Item No: 2.3	Classification: Open	Date: 22 February 2023	Meeting Name: Council Assembly
Report title:		Treasury Management Strategy and Capital Strategy 2023-24	
Wards or Groups affected:		All	
From:		Strategic Director of Finance and Governance	

RECOMMENDATIONS

That council assembly notes:

1. The significant movements in the macro-economic environment and financial markets worldwide in 2022-23 and that this will require a reset of the Council's Treasury Management Strategy.

2. That the council continues to invest in an ambitious long-term capital programme that provides significant ongoing benefits throughout the Borough, and revenue streams to support council services.

3. That council assembly approves:

   a. The Capital Strategy 2023-24 at Appendix A

   b. The Treasury Management Strategy Statement 2023-24 at Appendix B

   c. The Investment Management Strategy 2023-24 at Appendix C

   d. The Minimum Revenue Provision Statement 2023-24 at Appendix D

   e. The Prudential Indicators for 2023-26 at Appendix E

BACKGROUND INFORMATION

4. Each year, council assembly agrees an annual strategy covering the management of council debt, capital and treasury investments. The strategy is to be agreed following consultation with the audit, governance and standards committee.

5. Treasury management is the management of the authority's cash flows, borrowing and investments. The council is exposed to financial risks from treasury management activities including possible losses associated with council investment and the potential for increased borrowing costs arising from market movements. The identification,

monitoring and control of financial risks are therefore a crucial part of the financial management and governance arrangements of the council.

6. Since 2019-20, the council has been required to produce a capital strategy report (Appendix A) providing a high level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of local public services along with an overview of how any associated risks are managed and the implications for future financial sustainability.

7. Southwark council has a long tradition of investing in local infrastructure and facilities that support the development of the borough for the benefit of residents and businesses. This investment has been sustained throughout austerity and the more recent pandemic, and has fundamentally supported the generation of new financial resources via a growing council tax base and business expansion. The resulting revenue streams have helped to support basic council services, and on-going capital investment will seek to enhance this income further.

8. Over the previous decade, there have been reliable returns from these income sources. As a result, there has been little need to conduct any fundamental review of capital strategies. Looking forward, there will be increased uncertainty not least as a consequence of the volatility of the economy and especially the impact of rising inflation and interest rates and central government policy on local government financing. These factors are likely to remain major influences on the Authority’s treasury management strategy for 2023-24 and beyond.

9. Under financial delegation, the Strategic Director of Finance and Governance is responsible for all executive and operational decisions on treasury management. This treasury management strategy, together with supporting prudential indicators and policies will ensure that these responsibilities can be carried out effectively. Adherence to this strategy is reported to Council Assembly mid-way through each year and at outturn.

KEY ISSUES FOR CONSIDERATION

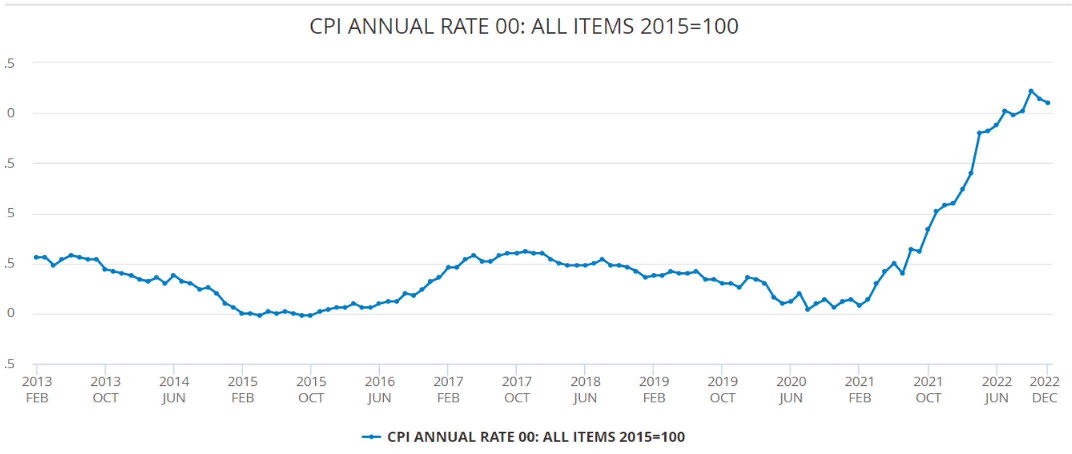
Economic Background

10. The economic landscape in 2022-23 has been shaped by the continuing war in Ukraine, political turmoil in the United Kingdom and rapidly worsening financial outlook both at home and abroad.

