Title: Annual Treasury Management Report 2021/22

Lead Officer: Richard Wilson, Principal Accountant (Capital & Treasury) 01926 456801

Portfolio Holder: Councillor Richard Hales

Wards of the District directly affected: All

Summary

The Council is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 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).

This report covers the Council's performance for the whole of 2021/22 and is attached as Appendix A.

Recommendation(s)

(1) That the Members of the Overview and Scrutiny Committee note the contents of this report in respect of the Council's Treasury Management activities during 2021/22.

(2) That the Overview & Scrutiny Committee recommend to Council that in future updates on Treasury Management should be considered by the Audit & Standards Committee and the Constitution and relevant Policies are updated to reflect this.

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1 Background/Information

1.1 The Treasury Management Strategy for 2021/22 and the Council's Treasury Management Practices, in accordance with the Code of Practice for Treasury Management, require that the Treasury Management function reports on its activities during the year by no later than 30 September in the year after that being reported on.

1.2 During 2021/22 the minimum reporting requirements were that the full Council should receive the following reports:

- an annual treasury strategy in advance of the year (Council 24/2/2021)
- a mid-year (minimum) treasury update report (Finance & Audit Scrutiny 03/11/2021)
- an annual review following the end of the year describing the activity compared to the strategy (this report)

1.3 In addition, this Council receives a half-yearly treasury management update reports for the second half of 2021/22, which accompanies this report.

1.4 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.

1.5 This Council is required to confirm that it has complied with the requirement under the Code to give prior scrutiny to all the above treasury management reports. In previous years this has been undertaken within the scrutiny function of Finance & Audit Scrutiny Committee. As that Committee has ceased to exist and the Council only has a Scrutiny Committee, it was considered by officers that the report for now should come to the Overview & Scrutiny Committee before they were reported to the full Council.

1.6 Officers have considered this and, on reflection, in future feel that this work is more closely aligned with the Audit & Standards Committee and therefore it is recommended that this should fall under the remit of the Audit & Standards Committee. Officers have undertaken comparison work with other councils and found that there is no unified approach across the sector. Grant Thornton tend to see treasury management reports being considered by an Audit Committee, with anything required then also going to Cabinet on the proposed approach (with referal to Council for certain decisions). This will not remove the ability for the Overview & Scrutiny Committee to consider any report regarding treasury management that is on the Cabinet agenda.

1.7 The report comments, where appropriate, on the Council's actual performance against what was forecast in the 2021/22 Treasury Management Strategy as well as, in certain instances, latest forecasts. The Council is also required to comment on its performance against its Annual Investment Strategy for the year.

1.8 The report consists of the following Appendices:

Appendix A - Annual Treasury Management Report 2021/22
Appendix B – Glossary of Terms.

2 Alternative Options available to Council

2.1 As explained in paragraph 1.1, the Code of Practice mandates that Annual Treasury Management Performance must be reported by 30 September after that financial year has closed, demonstrating compliance with the Prudential Code, or explaining any divergence for the approved Treasury Management Strategy and Prudential Indicators..

2.2 The Council had announced that it will divest from fossil fuels at the earliest opportunity; no later than the end of 2025, and ideally by the end of 2022. The Council was able to take advantage of market movements to divest in September 2021, as outlined in this report.

2.3 The Council may consider varying its investment vehicles or counterparty limits; however this would alter the potential credit and liquidity risks.

3 Consultation and Member's comments

3.1 This is a report on fact and subject to following reporting guidelines.

4 Implications of the proposal

4.1 Legal/Human Rights Implications

4.1.1 None directly arising.

4.2 Financial

4.2.1 The Treasury Management Strategy has a significant impact on the Council's budget through its objective of maximising investment income and minimising interest payable whilst ensuring the security and liquidity of financial resources.

4.2.2 The Council relies on interest received to fund the services it provides. The gross interest received in 2021/22, including non-Treasury Management interest, was £537,600. The interest paid to the HRA on its balances was £15,100, with a net of £522,500 retained by the General Fund. The table below compares this with budgeted figures:

	Original 2021/22 Budget £'000	Latest 2021/22 Budget £'000	2021/22 Actual £'000
Gross investment interest	649	544	538
less HRA allocation	-123	-115	-15
Net interest to General Fund	**526**	**430**	**523**

4.2.3 The main reason for the net interest to the General Fund increasing against the latest budget is that the HRA has been reliant on internal borrowing from the General Fund, in lieu of taking PWLB loans, and so is receiving the returns on the HRA reserves and balances reduced by the internal borrowing.

4.2.4 Borrowing costs to the HRA from the 2012 Self-Financing of £4.766m are unchanged from previous financial years and are charged directly to the HRA. The expected borrowing for new HRA capital expenditure had not been drawn down as at 31 March 2022, it being better value during the year to utilise internal borrowing rather than borrow long-term loans.

4.2.5 The £12 million PWLB loan taken during 2019/20 is charged to the General Fund and the full year interest costs are £220,800. A further £60 million of General Fund loans were borrowed from the PWLB by 31 March 2022, to finance the loan to the Crewe Lane housing joint venture, with £50 million having been advanced at 31 March 2022, the final £10 million being advanced on 1 April 2022. The interest paid on the PWLB loans for the joint venture (JV) during 2021/22 was £342,800 and the interest received from the JV was £1.190m, which has been excluded from the table above to aid prior year comparisons.

4.3 Council Plan

4.3.1. External impacts

The Treasury Management function is an underpinning activity that enables the Council to meet its vision by maximising investment returns and minimising borrowing costs, while managing the risk to the Council's funds and maintaining liquidity, so that the Council can meet its financial obligations through a well-managed cash flow. This protects services and benefits the Council's customers and other stakeholders.

People - Health, Homes, Communities – Treasury Management indirectly enables financial resources to be ready for the Council to meet the following intended outcomes: Improved health for all; Housing needs for all met; Impressive cultural and sports activities; Cohesive and active communities.

Services - Green, Clean, Safe – Treasury Management is a support function towards to overall achievement of the Council's intended outcomes: Becoming a net-zero carbon organisation by 2025; Total carbon emissions within Warwick District are as close to zero as possible by 2030; Area has well looked after public spaces; All communities have access to decent open space; Improved air quality; Low levels of crime and ASB. In terms of becoming a net-zero carbon organisation, the Council aims to disinvest the equity funds from any carbon-related organisations at the earliest opportunity – and no later than the end of 2025 - that the current economic conditions allow, and seek new 'green' investment opportunities that meet the overarching Treasury Management framework that the Council must operate within.

