Finance Committee

Date: **13 March 2024**

Item: **Treasury Activities, Policies and Strategies**

This paper will be considered in public

1 Summary

1.1 This paper provides a brief update on our key treasury activities for the period from 23 September 2023 to 23 February 2024 (the Reporting Period) including a summary of the proposed changes to the Treasury Management Policies and Strategies.

1.2 Appended are the proposed TfL Treasury Management Strategy (TMS) for 2024/25, the proposed TfL Treasury Management Policies (TMP) and the proposed TfL Group Policy Relating to the Use of Derivative Investments (Derivatives Policy), along with the proposed Places for London Limited (Places, TfL's property development company) Treasury Management Strategy (Places TMS) and the Places for London Treasury Management Policies (Places TMP).

1.3 Approval of these strategies and policies is within the authority of the Committee. The Committee is asked to exercise that authority in relation to each of the TfL and Places TMS, each of the TfL and Places TMP and the Derivatives Policy.

1.4 A paper is included on Part 2 of the agenda, which contains exempt supplemental information. The information is exempt by virtue of paragraph 3 of Schedule 12A of the Local Government Act 1972 in that it contains information relating to the financial affairs of TfL or of a sensitive nature to our listed counterparties. Any discussion of that exempt information must take place after the press and public have been excluded from this meeting.

2 Recommendations

2.1 The Committee is asked to note the paper and the exempt supplementary information on Part 2 of the agenda and:

(a) approve the proposed TfL Treasury Management Strategy (TMS) 2024/25, attached as Appendix 1 to this paper, including the Investment Strategy, the Borrowing Strategy, the Liquidity Strategy, the Risk Management Strategy;

(b) approve the proposed TfL Treasury Management Policies attached as Appendix 2 to this paper;

(c) approve the proposed TfL Group Policy Relating to the Use of Derivative Investments attached as Appendix 3 to this paper;

(d) approve the proposed Places for London Limited Treasury Management Strategy, attached as Appendix 4 to this paper, including the Borrowing Strategy; the Investment Strategy; the Liquidity Strategy and Banking and Cash Management explanation;

(e) approve the proposed Treasury Management Policies for Places for London Limited attached as Appendix 5 to this paper; and

(f) subject to the approval of the TMS 2024/25 and approval of the TfL Group Policy Relating to the Use of Derivative Investments (Derivatives Policy) by the Committee (pursuant to paragraph 2.1(c) above)), approve, pursuant to Section 49 of the Transport for London Act 2008 (as amended by the Transport for London Act 2016, together the Act), and in accordance with the Derivatives Policy for 2024/25, Transport for London Finance Limited (as a qualifying TfL subsidiary for the purposes of the Act) entering into derivative investment(s) in relation to:

(i) mitigating exchange rate risk related to specific currency exposures arising from the procurement of goods or services by any member of the TfL Group or grants or revenues payable in currencies other than Sterling to any member of the TfL Group in the ordinary course of business as soon as practicable once the quantum of exchange rate risk to any member of the TfL Group is established;

(ii) mitigating exchange rate risk arising from any TfL Group investments in foreign currencies and/or any TfL Commercial Paper (Euros or US Dollars) borrowing in accordance with the TMS 2024/25;

(iii) mitigating commodity rate and/or price risk related to specific commodity (including fuel and electricity) exposures arising from the procurement of goods or services by any member of the TfL Group in the ordinary course of business as soon as practicable once the quantum of commodity risk to any member of the TfL Group is established;

(iv) mitigating interest rate risk and if applicable currency risk related to any existing, imminent and future TfL Group borrowing (including any leases), once the borrowing has become certain and authorised in accordance with the TMS 2024/25; and

(v) mitigating inflation risk related to specific exposures arising from the procurement of goods or services by any member of the TfL Group once the quantum of inflation risk to any member of the TfL Group is established; and mitigating risk related to any index reflecting any of the above matters referred to in paragraphs 2.1(f)(i) to (iv) above.

3 Key Highlights

3.1 During the Reporting Period, we have complied at all times with each of the TfL TMS, the TfL TMP, the Derivatives Policy, the Places TMS and the Places TMP, each approved by the Committee on 8 March 2023. We have also complied with the Greater London Authority (GLA) Responsible Investment Policy approved by the Mayor on 25 April 2023.

