CORPORATE GOVERNANCE COMMITTEE – 17th NOVEMBER 2023

QUARTERLY TREASURY MANAGEMENT REPORT

REPORT OF THE DIRECTOR OF CORPORATE RESOURCES

Purpose of report

1. The purpose of this report is to update the Committee on the actions taken in respect of treasury management for the quarter ending 30th September 2023 (Quarter 2).

Policy Framework and Previous Decisions

2. Within the County Council's Constitution, Part 3 – responsibility for functions, the functions delegated to the Corporate Governance Committee include 'that the Council's Treasury Management arrangements are appropriate and regularly monitored'.

3. The Annual Treasury Management Strategy and Annual Investment Strategy (AIS) for 2023-27 form part of the Council's Medium Term Financial Strategy (MTFS). These were considered and supported by the Corporate Governance Committee in January 2023 and approved by full Council in February 2023.

4. The Treasury Management Strategy requires quarterly reports to be presented to the Corporate Governance Committee, to provide an update on any significant events in treasury management. The aim of these reporting arrangements is to ensure that those with responsibility for the treasury management function appreciate the implications of treasury management policies and activities, and that those implementing policies and executing transactions have properly fulfilled their responsibilities with regard to delegation and reporting. This is in line with the CIPFA Treasury Management Code.

5. An update in respect of Quarter 1 2023/2024 was provided to the Committee on 22nd September

Background

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

7. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's low risk appetite, providing adequate liquidity initially before considering investment return. The second main function of the Treasury Management service is the funding of the Council's capital plans. These capital plans

provide a guide to the borrowing need of the Council, essentially the longer-term cash flow planning, to ensure that the Council can meet its capital spending obligations. This management of longer-term cash may involve arranging long or short-term loans or using longer-term cash flow surpluses. Treasury risk management at the Council is conducted within the framework of CIPFA's Treasury Management Code of Practice.

8. Capital investments in services, including those within the Corporate Asset Investment Fund, are part of the Capital Strategy (and are part of the capital programme), rather than the Treasury Management Strategy. The capital programme is monitored and reported regularly to the Scrutiny Commission and the Cabinet.

Economic Background

9. The Council's treasury management adviser, Link Asset Management (Link), provides a periodic update outlining the global economic outlook and monetary policy positions. An extract from that report is attached as Appendix A to this report. The key points are summarised in the following paragraphs.

10. Inflation as measured by the consumer price index (CPI) fell from 8.7% in April to 6.7% in August. This is the lowest rate seen in the UK since February 2022, but still remains the highest in the G7. Core CPI (CPI excluding energy and food prices) declined to 6.2% in August, down from 7.1% in April and May, which was at that point a 31 year high.

11. July saw a 0.5% month on month fall in GDP, suggesting that underlying growth has lost momentum since earlier in the year. The decline in July is believed to have been driven by an increase in strike action, with almost twice as many working days lost to strikes in July (281,000) than in June (160,000). Output also fell in 10 out of the 17 sectors, indicating that there is also an air of underlying weakness

12. Commentators feel that as the growing drag from higher interest rates intensifies over the next six months, the economy will continue to lose momentum and soon fall into a mild recession.

Action Taken During Quarter 2 to September 2023

Private Debt and Bank Risk Sharing Funds

13. The table overleaf provides an overview of the Council's investments in private debt and bank risk sharing funds. As well as showing the current capital levels within each fund the table also shows the Net Asset Value (NAV), and Internal Rate of Return (IRR) for each fund.

Summary Private Debt and CRC:

	Total Commitment (£m)	Capital remaining (£m)	NAV (£m)	IRR (Since Incep'n)	Total Income Rec'd	During Qtr Capital Movement (£m)	Income (£m)
2017 Mac IV	20.0	6.1	6.3	4.68%	3.8	- 0.8	-
MAC VI	20.0	18.5	20.3	7.10%	0.5	-	-
CRC CFR 5	15.0	15.0	16.4	-	-	-	-

14. The Council received its 27th distribution from the Partners Mac IV (2017) fund during the quarter in the form of invested capital (shown as a negative figure in the table above).

