Report To:	**Audit and Standards Committee**
Date:	**4 July 2022**
Report Title:	**Treasury Management Annual Report 2021/22**
Report of:	**Chief Finance Officer**
Ward(s):	**All**
Purpose of report:	**To present the Annual Treasury Management Report for 2021/22.**
Officer Recommendations:	**To recommend to Full Council (via Cabinet):** **(1) To agree the Annual Treasury Management report for 2021/22.** **(2) To approve the 2021/22 Prudential and Treasury Indicators included in the report.**
Reasons for recommendations:	**Requirement of CIPFA Treasury Management in the Public Sector Code of Practice (the Code) and this has to be reported to Full Council.**
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1 Introduction

1.1 The Council is required, under the Local Government Act 2003, to produce an annual review of Treasury Management 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).

1.2 During 2021/22, the Full Council received the annual Treasury Management Strategy Statement (TMSS), whilst Cabinet were presented with the 2021/22 Treasury Management Update Report in relation to the sources and methods of borrowing and approved organisations for lending temporarily surplus funds.

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

2 Treasury Management 2021/22

2.1 Treasury Management is an integral part of the Council's overall finances and the performance of this area is very important. Whilst individual years obviously matter, performance is best viewed on a medium/long term basis. The action taken in respect of the debt portfolio in recent years has been extremely beneficial and has resulted in savings. Short term gains might, on occasions, be sacrificed for longer term certainty and stability.

2.2 The criteria for lending to Banks are derived from the list of approved counter parties provided by the Council's Treasury Management advisors, Link Asset Services. The list is amended to reduce the risk to the Council by removing the lowest rated counterparties and reducing the maximum loan duration.

2.3 In addition, Treasury Management updates are included within the quarterly performance management reports, considered by both the Cabinet and the Policy and Performance Advisory Committee. The regulatory environment places a much greater responsibility on Members for the review and scrutiny of treasury management policy and activities. This report is 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 report will be considered by the Cabinet at its meeting on 7 July 2022 meeting.

2.4 This Council also confirms that it has complied with the requirement under the Code to give prior scrutiny to all the above treasury management reports by the Audit & Standard Committee before they were reported to the full Council. Member training on treasury management issues was undertaken on 21 October 2021, which is to support Members' scrutiny role and further training is expected to take place in 2022-23.

This report summarises:

- Capital activity during the year;
- Impact of this activity on the Council's underlying indebtedness (the Capital Financing Requirement (CFR));
- Reporting of the required prudential and treasury indicators and changes to be approved;
- 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;
- Debt activity and investment activity.
- Economic and Interest Rates

2.5 An economic commentary for the year provided by the Council's treasury management advisors is provided at Appendix E to this report. Bank Rate was 0.1% at the beginning of the year and despite the economy gathering momentum after pandemic restrictions eased, market expectation was for rises to be delayed until 2022. Rising, persistent inflation changed that with Bank Rate rising to 0.75% at the end of the year.

2.6 During 2021 CIPFA published changes to its Prudential Code and Treasury Management Code of Practice. These follow the Public Accounts Committee's recommendation that the prudential framework should be further tightened following continued borrowing by some authorities for investment purposes.

2.7 In addition, HM Treasury issued, in May 2022, updated guidance on PWLB lending to authorities where there is more than a negligible risk of non-repayment. In the same month the Levelling Up and Regeneration Bill announced in the Queens Speech gives government more oversight of the Prudential Framework.

2.8 The main points of these new Codes, PWLB guidance and Levelling Up and Regeneration Bill are summarised at Appendix D.

2.11 On the debt portfolio, no new loans were taken, and external debt is around £51.673m. The MTFS 2021-22 capital programme includes a funding requirement of £95.2m to be funded from borrowing. However, due to the strength of the Council's balance sheet, it is expected to be possible to use internal balances to fund this on a temporary basis instead of raising new loans.

2.10 The loan portfolio has produced a level of performance in the period in which performance figures have been calculated. Adding significant value in a period of extremely low interest rates is very difficult. Given that interest rates are unlikely to rise for the next two years, low levels of returns are likely to continue and the cost of getting investment decisions wrong is unlikely to be significant.

