EAST SUSSEX FIRE AUTHORITY

Date:	15 June 2023
Title:	Treasury Management – Stewardship Report for 2022/23
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Background Papers:

East Sussex Fire Authority - 10 February 2022 – Agenda Item 90: Treasury Management Strategy for 2022/23

Policy and Resources Panel - 10 November 2022 – Agenda Item 57: Half yearly report for 2022/23

East Sussex Fire Authority - 9 February 2023 – Agenda Item 202: Treasury Management Strategy for 2023/24

CIPFA Treasury Management in the Public Services Code of Practice and cross sector guidance notes

Local Government Act 2003

CIPFA Prudential Code

Appendices:

1. Economic Overview
2. Counterparty List

Implications:

CORPORATE RISK		**LEGAL**	✓
ENVIRONMENTAL		**POLICY**	
FINANCIAL	✓	**POLITICAL**	
HEALTH & SAFETY		**OTHER (please specify)**	
HUMAN RESOURCES		**CORE BRIEF**	
EQUALITY IMPACT ASSESSMENT			

PURPOSE OF REPORT: The Annual Treasury Management Stewardship Report is a requirement of the Fire Authority's reporting procedures and informs Members of Treasury Management performance and compliance with Prudential Indicators for 2022/23.

EXECUTIVE SUMMARY: The Fire Authority has complied with its approved Treasury Management Strategy and Prudential Indicators for the year.

The Bank of England (BoE) Base Rate increased on eight consecutive occasions during 2022/23. From 0.75% in April 2022 to a closing rate of 4.25% by March 2023. The Bank of England has taken this action to help mitigate inflationary pressures during the year.

The average rate of interest received in 2022/23 through Treasury Management activity was 2.19%. This reflected the Fire Authority's continuing prioritisation of security and liquidity over yield.

No new borrowing was undertaken and two loans totalling £0.481m were repaid during the year. Total loan debt outstanding was £9.817m as at 31 March 2023 and the average interest rate was 4.52%.

The projected outturn of the Fire Authority's Capital Financing Requirement (CFR), a measure of the underlying need to borrow is £9.817m.

Decisions on investment have been taken in the context of the prevailing economic climate, the current approved capital programme and the requirement to fund it over the medium term. No investment in longer duration funds was made during the year.

The economic climate is evolving rapidly, as summarised in the commentary from Link Asset Services (Appendix 1). At this time opportunities are being explored to secure investment returns within the acceptable risk parameters set out in the Authority's agreed Strategy.

During the year the Authority has invested in Environmental, Social and Governance (ESG) funds that meet its policy criteria for security and liquidity and offer comparable or better returns than similar non ESG funds.

RECOMMENDATIONS The Fire Authority is asked to note the Treasury Management performance for 2022/23.

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1 INTRODUCTION

1.1 The Fire Authority's treasury management activities are regulated by a variety of professional codes and statutes and guidance:

a. The Local Government Act 2003 (the Act), which provides the powers to borrow and invest as well as providing controls and limits on this activity;
b. Statutory Instrument (SI) 3146 2003 develops the controls and powers within the Act;
c. The SI requires the Fire Authority to undertake any borrowing activity with regard to the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code for Capital Finance in Local Authorities;
d. Under the Act the Department for Levelling Up, Housing & Communities (DLUHC) has issued Investment Guidance to structure and regulate the Authority's investment activities.

1.2 The Fire Authority has adopted the CIPFA Code of Practice for Treasury Management in the Public Sector and operates its treasury management service in compliance with this Code and the above requirements. These require that the prime objective of the treasury management activity is the effective management of risk, and that its borrowing activities are undertaken on a prudent, affordable and sustainable basis and its treasury management practices demonstrate a low risk approach.

1.3 The Code requires the regular reporting of treasury management activities to:

a. Forecast the likely activity for the forthcoming year (in the Annual Treasury Strategy Report);
b. Review actual activity for the preceding year (this report);
c. A mid year review; and
d. A change in the Strategy (if and when required).

