Brighton & Hove City Council

Strategy, Finance & City Regeneration Committee

Agenda Item 65

Subject: **Treasury Management Strategy Statement 2023/23 - Mid Year Review**

Date of meeting: **7 December 2023**

Report of: **Chief Finance Officer**

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Ward(s) affected: **All**

For general release

1. Purpose of the report and policy context

1.1 The 2023/24 Treasury Management Strategy Statement (TMSS) was approved by Policy & Resources Committee on 9 February 2023 and full Council on 23 February 2023.

1.2 The TMSS sets out the role of Treasury Management and includes the Annual Investment Strategy (AIS) which sets out the key parameters for investing council cash funds.

1.3 It is recommended good and proper practice that Members receive half yearly reports and review and endorse treasury management actions during the year. The purpose of this report is to advise of the actions taken in the first half of 2023/24.

2. Recommendations

2.1 That Strategy, Finance & City Regeneration Committee notes the key actions taken during the first half of 2023/24 to meet the Treasury Management Strategy Statement and practices (including the investment strategy) as set out in this report.

2.2 That Strategy, Finance & City Regeneration Committee notes the reported compliance with the Annual Investment Strategy for the 6 month period up to the end of September 2023.

2.3 That Strategy, Finance & City Regeneration Committee notes that the approved maximum indicator for investment risk of 0.05% has been adhered to and the authorised borrowing limit and operational boundary have not been exceeded.

3. Context and background information

3.1 The council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available (i.e. liquid) when it is needed. Effective cash flow planning enables surplus monies to be invested in counterparties or instruments commensurate with the council's risk appetite, providing adequate cash availability (liquidity) is maintained.

3.2 The second main function of the treasury management service is the funding of the council's capital plans. These capital plans provide a guide to the borrowing need of the council, essentially the longer-term cash flow planning, to ensure that the council can meet its capital spending obligations. This management of longer-term cash may involve arranging long or short-term loans or using longer-term cash flow surpluses. On occasion, when it is prudent and economic, any debt previously drawn on may be restructured to meet the council's risk or cost objectives.

3.3 The Chartered Institute of Public Finance & Accountancy (CIPFA) defines treasury management 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."

Economic Background

3.4 The council's treasury advisors, Link Asset Services, have provided their assessment of the UK and global economic landscapes over 2023/23 at **Appendix 2**.

Treasury Management Strategy

3.5 A summary of the actions taken in the 6 months to September 2023 is provided in **Appendix 3** to this report. The main points are:

- No new borrowing was entered into during the period;
- A total of £6.2m PWLB debt was repaid on maturity during the period;
- A £10.0m market loan was repaid on maturity during September;
- The highest risk indicator during the period was 0.021% which is well below the maximum benchmark of 0.050%;
- The return on investments has not met the target benchmark rate, as explained in paragraph 3.16;
- Total borrowing activity has operated within the borrowing limits approved by full Council.

3.6 Treasury management activity for the half-year has focused on a short-term horizon as summarised in the table below:

	Amount invested 1 Apr 2023 to 30 Sep 2023			
	Fixed deposits	Money market funds & Notice Accounts	Total	
Up to 1 week	-	£324.4m	£324.4m	79.8%
Between 1 week & 1 month	-	-	-	0%
Between 1 month & 3 months	-	-	-	0%

Over 3 months	£82.0m	-	£82.0m	20.2%
	£82.0m	**£324.4m**	**£406.4m**	**100.0%**

Summary of Treasury Activity April 2023 to September 2023

3.7 The following table summarises the treasury activity in the half year to September 2023 compared to the corresponding period in the previous year:

April to September	**2022/23**	**2023/24**
Long-term borrowing raised (General Fund)	(£25.0m)	(£0.0m)
Long-term borrowing raised (HRA)	(£25.0m)	(£0.0m)
Long-term borrowing repaid (General Fund)	£1.0m	£7.8m
Long-term borrowing repaid (HRA)	£0.6m	£8.4m
Short-term borrowing (raised)/repaid	£1.5m	£4.5m
Investments made	£418.1m	£406.4m
Investments maturing	(£420.6m)	(£419.3m)

3.8 As at Targeted Budget Monitoring (TBM) period month 7 (October), an underspend of £1.611m had been reported within the Financing Costs Budget for the year. This underspend is largely as a result of increased investment income earned as a result of the increase in interest rates.

