Treasury Management Annual Report 2022/23

Telford & Wrekin Council

Contents

Treasury Management Annual Report 2022/23

Purpose

This Council is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2022/23. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management, (the Code), and the CIPFA Prudential Code for Capital Finance in Local Authorities, (the Prudential Code).

During 2022/23 the minimum reporting requirements were that the full Council should receive the following reports:

- an annual treasury strategy in advance of the year,
- a mid-year, (minimum), treasury update report, and
- an annual review following the end of the year describing the activity compared to the strategy, (this report)

The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This report is, therefore, important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by members.

This Council confirms that it has complied with the requirement under the Code to give prior scrutiny to all of the above treasury management reports by the Audit Committee before they were reported to the full Council. Member training on treasury management issues was undertaken during the year on 24th January 2023 in order to support members' scrutiny role.

Executive Summary

During 2022/23, the Council complied with its legislative and regulatory requirements. The key actual prudential and treasury indicators detailing the impact of capital expenditure activities during the year, with comparators, are as follows:

Prudential and treasury indicators	31.3.22 Actual (£'000)	2022/23 Original (£'000)	31.3.23 Actual (£'000)
Capital expenditure			
• Total	57,367	139,578	75,702
Capital Financing Requirement:			
• Total	500,140	600,793	520,687
• Less Other Long Term Liabilities	(50,880)	(47,888)	(47,888)
• Loans CFR	449,260	553,905	472,799
Gross borrowing			
• External Debt	282,743	401,700	347,221
Treasury Investments			
• Longer than 1 year	0	0	0
• Under 1 year	36,522	15,000	38,499
• Total	36,522	15,000	38,499
Net borrowing			
• Total	246,221	386,700	308,722

Other prudential and treasury indicators are to be found in the main body of this report. The Director of Finance & HR also confirms that borrowing was only undertaken for a capital purpose and the statutory borrowing limit, (the authorised limit), was not breached.

The financial year 2022/23 continued the challenging environment of previous years as the Bank of England began to increase the base rate in an attempt to stabilise inflation which hit a 40 year high in October 2022 of 11.1%. The base rate rose from 0.75% at the beginning of the year to 4.25% by the end of March 2023.

It should be noted that borrowing can only be undertaken to fund capital investment and not to support the revenue budget which supports the delivery of most Council services. The capital investment generates assets for the Council and the total value of assets held, excluding Infrastructure Assets, at 31 March 2023 was £621.7m some £274.5m greater than debt outstanding. In addition the Council also holds over £200m of other, Infrastructure, assets.

Introduction and Background

This report summarises the following:-

- Capital activity during the year;
- Impact of this activity on the Council's underlying indebtedness, (the Capital Financing Requirement);
- The actual prudential and treasury indicators;
- Overall treasury position identifying how the Council has borrowed in relation to this indebtedness, and the impact on investment balances;
- Summary of interest rate movements in the year;
- Detailed debt activity; and
- Detailed investment activity.

1. The Council's Capital Expenditure and Financing

The Council undertakes capital expenditure on long-term assets. These activities may either be:

- Financed immediately through the application of capital or revenue resources (capital receipts, capital grants, revenue contributions etc.), which has no resultant impact on the Council's borrowing need; or
- If insufficient financing is available, or a decision is taken not to apply resources, the capital expenditure will give rise to a borrowing need.

The actual capital expenditure forms one of the required prudential indicators. The table below shows the actual capital expenditure and how this was financed.

Capital Expenditure (£'000)	31.3.22 Actual	2022/23 Original	31.3.23 Actual
General Fund Service	47,213	116,528	60,211
Housing Investment Programme (NuPlace Ltd)	5,954	18,300	10,920
Property Investment Portfolio	4,200	4,750	4,571
Solar Farm	0	0	0
Capital Programme Expenditure	**57,367**	**139,578**	**75,702**
Financed in year from Government Grants, Capital Receipts, Revenue Contribution & External sources	37,036	39,292	50,449
Unfinanced capital expenditure (Borrowing)	**20,331**	**100,286**	**25,253**

2. The Council's Overall Borrowing Need

The Council's underlying need to borrow for capital expenditure is termed the Capital Financing Requirement (CFR). This figure is a gauge of the Council's indebtedness. The CFR results from the capital activity of the Council and resources used to pay for the capital spend. It represents the 2022/23 unfinanced capital expenditure (see above table), and prior years' net or unfinanced capital expenditure which has not yet been paid for by revenue or other resources.

Part of the Council's treasury activities is to address the funding requirements for this borrowing need. Depending on the capital expenditure programme, the treasury team organises the Council's cash position to ensure that sufficient cash is available to meet the capital plans and cash flow requirements. This may be sourced through borrowing from external bodies, (such as the Government, through the Public Works Loan Board [PWLB], or the money markets), or utilising temporary cash resources within the Council.

