City of BRADFORD METROPOLITAN DISTRICT COUNCIL

Report of the Director of Finance to the meeting of Governance and Audit to be held on 15 June 2023

Subject:

Annual Treasury Management Report 2022-23

Summary statement:

This report shows the Council's Treasury Management activities for the year ending 31 March 2023

EQUALITY & DIVERSITY:

Equality assessments and Equality objectives – There are no equality and diversity implications directly arising from this report.

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Director of Finance

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Portfolio: Corporate Services

Overview & Scrutiny Area:

Corporate Services

Annual Treasury Management Review 2022-23

1. Introduction

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

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

- an annual treasury strategy in advance of the year (Governance and Audit Committee 24/03/2022 and Council 17/05/2022)
- a mid-year, (minimum), treasury update report (Governance and Audit Committee 24/11/2022 and Council 13/12/2022)
- an annual review following the end of the year describing the activity compared to the strategy, (this report)

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

This Council confirms that it has complied with the requirement under the Code to give prior scrutiny to all of the above treasury management reports by the Governance and Audit Committee before they were reported to the full Council.

Member training on treasury management issues was undertaken during the year on 24th November 2022 in order to support members' scrutiny role.

2. Overall Treasury Position as at 31st March 2023

The Council's treasury management debt and investment position is organised by the treasury management service, in order to ensure adequate liquidity for revenue and capital activities, security for investments and to manage risks within all treasury management activities. Procedures and controls to achieve these objectives are well established both through member reporting detailed in the summary, and through officer activity, detailed in the Council's Treasury Management Practices.

At the end of 2022-23 the Council's treasury, (including borrowing by PFI and finance leases), position was as follows:

	31 March 2022 Principal £'m	Rate/ Return	31 March 2023 Principal £'m	Rate/ Return
Fixed rate funding:				
-PWLB	292.3		366.8	
-Market	36.2	4.79%	36.2	4.79%
-Other	5.6		12.1	
PFI and other finance leases	146.9		138.2	
Short term borrowing	37.0		50.0	
Total debt	**518.0**		**603.3**	
CFR	709.2		766.7	
Over / (under) borrowing	(191.2)		(163.4)	
Total investments	186.1	0.13%	48.3	1.57%
Net debt	**331.9**		**555.0**	

3. Prudential Indicators

3.1 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.

Actual capital expenditure forms one of the required prudential indicators. The table below shows the actual capital expenditure and how this was financed. Capital expenditure has increased compared to the previous year as the Council has a number of large construction schemes underway.

	2021-22 Actual £'m	2022-23 Estimate as at Q2 £'m	2022-23 Actual £'m
Capital expenditure	**105.1**	**170.4**	**154.1**
Financed in year	70.1	87.4	76.7
Unfinanced capital expenditure	**35.0**	**83.0**	**77.4**

3.2 The Council's Overall Borrowing Need

The Council's underlying need to borrow for capital expenditure is termed the Capital Financing Requirement (CFR). The CFR is simply the total historic outstanding capital expenditure, which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's indebtedness and so the underlying borrowing need. Any capital expenditure above, which is not immediately paid for through a revenue or capital resource, will increase the CFR.

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.

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

The 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 MRP Policy adopted in the original Treasury Management Strategy Report for 2022-23,approved by the Council on 17-05-2022, was subject to revision during the year. The Council's updated 2022-23 MRP Policy, (as required by the Department for Levelling Up, Housing and Communities (DLUHC) Guidance), was approved as part of the Budget Report for 2022-23 on 23rd February 2023.

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

CFR	31 March 2022 Actual £'m	31 March 2023 Budget £'m	31 March 2023 Actual £'m
Opening balance	698.8	755.0	709.2
Add unfinanced capital expenditure	35.0	103.0	77.4
Less MRP	(20.0)	(22.0)	(16.7)
Less PFI & finance lease repayments	(4.6)	(5.0)	(3.2)
Closing balance	709.2	831.0	**766.7**

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 (21-22), plus the estimates of any additional capital financing requirement for the current year (2022-23) and next two financial years. This essentially means that the Council is not borrowing to support revenue expenditure. The Council has complied with this prudential indicator.

The table below highlights the Council's gross borrowing position against the CFR. The CFR figure is less than budgeted due to slippage on the capital programme, which has resulted in a lower requirement to borrow.

