AGENDA ITEM:

Executive Overview & Scrutiny Committee: 13 September 2023
Cabinet: 26 September 2023

Report of: **Head of Finance, Procurement and Commercial Services**

Relevant Corporate Director: Housing, Transformation and Resources

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SUBJECT: TREASURY MANAGEMENT AND PRUDENTIAL INDICATORS Q1 MONITORING 2023-24

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 2023/24 and to report on the Prudential Indicators, where available.

2.0 RECOMMENDATION

2.1 To note the Treasury Management activity and Prudential Indicator performance for the first quarter of 2023/24.

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 The economy has weathered the drag from higher inflation better than was widely expected. The 0.2% m/m rise in real GDP in April, following March's 0.3% m/m contraction will further raise hopes that the economy will escape a recession this year. Some of the strength in April was due to fewer strikes by train workers and teachers in that month. Moreover, some of the falls in activity in other areas in April were probably temporary too.

4.2 CPI inflation stayed at 8.7% in May (consensus 8.4%) and, perhaps more worryingly, core CPI inflation rose again, from 6.8% to a new 31-year high of 7.1%. The rise in core inflation built on the leap from 6.2% in March to 6.8% and means it is accelerating in the UK while it is slowing in the US and the Euro-zone (both fell to 5.3%). A further decline in fuel inflation, from -8.9% to -13.1%, and the second fall in food inflation in as many months, from 19.3% to 18.7%, explained why overall CPI inflation didn't rise. And the scheduled fall in the average annual utility price from £2,500 to £2,074 on 1st July means overall CPI inflation will probably ease in the coming months. But the problem is that the recent surge in core inflation and the reacceleration in wage growth shows that domestic inflationary pressures are still strengthening.

4.3 The Bank of England has now increased interest rates fourteen 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 further increase Bank Rate in the second quarter of 2023 to combat stubborn inflationary pressures. It is not expected to raise rates beyond 5.50%, but it is possible.

Link Group Interest Rate View	26.06.23												
	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26
BANK RATE	5.00	5.50	5.50	5.50	5.25	4.75	4.25	3.75	3.25	2.75	2.75	2.50	2.50
3 month ave earnings	5.30	5.60	5.50	5.30	5.00	4.50	4.00	3.50	3.00	2.70	2.60	2.50	2.50
6 month ave earnings	5.80	5.90	5.70	5.50	5.10	4.60	4.00	3.50	3.00	2.70	2.60	2.60	2.60
12 month ave earnings	6.30	6.20	6.00	5.70	5.30	4.80	4.10	3.60	3.10	2.80	2.70	2.70	2.70
5 yr PWLB	5.50	5.60	5.30	5.10	4.80	4.50	4.20	3.90	3.60	3.40	3.30	3.30	3.20
10 yr PWLB	5.10	5.20	5.00	4.90	4.70	4.40	4.20	3.90	3.70	3.50	3.50	3.50	3.40
25 yr PWLB	5.30	5.40	5.20	5.10	4.90	4.70	4.50	4.20	4.00	3.90	3.80	3.80	3.70
50 yr PWLB	5.00	5.10	5.00	4.90	4.70	4.50	4.30	4.00	3.80	3.60	3.60	3.50	3.50

4.4 Gilt yield curve movements have shifted upwards, especially at the shorter end of the yield curve since our previous forecast but remain relatively volatile. PWLB 5 to 50 years Certainty Rates are, generally, in the range of 4.90% to 5.60%. We view the markets as having built in, already, nearly all the effects on gilt yields of the likely increases in Bank Rate and the elevated inflation outlook.