Reducing the CFR – the Council's underlying borrowing need (CFR) is not allowed to rise indefinitely. Statutory controls are in place to ensure that capital assets are broadly charged to revenue over the life of the asset. The Council is required to make an annual revenue charge, called the Minimum Revenue Provision – MRP, to reduce the CFR. This is effectively a repayment of the borrowing need. This differs from the treasury management arrangements which ensure that cash is available to meet capital commitments. External debt can also be borrowed or repaid at any time, but this does not change the CFR.

The Council's 2022/23 MRP Policy, (as required by DLUHC Guidance), was approved as part of the Treasury Management Strategy Report for 2022/23 on 3rd March 2023.

The Council's CFR for the year is shown below, and represents a key prudential indicator. It includes PFI and leasing schemes on the balance sheet, which technically increase the Council's borrowing need. No borrowing is actually required against these schemes as a borrowing facility is included in the contract.

CFR (£'000): *General Fund*	31.3.22 Actual	2022/23 Original	31.3.23 Actual
General Funded Service	383,374	402,480	395,020
Housing Investment Programme (NuPlace Ltd)	59,454	64,054	61,997
Property Investment Portfolio	53,512	57,617	59,870
Solar Farm	3,800	3,800	3,800
Closing balance	**500,140**	**527,951**	**520,687**
Less Other Long Term Liabilities	(50,880)	(47,888)	(47,888)
Loans CFR	**449,260**	**480,063**	**472,799**

Borrowing activity is constrained by prudential indicators for gross borrowing and the CFR, and by the authorised limit.

Gross borrowing and the CFR - in order to ensure that borrowing levels are prudent over the medium term and only for a capital purpose, the Council should ensure that its gross external borrowing does not, except in the short term, exceed the total of the capital financing requirement in the preceding year (2022/23) plus the estimates of any additional capital financing requirement for the current (2023/24) and next two financial years. This essentially means that the Council is not borrowing to support revenue expenditure. This indicator would allow for some flexibility to borrow in advance of the Councils immediate capital needs. The table below highlights the Council's gross borrowing position against the CFR. The Council has complied with this prudential indicator.

	31.3.22 Actual (£'000)	2022/23 Original (£'000)	31.3.23 Actual (£'000)
Gross borrowing position (external debt)	282,743	359,746	347,221

	31.3.22 Actual (£'000)	2022/23 Original (£'000)	31.3.23 Actual (£'000)
Loans CFR	449,260	553,905	472,799
(Under) / over funding of CFR	(166,517)	(194,159)	(125,578)

The authorised limit - the authorised limit is the "affordable borrowing limit" required by section 3 of the Local Government Act 2003. Once this has been set, the Council does not have the power to borrow above this level. The table below demonstrates that during 2022/23 the Council has maintained gross borrowing within its authorised limit.

The operational boundary – the operational boundary is the expected borrowing position of the Council during the year. Periods where the actual position is either below or over the boundary are acceptable subject to the authorised limit not being breached.

Actual financing costs as a proportion of net revenue stream - this indicator identifies the trend in the cost of capital, (borrowing and other long term obligation costs net of investment income), against the net revenue stream. See Appendix A for comparators.

	2022/23
Maximum gross borrowing position during the year	£347.7m
Authorised limit (Borrowing)	£495.0m
Operational boundary (Borrowing)	£475.0m
Financing costs as a proportion of net revenue stream	4.77%

3. Treasury Position as at 31st March 2023

The Council's treasury management debt and investment position is organised by the treasury management service in order to ensure adequate liquidity for revenue and capital activities, security for investments and to manage risks within all treasury management activities. Procedures and controls to achieve these objectives are well established both through member reporting detailed in the summary, and through officer activity detailed in the Council's Treasury Management Practices. At the end of 2022/23 the Council's treasury, (excluding borrowing by PFI and finance leases), position was as follows:

DEBT PORTFOLIO	31.3.22 Principal (£'000)	Interest Rate %	31.3.23 Principal (£'000)	Interest Rate %	Movement in Principal (£'000)
Fixed rate funding:					
- PWLB	201,714	2.55%	210,884	2.52%	9,170
- Municipal Loans	0.0	0.0%	308	2.10%	308
- Market	40,000	4.17%	40,000	4.17%	0.0
Variable rate funding:					
- Temporary	41,029	0.14%	96,029	1.91%	55,000
Total debt	**282,743**	**2.47%**	**347,221**	**2.65%**	**64,478**
Loans CFR	**449,260**		**472,799**		**23,539**
Over / (under) borrowing	**(166,517)**		**(125,578)**		**40,939**
Total investments	**36,522**	**0.07%**	**38,499**	**2.10%**	**1,977**
Net debt	**246,221**		**308,722**		**62,502**

