



CORPORATE GOVERNANCE COMMITTEE – 16th SEPTEMBER 2024

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 June 2024 (Quarter 1).

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 2024-28 form part of the Council's Medium Term Financial Strategy (MTFS). These were considered and supported by the Corporate Governance Committee in January 2024 and approved by full Council in February 2024.
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 4 2023/2024 was provided to the Committee on 20th May 2024 as part of the Annual Treasury Management Report 2023/24.

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 Investing in Leicestershire Programme, 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) decreased in the quarter, from 2.3% in April to 2.0% in May. This represents the first time CPI has reached the Bank of England target since July 2021. Core CPI (CPI excluding energy and food prices) has also continued to decline, reaching 3.5% in May. However, the persistence in domestic inflationary pressures is fading more slowly than the Bank of England expected. Even so, it is felt that there is scope for inflation to fall further.
11. GDP growth has stagnated with 0% month-on-month growth in April This follows a 0.7% quarter-on-quarter growth in Q4 2023/24, which moved the economy out of a technical recession. This slight stagnation is believed to be driven by inclement weather.

Notable events subsequent to Link's Quarter 1 Update

12. CPI remained stable at 2.0% in June, before increasing slightly to 2.2% in July. Whilst a rise was predicted, this was less than forecast. The uptick is believed to have been caused by the prices of gas and electricity falling at a slower rate year-on-year. Core CPI also remained stable at 3.5% in June, before decreasing to 3.3% in July.
13. GDP growth in May was 0.4% month-on-month, suggesting the impact of higher interest rates and higher inflation are starting to fade, followed by 0.0% month-on-month growth in June.
14. Following the 1st August Monetary Policy Committee meeting, the Bank of England reduced the bank rate by 0.25% to 5.00%, the first cut since the bank started raising rates in December 2021. Link forecast the next decrease is likely to be made in Quarter 3 2024

Action Taken During Quarter 1 to June 2024

Private Debt and Bank Risk Sharing Funds

15. The table below 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:						During Qtr	
	Total Commitment (£m)	Capital invested (£m)	NAV (£m)	IRR (Since Incep'n)	Total Income Rec'd	Capital Repaid (£m)	Income (£m)
2017 Mac IV	20.0	3.5	3.9	4.80%	3.8	- 0.9	-
MAC VI	20.0	14.8	16.6	7.59%	1.6	- 2.9	0.7
CRC CFR 5	15.0	15.0	16.0	11.60%	2.5	-	1.3
MAC VII	10.0	5.6	5.9	-	-	-	-

16. The Council received its 32nd, 33rd and 34th distributions 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).
17. The Council received its 8th, 9th, 10th and 11th distributions from the MAC VI fund during the quarter totalling £3.6m. Of the £3.6m received, £2.9m represented a return of invested capital (shown as a negative figure in the table above), with the remaining £0.7m being income.
18. The Council received its 4th and 5th distributions from the Christofferson Robb and Company's (CRC) Capital Relief Fund 5 (CRF 5). The total receipt of £1.3m is represented wholly by income.
19. The Council received no further capital calls to the Partners MAC VII fund in quarter 1. As this investment is still in the investment period the IRR cannot yet be calculated reliably.
20. It is worth noting that the NAV on all four funds is in excess of the remaining capital invested.

Short Term Investments

21. 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) ¹	Maturities (£m)	APR Maturities	New Loans (£m)	APR New Loans
Current Qtr	409.4	5.38%	185	208.2	5.42%	214.4	5.20%
Prior Qtr	403.2	5.47%	113	130.1	5.01%	95.0	5.32%
Change	↑ 6.2	↓ 0.09%	↑ 72.0	↑ 78.1	↑ 0.41%	↑ 119.4	↓ 0.12%

