Audit Committee		Agenda Item:
Meeting Date	24 July 2023	
Report Title	Annual Treasury Management Report 2022/23	
EMT Lead	Lisa Fillery, Director of Resources	
Head of Service	Claire Stanbury, Head of Finance and Procurement	
Lead Officers	Claire Stanbury, Head of Finance and Procurement Olga Cole, Management Accountant	
Classification	Open	

Recommendations	1. To note the Treasury Management outturn report for 2022/23.

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 2022.

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 2022/23 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 2022/23; and
- confirms compliance with Treasury limits and Prudential Indicators.

2. Background

Borrowing Requirement and Debt Management

2.1 The overall borrowing position is summarised below:

	Balance on 31/3/2022 £’000	Movement in Year £’000	Balance on 31/3/2023 £’000
Capital Financing Requirement	47,774	632	48,406
External Borrowing	(10,000)	0	(10,000)
Cumulative External Borrowing Requirement	**37,774**	**632**	**38,406**

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 accounted for as a charge to the General Fund.

2.3 The reason for the increase in the CFR in 2022/23 is due to the increase in the unfunded capital spend.

2.4 As outlined in the treasury strategy, the Authority’s chief objective when borrowing has been to strike an appropriately low risk balance between securing lower interest costs 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 and, where practicable, to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing.

2.5 The cost of both long and short-term borrowing rose dramatically over the year, with rates at the end of March around 2% - 4% higher than those at the beginning of April. Rate rises have been driven primarily by inflation and the need for central banks to control this by raising interest rates. Particularly dramatic rises were seen in September after the ‘mini-budget’ included unfunded tax cuts and additional borrowing to fund consumer energy price subsidies: over a twenty-four-hour period some PWLB rates increased to 6%. Rates have now fallen from September peaks but remain volatile and well above recent historical norms. The PWLB 10 year maturity certainty rate stood at 4.33% at 31st March 2023, 20 years at 4.70% and 30 years at 4.66%.

2.6 The table below summarises the Council's borrowing portfolio from other local authorities at 31 March 2023.

Local Authority	Loan Value £'000	Borrowing Rate	Duration of the Loan	Borrowing Date	Loan Repayment Date
West Midlands Combined Authority	5,000	1.05%	1 year	07/04/2022	06/04/2023
North Northamptonshire Council	5,000	4.30%	1 year	27/02/2023	26/02/2024

Investment Activity

2.7 The Council holds significant investment funds, representing income received in advance of expenditure plus balances and reserves held. During 2022/23, the Council held average daily cash balances of £30 million (£38 million for 2021/22) and our Money Market balances closed at £6.6 million at 31 March 2023.

2.8 The Council's budgeted investment income for 2022/23 was £166,000 and the actual income received was £704,000, of which £123,084 was from the Council's long-term investment in the Church, Charities and Local Authorities (CCLA) Mutual Investment Property Fund.

2.9 The table below summarises the Council's investment portfolio at 31 March 2023. 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 2023.

Counterparty (MMF = Money Market Funds)	Long-Term Rating	Balance Invested at 31 March 2023 £'000
Morgan Stanley MMF	AAAmmf	2,130
Black Rock MMF	AAAmmf	3,000
Deutsche MMF	AAAmmf	1,420
CCLA Property Fund	unrated	3,000
Total		**9,550**

2.10 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.

2.11 The treasury management position at 31st March 2023 and the changes during the year is summarised below:

Investments	Balance on 31/03/22 £'000	Movement in Year £'000	Balance on 31/03/23 £'000	Average Rate at 31/03/23 %
Cash and Cash Equivalents	15,735	(9,185)	6,550	1.88
Short-Term Investments	7,600	(7,600)	0	0
Long-Term Investments	3,000	0	3,000	4.10
TOTAL INVESTMENTS	**26,335**	**(16,785)**	**9,550**	
Borrowing				
Short-Term Borrowing	(10,000)	0	(10,000)	0.90
TOTAL BORROWING	**(10,000)**	**0**	**(10,000)**	

2.12 The long-term investment shown in the table above is the Council's investment in the CCLA Property Fund. Accounting requirements dictate that financial instruments, which include this investment, are carried in the balance sheet at fair value. The fair value for this fund is based on the market price which as at 31 March 2023 was £2.863 million.

2.13 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 Debt Management Agency Deposit Facility (DMADF).

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

2.15 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.

2.16 The investments permissible by the 2022/23 Treasury Strategy were:

Counterparty	**Cash Limits**
The UK Government	Unlimited
Local Authorities and other government entities	£3m
Major UK banks / building societies 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, Multi Asset Funds	£3m each
CCLA Property Fund	£3m
Registered providers (unsecured)	£3m in aggregate
Secured Investments	£3m in aggregate
Other Investments	£3m in aggregate
Non treasury investments	To be agreed on a case by case basis

2.17 This Council 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 lower 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

2.18 The maximum permitted duration for unsecured deposits with major UK Banks and building societies is 13 months. For 2022/23 the Director of Resources in consultation with chair of Policy & Resources Committee could consider longer duration. Bonds could have been purchased with a maximum duration of five years.

2.19 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 2023 the Council held £4.173 million of a longstanding portfolio of 12 investment properties within the borough. These investments generated £0.2 million of investment income for the Council in 2022/23 after taking account of direct costs, representing a rate of return of 5.8%.

External Context

2.20 The war in Ukraine continued to keep global inflation above central bank targets and the UK economic outlook remained relatively weak with the chance of a mild recession, which at the date of drafting has not yet occurred. The economic backdrop during the January to March period continued to be characterised by high energy and commodity prices, high inflation, and the associated impact on household budgets and spending.

