

CYNGOR SIR POWYS COUNTY COUNCIL.

AUDIT COMMITTEE

24th June 2022

CABINET EXECUTIVE

5th July 2022

**REPORT AUTHOR: County Councillor David Thomas
Portfolio Holder for Finance and Corporate
Transformation**

**REPORT TITLE: Treasury Management Quarter 4 Report and Annual
Review**

REPORT FOR: Information

1 Purpose

- 1.1 CIPFA's 2009 Treasury Management Bulletin suggested:
'In order to enshrine best practice, it is suggested that authorities report formally on treasury management activities at least twice a year and preferably quarterly.'

The CIPFA Code of Practice on Treasury Management emphasises a number of key areas including the following:

xi. Treasury management performance and policy setting should be subject to scrutiny prior to implementation.

- 1.2 In line with the above, this report is providing information on the activities for the quarter ending 31st December 2021.

2 Background

- 2.1 The Treasury Management Strategy approved by Full Council on 25th February 2021 can be found here.

<https://powys.moderngov.co.uk/documents/s57662/Appendix%20F%20Capital%20Strategy%20and%20Treasury%20Management%20Strategy.pdf>

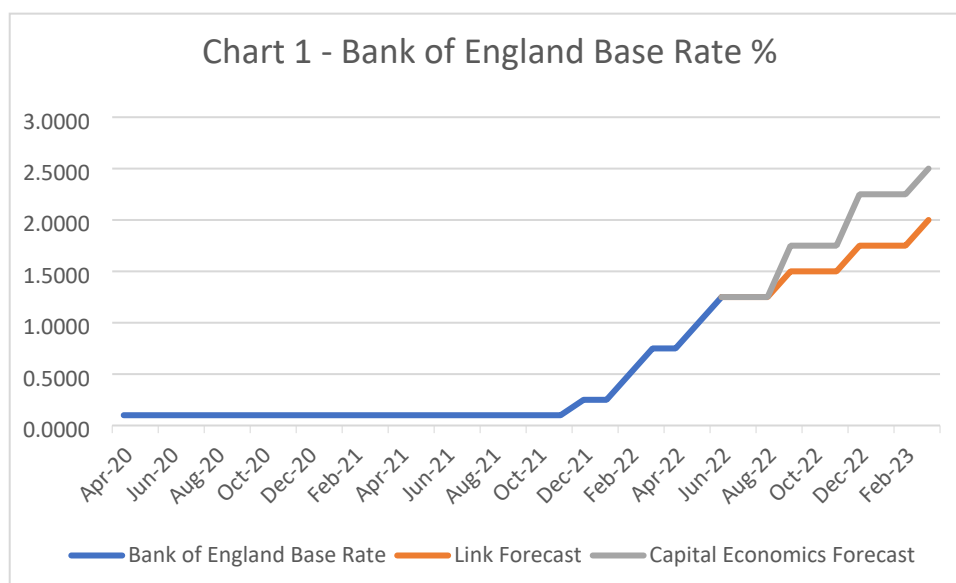
- 2.2 The Authority's investment priorities within the Strategy are.

- (a) the security of capital and
- (b) the liquidity of its investments.

- 2.3 The Authority aims to achieve the optimum return on its investments commensurate with proper levels of security and liquidity. The risk appetite has been low in order to give priority to security of investments.
- 2.4 With interest rates for investments remaining significantly lower than borrowing rates, the use of cash reserves as opposed to borrowing is prudent and cost-effective.

3 Advice

3.1 Investments



- 3.2 The chart above shows how the Bank of England base rate has changed over the last two years and the forecast from Link and Capital Economics to the end of 2022/23 (the forecasts were provided by the Council's advisors on the 20th May 2022).
- 3.3 Short-term money market investment rates have continued to increase following the two increases to the Bank Rate in the last quarter of 2021/22. This has increased the interest rate on the deposit account with the councils' main bankers from 0.16% to 0.66 at the end of the year. However, given the surplus of cash held by other local authorities' investment returns on inter-authority lending are expected to remain low.
- 3.4 When looking at temporary investing, the Treasury team consider the bank fee to set up the arrangement, because of this cost some investments are not cost effective for very short periods of time. However, the Authority does not have sufficient certainty around its cashflow to lend for longer periods where the return is higher.
- 3.5 The Welsh Government repayable funding the council received in March 2021 towards the Global Centre of Rail Excellence (GCRE) is currently

being held in the Council's deposit accounts until it is required for the project. This has generated £13k of interest which, under the terms of the agreement, this interest must be used towards this scheme and is not available for the Council to use.

