ANNEX III

TREASURY MANAGEMENT STRATEGY 2025/26

Contents

1.0 Introduction

1.1 This strategy considers how the Council's borrowing and treasury investments are arranged and managed. It sets out how the Council manages its loan debt and treasury investments to meet its longer term borrowing needs as well as its day to day cashflows.

1.1 The Council's financial difficulties (underpinning the issuing of a Section 114 notice in June 2023) relate to the extremely high level of the Council's loan debt combined with the Council's reliance on failed high value investments in the commercial companies to fund the borrowing costs. The plans for addressing this are considered mainly in the Capital Strategy and the Investment Strategy (at Annex I and Annex II). The Treasury Management Strategy sets out proposals for how the Council's loan debt is managed and the Council's Minimum Revenue Provision (MRP) (at Appendix A).

1.2 The report also sets out the Council's Policy Statement for Minimum Revenue Provision (MRP) which confirms the Council's unaffordable revenue charge for MRP (under current and regulations and guidance) and describes the Government arrangements which permit the MRP charge to be reduced whilst the Council is receiving Exceptional Financial Support from government.

1.3 This strategy also includes debt reduction plan principles for the Council to follow as it continues to develop a Debt Reduction Plan (at Appendix E).

1.4 The Local Government Act 2003 and supporting regulations require the Council to 'have regard to' CIPFA's Prudential Code and Treasury Management Code, and to Government Investment Guidance. Treasury Management is defined by the Code as *"The management of the organisation'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."*

1.5 For the Council, the key aspects of this are its loan debt and borrowing costs, together with the security of its (relatively small) treasury management investments. The Council's investments which have been made for service purposes including the loans and shares in the Council's commercial companies are the subject of the Investment Strategy (at Annex II).

2.0 Treasury Management Risk Appetite, Objectives and Policy

2.1 The main treasury management risks which the Council is exposed to include:

- Interest rate risk: the risk that future borrowing costs rise.
- Liquidity and refinancing risks: the risk that the Council cannot obtain funds when needed.
- Credit risk: the risk of default in the Council's treasury investments.

2.2 The Council's borrowing costs are far higher than the Council's forecast resources can support. Key actions to address this are underway and have been jointly developed by the Council, its Commissioners and the Government. In this position, the Council's risk appetite in relation to treasury management must be very low. Stable and predictable charges to revenue account from treasury activities are therefore a high priority to the Council.

2.3 The Council's objectives in relation to treasury management are to "…*obtain funding and manage the Council's loan debt and treasury investments at a net cost which is as low as possible consistent with a high degree of interest cost stability and a very low risk to sums invested".* This does not mean that it is possible to avoid treasury risks. A balance has to be struck with an emphasis on prudence and stability.

2.4 CIPFA's Treasury Management Code asks authorities to adopt a standard policy statement and four key clauses in relation to treasury management (details in Appendix B). The Council's finance team has limited capacity to proactively manage treasury risks or use advanced treasury techniques or instruments. Treasury activities are limited to:

- Borrowing from the Public Works Loan Board (PWLB) and via the money market;
- Borrowing when required (subject to regular checks by Government);
- Making short term treasury management investments;
- Restructuring of loan debt.

2.5 As the Council is in intervention and requires Exceptional Financial Support from government, there are likely to be specific conditions that restrict the Council's borrowing activity. Due to the scale of the debt held these will include regular reporting of the cash flow position and advance approval for any borrowing required. The Council's borrowing will be with PWLB.

3.0 Current Treasury Position

3.1 The Council's loan debt outstanding and treasury investments 31 December 2024 are as follows:

		Principal		Ave. rate
Borrowing		£m	£m	%
Long term borrowing:				
Fixed rate funding	PWLB	1,699.4		2.62
	Market	30		4.48
			1,729.40	2.66
Variable rate funding	PWLB	0		-
	Market	0		-
			0	
Other long term liabilities (PFI)			20.9	3.73
Total long term borrowing			1,750.30	2.67
Short term borrowing	PWLB		411.20	5.12
	LOCALS		-	-
Total Borrowing			2,161.50	5.12
Treasury Investments				
- Short term WBC Treasury			49.30	4.78

4.0 Borrowing Requirement and Loan Debt Maturity Profile

4.1 The Council's borrowing requirement is the amount the Council expects to need to borrow in the year, due to a forecast increase in overall loan debt plus maturing loans needing to be replaced.