Money - Infrastructure, Enterprise, Employment – Treasury Management is a fundamental part of effective money management and indirectly aids the following intended outcomes: Dynamic and diverse local economy; Vibrant town centres; Improved performance/productivity of local economy; Increased employment and income levels.

4.3.2. **Internal impacts of the proposals**

The Treasury Management function enables the Council to meet its vision, primarily through having suitably qualified and experienced staff deliver the service in accordance with the Council's Treasury Management Practices and the national framework that local government operates.

People - Effective Staff –All staff are properly trained; All staff have the appropriate tools; All staff are engaged, empowered and supported and that the right people are in the right job with the right skills and right behaviours. Staff have access to the Council's treasury management advisers, the Link Group, who provide additional support and training to staff and members.

Services - Maintain or Improve Services – Treasury Management indirectly helps with the following intended outcomes: Focusing on our customers' needs; Continuously improve our processes and Increase the digital provision of services.

Money - Firm Financial Footing over the Longer Term - Treasury Management is a fundamental part of effective both short and long term money management and indirectly aids the following intended outcomes: Better return/use of our assets; Full Cost accounting; Continued cost management; Maximise income earning opportunities and Seek best value for money.

4.4 **Environmental/Climate Change Implications**

4.4.1 None directly attributable to the Treasury Mananagement activities of the Council since the Council divested in equity funds which had investments in fossil fuel companies.

4.5 **Analysis of the effects on Equality**

4.5.1 None directly attributable to the Treasury Mananagement activities, which is a support to all services across the Council but operates under tightly defined financial rules.

4.6 **Data Protection**

4.6.1 Treasury Management activities are between financial institutions, under the regulations of the financial markets.

4.7 **Health and Wellbeing**

4.7.1 Not applicable.

5 Risk Assessment

5.1 The Council maintained a cautious approach, as advocated by the regulatory framework, given experience from the 2008 financial crisis and the COVID-19 pandemic, with investments subject to low counterparty risk considerations, with relatively low returns compared to borrowing rates.

5.2 Investing the Council's funds unavoidably creates some risk, as would simply leaving the funds in a bank account. Treasury Management aims to manages risk through the application of the SLY principle: Security(S) ranks uppermost followed by Liquidity (L) and finally Yield(Y).

5.3 In addition to credit ratings themselves, the Council has regard to any ratings watch notices issued by the rating agencies, as well as articles in the Financial press, market data and intelligence from benchmarking groups. It will also use Credit Default Swap (CDS) data as supplied by its treasury advisers (Link Asset Services) to determine the suitability of investing with counterparties.

5.4 Although not used in 2021/22, or the previous financial year, Corporate Bonds and Floating Rate Notes (FRNs) introduce counterparty credit risk into the portfolio by virtue of the fact that it is possible that the institution invested in could become bankrupt, leading to the loss of all or part of the Council's investment. This is mitigated by only investing in Corporate Bonds or FRNs with a strong Fitch credit rating, in this case 'A', and issued as Senior Unsecured debt which ranks above all other debt in the case of a bankruptcy.

5.5 Covered Bonds also reduce risk since the bond is 'backed' by high quality assets such as prime residential mortgages, ensuring that if the bond issuer defaults there are sufficient assets that can be realised in order to repay the bond in full. Again, these were not used during 2021/22.

5.6 While Corporate Equity Funds can help to ensure capital security in real (as opposed to nominal) terms, they can risk capital loss due to market price fluctuations. This was evidenced with extreme movements worldwide in March 2020 as the extent and far-reaching consequences of COVID-19 saw investors 'take flight'. However, 2020/21 and the first half of 2021/22 experienced a significant recovery for both equity funds, providing an opportunity to divest in September 2021 an make a realised capital gain of £406,000.

6 Conclusion/Reasons for the Recommendation

6.1 The 2021/22 Annual Treasury Management Report is contained at Appendix A and demonstrates that the Council's Treasury Management activity was compliant with Prudential Indicators and the requirements of the Prudential Code.

Background papers:

- CIPFA Treasury Management Code of Practice

- CIPFA Prudential Code for Capital Finance in Local Authorities

Supporting documents:

- Annual Treasury Management Strategy 2021/22 (Council 24/2/2021)

Appendix A

2021/22 Annual Treasury Management Report

1. Investment strategy and control of interest rate risk

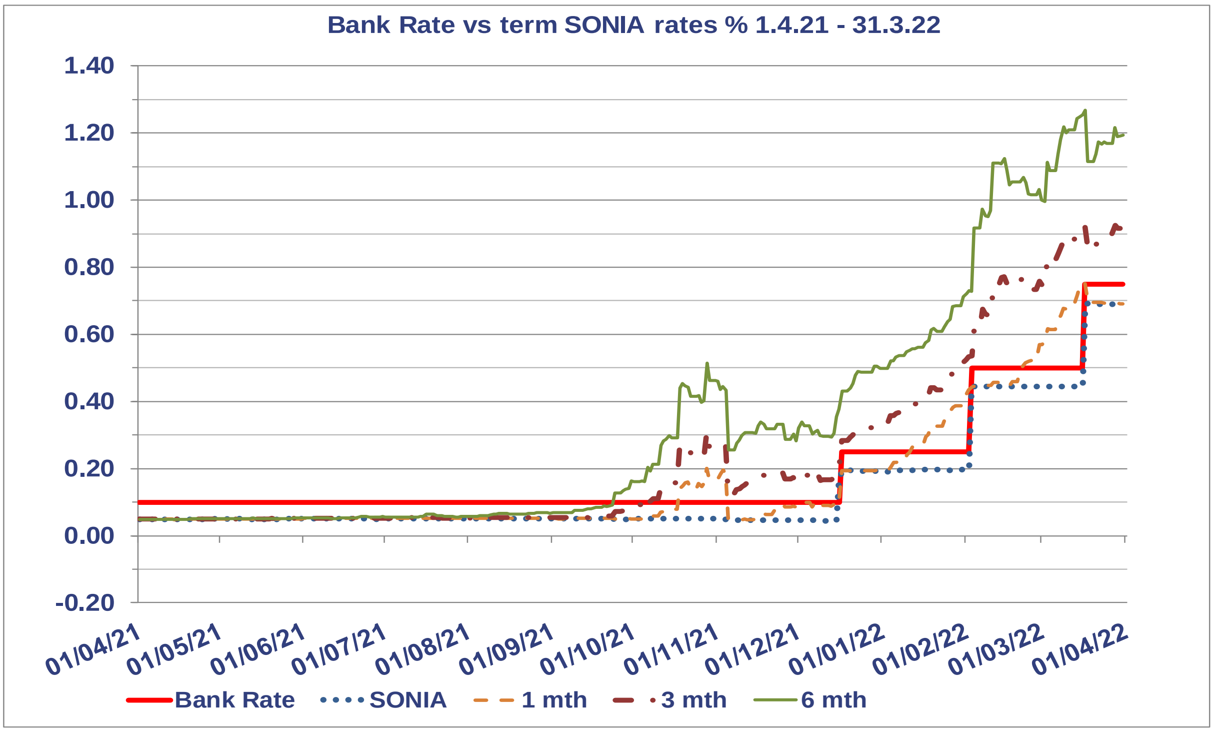
1.1. Investment returns remained close to zero for much of 2021/22. Most local authority lending managed to avoid negative rates and one feature of the year was the continued growth of inter local authority lending. The expectation for interest rates within the treasury management strategy for 2021/22 was that Bank Rate would remain at 0.1% until it became clear to the Bank of England that the emergency level of rates introduced at the start of the Covid-19 pandemic were no longer necessitated.

