

## Appendix 1

### Treasury Management Strategy Statement 2026/27

#### 1. Introduction

##### 1.1 Treasury Management Overview

Treasury management is the management of the Council's cash flows, borrowing and investments, and the associated risks. The Council has borrowed and invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of financial risk are therefore central to the Council's prudent financial management.

Treasury risk management at the Council is conducted within the framework of the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice 2021 Edition* (the CIPFA Code) which requires the Council to approve a Treasury Management Strategy before the start of each financial year. This report fulfils the Council's legal obligation under the *Local Government Act 2003* to have regard to the CIPFA Code.

Investments held for service or commercial purposes are considered in the Capital & Investment Strategy document which is included as an appendix to the Council's Budget and Council Tax 2026/27 and Financial Outlook

##### 1.2 External Context

###### 1.2.1 Economic Background (per Arlingclose January 2026):

The most significant impacts on the Council's Treasury Management Strategy for 2026/27 are expected to include: the influence of the Government's 2025 Autumn Budget, lower short-term interest rates alongside higher medium- and longer-term rates, slower economic growth, together with ongoing uncertainties around the global economy, stock market sentiment, and geopolitical issues.

The Bank of England's Monetary Policy Committee (MPC) cut Bank Rate to 3.75% in December 2025, as had been widely expected. The vote to cut was 5-4, with the minority instead favouring holding rates at 4.00%. Those members wanting a cut judged that disinflation was established while those preferring to hold Bank Rate argued that inflation risks remained sufficiently material to leave rates untouched at this stage.

Figures from the Office for National Statistics showed that the UK economy expanded by 0.1% in the third quarter of the calendar year, this was unrevised from the initial estimate. The most recent Monetary Policy Report (November) projected modest economic growth, with Gross Domestic Product (GDP) expected to rise by 0.2% in the final calendar quarter of 2025. Annual growth is forecast to ease from 1.4% before improving again later,

reflecting the delayed effects of lower interest rates, looser monetary conditions, stronger global activity, and higher consumer spending. The view of modest economic growth going forward was echoed by the Office for Budget Responsibility in its Economic and fiscal outlook published in line with the Autumn Statement which revised down its estimate of annual real GDP to around 1.5% on average between 2025 and 2030.

Consumer Price Index (CPI) inflation was 3.2% in November 2025, down from 3.6% in the previous month and below the 3.5% expected. Core CPI eased to 3.2% from 3.4%, contrary to forecasts of remaining at 3.6%. Looking forward, the MPC continues to expect inflation to fall, to around 3% in calendar Q1 2026, before steadily returning to the 2% target by late 2026 or early 2027.

The labour market continues to ease with rising unemployment, falling vacancies and flat inactivity. In the three months to October 2025, the unemployment rate increased to 5.1%, higher than the level previously expected by the Bank of England (BoE), while the employment rate slipped to 74.9%. Pay growth for the same period eased modestly, with total earnings (including bonuses) growth at 4.7% and while regular pay was 4.6%.

The US Federal Reserve also continued to cut rates, including reducing the target range for the Federal Funds Rate by 0.25% at its December 2025 meeting, to 3.50%-3.75%, in line with expectations. The minutes of the meeting noted that most Fed policymakers judged that further rate cuts would be likely in 2026 if inflation continues to ease, however they were still divided in their assessment of the risks between inflation and unemployment.

The European Central Bank (ECB) kept its key interest rates unchanged in December for a fourth consecutive meeting, maintaining the deposit rate at 2.00% and the main refinancing rate at 2.15%. The ECB maintained that future policy decisions will remain data-dependent, that inflation is close to its 2.00% target and that the euro area economy continues to expand despite a challenging global environment, including heightened geopolitical risks and trade tensions.

### **1.2.2 Credit Outlook (December 2025):**

Credit Default Swap (CDS) prices, which spiked in April 2025 following President Trump's 'Liberation Day' tariff announcements, have since trended lower, returning to levels broadly consistent with their 2024 averages. Although CDS prices rose modestly in October, the overall credit outlook remains stable, and credit conditions are expected to remain close to the range seen over the past two years.

While lower interest rates may weigh on banks' profitability, strong capital positions, easing inflation, steady economic growth, low unemployment, and reduced borrowing costs for households and businesses all support a favourable outlook for the creditworthiness of institutions on (the Council's treasury management advisor) Arlingclose's counterparty list. Arlingclose's advice on approved counterparties and

recommended investment durations is kept under continuous review and will continue to reflect prevailing economic and credit conditions.

### 1.2.3 Interest Rate Forecast (December 2025):

Arlingclose, the Council's treasury management adviser, currently forecasts that the Bank of England's Monetary Policy Committee will continue to reduce Bank Rate through 2025 and 2026, reaching around 3.25%. This forecast reflects amendments made following the Autumn Budget and an assessment of the fiscal measures and their market implications, and following the BoE MPC meeting held on 18<sup>th</sup> December 2025.

Long-term gilt yields, and therefore interest rates payable on long-term borrowing, are expected to remain broadly stable on average, though with continued volatility, and to end the forecast period marginally lower than current levels. Yields are likely to stay higher than in the pre-quantitative tightening era, reflecting ongoing balance sheet reduction and elevated bond issuance. Short-term fluctuations are expected to persist in response to economic data releases and geopolitical developments.

A more detailed economic and interest rate forecast provided by Arlingclose is in Annex A.

For the purpose of setting the Council's Budget, it has been assumed that short term treasury investments will be made at an average rate of 3.29% and long-term strategic investments will yield an average rate of 4.04%. It is forecast that new loans will be borrowed at an average rate of 4.91% during 2026/27.

## 1.3 Local Context

**1.3.1 Council's position as at 31<sup>st</sup> December 2025:** The Council held £285.250m of borrowing and £48.200m of treasury investments. This is set out in further detail in Table 1 below.

