Appendix

Mid-Year Monitoring Report 2022/23
Treasury Management and Prudential Indicators: 1 April 2022 to 31 August 2022

1. Introduction

1.1 The Council’s treasury management activities are regulated by a variety of professional codes and statutes and guidance:

- The Local Government in Scotland Act 2003 (the Act), which provides the powers to borrow and invest as well as providing controls and limits on this activity;
- The Act permits the Scottish Ministers to set limits either on the Council or nationally on all local authorities restricting the amount of borrowing which may be undertaken (although no restrictions have been made as yet during 2022/23).
- Statutory Instrument (SSI) 29 2004, requires the Council to undertake any borrowing activity with regard to the CIPFA Prudential Code for Capital Finance in Local Authorities, and therefore to operate the overall treasury function with regard to the CIPFA Code of Practice for Treasury Management in the Public Services; and the treasury activity with regard to the CIPFA Code of Practice for Treasury Management in Local Authorities.
- Statutory Instrument (SSI) 123 2016, set out statutory arrangements for local authority borrowing and lending and the requirement to maintain a loans fund and replace the statutory arrangements set out in Schedule 3 of the Local Government (Scotland) Act 1975 (Schedule 3).

1.2 The regulatory framework of treasury management requires that the Council receive a mid-year treasury review, in addition to the forward looking annual treasury strategy and backward looking annual treasury report. This report meets that requirement and also incorporates the needs of the Prudential Code to ensure adequate monitoring of the capital expenditure plans and the Council’s prudential indicators. The Treasury Strategy and Prudential Indicators were previously reported to Council on 23 March 2022. The current position is shown (where appropriate) and revisions to the 2022/23 estimate are provided where required.

1.3 In December 2017, the Chartered Institute of Public Finance and Accountancy, (CIPFA), issued revised Prudential and Treasury Management Codes. As from 2019/20, all local authorities require to prepare a Capital Strategy which provides the following:

- a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services;
- an overview of how the associated risk is managed; and
- the implications for future financial sustainability

The Council’s Capital Strategy was reported to and agreed by Council on 23 March 2022.

1.4 This report sets out:

- Key changes to the Council's capital activity (the prudential indicators);
- An economic update for the first part of the 2022/23 financial year;
- The actual and proposed treasury management activity (borrowing and investment); and
- The risk approach to treasury management (the treasury management indicators).

2. Key Prudential Indicators

2.1 This part of the report is structured to update:

- The Council's capital expenditure plans and how these plans are being financed;
- The impact of the changes in the capital expenditure plans on the PIs and the underlying need to borrow;
- Compliance with the limits in place for borrowing activity; and
- Policy on the statutory repayment of loans fund advances

2.2 **Capital Expenditure** – Table A shows the current position and revised estimates for capital expenditure for 2022/23 only.

Table A:

£000	**2022/23 Original Estimate**	**Current Position**	**2022/23 Projected Outturn***
General Services	51,506	3,857	49,856
HRA	47,233	7,416	63,322
Capital Expenditure	**98,739**	**11,273**	**113,178**
Financed by:			
Capital receipts	0	0	0
Capital grants	34,352	3,850	36,266
Revenue / other	9,221	0	288
Net financing need for the year	**55,166**	**7,423**	**76,624**

* it should be noted that the Projected Outturn figures include additional slippage from 2021/22 that were not known at the time of the Original Estimate

2.2.1 The movement in the level of anticipated capital expenditure is mainly due to the inclusion of additional slippage following the year end; a reduction in anticipated capital receipts; an increase in spend related to external funding offset by slippage levels identified to date. The anticipated spends and resources are regularly reported to Members through budgetary control reports.

2.3 **Impact of changes in Capital Expenditure Plans** – Table B shows the CFR, which is the underlying external need to borrow for a capital purpose while Table C shows the expected debt position over the period.

