CHESHIRE FIRE AUTHORITY

MEETING OF: **CHESHIRE FIRE AUTHORITY**
DATE: **4th DECEMBER 2024**
REPORT OF: **TREASURER & HEAD OF FINANCE**
AUTHOR: **JAMES CUNNINGHAM**

SUBJECT: TREASURY MANAGEMENT – MID YEAR REPORT 2024-25

Purpose of Report

1. To update Members on performance against the Authority's Treasury Management Strategy (TMS).

Recommended That Members**:**

[1] note the report; and

[2] note the future requirement for borrowing to support the ongoing Capital Programme; and

[3] note the need to consider the approach to the longer term investment of the capital receipts from house sales.

Background

2. The first requirement for treasury management is to ensure that the organisational cash flow is adequately planned with cash being available when it is needed. Surplus monies are invested in low risk counter-parties or instruments commensurate with the low risk appetite, providing adequate liquidity initially before considering investment return. This means the order of priority for all investment decisions is Security, Liquidity (access to cash) and then Yield (interest earned).

3. The second main function of treasury management is the funding of capital plans. These capital plans provide a guide to the borrowing need which is essentially the longer term cash flow planning to ensure that capital spending obligations can be met. The management of longer term cash may involve arranging long or short term loans or by using longer term cash flow surpluses. On occasion any debt currently held may be re-structured in line with risk or cost objectives.

4. Accordingly, treasury management is defined as:

   "The management of the authority's borrowing, investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

5. This report has been written in accordance with the requirements of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised 2021) which recommends that those charged with governance are updated on treasury management activities regularly by way of a strategy at the start of the year, followed by quarterly reviews (at Performance and Overview Committee) and an outturn report.

6. CIPFA published revised Prudential and Treasury Management Codes on 20 December 2021 with formal adoption being required for the 2023/24 financial year.

7. The Authority had regard to these changes when approving an annual Treasury Management Strategy and an associated Capital Strategy for 2023/24 on 15 February 2023. It also did so in February 2024.

8. This mid-year report has been prepared in compliance with CIPFA's Code of Practice on Treasury Management, and covers the following:

    - An economic update for the first part of the 2024/25 financial year;
    - A review of the Treasury Management Strategy Statement (including the Annual Investment Strategy);
    - The capital expenditure and borrowing position;
    - A review of the investment portfolio for 2024/25;
    - A review of compliance with Treasury and Prudential Limits for 2024/25.

ECONOMIC BACKGROUND

9. The first half of 2024/25 (April-Sept) saw:

    - Labour winning the General Election on the 4th July, with an 156 seat majority.
    - Interest rates held at 5.25% until a ¼ rate cut on 25th July 2024. Expected cuts in the interest rate are taking longer to materialise, as the Monetary Policy Committee of the Bank Of England continues to manage inflation against a backdrop of slowing economic output.
    - GDP continues to decline.
    - CPI inflation falling to 1.7% in September, the lowest seen since October 2021.

10. The Bank Of England's blunt tool for managing inflation down through high interest rates appears to have worked. However there has been a reduction in business confidence and GDP, businesses being unwilling to make loan funded investment due to the high cost of borrowing.

11. Whilst the Bank of England has been messaging that interest rates would start to fall in 2024, it has taken longer than expected. A number of forecasts now suggest rates will eventually fall to 4%-3.75% by the end of next year. This leaves many businesses with the invidious decision to either continue to hold up on loan funded investment or to take the cost of higher interest rates and either pass to the consumer or to reduce profit margin.

12. The Chancellor gave her first Budget speech on the 30th October 2024. She set out ambitious investment plans in the public sector, however funded through extending the fiscal rules on borrowing and a sizeable tax rise for businesses through the Employer National Insurance contribution.

13. The Authority has appointed Link Group as its treasury advisors and part of their service is to assist with formulating a view on interest rates. The latest forecast on 11th November sets out a view that short, medium and long-dated interest rates will be elevated for some little while, as the Bank of England seeks to squeeze inflation out of the economy.