1.4 This report sets out:

a. A summary of the strategy agreed for 2022/23 and the economic factors affecting the strategy in the year;
b. The Fire Authority's treasury activity during the year on borrowing and short term investments;
c. The Prudential Indicators which relate to the Treasury function and compliance with limits

1.5 An Economic overview of the prevailing economic climate during 2022/23 is at Appendix 1.

2 2022/23

2.1 Strategy for 2022/23

2.1.1 At its meeting on 10 February 2022 the Fire Authority agreed its Treasury Management Strategy for 2022/23, taking into account the economic scene, including forecast levels of interest rates. At the same time, the Treasury Management Policy Statement was agreed for 2022/23 as set out below.

2.1.2 East Sussex Fire Authority defines its treasury management activities as:

"The management of the organisation's cash flows, its banking, money market and capital market transactions, the effective management of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

The Fire Authority regards the successful identification, monitoring and management of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation.

This Authority acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving best value in treasury management, and to employing suitable performance measurement techniques, within the context of effective risk management.

Borrowing

2.1.3 The Fire Authority at the beginning of 2022/23 did not expect to undertake any additional external borrowing in the next 12 months. Future borrowing would need to be considered in the short to medium term in order to fund the Capital Strategy.

2.1.4 Opportunities to reschedule debt have been monitored but have not arisen as yet.

Investment

2.1.5 When the strategy was agreed in February 2022, it emphasised the continued importance of taking account of the current and predicted future state of the financial sector. The Treasury Management advisors (Link Asset Services) commented on short term interest rates, the UK economy, inflation, the outlook for long term interest rates and these factors were taken into account when setting the strategy.

2.1.6 The Fire Authority continues to explore Investment options that meet Environment, Social and Governance (ESG) aims. The parameter acts as an added 4th consideration to investment decisions behind Security, Liquidity and Yield. The preservation of capital is the Authority's principal and overriding priority.

2.1.7 The Authority makes use of the creditworthiness service provided by Link Asset Services. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies - Fitch, Moodys and Standard and Poors. The credit ratings of counterparties are supplemented with the following overlays:

- credit watches and credit outlooks from credit rating agencies;
- credit default swap (CDS) spreads to give early warning of likely changes in credit ratings; and

- sovereign ratings to select counterparties from only the most creditworthy countries.

The strategy continued with the policy of pursuing minimum risk but was also intended to deliver secure investment income of at least bank rate on the Fire Authority's cash balances.

2.1.8 The Strategy aimed to ensure that in the economic climate that a prudent approach was maintained. This would be achieved through investing with selected banks and funds which met the Authority's rating criteria. The emphasis would continue on security (protection of the capital sum invested) and liquidity (keeping money readily available for expenditure when needed) rather than yield. The strategy continued with this prudent approach.

2.2 Interest on short term investment balances

2.2.1 The total amount received in short term interest for the 2022/23 was £435,470 at an average rate of 2.19%, the average base rate for the year was 2.30%. A combination of Money Market Funds, Bank Notice Accounts and Bank Fixed Term Deposits were used over the past 12 months.

2.2.2 Full detail of the interest received has been set out in paragraph 3.7.4

2.3 Long term borrowing

2.3.1 No borrowing was undertaken in 2022/23. The total outstanding loan debt at 31 March 2023 was £9,817,000. There were two PWLB loan maturities in year both on the 31 March 2023 for £382,000 and £99,000. The average interest rate on external debt for the year was 4.52%. A further three loans will mature in 2023/24, two on the 30 September 2023 totalling £236,000 at fixed rates of 5.75% and 4.875% and one further loan on the 31 December 2023, £164,000 at a fixed rate of 4.875%.

2.3.2 No rescheduling was undertaken during the year as the average 1% differential between PWLB new borrowing rates and premature repayment rates has made rescheduling unviable.

2.4 Short term borrowing

2.4.1 No borrowing was undertaken on a short-term basis during 2022/23 to cover temporary overdraft situations.

3 PRUDENTIAL INDICATORS AND LIMITS RELATING TO TREASURY MANAGEMENT ACTIVITIES

3.1 The limits set for 2022/23

The Strategy Report for 2022/23 set self-imposed prudential indicators and limits. There are on an annual basis and monitored. They comprise:

- Authorised limit for borrowing (see 3.2 below)
- Interest rate exposure (see 3.3 below)
- Maturity structure of debt (see 3.4 below)

- Maturity structure of investments (see 3.5 below)
- Compliance with the treasury management code of practice (see 3.6 below)
- Interest on our investments (see 3.7 below)
- Capital Financing Requirement and Minimum Revenue Provision Statement (see 3.8 below)

None of the limits were exceeded in 2022/23.

