Title of meeting:	Governance and Audit and Standards Committee Cabinet City Council
Date of meeting:	Governance and Audit and Standards Committee 20 July 2022 Cabinet 26 July 2022 City Council 11 October 2022
Subject:	Treasury Management Outturn Report 2021/22
Report by:	Director of Finance and Resources (Section 151 Officer)
Wards affected:	All
Key decision:	No
Full Council decision:	Yes

1. Executive Summary

1.1 The Chartered Institute of Public Finance & Accountancy's (CIPFA) Prudential Code of Practice requires local authorities to calculate prudential indicators before the start of and after each financial year. The CIPFA Code of Practice on Treasury Management also requires the S.151 Officer to prepare an annual report on the outturn of the previous year. This information is shown in Appendix A of the report.

2. Purpose of Report

2.1 To inform members and the wider community of the Council's treasury management activities in 2021/22 and of the Council's treasury management position as of 31 March 2022.

3. Recommendations

3.1 It is recommended that the actual prudential and treasury management indicators based on the unaudited accounts, as shown in Appendix B, be noted (an explanation of the prudential and treasury management indicators is contained in Appendix C).

4. Background

4.1 The Local Government Act 2003 requires local authorities to have regard to the Chartered Institute of Public Finance and Accountancy's (CIPFA) Prudential Code for Capital Finance in Local Authorities.

5. Reasons for Recommendations

5.1 The net cost of Treasury Management activities and the risks associated with those activities have a significant effect on the Council's overall finances. Consequently, in accordance with good governance, the S.151 Officer is required to report to the Council on those activities.

6. Integrated impact assessment

6.1 An integrated impact assessment is not required, as the recommendations do not directly impact on service or policy delivery. Any changes made arising from this report would be subject to investigation in their own right.

7. Legal implications

7.1 The S.151 Officer is required by the Local Government Act 1972 and by the Accounts and Audit Regulations 2015 to ensure that the Council's budgeting, financial management, and accounting practices meet the relevant statutory and professional requirements. Members must have regard to and be aware of the wider duties placed on the Council by various statutes governing the conduct of its financial affairs.

8. Director of Finance & Resources (Section 151 Officer) comments

8.1 All financial considerations are contained within the body of the report and the attached appendices

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Signed by Director of Finance & Resources (Section 151 Officer)

Appendices:

Appendix A: Treasury Management Outturn Report
Appendix B: Prudential and Treasury Management Indicators
Appendix C: Explanation of Prudential and Treasury Management Indicators

Background list of documents: Section 100D of the Local Government Act 1972

The following documents disclose facts or matters, which have been relied upon to a material extent by the author in preparing this report:

Title of document	Location
1 Information pertaining to the treasury management outturn	Financial Services
2	

APPENDIX A

TREASURY MANAGEMENT OUTTURN REPORT

1. GOVERNANCE

Treasury management activities were performed within the Prudential Indicators approved by the City Council.

Treasury management activities are also governed by the Treasury Management Policy Statement, Annual Minimum Revenue Provision for Debt Repayment Statement and Annual Investment Strategy approved by the City Council.

2. COMBINED BORROWING AND INVESTMENT POSITION (NET DEBT)

On 31 March 2022, the Council had gross debt including finance leases and private finance initiative (PFI) schemes of £763m and gross investments of £451m giving rise to a net debt of £312m. Major components of the Council's gross investments of £451m include the Council's general and earmarked reserves of £251m, and capital grants received but yet to be applied to finance capital expenditure of £147m.

