

## CABINET

THURSDAY 29<sup>TH</sup> AUGUST 2024

## COUNCIL

TUESDAY 17<sup>TH</sup> SEPTEMBER 2024

### REPORT OF THE PORTFOLIO HOLDER FOR OPERATIONS AND FINANCE

### ANNUAL REPORT ON THE TREASURY MANAGEMENT SERVICE AND ACTUAL PRUDENTIAL INDICATORS 2023/24

#### EXEMPT INFORMATION

None

#### PURPOSE

The Annual Treasury report is a requirement of the Council's reporting procedures. It covers the Treasury activity for 2023/24, and the actual Prudential Indicators for 2023/24.

The report meets the requirements of both the CIPFA Code of Practice on Treasury Management and the CIPFA Prudential Code for Capital Finance in Local Authorities. The Council is required to comply with both Codes in accordance with Regulations issued under the Local Government Act 2003. It also provides an opportunity to review the approved Treasury Management Strategy for the current year and enables Members to consider and approve any issues identified that require amendment.

#### RECOMMENDATIONS

That Council ;

1. **Approve the actual 2023/24 Prudential and Treasury Indicators within the report and shown at Appendix 1; and**
2. **Note the Annual Treasury Management Report for 2023/24**

#### EXECUTIVE SUMMARY

This report covers Treasury operations for the year ended 31<sup>st</sup> March 2024 and summarises:

- the Council's Treasury position as at 31<sup>st</sup> March 2024; and
- Performance Measurement

The key points raised for 2023/24 are:

1. The Council's Capital Expenditure and Financing 2023/24
2. The Council's Overall Borrowing Need
3. Treasury Position as at 31<sup>st</sup> March 2024

4. The Strategy for 2023/24
5. Borrowing Outturn for 2023/24
6. Investment Outturn for 2023/24
7. Performance Measurement
8. The Economy and Interest Rates
9. Property Funds
10. Other Issues

The Treasury Function has achieved the following favourable results:

- The Council has complied with the professional codes, statutes and guidance;
- There are no issues to report regarding non-compliance with the approved prudential indicators;
- The Council maintained an average investment balance externally invested of £67.4m and achieved an average return of 4.92% (budgeted at £38.2m and an average return of 3.4%).
- The closing weighted average internal rate on borrowing is 4.05% (4.05% for 2023/24);
- The Treasury Management Function has achieved an outturn investment income of £3.4m compared to an original budget of £1.3m Investment balances were higher than budgeted throughout the year, and the average interest rates rose significantly.
- We also received £487k in dividends from our property fund investments (£458k in 2022/23), compared to a budget of £420k. However, the net value of the investments has fallen by £1.82m as at 31<sup>st</sup> March 2024.

During 2023/24 the Council complied with its legislative and regulatory requirements.

The Executive Director Finance confirms that there was no overall increase in borrowing within the year and the Authorised Limit was not breached.

At 31<sup>st</sup> March 2024, the Council's external debt was £63.060m (£63.060m at 31<sup>st</sup> March 2023) and its external investments, excluding property funds and bank account, totalled £59.108m (£60.610m at 31<sup>st</sup> March 2023).

## **RESOURCE IMPLICATIONS**

There are no financial implications or staffing implications arising directly from the report.

## **LEGAL/RISK IMPLICATIONS BACKGROUND**

The Council is aware of the risks of passive management of the Treasury Portfolio and with the support of Link Asset Services, the Council's current Treasury advisers, has proactively managed its debt and investments during the year.

## **EQUALITIES IMPLICATIONS**

None

## **SUSTAINABILITY IMPLICATIONS**

None

## **REPORT AUTHOR**

If Members would like further information or clarification prior to the meeting please contact Joanne Goodfellow, telephone 01827 709241 or email [joanne-goodfellow@tamworth.gov.uk](mailto:joanne-goodfellow@tamworth.gov.uk)

## **LIST OF BACKGROUND PAPERS**

- Local Government Act 2003;
- Statutory Instruments: 2003 No 3146 & 2007 No 573;
- CIPFA Code of Practice on Treasury Management in Public Services;
- Treasury Management Strategy 2023/24 (Council 28th February 2023);
- Treasury Management Mid-Year Review 2023/24 (Council 12th December 2023);
- Treasury Outturn Report 2022/23 (Council 19th September 2023).

## **APPENDICES**

**Appendix 1 – Prudential and Treasury Indicators**

**Appendix 2 – Borrowing and Investment Rates**

## Annual Treasury Management Review 2022/23

This Council is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2023/24. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).

During 2023/24 the minimum reporting requirements were complied with:

- an annual treasury strategy in advance of the year (Council 28th February 2023)
- a mid-year (minimum) treasury update report (Council 12th December 2023)
- an annual review following the end of the year describing the activity compared to the strategy (this report).

In addition, Cabinet has received quarterly Treasury Management updates as part of the quarterly performance reports.

The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This report is, therefore, important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by members. This Council confirms that it has complied with the requirement under the Code to provide scrutiny of all of the above Treasury Management Reports to the Audit and Governance Committee. Member training on Treasury Management issues was provided in February 2024 and further training is planned during 2024/25.

During 2023/24, the Council complied with its legislative and regulatory requirements. The key actual prudential and treasury indicators detailing the impact of capital expenditure activities during the year, with comparators, are as follows.

| Prudential & Treasury Indicators | 2022/23      | 2023/24        | 2023/24       |
|----------------------------------|--------------|----------------|---------------|
|                                  | Actual<br>£m | Estimate<br>£m | Actual<br>£m  |
| Capital Expenditure              |              |                |               |
| Non HRA                          | 4.889        | 30.988         | <b>12.416</b> |
| HRA                              | 13.876       | 14.613         | <b>11.320</b> |
| <b>Total</b>                     | 18.765       | 45.601         | <b>23.737</b> |
| Capital Financing Requirement    |              |                |               |
| Non HRA                          | 3.785        | 6.608          | <b>4.092</b>  |
| HRA                              | 69.982       | 71.582         | <b>70.507</b> |
| <b>Total</b>                     | 73.767       | 78.190         | <b>74.600</b> |
| Gross Borrowing                  |              |                |               |
| External Debt                    | 63.060       | 63.060         | <b>63.060</b> |
| Investments                      |              |                |               |
| Longer than 1 year               | 10.842       | -              | <b>10.143</b> |
| Less than 1 year                 | 60.49        | 15.194         | <b>56.670</b> |
| <b>Total</b>                     | 71.332       | 15.194         | <b>66.813</b> |
| <b>Net Borrowing</b>             | -8.272       | 47.866         | <b>-3.753</b> |

It should be noted that **£30m** of Capital scheme spend has been re-profiled into 2024/25 (also including re-profiling from previous years) which has increased investment balances.