3.2 In November 2023 Moody’s upgraded TfL’s long-term rating to A3 from Baa1, and the outlook has moved from Stable to Positive. Our ratings with S&P and Fitch have been affirmed and remain unchanged at A+ (Positive) and AA- (Negative).

3.3 Our ongoing collaboration with the GLA is progressing. We received approval from the GLA Group Collaboration Board in December 2023 for the design and to proceed with the implementation. The collaboration is expected to conclude in June 2024, at which point we expect to invest further in London Treasury Liquidity Fund LP (LTLF).

4 Liquidity Update

4.1 The TfL TMP state that, for prudent financial management purposes, TfL will aim to maintain a minimum level of cash reserves of at least 60 days’ worth of forecast annual operating expenditure. On average. 60 days’ worth of forecast annual operating expenditure is approximately £1.3bn for 2024/25. The Long-Term Funding Settlement agreed with Government in August 2022 requires that usable cash reserves are maintained at no more than £1.2bn on average, and no more than £1.3bn at the end of the financial year. We continue to balance these requirements by aiming to maintain our cash balances at around £1.2bn on average, however there will be occasions when our cash balances fall slightly below the 60 days aim stated by our Liquidity Policy. The Long-Term Funding Settlement ends in March 2024.

4.2 On 18 December 2023 the Department for Transport agreed to provide £250m capital funding to TfL for the 2024/25 financial year. Two tranches totalling £195m for this have already been received and the remaining £55m will be received in instalments by April 2024. There is no cash condition attached to this funding.

4.3 We remain confident that we retain sufficient liquidity to meet our financial obligations when they become due.

5 Investment Update

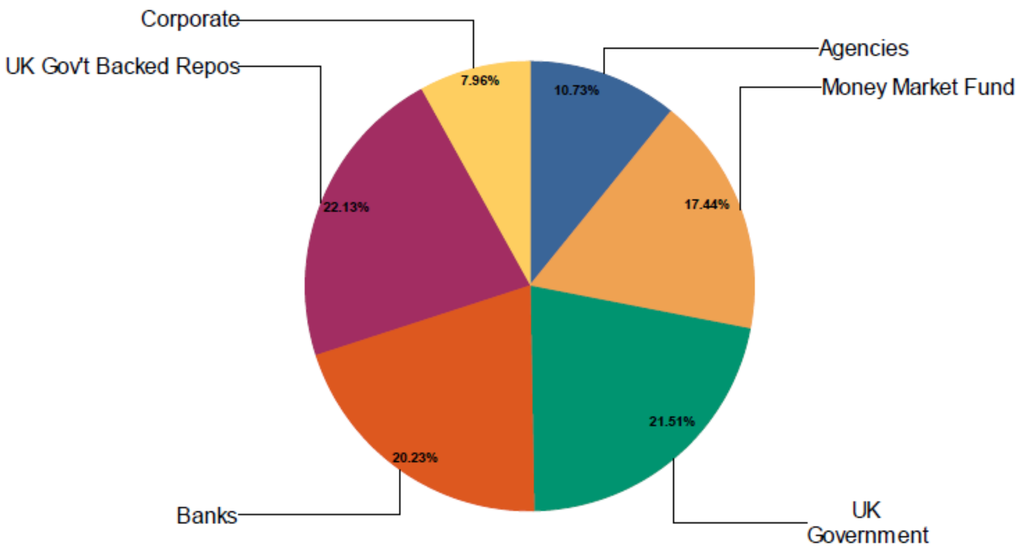
5.1 During the Reporting Period we have continued to diversify cash investments by country, sector, tenor, and counterparty. The maximum duration of investments has remained at three months. The Bank of England has continued to keep the base rate steady at 5.25 per cent over the Reporting Period.

5.2 Our investments remain short dated with 89.9 per cent maturing within two months. The weighted average maturity of investments over the Reporting Period increased from 18 days to 25 days.

5.3 The weighted average investment yield on 23 February 2024 was 5.28 per cent, nine basis points higher than the Sterling Overnight Index Average benchmark.

5.4 While we have continued to prioritise investments in short dated, highly rated instruments, we continue to seek opportunities to diversify the portfolio and maximise yield, within the bounds of our TMS and TMP. As of 23 February 2024, we held a diversified portfolio of investments in supra-nationals, government agencies and highly rated financial and corporate investments, as shown in Chart 1.

