WEST OXFORDSHIRE DISTRICT COUNCIL	**WEST OXFORDSHIRE DISTRICT COUNCIL**
Name and date of Committee	**FINANCE AND MANAGEMENT OVERVIEW AND SCRUTINY COMMITTEE** **WEDNESDAY 6 SEPTEMBER 2023**
Subject	**2022/23 TREASURY OUTTURN**
Wards affected	All
Accountable member	Cllr Levy Cabinet Member for Finance Email: dan.levy@westoxon.gov.uk
Accountable officer	James Howse, Interim Director of Finance Tel: (01993) 861210 Email: James.Howse@westoxon.gov.uk
Summary/Purpose	To advise members of treasury management activity and the performance of internal and external fund managers for 2022/23
Annexes	
Recommendations	That Treasury Management and the performance of internal and external funds for 2022/23 are noted.
Key Decision	NO
Exempt	NO

1. BACKGROUND AND SUMMARY

1.1. The overall performance of our investments in 2022/23 was mixed, returning interest of £1,319,547 or 4.09% against a revenue budget of £1,139,501 but suffering an unrealised capital loss of 9.16% or £1,269,757 in the 12 months to 31st March 2023.

1.2. The capital value of our pooled funds has decreased by £1.269m as they continued to be affected by prevailing economic conditions in world markets, the war in Ukraine, bond and gilt markets and inflation. The pooled funds are intended to be long term investments where short term fluctuations in capital value are expected but some will provide capital appreciation over the long term.

1.3. 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.

1.4. The council has benefitted from a higher revenue return due to unprecedented increases in Base Rate in an attempt to bring inflation back down to 2.5%. As a consequence of this increase in base rates, bond returns and fixed interest returns have incurred unrealised capital losses of £1.269m. These funds are being monitored closely by Arlingclose and they continue to advise that the capital values will recover over the next 2-5 years as gilts and bond revenue return rates start to decline again.

1.5. The Council took out a one month temporary loan of £5m in March 2023 to provide operational cashflow due to the lack of Council Tax and Business Rates income in February and March. In the second half of March the Council received unexpected income which was not included in the cashflow forecast, meaning that we could have met our liabilities without the loan. The additional income received is analysed in the table below.

Unforecast Income	£
Garden Waste prepayments	582,755
Investment Property rent in advance	371,626
Trade Waste prepayments	118,201
S106	219,367
ICT purchases recharged to partner Councils	193,010
Invoice payments received	958,151
Council Tax prepayments	543,346
Grants - Housing, BEIS, Ctax Fuel	799,395
	3,785,851

1.6. The Council complied with all Prudential Indicators for 2022/23 as set in the budget approved by full Council in February 2022.

2. ECONOMIC & FINANCIAL MARKETS BACKGROUND

2.1. Central Bank 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.

2.2. 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.

2.3. 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 hikes of 0.5% in December 2022 and February 2023 and then 0.25% 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.

3. INVESTMENT ACTIVITIES

3.1. A counterparty list recommended and reviewed by treasury management advisors Arlingclose was received monthly and the treasury team used this to evaluate options. At the end of the period any non-UK banks/institutions on its counterparty list were reduced to 35 days as a precautionary measure, bought about by uncertainty in the market. The treasury team, as with 2021/22, still held the majority of in-house balances in liquid Money Market Funds and Call Accounts, but throughout of 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 the services the authority provides to the public and provided funding for the authority's capital programme, without the need to borrow.

3.2. Both the CIPFA and the CLG's Investment Guidance require the Authority 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 2022/23. 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 statutory criteria
- Real Estate Investment Trust (REIT)
- Housing Association Bond

Investment Background

3.3. The Authority holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. During 2022/23, the Authority investment balance ranged between £20.68 million and £47.38 million. These balances include £10.261m of external loans to Cottsway & Southill Solar, £15.283m in Pooled Funds and £17.588m 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 & Charges and government funding and money going out for Precepts and paying the Council's bills.

