CYNGOR SIR *POWYS* COUNTY COUNCIL.

AUDIT COMMITTEE
29th September 2023

CABINET EXECUTIVE
19th September 2023

REPORT AUTHOR:	**County Councillor David Thomas** **Portfolio Holder for Finance and Corporate Transformation**
REPORT TITLE:	**Treasury Management Quarter 1 Report**
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 30th June 2023.

2 Background

2.1 The Capital and Treasury Management Strategy (CTMS) approved by Full Council on 23rd February 2023 can be found here - powys.moderngov.co.uk/documents/s77379/Appendix H Capital and Treasury Management Strategy 2023-28.pdf

3 Advice

3.1 Investments

3.2 The Authority's investment priorities within the Strategy are.

(a) the security of capital, then,
(b) the liquidity of its investments then
(c) the yield

3.3 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. With interest rates for investments remaining lower than borrowing rates, the use of cash reserves as opposed to borrowing is prudent and cost-effective.

3.4 Short-term money market investment rates have continued to increase following the two increases to the Bank Rate in the last quarter. Due to the uncertainty around the short term cash requirements, we have continued to hold any surplus funds in the council's deposit accounts. These funds have earned interest totalling £0.16 million for the first quarter of this financial year.

3.5 Investment returns on inter-authority lending have increased in line with the increased interest rates. 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.

3.6 The Authority had no other investments on 30th June 2023.

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

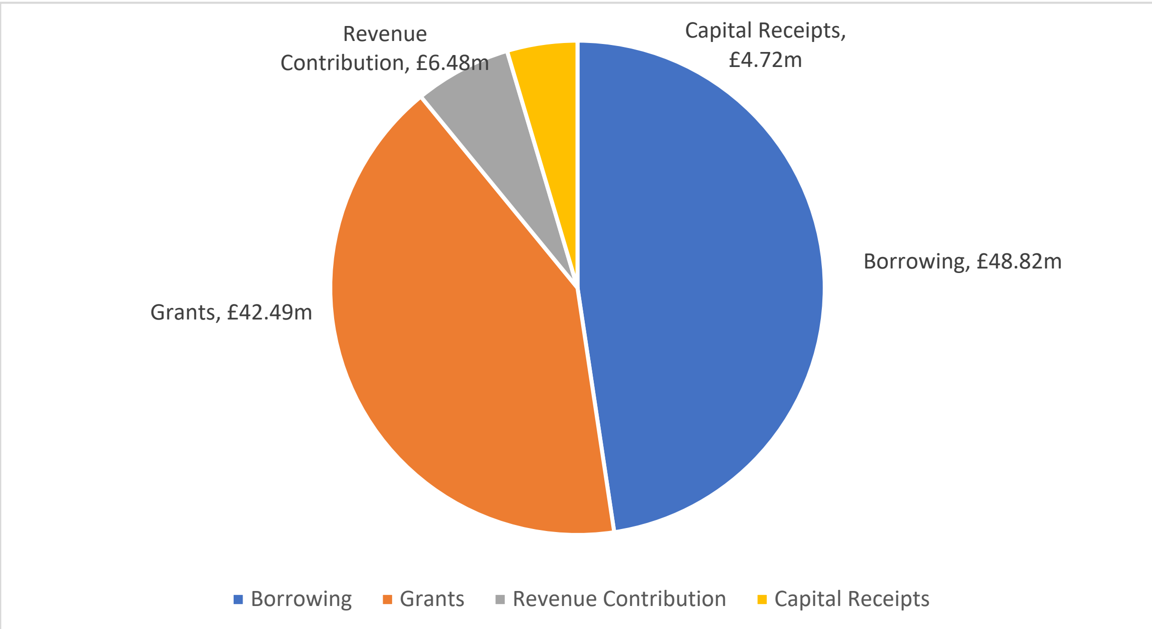
3.10 The 2023/24 Capital Programme was approved by Council on the 23rd February 2023. It included capital schemes totalling £93.29 million, of which £23.48 million related to the Housing Revenue Account (HRA). The programme has been updated following the reprofiling of projects and additional grants received from Welsh Government. The revised programme at the 30th June 2023 is budgeted at £102.50 million following the successful award of additional grants and the reprofiling of budgets between financial years. Actual spend amounts to £7.61 million, representing 7.4% of the total budget.

