

FAREHAM

BOROUGH COUNCIL

Report to Audit and Governance Committee

Date: 21 November 2022

Report of: Deputy Chief Executive Officer

Subject: Treasury Management Strategy

SUMMARY

In accordance with the Chartered Institute of Public Finance and Accountancy (CIPFA) Treasury Management Code of Practice, the Council is required to maintain a Treasury Management Strategy and provide updates on the implementation of that Strategy.

The Audit and Governance Committee is the responsible body to examine and assess the effectiveness of the Council's Treasury Management Policy and Strategy. In accordance with this role, this report sets out the mid-year review of treasury management activity up to 30 September 2022 which confirms compliance with the strategy approved by Full Council on 25 February 2022.

RECOMMENDATION

It is RECOMMENDED that the Audit and Governance Committee: -

- a) reviews the contents of the report; and
- b) provide comments in terms of the effectiveness of the treasury management strategy.

INTRODUCTION

1. The CIPFA (Chartered Institute of Public Finance and Accountancy) Code of Practice for Treasury Management recommends that members be updated on treasury management at least twice yearly (mid-year and at year end). This report therefore ensures the Council is implementing best practice in accordance with the Code.
2. The Council's Treasury Management Strategy for 2022/23 was approved by Full Council on 25 February 2022.
3. The Council has borrowed and invested large sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk remains central to the Council's treasury management strategy.
4. An economic commentary by the Council's Treasury Advisors, Arlingclose, can be found in Appendix B.
5. The Prudential Code includes a requirement for local authorities to provide a Capital Strategy, a summary document approved by Full Council, covering capital expenditure and financing, treasury management and non-treasury investments. The Council's Capital Strategy for 2022/23 was approved by Full Council on 25 February 2022.
6. CIPFA published its revised Treasury Management Code of Practice (the TM Code) and Prudential Code for Capital Finance in December 2021. The key changes in the two codes are around permitted reasons to borrow, knowledge and skills, and the management of non-treasury investments. The principles within the two Codes took immediate effect although local authorities could defer introducing the revised reporting requirements within the revised Codes until the 2023/24 financial year if they wish which the Council has elected to do.
7. This report also includes progress to 30 September 2022 on the Capital Programme.

BORROWING ACTIVITY

8. At 30 September 2022, the Council held £53 million of loans, (a similar position to 31 March 2022). The Council expects to borrow up to an additional £5 million in 2022/23 to part fund the capital programme.
9. The Council's main objective when borrowing continues to be striking an appropriately low risk balance between securing low interest rates and achieving cost certainty over the period for which the funds are required.
10. Borrowing activity to 30 September 2022 was:

	Balance on 31 March 2022 £'000	Balance on 30 Sept 2022 £'000	Average Rate
Long-term borrowing	40,000	40,000	3.50%
Short-term borrowing	10,000	10,000	0.98%
Portchester Crematorium	3,199	3,336	0.80%
Total Borrowing	53,199	53,336	

11. The Council holds investments from Portchester Crematorium Joint Committee which is treated as a temporary loan.
12. The Council's future long-term borrowing is likely to come from the Private Works Loan Board (PWLB). Over the April-September period, short term PWLB rates rose dramatically, particular in late September after the Chancellor's 'mini-budget' included unfunded tax cuts and additional borrowing to fund consumer energy price subsidies. Exceptional volatility threatened financial stability, requiring Bank of England intervention in the gilt market.
13. PWLB interest rates rose by over 2% during the period in both the long and short term. As an indication, the 5-year maturity certainty rate rose from 2.30% on 1 April to 5.09% on 30 September; over the same period the 30-year maturity certainty rate rose from 2.63% to 4.68%.
14. There was no new PWLB borrowing during this period and therefore no implications for the Council with the increased rates.

INVESTMENT ACTIVITY

15. The Council holds invested funds, representing income received in advance of expenditure plus balances and reserves held. During the six-month period, the Council's investment balance ranged between £21 and £28 million due to timing differences between income and expenditure.
16. 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 treasury investments before seeking the optimum 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.
17. Security of capital has remained the Council's main investment objective. This has been maintained by following the Council's counterparty policy as set out in its Treasury Management Strategy Statement for 2022/23. The policy details the high quality and secure counterparty types the Council can invest with.
18. £12 million of the Council's investments is invested in externally managed strategic pooled multi-asset and property funds 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 an average total return of -2.57%, comprising a 3.86% income return which is used to support

services in year, and 6.43% of unrealised capital loss.

19. These funds have no defined maturity date but are available for withdrawal after a notice period. Their performance and continued suitability in meeting the Council's investment objectives are regularly reviewed. 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.
20. Details on investment activity to 30 September 2022 are summarised in the table below:

	Balance on 31 March 2022 £'000	Balance on 30 Sept 2022 £'000	Average Rate
Long-Term Pooled Funds	11,889	10,979	3.86%
Money Market Funds	9,000	8,400	2.03%
Banks and Building Societies	1,300	2,000	1.99%
Local Authorities	0	3,000	1.84%
Debt Management Office	0	3,000	1.43%
Total Investments	22,189	27,379	

21. The Debt Management Office, in the table above, is an executive agency of HM Treasury, responsible for debt and cash management for the UK Government.

COMMERCIAL PROPERTIES (NON-TREASURY INVESTMENTS)

22. The definition of investments in CIPFA's revised 2021 Treasury Management Code covers all the financial assets of the Council as well as other non-financial assets which the Council holds primarily for financial return.
23. Since the Executive approval of a Commercial Property Investment Acquisition Strategy in January 2013, the Council has purchased 10 commercial investment properties as summarised below and is expected to generate rental income of £2.2 million during 2022/23.

Property Type	Value at 31 March 2021 £'000	Value at 31 March 2022 £'000
Retail	19,545	21,745
Commercial (Industrial)	10,665	11,730
Other (Healthcare)	2,130	2,210
Total	32,340	35,685

24. The year-on-year increase in value is principally due to a recovery in the investment market, following the COVID 19 pandemic. This has been across most property sectors, albeit High Street retail remains problematic. The

Council's exposure to this is limited and the focus is on out of town, which has performed much better. Key lease events have had a slightly negative effect on some of these properties, reflecting the cyclical nature of this type of investment. Value has also been affected by a reduction in the Average Weighted Unexpired Lease Term of this portfolio.

25. The Council's total investment property portfolio is shown below. This is more balanced, albeit retail holdings do increase with more exposure to the High Street. This is due to longstanding strategic ownerships, rather than pure investments.

Property Type	Value at 31 March 2021 £'000	Value at 31 March 2022 £'000
Retail	30,673	34,045
Commercial	19,675	23,682
Other	4,645	4,388
Office	4,083	4,740
Leisure	1,225	1,481
Total	60,301	68,336

26. The overall investment property portfolio has increased in value by £8 million mainly due a recovery in the investment market following COVID 19.
27. Property valuations are undertaken annually, to ensure that the Council's balance sheet reflects the current opinion of the value of the Council's assets. Fluctuations in value do not represent actual gains or losses, but do indicate market sentiment, which is often linked to rental income levels and lease terms and conditions.

