EXECUTIVE **20 JUNE 2022**

SUBJECT:	**TREASURY MANAGEMENT STEWARDSHIP AND ACTUAL PRUDENTIAL INDICATORS REPORT 2021/22 (OUTTURN)**
DIRECTORATE:	**CHIEF EXECUTIVE AND TOWN CLERK**
LEAD OFFICER:	**COLLEEN WARREN – FINANCIAL SERVICES MANAGER**

1. Purpose of Report

1.1 The annual Treasury Management stewardship report is a requirement of the Council's reporting procedures under regulations issued under the Local Government Act 2003. It covers the treasury management activities and the actual prudential and treasury indicators for 2021/22. 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. Executive Summary

2.1 During 2021/22 the Council complied with its legislative and regulatory requirements. The key prudential indicators for the year, with comparators, are as follows:

Actual Prudential Indicators	**2021/22 £000**	**2020/21 £000**
Actual Capital Expenditure	21,895	19,589
Capital Financing Requirement		
General Fund	68,407	67,501
HRA	74,452	70,274
Total	**142,859**	**137,775**
Net borrowing (borrowing less investments)	**75,327**	**89,548**
External debt (borrowing)	**125,177**	**123,448**
Investments		
• Longer than 1 year*		
• Under 1 year	49,850	33,900
• Total	**49,850**	**33,900**

Other prudential and treasury indicators are to be found in section 4. Please note that the figures above and all other figures in this report are based on figures which are subject to the conclusion of final accounts.

3. Background

3.1 The prudential system for capital expenditure is now well established. One of the requirements of the Prudential Code is to ensure adequate monitoring of the capital expenditure plans, prudential indicators (PIs) and treasury management response to these plans. This report fulfils that requirement and shows the status of the Prudential Indicators at 31st March 2022. For the 2021/22 financial year the minimum reporting requirements were that members should receive the following reports:

- an annual Treasury Management Strategy in advance of the year (Council 2nd March 2021)
- a mid-year Treasury Update report (Executive 18th November 2021)
- an annual report following the year describing the activity compared to the strategy (this report)

3.2 Recent changes in the regulatory environment place a much greater onus on members for the review and scrutiny of treasury management policy and activities. This report is important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by members.

3.3 In compliance with the Prudential Code treasury management reports are scrutinised by Performance Scrutiny Committee and reviewed by the Executive prior to reporting to full Council if required. Member training for the Performance Scrutiny and Audit Committees was undertaken on 18th November 2021 and 1st February 2022 in order to support their roles in scrutinising the treasury management strategy and policies.

4. Summary of Performance against Treasury Management Strategy 2021/22

4.1 The full details of transactions in the year and performance against the Prudential Indicators are included at Appendices A and B.

4.2

Actual Prudential Indicators	2021/22	2020/21
Actual Capital Expenditure	21,895	19,589
Capital Financing Requirement		
General Fund	68,407	67,501
HRA	74,452	70,274
Total	**142,859**	**137,775**
Financing Costs as a proportion of Net Revenue Stream		
General Fund	24.0%	22.6%
HRA	31.6%	31.4%

4.3 The Chief Finance Officer confirms that borrowing was only undertaken for a capital purpose and the statutory borrowing limit, the Authorised Limit was not breached.

Additional borrowing of £3.35m was taken in 2021/22.

At 31st March 2022, the principal value of the Council's external debt was £125.177m (£123.448m at 31st March 2021) and that of its investments was £49.85m (£33.9m at 31st March 2021).

4.4 The increase in General Fund Financing costs as a % of net revenue stream in 2021/22, when compared with 2020/21, is due additional MRP charges and lower rates of return on investments. The slight increase in HRA Financing costs results from borrowing arrangements being at rates lower than those for borrowing taken previously but also higher levels of depreciation.

4.5 The financial year 2021/22 continued the challenging environment of previous years; the effect of the Covid 19 pandemic, low investment returns and continuing counterparty risk were the main features.

4.6 Key issues to note from activity during 2021/22:

- The Council's total debt (including leases and lease-type arrangements) at 31st March 2021 was £125.177m (Appendix A section 4.4) compared with the Capital Financing Requirement of £142.86m (Appendix A section 3.5). This represents an under-borrowing position of £17.68m, which is currently being supported by internal resources. Additional long-term borrowing will be taken in future years to bring levels up to the Capital Financing Requirement, subject to liquidity requirements, if preferential interest rates are available.
- The Council's Investments at the 31st March 2022 were £49.85m (Appendix A section 4.3), which is £15.95m higher than at 31st March 2021. Average investment balances for 2021/22 were £44.7m, which was higher than estimated balances of £24.7m in the Medium Term Financial Strategy 2021-26 due to high balances being made available through government grants. It should be noted that this refers to the principal amounts of investments held, whereas the investment values included in the balance sheet are based on fair value. In most cases, this will simply be equal to the principal invested, unless the investment has been impaired.
- Actual investment interest earned on balances was £76.7k compared to £27k estimated in the Medium Term Financial Strategy 2021-26 (Appendix A section 10.2).
- The interest rate achieved on investments was 0.19% (for 2021/22 the average was 0.53%) which reflects the low yield environment during the year. The rate is no longer compared to the LIBID rate which ceased in December 2021.