Other prudential and treasury indicators are to be found further in this report. The Executive Director Finance confirms that there was no overall increase in borrowing in year and the statutory borrowing limit (the authorised limit) was not breached.

**1. The Council’s Capital Expenditure and Financing 2023/24**

The Council undertakes capital expenditure on long-term assets. These activities may either be:

- Financed immediately through the application of capital or revenue resources (capital receipts, capital grants, revenue contributions etc.), which has no resultant impact on the Council’s borrowing need; or
- If insufficient financing is available, or a decision is taken not to apply internal funds, the capital expenditure would give rise to a borrowing need.

The actual capital expenditure forms one of the required prudential indicators. The table below shows the actual capital expenditure and how this was financed.

| General Fund                          | 2022/23<br>Actual<br>£m | 2023/24<br>Estimate<br>£m | 2023/24<br>Actual<br>£m |
|---------------------------------------|-------------------------|---------------------------|-------------------------|
| Capital Expenditure                   | 4.889                   | 30.988                    | <b>12.416</b>           |
| Financed in year                      | 4.837                   | 27.331                    | <b>11.902</b>           |
| <b>Unfinanced capital expenditure</b> | 0.052                   | 3.657                     | <b>0.515</b>            |
| HRA                                   | 2022/23<br>Actual<br>£m | 2023/24<br>Estimate<br>£m | 2023/24<br>Actual<br>£m |
| Capital Expenditure                   | 13.876                  | 14.613                    | <b>11.320</b>           |
| Financed in year                      | 13.788                  | 13.757                    | <b>10.795</b>           |
| <b>Unfinanced capital expenditure</b> | 0.088                   | 0.856                     | <b>0.526</b>            |

**2. The Council’s Overall Borrowing Need**

The Council’s underlying need to borrow to finance capital expenditure is termed the Capital Financing Requirement (CFR). This figure is a gauge of the Council’s indebtedness. The CFR results from the capital activity of the Council and resources used to pay for the capital spend. It represents the 2023/24 unfinanced capital expenditure (see above table), and prior years’ net or unfinanced capital expenditure which has not yet been paid for by revenue or other resources.

Part of the Council’s treasury activities is to address the funding requirements for this borrowing need. Depending on the capital expenditure programme, the treasury service organises the Council’s cash position to ensure that sufficient cash is available to meet the capital plans and cash flow requirements. This may be sourced through borrowing from external bodies (such as the Government, through the Public Works Loan Board [PWL] or the money markets), or utilising temporary cash resources within the Council.

**Reducing the CFR** – the Council’s (non HRA) underlying borrowing need (CFR) is not allowed to rise indefinitely. Statutory controls are in place to ensure that capital assets are broadly charged to revenue over the life of the asset. The Council is required to make an annual revenue charge, called the Minimum Revenue Provision (MRP), to reduce the CFR. This is effectively a repayment of the non-Housing Revenue Account (HRA) borrowing need (there is no statutory requirement to reduce the HRA CFR). This differs from the treasury management arrangements which ensure that cash is available to meet capital commitments. External debt can also be borrowed or repaid at any time, but this does not change the CFR.

The total CFR can also be reduced by:

the application of additional capital financing resources (such as unapplied capital receipts); or

charging more than the statutory revenue charge (MRP) each year through a Voluntary Revenue Provision (VRP).

The Council’s 2023/24 MRP Policy (as required by DLUHC Guidance) was approved as part of the Treasury Management Strategy Report for 2023/24 on 28th February 2023.

The Council’s CFR for General Fund and the HRA for the year are shown below, and represent a key prudential indicator.

| CFR: General Fund                             | 31st March 2023<br>Actual £m | 31st March 2024<br>Budget £m | 31st March 2024<br>Actual £m |
|---|------------------------------|------------------------------|------------------------------|
| Opening balance                               | 3.937                        | 3.909                        | <b>3.785</b>                 |
| Add unfinanced capital expenditure (as above) | 0.052                        | 3.657                        | <b>0.515</b>                 |
| Less MRP/VRP                                  | (0.204)                      | (0.214)                      | <b>(0.207)</b>               |
| Less PFI & finance lease repayments           | -                            | -                            | -                            |
| <b>Closing balance</b>                        | <b>3.785</b>                 | <b>7.352</b>                 | <b>4.092</b>                 |

| CFR: HRA                                      | 31st March 2023<br>Actual £m | 31st March 2024<br>Budget £m | 31st March 2024<br>Actual £m |
|---|------------------------------|------------------------------|------------------------------|
| Opening balance                               | 69.893                       | 69.982                       | <b>69.981</b>                |
| Add unfinanced capital expenditure (as above) | 0.088                        | 3.657                        | <b>0.526</b>                 |
| Less MRP/VRP                                  | -                            | -                            | -                            |
| Less PFI & finance lease repayments           | -                            | -                            | -                            |
| <b>Closing balance</b>                        | <b>69.981</b>                | <b>73.639</b>                | <b>70.507</b>                |

Borrowing activity is constrained by prudential indicators for gross borrowing and the CFR, and by the authorised limit.

**Gross borrowing and the CFR** - in order to ensure that borrowing levels are prudent over the medium term and only for a capital purpose, the Council should ensure that its gross external borrowing does not, except in the short term, exceed the total of the capital financing requirement in the preceding year (2023/24 plus the estimates of any additional capital financing requirement for the current (2024/25) and next two financial years. This essentially means that the Council is not borrowing to support revenue expenditure. This indicator allowed the Council some flexibility to borrow in advance of its immediate capital needs in 2023/24. The table below highlights the Council's gross borrowing position against the CFR. The Council has complied with this prudential indicator.

| Gross borrowing and the CFR | 31st March 2023<br>Actual £m | 31st March 2024<br>Budget £m | 31st March 2024<br>Actual £m |
|-----------------------------|------------------------------|------------------------------|------------------------------|
| Gross borrowing position    | 63.060                       | 63.060                       | 63.060                       |
| CFR                         | 73.767                       | 78.190                       | 74.600                       |
| Under / Over funding of CFR | -10.707                      | -15.129                      | -11.540                      |

The lower than estimated CFR reflects re-profiling of spend within the capital programme to 2024/25 and lower than forecast borrowing.

**The Authorised Limit** - the authorised limit is the “affordable borrowing limit” required by s3 of the Local Government Act 2003. Once this has been set, the Council does not have the power to borrow above this level. The table below demonstrates that during 2023/24 the Council has maintained gross borrowing within its authorised limit.