3.11 Table 1 - Breakdown by service

Service	Original Budget	Virements Approved	Revised Budget	Actuals	Commitments	Remaining Budget	
	£,000	£,000	£,000	£,000	£,000	£,000	%
Adult Services	200	922	1,122	6	240	1,116	99.5%
Childrens Services	0	379	379	23	43	356	93.9%
Education	33,005	(4,862)	28,143	3,047	11,193	25,096	89.2%
Highways Transport & Recycling	12,681	6,135	18,816	2,513	4,557	16,303	86.6%
Property, Planning & Public Protection	100	998	1,098	50	237	1,048	95.4%
Community Development	922	1,337	2,259	(42)	739	2,301	101.9%
Housing General Fund	1,748	1,279	3,027	533	461	2,494	82.4%
Economy & Digital Services	16,196	(1,690)	14,506	(344)	7,908	14,850	102.4%
Finance	4,953	(454)	4,499	0	75	4,499	100.0%
Total Capital	**69,805**	**4,044**	**73,849**	**5,786**	**25,453**	**68,063**	**92.2%**
Housing Revenue Account	23,482	5,165	28,647	1,826	4,822	26,821	93.6%
TOTAL	**93,287**	**9,209**	**102,496**	**7,612**	**30,275**	**94,884**	**92.6%**

3.12 Currently 48%, £48.82 million, of the capital expenditure is budgeted to be financed by borrowing, the interest cost for this is charged to the revenue account. Finance will be working with the services to ensure the profiling of budgets is accurate to effectively manage the borrowing.

3.13 Chart 1 – Capital Programme funding



3.14 Inflation continues to have a severe impact on the cost of schemes due to rising material and construction costs. It is unclear at this stage how this will impact the programme over the coming years. Services are aware of the impact and are mitigating these increases as far as possible but is likely that schemes will be reduced or paused. Any additional funding required is likely to be raised with further borrowing, this will increase costs on the revenue budget so must be minimised.

3.15 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.

3.16 Part of the Council's treasury activities is to address the funding requirements for this borrowing need. Depending on the capital expenditure, the Council's cash position is managed 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.

3.17 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.

3.18 Capital Financing Requirement (CFR)

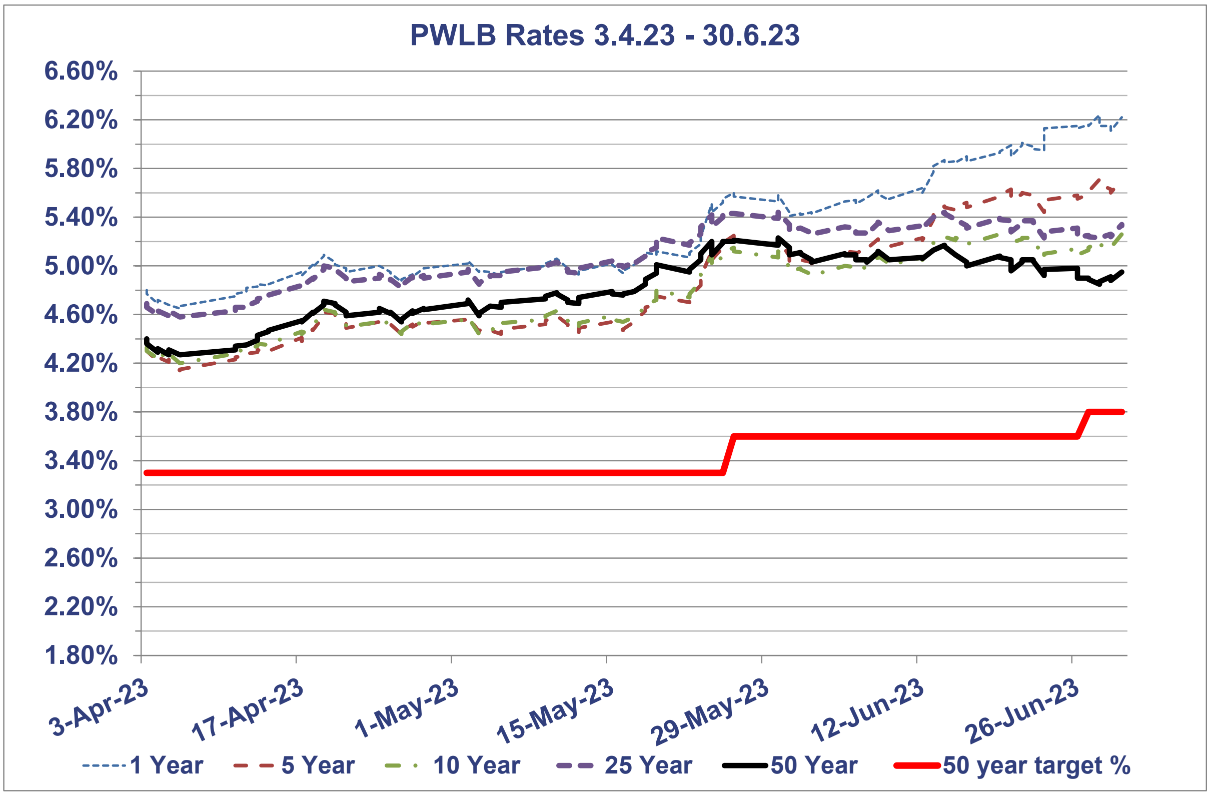
£'m	Total	HRA	Council Fund
Opening Balance – 1st April 2023			
Original Estimates[1]	**439.71**	108.5	331.21
Actual Balance	**422.21**	104.31	317.90
Closing Balance – 31st March 2024			
Original Estimates[1]	**466.79**	119.45	347.34
Quarter 1 Estimate	**465.53**	120.76	344.77
Closing Balance – 31st March 2025			
Original Estimates[1]	**498.71**	135.79	362.92
Quarter 1 Estimate	**497.81**	136.75	361.06
Closing Balance – 31st March 2026			
Original Estimates[1]	**536.72**	157.13	379.59
Quarter 1 Estimate	**529.73**	157.74	369.99

[1] Original estimate included in the CTMS approved by Full Council on 23rd February 2023.

