# Overview and Scrutiny Committee

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| **Title** | Outturn, Quarter 1 and Mid-year Treasury Management Strategy and Performance Update 2023-24 |
| **Date of meeting** | 07 November 2023 |
| **Report of** | Executive Director of Strategy & Resources (Section 151 Officer) |
| **Wards** | All |
| **Status** | Public |
| **Urgent** | No |
| **Appendices** | Appendix A – Summary of changes in capital programme |
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## Summary


This report updates on treasury management performance through the first half of 2023/24, presenting data at three points in time as comparators. These are 2022/23 outturn (31 March 2023), end of quarter one (30 June 2023) and the mid-year point (30 September 2023).

The strategies set out in the Treasury Management Strategy approved by Council on the 28 February 2023 remain in place and there have been no breaches of strategy in relation to debt or investments. However, we are recommending that both the Operational Boundary and the Authorised Limit are increased to reflect expected borrowing requirements through 23/24, which have increased significantly since the Authorised Limit was set in February 2023 due to the reasons set out in paragraph 1.19.

In the six months to 30 September 2023, £45m of PWLB borrowing has been taken to support the HRA and £15m for the General Fund. This was based on a need identified within the HRA capital expenditure plans and affordability is documented in the HRA 30-year business plan.

This report sets out the expected borrowing plans for the second half of 23/24 within the context of the Council's capital programme approved at September 2023 Cabinet and expected use of reserves through 23/24 based on forecast outturn as at Q2. After factoring expected use of reserves and increases to capital expenditure expected over 23/24, the treasury team would now expect to borrow a further £228m over the remainder of 2023/24, taking the council's external borrowing to £975m, which requires

a revision to the Authorised Limit for total debt. The Authorised Limit was set at £920m for total external debt and other long-term liabilities over the period 23/24 and this report sets out the reasons for the recommended increase to £1,259m to reflect updated data around use of reserves and the capital programme. Note that the Operational Boundary and Authorised Limit are not, in themselves, an indication of the sustainability or viability of the capital programme. They are, rather, operational indicators for the treasury team to ensure that any borrowing requirements are consistent with the capital programme.

Investment performance throughout the same period has been above the benchmark. We achieved an average rate of return on our investment portfolio of 4.58% over the period against a benchmark of 4.55% and are achieving 5.30% as of 30 September 2023. This benchmark is the SONIA rate at which banks will lend to one another. This report confirms continued adherence to the investment strategy agreed in the 2023/24 Treasury Management Strategy Statement (TMSS) and confirms the treasury team continue to operate within the bounds of the counterparty criteria and agreed processes set out in the TMSS.

# Recommendations

**That the Committee**

1. **Note the report, the treasury activity and performance updates against the Prudential Indicators**

2. **Make recommendations to Cabinet and Council on the proposed approval of an increase to the council's Operational Boundary and Authorised Limit for External Debt to reflect the council's current expectations around use of reserves over 23-24 and capital expenditure requiring prudential borrowing.**

3. **Consider making any further recommendations to Cabinet or Council**

## 1. Reasons for the Recommendations

1.1 **Capital Strategy**

In December 2021, the Chartered Institute of Public Finance and Accountancy, (CIPFA), issued revised Prudential and Treasury Management Codes. These require all local authorities to prepare a Capital Strategy which included the following: -

- a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services;
- an overview of how the associated risk is managed;
- the implications for future financial sustainability.

1.2 **Treasury Management**

The Council, by legislation, is bound to set and operate a balanced budget, which broadly means cash raised during the year will meet its cash expenditure. Part of the treasury management operations ensure this cash flow is adequately planned, with surplus monies being invested in low-risk counterparties, maintaining adequate liquidity 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's risk or cost objectives.

Accordingly, treasury management is defined 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."*

1.3 **Introduction**

This report has been written in accordance with the requirements of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised 2021).

The primary requirements of the Code are as follows:

1. Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.

2. Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.

3. Receipt by full Council of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead, a Mid-year Review Report and an Annual Report, (stewardship report), covering activities during the previous year. (Quarterly reports are also required for the periods ending April to June and October to December but may be assigned to a designated committee or panel as deemed appropriate to meet the Treasury Management governance and scrutiny aspects of the Council.)

4. Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

5. Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body. For this Council the delegated body is Overview and Scrutiny Committee.

1.4 This mid-year report has been prepared in compliance with CIPFA's Code of Practice on Treasury Management, and covers the following:

- An economic update for the first half of the 2023/24 financial year;
- A review of the Treasury Management Strategy Statement and Annual Investment Strategy;
- The Council's capital expenditure, as set out in the Capital Strategy, and prudential indicators;
- A review of the Council's investment portfolio for 2023/24;
- A review of the Council's borrowing strategy for 2023/24;
- A review of compliance with Treasury and Prudential Limits for 2023/24.

