Bath & North East Somerset Council		
MEETING	**Cabinet**	
MEETING DATE:	**10th / 11th February 2022**	EXECUTIVE FORWARD PLAN REFERENCE: E 3300
TITLE:	**Treasury Management Performance Report to 31st December 2021**	
WARD:	All	
AN OPEN PUBLIC ITEM		

List of attachments to this report:

Appendix 1 – Performance Against Prudential Indicators
Appendix 2 – The Council's Investment Position at 31st December 2021
Appendix 3 – Average monthly rate of return for 1st 9 months of 2021/22
Appendix 4 – The Council's External Borrowing Position at 31st December 2021
Appendix 5 – Arlingclose's Economic & Market Review Q3 of 2021/22
Appendix 6 – Interest & Capital Financing Budget Monitoring 2021/22
Appendix 7 – Summary Guide to Credit Ratings
Appendix 8 – Extract from Treasury Management Risk Register

1 THE ISSUE

1.1 Treasury risk management at the Authority is conducted within the framework of the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2017 Edition (the CIPFA Code), which requires the Council to approve a Treasury Management Strategy before the start of each financial year, review performance during the year, and approve an annual report after the end of each financial year.

1.2 This report gives details of performance against the Council's Treasury Management Strategy for 2021/22 for the first nine months of 2021/22.

2 RECOMMENDATION

The Cabinet agrees that;

2.1 The Treasury Management Report to 31st December 2021, prepared in accordance with the CIPFA Treasury Code of Practice, is noted.

2.2 The Treasury Management Indicators to 31st December 2021 are noted.

3 THE REPORT

Summary

3.1 The average rate of investment return for the first nine months of 2021/22 is 0.26%, which is 0.28% above the benchmark rate which has averaged -0.02% over the period.

3.2 The Council's Prudential Indicators for 2021/22 were agreed by Council in February 2021 and performance against the key indicators is shown in **Appendix 1**. All indicators are within target levels.

Summary of Returns

3.3 The Council's investment position as at 31st December 2021 is given in **Appendix 2**. The balance of deposits as at 31st December 2021, compared to those as at 30th September 2021, are also set out in the pie charts in this appendix.

3.4 Gross interest earned on investments totalled £170k. **Appendix 3** details the investment performance, showing the average rate of interest earned over this period was 0.26%, which was 0.28% above the benchmark rate of average 7 day LIBID +0.05% (-0.02%). This excess is mainly due to the £5m investment held in the CCLA Local Authority Property Fund, which is a long term strategic investment earning a higher estimated rate of interest of 3.4%, based on the first nine months of 2021/22.

Summary of Borrowings

3.5 The Council's external borrowing as at 31st December 2021 totalled £220.8 million and is detailed in **Appendix 4**.

3.6 On 1st April 2021, the Council repaid £15.0 million of short term borrowing from a local authority, which had been borrowed last year for general cashflow requirements and to lower liquidity risks arising from uncertainties surrounding the Covid-19 pandemic.

3.7 A further £5m short term loan was repaid at maturity on 25th November 2021 without the need to replace the loan at present, due to the Council's current high cash balances.

3.8 The Council's Capital Financing Requirement (CFR) as at 31st March 2021 was £326.9 million. This represents the Council's underlying need to borrow to finance capital expenditure, and demonstrates that the borrowing taken to date relates to funding historical capital spend.

3.9 The difference between the CFR and the current borrowing of £220.8 million represents re-investment of the internal balances including reserves, reducing the in-year borrowing costs in excess of the potential investment returns.

3.10 Following Local Government Reorganisation in 1996, Avon County Council's residual debt is administered by Bristol City Council. All successor Unitary Authorities make an annual contribution to principal and interest repayment, for which there is a provision in the Council's revenue budget. The amount of residual debt outstanding as at 31st March 2021 apportioned to Bath & North East Somerset Council is £10.9m. Since this borrowing is managed by an external body and treated in the Council's Statement of Accounts as a deferred liability, it is not included in the borrowing figures referred to in paragraph 3.5.

3.11 The borrowing portfolio as at 31st December 2021 is shown in **Appendix 4**.

Strategic & Tactical Decisions

3.12 As shown in the charts in **Appendix 2**, the investment portfolio of £82.9 million as at 31st December 2021 is diversified across Money Market Funds, Local Authorities, the Government's Debt Mgt Account Deposit Facility, Strategic funds and in highly rated UK Banks. The Council uses AAA rated Money Market funds to maintain short term liquidity.

3.13 The Council has a deposit of £5m in the Lloyd's Bank 95-day notice sustainability deposit account, in line with the ESG focussed short term deposit section of the approved 2021/22 Treasury Management Strategy.

3.14 On the 27th of September 2021 Handlesbanken plc, a UK domiciled bank, was added back onto the list of authorised counterparties recommended by Arlingclose, the Council's Treasury Management Advisors. In line with the limits set out in the Treasury Management Strategy, the Council can now return to using Handelsbanken to make deposits of up to £10m, due to their AA- credit rating.

3.15 The Council does not hold any direct investments with banks in countries within the Eurozone reflecting both on the underlying debt issues in some Eurozone countries and the low levels of interest rates.

3.16 The potential for making future ESG focussed investments was included in the 2021/22 Treasury Management Strategy for the first time and was approved by Council in February 2021. Following a review carried out by Arlingclose of possible ESG (Environmental, Social and Corporate Governance) funds, and their presentation of findings and recommendations to Officers and Members in August 2021, the Chief Finance Officer agreed the investment of £5m split across the following two ESG focussed funds;

- £3m into FP Foresight UK Infrastructure fund; &
- £2m into VT Gravis Clean energy income fund;

3.17 On 30th November 2021, the Council made the first of its purchases of shares into the 2 funds with £1.5m placed with FP Foresight and £1m placed with VT Gravis. A further purchase of the same amount is planned for late February / early March 2022, which will be 3 months from the initial investment.

3.18 The Council's investment portfolio as at 31st December 2021 includes a total of £7.5m invested longer term, with the £2.5m detailed in 3.17 as well as the £5m in the CCLA Local Authorities Property Fund.

