Portsmouth CITY COUNCIL

Title of meeting:	Governance and Audit and Standards Committee Cabinet Full Council
Date of meeting:	Governance and Audit and Standards Committee 10 July 2024 Cabinet 23 July 2024 Full Council 15 October 2024
Subject:	Treasury Management Outturn Report 2023/24
Report by:	Director of Finance and Resources (Section 151 Officer)
Wards affected:	All
Key decision:	No
Full Council decision:	Yes

1. Purpose of report

To inform members and the wider community of the Council's treasury management activities in 2023/24 and of the Council's treasury management position as of 31 March 2024.

2. Recommendations

It is recommended that the Cabinet

1. Note the actual prudential and treasury management indicators based on the unaudited accounts, as shown in Appendix B, (an explanation of the prudential and treasury management indicators is contained in Appendix C).
2. Recommend that Full Council note the content of the report.

3. Background

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. The Code 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.

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4. Reasons for recommendations

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.

5. Integrated impact assessment

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.

6. Legal implications

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.

7. Director of Finance's comments

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

………………………………………………
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:

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

The recommendation(s) set out above were approved/ approved as amended/ deferred/ rejected by ……………………………… on ………………………………

………………………………………………
Signed by:

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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 2024, the Council had gross debt including finance leases and private finance initiative (PFI) schemes of £734m and gross investments of £302m giving rise to a net debt of £432m. Major components of the Council's gross investments of £302m include general and earmarked reserves of £267m and capital grants unapplied of £34m.

3. Borrowing Activity

During 2023/24, the Council maintained an under-borrowed position and so no new borrowing was undertaken. The Council's underlying need to borrow (the Capital Financing Requirement) was £969m on 31 March 2024, and was not fully funded with loan debt since, as mentioned, the Council's actual gross debt of £734m was being maintained at a lower level by using other cash balances (i.e. Earmarked Reserves and Capital Grants) on a temporary basis. This is also termed "Internal Borrowing" and amounted to £235m. This strategy is a prudent and cost-effective approach in the current economic climate but requires ongoing monitoring as interest rates start to fall.

If any new loans had been taken from the PWLB during 2023/24, the interest rates that would have been payable across the loan period are shown in Figure 1 below:

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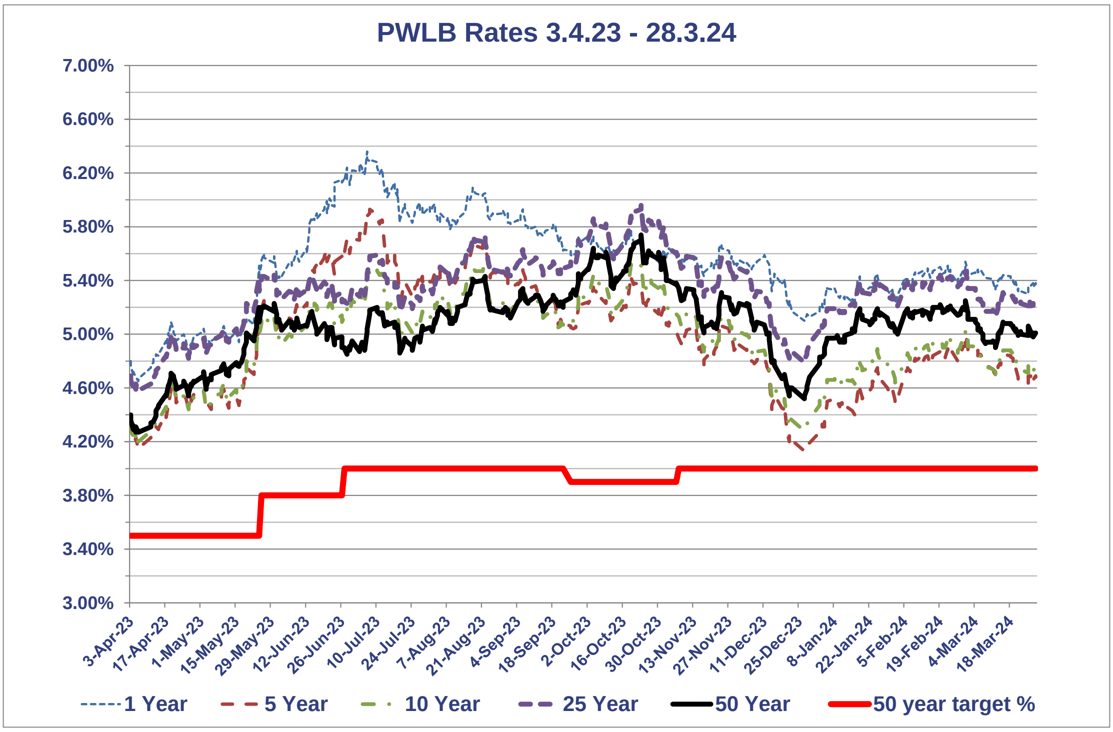

