

# **Annual Treasury Management Review 2023/24**

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Melton Borough Council  
July 2024

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# Annual Treasury Management Review 2023/24

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## 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 2023/24. 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 2023/24 the minimum reporting requirements were that the Full Council should receive the following reports:

- an annual treasury strategy in advance of the year (Council 23/02/2023)
- a mid-year, (minimum), treasury update report (Council 14/12/2023)
- an annual review following the end of the year describing the activity compared to the strategy, (this report)

In addition, the Council is also required to report quarterly on treasury management activities which were received by the Cabinet (in their delegated scrutiny role) on the following dates 13/09/2023 and 06/03/2024.

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 Cabinet before they were reported to the Full Council. Member training on treasury management issues was undertaken during the year in November 2023 in order to support members' scrutiny role.

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## Executive Summary

During 2023/24, 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	31.3.23 Actual £000	2023/24 Latest Budget £000	31.3.24 Actual £000
Capital expenditure			
• Non-HRA	866	15,576	1,667
• HRA ( <i>if applicable</i> )	3,448	5,763	3,647
• Total	4,314	21,339	5,314
Capital Financing Requirement:			
• Non-HRA	54	43	43
• HRA ( <i>if applicable</i> )	31,484	31,484	31,484
• Total	31,538	31,527	31,527
Gross borrowing	31,413	31,413	31,413
External debt	54	43	43
Investments			
• Longer than 1 year	2,000	2,000	2,000
• Under 1 year	17,620	21,500	16,980
• Total	19,620	23,500	18,980
Net borrowing	11,793	7,913	12,433

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

## 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.

£'000 General Fund	31.3.23 Actual	2023/24 Budget	31.3.24 Actual
<b>Capital expenditure</b>	<b>866</b>	<b>15,576</b>	<b>1,667</b>
Financed in year	866	15,513	1,667
<b>Unfinanced capital expenditure</b>	<b>0</b>	<b>0</b>	<b>0</b>

£'000 HRA ( <i>where relevant</i> )	31.3.23 Actual	2023/24 Budget	31.3.24 Actual
<b>Capital expenditure</b>	<b>3,448</b>	<b>5,763</b>	<b>3,647</b>
Financed in year	3,448	5,763	3,647
<b>Unfinanced capital expenditure</b>	<b>0</b>	<b>0</b>	<b>0</b>

## 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 2023/24 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 service 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 (non HRA) 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 non-Housing Revenue Account (HRA) borrowing need, (there is no statutory requirement to reduce the HRA CFR). 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 total CFR can also be reduced by:

- the application of additional capital financing resources, (such as unapplied capital receipts); or
- charging more than the statutory revenue charge (MRP) each year through a Voluntary Revenue Provision (VRP).

The Council's 2023/24 MRP Policy, (as required by DLUHC Guidance), was approved as part of the Treasury Management Strategy Report for 2023/24 on 23/02/2023.

The Council's CFR for the year is shown below, and represents a key prudential indicator.

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Housing authorities to show separate General Fund and HRA CFR tables

CFR (£'000): General Fund	31.3.23 Actual	2023/24 Budget	31.3.24 Actual
Opening balance	66	54	54
Add unfinanced capital expenditure (as above)	0	0	0
Less MRP/VRP*	-12	-11	-11
Less PFI & finance lease repayments	0	0	0
Closing balance	54	43	43

CFR (£'000): HRA	31.3.23 Actual	2023/24 Budget	31.3.24 Actual
Opening balance	31,484	31,484	31,484
Add unfinanced capital expenditure (as above)	0	0	0
Less VRP*	0	0	0
Less PFI & finance lease repayments	0	0	0
Closing balance	31,484	31,484	31,484

\* Includes voluntary application of capital receipts

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 (2023/24) plus the estimates of any additional capital financing requirement for the current (2024/25) and next two financial years. This essentially means that the Council is not borrowing to support revenue expenditure. This indicator allowed the Council some flexibility to borrow in advance of its immediate capital needs in 2023/24. The table below highlights the Council's gross borrowing position against the CFR. The Council has complied with this prudential indicator.

	31.3.23 Actual £'000	2023/24 Budget £'000	31.3.24 Actual £'000
Gross borrowing position (including finance lease)	31,467	31,456	31,456
CFR	31,538	31,527	31,527
Under / over funding of CFR	(71)	(71)	(71)

**The authorised limit** - the authorised limit is the “affordable borrowing limit” required by s3 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 2023/24 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.

	2023/24 £'000
Authorised limit	46,000
Maximum gross borrowing position during the year	31,456
Operational boundary	34,000
Average gross borrowing position	31,467
Financing costs as a proportion of net revenue stream - General Fund	-19.13%
Financing costs as a proportion of net revenue stream - HRA	26.50%



### 3. Treasury Position as of 31st March 2024

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 2023/24 the Council's treasury position, (excluding borrowing by PFI and finance leases) was as follows:-

<b>DEBT PORTFOLIO</b>	<b>31.3.23 Principal £'000</b>	<b>Rate/ Return</b>	<b>Average Life yrs</b>	<b>31.3.24 Principal £'000</b>	<b>Rate/ Return</b>	<b>Average Life yrs</b>
Fixed rate funding:						
-PWLB	31,413	3.72%	26	31,413	3.72%	25
<b>CFR (excluding finance lease)</b>	<b>31,484</b>			<b>31,484</b>		
<b>Over / (under) borrowing</b>	<b>(71)</b>			<b>(71)</b>		
<b>Total investments</b>	<b>19,620</b>	<b>2.19%</b>	<b>£17.6m under 1yr £2m over 1yr</b>	<b>18,980</b>	<b>5.07%</b>	<b>£16.98m under yr, £2m over 1 yr</b>
<b>Average Net rate of return (investment return less borrowing rate)</b>		<b>2.37%</b>			<b>4.81%</b>	