3.6 The Authority had no other investments on 31st March 2022. The total interest received during the year was £38k.

3.7 Credit Rating Changes

3.8 There have been no credit rating changes relevant to this Authority's position during the last quarter.

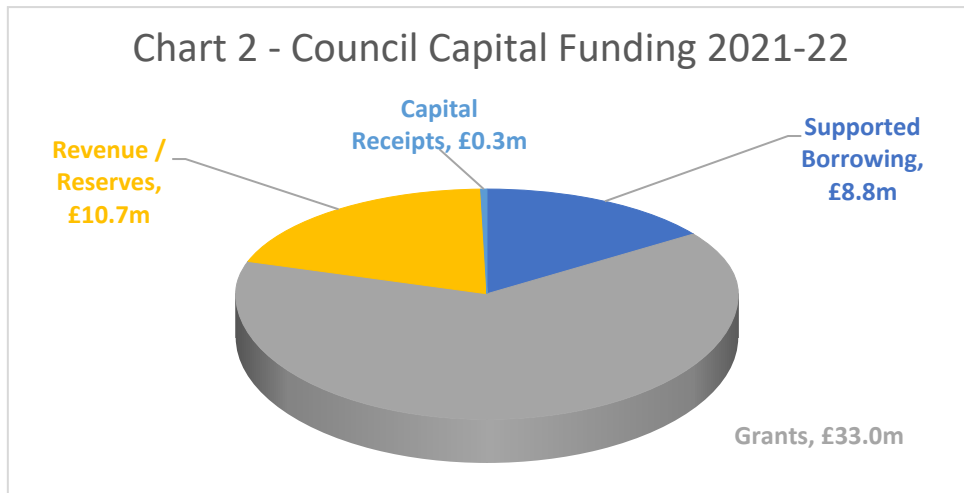
3.9 The Authority's Capital Position

3.10 The council approved the 2021 to 2031 Treasury Management and Capital Strategy on the 25th of February 2021. This included a Capital Programme for 2021/22 totalling £101.53 million.

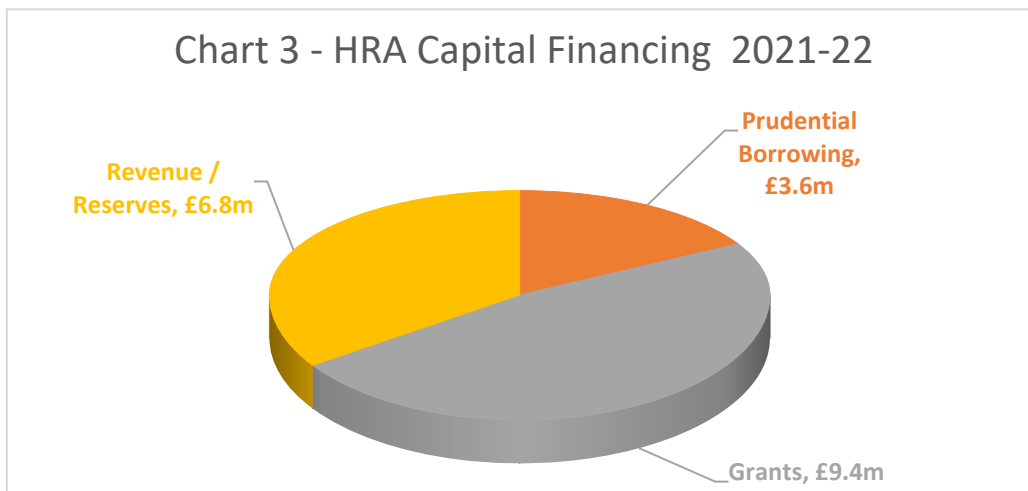
3.11 The table below shows a summary of 2021/22 capital expenditure,

Service Area	2021/22 £'m
Schools	£12.929m
Social Care	£1.871m
Highways, Transport & Recycling	£21.310m
Leisure & Recreation	£2.292m
Housing & Community Development	£63418m
Property, Planning and Public Protection	£1.888m
Economy & Digital	£6.104m
Sub Total	£52.812m
Housing Revenue Account	£19.783m
Total	£72.595m

3.12 Chart 2 below sets out how the Council funded element of the capital programme is funded, 17% will be funded through borrowing, the interest cost for this is charged to the revenue account.



3.13 Chart 3 below sets out how the Housing Revenue Account (HRA) funded element of the capital programme is funded, 18% will be funded through borrowing, the interest cost for this is charged to the HRA revenue account.



3.14 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. It represents the current year's unfinanced capital expenditure and prior years' net or unfinanced capital expenditure which has not yet been paid for by revenue or other resources.

3.15 Part of the Council's treasury activities is to address the funding requirements for this borrowing need. Depending on the capital expenditure programme, the finance team organises the Council's cash position to ensure that sufficient cash is available to meet the capital plans and cash flow requirements. This may be sourced through external borrowing or utilising temporary cash resources within the Council.

3.16 Net external borrowing (borrowings less investments) should not, except in the short term, exceed the total of CFR in the preceding year plus the

estimates of any additional CFR for the current year and next two financial years. This allows some flexibility for limited early borrowing for future years.

3.17 Capital Financing Requirement (CFR)

£'m	2020/21	2021/22
Original Estimates 25/02/2021	422.77	468.58
Quarter 1 estimate	397.10	436.96
Quarter 2 estimate	397.10	431.17
Quarter 3 estimate	397.10	419.11
Actual	397.10	405.21

3.18 The budget reprofiling into future financial years has reduced the CFR as shown in the above table. As outlined in the amendment of the 2022/23 Budget approved by Council on the 3rd March 2022, the additional funds provided by Welsh Government, Capital (£3.6m) and Revenue (£2.3m), together with the projected underspend on MRP for 2021/22 (£1.5m) has been used to fund existing Capital schemes reducing the CFR.

