London Borough of Waltham Forest Annual Treasury Management Review

2022/23

Contents

Annual Treasury Management Review 2022/23

Introduction

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 2022/23. 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 2022/23 the minimum reporting requirements were that the full Council should receive the following reports:

- an annual treasury strategy in advance of the year (Council 03/03/2022).
- a mid-year, (minimum), treasury update report (Council 13/10/2022).
- 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 and Governance Committee before they were reported to the full Council. Member training on treasury management issues was undertaken during the year on 13/10/2022 in order to support members' scrutiny role.

Executive Summary

During 2022/23, 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 – the 2022/23 comparators are the original budget presented to council on the 3rd March 2022 and amended - are as follows:

Prudential and treasury indicators **Capital Expenditure**	**2021/22 Actual £000**	**2022/23 Original Estimate £000**	**2022/23 Actual £000**
General Fund	88,298	98,523	79,200
HRA	54.639	79,755	35,700
Total Capital Programme	142,937	178,278	114,900
Capital Financing Requirement: • Non-HRA • HRA • Total	 332,656 212,255 544,911	 350,989 250,193 601,181	 376,464 212,255 588,720
Gross borrowing	423,395	583,258	450,323
External debt* Finance Leases/PFI	381,144 42,251	544,474 38,784	415,442 34,881
Investments • Longer than 1 year • Under 1 year • Total	 - (74,423) (74,423)	 (70,000) (70,000)	 (59,828) (59,828)
Net borrowing	348,972	513,258	390,495

The Council's actual under-borrowing position for 2022/23 is £173.3m. Investments in the special purpose vehicle and property investments did not materialise. Balances in reserves did not deplete as expected to externalise debt so reliance was made on internal borrowing.

- The Council's average investments for the year is £71m with an average rate 1.93% against the benchmark of the average o/n SONIA (Sterling Overnight Interbank Average Rate) of 2.23%.
- In 2022/23 the investment income is £0.437m.

Other prudential and treasury indicators are to be found in the main body of this report. The Strategic Director of Resources (S151 Officer) confirms that borrowing was only undertaken for a capital purpose and the statutory borrowing limit, (the authorised limit), was not breached.

The financial year 2022/23 continued with the challenging investment environment of previous years, namely low investment returns.

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.

General Fund	2021/22 Actual £000	2022/23 Original Estimate £000	2022/23 Actual £000
Capital expenditure	**88,298**	**99,012**	**79,200**
Capital Receipts	(5,552)	(2,146)	(3,000)
Capital Grants & Reserves	(26,655)	(24,323)	(30,600)
Self- Financing	(37,101)	(5,828)	(21,900)
Revenue	(1,122)	(3,974)	(1,400)
Unfinanced capital expenditure	**(17,868)**	**(62,741)**	**(22,300)**

HRA	2021/22 Actual £000	2022/23 Original Estimate £000	2022/23 Actual £000
Capital expenditure	**54,639**	**54,407**	**35,700**
Financed in year	(43,016)	(39,880)	(35,700)
unfinanced capital expenditure	**-**	**(14,527)**	**-**

Resources – the Council's cash balances comprise revenue and capital resources and cash flow monies. The Council's core cash resources comprised as follows:

General Fund - Balance Sheet Resources	**31 March 2022 £000**	**31 March 2023 £000**
Capital receipts	17,555	13,757
Unapplied Capital Grants	1,204	3,697
Earmarked Reserves	78,330	69,400
Grant Reserves	23,229	22,227
Provisions	21,225	11,955
General fund Balance	14,906	14,905
Total	**156,449**	**135,941**

HRA Balance Sheet Resources (£m)	**31 March 2022 £000**	**31 March 2023 £000**
Balances	5,479	6,000
Earmarked reserves	3,436	1,652
Total	**8,915**	**7,652**

2. The Council's Overall Borrowing Need

The Council's underlying need to borrow to finance capital expenditure is termed as the Capital Financing Requirement (CFR).

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 (2022/23) plus the estimates of any additional capital financing requirement for the current (2023/24) 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 2022/23. The table below highlights the Council's gross borrowing position against the CFR. The Council has complied with this prudential indicator.

General Fund	31 March 2022 Actual £'000	31 March 2023 Estimate £'000	31 March 2023 Actual £'000
CFR General Fund (£m)	332,656	350,989	376,464
CFR HRA (£m)	212,255	250,193	212,255
Total CFR (£m)	**544,911**	**601,181**	**588,720**
Gross borrowing position	(423,395)	(583,258)	(450,323)
Under funding of CFR	**121,516**	**17,923**	**138,397**

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

As at 31st March 2023 the Council under-borrowed position is £173.2m, less finance lease and PFI of £34.8m is £138.4m. In 2021/22 the under-borrowed position was £163m less finance and PFI of £42m was £121m.

