Sunderland City Council

Item No. 5

AUDIT AND GOVERNANCE COMMITTEE **21 July 2023**

TREASURY MANAGEMENT – REVIEW OF PERFORMANCE 2022/2023

Report of the Director of Finance

1 Purpose of the Report

1.1 To report on the Treasury Management borrowing and investment performance for 2022/2023.

2 Description of Decision (Recommendation)

2.1 The Committee is requested to note the Treasury Management performance for 2022/2023.

3 Introduction

3.1 This report sets out the annual borrowing and investment performance for the financial year 2022/2023 in accordance with the requirements of the Treasury Management Policy Statement and Treasury Management Strategy approved by Council on 2nd March 2022. The Treasury Management Strategy comprises the approved Council strategy for borrowing and its policies for managing its investments (which give priority to the security and liquidity of the funds over yield of those investments).

3.2 The Treasury Management Policy Statement and Strategy complied with best practice, including the Ministry of Housing, Communities and Local Government's 'Statutory Guidance on Local Government Investments' updated in February 2018 and also incorporates the recommendations included in the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management, updated in December 2017.

4 Review of Performance 2022/2023

Summary

4.1 The performance of the Council's Treasury Management function continues to maximise financial savings. The average interest rate of the Council's borrowing at 2.55% is low and the Council's treasury management advisor reports this compares favourably with their other local authority clients as does the 2.16% rate of return achieved on investments.

4.2 Whilst the impact of Covid-19 on financial markets has subsided, this has been replaced by the global fallout of Russia's invasion of Ukraine in February 2022 and heightened tension between China, Taiwan and the United States. Unprecedented pressure on household incomes linked to soaring energy prices and food bills which haven't been offset by wage growth has added to tensions in the economy.

Borrowing Strategy and Performance – 2022/2023

4.3 The basis of the agreed Borrowing Strategy was to:

- continuously monitor prevailing interest rates and forecasts;
- secure long-term funds to meet the Council's future borrowing requirement when market conditions were favourable;
- use a benchmark financing rate of 3.00% for long-term borrowing (i.e. all borrowing for a period of one year or more); and
- take advantage of debt rescheduling opportunities as appropriate.

4.4 The Borrowing Strategy has been reviewed by this Committee in July and November 2022 and February 2023 and was updated where necessary to reflect changing circumstances. The Borrowing Strategy for 2022/2023 was based upon internal expertise, supplemented with market data, market information and leading economic forecasts provided by the Council's treasury management adviser, Link Asset Services.

4.5 The strategy for 2022/2023 was to adopt a pragmatic approach in identifying the low points in the interest rate cycle at which to borrow, and to respond to any changing circumstances to seek to secure benefit for the Council. A benchmark financing rate of 3.00% for long-term borrowing was set for 2022/2023 in light of the views prevalent at the time the Treasury Management policy was set in March 2022.

4.6 Interest rate rises in 2022/2023 were originally expected to be small and gradual but by August 2022 it had become clear that inflation was moving up towards 40-year highs and the Bank of England (BoE) would need to take action. The Base Rate started April 2022 at 0.75% but has risen by between 0.25% and 0.75% at each of the next eight meetings of the Monetary Policy Committee (MPC), reaching 4.25% on 23rd March 2023 in an attempt to combat ongoing inflationary pressures, even at the risk of hampering growth, without pushing the economy into recession.

4.7 Consumer Price Index (CPI) inflation surged during the year, peaking at 11.1% in October 2022 and any hopes for significant falls from this level will largely depend on movements in the gas and electricity markets as well as supply-side factors impacting food prices. Whilst most commentators expect the CPI measure of inflation to drop back towards 4% by the end of 2023, as at February 2023 the rate was 10.4% which is over five times the BoE target of 2%.

4.8 Link Asset Services originally expected a gradual rise in PWLB rates over the course of 2022/2023, reflecting an easing of Covid restrictions and the anticipated return to normality. However the escalating conflict in Ukraine, other geo-political tensions, the fallout from the government's huge fiscal loosening plans announced by the then Chancellor and spiralling inflation meant volatility in the financial markets continued. 50-year PWLB interest rates started the financial year in April 2022 at 2.42% (inclusive of the 0.20% discount available to Local Authorities) and rose steadily until reaching a peak of 5.51% on 28th September 2022. From then rates fell to 3.58% at the end of November 2022 before gradually rising to end the financial year at 4.41%.

