Open Report on behalf of Andrew Crookham, Executive Director – Resources

Report to:	**Overview and Scrutiny Management Board**
Date:	**23 February 2023**
Subject:	**Treasury Management Performance 2022/23 - Quarter 3 to 31 December 2022**

Summary:

This report details the treasury management activities and performance for Quarter 3 of 2022/23 to 31 December 2022, comparing this to the Treasury Management Strategy and Annual Investment Strategy 2022/23 that was approved by the Executive Councillor for Resources, Communications and Commissioning on 14 March 2022. This report meets the reporting requirements as detailed in the CIPFA Code of Practice for Treasury Management that the Council follows.

Actions Required:

The Overview and Scrutiny Management Board is invited to review the report and seek assurance on the treasury management activities and performance.

1. Background

1.1. The Treasury Management Strategy and Annual Investment Strategy 2022/23 sets the framework for how we manage the cashflow, borrowing and treasury investments of the Council and the risks involved.

1.2. Actual activity and performance compared to this strategy is reported quarterly, this report being the third quarter report for 2022/23 covering the period up to 31st December 2022.

1.3. Activity and performance up to 31st December 2022 compared to the strategy is detailed in the Conclusion in Section 2 below. Supporting information is detailed in the attached appendices.

2. Conclusion

Comparison of Activity and Performance to Strategy for Period up to 31st December 2022

Interest Rate Forecast:

***Strategy*:**

At the time of writing the Strategy:

- *Short term rates had increased in the final quarter of 2021/22 as the MPC increased Base Rate to 0.50% from 0.10%, in a measure to tackle rising inflation. Further increases in Bank Rate were forecast for March, May, and November where it was expected to end the year at 1.25%.*
- *Long term rates were expected to remain flat over the year in all periods ranging from 2.30% to 2.60% with little difference between any period as short-term gilts increased with short term interest rates and longer dated gilts were impacted by inflation concerns.*
- *This forecast was based on the backdrop of a stronger economy after Covid, but with CPI inflation forecast to reach a peak of 7.25% in April amid concerns over supply side shortages, a tight labour market and demands for wage increases.*

Activity and Performance to 31st December 2022:

Short term Rates.	In line with countries worldwide, the MPC has increased Base Rate for the 6th time in 2022/23 to curb the increase in inflation. Base Rate at the end of December 2022 was at 3.50%. Further increases are expected to August 2023, as Base is now expected to peak at 4.50% , then start to fall back as inflation comes down from current high levels. This is in contrast to market expectations for Base in September of 5.25%, prior to the Autumn Statement on 17th November which restored fiscal credibility after the fiscal 'loosening ' polices of the previous Prime Minister.
Long Term Rates.	Gilt yields, which impact long-term borrowing rates, have been caught up in the global surge in bond yields triggered by the strong rise in inflation the US in May, and have been on a march upwards since the start of the year. The graph shows that gilts yields rose sharply at the end of September following the Governments fiscal stimulus plans with the 30-year gilt rising from 3.60% to 5.10% as an example. The Bank of England were forced to buy up long dated gilts to restore 'orderly market conditions' and postpone its reduction of its Quantitative Easing program. The reversal of the planned fiscal loosening stimulus policies have brought gilt yields back to levels seen before the September increases and QE has commenced. PWLB rates have fallen back to the 4.2% to

	4.60% range Link forecast long term yields to fall again by the end of 2023.
Economic Review.	Economies worldwide have been dominated by the emergence of rising inflation since the start of the year brought about by increasing food, energy, and commodity prices because of supply side shortages, the Russian invasion of Ukraine and a tightening labour market. CPI inflation peaked at 11.1% in October 2022 and has since fell back to 10.7% in November 2022 and is expected to fall back sharply in 2023 as energy price inflation, goods price inflation and food price inflation are all expected to fall as prices fall back in these areas and shortages fade. Although a recession is predicted and GDP in Q4 is projected to contract by around 0.1% for the quarter, amounts are marginal and recession could be avoided in 2022 if contractions are smaller than predicted in November and December. Households are losing confidence and increasing their savings as interest rates rise. Public service strikes and the continue cost of living squeeze continue to dominate at present holding back any prospects of growth in the near term.

Appendix A shows a graph of key interest rate movements in 2022/23 to date, together with the interest rate forecast and commentary from Link Asset Services Ltd (TM Advisor) dated 19th December 2022.