15. The Council received no further distributions from the MAC VI fund during the quarter.

16. There were no further commitments to or distributions from Christofferson Robb and Company's (CRC) Capital Relief Fund 5 (CRF 5). As this investment is still in the investment period the IRR cannot yet be calculated reliably. The NAV for this fund is also as at 31st August – the last reported position prior to this committee meeting.

<u>Short Term Investments</u>

17. A summary of movements and key performance indicators (KPIs) in the Council's investment loan portfolio can be viewed in the table below. The table details the portfolio Annual Percentage Rate (APR) of the portfolio, the average APR of loans matured, and new loans placed. The table also shows the weighted average maturity (WAM) of the portfolio.

KPIs Loans only:

	Total Loans	APR (Loans Only)	WAM (Days)	Maturities (£m)	APR Maturities	New Loans (£m)	APR New Loans
Current Qtr	383.0	5.29%	168	141.9	5.01%	133.0	5.76%
Prior Qtr	391.9	4.70%	179	185.5	3.61%	151.9	5.58%
Change	↓ 8.9	↑ 0.59%	↓ 11.0	↓ 43.6	↑ 1.40%	↓ 18.9	↑ 0.18%

*WAM excludes MMFs as these are O/N maturity

18. The total balance available for short term investment decreased by £8.9m during the quarter. This was anticipated due to early PWLB debt repayments totalling £29.8m.

19. Official figures show a better-than-expected decrease in CPI from June to August, with the MPC voting against increasing the base rate beyond 5.25% in September. With market sentiment thus shifting towards the base rate having peaked, the

replacement margin on new loans (vs maturities) decreased to 0.75% from 1.97% in the last quarter.

20. Nonetheless, the average rate on the loans portfolio rose 0.59% in the quarter.

21. The Loans weighted average maturity (WAM) decreased by 11 days and indicates that the portfolio will be slightly more sensitive to movements in interest rates (whether these are up or down). This was primarily driven by less cash being available to lend longer due to the early repayment of elements of the Council's debt portfolio.

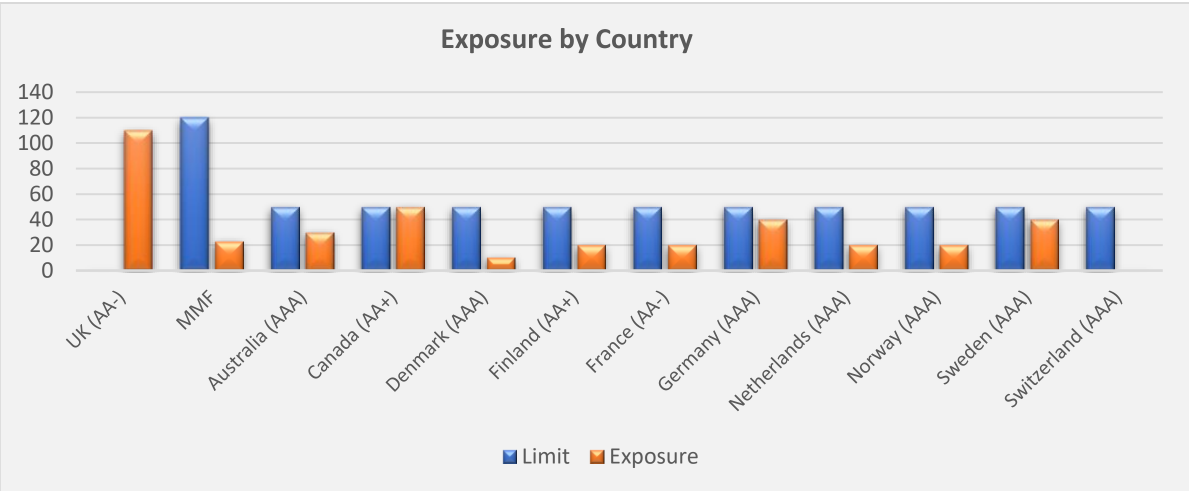
22. The loan portfolio at the end of September was invested with the counterparties shown in the table below, listed by original investment date:

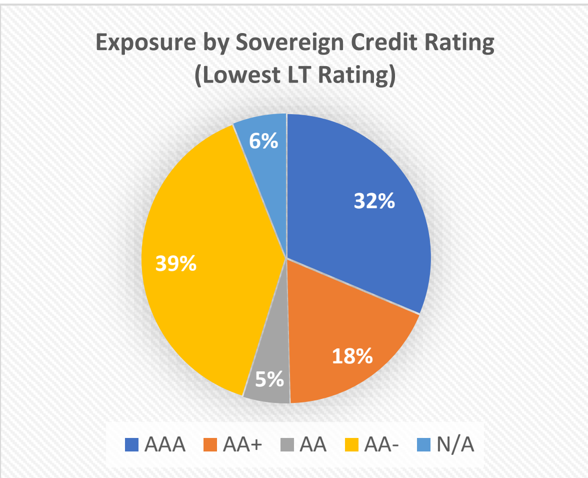
	£m	Maturity Date
Instant Access		
Money Market Funds	23.0	October 2023
6 Months		
National Bank of Canada	10.0	October 2023
Lloyds (CD)	15.0	October 2023
Close Brothers	5.0	November 2023
Lloyds (CD)	20.0	December 2023
Close Brothers	10.0	March 2023
Close Brothers	20.0	March 2024
12 Months		
Landesbank Hessen Thuringen	10.0	October 2023
DNB Bank (CD)	10.0	November 2023
DNB Bank (CD)	10.0	January 2024
National Westminster Bank Plc	10.0	January 2024
DZ Bank (CD)	10.0	February 2024
DZ Bank (CD)	10.0	February 2024
National Westminster Bank Plc	20.0	March 2024
Seb (CD)	20.0	March 2024
Rabobank (CD)	10.0	March 2024
Commonwealth Bank of Australia (CD)	10.0	April 2024
Toronto Dominion Bank	20.0	May 2024
Credit Industrial Et Commercial (CD)	10.0	May 2024
Swed Bank (CD)	20.0	May 2024
Bank of Montreal	20.0	May 2024
Australia & New Zealand Bank	20.0	May 2024
Rabobank (CD)	10.0	June 2024
National Westminster Bank Plc	10.0	July 2024
Nordea Bank (CD)	20.0	August 2024
Credit Industrial Et Commercial	10.0	September 2024
Landesbank Hessen Thuringen	10.0	September 2024

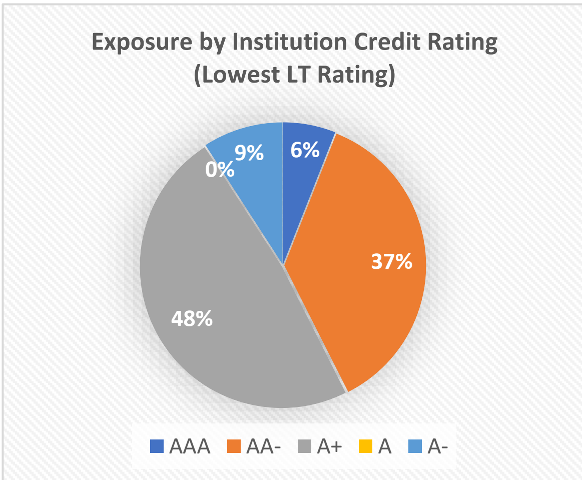
Beyond 12 Months but included in short term investments		
Danske Bank#	10.0	September 2027
Short term investments total	**383.0**	
Beyond 12 Months		
Partners Group (Private Debt) 2017	6.1	Estimated 2024
Partners Group (Private Debt) 2021	18.5	Estimated 2026
CRC CRF 5 (Bank Risk Sharing)	15.0	Estimated 2026
TOTAL PORTFOLIO BALACE: 30 September 2023	**422.6**	

#Danske Bank loan is included in short term investments for reporting in the tables above as the interest fixing is every six months.