**The Operational Boundary** – the operational boundary is the expected borrowing position of the Council during the year. Periods where the actual position is either below or over the boundary are acceptable subject to the authorised limit not being breached.

**Actual Financing Costs as a Proportion of Net Revenue Stream** - this indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

| Borrowing Limits   | GF £m   | HRA £m | Total £m |
|--|---------|--------|----------|
| Authorised limit   | 9.608   | 79.407 | 89.015   |
| Maximum gross borrowing position                                 | -       | 63.060 | 63.060   |
| Operational boundary   | -       | 63.060 | 63.060   |
| Average gross borrowing position                                 | -       | 63.060 | 63.060   |
|  |         |        |          |
| Budgeted financing costs as a proportion of net revenue stream % | (18.17) | 26.48  | 8.31     |
| Actual financing costs as a proportion of net revenue stream %   | (38.11) | 26.50  | (11.61)  |

### 3. Treasury Position as at 31<sup>st</sup> March 2024

The Council's debt and investment position is organised by the treasury management service in order to ensure adequate liquidity for revenue and capital activities, security for investments and to manage risks within all treasury management activities. Procedures and controls to achieve these objectives are well established both through member reporting detailed in the summary, and through officer activity detailed in the Council's Treasury Management Practices. At the beginning and the end of 2023/24 the Council's treasury (excluding borrowing by finance leases) position was as follows:

| General Fund                    | 31st March 2023 Principal<br>£m | Rate/<br>Return % | Average<br>Life yrs | 31st March 2024 Principal<br>£m | Rate/<br>Return % | Average<br>Life yrs |
|---------------------------------|---------------------------------|-------------------|---------------------|---------------------------------|-------------------|---------------------|
| <b>Total debt</b>               | -                               | -                 | -                   | -                               | -                 | -                   |
| <b>CFR</b>                      | <b>3.785</b>                    | -                 | -                   | <b>4.092</b>                    | -                 | -                   |
| <b>Over / (under) borrowing</b> | <b>(3.785)</b>                  | -                 | -                   | <b>(4.092)</b>                  | -                 | -                   |
| Investments:                    |                                 |                   |                     |                                 |                   |                     |
| - in house                      | 44.108                          | 2.16              | -                   | 43.297                          | 4.92              | -                   |
| <b>Total investments</b>        | <b>44.108</b>                   | <b>2.16</b>       | -                   | <b>43.297</b>                   | <b>4.92</b>       | -                   |

| HRA                             | 31st March 2023 Principal<br>£m | Rate/<br>Return % | Average<br>Life yrs | 31st March 2024 Principal<br>£m | Rate/<br>Return % | Average<br>Life yrs |
|---------------------------------|---------------------------------|-------------------|---------------------|---------------------------------|-------------------|---------------------|
| Fixed rate funding:             |                                 |                   |                     |                                 |                   |                     |
| -PWLB                           | 63.060                          | 4.05              | 31.73               | 63.060                          | 4.05              | 30.73               |
| <b>Total debt</b>               | <b>63.060</b>                   | <b>4.05</b>       | <b>31.73</b>        | <b>63.060</b>                   | <b>4.05</b>       | <b>30.73</b>        |
| <b>CFR</b>                      | <b>69.982</b>                   | -                 | -                   | <b>70.507</b>                   | -                 | -                   |
| <b>Over / (under) borrowing</b> | <b>(6.922)</b>                  | -                 | -                   | <b>(7.447)</b>                  | -                 | -                   |
| Investments:                    |                                 |                   |                     |                                 |                   |                     |
| - in house                      | 16.382                          | 2.16              | -                   | 13.373                          | 4.92              | -                   |
| <b>Total investments</b>        | <b>16.382</b>                   | <b>2.16</b>       | -                   | <b>13.373</b>                   | <b>4.92</b>       | -                   |



## Maturity Structures

The maturity structure of the debt portfolio was as follows:

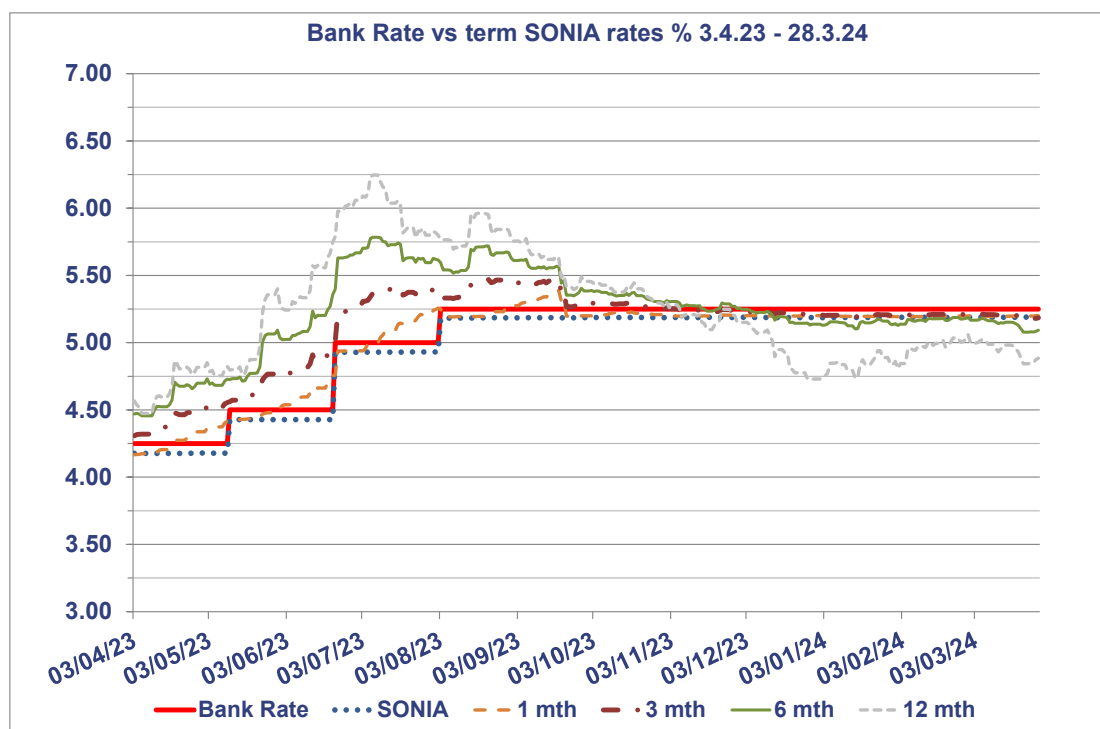
| Duration                       | 31st March 2023<br>Actual £m | 2023/24 original<br>limits % | 31st March 2024<br>Actual £m |
|--------------------------------|------------------------------|------------------------------|------------------------------|
| Under 12 months                | -                            | 20                           | -                            |
| 12 months and within 24 months | -                            | 20                           | -                            |
| 24 months and within 5 years   | -                            | 25                           | -                            |
| 5 years and within 10 years    | 1                            | 75                           | <b>1</b>                     |
| 10 years and within 15 years   | 4                            | 100                          | <b>4</b>                     |
| 15 years and within 50 years   | 58                           | 100                          | <b>58</b>                    |

All investments held by the Council were invested for up to one year, with the exception of £11.962m invested in property funds, which are held for the longer-term, 5 – 10 years.

