Brent	**Audit and Standards Advisory Committee** 18 July 2023
	Report from the Corporate Director of Finance and Resources

Treasury Management Outturn Report 2022/23

Wards Affected:	All
Key or Non-Key Decision:	N/A
Open or Part/Fully Exempt: (If exempt, please highlight relevant paragraph of Part 1, Schedule 12A of 1972 Local Government Act)	Open
No. of Appendices:	Six: Appendix 1 – Debt and Investment Portfolio Appendix 2 – Prudential Indicators Appendix 3 – Internal Investments – Average Rate vs Credit Risk Appendix 4 – MRP Strategy 2021/22 Appendix 5 – MRP Strategy 2022/23 Appendix 6 – MRP Strategy 2023/24
Background Papers:	None
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1.0 Introduction

1.1 This report updates members on Treasury Management activity and confirms that the Council has complied with its Prudential Indicators for 2022/23.

2.0 Recommendations

2.1 Audit and Standards Advisory Committee is asked to consider and note the 2022/23 Treasury Management Outturn report and the MRP Strategies in Appendix 4-6 and ask that it be forwarded to Cabinet and Full Council for approval, in compliance with CIPFA's Code of Practice on Treasury Management (the Code).

2.2 Note that for 2022/23 the Council has complied with its Prudential Indicators which were approved by Full Council on 24 February 2022 as part of the Council's Treasury Management Strategy Statement and Capital Strategy Statement.

3.0 Background

3.1 The Council's treasury management activity is underpinned by the CIPFA Code, which requires authorities to produce annually Prudential Indicators and a Treasury Management Strategy Statement on the likely financing and investment activity. The Code also recommends that members are informed of treasury management activities at least twice a year for 22/23.

3.2 The Council has borrowed money over the long term to support investment in the Council's infrastructure and also invests cash balances held for short periods. It is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk are central to the Council's treasury management strategy.

3.3 Treasury risk management at the Council is conducted within the framework of the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice (the CIPFA Code) which requires the Council to approve a treasury management strategy before the start of each financial year and, as a minimum, a semi-annual and annual treasury outturn report.

3.4 The 2021 Prudential Code includes a requirement for local authorities to provide a Capital Strategy, a summary document approved by full Council covering capital expenditure and financing, treasury management and non-treasury investments. The Council's Capital Strategy, complying with CIPFA's requirement, was approved by full Council on 24 February 2022.

4.0 Economic Background

4.1 The war in Ukraine continued to keep global inflation above central bank targets and the UK economic outlook remained relatively weak with the chance of a mild recession. The economic backdrop during the January to March period continued to be characterised by high energy and commodity prices, high inflation, and the associated impact on household budgets and spending.

4.2 Central Bank rhetoric and actions remained consistent with combatting inflation. The Bank of England, US Federal Reserve, and European Central

Bank all increased interest rates over the period, even in the face of potential economic slowdowns in those regions.

4.3 Starting the financial year at 5.5%, the annual CPI measure of UK inflation rose strongly to hit 10.1% in July and then 11.1% in October. Inflation remained high in subsequent months but appeared to be past the peak, before unexpectedly rising again in February. Annual headline CPI registered 10.4% in February, up from 10.1% in January, with the largest upward contributions coming from food and housing. RPI followed a similar pattern during the year, hitting 14.2% in October. In February RPI measured 13.8%, up from 13.4% in the previous month.

4.4 The labour market remained tight albeit with some ongoing evidence of potential loosening at the end of the period. The unemployment rate 3mth/year eased from 3.8% April-June to 3.6% in the following quarter, before picking up again to 3.7% between October-December. The most recent information for the period December-February showed an unemployment rate of 3.7%. The inactivity rate was 21.3% in the December-February quarter, slightly down from the 21.4% in the first quarter of the financial year. Nominal earnings were robust throughout the year, with earnings growth in December-February at as 5.7% for both total pay (including bonuses) and 6.5% for regular pay. Once adjusted for inflation, however, both measures were negative for that period and have been so throughout most of the year.

4.5 The Bank of England increased the official Bank Rate from 0.75% to 4.25% during the financial year. It has continued to increase, reaching 5.00% in June 2023 with expectations of further increases being necessary, possibly to 5.5% by September as the Monetary Policy Committee (MPC) attempt to prevent higher inflation and wage growth becoming embedded in the economy.