3.2 Authorised limit for borrowing

3.2.1 The table below sets out the actual 2021/22, original estimate and actual in 2022/23 for borrowing.

	2021/22 Actual £000	**2022/23 Original Estimate £000**	**2022/23 Actual £000**
Opening CFR	**10,698**	**10,298**	**10,298**
Capital Investment	1,894	5,426	3,633
Sources of Finance	(1,866)	(5,495)	(3,702)
MRP	(428)	(412)	(412)
Movement in year	**(400)**	**(481)**	**(481)**
Closing CFR	**10,298**	**9,817**	**9,817**
less Finance Lease Liability	-	-	-
Underlying Borrowing Requirement	**10,298**	**9,817**	**9,817**
Actual Long Term Borrowing	**10,298**	**9,817**	**9,817**
Over / (Under) Borrowing	-	-	-
Operational Boundary	**11,166**	**10,378**	**10,378**
Authorised Limit	**13,555**	**12,767**	**12,767**

3.2.2 The outturn for 2022/23 shows no under or over borrowing.

3.2.3 The borrowing limits set in each year include capacity to borrow in advance of need.

3.2.4 The Authorised limit is the “Affordable Borrowing Limit” required by S3 of the Local Government Act 2003 and must not be breached. The external borrowing at 31 March 2023 of £9,817,000 is under the Authorised limit set for 2022/23 of £12,767,000.

3.3 Interest rate exposure

3.3.1 The Fire Authority's Prudential Indicator continued the practice of seeking competitive fixed interest rate exposure for borrowing and lending.

	2022/23	2023/24	2024/25
Interest rate exposures	**Upper**	**Upper**	**Upper**
Limits on fixed interest rates based on net debt*	100%	100%	100%
Limits on variable interest rates based on net debt*	0%	0%	0%

**Net debt is borrowings less investments*

3.4 **Maturity structure of debt**

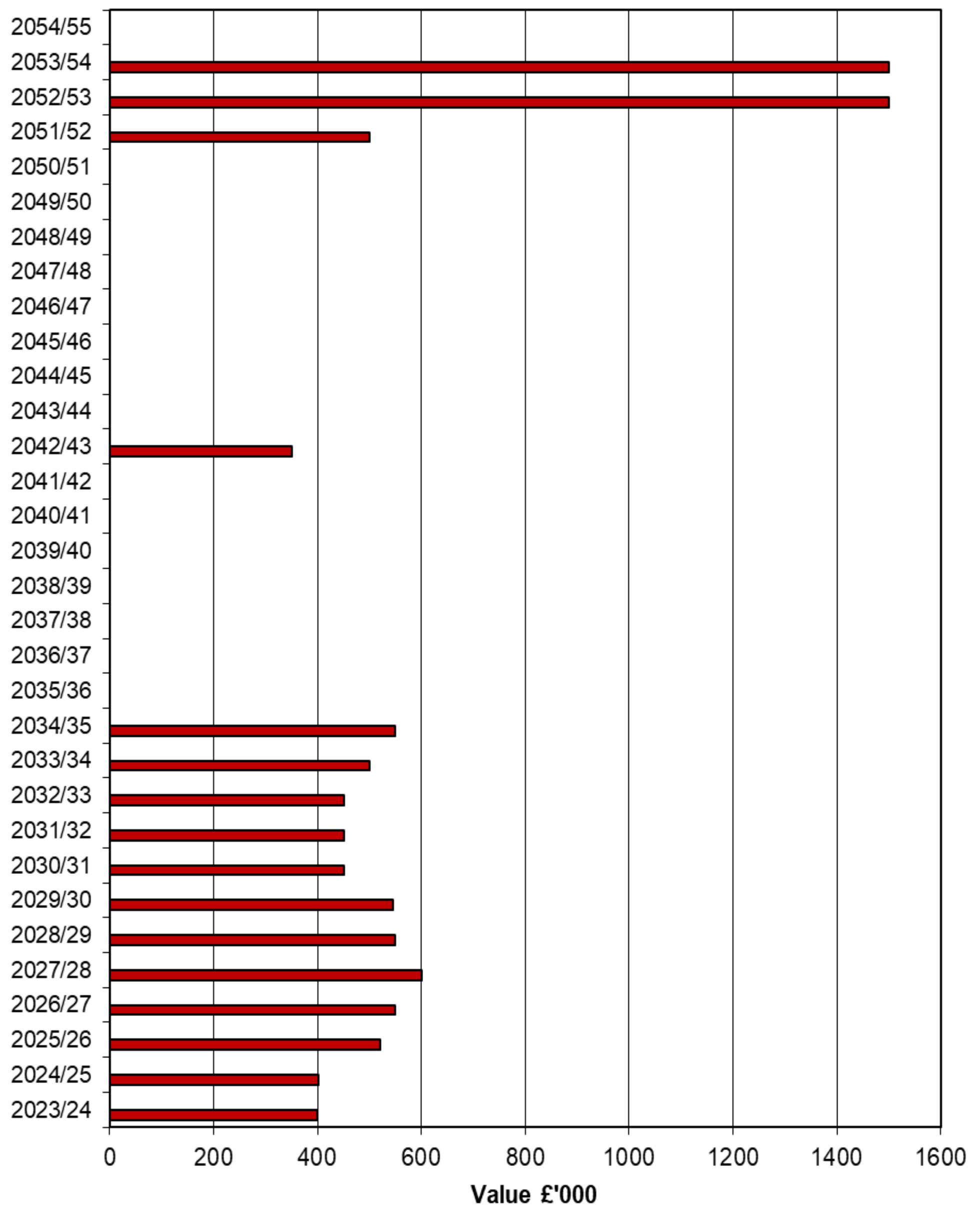
3.4.1 The Fire Authority set upper and lower limits for the maturity structure of its borrowings as follows.

