EXECUTIVE **30 MAY 2023**

SUBJECT:	**TREASURY MANAGEMENT STEWARDSHIP AND ACTUAL PRUDENTIAL INDICATORS REPORT 2022/23 (OUTTURN)**
REPORT BY:	**CHIEF FINANCE OFFICER**
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 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. Executive Summary

2.1 During 2022/23 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**	**2022/23 £000**
Actual Capital Expenditure	21,895	23,466
Capital Financing Requirement		
General Fund	68,407	68,881
HRA	74,452	77,222
Total	**142,859**	**146,103**
Net borrowing (borrowing less investments)	**75,327**	**85,277**
External debt (borrowing)	**125,177**	**121,962**
Investments		
• Longer than 1 year*		
• Under 1 year	49,850	85,277
• Total	**49,850**	**85,277**

Other prudential and treasury indicators are to be found in Appendix B. The Chief Finance Officer also confirms that borrowing was only undertaken for a capital purpose and the statutory borrowing limit, (the authorised limit), was not breached.

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 2023. For the 2022/23 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 1st March 2022)
- a mid-year Treasury Update report (Executive 17th November 2022)
- 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 17th November 2022 and 31st January 2023 in order to support their roles in scrutinising the treasury management strategy and policies.

4. Summary of Performance against Treasury Management Strategy 2022/23

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 The decrease in General Fund Financing costs as a % of net revenue stream in 2022/23, when compared with 2021/22, is due to a change in MRP policy, resulting in a reduction in MRP charges and a reduction in borrowing due to higher interest rates. There has been a minimal increase in HRA ratio of financing costs against rental income resulting from higher levels of depreciation and a decrease in rental income.

4.3 The financial year 2022/23 continued the challenging environment of previous years; the effect of the Covid 19 pandemic, the increase in inflation, the cost of living crisis, the challenge of pro-active investment of surplus cash for the first time in over a decade, and continuing counterparty risk were the main features.

4.4 Key Issues to Note from Activity during 2022/23:

- The Council's total debt (including leases and lease-type arrangements) at 31st March 2023 was £121.962m (Appendix A section 4.4) compared with the

Capital Financing Requirement of £146.103m (Appendix A section 3.5). This represents an under-borrowing position of £24.141m, 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 2023 were £49.85m (Appendix A section 4.3), which is £13.165m lower than at 31st March 2022. Average investment balances for 2022/23 were £55.6m, which was higher than estimated balances of £30m in the Medium Term Financial Strategy 2022-27 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 £1.167m compared to £126k estimated in the Medium Term Financial Strategy 2022-27 (Appendix A section 10.2).
- The interest rate achieved on investments was 2.10% (for 2021/22 the average was 0.19%).

4.5 **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 2023. The Council's actual average security risk for the portfolio as at 31st March 2023 is 0.012%, compared with the 0.012% for the budgeted portfolio. This reflects a very low risk portfolio and equates to a potential financial loss of £2,351 on the investment portfolio of £22m using individual risk of default percentages (£14.685m 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 2022/23 strategy set a maximum limit of 75% of the portfolio to be held in non-specified investments. At 31st March 2023, 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 0.08 years (29 days).

The actual liquidity indicators at 31st March 2023 were as follows:

- Liquid short term deposits of £14.685 million as at 31st March 2023.
- Weighted Average Life of the investment portfolio was 0.181 years (66 days). This reflects the changing investment landscape with a balance between maintaining cash for liquidity purposes and “laddering” deposits on a rolling basis to lock in the increase in investment rates as duration was extended.

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

4.6 **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 13 members within the East Midlands region. The following summary shows performance against the group average, Not Metropolitan districts and the population as a whole, indicating a lower than average risk portfolio, with much lower levels of investment balances achieving a level of return in excess of similar authorities.

	CoLC	Benchmarking Group Average	Non-Met Districts	Population Average
Principal at 31/3/23	£36,685,000	£97,264,194	£44,926,554	
Weighted Average rate of return at 31/3/23	4.09%	3.93%	3.6%	3.62%
Weighted average maturity at 31/3/23	66 days	68 days	63 days	65 days
Weighted average credit risk at 31/3/23	2.96	2.89	2.97	2.8

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 2022/23.