4.7 Risk Benchmarking

The following reports the outturn position against the security and liquidity benchmarks in the Treasury Management Strategy.

Security

- The average security risk gives the estimated default rate on the investment counterparties which comprise the portfolio at 31st March 2022. The Council's actual average security risk for the portfolio as at 31st March 2021 is 0.014%, compared with the 0.006% for the budgeted portfolio. Whilst higher than anticipated this reflects a very low risk portfolio and equates to a potential financial loss of £2,912 on the investment portfolio of £21m using individual risk of default percentages (£28.85m of our instruments do not have a counterparty credit rating).

- Specified Investments are high security sterling investments (i.e. high credit quality) with a maturity of no more than one year. Non-specified investments are all other investments representing a potentially greater risk; however the risk is still minimal due to the stringent controls over counterparty credit quality contained within the Investment Strategy. The 2021/22 strategy set a maximum limit of 75% of the portfolio to be held in non-specified investments. At 31st March 2022, 100% of the investment portfolio was held in specified investments. The Chief Finance Officer can report that the investment portfolio was maintained within this limit throughout the year.

Liquidity

In respect of this area the Council set liquidity benchmarks to maintain:

- Liquid short term deposits of at least £5 million available with a week's notice.
- Weighted Average Life benchmark was expected to be 0.11 years (40 days).

The actual liquidity indicators at 31st March 2021 were as follows:

- Liquid short term deposits of £28.85 million as at 31st March 2022.
- Weighted Average Life of the investment portfolio was 0.126 years (46 days). This reflects that larger amounts of investments were deposited in short term accounts to deal with cash flow requirements.

The Chief Finance Officer can report that liquidity arrangements were adequate throughout the year.

4.8 **Benchmarking**

The Council participates in the following benchmarking club:

- The Link Asset Services benchmarking club. Link Asset Services is the Council's treasury management advisors and they offer a benchmarking club for their clients. This is organised on a regional group basis. The group to which City of Lincoln belongs has 12 members within the East Midlands region. The following summary shows performance against the group average and against the benchmarking club as a whole, indicating a lower than average risk portfolio, with much lower levels of investment balances achieving a similar level of return.

	CoLC	Group Average	All club members
Principal at 31/3/22	£49,850,000	£121,919,777	£110,804,896
Weighted Average rate of return at 31/3/22	0.43%	0.54%	0.44%
Weighted average maturity at 31/3/22	46 days	103 days	74 days
Weighted average credit risk at 31/3/22	2.60	2.70	2.92

5. Strategic Priorities

5.1 Through its Treasury Management Strategy the Council seeks to reduce the amount of interest it pays on its external borrowing and maximise the interest it achieves on its investments in order to support the Medium Term Financial Strategy and the delivery of the Council's Vision 2025.

6. Organisational Impacts

6.1 Finance - The financial impacts are contained within the main body of the report and within appendices A and B.

6.2 Legal Implications including Procurement Rules - Section 15 of the Local Government Act 2003 requires local authorities 'to have regard (a) to such guidance as the Secretary of State may issue, and (b) to such other guidance as the Secretary of State may by regulations specify'. The Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 in Regulation 24 require local authorities to have regard to the TM Code of Practice. Investment guidance issued by the Ministry for Housing Communities and Local Government (MHCLG – now DLUHC) which came into effect from 1st April 2010 requires investment policy to emphasise security and liquidity over income.

7. Equality, Diversity and Human Rights

7.1 The Public Sector Equality Duty means that the Council must consider all individuals when carrying out their day-to-day work, in shaping policy, delivering services and in relation to their own employees.

It requires that public bodies have due regard to the need to:

- Eliminate discrimination
- Advance equality of opportunity
- Foster good relations between different people when carrying out their activities

Due to the nature of the report, no specific Equality Impact Analysis is required.

8. Risk Implications

8.1 The Council has the freedom to adopt its own treasury management policies. The CIPFA code of practice, which specifies the format and frequency of reporting, is part of the risk management procedures for treasury.

9. Recommendation

9.1 That Executive approves the actual prudential indicators contained within appendices A and B.

9.2 That Executive approves the annual treasury management report for 2021/22.

Key Decision	No
Do the Exempt Information Categories Apply?	No
Call in and Urgency: Is the decision one to which Rule 15 of the Scrutiny Procedure Rules apply?	No
How many appendices does the report contain?	2
List of Background Papers:	Link Annual Stewardship Reports for 2021/22 Medium Term Financial Strategy 2021-26 and 2022-27 Prudential Indicators 2021/22 – 2022/23 and Treasury Management Strategy 2021/22 and 2022/23
Lead Officer:	Colleen Warren – Financial Services Manager

Annual Report on the Treasury Management Service and Actual Prudential Indicators 2021/22

1. Introduction

1.1 The Council undertakes capital expenditure on long-term assets. These activities can be:

- Financed immediately through the application of capital or revenue resources (capital receipts, capital grants, revenue contributions etc.), which has no resultant impact on the Council's borrowing need; or
- If insufficient financing is available, or a decision is taken not to apply resources, the capital expenditure will give rise to a borrowing need.