BUDGETED INCOME AND OUTTURN

28. Since the start of the financial year, there have been five Bank Rate rises with the latest rate being 3% since 3 November. Our treasury advisor, Arlingclose, expects Bank Rate to rise further during 2022/23 to reach 4.25% by the end of the year.
29. The Council's net interest budget for 2022/23 is £678,800 (£637,078 actual in 2021/22). With the current Bank Rate expectations, the budget is likely to be exceeded and will be revised during the revised budget setting period.

COMPLIANCE WITH TREASURY AND PRUDENTIAL INDICATORS

30. The Council confirms compliance with its Treasury and Prudential Indicators for 2022/23, which was set on 25 February 2022 as part of the Council's Treasury Management Strategy.
31. Performance for the first half of the year is shown in Appendix C. During the financial year to date the Council has operated within the treasury limits and

prudential indicators.

Appendices: **A:** Treasury Management Strategy and Prudential Indicators 2022-23
 B: Economic Commentary and Outlook by Arlingclose
 C: Treasury and Prudential Indicators – half yearly performance

Background Papers: None

Reference Papers: Treasury Management Strategy and Prudential Indicators
 2022-23, Council, 25 February 2022

 Prudential Code for Capital Finance in Local Authorities
 (2021)

 Treasury Management in the Public Services Code of
 Practice (2021)

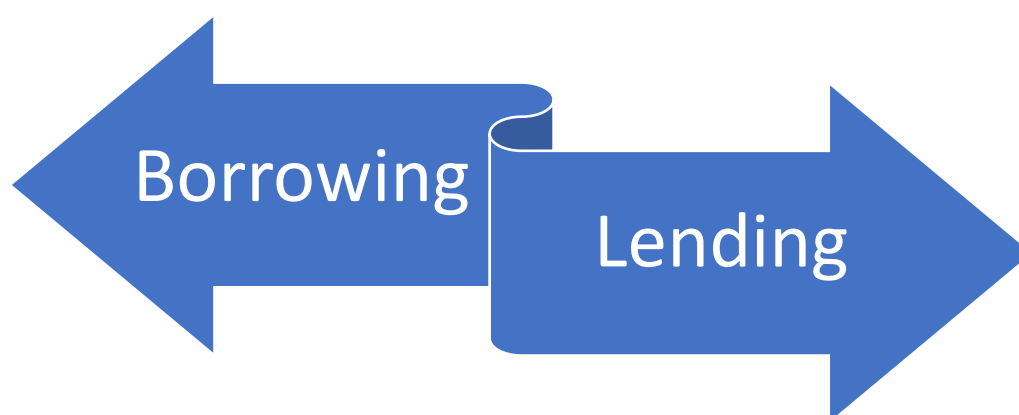
Enquiries:

For further information on this report please contact Caroline Hancock (Ext 4849)

FAREHAM

BOROUGH COUNCIL

TREASURY MANAGEMENT STRATEGY AND INVESTMENT STRATEGY 2022/23





INTRODUCTION

WHAT IS TREASURY MANAGEMENT?

1. Treasury Management is defined as:

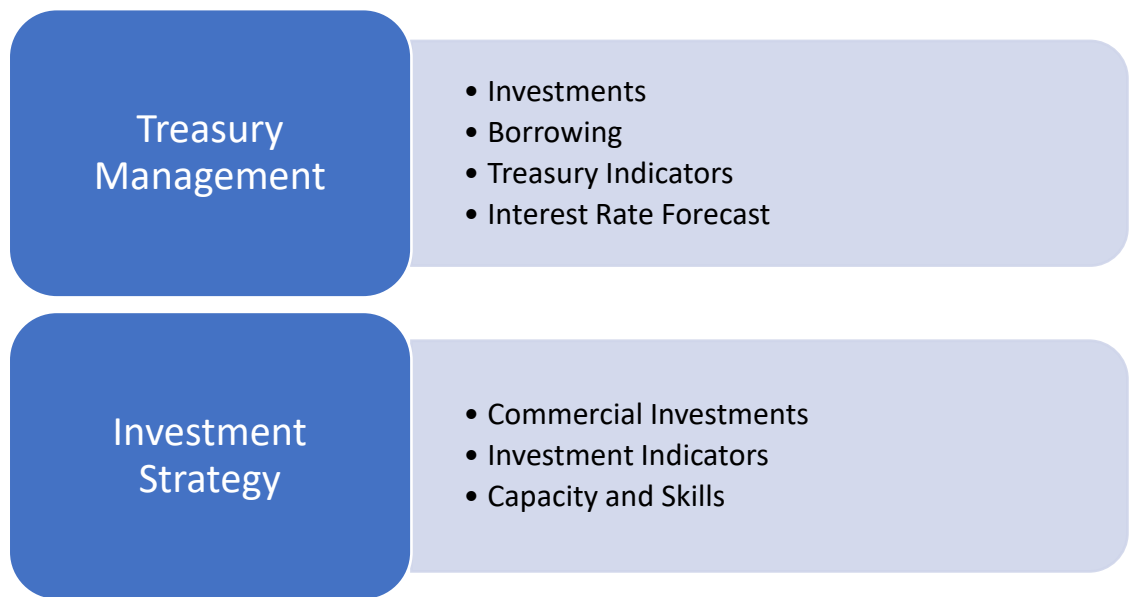
The management of the organisation's cash flows, its banking, money market and capital market transactions;

the effective control of the risks associated with those activities and the pursuit of optimum performance consistent with those risks.

2. The Council operates a balanced budget, which broadly means cash raised during the year will meet its cash expenditure. There are two aspects to the treasury management service:
 - a) To ensure the cash flow is adequately planned, with **cash being available when it is needed**. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's low risk appetite, providing adequate liquidity initially before considering investment return.
 - b) To ensure the cash flow meets the Council's **capital plans**. These capital plans provide a guide to the **borrowing need** of the Council. Essentially this is the longer term cash flow planning to ensure that the Council can meet its capital spending requirements. The management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses. On occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

CONTENT OF THE TREASURY MANAGEMENT AND INVESTMENT STRATEGIES

3. These strategies set out the expected approach to treasury management and investment activities for 2022/23. It covers two main areas:



4. The content of the Strategies is designed to cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, the CIPFA Treasury Management Code and the MHCLG Investment Guidance.

REPORTING REQUIREMENTS

5. The Council receives and approves three main reports each year in relation to Treasury Management, which incorporate a variety of policies, estimates and actuals. The three reports are:



6. The Executive Committee is responsible for the implementation and monitoring of these reports whilst the Audit and Governance Committee is responsible for the effective scrutiny of the treasury management strategy and policies.

TREASURY MANAGEMENT STRATEGY

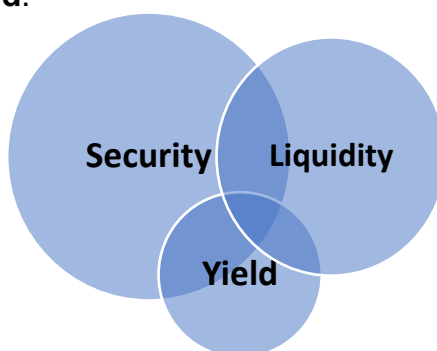
INVESTMENTS

Current Portfolio Position

7. The Council holds invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Council's investment balance has ranged between £16 million and £25 million and similar levels are expected to be maintained in the forthcoming year.

