For Publication

Bedfordshire Fire and Rescue Authority
31 October 2022

REPORT AUTHORS: **CHIEF FIRE OFFICER AND TREASURER**

SUBJECT: **TREASURY MANAGEMENT – MID-YEAR REVIEW REPORT TO 30 SEPTEMBER 2022**

For further information on this Report contact:

Mr G Chambers
Assistant Chief Officer/Treasurer
Tel No: 01234 845000

Background Papers:

Treasury Management Strategy 2022/23, as detailed in the Budget Book 2022/23.

Implications (tick ✓):

LEGAL		FINANCIAL	✓
HUMAN RESOURCES		EQUALITY IMPACT	
ENVIRONMENTAL		POLICY	
ORGANISATIONAL RISK		CORE BRIEF	
		OTHER (please specify)	

Any implications affecting this report are noted at the end of the report.

PURPOSE:

To provide an update on the Authority's Treasury Management to 30 September 2022.

RECOMMENDATION:

That the Fire and Rescue Authority consider and comment on the report.

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1. Introduction

1.1 Since 1 April 2006, the management of the Fire and Rescue Authority's (FRA) Treasury operations has been undertaken by the Authority's Finance staff. Treasury management activities are undertaken with the objective of maximising return/minimising cost, consistent with minimising risk. When investing, the over-riding principle is the maintenance of the capital sum.

In order to support this function, the Authority also employs Link Asset Services to provide independent, professional treasury advice.

1.2 The FRA's banking facilities are also arranged and monitored by the Finance staff.

1.3 The FRA adopted the Code of Practice for Treasury Management in the Public Services published by the Chartered Institute of Public Finance and Accountancy (CIPFA), revised in 2017. One of the requirements of the CIPFA Code is for there to be regular reports on Treasury Management to be presented to the appropriate 'committee'. This is the mid-year Review Report for 2022/23 to 30 September 2022.

1.4 The FRA is asked to note the report, as there are no changes requested to the Prudential Indicators, approval is not required by the FRA.

2. Treasury Management Reports

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

- A review of the Treasury Management Strategy Statement and Annual Investment Strategy;
- The Authority's capital expenditure (prudential indicators);
- A review of the Authority's investment portfolio for 2022/23;
- A review of the Authority's borrowing strategy for 2022/23;
- A review of any debt rescheduling undertaken (if applicable) during 2022/23;
- A review of compliance with Treasury and Prudential Limits for 2022/23; and
- An economic update for the first six months of 2022/23.

3. Treasury Management Training

3.1 The Responsible Officer (the Section 151 Officer) must ensure that Group/FRA Members tasked with treasury management responsibilities, including those responsible for scrutiny, have access to training relevant to their needs and those responsibilities.

3.2 Training was provided to Members by our Treasury Advisor's, Link Asset Services in July 2022, this can again be arranged at the Members request and is recommended by the Treasurer.

4. Treasury Management Strategy Statement (TMSS) and Annual Investment Strategy Update

For the current year, these were approved by the FRA on 24th March 2022. There are no policy changes to the TMSS, the details in this report update the position in the light of the updated economic position and budgetary changes already approved.

5. Authorities Capital Position (Prudential Indicators)

This part of the report is structured to update:

- Capital expenditure plans

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

5.1 Prudential Indicator for Capital Expenditure

This table shows the revised estimates for capital expenditure and the changes since the capital programme was agreed at the Budget.

Capital Expenditure by Service	**2022/23 Original Estimate £'000**	**Current Position £'000**	**2022/23 Revised Estimate £'000**
As per Budget Book	1,357	532	876

5.2 Changes to the Financing of the Capital Programme

The table below draws together the main strategy elements of the capital expenditure plans (above), highlighting the original supported and unsupported elements of the capital programme, and the expected financing arrangements of this capital expenditure. The borrowing element of the table increases the underlying indebtedness of the Authority by way of the Capital Financing Requirement (CFR), although this will be reduced in part by revenue charges for the repayment of debt (the Minimum Revenue Provision). This direct borrowing need may also be supplemented by maturing debt and other treasury requirements.

