Rother District Council

Report to:	Audit and Standards Committee
Date:	2 October 2023
Title:	Treasury Management Update
Report of:	Aleksandra Janowicz – Interim Chief Finance Officer
Purpose of Report:	To note the Council's treasury activities for the first financial quarter ending the 30 June 2023.
Officer Recommendation(s):	It be **RESOLVED**: That the report be noted.

Introduction

1. The Council's Investment Strategy requires regular reports to be presented to this Committee on its treasury management activities. In managing these, the Council has implemented the Department of Levelling Up, Housing and Communities (DLUHC) investment guidance and followed the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management.

2. The investment activity to date conforms to the approved strategy and the Council has had no liquidity difficulties. Members are reminded that investment activity is also reported through the Members' Bulletin. This report focuses on the financial period ending the 30 June 2023 and is based on the latest available data.

3. Members will note that the figures quoted within the report are either actuals or estimates as stated and the outturn position at year end is draft subject to change following completion of the audit of 2022/23 accounts.

Financial Investments review

4. As of 30 June 2023, the Council's total investments were around £22.5 million with £14.5m invested in short term call accounts (£20.6m and £12.6m respectively at Quarter 4 2022/23) and £8 million in Property Funds (no change from Quarter 4). Funds managed internally are mainly in call accounts, but we are reviewing rates available on the market to invest in fixed term deposits to benefit from higher rates. We have engaged with the market via an online platform to open MMF (liquidity) funds. Members will note that a significant element of the £14.5m balance relates to cash owed to public bodies, e.g. council tax precepts, shares of business rates.

5. The Council's investments are currently predicted to have yielded interest income of £232,000 in Quarter 1 of this financial year, including income generated by the property funds (CCLA and Hermes). The budget for the year is £586,000 so we likely have already achieved 39% of it. This is mainly due to

an increased focus on treasury management activities and the incremental Bank of England interest rates increases. This amount could be inflated by a further £38,000 for the interest accruing on the loan provided so far to the Rother DC Housing Company Ltd.

6. Forecasting into the future to arrive at the annual outturn figure is difficult as it depends on a variety of factors and assumptions. It is highly likely that the budget will be achieved, but the range of possible outcomes is expected to be in excess of £510,000 surplus as we look to diversify our treasury deposits. Whereas we had enjoyed exceptionally good call account rates from our bankers, these fell significantly late in July. To mitigate this, we opened a new Lloyds Treasury Call Account with rates similar to those we had previously benefitted from and where we now invest any excess cash daily. In order to maintain the yield, we need to assess opportunities and risks in other products which we are exploring and preparing for.

7. The possible outcomes for the variance are dependant, amongst others, on:

- any further movement in Bank of England rate and its impact on what banks are prepared to offer as a result;

- the level of funds available to invest, which will in turn be heavily dependent on cashflows relating to capital expenditure. As the capital programme is being reviewed and borrowing rates from the Public Works Loan Board (PWLB) are at very elevated levels (5.64% interest rate for a new 50-year annuity loan as at September 2023), there is a high level of uncertainty around this; and

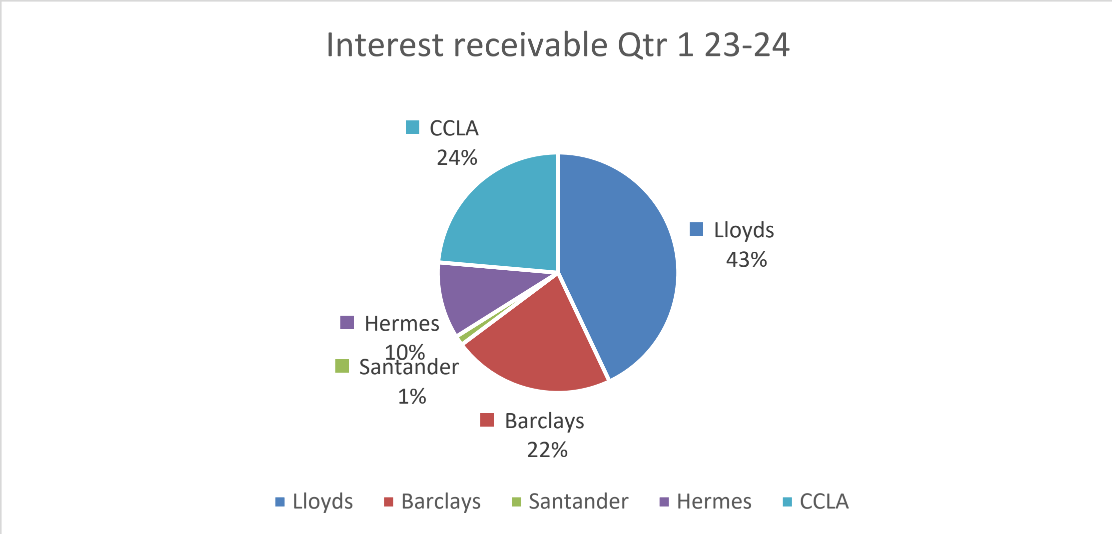
- on activity levels at the Rother DC Housing Company Ltd which will determine how much loan funding is required from the Council.