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 2022/23 Medium Term Financial Strategy 2022-27 and 2023-28 Prudential Indicators 2022/23 – 2023/24 and Treasury Management Strategy 2022/23 and 2023/24
Lead Officer:	Colleen Warren – Financial Services Manager

Appendix A

Annual Report on the Treasury Management Service and Actual Prudential Indicators 2022/23

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 2022/23

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

	2022/23 Actual £'000	2022/23 Revised Estimate £'000	2021/22 Actual £'000
General Fund capital expenditure	10,818	17,860	6,631
HRA capital expenditure	12,647	20,499	15,264
Total capital expenditure	**23,465**	**38,359**	**21,895**
Resourced by:			
Capital receipts	1,934	2,469	1,340
Capital grants & contributions	10,330	14,385	9,821
Direct Revenue Financing	62	4,824	215
Major repairs reserve	7,465	9,348	3,842
Un-financed capital expenditure (additional need to borrow)	**3,674**	**7,333**	**6,677**

2.2 Further details on 2022/23 Capital Expenditure and Financing can be found in the Financial Performance Detailed Outturn 2022/23 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 2022/23 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 2022/23 was approved by Council on 1st March 2022 as part of the Prudential Indicators 2022/23 – 2024/25 and Treasury Management Strategy 2022/23. The MRP policy for 2022/23 was revised as part of the Prudential Indicators 2023/24 – 2025/26 and Treasury Management Strategy 2023/24 and approved by Full Council on 28th February 2023.

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.

Capital Financing Requirement General Fund	**31 March 2023 Actual £'000**	**31 March 2023 Revised Estimate £'000**	**31 March 2022 Actual £'000**
Opening balance 1 April	68,407	68,407	67,502
Plus un-financed capital expenditure	1,298	8,299	2,500
Finance leases	0	0	0
Less MRP/VRP*	(824)	(1,687)	(1,444)
Use of capital receipts	0	(3,221)	(150)
Closing balance 31 March	**68,881**	**71,798**	**68,407**

Capital Financing Requirement HRA	**31 March 2023 Actual £'000**	**31 March 2023 Revised Estimate £'000**	**31 March 2022 Actual £'000**
Opening balance 1 April	74,451	74,451	70,273
Plus un-financed capital expenditure	2,771	3,552	4,178
Closing balance 31 March	**77,222**	**78,003**	**74,451**

* includes finance lease repayments

4. Treasury Position at 31st March 2023

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 2022/23 the Chief Finance Officer managed the borrowing position to £121.962 million. The treasury position at the 31st March 2023 compared with the previous year was:

	31 March 2023		31 March 2022	
	Principal £'000	**Average Rate (full year)**	**Principal £'000**	**Average Rate (full year)**
Borrowing Position				
Fixed Interest Rate Debt	121,962	3.02%	125,177	3.02%
Variable Interest Rate Debt	0	N/A	0	N/A
Total Debt (borrowing) *	121,962	3.02%	125,177	3.02%
Capital Financing Requirement (borrowing only)	146,103	N/A	142,858	N/A
Over/(under) borrowing	(24,141)	N/A	(17,680)	N/A
Investment Position				
Fixed Interest Investments	22,000	2.17%	21,000	0.30%
Variable Interest Investments	14,685	2.01%	28,850	0.05%
Total Investments **	36,685	2.10%	49,850	0.19%
Net Borrowing Position	**85,277**		**75,327**	

* 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 2022/23.

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 2023 was £121.962 million as shown below:

	31 March 2023 Actual £'000	**31 March 2023 Revised Estimate £'000**	**31 March 2022 Actual £'000**
Gross borrowing	121,962	121,962	125,177
Other long term liabilities	0	0	0
Total External debt	**121,962**	**121,962**	**125,177**

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

	31 March 2023 Actual £'000	31 March 2022 Actual £'000
Under 12 months	12,500	13,215
12 months and within 24 months	2,000	2,500
24 months and within 5 years	3,397	2,897
5 years and within 10 years	11,862	11,462
10 years and above	92,203	95,103
Total	**121,962**	**125,177**

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

	31 March 2023 Actual £'000	31 March 2022 Actual £'000
Longer than 1 year	0	0
Under 1 year	36,685	49,850
Total	**36,685**	**49,850**

5. The Strategy for 2022/23

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 2022/23

6.1 Borrowing

6.1.1 No new long term borrowing was taken out 2022/23; short term borrowing of £5m was taken in 2022/23. PWLB, short term and annuity borrowing of £8.215m was repaid in 2022/23.