3.9 The following table summarises how the day-to-day cash flows in the half-year have been funded compared to the same period in the previous year:

April to September	2022/23	2023/24
Net cash flow (shortage)/surplus	**(£49.7m)**	**£7.0m**
Represented by:		
Increase/(reduction) in long-term borrowing	£48.5m	(£16.2m)
Increase/(reduction) in short-term borrowing*	(£1.5m)	(£4.5m)
Reduction/(increase) in investments	£2.5m	£12.9m
Reduction/(increase) in bank balance	£0.2m	£0.2m

*including South Downs National Park external investments

3.10 The large change in the cashflow profile compared to the previous year is largely as a result of repayment of covid advances back to central government in 2022/23.

Investment Strategy

3.11 A summary of investments made by the in-house team and outstanding as at 30 September 2023 in the table below shows that investments continue to be held in highly rated, short term instruments:

‘AAA’ rated money market funds	£27.12m	17%
‘AA’ rated institutions*	£50.00m	31%
‘A’ rated institutions	£72.50m	46%
‘BBB’ rated institutions	£0.00m	0%
Unrated Funds	£10.00m	6%
Total	**£159.62m**	**100%**
Period – less than one week	£37.12m	23%

Period – between one week and one month	£0.00m	0%
Period – between one month and three months	£0.00m	0%
Period – between three months and 1 year	£58.50m	37%
Period – more than 1 year**	£64.00m	40%
Total	**£159.62m**	**100%**

* *For the purposes of this analysis, other Local Authorities are assumed to have the same credit rating as the UK government (AA).*

** *All investments that are over one year either have a legal offset against debt with the same counterparty, or are with other Local Authorities.*

Risk

3.12 As part of the investment strategy for 2023/24 the Council agreed a maximum risk benchmark of 0.05% i.e. there is a 99.95% probability that the council will receive its investments back. The benchmark is a simple target that measures the risk based on the financial standing of counterparties and length of each investment based on historic default rates. The actual risk indicator has varied between 0.021% and 0.011% between April 2023 and September 2023. It should be remembered however that the benchmark is an 'average risk of default' measure and does not constitute an expectation of loss against a particular investment.

3.13 In July 2022, Internal Audit undertook an audit of the Treasury Management function. The audit opinion concluded that "substantial assurance" is provided on the effectiveness of the control framework operating and mitigating risks for treasury management. There were no recommendations or actions ~~were~~ required in response to the audit.

Compliance with the Annual Investment Strategy

3.14 For the reporting period, the information in this report provides assurance that the Annual Investment Strategy has been complied with in full.

Investment Performance

3.15 The council's investment portfolio (excluding pooled funds) achieved an average rate of 4.26% over the first six months of the year. This is against a benchmark rate of 4.73% for the same period.

3.16 The investment performance has therefore underperformed the benchmark rate by 0.47% in the first six months of the year. This is to be expected in a rising interest rate environment as it takes time for investments to mature and to be re-invested at higher rates, whilst the benchmark instantly responds to the changes in Base Rate.

3.17 The current forecast estimates that the average investment rate earned over the full year will be 4.65%. As set out in Appendix 2, Link Asset Services are currently forecasting that interest rates have peaked at 5.25%, and will gradually start to reduce from September 2024.

3.18 Officers have been mindful of balancing the desire to lock into attractive interest rates while they are at the peak with the need to maintain sufficient liquidity to allow the council to avoid external borrowing as long as possible. A raft of new deals were undertaken when six month to one year investment rates peaked at over 6.00% during July and August 2023, with no new deals undertaken during September to take the opportunity to increase liquidity.

3.19 The Royal London (RLAM) short dated funds total return (capital and revenue combined) was 7.81% for the year to 30 September 2023. The total return since inception (i.e. since the initial investment date) is -1.42%, resulting from a decline in capital value since the initial investment. The reduction of capital value is not a reduction in the worth of the individual assets in the fund but reflects a "marked to market" valuation of the funds at the end of each month, declining due to the steep rise in interest rates since December 2021. As interest rates stabilise and start to reduce, the capital value is expected to recover.

