Cabinet

9 November 2023

Treasury Management Half Year Monitoring Report

Recommendation

That Cabinet receives and comments upon the update on Treasury Management activity and performance in respect of the first 6 months of the 2023/24 financial year.

1. Executive Summary

1.1 The CIPFA (Chartered Institute of Public Finance and Accountancy) Code of Practice for Treasury Management 2021 recommends that members be updated on treasury management activities at least quarterly.

1.2 Treasury activity has previously been reported half-yearly and at year end to Cabinet, and this will continue. Quarterly reporting to Resources and Fire and Rescue Overview and Scrutiny Committee has also been introduced this year and provides additional opportunity for oversight and assurance regarding this aspect of the Council's financial activities. In this way the Council meets best practice in accordance with the Code.

1.3 The Treasury Management Strategy sets out that Council delegates to Cabinet responsibility for receiving and reviewing monitoring reports and acting on recommendations in respect of treasury management activity.

1.4 The first quarterly report for this financial year was considered at the quarterly Resources and Fire & Rescue Overview and Scrutiny Committee meeting held on 13 September 2023. This half year report will, following this Cabinet meeting, be taken to the Overview and Scrutiny Committee's next meeting in December.

1.5 This mid-year report has been prepared in compliance with CIPFA's Code of Practice on Treasury Management, and includes coverage of the following:

i.) A review of the Treasury Management Strategy Statement

ii.) A review of the Council's investment portfolio for 2023/24 (Section 2);

iii.) A review of the Council's borrowing strategy for 2023/24, including comments on any debt rescheduling undertaken during 2023/24 (Section 3);

iv.) The Council’s capital expenditure, as set out in the Capital Strategy, and prudential indicators (Appendix 2 of this report);

v.) An economic update for the first half of the 2023/24 financial year (Appendix 3).

1.6 The following highlights are detailed in this report:

i.) Total borrowings reduced by £49 million following a decision to repay six Public Works Loan Board (PWLB) loans early. This early repayment makes the borrowing position more efficient.

ii.) A debt early settlement discount of £1.9 million was gained on the early settlement of the six PWLB loans. In line with accounting standards the gain will be spread over the next 10 years with £193,000 being recognized in the revenue account each year and is included as part of the emerging 2024/25 budget position.

iii.) Total treasury investments were £391m on 30 September 2023 compared to the opening balance on 1 April 2023 of £457m, a reduction of £66m largely due to the early repayment of the £49m PWLB debt towards the end of the first quarter.

iv.) Liquid funds (*funds that can be accessed very quickly*) decreased by £50m. Again, the reduction was largely due to the debt early settlement.

v.) Investments on fixed maturity terms increased by £30m reflecting our first ever investments in the Housing Association sector, and divestments from a Santander bank deposit fund and a BlackRock variable net asset value investment.

vi.) Interest rates continued to move upwards during the greater part of the half year in response to high inflation and an increasing Bank of England (BOE) base rate which rose by 100bps from 4.25% to 5.25%. The Bank had consecutively raised the rate in the past fourteen monetary policy meetings, with the exception of the 20 September meeting where they left the rate unchanged at 5.25%.

vii.) Interest income on treasury investments of £8.89m was recorded during the six months, against a budget of £1.8m. Whilst these significant additional returns are welcomed in the context of the wider council budget, there needs to be a degree of caution around how this influences the budget setting for returns, which are influenced by the level of cash available, interest rates and need for external borrowing.

viii.) The option in the approved Treasury Management Strategy to explore paying a three year £104m pension prepayment was not taken in light of the outlook for interest rates in March 2023.

ix.) The Treasury team have continued to ensure they are up to date with developments in the sector, including undertaking formal technical training from CIPFA, and receiving market updates and briefings from third parties.

2. Annual Investment Strategy

2.1 The Treasury Management Strategy Statement (TMSS) for 2023/24, which includes the Annual Investment Strategy, was approved by the Council on 7 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; and
- yield.

2.2 The Council's aim is to achieve the optimum return (yield) on its investments commensurate with proper and prudent levels of security and liquidity, aligned with the Council's risk appetite. This is in-line with the CIPFA Prudential Code, which governs our Treasury Management activity. In the current economic climate, over and above keeping investments short-term to cover cash flow needs, we are looking to achieve this by seeking out the value available from investing in periods up to 36 months with high credit rated financial institutions.

2.3 The Council has an investment portfolio funded by reserves and cash arising from daily receipts being more than payments on a short-term basis.

Investment balances

2.4 The average level of funds available for investment purposes during the half year was **£430m**. 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.

2.5 Total investments balance reduced by £67m from the £457m at the end of the last financial year to £391m on 30 September 2023, mainly because of the amount applied towards the early settlement of the £49m PWLB loans. Over 70% (£272m) of the total treasury investments were managed in-house through fixed term lending to local authorities, housing associations and local building societies, while 26% (£102m) was externally managed through money market funds and special purpose variable net asset value funds. The remainder, 4% (£17m) was held in a call account with the Council's main bank as a reserve liquidity fund.

Table 1 Investment Balances movements during the half year

Investment Type in £ Millions	Balance at 31 March 2023	Movement during H1	Balance at 30 September 2023
Building Society Loans	50	0	50
Housing Association Loans	0	30	30
Local Authority Loans	200	-8	192
Bank Deposits	38	-21	17
Managed In House	**288**	**1**	**289**
Money Market Funds	112	-50	63
VNAV Funds	57	-18	39
Externally Managed	**169**	**-68**	**102**
Total Funds	**457**	**-67**	**391**

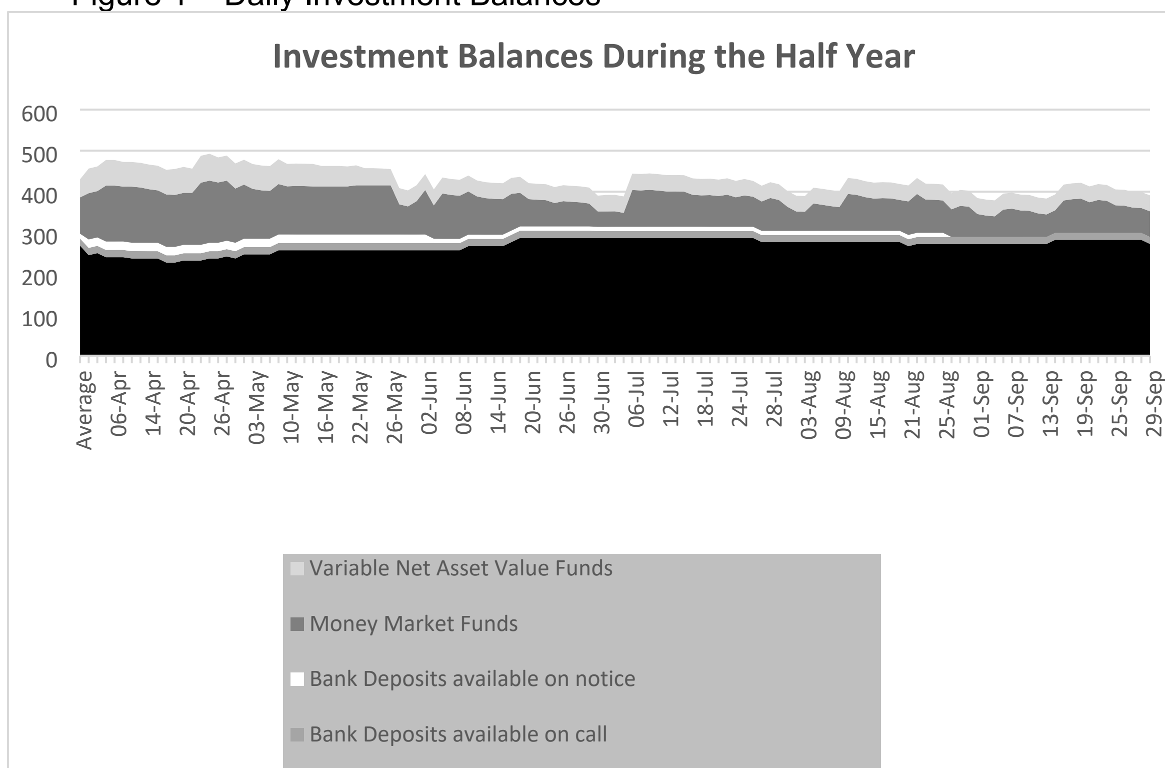
2.6 **Total liquid funds** (bank balances plus money market funds) reduced from £150m at the beginning of the financial year to £80m on 30 September 2023. The high liquidity at the beginning of the financial year had been planned to cover the potential pension fund prepayment which, was not ultimately proceeded with (see paragraphs 2.23 and 2.24).