4.9 The following table shows the average PWLB borrowing rates for each quarter in 2022/2023.

2022/2023	Qtr 1 (Apr - June) %	Qtr 2 (July – Sept) %	Qtr 3 (Oct – Dec) %	Qtr 4 (Jan – Mar) %
SONIA Overnight Rate	0.89	1.55	2.75	3.77
1 year	2.32*	3.27*	4.16*	4.48*
5 year	2.58*	3.25*	4.38*	4.22*
10 year	2.84*	3.41*	4.44*	4.31*
25 year	3.08*	3.79*	4.67*	4.70*
50 year	2.81*	3.52*	4.20*	4.39*

* Rates take account of the 0.2% discount to PWLB rates available to eligible authorities (including the Council) from 1st November 2012.

4.10 In line with discussions with the Council's economic advisors, the Council took advantage of the low borrowing rate troughs that have occurred and has taken out £50 million of new borrowing during the financial year. These rates were considered opportune, and the Treasury Management team continues to closely monitor PWLB rates in line with future capital programme requirements. The new borrowing is summarised in the following table.

Duration	Date of the transaction	Start	Matures	Rate %	Loan Amount £m
48 years	02/08/2022	09/08/2022	09/08/2070	2.79*	50.0

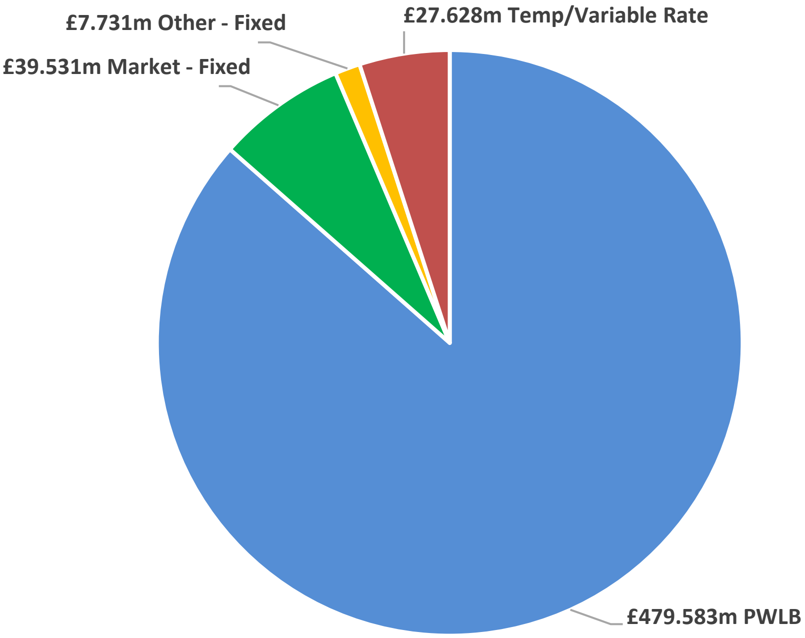
*rate takes account of the 0.20% discount to PWLB rates available to the Council.

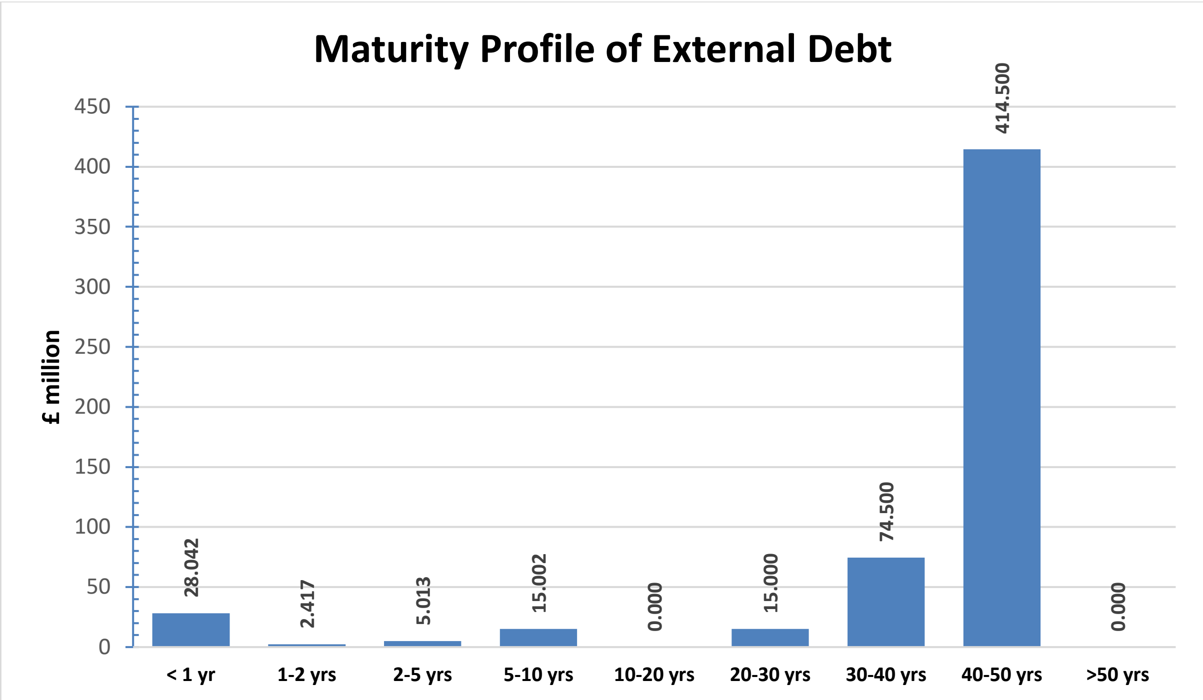
4.11 The Treasury Management Strategy for 2022/2023 included provision for debt rescheduling, whilst accepting that because of the very low underlying rate of the Council's long-term debt it would be difficult to refinance long-term loans at interest rates lower than those already in place. As expected, rates have not been sufficiently favourable for debt rescheduling in 2022/2023.

