Audit Committee

26th September 2022

Report of: Service Director: Finance

Title: Treasury Management Annual Report 2021/22

Ward: City Wide

Officer Presenting Report: Ravi Lakhani, Head of Strategic Finance

Contact Telephone Number: 07342 086687

Recommendation
The Audit Committee note the Annual Treasury Management Report for 2021/22, as detailed in Appendix A.

Summary
The Council is required to produce an annual treasury management review of activities and the actual treasury indicators in accordance with Local Government regulations.

The significant issues in the report are:

- The Council has complied with treasury management legislative and regulatory requirements during the period and all transactions were in accordance with the approved Treasury Management Strategy.

- The 2021–2026 Treasury Strategy identified a medium term borrowing requirement of £260m to support the existing and future Capital Programme. The Council's agreed policy is to defer borrowing while it has significant levels of cash balances (£237m at March 2022), noting if the financial environment changes and borrowing was deemed advantageous the Council may borrow over appropriate maturity periods.

- The Council's long term debt at 31 March 2022 was £451m with an average annual interest rate of 4.48%. Investments were £237m at the 31 March 2022 with an average annual interest rate of 0.13%.

Policy

There are no policy implications as a direct result of this report.

Consultation

1. **Internal**

   Executive & Service Directors, and Deputy Mayor – Finance, Governance & Performance.

2. **External**

   Link Asset Services – the Council's external treasury management advisors

Background and Context

1. The Council's treasury management activity is underpinned by CIPFA's Code of Practice on Treasury Management (the Code), which requires local authorities to produce annually Prudential Indicators and a Treasury Management Strategy Statement on the likely financing and investment activity. The Code also requires reports to full Council mid-year and after the year end. The 2021/22 outturn report is set out as Appendix A.

2. The Code also requires the Council to nominate one of its Committees to have responsibility for scrutiny of its treasury management strategy, policy and activity. Council has delegated that responsibility to the Audit Committee. Overall responsibility for treasury management remains with the Council. No treasury management activity is without risk; the effective identification and management of risk are integral to the Council's treasury management objectives.

3. Treasury management is defined as:

   "The management of the local authority's borrowing, investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks".

Other Options Considered

Not applicable

Risk Assessment

The principal risks associated with treasury management are:

Risk	Mitigation
Loss of investments as a result of failure of counterparties	Limiting the types of investment instruments used, setting strict lending criteria and only lending to high quality counterparties, and limiting the extent of exposure to individual counterparties
Increase in the net financing costs of the authority due to borrowing at high rates of interest / lending at low rates of interest	Planning and undertaking borrowing and lending in light of assessments of future interest rate movements, and by undertaking most long term borrowing at fixed rates of interest (to reduce the volatility of capital financing costs)

Public Sector Equality Duties

None necessary for this report

Legal and Resource Implications

Legal

The Council is under a duty to manage its resources prudently and therefore due consideration must always be given to its borrowing and lending strategy. A wide range of local authority financial activities, including borrowing, lending, financial management, and the approval of types of investment vehicle are governed by legislation and various regulations. The Council is obliged to comply with these. **(Legal advice provided by Tim O'Gara - Service Director: Legal and Democratic Services)**

Financial

(a) Revenues

The financing costs arising from planned borrowing are provided for in the revenue budget and medium term financial plan. Any additional operating costs arising from capital investment must be contained within the revenue budget of the

relevant department.

(b) Capital
Not Applicable
(Financial advice provided by Jon Clayton – Capital and Investments Manager)

Land
Not applicable

Personnel
Not Applicable

Appendices:
Appendix A – Treasury Management Annual Report 2021/22

LOCAL GOVERNMENT (ACCESS TO INFORMATION) ACT 1985
Background Papers:

None

Appendix A

Treasury Management Annual Report 2021/22

Purpose of the report:

1. Under the CIPFA Code of Practice on Treasury Management (the Code) the Section 151 Officer is required to produce an outturn report on activities in the year to account for how the Strategy, set at the start of the year has been implemented. This report meets the requirements of both the Code and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).

Background

2. The Council's treasury management activity is underpinned by CIPFA's Code of Practice on Treasury Management (the Code), which requires local authorities to produce annually Prudential Indicators and a Treasury Management Strategy Statement on the likely financing and investment activity. The Code also requires reports to full Council mid-year and after the year end.

3. The Code also requires the Council to nominate one of its Committees to have responsibility for scrutiny of its treasury management strategy, policy and activity. Council has delegated this responsibility to the Audit Committee. Overall responsibility for treasury management remains with the Council. No treasury management activity is without risk; the effective identification and management of risk are integral to the Council's treasury management objectives.