Table B:

£000	2022/23 Original Estimate	2022/23 Projected Outturn
Opening CFR (1 April 2022)	**698,886**	**680,113**
New Borrowing	45,621	67,172
LTL repayment in year	(3,372)	(3,370)
Closing CFR (31 Match 2023)	**741,135**	**743,915**
movement in CFR	**42,249**	**63,802**
Net financing need for the year (Table A)	55,166	76,624
Loan repayments in year - excluding LTL (PPP)	(9,545)	(9,452)
New Borrowing - Movement in CFR (from previous year)	**45,621**	**67,172**

Table C:

£000	2022/23 Original Estimate	Current Position	2022/23 Projected Outturn
External Debt			
Estimated/Actual Debt at 1 April 2022	604,941	562,007	574,570
Maturing Debt	(268,722)	(127,000)	(262,677)
Movement in Borrowing			
New Borrowing - Maturing Debt	268,722	127,000	262,677
Borrowing adjustment in relation to over borrowing at year end	0	0	0
New Borrowing – CFR (Table B)	45,621	0	67,172
Debt at 31 March (1)	**650,562**	**562,007**	**641,742**
Long Term Liabilities (LTL) at 1 April	92,614	92,485	92,485
LTL repayment in year (Table B)	(3,372)	(1,404)	(3,370)
LTL at 31 March (2)	**89,242**	**91,081**	**89,115**

Actual Debt at 31 March (1) + (2)	**739,804**	**653,088**	**720,857**
CFR from Table B	**741,135**	**n/a**	**743,915**
Under/(Over) Borrowing	**1,331**	**n/a**	**13,058**

2.3.1 The external debt figures included within Table C now includes both short term and long term debt. This is due to the current strategy of using short term borrowing to fund long term capital investment enabling the Council to take advantage of lower interest rates. The reduction in the estimated external debt for 2022/23 is due to a reduction in the net capital financing need for the year.

2.3.2 The CFR is calculated on a year-end position based on the Council's balance sheet and therefore the current position is not shown. The CFR has reduced from the original estimate due to the forecast level of capital expenditure in 2022/23 being less than budgeted. The Chief Officer - Resources can report that the Council is currently on target to meet the 2022/23 revised estimates for both indicators.

2.3.3 Table C highlights that the borrowing of the Council is forecasting a minimal under-borrowed position against the CFR at 31 March 2023.

2.4 **Compliance with the limits in place for borrowing activity** – A key control over the treasury activity is a prudential indicator to ensure that over the medium term, gross borrowing will only be for a capital purpose.

Gross borrowing should not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional CFR for 2021/22 and next two financial years. This allows some flexibility for limited early borrowing for future years.

The Council has approved a policy for borrowing in advance of need which will be adhered to if this proves prudent. The revised indicator is detailed in Table D and is illustrated by comparing the estimated gross debt as at 31 March 2022 with the CFR as at 31 March 2025. The Chief Officer - Resources reports that no difficulties are envisaged for the current year in complying with this prudential indicator.

Table D:

£000	**2022/23 Original Estimate**	**2022/23 Projected Outturn**
CFR at 31 March 2022		
Estimate/Actual (From Table B above)	**698,886**	**680,113**
Estimated movement in CFR		
2022/23 (From Table B above)	42,249	63,802
2023/24	67,898	82,507
2024/25	37,805	37,805
Anticipated CFR at 31 March 2025	**846,838**	**864,227**
Gross Debt at 31 March 2023 Table C above)	**739,804**	**730,857**

2.4.1 The Operational Boundary is detailed in Table E below and is the limit beyond which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt.

Table E:

£000	**2022/23 Original Estimate**	**Current Position**	**2022/23 Projected Outturn**
External Debt	813,785	653,088	803,943

2.4.2 A further prudential indicator controls the overall level of borrowing. This is the Authorised Limit which is detailed in Table F and represents the limit beyond which borrowing is prohibited, and needs to be set and revised by Members. It reflects the level of borrowing which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. It is the expected maximum borrowing need with some headroom for unexpected movements. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003.