Capital Expenditure	2022/23 Original Estimate £'000	2022/23 Revised Estimate £'000
Total Capital Expenditure	1,357	1,357
Financed by:		
Capital receipts	35	7
Capital grants	0	0
Capital reserves	453	0
Revenue	869	869
Total financing	**1,357**	**876**
Borrowing Requirement	0	0

5.3 **Changes to the Prudential Indicators for the Capital Financing Requirement (CFR), External Debt and the Operational Boundary**

The table below shows the CFR, which is the underlying external need to incur borrowing for a capital purpose. It also shows the expected debt position over the period, which is termed the operational Boundary.

Prudential Indicator – Capital Financing Requirement

We are on target to achieve the original forecast Capital Financing Requirement.

Prudential Indicator – the Operational Boundary for external debt

	2022/23 Original Estimate £’000	**Current Position £’000**	**2022/23 Revised Estimate £’000**
Prudential Indicator – Capital Financing Requirement			
TOTAL CFR	**7,273**	**7,273**	**7,273**
Net movement in CFR	**(233)**	**(233)**	**(233)**
Prudential Indicator – the Operational Boundary for external debt			
Borrowing	9,987	9,987	9,987
Other long term liabilities*	0	0	0
Total debt (year end position)	**9,987**	**9,987**	**9,987**

5.4 Limits to Borrowing Activity

The first key control over the treasury activity is a prudential indicator to ensure that over the medium term, net borrowing, (borrowings less investments) will only be for a capital purpose. Gross external borrowing should not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional CFR for 2022/23 and next two financial years. This allows some flexibility for limited early borrowing for future years. The Authority has approved a policy for borrowing in advance of need which will be adhered to if this proves prudent.

	2022/23 Original Estimate £’000	Current Position £’000	2022/23 Revised Estimate £’000
Borrowing	9,987	9,987	9,987
Other long term liabilities	0	0	0
Total debt	**9,987**	**9,987**	**9,987**
CFR* (year end position)	**7,040**	**7,040**	**7,040**

The Treasurer reports that no difficulties are envisaged for the current future years in complying with this prudential indicator.

A further prudential indicator controls the overall level of borrowing. This is the Authorised Limit which represents the limit beyond which borrowing is prohibited, and needs to be set and revised by Members. It reflects the level of borrowing which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. It is the expected maximum borrowing need with some headroom for unexpected movements. This is the statutory limit determined under section 3(1) of the Local Government Act 2003.

Authorised limit for external Debt	2022/23 Original Indicator £’000	Current Position £’000	2022/23 Revised Indicator £’000
Borrowing	9,987	9,987	9,987
Other long term liabilities	2,200	2,200	2,200
Total	**12,187**	**12,187**	**12,187**

6. Borrowing/Investment Strategy for 2022/23

6.1 It was anticipated at the beginning of 2022/23 that the Authority would have surplus funds available for short-term investment, either within its Special Interest Bearing Account (SIBA) at its bankers or through the money market. As at the 30th September 2022 the SIBA account is paying a rate of 0.30%.

6.2 The Authority's call-account with Barclays Bank has been used during 2022/23. As at the 30th September 2022 the Barclays account is paying a rate of 1.81% (between £750K-£3M)

6.3 This Authority's 120-Day Interest account with Santander has been used during 2022/23. As at the 30th September 2022 this account is paying a rate of 1.18% as notice for withdrawal has been given.

6.4 This Authority's 180-Day Interest account with Santander has been used during 2022/23. As at the 30th September 2022 this account is paying a rate of 1.21% as notice of withdrawal has been given.

6.5 The Authority had three fixed term deposits maturing during the first half of 2022/23. One with Goldman Sachs (£2M) and two with Qatar National Bank (£2.25M and £2.5M). Six new fixed term deposits have been placed during the first half of 2022/23, via our Treasury Agents, Link Asset Services. Three are with First Abu Dhabi Bank for 9 months (£2M @ 1.81%), 1 year (£1M @ 2.24%) and six months (£2M @ 2.19%). Two are with Lloyds Corporate Bank for 6 months (£3M @ 1.67% and £2M @ 2.29%). The remainder deposit was placed with Standard Chartered Bank for 6 months (£4M @ 2.32%) in their sustainable fixed term deposit.

6.6 This Authority's 95-Day Interest account with Lloyds Bank has been used during 2022/23. However, funds were recalled and returned to us on 23rd May.