The maturity structure of the debt portfolio was as follows:

	31.3.22 Actual		2022/23 original limits %		31.3.23 Actual	
	(£'000)	%	Lower	Upper	(£'000)	%
Under 12 months	51,437	18.2	0.0	70.0	107,208	30.9
12 months and within 24 months	10,250	3.6	0.0	30.0	21,705	6.3
24 months and within 5 years	31,800	11.2	0.0	50.0	33,196	9.6
5 years and within 10 years	42,899	15.2	0.0	75.0	45,679	13.2
10 years and within 30 years	36,357	12.9	0.0	75.0	34,433	9.9
30 years and above*	110,000	38.9	25.0	100.0	105,000	30.1
Total Borrowing	**282,736**	**100.0**			**347,221**	**100.0**

** this includes £25m Lenders Option Borrowers Options (LOBO) loans that are potentially callable at certain points before the maturity date.*

INVESTMENT PORTFOLIO	31.3.22 Actual (£'000)	31.3.22 Actual Split %	31.3.23 Actual (£'000)	31.3.23 Actual Split %
Treasury investments				
Banks	3,842	9.5	4,419	11.4
DMADF (H M Treasury)	27,700	75.8	29,100	75.6
Money Market Funds	4,980	14.7	4,980	12.9
Total managed in house	**36,522**	**100.0**	**38,499**	**100.0**
Total managed externally	0		0	
Total Treasury Investments	**36,522**	**100.0**	**38,499**	**100.0**

The maturity structure of the investment portfolio was as follows:

	31.3.22 Actual £000	2022/23 Budget £000	31.3.23 Actual £000
Investments			
Longer than 1 year	0	0	0
Up to 1 year	36,522	15,000	38,499
Total	**36,522**	**15,000**	**38,499**

4. 2022/23 Treasury Strategy

4.1 2022/23 Borrowing Strategy

In 2022/23 the level of Council borrowing was below its underlying need to borrow (the Capital Financing Requirement (CFR)). This was due to positive cash flow arising from Council's reserves and balances being available to support the treasury position. This strategy was prudent as investment returns were initially low and minimising counterparty risk on placing investments also needed to be considered. In 2022/23 itself, cashflow benefits reduced and were replaced by borrowing.

A cost of carry generally remained in place during the year on any new long-term borrowing that was not immediately used to finance capital expenditure, as it would have caused a temporary increase in cash balances; this would have incurred a revenue cost – the difference between (higher) borrowing costs and (lower) investment returns. As the cost of carry dissipated, the Council sought to avoid taking on long-term borrowing at elevated levels (>4%) and has focused on a policy of internal and temporary borrowing, supplemented by short-dated borrowing (<3 years) as appropriate.

The policy of avoiding new borrowing by running down spare cash balances has served well over the last few years. However, this has been kept under review to avoid incurring higher borrowing costs in the future when the Authority may not be able to avoid new borrowing to finance capital expenditure and/or the refinancing of maturing debt.

Against this background and the risks within the economic forecast, caution was adopted with the treasury operations. The Director of Finance & HR therefore monitors interest rates in financial markets and adopts a pragmatic strategy based upon the following principles to manage interest rate risks*:*

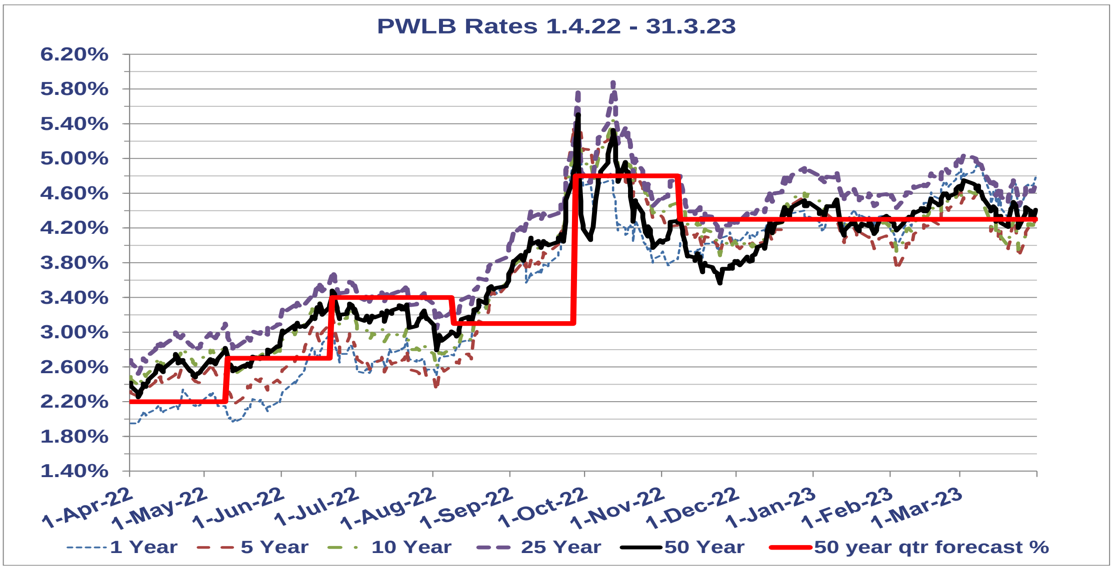
- if it had been felt that there was a significant risk of a sharp FALL in long and short-term rates, (e.g., due to a marked increase of risks around relapse into recession or of risks of deflation although clearly this has not been the case recently), then long term borrowings would have been postponed, and potential rescheduling from fixed rate funding into short term borrowing would have been considered.
- if it had been felt that there was a significant risk of a much sharper and sustained RISE in long and short-term rates than initially expected, perhaps arising from an acceleration in the start date and in the rate of increase in central rates in the USA and UK, an increase in world economic activity or a sudden increase in inflation risks, then the portfolio position would have been re-appraised. Most likely, fixed rate funding would have been drawn whilst interest rates were lower than they were projected to be in the next few years. Clearly no one has a crystal ball and officers take decisions based on the best available advice from external specialist advisors although market conditions can change quickly and unexpectedly for example arising from reactions to world events.

