AGENDA ITEM 12

REPORT TO AUDIT AND GOVERNANCE COMMITTEE

30 NOVEMBER 2026

REPORT OF CHIEF FINANCIAL OFFICER

TREASURY MANAGEMENT STRATEGY MID YEAR REPORT 2026/27

SUMMARY

This report informs Members of the performance against the treasury management and prudential indicators set in the 2026-27 Treasury Management & Capital Strategy reports approved by Council in February 2026.

Introduction

The Authority has adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice (the CIPFA Code) which requires the Authority to approve treasury management semi-annual and annual reports.

The Authority's Treasury Management Strategy for 2026/27 was approved by Council on 18th February 2026. 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 risk remains central to the Authority's treasury management strategy.

External Context

Arlingclose, Stockton's Treasury Management advisors, have provided us with the following commentary on the external environment.

Economic background: The key story remained the conflict in the Middle East and its impact on global energy prices and inflation. Although energy prices had shown signs of moderating towards the end of (calendar) Q2, the continuing conflict pushed oil and gas up sharply once again in Q3. Around mid-September, Brent oil and UK gas prices were over 30% and 70% higher respectively compared to the period preceding the Bank of England's (BoE) July Monetary Policy Report (MPR).

Given the inflationary impact of the previous energy shock from the Russia/Ukraine war, central bank policymakers remained alert to higher energy prices feeding into wider price and wage-setting behaviour ('second-round effects'). In the UK, higher fuel and energy prices were evident in headline inflation, but there was limited evidence of material second-round effects. At the same time, underlying wage pressures continued to moderate, and the labour market remained relatively loose.

The BoE's Monetary Policy Committee (MPC) maintained Bank Rate at 3.75% throughout the period. In April the MPC voted by 8-1 to leave rates unchanged, with one member wanting a 0.25% increase. The voting subsequently became more hawkish, moving to 7-2

in June and 6-3 in both July and September, with all dissenters preferring to increase Bank Rate to 4.00%. The change in voting patterns reflected increasing policymaker concern over the persistence of the energy shock and the risk that higher headline inflation could become embedded in domestic prices and wages.

At the September MPC meeting, the Committee judged the inflation risks were further to the upside compared to its July MPR. Energy prices had risen again and borrowing costs were materially higher than before the US/Iran conflict. Despite expecting inflation would rise further in the near-term, most members believed that a soft labour market, spare capacity and restrictive monetary conditions would reduce inflation over time. Moreover, the data showed there was still little evidence of material second-round effects, although the MPC emphasised that the risk of these effects would increase the longer elevated and volatile energy prices persisted.

UK headline consumer price inflation (CPI) initially declined, suggesting the initial energy shock was not spreading into a wider range of goods and services. However, later in the period inflation picked up again, with CPI rising from 2.6% in June to 3.1% in August due largely to higher transport costs. Core CPI was 2.6% in July and August, suggesting the divergence between that and headline inflation was due to energy rather than a broad increase in underlying inflation.

UK economic activity was somewhat stronger than initially anticipated over the period. GDP expanded by 0.6% in the first quarter of the calendar year and 0.5% in the second quarter, slightly stronger than the initial estimate of 0.4%. Monthly activity was more volatile, with a contraction of -0.1% in April, followed by gains of 0%, 0.3% and 0.4% in May, June and July respectively.

Labour market data continued to show softening employment conditions. The unemployment rate fell to 4.9% in April and remained at that level to July, against expectations it would tick up. Job vacancies also continued to decline, to 702,000 in the three months to July. Earnings growth moderated, with regular earnings at 3.5% in the three months to July and total earnings at 3.9%, suggesting weaker labour demand was continuing to restrain domestic wage pressures.

Arlingclose, the authority's treasury adviser, expects Bank Rate will stay at 3.75%. However, higher energy prices due to the ongoing conflict(s) and the government's Budget have increased the near-term upside risks. Moreover, stronger inflation projections, which accompanied the September MPC decision, shifted market expectations for Bank Rate higher. In addition, despite little evidence of second-round effects to date, the changing tone of the MPC minutes suggests it may not need something seismic to tip the Committee to increase Bank Rate.