3.19 Borrowing / Re-scheduling

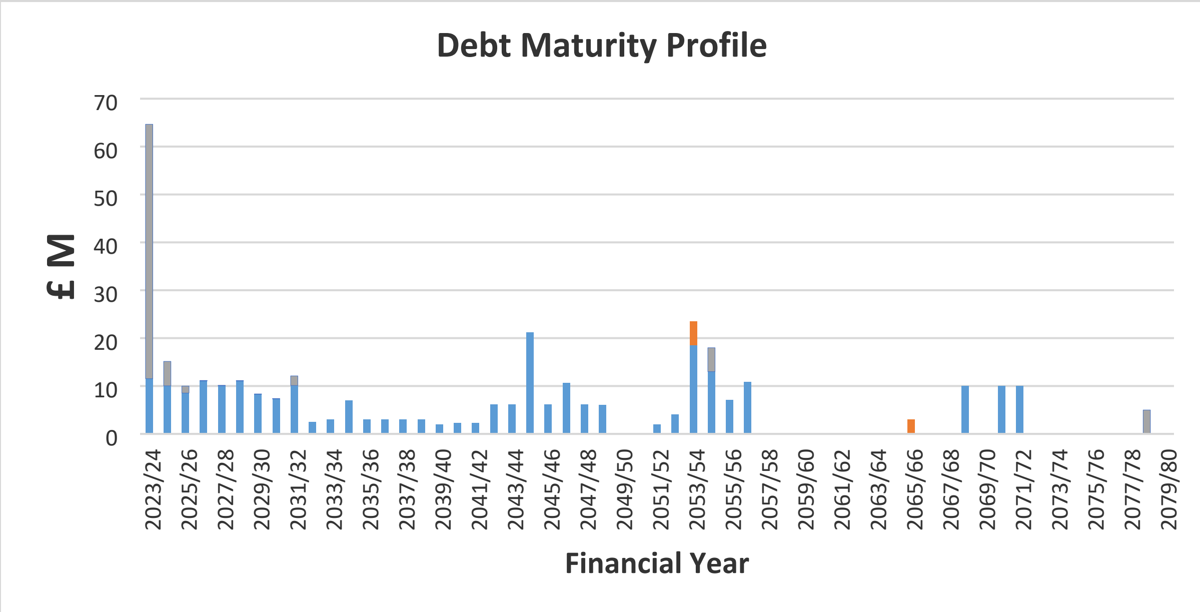
3.20 Effective management of the Authority's debt is essential to ensure that the impact of interest payable is minimised against our revenue accounts whilst maintaining prudent borrowing policies.

3.21 The chart below shows the changes in PLWB interest rates since the start of the April 20223. PWLB borrowing rates are based on the Gilts market. Overall, rates have increased since the last report but remain significantly higher than the 50 year target.



3.22 A prohibition is still in place to deny access to borrowing from the Public Works Loan Board (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.

3.23 Debt Maturity Profile



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

3.24 £5.00 million borrowing from another local authority has been repaid during the last quarter together, this has been refinanced by the PWLB borrowing that was taken out in late March 2023. With the uncertain economic position and as outlined by Link later in this report, it is anticipated that borrowing rates will fall over the next few years, so we need to ensure that the council isn't locked into higher rate borrowing for long periods, to allow flexibility to take advantage should rates drop.

3.25 A further £1.50 million PWLB is due to be repaid in the next quarter together with £5.00 million borrowed from another local authority. The council is still holding £17.40 million for the Global Centre of Rail Excellence (GCRE) and had until 31 March 2023 to progress to the full business case position. Correspondence with Welsh Government have since highlighted that the Council would like to return this as it feels the circumstances of the original agreement have changed significantly. Depending on the amounts being repaid during the next quarter it may need to be replaced with some short term borrowing to absorb this repayment alongside the commitments in the capital programme.

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

3.27 PWLB Loans Rescheduling

3.28 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. Existing borrowing rates remain lower than current rates, therefore no debt rescheduling has been undertaken to date in the current financial year.

3.29 Financing Costs to Net Revenue Stream

3.30 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	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate
From the approved CTMS 2023/24			
Financing Costs	13.66	14.49	14.65
Net Revenue Stream	326.54	338.53	348.39
%	*4.2%*	*4.3%*	*4.2%*
Quarter 1 estimates			
Financing Costs	12.71	14.48	14.3
Net Revenue Stream	326.54	338.53	348.39
%	*3.9%*	*4.3%*	*4.1%*

3.31 The table above shows the capital financing costs and the change between those disclosed in the 2023/24 Treasury Management and Capital Strategy. Interest rates are expected to continue to rise in the short term before reducing. There is significant risk that these costs may increase if rates increase faster or do no fall in line with the current forecast. The latest estimates assume that significant further borrowing will be required before the end of the financial year. The amount will depend on the cash position of the council and the interest rates available so this figure may change before the end of the financial year. There is sufficient budget to cover these costs in this financial year, future years increases will need to be factored into the proposed 2024/25 budget.

