Annual Treasury Management Review

2021/22

Telford & Wrekin Council

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Annual Treasury Management Review 2021/22

Purpose

This Council is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2021/22. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management, (the Code), and the CIPFA Prudential Code for Capital Finance in Local Authorities, (the Prudential Code).

During 2021/22 the minimum reporting requirements were that the full Council should receive the following reports:

- an annual treasury strategy in advance of the year,
- a mid-year, (minimum), treasury update report, and
- an annual review following the end of the year describing the activity compared to the strategy, (this report)

The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This report is, therefore, important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by members.

This Council confirms that it has complied with the requirement under the Code to give prior scrutiny to all of the above treasury management reports by the Audit Committee before they were reported to the full Council. Member training on treasury management issues was undertaken during the year on 03/03/2022 in order to support members' scrutiny role.

Executive Summary

During 2021/22, the Council complied with its legislative and regulatory requirements. The key actual prudential and treasury indicators detailing the impact of capital expenditure activities during the year, with comparators, are as follows:

Prudential and treasury indicators	31.3.21 Actual £000	2021/22 Original £000	31.3.22 Actual £000
Capital expenditure			
• Total	57,710	101,855	57,367
Capital Financing Requirement:			
• Total	480,078	541,572	500,140
• Less Other Long Term Liabilities	(50,398)	(50,895)	(50,880)
• Loans CFR	429,680	490,677	449,260
Gross borrowing			
• External Debt	281,085	359,746	282,743
Investments			
• Longer than 1 year	0	0	0
• Under 1 year	20,652	15,000	36,522
• Total	20,652	15,000	36,522
Net borrowing			
• Total	260,433	344,746	246,221

Other prudential and treasury indicators are to be found in the main body of this report. The Director of Finance & HR also confirms that borrowing was only undertaken for a capital purpose and the statutory borrowing limit, (the authorised limit), was not breached.

The financial year 2021/22 continued the challenging investment environment of previous years, namely low investment returns.

Borrowing can only be undertaken to fund capital investment and not to support the revenue budget which supports the delivery of most Council services. The total value of assets held by the Council at 31 March 2022 was £788.4m some £505.7m greater than debt outstanding.

Introduction and Background

This report summarises the following:-

- Capital activity during the year;
- Impact of this activity on the Council's underlying indebtedness, (the Capital Financing Requirement);
- The actual prudential and treasury indicators;
- Overall treasury position identifying how the Council has borrowed in relation to this indebtedness, and the impact on investment balances;
- Summary of interest rate movements in the year;
- Detailed debt activity; and
- Detailed investment activity.

1. The Council's Capital Expenditure and Financing

The Council undertakes capital expenditure on long-term assets. These activities may either be:

- Financed immediately through the application of capital or revenue resources (capital receipts, capital grants, revenue contributions etc.), which has no resultant impact on the Council's borrowing need; or
- If insufficient financing is available, or a decision is taken not to apply resources, the capital expenditure will give rise to a borrowing need.

The actual capital expenditure forms one of the required prudential indicators. The table below shows the actual capital expenditure and how this was financed.

£'000 General Fund	31.3.21 Actual	2021/22 Budget	31.3.22 Actual
Capital expenditure • Capital Programme	57,710	101,855	57,367
Financed in year	35,300	41,642	37,036
Unfinanced capital expenditure	**22,410**	**60,213**	**20,331**

2. The Council's Overall Borrowing Need

The Council's underlying need to borrow for capital expenditure is termed the Capital Financing Requirement (CFR). This figure is a gauge of the Council's indebtedness. The CFR results from the capital activity of the Council and resources used to pay for the capital spend. It represents the 2021/22 unfinanced capital expenditure (see above table), and prior years' net or unfinanced capital expenditure which has not yet been paid for by revenue or other resources.

Part of the Council's treasury activities is to address the funding requirements for this borrowing need. Depending on the capital expenditure programme, the treasury service organises the Council's cash position to ensure that sufficient cash is available to meet the

capital plans and cash flow requirements. This may be sourced through borrowing from external bodies, (such as the Government, through the Public Works Loan Board [PWLB], or the money markets), or utilising temporary cash resources within the Council.

Reducing the CFR – the Council's underlying borrowing need (CFR) is not allowed to rise indefinitely. Statutory controls are in place to ensure that capital assets are broadly charged to revenue over the life of the asset. The Council is required to make an annual revenue charge, called the Minimum Revenue Provision – MRP, to reduce the CFR. This is effectively a repayment of the borrowing need. This differs from the treasury management arrangements which ensure that cash is available to meet capital commitments. External debt can also be borrowed or repaid at any time, but this does not change the CFR.

The total CFR can also be reduced by:

- the application of additional capital financing resources, (such as unapplied capital receipts); or
- charging more than the statutory revenue charge (MRP) each year through a Voluntary Revenue Provision (VRP).

The Council's 2021/22 MRP Policy, (as required by DLUHC Guidance), was approved as part of the Treasury Management Strategy Report for 2021/22 on 04/03/2021.

