Audit Committee		Agenda Item:
Meeting Date	25 July 2022	
Report Title	Annual Treasury Management Report 2021/22	
EMT Lead	Lisa Fillery, Director of Resources	
Head of Service	Phil Wilson, Head of Finance and Procurement	
Lead Officers	Phil Wilson, Head of Finance and Procurement and Olga Cole, Management Accountant	
Classification	Open	

Recommendations	1. Approve the Treasury Management stewardship report for 2021/22.
	2. Approve the Prudential and Treasury Management Indicators within the report.

1. Purpose of Report and Executive Summary

1.1 The Council's Treasury Management activity is underpinned by the Chartered Institute of Public Finance and Accountancy's (CIPFA's) Code of Practice on Treasury Management ("the Code"), which requires local authorities to produce annual Prudential Indicators and a Treasury Management Strategy Statement on the likely financing and investment activity. The Code also recommends that members are informed of Treasury Management activities at least twice a year. The latest version of the Code was adopted by the Council in February 2021.

1.2 Treasury Management is defined as "the management of the Council's 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". No Treasury Management activity is without risk; the effective identification and management of risk are integral to the Council's Treasury Management objectives.

1.3 For 2021/22 the Investments Section of the Kent County Council (KCC) Finance Department had operational responsibility for the daily treasury management duties. KCC Finance in undertaking this work had to comply with this Council's Treasury Management Strategy. Overall responsibility for Treasury Management remained with the Council.

1.4 This report:

- is prepared in accordance with the CIPFA Treasury Management Code and the Prudential Code;
- details the implications of treasury decisions and transactions;
- gives details of the outturn position on Treasury Management transactions in 2021/22; and
- confirms compliance with Treasury limits and Prudential Indicators.

1.5 This report will be submitted to Council on 12 October 2022.

2. Background

Borrowing Requirement and Debt Management

2.1 The overall borrowing position is summarised below:

	Balance on 31/3/2021 £'000	**Movement in Year £'000**	**Balance on 31/3/2022 £'000**
Capital Financing Requirement	48,373	(599)	47,774
External Borrowing	(15,000)	5,000	(10,000)
Cumulative External Borrowing Requirement	**33,373**	**4,401**	**37,774**

2.2 Where capital expenditure is to be financed in future years by charges to revenue as assets are used by the Council, the expenditure results in an increase in the Capital Financing Requirement (CFR), a measure of the capital expenditure incurred historically by the Council that has yet to be financed.

2.3 The reason for the reduction in the CFR in 2021/22 is due to the Minimum Revenue Provision offsetting the capital spend funded from borrowing.

2.4 The table below summarises the Council's borrowing portfolio from other local authorities at 31 March 2022.

Local Authority	**Loan Value £'000**	**Borrowing Rate**	**Duration of the Loan**	**Borrowing Date**	**Loan Repayment Date**
Derbyshire County Council	5,000	0.30%	1 year	08/04/2021	07/04/2022
London Borough of Islington	5,000	0.40%	1 year	28/02/2022	27/02/2023

Investment Activity

2.5 The Council holds significant investment funds, representing income received in advance of expenditure plus balances and reserves held. During 2021/22, the Council held average daily cash balances of £38 million (£38 million for 2020/21).

2.6 The Council's budgeted investment income for 2021/22 was £168,770 and the actual income received was £114,600, of which £106,000 was from the Council's long-term investment in the Church, Charities and Local Authorities (CCLA) Mutual Investment Property Fund.

2.7 The table below summarises the Council's investment portfolio at 31 March 2022. All investments made were in line with the Council's approved credit rating criteria at the time of placing the investment, and still met those criteria at 31 March 2022.

Counterparty (MMF = Money Market Funds)	**Long-Term Rating**	**Balance Invested at 31 March 2022 £'000**
Invesco MMF	AAAmmf	735
Goldman Sachs MMF	AAAmmf	3,000
SSgA MMF	AAAmmf	3,000
Morgan Stanley MMF	AAAmmf	3,000
Black Rock MMF	AAAmmf	3,000
Aberdeen MMF	AAAmmf	3,000
Debt Management Office	AA-	7,600
CCLA Property Fund	unrated	3,000
Total		**26,335**

2.8 The ratings above are from Fitch credit rating agency. A description of the grading is provided below:

- AAAmmf: Funds have very strong ability to meet the dual objectives of providing liquidity and preserving capital.
- AA-: Expectations of very low default risk