Borrowing Strategy

3.20 The council operates separate debt portfolios for the General Fund and the HRA following the introduction of the HRA Self-Financing regime in 2012.

3.21 The General Fund (GF) has been carrying an internal borrowing position (i.e. where the General Fund borrows cash from its own reserves) since 2008, initially as a response to the financial crisis. The reserves and balances are reviewed regularly to ensure that the cash will remain available to continue to support the internal borrowing.

3.22 A total of £67.500m of PWLB borrowing for the General Fund was undertaken between March 2019 and May 2022 at an average rate of 2.04%. This borrowing was undertaken to support the General Fund capital programme and to reduce the internal borrowing position in light of rising interest rates. No further external borrowing has been undertaken as borrowing rates have increased to a point which currently makes long term borrowing an expensive option, particularly as rates are forecast to reduce within the medium term.

3.23 The officer Capital Programme Board is currently reviewing capital investment requirements to assess the likely future borrowing need including the timing of the borrowing need.

3.24 The council's advisors are forecasting that interest rates have now peaked, and will start reducing towards the end of 2024. Therefore it is expected that any further GF borrowing need during the year will be met by using existing cash balances and/or short-term borrowing from other local authorities.

3.25 The Housing Revenue Account (HRA) adopts a fully funded borrowing position (i.e. the HRA does not borrow from its own reserves, but instead undertakes borrowing for its entire borrowing requirement). The HRA has undertaken a total of £116.000m of borrowing between March 2019 and May 2022 at an average rate of 1.84% to support the HRA Capital Programme. A portion of this (£9.826m) was "borrowed in advance of need" to take advantage of attractive interest rates at a time where they were forecast to rise steeply. This will be applied to the 2023/24 HRA capital programme.

3.26 As outlined in paragraph 3.24 above, interest rates are currently too high to consider long term borrowing. Therefore any further HRA borrowing need will be met by borrowing from the General Fund.

3.27 A summary of the council's debt portfolio is summarised in **Appendix 3**.

Treasury Advisors

3.28 The council has a 4-year contract for treasury advisory services with Link Asset Services (LAS), which started 1 April 2020.

3.29 The council recognises that responsibility for decisions remains with the organisation at all times and ensures that undue reliance is not placed upon external service providers. It also recognises that there is value in employing external providers of treasury management services in order to access specialist skills and resources.

4. Analysis and consideration of alternative options

4.1 This report sets out action taken in the 6 months to September 2023 and is therefore for noting only. However, Treasury management actions have been fully complied with and have been carried out within the parameters of the AIS, TMSS and Prudential Indicators.

5. Community engagement and consultation

5.1 The council's external treasury advisors have been consulted over the content of this report. No other consultation has been undertaken.

6. Conclusion

6.1 Treasury management is governed by a code that is recognised as "best and proper practice" under the Local Government Act 2003. The Code requires a minimum of two reports per year, one of which is required to review the previous year's performance. This report fulfils this requirement.

7. Financial implications

7.1 The financial implications of treasury management activity are reflected in the financing costs budget set out in paragraph 3.8.

Finance officer consulted: James Hengeveld   Date consulted: 23/11/2023

8. Legal implications

8.1 The TMSS is approved and associated actions are carried out under the powers given to the Council by Part 1 of the Local Government Act 2003 to invest for the purposes of the prudent management of its financial affairs (section 12).

8.2 Local authorities are required to have regard to statutory guidance in the form of the Prudential Code for Capital Finance in Local Authorities (updated in December 2021), issued by the Chartered Institute of Public Finance and Accountancy (CIPFA) when carrying out functions under Part 1 of the Act.

8.3 The council's approach is considered to be consistent with the requirements of the Act and the aforementioned Code.

Lawyer consulted: Victoria Simpson   Date consulted 21.11.23

9. Equalities, Sustainability and other significant implications

9.1 There are no direct implications arising from this report.

Supporting Documentation

1. Appendices

1. Glossary of terms
2. Economic Overview – Link Asset Services
3. A summary of the action taken in the period April 2023 to September 2023