

Decision maker	Leadership Team	 THE ROYAL BOROUGH OF KENSINGTON AND CHELSEA
Date of Report	8 th November 2023	
Forward Plan ref:	KD06579	
Report title	Treasury Management Mid-Year Report 2023/24	
Reporting officer	Mike Curtis, Executive Director of Resources	
Key decision	Yes	
Access to information classification	Public	
Wards	All	

1. EXECUTIVE SUMMARY

- 1.1. This is the treasury management activity report for the period from 1 April 2023 to 30 September 2023.
- 1.2. The purpose of this report is to present the Council's treasury management activity to 30 September 2023 (Q2 – half-way through the financial year).
- 1.3. The treasury management activity report covers:
 - Economic background
 - Treasury position as at 30 September 2023
 - Delivery of the Treasury Management Strategy for 2023/24
 - Treasury borrowing
 - Capital expenditure and borrowing limits
 - Compliance with treasury limits

2. RECOMMENDATIONS

- 2.1. It is recommended that Leadership Team refer the report to Full Council.

3. ECONOMIC BACKGROUND

- 3.1. At the beginning of the 2023/24 financial year, CPI inflation was recorded at 8.7%, and has gradually decreased, currently standing at 6.7% (September 2023), reflecting a decrease of 2% in the first half of the year.

- 3.2. On 21 September 2023 the Bank of England Monetary Policy Committee (MPC) voted unanimously to reduce the stock of UK government bond purchases held for monetary policy purposes, and financed by the issuance of central bank reserves, by £100 billion over the next twelve months, to a total of £658 billion.
- 3.3. UK GDP is estimated to have grown by 0.2% in August 2023, following a fall of 0.5% in July. The Bank of England expects GDP to rise only slightly in 2023 Q3. Underlying growth in the second half of 2023/24 is also likely to be weaker than expected.
- 3.4. The MPC voted to maintain the UK base rate at 5.25% in September 2023. Previous months saw three rate hikes in May 2023 (to 4.50%), June 2023 (to 5.00%) and in August 2023 (to 5.25%). The rise in the base rate was driven by elevated inflation and wage growth; however, it is now anticipated to have reached its highest point.
- 3.5. The Council's treasury consultant, Arlingclose, upgraded its interest rate and gilt yield forecast on 25 September 2023. The official bank rate is forecast to remain at 5.25% for the remainder of 2023/24. Conversely, gilt yields are expected to fall slightly over the forecast period.
- 3.6. Arlingclose's interest rate and gilt yield forecast is set out in Table 1:

Table 1: Interest Rate and Gilt Yield Forecast

	Current	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26
Official Bank Rate													
Upside risk	0.00	0.25	0.50	0.50	0.75	0.75	0.75	0.75	0.75	0.75	0.75	1.00	1.00
Central Case	5.25	5.25	5.25	5.25	5.00	4.75	4.25	4.00	3.75	3.50	3.25	3.00	3.00
Downside risk	0.00	0.00	-0.25	-0.50	-0.75	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
3-month money market rate													
Upside risk	0.00	0.25	0.50	0.50	0.75	0.75	0.75	0.75	0.75	0.75	0.75	1.00	1.00
Central Case	5.40	5.40	5.40	5.30	5.15	4.80	4.30	4.10	3.80	3.50	3.25	3.05	3.05
Downside risk	0.00	0.00	-0.25	-0.50	-0.75	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
5yr gilt yield													
Upside risk	0.00	0.50	0.70	0.70	0.85	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Central Case	4.38	4.50	4.50	4.40	4.25	4.00	3.75	3.50	3.40	3.30	3.30	3.30	3.35
Downside risk	0.00	-0.50	-0.70	-0.85	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
10yr gilt yield													
Upside risk	0.00	0.50	0.70	0.70	0.80	0.90	1.00	1.10	1.20	1.20	1.20	1.20	1.20
Central Case	4.27	4.40	4.35	4.30	4.25	4.15	4.00	3.80	3.75	3.65	3.60	3.65	3.70
Downside risk	0.00	-0.50	-0.70	-0.85	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
20yr gilt yield													
Upside risk	0.00	0.50	0.70	0.70	0.80	0.90	1.00	1.10	1.20	1.20	1.20	1.20	1.20
Central Case	4.67	4.65	4.60	4.55	4.45	4.35	4.25	4.20	4.20	4.20	4.20	4.20	4.20
Downside risk	0.00	-0.50	-0.70	-0.85	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
50yr gilt yield													
Upside risk	0.00	0.50	0.70	0.70	0.80	0.90	1.00	1.10	1.20	1.20	1.20	1.20	1.20
Central Case	4.25	4.25	4.20	4.15	4.10	4.10	4.10	4.10	4.10	4.10	4.10	4.10	4.10
Downside risk	0.00	-0.50	-0.70	-0.85	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00

PWLB Standard Rate (Maturity Loans) = Gilt yield + 1.00%; PWLB Certainty Rate (Maturity Loans) = Gilt yield + 0.80%
 PWLB HRA Rate (Maturity Loans) = Gilt yield + 0.40%; UKIB Rate (Maturity Loans) = Gilt yield + 0.60%

4. TREASURY POSITION AS AT 30 SEPTEMBER 2023

- 4.1. The Council's debt and investment positions at the beginning and end of the half year were as follows:

£m	Principal	Rate	Principal	Rate
	30-Sep-23 £m	30-Sep-23 £m	31-Mar-23 £m	31-Mar-23 £m
Fixed Rate Borrowing				
Public Works Loan Board	-229.22	3.32%	-229.23	3.32%
Loan Total	-229.22	3.32%	-229.23	3.32%
Investments				
Fixed Term deposits	10.00	4.00%	10.00	4.00%
VNAV Fund	22.54	n/a	22.54	n/a
Money Market Funds	16.50	5.32%	12.70	4.09%
Deposit Total	49.04	4.82%	45.24	4.05%
Net Cash Balance	-180.18		-183.99	

4.2. The following table provides a summary of how the portfolio was invested as at 30 September 2023:

Counterparty Type	Investment Type	Amount £m	Percentage of Total Investment	Weighted Average Rate of Return
Local Authorities	Fixed Deposit	10.00	20.39%	4.00%
Money Market Funds	MMF	16.50	33.65%	5.32%
RLAM Investment Grade Credit Fund	VNAV Fund	22.54	45.96%	n/a
Total		49.04	100.0%	4.82%

Appendix B shows the volume and value of investments made with approved lending list counterparties.

5. TREASURY MANAGEMENT STRATEGY FOR 2023/24

5.1. The Treasury Management Strategy Statement (TMSS) for 2023/24 was approved by full council on 1 March 2023, and was based on the expectation that the Bank of England would continue to raise the bank rate in 2023 to subdue inflationary pressures. Inflation has proved more resilient than expected with previous forecasts stating a peak of 4.25%.

- 5.2. At the time, gilt yields were expected to remain flat at levels over the medium term, with five, ten and 20-year gilt yields expected to average around 3.5%, 3.5%, and 3.85% respectively over the three-year period to December 2025. As seen in table 1, gilt yields are now expected to be slightly higher over the forecasted period.
- 5.3. The Council has continued to follow its strategy, although with lower levels of cash balances this has limited investments to MMFs and local authority investments to ensure sufficient liquidity is maintained.
- 5.4. Benchmark rates rose throughout Q1 and Q2 for 2023/24, with the Council's investments performing slightly under the SONIA benchmark. The following table shows the weekly average of the Council's performance excluding the Short Dated Corporate Bond against Sterling Overnight Index Average (SONIA) rate.

Cash Yields Relative to SONIA

Quarter Ended	Balance	Weighted Average Rate	Average Sonia rate
	£m	%	%
Q1	70.54	4.30%	4.39%
Q2	49.04	4.88%	5.09%
Average 1 April - 30 September 2023	69.12	4.59%	4.75%

- 5.5. The Council's budgeted investment return for the year on external investment is £5.215m. Investment income for the mid-year to 30 September 2023 is £825k, with a total projection of £4.599m interest earned for the financial year 2023/24. In addition to interest earned on cash holdings, the short dated corporate bond received a coupon income of £451k for April to September 2023, as detailed in the following table.

Investment Grade Credit Fund Income Distribution	
Date	Distribution
30-Jun-23	209,573
30-Sep-23	241,108
Total	450,681

- 5.6. As of 30 September 2023, the Council holds two deposits with one local authority. These deposits are earning a rate of 4.00% each and will be maturing in October and December of this year. These deposits will generate interest of £0.382m.

- 5.7. The average cash balance held by the Council over the period was £69.118m (including the allocation to the short-dated bond fund) between 1 April and 30 September 2023.

6. TREASURY BORROWING

- 6.1. The Council has an increasing capital financing requirement (CFR). Officers will continue to monitor interest rates to identify suitable borrowing opportunities.
- 6.2. Following the implementation of the self-financing initiative, the HRA has continued to be partly funded, using the Council's general fund cash reserves. The HRA has paid interest to the general fund for the use of this money. This is charged at a fixed rate of 2.14%.
- 6.3. It is anticipated that the Council will undertake new external borrowing this financial year. Officers will monitor the market for the most favourable rates and assess the possibility of loans from local authorities, Banks and the PWLB market to fund its capital programme and achieve the most favourable rates for the Council.
- 6.4. The Council's loan portfolio is solely fixed rate; and with the rising interest rates on investment balances, the Council's net cost of carry has narrowed as the returns on the Council's cash has increased.

7. CAPITAL EXPENDITURE AND BORROWING LIMITS

- 7.1. At 30 September, the total forecast for capital spending in 2023/24 is £198.2m, which is below the budgeted amount of £257.3m. An update to this position will be reported to the Leadership Team as part of the budget monitoring process.

8. COMPLIANCE WITH TREASURY LIMITS

- 8.1. During the financial year, the Council operated within the treasury limits. The detailed outturn for Treasury Management Prudential Indicators is shown in **Appendix A**.
- 8.2. Other non-Treasury related Prudential Indicators are set and monitored as part of the Council's Budget process.

9. LEGAL IMPLICATIONS

- 9.1 The Local Government Act 2003 ("the Act") and the Local Authorities (Capital Financing and Accounting) (England) Regulations 2003 require the Council to 'have regard to' the Prudential Code and to set Prudential Indicators for the next three years to ensure that the Council's capital

investment plans are affordable, prudent and sustainable.

Mike Curtis
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Background papers: CIPFA Code of Practice on Treasury Management for the Public Sector

DLUHC Guidance on Local Government Investments

Contact Officer e-mail: kmartin3@westminster.gov.uk

Mandatory clearance requirements for all Key and Executive Decision reports

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