LONDON BOROUGH OF CROYDON

REPORT:	**AUDIT AND GOVERNANCE COMMITTEE**
DATE OF MEETING	**30 November 2023**
REPORT TITLE:	**Treasury Management Strategy Statement and Annual Investment Strategy Mid-Year Review 2023/24**
CORPORATE DIRECTOR / DIRECTOR:	**Jane West, Corporate Director of Resources and S151 Officer**
LEAD OFFICER:	**Matthew Hallett, Acting Head of Treasury and Pensions**
LEAD MEMBER:	**Councillor Jason Cummings, Cabinet Member for Finance**
DECISION TAKER:	**Not applicable to this report**
AUTHORITY TO TAKE DECISION:	**Not applicable to this report**
KEY DECISION?	**No**
CONTAINS EXEMPT INFORMATION?	**No** / **Public**
WARDS AFFECTED:	**All**

1. SUMMARY OF REPORT

1.1 This Report reviews the Council's treasury management activities for the first six months of financial year 2023/24. It is prepared in accordance with the requirements of the Chartered Institute of Public Finance and Accountancy (CIPFA) codes of practice in respect of capital finance and treasury management. The codes recommend that members are advised of treasury management activities of the first six months of each financial year and of compliance with various strategies and policies agreed by the Council. The report:

- Reviews compliance with the Treasury Management Strategy Statement (TMSS) and Annual Investment Strategy as agreed by full Council (Budget Council) on 8 March 2023 (Minute 37/21 applies);
- Reviews treasury borrowing and investment activity for the period 1 April 2023 to 30 September 2023; and
- Demonstrates compliance with agreed Treasury and Prudential Indicators and the CIPFA Prudential Code for Capital Finance.

2. RECOMMENDATION

2.1 The Audit and Governance Committee is recommended to note the contents of the mid-year report on the treasury management activity for 2023/24.

3 DETAIL

3.1 Capital Strategy

3.1.1 In December 2021, CIPFA issued revised versions of "The Prudential Code for Capital Finance in Local Authorities." ("Prudential Code") and "Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes" ("the Code"). These require all local authorities to prepare a Capital Strategy which is to provide the following:

- a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services;
- an overview of how the associated risk is managed; and
- the implications for future financial sustainability.

3.2 Treasury management

3.2.1 With Government support the Council operates a balanced budget, which broadly means that cash raised during the year will meet its cash expenditure. Part of the treasury management operation ensures that this cash flow is adequately planned, with surplus monies being invested with low-risk counterparties, providing adequate liquidity before considering optimising investment return.

3.2.2 The second main function of the treasury management service is the funding of the Council's capital plans. These plans provide a guide to the borrowing need of the Council, essentially the longer-term cash flow planning to ensure the Council can meet its capital spending operations. This management of longer-term cash may involve arranging long- or short- term loans or using longer term cash flow surpluses. On occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

3.2.3 Accordingly, treasury management is defined as:

> "The management of the local authority's borrowing, investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

3.3 Treasury Management in the Public Services: Code of Practice and Cross Sectoral Guidance Notes

3.3.1 This report has been written in accordance with the Code the primary requirements of which are as follows:

- The creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities;

- The creation and maintenance of Treasury Management Practices which set out the way in which the Council will seek to achieve those policies and objectives;

- To provide Council with an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead, a mid-year Review Report and an Annual Report (stewardship report) covering activities during the previous year;

- The delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions; and

- The delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body. For this Council the designated body is the Audit and Governance Committee.

3.3.2 This mid-year report has been prepared in compliance with the codes and covers the following:

- An economic update for the first half of the 2023/24 financial year (Section 3.4);
- A medium-term interest rates forecast (Section 3.5)
- The Council's capital expenditure, as set out in the Capital Strategy, and prudential indicators (Section 3.7);
- A review of the Council's borrowing strategy and debt re-scheduling (Section 3.8);
- A review of the Council's investment strategy (Section 3.9);
- A review of compliance with Treasury and Prudential Limits (Section 3.10)

3.4 Economic update

3.4.1 A commentary provided by the Council's independent treasury advisers Link Group (Link) in the first week of October 2023 is included as Appendix A.