Borrowing Requirement

	2025/26	2026/27	2027/28	2028/29
	£m	£m	£m	£m
Forecast increase in gross loan debt	77	67	67	69
Maturing loans	338	20	18	18
Total amount required to be borrowed	**415**	**87**	**85**	**87**

4.2 Details of the forecast increases in loan debt are set out below.

Increase in loan debt

	2025/26	2026/27	2027/28	2028/29
	£m	£m	£m	£m
Planned prudential borrowing for capital	10	6	5	8
Revenue shortfall - met by capitalisation direction	75	0	0	0
Later year revenue shortfalls - funding to be resolved	0	70	70	70
Less 'business as usual' MRP	-8	-9	-9	-9
Other cashflows eg movements in reserves	0	0	0	0
Forecast increase in gross loan debt	**77**	**67**	**67**	**69**

4.3 The main reason for the increase in debt is the requested Capitalisation Directive required to cover revenue expenditure until the Council is in a more sustainable financial position. The main element of the Capitalisation Directive will be to cover the loss of revenues arising from the suspension of interest previously paid by the wholly owned companies. Any new borrowing to support the capital programme will be subject to government approval. The capital programme for 2025/26 will only contain essential regulatory, health and safety and asset management expenditure, planned borrowing to support capital expenditure agreed in 2024/25 and some limited investment to realise revenue savings (please see Capital Strategy Annex I).

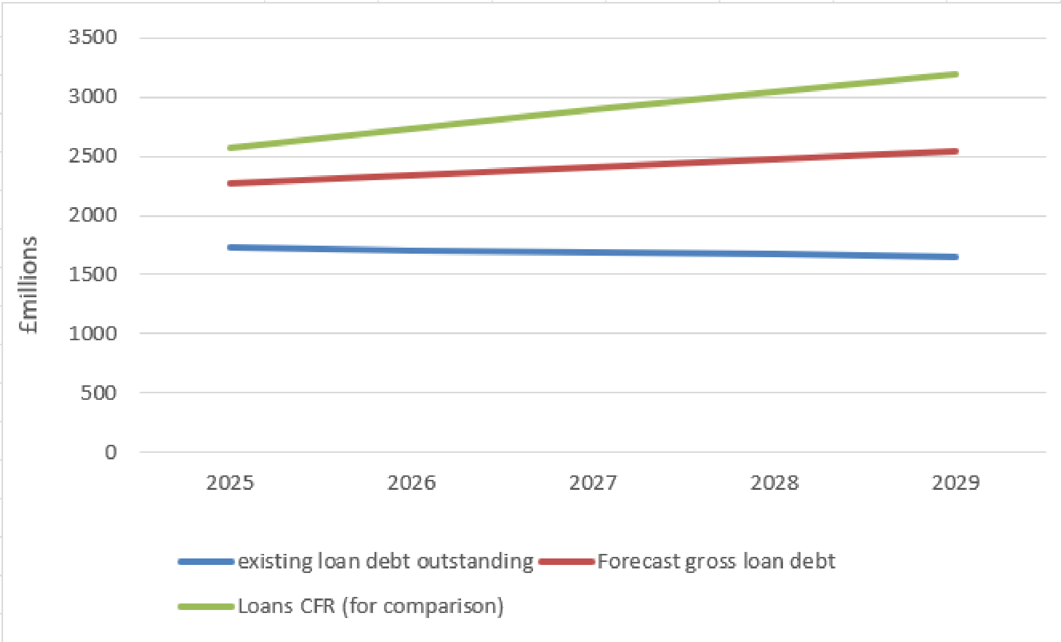
4.4 £338 million of the Council's existing borrowing matures in 2025/26, and this will need to be reborrowed (please see Appendix G Long Term Borrowing Maturity Profile). Replacement borrowing may also be required for Lender's Option Borrower's Option (LOBO) loans, if the lender exercises their right to increase the interest rate on the loan and the Council decides to repay the loan rather than accepting the increased rate. There are only £15 million of LOBO loans outstanding.