3 Treasury Management Activity

3.1 The timetable for reporting Treasury Management activity in 2021 and 2022 are shown in the table below. This takes into account the timescale for the publication of each Committee agenda and is on the basis that it is preferable to report on activity for complete months. Any extraordinary activity taking place between the close of the reporting period and the date of the Audit and Standards Committee meeting will be reported verbally at that meeting.

Meeting date	Reporting period for transactions
26 July 2021	2020/21 Annual Report
27 September 2021	1 April to 31 July 2021
15 November 2021	1 August to 31 October 2021
14 March 2022	1 November to 31 December 2021
4 July 2022	2021/22 Annual Report (up to 31 March 2022)

4. Overall Summary of Activity 2021/22

4.1 The table below lists the key elements of the 2021/22 Strategy and records actual performance against each one of them.

Key Element	**Target in Strategy**	**Actual Performance**	
Borrowing			
Underlying need to borrow (CFR) at year end	£95.249 million	£96.005 million	-
External Debt	£62.793 million	£51.673 million	-

Key Element	Target in Strategy	Actual Performance	
Under borrowing at year end	£32.456 million	£43.381 million	-
New external long-term borrowing in year	None anticipated	None undertaken	✓
Debt rescheduling in year	Review options but not anticipated	Options kept under review, none undertaken	✓
Interest payments on external borrowing	£1.71 million	£1.71 million	✓
Investments			
Minimum counterparty credit ratings for unsecured investments	Long-term BBB+- (does not apply to Government and other local authorities which have the highest ratings)	At least Long-term A	✓
Interest receipts from external investments	£0.100 million	£0.021 million	✓
Appointment of Investment Consultants			
Independent Treasury Adviser to be retained	Link Treasury Services Limited retained as Treasury Adviser	Link Treasury Services Limited retained as Treasury Adviser	✓
Reporting and Training			
Reports to be made to Audit and Standards Committee and Cabinet	Every regular meeting	Every regular meeting.	✓
Briefing sessions for Councillors and Staff	Treasury Adviser to provide	Staff training 21 21 October 2021	✓

5. Detailed Analysis – Borrowing

5.1 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.

5.2 A cost of carry remained during the year on any new long-term borrowing that was not immediately used to finance capital expenditure, as it would have caused a temporary increase in cash balances; this would have incurred a revenue cost – the difference between (higher) borrowing costs and (lower) investment returns.

5.3 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.

5.4 Against this background and the risks within the economic forecast, caution was adopted with the treasury operations. The Chief Finance Officer therefore monitored interest rates in financial markets and adopted a pragmatic strategy.

5.5 In accounting terms, the underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR) while usable reserves and working capital are the underlying resources available for investment.

5.6 The CFR is, in simple terms, the amount of capital expenditure which has been incurred by the Council but which has not yet been paid for (by using, for example, grants, capital receipts, reserves or revenue income) and in the meantime is covered by internal or external borrowing. 'External borrowing' is where loans are raised from the Public Works Loans Board (PWLB) or banks. Alternatively, it is possible to 'internally borrow' the significant levels of cash which has been set aside in Balances and Reserves and which would otherwise need to be invested with banks or other counterparties.

5.7 As noted above, the level of CFR increases each year by the amount of unfinanced capital expenditure and is reduced by the amount that the Council sets aside for the repayment of borrowing. The original CFR projection for 2021/22, the revised position reported at the time of producing the Treasury Strategy 2022/23 (February 2022) and the final position for the year are shown in the table below. The variation between the revised and final position reflects the changing profile of capital spend across financial years, particularly allocations in the capital programme in respect of facilitating loans to Lewes Housing investment Company, and Aspiration Homes LLP.

	2021/22 Original	**2021/22 Revised**	**2021/22 Outturn**
	£m	**£m**	**£m**
Opening CFR	88.387	89.268	**89.268**
Capital expenditure in year (Appendix C)	50.917	27.219	**14.229**
Less financed	(19.188)	(20.902)	**(7.158)**
Less amount set aside for debt repayment	(0.376)	(0.336)	**(0.334)**
Closing CFR	**119.740**	**95.249**	**96.005**

5.8 The overall CFR can be split between the General Fund and the Housing Revenue Account as follows:

	2021/22	**2021/22**
Description	Revised	**Outturn**
CFR Component	£m	**£m**
General Fund	23.699	**20.096**

Housing Revenue Account	71.550	**75.909**
Total	**95.249**	**96.005**

5.9 The following table compares the CFR with the amount that the Council holds in balances and reserves as well as working capital (day to day cash movements as well as grants, developer contributions and capital receipts held, pending their use).

