Audit, Risk & Assurance Committee

Date	4th December 2023
Report title	Treasury Management Mid-Year Report 2023/24
Portfolio Lead	Cllr Bob Sleigh OBE
Accountable Chief Executive	Laura Shoaf Chief Executive Email: Laura.Shoaf@wmca.org.uk Tel: 0121 214 7444
Accountable Employee	Linda Horne WMCA Executive Director of Finance and Business Hub Email: Linda.Horne@wmca.org.uk
Report has been considered by	Not Applicable

Recommendation(s) for action or decision:

ARAC is recommended to:

1 Note the report.

1. Introduction

1.1 The report has been written in accordance with the requirements of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised 2021). The primary requirements of the Code are as follows:

1. Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Authority's treasury management activities.
2. Creation and maintenance of Treasury Management Practices which set out the manner in which the Authority will seek to achieve those policies and objectives.
3. Receipt by the full Board of 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.
4. Delegation by the Authority of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.
5. Delegation by the Authority of the role of scrutiny of treasury management strategy and policies to a specific named body. For this Authority the delegated body is the Audit, Risk, and Assurance Committee:

1.2 This mid-year report has been prepared in compliance with CIPFA's Code of Practice on Treasury Management, and includes the following:

- A review of the Authority's investment portfolio for 2023/24;
- A review of the Authority's borrowing strategy for 2023/24;
- A review of any debt rescheduling undertaken during 2023/24;
- A review of compliance with Treasury and Prudential Limits for 2023/24;
- Outlook for remainder of 2023/24.

2. Treasury Management Mid-Year Review 2023/24

2.1 Table 1 shows WMCA borrowing and investments held at 1 April 2023 and 30 September 2023. It shows that net investments have increased by £153.9m mostly as a result of grants being received in advance of need as documented below.

	April 2023 £m	**Change**	**Sept 2023 £m**	**Notes**
Borrowing	(507.9)	(89.9)	(597.8)	Drawdown of Phoenix Group £100m loan, August 2023
Investments	712.0	243.8	955.8	Receipt of government grants in advance of expenditure (AEB, CRSTS)
Net Investments	**204.1**	**153.9**	**358.0**	

3 Borrowing Activity

3.1 As notified in previous reports, to unwind a proportion of it's historic under borrowed position and to mitigate against increases in interest rates, the Authority arranged a forward-dated loan of £100m with Phoenix Group in February 2022. The cash drawdown date was set at 1 August 2023, but the interest rate was set as at commercial terms as of the agreement date (1 February 2022.) In comparison with the equivalent PWLB rate for this loan on 1 August 2023 WMCA has gained a notional interest saving of £91m over the term of the loan. The cash was drawn down per schedule and is linked specifically to service the existing capital financing requirements of the Investment Programme.

3.2 It is not anticipated that any further borrowing activity will take place during financial year 2023/24. WMCA's central strategy - as set out in the Treasury Management Strategy approved by Board in February 2023 - is to defer further borrowing whilst PWLB rates remain elevated.

