

REPORT

SUBJECT:	TREASURY MANAGEMENT ACTIVITY UPDATE - QUARTER 2 2023/24
MEETING:	Governance & Audit Committee
DATE:	4th December 2023
DIVISIONS/WARD AFFECTED:	All

1. **PURPOSE:**

- 1.1. The Prudential Code and CIPFA treasury guidance require local authorities to produce annually a Treasury Management Strategy Statement and Prudential Indicators on their likely financing and investment activity, and to ensure that the appropriate governance function that oversees the treasury management activities of the Authority is kept informed of activity quarterly.
- 1.2. The Authority's treasury management strategy for 2023/24 was approved by Council on 9th March 2023. Over the second quarter of the year the Authority has continued to borrow and invest substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk remains central to the Authority's treasury management strategy.
- 1.3. This report represents the second update of treasury management activity during 2023/24 following the Quarter 1 report being considered by this Committee on the 27th of July 2023.

2. **RECOMMENDATIONS:**

That Governance & Audit committee review the treasury management activities and the performance achieved in the second quarter of 2023/24 as part of their delegated responsibility to provide scrutiny of treasury policy, strategy and activity on behalf of Council.

3. **KEY ISSUES:**

3.1. **Key data metrics during the quarter:**

Type	Metric	Start of Quarter	End of Quarter
External	Bank of England base rate	4.5%	5.25%
External	UK Consumer Prices Index	7.9%	6.7%
External	10-year UK gilt yield	4.39%	4.45%
Internal	Borrowing	180.8m	179.4m
Internal	Borrowing Average rate	3.24%	3.38%
Internal	Investments	25.0m	34.0m
Internal	Investment Average rate	4.54%	4.88%
Internal	Credit score/rating	AA- / 3.90	AA- 3.91

3.2. **Key messages:**

Treasury management activities undertaken during the quarter complied fully with the CIPFA code and the limits and indicators as set out in the Authority's approved Treasury Management Strategy.

A movement from Money Market Funds into Government investment products to reduce

overall “bail in” risk in light of the comparatively similar returns on both investments.

Cash balances remain resolutely high resulting in overall borrowing remaining fairly static whilst investment balances increased over the period.

£3.6m of Lender Option Borrower Option loans were called during the quarter. The Authority chose to repay these at nil cost.

A new Environmental, Social and Governance (ESG) specific investment product has been opened during the second quarter and will be prioritised for investment going forward.

4. **ECONOMIC SUMMARY**

- 4.1. During the second quarter of 2023/24 UK inflation remained stubbornly high over much the period compared to the US and euro zone, keeping expectations elevated of how much further the Bank of England (BoE) would hike rates compared to the regions. However, inflation data published in the latter part of the period undershot expectations, causing financial markets to reassess the peak in BoE Bank Rate. This was followed very soon after by the BoE deciding to keep Bank Rate on hold at 5.25% in September, against expectation for another 0.25% rise.
- 4.2. Shortly after the period ended, CPI inflation year on year to October was announced at 4.6%, a higher-than-expected fall from 6.7% in September. The sharp fall in the headline rate was flagged well in advance and CPI may ease more slowly from here, particularly with current levels of wage growth. The MPC is not likely to be in any hurry to cut Bank Rate, although we expect economic growth to slow more materially as time passes.

5. **BORROWING ACTIVITY DURING THE QUARTER:**

- 5.1. UK gilt yields have remained volatile, as in the first quarter since early April following signs that UK growth had been more resilient, inflation stickier than expected, and that the Bank of England saw persistently higher rates through 2023/24 as key to dampening domestic demand.
- 5.2. Gilt yields, and consequently PWLB borrowing rates, rose and broadly remained at elevated levels. On 30th September, the PWLB certainty rates for maturity loans were 5.26% for 10 year loans, 5.64% for 20-year loans and 5.43% for 50-year loans. Their equivalents on 30th June 2023 were 5.26%, 5.37% and 4.95% respectively.
- 5.3. In an environment of rising interest rates the authority has benefited from arranging forward starting short term loans. Short-term loans have been arranged up to ten months in advance at rates lower than those available at the start date and in some cases at rates lower than those available on the authorities’ investments. As we are likely to have reached peak interest rate this strategy will no longer be viable
- 5.4. The authorities’ borrowing position at the end of the second quarter can be seen below:

	30.6.23 Balance £m	30.6.23 Weighted Average Rate %	30.6.23 Weighted Average Maturity (years)	Balance Movement	30.9.23 Balance £m	30.9.23 Weighted Average Rate %	30.9.23 Weighted Average Maturity (years)
Public Works Loan Board	118.7	3.3	21.4	(2.8)	115.9	3.2	21.7
Banks (LOBO)	13.6	4.8	18.5	(3.6)	10.0	4.9	18.4
Welsh Gov Interest Free	5.5	0.0	3.3	(0.0)	5.5	0.0	3.0

Local authorities/Other	43.0	3.1	0.3	5.0	48.0	3.9	0.5
Total borrowing	180.8	3.2	15.6	(1.4)	179.4	3.4	15.2

5.5. The authorities total borrowing has remained fairly static over the second quarter. One lender exercised their option to call and increase the interest rate on a £3.6m Lender's Option Borrower's Option Loan from 4.6% to 6.12%. The authority chose to repay this loan at no extra cost, financing from the repayment through short term cashflows. Principal repayment of PWLB equal instalment of principal (EIP) loans has reduced the balance by a further £2.8m. This movement was offset with a new temporary loan of £5m.

