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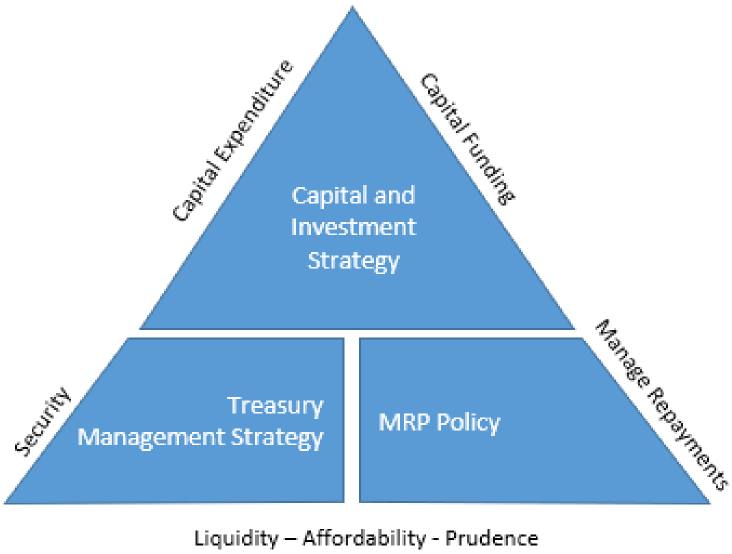
Annex F

Capital, Investment and Treasury Management Strategy 2025/26

1. INTRODUCTION

1.1 The Capital, Investment and Treasury Management Strategy provides an overview of the three main components of capital planning. We have chosen to amalgamate the strategies into a single document because the Capital Programme, our Investment Strategy and our approach to Treasury Management cannot operate independently of one another. They are parts of an overall approach:

- **Capital expenditure and investments:** the Capital Programme; supporting Corporate, Directorate and Service priorities and the Investment Programme; generating income and supporting economic growth;
- **Financing our capital plans, and maintaining liquidity:** the Treasury Management Strategy; setting out how the capital programme will be financed and how cash investments will be managed; and
- **Repaying our debt in a prudent way:** the Minimum Revenue Provision (MRP) Policy, setting out how we use the revenue budget to repay debt.



This report sets out a high-level overview of how capital expenditure, capital financing, investments and treasury management activity contribute to the provision of services, along with an overview of how associated risk is managed and the implications for future financial sustainability.

1.2 The strategy sets out a clear picture of the ambition of the Council regarding capital expenditure and investment plans, within the financial constraints, risk appetite and regulatory framework that the Council operates.

1.3 The strategy is presented in the following elements, that set out the Council's approach to capital, investment and treasury management:

a. Capital Overview - capital expenditure planning, risk management and long-term sustainability of capital expenditure plans (Section 2)

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b. Investment Overview – setting out investment plans focusing on the approach to service and commercially led investment (Section 3);

c. The Treasury Management Strategy Statement (TMSS) – setting out how we borrow and invest to support our capital financing requirement (Section 4)

d. The Minimum Revenue Provision (MRP) Policy – setting out how we repay capital borrowing (included as the final page of this document, Annex G to the Budget)

1.4 Decisions made this year on capital, investment and treasury management will have financial consequences for the Council for many years into the future. They are therefore subject to both a national regulatory framework and to local policy framework, summarised in this report.

1.5 Our strategy will:

- Set out how we ensure that capital expenditure contributes to the achievement of corporate priorities and the organisation strategy;
- Explain how the Capital Programme is financed and demonstrate that it is affordable and sustainable;
- Explain the Council's approach to investments; and
- Set out and fulfil the Council's regulatory requirements in respect of Borrowing, Treasury Management and Investment.

2. CAPITAL OVERVIEW

Capital Expenditure and Financing:

2.1 The Council incurs two types of capital expenditure:

- service delivery capital programme expenditure
- capital investment

2.2 This section sets out the Council's capital expenditure and financing plans over the medium-term, provides an overview of the governance arrangements for approval and monitoring of expenditure and provides a projection of the capital financing requirement and how this will be funded and repaid. It links to the Council's borrowing strategy and sets out the Council's statutory duty to make an annual revenue provision for the repayment of debt, detailed in the MRP Policy (Annex G to the Budget).

Capital Expenditure

2.3 Capital expenditure refers to Local Authority spending on assets such as property, infrastructure, vehicles and equipment that will be used for more than one year. In Local Government this includes spending on assets owned by other bodies and loans and grants to other bodies, enabling them to buy assets.

2.4 The 2025/26 – 2029/30 Capital Programme, sets out capital expenditure plans of £1,399m, as summarised in Table 1. Our capital expenditure can be broken into three categories:

- Approved Capital Budget of £1,012m.
- Capital Pipeline of £382m, schemes that represent the capital ambitions of the Council but are subject to further detailed business cases and Member approval.

- Capital Investments of £4m, relating to expenditure on existing investment assets and capital loans to Council subsidiaries to spend on existing assets, ensuring the Council's compliance with the Prudential Code.

Table 1 - Estimates of Capital Expenditure 6

	2023/24 Actual	2024/25 Forecast	2025/26 Budget	2026/27 Budget	2027/28 Budget	2028/29 Budget	2029/30 Budget	Total Budget
	£m	£m	£m	£m	£m	£m	£m	£m
Capital Programme - Budget	298	314	340	271	180	125	97	**1,012**
Capital Programme - Pipeline	-	42	62	84	68	67	100	**382**
Sub-total Capital Programme	**298**	**356**	**402**	**355**	**248**	**192**	**197**	**1,394**
Commercial Spend	1	25	4	0	-	-	-	**4**
TOTAL	**299**	**381**	**406**	**355**	**248**	**192**	**197**	**1,399**

2.5 Our medium-term approach to financial planning means we aim to deliver an ambitious Capital Programme of c£1,399m over the next 5 years, if all pipeline proposals are approved and delivered. The revenue implications of this proposed programme are integrated and factored into the Medium-Term Financial Strategy (MTFS) to 2029/30.

2.6 Planned capital investment will deliver significant investment in:

- The development of a greener future through the Net Zero 2030 and 2050 carbon reduction schemes and other projects contributing to the carbon and green agenda such as rooftop solar, electric vehicle infrastructure and low emission buses and vehicles;
- A Highway Maintenance programme delivering improvements to roads and footways across the County;
- Community led projects in our towns and high streets through the Your Fund Surrey scheme;
- Developing Farnham town centre and surrounding infrastructure;
- Creating a number of sites to look after our vulnerable older adults, through building Extra Care and Independent Living accommodation where residents can live independently for longer and integrate into the community;
- Delivering additional local places for children with Special Educational Needs and Disabilities – a key part in containing costs within the revenue budget;
- Providing additional capacity in schools, to provide a rich education with Schools Basic Needs funding;
- Investment in in-county alternative provision places and improvements for improved pupil support
- Investment in libraries across the County;
- Maintaining and developing our road infrastructure to help grow a sustainable economy, deliver safer and greener routes; and
- Accelerating our Property Rationalisation and Agile Corporate Estate Programme.

2.7 Capital projects are subject to a rigorous governance process to ensure they are aligned with the Council's priorities of:

- Growing a sustainable economy so everyone can benefit;
- Tackling health inequality;
- Enabling a greener future; and
- Empowering communities.

2.8 Fundamentally, they are approved on the principles of strategic fit, value for money, affordability and deliverability. Projects need to demonstrate value for money and that they are capable of being delivered within expected timescales.

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2.9 Strategic Capital Groups (SCGs) for Infrastructure, Property and IT develop projects throughout the budget setting process which are scrutinised and approved by the Capital Programme Panel (CPP); a group of senior officers from across the organisation. Projects approved by CPP are then included in the budget when approved by Cabinet and Council. Fig 1, below summarises this process.

Fig 1: Capital Approval Process

	Strategic Mandate	Business Case	Delivery
Capital Strategy Groups	Strategic Mandates are developed and submitted to CPP	Approve Low Governance Schemes already in the budget where: Up to £1m and already been to Cabinet OR Up to 250k if not already been to Cabinet	Approve variations in scheme cost up to 10% and £250k
Capital Programme Panel	CPP approve Strategic Mandates	Approve Medium Governance Schemes where: Been to Cabinet and already in budget OR Up to £1m	Approve variations in scheme cost up to 10% and £500k
Cabinet		Approve High Governance Schemes or over £1m	Approve variations in scheme cost over 10% and £500k

Capital Funding

2.10 All capital expenditure must be financed, either from external sources (government grants and other contributions), the Council's own resources (revenue, reserves and capital receipts) or debt (borrowing, leasing and Private Finance Initiatives). The planned financing of the capital programme (as set out in Table 1 above), is as follows:

Table 2 - Capital Financing

	2023/24 Actual £m	2024/25 Forecast £m	2025/26 Budget £m	2026/27 Budget £m	2027/28 Budget £m	2028/29 Budget £m	2029/30 Budget £m	Total Budget £m
Grants and Contributions	92	99	127	116	85	109	150	**588**
Revenue budgets	6	6	1	1	1	1	1	**4**
Capital receipts	45	23	32	26	11	8	8	**86**
Borrowing	155	253	246	211	152	73	38	**721**
TOTAL	**299**	**381**	**406**	**355**	**248**	**192**	**197**	**1,399**

2.11 **Asset disposals:** When a capital asset is no longer needed, it may be sold so that the proceeds, known as capital receipts, can be spent on new assets or to repay debt. Repayments of capital grants, loans and investments also generate capital receipts.

2.12 Table 2 above, shows the planned usage of £86m of capital receipts from the sale of Council assets to finance expenditure from 2025/26 onwards. Receipts are only included as sources of financing when there is a high level of confidence over the value and timing of their delivery. This approach is taken to ensure a prudent estimate of borrowing is factored into capital plans and included in the revenue budget for finance costs.