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 2022/23 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.

	2022/23 £000
Authorised limit	661,299
Operational boundary	601,181
Maximum gross borrowing position during the year	450,323

3.Treasury Position

The Council's investments and debts outstanding as at 31st March 2023 are £59.8m and £415.4m respectively. The Council's Investments and debts summary are as follow:

	31 March 2022 Principal £'000	Rate/ Return	Interest £'000	31 March 2023 Principal £'000	Rate/ Return	Interest £'000
Fixed rate funding:						
-PWLB	236,286	4.08%	(8,793)	332,874	3.79%	(11,142)
-Market	60,856	3.60%	(2,165)	45,568	4.38%	(2,186)
-Temporary Loan	84,000	0.30%	(457)	37,000	4.31%	(248)
Total debt	**381,142**	**3.16%**	**(11,415)**	**415,442**	**3.90%**	**(13,576)**
CFR	**544,911**			**588,720**		
Over / (under) borrowing	(163,769)			(173,278)		
Investments:						
- in house	74,423	0.28%	0.127	59,828	3.52%	0.437
Total investments	**74,423**	**0.28%**	**(11,288)**	**59,828**	**3.52%**	**(13,139)**

The maturity structure of the investment portfolio as follows.

	31 March 2022 Actual £000	2022/23 Original Estimate £000	31 March 2023 Actual £000
Investments			
Longer than 1 year	-	-	-
Under 1 year	74,423	70,000	59,828
Total	74,423	70,000	59.828

The maturity structure of the debts portfolio as follows:

	31 March 2022 Actual £000	2022/23 original limits £000	31 March 2023 Actual £000
Under 12 months	102,822	18,368	40,456
12 months and within 24 months		33,446	9,801
24 months and within 5 years	16,204	13,511	7,151
5 years and within 10 years	24,074	29,818	75,064
10 years and within 20 years	45,637	46,727	44,125

20 years and within 30 years	5,115	64,600	2,373
30 years and within 40 years	104,318	111,785	96,073
Over 40 years		50,362	140,399
Total	**381,142**	**368,617**	**415,442**

The Council's treasury management debts and investments position is organised by the treasury management service 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.

4. The Strategy for 2022/23

4.1 Investment Strategy

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 3/03/2022. This policy sets out the approach for choosing investment counterparties and is based on credit ratings provided by the three main credit rating agencies, supplemented by additional market data.

In 2022/23 market-implied expectations for the path of Bank Rate over the year ahead had risen, with market pricing consistent with an increase in Bank Rate of 5.00 percentage points, in June 2023, gradually from 4.50% in May 2023 and 4.25% in March 2023. The Council had no liquidity difficulties.

The Treasury team kept the investments short-term (within 365 days). Investment returns have increased with market rate during 2022/23. The expectation for interest rates within the treasury management strategy for 2022/23 was that Bank Rate would stay at 3.25% during 2022/23 as it was not expected that the MPC would be able to deliver on an increase in Bank Rate. Over the last two years, the coronavirus outbreak has done huge economic damage to the UK and to economies around the world.

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 able to cope with extreme stressed market and economic conditions.

Investment balances have been kept to a minimum through the agreed strategy of using reserves, balances to support internal borrowing, and borrowing externally from the financial markets. External borrowing has 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

During 2022-23, 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 low and minimising counterparty risk on placing investments also needed to be considered.

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. 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 Strategic Director of Resources (S151 Officer) therefore monitored interest rates in financial markets and adopted a pragmatic strategy based upon the following principles to manage interest rate risks.

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

Rescheduling
The Council did not undertake any long-term loan rescheduling in the year.

Other Issues (Regulatory changes) Appendix A

Consultation on the Future of the IFRS 9 Statutory Override

The Department for Levelling Up, Housing and Communities (DLUHC) has released a consultation in advance of the current expiry of the qualifying Pooled Fund override to IFRS 9 accounting requirements. The current regulation 30k which was introduced on the 1st April 2018 came to an end on 31st March 2023 and the consultation includes 3 options.

Allow for the statutory override to elapse
Local authorities will be required to apply IFRS 9 as adopted by the code. Application of proper accounting practice adopted in the code (including IFRS 9) is the responsibilities of the Local Authorities and subject to extend audit. Where there is no statutory override in place the fair value movement on any pooled investment funds will need to be recognised as a losses and gains to the revenue account.