Figure 1: PWLB Certainty Rates available during 2023/24

Debt rescheduling opportunities have been limited in the current economic climate, as the average 1% differential between PWLB new borrowing rates and premature repayment rates (i.e. early redemption penalties) made rescheduling unviable. Therefore, no debt rescheduling, or early repayment of debt has been undertaken during 2023/24 as it has not been financially advantageous for the Council to do so.

The Council's gross debt on 31 March 2024 of £734m is within the Council's authorised limit (the maximum amount of borrowing permitted by the Council) of £1,029m and the Council's operational boundary (the maximum amount of borrowing that is expected) of £997m. 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.

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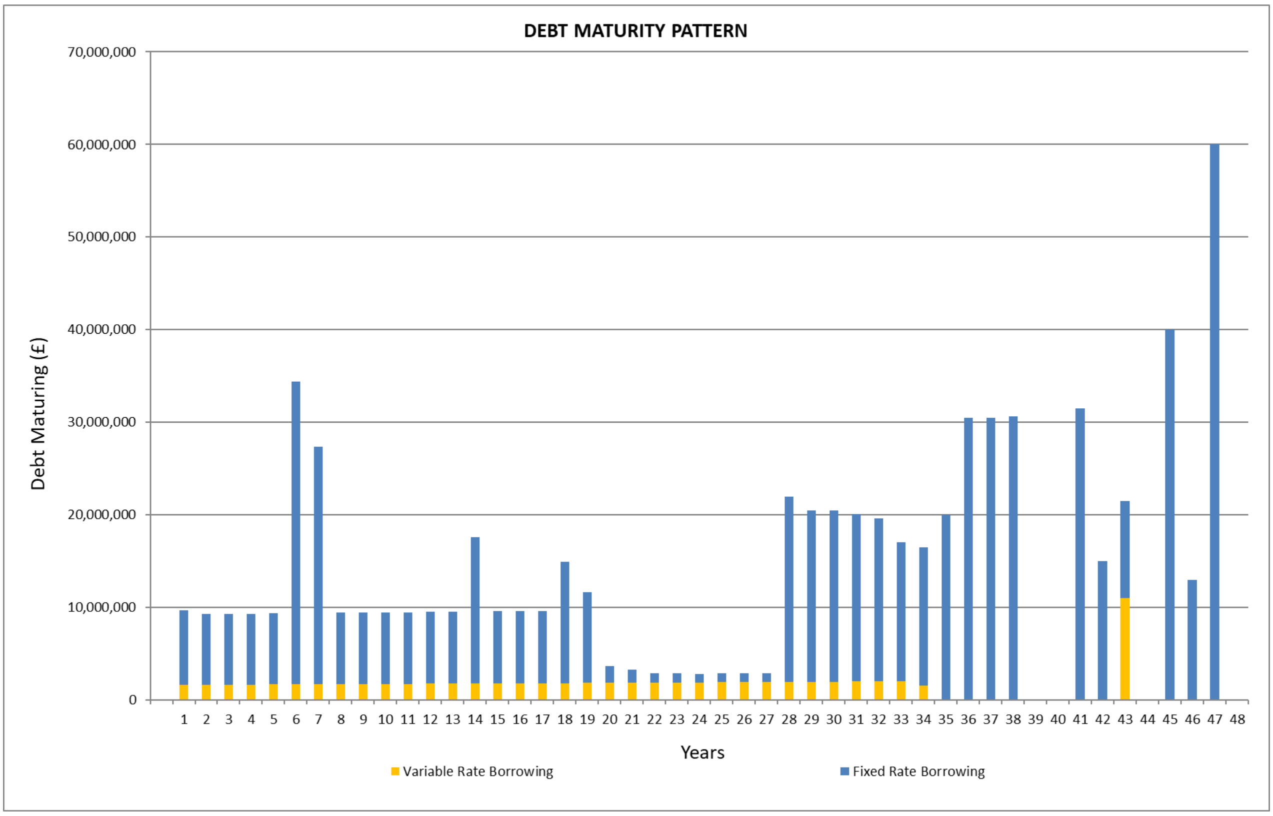