### 4. The Strategy for 2023/24

#### 4.1 Investment strategy and control of interest rate risk

Investment Benchmarking Data – Sterling Overnight Index Averages (Term) 2023/24



| FINANCIAL YEAR TO QUARTER ENDED 28/03/2024 |            |            |            |            |            |            |
|--|------------|------------|------------|------------|------------|------------|
|  | Bank Rate  | SONIA      | 1 mth      | 3 mth      | 6 mth      | 12 mth     |
| <b>High</b>                                | 5.25       | 5.19       | 5.39       | 5.48       | 5.78       | 6.25       |
| <b>High Date</b>                           | 03/08/2023 | 28/03/2024 | 19/09/2023 | 30/08/2023 | 07/07/2023 | 07/07/2023 |
| <b>Low</b>                                 | 4.25       | 4.18       | 4.17       | 4.31       | 4.46       | 4.47       |
| <b>Low Date</b>                            | 03/04/2023 | 04/04/2023 | 03/04/2023 | 03/04/2023 | 06/04/2023 | 06/04/2023 |
| <b>Average</b>                             | 5.03       | 4.96       | 5.02       | 5.13       | 5.23       | 5.25       |
| <b>Spread</b>                              | 1.00       | 1.01       | 1.22       | 1.17       | 1.33       | 1.77       |

Investment returns picked up throughout the course of 2023/24 as central banks, including the Bank of England, continued to respond to inflationary pressures that were not transitory, and realised that tighter monetary policy was called for.

Starting April at 4.25%, Bank Rate moved up in stepped increases of either 0.25% or 0.5%, reaching 5.25% by August. By the end of the financial year, no further increases were anticipated. Indeed, the market was pricing in a first cut in Bank Rate in either June or August 2024.

The upward sloping yield curve that prevailed throughout 2023/24 meant that local authorities continued to be faced with the challenge of proactive investment of surplus cash, and this emphasised the need for a detailed working knowledge of cashflow projections so that the appropriate balance between maintaining cash for liquidity purposes, and “laddering” deposits on a rolling basis to lock in the increase in investment rates as duration was extended, became an on-going feature of the investment landscape.

With bond markets selling off, UK equity market valuations struggled to make progress, as did property funds, although there have been some spirited, if temporary, market rallies from time to time – including in November and December 2023. However, the more traditional investment options, such as specified investments (simple to understand, and less than a year in duration), have continued to be at the forefront of most local authority investment strategies, particularly given Money Market Funds have also provided decent returns in close proximity to Bank Rate for liquidity purposes. In the latter part of 2023/24, the local authority to local authority market lacked any meaningful measure of depth, forcing short-term investment rates above 7% in the last week of March.

While the Council has taken a prudent approach to investing surplus monies, it is also fully appreciative of changes to regulatory requirements for financial institutions in terms of additional capital and liquidity that came about in the aftermath of the Global Financial Crisis of 2008/09. These requirements have provided a far stronger basis for financial institutions, with annual stress tests by regulators evidencing how institutions are now far more able to cope with extreme stressed market and economic conditions.

#### **4.2 Borrowing strategy and control of interest rate risk**

During 2023/24, the Council maintained an under-borrowed position. This meant that the capital borrowing need, (the Capital Financing Requirement), was not fully funded with loan debt as cash supporting the Council’s reserves, balances and cash flow was used as an interim measure. This strategy was prudent as although near-term investment rates were equal to, and sometimes higher than, long-term borrowing costs, the latter are expected to fall back through 2024 and 2025 as inflation concerns are dampened. The Council has sought to minimise the taking on of long-term borrowing at elevated levels (>4%) and has focused on a policy of internal and temporary borrowing, supplemented by short-dated borrowing (<5 years) as appropriate.

Against this background and the risks within the economic forecast, caution was adopted with the treasury operations. The Executive Director Finance therefore monitored interest rates in financial markets and adopted a pragmatic strategy based upon the following principles to manage interest rate risks

- if it had been felt that there was a significant risk of a sharp FALL in long and short term rates, (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), then long term borrowings would have been postponed, and potential rescheduling from fixed rate funding into short term borrowing would have been considered.
- if it had been felt that there was a significant risk of a much sharper RISE in long and short-term rates than initially expected, perhaps arising from the stickiness of inflation in the major developed economies, then the portfolio position would have been re-appraised. Most likely, fixed rate funding would have been drawn whilst interest rates were lower than they were projected to be in the next few years.

Interest rate forecasts initially suggested further gradual rises in short, medium and longer-term fixed borrowing rates during 2023/24. Bank Rate had initially been forecast to peak at 4.5% but it is now expected to have peaked at 5.25%.

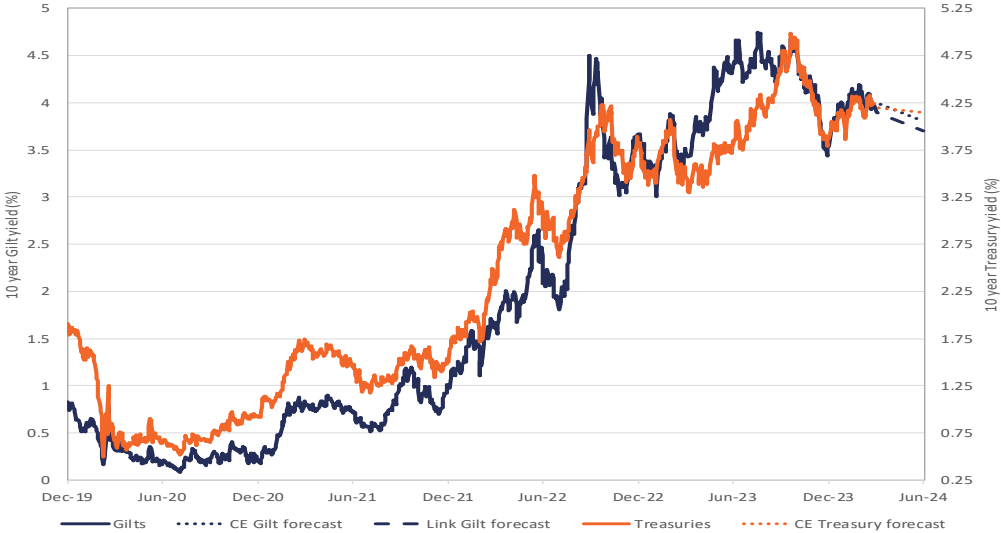
By January it had become clear that inflation was moving down significantly from its 40-year double-digit highs, and the Bank of England signalled in March 2024 that the next move in Bank Rate would be down, so long as upcoming inflation and employment data underpinned that view. Currently the CPI measure of inflation stands at 3.4% but is expected to fall materially below 2% over the summer months and to stay there in 2025 and 2026. Nonetheless, there remain significant risks to that central forecast, mainly in the form of a very tight labour market putting upward pressure on wages, and continuing geo-political inflationary risks emanating from the prevailing Middle East crisis and the Russian invasion of Ukraine.

