North Devon Council

Report Date: Monday, 6 November 2023

Topic: Mid Year Treasury Management Report 2023/24

Report by: Adam Tape, Head of Governance

1. Introduction

1.1 This mid-year report has been prepared in compliance with CIPFA's Code of Practice on Treasury Management, and covers the following:

- An economic update for the first part of the 2023/24 financial year (appendix A);
- A review of the Treasury Management Strategy Statement and Annual Investment Strategy;
- The Council's capital expenditure and prudential indicators;
- A review of the Council's investment portfolio for 2023/24;
- A review of the Council's borrowing strategy for 2023/24;
- A review of any debt rescheduling undertaken during 2023/24;
- A review of compliance with Treasury and Prudential Limits for 2023/24.

2. Recommendations

The Committee is asked to recommend to full Council that:

2.1 The changes to the prudential indicators be approved.

2.2 The report and the treasury activity be noted.

3. Reasons for Recommendations

3.1 This Council is required through regulations issued under the Local Government Act 2003 to produce a mid year treasury report reviewing treasury management activities and the prudential and treasury indicators for 2023/24. This report meets the requirements of the CIPFA Code of Practice on Treasury Management (revised 2021).

3.2 This Council is also required under the Code to give prior scrutiny to the treasury management reports by the Policy Development Committee before they are reported to the full Council.

4. Report

4.1 Treasury Management Strategy Statement and Annual Investment Strategy update

The Treasury Management Strategy Statement (TMSS) for 2023/24 was approved by this Council on 22nd February 2023.

The underlying TMSS approved previously requires revision in the light of economic and operational movements during the year. The proposed changes are set out below:

Prudential Indicator 2023/24	Original Estimate £000	Revised Prudential Indicator £000
Capital Financing Requirement	33,323	29,960
Operational Boundary	21,771	11,922

Section 4.3 of this report gives further information on the Capital Financial Requirement and the Operational Boundary.

4.2 The Council's Capital Position (Prudential Indicators)

This part of the report is structured to update:

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

Prudential Indicator for Capital Expenditure

This table shows the revised estimates for capital expenditure and the changes since the capital programme was agreed at the budget.

Capital Expenditure by Service	2023/24 Original Estimate £000	Current Position 30/09/23 £000	2023/24 Revised Estimate £000
Customer Focus	185	113	308
Environmental Enhancement	742	154	2,375
Governance	0	0	0
Place & Regeneration	16,730	3,588	9,250
Planning, Housing & Health	3,590	1,467	5,162
Total	**21,247**	**5,322**	**17,095**

Changes to the Financing of the Capital Programme

The table below draws together the capital expenditure plans (above), and the expected financing arrangements of this capital expenditure. 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).

Capital Expenditure	2023/24 Original Estimate £000	2023/24 Revised Estimate £000
Total capital spend	**21,247**	**17,095**
Financed by:		
Capital receipts	(150)	(320)
Capital grants	(11,313)	(10,003)
Capital reserves	(1,234)	(1,522)
Total financing	**(12,697)**	**(11,845)**
Borrowing requirement	**8,550**	**5,250**

4.3 Changes to the Prudential Indicators for the Capital Financing Requirement (CFR), External Debt and the Operational Boundary

The table below shows the borrowing requirement (above), the reduction for the Minimum Revenue Provision (MRP) and impact on the CFR, which is the underlying external need to incur borrowing for a capital purpose. It also shows the expected debt position over the period, which is termed the Operational Boundary.

	2023/24 Original Estimate £000	2023/24 Revised Estimate £000
Prudential Indicator – Capital Financing Requirement		
Borrowing requirement	8,550	5,250
Finance Leases – Capital costs	1,270	1,767
Minimum Revenue Provision	(747)	(741)
Finance Lease Principal Payments (MRP)	(232)	(182)
Movement in CFR	8,841	6,094
Revised Total CFR	**33,323**	**29,960**
Prudential Indicator – the Operational Boundary for external debt		
Borrowing	19,000	9,000
Other long term liabilities	2,771	2,922
Total debt (year-end position)	**21,771**	**11,922**

Prudential Indicator – Capital Financing Requirement

The forecast Capital Financing Requirement has decreased by circa £3.4m from the original budget. This is due to the re-profiling of the capital programme with expenditure being slipped to future financial years for projects such as Future High Streets project.

Prudential Indicator – the Operational Boundary for external debt

The forecast external PWLB borrowing has decreased by £10m from the original budget in part by the reduced capital expenditure as above and higher year end cash flow balance projections. Section 4.5 looks at the borrowing strategy in more detail.