3.19 The Council's average investment return for short-term investments is currently 0.05%, in line with the budgeted level of 0.05%. The return on the £5m long-term strategic investment in the CCLA Local Authority Property Fund is estimated to be in line with the budgeted rate of 3.5%. The current forecast is for an overachievement of interest income from investments of £70k due to the Council's cash balances being higher than was forecast when the budget was set, as well as the additional income generated from the 2 new ESG funds which are expected to yield 3-4%.

Future Strategic & Tactical Issues

3.20 The Council's Treasury Management Advisor's economic and market review for the third quarter of 2021/22 is included in **Appendix 5**.

3.21 The benefits of the Council's current policy of internal borrowing are monitored regularly against the likelihood that long term borrowing rates are forecast to rise in future years. The focus remains on the rate of increase and the medium-term peak.

3.22 Any additional borrowing to take place in 2021/22 will therefore be balanced between a need to maintain an appropriate working cash balance and taking advantage of favourable movements in long term borrowing rates.

3.23 Following the Public Accounts Committee's recommendation that the prudential framework should be further tightened following continued borrowing by some authorities for investment purposes, in September 2021 CIPFA issued the revised Prudential Code and Treasury Management Code of Practice and Guidance Notes in draft form, and opened the latest consultation process on their proposed changes. The proposed changes include clarifications over the purpose and affordability of borrowing and some additional prudential indicators.

3.24 Once finalised, these changes will be incorporated into the Council's Treasury Management Strategy.

Borrowing update

3.25 Due to the high cash balances held by the Council at the end of 2020/21, a decision was made to repay the £15m one-year loan taken at the start of 2020/21 from the London Borough of Bromley upon its 1st April 2021 maturity date.

3.26 A further £5m of short term loans was repaid on 25th November without the need to replace the loan due to the council's high cash balances. No further borrowing has been taken during the first three quarters.

3.27 In Q1 the Council sought advice from its treasury advisors on the opportunity to make an early repayment of a £10m LOBO loan during 2021/22 as part of a debt rescheduling approach. In consultation with the Cabinet Member for Economic Development & Resources, the s151 Officer made the decision to pursue this restructuring, on the basis that it will provide revenue savings and reduce risk by replacing the LOBO debt with a shorter duration PWLB loan more aligned to the Council's future borrowing profile.

3.28 During the period the lender of the LOBO carried out their due diligence on the Council prior to execution of the repayment, interest rates increased. Upon re-assessment of the repayment with updated interest rates, it was assessed that it no longer appeared to be a value for money exercise, and it was decided that the Council would not proceed at this time. It was agreed that in their monitoring of future interest rate changes, our treasury advisors would conduct a future assessment on a repayment option should interest rates move in a way which would make the deal more favourable.

Budget Implications

3.29 A breakdown of the revenue budget showing interest and capital financing and the forecast year end position based on the period April to December 2021 is included in **Appendix 6**. An overall underspend of £0.730m is currently forecast, mainly related to the temporary high levels of cash balances currently held, resulting in a delay in the need to borrow and therefore incurring lower than budgeted interest costs.

Revisions to CIPFA Codes of Practice

3.30 CIPFA published revised Prudential and Treasury Management Codes in December 2021. The Prudential Code takes immediate effect although detailed reporting requirements may be deferred until the 2023/24 financial year, and will be included in the Treasury Management Strategy for that year.

4 STATUTORY CONSIDERATIONS

4.1 This report is for information only.

5 RESOURCE IMPLICATIONS (FINANCE, PROPERTY, PEOPLE)

5.1 The financial implications are contained within the body of the report.

6 RISK MANAGEMENT

6.1 A risk assessment related to the issue and recommendations has been undertaken, in compliance with the Council's decision making risk management guidance.

6.2 The Council’s lending & borrowing list is regularly reviewed during the financial year and credit ratings are monitored throughout the year. All lending/borrowing transactions are within approved limits and with approved institutions. Investment and borrowing advice is provided by our Treasury Management consultants, Arlingclose.

6.3 The CIPFA Treasury Management in the Public Services: Code of Practice requires the Council nominate a committee to be responsible for ensuring effective scrutiny of the Treasury Management Strategy and policies. The Corporate Audit Committee carries out this scrutiny.

6.4 In addition, the Council maintain a risk register for Treasury Management activities, which is regularly reviewed and updated where applicable during the year. An extract from the risk register, detailing how the top 5 market risks are managed, is included as **Appendix 8**.

7 CLIMATE CHANGE

7.1 The Council will continue to avoid any direct treasury management investments in fossil fuel related companies and will engage with its advisors to explore and assess the potential for any future investment opportunities in funds with a Renewable Energy & Sustainability focus as these products continue to be developed by the market in response to the Climate & Nature Emergency agenda.

7.2 An ESG section has been added to the Treasury Management Strategy document for the 2021/22 period and the treasury team will actively consider investment options permitted under the new guidelines.

7.3 As detailed under 3.13, a £5m deposit in the Lloyd's 95-day sustainability account was made during the quarter. This account is a deposit product of Lloyds Bank which helps to support ESG focussed projects by offering discounted funding rates to projects with a green/sustainable goal.

7.4 As detailed under 3.17, the first of 2 purchases in two ESG funds have now taken place, with the final purchase anticipated in February/March 2022, which would take the Council's position to £5m in long term ESG investment funds.

8 OTHER OPTIONS CONSIDERED

8.1 None

9 CONSULTATION

9.1 Consultation has been carried out with the Cabinet Member for Economic Development & Resources, Chief Finance Officer and Monitoring Officer.

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Background papers	2021/22 Treasury Management & Investment Strategy
Please contact the report author if you need to access this report in an alternative format	

APPENDIX 1
Performance against Treasury Management Indicators agreed in Treasury Management Strategy Statement

1. Treasury Borrowing limits

These limits include current commitments and proposals in the budget report for capital expenditure, plus additional headroom over & above the operational limit for unusual cash movements.

The Authorised limits for external debt include current commitments and proposals in the budget report for capital expenditure, plus additional headroom over and above the operational limit for unusual cash movements.

