monmouthshire county council
sir fynwy

REPORT

SUBJECT:	**TREASURY MANAGEMENT OUTTURN REPORT 2022/23**
MEETING:	**Governance & Audit Committee**
DATE:	**27th July 2023**
DIVISIONS/WARD AFFECTED:	**All**

1. PURPOSE:

1.1. During 2022/23, the Council's treasury management activity was underpinned by the Chartered Institute of Public Finance and Accountancy's (CIPFA) Prudential Code for Capital Finance in Local Authorities (the Prudential Code), and complimented by the CIPFA guidance "Treasury Management in the Public Services" which sets out good practice in treasury management.

1.2. These place a requirement on local authorities to produce annually a Treasury Management Strategy Statement and Prudential Indicators on their likely financing and investment activity, and to ensure that the appropriate governance function that oversees the treasury management activities of the Authority is kept informed of activity.

1.3. This report represents the second update of treasury management activity during 2022/23 following the mid-year report to Governance & Audit committee on the 24th November 2022.

2. RECOMMENDATIONS:

2.1. That Governance & Audit committee review the results of treasury management activities and the performance achieved in 2022/23 as part of their delegated responsibility to provide scrutiny of treasury policy, strategy and activity on behalf of Council.

3. SUMMARY OF KEY ISSUES:

3.1. The continuing economic fallout from the coronavirus pandemic, together with the war in Ukraine, higher inflation, higher interest rates, and market volatility were major issues that impacted treasury activity over the period.

3.2. The Bank of England increased the official Bank Rate to 4.25% during the financial year. From 0.75% in March 2022, the Monetary Policy Committee (MPC) pushed through rises at every subsequent meeting over the period, with recent hikes of 50bps in December and February and then 25bps in March, taking Bank Rate to 4.25%.

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

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

3.5. In a local context the broad treasury strategy of the Authority continued with the approach of keeping borrowing and investments below their underlying levels, known as internal borrowing, in order to reduce counterparty risk and keep interest costs low.

3.6. However, at the year-end date, and in an environment of increasing interest rates the Authority looked to provide some certainty by locking into additional longer-term loans marginally before they were actually required to fund expenditure. This position has unwound itself since year-end as temporary borrowing has matured, to take the authority back into an overall position of internal borrowing.

3.7. To that end, at the 31st March 2023 the Authority had a borrowing Capital Financing Requirement (CFR) of £190.9m and gross external borrowing of 198.7m.

3.8. Total borrowing has increased year-on-year by £23.2m which is due to a rising CFR, and the additional longer-term borrowing taken, as noted in 3.6 above, prior to temporary borrowing maturing.

3.9. With borrowing rates increasing considerably during the year and with further rises expected in the near term, the Authority looked to secure additional long-term borrowing at comparatively low rates. This has increased the proportion of long-term to short-term borrowing over the year from 59:41 to 67:33, providing an added element of balance and certainty over future interest payments. Further details of the overall maturity structure of borrowing are noted in table 11 of this report.

3.10. In year, the Authority's total treasury investments reduced by £9.5m to £38.5m due to the continuation of an internal borrowing strategy. Balances during the year ranged from between £14.5m and £79.3m due to timing differences between income and expenditure.

3.11. The Authority continues to hold a minimum of £10m of investments to meet the requirements of a professional client under the MIFID II regulations (Markets in financial instruments directive), and which permits access to a wider range of investment vehicles.

3.12. £4m of the Authority's investments are held in externally managed strategic pooled multi-asset and property funds where short-term security and liquidity are lesser considerations, and the objectives instead are regular revenue income and longer-term price stability. These funds generated an average 4.47% (£178k) income return, however volatile conditions within equity, bond and property markets resulted in a £401k (-10.10%) unrealised capital loss over the period. It is important to note that unrealised capital movements on these funds do not impact the income and expenditure account of the Authority and will only materialise at the time that the investments are liquidated. The Authority maintains a treasury risk reserve to mitigate against this risk.

3.13. As shown in section 9 the Authority achieved a saving of £157,000 against net treasury budgets of £3.86m, however there were large variations to budget across interest payable and receivable due to the volatile interest rate environment experienced during the year.

3.14. In respect of non-treasury investments (those categorised as either for service purposes to explicitly to further service objectives, and/or for commercial purposes), these continued to generate a return of £545k during the year which contributed to the running of Council services.

3.15. As reported in section 11, the Authority complied with the CIPFA code of practice on treasury management, and acted within the approved 2022/23 Treasury management strategy and indicators during the year.

4. INTRODUCTION

4.1. The Authority's treasury management strategy for 2022/23 was approved by Council on 3rd March 2022. The Authority has borrowed and invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk remains central to the Authority's treasury management strategy.

4.2. Treasury risk management at the Authority is conducted within the framework of the CIPFA Prudential code and Treasury Management in the Public Services which requires the Authority to approve a treasury management strategy before the start of each financial year and, for 2022/23, as a minimum a semi-annual and annual treasury outturn report.