Treasury Investment Strategy

8. The CIPFA Code requires 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**.



9. 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. Where balances are expected to be invested for more than one year, the Council will aim to achieve a total return that is equal or higher than the prevailing rate of inflation, in order to maintain the spending power of the sum invested.
10. Given the increasing risk and very low returns from short-term unsecured bank investments, the Council has diversified **into more secure and/or higher yielding asset classes**. This is the case for the estimated £16 million that is available for longer-term investment. The Council's surplus cash remains invested in short-term unsecured bank deposits and money market funds. This diversification represents a continuation of the strategy adopted in 2018/19.
11. Under the new IFRS 9 standard, the accounting for certain investments depends on the Council's **business model** for managing them. The Council aims to achieve value from its treasury investments by a business model of collecting the contractual cash flows and therefore, where other criteria are also met, these investments will continue to be accounted for at amortised cost.

Approved Counterparties

12. The Council may invest its surplus funds with any of the counterparty types in the table below, subject to the limits shown.

Sector	Time Limit	Counterparty Limit	Sector Limit
UK Government	50 years	Unlimited	n/a
Local authorities and other government entities	25 years	£4m	Unlimited
Secured investments*	25 years	£4m	Unlimited
Banks (unsecured)*	13 months	£2m	Unlimited
Building Societies (unsecured)*	13 months	£2m	£4m
Money market funds*	n/a	£4m	Unlimited
Strategic pooled funds	n/a	£5m	£20m

13. Treasury investments in the sectors marked with an asterisk will only be made with entities whose lowest published **long-term credit rating is no lower than A-**. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used. However, investment decisions are never made solely based on credit ratings, and all other relevant factors including external advice will be taken into account.
14. For entities without published credit ratings, investments may be either (a) where external advice indicates the entity to be of similar credit quality; or (b) to a maximum of £2 million per counterparty as part of a diversified pool.
15. Summary of counterparty types:
- a) **Government:** Loans, bonds and bills issued or guaranteed by national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is generally a lower risk of insolvency, although they are not zero risk. Investments with the UK Government are deemed to be zero risk due to its ability to create additional currency and therefore may be made in unlimited amounts for up to 50 years.
 - b) **Secured investments:** Investments secured on the borrower's assets, which limits the potential losses in the event of insolvency. The amount and quality of the security will be a key factor in the investment decision. Covered bonds and reverse repurchase agreements with banks and building societies are exempt from bail-in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the higher of the collateral credit rating and the counterparty credit rating will be used. The combined secured and unsecured investments in any one bank will not exceed the cash limit for secured investments.
 - c) **Banks and Building Societies (unsecured):** Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to

the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail. See below for arrangements relating to operational bank accounts.

- d) **Money Market Funds:** Pooled funds that offer same-day or short notice liquidity and very low or no price volatility by investing in short-term money markets. They have the advantage over bank accounts of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a small fee. Although no sector limit applies to money market funds, the Council will take care to diversify its liquid investments over a variety of providers to ensure access to cash at all times.
 - e) **Strategic Pooled Funds:** Bond, equity and property funds that offer enhanced returns over the longer term but are more volatile in the short term. These allow the Council to diversify into asset classes other than cash without the need to own and manage the underlying investments. 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 Council's investment objectives will be monitored regularly.
16. The Council may also invest its surplus funds in corporates (loans, bonds and commercial paper issued by companies other than banks), registered providers (loans to, and bonds issued or guaranteed by, registered providers of social housing or registered social landlords, formerly known as housing associations) and real estate investment trusts, subject to meeting the minimum credit rating criteria and time limits recommended by the Council's treasury advisers.

Operational Bank Accounts

17. The Council may incur operational exposures, for example through current accounts, collection accounts and merchant acquiring services, to any UK bank with credit ratings no lower than BBB- and with assets greater than £25 billion. These are not classed as investments but are still subject to the risk of a bank bail-in, and balances will therefore be kept below £4 million per bank. The Bank of England has stated that in the event of failure, banks with assets greater than £25 billion are more likely to be bailed-in than made insolvent, increasing the chance of the Council maintaining operational continuity.

Risk Assessment and Credit Ratings

18. Credit ratings are obtained and monitored by the Council's treasury advisers, who will notify changes in ratings as they occur. The credit rating agencies in current use are listed in the Treasury Management Practices document. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:
- no new investments will be made,
 - any existing investments that can be recalled or sold at no cost will be, and

- full consideration will be given to the recall or sale of all other existing investments with the affected counterparty.
19. Where a credit rating agency announces that a credit rating is on review for possible downgrade (also known as “rating watch negative” or “credit watch negative”) so that it may fall below the approved rating criteria, then only investments that can be withdrawn on the next working day will be made with that organisation until the outcome of the review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.

Other Information on the Security of Investments

20. The Council understands that credit ratings are good, but not perfect predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations, in which it invests, including credit default swap prices, financial statements, information on potential government support and reports in the quality financial press and analysis and advice from the Council treasury management adviser. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may otherwise meet the above credit rating criteria.
21. When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2008 and 2020, this is not generally reflected in credit ratings, but can be seen in other market measures. In these circumstances, the Council will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the Council’s cash balances, then the surplus will be deposited with the UK Government, or with other local authorities. This will cause investment returns to fall but will protect the principal sum invested.
22. The following **internal measures** are also in place:
- Investment and borrowing decisions formally recorded and endorsed using a Counterparty Decision Document.
 - Monthly officer reviews of the investment and borrowing portfolio and quarterly reviews with the Chief Executive Officer.

Investment Limits

23. The Council’s revenue reserves available to cover investment losses are forecast to be £5 million on 31st March 2022. In order to minimise risk, in the case of a single default, the maximum that will be lent to any one organisation (other than the UK Government) will be **£5 million**. A group of entities under the same ownership will be treated as a single organisation for limit purposes.
24. Limits are also placed on fund managers, investments in brokers’ nominee

accounts and foreign countries as in the table below. Investments in pooled funds and multilateral development banks do not count against the limit for any single foreign country, since the risk is diversified over many countries.

	Cash limit
Any group of pooled funds under the same management	£10m per manager
Negotiable instruments held in a broker's nominee account	£10m per broker
Foreign countries	£4m per country

Liquidity Management

25. The Council uses a purpose-built cash flow forecasting spreadsheet to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a prudent basis to minimise the risk of the Council being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Council's medium-term financial plan and cash flow forecast.
26. The Council will spread its liquid cash over at least **four providers** (e.g. bank accounts and money market funds) to ensure that access to cash is maintained in the event of operational difficulties at any one provider.

Environmental, Social and Governance (ESG) Policy

27. The Council will seek to move towards investments that improve the environment, bring wider social benefits, and are with organisations with good governance.
28. The Council will give weight to the environmental, social and governance elements of credit ratings in making investment decisions, provided that the overall risk profile of the investment portfolio (including liquidity risk) is not compromised, and that decisions remain consistent with responsible financial management and stewardship.

BORROWING

Current Portfolio Position

29. The Council's borrowing position at 31 March 2021, with forward projections are summarised below.

£'000	2021/22 Revised	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate
Debt at 1 April	55,967	72,700	77,700	78,700	76,700
Expected change in debt	7,000	5,000	1,000	(2,000)	(2,000)

£'000	2021/22 Revised	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate
Gross Debt at 31 March	62,967	77,700	78,700	76,700	74,700

30. Debt at 31 March 2022 is projected to be lower than originally estimated last year due to the use of internal borrowing rather than borrowing externally to fund the capital programme.