1.5 **Economic update (first half of the year)**

- At 31 March 2023, the Bank of England's (BOE) Monetary Policy Committee (MPC) had set the base rate at 4.25%. Over the first half 2023/24, this has been increased by 100 basis points (bps) to 5.25% which some commentators including Link, the Council's treasury advisors, expect to be the peak of the tightening cycle. The impact for this on Barnet Council has been increased investment returns from more responsive, liquid investment assets, such as money market funds (MMFs).

- Short, medium and long dated gilts remain elevated as inflation remained high compared to forecasts by BoE at the beginning of the year. As the Council's primary source of long-term borrowing, the Public Work Loans Board (PWLB) prices its loans at gilts plus a mark-up; this has meant the cost of new borrowing has remained high.
- Consumer Price Index (CPI) inflation has fallen from 8.7% in April to 6.7% in August, its lowest rate since February 2022, but still the highest in the G7. Core CPI inflation declined to 6.2% in August from 7.1% in April and May, a then 31 years high. There has been a cooling in labour market conditions, but no evidence yet that it has led to an easing in wage growth (as the 3-month year on year growth of average earnings rose to 7.8% in August, excluding bonuses). These conditions reflect an improving situation as inflation begins to move in the direction of the BOE's 2% target, however wage growth continuing to stay high may keep inflation levels elevated due to the price-wage echo. In respect of implications for Barnet council, services have faced higher costs causing strain on budgets. There may be pressure on salary budgets in future years to meet higher workforce wage demands in the face of elevated price levels.

1.6 In its latest monetary policy meeting on 20 September, the Bank of England left interest rates unchanged at 5.25%. The weak August CPI inflation release, the recent loosening in the labour market and downbeat activity surveys indicating low economic growth appear to have convinced the Bank of England that it has raised rates high enough.

1.7 Link expect that, as the growing drag from higher interest rates intensifies over the next six months, the economy will continue to lose momentum and soon fall into a mild recession. Their view is that strong labour demand, fast wage growth and government handouts have all supported household incomes over the past year and with CPI inflation past its peak and expected to decline further, the economy has got through the cost-of-living crisis without recession. Link suggest that despite the largest falls in real household disposable incomes having happened, the phasing out of financial support packages provided by the government during the energy crisis means real incomes are unlikely to grow strongly and that higher interest rates will also soon take a greater hold. Link expect the Bank of England to keep interest rates at the probable peak of 5.25% until the second half of 2024.

1.8 **Interest Rate Forecasts**

The Council has appointed Link Group as its treasury advisors and part of their service is to assist the Council to formulate a view on interest rates. The PWLB rate forecasts below are based on the Certainty Rate of gilts + 80bps (the standard rate of gilts + 100bps, minus 20 bps certainty rate discount which has been accessible to most authorities since 1st November 2012).

1.9 The latest forecast on 25th September sets out a view that short, medium and long-dated interest rates will be elevated for some time, as the Bank of England seeks to squeeze inflation out of the economy, however. The forecast also anticipated a reduction to short, medium and long-term over the next 24 months. The reduction in rates implied by this forecast will be considered when taking out new borrowing, specifically it may be appropriate to take short-term borrowing with a view refinancing rather than locking into high medium to long-term rates now. This approach is based on insight by industry experts, however, there is always a risk that interests do not fall as forecast or, indeed, increase further.

| Link Group Interest Rate View | 25.09.23 | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Dec-23 | Mar-24 | Jun-24 | Sep-24 | Dec-24 | Mar-25 | Jun-25 | Sep-25 | Dec-25 | Mar-26 | Jun-26 | Sep-26 | Dec-26 |
| BANK RATE | 5.25 | 5.25 | 5.25 | 5.00 | 4.50 | 4.00 | 3.50 | 3.00 | 2.75 | 2.75 | 2.75 | 2.75 | 2.75 |
| 3 month ave earnings | 5.30 | 5.30 | 5.30 | 5.00 | 4.50 | 4.00 | 3.50 | 3.00 | 2.80 | 2.80 | 2.80 | 2.80 | 2.80 |
| 6 month ave earnings | 5.60 | 5.50 | 5.40 | 5.10 | 4.60 | 4.10 | 3.60 | 3.10 | 2.90 | 2.90 | 2.90 | 2.90 | 2.90 |
| 12 month ave earnings | 5.80 | 5.70 | 5.50 | 5.20 | 4.70 | 4.20 | 3.70 | 3.20 | 3.00 | 3.00 | 3.00 | 3.00 | 3.00 |
| 5 yr PWLB | 5.10 | 5.00 | 4.90 | 4.70 | 4.40 | 4.20 | 4.00 | 3.90 | 3.70 | 3.70 | 3.60 | 3.60 | 3.50 |
| 10 yr PWLB | 5.00 | 4.90 | 4.80 | 4.60 | 4.40 | 4.20 | 4.00 | 3.80 | 3.70 | 3.60 | 3.60 | 3.50 | 3.50 |
| 25 yr PWLB | 5.40 | 5.20 | 5.10 | 4.90 | 4.70 | 4.40 | 4.30 | 4.10 | 4.00 | 3.90 | 3.80 | 3.80 | 3.80 |
| 50 yr PWLB | 5.20 | 5.00 | 4.90 | 4.70 | 4.50 | 4.20 | 4.10 | 3.90 | 3.80 | 3.70 | 3.60 | 3.60 | 3.60 |

