Item: 4

Investments Sub-committee: 20 November 2025.

Treasury Management – Mid-year Update 2025/26.

Report by Head of Finance.

1. Overview

1.1. Regulation 21 of the Council's Financial Regulations confirms that the Council has adopted the key recommendations of the Chartered Institute of Public Finance and Accountancy's Code of Practice for Treasury Management in the Public Services (the Code).

1.2. The Code defines treasury management to include investment activities.

1.3. The Council's investment priorities can be summarised as maintaining:

- The security of capital.
- The liquidity of its investments.

1.4. The Council aims to achieve the optimum return on its investments commensurate with proper levels of security and liquidity. The risk appetite of the Council is low in order to give priority to security of its investments. This is in keeping with the nature of the Strategic Reserve Fund, which is to provide for the benefit of Orkney and its inhabitants, whilst having regard to the Fund's long-term obligations in terms of the decommissioning of the Flotta Oil Terminal in the future.

1.5. The Financial Regulations refer to maintenance of the Treasury Management Policy Statement and Treasury Management Practices as the cornerstone for effective treasury management and the requirement to report annually on the Treasury Management function.

1.6. A detailed analysis of the Treasury Management Performance for the six-month period to 30 September 2025, is attached as Appendix 1 to this report, and covers the following activities:

- Borrowing activity.
- Temporary loans.
- Strategic Reserve Fund.

1.7. The conclusion of the analysis of performance is that existing treasury management practices have operated effectively over the first six months of financial year 2025/26.

2. Recommendations

2.1. It is recommended that members of the Sub-committee:

i. Scrutinise the mid-year update, attached as Appendix 1 to this report, prepared by Link Treasury Services, the Council's Treasury Adviser, which covers the following elements of treasury management , in order to obtain assurance that the Treasury Management Practices are operating effectively:

- An economic update for the first half of financial year 2025/26.
- A review of the Treasury Management Strategy Statement and Annual Investment Strategy.
- The Council's capital expenditure, as set out in the Capital Strategy and prudential indicators.
- A review of the Council's investment portfolio for 2025/26.
- A review of the Council's borrowing strategy for 2025/26.
- A review of compliance with Treasury and Prudential Limits for 2025/26.

3. Treasury Management Performance

3.1. As at 30 September 2025, the Council's debt portfolio stood at £50,000,000 with loan maturities ranging over periods from one to 44.5 years. Overall, this represents an average cost of borrowing of 3.90% per annum, with an average weighted duration of 24.03 years.

3.2. The cost of this debt is managed as part of the loan charges associated with the capital programme and has been offset in the short term with surplus funds placed on deposit for periods of up to one year at an average rate of 4.21% for the first half of financial year 2025/26.

3.3. The prime objective for the managed funds remains to maintain or increase their real value over time, while at the same time generating an annual return which meets the targets set by the Council. These objectives normally require to be measured over a number of years while acknowledging that abnormal fluctuations in the short term do create a cause for concern.

For Further Information please contact:
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Implications of Report

1. **Financial:** The Financial Regulations refer to maintenance of the Treasury Management Policy Statement and Treasury Management Practices as the cornerstone for effective treasury management and the requirement to report annually on the Treasury Management function.
2. **Legal:** Treasury Management arrangements help the Council meet its statutory obligation to secure best value.
   Section 40 of the Local Government in Scotland Act 2003 provides local authorities with the power to invest money. This power may be exercised in accordance with regulations made by Scottish Ministers under this section.
   Section 95 of the Local Government (Scotland) Act 1973 states that every local authority shall make arrangements for the proper administration of their financial affairs and shall secure that the proper officer has responsibility for the administration of those affairs.
3. **Corporate Governance:** On 20 February 2024, the Policy and Resources Committee noted that, from 2024/25 onwards, the Investments Sub-committee would be responsible for ongoing monitoring and scrutiny of the approved Treasury Management Strategy Statement, including a mid-year review and annual review.
4. **Human Resources:** None directly related to the recommendations in this report.
5. **Equalities:** An Equality Impact Assessment is not required for financial monitoring.
6. **Island Communities Impact:** An Island Communities Impact Assessment is not required for financial monitoring.
7. **Links to Council Plan**: The proposals in this report support and contribute to improved outcomes for communities as outlined in the following Council Plan strategic priorities:
   ☐ Growing our economy.
   ☐ Strengthening our Communities.
   ☐ Developing our Infrastructure.
   ☐ Transforming our Council.
8. **Links to Local Outcomes Improvement Plan:** The proposals in this report support and contribute to improved outcomes for communities as outlined in the following Local Outcomes Improvement Plan priorities:
   ☐ Cost of Living.
   ☐ Sustainable Development.
   ☐ Local Equality.
   ☐Improving Population Health.

