Treasury Management Mid-Year Review 2022-23

The Council's Treasury Management Strategy for 2022/23 was approved by Council on 23rd February 2022. This section of the report provides an update on treasury management activity for the period 1 April to 31 October 2022

Economic update and interest rate forecasts

<u>Recent events</u>

Since the end of September, the new Government has scrapped the reduction in the basic rate of income tax by 1p in the £; maintained the higher band 45p in the £ income tax rate; did not reduce Corporation Tax to 19% from 25%; only put in place support for businesses and households for 6 months (October to March) regarding caps on the unit costs of gas and electricity.

In addition, the Bank of England has had to intervene in the longer part of the gilt market to ensure that pension funds did not have to undertake a "fire sale" of assets to raise cash to pay for margin calls, arising from the sell-off of long-dated gilts (yields rising) in the wake of the former Chancellor's policy to seek to boost growth with unfunded tax cuts.

In recent days, calm has returned to the markets, the £ has risen from a historic low of $1.03 to $1.14, and the cumulative movement in gilt yields since the turn of the year is now broadly in line with that seen in the US and Euro-zone bond markets.

The new Chancellor will announce new fiscal policies in the Autumn Statement on 17th November, which seek to ensure that the public finances are kept on a sound footing and that any projected gaps (possibly £50bn to £60bn) are fully funded from services efficiencies and/or net tax increases.

<u>Bank Rate</u>

The Bank of England's Monetary Policy Committee (MPC) increased Bank Rate to a 14 year high of 3.00% from 2.25% at its meeting on Thursday 3rd November. The MPC continues to grapple with getting inflation back on track over a three-year horizon.

The Bank's Quarterly Monetary Policy Report from its meeting on 3rd November stated that the UK economy is headed for eight quarters of negative growth based on the market's expectation for Bank Rate to increase to 5.25%. Since then, market expectations have been recalibrated, and the market now expects a peak in Bank Rate of between 4.5% and 4.75%.

These views are similar to those held by the Council's treasury advisors, Link Group, who expect to see interest rates peaking in May 2023 at 4.50%. There are several challenges to the Bank, however, that could see them leave rates at this level until early 2024.

a) The tight labour market (unemployment is at a 48 year low 3.5%), which shows no signs of dissipating, and that could mean wage increases continue to be north of 5% well into 2023 (.

b) The prospect that unless the workforce participation rate increases and/or immigration policies are relaxed, there is no clear route that would give rise to sustainable increases in economic growth.

c) Inflation could be somewhat "sticky" if the Russian invasion of Ukraine remains unresolved and puts continued pressure on global energy prices and staple foods (e.g., wheat), among the many areas negatively impacted.

Against this backdrop, the Link Group forecast sees Bank Rate increasing 50 basis points in both December and February before the MPC scales down the rate of increase to 25 basis points in both March and May 2023.

PWLB Rates

It is expected that investors will still remain nervous over the UK's future fiscal policy and the longer dated rates in the table below reflect the potential demand by foreign investors for a "confidence premium" in the light of recent market volatility.

The monetary policies of other countries, in particular the US, will have an impact on global bond markets, with a knock-on impact upon PWLB rates. Geo-political events in countries such as Iran, North Korea, Taiwan and China will continue to lead to frequent whipsawing in equity, bond, commodity and currency markets. The climate will also play a large part in how high energy prices stay and for how long.

Table 1: Interest Rate Forecasts

The following are the latest forecasts from Link Group.

Bank Rate	2.50%	4.25%	4.50%	4.50%	4.50%	4.00%	3.75%	3.50%	3.25%	3.00%
PWLB Rates										
- 5 years	4.30%	4.30%	4.20%	4.10%	4.00%	3.90%	3.80%	3.60%	3.50%	3.40%
- 10 years	4.50%	4.50%	4.40%	4.30%	4.20%	4.00%	3.90%	3.70%	3.60%	3.50%
- 25 years	4.70%	4.70%	4.60%	4.50%	4.40%	4.30%	4.10%	4.00%	3.90%	3.70%
- 50 years	4.30%	4.40%	4.30%	4.20%	4.10%	4.00%	3.80%	3.70%	3.60%	3.40%

A review of the Treasury Management Strategy and Annual Investment Strategy

These strategies were approved by Council on 23rd February 2022 as part of the Capital & Investment Strategy for 2022/23. Officers are satisfied that the strategies remain fit for purpose.

Some of the original prudential indicators were revised in the April-July treasury management update (presented to this committee on 14th September). Further changes are required to some of the indicators as a result of the forecast 2022/23 capital outturn. The following table compare the previous prudential indicators (the indicators agreed on 14th September) against the latest revised indicators.

