Audit and Governance Committee
30th July 2026

EXECUTIVE HEAD OF FINANCE
REPORT NO: FIN2615

TREASURY MANAGEMENT AND NON-TREASURY INVESTMENT OPERATIONS 2025/26 – Quarter 4 – Outturn

SUMMARY:
This report sets out the draft activities of the Treasury Management and non-Treasury Investment Operations for quarter 4 in the financial year 2025/26, and reports on compliance with Prudential Indicators, pending the statement of accounts being signed off by the Council's external auditors.

RECOMMENDATIONS:
Members are requested to:

(i) Make any recommendations, as appropriate, to the Cabinet on the contents of this report in relation to the treasury management and non-treasury investment operations carried out.

1. INTRODUCTION

1.1 This report sets out the Treasury Management and Non-Treasury Investment operation performance for Quarter 4, outturn, 2025/26, pending the statement of accounts being signed off by the Council's external auditors. This report is a statutory requirement under the CIPFA Code of Practice on Treasury Management.

1.2 Full Council approved the Annual Treasury Management Strategy and Non-Treasury Investment Strategy for the financial year 2025/26 in February 2025. The Council's treasury management activity is underpinned by CIPFA's Code of Practice on Treasury Management 2021 ("the Code") and is fully incorporated into the Council's adopted strategy.

2. PURPOSE

2.1 This report sets out compliance with the strategy and performance against Prudential Indicators to the end of March 2026 within appendices (1-4):

Appendix 1

- The **Treasury Management operations** which sets out how the Council's treasury service operated during the period to March 2026;
- The **Treasury Management Borrowing** which sets out the Council's borrowing during the period to March 2026, and;
- The **Treasury Management Investments** which sets out the Council's Treasury Management investment operations for the period to March 2026.

Appendix 2

- the **Prudential indicators** performance is compared to the indicators set out in the Annual Capital Strategy for the year 2025/26.

Appendix 3

- The list of borrowing counterparties as at end of March 2026.

Appendix 4

- Market commentary regarding from the Council's treasury management advisors Arlingclose

3 BACKGROUND

3.1 The Chartered Institute of Public Finance and Accountancy (CIPFA) have issued guidance on the aims and requirements of a Capital Strategy focusing on a whole organisation approach to prudent, sustainable, and resilient local government investment.

3.2 CIPFA have also issued two professional Codes of Practice to which the Council is required to "have regard to". These Codes provide frameworks that are designed to support local strategic planning, local asset management planning and proper option appraisal:

- The Prudential Code – developed to support local authorities in taking decisions around their capital investment programmes. The objectives of the Prudential Code are to ensure, within a clear reporting framework, that a local authority's capital expenditure plans and investment plans are affordable and proportionate; that all external borrowing and other long-term liabilities are within prudent and sustainable levels; that the risks associated with investments for commercial purposes are proportionate to their financial capacity; and that treasury management decisions are taken in accordance with good professional practice.

- The Treasury Management Code - Treasury Management is defined as 'The management of the organisation's borrowing, investments, and cash flows, including its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks'.

3.3 The primary purpose of the treasury management operation is to ensure that cash flow is adequately planned, with cash being available when it is needed to deliver the Councils services. The secondary function of the treasury management operation is the funding of the Council's capital programme and manage cashflow requirements over a longer-term period.

3.4 Non-treasury investment operations should ensure that all investments made primarily for service reasons. Then, second to this, the function of investment management is to generate returns.

3.5 This quarterly report provides an update and includes the requirement in the 2021 Code of quarterly reporting of the treasury management prudential indicators.

4 CONCLUSIONS ON THE TREASURY MANAGEMENT AND NON-TREASURY INVESTMENT OPERATIONS DURING Q4 2025/26

4.1 All treasury activity was conducted within the approved Treasury Management Practices (TMP's).

4.2 Borrowing maturity has now moved towards longer term to give cost certainty and lower interest rate exposure risk, providing more interest rate stability on borrowing.

5 KEY RISKS

5.1 The Council has borrowed 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.

5.2 The key risks to the Councils delivery of successful treasury and non-treasury investment options include:

- Inflation levels: Inflation rates are now reducing after a prolonged period of increased levels.
- Bank of England Base rate: Base rate is at 3.75% with a change in predictions recently from a slow reduction to maintaining this level if not having a slight increase.
- Delivery of Capital Programme: Will impact borrowing requirements and timing will impact rates achievable for both borrowing and investments during the years.
- Delivery of the capital receipts pipeline within the agreed MTFS timeframes to reduce the need to borrow.