2.9 The treasury management position for the year is summarised below:

Investments	Balance on 31/03/21 £'000	Movement in Year £'000	Balance on 31/03/22 £'000	Average Rate at 31/03/22 %
Cash and Cash Equivalents	20,115	(4,380)	15,735	0.52
Short-Term Investments	0	7,600	7,600	0.41
Long-Term Investments	3,000	0	3,000	3.54
TOTAL INVESTMENTS	**23,115**	**3,220**	**26,335**	
Borrowing				
Short-Term Borrowing	(15,000)	5,000	(10,000)	0.35%
TOTAL BORROWING	**(15,000)**	**5,000**	**(10,000)**	

2.10 The long-term investment shown in the table above is the Council's investment in the CCLA Property Fund.

2.11 In keeping with the Department for Levelling Up, Housing and Communities (DLUHC) Guidance on Investments, the Council maintained a sufficient level of liquidity through the use of Money Market Funds, overnight deposits and the use of call accounts.

2.12 The Council sought to optimise returns commensurate with its objectives of security and liquidity.

2.13 The criteria applied by the Director of Resources for the approval of a counter party for deposits are:

- credit rating - a minimum long-term of A-;
- credit default swaps;
- share price;
- reputational issues;
- exposure to other parts of the same banking group; and
- country exposure.

2.14 The investments permissible by the 2021/22 Treasury Strategy were:

Counterparty	Cash Limits
The UK Government (Debt Management Account Deposit Facility) and Treasury Bills	Unlimited
Local Authorities and other government entities	£3m
Major UK banks / building societies. (Barclays, HSBC, Lloyds Banking Group, RBS Group, Santander UK, Nationwide, Standard Chartered) unsecured deposits	£3m

Counterparty	Cash Limits
Svenska Handelsbanken unsecured deposits	£3m
Leeds Building Society unsecured deposits	£1.5m
Close Brothers unsecured deposits	£1.5m
Money Market Funds	£3m each
Strategic Pooled Funds e.g. Absolute return, Equity income, Corporate Bond Funds	£3m each
CCLA Property Fund	£3m
Supranational Bonds	£3m in aggregate
Corporate Bonds	£3m in aggregate
Covered Bonds	£3m in aggregate with £1m limit per bank
Non treasury investments	To be agreed on a case by case basis

2.15 This administration takes the view that the Capital Strategy should reflect the following principles:

- investing in sustainable, affordable and social housing to increase overall supply;
- using the ability to borrow at low rates of interest for the benefit of the physical and social infrastructure of the borough and for broader social value; and,
- ensuring that the costs of borrowing are manageable long term within the revenue budget

2.16 The maximum permitted duration for deposits is 13 months. For 2021/22 the Director of Resources in consultation with the Leader and Cabinet Member for Finance could consider longer duration. Bonds could have been purchased with a maximum duration of five years.

2.17 The definition of investments in CIPFA's revised 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. At 31 March 2022 the Council held £4.03 million of a longstanding portfolio of 13 investment properties within the borough. These investments generated £0.2 million of investment income for the Council in 2021/22 after taking account of direct costs, representing a rate of return of 5.2%.

External Context

2.18 The continuing economic recovery from coronavirus pandemic, together with the war in Ukraine, higher inflation, and higher interest rates were major issues over the period.

2.19 In its March interest rate announcement, the Monetary Policy Committee (MPC) noted that the invasion of Ukraine had caused further large increases in energy and other commodity prices, with the expectation that the conflict will worsen supply chain disruptions around the world and push CPI inflation to around 8% later in 2022, even higher than forecast only a month before in the February MPC. The Committee also noted that although Gross Domestic Product (GDP) in January was stronger than expected with business confidence holding up and the labour market remaining robust, consumer confidence had fallen due to the squeeze in real household incomes.

2.20 The Government's jobs furlough scheme insulated the labour market from the worst effects of the pandemic. The labour market began to tighten and demand for workers grew strongly as employers found it increasingly difficult to find workers to fill vacant jobs.

2.21 With the fading of lockdown activity in consumer-facing sectors improved substantially as did sectors such as oil and mining with the reopening of oil rigs but materials shortages and the reduction in the real spending power of households and businesses dampened some of the growth momentum. The annual growth rate was revised down slightly to 7.4% (from 7.5%) following a revised 9.3% fall in 2020.

2.22 Bank Rate was 0.1% at the beginning of the reporting period, increased to 0.25% in December 2021, the Bank of England raised it further to 0.50% in February 2022 and 0.75% in March 2022.

Credit Review

2.23 The outlook on a number of UK banks and building societies on the Council's counterparty list was revised upwards by Fitch and Moody's to 'stable', recognising their improved capital positions compared to 2020 and better economic growth prospects in the UK.

2.24 The successful vaccine rollout programme was credit positive for the financial services sector in general and improved the economic outlook.

