing of £161.37M at the end of 2023/24 compared to £157.14M for 2022/23. This strategy enabled a reduction in net borrowing costs (despite foregone investment income) and reduced overall treasury risk.
12.	As outlined in the treasury strategy, the chief objective when borrowing has been to strike an appropriately risk balance between securing lower interest costs and achieving cost certainty over the period for which funds are required, with flexibility to renegotiate loans should long-term plans change being a secondary objective. The borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. At the present time short term interest rates are higher than long term interest rates.
13.	After substantial rises in interest rates since 2021 many central banks have now begun to reduce rates, albeit slowly. Gilt yields were volatile over the 6-month period and have reduced slightly between April and September 2024. Much of the downward pressure from lower inflation figures was counteracted by upward pressure from positive economic data. Data from the US continues to impact global bond markets including UK gilt yields.
14.	The PWLB certainty rate for 10-year maturity loans was 4.80% at the beginning of the half year and 4.79% at the end. The lowest available 10-year maturity rate was 4.52% and the highest was 5.18%. Rates for 20-year maturity loans ranged from 5.01% to 5.57% during the half year, and 50-year maturity loans from 4.88% to 5.40%.
15.	Whilst the cost of short-term borrowing from other local authorities spiked to around 7% in late March 2024, primarily due a dearth of LA-LA lending/borrowing activity during the month, as expected shorter-term rates reverted to a more normal range and were generally around 5.00% - 5.25%. The average rate for short-term loans at 30th September 2024 on £29M was 5.29%. Any borrowing will be done in consultation with our advisors as although short term borrowing is currently higher than 20 year maturity debt at 5.27% (5.47% less 0.20% certainty discount), long term debt is expected to fall in the medium term and the overall costs assessed.
16.	The PWLB HRA rate which is 0.4% below the certainty rate is available to June 2025. The discounted rate is to support local authorities borrowing for the Housing Revenue Account and for refinancing existing HRA loans, providing a window of opportunity for HRA-related borrowing and to replace £12M of loans relating to the HRA maturing during this time frame.

17.	During the first 6 month of the year, no long term loans were taken, and short term borrowing is detailed in Table 6 below, of the £39M taken £29M is currently still outstanding.

Table 6: New loans taken in 2024/25

Loans Taken in Year	Date	Amount £M	Rate %	Period
Local Authority Loan 1	17/05/2024	5,000,000	5.350%	6 Months
Local Authority Loan 2	16/05/2024	5,000,000	5.350%	2.5 Months
Local Authority Loan 3	20/05/2024	5,000,000	5.350%	4 Months
Local Authority Loan 4	20/05/2024	2,000,000	5.350%	6 Months
Local Authority Loan 5	20/05/2024	2,000,000	5.350%	6 Months
Local Authority Loan 6	18/06/2024	5,000,000	5.350%	6 Months
Local Authority Loan 7	22/08/2024	5,000,000	5.000%	3 Months
Local Authority Loan 8	20/09/2024	5,000,000	4.950%	3 Months
Local Authority Loan 9	24/09/2024	5,000,000	5.050%	2 Weeks
Total Borrowing		**39,000,000**		

18.	This will be kept under review during 2024/25 with the need to resource the capital programme. In addition, given the rising costs of materials and of borrowing, the capital programme will be kept under regular review to ensure ongoing Value for Money and the phasing of capital works reviewed to ensure capital financing budgets accurately reflect the profile of borrowing needed. The council with its advisor Arlingclose will evaluate and pursue options for lower cost solutions and opportunities, together with the 'cost of carry' and breakeven analysis.
19.	The PWLB remained the Council's preferred source of long term borrowing in 2024/25, given the transparency and control that its facilities continue to provide. However, PWLB funding margins have lurched quite substantially and there remains a strong argument for diversifying funding sources, particularly for the HRA who are not restricted to borrowing from PWLB, like the general fund, (as a result of the Council being awarded extraordinary financial support), if rates can be achieved on alternatives which are below gilt yields + 0.80%. This is kept under constant review in consultation with our TM advisors.
20.	The chart below shows the pattern of the PWLB Certainty Rate 3-month moving average over the last year. Rates fell sharply in both August and September for a few days following market events but have since been on an upward trajectory.

