

## APPENDIX 1

### TREASURY MANAGEMENT MID YEAR REVIEW REPORT 2022/23

#### 1. INTRODUCTION AND BACKGROUND

The Chartered Institute of Public Finance and Accountancy's Code of Practice on Treasury Management 2009 was adopted by this Council in February 2010 and this Council fully complies with its requirements. The Code was revised in 2011 and further revised in 2017.

The primary requirements of the Code are as follows:

1. Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.
2. Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.
3. Receipt by the Council of an annual treasury management strategy report (including the annual investment strategy and minimum revenue provision report) for the year ahead, a mid year review and an annual review report of the previous year.
4. 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, which in this Council is the Chief Officer Resources.
5. Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specified named body which in this Council is the Corporate Overview & Performance Scrutiny Committee.

Treasury management in this context is defined as:

*"The management of the local authority's 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."*

The purpose of this report is to meet one of the above requirements of the CIPFA Code, namely the mid-year review of treasury management activities, for the financial year 2022/23.

#### 2. THIS TREASURY MANAGEMENT MID YEAR REVIEW REPORT COVERS

- ❖ Economic Background during the period
- ❖ Interest Rate Forecast
- ❖ Treasury Advisors
- ❖ The Council's treasury position as at 30 September 2022;
- ❖ Borrowing and investment rates for the first half of 2022/23;
- ❖ Mid-year review of the borrowing strategy 2022/23;
- ❖ Borrowing outturn for the first half of 2022/23;
- ❖ Debt rescheduling for the first half of 2022/23;

## APPENDIX 1

### TREASURY MANAGEMENT MID YEAR REVIEW REPORT 2022/23

- ❖ Compliance with treasury limits and Prudential Indicators for the first half of 2022/23;
- ❖ Mid-year review of the investment strategy for 2022/23;
- ❖ Investment outturn for the first half of 2022/23;
- ❖ Other treasury management issues.

### 3. ECONOMIC BACKGROUND DURING PERIOD

The second quarter of 2022/23 saw:

- GDP revised upwards in Q1 2022/23 to +0.2% q/q from -0.1%, which means the UK economy has avoided recession for the time being;
- Signs of economic activity losing momentum as production fell due to rising energy prices;
- CPI inflation eased from 10.1% in July to 9.9% in August, though inflation has not peaked yet. The easing in August was mainly due to a decline in fuel prices reducing fuel inflation from 43.7% to 32.1%. And with the oil price now just below \$90pb, we would expect to see fuel prices fall further in the coming months.- The unemployment rate fall to a 48-year low of 3.6% due to a large shortfall in labour supply;
- Bank Rate rise by 100bps over the quarter, taking Bank Rate to 2.25% with further rises to come;
- Gilt yields surge and sterling fall following the “fiscal event” of the new Prime Minister and Chancellor on 23rd September.

The Monetary Policy Committee (MPC) has now increased interest rates seven times in as many meetings in 2022 and has raised rates to their highest level since the Global Financial Crisis. Even so, coming after the Fed and ECB raised rates by 75 basis points (bps) in their most recent meetings, the Bank of England’s latest 50 basis points hike looks relatively conservative. However, the UK’s status as a large importer of commodities, which have jumped in price, means that households in the UK are now facing a much larger squeeze on their real incomes.

we now expect the MPC to increase interest rates further and faster, from 2.25% to a peak of 4.50% in February 2023. The combination of the government’s fiscal loosening, the tight labour market and sticky inflation expectations means that the MPC raised interest rates by 75bps at the policy meetings in November (to 3.00%) and 50 basis points in December (to 3.50%). It is expected that further 50 basis point hikes in February and March will increase the rate to 4.50%. Market expectations for what the MPC will do are volatile. If Bank Rate climbs to these levels the housing market looks very vulnerable, which is one reason why the peak in our forecast is lower than the peak of 5.50% - 5.75% priced into the financial markets at present.