3.5 Interest rate forecasts

3.5.1 Part of the service provided by Link is to assist the Council to formulate a view on interest rates. Their PWLB rate forecasts in Table 1 below are based on the Certainty Rate (the standard rate minus 20 bps) which has been accessible to most authorities since 1 November 2012.

3.5.2 Their latest forecast sets out a view that short, medium and long-dated interest rates will be elevated for some while, as the Bank of England seeks to squeeze inflation out of the economy.

Table 1 Interest rates forecast

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
BANK RATE	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

3.6 Treasury Management Strategy Statement and Annual Investment Strategy Update

3.6.1 The TMSS and Annual Investment Strategy for 2023/24 were approved by full Council on 8 March 2023 (Minute 37/21 applies). No policy changes are recommended.

3.7 Capital Expenditure and Prudential Indicators

3.7.1 The paragraphs in this section cover:

- The Council’s capital expenditure plans;
- How these plans are being financed;
- The impact of the changes in the capital expenditure plans on the prudential indicators and the underlying need to borrow; and
- Compliance with the limits in place for borrowing activity.

3.7.2 Table 2 below shows the original capital budget as agreed by full Council on 8 March 2023 (Minute 37/21 applies), the revised budget agreed by Cabinet on 25 October 2023, the actual spend at 30 September 2023 and the outturn forecast at month six. Explanations of the evolution of the budget are provided in detail in the Cabinet reports.

Table 2 Capital expenditure by service

	Original Budget £m	Revised Budget £m	Actual at 30 September 2023 £m	Outturn Forecast £m
Housing	3.4	5.1	1.0	3.2
Assistant Chief Executive	7.1	8.7	0.4	5.2
Children, Young People and Education	12.0	16.7	3.8	0.3
Sustainable Communities, Regeneration and Economic Recovery	32.9	44.8	5.2	37.3
Resources	6.0	6.4	1.0	17.1
Corporate				
Capitalisation Direction	63.0	63.0	-	63.0
Total General Fund	**124.4**	**144.7**	**11.4**	**126.1**
HRA	32.6	33.2	3.1	38.9
Total	**157.0**	**177.9**	**14.5**	**165.0**

3.7.3 The table below details the funding sources of the capital programme and their evolution through the first half of the year. The borrowing element in the table increases the underlying indebtedness of the Council by way of the Capital Financing Requirement (CFR), although this will be reduced in part by revenue charges for the repayment of debt (MRP). This direct borrowing need may also be supplemented by maturing debt and other treasury requirements.

Table 3 Financing of capital expenditure

	Original Budget £m	Revised Budget £m	Outturn Forecast £m
Capital receipts	45.0	45.0	84.5
Capital grants and other	24.1	27.2	17.8
Capital reserves	6.1	15.8	15.3
Section 106	1.6	1.2	0.3
Community Infrastructure Levy	1.8	9.7	8.1
HRA Right to Buy Receipts	2.1	2.1	2.1
HRA Reserves	1.1	1.1	6.8
HRA Revenue	13.9	13.9	13.9
HRA Major Repairs Allowance	15.5	16.1	16.1
Total financing	**111.2**	**132.1**	**165.0**
Underlying need to borrow	**45.8**	**45.8**	**-**
Less Minimum Revenue Provision	**-28.3**	**-28.3**	**-28.3**
Borrowing Requirement	**17.5**	**17.5**	**-28.3**

3.7.4 The key controls over treasury management activity to ensure that, over the medium term, borrowing will only be for capital purposes are the prudential indicators. Gross external borrowing should not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional CFR for the current year and the next two financial years. This allows some flexibility for limited early borrowing for future years. Full Council has approved a policy for borrowing in advance of need. The table below shows changes in the CFR and borrowing requirements reflecting the actual outturn for 2022-23 and arising from the changes in the capital programme described above.