The maturity structure of the debt portfolio was as follows:

	<b>31.3.23 Actual £'000</b>	<b>31.3.24 Actual £'000</b>
Under 12 months	0	98
12 months and within 24 months	98	2,000
24 months and within 5 years	4,000	2,300
5 years and within 10 years	600	300
10 years and within 20 years	5,000	5,000
20 years and within 30 years	10,340	10,340
30 years and within 40 years	11,375	11,375
40 years and within 50 years	0	0

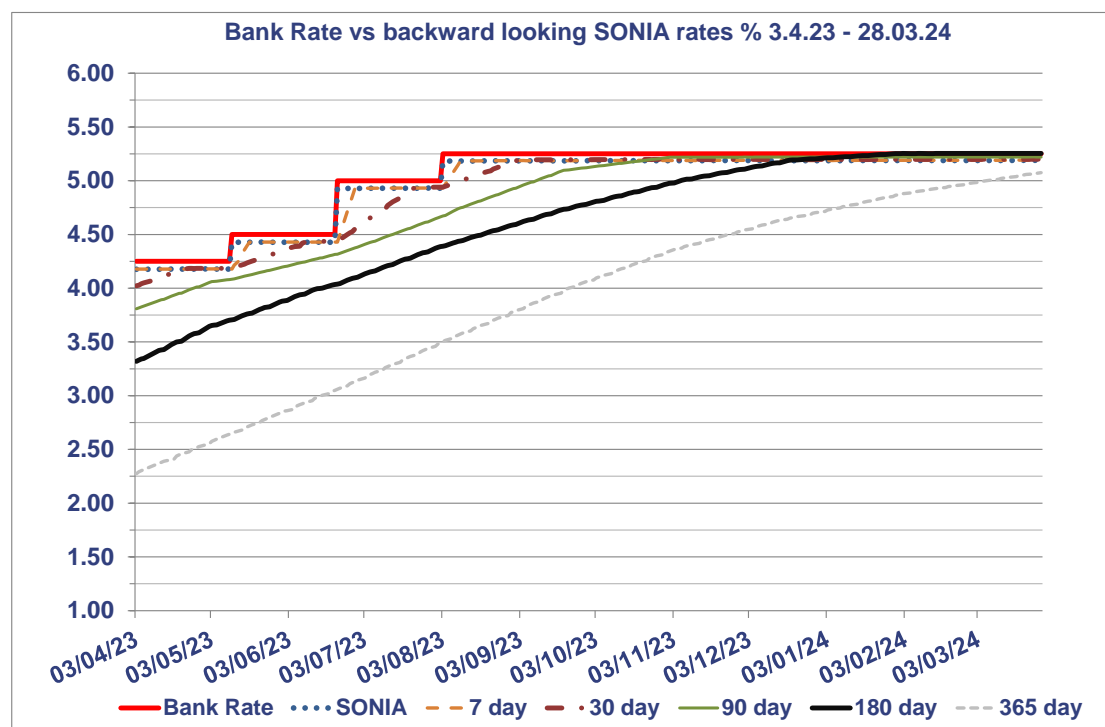
The maturity structure of the investment portfolio was as follows:

	31.3.23 Actual £000	2023/24 Budget £000	31.3.24 Actual £000
Investments			
Longer than 1 year	2,000	2,000	2,000
Up to 1 year	17,620	21,500	16,980
Total	<b>19,620</b>	<b>23,500</b>	<b>18,980</b>

## 4. The Strategy for 2023/24

### 4.1 Investment strategy and control of interest rate risk

Investment Benchmarking Data – Sterling Overnight Index Averages (Backward-looking) 2023/24



FINANCIAL YEAR TO QUARTER ENDED 28/03/2024							
	Bank Rate	SONIA	7 day	30 day	90 day	180 day	365 day
<b>High</b>	5.25	5.19	5.19	5.20	5.22	5.25	5.08
<b>High Date</b>	03/08/2023	28/03/2024	28/03/2024	26/03/2024	25/03/2024	22/03/2024	28/03/2024
<b>Low</b>	4.25	4.18	4.18	4.02	3.81	3.32	2.27
<b>Low Date</b>	03/04/2023	04/04/2023	11/04/2023	03/04/2023	03/04/2023	03/04/2023	03/04/2023
<b>Average</b>	5.03	4.96	4.96	4.93	4.84	4.64	3.93
<b>Spread</b>	1.00	1.01	1.01	1.18	1.41	1.94	2.80

The following commentary has been provided by the Council's Treasury Management advisors:

Investment returns picked up throughout the course of 2023/24 as central banks, including the Bank of England, continued to respond to inflationary pressures that were not transitory, and realised that tighter monetary policy was called for.

Starting April at 4.25%, Bank Rate moved up in stepped increases of either 0.25% or 0.5%, reaching 5.25% by August. By the end of the financial year, no further increases were anticipated. Indeed, the market is pricing in a first cut in Bank Rate in either June or August 2024.

The upward sloping yield curve that prevailed throughout 2023/24 meant that local authorities continued to be faced with the challenge of proactive investment of surplus cash, 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, UK equity market valuations struggled to make progress, as did property funds, although there have been some spirited, if temporary, market rallies from time to time – including in November and December 2023. However, the more traditional investment options, such as specified investments (simple to understand, and less than a year in duration), have continued to be at the forefront of most local authority investment strategies, particularly given Money Market Funds have also provided decent returns in close proximity to Bank Rate for liquidity purposes. In the latter part of 2023/24, the local authority to local authority market lacked any meaningful measure of depth, forcing short-term investment rates above 7% in the last week of March.