9. **Environmental and Climate Risk:** Environmental, Social and Governance factors are recognised as having the potential to impact the Fund.
10. **Risk:** Reviewing the performance quarterly ensures that the treasury management processes are being adhered to and provides assurance that associated risks are being managed effectively.
11. **Procurement:** None directly related to the recommendations in this report.
12. **Health and Safety:** None directly related to the recommendations in this report.
13. **Property and Assets:** None directly related to the recommendations in this report.
14. **Information Technology:** None directly related to the recommendations in this report.
15. **Cost of Living:** None directly related to the recommendations in this report.

List of Background Papers

Policy and Resources 18 February 2025 – Treasury Management Strategy Statement 2025/26.

Appendix

Appendix 1 – Treasury Management Update – Mid-year review 2025/26.

Classification: Confidential

Treasury Management Strategy Statement and Annual Investment Strategy

Mid-Year Review Report 2025/26

MUFG Corporate Markets

A division of MUFG Pension & Market Services

Contents

1 Background

1.1 Treasury Management

The Council operates a balanced budget, which broadly means cash raised during the year will meet its cash expenditure. Part of the treasury management operations ensure this cash flow is adequately planned, with surplus monies being invested in low-risk counterparties, providing adequate liquidity initially before considering optimising investment return.

The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer-term cash flow planning to ensure the Authority can meet its capital spending operations. This management of longer-term cash may involve arranging long or short-term loans, or using longer term cash flow surpluses, and on occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

Accordingly, treasury management is defined as:

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

1.2 CIPFA Consultation on Treasury Management and Prudential Codes of Practice

The Chartered Institute of Public Finance and Accountancy is currently consulting local authorities in respect of potential changes to the Codes. At this juncture, the focus seems to primarily be on the Non-Treasury investment aspects of local authority activity. Officers will provide an update on any material developments/changes in due course.

2 Introduction

This report has been written in accordance with the requirements of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised 2021).
The primary requirements of the Code are as follows:

1. Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Authority's treasury management activities.

2. Creation and maintenance of Treasury Management Practices which set out the manner in which the Authority will seek to achieve those policies and objectives.

3. Receipt by the full Council/Board of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy – for the year ahead, a Mid-year Review Report and an Annual Report, (stewardship report), covering activities during the previous year. (Quarterly reports are also required for the periods ending April to June and October to December but may be assigned to a designated committee or panel as deemed appropriate to meet the Treasury Management governance and scrutiny aspects of the Council.)

4. Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

5. Delegation by the Authority of the role of scrutiny of treasury management strategy and policies to a specific named body. For this Council, the delegated body is the Policy and Resources Committee.

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

- An economic update for the first half of the 2025/26 financial year;
- A review of the Treasury Management Strategy Statement and Annual Investment Strategy;
- The Council's capital expenditure, as set out in the Capital Strategy, and prudential indicators;
- A review of the Council's investment portfolio for 2025/26;
- A review of the Council's borrowing strategy for 2025/26;
- A review of any debt rescheduling undertaken during 2025/26;
- A review of compliance with Treasury and Prudential Limits for 2025/26.

3 Economics and Interest Rates

3.1 Economics Update

- The first half of 2025/26 saw:
  - A 0.3% pick up in GDP for the period April to June 2025. More recently, the economy flatlined in July, with higher taxes for businesses restraining growth.
  - The 3m/yy rate of average earnings growth excluding bonuses has fallen from 5.5% to 4.8% in July.
  - CPI inflation has ebbed and flowed but finished September at 3.8%, whilst core inflation eased to 3.6%.
  - The Bank of England cut interest rates from 4.50% to 4.25% in May, and then to 4% in August.
  - The 10-year gilt yield fluctuated between 4.4% and 4.8%, ending the half year at 4.70%.
- From a GDP perspective, the financial year got off to a bumpy start with the 0.3% m/m fall in real GDP in April as front-running of US tariffs in Q1 (when GDP grew 0.7% on the quarter) weighed on activity. Despite the underlying reasons for the drop, it was still the first fall since October 2024 and the largest fall since October 2023. However, the economy surprised to the upside in May and June so that quarterly growth ended up 0.3% q/q. Nonetheless, the 0.0% m/m change in real GDP in July will have caused some concern, with the hikes in taxes for businesses that took place in April this year undoubtedly playing a part in restraining growth. The weak overseas environment is also likely to have contributed to the 1.3% m/m fall in manufacturing output in July. That was the second large fall in three months and left the 3m/3m rate at a 20-month low of -1.1%. The 0.1% m/m rise in services output kept its 3m/3m rate at 0.4%, supported by stronger output in the health and arts/entertainment sectors. Looking ahead, ongoing speculation about further tax rises in the Autumn Budget on 26 November will remain a drag on GDP growth for a while yet. GDP growth for 2025 is forecast by Capital Economics to be 1.3%.
- Sticking with future economic sentiment, the composite Purchasing Manager Index for the UK fell from 53.5 in August to 51.0 in September. The decline was mostly driven by a fall in the services PMI, which declined from 54.2 to 51.9. The manufacturing PMI output balance also fell, from 49.3 to 45.4. That was due to both weak overseas demand (the new exports orders balance fell for the fourth month in a row) and the cyber-attack-induced shutdown at Jaguar Land Rover since 1 September reducing car production across the automotive supply chain. The PMIs suggest tepid growth is the best that can be expected when the Q3 GDP numbers are released.
- Turning to retail sales, and the 0.5% m/m rise in volumes in August was the third such rise in a row and was driven by gains in all the major categories except fuel sales, which fell by 2.0% m/m. Sales may have been supported by the warmer-than-usual weather. If sales were just flat in September, then in Q3 sales volumes would be up 0.7% q/q compared to the 0.2% q/q gain in Q2.