Link Group Interest Rate View	11.11.24												
	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27	Jun-27	Sep-27	Dec-27
BANK RATE	4.75	4.50	4.25	4.00	4.00	3.75	3.75	3.75	3.50	3.50	3.50	3.50	3.50
3 month ave earnings	4.70	4.50	4.30	4.00	4.00	4.00	3.80	3.80	3.80	3.50	3.50	3.50	3.50
6 month ave earnings	4.70	4.40	4.20	3.90	3.90	3.90	3.80	3.80	3.80	3.50	3.50	3.50	3.50
12 month ave earnings	4.70	4.40	4.20	3.90	3.90	3.90	3.80	3.80	3.80	3.50	3.50	3.50	3.50
5 yr PWLB	5.00	4.90	4.80	4.60	4.50	4.50	4.40	4.30	4.20	4.10	4.00	4.00	3.90
10 yr PWLB	5.30	5.10	5.00	4.80	4.80	4.70	4.50	4.50	4.40	4.30	4.20	4.20	4.10
25 yr PWLB	5.60	5.50	5.40	5.30	5.20	5.10	5.00	4.90	4.80	4.70	4.60	4.50	4.50
50 yr PWLB	5.40	5.30	5.20	5.10	5.00	4.90	4.80	4.70	4.60	4.50	4.40	4.30	4.30

14. Unfortunately, the forecast PWLB rates remain stubbornly high. Our current strategy is to continue to utilise internal borrowing and avoid taking on loans. When we do need to take on a loan it would be for a shorter period (3-5 years) and then re-finance for a longer period (40-50 years) once rates have fallen.

TREASURY MANAGEMENT STRATEGY STATEMENT UPDATE

15. The Treasury Management Strategy Statement (TMSS) was approved by the Authority on February 2024.

16. The Authority authorised the sale of the nine houses held at Stockton Heath. The houses were originally in place to support a Day Crew duty system. However, Stockton Heath moved to the on-call duty system and is now part of the Nucleus Day Crew system shared with Birchwood as a result of the CRMP 24-28 fire cover review. As such the houses are no longer required by the Service.

17. The Capital Receipt from the sale of the houses is planned to be used to part fund the rebuild of the fire stations at Ellesmere Port and Warrington. The Authority is committed to rebuilding these stations in the life of the current CRMP.

18. In light of the falling interest rates, Members may wish to consider amending the Treasury Management Strategy in terms of the maximum length of investment held. The current Strategy sets out that we do not hold deposits with a maturity of greater than a year.

19. Given a station re-build project will have a significant lead time (design, consultation, planning and tender), Members may wish to consider placing the receipts from the house sales from Stockton Heath on a longer term deposit to match this timeframe.

CAPITAL PROGRAMME AND BORROWING

20. In preparing the Capital Programme, attention is given to understanding the potential liabilities and risks associated with the expenditure and funding of expenditure, in particular, the combined impact on the overall financial position of the Authority in terms of revenue and capital budgets. This is to ensure that such activity remains proportionate. There is a relationship in anticipating that borrowing which will be required to fund the Capital Programme and the associated Minimum Revenue Provision and interest payable revenue costs.

21. The table below provides an indication of the Capital Programme, the resulting amount of annual borrowing required and the associated revenue financing costs estimated over the next few years. Members should note that the Modernisation Programme is under review and the outcome will impact the estimates.

Table 1: Capital Expenditure Forecasts	**2024/25 £'000s**	**2025/26 £'000s**	**2026/27 £'000s**	**2027/28 £'000s**
Forecast Capital Programme	4,643	3,965	9,905	9,655
To be Funded by new borrowing	250	250	4,500	4,500
Estimated associated revenue cost of existing plus new borrowing (MRP & Interest Payable)	1,110	1,722	2,018	2,298

22. The Authority currently has a loan portfolio of £11.5m which includes external borrowing of £11m to finance the Training Centre project, secured from PWLB at favourably low fixed rates in March 2021 (£4m at 1.99%), July 2021 (£4m at 1.65%) and November 2021 (£3m at 1.63%). There is a £0.4m loan to be repaid on the 31st March 2025.

23. In addition to the loans for the Training Centre, it was anticipated that the Authority would take out further loans to fund the purchase of houses at Wilmslow (£3.4m) and the re-build of Crewe fire station (£7.3m). The

Authority has currently avoided taking these loans by utilising cash reserves. However this is only a short term relief and the loans will need to be taken at some point.

24. In addition to the loans taken and loan requirement above, Table 1 sets out the forecast Capital Programme and how much we would fund by new borrowing. The largest element of the forecast Capital Programme relates to the re-builds anticipated at Ellesmere Port and Warrington. However, it must be stressed that these are only estimates at this stage as there as are yet no firm plans. The total of loans taken and expected to be taken to fund the Capital Programme is termed the Capital Financing Requirement.