6.1.2 The average rate achieved for borrowing (excluding finance and embedded leases) in 2022/23 was 3.02%, which compares favourably to the target of 4.25% (2021/22 3.02% actual compared to the target of 4.75%). The average rate has remained low due to an increase in internal borrowing whilst interest rates are high.

	31 March 2023 Actual £'000	**31 March 2022 Actual £'000**
Interest payable on borrowing	3,840	3,797
- General Fund	1,408	1,372
- HRA	2,432	2,425
Interest payable on finance leases	0	0
- General Fund	0	0
- 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 2022/23 plus the expected changes to the CFR over 2022/23 and 2023/24 from financing the capital programme. This indicator allows the Council some flexibility to borrow in advance of its immediate capital needs in 2022/23. The table below highlights the Council's net borrowing position against the CFR. The Council has complied with this prudential indicator.

	31 March 2023 Actual £'000	March 2023 Revised Estimate £'000	31 March 2022 Actual £'000
Net borrowing position	85,277	76,962	75,327
Capital Financing Requirement	146,103	149,801	142,858

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 2022/23 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.

	2022/23 £'000
Authorised Limit (revised estimate)	136,920
Maximum gross borrowing position during 2022/23	125,177
Operational Boundary (revised estimate)	133,162
Average gross borrowing position during 2022/23	127,162
Minimum gross borrowing position during the year	121,962

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 -	2022/23 Actual %	2022/23 Revised Estimate %	2021/22 Actual %
General Fund	17.9%	13.2%	24.0%
HRA	33.5%	27.5%	31.6%

The reduction in General Fund Financing costs as a % of net revenue stream in 2022/23, when compared with 2021/22, is due to reduction in MRP post policy change and letting debt mature rather than refinancing.

The increase in HRA Financing costs ratio reflect higher than anticipated levels of depreciation.

8. Economic Background for 2022/23

The following commentary on the economic conditions for 2022/23 is provided by Link Asset Services, the Council’s treasury management advisers.

8.1 <u>UK Economy.</u>

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

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

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

Q2 of 2022 saw UK GDP deliver growth of +0.1% q/q, but this was quickly reversed in the third quarter, albeit some of the fall in GDP can be placed at the foot of the extra Bank Holiday in the wake of the Queen's passing. Q4 GDP was positive at 0.1% q/q. Most recently, January saw a 0.3% m/m increase in GDP as the number of strikes reduced compared to December. In addition, the resilience in activity at the end of 2022 was, in part, due to a 1.3% q/q rise in real household disposable incomes. A big part of that reflected the £5.7bn payments received by households from the government under the Energy Bills Support Scheme.

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

The UK unemployment rate fell through 2022 to a 48-year low of 3.6%, and this despite a net migration increase of c500k. The fact remains, however, that with many economic participants registered as long-term sick, the UK labour force shrunk by c500k in the year to June. Without an increase in the labour force participation rate, it is hard to see how the UK economy will be able to grow its way to prosperity, and with average wage increases running at over 6% the MPC will be concerned that wage inflation will prove just as sticky as major supply-side shocks to food (up 18.3% y/y in February 2023) and energy that have endured since Russia's invasion of Ukraine on 22 February 2022.

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

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

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

Our economic analysts, Capital Economics, expect real GDP to contract by around 0.2% q/q in Q1 and forecast a recession this year involving a 1.0% peak-to-trough fall in real GDP.

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

As for equity markets, the FTSE 100 started 2023 strongly, rising to a record high of 8,014 on 20th February, as resilient data and falling inflation boosted earnings. But global equities fell sharply after concerns over the health of the global banking system emerged early in March. The fall in the FTSE 100 was bigger than the drop in the US S&P 500. Indeed, at around 7,600 now, the FTSE is 5.2% below its record high on 20th February, while the S&P 500 is only 1.9% lower over the same period. That's despite UK banks having been less exposed and equity prices in the UK's financial sector not falling as far. It may be due to the smaller decline in UK interest rate expectations and bond yields, which raise the discounted value of future earnings, compared to the US.