4.4 Limits to Borrowing Activity

The first key control over the treasury activity is a prudential indicator to ensure that over the medium term, net borrowing (borrowings less investments) will only be for a capital purpose. **Gross 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 2023/24 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 will be adhered to if this proves prudent.

	2023/24 Original Estimate £000	**Current Position 30/09/23 £000**	**2023/24 Revised Estimate £000**
Borrowing	19,000	3,000	9,000
Other Long term Liabilities	2,771	2,500	2,922
Total debt	**21,771**	**5,500**	**11,922**
CFR (year end position)	33,323		29,960
Under / over borrowing	(11,552)		(18,038)

A further prudential indicator controls the overall level of borrowing. This is the **Authorised Limit** that represents the limit beyond which borrowing is prohibited, and needs to be set and revised by Members. It reflects the level of borrowing which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. 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.

Authorised limit for external debt	**2023/24 Original Indicator £000**	**2023/24 Revised Indicator £000**
Borrowing	33,000	33,000
Other long term liabilities	4,500	4,500
Total	37,500	37,500

The Extraordinary Council meeting held on 14th June 2021 approved the increase in the authorised borrowing limit to £37.5m as part of the report detailing the purchase of a strategic asset.

4.5 Borrowing

The Council's forecast capital financing requirement (CFR) for 2023/24 is £30m. The CFR denotes the Council's underlying need to borrow for capital purposes. If the CFR is positive the Council may borrow from the Public Works Loan Board (PWLB), or the market (external borrowing), or from internal balances on a temporary basis (internal borrowing). The balance of external and internal borrowing is generally driven by market conditions.

At present, the Council has projected total external borrowing of £9m with £3m long term liabilities (finance leases) whilst utilising £18m of cash flow funds in lieu of borrowing (internal borrowing). This is a prudent and cost effective approach in the current economic climate and reduces the net interest cost to the Council, but will require ongoing monitoring of economic conditions and our own cash flow balances to support the internal borrowing.

The capital programme is being kept under regular review due to the effects of inflationary pressures, shortages of materials and labour. Our borrowing strategy will, therefore, also be regularly reviewed and then revised, if necessary, to achieve optimum value and risk exposure in the long-term.

The cash balances have allowed external borrowing to remain at £3m as at 30th September. The current forecast is for an additional £6m of external borrowing during the financial year, but the exact amount will depend on any capital spend slippages and our cash flow balances towards the financial year end. Given current market volatility any borrowing undertaken is likely to be short term, as PWLB rates are expected to fall back as Bank Rate is reduced in a couple financial years' time.

PWLB maturity certainty rates (gilts plus 80bps) year to date to 29th September 2023

Gilt yields and PWLB certainty rates were on a generally rising trend throughout the first half of 2023/24. At the beginning of April, the 5-year rate was the cheapest part of the curve and touched 4.14% whilst the 25-year rate was relatively expensive at 4.58%.

July saw short-dated rates peak at their most expensive. The 1-year rate spiked to 6.36% and the 5-year rate to 5.93%. Although, in due course, short-dated rate expectations fell, the medium dates shifted higher through August and the 10-year rate pushed higher to 5.51% and the 25-year rate to 5.73%. The 50-year rate was 4.27% on 5th April but rose to 5.45% on 28th September.

We forecast rates to fall back over the next two to three years as inflation dampens. The CPI measure of inflation is expected to fall below 2% in the second half of 2024, and we forecast 50-year rates to stand at 3.90% by the end of September 2025. However, there is considerable gilt issuance to be digested by the market over the next couple of years, as a minimum, so there is a high degree of uncertainty as to whether rates will fall that far.

HIGH/LOW/AVERAGE PWLB RATES FOR 01.04.23 – 29.09.23

The

	1 Year	5 Year	10 Year	25 Year	50 Year
Low	4.65%	4.14%	4.20%	4.58%	4.27%
Date	06/04/2023	06/04/2023	06/04/2023	06/04/2023	05/04/2023
High	6.36%	5.93%	5.51%	5.73%	5.45%
Date	06/07/2023	07/07/2023	22/08/2023	17/08/2023	28/09/2023
Average	5.62%	5.16%	5.01%	5.29%	5.00%
Spread	1.71%	1.79%	1.31%	1.15%	1.18%

4.6 Debt Rescheduling

Debt rescheduling opportunities have increased over the course of the past six months and will be considered if giving rise to long-term savings. However, no debt rescheduling has been undertaken to date in the current financial year.