25. There continues to be building cost inflation impacting upon our Fire Station Modernisation programme. Whilst works have started at Knutsford and Winsford in 2024/25, a review of the requirements is taking place Frodsham and the 4 stations left to complete the programme in 2025/26. A revised Capital Programme will be presented to Members in February 2025.

26. Table 1 includes estimates for loan interest rates and timings of when additional funding will be taken. £10.5m is required for Wilmslow and Crewe (currently funded through internal borrowing); a further £9m for the fire station rebuilds and £1.25m for house refurbishment has already been factored into the estimated revenue impact from interest repayment and MRP calculation.

27. Historically, the Authority has financed the majority of its Capital Programme from reserves and capital grants. However there have been no Capital Grants available since 2014, since when the Authority has used PWLB loans to enable significant capital works. As such all capital funding will come from Revenue, either by direct spend, repayment of loans or setting aside money to a capital reserve for future projects.

28. The following tables show the actual debt maturity profile of current borrowing as at 31 October 2024 and a comparison with approved Upper and Lower Limits.

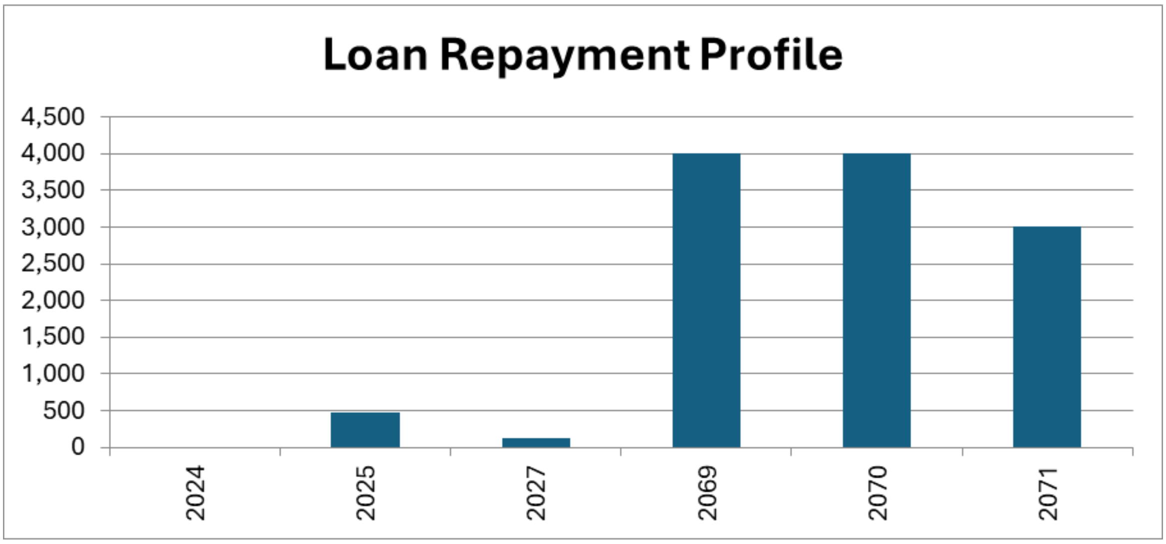


Table 2: Maturity Structure of Authority Borrowing	Lower Limit %	Upper Limit %	Actual 31/10/24 %	Amount £ 000
Under 12 months	0%	15%	4%	467
12 months to 2 years	0%	15%	1%	119
2 years to 5 years	0%	25%	0%	0
5 years to 10 years	0%	25%	0%	0
10 years and above	50%	100%	99%	11,000
TOTAL			**104%**	**11,586**

29. The above indicators are designed to be a control over an authority having large concentrations of fixed rate debt having to be replaced at times of uncertainty over interest rates. The limits will be reviewed for the next Treasury Management Strategy paper in February 2025 and the upper limits are likely to be amended to take account of the potential to undertake shorter term borrowing followed by re-financing to avoid being tied to high interest rates for a long time.

30. Advice has again been sought from the Authority's Treasury Management advisors on the potential for debt restructuring. They suggest that opportunities have been very limited in the current economic climate given the structure of interest rates and associated early loan repayment penalties. No debt rescheduling has therefore been undertaken or is anticipated in the current financial year.