Interest rate forecasts were initially suggesting only gradual rises in short, medium and longer-term fixed borrowing rates during 2022/23 but by August it had become clear that inflation was moving up towards 40-year highs, and the Bank of England engaged in monetary policy tightening at every Monetary Policy Committee meeting during 2022, and into 2023, either by increasing Bank Rate by 0.25% or 0.5% each time. Currently the CPI measure of inflation is still above 10% in the UK but is expected to fall back towards 4% by year end. Nonetheless, there remain significant risks to that central forecast.

High / Low / Average PWLB Rates for 2022/23

	1 Year	5 Year	10 Year	25 Year	50 Year
Low	1.95%	2.18%	2.36%	2.52%	2.25%
Date	01/04/22	13/05/22	04/04/22	04/04/22	04/04/22
High	5.11%	5.44%	5.45%	5.88%	5.51%
Date	28/09/22	28/09/22	12/10/22	12/10/22	28/09/22
Average	3.57%	3.62%	3.76%	4.07%	3.74%
Spread	3.16%	3.26%	3.09%	3.36%	3.26%

PWLB Rates 2022/23



PWLB rates are based on gilt (UK Government bonds) yields through HM Treasury determining a specified margin to add to gilt yields. The main influences on gilt yields are Bank Rate, inflation expectations and movements in US treasury yields. Inflation targeting by the major central banks has been successful over the last 30 years in lowering inflation and the real equilibrium rate for central rates has fallen considerably due to the high level of borrowing by consumers: this means that central banks do not need to raise rates as much now to have a major impact on consumer spending, inflation, etc. This has pulled down the overall level of interest rates and bond yields in financial markets over the last 30 years. Indeed, in recent years many bond yields up to 10 years in the Eurozone turned negative on expectations that the EU would struggle to get growth rates and inflation up from low levels. In addition, there has, at times, been an inversion of bond yields in the US whereby 10-year yields have fallen below shorter-term yields. In the past, this has been a precursor of a recession.

However, since early 2022, yields have risen dramatically in all the major developed economies, first as economies opened post-Covid; then because of the inflationary impact of the war in Ukraine in respect of the supply side of many goods. In particular, rising cost pressures emanating from shortages of energy and some food categories have been central to inflation rising rapidly. Furthermore, at present the FOMC, ECB and Bank of England are all being challenged by persistent inflation that is exacerbated by very tight labour markets and high wage increases relative to what central banks believe to be sustainable

4.2 2022/23 Treasury Investment Strategy

Investment returns picked up throughout the course of 2022/23 as central banks, including the Bank of England, realised that inflationary pressures were not transitory, and that tighter monetary policy was called for.