## APPENDIX 1

### TREASURY MANAGEMENT MID YEAR REVIEW REPORT 2022/23

#### 4. INTEREST RATE FORECASTS

The Council's treasury advisor, Link Group, has provided the following forecast:

Link Group Interest Rate View	19.12.22												
	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25
BANK RATE	3.50	4.25	4.50	4.50	4.50	4.00	3.75	3.50	3.25	3.00	2.75	2.50	2.50
3 month ave earnings	3.60	4.30	4.50	4.50	4.50	4.00	3.80	3.30	3.00	3.00	2.80	2.50	2.50
6 month ave earnings	4.20	4.50	4.60	4.50	4.20	4.10	3.90	3.40	3.10	3.00	2.90	2.60	2.60
12 month ave earnings	4.70	4.70	4.70	4.50	4.30	4.20	4.00	3.50	3.20	3.10	3.00	2.70	2.70
5 yr PWLB	4.20	4.20	4.20	4.10	4.00	3.90	3.80	3.60	3.50	3.40	3.30	3.20	3.10
10 yr PWLB	4.30	4.40	4.40	4.30	4.10	4.00	3.90	3.80	3.60	3.50	3.40	3.30	3.30
25 yr PWLB	4.60	4.60	4.60	4.50	4.40	4.20	4.10	4.00	3.90	3.70	3.60	3.50	3.50
50 yr PWLB	4.30	4.30	4.30	4.20	4.10	3.90	3.80	3.70	3.60	3.50	3.30	3.20	3.20

The latest forecast on 19th December sets out a view that both short 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, whilst the government is providing a package of fiscal loosening to try and protect households and businesses from the ravages of ultra-high wholesale gas and electricity prices.

As shown in the forecast table above, further increases in Bank Rate are now expected during 2023/24, from 3.5% as at the date of this report to 4.5% in quarter 1 of 2023/24, with subsequent decreases during 2024/25 and 2025/26.

#### Forecasts for PWLB rates and gilt and treasury yields

As the interest forecast table for PWLB certainty rates above shows, there is likely to be a rise over the forecast period, with some degree of uplift due to rising treasury yields in the US.

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 above 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 27th September sets out a view that both short 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, whilst the government is providing a package of fiscal loosening to try and protect households and businesses from the ravages of ultra-high wholesale gas and electricity prices.

The increase in PWLB rates reflects a broad sell-off in sovereign bonds internationally but more so the disaffection investors have with the position of the UK public finances after September's "fiscal event". To that end, the MPC has tightened short-term interest rates with a view to trying to slow the economy sufficiently to keep the secondary effects of inflation – as measured by wage rises – under control, but its job is that much harder now.

## APPENDIX 1

### TREASURY MANAGEMENT MID YEAR REVIEW REPORT 2022/23

#### **Gilt and treasury yields**

Throughout 2022/23, gilt yields have been on an upward trend. They were initially caught up in the global surge in bond yields triggered by the surprisingly strong rise in CPI inflation in the US in May. The rises in two-year gilt yields (to a peak of 2.37% on 21st June) and 10-year yields (to a peak of 2.62%) took them to their highest level since 2008 and 2014 respectively.

However, the upward trend was exceptionally sharp at the end of September as investors demanded a higher risk premium and expected faster and higher interest rate rises to offset the government's extraordinary fiscal stimulus plans. The 30-year gilt yield rose from 3.60% to 5.10% following the "fiscal event", which threatened financial stability by forcing pension funds to sell assets into a falling market to meet cash collateral requirements.

In response, the Bank did two things. First, it postponed its plans to start selling some of its quantitative easing (QE) gilt holdings until 31st October. Second, it committed to buy up to £65bn of long-term gilts to "restore orderly market conditions" until 14th October. In other words, the Bank is restarting QE, although for financial stability reasons rather than monetary policy reasons.

Since the Bank's announcement on 28th September, the 30-year gilt yield has fallen back from 5.10% to 3.83%. The 2-year gilt yield dropped from 4.70% to 4.30% and the 10-year yield fell back from 4.55% to 4.09%.

#### **5. TREASURY ADVISORS**

The Council uses external treasury management advisors. The Council recognises that responsibility for Treasury Management decisions remains with the Authority at all times and will ensure that undue reliance is not placed upon our external service providers.

It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented and subjected to regular review.

The Council retendered for the provision of Treasury Management advisory services during 2022. This resulted in the appointment of Link Asset Services for a period of two years from 1<sup>st</sup> May 2022 until 30<sup>th</sup> April 2024, with an option to extend for a further two years at 12-month intervals.