3.19 Borrowing / Re-scheduling

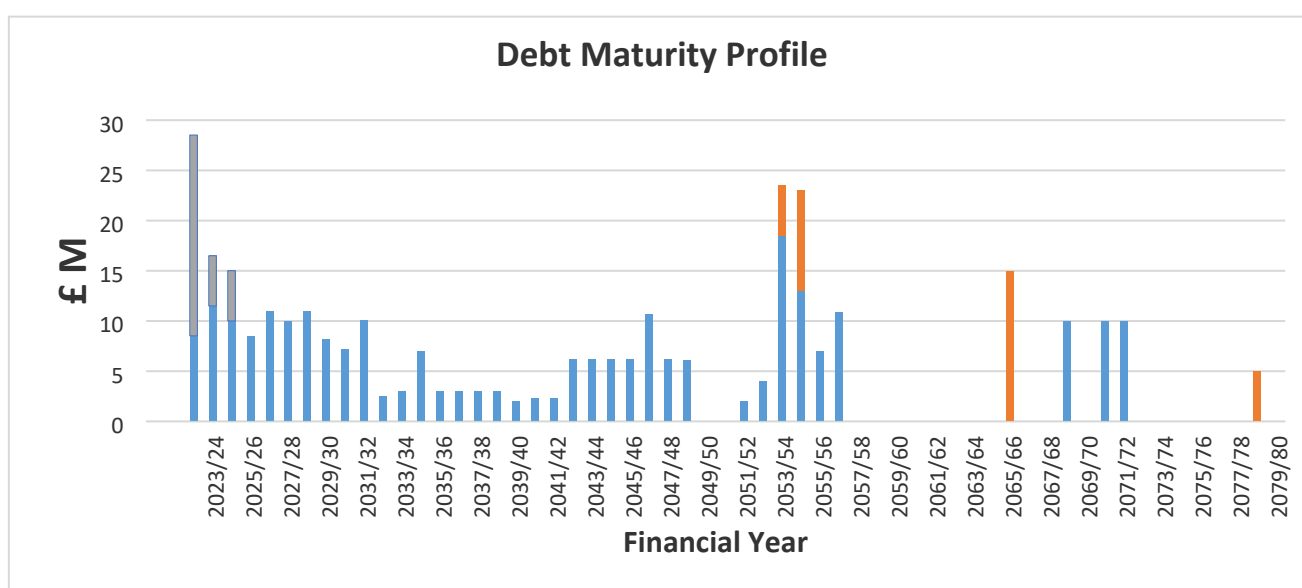
3.20 Effective management of the Authority's debt is essential to ensure that the impact of interest payable is minimised against our revenue accounts whilst maintaining prudent borrowing policies.

3.21 A prohibition is still in place to deny access to borrowing from the PWLB for any local authority which had purchase of assets for yield in its three year capital programme. There are currently no schemes for yield in the Capital Programme. With the significant amounts of borrowing in the future Capital Programme, the inability to access PWLB borrowing will need to be a major consideration for any future purchases of assets for yield. The additional income these assets generate must be sufficient to cover the increased borrowing costs, as borrowing sources other than the PWLB are likely to be more expensive.

3.22 The following table outlines the councils borrowing at the 31st March. When this is compared to the CFR figure for 31st March 2022, the Authority being under borrowed by £33.96 million. Using cash reserves as opposed to borrowing has been a prudent and cost-effective approach over the last few years. However, members will be aware that internal borrowing is only a temporary situation and officers have advised that, based on capital estimates, it will be necessary for the Authority to borrow at stages over the next few years.

£'m	2020/21	2021/22
PWLB	238.19	260.64
Market Loans	35.00	35.00
Inter Authority Borrowing	50.00	30.00
GCRE Repayable Funding	33.00	33.00
Zero % Loans	3.34	3.73
Sub Total	359.53	362.37
Celtic Energy S106	19.50	8.87
Total	379.03	371.25

3.23 Debt Maturity Profile as at 31st March 2022.



Key Blue = PWLB; Grey = Inter Authority Borrowing; Orange = Market Loans

3.24 No external borrowing was required during the last quarter of 2021/22.

3.25 A total of £7.5 million PWLB and £30 million of borrowing from other local authorities and has been repaid during the year. During the year £30 million of borrowing was sourced from the PWLB with a further £10 million sourced from other local authorities.

3.26 The staged repayment of the Nant Helen section 106 deposit is continuing as the backfilling works on the site progress, this is shown in the earlier table. This is also reducing the cash position of the authority; this repayment will reduce the amount the council is under borrowed.

3.27 With the changes to the MRP policy and the delayed requirement to borrow, the revenue budget set aside to cover these costs has been underutilised in this financial year, however as demonstrated in the tables later in the report, these costs are likely to increase year on year.

3.28 PWLB Loans Rescheduling

3.29 Debt rescheduling opportunities have been very limited in the current economic climate and following the various increases in the margins added to gilt yields which have impacted PWLB new borrowing rates since October 2010. No debt rescheduling has therefore been undertaken to date in the current financial year.