Borrowing Strategy

31. The Council's main objective when borrowing money is to strike an appropriately low risk balance between **securing low interest costs** and achieving **certainty of those costs** over the period for which funds are required. The flexibility to renegotiate loans should the Council's long-term plans change is a secondary objective.
32. Given the significant cuts to public expenditure and in particular to local government funding, the Council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio.
33. With short-term interest rates currently much lower than long-term rates, it is likely to be more cost effective in the short term to either **use internal resources**, or to **borrow short-term** loans instead.
34. By doing so, the Council can reduce net borrowing costs (despite foregone investment income) and **reduce overall treasury risk**. The benefits of internal borrowing or short-term borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise modestly.
35. Our treasury advisers will assist the Council with this '**cost of carry**' and breakeven analysis. Its output may determine whether the Council borrows additional sums at long-term fixed rates in 2022/23 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.
36. The Council has previously raised all of its long-term borrowing from the PWLB but will consider long-term loans from other sources including banks, pensions and local authorities, and will investigate the possibility of issuing bonds and similar instruments, in order to lower interest costs and reduce over-reliance on one source of funding in line with the CIPFA Code.
37. PWLB loans are no longer available to local authorities planning to buy investment assets primarily for yield.
38. Alternatively, the Council may arrange forward starting loans, where the interest rate is fixed in advance, but the cash is received in later years. This would enable certainty of cost to be achieved without suffering a cost of carry in the intervening period.

39. In addition, the Council may borrow further short-term loans to cover unexpected cash flow shortages.

Sources of Borrowing

40. The approved sources of long-term and short-term borrowing are:
- HM Treasury's PWLB lending facility (formerly the Public Works Loan Board).
 - Any institution approved for investments.
 - Any other bank or building society authorised to operate in the UK.
 - Any other UK public sector body.
 - UK public and private sector pension funds (except the Hampshire County Council Pension Fund).
 - Capital market bond investors.
 - UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues.
41. In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:
- Leasing
 - Hire purchase
 - Private Finance Initiative
 - Sale and leaseback
42. **Municipal Bonds Agency:** UK Municipal Bonds Agency plc was established in 2014 by the Local Government Association as an alternative to the PWLB. It issues bonds on the capital markets and lends the proceeds to local authorities. This is a more complicated source of finance than the PWLB for two reasons: borrowing authorities will be required to provide bond investors with a guarantee to refund their investment in the event that the agency is unable to for any reason; and there will be a lead time of several months between committing to borrow and knowing the interest rate payable. Any decision to borrow from the Agency will therefore be the subject of a separate report to full Council.
43. **Short-Term and Variable Rate Loans:** These loans leave the Council exposed to the risk of short-term interest rate rises and are therefore subject to the interest rate exposure limits in the treasury management indicators below.
44. **Debt Rescheduling:** The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. The Council may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall cost saving or a reduction in risk.
45. **Borrowing Limits:** These have been set as part of the Capital Strategy for 2022/23.

TREASURY MANAGEMENT INDICATORS

46. The Council measures and manages its exposures to treasury management risks using the following three treasury management indicators.
47. *Treasury Management Indicator 1 - Principal sums invested for longer than a year:* 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 limits on the long-term principal sum invested to final maturities beyond the year end will be:

£M	2021/22 Revised	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate
Limit on principal invested beyond year end	14	15	16	17	18

48. *Treasury Management Indicator 2 - Maturity structure of borrowing:* This treasury indicator is set to control the Council's exposure to refinancing risk. The upper and lower limits on the maturity structure of borrowing will be:

Maturity structure of borrowing	Upper Limit %	Lower Limit %
- Loans maturing within 1 year	50	0
- Loans maturing within 1 - 2 years	50	0
- Loans maturing within 2 - 5 years	50	0
- Loans maturing within 5 - 10 years	50	0
- Loans maturing in over 10 years	100	100

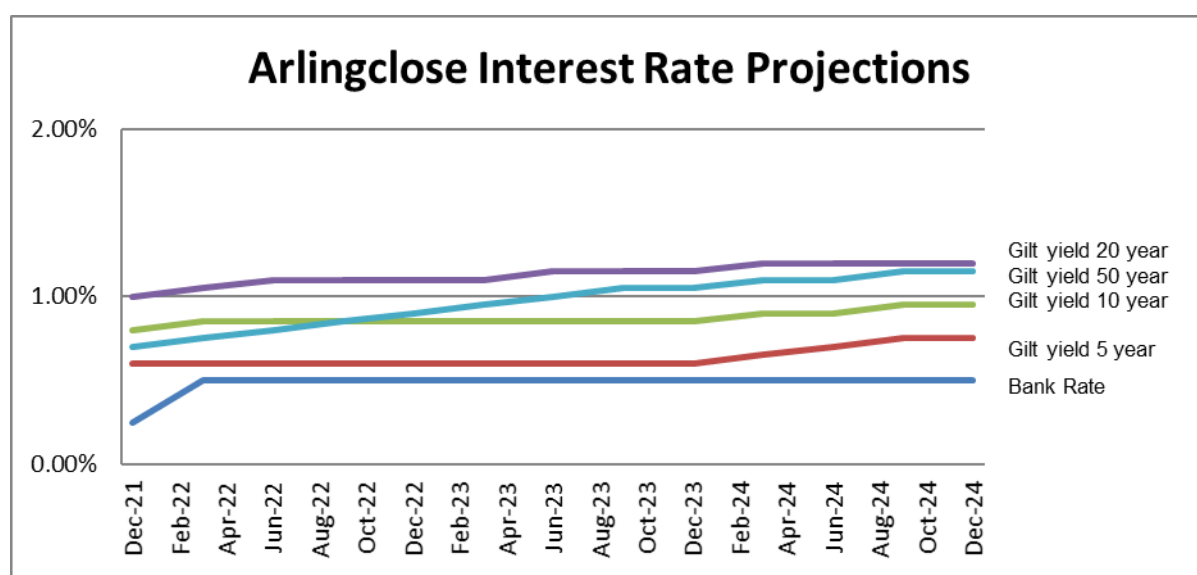
49. Time periods start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment.
50. *Treasury Management Indicator 3 - Housing Revenue Account (HRA) ratios:* As a result of the HRA Reforms in 2012, the Council moved from a subsidy system to self-financing and was required to take on **£49.3 million** of debt. The table below shows additional local indicators relating to the HRA in respect of this debt.

	2021/22 Revised	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate
HRA debt £'000	49,268	49,268	49,268	49,268	49,268
HRA revenues £'000	12,510	12,983	13,104	13,638	14,062
Number of HRA dwellings	2,422	2,422	2,414	2,406	2,398
Ratio of debt to revenues %	3.94:1	3.79:1	3.76:1	3.61:1	3.50:1
Debt per dwelling £	£20,340	£20,340	£20,407	£20,475	£20,543

Debt repayment fund £'000	£5,700	£6,840	£7,980	£9,120	£10,260
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INTEREST RATE FORECAST

51. The Council's treasury management adviser, Arlingclose, assist the Council to formulate a view on interest rates. The latest detailed economic and interest rate forecast provided by Arlingclose is attached at Annex 1.
52. The following graph and commentary gives the Arlingclose's central view on interest rates.