**Table 1: Balance Sheet Summary**

|                                 | 31/12/2025       | 31/12/2025   |
|---------------------------------|------------------|--------------|
|                                 | Actual portfolio | Average rate |
|                                 | £m               | %            |
| <b>External borrowing:</b>      |                  |              |
| Public Works Loan Board         | 225.250          | 3.41%        |
| Local authorities               | 50.000           | 4.46%        |
| LOBO loans from banks           | 10.000           | 4.50%        |
| <b>Total external borrowing</b> | <b>285.250</b>   | <b>3.63%</b> |
| <b>Treasury investments:</b>    |                  |              |
| Local authorities               | 5.000            | 4.10%        |

|                                   | 31/12/2025              | 31/12/2025          |
|-----------------------------------|-------------------------|---------------------|
|                                   | <b>Actual portfolio</b> | <b>Average rate</b> |
|                                   | <b>£m</b>               | <b>%</b>            |
| <i>Banks (unsecured)</i>          | 5.200                   | 4.18%               |
| <i>Money market funds</i>         | 28.000                  | 3.91%               |
| <i>Strategic pooled funds</i>     | 10.000                  | 0.00%               |
| <b>Total treasury investments</b> | <b>48.200</b>           | <b>3.15%</b>        |
| <b>Net debt</b>                   | <b>237.050</b>          |                     |

### 1.3.2 Capital Financing Requirement:

The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The Council's current strategy is to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing.

The Council's Capital Financing Requirement (CFR, or underlying need to borrow) excluding lease financing as at 31<sup>st</sup> March 2026 is expected to be £392.816m and is forecast to rise to £464.627m by March 2027 as capital expenditure is incurred.

CIPFA's *Prudential Code for Capital Finance in Local Authorities* recommends that the Council's total debt should be lower than its highest forecast CFR over the next three years. The Council expects to comply with this recommendation during 2026/27.

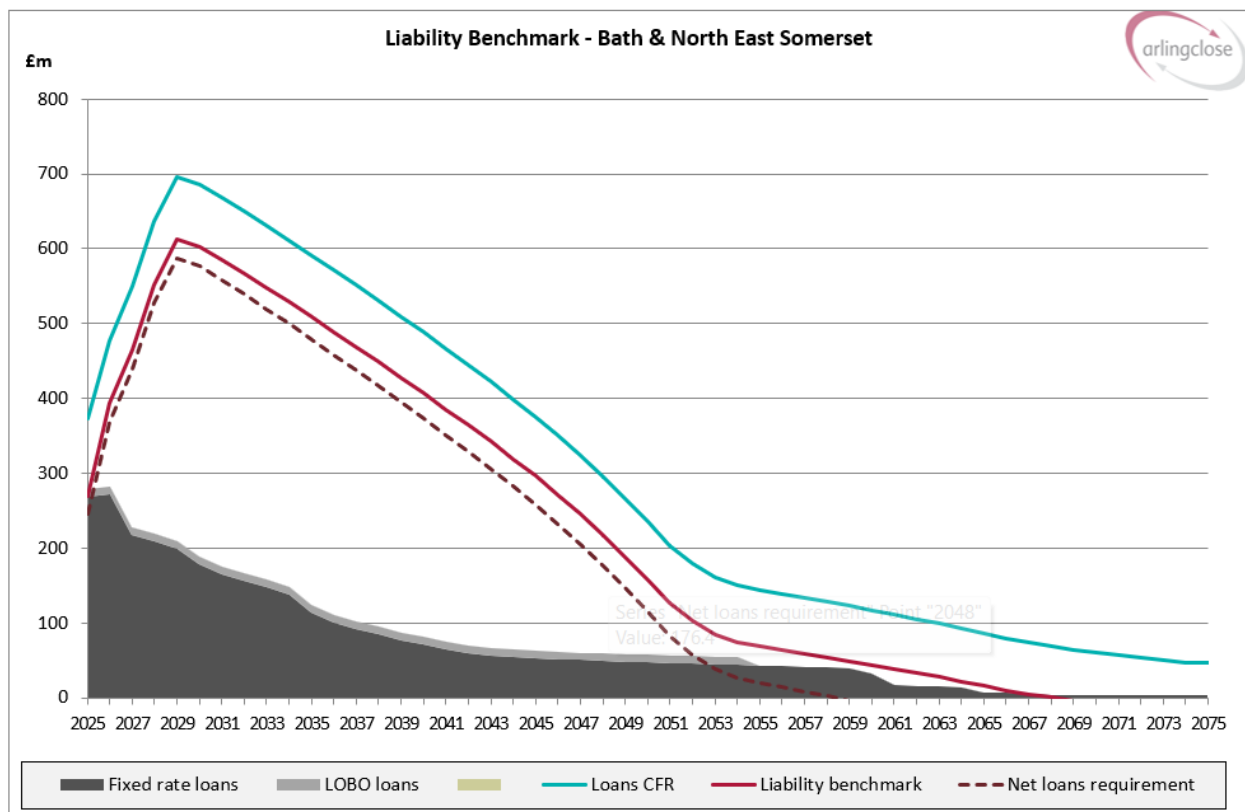
### Liability Benchmark

The liability benchmark is an important tool to help establish whether the Council is likely to be a long-term borrower or long-term investor in the future and so shape its strategic focus and decision making. The liability benchmark itself represents an estimate of the cumulative amount of external borrowing the Council must hold to fund its current capital and revenue plans while keeping treasury investments at the minimum level required to manage day-to-day cash flow.

