Appendix A

Treasury Management Outturn Performance Review

1.0 Introduction

The Council adopted the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice* (the CIPFA Code) which requires the Council to approve treasury management semi-annual and annual reports.

The Council's treasury management strategy for 2021/22 was approved at a meeting on 24th February 2021. The Council does borrow and invest substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk remain central to the Council's treasury management strategy.

Treasury risk management at the Authority is conducted within the framework of the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice (the CIPFA Code) which requires the Authority to approve a treasury management strategy before the start of each financial year and, as a minimum, a semi-annual and annual treasury outturn report.

The Prudential Code includes a requirement for local authorities to provide a Capital Strategy, a summary document approved by full Council covering capital expenditure and financing, treasury management and non-treasury investments. The Authority's Capital Strategy, complying with CIPFA's requirement, was approved by full Council on 24th February 2021.

2.0 External Context

2.1 Economic background

The continuing economic recovery from coronavirus pandemic, together with the war in Ukraine, higher inflation, and higher interest rates were major issues over the period.

Bank Rate was 0.1% at the beginning of the reporting period. April and May saw the economy gathering momentum as the shackles of the pandemic restrictions were eased. Despite the improving outlook, market expectations were that the Bank of England would delay rate rises until 2022. Rising, persistent inflation changed that.

UK CPI was 0.7% in March 2021 but thereafter began to steadily increase. Initially driven by energy price effects and by inflation in sectors such as retail and hospitality which were re-opening after the pandemic lockdowns, inflation then was believed to be temporary. Thereafter price rises slowly became more widespread, as a combination of rising global costs and strong demand was exacerbated by supply shortages and transport dislocations. The surge in wholesale gas and electricity prices led to elevated inflation expectations. CPI for February 2022 registered 6.2% year on year, up from 5.5% in the previous month and the highest reading in the National Statistic series. Core inflation, which excludes the more volatile components, rose to 5.2% year on year from 4.4%.

Following the pandemic the labour market began to tighten and demand for workers grew strongly as employers found it increasingly difficult to find workers to fill vacant jobs. Having peaked at 5.2% in December 2020, unemployment continued to fall and the most recent labour market data for the three months to January 2022 showed the unemployment rate at 3.9% while the employment rate rose to 75.6%. Headline 3-month average annual growth rate for wages were 4.8% for total pay and 3.8% for regular pay. In real terms, after adjusting for inflation, total pay growth was up 0.1% while regular pay fell by 1.0%.

With the fading of lockdown restraints, activity in consumer-facing sectors improved substantially as did sectors such as oil and mining with the reopening of oil rigs but materials shortages and the reduction in the real spending power of households and businesses dampened some of the growth momentum. Gross domestic product (GDP) grew by an upwardly revised 1.3% in the fourth calendar quarter of 2021 according to the final estimate (initial estimate 1.0%) and took UK GDP to just 0.1% below where it was before the pandemic. The annual growth rate was revised down slightly to 7.4% (from 7.5%) following a revised 9.3% fall in 2020.

Having increased Bank Rate from 0.10% to 0.25% in December, the Bank of England raised it further to 0.50% in February and 0.75% in March. At the meeting in February, the Monetary Policy Committee (MPC) voted unanimously to start reducing the stock of its asset purchase scheme by ceasing to reinvest the proceeds from maturing bonds as well as starting a programme of selling its corporate bonds.

In its March interest rate announcement, the MPC noted that the invasion of Ukraine had caused further large increases in energy and other commodity prices, with the expectation that the conflict will worsen supply chain disruptions around the world and push CPI inflation to around 8% later in 2022, even higher than forecast only a month before in the February Monetary Policy Report. The Committee also noted that although GDP in January was stronger than expected with business confidence holding up and the labour market remaining robust, consumer confidence had fallen due to the squeeze in real household incomes.

