NEWARK & SHERWOOD DISTRICT COUNCIL

Report to:	Audit & Governance Committee Meeting 22 November 2023
Director or Business Manager Lead:	Nick Wilson, Business Manager Financial Services
Lead Officer:	Andrew Snape, Assistant Business Manager Financial Services ext 5323

Report Summary	
Report Title	Treasury Management Mid-Year Report 2023/24
Purpose of Report	To provide an update on the Council's Treasury Activity and Prudential Indicators for the first half of 2023/24
Recommendations	That the treasury management activity be noted and recommend to Full Council on 12 December; and The Prudential Indicators detailed in Section 6 & 7 of the report be noted.
Reason for Recommendation	To allow Committee to note Treasury Management Activity and recommend it to Full Council and To allow Committee to note the Prudential Indicators

1.0 Background Information

1.1 This report has been written in accordance with the requirements of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised 2017). The primary requirements of the Code are as follows:

- Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.
- Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.
- Receipt by the full council of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead, a Mid-year Review Report and an Annual Report, (stewardship report), covering activities during the previous year.
- Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

- Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body. For this Council the delegated body is the Audit and Governance Committee.

1.2 This mid-year report has been prepared in compliance with CIPFA's Code of Practice on Treasury Management, and covers the following:
- An economic update for the first part of the 2023/24 financial year;
- A review of the Treasury Management Strategy Statement and Annual Investment Strategy;
- The Council's capital expenditure, as set out in the Capital Strategy, and prudential indicators;
- A review of the Council's investment portfolio for 2023/24;
- A review of the Council's borrowing strategy for 2023/24;
- A review of any debt rescheduling undertaken during 2023/24;
- A review of compliance with Treasury and Prudential Limits for 2023/24.

1.3 Treasury Management is defined as: "The management of the local authority's borrowing, investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks".

1.4 The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer term cash flow planning to ensure the Council can meet its capital spending operations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses, and on occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

2.0 Summary of Treasury Balances as at 30 September 2023

2.1 Below is a summary of the Councils borrowing position as at 30 September 2023, further information is available at section 4.

Balance on 01/04/2023 £m		**Balance on 30/09/2023 £m**
90.769	Total Borrowings	89.755
5.009	Total Other Long Term Liabilities	5.009
95.778	**TOTAL EXTERNAL DEBT**	**94.764**

2.2 Below is a summary of the Councils investment position as at 30 September 2023, further information is available at section 5.

Balance on 01/04/2023 £m		Balance on 30/09/2023 £m
49.575	Total Short Term Investments	49.915
12.500	Total Long Term Investments	12.500
62.075	**TOTAL INVESTMENTS**	**62.415**

2.3 Below is a summary of the Councils capital expenditure position as at 30 September 2023, further information is available at section 3.

Capital Expenditure	2023/24 Initial Capital Budget £m	2023/24 Revised Estimate £m	2023/24 Current Expenditure £m
General Fund Expenditure	66.294	74.073	16.703
HRA Expenditure	23.045	16.887	4.345
Total Capital Expenditure	**89.339**	**90.960**	**21.048**

2.4 **Prudential Indicators**, during the first half of the financial year there was no breach in the prudential indicators.

Treasury Management Strategy Statement (TMSS) and Annual Investment Strategy update

2.5 The Treasury Management Strategy Statement (TMSS) for 2023/24 was approved by Full Council on 9 March 2023. There are no suggested policy changes to the TMSS within this report; the details in this report update the position in the light of the updated economic position and capital budget changes approved at Policy and Finance throughout the year.

3.0 The Council's Capital Position

3.1 This part of the report is structured to update:

- The Council's capital expenditure plans;
- How these plans are being financed;
- The impact of the changes in the capital expenditure plans on the prudential indicators and the underlying need to borrow; and
- Compliance with the limits in place for borrowing activity.

3.2 The table below shows the revised estimates for capital expenditure and the changes since the Capital Programme was agreed within the Capital budget on 9 March 2023.