While the Council has taken a prudent approach to investing surplus monies, 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 Global Financial Crisis of 2008/09. 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.

## **4.2 Borrowing strategy and control of interest rate risk**

During 2023/24, the Council maintained an under-borrowed position. This meant that the capital borrowing need, (the Capital Financing Requirement), was not fully funded with loan debt as cash supporting the Council’s reserves, balances and cash flow was used as an interim measure. This strategy was prudent as although near-term investment rates were equal to, and sometimes higher than, long-term borrowing costs, the latter are expected to fall back through 2024 and 2025 as inflation concerns are dampened. The Council has sought to minimise the taking on of long-term borrowing at elevated levels (>4%) and has focused on a policy of internal and temporary borrowing, supplemented by short-dated borrowing (<5 years) as appropriate.

Interest rate forecasts initially suggested further gradual rises in short, medium and longer-term fixed borrowing rates during 2023/24. Bank Rate had initially been forecast to peak at 4.5% but it is now expected to have peaked at 5.25%.

By January it had become clear that inflation was moving down significantly from its 40-year double-digit highs, and the Bank of England signalled in March 2024 that the next move in Bank Rate would be down, so long as upcoming inflation and employment data underpinned that view. Currently the CPI measure of inflation stands at 3.4% but is expected to fall materially below 2% over the summer months and to stay there in 2025 and 2026. Nonetheless, there remains significant risks to that central forecast, mainly in the form of a very tight labour market putting upward pressure on wages, and continuing geo-political inflationary risks emanating from the prevailing Middle East crisis and the Russian invasion of Ukraine.

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Forecasts at the time of approval of the treasury management strategy report for 2023/24 were as follows: -

Link Group Interest Rate View		08.11.22												
		Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25
<b>BANK RATE</b>		3.50	4.25	4.50	4.50	4.50	4.00	3.75	3.50	3.25	3.00	2.75	2.50	2.50
3 month ave earnings		3.60	4.30	4.50	4.50	4.50	4.00	3.80	3.30	3.00	3.00	2.80	2.50	2.50
6 month ave earnings		4.20	4.50	4.60	4.50	4.20	4.10	3.90	3.40	3.10	3.00	2.90	2.60	2.60
12 month ave earnings		4.70	4.70	4.70	4.50	4.30	4.20	4.00	3.50	3.20	3.10	3.00	2.70	2.70
5 yr PWLB		4.30	4.30	4.20	4.10	4.00	3.90	3.80	3.60	3.50	3.40	3.30	3.20	3.10
10 yr PWLB		4.50	4.50	4.40	4.30	4.20	4.00	3.90	3.70	3.60	3.50	3.40	3.30	3.20
25 yr PWLB		4.70	4.70	4.60	4.50	4.40	4.30	4.10	4.00	3.90	3.70	3.60	3.50	3.50
50 yr PWLB		4.30	4.40	4.30	4.20	4.10	4.00	3.80	3.70	3.60	3.40	3.30	3.20	3.20

Throughout the course of the last twelve months there has been a change in interest rates. The tables below provide a schedule of the indicative rates provided by LINK throughout the year which outlines the changes.

Link Group Interest Rate View		24.05.23												
		Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26
<b>BANK RATE</b>		4.75	5.00	5.00	4.75	4.50	4.00	3.50	3.25	2.75	2.50	2.50	2.50	2.50
3 month ave earnings		4.80	5.00	5.00	4.80	4.50	4.00	3.50	3.30	2.80	2.50	2.50	2.50	2.50
6 month ave earnings		5.10	5.20	5.10	4.90	4.50	3.90	3.40	3.20	2.90	2.60	2.60	2.60	2.60
12 month ave earnings		5.40	5.40	5.30	5.00	4.50	3.90	3.40	3.20	2.90	2.70	2.70	2.70	2.70
5 yr PWLB		5.00	5.00	5.00	4.80	4.50	4.10	3.70	3.50	3.30	3.20	3.20	3.10	3.10
10 yr PWLB		5.00	5.00	5.00	4.80	4.40	4.10	3.80	3.60	3.50	3.40	3.30	3.30	3.30
25 yr PWLB		5.30	5.30	5.20	5.10	4.80	4.50	4.20	4.00	3.80	3.70	3.60	3.60	3.60
50 yr PWLB		5.10	5.10	5.00	4.90	4.60	4.30	4.00	3.80	3.60	3.50	3.40	3.40	3.40

