TITLE	**Treasury Management Mid Year Report 2022-23**
FOR CONSIDERATION BY	Audit Committee on 30 November 2022
WARD	None Specific
LEAD OFFICER	Deputy Chief Executive - Graham Ebers

OUTCOME / BENEFITS TO THE COMMUNITY

To demonstrate that the Council's treasury function has effectively managed the Council's debt and cash balances to support the funding of the delivery of the Council's key priorities.

RECOMMENDATION

The Audit Committee is asked to support the Treasury Management Mid-Year Report 2022-23 and recommend it to Council and note:

1) that all approved indicators set out in the Treasury Management Strategy have been adhered to; with the exceptions of internal borrowing which is forecast to be higher than set out in the strategy and ratio of financing costs to net revenue stream – General Fund.

2) due to the current uncertainty in the interest rate market, the internal borrowing parameter is being reviewed with our external treasury management advisors and will be reported back as part of treasury management strategy.

3) the contents of "Table A", as set out in the report, which shows the net benefit per council tax band D equivalent, from the income generated less the financing costs on all borrowing to date equates to £15.29 per band D for 2022/23. This income is used by the Council to continue to provide priority services for the borough residents.

4) As at the end of September 2022, the forecast for the total external general fund debt was £112m at March'23, which reduces to £81m after taking into account cash balances (net indebtedness) reducing interests costs in the current economic climate.

5) The Executive agreed on 27th October 2022, recommendation 3 of the Capital Monitoring 2022/23 – Q2 report 'note that due to the current uncertainty surrounding higher interest rates, as part of our financial management process, a review is to be undertaken to determine what capital projects can be postponed this year, to minimise exposure to borrowing at high rates. Any postponement is to be agreed at Executive.'

SUMMARY OF REPORT

This report provides a summary of the treasury management operations during the first six months of 2022/23. It is presented for the purpose of monitoring and review, in accordance with Council's treasury management practices. The Council adhered to all agreed prudential indicators with the exception of internal borrowing. This includes ensuring the necessary liquidity to deliver on the day-to-day operations of the Council.

There are two aspects of treasury performance: debt management which relates to the Council's borrowing and cash investment which relates to the investment of cash balances.

Key highlights from this report to note are:

- All approved indicators set out in the Treasury Management Strategy have been adhered to with the exceptions of internal borrowing and ratio of financing costs to net revenue stream – GF. Although internal borrowing is higher than the forecast in the strategy, this is positive on the basis, the Council has reduced the need for external borrowing by utilising cash balances more than was planned in the strategy.

  When the strategy was set, the interest rate market was fairly stable with regards to future forecasts of interest rates remaining low. Based on these market conditions, the Council would have looked to secure some medium to long external borrowing. However, due to the recent volatility and rise in interest rates, alongside a reduction in capital spend and the maintaining of cash balances, it is financially more prudent to minimise external borrowing, thus avoid higher external debt costs. This approach has been discussed with our external treasury management advisors and is considered prudent due to the strength of our cash balances forecast for this financial year.

- The annual benefit from the income generated less the financing costs on all borrowing to date equates to £15.29 per council tax band D property for 2022/23. This benefit is reinvested into supporting Council wide services.

- Net indebtedness after cash balances is £51m at end of September and forecast to rise to £81m at the end of the financial year.

- The average interest rate of external borrowing for 2022/23 is forecast to be 1.56%.

A detailed breakdown of the Council's performance in these areas is summarised below.

Prudential Indicators Debt and Investment

The table summarises the prudential indicators, comparing the limits set in the strategy and the forecast position at outturn (31 March 2023). These are primary indicators designed to ensure the key objectives of the Prudential Code are met and that local authorities' capital investment plans are affordable, prudent and sustainable; that treasury management decisions are taken in accordance with good professional practice.

Key highlights to note are;

- Authorised and operational boundary limits are forecast to be lower than the treasury strategy. This is because the Capital financing requirement (CFR) is forecast to reduce due to savings in the capital programme and re-profiling of capital expenditure to later financial years. The CFR is a calculation of historic capital expenditure less that already paid for, required to arrive at the annual level of debt repayment.

- General fund external borrowing is forecast to be lower than expected as a result of the reprofiling. Furthermore, the internal borrowing level is being increased to offset the impact from high interest rates and volatility in the market. The Council will look to minimise new external borrowing through utilising its cash balances. This will avoid higher external debt costs.

- The net general fund financing costs of the Council are forecast to remain small, at £0.1m which is 0.1% of the net revenue expenditure. The movement on this from the original budgets is as a result of reducing the interest charge to town centre (to better reflect the actual interest costs) to help maintain its movement to a surplus following significant economic challenges.