3.30 Financing Costs to Net Revenue Stream

3.31 This indicator identifies the trend in the cost of capital, (borrowing and other long term obligation costs net of investment income), against the Councils net revenue budget (net revenue stream). The estimates of financing costs include current commitments and the proposals in the capital programme.

£'m	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
From the approved Treasury Management and Capital Strategy 2021/22			
Financing Costs	13.59	16.55	17.61
Net Revenue Stream	279.81	281.26	282.17
%	4.8%	5.9%	6.2%
Quarter 1 estimates (before any over provision)			
Financing Costs	11.14	13.09	14.35
Net Revenue Stream	279.81	281.26	282.17
%	4.0%	4.7%	5.1%
Quarter 2 estimates (before any over provision)			
Financing Costs	10.70	11.73	12.89
Net Revenue Stream	279.81	281.26	282.17
%	3.8%	4.2%	4.6%
Quarter 3 estimates (before any over provision)			
Financing Costs	10.85	11.29	12.17
Net Revenue Stream	279.81	302.33	314.29
%	3.9%	3.7%	3.9%
Actual Position			
Financing Costs	10.89	TBC	
Net Revenue Stream	279.81		
%	3.9%		

3.32 The table above shows the capital financing costs incurred in 2021/22 and the change between those disclosed in the Treasury Management and Capital Strategy included as part of the 2021/22 Budget report.

3.33 The decrease has been caused by three factors.

1. The updated Minimum Revenue Policy (MRP) approved by Council in March 2021 has realigned these costs more equally across the life of the assets involved.
2. The reduced borrowing requirement to support the capital programme in 2020/21 and future years. This has been the result of reprofiling of budgets into future years and funding from Welsh Government being made available earlier than anticipated. This has allowed the council to defer the date that it expected to take out additional borrowing, reducing the current interest costs, however this borrowing will still be required in the future.
3. As outlined in the amendment of the 2022/23 Budget approved by Council on the 3rd March 2022, the additional funds provided by Welsh Government, Capital (£3.6m) and Revenue (£2.3m), together with the projected underspend on MRP for 2021/22 (£1.5m) has been used to fund existing Capital schemes.

3.34 Prudential Indicators

3.35 All Treasury Management Prudential Indicators were complied with in the quarter ending 31st March 2022.

3.36 Economic Background and Forecasts

3.37 The forecast of interest rates by the Authority's advisor at the 31st March 2022 are shown below, an increase in the rates is expected over the next few years which will increase the cost of borrowing.

Link Group Interest Rate View		7.2.22											
	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25
BANK RATE	0.75	1.00	1.00	1.25	1.25	1.25	1.25	1.25	1.25	1.25	1.25	1.25	1.25
3 month av. earnings	0.80	1.00	1.00	1.20	1.20	1.20	1.20	1.20	1.20	1.20	1.20	1.20	1.20
6 month av. earnings	1.00	1.10	1.20	1.30	1.30	1.30	1.30	1.30	1.30	1.30	1.30	1.30	1.30
12 month av. earnings	1.40	1.50	1.60	1.70	1.70	1.60	1.60	1.50	1.40	1.40	1.40	1.40	1.40
5 yr PWLB	2.20	2.30	2.30	2.30	2.30	2.30	2.30	2.30	2.30	2.30	2.30	2.30	2.30
10 yr PWLB	2.30	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40
25 yr PWLB	2.40	2.50	2.50	2.60	2.60	2.60	2.60	2.60	2.60	2.60	2.60	2.60	2.60
50 yr PWLB	2.20	2.30	2.30	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40

3.38 The economic background provided by our treasury advisers; Link Group at the 31st March 2022 is attached at Appendix A.

3.39 VAT

3.40 The Technical Section of Finance act as the authority's VAT section. VAT can pose a risk to the authority hence this report includes VAT information.

3.41 The monthly VAT returns were submitted within the required deadlines during this quarter.

3.42 Key Performance Indicators - The VAT KPI's for 2021/22 are attached at Appendix B.

4. Resource Implications

a. N/A

5. Legal implications

5.1 N/A

6. Data Protection

6.1 N/A

7. Comment from local member(s)

7.1 N/A

8. Impact Assessment

8.1 N/A

9. Recommendation

9.1 This report has been provided for information and there are no decisions required. It is recommended that this report be accepted.

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Head of Service:	Jane Thomas

Appendix A

Economics update, provided by Link.

Note:

This was produced by Link in the April 2022 as a review of January to March 2022. Since this was drafted unprecedented global factors are having significant impacts on all areas of the economy.

The first quarter of 2022 saw:

- A 0.8% m/m rise in GDP in January more than reverse December's Omicron-induced 0.2% m/m fall;
- Signs that the economy has been resilient to the war in Ukraine so far;
- A further rise in CPI inflation to a new 30-year high of 6.2% in February;
- A fall in the unemployment rate to 3.9% and a diminished supply of workers fuelling faster wage growth;
- Bank Rate rising by 50bps, taking Bank Rate to the pre-virus and post-Global Financial Crisis high of 0.75%;
- The war in Ukraine contribute to financial conditions being as tight as after the Brexit vote in 2016.

