Report title	Treasury Management Report – Mid Year 2023/24
Report author	A Ismailov - Senior Accountant
Department	Financial Services
Exempt?	No
Exemption type	Not applicable
Reasons for exemption	Not applicable

Purpose of report:

For information

Synopsis of report:

This is the report on Council's treasury management activity and performance in the first half of the 2023/24 financial year focusing on financing and liquidity, cash management and risk management.

The report also reflects on the mid-year review of Council's treasury and investment strategies, along with prudential indicators, and compliance with the limits set for 2023/24.

Recommendation:

Members are invited to note the content of the report.

1. Background Information

1.1. The Council's treasury management activity is underpinned by CIPFA's (Chartered Institute of Public Finance and Accountancy) Code of Practice on Treasury Management ("the Code"), and the CIPFA Prudential Code for Capital Finance in Local Authorities ("the Prudential Code"). These require local authorities to produce annually Prudential Indicators and a Treasury Management Strategy Statement on the likely financing and investment activity. From 2023/24, the Code also recommends that members are informed of treasury management activities quarterly.

1.2. The Council's Treasury Management Strategy for 2023/24 was approved at Full Council on 09 February 2023. This report sets out the Council's performance against the criteria in this report in the first half of 2023/24.

1.3. 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."

1.4. No treasury management activity is without risk; The Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the

analysis and reporting of treasury management activities focuses on their risk implications for the organisation, and any financial instruments entered into to manage these risks.

1.5. The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This report, therefore, provides details of the treasury activities and highlights compliance with the Council's policies previously approved by the members.

1.6. In its oversight role, the Overview and Scrutiny Select Committee will consider this report on 13 December 2023.

2. Prudential and Treasury Indicators and Compliance

2.1. In compliance with the requirements of the Code this report provides members with a summary report of the treasury management activity during the first half of financial year of 2023/24 ("H1 2023/24"). Officers can confirm that during H1 2023/24, the Council complied with all its legislative and regulatory requirements and its Treasury Management Strategy Statement and Treasury Management Practices.

2.2. There are no proposed changes to the current Treasury Management Strategy.

2.3. During the first half of the year the Council operated within the treasury and prudential indicators set out in the Council's Treasury Management Strategy and in compliance with the Council's Treasury Management Practices and a prudent approach was taken in relation to all investment activity with priority being given to security and liquidity over yield.

2.4. A full set of prudential and treasury indicators for H1 2023/24 are set out in Appendix A

3. Risk management

3.1. The Council aims to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity. The Treasury Management Strategy Statement ("TMSS") for 2023/24, which includes the Annual Investment Strategy, sets out the Council's investment priorities as being:

Credit risk
Counterparty credit quality is assessed and monitored with reference to credit ratings including a minimum sovereign credit rating and Credit Default Swap (CDS) overlay information.

Liquidity risk
In keeping with the DLUHC Guidance on Investments, the Council maintains a sufficient level of liquidity using Money Market Funds and call accounts.

Yield
The Council seeks to optimise returns commensurate with its objectives of security and liquidity.

4. Economic update

4.1. The following section was provided by the Council's Treasury Advisors, Link Group and reflects the market position in October 2023:

4.2. The first half of 2023/24 saw:

- Interest rates rise by a further 100 basis points, 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% month on month decline in real GDP (Gross Domestic Product) in July, mainly due to more strikes.
- CPI (Consumer Price Index) 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 3-month year on year growth of average earnings rose to 7.8% in August, excluding bonuses).

4.3. The 0.5% month on month 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.

4.4. 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.

4.5. The 0.4% month on month 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.

4.6. 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.

4.7. 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 1.017mln in July to 0.989mln 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.

4.8. 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 3-month year on year rate rose from 8.4% 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% 3-month year on year

in June to 8.1%, it is still well above the Bank of England's prediction for it to fall to 6.9% in September.

4.9. 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.

4.10. 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 voted for no change and the other four voted for a 25bps hike.

4.11. Like the US Federal Reserve, 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".

4.12. 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.

4.13. 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).

4.14. 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 administration 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.

4.15. 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.

5. Borrowing Activity in H1 2023/24

5.1. 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 H1 2023/24 unfinanced capital expenditure, and prior years' net or unfinanced capital expenditure which has not yet been paid for by revenue or other resources.

5.2. Part of the Council's treasury activities is to monitor cash position and organise financing against the borrowing needs. Financing sourced through combination of external 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.

5.3. No new borrowing was undertaken during H1 2023/24 meaning that the Council continued to maintain an under-borrowed position. This meant that the capital borrowing need, the CFR, was not fully funded with loan debt, as cash supporting the Council's reserves, balances and cash flow was used as an interim measure in the sharply rising interest rates environment and the period of low capital spend.