Capital expenditure activity is regulated by the CIPFA Prudential Code, which requires actual outturn to be reported in the following areas: -

- Capital expenditure;
- Capital Financing Requirement;
- Debt;
- Ratio of financing costs to net revenue stream.

The remaining prudential indicators are included to make the annual reporting comprehensive and to comply with the requirements of the Treasury Management Code.

1.2 Part of the Council's treasury activities is to address any borrowing need, either through borrowing from external bodies, or utilising temporary cash resources within the Council. The wider treasury activities also include managing the Council's cash flows, its previous borrowing activities and the investment of surplus funds. These activities are structured to manage risk foremost, and then optimise performance. This area of activity is regulated by the CIPFA Code of Practice on Treasury Management.

1.3 Wider information on the regulatory requirements is shown in section 11.

2. The Council's Capital Expenditure and Financing 2021/22

2.1 This forms one of the required prudential indicators and shows total capital expenditure for the year and how this was financed.

	2021/22 Actual £'000	2021/22 Revised Estimate £'000	2020/21 Actual £'000
General Fund capital expenditure	6,631	20,398	3,212
HRA capital expenditure	15,264	30,248	16,377
Total capital expenditure	**21,895**	**50,646**	**19,589**
Resourced by:			
Capital receipts	1,340	5,656	1,633
Capital grants & contributions	9,821	15,214	4,553
Direct Revenue Financing	215	6,186	663
Major repairs reserve	3,842	10,514	4,044
Un-financed capital expenditure (additional need to borrow)	**6,677**	**13,076**	**8,696**

2.2 Further details on 2021/22 Capital Expenditure and Financing can be found in the Financial Performance Detailed Outturn 2021/22 report elsewhere on the agenda.

3. The Council's Overall Borrowing Need

3.1 The Council's underlying need to borrow is called the Capital Financing Requirement (CFR). This figure is a gauge for the Council's debt position and represents 2021/22 and prior years' net capital expenditure that has not yet been charged to revenue or other resources.

3.2 Part of the Council's treasury activities is to address this borrowing need, either through borrowing from external bodies, or utilising temporary cash resources within the Council.

3.3 The General Fund element of the CFR is reduced each year by a statutory revenue charge (called the Minimum Revenue Provision - MRP). The total CFR can also be reduced by:

- the application of additional capital resources (such as unapplied capital receipts); or
- charging more than the statutory revenue charge (MRP) each year through a Voluntary Revenue Provision (VRP) or depreciation.

3.4 The Council's MRP policy for 2021/22 was approved by Council on 2nd March 2021 as part of the Prudential Indicators 2021/22 – 2023/24 and Treasury Management Strategy 2021/22.

3.5 The Council's CFR for the year is shown below and represents a key prudential indicator. The CFR includes leasing schemes which increase the Council's borrowing need. No borrowing is actually required against these schemes as a borrowing facility is included in the contract. During the year land appropriations resulted in an appropriation between the General Fund and HRA CFR.

Capital Financing Requirement General Fund	**31 March 2022 Actual £'000**	**31 March 2022 Revised Estimate £'000**	**31 March 2021 Actual £'000**
Opening balance 1 April	67,502	67,502	68,562
Plus un-financed capital expenditure	2,500	9,129	597
Finance leases	0	0	(105)
Less MRP/VRP*	(1,444)	(1,444)	(1,552)
Use of capital receipts	(150)	(3,372)	0
Closing balance 31 March	**68,407**	**71,815**	**67,502**

Capital Financing Requirement HRA	**31 March 2022 Actual £'000**	**31 March 2022 Revised Estimate £'000**	**31 March 2021 Actual £'000**
Opening balance 1 April	70,273	70,273	62,174
Plus un-financed capital expenditure	4,178	3,947	8,099
Closing balance 31 March	**74,451**	**74,220**	**70,273**

* includes finance lease repayments

4. Treasury Position at 31st March 2022

4.1 Whilst the Council's gauge of its underlying need to borrow is the CFR, the Chief Finance Officer and the treasury team manage the Council's actual borrowing position by either:

- borrowing to the CFR,
- choosing to temporarily utilise some flow funds instead of borrowing (under-borrowing)
- borrowing for future increases in the CFR (borrowing in advance of need).

4.2 It should be noted that the figures in this report are based on the principal amounts borrowed and invested and so may differ from those in the final accounts by items such as accrued interest (outstanding interest due to be paid and received as at 31st March), or where the carrying amount is based on fair values.

