AUDIT COMMITTEE – 27 JULY 2023

PART I – DELEGATED

8. TREASURY MANAGEMENT ANNUAL REPORT 2022/23 (DoF)

1. Summary

1.1 Purpose of the report

1.1.1 This 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 Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice on Treasury Management, (the Code), and the CIPFA Prudential Code for Capital Finance in Local Authorities, (the Prudential Code).

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

- An annual treasury strategy in advance of the year (Council February 2022)
- A mid-year year review (December Audit Committee)
- An annual review following the end of the year describing activity compared to the strategy, (this report)

1.1.3 The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This report provides details of the year end position for treasury activities and highlights compliance with the Council's policies previously approved by members.

1.1.4 This Council confirms that it has complied with the requirement under the Code to give scrutiny to all of the above treasury management reports by the Audit Committee. Following scrutiny by the Audit Committee, the report will be presented to Full Council in October.

1.2 Key Prudential and Treasury Indicators

1.2.1 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:

Prudential and treasury indicators	31.3.22 Actual £m	2022/23 Original Budget £m	31.3.23 Actual £m
Total Capital Financing Requirement	36.630	34.550	30.068
Gross borrowing	8.000	8.000	8.000
External debt	8.000		8.000
Investments	24.273		23.216
Net borrowing / (Investments)	**(16.273)**		**(15.216)**

Details

2.1 The Chartered Institute of Public Finance and Accountancy (CIPFA) defines treasury management as: “the management of the local authority’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”.

2.2 The Council’s 2022/22 Treasury Management Policy, as approved by Council on 22 February 2022, has the primary objectives of safeguarding the repayment of the principal and interest of its investments on time, and then ensuring adequate liquidity, with the investment return being the final objective.

2.3 This report provides the Committee with an overview of Treasury Management performance for 2022/23 including the actual prudential and treasury indicators as prescribed by the Prudential Code for Capital Finance (revised 2021) and the Treasury Management Code of Practice (revised 2021).

2.4 The Council has appointed treasury advisors to assist with our treasury management, Link Treasury Services Ltd, part of Link Group.

2.5 The economic environment has a significant impact on treasury management activity and performance. Information on interest rates for investments and borrowing is contained in the main body of the report. In addition, a commentary on wider economic performance during 2022/23 has been provided by Link Group and is at Appendix 1 to this report.

2.6 **The Council’s Capital Expenditure and Financing**

2.6.1 The Council’s capital expenditure plans are one of the key drivers of treasury management activity. The outputs of the capital expenditure plans are reflected in prudential indicators, which are designed to assist members’ overview and confirm capital expenditure plans.

2.6.2 The Council undertakes capital expenditure on long term assets. These activities may either be:

- Financed immediately through the application of capital or revenue resources (capital receipts, capital grants, revenue contributions etc.), which has no resultant impact on the Council’s borrowing need; or
- If insufficient financing is available, or a decision is taken not to apply resources, the capital expenditure will give rise to a borrowing need.

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

	2021/22 Actual £m	2022/23 Original Budget £m	2022/23 Actual £m
Capital Expenditure	3.709	5.974	6.700

Financed in Year	(3.441)	(3.071)	(6.700)
Unfinanced Capital Expenditure	**0.268**	**2.903**	**0.000**

2.7 **The Council's Overall Borrowing Need**

2.7.1 The Council's underlying need to borrow for capital expenditure is termed the Capital Financing Requirement (CFR). This figure is a gauge of the Council's indebtedness. The CFR results from the capital activity of the Council and resources used to pay for the capital spend. It represents the cumulative unfinanced capital expenditure (see above table) which has not yet been paid for by revenue or other resources.

2.7.2 Part of the Council's treasury activities is to address the funding requirements for this borrowing need. Depending on the capital expenditure programme, the treasury service organises the Council's cash position to ensure that sufficient cash is available to meet the capital plans and cash flow requirements. This may be sourced through borrowing from external bodies, (such as the Government, through the Public Works Loan Board [PWLB], or the money markets), or utilising temporary cash resources within the Council.

2.7.3 The Council's underlying borrowing need (CFR) is not allowed to rise indefinitely. Statutory controls are in place to ensure that capital assets are broadly charged to revenue over the life of the asset. The Council is required to make an annual revenue charge, called the Minimum Revenue Provision (MRP), to reduce the CFR. This is effectively a repayment of the borrowing need. This differs from the treasury management arrangements which ensure that cash is available to meet capital commitments. External debt can also be borrowed or repaid at any time, but this does not change the CFR.