Investments:

***Strategy*:**

- *Investment priority – security first, liquidity second and finally yield.*
- *Aim to invest in all periods up to two years to suit direction of interest rates, at rates in excess of market levels.*
- *Low risk counterparty strategy adopted: minimum long-term rating for approved counterparties set at 'A' and Sovereign Rating of 'AA-' for any two from three credit rating agencies.*

Activity and Performance to 31st December 2022:

Investment Position and Performance.	Cash balances, in the main, have fallen to the £250m mark over the period and was £253.9m on 31st December 2022. This fall in balances is predicted as cash balances are used to finance the capital programme in 2022/23 (known as internal borrowing) and no external borrowing is undertaken in line with meeting the Liability Benchmark forecast. At the same time interest rates have risen over the period in line with the Base Rate increases and the average Investment Return for the period was 1.759%. This is still below the new SONIA

	benchmark return of 2.079%, the main reason for this being the time lag of existing investments falling out at low rates failing to keep in line with the rapid rise in interest rate benchmarks. The WAM of the portfolio remained around 114 days. The interest rate return on 31st December 2022 was 3.63% and at the time of writing was 3.76%. Link Benchmarking data however does show that LCC's return on 31st December 2022 was in excess of the benchmarking comparators in the group by some margin and above that expected for the Risk Banding chosen. **Appendix B** shows the Investment activity and performance dashboard as of 31st December 2022.
Lending List Changes.	In accordance with the Annual Investment Strategy, maximum amount limits have reduced as the average cash balance drops below £300m. On 31st December 2022 no lending to Counterparties exceeded these limits. Swiss bank, Credit Suisse, has been removed from the Counterparty list following a reduction in credit rating and the Council had no exposure to this bank. There have been no changes to the Annual Investment Strategy that sets the Council's investment risk appetite during the period, however the UK Sovereign rate of AA- has been put on negative outlook by two of the three agencies recently due to the recent economic turmoil. If downgraded, this will put the UK below the minimum Sovereign Rating limit outlined in the current Investment Strategy. For the 2023 Strategy, to overcome this issue, it is proposed to exclude the UK from this minimum limit. The Lending List on 31st December 2022 is shown in **Appendix C**.

Appendix D shows a full list of investments held on 31st December 2022, combined with the creditworthiness list provided by Link Asset Services (TM Advisor).

Borrowing:

***Strategy*:**

- *Long term external borrowing at start of year was £476.1m, costing 3.733%.*
- *New borrowing requirement for 2022/23 to finance capital programme was set at £114.437m.*
- *Regard will be made to the Debt Liability Benchmark, as it is refined during 2022/23, before any new borrowing is undertaken, taking into consideration the cash balance of the Council.*
- *Any external long-term borrowing would be taken with the aim to reduce the overall cost of debt and for periods to ensure an even debt maturity profile.*

Activity and Performance to 31st December 2022:

Revised Borrowing Requirement.	After adjusting for internal borrowing carried forward, rephasing of the capital programme, and voluntary repayment of debt, the borrowing requirement on 31st December 2022 is now £0.00m.
Borrowing Position and Performance.	No external borrowing has been undertaken in the period to date as PWLB rates have risen and the new Treasury Indicator known as the Debt Liability Benchmark, which determines the amount to borrow based on the required level of cash required for liquidity and estimated use of reserves, is showing that we are above the benchmark for 2022/23 and therefore are not required to borrow. **Appendix E** shows the Debt Liability Benchmark as of 31st December 2022. The level and cost of the Council's borrowing on 31st December 2022 has fallen to £469.8m /3.729% due to maturing debt to date and is forecast to fall to £467.8 / 3.725% at the year end.
Temporary Borrowing.	No temporary borrowing was taken in the period.
Debt Rescheduling.	No debt rescheduling was undertaken in the period.
Prudential Indicator Limits 2022/23.	All prudential limits were met with no breaches during the period.

Appendix F shows borrowing detail and latest maturity profile on 31st December 2022.

3. Consultation

a) Risks and Impact Analysis

Risk and impact analysis for treasury management forms TMP1 of the Treasury Management Practices that are required by the CIPFA Code of Practice. A treasury management risk register details the main risks for treasury management, and this is reviewed annually. Both the TMPs and the risk register are held in the Corporate Section of Financial Strategy at County Offices.

4. Appendices

These are listed below and attached at the back of the report	
Appendix A	Movement of Key Interest Rates for 2022/23 to date and Latest Interest Rate Forecast and Commentary from Link Asset Services Ltd
Appendix B	Investments: Activity and Performance on 31st December 2022
Appendix C	Authorised Lending List on 31st December 2022 and Credit Rating Key
Appendix D	Investment Analysis Review on 31st December 2022 - Link Asset Services Ltd
Appendix E	Debt Liability Benchmark on 31st December 2022
Appendix F	Borrowing: Activity and Performance and Long-Term Maturity Profile on 31st December 2022

5. Background Papers

The following background papers as defined in the Local Government Act 1972 were relied upon in the writing of this report.

Document title	Where the document can be viewed
Treasury Management Strategy Statement and Annual Investment Strategy 2022/23 - 14/3/2022	Decision - Treasury Management Strategy Statement and Annual Investment Strategy 2022/23 (moderngov.co.uk)
Council Budget 2022/23 - 18/2/2022	Agenda for Council on Friday, 18th February, 2022, 10.00 am (moderngov.co.uk)

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