1.2. The Bank of England and the Government also maintained various monetary and fiscal measures, supplying the banking system and the economy with massive amounts of cheap credit so that banks could help cash-starved businesses to survive the various lockdowns/negative impact on their cashflow. The Government also supplied huge amounts of finance to local authorities to pass on to businesses. This meant that for most of the year there was much more liquidity in financial markets than there was demand to borrow, with the consequent effect that investment earnings rates remained low until towards the turn of the year when inflation concerns indicated central banks, not just the Bank of England, would need to lift interest rates to combat the second-round effects of growing levels of inflation (CPI was 6.2% in February).

1.3. 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 financial crisis. 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.

1.4. Investment balances have been kept to a minimum through the agreed strategy of using reserves and balances to support internal borrowing, rather than borrowing externally from the financial markets, other than the 'back-to-back' loans for the housing joint venture. External borrowing would have incurred an additional cost, due to the differential between borrowing and investment rates as illustrated in the charts shown above and below. Such an approach has also provided benefits in terms of reducing counterparty risk exposure, by having fewer investments placed in the financial markets.

1.5. The tables below shows rate movements during the year, incorporating the new SONIA rather than the previous LIBID date (please see the Glossary):



	Bank Rate	SONIA	1 mth	3 mth	6 mth
High	0.75	0.69	0.75	0.93	1.27
High Date	17/03/2022	18/03/2022	16/03/2022	28/03/2022	17/03/2022
Low	0.10	0.05	0.05	0.05	0.05
Low Date	01/04/2021	15/12/2021	10/11/2021	14/04/2021	09/04/2021
Average	0.19	0.14	0.17	0.24	0.34
Spread	0.65	0.65	0.71	0.88	1.22

2. Borrowing strategy and control of interest rate risk

2.1. During the last financial year the Council maintained an under-borrowed position. This meant that the capital borrowing need (the Capital Financing Requirement) was not fully funded with loan debt, as cash supporting the Council's reserves, balances and cash flow was used as an interim measure. This strategy was prudent as investment returns were low and minimising counterparty risk on placing investments also needed to be considered.

2.2. A cost of carry remained during the year on any new long-term borrowing that was not immediately used to finance capital expenditure, as it would have caused a temporary increase in cash balances; this would have incurred a revenue cost – the difference between (higher) borrowing costs and (lower) investment returns. This must be balanced against potential interest rate increases, which could cause higher interest costs once long-term loans are taken.

2.3. As the PWLB loans for the housing joint venture were matched 'back to back' with capital loans the preceding paragraph does not apply to these loans, and the Council has made the loans at market rates (to comply with European competition laws) there should be no 'cost of carry' to the Council.

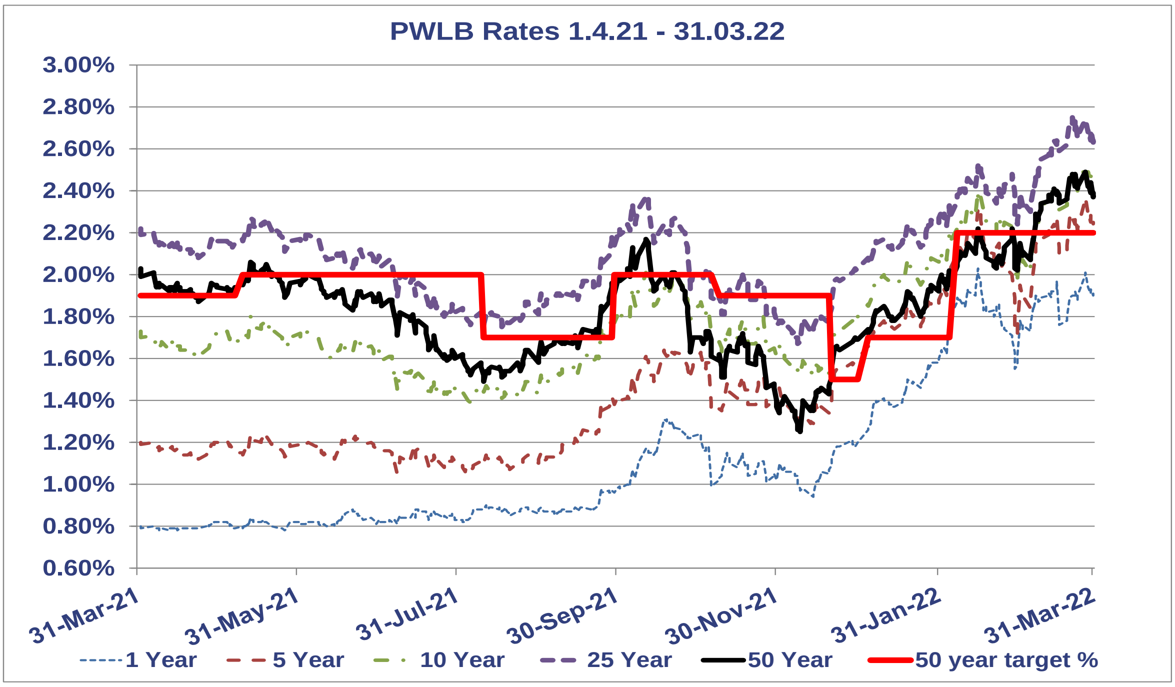
2.4. The policy of avoiding new borrowing by running down spare cash balances, has served well over the last few years. However, this was kept under review to avoid incurring higher borrowing costs in the future when this authority may not be able to avoid new borrowing to finance capital expenditure and/or the refinancing of maturing debt.