The Council's CFR for the year is shown below, and represents a key prudential indicator. It includes PFI and leasing schemes on the balance sheet, which increase the Council's borrowing need. No borrowing is actually required against these schemes as a borrowing facility is included in the contract.

CFR (£'000): *General Fund*	31.3.21 Actual	2021/22 Budget	31.3.22 Actual
Closing balance	**480,078**	**541,572**	**500,140**
Less Other Long Term Liabilities	(50,398)	(50,895)	(50,880)
Loans CFR	**429,68**	**490,677**	**449,260**

Borrowing activity is constrained by prudential indicators for gross borrowing and the CFR, and by the authorised limit.

Gross borrowing and the CFR - in order to ensure that borrowing levels are prudent over the medium term and only for a capital purpose, the Council should ensure that its gross external borrowing does not, except in the short term, exceed the total of the capital financing requirement in the preceding year (2021/22) plus the estimates of any additional capital financing requirement for the current (2022/23) and next two financial years. This essentially means that the Council is not borrowing to support revenue expenditure. This indicator allowed the Council some flexibility to borrow in advance of its immediate capital needs in 2021/22. The table below highlights the Council's gross borrowing position against the CFR. The Council has complied with this prudential indicator.

	31.3.21 Actual	2021/22 Budget	31.3.22 Actual
Gross borrowing position (external debt)	£281.085m	£359.746m	£282.743m

	31.3.21 Actual	2021/22 Budget	31.3.22 Actual
Loans CFR	£429.680m	£490.677m	£449.260m
(Under) / over funding of CFR	(£148.595m)	(£130.931m)	(£166.517m)

The authorised limit - the authorised limit is the "affordable borrowing limit" required by s3 of the Local Government Act 2003. Once this has been set, the Council does not have the power to borrow above this level. The table below demonstrates that during 2021/22 the Council has maintained gross borrowing within its authorised limit.

The operational boundary – the operational boundary is the expected borrowing position of the Council during the year. Periods where the actual position is either below or over the boundary are acceptable subject to the authorised limit not being breached.

Actual financing costs as a proportion of net revenue stream - this indicator identifies the trend in the cost of capital, (borrowing and other long term obligation costs net of investment income), against the net revenue stream. See Appendix A for comparators.

	2021/22
Maximum gross borrowing position during the year	£282.7m
Authorised limit (Borrowing)	£450.0m
Operational boundary (Borrowing)	£430.0m
Financing costs as a proportion of net revenue stream	3.84%

3. Treasury Position as at 31st March 2022

The Council's treasury management debt and investment position is organised by the treasury management service in order to ensure adequate liquidity for revenue and capital activities, security for investments and to manage risks within all treasury management activities. Procedures and controls to achieve these objectives are well established both through member reporting detailed in the summary, and through officer activity detailed in the Council's Treasury Management Practices. At the end of 2021/22 the Council's treasury, (excluding borrowing by PFI and finance leases), position was as follows:

DEBT PORTFOLIO	31.3.21 Principal	Interest Rate %	31.3.22 Principal	Interest Rate %	Movement in Principal
Fixed rate funding:					
- PWLB	£169.0m	2.57%	£201.8m	2.55%	£32.8m
- Market	£40.0m	4.17%	£40.0m	4.17%	£0.0m
Variable rate funding:					
- Temporary	£72.1m	0.77%	£41.0m	0.14%	(£31.1m)
Total debt	**£281.1m**	**2.52%**	**£282.8m**	**2.47%**	**£1.7m**
Loans CFR	**£429.7m**		**£449.3m**		**£19.6m**
Over / (under) borrowing	**(£148.6m)**		**(£166.6m)**		**(£18.0m)**
Total investments	**£20.7m**	**0.00%**	**£36.5m**	**0.07%**	**£15.8m**
Net debt	**£260.4m**		**£246.3m**		**(£14.1m)**

The maturity structure of the debt portfolio was as follows:

	31.3.21 Actual		2021/22 original limits %		31.3.22 Actual	
	£m	%	Lower	Upper	£m	%
Under 12 months	£79.2m	28.2	0.0	70.0	£51.4m	18.2
12 months and within 24 months	£7.2m	2.5	0.0	30.0	£10.3m	3.6
24 months and within 5 years	£21.6m	7.7	0.0	50.0	£31.8m	11.2
5 years and within 10 years	£27.4m	9.7	0.0	75.0	£42.9m	15.2
10 years and above*	£145.7m	51.9	25.0	100.0	£146.4m	51.8

** this includes £25m Lenders Option Borrowers Options (LOBO) loans that are potentially callable at certain points before the maturity date.*

INVESTMENT PORTFOLIO	31.3.21 Actual £000	31.3.21 Actual %	31.3.22 Actual £000	31.3.22 Actual %
Treasury investments				
Banks	3,072	14.9	3,842	9.5
DMADF (H M Treasury)	12,600	61.0	27,700	75.8
Money Market Funds	4,980	24.1	4,980	14.7
Total managed in house	**20,652**	**100%**	**36,522**	**100%**
Total managed externally	0		0	
TOTAL TREASURY INVESTMENTS	**20,652**	**100%**	**36,522**	**100%**

