

## REPORT TO EXECUTIVE



<b>DATE</b>	<b>20 September 2023</b>
<b>PORTFOLIO</b>	<b>Resources and Performance Management</b>
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## 2023/24 Treasury Management Report – Quarter 1 (April-June)

## PURPOSE

- To report treasury management activity for the first quarter of 2023/24 covering the period 1 April to 30 June 2023.

## RECOMMENDATION

- The Executive is requested to;
  - Note the treasury management activities undertaken during the period 1 April to 30 June 2023, and;

Recommend that Full Council;

- Endorse the quarterly update on the Treasury Management Strategy 2023/24 in compliance with the requirements of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management.

## REASONS FOR RECOMMENDATION

- To inform members of the treasury management activity in the first quarter of 2023/24 and to fulfil statutory and regulatory requirements.

## SUMMARY OF KEY POINTS

- Background**  
The Council operates a balanced budget, which broadly means cash raised during the year will meet its cash expenditure. The first main function of treasury management

operations is to ensure this cash flow is adequately planned, with surplus monies being invested in low risk counterparties, providing adequate liquidity initially before considering maximising investment return.

The second main function of the treasury management service is to ensure 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 commitments. This management of longer term cash may involve arranging long or short term loans, or using cash flow surpluses, and, on occasions, any current debt may be restructured to meet Council risk or cost objectives.

Treasury management is defined as:

“The management of the organisation's borrowing, investments and cash flows, including 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 monitoring requirements for treasury activity were set out in the Treasury Management Strategy Statement (TMSS) which included the Prudential and Treasury Indicators for 2023/24 – 2025/26, approved by Full Council on 22 February 2023.

## 5. **Introduction**

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 (2021).

The primary requirements of the Code are as follows:

1. Creation and maintenance of a Treasury Management Strategy 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 Full Council of an annual Treasury Management Strategy - 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.
4. **Additionally from 2023/24, quarterly reports for scrutiny to the Executive, to include updated Treasury/Prudential Indicators (this report). These are included at Appendix 1.**
5. 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.
6. 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 Scrutiny Committee.

This quarterly 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 quarter of 2023/24;
- A review of the Treasury Management Strategy 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.

## 6. **Economic Update (Provided by Link Asset Services)**

- The first quarter of 2023/24 saw:
  - A 0.2% m/m rise in real GDP in April, partly due to fewer strikes;
  - CPI inflation falling from 10.1% to 8.7% in April, before remaining at 8.7% in May. This was the highest reading in the G7;
  - Core CPI inflation rise in both April and May, reaching a new 31-year high of 7.1%;
  - A tighter labour market in April, as the 3myy growth of average earnings rose from 6.1% to 6.5%;
  - Interest rates rise by a further 75bps over the quarter, taking Bank Rate from 4.25% to 5.00%;
  - 10-year gilt yields nearing the "mini-Budget" peaks, as inflation surprised to the upside.
  - The economy has weathered the drag from higher inflation better than was widely expected. The 0.2% m/m rise in real GDP in April, following March's 0.3% m/m contraction will further raise hopes that the economy will escape a recession this year. Some of the strength in April was due to fewer strikes by train workers and teachers in that month. Moreover, some of the falls in activity in other areas in April were probably temporary too. Strikes by junior doctors and civil servants contributed to the fall in health output (0.9% m/m) and the meagre 0.1% m/m increase in public administration.
  - The 0.3% m/m rise in retail sales volumes in May was far better than the consensus forecast of a 0.2% m/m decline and followed the robust 0.5% m/m rise in April. Some of the rise was due to the warmer weather. Indeed, the largest move was a 2.7% m/m jump in non-store sales, due to people stocking up on outdoor-related goods. But department stores also managed to squeeze out a 0.6% m/m rise in sales and the household goods sub-sector enjoyed a reasonable performance too. Overall, the figures were far better than analysts had expected. In addition, the GfK measure of consumer confidence rebounded from -27 to a 17-month high of -24 in June.
  - The recent resilience of the economy has been due to a confluence of factors including the continued rebound in activity after the pandemic, households spending some of their pandemic savings, and the tight labour market and government handouts both supporting household incomes. That said, as government support fades, real household incomes are unlikely to grow rapidly. Furthermore, higher interest rates will mean GDP is likely to contract later this

year. Our central assumption is that inflation will drop to the 2.0% target only if the Bank triggers a recession by raising rates from 5.00% now to at least 5.5% and keeps rates there until at least mid-2024. Our colleagues at Capital Economics estimate that around 60% of the drag on real activity from the rise in rates has yet to bite, and the drag on the quarterly rate of real GDP growth over the next year may be about 0.2ppts bigger than over the past year.

