FAREHAM
BOROUGH COUNCIL

Report to the Executive for Decision
07 November 2022

Portfolio:	Policy and Resources
Subject:	**Treasury Management and Capital Monitoring 2022/23**
Report of:	Deputy Chief Executive Officer
Corporate Priorities:	A dynamic, prudent and progressive Council

Purpose:
This report summarises the Council's borrowing and investment activity and capital expenditure up to 30 September 2022 and provides details of the Council's money market transactions. It also provides information on the performance against the Treasury and Prudential Indicators.

Executive summary:
During the first half of the year the Council operated within the Treasury and Prudential Indicators.

The overall treasury position is set out in the following table:-

	31 March 2022 Actual £'000	30 Sept 2022 Actual £'000
Total borrowing	53,199	53,336
Total investments	(22,189)	(27,379)
Net borrowing	**31,010**	**25,957**

The Council's net interest budget for 2022/23 is £678,800. With the Bank Rate expected to reach 5% by the end of the year, the budget is likely to be exceeded and will be revised during the revised budget setting period.

A summary of the capital programme expenditure against budgets in the current year, is set out in the following table:-

Capital Programme	Revised Budget 2022/23 £	Budget to 30 Sep 22 £	Actual to 30 Sep 22 £	Variation £
General Fund	16,213,400	1,563,200	1,299,029	-264,171
HRA	9,460,300	3,148,200	3,516,801	368,601
Total	**25,673,700**	**4,711,400**	**4,815,830**	**104,430**

Recommendation:
It is recommended that the Executive notes the Treasury Management and Capital Monitoring Report for 2022/23.

Reason:
To inform the Executive of the Council's borrowing, investment and capital programme activity up to 30 September 2022.

Cost of proposals:
Not applicable.

Appendices:	**A:** Economic Commentary and Outlook by Arlingclose **B:** Treasury and Prudential Indicators 2022/23 half yearly performance
Background papers:	None
Reference papers:	Treasury Management Strategy and Prudential Indicators 2022-23, Council, 25 February 2022 Finance Strategy, Capital Programme, Revenue Budget and Council Tax 2021/22, Executive, 7 February 2022 Housing Revenue Account 2022/23, Executive, 7 February 2021 Capital and Treasury Management Outturn 2021/22, Executive, 5 September 2022 Prudential Code for Capital Finance in Local Authorities (2021) Treasury Management in the Public Services Code of Practice (2021)

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BOROUGH COUNCIL

Executive Briefing Paper

Date:	07 November 2022
Subject:	Treasury Management & Capital Monitoring 2022/23
Briefing by:	Deputy Chief Executive Officer
Portfolio:	Policy and Resources

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 A.

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%.

INVESTMENT ACTIVITY

14. 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.

15. 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.

16. 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.

17. £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.

18. These funds have no defined maturity date but are available for withdrawal after a notice period but it is intended to hold onto the funds longer term. 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.

19. 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**	

COMMERCIAL PROPERTIES (NON-TREASURY INVESTMENTS)

20. 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.

21. 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**

22. 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.

23. 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**

24. The overall investment property portfolio has increased in value by £8 million mainly due a recovery in the investment market following COVID 19.

25. 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

26. Since the start of the financial year, there have been four Bank Rate rises with the latest rate being 2.25% since 22 September. Our treasury advisor, Arlingclose, expects Bank Rate to rise further during 2022/23 to reach 5% by the end of the year.

27. 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

28. 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.

29. Performance for the first half of the year is shown in Appendix B. During the financial year to date the Council has operated within the treasury limits and prudential indicators.

CAPITAL PROGRAMME

30. On 7 February 2022, the Executive approved the 2021/22 capital programme of £19.9 million for the General Fund and Housing Revenue Account (HRA).

31. Details of actual capital expenditure in 2021/22 were reported to the September Executive and a total carry forward of £1.98 million was added to the capital programme bringing the total to £21.9 million for 2022/23.

