Executive Overview & Scrutiny Committee: 6 September 2022

CABINET: 13 September 2022

Report of:	**Head of Finance, Procurement and Commercial Services**
Relevant Portfolio Holder:	**Councillor Adam Yates**
Contact for further information:	**Mr J Smith (Extn.5093)** **(E-mail: Jonas.Smith@westlancs.gov.uk)**

SUBJECT: 2022/23 TREASURY MANAGEMENT AND PRUDENTIAL INDICATORS Q1 MONITORING

Wards affected: Borough wide

1.0 PURPOSE OF THE REPORT

1.1 To set out details of Treasury Management operations for the first quarter of 2022/23 and to report on the Prudential Indicators, where available.

2.0 RECOMMENDATIONS

EXECUTIVE OVERVIEW & SCRUTINY COMMITTEE:

2.1 That the Treasury Management activity and Prudential Indicator performance for the first quarter of 2022/23 be noted and agreed comments be forwarded to Cabinet to consider.

2.2 That future Treasury Management monitoring reports be submitted to the Budget/Council Plan Committee, unless there are specific recommendations for this Committee and Cabinet to consider.

CABINET:

2.3 That, subject to consideration of the agreed comments of the Executive Overview & Scrutiny Committee, the Treasury Management activity and Prudential Indicator performance for the first quarter of 2022/23 be noted.

2.4 That future Treasury Management monitoring reports be submitted to the Budget/Council Plan Committee, unless there are specific recommendations for Cabinet to consider.

3.0 BACKGROUND

3.1 The Council has adopted the CIPFA Treasury Management Code of Practice in Local Authorities. One condition of the Code is that a report must be made quarterly to the Council on the activities of the Treasury Management function including the exercise of Treasury Management powers delegated to the Head of Finance, Procurement and Commercial Services.

3.2 The CIPFA Prudential Code for Capital Finance sets out a range of prudential indicators to assess whether an authority's financial position is prudent, affordable and sustainable. It is best practice that performance on these indicators is reported to Members on a regular basis.

4.0 ECONOMICS UPDATE AND INTEREST RATE FORECAST

4.1 Following the 0.1% m/m fall in GDP in March and the 0.3% m/m contraction in April, the economy is now moving towards a recession (two quarters of falling output in a row). Indeed, GDP would need to rise by 0.4-0.5% m/m in both May and June to prevent the economy from contracting in Q2 as a whole. That said, without the joint wind down of the COVID-19 Test and Trace and vaccination programme, GDP would have risen by 0.2% m/m and 0.1% m/m in March and April respectively.

4.2 CPI inflation rose from 9.1% in May to a new 40-year high of 9.4% in June and it is not yet close to its peak. It is currently forecast that food price inflation will rise above 10% in September and coupled with an expected 60% rise in utility prices in October could see CPI inflation to a peak of around 13% towards the end of the 2022.

4.3 The Bank of England has now increased interest rates five times in as many meetings and raised rates to their highest level since the Global Financial Crisis. As can be seen in the table below it is Link's view that they will increase Bank Rate during the remainder of 2022 and into Q1 2023 to combat the sharp increase in inflationary pressures. It is not expected to raise rates beyond 2.75%, but it is possible.

Link Group Interest Rate View	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25
BANK RATE	**2.25**	**2.50**	**2.75**	**2.75**	**2.75**	**2.50**	**2.50**	**2.25**	**2.25**	**2.25**	**2.25**	**2.25**	**2.00**

4.4 The general situation is for volatility in bond yields to endure as investor fears and confidence ebb and flow i.e., equities, or the safe haven of government bonds, despite material inflationary concerns. The overall longer-run trend is for gilt yields and PWLB rates to rise moderately in the near-term, given the extent to which market expectations are already priced in and then to fall back once inflation starts to fall through 2023.

Link Group Interest Rate View	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25
5yr PWLB	**2.80**	**3.00**	**3.10**	**3.10**	**3.00**	**3.00**	**2.90**	**2.90**	**2.80**	**2.80**	**2.80**	**2.70**	**2.70**
10yr PWLB	**3.00**	**3.20**	**3.30**	**3.30**	**3.20**	**3.10**	**3.10**	**3.00**	**3.00**	**3.00**	**2.90**	**2.90**	**2.80**
25yr PWLB	**3.40**	**3.50**	**3.50**	**3.50**	**3.50**	**3.40**	**3.40**	**3.30**	**3.30**	**3.20**	**3.20**	**3.20**	**3.10**
50yr PWLB	**3.10**	**3.20**	**3.20**	**3.20**	**3.20**	**3.10**	**3.10**	**3.00**	**3.00**	**2.90**	**2.90**	**2.90**	**2.80**

5.0 INVESTMENTS

5.1 The Treasury Management Strategy Statement (TMSS) for 2022/23, which includes the Annual Investment Strategy, was approved by the Council on 23rd 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. In the current economic climate, it is considered appropriate to keep investments short-term to cover cash flow needs, but also to seek out value available in periods up to 12 months with high credit rated financial institutions.