53. Arlingclose is forecasting that Bank Rate will continue to rise in calendar Q1 2022 to subdue inflationary pressures and the perceived desire by the Bank of England to move away from emergency levels of interest rates.
54. Investors continue to price in multiple rises in Bank Rate over the next forecast horizon, and Arlingclose believes that although interest rates will rise again, the increases will not be to the extent predicted by financial markets. In the near-term, the risks around Arlingclose's central case are to the upside while over the medium-term the risks become more balanced.
55. Yields are expected to remain broadly at current levels over the medium-term, with the 5, 10 and 20 year gilt yields expected to average around 0.65%, 0.90%, and 1.15% respectively. The risks around for short and medium-term yields are initially to the upside but shifts lower later, while for long-term yields the risk is to the upside. However, as ever there will almost certainly be short-term volatility due to economic and political uncertainty and events.

Other Items

56. The CIPFA Code requires the Council to include the following in its Treasury Management Strategy.

57. **Policy on Apportioning Interest to the HRA:** On 28 March 2012, the Council borrowed £40 million from the Public Works Loan Board (PWLB) to buy itself out of the HRA subsidy System. The monies were borrowed by the General Fund on behalf of the HRA. The interest on these loans is charged to the HRA on a half-yearly basis at the rate charged by PWLB. A further £9.268 million was lent by the General Fund to the HRA to complete the buyout. Interest on this element is charged at the average weighted rate of the PWLB loans.
58. The unfunded HRA capital financing requirement is also charged to the HRA at the average weighted rate of the PWLB loans.
59. The General Fund credits the HRA with interest earned on HRA credit balances calculated on the monthly movement in reserve balances and applied at year end. The rate used is the weighted interest rate on General Fund investments and cash balances.
60. **Markets in Financial Instruments Directive:** The Council has opted up to professional client status with its providers of financial services, including advisers, banks, brokers and fund managers, allowing it access to a greater range of services but without the greater regulatory protections afforded to individuals and small companies. Given the size and range of the Council's treasury management activities, the Chief Financial Officer believes this to be the most appropriate status.

Financial Implications

61. The budget for net interest received in 2022/23 for the General Fund is £678,800 and the budget for net interest paid in 2022/23 for the HRA is £1,697,300. If actual levels of investments and borrowing, and actual interest rates differ from that forecast, performance against budget will be correspondingly different.

Other Options Considered

62. The CIPFA Code does not prescribe any particular treasury management strategy for local authorities to adopt. The Chief Financial Officer believes that the above strategy represents an appropriate balance between risk management and cost effectiveness. Some alternative strategies, with their financial and risk management implications, are listed below.

Alternative	Impact on income and expenditure	Impact on risk management
Invest in a narrower range of counterparties and/or for shorter times	Interest income will be lower	Lower chance of losses from credit related defaults, but any such losses may be greater
Invest in a wider range of counterparties and/or for longer times	Interest income will be higher	Increased risk of losses from credit related defaults, but any such losses may be smaller
Borrow additional sums at long-term fixed interest rates	Debt interest costs will rise; this is unlikely to be	Higher investment balance leading to a higher impact in

	offset by higher investment income	the event of a default; however long-term interest costs may be more certain
Borrow short-term or variable loans instead of long-term fixed rates	Debt interest costs will initially be lower	Increases in debt interest costs will be broadly offset by rising investment income in the medium term, but long-term costs may be less certain
Reduce level of borrowing	Saving on debt interest is likely to exceed lost investment income	Reduced investment balance leading to a lower impact in the event of a default; however long-term interest costs may be less certain

INVESTMENT STRATEGY

63. The Council invests its money for three broad purposes:
- because it has surplus cash as a result of its day-to-day activities, for example when income is received in advance of expenditure (known as **treasury management investments**),
 - to support local public services by lending to or buying shares in other organisations (**service investments**), and
 - to earn investment income (known as **commercial investments** where this is the main purpose).
64. This investment strategy meets the requirements of statutory guidance issued by the Government in January 2018 and focuses on the third of these categories.
65. The Council does not currently have any service investments.

COMMERCIAL INVESTMENTS

66. The Council invests in local and some regional UK commercial property with the intention of making a profit that will be spent on local public services.
67. Since the Executive approval of a Commercial Property Investment Acquisition Strategy in January 2013, the Council has purchased commercial investment properties currently valued at **£32.3 million** and expected to generate rental income of £2.7 million during 2022/23.

Property Type	Current Value £'000
Retail	19,545
Commercial	10,665
Other	2,130

Total	32,340
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68. The Council's total Commercial property portfolio, shown below, is valued at **£61.5 million** and includes Fareham Shopping Centre, Faretec and industrial estates at Palmerston Business Park and Newgate Lane.

Property Type	Current Value £'000
Retail	30,672
Commercial	19,675
Other	4,645
Office	4,000
Leisure	2,533
Total	61,525

69. A fair value assessment of the Council's more recent commercial property purchases has been made within the past twelve months, and the underlying assets provide security for capital investment.
70. The Council assesses the risk of loss before entering into and whilst holding property investments. These risks are managed by ensuring:
- funds available for new purchases are disaggregated to limit the overall impact that any single investment would have on the Council's finances;
 - there is a mix of property types in the portfolio e.g. retail, industrial, etc.;
 - new purchases are only considered with existing tenants of "high quality" and sufficiently long tenancy term;
 - appropriate checks are carried out to ascertain the tenant's reliability;
 - other "due diligence" is undertaken to protect the Council's investment as far as possible such as checks on planning conditions, land contamination issues and planning policy issues.

Proportionality

71. The Council is dependent on profit generating investment activity to achieve a balanced revenue budget. The table below shows the extent to which the expenditure planned to meet the service delivery objectives is dependent on achieving the expected net profit from investments over the lifecycle of the Medium-Term Financial Strategy.

£'000	2020/21 Actual	2021/22 Revised	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate
Gross service expenditure	46,686	45,620	45,198	46,588	47,197	47,322
Investment income	4,645	5,779	5,477	5,432	5,427	5,427
Proportion	9.9%	12.7%	12.1%	11.7%	11.5%	11.5%

INVESTMENT INDICATORS

72. The Council has set the following three investment indicators to assess the Council's total risk exposure as a result of its investment decisions.
73. *Investment Indicator 1 - Total risk exposure:* The first indicator shows the Council's total exposure to potential investment losses.

£'000	2020/21 Actual	2021/22 Revised	2022/23 Estimate
Treasury Management Investments	18,625	15,000	15,000
Commercial Investments	61,525	61,525	61,525
Total	80,150	76,525	76,525

74. *Investment Indicator 2 - How investments are funded:* Government guidance is that these indicators should include how investments are funded. Since the Council does not normally associate particular assets with particular liabilities, this guidance is difficult to comply with. However, the following investments could be described as being funded by borrowing. The remainder of the Council's investments are funded by usable reserves and income received in advance of expenditure.

£'000	2020/21 Actual	2021/22 Revised	2022/23 Estimate
Treasury Management Investments	0	0	0
Commercial Investments	31,042	30,272	29,479
Total	31,336	30,272	29,479

75. *Investment Indicator 3 - Rate of return received:* This indicator shows the investment income received less the associated costs, including the cost of borrowing where appropriate, as a proportion of the sum initially invested.