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Treasury Management Outturn Report 2025/26

Introduction

The Council adopted the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice* (the CIPFA Code). This quarterly report includes the requirement in the 2021 Code of quarterly reporting of the treasury management provides an update of the treasury management prudential indicators. The non-treasury prudential indicators are included in Appendix 2.

The Council's treasury management strategy for 2025/26 was approved at a meeting on 27th February 2025. The Authority has borrowed 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 Council's treasury management strategy.

Local Context

On 31st March 2026, the Council had net borrowing of £117.1m (31st March 2025: £127m), defined as external borrowing less treasury investments, cash and cash equivalents 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) summarised in Table 1 below.

Table 1: Draft Balance Sheet Summary

	31.3.25 Actual £m	31.3.26 Actual*** £m
General Fund CFR	174.2	174.1
Less: Other debt liabilities*	0.6	0.3
Loans CFR	**173.6**	**173.8**
External borrowing**	166.0	149.0

* leases that form part of the Authority's total debt
** shows only loans to which the Authority is committed and excludes optional refinancing
*** Actual figures are subject to change until accounts are signed off by External Auditors, EY.

The treasury management position at 31st March 2026 and the change during the year is shown in Table 2 below.

Table 2: Treasury Management Summary

	31.3.25 Balance £m	Movement £m	31.3.26 Balance £m	31.3.26 Rate %
Long-term borrowing				
- PWLB	62.0	65.0	127.0	4.75
- Other	2.0	10.0	12.0	4.58
Short-term borrowing	102.0	(92.0)	10.0	4.58
Total borrowing	**166.0**	**(17.0)**	**149.0**	
Long-term investments	16.0	(3.0)	13.0	4.75
Short-term investments	5.0	8.0	13.0	5.76
Cash and cash equivalents	18.0	(12.1)	5.9	4.07
Total investments	**39.0**	**(7.1)**	**31.9**	
Net borrowing	**127.0**	**(9.9)**	**117.1**	

Borrowing Strategy and Activity

As outlined in the treasury strategy, the Authority's chief objective when borrowing has been to strike an appropriate risk balance between securing interest costs within its Medium Term Financial Strategy (MTFS) assumptions 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 slightly decreased over most of the last financial year; reflecting expectations of lower interest rates, supporting a lower MTFS assumption in 2026/27. Subsequent to the war in the Middle East however, gilt yields saw a rapid rise to above the rate assumed in the MTFS at the beginning of the 2025/26 financial year.

The PWLB certainty rate for 10-year maturity loans was 5.38% at the beginning of the period and 5.72% at the end. The lowest available 10-year maturity certainty rate was 5.13% and the highest was 5.88%. Rates for 20-year maturity loans ranged from 5.71% to 6.37% during the period, and 50-year maturity loans from 5.46% to 6.24%. The cost of short-term borrowing from other local authorities has been similar to or a little above Bank of England Base Rate for most of the period, with interest rates between 4.0% and 4.5%. However, as is commonly seen, rates rose higher towards the end of the financial year, with rates of 5.0% - 7.0% being seen.

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.

The Authority currently holds £111m in commercial investments primarily for financial return that were purchased prior to the change in the CIPFA Prudential Code. Before undertaking further additional borrowing the Authority will review the options for exiting these investments to reduce the impact of borrowing costs and risk on the revenue account.

Loans Portfolio

At 31st March 2026 the Authority held £149m of loans, (a decrease of £17m from the position as of 31st March 2025), as part of its strategy for funding previous and current years' capital programmes. Outstanding loans on 31st March 2026 are summarised in Table 3A below.

Table 3A: Borrowing Position

	31.3.25 Balance £m	Net Movement £m	31.03.26 Balance £m	31.03.26 Weighted Average Rate %
Public Works Loan Board (all long-term)	62.0	65.0	127.0	4.75
Local authorities (long-term)	2.0	10.0	12.0	4.58
Local authorities (short-term)	102.0	(92.0)	10.0	4.58
Total borrowing	**166.0**	**(17.0)**	**149.0**	

The average rate on the Authority's short-term loans at 31st March 2026 was 4.58%, this compares with 4.41% 3 months ago.