2.13 Government have recently extended the ability of Council's to utilise capital receipts for revenue expenditure in specific circumstances. The Council currently has no plans to utilise this flexibility from 2025/26 onwards.

2.14 **Gross additional borrowing** of £246m for 2025/26 is required, £217m net of MRP and refinancing of long-term borrowing.

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Table 3 – Additional borrowing requirement

	31/03/2024 Actual £m	30/11/2024 Actual £m	31/03/2025 Estimate £m	31/03/2026 Forecast £m	31/03/2027 Forecast £m	31/03/2028 Forecast £m	31/03/2029 Forecast £m	31/03/2030 Forecast £m
Long term borrowing	472	468	463	455	446	440	435	430
Short term borrowing	295	525	535	535	-	-	-	-
Total borrowing	**767**	**993**	**998**	**990**	**446**	**440**	**435**	**430**
Forecast additional borrowing	-	5	-	216	928	1,036	1,061	1,047
Total forecast borrowing	**767**	**998**	**998**	**1,206**	**1,374**	**1,476**	**1,496**	**1,477**

2.15 Beyond March 2026 the split between long term and short-term borrowing will depend on decisions made in line with the Treasury Management Strategy below. This will include considerations about the prevailing rate of interest, the proportionality of the existing borrowing portfolio and other relevant considerations.

2.16 Borrowing is only a temporary source of finance, since loans and leases must be repaid, and this is therefore replaced over time by other financing, usually from revenue which is known as Minimum Revenue Provision (MRP). The Council's forecast MRP over the MTFS is set out in the following table and is based on the full MRP policy (Annex G).

Table 4 - Repayment of Debt Finance through Minimum Revenue Provision

	2023/24 Actual £m	2024/25 Forecast £m	2025/26 Budget £m	2026/27 Budget £m	2027/28 Budget £m	2028/29 Budget £m	2029/30 Budget £m
MRP	27	31	37	42	47	50	52

2.17 The Council's cumulative outstanding amount of debt finance is measured by the Capital Financing Requirement (CFR). This increases with new debt-financed capital expenditure on service delivery and on investments and reduces with MRP and capital receipts used to replace debt.

2.18 Based on the above figures for expenditure and financing, the Council's estimated CFR over the medium-term is set out in table 4.

Table 5 - Prudential Indicator: Estimates of Capital Financing Requirement

As at 31st March	2023/24 Actual £m	2024/25 Forecast £m	2025/26 Budget £m	2026/27 Budget £m	2027/28 Budget £m	2028/29 Budget £m	2029/30 Budget £m
Capital Programme	1,063	1,262	1,468	1,637	1,741	1,762	1,744
Investment Programme	440	456	451	442	433	425	416
TOTAL	**1,503**	**1,718**	**1,919**	**2,079**	**2,174**	**2,187**	**2,160**

2.19 Our capital plans lead to a £443m increase in the estimated CFR over the five-year period, from £1,718m to £2,160m (£721m of additional borrowing (see table 2), offset by £227m of MRP payments (see table 3) and £37m of PFI and finance lease adjustments). The revenue implications of this are set out below.

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Revenue Budget Implications

2.20 Although capital expenditure is not charged directly to the revenue budget, interest payable on loans, and MRP are charged to revenue, offset by any investment income receivable. This is referred to as net financing costs.

2.21 Current projections show that net financing costs, contained within the central income and expenditure budget projections over the MTFS, rise from a net £41m in 2024/25 to £75m net in 2029/30. The gross and net costs of financing our capital plans are set out in the table, below.

Table 6 – Net Finance Cost

	2023/24 Actual	2024/25 Forecast	2025/26 Budget	2026/27 Budget	2027/28 Budget	2028/29 Budget	2029/30 Budget
	£m	£m	£m	£m	£m	£m	£m
MRP (not including PFI)	27	31	37	42	47	50	52
Interest Cost	34	30	34	37	38	40	41
Finance Cost	**61**	**61**	**71**	**79**	**85**	**90**	**94**
Investment Income	19	19	19	19	19	19	19
TOTAL	**42**	**41**	**52**	**60**	**66**	**72**	**75**

2.22 The proportion of finance cost to net revenue stream is a key indicator of direction of travel relative to medium term revenue resources and provides insight into the affordability of finance costs. Full revenue implications of net finance cost are set out in the TMSS (Section 4).

2.23 The Council's finance costs are increasing as a proportion of the net revenue budget, which is expected with an expanding Capital Programme, rising from c.4% in 2024/25 to 6% in 2029/30. This increase is partially contained through schemes enabling delivery of revenue efficiencies or income generation that finance themselves and offset the associated borrowing costs.

2.24 The below schemes are included in the Capital Programme on the basis of covering their own financing costs over the MTFS:

Approved Budget - £69m total spend over MTFS

- £22m – Looked After Children Schemes
- £13m – ASC Extra Care Housing
- £12m – ASC Supported Independent Living – Learning Disabilities Phase 1
- £7m – Sunbury Hub
- £6m – ASC Supported Independent Living – mental health
- £5m – ASC Independent Living / Short Breaks
- £3m – Staines Hub
- £1m – Various smaller schemes

Pipeline – £67m (to be approved after scrutiny of value for money, sustainability and assessment of deliverability)

- £21m – Materials Recovery Facility
- £12m – ASC Supported Independent Living – Learning Disabilities Phase 2
- £9m – ASC nursing / residential care
- £4m – Biodiversity Net Gain
- £4m – Household Loan Scheme

- £4m – net zero 2030 rooftop solar
- £3m – net zero 2030 LEDs
- £3m – SME decarbonisation loan scheme
- £2m – Agile Office Estate Strategy
- £1m – Basingstoke Canal Campsite Improvements
- £1m – Surrey Farms Investment Plan
- £1m – 2050 – Investment in decarbonisation schemes to draw in carbon offset / inset finance
- £1m – Transformation Scheme – Libraries Open Access
- £1m – Various smaller schemes

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Financial Sustainability

2.25 Due to the very long-term nature of capital expenditure and financing, the revenue budget implications of expenditure incurred over the MTFS will extend for up to 50 years into the future. The Section 151 Officer is satisfied that the proposed Capital Programme is prudent, affordable and sustainable, because it remains proportional to the Council's overall revenue budget.

Environmental Sustainability

2.26 Capital expenditure over the next 5-year period includes c.£353m of schemes that will contribute to carbon reduction, action on climate change and enabling a greener future. Of this spend, c.£188m is included for schemes in the approved budget and a further c.£165m for schemes in the pipeline, which are subject to ongoing development, scrutiny and challenge before being approved. The Council will continue to take direct action on environmental sustainability for future generations as part of the Carbon Net Zero targets set for 2030 and 2050.

3. INVESTMENT OVERVIEW

3.1 In addition to service-led capital expenditure, the Council has invested its money for a further three broad purposes:

- To support local public services by setting up, lending to or buying shares in other organisations (service investments);
- To earn investment income (known as commercial investments where this is the main purpose); and
- As a result of surplus cash from its day-to-day activities, for example when income is received in advance of expenditure (known as treasury management investments);

3.2 This investment strategy meets the requirements of the statutory guidance issued by the government in January 2018 and focuses on the first and second of these categories.

3.3 The statutory guidance defines investments as 'all of the financial assets of a local authority as well as other non-financial assets that the organisation holds primarily or partially to generate a profit; for example, investment property portfolios.' The Council interprets this to exclude (a) trade receivables which meet the accounting definition of financial assets but are not investments in the everyday sense of the word and (b) property held partially to generate a profit but primarily for the provision of local public services. This aligns the Council's definition of an investment with that in the 2021 edition of the CIPFA Prudential Code.

Service Investments: Loans and Equity

6 3.4 **Overview:** The Council invests money in its subsidiaries and other organisations to support local public services and stimulate local economic growth. Subsidiaries of this nature include:

- Hendeca Group Ltd – a Local Authority Trading Company (LATCo) wholly owned by the Council for the provision of business services.
- Surrey Choices Ltd – a LATCo, wholly owned by the Council to deliver support options for young people and adults with a range of disabilities.

3.5 **Security:** The main risk when making service loans is that the borrower will be unable to repay the principal lent and/or the interest due. In order to limit this risk and ensure that total exposure to service loans remains prudent, decisions on service loans are made in the context of their value, the stability of the counterparty and an assessment of the risk of default. The current value of service loans is set out as follows:

Table 7 - Loans for service purposes in £ millions

Category of borrower	31/03/2024 actual			2025/26
	Balance owing £m	Loss allowance £m	Net figure in accounts £m	Approved limit £m
Subsidiaries	2	-	2	10

3.6 Accounting standards require the Council to set aside loss allowance for loans, reflecting the likelihood of non-payment. The figures for loans in the Council's Statement of Accounts are shown net of this loss allowance. However, the Council makes every reasonable effort to collect the full sum advanced and has appropriate credit control arrangements in place to recover overdue repayments. In the case of our service loans, these allowances are nil.

3.7 **Risk assessment:** The Council assesses the risk of loss before entering into and whilst holding service loans by reference to their financial position, past experience and other factors. We wholly own our subsidiaries for service purposes and so their financial position is subject to the same rigour and control as that of the Council.

Commercial Investments: Property

3.8 **Overview:** The Council holds investments in local commercial property; office space, leisure and retail, with the intention of supporting Surrey's economy and generating a surplus that will be spent on local public services. The table below shows the value of our investments by main category, including those under construction where the ultimate use is to be determined. The movement represents the net position of additional capital expenditure, depreciation, revaluations and disposals.