Figure 2: Debt Maturity Pattern for 2024/25 onwards

4. Investment Activity

Investment returns rose steadily for much of 2023/24 at a faster rate and to higher levels than forecast. Starting April at 4.25%, Bank Rate moved up in stepped increases of either 0.25% or 0.5%, reaching 5.25% by August 2023 and remained at this level to the end of the financial year.

Greater investment returns through higher interest rates came about during the year as central banks, including the Bank of England, realised that inflationary pressures were not transitory and tighter monetary policy was needed. As a result, an upward sloping yield curve prevailed throughout 2023/24. For local authorities with sufficient cash balances, this sea-change in investment rates emphasised the need for an appropriate balance to be achieved between maintaining cash for liquidity purposes and securing investments on a rolling basis to lock in the higher investment rates as they became available.

The change in the Bank Rate in the year can be seen in the graph below, together with the effect on inter-bank lending rates.

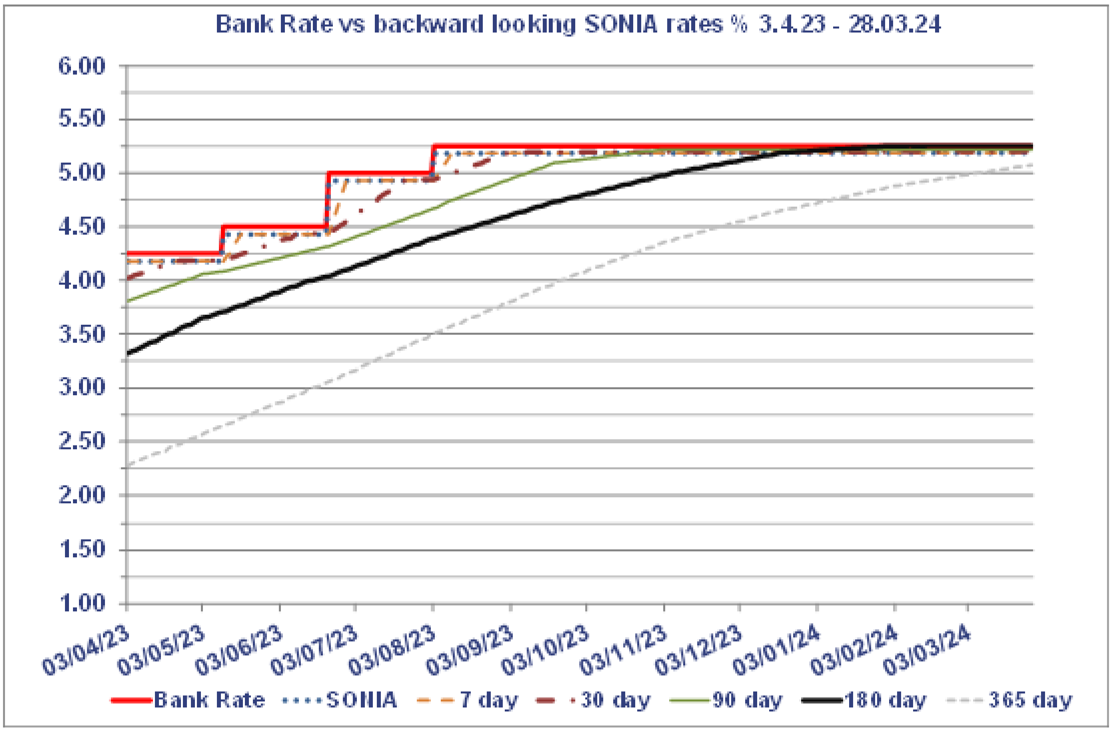

Figure 3: Investment Benchmarking Data - Sterling Overnight Index Averages (SONIA) Backward Looking 2023/24

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 Financial Crisis of 2008. 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.

For the Council, 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 higher borrowing costs as shown in figure 1 and lower investment returns for much of the year as illustrated in figure 3 above and the table below. The Council has therefore avoided taking on long-term borrowing at the elevated levels available and has focused on internal borrowing. 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 £405m during 2023/24. As at 31 March 2024, the Council had £302m invested. The main reason for the decrease, is due to the use of reserves and balances to facilitate the acquisition of the additional housing stock towards the end of February 2024.

The investment activities in the year conformed to the approved strategy, with the Council having no liquidity difficulties. The performance of the investment portfolio is summarized in the tables below.

Year	Overall Return
2021/2022	0.31%
2022/2023	1.42%
2023/2024	4.98%

Table 1: Annual Average Returns on Investments

