APPENDIX A

TREASURY MANAGEMENT MID YEAR REVIEW 2021/22

A1. SUMMARY OF TREASURY MANAGEMENT INDICTORS

The City Council approved the authorised limit (the maximum amount of borrowing permitted by the Council) and the operational boundary (the maximum amount of borrowing that is expected) on 9th February 2021. The Council's debt at 30th September was as follows:

Prudential Indicator	**Limit** £m	**Actual** £m
Authorised Limit - the maximum amount of borrowing permitted by the Council	963	768
Operational Boundary - the maximum amount of borrowing that is expected	945	768

The maturity structure of the Council's fixed rate borrowing was:

	Under 1 Year	**1 to 2 Years**	**3 to 5 Years**	**6 to 10 Years**	**11 to 20 Years**	**21 to 30 Years**	**31 to 40 Years**	**41 to 50 Years**
Minimum proportion of loans maturing	0%	0%	0%	0%	0%	0%	0%	0%
Maximum proportion of loans maturing	10%	10%	10%	20%	30%	40%	40%	50%
Actual proportion of loans maturing	1%	1%	4%	13%	13%	5%	32%	31%

The maturity structure of the Council's variable rate borrowing was:

	Under 1 Year	**1 to 2 Years**	**3 to 5 Years**	**6 to 10 Years**	**11 to 20 Years**	**21 to 30 Years**	**31 to 40 Years**	**41 to 50 Years**
Minimum proportion of loans maturing	0%	0%	0%	0%	0%	0%	0%	0%
Maximum proportion of loans maturing	10%	10%	10%	20%	30%	40%	40%	40%
Actual proportion of loans maturing	2%	2%	6%	11%	23%	25%	17%	14%

Surplus cash invested for periods longer than 365 days at 30th September 2021 was:

	Limit £m	**Quarter 1 Actual** £m
Maturing after 31/3/2022	200	82
Maturing after 31/3/2023	134	41
Maturing after 31/3/2024	103	4

A2. GOVERNANCE

The Treasury Management Policy approved by the City Council on 16th March 2021 provides the framework within which treasury management activities are undertaken.

There have been no breaches of these policies during 2021/22 up to the period ending 30th September 2021.

A3. INTEREST RATE FORECASTS

When the Bank of England's Monetary Policy Committee (MPC) met on 24th September there was a major shift in the tone of the MPC's minutes at this meeting from the previous meeting in August which had majored on indicating that some tightening in monetary policy was now on the horizon, but also not wanting to stifle economic recovery by too early an increase in Bank Rate. However, this time the MPC's words indicated there had been a marked increase in concern that more recent increases in prices, particularly the increases in gas and electricity prices in October and due again next April, are, indeed, likely to lead to faster and higher inflation expectations and underlying wage growth, which would in turn increase the risk that price pressures would prove more persistent next year than previously expected. Indeed, to emphasise its concern about inflationary pressures, the MPC pointedly chose to reaffirm its commitment to the 2% inflation target in its statement; this suggested that it was now willing to look through the flagging economic recovery during the summer to prioritise bringing inflation down next year. This is a reversal of its priorities in August and a long way from words at earlier MPC meetings which indicated a willingness to look through inflation overshooting the target for limited periods to ensure that inflation was 'sustainably over 2%'. Indeed, whereas in August the MPC's focus was on getting through a winter of temporarily high energy prices and supply shortages, believing that inflation would return to just under the 2% target after reaching a high around 4% in late 2021, now its primary concern is that underlying price pressures in the economy are likely to get embedded over the next year and elevate future inflation to stay significantly above its 2% target and for longer.

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 forecasts are shown below.

Link Group Interest Rate View	29.9.21									
	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
BANK RATE	0.10	0.10	0.25	0.25	0.25	0.25	0.50	0.50	0.50	0.75
3 month ave earnings	0.10	0.10	0.20	0.20	0.30	0.40	0.50	0.50	0.60	0.70
6 month ave earnings	0.20	0.20	0.30	0.30	0.40	0.50	0.60	0.60	0.70	0.80
12 month ave earnings	0.30	0.40	0.50	0.50	0.50	0.60	0.70	0.80	0.90	1.00
5 yr PWLB	1.40	1.40	1.50	1.50	1.60	1.60	1.60	1.70	1.70	1.70
10 yr PWLB	1.80	1.80	1.90	1.90	2.00	2.00	2.00	2.10	2.10	2.10
25 yr PWLB	2.20	2.20	2.30	2.30	2.40	2.40	2.40	2.50	2.50	2.60
50 yr PWLB	2.00	2.00	2.10	2.20	2.20	2.20	2.20	2.30	2.30	2.40