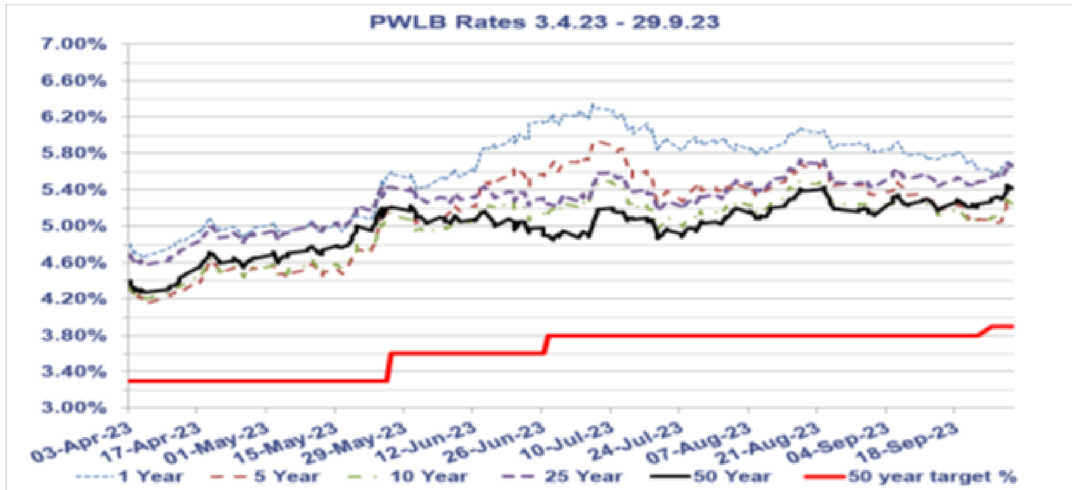
5.4. Table 1 sets out the borrowing activity in H1 2023/24.

Table 1 – Borrowing activity in H1 2023/24

	Opening Balance £'000	New borrowing £'000	Borrowings repaid £'000	Closing balance £'000
HRA – PWLB	100,000	0	0	100,000
General Fund - PWLB	499,000	0	0	499,000
General Fund – Other	44,181	0	281	43,900
	643,181	**0**	**281**	**642,900**

5.5. 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. Gilt yields and PWLB certainty rates were on a rising trend throughout the first half of 2023/24. At the beginning of April, the 5-year rate was the cheapest part of the curve and touched 4.14% whilst the 25-year rate was relatively expensive at 4.58%.

5.6. July saw short-dated rates peak at their most expensive. The 1-year rate spiked to 6.36% and the 5-year rate to 5.93%. Although, in due course, short-dated rate expectations fell, the medium dates shifted higher through August and the 10-year rate pushed higher to 5.51% and the 25-year rate to 5.73%. The 50-year rate was 4.27% on 5th April but rose to 5.45% on 28th September. The actual PWLB rates during H1 2023/24 were as follows:



5.7 The Department for Levelling Up, Housing and Communities (DLUHC) has policy responsibility for the Prudential Framework under which local authorities borrow and invest. In May 2022, the Government introduced The Levelling Up and Regeneration Bill (LUR Bill), which includes new provisions that expand the government's statutory powers to directly tackle excessive risk within local government capital system. A local authority comes into scope of the new powers when a 'trigger point' is breached with respect to either of the four capital risk metrics as set out in the LUR Bill.

5.8 DLUHC's consultation process on how the capital risk metrics are calculated was completed at the end of September 2023 but as yet officers are not aware of the outcomes or what it means for the Council. The 2024/25 Treasury Management Strategy will discuss the impact of the capital risk metrics resulting from the new regulations, along with any additional affordability and borrowing capacity constraints that may be placed on the Council as a result.

6. Interest rates in H1 2023/24

6.1. Bank rates continued to rise during H1 2023/24 (by further 100basis points). At the start of August, the Bank of England's Monetary Policy Committee (MPC) increased Bank Rate by 25 basis points to 5.25%.

6.2. Despite the tighter monetary policy, the UK economy surprised to the upside during in the second quarter of 2023, as GDP rose by 0.2%. The market expected a further 25 basis points interest rate hikes (from 5.25% to 5.50%) at the most recent Bank of England's policy meeting at the end of September, however, the bank has held the rate.

6.3. Overall, with economic activity still resilient, and wage growth and services inflation (a key consideration for the Bank of England) both stronger than originally expected, markets still anticipate further monetary policy tightening in the pipeline.

6.4. While the Council continues to take 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 financial crisis. 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.

