

TREASURY MANAGEMENT Q1 REPORT 2023/24

Report of the Deputy Chief Executive (Section 151 Officer)

1 INTRODUCTION AND PURPOSE OF REPORT

- 1.1 The CIPFA (Chartered Institute of Public Finance and Accountancy) Code of Practice for Treasury Management recommends that Members be updated on treasury management activities regularly (annual, mid-year and quarterly reports). This report therefore ensures this Council is implementing best practice in accordance with the Code.

2. ECONOMICS UPDATE

- 2.1 The first quarter of 2023/24 saw:

- A 0.2% month on month (m/m) rise in real GDP in April, partly due to fewer strikes;
- CPI inflation falling from 10.1% to 8.7% in April, before remaining at 8.7% in May. This was the highest reading in the G7;
- Core CPI inflation¹ rise in both April and May, reaching a new 31-year high of 7.1%;
- A tighter labour market in April, as the 3-month average of the annual rate (myy) growth of average earnings rose from 6.1% to 6.5%;
- Interest rates rise by a further 75 basis points (bps) over the quarter, taking Bank Rate from 4.25% to 5.00%;
- 10-year gilt yields nearing the 'mini-Budget' peaks, as inflation surprised to the upside.

- 2.2 The economy has weathered the drag from higher inflation better than was widely expected. The 0.2% m/m rise in real GDP in April, following March's 0.3% m/m contraction will further raise hopes that the economy will escape a recession this year. Some of the strength in April was due to fewer strikes by train workers and teachers in that month. Moreover, some of the falls in activity in other areas in April were probably temporary too. Strikes by junior doctors and civil servants contributed to the fall in health output (0.9% m/m) and the meagre 0.1% m/m increase in public administration.

- 2.3 The fall in the composite Purchasing Managers Index (PMI) from 54.0 in May to a three-month low of 52.8 in June (>50 points to expansion in the economy, <50 points to contraction) was worse than the consensus forecast of 53.6. Both the services and manufacturing PMIs fell. The decline in the services PMI was bigger (from 55.2 to 53.7), but it remains consistent with services activity expanding by an annualised 2%. The fall in the manufacturing PMI was smaller

¹ Core inflation represents the long run trend in the price level. In measuring long run inflation, transitory price changes should be excluded. One way of accomplishing this is by excluding items frequently subject to volatile prices, like food and energy.

(from 47.1 to 46.2), but it is consistent with the annual rate of manufacturing output falling from -0.8% in April to around -5.0%. At face value, the composite PMI points to the 0.1% q/q rise in GDP in Q1 2023 being followed by a 0.2% q/q gain in Q2 2023.

- 2.4 Meanwhile, the 0.3% m/m rise in retail sales volumes in May was far better than the consensus forecast of a 0.2% m/m decline and followed the robust 0.5% m/m rise in April. Some of the rise was due to the warmer weather. Indeed, the largest move was a 2.7% m/m jump in non-store sales, due to people stocking up on outdoor-related goods. But department stores also managed to squeeze out a 0.6% m/m rise in sales and the household goods sub-sector enjoyed a reasonable performance too. Overall, the figures were far better than analysts had expected. In addition, the GfK measure of consumer confidence rebounded from -27 to a 17-month high of -24 in June.
- 2.5 The recent resilience of the economy has been due to a confluence of factors including the continued rebound in activity after the pandemic, households spending some of their pandemic savings, and the tight labour market and government handouts both supporting household incomes. That said, as government support fades, real household incomes are unlikely to grow rapidly. Furthermore, higher interest rates will mean GDP is likely to contract later this year. Our central assumption is that inflation will drop to the 2.0% target only if the Bank triggers a recession by raising rates from 5.00% now to at least 5.5% and keeps rates there until at least mid-2024. Our colleagues at Capital Economics estimate that around 60% of the drag on real activity from the rise in rates has yet to bite, and the drag on the quarterly rate of real GDP growth over the next year may be about 0.2ppts bigger than over the past year.
- 2.6 The labour market became tighter over the quarter and wage growth reaccelerated. Labour demand was stronger than the consensus had expected. The three-month change in employment rose from +182,000 in March to +250,000 in April. Meanwhile, labour supply continued to recover as the size of the labour force grew by 303,000 in the three months to April. That was supported by a further 140,000 decline in inactivity as people returned to work from retirement and caring responsibilities (while inactivity due to long-term sick continued to rise). But it was not enough to offset the big rise in employment, which meant the unemployment rate fell from 3.9% to 3.8%
- 2.7 The tighter labour market supported wage growth in April, although the 9.7% rise in the National Living Wage on 1st April (compared to the 6.6% increase in April last year) probably had a lot to do with it too. The 3myy rate of average earnings growth reaccelerated from 6.1% to 6.5% (consensus 6.1%) and UK wage growth remains much faster than in the US and the Euro-zone. In addition, regular private sector wage growth increased from 7.1% 3myy to 7.6%, which left it well above the Bank's forecast for it to fall below 7.0%. Overall, the loosening in the labour market appears to have stalled in April and regular private sector wage growth was well above the Bank's forecast.
- 2.8 CPI inflation stayed at 8.7% in May (consensus 8.4%) and, perhaps more worryingly, core CPI inflation rose again, from 6.8% to a new 31-year high of 7.1%. The rise in core inflation built on the leap from 6.2% in March to 6.8% and means it is accelerating in the UK while it is slowing in the US and the Euro-zone (both fell to 5.3%). A further decline in fuel inflation, from -8.9% to -13.1%, and the second fall in food inflation in as many months, from 19.3% to 18.7%, explained why overall CPI inflation didn't rise. And the scheduled fall in the average annual utility price from £2,500 to £2,074 on 1 July means overall CPI inflation will probably ease in the coming months. But the problem is that the