3.32 The change has been caused by the reduced borrowing requirement to support the capital programme in 2022/23 and future years. This has been the result of reprofiling of budgets into future years. 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.

3.33 Prudential Indicators

3.34 All Treasury Management Prudential Indicators were complied with in the quarter ending 30th June 2023.

3.35 Economic Background and Forecasts

3.36 The forecast of interest rates by the Authority's advisor at the 26th June 2023 are shown below. The rates have fluctuated over the last few months but are expected to reduce slightly over the next few years. The current higher rates will increase the cost of borrowing over the next few years. The revised Medium Term Financial Strategy has been updated to take account of these changes.

Link Group Interest Rate View	26.06.23												
	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26
BANK RATE	5.00	5.50	5.50	5.50	5.25	4.75	4.25	3.75	3.25	2.75	2.75	2.50	2.50
3 month ave earnings	5.30	5.60	5.50	5.30	5.00	4.50	4.00	3.50	3.00	2.70	2.60	2.50	2.50
6 month ave earnings	5.80	5.90	5.70	5.50	5.10	4.60	4.00	3.50	3.00	2.70	2.60	2.60	2.60
12 month ave earnings	6.30	6.20	6.00	5.70	5.30	4.80	4.10	3.60	3.10	2.80	2.70	2.70	2.70
5 yr PWLB	5.50	5.60	5.30	5.10	4.80	4.50	4.20	3.90	3.60	3.40	3.30	3.30	3.20
10 yr PWLB	5.10	5.20	5.00	4.90	4.70	4.40	4.20	3.90	3.70	3.50	3.50	3.50	3.40
25 yr PWLB	5.30	5.40	5.20	5.10	4.90	4.70	4.50	4.20	4.00	3.90	3.80	3.80	3.70
50 yr PWLB	5.00	5.10	5.00	4.90	4.70	4.50	4.30	4.00	3.80	3.60	3.60	3.50	3.50

3.37 The economic background provided by our treasury advisers; Link Group at the 30th June 2023 is attached at Appendix A. It should be noted that this was provided at the end of the quarter and certain factors may have changed since then.

3.38 Sundry Debt

3.39 The prompt collection of debt and encouraging payment as soon as possible helps the Councils cashflow position, reducing the need for short term borrowing.

3.40 The following table outlines the Council's outstanding sundry debt at the 10th July 2023 of £17.29 million, up from £11.64 million last quarter. This does not include Council Tax arrears.

Service	Current Debt (30 days or less)	Aged Debt (31 to 60 days)	Aged Debt (61 - 90 days)	Aged Debt (Over 90 days)	Total Aged Debt	Change from previous quarter	Trend Since Q1 2022/23
Adult Services [2]	**1,387,853**	5,143,697	217,682	6,421,736	**11,783,115**	4,885,980	
Childrens Services	**0**	36,979	989	161,131	**199,099**	26,589	
Corporate, Legal & Democratic Services	**730**	167	0	5,880	**6,047**	(12,854)	
Economy & Digital Services	**48,379**	673	304	71,177	**72,153**	(380,559)	
Finance	**231,582**	85,879	158,464	625,332	**869,675**	188,093	
Highways, Transport & Recycling	**794,568**	262,491	153,384	684,155	**1,100,029**	(68,003)	
Housing	**103,016**	22,088	630	1,027,948	**1,050,665**	392,491	
Community Services	**12,804**	4,006	4,937	43,131	**52,075**	3,536	
Other	**36,776**	5,672	1,606	36,176	**43,454**	(329,872)	
Property, Planning & Public Protection	**280,728**	48,583	34,151	1,374,661	**1,457,394**	630,145	
Schools	**23,130**	198,132	0	390,548	**588,679**	311,688	
Workforce & Organisation Development	**130,816**	40,872	10,434	17,567	**68,872**	(381)	
Total	**3,050,382**	**5,849,237**	**582,579**	**10,859,442**	**17,291,258**	**5,646,854**	

[2] There is a further £0.03 million outstanding debt with the local health board that sits outside this figure.

3.41 The £3.05 million shown in the current debt column relates to invoices that are less than 30 days old, overdue debt is classed as overdue when it is above 30 days after the invoice date.

3.42 The total debt represents 27% of the annual generated income (excluding Council Tax and NNDR), if you exclude the current debt (less than 30 days old) this falls to 23% up from 16% last quarter.

3.43 There is a significant level of aged debt (over 30 days old) which has increased by £5.65 million since the last quarter. The majority of that increase relates to Powys Teaching Health Board (PtHB) debt mainly within adult social care.