## APPENDIX 1

### TREASURY MANAGEMENT MID YEAR REVIEW REPORT 2022/23

#### 6. TREASURY POSITION AS AT 30 SEPTEMBER 2022

The Council's debt and investment position at the beginning of the year and the end of the half year was as follows:

The table illustrates that the total debt outstanding as at 30 September 2022 was £228.8 million, comprising of long term debt of £169.45 million and short term debt of £59.4 million.

	31March 2022 Principal	Average Rate/ Return	30Sept 2022 Principal	Average Rate/ Return	Increase/ (Decrease) in Borrowing
	<u>£000</u>		<u>£000</u>		<u>£000</u>
Fixed Rate Funding:					
- PWLB	74,067	4.06%	74,056	4.02%	(10)
- Market Loans	14,000	1.40%	18,000	1.26%	4,000
Variable Rate Funding:					
- Market (LOBO *)	4,000	4.5%	4,000	4.50%	0
Interest Free Loans:					
Welsh Government	73,395	0.00%	73,395	0.00%	0
<b>Total Long Term Debt</b>	<b>165,462</b>	<b>3.70%</b>	<b>169,451</b>	<b>3.53%</b>	<b>3,990</b>
Short Term Loans(<365 days)	62,365	0.32%	59,365	0.51%	(3,000)
<b>Total Debt</b>	<b>227,827</b>	<b>2.35%</b>	<b>228,816</b>	<b>2.43%</b>	<b>990</b>
Investments:					
- Short Term	100,000	0.04%	96,300	0.82%	(3,700)
<b>Total Investments</b>	<b>100,000</b>		<b>96,300</b>		<b>(3,700)</b>

\* LOBO – Lenders Option Borrowers Option. This loan has a fixed rate for the first two years of 3.85%. The remaining period of the loan (which we are now in) has a rate of 4.5%, but the lender can increase this rate at six month intervals.

## APPENDIX 1

### TREASURY MANAGEMENT MID YEAR REVIEW REPORT 2022/23

#### 7. BORROWING AND INVESTMENT RATES IN 2022/23

The following table displays a selection of interest rates prevailing as at 1<sup>st</sup> April 2022 and 30<sup>th</sup> September 2022.

	01/04/2022	30/09/2022
Bank Base Rate	0.75%	2.25%
1 Month SONIA Rate	0.69%	2.26%
PWLB 10 year Maturity	2.66%	5.15%
PWLB 15 year maturity	2.83%	5.14%
PWLB 25 year maturity	2.85%	4.98%

#### 8. MID YEAR REVIEW OF THE BORROWING STRATEGY FOR 2022/23

The Treasury Management Strategy Statement for 2022/23 was approved by Council in March 2022. The Borrowing Strategy adopted as part of this was as follows:

*To utilise the Authority's overdraft facility:*

To fund unexpected daily cash deficits;  
To fund temporary cash shortfalls where there are no other sources of funding available within the marketplace.

*To borrow over the short term:*

To fund temporary cash shortfalls;  
To maintain a suitably balanced maturity profile; to make short term savings required in order to meet budgetary constraints;  
In anticipation of securing longer term loans at more attractive rates.

*To borrow over the long term:*

To reduce the Authority's average cost of borrowing;  
To maintain a stable, longer term portfolio;  
To maximise the potential for future debt rescheduling.

*If appropriate to avoid all new external borrowing:*

To maximise savings in the short term;  
To run down temporary investment levels;  
To minimise exposure to interest rate and credit risk.

Borrowings undertaken during the period (see section 7 below) have been done so in accordance with this strategy and has focused on short term borrowings in order to minimise borrowing costs. Current short-term borrowing rates continue to be very low, however are likely to increase following the forecast increases to the Bank of England Base Rate. The Authority is therefore taking advantage of such rates and is predominantly borrowing short term where necessary to fund the remainder of its capital expenditure and maturing debt until such time the market indicates that long term rates would be more advantageous. In March 2021 the Welsh Government awarded the Authority an interest free specific loan in relation to the Rail Track project, whilst this has resulted in an increase to the level of the Council's longer-term debt this

## APPENDIX 1

### TREASURY MANAGEMENT MID YEAR REVIEW REPORT 2022/23

resource has reduced the need to borrow externally in the first half of the 2022/23 financial year.

