Leeds
CITY COUNCIL

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TREASURY MANAGEMENT OUTTURN 2022/23

Date: 21st June 2023

Report of: Chief Officer Financial Services

Report to: Executive Board

Will the decision be open for call in? ☒Yes ☐No

Does the report contain confidential or exempt information? ☐Yes ☒No

Brief Summary

1.1 This report sets out for Members' approval the Treasury Management Outturn report for 2022/23.

1.2 This report shows that net external debt as at 31st March 2023 was £2,397m which is £5m lower than the February 2023 forecast. This movement is due to lower than anticipated revenue balances of £7m and a decrease in assumed treasury borrowing of £12m for the capital programme. The level of debt and liabilities should be viewed in the context of the Council's long-term assets which were valued at £6.779bn as at 31st March 2022. The equivalent total asset value at 31st March 2023 is not yet available, as the Council's 2022/23 draft accounts are not yet completed.

1.3 The level of debt has remained within the Authorised Limit and Operational Boundary as approved by the Council in February 2023.

1.4 The average rate of interest paid on the Council's external debt was 3.22% for 2022/23 down slightly from 3.28% recorded in 2021/22.

1.5 The outturn position for debt costs within the revenue budget was an underspend of £6.4m before taking into account the impact on MRP of applying the remaining balance of the Merion House capital receipt to reduce debt. This £6.4m underspend arose primarily because of opportunities to borrow at lower interest rates during the year, lower than anticipated overall borrowing requirement and lower than anticipated MRP. External interest income was also higher than had been budgeted for, as interest rates rose during the year.

1.6 A further saving of £22.3m in the level of MRP has been generated as a result of applying the remaining Merrion House capital receipt to reduce debt. This saving has been transferred to earmarked reserves to be carried forward for use in future years.

Recommendations

That the Executive Board:

2.1 Note the Treasury Management outturn position for 2022/23 and that treasury activity has remained within the treasury management strategy and policy framework

What is this report about?

3.1 This Treasury Management Outturn Report for 2022/23 provides a final update on loans undertaken to fund the capital programme requirements for both General Fund and HRA. Treasury activity during the year was conducted within the approved borrowing limits for the year and resulted in an overall saving to the revenue budget of £6.4m.

What impact will this proposal have?

4.1 The 2022/23 treasury management strategy was approved by Executive Board on 9th February 2022. This report provides members with a final update on Treasury Management strategy and operations in 2022/23.

How does this proposal impact the Three Pillars of the Best City Ambition?

☒Health and Wellbeing ☒Inclusive Growth ☒Zero Carbon

5.1 The Treasury Management strategy secures funding to support the Council's Policies and City Priorities as set out in the Council's capital programme and is consistent with the Best City Ambition and 3 key pillars.

5.2 Equality, diversity, cohesion, and integration requirements are addressed as part of individual capital scheme and programme approvals. The borrowing to deliver these capital schemes is executed through treasury strategy and as such there are no further equality, diversity, cohesion, and integration issues.

What consultation and engagement has taken place?

Wards Affected:
Have ward members been consulted? ☐Yes ☒No

6.1 This report is an update on strategy as presented to Executive Board in February 2023, as such no consultation has taken place. However, consultation with the Council's treasury advisors takes place regularly throughout the year.

6.2 The borrowing requirement is an outcome of the capital programme which has been the subject of consultation and engagement as outlined in the February capital programme report approved by full Council.

What are the resource implications?

7.1 This update on the treasury strategy recognises the borrowing necessary to fund the capital programme requirements of both General Fund and HRA. The revenue costs of borrowing are included within the revenue budgets of the General Fund and HRA.

7.2 A surplus of £6.4m has been generated, primarily because of opportunities to borrow at lower interest rates during the year, a lower than anticipated overall borrowing requirement and lower than anticipated MRP. External interest costs were £5.2m below budget, of which £4.0m was attributable to the general fund and the remainder to the HRA. The MRP charge for the year was £1.9m lower than had been budgeted for, largely as a result of slippage in the 2021/22 capital programme. External interest income was also £1.0m higher than had been budgeted for, as interest rates rose during the year.

7.3 The total underspend of £28.7m in the debt budget also includes the application of the remaining £22.3m balance of the Merrion House capital receipt which has been used to repay debt, with a consequent reduction in the level of MRP. The resulting saving has been transferred to an earmarked revenue reserve to be carried forward to future years.

What are the key risks and how are they being managed?

8.1 This report sets out the performance against the 2022/23 Treasury strategy. The execution of the strategy and associated risks are kept under regular review through:

- Monthly reports to the officer led Finance Performance Group.
- Quarterly strategy meetings with the Chief Officer Financial Services and the Council's treasury advisors and
- Regular market, economic and financial instrument updates, and access to real time market information.

8.2 The above monitoring mitigates the directorate level risk of "Failure to recover money invested in other financial institutions" and in addition the Treasury Management Strategy is linked to the corporate risk on 'Financial Forecasting'.