Financial markets: After the sharp deterioration early in the period, financial market sentiment improved somewhat as there were ongoing hopes that the US/Iran war would be resolved. However, towards the end of the period, signs of any potential resolution appeared premature and oil prices rose alongside inflation and bond yields while equity market volatility increased as investors weighed conflict-related as well as AI-related concerns.

Bond yields in both the US and UK increased markedly over the period, with the gap between gilts and US Treasuries tightening towards the end of the period. While term premia are still embedded in gilt yields given the relatively uncertain fiscal outlook, a more hawkish Fed alongside persistent US inflation and fiscal concerns have pushed the yields on US Treasuries to their highest levels in years.

Over the period, the 10-year UK benchmark gilt yield started at 4.86% and ended at a high of 5.43%. The 20-year gilt yield starting at 5.45% and finished at 5.93%, another high for the period. The Sterling Overnight Rate (SONIA) averaged 3.73% over the period to 30th September.

Credit review: Arlingclose maintained its advised recommended maximum unsecured duration limit on the majority of the banks on its counterparty list at 6 months. The other banks remain on 100 days.

During the period, Fitch upgraded numerous banks due to a rating methodology change, as well as the reference obligations used for Issuer Default Ratings and introduced more differentiated notching between deposits, senior preferred, senior unsecured and senior non-preferred debt ratings.

Later in the period, Moody's changed the outlook on HSBC to Positive from Stable, while also affirming its long-term deposit rating. This follows a similar action from S&P on HSBC's outlook a few months prior to this.

Financial market volatility is expected to remain a feature, at least in the near term and, credit default swap levels will continue to be monitored for signs of ongoing credit stress. As ever, the institutions and durations on the Authority's counterparty list recommended by Arlingclose remain under constant review.

Local Context

On 31st March 2026, the Authority had net borrowing of £138.32m arising from its revenue and capital income and expenditure. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. These factors are summarised in Table 1 below.

Table 1: Balance Sheet Summary

	31.3.26 Actual £m
General Fund CFR	202.27
Less: Other debt liabilities	-9.14
Borrowing CFR	**193.13**
Less: Usable reserves	-88.63
Add: Working capital	33.82
Net Borrowing / (Investments)	**138.32**

The treasury management position at 30th September 2026 and the change over the six-month period is shown in Table 2 below.

Table 2: Treasury Management Summary

	31.3.26 Balance £m	Movement £m	30.9.26 Balance £m
Long-term borrowing	93.63	-6.08	87.55
Short-term borrowing	75.35	-5.31	70.04
Total borrowing	**168.98**	**-11.39**	**157.59**
Long-term investments	-13.28	0.22	-13.06
Short-term investments	0.00	0.00	0.00
Cash and cash equivalents	-17.38	-5.59	-22.97
Total investments	**-30.66**	**-5.37**	**-36.03**
Net Borrowing	**138.32**	**-16.76**	**121.56**

Borrowing Strategy and Activity

As outlined in the treasury strategy, the Authority's chief objective when borrowing has been to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required, with flexibility to renegotiate loans should the Authority's long-term plans change being a secondary objective. The Authority's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio.

Gilt yields have been volatile, reflecting expectations of tighter monetary policy compared to previous expectations due to the war. Long-term gilt yields are very high, with investors lacking confidence in UK fiscal plans.

The PWLB certainty rate for 10-year maturity loans was 5.62% at the beginning of the period and 6.17% at the end. Rates for 20-year maturity loans moved from 6.13% to 6.61% during the period, and 50-year maturity loans from 6.01% to 6.37%. The cost of short-term borrowing from other local authorities has been above Bank Rate during the period at 3.8% to 5.5%: costs have risen throughout the period. This is primarily due to many local authorities avoiding more expensive long-term rates and relying more heavily on the short-term market. Low cash levels and the non-receipt of SEND grants are also likely to have contributed to a high borrowing demand.

CIPFA's 2021 Prudential Code is clear that local authorities must not borrow to invest primarily for financial return and that it is not prudent for local authorities to make any investment or spending decision that will increase the capital financing requirement and so may lead to new borrowing, unless directly and primarily related to the functions of the Authority. PWLB loans are no longer available to local authorities planning to buy investment assets primarily for yield unless these loans are for refinancing purposes. The Authority has no new plans to borrow to invest primarily for financial return.