3.4. 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

3.5. Interest earned in 2022/23 from investments held was £360,465 from short-term deposits and overnight deposits, and £959,082 from long term, Pooled Funds, Extended Loans and Bonds. See Table 2 below for more detail. The return on an average investment balance of £44.483m was 4.09%. The net surplus of £180,046 above budget for the year is made up of a £76,947 underachievement of interest income compared to budget from Pooled Funds and £240,464 overachievement of income compared to budget was made on Bank of England Debt Management Office (Central Government) Short term deposit and overnight deposits with Money Market Funds and Call Accounts.

3.6. In 2021/22 the decision was made to invest a further £4m in high yielding pooled funds using cash balances and the redemption of the Payden and Sterling fund which was underperforming. In 2022/23 funds were added to the Aegon Fund and to the CCLA diversified funds at a level of £2m for each fund. Investments of £13.982m in Pooled Funds returned 3.67% in dividends and made an unrealised loss of 9.16% (£1.269m) on its capital value compared to £151,558 loss in 2021/22 (see table 1). The capital values as at 31st March 2023 stand at £12.375m, £1.614m lower than the original investments. The loss was due to the continuation of economic uncertainties that started in 2021/22 and the unprecedented market conditions occurring due to the high inflation and the fear of recession.

Externally Managed Funds

3.7. Nine years ago the authority 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 1 below.

Table 1 Current Pooled Funds

Fund Manager	Original Investment	Value 31st March 2022	Investment Changes in Year	Value 31st March 2023	2022/23 Dividends Received	2022/23 Capital Gain/(Loss)	Captial Gain/(Loss) vs Original Investment
	£	£	£	£	£	£	£
Payden & Rygel (L)	2,000,000	2,022,253	-2,006,605	3	24,897	-15,644	-6,609
UBS (B/E)	2,000,000	1,753,180		1,466,810	96,242	-286,370	-533,190
Schroders (E)	1,000,000	936,380		886,450	66,692	-49,929	-113,550
Threadneedle UK (E)	1,000,000	1,047,851		1,053,841	36,965	5,990	53,841
CCLA Div (B/E)	1,000,000	1,033,970	2,000,000	2,771,963	83,776	-262,008	-228,037
M&G Strategic (B)	2,000,000	1,950,281		1,752,651	70,041	-197,630	-247,349
Royal London (L)	1,982,791	1,907,033		1,784,670	53,360	-122,363	-198,120
Aegon (L)	1,000,000	1,000,826	2,000,000	2,659,023	154,104	-341,804	-340,977
Total –current funds	11,982,791	11,651,774	1,993,395	12,375,411	586,077	-1,269,758	-1,613,991

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

Liquidity = transferable to cash within 2 days
Bond = effectively a loan
Equity = stocks & shares

3.8. 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 2022/23, these funds generated a total dividend return of £586,077 (3.67%) - income that is used to support services in year, and a £1.269m (9.16%) of capital loss.

3.9. The funds were reviewed during 2021-22 with Arlingclose and it was decided to invest £2m more each into CCLA Diversified and Aegon at the start of 2022-23. Unfortunately, the funds did not appreciate in value as expected due to the ongoing uncertainty in global economics.

3.10. There is a statutory override in place until 31st March 2025 whereby any unrealised fair value gains or losses on pooled investment funds i.e. funds that have not been sold, do not have to be recognised in our General Fund. Instead, these fair value movements are taken into an unusable reserve account.

3.11. The investment income budget for 2022/23 was set at £1,139,501 in February 2022. Actual investment receipts exceeded budget by £180,046 with the overall level of return of 4.09% and with an average investment balance of £44.483m for the financial year. The overall performance is shown in the table below:

Table 2 Investment Performance 2022/23

Investment Performance: 1st April 2022 to 31st March 2023	Pooled Funds	In-House investments	Housing Association Bond	Housing REIT	External Loans	**Total**
Budget (£)	663,025	100,000	65,068	23,175	288,233	**1,139,501**
Budgeted return (%)	4.26	0.75	4.75	2.25	2.86	**2.69**
Average Balances (£)	15,283,365	17,588,840	1,250,000	1,000,000	10,261,781	**44,483,986**
Interest earned (£)	586,077	360,465	55,958	26,875	290,171	**1,319,546**
Over/(Under) Budget (£)	(76,948)	260,465	(9,110)	3,700	1,938	**180,045**
Gross rate of Return (%)	4.16%	2.05%	4.75%	2.69%	2.84%	**4.09%**