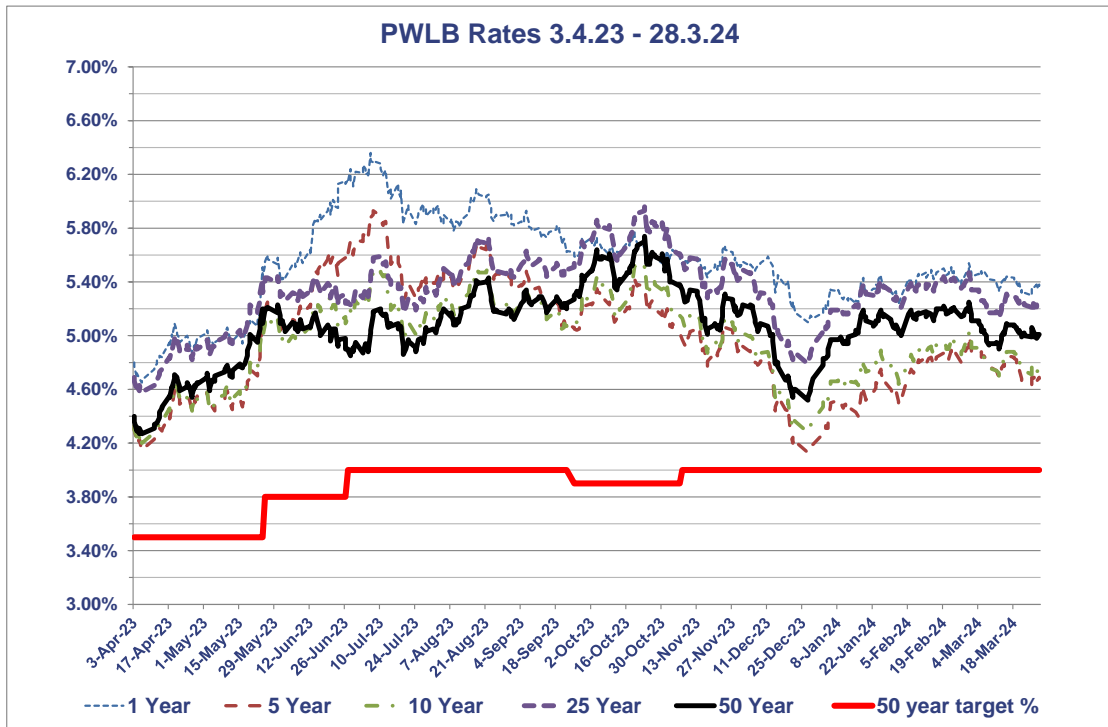
Link Group Interest Rate View		26.06.23												
		Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26
<b>BANK RATE</b>		5.00	5.50	5.50	5.50	5.25	4.75	4.25	3.75	3.25	2.75	2.75	2.50	2.50
3 month ave earnings		5.30	5.60	5.50	5.30	5.00	4.50	4.00	3.50	3.00	2.70	2.60	2.50	2.50
6 month ave earnings		5.80	5.90	5.70	5.50	5.10	4.60	4.00	3.50	3.00	2.70	2.60	2.60	2.60
12 month ave earnings		6.30	6.20	6.00	5.70	5.30	4.80	4.10	3.60	3.10	2.80	2.70	2.70	2.70
5 yr PWLB		5.50	5.60	5.30	5.10	4.80	4.50	4.20	3.90	3.60	3.40	3.30	3.30	3.20
10 yr PWLB		5.10	5.20	5.00	4.90	4.70	4.40	4.20	3.90	3.70	3.50	3.50	3.50	3.40
25 yr PWLB		5.30	5.40	5.20	5.10	4.90	4.70	4.50	4.20	4.00	3.90	3.80	3.80	3.70
50 yr PWLB		5.00	5.10	5.00	4.90	4.70	4.50	4.30	4.00	3.80	3.60	3.60	3.50	3.50

Link Group Interest Rate View		25.09.23												
		Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26
<b>BANK RATE</b>		5.25	5.25	5.25	5.00	4.50	4.00	3.50	3.00	2.75	2.75	2.75	2.75	2.75
3 month ave earnings		5.30	5.30	5.30	5.00	4.50	4.00	3.50	3.00	2.80	2.80	2.80	2.80	2.80
6 month ave earnings		5.60	5.50	5.40	5.10	4.60	4.10	3.60	3.10	2.90	2.90	2.90	2.90	2.90
12 month ave earnings		5.80	5.70	5.50	5.20	4.70	4.20	3.70	3.20	3.00	3.00	3.00	3.00	3.00
5 yr PWLB		5.10	5.00	4.90	4.70	4.40	4.20	4.00	3.90	3.70	3.70	3.60	3.60	3.50
10 yr PWLB		5.00	4.90	4.80	4.60	4.40	4.20	4.00	3.80	3.70	3.60	3.60	3.50	3.50
25 yr PWLB		5.40	5.20	5.10	4.90	4.70	4.40	4.30	4.10	4.00	3.90	3.80	3.80	3.80
50 yr PWLB		5.20	5.00	4.90	4.70	4.50	4.20	4.10	3.90	3.80	3.70	3.60	3.60	3.60