The Operational boundary for external debt is based on the same estimates as the authorised limit but without the additional headroom for unusual cash movements. This level also factors in the proposed approach to use internal cash-flow and future capital receipts as the preferred financing method for the capital programme.

	2021/22 Prudential Indicator	Actual as at 31st Dec 2021
Operational boundary – borrowing	£408m	£220.8m
Operational boundary – other long-term liabilities	£4m	£0m
Operational boundary – TOTAL	**£412m**	**£220.8m**
Authorised limit – borrowing	£438m	£220.8m
Authorised limit – other long-term liabilities	£4m	£0m
Authorised limit – TOTAL	**£442m**	**£220.8m**

2. Average Credit Rating*

The Council has adopted a voluntary measure of its exposure to credit risk by monitoring the weighted average credit rating of its investment portfolio. A summary guide to credit ratings is set out at **Appendix 7**.

	2021/22 Prudential Indicator	Actual as at 31st Dec 2021
	Rating	Rating
Minimum Portfolio Average Credit Rating	A-	AA

* *The calculation excludes the strategic investment in the CCLA Local Authority's Property Fund which is unrated.*

3. Liquidity

The Authority has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments within a rolling three-month period, without additional borrowing.

Liquidity risk indicator	2021/22 Prudential Indicator	Minimum During Quarter	Date of minimum
Minimum liquid cash balance in period	£15m	£41.5m	29th Nov

4. Interest rate exposures
This indicator is set to control the Council's exposure to interest rate risk. The upper limits on fixed and variable rate interest rate exposures, expressed as an amount of net principal borrowed.

	2021/22 Prudential Indicator	Actual as at 31st Dec 2021
Upper limit on fixed interest rate exposures	£408m	£200.8m
Upper limit on variable interest rate exposures	£184m	£20m

Fixed rate investments and borrowings are those where the rate of interest is fixed for at least 12 months, measured from the start of the financial year or the transaction date if later. All other instruments are classed as variable rate.

The Fixed rate limit is the total borrowing which can be at fixed interest rate, less any investments for a period greater than 12 months which has a fixed interest rate.

The Variable rate limit is the maximum amount of total borrowing which can be at variable interest rates.

5. Maturity Structure of borrowing
This indicator is set to control the Council's exposure to refinancing risk.

	Upper Limit	Lower Limit	Actual as at 31st Dec 2021
	%	%	%
Under 12 months	50	Nil	11.3
12 months and within 24 months	50	Nil	0
24 months and within 5 years	75	Nil	0
5 years and within 10 years	75	Nil	6.8
10 years and within 25 years	100	25	50.2
Over 25 years	100		31.7

* The CIPFA Treasury management Code now requires the prudential indicator relating to Maturity of Fixed Rate Borrowing to reference the maturity of LOBO loans to the earliest date on which the lender can require payment, i.e. the next call date (which are at 6 monthly intervals for the £20m of LOBO's). However, the Council would only consider repaying these loans if the Lenders exercised their options to alter the interest rate.

6. Upper limit for total principal sums invested for over 364 days
The purpose of this indicator is to control the Authority's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the long-term principal sum invested to final maturities beyond the period end will be:

Price risk indicator	2021/22 Prudential Indicator	Actual as at 31st Dec 2021
Limit on principal invested beyond 31st March 2022	£50m	£7.5m*
Limit on principal invested beyond 31st March 2023	£20m	£7.5m*
Limit on principal invested beyond 31st March 2024	£10m	£7.5m*

*The Council includes the CCLA LA Property Fund & two long term ESG Investments against this indicator as they are both held as Long Term Strategic Investments.

APPENDIX 2

The Council's Investment position at 31st December 2021

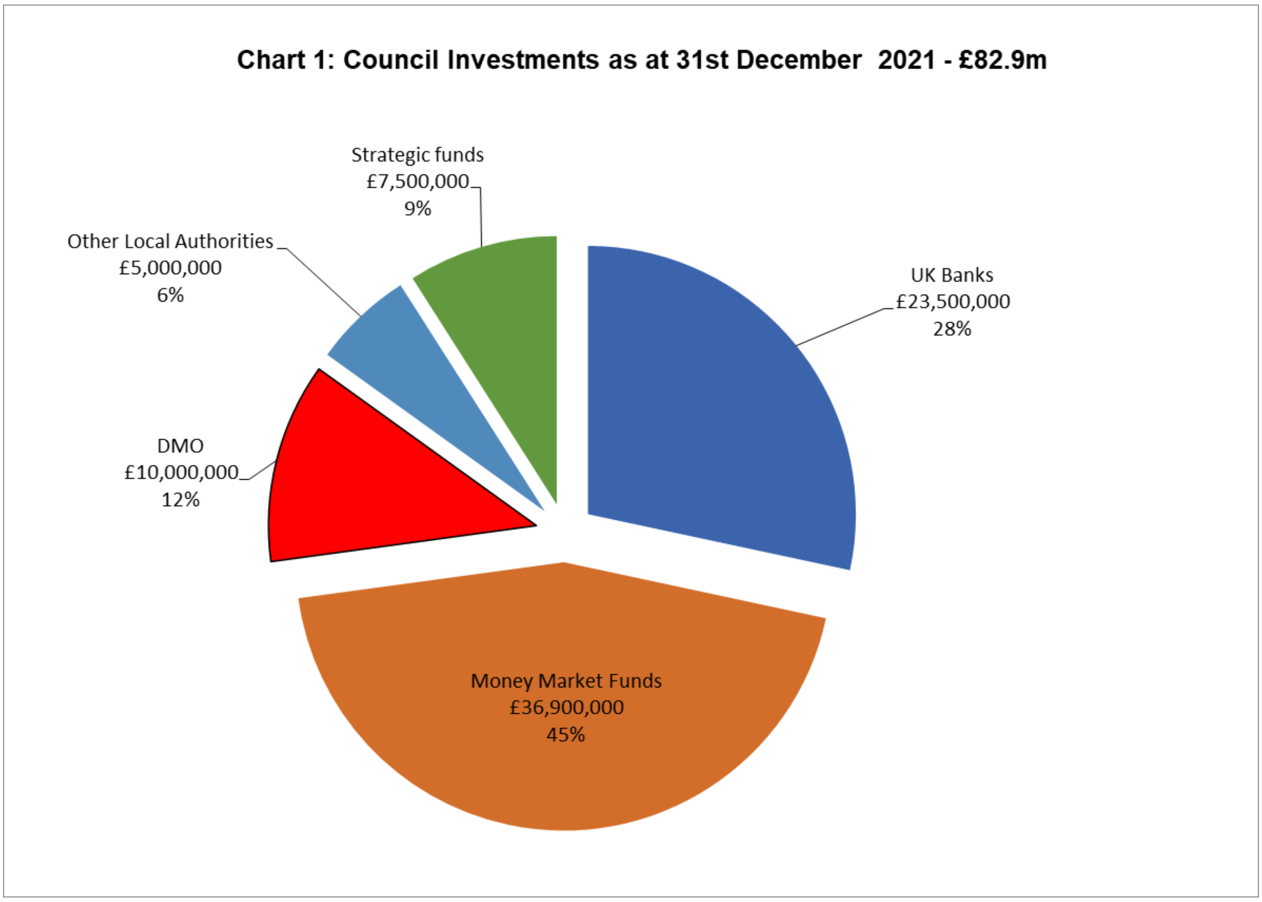
The term of investments is as follows:

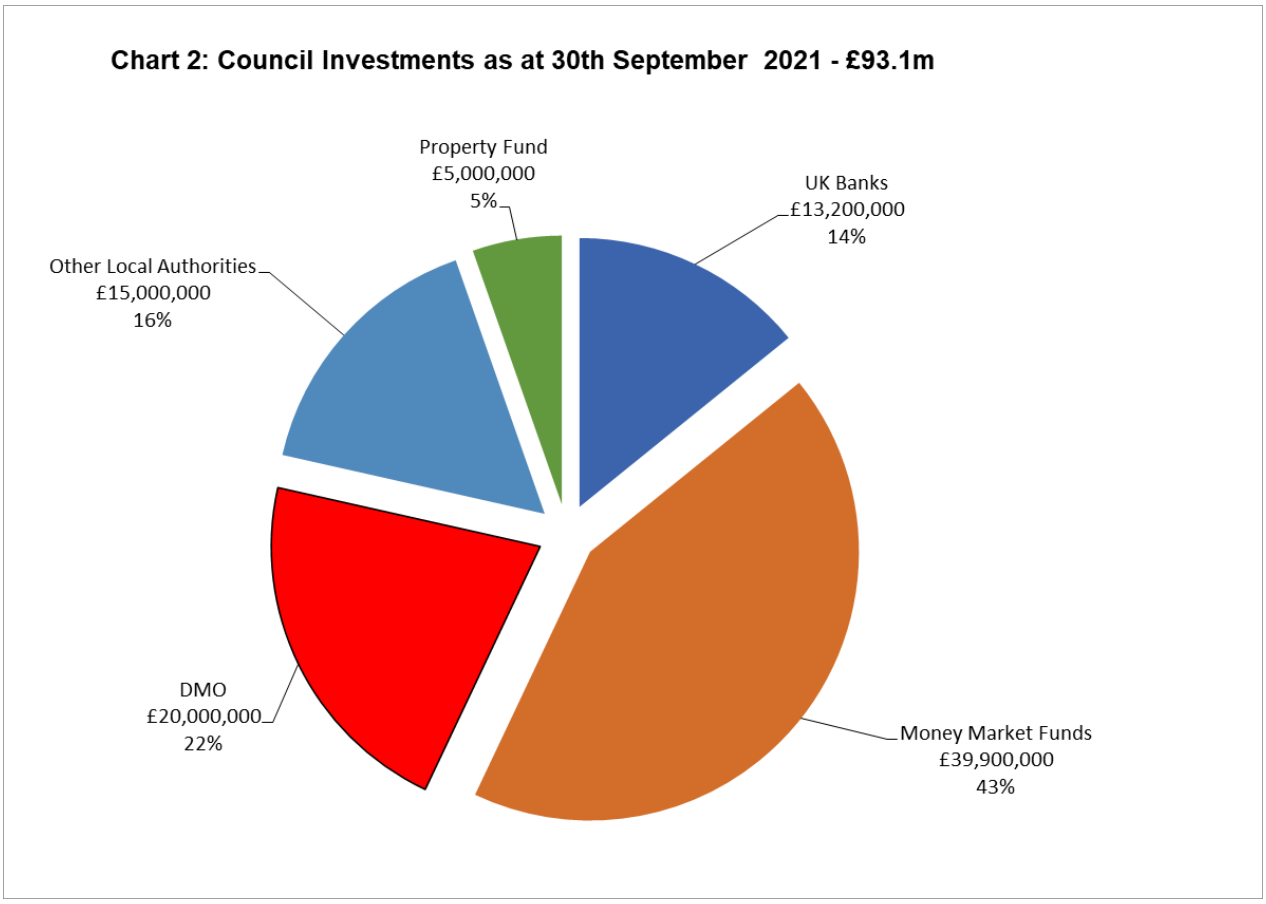
Term Remaining	**Balance at 31st Dec 2021**
	£m
Notice (instant access funds)	50.4
Up to 1 month	0
1 month to 3 months	15.0
3 months to 6 months	5.0
6 months to 12 months	5.0
Strategic Funds	7.5
Total	**82.9**

The investment figure is made up as follows:

	Balance at 31st Dec 2021
	£m
B&NES Council	80.3
Schools	2.6
Total	**82.9**

The Council had a total average net positive balance of £80.3m during the period April 2021 to December 2021.