<u>Review of Strategy 2022/23</u>

8.3 Table 1, shows that net borrowing in 2022/23 was £2,397m, £5m lower than the February 2023 forecast. This movement is due to lower than anticipated revenue balances of £7m, and a decrease in assumed treasury borrowing of £12m for the capital programme. The actual movement in the capital programme is explained in the Financial Outturn report elsewhere on the agenda.

TABLE 1

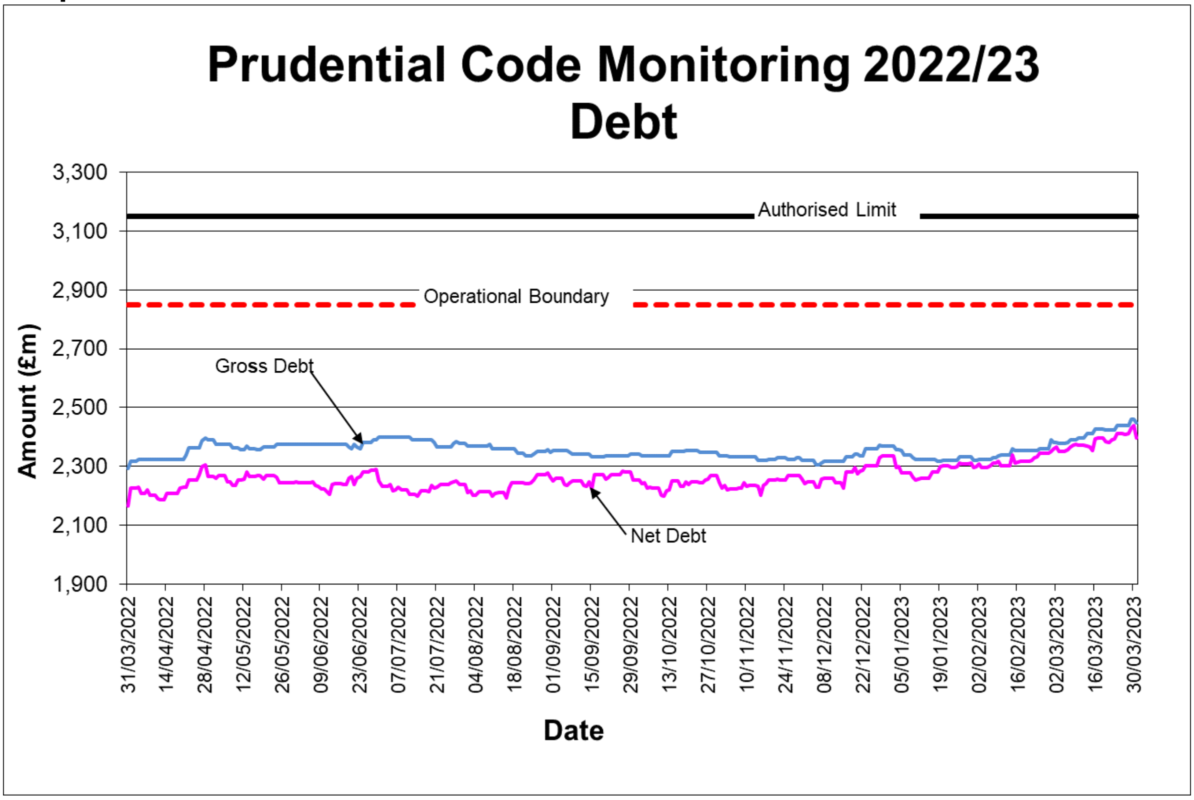
ANALYSIS OF BORROWING 2022/23	2022/23 Nov 22 Report £m	2022/23 Feb 23 Report £m	2022/23 This Report £m
Net Borrowing at 1 April	2,165	2,165	**2,165**
New Borrowing for the Capital Programme – GF	152	123	**107**
New Borrowing for the Capital Programme – HRA	43	36	**40**
Debt redemption costs charged to Revenue (Incl HRA)	(61)	(60)	**(60)**
Reduced/(Increased) level of Revenue Balances	138	138	**145**
Net Borrowing at 31 March	2,437	2,402	**2,397**
Capital Financing Requirement*			**2,783**
Other long term liabilities capital financing requirement			**519**
Net Borrowing 31st March comprised as follows			
Long term Fixed	2,259	2,279	2,279
Variable (less than 1 Year)	20	0	0
New Borrowing	182	147	154
Short term Borrowing	16	16	16
Total External Borrowing	2,477	2,442	2,449
Less Investments	40	40	52
Net External Borrowing	**2,437**	**2,402**	**2,397**
% borrowing funded by short term and variable rate loans	9%	7%	7%
Limit for variable rate Borrowing	40%	40%	40%

***** The Capital Financing Requirement (CFR) is the maximum level of debt (i.e. borrowing and finance leasing) that the Council can hold for its current year capital purposes. The Council is also allowed to borrow in advance for up to two future years capital programmes.

8.4 The level of debt and liabilities should be viewed in the context of the Council's assets which were valued at approximately £6.779bn as at 31st March 2022. The equivalent total asset value at 31st March 2023 is not yet available, as the Council's 2022/23 draft accounts are not yet completed. The Capital programme outturn position is reported in the June Financial Performance - Outturn Report to Executive Board elsewhere on the agenda.

