REPORT TO:	Executive Board
DATE:	16 November 2023
REPORTING OFFICER:	Operational Director – Finance
PORTFOLIO:	Corporate Services
TITLE:	Treasury Management 2023-24 Half Year Update
WARDS:	Boroughwide

1.0 PURPOSE OF REPORT

1.1 The purpose of this report is to provide an update regarding investment and borrowing activities undertaken during the first half of the financial year to 30 September 2023, as required by the Treasury Management Policy.

2.0 RECOMMENDED: That the report be noted.

3.0 SUPPORTING INFORMATION

Economic Outlook

3.1 The following analysis of the economic situation has been provided by Link Asset Services, the Council's treasury management advisors.

3.2 During the six months ended 30 September 2023

- Interest rates rose by a further 1%, taking the Bank Rate from 4.25% to 5.25% and, possibly, the peak in the cycle.
- Short, medium and long-dated gilts remain elevated as inflation continued at higher levels than forecast.
- There was a 0.5% month on month decline in real GDP in July, mainly due to more strikes.
- CPI inflation fell from 8.7% in April to 6.7% in August, its lowest rate since February 2022, but still the highest in the G7.
- Core CPI inflation reduced to 6.2% in August from 7.1% in April, which had been a 31 year high.
- There was a cooling in labour market conditions, but no evidence yet that it has led to an easing in wage growth.

3.3 The 0.5% month on month fall in GDP in July suggests that underlying growth has lost momentum since earlier in the year. Some of the weakness in July was due to there being almost twice as many working days lost to strikes in July (281,000) than in June (160,000).

3.4 The 0.4% month on month rebound in retail sales volumes in August is not as good as it looks as it partly reflected a pickup in sales after the unusually wet weather in July. Sales volumes in August were 0.2% below their level in May, suggesting much of the resilience in retail activity in the first half of the year has faded.

3.5 As the growing drag from higher interest rates intensifies over the next six months, we think the economy will continue to lose momentum and soon fall into a mild recession. Strong labour demand, fast wage growth and Government handouts have all supported household incomes over the past year. With CPI inflation past its peak and expected to decline further, the economy has got through the cost-of-living crisis without recession. But even though the worst of the falls in real household disposable incomes are behind us, the phasing out of financial support packages provided by the Government during the energy crisis means real incomes are unlikely to grow strongly. Higher interest rates will soon bite harder too. We expect the Bank of England to keep interest rates at the probable peak of 5.25% until the second half of 2024. Mortgage rates are likely to stay above 5.0% for around a year.

3.6 The tightness of the labour market continued to ease, with employment in the three months to July falling by 207,000. The further decline in the number of job vacancies from 1.017m in July to 0.989m in August suggests that the labour market has loosened a bit further since July though the supply of labour is still 0.3% below its pre-pandemic February 2020 level.

3.7 CPI inflation declined from 6.8% in July to 6.7% in August, the lowest rate since February 2022. The biggest positive surprise was the drop in core CPI inflation, which declined from 6.9% to 6.2%. That reverses all the rise since March and means the gap between the UK and elsewhere has shrunk (US core inflation is 4.4% and in the Euro-zone it is 5.3%).

3.8 In its latest monetary policy meeting on 20 September, the Bank of England left interest rates unchanged at 5.25%. The weak August CPI inflation release, the recent loosening in the labour market and the downbeat activity surveys appear to have convinced the Bank of England that it has already raised rates far enough.

3.9 The yield on 10-year Gilts fell from a peak of 4.74% on 17th August to 4.44% on 29th September, mainly on the back of investors revising down their interest rate expectations. But even after their recent pullback, the rise in Gilt yields has exceeded the rise in most other Developed Market government yields since the start of the year. Looking forward, once inflation falls back, Gilt yields are set to reduce further. A (mild) recession over the next couple of quarters will support this outlook if it helps to loosen the labour market (higher unemployment/lower wage increases).