Prudential Indicators	**Treasury Strategy**	**Forecast Outturn March '23**
	£m	**£m**
Affordability		
Limits		
Authorised Limit (Note: CFR*120%)	760	589
Operational Boundary (Note: CFR*110%)	696	540
Performance Indicators		
Capital financing requirement – General Fund (GF)	554	412
Capital financing requirement – HRA	79	79
Gross external borrowing – General Fund (GF)	388	112
Gross external borrowing - HRA	69	66
% of internal borrowing to CFR – General Fund (GF)	30%	73%
% of internal borrowing to CFR - HRA	13%	17%
Ratio of financing costs to net revenue stream - GF	-0.60%	0.10%
Ratio of financing costs to net revenue stream - HRA	29.90%	29.69%
Prudence		
Maturity structure of borrowing	See table B	

Council's Net Indebtedness

Net indebtedness represents the underlying debt position the Council holds. The table below shows how this is calculated. Included below are the estimates from the 22/23 treasury management strategy, the mid-year position and the forecast position for March '23. The previous years outturn is included for comparison.

	Treasury Strategy £m	Mid-Year (30th Sept) £m	Forecast Outturn March '23 £m	Outturn March '22 £m
General Fund – Capital Financing Requirement	554	397	412	382
Less Internal funded borrowing	(166)	(248)	(300)	(186)
External Debt Total	388	149	112	196
Less Cash investment balances	(152)	(98)	(31)	(124)
Net Indebtedness Total	**236**	**51**	**81**	**72**

As at the mid-year position (30th September 2022), total external borrowing for the general fund was £149m and treasury investments (cash investment balances) were £98m resulting in net indebtedness of £51m. The HRA borrowing is excluded from this calculation as it is a ringfenced account with external borrowing funded from housing tenants.

As set out in the treasury management strategy, net indebtedness was estimated to be £236m for 2022/23. The mid-year net indebtedness position of £51m and the forecast outturn of £81m are comfortably within the estimates set out in the strategy. This is driven largely by the capital financing requirement forecast to be £412m rather than £554m forecast in the strategy. This is due to savings in the 22/23 capital programme aswell as capital reprofiling (moving expenditure back to later years). This will result in external borrowing forecast to be £112m at 31st March 2023, £276m less than estimated in the strategy and significantly down from £196m at March '2022.

Due to the recent unexpected increases in interest rates and continued uncertainty in the market, the Council are looking to minimise external borrowing and thus avoid high borrowing costs. Underlying cash balances are expected to be slightly above those forecast in the strategy. This allows the Council to avoid external borrowing by using up cash investment balances and therefore reducing exposure to high interest rates. Cash balances are forecast to be significantly lower at £31m down from £152m. This does create a higher level of internal borrowing, which is forecast to be c70% for the general fund. The Council have reviewed the underlying cash balances (reserves + working capital) and are confident these can support a high level of internal borrowing for 2022/23. Further work will be undertaken during the next 6 months to review the cashflow and to take into account the new medium term financial plan requirements.

The Council are monitoring interest rates very closely and working with our treasury management advisors to review the latest interest rate forecasts which currently suggest interest rates are expected to peak in 2023. Operating a high level of internal borrowing will help offset the impact from higher interest rates. It is expected that the Council will need to borrow next financial year to support the capital programme. The timing of this borrowing requirement will be developed over the coming months taking into account updated forecasts for capital expenditure, cash balances and interest rates.

The average interest rate on the Council's external debt is forecast to be 1.56% across the year. This is expected to rise next financial year with the recent increases in interest rates.

Cost of Financing Debt

The table below shows the gross financing costs of servicing the external debt. Gross financing costs reflect the annual interest costs payable and an amount for Minimum Revenue Provision (MRP). To understand the true cost of this, it is important to take into account the income from treasury investments, contributions from 'invest to save' schemes, income from investment / commercial properties which all contribute to reducing the annual cost of this financing. Furthermore, for completeness and transparency the table has been extended to show additional income the Council receives from our assets which contributes towards the funding of key services the Council provide. This is the income over and above the amount used to contribute towards the financing costs of the borrowing.

Taking these factors into account, for the general fund the net annual benefit from the income generated less the financing costs on all borrowing to date equates to £15.29 per council tax band D property for 2022/23 as set out below. This income is used by the Council to continue to provide priority services for the borough residents.