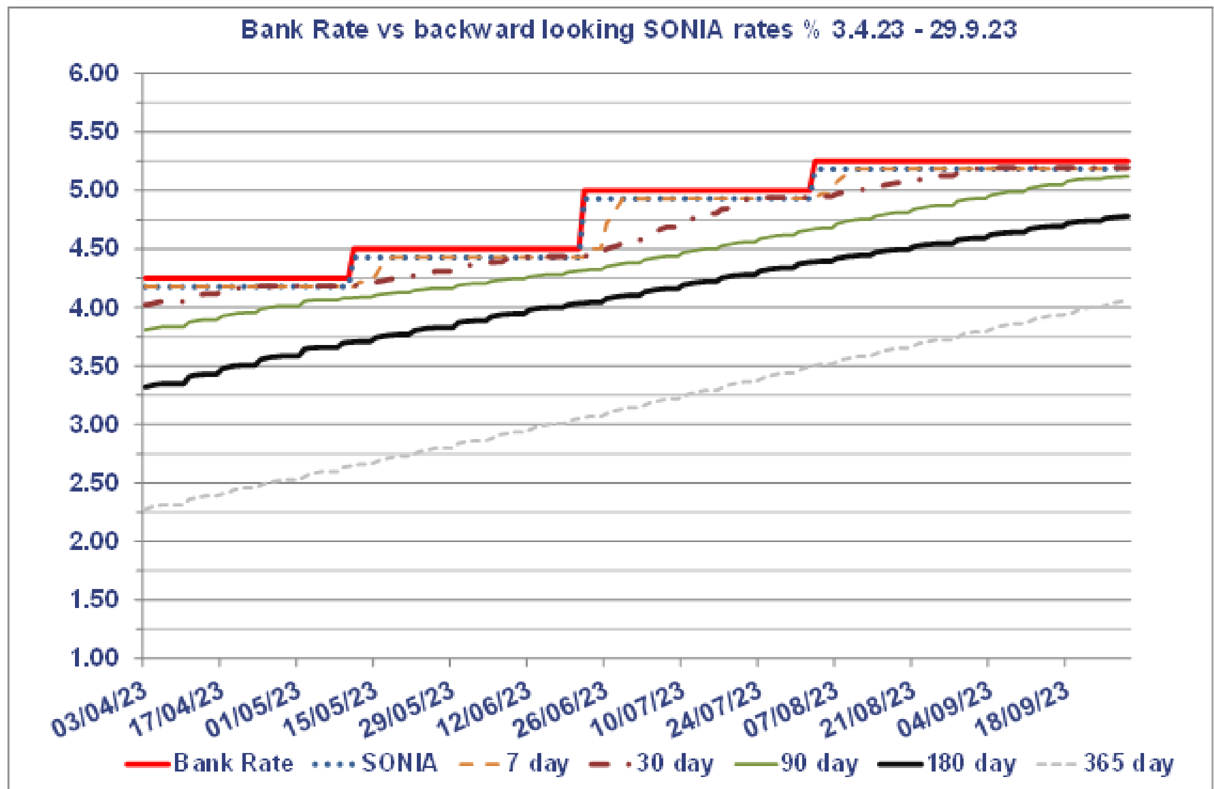
6.5. Investment balances have been kept to a minimum through the agreed strategy of using reserves and balances to support internal borrowing, rather than borrowing externally from the financial markets. External borrowing would have incurred an additional cost, due to

the differential between borrowing and investment rates. This also provides benefits of reducing counterparty risk exposure, by fewer investments in the financial markets.

Interest rate benchmark

6.6. The Council uses the Sterling Overnight Index Average ("SONIA") as a benchmark interest rate. This is published daily and measures the cost of overnight borrowing on a backward-looking basis.

6.7. The SONIA (backward-looking) rates during the H1 2023/24 were as follows:



	Bank Rate	SONIA	7 day	30 day	90 day	180 day	365 day
High	5.25	5.19	5.19	5.20	5.12	4.78	4.06
High Date	03/08/2023	29/09/2023	04/09/2023	27/09/2023	29/09/2023	29/09/2023	29/09/2023
Low	4.25	4.18	4.18	4.02	3.81	3.32	2.27
Low Date	03/04/2023	04/04/2023	11/04/2023	03/04/2023	03/04/2023	03/04/2023	03/04/2023
Average	4.81	4.74	4.71	4.64	4.44	4.10	3.16
Spread	1.00	1.01	1.01	1.17	1.31	1.46	1.79

6.8. The Council's actual interest rate performance during H1 2023/24 was 4.63%. The Council's overall performance compares favourably with the average SONIA rates (given the current environment of continuous bank rate increases) as can be seen in the above table.

6.9. The Council's Treasury Management Strategy sets out a lower rate of interest for the Housing Revenue Account based on the risk-free nature of the account. This lower rate is achieved by deducting the credit risk margin from the actual rate achieved by the Council. The resulting interest rate applicable to the HRA during H1 2023/24 was 4.43%.

6.10. The Council invests in two Pooled Funds (operated by CCLA (Churches, Charities and Local Authorities) Investment Management Limited). These allow the Council to diversify into asset classes other than cash without the need to own and manage the underlying investments. Investments in these funds are long term in nature and over long-term horizons they provide investors with relatively strong levels of interest (in the form of

dividends). However, the capital values of these assets can be subject to large fluctuations (both up and down) over relatively short time frames.

6.11. The movement of the Council's two CCLA pooled funds is as follows:

Table 2 – Pooled Funds in H1 2023/24				
	Original Investment £	**Value 31 Mar 2023 £**	**Value 30 Sep 2023 £**	**Annualised Return %**
CCLA Property Fund	2,000,000	2,263,467	2,233,866	5.26
CCLA Diversified Income Fund	2,000,000	1,894,514	1,865,384	3.35

The differences between the Original Sums invested and the Values on 30 September 2023 are held on the Council's Balance Sheet in the Pooled Investments Adjustment Account.

7. Investments in H1 2023/24

7.1. The Council's investment policy is governed by DLUHC investment guidance and is reflected in the Annual Investment Strategy approved by the Council each year. 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 first half of financial year of 2023/24 conformed to the approved strategy, and the Council had no liquidity difficulties.