2.7.4 The total CFR can also be reduced by:

- the application of additional capital financing resources, (such as unapplied capital receipts); or
- charging more than the statutory revenue charge (MRP) each year through a Voluntary Revenue Provision (VRP).

2.7.5 The Council's 2022/23 MRP Policy, (as required by DLUHC Guidance), was approved as part of the Treasury Management Strategy Report for 2022/23 on 22 February 2022.

2.7.6 The Council's CFR for the year is shown below and is a key prudential indicator.

Capital Financing Requirement	2021/22 Actual £m	2022/23 Original Budget £m	2022/23 Actual £m
Opening CFR relating to Capital programme	42.904	31.781	36.630
Add unfinanced Capital Expenditure (as above)	0.268	2.903	0.000
Less MRP	(0.168)	(0.134)	(0.188)
Less repayment of capital loans	(6.374)	0.000	(6.374)
Total Closing CFR	**36.630**	**34.550**	**30.068**

Movement in the CFR	(6.274)	2.769	(6.562)

Note 1: The CFR may be subject to revision following the completion of the 2019/20, 2020/21 and 2021/22 and 2022/23 audits.

2.7.7 The CFR should include finance leases on the balance sheet, which increase the Council's borrowing need. Although, no external borrowing is required against these schemes as a borrowing facility is included within the contract. The Council's acquisition of the headlease for three hospitality units during the year must be accounted for as a finance lease under proper accounting practices. The associated asset and liability will be brought onto the Council's balance sheet in the 2022/23 accounts following the receipt of the annual asset valuations. This will require the CFR to be restated.

2.8 **Limits to Borrowing Activity**

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

2.8.2 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.

	2021/22 Actual £m	2022/23 Original Budget £m	2022/23 Actual £m
Gross borrowing position	8.000	8.000	8.000
CFR	36.630	34.550	30.068
Under funding of CFR (internal borrowing)	(28.630)	(26.550)	(22.068)

2.8.3 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.

2.8.4 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.

2.8.5 **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.

2022/23	Capital Investment
Authorised limit	£39.000m
Maximum gross borrowing position during the year	£8.000m
Operational boundary	£37.000m
Average gross borrowing position	£8.000m
Financing costs as a proportion of net revenue stream (net income)	-4.52%

2.8.6 External borrowing is well below the operational boundary for external debt predominantly due to re-phasing of the capital programme during the year. The difference between the CFR and external borrowing is met by internal borrowing. This is the use of cash balances (arising from working capital, earmarked reserves and general balances) to finance the expenditure on a short term basis.

2.9 Treasury Position as at 31 March 2023

2.9.1 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. At the end of 2022/23 the Council's treasury position (excluding borrowing by finance leases and non treasury investments) was as follows:

Debt Portfolio	31.3.22 Principal	Rate/ Return	Average Life years	31.3.23 Principal	Rate/ Return	Average Life years
Fixed rate financing:						
PWLB	£8.000m	2.41%	46.5	£8.000m	2.41%	45.5
Total debt	**£8.000m**	**2.41%**	**46.5**	**£8.000m**	**2.41%**	**45.5**
CFR	**£36.630m**			**£30.068m**		
Over / (under) borrowing	**£28.630m**			**£22.068m**		
Total investments	**£24.273m**			**£23.216m**		
Net debt / (Investments)	**(£16.273m)**			**(£15.216m)**		

The maturity structure of the debt portfolio was as follows:

	31.3.22 Actual £m	2022/23 original upper limits %	31.3.23 Actual £m	31.3.23 Actual %
Within 50 years	8.000	n/a	8.000	100%

Investment Portfolio	31.3.22 Actual £m	31.3.22 Actual %	31.3.23 Actual £m	31.3.23 Actual %
Treasury investments				
Banks	8.926	36.77%	2.544	10.96%
Local and Police authorities	0.000	0.00%	5.000	21.54%
DMADF (H M Treasury)	13.000	53.56%	13.275	57.18%
Total managed in house	21.926	90.33%	20.819	89.68%
Short Term Fixed Income	2.347	9.67%	2.397	10.32%
Total managed externally	2.347	9.67%	2.397	10.32%
Total Treasury Investments	**24.273**	**100.00%**	**23.216**	**100.00%**
Non-Treasury investments				
Loans to Joint Ventures	4.695	83.39%	4.695	83.69%
Other Long Term Loans	0.935	16.61%	0.915	16.31%
Total Non-Treasury Investments	**5.630**	**100.00%**	**5.610**	**100.00%**
Treasury investments	24.273	81.17%	23.216	80.54%
Non-Treasury investments	5.630	18.83%	5.610	19.46%
Total of All Investments	**29.903**	**100.00%**	**28.826**	**100.00%**