	Average Value (Proportion) of Portfolio	Return to December 2023	Return to March 2024
Externally Managed Funds - Tradable Instruments	£11M (3%)	7.57%	5.47%
Tradable Structured Interest-Bearing Deposit	£10M (2%)	6.96%	3.03%
Vanilla Interest Bearing Deposits	£383M (95%)	4.73%	5.02%
Overall Return	**100%**	**4.86%**	**4.98%**

Table 2: Analysis of 2023/24 returns by investment type[1]

The overall improvement in the performance of the portfolio during 2023/24 was maintained in the last quarter of the year. This was due to the bulk of the investment portfolio continuing to be invested in vanilla interest-bearing deposits that have generated an average return of 5.02% through 2023/24.

This higher return was also enhanced by an improvement in the market value of externally managed funds over the course of this financial year. These funds consist of tradable instruments such as corporate bonds which make up 3% of the portfolio.

The Council also has £10m invested in two tradable structured interest-bearing notes until December 2024, at fixed interest rates of 3.76% and 3.82%. These tradable structured interest-bearing notes make up the remaining 2% of the investment portfolio. When a tradable instrument pays interest at a rate below current market rates, its reduced market value reflects its actual value at the point at which it is traded, resulting in the average return of 3.03% for 2023/24. However, if a tradable instrument is not traded but is held to maturity, then its value will be equal to the original principal sum invested plus the accrued interest earned at the fixed interest rates quoted above.

39% of the investment portfolio matures in the first quarter of 2024/25, any surplus funds available during this period will be reinvested in accordance with the Council's Treasury Management Strategy.

[1] Externally Managed Funds are traded on the open market and managed by an external asset management company
Tradable Structured Interest Bearing Deposit - are placed with financial institutions, are deposit accounts and may include complex structured financial instruments
Vanilla Interest Bearing Deposits are cash deposits that just earn interest, they are easily accessible and less complex

5. Revenue Costs of Treasury Management Activities in 2023/24

Net expenditure on treasury management activities, compared to the revised budget, for both the General Fund and the HRA are shown below.