The UK economy got off to a good start in Q1, growing by 0.8% m/m in January. That more than reversed the 0.2% m/m fall in December triggered by the Omicron wave. It took GDP 0.8% above the pre-virus February 2020 level.

The survey data suggest that the economy continued to rebound swiftly in February. The S&P Global/CIPS all-sector Purchasing Managers Index rose from 54.4 in January to an eight-month high of 59.8 in February, suggesting near-term annualised growth in the region of 5%. The economy has proven resilient to the effects of the war in Ukraine so far but whether it can ride out the upcoming cost-of-living squeeze is a matter of conjecture.

In Q4, all the solid 1.3% q/q rise in nominal household disposable income was wiped out by a 1.4% q/q rise in consumer prices. That meant that real household incomes fell by 0.1% q/q, the third fall in a row. And the GfK measure of consumer confidence has now fallen for four consecutive months, reaching a 17-month low in March.

With inflation set to keep rising, households are in for a prolonged period of negative real wage growth. The surge in CPI inflation to a new 30-year high of 6.2% in February means that it is now more than three times the Bank of England's 2% target. The rise in core inflation

(excluding energy, food and alcohol) from 4.4% in January to 5.2% in February also left it at a 30-year high. A 1.0% m/m price rise this February meant that food and drink inflation rose from 4.3% to 5.1%. That was the highest rate since September 2011.

CPI inflation is expected to peak at around 8.3% in April and will stay above 7.0% for most of 2022 and above 3.0% for most of 2023. The scheduled 54% rise in utility prices on 1st April will add an extra 1.4ppts to CPI inflation in April. And the surge in agricultural commodity prices triggered by the war in Ukraine means that food price inflation is expected to soon climb above 6%.

The Chancellor announced some support for households in his Spring Fiscal Statement in March, in the form of tax cuts. Despite the downward revision to the Office for Budget Responsibility's (OBR) real GDP growth forecast for this year (from 6.0% to 3.8%) and for next year (from 2.1% to 1.8%), the OBR's public finances forecasts still improved and gave the Chancellor a windfall of about £20bn. Nevertheless, the £9.2bn (0.4% of GDP) package for 2022/23, or £18.2bn (0.8% of GDP) if the support measures announced in February are included, will help to offset about half the blow to household finances from higher energy and food bills.

Households are drawing on their estimated £161bn of excess savings to offset lower real incomes. The household saving rate dropped from 7.5% in Q3 to 6.8% in Q4. And the £4.0bn rise in cash sitting in households' bank accounts in February, which was smaller than the 2019 average rise of £4.6bn, suggests that households have stopped adding to their excess savings and have begun to reduce them.

Meanwhile, the tight labour market will fuel the Bank of England's fears that high inflation is feeding through into a rise in wage growth that will feed back into inflation. The unemployment rate fell from 4.1% in December to 3.9% in January. That is only just above the pre-virus rate of 3.8%.

Job vacancies increased to a new record high of 1.3 million in February and maintained the upward pressure on wage growth. The 3myy rate of average earnings growth rose from 4.6% in December to 4.8% in January. And earnings excluding bonuses rose by another strong 0.4% m/m, which lifted its 3myy rate from 3.7% to 3.8%.

Meanwhile, the lasting financial market effects from the war in Ukraine so far appear to be higher commodity prices, higher interest rate expectations and wider corporate bond spreads. UK financial conditions have tightened to levels similar to those seen after the Brexit referendum in 2016.

Gilt yields have risen back above their pre-war levels, driven largely by an increase in breakeven inflation rates.

MPC meetings 4th February and 17th March 2022

- 4 After the Bank of England became the first major western central bank to put interest rates up in this upswing in December, it has quickly followed up its first 0.15% rise by a further two 0.25% rises to 0.75%, in what is very likely to be a series of increases during 2022.
- 5 The Monetary Policy Committee voted by a majority of 5-4 to increase Bank Rate by 25bps to 0.5% on 4th February, with the minority preferring to increase Bank Rate by 50bps to 0.75%. The Committee also voted unanimously for the following: -
 - a. to reduce the £875n stock of UK government bond purchases, financed by the issuance of central bank reserves, by ceasing to reinvest maturing assets.
 - b. to begin to reduce the £20bn stock of sterling non-financial investment-grade corporate bond purchases by ceasing to reinvest maturing assets and by a programme of corporate bond sales to be completed no earlier than towards the end of 2023.
- 6 The Bank again sharply increased its forecast for inflation – to now reach a peak of 7.25% in April, well above its 2% target.
- 7 The Bank estimated that UK GDP rose by 1.1% in quarter 4 of 2021 but, because of the effect of Omicron, GDP would be flat in quarter 1, but with the economy recovering during February and March. Due to the hit to households' real incomes from higher inflation, it revised down its GDP growth forecast for 2022 from 3.75% to 3.25%.
- 8 The Bank is concerned at how tight the labour market is with vacancies at near record levels and a general shortage of workers - who are in a very favourable position to increase earnings by changing job.
- 9 By the time the MPC met in March, the Russian invasion of Ukraine was well established. Serious supply side shocks impacting energy and food stuffs, as well as impediments to global trade, had persuaded MPC members, by a majority of 8-1, to increase Bank Rate to 0.75% but caution as to the extent of further increases was emphasised. One member of the MPC wanted rates to stay on hold at 0.5%.
- 10 The CPI measure of inflation is now expected to exceed 8% in Q1 2022/23, and despite measures announced by the Chancellor in his Spring Fiscal Statement to try to reduce the impact of the cost-of-living squeeze on households by reducing fuel duty by 5p a litre and increasing the threshold for employees paying National Insurance by £3,000 from July, we are still about to see the biggest squeeze on households' living standards for over 50 years.
- 11 **The MPC's forward guidance on its intended monetary policy** on raising Bank Rate versus selling (quantitative tightening) holdings of bonds is as follows: -
 - a. Raising Bank Rate as "the active instrument in most circumstances".