5.2 As a result of the SORP review, there were several changes to the criteria used for deciding upon counterparties for investment purposes as set out below.

Type of Counterparty	Maximum loan by Council	Maximum Period
Major British Based Banks and Subsidiaries with at least A- credit rating.	£5m	Up to £5m 364 days Up to £3m 3 years
British Based Building Societies. – Only those with at least A- credit rating as advised by Link.	£5m	Up to £5m 364 days Up to £3m 3 years
Other Local Authorities, where agreed.	£5m	Up to 5 years
Property Funds, Corporate Bonds, Infrastructure Investments	£3m	Up to 3 years for Corporate, and 5 years for Property and Infrastructure
Money Market Funds AAA rated	£3m	N/A Callable deposits

5.3 The following table provides details on investment activity during the first 3 months of this year and last year.

INVESTMENT PORTFOLIO	31.3.22 Actual £000	31.3.22 Actual %	30.6.22 Actual £000	30.6.22 Actual %
Treasury investments				
Banks	11,500	41%	8,000	38%
Building Societies - rated	11,500	41%	8,000	38%
Building Societies – unrated		0%		0%
Local authorities	5,000	18%	5,000	24%
DMADF (H M Treasury)		0%		0%
etc				
Total managed in house	28,000	100%	21,000	100%
Bond funds				
Property funds				
Cash fund managers				
Total managed externally	0	0%	0	0%
TOTAL TREASURY INVESTMENTS	28,000	100%	21,000	100%

Non Treasury investments				
Third party loans				
Subsidiaries	1,575	100%	1,575	100%
Companies				
Property				
etc				
TOTAL NON TREASURY INVESTMENTS	1,575	100%	1,575	100%

Treasury investments	28,000	95%	21,000	93%
Non Treasury investments	1,575	5%	1,575	7%
TOTAL OF ALL INVESTMENTS	29,575	100%	22,575	100%

The maturity structure of the investment portfolio was as follows:

	31.3.22 Actual £000	30.6.22 Actual £000
Investments		
Longer than 1 year		
Up to 1 year	29,575	22,575
Total	29,575	22,575

The gross interest earned was as follows:

	31.3.22 Actual £	30.6.22 Actual £
Gross interest earned	133,472	66,683

5.4 Following the SORP review in 2019, the Treasury Management investment return budget for 2020/21 was increased by £326k to £499.8k. This target was based upon the view that the Council would have £10m available for short-term investments i.e., Banks/Building Societies up to 12 months and £10m available to invest in longer term, higher return vehicles i.e., Property/Investment/Infrastructure Funds and increasing rates of return on investments.

5.5 The 2022/23 budget was increased by a further £100k to £599.8k in February 2022 due to the forecast rise of interest rates and increase of investment returns.

5.6 It should be noted that although the Council had £22.575m out on investment at the end of June as per the table in 5.3 the total included several items of one-off funding from central government to support households and businesses during the pandemic and current cost of living crisis. Specifically, Covid-19 Additional Relief Fund £2.2m, S31 Relief funding of £4m and Energy Rebate funding of £3m. Consequently, true Council cash balances were around £13.3m and therefore the £10m earmarked to invest in the longer term was not available.

5.7 As part of the ongoing work to achieve best value in Treasury Management, we continually monitor our performance against a benchmark figure of the average 3-month SONIA interest rate. The average rate of interest earned at the end of June 2022 was 1.157% which exceeded the benchmark average of 1.1025%.

5.8 The reduction in balances as set out in 5.6 means the Council will not achieve the investment income as anticipated under the SORP review. It is projected that the overall shortfall will be £346k, of which it is estimated that £240k is attributable to the GRA and £106k to the HRA.

6.0 BORROWING

6.1 No long-term borrowing was undertaken during the first quarter of 2022/23, however, given the true balances held for investment by the Council as set out in 5.6 and the ongoing large scale capital investment it is almost certain that there will be a need to borrow during 2022/23.