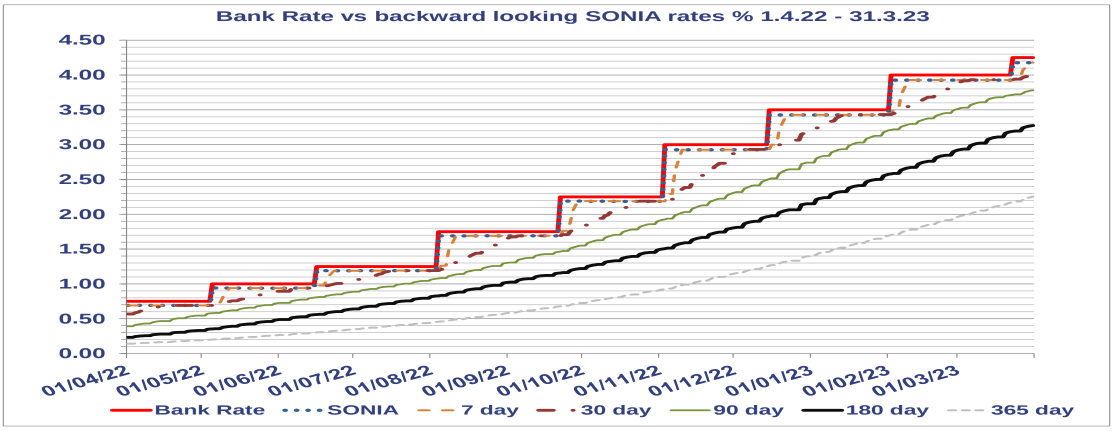
Starting April at 0.75%, Bank Rate moved up in stepped increases of either 0.25% or 0.5%, reaching 4.25% by the end of the financial year, with the potential for further increases in 2023/24.

The sea-change in investment rates meant local authorities were faced with the challenge of pro-active investment of surplus cash for the first time in over a decade, and this emphasised the need for a detailed working knowledge of cashflow projections so that the appropriate balance between maintaining cash for liquidity purposes, and “laddering” deposits on a rolling basis to lock in the increase in investment rates as duration was extended, became an on-going feature of the investment landscape.

With bond markets selling off, equity valuations struggling to make progress and, latterly, property funds enduring a wretched Q4 2022, the more traditional investment options, such as specified investments (simple to understand, and less than a year in duration) became more actively used.
Meantime, through the autumn, and then in March 2023, the Bank of England maintained various monetary policy easing measures as required to ensure specific markets, the banking system and the economy had appropriate levels of liquidity at times of stress.

Nonetheless, while the Council has taken a cautious approach to investing, it is also fully appreciative of changes to regulatory requirements for financial institutions in terms of additional capital and liquidity that came about in the aftermath of the Great Financial Crisis of 2008/9. These requirements have provided a far stronger basis for financial institutions, with annual stress tests by regulators evidencing how institutions are now far more able to cope with extreme stressed market and economic conditions.

Investment Benchmarking Data – Sterling Overnight Index Averages (Backward-looking) 2022/23



FINANCIAL YEAR TO QUARTER ENDED 31/03/2023							
	Bank Rate	SONIA	7 day	30 day	90 day	180 day	365 day
High	4.25	4.18	4.18	4.00	3.78	3.27	2.25
High Date	23/03/2023	31/03/2023	31/03/2023	31/03/2023	31/03/2023	31/03/2023	31/03/2023
Low	0.75	0.69	0.69	0.57	0.39	0.23	0.14
Low Date	01/04/2022	28/04/2022	29/04/2022	01/04/2022	01/04/2022	01/04/2022	01/04/2022
Average	2.30	2.24	2.20	2.09	1.81	1.42	0.90
Spread	3.50	3.49	3.49	3.43	3.39	3.04	2.11

5. Borrowing Outturn

Treasury Borrowing – During the year 3 new PWLB loans were raised
Borrowing - loans were drawn to fund the net unfinanced capital expenditure and naturally maturing debt.

The loans drawn were:

Lender	Date Raised	Principal	Type	Interest Rate	Duration
PWLB	*28/04/2022	£5.0m	Fixed interest rate - Annuity	2.56%	10 years
PWLB	*09/08/2022	£5.0m	Fixed interest rate - EIP	2.34%	12 years
PWLB	*22/12/2022	£10.0m	Fixed interest rate - Maturity	4.16%	1.5 years

This compares with a budget assumption of borrowing at an interest rate of 2.5%.
*loans included in 2022/23 Treasury Update Report presented to Audit Committee 24th January 2023.

Borrowing in advance of need
The Council has not borrowed more than, or in advance of its needs, purely in order to profit from the investment of the extra sums borrowed.

Early Repayments or Rescheduling
No loans were repaid early or rescheduled during the year as the average 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

Debt Performance
As highlighted in Section 3 the average interest rate for borrowing rose slightly over the course of the year from 2.47% to 2.65% as the cost of replacing temporary loans increased in line with the movements in the base rate.

6. Treasury Investment Outturn

Investment Policy – the Council's investment policy is governed by DLUHC investment guidance, which has been implemented in the annual investment strategy approved by the Council on 3rd March 2022. This policy sets out the approach for choosing investment counterparties, and is based on credit ratings provided by the three main credit rating agencies.

The investment activity during the year conformed to the approved strategy, and the Council had no liquidity difficulties.