GDP growth in the euro zone increased by 0.3% in calendar Q4 2021 following a gain of 2.3% in the third quarter and 2.2% in the second. Headline inflation remains high, with CPI registering a record 7.5% year-on-year in March, the ninth successive month of rising inflation. Core CPI inflation was 3.0% year on year in March, was well above the European Central Bank's target of 'below, but close to 2%, putting further pressure on its long-term stance of holding its main interest rate of 0%.

The US economy expanded at a (downwardly revised) annualised rate of 6.9% in Q4 2021, a sharp increase from a gain of 2.3% in the previous quarter. In its March 2022 interest rate announcement, the Federal Reserve raised the Fed Funds rate to between 0.25% and 0.50% and outlined further increases should be expected in the coming months. The US Federal Reserve also repeated its plan to reduce the asset purchase programme which may start by Summer 2022.

2.2 Credit review

In the first half of 2021/22 credit default swap (CDS) spreads were flat over most of period and are broadly in line with their pre-pandemic levels. In September spreads rose by a few basis points due to concerns around Chinese property developer Evergrande defaulting but then fell back. Fitch and Moody's revised upward the outlook on a number of UK banks and building societies on the Authority's counterparty to 'stable', recognising their improved capital positions compared to 2020 and better economic growth prospects in the UK.

Fitch also revised the outlook for Nordea, Svenska Handelsbanken and Handelsbanken plc to stable. The agency considered the improved economic prospects in the Nordic region to have reduced the baseline downside risks it previously assigned to the lenders.

Having completed its full review of its credit advice on unsecured deposits, in September Arlingclose extended the maximum duration limit for UK bank entities on its recommended lending list from 35 days to 100 days; a similar extension was advised in December for the non-UK banks on this list.

2.3 Financial markets

The conflict in Ukraine added further volatility to the already uncertain inflation and interest rate outlook over the period. The Dow Jones started to decline in January but remained above its pre-pandemic level by the end of the period while the FTSE 250 and FTSE 100 also fell and ended the quarter below their pre-March 2020 levels.

Bond yields were similarly volatile as the tension between higher inflation and flight to quality from the war pushed and pulled yields, but with a general upward trend from higher interest rates dominating as yields generally climbed.

The 5-year UK benchmark gilt yield began the quarter at 0.82% before rising to 1.41%. Over the same period the 10-year gilt yield rose from 0.97% to 1.61% and the 20-year yield from 1.20% to 1.82%.

The Sterling Overnight Rate (SONIA) averaged 0.39% over the quarter.

2.4 Regulatory changes

In August 2021 HM Treasury significantly revised guidance for the PWLB lending facility with more detail and 12 examples of permitted and prohibited use of PWLB loans. Authorities that are purchasing or intending to purchase investment assets primarily for yield will not be able to access the PWLB except to refinance existing loans or externalise internal borrowing. Acceptable use of PWLB borrowing includes service delivery, housing, regeneration, preventative action, refinancing and treasury management.

CIPFA published its revised Prudential Code for Capital Finance and Treasury Management Code on 20th December 2021. The key changes in the two codes are around permitted reasons to borrow, knowledge and skills, and the management of non-treasury investments. Whilst the principles of the Prudential Code took immediate effect revised reporting requirements will commence in 2023/24.

3.0 Local Context

On 31st March 2022, the Council had net investing of £14.15m arising from its revenue income and capital income and expenditure. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. These factors are summarised in Table 1 below.

Table 1: Balance Sheet Summary

	31.3.22 Actual £m
General Fund CFR	70.4
Less: *Other debt liabilities	0.5
Total CFR	**69.9**

External borrowing	38.9
Internal borrowing	**31.0**
Less: Usable reserves	74.6
Less: Working capital[1]	31.7
Net (Investing) or New Borrowing	**(75.3)**

Note [1] Current assets less current liabilities.

The Council pursued its strategy of keeping borrowing and investments below their underlying levels, sometimes known as internal borrowing, to reduce risk and keep interest costs low.