Table 8 - Property held for investment purposes in £ millions

Property type	Actual purchase cost £m	31/03/2024 actual	
		Closing value £m	Movement £m
Office	118	71	(47)
Retail	6	3	(3)
Leisure	1	1	-
Total	**125**	**75**	**(50)**

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3.9 **Security:** In accordance with government guidance, the Council considers a property investment to be secure if its accounting valuation is at, or higher than, its purchase cost including taxes and transaction costs.

3.10 The fair value of the Council's investment property portfolio is less than the purchase cost, reflecting the challenging commercial environment in which our investment properties operate, with particular pressure on retail. The Council continues to explore mitigating actions to protect the capital invested, such as alternate uses where appropriate. The Council holds investment properties for long-term rental income, and short-term fluctuation in investment values can be expected.

Commercial Investment – Equity Investments and Loans

3.11 **Overview:** The Council wholly owns Halsey Garton Property Ltd (HGP) and Surrey Property Group (SPG) which has a portfolio of national investment properties used to generate a return to the Council. The Council also wholly owns Halsey Garton Residential Ltd (HGR), which holds a portfolio of Surrey-based residential properties. The financial return from both companies takes the form of interest on the outstanding loan and dividend payments (where possible). The total value of our investment in SPG and HGR as at 31st March 2024 is set out below. The investment in SPG was impaired following a fair value review undertaken during the 2023/24 financial year end.

Table 9 - Equity and Loans to SPG and HGR in £ millions

Category of investment	31/03/2024 actual		
	Balance owing £m	Loss allowance £m	Net figure in accounts £m
Equity shares	97	(66)	31
Loans	242	(3)	239

3.12 Accounting standards require the Council to set aside loss allowance for investments, reflecting an assessment of risk. The figures in the Council's Statement of Accounts are shown net of this loss allowance. However, the Council makes every reasonable effort to collect the full sum advanced and has appropriate credit control arrangements in place to recover overdue repayments.

3.13 The Council also holds shares in the UK Municipal Bonds Agency (UKMBA), whose aim is to reduce the long-term borrowing costs of Local Authorities who join together to issue local authority bonds. The share value (initial cost £0.5m) has been written out of the Council's balance sheet because the UKMBA set out a material uncertainty in its November 2020 accounts that would cast doubt on the company's ability to continue as a going concern. This material uncertainty continues and therefore the Council's position remains unchanged.

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Managing the debt used to finance subsidiary loans

3.14 In previous financial years, the Council has borrowed money to lend on to Halsey Garton Property Ltd, in order to enable investment in property to generate a revenue income for the Council to support service delivery. Alongside the equity shares, these loans are set out in Table 8, above.

3.15 The council amended its MRP policy in 2022/23 to comply with changes that came into force for the 2023/24 financial year, which included a requirement to charge MRP on all subsidiary loans relating to investment properties, to ensure the money is set aside to repay debt without relying on the subsidiary selling assets or negotiating new debt. As such, the council provide MRP on capital loans in full, as it does for any other assets.

3.16 The Council's policy of providing for MRP in full means it is compliant with the latest guidance and there are no changes proposed to the policy for 2025/26 (MRP Policy (Annex G)). The Council's debt in relation to the loans to SPG are serviced over the life of the asset. When the subsidiary repays its loans, any resulting surplus would be recognised as a gain (a capital receipt) at the point of repayment.

Security

3.17 The value of property owned by Halsey Garton Property Ltd at 31st March 2024 was assessed as being £100m lower than cost, representing a 31% reduction, largely due to pressures on the retail environment. The Council has undertaken a fair value assessment of its investment in Halsey Garton Property Ltd and has subsequently impaired its investment in the company (table 8). However the company is holding the assets for long-term rental income and short-term variations in fair value should be expected. Over the long term, we would expect asset values to recover.

Risk Assessment and Liquidity

3.18 **Risk assessment:** The Council assesses the risk of loss before entering into and whilst holding property or subsidiary investments through a thorough analysis of the market and economic conditions using external advisors where necessary. Separately, the Council has a comprehensive risk management strategy to mitigate risks of over-spend or income shortfalls to the base budget position.

3.19 **Liquidity:** Compared with other investment types, property is relatively difficult to sell and convert to cash at short notice and can take a considerable period to sell in certain market conditions. The Council is not reliant on investments in property to maintain its liquidity and manages liquidity through other investments and borrowing. The Council has reserves and contingencies to maintain stability in the event of a period of lower returns from its investment portfolio.

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Loan Commitments and Financial Guarantees

3.20 Although not strictly counted as investments, since no money has exchanged hands yet, loan commitments and financial guarantees carry similar risks to the Council and are included here for completeness.

3.21 We do not currently extend financial guarantees to other organisations, however if we chose to be part of a joint bond issue with UKMBA, we would be liable for defaults of other Local Authorities in proportion to the total amount of the bond. It is highly unlikely that another Local Authority would default and so the risk is theoretical rather than a practical reality.

Proportionality

3.22 The Council's revenue budget includes an element of profit generating investment activity to support services. Table 9 below shows the extent to which the expenditure planned to meet the service delivery objectives and/or place making role of the Council is dependent on achieving the expected net profit from investments over the lifecycle of the MTFS. Investment activity is forecast at around 1.5% of the Council's net revenue budget over the medium-term. Should we fail to achieve the expected net return, the Council would manage the impact on budget through use of contingency in the current financial year and a re-assessment of financial plans for the remainder of the medium-term.

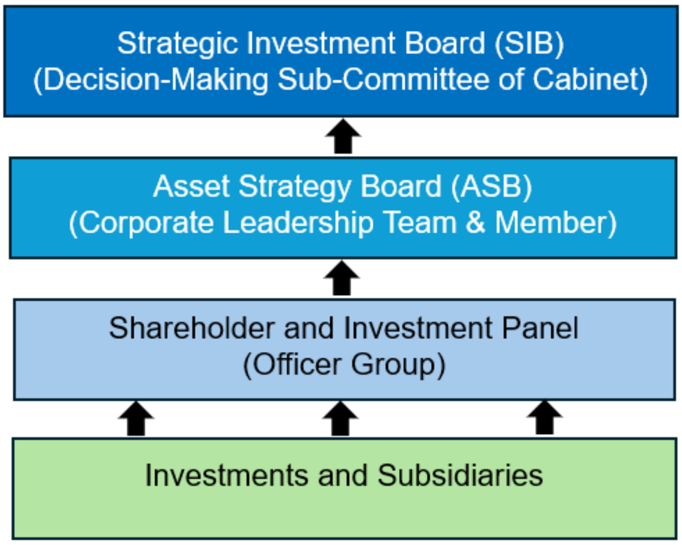
Table 10 - Proportionality of Investments

	2023/24 Actual	2024/25 Forecast	2025/26 Budget	2026/27 Budget	2027/28 Budget	2028/29 Budget	2029/30 Budget
Investment income £m	19	19	19	19	19	19	19
Net revenue budget £m	1,102	1,208	1,264	1,271	1,272	1,274	1,275
Proportion %	**1.7%**	**1.6%**	**1.5%**	**1.5%**	**1.5%**	**1.5%**	**1.5%**

Commercial Governance

3.23 Commercial investments are taken through a rigorous Officer and Member led process to ensure that decisions are taken with an adequate level of scrutiny. The diagram, below, shows the governance groups charged with delivering commercial investments:

Fig 2: Commercial Governance



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3.24 At officer level, oversight is provided by the Shareholder Investment Panel (SHIP) with representation from Finance (Chair), Land & Property and Legal.

3.25 The Asset Strategy Board (ASB) oversee and review the strategic decisions proposed for all Council owned assets taken at Shareholder Investment Panel and Capital Programme Panel, including monitoring delivery against the Asset & Place Strategy (2019-2030) and assessing that the Council is optimising the use of its assets, delivering value for money to residents.

3.26 The Member led Strategic Investment Board (SIB) monitors the Council's investment properties and subsidiary companies to ensure satisfactory performance and effective risk management. SIB provides effective oversight, ensuring alignment with the strategic objectives and values of the Council. SIB safeguards the Council's interests and takes decisions in matters that require the approval of the Council as owner or as a shareholder of a company.

Investment Indicators

3.27 The Council has set the following quantitative indicators to allow elected members and the public to assess the Council's total risk exposure as a result of its investment decisions.

3.28 **Total risk exposure:** The first indicator shows the Council's total exposure to potential investment losses. This includes amounts the Council is contractually committed to lend but have yet to be drawn down and guarantees the Council has issued over third-party loans.

Table 11 - Total investment exposure in £millions

Total investment exposure	31/03/2024 Actual £m	31/03/2025 Forecast £m	31/03/2026 Forecast £m
Treasury management investments	41	50	50
Service investments: loans	2	2	2
Commercial and economic growth investments: property	75	100	104
Commercial investments: loans	239	239	239
Commercial investments: shares	31	31	31
Total investments	**388**	**422**	**426**

3.29 **How investments are funded:** Government guidance is that these indicators should include how investments are funded. Since the Authority does not normally associate particular assets with particular liabilities, this guidance is difficult to comply with. However, the following investments could be described as being funded by borrowing. The remainder of the Authority's investments are funded by usable reserves and income received in advance of expenditure.

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Table 12 - Investments funded by borrowing in £millions

Total investments funded by borrowing	31/03/2024 Actual £m	31/03/2025 Forecast £m	31/03/2026 Forecast £m
Commercial and economic growth investments: property	75	100	104
Commercial investments: loans	239	239	239
Commercial investments: shares	31	31	31
Total investments	**345**	**370**	**374**

3.30 **Rate of return received:** This indicator shows the investment income received less the associated costs, including the cost of borrowing where appropriate, as a proportion of the sum initially invested. Note that due to the complex local government accounting framework, not all recorded gains and losses affect the revenue account in the year they are incurred.