8.5 In 2022/23 the level of debt remained within Authorised limits during the year, and this is shown in Graph 1. The Authorised Limit is the maximum permitted amount of borrowing the Council can have outstanding at any given time and has not been breached during 2022/23. The Operational Boundary is a key management tool and can be breached temporarily depending on cash flow. This limit acts as a warning mechanism to prevent the Authorised Limit from being breached. Treasury Management activity has resulted in no breach of its prudential indicators, which are detailed in Appendix A. All other prudential indicators are within the normal tolerance levels of treasury management.

Graph 1



8.6 The 2022/23 borrowing strategy was initially to fund the capital programme borrowing requirement from longer term borrowing to reduce interest rate risk, taking advantage of long-term funding opportunities when they arise during the year. Short term borrowing is used during the year to temporarily fund the borrowing requirement where necessary, ensuring that long term borrowing is not undertaken at unfavourable rates. Whilst this approach continues to deliver lower costs of financing, the level of borrowing funded by short terms loans has increased to £170m at 31/03/2023. During 2022/23 both actual short- and long-term rates have increased significantly however the Council's advisors are forecasting that rates will fall back from currently levels which are the highest seen in over a decade. As a result, the strategy has been updated to fund from short term until longer term rates fall at which time short term funding will be switched into lower cost longer term funding. In addition, the government will bring forward a new discounted PWLB policy margin to support local authorities borrowing for Housing Revenue Accounts and the delivery of social housing. The Council's HRA currently has capacity to borrow £129m at these reduced rates when they are introduced by HMT in June.

8.7 Since the economic update to Members in February, the uncertainty surrounding the impact of the Covid-19, Ukraine and continuing supply chain disruption have provided the backdrop for the economic performance outlined below. Inflation is expected to fall reasonably quickly from its current levels of over 10% during the rest of 2023/24 although the exact pace and timing of this fall remains uncertain.

- The Monetary Policy Committee (MPC) increased the bank rate from its emergency level of 0.10% to 0.25% on 16/12/2021. Since that initial move the MPC have steadily raised rates a further 11 times to its current level of 4.50% from 11th May 2023. Whilst base rate is currently at 4.50% many market commentators expect that the peak may be higher than this however expectations are that by the end of 2023/24 a fall in base rate will be seen. In addition, the MPC had issued total Quantitative Easing (QE) of £895bn although from November 2022 the MPC has been slowly unwinding this in a process called Quantitative

Tightening (QT) by selling some holding into the market and allowing other to naturally mature.

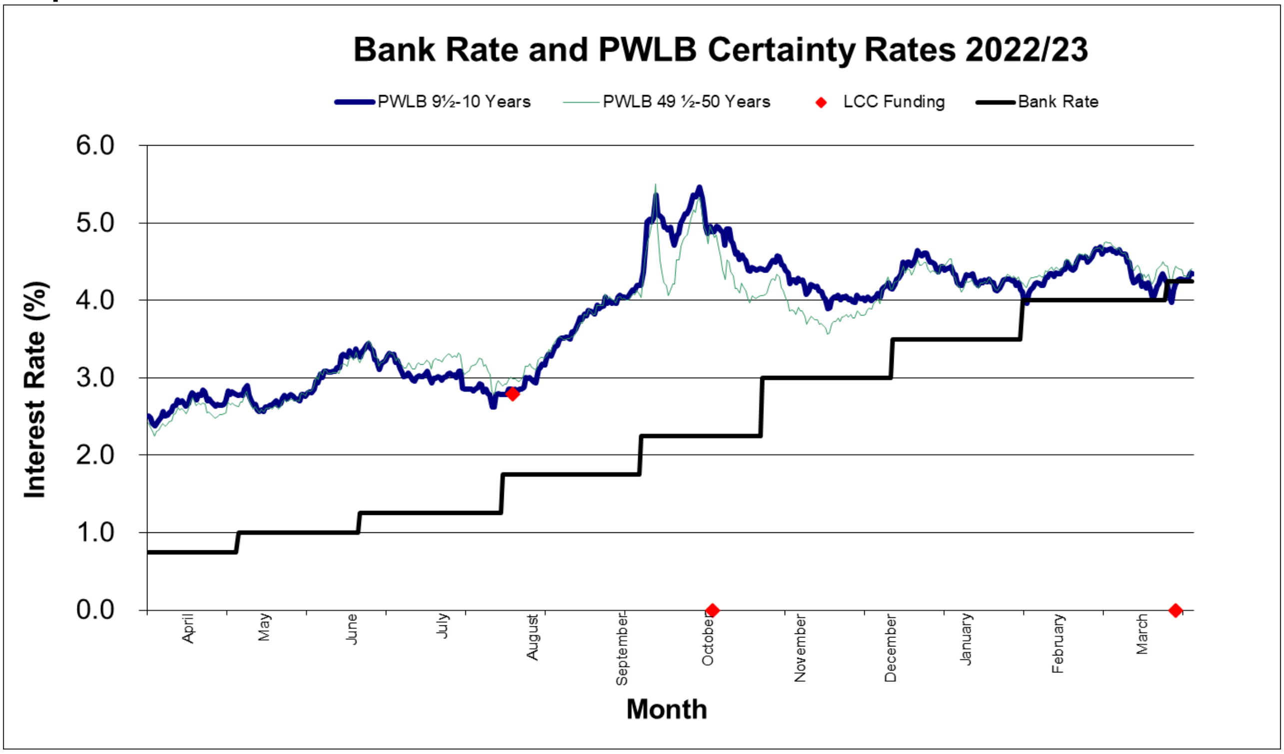
- During 2021/22 and 2022/23 inflation pressures Increased from around 2% to a peak in October 2022 of 11.1% and these have squeezed household disposable incomes. Inflation as at April 2023 has fallen back to 8.7% which was 0.5% above market expectations and whilst inflation is expected to fall further during 2023/24 as supply side shocks in food and energy begin to fall out of the calculation it is an indication that inflation may remain higher than the 2% target for longer.
- As inflation has risen GDP has subsequently fallen with the last 4 quarters posting growth rates which whilst positive are very close to 0%. This has been against a backdrop of stubborn inflationary pressures, easing of COVID restrictions in most developed economies, the ongoing Russian Invasion of Ukraine and changing UK policy priorities.
- The unemployment rate in the UK has increased from a low of 3.50% in August 2022 to 3.90% in March 2023 however this is still considered to indicate a tight labour market. When taken with CPI Inflation this has also driven the growth in wages in the economy which has been running at around 6% during most of the year with March posting a figure of 5.80%.
- These factors make it a difficult judgement call as to when to begin reducing base rates and by how much across many developed economies.
- In the United States the hawkish tone from Federal Open Markets Committee (FOMC) members has led to markets pricing in further increases of 25-50bp of rate tightening from its current level of 4.75% to 5.00%. The FOMC is also expected to continue unwinding its stock of QE held on its balance sheet however recent bank failures may cause the FOMC to be more circumspect in this regard until stability is assured. Inflation in the US in currently 4.90% down from the US peak of 9.10% in June 2022
- More positively the US economy has been adding between 250k to 350k of jobs per month except for March 2023 which was 165k. US unemployment currently stands at 3.4% posted in April and again indicates a very tight labour market.
- In Europe, the inflation rate has fallen below 7% however the ECB is expected to want to dampen Inflationary pressures so further increases in policy rates from the current 3.75% are expected. Overall EU growth is like the UK expected to be subdued at 0.1% in March and with unemployment across the area falling to 6.5%.

