

Committee Name and Date of Committee Meeting

Audit Committee – 29 November 2022

Report Title

Mid-Year Treasury Management and Prudential Indicators Monitoring Report – 2022/23

Is this a Key Decision and has it been included on the Forward Plan?

No

Strategic Director Approving Submission of the Report

Judith Badger, Strategic Director of Finance and Customer Services

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Ward(s) Affected

Borough-Wide

Report Summary

Mid-Year Treasury Review

The regulatory framework of treasury management requires that the Council produces a mid-year treasury review, in addition to the forward looking annual treasury strategy and backward looking annual treasury outturn report.

This report is the mid-year review for 2022/23. It also incorporates the needs of the Prudential Code to ensure adequate monitoring of the capital expenditure plans and the Council's prudential indicators (PIs).

It is also a requirement that any proposed changes to the 2022/23 prudential indicators are approved by Council.

The monitoring as set out in the Appendix to the report is structured to highlight the key changes to the Council's capital activity (the PIs) and the actual and proposed treasury management activity (borrowing and investment).

Recommendations

1. Audit Committee is asked to note the contents of the report.

List of Appendices Included

Appendix – Mid-Year Treasury Management and Prudential Indicators Monitoring Report – 2022/23.

Background Papers

Budget and Council Tax Setting Report 2022/23 to Council on 2nd March 2022, Including the Treasury Management Strategy 2022/23

Consideration by any other Council Committee, Scrutiny or Advisory Panel

No.

Council Approval Required

No

Exempt from the Press and Public

No.

1.	Background
1.1	Mid-Year Treasury Review – The CIPFA Treasury Management Code of Practice includes a requirement that Members receive a mid-year treasury review, in addition to the forward looking annual treasury strategy and backward looking annual treasury report required previously.
1.2	This review as fully set out in the Appendix meets these requirements. It also incorporates the needs of the Prudential Code to ensure adequate monitoring of the capital expenditure plans and the Council’s prudential indicators (PIs). The Treasury Management Strategy and PIs were previously reported to Cabinet on 14 th February 2022 and approved by Council on 2nd March 2022.
2.	Key Issues
2.1	Mid-Year Treasury Review – The review as set out in the Appendix provides Members with details of mid-year performance against the plan.
2.2	<p>a. Investments - the primary governing principle remains security over return and the criteria for selecting counterparties continues to reflect this.</p> <p>b. Borrowing – The Council will maintain it’s strategy of being under-borrowed against the capital financing requirement. The Council borrowed £227m of long term PWLB funds during 2021/22 to take advantage of the low PWLB interest rates available at the time. This was replacing short term borrowing as it matured. No borrowing has taken place during 2022/23 as the Council has cash balances remaining from the borrowing taken in 2021/22, that it has been able to invest a on short term basis to generate additional income for the Council. Making use of the current financial market conditions, which have lifted investment returns.</p> <p>Crucially, it is not expected that the Council will need to borrow any funds for the remainder of the 2022/23 financial year. This is helpful given borrowing rates have risen significantly during 2022/23 and are expected to peak in December 2022 before falling during 2023/24. As a result the Council has made significant savings on borrowing costs, against the plan set out in the Medium Term Financial Strategy, as the Council has not been required to borrow in the current high interest rate market. Moving forwards the Council will use a short term borrowing strategy if any borrowing is required, to mitigate costs. The borrowing position will remain under review and an update of the strategy will be presented to Members within the Budget and Council Tax 2023/24 report to Council in March 2023.</p> <p>c. Governance - strategies and monitoring are reviewed by Audit Committee.</p> <p>d. Whilst the Council’s approach to Treasury Management in recent years, utilising short term borrowing in particular, has generated significant savings for the Council, essential to achieving balanced budgets, the future outlook is more challenging. With increasing interest rates for borrowing, as a result of the increases in the Bank of England Base Rate, when the Council does need to borrow, it will be at much higher levels</p>