	2020/21 Actual	2021/22 Revised	2022/23 Estimate
Treasury Management Investments	3.3%	3.5%	2.7%
Commercial Investments	5.2%	5.6%	5.4%
Total	4.7%	5.1%	4.7%

CAPACITY AND SKILLS

Training

76. The CIPFA Code requires the responsible officer to ensure that members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsible for scrutiny.
77. Treasury management officers regularly attend training courses, seminars and

conferences provided by the Council's treasury management advisers and CIPFA.

78. Property services officers also regularly attend training courses, seminars and conferences provided RICS (Royal Institution of Chartered Surveyors) accredited/approved providers.

Use of Treasury Management Consultants

79. The Council has appointed Arlingclose as treasury management advisers and receives specific advice on investment, debt and capital finance issues.
80. The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers.
81. It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented and subjected to regular review.

ARLINGCLOSE ECONOMIC AND INTEREST RATE FORECAST

Economic Background – December 2021

The ongoing impact on the UK from coronavirus, together with higher inflation, higher interest rates, and the country's trade position post-Brexit, will be major influences on the Authority's treasury management strategy for 2022/23.

The Bank of England (BoE) increased Bank Rate to 0.25% in December 2021 while maintaining its Quantitative Easing programme at £895 billion. The Monetary Policy Committee (MPC) voted 8-1 in favour of raising rates, and unanimously to maintain the asset purchase programme.

Within the announcement the MPC noted that the pace of the global recovery was broadly in line with its November Monetary Policy Report. Prior to the emergence of the Omicron coronavirus variant, the Bank also considered the UK economy to be evolving in line with expectations, however the increased uncertainty and risk to activity the new variant presents, the Bank revised down its estimates for Q4 GDP growth to 0.6% from 1.0%. Inflation was projected to be higher than previously forecast, with CPI likely to remain above 5% throughout the winter and peak at 6% in April 2022. The labour market was generally performing better than previously forecast and the BoE now expects the unemployment rate to fall to 4% compared to 4.5% forecast previously but notes that Omicron could weaken the demand for labour.

UK CPI for November 2021 registered 5.1% year on year, up from 4.2% in the previous month. Core inflation, which excludes the more volatile components, rose to 4.0% y/y from 3.4%. The most recent labour market data for the three months to October 2021 showed the unemployment rate fell to 4.2% while the employment rate rose to 75.5%. In October 2021, the headline 3-month average annual growth rate for wages were 4.9% for total pay and 4.3% for regular pay. In real terms, after adjusting for inflation, total pay growth was up 1.7% while regular pay was up 1.0%. The change in pay growth has been affected by a change in composition of employee jobs, where there has been a fall in the number and proportion of lower paid jobs.

Gross domestic product (GDP) grew by 1.3% in the third calendar quarter of 2021 according to the initial estimate, compared to a gain of 5.5% q/q in the previous quarter, with the annual rate slowing to 6.6% from 23.6%. The Q3 gain was modestly below the consensus forecast of a 1.5% q/q rise. During the quarter activity measures were boosted by sectors that reopened following pandemic restrictions, suggesting that wider spending was flat. Looking ahead, while monthly GDP readings suggest there had been some increase in momentum in the latter part of Q3, Q4 growth is expected to be soft.

GDP growth in the euro zone increased by 2.2% in calendar Q3 2021 following a gain of 2.1% in the second quarter and a decline of -0.3% in the first. Headline inflation has been strong, with CPI registering 4.9% year-on-year in November, the fifth successive month of inflation. Core CPI inflation was 2.6% y/y in November, the fourth month of

successive increases from July's 0.7% y/y. At these levels, inflation is above the European Central Bank's target of 'below, but close to 2%', putting some pressure on its long-term stance of holding its main interest rate of 0%.

The US economy expanded at an annualised rate of 2.1% in Q3 2021, slowing sharply from gains of 6.7% and 6.3% in the previous two quarters. In its December 2021 interest rate announcement, the Federal Reserve continue to maintain the Fed Funds rate at between 0% and 0.25% but outlined its plan to reduce its asset purchase programme earlier than previously stated and signalled they are in favour of tightening interest rates at a faster pace in 2022, with three 0.25% movements now expected.

Credit Outlook – December 2021

Since the start of 2021, relatively benign credit conditions have led to credit default swap (CDS) prices for the larger UK banks to remain low and had steadily edged down throughout the year up until mid-November when the emergence of Omicron has caused them to rise modestly. However, the generally improved economic outlook during 2021 helped bank profitability and reduced the level of impairments many had made as provisions for bad loans. However, the relatively recent removal of coronavirus-related business support measures by the government means the full impact on bank balance sheets may not be known for some time.

The improved economic picture during 2021 led the credit rating agencies to reflect this in their assessment of the outlook for the UK sovereign as well as several financial institutions, revising them from negative to stable and even making a handful of rating upgrades.

Looking ahead, while there is still the chance of bank losses from bad loans as government and central bank support is removed, the institutions on the Authority's counterparty list are well-capitalised and general credit conditions across the sector are expected to remain benign. Duration limits for counterparties on the Authority's lending list are under regular review and will continue to reflect economic conditions and the credit outlook.

Underlying assumptions – December 2021

- The global recovery from the pandemic has entered a more challenging phase. The resurgence in demand has led to the expected rise in inflationary pressure, but disrupted factors of supply are amplifying the effects, increasing the likelihood of lower growth rates ahead. The advent of the Omicron variant of coronavirus is affecting activity and is also a reminder of the potential downside risks.
- Despite relatively buoyant activity survey data, official GDP data indicates that growth was weakening into Q4 2021. Other data, however, suggested continued momentum, particularly for November. Retail sales volumes rose 1.4%, PMIs increased, and the labour market continued to strengthen. The end of furlough did not appear to have had a significant impact on unemployment. Wage growth is elevated.

- The CPI inflation rate rose to 5.1% for November and will rise higher in the near term. While the transitory factors affecting inflation are expected to unwind over time, policymakers' concern is persistent medium term price pressure.
- These factors prompted the MPC to raise Bank Rate to 0.25% at the December meeting. Short term interest rate expectations remain elevated.
- The outlook, however, appears weaker. Household spending faces pressures from a combination of higher prices and tax rises. In the immediate term, the Omicron variant has already affected growth – Q4 and Q1 activity could be weak at best.
- Longer-term government bond yields remain relatively low despite the more hawkish signals from the BoE and the Federal Reserve. Investors are concerned that significant policy tightening in the near term will slow growth and prompt the need for looser policy later. Geo-political and coronavirus risks are also driving safe haven buying. The result is a much flatter yield curve, as short-term yields rise even as long-term yields fall.
- The rise in Bank Rate despite the Omicron variant signals that the MPC will act to bring inflation down whatever the environment. It has also made clear its intentions to tighten policy further. While the economic outlook will be challenging, the signals from policymakers suggest their preference is to tighten policy unless data indicates a more severe slowdown.

Forecast – December 2021

- The MPC will want to build on the strong message it delivered this month by tightening policy despite Omicron uncertainty.
- Arlingclose therefore expects Bank Rate to rise to 0.50% in Q1 2022, but then remain there. Risks to the forecast are initially weighted to the upside but becoming more balanced over time. The Arlingclose central forecast remains below the market forward curve.
- Gilt yields will remain broadly flat from current levels. Yields have fallen sharply at the longer end of the yield curve, but expectations of a rise in Bank Rate have maintained short term gilt yields at higher levels.
- Easing expectations for Bank Rate over time could prompt the yield curve to steepen, as investors build in higher inflation expectations.

