Council name	**COTSWOLD DISTRICT COUNCIL**
Name and date of Committee	**AUDIT AND GOVERNANCE COMMITTEE– 25 JULY 2023**
Subject	**TREASURY MANAGEMENT OUTTURN REPORT 2022/23**
Wards affected	N/A
Accountable member	Cllr Mike Evemy, Deputy Leader and Cabinet Member for Finance Email: mike.evemy@cotswold.gov.uk
Accountable officer	David Stanley, Deputy Chief Executive and S151 Officer Email: David.stanley@cotswold.gov.uk
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Summary/Purpose	To receive and discuss details of the Council's Treasury management performance for the period 01 April 2022 to 31 March 2023.
Annexes	Annex A – Economic Background
Recommendation(s)	*That Audit and Governance Committee resolves to:* *1. Consider the Council's Treasury Management performance for the period 1 April 2022 to 31 March 2023.* *2. Agree any comments to be passed to full Council when considering this item.*
Corporate priorities	The Council's Treasury Management Strategy underpins all of the Council Priorities and is relevant to the Council principle of "Value for money – we will use the council's resources wisely but will invest in the fabric and future of the district."
Key Decision	NO
Exempt	NO

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Consultees/ Consultation	Arlingclose Limited – Council's treasury advisors

1. TREASURY MANAGEMENT - INTRODUCTION

1.1 The purpose of the treasury management operation is to ensure that cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in counterparties or instruments commensurate with the Council's low risk approach, pursuing optimum performance while ensuring that security of the investment is considered ahead of investment return. The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure.

1.2 The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer-term cash flow planning, to ensure the Council can meet its capital spending obligations. The management of longer-term cash may involve the arrangement of long and/or short-term loans (external borrowing) or may use longer term cash flow surpluses in lieu of external borrowing (internal borrowing).

1.3 The Council continued to engage the services of Arlingclose for independent treasury advice during the year 2022/23. Arlingclose provide specialist treasury support to 25% of UK local authorities. They provide a range of treasury management services including technical advice on investment management and long-term capital financing. They advise on investment trends, developments, and opportunities consistent with the Council's Treasury Management Strategy.

1.4 The Council's treasury management advisors have provided commentary on the economic background that prevailed during 2022/23. This commentary is provided within Annex A.

2. EXECUTIVE SUMMARY

2.1 This report covers the Treasury Management activity and performance of Cotswold District Council for the period 01 April 2022 to 31 March 2023.

2.2 During the year the Council operated within the treasury limits and prudential indicators as set out in the Treasury Management Strategy approved by Council on the 16 February 2022. Investment interest for 2022/23 has produced a net surplus of £0.511m against the original budget set in February 2022 of £0.582m largely due to increases in interest rates throughout the year and higher levels of surplus cash balances available to invest than budgeted.

2.3 The Council's strategy has been to diversify investments into Pooled Funds in order to reduce risk and increase returns. Pooled Funds have maintained strong returns of dividends and returned over 4.16% (£0.449m) against the £12.5m invested in this area (further details provided in section 4.2)This compares to returns achieved of 1.88% for cash invested in money market funds and call accounts and 2.3% where cash is invested with Government

2.4 The capital values of the Pooled Funds decreased by £1,028,337 from £12.557m to £11.528 during 2022/23. Further detail provided in paragraph 6.2 to 6.7.

2.5 The Council holds a £0.500m loan administered by Abundance Investments Limited for the purpose of Community Municipal Investments. The Council's first Community Municipal Investment (CMI), named 'Cotswold Climate Investment' (CCI) which targeted a £0.500m fundraise closed on the 16 August 2022, fully funded by over 450 investors.

2.6 Due to the rescinding of the Council's Recovery Investment Strategy and slippage in capital expenditure, the Council has continued to have no requirement to borrow or hold any further external debt as at 31 March 2023.

2.7 The treasury management position as at 31 March 2023 is set out in table 1 below together with the year-on-year movements.