5.10 The Council's long-term loan portfolio at 31 March 2022 was:

Lender	Interest	Amount £m	Rate %	Maturity
PWLB	Fixed	4.000	2.70	01-03-2024
PWLB	Fixed	5.000	3.30	01-03-2032
PWLB	Fixed	2.000	3.05	01-09-2027
PWLB	Fixed	2.000	2.76	01-09-2024
PWLB	Fixed	4.000	2.97	01-09-2026
PWLB	Fixed	5.000	3.28	01-09-2031
PWLB	Fixed	4.000	2.63	01-09-2023
PWLB	Fixed	5.000	3.44	01-03-2037
PWLB	Fixed	6.673	3.50	01-03-2042
PWLB	Fixed	5.000	3.43	01-09-2036
PWLB	Fixed	4.000	3.01	01-03-2027
	Sub-total	**46.673**		
Barclays	Fixed	5.000	4.50	06-04-2054
	Sub-total	**5.000**		
	Total	**51.673**		

5.11 The Council's objective when borrowing has been to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required, with flexibility to renegotiate loans should the Council's long-term plans change being a secondary objective.

5.12 In the table above the Barclays loan was taken out in April 2004 with a term of 50 years. In June 2016, the bank decided to permanently waive its contractual right to vary the interest rate on this loan, which was effectively fixed at the rate of interest applicable at that time, 4.5%.

5.13 Total interest paid on external long-term borrowing in the year was £1.71m, which was consistent with the revised budget for the year. No new long-term borrowing was undertaken. The Council remained eligible to access the Government's 'Certainty Rate' allowing the Council to borrow, had it been appropriate to do so, at a reduction of 0.2% on the Standard Rate.

5.14 Through the year, officers, supported by Link Treasury Services Limited, monitored opportunities for the rescheduling of external loans and the possibility of repayment utilising cash balances that would otherwise be invested. No beneficial rescheduling opportunities were identified, and the loan portfolio remained unchanged through the year.

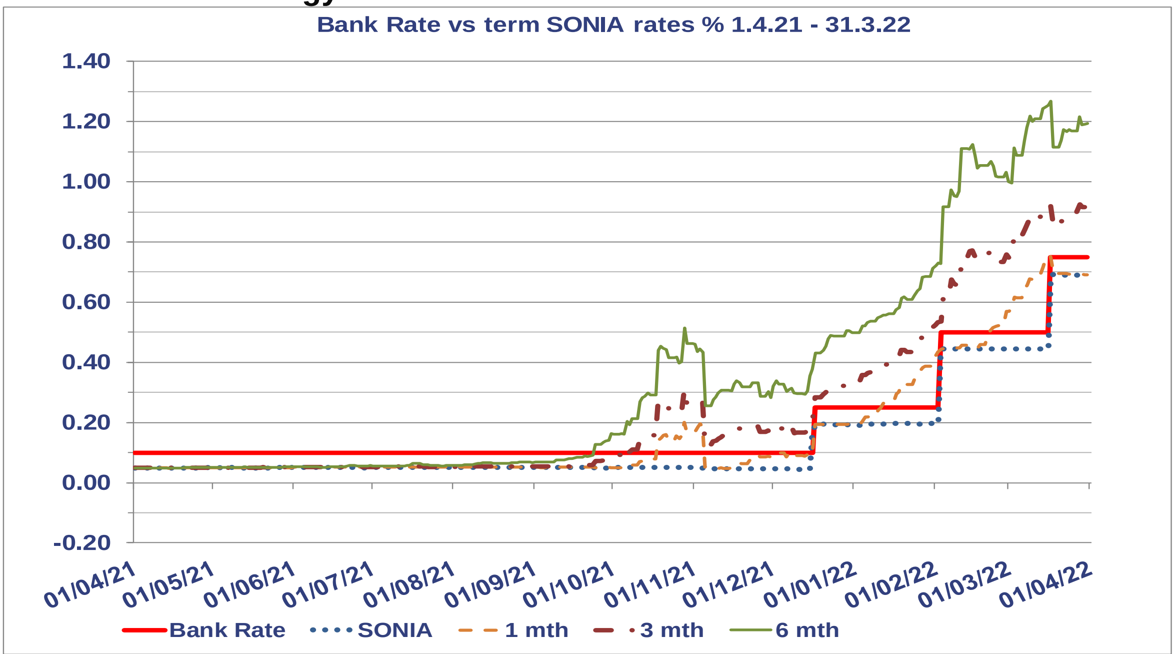
5.15 As determined by the Council, two separate Loans Pools operated in 2021/22, for the General Fund and HRA, respectively. At 31 March 2022 the balance on internal loans from the General Fund to the Housing Revenue Account (HRA) was £19.236m, an increase of £4.360m compared with the previous year, which comprised new lending as funding for the construction of new homes. Interest was charged on internal borrowing at 0.99% (equivalent to a one-year maturity loan from the PWLB at the start of the financial year).