23. The graphs below show the exposure of the short-term investments by country, sovereign rating and institution rating:



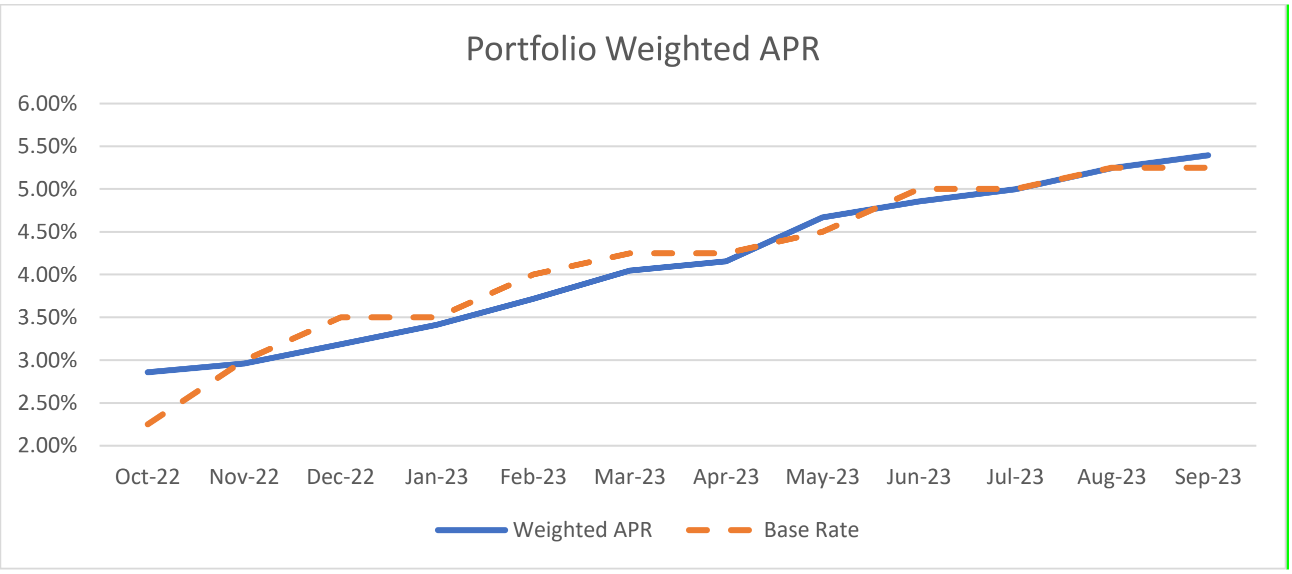




24. These graphs provide an indication of the Council's exposure to credit risk but it should be noted long term credit rating is just one of the components used to determine the list of acceptable counterparties; short-term ratings, ratings outlook, rating watches, credit default swap movements (the cost of insuring against a default) and general economic conditions are also factored in before the counterparty list is drawn up.

Total Portfolio

25. The total portfolio weighted APR increased from 4.86% in Q1 23-24 to 5.39% in Q2 23-24. The chart below shows the weighted APR achieved by the treasury portfolio compared to the BoE base rate. The graph shows that the portfolio APR dropped below base rate during December 2022 and, with the exception of May and September 2023, has stayed slightly below since. Most investments within the portfolio are on a fixed interest basis so changes in base rate do not immediately have a material impact on the APR achieved. One indicator for how big this lag is the WAM. This shows the average length of time remaining until the Council's short-term investments mature and can be viewed in the table below paragraph 16. As investments mature and are reinvested the current expectation is that these will be at a higher rate, and as base rate peaks the APR is likely to move up in line or above base rate. Members should note that it is the future expectation for base rate that drives the price achieved.



Loans to Counterparties that breached authorised lending list

26. There were no loans active during the period that breached the authorised counterparty list at the time that the loan was made.