<u>USA.</u>

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

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

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

<u>EU.</u>

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

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 1st March 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 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 2023 £'000**	**31 March 2022 £'000**
Balances	2,420	2,193
Earmarked reserves	7,040	12,473
Provisions	1,985	2,197
Usable capital receipts	13	30
Total	**11,458**	**16,893**
Balance Sheet Resources (draft) - HRA	**31 March 2023 £'000**	**31 March 2022 £'000**
Balances	1,184	1,025
Earmarked reserves	3,509	2,880
Usable capital receipts	6,405	5,678
Total	**11,098**	**9,583**
Total General Fund & HRA	**22,556**	**26,476**

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 £55.6m and received an average return of 2.10%. The comparable performance indicator is SONIA 7 day uncompounded (2.23%).

10.2 In 2022/23, £1.167m interest was earned on balances (£76k in 2021/22). This is £1.041m more than the £126k estimated in the Medium Term Financial Strategy 2022-27 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 2022-27 Budget £'000	Outturn 2022/23 £'000
Interest earned - General fund & other commitments	60	553
- HRA	66	614
Total interest earned	**126**	**1,167**
Average balance invested in year	30,000	55,555
Average interest rate achieved	0.42%	2.10%

* 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 2023.

The Economic Background for 2022/23 (Section 8) sets out the economic conditions during this period. Below is Link's forecast for interest rates at 31 March 2023.

Link Group Interest Rate View 27.03.23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25
BANK RATE	4.50	4.50	4.25	4.00	3.50	3.25	3.00	2.75	2.75	2.50	2.50
3 month ave earnings	4.50	4.50	4.30	4.00	3.50	3.30	3.00	2.80	2.80	2.50	2.50
6 month ave earnings	4.50	4.40	4.20	3.90	3.40	3.20	2.90	2.80	2.80	2.60	2.60
12 month ave earnings	4.50	4.40	4.20	3.80	3.30	3.10	2.70	2.70	2.70	2.70	2.70
5 yr PWLB	4.10	4.10	3.90	3.80	3.70	3.60	3.50	3.40	3.30	3.20	3.20
10 yr PWLB	4.20	4.20	4.00	3.90	3.80	3.70	3.50	3.50	3.40	3.30	3.30
25 yr PWLB	4.60	4.50	4.40	4.20	4.10	4.00	3.80	3.70	3.60	3.50	3.50
50 yr PWLB	4.30	4.20	4.10	3.90	3.80	3.70	3.50	3.50	3.30	3.20	3.20

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 2022/23 Treasury Management Strategy.

Security

- The Council's security risk for the portfolio as at 31st March 2023 is 0.012%, which compares with the 0.012% for the budgeted portfolio. This gives the estimated default rate on the investment counterparties which comprise the portfolio at 31st March 2023. This equates to a potential financial loss of £2,351 on the investment portfolio of £22m - £14.685m 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 2022/23 strategy set a maximum limit of 75% of the portfolio to be held in

non-specified investments. At 31st March 2023, 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 0.08 years (29 days).

The actual liquidity indicators at 31st March 2023 were as follows:

- Liquid short term deposits of £14.685 million as at 31st March 2023.
- Weighted Average Life of the investment portfolio was 0.181 years (66 days).

11.2 **Performance Indicators set for 2022/23**

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 2022/23, 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 SONIA overnight average
- Investments – Investment rate achieved against SONIA overnight average
- 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 2022/23);

- 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 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.