	<p>than had been assumed in the Council's approved Medium Term Financial Strategy. The increases in borrowing rates could not have been projected by the Council and work is underway to plan how the Council can best navigate through the current challenges presented by the financial markets. It should be noted that it is expected that borrowing rates will reduce over the next couple of years, linked to the projections that inflation will return back to the Bank of England's target 2% level.</p>
3.	Options considered and recommended proposal
3.1	Mid-Year Treasury Review – The review as set out in the Appendix indicates performance is in line with the plan and no proposals to vary the approach for the remainder of the year are proposed.
4.	Consultation on proposal
4.1	The continuing approach to treasury management has been discussed with the Council's external Treasury Management Advisers, Link Asset Services, who have confirmed this is a prudent approach given current market conditions. Link Asset Services will continue to monitor borrowing rates and inform the Council if there are opportunities to borrow at advantageous rates.
5.	Timetable and Accountability for Implementing this Decision
5.1	The report is for Audit Committee information and noting.
6.	Financial and Procurement Advice and Implications
6.1	Treasury Management forms an integral part of the Council's overall financial arrangements.
6.2	The assumptions supporting the capital financing budget for 2022/23 and for future years covered by the Council's MTFs were reviewed in light of economic and financial conditions and the capital programme.
6.3	The current strategy is to maintain the Council's position of being under-borrowed against the Capital Financing Requirement. Due to the PWLB borrowing taken out in 2021/22 it is not anticipated that any further borrowing will be required during 2022/23, as a result the Council will make significant savings on borrowing costs during 2022/23, whilst also making greater investment returns through having greater cash balances to invest. The Council will continue to seek opportunities to convert its short term borrowing into long term when PWLB rates allow. Given the significant increases in interest rates during 2022/23 this is not currently possible, but rates are forecast to fall during 2023/24. Therefore, this remains under review given that market conditions can fluctuate significantly, a further update will be provided as part of the Council's Treasury Management Strategy for 2023/24.
6.4	There are no direct procurement implications arising from this report.

7.	Legal Advice and Implications
7.1	It is a requirement that changes to the Council's prudential indicators are approved by Council
8.	Human Resources Advice and Implications
8.1	There are no Human Resource implications arising from the report.
9.	Implications for Children and Young People and Vulnerable Adults
9.1	The report does not impact the Children's and Adult Social care budgets.
10.	Equalities and Human Rights Advice and Implications
10.1	There are no implications arising from this report to Equalities and Human Rights.
11.	Implications for CO2 Emissions and Climate Change
11.1	No direct implications.
12.	Implications for Partners
12.1	There are no implications arising from this report to Partners or other directorates.
13.	Risks and Mitigation
13.1	Regular monitoring of treasury activity ensures that risks and uncertainties are addressed at an early stage and hence kept to a minimum.
14.	Accountable Officers
	Rob Mahon, Assistant Director Financial Services
	Owen Campbell, Head of Corporate Finance

Mid-Year Prudential Indicators and Treasury Management Monitoring

1. Introduction and Background

- 1.1 The CIPFA Treasury Management Code of Practice includes a requirement that the Council receive a mid-year treasury review, in addition to the forward looking annual treasury strategy and backward looking annual treasury report required previously.
- 1.2 This report meets that requirement. It also incorporates the needs of the Prudential Code to ensure adequate monitoring of the capital expenditure plans and the Council's prudential indicators (PIs). The Treasury Management Strategy and PIs for 2022/23 were previously reported to Cabinet on 14th February 2022 and approved by Council on 2nd March 2022.
- 1.3 The Council's revised capital expenditure plans and the impact of these revised plans on its financing are set out below in Sections 2.2 and 2.3 respectively. The Council's capital spending plans provide a framework for the subsequent treasury management activity. Section 3 onwards sets out the impact of the revised plans on the Council's treasury management indicators.
- 1.4 The underlying purpose of the report supports the objective in the CIPFA Code of Practice on Treasury Management and the Communities & Local Government Investment Guidance. This states that Members receive and adequately scrutinise information on the treasury management service.
- 1.5 The underlying economic and financial environment remains difficult for the Council. On investment the main challenge relates to concerns over investment counterparty risk. This background encourages the Council to continue maintaining investments short term and with low risk counterparties. The Bank of England base rate has risen from 0.75% to 3% during 2022/23 which has significantly increased the interest available on investments.
- 1.6 The Council's use of long term PWLB borrowing during 2021/22 (£227m) resulted in the level of short term borrowing gradually falling as short term borrowing matured. With the Council carrying this £227m, there was no requirement for the Council to borrow during 2022/23 whilst rates have soared. Allowing the Council to temporarily reduce borrowing costs, through reliance on cash borrowed during 2021/22. This has provided certainty of borrowing costs and mitigated the risk of borrowing having to be taken in the future at higher rates.
- 1.7 PWLB rates fluctuate, during 2022/23 to date the rates have seen highs of 5.5% for a 50 year PWLB loan and lows of 2.42% with the 50 year rate currently standing at 3.87%. These are the highest rates for a number of years. This further emphasises the positive deals that the Council took during 2021/22, with the £227m being borrowed at an average of 1.53%. Short term borrowing rates have also increased with 6 month borrowing rates standing at around 3.1%, compared with 0.02% in September 2021 This has not affected the Council's borrowing costs during 2022/23 as no borrowing has been taken and rates have