8.8 Graph 2 shows the movement in PWLB interest rates over the year. Underlying Gilt yields have risen during 2022/23 by around 1.5% to 2.0% over the year in longer dated periods. Longer term PWLB rates (49½-50 year) have varied during the year but ended the year at 4.41% but reached a high of 5.51% in late September and achieved a low point of 2.25% in April 2022. Shorter term rates (9½-10 year) have also risen from the start of the year and again hit a low point in early April. PWLB rates can now be summarised as follows

- **PWLB Standard Rate** is gilt plus 100 basis points (G+100bps)
- **PWLB Certainty Rate** is gilt plus 80 basis points (G+80bps)
- **Local Infrastructure Rate** is gilt plus 60bps (G+60bps)

Graph 2 also shows the long-term funding activity undertaken as detailed in Table 2.

Graph 2



8.9 The strategy for 2022/23 has resulted in a surplus of £6.4m, primarily due to funding at lower rates than anticipated and by lower borrowing activity due to higher than anticipated revenue balances and lower than anticipated MRP.

8.10 Table 2 shows £23.426m of longer-term borrowing was secured during the year with £20m of this being from the PWLB together with £3.42m of SALIX funding. The table also shows that while no market loans options were exercised during the entire year, £1.3m of normal EIP (Equal Instalment of Principal) repayments were made on SALIX loans, whilst £37.6m of PWLB loans reached maturity during the period. Approximately half of market loans outstanding are termed Lenders Option Borrowers Option (LOBO) and contain clauses which allows the lender, at pre-determined dates, to vary the interest rate on the loan. If one of these options is exercised and the new rate is not accepted, the borrower then has the option to repay the loan without penalty. No options were exercised during 2022/23.