	31 March 2022 Actual £'m	31 March 2023 Budget £'m	31 March 2023 Actual £'m
Capital Financing Requirement	709.2	831.0	766.7
Gross borrowing position	518.0	574.8	603.3
(Under) / over funding of CFR	**191.2**	**256.2**	**163.4**

3.3 Treasury Indicators

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

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

Actual financing costs as a proportion of net revenue stream - this indicator identifies the trend in the cost of capital, (borrowing and other long term obligation costs net of investment income), against the net revenue stream to be met from government grants and local taxpayers.

	2022-23 £'m
Authorised limit	860.0
Maximum gross borrowing position during the year	603.3
Operational boundary	840.0
Financing costs as a proportion of net revenue stream	12.6%

The maturity structure of the debt portfolio was as follows:

	31 March 2022 Actual £'m	**31 March 2023 Actual £'m**
Under 12 months	67.5	58.5
12 months and within 24 months	6.5	9.7
24 months and within 5 years	37.3	64.1
5 years and within 10 years	54.6	56.3
10 years and within 20 years	45.0	57.0
20 years and within 30 years	15.0	40.0
30 years and within 40 years	86.4	71.6
40 years and within 50 years	58.8	107.9

4.The Treasury Strategy for 2022-23

4.1 Investment strategy and control of interest rate risk

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

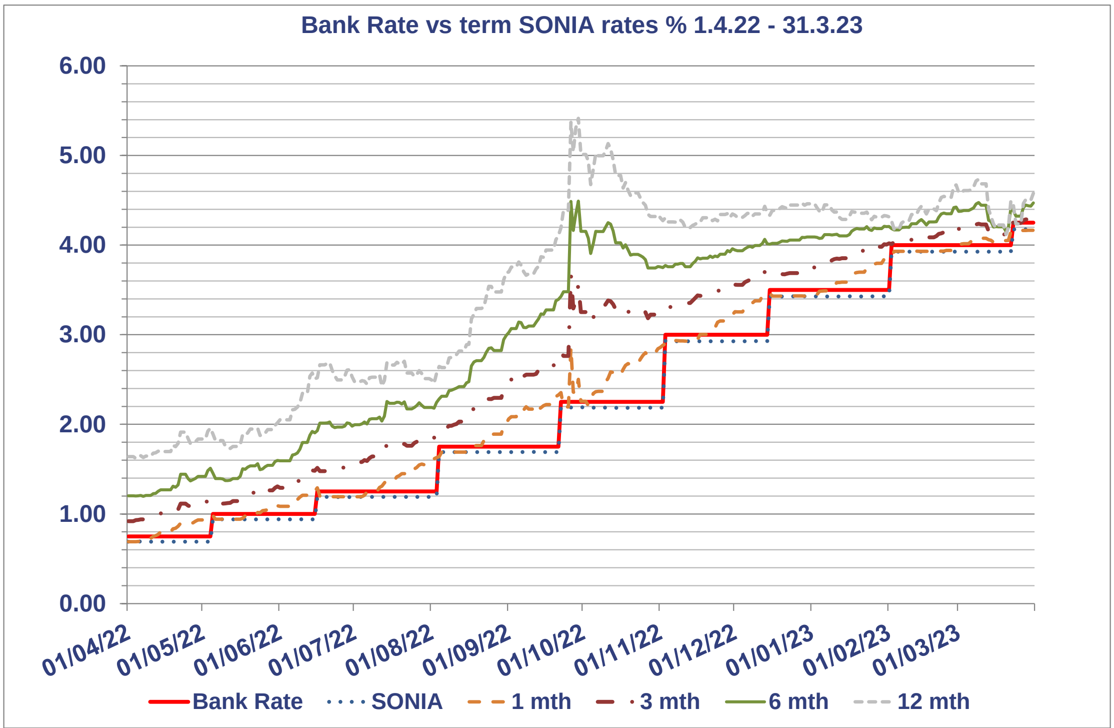
Starting April at 0.75%, Bank Rate moved up in stepped increases of either 0.25% or 0.5%, reaching 4.25% by the end of the financial year, with the potential for a further one or two increases in 2023-24.

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

With bond markets selling off, equity valuations struggling to make progress and, latterly, property funds enduring a wretched Q4 2022, the more traditional investment options, such as specified investments (simple to understand, and less than a year in duration) became more actively used.

Meantime, through the autumn, and then in March 2023, the Bank of England maintained various monetary policy easing measures as required to ensure specific markets, the banking system and the economy had appropriate levels of liquidity at times of stress.

