Quarter 1 Review 2022-23: Treasury Management and Annual Investment Strategy

Governance & Audit Committee	28 September 2022
Report Author	Chris Blundell, Acting Deputy Chief Executive and Section 151 Officer
Portfolio Holder	Councillor David Saunders, Cabinet Member for Finance
Status	For Decision
Classification	Unrestricted
Previously Considered by	N/A
Ward	Thanet Wide

Executive Summary:

This report summarises treasury management activity and prudential/ treasury indicators for the first quarter of 2022-23.

The Chartered Institute of Public Finance and Accountancy (CIPFA) defines treasury management as:

> *"The management of the local authority's borrowing, 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."*

The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This report is, therefore, important in that respect, as it provides details of the 2022-23 first quarter position for treasury activities.

Key reporting items to consider include:

- 2022-23 first quarter capital expenditure on long term assets was £2.1m (2021-22 Q1: £1.9m), against a full-year budget of £54.7m.
- The council's gross debt, also called the borrowing position, at 30 June 2022 was £20.0m (30 June 2021: £24.2m).
- The council's underlying need to borrow to finance its capital expenditure, also called the Capital Financing Requirement (CFR), is estimated to be £68.0m at 31 March 2023 as per the 2022-23 Treasury Management Strategy Statement (TMSS) (31 March 2022: £51.7m).
- The council has held less gross debt than its CFR and accordingly has complied with the requirement not to exceed its authorised borrowing limit of £81m.
- As at 30 June 2022 the council's investment balance was £50.8m (30 June 2021: £47.3m).

Recommendation(s):

That the Governance & Audit Committee notes, and makes comments on as appropriate, this report.

Corporate Implications

Financial and Value for Money

The financial implications are highlighted in this report.

Legal

Section 151 of the 1972 Local Government Act requires a suitably qualified named officer to keep control of the council's finances. For this council, this is the Acting Deputy Chief Executive, and this report is helping to carry out that function.

Risk Management

Risk management is as per the provisions of the annual TMSS, Minimum Revenue Provision Policy Statement and Annual Investment Strategy.

Corporate

Failure to undertake this process will impact on the council's compliance with the Treasury Management Code of Practice.

1 Background

1.1 Treasury management

CIPFA defines treasury management as:

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> *the effective control of the risks associated with those activities; and*
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The council operates a balanced budget, which broadly means cash raised during the year will meet its cash expenditure. Part of the treasury management operation is to ensure this cash flow is adequately planned, with surplus monies being invested in low risk counterparties, providing adequate liquidity initially before considering optimising investment return.

The second main function of the treasury management service is the funding of the council's capital plans. These capital plans provide a guide to the borrowing need of the council, essentially the longer term cash flow planning to ensure the council can meet its capital spending operations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses, and on occasion any debt previously drawn may be restructured to meet council risk or cost objectives.

2 Introduction

2.1 The CIPFA Code of Practice for Treasury Management recommends that members be updated on treasury management activities regularly (annual, mid-year and quarterly reports). This report, therefore, ensures this council is implementing best practice in accordance with the Code.

3 Treasury Management Strategy Statement and Annual Investment Strategy Update

3.1 The TMSS for 2022-23, which includes the Annual Investment Strategy, Capital Strategy and Non-Treasury Investment Report, was approved by the council on 10 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

3.2 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. Details of investments are shown in the table in section 5.4.

3.3 **Creditworthiness**
Significant levels of downgrades to Short and Long Term credit ratings have not materialised since the pandemic began in March 2020. In the main, where they did change, any alterations were limited to Outlooks (an indication of a credit rating agency's view regarding the potential direction of a credit rating). However, as economies have reopened, there have been some instances of previous lowering of Outlooks being reversed.

3.4 **Investment counterparty criteria**
The current investment counterparty criteria selection approved in the TMSS is meeting the requirement of the treasury management function as described in sections 1.1 and 3.2.

3.5 **CDS prices**
Although Credit Default Swap (CDS) prices (these are market indicators of credit risk) for banks (including those from the UK) spiked at the outset of the pandemic in 2020, they have subsequently returned to near pre-pandemic levels. However, sentiment can easily shift, so it remains important to undertake continual monitoring of all aspects of risk and return in the current circumstances.

3.6 **Investment balances**
The average level of funds available for investment purposes during the quarter was £53.960m. The level of funds available was mainly dependent on the timing of precept payments, receipt of grants and progress on the capital programme.

3.7 The yield on deposits for the first quarter of the financial year is 0.86% against a benchmark 7 day SONIA compounded rate of 0.78%.

The Council's budgeted investment return for 2022-23 is £167k (£42k quarter-year) and performance for the first quarter of the financial year is above budget at £115k.

3.8 **Approved limits**
Officers can confirm that the approved limits within the Annual Investment Strategy were not breached during the quarter ended 30th June 2022 except as described below.

3.9 Due to an error by one of the Council's financial providers, interest on a deposit in a money market fund was added to the deposit rather than being sent to the Council's bank account. This caused the Council's £6m limit per fund to be exceeded by £4,385 for the period from 1 June to 8 June 2022.

3.10 Despite reassurances to the contrary, the same error reoccured the following month, this time causing the limit to be exceeded by £5,335 from 1 July to 4 July 2022.

3.11 **Impact of inflation**

The significant increase in inflation has not been matched by the increase in interest rates, which has had an adverse impact on the real value (relative price adjusted for inflation) of the council's investment balances. However, the impact on the council's balance sheet as a whole has been acceptable, due to factors such as the council's borrowing requirement (as represented by the CFR) and its land and property assets. Inflation reduces the real value of the council's borrowing/debt whereas this is not necessarily the case for its land and property assets because, unlike the council's debt, their nominal value is variable.