The maturity structure of the investment portfolio was as follows:

	31.3.21 Actual £000	2021/22 Budget £000	31.3.22 Actual £000
Investments			
Longer than 1 year	0	0	0
Up to 1 year	20,652	15,000	36,522
Total	**20,652**	**15,000**	**36,522**

4. The Strategy for 2021/22

4.1 Investment strategy and control of interest rate risk

Investment returns remained close to zero for much of 2021/22. Most local authority lending managed to avoid negative rates and one feature of the year was the continued growth of inter local authority lending. The expectation for interest rates within the treasury management strategy for 2021/22 was that Bank Rate would remain at 0.1% until it was clear to the Bank of England that the emergency level of rates introduced at the start of the Covid-19 pandemic were no longer necessitated.

The Bank of England and the Government also maintained various monetary and fiscal measures, supplying the banking system and the economy with massive amounts of cheap credit so that banks could help cash-starved businesses to survive the various lockdowns/negative impact on their cashflow. The Government also supplied huge amounts of finance to local authorities to pass on to businesses. This meant that for most of the year there was much more liquidity in financial markets than there was demand to borrow, with the consequent effect that investment earnings rates remained low until towards the turn of the year when inflation concerns indicated central banks, not just the Bank of England, would need to lift interest rates to combat the second-round effects of growing levels of inflation (CPI was 6.2% in February).

Investment balances have been kept to a minimum through the agreed strategy of using reserves and balances to support internal borrowing, rather than borrowing externally from the financial markets. External borrowing would have incurred an additional cost, due to the differential between borrowing and investment rates. Such an approach has also provided benefits in terms of reducing the counterparty risk exposure, by having fewer investments placed in the financial markets.

4.2 Borrowing strategy and control of interest rate risk

During 2021/22, the Council maintained an under-borrowed position. This meant that the capital borrowing need, (the Capital Financing Requirement), was not fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow was used as an interim measure. This strategy was prudent as investment returns were very low and minimising counterparty risk on placing investments also needed to be considered.

The policy of avoiding new borrowing by running down spare cash balances has served well over the last few years. However, this was kept under review to avoid incurring higher borrowing costs in the future when this authority may not be able to avoid new borrowing to finance capital expenditure and/or the refinancing of maturing debt.

Against this background and the risks within the economic forecast, caution was adopted with the treasury operations. The Director of Finance therefore monitored interest rates in financial markets and adopted a pragmatic strategy based upon the following principles to manage interest rate risks:

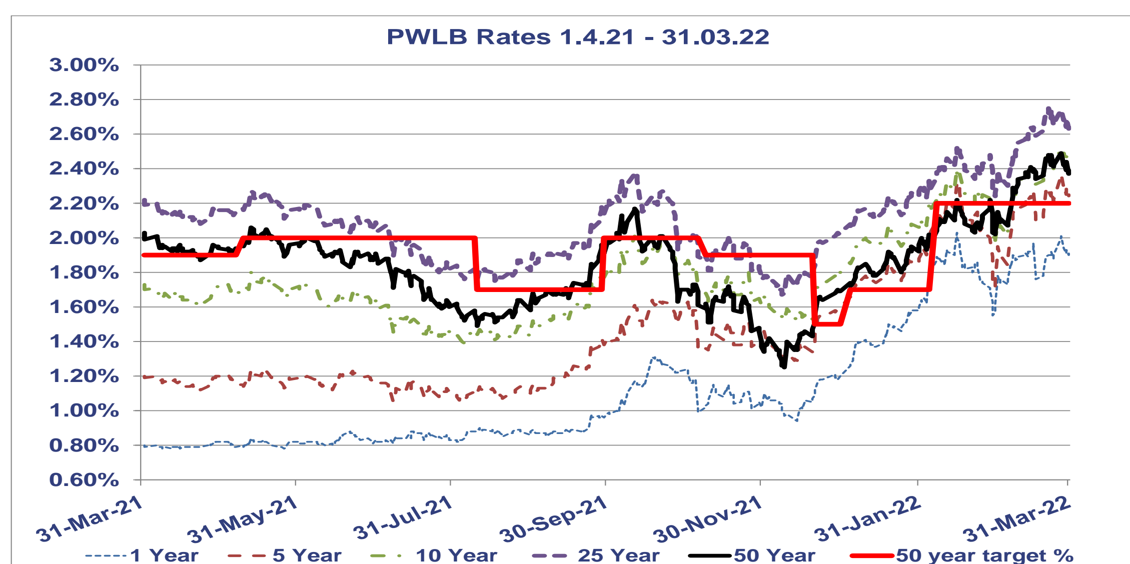
- if it had been felt that there was a significant risk of a sharp FALL in long and short term rates, (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), then long term borrowings would have been postponed, and potential rescheduling from fixed rate funding into short term borrowing would have been considered.
- if it had been felt that there was a significant risk of a much sharper RISE in long and short term rates than initially expected, perhaps arising from an acceleration in the start date and in the rate of increase in central rates in the USA and UK, an increase in world economic activity or a sudden increase in inflation risks, then the portfolio position would have been re-appraised. Most likely, fixed rate funding would have been drawn whilst interest rates were lower than they were projected to be in the next few years.

