TREASURY MANAGEMENT UPDATE: Quarter Ended 30th June 2024 (Q1 2024/25)

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. This report, therefore, ensures this Council is implementing best practice in accordance with the Code.

Appendix A: Prudential Indicators

Capital Expenditure and funding

Capital Expenditure	2024/25 Indicator £m	2024/25 Actual at 30.06.2024 £m	2024/25 Forecast Outturn £m
Capital Bids	120.4	7.4	111.4
Total	**120.4**	**7.4**	**111.4**

The reduction in capital expenditure is the result of capital moratorium. Which is in place to manage the new borrowing cost.

Financed By	2024/25 Indicator £m	2024/25 Actual at 30.06.2024 £m	2024/25 Forecast Outturn £m
Capital receipts to be used to fund capital programme	0	0.2	0
Capital grants & contributions	60.4	7.2	60.4
Revenue contributions	0.8	0	0.8
Transformation/invest to Save	22.2	0	22.2
Net Financing Requirement	36.9	0	27.9
Total	**120.4**	**7.4**	**111.4**

Capital Financing Requirement	2024/25 Indicator £m	2024/25 Forecast Outturn £m
CFR B/fwd	635.1	635.1
Net financing requirement	36.9	27.9
Less MRP & Other financing	(18.1)	(18.1)
CFR C/fwd	**653.8**	**644.8**

Ratio of Gross Financing Costs to Net Revenue Budget	2024/25 Indicator	2024/25 Forecast Outturn
Total Ratio	16.4%	17.1%

The latest capital BCR report forecasts an overspend on capital financing of £3.5m. This is due to an overspend on Minimum Revenue Provision (MRP) of £0.9m and on interest payable of £2.5m. These pressures have arisen due to:

- A review of MRP in 2023/24 has shown that there no further savings to be made, and that some previous assets under construction were not included in the calculation
- Interest rates have remained high leading to pressure on the interest payable budget.

To tackle this a capital moratorium is in place to reduce capital spend. This is in place for all capital spend apart from that which is; grant funded, statutory or a health & safety requirement or an invest to save.

Debt

Gross debt & capital financing requirement	**2024/25 Indicator £m**	**2024/25 Actual at 30.06.2024 £m**	**2024/25 Forecast Outturn £m**
External Borrowing			
Market Borrowing	500.0	512.5	500.0
Repayment of borrowing	-33.0	-54.5	-33.0
Expected change in borrowing	51.7	40.0	51.7
Other long-term liabilities	27.2	27.2	27.2
Gross Debt	**545.9**	**525.2**	**545.9**
CFR	**653.8**		**644.8**
% Of Gross Debt to CFR	**83.5%**		**84.7%**

The total debt is less than indicated and this is being managed carefully, both through the capital moratorium and through treasury management policies and procedures. External borrowing is kept to a minimum and internal borrowing is maximised.

Boundaries and Limits

Operational Boundary	**2024/25 Indicator £m**	**2024/25 Forecast Outturn £m**
Borrowing	653.8	644.8
Other long-term liabilities	27.2	27.2
Total	**681.1**	**672.1**

Authorised Limit	**2024/25 Indicator £m**	**2024/25 Forecast Outturn £m**
Borrowing*	663.8	644.8
Other Liabilities	27.2	27.2
Total Authorised Limit	**691.1**	**672.1**

The operational boundary and authorised limit are forecast to be to be as indicated. However, please see the comments about IFRS16. The changes required by this new accounting standard mean that both limits are expected to need to increase. This is because some leases will need to be shown as assets on the balance sheet, and will therefore will need to show as needing borrowing and MRP to finance them, in the accounts. In practice, however the changes will not affect cashflow or additional cash borrowing.

Borrowing

Maturity Structure of borrowing	**Upper Limit**	**As of 30 June 2024 £m**	**As of 30 June 2024 %**
Under 12 months	40%	78.0	16%
12 months to 2 years	20%	46.0	9%
2 years to 5 years	30%	23.5	5%
5 years to 10 years	80%	30.8	6%
10 years and above	100%	319.6	64%

Investments

	2024/25 Indicator £m	**2024/25 Actual at 30.06.2024 £m**	**2024/25 Forecast Outturn £m**
Principal sums invested >365 days	10	**0**	**10**

Investment Portfolio '000	**30 June 2024**		
	Principal	Average Rate (%)	Average Life (days)
MMFs	7,300	5.24%	1
Banks	20,000	5.18%	180
Local Authorities	7,000	5.35%	30
Total Investments	**34,300**	4.13%	105

Current investment balances are being kept liquid to help support daily cashflow management and the council's underlying internal borrowing position whilst at the same time maximising the investment rates available. In line with our new Green ESG policy we have made two £10m investments for one month into a green portfolio.