Table 13 - Investment rate of return (net of all costs)

Investments net rate of return	2023/24 Actual	2024/25 Forecast	2025/26 Forecast
Service investments	0.0%	0.0%	0.0%
Commercial investments: property	3.1%	3.1%	3.0%
Commercial investments: shares and loans	4.3%	4.3%	4.3%

4. Treasury Management Strategy Statement 2025/26

Introduction

4.1 Treasury management is the management of the Authority's cash flows, borrowing and investments, and the associated risks. The Authority 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 Authority's prudent financial management.

4.2 Treasury management at Surrey County 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.

4.3 This report fulfils the Council's legal obligation under the Local Government Act 2003 to have regard to the CIPFA Code. A full set of Prudential Indicators is set out in Annex 1 and a number of Treasury limits and indicators are set out below.

4.4 The Council tends to be cash rich in the short-term as revenue income (e.g. Council Tax, Business Rates and Government Grants) is typically received before it is spent, but cash poor in the long-term as capital expenditure is incurred before being financed. Surplus cash is invested until required, while a shortage of cash will be met by borrowing, to avoid excessive credit balances or overdrafts in the bank current account.

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4.5 Managing the cost of the Council's borrowing is at the heart of the Treasury Management Strategy (TMS) and we work proactively with our Treasury Management advisor, Arlingclose on a continual basis, to ensure that our approach represents the best balance between minimising cost and managing the risk of interest rate changes. Regular meetings with Arlingclose coincide with Bank of England Monetary Policy Committee meetings, however our strategy is under constant review throughout the year, and we can call on Arlingclose's expertise whenever required.

4.6 The Treasury Management Strategy is supported by four TMS annexes:

1. Prudential indicators – a Code requirement which supports our approach to borrowing, managing risk and highlighting our capital financing requirement.
2. Detailed external context – a detailed summary from Arlingclose of the current and future economic climate, risks and opportunities along with detailed interest rate forecasts.
3. Investment & Debt Portfolio Position as at 30 November 2024 – to highlight the current range of debt and investments.
4. Glossary of Terms

External Context

4.7 **Economic background:** The impact on the UK from the government's Autumn Budget, slower interest rate cuts, modestly weaker economic growth over the medium term, together with the impact from President-elect Trump's second term in office and uncertainties around US domestic and foreign policy, will be major influences on the Authority's treasury management strategy for 2025/26.

4.8 The Bank of England's (BoE) Monetary Policy Committee (MPC) reduced Bank Rate to 4.75% at its meeting in November 2024, having previously cut by 25bp from the 5.25% peak at the August MPC meeting. At the November meeting, eight Committee members voted for the cut while one member preferred to keep Bank Rate on hold at 5%.

4.9 The November quarterly Monetary Policy Report (MPR) is forecasting Gross Domestic Product (GDP) growth to pick up to around 1.75% (four-quarter GDP) in the early period of the BoE's forecast horizon before falling back. The impact from the Budget pushes GDP higher in 2025 than was expected in the previous MPR, before becoming weaker. Current GDP growth was shown to be 0.5% between April and June 2024, a downward revision from the 0.6% rate previously reported by the Office for National Statistics (ONS).

4.10 Office for National Statistics (ONS) figures reported the annual Consumer Price Index (CPI) inflation rate at 1.7% in September 2024, down from 2.2% in the previous month and lower than the 1.9% expected. Core CPI also declined further than expected to 3.2% against a forecast of 3.4% and the previous month's 3.6%. The outlook for CPI inflation in the November MPR showed it rising above the MPC's 2% target from 2024 into 2025 and reaching around 2.75% by the middle of calendar 2025. This represents a modest near-term increase due to the ongoing impacts from higher interest rates, the

Autumn Budget, and a projected margin of economic slack. Over the medium-term, once these pressures ease, inflation is expected to stabilise around the 2% target.

4.11 The labour market appears to be easing slowly however, but the data still requires treating with some caution. The latest figures reported the unemployment rate fell to 4.0% in the three months to August 2024, while economic inactivity also declined. Pay growth for the same period was reported at 4.9% for regular earnings (excluding bonuses) and 3.8% for total earnings. Looking ahead, the BoE MPR showed the unemployment rate is expected to increase modestly, rising to around 4.5%, the assumed medium-term equilibrium unemployment rate, by the end of the forecast horizon.

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4.12 The US Federal Reserve has also been cutting interest rates, bringing down the Fed Funds Rate by 0.25% at its November 2024 monetary policy meeting to a range of 4.5%-4.75%. Further interest rate cuts are expected, but uncertainties around the potential inflationary impact of incoming President Trump's policies may muddy the waters in terms of the pace and magnitude of further rate reductions. Moreover, the US economy continues to expand at a decent pace, rising at an annual rate of 2.8% in the third quarter of 2024, and inflation remains elevated suggesting that monetary policy may need to remain more restrictive in the coming months than had previously been anticipated.

4.13 Euro zone inflation fell below the European Central Bank (ECB) 2% target in September 2024, the first time in over three years. This allowed the ECB to continue its rate cutting cycle and reduce its three key policy rates by 0.25% in October. Inflation is expected to rise again in the short term, but then fall back towards the 2% target during 2025, with the ECB remaining committed to maintaining rates at levels consistent with bringing inflation to target, but without suggesting a specific path.

4.14 **Credit outlook:** Credit Default Swap (CDS) prices have typically followed a general trend downwards during 2024, reflecting a relatively more stable financial period compared to the previous year. Improved credit conditions in 2024 have also led to greater convergence in CDS prices between ringfenced (retail) and non-ringfenced (investment) banking entities again.

4.15 High interest rates can lead to a deterioration in banks' asset quality through increased loan defaults and volatility in the value of capital investments. Fortunately, the rapid interest rate hikes during this monetary tightening cycle, while putting some strain on households and corporate borrowers, has not caused a rise in defaults, and banks have fared better than expected to date, buoyed by strong capital positions. Low unemployment and robust wage growth have also limited the number of problem loans, all of which are positive in terms of creditworthiness.

4.16 Moreover, while a potential easing of US financial regulations under a Donald Trump Presidency may aid their banks' competitiveness compared to institutions in the UK and other regions, it is unlikely there will be any material impact on the underlying creditworthiness of the institutions on the counterparty list maintained by Arlingclose, the authority's treasury adviser.

4.17 Overall, the institutions on our adviser Arlingclose's counterparty list remain well-capitalised and their counterparty advice on both recommended institutions and maximum duration remain under constant review and will continue to reflect economic conditions and the credit outlook.

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4.18 Interest **rate forecast (November 2024):** The Authority's treasury management adviser Arlingclose forecasts that The Bank of England's Monetary Policy Committee will continue reducing rates during through 2025, taking Bank Rate to around 3.75% by the end of the 2025/26 financial year. The effect from the Autumn Budget on economic growth and inflation has reduced previous expectations in terms of the pace of rate cuts as well as pushing up the rate at the end of the loosening cycle.

4.19 Arlingclose expects long-term gilt yields to remain broadly at current levels on average (amid continued volatility), but to end the forecast period modestly lower compared to now. Yields will continue remain relatively higher than in the past, due to quantitative tightening and significant bond supply. As ever, there will be short-term volatility due to economic and (geo)political uncertainty and events.

4.20 A more detailed economic and interest rate forecast provided by Arlingclose is in the TMS Annex 2.

4.21 For the purpose of setting the budget, it has been assumed that new treasury investments will be made and that new loans will be borrowed at an average rate of 4.25% across the year.

Local Context:

4.22 On 31 March 2024 the Council held £743.2m borrowing (£461m of long-term borrowing and £282.2m short-term borrowing) and £41m of cash investments. By 30th November 2024, this had increased to £970.8m borrowing (£458.1m of long-term borrowing and £512.7m of short-term borrowing), with £68.4m of investments. The increase in borrowing is driven by the capital expenditure incurred by the Council through the year, in line with the approved 2024/25 capital programme.

4.23 The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while balance sheet resources 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.

4.24 Internal borrowing allows the Council to utilise its internal cash balances (i.e. working capital and reserves) which are not required in the short to medium-term in order to reduce risk and keep interest costs low. Forecast changes in these sums are shown in the balance sheet analysis in Table 13 below.

Table 14 - Balance sheet summary and forecast

	31/03/2024 Actual £m	31/03/2025 Estimate £m	31/03/2026 Forecast £m	31/03/2027 Forecast £m	31/03/2028 Forecast £m	31/03/2029 Forecast £m	31/03/2030 Forecast £m
	£m	£m	£m	£m	£m	£m	£m
Capital financing requirement	1,503	1,718	1,919	2,079	2,174	2,187	2,160
Less: other debt liabilities	(88)	(81)	(74)	(67)	(59)	(52)	(44)
Loans CFR	**1,415**	**1,637**	**1,845**	**2,013**	**2,115**	**2,135**	**2,116**
Less: external long term borrowing	(472)	(463)	(455)	(446)	(440)	(435)	(430)
Less: external short term borrowing	(295)	(535)	-	-	-	-	-
Internal borrowing (based on projection of level of reserves, balances and working capital)	(648)	(639)	(639)	(639)	(639)	(639)	(639)
Projected additional external borrowing requirement	**-**	**-**	**751**	**928**	**1,036**	**1,061**	**1,047**

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4.25 The Council has an increasing CFR over the period to 31 March 2030, due to the proposed Capital Programme and approved investment strategy projects. The maximisation of internal borrowing leads to a borrowing requirement above the Council's ability to utilise its internal resources to fund this capital expenditure. It will therefore be required to raise additional external borrowing over the forecast period.

4.26 The Council is currently holding high levels of short-term borrowing due to the recent interest rate environment, which has seen long term interest rates remain at higher rates. While this strategy reduces the interest payable over the medium term it does increase the Council's exposure to interest rate volatility. The Council's strategy will be to increase long term borrowing and reduce this risk as prevailing interest rates reduce.

