SURREY
COUNTY COUNCIL

Audit & Governance Committee
5 June 2023

2022/23 Treasury Management Outturn Report

Purpose of the report:

This report summarises the Council's treasury management activities during 2022/23, as required, to ensure compliance with the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice (the CIPFA Code) which requires the Authority to approve a treasury management annual report after the end of each financial year.

Recommendations:

It is recommended that the Committee:

- Note the content of the Treasury Management Outturn Report for 2022/23 and compliance with all Prudential Indicators.

Background:

1. The Authority has adopted the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice* (the CIPFA Code) which requires the Authority to approve Treasury Management semi-annual and annual outturn reports. This is the annual outturn report for 2022/23.

2. The Authority's Treasury Management Strategy Statement and Prudential Indicators for 2022/23 were approved at Audit & Governance Committee on 24 January 2022. The investment and borrowing of cash exposes the Council 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 are therefore central to the Authority's Treasury Management Strategy.

3. An economic commentary provided by our expert Treasury Management Advisors, Arlingclose, is included in Annex 1 (produced in April 2023).

4. Interest rate forecast, provided by our expert Treasury Management Advisors, Arlingclose is included in Annex 2 (produced in May 2023).

Treasury Management Annual Report 2022/23

Overview

5. On 31 March 2023, the Authority had net borrowing of £536m arising from its revenue and capital income and expenditure, a decrease of £30m since 31 March 2022. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), which represents the amount of capital expenditure that is not funded from capital receipts, government grants, third party contributions or revenue.

6 6. Net borrowing has decreased due to an increase in working capital, offset in part by an increase in the CFR due to new capital expenditure funded from borrowing being higher than the minimum revenue provision for the year. This is set out in table 1, below:

Table 1: Balance Sheet Summary

	31/03/22 Balance £m	2022/23 Movement £m	31/03/23 Balance £m
General Fund CFR	1,335	54	1,389
Less PFI Liabilities	(91)	10	(81)
Gross Borrowing Requirement	**1,244**	**64**	**1,308**
Less usable reserves and working capital	(678)	(94)	(772)
Net Borrowing Requirement	**566**	**(30)**	**536**

Note: Columns may not sum due to rounding

7. The Treasury Management Strategy for 2022/23, approved by Audit & Governance Committee in January 2022, continued the policy of internal borrowing wherever possible. This maintains borrowing below its underlying level by using available reserves and working capital to reduce the need for external borrowing. This minimises interest rate risks and keeps interest costs and the cost of carry lower.

8. The Council also manages cash on behalf of Surrey Police and Crime Commissioner, the balance of which was £33m as at 31 March 2023. The Council accounts for this as short-term borrowing. The treasury management position as at 31 March 2023 and the year-on-year change is show in table 2 below.

Table 2: Treasury Management Summary

	31/03/22 Balance £m	2022/23 Movement £m	31/03/23 Balance £m
Long-term borrowing	481*	(15)	466*
Short-term borrowing	200	(66)	134
Surrey Police	26	7	33
Total borrowing	**707**	**(74)**	**633**
Money Market Funds	(141)	44	(97)
Net borrowing	**566**	**(30)**	**536**

*Total long term borrowing is £480m. This includes £13.7m of Local Enterprise Partnership (LEP) and Salix loans which are managed outside of the Treasury Management function.

Borrowing Activity

9. At 31 March 2023, the Authority held £633m of borrowing, a decrease of £74m on the previous year. The sources of borrowing, interest rates and the year-on-year change is show in table 3 below.

Table 3: Borrowing Position

	31/03/22 Balance £m	2022/23 Net Movement £m	31/03/23 Balance £m	31/03/23 Rate %
Public Works Loan Board (PWLB)	471	(15)	456	3.61
Banks (fixed-term)	10	0	10	5.00
Local authorities (short-term)	200	(66)	134	3.64
Surrey Police & Crime Commissioner	26	7	33	4.25
Total borrowing	**707**	**(74)**	**633**	

10. The Authority's primary consideration when borrowing money has been to strike a balance between securing low interest rates and achieving cost certainty over a period for which funds are required. This position provides short term efficiencies with the flexibility to secure longer dated loans as and when the level of funds available for internal borrowing reduces, or financial forecasts indicate that external borrowing rates may increase. No new long term borrowing was undertaken during 2022/23, as internal borrowing was maximised and short-term borrowing was utilised to manage cash flow. Discussions have been taking place with Arlingclose immediately after the Bank of England's Monetary Policy Committee meetings, to review interest rate forecasts, assess the cost of carry and review the need to undertake further borrowing in advance for future years' planned expenditure.