Debt Rescheduling

27. During Q2 2023/2024, gilt yields, which underpin PWLB rates, remained at levels sufficient to consider further longer-term debt rescheduling opportunities.

28. After consultation with Link, our treasury management advisors, a decision was taken to reschedule the following loans:

		Start Date	Maturity	Principle	Interest Rate	Interest PA	Premium/ (discount)	Premature repayment rate	Remaining Principal
492248	PWLB	28/09/2006	25/09/2052	12,035,000	4.05%	487,418	-966,918	4.54%	0
492424	PWLB	06/11/2006	25/09/2052	13,500,000	4.05%	546,750	-1,284,786	4.65%	0
461697	PWLB	27/03/1987	31/12/2043	1,945,275	9.00%	189,000	1,105,802	4.65%	865,434
				2,345,000	9.00%	211,050	1,304,173	4.72%	
				29,825,275	**4.76%**	**1,434,218**	**158,271**		

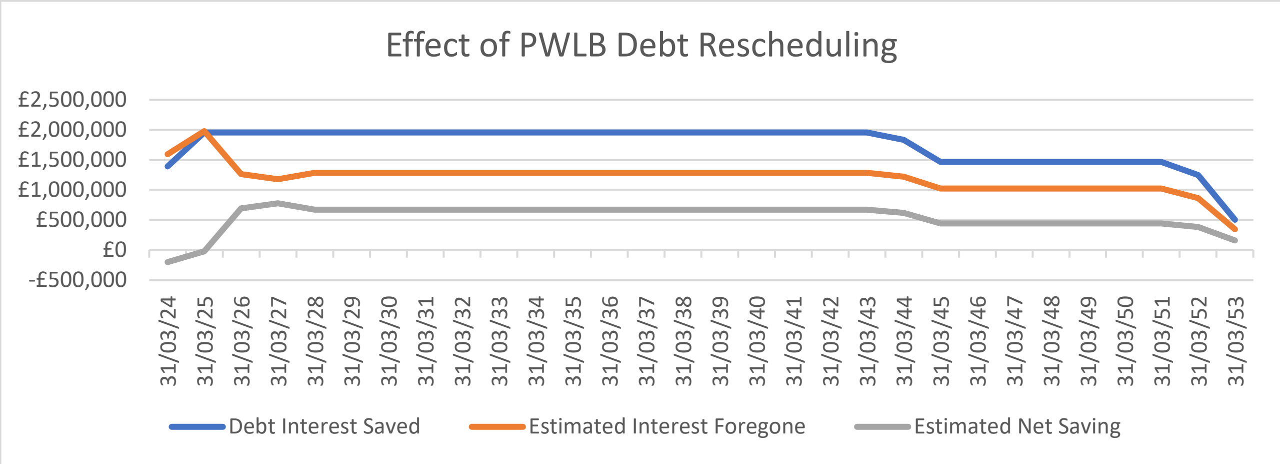
29. Rescheduling the above loans resulted in a net premium of £158,271 for the Council. Note that the above premium is offset by the discount (-£160,782) on the repayment undertaken in the previous quarter as reported in the Q1 Treasury Management report.