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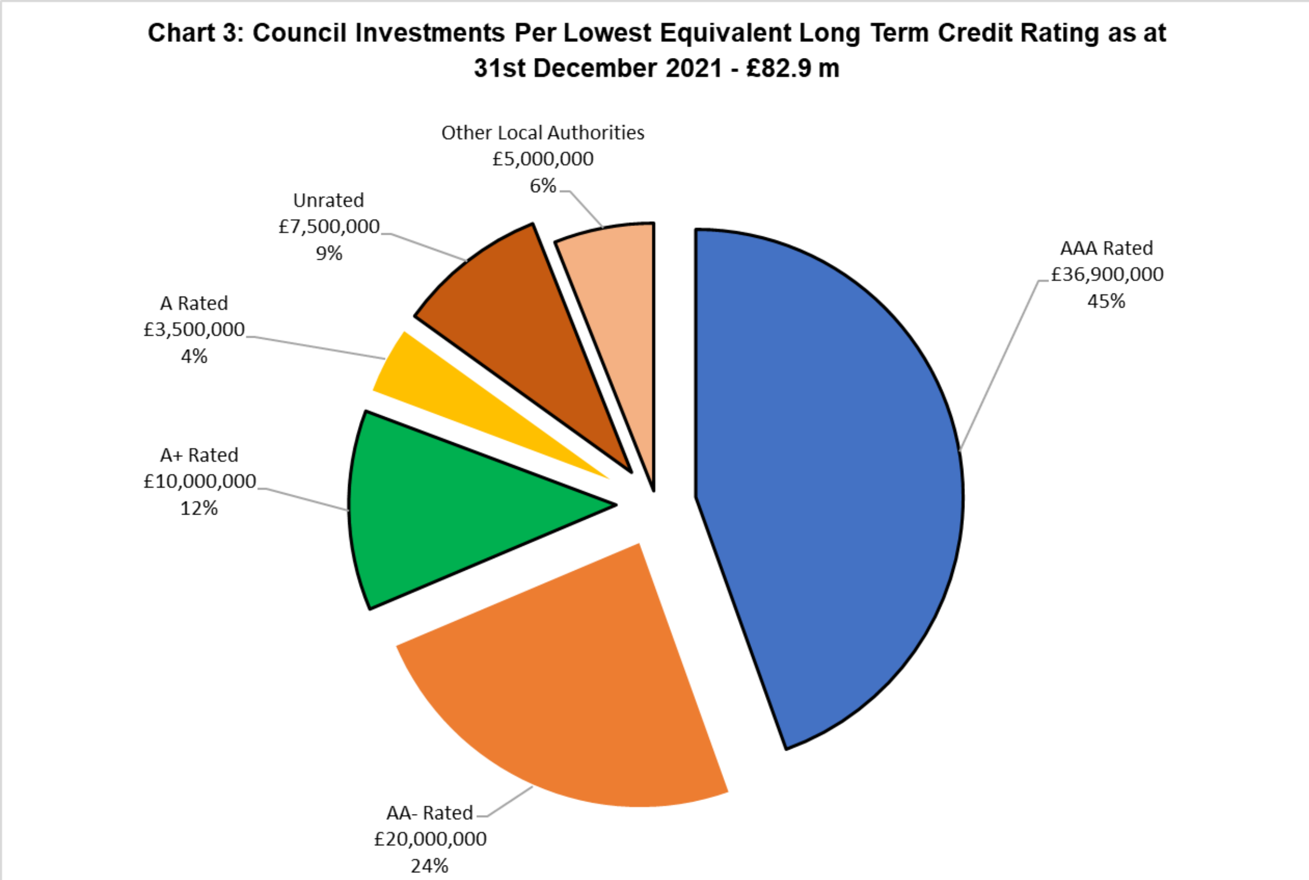
Chart 3: Council Investments Per Lowest Equivalent Long Term Credit Rating as at 31st December 2021 - £82.9 m
Other Local Authorities £5,000,000 6%
Unrated £7,500,000 9%
A Rated £3,500,000 4%
A+ Rated £10,000,000 12%
AA- Rated £20,000,000 24%
AAA Rated £36,900,000 45%

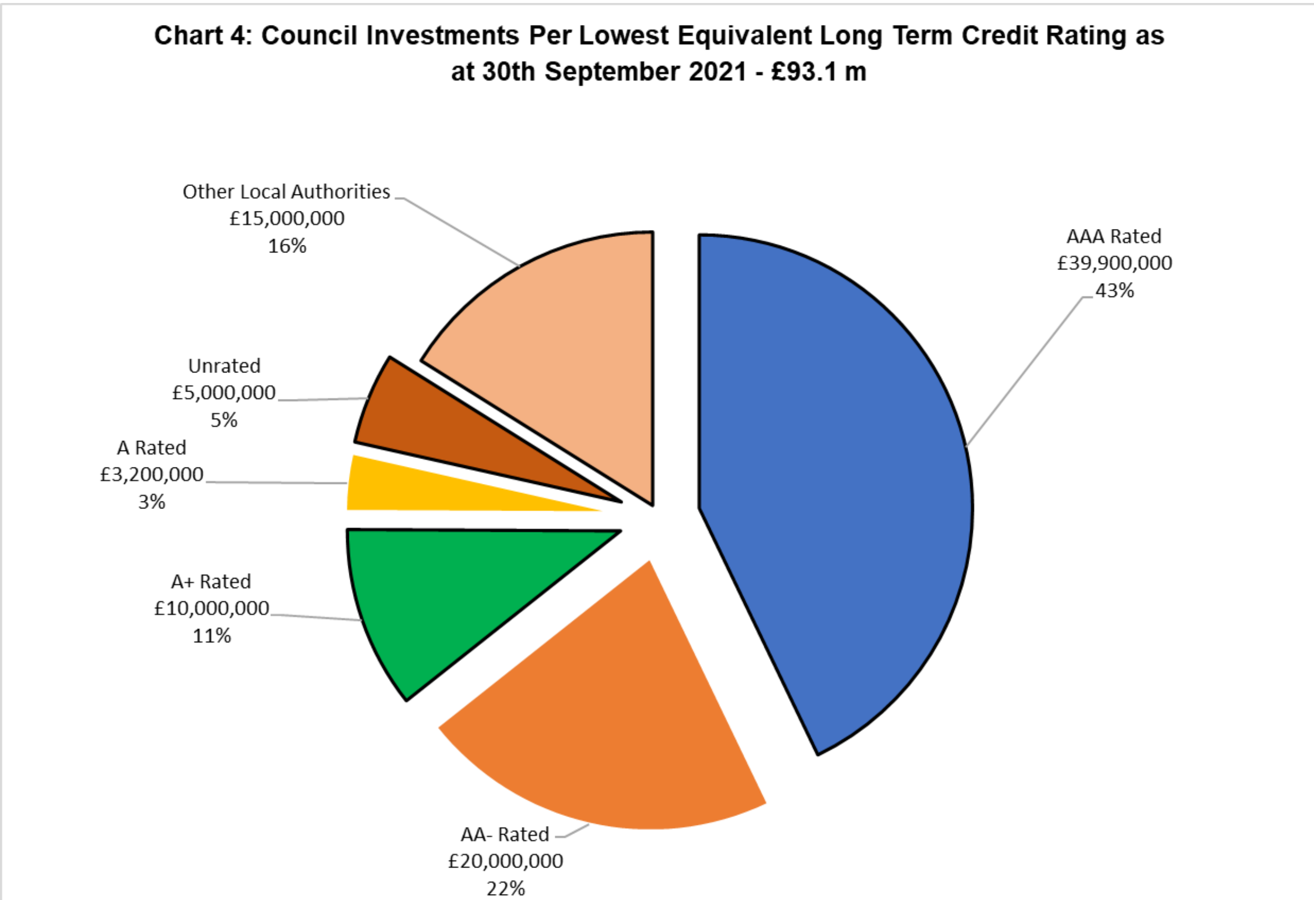
Chart 4: Council Investments Per Lowest Equivalent Long Term Credit Rating as at 30th September 2021 - £93.1 m
Other Local Authorities £15,000,000 16%
Unrated £5,000,000 5%
A Rated £3,200,000 3%
A+ Rated £10,000,000 11%
AA- Rated £20,000,000 22%
AAA Rated £39,900,000 43%

