Performance and Resources Scrutiny Programme 2023/24

Report to: the Office of the Police, Fire and Crime Commissioner for Essex

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Author on behalf of Chief Officer:	**Matt Tokley, Chief Accountant**
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1.0 Purpose of Report

1.1 This report identifies the 2023/24 provisional outturn position for the Force. To present the annual treasury review/outturn report for 2023/24. The Chartered Institute of Public Finance and Accountancy (CIPFA) definition of treasury management is *'The management of the organisation's 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'.*

2.0 Recommendations

2.1 Chief Officers are recommended to formally note the treasury management outturn position for 2023/24.

3.0 Executive Summary

3.1 Noted within Section 1 of the main body of the report. This report provides an overview for how the PFCC's cash balances have been managed during 2023/24, whether there have been any deviations to the 2023/24 Treasury Management Strategy (TMS), and what investments and borrowings (where applicable) were undertaken during the year.

4.0 Introduction/Background

4.1 This report sets out the provisional outturn, highlighting the changes from the Month 12 position. During 2023/24 the PFCC has adopted the *CIPFA Treasury Management in the Public Services: Code of Practice (the CIPFA Code*) which requires the PFCC to approve a treasury management strategy before the start of each financial year as well as produce quarterly and annual treasury management outturn reports. This report fulfils the PFCC's legal obligation under the Local Government Act 2003 to have regard to the CIPFA Code.

4.2 The PFCC's Treasury Management Strategy (TMS) for 2023/24 was presented to the Extraordinary Strategic Board on the 22nd April 2024. The CIPFA Prudential Code also includes a requirement for the PFCC to provide a Capital Strategy and Investment Strategy, documents which cover capital expenditure and financing, and non-treasury investments. In addition, the documents set out the approved thresholds for external borrowing for the upcoming financial year. The Capital Strategy and Investment Strategy for the 2023/24 financial year were also approved on the 22nd April 2024.

4.3 The PFCC has 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. The successful identification, monitoring and control of risk remains central to the PFCC's TMS. The approach to dealing with this risk is covered within the main body of the report.

5.0 External Context / Economic Background

5.1 UK inflation continued to decline from the 8.7% rate seen at the start of 2023/24. By the last quarter of the financial year consumer price inflation (CPI) had fallen to 3.4% in February but was still above the Bank of England (BoE) 2% target at the end of the period.

5.2 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 marginally compared to 2022, and 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.

5.3 Having begun the financial year at 4.25%, the BoE's Monetary Policy Committee (MPC) increased the base rate to 5.25% in August 2023, which continued through to the end of the financial year. 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.

5.4 Following the February MPC meeting, Arlingclose, the authority's treasury advisers, maintained its central view that 5.25% remains the peak in base rate and that interest rates will most likely start to be cut later in 2024. The risks in the short-term are deemed to be to the downside as a rate cut may come sooner than expected, but then more broadly balanced over the medium term.

5.5 Sentiment in financial markets remained uncertain and bond yields continued to be volatile over the year. During the first half of the year, yields rose as interest rates continued to be pushed up in response to rising inflation. From October they started declining again before falling sharply in December due to falling inflation and expected cuts in interest rates in 2024. When it emerged in January that inflation was stickier than expected and the BoE having no immediate inclination to cut rates, yields rose once again.

5.6 In response to an improving outlook for credit markets, in January 2024 Arlingclose moved away from its previous temporary stance of a 35-day maximum duration and increased its advised recommended maximum unsecured duration limit on all banks on its counterparty list to 100 days (the PFCC was not impacted by this as no fixed-term deposits were held at the time with any banks). During the year, the UK sovereign outlook was also upgraded to stable by all three main credit agencies.

5.7 Heightened market volatility is expected to remain a feature, at least in the near term, and credit default swap levels will be monitored for signs of ongoing credit stress. As ever, the institutions and durations on the PFCC's counterparty list (as recommended by Arlingclose and incorporated into the 2024/25 TMS) remain under constant review.

6.0 Current Work and Performance

6.1 On 31st March 2024, the PFCC had net borrowing of (£5.83m) compared to £0.97m net investments, at 31st March 2023, relating to income and expenditure from its revenue and capital activities. This is presented in Table 1 below.

