

Appendix 1

DENBIGHSHIRE COUNTY COUNCIL

ANNUAL TREASURY MANAGEMENT REPORT 2023/24

Liz Thomas
Head of Finance and Audit

CONTENTS

Section	Title
1	Background
2	Economic Background
3	Borrowing Activity
4	Investment Activity
5	Compliance with Prudential Indicators
6	Money Laundering Update
	Annex A - PWLB borrowing rates and UK Money Market rates
	Annex B – Compliance with Prudential Indicators 2023/24
	Annex C – Glossary

1. Background

- 1.1 The Council's treasury management activity is underpinned by CIPFA's Code of Practice on Treasury Management ("the Code"), which requires local authorities to produce Prudential Indicators annually and a Treasury Management Strategy Statement on the likely financing and investment activity for the coming year. The Code also recommends that members are informed of treasury management activities at least four times a year. Reports are presented quarterly to the Governance and Audit Committee which is the committee with responsibility for the scrutiny of the Council's treasury policy, strategy and activity, as well as the annual report made to cabinet and the report to full Council for approval of the annual treasury strategy.
- 1.2 Treasury management is defined as "the management of the local authority's investments and 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."
- 1.3 The Council has borrowed and invested substantial sums of money and is therefore exposed to financial risks, including the loss of invested funds and the revenue effect of changing interest rates. This report covers treasury activity and the associated monitoring and control of risk.

2. Economic Background

- 2.1 UK inflation continued to decline from the 8.7% rate seen at the start of 2023/24. By the last quarter of 2023/24, headline consumer price inflation (CPI) had fallen to 3.4% in February but was still above the Bank of England's 2% target at the end of the period. The core measure of CPI, i.e. excluding food and energy, also slowed in February to 4.5% from 5.1% in January, a rate that had stubbornly persisted for three consecutive months.
- 2.2 The UK economy entered a technical recession in the second half of 2023, as growth rates of -0.1% and -0.3% respectively were recorded for Q3 and Q4. Over the 2023 calendar year GDP growth only expanded by 0.1% compared to 2022. Of the recent monthly data, the Office for National Statistics reported a rebound in activity with the economy expanding 0.2% in January 2024. While the economy may somewhat recover in Q1 2024, the data suggests that prior increases in interest rates and higher price levels are depressing growth, which will continue to bear down on inflation throughout 2024.
- 2.3 Labour market data provided a mixed message for policymakers. Employment and vacancies declined, and unemployment rose to 4.3% (3mth/year) in July 2023. The same month saw the highest annual growth

rate of 8.5% for total pay (i.e. including bonuses) and 7.8% for regular pay growth (i.e. excluding bonuses). Thereafter, unemployment began to decline, falling to 3.9% (3mth/year) in January and pay growth also edged lower to 5.6% for total pay and 6.1% for regular pay, but remained above the Bank of England's forecast.

- 2.4 Having begun the financial year at 4.25%, the Bank of England's Monetary Policy Committee (MPC) increased Bank Rate to 5.25% in August 2023 with a 3-way split in the Committee's voting as the UK economy appeared resilient in the face of the dual headwinds of higher inflation and interest rates. Bank Rate was maintained at 5.25% through to March 2024. The vote at the March Committee was 8-1 in favour of maintaining rates at this level, with the single dissenter preferring to cut rates immediately by 0.25%. Although financial markets shifted their interest rate expectations downwards with expectations of a cut in June, the MPC's focus remained on assessing how long interest rates would need to be restrictive in order to control inflation over the medium term.

3. **Borrowing Activity**

- 3.1 The Council borrows to fund capital expenditure, which is money spent on assets that will be used for more than one year.
- 3.2 The table below shows the level of the Council's borrowing from the Public Works Loan Board (PWLB) at the start and the end of the year.