Table 1: Treasury Management Summary

	31/3/2022 Actual £m	2022/23 Movement £m	31/3/2023 Balance £m	31/3/2023 Rate %
Short-term borrowing	-	0.451	0.451	2.20
Total borrowing	**-**	**0.451**	**0.451**	**2.20**
Long-term investments	12.551	(1.029)	11.522	4.16
Short-term investments	5.571	(1.210)	4.361	2.30
Cash and cash equivalents	14.795	(2.712)	12.083	1.88
Total investments	**32.917**	**(4.950)**	**27.965**	**2.68**
Net Investments	**32.917**	**(5.402)**	**27.515**	

3. BACKGROUND

3.1 In February 2011, the Council adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice (the CIPFA Code). The CIPFA Code requires the Council to approve reports on treasury management activities at the end of the first half of the financial year and at the end of the financial year.

3.2 The Council's Treasury Management Strategy for 2022/23 was approved at the Council meeting on the 16 February 2022. The Council has invested substantial sums of money and is therefore exposed to financial risks including changes in capital value of funds, the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk are central to the Council's treasury management strategy.

4. BORROWING

4.1 Local authorities can borrow from the Public Works Loan Board (PWLB) provided they can confirm they are not to purchase 'investment assets primarily for yield' in the current or next two financial years, with confirmation of the purpose of capital expenditure from the S151 Officer. Authorities that are purchasing or intending to purchase investment assets primarily for yield will not be able to access the PWLB except to re-finance existing loans or externalise internal borrowing.

4.2 Acceptable use of PWLB borrowing includes service delivery, housing, regeneration, preventative action, re-financing debt and treasury management.

4.3 Competitive market alternatives are available for authorities with or without access to the PWLB. However, the financial strength of the individual authority and borrowing purpose will be scrutinised by commercial lenders.

4.4 The Council is not planning to purchase any investment assets primarily for yield within the next three years and so is able to fully access the PWLB.

4.5 The Council's first Community Municipal Investment (CMI), named 'Cotswold Climate Investment' (CCI) which targeted a £0.500m fundraise closed on the 16 August 2022, fully funded by over 450 investors. As at the 31 March 2023 the Council therefore held a £0.451m loan administered through Abundance Investments Limited for the purpose of Community Municipal Investments at a rate of 2.2%.

4.6 The Council has no further borrowing considerations. There are plans to borrow in the future to fund the Capital Programme. Any borrowing undertaken will be subject to approval by either Cabinet or Council as appropriate.

4.7 In order to determine whether the Council needs to borrow, the underlying need to borrow needs to be compared against the Council's internal borrowing capacity. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR) which is total capital expenditure to be funded by borrowing less any revenue provision made for the Minimum Revenue Provision.

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4.8 Whilst there may be an underlying need to borrow, the Council may not actually undertake external borrowing and may instead use its internal cash balances to fund the borrowing requirement which is known as "internal borrowing."

4.9 For Cotswold District Council, there is a small underlying need to borrow of £0.020m and significant internal borrowing capacity as set out in Table 2 below:

Table 2: Balance Sheet Summary

	31/3/22 Actual £m	2022/23 Movement £m	31/3/23 Actual £m
General Fund CFR	0.016	0.004	0.020
Less: External Borrowing	0	-0.451	-0.451
Less: Usable Reserves	-25.677	2.819	-22.858
Less: Working Capital	-7.262	2.586	-4.676
Available for investment or internal borrowing	**-32.923**	**4.958**	**-27.965**

*A positive figure would indicate a need to externally borrow

4.10 If interest rates were to rise by 1%, then investment income would average 3.68%, whilst borrowing costs (based on 20-year PWLB Loan) would be 5.62%. For every £1m borrowed the cost of carry would cost an additional £19,400 per annum.