1.10 **Treasury Management Strategy Statement and Annual Investment Strategy Update**

The TMSS for 2023/24 was based on data available at 31 December 2022 and was approved by Council on 28 February 2023. This report uses updated capital programme data presented at Cabinet in September 2023 and, due to increases in expected borrowing requirements, will recommend changes to the Operational Boundary and Authorised Limit within the 23-24 TMSS.

1.11 **The Council's Capital Position (Prudential Indicators)**

This part of the report is structured to update:

- The Council's capital expenditure plans;
- How these plans are being financed;
- The impact of the changes in the capital expenditure plans on the prudential indicators and the underlying need to borrow; and
- Compliance with the limits in place for borrowing activity.

1.12 **Prudential Indicator for Capital Expenditure**

This table shows the revised estimates for capital expenditure and the changes since the capital programme that was presented at the December Policy and Resources (P&R) Committee meeting. This report uses the December P&R capital programme data as a comparator because this is the data that was used to prepare the 2023/24 TMSS.

In addition, the treasury team has added £45m of Prudential Borrowing relating to the purchase of properties for the HRA (Colindale Gardens) that was not included in the Capital Tables presented at September 2023 Cabinet. This additional prudential borrowing has been factored into our recommended revisions to the Operational Boundary and Authorised Limit in section 1.23.

| Forecasted Capital Expenditure 2023/24 (£m) | Original Estimate Agreed at December 22 P&R | Revised Estimate Agreed at September 23 Cabinet | Change in Forecast |
|---|---|---|---|
| General Fund | 210.741 | 271.537 | 60.796 |
| HRA | 100.569 | 160.971* | 60.402 |
| **Total Capital Expenditure** | **311.310** | **432.509*** | **121.199** |

*These capital expenditure estimates include £45m relating to Colindale Gardens – actual capital expenditure relating to Colindale Gardens may be higher due to use of other sources of financing not included above.*

1.13 **Changes to the Financing of the Capital Programme**

The table below shows the financing arrangements of the capital expenditure set out in 1.12. The borrowing element of the table increases the underlying indebtedness of the council by way of the Capital Financing Requirement (CFR), although this will be reduced in part by revenue charges for the repayment of debt, the Minimum Revenue Provision (MRP). This direct borrowing need may also be supplemented by maturing debt and other treasury requirements. This analysis shows that the Net Finance Requirement has increased by £81m since the 23-24 TMSS was set in February 2023.

| Financing of Capital Expenditure 2023/24 (£m) | Original Estimate Agreed at December 22 P&R | Revised Estimate Agreed at September 23 Cabinet | Change in Forecast |
|---|---|---|---|
| **Total Capital Expenditure** | **311.310** | **432.509** | **121.199** |
| **Financed by:** | | | |
| Capital Receipts | 14.581 | 20.404 | 5.823 |
| Capital Grants | 72.486 | 104.693 | 32.207 |
| Capital Reserves | 36.227 | 39.112 | 2.885 |
| Revenue | 13.134 | 12.378 | (0.756) |
| **Net Financing Requirement** | **174.882** | **255.922** | **81.04** |

1.14 Note that the council operates two pools of debt, General Fund (GF) and the Housing Revenue Account (HRA), with each fund servicing the interest costs of a proportionate share of debt. However, for the purposes of compliance with the prudential indicators and for the policy of borrowing in advance of need the capital financing requirement, the council will use the combined capital financing requirement of the two pools. This does not conflict with the need to ensure the affordability of debt for each pool and is consistent with the Chartered Institute for Public Finance and Accountancy (CIPFA) Prudential Code for Capital Finance in Local Authorities (Prudential Code).

1.15 **Changes to the Prudential Indicators for the Capital Financing Requirement (CFR), External Debt and Operational Boundary**

This table below shows the CFR, which is the underlying external need to incur borrowing for a capital purpose. It also shows the expected debt position over the period, which is termed the Operational Boundary.