	Balance at 01/04/2023 £000	Maturing loans £000	Premature repayments £000	New Borrowing £000	Balance at 31/03/2024 £000
Fixed rate loans – Public Works Loan Board (PWLB)	231,476	9,392	0	60,000	282,084
Total borrowing	231,476	9,392	0	60,000	282,084

- 3.3 The Council has been accessing PWLB loans to fund on-going capital commitments and temporary borrowing from other local authorities to cover short-term cash flow requirements.
- 3.4 As a result of this borrowing and the rise in interest rates during the year, the average rate on the Council's debt increased from 4.15% at 1 April 2023 to 4.50% at 31 March 2024.
- 3.5 Annex A shows how interest rates for borrowing have moved over the course of the year.

4. **Investment Activity**

- 4.1 The Council held short-term investments of £15.4m at the end of 2023/24. These represent the Council's working cash balances.
- 4.2 The Welsh Government's Investment Guidance requires local authorities to focus on security (keeping the money safe) and liquidity (making sure the Council never runs out of cash) as the primary objectives of a prudent investment policy. The Council's aim was to achieve a return on investments in line with these principles. The return is important but is a secondary consideration and the priority is the security of the sums invested.
- 4.3 The table below shows the level of the Council's investments at the start and the end of the year.

	Balance at 01/04/2023 £000	Investments Raised £000	Investments Repaid £000	Balance at 31/03/2024 £000
Investments	24,200	475,000	483,800	15,400

- 4.4 Security of capital remained the Council's main investment objective. This was maintained by following the Council's counterparty policy as set out in its Treasury Management Strategy Statement for 2023/24 which defined "high credit quality" organisations as those having a long-term credit rating of A- or higher if domiciled in the UK or a foreign country with a sovereign rating of AA+ or higher.

Unsecured Bank Deposits

- 4.5 Conventional bank deposits have become riskier because of a lower likelihood that the UK and other governments will support failing banks. As the Banking Reform Act 2014 was implemented in the UK from January 2015, banks were no longer able to rely on government bail-outs if they got into difficulty. They would be required instead to bail themselves out by taking a proportion of investors' deposits to build up their capital. This new risk has been termed 'bail-in' risk and is potentially a greater risk to investors than the 'bail-out' risk of the past.
- 4.6 Given the increasing risk and continued low returns from short-term unsecured bank investments, the Council has only held a minimal amount of investments for short-term cash flow purposes and has placed a far greater emphasis on investing with the UK Government's Debt Management Office and other local authorities in order to minimise these risks.

Credit Risk Management

- 4.7 Counterparty credit quality was assessed and monitored with reference to the following:

- credit ratings (minimum long-term counterparty rating of A- across rating agencies Fitch / S&P / Moody's);
- analysis of funding structure and susceptibility to bail-in;
- credit default swap prices;
- financial statements;
- information on potential government support;
- share prices.

Liquidity Management

- 4.8 In keeping with the WG's guidance on investments, the Council maintained a sufficient level of liquidity through the use of overnight deposits and instant access call accounts. The Authority uses purpose-built cash flow forecasting software to determine the maximum period for which funds may prudently be committed.

Yield

- 4.9 The Council sought to achieve the best return balanced against its objectives of security and liquidity. The UK Bank Rate was increased at regular intervals during 2023/24 and ended the year at a level of 5.25%, therefore the Council's return from investments has also increased during the year.
- 4.10 All investments made during the year complied with the Council's agreed Treasury Management Strategy, Prudential Indicators, Treasury Management Practices and prescribed limits. Maturing investments were repaid to the Council in full and in a timely manner.

5. Compliance with Prudential Indicators

- 5.1 The Council can confirm that it has complied with its Prudential Indicators for 2023/24, which were set in February 2023 as part of the Council's Treasury Management Strategy Statement. Details can be found in Annex B.
- 5.2 In compliance with the requirements of the CIPFA Code of Practice this report provides members with a summary report of the treasury management activity during 2023/24. None of the Prudential Indicators have been breached and a prudent approach has been taken in relation to investment activity with priority being given to security and liquidity over yield.

6. Money Laundering Update

- 6.1 The Council is alert to the possibility that it may become the subject of an attempt to involve it in a transaction involving the laundering of money. Accordingly, it has a Money Laundering Policy and maintains procedures for verifying and recording the identity of counterparties and reporting suspicions, and will ensure that relevant staff are properly trained.