- With the November Budget edging nearer, the public finances position looks weak. Public net sector borrowing of £18.0bn in August means that after five months of the financial year, borrowing is already £11.4bn higher than the OBR forecast at the Spring Statement in March. The overshoot in the Chancellor's chosen fiscal mandate of the current budget is even greater with a cumulative deficit of £15.3bn. All this was due to both current receipts in August being lower than the OBR forecast (by £1.8bn) and current expenditure being higher (by £1.0bn). Over the first five months of the financial year, current receipts have fallen short by a total of £6.1bn (partly due to lower-than-expected self-assessment income tax) and current expenditure has overshot by a total of £3.7bn (partly due to social benefits and departmental spending). Furthermore, what very much matters now is the OBR forecasts and their impact on the current budget in 2029/30, which is when the Chancellor's fiscal mandate bites. As a general guide, Capital Economics forecasts a deficit of about £18bn, meaning the Chancellor will have to raise £28bn, mostly through higher taxes, if she wants to keep her buffer against her rule of £10bn.

- The weakening in the jobs market looked clear in the spring. May's 109,000 m/m fall in the PAYE measure of employment was the largest decline (barring the pandemic) since the data began and the seventh in as many months. The monthly change was revised lower in five of the previous seven months too, with April's 33,000 fall revised down to a 55,000 drop. More recently, however, the monthly change was revised higher in seven of the previous nine months by a total of 22,000. So instead of falling by 165,000 in total since October, payroll employment is now thought to have declined by a smaller 153,000. Even so, payroll employment has still fallen in nine of the ten months since the Chancellor announced the rises in National Insurance Contributions (NICs) for employers and the minimum wage in the October Budget. The number of job vacancies in the three months to August stood at 728,000. Vacancies have now fallen by approximately 47% since its peak in April 2022. All this suggests the labour market continues to loosen, albeit at a declining pace.

- A looser labour market is driving softer wage pressures. The 3m/yy rate of average earnings growth excluding bonuses has fallen from 5.5% in April to 4.8% in July. The rate for the private sector slipped from 5.5% to 4.7%, putting it on track to be in line with the Bank of England's Q3 forecast (4.6% for September).

- CPI inflation fell slightly from 3.5% in April to 3.4% in May, and services inflation dropped from 5.4% to 4.7%, whilst core inflation also softened from 3.8% to 3.5%. More recently, though, inflation pressures have resurfaced, although the recent upward march in CPI inflation did pause for breath in August, with CPI inflation staying at 3.8%. Core inflation eased once more too, from 3.8% to 3.6%, and services inflation dipped from 5.0% to 4.7%. So, we finish the half year in a similar position to where we started, although with food inflation rising to an 18-month high of 5.1% and households' expectations for inflation standing at a six year high, a further loosening in the labour market and weaker wage growth may be a requisite to UK inflation coming in below 2.0% by 2027.

- An ever-present issue throughout the past six months has been the pressure being exerted on medium and longer dated gilt yields. The yield on the 10-year gilt moved sideways in the second quarter of 2025, rising from 4.4% in early April to 4.8% in mid-April following wider global bond market volatility stemming from the "Liberation Day" tariff announcement, and then easing back as trade tensions began to de-escalate. By the end of April, the 10-year gilt yield had returned to 4.4%. In May, concerns about stickier inflation and shifting expectations about the path for interest rates led to another rise, with the 10-year gilt yield fluctuating between 4.6% and 4.75% for most of May. Thereafter, as trade tensions continued to ease and markets increasingly began to price in looser monetary policy, the 10-year yield edged lower, and ended Q2 at 4.50%.

- More recently, the yield on the 10-year gilt rose from 4.46% to 4.60% in early July as rolled-back spending cuts and uncertainty over Chancellor Reeves' future raised fiscal concerns. Although the spike proved short lived, it highlighted the UK's fragile fiscal position. In an era of high debt, high interest rates and low GDP growth, the markets are now more sensitive to fiscal risks than before the pandemic. During August, long-dated gilts underwent a particularly pronounced sell-off, climbing 22 basis points and reaching a 27-year high of 5.6% by the end of the month. While yields have since eased back, the market sell-off was driven by investor concerns over growing supply-demand imbalances, stemming from unease over the lack of fiscal consolidation and reduced demand from traditional long-dated bond purchasers like pension funds. For 10-year gilts, by late September, sticky inflation, resilient activity data and a hawkish Bank of England have kept yields elevated over 4.70%.