**Table 2: Prudential Indicator: Liability Benchmark**

|                               | <b>31.3.25<br/>Actual<br/>£m</b> | <b>31.3.26<br/>Estimate<br/>£m</b> | <b>31.3.27<br/>Forecast<br/>£m</b> | <b>31.3.28<br/>Forecast<br/>£m</b> | <b>31.3.29<br/>Forecast<br/>£m</b> |
|-------------------------------|----------------------------------|------------------------------------|------------------------------------|------------------------------------|------------------------------------|
| Loans CFR                     | 373.000                          | 392.820                            | 464.627                            | 552.118                            | 611.968                            |
| Less: Balance sheet resources | (118.100)                        | (99.710)                           | (99.710)                           | (99.710)                           | (99.710)                           |
| <b>Net loans requirement</b>  | <b>254.900</b>                   | <b>293.106</b>                     | <b>364.917</b>                     | <b>452.408</b>                     | <b>512.258</b>                     |
| Plus: Liquidity allowance     | 15.000                           | 15.000                             | 15.000                             | 15.000                             | 15.000                             |
| <b>Liability benchmark</b>    | <b>269.900</b>                   | <b>308.106</b>                     | <b>379.917</b>                     | <b>467.408</b>                     | <b>527.258</b>                     |

Following on from the medium-term forecasts in Table 2 above, the long-term liability benchmark assumes capital expenditure funded by borrowing of around £71.811m for 2026/27, minimum revenue provision on new capital expenditure based on a 25 year asset life and income, and expenditure increasing by inflation of 2% a year. This is shown in the chart below together with the maturity profile of the Council's existing borrowing:



When we compare actual borrowing (the grey slopes) to the Liability Benchmark (solid red line) the model anticipates that the Council will be in a under borrowed position between 2026 and 2066. When the Council is considering new long-term borrowing, this funding gap can be used, as a useful guide to the optimal amount and length of borrowing required in order to minimise interest rate and credit risk.

## **2. Borrowing Strategy**

### **2.1 Current Borrowing**

The Council currently holds £285.250m of loans, an increase £18.300m on the previous year. The Council has taken out £90.000m in new borrowing between January 2025 & December 2025, of which £65.000m was to replace maturing borrowing, £15.000m was in in order to keep cash balances in line with the Liability Indicator and £10.000m was to cover a pension prepayment. This was netted off by £6.700m in PWLB annuity loan repayments and £65.000m in repayment of maturing loans.

### **2.2 Objectives**

The Council's chief objective when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving certainty of those costs over the period for which funds are required. The flexibility to renegotiate loans should the Council's long-term plans change is a secondary objective.

### **2.3 Strategy**

Given the significant cuts to public expenditure and in particular to local government funding, the Council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio.

Short-term interest rates have fallen over the past year, and are expected to fall a little further, so it is therefore likely to be more cost effective over the medium term to borrow short term loans. The risks of this approach will be managed by keeping the Council's interest rate exposure within the limit set in the treasury management prudential indicators. By doing so, the Council is able to reduce net borrowing costs over time and overall treasury risk.

The benefits will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years. Arlingclose may assist the Council with this 'cost of carry' and breakeven analysis. Its output may determine whether the Council borrows additional sums at long-term fixed rates in 2026/27 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.

The Council has previously raised the majority of its long-term borrowing from the PWLB but will consider long-term loans from other sources including banks, pensions and local authorities, and it may consider investigating the possibility of issuing bonds and similar instruments, in order to lower interest costs and reduce over-reliance on one source of funding in line with the CIPFA Code. PWLB loans are no longer available to local authorities planning to buy investment assets primarily for yield; the Council intends to avoid this activity in order to retain its access to PWLB loans.

Alternatively, the Council may arrange forward starting loans, where the interest rate is fixed in advance, but the cash is received in later years. This would enable certainty of cost to be achieved without suffering a cost of carry in the intervening period.

In addition, the Council may borrow further short-term loans to cover unplanned cash flow shortages.

## **2.4 Sources of Borrowing**

The approved sources of long-term and short-term borrowing are:

- HM Treasury's PWLB lending facility
- National Wealth Fund Ltd (formerly UK Infrastructure Bank Ltd)
- any institution approved for investments (see below)
- any other bank or building society or insurance company authorised to operate in the UK
- any other UK public sector body
- UK public and private sector pension funds (except the Avon Pension Fund)
- capital market bond investors
- retail investors via a regulated peer-to-peer platform
- special purpose companies created to enable local authority bond issues.

**Other Sources of Debt Finance:** In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:

- leasing
- hire purchase
- Private Finance Initiative
- sale and leaseback

**2.4.1 LOBO's:** The Council has £10.000m of Lender Option Borrower Option (LOBO) loans where the lender has the option to propose an increase in the interest rate at set dates, following which the Council has the option to either accept the new rate or to repay the loan at no additional cost. These LOBO's have options due up in 2026/27 and it is possible that lenders will exercise their options. If they do, the Council will consider the option to repay LOBO loans after reviewing the refinancing risk in later years. Total borrowing via LOBO loans will be limited to the current £10.000m.

**2.4.2 Short-term and Variable Rate Loans:** These loans leave the Council exposed to the risk of short-term interest rate rises and are therefore subject to the interest rate exposure limits in the treasury management indicators below. Financial derivatives may be used to manage this interest rate risk (see section below).

**2.4.3 Debt Rescheduling:** The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. Other lenders may also be prepared to negotiate premature

redemption terms. The Council may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall cost saving or a reduction in risk. The recent rise in interest rates means that more favourable debt rescheduling opportunities should arise than in previous years.

### **3. Treasury Investment Strategy**

#### **3.1 Current Investments**

The Council holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Council's treasury investment balance has ranged between £28.800m and £80.100m and similar levels are expected to be maintained in the forthcoming year.

#### **3.2 Objectives**

The CIPFA Code requires the Council to invest its treasury funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Council's 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. The Council aims to be a responsible investor and will consider environmental, social and governance (ESG) issues when investing.

#### **3.3 Strategy**

As demonstrated by the liability benchmark above, the Council expects to be a long-term borrower and new treasury investments will therefore be made primarily to manage day-to-day cash flows using short-term low risk instruments in line with advice from Arlingclose.