Interest rate forecasts expected only gradual rises in medium and longer-term fixed borrowing rates during 2021/22 and the two subsequent financial years until the turn of the year, when inflation concerns increased significantly. Internal, variable, or short-term rates, were expected to be the cheaper form of borrowing until well in to the second half of 2021/22.

HIGH/LOW/AVERAGE PWLB RATES FOR 2021/22

	1 Year	5 Year	10 Year	25 Year	50 Year
01/04/2021	0.80%	1.20%	1.73%	2.22%	2.03%
31/03/2022	1.91%	2.25%	2.43%	2.64%	2.39%
Low	0.78%	1.05%	1.39%	1.67%	1.25%
Low date	08/04/2021	08/07/2021	05/08/2021	08/12/2021	09/12/2021
High	2.03%	2.37%	2.52%	2.75%	2.49%
High date	15/02/2022	28/03/2022	28/03/2022	23/03/2022	28/03/2022
Average	1.13%	1.45%	1.78%	2.10%	1.85%
Spread	1.25%	1.32%	1.13%	1.08%	1.24%

PWLB RATES 2021/22



PWLB rates are based on gilt (UK Government bonds) yields through H.M. Treasury determining a specified margin to add to gilt yields. The main influences on gilt yields are Bank Rate, inflation expectations and movements in US treasury yields. Inflation targeting by the major central banks has been successful over the last 30 years in lowering inflation and the real equilibrium rate for central rates has fallen considerably due to the high level of borrowing by consumers: this means that central banks do not need to raise rates as much now to have a major impact on consumer spending, inflation, etc. This has pulled down the overall level of interest rates and bond yields in financial markets over the last 30 years. We have seen, over the last two years, many bond yields up to 10 years in the Eurozone turn negative on expectations that the EU would struggle to get growth rates and inflation up from low levels. In addition, there has, at times, been an inversion of bond yields in the US whereby 10 year yields have fallen below shorter term yields. In the past, this has been a precursor of a recession. Recently, yields have risen since the turn of the year on the back of global inflation concerns.

5. Borrowing Outturn

Treasury Borrowing – During the year 8 new PWLB loans were raised
Borrowing - loans were drawn to fund the net unfinanced capital expenditure and naturally maturing debt.

The loans drawn were:

Lender	Date Raised	Principal	Type	Interest Rate	Duration
PWLB	*31/08/2021	£5.0m	Fixed interest rate - Annuity	1.23%	12 years
PWLB	*27/10/2021	£5.0m	Fixed interest rate - Annuity	1.69%	12 years
PWLB	*09/11/2021	£5.0m	Fixed interest rate - Annuity	1.65%	12 years
PWLB	*11/11/2021	£5.0m	Fixed interest rate - Annuity	1.49%	12 years
PWLB	17/02/2022	£5.0m	Fixed interest rate - EIP	2.12%	10 years
PWLB	17/03/2022	£5.0m	Fixed interest rate - EIP	1.24%	12 years
PWLB	21/03/2022	£5.0m	Fixed interest rate - Annuity	2.21%	12 years
PWLB	29/03/2022	£5.0m	Fixed interest rate - Annuity	2.27%	10 years

This compares with a budget assumption of borrowing at an interest rate of 2.5%.
*loans included in 2021/22 Treasury Update Report presented to Audit Committee 25th January 2022

Borrowing in advance of need
The Council has not borrowed more than, or in advance of its needs, purely in order to profit from the investment of the extra sums borrowed.

Early Repayments or Rescheduling
No loans were repaid early or rescheduled during the year as the average 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

Debt Performance
As highlighted in Section 3 the average interest rate for borrowing fell slightly over the course of the year from 2.52% to 2.47%

6. Investment Outturn

Investment Policy – the Council's investment policy is governed by DLUHC investment guidance, which has been implemented in the annual investment strategy approved by the Council on 04/03/2021. This policy sets out the approach for choosing investment counterparties, and is based on credit ratings provided by the three main credit rating agencies.

The investment activity during the year conformed to the approved strategy, and the Council had no liquidity difficulties.

Investments held by the Council

- The Council maintained an average daily balance of £28.053m of internally managed funds.
- The internally managed funds earned an average rate of return of 0.07%.
- The comparable performance indicator is the average 7-day SONIA rate, which was 0.06%.

Investments (£m)	31.3.21	31.3.22
Cash Investments	20.652	36.522

At the 31.03.2022 total usable reserves were £137.6m, which has supported the overall cash flow position and the level of internal borrowing.