Table 4 Borrowing and CFR

	Original Budget £m	Outturn Projection £m
Borrowing	1,437.4	1,239.6
Other long term liabilities	66.0	65.7
Total debt	**1,503.4**	**1,305.3**
CFR (year end position) - GF	1,415.6	1,385.1
CFR (year end position) - HRA	373.5	363.5
CFR (year end position) - Total	**1,789.1**	**1,748.6**

3.7.5 The Prudential Indicators relevant to the capital programme and its borrowing implications are the Operational Boundary (the expected debt position) and the Authorised Limit (the limit beyond which borrowing is prohibited).

Table 5 Operational Boundary and Authorised Limit

	Agreed as per TMSS £m	Outturn Projection £m
Operational Boundary	1,503.4	1,305.3
Authorised Limit	1,553.4	1,355.3

3.7.6 The Authorised Limit includes a buffer of £50m to cover unexpected cashflow shortages.

3.8 Borrowing Strategy

3.8.1 During 2023/24 the Council has been operating in accordance with the borrowing limits approved by full Council on 8 March 2023. As discussed above, the current limits for the year are:

- Operational Boundary - £1,503.4m
- Authorised Limit - £1,553.4m

3.8.2 The level of the Council's borrowing, which is measured against the limits, was £1,345.5m on 1 April 2023 reduced to £1,305.3m on 30 September 2023. Details are provided in Table 6 below.

Table 6 Borrowing

	1 April 2023 £m	30 September 2023 £m
Temporary – other local authorities	273.0	125.0
Long term – PWLB	860.9	974.6
Long term – UK banks	20.0	20.0
Long term – LEEF	8.6	5.0
Long term – other local authorities	13.0	13.0
Long term – European Investment Bank	102.0	102.0
Other Long Term Liabilities	68.0	65.7
TOTAL	**1,345.50**	**1,305.3**

3.8.3 The Council has continued to pay off as much external debt as it is able. During the year to date it has reduced its external debt by £37.9m. During the period £208.0m of temporary loans from other local authorities and £3.6m from the Mayor of London's Energy Efficiency Fund have matured (see table 7). The Council has refinanced £60m with other local authorities and £113.7m with PWLB at an average rate of 5.57%. Refinancing loans at higher interest rates has led to an increase of approximately £5.5m p.a. to the Council's cost of borrowing. The Council will look to further reduce its reliance on external debt as it continues with its asset disposal plan.

Table 7 Loans Maturing 1 April 2023 to 30 September 2023

Counterparty	**Principal £**	**Interest Rate**	**Maturity Date**
GLA - Amber Green LEEF	3,574,591	1.800	13/09/23
North Somerset District Council	6,000,000	1.370	03/04/23
North Yorkshire County Council	10,000,000	4.100	11/04/23
North Yorkshire County Council	10,000,000	4.250	13/04/23
Caerphilly County Borough Council	5,000,000	4.100	18/04/23
Wiltshire Council	10,000,000	4.250	18/04/23
Gloucestershire County Council	5,000,000	4.150	19/04/23
Mid Devon District Council	3,000,000	4.000	24/04/23
Derbyshire County Council	10,000,000	0.450	28/04/23
West Midlands CA	10,000,000	1.000	28/04/23
Somerset CC Rollover	5,000,000	1.150	02/05/23
Mansfield District Council	2,000,000	1.000	02/05/23
Guildford Borough Council	5,000,000	0.450	08/05/23
Somerset County Council Pension Fund	5,000,000	1.250	31/05/23
Somerset County Council	5,000,000	1.250	31/05/23
NEXUS	5,000,000	1.350	05/06/23
Wigan Council	5,000,000	1.750	05/06/23
Tewkesbury Borough Council	2,000,000	1.920	06/06/23
Hertsmere Borough Council	5,000,000	1.400	14/06/23
Islington London Borough Rollover	5,000,000	3.500	19/06/23
East Suffolk Council	5,000,000	1.350	28/06/23