IFRS 16 - Implementation impacts

The Treasury Management Strategy and this Q1 update does not reflect as yet changes to accounting for leases under IFRS 16 which came into effect on 1 April 2024. These changes require that certain leased assets not currently reported as part of the PCC's balance sheet may need to be brought on balance sheet. Should this be the case it will increase the value of Other Long-Term Liabilities. Officers are currently evaluating the impact of these changes and will bring back the results of this exercise in due course.

This may require the authorised and operational boundaries to be reviewed to accommodate the additional long-term liabilities arising from any new leases identified as part of this exercise.

Appendix B: Economic Update from our Treasury Management Advisors and Narrative around the Council's financial position

1. Economics update

- The first quarter of 2024/25 saw:
  - GDP growth flatlining in April following positive Q4 2023/24 growth figures of 0.7% quarter on quarter.
  - A stalling in the downward trend in wage growth, with the headline 3 month year on year rate staying at 5.9% in April.
  - CPI inflation falling from 2.3% in April to 2.0% in May.
  - Core CPI inflation decreasing from 3.9% in April to 3.5% in May.
  - The Bank of England holding rates at 5.25% in May and June.
  - 10-year gilt yields climbing to 4.35% in April, before closing out at 4.32% in May.
- The news that the economy grew by 0.7% quarter on quarter in Q4 2023/24 confirmed that it moved out of its very mild technical recession that prevailed at the back end of 2023. However, data released for April and May so far shows a slight stalling in the recovery.

- On a more positive note, the 2.9% month on month increase in retail sales volumes in May more than reversed the 1.8% m/m drop in April. With inflation falling back to target, Bank Rate likely to be reduced soon and with consumer confidence improving, retail sales may well continue to strengthen.

- Investment will only make a modest contribution to GDP growth. With the industrial sector still 12% smaller than in 2019, excess capacity will continue to cap the need for industrial firms to invest. But improving business sentiment should raise investment by services' firms. Further, a fall in mortgage rates should trigger a recovery in residential investment.

- Nonetheless, the on-going stickiness of wage growth in April will be a lingering concern for the Bank of England.

- The fall in CPI inflation in May back to the Bank's 2% target for the first time since July 2021 will have come as welcome news to the Bank. Furthermore, with CPI inflation of 3.3% in the US and 2.6% in the Euro-zone in May, the UK appears to have won the race to get CPI inflation back to 2.0%. A further easing in food inflation from 2.8% in April to 1.6% in May played a part in the fall in overall CPI inflation and with food producer price inflation at just 0.2% in May, food price inflation will probably soon fall to zero.

- There was little chance that the Bank would cut rates at its June meeting, given upside surprises on services CPI inflation and wage growth. But several developments implied a rate cut is getting closer (August?).

- Throughout the quarter there was a degree of volatility in the gilt market, and, by way of example, the 10-year gilt yield rose from 4.05% on 2nd April to finish at 4.15% on 28th June but it has exceeded 4.30% on several occasions. Overall, investors judged that interest rates will need to remain high for longer to keep inflation around the 2.0% target.

MPC meetings 9th May and 20th June 2024

- On 9th May, the Bank of England's Monetary Policy Committee (MPC) voted 7-2 to keep Bank Rate at 5.25%. This outcome was repeated on 20th June.
- Nonetheless, with UK CPI inflation now back at 2% and set to fall further over the coming months, Ramsden and Dhingra – who voted again to reduce rates immediately to 5.00% in June – may shortly be joined by some members in the no-change camp, for whom the June decision was "finely balanced" as the upside news on services price inflation was more likely to be a reflection of one-off effects and volatile components rather than factors that would push up "medium-term inflation".

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, updated on 28th May, sets out a view that both short and long-dated interest rates will start to fall once it is evident that the Bank of England has been successful in squeezing excess inflation out of the economy, despite a backdrop of a stubbornly robust economy and a tight labour market.

Moreover, whatever the shape of domestic data, recent gilt market movements have been heavily influenced by the sentiment pertaining to US monetary policy. Again, inflation and labour data has proven sticky and the market's expectation for rate cuts has gradually reduced throughout the course of the year, so that possibly rates may not be cut more than once, or possibly twice, before the end of 2024. In any event, even if the Bank of England starts to cut rates first, it may mean that the medium and longer parts of the curve take longer to fully reflect any such action until the US yield curve shifts lower too. Given the potential inflationary upside risk to US treasuries if Trump wins the presidential election in November (increased tariffs on imports from China for example), therein lies a further risk to yields remaining elevated for longer.