4.3 During 2021/22 the Chief Finance Officer managed the borrowing position to £125.177 million. The treasury position at the 31st March 2021 compared with the previous year was:

	31 March 2022		31 March 2021	
	Principal £'000	**Average Rate (full year)**	**Principal £'000**	**Average Rate (full year)**
Borrowing Position				
Fixed Interest Rate Debt	125,177	3.02%	123,448	3.25%
Variable Interest Rate Debt	0	N/A	0	N/A
Total Debt (borrowing) *	125,177	3.02%	123,448	3.25%
Capital Financing Requirement (borrowing only)	142,858	N/A	137,775	N/A
Over/(under) borrowing	(17,680)	N/A	(14,327)	N/A
Investment Position				
Fixed Interest Investments	21,000	0.30%	19,000	0.41%
Variable Interest Investments	28,850	0.05%	14,900	0.10%
Total Investments **	49,850	0.19%	33,900	0.20%
Net Borrowing Position	**75,327**		**89,548**	

* Excludes local Bonds & Mortgages and other long-term liabilities (e.g. finance leases)

** The interest rate given differs from the interest rate given in Paragraph 4.6 of the main report because the rates above are for investments held at 31 March whereas the average rate of investment is for investments held during 2021/22.

4.4 The total debt position also includes other long term liabilities such as finance leases and embedded leases within service contracts. The total debt position at 31st March 2022 was £125.177 million as shown below:

	31 March 2022 Actual £'000	**31 March 2022 Revised Estimate £'000**	**31 March 2021 Actual £'000**
Gross borrowing	125,177	136,000	123,448
Other long term liabilities	0	0	0
Total External debt	**125,177**	**136,000**	**123,448**

4.5 The maturity structure of the debt portfolio was as follows:

	31 March 2022 Actual £'000	31 March 2021 Actual £'000
Under 12 months	13,215	7,710
12 months and within 24 months	2,500	8,215
24 months and within 5 years	2,897	6,072
5 years and within 10 years	11,462	10,696
10 years and above	95,103	90,755
Total	**125,177**	**123,448**

4.6 The maturity structure of the investment portfolio was as follows:

	31 March 2022 Actual £'000	31 March 2021 Actual £'000
Longer than 1 year	0	0
Under 1 year	49,850	33,900
Total	**49,850**	**33,900**

5. The Strategy for 2021/22

5.1 The Council's overall core borrowing objectives are:

- To reduce the revenue costs of debt in line with the targets set for the Chief Finance Officer by Council (see local indicators).
- To manage the Council's debt maturity profile, leaving no one future year with a high level of repayments that might cause problems in re-borrowing.
- To effect funding at the cheapest cost commensurate with future risk.
- To forecast average future interest rates and borrow accordingly i.e. short term/variable when rates are 'high', long term/fixed when rates are 'low'.
- To monitor and review the level of variable rate loans in order to take greater advantage of interest rate movements.
- To proactively reschedule debt in order to take advantage of potential savings as interest rates change. Each rescheduling exercise will be considered in terms of the effect of premiums and discounts on the General Fund and the Housing Revenue Account.
- To manage the day-to-day cash flow of the Authority in order to, where possible, negate the need for short-term borrowing. However, short-term borrowing will be incurred, if it is deemed prudent to take advantage of good investment rates.

6. Actual Debt Management Activity during 2021/22

6.1 Borrowing

6.1.1 Long term borrowing, totalling £5m was taken in 2021/22; short term borrowing of £5m was taken in 2021/22; of this £6.645m were replacement loans. The 3% stock, PWLB, short term and annuity borrowing of £8.271m was repaid in 2021/22.

6.1.2 The average rate achieved for borrowing (excluding finance and embedded leases) in 2021/22 was 3.02%, which compares favourably to the target of 4.25% (2020/21 3.25% actual compared to the target of 4.75%). The decrease in rate is due to short term borrowing through other local authorities and new and replacement PWLB borrowing at favourable rates.

	31 March 2022 Actual £'000	31 March 2021 Actual £'000
Interest payable on borrowing	3,797	3,912
- General Fund	1,372	1,485
- HRA	2,425	2,427
Interest payable on finance leases	0	2
- General Fund	0	2
- HRA	0	0

6.2 Rescheduling

6.2.1 No rescheduling was undertaken during the year as the differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

7. Prudential Indicators and Compliance Issues

7.1 Some of the required prudential indicators provide either an overview or specific limits on treasury activity. These are shown below:

7.2 Net Borrowing and the CFR

7.2.1 In order to ensure that borrowing levels are prudent over the medium term the Council's external borrowing, net of investments, must only be for a capital purpose. This essentially means that the Council is not borrowing to support revenue expenditure. Net borrowing should not therefore, except in the short term, have exceeded the CFR for 2021/22 plus the expected changes to the CFR over 2021/22 and 2022/23 from financing the capital programme. This indicator allows the Council some flexibility to borrow in advance of its immediate capital needs in 2021/22. The table below highlights the Council's net borrowing position against the CFR. The Council has complied with this prudential indicator.

	31 March 2022 Actual £'000	31 March 2022 Revised Estimate £'000	31 March 2021 Actual £'000
Net borrowing position	75,327	103,000	89,548
Capital Financing Requirement	142,858	146,035	137,775

7.3 The Authorised Limit and Operational Boundary

7.3.1 The Authorised Limit is the "Affordable Borrowing Limit" required by section 3 of the Local Government Act 2003. The Council does not have the power to borrow above this level. The table below demonstrates that during 2021/22 the Council has maintained gross borrowing within its Authorised Limit.

7.3.2 The Operational Boundary is the expected borrowing position of the Council during the year, and periods where the actual position is either below or over the Boundary is acceptable subject to the Authorised Limit not being breached.