not changed on existing loans. The Council keeps interest rates under constant review within its borrowing strategies and decisions on the mix of long-term and short-term borrowing.

- 1.8 The Strategic Director Finance & Customer Services can report that the basis of the Treasury Management Strategy, the Investment Strategy and the PIs have not changed from that set out in the approved Treasury Management Strategy (Council March 2022).

2. **Key Prudential Indicators**

- 2.1. This part of the report is structured to update:

- The Council's latest capital expenditure plans;
- How these plans are being financed;
- The impact of the changes in the capital expenditure plans on the PIs and the underlying need to borrow; and
- Compliance with the limits in place for borrowing activity.

2.2 **Capital Expenditure (PI)**

- 2.2.1 This table shows the current forecast estimates for capital expenditure. This position reflects slippage on the capital programme and new scheme approvals during the year.

Capital Expenditure by Service	2022/23 Original Estimate £m	2022/23 Revised Estimate £m
Children and Young People's Services	11.051	13.789
Assistant Chief Executive	0.210	0.496
Adult Care & Housing	6.065	7.659
Finance and Customer Services	7.609	7.739
Regeneration and Environment	148.567	99.892
Capitalisation Direction	6.000	1.000
Total Non-HRA	179.502	130.575
Adult Care & Housing – HRA	65.272	43.272
Total HRA	65.272	43.272
Total	244.774	173.847

2.3 **Impact of Capital Expenditure Plans**

2.3.1 **Changes to the Financing of the Capital Programme**

The table below draws together the main strategy elements of the capital expenditure plans (above), highlighting the expected financing arrangements of this capital expenditure.

Capital Expenditure	2022/23 Original Estimate £m	2022/23 Revised Estimate £m
Total spend	244.774	173.847
Financed by:		
Capital receipts	11.528	5.697
Capital grants, capital contributions & other sources of capital funding	152.453	111.964
Borrowing Need	80.793	56.186
Total Financing	244.774	173.847
Unsupported Borrowing	80.793	56.186
Borrowing Need	80.793	56.186

The borrowing element of the table increases the underlying indebtedness of the Council by way of the Capital Financing Requirement (CFR), although this will be reduced in part by revenue charges for the repayment of debt (the Minimum Revenue Provision (MRP)). This direct borrowing need may also be supplemented by maturing debt and other treasury requirements.

2.3.2 The decrease in borrowing need for 2022/23 (£24.607m) reflects the re-profiling of capital expenditure & financing.

2.3.3 **Changes to the Capital Financing Requirement (PI), External Debt and the Operational Boundary (PI)**

The table below shows the CFR, which is the underlying external need to borrow for a capital purpose. It also shows the expected debt position over the period. This expected debt position has previously been used as the basis for the Operational Boundary PI. This was set at the beginning of the financial year at £945.559m. There may be periods where the actual position rises above the Operational Boundary, but this is acceptable practice. It is the Authorised Limit which the Council must not breach. It is not expected that the Operational Boundary will be breached. The Council will continue to use a combination of long and short term borrowing and remain under-borrowed.