The treasury management position as at 31st March 2022 and the change during the year is shown in Table 2 below.

Table 2: Treasury Management Summary

	30.3.21 Balance £m	Movement £m	31.3.22 Balance £m	31.3.22 Rate %
Long-term borrowing	39.43	(0.51)	38.92	2.83
Short-term borrowing	0.00	0.00	0.00	0.00
Total borrowing	**39.43**	**(0.51)**	**38.92**	
Long-term investments	4.00	0.00	4.00	3.62
Short-term investments	0.00	21.00	21.00	0.32
Cash and cash equivalents	28.34	(0.27)	28.07	0.45
Total investments	**32.34**	**20.73**	**53.07**	
Net borrowing	**7.09**		**(14.15)**	

The movement in the cash and cash equivalent has been as result of council tax and NNDR receipts and Government cash funding for Covid 19 (temporary holding of business grants from Central Government and increased S31 Grant income); these funds were invested in bank deposits and Money Market Funds for easy access and liquidity reasons.

3.1 Borrowing Strategy during the period

At 31st March 2022, the Council held £38.92m of loans, a decrease of £0.51m from 31st March 2021. Outstanding loans on 31st March are summarised in Table 3 below.

Table 3: Borrowing Position

	30.3.21 Balance £m	Net Movement £m	31.3.22 Balance £m	31.3.22 Weighted Average Rate %	31.3.22 Weighted Average Maturity (years)
Public Works Loan Board	39.43	-0.51	38.92	2.83%	22.3
Local authorities (short-term)	0.00	0.00	0.00	0.00%	0.0
Total borrowing	**39.43**	**-0.51**	**38.92**		**22.3**

The Council's chief objective when borrowing has been to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required, with flexibility to renegotiate loans should the Council's long-term plans change being a secondary objective.

With short-term interest rates remaining much lower than long-term rates, the Council considered it to be more cost effective in the near term to use internal resources or short-term loans instead. The Council had not used short-term loans facility so far in this financial year.

Although it was anticipated that the Council's CFR would increase due to the capital programme. However some schemes have been delayed, and also schemes that have gone ahead have been funded by grants, with the result that no new loans have been taken out.

Long-dated Loans borrowed	PWLB Reference	Amount £	Rate %	Period (Years)
PWLB 1	495152	5,000,000	3.91	36
PWLB 2	495153	5,000,000	3.90	35
PWLB 3	502463	246,843	2.24	1
PWLB 4	504487	657,174	3.28	24
PWLB 5	504598	872,921	3.10	25
PWLB 6	504810	434,680	2.91	25
PWLB 7	504922	353,772	3.10	25
PWLB 8	504993	286,425	2.92	25
PWLB 9	505255	565,688	2.31	25

PWLB 10	505372	433,927	2.18	25
PWLB 11	505649	777,720	2.67	26
PWLB 12	506436	5,000,000	2.78	15
PWLB 13	508696	7,280,439	2.49	17
PWLB 15	509389	11,963,000	2.18	17
Total borrowing		**38,883,833**	**2.83**	**23**

The Council's borrowing decisions are not predicated on any one outcome for interest rates and a balanced portfolio of short- and long-term borrowing was maintained.

3.2 Treasury Investment Activity

The Council holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. The investment position is shown in table 4 below.

Table 4: Treasury Investment Position

The weighted average interest rate for the investment portfolio up to 31.03.2022 was 0.82%.

	30.3.21 Balance £	Net Movement £m	31.3.22 Balance £m	31.3.22 Weighted Income Return* %	31.3.22 Weighted Average Maturity days
Banks & building societies (unsecured)	14,693,000	(9,626,000)	5,067,000	0.01%	1
Government (incl. local authorities)	0	21,000,000	21,000,000	0.32%	97
Money Market Funds	13,650,000	9,350,000	23,000,000	0.44%	1
Loans to other organisation	7,252,900	(277,700)	6,975,200	2.54%	>365
Other Pooled Funds .					
- *Property funds*	4,000,000	0	4,000,000	3.62%	>365
Total investments	**39,595,900**	**20,446,300**	**60,042,200**	**0.82%**	

*Weighted Income return is based on the rate of return and the investments held as at 31/03/2022

3.3 Risk Management

Both the CIPFA Code and government guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its treasury investments before seeking the optimum rate of return, or yield. The Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

Given the increasing risk and low returns from short-term unsecured bank investments, the Council has maintained a diversified portfolio of asset classes as shown in table 4 above.