Police & Crime Commissioner For Avon And Somerset	3,000,000	3.200	03/07/23
Somerset County Council	5,000,000	3.200	03/07/23
Horsham District Council	2,000,000	3.200	03/07/23
Guildford Borough Council	5,000,000	0.500	05/07/23
Gloucestershire County Council	5,000,000	0.500	05/07/23
Police and Crime for Avon & Somerset	5,000,000	1.250	05/07/23
Elmbridge Borough Council	5,000,000	1.850	06/07/23
Brighton & Hove City Council	5,000,000	1.850	06/07/23
Islington London Borough	10,000,000	0.500	13/07/23
NEXUS	5,000,000	0.500	14/07/23
South Derbyshire DC	5,000,000	0.500	19/07/23
East Suffolk Council	5,000,000	1.600	26/07/23
West of England Combined Authority	5,000,000	0.600	27/07/23
Somerset CC Pension Fund	5,000,000	1.650	31/07/23
Wealden D.C.	5,000,000	1.600	22/08/23
Renfrewshire Council	5,000,000	2.300	01/09/23
South Ayrshire Council	5,000,000	2.300	04/09/23
South Ayrshire Council	5,000,000	2.300	29/09/23
Total	**211,574,591.00**		

Table 8 New Loans taken out 1 April 2023 to 30 September 2023

Counterparty	Principal £	Interest Rate	Start Date	Maturity Date
Rugby Borough Council	5,000,000	4.700	06/04/23	04/04/24
West Midlands CA	10,000,000	3.850	28/04/23	26/04/24
Furness Building Society	5,000,000	4.900	10/05/23	08/05/24
Argyll & Bute	5,000,000	5.300	12/06/23	10/06/24
Mole Valley DC	2,000,000	5.300	12/06/23	10/06/24
Test Valley BC	5,000,000	6.000	05/07/23	03/07/24
Test Valley BC	5,000,000	6.000	31/08/23	29/08/24
Vale Of Glamorgan Council	3,000,000	4.650	28/04/23	31/10/23
North Yorkshire	10,000,000	4.600	11/04/23	11/10/23
North Yorkshire	10,000,000	4.600	13/04/23	13/10/23
PWLB	75,100,000	5.990	03/07/23	04/07/25
PWLB	5,000,000	6.160	19/07/23	21/07/25
PWLB	3,575,000	5.670	14/09/23	16/09/25
PWLB	5,000,000	5.400	29/09/23	01/10/25
PWLB	15,000,000	6.170	13/07/23	13/07/26
PWLB	10,000,000	5.670	01/09/23	01/09/26
Total	**173,675,000.00**			

3.8.4 The Council continues to maintain an under-borrowed position. This means that the underlying capital borrowing need (CFR), is not fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow is used as an interim measure.

3.8.5 The Council's effective interest payable on debt currently stands at 3.5%.

3.9 Investment Strategy

3.9.1 From time to time, under Section 15 (1) of the Local Government Act 2003 the Secretary of State issues statutory guidance on local government investments to which local authorities are required to "have regard." This guidance was taken into account in the investment policy parameters set within the Council's TMSS, MRP Policy Statement and Annual Investment Strategy as approved by full Council on 8 March 2023 (Minute 37/21 applies). In accordance with the Code it sets out the Council's investment priorities as being security of capital, liquidity and yield.

3.9.2 The current guidance defines investments as "Specified" and "Non-specified"

3.9.3 An investment is a specified investment if all the following apply:

- the investment and any associated payments or repayments are denominated in sterling;
- the investment has a maximum maturity of one year;
- the investment is not defined as capital expenditure; and
- the investment is made with a body or in an investment scheme described as high quality or with the UK Government, a UK local authority or a parish or community council.