2.3.4 In addition to showing the underlying need to borrow, the Council's CFR includes other long term liabilities which have been brought on balance sheet, for example, PFI schemes and finance lease assets. No borrowing is actually required against these schemes as a borrowing facility is already included in the contract and there has been no change in the borrowing need resulting from these requirements.

2.3.5 The current CFR estimate for 2022/23 is £904.706m and this figure represents an increase of £47.770m when compared to the 2021/22 year-end position of £856.936m. The increase is predominantly due to reflecting the Councils approved Capital Programme within the revised CFR estimate, a further

adjustment is made to reflect the repayments of borrowing within PFI schemes. These two adjustments are detailed below;

- The estimated borrowing need for the year £56.186m net of the Minimum Revenue Provision charge for the year (£4.796m)
- The repayments of borrowing contained within PFI and similar schemes (£3.620m).

Prudential Indicator – Capital Financing Requirement	2022/23 Original Estimate £m	2022/23 Revised Estimate £m
CFR – Non Housing	510.575	479.376
CFR – Housing	320.876	308.447
Total CFR excluding PFI, finance leases and similar arrangements	831.451	787.823
Net movement in CFR excluding PFI, finance leases and similar arrangements	95.018	51.390
Cumulative adjustment for PFI, finance leases and similar arrangements	116.883	116.883
Net movement in CFR	-3.620	-3.620
Total CFR including PFI, finance leases and similar arrangements	948.334	904.706
Net movement in overall CFR	91.398	47.770
Prudential Indicator – Operational Boundary	Original Estimate	Current Position
Borrowing	828.676	783.945
Other long term liabilities*	116.883	116.883
Total Debt 31 March	945.559	900.828

* Includes on balance sheet PFI schemes, finance leases and similar arrangements, etc.

3. Limits to Borrowing Activity

- 3.1 The first key control over the treasury activity is a PI to ensure that over the medium term, gross and net borrowing will only be for a capital purpose. Gross and net external borrowing should not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional CFR for 2022/23 and next two financial years. This allows some flexibility for limited early borrowing for future years. The Council has approved a policy for

borrowing in advance of need which would only be undertaken if this proves prudent to do so.

RMBC	2022/23 Original Estimate £m	2022/23 Revised Estimate £m
Gross Borrowing	798.676	753.945
Plus Other Long Term liabilities*	116.883	116.883
Total Gross Borrowing	915.559	870.828
CFR*	948.334	904.706
Total Gross Borrowing	915.559	870.828
Less Investments	50.000	50.000
Net Borrowing	865.559	820.828
CFR*	948.334	904.706

* Includes on balance sheet PFI schemes, finance leases and similar arrangements, etc.

- 3.2 The Strategic Director for Finance & Customer Services reports that no difficulties are envisaged for the current or future years in complying with this PI.
- 3.3 A further PI controls the overall level of borrowing. This is the Authorised Limit which represents the limit beyond which borrowing is prohibited, and needs to be set and revised by Members. It is the expected maximum borrowing need with some headroom for unexpected movements. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Council does not expect to breach this limit.

Authorised limit for external debt (RMBC)	2022/23 Original Indicator £m	2022/23 Revised Indicator £m
Borrowing	851.451	807.823
Other long term liabilities*	119.221	119.221
Total	970.672	927.044

* Includes on balance sheet PFI schemes, finance leases and similar arrangements, etc.

4. Treasury Strategy 2022/23

4.1 Debt Activity during 2022/23

4.1.1 The expected borrowing need is set out below:

RMBC	2022/23 Original Estimate £m	2022/23 Revised Estimate £m
CFR	948.334	904.706
Less Other Long Term Liabilities*	116.883	116.883
Net Adjusted CFR (y/e position)	831.451	787.823
Borrowed at 30/09/22	758.280	721.274
Invested at 30/09/22	-50.000	-172.950
Under borrowing at 30/09/22	123.172	239.499
Borrowed at 30/09/22	758.280	721.274
Estimated additional borrowing to be taken October to March 2023	0.000	0.000
Total Borrowing	758.280	721.274
Under borrowing at 31/03/23	73.171	66.549
Level of short term borrowing as 31/3/23		56.000

* Includes on balance sheet PFI schemes, finance leases and similar arrangements, etc.