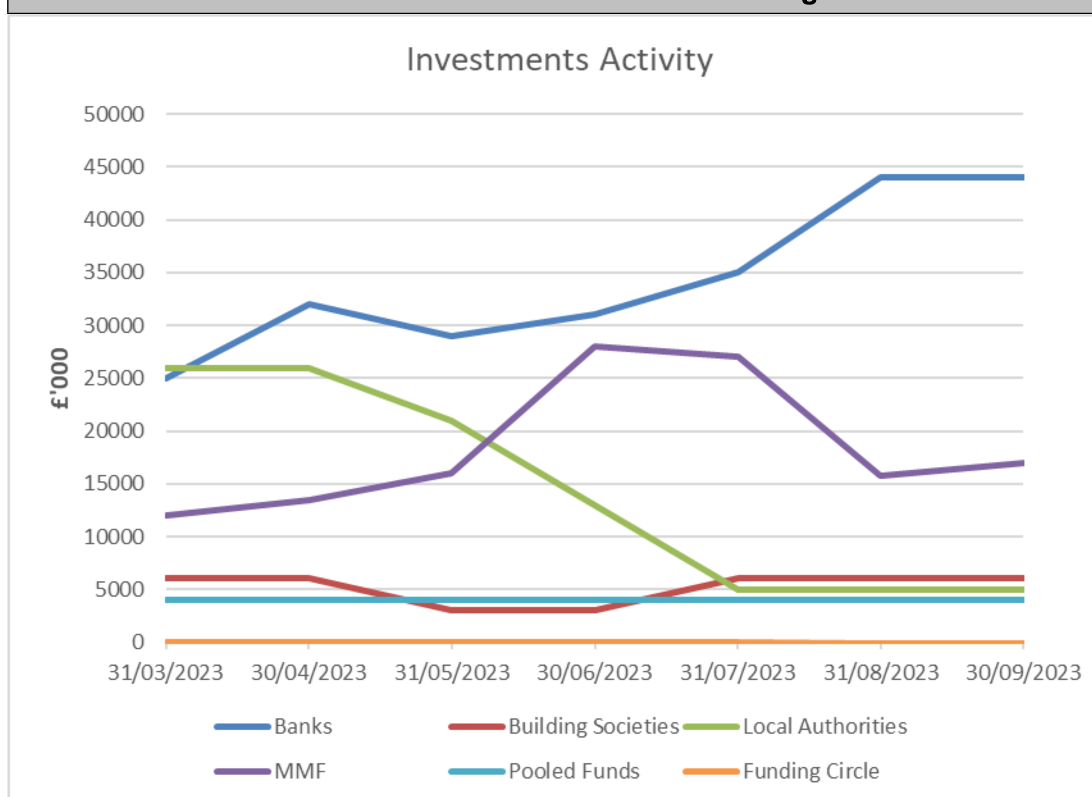
7.2. Investments of £76.0million were held by the Council as of 30 September 2023 with investment turnover principally driven by the availability of counterparties that meet the criteria set out in the Annual Investment Strategy. Table 3 below summarises investment activity during the first half of the year , split between the sectors of the counterparties that the funds were invested with.

Table 3 - Investment activity in H1 2023/24				
	Opening Balance	**New Investments**	**Investments Recalled**	**Closing Balance**
	£000	£000	£000	£000
Specified Investments				
Banking sector	25,000	53,000	34,000	44,000
Building societies	6,000	9,000	9,000	6,000
Local Authorities	26,000	8,000	29,000	5,000
Money Market Funds	12,000	74,000	69,000	17,000
Unspecified Investments				
Pooled Funds & Investment Schemes	4,000	0	0	4,000
Funding Circle	42	0	14	28
	73,042	**144,000**	**141,014**	**76,028**

7.3. Aside from the parameters set in the Annual Investment Strategy, the main factors that determine the amount of investment income are the level of interest rates, cash flow and the level of reserves and balances. The impact of capital cash flows – receipts from sales and timing of capital projects – also has a significant impact on cash flows.

7.4. The monthly movement in balances between these categories during H1 2023/24 is set out in Table 4 below and reflects the available counterparties and investment rates at that time.

Table 4 - Movement between investments during H1 2023/24



7.5. A full list of investments held as of 30 September 2023 is set out in Appendix C.

8. Non-treasury Investments

8.1. The Prudential Code, TM Code and DLUHC regulations include guidance on what is termed "non-treasury" investments. These are predominantly investments for commercial return such as:

- commercial loans to companies and other organisations, and
- holding property for a financial return (investment property).

The Council owns a significant investment property portfolio which is now managed through its developing Asset Management Strategy and provided loans to its wholly owned companies and local community groups.

<u>Commercial Loans</u>

8.2. The Council has funded its three wholly owned companies via Loan Facilities (that have been approved by the Full Council at rates set in accordance with the competition rules) which enabled them to buy some of the properties resulting from the Council's regeneration schemes. There are no plans in the current Capital Programme to increase investments in these areas. The table below sets out the list of loan facilities and movements in their balances in H1 2023-24.

Loan Type	31/03/2023 Investment £'000	H1 2023/24 Movement £'000	30/09/2023 Investment £'000	Interest Rate %
Development Loans - Addlestone One	25,326		25,326	5.04
Development Loans – Magna Square	11,838		11,838	4.22
Development Loans - Other	1,000		1,000	4.86
Working Capital Loans	445		445	7.54
Working Capital Loans	300		300	7.36

Working Capital Loans	2,100	400	2,500	7.40
Totals	**41,009**	**400**	**41,409**	

8.3. The Working Capital Loan Facilities approved in October 2020 allowed a sum of £3m available to draw down as required. Of this amount £500,000 is still available to drawdown. It is anticipated that this will be required before the end of this financial year.

Property performance measurement

8.4. To better describe the role the investment property portfolio plays in the Council's capital and revenue strategies a set of performance reporting measures were approved as part of both the Annual Asset Management Strategy and the Capital & Investment Strategy.

8.5. Appendix D sets out the key performance indicators in H1 2023-24. These will be further developed during 2023-24 using benchmarking analysis relative to the broader market, based on frequent data via a subscription to MSCI Analytics. Work on uploading data to MSCI is currently being undertaken.