recent surge in core inflation and the reacceleration in wage growth shows that domestic inflationary pressures are still strengthening.

- 2.9 This suggests the Bank may have more work to do than the Fed or ECB². Indeed, the Bank of England sounded somewhat hawkish in the June meeting. This came through most in the MPC's decision to step up the pace of hiking from the 25bps at the previous two meetings. The 7-2 vote, with only two members voting to leave rates unchanged at 4.50%, revealed support for stepping up the fight against high inflation.
- 2.10 That said, the Bank has not committed to raising rates again or suggested that 50bps rises are now the norm. What it did say was that 'the scale of the recent upside surprises in official estimates of wage growth and services CPI inflation suggested a 0.5 percentage point increase in interest rates was required at this particular meeting'. Moreover, the Committee did not strengthen its forward guidance that any further rate hikes would be conditional on the data. However, it looks highly probable, given the on-going strength of inflation and employment data, that the Bank will need to raise rates to at least 5.5% and to keep rates at their peak until the mid-point of 2024. We still think it is only a matter of time before the rise in rates weakens the economy sufficiently to push it into recession. That is why instead of rising to between 6.00%-6.25%, as is currently priced in by markets, we think rates are more likely to peak between 5.50-6.00%. Our forecast is also for rates to be cut in the second half of 2024, and we expect rates to then fall further than markets are pricing in.
- 2.11 Growing evidence that UK price pressures are becoming increasingly domestically generated has driven up market interest rate expectations and at one point pushed the 10-year gilt yield up to 4.49% in late June, very close to its peak seen after the "mini-budget". Yields have since fallen slightly back to 4.38%. But growing expectations that rates in the UK will remain higher for longer than in the US mean they are still more than 70bps above US yields. While higher interest rates are priced into the markets, the likely dent to the real economy from the high level of interest rates is not. That's why we think there is scope for market rate expectations to fall back in 2024 and why we expect the 10-year PWLB Certainty Rate to drop back from around 5.20% to 5.00% by the end of this year and to 4.20% by the end of 2024.
- 2.12 The pound strengthened from \$1.24 at the start of April to a one-year high at \$1.26 in early May, which was partly due to the risks from the global banking issues being seen as a bigger problem for the US than the UK. The pound then fell back to \$1.23 at the end of May, before rising again to \$1.28 in the middle of June as the strong core CPI inflation data released in June suggested the Bank of England was going to have to raise rates more than the Fed or ECB in order to tame domestic inflation. However, sterling's strong run may falter because more hikes in the near term to combat high inflation are likely to weaken growth (and, hopefully, at some point inflation too) to such a degree that the policy rate will probably be brought back down, potentially quite quickly, as the economic cycle trends downwards decisively. This suggests that additional rate hikes are unlikely to do much to boost the pound.
- 2.13 In early April, investors turned more optimistic about global GDP growth, pushing up UK equity prices. But this period of optimism appears to have been short-lived. The FTSE 100 has fallen by 4.8% since 21 April, from around 7,914

² **FED** (The Federal Reserve System) is the central banking system of the United States. Its core responsibilities include setting interest rates, managing the money supply, and regulating financial markets. **ECB** (The European Central Bank) is the prime component of the Eurosystem and the European System of Central Banks as well as one of seven institutions of the European Union. It is one of the world's most important central banks.

to 7,553, reversing part of the 7.9% rise since 17 March. Despite the recent resilience of economic activity, expectations for equity earnings have become a bit more downbeat. Nonetheless, further down the track, more rate cuts than markets anticipate should help the FTSE 100 rally.

2.14 MPC meetings 11 May and 22 June 2023

- 2.14.1 On 11 May, the Bank of England’s Monetary Policy Committee (MPC) increased Bank Rate by 25bps to 4.50%, and on 22 June moved rates up a further 50bps to 5.00%. Both increases reflected a split vote, seven members voting for an increase and two for none.
- 2.14.2 Nonetheless, with UK inflation significantly higher than in other G7 countries, the MPC will have a difficult task in convincing investors that they will be able to dampen inflation pressures anytime soon. Talk of the Bank’s inflation models being “broken” is perhaps another reason why gilt investors are demanding a premium relative to US and Euro-zone bonds, for example.
- 2.14.3 Of course, what happens outside of the UK is also critical to movement in gilt yields. The US Federal Open Market Committee has already hiked short-term rates to a range of 5.00%-5.25%, but a further increase is pencilled in for July, whilst the ECB looks likely to raise its Deposit rate at least once more to a peak of 3.75%, with upside risk of higher to come.