- The FTSE 100 fell sharply following the “Liberation Day” tariff announcement, dropping by more than 10% in the first week of April - from 8,634 on 1 April to 7,702 on 7 April. However, the de-escalation of the trade war coupled with strong corporate earnings led to a rapid rebound starting in late April. As a result, the FTSE 100 closed Q2 at 8,761, around 2% higher than its value at the end of Q1 and more than 7% above its level at the start of 2025. Since then, the FTSE 100 has enjoyed a further 4% rise in July, its strongest monthly gain since January and outperforming the S&P 500. Strong corporate earnings and progress in trade talks (US-EU, UK-India) lifted share prices and the index hit a record 9,321 in mid-August, driven by hopes of peace in Ukraine and dovish signals from Fed Chair Powell. September proved more volatile and the FTSE 100 closed Q3 at 9,350, 7% higher than at the end of Q1 and 14% higher since the start of 2025. Future performance will likely be impacted by the extent to which investors’ global risk appetite remains intact, Fed rate cuts, resilience in the US economy, and AI optimism. A weaker pound will also boost the index as it inflates overseas earnings.

MPC meetings: 8 May, 19 June, 7 August, 18 September 2025

- There were four Monetary Policy Committee (MPC) meetings in the first half of the financial year. In May, the Committee cut Bank Rate from 4.50% to 4.25%, while in June policy was left unchanged. In June’s vote, three MPC members (Dhingra, Ramsden and Taylor) voted for an immediate cut to 4.00%, citing loosening labour market conditions. The other six members were more cautious, as they highlighted the need to monitor for “signs of weak demand”, “supply-side constraints” and higher “inflation expectations”, mainly from rising food prices. By repeating the well-used phrase “gradual and careful”, the MPC continued to suggest that rates would be reduced further.

- In August, a further rate cut was implemented. However, a 5-4 split vote for a rate cut to 4% laid bare the different views within the Monetary Policy Committee, with the accompanying commentary noting the decision was “finely balanced” and reiterating that future rate cuts would be undertaken “gradually and carefully”. Ultimately, Governor Bailey was the casting vote for a rate cut but with the CPI measure of inflation expected to reach at least 4% later this year, the MPC will be wary of making any further rate cuts until inflation begins its slow downwards trajectory back towards 2%.

- The Bank of England does not anticipate CPI getting to 2% until early 2027, and with wages still rising by just below 5%, it was no surprise that the September meeting saw the MPC vote 7-2 for keeping rates at 4% (Dhingra and Taylor voted for a further 25bps reduction).

- The Bank also took the opportunity to announce that they would only shrink its balance sheet by £70bn over the next 12 months, rather than £100bn. The repetition of the phrase that “a gradual and careful” approach to rate cuts is appropriate suggests the Bank still thinks interest rates will fall further but possibly not until February, which aligns with both our own view and that of the prevailing market sentiment.

3.2 Interest Rate Forecasts

The Authority has appointed MUFG Corporate Markets as its treasury advisors and part of their service is to assist the Council to formulate a view on interest rates. The PWLB rate forecasts below are based on the Certainty Rate (the standard rate minus 20bps) which has been accessible to most authorities since 1 November 2012.

MUFG Corporate Markets’ latest forecast on 11 August sets out a view that short, medium and long-dated interest rates will fall back over the next year or two, although there are upside risks in respect of the stickiness of inflation and a continuing tight labour market, as well as the size of gilt issuance.

MUFG Corporate Markets Interest Rate View 11.08.25													
	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27	Jun-27	Sep-27	Dec-27	Mar-28	Jun-28	Sep-28
BANK RATE	4.00	4.00	3.75	3.75	3.50	3.50	3.50	3.50	3.25	3.25	3.25	3.25	3.25
3 month ave earnings	4.00	4.00	3.80	3.80	3.50	3.50	3.50	3.50	3.30	3.30	3.30	3.30	3.30
6 month ave earnings	4.00	3.90	3.70	3.70	3.50	3.50	3.50	3.50	3.30	3.30	3.40	3.40	3.40
12 month ave earnings	4.00	3.90	3.70	3.70	3.50	3.50	3.50	3.50	3.30	3.40	3.50	3.60	3.60
5 yr PWLB	4.80	4.70	4.50	4.40	4.30	4.30	4.30	4.20	4.20	4.20	4.20	4.10	4.10
10 yr PWLB	5.30	5.20	5.00	4.90	4.80	4.80	4.80	4.70	4.70	4.70	4.70	4.60	4.60
25 yr PWLB	6.10	5.90	5.70	5.70	5.50	5.50	5.50	5.40	5.40	5.30	5.30	5.30	5.20
50 yr PWLB	5.80	5.60	5.40	5.40	5.30	5.30	5.30	5.20	5.20	5.10	5.10	5.00	5.00

4 Treasury Management Strategy Statement and Annual Investment Strategy Update

The Treasury Management Strategy Statement, (TMSS), for 2025/26 was approved by this Council on 18 February 2025.