2.5. Against this background and the risks within the economic forecast, caution was adopted with the Treasury operations. The Treasury team monitored interest rates in financial markets and adopted a pragmatic strategy based on the following principle to manage interest rate risks:

- During 2021/22, until the Russian invasion of Ukraine, it had been felt that there was a limited risk of a significant change in long and short term rates. Therefore, it was decided to postpone the draw down of further long-term General Fund or HRA, to minimise these additional debt holding costs.

2.6. Interest rate forecasts expected only gradual rises in medium and longer term fixed borrowing rates during 2021/22 and the two subsequent financial years. Internal, variable, or short-term rates, were expected to be the cheaper form of borrowing over the period, until well in to the second half of 2021/22.

Link Group Interest Rate View		10.8.21									
	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
BANK RATE	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.25	0.25	0.25	0.50
3 month ave earnings	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.30	0.30	0.30	0.50
6 month ave earnings	0.10	0.10	0.10	0.10	0.10	0.10	0.20	0.30	0.40	0.50	0.50
12 month ave earnings	0.20	0.20	0.20	0.20	0.20	0.30	0.30	0.40	0.50	0.60	0.70
5 yr PWLB	1.20	1.20	1.20	1.30	1.30	1.30	1.40	1.40	1.40	1.50	1.50
10 yr PWLB	1.60	1.60	1.70	1.70	1.80	1.80	1.90	1.90	1.90	2.00	2.00
25 yr PWLB	1.90	2.00	2.10	2.20	2.30	2.30	2.30	2.40	2.40	2.40	2.50
50 yr PWLB	1.70	1.80	1.90	2.00	2.10	2.10	2.10	2.20	2.20	2.20	2.30



2.7. PWLB rates are based on, and are determined by, gilt (UK Government bonds) yields through H.M.Treasury determining a specified margin to add to gilt yields. The main influences on gilt yields are Bank Rate, inflation expectations and movements in US treasury yields. Inflation targeting by the major central banks has been successful over the last 30 years in lowering inflation and the real equilibrium rate for central rates has fallen considerably due to the high level of borrowing by consumers: this means that central banks do not need to raise rates as much now to have a major impact on consumer spending, inflation, etc. This has pulled down the overall level of interest rates and bond yields in financial markets over the last 30 years. We have seen, over the last two years, many bond yields up to 10 years in the Eurozone turn negative on expectations that the EU would struggle to get growth rates and inflation up from low levels. In addition, there has, at times, been an inversion of bond yields in the US whereby 10 year yields have fallen below shorter term yields. In the past, this has been a precursor of a recession. Recently, yields have risen since the turn of the year on the back of global inflation concerns.

2.8. Gilt yields fell sharply from the spring of 2021 through to September and then spiked back up before falling again through December. However, by January sentiment had well and truly changed, as markets became focussed on the embedded nature of inflation, spurred on by a broader opening of economies post the pandemic, and rising commodity and food prices resulting from the Russian invasion of Ukraine.

2.9. At the close of the day on 31 March 2022, all gilt yields from 1 to 5 years were between 1.11% – 1.45% while the 10-year and 25-year yields were at 1.63% and 1.84%.

2.10. Regarding PWLB borrowing rates, the various margins attributed to their pricing are as follows:

- **PWLB Standard Rate:** gilt plus 100 basis points (G+100bps)
- **PWLB Certainty Rate:** gilt plus 80 basis points (G+80bps)
- **PWLB HRA Standard Rate:** gilt plus 100 basis points (G+100bps)
- **PWLB HRA Certainty Rate:** gilt plus 80bps (G+80bps)
- **Local Infrastructure Rate:** gilt plus 60bps (G+60bps)

2.11. There is likely to be a further rise in short dated gilt yields and PWLB rates over the next three years as Bank Rate is forecast to rise from 0.75% in March 2022 to 1.25% later this year, with upside risk likely if the economy proves resilient in the light of the cost-of-living squeeze. Medium to long dated yields are driven primarily by inflation concerns but the Bank of England is also embarking on a process of Quantitative Tightening when Bank Rate hits 1%, whereby the Bank’s £895bn stock of gilt and corporate bonds will be sold back into the market over several years. The impact this policy will have on the market pricing of gilts, while issuance is markedly increasing, was an unknown at the end of the financial year.

3. Borrowing Outturn

3.1. **Borrowing** – Due to the Crewe Lane housing joint venture, £60 million of new PWLB was undertaken in 2021/22

3.2. The total PWLB borrowing is shown in the table below, including the new loans. While there is no naturally maturing HRA debt until 2053, the £60 million of housing joint venture loans were for periods not exceeding 5.5 years.

PWLB Loan No.	Fund	Start Date	Interest Rate	Balance 31 Mar 2022	Maturity Date
500847	HRA	28 Mar 2012	3.52%	£5,000,000	28 Mar 2053
500840	HRA	28 Mar 2012	3.52%	£8,000,000	28 Mar 2053
500846	HRA	28 Mar 2012	3.51%	£5,000,000	28 Mar 2054
500843	HRA	28 Mar 2012	3.51%	£8,000,000	28 Mar 2054
500835	HRA	28 Mar 2012	3.51%	£5,000,000	28 Mar 2055
500844	HRA	28 Mar 2012	3.51%	£8,000,000	28 Mar 2055
500852	HRA	28 Mar 2012	3.51%	£5,000,000	28 Mar 2056
500839	HRA	28 Mar 2012	3.51%	£8,000,000	28 Mar 2056
500854	HRA	28 Mar 2012	3.50%	£5,000,000	28 Mar 2057
500845	HRA	28 Mar 2012	3.50%	£8,000,000	28 Mar 2057
500837	HRA	28 Mar 2012	3.50%	£5,000,000	28 Mar 2058
500838	HRA	28 Mar 2012	3.50%	£8,000,000	28 Mar 2058
500850	HRA	28 Mar 2012	3.50%	£5,000,000	28 Mar 2059
500853	HRA	28 Mar 2012	3.50%	£8,000,000	28 Mar 2059
500849	HRA	28 Mar 2012	3.49%	£5,000,000	28 Mar 2060
500851	HRA	28 Mar 2012	3.49%	£8,000,000	28 Mar 2060
500848	HRA	28 Mar 2012	3.49%	£5,000,000	28 Mar 2061
500841	HRA	28 Mar 2012	3.49%	£8,000,000	28 Mar 2061
500836	HRA	28 Mar 2012	3.48%	£8,000,000	28 Mar 2062
500842	HRA	28 Mar 2012	3.48%	£11,157,000	28 Mar 2062
113015	GF	16 Sep 2019	1.84%	£12,000,000	28 Aug 2059
385189	GF	05 Aug 2021	1.10%	£15,000,000	04 Feb 2027
385191	GF	05 Aug 2021	1.06%	£15,000,000	04 Aug 2026
385193	GF	05 Aug 2021	1.03%	£10,000,000	04 Jan 2026
385195	GF	05 Aug 2021	0.96%	£10,000,000	04 Feb 2025
499722	GF	31 Mar 2022	2.20%	£5,000,000	31 Jul 2025
499725	GF	31 Mar 2022	2.02%	£5,000,000	30 Sep 2023
				£208,157,000	