4.3. This treasury outturn report presents the following information:

- An update on the external market conditions impacting treasury activity during the year;
- An update of the movement in treasury balances and performance against budget during the year;
- details of borrowing strategy, investment activity and non-treasury investment performance;
- compliance with treasury limits and indicators for the year.

5. External market conditions

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

5.2. Central Bank rhetoric and actions remained consistent with combatting inflation. The Bank of England, US Federal Reserve, and European Central Bank all increased interest rates over the period, even in the face of potential economic slowdowns in those regions.

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

5.4. Following the decision by the UK government under Rishi Sunak and Jeremy Hunt to reverse some of the support to household energy bills announced under Liz Truss, further support in the form of a cap on what energy suppliers could charge household was announced in the March Budget to run from April until end June 2023. Before the announcement, typical household bills had been due to rise to £3,000 a year from April.

5.5. The labour market remained tight albeit with some ongoing evidence of potential loosening at the end of the period. The unemployment rate 3mth/year eased from 3.8% April-June to 3.6% in the following quarter, before picking up again to 3.7% between October-December. The most recent information for the period December-February showed an unemployment rate of 3.7%.

5.6. The inactivity rate was 21.3% in the December-February quarter, slightly down from the 21.4% in the first quarter of the financial year. Nominal earnings were robust throughout the year, with earnings growth in December-February at as 5.7% for both total pay (including bonuses) and 6.5% for regular pay. Once adjusted for inflation, however, both measures were negative for that period and have been so throughout most of the year.

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

5.8. The Bank of England increased the official Bank Rate to 4.25% during the financial year. From 0.75% in March 2022, the Monetary Policy Committee (MPC) pushed through rises at every subsequent meeting over the period, with recent hikes of 50bps in December and February and then 25bps in March, taking Bank Rate to 4.25%. March's rise was voted by a majority of 7-2, with two MPC members preferring to maintain Bank Rate at 4.0%. The Committee noted that inflationary pressures remain elevated with growth stronger than was expected in the February Monetary Policy Report. The February vote was also 7-2 in favour of a hike, and again with two members preferring to keep Bank Rate on hold.

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

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

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

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

5.13. **Credit review:** Early in the period, Moody's affirmed the long-term rating of Guildford BC but revised the outlook to negative. The agency also downgraded Warrington BC and Transport for London.

5.14. In July Fitch revised the outlook on Standard Chartered and Bank of Nova Scotia from negative to stable and in the same month Moody's revised the outlook on Bayerische Landesbank to positive. In September S&P revised the outlook on the Greater London Authority to stable from negative and Fitch revised the outlook on HSBC to stable from negative.

5.15. The following month Fitch revised the outlook on the UK sovereign to negative from stable. Moody's made the same revision to the UK sovereign, following swiftly after with a similar move for a number of local authorities and UK banks including Barclays Bank, National Westminster Bank (and related entities) and Santander.

5.16. During the last few months of the reporting period there were only a handful of credit changes by the rating agencies, then in March the collapse of Silicon Valley Bank (SVB) in the US quickly spilled over into worries of a wider banking crisis as Credit Suisse encountered further problems and was bought by UBS.

5.17. Credit Default Prices had been rising since the start of the period on the back of the invasion of Ukraine, and in the UK rose further in September/October at the time of the then-government's mini budget. After this, CDS prices had been falling, but the fallout from SVB caused a spike on the back of the heightened uncertainty. However, they had moderated somewhat by the end of the period as fears of contagion subsided, but many are still above their pre-March levels reflecting that some uncertainty remains.

5.18. On the back of this, Arlingclose reduced its recommended maximum duration limit for unsecured deposits for all UK and Non-UK banks/institutions on its counterparty list to 35 days as a precautionary measure. No changes were made to the names on the list.

5.19. As market volatility is expected to remain a feature, at least in the near term and, as ever, the institutions and durations on the Authority's counterparty list recommended by Arlingclose remains under constant review.

5.20. Local authorities remain under financial pressure, but Arlingclose continues to take a positive view of the sector, considering its credit strength to be high. Section 114 notices have been issued by only a handful of authorities with specific issues. While Arlingclose's advice for local authorities on its counterparty list remains unchanged, a degree of caution is merited with certain authorities.

6. <u>Movement in Treasury balances</u>

6.1. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available to offset the CFR or for investment.

6.2. The Authority pursued its strategy of keeping borrowing and investments below their underlying levels for the majority of the year, known as internal borrowing, in order to reduce risk and keep interest costs low. At the year end and in an environment of increasing interest rates the Authority looked to provide some certainty by locking into additional loans marginally before they were actually required to fund expenditure. This position has unwound itself since year-end through maturing temporary borrowing, to take the authority back into an overall position of internal borrowing. These factors are summarised in Table 1 below.