4 Historic Borrowing

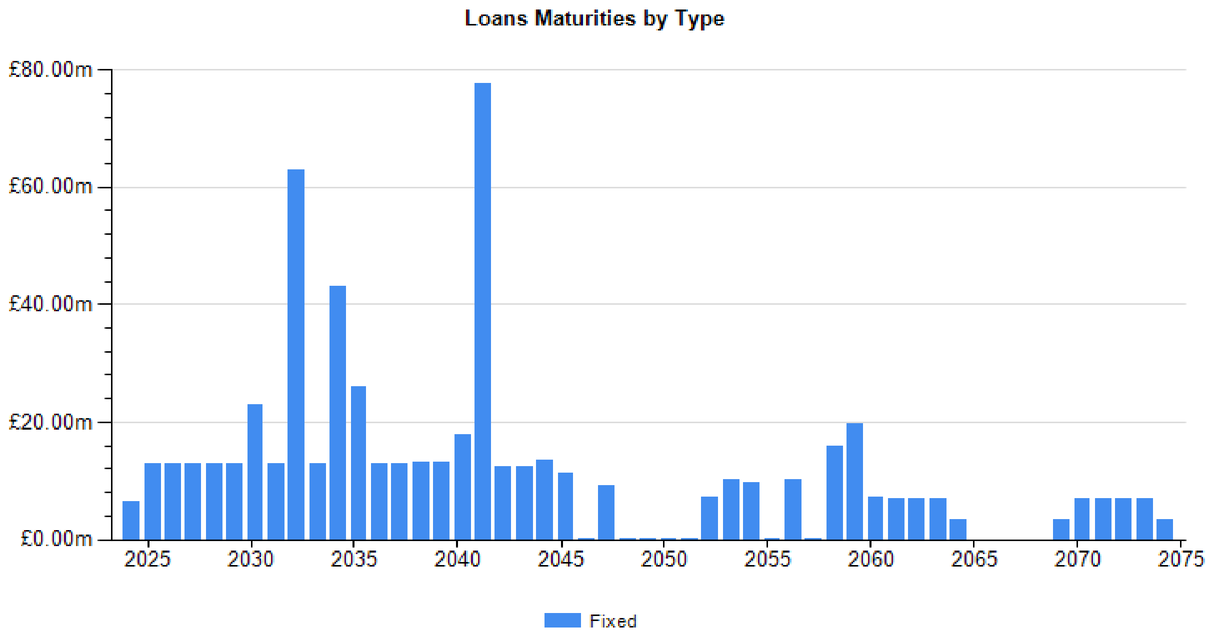
4.1 The main source of historic borrowing for WMCA has been the Public Works Loans Board (PWLB). The Director of Finance continues to review the opportunities to reschedule debt and works closely with specialist treasury advisors to explore alternative best value borrowing options. No rescheduling has taken place to date in 2023/24. However, now that the whole of the yield curve has shifted higher there may be better opportunities in the future, although only prudent and affordable debt rescheduling will be considered.

4.2 Table 2 provides a breakdown of borrowing held at 1st April 2023 and 30th September 2023. It shows that borrowing has increased by £89.9m due to the uptake of a £100m Phoenix Group loan (see 3.1) offset by annuity and EIP principal repayments on PWLB and UKIB loans during the year. The average interest rate for the portfolio as at 30th September is 2.93%.

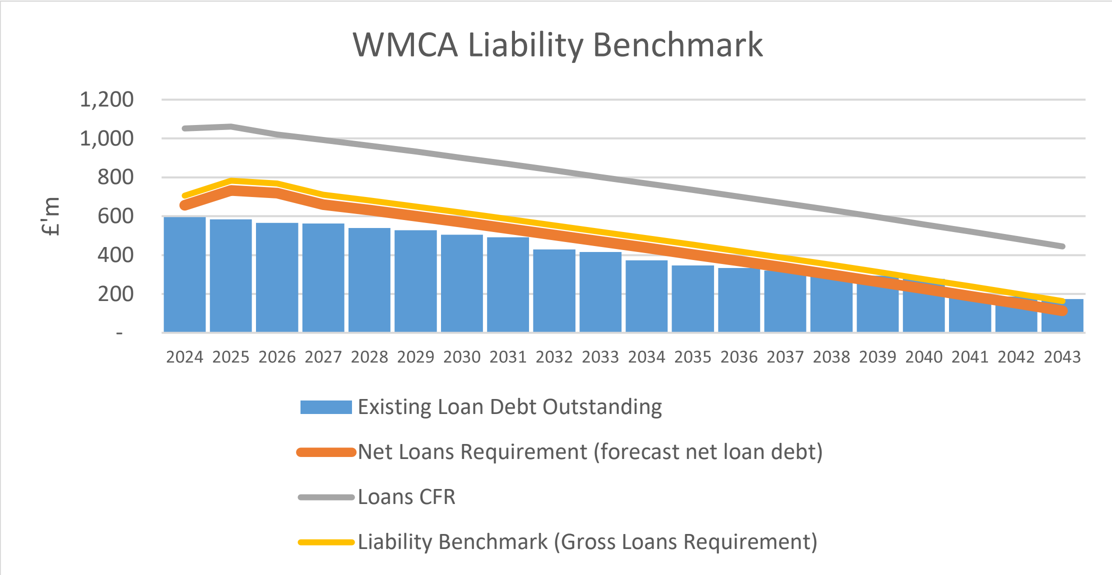
	Balance at 1 April 2023 £m	**Repaid in Year £m**	**Raised in Year £m**	**Balance at 30 Sept 2023 £m**
PWLB	488.3	9.9	-	478.4
Phoenix Group	-	-	100.0	100.0
Barclays	10.00	-	-	10.00
UKIB	9.6	0.2	-	9.4
Total Long-Term Borrowing	**507.9**	**10.1**	**100.0**	**597.8**