2.7 As depicted in the chart below, all other investment types slightly reduced except for the investments in fixed deposits with local authorities, housing associations and building societies which increased from £250m at the end of last financial year to £272m at the end of the half year. The decision to increase the fixed deposits category was anchored on locking in the current high interest rates longer to limit the investment portfolio's exposure to downward repricing of interest rates expected when inflation and the base rate begin to fall in near medium term.

2.8 Throughout the half year we have maintained about £17m in a call account with the Council's main bank as a reserve instant access account in case we experience any technical issues with withdrawals from the liquid money market funds or emergency payments that need to be made after the cut off time for withdrawing from money market fund pools. This ensures the Council will always have cash to meet its statutory duties regardless of system malfunctioning or delays at the money market trading platform.

2.9 Also salient on this investment balances chart is the discontinuation of the white area in the middle of the chart representing bank deposits available on notice following the divestment from two notice deposit accounts due to the lower-than-average interest rates the bank was paying.

Figure 1 – Daily Investment Balances



Creditworthiness

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

2.11 The Council uses Fitch, Standard & Poors (S&P) and Moodys ratings to assess the creditworthiness of Treasury investment counterparties. A creditworthiness ratings table can be found in Appendix 4.

2.12 As stipulated in the Treasury Management Strategy, investments have been made in either UK based banks, rated building societies with a minimum of A- Fitch credit rating, and UK local authorities. As at 31 August all the four building societies we have investment balances with were rated A- while four money market funds were rated AAA and two were rated AA- and A1, respectively.

2.13 While a number of local authorities have issued Section 114 notices and many others are reported to be facing serious financial challenges, the sector generally remains a relatively safe investment destination due to statutory protection. Where a loan is made to a UK local authority, the lender is provided with a statutory protection via the Local Government Act 2003. It means that all money borrowed by a local authority, together with any interest on the money borrowed, shall be charged, on all the revenues of the authority. There are only a small number of local authorities that have a formal credit rating, so all lenders will rely on this statutory protection when they arrange any loans with a UK based local authority. The CIPFA Code of Practice on Local Authority

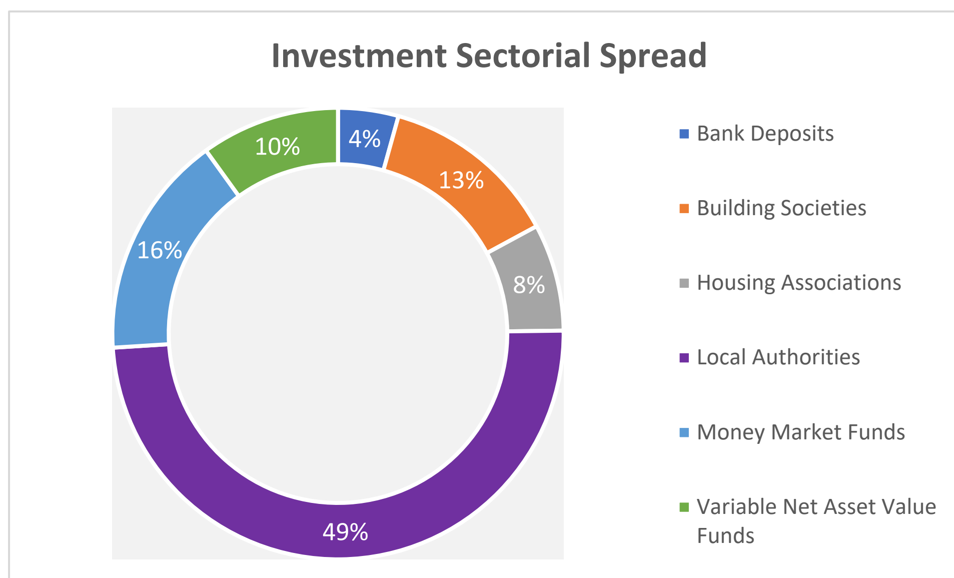
Accounting also includes wording to support this view, as they say "Local authorities shall not recognise a loss allowance for expected credit losses on a financial asset where the counterparty for a financial asset is central government or a local authority for which relevant statutory provision prevents default."

2.14 Despite the cover provided in paragraph 2.13, the Council still endeavours to invest with local authorities that have good financial standing. Several financial checks are completed before entering into a loan agreement. The Council does not lend to other local authorities that have recently issued Section 114 notices, capitalisation notices or have been identified publicly as financially struggling. The current local authority investment portfolio does not include any Councils who have issued these notices.

Investment Counterparty Criteria

2.15 As set out in the approved 2023/24 Treasury Management Strategy, we have continued to prioritize security and liquidity with yields being considered within these two parameters. The approach resulted in the Council's treasury investments being spread across diverse sectors which exhibit strong security and liquidity features. The graph below (*Figure 1*) illustrates which sectors and in what proportions where the treasury funds were invested as of 30 September 2023:

Figure 2 – Investments Sectorial Spread

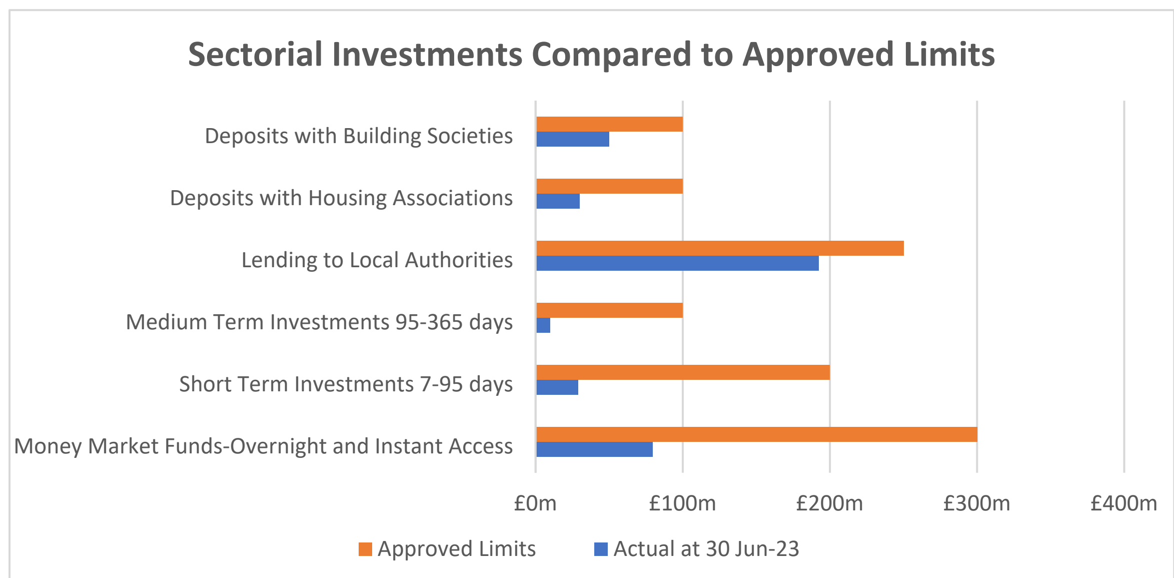


2.16 Local authorities, housing associations and building societies together held 70% of the Council's treasury funds on fixed term loans with varying durations of up to January 2026. Investments held with local authorities alone amounted to £192m equivalent to 49% of the total investment portfolio. As pointed out above, investments in local authorities remain the safest investments, regardless of the increasing financial pressures in the sector, due to the statutory protection.

2.17 While the investment counterparty criteria selection included Housing Associations, we had not invested in any housing association until the first quarter when we placed three fixed term loan investments with three different housing associations worth £30m. This expansion is increasing the range of viable investment options open to us and reduces the investment concentration risk profile.

2.18 The counterparty and sectoral total investments were all within the limits set in the Treasury Management Strategy approved by the Council. The graph below (*Figure 3*) illustrates how the sectorial exposures compared to the approved sector limits:

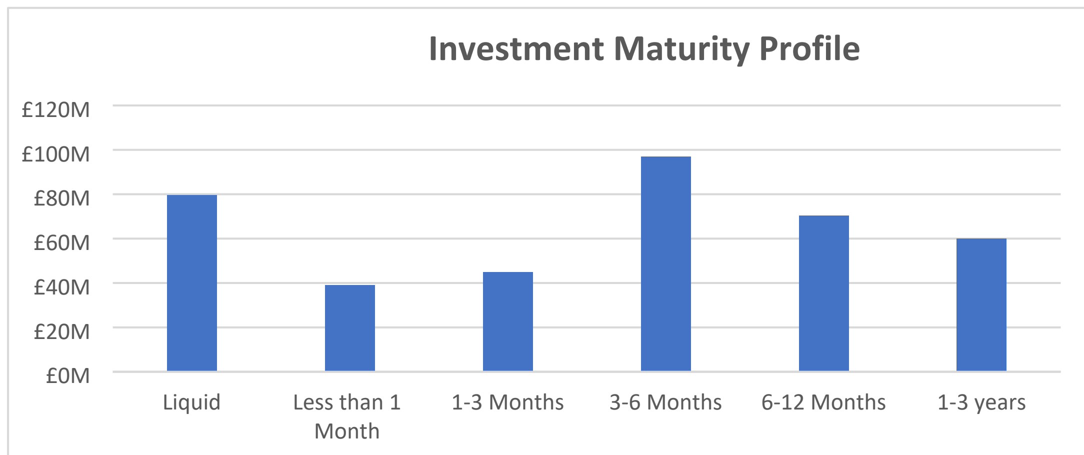
Figure 3 – Sectorial Investments Compared to Approved Limits



Investments Maturity Profile

2.19 With the bulk of the investment funds being held for financing the Council's capital programme, the maturity profile of the investments depicted in the chart below tended to lean mostly to the short-term, with 85% of maturing within twelve months and only 15% maturing over 12 months. This is also in line with the prevailing market where borrowers and funds are reluctant to commit to long term securities as they will be tied to expensive debt/deposits when the long-term market expectation is that interest rates will begin to fall in the medium-term as inflation declines. The chart below illustrates the maturity profile of the investments at the end of the quarter:

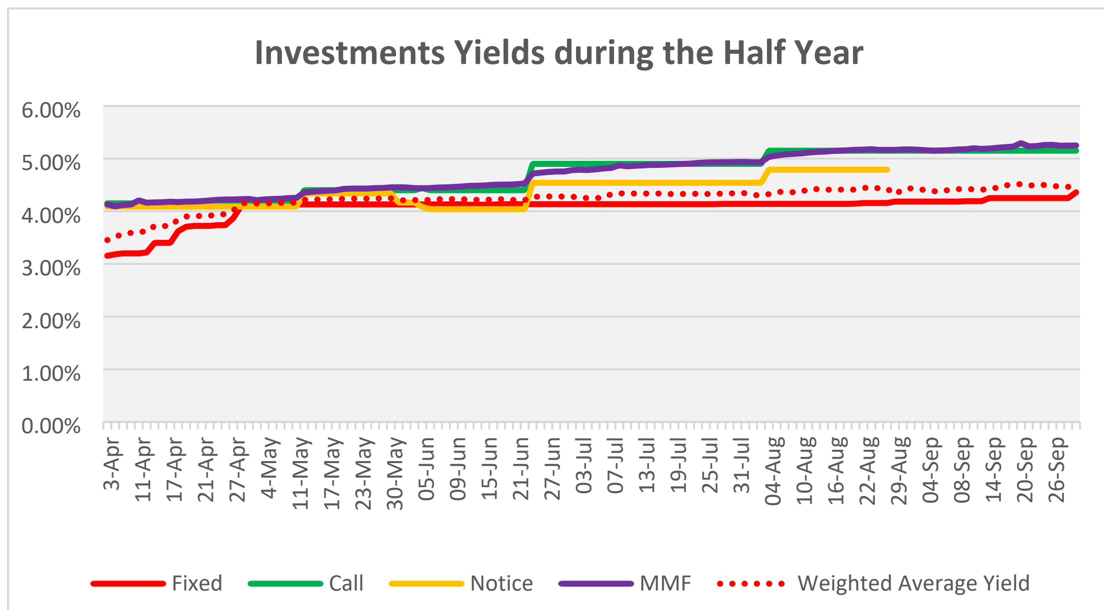
Figure 4 – Investment Maturity Profile



Investment Yield

2.20 During the period market interest rates continued with the upward trend that started during the last months of the pandemic and continued to rise further due to subsequent global and national political and economic events. The Council's treasury investment yields followed this pattern with the maturing and liquid funds being reinvested at improving interest rates. However, a few long-dated fixed deposits that were placed during the low interest era and are yet to mature, slowed down the upward trend of the portfolio yield as illustrated in the following graph where the solid red line reflects the lagging average yield from fixed deposits. All of these fixed term investments had repriced by the end of the first quarter leading to an average fixed investment interest rate of 4.36% compared to 3.15% at end of last financial year and 0.46% at June 2022.