Investments held by the Council

- The Council maintained an average daily balance of £29.659m of internally managed funds.
- The internally managed funds earned an average rate of return of 2.1%
- The comparable performance indicator is the average SONIA rate, which was 2.2%
- The majority of the portfolio is held within the Governments secure Debt Management Office for security, in line with the strategy, which pays slightly lower than market average interest rates.

Investments (£'000)	31.3.22	31.3.23
Cash Investments	36,522	38,499

At the 31st March 2023 the Councils total usable reserves were £116.2m, which has supported the overall cash flow position and the level of internal borrowing.

7. 2022/23 Overall Outturn

Overall a net benefit of £3.951m was made against budget for the year. The sound overall position has resulted from a mix of cash flow benefits plus pro-active treasury management activities through the active management of borrowing and taking advantage of low interest rates at the beginning of the year.

8. Shropshire Council Debt

The Council makes an annual contribution towards Shropshire Council costs on pre disaggregation debt (i.e. pre unitary inception). The contribution in 2022/23 was £1.148m and interest paid averaged 4.7%. The rate of interest paid on this is managed by Shropshire and is considerably higher than the rate payable by Telford & Wrekin Council on its borrowing.

9. Leasing

Each year the Council arranges both finance leases and operating leases for assets such as vehicles, computers and equipment. This helps spread the cost over a number of years in line with the anticipated life of the equipment.

During 2022/23 no new leases were arranged.

10. The Economy and Interest Rates

10.1 UK Economy

Against a backdrop of stubborn inflationary pressures, the easing of Covid restrictions in most developed economies, the Russian invasion of Ukraine, and a range of different UK Government policies, it is no surprise that UK interest rates have been volatile right across the curve, from Bank Rate through to 50-year gilt yields, for all of 2022/23.
Market commentators' misplaced optimism around inflation has been the root cause of the rout in the bond markets with, for example, UK, EZ and US 10-year yields all rising by over 200bps in 2022. The table below provides a snapshot of the conundrum facing central banks: inflation is elevated but labour markets are extra-ordinarily tight, making it an issue of fine judgment as to how far monetary policy needs to tighten.

	UK	Eurozone	US
Bank Rate	4.25%	3%	4.75%-5%
GDP	0.1%q/q Q4 (4.1%y/y)	+0.1%q/q Q4 (1.9%y/y)	2.6% Q4 Annualised
Inflation	10.4%y/y (Feb)	6.9%y/y (Mar)	6.0%y/y (Feb)
Unemployment Rate	3.7% (Jan)	6.6% (Feb)	3.6% (Feb)

Q2 of 2022 saw UK GDP deliver growth of +0.1% q/q, but this was quickly reversed in the third quarter, albeit some of the fall in GDP can be placed at the foot of the extra Bank Holiday in the wake of the Queen's passing. Q4 GDP was positive at 0.1% q/q. Most recently, January saw a 0.3% m/m increase in GDP as the number of strikes reduced compared to December. In addition, the resilience in activity at the end of 2022 was, in part, due to a 1.3% q/q rise in real household disposable incomes. A big part of that reflected the £5.7bn payments received by households from the government under the Energy Bills Support Scheme.

Nevertheless, CPI inflation picked up to what should be a peak reading of 11.1% in October, although hopes for significant falls from this level will very much rest on the movements in the gas and electricity markets, as well as the supply-side factors impacting food prices. On balance, most commentators expect the CPI measure of inflation to drop back towards 4% by the end of 2023. As of February 2023, CPI was 10.4%.

The UK unemployment rate fell through 2022 to a 48-year low of 3.6%, and this despite a net migration increase of c500k. The fact remains, however, that with many economic participants registered as long-term sick, the UK labour force shrunk by c500k in the year to June. Without an increase in the labour force participation rate, it is hard to see how the UK economy will be able to grow its way to prosperity, and with average wage increases running at over 6% the MPC will be concerned that wage inflation will prove just as sticky as major supply-side shocks to food (up 18.3% y/y in

February 2023) and energy that have endured since Russia's invasion of Ukraine on 22 February 2022.

Bank Rate increased steadily throughout 2022/23, starting at 0.75% and finishing at 4.25%.

In the interim, following a Conservative Party leadership contest, Liz Truss became Prime Minister for a tumultuous seven weeks that ran through September and October. Put simply, the markets did not like the unfunded tax-cutting and heavy spending policies put forward by her Chancellor, Kwasi Kwarteng, and their reign lasted barely seven weeks before being replaced by Prime Minister Rishi Sunak and Chancellor Jeremy Hunt. Their Autumn Statement of the 17th of November gave rise to a net £55bn fiscal tightening, although much of the "heavy lifting" has been left for the next Parliament to deliver. However, the markets liked what they heard, and UK gilt yields have reversed the increases seen under the previous tenants of No10/11 Downing Street, although they remain elevated in line with developed economies generally.