At 30th September 2026 the Authority held £157.59m of loans, a decrease of £11.39m since 31st March 2026. Details of outstanding loans on this date are summarised in Table 3 below.

Table 3: Borrowing Position

	31.3.26 Balance £m	Q2 Net Movement £m	30.9.26 Balance £m	30.9.26 Weighted Average Rate %	30.9.26 Weighted Average Maturity (years)
Public Works Loan Board	111.17	-26.39	84.78	3.59	8.94
Banks (LOBO)	16.00	-5.00	11.00	4.80	17.00
Local Authorities	41.81	20.00	61.81	4.34	1.70
Others (fixed-term)	0.00	0.00	0.00	2.50	0.73
Total borrowing	**168.98**	**-11.39**	**157.59**	**3.94**	**6.66**

The Authority's short-term borrowing increased by £20 million during the period as part of a deliberate treasury management strategy to replace maturing long-term debt with short-term borrowing whilst interest rates remain relatively high and borrowing options continue to be monitored. Notwithstanding this, total external borrowing decreased by £11.39 million over the six-month period. This reduction was driven by favourable in-year cash flows, resulting in a lower borrowing requirement at 30 September.

LOBO loans: At the 30th September the Authority held £11m of LOBO (Lender's Option Borrower's Option) loans where the lender has the option to propose an increase in the interest rate as set dates, following which the Authority has the option to either accept the new rate or to repay the loan at no additional cost. No banks exercised their option during the first six months of the year but a £5m loan did mature during this period.

Over the medium term it is estimated the authority, based on the current capital programme and the fact the authority has internally borrowed over the previous years will be required to undertake significant borrowing. In the higher rate environment that we are currently operating in this will mean higher costs of borrowing. Future borrowing requirements and financial requirements are currently being analysed, and information will be provided as part of future MTFP and Treasury reports.

Treasury Investment Activity

CIPFA revised TM Code defines treasury management investments as those which arise from the Authority's cash flows or treasury risk management activity that ultimately represents balances which need to be invested until the cash is required for use in the course of business.

The Authority holds invested funds, representing income received in advance of expenditure plus balances and reserves held. During the year, the Authority's investment balances fluctuated due to timing differences between income and expenditure. The investment position at the end of September is shown in table 4 below.

Table 4: Treasury Investment Position

	31.3.26 Balance £m	Net Movement £m	30.9.26 Balance £m
Banks & building societies (unsecured)	-0.06	0.01	-0.05
Government (incl. local authorities)	0.00	-3.60	-3.60
Property Fund	-13.28	0.22	-13.06
Shares / Cash	0.00	-0.01	-0.02
Money Market Funds	-17.32	-1.98	-19.30
Total investments	**-30.66**	**-5.36**	**-36.03**

Both the CIPFA Code and government guidance require the Authority to invest its funds prudently, and to have regard to the security and liquidity of its treasury investments before seeking the optimum rate of return, or yield. The 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.

The Authority expects to be a long-term borrower and new treasury investments are therefore primarily made to manage day-to-day cash flows using short-term low risk instruments. The existing portfolio of strategic pooled funds will be maintained to diversify risk into different asset classes and boost investment income.

Bank Rate remained at 3.75% during the period. DMADF deposit rates were broadly stable between April and September 2026, reflecting a Bank Rate of 3.75%, with investment yields typically around 3.7% to 3.8% depending on maturity and money market rates between 3.7% and 4.9%.

The progression of risk and return metrics are shown in the extracts from Arlingclose's quarterly investment benchmarking in Table 5 below.

Table 5: Investment Benchmarking – Treasury investments managed in-house

	Credit Score	Credit Rating	Bail-in Exposure	WAM* (days)	Rate of Return %
31.03.2026	4.69	A+	100%	2	4.16%
30.06.2026	4.53	A+	85%	2	3.34%
30.09.2026	4.45	AA-	84%	1	3.50%
Similar LAs	4.64	A+	78%	73	4.51%
All LAs	4.58	A+	67%	10	4.16%

*Weighted average maturity

Externally Managed Pooled Funds: £13.06m of the Authority's investments are held in an externally managed strategic pooled property fund where short-term security and liquidity

are lesser considerations, and the objectives instead are regular revenue income and long-term price stability.