8. The total variance (surplus) estimated in the Revenue and Capital Monitoring report for Quarter 1 is £710,000, as it includes interest accruing on the Housing Company loan (estimated to be around £200,000 for the year).

9. Officers will apply the principles of security, liquidity and yield in their treasury decisions, both when continuing with the current products and exploring others. Advice will be sought from Link Treasury Services as appropriate.

10. The investment portfolio and Property Fund values as at Quarter 1 are detailed in Appendix A.

11. Estimated Quarter 1 interest receivable breakdown is depicted in the graph overleaf:



Borrowing

12. The Council's Capital Financing Requirement (CFR) shows how much of its capital expenditure is financed by borrowing and is summarised in Appendix B. The capital programme budget has been reviewed during Quarter 1 in view of the complexity of several of the proposed schemes and the rapidly changing financial landscape in terms of inflationary pressures, interest and borrowing rate changes. The CFR position has changed as a result. The forecast outturn for the year is now £57.0 million. Members will also note that the capital programme continues to be reviewed for affordability as part of ongoing monitoring of the capital programme and a revised budget for the CFR will be developed as part of this work.

13. The value of outstanding loans as at the 30 June 2023 was £31.8m and the borrowing portfolio is also shown in Appendix B. This is £11.6m lower than the CFR, which means the Council has 'under-borrowed' and effectively borrowed internally using up its cash balances, rather than borrowing when interest rates are high.

14. Officers will continue to keep borrowing policy under review and use internal balances where possible to minimise borrowing costs.

Treasury and Prudential Indicators

15. It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. The Council's approved Treasury and Prudential Indicators (affordability limits) are included in the approved Treasury Management Strategy. During the financial year to date, the Council has operated within the treasury and prudential indicators set out in the Council's Treasury Management Strategy Statement and in compliance with the Council's Treasury Management Practices.

16. The current prudential and treasury indicators, such as the Council's Authorised and Operational external borrowing limits, were approved by Cabinet on the 27 February 2023 as part of the Council's Treasury Management Strategy and are shown in Appendix C. Members will note that the current borrowing levels

shown in Appendix B are comfortably within both limits. No amendments to the Treasury Management Strategy are proposed as a result of this report.

17. The ratio of Net Financing Costs (NFC) to the Net Revenue Stream in the original budget was to be 5.06%, but is now predicted to be -0.99%. This is both due to the review of and subsequent delay in the capital programme delivery referred to above and the additional investment income received, which reduces the NFC. The Prudential Indicators are shown in Appendix C.

Non-Treasury Investments

18. The table below shows property rental income for the year against the approved budget and is split between existing assets and those purchased through the Property Investment Strategy (PIS):

Property Type	Net Budget 2023/24 (Rent income and expense)	Qtr 1 Estimate for annual Net Rent Income and expense	Variance	Return on Investment	Notional interest	Return on Investment after notional interest applied
	£000	£000	£000	%	£000	%
Non-PIS	(669)	(665)	4	5.26	n/a	5.26
PIS	(1,536)	(1,573)	(37)	5.29	586	3.33
Total	**(2,205)**	**(2,238)**	**(33)**	**5.27 (ave)**	**586**	**4.29 (ave)**

19. The above table shows the return on investment on all PIS properties, including notional borrowing costs. Appendix D shows detail including the total cost of purchase as well as net income predicted to be achieved by year end.