6. **INVESTMENT ACTIVITY DURING THE QUARTER:**

6.1. During the second quarter, the authority's investment balances ranged from between £22.3m and £55.0m due to timing differences between income and expenditure. The movement in investments during the quarter was:

	30.6.23 Balance	Net Movement	30.9.23 Balance	30.9.23 Income Return	30.9.23 Weighted Average Maturity Days
	£m	£m	£m	%	
Banks & building societies (unsecured)	(0.5)	(1.5)	(2.0)	Average 4.64%	Up to 180 days
Government (incl. local authorities)	(3.0)	(21.5)	(24.5)		
Money Market Funds (MMFs)	(17.5)	14.0	(3.5)	6.11%	N/A
Multi asset income, Pooled funds	(4.0)	0.0	(4.0)		
Total investments	(25.0)	(9.0)	(34.0)		

6.2. UK Bank Rate increased by 0.75% over the quarter, from 4.5% at the end of June to 5.25% by the end of September. Short-dated cash rates rose commensurately, with 3-month rates rising to around 5.32% and 12-month rates to nearly 5.83%. The rates on DMADF deposits also rose, ranging between 5.17% and 5.24% by the end of September and Money Market Rates between 5.35% and 5.19%.

6.3. At the end of the first quarter the DMADF offered comparably higher returns and lower bail in risk compared to Money market funds. As such, during the second quarter the Authority moved a higher proportion of investments to the DMADF. The returns of each investment will be monitored over the third quarter.

6.4. £4m of the Authority's investments are invested in externally managed strategic pooled multi-asset and property funds where short-term security and liquidity are lesser considerations, and the objectives instead are regular revenue income and longer-term price stability. These funds generated £108k or an annualised average 6.11% income return, together with a £76k unrealised capital loss over the second quarter. Total unrealised capital losses since purchase stand at £506k.

7. **NON-TREASURY INVESTMENTS:**

7.1. The authority continues to hold £31.4m of non-financial asset investments and their forecast performance can be seen in the table below:

	Forecast Net (income) / loss @ Month 6 2023/24 £000's	Carrying Value 31.03.23 £000's	Net return 2023/24 %	Net return 2022/23 %
Oak Grove Solar Farm	(559)	5,485	10.19	13.44
Newport Leisure Park & service loan	(219)	19,756	1.11	0.01
Castlegate Business Park	216	6,159	(3.51)	(6.58)
Total	(562)	31,400	1.79	1.06

7.2. The investment at Newport Leisure park continues to provide a net income stream for the Authority, although this remains lower than the expected 2% return after borrowing until currently negotiated rent free periods end.

7.3. The investment in Castlegate is still providing a net negative ROI, however continued negotiations with interested parties should bring back a positive net return in 2024-25 following rent free periods. This continues to represent a significant improvement on the position since the anchor tenant vacated their space in Spring 2022.

7.4. One non-treasury investment was disposed of during the period, relating to the commercial loan with Broadway Partners Limited (BPL). Following an administration process, in September the administrators identified a buyer for BPL and a deal was concluded shortly after. On 27th of September all outstanding loan principal and interest due was repaid. The interest received over the life of the loan totalled £159k.

8. **ESG:**

8.1. A new ESG specific investment product has been opened during the second quarter of the year. This fund aims to provide security of capital and liquidity while also focusing on the performance of the underlying issuers on a range of environmental, social and governance metrics.

8.2. The authority's investment portfolio is reviewed against three ethical investment charters which are updated each quarter. Any funds which do not sign up to each of the three charters will be removed from the investment portfolio.

9. **CONSULTEES**

Cabinet Member - Resources

Deputy Chief Executive, (Section 151 officer)

Arlingclose Limited – External Treasury management advisors to Monmouthshire CC

10. **BACKGROUND PAPERS**

Appendix 1

Glossary of treasury terms

11. **AUTHORS**

Daniel Francis
Finance Business Partner
Email: danielfrancis@monmouthshire.gov.uk
Phone: (01633) 644895

Jonathan S. Davies
Head of Finance
email: jonathandavies2@monmouthshire.gov.uk
phone: (01633) 644114