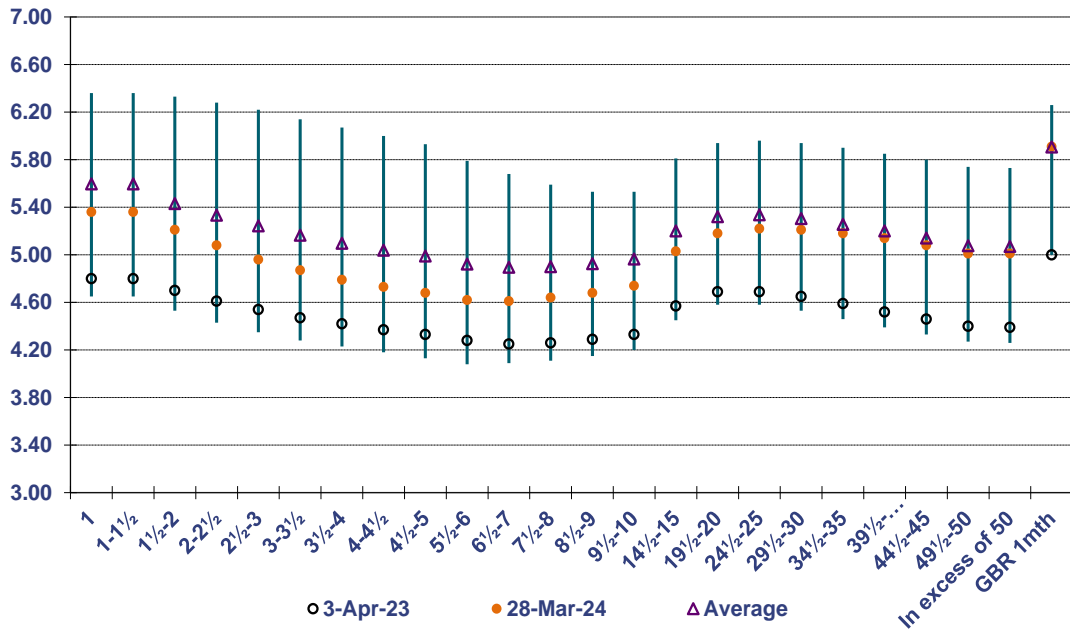
Link Group Interest Rate View		06.11.23												
		Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26
<b>BANK RATE</b>		5.25	5.25	5.25	5.00	4.50	4.00	3.50	3.25	3.00	3.00	3.00	3.00	3.00
3 month ave earnings		5.30	5.30	5.30	5.00	4.50	4.00	3.50	3.30	3.00	3.00	3.00	3.00	3.00
6 month ave earnings		5.60	5.50	5.40	5.10	4.60	4.10	3.60	3.40	3.10	3.10	3.10	3.10	3.10
12 month ave earnings		5.80	5.70	5.50	5.20	4.70	4.20	3.70	3.50	3.30	3.30	3.30	3.30	3.30
5 yr PWLB		5.00	4.90	4.80	4.70	4.40	4.20	4.00	3.80	3.70	3.60	3.50	3.50	3.50
10 yr PWLB		5.10	5.00	4.80	4.70	4.40	4.20	4.00	3.80	3.70	3.70	3.60	3.60	3.50
25 yr PWLB		5.50	5.30	5.10	4.90	4.70	4.50	4.30	4.20	4.10	4.10	4.00	4.00	4.00
50 yr PWLB		5.30	5.10	4.90	4.70	4.50	4.30	4.10	4.00	3.90	3.90	3.80	3.80	3.80

Link Group Interest Rate View		08.01.24												
		Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27
<b>BANK RATE</b>		5.25	5.25	4.75	4.25	3.75	3.25	3.00	3.00	3.00	3.00	3.00	3.00	3.00
3 month ave earnings		5.30	5.30	4.80	4.30	3.80	3.30	3.00	3.00	3.00	3.00	3.00	3.00	3.00
6 month ave earnings		5.20	5.10	4.60	4.10	3.70	3.30	3.10	3.10	3.10	3.10	3.10	3.10	3.10
12 month ave earnings		5.00	4.90	4.40	3.90	3.60	3.20	3.10	3.10	3.10	3.10	3.10	3.20	3.20
5 yr PWLB		4.50	4.40	4.30	4.20	4.10	4.00	3.80	3.70	3.60	3.60	3.50	3.50	3.50
10 yr PWLB		4.70	4.50	4.40	4.30	4.20	4.10	4.00	3.90	3.80	3.70	3.70	3.70	3.70
25 yr PWLB		5.20	5.10	4.90	4.80	4.60	4.40	4.30	4.20	4.20	4.10	4.10	4.10	4.10
50 yr PWLB		5.00	4.90	4.70	4.60	4.40	4.20	4.10	4.00	4.00	3.90	3.90	3.90	3.90

**PWLB RATES 2023/24**



**PWLB Certainty Rate Variations 3.4.23 to 28.3.24**



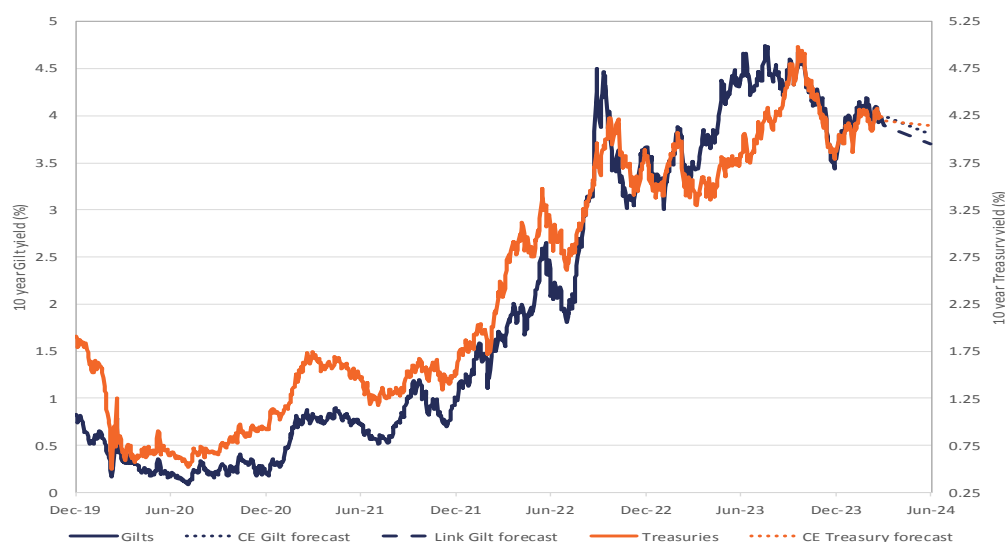
**HIGH/LOW/AVERAGE PWLB RATES FOR 2023/24**

	1 Year	5 Year	10 Year	25 Year	50 Year
<b>Low</b>	4.65%	4.13%	4.20%	4.58%	4.27%
<b>Date</b>	06/04/2023	27/12/2023	06/04/2023	06/04/2023	05/04/2023
<b>High</b>	6.36%	5.93%	5.53%	5.96%	5.74%
<b>Date</b>	06/07/2023	07/07/2023	23/10/2023	23/10/2023	23/10/2023
<b>Average</b>	5.54%	4.99%	4.97%	5.34%	5.08%
<b>Spread</b>	1.71%	1.80%	1.33%	1.38%	1.47%

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 levels of persistent inflation that are exacerbated by very tight labour markets and high wage increases relative to what central banks believe to be sustainable.