32. Since the capital programme was approved earlier in the year, a number of new schemes or amendments to scheme budgets have been added, giving a revised total of £25.7 million:-

- Revised Daedalus capital schemes - £955,400
- Revised Fareham Live - £3,374,700 additional budget
- Revised Osborn Road Multi-Storey Car Park - £1,770,000 reduction in budget in 2022/23
- 166 Southampton Road Repairs - £1,193,500
- Salterns Recreation Ground Interim Sea Defence Works - £78,000

33. The following table sets out the updated capital programme for 2022/23 and has been used as the basis for monitoring progress to 30 September 2022:-

	Approved Programme £	**2021/22 Slippage £**	**New/ Amended Schemes £**	**Total £**
Health and Public Protection	0	9,400	0	9,400
Streetscene	55,000	-16,900	0	38,100
Leisure and Community	2,557,600	-168,300	3,374,700	5,764,000
Housing	500,000	145,800	0	645,800
Planning and Development	70,000	82,500	78,000	230,500
Policy and Resources	8,778,200	368,500	378,900	9,525,600
Total General Fund	**11,960,800**	**421,000**	**3,831,600**	**16,213,400**
Housing Revenue Account	7,898,000	1,562,300	0	9,460,300
Updated 2022/23 Capital Programme	**19,858,800**	**1,983,300**	**3,831,600**	**25,673,700**

MAJOR CAPITAL SCHEMES

34. The Council has a number of major capital schemes where budgeted expenditure for 2022/23 is in excess of £500,000. These schemes, with forecast budget to 30 September 2022, are detailed in the following table:-

Capital Scheme	**Budget 2022/23**	**Budget to 30 Sep 22**	**Actual to 30 Sep 22**	**Variation**

	£	£	£	£
Fareham Live	5,310,200	700,000	642,790	-57,210
HRA Improvements to Existing Stock	2,716,400	1,338,200	1,743,422	405,222
HRA Station Road New Build	1,808,000	800,000	745,036	-54,964
HRA Sea Lane and Stubbington Lane	1,600,500	600,000	548,350	-51,650
Solent Airport AGL/PBN	1,300,000	10,000	6,875	-3,125
166 Southampton Road Repairs	1,193,500	10,000	1,495	-8,505
HRA Stock Repurchases	1,000,000	100,000	103,000	3,000
Osborn Road Multi-Storey Car Park	980,000	0	0	0
HRA Coldeast Scout Hut New Build	740,600	10,000	4,043	-5,957
Civic Offices Improvements	680,500	10,000	9,959	-41
HRA Queens Road New Build	538,500	200,000	160,450	-39,550

35. Progress updates on the major schemes are detailed below:-

(a) Construction at **Fareham Live** began in August 2022. Currently the contractor is demolishing the Octagon Lounge and deconstructing the areas around the auditorium and the northern elevation. The remodelled venue will open in Spring 2024.

(b) Expenditure for **HRA Improvements to Existing Stock** is overspent against the budget for the first 6 months. The Forward Plan for the year has been reviewed to take account of priorities and anticipated cost increases in all areas and the capital improvements budget will be revised to reflect this.

(c) There is good progress on the **Station Road New Build** scheme. The roof is nearly finished, and internal works are progressing. The scheme should complete in March 2023.

(d) Works at **Stubbington Lane New Build** are going well and due to complete on time in March 2023. Access and drainage design at **Sea Lane** are now complete and applying for the S.278 from Hampshire Highways and various consents from Southern Water are being pursued.

(e) Work on the detailed design for the **Solent Airport Aeronautical Ground Lighting and Performance-based Navigation System** is progressing, with the submission of planning application imminent. On conclusion of the design process, tenders will be requested December or early in 2023.

(f) Repairs at **166 Southampton Road** are pending planning consent with the proposed tenant B&M. Some highway issues have been raised by Hampshire County Council and are being addressed.

(g) There has been one **HRA Stock Repurchase** in the first half of the year to be funded from capital receipts. The focus for spending the 1-4-1 capital receipts will be towards new builds as there is now less time pressure to spend the receipts which has increased from 3 years to 5 years.