4.12 The Council's borrowing portfolio position at 31st March 2023 is set out below.

Borrowing Summary at:	31 March 2023		
	Principal	Interest	Ave rate %
Fixed			
PWLB	479,583,333	11,777,204	2.46
Market - Fixed	39,531,020	1,741,445	4.41
Other - Fixed	7,731,391	306	0.00
	526,845,744	13,518,955	2.57
Variable			
Temporary/Other - Variable	27,627,962	618,306	2.24
	27,627,962	618,306	2.24
TOTAL BORROWING:	**554,473,706**	**14,137,261**	**2.55**
TOTAL INVESTMENTS: (All Managed In-house)	**240,770,076**		

NET POSITION:	(313,703,630)





4.13 The Council had a net borrowing position of £313.704 million representing the difference between gross debt and total investments. The net borrowing position is expected to widen (increase) further over the next few years as the Council will need to take out additional borrowing to fund its capital programme

Prudential Indicators – 2022/2023

4.14 All external borrowing and investments undertaken in 2022/2023 have been subject to the monitoring requirements of the Prudential Code. Under the Code, Authorities must set borrowing limits (Authorised Borrowing Limit for External Debt and Operational Boundary for External Debt) and must also report on the Council's performance for all other Prudential Indicators as follows:

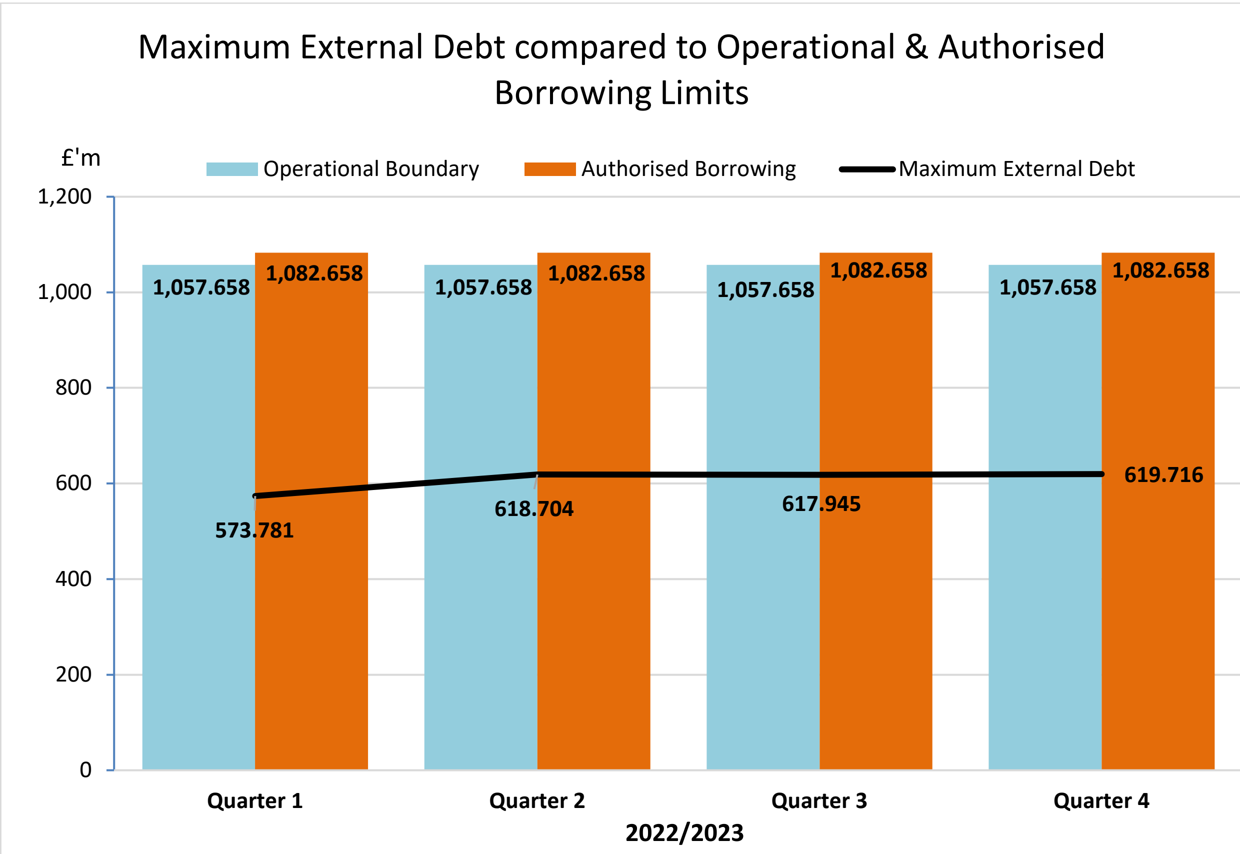
4.15 The statutory limit under section 3(1) of the Local Government Act 2003 (known as the Authorised Borrowing Limit for External Debt) was set by the Council for 2022/2023 as follows:

	£m
Borrowing	939.926
Other Long-Term Liabilities	142.732
Total	1,082.658

The Operational Boundary for External Debt for 2022/2023 was set as follows:

	£m
Borrowing	914.926
Other Long-Term Liabilities	142.732
Total	1,057.658

The Council's maximum external debt in respect of borrowing in 2022/2023 was £619.716 million and is within the borrowing limits set by both of these indicators.



4.16 The table below shows that all other Treasury Management Prudential Indicators have also been complied with:

	Prudential Indicators	2022/2023	
		Limit	Actual
P9	**Maturity Pattern**	Upper Limit	
	Under 12 months	50%	6.74%
	12 months and within 24 months	60%	0.44%
	24 months and within 5 years	80%	0.99%
	5 years plus	100%	93.68%
	A lower limit of 0% for all periods		
P10	**Upper limit for total principal sums invested for over 365 days**	£75.0m	0

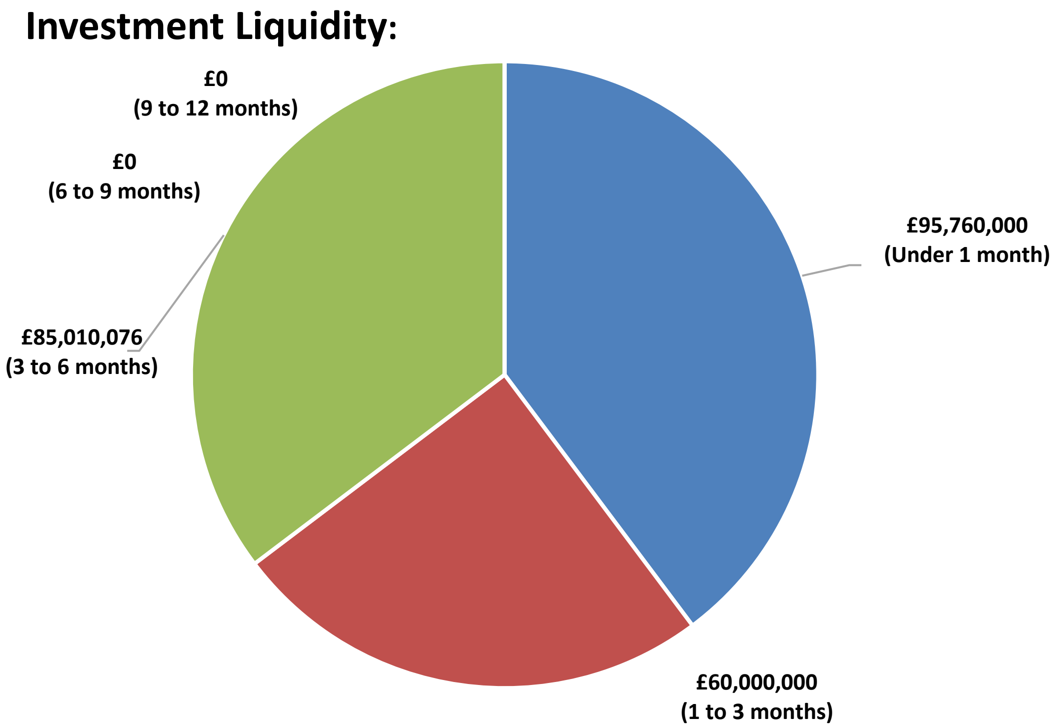
5 Investment Strategy and Performance - 2022/2023