- There are no policy changes to the TMSS; the details in this report update the position in the light of the updated economic position and budgetary changes already approved.

5 The Council's Capital Position (Prudential Indicators)

This part of the report is structured to update:

- The Council's capital expenditure plans;
- How these plans are being financed;
- The impact of the changes in the capital expenditure plans on the prudential indicators and the underlying need to borrow; and
- Compliance with the limits in place for borrowing activity.

5.1 Prudential Indicator for Capital Expenditure

This table shows the revised estimates for capital expenditure and the changes since the capital programme was agreed for 2025/26.

Capital Expenditure by Service	2025/26 Original Estimate £m	Current Position £m	2025/26 Revised Estimate £m
Social Care	2.258	1.939	1.367
Roads and Transportation	2.684	0.863	6.512
Education and Leisure	0.766	-0.048	0.792
Marine Services	5.157	0.023	6.353
Other Services	4.000	2.629	6.742
SRF – Windfarm	10.000	2.135	9.900
Finance Leases	2.000	0.000	2.000
Non-HRA	**26.865**	**7.541**	**33.666**
HRA	0.000	1.766	2.608
Total capital expenditure	**26.865**	**9.307**	**36.274**

The revised budget for 2025/26 reflects the following changes since the TMSS was approved in February 2025:

- Slippage of £1.719M from 2024/25 added to the capital programme for 2025/26.
- Slippage of £0.310M from 2024/25 added to the capital programme for 2025/26.
- Addition of £12.636M for Archaeology and the Environment Science Facility, Coastal Change Adaptation, Quanterness WindFarm, Inter-Islands Connectivity, Bus Infrastructure Fund and Covid Recovery project.
- £1.698M temporary increase to Plant & Vehicle Replacement Programme and Minor Improvements to Piers.
- Addition of £3.142M for Houton Infrastructure, Nature Restoration Fund, Active Travel, Viking Gallery, Bus Infrastructure Fund, Rendall Road Bike Shelter, House Purchases, Climate Emergency and Birsay Campsite Development.
- Removal of £.096M for Cycling Walking and Safer Routes Scheme.

5.2 Changes to the Financing of the Capital Programme

The table below draws together the main strategy elements of the capital expenditure plans (above), highlighting the original supported and unsupported elements of the capital programme, and the expected financing arrangements of this capital expenditure. The borrowing element of the table increases the underlying indebtedness of the Council by way of the Capital Financing Requirement (CFR), although this will be reduced in part by revenue charges for the repayment of debt (the Minimum Revenue Provision). This borrowing need may also be supplemented by maturing debt and other treasury requirements.

Capital Expenditure	2025/26 Original Estimate £m	2025/26 Revised Estimate £m
Total capital expenditure	**26.865**	**36.274**
Financed by:		
Capital receipts	0.235	0.235
Capital grants	5.983	11.964
Capital reserves	0.053	0.965
Finance leases	2.000	2.000
Revenue	0.569	0.951
Total financing	**8.84**	**16.115**
Borrowing requirement	**18.025**	**20.159**

5.3 Changes to the Prudential Indicators for the Capital Financing Requirement (CFR), External Debt and the Operational Boundary

The table below shows the CFR, which is the underlying external need to incur borrowing for a capital purpose. It also shows the expected debt position over the period, which is termed the Operational Boundary.

Prudential Indicator – Capital Financing Requirement

We are no longer on target to achieve the forecast Capital Financing Requirement with current estimates for slippage on the capital programme being £9.549M by 31 March 2026, against a revised budget for financial year 2025/26 of £36.274M.

Prudential Indicator – the Operational Boundary for external debt

	2025/26 Original Estimate £m	2025/26 Revised Estimate £m
CFR – non housing	65.096	72.179
CFR – housing	8.421	11.064
SRF - Windfarms	10.000	9.900
Total CFR	**83.517**	**93.143**
Net movement in CFR	**15.560**	**9.626**
Borrowing	85.000	85.000
Other long-term liabilities*	5.000	5.000
Total debt (year end position)	**65.000**	**65.000**

** On balance sheet PFI schemes and lease liabilities recognised under IFRS16 etc.*

5.4 Limits to Borrowing Activity

The first key control over the treasury activity is a prudential indicator to ensure that over the medium term, net borrowing (borrowings less investments) will only be for a capital purpose*. **Gross external borrowing** should not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional CFR for 2025/26 and next two financial years. This allows some flexibility for limited early borrowing for future years. The Council has approved a policy for borrowing in advance of need which will be adhered to if this proves prudent.