3 Interest rate forecasts

- 3.1 The Council has appointed Link Group as its treasury advisors and part of their service is to assist the Council to formulate a view on interest rates. The PWLB rate forecasts below are based on the Certainty Rate (the standard rate minus 20bps) which has been accessible to most authorities since 1 November 2012.
- 3.2 The latest forecast, made on 26 June, sets out a view that both short and long-dated interest rates will be elevated for some little while, as the Bank of England seeks to squeeze inflation out of the economy, against a backdrop of a stubbornly robust economy and a tight labour market.
- 3.3 You will note that our forecasts have steadily increased during the quarter as the data continued to spring upside surprises, and the Bank of England continued to under-estimate how prevalent inflation is, and how tight the labour market is. The Government has also noted that despite immigration increasing markedly, high levels of ill-health amongst the workforce has led to wage demands remaining strong until such time as there is a loosening in demand for business services.
- 3.4 Current PWLB rate forecasts below are based on the Certainty Rate

Link Group Interest Rate View 26.06.23

	June 2023	Sept 2023	Dec 2023	March 2024	June 2024	Sept 2024	Dec 2024	March 2025	June 2025	Sept 2025	Dec 2025	March 2026	June 2026
Bank Rate	5.00%	5.50%	5.50%	5.50%	5.25%	4.75%	4.25%	3.75%	3.25%	2.75%	2.75%	2.50%	2.50%
3m ave earn *	5.30%	5.60%	5.50%	5.30%	5.00%	4.50%	4.00%	3.50%	3.00%	2.70%	2.60%	2.50%	2.50%
6m ave earn *	5.80%	5.90%	5.70%	5.50%	5.10%	4.60%	4.00%	3.50%	3.00%	2.70%	2.60%	2.60%	2.60%
12m ave earn *	6.30%	6.20%	6.00%	5.70%	5.30%	4.80%	4.10%	3.60%	3.10%	2.80%	2.70%	2.70%	2.70%
5y PWLB	5.50%	5.60%	5.30%	5.70%	4.80%	4.50%	4.20%	3.90%	3.60%	3.40%	3.30%	3.30%	3.20%
10y PWLB	5.10%	5.20%	5.00%	4.90%	4.70%	4.40%	4.20%	3.90%	3.70%	3.50%	3.50%	3.50%	3.40%
25y PWLB	5.30%	5.40%	5.20%	5.10%	4.90%	4.70%	4.50%	4.20%	4.00%	3.90%	3.80%	3.80%	3.70%
50y PWLB	5.00%	5.10%	5.00%	4.90%	4.70%	4.50%	4.30%	4.00%	3.80%	3.60%	3.60%	3.50%	3.50%

- * LIBOR and LIBID rates ceased at the end of 2021. In a continuation of previous views, money market yield forecasts are based on expected average earnings by local authorities for 3 to 12 months. The Link forecast for average earnings are averages i.e., rates offered by individual banks may differ significantly from these averages, reflecting their different needs for borrowing short-term cash at any one point in time.

3.5 **A Summary Overview of the Future Path of Bank Rate**

- The Link central forecast for interest rates was previously updated on 25 May 2023 and reflected a view that the MPC would be keen to further demonstrate its anti-inflation credentials by delivering a succession of rate increases. This has happened to a degree, especially as it moved to a more aggressive 0.5% hike in June but, with inflation remaining elevated, we anticipate that Bank Rate will need to increase to at least 5.5%, if not higher, to sufficiently slow the UK economy and loosen the labour market.
- Moreover, it is still anticipated that the Bank of England will be keen to loosen monetary policy when the worst of the inflationary pressures are behind us, but timing on this will remain one of fine judgment: cut too soon, and inflationary pressures may well build up further; cut too late and any downturn or recession may be prolonged. Our current judgment is that rates will have to increase and stay at their peak until the second quarter of 2024 as a minimum.
- In the upcoming months, forecasts will be guided not only by economic data releases and clarifications from the MPC over its monetary policies and the Government over its fiscal policies, but also international factors such as policy development in the US and Europe, the provision of fresh support packages to support the faltering recovery in China as well as the on-going conflict between Russia and Ukraine and whether there are any further implications for Russia itself following the recent aborted mutiny by the Wagner group.
- On the positive side, consumers are still estimated to be sitting on excess savings left over from the pandemic, which could cushion some of the impact of the above challenges and may be the reason why the economy is performing somewhat better at this stage of the economic cycle than may have been expected. However, most of those excess savings are held by more affluent people whereas lower income families already spend nearly all their income on essentials such as food, energy and rent/mortgage payments.