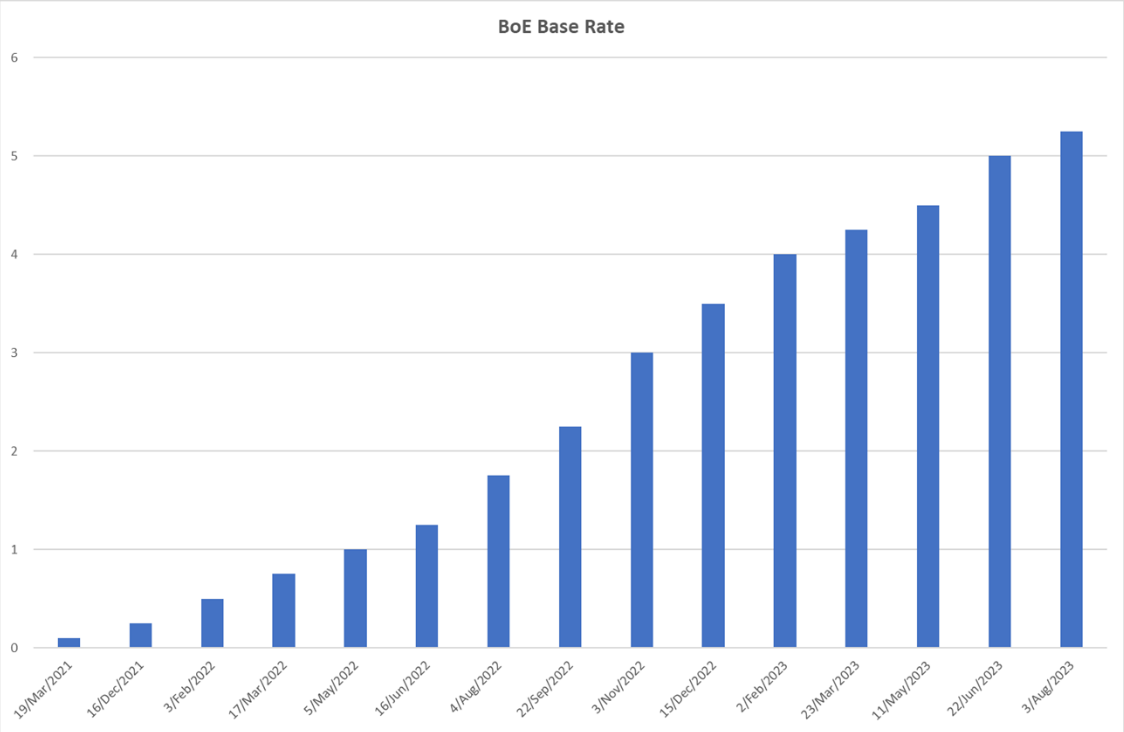
Economic Update and Outlook

20. The ongoing impact on the UK from the war in Ukraine, together with the highest inflation for the last 40 years, rising interest rates, uncertainties over government policy and an uncertain economic outlook continue to impact on current treasury management activities.

21. Inflation is significantly eroding the Council's spending power. At its 2 August 2023 meeting, the Bank of England's Monetary Policy Committee (MPC) has updated projections which show the annual Consumer Price Index inflation rate falling back from its very high level, of around 10% since the summer of 2022 up to March 2023, to around 8.7% in May and 7.9% in June, but the fall was not as sharp as previously hoped for. It is predicted to fall further by the end of this calendar year to around 5% and come back closer to the target of 2% only in three years' time. However, previous such projected falls have not always materialised as inflation is proving stubborn in the UK, whilst being in decline elsewhere in other major economies (the June reading was the highest in the G7). Past increases in energy and other goods prices falling out of the calculation of the annual rate, have not yet materially changed the situation and the country seems to be feeling the combined effect of remaining high energy

and food prices as well as worker shortages, which do not allow for the inflationary pressures to ease. To the contrary, the recent reacceleration in wage growth shows that domestic inflationary pressures are still strengthening.

22. At the recent meeting of the Bank of England's MPC in August 2023, it was agreed to increase the bank base rate by a further 0.25% to 5.25% to help control inflation. For comparison, in December 2021 it was 0.1%. It was the fourteenth rise in interest rates since then (see graph below).