7. Overall Outturn for 2021/22

Overall a net benefit of £4.425m was made against budget for the year. The sound overall position has resulted from a mix of cash flow benefits plus pro-active treasury management activities through the active management of borrowing and taking advantage of low interest rates prevailing for the year.

8. Shropshire Council Debt

The Council makes an annual contribution towards Shropshire Council costs on pre disaggregation debt (i.e. pre unitary inception). The contribution in 2021/22 was £1.201m and interest paid averaged 4.9%. The rate of interest paid on this is managed by Shropshire and is considerably higher than the rate payable by Telford & Wrekin Council on its borrowing.

9. Leasing

Each year the Council arranges operating leases for assets such as vehicles, computers and equipment. This helps spread the cost over a number of years in line with the anticipated life of the equipment.

Two leasing drawdowns were completed for 2021/22, one in October and the other in January. These consisted of –

- Finance lease from Triple Point totalling £0.110m which funded the acquisition of gym equipment at Horsehay, and
- Finance lease from Society Generale Equipment Financing totalling £0.03m which funded grounds maintenance equipment at Horsehay Golf Centre.

10. The Economy and Interest Rates

UK. Economy. Over the last two years, the coronavirus outbreak has done huge economic damage to the UK and to economies around the world. After the Bank of England took emergency action in March 2020 to cut Bank Rate to 0.10%, it left Bank Rate unchanged at its subsequent meetings until raising it to 0.25% at its meeting on 16th December 2021, 0.50% at its meeting of 4th February 2022 and then to 0.75% in March 2022.

The UK economy has endured several false dawns through 2021/22, but with most of the economy now opened up and nearly back to business-as-usual, the GDP numbers have been robust (9% y/y Q1 2022) and sufficient for the MPC to focus on tackling the second-round effects of inflation, now that the CPI measure has already risen to 6.2% and is likely to exceed 8% in April.

Gilt yields fell towards the back end of 2021, but despite the war in Ukraine gilt yields have shot higher in early 2022. At 1.38%, 2-year yields remain close to their recent 11-year high and 10-year yields of 1.65% are close to their recent six-year high. These rises have been part of a global trend as central banks have suggested they will continue to raise interest rates to contain inflation.

Historically, a further rise in US Treasury yields will probably drag UK gilt yields higher. There is a strong correlation between the two factors. However, the squeeze on real household disposable incomes arising from the 54% leap in April utilities prices as well as rises in council tax, water prices and many phone contract prices, are strong headwinds for any economy to deal with. In addition, from 1st April 2022, employees also pay 1.25% more in National Insurance tax. Consequently, inflation will be a bigger drag on real incomes in 2022 than in any year since records began in 1955.

Average inflation targeting. This was the major change in 2020/21 adopted by the Bank of England in terms of implementing its inflation target of 2%. The key addition to the Bank's forward guidance in August 2020 was a new phrase in the policy statement, namely that "it does not intend to tighten monetary policy until there is clear evidence that significant progress is being made in eliminating spare capacity and *achieving the 2% target sustainably*". That mantra now seems very dated. Inflation is the "genie" that has escaped the bottle, and a perfect storm of supply side shortages, labour shortages, commodity price inflation, the impact of Russia's invasion of Ukraine and subsequent Western sanctions all point to inflation being at elevated levels until well into 2023.

USA. The flurry of comments from Fed officials following the mid-March FOMC meeting – including from Chair Jerome Powell himself – hammering home the hawkish message from the mid-March meeting, has had markets pricing in a further 225bps of interest rate increases in 2022 on top of the initial move to an interest rate range of 0.25% - 0.5%.

In addition, the Fed is expected to start to run down its balance sheet. Powell noted that the rundown could come as soon as the next meeting in May.

The upward pressure on inflation from higher oil prices and potential knock-on impacts on supply chains all argue for tighter policy (CPI is estimated at 7.8% across Q1), but the hit to real disposable incomes and the additional uncertainty points in the opposite direction.

More recently, the inversion of the 10y-2y Treasury yield spread at the end of March led to predictable speculation that the Fed's interest rate hikes would quickly push the US economy into recession. Q1 GDP growth is likely to be only between 1.0% and 1.5% annualised (down from 7% in Q4 2021). But, on a positive note, the economy created more than 550,000 jobs per month in Q1, a number unchanged from the post-pandemic 2021 average. Unemployment is only 3.8%.

EU. With euro-zone inflation having jumped to 7.5% in March it seems increasingly likely that the ECB will accelerate its plans to tighten monetary policy. It is likely to end net asset purchases in June – i.e., earlier than the Q3 date which the ECB targeted in March. And the market is now anticipating possibly three 25bp rate hikes later this year followed by more in 2023. Policymakers have also hinted strongly that they would re-start asset purchases if required. In a recent speech, Christine Lagarde said "we can design and deploy new instruments to secure monetary policy transmission as we move along the path of policy normalisation."

While inflation has hit the headlines recently, the risk of recession has also been rising. Among the bigger countries, Germany is most likely to experience a "technical" recession because its GDP contracted in Q4 2021, and its performance has been subdued in Q1 2022. However, overall, Q1 2022 growth for the Eurozone is expected to be 0.3% q/q with the y/y figure posting a healthy 5.2% gain. Finishing on a bright note, unemployment fell to only 6.8% in February.