	Lower Limit	Upper Limit	At 31 March 2023
Under 12 months	0%	25%	4%
12 months and within 24 months	0%	40%	4%
24 months and within 5 years	0%	60%	17%
5 years and within 10 years	0%	80%	25%
10 years and within 20 years	0%	80%	14%
20 years and within 30 years	0%	80%	20%
30 years and within 40 years	0%	80%	15%
Over 40 years	0%	80%	0%

3.4.2 Any new borrowing undertaken would give due consideration to the debt maturity profile, ensuring that an acceptable amount of debt is due to mature in any one financial year. This helps to minimise the authority's exposure to the risk of having to replace a large amount of debt in any future years when interest rates may be unfavourable.

3.4.3 No new borrowing was undertaken in 2022/23. The following graph shows the majority of debt matures in the next 10 to 20 years with some longer dated maturities out to 2053/54. Three loans are to be repaid in 2023/24 totalling £400,000.

3.4.4 Fire Authority PWLB Loans Maturity Profile 31 March 2023



3.5 Maturity Structure of Investments

3.5.1 The table below shows the actual sums invested for longer than one year during 2022/23 compared to the limit.

	2022/23 Limit £m	2022/23 Actual £m
Principal Sums invested for longer than 365 days	2.50	0.00

3.6 Compliance with the Treasury Management Code of Practice

East Sussex Fire Authority has adopted the CIPFA Code of Practice for Treasury Management in the Public Services.

3.7 Interest on Investments

3.7.1 During 2022/23 the Bank of England increased bank rate on eight consecutive opportunities, the movements summarised below.

	New Rate	Movement
5 May 2022	1.00%	+0.25%
16 June 2022	1.25%	+0.25%
4 August 2022	1.75%	+0.50%
22 September 2022	2.25%	+0.50%
3 November 2022	3.00%	+0.75%
16 December 2022	3.50%	+0.50%
3 February 2023	4.00%	+0.50%
23 March 2023	4.25%	+0.25%

3.7.2 There have been continued uncertainties in the markets during the year due to global supply chain disruption, inflationary pressure and geopolitical turmoil.

3.7.3 The strategy for 2022/23 continued the prudent approach and ensured that all investments were only to the highest quality rated banks and financial institutions up to a period of 3 years based on the estimates of capital expenditure.