4. Treasury management is defined as:

   "The management of the local authority's borrowing, investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

5. The Council's investment priorities will be security first, portfolio liquidity second and then yield, (return).

The Economy and Interest Rates for 2021/22

6. *The Bank of England use interest rates to manage inflation and this has a subsequent effect on the economy and the rates at which the Council can borrow and invest at.*

7. **UK. Economy**. Over the last two years, the coronavirus outbreak has done significant economic damage to the UK and to economies around the world. After the Bank of England took emergency action in March 2020 to cut Bank Rate to 0.10%, it left Bank Rate unchanged at its subsequent meetings until raising it to 0.25% at its meeting on 16th December 2021, 0.50% at its meeting of 4th February 2022 and then to 0.75% in March 2022.

   The UK economy experienced several false dawns through 2021/22, but with most of the

economy now opened up and nearly back to business-as-usual, the GDP numbers have been robust (9% y/y Q1 2022) and sufficient for the MPC to focus on tackling the second-round effects of inflation, now that the CPI measure has already risen to 6.2% (as at March 22) and is significantly exceeding this in the summer of 2022.. *(Note further information on the recent changes to inflation in 22/23 will be reported in the Treasury Management mid-year report and finance monitoring reports).*

Gilt yields fell towards the end of 2021, but despite the war in Ukraine gilt yields have increased in early 2022. At 1.38%, 2-year yields remain close to their recent 11-year high and 10-year yields of 1.65% are close to their recent six-year high. These rises have been part of a global trend as central banks have suggested they will continue to raise interest rates to contain inflation.

USA. Their were a number of "hawkish" comments from Federal Reserve officials in March 2022 as part of the Federal Open Market Committee meeting that had markets pricing in a further 225bps of interest rate increases in 2022 on top of the initial move to an interest rate range of 0.25% - 0.5%.

The upward pressure on inflation from higher oil prices and potential knock-on impacts on supply chains all indicate for tighter policy (CPI was estimated at 7.8% across Q1), but the impact to real disposable incomes and the possibility of a recession points to the opposite.

EU. With euro-zone inflation having jumped to 7.5% in March it indicates that the European Central Bank will accelerate its plans to tighten monetary policy. It is likely to end net asset purchases and the market is now anticipating possibly three 25bp interest rate hikes in the calendar year followed by more in 2023.

While inflation has hit the headlines recently, the risk of recession has also been rising. Among the bigger countries, Germany is most likely to experience a "technical" recession because its GDP contracted in Q4 2021, and its performance has been subdued in Q1 2022. However, overall, Q1 2022 growth for the Eurozone was expected to be 0.3% q/q with the y/y figure posting a healthy 5.2% gain.

China. After the effort to restrict the virus outbreak in Q1 of 2020, economic recovery was strong in the rest of the year; however, 2021 has seen the economy negatively impacted by further outbreaks of Covid-19 in large cities with official GDP numbers c4% y/y.

World growth. World growth is estimated to have expanded 8.9% in 2021/22 following a contraction of 6.6% in 2020/21.

Deglobalisation. Until recent years, world growth has been boosted by increasing globalisation i.e. countries specialising in producing goods and commodities in which they have an economic advantage and which they then trade with the rest of the world. This has boosted worldwide productivity and growth, and, by lowering costs, has also depressed inflation. However, the rise of China as an economic superpower over the last 30 years, which now accounts for 18% of total world GDP (the USA accounts for 24%), and Russia's recent invasion of Ukraine, has unbalanced the world economy. In addition, after the pandemic exposed how frail extended

supply lines were around the world, both factors are now likely to lead to a sharp retrenchment of economies and an increase in inflation.

It is, therefore, likely that we are heading into a period where there will be a reversal of world globalisation and will likely lead to a reduction of world growth rates.

Central banks' monetary policy. During the pandemic, the governments of western countries have provided significant fiscal support to their economies which has resulted in a big increase in total government debt in each country. It is therefore important that bond yields stay low while debt to GDP ratios slowly reduce under the impact of economic growth. This provides governments with a good reason to amend the mandates given to central banks to allow higher average levels of inflation than we have generally seen over the last couple of decades. Both the Federal Reserve and Bank of England have already changed their policy towards implementing their existing mandates on inflation, (and full employment), to hitting an average level of inflation. Greater emphasis could also be placed on hitting subsidiary targets e.g. full employment before raising rates. Higher average rates of inflation would also help to erode the real value of government debt more

Treasury position as at 31 March 2022:

8. The table below indicates the balance of borrowing and investments at the beginning and end of the year and average borrowing cost and investment returns for each period:

	31 March 2021		**31 March 2022**	
	£m	**Average Rate %**	**£m**	**Average Rate %**
Long Term Debt (fixed rates) - PWLB[1]	331	4.63	331	4.63
Long Term Debt (fixed rates) – LOBOS[2]	70	4.09	70	4.09
Long Term Debt (fixed rates) – Market	50	4.04	50	4.04
Short Term Borrowing	-	-	-	-
Total borrowing	**451**	**4.48**	**451**	**4.48**
Investments	207	0.30	237	0.13
Net Borrowing Position	**244**		**214**	

1Public Works Loan Board

2 Lender option Borrower option (LOBO)

9. The total borrowing excludes accrued interest of £5m (£5m at 31/3/21) and the outstanding finance on PFI and service contracts of £125m at 31 March 2021 (£133m at 31/3/21).