4.27 The CFR represents the Councils total underlying need to borrow to totally fund the historic and planned capital programme. The Council's use of internal borrowing where available means that the current level of borrowing is below the total CFR. Were the internal resources not available to maintain the current level of internal borrowing then this would need to be met by additional external borrowing above that set out in table 13, further increasing the Council's exposure to interest rate risk. The table above shows that the Council anticipates an ongoing ability to utilise short-term internal resources to continue to reduce the overall borrowing required over the Medium Term Financial Strategy period.

4.28 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. Table 13 shows that the Council expects to comply with this recommendation during 2025/26.

4.29 **Liability benchmark:** To compare the Council's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing. This assumes the same forecasts as table 13 above, but that cash and investment balances are kept to a minimum level of £50m at each year-end to maintain sufficient liquidity but minimise credit risk. This cash and investment balance is the difference between the dotted red line and solid red line in the graph below.

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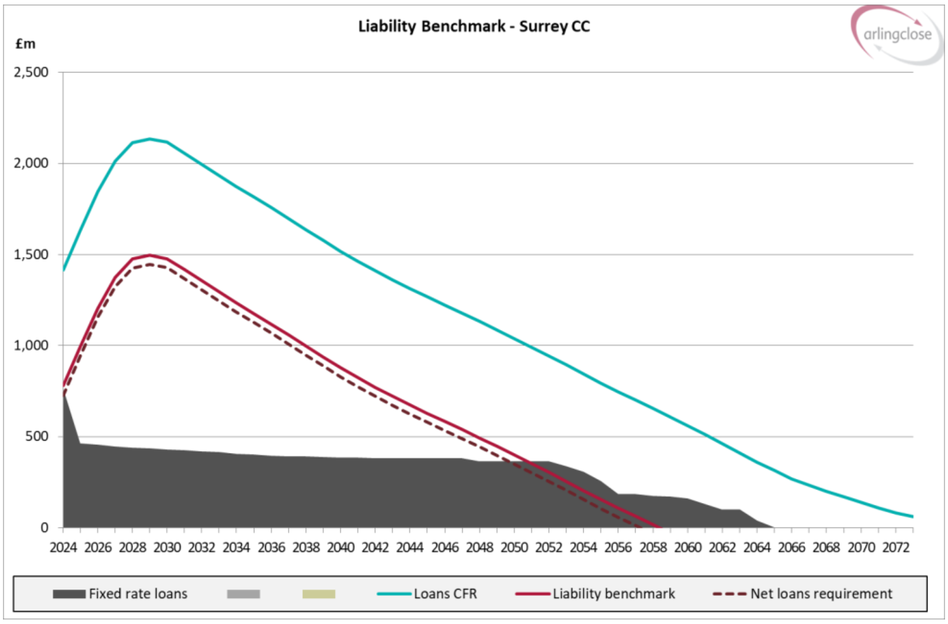
4.30 The liability benchmark is an important tool to help establish whether the Council is likely to be a long-term borrower or long-term investor in the future, and so shape its strategic focus and decision making. The liability benchmark itself represents an estimate of the cumulative amount of external 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 15 – Liability Benchmark

Position at 31 March	2023/24 Actual £m	2024/25 Projected £m	2025/26 ← ---------- £m	2026/27 £m	2027/28 Estimated £m	2028/29 £m	2029/30 ---------- → £m
Loans CFR	1,415	1,637	1,845	2,013	2,115	2,135	2,116
External borrowing	(767)	(463)	(455)	(446)	(440)	(435)	(430)
Internal (over) borrowing	**648**	**1,174**	**1,390**	**1,567**	**1,675**	**1,700**	**1,686**
Balance sheet resources	(689)	(689)	(689)	(689)	(689)	(689)	(689)
Net investments / (new borrowing)	**41**	**(485)**	**(701)**	**(878)**	**(986)**	**(1,011)**	**(997)**
Treasury investments	41	50	50	50	50	50	50
New borrowing	**0**	**535**	**751**	**928**	**1,036**	**1,061**	**1,047**
Net loans requirement	726	948	1,156	1,324	1,426	1,446	1,427
Liquidity allowance	54	50	50	50	50	50	50
Liability benchmark	**780**	**998**	**1,206**	**1,374**	**1,476**	**1,496**	**1,477**

Graph 1: Liability benchmark



4.31 The long-term liability benchmark assumes:

- Capital expenditure funded by borrowing as per the 2025-30 Capital Programme, with no further assumed expenditure factored in beyond the MTFS period;
- Projects in the Capital Programme (Budget and Pipeline) and approved investment strategy spend are included;
- Minimum Revenue Provision (MRP) on new capital expenditure is based on the attached MRP policy;

- Reserves and Balances are based on proposed and approved use over the life of the Medium-Term Financial Strategy (MTFS); and
- The benchmark is based on our assumptions on capital expenditure and the external loans requirement may not ultimately reduce to zero as future capital expenditure is approved.

4.32 Overall, the liability benchmark shows that we are currently borrowing exactly what we need, because the amount of external debt (grey shaded area) matches the liability benchmark (red line). As we progress over the medium term, the gap between total external debt and the liability benchmark grows, meaning that we need to borrow more money to meet our financing requirement. We aim to avoid a scenario where our external debt exceeds our liability benchmark, as it indicates that we are borrowing more than we need – i.e. borrowing to invest, carrying with it an increased risk of investment returns. While the graph shows this happening in 2050, this does assume that there is no capital expenditure funding by borrowing after 2029/30, which is unlikely. 6

4.33 The difference between the CFR (underlying need to borrow – represented by the blue line) and actual external borrowing represents the level of internal borrowing (utilisation of short term reserves and balances). The current strategy to internally borrow continues to support the Council's financial position in the short to medium-term.

4.34 As shown, the Council's current debt portfolio is long dated and there are no significant repayments until the 2050s. An alternate strategy would be to increase our long-term fixed rate borrowing now. The liability benchmark illustrates that if we were to do so, it would be for a reasonably modest amount over a period of up to 20 years (to avoid a significant amount of fixed-rate debt exceeding our liability benchmark).

Borrowing Strategy

4.35 **Objectives:** Authority currently holds £917m of loans, an increase of £150m on the previous year, as part of its strategy for funding previous years' capital programmes. The balance sheet forecast in table 1 shows that the Authority expects to borrow up to £250m in 2025/26. The Authority may also borrow additional sums to pre-fund future years' requirements, providing this does not exceed the authorised limit for borrowing of £1,272m (table 5).

4.36 **Objectives:** The Council's main objective when borrowing money is to strike an appropriate balance between securing low interest costs and achieving certainty of those costs over the period for which funds are required. To achieve this, the key aim is to maximise internal borrowing and use short-term borrowing to manage cashflow shortfalls, striking a balance between cheaper short-term loans and long-term fixed rate loans where the future cost is known but higher. The Council does not borrow to invest for the primary purpose of financial return and therefore retains full access to the Public Works Loans Board.

4.37 **Strategy**: The Council is facing unprecedented financial pressures, principally driven by rising need for services from residents and the increasing costs of providing such services. Given the significant cuts to public expenditure and in particular to local government funding, the Authority's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt

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portfolio. Short-term interest rates are currently higher than in the recent past but are expected to fall in the coming year and it is therefore likely to be more cost effective over the medium-term to either use internal resources, or to borrow short-term loans instead. The risks of this approach will be managed by keeping the Authority's interest rate exposure within the limit set in the treasury management prudential indicators, see below.

4.38 By doing so, the Authority is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of internal / short-term borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years. Arlingclose will assist the Authority with this 'cost of carry' and breakeven analysis. Its output may determine whether the Authority borrows additional sums at long-term fixed rates in 2025/26 with a view to keeping future interest costs low, even if this causes additional cost in the short-term. The Council's current exposure to interest rate risk is high die to the level of short term borrowing. Consideration will be give to converting some of this short term borrowing to long term borrowing, as and when interest rates begin to reduce, in line with market expectations.

4.39 The Authority 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 will investigate 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 Authority intends to avoid this activity in order to retain its access to PWLB loans.

4.40 Alternatively, the Authority 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.

4.41 In addition, the Authority may borrow [further] short-term loans to cover unplanned cash flow shortages

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

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

4.43 The Council has previously raised the majority of its long-term borrowing from the PWLB. For short-term borrowing, the Council has, and will continue, to use other sources of finance, such as loans from other Local Authorities, pension funds and other public bodies as these are often available at more favourable rates. These short-term loans leave the Council exposed to the risk of interest rate rises and are therefore subject to the interest rate exposure limits in the treasury management indicators below.

4.44 Under the Prudential Code, an authority must not borrow to invest primarily for financial return. It is not prudent for local authorities to make any investment or spending decision that will increase the capital financing requirement, and so may lead to new borrowing, unless directly and primarily related to the functions of the authority and where any financial returns are either related to the financial viability of the project in question or otherwise incidental to the primary purpose. Authorities with commercial land and property may invest in maximising its value, including repair, renewal and updating of the properties. This Strategy certifies that the Council's capital spending plans do not include the acquisition of assets primarily for yield. 6

4.45 **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 (PFI)
- sale and leaseback
- similar asset-based finance

All such sources of finance are subject to a robust options appraisal.

4.46 **Municipal Bonds Agency:** UK Municipal Bonds Agency plc was established in 2014 by the Local Government Association as an alternative to the PWLB. It issues bonds on the capital markets and lends the proceeds to local authorities. This is a more complicated source of finance than the PWLB for two reasons: borrowing authorities will be required to provide bond investors with a guarantee to refund their investment in the event that the agency is unable to for any reason; and there will be a lead time of several months between committing to borrow and knowing the interest rate payable. Any decision to borrow from the Agency will therefore be the subject of a separate report. Our current strategy generally favours PWLB borrowing for long term debt due to ease of access to borrowing and certainty of low rates, however this is periodically reviewed with Arlingclose and when a decision for increased long-term borrowing is made all options will be scrutinised.