7.3.3 The table below shows the highest borrowing position reached in the year (including temporary borrowing and other long term liabilities) compared to the Authorised Limit and Operational Boundary.

	2021/22 £'000
Authorised Limit (revised estimate)	163,633
Maximum gross borrowing position during 2021/22	127,887
Operational Boundary (revised estimate)	160,833
Average gross borrowing position during 2021/22	124,933
Minimum gross borrowing position during the year	120,177

7.4 Actual financing costs as a proportion of net revenue stream

7.4.1 This indicator identifies the trend in the cost of capital (borrowing and other long-term obligation costs net of investment income) against the net revenue stream.

Financing costs as a proportion of net revenue stream -	2021/22 Actual %	2021/22 Revised Estimate %	2020/21 Actual %
General Fund	24.0%	26.6%	22.6%
HRA	31.6%	30.7%	31.4%

The increase in General Fund Financing costs as a % of net revenue stream in 2021/22, when compared with 2020/21, is due to increased MRP charges and lower rates of return on investments.

The HRA Financing costs results reflect higher than anticipated levels of depreciation.

8. Economic Background for 2021/22

The following commentary on the economic conditions for 2021/22 is provided by Link Asset Services, the Council's treasury management advisers.

8.1 **UK. Economy.** Over the last two years, the coronavirus outbreak has done huge economic damage to the UK and to economies around the world. After the Bank of England took emergency action in March 2020 to cut Bank Rate to 0.10%, it left Bank Rate unchanged at its subsequent meetings until raising it to 0.25% at its meeting on 16th December 2021, 0.50% at its meeting of 4th February 2022 and then to 0.75% in March 2022.

The UK economy has endured several false dawns through 2021/22, but with most of the economy now opened up and nearly back to business-as-usual, the GDP numbers have been robust (9% y/y Q1 2022) and sufficient for the MPC to focus on tackling the second-round effects of inflation, now that the CPI measure has already risen to 6.2% and is likely to exceed 8% in April.

Gilt yields fell towards the back end of 2021, but despite the war in Ukraine gilt yields have shot higher in early 2022. At 1.38%, 2-year yields remain close to their recent 11-year high and 10-year yields of 1.65% are close to their recent six-year high. These rises have been part of a global trend as central banks have suggested they will continue to raise interest rates to contain inflation.

Historically, a further rise in US Treasury yields will probably drag UK gilt yields higher. There is a strong correlation between the two factors. However, the squeeze on real household disposable incomes arising from the 54% leap in April utilities prices as well as rises in council tax, water prices and many phone contract prices, are strong headwinds for any economy to deal with. In addition, from 1st April 2022, employees also pay 1.25% more in National Insurance tax. Consequently, inflation will be a bigger drag on real incomes in 2022 than in any year since records began in 1955.

Average inflation targeting. This was the major change in 2020/21 adopted by the Bank of England in terms of implementing its inflation target of 2%. The key addition to the Bank's forward guidance in August 2020 was a new phrase in the policy statement, namely that "it does not intend to tighten monetary policy until there is clear evidence that significant progress is being made in eliminating spare capacity and *achieving the 2% target sustainably*". That mantra now seems very dated. Inflation is the "genie" that has escaped the bottle, and a perfect storm of supply side shortages, labour shortages, commodity price inflation, the impact of Russia's invasion of Ukraine and subsequent Western sanctions all point to inflation being at elevated levels until well into 2023.

USA. The flurry of comments from Fed officials following the mid-March FOMC meeting – including from Chair Jerome Powell himself – hammering home the hawkish message from the mid-March meeting, has had markets pricing in a further 225bps of interest rate increases in 2022 on top of the initial move to an interest rate range of 0.25% - 0.5%.

In addition, the Fed is expected to start to run down its balance sheet. Powell noted that the rundown could come as soon as the next meeting in May.

The upward pressure on inflation from higher oil prices and potential knock-on impacts on supply chains all argue for tighter policy (CPI is estimated at 7.8% across Q1), but the hit to real disposable incomes and the additional uncertainty points in the opposite direction.

More recently, the inversion of the 10y-2y Treasury yield spread at the end of March led to predictable speculation that the Fed's interest rate hikes would quickly push the US economy into recession. Q1 GDP growth is likely to be only between 1.0% and 1.5% annualised (down from 7% in Q4 2021). But, on a positive note, the economy created more than 550,000 jobs per month in Q1, a number unchanged from the post-pandemic 2021 average. Unemployment is only 3.8%.

EU. With euro-zone inflation having jumped to 7.5% in March it seems increasingly likely that the ECB will accelerate its plans to tighten monetary policy. It is likely to end net asset purchases in June – i.e., earlier than the Q3 date which the ECB targeted in March. And the market is now anticipating possibly three 25bp rate hikes later this year followed by more in 2023. Policymakers have also hinted strongly that they would re-start asset purchases if required. In a recent speech, Christine Lagarde said "we can design and deploy new instruments to secure monetary policy transmission as we move along the path of policy normalisation."