APPENDIX 3

Average rate of return on investments for 2021/22

	Apr. %	May %	Jun. %	Jul. %	Aug. %	Sep. %	Oct. %	Nov. %	Dec. %	Average
Average rate of interest earned	0.29	0.30	0.27	0.25	0.25	0.23	0.22	0.24	0.35	0.26%
Benchmark = Average 7 Day LIBID rate +0.05% (source: Arlingclose)	-0.03	-0.03	-0.03	-0.03	-0.03	-0.03	-0.03	-0.03	0.04	-0.02%
Performance against Benchmark %	+0.32	+0.33	+0.30	+0.29	+0.30	+0.26	+0.25	+0.27	+0.31	+0.29%

APPENDIX 4

Council's External Borrowing at 31st December 2021

Lender	Amount outstanding	Start date	End date	Interest rate
Long term				
PWLB489142	10,000,000	15/10/2004	15/10/2034	4.75%
PWLB497233	5,000,000	12/05/2010	15/08/2035	4.55%
PWLB497234	5,000,000	12/05/2010	15/02/2060	4.53%
PWLB498834	5,000,000	05/08/2011	15/02/2031	4.86%
PWLB498835	10,000,000	05/08/2011	15/08/2029	4.80%
PWLB498836	15,000,000	05/08/2011	15/02/2061	4.96%
PWLB503684	5,300,000	29/01/2015	08/04/2034	2.62%
PWLB503685	5,000,000	29/01/2015	08/10/2064	2.92%
PWLB505122	16,546,973	20/06/2016	20/06/2041	2.36%
PWLB508126	8,929,760	06/12/2018	20/06/2043	2.38%
PWLB508202	9,640,378	12/12/2018	20/06/2068	2.59%
PWLB508224	4,456,620	13/12/2018	20/06/2043	2.25%
PWLB505744	8,385,987	24/02/2017	15/08/2039	2.28%
PWLB505966	8,588,372	04/04/2017	15/02/2042	2.26%
PWLB506052	7,298,766	08/05/2017	15/02/2042	2.25%
PWLB506255	6,714,422	10/08/2017	10/04/2067	2.64%
PWLB506729	8,925,963	13/12/2017	10/10/2042	2.35%
PWLB506995	8,947,355	06/03/2018	10/10/2042	2.52%
PWLB506996	9,194,007	06/03/2018	10/10/2047	2.62%
PWLB507749	9,092,523	10/09/2018	20/07/2043	2.42%
PWLB508485	19,473,504	11/02/2019	20/07/2068	2.52%
PWLB509840	9,322,004	04/09/2019	20/07/2044	1.40%
KBC Bank N.V *	5,000,000	08/10/2004	08/10/2054	4.50%
KBC Bank N.V *	5,000,000	08/10/2004	08/10/2054	4.50%
Commerzbank AG Frankfurt*	10,000,000	27/04/2005	27/04/2055	4.50%
Medium term				
Portsmouth C.C.	5,000,000	19/12/2019	19/12/2022	1.65%
Total Borrowing	**220,816,633**			

*All LOBO's (Lender Option / Borrower Option) have reached the end of their fixed interest period and have reverted to the variable rate of 4.50%. The lender has the option to change the interest rate at 6 monthly intervals. Should the lender use the option to change the rate, then at this point the borrower has the option to repay the loan without penalty.

Appendix 5: Arlingclose Economic summary and forecast

Economic background: The economic recovery from coronavirus pandemic, together with higher inflation and higher interest rates were major issues over the period.
The Bank of England (BoE) increased Bank Rate to 0.25% in December 2021 but maintained its Quantitative Easing programme at £895 billion. The Monetary Policy Committee (MPC) voted 8-1 in favour of raising rates, and unanimously to maintain the asset purchase programme.

