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AUDIT COMMITTEE/ EXECUTIVE / COUNCIL

Portfolio Area: Resources

Date: **6 September 2023 / 20 September 2023 / 18 October 2023**

ANNUAL TREASURY MANAGEMENT REVIEW 2022/23 AND PRUDENTIAL INDICATORS

NON-KEY DECISION

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1 PURPOSE

1.1 To review the operation of the 2022/23 Treasury Management and Investment Strategy.

2 RECOMMENDATIONS

2.1 Audit Committee

That, subject to any comments by the Audit Committee to the Executive, the 2022/23 Annual Treasury Management Review be recommended to Council for approval.

2.2 Executive

That, subject to any comments made by the Executive, in addition to those made by the Audit Committee, the 2022/23 Annual Treasury Management Review be recommended to Council for approval.

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2.3 Council

That, subject to any comments from the Audit Committee and the Executive, 2022/23 Annual Treasury Management Review be approved.

3 BACKGROUND

3.1 Regulatory Requirement

3.1.1 The Council is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2022/23. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management, (the Code), and the CIPFA Prudential Code for Capital Finance in Local Authorities, (the Prudential Code).

3.1.2 During 2022/23 the minimum reporting requirements were that the Council should receive the following reports:

- an annual treasury strategy in advance of the year (Council 24 February 2022)
- a mid-year treasury update report (Council 14 December 2022)
- an annual review following the end of the year describing the activity compared to the strategy (this report).

3.1.3 In December 2017, CIPFA revised the Code to require, all local authorities to report on:

- a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services;
- an overview of how the associated risk is managed; and
- the implications for future financial sustainability.

These elements are covered in the annual Capital Strategy reported to Council in February each year.

3.1.4 The regulatory environment places responsibility on Members for the review and scrutiny of treasury management policy and activities. This report is, therefore, important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by Members.

3.1.5 This report summarises:

- Capital activity during the year;
- Impact of this activity on the Council's underlying indebtedness (the Capital Financing Requirement);
- The actual prudential and treasury indicators;
- Overall treasury position identifying how the Council has borrowed in relation to this indebtedness, and the impact on investment balances;
- Summary of interest rate movements in the year;
- Detailed debt activity; and
- Detailed investment activity.

3.1.6 Officers confirm that they have complied with the requirement under the Code to give prior scrutiny to all of the above treasury management reports by the Audit Committee and the Executive before they were reported to the Council.

3.2 Executive Summary

3.2.1 During 2022/23, the Council complied with its legislative and regulatory requirements. The key actual prudential and treasury indicators detailing the impact of capital expenditure activities during the year, with comparators, are as follows:

Table 1

Prudential and treasury indicators	31.3.22 Actual £000	2022/23 Original £000	31.3.23 Actual £000
Capital expenditure			
GF	24,106	30,510	17,814
HRA	36,727	64,666	43,966
Total	**60,833**	**95,176**	**61,780**
Capital Financing Requirement:			
GF	46,366	45,802	49,733
HRA	258,581	277,784	264,585
Total	**304,947**	**323,586**	**314,318**
Gross borrowing	**234,820**	**285,304**	**235,057**
Investments			
• Longer than 1 year	7,300	7,300	2,300
• Under 1 year	61,450	40,435	40,985
• Total	68,750	47,732	43,285
Net borrowing	**166,070**	**237,572**	**191,772**

Other prudential and treasury indicators are to be found in the main body of this report. The Chief Finance Officer also confirms that borrowing (internal and external) was only undertaken for a capital purpose and the statutory borrowing limit (the authorised limit) was not breached.

3.2.2 It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. During the year the Council has operated within the treasury and prudential indicators set out in the Council’s Treasury Management Strategy Statement for 2022/23.

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

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4 THE COUNCIL'S CAPITAL EXPENDITURE AND FINANCING

4.1.1 Capital expenditure[1] can be financed either by capital resources the Council has on its balance sheet (e.g. capital receipts and capital grants) or by making a revenue contribution to capital. If sufficient capital resources are not available to fund the expenditure the Council would need to borrow to meet the funding gap. This borrowing may be taken externally in new loans or internally from cash balances held by the Council. The need to borrow is measured and reported through the Prudential Indicators.