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21.	Borrowing decisions are not predicated on any one outcome for interest rates and a balanced portfolio of short and long term borrowing was maintained.

<u>Loan Restructuring</u>

22.	The continuing rise in gilt yields since early 2022 resulted in some PWLB loans being in or close to a discount position if repaid early. However, as these would need to be replaced by new loans at higher interest rates, this isn’t a cost-effective option.

<u>Lender’s Option Borrower’s Option Loans (LOBOs)</u>

23.	LOBO (Lender’s Option Borrower’s Option) loans are where the lender has the option to propose an increase in the interest rate at set dates, which can either be accepted or repay the loan at no additional cost. As reported previously with market interest rates having risen, the probability of LOBOs being called increased. The remaining £4M LOBO loans has call dates within the next 12 months, we will continue to monitor and take appropriate action.

<u>Other Debt Activity</u>

24.	Although not classed as borrowing the Council has previously raised capital finance via Private Finance Initiative (PFI). The forecast balance at the end of the year, after allowing for repayment in year of £3.29M is £37.11M.
25.	In addition, the council holds debt in relation to debt transferred from Hampshire County Council of £12.19M from when we became a unitary authority on the 1 April 1997. This is being repaid over 50 years at £0.36M per annum.

INVESTMENT ACTIVITY

26.	Both the CIPFA Code and government guidance require the Authority to invest its funds prudently, and to have regard to the security and liquidity of its treasury investments before seeking the optimum rate of return, or yield. The objective when investing money is to strike an appropriate balance between risk and return,

	minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.
27.	As demonstrated by the liability benchmark in this report, the council expects to be a long-term borrower and new treasury investments are therefore primarily made to manage day-to-day cash flows using short-term low risk instruments. The existing portfolio of strategic pooled funds will be maintained to diversify risk into different asset classes and boost investment income
28.	The Council maintained its strategy of offsetting investment and borrowing to reduce treasury costs.
29.	Invested funds represent income received in advance of expenditure plus balances and reserves. During the year investment balances have ranged between £90.30M and £35.83M and are currently £44.80M and expected to be £48.00M by year end. Movement in year is summarised in Table 7 below.
30.	***Table 7: Investment activity during the year***

	Balance on 01/04/2023	Investments Repaid	New Investments	Balance on 30/09/2022	(Increase)/ Decrease in Investment for Year	Average Life of Investments
	£M	£M	£M	£M	£M	Life
Multi- National Bonds (not subject to bail in)	(1.03)	(0.00)	0.00	(1.02)	0.00	6 months
Money Market Funds and Call Account	(7.83)	236.29	(245.23)	(16.78)	(8.95)	on day notice
Government & Local Authority	0.00	89.40	(89.40)	0.00	0.00	0 days
Managed Externally (CCLA Pooled funds)	(27.00)	0.00		(27.00)	0.00	Unspecified
Total Investments	**(35.86)**	**325.68**	**(334.63)**	**(44.80)**	**(8.94)**	

31.	Bank Rate reduced from 5.25% to 5.00% in August 2024 with short term interest rates largely being around these levels. The rates on DMADF deposits in last quarter ranged between 5.19% and 5.20% and money market rates between 4.94% and 5.20%. Forecast income is now £2.54M, slightly higher (£0.31M) than originally budgeted £2.23M.
32.	Security of capital has remained the council's main investment objective. This has been maintained by following the counterparty policy as set out in its TM Strategy Statement. The council has adopted a voluntary measure of its exposure to credit risk, by monitoring the average credit rating of its investment portfolio, which is supplied by our advisors. This is calculated by applying a score to each investment (AAA=1, AA+=2, etc.) and taking the arithmetic average, weighted by the size of each investment.

	Target	Actual
Portfolio average credit rating	A	A+

33.	Counterparty credit quality is assessed and monitored with reference to credit ratings across rating agencies Fitch, S&P and Moody's. The council's minimum long-term counterparty rating is A-. For financial institutions analysis is of funding structure and susceptibility to bail-in, credit default swap prices, financial statements, information on potential government support and reports in the quality financial press.

34. **Benchmarking:** Our advisors produce quarterly benchmarking which shows the breakdown of our investments and how we compare to their other clients and other English Unitary. A summary is shown below, Appendix 3 shows full analysis.