Table 1: Balance Sheet Summary

	31.3.22 £m	Movement £m	31.3.23 £m
General Fund CFR	189.4	3.9	193.3
Less: *Other debt liabilities	(2.4)	(0.0)	(2.4)
Borrowing CFR	**187.0**	**3.9**	**190.9**
Less: External borrowing	(175.5)	(23.2)	(198.7)
Net External borrowing	**11.5**	**(19.3)**	**(7.8)**
Less: Usable reserves	(42.7)	2.9	(39.8)
Less: Working capital	(16.8)	25.8	9.0

(Net Investments) at 31st March 2023	(48.0)	9.5	(38.5)

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

6.3. On 31st March 2023, the Authority had net investments of £38.5m arising from its revenue and capital income and expenditure activity.

6.4. Whilst this has reduced compared to investment balances held at the start of the year, balances over the year ranged from between £14.5m and £79.3m due to timing differences between income and expenditure and borrowing activity.

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

Table 2: Borrowing and Investment Summary

	31.3.22 Balance £m	31.3.22 Rate %	Movement	31.3.23 Balance £m	31.3.23 Rate %
Long-term borrowing	104.3	3.1	28.7	133.0	3.2
Short-term borrowing	71.2	0.2	(5.5)	65.7	2.8
Total borrowing	**175.5**	**2.0**	**23.2**	**198.7**	**3.1**
Long-term investments	0.0	N/A	0.0	0.0	N/A
Short-term investments	(14.0)	0.1	1.0	(13.0)	2.1
Pooled Funds	(4.0)	3.4	0.0	(4.0)	4.5
Cash and cash equivalents	(30.0)	Included in ST above	8.5	(21.5)	Included in ST above
Total investments	**(48.0)**	**0.4**	**9.5**	**(38.5)**	**2.36**
Net Borrowing	**127.5**		**32.7**	**160.2**	

6.6. The authorities net borrowing position has increased over the year which is reflective of an increasing CFR, and additional long term loans taken out during the year to provide a further degree of certainty over future interest costs in a rising interest rate environment.

7. **Borrowing activity during the year**

7.1. The Authority's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio and, where practicable, to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing.

7.2. The cost of both long and short-term borrowing rose dramatically over the year, with rates at the end of March 2023 around 2% - 4% higher than those at the beginning of the year. Rate rises have been driven primarily by inflation and the need for central banks to control this by raising interest rates.

7.3. Particularly dramatic rises were seen in September after Liz Truss' 'mini-budget' included unfunded tax cuts and additional borrowing to fund consumer energy price subsidies. Over a twenty-four-hour period some PWLB rates increased to 6%. Rates have now fallen from September peaks but remain volatile and well above recent historical norms. The PWLB 10 year maturity certainty rate stood at 4.33% at 31st March 2023, 20 years at 4.70% and 30 years at 4.66%.

7.4. The Authority mitigates against the risk of rising interest rates by holding a balanced portfolio of long and short term loans that are not overly exposed to any one event impacting the level of interest rates.

However, it is inevitable that in a rising interest rate environment, that overall interest rate costs for an authority who is a net borrower from the market will rise over time.

7.5. At 31st March 2023 the Authority held £198.7m of loans, an increase of £23.2m to 31st March 2022, as part of its strategy for funding previous and current years' capital programmes. Outstanding loans on 31st March are summarised in Table 3 below.

Table 3: Borrowing Position

	31.3.22 Balance £m	31.3.22 Weighted Average Rate %	31.3.22 Weighted Average Maturity (years)	Balance Movement	31.3.23 Balance £m	31.3.23 Weighted Average Rate %	31.3.23 Weighted Average Maturity (years)
Public Works Loan Board	86.8	3.1	24.8	33.0	119.8	3.3	22.8
Banks (LOBO)	13.6	4.8	19.8	0.0	13.6	4.8	18.8
Welsh Gov Interest Free	6.0	0.0	3.3	(0.8)	5.3	0.0	3.0
Local authorities/Other	69.0	0.1	0.3	(9.0)	60.0	2.6	0.5
Total borrowing	**175.5**	**2.0**	**14.0**	**23.2**	**198.7**	**3.1**	**15.2**

7.6. Whilst the Council has significant long-term borrowing requirements, the Council has continued its strategy of internal borrowing, where the Council seeks to use its existing cash balances and reserves to afford its capital expenditure prior to the necessity to take out external borrowing.

7.7. However the Authority's chief objective when borrowing has always been to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required, with flexibility to renegotiate loans should the Authority's long-term plans change being a secondary objective.

7.8. To that end, during the year some short-term borrowing was replaced with long-term PWLB borrowing at competitive rates of interest.