5 Liability Benchmark

5.1 The chart below outlines the maturity profile of existing WMCA debt. The next significant single maturity will occur in 2032 with sporadic maturities from that point onwards. The maturity profile is important for WMCA to monitor refinancing risk – that is, to ensure when new debt is taken out sufficient gaps are maintained between maturities to aid cash planning. It is possible that upon maturing, WMCA will need to re-finance the debt, but these decisions will be taken at the point of maturity, influenced by available cash levels and the prevailing rates of interest at the time.



5.2 In consideration of its borrowing strategy WMCA also has regard to its **liability benchmark**, a mandatory indicator as prescribed by the CIPFA Treasury Management Code of Practice. This plots the expected path of its Capital Financing Requirement (CFR or, underlying need to borrow) over time and then overlays with minimum revenue provision (sums set aside for the repayment of debt), cash backed balances and the existing debt profile. The outcome produces a benchmark for new borrowing/refinancing which can be assessed against interest rate forecasts for sensitivity. The chart below shows WMCA's revised benchmark for 2023/24 onwards which is heavily influenced by the borrowing need arising from the WMCA Investment Programme as per the first devolution deal in 2016:



6. Investment Activity

6.1 For the period 1st April 2023 to 30 September 2023, all short-term investments have given a return to the Authority of **£15.026m**. All treasury management activities undertaken during the year complied with the Annual Investment Strategy (contained within the Treasury Management Strategy Statement) approved by WMCA Board in February 2023. Investments are placed directly with financial institutions, or using various money market brokers: IdealTrade.net, ITS, Tradition, Tullet Prebon, Martin Brokers, BGC and King & Shaxson.

6.2 In August 2023, in light of press coverage regarding WMCA's deposits with Woking Borough Council and the more widely reported funding issues at various local authorities Treasury Management Group (TMG) met and adopted the following operating restrictions on future investments with counterparties:

- No forward dated trades beyond 1 month ahead;
- Increase in rolling 3 month liquidity requirement from £20m to £50m; and
- Review of internal benchmark range of counterparty financial performance prior to trade agreements

These restrictions will be reviewed at future TMG meetings and are made under the following criteria within the approved Annual Investment Strategy:

"Other information on the security of investments: WMCA understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may otherwise meet the above criteria."

6.3 Table 3 below shows investments currently held with authorities that have issued Section 114 notices. Where S114 notices are in place no further investments will be placed with that authority. Officers at Woking Borough Council and Birmingham City

Council have provided written assurance that fixed term deposits will be repaid on the specified maturity dates.

Local Authority	Start Date	Maturity Date	Principal Outstanding / Value £m
Woking BC	25/04/2023	25/01/2024	5
Woking BC	25/04/2023	23/04/2024	5
Woking BC	19/07/2023	17/07/2024	5

Birmingham CC	27/10/2023	29/07/2024	15
Birmingham CC	29/07/2024	23/01/2025	10

6.4 Following a review of compliance limits in September 2023 a control failure within the authority's Treasury Management software was discovered which impacted on the operating parameters for loan limits with counterparties. A software update has now taken place to ensure systems are operating as intended with additional measures incorporated to strengthen reporting, segregation of duties, and protocols/procedures for system changes and updates in future.

6.5 Table 4 below shows investments (excluding strategic investments) held **as at the 30 September 2023** totalled £955.8m, split into the following categories:

Class	Principal Outstanding £m	Average Return %
Fixed Term Deposits	921.1	3.85
Money Market Funds	34.0	5.23
Bank Call Accounts	0.7	5.25
Total Investments	**955.8**	

A detailed list of all current (as at 30th September) and committed future investments is included at Appendix A. Fixed term deposits are placed across 55 local authorities and 9 banks/financial institutions.