The Council's existing portfolio of investments in strategic pooled funds, £5.000m in CCLA Local Authority Property Fund, £3.000m in FP Foresight UK Infrastructure Income Fund, and £2.000m in the VT Gravis Clean Energy Income Fund, will be maintained to diversify risk into different sectors and boost investment income, further details of this are provided in section 3.8.

Under the Markets in Financial Instruments Directive (MiFID) II, the Council has opted up to professional client status with its providers of financial services, including advisers, banks, brokers and fund managers, allowing it access to a greater range of services but without the greater regulatory protections afforded to individuals and small companies. Given the size and range of the Council's treasury management activities, the Director of Finance (S151 Officer) believes this to be the most appropriate status.



To be categorised as Professional the Council must hold at least a £10.000m investment balance, the Council's three pooled investments mentioned above, which are medium – long term investments, guarantee that this balance will always be held. By placing this required £10.000m balance in these three pooled funds, the Council aims to achieve a total return that is equal or higher than the long-term average rate of inflation thus preserving the spending power of this £10.000m balance.

The CIPFA Code does not permit local authorities to both borrow and invest long-term for cash flow management. But the Council may make long-term investments for treasury risk management purposes, including to manage interest rate risk by investing sums borrowed in advance for the capital programme for up to three years; to manage inflation risk by investing usable reserves in instruments whose value rises with inflation; and to manage price risk by adding diversification to the strategic pooled fund portfolio.

The total amount borrowed will not exceed the 2026/27 authorised borrowing limit of £473.000m. The maximum period between borrowing and expenditure is expected to be three years, although loans are linked with its budgeted programme, individual items within that programme are not linked to the loans at a granular level.

Under the International Financial Reporting Standard (IFRS) 9, the accounting for certain investments depends on the Council's "business model" for managing them. The Council aims to achieve value from its treasury investments by a business model of collecting the contractual cash flows and therefore, where other criteria are also met, these investments will continue to be accounted for at amortised cost.

### 3.4 Approved Counterparties

The Council may invest its surplus funds with any of the counterparty types in Table 3 below, subject to the limits shown.

**Table 3: Treasury Investment Counterparties and Limits**

| <b>Sector</b>                                 | <b>Minimum Credit Rating*</b> | <b>Time Limit</b> | <b>Counterparty Limit</b> | <b>Sector Limit</b> |
|-----------------------------------------------|-------------------------------|-------------------|---------------------------|---------------------|
| The UK Government                             | N/A                           | 5 years           | Unlimited                 | Unlimited           |
| Local authorities & other government entities | N/A                           | 5 years           | £10.000m                  | Unlimited           |
| Secured investments                           | A-                            | 5 years           | £10.000m                  | Unlimited           |
| Banks (secured)                               | A-                            | 5 years           | £10.000m                  | Unlimited           |
| Banks (unsecured)                             | A-                            | 13 months         | £10.000m                  | £40.000m            |
| Building societies (unsecured)                | A-                            | 13 months         | £10.000m                  | £15.000m            |

| Sector                           | Minimum Credit Rating* | Time Limit | Counterparty Limit | Sector Limit |
|----------------------------------|------------------------|------------|--------------------|--------------|
| Registered providers (unsecured) | A-                     | 5 years    | £5.000m            | £5.000m      |
| Money market funds               | AAAmmf                 | n/a        | £10.000m           | £60.000m     |
| Strategic pooled funds           | N/A                    | n/a        | £5.000m            | £10.000m     |
| Foreign countries per country    | AA+                    | 13 months  | £10.000m           | £10.000m     |
| ESG focussed short term deposits | A-                     | 13 months  | £5.000m            | £5.000m      |
| Other investments                | A-                     | 5 years    | £5.000m            | £5.000m      |

This table must be read in conjunction with the notes below.

**\* Minimum Credit Rating:** Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used. However, investment decisions are never made solely based on credit ratings, and all other relevant factors including external advice will be taken into account.

For entities without published credit ratings, investments may be made where external advice indicates the entity to be of similar credit quality.

**3.4.1 Government:** Loans to, and bonds and bills issued or guaranteed by, national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is generally a lower risk of insolvency, although they are not zero risk. Investments with the UK Government are deemed to be zero credit risk due to its ability to create additional currency and therefore may be made in unlimited amounts for up to 5 years.

**3.4.2 Local Authorities and Other Government Entities:** Although most UK local authorities have not opted to obtain a formal credit rating from either Fitch, Moody's or Standard & Poors, they are considered quasi-governmental by advisors and therefore are assigned the same rating as the UK Government for the purpose of establishing credit criteria. No local authority has ever defaulted in its loan arrangements. The above withstanding the Council will consider other factors including; if a S114 Notice has been issued, if exceptional financial support is requested/granted and the status of the authorities' statement of accounts.

**3.4.3 Secured Investments:** Investments secured on the borrower's assets, which limits the potential losses in the event of insolvency. The amount and quality of the security will be a key factor in the investment decision. Covered bonds, secured deposits and reverse repurchase agreements with banks and building societies are exempt from bail-in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the higher of the collateral credit rating and the counterparty

credit rating will be used. The combined secured and unsecured investments with any one counterparty will not exceed the cash limit for secured investments.

**3.4.4 Banks and Building Societies (Unsecured):** Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail. See below for arrangements relating to operational bank accounts.

**3.4.5 Registered Providers (Unsecured):** Loans to, and bonds issued or guaranteed by, registered providers of social housing or registered social landlords, formerly known as housing associations. These bodies are regulated by the Regulator of Social Housing (in England), the Scottish Housing Regulator, the Welsh Government and the Department for Communities (in Northern Ireland). As providers of public services, they retain the likelihood of receiving government support if needed.

**3.4.6 Money Market Funds (MMFs):** Pooled funds that offer same-day or short notice liquidity and very low or no price volatility by investing in short-term money markets. They have the advantage over bank accounts of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a small fee. The Council will take care to diversify its liquid investments over a variety of providers to ensure access to cash at all times.