Table 3B: Long-dated Loans borrowed

	Amount £m	Rate %	Period (Years)
PWLB Maturity Loan	127.0	4.75	2-4
Horsham District Council	2.0	5.10	2
South Yorkshire Mayoral Combined Authority	5.0	4.45	3
Torbay Borough Council	5.0	4.50	4
Total long-term borrowing	**139.0**		

The Council's new borrowing decisions to replace existing borrowing as current loans mature are determined by a cashflow projection including the achievement and timing of capital receipts from planned property sales.

Forward starting loans
No forward starting loans were obtained during Q4.

There remains a strong argument for diversifying funding sources, particularly if rates can be achieved on alternatives which are below PWLB. The Authority will evaluate and pursue these lower cost solutions and opportunities with its advisor Arlingclose, including coordinating borrowing from the recently announced North Hampshire Unitary Council partners.

Treasury Investment Activity

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

The Council holds some invested funds, representing income received in advance of expenditure plus balances and reserves held. The investment position is shown in table 4 below.

Table 4: Treasury Investment Position

	31.3.25 Balance £m	Net Movement £m	31.03.26 Balance £m	31.03.26 Income Return %
Banks & building societies	0.3	(0.2)	0.1	3.88
Local authorities and other govt entities	5.0	8.0	13.0	4.17
Money Market Funds	17.7	(11.9)	5.9	4.09
Other Pooled Funds				
- *Strategic bond funds*	6.0	0	6.0	4.91
- *Equity income funds*	5.0	0	5.0	7.62
- *Property funds*	3.0	(3.0)	-	-
- *Multi asset income funds*	2.0	0	2.0	5.81
Total investments	**39.0**	**(7.0)**	**32.0**	

Both the CIPFA Code and government guidance require the Council 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 Council'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.

As demonstrated by the liability benchmark in this report, the Council 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.

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	Weighted Average Maturity (days)	Rate of Return %
31.03.2025	5.14	A+	78%	7	5.65
31.03.2026	4.66	A+	32%	9	7.10
Similar LAs	**4.57**	**A+**	**58%**	**45**	**4.67**
All LAs	**4.60**	**A+**	**64%**	**10**	**4.46**

Externally Managed Pooled Funds
£13m of the Council's investments is invested in externally managed strategic pooled funds where short-term security and liquidity are lesser considerations, and the objectives instead are regular revenue income and long-term price stability.

Most asset classes achieved positive performance over the first half of the 2025/26 financial year, although conditions remained volatile and heavily influenced by political and macroeconomic developments.

The Authority has budgeted £540k income from these investments in 2025/26. Income received up to 31st March was £610k.

Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Council's medium- to long-term 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. On the assumption that when published regulations follow this policy announcement, 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 had set up a reserve of £1m to mitigate the impact of the statutory override not being extended. Given current budgetary pressures and the extension of the override the authority decided to release £1m from this reserve.

Non-Treasury Investments

The definition of investments in the Treasury Management Code now covers all the financial assets of the Council as well as other non-financial assets which the Council 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) and or for commercial purposes (made primarily for financial return).

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

The Authority also held £117m of such investments in:

- directly owned property £111m
- loans to local businesses and landlords £4.5m
- Subsidiaries £2.3m

A full list of the Council's non-treasury investments is available.

Treasury Performance

The Council measures the financial performance of its treasury management activities both in terms of its impact on the revenue budget and its relationship to benchmark interest rates.

Compliance

The Section 151 Officer reports that all treasury management activities undertaken during the year complied fully with the principles in the Treasury Management Code and the Authority's approved Treasury Management Strategy. Compliance with specific investment limits is demonstrated in table 7 below.

Table 7: Investment Limits	**31.03.26 Actual**	**2025/26 Limit**	**Complied?**
Any group of pooled funds under the same management	0	15m	Yes
Negotiable instruments held in a broker's nominee account	0	15m	Yes
Limit per non-UK country	0	6m	Yes

Compliance with the Authorised Limit and Operational Boundary for external debt is demonstrated in table 8 below.

Table 8: Debt and the Authorised Limit and Operational Boundary	**31.03.26 Actual**	**2025/26 Operational Boundary**	**2025/26 Authorised Limit**	**Complied?**
Borrowing	149.0	150.0	180.0	Yes
Finance Leases	**0.4**	**1.8**	**2.0**	Yes
Total debt	**149.4**	**151.8**	**182.0**	

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.