Extend the statutory override on a time-limited basis
The government would amend the statutory provision to continue from 1st April 2023 for a specified number of years, after which the statutory override would elapse unless further extended. A further consideration could be to make clear that the government does not except the statutory override to be extended further, following any extension.

Make the statutory override permanent.
The government would amend the statutory provision to remove any time limit and the statutory override would continue to apply from 1st April 2023, unless a future decision were to be made to remove or modify the regulations.

Economic and Interest rates Forecast Appendix B

The Bank of England's MPC acted for a thirteenth consecutive meeting in June, but contrary to market expectations for a 25bps move, it hiked Bank Rate by a further 50bps to 5.00%. There was no change to the voting pattern for a fifth consecutive meeting, with Swati Dhingra and Silvana Tenreyro continuing to vote for no change, arguing that the full extent of hikes made to date had yet to feed through to the economy. In terms of the seven members who voted for the 50bps move, the minutes of the meeting provided the following justification - The MPC recognises that the second-round effects in domestic price and wage developments generated by external cost shocks are likely to take longer to unwind than they did to emerge. There has been significant upside news in recent data that indicates more persistence in the inflation process, against the background of a tight labour market and continued resilience in demand. On the guidance for rates, the minutes were unchanged, stating that the Committee "...will continue to monitor closely indications of persistent inflationary pressures in the economy, including the tightness of labour market conditions and the behaviour of wage growth and services price inflation. If there were to be evidence of more persistent pressures, then further tightening in monetary policy would be required." Looking ahead, the MPC expects growth to be flat in Q2, with it picking up to 0.25% in an "uncertain" Q3. On inflation, the minutes reiterated that price pressures are expected to fall significantly in the second half of this year, with the recent rise in yields also adding to downside pressure on CPI. Finally, Bank Governor Bailey, in his letter to the Chancellor, echoed the sentiment in other major Western Central Banks, saying that the MPC will do what is needed to return CPI to its target. Following the hike to 5%, market expectations now show a further 0.75% of hikes through meetings in August and September but pricing is wavering as to which meeting may provide the 50bps move. Thereafter, November shows the pricing in of another 25bps hike, taking Bank Rate to 6%. Pricing does edge higher to a peak in January 2024, but it is short of a further hike, with levels then easing back modestly through to May. The table below includes Link's and Capital Economics' latest forecasts. Capital Economics revised their forecast in light of the June decision with their revised forecast provided in the table below. Link will review their forecast in the coming days and update clients accordingly. On the investment front, the recent shift in market sentiment and the 50bps June hike has shifted the whole curve higher by around 30-40bps.

Interest Rate Forecasts								
Bank Rate	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25
Link	4.75%	5.00%	5.00%	4.75%	4.50%	4.00%	3.50%	3.25%
Cap Econ	5.00%	5.25%	5.25%	5.25%	5.25%	4.75%	4.50%	4.00%
5Y PWLB RATE								
Link	5.00%	5.00%	5.00%	4.80%	4.50%	4.10%	3.70%	3.50%
Cap Econ	5.40%	5.10%	4.80%	4.60%	4.40%	4.20%	4.00%	4.00%
10Y PWLB RATE								
Link	5.00%	5.00%	5.00%	4.80%	4.40%	4.10%	3.80%	3.60%
Cap Econ	5.20%	5.00%	4.80%	4.60%	4.50%	4.30%	4.10%	4.00%
25Y PWLB RATE								
Link	5.30%	5.30%	5.20%	5.10%	4.80%	4.50%	4.20%	4.00%
Cap Econ	5.30%	5.20%	5.10%	4.90%	4.70%	4.50%	4.30%	4.30%
50Y PWLB RATE								
Link	5.10%	5.10%	5.00%	4.90%	4.60%	4.30%	4.00%	3.80%
Cap Econ	4.90%	4.90%	4.90%	4.80%	4.60%	4.40%	4.30%	4.20%

Glossary of Terms Appendix C

ALMO: An Arm's Length Management Organisation is a not-for-profit company that provides housing services on behalf of a local authority. Usually an ALMO is set up by the authority to manage and improve all or part of its housing stock.

LAS: Link Asset Services, Treasury solutions – the council's treasury management advisers.

CE: Capital Economics - is the economics consultancy that provides Link Asset Services, Treasury solutions, with independent economic forecasts, briefings and research.

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).

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 – CPI. 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.

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.

VRP: a voluntary revenue provision to repay debt, in the annual budget, which is additional to the annual MRP charge, (see above definition).