**3.4.7 Strategic Pooled Funds:** Bond, equity and property funds that offer enhanced returns over the longer term but are more volatile in the short term. These allow the Council to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Council's investment objectives will be monitored regularly. Note that this classification covers the Council's two ESG investments and the investment in the CCLA property fund.

**3.4.8 Foreign Countries:** This category covers investment with both the governments of foreign countries and banks based in foreign countries. Where a bank is domiciled in a foreign country, the bank must meet the minimum credit criteria set out in Table 3 of A- for 'Banks (unsecured)' and be domiciled in a country which meets the minimum credit rating criteria set of AA+.

**3.4.9 Other Investments:** This category covers treasury investments not listed above, for example unsecured corporate bonds and unsecured company loans. Non-bank companies cannot be bailed-in but can become insolvent placing the Council's investment at risk. Any investment under this category will only be made following a favourable external credit assessment and on the specific advice of the Council's treasury management adviser.

**Note:** Investments in pooled funds and multilateral development banks do not count against the limit for any single foreign country, since the risk is diversified over many countries.

**3.4.10 Operational Bank Accounts:** The Council may incur operational exposures, for example through current accounts, collection accounts and merchant acquiring services, to any UK bank with credit ratings no lower than BBB- and with assets greater than £25 billion. These are not classed as investments but are still subject to the risk of a bank bail-in. The Bank of England has stated that in the event of failure, banks with assets greater than £25 billion are more likely to be bailed-in than made insolvent, increasing the chance of the Council maintaining operational continuity.

### **3.5 Risk Assessment and Credit Ratings**

Credit ratings are obtained and monitored by the Council's treasury advisers, who will notify changes in ratings as they occur. The credit rating agencies in current use are listed in the Treasury Management Practices document. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:

- no new investments will be made,
- any existing investments that can be recalled or sold at no cost will be, and
- full consideration will be given to the recall or sale of all other existing investments with the affected counterparty.

Where a credit rating agency announces that a credit rating is on review for possible downgrade (also known as "negative watch") so that it may fall below the approved rating criteria, then only investments that can be withdrawn on the next working day will be made with that organisation until the outcome of the review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.

**3.5.1 Other Information on the Security of Investments:** The Council understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support, reports in the quality financial press and analysis and advice from the Council's treasury management adviser. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may otherwise meet the above criteria.

The Council is aware that investing with certain counterparties, while considered secure from a purely financial perspective, may leave it open to criticism, valid or otherwise, that may affect its public reputation, and this risk will therefore be taken into account when making investment decisions.

When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2008, 2020 and 2022, this is not generally reflected in credit ratings, but can be seen in other market measures. In these circumstances, the Council will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the Council's cash balances, then the surplus will be deposited with the UK Government, or with other local authorities. This will cause investment returns to fall but will protect the principal sum invested.

### **3.6 Investment Limits**

The Council's revenue reserves (including earmarked reserves) available to cover investment losses was £89.376m as at 31<sup>st</sup> March 2025. To limit risk from any single default, the maximum that will be lent to any one organisation (other than the UK Government) will be £10.000m which represents 11.19% of reserves. A group of banks under the same ownership will be treated as a single organisation for limit purposes. Investments in pooled funds and multilateral development banks do not count against the limit for any single foreign country, since the risk is diversified over many countries.

### **3.7 Liquidity Management**

The Council uses forward looking forecasting based on prior year cashflows combined with knowledge of upcoming income/spending to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a prudent basis to minimise the risk of the Council being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Council's medium-term financial plan and cash flow forecast.

The Council will spread its liquid cash over at least four providers (e.g. bank accounts and money market funds) to ensure that access to cash is maintained in the event of operational difficulties at any one provider.

### **3.8 Environment Social and Governance Investment Approach**

**3.8.1 The Climate Emergency:** In 2019 Bath and North East Somerset Council declared a Climate Emergency reflecting the concern that the Council has over climate change, and the commitment of the Council to address the issue with regards to evaluating the climate change impact of all our decisions.

**3.8.2 Background:** The CIPFA Treasury Management Code and Investment Guidance issued by the Government state that the main principles in investing are Security, Liquidity and Yield in that order. However, as part of the 2021 Code, CIPFA now requires local authorities to have some consideration of ESG factors when investing.

### **3.8.3 Long Term ESG Investments:**

In the Treasury Management Strategy 2021/22 the Council adopted an ESG investment approach as part of its 2021/22 Investment Strategy. Resulting in a long-term investment of £5.000m investment split across the following two ESG focused funds;

- £3.000m into FP Foresight UK Infrastructure fund; &
- £2.000m into VT Gravis Clean energy income fund.

### **3.8.4 Short Term ESG Investments:**

When investing in banks and funds, the Council will prioritise banks that are signatories to the UN Principles for Responsible Banking and funds operated by managers that are signatories to the UN Principles for Responsible Investment, the Net Zero Asset Managers Alliance and/or the UK Stewardship Code.

The Council may also consider options for investment in short-term funds with institutions who ring fence the use of such funds for ESG related matters. The criteria for credit rating of security of such deposits will need to remain in line with the wider Council policy, however where appropriate and at the Council's discretion, some flexibility will be provided to allow for slightly longer durations of investment and potentially lower returns in order to support the ESG focus. Where such flexibility is used, the investment will be subject to agreement of the S151 Officer taking these factors into consideration.

Direct involvement and financing of Green energy projects is treated as capital expenditure, and as such is not covered within the remit of treasury management.

## **3.9 Other Matters**

**Avon Pension Fund Investments:** The Council's Treasury Management team also manage the Avon Pension Fund's internally held cash on behalf of the Fund. The cash balance held internally is a working balance to cover pension payments at any point in time and it is estimated will be an average of £40.000m, being around 0.70% of the overall assets of the Fund. The regulations require that this cash is accounted for separately and invested separately from the Council's cash.