Treasury Management Prudential Indicators

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

1. Liability Benchmark

This indicator compares the Council'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 £21m. This incorporates £16m invested in strategic pooled funds, that cannot be sold at short notice, and an additional £5m liquidity buffer to manage short-term cashflow requirements. Whilst the £5m liquidity buffer has been maintained the pooled funds element has been reduced to £13m, due to the sale of some funds to mitigate the losses of a fund which was closing. The original £21m was set as the pooled funds were long term investments but had little impact on the liquidity for cashflow purposes hence the minimum level of cash held has not been increased. The updated minimum level of £18m is reflected in the Treasury Management Strategy for 2026/27.

	31.3.25 Actual	31.3.26 Actual	31.3.27 Forecast	31.3.28 Forecast
Loans CFR	173.3	173.8	156.8	156.9
Less: Balance sheet resources	45.1	41.1	39.8	40.3
Net loans requirement	128.2	132.7	117.0	116.6
Plus: Liquidity allowance	21.0	18.0	18.0	18.0
Liability benchmark	**149.2**	**150.7**	**135.0**	**134.6**
Existing borrowing*	**166.0**	**149.0**	**100.0**	**90.0**

* shows only loans to which the Authority is committed and excludes optional refinancing

The Liability Benchmark indicated the minimum amount of external borrowing required each year to ensure the council has sufficient money to pay its bills. Actual borrowing is usually above the liability benchmark to account for variation in the councils cashflow requirements, borrowing will also be taken out in advance of maturing debt when interest rates are favourable.

2. 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:

	Upper Limit (%)	Lower Limit (%)	31.03.26 Actual (%)	Complied?
Under 12 months	100	0	0	Yes
12 months and within 24 months	100	0	56	Yes
24 months and within 5 years	100	0	44	Yes
5 years and within 10 years	100	0	0	Yes
10 years and above	100	0	0	Yes

Time periods start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment.

3. 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 limits are:

	2025/26	2026/27	2027/28
Limit on principal invested beyond year end	£30m	£30m	£20m
Actual principal invested beyond year end	£13m	£13m	£13m
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.

Additional indicators

Security
The Council has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average credit rating and credit score of its investment portfolio. This is calculated by applying a score to each investment (AAA=1, AA+=2, etc.) and taking the arithmetic average, weighted by the size of each investment. Unrated investments are assigned a score based on their perceived risk.

	2025/26 Target	31.03.26 Actual	Complied?
Portfolio average credit rating	A+	A+	Yes
Portfolio average credit score	5	4.66	Yes

Liquidity
The Council has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments within a rolling three-month period, without additional borrowing.

	31.03.26 Actual	2025/26 Target	Complied?
Total cash available within 3 months	5.9	5	Yes

Interest Rate Exposures: This indicator is set to control the Authority's exposure to interest rate risk. The indicator shows the impact of replacing borrowing maturing in the next 12 months if interest rates change by 1% up or down.

Interest rate risk indicator	**2025/26 Target**	**31.03.26 Actual**	**Complied?**
Upper limit on one-year revenue impact of a 1% rise in interest rates	£2m	£545k	Yes
Upper limit on one-year revenue impact of a 1% fall in interest rates	-£2m	-£545k	Yes

CIPFA encourages the use of this indicator but does not require or recommend it; this is our recommended replacement indicator, which matches the one in the statement of accounts disclosure notes.

For context, the changes in interest rates during the quarter were:

	31/3/25	31/03/26
Bank Rate	4.50%	3.75%
1-year PWLB certainty rate, maturity loans	4.82%	5.04%
5-year PWLB certainty rate, maturity loans	4.94%	5.32%
10-year PWLB certainty rate, maturity loans	5.38%	5.77%
20-year PWLB certainty rate, maturity loans	5.88%	6.24%
50-year PWLB certainty rate, maturity loans	5.63%	6.07%

The impact of a change in interest rates is calculated on the assumption that maturing loans and investment will be replaced at new market rates.

Prudential Indicators - Outturn 2025/26

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

It is now a requirement of the CIPFA Prudential Code that these are reported on a quarterly basis.

Capital Expenditure

The Council has undertaken and is planning capital expenditure as summarised below:

	2024/25 Actual	2025/26 Actual	2026/27 Budget	2027/28 Forecast
Capital expenditure	14.3	5.6	3.6	2.7

The main General Fund capital projects to date have included Union Yard, and Aldershot Crematorium.

Capital Financing Requirement

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 and reduces with MRP and capital receipts used to replace debt.