4.47 **Short-term and variable rate loans**: These loans leave the Authority 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).

4.48 **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 Authority 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.

Borrowing Costs

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4.49 Gross borrowing costs include interest payable and the statutory charge on the general fund for MRP. The gross borrowing costs associated with the 2025/26 to 2029/30 Capital Programme increase from £71m in 2025/26 to £94m by 2029/30.

4.50 Paragraph 1.18 of Annex 1 shows the ratio of gross financing costs against the net revenue stream (the amount funded from council tax, business rates and general government grants). Gross borrowing costs as a proportion of net revenue stream increases over the MTFS period from 5.6% in 2025/26 to 7.3% in 2029/30.

4.51 Net borrowing costs are calculated after offsetting interest and investment income and over the same period, net borrowing costs grow from £52m in 2025/26 to £75m in 2029/30.

4.52 Paragraph 1.19 of Annex 1 shows net borrowing costs against the net revenue stream increasing from 4.1% in 2025/26 to 5.9% in 2029/30.

4.53 Offsetting the increase in borrowing costs; many of the capital schemes are crucial to delivering revenue efficiencies, cost containment or income generation. After accounting for interest, investment and rental income to be generated by pipeline projects, net borrowing costs are projected to be contained within the budget envelope for the MTFS period.

Treasury Investment Strategy

4.54 The Council holds invested funds representing income received in advance of expenditure plus reserves. For the first half of 2024/25, the Council held average balances of £66.8m, compared with £98m for the equivalent period in 2023/24. The average return for the first half of 2024/2025 was 5.14%. Cash balances are expected to reduce during the remainder of 2024/25 and over the MTFS.

4.55 **Objectives:** The CIPFA Code requires the Authority 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 Authority'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. Where balances are expected to be invested for more than one year, the Authority will aim to achieve a total return that is equal or higher than the prevailing rate of inflation, in order to maintain the spending power of the sum invested. The Authority aims to be a responsible investor and will consider environmental, social and governance (ESG) issues when investing.

4.56 **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**.**

4.57 While the Council's investment balances remain low (less than £150m), Money Market Funds and short-term bank deposits will be utilised, with a cash limit per counterparty/fund of £25m. If the economic situation changes, which results in a decision to undertake additional borrowing, resulting in higher cash balances, other investment counterparties may be considered and the counterparty limits set out below would apply.

4.58 **ESG policy**: Environmental, social and governance (ESG) considerations are increasingly a factor in global investors' decision making, but the framework for evaluating investment opportunities is still developing and therefore the Authority's ESG policy does not currently include ESG scoring or other real-time ESG criteria at an individual investment level. When investing in banks and funds, the Authority 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. 6

4.59 **Business models**: Under the IFRS 9 standard, the accounting for certain investments depends on the Authority's "business model" for managing them. The Authority 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.

4.60 **Approved counterparties**: The Authority may invest its surplus funds with any of the counterparty types in table 3 below, subject to the limits shown.

Table 16 - Approved investment counterparties and limits

Credit rating	Banks unsecured	Banks secured	Government*
UK Govt	n/a	n/a	£ Unlimited 50 years
A- and above	£10m 6 months	£20m 13 months	£20m 13 months
None	£1m 6 months	n/a	n/a
Pooled Funds	£25m per fund		

* UK Local Authorities

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

4.61 **Minimum credit rating:** Treasury investments in the sectors marked with an asterisk will only be made with entities whose lowest published long-term credit rating is no lower than A-. 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.

4.62 **UK Government:** Sterling-denominated investments with or explicitly guaranteed by the UK Government, including the Debt Management Account Deposit Facility, treasury bills and gilts. These are deemed to be zero credit risk due to the government's ability to create additional currency and therefore may be made in unlimited amounts for up to 50 years.

4.63 **Local authorities and other government entities:** Loans to, and bonds and bills issued or guaranteed by, other 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.

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4.64 **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.

4.65 **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.

4.66 **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.

4.67 **Money market funds:** 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. Although no sector limit applies to money market funds, the Authority will take care to diversify its liquid investments over a variety of providers to ensure access to cash at all times.

4.68 **Strategic pooled funds:** Bond, equity and property funds, including exchange traded funds, that offer enhanced returns over the longer term but are more volatile in the short term. These allow the Authority 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 can be either withdrawn after a notice period or sold on an exchange, their performance and continued suitability in meeting the Authority's investment objectives will be monitored regularly.

4.69 **Real estate investment trusts:** Shares in companies that invest mainly in real estate and pay the majority of their rental income to investors in a similar manner to pooled property funds. As with property funds, REITs offer enhanced returns over the longer term, but are more volatile especially as the share price reflects changing demand for the shares as well as changes in the value of the underlying properties.

4.70 **Other investments:** This category covers treasury investments not listed above, for example unsecured corporate bonds and unsecured loans to companies and universities. Non-bank companies cannot be bailed-in but can become insolvent placing the Authority's investment at risk.

4.71 **Operational bank accounts:** The Authority may incur operational exposures, for example though 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, and balances will therefore be kept below £1m where practical. 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 Authority maintaining operational continuity. 6

4.72 **Risk assessment and credit ratings**: Credit ratings are obtained and monitored by the Authority'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.

4.73 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.

4.74 **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 Authority'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.

4.75 **Reputational aspects:** The Council is aware that investment 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.

4.76 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, however can be seen in other market measures. In these circumstances, the Authority will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain

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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 Authority's cash balances, then the surplus will be deposited with the UK Government or other local authorities. This will cause investment returns to fall but will protect the principal sum invested.

4.77 **Investment limits**: The Council's revenue reserves available to cover investment losses are forecast to be £78.4m on 31st March 2025. This consists of the Budget Equalisation Reserve, the Revolving Investment and Infrastructure Fund and the Interest Rate Reserve. In order that no more than 30% of available reserves will be put at risk in the case of a single default, the maximum that will be lent to any one organisation (other than the UK Government) will be £20 million. A group of entities under the same ownership will be treated as a single organisation for limit purposes.

Table 17 – Investment Limits

	Cash limit
Any single organisation, except the UK Central Government	£20m each
UK Central Government	Unlimited
Any group of organisations under the same ownership	£20m per group
Any group of pooled funds under the same management (including Money Market Funds)	£25m per manager
Money Market Funds (Total)	Unlimited
Unsecured investments with Building Societies	£10m in total

4.78 **Liquidity management:** The Council uses cash flow forecasting 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 Authority being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Authority's medium-term financial plan and cash flow forecast.

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

Treasury Management Prudential Indicators

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

4.81 **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:

Refinancing rate risk indicator	**Upper limit**	**Lower limit**
Under 12 months	60%	0%
12 months and within 24 months	50%	0%

24 months and within 5 years	50%	0%
5 years and within 10 years	75%	0%
10 years and above	100%	25%

Time periods start on the first day of each financial year. The maturity date of borrowing is the date of the loans are due to be repaid.

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4.82 **Long-term treasury management investments:** The purpose of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments. The prudential limits on the long-term treasury management investments will be:

Price risk indicator	2024/25	2025/26	2026/27	No fixed date
Limit on principal invested beyond year end	£40m	£20m	£10m	£40m

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.

Related Matters

4.83 The CIPFA Code requires the Council to include the following in its treasury management strategy.

4.84 **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).

4.85 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.

4.86 Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria. The current value of any amount due from a derivative counterparty will count against the counterparty credit limit and the relevant foreign country limit.

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

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4.88 **Markets in Financial Instruments Directive**: The Council has opted in 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 Section 151 Officer believes this to be the most appropriate status.

4.89 **Treasury Management Advice:** Surrey County Council has appointed Arlingclose Limited as Treasury management advisers and receives specific advice on investments, debt and capital finance matters.

4.90 **Treasury Management Training**: Member and Officer training needs are assessed regularly as part of the staff appraisal process. Additional training will be provided as and when there is a change in roles and responsibilities. The Council also benefits from the Orbis partnership Centre of Expertise, which provides a robust Treasury team providing day to day treasury management operational activities to Surrey County Council, Brighton & Hove City Council and East Sussex County Council.

Knowledge and Skills

4.91 The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. The Council pays for officers to study towards relevant professional qualifications including CIPFA.

4.92 All officers involved in the treasury and investment management function have access to relevant technical guidance and training to enable them to acquire and maintain the appropriate level of expertise, knowledge and skills to undertake the duties and responsibilities allocated to them. The Council currently employs treasury management advisors through Arlingclose (who commenced a new four-year contract from 1st January 2022) and seeks external legal and property related advice and due diligence as required. The Council’s investment Strategy is supported by guidance from our advisors, Savills. The Council’s Treasury Management and borrowing strategies are supported by guidance from our advisors, Arlingclose. Both are on hand to guide key decisions and provide proactive advice in response to emerging market trends.

4.93 Those charged with governance (Members of the Audit and Governance Committee and the Resources and Performance Select Committee) recognise their individual responsibility to ensure that they have the necessary skills to complete their role effectively. The Section 151 Officer will ensure that elected members tasked with treasury management responsibilities, including those responsible for scrutiny, have access to training relevant to their needs and responsibilities. This will be reviewed regularly, to ensure up to date.

4.94 The Orbis Centre of Expertise for Treasury Management creates a central team of pooled expertise to provide robust services which are resilient to meet the changing service needs of partners.

4.95 Where Council staff do not have the knowledge and skills required, use is made of external advisers and consultants that are specialists in their field. This approach is more cost effective than employing such staff directly and ensures that the Council has access to knowledge and skills commensurate with its risk appetite. 6

Financial Implications

4.96 The budget for investment income and interest payable are set out in the 2025/26 budget and MTFS to 2029/30 and are based on interest rate forecasts (as set out above) and a mix of short-term borrowing and the existing long-term fixed rate debt portfolio. If actual levels of investments and borrowing, or actual interest rates, differ from those forecast, performance against budget will be correspondingly different.

