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 2022/23 was approved at a meeting on 23rd February 2022. 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 23rd February 2022.

2.0 External Context

2.1 The UK Economy

(This commentary has been provided by Link Group, the council's new treasury advisors from March 2023)

Against a backdrop of stubborn inflationary pressures, the easing of Covid restrictions in most developed economies, the Russian invasion of Ukraine, and a range of different UK Government policies, it is no surprise that UK interest rates have been volatile right across the curve, from Bank Rate through to 50-year gilt yields, for all of 2022/23.

Market commentators' misplaced optimism around inflation has been the root cause of the rout in the bond markets with, for example, UK, EZ and US 10-year yields all rising by over 200bps in 2022. The table below provides a snapshot of the conundrum facing central banks: inflation is elevated but labour markets are extra-ordinarily tight, making it an issue of fine judgment as to how far monetary policy needs to tighten.

Table 1: Economic Indicators

	UK	Eurozone	US
Bank Rate	4.25%	3%	4.75%-5%
GDP	+0.1%q/q Q4 (4.1%y/y)	+0.1%q/q Q4 (1.9%y/y)	2.6% Q4 Annualised
Inflation	10.4%y/y (Feb)	6.9%y/y (Mar)	6.0%y/y (Feb)
Unemployment Rate	3.7% (Jan)	6.6% (Feb)	3.6% (Feb)

Quarter 2 of 2022 saw UK GDP deliver growth of +0.1% quarter/quarter, but this was quickly reversed in the third quarter, albeit some of the fall in GDP can be placed at the foot of the extra Bank Holiday in the wake of the Queen's passing. Quarter 4 GDP was positive at 0.1% quarter/quarter. Most recently, January saw a 0.3% month/month increase in GDP as the number of strikes reduced compared to December. In addition, the resilience in activity at the end of 2022 was, in part, due to a 1.3% quarter/quarter rise in real household disposable incomes. A big part of that reflected the £5.7bn payments received by households from the government under the Energy Bills Support Scheme.

Nevertheless, CPI inflation picked up to what should be a peak reading of 11.1% in October, although hopes for significant falls from this level will very much rest on the movements in the gas and electricity markets, as well as the supply-side factors impacting food prices. On balance, most commentators expect the CPI measure of inflation to drop back towards 4% by the end of 2023. As of February 2023, CPI was 10.4%.

The UK unemployment rate fell through 2022 to a 48-year low of 3.6%, and this despite a net migration increase of around 500k. The fact remains, however, that with many economic participants registered as long-term sick, the UK labour force shrunk by around 500k in the year to June. Without an increase in the labour force participation rate, it is hard to see how the UK economy will be able to grow its way to prosperity, and with average wage increases running at over 6% the MPC will be concerned that wage inflation will prove just as sticky as major supply-side shocks to food (up 18.3% year/year in February 2023) and energy that have endured since Russia's invasion of Ukraine on 22 February 2022.

Bank Rate increased steadily throughout 2022/23, starting at 0.75% and finishing at 4.25%.

In the interim, following a Conservative Party leadership contest, Liz Truss became Prime Minister for a tumultuous seven weeks that ran through September and October. Put simply, the markets did not like the unfunded tax-cutting and heavy spending policies put forward by her Chancellor, Kwasi Kwarteng, and their reign lasted barely seven weeks before being replaced by Prime Minister Rishi Sunak and Chancellor Jeremy Hunt. Their Autumn Statement of the 17th of November gave rise to a net £55bn fiscal tightening, although much of the "heavy lifting" has been left for the next Parliament to deliver. However, the markets liked what they heard, and UK gilt yields have reversed the increases seen under the previous tenants of No10/11 Downing Street, although they remain elevated in line with developed economies generally.

As noted above, GDP has been tepid throughout 2022/23, although the most recent composite Purchasing Manager Indices for the UK, US, EZ and China have all surprised to the upside, registering survey scores just above 50 (below suggests economies are contracting, and above suggests expansion). Whether that means a shallow recession, or worse, will be avoided is still unclear. Ultimately, the MPC will want to see material evidence of a reduction in inflationary pressures and a loosening in labour markets. Realistically, that is an unlikely outcome without unemployment rising and wage settlements falling from their current levels. At present, the bigger rise in employment kept the ILO unemployment rate unchanged at 3.7% in January. Also, while the number of job vacancies fell for the ninth consecutive month in February, they remained around 40% above pre-pandemic levels.

Our economic analysts, Capital Economics, expect real GDP to contract by around 0.2% quarter/quarter in Quarter 1 and forecast a recession this year involving a 1.0% peak-to-trough fall in real GDP.