Figure 5 – Investment Yield during the Half Year



2.21 The increasing interest rates referred to above, together with adjustments to the mix of investments, resulted in treasury activities outperforming the budget after recording total income of £8.89m compared to a half-year budget of £1.8m. The interest income budget for the year was set up before the increase in interest rates.

2.22 The recorded £8.89m interest income represents an annualized yield of 4.13% on an average investment portfolio of £430m. The Treasury activities income was earned on investments that are managed inhouse and externally managed as shown in the table below:

First Half Year Investment Yields	Yield in £'000s	Budget HY	Yield in %	Relevant Benchmark
Managed In House	**6,089**	**1,479**	**4.10%**	**3.74%**
Money Market Funds	2,168		4.89%	4.37%
Variable Net Asset Value Funds	632		2.86%	2.83%
Externally Managed	**2,800**	**861**	**4.22%**	
Total Funds	**8,889**	**2,341**	**4.13%**	

2.23 It is positive to highlight that all the yields surpassed the relevant benchmarks.

Pension Early Payment

2.24 The 2023/24 Treasury Management Strategy included an option to pay the Council's 3year pension fund contributions for the valuation period 2023/24 to 2025/26 in one lump sum at the start of the valuation period, with the preference being to do this in April 2023. This would have resulted in the Council being given a discount of £6m compared to cash payments made at normal monthly intervals. In anticipation of this potential decision, and in order to act in a timely fashion, the Treasury Management Team maintained a larger amount of investments in more liquid money market funds a few weeks before year end through to early April.

2.25 Following exploration of the business case for the prepayment, the section 151 officer (Executive Director for Resources), in consultation with the Pensions and Finance teams, took a decision to not make the prepayment. Given interest rates on mainstream investments had continued to rise, the business case highlighted that an equivalent return could be delivered through core Treasury Management activity, with the added benefit of funds being more accessible than being locked away for three years by the pensions prepayment approach.

2.26 The business case indicated that not making the early payment would result in an expected net yield of 4.4% over three years compared to the 4% yield for the early payment option. Following the decision, the cash has been invested with local authorities, housing associations, and building societies at rates that are actually earning more than the prepayment discount would have delivered, further justifying the decision.

2.27 The annual saving of £500,000 included in the Medium-Term Financial Strategy predicated on making the Pension Fund early payment is therefore still being delivered, albeit through Treasury.

3. Borrowing

3.1 Total borrowing stood at £272m at 30 September 2023, compared to £321m at the start of the financial year on 1 April 2023. The reduction was due to the early repayment of six loans. No new borrowing was undertaken during the half year ended 30th September 2023. It is anticipated that no new borrowing will be undertaken during the remainder of this fiscal year.

3.2 While no new loans were drawn, due to market conditions around interest rates and gilt yield the Council was able to take the opportunity to repay prematurely some of our debt. Normally the Council faces repayment penalties that prevents repayment, however, conditions shifted to enable a £1.9m repayment discount. The discount arises due to the Public Works Loan Board (PWLB) being able to re-lend the funds at interest rates higher than the loans the Council holds, so the discount incentivises Councils to repay early.

3.3 The table below summarizes the loan early settlement transaction:

PWLB Early Repayment	GBP
Total Principal to be repaid	49,000,000
Discount	1,925,404
Net Payment after discount	**47,074,596**
Accrued interest to be repaid	315,956
Total Repayment	**47,390,552**

3.4 Another factor in the debt early repayment decision was that this reduced our over-borrowed position, moving the debt more towards our liability benchmark. The decision also reduced peak exposure to debt in loan repayments in future years (this can be seen in Appendix 1, Graph 3), which will allows the Council to re-profile this exposure more effectively as we take out future debt to finance our capital programme, thereby delivering on one of the borrowing objectives set out in the 2023/24 Treasury Management Strategy.

3.5 The only other borrowing activities related to interest payments made to PWLB which is done every half year and we can confirm that the interest payments that fell due at the end of the half year were paid on time. The early settlement of the £49m debt resulted in the September debt interest bill reducing to £6.97m compared to £8m that was incurred last financial year during the first half of that year.

Debt Rescheduling

3.6 Debt rescheduling opportunities have increased significantly in the period where gilt yields, which underpin PWLB rates and market loans, have risen materially. However, during the half year under review, no viable opportunity was identified to reschedule the Council's PWLB debt.

PWLB maturity certainty rates (gilts plus 80bps) year to date to 29 September 2023

3.7 Gilt yields and PWLB certainty rates were on a generally rising trend throughout the first half of 2023/24. At the beginning of April, the 5-year rate was the cheapest and touched 4.14% whilst the 25-year rate was relatively expensive at 4.58%.

3.8 July saw short-dated rates peak at their most expensive. The 1-year rate spiked to 6.36% and the 5-year rate to 5.93%. Although, in due course, short-dated rate expectations fell, the medium dates shifted higher through August and the 10-year rate pushed higher to 5.51% and the 25-year rate to 5.73%. The 50-year rate was 4.27% on 5 April but rose to 5.45% on 28th September. It is expected that rates will fall back over the next two to three years as inflation dampens. The CPI (Consumer Price Index) measure of inflation is expected to fall below 2% in the second half of 2024, and we forecast 50-year rates to stand at 3.90% by the end of September 2025.

HIGH / LOW / AVERAGE PWLB RATES FOR 01/04/23 – 29/09/23

	1 Year	5 Year	10 Year	25 Year	50 Year
Low	4.65%	4.14%	4.20%	4.58%	4.27%
Date	06/04/2023	06/04/2023	06/04/2023	06/04/2023	05/04/2023
High	6.36%	5.93%	5.51%	5.73%	5.45%
Date	06/07/2023	07/07/2023	22/08/2023	17/08/2023	28/09/2023
Average	5.62%	5.16%	5.01%	5.29%	5.00%
Spread	1.71%	1.79%	1.31%	1.15%	1.18%

3.9 The current PWLB rates are set as margins over gilt yields as follows: -.

- **PWLB Standard Rate** is gilt plus 100 basis points (G+100bps)
- **PWLB Certainty Rate (GF)** is gilt plus 80 basis points (G+80bps)
- **PWLB Local Infrastructure Rate** is gilt plus 60 basis points (G+60bps)
- **PWLB Certainty Rate (HRA)** is gilt plus 40bps (G+40bps)

3.10 The **UK Infrastructure Bank** will lend to local authorities that meet its scheme criteria at a rate currently set at gilt plus 40bps (G+40bps).