The graph and table below illustrate bank rates for the 2022-23 year.



FINANCIAL YEAR TO QUARTER ENDED 31/3/2023						
	Bank Rate	**SONIA**	**1 mth**	**3 mth**	**6 mth**	**12 mth**
High	4.25	4.18	4.17	4.30	4.49	5.41
High Date	23/03/2023	31/03/2023	31/03/2023	31/03/2023	29/09/2022	29/09/2022
Low	0.75	0.69	0.69	0.92	1.20	1.62
Low Date	01/04/2022	28/04/2022	01/04/2022	01/04/2022	07/04/2022	04/04/2022
Average	2.30	2.24	2.41	2.72	3.11	3.53
Spread	3.50	3.49	3.48	3.38	3.29	3.79

While the Council has taken a cautious approach to investing, it is also fully appreciative of changes to regulatory requirements for financial institutions in terms of additional capital and liquidity that came about in the aftermath of the Great Financial Crisis of 2008-09. These requirements have provided a far stronger basis for financial institutions, with annual stress tests by regulators evidencing how institutions are now far abler to cope with extreme stressed market and economic conditions.

Investment balances have been kept to a minimum through the agreed strategy of using reserves and balances to support internal borrowing, rather than borrowing externally from the financial markets. External borrowing incurs an additional cost, due to the differential between borrowing and investment rates as illustrated in the charts shown above and Appendix 2. Such an approach has also provided benefits in terms of reducing counterparty risk exposure, by having fewer investments placed in the financial markets.

4.2 Investment Outturn 22-23

The Councils investment position at the end of 2022-23 is summarised below

INVESTMENT PORTFOLIO	2021-22		2022-23	
	£'m	%	£'m	%
Treasury investments				
Banks	103.5m	55	-	-
DMADF	5.0m	3	-	-
Money Market Funds	77.6m	42	48.3	100
Total managed in house	**186.1m**	**100**	**48.3**	**100**

The maturity structure of the investment portfolio was as follows:

	2021-22 Actual £'m	2022-23 Actual £'m
Investments		
Longer than 1 year	0.0	0.0
Up to 1 year	186.1	48.3

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 17/05/22. 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. How-ever cash balances have reduced during the year and the strategy will need to be reviewed during 2023-24.

Investments held by the Council - The Council maintained an average balance of £33.75m of internally managed funds. The internally managed funds earned an average rate of return of 2.85%. The comparable performance indicator is the average overnight SONIA rate was 2.304%. The total investment income was £1.424m.

5.Borrowing

5.1 Borrowing strategy and control of interest rate risk

Borrowing is undertaken to fund net unfinanced capital expenditure and naturally maturing debt and also to maintain cash flow liquidity requirements. During 2022-23, 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 investment returns were very low and minimising counterparty risk on placing investments also needed to be considered.

A cost of carry generally remained in place during the year on any new long-term borrowing that was not immediately used to finance capital expenditure, as it would have caused a temporary increase in cash balances; this would have incurred a revenue cost – the difference between (higher) borrowing costs and (lower) investment returns.

The policy of avoiding new borrowing by running down spare cash balances has served well over the last few previous years. However, due to an increase in capital spend and a reduction in reserves and balances there was a need to complete additional PWLB Borrowing. New loans totalling £90m, with an average rate of interest of 3.89% have been completed during 2022-23.