In the current economic climate, it is considered that the approved strategy is still fit for purpose and therefore no revisions are proposed.

### 9. BORROWING OUTTURN FOR THE FIRST HALF OF 2022/23

#### Long Term Borrowing

##### *Definition*

Long term borrowing relates to debt taken out for a period of greater than one year. It is taken out for periods of 1 year up to 50 years. This borrowing is required to finance capital expenditure undertaken in the year that is funded through:

- Borrowing approvals from Welsh Government, known as un-hypothecated supported borrowing (USB), for which revenue support for the borrowing costs is provided through the revenue support grant;
- Prudential borrowing, for which borrowing costs are funded through revenue savings.

##### *Total outstanding as at 30<sup>th</sup> September 2022*

The total long term debt outstanding as at 30<sup>th</sup> September 2022 was £169.45 million. This is made up of debt taken from the Public Works Loan Board (PWLB), from other local authorities (through the market place), Specific Welsh Government Loans and from the market (LOBO). This debt is due to be repaid within the following years:

Maturing Within	£000s
1YR	2,909
1-2YRS	8,764
2-3YRS	15,451
3-4YRS	15,277
4-5YRS	12,609
5-6YRS	6,037
6-10YRS	19,980
10-15YRS	9,570
15+ YRS	78,854
<b>Total</b>	<b>169,451</b>

##### *New borrowings for the First Half of 2022/23*

Long-Term borrowings of £8m (Market Loans) have been repaid during the financial year. New Market Loans of £12m have been received to 30 September 2022.

#### Short Term Borrowing

##### *Definition*

Short term borrowing relates to debt taken out for a period of less than one year i.e. it will all be fully repaid within a year. These short term loans are taken out to manage the Authority's short term cash flow i.e. to fund deficits in cash flow on a daily basis

## APPENDIX 1

### TREASURY MANAGEMENT MID YEAR REVIEW REPORT 2022/23

pending receipt of income from grants or other sources, or pending the taking out of longer term debt to fund capital expenditure whilst we wait for advantageous longer term borrowing opportunities. Current short term borrowing rates are very low and are forecast to stay at these levels for the short term. The Authority is therefore taking advantage of such rates and is borrowing short term to fund its capital expenditure and maturing debt until such time the market indicates that long term rates are more advantageous.

#### **Total outstanding as at 30<sup>th</sup> September 2022**

The total short term debt outstanding as at 30<sup>th</sup> September 2022 was £59.4 million. This is made up of debt taken from other local authorities through the market place.

#### **New borrowings for the First Half Year of 2022/23**

Appendix A lists the short term loan activity during for the first half year and shows that over the period a total of £62.4 million loans were brought forward from the previous year and £36million of new short term loans were raised. A total of £39 million of these loans were repaid during the first half year, leaving a balance outstanding as at 30<sup>th</sup> September 2022 of £59.4 million.

The following table gives a summary which shows that the average rate of interest paid was in line with the benchmark.

	Total Value of Loans during the period	Average Loan	Interest paid during the period	Average Interest Rate	Average Loan Days during 2022/23	Benchmark Interest Rate *
<b>Short Term borrowing</b>	£98.4M	£3.8M	£73K	0.51%	206.7	1.70%

\* Benchmark = 1.70% Budgeted interest rate for short term borrowings

## 7. DEBT RESCHEDULING

No debt rescheduling was undertaken during the period.

## 8. COMPLIANCE WITH TREASURY LIMITS

During the financial year the Council operates within the treasury limits and Prudential Indicators set out in the Treasury Strategy Statement 2022/23, approved by Council in March 2022.



## APPENDIX 1

### TREASURY MANAGEMENT MID YEAR REVIEW REPORT 2022/23

#### Operational Boundary for external debt

The Council resolved that this limit be set at £237 million for 2022/23. The average level of borrowings to the 30<sup>th</sup> September 2022 was £220.3 million, this is well below the limit.