10. In addition to the Treasury investments above (£237m), the authority also has
    - long term service investments costing £13m primarily relating to the holdings in Bristol Port Company (£3m) and a property fund to support Homelessness and Temporary Accommodation (£10m), and
    - long term service loans costing £28m, primarily relating to loans to wholly owned subsidiaries £24m and external organisations (£4m).
    - These investments and loans support the delivery of council functions, provide service benefits and have a positive social impact.

11. The Net debt has decreased by £30m from £244m to £214m primarily due to;

- Funding of the capital programme financed by Prudential borrowing +£43m as set out in Appendix 1 para 3.
- Minimum Revenue Provision (MRP) – (£7m)
- Net change in Reserves and provisions +£16m
- Other changes to working capital and balances (£82m)

Long Term Borrowing – Strategy and outturn

12. The 2021–2026 Treasury Strategy (approved 23rd February 2021) identified a net medium term borrowing requirement of £260m to support the existing and future Capital Programme with the debt servicing costs predominately met from revenue savings from capital investment and the economic development fund. The £260m was planned to be borrowed in the following periods, 21/22, £100m, 22/23 - £75m, 23/24 - £30m, 24/25 - £35m and 25/26 - £20m.

13. The Council's Strategy is also to defer borrowing while it has significant levels of liquid treasury investments, £237m at March 2022 (£207m at March 2021). However, the Strategy also considers where the financial environment changes and borrowing is deemed advantageous the Council will seek to borrow over appropriate maturity periods. Deferring borrowing reduces the "net" revenue interest cost of the Authority as well as reducing the Councils exposure to counter party risk for its investments. The Council recognises that utilising investments in lieu of borrowing clearly has a finite duration and that future borrowing will be required to support capital expenditure (see 2021/22 Treasury Management Strategy approved by Council 23rd February 2021).

    https://democracy.bristol.gov.uk/documents/s57091/Appendix%204%20-%20Treasury%20Management%20Strategy%20202122.pdf

14. Borrowing activity in year was in accordance with the Strategy approved at the beginning of the year**:**

    - **Borrowing** – No borrowing was undertaken during the year as the authority maintained higher levels of investments, on average circa £240m, that was higher than anticipated for a variety of reasons including the advance receipt of grants, and the time taken to progress capital schemes where the source of financing was external borrowing.

    - **Rescheduling –** No debt rescheduling activity was undertaken in 2021/22. As set out in the Treasury Mid-Year report the total life cycle cost of rescheduling loans on a discounted cash-flow basis has been reviewed with no loans providing a positive cash-flow benefit to the authority. This would in part be due to the large early repayment penalties that the authority would incur, circa £213m penalty to repay the £331m of PWLB loans early as at 31st March 2022 (the penalty at 31/03/21 was £270m).

Annual Investment Strategy and Outturn

15. Investment returns remained low during 2021/22 due to the low interest rate environment that persisted throughout the year. 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 was clear to the Bank of England that the

emergency level of rates introduced at the start of the Covid-19 pandemic were no longer necessary

The Bank of England and the Government also maintained various monetary and fiscal measures, supplying the banking system and the economy with large amounts of "cheap" credit so that banks could help "cash-starved" businesses to survive the various lockdowns and the associated negative impacts on their cashflow. The Government also supplied large 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 7% in March 2022).

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 in 2008-09. 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.

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. External borrowing would have incurred an additional cost, due to the differential between borrowing and investment rates. Such an approach has also provided benefits in terms of reducing counterparty risk exposure, by having fewer investments placed in the financial markets.

16. Security of capital remained the Council's main investment objective. This was maintained by following the Council's policy for assessing institutions to which the council might lend. 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.).

17. Treasury Investments held by the Council - the Council maintained an average balance of £240m (£194m 2020/21) of internally managed funds. The internally managed funds received an average return of 0.13% (0.30% 2020/21). The comparable performance indicator is the Sterling Overnight Index average (SONIA) 7-day LIBID rate, which was 0.14% so approximately in line with benchmark

Compliance with Treasury Limits and Treasury Related Prudential Indicators

18. The Council can confirm that:

- All treasury related transactions were undertaken by authorised officers and within the limits and parameters approved by the Council;

- All investments were to counterparties on the approved lending list

- The Council operated within the Prudential Indicators within Appendix 1.