Within the announcement the MPC noted that the pace of the global recovery was broadly in line with its November Monetary Policy Report. Prior to the emergence of the Omicron coronavirus variant, the Bank also considered the UK economy to be evolving in line with expectations, however the increased uncertainty and risk to activity the new variant presents, the Bank revised down its estimates for Q4 GDP growth to 0.6% from 1.0%. Inflation was projected to be higher than previously forecast, with CPI likely to remain above 5% throughout the winter and peak at 6% in April 2022. The labour market was generally performing better than previously forecast and the BoE now expects the unemployment rate to fall to 4% compared to 4.5% forecast previously, but notes that Omicron could weaken the demand for labour.

UK CPI for November 2021 registered 5.1% year on year, up from 4.2% in the previous month. Core inflation, which excludes the more volatile components, rose to 4.0% y/y from 3.4%. The most recent labour market data for the three months to October 2021 showed the unemployment rate fell to 4.2% while the employment rate rose to 75.5%.

Government support in the form of the furlough scheme ended on 30th September 2021 but the subsequent impact on jobs appears to have been more muted than previously been feared. In October 2021, the headline 3-month average annual growth rate for wages were 4.9% for total pay and 4.3% for regular pay. In real terms, after adjusting for inflation, total pay growth was up 1.7% while regular pay was up 1.0%. The change in pay growth has been affected by a change in composition of employee jobs, where there has been a fall in the number and proportion of lower paid jobs.

Gross domestic product (GDP) grew by 1.1% in the third calendar quarter of 2021 according to the final estimate (initial estimate 1.3%), compared to a gain of 5.4% q/q in the previous quarter, with the annual rate slowing to 6.8% from 23.6%. The data however predates the escalation in virus infections caused by the Omicron variant in December which will very likely result in a slowdown in activity in Q4.

GDP growth in the euro zone increased by 2.2% in calendar Q3 2021 following an upwardly revised gain of 2.2% in the second quarter and decline of -0.2% in the first. Headline inflation has been strong, with CPI registering 5.0% year-on-year in December, the sixth successive month of inflation. Core CPI inflation was 2.6% y/y in December, unchanged from November but well up from July's recent low of 0.7% y/y. At these levels, inflation is above the European Central Bank's target of 'below, but close to 2%', putting some pressure on its long-term stance of holding its main interest rate of 0%.

The US economy expanded at an upwardly revised annualised rate of 2.3% in Q3 2021, slowing sharply from gains of 6.7% and 6.3% respectively in the previous two quarters. In its December 2021 interest rate announcement, the Federal Reserve continue to maintain the Fed Funds rate at between 0% and 0.25% but outlined its plan to reduce its asset purchase programme earlier than previously stated and signalled they are in favour of tightening interest rates at a faster pace in 2022, with three 0.25% movements now expected.

Financial markets: Ongoing monetary and fiscal stimulus together with rising economic growth supported equity markets over the period, but higher inflation and the prospect of higher interest rates mixed with a new coronavirus variant ensured it was a bumpy period. The Dow Jones hit another record high during the quarter while the UK-focused FTSE 250 index continued making gains over pre-pandemic levels. The more internationally focused FTSE 100 saw more modest gains over the period and remains below its pre-crisis peak.

Inflation worries dominated bond yield movements over the period as initial expectations for transitory price increases turned into worries higher inflation was likely to persist for longer meaning central bank action was likely to start sooner and rates increase at a faster pace than previously thought.

The 5-year UK benchmark gilt yield began the quarter at 0.62% before rising to 0.82%. Over the same period the 10 year gilt yield fell from 1.00% to 0.97% and the 20-year yield declined from 1.35% to 1.20%.

The Sterling Overnight Rate (SONIA) averaged 0.07% over the quarter.

Credit review: Relatively benign credit conditions caused credit default swap (CDS) prices for the larger UK banks to remain low and had steadily edged down throughout the year up until mid-November when the emergence of Omicron has caused them to rise modestly but have since continued their downward trajectory.

The pronounced gap in spreads between UK ringfenced and non-ringfenced entities continued to narrow and has now all but disappeared. At the end of the period Barclays Bank Plc was trading the highest at 53bps and Santander UK Plc the lowest at 26bps. The other ringfenced banks were trading between 34-37bps and Nationwide Building Society was 44bps.

There were a small number of credit rating and outlook changes over the period with Moody's downgrading DZ Bank to Aa2 and upgrading Co-operative Bank to Ba3 while Fitch revised the outlook on Australia and Rabobank to stable and S&P upgraded Nationwide BS, Standard Chartered Bank and Danske Bank to A+.

The ongoing vaccine rollout programme is credit positive for the financial services sector in general but there remains uncertainty around the full extent of the losses banks and building societies will suffer due to the pandemic-related economic slowdown, but the sector is in a generally better position now compared to earlier this year and 2020.

At the end of the period Arlingclose had completed its full review of its credit advice on unsecured deposits for UK and non-UK institutions whereby the maximum duration for all recommended counterparties were extended to 100 days.

As ever, the institutions and durations on the Authority's counterparty list recommended by treasury management advisors Arlingclose remain under constant review.

Outlook for the remainder of 2021/22 and beyond:

	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24
Official Bank Rate													
Upside risk	0.00	0.00	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Arlingclose Central Case	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Downside risk	0.00	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25

Arlingclose expects Bank Rate to rise again in Q1 2022. We believe the MPC will want to build on the strong message it delivered in December month by tightening policy despite Omicron uncertainty.

Arlingclose therefore expects Bank Rate to rise to 0.50% in Q1 2022, but then remain there. Risks to the forecast are initially weighted to the upside but becoming more balanced over time. The Arlingclose central forecast remains below the market forward curve.

Gilt yields are expected to remain broadly flat from current levels. Yields have fallen sharply at the longer end of the yield curve, but expectations of a rise in Bank Rate have maintained short term gilt yields at higher levels.

Easing expectations for Bank Rate over time could prompt the yield curve to steepen, as investors build in higher inflation expectations.

The risks around the gilt yield forecasts vary. The risk for short and medium term yields is initially on the upside but shifts lower later. The risk for long-term yields is weighted to the upside.

The global recovery from the pandemic has entered a more challenging phase. The resurgence in demand has led to the expected rise in inflationary pressure, but disrupted factors of supply are amplifying the effects, increasing the likelihood of lower growth rates ahead. The advent of the Omicron variant of coronavirus is affecting activity and is also a reminder of the potential downside risks.