3.3. **Rescheduling** - No rescheduling was done during the year as the average 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling economically unviable. This had been expected to remain the case for several years but recently rising interest rates mean that this will be kept under review.

3.4. **Summary of debt transactions** – The £208.157m debt portfolio had an average interest rate of 2.75%, which took advantage of historically low PWLB rates for the new debt taken during 2021/22. The HRA loans relating to the Self-Financing borrowing incurred in 2011/12 have a 3.50% average rate. The debt incurred £5.329m interest in cash terms during the year, of which £4.766m was charged to the HRA. The full year interest cost of the General Fund loans in 2022/23 will be £0.955m, an average interest rate of 1.33%.

3.5. **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.

4. Investment Outturn

4.1. **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 24 February 2021, following Executive on 11 February 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.).

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

4.3. **Resources** – the Council's cash balances comprise revenue and capital resources and cash flow monies. The Council's core cash resources comprised as below, showing an increase of £9.628 million (11.7%):

Balance Sheet Resources	31/3/21 £'000	31/3/22 £'000	Movement £'000
Balances (GF, Collection Fund)	-5,250	2,342	7,592
Balances (HRA)	7,507	7,701	194
Earmarked reserves / other balances	67,309	69,999	2,690
Provisions	5,656	4,235	-1,421
Capital Receipts Reserve	7,257	7,830	573
Total	**82,479**	**92,107**	**9,628**

4.4. **Investments held by the Council**

- The Council maintained an average balance of £73.7m of internally managed funds.
- The internally managed funds earned an average rate of return of 0.71%.
- The comparable performance indicator is the average 7-day and up to 3-months LIBID rate, which was 0.07%; the equivalent SONIA rate was 0.09% from January 2022.
- This compares with a latest budget assumption of £78.8m investment balances earning an average rate of 0.55%.
- Investment income excluding housing joint venture interest was £522,500, compared to a latest budget of £429,700.
- During 2021/22 the Council made investments of £558.484m and had repayments of £537.379m, a net increase of £21.104m, partly due to a £10m PWLB loan being held overnight on 31 March 2022 before being lent to the housing joint venture on 1 April 2022 (see also paragraph 8.4).

4.5. **Investments held by fund managers**

Until September 2021 the Council used two external fund managers to invest part of its cash balances. The performance of the managers (capital movement and dividend) against the benchmark FTSE All-Share return was:

Fund Manager	Investment held (nominal) £'000	Return to divest	Benchmark to divest
Columbia Threadneedle	3,000	9.2%	4.6%
Royal London	3,000	5.9%	4.6%
Total	**6,000**	**7.6%**	**4.6%**

4.6. Following the large capital losses incurred during 2019/20 position, and the reversals in 2020/21 of unrealised capital gains of £1.3m, the stock market made suffient improvement during the first half of the year to be able to divest of these equity funds (with their fossil fuel exposure) and realise an actual net capital gain of £0.406m, as shown below:

Fund Manager	Balance at 31/3/21 £'000	Dividend 21/22 £'000	Gain £'000	Balance at 31/3/22 £'000
Columbia Threadneedle	3,357	85	252	-
Royal London	3,284	58	154	-
Total	**6,641**	**143**	**406**	**-**

4.7. The Council is now fully divested of corporate equity funds. Given the amount of planned borrowing required to support the capital programme, it is not expected that the Council will be looking to invest in other equity funds in the medium term.

5. Other Issues

5.1. **Non-treasury management investments**. These predominantly include long-term debtors, where the borrower repays interest in addition to the principal lent to them. All interest rates are above "soft loan" rates (defined as preferential terms below normal 'market' rates). During 2021/22 the Council made new long-term loans for capital purposes of £100,000. Details of these loans and the due diligence taken is outlined in the Statement of Accounts 2021/22; none have required impairment under the IFRS 9 ECL model. The purpose of these loans is to stimulate economic development in the District rather than an overriding purpose of income generation, which is a minor consideration with these loans.

6. Capital expenditure and financing

6.1. 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.

6.2. The actual capital expenditure forms one of the required prudential indicators. The table below shows the actual capital expenditure of £99.181m and how this was financed, with a total of £74.404m being unfunded, i.e. subject to borrowing.

Capital expenditure	2020/21 Actual £'000	2021/22 Budget £'000	2021/22 Actual £'000
General Fund	11,275	17,515	12,985
HRA	33,135	59,533	36,096
Non-financial investments (long-term loans to third parties)*	350	100	50,100
Total (A)	**44,760**	**77,148**	**99,181**

* The Council has not made any 'commercial activities' where yield is the primary purpose. These loans are primarily for housing purposes.