Performance Indicators set for 2021/22

19. One of the key requirements in the Code is the formal introduction of performance measurement relating to investments, debt, and capital financing activities. Whilst investment performance criteria have been well developed and universally accepted, debt performance indicators continue to be a more problematic area with the traditional average portfolio rate of interest acting as the main guide. The Council's performance indicators were set out in the Annual Treasury Management Strategy.

20. The following performance indicators have been set:
    - Debt / Borrowing – Average rate of borrowing for the year compared to the average available.
      No borrowing undertaken during the year

    - Investments – Internal returns above the 7 day LIBID rate
      Average rate for the year 0.13% vs. annual average 7 day LIBID of negative 0.04%
      (The Bank of England now recommend the use of the SONIA rate mentioned above). This rate was positive 0.14%)

Consultation and scrutiny input

21. The report has been discussed with the Council's external treasury management advisers and internally with Strategic & Service Directors, and Deputy Mayor – Finance, Governance & Performance.

Risk Assessment

22. The principal risks associated with treasury management are:

Risk	**Mitigation**
Loss of investments as a result of failure of counterparties	Limiting the types of investment instruments used, setting strict lending criteria and only lending to high quality counterparties, and limiting the extent of exposure to individual counterparties
Increase in the net financing costs of the authority due to borrowing at high rates of interest / lending at low rates of interest	Planning and undertaking borrowing and lending in light of assessments of future interest rate movements, and by undertaking most long term borrowing at fixed rates of interest (to reduce the volatility of capital financing costs)

Public sector equality duties:

23. There are no proposals in this report, which require either a statement as to the relevance of public sector equality duties or an Equalities Impact Assessment.

Environmental checklist / eco impact assessment

24. There are no proposals in this report which have environmental impacts

Legal and Resource Implications

25. Legal- the Council is under a duty to manage its resources prudently and therefore due consideration must always be given to its borrowing and lending strategy. A wide range of local authority financial activities, including borrowing, lending, financial management, and the approval of types of investment vehicle are governed by legislation and various regulations. The Council is obliged to comply with these.

    Advice provided by Tim O'Gara (Service Director: Legal and Democratic Services)

Financial

(a) Revenue

26. The financing costs arising from planned borrowing are provided for in the revenue budget and medium term financial plan.

    Advice given by Jon Clayton (Capital and Investment Manager)

(b) Capital

27. There is no direct capital investment implications contained within this report.

Land

28. There are no direct implications for this report.

Personnel

29. There are no direct implications for this report.

Appendices:

Appendix 1: Treasury Management Annual Report 2021/22

LOCAL GOVERNMENT (ACCESS TO INFORMATION) ACT 1985

Background Papers:

30. Treasury Management Strategy 2021/22
https://democracy.bristol.gov.uk/documents/s57091/Appendix%204%20-%20Treasury%20Management%20Strategy%20202122.pdf

Appendix 1

Annual Report on the Treasury Management Service 2021/22 (Incorporating Outturn Prudential Indicators)

Introduction

1. This report summarises:

   - The capital activity during the year
   - What resources the Council applied to pay for this activity;
   - The impact of this activity on the Council's underlying indebtedness (the Capital Financing Requirement);
   - The reporting of the required prudential indicators;
   - Overall treasury position identifying how the Council has borrowed in relation to this indebtedness, and the impact on investment balances;
   - A summary of interest rate movements in the year;
   - The detailed debt activity;
   - The detailed investment activity;
   - Local Issues

The Council's Capital Expenditure and Financing 2020/21

2. The Council undertakes capital expenditure to invest in the acquisition and enhancement of 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.

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

	2020/21 Actual £m	2021/22 Original Budget £m	2021/22 P9 - Final Budget £m	2021/22 Actual £m
Non-HRA capital expenditure	127*1	210	151	119*1
HRA capital expenditure	39	111	53	39
Total capital expenditure	**166**	**321**	**204**	**158**
Resourced by:				
Capital receipts	35	86		17
Capital grants	74	106		65
HRA Self Financing	22	40		29
Prudential borrowing	30	77		43
Revenue	4	12		3
Service Concession Contract – Waste Vehicles*1	1	-		1
Total Resources	**166**	**321**		**158**

*1 – Technical accounting adjustment required for Waste Service Concession Contract in accordance with International Financial Reporting Standards.

The Council's Overall Borrowing Need

4. The Council's underlying need to borrow is called the Capital Financing Requirement (CFR). This figure is a gauge of the Council's debt position. It represents 2021/22 and prior years' net capital expenditure that has not yet been paid for by revenue or other resources.