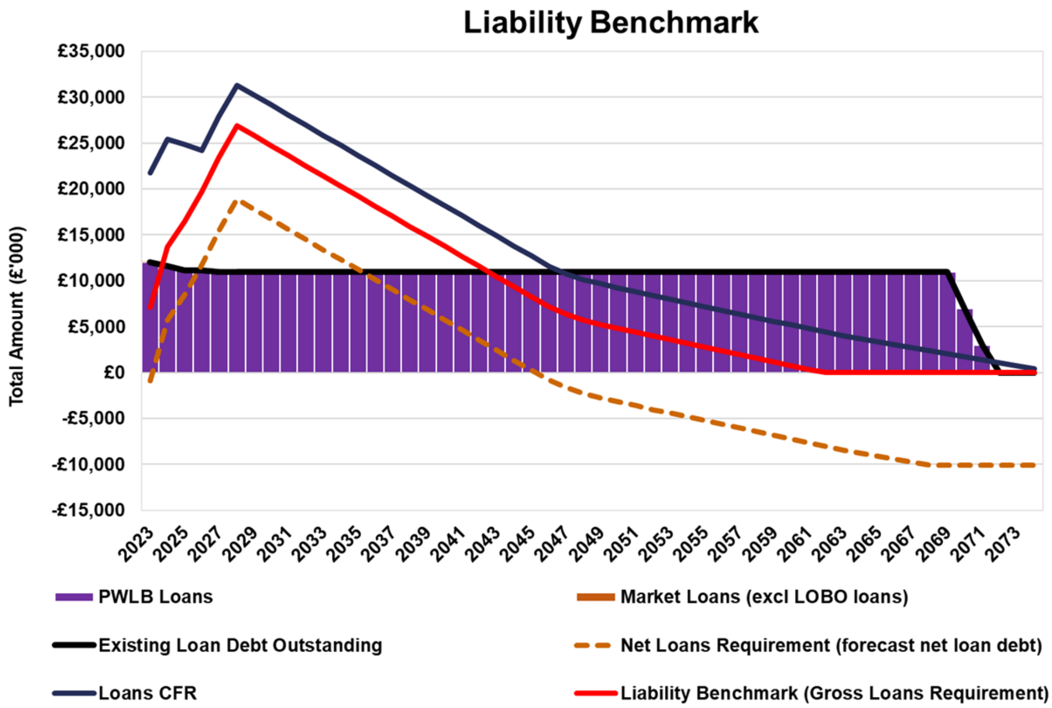
LIABILITY BENCHMARK

31. A new prudential indicator from 2023/24 is the Liability Benchmark (LB). The Authority is required to estimate and measure the LB for the

forthcoming financial year and the following two financial years, as a minimum. However, CIPFA strongly recommends that the LB is produced for at least ten years and should ideally cover the full debt maturity profile of a public body. The chart below covers the Authority's full debt maturity profile as recommended.

32. There are four components to the Liability Benchmark:

1. **Existing loan debt outstanding**: the Authority's existing loans that are still outstanding in future years.
2. **Loans Capital Financing Requirement (CFR)**: this is calculated in accordance with the loans CFR definition in the Prudential Code and projected into the future based on approved prudential borrowing and planned MRP.
3. **Net loans requirement**: this shows the Authority's gross loan debt less treasury management investments at the last financial year-end, projected into the future and based on approved prudential borrowing, planned MRP and any other major cash flows forecast.
4. **Liability benchmark (or gross loans requirement)**: this equals net loans requirement plus short-term liquidity allowance.



33. The aim of the LB is to minimise/reduce refinancing, interest rate and credit risks by informing the timing and duration of new external borrowing.

34. The position is largely unchanged from that reported in the Treasury Management Strategy and shows that the Authority's LB is currently rising sharply to a peak in around 2028 indicating the additional borrowing requirement associated with delivery of the currently approved major

estates projects. This requirement then reduces as provision is made to repay outstanding borrowing via the annual MRP charge whilst no further Capital Expenditure financed by borrowing is currently planned beyond 2028.

35. In view of this, by around 2043 the LB will have reduced back down to the level of the existing loan portfolio, indicating that although there is a significant short to medium term requirement for new borrowing, this borrowing would ideally be for a range of durations up to around 20 years, i.e. filling the white triangular period in the chart between 2023 and 2038 where the LB (red line) exceeds the current loan portfolio (black line/bar chart).

36. The chart continues to show that that the existing loan debt portfolio will be fully repaid by 2072 and that the requirement to borrow (CFR) will also be reduced to nil by 2074, indicating that the Authority's current MRP policy remains prudent and appropriate.