As noted above, GDP has been tepid throughout 2022/23, although the most recent composite Purchasing Manager Indices for the UK, US, EZ and China have all surprised to the upside, registering survey scores just above 50 (below suggests economies are contracting, and above suggests expansion). Whether that means a shallow recession, or worse, will be avoided is still unclear. Ultimately, the MPC will want to see material evidence of a reduction in inflationary pressures and a loosening in labour markets. Realistically, that is an unlikely outcome without unemployment rising and wage settlements falling from their current levels. At present, the bigger rise in employment kept the ILO unemployment rate unchanged at 3.7% in January. Also, while the number of job vacancies fell for the ninth consecutive month in February, they remained around 40% above pre-pandemic levels.

Our economic analysts, Capital Economics, expect real GDP to contract by around 0.2% q/q in Q1 and forecast a recession this year involving a 1.0% peak-to-trough fall in real GDP.

The £ has remained resilient of late, recovering from a record low of $1.035, on the Monday following the Truss government's "fiscal event", to $1.23. Notwithstanding the £'s better run of late, 2023 is likely to see a housing correction of some magnitude as fixed-rate mortgages have moved above 4.5% and affordability has been squeezed despite proposed Stamp Duty cuts remaining in place.

As for equity markets, the FTSE 100 started 2023 strongly, rising to a record high of 8,014 on 20th February, as resilient data and falling inflation boosted earnings. But global equities fell sharply after concerns over the health of the global banking system emerged early in March. The fall in the FTSE 100 was bigger than the drop in the US S&P 500. Indeed, at around 7,600 now, the FTSE is 5.2% below its record high on 20th February, while the S&P 500 is only 1.9% lower over the same period. That's despite UK banks having been less exposed and equity prices in the UK's financial sector not falling as far. It may be due to the smaller decline in UK interest rate expectations and bond yields, which raise the discounted value of future earnings, compared to the US.

10.2 USA Economy

The flurry of comments from Fed officials over recent months suggest there is still an underlying hawkish theme to their outlook for interest rates. Markets are pricing in a further interest rate increases of 25-50bps, on top of the current interest rate range of 4.75% - 5%.

In addition, the Fed is expected to continue to run down its balance sheet once the on-going concerns about some elements of niche banking provision are in the rear-view mirror.
As for inflation, it is currently at c6% but with the economy expected to weaken during 2023, and wage data already falling back, there is the prospect that should the economy slide into a recession of any kind there will be scope for rates to be cut at the backend of 2023 or shortly after.

10.3 EU Economy

Although the Euro-zone inflation rate has fallen below 7%, the ECB will still be mindful that it has further work to do to dampen inflation expectations and it seems destined to raise rates to 4% in order to do so. Like the UK, growth has remained more robust than anticipated but a recession in 2023 is still seen as likely by most commentators.

11. Other

IFRS 16: The implementation of the new IFRS 16 Leases accounting standard, for Local Government, has been further delayed until 2024/25.

Prudential and Treasury Indicators are detailed in Appendix Ai.

Appendix Ai: Prudential and treasury indicators

1. PRUDENTIAL INDICATORS	2021/22	2022/23	2022/23
	actual	original	actual
	£'000	£'000	£'000
Capital Expenditure	57,367	139,578	75,702
Ratio of financing costs to net revenue stream	3.84%	7.3%	4.77%
Gross borrowing requirement General Fund			
brought forward 1 April	281,085	301,400	282,743
carried forward 31 March	282,743	401,700	347,221
in year borrowing requirement	1,658	100,300	64,478
Loans CFR	449,260	553,905	472,799
Annual change in Loans CFR	19,580	99,074	23,539

2. TREASURY MANAGEMENT INDICATORS	2021/22	2022/23	2022/23
	actual	original	actual
	£'000	£'000	£'000
Authorised Limit for external debt -			
borrowing	450,000	495,000	495,000
other long term liabilities	64,000	64,000	64,000
TOTAL	514,000	559,000	559,000
Operational Boundary for external debt -			
borrowing	430,000	475,000	475,000
other long term liabilities	60,000	60,000	60,000
TOTAL	490,000	535,000	535,000
Actual external debt	282,743	401,700	347,221

Maturity structure of fixed rate borrowing during 2022/23	**upper limit**	**lower limit**	**31.03.23**
Under 12 months	0.0%	70.0%	30.9%
12 months and within 24 months	0.0%	30.0%	6.3%
24 months and within 5 years	0.0%	50.0%	9.6%
5 years and within 10 years	0.0%	75.0%	13.2%
10 years and within 30 years	0.0%	75.0%	9.9%
30 years and above	0.0%	100.0%	30.1%
Maturity structure of investments during 2021/22	upper limit	lower limit	
Longer than 1 year	0.0%	95.0%	0.0%
Up to 1 year	0.0%	100.0%	100.0%

Credit risk indicator	2021/22 Actual	2022/23 Target	2022/23 Actual
Portfolio average credit score	1.44	6 or lower	1.46

Target – 6 or lower is equivalent to a credit rating of ‘A’ or higher

ABBREVIATIONS USED IN THIS REPORT

CFR: capital financing requirement - the council's annual underlying borrowing need to finance capital expenditure and a measure of the council's total outstanding indebtedness.