### Graph of 10-year UK gilt yields v. US treasury yields (inclusive of Link's and Capital Economics' forecasts)



Gilt yields have generally been on a continual rise since the start of 2021, peaking in the autumn of 2023. Currently, yields are broadly range bound between 3.5% and 4.25%.

At the close of the day on 28 March 2024, all gilt yields from 1 to 50 years were between 3.81% and 4.56%, with the 1 year being the highest and 6-7 years being the lowest yield.

Regarding PWLB borrowing rates, the various margins attributed to their pricing are as follows: -

- **PWLB Standard Rate** is gilt plus 100 basis points (G+100bps)
- **PWLB Certainty Rate** is gilt plus 80 basis points (G+80bps)
- **Local Infrastructure Rate** is gilt plus 60bps (G+60bps)
- **HRA Borrowing rate** is gilt plus 40 40bps (G+40bps)

There is likely to be a fall in gilt yields and PWLB rates across the whole curve over the next one to two years as Bank Rate falls and inflation (on the Consumer Price Index measure) moves below the Bank of England's 2% target.

As a general rule, short-dated gilt yields will reflect expected movements in Bank Rate, whilst medium to long-dated yields are driven primarily by the inflation outlook.

The Bank of England is also embarking on a process of Quantitative Tightening. The Bank's original £895bn stock of gilt and corporate bonds will gradually be sold back into the market over several years. The impact this policy will have on the market pricing of gilts, while issuance is markedly increasing, and high in historic terms, is an unknown at the time of writing.

## 5. Borrowing Outturn

There were no borrowing requirements during 2023/24.

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.

No rescheduling was done during the year as the approximate 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

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## 6. 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 23/02/2023. This policy sets out the approach for choosing investment counterparties and is based on credit ratings provided by the three main credit rating agencies, supplemented by additional market data, (such as rating outlooks, credit default swaps, bank share prices etc.).

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

**Resources** – the Council’s cash balances comprise revenue and capital resources and cash flow monies. The Council’s core cash resources comprised as follows:

Balance Sheet Resources (£m)	31.3.23	31.3.24
Balances	1,651	2,050
Earmarked reserves	13,942	12,850
Provisions	317	235
Usable capital receipts	4,279	3,724
<b>Total</b>	<b>20,189</b>	<b>18,859</b>

### Investments held by the Council

- The Council maintained an average balance of £25.4m of internally managed funds.
- The internally managed funds earned an average rate of return of 5.065%.
- The comparable performance indicator is the average 7-day SONIA rate, which was 5.0077%.
- This compares with a budget assumption of £23.5m investment balances earning an average rate of 2.51%.
- Total investment income was £1.264m compared to a budget of £590k

## 7. The Economy and Interest Rates

The following commentary has been provided by the Council’s Treasury Management advisors:

### UK Economy

Against a backdrop of stubborn inflationary pressures, the Russian invasion of Ukraine, and war in the Middle East, UK interest rates have continued to be volatile right across the curve, from Bank Rate through to 50-year gilt yields, for all of 2023/24.

Markets have sought an end to central banks’ on-going phase of keeping restrictive monetary policy in place on at least one occasion during 2023/24 but to date only the Swiss National Bank has cut rates and that was at the end of March 2024.

UK, EZ and US 10-year yields have all stayed stubbornly high throughout 2023/24. The table below provides a snapshot of the conundrum facing central banks: inflation is easing, albeit gradually, but labour markets remain very tight by historical comparisons, making it an issue of fine judgment as to when rates can be cut.

	<b>UK</b>	<b>Eurozone</b>	<b>US</b>
<b>Bank Rate</b>	5.25%	4%	5.25%-5.5%
<b>GDP</b>	-0.3%q/q Q4 (-0.2%y/y)	+0.0%q/q Q4 (0.1%y/y)	2.0% Q1 Annualised
<b>Inflation</b>	3.4%y/y (Feb)	2.4%y/y (Mar)	3.2%y/y (Feb)
<b>Unemployment Rate</b>	3.9% (Jan)	6.4% (Feb)	3.9% (Feb)

The Bank of England sprung no surprises in their March meeting, leaving interest rates at 5.25% for the fifth time in a row and, despite no MPC members no longer voting to raise interest rates, it retained its relatively hawkish guidance. The Bank's communications suggest the MPC is gaining confidence that inflation will fall sustainably back to the 2.0% target. However, although the MPC noted that "the restrictive stance of monetary policy is weighing on activity in the real economy, is leading to a looser labour market and is bearing down on inflationary pressures", conversely it noted that key indicators of inflation persistence remain elevated and policy will be "restrictive for sufficiently long" and "restrictive for an extended period".

Of course, the UK economy has started to perform a little better in Q1 2024 but is still recovering from a shallow recession through the second half of 2023. Indeed, Q4 2023 saw negative GDP growth of -0.3% while y/y growth was also negative at -0.2%.