GENERAL FUND	Revised Estimate 2023/24 £000	Actual 2023/24 £000	Variance +/- £000
Interest Payable:			
PWLB	18,742	18,742	-
Other Long-Term Loans	1,643	1,643	-
HCC Transferred Debt	651	651	-
Interest on Finance Lease	189	189	-
Interest on Service Concession Arrangements (including PFIs)	4,191	4,202	11
Interest Payable to External Organisations	23	58	35
Interest Payable on school and other internal balances	76	397	321
Interest recharged to HRA	(7,272)	(7,258)	14
Premiums and Discounts on Early Redemption of Debt	102	39	(63)
	18,345	**18,663**	**318**
Less Investment Income:			
Interest on Investments	(18,206)	(20,108)	(1,902)
Other interest receivable	(1,597)	(2,071)	(474)
Interest paid to HRA	1,506	1,961	455
Net Interest Paid	**48**	**(1,555)**	**(1,603)**
Provision for Repayment of Debt	**9,005**	**9,811**	**806**
Debt Management Costs	**858**	**825**	**(33)**
	9,911	**9,081**	**(830)**

Table 3: General Fund - Treasury Management Activities

HRA	Revised Estimate 2023/24 £000	Actual 2023/24 £000	Variance +/- £000
Interest Payable:			
PWLB	704	704	-
Interest Paid to the General Fund	7,272	7,258	(14)
	7,976	**7,962**	**(14)**
Less Investment Income:			
Interest received from the General Fund	(1,506)	(1,961)	(455)
Interest due to Leaseholders	132	132	0
	(1,374)	**(1,829)**	**(455)**
	6,602	**6,133**	**(469)**

Table 4: HRA - Treasury Management Activities

The largest variance for the General Fund relates to interest on investments as this was £1.9m higher than the revised estimate for the year. This was due to the stronger than expected rates available on investments, particularly in the latter part of the year as well as more surplus cash than anticipated being available to invest due to the large housing stock purchase taking place slightly later than planned. An additional £474,000 was also received from loans to external bodies, the majority of which was interest due on loans and advances that had been made to the Council's subsidiaries. This was partly offset by an increase in interest payable to external organisations compared to the budget of £321,000 due to a higher rate of interest being applied to the balances held for the Council's schools and other external bodies.

In turn, the HRA benefitted from £455,000 more in interest receipts from the General Fund due to its share of investment interest earnt on HRA balances.

The provision for the repayment of debt was £806,000 higher than the budget. £307,000 of this was due to additional provision having to be made because of decreases in the market value of some investment properties. The remainder was a result of reprofiling of the MRP applicable to existing assets to reflect the economic life of those assets more accurately.

Overall net treasury management costs for the General Fund and HRA combined were £1.3m below the revised budget.

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APPENDIX B - Prudential and Treasury Management Indicators

1. Capital financing requirement	Original Estimate	Revised Estimate	Actual
	£'000	£'000	£'000
General Fund	736,276	654,399	630,131
Housing Revenue Account (HRA)	331,292	342,621	338,851
Total	1,067,568	997,020	968,982

2. Authorised Limit	Original Limit	Revised Limit	Actual
	£'000	£'000	£'000
Long Term Borrowing	1,057,469	986,921	691,197
Other Long Term Liabilities	42,494	42,494	42,494
Total	1,099,963	1,029,415	733,691

3. Operational Boundary	Original Limit	Revised Limit	Actual
	£'000	£'000	£'000
Long Term Borrowing	1,025,074	954,526	691,197
Other Long Term Liabilities	42,494	42,494	42,494
Total	1,067,568	997,020	733,691

4. Ratio of financing costs to net revenue stream	Original Estimate	Revised Estimate	Actual
General Fund	10.5%	5.4%	4.3%
Housing Revenue Account (HRA)	6.9%	6.6%	6.0%

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%	10%
30 years and within 40 years	0%	40%	29%
Over 40 years	0%	40%	28%

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%	20%	7%
5 years and within 10 years	0%	20%	12%
10 years and within 20 years	0%	30%	25%
20 years and within 30 years	0%	40%	27%
30 years and within 40 years	0%	40%	10%
Over 40 years	0%	40%	15%

7. Principal sums invested over 365 days	Original Limit	Revised Limit	Actual
	£'000	£'000	£'000
Maturing after 31/3/2025	130,000	130,000	7,700
Maturing after 31/3/2026	50,000	50,000	4,800
Maturing after 31/3/2027	50,000	50,000	-

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APPENDIX C - Explanation of 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

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.

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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 over 365 Days

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