The progression of risk and return metrics are shown in the extracts from Arlingclose's quarterly investment benchmarking in Table 5 below.

Table 5: Investment Benchmarking – Treasury investments managed in-house

	Credit Score	**Credit Rating**	**Bail-in Exposure %**	**Weighted Average Maturity (days)**	**Rate of Return %**
30.09.2021	4.54	A+	82	3	0.63
31.03.2022	4.10	AA-	57	15	0.82
Similar LAs	4.37	AA-	61	43	1.18
All LAs	4.39	AA-	60	14	0.97

*Weighted average maturity

£4.0m of the Council's investments are held in externally managed strategic pooled property funds – CCLA Property Fund where short-term security and liquidity are lesser considerations, and the objectives instead are regular revenue income and long-term price stability. This fund generated a total return of £144,951 (3.62%), for period of 1st April to 31st March 2022 which is used to support services in year.

Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Council's investment objectives are regularly reviewed. Strategic fund investments are made in the knowledge that capital values will move both up and down on months, quarters and even years; but with the confidence that over a three- to five-year period total returns will exceed cash interest rates. In light of their performance over the medium-term and the Council's latest cash flow forecasts, investment in these funds has been maintained.

3.4 Non-Treasury Investments

The definition of investments in CIPFA's revised Treasury Management Code now covers all the financial assets of the Council as well as other non-financial assets which the Authority holds primarily for financial return. This is replicated in DLUHC's Investment Guidance, in which the definition of investments is further broadened to also include all such assets held partially for a financial return.

The Authority also held £69.6m of such investments in:

- directly owned property £69.5m
- shareholding in subsidiaries £0.1m (not yet active)

Table 6: Property held for investment purposes in £'000

Property	**Actual**	**31.3.2022 actual**	
	31st Mar 2021	**Gains or (losses)**	**Value in accounts**
Existing Portfolio	33,891	(290)	33,601
Unit 8 Stonehill	2,150	0	2,150
80 Wilbury Way	1,775		1,775
Shawlands Retail Park	5,543	(20)	5,523
1400 & 1500 Parkway, Fareham	4,200	(50)	4,150
Units 21a, 21b,23a,b,c Little End Road, St Neots	3,400	(110)	3,290
Rowley Centre, St Neots	4,008	(705)	3,303
Tri-link, Wakefield	14,250	(50)	14,200
Alms Close	1,503	20	1,523
TOTAL	**70,720**	**(1,205)**	**69,515**

These investments generated £4.85m of investment income for the Authority for 2021/22, generating a yield of 6.98%.

The Authority is dependent on profit generating investment activity to achieve a balanced revenue budget. The table below shows the extent to which the expenditure planned to meet the service delivery objectives and/or place making role of the Authority is dependent on achieving the expected net profit from investments over the lifecycle of the Medium-Term Financial Strategy.

Table 7: Proportionality of Investments in £'000

	2019/20 Actual £000s	2020/21 Actual £000s	2021/22 Actual(2) £000s	2022/23 Budget £000s	2023/24 Budget £000s
Gross service expenditure	72,470	121,354(1)	83,281	64,296	63,936
Investment income					
Commercial Property	5,117	4,892	4,869	4,716	4,650
Service Investments	313	293	275	325	325
Proportion	7.49%	4.27%(1)	6.18%	7.84%	7.78%

Notes (1) Gross expenditure higher than normal due to covid business grant expenditure. (2) Provisional figures.