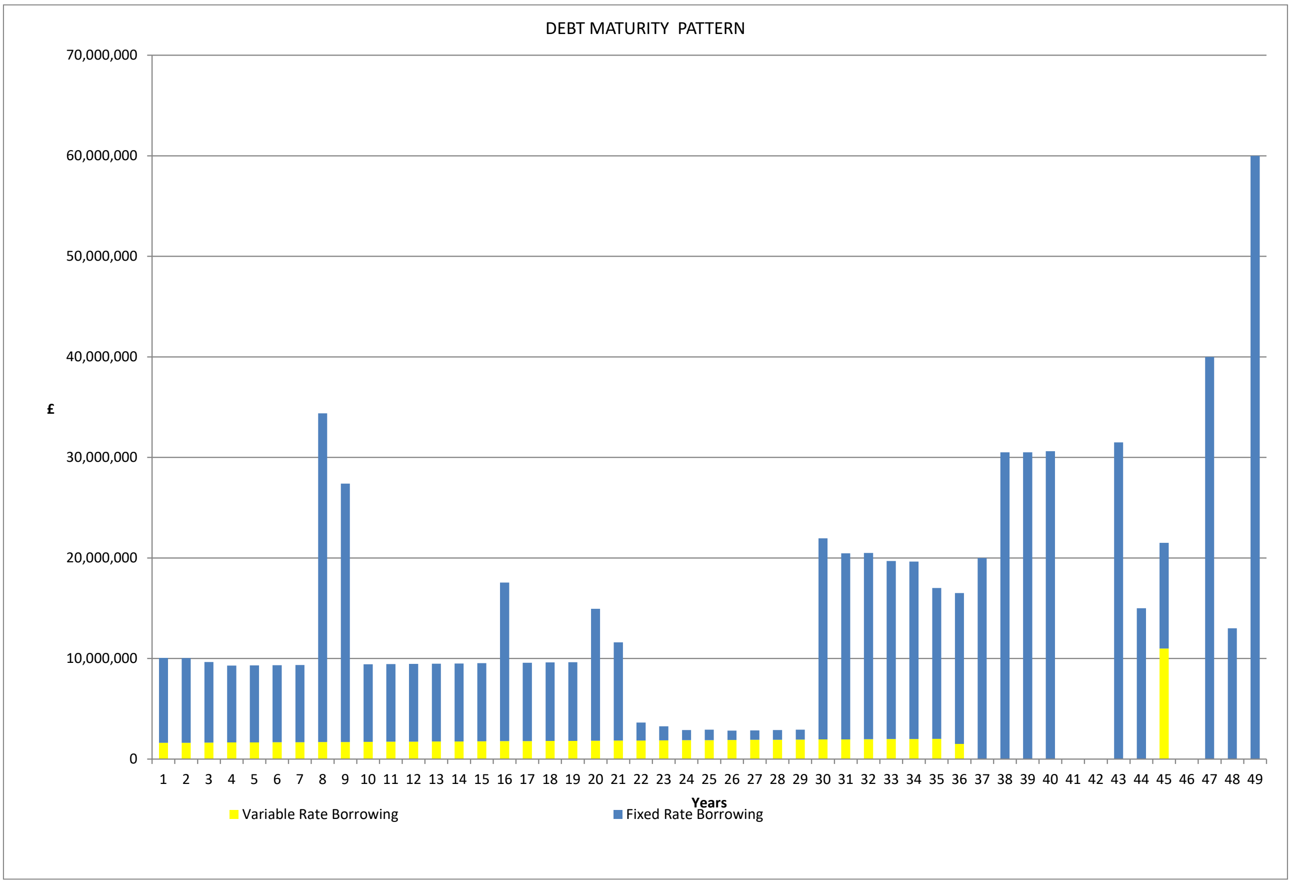
3. BORROWING ACTIVITY

Due to investment concerns, both counterparty risk and low investment returns, no borrowing was undertaken during the year.

The Council's underlying need to borrow on 31 March 2022 was £857m, £94m more than its actual gross debt of £763m. This shortfall of £94m is funded by internal borrowing from the Council's reserves and will need to be borrowed externally at some point in the future.

Debt rescheduling opportunities have been limited in the current economic climate and following the various increases in the margins added to gilt yields, which has affected PWLB new borrowing rates since October 2010. No debt rescheduling was undertaken during 2021/22.

The Council's gross debt on 31 March 2022 of £763m is within the Council's authorised limit (the maximum amount of borrowing permitted by the Council) of £876m and the Council's operational boundary (the maximum amount of borrowing that is expected) of £863m. The Council aims to have a reasonably even maturity profile so that the Council does not have to replace a large amount of borrowing in any particular year when interest rates might be high. The maturity profile of the Council's borrowing (see graph below) is within the limits contained in the Council's Treasury Management Policy.