(h) Following a number of design/brief changes for the **Osborn Road Multi-Storey Car Park,** a design for a surface car park is being pursued following demolition of the existing structure. Once the design is accepted, planning permission will be sought in the new year.

(i) The **Coldeast Scout Hut New Build** scheme will be called Ophelia Court. There was a delay going to tender due to gaining the necessary permissions to trench the road for the sewer connection. Tenders are due back in November with start on site expected in Spring 2023.

(j) Works for the **Civic Offices Improvement Programme** in 2022/23 includes replacement fire doors, ground floor refurbishment and the upgrade of LED lighting on three floors.

(k) **Queens Road New Build**. The roof is battened and tiling underway. There are currently no issues and should complete on time early 2023.

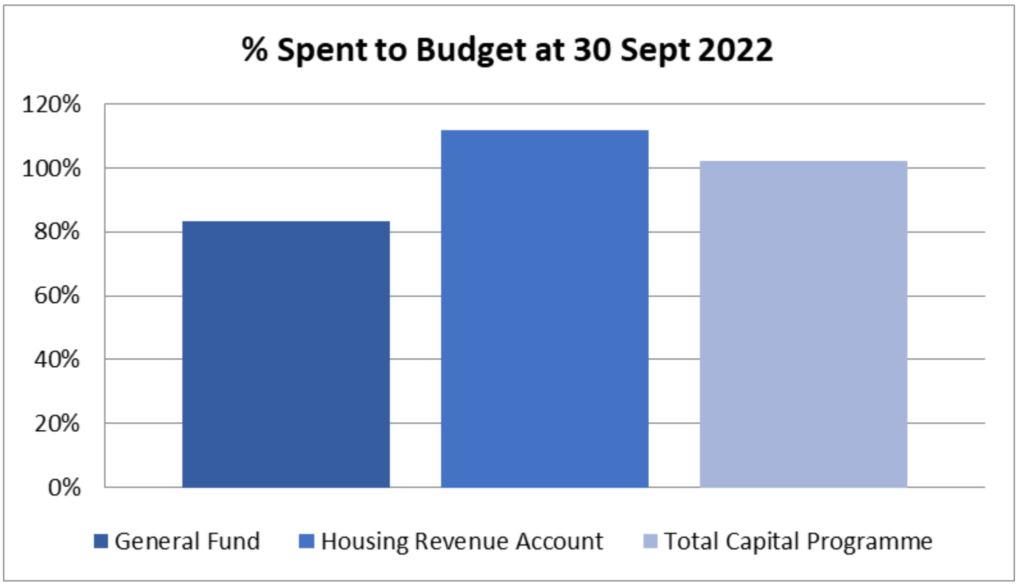
CAPITAL MONITORING

36. The following table provides summary information for the period to 30 September 2022, for all the schemes within each portfolio.