As at 31 March 2022, the council's investments were £51.308m, its CFR was £51.679m and the net book value of its long term assets (property, plant, equipment, heritage assets and investment property) was £295.945m. (Please note that the council's 2021-22 accounts have not yet been audited and hence these figures are subject to change).

However, the council's treasury position is being reviewed and it is anticipated that, in connection with this, changes may be proposed to the 2022-23 Treasury Management Strategy Statement in the 2022-23 Mid Year Treasury Review report.

4 **Borrowing**

4.1 No new external borrowing was undertaken from the PWLB during the quarter ended 30th June 2022.

4.2 **PWLB maturity certainty rates year to date to 30th June 2022**
Gilt yields and PWLB rates were on a rising trend between 1st April and 30th June.

The 50 year PWLB target certainty rate for new long-term borrowing started 2022-23 at 2.20% before increasing to 2.70% in May before moving even higher to 3.40% in June.

4.3 **Debt rescheduling**

Debt rescheduling opportunities have been very limited in the current economic climate and following the various increases in the margins added to gilt yields which have impacted PWLB new borrowing rates since October 2010. No debt rescheduling has therefore been undertaken to date in the current financial year.

5 Compliance with Treasury and Prudential Limits

5.1 Prudential and treasury Indicators are shown below

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 TMSS for 2022-23, except as described in sections 3.8 to 3.10 above. The Director of Finance reports that no other difficulties are envisaged for the current or future years in complying with these indicators.

5.2 Indicator for Capital Expenditure

The revised GF budget includes net reprofiling of £27.028m (£42.478m unspent budgets from 2021-22 that have been rolled into 2022-23 less £15.450m subsequently transferred to 2023-24). The revised HRA budget reflects the reprofiling of £15.279m budget from 2022-23 to 2023-24.

Capital Expenditure	2022-23 Original Budget £m	Actual spend as at 30-06-22 £m	2022-23 Revised Budget £m
General Fund	18.710	1.215	46.241
HRA	21.998	0.872	8.454
Total	**40.708**	**2.087**	**54.695**

Monitoring information on the capital programme at scheme level, including forecasts to the end of the financial year, is included in the regular Cabinet Budget Monitoring Reports.

5.3 Indicators for Borrowing Activity

5.3.1 A key control over the treasury activity is a prudential indicator to ensure that over the medium term, borrowing will only be for a capital purpose. Gross external borrowing should not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional CFR for 2022-23 and next two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue or speculative purposes.

5.3.2 **Operational boundary:** This is the limit beyond which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt and the ability to fund under-borrowing by other cash resources.

5.3.3 **Authorised Limit:** This represents the limit beyond which borrowing is prohibited, and needs to be set and revised by Members. It reflects the level of borrowing which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. It is the expected maximum borrowing need with some headroom for unexpected movements. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003.

	£m
Gross external debt as at 30 June 2022	20.047
CFR as at 31 March 2022	51.679
CFR as at 31 March 2023 (estimate as per 2022-23 TMSS)	67.963
Operational Boundary (debt) 2022-23	76.000
Authorised Limit (debt) 2022-23	81.000

The Section 151 Officer reports that no difficulties are envisaged for the current or future years in complying with these prudential indicators.

5.3.4 **Maturity Structures of Borrowing:** These gross limits are set to reduce the council's exposure to large fixed rate sums falling due for refinancing.

	2022-23 Original Upper Limit	Current Position – Actual at 30-06-22	2022-23 Revised Upper Limit
Maturity structure of fixed rate borrowing			
Under 12 months	50%	24.1%	50%
1 year to under 2 years	50%	0.7%	50%
2 years to under 5 years	50%	13.3%	50%
5 years to under 10 years	50%	11.7%	50%
10 years to under 20 years	50%	35.6%	50%
20 years to under 30 years	50%	9.6%	50%
30 years to under 40 years	50%	0.0%	50%
40 years to under 50 years	50%	5.0%	50%
50 years and above	50%	0.0%	50%

The current position shows the actual percentage of fixed rate debt the authority has within each maturity span. None of the upper limits have been breached.

5.4 Indicator for Investments

The council held £50.827m of investments as at 30 June 2022, with maturities all under one year (£51.758m at 31 March 2022). The constituent investments are:

Sector	Country	Total £m
Banks	UK	4.634
Money Market Funds	UK	45.193
Bond Funds	UK	1.000
Total		**50.827**

6 Options

6.1 The recommended option (to ensure regulatory compliance as set out in section 1 of this report) is that the Governance & Audit Committee notes, and makes comments on as appropriate, this report.

6.2 Alternatively, the Governance & Audit Committee may decide not to do this and advise the reason(s) why.

7 Disclaimer

7.1 This report (including annexes) is a technical document focussing on public sector investments and borrowings and, as such, readers should not use the information contained within the report to inform personal investment or borrowing decisions. Neither Thanet District Council nor any of its officers or employees makes any representation or warranty, express or implied, as to the accuracy or completeness of the information contained herein (such information being subject to change without notice) and shall not be in any way responsible or liable for the contents hereof and no reliance should be placed on the accuracy, fairness or completeness of the information contained in this document. Any opinions, forecasts or estimates herein constitute a judgement and there can be no assurance that they will be consistent with future results or events. No person accepts any liability whatsoever for any loss howsoever arising from any use of this document or its contents or otherwise in connection therewith.

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Reporting to: Colin Carmichael, Interim Chief Executive

Corporate Consultation Undertaken

Finance: N/A
Legal: Sameera Khan, Interim Head of Legal & Monitoring Officer