6.2 The Section 151 Officer is the Money Laundering Reporting Officer with the Deputy Section 151 Officer as the Deputy. There haven't been any cases of money laundering reported since the start of Denbighshire to date and the risk to the Council is considered to be minimal.

Annex A

Interest Rates 2023/24

Public Works Loan Board (PWLB) borrowing rates and UK Money Market rates during the year were:

Example PWLB Borrowing rates (The rate at which the Council could borrow money from the Government)

Start Date	Length of Loan		
	1yr %	19½-20 yrs %	49½-50 yrs %
03-Apr-23	4.97	4.86	4.56
29-Sep-23	5.88	5.83	5.61
28-Mar-24	5.56	5.38	5.21

Example Bank Rate, Money Market rates (The rate at which the Council could invest with banks)

Date	Bank Rate %	7-day Investment Rates %	1-month Investment Rates %	6-month Investment Rates %
01-Apr-23	4.25	4.20	4.11	4.59
30-Sep-23	5.25	5.19	5.22	5.63
31-Mar-24	5.25	5.22	5.21	5.14

Annex B

Compliance with Prudential Indicators 2023/24

1 Estimated and Actual Capital Expenditure

- 1.1 This indicator is set to ensure that the level of proposed investment in capital assets remains within sustainable limits and, in particular, to consider the impact on the Council Tax and in the case of the HRA, housing rent levels.

Capital Expenditure	2023/24 Estimated February 2023 £000	2023/24 Outturn March 2024 £000
Non-HRA	92,344	82,861
HRA	19,537	13,781
Total	111,881	96,642

2 Estimated and Actual Ratio of Financing Costs to Net Revenue Stream

- 2.1 This is an indicator of affordability and demonstrates the revenue implications of capital investment decisions by highlighting the proportion of the revenue budget required to meet the borrowing costs associated with capital spending. The financing costs include existing and proposed capital commitments.

Ratio of Financing Costs to Net Revenue Stream	2023/24 Estimated February 2023 £000	2023/24 Outturn March 2024 £000
Financing Costs	15,243	15,308
Net Revenue Stream	250,793	256,563
Non-HRA Ratio	6.08%	5.97%
Financing Costs	7,471	6,950
Net Revenue Stream	18,233	18,373
HRA Ratio	40.98%	37.83%

3 Capital Financing Requirement

- 3.1 The Capital Financing Requirement (CFR) measures the Council's underlying need to borrow for a capital purpose. In order to ensure that over the medium-term net borrowing will only be for a capital purpose, the Council ensures that net external borrowing does not, except in the short term, exceed the CFR in the preceding year plus the estimates of any additional CFR for the current and next two financial years. The following table shows that the Council's borrowing is less than the Council's CFR.

Capital Financing Requirement	2023/24 Estimated February 2023 £000	2023/24 Outturn March 2024 £000
Non-HRA	306,082	279,930
HRA	90,958	83,126
Total	397,040	363,056
Actual external borrowing	292,084	318,584

NB The outturn figures are taken from the pre-audited Statement of Accounts 2023/24 so they may be subject to change.

4 **Authorised Limit and Operational Boundary for External Debt**

Summary Table:

2023/24	31/03/2024 £000
External Borrowing	318,584
Operational Boundary	345,000
Authorised Limit	350,000

- 4.1 **Operational Boundary:** This limit is set to reflect the Council's best view of the most likely prudent (i.e. not worst case) levels of borrowing activity.
- 4.2 **Authorised Limit:** This is the maximum amount of external debt that can be outstanding at one time during the financial year. The limit, which is expressed gross of investments, is consistent with the Council's existing commitments, proposals for capital expenditure and financing and with its approved treasury policy and strategy and also provides headroom over and above for unusual cash movements.
- 4.3 The levels of debt are measured on an ongoing basis during the year for compliance with the Authorised Limit and the Operational Boundary. The Council maintained its total external borrowing and other long-term liabilities within both limits; at its peak this figure was £318.6m. In addition to external borrowing, the Council uses its own reserves and balances to fund capital expenditure and this is known as internal borrowing.