Other options considered

4.97 The CIPFA Code does not prescribe any particular treasury management strategy for Local Authorities to adopt. The Section 151 Officer 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.

Alternative	Impact on income and expenditure	Impact on risk management
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

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Prudential Indicators 2024/25

1.1 The Local Government Act 2003 requires the Council to have regard to the Chartered Institute of Public Finance and Accountancy's Prudential Code for Capital Finance in Local Authorities (the Prudential Code) when determining how much money it can afford to borrow. The objectives of the Prudential Code are to ensure, within a clear framework, that the capital investment plans of Local Authorities are affordable, prudent and sustainable, and that treasury management decisions are taken in accordance with good professional practice. To demonstrate that the Council has fulfilled these objectives, the Prudential Code sets out the following indicators that must be set and monitored each year.

1.2 The Council has adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice.

Estimates of capital expenditure

1.3 The Council's planned capital expenditure and financing is summarised in Table 1. This prudential indicator is a summary of the Council's annual capital expenditure plans, both those agreed previously, and those forming part of this budget cycle.

Table 1 - Actual and estimated capital expenditure	2024/25 Projected £m	2025/26 ← £m	2026/27 ---- Estimated £m	2027/28 ---- £m	2028/29 ---- £m	2029/30 → £m
Capital programme expenditure (incl pipeline)	356	402	355	248	192	197
Approved investment strategy spend	25	4	0	-	-	-
Financed By:						
- Government grants and third party contributions	99	127	116	85	109	150
- Capital Receipts	23	32	26	11	8	8
- Revenue and reserves	6	1	1	1	1	1
Net financing need for the year*	**253**	**246**	**211**	**152**	**73**	**38**

*Capital expenditure to be met by borrowing

The Council's borrowing need (the capital financing requirement)

1.4 Table 2 sets out the Council's estimated capital financing requirement (CFR). The CFR represents capital expenditure funded by external debt and internal borrowing and not by capital receipts, revenue contributions, capital grants or third party contributions at the time of spending. The CFR therefore measures a Council's underlying need to borrow for a capital purpose. Any capital expenditure which has not been funded from locally determined resources will increase the CFR. The CFR reduces by the Minimum Revenue Provision (MRP).

1.5 The MRP is a statutory annual revenue charge which reduces the borrowing need in a similar way to paying principal off a household mortgage.

1.6 The CFR includes any other long-term liabilities, e.g. PFI schemes, finance leases. Whilst these increase the CFR, and therefore the Council's borrowing requirement, these types of scheme include a borrowing facility and so the Council is not required to separately borrow for these schemes and they therefore do not form part of the Council's underlying need to borrow.

1.7 The CFR is increasing over the MTFS period which results in an increase in external debt (after we have maximised internal borrowing) and therefore an increase in the revenue cost of borrowing.

1.8 This is reflected in an increased Operational Boundary and Authorised Limit as shown 6
in Tables 4 and 5. Table 6 - Ratio of financing costs to net revenue stream, shows that the revenue cost of debt is an increasing but remains a relatively low proportion of our overall budget. The impact of funding the Capital Programme is built into the revenue budget and MTFS.

Table 2: Capital Financing Requirement (CFR)	2024/25 Projected £m	2025/26 ← £m	2026/27 ---------- £m	2027/28 Estimated £m	2028/29 ---------- £m	2029/30 → £m
Opening CFR	**1,503**	**1,718**	**1,919**	**2,079**	**2,174**	**2,187**
Movements:						
- Minimum revenue provision	(31)	(38)	(44)	(49)	(54)	(57)
- PFI & finance leases	(7)	(7)	(7)	(7)	(7)	(7)
- Net financing need	253	246	211	152	73	38
Total movement	214	201	160	95	12	(26)
Closing CFR	**1,718**	**1,919**	**2,079**	**2,174**	**2,187**	**2,161**

Gross borrowing and the capital financing requirement

1.9 In order to ensure that over the medium-term borrowing will only be for a capital purpose, the Council should ensure that its debt does not, except in the short-term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for the current and next 2 financial years. This allows some flexibility for early borrowing in advance of need, but ensures that borrowing is not undertaken for revenue purposes. This is a key indicator of prudence.

1.10 Total debt is expected to remain below the CFR during the forecast period.

Table 3: Gross Borrowing	2024/25 Projected £m	2025/26 ← £m	2026/27 ---------- £m	2027/28 Estimated £m	2028/29 ---------- £m	2029/30 → £m
Gross Borrowing	767	998	1,206	1,374	1,476	1,496
CFR	1,718	1,919	2,079	2,174	2,187	2,161

The Council's operational boundary for external debt

1.11 Table 4 sets out the Council's operational boundary, an indicator against which to monitor its external debt position. It is based on the Council's estimate of the most likely (i.e. prudent but not worst case) scenario for external debt. It links directly to the Council's estimates of capital expenditure, the CFR and cash flow requirements and is a key management tool for in-year monitoring.

1.12 Within the operational boundary, figures for borrowing and other long-term liabilities are separately identified. Other long-term liabilities comprise finance lease, PFIs and other liabilities that are not borrowing but form part of the Council's debt position.

1.13 The operational boundary is not a limit and actual borrowing could vary around this boundary for short periods during the year. It should act as an indicator to ensure the authorised limit is not breached. The operational boundary increases over the MTFS period to reflect an increasing underlying need to borrow linked to the Capital Programme. We monitor against the indicator throughout the year.

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Table 4: Operational Boundary	2024/25 Agreed £m	2025/26 ← ---- £m	2026/27 £m	2027/28 Estimated £m	2028/29 £m	2029/30 ---- → £m
Borrowing	1,091	1,404	1,613	1,750	1,790	1,775
PFI & finance leases	88	81	74	67	59	52
Total	**1,179**	**1,485**	**1,687**	**1,816**	**1,849**	**1,827**
Estimated external debt	998	1,206	1,374	1,476	1,496	1,477

The Council's authorised limit for external debt

1.14 Table 5 sets out the Council's authorised limit for external debt. This key prudential indicator represents a control on the maximum level of borrowing. It is a statutory limit determined under section 3(1) of the Local Government Act 2003 and represents a limit beyond which external debt is prohibited. It is the maximum amount of debt that the Council can legally owe.

1.15 The Government retains an option to control either the total of all Councils' plans, or those of a specific Council, although this power has not yet been exercised since the introduction of the Prudential Code.

1.16 The Authorised limit provides headroom over and above the operational boundary for unusual cash movements and potential additional borrowing to meet the ambitions of the Council in respect of its investment strategy.

1.17 As with the operational boundary, the limit separately identifies borrowing from other long-term liabilities such as finance leases and PFIs. The authorised limit increases over the MTFS period to reflect an increasing underlying need to borrow linked to the Capital Programme.

Table 5: Authorised Limit	2024/25 Agreed £m	2025/26 ← ---- £m	2026/27 £m	2027/28 Estimated £m	2028/29 £m	2029/30 ---- → £m
Borrowing	1,183	1,602	1,853	2,023	2,084	2,074
PFI & finance leases	88	81	74	67	59	52
Total	**1,272**	**1,683**	**1,926**	**2,090**	**2,143**	**2,125**
Estimated external debt	998	1,206	1,374	1,476	1,496	1,477

Estimated ratio of gross financing costs to net revenue stream

1.18 This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet financing costs.

	2023/24 Actual	2024/25 Forecast	2025/26 Budget	2026/27 Budget	2027/28 Budget	2028/29 Budget	2029/30 Budget
Proportion of gross financing costs to net revenue budget	5.5%	5.0%	5.6%	6.2%	6.7%	7.1%	7.4%

Estimated ratio of net financing costs to net revenue stream

1.19 This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet net financing costs (net of investment income).

	2023/24 Actual	2024/25 Forecast	2025/26 Budget	2026/27 Budget	2027/28 Budget	2028/29 Budget	2029/30 Budget
Proportion of net financing costs to net revenue budget	3.8%	3.4%	4.1%	4.7%	5.2%	5.6%	5.9%

1.20 The revenue implications of potential, yet to be identified, investment opportunities that meet the Council's long-term capital strategy criteria, will be funded from the investment returns of such investments. If there is a delay in the realisation of sufficient returns, then costs will be funded from the Council's Revolving Infrastructure & Investment Fund reserve. 6

Net income from commercial and service investments to net revenue stream

1.21 This is an indicator of affordability and highlights the net financial impact on the authority of its entire non-treasury investment income.

	2023/24 Actual	2024/25 Forecast	2025/26 Budget	2026/27 Budget	2027/28 Budget	2028/29 Budget	2029/30 Budget
Total net income service and commercial investments	19	19	19	19	19	19	19
Proportion of net revenue budget	1.7%	1.6%	1.5%	1.5%	1.5%	1.5%	1.5%

TMS Annex 2 - Arlingclose Economic & Interest Rate Forecast – November 2024

Underlying assumptions

2.1 As expected, the Bank of England Monetary Policy Committee (MPC) cut Bank Rate to 4.75% in November in an 8-1 vote. However, the outlook for monetary policy has changed following the new government’s fiscal plans, as delivered in the recent
6 Budget.

2.2 The Budget contained measures that will boost demand, in a constrained supply environment, while pushing up direct costs for employers. The short to medium-term inflationary effects of the Budget require a change to our Interest Rate Forecast.

2.3 UK GDP recovered well in H1 2024 from technical recession, but underlying growth appears relatively subdued. However, the Budget will significantly boost government spending over the short-term, with few offsetting measures to subdue household demand, so GDP growth is likely to rise relatively steeply.

