Annual Treasury Management Review
2022/23

North Herts Council
April 2023

Contents

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Purpose

This 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).

During 2022/23 the minimum reporting requirements were that the full Council should receive the following reports:

- an annual treasury strategy in advance of the year (Council 11/02/2022)
- a mid-year, (minimum), treasury update report (Council 13/12/2022)
- an annual review following the end of the year describing the activity compared to the strategy, (this report)

In addition, Cabinet and the Finance, Audit and Risk (FAR) Committee have received quarterly treasury management update reports.

The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This report is, therefore, 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.

This Council confirms that it has complied with the requirement under the Code to give prior scrutiny to all of the above treasury management reports by the Finance, Audit and Risk (FAR) Committee before they were reported to Cabinet / Full Council. Members are provided with an annual training session on Local Government finance, which takes place in June each year. All members are invited, with a focus on new members attending. Members of Finance, Audit and Risk Committee are now provided with a short training session before each meeting. The content of these sessions is guided by members needs, and treasury management will be considered as a topic for 2023/24.

Executive Summary

During 2022/23, the Council complied with its legislative and regulatory requirements. The key actual prudential and treasury indicators detailing the impact of capital expenditure activities during the year, with comparators, are as follows:

Prudential and treasury indicators	31.3.22 Actual £000	2022/23 Original Budget £000	31.3.23 Actual £000
Capital expenditure	1.434	7.546	6.923
Capital Financing Requirement:	-4.446	-3.183	-2.719
Gross borrowing	0.387	0.367	0.367
External debt	0.387	0.367	0.367
Investments	57.500	47.280	50.500
Net borrowing	-57.133	-46.913	-50.133

Other prudential and treasury indicators are to be found in the main body of this report. 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.

Introduction and Background

This report summarises the following:-

- Capital activity during the year;
- Impact of this activity on the Council's underlying indebtedness, (the Capital Financing Requirement);
- The actual prudential and treasury indicators;
- Overall treasury position identifying how the Council has borrowed in relation to this indebtedness, and the impact on investment balances;
- Summary of interest rate movements in the year;
- Detailed debt activity; and
- Detailed investment activity.

1. The Council's Capital Expenditure and Financing

The Council undertakes capital expenditure on long-term assets. These activities may either 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.

The actual capital expenditure forms one of the required prudential indicators. The table below shows the actual capital expenditure and how this was financed.

£m General Fund	31.3.22 Actual	2022/23 Working Budget	31.3.23 Actual
Capital expenditure	**1.434**	**8.370**	**6.923**
Financed in year	0.787	6.570	5.192
Unfinanced capital expenditure	**0.647**	**1.800**	**1.731**

2. The Council's Overall Borrowing Need

The Council's underlying need to borrow for capital expenditure is termed the Capital Financing Requirement (CFR). This figure is a gauge of the Council's indebtedness. The CFR results from the capital activity of the Council and resources used to pay for the capital spend. It represents the 2022/23 unfinanced capital expenditure (see above table), and prior years' net or unfinanced capital expenditure which has not yet been paid for by revenue or other resources.

Part of the Council's treasury activities is to address the funding requirements for this borrowing need. Depending on the capital expenditure programme, the treasury service organises the Council's cash position to ensure that sufficient cash is available to meet the capital plans and cash flow requirements. This may be sourced through borrowing from external bodies, (such as the Government, through the Public Works Loan Board [PWLB], or the money markets), or utilising temporary cash resources within the Council.

The Council's 2022/23 MRP Policy, (as required by DLUHC Guidance), was approved as part of the Treasury Management Strategy Report for 2022/23 on 11/02/2022.

The Council's CFR for the year is shown below, and represents a key prudential indicator.

CFR (£m): General Fund	31.3.22 Actual £m	2022/23 Working Budget £m	31.3.23 Actual £m
Opening balance	-5.089	-4.446	-4.446
Add unfinanced capital expenditure (as above)	0.647	1.800	1.731
Less Finance Lease Repayments	0.004	0.004	0.004
Closing balance	-4.446	-2.650	-2.719

The negative closing balances mean that the Council does not have a need to borrow.