5.16 No temporary borrowing was undertaken during the course of the financial year and consequently, there were no temporary loans outstanding at 31 March 2021.

6.0 Detailed Analysis - Investments

6.1 In a relatively short period since the onset of the COVID-19 pandemic, the global economic fallout was sharp and large. Market reaction was extreme with large falls in equities, corporate bond markets and, to some extent, real estate echoing lockdown-induced paralysis and the uncharted challenges for governments, businesses, and individuals.

Investment strategy and control of interest rate risk



	Bank Rate	SONIA	1 mth	3 mth	6 mth
High	0.75	0.69	0.75	0.93	1.27
High Date	17/03/2022	18/03/2022	16/03/2022	28/03/2022	17/03/2022
Low	0.10	0.05	0.05	0.05	0.05
Low Date	01/04/2021	15/12/2021	10/11/2021	14/04/2021	09/04/2021
Average	0.19	0.14	0.17	0.24	0.34
Spread	0.65	0.65	0.71	0.88	1.22

6.2 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.

6.3 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).

6.4 While the Council has taken a cautious approach to investing, it is also fully appreciative of changes to regulatory requirements for financial institutions in terms of additional capital and liquidity that came about in the aftermath of the financial crisis. These requirements have provided a far stronger basis for financial institutions, with annual stress tests by regulators evidencing how institutions are now far more able to cope with extreme stressed market and economic conditions.

6.5 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 as illustrated in the charts shown above and below. Such an approach has also provided benefits in terms of reducing counterparty risk exposure, by having fewer investments placed in the financial markets.

6.6 The Council held an average of £31.99m as cash during the year. This comprised working cash balances, capital receipts, earmarked reserves and developer contributions held pending their use.

6.7 The Council's general policy objective is to invest its surplus funds prudently. Throughout 2021/22, the Council's investment priorities continued to be:

Highest priority - Security of the invested capital;

Followed by - Liquidity of the invested capital;

Finally - An optimum yield commensurate with security and liquidity.

6.8 All of the Council's investments were managed in-house. Security of capital was maintained by following the counterparty policy set out in the Investment Strategy for 2021/22. Investments made during the year included:

- Fixed Term Deposits with the Debt Management Office (DMO) (a total of £258.1 million – 44 occasions);

- Fixed Term Deposits with other Local Authorities (a total of £20 million – 4 occasions);

- Fixed Term Deposits with UK Banks and Building Societies (a total of £10 million – 2 occasions);

- Fixed Term Deposit with overseas Banks and Building Societies (a total of £15 million – 3 occasions)

- Investments in Money Market Funds (MMFs) (average daily balance held in year £0.001 million);
- United Kingdom Treasury Bills (none);

- Tradable Investments - Floating Rate Notes, Certificates of Deposit, Bonds (none);

