WEST OXFORDSHIRE DISTRICT COUNCIL	**WEST OXFORDSHIRE DISTRICT COUNCIL**
Name and date of Committee	**AUDIT AND GOVERNANCE COMMITTEE - 25 JULY 2024**
Subject	**2023/24 TREASURY OUTTURN**
Wards affected	**ALL**
Accountable member	Cllr Smith Cabinet Member for Finance Email: alaric.smith@westoxon.gov.uk
Accountable officer	Madhu Richards, Director of Finance Tel: (01993) 861239 Email: Madhu.Richards@westoxon.gov.uk
Report Author	Sian Hannam, Treasury Accountant sian.hannam@publicagroup.uk
Purpose	To advise members of treasury management activity and the performance of internal and external fund managers for 2023/24
Annexes	A – Pooled Fund Detailed Analysis B – Pooled Funds Summary
Recommendations	That the Audit and Governance Committee resolves to: 1. Note the Treasury Management and performance of internal and external funds for 2023/24.
Corporate Priorities	• Putting Residents First • A Good Quality of Life for All • A Better Environment for People and Wildlife • Responding to the Climate and Ecological Emergency • Working Together for West Oxfordshire
Key Decision	No
Exempt	No
Consultees/ Consultation	None

1. BACKGROUND AND SUMMARY

1.1. The overall performance of our investments in 2023/24 was favourable, returning interest of £1,726,274 (4.97%) against a revenue budget of £1,227,228 and achieving an unrealised capital gain of £439,475 (3.27%) in the 12 months to 31st March 2024.

1.2. The capital value of our pooled funds has increased by £439,475 but continued to be affected by uncertainty in the financial markets. The effect in 2023/24 was mostly positive due to buoyed global equities, resilient economic data and falling inflation. Pooled funds are intended to be long term investments where short-term fluctuations in capital value are expected but will provide capital appreciation over the long term.

1.3. After an initial period of caution due to the likelihood of recession, the UK economy fared better than anticipated with a shallow recession, falling inflation and improved consumer confidence providing support for UK equities, with stocks trading at attractive valuations relative to their global peers.

1.4. The council has benefitted from a higher revenue return due to sustained high Base Interest Rate to bring inflation back down to 2.5%. 2023/24 incurred unrealised capital gains of £0.439m, these funds are being monitored closely by Arlingclose and they continue to advise that the capital values will recover over the next 2-3 years as gilts and bond revenue return rates start to decline again.

1.5. The Council complied with all but one (see section 9.4) of the Prudential Indicators for 2023/24 as set in the February 2023 budget.

2 Economic & Financial Markets Background

2.1 UK inflation continued to decline from the 8.7% rate seen at the start of 2023/24. By the last quarter of the financial year headline consumer price inflation (CPI) had fallen to 3.4% in February but was still above the Bank of England's 2% target at the end of the period.

2.2 The UK economy entered a technical recession in the second half of 2023, as growth rates of -0.1% and -0.3% respectively were recorded for Q3 and Q4. Over the 2023 calendar year GDP growth only expanded by 0.1% compared to 2022. Of the recent monthly data, the Office for National Statistics reported a rebound in activity with economy expanding 0.2% in January 2024. While the economy may recover in Q1 2024, the data suggests that prior increases in interest rates and higher price levels are depressing growth, which will continue to bear down on inflation throughout 2024.

2.3 Having begun the financial year at 4.25%, the Bank of England's Monetary Policy Committee (MPC) increased Bank Rate to 5.25% in August 2023 as the UK economy appeared resilient in the face of the dual headwinds of higher inflation and interest rates. The Bank Rate was maintained at 5.25% through to March 2024. Although financial markets shifted their interest rate expectations downwards with expectations of a cut in June, the MPC's focus remained on assessing how long interest rates would need to be restrictive in order to control inflation over the medium term.

Local Context

2.4 The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while balance sheet resources are the underlying resources available for investment. These items are summarised in the tables below.