4.1.2 The actual capital expenditure forms one of the required prudential indicators. The table below shows the actual capital expenditure and how this was financed.

Table 2

2022/23 Capital Expenditure and Financing			
	31.3.22 **£'000**	**2022/23 Working Budget** **£'000**	**31.3.23** **£'000**
General Fund			
Capital Expenditure:	24,106	23,927	17,814
Financed excluding borrowing	(11,743)	(23,927)	(12,928)
Unfinanced capital expenditure (borrowing)	**12,363**	**0**	**4,886**
HRA			
Capital Expenditure:	36,727	42,338	43,966
Financed excluding borrowing	(11,730)	(42,338)	(39,392)
Unfinanced capital expenditure (borrowing)	**24,997**	**0**	**4,574**

4.2 THE COUNCIL'S OVERALL BORROWING NEED

4.2.1 The Council's underlying need to borrow to finance capital expenditure is termed the Capital Financing Requirement (CFR). It represents the amount of debt it needs to/has taken out to fund the capital programme (and includes both internal and external borrowing). The CFR is then reduced as debt repayments are made and Minimum Revenue Provisions are made. A separate CFR is calculated for the General Fund and Housing Revenue Account and any transfers of assets (such as land or buildings) between the two accounts will impact on each fund's CFR. The CFR will go up on the fund "receiving" the assets and go down (by the same amount) on the fund "giving" the asset.

4.2.2 The Council's 2022/23 Minimum Revenue Provision Policy (MRP), as required by DLUHC Guidance, was approved as part of the Treasury Management Strategy Report for 2022/23 on 24 February 2022.

[1] Council expenditure can be classified as capital when it is used to purchase assets with a life of more than one year, exceeds £5,000 in value and meets the guidelines laid out in CIPFA accounting practices.

The MRP charged to the General Fund in 2022/23 was £214,609 of which:

- £35,119 is funded from investment property
- £48,787 is funded by the Garage Improvements Programme
- £130,703 is a net cost to the General Fund

4.2.3 The Council's CFR for the year is shown below, and represents a key prudential indicator. It includes finance leases included on the balance sheet, which increase the Council's borrowing need. No borrowing is actually required against these schemes as a borrowing facility is included in the contract.

Prudential Indicator – Capital Financing Requirement
Table 3

CFR (£'000): General Fund	31.3.22 Actual	2022/23 Budget	31.3.23 Actual
Opening balance *	35,516	37,920	46,366
Add: unfinanced capital expenditure (as above)	12,363	8,448	4,886
Less:			
Unfinanced capital expenditure from prior years now financed	(757)		(510)
MRP	(195)	(473)	(215)
Finance lease repayments	(561)	(93)	(239)
Appropriations to / from HRA	0	0	(540)
Other	0	0	(15)
Closing balance	**46,366**	**45,802**	**49,733**

* Includes a £11Million technical adjustment for Queensway LLP and £7Million of Local enterprise Partnership (LEP) loans.

CFR (£'000): HRA	31.3.22 Actual	2022/23 Budget	31.3.23 Actual
Opening balance	233,093	262,144	258,581
Add:			
Unfinanced capital expenditure (as above)	24,997	15,640	4,574
New finance lease	491	0	890
Appropriations to / from GF	0	0	540
Closing balance	**258,581**	**277,784**	**264,585**

4.2.4 Borrowing activity is constrained by prudential indicators for gross borrowing and the CFR, and by the authorised limit.