11. UK (and global) inflation has remained high. CPI was 10.5% in December after reaching a high of 11.1% in October 2022. The energy regulator, Ofgem, increased the energy price cap by 54% in April, while a further increase in the cap from October was dampened by the UK government stepping in to provide support to limit bills to £2,500 annually until 2024. The government subsequently amended this

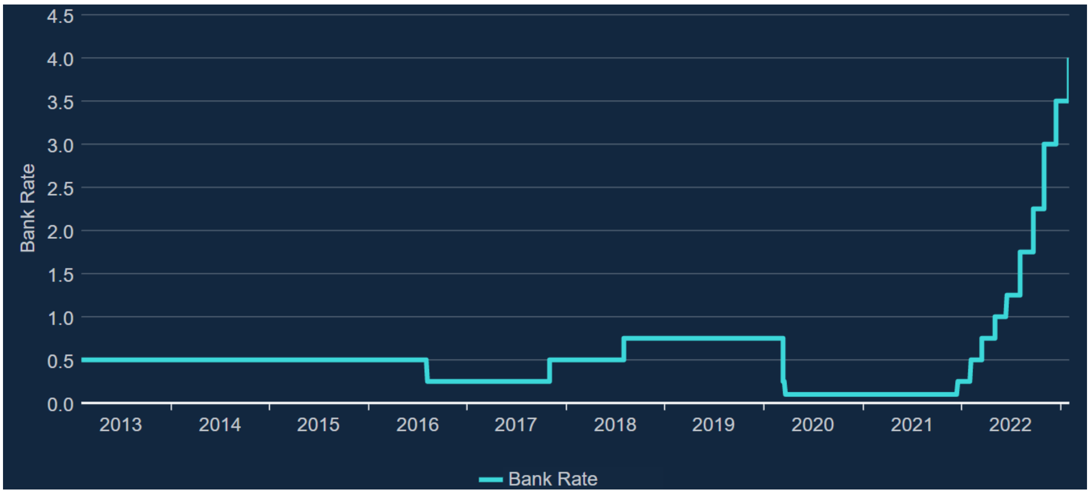
support at the Autumn Statement in November, increasing the cap to around £3,000.

CPI Inflation 2012 – 2022



12. From a base of 0.75% in March 2022, the Bank of England's Monetary Policy Committee (MPC) pushed through interest rate rises of 0.25% in each of the following two MPC meetings, before raising rates by 0.50% in August and again in September to 2.25%. However, in the last few months the Bank further increased the rate by 0.75% to 3% in November, by 0.5% to 3.5% in December and recently by another 0.5% on 2 February 2023.

Bank of England base rate 2013 - 2022



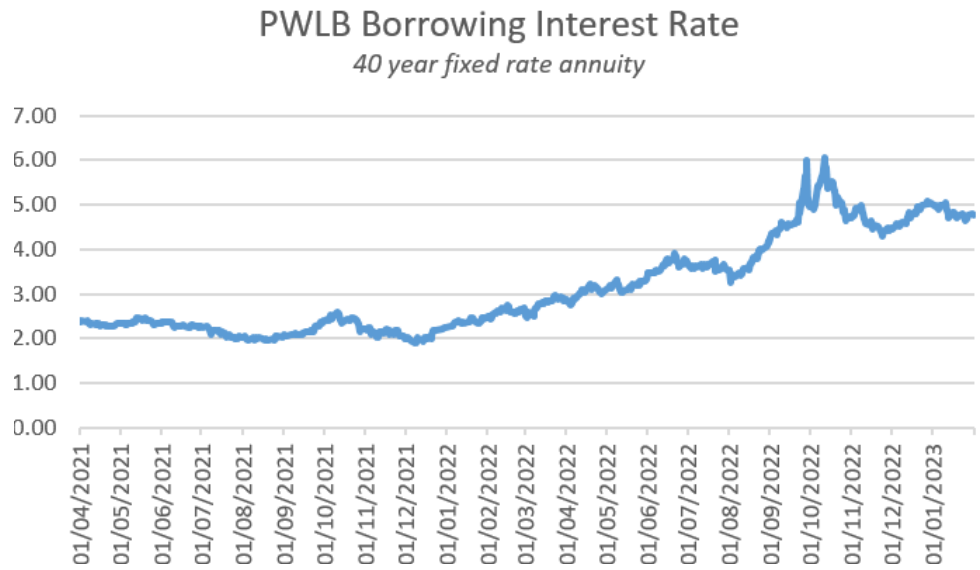
13. On 23 September 2022, the UK government, following a change of leadership, announced some measures in a 'mini budget', loosening fiscal policy with a view to boosting the UK GDP's trend growth rate to 2.5%. This unsettled markets and triggered a series of events including;

