SURREY
COUNTY COUNCIL

Audit & Governance Committee
5 June 2024

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2023/24 Treasury Management Outturn Report

Purpose of the report:

This report summarises the Council's treasury management activities during 2023/24, 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 2023/24 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 2023/24, including the treasury management prudential indicators.

2. The Authority's Treasury Management Strategy Statement and Prudential Indicators for 2023/24 were approved at Audit & Governance Committee on 18 January 2023 and formed part of the Budget Setting Papers approved by the County Council on 7 February 2023. 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 2024).

4. Interest rate forecast, provided by our expert Treasury Management Advisors, Arlingclose is included in Annex 2 (produced in May 2024).

Treasury Management Annual Report 2023/24

Overview

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5. On 31 March 2024, the Authority had net borrowing of £702m arising from its revenue and capital income and expenditure, an increase of £166m since 31 March 2023. 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. The Treasury Management Strategy for 2023/24, approved by Audit & Governance Committee in January 2023, 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.

7. Net borrowing has increased over the period due to a reduction in working capital and 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

	31/03/23 Balance £m	**2023/24 Movement £m**	**31/03/24 Balance £m**
General Fund CFR	1,389	128	1,517
Less PFI Liabilities	(81)	(5)	(86)
Gross Borrowing Requirement	**1,308**	**123**	**1,431**
Less usable reserves and working capital	(772)	43	(729)
Net Borrowing Requirement	**536**	**166**	**702**

Note: Columns may not sum due to rounding

8. The Council also manages cash on behalf of Surrey Police and Crime Commissioner, the balance of which was £36m as at 31 March 2024. The Council accounts for this as short-term borrowing. The treasury management position as at 31 March 2024 and the year-on-year change is show in table 2 below.

Table 2: Treasury Management Summary

	31/03/23 Balance £m	2023/24 Movement £m	31/03/24 Balance £m
Long-term borrowing	466	(5)	461
Short-term borrowing	134	112	246
Surrey Police	33	3	36
Total borrowing	**633**	**110**	**743**
Money Market Funds	(97)	56	(41)
Net borrowing	**536**	**166**	**702**

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Borrowing Strategy & Activity

9. As outlined in the treasury strategy, the Authority's chief objective when borrowing has been to strike an appropriately low risk balance between securing lower 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. 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. The Authority's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio.

10. Interest rates have seen substantial rises over the last two years, although these rises have now begun to plateau. Gilt yields fell in late 2023, reaching April 2023 lows in December 2023 before rebounding to an extent in the first three months of 2024. Gilt yields have remained volatile, seeing upward pressure from perceived sticker inflation at times and downward pressure from falling inflation and a struggling economy at other times.

11. On 31 December, the PWLB certainty rates for maturity loans were 4.74% for 10-year loans, 5.18% for 20-year loans and 5.01% for 50-year loans. Their equivalents on 31 March 2023 were 4.33%, 4.70% and 4.41% respectively.

12. The cost of short term borrowing from other local authorities has generally risen with Base Rate over the year. Interest rates peaked at around 7% towards the later part of March 2024 as many authorities required cash at the same time. These rates have fallen back to more normal market levels in April 2024.

13. At 31 March 2024, the Authority held £743m of borrowing, a increase of £110m 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

	31/03/23 Balance £m	2023/24 Net Movement £m	31/03/24 Balance £m	31/03/24 Rate %
Public Works Loan Board (PWLB)	456	(5)	451	3.67
Banks (fixed-term)	10	-	10	5.00
Local authorities (short-term)	134	112	246	6.22
Surrey Police & Crime Commissioner	33	3	36	5.28
Total borrowing	**633**	**110**	**743**	

14. The Authority's borrowing decisions are not predicated on any one outcome for interest rates and a balanced portfolio of short- and long-term borrowing was maintained.

15. No new long term borrowing was undertaken during 2023/24, as internal borrowing was maximised and short-term borrowing was utilised to manage cash flow. Regular discussions take 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.

16. The CIPFA Treasury Management Code now defines treasury management investments as those investments which arise from the Authority's cash flows to 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.

Treasury Investment Activity

17. 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.

18. 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.

19. The Council's average daily level of cash investments was £89.4m during 2023/24, compared to an average of £113.7m during 2022/23. This reflects the Council's strategic policy to maintain sufficient liquidity during this time and continue to borrow over shorter periods when appropriate. 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 2023/24, due to cash balances being held to maintain sufficient liquidity.