4.3 Limits to Borrowing Activity

4.4 Gross borrowing and the CFR - in order to ensure that borrowing levels are prudent over the medium term and only for a capital purpose, the Council should ensure that its gross external borrowing does not, except in the short term, exceed the total of the capital financing requirement in the preceding year (2022/23) plus the estimates of any additional capital financing requirement for the current (2023/24) and next two financial years. This essentially means that the Council is not borrowing to support revenue expenditure. This indicator allowed the Council some flexibility to borrow in advance of its immediate capital needs in 2022/23. The table below highlights the Council's gross borrowing position against the CFR. The Council has complied with this prudential indicator.

Table 4

	31.3.22 Actual £'000	2022/23 Budget £'000	31.3.23 Actual £'000
Gross borrowing position	£234,820	£285,304	£235,057
CFR	£304,947	£323,586	£314,318
(Under) / over funding of CFR	**(£70,127)**	**(£38,282)**	**(£79,261)**

4.5 The **authorised limit** - the authorised limit is the "affordable borrowing limit" required by s3 of the Local Government Act 2003. Once this has been set, the Council does not have the power to borrow above this level. The table below demonstrates that during 2022/23 the Council has maintained gross borrowing within its authorised limit.

4.6 The **operational boundary** – the operational boundary is the expected borrowing position of the Council during the year. Periods where the actual position is either below or over the boundary are acceptable subject to the authorised limit not being breached.

4.7 **Actual financing costs as a proportion of net revenue stream** - this indicator identifies the trend in the cost of capital, (borrowing and other long term obligation costs net of investment income), against the net revenue stream.

Table 5

Authorised limits	**HRA 2022/23 £m**	**GF 2022/23 £m**
Authorised limit	280	82
Maximum gross borrowing position during the year	226	9
Operational boundary	268	67

Authorised limits	**HRA 2022/23 £m**	**GF 2022/23 £m**
Average gross borrowing position	226	9
Financing costs as a % of net revenue stream	17%	6%

4.8 TREASURY MANAGEMENT ACTIVITIES

4.9 TREASURY POSITION AS AT 31 MARCH 2023

4.9.1 The Council's treasury management debt and investment position is organised by the treasury management service in order to ensure adequate liquidity for revenue and capital activities, security for investments and to manage risks within all treasury management activities. Procedures and controls to achieve these objectives are well established both through Member reporting detailed in the summary, and through officer activity detailed in the Council's Treasury Management Practices.

4.9.2 At the end of 2022/23 the Council's treasury position (excluding finance leases), was as follows:

Table 6

Treasury Position						
	2021/22			**2022/23**		
	31 March 2022 Principal £'000s	**Rate / Return %**	**Average Life (Yrs)**	**31 March 2023 Principal £'000s**	**Rate / Return %**	**Average Life (Yrs)**
PWLB Borrowing	227,750	3.28	13	227,487	3.28	12
Other Borrowing (LEP)	7,070	0	8	7,570	0	7
Total Debt	**234,820**			**235,057**		
Capital Financing Requirement	304,947			314,318		
Total Investments	79,930			55,241		
Over/(Under) borrowing	**9,803**			**(24,020)**		

The maturity structure of the debt portfolio was as follows:

Table 7

Debt Maturity Structure	31.3.22 Actual £'000	2022/23 original limits £'000	31.3.23 Actual £'000
Within 1 Year	0		0
Over 1 not over 2 years	263		500
Over 2 not over 5 years	15,570		26,026

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Debt Maturity Structure	31.3.22 Actual £'000	2022/23 original limits £'000	31.3.23 Actual £'000
Over 5 not over 10 years	57,656		64,700
Over 10 not over 15 years	99,963		100,663
Over 15 not over 20 years	51,811		37,658
Over 20 not over 30 years	4,557		5,510
Over 30 years	5,000		0
Total Debt	**234,820**	**362,503**	**235,057**

Investment Portfolio	31.3.22 Actual £000	31.3.22 Actual %	31.3.23 Actual £000	31.3.23 Actual %
Treasury investments – all managed in house				
Banks and Building Societies	55,000	80%	26,600	61%
Local authorities	7,300	11%	7,300	17%
Money Market Funds	6,450	9%	9,402	22%
Total treasury investments	**68,750**	**100%**	**43,302**	**100%**