3.44 The table in 3.40 shows that around two thirds of the over three month debt is adult social care debt. This is more difficult to collect as Welsh Government will not allow bailiff action on residential care fees and court action only as a last resort. This debt relates to a high proportion of elderly and vulnerable customers, and often deferred charges are placed on their properties, which requires waiting for houses to be sold and estates to be realised which is often a lengthy process.

3.45 The table below shows the key performance indicators since the start of the financial year.

£'m	PtHB Debt	Non PtHB Debt	Total Debt	Deferred Charge Secured	Payments Received	Debt Written off [3]	Collection Rate
April	3.130	13.280	16.410	0.470	7.491	0.000	37%
May	7.350	12.490	19.840	0.404	3.383	0.001	45%
June	6.910	11.990	18.900	0.404	4.288	0.000	48%

[3] Debt is written off in line with the council's debt policy.

3.46 Council Tax and NNDR Collection

3.47 The in-year collection rates at the end of June 2023 (Quarter 1) for Council tax and NNDR are shown below.

Council Tax 27.28% (0.02% down compared to same point during 2022/23)
NNDR 31.33% (5.58% up compared to same point during 2022/23)

3.48 £5.28 million of Council Tax and £0.95 million NNDR remains uncollected from previous financial years. Collection of monies during the ongoing cost of living crisis is challenging, however robust procedures are in place to pursue all monies owed to the Council, both for the current year and previous final years.

3.49 VAT

3.50 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.

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

3.52 Key Performance Indicators - The VAT KPI's for 2023/24 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.

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Appendix A – Update provided by Link Group on the 30th June 2023

1. Economics update

- The first quarter of 2023/24 saw:
  - A 0.2% m/m rise in real GDP in April, partly due to fewer strikes;
  - CPI inflation falling from 10.1% to 8.7% in April, before remaining at 8.7% in May. This was the highest reading in the G7;
  - Core CPI inflation rise in both April and May, reaching a new 31-year high of 7.1%;
  - A tighter labour market in April, as the 3myy growth of average earnings rose from 6.1% to 6.5%;
  - Interest rates rise by a further 75bps over the quarter, taking Bank Rate from 4.25% to 5.00%;
  - 10-year gilt yields nearing the "mini-Budget" peaks, as inflation surprised to the upside.
- The economy has weathered the drag from higher inflation better than was widely expected. The 0.2% m/m rise in real GDP in April, following March's 0.3% m/m contraction will further raise hopes that the economy will escape a recession this year. Some of the strength in April was due to fewer strikes by train workers and teachers in that month. Moreover, some of the falls in activity in other areas in April were probably temporary too. Strikes by junior doctors and civil servants contributed to the fall in health output (0.9% m/m) and the meagre 0.1% m/m increase in public administration.
- The fall in the composite Purchasing Managers Index (PMI) from 54.0 in May to a three-month low of 52.8 in June (>50 points to expansion in the economy, <50 points to contraction) was worse than the consensus forecast of 53.6. Both the services and manufacturing PMIs fell. The decline in the services PMI was bigger (from 55.2 to 53.7), but it remains consistent with services activity expanding by an annualised 2%. The fall in the manufacturing PMI was smaller (from 47.1 to 46.2), but it is consistent with the annual rate of manufacturing output falling from -0.8% in April to around -5.0%. At face value, the composite PMI points to the 0.1% q/q rise in GDP in Q1 2023 being followed by a 0.2% q/q gain in Q2 2023.
- Meanwhile, the 0.3% m/m rise in retail sales volumes in May was far better than the consensus forecast of a 0.2% m/m decline and followed the robust 0.5% m/m rise in April. Some of the rise was due to the warmer weather. Indeed, the largest move was a 2.7% m/m jump in non-store sales, due to people stocking up on outdoor-related goods. But department stores also managed to squeeze out a 0.6% m/m rise in sales and the household goods sub-sector enjoyed a reasonable performance too. Overall, the figures were far better than analysts had expected. In addition, the GfK measure of consumer confidence rebounded from -27 to a 17-month high of -24 in June.
- The recent resilience of the economy has been due to a confluence of factors including the continued rebound in activity after the pandemic, households spending some of their pandemic savings, and the tight labour market and

government handouts both supporting household incomes. That said, as government support fades, real household incomes are unlikely to grow rapidly. Furthermore, higher interest rates will mean GDP is likely to contract later this year. Our central assumption is that inflation will drop to the 2.0% target only if the Bank triggers a recession by raising rates from 5.00% now to at least 5.5% and keeps rates there until at least mid-2024. Our colleagues at Capital Economics estimate that around 60% of the drag on real activity from the rise in rates has yet to bite, and the drag on the quarterly rate of real GDP growth over the next year may be about 0.2ppts bigger than over the past year.