But it was a strange recession. Unemployment is currently sub 4%, against a backdrop of still over 900k of job vacancies, and annual wage inflation is running at above 5%. With gas and electricity price caps falling in April 2024, the CPI measure of inflation - which peaked at 11.1% in October 2022 – is now due to slide below the 2% target rate in April and to remain below that Bank of England benchmark for the next couple of years, according to Capital Economics. The Bank of England still needs some convincing on that score, but upcoming inflation and employment releases will settle that argument shortly. It is noted that core CPI was still a heady 4.5% in February and, ideally, needs to fall further.

Shoppers largely shrugged off the unusually wet weather in February, whilst rising real household incomes should support retail activity throughout 2024. Furthermore, the impact of higher interest rates on household interest payments is getting close to its peak, even though fixed rate mortgage rates on new loans have shifted up a little since falling close to 4.5% in early 2024.

From a fiscal perspective, the further cuts to national insurance tax (from April) announced in the March Budget will boost real household disposable income by 0.5 - 1.0%. After real household disposable income rose by 1.9% in 2023, Capital Economics forecast it will rise by 1.7% in 2024 and by 2.4% in 2025. These rises in real household disposable income, combined with the earlier fading of the drag from previous rises in interest rates, means GDP growth of 0.5% is envisaged in 2024 and 1.5% in 2025. The Bank of England is less optimistic than that, seeing growth struggling to get near 1% over the next two to three years.

As for equity markets, the FTSE 100 has risen to nearly 8,000 and is now only 1% below the all-time high it reached in February 2023. The modest rise in UK equities in February was driven by strong performances in the cyclical industrials and consumer discretionary sectors, whilst communications and basic materials have fared poorly.

Despite its performance, the FTSE 100 is still lagging behind the S&P 500, which has been at an all-time high for several weeks.

### **USA Economy.**

Despite the markets willing the FOMC to cut rates as soon as June 2024, the continued resilience of the economy, married to sticky inflation, is providing a significant headwind to a change in monetary policy. Markets currently anticipate three rate cuts this calendar year, but two or less would not be out of the question. Currently, policy remains flexible but primarily data driven.

In addition, the Fed will want to shrink its swollen \$16 trillion balance sheet at some point. Just because the \$ is the world's foremost reserve currency (China owns over \$1 trillion) does not mean the US can continually run a budget deficit. The mix of stubborn inflation and significant treasury issuance is keeping treasury yields high. The 10 year stands at 4.4%.

As for inflation, it is currently a little above 3%. The market is not expecting a recession, but whether rates staying high for longer is conducive to a soft landing for the economy is uncertain, hence why the consensus is for rate cuts this year and into 2025...but how many and when?

### **EZ Economy.**

Although the Euro-zone inflation rate has fallen to 2.4%, the ECB will still be mindful that it has further work to do to dampen inflation expectations. However, with growth steadfastly in the slow lane (GDP flatlined in 2023), a June rate cut from the current 4% looks probable.

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## 9. Other Issues

### **IFRS 9 fair value of investments**

Following the consultation undertaken by the Department of Levelling Up, Housing and Communities [DLUHC] on IFRS 9, the Government has extended the mandatory statutory override for local authorities to reverse out all unrealised fair value movements resulting from pooled investment funds to 31<sup>st</sup> March 2025. Local authorities are required to disclose the net impact of the unrealised fair value movements in a separate unusable reserve throughout the duration of the override in order for the Government to keep the override under review and to maintain a form of transparency.

Due to the risks around this type of investment and the potential fluctuations in valuations that could lead to a deficit that would be charged to the General Fund as a direct cost, the Council has established a reserve in order to help offset any potential deficits that might arise in future should the statutory override be removed.

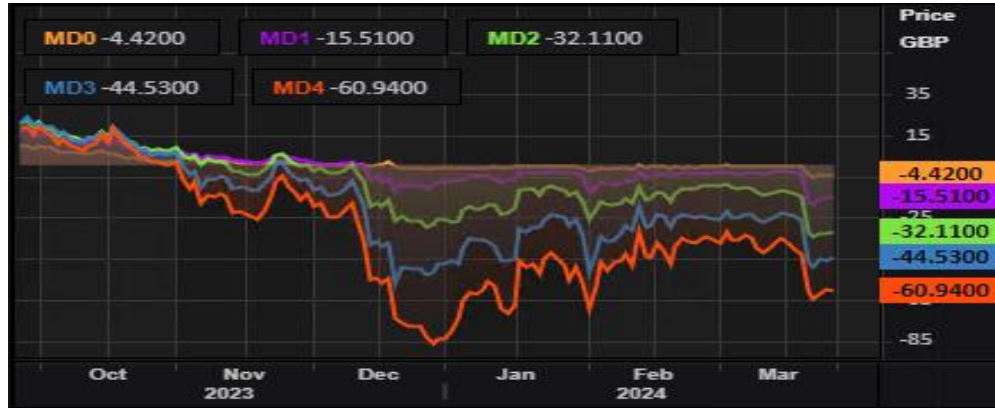
### **IFRS 16**

The implementation of IFRS16 has been delayed until 2024/25. When introduced it will bring currently off-balance sheet leased assets onto the balance sheet. Work is currently being undertaken to assess the impact of these changes. The Operational Boundary and Authorised Limit may, therefore, need to be amended mid-year once the detailed impact is known for each authority.