### **PWLB Borrowing Rates**

PWLB rates are based on gilt (UK Government bonds) yields through HM Treasury determining a specified margin to add to gilt yields. The main influences on gilt yields are Bank Rate, inflation expectations and movements in US treasury yields. Inflation targeting by the major central banks has been successful over the last 30 years in lowering inflation and the real equilibrium rate for central rates has fallen considerably due to the high level of borrowing by consumers: this means that central banks do not need to raise rates as much now to have a major impact on consumer spending, inflation, etc. This has pulled down the overall level of interest rates and bond yields in financial markets over the last 30 years. Indeed, in recent years many bond yields up to 10 years in the Eurozone turned negative on expectations that the EU would struggle to get growth rates and inflation up from low levels. In addition, there has, at times, been an inversion of bond yields in the US whereby 10-year yields have fallen below shorter-term yields. In the past, this has been a precursor of a recession.

However, since early 2022, yields have risen dramatically in all the major developed economies, first as economies opened post-Covid; then because of the inflationary impact of the war in Ukraine in respect of the supply side of many goods. In particular, rising cost pressures emanating from shortages of energy and some food categories have been central to inflation rising rapidly. Furthermore, at present the FOMC, ECB and Bank of England are all being challenged by levels of persistent inflation that are exacerbated by very tight labour markets and high wage increases relative to what central banks believe to be sustainable.

# Graph of UK gilt yields v. US treasury yields



Gilt yields have generally been on a continual rise since the start of 2021, peaking in the autumn of 2023. Currently, yields are broadly range bound between 3.5% and 4.25%.

At the close of the day on 28 March 2024, all gilt yields from 1 to 50 years were between 3.81% and 4.56%, with the 1 year being the highest and 6-7 years being the lowest yield.

Regarding PWLB borrowing rates, the various margins attributed to their pricing are as follows: -

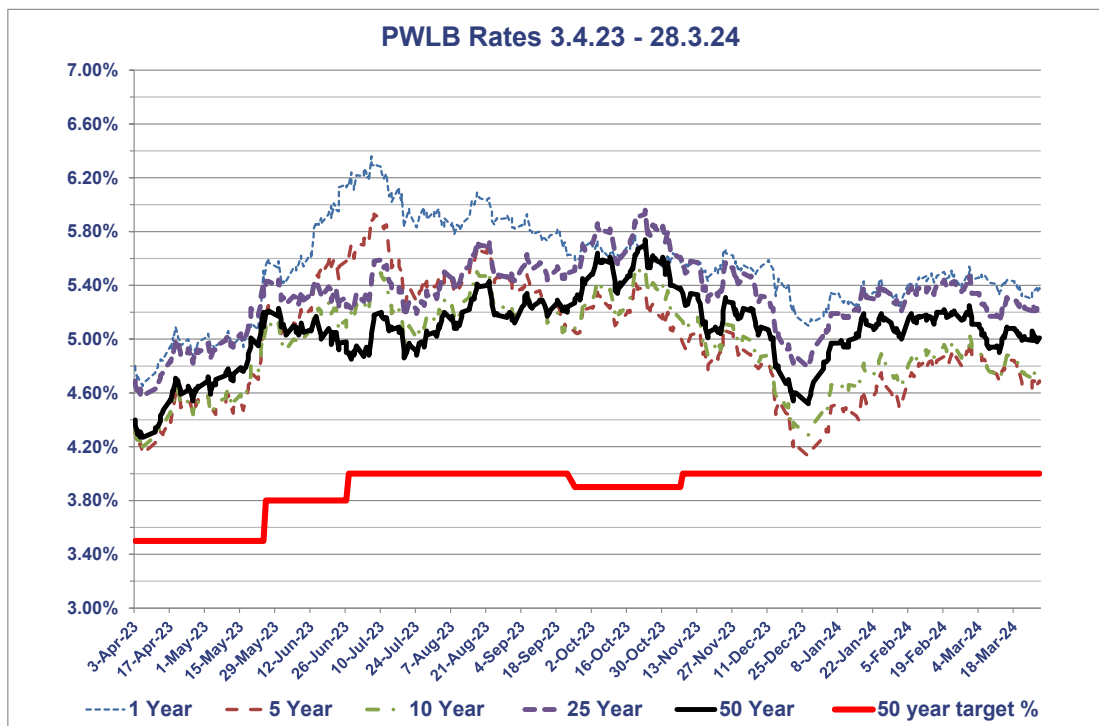
- **PWLB Standard Rate** is gilt plus 100 basis points (G+100bps)
- **PWLB Certainty Rate** is gilt plus 80 basis points (G+80bps)
- **Local Infrastructure Rate** is gilt plus 60bps (G+60bps)
- **HRA Borrowing rate** is gilt plus 40 40bps (G+40bps)

There is likely to be a fall in gilt yields and PWLB rates across the whole curve over the next one to two years as Bank Rate falls and inflation (on the Consumer Price Index measure) moves below the Bank of England’s 2% target.

As a general rule, short-dated gilt yields will reflect expected movements in Bank Rate, whilst medium to long-dated yields are driven primarily by the inflation outlook.

The Bank of England is also embarking on a process of Quantitative Tightening. The Bank’s original £895bn stock of gilt and corporate bonds will gradually be sold back into the market over several years. The impact this policy will have on the market pricing of gilts, while issuance is markedly increasing, and high in historic terms, is an unknown at the time of writing.

The graph and tables for PWLB rates below and in Appendix 2 show, for a selection of maturity periods, the average borrowing rates, the high and low points in rates, spreads and individual rates at the start and the end of the financial year.



## 5. Borrowing Outturn for 2023/24

### Treasury Borrowing

Due to the elevated cost of borrowing long-term, no borrowing was undertaken during the year.