4.6 The Bank’s credibility issues mean that it can no longer afford to wait until the effect of past increases in Bank Rate affect activity. This suggests that further monetary tightening is necessary to have the desired immediate effect on inflation.

4.7 The lagged effect of aggressive monetary tightening will increasingly pressure economic activity. A recession appears inevitable. Household spending will be affected by increases in mortgage payments, while business investment/spending will fall back due to higher borrowing costs. Unemployment will increase.

4.8 Uncertainty continued to be a key driver of financial market sentiment and bond yields remained relatively volatile due to concerns over elevated inflation and higher interest rates, as well as the likelihood of the UK entering a recession and for how long the Bank of England would continue to tighten monetary policy. Towards the end of the period, fears around the health of the banking system following the collapse of Silicon Valley Bank in the US and purchase of Credit Suisse by UBS caused further volatility.

4.9 During 2022/23; the 5-year UK benchmark gilt yield rose from 1.41% to peak at 4.70% in September before ending the financial year at 3.36%. Over the same timeframe the 10-year gilt yield rose from 1.61% to peak at 4.51% before falling back to 3.49%, while the 20-year yield rose from 1.82% to 4.96% and then declined to 3.82%. The Sterling Overnight Rate (SONIA) averaged 2.24% over the period.

4.10 Despite household budgets remaining under pressure, consumer confidence rose to -36 in March, following readings of -38 and -45 in the previous two months, and much improved compared to the record-low of -49 in September. Quarterly GDP was soft through the year, registering a 0.1% gain in the April-June period, before contracting by (an upwardly revised) -0.1% in the subsequent quarter. For the October-December period was revised upwards to 0.1% (from 0.0%), illustrating a resilient but weak economic picture. The annual growth rate in Q4 was 0.6%.

4.11 The UK economy has been resilient in the face of the dual headwinds of inflation and interest rates, albeit the majority rise in Bank Rate is yet to impact households. Government cost of living support, stronger wage growth and household savings have had an offsetting effect, while timing issues around mortgage resets have delayed the impact of monetary tightening.

4.12 Global bond yields remain volatile, although UK gilt yields have been more affected by its seemingly idiosyncratic inflation issues. The Federal Reserve and other central banks see persistently higher policy rates through 2023 as key to dampening domestic inflationary pressure.

4.13 After reaching 9.1% in June, annual US inflation slowed for eight consecutive months to 6% in February. The Federal Reserve continued raising interest rates over the period with consecutive increases at each Federal Open Market Committee meetings, taking policy rates to a range of 4.75%- 5.00% at the March meeting.

4.14 From the record-high of 10.6% in October, Eurozone CPI inflation fell steadily to 6.9% in March 2023. Energy prices fell, but upward pressure came from food, alcohol, and tobacco. The European Central Bank continued increasing interest rates over the period, pushing rates up by 0.50% in March, taking the deposit facility rate to 3.0% and the main refinancing rate to 3.5%.

5.0 Revised CIPFA code and PWLB Lending guidance

5.1 In May 2022, HM Treasury provided updated guidance to local authorities to ensure their capital plans would be compliant with ongoing access to the PWLB borrowing facility, building upon lending terms originally published in November 2020.

5.2 The revised guidance clarified that “The PWLB will not typically advance new loans if there is a more than negligible risk that the newly advanced PWLB loan will not be repaid without future government support”. However, the guidance goes on to comment that authorities following the Prudential Code would generally be adequately managing risk.

5.3 The existing guidance provided by HM Treasury includes examples of permitted and prohibited use of PWLB funds. Authorities that are purchasing or intending to purchase investment assets primarily for yield will not be able to access the PWLB except to refinance existing loans or externalise internal borrowing. Acceptable use of PWLB borrowing includes service delivery, housing, regeneration, preventative action, refinancing and treasury management. The restrictions do not impact the Council as we have any commercial activities within the Capital Programme.

5.4 CIPFA published its revised Prudential Code for Capital Finance and Treasury Management Code on 20th December 2021. The key changes in the two codes are around permitted reasons to borrow, knowledge and skills, and the management of non-treasury investments.