While inflation has hit the headlines recently, the risk of recession has also been rising. Among the bigger countries, Germany is most likely to experience a "technical" recession because its GDP contracted in Q4 2021, and its performance has been subdued in Q1 2022. However, overall, Q1 2022 growth for the Eurozone is expected to be 0.3% q/q with the y/y figure posting a healthy 5.2% gain. Finishing on a bright note, unemployment fell to only 6.8% in February.

China. After a concerted effort to get on top of the virus outbreak in Q1 of 2020, economic recovery was strong in the rest of the year; however, 2021 has seen the economy negatively impacted by political policies that have focussed on constraining digital services, restricting individual freedoms, and re-establishing the power of the One-Party state. With the recent outbreak of Covid-19 in large cities, such as Shanghai, near-term economic performance is likely to be subdued. Official GDP numbers suggest growth of c4% y/y, but other data measures suggest this may be an overstatement.

Japan. The Japanese economic performance through 2021/22 is best described as tepid. With a succession of local lockdowns throughout the course of the year, GDP is expected to have risen only 0.5% y/y with Q4 seeing a minor contraction. The policy rate has remained at -0.1%, unemployment is currently only 2.7% and inflation is sub 1%, although cost pressures are mounting.

World growth. World growth is estimated to have expanded 8.9% in 2021/22 following a contraction of 6.6% in 2020/21.

Deglobalisation. Until recent years, world growth has been boosted by increasing globalisation i.e. countries specialising in producing goods and commodities in which they have an economic advantage and which they then trade with the rest of the world. This has boosted worldwide productivity and growth, and, by lowering costs, has also depressed inflation. However, the rise of China as an economic superpower over the last 30 years, which now accounts for 18% of total world GDP (the USA accounts for 24%), and Russia's recent invasion of Ukraine, has unbalanced the world economy. In addition, after the pandemic exposed how frail extended supply lines were around the world, both factors are now likely to lead to a sharp retrenchment of economies into two blocs of western democracies v. autocracies. It is, therefore, likely that we are heading into a period where there will be a reversal of world globalisation and a decoupling of western countries from dependence on China (and to a much lesser extent Russia) to supply products and vice versa. This is likely to reduce world growth rates.

Central banks' monetary policy. During the pandemic, the governments of western countries have provided massive fiscal support to their economies which has resulted in a big increase in total government debt in each country. It is therefore very important that bond yields stay low while debt to GDP ratios slowly subside under the impact of economic growth. This provides governments with a good reason to amend the mandates given to central banks to allow higher average levels of inflation than we have generally seen over the last couple of decades. Both the Fed and Bank of England have already changed their policy towards implementing their existing mandates on inflation, (and full employment), to hitting an average level of inflation. Greater emphasis could also be placed on hitting subsidiary targets e.g. full employment before raising rates. Higher average rates of inflation would also help to erode the real value of government debt more quickly.

9. Investment Position

9.1 The Council's investment policy is governed by DLUHC Guidance, which has been implemented in the Annual Investment Strategy approved by Council on 2nd March 2021. 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 investment activity during the year conformed to the approved strategy, and the Council had no liquidity difficulties.

9.2 The Council's longer-term cash balances comprise primarily revenue and capital resources, although these are influenced by cash flow considerations. The Council's core cash resources comprised as follows, and meet the expectations of the budget.

Balance Sheet Resources (draft) - General Fund	**31 March 2022 £'000**	**31 March 2021 £'000**
Balances	2,193	2,667
Earmarked reserves	12,473	19,563
Provisions	2,197	2,353
Usable capital receipts	30	623
Total	**16,893**	**25,206**
Balance Sheet Resources (draft) - HRA	**31 March 2022 £'000**	**31 March 2021 £'000**
Balances	1,025	1,075
Earmarked reserves	2,880	2,617
Usable capital receipts	5,678	3,889
Total	**9,583**	**7,581**
Total General Fund & HRA	**26,476**	**32,787**

Please note that at the time of writing the year end position is yet to be finalised and the balance sheet resources are draft, subject to approval of recommendations made in the outturn report.

10. Investments Held by the Council

10.1 The Council does not have the expertise or resources to actively use a wide range of investment products and therefore performance tends to be more stable but lower over the longer term than for professionally managed funds (whose performance may fluctuate more). The Council maintained an average balance of £44.695m and received an average return of 0.19%. The comparable performance indicator was previously the average 7-day LIBID rate; this is no longer available and the Treasury team are working with our advisors to develop a revised performance indicator.

10.2 In 2021/22, £76k interest was earned on balances (£72k in 2020/21). This is £49k more than the £27k estimated in the Medium Term Financial Strategy 2021-26 primarily due to increases in the BoE base rate during the year and higher than anticipated levels of balances. The analysis of this result is shown in the table below.

	MTFS 2021-26 Budget £'000	**Outturn 2021/22 £'000**
Interest earned - General fund & other commitments	18	52
- HRA	9	24

Total interest earned	**27**	**76**
Average balance invested in year	24,700	44,695
Average interest rate achieved	0.13%	0.19%

* The interest rate given differs from that given in Paragraph 4.3 of the main report because this is an average interest for the year whereas the interest rate given in paragraph 4.3 is a rate for balances at 31 March 2022.