UK commercial property experienced some weakness in capital values over the period as higher gilt yields and interest rates continued to weigh on valuations. However, rental income remained relatively resilient. Property capital values had already undergone a significant adjustment following the rise in interest rates during 2022 and have recovered only modestly since, meaning recent falls have generally been relatively limited.

Income distributions from strategic pooled funds generally remained resilient over the period, despite the volatility in underlying asset prices.

The fund generated a return of £0.620m (4.13%) during 2025/26 and has generated £0.311m (4.20%) in dividend payments for the first six months of the year. This income is being used to support the medium-term financial plan.

Because the Authority's externally managed funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Authority's investment objectives are regularly reviewed. Strategic fund investments are made in the knowledge that capital values will move both up and down on months, quarters and even years; but with the confidence that over a three- to five-year period total returns will exceed cash interest rates.

Statutory override: Further to consultations in April 2023 and December 2024 MHCLG wrote to finance directors in England in February 2025 regarding the statutory override on accounting for gains and losses in pooled investment funds. The statutory override will be extended up until the 1st April 2029 for investments already in place before 1st April 2024. The override will not apply to any new investments taken out on or after 1st April 2024.

The Authority has set up a reserve of £1.000m to mitigate the impact of the statutory override not being extended and unrealised losses on pooled investment funds are required to be recognised.

CIPFA Consultation: During the period CIPFA consulted on potential changes to their Prudential and Treasury Management Codes and the associated guidance notes. If implemented there may be substantial changes to reporting requirements and indicators in the future.

Non-Treasury Investments

The definition of investments in the Treasury Management Code now covers all the financial assets of the Authority as well as other non-financial assets which the Authority holds primarily for financial return. Investments that do not meet the definition of treasury management investments (i.e. management of surplus cash) are categorised as either for service purposes (made explicitly to further service objectives) or for commercial purposes (made primarily for financial return).

Investment Guidance issued by the Ministry of Housing, Communities and Local Government (MHCLG) and Welsh Government also includes within the definition of investments all such assets held partially or wholly for financial return.

The Council also held £15.109m of such investments in;

- directly owned property £14.890m
- loans to local businesses £0.015m
- other £0.204m

These investments generated £0.917m of investment income for the Council after taking account of direct costs in 2025/26, representing a rate of return of 6.16%.

Compliance

The Chief Financial Officer reports that the majority of the treasury management activities undertaken during the year complied fully with the CIPFA Code of Practice and the Council's approved Treasury Management Strategy. Compliance with specific investment limits is demonstrated in the tables below.

Compliance with the authorised limit and operational boundary for external debt is demonstrated in table 6 below.

Table 6: Debt and the Authorised Limit and Operational Boundary

	Maximum in Year £m	30.9.26 Actual £m	2026/27 Operational Boundary £m	2026/27 Authorised Limit £m	Complied? Yes/No
Borrowing	173.11	157.59	216.00	231.00	Yes
PFI and Finance Leases	5.06	5.06	5.06	5.06	Yes
Total debt	**178.17**	**162.65**	**221.06**	**236.06**	

Since the operational boundary is a management tool for in-year monitoring it is not significant if the operational boundary is breached on occasions due to variations in cash flow, and this is not counted as a compliance failure.

Compliance with specific investment limits is demonstrated in table 7 below;

Table 7: Investment Limits

Sector	Counterparty limit	Sector limit	Maximum	30.9.26 Actual	Complied? Yes/No
The UK Government	Unlimited	n/a	£30,800,000	£3,600,000	Yes
Local authorities & other government entities	£5,000,000	Unlimited	£0	£0	Yes
Secured investments	£5,000,000	Unlimited	£0	£0	Yes
Banks (unsecured)	£2,500,000	Unlimited	£1,193,000	£50,000	Yes