3.9.4 A non-specified investment is any investment that does not meet all the conditions in paragraph 3.9.3 above.

3.9.5 It is the Council's priority when undertaking treasury activities to ensure security of capital and liquidity, and to obtain an appropriate level of return which is consistent with the Council's risk appetite. Investment instruments identified for use by the Council during 2023/24 as advised in the current Treasury Management Strategy are detailed in Appendix C. In the current economic climate, it is considered appropriate to keep investments short term to cover cash flow needs.

3.9.6 Investment activity in the first half of the year conformed to the approved strategy with an average monthly balance of £60.4m being maintained in temporary investments. As at 30 September 2023 investments were as follows:

Table 9 Investment Balances at 30 September 2023

Investment	£m
Money Market Funds	58.3
Banks as in approved credit list	-
TOTAL	**58.3**

In addition the Pension Fund had balances of £45.0m.

3.9.8 The Corporate Director of Resources confirms that the approved limits within the Annual Investment Strategy were not breached during the first six months of 2023/24.

3.10 Compliance with Treasury and Prudential Limits

3.10.1 It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. During the half year ended 30 September 2023, the Council has operated within the treasury and prudential indicators set out in the TMSS.

3.10.2 All treasury management operations have been conducted in compliance with the Council's Treasury Management Practices.

4. CONSULTATION

4.1 This report has been prepared using advice from the Council's Treasury Adviser, Link.

5. CONTRIBUTION TO COUNCIL PRIORITIES

5.1 Sound financial management: the report asks the Committee to note the contents of the mid-year report on the treasury management activity for 2023/24 as part of the proper financial administration of the Council.

This supports the Council priority of OUTCOME 1 "Balances the books, listens to residents and delivers good, sustainable services."

6. FINANCIAL CONSIDERATIONS

6.1 There are no additional financial considerations arising from this report.

Approved by: Allister Bannin on behalf of Jane West, Corporate Director of Resources (S151 Officer), 20/11/2023.

7. HUMAN RESOURCES CONSIDERATIONS

7.1 Ensuring the council maintains a balanced budget and a prudent approach to treasury management, borrowing, and debt repayment are matters of interest to the council's workforce, and workforce representatives, which will impact upon recruitment, retention and employee engagement.

Approved by: Dean Shoesmith, Chief People Officer, 15/11/2023.

8. LEGAL CONSIDERATIONS

8.1 The Head of Litigation and Corporate Law comments on behalf of the Director of Legal Services and Monitoring Officer that the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 (as amended) made pursuant to the Local Government Act 2003 require the Council to have regard to CIPFA's Prudential Code for Capital Finance in Local Authorities ("The Prudential Code"). Regulations 23 and 24 provide respectively that capital receipts may only be used for specified purposes and that in carrying out its capital finance functions, a local authority must have regard to the code of practice in "Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes" ("The Treasury Code") issued by CIPFA.

8.2 In relation to the Annual Investment Strategy, the Council is required to have regard to the Guidance issued by the Secretary of State under section 15(1)(a) of the Local Government Act 2003 entitled "Statutory guidance on Local Government Investments 3rd Edition" which is applicable from and effective for financial years commencing on or after 1 April 2018.

8.3 In addition, the Prudential Code and the Treasury Code contain investment guidance which complements the Statutory Guidance mentioned above.

8.4 Local authorities are required to have regard to the current editions of the CIPFA codes by regulations 2 and 24 of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 as amended.

8.5 Under the provisions of Section 3(1) and (8) of the Local Government Act 2003, the Council must determine and keep under review how much money it can afford to borrow, and the function of determining and keeping these levels under review is a Council, rather than an executive function.

8.6 The Council must also have regard to the Guidance issued by the Secretary of State under Section 21(1A) of the Local Government Act 2003 entitled "Statutory guidance on minimum revenue provision".

8.7 As set out earlier in the report, the Prudential Code requires authorities to prepare a capital strategy.

8.8 Under Directions dated 20 July 2023, issued by the Secretary of State under Section 15(5) of the Local Government Act 1999, the Council must, amongst other things "secure as soon as practicable that all the Authority's functions are exercised in conformity with the best value duty, thereby delivering improvements in services and outcomes for the people of Croydon".