Capital Expenditure	2023/24	2023/24	Actual Spend as at 30 September 2023

	Original Budget Approved 9 March 2023 £m	Revised Budget as at 30 September 2023 £m	£m
General Fund Expenditure	66.294	74.073	16.703
HRA Expenditure	23.045	16.887	4.345
Total Capital Expenditure	**89.339**	**90.960**	**21.048**
Financed By:			
Capital Receipts	5.738	2.935	
Capital Grants & CIL	34.592	47.853	
Capital Reserves	0.754	6.662	
Revenue	17.992	13.088	
Total Financing	**59.076**	**70.538**	
Borrowing Requirement	**30.263**	**20.422**	

3.3 The financing of the Capital Programme will be determined by the S151 Officer at the year-end based on best use of resources.

The movement from the Budget approved 9 March 2023 relates to approved capital carry forward requests and approved variations to the capital programme as shown in the table below.

Original Capital Budget Approved 23/24	**£89.339m**
Capital Slippages Carried Forward	£28.642m
Cabinet Approvals 12.09.23	(£8.331m)
Cabinet Variations requested 05.12.23	(£18.751m)
New Revised Budget	**£90.960m**

4.0 Borrowing Strategy

4.1 At 30 September 2023 the Council held £89.755m of loans, as part of its strategy for funding previous years' borrowing within those capital programmes.

4.2 Borrowing Activity in 2023/24

	General Fund		HRA	
	Balance on 01/04/2023 £m	Balance on 30/09/2023 £m	Balance on 01/04/2023 £m	Balance on 30/09/2023 £m
Short Term Borrowing	0.340	0.843	8.994	7.478
Long Term Borrowing	3.500	3.500	77.935	77.935
Total Borrowing	**3.840**	**4.343**	**86.929**	**85.413**
Other Long Term Liabilities	5.009	5.009	0.000	0.000
Total External Debt	**8.849**	**9.352**	**86.929**	**85.413**
CFR	28.018	48.320	106.601	103.571
Under / (over) borrowing	**19.169**	**38.968**	**19.672**	**18.158**

4.3 As the Council is in a significant under borrowed position, as per the table in 4.2, there may be a requirement during the remainder of the financial year where new borrowing is required. Any new borrowing will be within the approved Treasury Management Borrowing Strategy framework and will have been reviewed by the S151 Officer for cost effectiveness as whether to borrow shorter term or long term in relation to interest rate forecasts.

4.4 **LOBOs**: The Council holds £3.5m of LOBO (Lender's Option Borrower's Option) loans where the lender has the option to propose an increase in the interest rate at set dates, following which the Council has the option to either accept the new rate or to repay the loan at no additional cost. All of the £3.5m of LOBOS had options during the last 6 months, none of which were exercised by the lender. The Council acknowledges there is an element of refinancing risk even though in the current interest rate environment lenders are unlikely to exercise their options.

4.5 **Internal borrowing*:*** For the Council, the use of internal resources in lieu of borrowing has continued to be the most cost effective means of funding of capital expenditure that has not been funded from grants and other resources. This has lowered overall treasury risk by reducing both external debt and temporary investments. However, this position will not be sustainable over the medium to longer term as the Council needs to use reserves for the purpose they were set aside for, and external borrowing may need to be undertaken.

4.6 **Debt rescheduling*:*** The premium charge for early repayment of PWLB debt remains relatively expensive for the loans in the Council's portfolio and therefore unattractive for debt rescheduling activity. No rescheduling activity was undertaken or is proposed during the rest of the financial year as a consequence.

5.0 Investment Activity

5.1 The Guidance on Local Government Investments in England gives priority to security and liquidity and the Council's aim is to achieve a return commensurate with these principles.

5.2 **Investment Activity in 2023/24**

Type of Investment	Balance on 01/04/2023 £m	Balance on 30/09/2023 £m	Average Interest Rate
Short term Investments			
Fixed Term Deposits:			
Santander	5.000	5.000	4.01%
Lloyds 95 Day Notice	5.000	5.000	3.92%
Close Brothers	2.000	2.000	5.60%
Goldman Sachs International Bank	5.000	5.000	5.53%
Standard Chartered	3.000	3.000	5.36%
Standard Chartered Sustainable Deposit	12.000	12.000	5.39%
Money Market Funds:			
Goldman Sachs	0.010	0.460	5.22%
Deutsche Bank	1.475	0.045	5.13%
Invesco	2.550	3.170	5.33%