4.7 Compliance with Treasury and Prudential Limits

It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. During the half year ended 30th September 2023, the Council has operated within the treasury and prudential indicators set out in the Council's Treasury Management Strategy Statement for 2023/24. The Chief Finance Officer reports that no difficulties are envisaged for the current or future years in complying with these indicators.

All treasury management operations have also been conducted in full compliance with the Council's Treasury Management Practices.

4.8 Annual Investment Strategy

The Treasury Management Strategy Statement (TMSS) for 2023/24, which includes the Annual Investment Strategy, was approved by the Council on 22nd February 2023. In accordance with the CIPFA Treasury Management Code of Practice, it sets out the Council's investment priorities as being:

- Security of capital
- Liquidity
- Yield

The Council will aim to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity and with the Council's risk appetite. In the current economic climate it is considered appropriate to keep investments short term to cover cash flow needs, but also to seek out value available in periods up to 12 months with high credit rated financial institutions, using the Link suggested creditworthiness approach.

Creditworthiness.

Following the Government's fiscal event on 23rd September, both S&P and Fitch have placed the UK sovereign debt rating on Negative Outlook, reflecting a downside bias to the current ratings in light of expectations of weaker finances and a challenging economic outlook. Nothing further has evolved in the first half of 2023/24.

Investment Counterparty criteria

The current investment counterparty criteria selection approved in the TMSS is meeting the requirement of the treasury management function

Investment balances

The Council held £12.9m of investments as at 30 September 2023 (£5.7m at 31 March 2023) and the investment portfolio yield for the first six months of the year was 4.01% against the benchmark 7 day average SONIA rate of 4.71.

The Council's budgeted investment return for 2023/24 was £120,000. As at 30th September 2023 £240,000 investment interest was earned in the half-year period.

As at 30 September 2023 we are forecasting total investment interest return of circa £400,000 for the financial year. In addition, using the cash flow balances for internal borrowing has reduced the borrowing costs on the expenditure budget and we are currently forecasting a £164,000 underspend on the interest payable budget for the year.

There is no anticipated use of the Treasury Management reserve during 2023/24 and so the full reserve balance of £275,000 can be carried forward to help protect and mitigate against higher borrowing costs in future financial years.

The Chief Financial Officer confirms that the approved limits within the Annual Investment Strategy were not breached during the first six months of 2023/24.

Investment performance year to date as of 29th September 2023

	Bank Rate	SONIA	7 day	30 day	90 day	180 day	365 day
High	5.25	5.19	5.19	5.20	5.12	4.78	4.06
High Date	03/08/2023	29/09/2023	04/09/2023	27/09/2023	29/09/2023	29/09/2023	29/09/2023
Low	4.25	4.18	4.18	4.02	3.81	3.32	2.27
Low Date	03/04/2023	04/04/2023	11/04/2023	03/04/2023	03/04/2023	03/04/2023	03/04/2023
Average	4.81	4.74	4.71	4.64	4.44	4.10	3.16
Spread	1.00	1.01	1.01	1.17	1.31	1.46	1.79

Non-Treasury Management Investments

The PWLB will no longer provide loans for 'debt for yield' projects where financial assets and property are purchased primarily for financial return. This would also mean no PWLB loans for the rest of the capital programme in that year.

The Chief Finance Officer confirms there have been no ‘debt for yield’ projects included in the current capital programme.

5. Resource Implications

5.1 As detailed in the report.

6. Equalities Assessment

6.1 There are not any equalities implications anticipated as a result of this report, as the purpose of this report is to present the Council’s financial position only.

7. Environmental Assessment

7.1 The Council has held funds in a sustainable deposit account during the half year period. These deposits have an underlying commitment to supporting activities that provide sustainable and environmentally friendly services and products.

8. Corporate Priorities

8.1 The Treasury management function supports the delivery of the Councils capital programme and ensures cash flows meets the day to day requirements for service delivery

9. Constitutional Context

9.1 The decision in respect of the recommendations in this report can be made by this Committee pursuant to delegated powers provided in Part 3 Annexe 1, para 1(c)

9.2 The power to decide on one or more of the recommendations in this report is reserved to Council pursuant to Article 4.5.26 and Part 4 (Financial Procedure Rules) para 13.8 and as such the recommendation must be referred to Council to ratify.

10. Statement Of Confidentiality

10.1 This report contains no confidential or exempt information under the provisions of Schedule 12A of 1972 Act.

11. Statement Of Internal Advice

11.1 The author (below) confirms that advice has been taken from all appropriate Councillors and Officers.

Jon Triggs, Director of Resources and Deputy Chief Executive