Table 4: Long-dated Loans borrowed

	Amount £m	Rate %	Period (years)
PWLB Maturity Loan	2.0	4.78	4
PWLB Maturity Loan	2.0	4.8	6
PWLB Maturity Loan	2.0	4.8	7
PWLB Maturity Loan	2.0	4.81	8
PWLB Maturity Loan	3.5	4.82	8
PWLB EIP Loan	1.81	2.31	8
PWLB Maturity Loan	3.5	4.84	10
PWLB EIP Loan	4.5	3.81	13
PWLB Maturity Loan	2.0	2.8	26
PWLB Annuity Loan	2.0	2.82	27
PWLB Maturity Loan	5.0	3.24	38
PWLB Maturity Loan	5.0	3.22	40
Total	**35.31**		

7.9. **Other borrowing activity**

7.10. PWLB funding margins continued to lurch quite substantially during the year and there remains a strong argument for diversifying funding sources, particularly if rates can be achieved on alternatives which are below gilt yields + 0.80%. The Authority will evaluate and pursue these lower cost solutions and opportunities with its advisor Arlingclose.

7.11. **LOBO Loans:** The Authority continues to hold £13.6m of LOBO (Lender's Option Borrower's Option) loans where the lender has the option to propose an increase in the interest rate as set dates, following which the Authority has the option to either accept the new rate or to repay the loan at no additional cost. No banks exercised their option during the year, however in a rising interest rate environment the risk of call increases, and the Authority will closely monitor the position moving forward.

7.12. CIPFA's 2021 Prudential Code is clear that local authorities must not borrow to invest primarily for financial return and that it is not prudent for local authorities to make any investment or spending decision that will increase the capital financing requirement, and so may lead to new borrowing, unless directly and primarily related to the functions of the Authority. PWLB loans are no longer available to local authorities planning to buy investment assets primarily for yield unless these loans are for refinancing purposes.

7.13. The Authority currently holds commercial investments that were purchased prior to the change in the CIPFA Prudential Code. The Authority is not planning to purchase any investment assets primarily for yield within the next three years and so is able to access PWLB borrowing if considered cost effective.

8. Investment activity during the year

8.1. Treasury management investments as investments that arise from the organisation's cash flows or treasury risk management activity that ultimately represents balances that need to be invested until the cash is required for use in the course of business.

8.2. The Authority holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. During the year, the Authority's investment balances ranged from between £14.5m and £79.3m due to timing differences between income and expenditure. The investment position at year end was:

Table 5: Treasury Investment Position

	31.3.22 Balance £m	Net Movement £m	31.3.23 Balance £m	31.3.23 Income Return %	31.3.23 Weighted Average Maturity Days
Banks & building societies (unsecured)	(2.0)	0.0	(2.0)	Average 2.1%	Up to 180 days
Government (incl. local authorities	(14.0)	1.0	(13.0)		
Money Market Funds (MMFs)	(28.0)	8.5	(19.5)		
Multi asset income, Pooled funds	(4.0)	0.0	(4.0)	4.5%	N/A
Total investments	**(48.0)**	**9.5**	**(38.5)**		

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

8.4. Bank Rate has increased from 0.75% at the beginning of the year to 4.25% at the end of March 2023. Short-dated cash rates, which had ranged between 0.7% - 1.5% at the beginning of April, rose by around 3.5% for overnight/7-day maturities and 3.3% for 6-12 month maturities.

8.5. By end March 2023, the rates on DMADF deposits ranged between 4.05% and 4.15%. The return on the Council's sterling Low Volatility Net Asset Value (LVNAV) Money Market Funds ranged between 0.50% - 0.58% p.a. in early April and between 4.01% and 4.12% at the end of March.

8.6. £4m of the Authority's investments are invested in externally managed strategic pooled multi-asset and property funds where short-term security and liquidity are lesser considerations, and the objectives instead are regular revenue income and longer-term price stability. These funds generated an average £178k (4.47%) income return, together with a £401k (-10.10%) unrealised capital loss.

8.7. UK and global equities remained volatile against a backdrop of high and sticky inflation, rapid policy rates tightening and an increasing risk of recession. There was a large sell-off in global equities in April, and again in June and September for both UK and global equities. The total return on the FTSE All Share index for the 12 months ending March 2023 was 2.9% and 5.4% for the FTSE 100

8.8. The negative correlation between bonds and equities, which had featured for some years, turned positive in 2022 as both bonds and equities sold off simultaneously against an outlook of sticky inflation and high interest rates. Simultaneously, tighter financial conditions, higher bond yields and challenges in some segments of commercial real estate (e.g. offices post-COVID, high street shops and shopping centres) saw commercial property values fall during 2022, with a large fall in the final calendar quarter.

8.9. Because pooled funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Authority's medium to long-term investment objectives are regularly reviewed. Strategic fund investments are made in the knowledge that capital values will move both up and down on months, quarters and even years; but with the confidence that over a three to five-year period total returns should exceed cash interest rates.

8.10. The Authority maintains a treasury risk reserve to mitigate against the risk that capital losses on pooled funds are realised and result in a charge against the Council Fund.