Approved by: Sandra Herbert, Head of Litigation & Corporate Law, on behalf of the Director of Legal Services and Monitoring Officer (17/11/2023).

9. EQUALITIES CONSIDERATIONS

9.1 The Council has a statutory duty to comply with the provisions set out in the Sec 149 Equality Act 2010. The Council must therefore have due regard to:

(a) eliminate discrimination, harassment, victimisation and any other conduct that is prohibited by or under this Act;

(b) advance equality of opportunity between persons who share a relevant protected characteristic and persons who do not share it

(c) foster good relations between persons who share a relevant protected characteristic and persons who do not share it.

9.2 There are no specific equalities issues set out in this report.

Approved by: Naseer Ahmad for the Equalities Programme Manager. (15/11/2023)

10. OTHER CONSIDERATIONS

10.1 There are no Customer Focus, Environment and Design, Crime and Disorder or Human Rights considerations arising from this report.

11. FREEDOM OF INFORMATION

11.1 This report contains only information that can be publicly disclosed.

12. DATA PROTECTION IMPLICATIONS

12.1 Will the subject of the report involve the processing of ‘personal data’?

No.

Has a data protection impact assessment (DPIA) been completed?

No.

CONTACT OFFICER:

Matthew Hallett, Acting Head of Pensions and Treasury,

BACKGROUND DOCUMENTS:

None

APPENDICES:

A Economic update
B PWLB rates
C Investment instruments

APPENDIX A

Economic update (as prepared by Link in the first week of October 2023)

- The first half of 2023/24 saw:
  - Interest rates rise by a further 100bps, taking Bank Rate from 4.25% to 5.25% and, possibly, the peak in the tightening cycle.
  - Short, medium and long-dated gilts remain elevated as inflation continually surprised to the upside.
  - A 0.5% m/m decline in real GDP in July, mainly due to more strikes.
  - CPI inflation falling from 8.7% in April to 6.7% in August, its lowest rate since February 2022, but still the highest in the G7.
  - Core CPI inflation declining to 6.2% in August from 7.1% in April and May, a then 31 years high.
  - A cooling in labour market conditions, but no evidence yet that it has led to an easing in wage growth (as the 3myy growth of average earnings rose to 7.8% in August, excluding bonuses).
- The 0.5% m/m fall in GDP in July suggests that underlying growth has lost momentum since earlier in the year. Some of the weakness in July was due to there being almost twice as many working days lost to strikes in July (281,000) than in June (160,000). But with output falling in 10 out of the 17 sectors, there is an air of underlying weakness.
- The fall in the composite Purchasing Managers Index from 48.6 in August to 46.8 in September left it at its lowest level since COVID-19 lockdowns reduced activity in January 2021. At face value, it is consistent with the 0.2% q/q rise in real GDP in the period April to June, being followed by a contraction of up to 1% in the second half of 2023.
- The 0.4% m/m rebound in retail sales volumes in August is not as good as it looks as it partly reflected a pickup in sales after the unusually wet weather in July. Sales volumes in August were 0.2% below their level in May, suggesting much of the resilience in retail activity in the first half of the year has faded.
- As the growing drag from higher interest rates intensifies over the next six months, we think the economy will continue to lose momentum and soon fall into a mild recession. Strong labour demand, fast wage growth and government handouts have all supported household incomes over the past year. And with CPI inflation past its peak and expected to decline further, the economy has got through the cost-of-living crisis without recession. But even though the worst of the falls in real household disposable incomes are behind us, the phasing out of financial support packages provided by the government during the energy crisis means real incomes are unlikely to grow strongly. Higher interest rates will soon bite harder too. We expect the Bank of England to keep interest rates at the probable peak of 5.25% until the second half of 2024. Mortgage rates are likely to stay above 5.0% for around a year.