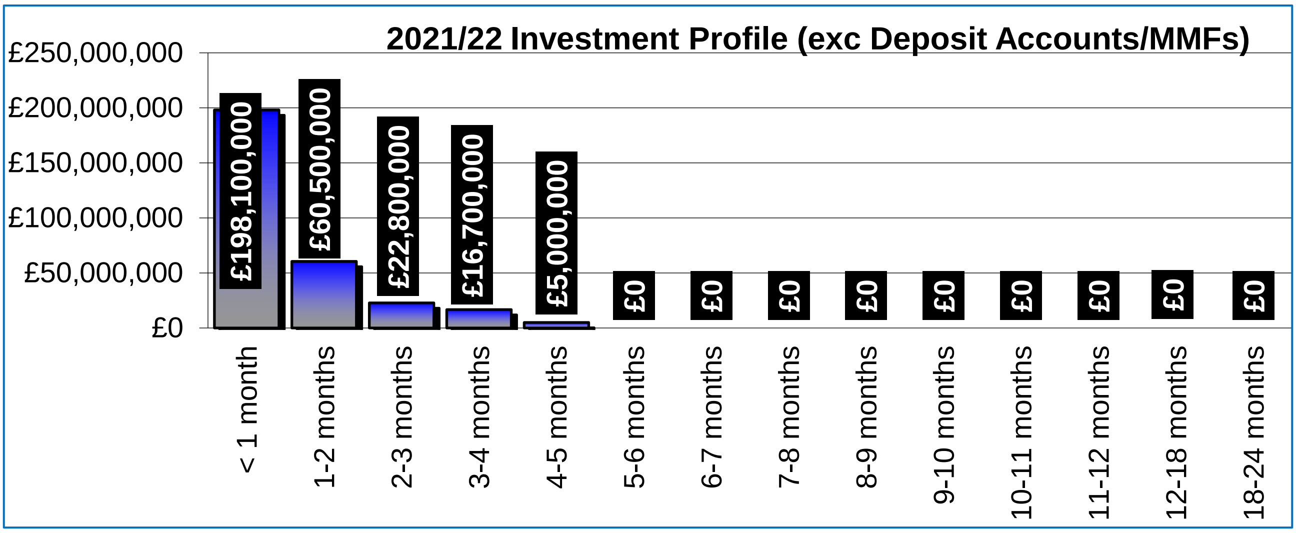
- Deposit accounts with UK Banks (average daily balance held in year £7.29 million);

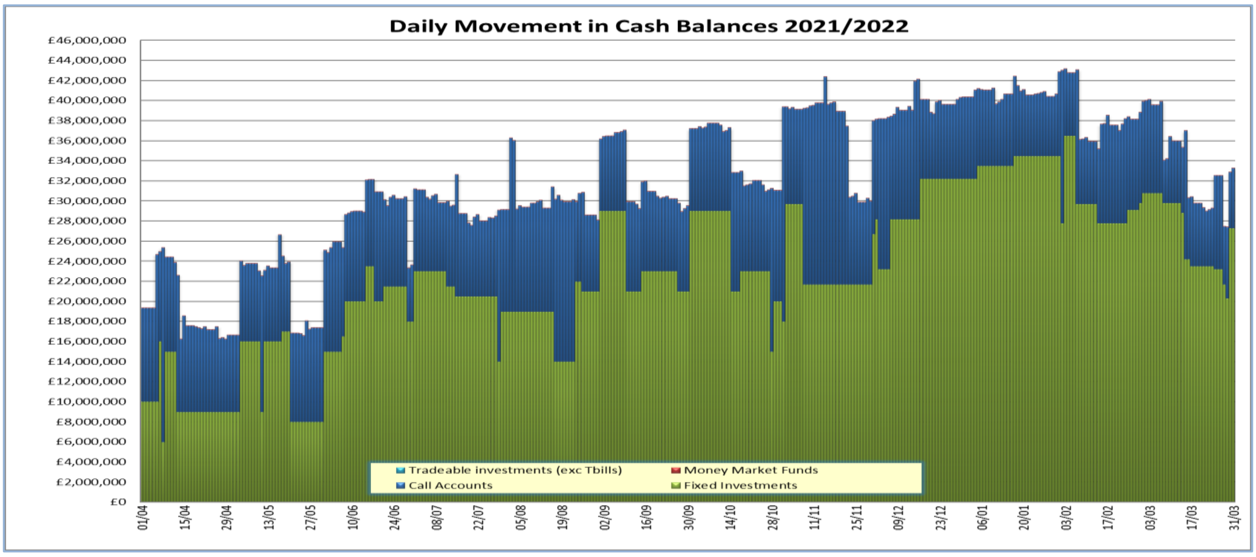
- Deposit accounts with UK Building Societies (none);

- Overnight deposits with the Council's banker, Lloyds Bank (average daily balance held in year £1.9 million).