Financing of capital expenditure	2020/21 Actual £'000	2021/22 Budget £'000	2021/22 Actual £'000
Capital receipts	815	1,761	2,960
Capital grants and contributions	5,215	20,963	9,814
Reserves	9,528	15,565	11,188
Revenue contributions	422	782	815
Subtotal (B)	**15,980**	**39,070**	**24,777**
Net borrowing need for the year (A – B)	**28,780**	**38,078**	**74,404**

7. Treasury limits and prudential indicators

7.1. The Prudential Capital Finance system, introduced in 2004, is regulated by a number of 'Prudential Indicators', a number of which are relevant for treasury management purposes and are included in the Annual Strategy Report. The table below shows the 2021/22 outturn against the budget and previous year's budget:

Prudential Indicators (1)	2020/21 Actual £'000	2021/22 Budget £'000	2021/22 Actual £'000
Authorised Limit for External Debt			
Borrowing	283,907	308,515	308,515
Other Long term Liabilities	1,012	1,000	1,000
Total	**284,919**	**309,515**	**309,515**
Operational Boundary for External Debt			
Borrowing	261,907	286,515	286,515
Other Long term Liabilities	1,012	1,000	1,000
Total	**262,919**	**287,515**	**287,515**
Actual External Debt at Year End			
Long Term Borrowing	148,157	263,157	208,157
Long Term Liabilities	12	1,000	0
Total	**148,169**	**264,157**	**208,157**

7.2. Due to the delay in some capital expenditure and the deferral of existing borrowing requirements, actual external debt did not increase during the year and did not exceed either the Authorised Limit or the Operational Boundary.

Prudential Indicators (2)	**2020/21 Actual £'000**	**2021/22 Budget £'000**	**2021/22 Actual £'000**
Actual Capital Expenditure for Year			
General Fund	8,201	17,615	63,085
Housing Revenue Account	20,183	59,533	36,096
Overall	**28,384**	**77,148**	**99,181**
Capital Financing Requirement			
General Fund	23,836	78,190	80,229
Housing Revenue Account	161,160	194,539	178,926
Total CFR	**184,996**	**272,728**	**259,155**
Gross borrowing position	148,169	264,157	208,157
Under (-) / over funding of CFR	-36,827	-8,571	-50,998

7.3. The under funding of £50.998m represents borrowing for capital expenditure already incurred that has not yet been taken, relying on 'internal borrowing'.

Prudential Indicators (3)	**2020/21 Actual %**	**2021/22 Budget %**	**2021/22 Actual %**
Financing Costs as a % of Net Revenue Stream			
General Fund	-0.31%	3.06%	-10.80%
Housing Revenue Account	39.01%	44.63%	*41.57%*
Overall	**17.53%**	**28.82%**	***25.49%***

7.4. The General Fund borrowed for the housing joint venture (JV), albeit at low interest rates, but the income from the JV have reduced net financing costs. No new HRA borrowing took place in the year, resulting in the actual financing costs being lower than budgeted.

7.5. The indicators were complied with, as the external borrowing outstanding at the year-end was the £136.157m PWLB debt in respect of the 2012 HRA Self Financing, £12m General Fund PWLB debt from 2019 for expenditure on leisure centres and the new £60m for the housing JV. This debt is all fixed rate, maturing as shown in paragraph 3.2 above, and within indicators shown above.

7.6. Below are the indicators relating to borrowing:

Upper limit to fixed interest rate and variable interest rate exposures

Exposure limits	**Strategy Report**	**Actual**
Upper Limit Fixed Rate	100%	100%
Upper Limit Variable Rate	30%	30%

Upper and lower limits respectively for the maturity structure of borrowing

Strategy 2021/22	Fixed		Variable	
Period	**Upper**	**Lower**	**Upper**	**Lower**
Under 12 months	20%	0%	100%	0%
12 months and within 24 months	20%	0%	100%	0%
24 months and within 5 years	20%	0%	100%	0%
5 years and within 10 years	20%	0%	100%	0%
10 years and above	100%	0%	n/a	n/a

7.7. The final indicator monitors the amount invested for periods longer than 365 days which in 2021/22 was set at 70% of the investment portfolio subject to a maximum of £30 million at any one time. During 2021/22 the Council entered into no investments for 365 days or over, assuring compliance with the indicator.

8. Annual investment strategy and investment performance

8.1. The Government guidance on local government investments requires the production of an Annual Investment Strategy that includes an outline of the investment vehicles that the Council would use and separates them off into Specified and Non-Specified investments. The 2021/22 Annual Investment Strategy was approved in February 2021, as part of the 2021/22 Annual Treasury Mnanagement Strategy report.

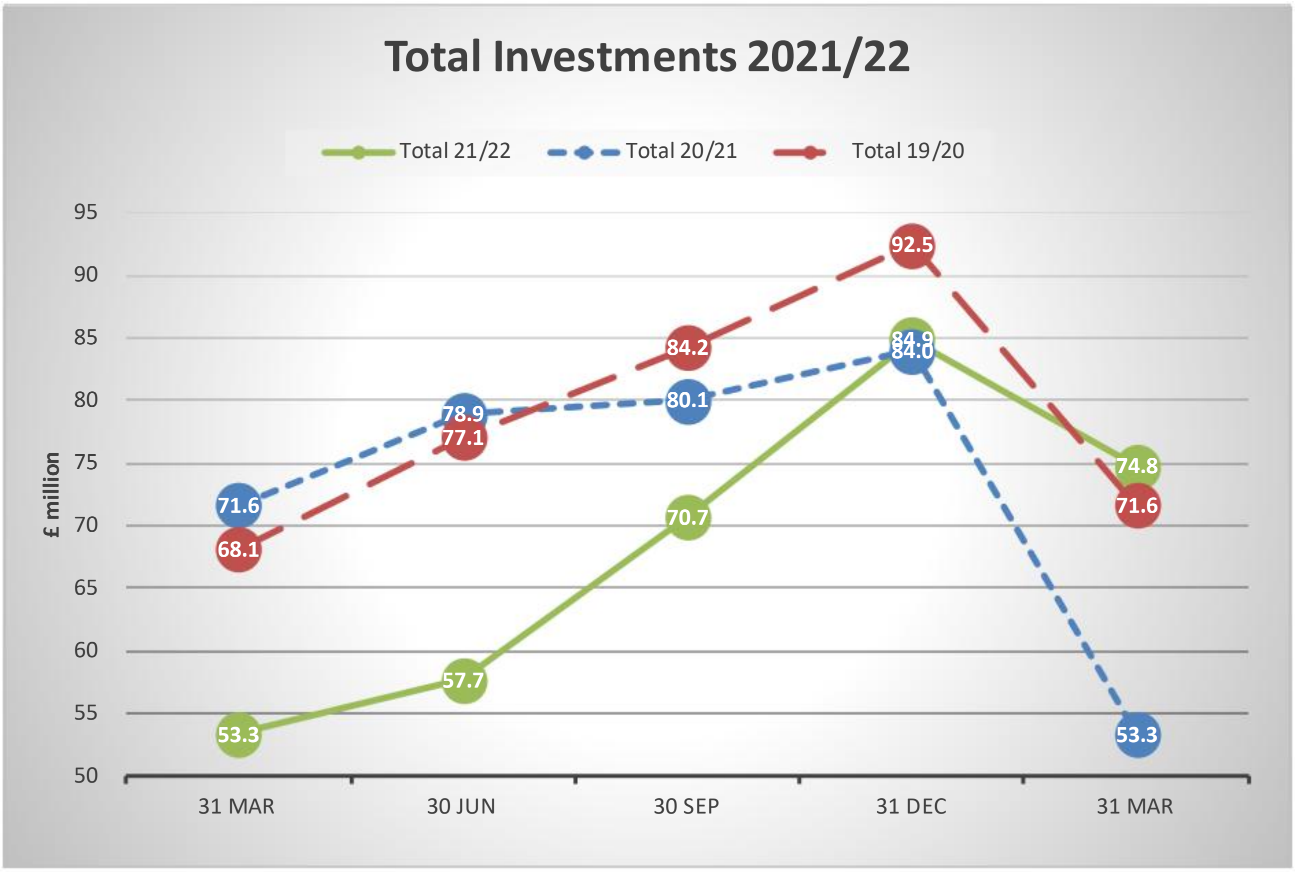
8.2. The in-house function has invested the Council's cash funds in fixed term money market deposits, equity funds and Money Market Funds. No Corporate Bonds or Certificates of Deposit (CD's) were used during 2021/22, and the equity funds were divested. The table below illustrates the performance for the year of the in-house function for each category invested in, the Benchmark utilising SONIA for the second half of the year, which has resulted in returns 'under-performing' more that would otherwise have been the case using LIBID. SONIA will replace LIBID in future treasury strategies.