	Credit Score	Credit Rating	Bail-in Exposure	Weighted Average Maturity	Rate of Return %
31.03.2024	4.52	A+	89%	44	5.06
30.09.2024	4.53	A+	94%	12	5.12
Similar LAs	4.65	A+	60%	100	5.09
All LAs	4.60	A+	61%	11	4.90

35. Investments managed internally are currently averaging a return of 5.03% (which is slightly higher than both the average unitary authority at 5.01% and other LA's at 4.91%), whilst maintaining the same credit rating of A+.

Total income returns at 5.12% is also slightly higher than other unitary (5.09%) and above LA's (4.90%).

Due to operating on a cash flow basis for investments to avoid higher borrowing costs and maintained lower cash balances, £17.8M compared to £55.7M for other Unitaries and £60.1M for other Local Authority, which accounts for our higher than average funds exposed to bail in but as these are available on 1 day notice, there are no concerns with this.

Cash is performing well in the current financial environment which accounts for our total return (after allowing for loss on our strategic funds) is lower 3.39% compared to 5.50% for other Unitaries and 5.42% for other Local Authority but has performed better over the last the medium term, see paragraph 42 below.

We hold 58% of our investments in historic strategic funds which offer higher return over the long term, as detailed in paragraphs 23 to 28. The capital value of our external strategic funds has increased slightly, £0.04M in the quarter. The income return over the longer term was and remains the driver to invest, although this is kept under review for opportunities to divest.

Liquidity Management

36. In keeping with the DLUHC's Guidance on Investments, the Council maintained a sufficient level of liquidity through the use of Money Market Funds and call accounts. There is no perceived risk that the Council will be unable to raise finance to meet its commitments. The Council also has to manage the risk that it will be exposed to replenishing a significant proportion of its borrowing at a time of unfavourable interest rates. The Council would only borrow in advance of need where there is a clear business case for doing so and will only do so for the current capital programme or to finance future debt maturities.

Externally Managed Funds

37. The council has invested £27M in pooled property funds as an alternative to buying property directly. As previously reported these funds offer the potential for enhanced returns over the longer term but may be more volatile in the shorter term. They are managed by professional fund managers which allows diversification into asset classes other than cash without the need to own and manage the underlying investments.

38. These funds have no defined maturity date but are usually available for withdrawal after a notice period (180 days). The performance and continued suitability in meeting the investment objectives is regularly reviewed.

Strategic fund investments are made in the knowledge that capital values will move both up and down on months, quarters and even years; but with the confidence that over a three to five-year period total returns will exceed cash interest rates.

39. UK commercial property values started to stabilise, then improve slightly towards the end of the period, with interest rates being cut from their peak and investor attention turning to the timing of further interest rate cuts. Transaction activity remains somewhat subdued but signs of recovery in the occupier and rental markets as well as moderate economic growth and further falling interest rates are hoped to be favourable for an improving property sector outlook over the medium term. Capital growth is expected to be gradual while income levels remain strong for many sub-sectors.

40. Considering the performance over the long-term and the latest cash flow forecasts, these funds have been maintained but will be monitored carefully especially as the statutory override on accounting for gains and losses on pooled investment funds is likely to end on 31st March 2025, when any difference between initial investment and the current value will be a cost/gain. The Investment Risk reserve was created to mitigate the impact of the statutory override not being extended and unrealised losses being recognised.

Tables 9 below shows current value and income due in year, together with the performance of the fund since we invested compared to cash.

We have ongoing discussions with Arlingclose about the implications for the investment strategy and what action may need to be taken, current advice is to give notice on part of the fund once we have seen two consecutive increases in the value of fund.

41. The change in the funds' capital values and income earned in 2024/25 is shown below.

Table 9 – Property Fund Performance 2024/25

Quarter Ending	Valuation £M	Movement since Reported in SOA	Dividends £M
1st April	24.79		
30th June	24.67	(0.12)	0.34
30th September	24.71	(0.09)	0.32 *
Total			0.66
**Forecast*			

42. Although there is currently an unrealised capital loss of £2.29M at 30 September 2024, since investing £9.76M of dividends have been earned, a net return of £7.47M which equates to an annualised income return of 3.86% compared to the average bank rate of 1.27% for the same period. This also compares favourably to the investments that were made directly in property, which gave a net return of 2.13% in 2023/24 after financing costs as detailed below.