China. After a concerted effort to get on top of the virus outbreak in Q1 of 2020, economic recovery was strong in the rest of the year; however, 2021 has seen the economy negatively impacted by political policies that have focussed on constraining digital services, restricting individual freedoms, and re-establishing the power of the One-Party state. With the recent outbreak of Covid-19 in large cities, such as Shanghai, near-term economic performance is likely to be subdued. Official GDP numbers suggest growth of c4% y/y, but other data measures suggest this may be an overstatement.

Japan. The Japanese economic performance through 2021/22 is best described as tepid. With a succession of local lockdowns throughout the course of the year, GDP is expected to have risen only 0.5% y/y with Q4 seeing a minor contraction. The policy rate has remained at -0.1%, unemployment is currently only 2.7% and inflation is sub 1%, although cost pressures are mounting.

World growth. World growth is estimated to have expanded 8.9% in 2021/22 following a contraction of 6.6% in 2020/21.

Deglobalisation. Until recent years, world growth has been boosted by increasing globalisation i.e. countries specialising in producing goods and commodities in which they have an economic advantage and which they then trade with the rest of the world. This has boosted worldwide productivity and growth, and, by lowering costs, has also depressed

inflation. However, the rise of China as an economic superpower over the last 30 years, which now accounts for 18% of total world GDP (the USA accounts for 24%), and Russia's recent invasion of Ukraine, has unbalanced the world economy. In addition, after the pandemic exposed how frail extended supply lines were around the world, both factors are now likely to lead to a sharp retrenchment of economies into two blocs of western democracies v. autocracies. It is, therefore, likely that we are heading into a period where there will be a reversal of world globalisation and a decoupling of western countries from dependence on China (and to a much lesser extent Russia) to supply products and vice versa. This is likely to reduce world growth rates.

Central banks' monetary policy. During the pandemic, the governments of western countries have provided massive fiscal support to their economies which has resulted in a big increase in total government debt in each country. It is therefore very important that bond yields stay low while debt to GDP ratios slowly subside under the impact of economic growth. This provides governments with a good reason to amend the mandates given to central banks to allow higher average levels of inflation than we have generally seen over the last couple of decades. Both the Fed and Bank of England have already changed their policy towards implementing their existing mandates on inflation, (and full employment), to hitting an average level of inflation. Greater emphasis could also be placed on hitting subsidiary targets e.g. full employment before raising rates. Higher average rates of inflation would also help to erode the real value of government debt more quickly.

11. Other

IFRS 16: The implementation of the new IFRS 16 Leases accounting standard, for Local Government, has been further delayed until 2024/25.

Prudential and Treasury Indicators are detailed in Appendix A.

12. 2022/23 Treasury Update

The remainder of this report deals with the current financial year based largely on information to 31 May 2022.

12.1. 2022/23 Treasury Strategy

The strategy for 2022/23 was approved by Full Council 3rd March 2022. The strategy is to continue to keep investments as short term, where possible, to reduce the need to borrow thus reducing investment exposure and maximising overall returns to the revenue account. We will review investment opportunities if they arise and also review borrowing opportunities as we progress through the year and look to take advantage of advantageous interest rates where appropriate. The Medium Term Financial Strategy 2022/23 – 2025/26, approved by Full Council on 3rd March 2022, will see the Council continue to invest in significant regeneration projects including highways and building homes and commercial property as part of the approved Housing Investment Programme and the Property Investment Programme.

In order to comply with MiFID II the Council will maintain a minimum investment balance of £10m.

12.2. Interest Rates

The Bank of England increased the base rate from 0.75% to 1.0% on 5th May 2022 as it continued to seek to control increasing inflation which hit a 30 year high of 7% (CPI) in March and increased further to 9% in April the fallout as higher prices for goods due to stock shortages as economies start to open up following the pandemic, along with higher energy prices and Russia's invasion of Ukraine which has led more increases in the prices of energy and food. It is anticipated that the base rate will continue to rise throughout 2022/23 finishing the year at 2.0%.

12.3. Prudential Regime

This Council agreed its required indicators at Council on 3rd March 2022.

The Council has operated within the Treasury Limits and Prudential Indicators set.

The Council set itself an Operational Limit for external debt of £475m for 2022/23 and an Authorised limit of £495m. Our total borrowing outstanding as at 31st May 2022 (excluding PFI) is £285.8m which is within both limits.

12.4. Borrowing

Treasury Borrowing – During the year 1 new PWLB loan has been raised
Borrowing – the loan was drawn to fund the net unfinanced capital expenditure and naturally maturing debt.

The loans drawn were:

Lender	Date Raised	Principal	Type	Interest Rate	Duration
PWLB	28/04/2022	£5.0m	Fixed interest rate - Annuity	2.56%	11 years

In total £10.4m of PWLB Loans are due to mature during the year.