**Prudential Indicator – Capital Financing Requirement**

The projected CFR changes with in-year revisions to the council's capital expenditure plans as these drive the level of prudential borrowing required. The table below shows the latest revised projection of CFR at 31 March 2024 based on updated capital programme data and reserve usage forecasted through 2023/24.

| Updated projection of CFR (£'000) | Revised Projection | Projected within 23-24 TMSS | CFR in draft 2022/23 Accounts |
|---|---|---|---|
| Projected CFR 31 March 2024 (23-24 TMSS) | 1,138,498 | | |
| Adjustment for actual CFR at 1 April 2023 | (38,422) | 975,593 | 937,171 |
| Increase Prudential Borrowing | 81,000 | | |

| | | | |
|---|---|---|---|
| **Projected CFR 31 March 2024 (updated data)** | **1,181,076** | | |

**Prudential Indicator – Operational Boundary**

1.16 The Treasury Team set its Operational Boundary and Authorised Limit in February 2023 based on data available at 31 December 2022. At that time the Treasury Team were working to the following data points:

| | |
|---|---|
| **Expected Treasury assets at 1 April 2023** | £163m |
| **Expected Prudential Borrowing 23-24** | £175m |
| **Expected Prudential Borrowing 24-25** | £120m |
| **Externalised Internal Borrowing** | Nil |
| **Target Treasury assets at 31 March 2024 (liquidity buffer)** | £30m |

1.17 The treasury team then set its Operational Boundary for 23-24 as the level of external borrowing required over 23-24 to cover both 23-24 and 24-25 prudential borrowing requirements (i.e., to allow forward borrowing against the agreed capital programme for 2-years). This Operational Boundary allowed for expected investments at 1 April 2023 of £163m and our target liquidity buffer of £30m at 31 March 2024. This gave an Operational Boundary for external debt of £808m over 23-24 i.e., scope for £121m of additional borrowing over 23-24. The expectation of other long-term liabilities (OLTL) to total to £11.925m, made up of the Public Finance Initiative (PFI) lease liability relating to streetlighting, has not changed and therefore the Operational Boundary for External Debt and OLTL was set at £820m. Further details of how the Operational Boundary was set is explained in the 23-24 TMSS.

1.18 The Treasury Team than set its Authorised Limit as £100m in addition to its Operational Boundary (as has been the practice for previous TMSS) giving total scope of £221m of borrowing over 23-24. In addition, significant levels (around £200m) of forward borrowing had been taken through 20-21 and 21-22 when interest rates were substantially lower.

1.19 We have reviewed the data points set out in 1.17 above at 30 September 2023 and found significant differences as follows:

- The council's Treasury assets at 31 March 2023 were £104m not £163m
- A significant increase in Prudential Borrowing over 23-24 of £81m (as explained in 1.13)
- A significant expected use of usable reserves which would mean externalising internal borrowing of £116m

A more detailed explanation of the implication of these changes from a borrowing perspective is set out below:

1.20 The lower-than-expected treasury assets is due to repayment of Covid grants made available by central government for the council to pay to businesses that could meet specific eligibility criteria, use of usable reserves in 2022/23 and other ebbs and flows of liquidity ("working capital"). The impact of lower than forecasted opening investment balances is an increased financing requirement as capital expenditure previously planned to be met from cash balances now need to be met through external borrowing.

1.21 The capital programme's prudential borrowing requirement to year end 2023/24 has increased by £81m relative to data available at 31 December 2022. The treasury team has undertaken a very high-level analysis of the changes to the capital programme since December 2022 and understands the main increases for 23-24 since December 2022 are Colindale Gardens (£45m), Care Homes: Meadowside and Dellfield (£25m),the Burroughs Hendon (£4m), Roads (£4m) and New Depot (£13m). Some capital streams have reduced expected prudential borrowing. A summary of the treasury team's analysis is provided in appendix A.

1.22 We understand from the closing team that the council is planning to use £116.3m of usable reserves in 2023/24. This includes £16.3m of capital receipts, £53.3m of unapplied capital grants, £43.1m of earmarked reserves, £3.7m of provisions and a small contribution to the HRA reserve. It is very important to note that these reserves are not held as cash as they have been employed to finance historical capital projects as a way of avoiding the cost of external borrowing (this is known as "internal borrowing"). As a result of this, the use of reserves, including historical capital receipts and grants, means that the treasury team would need to externalise its internal borrowing (take new external loans), therefore increasing the council's external borrowing requirement over 23/24.

| Usable Reserves (£'000) | Impact of 2023/24 Reserve Drawdown | | |
|---|---|---|---|
| | Opening Balance | Drawdown 2023/24 | Closing Balance |
| General Fund Balance | -15,082 | 0 | -15,082 |
| Housing Revenue Account Balance | -6,120 | -194 | -6,314 |
| Collection Fund Adjustment Account | -4,692 | 0 | -4,692 |
| Earmarked reserves / other balances | -139,543 | 43,138 | -96,405 |
| *Capital Receipts Reserve - GF* | *-9,083* | *6,233* | *-2,850* |
| *Capital Receipts Reserve - HRA* | *-34,744* | *10,059* | *-24,685* |
| **Capital Receipts total** | **-43,827** | **16,292** | **-27,535** |
| Provisions (exc. any accumulating absences) | -15,358 | 3,719 | -11,639 |
| Capital Grants Unapplied (Incl S106) | -118,397 | 53,347 | -65,050 |
| **Grand Total** | **-343,019** | **116,302** | **-226,717** |