5. Part of the Council's treasury activities is to address this borrowing need, either through borrowing from external bodies, or utilising temporary cash resources within the Council.

6. Reducing the CFR – Whilst under treasury management arrangements actual debt can be borrowed or repaid at any time within the confines of the annual treasury strategy, the Council is required to make an annual revenue charge to reduce the CFR – effectively a repayment of the Non-Housing Revenue Account (HRA) borrowing need. There is no statutory requirement to reduce the HRA CFR.

7. This statutory revenue charge is called the Minimum Revenue Provision - MRP. The total CFR can also be reduced by:

- the application of additional capital resources (such as unapplied capital receipts); or
- charging more than the statutory revenue charge (MRP) each year through a Voluntary Revenue Provision (VRP).

8. The Council's 2021/22 MRP Policy (as required by CLG Guidance) was approved on the 25th February 2021.

9. The Council's CFR for the year is shown below, and represents a key prudential indicator. Accounting rule changes in previous years has meant that PFI schemes are now included on the balance sheet, which increases the Council's borrowing need, the CFR. No borrowing is actually required against these schemes as a borrowing facility is included in the contract.

CFR	General Fund 31 March 2021 Actual £m	General Fund 31 March 2022 Actual £m	HRA 31 March 2021 Actual £m	HRA 31 March 2022 Actual £m	Total CFR 31 March 2022 Actual £m
Opening balance	**625**	**641**	**245**	**245**	**886**
Add unfinanced capital expenditure (as above)	30	43	-	-	43
Less MRP/VRP	(5)	(5)	-	-	(5)
Less application of Capital Resources	(1)	(2)			(2)
PFI, Service Concession and finance lease adjustments	(8)	(8)	-	-	(8)
Closing balance	**641**	**669**	**245**	**245**	**914**

Treasury Position at 31 March 2022

10. Whilst the Council's gauge of its underlying need to borrow is the CFR, Finance can manage the Council's actual borrowing position by either:

- Borrowing to the CFR; or
- Choosing to utilise some temporary internal cash flow funds in lieu of borrowing or
- Borrowing for future increases in the CFR (borrowing in advance of need).

11. The figures in this report are based on the principal amounts borrowed and invested and so may differ from those in the final accounts by items such as accrued interest.

	31 March 2021		31 March 2022	
	Principal £m	**Average Rate %[2]**	**Principal £m**	**Average Rate %[2]**
Fixed Interest Rate Debt	331	4.63	331	4.63
Variable Interest Rate Debt	-	-	-	-
Market Debt – LOBO[1]	70	4.09	70	4.09
Market Debt	50	4.04	50	4.04
PFI / Service Contracts	133	-	125	-
Total Debt	**584**	**4.48**	**576**	**4.48**
Debt administered of behalf of Unitary Authorities (Ex Avon Debt)	(39)	-	(38)	-
Revised Debt	545	4.48	538	4.48
Capital Financing Requirement	886		914	
Over/(Under) borrowing	(341)		(376)	
Investment position				
Investments (Fixed & Call)	207	0.30	237	0.13
Net borrowing position (excl leasing arrangements)	**244**	**-**	**214**	**-**

1 Lender option Borrower option (LOBO) , 2 reflect the average rate for the year taking account of new loans and repayments.

12. The fixed Interest rate debt is apportioned between the General Fund and HRA as set out in the table below.

Fixed Interest Rate Debt	**31 March 2021 £m**		**31 March 2022 £m**	
	Principal £m	**Average Rate%**	**Principal £m**	**Average Rate%**
General Fund	211	4.26	211	4.26
HRA	245	4.68	240	4.68
Total	456	4.48	451	4.48

13. The maturity structure of the debt portfolio (excluding accrued interest) was as follows:

	Approved Min Limit%	**Approved Max Limit%**	**31 March 2021**		**31 March 2022**	
			Actual £m	**%**	**Actual £m**	**%**
Under 12 Months	0	20	-	-	5	1
1 to 2 years	0	20	5	1	-	-
2 to 5 years	0	40	20	4	32	7
5 to 10 years	0	40	34	8	22	5
10 years and over	25	100	392	87	392	87
Total			**451**	**100**	**451**	**100**

14. The Council hold £70m of LOBOS with maturities averaging 39 years. Inherent within these loan instruments are options (averaging an option every 3.5 years) that could give rise to the debt being repaid early. These loans are regularly reviewed with the current and expected structure of interest rates. The risk of the lenders exercising their options was currently low for the short to medium term based on the interest rates as at the 31st March 2022. Therefore, the maturity of these loans in the above table is based on their maturity date, 10 years and over.

    However, with the current rising interest environment it is anticipated that there may be opportunities to refinance these loans over the short to medium term.