Balance Sheet resources

Balance Sheet Summary	31.3.24 Actual £m	31.3.25 Forecast £m
General Fund CFR	28.08	32.46
External borrowing	0	2.00
Internal borrowing	28.08	30.46
Less Balance Sheet resources	(32.03)	(27.88)
Net Investments	(3.95)	2.57

Treasury Management Summary

	31.3.23 Balance £m	Movement £m	31.03.24 Balance £m	31.03.24 Rate %
Short-term borrowing	5.013	(5.013)	0	N/A
Total borrowing	5.013	(5.013)	0	
Long-term investments	13.375	0.393	13.768	4.91
Short-term investments	0.064	0.013	0.077	5.29
Cash and cash equivalents	8.159	(6.024)	2.135	5.29
Total investments	**21.598**	**(5.618)**	**15.980**	**4.97**
Net investments	**16.585**	**(0.605)**	**15.980**	

3. Investment Activities

3.1 A counterparty list recommended and reviewed by treasury management advisors Arlingclose is received monthly and the treasury team use this to evaluate options. In response to an improving outlook for credit markets, in January 2024 Arlingclose moved away from its previous temporary stance of a 35-day maximum duration and increased its advised recommended maximum unsecured duration limit on all banks on its counterparty list to 100 days. The treasury team, as with 2022/23, still held the majority of in-house balances in liquid MMF's and Call Accounts, but throughout the year were able to take advantage of short-term deposits with the UK Debt

Management Office (DMO) achieving higher rates than the MMF's. This enabled continued cash support for services the Council provides to the public and provided funding for the Council's capital programme, without the need to borrow.

Treasury Investment Position

	31.3.23 Balance £m	Net Movement £m	31.12.24 Balance £m	31.12.24 Income Return %
Banks & building societies (unsecured)	3.843	(3.843)	0.000	N/A
Bank of England DMADF		0.000	0.000	5.19
Money Market Funds	4.316	(2.181)	2.135	5.29
Other Pooled Funds				
- *Equity & Multi Asset income funds*	8.884	0.317	9.201	4.91
- Bond income funds	3.555	0.137	3.692	4.91
- *Real Estate Investment Trusts*	1.000	(0.047)	0.953	2.85
Total investments	**21.598**	**(5.618)**	**15.980**	**4.97**

3.2 Both the CIPFA and the CLG's Investment Guidance require the Council to invest prudently and have regard to the security and liquidity of investments before seeking the optimum yield. This was maintained by following the Council's counterparty policy as set out in its Treasury Management Strategy Statement for 2023/24. Investments during the year included:

- Investments in AAA-rated Stable Net Asset Value Money Market Funds
- Call accounts and deposits with the UK Debt Management Office (DMO)
- Pooled funds (collective investment schemes) meeting the criteria in SI 2004 No 534 and subsequent amendments.
- Real Estate Investment Trust (REIT)
- Housing Association Bond

3.3 As demonstrated by the liability benchmark in this report, the Council expects to be a long-term borrower and new treasury investments are therefore primarily made to manage day-to-day cash flows using short-term low risk instruments. The existing portfolio of strategic pooled funds will be maintained to diversify risk into different asset classes and boost investment income.

3.4 The progression of risk and return metrics are shown in the Arlingclose quarterly investment benchmarking report; the results of which are summarised in the table below.

Investment Benchmarking – Treasury investments managed in-house

	Credit Score	Credit Rating	Bail-in Exposure	Weighted Average Maturity (days)	Rate of Return %
31.03.2023	3.92	AA-	61%	4	-1.07
30.09.2023	4.32	AA-	60%	7	6.39
30.12.2023	4.67	A+	95%	2	6.73
31.03.2024	5.19	A+	100%	1	7.8
Similar LAs	**4.9**	**A+**	**61%**	**50**	**5.2**
All LAs	**4.82**	**A+**	**61%**	**9**	**5.03**

At the end of September the Council had £7.5m in MMFs and £5m in the DMO, so 60% exposure to Bail-in. At that time DMO interest rates were more favourable than MMF's so more liquidity could be invested there. At the end of December interest rates with the DMO were still between 10 and 20 basis points lower than the MMF's and therefore we invested in the MMF's (£15m) before investing elsewhere. The Council also had a £3m short term investment with Lloyds Bank which is also exposed to Bail-in. So 95% due to £18m of the £19m available to invest was in MMF's and a Lloyds short term deposit. At the end of the year, it is 100%.