Investments held will operate within the framework of this Investment Strategy, but the maximum counterparty limit and investment term with any counterparty are set annually by the Avon Pension Fund Committee. These limits are in addition to the Council's limits for counterparties as set out in Appendix 2.

The Pension Fund's investment managers are responsible for the investment of cash held within their portfolios, and this policy does not relate to their cash investments.

## **4. Treasury Management Prudential Indicators**

The Council measures and manages its exposures to treasury management risks using the following indicators.

### **4.1 Treasury Borrowing Limits for 2026/27 to 2028/29**

It is a statutory duty under s.3 of the Local Government Act 2003, and supporting regulations, for the Council to determine and keep under review how much it can afford to borrow. This amount is termed the 'Affordable Borrowing Limit'.

The Council must have regard to the Prudential Code when setting the Affordable Borrowing Limit. The Code requires a Council to ensure that its total capital investment remains within sustainable limits and, in particular, that the impact upon its future Council tax levels is 'acceptable'.

The Affordable Borrowing Limit must include all planned capital investment to be financed by external borrowing and any other forms of liability, such as credit arrangements. The Affordable Borrowing Limit is to be set on a rolling basis for the forthcoming year and two successive financial years.

The Authorised limits for external debt include current commitments and proposals in the budget report for capital expenditure, plus additional headroom over and above the operational limit for unusual cash movements.

The Operational Boundary for external debt is based on the same estimates as the authorised limit but without the additional headroom for unusual cash movements. This level also factors in the proposed approach to use internal cash-flow and future capital receipts as the preferred financing method for the capital programme.

***Table 4: Operational Boundary and Authorised Limit***

|                                                    | <b>2026/27<br/>£m</b> | <b>2027/28<br/>£m</b> | <b>2028/29<br/>£m</b> |
|----------------------------------------------------|-----------------------|-----------------------|-----------------------|
| Operational Boundary – Borrowing                   | 438                   | 526                   | 587                   |
| Operational Boundary – Other Long-Term Liabilities | 8                     | 8                     | 7                     |
| <b>Operational Boundary – TOTAL</b>                | <b>446</b>            | <b>534</b>            | <b>594</b>            |
| Authorised Limit- Borrowing                        | 465                   | 552                   | 612                   |
| Authorised Limit – Other Long-Term Liabilities     | 8                     | 8                     | 7                     |
| <b>Authorised Limit – TOTAL</b>                    | <b>473</b>            | <b>560</b>            | <b>619</b>            |

## 4.2 Security

The Council has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average credit rating of its investment portfolio. This is calculated by applying a score to each investment (AAA=1, AA+=2, etc.) and taking the arithmetic average, weighted by the size of each investment. Unrated investments are assigned a score based on their perceived risk.

**Table 5: Portfolio Average Credit Rating Criteria**

| Credit Risk Indicator           | Target |
|---------------------------------|--------|
| Portfolio average credit rating | A-     |

## 4.3 Liquidity

The Council has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments within a rolling three-month period, without additional borrowing.

**Table 6: Minimum 3 Month Liquidity Limit**

| Liquidity Risk Indicator             | Target   |
|--------------------------------------|----------|
| Total cash available within 3 months | £15.000m |

## 4.4 Interest Rate Exposure

This indicator is set to control the Council's exposure to interest rate risk. The upper limits on the one-year revenue impact of a 1% rise or fall in interest rates will be:

**Table 7. Interest Rate Risk Indicator**

| Interest Rate Risk Indicator                                          | Limit       |
|-----------------------------------------------------------------------|-------------|
| Upper limit on one-year revenue impact of a 1% rise in interest rates | +/- £0.800m |
| Upper limit on one-year revenue impact of a 1% fall in interest rates | +/- £0.800m |

The impact of this limit is that the Council should never be holding a maturity adjusted net debt/investment position of more than £0.800m subject to variable interest rates.

The impact of a change in interest rates is calculated on the assumption that maturing loans and investments will be replaced at new market rates, this includes amounts which are maturing each year in PWLB annuity loans.



## 4.5 Maturity Structure of Borrowing

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

**Table 8: Borrowing Maturity Limits**

| Refinancing Rate Risk Indicator | Upper Limit | Lower Limit |
|---------------------------------|-------------|-------------|
| Under 12 months                 | 30%         | 0%          |
| 12 months and within 24 months  | 30%         | 0%          |
| 24 months and within 5 years    | 50%         | 0%          |
| 5 years and within 10 years     | 75%         | 0%          |
| 10 years and within 20 years    | 75%         | 0%          |
| 20 years and within 30 years    | 100%        | 0%          |
| 30 years and within 40 years    | 100%        | 0%          |
| 40 years and within 50 years    | 100%        | 0%          |

Time periods start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment. For LOBO's this will now be shown as the date of their maturity.

## 4.6 Long-Term Treasury Management Investments

This indicator looks at investments that at inception are for over 364 days or with no fixed maturity date. The purpose of which is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the long-term principal sum invested to final maturities beyond the period end will be:

**Table 9: Investment Maturity Limits**

| Price risk indicator                        | 2026/27  | 2027/28  | 2028/29  | No Fixed Date |
|---------------------------------------------|----------|----------|----------|---------------|
| Limit on principal invested beyond year end | £20.000m | £20.000m | £10.000m | £10.000m      |

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

## **5. Related Matters**

The CIPFA Code requires the Council to include the following in its Treasury Management Strategy.

### **5.1 Treasury Management Advisers**

The Council has appointed Arlingclose Limited as treasury management advisers and receives specific advice on investment, debt and capital finance issues, although responsibility for final decision making remains with the Council and its officers. The services received include:

- advice and guidance on relevant policies, strategies and reports,
- advice on investment decisions,
- notification of credit ratings and changes,
- other information on credit quality,
- advice on debt management decisions,
- accounting advice,
- reports on treasury performance,
- forecasts of interest rates, and
- training courses.

The quality of this service is monitored by officers on a regular basis, focusing on supply of relevant, accurate and timely information across the headings above.