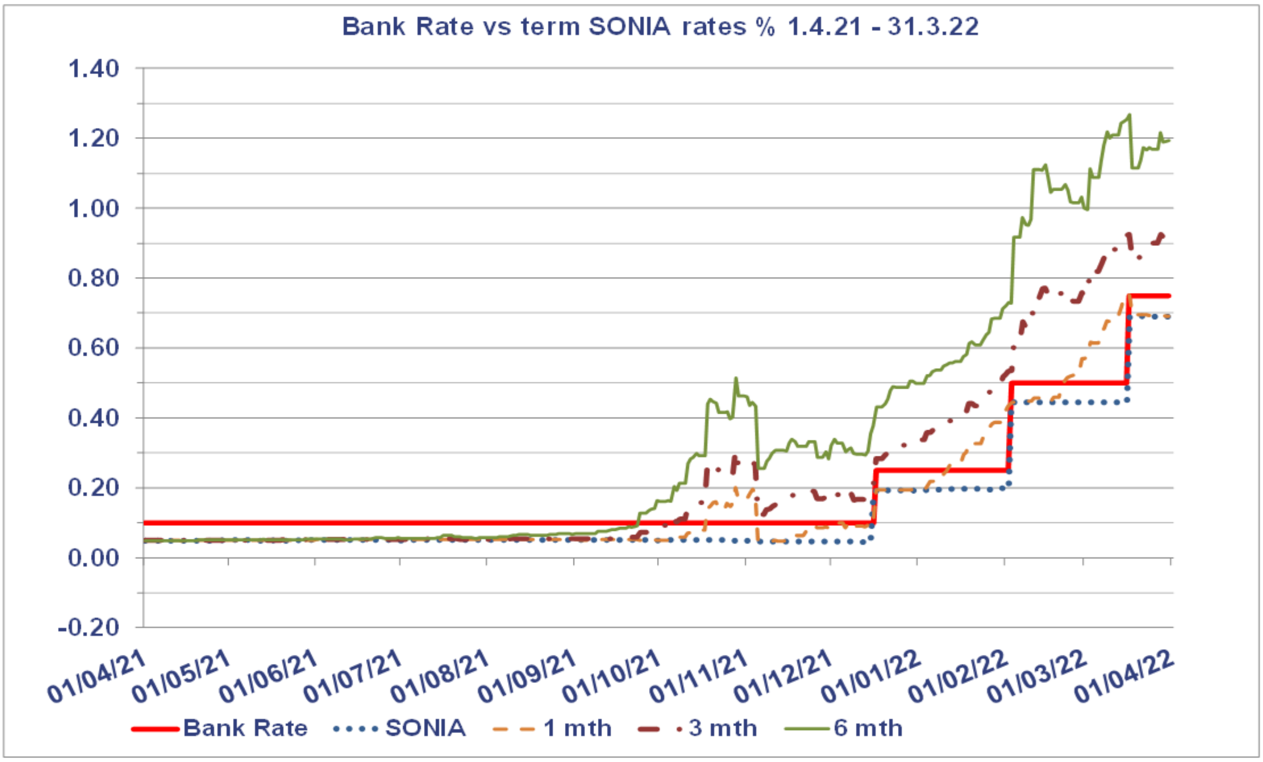
4. INVESTMENT ACTIVITY

Investment returns remained close to zero for much of 2021/22. The expectation for interest rates within the treasury management strategy for 2021/22 was that Bank Rate would remain at 0.1% until it was clear to the Bank of England that the emergency level of rates introduced at the start of the Covid-19 pandemic were no longer necessitated.

The Bank of England and the Government also maintained various monetary and fiscal measures, supplying the banking system and the economy with massive amounts of cheap credit so that banks could help cash-starved businesses to survive the various lockdowns/negative impact on their cashflow. The Government also supplied substantial amounts of finance to local authorities to pass on to businesses. This meant that for most of the year there was much more liquidity in financial markets than there was demand to borrow, with the consequent effect that investment earnings rates remained low until towards the turn of the year when inflation concerns indicated central banks, not just the Bank of England, would need to lift interest rates to combat the second-round effects of growing levels of inflation (CPI was 7.0% in March).

The Bank of England base rate was 0.10% until 16 December 2021 when it was increased to 0.25%. Further increases followed on 03 February 2022 to 0.50%, and on 17 March to 0.75%. This can be seen in the graph below, together with the effect on inter-bank lending rates.