Table F:

£000	2022/23 Original Estimate	Current Position	2022/23 Projected Outturn
External Debt	887,776	653,088	877,028

3. Economic Outlook

3.1 UK

- The Monetary Policy Commission (MPC) has increased Bank Rate to 2.25% from 1.75%. The UK now has a new Prime Minister, a new Chancellor and new economic policies that seek to grow the UK economy faster than at any time since the 1980s. The Government intends to reduce the basic rate of income tax by 1p in the £; scrap the 45p in the £ higher income tax rate; reverse the 1.25% NI Health & Social Levy from November; not increase Corporation Tax from 19% to 25% as previously anticipated; reduce Stamp Duty on house purchases with an emphasis on helping first time buyers; scrap caps on bankers' bonuses; support businesses and households with caps on the unit costs of gas and electricity for 6 and 24 months respectively. There is every chance that the on-going steep rises in gas, electricity and food inflation, when added to significant increases in fixed rate mortgages and rents, may see the UK head into recession despite the Government's best intention to prevent this occurrence.

3.2 Scotland

- The Scottish Government will see its overall funding levels increase through and beyond the Spending Review period. However, inflation will erode this growth. In real terms funding will remain slightly below that of 2022/23 for most of the Spending Review period, increasing only modestly in its last year. Income tax is still expected to reduce the size of the Budget, but only in the first year of the Spending Review. From 2024 -25 the UK Government intends to reduce the basic rate of income tax to 19 per cent. The income tax BGA will reduce accordingly, thus supporting net Scottish income tax funding.

- With inflationary pressures intensifying further since December 2021, it is anticipated that annual CPI inflation will peak at 8.7 per cent in 2022 Q4. Rising global energy prices, exacerbated by the conflict in Ukraine, have driven large increases in the Ofgem energy price cap in April and October 2022. It is forecasted that real average earnings to decrease by 2.7 per cent in 2022/23. This is because nominal earnings are not expected to keep pace with rising inflation. Low income households are expected to be disproportionately affected.

- House prices will continue to rise but not as quickly as previously forecast. The rising cost of living and rising interest rates will put pressure on how much households can afford to spend on moving home.

- Security spending is expected to increase from £4.2 billion in 2022-23 to £6.8 billion in 2027-28. The Scottish Government plans to replace payments devolved but administered by DWP with Scottish payments by the end of 2025.

3.3 **International update**

- The US FOMC (Federal Open Market Committee) has increases of 300 basis points in the year to date and is expected to increase rates further before the end of the year. Similarly, the European Central Bank has also started to tighten monetary policy, albeit from an ultra-low starting point, as have all the major central banks apart from Japan. Arguably, though, it is US monetary policies that are having the greatest impact on global bond markets.

- What happens in Ukraine will also impact the global economy, but particularly in Europe. The search for alternative providers of energy, other than Russia, will take both time and effort. The weather will also play a large part in how high energy prices stay and for how long.

3.4 Based upon the above information, the Council's treasury advisor, Link Asset Services, has provided the following interest rate forecast. As at September 2022 (this is significantly different than 2 months previous due to the ongoing volatility of the market):

Table G:

Link Group Interest Rate View	27.09.22											
	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25
BANK RATE	4.00	5.00	5.00	5.00	4.50	4.00	3.75	3.25	3.00	2.75	2.75	2.50
3 month ave earnings	4.50	5.00	5.00	5.00	4.50	4.00	3.80	3.30	3.00	2.80	2.80	2.50
6 month ave earnings	4.70	5.20	5.10	5.00	4.60	4.10	3.90	3.40	3.10	3.00	2.90	2.60
12 month ave earnings	5.30	5.30	5.20	5.00	4.70	4.20	4.00	3.50	3.20	3.10	3.00	2.70
5 yr PWLB	5.00	4.90	4.70	4.50	4.20	3.90	3.70	3.50	3.40	3.30	3.20	3.20
10 yr PWLB	4.90	4.70	4.60	4.30	4.10	3.80	3.60	3.50	3.40	3.30	3.20	3.20
25 yr PWLB	5.10	4.90	4.80	4.50	4.30	4.10	3.90	3.70	3.60	3.60	3.50	3.40
50 yr PWLB	4.80	4.60	4.50	4.20	4.00	3.80	3.60	3.40	3.30	3.30	3.20	3.10