Although MMF's are technically exposed to Bail-in the risk is minimal because of the diversification of each fund.

4. Investment Background

4.1 The Council holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. During 2023/24, the Council's investment balance ranged between £25.084 million and £50.519 million. These balances included £9.788m of external loans to Cottsway and Southill Solar, £13.163m in Pooled Funds and £16.272 in cash balances invested in the MMF and DMO. Cash balances fluctuate significantly due to the timing differences in collecting Council Tax, Business Rates, Fees and Charges and government funding and money going out for Precepts and paying the Council's bills.

4.2 Multiple years of funding the capital programme with internal borrowing have reduced cash reserves and the expectation is that there will be reduced levels of invested short term and overnight funds going forward and the Council will need to borrow to fund future capital programmes. New processes are in place to manage cashflow more effectively and reduce the need for large buffers of cash on hand. Managing working capital more effectively reduces our need to borrow and ensures we are earning the maximum amount of return from long term pooled funds.

Investment Returns

4.3 Interest earned in 2023/24 from investments held was £777,008 from short-term deposits and overnight deposits, and £949,266 from long term, Pooled Funds, Extended Loans and Bonds. The return on an average investment balance of £40.063m was 4.97% The net surplus of £449,046 above the budget for the year is made up of a £8,174 over achievement of interest income compared to budget from Pooled Funds and the Housing REIT, and £440,872 overachievement of income compared to budget was made on Bank of England Debt Management Office (Central Government) short term deposits and overnight deposits with Money Market Funds and Call Accounts.

4.4 Investments of £13.982m in Pooled Funds returned 4.57% in dividends and made and unrealised gain of 3.55% (£0.439m) on its capital value compared to a £1.269m loss in 2022/23 (see table below). The capital values as at 31st March 2024 stand at £12.814m, £1.167m lower than the original investments. The loss in 2022/23 was due to the continuation of economic uncertainties that started in 2021/22 and the unprecedented market conditions, and in 2023/24 we have seen an extension of uncertain financial markets with interest rates pushed higher as a response to high inflation. Bond yields continued to be volatile, in contrast global equities were buoyed by healthy corporate earnings, resilient economic data and moderating inflation and the view central banks had reached the peak of their rate tightening cycles.

5. Externally Managed Funds

5.1 Ten years ago the Council decided to invest £12m over several pooled funds. Some of the original funds have been sold and then re-invested into new ones. The performance of each of the current Pooled Funds can be seen in the table below.

Current Pooled Funds

Fund Manager	Original Investment	Value 31st March 2023	Value 31st March 2024	Dividends Received 2023/24	2023/24 Gain/(Loss)	Gain/(Loss) v Original Investment
	£	£	£	£	£	£
UBS (B/E)	2,000,000	1,466,810	1,466,417	93,100	(393)	(533,583)
Schroders (E)	1,000,000	886,450	890,477	62,724	4,027	(109,523)
Threadneedle UK (E)	1,000,000	1,053,841	1,093,543	38,314	39,702	93,543
CCLA Div (B/E)	3,000,000	2,771,963	2,908,273	97,021	136,310	(91,727)
M&G Strategic (B)	2,000,000	1,752,651	1,827,489	85,245	74,838	(172,511)
Royal London (L)	1,982,791	1,784,670	1,842,579	76,924	57,909	(140,212)
Aegon (L)	3,000,000	2,659,023	2,786,106	186,087	127,084	(213,894)
Total –current funds	**13,982,791**	**12,375,408**	**12,814,884**	**639,415**	**439,476**	**(1,167,907)**