The Council's Treasury advisers predict that the Bank rate is likely to peak between 5.50% and 6%.

23. The UK economy grew by 0.2% between January and June 2023 according to the Office for National Statistics, and the Bank of England forecasts Gross Domestic Product (GDP) will be around the same in the second quarter of the calendar year (back in February it was predicted to record a 0.7% decline), reflecting more resilient household income and retail sales volumes than previously thought. Some more recent indicators, however, show signs of weakening, with less resilient growth and lower consumer confidence.

24. Credit rating agencies have reflected the difficult UK position by affirming its AA- rating with a Negative Outlook as of 2 June 2023, citing rising government debt, weak growth and the risk of more persistent inflation, rising borrowing costs, pressures due to cost-of-living crisis and the proximity of general elections (Fitch).

25. Forecasting economic activity in the current climate is fraught with difficulties. Officers will continue to monitor closely any future changes and will factor them into the Council's next update of the Medium Term Financial Plan in due course.

26. The impact on the Council of all of the above is higher costs of providing services, higher potential borrowing costs (PWLB 50-year loan rate rose from under 2% at the end of 2021 to 5.64% at the time of writing) which may render some capital projects unviable and have a possible negative impact on council tax collection rates, as the cost-of-living crisis hits thousands of families across the district.

Other issues

27. The value of investments in Property Funds has remained stable since the end of the last financial year and is £7.457m. The value is therefore currently £542,596 less than originally invested. Members will be reminded that any gains or losses on such long-term investments will only be realised at the point of withdrawal from the fund. Property funds still provide a healthy income stream in the form of quarterly distributions and are expected to contribute £296,000 in the financial year to 31 March 2024.

28. It is also worth mentioning again that, following a consultation on the IFRS9 statutory override, the government announced an extension of the override for a further two years until 25 March 2025. This allows councils to override fair value movements on pooled investments (like this Council's CCLA and Hermes) in order to protect themselves from market volatility. Such movements are still being reversed from the General Fund and into unusable reserves and as such, they do not have an impact on budget setting. Without the override, negative movements in their value would cause a budget deficit and require more funds to be withdrawn from reserves.

Conclusion

29. The investment activity conforms to the approved strategy and the Council has no liquidity difficulties.

Other Implications	Applies?	Other Implications	Applies?
Human Rights	No	Equalities and Diversity	No
Crime and Disorder	No	External Consultation	No
Environmental	No	Access to Information	No
Risk Management	No	Exempt from publication	No

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Appendices:	Appendix A – Investments Portfolio Appendix B – Capital Financing Requirement & Borrowing Portfolio Appendix C – Prudential Indicators Appendix D – Performance of PIS properties
Relevant Previous Minutes:	None
Background Papers:	Capital, Investment and Treasury Management Strategy Report to Cabinet, 27 February 2023
Reference Documents:	None

Appendix A

Investments Portfolio

Deposit	Type of account	Maturity Date	Amount Invested £	Interest Rate 30 June 2023 %	Share %
Lloyds - General (RFB)	Call	N/A	9,329,329	4.9	41.53%
Bank of Scotland (RFB)	Call	N/A	46	0.01	0.00%
Barclays - Call Account (NRFB)	Call	N/A	5,136,797	3.60	22.86%
Santander - Call Account	Call	N/A	214	2.93	0.00%
CCLA Local Authority Property Fund	Long Term	N/A	5,000,000	0	22.26%
HERMES Property Fund	Long Term	N/A	2,999,998	0	13.35%
Total			**22,466,384**		**100.00%**
Total managed in-house			14,466,386		
Total managed externally			7,999,998		
Total Treasury Investments			**22,466,384**		

Property Funds

Name of Property Fund	Original Investment Value	Value 31/03/2023	Value 30/6/2023	Change since start of financial year	Change since original investment made
	£	£	£	£	£
CCLA Property Fund	5,000,000	4,733,177	4,726,609	(6,568)	(273,391)
HERMES Property Fund	2,999,998	2,732,630	2,730,892	(1,738)	(269,105)
Total	**7,999,998**	**7,465,808**	**7,457,501**	**(8,306)**	**(542,496)**