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

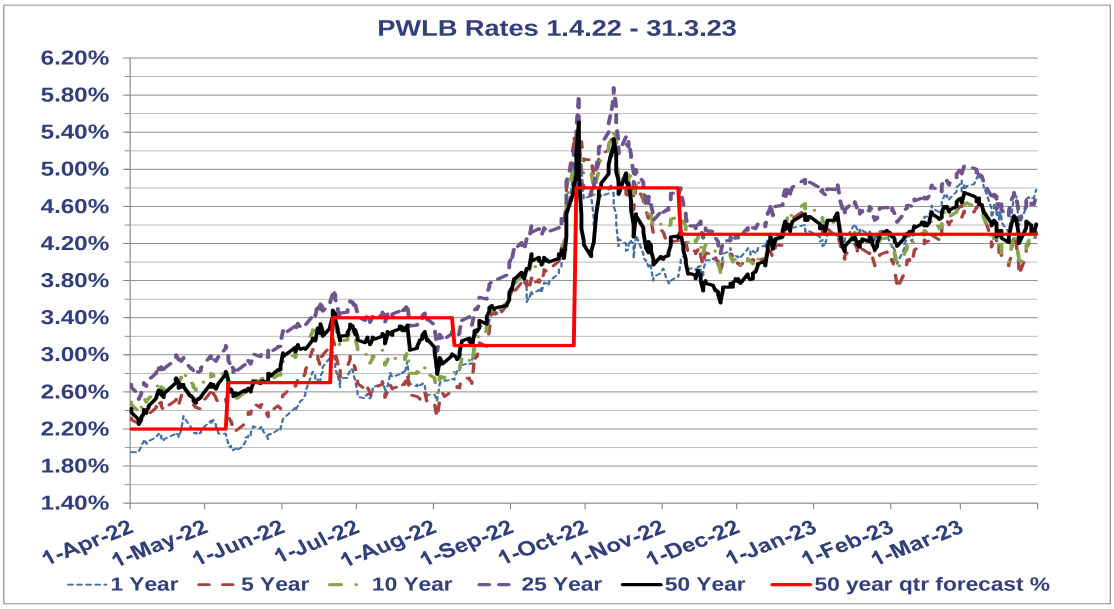
- if it had been felt that there was a significant risk of a sharp FALL in long and short term rates, (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), then long term borrowings would have been postponed, and potential rescheduling from fixed rate funding into short term borrowing would have been considered.

- if it had been felt that there was a significant risk of a much sharper RISE in long and short term rates than initially expected, perhaps arising from an acceleration in the start date and in the rate of increase in central rates in the USA and UK, an increase in world economic activity or a sudden increase in inflation risks, then the portfolio position would have been re-appraised. Most likely, fixed rate funding would have been drawn whilst interest rates were lower than they were projected to be in the next few years.

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

Link Group Interest Rate View	7.2.22											
	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25
BANK RATE	1.00	1.00	1.25	1.25	1.25	1.25	1.25	1.25	1.25	1.25	1.25	1.25
3 month ave earnings	1.00	1.00	1.20	1.20	1.20	1.20	1.20	1.20	1.20	1.20	1.20	1.20
6 month ave earnings	1.10	1.20	1.30	1.30	1.30	1.30	1.30	1.30	1.30	1.30	1.30	1.30
12 month ave earnings	1.50	1.60	1.70	1.70	1.60	1.60	1.50	1.40	1.40	1.40	1.40	1.40
5 yr PWLB	2.30	2.30	2.30	2.30	2.30	2.30	2.30	2.30	2.30	2.30	2.30	2.30
10 yr PWLB	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40
25 yr PWLB	2.50	2.50	2.60	2.60	2.60	2.60	2.60	2.60	2.60	2.60	2.60	2.60
50 yr PWLB	2.30	2.30	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40