Table 1: Balance Sheet Summary

	31st March 2023 Actual £m	31st March 2024 Actual £m	Movement £m
Capital financing requirement	17.03	26.56	9.53
Usable reserves	(28.90)	(27.33)	1.57
Working capital	10.90	6.60	(4.30)
Net (borrowing)/investments	**0.97**	**(5.83)**	**6.80**

6.2 Table 1 also refers to the Capital Financing Requirement (CFR) which represents the underlying need to borrow for capital purposes. Usable reserves and working capital are the underlying resources available for investment. The above figures reflect the Balance Sheet position at the time of writing and may be subject to change pending completion of the 2023/24 unaudited Statement of Accounts process.

6.3 The treasury management cashbook position as at 31st March 2024 and the change over the twelve-month period is shown in Table 2 below. It should be noted that the short-term borrowing position of (£5.83m) has principally arisen due to the requirement to remove in excess of £5m third party monies from the Balance Sheet for statutory accounting purposes.

Table 2: Treasury Management Summary

	31st March 2023 Actual £m	31st March 2024 Actual £m	Movement £m
Long-term borrowing	0.00	0.00	0.00
Short-term borrowing	0.00	(5.83)	(5.83)
Total external borrowing	**0.00**	**0.00**	**0.00**
Long-term investments	0.00	0.00	0.00
Short-term investments	0.00	0.00	0.00
Cash and cash equivalents	0.97	0.00	(0.97)
Total investments	**0.97**	**0.00**	**(0.97)**
Total net investments	**0.97**	**0.00**	**(0.97)**

6.4 The CIPFA Treasury Management Code now defines treasury management investments as those investments which arise from the PFCC's cash flows or treasury risk management activity that ultimately represents balances that need to be invested until the cash is required in the course of the organisation's core activities.

6.5 The PFCC holds invested funds, representing income received in advance of expenditure plus balances and reserves. During 2023/24 the PFCC's total cash and investment balance ranged between (£3m) and £52m. During this time there were two instances of short-term external borrowing, as discussed further in this paper.

6.6 Both the CIPFA Code and government guidance require the PFCC to invest its funds prudently, and to have regard to the security and liquidity of its treasury investments before seeking the optimum rate of return, or yield. The PFCC's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving low investment income.

6.7 The table below summarises the actual cash, investments and borrowing held at year-end. Please refer to Appendix A for further supporting detail.

Table 3: Cash, Investments and Borrowing

	31st March 2023 Actual £m	31st March 2024 Actual £m	Movement £m
Call accounts	2.51	0.01	(2.50)
Money market funds	1.60	0.00	(1.60)
Lloyds current account	1.00	(0.68)	(1.68)
Total	**5.11**	**(0.67)**	**(5.78)**

6.8 The table below provides a reconciliation for the actual cash, investments and borrowing held at 31st March 2024 (as per Table 3) compared to those presented in Table 2, which comprise the total 'Short-Term Investments', 'Cash and Cash Equivalents' and 'Short-Term Borrowing' values recognised in the 2023/24 year-end PFCC/Group Balance Sheet position.

Table 4: Reconciliation to year-end Balance Sheet position

	31st March 2023 Actual £m	31st March 2024 Actual £m	Movement £m
Total actual cash & investments held	5.11	(0.67)	(5.78)
Less: monies held on behalf of third parties (seizures under POCA and PACE)	(4.13)	(5.19)	(1.06)
Add: petty cash advances/imprest	0.06	0.05	(0.01)
Less: unpresented amounts (operational bank accounts)	(0.07)	(0.02)	0.06
Total cash & cash equivalents, short-term investments & borrowing (as per balance sheet)	**0.97**	**(5.83)**	**(6.80)**

6.9 The above table incorporates elements of cashbook values from the Balance Sheet based on the accounting position at the 31st March. This includes unpresented amounts for force bank accounts reflecting a higher bank balance than recorded in the Balance Sheet at year-end. This relates to timings issues in respect of when amounts were processed onto the financial system. In addition, third-party monies relating to seizures have also been deducted to arrive at the element of cash, investments and borrowings, which the PFCC will report in its accounts at year-end.

6.10 As shown in the opening row of Table 4, actual cash and investments decreased by just under £6m during 2023/24. Generally, levels of both payments and receipts increased over the twelve-month period when compared to the preceding year, 2022/23. In respect of payments, the main increase related to payroll costs for officers, staff and pensioners which increased by £12.3m (£252.1m in 2023/24, compared to £239.8m in 2022/23). This increase included the impact of additional Police Officers being recruited into the force and the related establishment growing, as well as pay inflation. Indirect employee costs relating to the HMRC and Essex Pension Fund increased by £6.5m (£111.0m in 2023/24 compared to £104.5m in 2022/23). The increased value of supplier payments of £141.3m in 2023/24 compared to £131.9m in 2022/23 (£9.4m increase) was comprised of additional revenue and capital commitments as well as lump sum payments to pensioners.