6.9 In keeping with Government guidance on investments, the Council maintained a sufficient level of liquidity through the use of Money Market Funds (MMF), overnight deposits and deposit accounts, the average daily balance held being £0.001 million.

6.10 A full list of investments (excluding deposit account or MMF transactions) made or maturing in the year is given at Appendix B. All investments were made with UK institutions, and no new deposits were made for periods in excess of one year. The first chart below gives an analysis of aggregate fixed term deposits by duration. The second chart shows how the total amount invested varied from day to day over the course of the year, from a low of £16.21m to a high of £43.16m. The movement largely reflects the cycle of grant, council tax and business rate receipts and precept payments made.





6.11 The income return generated from investments in the year was £0.021 million, below the total budget for investment income of £0.100 million. This position arose as a result of the requirement to re-profile major projects within the approved capital programme, ensuring an increase in the short-term availability of additional cash for investment.

6.12 The average rate of return from investments at the end of each quarter in 2021/22 is shown in the table below, along with comparative benchmark information, SONIA rate.

Average rate of investments in:	Lewes District Council	SONIA
Quarter 1 ending 30 June 2021	0.01%	0.047%
Quarter 2 ending 30 September 2021	0.00%	0.048%
Quarter 3 ending 31 December 2021	0.02%	0.08%
Quarter 4 ending 31 March 2022	0.27%	0.19%
Whole year 2021/22	0.14%	0.14%

7. Compliance with Prudential Indicators

7.1 The Council can confirm that it has complied with its Prudential Indicators for 2021/22. A detailed review of each of the Prudential Indicators is at Appendix A.

8. Investment Consultants

8.1 The Council has recently appointed Link Treasury Services Limited as its Treasury Adviser for an initial two-year term expiring on 30 May 2023, with the Council having the option to extend, if required. The Link Treasury Services has been appointed to support both the Lewes District Council and Eastbourne Borough Council, given that a shared finance team (with treasury management responsibility) has been established.

9. Reporting and Training

9.1 The Chief Finance Officer reported the details of treasury management activity to each regular meeting of the Audit and Standards Committee and Cabinet held in 2021/22. A mid-term summary report was issued in November 2021.

9.2 The training needs of the Council's treasury management staff were reviewed as part of the annual corporate staff appraisal/training needs assessment process for all Council employees. Members of staff attended, where appropriate, Links workshops alongside colleagues from other local authorities during 2021/22. In 2021/22, Link Asset Services continue to meet with Council officers to explain developments within the sector, as well as review the Council's own investment and debt portfolios.

10 Other

10.1 CIPFA consultations: In February 2021 CIPFA launched two consultations on changes to its Prudential Code and Treasury Management Code of Practice. These follow the Public Accounts Committee's recommendation that the prudential framework should be further tightened following continued borrowing by some authorities for investment purposes. These are principles-based consultations and will be followed by more specific proposals later in the year.

10.2 **IFRS 16:** The implementation of the new IFRS 16 Leases accounting standard was due to come into force for local authorities from 1st April 2022. Following a consultation CIFPA/LASAAC announced an optional two-year delay to the implementation of this standard a decision which was confirmed by the Financial Reporting Advisory Board in early April 2022. Authorities can now choose to adopt the new standard on 1st April 2022, 1st April 2023 or 1st April 2024. The Chief Finance Officer intends for the Council to adopt the new standard on 1st April 2024, if resources permit adoption from April 2023 will be considered

11. Non-treasury investments

11.1 At its previous meeting, the Committee requested that information should be included in this report about the Council's 'non-treasury' investment activity e.g. loans to Council-owned companies or the purchase of property assets for the purpose of income generation.