The £ has remained resilient of late, recovering from a record low of $1.035, on the Monday following the Truss government's "fiscal event", to $1.23. Notwithstanding the £'s better run of late, 2023 is likely to see a housing correction of some magnitude as fixed-rate mortgages have moved above 4.5% and affordability has been squeezed despite proposed Stamp Duty cuts remaining in place.

2.2 Equity Markets

As for equity markets, the FTSE 100 started 2023 strongly, rising to a record high of 8,014 on 20th February, as resilient data and falling inflation boosted earnings. But global equities fell sharply after concerns over the health of the global banking system emerged early in March.

The fall in the FTSE 100 was bigger than the drop in the US S&P 500. Indeed, at around 7,600 now, the FTSE is 5.2% below its record high on 20th February, while the S&P 500 is only 1.9% lower over the same period. That's despite UK banks having been less exposed and equity prices in the UK's financial sector not falling as far. It may be due to the smaller decline in UK interest rate expectations and bond yields, which raise the discounted value of future earnings, compared to the US.

2.3 Global

USA. The flurry of comments from Federal Reserve (Fed) officials over recent months suggest there is still an underlying hawkish theme to their outlook for interest rates. Markets are pricing in a further interest rate increases of 25-50bps, on top of the current interest rate range of 4.75% - 5%.

In addition, the Fed is expected to continue to run down its balance sheet once the on-going concerns about some elements of niche banking provision are in the rear-view mirror.

As for inflation, it is currently at c6% but with the economy expected to weaken during 2023, and wage data already falling back, there is the prospect that should the economy slide into a recession of any kind there will be scope for rates to be cut at the backend of 2023 or shortly after.

EU. Although the Euro-zone inflation rate has fallen below 7%, the ECB will still be mindful that it has further work to do to dampen inflation expectations and it seems destined to raise rates to 4% in order to do so. Like the UK, growth has remained more robust than anticipated but a recession in 2023 is still seen as likely by most commentators.

2.4 Regulatory changes

IFRS 9 Fair Value of Assets
Following the consultation undertaken by the Department of Levelling Up, Housing and Communities (DLUHC) on IFRS 9, the Government has extended the mandatory statutory override for local authorities to reverse out all unrealised fair value movements resulting from pooled investment funds to 31st March 2025. Local authorities are required to disclose the net impact of the unrealised fair value movements in a separate unusable reserve throughout the duration of the override in order for the Government to keep the override under review and to maintain a form of transparency. This regulation applies to the CCLA Property Fund.

IFRS 16 Leases
IFRS16 which will have the effect of bringing currently off-balance sheet leased assets onto the balance sheet, has been delayed until 2024/25.

3.0 Local Context

On 31st March 2023, the Council had net investing of £21.16m 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 2 below.

Table 2: Balance Sheet Summary

	31.3.23 Actual £m
General Fund CFR	72.3
Less: *Other debt liabilities	(0.5)
Total CFR	**71.8**
External borrowing	(34.4)

Internal borrowing	(17.8)
Balance Sheet Resources[(1)(2)]	(74.9)
Investments	**(55.3)**

[(1)]Includes debtors, stock, cash,reserves, less overdraft, creditors, provisions, long term liabilities, unusable reserves.
[(2)]This is an estimate as the actual figure is not yet available.

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 2023 and the change during the year is shown in Table 3 below.

Table 3: Treasury Management Summary

	30.3.22 Balance £m	Movement £m	31.3.23 Balance £m	31.3.23 Rate %[(1)]
Long-term borrowing	38.92	(4.56)[(2)]	34.36	2.83
Short-term borrowing	0.00	0.00	0.00	
Total borrowing	**38.92**	**(4.56)**	**34.36**	**2.83**
Long-term investments	4.00	0.00	4.00	3.98
Short-term investments	21.00	19.00	40.00[(3)]	3.96
Cash and cash equivalents	28.07	(16.55)	11.52	3.78
Total investments	**53.07**	**2.45[(4)]**	**55.52**	**3.92**
Net Investing	**(14.15)**	**(7.01)**	**(21.16)**	

[(1)] Weighted average
[(2)]The borrowing from PWLB to fund loan to Places for People has been repaid, as Places for People repaid the loan to them.
[(3)]This does not include loans to local organisations, as these are not considered investments. This is DMO deposits.
[(4)]This is a net movement, investments made were £398.89m and investments returned £396.44m.

The movement in borrowing is as a result of Places for People repaying the loan from the council in full on 30th September 2022, the borrowing from PWLB used to finance the loan was repaid on 5th October 2022 (see table 4). In addition there has been a move away from use of MMFs and deposits (cash and cash equivalent) to DMO (Short-term investments), in anticipation of potential market stresses.

3.1 Borrowing Strategy during the period

At 31st March 2023, the Council held £34.36m of loans, a decrease of £4.56m from 31st March 2022. The main decrease resulted from the council repaying PWLB borrowing related to the Places for People loan. Outstanding loans on 31st March are summarised in Table 4 below.