3.6 **Forecast PWLB RATES**

- Gilt yield curve movements have shifted upwards, especially at the shorter end of the yield curve since our previous forecast but remain relatively volatile. PWLB 5 to 50 years Certainty Rates are, generally, in the range of 4.90% to 5.60%.
- We view the markets as having built in, already, nearly all the effects on gilt yields of the likely increases in Bank Rate and the elevated inflation outlook.

3.7 **The balance of risks to the UK economy:**

- The overall balance of risks to economic growth in the UK is to the downside.

3.8 **Downside risks to current forecasts for UK gilt yields and PWLB rates include:**

- **Labour and supply shortages** prove more enduring and disruptive and depress economic activity (accepting that in the near-term this is also an upside risk to inflation and, thus, the rising gilt yields we have seen of late).
- **The Bank of England** increases Bank Rate too fast and too far over the coming months, and subsequently brings about a deeper and longer UK recession 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.
- **A broadening of banking sector fragilities**, which have been successfully addressed in the near-term by central banks and the market generally, but which may require further intervention if short-term interest rates stay elevated for longer than is anticipated.

3.9 **Upside risks to current forecasts for UK gilt yields and PWLB rates:**

- Despite the recent tightening by 0.5%, **the Bank of England proves too timid** in its pace and strength of increases in Bank Rate and, therefore, allows inflationary pressures to remain elevated for a longer period within the UK economy, which then necessitates Bank Rate staying higher for longer than we currently project.
- **The pound weakens** because of a lack of confidence in the UK Government's fiscal policies, resulting in investors pricing in a risk premium for holding UK sovereign debt.
- **Longer-term US treasury yields** rise strongly if inflation remains more stubborn than the market currently anticipates, pulling gilt yields up higher consequently.
- **Projected gilt issuance**, inclusive of natural maturities and quantitative tightening (QT), could be too much for the markets to comfortably digest without higher yields compensating.

4 **Treasury Management Activity**

- 4.1 The overall treasury position as at 30 June 2023 is shown in the table below:

Treasury Position	Financial Year 2023/24 Quarter 1				Financial Year 2022/23 Quarter 4			
	General Fund		HRA		General Fund		HRA	
	£000	%	£000	%	£000	%	£000	%
	as at 30.06.23		as at 30.06.23		as at 31.03.23		as at 31.03.23	
Fixed Rate Funding:								
PWLB	330,975	3.14%	75,494	4.76%	330,975	3.14%	75,494	4.76%
Market (LOBO)	10,942	4.26%	6,558	4.26%	10,942	4.26%	6,558	4.26%
Market (converted LOBOs)	37,517	3.89%	22,483	3.89%	37,517	3.89%	22,483	3.89%
Market (other long-term loans)	40,000	2.33%	0	0%	40,000	2.33%	0	0%
Market (short-term fixed)	140,000	3.98%	0	0%	125,000	2.55%	0	0%
Market (short-term fixed, variable rate)	10,000	5.00%	0	0%	20,000	4.30%	0	0%
Market (short-term variable)	30,000	5.00%	0	0%	30,000	4.25%	0	0%
Salix loans	3,700	0%	0	0%	4,365	0%	0	0%
Sub-total	603,134		104,435		598,799		104,435	
Variable Rate Funding:								
Market (short-term)	20	5.00%	0	0%	20	4.25%	0	0%
Sub-total	20		0		20		0	
Total Debt	603,154	3.45%	104,535	4.54%	598,819	3.10%	104,535	4.54%
Total Investments	57,350	4.65%	0	0%	66,150	4.35%	0	0%
Net Debt	545,804		104,535		532,669		104,535	

Net debt has marginally increased between the start of 2023/24 and the end of Q1, rising from £637.204m to £650.339m. The overall cost of borrowing (GF and HRA) has moved from 3.31% to 3.61% reflecting the increase in short-term borrowing rates between periods.

5 Annual Investment Strategy (AIS)

5.1 The Treasury Management Strategy Statement (TMSS) for 2023/24, which includes the Annual Investment Strategy, was approved by the Council on 23 February 2023. In accordance with the CIPFA Treasury Management Code of Practice, it sets out the Council's investment priorities as being:

- Security of capital
- Liquidity
- Yield

5.2 The Council will aim to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity, aligned with the Council's risk appetite. In the current economic climate, over and above keeping investments short-term to cover cash flow needs, there is a benefit to seek out value available in periods up to 12 months with high credit rated financial institutions, using the Link suggested creditworthiness approach, including a minimum sovereign credit rating and Credit Default Swap (CDS) overlay information.

5.3 As shown by the charts in 5.8 below and the interest rate forecasts in Section 3, investment rates have improved dramatically during the first quarter of 2023/24 and are expected to improve further as Bank Rate continues to increase over the next few months.

5.4 Creditworthiness.

There have been few changes to credit ratings over the quarter under review. However, officers continue to closely monitor these, and other measures of creditworthiness to ensure that only appropriate counterparties are considered for investment purposes.