1.23 The table below shows the aggregated impact of the changes to the capital programme, opening investment balances and use of reserves, and the resultant requirement for external borrowing and the Operational Boundary and Authorised Limit implied by this.

| £m<br>*negative number indicates asset or cash inflow | Based on 31 December 2022 data | Based on 30 September 2023 data | Delta | Comment on delta |
|---|---|---|---|---|
| Borrowing 1 April 2023 | 689 | 687 | (2) | Repayment on Principal only loans |
| Expected Treasury Investments at 1 April 2023 | (163)* | (104)* | 59 | see 1.21 |
| Expected Prudential Borrowing over 23/24 | 175 | 256 | 82 | see 1.22 |
| Externalised Internal Borrowing over 23/24 | 0 | 116 | 116 | See 1.23 |

| | | | | |
|---|---|---|---|---|
| Expected MRP over 23/24 | (12)* | (12)* | 0 | MRP provision improves expected cash position of Treasury |
| Expected Actual Borrowing over 23/24: | (30)* | (286)* | (256)* | |
| Expected Treasury Investments 31 March 2024 | (30)* | (30)* | 0 | Liquidity buffer |
| Expected Total External Borrowing 31 March 2024 | 719 | 973 | 254 | New forecast for borrowing - does not account for principal repaid in year |
| **Operational Boundary for External Debt** | **808** | **1,147** | **339** | |
| Other long-term Liabilities (OLTL) | 12 | 12 | 0 | Joint streetlighting PFI lease liability |
| **Operational Boundary for External Debt and OLTL** | **820** | **1,159** | **339** | |
| **Authorised Limit** | **920** | **1,259** | **339** | |

1.24 In summary, the 2023/24 TMSS set out an Authorised Limit of £920m based on the available data at 31 December 2023. Following the same methodology for updated data at 30 September 2023, this report recommends that the Operational Boundary is increased to £1,159m and the Authorised Limit is increased to £1,259m to allow the treasury team to borrow up in line with the council's capital programme and expected use of reserves over 2023-24.

1.25 Note that the Operational Boundary and Authorised Limit are not, in themselves, an indication of the sustainability and viability of the capital programme. They are, rather, operational indicators for the treasury team to ensure that any borrowing requirements are consistent with the capital programme. This means that the treasury team is not "signing off" on the level of borrowing requested as being viable, rather reacting to the level of borrowing implied by the capital programme and need to externalise internal borrowing due to use of reserves. Whilst each capital project is assessed for viability and sustainability at an individual level it is important that in aggregate the council is satisfied that the implied increase to borrowing does not introduce unnecessary or unsustainable risks to the council. and the treasury team will raise this point with the Capital Strategy Board.

1.26 We recommend the impact of higher borrowing within the treasury cost centre is understood and reflected in the council's MTFS (see 1.37).

1.27 **Borrowing**

The table below shows the actual movement of the council's external borrowing since 31 March 2023 to 30 September 2023 (£744.1m) and gives a projection of the position at 31 March 2024 (£945.1m). The treasury team may rebase HRA assets at 1 April 2023 after analysing the HRA's CFR and reserve position. This analysis may impact on the split of borrowing between HRA and General Fund.

| Actual and Projected External Borrowing 23/24 | 31/03/2023 Actual | | 30/06/2023 Actual | | 30/09/2023 Actual | | 31/03/2024 Projected | |
|---|---|---|---|---|---|---|---|---|
| £m | GF | HRA | GF | HRA | GF | HRA | GF | HRA |
| PWLB | 242.1 | 379.4 | 257.1 | 379.4 | 256.6 | 424.4 | 485.3 | 424.4 |
| Market Loans | 32.4 | 30.1 | 32.4 | 30.1 | 32.4 | 30.1 | 32.4 | 30.1 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Salix | 3.9 | 0.0 | 3.3 | 0.0 | 3.3 | 0.0 | 2.9 | 0.0 |
| Total Loans | 278.5 | 409.5 | 292.9 | 409.5 | 292.4 | 454.5 | 520.6 | 454.5 |

A summary of long-term loans taken out over the period 1 April 2023 to 30 September 2023 is set out below:

| Principal (£m) | Fund | Start Date | End Date | Rate | Structure | Lender |
|---|---|---|---|---|---|---|
| 15 | General Fund | 03/04/2023 | 02/04/2038 | 4.03% | Annuity | PWLB |
| 45 | HRA | 20/07/2023 | 19/07/2073 | 4.90% | Annuity | PWLB |

Taking this into consideration, and a further £228m of expected borrowing, total year-end borrowing will be £975m.