### Borrowing in Advance of Need

The Council has not borrowed more than, or in advance of, its needs, purely in order to profit from the investment of the extra sums borrowed.

### Rescheduling

No rescheduling was done during the year as the approximate 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

## 6. Investment Outturn for 2023/24

**Investment Policy** – the Council’s investment policy is governed by DLUHC investment guidance, which has been implemented in the annual investment strategy approved by the Council on 28th February 2023. This policy sets out the approach for choosing investment counterparties, and is based on credit ratings provided by the three main credit rating agencies, supplemented by additional market data (such as rating outlooks, credit default swaps, bank share prices etc).

The investment activity during the year conformed to the approved strategy, and the Council had no liquidity difficulties.

**Resources** – the Council’s cash balances comprise revenue and capital resources and cash flow monies. The Council’s core cash resources comprised the following:

| Balance Sheet<br>Resources General Fund | 31st March<br>2023 £m | 31 <sup>st</sup> March<br>2024 £m |
|---|-----------------------|-----------------------------------|
| Balances                                | 9.615                 | <b>10.737</b>                     |
| Earmarked Reserves                      | 15.560                | <b>20.134</b>                     |
| Provisions                              | 1.825                 | <b>2.426</b>                      |
| Usable Capital Receipts                 | 12.601                | <b>11.612</b>                     |
| Capital Grants Unapplied                | 0.975                 | <b>1.221</b>                      |
| <b>Total GF</b>                         | <b>40.576</b>         | <b>46.130</b>                     |
| Balance Sheet<br>Resources HRA          | 31st March<br>2023 £m | 31 <sup>st</sup> March<br>2024 £m |
| Balances                                | 2.761                 | <b>2.220</b>                      |
| Earmarked Reserves                      | 10.599                | <b>9.708</b>                      |
| Provisions                              | -                     | -                                 |
| Usable Capital Receipts                 | 1.71                  | <b>2.320</b>                      |
| <b>Total HRA</b>                        | <b>15.07</b>          | <b>14.248</b>                     |
| <b>Total Authority<br/>Resources</b>    | <b>55.646</b>         | <b>60.378</b>                     |

**Investments held by the Council** – the Council maintained an average balance of £67.4m of internally managed funds. The internally managed funds earned an average rate of return of 4.92%. The comparable performance indicator is the average 3 month SONIA rate which was 5.13%. This compared with a budget assumption of £38.2m investment balances earning an average rate of 3.4%.

## 7. Performance Measurement

One of the key requirements in the Code is the formal introduction of performance measurement relating to investments, debt and capital financing activities. Whilst investment performance criteria have been well developed and universally accepted, debt performance indicators continue to be a more problematic area with the traditional average portfolio rate of interest acting as the main guide. The Council's performance indicators were set out in the Annual Treasury Management Strategy Statement.

This service has set the following local performance indicator:

➤ *Average external interest receivable in excess of 3 month SONIA rate;*

Whilst the assumed benchmark for local authorities is the 7 day SONIA rate, a higher target is set for internal performance.

The actual return of 4.92% is compared to the average 3 month SONIA of 5.13% (0.21% below target). This is due to the sharp increase in interest rates between 1<sup>st</sup> April 2023 and 31<sup>st</sup> March 2024, with some investments fixed at lower rates at the beginning of the year.

## 8. The Economy and Interest Rates

### UK Economy

Against a backdrop of stubborn inflationary pressures, the Russian invasion of Ukraine, and war in the Middle East, UK interest rates have continued to be volatile right across the curve, from Bank Rate through to 50-year gilt yields, for all of 2023/24.

Markets have sought an end to central banks' on-going phase of keeping restrictive monetary policy in place on at least one occasion during 2023/24 but to date only the Swiss National Bank has cut rates and that was at the end of March 2024.

UK, EZ and US 10-year yields have all stayed stubbornly high throughout 2023/24. The table below provides a snapshot of the conundrum facing central banks: inflation is easing, albeit gradually, but labour markets remain very tight by historical comparisons, making it an issue of fine judgment as to when rates can be cut.

|                          | <b>UK</b>                  | <b>Eurozone</b>           | <b>US</b>             |
|--------------------------|----------------------------|---------------------------|-----------------------|
| <b>Bank Rate</b>         | 5.25%                      | 4%                        | 5.25%-5.5%            |
| <b>GDP</b>               | -0.3%q/q Q4<br>(-0.2%/y/y) | +0.0%q/q Q4<br>(0.1%/y/y) | 2.0% Q1<br>Annualised |
| <b>Inflation</b>         | 3.4%/y/y (Feb)             | 2.4%/y/y (Mar)            | 3.2%/y/y (Feb)        |
| <b>Unemployment Rate</b> | 3.9% (Jan)                 | 6.4% (Feb)                | 3.9% (Feb)            |

The Bank of England sprung no surprises in their March meeting, leaving interest rates at 5.25% for the fifth time in a row and, despite no MPC members no longer voting to raise interest rates, it retained its relatively hawkish guidance. The Bank's communications suggest the MPC is gaining confidence that inflation will fall sustainably back to the 2.0% target. However, although the MPC noted that "the restrictive stance of monetary policy is weighing on activity in the real economy, is leading to a looser labour market and is bearing down on inflationary pressures", conversely it noted that key indicators of inflation persistence remain elevated and policy will be "restrictive for sufficiently long" and "restrictive for an extended period".

Of course, the UK economy has started to perform a little better in Q1 2024 but is still recovering from a shallow recession through the second half of 2023. Indeed, Q4 2023 saw negative GDP growth of -0.3% while y/y growth was also negative at -0.2%.

But it was a strange recession. Unemployment is currently sub 4%, against a backdrop of still over 900k of job vacancies, and annual wage inflation is running at above 5%. With gas and electricity price caps falling in April 2024, the CPI measure of inflation - which peaked at 11.1% in October 2022 - is now due to slide below the 2% target rate in April and to remain below that Bank of England benchmark for the next couple of years, according to Capital Economics. The Bank of England still needs some convincing on that score, but upcoming inflation and employment releases will settle that argument shortly. It is noted that core CPI was still a heady 4.5% in February and, ideally, needs to fall further.

Shoppers largely shrugged off the unusually wet weather in February, whilst rising real household incomes should support retail activity throughout 2024. Furthermore, the impact of higher interest rates on household interest payments is getting close to

its peak, even though fixed rate mortgage rates on new loans have shifted up a little since falling close to 4.5% in early 2024.