(L = Liquidity; B= Bond; E= Equity)

Liquidity = transferable to cash within 2 days

Bond = effectively a loan

Equity = stocks & shares

5.2 These monies are invested in externally managed strategic pooled bond, equity, and multi-asset funds where short-term security and liquidity are lesser considerations when compared with short term cash deposits, and the objectives instead are regular revenue income and long-term price stability. In 2023/24, these funds generated a total dividend return of £0.639m (4.55%) - income that is used to support services in year, and £0.439m (3.55%) of capital gain.

5.3 DLUHC published a consultation on the IFRS 9 pooled investment fund statutory override for English authorities for fair value gains and losses on pooled investment funds which was due to expire with effect from 2023/24. The options under evaluation were to allow the override to lapse, to extend it, or to make it permanent. The override was extended for two years and therefore will remain in place for the 2023/24 and 2024/25 financial years. Under the Regulations, gains and losses resulting from unrealised fair value movements relating to treasury pooled investment funds, that otherwise must be recognised in profit or loss under IFRS 9, are not charged to the revenue account, and must be taken into an unusable reserve account.

5.4 The investment income budget for 2023/24 was set at £1,277,228. Actual investment receipts exceeded budget by £449,046 with an overall level of return of 4.97% with an average investment balance of £40.063m for the financial year. The overall performance is shown in the table below:

Table 2 Investment Performance 2023/24

Investment Performance: 1st April 2023 to 31st March 2024	Pooled Funds	In-House Investments	Housing REIT	External Loans	**Total**
Budget (£)	628,541	337,000	31,200	280,487	**1,277,228**
Budgeted return (%)	4.69	2.70	3.00	3.50	**3.87**
Average Balances (£)	12,184,680	17,112,468	978,573	9,788,088	**40,063,808**
Interest earned (£)	639,415	777,008	28,500	281,351	**1,726,274**
(Over)/Under Budget (£)	(10,874)	(440,008)	2,700	(864)	**(449,046)**
Gross rate of Return (%)	4.55	5.29	2.91	2.87	**4.97**

6. Borrowing Strategy and Activity

6.1 As outlined in the Treasury Management Strategy, the Council's main objective when borrowing has been to strike an appropriately low risk balance between securing lower 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. The Council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio and, where practicable, to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing.

6.2 At 31st March 2024 the Council had no borrowing.

Table 3 Borrowing Position 2023/24

	31.03.2023 Balance £m	Net Movement £m	31.03.2024 Balance £m	Rate %
Local authorities (short-term)	5.013	(5.013)	-	-
Total borrowing	**5.013**	**(5.013)**	-	-

7. Compliance with Prudential Indicators

7.1 The Council can confirm that it has complied with all but one of the Prudential Indicators for 2023/24, which were set in February 2023 as part of the Council's Treasury Management Strategy and Capital Strategy. In compliance with the requirements of the CIPFA Code of Practice this report provides members with a summary report of the treasury management activity during 2023/24. A prudent approach has been taking in relation to investment activity with priority being given to security and liquidity over yield.

Debt Limits

	2023/24 Maximum	**31.3.23 Actual**	**2023/24 Operational Boundary**	**2023/24 Authorised Limit**	**Complied?** Yes/No
Borrowing	£5m	£5,013m	£37.9m	£42.9m	Yes
PFI and Finance Leases	**0**	**0**	**0**	**0**	N/A
Total debt	**£5m**	**£5.013m**	**£37.9**	**£42.9m**	

The Director of Finance reports that all treasury management activities undertaken during the quarter complied with the principles in the Treasury Management Code and the Council's approved

Treasury Management Strategy. Compliance with specific investment limits is demonstrated in the table below.