8.6. As with the treasury information, the provision of economic data helps to put some of the above metrics into perspective. An update on property related economic matters provided by Montagu Evans LLP reflecting the market position in September 2023 is set out in Appendix D.

9. Legal Implications

9.1. The powers for a local authority to borrow and invest are governed by the Local Government Act 2003 and associated Regulations. A local authority may borrow or invest for any purpose relevant to its functions, under any enactment, or for the purpose of the prudent management of its financial affairs. The Regulations also specify that authorities should have regard to the CIPFA Treasury Management Code, the Government Investments Guidance and the CIPFA Prudential Code for Capital Finance in Local Authorities when carrying out their treasury management functions.

10. Environmental/Sustainability/Biodiversity implications

10.1. Ethical or Sustainable investing is becoming a more commonplace discussion within the wider investment community. There are currently a small, but growing number of financial institutions and fund managers promoting Environmental, Social and Governance (ESG) products however the types of products we can invest in are constrained to those set out in our Investment Strategy which is driven by investment guidance, both statutory and from CIPFA, making it clear that all investing must adopt SLY principles – security, liquidity and yield: ethical issues must play a subordinate role to those priorities.

10.2. The Council does not invest directly in any companies – other than our own - and our investments are limited to investments with the banking sector (term deposits etc) and investments in property (our investment properties). We have £4million split between two pooled funds both managed by the CCLA and their approach to ESG can be found on their website.

11. Council Policy

11.1. This is set out in the Treasury Management Policy Statement, the Annual Investment Strategy, and associated Practices and Schedules.

11.2. The Council's treasury management policy statement states:

"The Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation, and any financial instruments entered into to manage these risks."

11.3. It is the security of investments that has always been the main emphasis of our treasury strategy. In balancing risk against return, Officers continue to place emphasis on the control of risk over yield following investment guidance, both statutory and from CIPFA, which make it clear that all investing must adopt SLY principles – security, liquidity and yield in that order.

12. Conclusions

12.1. The first half of 2023/24 continued the challenging investment environment with counterparty risk remaining our primary treasury management priority. The criteria in the Annual Investment Strategy are continuously reviewed to minimise risk as much as practicable whilst retaining the ability to invest with secure institutions.

12.2. During the half year ended 30th September 2023, the Council has operated within the treasury and prudential indicators set out in the Council's Treasury Management Strategy Statement for 2023/24. The Corporate Head of Finance reports that no difficulties are envisaged for the current or future years in complying with these indicators.

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

13. Appendices

- Treasury and Prudential Indicators 2023/24 as of 30 September 2023
- Borrowings as of 30 September 2023
- Investments as of 30 September 2023
- Property Performance Indicators as of September 2023
- Economic commentary for property as of 30 September 2023

Treasury and Prudential Indicators 2023/24 as of 30 September 2023

Treasury Indicators	2023/24 Budget (Year End) £'000	30.09.23 Actual £'000
Authorised limit for external debt	700,613	700,613
Operational boundary for external debt	675,613	675,613
Gross external debt	650,613	642,900
Investments	53,756	76,028
Net borrowing	596,857	566,872

Maturity structure of fixed rate borrowing - upper and lower limits		
Under 12 months	25%	2.42%
12 months to 2 years	25%	3.20%
2 years to 5 years	25%	4.03%
5 years to 10 years	50%	11.59%
10 years to 20 years	100%	10.69%
20 years to 30 years	100%	3.36%
30 years to 40 years	100%	17.42%
40 years to 50 years	100%	47.29%

Upper limit for principal sums invested over 365 days *(split by financial years beyond current year end):* **Year 1**	5,000	0

The Operational Boundary – This is the limit beyond which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt.

The authorised limit for external borrowing. – A further key prudential indicator represents a control on the maximum level of borrowing. This represents a limit beyond which external debt is prohibited, and this limit needs to be set or revised by the Full Council. It reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. This is the statutory limit determined under Section 3(1) of the Local Government Act 2003. The Government

retains an option to control either the total of all Councils' plans, or those of a specific Council, although this power has not yet been exercised.

This limit includes a "cushion" to allow for the non-repayment of any borrowing at the required time and headroom for rescheduling of debts (i.e. borrowing new money in advance of repayment of existing). This was not required during the quarter.

Maturity structure of fixed interest rate borrowing (Upper Limit) As the Council does not borrow at variable rates of interest, the upper limit on this type of debt will always be nil, therefore no table has been produced for variable interest rate borrowing.

Investment Treasury Indicator and Limit - total principal funds invested for greater than 365 days. These limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment and are based on the availability of funds after each year-end.

There were no investments made for a period of greater than 365 days as of 30 September 2023.

Prudential Indicators	2023/24 Budget £'000	30.09.23 Actual £'000
Capital expenditure – Original **Capital expenditure – Revised**	46,479 29,450	4,738
Capital Financing Requirement (CFR)	703,066	703,066
In-year borrowing requirement	7,603	7,603

Capital Expenditure – This prudential indicator is a summary of the Council's capital expenditure plans, and financing requirements. Any shortfall of resources results in a funding borrowing need.

The Council's borrowing need (the Capital Financing Requirement) - The Council's Capital Financing Requirement (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 underlying borrowing need. Any capital expenditure, which has not immediately been paid for, will increase the CFR.

The CFR does not increase indefinitely, as the Minimum Revenue Provision (MRP) is a statutory annual revenue charge which broadly reduces the borrowing need in line with each asset's life and so charges the economic consumption of capital assets as they are used.