Appendix B

Prudential and Treasury Indicators 2022/23

1. PRUDENTIAL INDICATORS	2022/23 Actual	2022/23 Estimated	2021/22 Actual
Capital Expenditure	**£'000**	**£'000**	**£'000**
General Fund	10,818	17,860	6,631
HRA	12,647	20,499	15,264
TOTAL	23,465	38,359	21,985
Ratio of financing costs to net revenue stream	**%**	**%**	**%**
General Fund	17.9%	13.2%	24.0%
HRA	33.5%	27.5%	31.6%
Borrowing requirement General Fund	**£'000**	**£'000**	**£'000**
Borrowing requirement at 1 April	68,407	68,407	67,501
Borrowing requirement at 31 March	68,881	71,798	68,407
In-year borrowing requirement	474	3,391	905
Borrowing requirement HRA	**£'000**	**£'000**	**£'000**
Borrowing requirement at 1 April	74,451	74,451	70,274
Borrowing requirement at 31 March	77,222	78,003	74,451
In-year borrowing requirement	2,771	3,552	4,178
Net Debt	**£'000**	**£'000**	**£'000**
Actual borrowing less investments	85,277	76,962	75,327
CFR	**£'000**	**£'000**	**£'000**
General Fund	68,881	71,798	68,407
HRA	77,222	78,003	74,451
TOTAL	146,103	149,801	142,858
Annual change in Capital Financing Requirement	**£'000**	**£'000**	**£'000**
General Fund	474	3,391	905
HRA	2,771	3,552	4,178
TOTAL	3,245	6,943	5,083

2. TREASURY MANAGEMENT INDICATORS	**2022/23 Revised**	**2022/23 Estimated**	**2021/22 Actual**
Authorised Limit for external debt –	**£'000**	**£'000**	**£'000**
Borrowing Other long term liabilities TOTAL	121,962 0 121,962	134,450 1,380 135,830	125,177 0 125,177
Operational Boundary for external debt -	**£'000**	**£'000**	**£'000**
Borrowing Other long term liabilities TOTAL	121,962 0 121,962	131,962 1,200 133,162	125,177 0 125,177
Actual external debt	**£'000**	**£'000**	**£'000**
General Fund HRA TOTAL	55,864 66,098 121,962	55,864 66,098 121,962	54,079 71,098 125,177
Upper limit for fixed interest rate exposure	**£m**	**Target £m**	**£m**
Net principal re fixed rate borrowing / investments	116.5	118.7	104.2
Upper limit for variable rate exposure	**£m**	**Target £m**	**£m**
Net principal re variable rate borrowing / investments *	48.8	52.0	(28.85)
Upper limit for total principal sums invested for over 1 year	**£'000**	**£m**	**£'000**
(per maturity date)	Nil	5	Nil

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

Maturity structure of fixed rate borrowing during 2022/23	**Actual %**	**Upper limit %**	**Lower limit %**
Under 12 months	6%	40	0
12 months and within 24 months	10%	40	0
24 months and within 5 years	2%	60	0
5 years and within 10 years	9%	80	0
10 years and above	73%	100	10

Appendix B

Local Indicators Treasury Management Indicators

	2022/23 Actual %	2022/23 Revised %	2021/22 Actual %
Debt - Borrowing rate achieved i.e., temporary borrowing (loans of less than 1 year)	0.55%	SONIA OVERNIGHT AVERAGE – 2.24%	0.55%

	2022/23 Actual %	2022/23 Revised %	2021/22 Actual %
Investment rate achieved	Achieved 2.10%	SONIA OVERNIGHT AVERAGE - 2.24%	Achieved 0.19%

	2022/23 Actual %	2022/23 Revised %	2021/22 Actual %
Average rate of Interest Paid on Council Debt (%)	3.02%	3.25%	3.02%

	2022/23 Actual %	2022/23 Target %	2021/22 Actual %
Interest on Debt as a % of Gross Revenue Expenditure	3.3%	4.3%	3.8%
General Fund	1.6%	2.4%	2.0%
HRA	8.5%	7.6%	7.6%

	2022/23 Actual (ave) %	2022/23 Target %	2021/22 Actual (ave) %
Upper limits on fixed interest rate investments	100%	100%	53%

	2022/23 Actual %	2022/23 Target %	2021/22 Actual %
Upper limits on fixed interest rate debt	100%	100%	100%

	2022/23 Actual (ave) %	2022/23 Target %	2021/22 Actual (ave) %
Upper limits on variable interest rate investments	49%	75%	47%

	2022/23 Actual %	2022/23 Target %	2021/22 Actual %
Upper limits on variable interest rate debt	0%	40%	0%