Vehicle	Return (annualised) £'000	Benchmark (annualised) £'000	Perform -ance £'000
Money Markets	21.4	10.6	10.8
Money Market Funds	5.4	38.5	-33.0
Call Accounts	6.5	8.1	-1.6
Total	**33.4**	**57.2**	**-23.8**

8.3. For more detail breakdown please refer to the second half year Treasury Management report.

8.4. The graph below shows how the total of the Council's investments varies through the year according to its cash flows, comparing 2021/22 (green solid line) with the previous two years (2020/21 blue short dashes, 2019/20 red long dashes,). It shows that during the first half of the financial year (April to September) the Council's investments were below the previous two years, but then rose to match the 2020/21 levels, ending the year above the previous two years. In part this is due to the final £10m from the PWLB being borrowed on 31 March 2022 and being invested overnight, before being lent to the housing joint venture on 1 April 2022.

8.5. Due to the relatively high level of investments and the 'cost of carry' for taking new PWLB loans to finance capital expenditure, the Council has continued to utilise internal borrowing, as outlined earlier.



9. Equity Funds

9.1. The two equity funds commenced in April 2017, each with a £3m nominal balance. Paragraphs 4.5 to 4.7 show the returns for 2021/22 and details of the divestment for these funds. The half-year treasury management report to this meeting has more details on these funds.

Fund	**Value of Fund 31 Mar 22 £'000**	**Value of Fund 31 Mar 21 £'000**
Royal London UK Equity Fund	-	3,597.4
Columbia Threadneedle UK Equity Income Fund	-	3,657.3
Total Equity Funds	**-**	**7,254.6**

10. Performance measurement

10.1. In addition to the in-house local benchmarks referred to in this document the Council participates in the Link Group Investment Benchmarking Club. This benchmarks the investment returns and also the maturity and credit risk inherent in the portfolio. The Council is part of a local group which consists of district and county councils and this Council's performance over the past year is reflected in the tables below:

Table A - Weighted Average Rate of Return (WARoR)

10.2. Table A shows that the Council's average return was above Link Group model portfolio rate of return and below with the local group in the first three quarters, before being slightly above in the final quarter, based on the risk in its portfolio.

	WDC WARoR %	Local Group WARoR %	Link Asset Services Model WARoR %	Performance against Link Asset Services Model Band
June Quarter	0.12	0.27	0.09	Inline
September Quarter	0.14	0.22	0.08	Above
December Quarter	0.14	0.26	0.09	Above
March Quarter	0.50	0.47	0.42	Inline
Average for Year	**0.23**	**0.31**	**0.17**	

10.3. There was a slightly higher average credit risk taken in this Council's portfolio, as shown below.

Table B - Weighted Average Credit Risk

	WDC	Local Group
June Quarter	2.46	2.60
September Quarter	2.78	2.64
December Quarter	2.77	2.81
March Quarter	3.03	2.59
Average for Year	**2.76**	**2.66**

10.4. This benchmark measures the average credit risk in the portfolio according to the institutions invested in and corresponds to the duration limits in Link Group's suggested credit methodology using a sliding scale of 1 to 7 where 1 indicates the least risk of default.

11. External treasury management advisers

11.1. Link Group continues to provide our Treasury Management Advisory service.

Glossary of Treasury Management related terms

LAS: Link Asset Services, Treasury Solutions – the Council's treasury management advisers.

CE: Capital Economics - is the economics consultancy that provides Link Asset Services, Treasury solutions, with independent economic forecasts, briefings and research.

CFR: Capital Financing Requirement - the Council's annual underlying borrowing need to finance capital expenditure and a measure of the Council's total outstanding indebtedness.

CIPFA: Chartered Institute of Public Finance and Accountancy – the professional accounting body that oversees and sets standards in local authority finance and treasury management.

CNAV: Constant Net Asset Value refers to funds that use amortised cost accounting to value all of their assets. They aim to maintain a Net Asset Value (NAV), or value of a share of the fund, at £1 (or currency equivalent) unless mark-to-market pricing of underlying assets moves outside of stipulated boundaries, and calculate their price to 2 decimal places, known as 'penny rounding'. Typical examples of such funds are government Money Market Funds.

COVID-19: a highly infectious respiratory disease caused by a new coronavirus. The disease was discovered in China in December 2019 and then spread around the world to become a pandemic, causing an unprecedented public health crisis and major economic impacts.

CPI: Consumer Price Index – the official measure of inflation adopted as a common standard by countries in the EU. It is a measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food and medical care. It is calculated by taking price changes for each item in the predetermined basket of goods and averaging them.