5.5 The principles of the Prudential Code took immediate effect although local authorities could defer introducing the revised reporting requirements until the 2023/24 financial year. The Council chose to delay introducing the revised reporting requirements until the 2023/24 financial year.

5.6 In March 2023, the PWLB launched a further borrowing rate at gilt yields + 0.40% for borrowing within the Housing Revenue Account, which became available on 15 June 2023. However, given the significant move in base rates since the announcement, borrowing is still significantly more expensive, so it is unlikely to have a material impact on the Council's future borrowing plans. For Example, a 20-year EIP loan for the HRA at the time of the Spring Budget announcement would have achieved a rate of 3.91% however at the time of the rate launch the rate that could be achieved was 4.83%.

6.0 Local Context

6.1 On 31st March 2022, the Council had total borrowing of £684.6m arising from its revenue and capital income and expenditure. The Council's underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR) while usable reserves and working capital are the underlying resources available for investment. These factors are summarised in Table 1 below.

Table 1: CFR and Borrowing Summary

Table 1: Balance Sheet Summary

	31.3.23 Actual £m
General Fund CFR	851.4
HRA CFR	294.9
Total CFR	**1,146.4**

*Other debt liabilities	36.2
Borrowing CFR	**1,182.6**
External borrowing	781.0
Internal (over) borrowing	
Less: Usable reserves	(491.2)
Less: Working capital	(173.6)
Investments (or new borrowing)	**116.2**

* finance leases, PFI liabilities and transferred debt that form part of the Council's total debt

6.2 Higher interest rates have increased the cost of short-term loans. The Council pursued its strategy of keeping external borrowing lower than its underlying level by temporarily using cash held for other purposes, known as internal borrowing, in order to reduce risk and minimise the interest costs incurred from external borrowing.

6.3 The treasury management position at 31st March 2023 and the change during the year is shown in Table 2 below.

Table 2: Treasury Management Summary

	31.3.22 Balance £m	**Movement £m**	**31.3.23 Balance £m**	**31.3.23 Rate %**
Long-term borrowing	566.4	128.9	695.3	3.80%
Short-term borrowing	124.2	(38.5)	85.7	0.38%
Total borrowing	**690.6**	**90.4**	**781.0**	
Cash and cash equivalents:* Money Market Funds	98.6	17.6	116.2	**0.06%**
Total investments	**98.6**	**17.6**	**116.2**	
Net borrowing	**592.0**	**72.8**	**664.8**	

* This relates to our short term Treasury investments (Money Market Funds and DMA deposits). Cash balances held are not deemed an investment so are not included in the above total.

6.4 Cash and cash equivalent investments represent deposits which are readily convertible into cash at immediate notice. Included within this total are Money Market Funds (MMF's) which are mutual funds which invest in high-quality short-term debt. Also included is the Debt Management Agency Deposit Facility (DMADF), which provides fixed deposits and is managed by the Debt Management Agency, which is a part of HM Treasury.

6.5 Borrowing has increased in the past year, in order to meet the requirements of our long-term Capital investment programme as internal cash resources were utilised.

7.0 Borrowing Strategy

7.1 At 31st March 2023 the Council held £781.0m of loans, (an increase of £96.4m in year), as part of its strategy for funding previous and current years' capital programmes. Outstanding loans on 31st March are summarised in Table 3 below.

Table 3: Borrowing Position

	31.3.22 Balance £m	**Net Movement £m**	**31.3.23 Balance £m**	**31.3.23 Weighted Average Rate %**	**31.3.23 Weighted Average Maturity (years)**
Public Works Loan Board	407.1	135.9	543.0	3.92	27.34
LOBO loans	70.5	-	70.5	4.68	42.63
Fixed Rate Loans (LT)	95.0	-	95.0	2.56	22.88
Local Authority Loans (ST)	112.0	(42.0)	70.0	3.01	0.39
Fixed Rate Loans (ST)	-	2.5	2.5	0	1
Total External Borrowing	**684.6**	**96.4**	**781.0**		

7.2 The Council has continued to borrow where necessary over the past year to meet the funding requirements of the agreed capital programmes.