11.2 **Lewes Housing Investment Company Limited**
Lewes Housing Investment Company (LHIC) is a wholly owned subsidiary of the Council. Incorporated in July 2017, LHIC was established to acquire, improve, and let residential property at market rents. A capital allocation of £2.5m was approved as potential commercial loan funding to facilitate property purchases. At 31 March 2022, a total of £2,065 working capital has been drawn down. The balance has been rolled forward into 2022/23. There have been no transactions during the period 1 April 2022 to 30 June 2022.

11.3 **Aspiration Homes LLP**

Aspiration Homes LLP (AH) is a limited liability Partnership owned equally by Lewes District Council and Eastbourne Borough Council. Incorporated in June 2017, AH was established for the purpose of developing housing to be let at affordable rent. A capital allocation of £17.5m was approved as potential commercial loan funding to AH to facilitate property purchases. At 31 March 2022, a total of £3,043,855 has been drawn down for the purchase of Gray's School, Newhaven, and Caburn Field, Ringmer. The balance has been rolled forward into 2022/23.

A working Capital facility loan of £100,000 has been agreed, at an interest rate of 2% above Base Rate. As at 31 March 2022, £20,000 of the working Capital facility loan had been drawn down. There have been no transactions during the period 1 April 2022 to 30 June 2022.

12. 2021/22 Environmental, Social and Governance (ESG) – updates.

12.1 The Cabinet at its meeting on 4 February 2021 approved the 2021/22 Treasury Management and Investment Strategy, which include Non-Specified investments in Green Energy Bonds and/or other ESG products that met the Council's internal and external due diligence criteria. Following this meeting, the Council external treasury management advisors (Link Asset Services) has been requested to conduct a review looking into what potential investment options would be available to the Council that would fulfil the Council's objective of supporting climate related activities including investing with regard to Environmental, Social and Governance concerns (ESG).

12.2 In terms of typical local authority investments, there is not a wide range of products in this area at the moment, although we expect to see more banks and funds providing specific products over the coming years. As this area continues to develop and become more prominent the council will continue to monitor it and make best use of ESG opportunities when they become available within the parameters of the Council's counterparty criteria and the requirement of the DLUHC Investment Guidance to prioritise security, liquidity before yield in that order of importance.

12.3 The Council now uses the **Standard Chartered Bank Sustainable Time Deposit**, which function just like a normal Time Deposit. The difference is in the sustainable impact where the deposits are referenced against qualifying sustainable loans and projects of Standard Chartered that meet their Green and Sustainable Product Framework. These loan and project assets include green financing, sustainable infrastructure projects, microfinance and access to finance for SME business banking. It addresses the long-term environmental challenges such as climate change, health and financial inclusion plus being dedicated towards financing sustainable loans and projects aligned to the United Nation's Sustainable Development Goals.

12.4 **Sustainable Development Goals**

13 Corporate plan and council policies

13.1 The priority themes were considered as part of the overall Capital Programme which forms part of the Treasury Management Strategy.

14 Financial appraisals

14.1 Financial appraisals were considered as part of the overall Capital Programme which forms part of the Treasury Management Strategy.

15 Legal implications

15.1 Comment from the Legal Services Team is not necessary for this routine monitoring report.

16 Risk management implications

16.1 Risks relating to the timing of borrowing and terms of borrowing are considered and advice is provided by Link. Risk management is considered for each of the schemes within the Capital Programme.

17 Equality analysis

17.1 Equality issues are considered

18 Appendices

18.1 Appendix A - Prudential Indicators 2021/22

18.2 Appendix B - List of Investments made and/or maturing in 2021/22

18.3 Appendix C - 2021/22 Capital Programme Summary

18.4 Appendix D - Revised CIPFA Codes, Updated PWLB Lending Facility Guidance

18.5 Appendix E - The Economy and Interest Rates

18.6 Appendix F - Glossary - Local Authority Treasury Management Terms

19 Background papers

19.1 The Background Papers used in compiling this report were as follows:

CIPFA Treasury Management in the Public Services code of Practice (the Code)

Cross-sectorial Guidance Notes

CIPFA Prudential Code

Treasury Management Strategy and Treasury Management Practices.

Link Asset Services Citywatch and interest rate forecasts