6.7 During the second half of 2022/23 this Authority will be considering using Money Market Funds for short-term investments. Operators use the credit ratings agencies which lay down investment restrictions to enable the funds to maintain its AAA status. Money Market Funds may also be governed by the Institutional Money Market Fund Association (IMMFA) which is a voluntary code of practice issued in 1992 by a trade body for Money Market Funds. This ensures all members offer a consistently high quality product by promoting best practice, transparency of fund values and a standardised format for published data.

6.8 Borrowing has not been undertaken in 2022/23 to finance the Capital Programme. The funding for the 2022/23 Capital Programme was through Reserves and Revenue contributions.

7. Interest Rate Movements During 2022/23

7.1 Bank base rate was 0.75% at the beginning of the year but by 22nd September had increased to 2.25%.

7.2 Interest rates applicable to temporary investments were short-term money market rates. These investments were fixed for a set period (between one month and one year), at a greater interest rate than bank base rate. During the first five months of 2022/23, three investments reached maturity, and then six were placed for a period between 6 months and 1 year. When placing these, a number of factors were considered, including cashflow, security, return etc in order to meet our Policies and at the same time get the best return.

8. Investment/Borrowing Operations

8.1 Investments:

Surplus cash is invested on a temporary basis through the money market. Levels of investment were £6.75M at the start of 2022/23 and increased to £14M as at 30th September 2022. In the year 2022/23 to 30th September 2022, £43,477 interest had been generated through these investments and through the local SIBA account, Barclays Account, Santander Accounts and Lloyds Account. Interest on PWLB borrowings totals of £210,817 will be paid on 30th September 2022. This will give a net interest paid position of £167,340 as at 30th September 2022.

8.2 The FRA's budgeted investment return (interest receivable) for 2022/23 was set at £65,400. However, due to the unexpected increase in Bank of England base rate this has been revised to an expected return of approximately £250,000 by 31st March 2023.

8.3 Long-Term Borrowing:

Debt rescheduling opportunities to date have been very limited in the economic climate given the consequent structure of interest rates, and following the increase in the margin added to gilt yields which has impacted PWLB new borrowing rates since October 2010. No debt rescheduling has therefore been undertaken to date in the current financial year.

Due to the current interest rates however, it may be possible to repay one of our PWLB loans resulting in a favourable position for the authority regarding revenue savings. We are now actively considering opportunities to do this and should a positive financial situation arise members will be asked to agree this course of action.

8.4 **Borrowing and Investments Outstanding:**

	Temporary Investments £000s	**Long-Term Borrowing £000s**
Outstanding at 1 April 2022	6,750	9,987
Raised	14,000	0
Repaid	6,750	0
Outstanding at 31 August 2022	**14,000**	**9,987**

NB – The Temporary Investments above do not include the balances from the Authority's bank Accounts

9. Performance Measurement

9.1 The success of cash flow management, and hence the Fire Authority's temporary investment and borrowing activity, is measured by comparing the actual rates of interest achieved and borne against a benchmark of the 7 day SONIA (Sterling Overnight Index Average) compounded rate.

9.2 For the period ending 31 August 2022, the average interest rate achieved from temporary investments, the SIBA Account, Barclays, Lloyds and Santander Accounts was 1.61%, higher than the average 7 day SONIA over the same period of 1.57%.

10. General Economic Conditions

10.1 In brief, the first five months of this financial year has seen:

- Inflation – Target Inflation (CPI) was at 6.20% on 1 April 2022 and at 10.10% by 31 August 2022 (+3.90% change).
- Headline Inflation (RPI) was at 8.20% on 1 April 2022 and at 12.30% by 31 August 2022 (+.4.10% change).

10.2 Economic Update - An economic update is provided at Appendix 1.

11. Economic Forecast – (Link Group Update 27th September 2022)

The Authority's Treasury Advisers, Link Asset Services, have provided the following forecast:

	End Q3 2022	**End Q4 2022**	**End Q1 2023**	**End Q2 2023**	**End Q3 2023**	**End Q4 2023**
Bank Rate	4.00%	5.00%	5.00%	5.00%	4.50%	4.00%
5yr PWLB rate	5.00%	4.90%	4.70%	4.50%	4.20%	3.90%
10yr PWLB rate	4.90%	4.70%	4.60%	4.30%	4.10%	3.80%
25yr PWLB rate	5.10%	4.90%	4.80%	4.50%	4.30%	4.10%
50yr PWLB rate	4.80%	4.60%	4.50%	4.20%	4.00%	3.80%