5.1 The Investment Strategy for 2022/2023 was approved by Council on 2nd March 2022. The general policy objective for the Council is the prudent investment of its treasury balances. The Council's investment priorities in order of importance are:

(A) The **security** of capital;
(B) The **liquidity** of its investments and then
(C) The Council aims to achieve the **optimum yield** on its investments, but this is commensurate with the proper levels of security and liquidity.

5.2 At 31st March 2023, the funds managed by the Council's in-house team amounted to £240.770 million and all investments complied with the Annual Investment Strategy.

Investment Summary at 31 March 2023 Borrower	Duration	Amount of Loan	Rate (%)	Start Date	Maturity Date
Call Accounts:					
NatWest SIBA	Overnight	1,500,000	1.00		Call
Prime MMF	Overnight	1,671,000	4.09		Call
Aberdeen Liquidity Fund	Overnight	46,809,000	4.06		Call
Insight Liquidity Fund	Overnight	25,780,000	4.12		Call
Lloyds 95 Day Notice	95d Notice	10,076	2.20		95 day
Sub-total:		**75,770,076**			
Fixed Term Deposits:					
Standard Chartered Bank	273 days	20,000,000	2.470	07-Jul-22	06-Apr-23
Santander UK Plc	273 days	30,000,000	3.310	24-Aug-22	24-May-23
Standard Chartered Bank	182 days	30,000,000	4.150	07-Dec-22	07-Jun-23
Close Brothers	365 days	5,000,000	2.800	13-Jul-22	13-Jul-23
Goldman Sachs Int Bank	182 days	30,000,000	4.095	23-Jan-23	24-Jul-23
Standard Chartered Bank	303 days	10,000,000	5.180	27-Sep-22	27-Jul-23
Goldman Sachs Int Bank	183 days	10,000,000	4.310	13-Mar-23	12-Sep-23
Standard Chartered Bank	183 days	10,000,000	4.470	13-Mar-23	12-Sep-23
Santander UK Plc	365 days	20,000,000	4.100	15-Sep-22	15-Sep-23
Sub-total:		**165,000,000**			
TOTAL:		**240,770,076**			



5.3 The table below shows the return received on these investments compared with the benchmark SONIA (Sterling Overnight Index Average) rate, which the Council uses to assess its performance.

	2022/2023 Return %	2022/2023 Benchmark %
In-house Managed Funds	**2.16**	**2.24**

The return on investments for 2022/2023 is slightly below the benchmark rate, which reflects the volatility in financial markets and the continued rise in the BoE Base Rate. The benchmark rate closely follows the Base Rate and therefore moves in line with any announcements on a daily basis. Fixed term deposits are locked in at the rate available when the investment was placed, which at the time offered a favourable return, but may not keep pace with upward movement in interest rates.

5.4 All investments placed in 2022/2023 have been made in accordance with the approved Investment Strategy and comply with the Criteria and the Approved Lending List approved by Council on 2nd March 2022.

5.5 The investment policy is regularly monitored and reviewed to ensure it has flexibility to take full advantage of any changes in market conditions to the benefit of the Council. Against a backdrop of inflationary pressures, the easing of Covid restrictions, the Russian invasion of Ukraine, and a range of different UK Government policies it is no surprise that UK interest rates have been volatile.

5.6 As reported during the year, investment returns picked up throughout 2022/2023 as the BoE tightened monetary policy. Opening 2022/2023 at 0.75% the Base Rate has risen steadily reaching 4.25% by March 2023, with the potential for further rises in 2023/2024.

5.7 Due to the continuing high volatility within the financial markets, particularly in the Eurozone, the Council continues to hold higher than normal levels of cash balances and advice from our Treasury Management advisers is to continue to restrict investments to shorter term periods.

5.8 As members will be aware, the regular updating of the Council's Authorised Lending List and Criteria is required in the light of financial institution mergers and changes in institutions' credit ratings. Changes made during 2022/2023 have been reported to members previously and the latest Lending List and Criteria are included in the Treasury Management First Quarterly Review 2023/2024 report appearing elsewhere on today's agenda for information.

6 Reason for Decision

6.1 To note the performance for 2022/2023.

7 Alternative Options

7.1 No alternatives are submitted for consideration