4. BORROWING STRATEGY AND ACTIVITY

4.1. As outlined in the Treasury Management Strategy, the Authority's chief objective when borrowing has been to strike a low risk balance between securing lower interest costs and achieving cost certainty over the period for which funds are required. Flexibility to renegotiate loans should the Authority's long-term plans change being a secondary objective. The Authority's borrowing strategy thus far has maintained borrowing and investments below their underlying levels, known as internal borrowing.

4.2 At 31st March 2023 the Authority held short term loans of £5m, an increase of £5m from 31st March 2022, to maintain sufficient operational cashflow to meet the Council's obligations. The loan was repaid in full in April 2023. Outstanding loans on 31st March are summarised in Table 3 below.

Table 3 Borrowing Position 2022/23

	31.03.2022 Balance £m	Net Movement £m	31.03.2023 Balance £m	Rate %
Local authorities (short-term)	-	5.0	5.013	4.40
Total borrowing	**-**	**5.0**	**5.013**	**4.40**

5. COMPLIANCE WITH PRUDENTIAL INDICATORS

5.1. The Council can confirm that it has complied with its Prudential Indicators for 2022/23, which was set in February 2022 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 2022/23. None of the Prudential Indicators have been breached and a prudent approach has been taking in relation to investment activity with priority being given to security and liquidity over yield.

Debt Limits

	2022/23 Maximum	**31.3.23 Actual**	**2022/23 Operational Boundary**	**2022/23 Authorised Limit**	**Complied?** Yes/No
Borrowing	£15m	£5.013m	£41.66m	£46.66m	Yes
PFI and Finance Leases	**0**	**0**	**0**	**0**	N/A
Total debt	**£5m**	**£5.013m**	**£41.66m**	**£46.66m**	

5.2. The Authority's chief 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. Flexibility to renegotiate loans should the Authority's long-term plans change being a secondary objective.

The Authority's borrowing strategy continues to address the key issue of affordability and thus far has maintained borrowing and investments below their underlying levels, known as internal borrowing.

6. LOOKING FORWARD

6.1. The Bank of England (BoE) Bank Rate currently stand at 5.25% and due to inflation still remaining high 6.8% the market is expecting a further two rate hikes in September and November to bring the peak to 5.75%. It is not expected that rates will start to be cut until the third quarter of 2024, although with the pressures on the mortgage and housing market this could happen sooner. The economy is no longer expected to enter a recession and the main concern lies with inflation which is being kept high due to wage growth. The Bank's Monetary Policy Committee does not intend to tighten monetary policy at least until there is clear evidence that significant progress is being made in eliminating spare capacity and achieving the 2% inflation target sustainably.

6.2. During Q1 of 2023/24, the Council has continued to benefit from high interest returns from short term investments through the MMF and DMO. At the end of Q1 interest income is £66,000 above target with a prudent forecast that this will rise to £309,000 by the end of the financial year. In addition, revenue returns from Pooled funds are forecast to be £43,000 higher than budget for the year.

6.3. Looking ahead, our advice from our Treasury Management experts is that the capital value of our pooled funds is likely to recover in the next 2-5 years. We would then have the option of cashing in some of our investments in order to support the capital programme. We will continue to work with our Treasury Advisors to ensure that our investment and borrowing appropriately balance risk and reward (investment values and return performance) in line with the Council's Treasury Management Strategy. This will include consideration of rescheduling our pooled funds and other investments should this become advantageous. Should the Council also need to consider borrowing over the coming year, the Council will need to consider the fixed nature as well as revenue return from investments held (which supports the delivery of front-line services) against the cost of external borrowing. An update on these and other Treasury matters will be reported to members during the course of the year in line with Council's constitution, its scheme of delegation and sector guidance.