Table 2

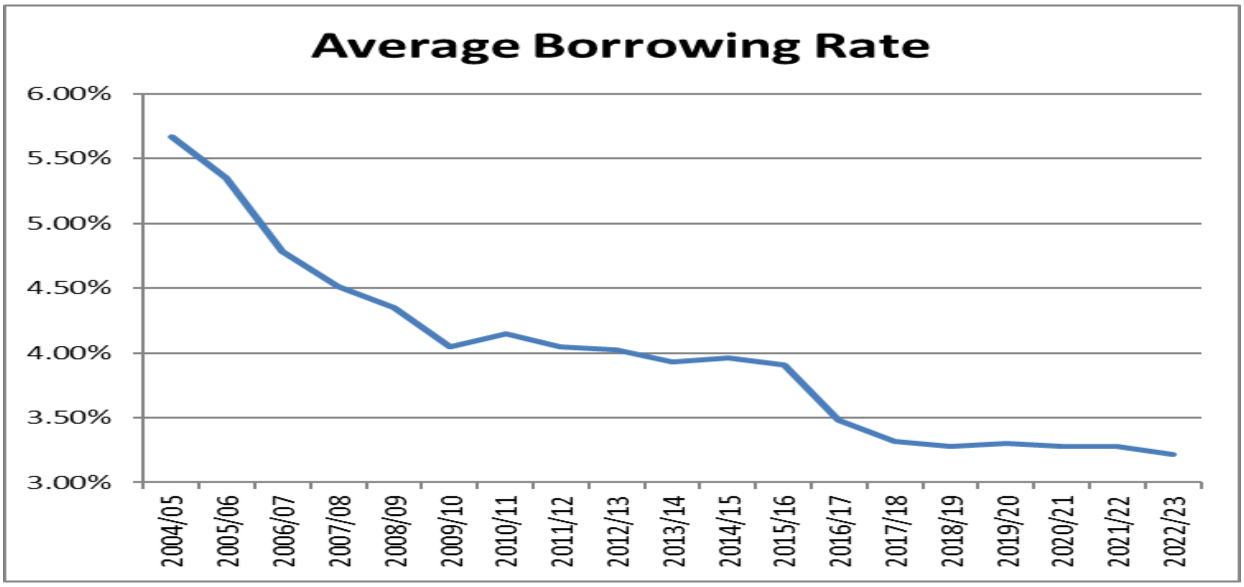
Loan repayments and borrowing 2022/23								
Loan Repayments					New Borrowing			
Date	Lender	Amount (£m)	Original Rate (%)	Discount Rate	Date	Amount (£m)	Term (Years)	Interest Rate (%)
PWLB Loans					PWLB			
04/03/2022	PWLB	8.812	3.74%	n/a	09/08/2022	20.000	48	2.79
17/05/2022	PWLB	8.812	3.26%	n/a				
11/05/2022	PWLB	10.000	2.95%	n/a				
21/05/2022	PWLB	10.000	2.90%	n/a				
Sub Total		**37.624**				**20.000**		
Non PWLB Loans					Non PWLB Loans			
01/04/2022	SALIX PH1	0.315	0.00	n/a	SALIX PH3	1.710	8	0.00
03/10/2022	SALIX PH1	0.315	0.00	n/a	SALIX PH3	1.710	8	0.00
01/09/2022	SALIX WLL	0.023	0.00	n/a				0.00
01/03/2023	SALIX WLL	0.024	0.00	n/a				
01/03/2022	SALIX PH2	0.618	0.00	n/a				
Sub Total		**1.295**				**3.420**		
Total		**38.919**			**Total**	**23.420**		

* Taken for the HRA account
Salix repayments are EIP Instalments

Interest Rate Performance and Average Maturity Profile

8.11 The average rate of interest paid on the Council's external debt was 3.22% (a small reduction from 3.28% in 2021/22) as shown in Graph 3. This stability in the average rate is due to the relatively low level of volatility in the external debt position and the impact of the timing of borrowing as well as the level of revenue balances used internally.

Graph 3



8.12 Whilst the average borrowing rate remains relatively low it is important to note the average maturity profile of the Council's debt. The average length of all loans to final maturity including temporary loans is 32.7 years. The average length of all loans to the next option date including temporary loans is 28.6 years. This provides a large degree of funding certainty within the overall debt portfolio.

What are the legal implications?

9.1 The operation of the Treasury Management function is governed by provisions set out under part 1 of the Local Government Act 2003 whereby the Council is required to have regard to the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code for Capital Finance in Local Authorities. In particular:

- The Prudential Code requires that full Council set certain limits on the level and type of borrowing before the start of the financial year together with several Prudential Indicators.
- Any in year revision of these limits must be approved by Council.
- Policy statements are prepared for approval by the Council at least two times a year.

9.2 Updated versions of both the Prudential Code for Capital Finance in Local Authorities and the Treasury Management in the Public Services Code of Practice were published in December 2021, with the accompanying guidance notes for practitioners being published in late January 2022. Although the new Codes applied immediately, the Prudential Code states that the changes to reporting requirements that they introduce can be deferred until the 2023/24 financial year. These new reporting requirements include changes to the capital strategy, prudential indicators, and investment reporting. The evaluation of these new requirements has been completed during 2022/23 and the strategy report presented to

Executive board and full Council in February 2023 which included an update on 2022/23 were compliant with the new requirements.

Options, timescales and measuring success

a) What other options were considered?

This report provides the outturn position for the 2022/23 Treasury Management strategy. This update is provided to Executive Board regarding Treasury Management operation and activity. As such other options are not considered in this report.

b) How will success be measured?

Treasury Management continues to adhere to its governance framework including the CIPFA Code of Practice, the Prudential Codes 2021 and revised CIPFA guidance notes issued in 2022. All borrowing and investments undertaken have been compliant with the governance framework. The updated CIPFA Codes have been reviewed to identify any changes which are necessary for the Council to continue to comply with them, and these changes have been introduced during 2022/23, in line with the required timescales. The full adoption of the codes is required for the 2023/24 financial year. Success will therefore be the continued optimal performance of the Treasury Management function within this framework.