	31.3.2025 actual	31.3.2026 actual	31.3.2027 forecast
CFR	174.2	174.1	157.1

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.

	31.3.2025 actual	31.3.2026 actual	31.3.2027 forecast
Debt (incl. leases)	166.6	149.3	100.3
Capital Financing Requirement	174.2	174.1	157.1

Debt and the Authorised Limit and Operational Boundary

The Council is legally obliged to set an affordable borrowing limit (also termed the Authorised Limit for external debt) each year. In line with statutory guidance, a lower "operational boundary" is also set as a warning level should debt approach the limit.

	Debt at 31.03.26	2025/26 Authorised Limit	2025/26 Operational Boundary	Complied?
Borrowing	149.0	180.0	150.0	Yes
Leases	0.3	2.0	1.8	Yes
Total debt	**149.3**	**182.0**	**151.8**	Yes

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

Net Income from Commercial and Service Investments to Net Revenue Stream
The Council’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.

	2024/25 actual	2025/26 actual	2026/27 forecast
Total net income from service and commercial investments	7.9	8.9	7.9
Proportion of net revenue stream	56.99%	67.27%	44.08%

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.

	2024/25 actual	2025/26 actual	2026/27 forecast
Financing costs (£m)	7.0	7.1	6.0
Proportion of net revenue stream	50.59%	68.72%	43.21%

Treasury Management Indicators
These indicators (Liability Benchmark, Maturity Structure of Borrowing, Long-Term Treasury Management Investments) are within the Treasury Management Report outturn 2025/26 at Appendix 1.

APPENDIX 3

LIST OF DEBT COUNTERPARTIES AS AT 31ST MARCH 2026

	Amount
PWLB	5,000,000
PWLB	5,000,000
South Yorkshire Mayoral Combined	5,000,000
PWLB	10,000,000
PWLB	15,000,000
PWLB	10,000,000
Torbay Borough Council	5,000,000
PWLB	20,000,000
PWLB	12,000,000
PWLB	20,000,000
PWLB	10,000,000
PWLB	15,000,000
PWLB	5,000,000
Bolton Metropolitan Borough Council	5,000,000
Thames Valley PCC	5,000,000
Horsham District Council	2,000,000
	149,000,000

External Context

Economic background

The financial year was largely dominated by two periods of significant uncertainty and volatility. The first being the US trade tariff 'Liberation Day' in April 2025 and the second was the US/Israel war with Iran at the end of February 2026.

After the initial fallout from US trade tariffs, the following months saw some improvements as equity markets made gains and bond yields eased modestly. However, in the UK this trend in bond yields reversed somewhat as an uncertain economic outlook together with concerns around the government's fiscal position and autumn Budget saw 'term premia' rise as investors demanded a higher return for holding gilts.

The Budget itself was more muted than had been expected. Despite a weak economic outlook, this helped UK markets perform better with gilt yields trending downwards, inflation easing, and expectations for cuts in Bank of England (BoE) Bank Rate increasing.

The end of February 2026 saw the start of the war between US/Israel and Iran. The conflict caused oil and other commodity prices to rise sharply as the shipping lanes in the region became effectively closed, restricting global oil supply. At the end of the period, the economic outlook remained highly uncertain in terms of its impact on inflation as well as countries' fiscal and monetary policy conditions around the globe.

Prior to the start of the war, headline UK consumer price inflation (CPI) inflation had generally been trending downwards, albeit the 3% in February 2026 was unchanged from January. Core CPI also stayed put at 3.1%. Inflation was expected to fall further over the coming months to the BoE's 2% target, but the war changed this. Inflation is now expected to rise again, but how quickly and by how much depends on the duration of the war and how long commodity prices are elevated.

The Office for National Statistics (ONS) reported the UK economy expanded by 0.1% in Q4 2025. This followed previous modest gains of 0.2% in Q2 and by 0.1% in Q3. Of the subsequent monthly figures, the ONS estimated that GDP showed no growth in January 2026. As this is from before the war started the impact on growth will not be seen formally in the data for a couple more months.

While the most recent labour market figures were slightly better than expected, the general trend has been one of persistent weakness. In the three months to January 2026, the unemployment rate rose to 5.2% (from 5.1%), while the employment rate held at 75.1%. Despite inflation being expected to rise in the coming months, labour market conditions remain loose and so any upward pressure on wages from general inflation is likely to be tempered by the weaker labour market environment.