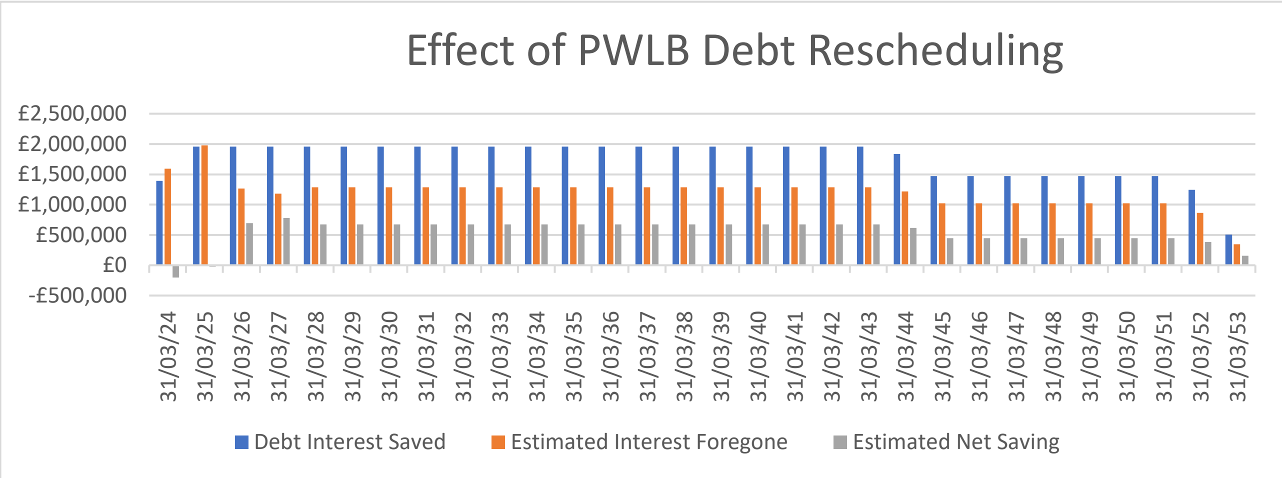
30. The overall impact of the debt rescheduling undertaken across Q1 and Q2 is shown in the table below.

		Start Date	Maturity	Principle	Interest Rate	Interest PA	Premium/ (discount)	Premature repayment rate	Remaining Principal
490987	PWLB	11/01/2006	25/09/2051	11,142,000	3.90%	434,538	-862,705	4.38%	0
492248	PWLB	28/09/2006	25/09/2052	12,035,000	4.05%	487,418	-966,918	4.54%	0
492424	PWLB	06/11/2006	25/09/2052	13,500,000	4.05%	546,750	-1,284,786	4.65%	0
461697	PWLB	27/03/1987	31/12/2043	1,131,741	9.00%	101,857	701,922	4.39%	865,434
				1,945,275	9.00%	175,075	1,105,802	4.65%	
				2,345,000	9.00%	211,050	1,304,173	4.72%	
				42,099,016	**4.65%**	**1,956,688**	**-2,512**		

31. By rescheduling debts across Q1 and Q2, the Council will save nearly £2.0m pa in fixed interest payments. However, with lower cash balances there will be a reduction on the interest that can be earnt. The graphs show the estimated net benefit, based on Link's assessment of what will happen to average investment earnings over the period as shown in the table below.

Average earnings in each year	Now
2023/24	5.30%
2024/25	4.70%
2025/26	3.00%
2026/27	2.80%
2027/28	3.05%
Years 6 to 10	3.05%
Years 10+	3.05%





Compliance with Prudential and Treasury Indicators

32. The prudential and treasury indicators are shown in Appendix B. It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. During the quarter ending 30th September 2023, the Council has operated within the treasury and prudential indicators set out in the Council's Treasury Management Strategy Statement for 2023/24. The Director of Corporate Resources reports that no difficulties are envisaged in complying with these indicators.

Resource Implications

33. The interest earned on revenue balances and the interest paid on external debt will impact directly onto the resources available to the Council. The budgeted income for interest generated by treasury management activities (excluding private debt and pooled property investments) for 2023/2024 was £13.6m. Current forecasts indicate that actual interest earned in 2023/2024 may reach as high as £20.0m. This forecasted overperformance is being driven by ongoing high levels of interest rates.

Recommendations

34. The Committee is asked to note this report.

Background papers

35. None.

Circulation under the Local Issues Alert Procedure

36. None.

Equality Implications

37. There are no discernible equality implications arising from this report.

Human Rights Implications

38. There are no human rights implications arising from this report.

Officers to Contact

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Appendices

Appendix A - Economic Overview (For the current financial year to September 2023)
Appendix B – Prudential and Treasury Indicators for 2023/24 as at 30 September 2023

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