Non-Treasury investments				
Subsidiaries	11,180	100%	11,939	100%
Total Non-Treasury Investments	**11,180**	**100%**	**11,939**	**100%**
Treasury investments	68,750	86%	43,302	78%
Non-Treasury investments	11,180	14%	11,939	22%
Total of all Investments	**79,930**	**100%**	**55,241**	**100%**

The maturity structure of the investment portfolio was as follows:

Table 8

Investment Maturity Structure	31.3.22 Actual £000	31.3.23 Actual £000
Within 1 Year	61,451	41,003
Longer than 1 year	18,479	14,238
Total Investments	**79,930**	**55,241**

4.9.3 In addition to the PWLB borrowing, the General Fund also has loans from the Local Enterprise Partnership (LEP) in relation to regeneration activities. Subject to discussion, these loans (£7,570k) are repayable, £500k in 2025 and the balance in 2030.

4.9.4 The non-treasury loan to the subsidiary is the loan made to Marshgate LTD (WOC), for the purchase and development of housing within the Borough in 2021/22 and 2022/23.

4.9.5 The fall in the treasury investment balances of £25m between 31 March 2022 and 31 March 2023 mainly reflects the use of internal borrowing to fund the capital programme rather than borrowing externally over the two years to 31 March 2023.

4.10 TREASURY MANAGEMENT STRATEGY 2022/23

4.10.1 The Treasury Management Strategy was approved by Council on 24 February 2022.

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

4.11 Borrowing

4.11.1 During 2022/23, the Council maintained an under-borrowed position and no new external borrowing was taken during the year. This meant that the capital borrowing need, (the Capital Financing Requirement), was not fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow was used as an interim measure. This strategy was prudent as interest rates on investments were initially low and this also minimised counterparty risk.

4.11.2 The policy of avoiding new borrowing by running down spare cash balances has served the Council well over the last few years. However, this has been kept under review to avoid incurring higher borrowing costs in the future when the Council may not be able to avoid new borrowing to finance capital expenditure and/or the refinancing of maturing debt. The Council has taken some limited borrowing in 2023/24 to ensure the Council's cashflow position is resilient and to ensure that if interest rates increase, large amounts of borrowing required are not all taken at higher rates.

4.11.3 Interest rate forecasts were initially suggesting only gradual rises in short, medium and longer-term fixed borrowing rates during 2022/23 but by August it had become clear that inflation was moving up towards 40-year highs, and the Bank of England engaged in monetary policy tightening at every Monetary Policy Committee meeting during 2022, and into 2023, either by increasing Bank Rate by 0.25% or 0.5% each time. Currently the CPI measure of inflation has fallen back to 6.8% by July 2023 in the UK but is expected to fall back towards 4% by year end. Nonetheless, there remain significant risks to that central forecast.

4.11.4 The PWLB certainty rate is gilts plus 80bps. During the year, gilt yields rose from the start of 2021, peaking in the autumn of 2022.