Northern Trust	11.300	12.000	5.27%
CCLA	2.240	2.240	5.07%
Total Short Term Investments	**49.575**	**49.915**	
Long term Investments			
CCLA Property Fund	7.000	7.000	4.81%
CCLA Diversified Income Fund	5.500	5.500	3.49%
Total Long Term Investments	**12.500**	**12.500**	
TOTAL INVESTMENTS	**62.075**	**62.415**	
Increase/ (Decrease) in Investments		0.340	

5.3 Both the CIPFA Code and government guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its treasury investments before seeking the optimum rate of return, or yield. The Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

6.0 Non-Treasury Investments

6.1 The definition of investments in CIPFA's revised Treasury Management Code now covers all the financial assets of the Council as well as other non-financial assets which the Council holds primarily for financial return or regeneration purposes. This is replicated in MLUHC's Investment Guidance, in which the definition of investments is further broadened to also include all such assets held partially for financial return or regeneration purposes.

Breakdown below of current Non-Treasury Investments held;

Counterpart	**Balance at 30/09/2023 £m**
Loans to Housing Associations	0.013
Loans to Parish Councils	0.011

6.2 These investments are due to generate £0.001m of investment income for the Council after taking account of direct costs, representing a rate of return of 6.31%.

6.3 Maturity Structure of Fixed Rate Borrowing. This indicator is to limit large concentrations of fixed rate debt needing to be replaced at times of uncertainty over interest rates.

	Upper Limit %	**Actual at 30/9/23 £m**	**Actual at 30/9/23 £m**	**Compliance**
Under 12 Months	15%	3.500	3.94%	Yes
12-24 Months	15%	11.000	12.37%	Yes
2-5 Years	30%	3.979	4.47%	Yes
5-10 Years	100%	21.831	24.55%	Yes
Over 10 Years	100%	48.602	54.66%	Yes

Limits to Investing Activity

6.4 **Security.** The Council has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average credit rating of its investment portfolio. This is calculated by applying a score to each investment (AAA=1, AA+=2, etc.) and taking the arithmetic average, weighted by the size of each investment. Unrated investments are assigned a score based on their perceived risk.

Credit risk indicator	Target	Actual	Compliance
Portfolio average credit rating	A	AA-	Yes

6.5 **Liquidity Risk Indicator**. The Council has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments within a banding period, without additional borrowing.

Total Cash Available within;	Limit	Actual 30/09/23	Compliance
3 Months	100%	64%	Yes
3-12 Months	80%	16%	Yes
Over 12 Months	60%	20%	Yes

6.6 **Principal Sums Invested for over 364 Days.** The purpose of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments.

Price risk indicator	Limit	Actual 30/09/23	Compliance
Limit on principal invested beyond year end	£15m	£12.5m	Yes

7.0 **Limits to Capital Activity**

7.1 **Capital Financing Requirement.** The table below shows the CFR, which is the underlying external need to incur borrowing for a capital purpose.

	2023/24 Original Estimate £m	2023/24 Revised Estimate £m
CFR – non housing	56.860	48.320
CFR – housing	108.439	103.571
Total CFR	**165.299**	**151.891**
Estimated Net Movements in CFR		**-13.408**

7.2 Capital Financing Costs to Net Revenue Stream. Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP are charged to revenue, offset by any investment income receivable. The net annual charge is known as financing costs; this is compared to the net revenue stream i.e. the amount funded from Council Tax, business rates and general government grants.

	2023/24 Original Estimate £m	**2023/24 Revised Estimate £m**
General Fund		
Financing Costs	-0.480	-0.515
Proportion of net revenue stream	-2.61%	-2.28%
Housing Revenue Account		
Financing Costs	14.464	13.966
Proportion of net rental stream	54.52%	51.49%

8.0 Economic Background/Interest Rate Forecast

8.1 **Appendix A and Appendix B** gives a summarised outlook for the economic background and interest rate forecast from our Treasury Consultants, Link.

Background Papers and Published Documents

Nil.

Appendix A

Economics 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% m/m 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 3myy 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% q/q 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% m/m 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 3myy 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 2nd 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 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 forecasts **Appendix B**

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 25th 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 1st 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