- The risks around the gilt yield forecasts vary. The risk for short and medium term yields is initially on the upside but shifts lower later. The risk for long-term yields is weighted to the upside.

APPENDIX B

ECONOMIC COMMENTARY AND OUTLOOK BY ARLINGCLOSE – EARLY OCTOBER 2022

Economic background: The ongoing conflict in Ukraine has continued to put pressure on global inflation and the economic outlook for UK and world growth remains weak. The UK political situation towards the end of the period following the 'fiscal event' increased uncertainty further.

The economic backdrop during the April to September period continued to be characterised by high oil, gas and commodity prices, ongoing high inflation and its impact on consumers' cost of living, no imminent end in sight to the Russia-Ukraine hostilities and its associated impact on the supply chain, and China's zero-Covid policy.

Central Bank rhetoric and action remained robust. The Bank of England, Federal Reserve and the European Central Bank all pushed up interest rates over the period and committed to fighting inflation, even when the consequences were in all likelihood recessions in those regions.

UK inflation remained extremely high. Annual headline CPI hit 10.1% in July, the highest rate for 40 years, before falling modestly to 9.9% in August. RPI registered 12.3% in both July and August. The energy regulator, Ofgem, increased the energy price cap by 54% in April, while a further increase in the cap from October, which would have seen households with average energy consumption pay over £3,500 per annum, was dampened by the UK government stepping in to provide around £150 billion of support to limit bills to £2,500 annually until 2024.

The labour market remained tight through the period but there was some evidence of easing demand and falling supply. The unemployment rate 3m/year for April fell to 3.8% and declined further to 3.6% in July. Although now back below pre-pandemic levels, the recent decline was driven by an increase in inactivity rather than demand for labour. Pay growth in July was 5.5% for total pay (including bonuses) and 5.2% for regular pay. Once adjusted for inflation, however, growth in total pay was -2.6% and -2.8% for regular pay.

With disposable income squeezed and higher energy bills still to come, consumer confidence fell to a record low of -44 in August, down -41 in the previous month. Quarterly GDP fell -0.1% in the April-June quarter driven by a decline in services output, but slightly better than the 0.3% fall expected by the Bank of England.

The Bank of England increased the official Bank Rate to 2.25% over the period. From 0.75% in March, the Monetary Policy Committee (MPC) pushed through rises of 0.25% in each of the following two MPC meetings, before hiking by 0.50% in August and again in September. August's rise was voted by a majority of 8-1, with one MPC member preferring a more modest rise of 0.25%. The September vote was 5-4, with five votes for an 0.5% increase, three for an 0.75% increase and one for an 0.25% increase. The Committee noted that domestic inflationary pressures are expected to

remain strong and so given ongoing strong rhetoric around tackling inflation further Bank Rate rises should be expected.

On 23rd September the UK government, following a change of leadership, announced a raft of measures in a 'mini budget', loosening fiscal policy with a view to boosting the UK's trend growth rate to 2.5%. With little detail on how government borrowing would be returned to a sustainable path, financial markets reacted negatively. Gilt yields rose dramatically by between 0.7% - 1% for all maturities with the rise most pronounced for shorter dated gilts. The swift rise in gilt yields left pension funds vulnerable, as it led to margin calls on their interest rate swaps and risked triggering large scale redemptions of assets across their portfolios to meet these demands. It became necessary for the Bank of England to intervene to preserve market stability through the purchase of long-dated gilts, albeit as a temporary measure, which has had the desired effect with 50-year gilt yields falling over 100bps in a single day.

Bank of England policymakers noted that any resulting inflationary impact of increased demand would be met with monetary tightening, raising the prospect of much higher Bank Rate and consequential negative impacts on the housing market.

After hitting 9.1% in June, annual US inflation eased in July and August to 8.5% and 8.3% respectively. The Federal Reserve continued its fight against inflation over the period with a 0.5% hike in May followed by three increases of 0.75% in June, July and September, taking policy rates to a range of 3% - 3.25%.

Eurozone CPI inflation reached 9.1% y/y in August, with energy prices the main contributor but also strong upward pressure from food prices. Inflation has increased steadily since April from 7.4%. In July the European Central Bank increased interest rates for the first time since 2011, pushing its deposit rate from -0.5% to 0% and its main refinancing rate from 0.0% to 0.5%. This was followed in September by further hikes of 0.75% to both policy rates, taking the deposit rate to 0.75% and refinancing rate to 1.25%.

Financial markets: Uncertainty remained in control of financial market sentiment and bond yields remained volatile, continuing their general upward trend as concern over higher inflation and higher interest rates continued to dominate. Towards the end of September, volatility in financial markets was significantly exacerbated by the UK government's fiscal plans, leading to an acceleration in the rate of the rise in gilt yields and decline in the value of sterling.

Due to pressure on pension funds, the Bank of England announced a direct intervention in the gilt market to increase liquidity and reduce yields.

Over the period the 5-year UK benchmark gilt yield rose from 1.41% to 4.40%, the 10-year gilt yield rose from 1.61% to 4.15%, the 20-year yield from 1.82% to 4.13% and the 50-year yield from 1.56% to 3.25%. The Sterling Overnight Rate (SONIA) averaged 1.22% over the period.

Credit review: Having completed its full review of its credit advice on unsecured deposits at UK and non-UK banks, in May Arlingclose extended the maximum duration limit for five UK banks, four Canadian banks and four German banks to six months.

The maximum duration for unsecured deposits with other UK and non-UK banks on Arlingclose's recommended list is 100 days. These recommendations were unchanged at the end of the period.

Arlingclose continued to monitor and assess credit default swap levels for signs of credit stress but made no changes to the counterparty list or recommended durations. Nevertheless, increased market volatility is expected to remain a feature, at least in the near term and, as ever, the institutions and durations on the Authority's counterparty list recommended by Arlingclose remains under constant review.

Economic outlook: Arlingclose expects Bank Rate to rise further during 2022/23 to reach 4.25% by the end of the year.

The MPC is particularly concerned about the demand implications of fiscal loosening, the tight labour market, sterling weakness and the willingness of firms to raise prices and wages.

The MPC may therefore raise Bank Rate more quickly and to a higher level to dampen aggregate demand and reduce the risk of sustained higher inflation. Arlingclose now expects Bank Rate to peak at 5.0%, with 200bps of increases this calendar year.

This action by the MPC will slow the economy, necessitating cuts in Bank Rate later in 2024.

Gilt yields will face further upward pressure in the short term due to lower confidence in UK fiscal policy, higher inflation expectations and asset sales by the BoE. Given the recent sharp rises in gilt yields, the risks are now broadly balanced to either side. Over the longer term, gilt yields are forecast to fall slightly over the forecast period.

Background: Monetary policymakers are behind the curve having only raising rates by 50bps in September. This was before the "Mini-Budget", poorly received by the markets, triggered a rout in gilts with a huge spike in yields and a further fall in sterling. In a shift from recent trends, the focus now is perceived to be on supporting sterling whilst also focusing on subduing high inflation.