9. Treasury performance

9.1. The Authority measures the financial performance of its treasury management activities both in terms of its impact on the revenue budget and its relationship to benchmark interest rates.

Table 6: Budget performance

	Actual £000's	Budget £000's	Over / (under) Budget
Interest Payable			
PWLB	3,363	2,725	639
Market loans	652	653	0
Short term loans	733	579	154
Total Interest payable on borrowing	**4,748**	**3,957**	**792**
Interest Receivable			

Invested cash short term	(759)	(100)	(659)
Pooled Funds	(179)	Included above	(179)
Finance lease income	(57)	Included above	(57)
Other Interest	(53)	0	(53)
Total income from Investments	**(1,049)**	**(100)**	**(949)**
Total	**3,700**	**3,857**	**(157)**

9.2. The combination of risk and return metrics are shown in the extracts from Arlingclose's quarterly investment benchmarking in Table 7 below.

Table 7: Investment Benchmarking – Treasury investments managed in-house

	Credit Score	Credit Rating	Bail-in Exposure	Weighted Average Maturity (days)	Rate of Return %
MCC 31.03.2022	AA-	3.81	59%	4	0.64
MCC 31.03.2023	AA-	4.46	62%	4	3.89
Similar LAs	AA-	4.41	25%	96	3.78
All LAs	A+	4.71	59%	12	3.66

10. **Non-Treasury Investments**

10.1. The definition of investments in CIPFA's Treasury Management Code covers all the financial assets of the Authority as well as other non-financial assets which the Authority holds primarily for financial return. Investments that do not meet the definition of treasury management investments (i.e. management of surplus cash) are categorised as either for service purposes (made explicitly to further service objectives) and/or for commercial purposes (made primarily for financial return).

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

10.3. The Authority held a net book value of £32.2m of such non-financial asset investments at the 31st March 2023 (£31.4m as at 31st March 2022) made up of:

	Net (income) / loss 2022/23 £000's	Carrying Value 31.03.23 £000's	Net return 2022/23 %	Net return 2021/22 %
Oak Grove Solar Farm	(737)	5,485	13.44	11.02
Newport Leisure Park & service loan	(2)	19,756	0.01	3.05
Castlegate Business Park	405	6,159	-6.58	0.66
Commercial loan – Broadway partners	(211)	763	0.78	0.78
Total	**(545)**	**32,163**		

10.4. The Authority also holds the following portfolio of legacy non-financial asset investments that have been held for over a decade and are retained for income generation, capital gain or to support wider economic development or broader policy objectives. Income generation for these assets is a secondary consideration and as such return against original investment would be considered negligible.

	Net (income) / loss 2022/23 £000's	Carrying Value 31.03.23 £000's
Agricultural Properties	33,600	27,800
Industrial Properties and Retail units	3,400	3,500

11. **Compliance with treasury limits and indicators**

11.1. The Section 151 officer reports that all treasury management activities undertaken during the year complied fully with the CIPFA code and the limits and indicators as set out in the Authority's approved Treasury Management Strategy.

11.2. **Borrowing limits:** Compliance with the authorised limit and operational boundary for external debt is demonstrated in table 8 below.

Table 8: Borrowing Limits

	2022/23 Maximum during the year £m	31.3.23 Actual £m	2022/23 Operational Boundary £m	2022/23 Authorised Limit £m	Complied? Yes/No
Borrowing	199.2	198.7	238.0	268.2	Yes
PFI, Finance Leases & Other LT liabs	2.4	2.3	2.9	4.4	Yes
Total debt	**201.6**	**201.0**	**240.9**	**272.6**	**Yes**

11.3. **Note**: Since the operational boundary is a management tool for in-year monitoring it is not significant if the operational boundary is breached on occasions due to variations in cash flow, and this is not counted as a compliance failure.

Table 9: Investment Limits

	Maximum in year	2022/23 Limit	Complied? Yes/No
The UK Government	£44.4m	Unlimited	Yes
Local Authorities per counterparty	£0m	£4m	Yes
Secured Investments	£0m	£4m	Yes
Banks per counterparty, rating A- or above	£2m (£3m total for the Councils operational bank)	£2m (£3m total for the Councils operational bank)	Yes
Building societies (unsecured)	£0m	£2m	Yes
Registered providers (e.g. Housing	£0m	£2m	Yes

Associations (unsecured)			
Money Market Funds	£4m	£4m	Yes
Any group of pooled funds under the same management	£2m	£5m	Yes
Real estate investment trusts	£0m	£5m	Yes
Limit per non-UK country	£0m	£4m	Yes
Other Investments	£0m	£2m	Yes

11.4. **Security:** The Authority has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average credit rating and credit score of its investment portfolio. This is calculated by applying a score to each investment (AAA=1, AA+=2, etc.) and taking the arithmetic average, weighted by the size of each investment. Unrated investments are assigned a score based on their perceived risk.

