Executive **15 June 2023**

Report of the Chief Finance Officer
Portfolio of the Executive Member for Finance & Performance

Treasury management annual report and review of prudential indicators 2022/23

Summary

1. The Council is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2022/23. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management, (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities, (the Prudential Code).

2. The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This report provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by members.

3. This report also confirms that the Council has complied with the requirement under the Code to give scrutiny to treasury management reports by Audit & Governance Committee.

Recommendations

4. Executive is asked to:

   Note the 2022/23 performance of treasury management activity and prudential indicators outlined in annex A.

   Reason: to ensure the continued performance of the treasury management function can be monitored and to comply with statutory requirements.

Background and analysis

The Economy and Interest Rates

5. 2022/23 has seen rising and volatile UK interest rates right across the curve, from Bank Rate through to 50-year gilt yields, and these have been affected by rising and 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. At present the Bank of England is being challenged by persistent inflation that is exacerbated by very tight labour markets and high wage increases relative to what the bank believes to be sustainable.

6. Bank Rate increased throughout 2022/23, starting at 0.75% and finishing at 4.25%. CPI inflation rose to peak at 11.1% in October 2022 and 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%.

7. Investment returns improved throughout 2022/23 due to successive Bank of England base rate increases which in turn was reflected in investment rates available. This was expected after the Bank of England had started to increase base rate towards the end of 2021/22 to combat rising inflation as the Bank of England realised that inflationary pressures were not transitory, and that tighter monetary policy was called for.

8. In terms of borrowing, PWLB rates are based on gilt (UK Government bonds) yields through HM Treasury determining a specified margin to add to gilt yields. The main influences on gilt yields are Bank Rate, inflation expectations and movements in US treasury yields. Since early 2022, yields have risen dramatically in all the major developed economies, first as economies opened post-Covid; then because of the inflationary impact of the war in Ukraine in respect of the supply side of many goods. In particular, rising cost pressures emanating from shortages of energy and some food categories have been central to inflation rising rapidly. It is projected that there is likely to be a fall in gilt yields and PWLB rates across the whole curve over the next one to two years as Bank Rate first rises to dampen inflationary pressures and a tight labour market, and is then cut as the economy slows, unemployment rises, and CPI inflation moves closer to the Bank of England's 2% target. As a general rule, short-dated gilt yields will reflect expected movements in Bank Rate, whilst medium to long-dated yields are driven primarily by the inflation outlook.

Overall treasury position as at 31 March 2023

9. The Council's year end treasury debt and investment position for 2022/23 compared to 2021/22 is summarised in the table below:

Debt	31/03/2023 £m	Average Rate %	31/03/2022 £m	Average Rate %
General Fund debt	154.9	3.17	159.6	3.21
Housing Revenue Account (HRA) debt	146.4	3.20	146.4	3.21
PFI	42.8	n/a	44.0	n/a
Total debt	344.1	3.18	350.0	3.21
Investments				
Councils investment balance	10.8	2.02	38.8	0.10

Table 1 summary of year end treasury position as at 31 March 2023

Borrowing requirement and debt

10. The Council's underlying need to borrow to finance capital expenditure is termed the Capital Financing Requirement (CFR).

	31 March 2023 Actual £m	31 March 2023 Budget £m	31 March 2022 Actual £m
CFR General Fund	292.8	323.1	275.5
CFR HRA	146.4	146.4	146.4
PFI	42.8	45.5	44.0
Total CFR	482.0	515.0	465.9

Table 2 capital financing requirement

Borrowing outturn for 2022/23

11. During 2022/23, the Council maintained an under-borrowed position. This meant that the capital borrowing need, (the Capital Financing Requirement), was not fully funded with loan debt, as cash supporting the Council's reserves, balances and cash flow was used as an interim measure. This strategy was still prudent as investment returns, while rising, were below borrowing rates which increased sharply across the curve in 2022/23.

12. The policy of avoiding new borrowing by running down spare cash balances, has served well over the last few years as it has helped to reduce the Councils cost of carry – the revenue cost difference between (higher) borrowing costs and (lower) investment returns. This policy is kept under review and as borrowing interest rates have increased sharply in the last year it makes sense to continue to internally borrow until rates start to decrease which they are predicted to do towards the end of 2023/24.

13. Where debt is required to finance the capital programme the Treasury team will look at temporary and short term borrowing options if internal borrowing cannot be maintained and also look out for, and at, opportunities to draw down long term debt at more favourable rates should the opportunities arise through either PWLB or market borrowing in order to try to minimise the longer-term impact of debt costs.

14. During 2022/23 no new loans were taken. Whilst the borrowing CFR has increased as anticipated, this was less than previously budgeted (see table 2) due to the reappraisal of the capital programme and actual expenditure being less than forecast, the latter been covered by internal borrowing.