4. Liability Benchmark

4.1 The purpose of this prudential indicator is to compare the authority's existing loans outstanding against a standardised assessment of need for external loan

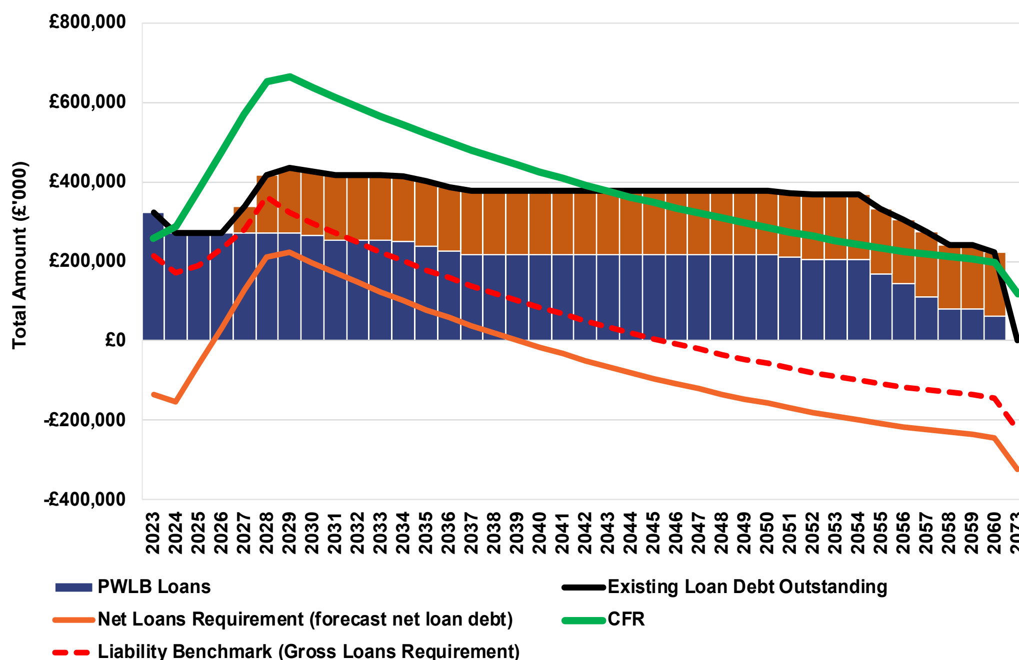
debt, called the liability benchmark. The benchmark reflects the borrowing required to finance capital spending but taking into account any ability to make use of cash balances instead of borrowing externally and taking account of the need to hold a certain amount of cash liquidity. If the existing external loans outstanding are below the debt required, the authority will potentially need to borrow to meet the shortfall. If the existing external loans outstanding are more than it needs, the resulting excess cash may need to be invested. The chart therefore provides insight to an authority on how much it needs to borrow, when, and to what maturities to match its planned borrowing needs.

4.2 The liability benchmark makes no assumptions about the level of future prudential borrowing beyond the horizon of the 5year Medium Term Financial Strategy and so the Capital Financing Requirement (CFR) and the liability benchmark tail off in the chart below, when in reality a rolling programme of new capital expenditure will be approved over time and the CFR will not reduce.

4.3 The liability benchmark is the lowest level of borrowing compared to the CFR borrowing requirement – borrowing only when reserves reach a set minimum level. This assumes that internal resources such as reserves and working capital are utilised and that cash and investment balances are reduced gradually over time.

4.4 The chart below shows how the recent repayment of debt has reduced external debt (the black line) and brought it closer to the benchmark (the dotted red line). Then as capital spending increases over the next few years and the Council utilises its reserves rather than borrowing more, the gap reduces further until the Council does start borrowing externally again (where the brown bars appear in 2027).

4.5 The cash liquidity buffer is reflected in the gap between the dotted red line (the liability benchmark) and the solid orange line (the net loans requirement). This buffer is set at £350m in the current year hence the large gap, but the buffer is planned to be brought down to £100m over time, representing a more efficient use of balance sheet resources, and this shows as a reduced gap between these two lines.



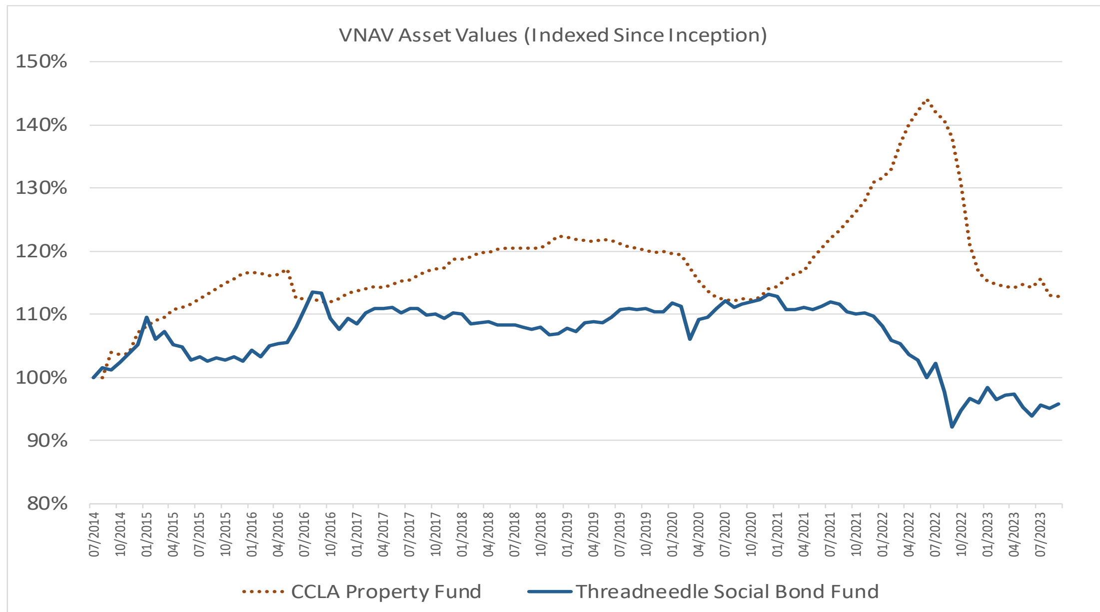
5. Variable Net Asset Value (VNAV) Investments

5.1 As noted earlier in the report, included in the treasury investments is £39m invested in variable net asset value investments as at 30 September 2023. These are investments that are traded in a way like listed stock where the value of the assets held vary up and down dependent on the performance of the funds. At the beginning of the 2023/24 financial year the Council had investments in three separate funds namely, the Threadneedle Social Bond Fund, CCLA Local Authority Property Fund and the BlackRock ICS Sterling Liquid Environmentally Aware Fund. During the first quarter, a decision was made to divest from the BlackRock fund and divert funds to fixed deposits where higher returns were prevailing. The remaining two funds have consistently paid good dividends.

5.2 During the half year, the three funds earned £0.632m in income, equivalent to 2.86% yield on the average investment balance of £44m held during the period.

5.3 The two remaining funds gained in value during the period of prevailing low interest rates, as shown in the graph below. However, both funds have experienced volatility driven by Covid followed by a period of stabilization.

5.4 Treasury officers are reviewing the balances on these funds in light of prevailing market conditions.



6. Non-Treasury Investments

6.1 In addition to managing the Council's treasury investments and borrowings, the Treasury officers are also responsible for managing other non-treasury investments, undertaken in pursuit of achieving the Council's economic, commercial, and social objectives. Among the ongoing non-treasury investments that the Treasury team is involved in are loans through the Warwickshire Recovery and Investment Fund, and loans to the Warwickshire Property and Development Group, and Educaterers, the schools catering local authority trading company.