15. The Council will continually review these loans in accordance with economic forecasts and will update the maturity structure of the debt portfolio accordingly and assess the future re-financing risks and opportunities exposed to the authority and report any changes within future monitoring reports.

16. The authority's borrowing strategy is to delay borrowing and use its existing resources to support the Capital Programme to reduce its exposure to counterparty risk and the net interest cost of the authority (cost of carry). The authority, as planned, did not undertake further borrowing while the authority maintained higher levels of investments than originally anticipated. This was due to a variety of reasons including the receipt of grants in advance and the time taken to progress capital schemes where the source of financing was external borrowing.

17. If it had been felt that there was a significant risk of a much sharper RISE in long and short term rates than expected, perhaps arising from an acceleration in bank rate, an increase in world economic activity or a sudden increase in inflation risks, then further borrowing would have been considered. Most likely, further fixed rate funding would have been drawn whilst interest rates were lower than they were projected to be over the short to medium term.

18. Interest rate forecasts expected only gradual rises in medium and longer-term fixed borrowing rates during 2021/22 and the two subsequent financial years until the turn of the year, when inflation concerns increased significantly. This change in interest rate forecasts is reflected in the table below (para 24)

Prudential Indicators and Compliance Issues

19. Some of the prudential indicators provide either an overview or specific limits on treasury activity. These are shown below:

20. **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 over the medium term. This essentially means that the Council is not borrowing to support revenue expenditure. The table below highlights the Council's gross borrowing position against the CFR. The Council has complied with this prudential indicator.

	31 March 2021 Actual £m	31 March 2022 Actual £m
Gross borrowing position	451	451
CFR (excluding PFI)	753	789

21. **The Authorised Limit** - The Authorised Limit is the "Affordable Borrowing Limit" required by Section 3 of the Local Government Act 2003. Once agreed the authorised limit cannot be breached. The Council does not have the power to borrow above this level. The table below demonstrates that during 2021/22 the Council has maintained gross borrowing within its Authorised Limit.

22. **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 is acceptable subject to the Authorised Limit not being breached.

23. **Actual financing costs as a proportion of net revenue stream** - This indicator identifies the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

	2021/22 £m
Authorised Limit	1,000
Operational Boundary	693
Average gross borrowing position (including PFI)	580
Financing costs as a proportion of net revenue stream: General Fund HRA	 6.60% 9.00%

Borrowing Rates in 2021/22

24. Gilt yields fell sharply from the spring of 2021 through to September and then picked back up before falling again through December. However, by the turn of the calendar year markets became focussed inflation, following the opening of economies post the pandemic, and rising commodity and food prices resulting from the Russian invasion of Ukraine.

    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%.

    The margin over gilt yields for the City Council to borrow from the Public Works Loan Board (PWLB) is the is a gilt plus 80 basis points.

    At the end of March rates were forecast to rise in short dated gilt yields and PWLB rates over the next three years as Bank Rate was forecast to rise from 0.75% in March 2022 to 1.25% during the next financial year. Medium and long dated yields were also forecast to rise

modestly over the short to medium term but recognised concerns around the impact from Quantitative Tightening when Bank Rate hits 1% and inflation post the pandemic.