### **5.2 Financial Derivatives**

Local authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk (e.g. interest rate collars and forward deals) and to reduce costs or increase income at the expense of greater risk (e.g. LOBO loans and callable deposits). The general power of competence in section 1 of the *Localism Act 2011* removes much of the uncertainty over local authorities' use of standalone financial derivatives (i.e. those that are not embedded into a loan or investment).

The Council will only use standalone financial derivatives (such as swaps, forwards, futures and options) where they can be clearly demonstrated to reduce the overall level of the financial risks that the Council is exposed to. Additional risks presented, such as credit exposure to derivative counterparties, will be taken into account when determining the overall level of risk. Embedded derivatives, including those present in pooled funds and forward starting transactions, will not be subject to this policy, although the risks they present will be managed in line with the overall treasury risk management strategy.

Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria, assessed using the appropriate credit rating for derivative exposures.

In line with the CIPFA Code, the Council will seek external advice and will consider that advice before entering into financial derivatives to ensure that it fully understands the implications.

### **5.3 External Funds**

Where schools have not opted to have their own bank account, the Council manages their investment balances as part of its own. The Council treats the schools' balances in its accounts as part of the Council's investment portfolio but assigns a return at a rate of base rate less 0.25% (capped to a minimum of zero where base rate drops below 0.25%) to schools for their respective balances.

### **5.4 Staff and Councillor Training**

The needs of the Council's treasury management staff for training in investment management are assessed every year as part of the staff performance development review process, and additionally when the responsibilities of individual members of staff change.

Staff regularly attend training courses, seminars and conferences provided by Arlingclose and CIPFA. Relevant staff are also encouraged to study professional qualifications from CIPFA, the Association of Corporate Treasurers and other appropriate organisations.

Training in treasury management is also provided to Members of the Audit Committee by the Council's treasury advisors, Arlingclose.

### **5.5 Financial Implications**

The budget for treasury management investment income in 2026/27 is £1.077m, based on an average investment portfolio of £30m at an average interest rate of 3.54%. The budget for debt interest paid in 2026/27 is £12.819m, based on an average debt portfolio of £330.977m at an average interest rate of 3.87%. If actual levels of investments and borrowing, or actual interest rates, differ from those forecasts, performance against budget will be correspondingly different.

Where investment income from strategic pooled funds exceeds budget, then 50% of the revenue savings may be transferred to the Capital Financing Reserve to mitigate the risk of capital losses in future years should valuation losses on fair value treasury assets require recognition, or where capital losses were crystallised on the sale of treasury assets.

### **5.6 Other Options Considered**

The CIPFA Code does not prescribe any particular treasury management strategy for local authorities to adopt. The Director of Finance (S151 Officer), having consulted the Cabinet Member for Resources, believes that the above strategy represents an

appropriate balance between risk management and cost effectiveness. Some alternative strategies, with their financial and risk management implications, are listed below.

**Table 10: Alternative Treasury Strategy Options Considered**

| <b>Alternative</b>                                                    | <b>Impact on Income and Expenditure</b>                                                  | <b>Impact on Risk Management</b>                                                                                                                |
|-----------------------------------------------------------------------|------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------|
| Invest in a narrower range of counterparties and/or for shorter times | Interest income will be lower                                                            | Lower chance of losses from credit related defaults, but any such losses may be greater                                                         |
| Invest in a wider range of counterparties and/or for longer times     | Interest income will be higher                                                           | Increased risk of losses from credit related defaults, but any such losses may be smaller                                                       |
| Borrow additional sums at long-term fixed interest rates              | Debt interest costs will rise; this is unlikely to be offset by higher investment income | Higher investment balance leading to a higher impact in the event of a default; however long-term interest costs may be more certain            |
| Borrow short-term or variable loans instead of long-term fixed rates  | Debt interest costs will initially be lower                                              | Increases in debt interest costs will be broadly offset by rising investment income in the medium term, but long-term costs may be less certain |
| Reduce level of borrowing                                             | Saving on debt interest is likely to exceed lost investment income                       | Reduced investment balance leading to a lower impact in the event of a default; however long-term interest costs may be less certain            |

## **Annex A – Arlingclose Economic & Interest Rate Forecast – 22<sup>nd</sup> December 2025**

### **Underlying assumptions:**

- The Bank of England duly delivered on expectations for a December rate cut, but, despite softer economic data over the past two weeks, the minutes highlighted increased caution surrounding both the inflation outlook and the speed of future easing. With a close vote of 5-4 in favour of a rate reduction, this suggests that the bar for further monetary easing may be higher than previously thought despite the possibility of the CPI rate falling to target in 2026.
- Budget policies and base effects will mechanically reduce the CPI rate in 2026, on top of the downward pressure arising from soft economic growth and the looser labour market. However, many policymakers appear concerned that household and business inflation and pricing expectations are proving sticky following recent bouts of high price and wage growth, which may allow underlying inflationary pressure to remain elevated. While, the Bank's measure of household expectations ticked lower in December, it remains above levels consistent with the 2% target at 3.5%.
- While policymakers hold valid concerns, these appear somewhat out of line with current conditions; CPI inflation fell to 3.2% in November, private sector wage growth continued to ease amid the highest unemployment rate since the pandemic, and the economy contracted in October after barely growing in Q3. Business surveys pointed to marginally stronger activity and pricing intentions in December but also suggested that the pre-Budget malaise was not temporary. These data are the latest in a trend suggesting challenging economic conditions are feeding into price and wage setting.
- Risks to the growth and inflation outlook lie to the downside, which may ultimately deliver lower Bank Rate than our central case. However, the minutes suggest that the bar to further rate cuts beyond 3.25% is higher and the near-term upside risks to our Bank Rate forecast have increased. Having said that, we believe inflation expectations will naturally decline alongside headline inflation rates.
- Investors appear to have given the UK government some breathing space following the Budget, with long-term yields continuing to trade at slightly lower levels than in late summer/early autumn. Even so, sustained heavy borrowing across advanced economies, the DMO's move towards issuing more short-dated gilts and lingering doubts about the government's fiscal plans will keep short to medium yields above the levels implied by interest rate expectations alone.