There is now an increased possibility of a special Bank of England MPC meeting to raise rates to support the currency. Followed by a more forceful stance over concerns on the looser fiscal outlook. The MPC is therefore likely to raise Bank Rate higher than would otherwise have been necessary given already declining demand. A prolonged economic downturn could ensue.

Uncertainty on the path of interest rates has increased dramatically due to the possible risk from unknowns which could include for instance another Conservative leadership contest, a general election, or further tax changes including implementing windfall taxes.

The government's blank cheque approach to energy price caps, combined with international energy markets priced in dollars, presents a fiscal mismatch that has contributed to significant decline in sterling and sharp rises in gilt yields which will feed through to consumers' loans and mortgages and business funding costs.

UK government policy has mitigated some of the expected rise in energy inflation for households and businesses flattening the peak for CPI, whilst extending the duration of elevated CPI. Continued currency weakness could add inflationary pressure.

The UK economy already appears to be in recession, with business activity and household spending falling. The short- to medium-term outlook for the UK economy is relatively bleak.

Global bond yields have jumped as investors focus on higher and stickier US policy rates. The rise in UK government bond yields has been sharper, due to both an apparent decline in investor confidence and a rise in interest rate expectations, following the UK government's shift to borrow to loosen fiscal policy. Gilt yields will remain higher unless the government's plans are perceived to be fiscally responsible.

The housing market impact of increases in the Base Rate could act as a "circuit breaker" which stops rates rising much beyond 5.0%, but this remains an uncertainty.

2022/23 INDICATORS – HALF YEARLY PERFORMANCE

PRUDENTIAL INDICATORS

1) Capital Expenditure and Financing

ON TRACK

This prudential indicator is a summary of the Council's capital expenditure plans and shows how these plans are being financed by capital or revenue resources. The revised budget includes £1.98 million carried forward from 2021/22.

Capital Expenditure and Financing	Revised Estimate £'000	Actual to 30 Sept £'000
Health and Public Protection	9	0
Streetscene	38	0
Leisure and Community	5,764	660
Housing	646	330
Planning and Development	231	0
Policy and Resources	9,526	309
Total General Fund	16,214	1,299
HRA	9,460	3,517
Total Expenditure	25,674	4,816
Capital Receipts	3,626	182
Capital Grants/Contributions	7,684	1,247
Capital Reserves	4,629	2,988
Revenue	1,802	399
Internal Borrowing	7,933	0
Total Financing	25,674	4,816

Expenditure to 30 September is within the overall revised budget for the year. The budgets will be reviewed and re-phased where applicable as part of the forthcoming budget setting process.

2) The Council's Borrowing Need (Capital Financing Requirement)

ON TRACK

The Capital Financing Requirement (CFR) is the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's underlying borrowing need. Any capital expenditure financed by borrowing will increase the CFR.

The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual revenue charge which broadly reduces the borrowing in line with the asset's life.

	Estimate £'000	Actual to 30 Sept £'000
General Fund	65,102	58,754
HRA	55,009	51,054
Total CFR	120,111	109,808

The CFR is lower than projected due to no internal borrowing for the first 6 months of the year.

3) Borrowing - Gross Debt and the Capital Financing Requirement

ON TRACK

Statutory guidance is that debt should remain below the capital financing requirement, except in the short-term. The indicator shows that total debt is expected to remain below the CFR.

£'000	Estimate	Actual to 30 Sept
Debt at 1 April	72,700	53,336
Capital Financing Requirement (CFR)	120,111	109,808

4) Borrowing - Limits to Borrowing Activity

ON TRACK

The actual debt levels are monitored against the Operational Boundary and Authorised Limit for External Debt, below.

£'000	Limit	Actual to 30 Sept
Operational Boundary	139,000	53,336
Authorised Limit	147,000	53,336

Total debt at 30 September was £53 million. During the first half of 2022/23 the Authorised Limit of £147 million was not breached at any time.

5) Financing Costs as % of Net Revenue Stream

ON TRACK

This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet financing costs, net of investment income.

	Estimate	Actual to 30 Sept
General Fund	7%	2%
HRA	15%	13%

TREASURY INDICATORS

6) Investments - Principal Sums Invested for Periods Longer than a year

ON TRACK

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.

£M	Estimate	Actual
Limit on principal invested beyond year end	15	11

£11 million is placed with externally managed strategic pooled diversified income funds which are long-term investments. The remaining investments are currently placed for less than a year to allow cash to be available for schemes in the capital programme that require internal borrowing.

7) Maturity Structure of Borrowing

ON TRACK

This indicator is set to control the Council's exposure to refinancing risk. The upper and lower limits on the maturity structure of fixed rate borrowing are:

Maturity Structure of Borrowing	Upper Limit %	Actual %
Loans maturing within 1 year	50	25
Loans maturing within 1 - 2 years	50	0
Loans maturing within 2 - 5 years	50	0
Loans maturing within 5 - 10 years	50	0
Loans maturing in over 10 years	100	75

The £40m HRA loans represent 75% of loans maturing in over 10 years. The Council holds investments from Portchester Crematorium which is treated as a temporary loan and £10 million short-term loans. These represent 25% of loans maturing within 1 year.

8) Housing Revenue Account (HRA) Ratios

ON TRACK

Due to the HRA Reforms in 2012, the Council moved from a subsidy system to self-financing and was required to take on £49.3 million of debt. The table below shows additional local indicators relating to the HRA in respect of this debt.

	Estimate	End of Year Forecast
HRA debt £'000	49,268	49,268
HRA revenues £'000	12,983	13,379
Number of HRA dwellings	2,422	2,422
Ratio of debt to revenues	3.79	3.79
Debt per dwelling £	£20,340	£20,340
Debt repayment fund £'000	£6,800	£6,840

INVESTMENT INDICATORS

9) Commercial Investments - Proportionality

ON TRACK

The Council is dependent on profit generating investment activity to achieve a balanced revenue budget. The table below shows the extent to which the expenditure planned to meet the service delivery objectives is dependent on achieving the expected net profit from investments over the lifecycle of the Medium-Term Financial Strategy.

£'000	2022/23 Budget	Actual to 30 Sept
Gross service expenditure	45,281	25,677
Investment income	4,308	2,810
Proportion	9.5%	10.9%

10) Total Risk Exposure

ON TRACK

This indicator shows the Council's total exposure to potential investment losses.

Total Investment Exposure	2022/23 Forecast £'000	Actual to 30 Sept £'000
Treasury Management Investments	15,000	27,379
Commercial Investments	61,525	68,336
Total	76,525	95,715

11) How Investments are Funded

ON TRACK

Government guidance is that these indicators should include how investments are funded. Since the Council does not normally associate particular assets with particular liabilities, this guidance is difficult to comply with. However, the following investments could be described as being funded by borrowing. The remainder of the Council's investments are funded by usable reserves and income received in advance of expenditure.

Investments Funded by Borrowing	2022/23 Forecast £'000	Actual to 30 Sept £'000
Treasury Management Investments	0	0
Commercial Investments	29,479	29,479
Total	29,479	29,479

12) Rate of Return Received

ON TRACK

This indicator shows the investment income received less the associated costs, including the cost of borrowing where appropriate, as a proportion of the sum initially invested.

Investments Net Rate of Return	2022/23 Estimate	Actual to 30 Sept
Treasury Management Investments	2.7%	1.3%
Commercial Investments	5.4%	3.2%
Total	4.7%	2.8%