The operational boundary can be exceeded on an occasional basis, and this is to be expected due to cash flow fluctuations. Sustained breaches however, would indicate that either the limit has been set too low, or that the Authority is breaching its prudential boundaries and that corrective action needs to be taken.

Monitoring of the operational boundary is undertaken on a daily basis and any such continual breaches would be investigated and a recommended course of action reported to Council.

#### Authorised Limit for external Debt

The Council resolved that this limit be set at £260.7 million for 2022/23. The Authorised Limit is set having regard to the operational boundary above.

The average level of borrowings for the first half year to the 30<sup>th</sup> September 2022 was £220.3 million, so well within the limit set.

The Authorised Limit must not be breached.

#### Maturity Structure of Fixed Rate Borrowing

The Council resolved the following limits for the maturity structure of fixed rate borrowings for 2022/23;

	Upper Limit	Lower Limit	Actual as at 30/09/2022
under 12 months	20%	0%	1.72%
12 months and within 24 months	20%	0%	5.17%
24 months and within 5 years	50%	0%	25.57%
5 years and within 10 years	75%	0%	15.35%
10 years and above	95%	25%	52.18%

The actual debt maturity profile at 30<sup>th</sup> September 2022 is well within the limits set.

#### Upper Limit on Variable Interest Exposure

Council resolved the upper limit on variable rate exposures for 2022/23 should be set at 30% of outstanding long term debt. This strategy limits the proportion of interest which is subject to variable rate terms and hence protects the Council against increased costs in times of rising interest rates.

The actual level of variable borrowings is £4 million (LOBO) which equates to 2.4% of the outstanding long term debt as at 30<sup>th</sup> September 2022, so is well within the limit set.

## APPENDIX 1

### TREASURY MANAGEMENT MID YEAR REVIEW REPORT 2022/23

#### 9. MID YEAR REVIEW OF INVESTMENT STRATEGY FOR 2022/23

The Annual Investment Strategy for 2022/23 adopted by Council in March 2022 was to maintain only temporary, short term investments and to make those investments in accordance with anticipated cash flow requirements (including the investing of sums borrowed at prevailing low interest rates in anticipation of capital spending). The Council's investment priorities are:

- a. the security of capital;
- b. The liquidity of its investments.

The Council also aims to achieve the optimum return on its investments commensurate with proper levels of security and liquidity. The risk appetite of this Council is low in order to give priority to the security of its investments.

In order to ensure that the Authority's investments are secure and that risk is minimised an investment matrix is used to determine investment counterparties, which factors in Fitch and Moody's credit ratings, credit default swap (CDS) spread data, and credit rating agency comments.

Currently, the approved investment counterparties available to the Authority are Barclays (the Authority's bank), Lloyds Bank, the Debt Management Account Deposit Facility (DMADF), other Local Authorities and the Public Sector Deposit Fund. In order to diversify its investment portfolio, the Authority has undertaken fixed term deposits with other banks in line with the counterparty list. Whilst interest rates receivable on these counterparties is low the security of the capital sum is high and there is no cost associated with placing cash there.

This strategy has been adhered to in determining the investments for the first half of 2022/23 outlined in section 10 below.

#### 10. INVESTMENT OUTTURN FOR THE FIRST HALF OF 2022/23

Appendix B gives details of the investments made during the first half of the year, and the following table gives a summary, which shows the Authority's average rate of return was below the benchmark.

	Total Value of Investments during period	Average Investment	Investment Returns	Average Rate of Return	Average Investment Days during 2022/23	Benchmark Return *
<b>Internally Managed</b>	£381.3M	£4.2M	£541k	0.82%	70.3	1.39%

\* Benchmark = 1 Month SONIA

1.39%

## **APPENDIX 1**

### **TREASURY MANAGEMENT MID YEAR REVIEW REPORT 2022/23**

No institutions in which investments were made had any difficulty in repaying investments and interest in full during the year.

It has been publicly noted that some Local Authorities have entered into arrangements to restructure their debt portfolios. Where the Council has outstanding investments with those Authorities, confirmation that the amounts due will be repaid in full on the maturity date has been received by Officers.

### **11. OTHER TREASURY MANAGEMENT ISSUES**

None to report