5. INVESTMENT PERFORMANCE

5.1 The Council invested funds representing income received in advance of expenditure plus balances and reserves held. During 2022/23, the Authority's investment balance ranged between £26.877 and £54.947 million due to timing differences between income and expenditure. The investment position is shown in table 3 below:

Table 3: Treasury Investment Position

	31/3/2022 Actual £m	2022/23 Movement £m	31/3/2023 Balance £m	31/3/2023 Rate %
Bank of England DMADF	5.50	(1.217)	4.283	2.24
Money Market Funds/Call Accounts	14.795	(2.712)	12.083	0.81
Real Estate Investment Trust (REIT)	1.030	(0.030)	1.000	2.83
Cash Plus Fund	1.072	0.024	1.096	2.26
Pooled Funds (1)	10.520	(1.017)	9.503	4.16
Net Investments	**32.917**	**(4.952)**	**27.965**	

(1) See breakdown at Table 4 and 5 below.

5.2 Both the CIPFA Code and government guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

5.3 Higher levels of cash were held at the start of the financial year due to the impact of the payment of the Government's Covid-19 grants to businesses on cash flow, these balances and diversified over several counterparties and Money Market Funds to manage credit and liquidity risk.

5.4 The investment income budget for 2022/23 is £0.510m, as approved in February 2022, investment income of £1.082m was achieved. Increases in the Base Rate have fed through to higher short-term deposit and MMF interest rates. These have increased from 1.92% at the start of the year to over 3.8% by March. There has been a small increase in Pooled Fund interest, further details are provided in section 6 of this report.

5.5 The year-end investment position analysed between investment types and the year-on-year change in show in table 4 below.

Table 4: Investment Position (Treasury Investments)

	31/3/2022 Actual £m	**2022/23 Movement £m**	**31/3/2023 Balance £m**	**31/3/2023 Rate %**
Banks & building societies (unsecured)	6.093	(2.989)	3.104	0.81
Government (incl. local authorities)	5.500	(1.217)	4.283	2.24
Money Market Funds	8.702	0.277	8.979	2.15
Other Pooled Funds				
- *Federated Cash plus fund*	1.072	0.024	1.096	2.26
- *CCLA Property Fund*	2.706	(0.441)	2.265	3.88
- *CCLA Diversified Multi Asset Income Fund*	1.036	(0.090)	0.946	2.85
- *Schroders Equity Income Fund*	0.859	(0.047)	0.812	6.04
- *M&G UK Strategic Bond Fund*	1.938	(0.127)	1.811	4.59
- *Investec Multi asset income fund*	1.926	(0.105)	1.821	3.85
- *Columbia Threadneedle Equity Income Fund*	2.055	(0.207)	1.848	3.32
Fundamentum - Real Estate Investment Trust	1.030	(0.030)	1.000	2.83
Total investments	**32.917**	**(4.951)**	**27.965**	**2.68**

6. EXTERNALLY MANAGED POOLED FUNDS

6.1 A key aspect of the Council's current investment strategy is to invest into pooled funds in order to increase investment returns. These funds do introduce higher levels of risk as the capital value is not protected and the value of the funds can go up and down. The funds can be drawn down at relatively short notice, but consideration would need to be given as to whether drawing them down would crystalise a capital loss. The funds themselves are invested in different investment classes and therefore risk within the pooled fund is diversified.

6.2 Of the Council's investments, £10.5m are held in externally managed strategic pooled cash, bond, equity, multi-asset and property funds with a further £1m held in a Cash Plus fund and £1m held in a Housing Real Estate Investment Trust (REIT) where short-term security and liquidity are lesser considerations, and the objectives instead are regular revenue income and long-term price stability. These funds generated a total return of £0.449m (4.16%) during 22/23 and the capital values on these funds decreased by £1.028m in the year to 31 March 2023 due to external economic factors as outlined in Annex A including political instability, global economic uncertainty and market confidence. Members are reminded that Pooled Funds are held for the longer-term and the capital value will fluctuate over each financial year.

6.3 The decrease in value is treated as an unrealised capital loss i.e., the loss is not recognised as any gain or loss will only be recognised at the point funds are sold. The Council did not make any further contributions to these funds during 2022/23 with the amount invested remaining at £12.5m.