Table 2: Updated Prudential Indicators 2022/23

Prudential Indicator	Previous £000	Revised £000
Capital Expenditure	58,952	18,929
Capital Financing Requirement	299,069	256,161
Gross External Borrowing	283,256	225,188
Internal Borrowing	15,813	30,973
Operational Boundary	300,000	260,000
Authorised Limit	330,000	330,000

The following paragraphs explain these indicators in more detail:

<u>Capital Expenditure</u>
The following table shows the original and revised estimates for capital expenditure for 2022/23 split between General Fund and HRA expenditure. A breakdown of the individual schemes is shown in Appendix F – Capital Outturn .

Table 2: Capital Expenditure Estimates 2022/23

Service	Previous £000	Revised £000
General Fund	34,421	4,428
HRA	24,531	14,501
Total	**58,952**	**18,929**

<u>Capital Financing</u>
This table shows how the above expenditure will be financed:

Table 3: Capital Financing Estimates 2022/23

	Previous £000	Revised £000
Capital receipts	(4,999)	(1,453)
Capital grants & contributions	(250)	(503)
Major repairs reserve	(3,564)	(8,095)
Borrowing	(50,139)	(8,878)
Total	**(58,952)**	**(18,929)**

<u>Capital Financing Requirement</u>
The table below shows the Capital Financing Requirement (CFR) for 2022/23. The CFR represents the Council's underlying need to borrow in order to finance its capital expenditure. The reduction in the CFR reflects the reduction in the forecast borrowing required in 2022/23:

Table 4: Capital Financing Requirement

	Previous £000	Revised £000
General Fund	218,414	187,188
HRA	80,655	68,973
Total	**299,069**	**256,161**

Gross External Borrowing

The table below shows the Council's forecast external borrowing at at 31 March 2023. It also compares the external borrowing against the capital financing requirement, demonstrating the forecast level of internal borrowing.

Table 5: External Borrowing and the Capital Financing Requirement

	Previous £000	Revised £000
External borrowing	283,256	225,188
Capital financing requirement	299,069	256,161
Internal borrowing	**15,813**	**30,973**

Operational Boundary and Authorised Limit for External Debt

The operational boundary is the level above which external debt is not normally expected to rise. It is set at the level of expected external borrowing plus some headroom for any unexpected short-term borrowing needs.

The authorised limit controls the overall level of borrowing. It is a statutory limit determined under section 3 (1) of the Local Government Act 2003, representing the limit beyond which any borrowing would be unlawful.

The operational boundary has been reduced due to the reduction in forecast external borrowing for the year. The authorised limit has been left unchanged to provide headroom in the event of any unexpected borrowing need.

Table 6: Operational Boundary and Authorised Limit for External Debt

	Previous £000	Revised £000
Operational Boundary for External Debt	300,000	260,000
Borrowing	327,000	327,000
Other long-term liabilities	3,000	3,000
Authorised limit for external debt	**330,000**	**330,000**

The Section 151 Officer confirms that no prudential indicators were breached in the period 1 April 2022 to 31 October 2022.

External borrowing activity

The following table summarises the external borrowing activity to date during the year and the borrowing position as at 31 October 2022.

Table 7: External Borrowings April – October 2022

	Short - Term £000	PWLB £000	Transferred Debt £000	Total £000
Borrowing at 1 April 2022	36,000	192,019	169	228,188
Maturing borrowings repaid	(18,000)	0	0	(18,000)
New borrowings	25,000	0	0	25,000
Borrowing at 31 October 2022	43,000	192,019	169	235,188
Average interest rate	**0.34%**	**2.37%**	**8.62%**	
Proportion of total borrowing	**24%**	**76%**	**0%**	

Borrowing activity during the period has been limited to taking out new short-term borrowings to replace some of the maturing borrowings. There have been no new PWLB borrowings during the period and no such borrowings are planned for the remainder of the year. It is envisaged that all maturing borrowings will be replaced with short-term borrowings.   This approach will maintain a prudent balance within the portfolio between long-term and short-term borrowings.

The following table shows the maturity profile of the Council's borrowings, i.e. the years when the borrowings will mature.   This demonstrates that the Council is not exposed to any years when there is a high amount of maturing borrowing requiring refinancing.

Table 8: Maturity Profile of Borrowings

Period	Amount £000	Proportion of total borrowing	Maximum upper limit
> 1 year	43,000	18%	50%
2 to 5 years	10,000	4%	50%
6 to 10 years	32,400	14%	50%
10 to 20 years	42,019	18%	
20 to 30 years	17,000	7%	100%
Over 30 years	90,769	39%	
Total	**235,188**	**100%**	

Investments

The Council held £22m of investments as at 31st October 2022 (nil at 31st March 2022). Interest earnings as at 31st October 2022 were £0.236m, representing an average rate of return of 1.6%.

Investments during the year have been fixed-term investments, mostly with UK banks and also with a select range of non-UK banks accessed via the Council's treasury advisors.