Investment Limits

	2023/24 Maximum £m	31.03.24 Actual £m	2023/24 Limit £m	Complied? Yes/No
Any single organisation, except the UK Government	3	0	5	YES
Any group of organisations under the same ownership	3	0	5	YES
Any group of pooled funds under the same management	0	0	5	YES
Limit per non-UK country	0	0	1	YES
Registered providers and registered social landlords	9.8	9.7	10	YES
Unsecured investments with banks	3	0	10	YES
Money Market Funds	15	2.1	25	YES
Strategic pooled funds	14	14	25	YES
Real Estate Investment Trusts	1	1	5	YES

8. Looking Forward

8.1 The Bank of England (BoE) Bank Rate currently stands at 5.25% and the Bank of England appears to be on the verge of loosening monetary policy. The MPC will cut rates to stimulate the UK economy but will be reluctant to do so significantly until it is sure there will be no lingering second-round effects. Arlingclose expect rate cuts from Q3 2024 to a low of around 3% by late 2025. Wage growth remains strong, buoyed by significant increases in minimum wage. Labour market data for April suggested that the market was loosening, with employment and vacancies down, and unemployment up. The balance of risks around Bank Rate lie to the upside; the Bank could hold rates until September or even Q4, and the developing upside risks to inflation could limit the extent of monetary easing.

8.2 When the capital value of our pooled funds has recovered, we will have the option of cashing in some of our investments in order to support the capital programme, but the Council will need to balance the need to generate a revenue return from interest - which supports the delivery of front-line services, against the cost of external borrowing. If the return from Treasury Management activity is higher than the cost of borrowing, then it would be wise to retain the pooled funds as the long-term investments they were intended to be. There are also implications to our status as a professional investor under MiFID 2 if we reduce our balance of external investments below £10m.

9. Treasury Management Prudential Indicators

9.1 As required by the 2021 CIPFA Treasury Management code, the Council monitors and measures the following prudential indicators.

Liability Benchmark – This indicator compares the Council's existing borrowing against a liability benchmark that has been calculated to show the lowest risk level of borrowing. The liability benchmark is a valuable tool to help establish whether the Council is likely to be a long-term borrower or long-term investor in the future, and so shape its strategic focus and decision making. It represents an estimate of the cumulative amount of external borrowing the Council must hold to fund its current capital and revenue plans while keeping treasury investments at the minimum level of £4m required to manage day-to-day cash flow

	31.3.24 Actual	31.3.25 Forecast	31.3.26 Forecast
Capital Financing Requirement (CFR)	28.08	32.46	39.38
Less Usable Reserves	(32.03)	(27.88)	(23.95)
Less Working Capital	(12.50)	(17.42)	(23.20)
Net Loans Requirement	(16.45)	(12.84)	(7.77)
Plus Liquidity Allowance	15.00	15.00	15.00
Liability Benchmark	(1.45)	2.16	7.23

As increasing liability benchmark demonstrates that the Council will become a long-term borrower.

9.2 Long Term Treasury Management Investments

The purpose of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments. The prudential limits on the long-term treasury management limits are:

	2024/25	2025/26	2026/27	No fixed date
Limit on principal invested beyond year end	£14m	£14m	£14m	£20m
Actual principal invested beyond year end	0	n/a	n/a	£14m
Complied?	YES	YES	YES	YES

Long-term investments with no fixed maturity date include strategic pooled funds, real estate investment trusts and directly held equity but exclude money market funds and bank accounts with no fixed maturity date as these are considered short-term.

9.3 Security

The Council 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.

	2023/24 Target	31.03.24	Complied?
Portfolio average credit rating	A-	A+	YES

9.4 Interest Rate Exposure

This indicator is set to control the Council's exposure to interest rate risk. The Bank Rate rose from 4.25% on 1st April 2023 to 5.25% in August 2023, it remained at this level as at 31st March 2024.