Investment Activity

11. The Authority holds invested funds, representing income received in advance of expenditure, plus reserves and balances held which have not been utilised for internal borrowing.

12. 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 investments before seeking the highest 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.

13. The Council's average daily level of cash investments was £113.7m during 2022/23, compared to an average of £59.6m during 2021/22. This reflects the Council's strategic policy to maintain sufficient liquidity during this time and continue to borrow over shorter periods when appropriate and the receipt of additional funding through the Safety Valve agreement and some significant capital receipts. The Council invests temporary cash surplus exclusively through the use of money market funds (MMF). Other investment facilities are available including brokers, direct dealing with counterparties through the use of call accounts or direct deal facilities, or with the government's debt management office. No new fixed term deposits have been agreed during 2022/23, due to cash balances being held to maintain sufficient liquidity.

14. The year-end investment position and the year-on-year change is shown in table 4 below:

Table 4: Investment Position (Treasury Investments)

	31/03/22 Balance £m	2022/23 Net Movement £m	31/03/23 Balance £m	31/03/23 Rate* %
Money Market Funds	141	(44)	97	1.83
Total Investments	**141**	**(44)**	**97**	**1.83**

*weighted average rate earned in the year

6 15. The weighted average return on all investments the Council received in the year to 31 March 2023 was 1.83%. Money Market Fund rates have been increasing over the year, reflecting increases to the Bank of England Base Rate. There is a short time lag of between 2 to 4 weeks of Money Market Fund catching up with the official rate, as fund managers roll maturing instruments into new instruments at higher investment rates.

Financial Implications

16. The outturn for interest paid, interest received and the minimum revenue provision are outlined in table 5 below.

Table 5: Revenue Implications of Treasury Management Activity

	Budget £m	Outturn £m	Variance £m
Interest Paid	17.9	18.1	0.2
Interest Received	(0.03)	(1.9)	(1.87)
MRP	24.7	23.8	(0.9)

17. The amount of the Authority's revenue budget required to be set aside for the future repayment of external borrowing is known as the Minimum Revenue Provision (MRP). This amount is calculated by reference to the Council's balance sheet as at the end of the previous financial year. The underspend on MRP relates to the capital underspend in the 2021/22 financial year, and less borrowing required to fund the capital spend.

18. The underspend on interest receivable reflects the higher than forecast cash balances held throughout the year and the higher interest environment. This is partially offset by the overspend on interest payable, also due to higher interest rates.

Compliance Report

19. All treasury management activities undertaken during 2022/23 complied fully with the CIPFA Code of Practice and the Authority's approved Treasury Management Strategy. Compliance with specific investment limits, the authorised limit and operational boundary for external debt, is demonstrated in tables 6 & 7 below.

Table 6: Debt Limits

	2022/23 Maximum actual position £m	31/03/23 Actual £m	2022/23 Operational Boundary £m	2022/23 Authorised Limit £m	Complied
Total			1,394	1,894	
Less: Other long term liabilities (PFI)			(87)	(87)	

Underlying Borrowing	740	633	1,307	1,807	✓

20. 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 considered a compliance failure. Total debt did not exceed the operational boundary at any point in 2022/23.

Table 7: Investment Limits 6

	2022/23 Maximum actual position £m	31/03/23 Actual £m	2022/23 Limit £m	Complied
UK Central Government	0	0	Unlimited	✓
Money Market Funds	239	97	Unlimited	✓
Any group of pooled funds under the same management	0	0	25	✓
Any group of organisations under the same ownership	0	0	20	✓
Any single organisation, except the UK Central Government	0	0	20	✓
Unsecured investments with Building Societies	0	0	10	✓

Treasury Management Indicators

21. The Authority measures and manages its exposure to treasury management risks using the following indicators.

Security: The Council understands that credit ratings are good, but not perfect, predictors of investment default. Full regard is therefore given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support, reports in the quality financial press and analysis. No investments will be made with an organisation if there are substantive doubts about its credit quality. In addition, if insufficient commercial organisations of high credit quality are available to invest the Council's cash balances, then the surplus will be deposited with the UK Government via the Debt Management Office or invested in government treasury bills or with other Local Authorities.