6.2 The Treasury Management function has managed cash flows in such a way as to avoid incurring borrowing costs despite the Council's GRA capital financing requirement (CFR), i.e. its underlying need to borrow to finance capital expenditure, being £23.5m at the end of 2021/22 as per the table in 7.3 below. Based on current 50-year PWLB rates 3.37% this would have cost the Council £792k in interest per annum.

6.3 In April 2020 a future service pension prepayment of £7.15m was made to the Lancashire Pension Fund which realised a revenue saving to the Council of £150k for each of the subsequent three years.

6.4 HM Treasury issued new guidance in November 2020 in relation to borrowing from the PWLB. It outlined permissible categories of local authority capital expenditure (service delivery, housing, regeneration, preventative action and treasury management). Any investment asset bought primarily for yield which

was acquired after 26 November 2020 would result in the authority not being able to access the
PWLB in that financial year or being able to use the PWLB to refinance this transaction at any point in the future.

6.5 The change in PWLB lending criteria is likely to impact the Commercial Property Strategy agreed at Council in July 2020 as part of the SORP process. It was agreed to invest up to £30m over three years for the purchase/construction of commercial properties. If the purchase is primarily for yield rather than for say regeneration, then PWLB borrowing to finance the Council capital programme would not be available.

7.0 PRUDENTIAL AND TREASURY INDICATORS

7.1 It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. During the quarter ended 30th June 2022, the Council has operated within the treasury and prudential indicators set out in the Council's Treasury Management Strategy Statement for 2022/23. The Head of Finance, Procurement and Commercial Services reports that no difficulties are envisaged for the current or future years in complying with these indicators.

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

7.3 The prudential and treasury indicators are shown below. It should be noted that a reconciliation of the Council's CFR position was carried out after the February 2022 Council meeting and the agreed slippage from the July 2022 capital outturn report have been incorporated into the revised budget for 2022/23 resulting in a change to the budgeted GRA and HRA figures although the overall CFR remains within approved limits.

Treasury Indicators	31.03.22 Actual £'000	2022/23 Original Budget £'000	2022/23 Revised Budget £'000	2022/23 Forecast outturn £'000
Authorised limit for external debt	88,212	153,571	153,571	153,571
Operational boundary for external debt	88,212	143,071	143,071	143,071
Gross external debt	88,212	88,212	88,212	88,212

Prudential Indicators	31.03.22 Actual £'000	2022/23 Original Budget £'000	2022/23 Revised Budget £'000	2022/23 Forecast outturn £'000
Capital expenditure				
Non - HRA	9,348	11,156	15,295	10,745
HRA	16,611	14,431	26,492	21,690
Total	25,959	25,587	41,787	32,435
Capital Financing Requirement (CFR)				
Non - HRA	23,525	18,048	28,431	28,431
HRA	88,419	125,023	104,017	99,179
Total	111,944	143,071	132,448	127,610
Annual change in CFR				
Non - HRA	1,098	9,434	4,906	4,906
HRA	6,702	6,997	15,598	10,760
Total	7,800	16,431	20,504	15,666
In year borrowing requirement				
Non - HRA	1,405	10,000	5,220	5,220
HRA	7,052	6,997	15,948	11,110
Total	8,457	16,997	21,168	16,330
Ratio of financing costs to net revenue stream				
Non - HRA	1.15%	-1.08%	-1.07%	-1.07%
HRA	12.91%	10.88%	12.06%	12.06%

8.0 SUSTAINABILITY IMPLICATIONS

8.1 There are no significant sustainability impacts associated with this report and, in particular, no significant impact on crime and disorder. The report has no significant links with the Sustainable Community Strategy.

9.0 RISK ASSESSMENT

9.1 The formal reporting to Council of Prudential Indicators and Treasury Management performance is part of the overall framework set out in Codes of Practice to ensure that the risks associated with this area are effectively controlled. Given the Council's strict investment criteria the risk of loss of investment funds is low, the sums invested can be very large, so treasury management activities are included in the Council's Key Risk Register.

Background Documents

The following background documents (as defined in Section 100D (5) of the Local Government Act 1972) have been relied on to a material extent in preparing this Report.

Date	Document	File Ref
2017	CIPFA Updated Prudential Code for Capital Finance in Local Authorities	Accountancy Office
2017	CIPFA Updated Treasury Management Code of Practice	Accountancy Office

Equality Impact Assessment

The decision does not have any direct impact on members of the public, employees, elected members and / or stakeholders. Therefore, no Equality Impact Assessment is required.

Appendices

Minute of the Executive Overview & Scrutiny Committee – 6 September 2022 (Cabinet only