- The labour market became tighter over the quarter and wage growth reaccelerated. Labour demand was stronger than the consensus had expected. The three-month change in employment rose from +182,000 in March to +250,000 in April. Meanwhile, labour supply continued to recover as the size of the labour force grew by 303,000 in the three months to April. That was supported by a further 140,000 decline in inactivity as people returned to work from retirement and caring responsibilities (while inactivity due to long-term sick continued to rise). But it was not enough to offset the big rise in employment, which meant the unemployment rate fell from 3.9% to 3.8%
- The tighter labour market supported wage growth in April, although the 9.7% rise in the National Living Wage on 1st April (compared to the 6.6% increase in April last year) probably had a lot to do with it too. The 3myy rate of average earnings growth reaccelerated from 6.1% to 6.5% (consensus 6.1%) and UK wage growth remains much faster than in the US and the Euro-zone. In addition, regular private sector wage growth increased from 7.1% 3myy to 7.6%, which left it well above the Bank's forecast for it to fall below 7.0%. Overall, the loosening in the labour market appears to have stalled in April and regular private sector wage growth was well above the Bank's forecast.
- CPI inflation stayed at 8.7% in May (consensus 8.4%) and, perhaps more worryingly, core CPI inflation rose again, from 6.8% to a new 31-year high of 7.1%. The rise in core inflation built on the leap from 6.2% in March to 6.8% and means it is accelerating in the UK while it is slowing in the US and the Euro-zone (both fell to 5.3%). A further decline in fuel inflation, from -8.9% to -13.1%, and the second fall in food inflation in as many months, from 19.3% to 18.7%, explained why overall CPI inflation didn't rise. And the scheduled fall in the average annual utility price from £2,500 to £2,074 on 1st July means overall CPI inflation will probably ease in the coming months. But the problem is that the recent surge in core inflation and the reacceleration in wage growth shows that domestic inflationary pressures are still strengthening.
- This suggests the Bank may have more work to do than the Fed or ECB. Indeed, the Bank of England sounded somewhat hawkish in the June meeting. This came through most in the MPC's decision to step up the pace of hiking from the 25bps at the previous two meetings. The 7-2 vote, with only two members voting to leave rates unchanged at 4.50%, revealed support for stepping up the fight against high inflation.
- That said, the Bank has not committed to raising rates again or suggested that 50bps rises are now the norm. What it did say was that "the scale of the recent upside surprises in official estimates of wage growth and services CPI inflation suggested a 0.5 percentage point increase in interest rates was required at this particular meeting". Moreover, the Committee did not strengthen its forward guidance that any further rate hikes would be conditional on the data. However, it looks highly probable, given the on-going strength of inflation and employment data, that the Bank will need to raise rates to at least 5.5% and to keep rates at their peak until the mid-point of 2024. We still think it is only a matter of time

before the rise in rates weakens the economy sufficiently to push it into recession. That is why instead of rising to between 6.00%-6.25%, as is currently priced in by markets, we think rates are more likely to peak between 5.50-6.00%. Our forecast is also for rates to be cut in the second half of 2024, and we expect rates to then fall further than markets are pricing in.

- Growing evidence that UK price pressures are becoming increasingly domestically generated has driven up market interest rate expectations and at one point pushed the 10-year gilt yield up to 4.49% in late June, very close to its peak seen after the “mini-budget”. Yields have since fallen slightly back to 4.38%. But growing expectations that rates in the UK will remain higher for longer than in the US mean they are still more than 70 bps above US yields. While higher interest rates are priced into the markets, the likely dent to the real economy from the high level of interest rates is not. That’s why we think there is scope for market rate expectations to fall back in 2024 and why we expect the 10-year PWLB Certainty Rate to drop back from c5.20% to 5.00% by the end of this year and to 4.20% by the end of 2024.

## 7. Interest Rate Forecast (Provided by Link Asset Services)

The Council has appointed Link Group as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates.

The latest forecast on 26<sup>th</sup> June 2023 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, against a backdrop of a stubbornly robust economy and a tight labour market.

You will note that our forecasts have steadily increased during the quarter (when compared to previous rate forecasts) as the data continued to spring upside surprises, and the Bank of England continued to under-estimate how prevalent inflation is, and how tight the labour market is. The Government has also noted that despite immigration increasing markedly, high levels of ill-health amongst the workforce has led to wage demands remaining strong until such time as there is a loosening in demand for business services.

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.