Benchmarking of Treasury Management activity is only undertaken on an ad-hoc basis as the structure of debt portfolios and balance sheets of similar authorities often reflect the timing of past spending and financing decisions and therefore can lead to anomalies. The CIPFA Prudential Code makes it clear that prudential indicators should not be used for benchmarking purposes for this reason. The latest benchmarking exercise was undertaken in January 2021 as at the balance sheet date of 31/03/2020 for a comparison of external debt in relation to fixed assets for the core cities and significant variations in the resultant metrics were noted. Comparative information on core cities balance sheets has been provided by the Council’s Treasury advisers during the year.

c) What is the timetable for implementation?

This report is to confirm the successful operation of the Treasury Management strategy within the established legal and operational framework and is a continuous and on-going process.

Appendices

1. Appendix A — Prudential indicators 2022/23 to 2024/25
2. Appendix B — Liability benchmark 2022/23
3. Appendix C — Prudential Code Monitoring – Debt 2022/23

Background papers

None

Appendix A - TMSS PI's

DM14b	Notes		Current 2022.23	Year+1 2023.24	Year+2 2024.25
PRUDENTIAL CODE INDICATORS					
CAPITAL EXPENDITURE					
Estimate of Capital Expenditure	a				
General Fund		£k	301,190	372,921	306,875
Housing Revenue Account		£k	145,927	144,529	170,152
Total		£k	447,117	517,450	477,027
Capital Financing Requirement	b				
Borrowing - General Fund		£k	2,024,777	2,138,962	2,223,993
Borrowing - Housing Revenue Account		£k	758,600	793,318	841,877
Sub Total Borrowing		£k	2,783,377	2,932,280	3,065,870
Other Long Term Liabilities - GF		£k	411,381	386,110	359,397
Other Long Term Liabilities - HRA		£k	107,623	99,376	90,579
Sub Total Other Long Term Liabilities		£k	519,004	485,486	449,976
Total Capital Financing Requirement		£k	3,302,381	3,417,766	3,515,846
EXTERNAL DEBT					
Operational Boundary	c				
External Borrowing		£k	2,850,000	2,850,000	2,900,000
Other Long Term Liabilities		£k	610,000	580,000	550,000
Total			3,460,000	3,430,000	3,450,000
Authorised Limit	c				
External Borrowing		£k	3,150,000	3,200,000	3,200,000
Other Long Term Liabilities		£k	630,000	600,000	570,000
Total		£k	3,780,000	3,800,000	3,770,000
Actual External Debt (year end Forecast)	d				
PWLB		£k	1,805,172	1,763,737	1,738,737
Market (Inc LOBO)		£k	474,319	472,084	469,529
Short term (Actual)		£k	170,000	0	0
Short term (Forecast)		£k	0	395,356	601,911
Total Gross External Debt		£k	2,449,492	2,631,177	2,810,177
Other Long Term Liabilities		£k	519,004	485,486	449,976
Total Including OLTL		£k	2,968,496	3,116,663	3,260,153
Gross Debt and the CFR	e				
External Borrowing			ok	ok	ok
Other Long term Liabilities			ok	ok	ok
Total Gross Debt and the CFR			ok	ok	ok
AFFORDABILITY					
Estimate of Financing Cost to Net revenue Stream	f				
External Borrowing Only - General Fund					
Financing Cost		£k	109,105	123,129	128,774
Net Revenue Stream		£k	521,942	573,357	615,012
Ratio		%	20.90%	21.48%	20.94%
Including Other Long Term Liabilities - GF	f				
Financing Cost		£k	157,524	171,361	176,729
Net Revenue Stream		£k	521,942	573,357	615,012
Ratio		%	30.18%	29.89%	28.74%
External Borrowing Only - Housing Revenue Account	f				
Financing Cost		£k	27,726	30,182	30,919
Net Revenue Stream		£k	249,609	266,931	277,599
Ratio		%	11.11%	11.31%	11.14%
Including Other Long Term Liabilities - HRA	f				
Financing Cost		£k	44,253	46,572	47,140
Net Revenue Stream		£k	249,609	266,931	277,599
Ratio		%	17.73%	17.45%	16.98%

INVESTMENTS					
Limit on non-Treasury Loans	g		80,000	80,000	80,000
Limit on non-Treasury Investments	g		250,000	250,000	250,000
Limit on Non Treasury loans and Investments			330,000	330,000	330,000
Estimate of Net Income from Investments for Commercial and Service Purposes	g				
Income		£k	7,052	6,710	7,030
Ratio of Income from Commerical and Service Puposes to Net revenue Stream		%	1.35%	1.17%	1.14%