2.25 Having completed its full review of its credit advice on unsecured deposits, in September Arlingclose extended the maximum duration limit for UK bank entities on its recommended lending list from 35 days to 100 days; a similar extension was advised in December for the non-UK banks on this list. As ever, the institutions and durations on the Council's counterparty list recommended by Arlingclose remains under constant review.

Revised CIPFA Codes, Updated PWLB Lending Facility Guidance

2.26 In August 2021 HM Treasury significantly revised guidance for the PWLB lending facility with more detail and 12 examples of permitted and prohibited use of PWLB loans. Authorities that are purchasing or intending to purchase investment assets primarily for yield will not be able to access the PWLB except to refinance existing loans or externalise internal borrowing. Acceptable use of PWLB borrowing includes service delivery, housing, regeneration, preventative action, refinancing and treasury management.

2.27 CIPFA published its revised Prudential Code for Capital Finance and Treasury Management Code on 20th December 2021. The key changes in the two codes are around permitted reasons to borrow, knowledge and skills, and the management of non-treasury investments.

2.28 To comply with the Prudential Code, authorities must not borrow to invest primarily for financial return. This Code also states that it is not prudent for local authorities to make investment or spending decision that will increase the Capital Financing Requirement unless directly and primarily related to the functions of the authority. Existing commercial investments are not required to be sold; however, authorities with existing commercial investments who expect to need to borrow should review the options for exiting these investments.

2.29 Borrowing is permitted for cashflow management, interest rate risk management, to refinance current borrowing and to adjust levels of internal borrowing. Borrowing to refinance capital expenditure primarily related to the delivery of a local authority's function but where a financial return is also expected is allowed, provided that financial return is not the primary reason for the expenditure. The changes align the CIPFA Prudential Code with the PWLB lending rules.

2.30 Unlike the Prudential Code, there is no mention of the date of initial application in the revised CIPFA Treasury Management (TM) Code. The TM Code now includes extensive additional requirements for service and commercial investments, far beyond those in the 2017 version.

2.31 Local authorities could defer introducing the revised reporting requirements for both of these Codes until the 2023/24 financial year. The implementation of these Codes was deferred by Swale Borough Council.

2.32 The Chartered Institute of Public Finance and Accountancy (CIPFA) and the Local Authority (Scotland) Accounts Advisory Committee (LASAAC) have decided to defer the implementation of International Financial Reporting Standard (IFRS) 16 on Leases until 1 April 2024. However, the Council will consider whether it wishes to adopt this standard for 2022/23 or 2023/24 as this will require a review of the Council's existing lease arrangements to determine what effect the new standard will have on their value in future accounts.

Compliance

2.33 The Council has complied with its Prudential and Treasury Management Indicators for 2021/22 which were set as part of the Treasury Management Strategy agreed by Council in February 2021.

2.34 In Appendix I the outturn position for the year against each Prudential Indicator is set out.

2.35 The Head of Finance and Procurement confirms that all treasury management activities undertaken during the year complied fully with the CIPFA Code of Practice and the Council's approved Treasury Management Strategy.

Treasury Advisers

2.36 Arlingclose has been the Council's treasury advisers since May 2009. Officers of the Council meet with Arlingclose regularly and high quality and timely information is received from them.

Capital Strategy

2.37 The Prudential Code includes a requirement for local authorities to provide a Capital Strategy, a summary document approved by full Council covering capital expenditure and financing, treasury management and non-treasury investments. The Council's Capital Strategy for 2021/22, complying with CIPFA's requirement, was approved by Council on 24 February 2021.

3. Proposal

3.1 Members are asked to approve the report.

4. Alternative Proposals

4.1 No alternative proposals have been considered and compliance with the CIPFA Code is mandatory.

5. Consultation Undertaken

5.1 Arlingclose have been consulted.

6. Implications

Issue	Implications
Corporate Plan	Supports delivery of the Council's objectives.
Financial, Resource and Property	As detailed in the report
Legal, Statutory and Procurement	CIPFA produce a framework for managing treasury activities, called a 'Code'. Councils are legally required to have regard to this Code and members of CIPFA are expected to comply with its requirements. This report fulfils the Council's legal obligation under the Local Government Act 2003 to have regard to both the CIPFA Code and the DLUHC Guidance
Crime and Disorder	Not relevant to this report
Environment and Climate/ Ecological Emergency	Not relevant to this report
Health and Wellbeing	Not relevant to this report
Safeguarding of Children, Young People and Vulnerable Adults	Not relevant to this report
Risk Management and Health and Safety	Not relevant to this report
Equality and Diversity	Not relevant to this report
Privacy and Data Protection	Not relevant to this report