Table 4: Borrowing Position

	30.3.22 Balance £m	Net Movement £m	31.3.23 Balance £m	31.3.23 Weighted Average Rate %	31.3.23 Weighted Average Maturity (years)
Public Works Loan Board	38.88	(4.54)	34.34	2.83%	21.4
Salix	0.04	(0.02)	0.02	0.00%	2.9
Short-term	0.00	0.00	0.00	0.00%	0.0
Total borrowing	**38.92**	**(4.56)**	**34.36**	**2.83%**	**21.4**

(1)There has been no short-term borrowing in 2022/23

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.

Table 5: Loan Schedule

Long-dated Loans borrowed	PWLB Reference	Amount £	Rate %	Period (Years)
PWLB 1	495152	5,000,000	3.91	34.75
PWLB 2	495153	5,000,000	3.90	35.75
PWLB 3	502463	83,196	2.24	0.35
PWLB 12	506436	5,000,000	2.78	14.52
PWLB 13	508696	7,291,685	2.49	15.96
PWLB 15	509389	11,963,000	2.18	16.25
Salix		26,320	0.00	2.89
Total borrowing		**34,364,201**	**2.83**	**21.41**

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 6 below.

Table 6: Treasury Investment Position

The weighted average interest rate for the investment portfolio up to 31.03.2023 was 3.85% (31.03.2022 0.82%).

	30.3.22 Balance £	Net Movement £m	31.3.23 Balance £m	31.3.23 Weighted Income Return[1,2] %	31.3.23 Weighted Average Maturity days
Banks & building societies (unsecured)	5,067,000	(3,946,000)	1,121,000	0.10%	1
Government (incl. local authorities)[4]	21,000,000	19,000,000	40,000,000	3.96%	22
Money Market Funds	23,000,000	(12,600,000)	10,400,000	3.68%	1
Loans to other organisation	6,975,200	(4,895,200)	2,080,000	4.24%[3]	1,936
Other Pooled Funds .					
- *Property funds*	4,000,000	0	4,000,000	3.98%	>365
Total investments	**60,042,200**	**(2,441,200)**	**57,601,000**	**3.85%**	

[1]Weighted Income return is based on the rate of return and the investments held as at 31/03/2023.

[2]Returns as at 31/03/2022, Banks and Building Societies 0.01%, Government 0.32%, MMFs 0.44%, Loans 2.54%, Property Fund 3.62%.

[3]This includes the annual average rate for the Urban and Civic loan, 4.28%, which is a variable (monthly) rate.

[4]The balance as at 30/03/22 is £17m DMO and £4m Thurrock, as at 31/03/2023 the balance is all DMO at £40m.

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 6 above.

The progression of risk and return metrics are shown in Table 7 below.

Table 7: Investment Benchmarking – Treasury investments managed in-house

	Portfolio Risk Score[(1)]	Average Credit Rating	Weighted Average Maturity (days)	Rate of Return %
30.09.2022	n/a	AA-	15	0.82
31.03.2023	1.04	AA	17	3.92

[(1)] This is a new measure from Link, will be used as a comparative from the next report, it works on a scale of 1 to 7, with 7 highest risk.

£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 £159,012 (3.98%), for period of 1st April 2022 to 31st March 2023 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 £70.8m of such investments in:

- directly owned property £70.7m
- shareholding in subsidiaries £0.1m (not yet active)

Table 8: Property held for investment purposes in £'000

Property	**Actual(1)**	**31.3.2023 Actual(1)**	
	31st Mar 2022	**Gains or (losses)**	**Value in accounts**
Existing Portfolio	33,603	(3,337)	30,266
Unit 8 Stonehill	2,150	331	2,481
80 Wilbury Way	1,775	98	1,873
Shawlands Retail Park	5,523	532	6,055
1400 & 1500 Parkway, Fareham	4,150	(113)	4,037
Units 21a, 21b,23a,b,c Little End Road, St Neots	3,290	31	3,321
Rowley Centre, St Neots	3,303	3,148	6,451
Tri-link, Wakefield	14,200	548	14,748
Alms Close	1,522	(75)	1,447
TOTAL	**69,516**	**1,162**	**70,679**

(1)The valuations are still subject to review and audit

These investments generated £5.36m (2021/22 £4.85m) of investment income for the Authority for 2022/23, an increase of 10% on 2021/22. This is a yield of 7.58% (2021/22 6.98%), maintaining a yield above treasury investments.