CIPFA: Chartered Institute of Public Finance and Accountancy – the professional accounting body that oversees and sets standards in local authority finance and treasury management.

CPI: consumer price index – the official measure of inflation adopted as a common standard by countries in the EU. It is a measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food and medical care. It is calculated by taking price changes for each item in the predetermined basket of goods and averaging them.

ECB: European Central Bank - the central bank for the Eurozone

EU: European Union

EZ: Eurozone -those countries in the EU which use the euro as their currency

Fed: the Federal Reserve System, often referred to simply as "the Fed," is the central bank of the United States. It was created by the Congress to provide the nation with a stable monetary and financial system.

FOMC: the Federal Open Market Committee – this is the branch of the Federal Reserve Board which determines monetary policy in the USA by setting interest rates and determining quantitative easing policy. It is composed of 12 members--the seven members of the Board of Governors and five of the 12 Reserve Bank presidents.

GDP: gross domestic product – a measure of the growth and total size of the economy.

G7: the group of seven countries that form an informal bloc of industrialised democracies--the United States, Canada, France, Germany, Italy, Japan, and the United Kingdom--that meets annually to discuss issues such as global economic governance, international security, and energy policy.

Gilts: gilts are bonds issued by the UK Government to borrow money on the financial markets. Interest paid by the Government on gilts is called a coupon and is at a rate that is fixed for the duration until maturity of the gilt, (unless a gilt is index linked to inflation); while the coupon rate is fixed, the yields will change inversely to the price of gilts i.e. a rise in the price of a gilt will mean that its yield will fall.

HRA: housing revenue account.

IMF: International Monetary Fund - the lender of last resort for national governments which get into financial difficulties.

LIBID: the London Interbank Bid Rate is the rate bid by banks on deposits i.e., the rate at which a bank is willing to borrow from other banks. It is the "other end" of the LIBOR (an offered, hence "ask" rate, the rate at which a bank will lend). These benchmarks ceased on 31st December 2021 and have, generally, been replaced by SONIA, the Sterling Overnight Index Average.

MHCLG: the Ministry of Housing, Communities and Local Government - the Government department that directs local authorities in England.

MPC: the Monetary Policy Committee is a committee of the Bank of England, which meets for one and a half days, eight times a year, to determine monetary policy by setting the official interest rate in the United Kingdom, (the Bank of England Base Rate, commonly called Bank Rate), and by making decisions on quantitative easing.

MRP: minimum revenue provision - a statutory annual minimum revenue charge to reduce the total outstanding CFR, (the total indebtedness of a local authority).

PFI: Private Finance Initiative – capital expenditure financed by the private sector i.e. not by direct borrowing by a local authority.

PWLB: Public Works Loan Board – this is the part of H.M. Treasury which provides loans to local authorities to finance capital expenditure.

QE: quantitative easing – is an unconventional form of monetary policy where a central bank creates new money electronically to buy financial assets, such as government bonds, (but may also include corporate bonds). This process aims to stimulate economic growth through increased private sector spending in the economy and also aims to return inflation to target. These purchases increase the supply of liquidity to the economy; this policy is employed when lowering interest rates has failed to stimulate economic growth to an acceptable level and to lift inflation to target. Once QE has achieved its objectives of stimulating growth and inflation, QE will be reversed by selling the bonds the central bank had previously purchased, or by not replacing debt that it held which matures. The aim of this reversal is to ensure that inflation does not exceed its target once the economy recovers from a sustained period of depressed growth and inflation. Economic growth, and increases in inflation, may threaten to gather too much momentum if action is not taken to 'cool' the economy.

RPI: the Retail Price Index is a measure of inflation that measures the change in the cost of a representative sample of retail goods and services. It was the UK standard for measurement of inflation until the UK changed to using the EU standard measure of inflation – Consumer Price Index. The main differences between RPI and CPI is in the way that housing costs are treated and that the former is an arithmetical mean whereas the latter is a geometric mean. RPI is often higher than CPI for these reasons.

SONIA: the Sterling Overnight Index Average. Generally, a replacement set of indices (for LIBID) for those benchmarking their investments. The benchmarking options include using a forward-looking (term) set of reference rates and/or a backward-looking set of reference rates that reflect the investment yield curve at the time an investment decision was taken.

TMSS: the annual treasury management strategy statement reports that all local authorities are required to submit for approval by the full council before the start of each financial year.