1.28 **PWLB maturity certainty rates (gilts plus 80bps) year to date to 29th September 2023**

Gilt yields and PWLB certainty rates were on a generally rising trend throughout the first half of 2023/24. At the beginning of April, the 5-year rate was the cheapest part of the curve and touched 4.14% whilst the 25-year rate was relatively expensive at 4.58%.

July saw short-dated rates peak at their most expensive. The 1-year rate spiked to 6.36% and the 5-year rate to 5.93%. Although, in due course, short-dated rate expectations fell, the medium dates shifted higher through August and the 10-year rate pushed higher to 5.51% and the 25-year rate to 5.73%. The 50-year rate was 4.27% on 5th April but rose to 5.45% on 28th September.

**PWLB rates between 01 April 2023 – 30 September 2023**

| | 1 Year | 5 Year | 10 Year | 25 Year | 50 Year |
|---|---|---|---|---|---|
| **Low** | 4.65% | 4.14% | 4.20% | 4.58% | 4.27% |
| **Date** | 06/04/2023 | 06/04/2023 | 06/04/2023 | 06/04/2023 | 05/04/2023 |
| **High** | 6.36% | 5.93% | 5.51% | 5.73% | 5.45% |
| **Date** | 06/07/2023 | 07/07/2023 | 22/08/2023 | 17/08/2023 | 28/09/2023 |
| **Average** | 5.62% | 5.16% | 5.01% | 5.29% | 5.00% |
| **Spread** | 1.71% | 1.79% | 1.31% | 1.15% | 1.18% |

1.29 **Link PWLB rate forecast**

Link forecast rates to fall back over the next two to three years as inflation dampens. The CPI measure of inflation is expected to fall below 2% in the second half of 2024, and Link forecast 50-year rates to stand at 3.90% by the end of September 2025. However, their forecast is caveated by highlighting that there is considerable gilt issuance to be digested by the market over the next couple of years, as a minimum, so there is a high degree of uncertainty as to whether rates will fall that far.

1.30 **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. However, now that the whole of the yield curve has shifted higher there may be better opportunities in the future, although only prudent and affordable debt rescheduling will be considered but will be considered if it will give rise to long-term savings.

1.31 **Compliance with Treasury and Prudential Limits**

It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. During the half year ended 30th September 2023, the Council has operated within the treasury and prudential indicators set out in the Council's Treasury Management Strategy Statement for 2023/24. However, as noted under 1.16 to 1.26 the treasury team is recommending that Operational Boundary Authorised Limit is increased to reflect the use of reserves and increase in capital programme seen since 31 December 2022.

All treasury management operations have also been conducted in full compliance with the Council's Treasury Management Practices.

1.32 **Annual Investment Strategy**

The TMSS for 2023/24, which includes the Annual Investment Strategy, was approved by the Council on 28 February 2023. 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

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, using the Link suggested creditworthiness approach, including a minimum sovereign credit rating and Credit Default Swap (CDS) overlay information. In practice, to support capital outlay and avoid refinancing while interest rates for borrowing are high, the treasury team are allowing fixed-term deposits to mature and reinvesting them in Money Market Funds (MMFs) until such time as they are being spent. This approach means that we have fewer term deposits in our portfolio and are also expecting to see overall total investment balances fall.

**Creditworthiness**

Following the Government's fiscal event on 23rd September 2022, both S&P and Fitch have placed the UK sovereign debt rating on Negative Outlook, reflecting a downside bias to the current ratings considering expectations of weaker finances and the economic outlook.

**Investment Counterparty criteria**

The current investment counterparty criteria selection approved in the TMSS is meeting the requirement of the treasury management function.

**CDS prices**

It is noted that sentiment in the current economic climate can easily shift, so it remains important to undertake continual monitoring of all aspects of risk and return in the current circumstances.

1.33 **Investment Balances and Performance**

The average level of funds available for investment purposes during the first half of the financial year was £143.233m. These funds were available on a temporary basis, and the level of funds available was mainly dependent on the timing of precept payments, receipt of grants and progress on the capital programme. In the April 2023, the council received significant funding from central government and borrowed £15m and in July 2023, a further £45m was borrowed – these cash balances fell through the periods shown below as expenditure was incurred, which explains why investment balances at the dates shown below were lower than the average balances available to invest through the year to date. The Council holds a minimum of £30m core cash balances in MMFs for cashflow purposes (i.e., funds available for on the day redemption).

| Date | Total Investments (£m) | Total Money Market Fund Investments (£m) | Fixed Deposits Investments (£m) | Average Rate of Return | Interest Accrued in Quarter to Date (£m) |
|---|---|---|---|---|---|
| 31/03/2023 | 108.300 | 39.000 | 69.300 | 3.71% | 2.645 |
| 30/06/2023 | 108.640 | 57.940 | 50.700 | 4.60% | 1.112 |
| 30/09/2023 | 105.910* | 45.910* | 60.000 | 5.30% | 1.913 |

**Balances include £20m of short-term loans borrowed on the inter-local authority market to manage cashflow*

1.34 **Approved Limits**

Officers can confirm that the approved limits within the Annual Investment Strategy were not breached during the 6-month period ended 30th September 2023.