15. During 2022/23 the following existing loans matured. The total of maturing loans was £4.7m.

Lender	Issue Date	Repayment Date	Amount £	Rate	Duration (years)
PWLB	23/11/2000	05/11/2022	2,000,000.00	4.75%	21.95
PWLB	03/04/2001	05/11/2022	1,000,000.00	4.75%	21.59
PWLB	15/11/2001	28/02/2023	1,700,000.00	4.50%	21.29

Table 3 – Maturing loans in 2022/23

16. No rescheduling was done during the year.

Investment outturn for 2022/23

17. The Council's investment policy is governed by DLUHC guidance, which has been implemented in the annual investment strategy approved by the Council on 17th February 2022. This policy sets out the approach for choosing investment counterparties and is based on credit ratings provided by the three main credit rating agencies, supplemented by additional market data, (such as rating outlooks, credit default swaps, bank share prices etc.). The Council will also consider environmental, social and governance issues when placing investments after the core investment priorities of security, liquidity and yield have been assessed and this will be

done through the use of the FTSE4Good index or any suitable alternative responsible investment index or information to be decided by the s151 officer. The investment activity during the year conformed to the approved strategy, and the Council had no liquidity difficulties.

18. The Council maintained an average investment balance of £52.422 in 2022/23 compared to £45.722m in 2021/22. The surplus funds earned an average rate of return of 2.02% in 2022/23 compared to 0.10% in 2021/22. Cash supporting the Council's reserves, balances and cash flow was used as an interim measure to delay and minimise long term borrowing throughout the year.

19. The level of cash balances available is largely dependent on the timing of the Council's cash flow as a result of precept payments, receipt of grants, receipt of developers contributions, borrowing for capital purposes, payments to its suppliers of goods and services and spend progress on the Capital Programme. Cash held compared with this time last year has increased rather than decreased due to the timing of these cash flows and the cash balances are therefore only available on a temporary basis. Cash balances have been helped in 2022/23 by a reappraisal of the capital programme and slower than expected capital spending.

20. The Council uses a benchmark indicator to assess the Councils investment performance, and this is the average Sterling Overnight Index Average (SONIA). SONIA is based on actual transactions reflecting the average of the interest rates that banks pay to borrow sterling overnight.

21. Table 5 shows the average investment performance for the financial year 2022/23 using SONIA. The comparators given are based on overnight and 7 day benchmarks. These comparators have been chosen as the Council has mainly held cash liquid or in short term notice deposits over the year and so as the Bank of England has increased interest rates from 0.75 to 4.25 during 2022/23 the Councils average rate of return, while increasing, has remained lower than SONIA due to the liquid nature of the cash holdings.

Benchmark	Average Benchmark Return %	Average Council Performance %
Overnight	2.24	2.02
7 day backward looking	2.23	2.02

Table 5 – SONIA vs. CYC comparison 2022/23

Consultation

22. The report will be reviewed and scrutinised by Audit and Governance Committee in July 2023.

Options

23. Not applicable.

Council Plan

24. Effective treasury management ensures the Council has sufficient liquidity to operate, safeguards investments, maximises return on those investments and minimises the cost of debt. This allows more resources to be allocated for delivering the Council's priorities as set out in the Council Plan.

Implications

25. This report has the following implications:

- **Financial** are contained throughout the main body of the report.
- **Human Resources (HR)** There are no HR implications.
- **One Planet Council / Equalities** There are no One Planet Council or equalities implications.
- **Legal** Treasury management activities have to conform to the Local Government Act 2003, which specifies that the Council is required to adopt the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice.
- **Crime and Disorder** There are no crime and disorder implications.
- **Information Technology (IT)** There are no IT implications.
- **Property** There are no property implications.
- **Other** There are no other implications.

Risk Management

26. The treasury function is a high-risk area due to the large value transactions that take place. As a result, there are strict procedures set out as part of the treasury management practices statement. The scrutiny of this and other monitoring reports is carried out by Audit and Governance Committee as part of the Council's system of internal control.

Contact Details

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<tr><td>Report Approved</td><td>√</td><td>Date</td><td>17th May 2023</td></tr>
<tr><td colspan="3">Wards Affected: List wards or tick box to indicate all</td><td>All</td><td>✓</td></tr>
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Background Papers:
None

Annexes:
Annex A: Prudential Indicators 2022/23

List of Abbreviations Used in this Report

CFR - Capital Financing Requirement
CIPFA - Chartered Institute of Public Finance & Accountancy
CPI - Consumer Price Index
CYC – City of York Council
DLUHC – Department for Levelling Up, Housing and Communities
MPC - Monetary Policy Committee
MRP - Minimum Revenue Provision
PWLB - Public Works Loan Board
SONIA – Sterling Overnight Index Average