Source:Link Treasury Management Advisors

3.5 Downside risks to current forecasts for UK gilt yields and PWLB rates currently include:

- **Labour and supply shortages** prove more enduring and disruptive and will depress economic activity (accepting that in the near-term this is also an upside risk to inflation and, thus, rising gilt yields).

- **The Bank of England** acts too quickly, or too far, over the next two years to raise Bank Rate and causes UK economic growth, and increases in inflation, to be weaker than we currently anticipate.

- **UK / EU trade arrangements** – if there was a major impact on trade flows and financial services due to complications or lack of co-operation in sorting out significant remaining issues.

- **Geopolitical risks,** for example in Ukraine/Russia, China/Taiwan/US, Iran, North Korea and Middle Eastern countries, which could lead to increasing safe-haven flows.

3.6 Upside risks to current forecasts for UK gilt yields and PWLB rates are as

- The **Bank of England is too slow** in its pace and strength of increases in Bank Rate and, therefore, allows inflationary pressures to build up too strongly and for a longer period within the UK economy, which then necessitates an even more rapid series of increases in Bank Rate faster than we currently expect.

- **The Government** acts too quickly to cut taxes and/or increases expenditure in the light of the cost-of-living squeeze.

- **The pound weakens** because of the UK's growing borrowing requirement resulting in investors pricing in a risk premium for holding UK sovereign debt.

- Longer term **US treasury yields** continue to rise strongly and pull gilt yields up even higher than currently forecast.

4. Treasury Management Activity

4.1 This part of the report is structured to update:

- The Council's expected borrowing need and details of under/(over) borrowing;
- Debt rescheduling and new borrowing;
- Debt charges; and
- Investments

4.2 **The Expected Borrowing Need** – This was set out in Table C (above) and demonstrates that at 31 August 2022 the Council is currently projecting and under-borrowed position to reduce risks in investments held and the cost of carry on investments. It should be noted that due to current economic climate the borrowing rates are significantly different than this time last year, with long term borrowing rates for periods greater than 25 years currently between 4.56% and 5.03%, depending on length of term for borrowing (as at 29 September 2022). This introduces an element of interest rate risk, as longer term borrowing rates may rise further; however, this position is being carefully monitored.

4.3 **Debt rescheduling and new borrowing** – The Council has not undertaken any debt rescheduling during the part of 2022/23 (to 31 August 2022). In the year to date naturally maturing debt of £174.606m has been repaid which has been mainly funded by loans from other local authorities.

4.4 **Debt Charges** – The revised estimate for debt charges for both the General Fund and the HRA is shown in Table H.

Table H:

£000	2022/23 Original Estimate	Current Position	2022/23 Revised Estimate
Borrowing	21,903	9,287	22,288
Other Long Term Liabilities	9,982	4,178	10,027
Total	**31,886**	**13,465**	**32,315**

4.5 **Investments** – The objectives of the Council's investment strategy are to ensure the re-payment of the principal and interest of its investments on time with the level of investment return being a secondary objective. Following on from the economic background above, the current investment climate has one over-riding risk consideration which is the risk of default.