4.5 Due to the scale of the outstanding debt the Council has a Debt Reduction Plan which sits alongside its Asset Rationalisation Plan (please see section 9). The capital receipts realised will be applied to either repay existing debt or to avoid future borrowing.

Loan maturity profile and liability benchmark

4.6 The forecast level of loan debt compared with the Council's existing loans outstanding is shown in the liability benchmark prudential indicator:

Liability benchmark prudential indicator Table



4.7 The gap between existing loans outstanding (the blue line) and the Council's forecast loan debt (the red line) shows the borrowing requirement over the MTFP period. This shows the borrowing need rising slowly due to relatively low loan maturities in those years. A longer term projection is usually helpful to assess whether the Council's maturity profile matches well to its forecast debt outstanding. For the Council a long term projection is inappropriate due to the uncertainty over future debt levels.

4.8 The prudential limits for the maturity structure of borrowing are a means of controlling the proportion of borrowing across the maturity profile and the Council's maturity limits are as follows:

Prudential indicator: Maturity structure for fixed rate borrowing

% of loans maturing in:	**< 12 months**	**1-5 years**	**5-10 years**	**10-20 years**	**> 20 years**
lower limit	0%	0%	0%	5%	10%
upper limit	35%	30%	30%	40%	60%
analysis	The 12 month limit is higher than would normally be the case due to the uncertainty over the Council's future debt position and the strategy to repay a sizeable volume of debt over the future years.				
objective	To manage loan debt within these limits, subject to future arrangements for government support.				

5.0 Interest Rate Risk

5.1 Interest rate risk is the risk that fluctuations in interest rates will create financial burden on the organisation's finances. Variable rate borrowing and short term borrowing are especially sensitive to interest rate changes. This Council with an extremely high level of loan debt is very vulnerable to interest rate changes. The Treasury Code asks local authorities to use their own prudential indicators for interest rate risk, appropriate to their circumstances.

Prudential indicator: interest rate risk limits

General Fund impact of a 1% rise in interest rates	c£5 million in 2025/26
Maximum % of short term and variable rate debt	35% in 2025/26
Analysis	These limits will need to be much lower in later years
Objective	To remain within the limit

6.0 Outlook for Interest Rates

6.1 The Council has appointed the Link Group as treasury adviser to the Council and part of their service is to assist the Council to inform the Council view on interest rates. Appendix C sets out the Link Group forecasts with background narrative. The forecast is that interest rates will reduce over the next two years, and that short term and long term rates will be at broadly similar levels but with short term borrowing becoming a little cheaper than long term borrowing. This suggests that some longer term borrowing might be deferred, given a reasonable prospect of lower rates in a year or two's time.

7.0 Borrowing Strategy

7.1 The borrowing requirement in paragraph 4 above shows a borrowing requirement of £415 million for 2025/26 mainly replacing maturing loans as well as supporting some limited capital expenditure. The Link interest rate forecasts above suggest that borrowing costs may start to fall during 2025/26. The Council's Debt Reduction Plan will also consider how capital receipts from asset rationalisation should be applied.

7.2 The Council's ongoing discussions with the Commissioners, government and the PWLB to develop funding solutions for the Council's borrowing and other financial problems have a major bearing on the borrowing strategy. In the short term, adverse revenue cashflows may require temporary borrowing whilst longer term plans to stabilise and reduce the Council's debt may make long term borrowing. The bulk of the prudential borrowing in the capital programme has largely been limited to funding for Victoria Square Woking Ltd and Thameswey group of companies and these are expected to be relatively short term.

7.3 A proportion of borrowing out to three years or so may be appropriate to match the likely timescales for realising capital receipts. This will be kept under review as part of the developing Debt Reduction Plan by the Director of Finance.

7.4 HRA borrowing is accounted for in accordance with Government regulations and CIPFA guidance using the HRA CFR as the measure of HRA debt and apportioning a share of interest costs to it. HRA prudential indicators are reported in the Capital Strategy (at Annex I) and will in future be included in the HRA Business Plan.

7.5 This strategy will be kept under review throughout the year in the light of interest rate conditions and the latest Council's financial position.