2.4 Private sector wage growth has eased to 4.8% yet remains high, while services inflation continues to hold above pre-pandemic levels. The increase in employers’ NICs, minimum and public sector wage levels could have wide ranging impacts on private sector employment demand and costs, but the near-term impact will likely be inflationary as these additional costs get passed to consumers.

2.5 CPI inflation was below the 2% target in September but will rise a little by year-end as energy price declines from the previous year fall out of the annual comparison. The Bank of England (BoE) estimates the Budget impact will see the CPI rate at 2.7% by year end 2025 and remain over target in 2026, as opposed to the prior projection of inflation easing back to and then below target by this point.

2.6 The MPC re-emphasised the gradual move to easing monetary policy, and we now believe the Budget measures have both reduced the pace of Bank Rate cuts and increased the low for this loosening cycle (although downside risks remain in the medium term).

2.7 The increase in borrowing, rise in inflation and shallower path for Bank Rate projected by the Office for Budget Responsibility (OBR) raised gilt yields. The material change in rate expectations means that yields will be generally higher in the post-Budget world.

2.8 US government yields have risen following Donald Trump’s and Republican victories in the US elections. Trump has run on a platform of policies that appear inflationary, calling into question the extent of policy loosening required from the Federal Reserve (which was already uncertain given continued solid US growth data). Higher US yields could also support higher UK yields.

Forecast

2.9 The Bank Rate was cut to 4.75% in November 2024.

2.10 The MPC will continue to lower Bank Rate to reduce the restrictiveness of monetary policy, but more slowly and to a higher level. We see another rate cut in February 2025, followed by one cut per quarter, in line with Monetary Policy Report publication, to a low of 3.75%.

2.11 Long-term gilt yields have risen to reflect both UK and US economic, monetary and fiscal policy expectations, and increases in bond supply. Volatility is likely to remain elevated as the market digests incoming data for clues around the impact of policy changes.

2.12 This uncertainty may also necessitate more frequent changes to our forecast than has been the case recently.

2.13 Upside risks to inflation over the next 12 months could limit the extent of monetary easing, but we see the risks as broadly balanced over the medium term.

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	Current	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27	Jun-27	Sep-27
Official Bank Rate													
Upside risk	0.00	0.00	0.25	0.50	0.50	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75
Central Case	4.75	4.75	4.50	4.25	4.00	3.75	3.75	3.75	3.75	3.75	3.75	3.75	3.75
Downside risk	0.00	0.00	-0.25	-0.25	-0.50	-0.50	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75
3-month money market rate													
Upside risk	0.00	0.00	0.25	0.50	0.50	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75
Central Case	4.95	4.80	4.60	4.35	4.10	3.90	3.85	3.85	3.85	3.85	3.85	3.85	3.85
Downside risk	0.00	0.00	-0.25	-0.25	-0.50	-0.50	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75	-0.75
5yr gilt yield													
Upside risk	0.00	0.60	0.70	0.80	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Central Case	4.30	4.20	4.10	4.05	3.95	3.90	3.90	3.90	3.95	4.00	4.05	4.05	4.05
Downside risk	0.00	-0.40	-0.50	-0.60	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65
10yr gilt yield													
Upside risk	0.00	0.60	0.70	0.80	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Central Case	4.41	4.40	4.35	4.35	4.35	4.30	4.30	4.30	4.35	4.35	4.35	4.35	4.35
Downside risk	0.00	-0.40	-0.50	-0.60	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65
20yr gilt yield													
Upside risk	0.00	0.60	0.70	0.80	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Central Case	4.84	4.80	4.75	4.70	4.65	4.65	4.65	4.65	4.65	4.65	4.65	4.65	4.65
Downside risk	0.00	-0.40	-0.50	-0.60	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65
50yr gilt yield													
Upside risk	0.00	0.60	0.70	0.80	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Central Case	4.35	4.50	4.45	4.40	4.35	4.35	4.35	4.35	4.35	4.35	4.35	4.35	4.35
Downside risk	0.00	-0.40	-0.50	-0.60	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65	-0.65

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%

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TMS Annex 3 - Investment & Debt Portfolio Position as at 30 November 2023

	Actual Portfolio £m	Interest Rate %
External borrowing:		
Public Works Loan Board	458	3.68
Market	10	5.00
Local Authorities (Incl. Surrey Police)	513	5.05
Other	12	0.00
Total external borrowing	**993**	
Other long-term liabilities:		
Private Finance Initiative	77	
Total other long-term liabilities	**77**	
Total gross external debt	**1,070**	
Treasury investments:		
Money Market Funds	68	4.79
Total treasury investments	**68**	
Net debt	**1,002**	

TMS Annex 4 - Glossary of Terms

CFR – Capital Financing Requirement

CIPFA – Chartered Institute of Public Finance Accountancy

CPI – Consumer Price Index

DLUHC – Department for Levelling Up, Housing and Communities

DMO – Debt Management Office

ECB – European Central Bank

GDP – Gross Domestic Product

LB – Liability Benchmark

MMF – Money Market Fund

MPC – Monetary Policy Committee

MRP – Minimum Revenue Provision

PWLB – Public Works Loan Board

TMSS – Treasury Management Strategy Statement

Annual Minimum Revenue Provision (MRP) Policy Statement 2025/26

1. When the Council finances capital expenditure by debt (borrowing), it must put aside resources to repay that debt in future years. The amount charged to the revenue budget for the repayment of debt is known as Minimum Revenue Provision (MRP). The Council is required by statute to make a prudent provision for the repayment of its debt. It is also required to 'have regard' to guidance on how to calculate this provision, issued by the Ministry of Housing, Communities and Local Government, most recently in 2024. 6

2. The broad aim of the guidance is to ensure that capital expenditure is financed over a period that is reasonably commensurate with that over which the capital expenditure provides benefits.

3. In developing this policy statement, the Council is satisfied that the guidelines for their annual amount of MRP will result in it making a prudent provision.

4. MRP is calculated by reference to the capital financing requirement (CFR) which is the total amount of past capital expenditure that has yet to be permanently financed, noting that debt must be repaid and therefore can only be a temporary form of funding. The CFR is calculated from the Authority's balance sheet in accordance with the Chartered Institute of Public Finance and Accountancy's Prudential Code for Capital Expenditure in Local Authorities, 2021 edition.

5. Where capital expenditure was incurred before 1 April 2008, the guidance suggests writing down the remaining Capital Financing Requirement by providing MRP of 4% per annum. The Council agreed in 2016/17 to write this amount off over the next 50 years, resulting in the whole balance being provided for over a finite period and far sooner than under the 4% reducing balance method.

6. As suggested in the guidance, for capital expenditure incurred on or after 1 April 2008 and funded through borrowing, the Council will calculate MRP by charging expenditure over the expected useful life of the relevant assets, on an annuity basis. MRP will be first charged in the year following the date that an asset becomes operational.

7. For the following types of capital expenditure, the Council has determined that an alternative methodology for determining the annual MRP charge should be adopted:

   - For assets acquired by finance leases or the Private Finance Initiative, MRP will be determined as being equal to the element of the rent or charge that goes to write down the balance sheet liability, or over the life of the asset.

   - For capital expenditure on loans to third parties which were made primarily for financial return rather than direct service purposes, MRP will be charged in accordance with the policy for the assets funded by the loan, including where appropriate, delaying MRP until the year after the assets become operational. This MRP charge will be reduced by the value any repayments of loan principal received during in the year, with the capital receipts so arising applied to finance the expenditure instead.

   - For capital expenditure on loans to third parties which were made primarily for service purposes, the Authority will make nil MRP except as detailed below for expected credit losses. Instead, the Authority will apply the capital receipts arising from the repayments of the loan principal to finance the expenditure in the year they are received.

   - For capital loans made on or after 7th May 2024 where an expected credit loss is recognised during the year, the MRP charge in respect of the loan will be no lower

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than the loss recognised. Where expected credit losses are reversed, for example on the eventual repayment of the loan, this will be treated as an overpayment.

- For capital loans made before 7th May 2024 and for loans where expected credit losses are not applicable, where a shortfall in capital receipts is anticipated, MRP will be charged to cover that shortfall over the remaining life of the assets funded by the loan.
- MRP for investment property purchases is based on an estimated useful life of 50 years, on an annuity basis, in order to appropriately match MRP to the period of time that the assets are expected to generate a benefit to the Council. This is in recognition that these assets are held for income generation purposes and that the Council holds a saleable asset, the capital receipt from which will be used to repay any outstanding debt when sold.
- The Council will determine MRP on equity investments based on a 20 year life. However, for equity investments in asset backed companies, a 50 year life will be assumed to match the Council's policy for investment assets.

8. The Council reserves the right to determine alternative MRP approaches in particular cases, in the interests of making prudent provision, where this is material, taking account of local circumstances, including specific project timetables and revenue-earning profiles.

9. Capital expenditure incurred during 2025/26 will not be subject to a MRP charge until 2026/27 or later.

10. Capital receipts - proceeds from the sale of capital assets are classed as capital receipts and are typically used to finance new capital expenditure. Where the Authority decides instead to use capital receipts to repay debt and hence reduce the CFR, the calculation of MRP will be adjusted as follows:

- Capital receipts arising on the repayment of principal on capital loans to third parties will be used to lower the MRP charge in respect of the same loans in the year of receipt, if any.
- Capital receipts arising on the repayment of principal on finance lease receivables will be used to lower the MRP charge in respect of the acquisition of the asset subject to the lease in the year of receipt, if any.
- Capital receipts arising from other assets which form an identified part of the Authority's MRP calculations will be used to reduce the MRP charge in respect of the same assets over their remaining useful lives, starting in the year after the receipt is applied.
- Any other capital receipts applied to repay debt will be used to reduce MRP in 10 equal instalments starting in the year after receipt is applied.

11. Each year a new MRP statement will be presented.