3.10 The pound weakened from its cycle high of $1.30 in the middle of July to $1.21 in late September. In the first half of the year, the pound bounced back strongly from the Truss led Government last Autumn. That rebound was in large part driven by the substantial shift up in UK interest rate expectations. However, over the past couple of months, interest rate expectations have dropped sharply as inflation started to come down, growth faltered, and the Bank of England called an end to its hiking cycle.

3.11 The FTSE 100 has gained more than 2% since the end of August, from around 7,440 on 31st August to 7,608 on 29th September. The rebound has been primarily driven by higher energy prices which boosted the valuations of energy companies. The FTSE 100's relatively high concentration of energy companies helps to explain why UK equities outperformed both US and Euro-zone equities in September. Nonetheless, as recently as 21st April the FTSE 100 stood at 7,914

Interest Rate Forecast

3.12 The following interest rate forecast has been provided by Link Asset Services.

Link Group Interest Rate View	25.09.23												
	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26
BANK RATE	5.25	5.25	5.25	5.00	4.50	4.00	3.50	3.00	2.75	2.75	2.75	2.75	2.75
3 month ave earnings	5.30	5.30	5.30	5.00	4.50	4.00	3.50	3.00	2.80	2.80	2.80	2.80	2.80
6 month ave earnings	5.60	5.50	5.40	5.10	4.60	4.10	3.60	3.10	2.90	2.90	2.90	2.90	2.90
12 month ave earnings	5.80	5.70	5.50	5.20	4.70	4.20	3.70	3.20	3.00	3.00	3.00	3.00	3.00
5 yr PWLB	5.10	5.00	4.90	4.70	4.40	4.20	4.00	3.90	3.70	3.70	3.60	3.60	3.50
10 yr PWLB	5.00	4.90	4.80	4.60	4.40	4.20	4.00	3.80	3.70	3.60	3.60	3.50	3.50
25 yr PWLB	5.40	5.20	5.10	4.90	4.70	4.40	4.30	4.10	4.00	3.90	3.80	3.80	3.80
50 yr PWLB	5.20	5.00	4.90	4.70	4.50	4.20	4.10	3.90	3.80	3.70	3.60	3.60	3.60

Short Term Borrowing Rates

3.13 The bank base rate has increased steadily from 4.25% on 31st March to 5.25% on 30th September 2023.

	Mar	Apr	May	Jun	Jul	Aug	Sep
	%	%	%	%	%	%	%
Base Rate	4.25	4.25	4.50	5.00	5.00	5.25	5.25
Call Money (Market)	4.15	4.15	4.40	4.90	4.90	5.20	5.15
1 Month (Market)	4.25	4.35	4.65	4.95	5.30	5.30	5.25
3 Month (Market)	4.45	4.70	5.00	5.40	5.50	5.55	5.55

Longer Term Borrowing Rates

	Mar	Apr	May	Jun	Jul	Aug	Sep
	%	%	%	%	%	%	%
1 Year (Market)	4.85	5.15	5.55	6.40	6.05	6.10	5.80
10 Year (PWLB)	4.35	4.55	4.97	5.25	5.14	5.19	5.28
25 Year (PWLB)	4.70	4.90	5.29	5.33	5.33	5.44	5.66

3.14 Market rates are based on suggested rates provided by Link Asset Services. The PWLB rate shown is the Fixed Term Certainty Rate for a new loan with the principal repayable on maturity.

Borrowing and Investments

Turnover during the period

	No of deals	Turnover £m
Short Term Borrowing	2	10
Short Term Investments	15	155

Position at month-end

	Mar £m	Apr £m	May £m	Jun £m	Jul £m	Aug £m	Sep £m
Total Borrowing	187	182	182	182	182	182	182
Total Investments	(92)	(82)	(112)	(117)	(117)	(117)	(112)
Call Account Balance	(10)	(12)	(22)	(17)	(13)	(9)	(12)

Investment benchmarking

Benchmark	Benchmark Return %	Performance Apr - Sep %	Investment Interest Earned £000
7 day	4.72	3.06	287
1 month	4.86	4.61	56
3 months	5.16	4.86	602
6 months	5.44	4.66	698
12 months	5.70	4.84	336
Over 12 months	-	2.55	339
Property Fund	-	3.94	197
Total			**2,515**

3.15 The above table shows the Council has underachieved on all benchmarks over the first six months of the year. This is due to two reasons. Firstly, that the Council only uses institutions with a very high credit quality, and secondly that the above figures show the interest earned over the last six months, whereas the benchmarks are based on new investments. In a rising rate environment this will cause a lag in the interest rates received, especially for longer duration investments. There are no benchmarks available for the Council's investment in the CCLA property fund, or for investments held over 12 months.