¹WAM excludes MMFs as these are overnight maturity

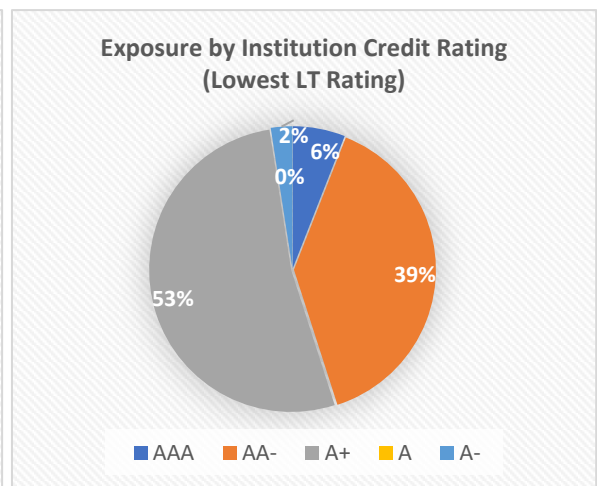
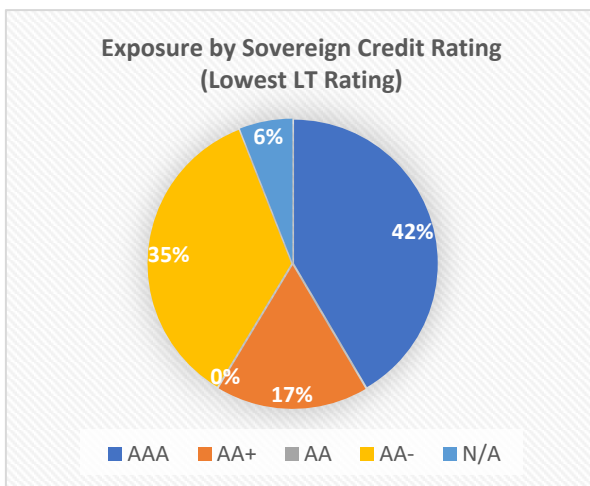
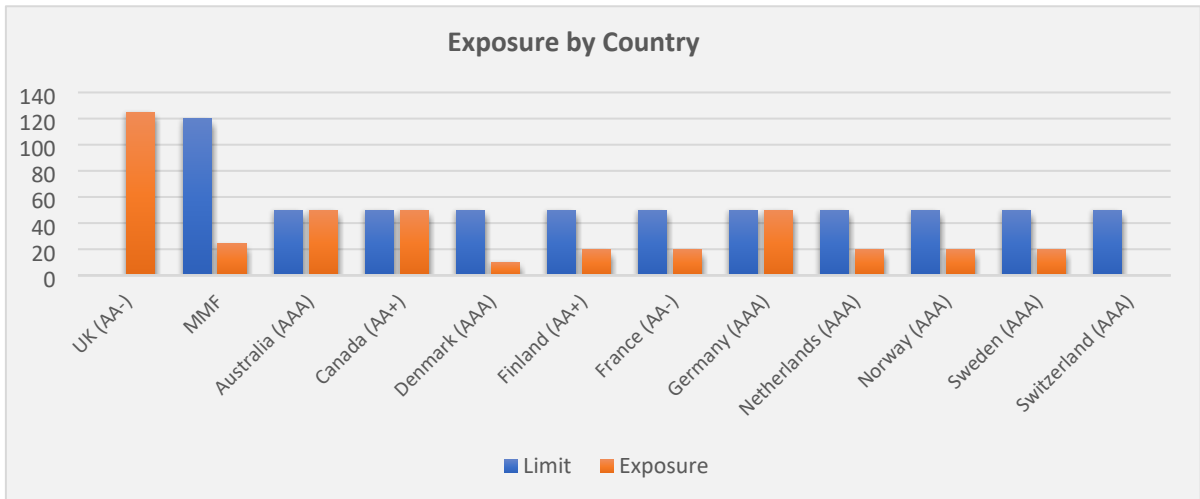
22. The total balance available for short term investment increased by £6.2m during the quarter.
23. Official figures show that CPI is now decreasing and generally stabilising at the Bank of England target of 2.0%. Market sentiment indicates that the base rate has peaked, with expectations of a decrease in quarter 3 2024 being priced into market rate offerings. As a result, replacement margin on new loans (vs maturities) has inverted to -0.22% from 0.31% in the last quarter.
24. As a result, the average rate on the loans portfolio fell by 0.09% in the quarter.
25. The Loans weighted average maturity (WAM) increased by 72 days and indicates that the portfolio will be more insulated against movements in interest rates (whether these are up or down). This was primarily driven by more cash being available to lend longer due to the high value of maturities in the quarter.
26. The loan portfolio at the end of June was invested with the counterparties shown in the table below, listed by original investment date:

	<u>£m</u>	<u>Maturity Date</u>
Instant Access		
Money Market Funds	24.4	July 2024
6 Months		
Goldman Sachs	10.0	July 2024
Goldman Sachs	10.0	September 2024
Goldman Sachs	15.0	September 2024
Landesbank Baden Wurtemberg	10.0	October 2024
Lloyds	15.0	October 2024
9 Months		
Den Norske Bank (DNB)	10.0	October 2024
12 Months		
National Westminster Bank Plc	10.0	July 2024
Nordea Bank	20.0	August 2024
Credit Industrial Et Commercial	10.0	September 2024
Landesbank Hessen Thuringen	10.0	September 2024
Landesbank Hessen Thuringen	10.0	October 2024
Commonwealth Bank of Australia	10.0	October 2024
DNB Bank	10.0	October 2024

National Bank of Canada	10.0	November 2024
National Westminster Bank PLC	10.0	November 2024
National Westminster Bank PLC	10.0	February 2025
National Westminster Bank PLC	20.0	February 2025
Rabo Bank	10.0	March 2025
National Westminster Bank PLC	25.0	April 2025
Skandinaviska Enskilda Banken AB (SEB)	20.0	April 2025
Commonwealth Bank of Australia (CBA)	10.0	April 2025
Macquarie Bank	10.0	April 2025
Toronto Dominion Bank	20.0	May 2025
Credit Industriel et Commercial (CIC)	10.0	May 2025
Bank of Montreal	20.0	May 2025
Deutsche Zentral (DZ)	20.0	May 2025
Australia & New Zealand Bank	20.0	May 2025
Rabo Bank	10.0	June 2025
Beyond 12 Months but included in short term investments		
Danske Bank [#]	10.0	September 2027
<u>Short term investments total</u>	409.4	
Beyond 12 Months		
Partners Group (Private Debt) 2017	3.5	Estimated 2024
Partners Group (Private Debt) 2021	14.8	Estimated 2026
CRC CRF 5 (Bank Risk Sharing)	15.0	Estimated 2026
Partners Group (Private Debt) 2023	5.6	Estimated 2028
<u>TOTAL PORTFOLIO BALANCE: 30 June 2024</u>	448.3	

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

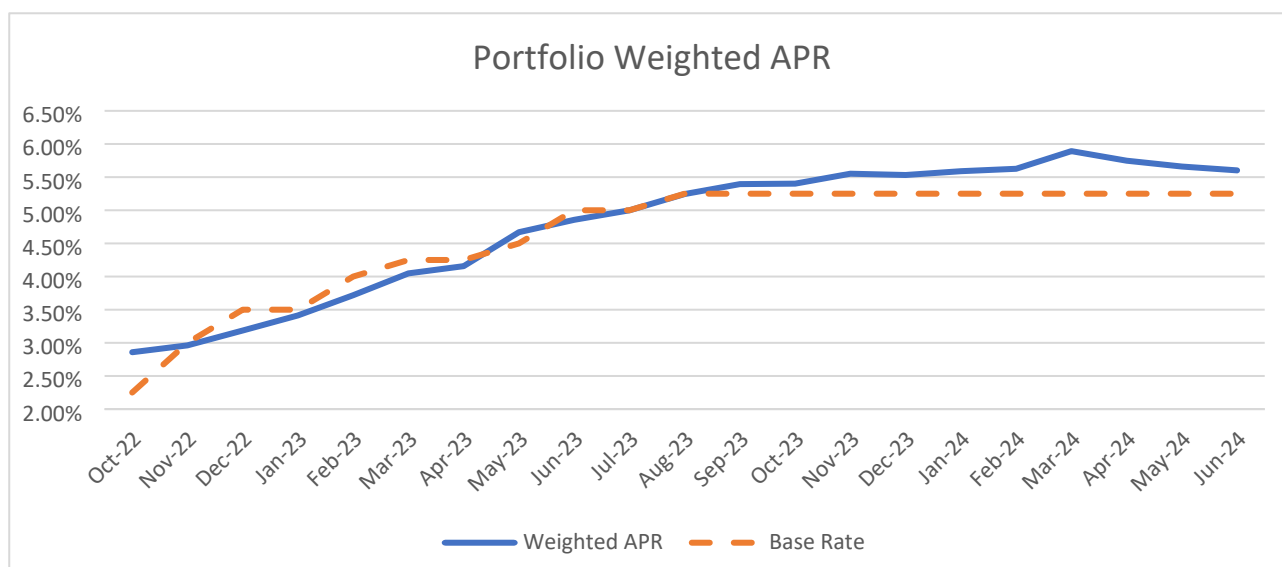
27. The graphs below show the exposure of the short-term investments by country, sovereign rating and institution rating:



28. 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

29. The total portfolio weighted APR decreased from 5.89% in Quarter 4 2023-2024 to 5.60% in Quarter 1 2024-2025. This is due to reductions in the rates available in the market, in anticipation of an upcoming reduction to the Bank of England base rate. The chart below shows the weighted APR achieved by the treasury portfolio compared to the BoE base rate. The graph shows that whilst base rates have stabilised since August 2023, the weighted APR of the portfolio has achieved a higher return in the months that followed. 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. It can be seen from the table in paragraph 21 that the average days to maturity of loans is 183 days – an increase of 72 from the last quarter.



Loans to Counterparties that breached authorised lending list

30. On 12th February 2024 Link downgraded the suggested lending duration for Close Brothers from 6 months to nil months. Close Brothers does not have a credit default swap (CDS) price, which typically determines Link's rating. However, Link noted a sharp and sustained fall in the Bank's equity price, which would typically be correlated with a sudden rise in the CDS price. As per the Council's Annual Investment Strategy this meant that Close Brothers was no longer an acceptable counterparty. The Bank's credit rating was later downgraded by Fitch to BBB+ on 20th February. At the opening of Quarter 1 2024/25, the council had one £5m loan outstanding with Close Brothers, which was repaid with full interest at expiry on 30th April 2024.

Debt Rescheduling

31. During April, the Council took advantage of a favourable debt rescheduling opportunity for its market debt loan with Barclays (£10.0m, 3.99%). After investigation and upon further advice from Link, the Council's treasury management consultants, a decision was made to repay the principal early. As a result of this action, the Council received a discount of £1.1m, after accounting for relevant execution fees.
32. The discount rate provided by Barclays was better than the PWLB equivalent premature repayment rate and hence the Council received a substantial discount.
33. As per the Link and Capital Economics long term forecasts, which suggest a reduction in the Bank of England base rate, repayment of this loan should also provide an opportunity for the Council to refinance in the future at a lower rate, potentially enabling further savings.

Compliance with Prudential and Treasury Indicators – Quarter 1

34. 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 June 2024, the Council has operated within the

treasury and prudential indicators set out in the Council's Treasury Management Strategy Statement for 2024/25, with the exception of the estimate of capital expenditure for 2024/25 which is now forecast to be £167m, £10m higher than the original estimate. The increase is fully funded by additional government capital grants and section 106 developer contributions in 2024/25. The Director of Corporate Resources reports that no difficulties are envisaged in complying with these indicators.

Resource Implications

35. 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 2024/2025 is £14.2m. Current bank interest forecasts show interest earned in 2024/2025 could be £19.2m. The increase in interest income is due to forecast Bank of England base rate levels being higher and for longer than forecast, and higher than estimated average Council balances. Average balances remain strong due to increases in earmarked reserves, latest phasing of spend on the capital programme and government grants received in advance. The forecast position is also compounded by the lag on changes to interest rates impacting the portfolio, as discussed in paragraph 20.

Recommendations

36. The Committee is asked to note this report.

Background papers

37. None.

Circulation under the Local Issues Alert Procedure

38. None.

Equality Implications

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

Human Rights Implications

40. There are no discernible human rights implications arising from this report.

Appendices

Appendix A - Economic Overview (For the quarter to June 2024)

Appendix B - Prudential and Treasury Indicators for 2024/25 as at 30th June 2024

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