Table 10: Credit Risk

	31.3.23 Actual	2022/23 Target	Complied?
Portfolio average credit	AA-/4.46	A-/5.0	Yes

11.5. **Maturity Structure of Borrowing:** This indicator is set to control the Authority's exposure to refinancing risk. The upper and lower limits on the maturity structure of all borrowing were:

Table 11: Maturity Structure of borrowing

Maturity	31.3.23 Actual	Lower Limit	Upper Limit	Complied?	31.3.22 Actual (For info)
Under 12 months	33%	0%	60%	Yes	41%
12 months and within 24 months	4%	0%	30%	Yes	2%
24 months and within 5 years	6%	0%	30%	Yes	6%
5 years and within 10 years	14%	0%	30%	Yes	6%
10 years and within 20 years	12%	0%	30%	Yes	12%
20 years and within 30 years	11%	0%	30%	Yes	15%
30 years and within 40 years	10%	0%	30%	Yes	7%
40 years and within 50 years	10%	0%	30%	Yes	11%
50 years and above	0%	0%	30%	Yes	0%

11.6. **Principal Sums Invested for Periods Longer than a year:** The purpose of this indicator is to control the Authority's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the long-term principal sum invested to final maturities beyond the period end were:

Table 12: Principal invested for period longer than a year

	During 2022/23

Actual principal invested for 365 days & beyond year end	£0m
Limit	£6m
Complied?	Yes

12. Other Issues

12.1. **IFRS 16:** The implementation of the new IFRS 16 Leases accounting standard was due to come into for force for local authorities from 1st April 2022. Following a consultation CIFPA/LASAAC announced an optional two year delay to the implementation of this standard, a decision which was confirmed by the Financial Reporting Advisory Board in early April 2022. Authorities can now choose to adopt the new standard on 1st April 2022, 1st April 2023 or 1st April 2024. The Authority intends to adopt the new standard on 1st April 2024.

13. REASONS

13.1. The Authority's Treasury Management Strategy for 2022/23 was underpinned by the adoption of the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code), and complimented by the CIPFA guidance "Treasury Management in the Public Services" which sets out good practice in treasury management.

13.2. The code requires the Authority to set a treasury strategy each financial year for financing and investment activities and recommends that members are informed of Treasury Management activities at the end of each quarter. This report therefore ensures this authority is embracing best practice in accordance with CIPFA's recommendations.

14. RESOURCE IMPLICATIONS

14.1. The outturn position is explained in the report, there are no other resource implications arising directly from this report.

15. CONSULTEES

Deputy Chief Executive, Chief Officer - Resources (Section 151 officer)

Arlingclose Limited – External Treasury management advisors to Monmouthshire CC

16. BACKGROUND PAPERS

Glossary of treasury terms

17. AUTHORS:

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Background paper: Glossary of Treasury Terms

Authorised Limit	The affordable borrowing limit determined in compliance with the Local Government Act 2003 (English and Welsh authorities) and the Local Government in Scotland Act 2003. This Prudential Indicator is a statutory limit for total external debt. It is set by the Authority and needs to be consistent with the Authority's plans for capital expenditure financing and funding. The Authorised Limit provides headroom over and above the *Operational Boundary* to accommodate expected cash movements. Affordability and prudence are matters which must be taken into account when setting this limit. (see **also** *Operational Boundary*, below)
Balances and Reserves	Accumulated sums that are maintained either earmarked for specific future costs or commitments or generally held to meet unforeseen or emergency expenditure.
Bail-in	Refers to the process which the banking regulatory authorities will use to restructure a financial institution which is failing or likely to fail. Unsecured creditors of and investors in that financial institution will participate in its restructure who will, as a consequence, incur a non-recoverable loss (commonly referred to as a 'haircut') on their obligation/investment. Local authority investments with banks and building societies such as term deposits, certificates of deposit, call accounts and non-collateralised bonds are unsecured investments and are therefore vulnerable to bail-in.
Bank Rate	The official interest rate set by the Bank of England's Monetary Policy Committee and what is generally termed at the "base rate". This rate is also referred to as the 'repo rate'.
Bond	A certificate of debt issued by a company, government, or other institution. The bond holder receives interest at a rate stated at the time of issue of the bond. The price of a bond may vary during its life.
Capital Expenditure	Expenditure on the acquisition, creation or enhancement of capital assets
Capital Financing Requirement (CFR)	The Council's underlying need to borrow for capital purposes representing the cumulative capital expenditure of the local authority that has not been financed.
Capital growth	Increase in the value of the asset (in the context of a collective investment scheme, it will be the increase in the unit price of the fund)
Capital receipts	Money obtained on the sale of a capital asset.
CIPFA	Chartered Institute of Public Finance and Accountancy
Constant Net Asset Value (CNAV)	Also referred to as Stable Net Asset Value. A term used in relation to the valuation of 1 share in a fund. This means that at all times the value of 1 share is £1/€1/US$1 (depending on the currency of the fund). The Constant NAV is maintained since dividend income (or interest) is either added to the shareholders' account by creating shares equal to the value of interest earned or paid to the shareholder's bank account, depending on which option is selected by the shareholder.
Collective Investment Schemes	Funds in which several investors collectively hold units or shares. The assets in the fund are not held directly by each investor, but as part of a pool (hence these funds are also referred to as 'Pooled Funds'). Unit Trusts and Open-Ended Investment Companies are types of collective investment schemes / pooled funds.

