CHESHIRE FIRE AUTHORITY

MEETING OF: **CHESHIRE FIRE AUTHORITY**
DATE: **28 JUNE 2023**
REPORT OF: **HEAD OF FINANCE**
AUTHOR: **WENDY BEBBINGTON**

SUBJECT: TREASURY MANAGEMENT ANNUAL REPORT 2022-23

Purpose of Report

1. To present a review of the Authority's treasury management activities undertaken during 2022-23.

Recommended: That

[1] the report on treasury management activity for 2022-23 be noted; and

[2] the performance against the Prudential and Treasury indicators be noted.

Background

2. The Chartered Institute of Public Finance and Accountancy (CIPFA) define treasury management as 'The management of the organisation's borrowing, investments and cash flows, including 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.'

3. The associated Code of Practice for Treasury Management recommends that those charged with governance are updated on treasury management activities regularly by way of a strategy at the start of the year, a mid-year review and an outturn report. In addition to these three major reports, from 2023-24, additional quarterly reporting (end of June/end of December) is also required. This new reporting requirement will be fulfilled by the inclusion of updated and forecast Treasury/Prudential Indicators within the main First Quarter and Third Quarter financial review reports considered by Performance and Overview Committee.

4. The regulatory environment places responsibility on Members for the review and scrutiny of treasury management policy and activities. This report provides Members with details of the treasury management activities undertaken in 2022/23. It also highlights compliance with the Authority's policies previously approved by Members.

5. This report includes details of:

   a. the Authority's loans portfolio position at 31 March 2023;
   b. the Authority's investment portfolio position at 31 March 2023;
   c. a summary of performance for the year 2022/23;
   d. the Authority’s performance in 2022/23 set against the key Prudential and Treasury Indicators

6. Members should be aware that all of the 2022/23 figures in this report remain subject to audit.

The Economy and Interest Rates

7. The Coronavirus Pandemic resulted in huge economic damage to the UK economy and to economies around the world and investment returns had remained close to zero for much of 2020/21 and 2021/22. The expectation for interest rates within the Treasury Management Strategy for 2022/23 was that the Bank Rate would begin a slow rise to normality during the year but would end the year at 0.75%. However, investment returns have picked up sharply throughout the course of 2022/23 as central banks, including the Bank of England, realised that inflationary pressures were not transitory, and that tighter monetary policy was called for. Starting April 2022 at 0.75%, the Bank Rate moved up in stepped increases of either 0.25% or 0.5%, reaching 4.25% by the end of the financial year, with the potential for a further one, or two increases in 2023/24.

8. While the Authority has maintained a cautious approach to investing, it is also fully appreciative of changes to regulatory requirements for financial institutions in terms of additional capital and liquidity that have been introduced over recent years. These requirements have provided a far stronger baseline for financial institutions, with annual stress tests by regulators evidencing how institutions are now far more able to cope with extreme stressed market and economic conditions.

9. Looking at Public Works Loan Board (PWLB) maturity loan borrowing rates, the 50 year rate started 2022/23 at 2.42% on 1/4/2022 and finished the year on 31/3/2023 at 4.41%, after hitting a high of 5.51% on 28/9/2022. Table 1 below provides a summary of PWLB rates comparing the high, low and average rates throughout the year.

Table 1

	1 Year	5 Year	10 Year	25 Year	50 Year
Low	1.95%	2.18%	2.36%	2.52%	2.25%
Date	01/04/2022	13/05/2022	04/04/2022	04/04/2022	04/04/2022
High	5.11%	5.44%	5.45%	5.88%	5.51%
Date	28/09/2022	28/09/2022	12/10/2022	12/10/2022	28/09/2022
Average	3.57%	3.62%	3.76%	4.07%	3.74%
Spread	3.16%	3.26%	3.09%	3.36%	3.26%

Outlook for 2023/24

10. In 2023/24, recent data suggests that the global economy had a better start to the year than previously feared. The plunge in wholesale gas prices since the end of last year has decreased the size of the drag on real incomes. As a result, markets expect falls in real consumer spending of about 1.0%, real business investment of around 12% and real residential investment in the region of 17%, which will result in overall GDP declining by around 1.0% over the first three quarters of this year.