5.5 Investment counterparty criteria

The current investment counterparty criteria selection approved in the TMSS is meeting the requirement of the treasury management function.

5.6 CDS prices³

For UK banks, these have retreated from the spikes caused by the Truss/Kwarteng policy approach in September 2022. Prices are not misaligned with other creditworthiness indicators, such as credit ratings. Nevertheless, it remains important to undertake continual monitoring of all aspects of risk and return in the current circumstances.

5.7 Investment balances

The average level of funds available for investment purposes during the quarter was £52.653m. These funds were available on a temporary basis, and the level of funds available was mainly dependent on the timing of precept payments, receipt of grants and progress on the capital programme. The Council does not hold core cash balances for investment purposes (i.e., funds available for more than one year).

5.8 The Council uses the Sterling Overnight Index Averages (SONIA) to benchmark its investment returns. There is a choice of using the forward looking (term) benchmarks and the backward-looking benchmarks. The forward-looking benchmark reflects where the market has moved to over time, whereas the Council uses the backward-looking benchmark as this reflects where the market was positioned when investments were placed.

Investment Performance (year to date) quarter ended 30 June 2023 Bank Rate vs backward looking SONIA

	Bank Rate	SONIA	7 day	30 day	90 day	180 day	365 day
High	5.00%	4.93%	4.93%	4.57%	4.38%	4.10%	3.14%
High Date	22.06.23	30.06.23	30.06.23	30.06.23	30.06.23	30.06.23	30.06.23
Low	4.25%	4.18%	4.18%	4.02%	3.81%	3.32%	2.27%
Low Date	03.04.23	04.04.23	11.04.23	03.04.23	03.04.23	03.04.23	03.04.23
Average	4.44%	4.37%	4.34%	4.27%	4.11%	3.74%	2.70%
Spread	0.75%	0.75%	0.75%	0.55%	0.57%	0.78%	0.87%

5.9 The table below illustrates the investment returns achieved during the first quarter of 2023/24 split by time duration.

Q1 2023/24	COUNCIL PERFORMANCE			
		Ave Balance Invested	% Return	Ave Duration (days)
Combined Investments	April 2023	£53.266m	4.35%	61.32
	May 2023	£53.310m	4.41%	44.08

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- ³ A Credit Default Swap (CDS) is a contract between two parties in which one party purchases protection from another party against losses from the default of a borrower for a defined period of time. CDS prices are often quoted in terms of credit spreads, the implied number of basis points that the credit protection seller receives from the credit protection buyer to justify providing the protection. A credit default swap (CDS) is a financial derivative that allows an investor to swap or offset their credit risk with that of another investor. To swap the risk of default, the lender buys a CDS from another investor who agrees to reimburse them if the borrower defaults.
 - Most CDS contracts are maintained via an ongoing premium payment similar to the regular premiums due on an insurance policy. A lender who is worried about a borrower defaulting on a loan often uses a CDS to offset or swap that risk.

Q1 2023/24	COUNCIL PERFORMANCE			
	June 2023	£51.377m	4.52%	27.93
Average Q1		£52.653m	4.42%	44.63

- 5.10 As illustrated in the table above, the Council's return for Q1 has *outperformed* the benchmark in all periods.
- 5.11 The budgeted investment return given in the initial Annual Investment Strategy Report for 2023/24 was 4.40%, assuming an average investment duration of up to three months. (This represents the Council's typical investment duration which is predominantly at the short end of the curve and fairly liquid to cater for cashflow needs). This was based on the interest rate forecast in February 2023 which assumed Bank rate would peak at 4.50% by Q2 2023. Bank rate has risen more quickly and steeply than those initial assumptions and the return for 2023/24 therefore requires revising upwards at this stage in the financial year. This is purely based on current expectations for Bank rate and not an expectation that the Council will place significant investments for longer periods than 3 months later in the year.
- 5.12 As noted in the table in 3.4 above, Link have raised their expectations, and while they do not foresee Bank Rate hitting 6% as the market has predicted, they envisage that Bank Rate will move higher (5.50%) and stay at these elevated levels for longer in light of the more persistent inflation backdrop.
- 5.13 Our suggested budgeted earnings rates have been revised somewhat higher for both 2023/24 and 2024/25 as Bank Rate shifts higher for longer and are set out in the table below.

	Q1 2023/24	TMSS (AIS) 2023/24)
2023/24	5.40%	4.40%
2024/25	4.30%	3.30%
2025/26	2.70%	2.60%
2026/27	2.50%	2.50%
Longer-term	2.80%	2.80%

- 5.14 **Approved limits**
Officers can confirm that the approved limits within the Annual Investment Strategy were not breached during the quarter ended 30 June 2023.