Forecast Interest rates as at 7th February 2022

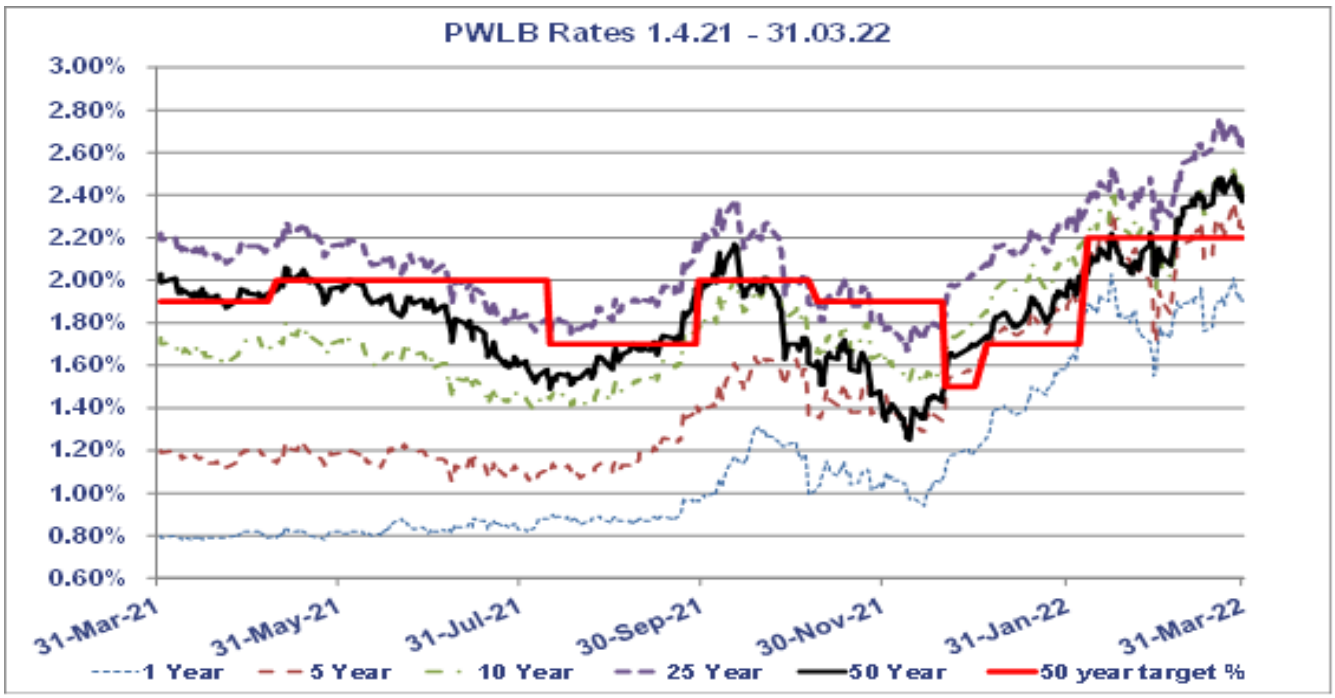
Period	Bank Rate %	PWLB Borrowing Rates % (including certainty rate adjustment)			
		5 year	10 Year	25 year	50 year
Mar 2022	0.75	2.20	2.30	2.40	2.20
Mar 2023	1.25	2.30	2.40	2.60	2.40
Mar 2024	1.25	2.30	2.40	2.60	2.40
Mar 2025	1.25	2.30	2.40	2.60	2.40

The latest forecast indicates that rates will rise faster and higher than originally forecast, as detailed in the table below, with further details to be included in the Treasury Management mid-year report.

Forecast Interest rates as at 15th September 2022

Period	Bank Rate %	PWLB Borrowing Rates % (including certainty rate adjustment)			
		5 year	10 Year	25 year	50 year
Oct 2022	2.25	2.80	3.00	3.40	3.10
Mar 2023	2.75	3.10	3.30	3.50	3.20
Mar 2024	2.50	2.90	3.10	3.40	3.10
Mar 2025	2.25	2.80	2.90	3.20	2.90

The impact on PWLB rates during the financial year ending the 31st March 2022 is highlighted in the graph below.



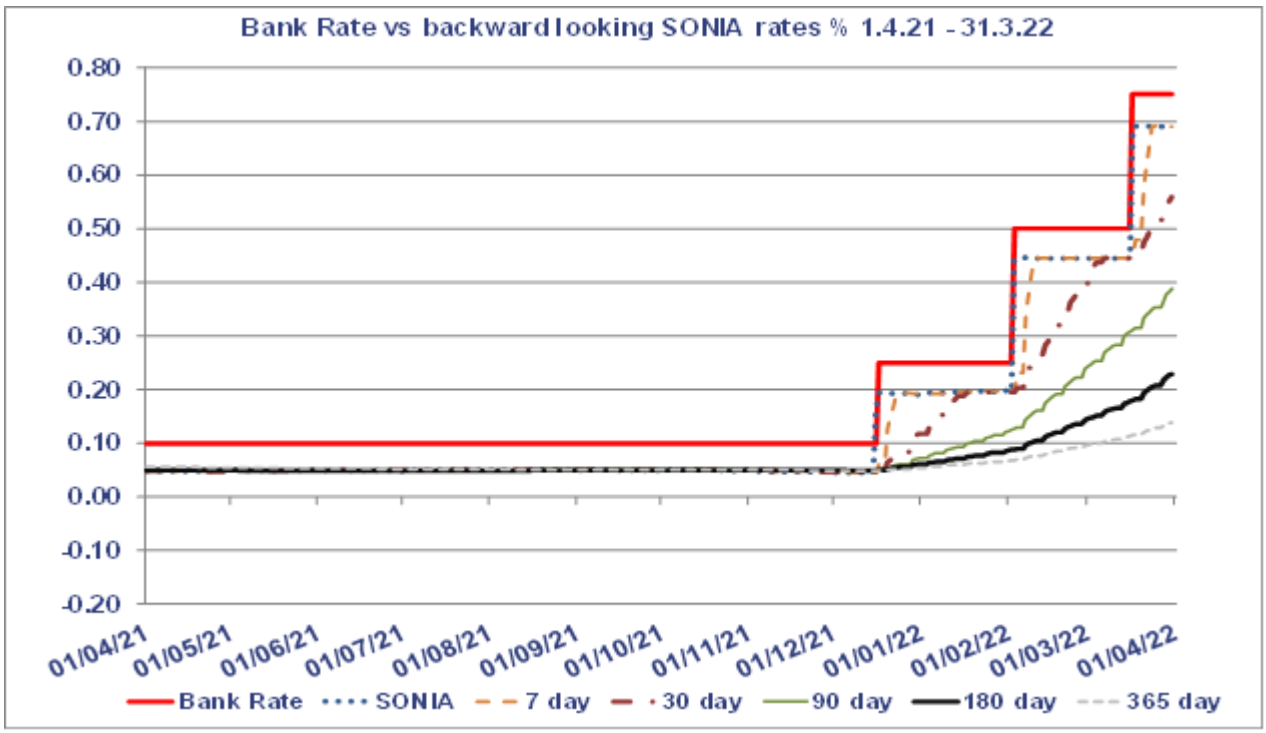
25. **Summary of Debt Transactions –** The authority did not have any loans scheduled to be repaid during year and to avoid increased counterparty risk along with low investment returns no borrowing was undertaken during the year. (So internal borrowing was used utilising the Council's cash balances)