<u>PWLB Borrowing</u>

7.6 The Council is likely to be dependent on the PWLB for most or all of its borrowing in 2025/26. The PWLB lends for a minimum period of 1 year. Regular meetings with MHCLG review and agree the Council's borrowing needs.

8.0 Policy on Borrowing in Advance of Need

8.1 Borrowing in advance of need' is where borrowing is taken before it is needed to meet the Council's operational cashflows. This results in surplus cash which requires investment until needed. Government Investment Guidance expects local authorities to have a policy for borrowing in advance, largely because of the increased treasury risks it creates including credit risk on the surplus cash invested.

8.2 The Council is a substantial net borrower, and in order to minimise its debt outstanding and its treasury investment exposures, it should only have surplus cash for short periods to cover in-year cashflows. The Council will not borrow more than or in advance of its needs purely to profit from the investment of the extra sums borrowed. It is highly unlikely that any borrowing would be undertaken in advance of need and any decision to do so would need to demonstrate significant financial and operational benefits and would require government approval. Regular meetings are held with Government to review any borrowing requirements before PWLB loans are drawn down. These meetings provide an additional external check on borrowing in advance of need.

8.3 In determining whether borrowing will be undertaken in advance of need the Council will:

- ensure that the Council's forecast borrowing requirement supports a clear need for borrowing in the coming one to three years to meet the authority's current plans and expected cashflows;
- ensure that the on going revenue liabilities created, and the implications for future plans and budgets have been considered, including the cost of carry of the borrowing until it is needed and the credit risk of the investment required;
- evaluate the economic and market factors that might influence the manner and timing of any decision to borrow;
- consider the merits and demerits of alternative forms of funding; and
- consider the alternative interest rate bases available, the most appropriate periods to fund and repayment profiles to use.

9.0 Debt Reduction and Restructuring

9.1 As part of the intervention there is a requirement on the Council to reduce the level of assets held hence the levels of outstanding debt. This forms a key part of the Council's overall Improvement and Recovery Plan. The Director of Finance is working with Commissioners to develop a Debt Reduction Plan (DRP) alongside the development of an Asset Rationalisation Plan. This joint work will ensure that the asset disposal programme is underpinned by a detailed option appraisal considering the benefits and risks of disposals and, in the case of company assets, the impact on the companies' cash flow position. It will need to balance the imperative to reduce debt with the need to secure a managed exit from commercial arrangements, achieve best consideration and optimise value for the public purse.

9.2 The attached principles for debt reduction have been drafted (see appendix E).

9.3 The key principle is that all proceeds from the sale of General Fund assets (including those from the Council's companies), will be presumed to be used to reduce debt, rather than fund further expenditure. The reduction in debt is likely initially to involve not borrowing, rather than actual repayment of PWLB debt, given the initial need for funding for the Capitalisation Directive.

9.4 The Council's debt problem related to the General Fund not the Housing Revenue Account. For HRA assets the primary consideration will be the sustainability of the HRA. HRA land disposals are likely to be required to reinvest in stock to meet the regulatory requirements and ensure that the investment is affordable in accordance with the Prudential Code and HRA rules.

9.5 Before the Council does actually repay PWLB debt, there will need to be discussions with Government on how the rules governing debt restructuring for local authorities apply. The PWLB operates a system of premiums or discounts on the repayment of borrowing which will impact on the interest savings that are achievable. The level of savings will be reduced unless the Council is given some dispensation.

9.6 Debt rescheduling is considered to be part of general Treasury Management and therefore decisions regarding debt rescheduling are delegated to the Chief Finance\S151 Officer as detailed in the delegated functions section of the Constitution.

9.7 Progress on the Debt Reduction and Asset Rationalisation Plans will be reported to Council and Executive as part of the Improvement and Recovery Plan and any debt rescheduling will be reported to the Executive in subsequent treasury monitoring reports.

10.0 Annual Investment Strategy for treasury management investments

Investment Policy

10.1 The Council's ongoing policies for treasury management investments are set out at Appendix D. These policies determine in particular the Council's arrangements for prioritising security, liquidity, and yield in that order, as recommended by the DLUHC Investment Guidance. They include the Council's criteria for making treasury investments of a high credit quality (using credit ratings and other information), and criteria for the maximum maturity of investments. The Director of Finance may also appoint investment managers.