6.11 For receipts, the council tax rise in 2023/24 contributed revenue income of £155.3m (£144.3m in 2022/23), an increase of £11.0m. Other central sources of government funding as well as several significant grants (as detailed within the TM update reports submitted throughout the year) contributed to an increase in cashflow of £16.3m (£268.0m in 2023/24 compared to £251.7m in 2022/23). Also of note was an increase in miscellaneous income of £3.1m (£45.8m in 2023/24 compared to £42.7m in 2022/23). This reflected the general upward trend in customer receipts as well as cross-force recharges. Other movements in income streams included a marginal increase in VAT reimbursements of £0.6m, additional Stansted Airport receipts from Manchester Airport Group of £1.1m, and a year-on-year increase in property sales of £0.9m. The latter was despite some late slippage in year for several ongoing disposals scheduled, mainly due to ongoing contractual issues.

6.12 The average level of investments (excluding the element relating to third party monies) over the twelve-month period was £19.487m (£20.924m in 2022/23). Interest earnings for the period were £1.202m (£0.418m 2022/23), representing an average return of 4.97% (2.00% 2022/23) continuing the upward trend over the last couple of financial years, as the PFCC benefitted from the buoyant UK interest rate position. Based on the rate of return in 2023/24, the deemed element of investment income earned on monies held on behalf of third parties was £0.234m with the remaining amount of £0.968m relating to force cash. However, both elements were recognised as investment income in year, with any subsequent repayment of interest due to third parties debited back against income in the year concerned.

6.13 Money market funds (MMF's) and local authority deposits provided competitive returns when compared to the Debt Management Account Deposit Facility (DMADF), with rates typically offering higher yield as well as same day liquidity. During the last quarter of 2023/24 the rates on DMADF deposits ranged between 5.00% and 5.20%, whilst returns on MMF's used by the PFCC ranged between 5.15% to 5.30%.

6.14 The PFCC's chief objective when undertaking external borrowing is to either cover short-term cashflow deficits or, where applicable, fund longer-term investment. The main factors considered are to strike an appropriately minimal risk balance between securing low interest costs and achieving cost certainty over the period.

6.15 As of 31st March 2024, the PFCC held no long-term external borrowing, a position which was consistent with the previous year-end. The PFCC did however hold an overdraft position at the 31st March 2024 with Lloyds bank, as shown in Table 3. There were also two instances of external short-term borrowing within 2023/24, £4m with Conwy County Borough Council and £4m with Coventry City Council. Both instances related to short-term cashflow-related borrowing during the first quarter of the year to maintain sufficient liquidity for treasury activities in line with the PFCC's TMS.

6.16 The Prudential Code is clear that the PFCC must not borrow to invest primarily for financial return and that it is not prudent for the PFCC to make any investment or spending decision that will increase the CFR (and thus potentially leading to new external borrowing) unless directly and primarily related to the functions of the organisation. During 2023/24 the PFCC has not invested in assets primarily for financial return, or that are not primarily related to the functions of the organisation.

6.17 Whilst the PFCC held no external borrowings (apart from its overdraft balance) at 31st March 2024, there was an increase in internal borrowing across the 2023/24 financial year, due to a diminished amount of capital resources available to fund an annual capital programme which exceeded £14.6m in value in 2023/24. Internal borrowing relates to the accounting mechanism whereby the PFCC can choose to defer financing it is capital expenditure in the year and use its cash resources instead. This produces an increase in the CFR which is then reduced by Minimum Revenue Provision (MRP) being applied in subsequent years. For 2023/24 the closing CFR was £26.554m compared to £17.028m at the end of 2022/23. The net increase of £9.526m related to unfinanced 2023/24 capital expenditure of £10.359m, offset by £0.833m MRP being charged to revenue in the year.

6.18 Financing costs, comprising interest payable and MRP incurred in the year were budgeted at £1.110m, with the outturn position of £0.839m reflecting a £0.271m saving, due to the interest budget of £0.206m only resulting in £0.006m of actual costs in the year, and the actual MRP charge equating to £0.833m compared to the budgeted £0.904m.