The CFR includes any other long-term liabilities (e.g. PFI schemes, finance leases). Whilst these increase the CFR, and therefore the Council's borrowing requirement, these types of schemes include a borrowing facility and so the Council is not required to separately borrow for these schemes. The Council currently has no such schemes.

In-year borrowing requirement for non-financial investments is any capital expenditure that has not been financed in the year.

APPENDIX B

Borrowings as of 30 Sep 2023

	Principal Sum £'000	Original Term (Years)	Annual Interest £	MATURITY	%
Housing Revenue Account					
PWLB - 500495	10,000	15	301,000	28 Mar 2027	3.01%
PWLB - 500498	10,000	20	332,000	29 Mar 2032	3.32%
PWLB - 500500	10,000	20	332,000	29 Mar 2032	3.32%
PWLB - 500501	10,000	20	332,000	29 Mar 2032	3.32%
PWLB - 500493	10,000	25	344,000	27 Mar 2037	3.44%
PWLB - 500496	10,000	25	344,000	27 Mar 2037	3.44%
PWLB - 500503	10,000	25	344,000	27 Mar 2037	3.44%
PWLB - 500494	10,000	30	350,000	28 Mar 2042	3.50%
PWLB - 500497	10,000	30	350,000	28 Mar 2042	3.50%
PWLB - 500499	10,000	30	350,000	28 Mar 2042	3.50%
	100,000		**3,379,000**	**Average Rate:**	**3.38%**
General Fund					
PWLB - 507919	10,000	5	195,000	17 Oct 2023	1.95%
Sheffield Combined Authority	5,000	2	25,000	19 Oct 2023	0.50%
PWLB - 507920	10,000	6	205,000	17 Oct 2024	2.05%
PWLB - 504312	10,000	10	256,000	17 Aug 2025	2.56%
PWLB - 506855	10,000	10	219,000	23 Jan 2028	2.19%
PWLB - 505012	4,000	12	86,400	08 Jun 2028	2.16%
PWLB - 507919	6,000	9	150,000	22 Dec 2028	2.50%
PWLB - 504520	15,000	15	414,000	04 Dec 2030	2.76%
PWLB - 176998	10,000	11	226,000	30 Mar 2031	2.26%
PWLB - 410351	10,000	11	167,000	28 Sep 2032	1.67%
PWLB - 505233	10,000	30	244,000	12 Jul 2046	2.44%
Phoenix Life Limited	38,900	40	1,125,858	02 May 2061	2.88%
PWLB - 505335	20,000	45	376,000	01 Sep 2061	1.88%
PWLB - 508328	10,000	43	247,000	31 Dec 2061	2.47%
PWLB - 508377	10,000	43	249,000	18 Jan 2062	2.49%
PWLB - 505968	15,000	45	351,000	04 Apr 2062	2.34%
PWLB - 505969	15,000	45	351,000	04 Apr 2062	2.34%
PWLB - 505972	20,000	46	470,000	05 Apr 2063	2.35%
PWLB - 505433	10,000	47	207,000	29 Sep 2063	2.07%
PWLB - 508192	10,000	45	243,000	12 Dec 2063	2.43%
PWLB - 508226	10,000	45	239,000	13 Dec 2063	2.39%
PWLB - 505434	14,000	48	289,800	29 Sep 2064	2.07%
PWLB - 505668	20,000	48	514,000	20 Jan 2065	2.57%
PWLB - 507420	40,000	47	980,000	29 May 2065	2.45%
PWLB - 507145	10,000	48	228,000	27 Mar 2066	2.28%
PWLB - 507416	40,000	48	984,000	25 May 2066	2.46%
PWLB - 505611	20,000	50	524,000	16 Dec 2066	2.62%
PWLB - 506991	10,000	50	240,000	05 Mar 2067	2.40%
PWLB - 507425	20,000	49	480,000	30 May 2067	2.40%
PWLB - 506125	10,000	50	230,000	12 Jun 2067	2.30%
PWLB - 506887	15,000	50	367,500	08 Feb 2068	2.45%
PWLB - 506888	15,000	50	367,500	08 Feb 2068	2.45%
PWLB - 507407	20,000	50	490,000	23 May 2068	2.45%
PWLB - 177081	40,000	50	932,000	30 Mar 2070	2.33%
PWLB - 434500	10,000	50	167,000	09 Nov 2071	1.67%
	542,900		**12,673,058**	**Average Rate:**	**2.33%**
Total Borrowings	**642,900**		**16,052,058**	**Annual Interes**	**2.50%**
	£'000				
Authorised Borrowing Limit 2022/23	700,613	(approved 09 Feb 2023 - Full Council)			
Borrowing to date	(642,900)				
Authorised Borrowing remaining	**57,713**				