On 19 May 2022 the Council launched a Municipal Investment Loan on the Abundance Platform: the Telford & Wrekin Climate Action Investment. This provides an opportunity for individuals to lend money to the Council which will be used to fund a range of projects across Telford & Wrekin to help tackle the climate emergency, including: replacing 2 fossil-fuel powered minibuses with electric minibuses; working with local organisations and businesses to improve energy efficiency in buildings; and installing renewable technologies, such as solar panels and ground source heat pumps into temporary/supported accommodation properties. With a target of raising £0.5m, loans are for a 5 year period at a fixed interest rate of 2.10% per annum. This is a new borrowing source for the Council (permitted in the approved Treasury Strategy), which is an alternative to PWLB and is specifically aimed to support the Council's Climate Change Agenda. The cost of borrowing to the Council, including fees, was comparable with PWLB rates at the time of entering the arrangement in that on the day the offer was launched the cost of the debt to the Council was lower than PWLB would have been. Legally, the investments are Loans from individual people to the Council.

12.5. Investments

The strategy for the year is to gain maximum benefit at minimum risk whilst achieving as a minimum, the overnight deposit rate. For the period to 31st May 2022 some £1,497m worth of investments have been made with the Debt Management Office (DMO), Lloyds Bank and Money Market Funds. Rates have ranged from an average of 0.53% to 0.82%

The Council holds investments in money market funds which gives increased diversification of counter-party risk and slightly higher yield whilst retaining a high degree of liquidity. These investment are held in one diversified fund.

The Council can place up to £15.0m with any Counterparty, with the exception of Treasury's DMO facility which is Government backed and therefore considered to be very secure so no limit is placed on investments with the DMO. At the end of May the greatest exposure with a single counterparty was £10.8m (58.2% of the portfolio) with the DMO.

INVESTMENT PORTFOLIO	31.5.22 Actual £000	31.5.22 Actual %
Treasury investments		
Banks	2,787	15.0
DMADF (H M Treasury)	10,800	58.2
Money Market Funds	4,980	26.8
Total managed in house	**18,567**	**100%**
Total managed externally	0	
TOTAL TREASURY INVESTMENTS	**18,567**	**100%**

12.6. Projected Performance 2022/23

Senior Finance Officers are closely monitoring the Treasury position, particularly with the likelihood of the continuing interest rate rises. The financial monitoring report presented to Cabinet on 14 July 2022 included a projected benefit of £2.5m from treasury management activities. Updates will be provided in future financial monitoring reports taken to Cabinet.

12.7 MRP Update

In November 2021 the Department for Levelling Up, Housing and Communities (DLUHC) launched a consultation seeking views on proposed changes to regulations in relation to the duty of local authorities to make prudent Minimum Revenue Provision each year. The consultation closed in February 2022. The proposals for change related to the exclusion of a proportion of debt from the MRP calculation, particularly relating to investment assets, capital loans and some operational assets. Following concerns raised by a number of authorities it was apparent that the proposed changes may have given rise to unintended consequences and DLUHC amended the proposals to allow additional flexibilities with respect to capital loans. At the time of writing this report, a further consultation is underway on the amended proposals which will inform the government's final response. It is currently intended that the proposed changes will take effect from the 2023/24 financial year and the Council will prepare the budget for 2023/24 and later years on the revised basis once known.

ABBREVIATIONS USED IN THIS REPORT

CFR: capital financing requirement - the council's annual underlying borrowing need to finance capital expenditure and a measure of the council's total outstanding indebtedness.

CIPFA: Chartered Institute of Public Finance and Accountancy – the professional accounting body that oversees and sets standards in local authority finance and treasury management.

CPI: consumer price index – the official measure of inflation adopted as a common standard by countries in the EU. It is a measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food and medical care. It is calculated by taking price changes for each item in the predetermined basket of goods and averaging them.

ECB: European Central Bank - the central bank for the Eurozone

EU: European Union

EZ: Eurozone -those countries in the EU which use the euro as their currency

Fed: the Federal Reserve System, often referred to simply as "the Fed," is the central bank of the United States. It was created by the Congress to provide the nation with a stable monetary and financial system.

FOMC: the Federal Open Market Committee – this is the branch of the Federal Reserve Board which determines monetary policy in the USA by setting interest rates and determining quantitative easing policy. It is composed of 12 members--the seven members of the Board of Governors and five of the 12 Reserve Bank presidents.

GDP: gross domestic product – a measure of the growth and total size of the economy.

G7: the group of seven countries that form an informal bloc of industrialised democracies--the United States, Canada, France, Germany, Italy, Japan, and the United Kingdom--that meets annually to discuss issues such as global economic governance, international security, and energy policy.

Gilts: gilts are bonds issued by the UK Government to borrow money on the financial markets. Interest paid by the Government on gilts is called a coupon and is at a rate that is fixed for the duration until maturity of the gilt, (unless a gilt is index linked to inflation); while the coupon rate is fixed, the yields will change inversely to the price of gilts i.e. a rise in the price of a gilt will mean that its yield will fall.