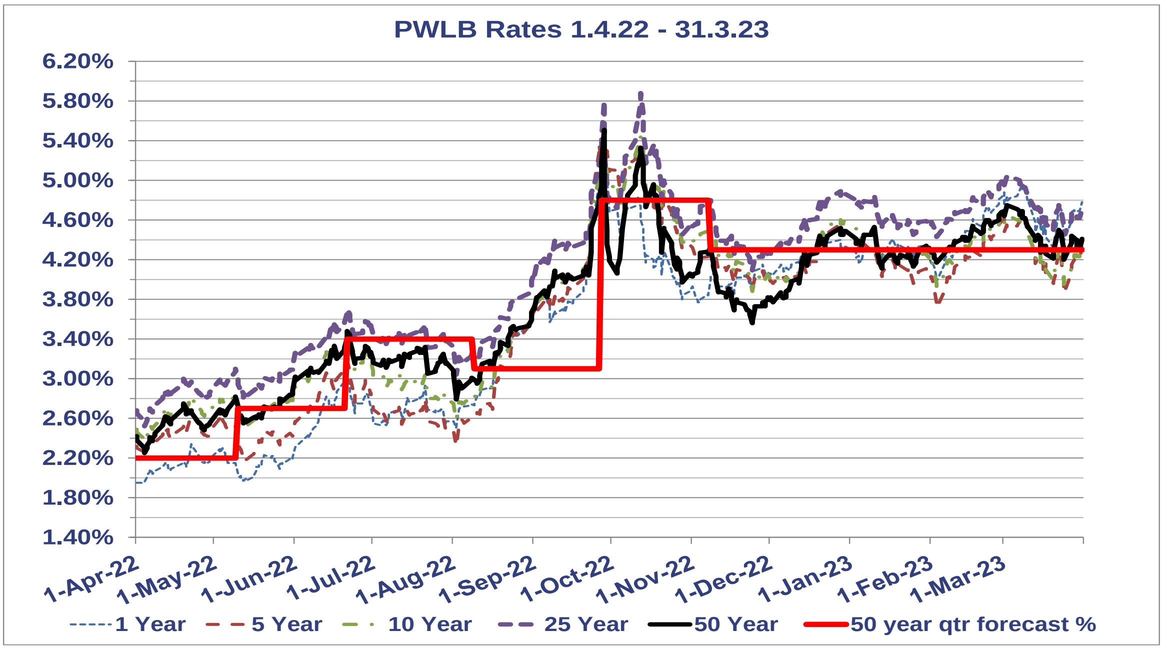
4.11.5 There is likely to be a fall in gilt yields and PWLB rates across the whole curve over the next one to two years as Bank Rates first rise to dampen inflationary pressures and is then cut as the economy slows, unemployment rises, and inflation (on the Consumer Price Index measure) moves closer to the Bank of England's 2% target.

4.11.6 As a general rule, short-dated gilt yields will reflect expected movements in Bank Rate, whilst medium to long-dated yields are driven primarily by the inflation outlook.

4.11.7 The Bank of England is also embarking on a process of Quantitative Tightening. The gradual reduction of the Bank's original £895Billion stock of gilt and corporate bonds will be sold back into the market over several years. The impact this policy will have on the market pricing of gilts, while issuance is markedly increasing, is an unknown at the time of writing.

4.11.8 The Chart below shows the volatility of the PWLB borrowing rates from 1 April 2022 to 31 March 2023.

PWLB RATES 2022/23
Chart 1



4.12 BORROWING OUTTURN

4.12.1 No new borrowing was undertaken during the year

4.12.2 Interest paid on PWLB borrowing during the year was £ 7,339,321 – Housing Revenue Account (HRA) and £44,188 - General Fund (GF)

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4.13 ANNUAL INVESTMENT STRATEGY

4.13.1 The Treasury Management Strategy Statement (TMSS) for 2022/23, which includes the Annual Investment Strategy, was approved by the Council on 24 February 2022. 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

4.13.2 There were no breaches to this policy in the year to 31 March 2023 with the investment activity conforming to the approved strategy. The Council had no liquidity difficulties and no funds have been placed with the Debt Management Office (DMO), demonstrating that counterparty limits and availability for placing funds approved in the TM Strategy were working effectively. It is possible that surplus funds that may be borrowed during 2022/23 will be placed in the DMO temporarily, if PWLB borrowing rates are advantageous and cash balances due to timing of taking out new loans would breach other counterparty limits.

4.13.3 The Specified and Non-Specified Investment Criteria (Appendix C) have been reviewed and updated in the Treasury Management Strategy 2022/23 agreed at Full Council in February 2022. Appendix C reflects the strategy in place for 2022/23. No further amendments are proposed at this stage.

4.13.4 In accordance with the Treasury Management Strategy, the Council invests its surplus cash balances that are committed for future approved spending. The policy sets out the approach for choosing investment counterparties, and is based on credit ratings provided by the three main credit rating agencies, supplemented by additional market data and counterparty limits dependant on level of cash balances held.