- b. After Bank Rate hit 0.50% to start reducing its gilt/bond holdings and to stop reinvesting maturing gilts.

Interest rate forecasts

The Council has appointed Link Group as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. The PWLB rate forecasts below are based on the Certainty Rate (the standard rate minus 20 bps) which has been accessible to most authorities since 1st November 2012.

The latest forecast on 4th February is compared below to the last forecast (20th December) in the previous quarter. A comparison of these forecasts shows that PWLB rates have increased generally and show a speed up in the rate of increase in Bank Rate as inflation is now posing a greater risk. The increase in PWLB rates reflects a broad sell-off in sovereign bonds internationally as inflation concerns abound. To that end, the MPC has tightened short-term interest rates with a view to trying to slow the economy sufficiently to keep the secondary effects of inflation – as measured by wage rises – under control, but without pushing the economy into recession. A difficult juggling act at the best of times, and now against a backdrop of the Russian invasion of Ukraine.

Link Group Interest Rate View 7.2.22														
	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	
BANK RATE	0.75	1.00	1.00	1.25	1.25	1.25	1.25	1.25	1.25	1.25	1.25	1.25	1.25	
3 month av. earnings	0.80	1.00	1.00	1.20	1.20	1.20	1.20	1.20	1.20	1.20	1.20	1.20	1.20	
6 month av. earnings	1.00	1.10	1.20	1.30	1.30	1.30	1.30	1.30	1.30	1.30	1.30	1.30	1.30	
12 month av. earnings	1.40	1.50	1.60	1.70	1.70	1.60	1.60	1.50	1.40	1.40	1.40	1.40	1.40	
5 yr PWLB	2.20	2.30	2.30	2.30	2.30	2.30	2.30	2.30	2.30	2.30	2.30	2.30	2.30	
10 yr PWLB	2.30	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	
25 yr PWLB	2.40	2.50	2.50	2.60	2.60	2.60	2.60	2.60	2.60	2.60	2.60	2.60	2.60	
50 yr PWLB	2.20	2.30	2.30	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	

Link Group Interest Rate View 20.12.21														
	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	Mar-25
BANK RATE	0.25	0.25	0.50	0.50	0.50	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.25
3 month ave earnings	0.20	0.30	0.50	0.50	0.60	0.70	0.80	0.90	0.90	1.00	1.00	1.00	1.00	1.00
6 month ave earnings	0.40	0.50	0.60	0.60	0.70	0.80	0.90	1.00	1.00	1.10	1.10	1.10	1.10	1.10
12 month ave earnings	0.70	0.70	0.70	0.70	0.80	0.90	1.00	1.10	1.10	1.20	1.20	1.20	1.20	1.20
5 yr PWLB	1.40	1.50	1.50	1.60	1.60	1.70	1.80	1.80	1.80	1.90	1.90	1.90	2.00	2.00
10 yr PWLB	1.60	1.70	1.80	1.80	1.90	1.90	2.00	2.00	2.00	2.10	2.10	2.10	2.20	2.30
25 yr PWLB	1.80	1.90	2.00	2.10	2.10	2.20	2.20	2.20	2.30	2.30	2.40	2.40	2.50	2.50
50 yr PWLB	1.50	1.70	1.80	1.90	1.90	2.00	2.00	2.00	2.10	2.10	2.20	2.20	2.30	2.30

A SUMMARY OVERVIEW OF THE FUTURE PATH OF BANK RATE

- The threat from Omicron was a wild card causing huge national concern at the time of December's MPC meeting; now despite record numbers of infection, the relatively low number of hospitalisations suggests there will be no further lockdowns (at least over spring and summer).