	2025/26 Original Estimate £m	**2025/26 Revised Estimate £m**
Borrowing	0	0
Total debt	65.000	65.000
CFR* (year end position)	83.517	93.143

A further prudential indicator controls the overall level of borrowing. This is **the Authorised Limit** which represents the limit beyond which borrowing is prohibited and needs to be set and revised by Members. It reflects the level of borrowing which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. It is the expected maximum borrowing need with some headroom for unexpected movements. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003.

Authorised limit for external debt	**2025/26 Original Indicator**	**2025/26 Revised Indicator**
Borrowing	95.000	95.000
Other long-term liabilities*	5.000	5.000
Total	100.000	100.000

6 Borrowing

The Council's capital financing requirement (CFR) for 2025/26 is £93.143m. The CFR denotes the Council's underlying need to borrow for capital purposes. If the CFR is positive the Council may borrow from the PWLB or the market (external borrowing), or from internal balances on a temporary basis (internal borrowing). The balance of external and internal borrowing is generally driven by market conditions. The table under paragraph 5.4 above shows the Council has borrowings of £50m and has utilised £43.143m of cash flow funds in lieu of borrowing. This is a prudent and cost-effective approach in the current economic climate but will require ongoing monitoring if gilt yields remain elevated, particularly at the longer-end of the yield curve (25 to 50 years).

Due to the overall financial position and the underlying need to borrow for capital purposes (the CFR), new external borrowing of £10m was undertaken in April 2025 from the PWLB at a rate of 4.61%. The capital programme is being kept under regular review due to the effects of on-going budgetary pressures. Our borrowing strategy will, therefore, also be regularly reviewed and then revised, if necessary, to achieve optimum value and risk exposure in the long-term.

It is anticipated that further borrowing from the PWLB will take place during this financial year, and there may be some drawdown of the approved loan from the National Wealth Fund to finance expenditure on the Quanterness Windfarm during the next 6 months.

PWLB maturity certainty rates (gilts plus 80bps) year to date to 30 September 2025

Gilt yields and PWLB certainty rates have remained relatively volatile throughout the six months under review, but the general trend has been for medium and longer dated parts of the curve to shift higher whilst the 5-year part of the curve finished September close to where it begun in April.

Concerns around the stickiness of inflation, elevated wages, households' inflation expectations reaching a six-year high, and the difficult funding choices facing the Chancellor in the upcoming Budget on 26 November dominated market thinking, although international factors emanating from the Trump administration's fiscal, tariff and geo-political policies also played a role.

At the beginning of April, the 1-year certainty rate was the cheapest part of the curve at 4.82% whilst the 25-year rate was relatively expensive at 5.92%. Early September saw the high point for medium and longer-dated rates, although there was a small reduction in rates, comparatively speaking, by the end of the month.

The spread in the 5-year part of the curve (the difference between the lowest and highest rates for the duration) was the smallest at 37 basis points whilst, conversely, the 50-years' part of the curve saw a spread of 68 basis points.

At this juncture, MUFG Corporate Markets still forecasts rates to fall back over the next two to three years as inflation dampens, although there is upside risk to all forecasts at present. The CPI measure of inflation is expected to fall below 2% in early 2027 but hit a peak of 4% or higher later in 2025.

The Bank of England announced in September that it would be favouring the short and medium part of the curve for the foreseeable future when issuing gilts, but market reaction to the November Budget is likely to be the decisive factor in future gilt market attractiveness to investors and their willingness to buy UK sovereign debt.

HIGH/LOW/AVERAGE PWLB RATES FOR 01.04.25 – 30.09.25

	1 Year	5 Year	10 Year	25 Year	50 Year
01/04/2025	4.82%	4.94%	5.38%	5.95%	5.63%
30/09/2025	4.58%	4.95%	5.53%	6.23%	5.98%
Low	4.36%	4.62%	5.17%	5.78%	5.46%
Low date	04/08/2025	02/05/2025	02/05/2025	04/04/2025	04/04/2025
High	4.84%	4.99%	5.62%	6.41%	6.14%
High date	02/04/2025	21/05/2025	03/09/2025	03/09/2025	03/09/2025
Average	4.55%	4.82%	5.40%	6.11%	5.83%
Spread	0.48%	0.37%	0.45%	0.63%	0.68%

- The current PWLB rates are set as margins over gilt yields as follows: -.
    - **PWLB Standard Rate** is gilt plus 100 basis points (G+100bps)
    - **PWLB Certainty Rate (GF)** is gilt plus 80 basis points (G+80bps)
    - **PWLB Local Infrastructure Rate** is gilt plus 60 basis points (G+60bps)
    - **PWLB Certainty Rate (HRA)** is gilt plus 40bps (G+40bps)

- The **National Wealth Fund** will lend to local authorities that meet its scheme criteria at a rate currently set at gilt plus 40bps (G+40bps).