4.14 Investment performance year to date as of 31 March 2023

4.14.1 The Council's current investment portfolio consists of "conventional" cash investments: deposits with banks and building societies, Money Market Funds and loans to other Local Authorities. No investments have been made with any of the other approved instruments within the Specified and Non-specified Investment Criteria (see Appendix D).

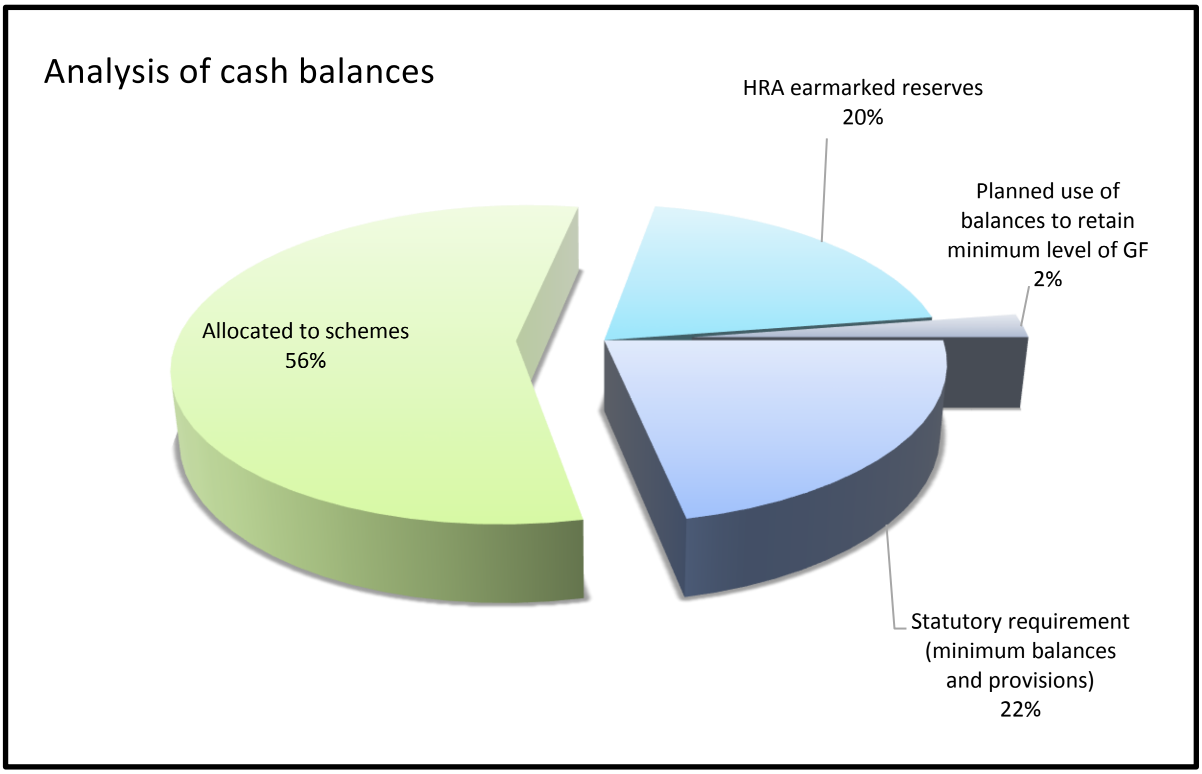
4.14.2 The average level of funds available for investment purposes during the year was £67Million, earning an average interest rate of 1.79%. Interest earned to 31 March 2023 was £1.2Million on treasury investments, against an original budget of £330K, contributing to General Fund (£363K) and Housing Revenue Account revenue income (£845K). Investment interest rates have since significantly increased with the movement in the Bank of England base rate and are now predicted to be an average 5.18% for 2023/24.

4.14.3 The Council's balances are made up of cash reserves e.g. HRA and General Fund balances, restricted use receipts e.g. right to buy one for one receipts and balances held for provisions such as business rate appeals.