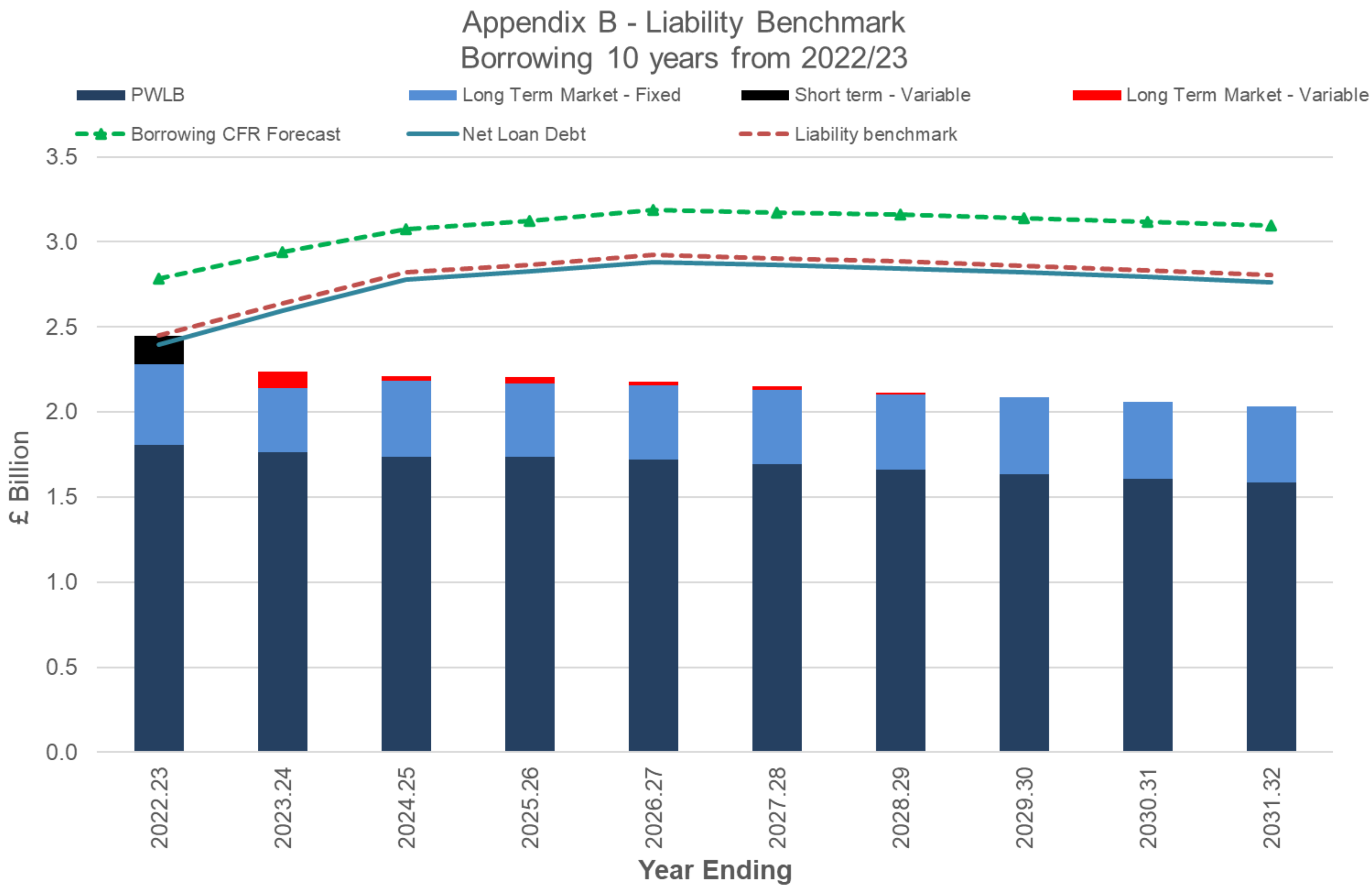
TREASURY MANAGEMENT CODE INDICATORS	
Liability Benchmark for Borrowing	See attached
Liability Benchmark for Investments	Not Applicable

Maturity Structure of Borrowing 2022/23	h	Lower	Upper	Actual 31/03/2023	%
under 12 mths		**0%**	**15%**	314,171	13%
12 mths and within 24 mths		**0%**	**20%**	52,556	2%
24 mths and within 5 years		**0%**	**35%**	157,060	6%
5 years and within 10 years		**0%**	**40%**	142,782	6%
10 years and within 20 years				95,000	
20 years and within 30 years				174,123	
30 years and within 40 years		**25%**	**90%**	679,302	73%
40 years and within 50 years				715,000	
50 years and above				125,000	
				2,454,994	100%

Upper limit for long term Treasury Investments to mature in following years	i	
Year +1		150,000
Year +2		150,000
Year +3		150,000