ANDREW HOPKINSON
CHIEF FIRE OFFICER

GAVIN CHAMBERS
TREASURER

Economic Update

Appendix 1

- The second quarter of 2022/23 saw:
  - GDP revised upwards in Q1 2022/23 to +0.2% q/q from -0.1%, which means the UK economy has avoided recession for the time being;
  - Signs of economic activity losing momentum as production fell due to rising energy prices;
  - CPI inflation ease to 9.9% y/y in August, having been 9.0% in April, but domestic price pressures showing little sign of abating in the near-term;
  - The unemployment rate fall to a 48-year low of 3.6% due to a large shortfall in labour supply;
  - Bank Rate rise by 100bps over the quarter, taking Bank Rate to 2.25% with further rises to come;
  - Gilt yields surge and sterling fall following the “fiscal event” of the new Prime Minister and Chancellor on 23rd September.
- The UK economy grew by 0.2% q/q in Q1 2022/23, though revisions to historic data left it below pre-pandemic levels.
- There are signs of higher energy prices creating more persistent downward effects in economic activity. Both industrial production (-0.3% m/m) and construction output (-0.8% m/m) fell in July 2022 for a second month in a row. Although some of this was probably due to the heat wave at the time, manufacturing output fell in some of the most energy intensive sectors (e.g., chemicals), pointing to signs of higher energy prices weighing on production. With the drag on real activity from high inflation having grown in recent months, GDP is at risk of contracting through the autumn and winter months.
- The fall in the composite PMI from 49.6 in August to a 20-month low preliminary reading of 48.4 in September points to a fall in GDP of around 0.2% q/q in Q3 and consumer confidence is at a record low. Retail sales volumes fell by 1.6% m/m in August, which was the ninth fall in 10 months. That left sales volumes in August just 0.5% above their pre-Covid level and 3.3% below their level at the start of the year. There are also signs that households are spending their excess savings in response to high prices. Indeed, cash in households’ bank accounts rose by £3.2bn in August, which was below the £3.9bn rise in July and much smaller than the 2019 average monthly rate of £4.6bn.
- The labour market remained exceptionally tight. Data for July and August provided further evidence that the weaker economy is leading to a cooling in labour demand. Labour Force Survey (LFS) employment rose by 40,000 in the three months to July (the

smallest rise since February). But a renewed rise in inactivity of 154,000 over the same period meant that the unemployment rate fell from 3.8% in June to a new 48-year low of 3.6%. The single-month data showed that inactivity rose by 354,000 in July itself and there are now 904,000 more inactive people aged 16+ compared to before the pandemic in February 2020. The number of vacancies has started to level off from recent record highs but there have been few signs of a slowing in the upward momentum on wage growth. Indeed, in July, the 3my/y rate of average earnings growth rose from 5.2% in June to 5.5%.

- CPI inflation eased from 10.1% in July to 9.9% in August, though inflation has not peaked yet. The easing in August was mainly due to a decline in fuel prices reducing fuel inflation from 43.7% to 32.1%. And with the oil price now just below $90pb, we would expect to see fuel prices fall further in the coming months.
- However, utility price inflation is expected to add 0.7% to CPI inflation in October when the Ofgem unit price cap increases to, typically, £2,500 per household (prior to any benefit payments). But, as the government has frozen utility prices at that level for two years, energy price inflation will fall sharply after October and have a big downward influence on CPI inflation.
- Nonetheless, the rise in services CPI inflation from 5.7% y/y in July to a 30-year high of 5.9% y/y in August suggests that domestic price pressures are showing little sign of abating. A lot of that is being driven by the tight labour market and strong wage growth. CPI inflation is expected to peak close to 10.4% in November and, with the supply of workers set to remain unusually low, the tight labour market will keep underlying inflationary pressures strong until early next year.
- During H1 2022, there has been a change of both Prime Minister and Chancellor. The new team (Liz Truss and Kwasi Kwarteng) have made a step change in government policy. The government's huge fiscal loosening from its proposed significant tax cuts will add to existing domestic inflationary pressures and will potentially leave a legacy of higher interest rates and public debt. Whilst the government's utility price freeze, which could cost up to £150bn (5.7% of GDP) over 2 years, will reduce peak inflation from 14.5% in January next year to 10.4% in November this year, the long list of tax measures announced at the "fiscal event" adds up to a loosening in fiscal policy relative to the previous government's plans of £44.8bn (1.8% of GDP) by 2026/27. These included the reversal of April's national insurance tax on 6th November, the cut in the basic rate of income tax from 20p to 19p in April 2023, the cancellation of next April's corporation tax rise, the cut to stamp duty and the removal of the 45p tax rate, although the 45p tax rate cut announcement has already been reversed.
- Fears that the government has no fiscal anchor on the back of these announcements has meant that the pound has weakened again, adding further upward pressure to interest rates. Whilst the pound fell to a record low of $1.035 on the Monday following the government's "fiscal event", it has since recovered to around $1.12. That is due to hopes that the Bank of England will deliver a very big rise in interest rates at the policy meeting on 3rd November and the government will lay out a credible medium-term plan in the near term. This was originally expected as part of the fiscal statement on 23rd November but has subsequently been