Despite relatively buoyant activity survey data, official GDP data indicates that growth was weakening into Q4 2021. Other data, however, suggested continued momentum, particularly for November. Retail sales volumes rose 1.4%, PMIs increased, and the labour market continued to strengthen. The end of furlough did not appear to have had a significant impact on unemployment. Wage growth is elevated.

The CPI inflation rate rose to 5.1% for November and will rise higher in the near term. While the transitory factors affecting inflation are expected to unwind over time, policymakers' concern is persistent medium term price pressure.

These factors prompted the MPC to raise Bank Rate to 0.25% at the December meeting. Short term interest rate expectations remain elevated.

The outlook, however, appears weaker. Household spending faces pressures from a combination of higher prices and tax rises. In the immediate term, the Omicron variant has already affected growth – Q4 and Q1 activity could be weak at best.

Longer-term government bond yields remain relatively low despite the more hawkish signals from the BoE and the Federal Reserve. Investors are concerned that significant policy tightening in the near term will slow growth and prompt the need for looser policy

later. Geo-political and coronavirus risks are also driving safe haven buying. The result is a much flatter yield curve, as short-term yields rise even as long-term yields fall.
The rise in Bank Rate despite the Omicron variant signals that the MPC will act to bring inflation down whatever the environment. It has also made clear its intentions to tighten policy further. While the economic outlook will be challenging, the signals from policymakers suggest their preference is to tighten policy unless data indicates a more severe slowdown.

APPENDIX 6

Interest & Capital Financing Costs – Budget Monitoring 2021/22

April 2021 to December 2021	**YEAR END POSITION** Budgeted Spend or (Income) £'000	Forecast Spend or (Income) £'000	Forecast over or (under) spend £'000	**ADV/FAV**
Interest & Capital Financing				
- Debt Costs	8,049	7,419	(630)	FAV
- Internal Repayment of Loan Charges	(10,338)	(10,338)	0	
- Ex Avon Debt Costs	1,020	990	(30)	FAV
- Minimum Revenue Provision (MRP)	8,307	8,307	0	
- Interest on Balances	(208)	(278)	(70)	FAV
Total	**6,830**	**6,100**	**(730)**	**FAV**

APPENDIX 7

Summary Guide to Credit Ratings

Rating	Details
AAA	Highest credit quality – lowest expectation of default, which is unlikely to be adversely affected by foreseeable events.
AA	Very high credit quality - expectation of very low default risk, which is not likely to be significantly vulnerable to foreseeable events.
A	High credit quality - expectations of low default risk which may be more vulnerable to adverse business or economic conditions than is the case for higher ratings.
BBB	Good credit quality - expectations of default risk are currently low but adverse business or economic conditions are more likely to impair this capacity.
BB	Speculative - indicates an elevated vulnerability to default risk, particularly in the event of adverse changes in business or economic conditions over time.
B	Highly speculative - indicates that material default risk is present, but a limited margin of safety remains. Capacity for continued payment is vulnerable to deterioration in the business and economic environment.
CCC	Substantial credit risk - default is a real possibility.
CC	Very high levels of credit risk - default of some kind appears probable.
C	Exceptionally high levels of credit risk - default is imminent or inevitable.
RD	Restricted default - indicates an issuer that has experienced payment default on a bond, loan or other material financial obligation but which has not entered into bankruptcy filings, administration, receivership, liquidation or other formal winding-up procedure, and which has not otherwise ceased operating.
D	Default - indicates an issuer that has entered into bankruptcy filings, administration, receivership, liquidation or other formal winding-up procedure, or which has otherwise ceased business.

APPENDIX 8

Extract from Treasury Management Risk Register – Top 5 Market Risks

			Current Risk Score										
			Likelihood					Impact					
	Risk Nr	Description	1	2	3	4	5	1	2	3	4	5	Management Action
			L		M	H		L		M	H		
1	R01	Liquidity Risk - The risk that cash will not be available when it is needed, that ineffective management of liquidity creates additional unbudgeted costs, and that the organisation's business/service objectives will be thereby compromised.		2						3			Obtain approval of annual Treasury Management Strategy by February Council. Carry out weekly reviews of investment portfolio and planned actions. Carry out monthly dashboard meeting with Chief Finance Officer. Consider short and medium term cash balances and cashflows to inform any short - medium term borrowing requirement.
2	R02	Interest Rate Risk - The risk that fluctuations in the levels of interest rates create an unexpected or unbudgeted burden on the organisation's finances, against which the organisation has failed to protect itself adequately			3					3			Monitor interest rates on a monthly basis and compare with budget to determine impact on Council finances and report through monthly Treasury Dashboard. Report implication of interest rate changes to Cabinet as part of quarterly Treasury Management Performance Report. Explore alternative potential investment products following new freedoms - including corporate bonds, gilts, Certificate of Deposits etc.
3	R03	Exchange Rate Risk - The risk that fluctuations in foreign exchange rates create an unexpected or unbudgeted burden on the organisation's finances, against which the organisation has failed to protect itself adequately.	1						2				Treasury Management Policies clearly record the need to eliminate currency exchange rate risks .
4	R04	Inflation Risk - The risk that prevailing levels of inflation cause an unexpected or unbudgeted burden on the organisation's finances, against which the organisation has failed to protect itself adequately.			3					3			Liaise with Chief Finance Officer to ensure Inflation both current and projected forms part of the medium term financial planning framework.
5	R05	Credit and Counterparty Risk - The risk of failure by a third party to meet its contractual obligations to the organisation under an investment, borrowing, capital, project or partnership financing, particularly as a result of the third party's diminished creditworthiness, and the resulting detrimental effect on the organisation's capital or current (revenue) resources.			3						4		Complete annual review of Counterparty List with external advisors to feed into Treasury Management Strategy. Regular review of counterparty financial standing through use of credit ratings, credit default swap rates and national press coverage and liaison with Chief Finance Officer and external advisors to consider any issues / change in circumstances of counterparties.