- The labour market became tighter over the quarter and wage growth reaccelerated. Labour demand was stronger than the consensus had expected. The three-month change in employment rose from +182,000 in March to +250,000 in April. Meanwhile, labour supply continued to recover as the size of the labour force grew by 303,000 in the three months to April. That was supported by a further 140,000 decline in inactivity as people returned to work from retirement and caring responsibilities (while inactivity due to long-term sick continued to rise). But it was not enough to offset the big rise in employment, which meant the unemployment rate fell from 3.9% to 3.8%
- The tighter labour market supported wage growth in April, although the 9.7% rise in the National Living Wage on 1st April (compared to the 6.6% increase in April last year) probably had a lot to do with it too. The 3myy rate of average earnings growth reaccelerated from 6.1% to 6.5% (consensus 6.1%) and UK wage growth remains much faster than in the US and the Euro-zone. In addition, regular private sector wage growth increased from 7.1% 3myy to 7.6%, which left it well above the Bank's forecast for it to fall below 7.0%. Overall, the loosening in the labour market appears to have stalled in April and regular private sector wage growth was well above the Bank's forecast.
- CPI inflation stayed at 8.7% in May (consensus 8.4%) and, perhaps more worryingly, core CPI inflation rose again, from 6.8% to a new 31-year high of 7.1%. The rise in core inflation built on the leap from 6.2% in March to 6.8% and means it is accelerating in the UK while it is slowing in the US and the Euro-zone (both fell to 5.3%). A further decline in fuel inflation, from -8.9% to -13.1%, and the second fall in food inflation in as many months, from 19.3% to 18.7%, explained why overall CPI inflation didn't rise. And the scheduled fall in the average annual utility price from £2,500 to £2,074 on 1st July means overall CPI inflation will probably ease in the coming months. But the problem is that the recent surge in core inflation and the reacceleration in wage growth shows that domestic inflationary pressures are still strengthening.
- This suggests the Bank may have more work to do than the Fed or ECB. Indeed, the Bank of England sounded somewhat hawkish in the June meeting. This came through most in the MPC's decision to step up the pace of hiking from the 25bps at the previous two meetings. The 7-2 vote, with only two members voting to leave rates unchanged at 4.50%, revealed support for stepping up the fight against high inflation.
- That said, the Bank has not committed to raising rates again or suggested that 50bps rises are now the norm. What it did say was that "the scale of the recent upside surprises in official estimates of wage growth and services CPI inflation suggested a 0.5 percentage point increase in interest rates was required at this

particular meeting". Moreover, the Committee did not strengthen its forward guidance that any further rate hikes would be conditional on the data. However, it looks highly probable, given the on-going strength of inflation and employment data, that the Bank will need to raise rates to at least 5.5% and to keep rates at their peak until the mid-point of 2024. We still think it is only a matter of time before the rise in rates weakens the economy sufficiently to push it into recession. That is why instead of rising to between 6.00%-6.25%, as is currently priced in by markets, we think rates are more likely to peak between 5.50-6.00%. Our forecast is also for rates to be cut in the second half of 2024, and we expect rates to then fall further than markets are pricing in.

- Growing evidence that UK price pressures are becoming increasingly domestically generated has driven up market interest rate expectations and at one point pushed the 10-year gilt yield up to 4.49% in late June, very close to its peak seen after the "mini-budget". Yields have since fallen slightly back to 4.38%. But growing expectations that rates in the UK will remain higher for longer than in the US mean they are still more than 70 bps above US yields. While higher interest rates are priced into the markets, the likely dent to the real economy from the high level of interest rates is not. That's why we think there is scope for market rate expectations to fall back in 2024 and why we expect the 10-year PWLB Certainty Rate to drop back from c5.20% to 5.00% by the end of this year and to 4.20% by the end of 2024.
- The pound strengthened from $1.24 at the start of April to a one-year high at $1.26 in early May, which was partly due to the risks from the global banking issues being seen as a bigger problem for the US than the UK. The pound then fell back to $1.23 at the end of May, before rising again to $1.28 in the middle of June as the strong core CPI inflation data released in June suggested the Bank of England was going to have to raise rates more than the Fed or ECB in order to tame domestic inflation. However, sterling's strong run may falter because more hikes in the near term to combat high inflation are likely to weaken growth (and, hopefully, at some point inflation too) to such a degree that the policy rate will probably be brought back down, potentially quite quickly, as the economic cycle trends downwards decisively. This suggests that additional rate hikes are unlikely to do much to boost the pound.

  In early April, investors turned more optimistic about global GDP growth, pushing up UK equity prices. But this period of optimism appears to have been short-lived. The FTSE 100 has fallen by 4.8% since 21st April, from around 7,914 to 7,553, reversing part of the 7.9% rise since 17th March. Despite the recent resilience of economic activity, expectations for equity earnings have become a bit more downbeat. Nonetheless, further down the track, more rate cuts than markets anticipate should help the FTSE 100 rally.

MPC meetings 11th May and 22nd June 2023

- On 11th May, the Bank of England's Monetary Policy Committee (MPC) increased Bank Rate by 25 basis points to 4.50%, and on 22nd June moved rates up a further 50 basis points to 5.00%. Both increases reflected a split vote – seven members voting for an increase and two for none.
- Nonetheless, with UK inflation significantly higher than in other G7 countries, the MPC will have a difficult task in convincing investors that they will be able to

dampen inflation pressures anytime soon. Talk of the Bank's inflation models being "broken" is perhaps another reason why gilt investors are demanding a premium relative to US and Euro-zone bonds, for example.