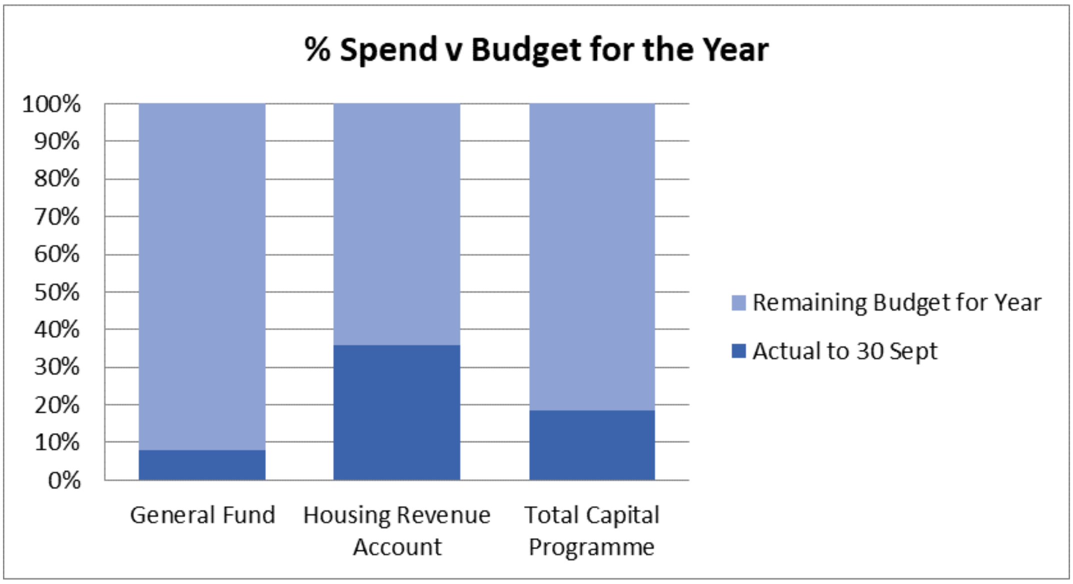
	Budget 2022/23	**Budget to 30 Sep 22**	**Actual to 30 Sep 22**	**Variation**
	£	**£**	**£**	**£**
Health and Public Protection	**9,400**	**0**	**0**	**0**
Streetscene	**38,100**	**0**	**0**	**0**
Leisure and Community	**5,764,000**	**750,000**	**660,290**	**-89,710**
- Buildings	5,615,400	700,000	642,790	-57,210
- Play and Parks	132,300	50,000	17,500	-32,500
- Other Community Schemes	16,300	0	0	0
Housing	**645,800**	**322,900**	**329,492**	**6,592**
Planning and Development	**230,500**	**0**	**0**	**0**
- Car Park Schemes	132,500	0	0	0
- Coastal Repairs	98,000	0	0	0
Policy and Resources	**9,525,600**	**490,300**	**309,247**	**-181,053**
- Daedalus	5,909,200	100,000	42,899	-57,101
- 166 Southampton Road Repairs	1,193,500	10,000	1,495	-8,505
- Osborn Road Multi-Storey Car Park	932,100	0	0	0
- Civic Offices Improvements	680,500	10,000	9,959	-41
- Vehicles and Plant	469,700	200,000	76,018	-123,982
- ICT	340,600	170,300	178,877	8,577
Total General Fund	**16,213,400**	**1,563,200**	**1,299,029**	**-264,171**
Housing Revenue Account				
- New Build	5,743,900	1,710,000	1,670,379	-39,621
- Improvements to Existing Stock	2,716,400	1,338,200	1,743,422	405,222
- Stock Repurchases	1,000,000	100,000	103,000	3,000
Total Housing Revenue Account	**9,460,300**	**3,148,200**	**3,516,801**	**368,601**
Total Capital Programme	**25,673,700**	**4,711,400**	**4,815,830**	**104,430**

37. The charts below show the actual expenditure to 30 September 2022 as a percentage of the programme for the equivalent period and for the whole year.

38. 102% of the capital programme has been spent compared to the profiled budget for the first half of the year.



39. 19% has been spent compared to the <u>total budget</u> for the year. The budgets will be reviewed again and re-phased where applicable as part of the forthcoming budget setting process.



RISK ASSESSMENT

40. In the current economic climate, there are continued risks that financial institutions holding Council investments could default and be unable to fulfil their commitments to repay the sums invested with them.

41. To help mitigate this risk, the Council maintains a list of approved institutions based on a grading system operated by the Council's treasury management advisors. Maximum limits are also set for investments with individual institutions.

42. With expected Bank Rate rises to 5% by the end of the year, there is a risk that the cost of borrowing for capital schemes could make future schemes unviable.

Enquiries:

For further information on this report please contact Caroline Hancock (Ext 4589).

APPENDIX A

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 5% 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.

APPENDIX B

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.

	Actual to

	Estimate £'000	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**

ON TRACK

11) 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.

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**

ON TRACK

12) 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.

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%**