2.21 The Bank of England increased the official Bank Rate to 4.25% during the financial year. From 0.75% in March 2022, the Monetary Policy Committee (MPC) pushed through rises at every subsequent meeting over the period, with recent hikes of 50bps in December and February and then 25bps in March, taking Bank Rate to 4.25%. The Committee noted that inflationary pressures remain elevated with growth stronger than was expected in the February Monetary Policy Report.

2.22 Uncertainty continued to be a key driver of financial market sentiment and bond yields remained relatively volatile due to concerns over elevated inflation and higher interest rates, as well as the likelihood of the UK entering a recession and for how long the Bank of England would continue to tighten monetary policy. Towards the end of the period, fears around the health of the banking system following the collapse of Silicon Valley Bank in the US and purchase of Credit Suisse by UBS caused further volatility.

2.23 The labour market remained tight albeit with some ongoing evidence of potential loosening at the end of the period.

Credit Review

2.24 Early in the period, Moody's affirmed the long-term rating of Guildford BC but revised the outlook to negative. The agency also downgraded Warrington BC and Transport for London.

2.25 In July Fitch revised the outlook on Standard Chartered and Bank of Nova Scotia from negative to stable and in the same month Moody's revised the outlook on Bayerische Landesbank to positive. In September S&P revised the outlook on the Greater London Authority to stable from negative and Fitch revised the outlook on HSBC to stable from negative.

2.26 The following month Fitch revised the outlook on the UK sovereign to negative from stable. Moody's made the same revision to the UK sovereign, following swiftly after with a similar move for a number of local authorities and UK banks including Barclays Bank, National Westminster Bank (and related entities) and Santander. As a result, Arlingclose reduced its recommended maximum duration limit for unsecured deposits for all UK and Non-UK banks/institutions on its counterparty list to 35 days as a precautionary measure. No changes were made to the names on the list.

2.27 During the last few months of the reporting period there were only a handful of credit changes by the rating agencies, then in March the collapse of Silicon Valley Bank (SVB) in the US quickly spilled over into worries of a wider banking crisis as Credit Suisse encountered further problems and was bought by UBS.

2.28 As market volatility is expected to remain a feature, at least in the near term, as ever, the institutions and durations on the Authority's counterparty list recommended by Arlingclose remains under constant review.

2.29 Local authorities remain under financial pressure, but Arlingclose continues to take a positive view of the sector, considering its credit strength to be high. Section 114 notices have been issued by only a handful of authorities with specific issues. While Arlingclose's advice for local authorities on its counterparty list remains unchanged, a degree of caution is merited with certain authorities.

CIPFA Code and PWLB Lending Facility Guidance

2.30 Authorities that are purchasing or intending to purchase investment assets primarily for yield are not 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.

2.31 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.

2.32 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.

2.33 DLUHC published a consultation on the IFRS 9 pooled investment fund statutory override for English authorities for fair value gains and losses on pooled investment funds which was due to expire with effect from 2023/24. The options under evaluation were to allow the override to lapse, to extend it, or to make it permanent. The override will be extended for two years and therefore remain in place for the 2023/24 and 2024/25 financial years. Under the Regulations, gains and losses resulting from unrealised fair value movements relating to treasury pooled investment funds, that otherwise must be recognised in profit or loss under IFRS 9, are not charges to the revenue account, and must be taken into an unusable reserve account.

Compliance

2.34 The Council has complied with its Prudential and Treasury Management Indicators for 2022/23 which were set as part of the Treasury Management Strategy agreed by Council in February 2022.

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

2.36 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

2.37 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

2.38 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 2022/23, complying with CIPFA's requirement, was approved by Council on 23 February 2022.

3. Proposal

3.1 Members are asked to note 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 Our treasury advisors, 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

Issue	Implications
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 2022/23

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 2022/23. 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	**2022/23 Actual £'000**
Total Capital Expenditure	**6,967**
Source of Funding	
Capital grants and other contributions	3,338
Earmarked reserves	1,812
Borrowing	1,660
Capital receipts	28
Direct Revenue Funding	129
Total Financing	**6,967**

A report on the 2022/23 Capital outturn was presented to Policy and Resources Committee on 12 July 2023.

Treasury Management and Prudential Indicators for 2022/23

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

Capital Financing Requirement	31/03/23 Estimate £'000	31/03/23 Actual £'000	31/03/23 Difference £'000
Total CFR	72,150	48,406	(23,744)
External Borrowing	(50,000)	(10,000)	40,000
Cumulative External Borrowing Requirement	**22,150**	**38,406**	**16,256**

External borrowing: as at 31 March 2023 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 leases, and other liabilities that are not borrowing but form part of the Council's debt.

Operational Boundary and Total Debt	31/03/23 Boundary £'000	31/03/23 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	31/03/23 Boundary £'000	31/03/23 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 2022/23

The Director of Resources confirms that there were no breaches to the Authorised Limit and the Operational Boundary during 2022/23.

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	**31/03/23 Estimate %**	**31/03/23 Actual %**	**Difference %**
General Fund Total	6.83	1.88	4.95

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:

	31/03/23 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:

	2022/23 £’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 2022/23

Investment Benchmarking

Average Actual Return on Investments 2022/23	Original Estimate Return on Investments 2022/23	Average Bank Rate 2022/23	Average 7-day SONIA Rate 2022/23
1.88%	0.92%	2.39%	2.24%

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