4.5.1 The Council held £24.525m of cash investments at 31 August 2022, and the constituent parts of the investment position are detailed in Table I:

Table I:

£000	Country	< 1 Year	1 – 2 Years	2 – 3 Years
Banks	UK	1,525	Nil	Nil
Money Market Fund	UK	23,000	Nil	Nil
Local Authorities	UK	0	Nil	Nil
Total	UK	24,525	Nil	Nil

4.5.2 Table J details the revised budget position for investment income. The original estimate has increased by £0.055m due to ongoing interest rates changes.

Table J:

£000	2022/23 Original Estimate	Current Position	2022/23 Revised Estimate
Investment Income	75	55	132

4.5.3 A regulatory development to address risk is the consideration and approval of benchmarks relating to investment security, liquidity and the level of return. Benchmarks are currently widely used to assess the level of return and investment performance, however the application of security and liquidity benchmarks are more subjective in nature.

- **Security** - The Council's maximum security risk benchmark for the current portfolio in relation to investment periods of up to one year (when compared to historic default tables) was set at 0.00% and the Chief Officer - Resources can report that there have been no defaults of principal sums invested in the year to date.

Creditworthiness - Significant levels of downgrades to Short- and Long-Term credit ratings have not materialised since the crisis in March 2020.

- **Liquidity** – The Chief Officer - Resources can report that liquidity arrangements were adequate during the year to date and that the liquidity facilities and benchmarks set by the Council as noted below were maintained:
    - Bank overdraft - £1.000m; and
    - Liquid short term deposits of at least £5.000m available on an overnight basis.

- **Return on Investments** – The Chief Officer - Resources can report that the investment return to date average 1.12%. Table K illustrates how this average return compares with the local benchmarks.

Table K:

Benchmark	Benchmark Return	Average Return
Compound 12 month SONIA*	1.04%	1.12%
Council's Instant Access Account	1.09%	1.12%

***** SONIA is Sterling Overnight Index Average and has replaced LIBOR & LIBID

5 Key Treasury Management Indicators

5.1 This part of the report is structured to update:

- Actual and estimates of the ratio of financing costs to net revenue stream;
- Upper limits on interest rate exposure:
- The maturity structure of borrowing; and
- Total principal sums invested.

5.2 **Actual and estimates of the ratio of financing costs to net revenue stream** – This indicator (as shown below in Table L) identifies the trend in the cost of capital against the net revenue stream.

Table L:

	2022/23 Original Estimate	2022/23 Revised Estimate
General Fund	7.77%	7.86%
HRA	27.08%	26.31%

5.3 **Upper Limits on Fixed and Variable Rate Exposure** – These indicators identify a maximum limit for fixed and variable interest rates based upon the debt position and were set at 100% and 50% respectively for 2022/23. The Chief Officer – Resources reports that the Council operates within these limits.

5.4 **Maturity Structures Of Borrowing** – These maximum limits are set to reduce the Council's exposure to large fixed rate loans (those instruments which carry a fixed interest rate for the duration of the instrument) which are due to naturally mature in any given period as detailed in Table M and show that the Council operates within limits set.

Table M:

Maturity Structure of Fixed Interest Rate Borrowing	2022/23 Original Limits	Current Position
Under 12 months	50%	46%
12 months to 2 years	50%	4%
2 years to 5 years	50%	3%
5 years to 10 years	50%	5%
10 years to 20 years	50%	4%
20 years to 30 years	50%	6%
30 years to 40 years	50%	5%
40 years to 50 years	100%	22%
50 years to 60 years	100%	5%
60 years to 70 years	100%	0%

5.5 **Total Principal Funds Invested** – These limits are set to reduce the need to temporarily borrow to cover any unexpected expenditure, and show limits to be placed on investments with final maturities beyond each year-end. The Council currently invests sums for periods greater than 365 days in Clydebank Property Company and hub West Scotland as detailed in Table N.

Table N:

	2022/23 Original Estimate	Current Position	2022/23 Revised Estimate
Principal sums invested > 365 days (maximum limit £7m)	£0.485m	£0.485m	£0.485m