- Devaluation of sterling against the dollar to its lowest ever level
- Sudden devaluation of UK gilts, boosting yields to levels not seen in ten years

- A major liquidity event in the UK Liability Driven Investment (LDI) Pensions sector, requiring serious intervention from the BOE including bond purchases and extended re-purchasing facilities.

14. A combination of BOE interventions and multiple fiscal policy u-turns from central government (following encouragement from the IMF) returned some confidence to markets and averted further deterioration in the nation's finances.

15. The increases in both the BOE base rate and UK Gilts are driving up the cost of external borrowing significantly. Whilst the PWLB remains the cheapest option, the cost of new borrowing (and refinancing maturing debt) has increased from 1.9% in December 2021 to 4.79% as at 30 December 2022 – an increase of over 250% in the space of 12 months. Rates briefly touched 6% during the peak of the political crisis in October.



Treasury Management Strategy

16. Treasury management is the management of the authority's cash flows, borrowing and investments. The council is exposed to financial risks from treasury management activity including possible losses associated with council investment and potential for increased borrowing costs arising from market movements. The identification, monitoring and control of financial risks are a crucial part of the financial management and governance arrangements of the council.

17. Treasury risk management is conducted within the framework of the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2021 Edition (the CIPFA Code) which requires the council to approve a treasury management strategy before the start of each financial year. This report fulfils the council's legal obligation under the Local Government Act 2003 to have regard to the CIPFA Code.

18. Investments held for service purposes or for commercial profit are considered in the Capital Strategy.

19. Under financial delegation, the Strategic Director of Finance and Governance is responsible for all executive and operational decisions on treasury management. This treasury management strategy, together with supporting prudential indicators and policies will ensure that these responsibilities can be carried out effectively.

20. Full details of the Council's proposed Treasury Management Strategy for 2023-24 can be found at Appendix B.

Investment Strategy

21. The council's investment objectives for treasury management are to preserve principal, provide liquidity and secure a return on investments consistent with the prior objectives of security and liquidity. This is in line with investment guidance produced by the Ministry of Housing, Communities and Local Government (MHCLG) now rebranded Department for Levelling Up, Housing and Communities (DLUHC).

22. The annual investment management strategy 2023-24 is attached at Appendix C. The strategy will allow investment across highly rated sovereigns, banks and other corporates, quasi-sovereigns, covered bonds whilst limiting excessive exposure to market volatility, and maintaining the overarching objective of ensuring appropriate security and liquidity. External fund managers will be utilised to implement the strategy when appropriate.

23. In considering the investment strategy for 2023-24 the council has taken advice from the external treasury adviser, in addition to ongoing engagement with the council's external fund managers, to ensure that any investment limits and restrictions remain appropriate to meet the investment objectives.

24. The investment strategy for the council for 2023-24 is proposed to remain unchanged as it is considered overall to be well structured to limit any undue risks to the security of assets and preservation of liquidity whilst also allowing the council and delegated managers to access suitable investment opportunities.

Capital Strategy

25. The Capital Strategy is an overarching document which sets the policy framework for the development, management and monitoring of capital investment. The strategy focuses on core principles that underpin the council's capital programme; its short, medium and long-term objectives; the key issues and risks that will impact the delivery of the programme and the governance framework required to ensure the capital programme is delivered providing value for money for residents of Southwark.

26. The capital strategy aligns with the priorities set out in the Southwark Plan and other key council strategies. The strategy is integrated with the medium-term financial strategy and treasury management strategy.

27. A full refresh of the capital programme is due in spring/summer 2023 and will be presented to Council Assembly. This follows a comprehensive review of all general fund and housing project lines and provides an opportunity to review capital funding and re-prioritise the programme in light of the current high interest rate/high inflation environment.

28. The strategy for 2023-24 can be found at Appendix A.

Minimum Revenue Provision

29. Each year, the General Fund sets aside sums known as the minimum revenue provision (MRP) to reduce its borrowing liabilities. The HRA may also set aside sums to reduce its own borrowing liabilities. The policy for MRP is set out in Appendix D and complies with the guidance issued by MHCLG in 2018.