Borrowing activity is constrained by prudential indicators for gross borrowing and the CFR, and by the authorised limit.

Gross borrowing and the CFR - in order to ensure that borrowing levels are prudent over the medium term and only for a capital purpose, the Council should ensure that its gross external borrowing does not, except in the short term, exceed the total of the capital financing requirement in the preceding year (2022/23) plus the estimates of any additional capital financing requirement for the current (2023/24) and next two financial years. This essentially means that the Council is not borrowing to support revenue expenditure. This indicator allows the Council some flexibility to borrow in advance of its immediate capital needs. The table below highlights the Council's gross borrowing position against the CFR. The Council has complied with this prudential indicator as all borrowing is historic and it is not economical to repay it.

	31.3.22 Actual £m	2022/23 Working Budget £m	31.3.23 Actual £m
Gross borrowing position	0.387	0.367	0.367
CFR	-4.446	-2.650	-2.719

The authorised limit - the authorised limit is the "affordable borrowing limit" required by s3 of the Local Government Act 2003. Once this has been set, 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.

The operational boundary – the operational boundary is the expected borrowing position of the Council during the year. Periods where the actual position is either below or over the boundary are acceptable subject to the authorised limit not being breached.

Actual financing costs as a proportion of net revenue stream - 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.

	2022/23 £m
Authorised limit	7.1
Maximum gross borrowing position during the year	0.387
Operational boundary	2.1
Average gross borrowing position	0.378
Financing costs as a proportion of net revenue stream	2.51%

3. Treasury Position as at 31st March 2023

The Council's treasury management debt and investment position is organised by the treasury management service in order to ensure adequate liquidity for revenue and capital activities, security for investments and to manage risks within all treasury management activities. Procedures and controls to achieve these objectives are well established both through member reporting detailed in the summary, and through officer activity detailed in the Council's Treasury Management Practices. At the end of 2022/23 the Council's treasury position was as follows:

DEBT PORTFOLIO	31.3.22 Principal £m	Rate/ Return	31.3.23 Principal	Rate/ Return
Fixed rate funding:				
-PWLB	0.387	10.11%	0.367	10.28%
-Market	0		0	
Variable rate funding:				
-PWLB	0		0	
-Market	0		0	
Total debt	**0.387**	**10.11%**	**0.367**	**10.28%**
CFR	**-4.446**		**-2.719**	
Over / (under) borrowing	**4.833**		**3.086**	
Total investments	**57.5**	**0.33%**	**50.5**	**4.19%**
Net debt	**57.113**		**50.133**	

The maturity structure of the debt portfolio was as follows:

	31.3.22 Actual £'000	31.3.23 Actual £'000
Under 12 months	19	21
12 months and within 24 months	21	21
24 months and within 5 years	57	50
5 years and within 10 years	40	25
10 years and above	250	250

INVESTMENT PORTFOLIO	31.3.22 Actual £m	31.3.22 Actual %	31.3.23 Actual £m	31.3.23 Actual %
Treasury investments				
Banks	6.0	10	11.0	22
Building Societies - rated	4.0	7	8.0	16
Building Societies – unrated	1.5	3	0.0	0
Local authorities	25.0	43	29.0	57
DMADF (H M Treasury)	21.0	37	2.5	5
TOTAL TREASURY INVESTMENTS	57.5	100%	50.5	100%

The maturity structure of the investment portfolio was as follows:

	31.3.22 Actual £m	31.3.23 Actual £m
Investments Longer than 1 Year	0	2.0
Investments Up to1 Year	57.5	48.5

The decrease in cash balances as at the end of 2022/23 (compared with 2021/22) is partly due to the balances that the Council was holding at 31/03/22 in relation to the Council Tax Rebate Grant that was repaid in 22/23.