Budget Monitoring

	Net Interest at 30th September 2023		
	Budget to Date £000	**Actual to Date £000**	**Variance (o/spend) £000**
Investments	(1,778)	(2,515)	737
Borrowings	550	550	-
Net Total	**(1,229)**	**(1,966)**	**737**

3.16 Due to the increase in interest rates during the period and larger than expected investment balances, the Council has generated an additional £737,000 net income over budget in the first half of the year from its treasury management activities. This is expected to increase further in the second half of the year, due to the investments balance continuing to be available.

New Long-Term Borrowing

3.17 No new long-term borrowing has been taken in this period.

Policy Guidelines

3.18 The Treasury Management Strategy Statement (TMSS) for 2023/24, which includes the Annual Investment Strategy, was approved by Council on 08 March 2023. It sets out the Council's investment priorities as being:

- Security of capital
- Liquidity
- Yield

3.19 The Council will therefore aim to achieve the optimum return (yield) on investments commensurate with proper levels of security and liquidity. In the current economic climate and the heightened credit concerns it is considered appropriate to keep the majority of investments short term and to ensure all investments are in in line with Sector's credit rating methodology.

Treasury Management Indicators

3.20 It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. The Council's approved Treasury and Prudential Indicators were set out in the Treasury Management Strategy Statement and are reviewed in Appendix 1.

Debt Rescheduling

3.21 No debt rescheduling was undertaken during the quarter.

4.0 POLICY IMPLICATIONS

4.1 None.

5.0 FINANCIAL IMPLICATIONS

5.1 The financial implications are as set out in the report.

6.0 IMPLICATIONS FOR THE COUNCIL'S PRIORITIES

6.1 There are no direct implications, however, the revenue budget and capital programme support the delivery and achievement of all the Council's priorities.

7.0 RISK ANALYSIS

7.1 The main risks with Treasury Management are security of investment and volatility of return. To mitigate these, the Council operates within a clearly defined Treasury Management Policy and annual borrowing and investment strategy, which sets out the control framework.

8.0 EQUALITY AND DIVERSITY ISSUES

8.1 None.

9.0 CLIMATE CHANGE IMPLICATIONS

9.1 None

10.0 LIST OF BACKGROUND PAPERS UNDER SECTION 100D OF THE LOCAL GOVERNMENT ACT 1972

10.1 There are no background papers under the meaning of the Act.

Appendix 1

Treasury and Prudential Indicators – 2023/24 – Quarter 2

	2022/23	2023/24	
Prudential Indicators	**Full Year Actual £000**	**Original Estimate £000**	**Quarter 2 Estimate £000**
Capital Expenditure	26,761	50,230	79,898
Net Financing Need for the Year *(Borrowing Requirement)*	7,311	19,719	37,856
Increase / (Decrease) in CFR *(Capital Financing Requirement)*	(2,412)	8,090	20,126
Ratio of Financing Costs to Net Revenue Stream *(Proportion of cost of borrowing to Council's net revenue)*	5.8%	4.4%	3.3%
External Debt *(Borrowing plus PFI and lease liabilities)*	540,350	517,713	527,713
Operational Boundary *(Limit of which external debit is not epected to exceed)*	559,675	552,679	552,679
Authorised Limit *(Limit beyound which external debit is prohibited)*	630,824	627,133	627,133

Maximum Principal invested > 365 days	**Investment Limit £000**	**2022/23 Actual £000**	**2023/24 Estimate £000**
Principal Sums Invested over 365 days	40,000	26,700	25,000