Corporate Bonds	Corporate bonds are bonds issued by companies. The term is often used to cover all bonds other than those issued by governments in their own currencies and includes issues by companies, supranational organisations and government agencies.
Corporate Bond Funds	Collective Investment Schemes investing predominantly in bonds issued by companies and supranational organisations.
CPI ***Also see RPI***	Consumer Price Index. (This measure is used as the Bank of England’s inflation target.)
Credit Default Swap (CDS)	A Credit Default Swap is similar to an insurance policy against a credit default. Both the buyer and seller of a CDS are exposed to credit risk. Naked CDS, i.e. one which is not linked to an underlying security, can lead to speculative trading.
Credit Rating	Formal opinion by a registered rating agency of a counterparty’s future ability to meet its financial liabilities; these are opinions only and not guarantees.
Cost of carry	When a loan is borrowed in advance of requirement, this is the difference between the interest rate and (other associated costs) on the loan and the income earned from investing the cash in the interim.
Credit default swaps	Financial instrument for swapping the risk of debt default; the buyer effectively pays a premium against the risk of default.
Diversification / diversified exposure	The spreading of investments among different types of assets or between markets in order to reduce risk.
Derivatives	Financial instruments whose value, and price, are dependent on one or more underlying assets. Derivatives can be used to gain exposure to, or to help protect against, expected changes in the value of the underlying investments. Derivatives may be traded on a regulated exchange or traded ‘over the counter’.
ECB	European Central Bank
Federal Reserve	The US central bank. (Often referred to as “the Fed”)
Floating Rate Notes	A bond issued by a company where the interest rate paid on the bond changes at set intervals (generally every 3 months). The rate of interest is linked to LIBOR and may therefore increase or decrease at each rate setting
GDP	Gross domestic product – also termed as “growth” in the economy. The value of the national aggregate production of goods and services in the economy.
General Fund	This includes most of the day-to-day spending and income. (All spending and income related to the management and maintenance of the housing stock is kept separately in the HRA).
Gilts (UK Govt)	Gilts are bonds issued by the UK Government. They take their name from ‘gilt-edged’: being issued by the UK government, they are deemed to be very secure as the investor expects to receive the full face value of the bond to be repaid on maturity.
Housing Revenue Account (HRA)	A ring-fenced account of all housing income and expenditure, required by statute

IFRS	International Financial Reporting Standards
Income Distribution	The payment made to investors from the income generated by a fund; such a payment can also be referred to as a 'dividend'
Investments - **Secured** - **unsecured**	Secured investments which have underlying collateral in the form of assets which can be called upon in the event of default Unsecured investments do not have underlying collateral. Such investments made by local authorities with banks and building societies are at risk of bail-in should the regulator determine that the bank is failing or likely to fail.
Liability Benchmark	Term in CIPFA's Risk Management Toolkit which refers to the minimum amount of borrowing required to keep investments at a minimum liquidity level (which may be zero).
LOBOs	LOBO stands for 'Lender's Option Borrower's Option'. The underlying loan facility is typically long term and the interest rate is fixed. However, in the LOBO facility the lender has the option to call on the facilities at predetermined future dates. On these call dates, the lender can propose or impose a new fixed rate for the remaining term of the facility and the borrower has the 'option' to either accept the new imposed fixed rate or repay the loan facility.
LVNAV (Low Volatility Net Asset Value)	From 2019 Money Market Funds will have to operate under a variable Net Value Structure with minimal volatility (fluctuations around £1 limited to between 99.8p to 100.2p)
Maturity	The date when an investment or borrowing is repaid.
Maturity profile	A table or graph showing the amount (or percentage) of debt or investments maturing over a time period. The amount or percent maturing could be shown on a year-by-year or quarter-by-quarter or month-by-month basis.
MiFID II	MiFID II replaced the Markets in Financial Instruments Directive (MiFID I) from 3 January 2018. It is a legislative framework instituted by the European Union to regulate financial markets in the bloc and improve protections for investors.
Money Market Funds (MMF)	Pooled funds which invest in a range of short term assets providing high credit quality and high liquidity.
Minimum Revenue Provision	An annual provision that the Authority is statutorily required to set aside and charge to the Revenue Account for the repayment of debt associated with expenditure incurred on capital assets
Non-Specified Investments	Term used in the Communities and Local Government Guidance and Welsh Assembly Guidance for Local Authority Investments. It includes any investment for periods greater than one year or those with bodies that do not have a high credit rating, use of which must be justified.
Net Asset Value (NAV)	A fund's net asset value is calculated by taking the current value of the fund's assets and subtracting its liabilities.
Operational Boundary	This is the limit set by the Authority as its most likely, i.e. prudent, estimate level of external debt, but not the worst case scenario. This limit links directly to the Authority's plans for capital expenditure, the estimates of the Capital Financing Requirement (CFR) and the estimate of cashflow requirements for the year.