Interest rate risk indicator	2023/24 Target	31.12.23 Actual	Complied?
Upper limit on one-year revenue impact of a 1% rise in interest rates	-135,000	- 402,962	No
Upper limit on one-year revenue impact of a 1% fall in interest rates	135,000	402,962	No

The impact of a change in interest rates is calculated on the assumption that maturing loans and investment will be replaced at new market rates. The approved Treasury Management Strategy assumed a lower Base Rate in the second half of the year, resulting in non compliance of this indicator.

10. Non-Treasury Management Prudential Indicators

The Authority measures and manages its capital expenditure, borrowing and service investments with references to the following indicators. It is now a requirement of the CIPFA Prudential Code that these are reported on a quarterly basis.

10.1 The Council has undertaken and is planning capital expenditure as summarised below.

	2023/24 Actual £m	2024/25 Forecast £m	2025/26 Forecast £m
Capital Expenditure	4.27	11.28	6.37

10.2 The Capital Strategy approved in February 2024 has reduced the level of capital investment over the life of the MTFS until interest rates have fallen sufficiently for the cost of capital for projects to be affordable. The Capital, Treasury Management and Investment strategies have all been updated as part of the 2024/25 budget setting process.

Capital Financing Requirement

	2023/24 Actual £m	2024/25 Forecast £m	2025/26 Forecast £m
General fund services	9.70	14.08	16.00
Capital Investments	18.38	18.38	23.38
Total CFR	28.08	32.46	39.38

10.3 Gross Debt and the Capital Financing Requirement

Statutory guidance is that debt should remain below the capital financing requirement, except in the short term. The Authority has complied and expects to continue to comply with this requirement in the medium term as is shown below.

	31.03.2024 actual	**31.03.2025 forecast**	**31.03.2026 forecast**
Debt (Incl.PFI & leases)	0.000	2.00	7.00
Capital Financing Requirement	28.08	32.46	39.38

10.4 Debt and the Authorised Limit and Operational Boundary

The Authority is legally obliged to set an affordable borrowing limit (also termed the Authorised Limit for external debt) each year. In line with statutory guidance, a lower "operational boundary" is also set as a warning level should debt approach the limit.

	Maximum debt 2023/24	**Debt at 31.03.24**	**2023/24 Authorised Limit**	**2023/24 Operational Boundary**	**Complied? Yes/No**
Borrowing	5.013m	0	55.06m	50.06m	Yes
Total Debt	**5.013m**	**0**	**0**	**0**	**Yes**

10.5 Net Income from Commercial and Service Investments to Net Revenue Stream

The Authority's income from commercial and service investments as a proportion of its net revenue stream is indicated below.

	2023/24 Forecast £m	2024/25 Budget £m	2025/26 Budget £m
Total Net Income from commercial & service investments	4.37	5.91	5.91
Net Revenue Stream (per MTFS)	14.17	15.15	15.23
Proportion of Net Revenue Stream	30.84%	39.01%	38.80%

10.6 Proportion of Financing costs to Net Revenue Stream

Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP / loans fund repayments are charged to revenue.

	2023/24 Actual £m	2024/25 Forecast £m	2025/26 Forecast £m
Total borrowing costs	0.501	1.611	1.818
Net Revenue Stream (per MTFS)	14.17	15.15	15.23
Proportion of Net Revenue Stream	3.54%	10.63%	11.93%

10.7 Conclusion

Overall, the Q4 position is positive, with above budget returns on investment income and the continued recovery of pooled fund capital values. With the anticipated fall of the Base Rate over the course of Q3 2024 to Q3 2025, Investment Recovery & capital projects could become more financially viable and meet the criteria of the Council's Investment Strategy.

11. Financial Implications

There are no financial implications arising from this report.

12. Legal Implications

There are no legal implications arising from this report.

13. Risk Assessment

None required as a result of this report.

14. Equalities Impact

No direct equalities impact with regards to the content of this report.

15. **Climate and Ecological Emergencies Implications**
None.

16. **Background Papers**
None.