6 **Borrowing**

6.1 **PWLB maturity Certainty Rates 1 April to 30 June 2023**

- 6.1.1 Gilt yields and PWLB rates were on a rising trend between 1 April and 30 June.
- 6.1.2 The 50-year PWLB Certainty Rate target for new long-term borrowing started 2023/24 at 3.30% before increasing to a peak of 3.80% in June. As can be seen, with rates elevated across the whole of the curve, it is prudent to not borrow long-term unless the Council requires certainty of rate and judges the cost to be affordable. (Please also note that from 15 June, HRA borrowing is 0.40% lower than the Certainty Rate)

6.2 **PWLB RATES Q1**

The following table summarises movements in PWLB Certainty rates from 1 year out to 50 years in Q1 2023/24.

PWLB	1 Year	5 Year	10 Year	25 Year	50 Year
Low	4.65%	4.14%	4.20%	4.58%	4.27%
Date	06.04.23	06.04.23	06.04.23	06.04.23	05.04.23
High	6.24%	5.71%	5.28%	5.44%	5.23%
Date	28.06.23	28.06.23	20.06.23	30.05.23	30.05.23
Average	5.32%	4.87%	4.78%	5.09%	4.82%
Spread	1.59%	1.57%	1.08%	0.86%	0.96%

6.3 Revised PWLB Borrowing trigger rates

The table below provides revised PWLB Certainty trigger borrowing rates.

	Q1 2023/24
5 years	3.60%
10 years	3.70%
25 years	4.00%
50 years	3.80%

Please note, the Council has now set trigger rates two years forward from now (this assumes that ideally long-term borrowing will not be taken for the next two years) and so trigger rates look at the forecasts for new PWLB long-term borrowing in 2025. This is because inflation is expected to start to fall throughout the remainder of 2023 and 2024 and therefore long-term rates by 2025 are expected to be lower. Two years forward is when we expect rates to have fallen back, and you will note that trigger levels are therefore way below where borrowing levels currently are.

- 6.4 The long-term (beyond 10 years) forecast for Bank Rate stands at 2.5%. As all PWLB certainty rates are currently significantly above this level, borrowing strategies will need to remain within that context. Overall, better value can generally be obtained at the shorter end of the curve and short-dated fixed LA to LA monies will continue to be the best option. Temporary borrowing rates will remain elevated for some time to come but may prove the best option whilst the market continues to wait for inflation, and therein gilt yields, to drop back later in 2023 and 2024.

7 Debt rescheduling

- 7.1 Debt rescheduling opportunities have increased significantly in the current quarter where gilt yields, which underpin PWLB rates and market loans, have risen materially. Members will be advised if there is value to be had by rescheduling or repaying a part of the debt portfolio.

8 Compliance with Treasury and Prudential Limits

- 8.1 The prudential and treasury Indicators are shown in Appendix 1.
- 8.2 It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. During the quarter ended 30 June 2023, the Council has operated within the treasury and prudential indicators set out in the Council's Treasury Management Strategy Statement for 2023/24. The Deputy Chief Executive (Section 151 Officer) reports that no difficulties are envisaged for the current or future years in complying with these indicators.

- 8.3 All treasury management operations have also been conducted in full compliance with the Council's Treasury Management Practices.

OTHER CONSIDERATIONS

9.1 FINANCIAL AND RISK ASSESSMENT CONSIDERATIONS

- 9.1.1 The financial implications are covered in the body of the report.
- 9.1.2 There are no further financial and risk considerations arising from the report. This report is produced as a finance report and discusses in detail risk mitigation processes which are at the heart of Treasury Management Policy. Treasury Management Risk Management is the practice of planning for unexpected expenditures. It is primarily about mitigating and avoiding the impact of the changing financial environment on the Council's cash flow objectives.
- 9.1.3 It is confirmed that the Deputy Section 151 Officer has signed off the financial implications detailed within the report.

9.2 LEGAL CONSIDERATIONS

- 9.2.1 There are no Legal and Governance implications to consider as a result of the report and recommendations.
- 9.2.2 The Council will ensure that all its treasury management activities comply with its statutory powers and regulatory requirements. In framing its credit and counterparty policy under Treasury Management Practice (TMP1) *Counterparty credit risk management*, it will ensure that there is evidence of counterparties' powers, authority and compliance in respect of the transactions they may effect with the Council, particularly with regard to duty of care and fees charged.
- 9.2.3 The Council recognises that future legislative or regulatory changes may impact on its treasury management activities and, so far as it is reasonably able to do so, will seek to manage the risk of these impacting adversely on the Council.

9.3 HUMAN RESOURCES IMPACT

- 9.3.1 There is no impact to the workforce or the workforce of partner organisations as a result of the report and recommendations.
- 9.3.2 The Council recognises the importance of ensuring that all staff involved in the treasury management function are fully equipped to undertake the duties and responsibilities allocated to them. It will therefore seek to appoint individuals who are both capable and experienced and will provide training for staff to enable them to acquire and maintain an appropriate level of expertise, knowledge and skills.
- 9.3.3 The Council will also ensure that Members tasked with treasury management responsibilities, including those responsible for scrutiny, have access to training relevant to their needs and those responsibilities.

- 9.3.4 The present arrangements, including a knowledge and skills schedule, are detailed in the relevant Treasury Management Practice (TMP). This *Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes* (the TM Code) revision for 2021 introduces strengthened requirements for skills and training.