The Economic Background for 2021/22 (see Section 8) sets out the economic conditions during this period. Below is Link's forecast for interest rates at 31 March 2022.

Link Group Interest Rate View 7.2.22	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25
BANK RATE	0.75	1.00	1.00	1.25	1.25	1.25	1.25	1.25	1.25	1.25	1.25	1.25	1.25
3 month av. earnings	0.80	1.00	1.00	1.20	1.20	1.20	1.20	1.20	1.20	1.20	1.20	1.20	1.20
6 month av. earnings	1.00	1.10	1.20	1.30	1.30	1.30	1.30	1.30	1.30	1.30	1.30	1.30	1.30
12 month av. earnings	1.40	1.50	1.60	1.70	1.70	1.60	1.60	1.50	1.40	1.40	1.40	1.40	1.40
5 yr PWLB	2.20	2.30	2.30	2.30	2.30	2.30	2.30	2.30	2.30	2.30	2.30	2.30	2.30
10 yr PWLB	2.30	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40
25 yr PWLB	2.40	2.50	2.50	2.60	2.60	2.60	2.60	2.60	2.60	2.60	2.60	2.60	2.60
50 yr PWLB	2.20	2.30	2.30	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40

11. Risk Benchmarking

The regulatory framework also requires the consideration and approval of security and liquidity benchmarks. Yield benchmarks are currently widely used to assess investment performance. Security and liquidity benchmarks are used to assess the level of risk in the investment portfolio and whether sufficient liquidity is being maintained.

11.1 The following reports the current position against the benchmarks originally approved in the 2021/22 Treasury Management Strategy.

Security

- The Council's security risk for the portfolio as at 31st March 2022 is 0.014%, which compares with the 0.006% for the budgeted portfolio. This gives the estimated default rate on the investment counterparties which comprise the portfolio at 31st March 2022. This equates to a potential financial loss of £2,912 on the investment portfolio of £21m - £28.85m of the portfolio is not subject to historic counterparty risk information
- Specified Investments are high security sterling investments (i.e. high credit quality) with a maturity of no more than one year. Non-specified investments are all other investments representing a potentially greater risk however the risk is still minimal due to the stringent controls over counterparty credit quality contained within the Investment Strategy. The 2021/22 strategy set a maximum limit of 75% of the portfolio to be held in non-specified investments. At 31st March 2022, 100% of the investment portfolio was held in specified investments. The Chief Finance Officer can report that the investment portfolio was maintained within this limit throughout the year.

Liquidity

In respect of this area the Council set liquidity benchmarks to maintain:

- Liquid short term deposits of at least £5 million available with a week's notice.
- Weighted Average Life benchmark was expected to be 0.11 years (40 days).

The actual liquidity indicators at 31st March 2022 were as follows:

- Liquid short term deposits of £28.85 million as at 31st March 2022.
- Weighted Average Life of the investment portfolio was 0.126 years (46 days).

11.2 **Performance Indicators set for 2021/22**

11.3 The Code of Practice on Treasury Management requires the Council to set performance indicators to assess the adequacy of the treasury management function over the year. The Chief Finance Officer set 8 local indicators for 2021/22, which aim to add value and assist the understanding of the main prudential indicators. These indicators, detailed in Appendix B, are:

- Debt – Borrowing rate achieved against average 7 day LIBOR – this is no longer available
- Investments – Investment rate achieved against average 7 day LIBID – this is no longer available.
- Average rate of interest paid on the Councils Debt during the year – this will evaluate performance in managing the debt portfolio to release revenue savings.
- The amount of interest on debt as a percentage of gross revenue expenditure.
- Limit on fixed interest rate investments
- Limit on fixed interest rate debt
- Limit on variable rate investments
- Limit on variable rate debt

Regulatory Framework, Risk and Performance

12. The Council's treasury management activities are regulated by a variety of professional codes, statutes and guidance:

- The Local Government Act 2003 (the Act), which provides the powers to borrow and invest as well as providing controls and limits on this activity;
- The Act permits the Secretary of State to set limits either on the Council or nationally on all local authorities restricting the amount of borrowing which may be undertaken (although no restrictions were made in 2021/22);
- Statutory Instrument (SI) 3146 2003, as amended, develops the controls and powers within the Act;
- The SI requires the Council to undertake any borrowing activity with regard to the CIPFA Prudential Code for Capital Finance in Local Authorities;

- The SI also requires the Council to operate the overall treasury function with regard to the CIPFA Code of Practice for Treasury Management in the Public Services;
- Under the Act the ODPM has issued Investment Guidance to structure and regulate the Council's investment activities;

Under section 238(2) of the Local Government and Public Involvement in Health Act 2007 the Secretary of State has taken powers to issue guidance on accounting practices.

12.1 The Council has complied with all of the above relevant statutory and regulatory requirements, which limit the levels of risk associated with its treasury management activities. In particular its adoption and implementation of both the Prudential Code and the Code of Practice for Treasury Management means both that its capital expenditure is prudent, affordable and sustainable, and its treasury practices demonstrate a low risk approach.