7.3 The Council's borrowing decisions are not predicated on any one outcome for interest rates. In year, the proportion of long-term debt has increased as the Council has borrowed to meet the requirements of its capital programme. Securing the long-term rates achieved in-year provides certainty for the development plans, allowing for predictable cashflows long into the future.

7.4 The Council has an increasing CFR due to the capital programme and an estimated borrowing requirement as determined by the Liability Benchmark, which also takes into account usable reserves and working capital. Having considered the appropriate duration and structure of borrowing based on realistic projections, it was decided to take a combination of both short-term borrowing and long-term repayment loans (with a mixture of both EIP and Maturity loan structures). Details around the new loans taken out in the current financial year are provided below.

Loan-dated Loans borrowed	Amount (£m)	Rate (%)	Period to maturity (years)
PWLB EIP Loan	20	3.18	20
PWLB Maturity Loan	40	3.15	50
PWLB Maturity Loan	20	4.1	50
PWLB Maturity Loan	40	3.87	50
PWLB EIP Loan	20	3.96	20

7.5 The Council has assessed all alternate options to PWLB and will continue to do so in the future, working closely with its Treasury advisor Arlingclose. Where there are possibilities to secure lower cost funding, these will be reviewed. In particular, there may be options to seek lower cost funding around the development of the low carbon heat network in South Kilburn; with a number of public and private bodies able to provide financing.

7.6 The Council continues to hold £70.5m of LOBO (Lender's Option Borrower's Option) loans where the lender has the option to propose an increase in the interest rate as set dates, following which the Council has the option to either accept the new rate or to repay the loan at no additional cost. No banks exercised their option during the year.

7.7 Due to the higher interest rate environment, there is an increased possibility that the options within our existing LOBO's will be exercised. Three LOBOs with a total value of £26m have options dates during 23/24. We will work closely with our Treasury advisers to identify and review the optimal solution if these options are exercised.

Minimum Revenue Provision

7.8 The Minimum Revenue Provision (MRP) is the charge to revenue made in respect of paying off the principal sum of the borrowing undertaken to finance the capital programme. The statutory guidance provides options for calculating a charge that is considered prudent. The approach for this calculation is approved as part of the budget setting process each February by Full Council in the Minimum Revenue Provision Statement.

7.9 A review of the MRP calculation was undertaken following a recommendation from our external auditors which has resulted in a change in approach for assets acquired prior to 2008. The expected economic life of these assets has been revised downwards from 100 years to 49 years following the change in approach for calculating the economic life of land. The updated MRP statements for the years 2021/22, 2022/23 and 2023/24 are included in Appendix 4-6.

8.0 Investment Activity

8.1 CIPFA published a revised Treasury Management in the Public Services Code of Practice and Cross-Sectoral Guidance Notes on 20th December 2021. These define treasury management investments as investments that arise from the organisation's cash flows or treasury risk management activity that ultimately represents balances that need to be invested until the cash is required for use in the course of business.

8.2 The Council holds invested funds, representing income received in advance of expenditure plus balances and reserves. During the year, the Council's investment balances ranged between £72.7m and £159.5m due to timing differences between income and expenditure. The investment position is shown in table 4 below.

8.3 The CIPFA Treasury Management Code requires local authorities to consider their counterparty policies in light of environmental, social and governance (ESG) information. The Council has regard to funds who have signed up to ESG related initiatives, including the UN Principles for responsible investment, the UK Stewardship Code and the Net-Zero Asset Managers Initiative.

Table 4: Treasury Investment Position

	31.3.22	Net	31.3.23	31.3.23	31.3.23
	Balance	**Movement**	**Balance**	**Income Return**	**Weighted Average Maturity**
	£m	**£m**	**£m**	**%**	**days**
Local authority deposit	-	-	-	2.77	30.76
Money Market Funds	98.6	17.6	116.2	2.16	1
Total investments	**98.6**	**17.6**	**116.2**		

8.4 Both the CIPFA Code and government guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its treasury investments before seeking the optimum rate of return, or yield. The Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

8.5 Increasing interest rates have led to improved returns on our short-dated holdings. At 31st March, the Council achieved circa 4.1% from MMF holdings, which compares to compares to 0.6% a year earlier. Rates have increased throughout the year, notwithstanding the volatility around the time of the mini-budget.