Investment Strategy

10.2 The Council has surplus cash to lend only for short periods, as part of day to day cashflow fluctuations and as part of maintaining adequate liquidity. For these purposes, the Council's treasury team will expect to hold around £15 million of treasury investments.

10.3 The Council's Money Market Fund limits have been reviewed. Any reduction in Money Market Fund limits may inhibit the Council in receiving and holding capital receipts arising from asset sales prior to them being used for the repayment of debt.

10.4 The Council currently holds no treasury management investments for which the remaining time to maturity is in excess of one year. Such investments are unlikely to be appropriate as the Council is a substantial net borrower and only needs to invest to cover short term cash flows. In the unlikely event that longer term investments become appropriate, the Council will apply a long term prudential limit for treasury management investments as follows:

Long term treasury management investments

Maximum investment limit: Limit	**2023/24** £20 million	**2024/25** £10 million	**Longer** £0 million
Analysis	The Council is a net borrower/high debt authority and will apply long term cash funds to repay debt.		
Objective	To remain within the limit or avoid long term treasury investments).		

10.5 Investments will accordingly be made with reference to cash flow requirements and the outlook for short-term interest rates (i.e. rates for investments up to 12 months). Were there to be any core balance of funds up to £10 million available for investment over a 0-5 year period, these funds that would be managed in discussion with Tradition UK or other UK money market brokers or investment advisers.

10.6 For its cash flow generated balances, the Council will seek to utilise its Lloyds business reserve account, money market funds and short-dated deposits (overnight to three months) using secure counterparties in order to benefit from the compounding of interest.

10.7 Link's view, along with many other commentators, is that UK interest rates (short and long term) will start to fall during 2024/25. This would mean a relatively small reduction in interest earned from the treasury investments. However, this would be more than offset by a similar reduction in interest costs on the larger value of borrowing.

10.8 The Council will receive monthly reports on its investment activity in budget monitoring, an annual monitoring report to the Overview and Scrutiny Committee and at the end of the financial year as part of its Annual Treasury Report.

11.0 Treasury management revenue budget

11.1 Based on the above interest rate outlook, borrowing strategy and treasury investment strategy, the revenue budget for treasury management is as follows:

	2024/25	2025/26	2026/27	2027/28	2028/29
	£000	£000	£000	£000	£000
gross interest payable	68,791	73,108	74,823	76,118	79,115
loan premium / discount charges	16	16	16	16	16
less capitalised interest	0	0	0	0	0
General Fund MRP	7,535	7,986	8,698	8,698	8,698
Gross financing costs	**76,342**	**81,111**	**83,537**	**84,831**	**87,829**
Interest charged to HRA	-5,538	-5,613	-5,688	-5,688	-5,864
Expenses charged to HRA	-36	-36	-36	-36	-36
Gen Fund gross financing costs	**70,804**	**75,498**	**77,849**	**79,143**	**81,966**
interest receivable:					
- treasury investments	-694	-488	-450	-450	-450
- ThamesWey and VSWL	-46,351	-46,064	-45,910	-45,883	-45,883
- other service investments	-719	-711	-711	-711	-711
'business as usual' budget	**23,040**	**28,236**	**30,778**	**32,099**	**34,922**
less suspended interest	46,351	46,064	45,910	45,883	45,883
General Fund treasury budget	**69,391**	**74,300**	**76,688**	**77,983**	**80,805**

11.2 The General Fund MRP includes only the amount that is expected to be charged to the revenue account for the year (i.e for 2025/26 it excludes £96.5m that has been requested to be deferred through the Exceptional Financial Support request to MHCLG).

11.3 Given the suspension of interest income from the Group Company investments, this interest burden is far higher than the Council is able to sustain, and longer term solutions are being considered with the Commissioners and DLUHC.

11.4 The budgeted cost in each year is based on the Council's current forecasts and plans. Actual interest costs will be affected by the nature of future Government extraordinary support, future interest rates, cashflows, the level of reserves and provisions, and any debt restructuring. Sections 5 and 6 above have discussed the potential volatility of the treasury budget due to the potential upsides or downsides to the interest rate outlook and the large scale of the Council's short term borrowing as a consequence of the debt reduction plan.