Building societies (unsecured)	£2,500,000	£5,000,000	£0	£0	Yes
Registered providers (unsecured)	£2,500,000	£12,500,000	£0	£0	Yes
Money market funds	£5,000,000	Unlimited	£25,000,000	£19,300,000	Yes
Strategic pooled funds	£15,000,000	£25,000,000	£13,058,000	£13,058,000	Yes
Real estate investment trusts	£5,000,000	£12,500,000	£0	£0	Yes
Other investments	£2,500,000	£5,000,000	£0	£0	Yes

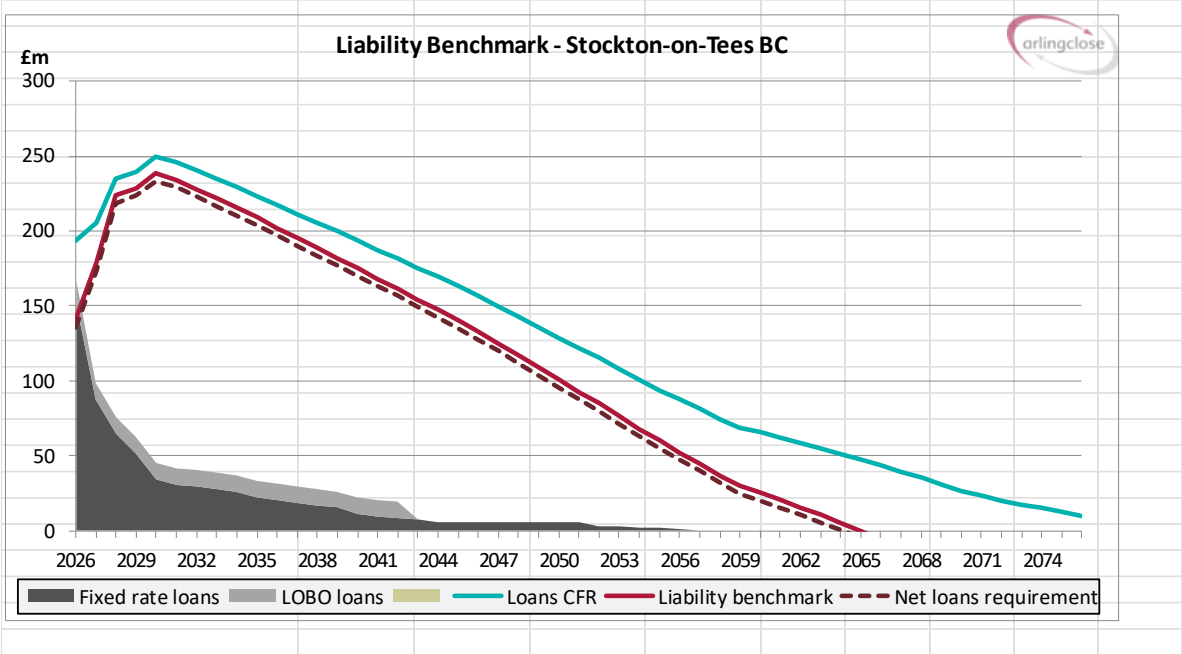
Treasury Management Prudential Indicators

As required by the 2021 CIPFA Treasury Management Code, the Authority monitors and measures the following treasury management indicators.

Liability Benchmark: This indicator compares the Authority's actual existing borrowing against a liability benchmark that has been calculated to show the lowest risk level of borrowing. 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. It 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 of £5m required to manage day-to-day cash flow.

	31.3.26 Actual £m	**31.3.27 Forecast £m**	**31.3.28 Forecast £m**	**31.3.29 Forecast £m**
Loans CFR	193.1	205.7	234.9	239.9
External Borrowing	-166.5	-98.6	-75.8	-62.7
Internal (over) Borrowing	**26.6**	**107.1**	**159.1**	**177.2**
Less: Balance sheet resources	-57.3	-32.1	-16.1	-16.0
Investments (New Borrowing)	**-30.6**	**75.0**	**143.0**	**161.2**
Treasury Investments	30.6	5.0	5.0	5.0
New Borrowing	**0.0**	**80.0**	**148.0**	**166.2**
Net Loans Requirement	135.9	173.6	218.8	223.9
Liquidity Allowance	5.0	5.0	5.0	5.0
Liability Benchmark	**140.9**	**178.6**	**223.8**	**228.9**

Following on from the medium-term forecast above, the long-term liability benchmark assumes capital expenditure funded by borrowing based on the current capital programme, minimum revenue provision on new capital expenditure and income, expenditure and reserves all increasing by inflation. This is shown in the chart below together with the maturity profile of the Authority's existing borrowing**.**



Whilst borrowing may be above the liability benchmark, strategies involving borrowing which is significantly above the liability benchmark carry higher risk.