8.6 Given the higher interest rate environment and the Council's need to hold cash for day-to-day requirements, deposits have been held in short term investments, providing the Council with improved liquidity. This has also led to increased investment income given the increased deposit rates that followed from changes in the Bank of England base rate. There was also a focus on holding funds with high credit ratings, providing increased security over the Council's investment portfolio.

8.7 The progression of risk and return metrics are shown in the extracts from Arlingclose's quarterly investment benchmarking in Table 5 below.

Table 5: Investment Benchmarking – Treasury investments managed in-house

	Credit Score	**Credit Rating**	**Bail-in Exposure**	**Weighted Average Maturity (days)**	**Rate of Return %**
31.03.2022	5.06	A+	100%	1	0.52%
31.03.2023	5.03	A+	100%	1	4.08%
Similar LAs	4.71	A+	61%	32	2.24%
All LAs	4.71	A+	**59%**	12	**1.59%**

*Weighted average maturity

8.8 In light of Russia's invasion, Arlingclose contacted the fund managers of our MMF funds and confirmed no direct exposure to Russian or Belarusian assets had been identified.

Non-Treasury Investments

8.9 The definition of investments in CIPFA's revised 2021 Treasury Management Code covers all the financial assets of the Council as well as other non-financial assets which the Council holds primarily for financial return. Investments that do not meet the definition of treasury management investments (i.e. management of surplus cash) are categorised as either for service purposes (made explicitly to further service objectives) and or for commercial purposes (made primarily for financial return). The non-Treasury investments are held to further service objectives and are therefore categorised as for service purposes. The non-Treasury investments are classified under shareholdings to subsidiaries and loans to subsidiaries, detailed in 8.10 below. The Council received approximately £3m of gross income from commercial property during the year. Investment property of £14.1m was held at year end.

8.10 Investment Guidance issued by the Department for Levelling Up Housing and Communities (DLUHC) and Welsh Government also broadens the definition of investments to include all such assets held partially or wholly for financial return.

8.11 The Council also held £256.3m of such investments in:

- Shareholding in subsidiaries £103.5m.

- Loans to subsidiaries £152.8m.

8.12 I4B Holdings Limited is a company wholly owned by Brent Council that was incorporated on 16 December 2016. The primary purpose of the company is to deliver the housing options defined in the Temporary Accommodation reform plan. As of 31st March 2023, the Council had provided funding of £182.1m to i4B (2021/22: £126.0m) which are secured against the company's properties. The Council received £5.2m (2021/22: £4.0m) in interest and fees for loans to I4B. The loans are secured against the properties held within the company.

8.13 First Wave Housing (FWH) is a registered provider of housing in Brent and is wholly owned by Brent Council. FWH was setup to manage properties previously owned by Brent Housing Partnership (BHP). The Council received £0.7m (2021/22: £1.1m) in interest for loans to FWH. As of 31 March 2023, there were outstanding loans to Brent Council totalling £34.7m (2021/22: £35.1m) which are secured against the properties held within the company.

8.14 These investments generated £5.9m (2021/22 £5.1m) of income for the Council in 2022/23. This investment income covers the borrowing cost of investing in housing through wholly owned subsidiaries. These borrowing costs would be incurred by the Council regardless of the method through which the Council develops new housing, however this is the vehicle of choice for such investments.

9.0 Compliance

9.1 The Corporate Director for Finance and Resources reports that all treasury management activities undertaken during the year complied fully with the CIPFA Code of Practice and the Council's approved Treasury Management Strategy.

9.2 Compliance with the authorised limit and operational boundary for external debt is demonstrated within Appendix 2 (Debt Limits).

10.0 Investment Training

10.1 The needs of the Council's treasury management staff for training in investment management are kept under review. These are considered as part of the staff appraisal process and additionally when the responsibilities of individual members of staff change.

11.0 Financial Implications

11.1 The implications are noted within the report.

12.0 Legal Implications

12.1 None identified.

13.0 Diversity Implications

13.1 None identified.

Related Documents:
Treasury Management Strategy Report to Council – 24 February 2022.

<u>Report sign off:</u> ***Minesh Patel*** Corporate Director for Finance and Resources