TABLE A

		Previous Year Outturn £,000	Forecast Outturn March '23 £,000
	General Fund – Financing Cost (Interest and MRP debt repayment)	8,827	8,701
	Less contributions towards financing costs from following areas:		
	- Invest to save schemes	(849)	(1,669)
	- Treasury investments	(1,616)	(1,116)
	- Housing, Local Economy and Regeneration	(6,977)	(5,767)
	Net Annual Financing Cost / (Benefit)	(615)	149
	Include additional income over and above the contributions shown above:		
	- Community investments	(1,016)	(1,295)
	Net Annual Benefit to the taxpayer	**(1,631)**	**(1,146)**

	Net Annual Benefit £m	(1,631)	(1,146)
	Divide by Council Tax Base (no. of band D equivalent properties)	73,297.00	74,946.30
	Benefit per band D property - £	**£22.25**	**£15.29**

Investment of Cash Balances

Cash flow balances vary significantly throughout the year due to differences in timing of income (council tax, developer contributions, grants, etc.) and timing of expenditure (running costs - revenue, and investment in assets and services – capital). During times when the council holds cash balances, investments will be made based on security, liquidity, and yield (in this order).

As highlighted in the table above, treasury investment returns are forecast to be c£1.1m of which c£0.7m is investment income from cash investments such as short-term loans to local authorities and returns from money market funds. Cash investment balances are forecast to be c£31m at the end of the financial year. Cash balances vary throughout the year and have reduced as external debt has been repaid and also been used to support higher internal borrowing. The average return on these balances is estimated to be 0.72%. The rate of returns are starting to increase as expected with the recent increases in interest rates, however more importantly for the Council is the security and liquidity of these balances before yield is considered.

The table below shows the Council's investments by type, including performance and year-end balance.

	Average Invested	Interest Received	Average rate of return	31st March 2023 Balance
	£m	**£m**	**%**	**£m**
Housing, Local Economy & Regeneration	£118.2m	£2.9m	2.46%	£116.2m
Treasury Investments				
- Fund Managers	£0.7m	£0.004m	0.61%	£0.7m
- Local Authorities	£60.8m	£0.5m	0.76%	£0.0m
- Money Markets	£27.9m	£0.2m	0.79%	£30.0m
Total	**£207.5m**	**£3.6m**	**1.73%**	**£146.8m**

Included within the Housing, Local Economy & Regeneration are the capital loans made to the Councils housing companies which support the development of new affordable housing. The Council have a statutory requirement under the Subsidy Control Act 2022 (previously known as state aid) to charge interest at the market rate which is higher than the investment returns the Council would achieve on treasury investments.

Maturity Structure of Borrowing

The maturity structure of the Council external borrowing is shown in 'Table B' below. This highlights the period for when external borrowing matures and becomes repayable. External debt is forecast to be £112m for the general fund and £66m for the HRA, totalling £178m.

TABLE B

	Forecast Outturn March '23
	£m
Less than 1 year	0
Between 1 and 2 years	56
Between 2 and 5 years	13
Between 5 and 10 years	26
Between 10 and 15 years	39
Between 15 and 20 years	0
Between 20 and 25 years	1
Between 25 and 30 years	3
More than 30 years	40
	178

The Council continue to best align the repayment of external borrowing with the reduction in the capital financing requirement. This will be related to capital receipts, developer contributions and income generation from capital investments. This work is done with support from our external treasury management advisors.

As highlighted in the table above, the Council have a mixture of maturities to align to expected timing of capital resources. This is to avoid the Council holding external debt longer than needed.

Due to the uncertainty around interest rates at present, any new borrowing will be taken out on a short-term basis, with a view to refinancing the loans at lower interest rates at maturity.

FINANCIAL IMPLICATIONS OF THE RECOMMENDATION
The Council faces severe funding pressures, particularly in the face of the COVID-19 crisis. It is therefore imperative that Council resources are focused on the vulnerable and on its highest priorities.

	How much will it Cost/ (Save)	Is there sufficient funding – if not quantify the Shortfall	Revenue or Capital?
Current Financial Year (Year 1)	See other financial information	Yes	Revenue
Next Financial Year (Year 2)	Not applicable	Yes	Revenue
Following Financial Year (Year 3)	Not applicable	Yes	Revenue

Other financial information relevant to the Recommendation/Decision
• the net benefit per council tax payer for the financing of all borrowing to date equates to c£15.29 per band D equivalent. • At March '23, total external general fund debt is forecast to be £112m and the Councils net indebtedness after cash balances is £81m. • The average interest rate of external borrowing is 1.56%.

Cross-Council Implications
None

Public Sector Equality Duty
This is a report on the performance of the treasury service of the Council and is not requesting any funding or service changes that would impact on any members of the community and thus has no equalities impact.

Climate Emergency – *This Council has declared a climate emergency and is committed to playing as full a role as possible – leading by example as well as by exhortation – in achieving a carbon neutral Wokingham Borough by 2030*
This is a report on the performance of the treasury service of the Council, and has no impact on the Council's carbon neutral objective.

Reasons for considering the report in Part 2
Not applicable

List of Background Papers
None

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