7 Debt Rescheduling

Debt repayment and rescheduling opportunities have increased over the course of the past six months and will be considered if giving rise to long-term savings. However, no debt repayments or rescheduling have been undertaken to date in the current financial year.

8 Compliance with Treasury and Prudential Limits

It is a statutory duty for the Council to determine and keep under review the affordable capital expenditure limits. During the half year ended 30 September 2025, the Council has operated within the treasury and prudential indicators set out in the Council's Treasury Management Strategy Statement for 2025/26. The Head of Finance reports that no difficulties are envisaged for the current or future years in complying with these indicators.

All treasury management operations have also been conducted in full compliance with the Authority's Treasury Management Practices.

9 Annual Investment Strategy

The Treasury Management Strategy Statement (TMSS) for 2025/26, which includes the Annual Investment Strategy, was approved by the Authority on 18 February 2025. In accordance with the CIPFA Treasury Management Code of Practice, it sets out the Council's investment priorities as being:

- Security of capital
- Liquidity
- Yield

The Council will aim to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity and with the Council's risk appetite. In the current economic climate, it is considered appropriate to keep investments short term to cover cash flow needs, but also to seek out value available in periods up to 12 months with high credit quality financial institutions, using the MUFG Corporate Markets suggested creditworthiness approach, including a minimum sovereign credit rating and Credit Default Swap (CDS) overlay information.

Creditworthiness
The UK's sovereign rating has proven robust through the first half of 2025/26. The Government is expected to outline in detail its future fiscal proposals in the Budget scheduled for 26 November 2025.

Investment Counterparty criteria
The current investment counterparty criteria selection approved in the TMSS is meeting the requirement of the treasury management function.

CDS prices
It is noted that sentiment in the current economic climate can easily shift, so it remains important to undertake continual monitoring of all aspects of risk and return in the current circumstances.

Investment balances

The average level of funds available for investment purposes during the first half of the financial year was £9.232m. The temporary loans portfolio has operated within policy during financial year 2025/26 and has realised a return of 4.21% as at 30 September 2025. This is ahead/behind of the 30-day Sterling Overnight Index Average rate performance benchmark (3.98%).

Treasury Portfolio investments held at 30 September 2025:

Treasury Investments – Managed in house	Principal (£m)	Interest Rate	Maturity Date
DMADF	2.800	3.97%	14/11/2025
DMADF	1.200	3.97%	21/11/2025
DZ Bank	2.000	4.12%	22/12/2025
CIC Bank	4.000	4.17%	04/02/2026
Aberdeen Standard Investments Money Market Fund	6.000	4.07%	Call
Blackrock ICS Heritage Shared Money Market Fund	3.700	4.06%	Call
Insight Liquidity Funds PLC	5.900	4.06%	Call
The Royal Bank of Scotland	0.045	2.00%	Call
Total investments	25.645		

Non-Treasury Strategic Reserve Fund Local Investments – Managed in-house	Actual (£m)	Performance in 24/25
Fishing Quota	4.300	2.84%
Private Companies	4.512	5.0%
Other	0.013	0.0%
Total Strategic Reserve Fund Investments – Managed in-house	**8.825**	

Treasury Strategic Reserve Fund – Managed externally	Actual (£m)	Performance Quarter ending 30/09/25	Benchmark
Equity Portfolio	56.304	10.7%	9.9%
Global Equity Portfolio	62.731	9.2%	10.2%
Diversified Growth Fund	20.026	4.9%	1.8%
High Yield Credit Strategies Fund	26.092	1.9%	2.3%
Private Loan Fund	6.053	n/a	n/a
UK Property Fund	24.287	0.9%	1.3%
Secured Income Fund	30.136	n/a	n/a
Corporate Bonds Fund	44.038	1.1%	1.4%
Total investments	**269.667**	5.0%	4.9%

Approved limits

Officers can confirm that the approved limits within the Annual Investment Strategy were not breached during the period ended 30 September 2025.