From a fiscal perspective, the further cuts to national insurance tax (from April) announced in the March Budget will boost real household disposable income by 0.5 - 1.0%. After real household disposable income rose by 1.9% in 2023, Capital Economics forecast it will rise by 1.7% in 2024 and by 2.4% in 2025. These rises in real household disposable income, combined with the earlier fading of the drag from previous rises in interest rates, means GDP growth of 0.5% is envisaged in 2024 and 1.5% in 2025. The Bank of England is less optimistic than that, seeing growth struggling to get near 1% over the next two to three years.

As for equity markets, the FTSE 100 has risen to nearly 8,000 and is now only 1% below the all-time high it reached in February 2023. The modest rise in UK equities in February was driven by strong performances in the cyclical industrials and consumer discretionary sectors, whilst communications and basic materials have fared poorly.

Despite its performance, the FTSE 100 is still lagging behind the S&P 500, which has been at an all-time high for several weeks.

### **USA Economy.**

Despite the markets willing the FOMC to cut rates as soon as June 2024, the continued resilience of the economy, married to sticky inflation, is providing a significant headwind to a change in monetary policy. Markets currently anticipate three rate cuts this calendar year, but two or less would not be out of the question. Currently, policy remains flexible but primarily data driven.

In addition, the Fed will want to shrink its swollen \$16 trillion balance sheet at some point. Just because the \$ is the world's foremost reserve currency (China owns over \$1 trillion) does not mean the US can continually run a budget deficit. The mix of stubborn inflation and significant treasury issuance is keeping treasury yields high. The 10 year stands at 4.4%.

As for inflation, it is currently a little above 3%. The market is not expecting a recession, but whether rates staying high for longer is conducive to a soft landing for the economy is uncertain, hence why the consensus is for rate cuts this year and into 2025...but how many and when?

### **EZ Economy.**

Although the Euro-zone inflation rate has fallen to 2.4%, the ECB will still be mindful that it has further work to do to dampen inflation expectations. However, with growth steadfastly in the slow lane (GDP flatlined in 2023), a June rate cut from the current 4% looks probable.

## **9. Investment in Property Funds**

Investment in property funds was included within the Commercial Investment Strategy, with the aim of generating improved returns of c.4-5% p.a. (plus asset growth) being long term investments of between 5 – 10 years (minimum) in order to make the necessary returns (after set up costs). Utilising the capital receipt proceeds of the sale of the Golf Course, a budget of £12m was allocated to long-term investment in a number of property funds. To date, the Council has invested £1.85m with Schrodgers UK Real Estate Fund, £6.057m with Threadneedle Property Unit Trust, and £4.057m with Hermes Federated Property Unit Trust. Total investment £11.962m.



| Fund Valuations                      | Investment | Valuation<br>31/03/2022 | Valuation<br>31/03/2023 | Valuation<br>31/03/2024 |
|--------------------------------------|------------|-------------------------|-------------------------|-------------------------|
| Schroders UK Real Estate Fund        | 1,848,933  | 2,139,618               | 1,727,176               | 1,567,521               |
| Valuation Increase / (reduction)     |            | 290,685                 | (121,757)               | (281,412)               |
| Threadneedle Property Unit Trust     | 2,000,249  | 2,097,097               | 1,732,373               | 1,648,601               |
| Valuation Increase / (reduction)     |            | 96,848                  | (267,875)               | (351,648)               |
| Threadneedle Property Unit Trust     | 4,056,536  | 4,407,163               | 3,640,676               | 3,464,625               |
| Valuation Increase / (reduction)     |            | 350,627                 | (415,860)               | (591,912)               |
| Hermes Federated Property Unit Trust | 4,056,500  | 4,450,808               | 3,741,712               | 3,462,647               |
| Valuation Increase / (reduction)     |            | 394,308                 | (314,788)               | (593,853)               |
| Total                                | 11,962,218 | 13,094,687              | 10,841,938              | 10,143,394              |
| Valuation Increase / (reduction)     |            | 1,132,469               | (1,120,280)             | (1,818,824)             |

The Council received £487k in dividends from its property fund investments in 2023/24 (£458k in 2022/23), £1.598m in total since 2018/19, offset against the valuation decrease of £1.819m over the same period.

## 10. Other Issues

### IFRS 9 fair value of investments

Following the consultation undertaken by the Department of Levelling Up, Housing and Communities [DLUHC] on IFRS 9, the Government has extended the mandatory statutory override for local authorities to reverse out all unrealised fair value movements resulting from pooled investment funds to 31<sup>st</sup> March 2025. Local authorities are required to disclose the net impact of the unrealised fair value movements in a separate unusable reserve throughout the duration of the override in order for the Government to keep the override under review and to maintain a form of transparency.

Risk management will need to take account of the 2018/19 Accounting Code of Practice proposals for the valuation of investments. Key considerations are:

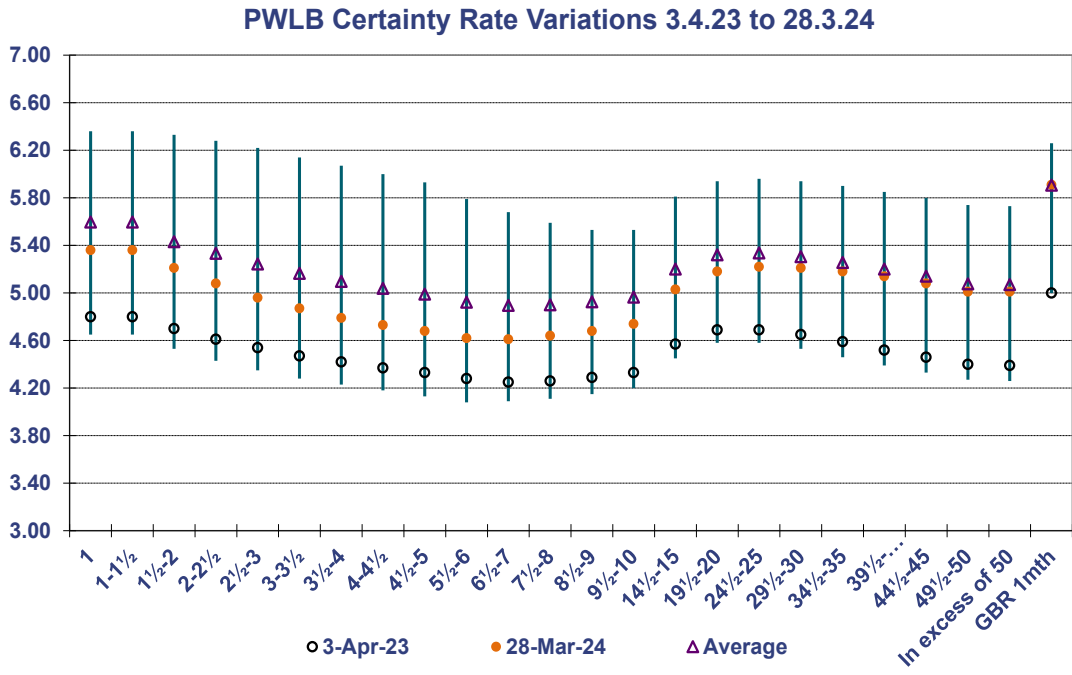
- Expected credit loss model. Whilst this should not be material for vanilla treasury investments such as bank deposits, this does impact our investment in property funds
- The valuation of investments previously valued under the available for sale category e.g., equity related to the “commercialism” agenda, property funds, equity funds and similar, will be changed to **Fair Value through the Profit and Loss (FVPL)**.