STRATEGIC POOLED FUND PORTFOLIO			SOUTHAMPTON CITY				From:	01/05/2014	To:	30/09/2024
FUND NAME	ASSET CLASS	No of Units Held in Period	Current Value £	Capital Growth £	Dividends Earned £	Holding Period (yrs)	Capital Return	Income Return	Total Return	Volatility
CCLA - LAMIT PROPERTY FUND	PROPERTY	9,091,173	24,706,172	-2,293,833	9,755,501	8.1	-8.50%	36.13%	27.64%	5.2%
GRAND TOTAL			24,706,172	-2,293,833	9,755,501	8.1	-8.50%	36.13%	27.64%	5.2%
			Unrealised capital loss since purchase:	-2,293,833		Annualised income return:		3.86%		
						Average Bank Rate:		1.27%		

43.	To cover future risk of any loss on the CCLA pooled property fund due to the expectation that statutory override will cease in 2026/27, £0.80M has transferred to the Investment Risk Reserve, with a further transfer of £0.40M to be made in 2024/25 and a further £0.40M earmarked for 2025/26.

Non – Treasury Investments

44.	The definition of investments in CIPFA's TM Code covers all the financial assets, as well as other non-financial assets which are held primarily for financial return. Investments that do not meet the definition of TM investments (i.e., management of surplus cash) are categorised as either for service purposes (made explicitly to further service objectives) and or for commercial purposes (made primarily for financial return).
45.	Investment guidance issued by the DLUHC also broadens the definition of investments to include all such assets held partially or wholly for financial return.
46.	Between 2016 and 2017, SCC implemented a strategy to invest in commercial properties with the expected return on investment being used to fund council services, known as the Property Investment Fund (PIF). To date the council has purchased 3 properties.
47.	The rate of return on investment in 2024/25 before borrowing costs and other on-costs was 6.03%. Borrowing costs of 3.90% were incurred giving a net rate of return of 2.13%.
48.	All of the properties remain fully let and the tenants are meeting their financial obligations under the leases (although one tenant has vacated the premises but continues to honour the lease). A full review of all assets is underway and may result in disposals in year.
49.	Investment properties are required to be revalued every year. The current valuation for those within the PIF is £25.19M, an increase in value compared with last year of £1.37M. Under current accounting rules changes in the value of investment properties do not impact on the General Fund.

50. **Table 10: Property Investment Fund**

Property	Actual	31.03.2023 Actual		31.03.2024 Actual		Outstanding Debt 31.03.2024	Outstanding Debt 31.03.2025
	Purchase Cost £M	Value in Accounts	Gain or (Loss) in Year	Value in Accounts	Gain or (Loss) in Year	£M	£M
Property 1	6.47	4.79	(0.09)	5.43	0.64	5.75	5.68
Property 2	14.69	10.61	(1.03)	11.52	0.91	13.05	12.91
Property 3	8.53	8.42	(0.74)	8.24	(0.18)	7.57	7.49
	29.69	23.82	(1.86)	25.19	1.37	26.37	26.08

MRP Regulations

51.	On 10th April 2024 amended legislation and revised statutory guidance were published on Minimum Revenue Provision (MRP). The majority of the changes take effect from 2025/26, although there is a requirement that for capital loans given on or after 7th May 2024 sufficient MRP must be charged so that the outstanding CFR in

	respect of the loan is no higher than the principal outstanding less the Expected Credit Loss (ECL) charge for that loan. The regulations also require that local authorities cannot exclude any amount of their CFR from their MRP calculation unless by an exception set out in law. Capital receipts cannot be used to directly replace, in whole or part, the prudent charge to revenue for MRP (there are specific exceptions for capital loans and leased assets). The MRP policy is reviewed and updated annually, and our TM advisors have offered to carry out an MRP health check to ensure that the policy complies with the updated guidance, provides a prudent level of MRP and identify any opportunities to recalculate the annual charge.
Compliance	
52.	The Chief Finance Officer reports that all TM activities undertaken during the year complied fully with the principles in the TM Code and the approved TM Strategy.