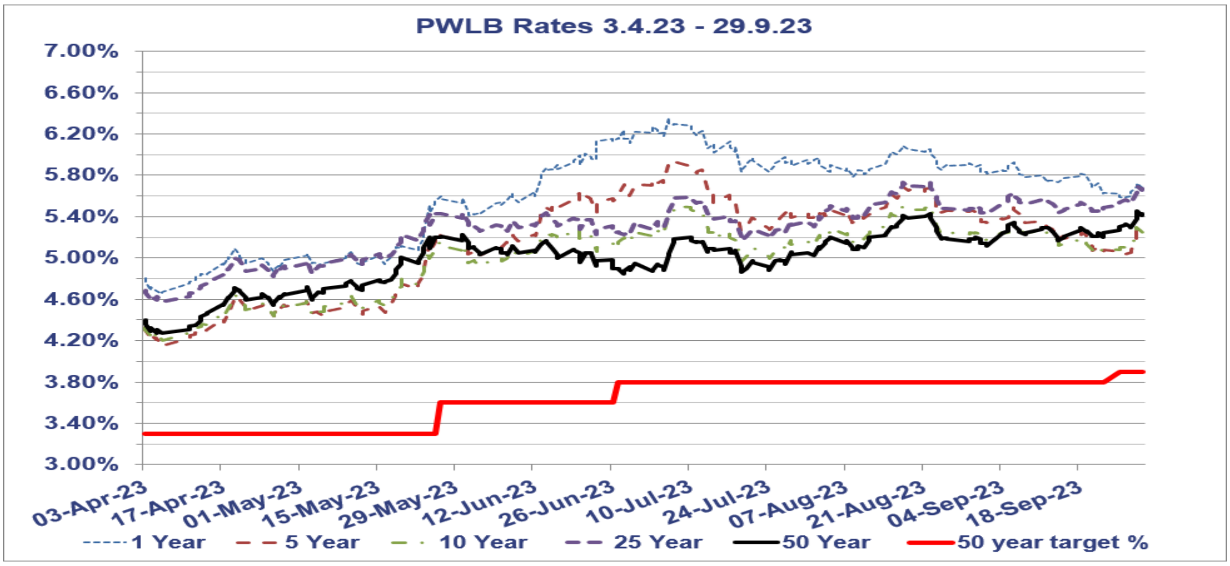
- The tightness of the labour market continued to ease, with employment in the three months to July falling by 207,000. The further decline in the number of job vacancies from 1.017m in July to 0.989m in August suggests that the labour market has loosened a bit further since July. That is the first time it has fallen below 1m since July 2021. At 3.0% in July, and likely to have fallen to 2.9% in August, the job vacancy rate is getting closer to 2.5%, which would be consistent with slower wage growth. Meanwhile, the 48,000 decline in the supply of workers in the three months to July offset some of the loosening in the tightness of the labour market. That was due to a 63,000 increase in inactivity in the three months to July as more people left the labour market due to long term sickness or to enter education. The supply of labour is still 0.3% below its pre-pandemic February 2020 level.
- But the cooling in labour market conditions still has not fed through to an easing in wage growth. While the monthly rate of earnings growth eased sharply from an upwardly revised +2.2% in June to -0.9% in July, a lot of that was due to the one-off bonus payments for NHS staff in June not being repeated in July. The headline 3myy rate rose from 8.4% (revised up from 8.2%) to 8.5%, which meant UK wage growth remains much faster than in the US and in the Euro-zone. Moreover, while the Bank of England's closely watched measure of regular private sector wage growth eased a touch in July, from 8.2% 3myy in June to 8.1% 3myy, it is still well above the Bank of England's prediction for it to fall to 6.9% in September.
- CPI inflation declined from 6.8% in July to 6.7% in August, the lowest rate since February 2022. The biggest positive surprise was the drop in core CPI inflation, which declined from 6.9% to 6.2%. That reverses all the rise since March and means the gap between the UK and elsewhere has shrunk (US core inflation is 4.4% and in the Euro-zone it is 5.3%). Core goods inflation fell from 5.9% to 5.2% and the further easing in core goods producer price inflation, from 2.2% in July to a 29-month low of 1.5% in August, suggests it will eventually fall close to zero. But the really positive development was the fall in services inflation from 7.4% to 6.8%. That also reverses most of the rise since March and takes it below the forecast of 7.2% the Bank of England published in early August.
- In its latest monetary policy meeting on 20 September, the Bank of England left interest rates unchanged at 5.25%. The weak August CPI inflation release, the recent loosening in the labour market and the downbeat activity surveys appear to have convinced the Bank of England that it has already raised rates far enough. The minutes show the decision was "finely balanced". Five MPC members (Bailey, Broadbent, Dhingra, Pill and Ramsden) voted for no change and the other four (Cunliffe, Greene, Haskel and Mann) voted for a 25bps hike.
- Like the US Fed, the Bank of England wants the markets to believe in the higher for longer narrative. The statement did not say that rates have peaked and once again said if there was evidence of more persistent inflation pressures "further tightening in policy would be required". Governor Bailey stated, "we'll be watching closely to see if further increases are needed". The Bank also retained the hawkish guidance that rates will stay "sufficiently restrictive for sufficiently long".
- This narrative makes sense as the Bank of England does not want the markets to decide that a peak in rates will be soon followed by rate cuts, which would loosen financial conditions and undermine its attempts to quash inflation. The language also gives the Bank of England the flexibility to respond to new developments. A rebound in services inflation, another surge in wage growth and/or a further leap in