1.35 **Treasury Management and Medium-Term Financial Strategy (MTFS)**

The authority is operating against a vastly different backdrop to that of recent years, whereby the costs associated with financing the capital programme through external borrowing were relatively low and enabled the council to hold higher cash balances as investments. A high inflationary environment has also increased the strain on revenue budgets.

As the council is now running down cash balances in favour of avoiding taking on new external borrowing, the previous internal borrowing approach is being unwound. Where the council has previously used the cash backing its usable reserves to finance capital projects and avoid external borrowing, the cost to the council of using this cash has been the foregone investment income on the balances before they had been spent, however this is typically lower than the cost of external borrowing, so it is more efficient to use internal borrowing.

The shift to using these reserves requires the treasury team to source external borrowing and therefore incur higher interest payable costs.

The impact of lower cash balances and higher external debt will mean the treasury team's cost centre will switch from a broad contribution to the council's budget to being a significant cost to the council's budget (before application of MRP). The treasury team have been working closely with teams across the finance department to support the modelling of this impact, factoring in the true cost of using reserves and externalising internal borrowing over the span of the MTFS. Initial analysis suggests that this cost is significant.

## 2. Alternative Options Considered and Not Recommended

2.1 The council has the option to keep high cash balances as investments and externalise all internal borrowing immediately, however this is not recommended due to the high cost of external borrowing and the cost of carry that would be incurred, where interest rates payable on loans outstrip rates of return achievable on investments.

2.2 To make an adjustment to the Operational Boundary and Authorised Limit, however these are important indicators of outturn against the council's initial plans and so should be used to inform decisions and revise plans to stay within the limits where necessary.

## 3. Post Decision Implementation

3.1 If the Committee identify any areas that they wish to scrutinise in-depth then Scrutiny Officers will request that a report be presented to a future meeting of the Committee and that the relevant Cabinet Member and officer attend to answer questions on the issues raised.

3.2 Following consideration of the report, the Committee may, in accordance with the following Committee Procedure Rules:

- 38.2.2 Make reports or recommendations to Full Council or the Cabinet with respect to the discharge of any functions which are the responsibility of the executive.
- 38.2.4 Make reports or recommendations to Full Council or the Cabinet with respect to the discharge of any functions which are not the responsibility of the executive.
- 38.2.6 Review or scrutinise the performance of anybody carrying out any function on behalf of or in partnership with the Council.

3.3 Committee Procedure Rule 40 details how the Cabinet and/or Council will deal with matters referred from the Overview and Scrutiny Committee or Sub-Committees

## 4. Corporate Priorities, Performance and Other Considerations

**Corporate Plan**

4.1 The Corporate Plan 2023-26 sets out one of its aims for the council as being financially responsible. Effective treasury management directly supports this aim, but being an effective treasury team and delivering to our treasury management strategy statement will support the organisation in meeting all other elements of the corporate plan through strong financial management.

4.2 The treasury team are also building Ethical, Social and Governance (ESG) considerations into the decision making around investments and have in 2023-24 placed a 'sustainable deposit' with Standard Chartered, where much of the onward lending by the bank goes to support sustainable development projects that address long-term environmental challenges.

**Risk Management**

4.3 The council's policy around counterparty credit worthiness and ensuring all investment activity is carried out within the bounds of the agreed TMSS investment criteria is part of the council's corporate risk register and the associated risks are monitored quarterly through this process.

**Insight**

4.4 The Council uses its treasury advisors Link to provide key insight to support its analysis around key investment and borrowing decisions.

**Social Value**

4.5 Through aiming to achieve security of the council's capital at the highest investment returns available, the Treasury team support the wider organisation in using its resources as effectively as possible to generate income that will support service delivery. Ensuring that we have sufficient liquidity, and that external borrowing is financed at the most opportune timing and at the lowest possible rates also help to keep the council's costs lower, enabling more resources to be directed towards delivering services that generate higher social value.