## Forecast:

- In line with our long-held forecast, Bank Rate was cut to 3.75% in December 2025.
- Continuing disinflation, rising unemployment, softening wage growth and low confidence suggests that monetary policy will continue to be loosened.
- Arlingclose expects Bank Rate to be cut to 3.25% by middle of 2026. However, near-term upside risks to the forecast have increased.
- Medium and long-term gilt yields continue to incorporate premia for UK government credibility, global uncertainty and significant issuance. These issues may not be resolved quickly, and we expect yields to remain higher.

|                                  | Current | Mar-26 | Jun-26 | Sep-26 | Dec-26 | Mar-27 | Jun-27 | Sep-27 | Dec-27 | Mar-28 | Jun-28 | Sep-28 | Dec-28 |
|----------------------------------|---------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| <b>Official Bank Rate</b>        |         |        |        |        |        |        |        |        |        |        |        |        |        |
| Upside risk                      | 0.00    | 0.25   | 0.50   | 0.50   | 0.50   | 0.50   | 0.50   | 0.50   | 0.50   | 0.50   | 0.50   | 0.50   | 0.50   |
| Central Case                     | 3.75    | 3.50   | 3.25   | 3.25   | 3.25   | 3.25   | 3.25   | 3.25   | 3.25   | 3.25   | 3.25   | 3.25   | 3.25   |
| Downside risk                    | 0.00    | 0.00   | -0.25  | -0.50  | -0.50  | -0.50  | -0.50  | -0.50  | -0.50  | -0.50  | -0.50  | -0.50  | -0.50  |
| <b>3-month money market rate</b> |         |        |        |        |        |        |        |        |        |        |        |        |        |
| Upside risk                      | 0.00    | 0.25   | 0.50   | 0.50   | 0.50   | 0.50   | 0.50   | 0.50   | 0.50   | 0.50   | 0.50   | 0.50   | 0.50   |
| Central Case                     | 3.82    | 3.55   | 3.30   | 3.30   | 3.30   | 3.30   | 3.30   | 3.30   | 3.30   | 3.30   | 3.35   | 3.35   | 3.35   |
| Downside risk                    | 0.00    | 0.00   | -0.25  | -0.50  | -0.50  | -0.50  | -0.50  | -0.50  | -0.50  | -0.50  | -0.50  | -0.50  | -0.50  |
| <b>5yr gilt yield</b>            |         |        |        |        |        |        |        |        |        |        |        |        |        |
| Upside risk                      | 0.00    | 0.40   | 0.45   | 0.50   | 0.55   | 0.60   | 0.65   | 0.70   | 0.70   | 0.70   | 0.70   | 0.70   | 0.70   |
| Central Case                     | 3.96    | 3.85   | 3.80   | 3.75   | 3.75   | 3.75   | 3.75   | 3.75   | 3.75   | 3.75   | 3.80   | 3.80   | 3.80   |
| Downside risk                    | 0.00    | -0.50  | -0.60  | -0.70  | -0.80  | -0.85  | -0.85  | -0.85  | -0.85  | -0.85  | -0.85  | -0.85  | -0.85  |
| <b>10yr gilt yield</b>           |         |        |        |        |        |        |        |        |        |        |        |        |        |
| Upside risk                      | 0.00    | 0.40   | 0.45   | 0.50   | 0.55   | 0.60   | 0.65   | 0.70   | 0.70   | 0.70   | 0.70   | 0.70   | 0.70   |
| Central Case                     | 4.52    | 4.40   | 4.35   | 4.30   | 4.30   | 4.30   | 4.30   | 4.30   | 4.30   | 4.30   | 4.35   | 4.35   | 4.35   |
| Downside risk                    | 0.00    | -0.50  | -0.60  | -0.70  | -0.80  | -0.85  | -0.85  | -0.85  | -0.85  | -0.85  | -0.85  | -0.85  | -0.85  |
| <b>20yr gilt yield</b>           |         |        |        |        |        |        |        |        |        |        |        |        |        |
| Upside risk                      | 0.00    | 0.40   | 0.45   | 0.50   | 0.55   | 0.60   | 0.65   | 0.70   | 0.70   | 0.70   | 0.70   | 0.70   | 0.70   |
| Central Case                     | 5.16    | 5.00   | 4.95   | 4.90   | 4.90   | 4.90   | 4.90   | 4.90   | 4.90   | 4.90   | 4.95   | 4.95   | 4.95   |
| Downside risk                    | 0.00    | -0.50  | -0.60  | -0.70  | -0.80  | -0.85  | -0.85  | -0.85  | -0.85  | -0.85  | -0.85  | -0.85  | -0.85  |
| <b>50yr gilt yield</b>           |         |        |        |        |        |        |        |        |        |        |        |        |        |
| Upside risk                      | 0.00    | 0.40   | 0.45   | 0.50   | 0.55   | 0.60   | 0.65   | 0.70   | 0.70   | 0.70   | 0.70   | 0.70   | 0.70   |
| Central Case                     | 4.74    | 4.65   | 4.60   | 4.60   | 4.60   | 4.60   | 4.60   | 4.60   | 4.60   | 4.60   | 4.65   | 4.65   | 4.65   |
| Downside risk                    | 0.00    | -0.50  | -0.60  | -0.70  | -0.80  | -0.85  | -0.85  | -0.85  | -0.85  | -0.85  | -0.85  | -0.85  | -0.85  |

PWLB Standard Rate = Gilt yield + 1.00%

PWLB Certainty Rate = Gilt yield + 0.80%

PWLB HRA Rate = Gilt yield + 0.40%

National Wealth Fund (NWF) Rate = Gilt yield + 0.40%