6.4 The change in the Authority's funds' capital values and income earned over the 12-month period is shown in Table 5.

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Table 5: Pooled Funds, Cash Plus and REIT

Fund Manager	Investment	1st April Fund Value	31st March Fund Value	Dividends in 2022/23	2022/23 Gain/(Loss)	Gain/ (Loss) to Initial Principal	% Return Capital & Dividend 2022/23
	£	£	£	£	£	£	%
CCLA Property	2,500,000	2,683,429	2,241,061	97,024	(442,368)	(258,939)	(12.87)
Schroders Income Maximiser (E)	1,000,000	847,022	801,858	60,367	(45,164)	(198,142)	1.79
M&G UK Income (E)	2,000,000	1,920,825	1,793,403	91,839	(127,422)	(206,597)	(1.85)
Investec Diversified Income (M)	2,000,000	1,921,396	1,814,069	77,045	(107,327)	(185,931)	(1.58)
Threadneedle Bond (B)	2,000,000	2,050,746	1,842,079	66,323	(208,667)	(157,921)	(6.94)
CCLA Diversified Income (M)	1,000,000	1,031,275	939,659	28,399	(91,616)	(60,341)	(6.13)
Federated Cash + (C)	1,000,000	1,071,894	1,096,121	-	24,227	96,121	2.26
Fundamentum Housing REIT	1,000,000	1,030,000	1,000,000	28,250	(30,000)	-	(0.17)
Total current funds	**12,500,000**	**12,556,587**	**11,528,250**	**449,247**	**(1,028,337)**	**(971,750)**	**(8.19)**

Key E- Equity, M-Multi asset, B- Bond, C-Cash

6.5 Pooled funds capital value fell significantly in the financial year, by 8.1%. This period has been a very difficult environment for bonds engendered by global central banks' determination to bring high and persistent inflation under control through increases in policy rates and strong rhetoric. The sell-off in gilts, other sovereign bonds and corporate bonds with a risk in gilt/bond yields (i.e., a fall in price) was reflected in the Council's bond and multi-asset income funds.

6.6 Significant financial market volatility and uncertainty remain due to stagflation fears, little sight of the war in Ukraine ending soon and ongoing supply chain issues, a lingering problem over the past 3 years, yet to be fully resolved.

6.7 As highlighted above, the nature of these funds is that values can fluctuate from one year to another. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Authority's investment objectives are monitored and discussed with Arlingclose on a regular basis. Strategic fund investments are made in the knowledge that capital values will move both up and down on months, quarters and even years; but with the confidence that over a three to five-year period total returns will exceed cash interest rates.

6.8 With the expectation of improved investment income returns during the 2023/24 financial year, it was recommended to Cabinet in July 2023 that any additional investment income above the budgeted level is transferred to a new earmarked reserve ("Treasury Management Risk") to manage higher borrowing costs in the short-term and to mitigate potential changes to the accounting treatment of gains and losses on pooled funds from March 2025.

7. INVESTMENT RETURNS

7.1 The outturn for investment income received in 2022/23 was £1.082m which equates to a 2.63% return (21/22 – 1.18%) on an average investment portfolio of £41.097 million against a budgeted £0.510m an average investment portfolio of £26.98 million. Net loans and investments made a surplus of £0.513m, for the 2022/23 financial year. See table 6 for details.