7. Appendices

7.1 Appendix I: Treasury Management and Prudential Indicators

8. Background Papers

None

Treasury Management and Prudential Indicators for 2021/22

Introduction

The Local Government Act 2003 requires the Council to have regard to the Chartered Institute of Public Finance and Accountancy's Prudential Code for Capital Finance in Local Authorities (the Prudential Code) when determining how much money it can afford to borrow. The objectives of the Prudential Code are to ensure, within a clear framework, that the capital investment plans of local authorities are affordable, prudent and sustainable, and that treasury management decisions are taken in accordance with good professional practice. To demonstrate that the Council has fulfilled these objectives, the Prudential Code sets out the following indicators that must be set and monitored each year.

This report compares the approved indicators with the outturn position for 2021/22. Actual figures have been taken from or prepared on a basis consistent with, the Council's Statement of Accounts

Capital Expenditure: The Council's capital expenditure and financing may be summarised as follows.

Capital Expenditure and Financing	**2021/22 Actual**
	£'000
Total Capital Expenditure	**6,083**
Source of Funding	
Capital grants and other contributions	4,829
Earmarked reserves	573
Borrowing	451
Capital receipts	201
Direct Revenue Funding	29
Total Financing	**6,083**

A report on the 2021/22 Capital outturn was presented to Policy and Resources Committee on 13 July 2022.

Treasury Management and Prudential Indicators for 2021/22

Capital Financing Requirement: The Capital Financing Requirement (CFR) measures the Council's underlying need to borrow for a capital purpose.

Capital Financing Requirement	31/03/22 Estimate	31/03/22 Actual	31/03/22 Difference
	£'000	**£'000**	**£'000**
Total CFR	61,789	47,774	(14,015)
External Borrowing	(35,000)	(10,000)	25,000
Cumulative External Borrowing Requirement	**26,789**	**37,774**	**10,985**

External borrowing: as at 31 March 2022 the Council had £10 million of external borrowing.

Operational Boundary for External Debt: The Operational Boundary is based on the Council's estimate of most likely (i.e. prudent but not worst case) scenario for external debt. It links directly to the Council's estimates of capital expenditure, the capital financing requirement and cash flow requirements, and is a key management tool for in-year monitoring. Other long-term liabilities comprise finance lease, and other liabilities that are not borrowing but form part of the Council's debt.

Operational Boundary and Total Debt	31/03/22 Boundary £'000	31/03/22 Actual Debt £'000	Complied
Borrowing	55,000	10,000	✓
Other Long-Term Liabilities	500	0	✓
Total Operational Boundary	**55,500**	**10,000**	✓

Authorised Limit for External Debt: The Authorised Limit is the affordable borrowing limit determined in compliance with the Local Government Act 2003. It is the maximum amount of debt that the Council can legally owe. The Authorised Limit provides headroom over and above the Operational Boundary for unusual cash movements.

Authorised Limit and Total Debt	31/03/22 Boundary £'000	31/03/22 Actual Debt £'000	Complied
Borrowing	70,000	10,000	✓
Other Long-Term Liabilities	2,000	0	✓
Total Authorised Limit	**72,000**	**10,000**	✓

Treasury Management and Prudential Indicators for 2021/22

The Director of Resources confirms that there were no breaches to the Authorised Limit and the Operational Boundary during 2021/22.

Ratio of Financing Costs to Net Revenue Stream: This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet financing costs, net of investment income.

Ratio of Financing Costs to Net Revenue Stream	31/03/22 Estimate %	31/03/22 Actual %	Difference %
General Fund Total	5.11	4.83	0.28

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

	31/03/22 Actual %	Upper Limit %	Lower Limit %	Complied
Under 12 months	100	100	0	✓
12 months and within 24 months	0	100	0	✓
24 months and within 5 years	0	100	0	✓
5 years and within 10 years	0	100	0	✓
10 years and above	0	100	0	✓

Principal Sums Invested for Periods Longer than 364 days: 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 limits on the long-term principal sum invested to final maturities beyond the period end were:

	2021/22 £'000
Actual Principal Invested Beyond Year End	3,000
Limit on Principal Invested Beyond Year End	10,000
Complied	✓

Treasury Management and Prudential Indicators for 2021/22

Investment Benchmarking

Average Actual Return on Investments 2021/22	Original Estimate Return on Investments 2021/22	Average Bank Rate 2021/22	Average 7-day SONIA Rate 2021/22
0.30%	0.50%	0.19%	0.15%

SONIA is the average of the interest rates that banks pay to borrow sterling overnight from other financial institutions and other institutional investors.