moved forward to an expected release date in October. Nevertheless, with concerns over a global recession growing, there are downside risks to the pound.

- The MPC has now increased interest rates seven times in as many meetings in 2022 and has raised rates to their highest level since the Global Financial Crisis. Even so, coming after the Fed and ECB raised rates by 75 basis points (bps) in their most recent meetings, the Bank of England's latest 50 basis points hike looks relatively dovish. However, the UK's status as a large importer of commodities, which have jumped in price, means that households in the UK are now facing a much larger squeeze on their real incomes.
- Since the fiscal event on 23rd September, we now expect the Monetary Policy Committee (MPC) to increase interest rates further and faster, from 2.25% currently to a peak of 5.00% in February 2023. The combination of the government's fiscal loosening, the tight labour market and sticky inflation expectations means we expect the MPC to raise interest rates by 100bps at the policy meetings in November (to 3.25%) and 75 basis points in December (to 4%) followed by further 50 basis point hikes in February and March (to 5.00%). Market expectations for what the MPC will do are volatile. If Bank Rate climbs to these levels the housing market looks very vulnerable, which is one reason why the peak in our forecast is lower than the peak of 5.50% - 5.75% priced into the financial markets at present.
- Throughout 2022/23, gilt yields have been on an upward trend. They were initially caught up in the global surge in bond yields triggered by the surprisingly strong rise in CPI inflation in the US in May. The rises in two-year gilt yields (to a peak of 2.37% on 21st June) and 10-year yields (to a peak of 2.62%) took them to their highest level since 2008 and 2014 respectively. However, the upward trend was exceptionally sharply at the end of September as investors demanded a higher risk premium and expected faster and higher interest rate rises to offset the government's extraordinary fiscal stimulus plans. The 30-year gilt yield rose from 3.60% to 5.10% following the "fiscal event", which threatened financial stability by forcing pension funds to sell assets into a falling market to meet cash collateral requirements. In response, the Bank did two things. First, it postponed its plans to start selling some of its quantitative easing (QE) gilt holdings until 31st October. Second, it committed to buy up to £65bn of long-term gilts to "restore orderly market conditions" until 14th October. In other words, the Bank is restarting QE, although for financial stability reasons rather than monetary policy reasons.
- Since the Bank's announcement on 28th September, the 30-year gilt yield has fallen back from 5.10% to 3.83%. The 2-year gilt yield dropped from 4.70% to 4.30% and the 10-year yield fell back from 4.55% to 4.09%.
- There is a possibility that the Bank continues with QE at the long-end beyond 14th October or it decides to delay quantitative tightening beyond 31st October, even as it raises interest rates. So far at least, investors seem to have taken the Bank at its word that this is not a change in the direction of monetary policy nor a step towards monetary financing of the government's deficit. But instead, that it is a temporary intervention with financial stability in mind.

- After a shaky start to the year, the S&P 500 and FTSE 100 climbed in the first half of Q2 2022/23 before falling to their lowest levels since November 2020 and July 2021 respectively. The S&P 500 is 7.2% below its level at the start of the quarter, whilst the FTSE 100 is 5.2% below it as the fall in the pound has boosted the value of overseas earnings in the index. The decline has, in part, been driven by the rise in global real yields and the resulting downward pressure on equity valuations as well as concerns over economic growth leading to a deterioration in investor risk appetite.