The maturity structure of the treasury investment portfolio was as follows:

	31.3.22 Actual £m	2022/23 Maximum £m	31.3.23 Actual £m
Longer than 1 year	0.000	10.000	0.000
Up to 1 year	24.273	n/a	23.216
Total	**24.273**		**23.216**

2.9.2 The Council also has commercial investments in property which are governed by the Investment Guidance issued by the Department for Levelling Up, Housing and Communities. The performance of the Property Investment Portfolio is overseen by the Shareholder and Commercial Ventures Panel. As such, it is not included in this report.

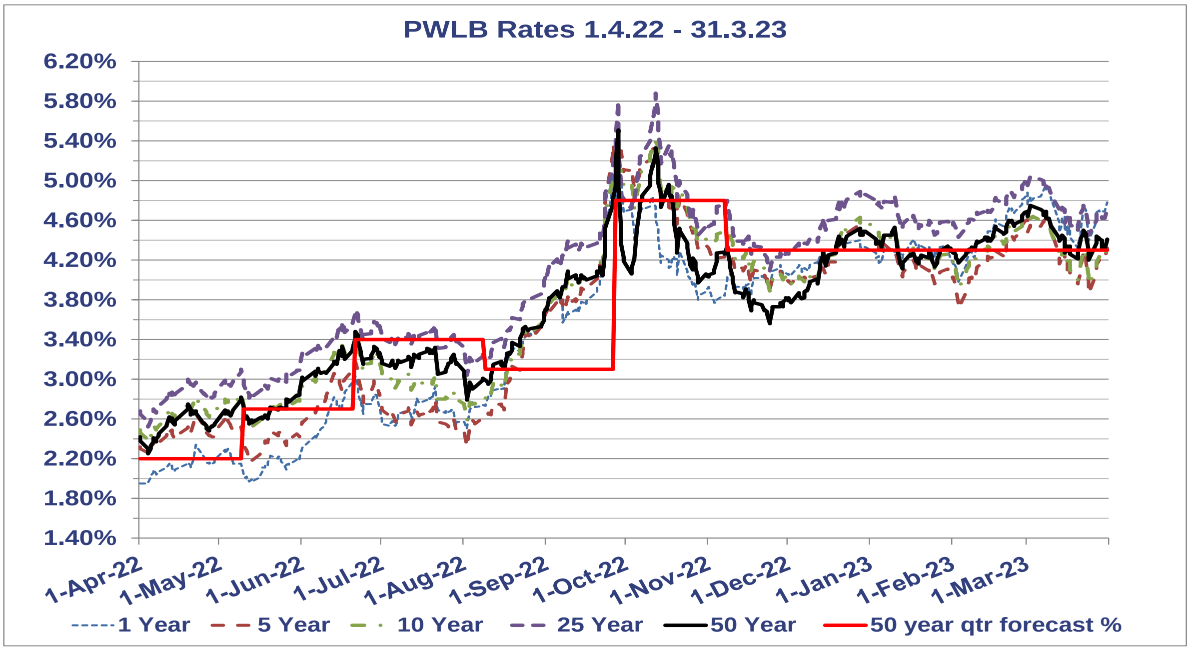
2.10 The Strategy for 2022/23 – Borrowing

2.10.1 When the Capital Strategy and Treasury Management Policy was set in February 2022, interest rate forecasts indicated gradual increases in short, medium and longer-term fixed borrowing rates during 2022/23 with considerable savings to be made by borrowing at the short end of the market.

2.10.2 The forecast provided by Link Group in December 2021 is shown in the following table:

Link Group Interest Rate View 20.12.21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25
BANK RATE	0.25	0.25	0.50	0.50	0.50	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.25
3 month ave earnings	0.20	0.30	0.50	0.50	0.60	0.70	0.80	0.90	0.90	1.00	1.00	1.00	1.00	1.00
6 month ave earnings	0.40	0.50	0.60	0.60	0.70	0.80	0.90	1.00	1.00	1.10	1.10	1.10	1.10	1.10
12 month ave earnings	0.70	0.70	0.70	0.70	0.80	0.90	1.00	1.10	1.10	1.20	1.20	1.20	1.20	1.20
5 yr PWLB	1.40	1.50	1.50	1.60	1.60	1.70	1.80	1.80	1.80	1.90	1.90	1.90	2.00	2.00
10 yr PWLB	1.60	1.70	1.80	1.80	1.90	1.90	2.00	2.00	2.00	2.10	2.10	2.10	2.20	2.30
25 yr PWLB	1.80	1.90	2.00	2.10	2.10	2.20	2.20	2.20	2.30	2.30	2.40	2.40	2.50	2.50
50 yr PWLB	1.50	1.70	1.80	1.90	1.90	2.00	2.00	2.00	2.10	2.10	2.20	2.20	2.30	2.30