| 5. | Resource Implications (Finance and Value for Money, Procurement, Staffing, IT and Property) |
|---|---|
| 5.1 | None in the context of this report. |
| **6.** | **Legal Implications and Constitution References** |
| 6.1 | Authorities are required by regulation to have regard to the CIPFA Prudential Code when carrying out their duties in England and Wales under Part 1 of the Local Government Act 2003. |
| 6.2 | Section 1: E4. of The Prudential Code requires authorities to look at capital expenditure plans, investments and debt in the light of overall organisational strategy and resources and ensure that decisions are being made with sufficient regard to the long-run financing implications and potential risks to the authority. |
| 6.3 | The Act also sets out in Part 1, 3.1. "A local authority shall determine and keep under review how much money it can afford to borrow" and gives the general power to do so and 12.b "A local authority may invest for the purposes of the prudent management of its financial affairs". |
| 6.4 | Section 3 of the Local Government Act 2003 places a duty on a local authority to determine and keep under review how much money it can afford to borrow. The Council has determined this limit to be £920m as set out in the TMSS and there has been no breach of the strategy. |
| 6.5 | Part 4A of the Council's constitution, section 2.15.2 sets out that "Cabinet will receive reports on its treasury management policies, practices and activities. This will also be considered by the Overview and Scrutiny Committee and Sub Committees. These reports will incorporate the prudential borrowing limits and performance indicators. |
| 6.6 | The terms of reference of the Overview & Scrutiny Committee and Sub-Committees (Council Constitution, Part 2B, Terms of Reference of Committees and Sub-Committees includes: "9.2.6 Performance Review - to receive selected monitoring reports (including KPI, financial performance and risk information) in relation to internally and externally delivered services" and that they may "9.4.1.2 Review and scrutinise the performance of the Council in relation to its policy objectives, performance targets and/or particular service areas. |
| 6.7 | The terms of reference state that "The Overview & Scrutiny Committee has the following powers and duties:<br>10.1 The Overview and Scrutiny Committee has the following power and duties:<br><br>10.1.1 To oversee an agreed work programme that can help secure service improvement through in-depth investigation of performance issues and the development of an effective strategy/policy framework for the council and partners;<br><br>10.1.2 To have general oversight of the council's scrutiny function;<br><br>10.1.3 To offer challenge and critical support to the Executive's policy development function and the long-term strategic direction of the borough;<br><br>10.1.4 To anticipate policy changes and determine their potential impact on residents and to recommend changes where these are appropriate;<br><br>10.1.5 To consider the council and partners' strategic approach to service delivery, using, where necessary, the power of overview and scrutiny committees to receive information from partner agencies and to require partner authorities to have regard to reports and recommendations from the Committee, as set out under Part Five of the Local Government and Public Involvement in Health Act 2007; |

10.1.6 To undertake detailed investigation of service/financial performance in order to recommend policy changes to the Executive and to undertake investigations;

10.1.7 To report scrutiny findings and recommendations to the Executive within 8 weeks of being published or to its next meeting, whichever is the sooner, in accordance with the council's constitution."

## 7. Consultation

7.1 There has not been any Consultation process followed in the preparation of this report.

## 8. Equalities and Diversity

8.1 Decision makers should have due regard to the public sector equality duty in making their decisions. The equalities duties are continuing duties they are not duties to secure a particular outcome. The equalities impact will be revisited on each of the proposals as they are developed. Consideration of the duties should precede the decision. It is important that Cabinet has regard to the statutory grounds in the light of all available material such as consultation responses. The statutory grounds of the public sector equality duty are found at section 149 of the Equality Act 2010 and are as follows:

A public authority must, in the exercise of its functions, have due regard to the need to:

a) Eliminate discrimination, harassment, victimisation and any other conduct that is prohibited by or under this Act;
b) Advance equality of opportunity between persons who share a relevant protected characteristic and persons who do not share it;
c) Foster good relations between persons who share a relevant protected characteristic and persons who do not share it.

Having due regard to the need to advance equality of opportunity between persons who share a relevant protected characteristic and persons who do not share it involves having due regard, in particular, to the need to:

a) Remove or minimise disadvantages suffered by persons who share a relevant protected characteristic that are connected to that characteristic;
b) Take steps to meet the needs of persons who share a relevant protected characteristic that are different from the needs of persons who do not share it;
c) Encourage persons who share a relevant protected characteristic to participate in public life or in any other activity in which participation by such persons is disproportionately low.

The steps involved in meeting the needs of disabled persons that are different from the needs of persons who are not disabled include, in particular, steps to take account of disabled persons' disabilities.

Having due regard to the need to foster good relations between persons who share a relevant protected characteristic and persons who do not share it involves having due regard, in particular, to the need to:

a) Tackle prejudice, and

b) Promote understanding.

Compliance with the duties in this section may involve treating some persons more favourably than others; but that is not to be taken as permitting conduct that would otherwise be prohibited by or under this Act. The relevant protected characteristics are:

a) Age
b) Disability
c) Gender reassignment
d) Pregnancy and maternity
e) Race
f) Religion or belief
g) Sex
h) Sexual orientation
i) Marriage and civil partnership

## 9. Background Papers

9.1 2023/24 Treasury Management Strategy Statement

9.2 Capital Programme September 2023