Link Group Interest Rate View	26.06.23											
	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26
BANK RATE	5.00	5.50	5.50	5.50	5.25	4.75	4.25	3.75	3.25	2.75	2.75	2.50
3 month ave earnings	5.30	5.60	5.50	5.30	5.00	4.50	4.00	3.50	3.00	2.70	2.60	2.50
6 month ave earnings	5.80	5.90	5.70	5.50	5.10	4.60	4.00	3.50	3.00	2.70	2.60	2.60
12 month ave earnings	6.30	6.20	6.00	5.70	5.30	4.80	4.10	3.60	3.10	2.80	2.70	2.70
5 yr PWLB	5.50	5.60	5.30	5.10	4.80	4.50	4.20	3.90	3.60	3.40	3.30	3.30
10 yr PWLB	5.10	5.20	5.00	4.90	4.70	4.40	4.20	3.90	3.70	3.50	3.50	3.50
25 yr PWLB	5.30	5.40	5.20	5.10	4.90	4.70	4.50	4.20	4.00	3.90	3.80	3.80
50 yr PWLB	5.00	5.10	5.00	4.90	4.70	4.50	4.30	4.00	3.80	3.60	3.60	3.50

## 8. Treasury Management Strategy update

The Treasury Management Strategy (TMS) for 2023/24, which includes the Annual Investment Strategy, was approved by this Council on 22 February 2023. There are no policy changes to the TMS included in this report.

## 9. **The Council's Capital Position**

The table below shows the financing of the Original Capital Budget approved by Full Council on the 22 February 2023 and the latest Revised Capital Budget as per the established Budget Monitoring Cycle and included elsewhere on the agenda. The net reduction is due to a combination of in year budget monitoring adjustments and reprofiling of capital expenditure into future years.

<b>Capital</b>	<b>2023/24 Original Estimate £'000</b>	<b>2023/24 Revised Estimate £'000</b>
<b>Total Budget</b>	<b>41,357</b>	<b>39,190</b>
Financed by:		
Capital receipts	2,547	2,908
Capital grants	22,525	20,270
Revenue	1,062	2,350
<b>Total financing</b>	<b>26,134</b>	<b>25,528</b>
<b>Borrowing need</b>	<b>15,223</b>	<b>13,662</b>

## 10. **Investment Portfolio 2023/24**

The Treasury Management Strategy Statement (TMSS) for 2023/24, which includes the Annual Investment Strategy, was approved by the Council on 22 February 2023. In accordance with the CIPFA Treasury Management Code of Practice, it sets out the Council's investment priorities as being:

- Security of capital
- Liquidity
- Yield

The Council will aim to achieve the optimum return on its investments commensurate with proper levels of security and liquidity and with the Council's risk appetite. In the current economic climate it is considered appropriate to keep investments short term to cover cash flow needs and avoid high borrowing costs where possible (internal borrowing), but also to seek out value available in periods up to 12 months with high credit rated financial institutions where cashflow projections are considered robust, using the Link suggested creditworthiness approach, including a minimum sovereign credit rating and Credit Default Swap (CDS) overlay information. As per the approved Investment Strategy, longer-term investments will be carefully assessed.

### **Investment Counterparty criteria**

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

### **CDS prices**

It is noted that sentiment in the current economic climate can easily shift, so it remains important to undertake continual monitoring of all aspects of risk and return in the current circumstances

The average daily level of funds deposited during the financial year to date is £2.6m with an average rate of return of 4.46%. Excluding longer-term property funds, the long-term loan to Burnley College and the Council's 'Sweep' account, the actual value of surplus funds under investment as at 30 June was £13m. These funds have been

available on a temporary basis, and the level of funds available was mainly dependent on the timing of precept payments, receipt of grants and progress on the Capital Programme.

There were 7 investments carried forward from 2022/23 totalling £17.8m, of which £3.8m was in a mixture of notice and call accounts with our bank HSBC, £4m was in a notice account with Santander, £8m was in fixed term deposits, and £2m was the loan made to Burnley College.

There have been two new fixed investments made during the period 1 April to 30 June 2023 totalling £6m. The table below shows the amount invested as at 30 June 2023, and the rate of return against the market benchmark.

Counterparties	Date of Investment	Investment As at 30 June 2023 £m	Current Return	Benchmark (average return)*
HSBC (31 Day Notice)**	12/08/2020	2.0	5.00%	4.614%
Santander (31 Day Notice)**	04/05/2023	1.0	4.03%	4.407%
LCC SIS Instant Access**	08/06/2023	4.0	4.75%	4.614%
Lloyds Bank Corporate Markets – 3 mth fixed	17/05/2023	4.0	4.67%	4.407%
Goldman Sachs – 3 mth fixed	08/06/2023	2.0	4.93%	4.614%
Burnley College Loan – 15 years fixed	28/03/2022	2.0	4.45%	NA

\* Benchmark: SONIA Compounded Backward Looking rate for date of investment

\*\* Rate is linked to movement in Bank Rate

The Council has an approved list of counterparties which governs treasury management investment activity. This list is a restricted list taking into consideration the credit rating of the institution concerned and there are also limits on the amount which can be invested with any particular institution from a particular sector e.g. building society, bank etc. and also any group of institutions within an overall banking group. As part of the daily operations of the treasury management dealings, in consultation with guidance from Link Asset Services and the money market brokers, decisions are taken by the Head of Finance & Property Services, temporarily suspending/revising operations with individual counterparties. The latest deposit counterparties list was approved by the Full Council on 22 February 2023.