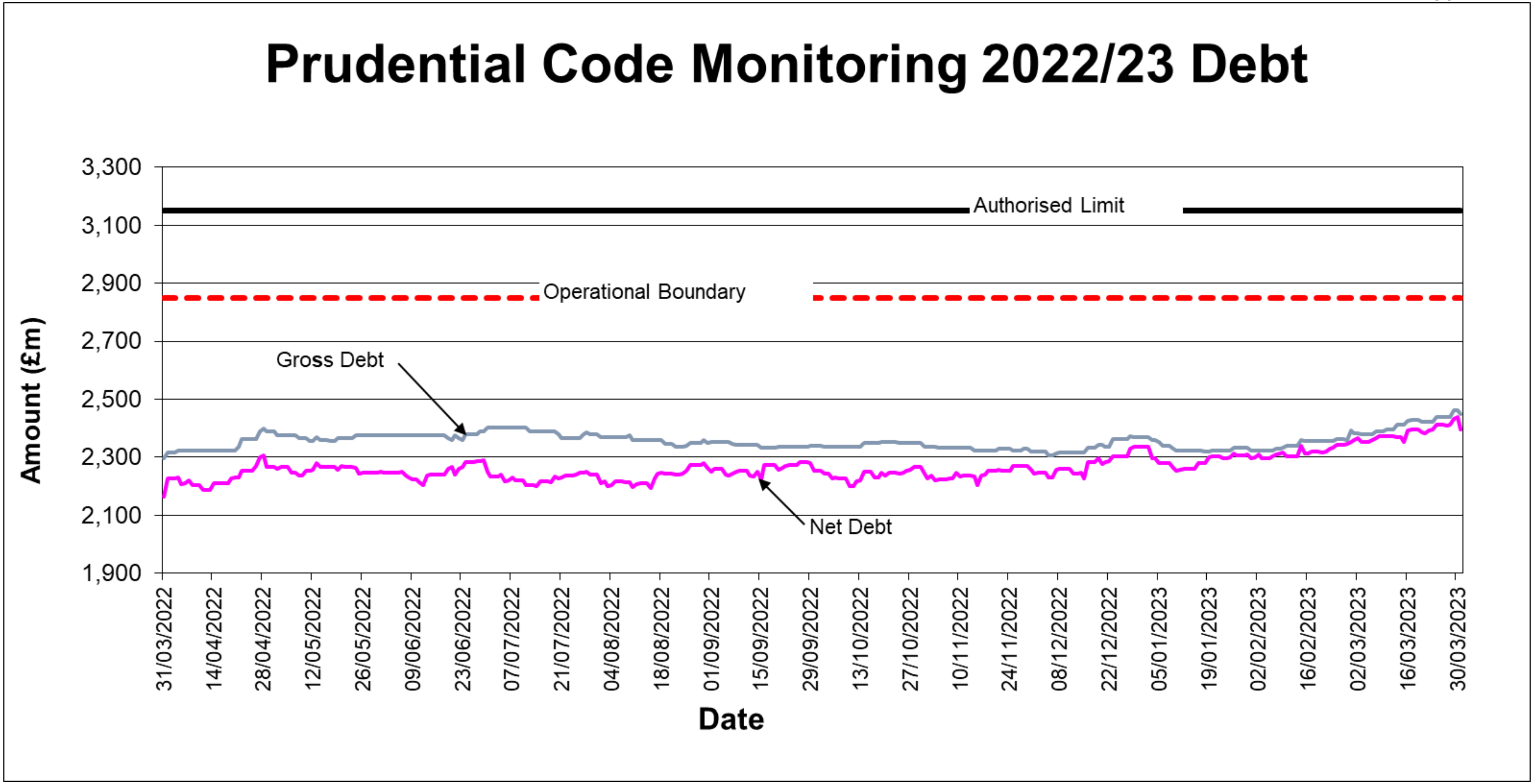
Notes

- a Forecast of capital expenditure for year at period end, actual at year end outturn
- b Forecast of CFR for year end at period end, actual at year end outturn
- c Authorised limit and Operational Boudary as set at the Outturn setting time should only change in exceptional circumstances
- d This is the year end forecast for DEBT and OLTL with Short term being the balancing figure
- e In order to ensure that over the medium term debt will only be for a capital purpose, the local authority should ensure that total gross debt does not, except in the short term, exceed the total of capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years. If in any of these years there is a reduction in the capital financing requirement, this reduction is ignored in estimating the cumulative increase in the capital financing requirement, which is used for comparison with gross external debt. This is a key indicator of prudence. (This is shown as "OK" or "Breach" depending on the result of the above comparison)
- f Code only requires full comparison of debt costs including OLTL to Net revenue Streams however the Council have always reported the external borrowing metrics which are more informative.
- g This is all investments under the code for Service or Commercial purposes and excludes Investments for TM purposes
- h This now includes all external debt including variable and short term external debt
- i This is non specified Treasury Management investments typically with a duration of greater than 364 days



Appendix B - Liability Benchmark
Borrowing 10 years from 2022/23
PWLB
Long Term Market - Fixed
Short term - Variable
Long Term Market - Variable
Borrowing CFR Forecast
Net Loan Debt
Liability benchmark
£ Billion
3.5
3.0
2.5
2.0
1.5
1.0
0.5
0.0
2022.23
2023.24
2024.25
2025.26
2026.27
2027.28
2028.29
2029.30
2030.31
2031.32
Year Ending

Appendix C



Prudential Code Monitoring 2022/23 Debt
Authorised Limit
Operational Boundary
Gross Debt
Net Debt
Amount (£m)
3,300
3,100
2,900
2,700
2,500
2,300
2,100
1,900
31/03/2022
14/04/2022
28/04/2022
12/05/2022
26/05/2022
09/06/2022
23/06/2022
07/07/2022
21/07/2022
04/08/2022
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