Liquidity: The Council manages its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments. The Council maintains a bank overdraft of £100,000, utilises overnight access Money Market Funds and accesses short term borrowing to meet cash flow requirements. The Local Authority market provides readily available funds.

Interest Rate Exposures:

The Council had £134m of short-term borrowing at 31 March 2023, with an additional £163m expected to be required to finance the 2023/24 capital programme, which would result in total of £297m by March 2024. Short term borrowing is subject to variable interest rates linked to the Bank of England (BoE) base rate, meaning it is subject to interest rate risk if the base rate increases. The BoE made its 12th consecutive rate increase in May, by a further 25 basis points to 4.5%, its highest level since 2008. The MPC reaffirmed its commitment to adjust Bank Rate as necessary to

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return inflation to the 2% target sustainably in the medium term, in line with its remit. Accordingly the Council's Treasury Management advisor Arlingclose has believes it is more likely than not that Bank Rate increases to 4.75% in June 2023.

The Council has set aside £1.6m in reserves to mitigate variable interest rate exposure which more than covers this interest exposure scenario. In addition, the Council continually monitors the capital programme throughout the year and will borrow to address requirements driven by the cash flow forecast, including updates on the level of capital expenditure being incurred against the programme budget.

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 fixed rate borrowing were:

Table 8: Maturity Structure of Borrowing

	31/03/23 Actual	Upper Limit	Lower Limit	Complied
Under 12 months	27%	60%	0%	✓
12 months and within 24 months	2%	50%	0%	✓
24 months and within 5 years	2%	50%	0%	✓
5 years and within 10 years	5%	75%	0%	✓
10 years and above	64%	100%	25%	✓

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 interest rate changes.

Table 9: Sums invested for more than one year

	2022/23 Maximum actual position £m	31/03/23 Actual £m	2022/23 Limit £m	Complied
Sums invested for longer than one year	0	0	20	✓

Other Non-Treasury Holdings and Activity

22. Although not classed as treasury management activities, the CIPFA Code requires the Authority to report on investments for policy reasons outside of normal treasury management. This includes service investments for operational and/or regeneration as well as commercial investments which are made mainly for financial reasons.

23. The Authority holds the following non-treasury investments:
    - £122m of directly owned investment property
    - £234m of loans to Halsey Garton Property Ltd
    - £93m of equity investments in Halsey Garton Property Ltd
    - £7m of loans to Halsey Garton Residential Ltd
    - £4m of equity investments in Halsey Garton Residential Ltd
    - £2m of loans to other subsidiaries

24. Such loans and investments have been approved in accordance with the Council's agreed processes. A register of such investments is maintained and performance information is reported to the Strategic Investment Board or the Shareholder and Investment Panel, in accordance with their Terms of Reference.

25. These non-treasury investments generated £8m of investment income for the Authority after taking account of direct costs and interest payable.

Implications:

Financial

26. The financial implications of this report are discussed in paragraph 16-18 and have been included in the outturn report to Cabinet on 30 May 2023.

Equalities and Diversity Implications

27. There are no direct equities implications of this report.

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Risk Management Implications

28. The risk management arrangements in relation to treasury management are discussed in paragraph 21.

Next steps:

i. The treasury team will continue to monitor the UK and overseas banking sector and will continue to update this Committee as appropriate.

ii. In line with the requirements the CIPFA Code, this Committee will receive a half yearly report on the Council's treasury management activities in November 2023 and a full year report for 2023/24 after the financial year end.

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Sources/background papers:
Capital Budget, Prudential Indicators & Treasury Management Strategy 2022/23
CIPFA Code of Practice for Treasury Management (2021 Edition)
CIPFA Prudential Code for Capital Finance in Local Authorities (2021 Edition)

Annexes:
Annex 1 - Arlingclose commentary on the External Context for Treasury Management activity – April 2023
Annex 2 - Arlingclose and Market Projections – 15 May 2023

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