Closer to home, the General Election is not expected to have a significant impact on UK monetary policy. There is minimal leeway for further tax cuts or added spending without negatively impacting market sentiment. It may even be the case that the Bank of England will steer clear of an August rate cut – should that be supported by the inflation data – in favour of weighing up fiscal policy implications and market sentiment in the aftermath of the election.

Accordingly, Link's central case is still for a rate cut before the end of September, but we are not committed to whether it will be in August or September. Thereafter, the path and speed of rate cuts is similar to that which we previously forecast, with Bank Rate eventually falling to a low of 3% by H2 2026.

However, given the increased uncertainty surrounding Link's central gilt market forecasts, and the significant issuance that will be on-going from several of the major central banks, it has marginally increased its PWLB forecasts by c20 to 30 basis points across the whole curve since the previous quarter.

In summary, regarding PWLB rates, movement in the short-end of the curve is expected to reflect Link's Bank Rate expectations to a large degree, whilst medium to longer-dated PWLB rates will remain influenced not only by the outlook for inflation, domestically and globally, but also by the market's appetite for significant gilt issuance (£200bn+ for each of the next few years). As noted at the Link March Strategic Issues webinars, there is upside risk to that part of our forecast despite the Debt Management Office skewing its issuance to the shorter part of the curve.

Link Group Interest Rate View	28.05.24											
	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27
BANK RATE	5.25	5.00	4.50	4.00	3.50	3.25	3.25	3.25	3.25	3.00	3.00	3.00
3 month ave earnings	5.30	5.00	4.50	4.00	3.50	3.30	3.30	3.30	3.30	3.00	3.00	3.00
6 month ave earnings	5.30	4.90	4.40	3.90	3.50	3.30	3.30	3.30	3.30	3.10	3.10	3.20
12 month ave earnings	5.10	4.80	4.30	3.80	3.50	3.40	3.40	3.40	3.40	3.20	3.30	3.40
5 yr PWLB	4.90	4.70	4.50	4.30	4.10	4.00	3.90	3.90	3.90	3.90	3.90	3.80
10 yr PWLB	5.00	4.80	4.60	4.40	4.30	4.10	4.10	4.10	4.00	4.00	4.00	3.90
25 yr PWLB	5.30	5.20	5.00	4.80	4.70	4.50	4.50	4.40	4.40	4.40	4.30	4.30
50 yr PWLB	5.10	5.00	4.80	4.60	4.50	4.30	4.30	4.20	4.20	4.20	4.10	4.10

- 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. Annual Investment Strategy

The Treasury Management Strategy Statement (TMSS) for 2024/25, which includes the Annual Investment Strategy, was approved by the Council on 21 February 2024. 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

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.

As shown by the charts below and the interest rate forecasts in section 2, investment rates have remained elevated during the first quarter of 2024/25 but are expected to fall back through the second half of 2024 as inflation reduces and the MPC starts to loosen monetary policy.

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.

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

CDS prices
For UK banks, these have remained low, and 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.**

Investment balances
The average level of funds available for investment purposes during the quarter was £42m. 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's budgeted investment return for 2024/25 is £1.7m, and performance for the year to date is in line with the budget.

4. Borrowing

Due to the overall financial position, the council borrowed £35m of short-term borrowings. £30m from PWLB at a rate of 5.40% and the £5m from other local authority at a rate of 5.25%.

It is anticipated that other borrowing will be undertaken during the later stages of this financial year in order to refinance maturing short-term borrowing and/or to finance new general fund capital expenditure. The timing of any borrowing will be influenced by the movement in interest rates (para 2)

PWLB maturity Certainty Rates 1st April to 30th June 2024
Gilt yields and PWLB rates remained relatively stable between 1st April and 30th June. Having said that, the spread between the low and high points during the quarter was between 0.3% and 0.45% across the curve.

The 50-year PWLB Certainty Rate target for new long-term borrowing (the low point of our forecast on a two-year timeline) started 2024/25 at 4.00% and increased to 4.20% on 28th May. As can be seen, with rates remaining elevated across the whole of the curve, it is advised to not borrow long-term unless the Authority wants certainty of rate and judges the cost to be affordable.

PWLB RATES 02.04.24 - 28.06.24 (note: 1st April & 29th and 30th June were bank holidays)