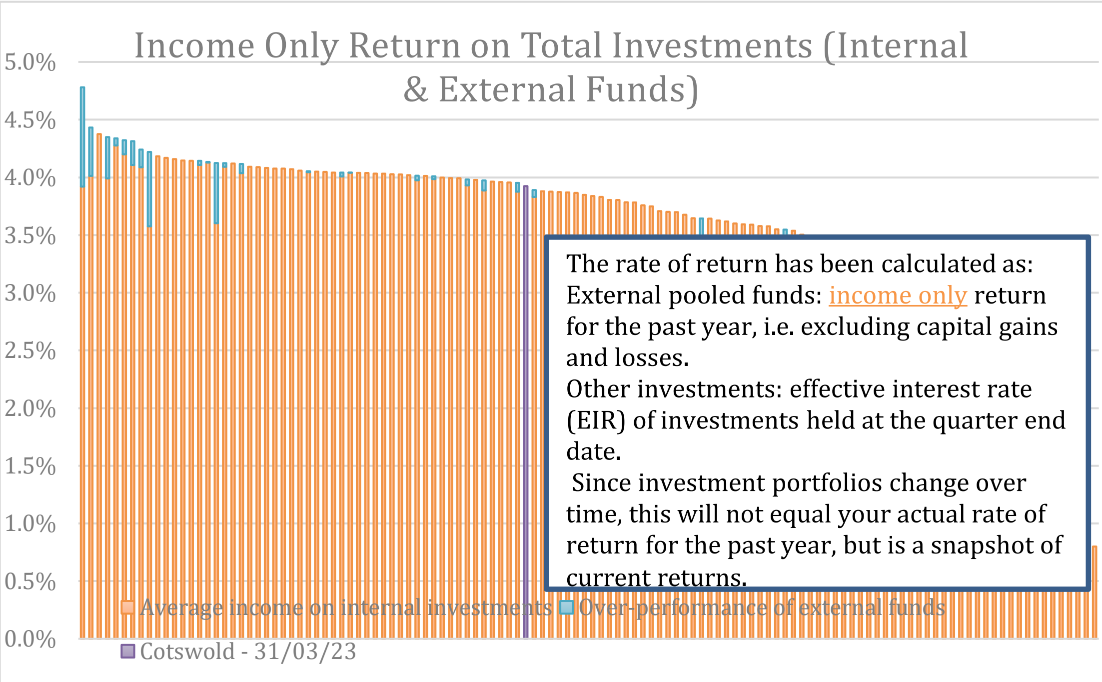
Table 6: Investment income and interest payable versus budget

Investment and Loan Income/Interest Payable	2022/23 Budget £m	2022/23 Actual £m	Variance Surplus/ (Deficit) £m
Community Municipal Borrowing (Interest payable)	(0.007)	(0.006)	0.001
Cottsway Loan*	0.060	-	(0.060)
Long Term Loans	0.012	0.011	(0.001)
Pooled Funds	0.400	0.421	0.021
Housing REIT	0.026	0.028	0.003
Short term	-	0.429	0.429
Call/MMF's	0.084	0.204	0.120
NET Income	**0.574**	**1,087**	**0.513**

*Drawdown of this loan planned for 2023/24

7.2 Table 7 overleaf shows that as at 31 March 2023, Cotswold District Council (purple bar) achieved the 54th highest average rate on investments from the 122 local authorities that Arlingclose support.

Table 7 Cotswold' District Council investment returns v Arlingclose clients (122) as at 31 March 2023.



8. COMPLIANCE REPORT

8.1 The Chief Finance Officer reports that all treasury management activities undertaken during 2022/23 complied fully with the CIPFA Code of Practice and the Authority's approved Treasury Management Strategy.

8.2 Compliance with the authorised limit and operational boundary for external debt is demonstrated in table 8 below.

Table 8: Debt Limits

	31.3.23 Actual £m	2022/23 Operational Boundary £m	2022/23 Authorised Limit £m	Complied
Borrowing	0.451	40.000	45.000	✓

8.3 A £0.500m loan administered by Abundance Investments Limited was taken out in 2022/23 for the purpose of Community Municipal Investments. The authority has no further external debt at 31 March 2023.

9. TREASURY MANAGEMENT INDICATORS

9.1 The Authority measures and manages its exposures to treasury management risks using the following indicators.

Security

9.2 The Authority has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average credit rating of its investment portfolio. This is calculated by applying a score to each investment (AAA=1, AA+=2, etc.) and taking the arithmetic average, weighted by the size of each investment. Unrated investments are assigned a score based on their perceived risk.

Table 9: Portfolio average credit rating

	31.3.23 Actual	2022/23 Target	Complied
Portfolio average credit	AA-	A-	✓

Principal Sums Invested for Periods Longer than 364 days:

9.3 The purpose of this indicator is to control the Authority's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the long-term principal sum invested to final maturities beyond the period end were:

Table 10: Limit on principal invested > 364 days

	2022/23	2023/24	2024/25
Actual principal invested beyond year end	£12.5m	£12.5m	£12.5m
Limit on principal invested beyond year end	£20m	£20m	£20m
Complied	✓	✓	✓

10. ALTERNATIVE OPTIONS

10.1 None

11. FINANCIAL IMPLICATIONS

11.1 The Council maintained an average investment portfolio of £41.097 million during 2022/23. The funds earned an average rate of return of 2.68%, this compares to 1.18% in 2021/22.