4. The Strategy for 2022/23

The strategy in 2022/23 was to continue lending to UK banks, building societies, money market funds and Local Authorities and allow investments with non-UK banks with a credit rating greater than AA- with a AAA Country rating. Only UK banks that met credit rating criteria ("BBB" or above for longer term deals, and F3 or above for short term deals) were on the Council's lending list. (These are Fitch definitions of ratings). Not all building societies are credit rated but this did not preclude them from the lending list as lending to a building society was dependant on their asset size. Where a society did have a rating, this was considered at the time of the deal taking into account the amount of investment and the length of the deal.

4.1 Investment strategy and control of interest rate risk

Investment returns picked up throughout the course of 2022/23 as central banks, including the Bank of England, realised that inflationary pressures were not transitory, and that tighter monetary policy was called for.

Starting April at 0.75%, Bank Rate moved up in stepped increases of either 0.25% or 0.5%, reaching 4.25% by the end of the financial year, with the potential for a further one or two increases in 2023/24.

The sea-change in investment rates meant local authorities were faced with the challenge of pro-active investment of surplus cash for the first time in over a decade, and this emphasised the need for a detailed working knowledge of cashflow projections so that the appropriate 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, became an on-going feature of the investment landscape.

With bond markets selling off, equity valuations struggling to make progress and, latterly, property funds enduring a wretched Q4 2022, the more traditional investment options, such as specified investments (simple to understand, and less than a year in duration) became more actively used.

Meantime, through the autumn, and then in March 2023, the Bank of England maintained various monetary policy easing measures as required to ensure specific markets, the banking system and the economy had appropriate levels of liquidity at times of stress.

Nonetheless, while the Council has taken a cautious approach to investing, it is also fully appreciative of changes to regulatory requirements for financial institutions in terms of additional capital and liquidity that came about in the aftermath of the Great Financial Crisis of 2008/9. These requirements have provided a far stronger basis for financial institutions, with annual stress tests by regulators evidencing how institutions are now far more able to cope with extreme stressed market and economic conditions.

4.2 Borrowing strategy and control of interest rate risk

The policy of avoiding new borrowing by running down spare cash balances which has served well over the last few years continued during 22/23.

5. Borrowing Outturn

Borrowing
No new borrowing was undertaken during the year

Borrowing in advance of need
The Council has not borrowed more than, or in advance of its needs, purely in order to profit from the investment of the extra sums borrowed.

Rescheduling

No rescheduling was done during the year as the average 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

Repayments

£20K of PWLB loans were repaid during the year, as they became due.