oil prices could conceivably force it to raise rates at the next meeting on 2nd November, or even pause in November and raise rates in December.

- The yield on 10-year Gilts fell from a peak of 4.74% on 17th August to 4.44% on 29th September, mainly on the back of investors revising down their interest rate expectations. But even after their recent pullback, the rise in Gilt yields has exceeded the rise in most other Developed Market government yields since the start of the year. Looking forward, once inflation falls back, Gilt yields are set to reduce further. A (mild) recession over the next couple of quarters will support this outlook if it helps to loosen the labour market (higher unemployment/lower wage increases).
- The pound weakened from its cycle high of $1.30 in the middle of July to $1.21 in late September. In the first half of the year, the pound bounced back strongly from the Truss debacle last autumn. That rebound was in large part driven by the substantial shift up in UK interest rate expectations. However, over the past couple of months, interest rate expectations have dropped sharply as inflation started to come down, growth faltered, and the Bank of England called an end to its hiking cycle.

The FTSE 100 has gained more than 2% since the end of August, from around 7,440 on 31st August to 7,608 on 29th September. The rebound has been primarily driven by higher energy prices which boosted the valuations of energy companies. The FTSE 100's relatively high concentration of energy companies helps to explain why UK equities outperformed both US and Euro-zone equities in September. Nonetheless, as recently as 21st April the FTSE 100 stood at 7,914.

APPENDIX B



	1 Year	5 Year	10 Year	25 Year	50 Year
Low	4.65%	4.14%	4.20%	4.58%	4.27%
Date	06/04/2023	06/04/2023	06/04/2023	06/04/2023	05/04/2023
High	6.36%	5.93%	5.51%	5.73%	5.45%
Date	06/07/2023	07/07/2023	22/08/2023	17/08/2023	28/09/2023
Average	5.62%	5.16%	5.01%	5.29%	5.00%
Spread	1.71%	1.79%	1.31%	1.15%	1.18%

The current PWLB rates are set as margins over gilt yields as follows: -.

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

APPENDIX C

Investment instruments

Specified investments

AAA rated money market funds - limit £20m
Debt Management Office – no limit
Royal Bank of Scotland* – limit £25m
Duration of up to one year.

*Royal Bank of Scotland is included as a specified investment since it is the Council's banker and the UK Government holds a majority stake.

Non-specified investments

All institutions included on Link weekly "Suggested Credit List" – limit £10m
All UK local authorities – limit £10m
Duration to be determined by the "Suggested Credit List" from Link