APPENDIX C

Investments as of 30 Sep 2023

	£'000		ORIGINAL TERM	MATURITY	%
Banks					
Term Deposits					
Sumitomo Mitsui Banking Corp (SMBC)	4,000		3 mth	04 Oct 2023	5.460
Qatar National Bank	1,000		6 mth	06 Oct 2023	5.020
GoldmanSachs International Bank	5,000		6 mth	11 Oct 2023	4.700
Handelsbanken	5,000		3 mth	17 Oct 2023	5.370
DBS Bank	1,000		9 mth	20 Nov 2023	4.450
National Bank of Kuwait	5,000		3 mth	29 Dec 2023	5.400
Overseas-Chinese Banking Corp (OCBC)	3,000		5 mth	08 Jan 2024	5.600
National Bank of Canada	1,000		6 mth	08 Feb 2024	5.620
Al Rayan Bank	5,000		6 mth	09 Feb 2024	5.410
Certificates of Deposit					
NatWest Bank	1,000		9 mth	17 Nov 2023	4.340
Lloyds Bank Plc	5,000		5 mth	11 Dec 2023	5.950
Danske Bank A/S	1,000		4 mth	08 Jan 2024	5.740
Toronto Dominion Bank	2,000		1 yr	12 Apr 2024	5.100
Standard Chartered Bank	3,000		1 yr	12 Apr 2024	5.040
Skandinaviska Enskilda Banken (SEB)	2,000		1 yr	12 Apr 2024	5.040
Total Banks	**44,000**	**58%**			
Building Societies					
Nationwide BS	3,000		3 mth	25 Oct 2023	5.270
Leeds BS	3,000		3 mth	17 Nov 2023	5.310
Total Building Society	**6,000**	**8%**	(50% Limit)		
Local Authorities					
London Borough of Newham	5,000		3 mth	17 Nov 2023	5.350
Total Local Authorities	**5,000**	**7%**			
Money Market Funds					
Aberdeen Liquidity Sterling Fund	3,000		********** On Call **********		Variable
Aviva Investors Sterling Liquidity Fund - Class 3	10,000		********** On Call **********		Variable
Insight Liquidity Fund PLC	4,000		********** On Call **********		Variable
Total Money Market Funds	**17,000**	**22%**			
Pooled Funds & Collective Investment Schemes					
CCLA Property Fund	2,000		**** 3 mth settlement ****		Variable
CCLA Diversified Income Fund	2,000		**** 3 mth settlement ****		Variable
Total Pooled Funds	**4,000**	**5%**			
Funding Circle					
Lending to small and medium sized companies	28		**** up to 5 years ****		Variable
Total Other Investments	**28**	**0%**	(with the ability to sell loans)		
Total Investments	**76,028**				

Investment Property Performance Indicators 2023/24 as of 30 September 2023

Revenue and Tenancy Management Performance

The following indicators measure the revenue performance and tenancy management performance of the Council's investment Properties.

KPI	Metric Description	YTD 30/09/2023 £
Investment Property budget variance	Increased Income Increased Expenditure	152,000 (107,000)
	Net Surplus / (Deficit)	45,000

KPI	Metric Description	YTD 30/09/2023
Income Return (Proportionality)	Investment income as a percentage of all general fund income (excluding Taxation)	42%
Investment Property Rent Arrears	As a percentage of the total portfolio income – taken prior to Quarterly due dates	3.31%
Vacancy Rates	As a percentage of the total portfolio area in SQ FT	7.54%
Tenant Retention	Number of renewals completed, and tenant breaks not exercised	78%

A breakdown of the changes in income and expenditure changes can be found in the Financial Monitoring Statement report to on the November 2023 Corporate Management Committee agenda.

Capital & Treasury Performance

KPI	Metric Description	31 March 2023
Capital Values	Difference in Capital Valuations annually. (March 2022 – March 2023)	- £24.8m
	Difference in Capital Valuations since purchase/construction	+ £13.3m
Loan to Value ratio	Amount of debt compared to the total asset value	97.5%
Interest cover ratio	The total net income from property investments compared to the total interest on associated borrowings	2.45 times
Debt cover ratio	The total net income from property investments compared to the total annual MRP and interest on associated borrowings	1.84 times
Average return on investments	Rental income divided by Capital Value	5.1%

There have been no changes to borrowing or interest payments during the first half of the year.

With regard to the Capital Values; the figures of -£24.8M reflects the fact that our investment property portfolio is heavily weighted in the office sector (approximately 64%), the majority of which have a shortening income profile which in turn leads to a yield swing affecting the capital return. The office sector has undergone a significant shift since October 2022 with persistent high inflation, interest rate hikes and volatility in the financial sector causing investor caution which adds to cautious valuations. In addition to the challenging market conditions particularly in the Southeast office sector, occupation activity remains sensitive to economic headwinds which include rising energy costs, the new rates revaluation, and ongoing build-cost inflation which have impacted the all-in occupational cost of space which has resulted in occupiers taking less space.

APPENDIX E

Economic Commentary provided by Montagu Evans LLP

HIGH-STREET RETAIL

The High Street sector's difficult set of challenges during, and off the back of the pandemic were well-documented as many retailers on the high street were not able to trade during the mandatory national lockdowns, revenues dramatically decreased. Retailer's online platforms boomed throughout this period as a result of changing consumer patterns which have now settled into an established alternative to in-store retail with a broader consumer base.

The road to recovery, since the Covid era, has not been easy with retailers facing a combination of new challenges including the cost-of-living crisis, high wage inflation, industrial action and rapidly increasing energy bills with weaning government support. The combination of these challenges in addition to decreased consumer confidence has led to considerable volatility in the relationship between in-store and online retail.

Wilko went into administration in August this year, which is the first major insolvency for the sector since M&Co in early February. The discount retailer employed 12,500 staff across 400 stores and two distribution warehouses. However, B&M have recently announced they will take on up to 51 of Wilko's stores.