11. CPI inflation has already fallen from its peak of 11.1% in October 2022 to 8.7% in April 2023 and will drop further this year. A lot of that will be due to falls in utility and fuel prices. Domestic inflationary pressures are also expected to ease as a higher unemployment rate leads to lower wage growth and the recession, forcing firms to absorb more of the rises in costs in their margins.

12. If the UK economy proves to be more resilient than most expect and/or inflation proves to be stickier, bank rates may rise above 5% and/or stay high well into 2024. However, the central forecast is that a recession will weaken domestic inflation pressures enough to allow the Bank to cut interest rates in the first half of 2024.

13. There is likely to be a fall in PWLB rates across the whole range of durations over the next one to two years as the Bank Rate first rises to dampen inflationary pressures and a tight labour market, and is then cut as the economy slows, unemployment rises, and inflation (on the Consumer Price Index measure) moves closer to the Bank of England’s 2% target.

Portfolio Position at 31 March 2023

14. A summary of the Authority’s long-term borrowing and investments at 31 March 2023 is shown in Table 2, including the equivalent treasury portfolio position at 31 March 2022 for reference.

Table 2 – Portfolio Position		
	31 March 2022 £000	31 March 2023 £000
Long Term Borrowing	12,012	12,012
Treasury Investments	(18,646)	(12,940)
Net Borrowing / (Investments)	(6,634)	(928)

Note: All investments held relate to Treasury Management activities. The Authority has not engaged in any commercial investments and has no non-treasury investments.

15. Long-term borrowing as at 31 March 2023 is made up entirely of maturity loans from the Public Works Loans Board (PWLB). This includes borrowing of £11m to finance the Training Centre project, secured from PWLB at favourably low fixed rates in March 2021 (£4m at 1.99%), July 2021 (£4m at 1.65%) and November 2021 (£3m at 1.63%). No new borrowing was entered into during 2022/23.

16. Investment balances (including cash on deposit in Money Market Funds) have reduced during 2022/23. This is due to expenditure on major estates projects during the year.

Treasury Management Performance 2022/23

Investments

17. Over recent years, it has been impossible to generate significant levels of investment income due to the 0.1% Bank Rate, leading to available short-term investment rates with suitable counterparties (financial institutions that investments are placed with) being barely above zero. However the increases to Bank Rate during 2022/23 and proactive cashflow management, have enabled the Authority to secure significantly increased short to medium term rates of return over recent months. Investment income in 2022/23 is £417k, increased from the £41k generated in 2021/22.

18. The Authority has continued with a cautious approach to its choice of counterparties. As at 31 March 2023, the Authority's investments are with UK Debt Management Office, Santander, Aberdeen Standard Liquidity Money Market Fund and in its National Westminster Bank Liquidity account, which the Authority continues to use regularly to manage day to day cashflows. An investment was also held with Goldman Sachs earlier in the year. The current investment counterparty criteria selection approved in the Treasury Management Strategy is meeting the requirement of the treasury management function.

19. There have been no instances of non-compliance with approved Annual Investment Strategy limits during the year.

Borrowing

20. The amount of borrowing as at 31 March 2023 is £12.012m. During 2022/23 interest rates have been monitored and no debt rescheduling took place during the year as the average 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

21. As previously reported to Members and in line with the currently approved Treasury Management Strategy, £11m of this current borrowing relates to the Training Centre.

22. The approved Treasury Management Strategy included provision for £7.5m of new external borrowing during 2022/23 mainly in respect of major estates projects at Crewe and Wilmslow. However, in view of the sharp rise in interest rates and current market volatility, together with reduced cashflow pressure from re-profiling of the Fire Station Modernisation programme expenditure into 2023/24 and 2024/25, the timing of this new borrowing is currently being deferred. Market rates and forecasts will continue to be kept under close review in order to secure the borrowing at the optimum point.

23. The Authority currently remains in an under-borrowed position, which means that decisions have been made to internally finance expenditure as opposed to entering into new external borrowing. As a result of deferring this planned 2022/23 new external borrowing, the position at 31 March 2023 is now forecast to be around £9.7m internally borrowed. This is consistent with the current strategy of increasing internal borrowing over the period of major estates projects delivery in order to minimise new long term external borrowing over this period. It will be achieved through careful cashflow management.