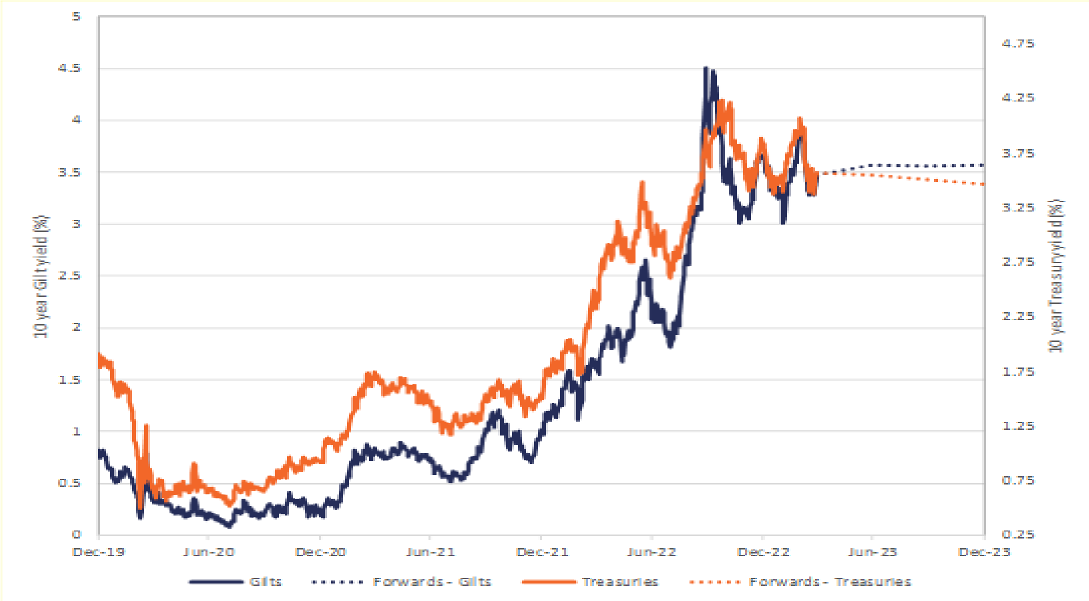
PWLB RATES 2022-23



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

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

Graph of UK gilt yields v. US treasury yields



Gilt yields have been on a continual rise since the start of 2021, peaking in the autumn of 2022. Currently, yields are broadly range bound between 3% and 4.25%.

At the close of the day on 31 March 2023, all gilt yields from 1 to 50 years were between 3.64% and 4.18%, with the 1 year being the highest and 6-7.5 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)

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 first rises to dampen inflationary pressures and a tight labour market, and is then cut as the economy slows, unemployment rises, and inflation (on the Consumer Price Index measure) moves closer to 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, but the scale and pace of this has already been affected by the Truss/Kwarteng "fiscal experiment" in the autumn of 2022 and more recently by the financial market unease with some US (e.g., Silicon Valley Bank) and European banks (e.g., Credit Suisse). The gradual reduction of the Bank's original £895bn stock of gilt and corporate bonds will 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, is an unknown at the time of writing.

5.2 Borrowing Outturn 2022-23

£15.511m of loans matured in January and February 2023 with an average rate of 6.85%. Due to increased capital spend and a reduction in reserve balances new loans of £90m were undertaken this year with an average rate of interest of 3.89%.

Summary of debt transactions – management of the debt portfolio resulted in a fall in the average interest rate of 0.24%.

5.3 Borrowing in advance of need

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

5.4 Rescheduling

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

6. Other Issues

6.1 None

7.Changes to the Treasury Management Policy

7.1 None

8. Financial and Resources Appraisal

8.1 The financial implications are set out in section 1 to 8 of this report

9. Risk Management and Governance Issues

9.1 The principal risks associated with treasury management are:

<u>Risk: Loss of investments as a result of failure of counterparties.</u>
Mitigation: Limiting the types of investment instruments used, setting lending criteria for counterparties, and limiting the extent of exposure to individual counterparties.

Risk: That the Council will commit too much of its investments in fixed term investments and might have to recall investments prematurely resulting in possible additional costs or new borrowing (Liquidity risk).
Mitigation: Ensuring that a minimum proportion of investments are held in short term investments for cash flow purposes.

Risk: Increase in the net financing costs of the Council due to borrowing at high rates of interest.
Mitigation: Planning and undertaking borrowing and lending in light of assessments of future interest rate movements, and by undertaking mostly long term borrowing at fixed rates of interest (to reduce the volatility of capital financing costs).

Risk: Higher interest rates increase borrowing making it more difficult to self-finance capital schemes. Debt servicing becomes less affordable and less sustainable and crowds out revenue spend.
Mitigation: To pause, delay or defer capital schemes. Also review opportunities to borrow in the future at current interest rates.

Risk: Return on non-treasury investments lower than expected.
Mitigation: Review and analysis of risk prior to undertaking non-treasury investments.

Risk: The Council's Minimum Revenue Policy charges an insufficient amount to the Revenue Estimates to repay debt.
Mitigation: Align the Minimum Revenue Policy to the service benefit derived from the Council's assets.

Risk: Associated with cash management, legal requirements and fraud.
Mitigation: These risks are managed through:

- Treasury Management Practices covering all aspects of Treasury management procedures including cash flow forecasting, documentation, monitoring, reporting and division of duties.
- All Treasury management procedures and transactions are subject to inspection by internal and external auditors. The Council also employs external financial advisors to provide information on market trends, credit rating alerts, lending criteria advice and investment opportunities.

Risk: Increase in capital financing costs due to inflationary forces resulting in increased cost pressures on current capital projects and higher costs compared to approved budgets.
Mitigation: Regular monitoring of the capital programme through comparison to budgets.

Risk: Anticipated borrowing is lower than expected because the 2023-24 capital programme is underspent. This is explained in more detail below, together with the actions being taken to reduce these risks:
Mitigation: The Council is required to set a balanced budget for its revenue estimates; so in broad terms, income received will match expenditure over the 2023-24 financial year. The 2023-24 revenue estimates cause only temporary cash

flow differences, for example when income is received in a different month to when the expenditure is incurred.