- Of course, what happens outside of the UK is also critical to movement in gilt yields. The US FOMC has already hiked short-term rates to a range of 5.00%-5.25%, but a further increase is pencilled in for July, whilst the ECB looks likely to raise its Deposit rate at least once more to a peak of 3.75%, with upside risk of higher to come.

2. Interest rate forecasts

The Council has appointed Link Group as its treasury advisors 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, made on 26th June, sets out a view that both short and long-dated interest rates will be elevated for some little while, as the Bank of England seeks to squeeze inflation out of the economy, against a backdrop of a stubbornly robust economy and a tight labour market.

You will note that our forecasts have steadily increased during the quarter as the data continued to spring upside surprises, and the Bank of England continued to under-estimate how prevalent inflation is, and how tight the labour market is. The Government has also noted that despite immigration increasing markedly, high levels of ill-health amongst the workforce has led to wage demands remaining strong until such time as there is a loosening in demand for business services.

Our current and previous PWLB rate forecasts below are based on the Certainty Rate.

Link Group Interest Rate View	26.06.23												
	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26
BANK RATE	5.00	5.50	5.50	5.50	5.25	4.75	4.25	3.75	3.25	2.75	2.75	2.50	2.50
3 month ave earnings	5.30	5.60	5.50	5.30	5.00	4.50	4.00	3.50	3.00	2.70	2.60	2.50	2.50
6 month ave earnings	5.80	5.90	5.70	5.50	5.10	4.60	4.00	3.50	3.00	2.70	2.60	2.60	2.60
12 month ave earnings	6.30	6.20	6.00	5.70	5.30	4.80	4.10	3.60	3.10	2.80	2.70	2.70	2.70
5 yr PWLB	5.50	5.60	5.30	5.10	4.80	4.50	4.20	3.90	3.60	3.40	3.30	3.30	3.20
10 yr PWLB	5.10	5.20	5.00	4.90	4.70	4.40	4.20	3.90	3.70	3.50	3.50	3.50	3.40
25 yr PWLB	5.30	5.40	5.20	5.10	4.90	4.70	4.50	4.20	4.00	3.90	3.80	3.80	3.70
50 yr PWLB	5.00	5.10	5.00	4.90	4.70	4.50	4.30	4.00	3.80	3.60	3.60	3.50	3.50

Link Group Interest Rate View	24.05.23												
	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26
BANK RATE	4.75	5.00	5.00	4.75	4.50	4.00	3.50	3.25	2.75	2.50	2.50	2.50	2.50
3 month ave earnings	4.80	5.00	5.00	4.80	4.50	4.00	3.50	3.30	2.80	2.50	2.50	2.50	2.50
6 month ave earnings	5.10	5.20	5.10	4.90	4.50	3.90	3.40	3.20	2.90	2.60	2.60	2.60	2.60
12 month ave earnings	5.40	5.40	5.30	5.00	4.50	3.90	3.40	3.20	2.90	2.70	2.70	2.70	2.70
5 yr PWLB	5.00	5.00	5.00	4.80	4.50	4.10	3.70	3.50	3.30	3.20	3.20	3.10	3.10
10 yr PWLB	5.00	5.00	5.00	4.80	4.40	4.10	3.80	3.60	3.50	3.40	3.30	3.30	3.30
25 yr PWLB	5.30	5.30	5.20	5.10	4.80	4.50	4.20	4.00	3.80	3.70	3.60	3.60	3.60
50 yr PWLB	5.10	5.10	5.00	4.90	4.60	4.30	4.00	3.80	3.60	3.50	3.40	3.40	3.40

Link Group Interest Rate View	27.03.23											
	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26
BANK RATE	4.50	4.50	4.25	4.00	3.50	3.25	3.00	2.75	2.75	2.50	2.50	2.50
3 month ave earnings	4.50	4.50	4.30	4.00	3.50	3.30	3.00	2.80	2.80	2.50	2.50	2.50
6 month ave earnings	4.50	4.40	4.20	3.90	3.40	3.20	2.90	2.80	2.80	2.60	2.60	2.60
12 month ave earnings	4.50	4.40	4.20	3.80	3.30	3.10	2.70	2.70	2.70	2.70	2.70	2.70
5 yr PWLB	4.10	4.10	3.90	3.80	3.70	3.60	3.50	3.40	3.30	3.20	3.20	3.10
10 yr PWLB	4.20	4.20	4.00	3.90	3.80	3.70	3.50	3.50	3.40	3.30	3.30	3.20
25 yr PWLB	4.60	4.50	4.40	4.20	4.10	4.00	3.80	3.70	3.60	3.50	3.50	3.40
50 yr PWLB	4.30	4.20	4.10	3.90	3.80	3.70	3.50	3.50	3.30	3.20	3.20	3.10

- LIBOR and LIBID rates ceased at the end of 2021. In a continuation of previous views, money market yield forecasts are based on expected average earnings by local authorities for 3 to 12 months.
- The Link forecast for average earnings are averages i.e., rates offered by individual banks may differ significantly from these averages, reflecting their different needs for borrowing short-term cash at any one point in time.