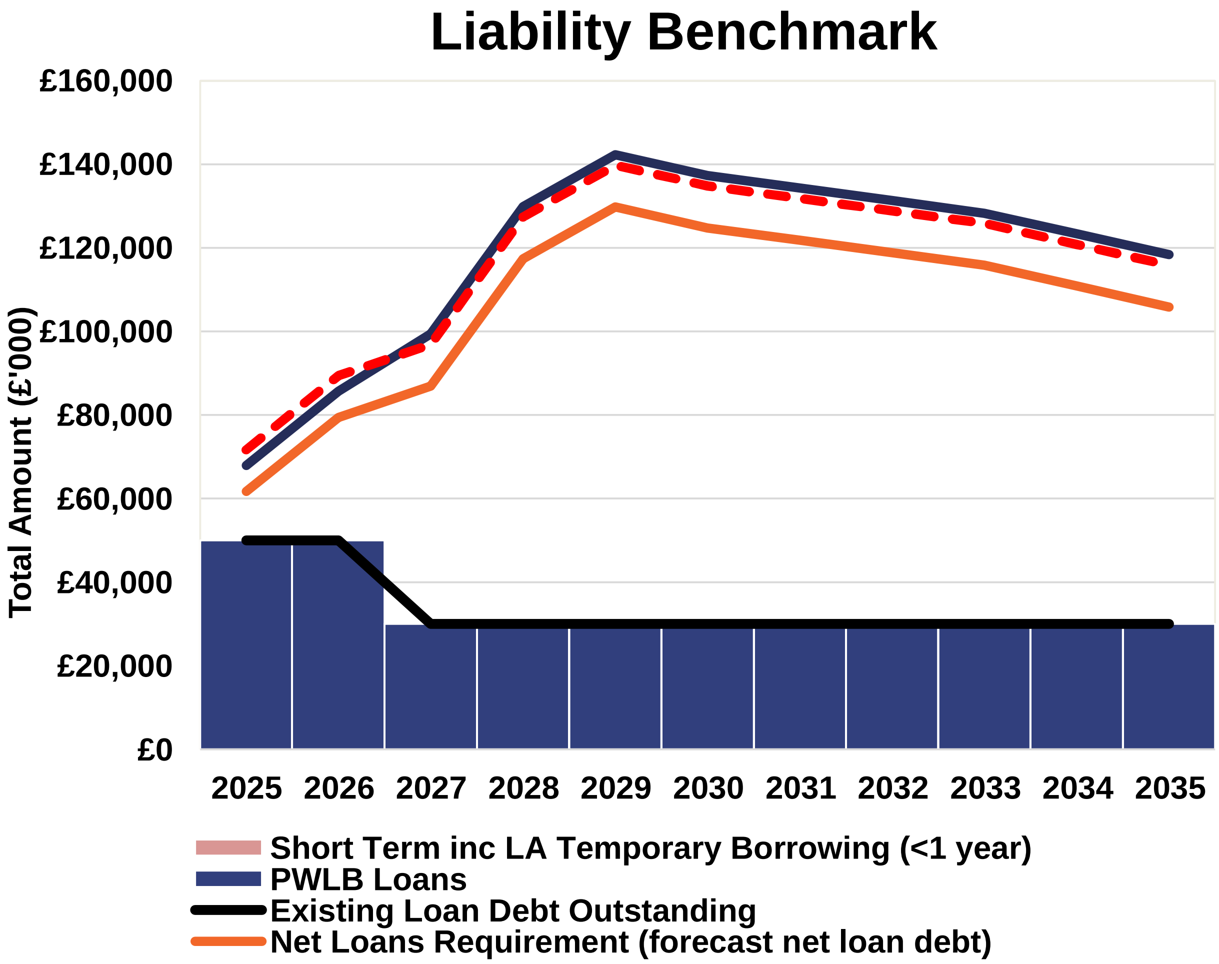
No performance figures are provided where full drawdown of the Council's commitment has not been concluded.

10 Other

1. Changes in Risk Appetite

The 2021 CIPFA Codes and guidance notes place importance on risk management. Where an authority changes its risk appetite e.g., for moving surplus cash into or out of certain types of investment funds or other types of investment instruments, this change in risk appetite and policy should be brought to members' attention in treasury management update reports.

APPENDIX 1: the CFR, Liability Benchmark and Borrowing



APPENDIX 2: Investment Portfolio

Investments held as of 30 September 2025 compared to our counterparty list:

Borrower	Principal (£)	Interest Rate	Start Date	Maturity Date	Lowest LT / Fund Rating	Historic Risk of Default	Expected Credit Loss (£)
The Royal Bank of Scotland Plc (RFB)	44,874	2.00%		Call	A+	0.000%	0
MMF Aberdeen Standard Investments	6,000,000	4.07%		MMF	AAAm		
MMF BlackRock	3,700,000	4.05%		MMF	AAAm		
MMF Insight	5,900,000	4.06%		MMF	AAAm		
DMO	2,800,000	3.97%	21/08/2025	14/11/2025	AA-	0.003%	0
DMO	1,200,000	3.97%	18/08/2025	21/11/2025	AA-	0.003%	0
DZ Bank AG (Deutsche Zentral-Genossenschaftsbank)	2,000,000	4.12%	22/08/2025	22/12/2025	A+	0.010%	210
Credit Industriel et Commercial	4,000,000	4.17%	04/08/2025	04/02/2026	A+	0.016%	642
Total Investments	**£25,644,874**	**4.07%**					£852

APPENDIX 3: Approved Countries for Investments as of 30 September 2025

Based on lowest available rating

AAA

- Australia
- Denmark
- Germany
- Netherlands
- Norway
- Singapore
- Sweden
- Switzerland

AA+

- Canada
- U.S.A.

AA

- Abu Dhabi (UAE)
- Finland
- Qatar

AA-

- **U.K.**

A+

- Belgium
- France