Investment Benchmarking Data – Sterling Overnight Index Average 2021/22



While the Council has taken a cautious approach to investing, it is also fully appreciative of changes to regulatory requirements for financial institutions in terms of additional capital and liquidity that came about in the aftermath of the budgetary crisis. These requirements have provided a far stronger basis for financial institutions, with annual stress tests by regulators evidencing how institutions are now far more able to cope with extreme stressed market and economic conditions.

Investment balances have been kept to a minimum through the agreed strategy of using reserves and balances to support internal borrowing, rather than borrowing externally from the financial markets. External borrowing would have incurred an additional cost, due to the differential between borrowing and investment rates as illustrated in the charts shown above and below. Such an approach has also provided benefits in terms of reducing counterparty risk exposure, by having fewer investments placed in the financial markets.

The Council's investments averaged £449.5m during 2021/22. As of 31 March 2022, the Council had, £451.1m invested. The performance of the investment portfolio is summarized in the table below.

	Proportion of Portfolio	Return to December 2021	Return to March 2022
Externally Managed Funds Consisting of Tradable Instruments	3%	0.07%	-4.01%
Tradable Structured Interest-Bearing Deposit	2%	-1.76%	-1.21%
Vanilla Interest Bearing Deposits	95%	0.48%	0.48%
Overall Return	**100%**	**0.42%**	**0.31%**

There was a sharp decline in the overall performance of the portfolio in the last quarter of 2021/22 which was attributable to £12.6m invested in externally managed funds consisting of tradable instruments such as corporate bonds. This was caused primarily by a fall in the market value of existing tradable instruments driven by the increase in current interest rates. If a tradable instrument is paying interest at a rate below current market rates, its market value will be less if it is traded at that point. If a tradable instrument is held to maturity its value will still equal the principal invested plus accrued interest.

The Council also has £10m invested in a floating rate tradable structured interest-bearing note paying SONIA (0.69% on 31 March) plus 0.12% with a floor of 1.65% and a cap of 3.50% maturing on 07 June 2023. This note has paid 1.65% since inception. This was a good rate when the note was purchased in June 2018.

The bulk of the investment portfolio, 95%, is invested in vanilla interest-bearing deposits that have generated an average return of 0.48% through 2021/22.

27% of the investment portfolio matures in the first quarter of 2022/23, and this will provide the opportunity to re-invest funds at the higher rates available now.

5. REVENUE COSTS OF TREASURY MANAGEMENT ACTIVITIES IN 2021/22

Expenditure on treasury management activities in both the General Fund and the HRA against the revised budget is shown below.

	Revised Estimate 2021/22 £000	Actual 2021/22 £000	Variance +/- £000
Interest Payable:			
PWLB	19,257	19,257	-
Other Long-Term Loans	1,210	1,210	-
HCC Transferred Debt	284	279	(5)
Interest on Finance Lease	191	191	-
Interest on Service Concession Arrangements (including PFIs)	5,149	5,149	-
Interest Payable to External Organisations	9	10	1
Premiums and Discounts on Early Redemption of Debt	100	100	-
	26,200	**26,196**	**(4)**
Deduct			
Investment Income:			
Interest on Investments	(1,272)	(1,414)	(142)
Other interest receivable	(1,576)	(1,576)	-
	23,352	**23,206**	**(146)**
Provision for Repayment of Debt	**10,084**	**10,214**	**130**
Debt Management Costs	**549**	**560**	**11**
	33,985	**33,980**	**(5)**

Interest on investments was £142,000 higher than the budget. Although there was a sharp fall in the market value of tradable investments, the returns on new vanilla interest bearing deposits increased because of anticipation in the financial markets that there would be increases in the Bank of England's base rate.

The provision for the repayment of debt was £130,000 higher than the budget. This was due to additional provision having to be made because of decreases in the market value of some investment properties. Overall, though, the market value of the investment property portfolio did increase.

Overall net treasury management costs were £5,000 above the revised budget.