However, the 2023-24 capital budget will cause a cash flow shortfall in the long term, which generates a borrowing requirement. While some of the capital budget is funded immediately, mainly with Government grants, other elements are not funded initially, leading to the cash flow deficit that requires borrowing.

Managing borrowing is part of the Treasury Management role. To help in its management, the Treasury Strategy identifies the element within the capital budget that is not funded straightaway, to anticipate the Council's borrowing requirement.

However, when the capital budget is underspent, the Council has a lower borrowing requirement than anticipated. This risk is managed in practice because the Council only borrows when there is an actual cash flow shortage. The uncertainty around spend against the capital budget makes cash flow management more difficult. For example, it is less likely that the Council would take advantage of a short-term fall in interest rates, without more certainty around the timing of any borrowing need. Actions that have taken place to manage the risks relating to this uncertainty in the timing of capital spend are: Councillor and Officer challenge sessions on the capital budget; increased scrutiny of the capital forecasts in the quarterly monitoring, and the collection of additional documentation around the critical paths of individual schemes.

10. Legal Appraisal

10.1 Any relevant legal considerations are set out in the report

11**. Other Implications**

11.1 Equality & Diversity – no direct implications
11.2 Sustainability implications – no direct implications
11.3 Green house Gas Emissions Impact – no direct implications
11.4 Community safety implications – no direct implications
11.5 Human Rights Act – no direct implications
11.6 Trade Unions – no direct implications
11.7 Ward Implications – no direct implications
11.8 Implication for Corporate Parenting – no direct implications
11.9 Issues arising from Privacy Impact Assessment– no direct implications

12. Not for publications documents

12.1 None

13. Options

13.1 None

14. Recommendations

14.1 That the report be noted by the Governance and Audit Committee and passed to full Council for adoption. This includes the actual 2022-23 prudential and treasury indicators in the report

15. Appendices

Appendix 1 Prudential and Treasury Indicators
Appendix 2 Borrowing and Investment Rates
Appendix 3 The Economy and Interest Rates
Appendix 4 Approved Counties for Investments as at 31st March 2023

Appendix 1: Prudential and Treasury indicators

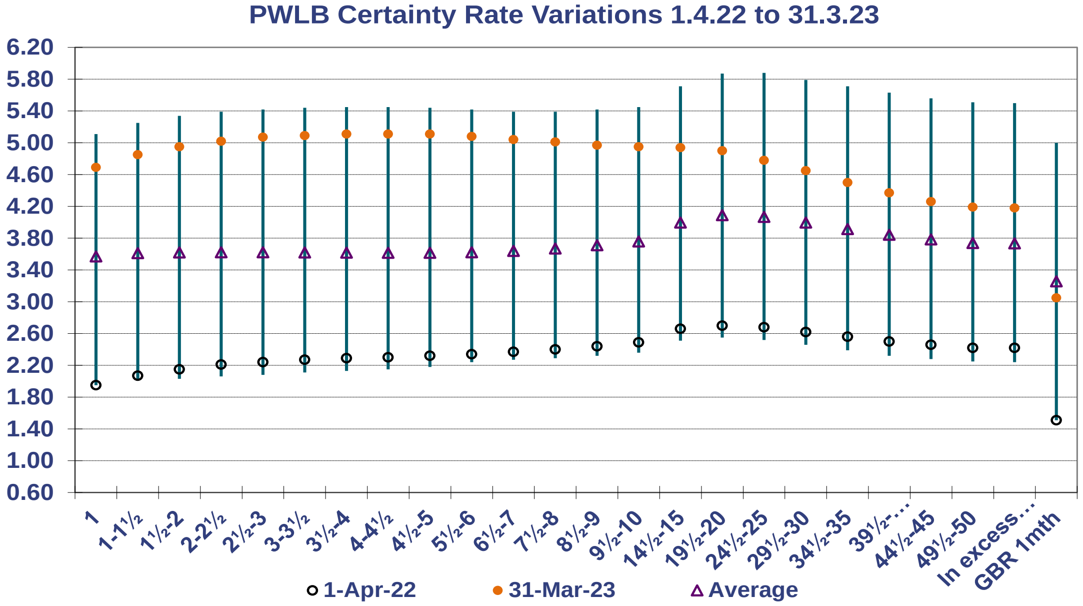
1. PRUDENTIAL INDICATORS	2021-22 Actual £'000	2022-23 Estimate £'000	2022-23 Actual £'000
Capital Expenditure	105,085	170,400	154,084
Ratio of financing costs to net revenue stream	13.2%	15.3%	12.6%*
Gross borrowing requirement General Fund	518,111	574,800	603,334
Capital Financing Requirement	709,246	831,000	766,735

*Note in future years some of the forecast debt will be directly funded by self-financing schemes, where income is generated to meet the cost of investment in the scheme.