Appendix B

Capital Financing Requirement

Capital Financing Requirement (CFR)	2023/24 Original Budget £ (000)	2023/24 Quarter 1 Forecast £ (000)
Opening Balance	31,896	43,469
Add unfinanced capital expenditure	108,764	13,998
Less Minimum Revenue Provision (MRP)	(224)	(515)
Closing Balance	**140,436**	**56,952**

Capital programme – revised at Quarter 1

	2023/24	2024/25	2025/26	2026/27	2027/28	Total
Capital Expenditure	27,696	68,045	23,503	8,694	28,183	**156,121**
Funded by:						
Capital Receipts	3,004	117	-	-	-	**3,121**
Grants and contributions	9,752	6,615	14,927	7,589	1,625	**40,508**
CIL	513	1,484	1,321	850	-	**4,168**
Borrowing	8,997	20,699	125	125	125	**30,071**
Capital Expenditure Charged to Revenue	230	130	130	130	130	**750**
Borrowing and Loan for RDC Housing Company Ltd	5,000	39,000	7,000	-	26,303	**77,303**
Section 106	200	-	-	-	-	**200**
Total	**27,696**	**68,045**	**23,503**	**8,694**	**28,183**	**156,121**

Current Borrowing Portfolio

Borrowing position at 30 June 2023					
Properties	**Amount o/s**	**Interest Rate**	**Term**	**Type**	**Full Year Repayments (capital and interest)**
PWLB 507499	£426,423	2.59%	50	Annuity	£16,102
PWLB 507503	£426,358	2.58%	50	Annuity	£16,070
PWLB 509130	£1,577,860	2.39%	50	Annuity	£56,729
PWLB 509131	£1,000,000	2.24%	50	Maturity	£22,400
PWLB 509165	£8,137,470	2.48%	50	Annuity	£297,572
PWLB 387276	£6,180,951	1.78%	50	Annuity	£190,804
PWLB 455425	£9,117,859	1.65%	50	Annuity	£273,881
Market	£5,000,000	1.70%	2	Maturity	£85,349*
Total Borrowing	**£31,866,920**				**£958,907**

Appendix C

Treasury Indicators (Borrowing Limits)

Treasury Indicators	2023/2024 £ (000)
Authorised Limit for External Debt	192,833
Operational boundary for External Debt	183,833
Gross External Debt (actual) at Quarter 1	31,867
Remaining Authorised Limit for External Debt	**160,966**

Prudential Indicators

Prudential Indicators	2023/24 Original Budget £ (000)	2023/24 Quarter 1 Forecast £ (000)
Capital Financing Requirement (CFR)	140,436	56,952
Annual Change in CFR	108,540	13, 483
In-Year Borrowing Requirements	108,764	13,998
Ratio of Financing costs to Net Revenue Stream (%)	5.06	-0.99

Appendix D

Properties purchased through the Property Investment Strategy

Property Investment strategy	Total Cost of Purchase £	Budgeted Net Surplus 2023/24 £	Forecast Net Surplus at Quarter 1 £	Variance £
14 Terminus Road Filling station	887,605	(79,800)	(79,800)	0
14 Terminus Road Garage /Showroom				0
16A Beeching Road	861,000	(32,350)	(32,350)	0
16B Beeching Road		(56,350)	(56,350)	0
18-40 Beeching Road	861,000	(78,850)	(78,850)	0
1-7, Wainwright Road	407,305	0	(3,798)	(3,798)
Glovers House, Bexhill	7,843,952	(473,820)	(473,820)	0
Land at Barnhorn Green, Bexhill	1,640,309	(194,980)	(194,980)	0
Market Square, Battle	3,256,184	50	(33,282)	(33,332)
35, Beeching Road, Bexhill (headlease)	695,359	(8,960)	(8,960)	0
64, Ninfield Road, Sidley	121,945	(577,900)	(577,900)	0
Sainsburys, Buckhurst Place	10,182,055	1,000	1,000	0
Land at Mount View Street, Bexhill	4,492,599	(17,500)	(17,500)	0
16 Beeching park Estate	427,875	(17,000)	(17,000)	0
18 Beeching park Estate				0
Total	**31,677,188**	**(1,536,460)**	**(1,573,590)**	**(37,130)**