30. Government guidance on the MRP requires that the general fund set aside prudent sums to reduce debt and long term liabilities (such as PFI schemes) arising from capital spend and that the council produces a statement on its MRP policy. MRP costs fall on revenue budgets and runs on for many years into the future, usually over the period to which the capital item provides an economic benefit or the duration of the revenue grant supporting the expenditure.

31. Under the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, a local authority is required to charge a minimum revenue provision annually to its revenue account in respect of capital financing obligations that arise in that year or arose in any prior year. Capital financing obligations represent debt or long-term liabilities taken to fund capital expenditure.

32. A council may not change the total MRP it is liable for but may prudently modify the timing of payments to improve affordability and take account of individual spend and financing characteristics.

33. The methodology and quantum of MRP are subject to scrutiny by the council's external auditors and must be based on robust estimates.

Prudential Indicators

34. Local authority borrowing, investment and capital finance activity is supported by the Prudential Code for Capital Finance and Treasury Management in the Public Services Code of Practice and Guidance published by the Chartered institute of Public Finance and Accountancy, backed by the Local Government Act 2003. The codes introduced a

series of indicators and limits, which the council assembly should agree annually.

35. The indicators for approval relate to 2023-24 to 2025-26 and are set out at Appendix E. The indicators are of a technical nature and include a self-imposed authorised limit on debt, which the council assembly must determine each year. Approval will ensure that the council meets its obligations under the 2003 Act and that the Strategic Director of Finance and Governance can carry out their financial responsibilities in this area.

SUPPLEMENTAL ADVICE FROM OTHER OFFICERS

Assistant Chief Executive, Governance and Assurance

36. The constitution determines that agreeing the treasury management strategy is a function of the council assembly and that review and scrutiny of strategies and policies is the responsibility of the audit and governance committee.

37. Financial standing orders require the Strategic Director of Finance and Governance to set out the treasury management strategy for consideration and decision by council assembly, and report on activity on a quarterly basis to cabinet and at mid and year-end to council assembly. Furthermore, all executive and operational decisions are delegated to the Strategic Director of Finance and Governance.

38. The Local Government Act 2003 and supporting regulations require local authorities to determine annual borrowing limits and have regard to the Prudential Code for Capital Finance, and the Treasury Management in the Public Services Code of Practice and Guidance, published by the Chartered Institute of Public Finance and Accountancy, when considering borrowing and investment strategies, determining or changing borrowing limits or prudential indicators.

39. Section 15(1) of the 2003 Act requires a local authority “to have regard (a) to such guidance as the Secretary of State may issue”. This guidance is found in the Ministry of Communities and Local Government Guidance on Local Authority Investments updated February 2018 and there is statutory guidance on the Minimum Revenue Provision (MRP) produced under amendments made to section 21(1A) of the 2003 Act by section 238(2) of the Local Government and the Public Involvement in Health Act 2007.

40. Members are advised to give approval to the recommendations, ensuring continuing compliance with Government guidance and CIPFA’s codes.

REASONS FOR URGENCY

41. The council is required to set a lawful budget by 11 March 2023. This report informs the council of the treasury management strategy which will support the budget.

REASONS FOR LATENESS

42. Due to the significant macro-economic movements globally, it was necessary to ensure the report used the latest information reasonably available to support the decision-making process.

BACKGROUND DOCUMENTS

Background Papers	Held at	Contact
None		

APPENDICES

No.	Title
Appendix A	Capital Strategy 2023-24 to 2031-32
Appendix B	Treasury Management Strategy 2023-24
Appendix C	Annual Investment Management Strategy 2023-24
Appendix D	Annual Minimum Revenue Provision Statement 2023-24
Appendix E	Prudential Indicators 2023-26

AUDIT TRAIL

Lead Officer	Duncan Whitfield, Strategic Director of Finance and Governance	
Report Author	Tim Jones - Departmental Finance Manager	
Version	Final	
Version Date	16 February 2022	
Key Decision	Yes	
CONSULTATION WITH OTHER OFFICERS / DIRECTORATES / CABINET MEMBER		
Officer Title	**Comments Sought**	**Comments Included**
Assistant Chief Executive, Governance and Assurance	Yes	Yes
Strategic Director of Finance and Governance	N/A	N/A
Cabinet Member	Yes	
Date final report sent to Constitutional Team		16 February 2022