6.2 The non-treasury investments activities are reported and monitored at other Council governance forums and are not included in this report.

7. Financial Implications

7.1 The financial implications of the Treasury Management outturn are set out in the body of the report.

8. Environmental Implications

8.1 As stated in the Council approved Treasury Management Strategy Statement (TMSS), the Council is committed to considering environmental, social, and governance (ESG) issues, and has a particular interest in terms of climate change and pursuing activities that have a positive social impact.

8.2 In the TMSS, the Council undertook to ensure an understanding of the degree to which investments may contribute towards climate change and where appropriate, move cash balances to funds that have are ESG driven targets, or

"green funds", to ensure our investment is contributing towards tackling ESG issues, among other undertakings, with security and liquidity of investments taking precedence.

8.3 **Environmental**: The majority (70%) of the treasury investments outstanding at the end of this half year (30th September 2023) were fixed-term deposits with other local authorities, housing associations and building societies. Of these deposits, 66% by value were with local authorities, housing associations or building societies with a climate action plan. However, as security and liquidity take priority over ESG impact, the Council divested from the Blackrock Liquid Environmentally Aware Fund. This was because the fund was deemed a Variable Net Asset Value fund (VNAV) which means that there was capital at risk.

8.4 **Governance:** Officers rely on credit rating for assessing governance alignment. Governance considerations are included as part of the credit rating process, such as whether the money market fund asset manager is suitably qualified, competent, and capable, and whether there is an experienced and credible senior management team and sufficient resources. Therefore, the high credit ratings suggest that there are robust governance procedures within the banks, building societies and money market funds in which the Council invested in the quarter.

8.5 **Social alignment**: It is assumed that other local authorities will largely align with the Council's objectives. They are likely to provide similar services to the communities within their area, and have similar objectives, such as promoting a thriving economy and supporting people to live their best lives. Similarly, the primary objective of most housing associations is to provide affordable housing, which aligns with the Council Plan objectives.

9. Timescales Associated with Next Steps

9.1 This report will be presented to Resources and Fire & Rescue Overview and Scrutiny Committee on 14 December 2023.

9.2 A further Treasury Management report on Q3 activity will be presented to Resources and Fire & Rescue Overview and Scrutiny Committee in February 2024.

9.3 A Treasury Management Outturn report and Investment Outturn report will be presented to Cabinet after the yearend.

Appendix

Appendix 1 – Investment and Borrowing Portfolio
Appendix 3 – Prudential Indicators
Appendix 3 – Economic Update
Appendix 4 – Creditworthiness ratings table

Background Papers
None.

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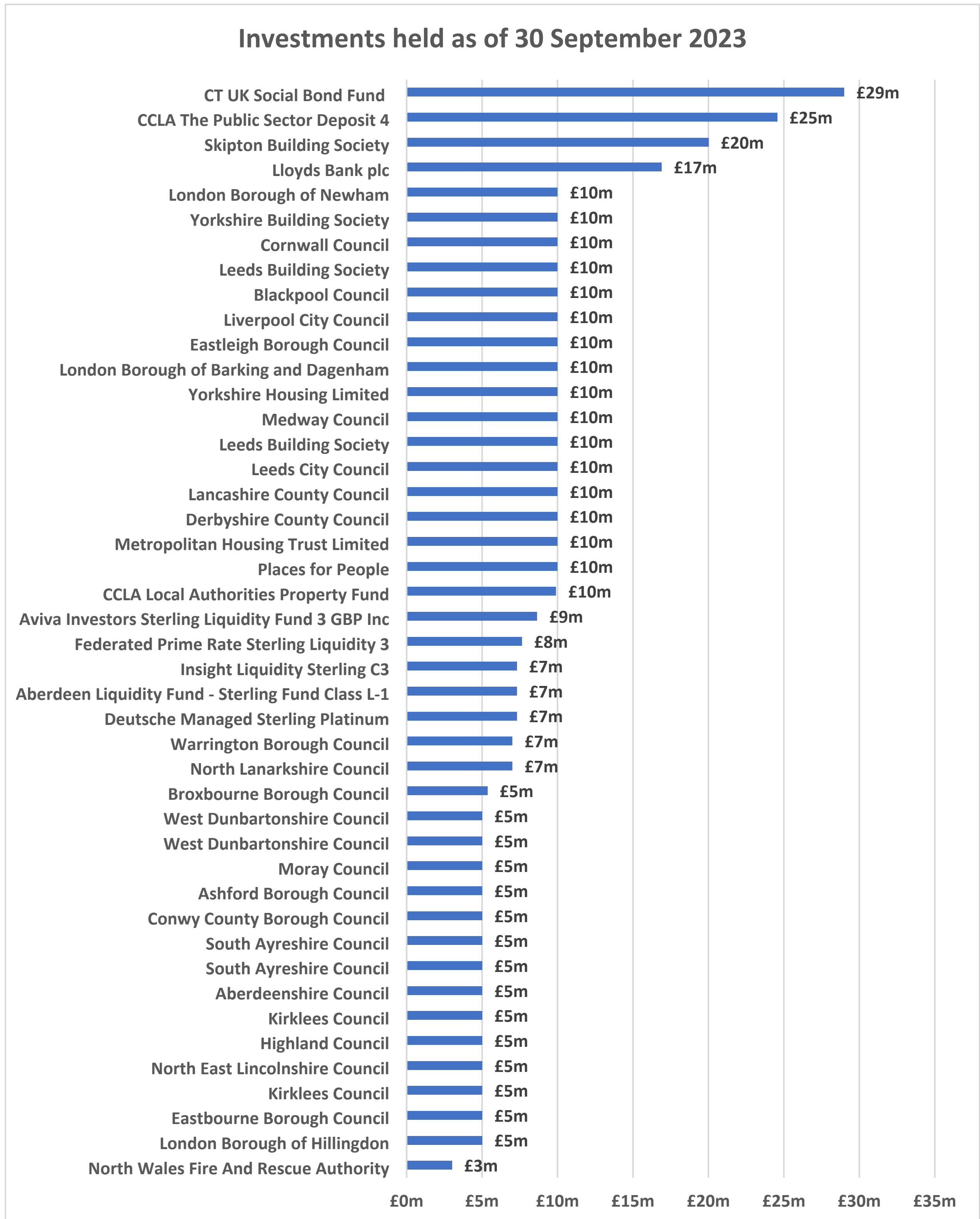
The report was circulated to the following members prior to publication:

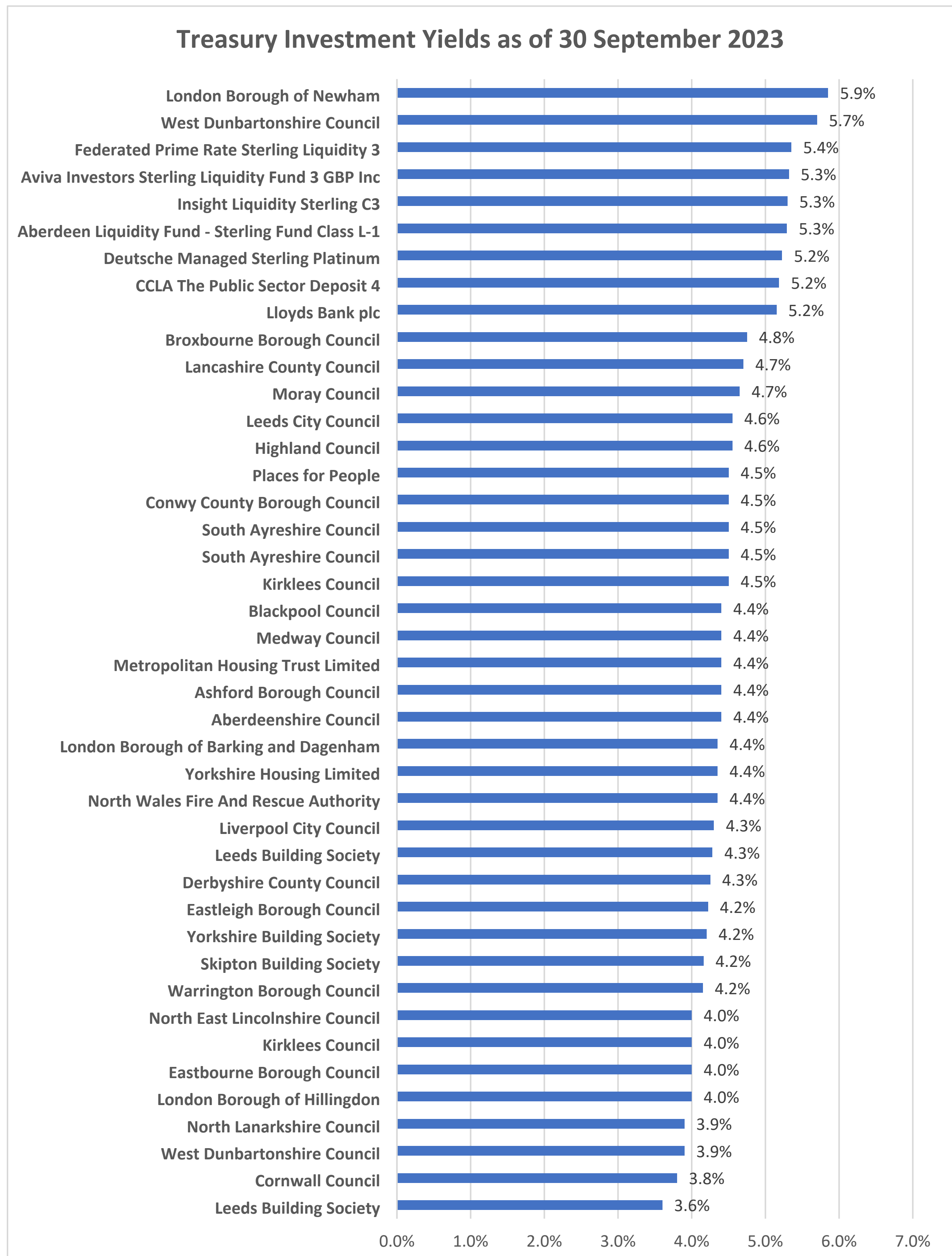
Local Member(s): N/A - This is a countywide matter.
Other Members: Leaders of the Labour, Liberal Democrats and Green Groups
Chair and Spokespersons of the Resources and Fire & Rescue Overview & Scrutiny Committee

APPENDIX 1: Investment and Borrowing Portfolios

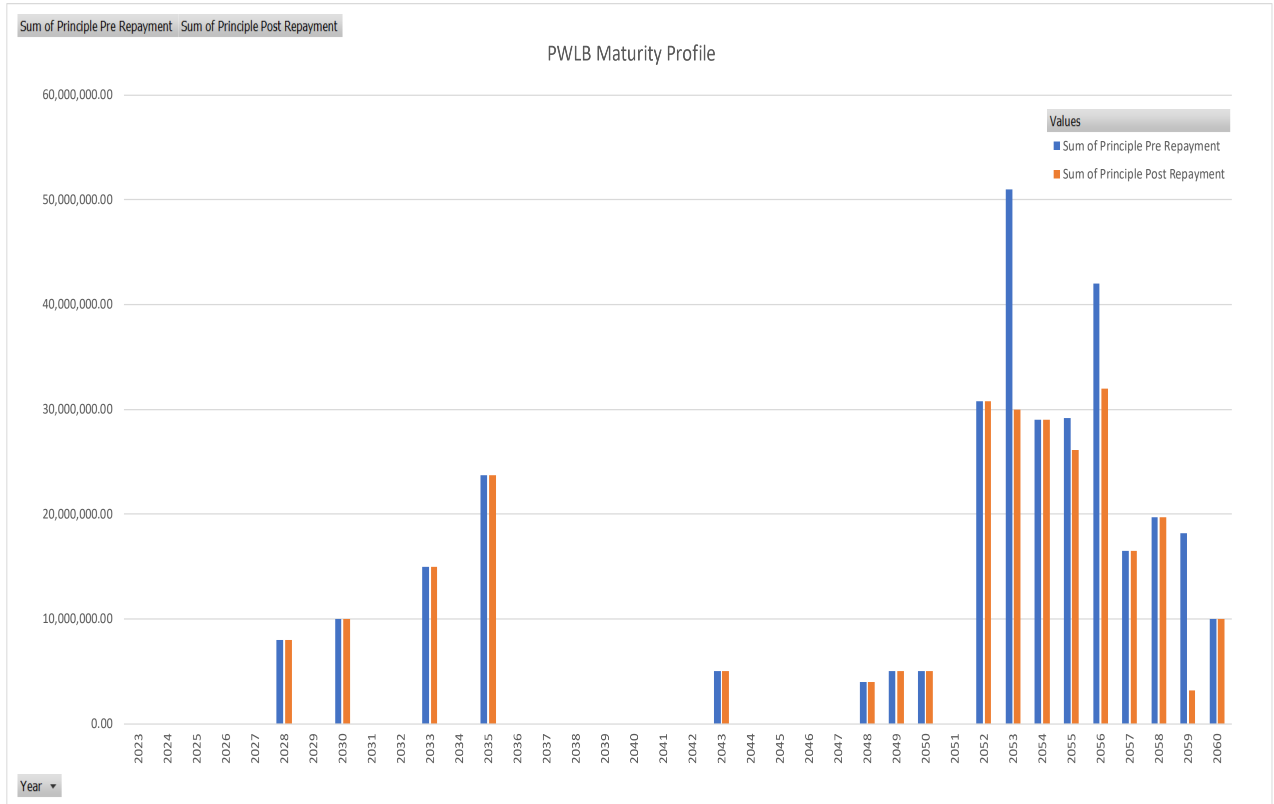
Investments held as of 30th September 2023



Investment yield as of the 30th September 2023



Borrowing profile as at the 30th of September 2023, compared to 31st March 2023.