12.0 Banking services

12.1 The Council's bankers, Lloyds, have a policy for Councils subject to a Section114 notice that requires the Executive to consider the Council's continued use of facilities which it has with Lloyds Bank in light of the issue of the Section 114 notice. Banking facilities are an essential part of the Council's current funding plans, to enable it to continue to provide its statutory services. In view of this the Council has the power to enter into and continue to use the banking facilities.

13.0 Use of External Service Providers

13.1 As previously stated, the Council uses Link Asset Services as its external treasury management advisors (who provide access to specialist skills and resources). The services provided include the following:-

- Provision of interest rate forecasts and advice on borrowing and investment strategies;
- Regular updates on economic and political changes;
- Forecasts of movements in Public Works Loan Board rates;
- Advice on debt rescheduling, funding policy, volatility and maturity profile analysis;
- Advice on investment counterparty creditworthiness;
- Provision of annual template documents and advice on the various Treasury Management reports; and
- Treasury Management training.

13.2 Although external treasury management advisors are used undue reliance is not placed upon the external service provider and the responsibility for treasury management decisions remains with the Council.

13.3 The Council uses money market brokers, and may also use other borrowing or investment advisers, managers and other treasury service providers. The Strategic Director for Finance may procure, appoint and dismiss all external treasury service providers as required.

14.0 Minimum Revenue Provision (MRP) Policy

14.1 Local authorities are required by law to '*charge to a revenue account a Minimum Revenue Provision (MRP) for that year'*. MRP is an annual amount set aside from the General Fund to meet the cost of capital expenditure that has not yet been financed from available resources. MRP is the mechanism to repay borrowing and other liabilities used to fund capital expenditure. The Council's Capital Financing Requirement (CFR) is the measure of the unfinanced capital outstanding (and detailed in the Capital Strategy at Annex I).

14.2 Local authorities are also required to produce an annual MRP Policy Statement which sets out how the charge to revenue account is calculated. The Council commissioned independent external review by Worth Technical Accounting Solutions to review its MRP policy and revenue charges. This review confirmed the Council, due predominantly to the policy of not charging MRP on the loans to companies has systematically understated. The cumulative under provision in the Council's accounts to 31 March 2025 is estimated at £503 million. MRP and MRP arrears are a high value component of the Council's financial challenges.

14.3 The latest government guidance on MRP has allowed for exceptions ("*Where local authorities are unable to manage financial pressures and as a consequence are financially unsustainable or at risk of being so, local authorities should approach the government for support", paragraph 21).* Exceptional circumstances were applied to the Council in 2024/25 as part of the government's Exceptional Financial Support package and a similar request has been made for Exceptional Financial Support in 2025/26.

14.4 As was the case for 2024/25, the Council has requested that it only make 'business as usual' MRP of £8 million for 2025/26 In its request for Exceptional Financial Support. This exceptional MRP relief, if approved, should allow the Council to set a legal budget for 2025/65. MRP arrangements in the longer term will need to be addressed by the longer term debt reduction plan. The Government accepts that Council cannot meet all the borrowing liabilities and the debt charge consequences and is committed to working with the Council on a long-term solution. All budget setting related MRP projections assume this will continue. The 2025/26 MRP policy is set out in Appendix A and requires annual approval as part of 2025/26 budget setting.

15.0 Skills, Capacity and Training

15.1 CIPFA's Treasury Management Practice (TMP10) expects officers and members to receive treasury management training appropriate to their roles. General treasury training has been, and will continue to be provided by Link, but establishing in house skills and capacity to an appropriate level continues to be a challenge for the Council.

15.2 The Strategic Director for Finance will continue to implement the recommendation of TMP 10 to identify the competencies required for the main roles at officer and member level, including knowledge and skills schedules and identifying the training needed to meet any gaps. At present the Council's skills and capacity at officer level is being enhanced through interim and consultancy appointments but it is necessary to ensure a good level of in house skills and capacity appropriate to the demands of the Council's debt and investment position.