- The MPC has now set out upon a monetary policy tightening spree. In March it voted 8-1 for rates to increase to 0.75%.
- Our forecast now expects the MPC to deliver another 0.25% increase in May to 1%; their position appears to be to go for sharp increases to get the job done and dusted but the cost-of-living squeeze will provide a headwind to tightening too far and too quickly, so for now we only have a further 0.25% increase in place for H2 2022.
- If, however, the MPC is becomes more heavily focused on combating inflation than on protecting economic growth, we will revise our forecast up further.
- However, 54% energy cap cost increases from April, together with 1.25% extra employee national insurance, food inflation around 5% and council tax likely to rise in the region of 5% too - these increases are going to hit lower income families hard despite some limited assistance from the Chancellor to postpone the full impact of rising energy costs.
- Consumers are estimated to be sitting on over £160bn of excess savings left over from the pandemic so that will cushion some of the impact of the above increases. But most of those holdings are held by more affluent people whereas poorer people already spend nearly all their income before these increases hit and have few financial reserves.
- The BIG ISSUE – will the current spike in inflation lead to a second-round effect in terms of labour demanding higher wages, (and/or lots of people getting higher wages by changing job)?
- If the labour market remains very tight during 2022, then wage inflation poses a greater threat to overall inflation being higher for longer, and the MPC may then feel it needs to take more action.

PWLB RATES

- The yield curve has flattened out considerably.
- We view the markets as having built in, already, nearly all the effects on gilt yields of the likely increases in Bank Rate.
- It is difficult to say currently what effect the Bank of England starting to sell gilts will have on gilt yields once Bank Rate rises to 1%: it is likely to act cautiously as it has already started on not refinancing maturing debt. A passive process of not refinancing maturing debt began in March when the 4% 2022 gilt matured; the Bank owns £25bn of this issuance. A pure roll-off of the £875bn gilt portfolio by not refinancing bonds as they mature, would see the holdings fall to about £415bn by 2031, which would be about equal to the Bank's pre-pandemic holding. Last August, the Bank said it would not actively sell gilts until the *“Bank Rate had risen to at least 1%”* and, *“depending on economic circumstances at the time.”*
- It is possible, but unlikely, that Bank Rate will not rise above 1% as the MPC could shift to relying on quantitative tightening (QT) to do the further

work of taking steam out of the economy and reducing inflationary pressures.

- Increases in US treasury yields over the next few years could add upside pressure on gilt yields though, more recently, gilts have been more correlated to movements in bund yields than treasury yields.

Forecasts for PWLB rates and gilt and treasury yields

The current PWLB rates are set as margins over gilt yields as follows: -

1. PWLB Standard Rate is gilt plus 100 basis points (G+100bps)
2. PWLB Certainty Rate is gilt plus 80 basis points (G+80bps)
3. PWLB HRA Standard Rate is gilt plus 100 basis points (G+100bps)
4. PWLB HRA Certainty Rate is gilt plus 80bps (G+80bps)
5. Local Infrastructure Rate is gilt plus 60bps (G+60bps)

Gilt yields. Since the start of 2021, we have seen a lot of volatility in gilt yields, and hence PWLB rates. Our current forecasts reflect much of the recent increases seen in global bond market yields generally since the turn of the year (2022).

Upside risk to gilt yield forecasts. While monetary policy in the UK will have a major impact on gilt yields, there is also a need to consider the potential impact that rising treasury yields in America could have on UK gilt yields. **As an average since 2011, there has been a 75% correlation between movements in US 10-year treasury yields and UK 10-year gilt yields.** This is a significant upward risk exposure to our forecasts for longer term PWLB rates. However, gilt yields and treasury yields do not always move in unison.

US treasury yields. US President Biden and the Democratic party have pushed through a huge programme of fiscal stimulus over the past couple of years, whilst the following factors were also in play: -

- 12 A fast vaccination programme had enabled a rapid opening up of the economy during 2021.
- 13 The economy has been growing swiftly over the second half of 2021/22, whilst unemployment has continued to fall/spare capacity in the labour market has tightened.

It was not much of a surprise that a combination of these factors would eventually cause an excess of demand in the economy which generated strong inflationary pressures. This has eventually been recognised by the Fed and an aggressive response to damp inflation down during 2022 and 2023 is expected.

The flurry of comments from Fed officials following the mid-March meeting – including from Chair Jerome Powell himself – hammering home the hawkish message from the mid-March meeting makes it difficult to see how the Fed will not tighten aggressively through 2022 as a minimum with markets expecting the Fed Funds Rate to hit close to 2% by year end.

In addition, the Fed will soon announce an increasing series of caps on the value of assets they allow to run off the balance sheet each month. That announcement could come as soon as May.

Downside risk to gilt yield forecasts. There are also possible downside risks from the huge sums of cash that the UK populace have saved during the pandemic; when savings accounts earn little interest, it is likely that some of this cash mountain could end up being invested in bonds and so push up demand for bonds and support their prices i.e., this would help to keep their yields down. How this will interplay with the Bank of England not reinvesting maturing gilts and then later selling gilts, will be interesting to monitor.

Significant risks to the forecasts

- 14 COVID vaccines do not work to combat new mutations and/or new vaccines take longer than anticipated to be developed for successful implementation.
- 15 The Government implements fiscal policies that suppresses GDP growth.
- 16 The MPC tightens monetary policy too quickly – by raising Bank Rate or unwinding QE.
- 17 The MPC tightens monetary policy too late to ward off building inflationary pressures.
- 18 Geo-political risks - on-going global power influence struggles between Russia/China/US/Iran and the Russian invasion of Ukraine.

The balance of risks to the UK economy: -

- 19 The overall balance of risks to economic growth in the UK is now to the downside unless excess savings are deployed by consumers to maintain their spending despite the cost-of-living squeeze.