5 Upper Limits for Fixed Interest Rate Exposure and Variable Interest Rate Exposure

- 5.1 These indicators allow the Council to manage the extent to which it is exposed to changes in interest rates. The exposures are calculated on a net basis i.e. fixed rate debt net of fixed rate investments. The upper limit for variable rate exposure allows for the use of variable rate debt to offset exposure to changes in short-term rates on the portfolio of investments.

	2023/24 Estimated %	2023/24 Actual Peak Exposure %
Upper Limit for Fixed Rate Exposure	100	100
Upper Limit for Variable Rate Exposure	40	14.4%

6 Maturity Structure of Fixed Rate Borrowing

- 6.1 This indicator is to limit large concentrations of fixed rate debt needing to be replaced at times of uncertainty over interest rates and is designed to protect against excessive exposures to interest rate changes in any one period, in particular in the course of the next ten years.
- 6.2 It is calculated as the amount of projected borrowing that is fixed rate maturing in each period as a percentage of total projected borrowing that is fixed rate.

Maturity structure of fixed rate borrowing	Upper limit %	Lower limit %	Actual Borrowing as at 31/03/2024 £000	Percentage of total as at 31/03/2024 %
under 12 months	40	0	11,659	4.13
12 months and within 24 months	40	0	41,096	14.57
24 months and within 5 years	40	0	31,976	11.34
5 years and within 10 years	40	0	46,232	16.39
10 years and above	100	30	151,121	53.57
Total			282,084	100.00

7 Total principal sums invested for periods longer than 364 days

- 7.1 This indicator is set in order to allow the Council to manage the risk inherent in investments longer than 364 days. For 2023/24 this limit was set at £10m. The Council did not have any investments which exceeded 364 days during 2023/24.

8 Adoption of the CIPFA Treasury Management Code

- 8.1 The Council confirmed its adoption of the CIPFA Code of Treasury Management at its Council meeting on 26 March 2002. The Council has incorporated the changes from the revised CIPFA Code of Practice into its treasury policies, procedures and practices.

GLOSSARY - Useful guide to Treasury Management Terms and Acronyms

BANK OF ENGLAND	UK's Central Bank
BANK RATE	Bank of England Interest Rate (also known as Base Rate)
CPI	Consumer Price Index – a measure of the increase in prices
RPI	Retail Price Index – a measure of the increase in prices
DMO	Debt Management Office – issuer of gilts on behalf of HM Treasury
FSA	Financial Services Authority - the UK financial watchdog
GDP	Gross Domestic Product – a measure of financial output of the UK
LIBID	London Interbank Bid Rate - International rate that banks lend to other banks
LIBOR	London Interbank Offer Rate – International rate that banks borrow from other banks (the most widely used benchmark or reference for short term interest rates)
PWLB	Public Works Loan Board – a Government department that lends money to Public Sector Organisations
MPC	Monetary Policy Committee - the committee of the Bank of England that sets the Bank Rate
LONG-TERM RATES	More than 12 months duration
SHORT-TERM RATES	Less than 12 months duration
BOND (GENERAL)	An investment in which an investor loans money to a public or private company that borrows the funds for a defined period of time at a fixed interest rate
GOVERNMENT BOND	A type of bond issued by a national government generally with a promise to pay periodic interest payments and to repay the face value on the maturity date
CORPORATE BOND	A type of bond issued by a corporation to raise money in order to expand its business

COVERED BOND

A corporate bond issued by a financial institution but with an extra layer of protection for investors whereby the investor has recourse to a pool of assets that secures or “covers” the bond if the financial institution becomes insolvent

GILT

A bond that is issued by the British government which is classed as a low risk investment as the capital investment is guaranteed by the government

REPO

A repurchase agreement involving the selling of a security (usually bonds or gilts) with the agreement to buy it back at a higher price at a specific future date
For the party selling the security (and agreeing to repurchase it in the future) it is a REPO
For the party on the other end of the transaction e.g. the local authority (buying the security and agreeing to sell in the future) it is a reverse REPO

FTSE 100

Financial Times Stock Exchange 100 - An index composed of the 100 largest companies listed on the London Stock Exchange which provides a good indication of the performance of major UK companies