4.0 Compliance

The Chief Finance Officer (s151 officer) reports that all treasury management activities undertaken during the financial year complied fully with the CIPFA Code of Practice and the Council's approved Treasury Management Strategy. Compliance with specific investment limits is demonstrated in table 9 below.

Compliance with the authorised limit and operational boundary for external debt is demonstrated in table 8 below.

Table 8: Debt Limits

	31.3.22 Actual £m	2021/22 Operational Boundary £m	2021/22 Authorised Limit £m	Complied?
General	10.04	70.00	80.00	Yes
Loans	4.63	15.00	20.00	Yes
CIS	24.25	30.00	35.00	Yes
Total debt	**38.92**	**115.00**	**135.00**	

Since the operational boundary is a management tool for in-year monitoring it is not significant if the operational boundary is breached on occasions due to variations in cash flow, and this is not counted as a compliance failure. Total debt was below the operational boundary all through the quarter.

Table 9: Investment Limits

	31.3.22 Actual £m	2021/22 Limit £m	Complied?
Deposit Accounts			
NatWest	5.07	Unlimited*	Yes
Government and LAs			
Debt Management Office (DMO) - HMG	17.00	unlimited	Yes
Thurrock Council	4.00	4.00	Yes
Money Market Funds			
Aberdeen Liquidity Fund	4.00	4.00	Yes
BlackRock Institutional sterling liquidity Fund	4.00	4.00	Yes
CCLA Public Sector Deposit Fund	4.00	4.00	Yes
Federated Short Term Prime Fund	4.00	4.00	Yes
Insight Liquidity Funds	1.50	4.00	Yes
Invesco	4.00	4.00	Yes
Legal & General Sterling Liquidity Fund	1.50	4.00	Yes
Total	**49.07**		

*Unlimited as this is the Council's transactional bank.

5.0 Treasury Management Indicators

The Council measures and manages its exposures to treasury management risks using the following indicators.

Security

The Council has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average credit rating of its investment portfolio. This is calculated by applying a score to each investment (AAA=1, AA+=2, etc.) and taking the arithmetic average, weighted by the size of each investment. Unrated investments are assigned a score based on their perceived risk.

	31.3.22 Actual	2021/22 Target	Complied?
Portfolio average credit rating	AA-	A-	Yes

Liquidity

The Council has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments within a rolling three-month period, without additional borrowing.

	30.3.22 Actual £m	2021/22 Target £m	Complied?
Total cash available within 3 months	28.07	2	Yes

Interest Rate Exposures

This indicator is set to control the Council's exposure to interest rate risk. The upper limits on the one-year revenue impact of a 1% rise or fall in interest were:

Interest rate risk indicator	31.3.22 Actual	2021/22 Limit	Complied?
Upper limit on one-year revenue impact of a 1% rise in interest rates	£503,500 (Income)	£128,000 (Expenditure)	Yes
Upper limit on one-year revenue impact of a 1% fall in interest rates	£34,600 (Expenditure)	£128,000 (Expenditure)	Yes

The impact of a change in interest rates is calculated on the assumption that maturing loans and investments will be replaced at current rates of the existing loans and investments. It is also assumed that the loans to be refinanced are those up to 24 months from 31st March 2022 (£246,843 PWLB 3).

Maturity Structure of Borrowing

This indicator is set to control the Council's exposure to refinancing risk. The upper and lower limits on the maturity structure of all borrowing were:

Borrowing Maturing	31.3.22 Actual	Upper Limit	Lower Limit	Complied?
Under 12 months	0.0%	80%	0%	Yes
12 months and within 24 months	0.6%	80%	0%	Yes
24 months and within 5 years	0.1%	80%	0%	Yes
5 years and within 10 years	0.0%	100%	0%	Yes
10 years and within 20 years	62.3%	100%	0%	Yes
20 years and above	37.0%	100%	0%	Yes
Total	**100%**			