2.10.3 This contrasts sharply with actual PWLB rates during the year as shown in the following graph as table:



	1 Year	5 Year	10 Year	25 Year	50 Year
Low	1.95%	2.18%	2.36%	2.52%	2.25%
Date	01/04/2022	13/05/2022	04/04/2022	04/04/2022	04/04/2022
High	5.11%	5.44%	5.45%	5.88%	5.51%
Date	28/09/2022	28/09/2022	12/10/2022	12/10/2022	28/09/2022

Average	3.57%	3.62%	3.76%	4.07%	3.74%
Spread	3.16%	3.26%	3.09%	3.36%	3.26%

2.10.4 During 2022/23, the Council maintained an under-borrowed position. 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 investment returns were initially low and minimising counterparty risk on placing investments also needed to be considered.

2.11 Borrowing Activity

2.11.1 During the year no new borrowing was undertaken.

2.11.2 The Council's current external borrowing portfolio is comprised of one loan of £8.000m from the Public Works Loan Board (PWLB). The loan is a long term loan with repayment on maturity, reflecting the expectation that the Council will have a long term borrowing requirement. The loan commenced in March 2019 and will run to September 2068 (49.5 years) at an annual interest rate of 2.41%.

2.11.3 Total interest payable for the year was £0.193m.

2.11.4 The Council has not borrowed more than, or in advance of its needs, purely to profit from the investment of the extra sums borrowed.

2.12 The Strategy for 2022/23 – Investments

2.12.1 In accordance with the CIPFA Prudential Code, it is the Council's priority to ensure security of capital and liquidity, and to obtain an appropriate level of return which is consistent with the Council's risk appetite.

2.12.2 During the year, investment returns increased as central banks attempted to address persistent high inflation with tighter monetary policy, recognising that the inflationary increases seen at the end of 2021/22 were not transitory and had not peaked. The Bank of England base rate was 0.75% on 1 April and moved up in stepped increases of either 0.25% or 0.5% throughout 2022/23, reaching 4.25% by the end of the financial year.

2.12.3 This has led to a rebalancing of the investment landscape with short term cash deposits and other Specified Investments (investments of less than a year in duration) becoming an attractive asset class when compared to bonds, equity, and property.

2.12.4 This has placed greater emphasis on proactive cashflow management and forecasting, as, for the first time in over a decade, cash balances (even relatively low values held for daily liquidity) are able to generate a significant contribution to the revenue budget through interest received.

2.13 Investment Activity

2.13.1 The Council's investment policy is governed by DLUHC investment guidance, which has been implemented in the annual investment strategy approved by the Council on 22 February 2022.

2.13.2 This 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, (such as rating outlooks, credit default swaps, bank share prices etc.).

2.13.3 Credit rating information is supplied by our treasury consultants, Link Group, on all counterparties that comply with the Council's criteria. Any counterparty failing to meet the criteria would be omitted from the counterparty (dealing) list. Any rating changes, rating watches (notification of a likely change), rating outlooks (notification of a possible longer term change) are provided to officers almost immediately after they occur and this information is considered before dealing.

2.13.4 There were no changes to the Council's counter party list during the year.

2.13.5 The policy also set out the following liquidity facilities/benchmarks to maintain:

- Authorised bank overdraft of £nil.
- Liquid short term deposits of at least £0.500m available with a week's notice.

2.13.6 The liquidity arrangements were adequate during the year.

2.13.7 The investment activity during the year conformed to the approved strategy.

2.13.8 The Council's cash balances comprise revenue and capital resources and cash flow monies. The Council's core cash resources comprised as follows:

Balance Sheet Resources	31.3.22 £m	31.3.23 £m
General Balances	5.361	4.964
Earmarked reserves	16.050	10.797
Provisions	1.344	3.232
Usable capital receipts	1.148	3.236
Total	**23.903**	**21.229**

Note: Values are taken from the unaudited 2022/23 draft Statement of Accounts and may be subject to change following the conclusion of the external audit.