After cutting Bank Rate to 3.75% in December 2025, the BoE's Monetary Policy Committee (MPC) voted 5-4 to hold rates in February 2026 and then unanimously to do so again in March. Until the war started, financial markets were expecting Bank Rate to be cut to 3.5% at the March meeting. However, the conflict in the Middle East quickly changed this. The MPC noted the risks to both inflation and growth and indicated they could move rates either up or down depending on the conditions. Financial markets quickly responded to this by pricing in rate hikes.

Following the March MPC meeting, Arlingclose, the authority's treasury adviser, revised its central interest rate view and now predicts Bank Rate will be held at 3.75%. However, the conflict makes the outlook for rates highly uncertain. In the short-term the risks are to the upside with the chance of higher Bank Rate should the MPC decide it wishes to quickly quash potential second-round effects from higher inflation. Further out, if Bank Rate is hiked quickly, the pace and magnitude of subsequent cuts could take it far lower than was previously anticipated as policymakers add significant stimulus to a much weaker economic growth outlook.

The US Federal Reserve had been cutting rates over the period, reducing Fed Funds Rate target range by 0.25% at its December meeting to 3.50%-3.75%. At the three subsequent meetings, the rate was held at the same range. Policymakers noted that while inflation was elevated, economic activity had been expanding but the war with Iran made the path of monetary policy highly uncertain. Despite this, the Fed still suggested that further rate cuts were likely in 2026 and 2027.

The European Central Bank (ECB) has kept its key interest rates on hold since June 2025, maintaining the deposit rate at 2.0% and main refinancing rate at 2.15%. At its March 2026 meeting, the ECB noted the war in the Middle East had significantly increased uncertainty, creating upside risks for inflation and downside risks for growth, leading it to revise up its forecasts accordingly.

Financial markets

After declining sharply early in the financial year following the announcement of US tariffs, sentiment in financial markets had improved but equity and bond markets remained volatile throughout. However, the latter part of the period was dominated by the US/Israel war with Iran, which saw equity markets fall sharply, and bond yields rise as concerns over the inflationary impact from sharply higher oil and other commodity prices outweighed the flight-to-quality into government bonds often seen in conflicts.

Equity markets had been registering gains after the declines during the April sell-off, but the war reversed this and markets saw another sharp drawdown. Both the FTSE 100 and 250 fell by around 10% over the month from the start of the conflict to the end of the financial year.

The period saw significant volatility in gilt yields. The 10-year UK benchmark gilt yield started the year at 4.65% and ended at 4.86%. However, over this time the 10-year yield hit a low of 4.23% and a high of 4.95% in the space of a month. It was a similar picture for the 20-year gilt which started at 5.18% and ended at 5.45% with a low and high of 4.92% and 5.55% respectively. The Sterling Overnight Rate (SONIA) averaged 4.01% over the 12 months to 31st March.

Credit review

Arlingclose maintained its recommended maximum unsecured duration limit on most of the banks on its counterparty list at 6 months. The other banks remain on 100 days.

Earlier in the period, Fitch upgraded NatWest Group and related entities to AA- from A+ and placed Clydesdale Bank's long-term A- rating on Rating Watch Positive. Fitch later upgraded Clydesdale Bank and HSBC, but downgraded Lancashire CC and Close Brothers.

Moody's affirmed OP Corporate's rating at Aa3 In May 2025. Later in the period, Moody's upgraded Transport for London, Allied Irish Banks, Bank of Ireland, Toronto-Dominion Bank, DZ Bank, Nordea and HSBC and downgraded Close Brothers. In the last quarter of 2025 S&P upgraded Clydesdale Bank, Allied Irish Banks and Bank of Ireland, and assigned Warrington Council a BBB+ rating.

After spiking in April 2025 following the US trade tariff announcements, UK credit default swap (CDS) prices had trended down before picking up modestly in October and November. After declining again in December and into the new calendar year, they rose sharply once again when the war in the Middle East started. They were still elevated at the end of the period, but prices for all banks on Arlingclose's counterparty list remained within limits deemed satisfactory for maintaining credit advice at current durations.

Overall, European banks' CDS prices have generally been flatter and lower compared to the UK, as have Singaporean and Australian lenders while some Canadian bank CDS prices have remained elevated since the beginning of the period in part due to ongoing trade tensions with the US.

Financial market volatility is expected to remain, and CDS levels will 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.