4.1.2 The Council is currently significantly under-borrowed. The delay in borrowing long-term reduces the cost of carrying borrowed monies when yields on investments are low relative to the borrowing rates. Based on current borrowing rates and investment returns the differential is around 1.17% and if the Council was fully borrowed the additional cost per year would amount to over £1.4m (Under borrowing and ST borrowing X 1.17%). The delay in taking out new long-term borrowing does give rise to an element of interest rate risk as longer term borrowing rates may rise. The Council borrowed £227m from the PWLB during 2021/22 to take advantage of low interest rates and mitigate some of this risk. Given that the bank base rate has increased over the current year this position is being closely monitored and the overall position carefully managed.

4.1.3 During the six months to 30 September 2022 the Council has not taken out any new borrowing. This is due to the long term PWLB borrowing taken out in 2021/22 which is replacing the temporary borrowing as the temporary borrowing matures. The level of short term borrowing is lower than in the previous year due to this policy of taking long term borrowing to replace the short term borrowing.

4.1.4 During the six months to 30 September 2022, the Council has repaid principal on long term maturity, Equal Instalment of Principal (EIP) and annuity loans from the PWLB, and short-term loans from the Local Authority lending market. The principal repaid, and interest rates are detailed in the table below.

The PWLB EIP loan of £1.3m is being repaid in equal half yearly instalments of £65,000 over its 10 year term. The final payment was made on 09/07/22 when the loan matured. There are 5 Annuity loans on which variable amounts of principal are repaid each six months.

Lender	Principal	Type	Interest Rate %
PWLB (10 year loan)	£2,800,000	Fixed Rate (Maturity)	3.22
PWLB	£65,000	Fixed rate (EIP)	1.89
PWLB	£101,950	Fixed rate (Annuity)	Various
Local Authority	£10,000,000	Temp	0.25
Local Authority	£10,000,000	Temp	0.25
Local Authority	£8,000,000	Temp	0.25
Local Authority	£5,000,000	Temp	0.20
Local Authority	£10,000,000	Temp	0.10

5. Investment Strategy 2022/23

5.1 Key Objectives

The primary objective of the Council's Investment Strategy is safeguarding the repayment of the principal and interest of its investments on time – the investment return being a secondary objective. The current difficult economic and financial climate has heightened the Council's over-riding risk consideration with regard to "Counterparty Risk". As a result of these underlying market concerns, officers continue to implement an operational investment strategy which maintains the tight controls already in place in the approved Investment Strategy.

5.1.1 To mitigate the risk of interest rates rising and to take advantage of low long term PWLB interest rates £227m of PWLB borrowing was taken in the 2021/22 financial year. This has resulted in the Council having a larger cash balance than usual. This cash balance is reducing as temporary borrowing becomes due for repayment.

5.1.2 The Council has been managing any cash surpluses into one of the following investment options, Debt Management Office (DMO currently at 2.7%), Bank Deposits (e.g. Goldman Sachs, currently 3.05%) and Other Local Authorities

(currently 2.73%). The Council has continued to use Money Market Funds (MMF's), which currently have interest rates of between 2.76% and 2.95%. The process for using MMF's is very efficient and effective, with the added benefit that the funds the Council can access are all AAA rated. Investment rates have risen significantly during 2022/23 due to the increase in the Bank of England base rate. The Council is also looking to place funds with other banks/building societies in order to gain more interest and reduce the cost of carry of the funds that have been borrowed.

5.2 **Current Investment Position**

The Council held £172.950m of investments at 30 September 2022, and the constituent parts of the investment position are:

Sector	Country	Up to 1 year £m	1 - 2 years £m	2 – 3 years £m
Banks	UK	10.000	0	0
DMO	UK	9.500	0	0
Local Authorities	UK	77.000	0	0
MMF's	UK	76.450	0	0
Total		172.950	0	0

5.3 **Risk Benchmarking**

A regulatory development is the consideration and approval of security and liquidity benchmarks. Yield benchmarks are currently widely used to assess investment performance. Discrete security and liquidity benchmarks are requirements to Member reporting and the following reports the current position against the benchmarks:

5.3.1 **Security** – The Council monitors its investments against historic levels of default by continually assessing these against the minimum criteria used in the Investment Strategy. The Council's approach to risk, the choice of counterparty criteria and length of investment ensures any risk of default is minimal when viewed against these historic default levels.