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

Table 4: Investment Position (Treasury Investments)

	31/03/23 Balance £m	2023/24 Net Movement £m	31/03/24 Balance £m	31/03/24 Rate* %
Money Market Funds	97	56	41	4.99
Total Investments	**97**	**56**	**41**	**4.99**

*weighted average rate earned in the year

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21. The weighted average return on all investments the Council received in the year to 31 March 2024 was 4.99%. 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

22. 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	25.1	28.7	3.6
Interest Received	(1.5)	(6.1)	(4.6)
MRP	29.4	26.9	(2.5)

23. 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 2022/23 financial year, and less borrowing required to fund the capital spend.

24. The over recovery 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

25. All treasury management activities undertaken during 2023/24 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

	2023/24 Maximum actual position £m	31/03/24 Actual £m	2023/24 Operational Boundary £m	2023/24 Authorised Limit £m	Complied
Underlying Borrowing	760	743	1,150	1,320	✓

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26. 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 2023/24.

Table 7: Investment Limits

	2023/24 Maximum actual position £m	31/03/24 Actual £m	2023/24 Limit £m	Complied
UK Central Government	0	0	Unlimited	✓
Money Market Funds	213	41	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 Prudential Indicators

27. As required by the 2021 CIPFA Treasury Management Code, 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 £246m of short-term borrowing at 31 March 2024, with an additional £223m expected to be required to finance the 2024/25 capital programme. 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. Having begun the financial year at 4.25%, the Bank of England's Monetary Policy Committee (MPC) increased Bank Rate to 5.25% in August 2023. Bank Rate was maintained at 5.25% through to March 2024. The MPC's focus remained on assessing how long interest rates would need to be restrictive in order to control inflation over the medium term. Arlingclose, the authority's treasury adviser, maintained its central view that 5.25% remains the peak in Bank Rate and that interest rates will most likely start to be cut later in the second half of 2024.

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The Council has set aside £1.6m in reserves to mitigate variable interest rate exposure. 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

	31/03/24 Actual	**Upper Limit**	**Lower Limit**	**Complied**
Under 12 months	39%	60%	0%	✓
12 months and within 24 months	1%	50%	0%	✓
24 months and within 5 years	2%	50%	0%	✓
5 years and within 10 years	4%	75%	0%	✓
10 years and above	54%	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

	2023/24 Maximum actual position £m	**31/03/24 Actual £m**	**2023/24 Limit £m**	**Complied**
Sums invested for longer than one year	0	0	20	✓

Other Non-Treasury Holdings and Activity

28. The definition of investments in the Treasury Management Code now 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 required to be reported on and are categorised as either for service purposes (made explicitly to further service objectives and/or regeneration) or for commercial purposes (made primarily for financial return).

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29. The Authority holds the following non-treasury investments as at the 31 March 2024:
    - £75m 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

30. 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.

31. These non-treasury investments generated £5m of investment income for the Authority after taking account of direct costs, minimum revenue provision and interest payable.

Future Changes

32. Following three rounds of consultation, the Department for Levelling Up, Housing and Communities (DLUHC) published its final consultation response, amendment regulations and revised statutory guidance on Minimum Revenue Provision (MRP) in April 2024.

33. The Council have participated in the consultations and reviewed the final guidance and concludes that the changes will have minimal impact, as the Minimum Revenue Provision Policy for 2024/25 considered by this Committee in January 2024 and full Council in February 2024 is compliant with the changes.

Implications:

Financial

34. The financial implications of this report are discussed in paragraphs 22-24 and have been included in the outturn report to Cabinet.

Equalities and Diversity Implications

35. There are no direct equalities implications of this report.

Risk Management Implications

36. The risk management arrangements in relation to treasury management are discussed in paragraph 27.

Legal Implications – Monitoring Officer

37. There are no direct legal implications of this report.

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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 2024 and a full year report for 2024/25 after the financial year end.

Report authors: Nikki O'Connor, Strategic Finance Business Partner (Corporate)

Contact details: nicola.oconnor@surreycc.gov.uk

Sources/background papers:

- Capital Budget, Prudential Indicators & Treasury Management Strategy 2023/24
- CIPFA Code of Practice for Treasury Management (2021 Edition)
- CIPFA Prudential Code for Capital Finance in Local Authorities (2021 Edition)

Annexes/Appendices:

- Annex 1 - Arlingclose commentary on the External Context for Treasury Management activity – April 2024
- Annex 2 - Arlingclose interest rate forecast

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