3.7.4 The table below sets out the average monthly rate received on our investments and compares it to the Bank of England Base rate to reflect the interest rates available in the market.

Month	Amount £	Monthly rate	Margin against Average Base rate	Average balance in month £m
April	12,178	0.75%	+0.00%	19.7
May	13,810	0.91%	+0.06%	17.9
June	15,239	1.09%	-0.04%	17.0
July	19,745	1.25%	+0.00%	18.6
August	36,150	1.70%	+0.00%	25.0
September	36,683	1.88%	-0.02%	23.7
October	45,707	2.37%	+0.12%	22.7
November	48,647	2.88%	-0.07%	20.5
December	48,882	3.06%	-0.21%	18.8
January	50,766	3.21%	-0.29%	18.6
February	51,594	3.62%	-0.35%	18.6
March	56,068	3.72%	-0.35%	17.7
Total in 2022/23	**435,470**	**2.19%**	**-0.11%**	**19.9**

3.7.5 The total amount received in short term interest for the year was £435,470 at an average rate of 2.19%. This was below the average base rates in the same period (2.30%). This is as a result of the investment portfolio taking time to catch up with Base rate as investments matured and the funds were able to be re-invested at higher rates.

3.7.6 Throughout the year bank notice accounts and fixed term deposits with banks were used to invest core balances up to duration of 12 months. Instant access cash money market funds were used to hold liquidity balances to meet day to day creditor requirements. Interest earned by the main liquidity buckets from 2021/22 to 2022/23 are detailed below.

Investment Type	Liquidity Bucket	Interest Earned 2021/22 (£)	Interest Earned 2022/23 (£)
Money Market Funds	Instant Access	5,907	129,473
Bank Notice Accounts	95 Day Notice	34,534	120,397
Fixed Term Deposits (Banks)	Fixed Term	17,917	185,600
	Total	**58,358**	**435,471**

3.7.7 The Treasurer and Officers continually reviewed the portfolio and the market situation with regard to investments. The approach to balance investment decisions in the medium to long term with the planned reduction in reserves and balances in the current economic climate continued to be a key consideration.

4 TREASURY MANAGEMENT ADVISORS

4.1 The Strategy for 2022/23 explained that the Fire Authority uses Link Asset Services as its treasury management consultant through the contract that exists with East Sussex County Council. A range of services has been provided including:

a) Technical support on treasury matters, capital finance issues and advice on reporting;
b) Economic and interest rate analysis;
c) Debt services which includes advice on the timing of borrowing;
d) Debt rescheduling advice surrounding the existing portfolio;
e) Generic investment advice on interest rates, timing and investme instruments;
f) Credit ratings from the three main credit rating agencies and other market information;
g) Assistance with training on treasury matters.

4.2 Whilst the advisers provide support to the internal treasury function, under current market rules and the CIPFA Code of Practice the final decision on treasury matters remained with the Authority. This service remains subject to regular review.

4.3 Link Asset Services is the largest provider of Treasury Management advice services to local authorities in the UK and they claim to be the market-leading treasury management service to their clients and better those offered by competitors. The advice will continue to be monitored regularly to ensure an excellent level of service provided to our Authority.

5 CONCLUSION

5.1 The prime objective of Treasury Management is the effective management of risk and that its activities are undertaken in a prudent affordable and sustainable basis. This report confirms the Authority has continued to follow an extremely prudent approach with the main criteria of security and liquidity before yield. The current emphasis must be to continue to be able to react quickly if market conditions worsen.

Appendix 1

2022/23 Economic Backdrop

Provided by Link Asset Services – April 2023

Against a backdrop of stubborn inflationary pressures, the easing of Covid restrictions in most developed economies, the Russian invasion of Ukraine, and a range of different UK Government policies, it is no surprise that UK interest rates have been volatile right across the curve, from Bank Rate through to 50-year gilt yields, for all of 2022/23.

Market commentators' misplaced optimism around inflation has been the root cause of the rout in the bond markets with, for example, UK, EZ and US 10-year yields all rising by over 200bps in 2022. The table below provides a snapshot of the conundrum facing central banks: inflation is elevated but labour markets are extra-ordinarily tight, making it an issue of fine judgment as to how far monetary policy needs to tighten.