Within the approved list of counterparties is scope to invest sums with other Local Authorities, up to a maximum of £8m, and not to exceed £6m per Local Authority. The Council has reinstated the Shared Investment Scheme (SIS) facility with Lancashire County Council to provide instant access to sums on deposit as an alternative to the 'Sweep' account. The SIS rate is linked to movement in the Bank Rate (unlike the Sweep account), and thus provides an improved return on sums deposited plus is instantly accessible to provide improved liquidity should this be necessary when compared to current notice account arrangements (31 day notice required).

The table below shows the maximum amount invested with any of the counterparties at any one time during the period April 2023 to 30 June 2023 against the maximum limits approved in the 2023/24 Treasury Management Strategy.

Counterparties	Maximum Limits £m	Highest level of Investment 2023/24 (£m)
HSBC*	50.0	12.0
Santander	4.0	4.0
Lloyds Bank Corporate Markets	4.0	4.0
Goldman Sachs	4.0	4.0
Lancashire CC SIS	6.0	4.0

\*Includes Sweep Account balance

#### 11. **Property Funds**

The council made two investments totalling £2m in property funds in 2018/19 for the purpose of increasing and diversifying our risk in investment income receivable and to help alleviate future revenue budget pressures. At the time of this report no dividends had been received as these tend to be receivable in the month following quarter end. An update will be provided as part of the Q2 monitoring cycle (Mid-Year Review).

#### 12. **Borrowing**

The Council's capital financing requirement (CFR) for 2023/24 is £80,097m. The CFR denotes the Council's underlying need to borrow for capital purposes. Below is a summary of the Councils' external indebtedness, as at 1 April 2023, and as at 30 June 2023.

Borrowing	1 Apr 23 £'000	30 June 23 £'000	Change Apr – June £'000
Public Works Loan Board	59,510	59,290	(220)
Temporary Market Loans	13	13	-
<b>Total</b>	<b>59,523</b>	<b>59,303</b>	<b>(220)</b>

**PWLB Loans** – No maturity loan repayments made during the period 1 April to 30 June 2023. One scheduled annuity repayment was made during the period totalling £220k.

**Temporary Market Loans** – The Council entered into a temporary loan for cashflow purposes during the period as below:

Loan	Loan Advanced £'000	Date From	Date To	Interest Rate	Total Interest Payable £'000
London Borough of Havering	3,000	21/04/2023	05/05/2023	4.15%	4.78
<b>Total</b>	<b>3,000</b>				<b>4.78</b>

#### 13. **Debt Rescheduling**

Debt rescheduling opportunities have been very limited in the current economic climate and following the various increases in the margins added to gilt yields recently linked to increases in the Bank Rate. No debt rescheduling has been undertaken to date in the current financial year. Only prudent and affordable debt rescheduling will be considered.



14. **Compliance with Treasury & Prudential Limits**

It is a statutory duty for the Council to determine and keep under review its affordable borrowing limits. The Council's approved Treasury and Prudential Indicators (affordability limits) are included in the approved Treasury Management Strategy.

During the financial year to date the Council's treasury management activities operated within the treasury limits and Prudential Indicators set out in the Council's Treasury Management Strategy in compliance with the Council's Treasury Management Practices.

An extract of the Prudential and Treasury Indicators are shown in Appendix 1.

15. **Interest Payable on External Borrowing / Interest Receivable**

Provision is made in the revenue budget to meet the net interest payable on external borrowing. The figure in the original budget for 2023/24 was set at £2,068,168 and remains unchanged.

The total interest receivable for temporary deposits placed in the first quarter is £189k, excluding dividends due for the period. The budget for the year for interest and dividend receipts was approved at £575k. On current projections, owing to a rising bank rate environment, additional interest from temporary surplus monies on deposit, is forecast to exceed the budget by £100k,. This will support the Council's Revenue Account and ensure a balanced financial position.

**FINANCIAL IMPLICATIONS AND BUDGET PROVISION**

16. None arising as a direct result of this report.

**POLICY IMPLICATIONS**

17. Compliance with the revised CIPFA Code of Practice on Treasury Management and the Council's approved Treasury Management Strategy Statement (TMSS).

**DETAILS OF CONSULTATION**

18. None.

**BACKGROUND PAPERS**

19. None.

**FURTHER INFORMATION**

**PLEASE CONTACT:**

**Craig Finn – Principal Accountant**