24. At this point increasing internal borrowing as detailed above, supported by short periods of temporary external borrowing if required, is considered to be manageable and a sensible target position in view of the current high cost of borrowing and forecasts that this will begin to reduce as the economy stabilises over the next two, to three years. The position was reviewed as part of the 2023/24 Treasury Management Strategy and will continue to be monitored closely.

25. The maturity structure for borrowing can be seen in Table 3. This indicator is designed to be a control over an authority having large concentrations of fixed rate debt which need to be replaced at times of uncertainty over interest rates. The limits set represent sensible boundaries and are intended to draw attention to potential issues before they arise. There are currently no potential issues.

Table 3 - Maturity Structure of Borrowing – 31/03/2023

	Upper Limit %	**Lower Limit %**	**Actual %**	**Amount £000**
Under 12 months	15	0	3	426
12 months and within 24 months	15	0	4	467
24 months and within 5 years	25	0	1	119
5 years and 10 years	25	0	0	0
10 years and above	100	50	92	11,000
Total			100	12,012

Prudential and Treasury Indicators

26. The Authority must approve Prudential and Treasury Indicators annually, to reflect the impact of the Capital Programme on the Authority's financial position. Table 4 below shows performance in 2022/23 against the indicators, which were approved by the Authority in February 2022.

Table 4: Prudential and Treasury Indicators			
Prudential Indicators	2022/23 Indicator £000	2022/23 Outturn £000	Comment
Capital expenditure Capital financing requirement Annual change in capital financing requirement	16,177 25,424 9,298	7,769 21,735 5,609	Pause / re-profiling of Fire Station Modernisation programme, later than anticipated start to Crewe new build and £0.5m underspend re: Wilmslow project.
Gross borrowing requirement: (Under) / Over borrowing	(5,912)	(9,723)	Deferral of planned £7.5m borrowing in 2022/23 offset by lower borrowing requirement due to lower spend as above.
Ratio of financing costs to net revenue stream	2.32%	2.23%	Deferral of new borrowing.
Treasury Indicators	2022/23 Indicator £000	2022/23 Outturn £000	
Authorised limit for external debt Operational boundary for external debt	24,212 22,212	24,212 22,212	Set 9/2/22, no change during 2022/23.
Actual external debt - Borrowing - Other long term liabilities Total	 19,512 0 19,512	 12,012 0 12,012	Planned £7.5m new borrowing deferred due to current high interest rates and improved cash balances resulting from re-profiling of Fire Station Modernisation programme into 2023/24 and 2024/25.
Upper limit of fixed interest rate exposure	100%	100%	
Upper limit of variable interest rate exposure	25%	Nil	No variable rate loans held or planned
Upper limit for principal sums invested for over 364 days	£nil	£nil	No longer term investments held or planned.

27. The above table shows that the Authority remained within both the authorised limit and operational boundary for external debt. These are limits on the amount of external debt permitted and include both loans and financial leases.

28. Capital expenditure in 2022/23 was lower than originally anticipated due to some re-profiling of expenditure relating to both the Fire Station Modernisation Programme and the Crewe Fire Station replacement project. In addition the project to purchase additional service housing in Wilmslow was completed with a final underspend of £0.5m.

Conclusion

29. Increases to the Bank Rate during 2022/23 and proactive cashflow management, have enabled the Authority to secure significantly increased investment returns over recent months which will continue into 2023/24. Opportunities for seeking improved returns will continue to be pursued within the approved confines of the Annual Investment Strategy.

30. Borrowing rates remain high and new borrowing is required to finance the major estates projects at Crewe and Wilmslow. In view of the recent sharp rise in interest rates and current market volatility, together with reduced cashflow pressure from re-profiling of the Fire Station Modernisation programme expenditure into 2023/24 and 2024/25, the timing of required new borrowing is currently being deferred. This will be secured at the optimum point taking into account available cash balances along with prevailing and forecast market rates.

Financial Implications

31. The report is in its nature financial and the implications are covered in the body of the report.

Legal Implications

32. All transactions between the Authority and counterparties are governed by the agreements between the two parties, and take into account advice from our Treasury Management partner Link Asset Services.

Equality and Diversity Implications

33. There are none.

Environmental Implications

34. There are none.

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BACKGROUND PAPERS: NONE