11.2 The Council budgeted for £0.582m in treasury investment and loan income for 2022/23. Actual performance was a surplus of £0.511m, with investment and loan income received of £1.093m.

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12. LEGAL IMPLICATIONS

12.1 None

13. RISK ASSESSMENT

13.1 Treasury risk is managed by the application of the Council's Treasury Management Strategy. This report discusses the impact of economic risk on the value and returns associated with the Council's investment portfolio together with the risk of low interest rates on the Council's revenue budget.

14. EQUALITIES IMPACT

14.1 None

15. CLIMATE AND ECOLOGICAL EMERGENCIES IMPLICATIONS

15.1 None

16. BACKGROUND PAPERS

16.1 None

(END)

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ANNEX A

ECONOMIC BACKGROUND

1.1 The war in Ukraine continued to keep global inflation above central bank targets and the UK economic outlook remained relatively weak with the chance of a mild recession. The economic backdrop during the January to March period continued to be characterised by high energy and commodity prices, high inflation, and the associated impact on household budgets and spending.

1.2 Central Bank rhetoric and actions remained consistent with combatting inflation. The Bank of England, US Federal Reserve, and European Central Bank all increased interest rates over the period, even in the face of potential economic slowdowns in those regions.

1.3 Starting the financial year at 5.5%, the annual CPI measure of UK inflation rose strongly to hit 10.1% in July and then 11.1% in October. Inflation remained high in subsequent months but appeared to be past the peak, before unexpectedly rising again in February. Annual headline CPI registered 10.4% in February, up from 10.1% in January, with the largest upward contributions coming from food and housing. RPI followed a similar pattern during the year, hitting 14.2% in October. In February RPI measured 13.8%, up from 13.4% in the previous month.

1.4 Following the decision by the UK government under Rishi Sunak and Jeremy Hunt to reverse some of the support to household energy bills announced under Liz Truss, further support in the form of a cap on what energy suppliers could charge household was announced in the March Budget to run from April until end June 2023. Before the announcement, typical household bills had been due to rise to £3,000 a year from April.

1.5 The Bank of England increased the official Bank Rate to 4.25% during the financial year. From 0.75% in March 2022, the Monetary Policy Committee (MPC) pushed through rises at every subsequent meeting over the period, with recent hikes of 50bps in December and February and then 25bps in March, taking Bank Rate to 4.25%. March's rise was voted by a majority of 7-2, with two MPC members preferring to maintain Bank Rate at 4.0%. The Committee noted that inflationary pressures remain elevated with growth stronger than was expected in the February Monetary Policy Report. The February vote was also 7-2 in favour of a hike, and again with two members preferring to keep Bank Rate on hold.

1.6 From the record-high of 10.6% in October, Eurozone CPI inflation fell steadily to 6.9% in March 2023. Energy prices fell, but upward pressure came from food, alcohol, and tobacco. The European Central Bank continued increasing interest rates over the period, pushing rates up by 0.50% in March, taking the deposit facility rate to 3.0% and the main refinancing rate to 3.5%.

1.7 UK and global equities remained volatile against a backdrop of high and sticky inflation, rapid policy rates tightening and an increasing risk of recession. There was a large sell-off in global equities in April, and again in June and September for both UK and global equities.

1.8 The negative correlation between bonds and equities, which had featured for some years, turned positive in 2022 as both bonds and equities sold off simultaneously against an outlook of sticky inflation and high interest rates. Simultaneously, tighter financial conditions, higher bond yields and challenges in some segments of commercial real estate (e.g., offices post-COVID, high street shops and shopping centres) saw commercial property values fall during 2022, with a large fall in the final calendar quarter.