The balance of risks to medium to long term PWLB rates: -

- 20 There is a balance of upside risks to forecasts for medium to long term PWLB rates because of the lengthy increase in inflation (>6% for the remainder of 2022 and only reducing slowly through 2023).

Appendix B

VAT - Key Performance Indicators

Creditor Invoices

VAT return for	No of high value Creditor invoices checked	No of Creditor invoices highlighted as requiring "proper" document for VAT recovery	% of creditor invoices checked requiring "proper" document for VAT recovery
Apr-21	205	0	0.00%
May-21	209	1	0.48%
Jun-21	286	1	0.35%
Jul-21	259	1	0.39%
Aug-21	189	0	0.00%
Sep-21	259	1	0.39%
Oct-21	253	0	0.00%
Nov-21	267	2	0.75%
Dec-21	229	1	0.44%
Jan-22	242	1	0.41%
Feb-22	286	2	0.70%
Mar-22	440	10	2.27%

Income Management Entries

VAT return for	No of entries checked by formula per the ledger account code used	No of entries needing follow up check (but not necessarily incorrect).	% of entries needing follow up check
Apr-21	697	0	0.00%
May-21	847	2	0.24%
Jun-21	972	4	0.41%
Jul-21	860	8	0.93%
Aug-21	869	0	0.00%
Sep-21	636	20 ¹	3.14%
Oct-21	892	2	0.22%
Nov-21	777	1	0.13%
Dec-21	866	0	0.00%
Jan-22	1,057	0	0.00%
Feb-22	1,083	0	0.00%
Mar-22	1,487	2	0.13%

¹ These relate to two cash amounts, but one of them was NMWTRA which is split over many budgets so is counted per budget line for consistency with past statistics.

Debtor Invoices

VAT return for	No of Debtor invoices checked	No of checked debtor invoices with incorrect VAT code used	% of debtor invoices with incorrect VAT code
Apr-21	88	0	0.00%
May-21	82	0	0.00%
Jun-21	86	0	0.00%
Jul-21	95	0	0.00%
Aug-21	72	0	0.00%
Sep-21	193	1	0.52%
Oct-21	105	0	0.00%
Nov-21	107	0	0.00%
Dec-21	145	0	0.00%
Jan-22	145	0	0.00%
Feb-22	110	13 ²	11.82%
Mar-22	203	0	0.00%

² Error was in HMRC's favour however as discovered in period there will be no loss to PCC except for the time needed to cancel and re-raise the invoices correctly.

Note: Debtors VAT checking is carried out by Finance via a work process prior to the invoice being raised hence the improvement in errors compared to previous years

Purchase Cards

VAT return for	No of transactions for which paperwork requested for checking	Resolvable errors discovered	Value of VAT potentially claimable but recharged to budget due to non- response	No of transactions where VAT claimed incorrectly	% of transactions available to be checked where VAT was claimed incorrectly	Value of VAT incorrectly claimed hence recharged to budget
Apr-21	193	15	£2,000.55	14	7.25%	£555.26
May-21	144	5	£1,165.80	16	11.11%	£849.52
Jun-21	153	5	£1,083.04	28	18.30%	£726.18
Jul-21	123	6	£1,289.84	23	18.70%	£858.25
Aug-21	61	5	£730.68	1	1.64%	£5.00
Sep-21	151	14	£1,028.56	9	5.96%	£711.13
Oct-21	93	2	£384.00	10	10.75%	£294.07
Nov-21	127	2	£621.25	12	9.45%	£830.02
Dec-21	155	3	£692.09	30	19.35%	£1,307.69
Jan-22	106	6	£520.22	21	19.81%	£6,652.83
Feb-22	92	5	£420.46	18	19.57%	£691.10
Mar-22	263	23	£6,036.91	25	9.51%	£912.85

Chargebacks to service areas

The upload of appropriate documents to the Barclaycard purchase card system to enable vat recovery was made mandatory in September 2017 as a result of the lack of response from service areas/establishments to provide documents when requested. Where no document has been uploaded, any VAT amount input against the transaction is charged to the service area as there is no evidence to support the vat recovery.

Any other VAT errors that come to light as a result of the various checks are also charged to the relevant service areas.

Budget holders are able to see this clearly as chargebacks are coded to account code EX400600 and the activity code used alongside this gives the reason why this chargeback has occurred.

The total amount charged back to service areas in 2021/22 was £130,279. The breakdown of this is as follows:

Potentially correctable errors

Reason	Amount £
Not a tax invoice ³	(21,490)
Powys County Council is not the named customer	0
No invoice uploaded to purchase card system	53,743
Invoice(s) do not match payment	4,273
No evidence to back recovery	252
No Signed Authenticated Receipt ⁴	85,130
Total	121,908

³ Includes VAT successfully recovered relating to errors in previous years

⁴ The majority of this figure relates to capital schemes and officers have obtained the relevant documentation and this will be refunded in 2022/23

Other errors

Reason	Amount £
Non-domestic VAT	145
No tax on invoice	3,156
Supply not to Powys County Council	1,794
Over-accounting for VAT	3,250
Internal payments	26
Total	8,371