PWLB is the Public Works Loans Board

Bank Rate is not expected to go up fast after the initial rate rise as the supply potential of the economy has not generally taken a major hit during the pandemic, so should be able to cope well with meeting demand without causing inflation to remain elevated in the medium-term, or to inhibit inflation from falling back towards the Bank of England's Monetary Policy Committee's (MPC's) 2% target after a surge to around 4% towards the end of 2021. Three increases in Bank rate are forecast in the period to March 2024, ending at 0.75%. However, these forecasts may well need changing within a relatively short time frame for the following reasons: -

- There are increasing grounds for viewing the economic recovery as running out of steam during the summer and now into the autumn. This could lead to a stagnant economy with inflation, known as stagflation, which would create a dilemma for the MPC as to which way to face.
- Current key supply shortages e.g., petrol and diesel, could spill over into causing economic activity in some sectors to take a significant hit.
- Rising gas and electricity prices in October and next April and increases in other prices caused by supply shortages and increases in taxation next April, are already going to deflate consumer spending power without the MPC having to take any action on Bank Rate to cool inflation.
- On the other hand, consumers are sitting on around £200bn of excess savings left over from the pandemic and it is uncertain when will they spend this sum.
- 1.6 million people came off furlough at the end of September, and be available to fill labour shortages in many sectors of the economy. So, supply shortages which have been driving up both wages and costs, could reduce significantly within the next six months or so and alleviate the MPC's current concerns.
- There could be further negative developments with Covid, on top of the flu season this winter, which could depress economic activity.

In summary, with the high level of uncertainty prevailing on several different fronts, these forecasts may need to be revised again in line with developments.

It also needs to be borne in mind that Bank Rate being cut to 0.10% was an emergency measure to deal with the Covid crisis hitting the UK in March 2020. At any time, the MPC could decide to simply take away that final emergency cut from 0.25% to 0.10% on the grounds of it no longer being warranted and as a step forward in the return to normalisation. In addition, any Bank Rate under 1% is both highly unusual and highly supportive of economic growth.

A4. BORROWING ACTIVITY

No borrowing was undertaken during the first half of 2020/21.

The Council's gross borrowing at 30th September 2021 of £768m is within the Council's Authorised Limit (the maximum amount of borrowing approved by City Council) of £963m and also within the Council's Operational Boundary (the limit beyond which borrowing is not expected to exceed) of £945m.

The Council plans for gross borrowing to have a reasonably even maturity profile. This is to ensure that the Council does not need to replace large amounts of maturing borrowing when interest rates could be unfavourable.

The actual maturity profile of the Council's borrowing is within the limits contained within the Council's Treasury Management Policy (see paragraph A1).

Early Redemption of Borrowing

Debt rescheduling opportunities have been limited in the current economic climate and following the various increases in the margins added to gilt yields which has impacted PWLB new borrowing rates since October 2010. During the quarter ended 30th September 2021 no debt rescheduling was undertaken.

With the exception of two loans all the Council's borrowings to finance capital expenditure are fixed rate and fixed term loans. This reduces interest rate risk and provides a high degree of budget certainty.

The Council's borrowing portfolio is kept under review to identify if and when it would be financially beneficial to repay any specific loans early. Repaying borrowing early invariably results in a premium (early repayment charges) by the PWLB that are sufficiently large to make early repayment of borrowing financially unattractive to the Council.

No debt rescheduling or early repayment of debt has been undertaken during the first half of 2021/22 as it has not been financially advantageous for the Council to do so.

A4. INVESTMENT ACTIVITY

The Council's investments averaged £409m during the first half of 2021/22 and made an average annualised return of 0.29%.

As shown by the interest rate forecasts in section A2, it is now impossible to earn the level of interest rates commonly seen in previous decades as all short-term money market investment rates have only risen weakly since Bank Rate was cut to 0.10% in March 2020. Given this environment and the fact that Bank Rate may only rise marginally, or not at all, before the second half of 2023, investment returns are expected to remain low.

Significant levels of downgrades to short and long term credit ratings have not materialised since the crisis in March 2020. In the main, where they did change, any alterations were limited to outlooks. However, as economies are beginning to reopen, there have been some instances of previous lowering of outlooks being reversed.

Although CDS prices (these are market indicators of credit risk) for banks (including those from the UK) spiked at the outset of the pandemic in 2020, they have subsequently returned to near pre-pandemic levels.

A5. COMBINED BORROWING AND INVESTMENT POSITION (NET DEBT)

The Councils net debt position at 30th September 2021 is summarised in the table below.

	Principal	**Average Interest Rate**	**Interest to 30th September 2021**
Borrowing (including finance leases & private finance initiative (PFI) schemes)	£768m	3.28%	£12.6m
Investments	(426m)	(0.29%)	(£0.6m)
Net Debt	£342m		£12.0m

*Although the Council's investments were £426m at 30th September 2021, the average sum invested over this period was £409m.