Chart 1 – Sector breakdown of TfL cash position on 23 February 2024



5.5 We continue to work with TfL's commercial property subsidiary, Places, to enable it to meet the requirements of its own Treasury Management Strategy and Policies, including the production of cash forecasts and depositing surplus cash. We plan to open Money Market Fund sub-accounts for Places before the end of this financial year, to allow for better diversification within their investments.

6 Risk Management Update

6.1 The level of floating rate borrowing, as a percentage of all borrowings outstanding, has increased slightly over the Reporting Period, from 6.6 per cent to 6.8 per cent. The level of floating rate borrowing is monitored and will move, within range during the Reporting Period according to cash flow needs, refinancings and the price and availability of floating rate debt. This increase has resulted primarily due to better access to commercial paper (CP). We remain comfortably within the maximum limit of 25 per cent set out in our TMS for 2023/24.

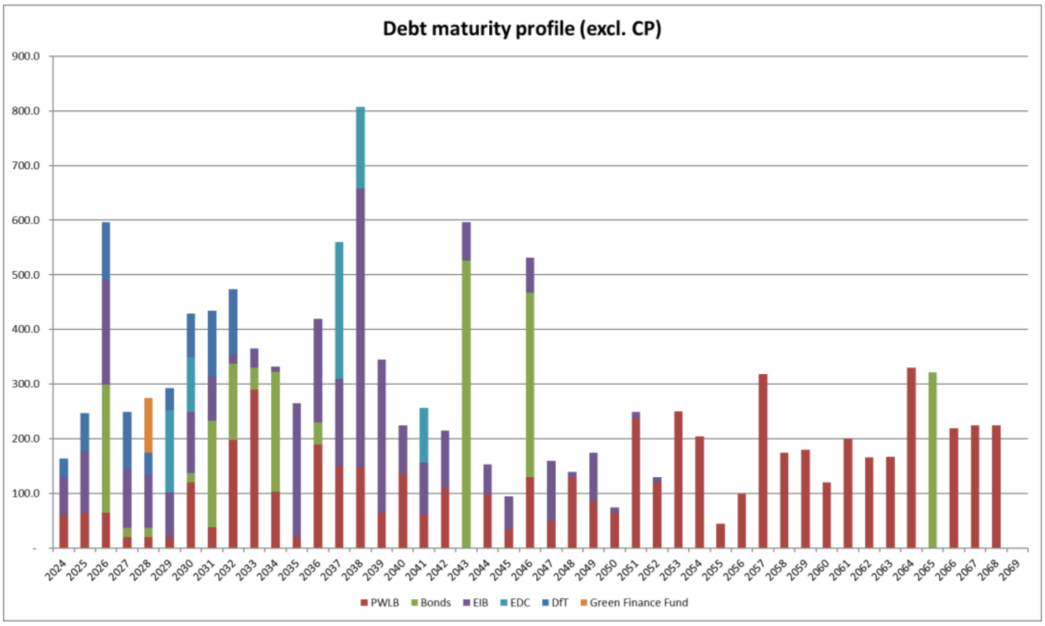
6.2 Although 6.8 per cent, or £874m, of total debt is exposed to floating interest rates, there is an element of natural hedge in the form of our short-term investments. This is because the income on those investments is also exposed to short-term interest rates. Therefore, a rise in interest rates on our floating rate debt is somewhat offset by a rise in interest receivable from our investment portfolio.

6.3 We continue to manage foreign exchange and interest rate risk, using derivatives to hedge material exposures relating to investments and commercial activities.

7 Borrowing Update

7.1 As of 23 February 2024, we had £12,784m in outstanding borrowing with an average tenor of 19 years and a weighted average interest rate of 3.46 per cent. We remained within the Authorised Limit for borrowing of £14,109m at all times during the Reporting Period. Chart 2 below shows our latest maturity profile.

Chart 2: Long-term debt maturity profile



7.2 We review the long-term debt maturity profile and ensure that debt maturities are spread evenly to avoid concentrated refinancing risk. Where we see large maturities, then we might seek to refinance these early, or forward hedge, to protect against interest rate risk or liquidity risk. We have added the maturity thresholds we observe to our TMP this year.