7.0 Compliance

Prudential Indicators

7.1 All treasury management activities undertaken during 2023/24 have complied with the CIPFA Code of Practice and the CIPFA Prudential Code, as reported to the PFCC during the year via quarterly update reports being submitted to the Strategic Board.

7.2 **Liability Benchmark:** This indicator compares the PFCC's actual existing borrowing against a liability benchmark that has been calculated to show the lowest risk level of borrowing. The liability benchmark is an important tool to help establish whether the PFCC is likely to be a long-term borrower or long-term investor in the future, and so shapes its strategic focus and decision making. It represents an estimate of the cumulative amount of external borrowing the PFCC must hold to fund its current capital and revenue plans while keeping treasury investments as the minimum level of £10m to manage day to day cashflow. The 2023/24 performance against this model (based on Table 1), as well as the forecast position at the end of the next two years is presented in Table 5 below.

Table 5 – Liability Benchmark

	31st March 2024 Forecast £m	31st March 2024 Actual £m	31st March 2025 Forecast £m	31st March 2026 Forecast £m
Capital financing requirement	26.20	26.56	41.74	50.04
Less: balance sheet resources	(13.60)	(20.73)	(25.00)	(20.00)
Net loans requirement	**(12.60)**	**(5.83)**	**(16.74)**	**(30.04)**
Plus: liquidity allowance	10.00	0.00	10.00	10.00
Liability benchmark	**(22.60)**	**(5.83)**	**(26.74)**	**(40.04)**
Existing borrowing (actual)	**0.00**	**(0.68)**	**0.00**	**0.00**

7.3 The PFCC has chosen not to externally borrow solely to meet its liquidity allowance target – this approach is consistent within the 2023/24 closing position and the table above, with this process also being clarified within the 2024/25 TMS.

7.4 **Gross Debt:** The PFCC is legally obliged to set an affordable external borrowing limit (also termed the authorised limit for external debt) each year. In line with statutory guidance a lower 'operational boundary' is also set as a warning level should external debt approach the affordable borrowing limit. This is calculated as the maximum level held at any one time during the financial year. Confirmation of the compliance with both the authorised limit and operational boundary key prudential indicators in 2023/24 are shown in Table 6 below.

Table 6 – Gross Debt Limits

	2023/24 - TMS	2023/24 - Actual	Complied (Yes/No)
Authorised limit - total external debt	£40m	£4m	Yes
Operational Boundary - total external debt	£35m	£4m	Yes

7.5 **Investment Counterparties:** Compliance with the approved investment counterparties list included in the 2023/24 TMS has been regularly reported in detail via the quarterly TM update reports process and has therefore not been reproduced here. The PFCC's investments have fully complied with the TMS throughout 2023/24 with the changes in relation to money market funds (MMF) criteria in the TMS assisting with the efficient management of the PFCC's liquid funds during the year.

7.6 **Proportion of Financing Costs to Net Revenue Stream:** Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP are both charged to revenue. The net annual charge is known as financing costs, which is compared to the net revenue stream (e.g. the amount funded from council tax and government grants). The 2023/24 proportion of financing costs compared to the net revenue stream, as well as the budgeted position for the next two years thereafter is presented in Table 7 below.

Table 7 – Proportion of Financing Costs to Net Revenue Stream

	2023/24 - Actual	2024/25 - Budget	2025/26 - Budget
Net financing costs	£0.839m	£1.813m	£3.777m
Net revenue stream	£363.684m	£385.538m	£391.024m
Proportion of net revenue stream	0.23%	0.47%	0.97%

7.7 The other prudential indicators within the TMS are as follows:

- Estimates of Capital Expenditure
- Estimates of Capital Financing Requirement
- Gross Debt and the Capital Financing Requirement

7.8 The above indicators are regularly reported to the PFCC, and this information has therefore not been re-produced here, with compliance accepted across the 2023/24 financial year in each case.

Treasury Management Indicators

7.9 The PFCC measured and managed its exposure to treasury management risks during 2023/24 using the following indicators.

7.10 **Interest rate exposure:** This indicator is set to control the PFCC's exposure to interest rate risk. The figures reflect the potential impact of a rise or decrease in the base rate by 1% with a potential adverse impact arising in each instance. The indicator for interest rate rises is based upon the potential exposure to additional interest payable. The indicator for interest rate reductions is based upon the potential exposure to reduced levels of investment income.