**PRUDENTIAL AND TREASURY INDICATORS**

**APPENDIX 1**

| <b>1. PRUDENTIAL INDICATORS</b>                       | <b>2022/23</b>  | <b>2023/24</b>  | <b>2023/24</b> |
|---|-----------------|-----------------|----------------|
| <b>Extract from budget and rent setting report</b>    | <b>Actual</b>   | <b>Original</b> | <b>Actual</b>  |
| <b>Capital Expenditure</b>                            | <b>£m</b>       | <b>£m</b>       | <b>£m</b>      |
| <b>Non - HRA</b>                                      | <b>4.889</b>    | <b>30.988</b>   | <b>12.416</b>  |
| <b>HRA</b>  | <b>13.876</b>   | <b>14.613</b>   | <b>11.320</b>  |
| <b>TOTAL</b>  | <b>18.765</b>   | <b>45.601</b>   | <b>23.737</b>  |
| <b>Ratio of financing costs to net revenue stream</b> | <b>%</b>        | <b>%</b>        | <b>%</b>       |
| <b>Non - HRA</b>                                      | <b>(26.854)</b> | <b>(18.17)</b>  | <b>(38.11)</b> |
| <b>HRA</b>  | <b>29.596</b>   | <b>26.48</b>    | <b>26.50</b>   |
| <b>Gross borrowing requirement General Fund</b>       | <b>£m</b>       | <b>£m</b>       | <b>£m</b>      |
| brought forward 1 April                               | 3.937           | 3.909           | 3.785          |
| carried forward 31 March                              | 3.989           | 7.566           | 4.300          |
| in year borrowing requirement                         | 0.052           | 3.657           | 0.515          |
| <b>Gross borrowing requirement HRA</b>                | <b>£m</b>       | <b>£m</b>       | <b>£m</b>      |
| brought forward 1 April                               | 69.893          | 69.982          | 69.982         |
| carried forward 31 March                              | 69.981          | 73.639          | 70.507         |
| in year borrowing requirement                         | 0.088           | 3.657           | 0.526          |
|   | <b>£m</b>       | <b>£m</b>       | <b>£m</b>      |
| <b>Gross debt</b>                                     | <b>63.060</b>   | <b>63.060</b>   | <b>63.060</b>  |
| <b>Capital Financing Requirement</b>                  | <b>£m</b>       | <b>£m</b>       | <b>£m</b>      |
| <b>Non – HRA</b>                                      | <b>3.785</b>    | <b>7.352</b>    | <b>4.092</b>   |
| <b>HRA</b>  | <b>69.981</b>   | <b>73.639</b>   | <b>70.507</b>  |
| <b>TOTAL</b>  | <b>73.766</b>   | <b>80.990</b>   | <b>74.600</b>  |
| <b>Annual change in Capital Financing Requirement</b> | <b>£m</b>       | <b>£m</b>       | <b>£m</b>      |
| <b>Non – HRA</b>                                      | <b>(0.152)</b>  | <b>3.443</b>    | <b>0.308</b>   |
| <b>HRA</b>  | <b>0.088</b>    | <b>3.657</b>    | <b>0.526</b>   |
| <b>TOTAL</b>  | <b>(0.064)</b>  | <b>7.100</b>    | <b>0.833</b>   |

| <b>2. TREASURY MANAGEMENT INDICATORS</b>                     | <b>2022/23</b> | <b>2023/24</b>  | <b>2023/24</b> |
|--|----------------|-----------------|----------------|
|  | <b>Actual</b>  | <b>Original</b> | <b>Actual</b>  |
|  | <b>£m</b>      | <b>£m</b>       | <b>£m</b>      |
| <b>Authorised Limit for external debt - General Fund</b>     |                |                 |                |
| borrowing  | 8.029          | 9.608           | 9.608          |
| other long term liabilities                                  | -              | -               | -              |
| TOTAL  | 8.029          | 9.608           | 9.608          |
| <b>Authorised Limit for external debt - HRA</b>              |                |                 |                |
| borrowing  | 79.407         | 79.407          | 79.407         |
| other long term liabilities                                  | -              | -               | -              |
| TOTAL  | 79.407         | 79.407          | 79.407         |
| <b>Operational Boundary for external debt - General Fund</b> | <b>£m</b>      | <b>£m</b>       | <b>£m</b>      |
| borrowing  | -              | -               | -              |
| other long term liabilities                                  | -              | -               | -              |
| TOTAL  | -              | -               | -              |
| <b>Operational Boundary for external debt - HRA</b>          | <b>£m</b>      | <b>£m</b>       | <b>£m</b>      |
| borrowing  | 63.060         | 63.060          | 63.060         |
| other long term liabilities                                  | -              | -               | -              |
| TOTAL  | 63.060         | 63.060          | 63.060         |
| <b>Actual external debt</b>                                  | <b>£m</b>      | <b>£m</b>       | <b>£m</b>      |
|  | 63.060         | 63.060          | 63.060         |



**HIGH/LOW/AVERAGE PWLB RATES FOR 2023/24**

|                | 1 Year     | 5 Year     | 10 Year    | 25 Year    | 50 Year    |
|----------------|------------|------------|------------|------------|------------|
| <b>Low</b>     | 4.65%      | 4.13%      | 4.20%      | 4.58%      | 4.27%      |
| <b>Date</b>    | 06/04/2023 | 27/12/2023 | 06/04/2023 | 06/04/2023 | 05/04/2023 |
| <b>High</b>    | 6.36%      | 5.93%      | 5.53%      | 5.96%      | 5.74%      |
| <b>Date</b>    | 06/07/2023 | 07/07/2023 | 23/10/2023 | 23/10/2023 | 23/10/2023 |
| <b>Average</b> | 5.54%      | 4.99%      | 4.97%      | 5.34%      | 5.08%      |
| <b>Spread</b>  | 1.71%      | 1.80%      | 1.33%      | 1.38%      | 1.47%      |