Permitted Investments	Term used by Scottish Authorities as those the Authority has formally approved for use.
Pooled funds	See Collective Investment Schemes (above)
Premiums and Discounts	In the context of local authority borrowing, (a) the premium is the penalty arising when a loan is redeemed prior to its maturity date and (b) the discount is the gain arising when a loan is redeemed prior to its maturity date. If on a £1 million loan, it is calculated* that a £100,000 premium is payable on premature redemption, then the amount paid by the borrower to redeem the loan is £1,100,000 plus accrued interest. If on a £1 million loan, it is calculated that a £100,000 discount receivable on premature redemption, then the amount paid by the borrower to redeem the loan is £900,000 plus accrued interest. PWLB premium/discount rates are calculated according to the length of time to maturity, current market rates (plus a margin), and the existing loan rate which then produces a premium/discount dependent on whether the discount rate is lower/higher than the coupon rate. *The calculation of the total amount payable to redeem a loan borrowed from the Public Works Loans Board (PWLB) is the present value of the remaining payments of principal and interest due in respect of the loan being repaid prematurely, calculated on normal actuarial principles. More details are contained in the PWLB's lending arrangements circular.
Private Finance Initiative (PFI)	Private Finance Initiative (PFI) provides a way of funding major capital investments, without immediate recourse to the public purse. Private consortia, usually involving large construction firms, are contracted to design, build, and in some cases manage new projects. Contracts can typically last for 30 years, during which time the asset is leased by a public authority.
Prudential Code	Developed by CIPFA and introduced on 01/4/2004 as a professional code of practice to support local authority capital investment planning within a clear, affordable, prudent and sustainable framework and in accordance with good professional practice.
Prudential Indicators	Indicators determined by the local authority to define its capital expenditure and asset management framework. They are designed to support and record local decision making in a manner that is publicly accountable; they are not intended to be comparative performance indicators between authorities.
PWLB	Public Works Loans Board. It is a statutory body operating within the United Kingdom Debt Management Office, an Executive Agency of HM Treasury. The PWLB's function is to lend money from the National Loans Fund to local authorities and other prescribed bodies, and to collect the repayments.
Quantitative Easing	In relation to the UK, it is the process used by the Bank of England to directly increase the quantity of money in the economy. It "does not involve printing more banknotes. Instead, the Bank buys assets from private sector institutions – that could be insurance companies, pension funds, banks or non-financial firms – and credits the seller's bank account. So the seller has more money in their bank account, while their bank holds a corresponding claim against the Bank of England (known as reserves). The end result is more money out in the wider economy". Source: Bank of England
Registered Provider of Social Housing	Formerly known as Housing Association
Revenue Expenditure	Expenditure to meet the continuing cost of delivery of services including salaries and wages, the purchase of materials and capital financing charges

RPI	Retail Prices Index. A monthly index demonstrating the movement in the cost of living as it tracks the prices of goods and services including mortgage interest and rent. Pensions and index-linked gilts are uprated using the CPI index.
SORP	Statement of Recommended Practice for Accounting (Code of Practice on Local Authority Accounting in the United Kingdom).
Specified Investments	Term used in the CLG Guidance and Welsh Assembly Guidance for Local Authority Investments. Investments that offer high security and high liquidity, in sterling and for no more than 1 year. UK government, local authorities and bodies that have a high credit rating.
Supported Borrowing	Borrowing for which the costs are supported by the government or third party.
Supranational Bonds	Instruments issued by supranational organisations created by governments through international treaties (often called multilateral development banks). The bonds carry an AAA rating in their own right. Examples of supranational organisations are those issued by the European Investment Bank, the International Bank for Reconstruction and Development.
Treasury Management Code	CIPFA's Code of Practice for Treasury Management in the Public Services.
Temporary Borrowing	Borrowing to cover peaks and troughs of cash flow, not to fund spending.
Term Deposits	Deposits of cash with terms attached relating to maturity and rate of return (interest)
Unsupported Borrowing	Borrowing which is self-financed by the local authority. This is also sometimes referred to as Prudential Borrowing.
Usable Reserves	Resources available to finance future revenue and capital expenditure
Variable Net Asset Value (VNAV)	A term used in relation to the valuation of 1 share in a fund. This means that the net asset value (NAV) of these funds is calculated daily based on market prices.
Working Capital	Timing differences between income/expenditure and receipts/payments
Yield	The measure of the return on an investment instrument