HRA: housing revenue account.

IMF: International Monetary Fund - the lender of last resort for national governments which get into financial difficulties.

LIBID: the London Interbank Bid Rate is the rate bid by banks on deposits i.e., the rate at which a bank is willing to borrow from other banks. It is the "other end" of the LIBOR (an offered, hence "ask" rate, the rate at which a bank will lend). These benchmarks ceased on 31st December 2021 and have, generally, been replaced by SONIA, the Sterling Overnight Index Average.

MHCLG: the Ministry of Housing, Communities and Local Government - the Government department that directs local authorities in England.

MPC: the Monetary Policy Committee is a committee of the Bank of England, which meets for one and a half days, eight times a year, to determine monetary policy by setting the official interest rate in the United Kingdom, (the Bank of England Base Rate, commonly called Bank Rate), and by making decisions on quantitative easing.

MRP: minimum revenue provision - a statutory annual minimum revenue charge to reduce the total outstanding CFR, (the total indebtedness of a local authority).

PFI: Private Finance Initiative – capital expenditure financed by the private sector i.e. not by direct borrowing by a local authority.

PWLB: Public Works Loan Board – this is the part of H.M. Treasury which provides loans to local authorities to finance capital expenditure.

QE: quantitative easing – is an unconventional form of monetary policy where a central bank creates new money electronically to buy financial assets, such as government bonds, (but may also include corporate bonds). This process aims to stimulate economic growth through increased private sector spending in the economy and also aims to return inflation to target. These purchases increase the supply of liquidity to the economy; this policy is employed when lowering interest rates has failed to stimulate economic growth to an acceptable level and to lift inflation to target. Once QE has achieved its objectives of stimulating growth and inflation, QE will be reversed by selling the bonds the central bank had previously purchased, or by not replacing debt that it held which matures. The aim of this reversal is to ensure that inflation does not exceed its target once the economy recovers from a sustained period of depressed growth and inflation. Economic growth, and increases in inflation, may threaten to gather too much momentum if action is not taken to 'cool' the economy.

RPI: the Retail Price Index is a measure of inflation that measures the change in the cost of a representative sample of retail goods and services. It was the UK standard for measurement of inflation until the UK changed to using the EU standard measure of inflation – Consumer Price Index. The main differences between RPI and CPI is in the way that housing costs are treated and that the former is an arithmetical mean whereas the latter is a geometric mean. RPI is often higher than CPI for these reasons.

SONIA: the Sterling Overnight Index Average. Generally, a replacement set of indices (for LIBID) for those benchmarking their investments. The benchmarking options include using a forward-looking (term) set of reference rates and/or a backward-looking set of reference rates that reflect the investment yield curve at the time an investment decision was taken.

TMSS: the annual treasury management strategy statement reports that all local authorities are required to submit for approval by the full council before the start of each financial year.

Appendix A: Prudential and treasury indicators

1. PRUDENTIAL INDICATORS	2020/21	2021/22	2021/22
Extract from budget setting report	**actual**	**original**	**actual**
	£'000	**£'000**	**£'000**
Capital Expenditure	£57,710	£101,855	£57,367
Ratio of financing costs to net revenue stream	4.35%	6.4%	3.84%
Gross borrowing requirement General Fund			
brought forward 1 April	£276,185	£299,533	£281,085
carried forward 31 March	£281,085	£359,746	£282,743
in year borrowing requirement	£4,900	£60,213	£1,658
Loans CFR	£429,680	£490,677	£449,260
Annual change in Loans CFR	£20,884	£59,315	£19,580

2. TREASURY MANAGEMENT INDICATORS	2020/21	2021/22	2021/22
	actual	**original**	**actual**
	£'000	**£'000**	**£'000**
Authorised Limit for external debt -			
borrowing	£450,000	£450,000	£450,000
other long term liabilities	£64,000	£64,000	£64,000
TOTAL	£514,00	£514,000	£514,000
Operational Boundary for external debt -			
borrowing	£430,000	£430,000	£430,000
other long term liabilities	£60,000	£60,000	£60,000
TOTAL	£490,000	£490,000	£490,000
Actual external debt	£281,085	£359,746	£282,743

Maturity structure of fixed rate borrowing during 2021/22	upper limit	lower limit	31.03.22
under 12 months	0.0%	70.0%	18.2%
12 months and within 24 months	0.0%	30.0%	3.6%
24 months and within 5 years	0.0%	50.0%	11.2%
5 years and within 10 years	0.0%	75.0%	15.2%
10 years and within 20 years	0.0%	100.0%	51.8%
Maturity structure of investments during 2021/22	upper limit	lower limit	
Longer than 1 year	0.0%	95.0%	0.0%
Up to 1 year	0.0%	100.0%	100.0%

Credit risk indicator	2020/21 Actual	2021/22 Target	2021/22 Actual
Portfolio average credit score	1.59	6 or lower	1.44

Target – 6 or lower is equivalent to a credit rating of 'A' or higher