5.3.2 **Liquidity** – In respect of this area the Council set liquidity facilities/benchmarks to maintain:

- Bank overdraft – on a day-to-day basis the Council works to an agreed overdraft limit of £100,000 with the Council's bankers. Whilst a short-term increase could be negotiated less expensive short-term borrowing is accessed through the financial markets to remain within the agreed overdraft.
- Liquid short-term deposits of at least £3m available within a week's notice.

The Strategic Director for Finance & Customer Services can report that liquidity arrangements were adequate during the year to date.

5.3.3 **Yield** – a local measure for investment yield benchmark is internal returns above the Overnight Sterling Overnight Index Average (SONIA).

The Strategic Director for Finance & Customer Services can report that the return to date averages 0.77%, against an average Overnight SONIA to the end of September 2022 of 1.22%. This is because some of the investments were placed in 2021/22 when interest rates were much lower. This has reduced the average return.

Based on the Council's current average cash investments of £217m, the additional return achieved at the benchmark rate would be £978k.

6. Revisions to the Investment Strategy

- 6.1 The counterparty criteria are continually under regular review but in the light of the current market conditions no recommendations are being put to Members to revise the Investment Strategy.

7. Treasury Management Prudential Indicators

7.1 Actual and estimates of the ratio of financing costs to net revenue stream

This indicator identifies the trend in the cost of capital (financing costs net of interest and investment income) against the net revenue stream.

	2022/23 Original Indicator %	2022/23 Current Position %
Non-HRA	5.31	6.04
HRA	16.80	14.68

- 7.2 The current position reflects in-year changes to the capital programme and minor fluctuations in interest rates.

7.3 Prudential indicator limits based on debt net of investments

- **Upper Limits on Fixed Rate Exposure** – This indicator covers a maximum limit on fixed interest rates.
- **Upper Limits on Variable Rate Exposure** – Similar to the previous indicator this identifies a maximum limit for variable interest rates based upon the debt position net of investments.

RMBC	2022/23 Original Indicator	Current Position
Limits on fixed interest rates based on net debt	100%	73.24%
Limits on variable interest rates based on net debt	50%	26.75%

7.4 **Maturity Structures of Borrowing**

These gross limits are set to reduce the Council's exposure to large fixed rate loans (those instruments which carry a fixed interest rate for the duration of the instrument) falling due for refinancing.

The current position shown below reflects the next call dates on those Council's LOBO loans that are not callable in 2022/23 and thus are regarded as fixed rate. The actual maturity date for most of these loans is greater than 50 years. This approach gives a better indication of risk and whilst there is a possibility that a loan is called with an increase in interest payable the likelihood of any LOBO loans being called in the current climate is assessed as zero for the next three years.

RMBC	2022/23 Original Indicator		Current Position	
	Lower	Upper	%	£m
Under 12 months	0%	60%	19.90%	143.500
12 months to 2 years	0%	35%	2.77%	20.000
2 years to 5 years	0%	45%	0.69%	5.000
5 years to 10 years	0%	45%	0.69%	5.000
10 years to 20 years	0%	45%	5.19%	37.438
20 years to 30 years	0%	50%	2.15%	15.521
30 years to 40 years	0%	50%	13.28%	95.815
40 years to 50 years	0%	55%	41.45%	299.000
50 years and above	0%	60%	13.86%	100.000

7.5 **Total Principal Funds Invested**

These limits are set to reduce the need for the early sale of an investment and show limits to be placed on investments with final maturities beyond each year-end.

The Council currently has no sums invested for periods exceeding 364 days due to market conditions. To allow for any changes in those conditions the indicator has been left unchanged.

RMBC	2022/23 Original Indicator £m	Current Position £m
Maximum principal sums invested > 364 days	10	0
Cash deposits	10	0

7.6 **Treasury Management Advisers**

Following a procurement exercise a new three year contract has been entered into with Link Asset Services Treasury Solutions (LAS) for the provision of treasury management and asset finance services. This commenced in January 2022.