Maturity Structure of Borrowing: This indicator is set to control the Authority's exposure to refinancing risk. The upper and lower limits on the maturity structure of all borrowing were:

	30.9.26 Actual	Upper Limit	Lower Limit	Complied
Under 12 months	44.45%	25%	0%	No
12 months and within 24 months	0.11%	40%	0%	Yes
24 months and within 5 years	24.72%	60%	0%	Yes
5 years and within 10 years	1.61%	80%	0%	Yes
10 years and above	29.11%	100%	0%	Yes

The upper limit for the proportion of borrowing repayable within 12 months was exceeded as a consequence of the Authority's strategy to utilise short-term borrowing rather than lock into longer-term debt at higher interest rates. The maturity date reflects the earliest point at which repayment can be demanded by the lender. The Authority will continue to review market conditions and, where appropriate, replace short-term borrowing with longer-term borrowing when rates become more economically advantageous.

Long-term Treasury Management Investments: The purpose of this indicator is to control the Authority's exposure to the risk of incurring losses by seeking early repayment of its investments. The prudential limits on the long-term treasury management limits are:

	2025/26	2026/27	2027/28
Actual principal invested beyond year end	£13.28m	£13.28m	£13.28m
Limit on principal invested beyond year end	£60m	£40m	£20m
Complied?	Yes	Yes	Yes

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

Prudential Indicators

The Authority measures and manages its capital expenditure borrowing with references to the following indicators.

Capital Expenditure: The Authority has undertaken and is planning capital expenditure as summarised below.

	2025/26 actual	2026/27 forecast	2027/28 forecast	2028/29 forecast
General Fund Services	£51.185m	£81.115m	£54.538m	£11.008m

The main focus of future capital expenditure will be centred around various town centre redevelopment schemes, Schools Investment Programme and transport related works.

Capital Financing Requirement: The Authority's cumulative outstanding amount of debt finance is measured by the capital financing requirement (CFR). This increases with new debt-financed capital expenditure and reduces with MRP and if utilised capital receipts used to replace debt.

	31.3.2026 actual	31.3.2027 forecast	31.3.2028 forecast	31.3.2029 forecast
General Fund CFR	£202.27m	£212.45m	£240.63m	£245.50m

Gross Debt and the Capital Financing Requirement: Statutory guidance is that debt should remain below the capital financing requirement, except in the short term. The Authority has complied and expects to continue to comply with this requirement in the medium term as is shown below.

	31.3.2026 actual	31.3.2027 forecast	31.3.2028 forecast	31.3.2029 forecast
Debt	£168.98m	£194.10m	£239.25m	£244.16m
Capital Financing Requirement	£202.27m	£212.45m	£240.63m	£245.50m

Net Income from Commercial and Service Investments to Net Revenue Stream: The Authority's income from commercial and service investments as a proportion of its net revenue stream has been and is expected to be as indicated below.

	2025/26 actual	2026/27 forecast	2027/28 budget	2028/29 budget
Total net income from service and commercial investments £m	£1.063m	£0.931m	£0.931m	£0.931m
Proportion of net revenue stream	0.53%	0.39%	0.37%	0.36%

The table identifies that the authority is not reliant on commercial and service investment income to maintain its core functions.

Proportion of Financing Costs to Net Revenue Stream: Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP are charged to revenue.

The net annual charge is known as financing costs; this is compared to the net revenue stream, i.e. the amount funded from Council Tax, business rates and general government grants.

	2025/26 actual	2026/27 forecast	2027/28 budget	2028/29 budget
Financing costs (£m)	£7.7m	£7.6m	£11.6m	£12.3m
Proportion of net revenue stream	2.7%	3.2%	4.7%	4.8%

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