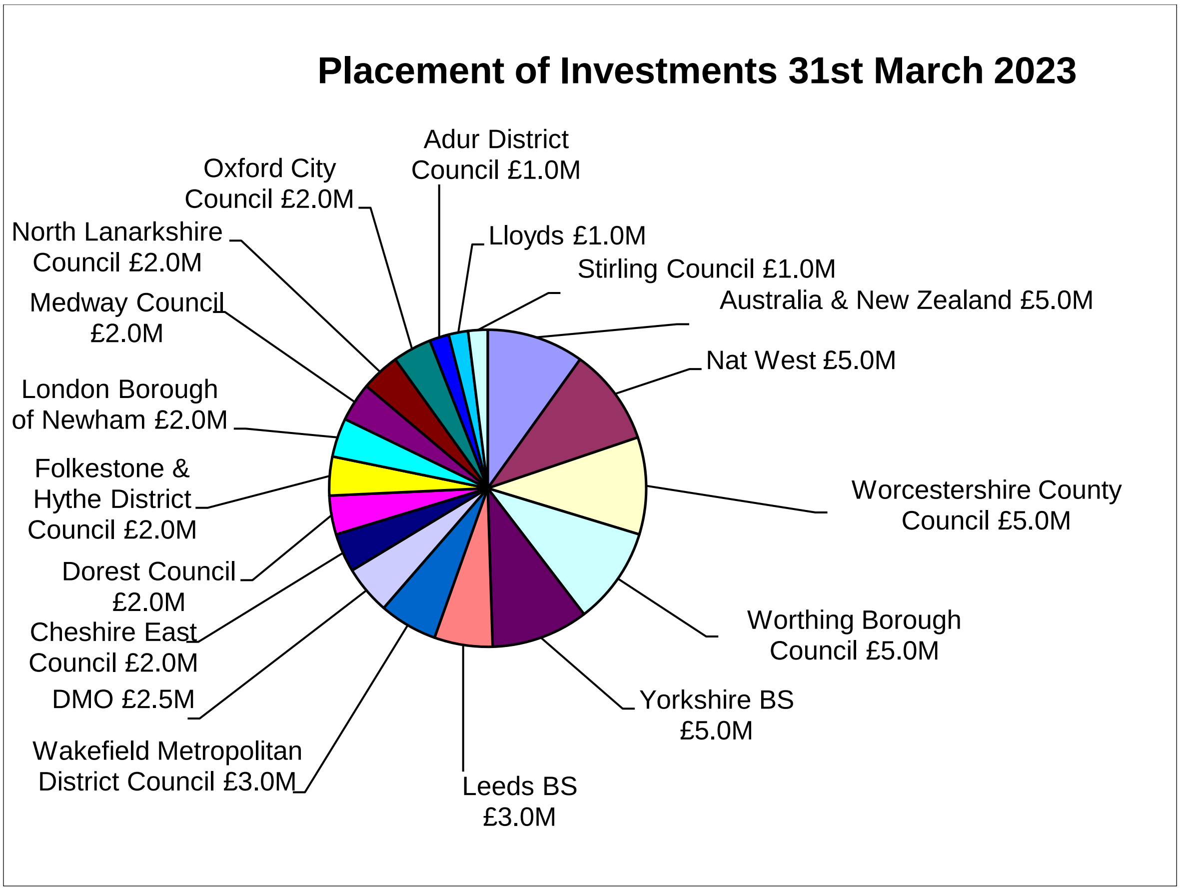
6. Investment Outturn

Investment Policy – the Council's investment policy is governed by DLUHC investment guidance, which has been implemented in the annual investment strategy approved by the Council on 11/02/22. This policy sets out the approach for choosing investment counterparties and is based on credit ratings provided by the Fitch credit rating agency for banks and asset size for building societies.

The investment activity during the year conformed to the approved strategy, and the Council had no liquidity difficulties.

Investments placed by Cash Managers – the Council used an external cash manager to invest some of its longer term cash balances, where the rate achieved (after fees) was better than could be obtained by the Council directly. At the start of the year, Tradition had £3.5m of outstanding investments. This arrangement came to an end during the year when the final two investments matured. These investments generated £9.0K of interest.

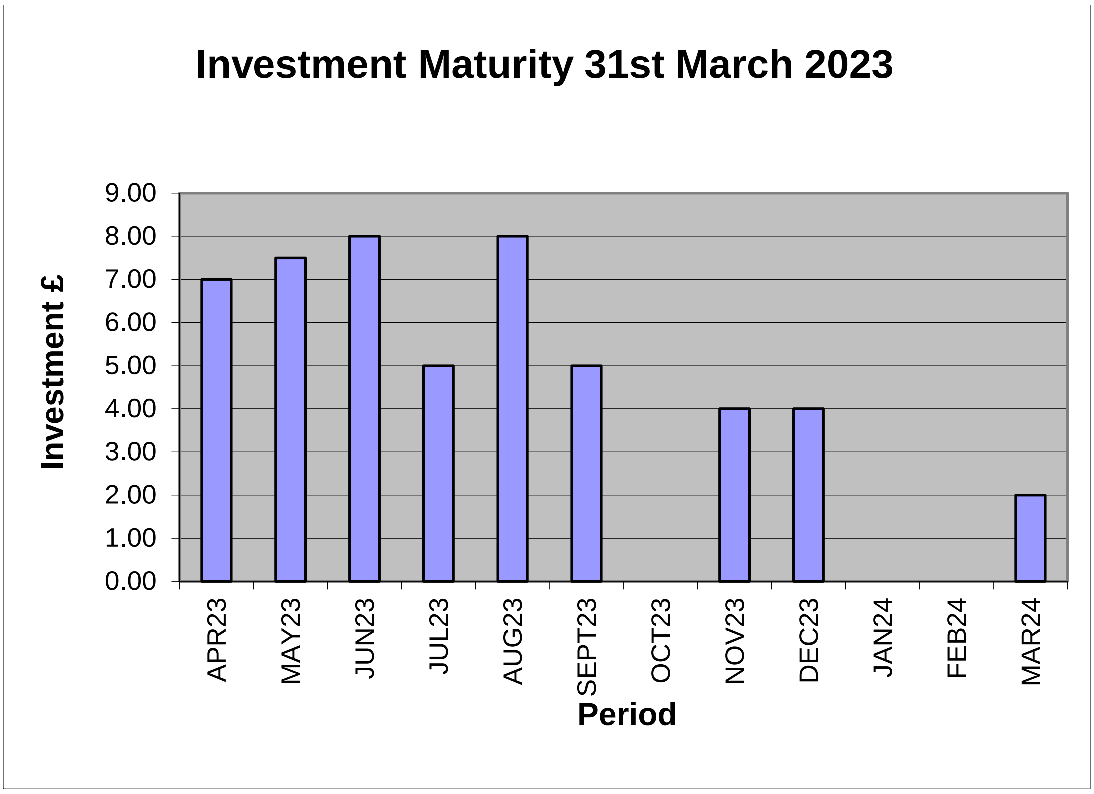
The pie chart below shows the spread of investment balances as at 31 March 2022. This is a snapshot in time that demonstrates the diversification of investments.