13. The Council is aware of the risks of passive management of the treasury portfolio and, with the support of Link Asset Services, the Council's advisers, has proactively managed its treasury position over the year. The Council has continued to utilise historically low borrowing costs and has complied with its internal and external procedural requirements. There is little risk of volatility of costs in the current debt portfolio as the interest rates are predominantly fixed, utilising long-term loans.

13.1 Shorter-term variable rates and likely future movements in these rates predominantly determine the Council's investment return. These returns can therefore be volatile and, whilst the risk of loss of principal is minimised through the annual investment strategy, accurately forecasting future returns can be difficult.

Prudential and Treasury Indicators 2021/22

1. PRUDENTIAL INDICATORS	2021/22 Actual	2021/22 Estimated	2020/21 Actual
Capital Expenditure	**£'000**	**£'000**	**£'000**
General Fund	6,631	20,398	3,212
HRA	15,264	30,248	16,377
TOTAL	21,985	50,646	19,589
Ratio of financing costs to net revenue stream	**%**	**%**	**%**
General Fund	24.0%	26.6%	22.9%
HRA	31.6%	30.7%	31.4%
Borrowing requirement General Fund	**£'000**	**£'000**	**£'000**
Borrowing requirement at 1 April	67,501	67,501	68,562
Borrowing requirement at 31 March	68,407	71,815	67,501
In-year borrowing requirement	905	4,313	597
Borrowing requirement HRA	**£'000**	**£'000**	**£'000**
Borrowing requirement at 1 April	70,274	70,274	62,174
Borrowing requirement at 31 March	74,451	74,220	70,274
In-year borrowing requirement	4,178	3,946	8,099
Net Debt	**£'000**	**£'000**	**£'000**
Actual borrowing less investments	75,327	100,633	89,548
CFR	**£'000**	**£'000**	**£'000**
General Fund	68,407	71,815	67,501
HRA	74,451	74,220	70,274
TOTAL	142,858	146,035	137,775
Annual change in Capital Financing Requirement	**£'000**	**£'000**	**£'000**
General Fund	905	4,313	(1,060)
HRA	4,178	3,947	8,099
TOTAL	5,083	8,260	7,039

2. TREASURY MANAGEMENT INDICATORS	**2021/22 Revised**	**2021/22 Estimated**	**2020/21 Actual**
Authorised Limit for external debt –	**£'000**	**£'000**	**£'000**
Borrowing	125,177	162,133	123,448
Other long term liabilities	0	1,500	0
TOTAL	125,177	163,633	123,448
Operational Boundary for external debt -	**£'000**	**£'000**	**£'000**
Borrowing	125,177	148,633	123,448
Other long term liabilities	0	1,200	0
TOTAL	125,177	160,833	123,448
Actual external debt	**£'000**	**£'000**	**£'000**
General Fund	54,079	63,000	52,909
HRA	71,098	73,000	70,539
TOTAL	125,177	136,000	123,448
Upper limit for fixed interest rate exposure	**£m**	**Target £m**	**£m**
Net principal re fixed rate borrowing / investments	104.2	125.3	104.5
Upper limit for variable rate exposure	**£m**	**Target £m**	**£m**
Net principal re variable rate borrowing / investments *	(28.85)	53.5	14.9
Upper limit for total principal sums invested for over 1 year	**£'000**	**£**	**£'000**
(per maturity date)	Nil	5	Nil

***negative due to holding variable investments only**

Maturity structure of fixed rate borrowing during 2021/22	**Actual %**	**Upper limit %**	**Lower limit %**
Under 12 months	11%	40	0
12 months and within 24 months	2%	40	0
24 months and within 5 years	2%	60	0
5 years and within 10 years	9%	80	0
10 years and above	76%	100	10

Local Indicators Treasury Management Indicators

	2021/22 Actual %	2021/22 Revised %	2020/21 Actual %
Debt - Borrowing rate achieved i.e. temporary borrowing (loans of less than 1 year)	Achieved 0.55%	LIBOR no longer available for comparison	Achieved 0.40% LIBOR 0.054% +0.36%

	2021/22 Actual %	2021/22 Revised %	2020/21 Actual %
Investment rate achieved	Achieved 0.19%	LIBID no longer available for comparison	Achieved 0.2% LIBID - 0.07% +0.27%

	2021/22 Actual %	2021/22 Revised %	2020/21 Actual %
Average rate of Interest Paid on Council Debt (%)	3.02%	3.25%	3.25%

	2021/22 Actual %	2021/22 Target %	2020/21 Actual %
Interest on Debt as a % of Gross Revenue Expenditure	3.8%	4.4%	3.6%
General Fund	2.0%	2.4%	1.88%
HRA	7.6%	8.1%	8.02%

	2021/22 Actual (ave) %	2021/22 Target %	2020/21 Actual %
Upper limits on fixed interest rate investments	53%	100%	56%

	2021/22 Actual %	2021/22 Target %	2020/21 Actual %
Upper limits on fixed interest rate debt	100%	100%	100%

	2021/22 Actual (ave) %	2021/22 Target %	2020/21 Actual %
Upper limits on variable interest rate investments	47%	75%	44%

	2021/22 Actual %	2021/22 Target %	2020/21 Actual %
Upper limits on variable interest rate debt	0%	40%	0%