5.0 INVESTMENTS

5.1 The Treasury Management Strategy Statement (TMSS) for 2023/24, which includes the Annual Investment Strategy, was approved by the Council on 22nd February 2023. 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	31.3.23 Actual £000	31.3.23 Actual %	30.6.23 Actual £000	30.6.23 Actual %
Treasury investments				
Banks	5,000	45%	10,000	63%
Building Societies - rated	1,000	9%	1,000	6%
Building Societies – unrated		0%		0%
Local authorities	5,000	45%	5,000	31%
DMADF (H M Treasury)		0%		0%
etc				
Total managed in house	11,000	100%	16,000	100%
Bond funds				
Property funds				
Cash fund managers				
Total managed externally	0	0%	0	0%
TOTAL TREASURY INVESTMENTS	11,000	100%	16,000	100%

Non Treasury investments				
Third party loans				
Subsidiaries	1,300	100%	1,300	100%
Companies				
Property				
etc				
TOTAL NON TREASURY INVESTMENTS	1,300	100%	1,300	100%

Treasury investments	11,000	89%	16,000	92%
Non Treasury investments	1,300	11%	1,300	8%
TOTAL OF ALL INVESTMENTS	12,300	100%	17,300	100%

The maturity structure of the investment portfolio was as follows:

	31.3.23 Actual £000	30.6.23 Actual £000
Investments		
Longer than 1 year		
Up to 1 year	12,300	17,300
Total	12,300	17,300

The gross interest earned was as follows:

	31.3.23 Actual £	30.6.23 Actual £
Gross interest earned	476,111	169,145

5.4 The 2023/24 gross investment income budget was agreed at £438.8k in February 2023 which reflected the anticipated increase in interest rates during the year and resulting increase in investment returns.

5.5 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 2023 was 4.064% which was less than the benchmark average of 4.37%.

5.6 At the end of Q1, higher than anticipated base rate increases mean that it is projected that the overall surplus will be £191k, of which it is estimated to be a £212k surplus attributable to the GRA and a £21k shortfall attributable to the HRA. The HRA shortfall is due to the under-borrowing position of the capital programme which attracts an item 8 charge on its Capital Financing Requirement (CFR).

6.0 BORROWING

6.1 No long-term borrowing was undertaken during the first quarter of 2023/24, however, given the ongoing large scale capital investment it is almost certain that there will be a need to borrow during 2023/24.

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 £23.1m at the end of 2022/23 as per the table in 7.3 below. Based on current 50-year PWLB rates 5.28% this would have cost the Council £1.22m in interest per annum.

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 allowed to access PWLB borrowing in that financial year nor could they refinance the 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 2023, the Council has operated within the treasury and prudential indicators set out in the Council’s Treasury Management Strategy Statement for 2023/24. 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 2023 Council meeting and the agreed slippage from the July 2023 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 remained unchanged.

Treasury Indicators	31.03.23 Actual £'000	2023/24 Original Budget £'000	2023/24 Revised Budget £'000	2023/24 Forecast outturn £'000
Authorised limit for external debt	88,212	146,514	146,514	146,514
Operational boundary for external debt	88,212	136,014	136,014	136,014
Gross external debt	88,212	88,212	88,212	88,212

Prudential Indicators	31.03.23 Actual £'000	2023/24 Original Budget £'000	2023/24 Revised Budget £'000	2023/24 Forecast outturn £'000
Capital expenditure				
Non - HRA	7,709	2,987	13,976	7,123
HRA	13,097	21,955	25,009	16,506
Total	20,806	24,942	38,985	23,629
Capital Financing Requirement (CFR)				
Non - HRA	23,177	29,339	28,083	27,567
HRA	92,957	106,675	108,555	108,448
Total	116,134	136,014	136,638	136,015
Annual change in CFR				
Non - HRA	-86	947	4,390	4,390
HRA	4,528	12,437	15,491	15,491
Total	4,442	13,384	19,881	19,881
In year borrowing requirement				
Non - HRA	228	1,347	4,790	4,790
HRA	4,890	12,812	15,866	15,866
Total	5,118	14,159	20,656	20,656
Ratio of financing costs to net revenue stream				
Non - HRA	-0.61%	0.47%	0.47%	0.47%
HRA	12.02%	11.29%	11.29%	11.29%

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.