6.6 The interest rate environment remained volatile over the first half of the financial year. In April base rate was at 4.25% with market expectations of one further rise in 2023; by June base rate had risen to 5.00% with market expectations rising to 6.25% by the close of the year; by late September base rate had risen to 5.25% but market expectations had cooled with no more than a 50% probability of a further rise.

6.7 Within the Annual Investment Strategy set out to Board in February 2021 it was noted that "*WMCA will continue to diversify into more secure and/or higher yielding asset classes during 2021/22. This is especially the case for the estimated £10m that is available for longer-term investment to ensure MiFID compliance."* Following evaluation of applicable investment products, WMCA has placed two strategic investments totalling £5m in 2021 with the CCLA Local Authority Property Fund (LAPF) and Fundamentum

Social Housing REIT. Dividend yields are c4.4% and c3.8% respectively. The investment horizon for these funds is set at a minimum of five years.

7 Performance measurement and Treasury Indicators

7.1 The WMCA treasury management function participates in benchmarking which compares WMCA's treasury management performance with other Local Authorities, to ensure that relative to other local authorities the Authority is achieving a fair investment return without any undue risk. Performance is also regularly reviewed at the monthly Treasury Management Group.

7.2 The Treasury Management Strategy approved by WMCA Board in February agreed a number of Treasury Management Indicators which as at the mid-year point have all been complied with as follows:

Indicator	Target	Status
Credit Risk	A Minus	Green
Liquidity Risk[1]	£20m Minimum	Green
Price Risk	< £25m invested longer than 1 year	Green
Refinancing Risk	Under 1year 75% Max 1 to 2 Years 50% Max 2 to 5 years 70% Max 5 to 10 Years 70% Max 10 Years and Over 70% Max	Green

1 Now increased to £50m (see section 6.2)

7.3 In addition to the above, compliance with the debt limit(s) is confirmed. WMCA debt stands at £597.8m following the uptake of a £100m Phoenix Group loan during the financial year. For clarity, the published operational and authorised limits for debt are £1,032m and £982m respectively. WMCA also has approval from HM Treasury (HMT) and Department for Levelling Up, Housing and Communities (DLUHC) to borrow for all its functions subject to operating within an agreed debt cap. The cap for 2023/24 is set at £1,234m and for 2024/25 is £1,277m.

7.4 In summary, the Section 151 Officer can confirm that all treasury management activities undertaken during the first half year complied fully with the CIPFA Code of Practice and the WMCA Treasury Management Strategy.

8 Borrowing Update

8.1 WMCA are closely monitoring external debt markets and developing appropriate debt strategies in light of the need to fund the Investment Programme over the Medium-Term Financial Plan timeline. The anticipated debt requirement published within the 2023/24 Treasury Management Strategy was as follows:

2022/23 TM Strategy	2023/24 £m	2024/25 £m	2025/26 £m	2026/27 £m
Forecast New Debt	100	-	-	-

8.2 As indicated in 3.2, after the uptake of £100m Phoenix Group borrowing in August 2023 no further borrowing is anticipated in year. Further, following the re-forecasting of the capital programme in 2023/24 and in combination with the continuing significant level of grants received in advance, it remains the central case that no further borrowing will need to be undertaken during the period of the current medium term financial plan. Consequently, WMCA will only look to borrow where there is a clear and obvious need with affordability and the "cost of carry" remaining the key influences on WMCA's borrowing strategy.

8.3 Market debt alternatives remain available to WMCA; however, the financial strength of individual authorities will be scrutinised by investors and commercial lenders.

9. **Economic Update**

9.1 The most recent economic forecast (25th September 2023) from our independent treasury advisors, Link Group, sets out the view that short, medium, and long-dated interest rates will be elevated for some little while, as the Bank of England seeks to squeeze inflation out of the economy:

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

9.2 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).

9.3 As the growing drag from higher interest rates intensifies over the next six months, the economy is likely to continue to lose momentum and potentially 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. The Bank of England is expected 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.