2. TREASURY MANAGEMENT INDICATORS	2021-22 Actual £'000	2022-23 Estimate £'000	2022-23 Actual £'000
Authorised Limit for external debt			
borrowing	371,111	651,900	465,115
other long term liabilities	146,900	138,100	138,219
TOTAL	**518,011**	**790,000**	**603,334**
Operational Boundary for external debt			
borrowing	371,111	631,900	465,115
other long term liabilities	146,900	138,100	138,219
TOTAL	**518,011**	**770,000**	**603,334**
Actual external debt	**518,011**		**603,334**

Maturity structure of fixed rate borrowing during 2022-23	upper limit	lower limit
under 12 months	20%	0%
12 months and within 24 months	20%	0%
24 months and within 5 years	50%	0%
5 years and within 10 years	50%	0%
10 years and within 20 years	90%	0%
20 years and within 30 years	90%	0%
30 years and within 40 years	90%	0%
40 years and within 50 years	90%	0%
Maturity structure of investments during 2022-23	upper limit	lower limit
Longer than 1 year	£20m	£0m

Appendix 2: Borrowing and Investment Rates



HIGH/LOW/AVERAGE PWLB RATES FOR 2022-23

	1 Year	5 Year	10 Year	25 Year	50 Year
Low	1.95%	2.18%	2.36%	2.52%	2.25%
Date	01/04/2022	13/05/2022	04/04/2022	04/04/2022	04/04/2022
High	5.11%	5.44%	5.45%	5.88%	5.51%
Date	28/09/2022	28/09/2022	12/10/2022	12/10/2022	28/09/2022
Average	3.57%	3.62%	3.76%	4.07%	3.74%
Spread	3.16%	3.26%	3.09%	3.36%	3.26%

Appendix 3: The Economy and Interest Rates

UK. Economy.

Against a backdrop of stubborn inflationary pressures, the easing of Covid restrictions in most developed economies, the Russian invasion of Ukraine, and a range of different UK Government policies, it is no surprise that UK interest rates have been volatile right across the curve, from Bank Rate through to 50-year gilt yields, for all of 2022-23.

Market commentators' misplaced optimism around inflation has been the root cause of the rout in the bond markets with, for example, UK, EZ and US 10-year yields all rising by over 200bps in 2022. The table below provides a snapshot of the conundrum facing central banks: inflation is elevated but labour markets are extra-ordinarily tight, making it an issue of fine judgment as to how far monetary policy needs to tighten.

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

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

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

The UK unemployment rate fell through 2022 to a 48-year low of 3.6%, and this despite a net migration increase of c500k. The fact remains, however, that with many economic participants registered as long-term sick, the UK labour force shrunk by c500k in the year to June. Without an increase in the labour force participation rate, it is hard to see how the UK economy will be able to grow its way to prosperity, and with average wage increases running at over 6% the MPC will be concerned that wage inflation will prove just as sticky as major supply-side shocks to food (up 18.3% y/y in February 2023) and energy that have endured since Russia's invasion of Ukraine on 22 February 2022.

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

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

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

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

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

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

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

In addition, the Fed is expected to continue to run down its balance sheet once the on-going concerns about some elements of niche banking provision are in the rear-view mirror.

As for inflation, it is currently at c6% but with the economy expected to weaken during 2023, and wage data already falling back, there is the prospect that should the economy slide into a recession of any kind there will be scope for rates to be cut at the backend of 2023 or shortly after.

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

Appendix 4: Approved Countries for Investments as at 31st March 2023

AAA

- Australia
- Denmark
- Germany
- Netherlands
- Norway
- Singapore
- Sweden
- Switzerland

AA+

- Canada
- Finland
- U.S.A.

AA

- Abu Dhabi (UAE)
- France

AA-

- Belgium
- Qatar
- **U.K.**