ECB: European Central Bank - the central bank for the Eurozone

EU: European Union

EZ: Eurozone -those countries in the EU which use the euro as their currency

Fed: The Federal Reserve System, often referred to simply as "the Fed," is the central bank of the United States. It was created by the Congress to provide the nation with a stable monetary and financial system.

Financial Instruments Revaluation Reserve: IFRS 9 'Financial Instruments – earmarking of gains not available to fund services' specifies that balances in the General Fund (or HRA balance) relating to unrealised, or volatile, gains from financial instruments classified as 'fair value through profit or loss' should be earmarked and not regarded as available to fund services. The Financial Instruments Revaluation Reserve (FIRR) holds the ciuumulative value of such gains or losses.

FOMC: The Federal Open Market Committee – this is the branch of the Federal Reserve Board which determines monetary policy in the USA by setting interest rates and determining quantitative easing policy. It is composed of 12 members--the seven members of the Board of Governors and five of the 12 Reserve Bank presidents.

FTSE: The Financial Times Stock Exchange, now known as FTSE Russell Group, is a British financial organization that specializes in providing index offerings for the global financial markets Informally known as the "Footsie".

GDP: Gross Domestic Product – a measure of the growth and total size of the economy.

G7: The group of seven countries that form an informal bloc of industrialised democracies - United States, Canada, France, Germany, Italy, Japan, and United Kingdom - that meets annually to discuss issues such as global economic governance, international security, and energy policy.

Gilts: Gilts are bonds issued by the UK Government to borrow money on the financial markets. Interest paid by the Government on gilts is called a coupon and is at a rate that is fixed for the duration until maturity of the gilt, (unless a gilt is index linked to inflation); while the coupon rate is fixed, the yields will change inversely to the price of gilts i.e. a rise in the price of a gilt will mean that its yield will fall.

HRA: Housing Revenue Account.

IFRS: International Financial Reporting Standard.

IMF: International Monetary Fund - the lender of last resort for national governments which get into financial difficulties.

LIBID: The London Inter Bank Bid Rate is the rate bid by banks on deposits i.e., the rate at which a bank is willing to borrow from other banks. It is the "other end" of the **LIBOR** (an offered, hence "ask" rate, the rate at which a bank will lend).

LIBOR: The London Inter Bank Offered Rate is the interest rate at which banks offer to lend funds (wholesale money) to one another in the international interbank market. It is a key benchmark rate that reflects how much it costs banks to borrow from each other but in the UK it was replaced by SONIA during 2021/22. Outside the London markey this is referred to as IBOR.

LVNAV: Low Volatility Net Asset Value (LVNAV) Money Market Funds are short-term MMFs. Funds are primarily invested in money market instruments, deposits and other short-term assets. Units in the fund are purchased or redeemed at a constant price so long as the value of the underlying assets do not deviate by more than 0.2% (20bps) from par (i.e. 1.00).

MHCLG: The Ministry of Housing, Communities and Local Government -the Government department that directs local authorities in England.

MPC: The Monetary Policy Committee is a committee of the Bank of England, which meets for one and a half days, eight times a year, to determine monetary policy by setting the official interest rate in the United Kingdom, (the Bank of England Base Rate, commonly called Bank Rate), and by making decisions on quantitative easing.

MRP: Minimum Revenue Provision -a statutory annual minimum revenue charge to reduce the total outstanding CFR, (the total indebtedness of a local authority).

PWLB: Public Works Loan Board – this is the part of H.M. Treasury which provides loans to local authorities to finance capital expenditure.

QE: Quantitative Easing – is an unconventional form of monetary policy where a central bank creates new money electronically to buy financial assets, such as government bonds, (but may also include corporate bonds). This process aims to stimulate economic growth through increased private sector spending in the economy and also aims to return inflation to target. These purchases increase the supply of liquidity to the economy; this policy is employed when lowering interest rates has failed to stimulate economic growth to an acceptable level and to lift inflation to target. Once QE has achieved its objectives of stimulating growth and inflation, QE will be reversed by selling the bonds the central bank had previously purchased, or by not replacing debt that it held which matures. The aim of this reversal is to ensure that inflation does not exceed its target once the economy recovers from a sustained period of depressed growth and inflation. Economic growth, and increases in inflation, may threaten to gather too much momentum if action is not taken to ‘cool’ the economy.

RPI: The Retail Price Index is a measure of inflation that measures the change in the cost of a representative sample of retail goods and services. It was the UK standard for measurement of inflation until the UK changed to using the EU standard measure of inflation – CPI. The main differences between RPI and CPI is in the way that housing costs are treated and that the former is an arithmetical mean whereas the latter is a geometric mean. RPI is often higher than CPI for these reasons.

SONIA: Sterling Over Night Index Average is the effective reference for overnight indexed swaps for unsecured transactions in the Sterling market. The SONIA itself is a risk-free rate. Unlike LIBOR it is backward looking measure.

TMSS: The annual treasury management strategy statement reports that all local authorities are required to submit for approval by the full Council before the start of each financial year.

VNAV: While CNAV and LVNAV funds use amortised cost accounting to value most or all of their assets, Variable Net Asset Value (VNAV) funds use mark-to-market pricing, meaning the unit price will change in light of changes to mark-to-market valuation of underlying assets, and dealing prices for VNAV funds are rounded to four decimal places. All funds except select types of Money Market Funds are priced on this basis.

VRP: A Voluntary Revenue Provision to repay debt, in the annual budget, which is additional to the annual MRP charge (see above definition).

Report Information Sheet

Committee / Date	Overview & Scrutiny Committee 28 September 2022
Title of report	Annual Treasury Management Report 2021/22

Officer / Councillor Approval *required	**Date**	**Name**
Ward Members(s)		N/A
Portfolio Holder	7/9/22	Richard Hales
Financial Services *		
Legal Services (*SDC)		
Other Services		
Chief Executive(s)	7/9/22	Andy Jones
Head of Services(s)*		
Section 151 Officer		Andrew Rollins
Monitoring Officer		
CMT (WDC)		No other responses
Leadership Co-ordination Group (WDC)		
Other organisations		N/A

Final decision by this Committee or rec to another Cttee / Council?	Yes/ No Recommendation to: Cabinet / Council ……………………. Committee
Contrary to Policy / Budget framework?	No/Yes
Does this report contain exempt info/Confidential? If so, which paragraph(s)?	No/Yes, Paragraphs:
Does this report relate to a key decision (referred to in the Cabinet Forward Plan)?	No/Yes, Forward Plan item – scheduled for ………… (date)
Accessibility Checked?	Yes/No