APPENDIX B

PRUDENTIAL AND TREASURY MANAGEMENT INDICATORS

1. Capital financing requirement	Original Estimate £'000	Revised Estimate £'000	Actual £'000
General Fund	720,426	655,251	628,168
Housing Revenue Account (HRA)	224,090	207,608	228,737
Total	944,516	862,859	856,905

2. Authorised Limit	Original Limit £'000	Revised Limit £'000	Actual £'000
Long Term Borrowing	911,532	824,971	711,272
Other Long Term Liabilities	51,340	51,340	51,340
Total	962,872	876,311	762,612

3. Operational Boundary	Original Limit £'000	Revised Limit £'000	Actual £'000
Long Term Borrowing	893,176	811,519	711,272
Other Long Term Liabilities	51,340	51,340	51,340
Total	944,516	862,859	762,612

4. Ratio of financing costs to net revenue stream	Original Estimate	Revised Estimate	Actual
General Fund	18.9%	16.7%	16.0%
Housing Revenue Account (HRA)	7.0%	6.5%	6.3%

5. Maturity Structure of Fixed Rate Borrowing	Lower Limit	Upper Limit	Actual
Under 12 months	0%	10%	1%
12 months and within 24 months	0%	10%	1%
24 months and within 5 years	0%	10%	4%
5 years and within 10 years	0%	20%	13%
10 years and within 20 years	0%	30%	14%
20 years and within 30 years	0%	40%	6%
30 years and within 40 years	0%	40%	34%
Over 40 years	0%	50%	27%

6. Maturity Structure of Variable Rate Borrowing	Lower Limit	Upper Limit	Actual
Under 12 months	0%	10%	2%
12 months and within 24 months	0%	10%	2%
24 months and within 5 years	0%	10%	7%
5 years and within 10 years	0%	20%	11%
10 years and within 20 years	0%	30%	23%
20 years and within 30 years	0%	40%	25%
30 years and within 40 years	0%	40%	15%
Over 40 years	0%	40%	15%

7. Principal sums invested over 365 days	Original Limit £'000	Revised Limit £'000	Actual £'000
Maturing after 31/3/2023	134,000	125,000	48,325
Maturing after 31/3/2024	103,000	50,000	8,800
Maturing after 31/3/2025	-	50,000	4,800

APPENDIX C

PRUDENTIAL AND TREASURY MANAGEMENT INDICATORS

1. ACTUAL CAPITAL FINANCING REQUIREMENT

This represents the underlying requirement to borrow for capital expenditure. It takes the total value of the City Council's fixed assets and determines the amount that has yet to be repaid or provided for within the Council's accounts.

The capital financing requirement is increased each year by any new borrowing and reduced by any provision for the repayment of debt. Broadly, the higher the capital financing requirement, the higher the amount that is required to be set aside for the repayment of debt in the following year.

2. AUTHORISED LIMIT

The authorised limit for external debt is the maximum amount of debt which the authority may legally have outstanding at any time. The authorised limit includes headroom to enable the Council to take advantage of unexpected movements in interest rates and to accommodate any short-term debt or unusual cash movements that could arise during the year.

3. OPERATIONAL BOUNDARY

The Operational Boundary is based on the probable external debt during the year. It is not a limit but acts as a warning mechanism to prevent the authorised limit (above) being breached.

4. RATIO OF FINANCING COSTS TO NET REVENUE STREAM 2021/22

This ratio reflects the annual cost of financing net debt as a proportion of the total revenue financing received. It therefore represents the proportion of the City Council's expenditure that is largely fixed and committed to repaying debt. The higher the ratio, the lower the flexibility there is to shift resources to priority areas and/or reduce expenditure to meet funding shortfalls.

For the General Fund, this is the annual cost of financing debt as a proportion of total income received from General Government Grants, Non-Domestic Rates and Council Tax.

The ratio of Housing Revenue Account (HRA) financing costs to net revenue stream is the annual cost of financing capital expenditure, as a proportion of total gross income received including housing rents and charges.

5. MATURITY STRUCTURE OF FIXED RATE BORROWING

The Council aims to have a reasonably even debt maturity profile so that it is not unduly exposed to refinancing risk in any particular year when interest rates may be high. The maturity structure of fixed rate borrowing matters less in future years as inflation will reduce the real value of the sums to be repaid.

6. MATURITY STRUCTURE OF VARIABLE RATE BORROWING

Variable rate borrowing could expose the Council to budgetary pressure if the interest rates increase. The maturity structure of variable rate borrowing matters less in future years as inflation will reduce the real value of the liability.

7. PRINCIPAL SUMS INVESTED FOR OVER 365 DAYS

Investing long term at fixed rates provides certainty of income and reduces the risk of interest rates falling.