Q2 of 2022 saw UK GDP deliver growth of +0.1% q/q, but this was quickly reversed in the third quarter, albeit some of the fall in GDP can be placed at the foot of the extra Bank Holiday in the wake of the Queen's passing. Q4 GDP was positive at 0.1% q/q. Most recently, January saw a 0.3% m/m increase in GDP as the number of strikes reduced compared to December. In addition, the resilience in activity at the end of 2022 was, in part, due to a 1.3% q/q rise in real household disposable incomes. A big part of that reflected the £5.7bn payments received by households from the government under the Energy Bills Support Scheme.

CPI inflation picked up to what should be a peak reading of 11.1% in October, although hopes for significant falls from this level will very much rest on the movements in the gas and electricity markets, as well as the supply-side factors impacting food prices. On balance, most commentators expect the CPI measure of inflation to drop back towards 4% by the end of 2023. As of February 2023, CPI was 10.4%.

The UK unemployment rate fell through 2022 to a 48-year low of 3.6%, and this despite a net migration increase of c500k. The fact remains, however, that with many economic participants registered as long-term sick, the UK labour force shrunk by c500k in the year to June. Without an increase in the labour force participation rate, it is hard to see how the UK economy will be able to grow its way to prosperity, and with average wage increases running at over 6% the MPC will be concerned that wage inflation will prove just as sticky as major supply-side shocks to food (up 18.3% y/y in February 2023) and energy that have endured since Russia's invasion of Ukraine on 22 February 2022.

Bank Rate increased steadily throughout 2022/23, starting at 0.75% and finishing at 4.25%.

GDP has been tepid throughout 2022/23, although the most recent composite Purchasing Manager Indices for the UK, US, EZ and China have all surprised to the upside, registering survey scores just above 50 (below suggests economies are contracting, and above suggests expansion). Whether that means a shallow recession, or worse, will be avoided is still unclear. Ultimately, the MPC will want to see material evidence of a reduction in inflationary pressures and a loosening in labour markets. Realistically, that is an unlikely outcome without unemployment rising and wage settlements falling from their current levels. At present, the bigger rise in employment kept the ILO unemployment rate unchanged at 3.7% in January. Also, while the number of job vacancies fell for the ninth consecutive month in February, they remained around 40% above pre-pandemic levels.

Equity markets, the FTSE 100 started 2023 strongly, rising to a record high of 8,014 on 20th February, as resilient data and falling inflation boosted earnings. But global equities fell sharply after concerns over the health of the global banking system emerged early in March. The fall in the FTSE 100 was bigger than the drop in the US S&P 500. Indeed, at around 7,600 now, the FTSE is 5.2% below its record high on 20th February, while the S&P 500 is only 1.9% lower over the same period. That's despite UK banks having been less exposed and equity prices in the UK's financial sector not falling as far. It may be due to the smaller decline in UK interest rate expectations and bond yields, which raise the discounted value of future earnings, compared to the US.

Appendix 2

Counterparty List 2022/23

Counterparty	Country/ Domicile	Instrument	Maximum investments	Max. maturity period
Counterparties in UK				
Debt Management and Depost Facilities (DMADF)	UK	Term Deposits	unlimited	1 yr
Government Treasury blls	UK	Term Deposits	unlimited	1 yr
Local Authorities	UK	Term Deposits	unlimited	1 yr
RBS/NatWest Group • Royal Bank of Scotland • NatWest	UK	Term Deposits (including callable deposits), Certificate of Deposits	£6m	1 yr
Lloyds Banking Group • Lloyds Bank • Bank of Scotland	UK		£6m	1 yr
Barclays	UK		£6m	1 yr
Santander UK	UK		£6m	1 yr
HSBC	UK		£6m	1 yr
Goldman Sachs IB	UK	Term Deposits	£6m	1 yr
Standard Chartered	UK	Term Deposits	£6m	1 yr
Handelsbanken (UK)	UK	Term Deposits	£6m	1 yr
Individual Money Market Funds (MMF) CNAV and LVNAV	UK/Ireland/ domiciled	AAA rated Money Market Funds	£6m	Liquidity/ instant access
Enhanced Money Market / Cash Funds (EMMFs) VNAV	UK/Ireland/ EU domiciled	AAA Bond Fund Rating	£6m	Liquidity