2.13.9 Investments held by the Council:

- The Council maintained an average balance of £28.972m of internally managed funds.
- The internally managed funds earned an average rate of return of 2.13%.
- The comparable performance indicator is the average 7 day Sterling Overnight Index Average (SONIA) rate, which was 2.23%.
- Total investment income from internally managed funds was £0.577m.
- Interest on loans to the Council's joint ventures was £0.187m

2.13.10 The Council keeps all internally managed treasury investments short term. There are no sums invested for greater than 364 days.

2.13.11 Investments held by fund managers:

The Council uses a Short Term Fixed Income fund managed by Royal London Asset Management (RLAM) to invest its longer term cash. The performance of the fund manager against the benchmark return was:

Fund	Investments Held at 31 March 2023	Annualised Return	Annualised Benchmark
Short Term Fixed Income	£2.397m	2.13%	2.26%

2.13.12 These investments are held with a long-term view and performance is assessed over medium term horizon of three to five years.

Policy/Budget Reference and Implications

3.1 The recommendations in this report are within the Council's agreed policy and budgets.

Financial Implications

4.1 This report provides formal assurance on the Council's compliance with its Treasury Management Strategy during the year. The Director of Finance confirms that borrowing was only undertaken for a capital purpose and the statutory borrowing limit, (the authorised limit), was not breached. The financial implications are set out in the main body of the report and the impact of interest rates on investment income and borrowing costs have been reported through the financial monitoring report during the year.

Legal, Equal Opportunities, Staffing, Environmental, Community Safety, Public Health, Customer Services Centre, Communications & Website, Risk Management and Health & Safety Implications

5.1 None specific arising from this report.

6 Risk Implications

6.1 The Code of Practice on Treasury Management identifies eight key risks that are inherent in Treasury Management activity. The Council's Treasury Management Policy sets out the risks that it is seeking to manage:

1.	**Liquidity Risk**	That the Council may not have the cash it needs on a day to day basis to pay its bills.	This risk is managed through forecasting and the retention by the Council of an adequate working capital balance. In addition, through the Public Works Loan Board and other organisations, the Council is able to access short term borrowing, usually within 24 hours.
2.	**Interest Rate Risk**	That the costs and benefits expected do not materialise due to changes in interest rates.	This risk is managed through the placing of different types and maturities of investments, the forecasting and monitoring of the interest budget (with assistance from the Council's retained advisors).

3.	**Exchange Rate Risk**	That losses or gains are made due to fluctuations in the prices of currency.	The Council does not engage in any significant non-sterling transactions.
4.	**Credit and Counterparty Risk**	That the entity holding Council funds is unable to repay them when due.	This risk is managed through the maintenance of a list of authorised counterparties, with separate limits to ensure that the exposure to this risk is limited.
5.	**Refinancing Risk**	That the loans taken by the Council will become due for repayment and need replacing at a time when there is limited finance available or interest rates are significantly higher.	The timing of loan maturities and likely timing of externalization of internal borrowing is monitored along with interest rate forecasts. Officers ensure that due dates are monitored and seek advice from the Council's advisors about when to raise any finance needed.
6.	**Legal and Regulatory Risk**	That the Council operates outside its legal powers.	This risk is managed through the Council's training and development of Officers involved in Treasury Management, the independent oversight of Internal and External Audit, and the advice (for example on the contents of this strategy) taken from the Council's Treasury advisors.
7.	**Fraud, Error and Corruption**	The risk that losses will be caused by impropriety or incompetence.	This risk is managed through the controls in the Council's financial procedures. For example, the segregation of duties between those making investment decisions and those transferring funds.
8.	**Market Risk**	That the price of investments held fluctuates, principally in secondary markets.	The majority of the Council's investments are not traded, but where they are (e.g. Property investment portfolio) the main investments' value comes from the income they generate which is generally long term and secure.

Recommendation

7.1 That the Committee notes the Treasury Management Annual Report.

Report prepared by: Hannah Doney, Head of Finance

Data Quality

Data sources: Treasury Management System; KPI Monitoring to SSOB; Link Reports

Data checked by: Hannah Doney, Head of Finance

Data rating: Tick

1	**Poor**	
2	**Sufficient**	
3	**High**	**x**

Background Papers

Capital Strategy and Treasury Management Strategy 2022/23 (published as part of the 2022/23 budget)

APPENDICES / ATTACHMENTS

Appendix 1 – Economic Commentary (provided by Link Group)

Appendix 2 - Commentary on Gilt Yields and PWLB Borrowing Rates (Provided by Link Group)