Euro and USD Commercial Paper

7.3 Historically TfL's borrowing has been restricted to GBP due to section 2(3) of the Local Government Act 2003, which provides that TfL, as a local authority for capital finance purposes, may not, without the consent of the Treasury, borrow otherwise than in sterling. On 5 December 2023, HM Treasury (HMT) granted permission for TfL to access short-term CP markets in Euros and US Dollars (USD).

7.4 The consent received from HMT will allow us to borrow in Euros and USD from CP markets and any such borrowing will be immediately swapped to a GBP equivalent in compliance with our risk management strategy. We have proposed some clarifications in our TMP and TMS in relation to this development.

GLA Green Finance Fund (GFF) borrowing - ULEZ loan

7.5 In October 2023 TfL entered into a £146.9m, four-year, loan agreement with the GLA as part of the GFF which provides debt finance to support the capital investment of carbon reduction and environmental projects. The loan facility will be drawn in two tranches and the rate of interest is fixed at the Public Works Loan Board (PWLB) Standard Fixed Interest Rate published, less 40 basis points. This is 20 basis points lower than the PWLB certainty rate that TfL has access to due to the competitive rate secured by the GLA for the GFF. We have drawn £100m under this agreement and expect to undertake a second drawdown to fund the remaining spend on the project in the near future.

Further GFF Applications

7.6 Following successful applications for additional green capital projects, further lending from the GFF has also been approved, subject to contract, to cover their capital costs. These projects support the Mayor's ambition for London to be net zero by 2030. The loan agreements are currently being drafted, so no loans have been disbursed yet. Borrowing undertaken from the GFF will form part of our annual borrowing plans, funding projects approved in our latest business plan. Where opportunities to fund projects outside the business plan are identified, these projects will be subject to affordability and financial tests to ensure TfL's affordability thresholds continue to be met.

UK Infrastructure Bank borrowing

7.7 In December 2023, TfL entered into a £300m loan agreement with the UK Infrastructure Bank (UKIB), which is our first loan agreement with them. The facility will be used to support the Docklands Light Railway rolling stock replacement programme. It has a three-year availability period and a tenor of around 40 years . Borrowing undertaken under this facility will form part of our annual borrowing plans. The interest rate is Gilts plus 40 basis points, representing a 40 basis point saving compared to the PWLB certainty rate.

Remaining 2023-2024 borrowing requirement

7.8 We expect to have £235m of long-term borrowing still to undertake before the end of 2023/24. This comprises £47m of incremental borrowing and £188m of refinancing. The £235m does not include refinancing of short-term borrowing, such as maturing CPs. We will continue to monitor our borrowing options and will draw on the most appropriate facility to meet our borrowing needs at the time.

8 Credit ratings

8.1 Our credit ratings as of 23 February 2024 are shown in the table below.

Table 1: TfL's credit ratings as of 23 February 2024

	Standard & Poor's	Moody's	Fitch
Long-term rating	A+	A3	AA-
Outlook	Positive	Positive	Negative
Short-term rating	A-1	P-2	F1+
Last update	25 May 2023 (affirmed)	23 November 2023 (upgraded)	10 January 2024 (affirmed)

8.2 We continued to engage with all three credit rating agencies during the Reporting Period. On 23 November 2023, Moody's upgraded the long-term rating for TfL to A3 from Baa1 and affirmed the short-term rating at P-2 (unchanged). The outlook has moved from stable to positive. This reflects TfL's improving operating performance, moderate capital programme following the completion of the Elizabeth line and more predictable funding arrangements with the government.

8.3 Fitch affirmed our ratings in January 2024. Our ratings with Fitch are the same as the UK sovereign ratings.

8.4 There have been no rating actions from S&P during the Reporting Period.

9 Banking

9.1 We have been working with our banking provider HSBC and outsourced partner BNP Paribas to build a new virtual bank account structure as part of the Places for London Limited Client Split Project. A new structure is required as 900 tenant deposit accounts and balances need to be transferred from Transport Trading Limited (TTL) to Places for London Limited. In November 2023 the new virtual account structure was added to the banking platform and 900 new virtual accounts were opened with their balances transferred to Places for London, meaning the tenants' deposits are being held in the now relevant entity. The project concluded in December 2023 when 900 virtual accounts in the old TTL hierarchy were closed.