26. The average rate of interest for the debt portfolio is 4.48%.

Investment Rates in 2021/22

27. Investment returns remained close to zero during 2021/22. The expectation for interest rates within the treasury management strategy for 2021/22 was that Bank Rate would remain at 0.10% and remain at this level until it was clear to the Bank of England that the emergency level of rates introduced at the start of the Covid-19 pandemic were no longer needed.

    The impact on investment rates is highlighted in the graph below.



	Bank Rate	SONIA	7 day	30 day	90 day	180 day	365 day
High	0.75	0.69	0.69	0.56	0.39	0.23	0.14
High Date	17/03/2022	18/03/2022	25/03/2022	31/03/2022	31/03/2022	31/03/2022	31/03/2022
Low	0.10	0.05	0.05	0.05	0.05	0.05	0.05
Low Date	01/04/2021	15/12/2021	16/12/2021	16/12/2021	16/12/2021	07/06/2021	13/12/2021
Average	0.19	0.14	0.13	0.12	0.09	0.07	0.06
Spread	0.65	0.65	0.65	0.51	0.34	0.18	0.09

28. The Council's investment policy is governed by Department for Levelling Up, Housing and Communities (DLUHC) guidance, which has been implemented in the annual investment strategy approved by the Council on 23rd 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.).

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

Local Issues

29. **Ethical and Equitable Investment Policy –** A refreshed "Ethical Equitable Investment Policy" was approved by Cabinet on the 18th January 2022. The Council approved their first policy, known as the Ethical Investment Policy on the 15th December 2011 that was subsequently updated in February 2015. It should be noted that there have been no breaches during the year.

Regulatory Framework, Risk and Performance

30. The Council's treasury management activities are regulated by a variety of professional codes and statutes and guidance:

    - The Local Government Act 2003 (the Act), which provides the powers to borrow and invest as well as providing controls and limits on this activity;
    - The Act permits the Secretary of State to set limits either on the Council or nationally on all local authorities restricting the amount of borrowing which may be undertaken (although no restrictions have been made);
    - Statutory Instrument (SI) 3146 2003, as amended, develops the controls and powers within the Act;
    - The SI requires the Council to undertake any borrowing activity with regard to the CIPFA Prudential Code for Capital Finance in Local Authorities;
    - The SI also requires the Council to operate the overall treasury function with regard to the CIPFA Code of Practice for Treasury Management in the Public Services;
    - Under the Act the DLUHC has issued Investment Guidance to structure and regulate the Council's investment activities.
    - Under section 238(2) of the Local Government and Public Involvement in Health Act 2007 the Secretary of State has taken powers to issue guidance on accounting practices. Guidance on Minimum Revenue Provision was issued under this section on 8th November 2007 and further amendments have been made since, the most recent being February 2018. It should also be noted that this provision is currently being reviewed and consulted upon as referred in previous treasury reports.

31. The Council has complied with all of the above relevant statutory and regulatory requirements which require the Council to identify and, where possible, quantify the levels of risk associated with its treasury management activities. In particular its adoption and implementation of both the Prudential Code and the Code of Practice for Treasury Management means both that its capital expenditure is prudent, affordable and sustainable, and its treasury practices demonstrate a low risk approach.

32. The Council has ensured that the principles of security, liquidity and yield (in that order) have been adhered to within the treasury operation. This implies that the safeguarding of the principal investment with a suitable high quality counterparty remains the Council's highest priority followed by liquidity (i.e. ease of access to the principal amount deposited) and yield (i.e. return) on investment.