Whilst the Christmas trading period proves to be an inkling of reassurance, the agility of retailers is being tested as to how effectively and quickly they can adapt to the cost-of-living crisis and bolster cash flow strength. Retailers are being forced to diversify and make strategic decisions, focussing on customers, going green and adapting to other new market trends.

Key Statistics

- In July 2023, UK retail footfall was 2.1% higher than the same month in 2022, according to MRI Springboard data.
- Retail investment volumes totalled £6.4 billion in the year to Q2 2023, compared to £7.2 billion in the year to Q1 2023
- Retail capital values declined in July 2023 with the MSCI index falling by 0.32% month-on-month, compared to a fall of 0.11% in June 2023.
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RETAIL WAREHOUSES

The UK retail warehouse market has shown resilience despite economic challenges. Consumer demand for big-ticket items has decreased. However, the market has shifted away from bulky goods, with grocery now occupying a significant share of retail warehouse stock. Discount homeware brands and value-oriented operators have grown, making the market less vulnerable to economic downturns. Essential product categories are the focus, mitigating the impact of reduced discretionary spending. Consumers are cutting non-essential spending and opting for value products, with essential spend rising. Grocery, an essential sub-category, has seen consistent spending growth.

The UK's retail warehouse investment market has recently witnessed fluctuations in yields, primarily attributed to the escalation of interest rates and shifts in investor sentiment. The market's stability hinges on the robustness of the occupational sector, which has demonstrated impressive resilience despite disruptions caused by events like the pandemic and the Ukraine conflict.

Factors such as low vacancy rates, strong retailer performance, and consistent net effective rents averaging around £18 per square foot contribute to this stability. There is also discussion over whether market rents on prime assets are artificially low, as retailers prefer lease renegotiations over vacating premises. Furthermore, competitive tension persists, but some investors may not fully appreciate the fundamental strength of the occupational market, resulting in yield movements that align with changes in interest rates and UK Bond yields.

The outlook for the future is looking more stable and the sector has repriced to a sensible level following the rise in debt costs over the last year and is once more seemingly well-priced versus other asset classes. The occupational market remains strong in so much as it is broadly fully let despite the recent Wilko administration in August 2023.

Key Statistics

- Vacancy rates were 5.4% in the summer months of 2022 and have fallen to 4.7% despite seeing Wilko go into administration.
- Prime Open A1 yields started the year at 5.50%. Currently, they sit at 5.75%.
- H1 has seen a total of £1.1bn in retail warehouse transactions, -13.5% down on H2 2022, and -17.9% down on the same period last year.

INDUSTRIAL

The first half of 2023 had the lowest take-up since 2013, but there's optimism for a rise in the second half. Investment volumes in the industrial sector reached £10.5 billion in the year to Q2 2023. This was down from £11.8 billion in the year to Q1 2023. Market sentiment remains uncertain due to economic data fluctuations, particularly regarding inflation and base rates, with further base rate increases expected. Investment volumes in H1 2023 reached £0.99bn, marking a 79% decline from H1 2022, especially affecting the logistics sector.

The MSCI industrial rental growth index grew by 0.40% month-on-month in July 2023, compared to growth 0.59% in June 2023. This was the strongest rental growth from the main sectors but marks a slowdown on last summer. Back in June 2022 industrial rental growth stood at 1.1%.

Online retail is forecasted to reach 35% by 2027, driven by fashion, food, and electronics. Manufacturing occupiers are seeking supply chain diversification, albeit at a gradual pace. With the UK's population expected to reach 71 million by 2023, there's a need for 224 million sq ft of additional warehouse space to accommodate housing requirements.

The sector remains a robust asset class and going forwards, the outward movement of yields and re-pricing of assets is predicted to encourage investor activity as buyer and seller intentions become more closely aligned.

Key Statistics

- Take-up across the UK for Grade A space over 100,000 sq ft reached circa 8 million sq ft in Q1 2023, which is 49% higher compared to the same period last year and 13% ahead of the 5-year quarterly average.
- H1 2023 saw a 79% decline in investment volumes compared to H1 2022, mainly impacting the logistics sector.
- Capital Availability: Equity raising has risen by 92% since 2019, with £667bn available in unlisted funds for real estate investment.

OFFICE

Occupiers are continuing to assess their occupational need as the widespread pandemic-driven hybrid working model transitions into the post-covid working environment. For some, this has seen a return to the office full time whereas as others have chosen to retain remote and flexible working options.

In the post-COVID era, offices remain essential, but tenant preferences are changing rapidly. They seek high-quality, well-located, sustainable buildings to attract and retain talent, willing to pay more for such spaces. These features enhance productivity, operational efficiency, and reduce carbon emissions. This shift is reshaping the risk-reward dynamics for investors as most existing office spaces don't meet these requirements, and supply is limited. Best-in-class, Grade A spaces are likely to fare better amid rising costs and a demand-supply imbalance caused by reduced development activity.

Moving forward, the onus is upon occupiers to decide upon their working models which often relates to the recruitment and retention of top talent and productivity targets. Reduced utilisation rates for those who do retain remote working will continually require assessment of where excess space can be limited to optimise portfolios. Focus on asset's ESG credentials will only intensify with the proximity to statutory dates.

Key Statistics

- Office rental growth contracted marginally in July 2023, with MSCI Market Rental Growth Index for offices recording growth of 0.17%, compared to a rise of 0.31% in June 2023.
- The MSCI Capital Growth Index for offices decreased by 2.14% month-on-month in July 2023, compared to the June 2023 figure of -2.17%.