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 9: Proportionality of Investments in £'000

	2021/22 Actual £000s	2022/23 Actual £000s	2022/23 Budget £000s	2023/24 Budget £000s	2024/25 Budget £000s
Gross service expenditure	87,203	79,968[1]	64,256	79,968	75,040
Net Investment income;					
Commercial Property	1,776	4,018	2,930	2,595	3,122
Service Investments	295	258	276	242	240
Proportion	2.38%	5.35%	4.99%	3.55%	4.48%

[1]The forecast has been used as the actual is not yet available.

3.5 ESG

Two products have been identified as possible investment opportunities for the council, that take into account ESG factors. Standard Chartered Bank offer a Sustainable Fixed Term Deposit, this deposit is linked to sustainable assets, and is referenced to the UN Sustainable Development Goals, funds are used to address issues such as climate change, health and education. The deposits have third party verification and the framework is reviewed annually.

The second potential product is the Barclays Green Deposit, a notice account. The funds are used for a range of products aimed at the transition to a lower carbon economy. The deposits are linked with Barclays' Green Bond Purchasing Programme, which covers projects including energy efficiency, renewable energy, green transport, sustainable food, and greenhouse gas emissions.

Both products are under review and the aim is to look at investing once the volatility in the market linked to US bank failures has passed, since both products will be linked to a single counterparty.

3.6 Business Continuity

In order to maintain the level of knowledge within the council relating to treasury, one of the finance business partners has undertaken to increase his knowledge of the treasury function. As a result of this he attended the initial meeting, in March, with the council's new treasury advisors (Link Group), and is booked on a CIPFA course Introduction to Treasury Management. He will also be involved in the update to the treasury management practices process notes.

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 10 below.

Table 10: Debt Limits

	31.3.23 Actual £m	2022/23 Operational Boundary £m	2022/23 Authorised Limit £m	Complied?
General	10.02	70.00	80.00	Yes
Service Loans	0.083	15.00	20.00	Yes
CIS	24.26	30.00	35.00	Yes
Total debt	**34.36**	**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 11: Investment Limits

	31.3.23 Actual £m	2022/23 Limit £m	Complied?
Deposit Accounts			
NatWest(1)	1.12	22.00	Yes
Barclays	0.001	4.00	Yes
Government and LAs			
Debt Management Office (DMO) - HMG	40.00	unlimited	Yes
Money Market Funds			
Aberdeen Liquidity Fund	1.50	4.00	Yes
BlackRock Institutional sterling liquidity Fund	1.50	4.00	Yes
CCLA Public Sector Deposit Fund	1.50	4.00	Yes
Federated Short Term Prime Fund	1.40	4.00	Yes

HSBC	1.55	4.00	Yes
Insight Liquidity Funds	0.85	4.00	Yes
Invesco	1.20	4.00	Yes
Legal & General Sterling Liquidity Fund	0.90	4.00	Yes
Total	**51.52**		
Long-term Investments CCLA Property Fund	4.00	5.00	Yes

(1)This is the council's transactional bank, therefore the limit was higher than other counterparties, the limit has been reduced to £4m in 2023/24

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.

Table 12: Credit Ratings[1]

	31.3.23 Actual	2022/23 Target	Complied?
Portfolio average credit rating	AA	A-	Yes

(1)Credit ratings (Fitch, investment grade) are in descending order AAA, AA+, AA, AA-,A+,A,A-,BBB+,BBB,BBB-.

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.

Table 13: Cash Availability

	30.3.23 Actual £m	2022/23 Target £m	Complied?
Total cash available within 3 months	51.52	10	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:

Table 14: Interest Rate Risk

Interest rate risk indicator	31.3.23 Actual	2022/23 Limit	Complied?
Upper limit on one-year revenue impact of a 1% rise in interest rates	£375,656 (Net Income)	£600,000 (Expenditure)	Yes
Upper limit on one-year revenue impact of a 1% fall in interest rates	£375,656 (Net Expenditure)	£600,000 (Expenditure)	Yes

The impact of a change in interest rates is calculated on the assumption that maturing loans and investments will be replaced at the same amount. The total interest earned in 2022/23 was £1.3m (2021/22 £0.3m) and total interest paid £1.0m (2021/22 £1.1m).

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:

Table 15: Borrowing Maturity

Borrowing Maturing	31.3.23 Actual	Upper Limit	Lower Limit	Complied?
Under 12 months	0.2%	80%	0%	Yes
12 months and within 24 months	0.0%	80%	0%	Yes
2 years 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	70.6%	100%	0%	Yes
20 years and above	29.1%	100%	0%	Yes
Total	**100%**			

Other Indicators - CIS
The council has adopted voluntary indicators for the Commercial Investment Strategy properties.

Table 16: Other Indicators

Indicator	2022/23 Forecast	2022/23 Actual
Interest Cover Ratio	2.3	2.3
Loan to Value Ratio	128.3%	106.0%
Gross Rent Multiplier	15.1	14.4