Table 8 - Interest Rate Exposure

	2023/24 - TMS interest rate position	31/3/24 interest rate position	2023/24 forecast impact - max tolerance	2024/24 actual impact	Complied (Yes/No)
Upper limit on one year revenue impact of a 1% rise in interest rates	4.00%	5.25%	100,000	N/A (no material borrowing)	Yes
Upper limit on one year revenue impact of a 1% fall in interest rates	4.00%	5.25%	100,000	N/A (no rate decrease)	Yes

7.11 **Security:** The PFCC has adopted a voluntary measure of its exposure to credit risk by using minimum credit rating criteria for the counterparties it invests money with. These credit ratings are provided by the three main credit agencies in the UK (Standard & Poors, Fitch and Moody's) and are used in addition to counterparty information received from the PFCC's treasury management advisors Arlingclose.

Table 9 - Minimum Credit Ratings for Counterparties

	2023/24 target	31/3/24 actual	Complied (Yes/No)
Minimum Credit Rating	A	A	Yes

7.12 **Liquidity:** The PFCC has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments on a daily basis, without the need for additional external borrowing. The amount available as well as the maximum amount utilised during 2023/24 is set out in Table 10 below.

Table 10 - PFCC Bank Overdraft Facility

`	2023/24 target maximum facility	2023/24 actual maximum facility	2023/24 actual maximum usage	Complied (Yes/No)
PFCC bank accounts	£3m	£3m	£2.2m	Yes

7.13 **Monies retained in same day access funds:** The PFCC seeks to keep a minimum amount of money in call accounts and money market funds to ensure it is fully able to meet unforeseen commitments as they arise. The guideline criteria and actual position in 2023/24 are shown in Table 11 below:

Table 11 - Monies Retained in Same Day Access Funds

`	2023/24 target	Complied (Yes/No)
Minimum amount of investment portfolio held in call accounts and money market funds	Lower of £10m or 50% of total investments	Yes

7.14 This indicator has been met primarily based on the PFCC's approach to maximising its investments within its five MMF's, which offer both liquidity benefit as well as competitive yields. Typically, other investment opportunities have only been progressed once the MMF limits have been fully utilised.

7.15 **Principal sums invested beyond 365 days:** The purpose of this indicator is to control the PFCC's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the total principal sum invested to maturity dates which exceed one year *for non-government investments only*, are shown in Table 12 below:

Table 12 – Investments Longer than One Year

`	2023/24 target	2023/24 actual	Complied (Yes/No)
Principal invested beyond one year in duration (non-government)	£0m	£0m	Yes

7.16 **Maturity structure of borrowing:** This indicator is set to control the PFCC's exposure to refinancing risk. The upper and lower limits on the maturity structure of external borrowing were set out in the 2023/24 TMS with various thresholds for differing time periods. As the PFCC only had two short-term instances of external borrowing during the year, this fell into the 'less than 12 months bracket' for which a 100% threshold applied. The PFCC therefore complied with this indicator.

8.0 Implications (Issues)

8.1 The implications are reported in the main body of the report.

9.0 Links to Police and Crime Plan Priorities

9.1 The force cashflow is used to help meet the priorities of the Police and Crime Plan.

10.0 Demand

10.1 N/A.

11.0 Risks/Mitigation

11.1 The related risks and the approach to managing these are reported in the main body of the report.

12.0 Equality and/or Human Rights Implications

12.1 N/A.

13.0 Health and Safety Implications

13.1 N/A.

14.0 Consultation/Engagement

14.1 N/A.

15.0 Actions for Improvement

15.1 N/A.

Appendix A

Investments position on 31st March 2023

	31/03/2023 £000	Start date	Maturity date	Approx. Rate %
Call/notice accounts				
Santander UK PLC	10			3.00%
Barclays Bank FIBCA	2,500			3.25%
Total	**2,510**			
Money market funds				
Insight	100			4.11%
Federated Hermes	1,000			4.09%
Aviva	500			4.11%
Total	**1,600**			
Other				
Lloyds current account	999			2.50%
	999			
Total treasury investments	**5,109**			

Investments position on 31st March 2024

	31/03/2024 £000	Start date	Maturity date	Approx. Rate %
Call/notice accounts				
Barclays Bank FIBCA	10			4.25%
Total	**10**			
Other				
Lloyds current account	(677)			5.00%
	(677)			
Total treasury investments	**(667)**			