9.4 EQUALITIES IMPACT

- 9.4.1 A full Equalities Impact Assessment was undertaken with the initial Treasury Management Strategy Report for 2023/24 that went to Council on 23 February 2023. This is a backward-looking performance report on that Strategy.

9.5 ENVIRONMENTAL IMPACT

- 9.5.1 Part of the revisions to the Treasury Management Code in December 2021 that will be incorporated into the Council's Treasury Management Policy Statement and Treasury Management Practices (TMPs), will provide further clarification of the way the Council is looking to incorporate environmental considerations in the Council's Investment Strategy.
- 9.5.2 Environmental, social and governance (ESG) issues are increasingly significant for investors and investment managers. This is better developed in equity and bond markets than for short-term cash deposits and there is a diversity of market approaches to ESG classification and analysis.
- 9.5.3 This means that a consistent and developed approach to ESG for the Council in its treasury management dealings will be challenging. The Council will consider its credit and counterparty policies in light of ESG information and develop ESG investment policies and treasury management practices consistent with the Council's own relevant policies where possible, for example, climate change policies. It is not expected that the Council's ESG policy will include ESG scoring or other real-time ESG criteria at individual investment level.

10 CONCLUSIONS AND RECOMMENDATIONS

- 10.1 The Council's treasury management function has functioned well in Q1 2023/24; investment performance has achieved a return of 4.42% and debt costs have been minimised at an overall rate of 3.61%
- 10.2 During the quarter the Council operated within the treasury limits and Prudential Indicators set out in the Council's Treasury Management Strategy Statement and in compliance with the Council's Treasury Management Practices.
- 10.3 The Council has had as its first priority the security of invested funds and its policy to place appropriate parameters (in terms of credit quality), to organisations with whom it invests. This has safeguarded the Council's investments during Q1 2023/24.
- 10.4 The challenges we foresee for the economy remain broadly that the CPI measure of inflation will need to fall considerably through the remainder of this year and labour market pressures will need to reduce materially to provide any possibility of a loosening in monetary policy. The MPC will have to remain cognisant of not being the unwitting catalyst to a large housing market

correction. The impact of interest rate decisions could have a more sizeable impact on activity as more households face up to an increasingly limited number of (re)mortgage options at likely far greater cost than they have been paying under their current deals.

- 10.5 While the Bank improved its economic outlook in May by the largest amount since it gained independence in 1997, and maintained this view at its June meeting, the impact of higher rates will weigh and there is now increasing talk of a recession in the UK. It seems almost inevitable that the economy will need to move into a negative growth scenario at some point in the next 12 months because the prevailing tight labour market conditions, and high pay demands, are inconsistent with a 2% inflation target. Rates will have to rise.
- 10.6 Regarding forecasts for PWLB rates, investors will likely remain nervous about the impact of inflation until there is unambiguous evidence it is falling materially and consistently. Forecasts are somewhat higher at the short end of the curve, although it is anticipated that gilt yields will fall back in due course once the economy slows and labour markets loosen. Countering this will be the considerable gilt issuance required, with £240bn expected this financial year, while the central bank is also reversing out at least £80bn of quantitative tightening through this period, meaning some investors may not be overly convinced of the merit of buying UK gilts if further inflationary upside surprises emerge over the coming months.
- 10.7 From a Treasury standpoint the Council whilst looking to borrow will, most probably, need to continue to focus on optimising its cashflow forecasts, and given the elevated level of rates right across the curve at present, seek to continue to fund either temporarily from local authorities or possibly with short-dated loans from the PWLB. Members will see from the latest forecast that we still expect both short and longer-term rates to be somewhat lower over the duration of the forecast. Nonetheless, if certainty becomes paramount within the Council's Debt Management Strategy, we will look to optimise any longer dated borrowing requirements, although this is not presently the case whilst short-term markets remain liquid.
- 10.8 The Cabinet is asked to:
- Note the report and treasury activity and approve any changes to the prudential indicators.

BACKGROUND PAPERS

There are none.

Anyone wishing to inspect the above background papers or requiring further information should contact Lorna Soufian