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# Appendix 1: Graphs

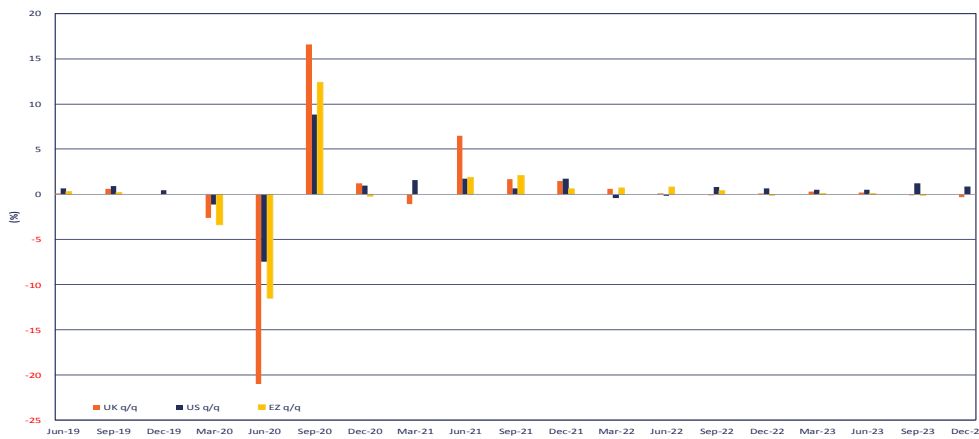
## Market Expectations for Future Increases in Bank Rate (3rd April 2024)



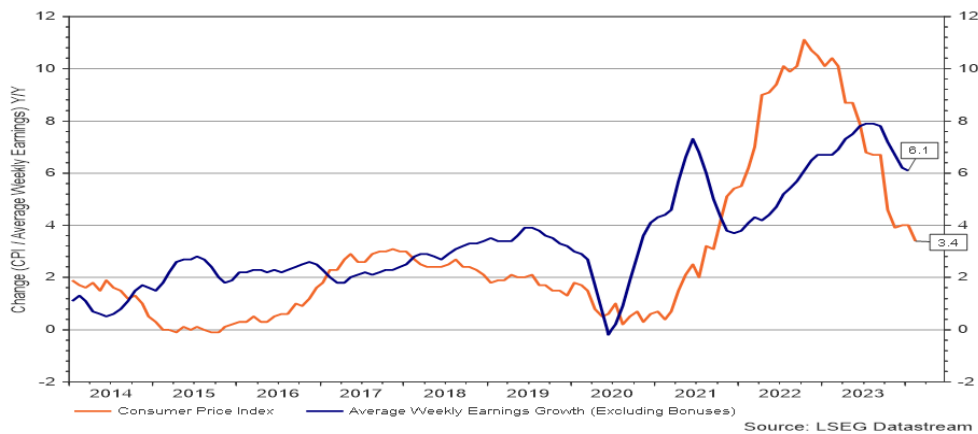
Source: Reuters Eikon

\*MD0 = Change in Bank Rate expected at MPC meeting to be held May 2024, MD1 = Jun-24, MD2 = Aug-24, MD3 = Sep-24, MD4 = Nov-24

## UK, US and EZ Quarterly GDP



## CPI v Average Weekly Earnings Growth



Source: LSEG Datastream

## Appendix 2: Investment Portfolio

Investments held as of 31st March 2024 compared to our counterparty list:

### Melton Borough Council

#### Current Investment List

Borrower	Principal (£)	Interest Rate	Start Date	Maturity Date	Lowest LT / Fund Rating	Historic Risk of Default	Expected Credit Loss (£)
MMF Invesco	980,000	5.26%		MMF	AAAm		
Lloyds Bank Plc (RFB)	2,000,000	5.14%	03/04/2023	02/04/2024	A+	0.000%	5
Qatar National Bank	1,000,000	5.27%	03/04/2023	02/04/2024	A+	0.000%	2
National Bank of Kuwait (International) PLC	1,000,000	5.12%	12/04/2023	11/04/2024	A	0.001%	13
Qatar National Bank	3,000,000	5.92%	31/05/2023	30/05/2024	A+	0.007%	218
Qatar National Bank	1,000,000	6.57%	27/06/2023	26/06/2024	A+	0.011%	105
Standard Chartered Bank (ESG)	1,000,000	6.21%	01/08/2023	31/07/2024	A+	0.015%	148
Standard Chartered Bank (ESG)	1,000,000	6.15%	04/09/2023	03/09/2024	A+	0.019%	189
Standard Chartered Bank (ESG)	1,000,000	5.84%	03/10/2023	02/10/2024	A+	0.022%	224
First Abu Dhabi Bank PJSC	1,000,000	5.78%	01/11/2023	31/10/2024	AA-	0.014%	136
National Bank of Kuwait (International) PLC	2,000,000	5.32%	17/01/2024	16/01/2025	A	0.035%	705
National Bank of Kuwait (International) PLC	1,000,000	5.32%	01/02/2024	31/01/2025	A	0.037%	371
National Bank of Kuwait (International) PLC	1,000,000	5.43%	12/03/2024	12/03/2025	A	0.042%	419
<b>Borrower - Funds</b>	<b>Principal (£)</b>	<b>Interest Rate</b>	<b>Start Date</b>	<b>Maturity Date</b>			
CCLA Property Fund	2,000,000	-0.50%					
<b>Total Investments</b>	<b>£18,980,000</b>	<b>4.98%</b>					
<b>Total Investments - excluding Funds</b>	<b>£16,980,000</b>	<b>5.63%</b>				<b>0.016%</b>	<b>£2,536</b>
<b>Total Investments - Funds Only</b>	<b>£2,000,000</b>	<b>-0.50%</b>					