4.14.4 In considering the Council's level of cash balances, Members should note that the General Fund MTFS and Capital Strategy have a planned use of resources over a minimum of 5 years and the HRA Business Plan (HRA BP) a planned use of resources over a 30 year period, which means, while not committed in the current year, they are required in future years.

4.14.5 The following chart shows the planned use of cash balances as at 31 March 2023.

Chart 2



4.14.6 The restrictive use of a proportion of the cash balances set out above, plus the planned use of resources in line with the Council's capital and revenue strategies mean that the investment balance of £43Million as at 31 March 2023 is not available for new expenditure.

4.14.7 **Other Prudential Indicators**

4.14.8 The ratio of financing costs to net revenue stream is equal to General Fund interest costs divided by the General Fund net revenue income from Council tax, Revenue Support Grant and retained business rates. The 2022/23 indicator is an average of 15.26% (General Fund 5.52%, HRA 17.18%). This means the cost of borrowing represents a small proportion of the General Fund's core resources but a larger portion of HRA resources.

5 IMPLICATIONS

5.1 Financial Implications

5.1.1 This report is of a financial nature and reviews the treasury management function for 2022/23. Any consequential financial impacts identified in the Capital strategy and Revenue budget monitoring reports have been incorporated into this report.

5.1.2 During the financial year Officers operated within the treasury and prudential indicators set out in the Council's Treasury Management Strategy Statement and in compliance with the Council's Treasury management practices.

5.2 Legal Implications

5.2.1 Approval of the Prudential Code Indicators and the Treasury Management Strategy are intended to ensure that the Council complies with relevant legislation and best practice.

5.2.2 There have been no changes to PWLB borrowing arrangements since the last Treasury report, however there are changes to the Prudential and Treasury Management codes from 2023/24. Officers will ensure that any changes are reflected in treasury operations and reporting requirements**.**

5.3 Risk Implications

5.3.1 The current policy of minimising external borrowing only remains financially viable while cash balances are high and the differentials between investment income and borrowing rates, although reducing still remain. As these conditions change the Council may need to take borrowing at higher rates which would increase revenue costs.

5.3.2 The Council's Treasury Management Strategy is based on limits for counterparties to reduce risk of investing with only a small number of institutions.

5.3.3 The thresholds and time limits set for investments in the Strategy are based on the relative ratings of investment vehicles and counter parties. These are designed to take into account the relative risk of investments and also to preclude certain grades of investments and counterparties to prevent loss of income to the Council.

5.3.4 There is a risk to the HRA BP's ability to fund the approved 30 year spending plans if interest rates continue to rise, this will be included in the revision to the BP in 2023.

5.4 Equalities and Diversity Implications

5.4.1 This report is technical in nature and there are no implications associated with equalities and diversity within this report. In addition to remaining within agreed counterparty rules, the council retains the discretion not to invest in countries that meet the minimum rating but where there are concerns over human rights issues. Counterparty rules will also be overlaid by any other ethical considerations from time to time as appropriate.

5.4.2 The Treasury Management Policy does not have the potential to discriminate against people on grounds of age; disability; gender; ethnicity; sexual orientation; religion/belief; or by way of financial exclusion. As such a detailed Equality Impact Assessment has not been undertaken.

5.5 Climate Change Implications

5.5.1 The Council's investment portfolio is sterling investments and not directly in companies. However, the Treasury Management (TM) team continue to review the use of Money Market funds to ensure, where possible, money market funds that invest in environmentally sustainable companies are used. In this way the TM team aligns with the Council's ambition to attempt to be carbon neutral by 2030.

BACKGROUND PAPERS

- BD1 Treasury Management Strategy including Prudential Code Indicators 2022/23 (Council 24 February 2022)

APPENDICES

- Appendix A - Investment and Borrowing Portfolio
- Appendix B - Specified and Non-Specified Investment Criteria
- Appendix C - Link detailed Economy and Interest rates review
- Appendix D - Counterparty List 31 March 2023