9.2 We are working with our banking provider and Places to implement an automated direct debit mandate process for new tenants, where the paper mandates are no longer posted to the payer's bank to set up the direct debit instruction. Automated Direct Debit Instruction Service is the first step towards paperless direct debits and will allow the new mandate instructions to be processed directly to the bank by our outsourced partner. Moving to a new electronic solution makes it quicker, easier, safer and reduces the chance of human error in setting up the Direct Debit Instruction.

10 TfL Treasury Management Policies and Strategy

10.1 The Committee is asked to approve the TMS for 2024/25, the updated TMP and Derivatives Policy and the Places TMS and TMP, as proposed. These are detailed in Appendices 1-5 with tracked changes from last year with key highlights noted below.

10.2 We have moved the detail regarding counterparty exposure limits from the TMS to the TMP and Derivatives Policy. It should be noted that the limits themselves have not changed, only where the information is presented.

TfL Treasury Management Strategy 2024/2025

10.3 This highlights the proposed strategies for investment, borrowing, liquidity and risk management for the financial year 2024/25, as well as proposed counterparty exposure limits. It sets out TfL's borrowing requirement for 2024/25.

10.4 A key change this year is that as part of the ongoing collaboration with the GLA, we propose to further invest in the LTLF and propose to increase the investment counterparty limit from £10m to £900m. Investment above £10m will only be made once the full due diligence for GLA collaboration has concluded, including the finalisation of all the appropriate controls and documentation. We will seek further Committee approval before investing above £10m with LTLF.

10.5 On 5 December 2023, HM Treasury, pursuant to a consent requirement under the Local Government Act 2003 for any non-Sterling borrowing, confirmed permission for TfL to access short term CP markets in Euros and US Dollars. This enables TfL to undertake such non-Sterling borrowing for the first time. Therefore, we have amended our TMS to detail our approach to Euro and USD CP issuance for 2024/25.

10.6 All references to 'investments' in the TMS 2024/25 refer to investments held for treasury management purposes only and do not cover non-treasury and/or non-financial assets related investments, which will be covered in the Investment Management Strategy for non-financial assets, which is the subject of another item on this agenda.

10.7 In relation to the Risk Management Strategy, the proposals to the Committee for derivative investments set out in Recommendation 2.1(f) have been approved by the statutory and managing Chief Finance Officers, as required under the Derivatives Policy.

10.8 The TMS notes that TfL's borrowing requirement for 2024/25 is expected to be £717m, excluding rolling CP's as set out in the TMS. This amount consists of £247m maturing borrowing that TfL intends to refinance and £470m of incremental borrowing. We retain several options for refinancing during the year, including capital markets transactions, the PWLB, the UKIB, the GLA, other financial institutions and issuance under our CP programme.

TfL Treasury Management Policies

10.9 We have added additional detail on how we consider the maturity structure of new borrowing. The TMP is included as Appendix 2.

TfL Group Policy Relating to the Use of Derivative Investments

10.10 The Derivatives Policy must be reviewed annually. This is because prior to section 49 (power to plan for risk mitigation) of the Transport for London Act 2008 being enacted, TfL agreed with the House of Commons Committee considering the original TfL promoted Bill, that an annual policy on the use and governance of derivative investments entered into under section 49, would be put in place and approved annually.

10.11 The Derivatives Policy has been reviewed and updated to include the counterparty exposure limits for derivatives, which were previously included the TMS. The proposed policy can be found with tracked changes in Appendix 3.

Places for London Limited Treasury Management Strategy

10.12 In March 2023, the Places for London TMS was approved by the Committee. The Places TMS comprises the Places for London Borrowing Strategy; Investment Strategy; Liquidity Strategy and Banking and Cash Management. The Places TMS has been reviewed to reflect how the entity has evolved further since it was separated financially in April 2022. As the strategy has been updated slightly, it has been provided with tracked changes in Appendix 4.

Places for London Limited Treasury Management Policies

10.13 The Places TMP has been reviewed and no material changes have been made. It has been provided with tracked changes in Appendix 5.

List of appendices to this report:

Appendix 1: TfL Treasury Management Strategy

Appendix 2: TfL Treasury Management Policies

Appendix 3: TfL Group Policy Relating to the Use of Derivative Investments

Appendix 4: Places for London Limited Treasury Management Strategy

Appendix 5: Places for London Limited Treasury Management Policies

A paper containing exempt supplementary information is included on Part 2 of the agenda.

List of background papers:
None

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