APPENDIX 2: Prudential Indicators

PRUDENTIAL INDICATOR (1). AFFORDABILITY PRUDENTIAL INDICATORS	2022/23 Actual	2023/24 Estimate	2024/25 Estimate
	£'000	**£'000**	**£'000**
Capital Expenditure	117,352	160,094	179,508
	%	**%**	**%**
Ratio of financing costs to net revenue stream	5.13%	4.33%	4.40%
Gross borrowing requirement	**£'000**	**£'000**	**£'000**
Gross Debt	321,413	272,413	272,413
Capital Financing Requirement as at 31 March	256,854	287,253	381,922
Under/(Over) Borrowing	(64,559)	14,840	109,509
	£'000	**£'000**	**£'000**
In year Capital Financing Requirement	10,503	11,083	11,299

PRUDENTIAL INDICATOR (2). TREASURY MANAGEMENT PRUDENTIAL INDICATORS	2022/23 Actual	2023/24 Estimate	2024/25 Estimate
Authorised limit for external debt -	**£'000**	**£'000**	**£'000**
Borrowing	386,000	490,000	625,000
TOTAL	**386,000**	**490,000**	**625,000**
Operational boundary for external debt -	**£'000**	**£'000**	**£'000**
Borrowing	321,413	467,851	597,155
TOTAL	**321,413**	**326,320**	**311,976**
Upper limit for fixed interest rate exposure			
Net principal re fixed rate borrowing / fixed term investments	100%	100%	100%
Upper limit for variable rate exposure			
Net principal re fixed rate borrowing / fixed term investments	25%	25%	25%
Upper limit for total principal sums invested for over 365	**£'000**	**£'000**	**£'000**
(per maturity date)	£150,000	£150,000	£150,000

Maturity structure of borrowing during year	upper limit	lower limit
under 12 months	20%	0%
12 months and within 24 months	40%	0%
24 months and within 5 years	60%	0%
5 years and within 10 years	100%	0%
10 years and above	100%	0%

Maturity structure of new variable rate borrowing during	upper limit	lower limit
under 12 months	35%	0%
12 months and within 24 months	45%	0%
24 months and within 5 years	65%	0%
5 years and within 10 years	100%	0%
10 years and above	100%	0%

APPENDIX 3: Economic Update (provided by Link Group)

1. Economic Update

- The first half of 2023/24 saw:
  - Interest rates rise by a further 100bps, taking Bank Rate from 4.25% to 5.25% and, possibly, the peak in the tightening cycle.
  - Short, medium, and long-dated gilts remain elevated as inflation continually surprised to the upside.
  - A 0.5% month on month decline in real GDP in July, mainly due to more strikes.
  - CPI inflation falling 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 declining to 6.2% in August from 7.1% in April and May, a then 31 years high.
  - A cooling in labour market conditions, but no evidence yet that it has led to an easing in wage growth (as the 3-month year on year growth of average earnings rose to 7.8% in August, excluding bonuses).
- The 0.5% m/m 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). But with output falling in 10 out of the 17 sectors, there is an air of underlying weakness.
- The fall in the composite Purchasing Managers Index from 48.6 in August to 46.8 in September left it at its lowest level since COVID-19 lockdowns reduced activity in January 2021. At face value, it is consistent with the 0.2% quarter on quarter rise in real GDP in the period April to June, being followed by a contraction of up to 1% in the second half of 2023.
- 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.
- 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. And 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.
- 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. That is the first time it has fallen below 1m since July 2021. At 3.0% in July, and likely to have fallen to 2.9% in August, the job vacancy rate is getting closer to 2.5%, which would be consistent with slower wage growth. Meanwhile, the 48,000 decline in the supply of workers in the three months to July offset some of the loosening in the tightness of the labour market. That was due to a 63,000 increase in inactivity in the three months to July as more people left the labour market due to long term sickness or to enter education. The supply of labour is still 0.3% below its pre-pandemic February 2020 level.
- But the cooling in labour market conditions still has not fed through to an easing in wage growth. While the monthly rate of earnings growth eased sharply from an upwardly revised +2.2% in June to -0.9% in July, a lot of that was due to the one-off bonus payments for NHS staff in June not being repeated in July. The headline 3 monthly year on year rate rose from 8.4% (revised

up from 8.2%) to 8.5%, which meant UK wage growth remains much faster than in the US and in the Euro-zone. Moreover, while the Bank of England's closely watched measure of regular private sector wage growth eased a touch in July, from 8.2% 3myy in June to 8.1% 3myy, it is still well above the Bank of England's prediction for it to fall to 6.9% in September.

- 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%). Core goods inflation fell from 5.9% to 5.2% and the further easing in core goods producer price inflation, from 2.2% in July to a 29-month low of 1.5% in August, suggests it will eventually fall close to zero. But the really positive development was the fall in services inflation from 7.4% to 6.8%. That also reverses most of the rise since March and takes it below the forecast of 7.2% the Bank of England published in early August.
- 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. The minutes show the decision was "finely balanced". Five MPC members (Bailey, Broadbent, Dhingra, Pill and Ramsden) voted for no change and the other four (Cunliffe, Greene, Haskel and Mann) voted for a 25bps hike.
- Like the US Fed, the Bank of England wants the markets to believe in the higher for longer narrative. The statement did not say that rates have peaked and once again said if there was evidence of more persistent inflation pressures "further tightening in policy would be required". Governor Bailey stated, "we'll be watching closely to see if further increases are needed". The Bank also retained the hawkish guidance that rates will stay "sufficiently restrictive for sufficiently long".
- This narrative makes sense as the Bank of England does not want the markets to decide that a peak in rates will be soon followed by rate cuts, which would loosen financial conditions and undermine its attempts to quash inflation. The language also gives the Bank of England the flexibility to respond to new developments. A rebound in services inflation, another surge in wage growth and/or a further leap in oil prices could conceivably force it to raise rates at the next meeting on 2 November, or even pause in November and raise rates in December.
- 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).
- 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 debacle 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.
- The FTSE 100 has gained more than 2% since the end of August, from around 7,440 on 31 August to 7,608 on 29 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 21 April the FTSE 100 stood at 7,914.

2. Interest Rate Forecasts

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 20 bps) which has been accessible to most authorities since 1st November 2012.

The latest forecast on 25 September sets out a view that short, medium, 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.

Our PWLB rate forecasts below are based on the Certainty Rate (the standard rate minus 20 bps, calculated as gilts plus 80bps) which has been accessible to most authorities since 1 November 2012.

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

APPENDIX 4 – Creditworthiness Ratings Table

Moodys	S&P	Fitch	Description
Aaa	AAA	AAA	Highest credit quality, minimum credit risk
Aa1, Aa2 Aa3	AA+, AA, AA-	AA+, AA, AA-	Very high credit quality, very low credit risk
A1, A2, A3	A+, A, A-	A+, A, A-	High credit quality (upper-medium grade)
Baa1, Baa2, Baa3	BBB+, BBB, BBB-	BBB+, BBB, BBB-	Good credit quality, currently low credit risk
Ba1, Ba2, Ba3	BB+, BB, BB-	BB+, BB, BB-	Speculative elements, issue faces uncertainties and adverse conditions
B1, B2, B3	B+, B, B-	B+, B, B-	High credit risk, but issue still able to meet financial commitments
Caa1, Caa2, Caa3	CCC+, CCC, CCC-	CCC	Issuer currently vulnerable, default likely
Ca	CC	CC	Issuer currently highly vulnerable, near default
C	R, SD, D	C, RD, D	Lower rating typically in fault on some or all of its financial obligations