Lorna Soufian on Tel: 0161 474 4026 or by email

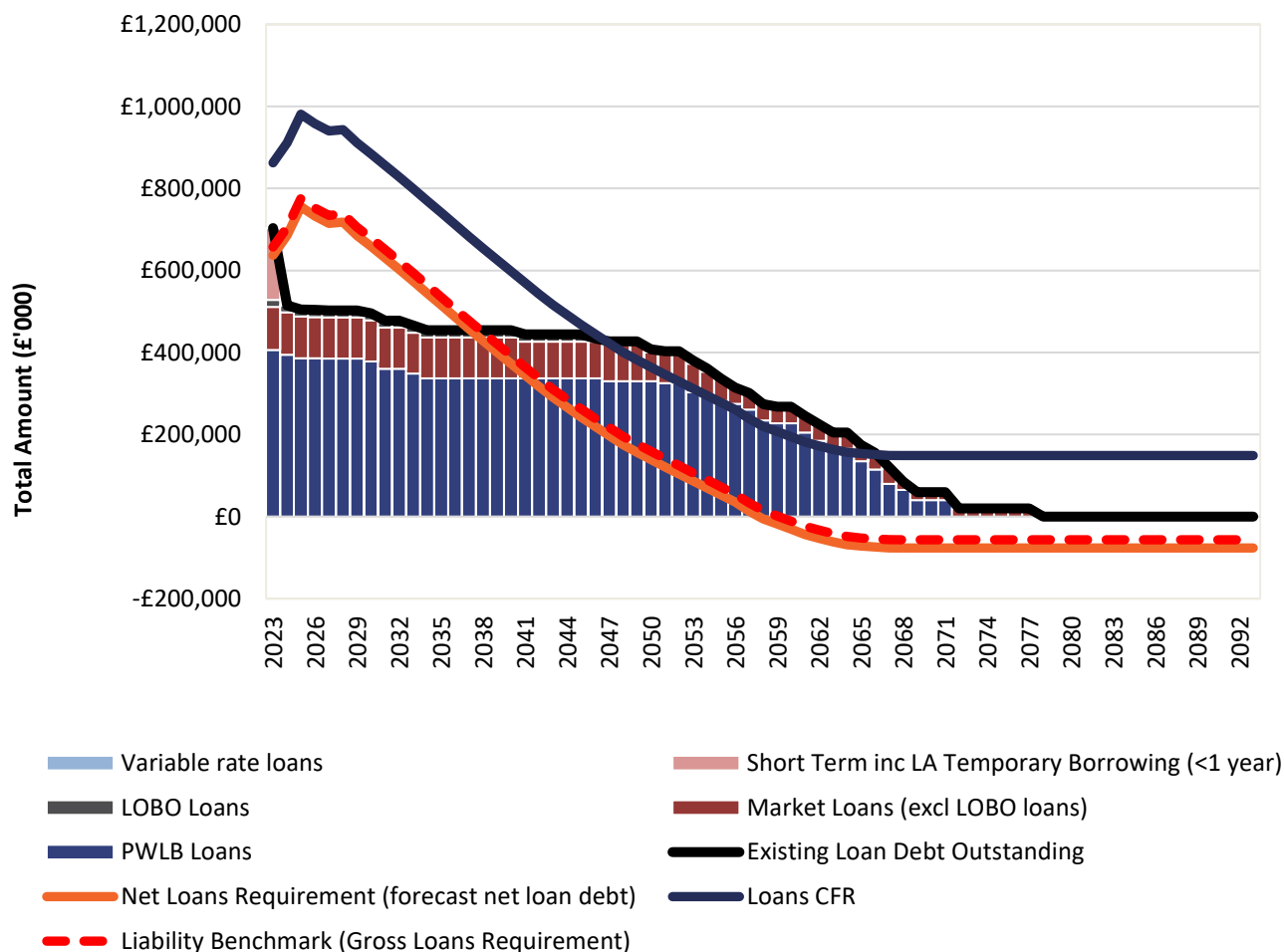
APPENDIX 1

Prudential and Treasury Indicators 2023/24 Q1

Capital Indicators

	Budget 2023/24 £M	Q1 2024/25 £M
Capital expenditure	188.479	169.512
Capital Financing Requirement (CFR)	939.398	911.098
Annual change in CFR	72.658	48,517
In-year borrowing requirement (excluding MRP)	96.777	73.284
Ratio of financing costs to net revenue stream (non HRA)	9.60%	8.76%
Ratio of financing costs to net revenue stream (HRA)	10.76%	10.82%
<i>Incremental impact of capital investment decisions:</i>		
Increase in council tax (band change) per annum	£45.54	£42.35
Increase in average housing rent per week	£1.38	£0.36

Liability Benchmark



Treasury Indicators

	2023/24 Budget £M	2023/24 Q1 £M
Authorised limit for external debt	976.000	976.000
Operational boundary for external debt	956.000	956.000
Gross external debt (maximum Q1)	812.530	721.389

Maturity Structure of fixed rate borrowing upper and lower limits

Period	2023/24 Lower	2023/24 Upper	Actual 30.06.23
Under 12 months	0%	30%	20%
12 months to 2 years	0%	20%	4%
2 years to 5 years	0%	20%	0%
5 years to 10 years	0%	20%	5%
10 years to 20 years	0%	20%	4%
20 years to 30 years	5%	30%	11%
30 years to 40 years	20%	50%	26%
40 years to 50 years	20%	50%	27%
50 years and above	0%	40%	3%

Interest Rate Limits

	2023/24 Budget %	2024/25 Q1 Actual %
Upper limit of variable interest rates based on gross debt	40%	6%

Principal Sums

	2023/24 Budget £M	2024/25 Actual Q1 £M
Upper limit for principal sums invested over 365 days	80	0