37. The chart then indicates that without any further new approved capital expenditure financed by borrowing beyond the period of the current Capital Strategy, the existing borrowing portfolio exceeds the LB after 2043. If this remains the case then it indicates either excess cash requiring investment or an opportunity to repay/restructure debt over this future period.

INVESTMENT PORTFOLIO 2024/25

38. The Annual Investment Strategy has the priorities of security, liquidity and yield. The aim is to achieve the optimum yield within the approved investment counter-parties which are scrutinised regularly for creditworthiness within the security principle. Liquidity is achieved within the forecast spending profile and cashflows.

39. Relatively high interest rates and proactive cashflow management have enabled the Authority to secure significantly increased short to medium term rates of return over the year and will again result in a surplus versus budget in 2024/25. It is however anticipated that the opportunity to generate ongoing investment returns at current levels will reduce towards the end of 2024/25 as planned capital expenditure, and the continuing deferral of approved borrowing, has a significant impact upon cashflow balances available for investment. In addition, the two recent drops in the Bank of England base rate have been passed immediately to deposit rates. Forecasts are for further drops in interest rates ahead.

40. Interest on balances earned to date is £260k to 31 October, with final 2024/25 outturn currently forecast to be around £600k.

41. The Authority has continued with a cautious approach to its choice of counterparties, making use of its External Treasury Management Advisor to monitor the risk profile of the counterparties with whom it places its money. As at 31 October 2024, the Authority's investments were either held in call accounts (immediately available) - Lloyds Bank of Scotland, Federated Hermes Money Market Fund, Aberdeen Standard Liquidity

Money Market Fund- or short term deposit accounts - Goldman Sachs, Lloyds and the HM Government Debt Management Office. The short term deposits mature between November 2024 and February 2025.

Investments 31/10/2023	£'000
Call accounts	
Lloyds	1,200
Federated Hermes MMF	1,885
Aberdeen Standard Liquidity MMF	2,435
Short term deposits	
Goldman Sachs	4,000
Lloyds BOS	4,000
Santander	3,000
DMO	1,600
Total	**18,120**

42. There have been no instances of non-compliance with approved Annual Investment Strategy limits during the year.

REVIEW OF COMPLIANCE WITH PRUDENTIAL INDICATORS

43. It is a statutory duty for those charged with governance to determine and keep under review a range of prudential indicators and treasury limits. During the financial year to date, treasury management activities have operated within the approved indicators and limits and in compliance with the Treasury Management Practices. The following table compares the estimated performance on key prudential indicators in 2024/25 against those approved by the Authority in February 2024.

Table 3: Prudential and Treasury Indicators			
Prudential Indicators	**2024-25 Indicator £000**	**2024-25 Estimate £000**	**Comment**
Capital expenditure	5,190	5,190	Capex spend on the station modernisation programme is being reviewed and Members will be updated at forthcoming Planning Days.
Capital financing requirement	24,817	25,008	
Annual change in capital financing requirement	(637)	(651)	
Gross borrowing requirement: (Under) / Over borrowing	(6,698)	(6,635)	We will continue to make use of internal borrowing to save on interest costs
Ratio of financing costs to net revenue stream	2.36%	2.33%	
Treasury Indicators	**2024-25 Indicator £000**	**2024-25 Estimate £000**	
Authorised limit for external debt	23,319	23,319	Set 14/02/24, no change during 2024-25.
Operational boundary for external debt	21,319	21,319	
Actual external debt			Current borrowing £11.586m. £0.467m is to be repaid on 31 March 2025. Dependent on cashflow management there may be short term borrowing toward the end of the fiscal year.
- Borrowing	18,119	11,586	
- Other long term liabilities	0	0	
Total	18,119	11,586	
Upper limit of fixed interest rate exposure	100%	100%	
Upper limit of variable interest rate exposure	25%	Nil	No variable rate loans held or planned
Upper limit for principal sums invested for over 364 days	£nil	£nil	Consider longer term deposit for house sales to match to Warrington / Ellesmere Port fire station builds

Financial Implications

44. The subject of this report is financial.

Legal Implications

45. The Local Government Act 2003 and the associated CIPFA Code of Practice for Treasury Management recommends that those charged with governance are updated on treasury management activities regularly by way of a strategy at the start of the year, followed by quarterly reviews and an outturn report.

Equality & Diversity Implications

46. There are no known equality and diversity issues arising from this report.

Environmental Implications

47. There are no known environmental issues arising from this report.

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BACKGROUND PAPERS: None