The average daily balance of investments was £60.0m with balances varying between £48.5m and £71.0m.

£1.31m of interest was generated from investments during the year. This is more than the estimated interest of £1.277m (as per Quarter 3 forecast).

The graph below shows the maturity profile of investments at 31st March 2023.



The level of risk of any investment will be affected by the riskiness of the institution where it is invested and the period that it is invested for. Where an institution has a credit rating this can be used to measure its riskiness. This can be combined with the period remaining on the investment to give a historic risk of default percentage measure. The table below shows the Historic Risk of Default for outstanding investments at 31 March. The most risky investment still has a risk of default of only around 0.044%. It should also be noted that in general the interest rate received is correlated to the risk, so the interest income received would be less if it took on less risk. All investments have been made in accordance with the Investment Strategy. The risk of default is also affected by the length of the investment.

Borrower	Interest Rate %	Principal	Days to Maturity from 31/03/22	Risk of Default %	Expected Credit Loss £
Yorkshire Building Society	3.88	2,000,000	3	0.000	7
Medway Council	3.9	2,000,000	3	0.000	0
Yorkshire Building Society	3.6	3,000,000	17	0.002	63
Wakefield Council	4.8	3,000,000	42	0.003	0
Australia and New Zealand Bank	4.14	2,000,000	45	0.006	111
DMO	3.975	2,500,000	48	0.003	0
Adur District Council	4.25	1,000,000	81	0.005	0
Worcestershire County Council	3.85	5,000,000	83	0.005	0
Cheshire East Council	4.55	2,000,000	88	0.005	0
Nat West	4.15	2,000,000	111	0.014	275

Stirling Council	3.95	1,000,000	122	0.008	0
North Lanarkshire Council	3.99	2,000,000	122	0.008	0
Leeds Building Society	4.00	3,000,000	129	0.016	479
Worthing Borough Council	3.9	5,000,000	139	0.009	0
Dorset Council	4.5	2,000,000	159	0.010	0
London Borough of Newham	4.4	2,000,000	168	0.010	0
Lloyds Bank	4.28	1,000,000	168	0.021	208
Nat West	4.4	2,000,000	234	0.029	579
Folkestone & Hythe District Council	4.4	2,000,000	244	0.015	0
Nat West	4.2	1,000,000	259	0.032	320
Australia and New Zealand Bank	4.58	1000,000	262	0.032	324
Oxford City Council	4.65	2,000,000	262	0.016	0
Australia and New Zealand Bank	4.4	2,000,000	355	0.044	878

Under IFRS 9, the Code does not recognise a loss allowance where the counterparty is central government or a local authority since relevant statutory provisions prevent default.