A SUMMARY OVERVIEW OF THE FUTURE PATH OF BANK RATE

- Our central forecast for interest rates was previously updated on 25th May and reflected a view that the MPC would be keen to further demonstrate its anti-inflation credentials by delivering a succession of rate increases. This has happened to a degree, especially as it moved to a more aggressive 0.5% hike in June but, with inflation remaining elevated, we anticipate that Bank Rate will need to increase to at least 5.5%, if not higher, to sufficiently slow the UK economy and loosen the labour market.
- Moreover, we also still anticipate the Bank of England will be keen to loosen monetary policy when the worst of the inflationary pressures are behind us – but timing on this will remain one of fine judgment: cut too soon, and inflationary pressures may well build up further; cut too late and any downturn or recession may be prolonged. Our current judgment is that rates will have to increase and stay at their peak until the second quarter of 2024 as a minimum.
- In the upcoming months, our forecasts will be guided not only by economic data releases and clarifications from the MPC over its monetary policies and the Government over its fiscal policies, but also international factors such as policy development in the US and Europe, the provision of fresh support packages to support the faltering recovery in China as well as the on-going conflict between Russia and Ukraine and whether there are any further implications for Russia itself following the recent aborted mutiny by the Wagner group.
- On the positive side, consumers are still estimated to be sitting on excess savings left over from the pandemic, which could cushion some of the impact of the above challenges and may be the reason why the economy is performing somewhat better at this stage of the economic cycle than may have been expected. However, most of those excess savings are held by more affluent people whereas lower income families already spend nearly all their income on essentials such as food, energy and rent/mortgage payments.

PWLB RATES

- Gilt yield curve movements have shifted upwards, especially at the shorter end of the yield curve since our previous forecast but remain relatively volatile. PWLB 5 to 50 years Certainty Rates are, generally, in the range of 4.90% to 5.60%.
- We view the markets as having built in, already, nearly all the effects on gilt yields of the likely increases in Bank Rate and the elevated inflation outlook.

The balance of risks to the UK economy: -

- The overall balance of risks to economic growth in the UK is to the downside.

Downside risks to current forecasts for UK gilt yields and PWLB rates include: -

- **Labour and supply shortages** prove more enduring and disruptive and depress economic activity (accepting that in the near-term this is also an upside risk to inflation and, thus, the rising gilt yields we have seen of late).

- **The Bank of England** increases Bank Rate too fast and too far over the coming months, and subsequently brings about a deeper and longer UK recession than we currently anticipate.

- **UK / EU trade arrangements** – if there was a major impact on trade flows and financial services due to complications or lack of co-operation in sorting out significant remaining issues.

- **Geopolitical risks,** for example in Ukraine/Russia, China/Taiwan/US, Iran, North Korea and Middle Eastern countries, which could lead to increasing safe-haven flows.

- **A broadening of banking sector fragilities,** which have been successfully addressed in the near-term by central banks and the market generally, but which may require further intervention if short-term interest rates stay elevated for longer than is anticipated.

Upside risks to current forecasts for UK gilt yields and PWLB rates: -

- Despite the recent tightening by 0.5%, the **Bank of England proves too timid** in its pace and strength of increases in Bank Rate and, therefore, allows inflationary pressures to remain elevated for a longer period within the UK economy, which then necessitates Bank Rate staying higher for longer than we currently project.

- **The pound weakens** because of a lack of confidence in the UK Government's fiscal policies, resulting in investors pricing in a risk premium for holding UK sovereign debt.

- Longer-term **US treasury yields** rise strongly if inflation remains more stubborn than the market currently anticipates, pulling gilt yields up higher consequently.

- Projected **gilt issuance, inclusive of natural maturities and QT,** could be too much for the markets to comfortably digest without higher yields compensating.

<u>Appendix B - </u>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-23	237	4	1.7%
May-23	247	1	0.4%
Jun-23	316	0	0.0%

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-23	789	0	0.0%
May-23	1,775	3	0.2%
Jun-23	1,116	3	0.3%

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-23	117	0	0.0%
May-23	90	0	0.0%
Jun-23	95	0	0.0%

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-23	106	1	£304.15	13	12.3%	£109.29
May-23	98	2	£522.91	6	6.1%	£323.64
Jun-23	76	3	£253.95	9	11.8%	£714.08

Chargebacks to service areas

The upload of appropriate documents to the BSM (Barclaycard Spend Management 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 amount charged back to service areas is £14,058 to date. The breakdown of this is as follows:

Potentially correctable errors

Reason	Amount £
Not a tax invoice	1,505
No invoice uploaded to purchase card system	9,045
Invoice(s) do not match payment	482
Total	**11,032**

Other errors

Reason	Amount £
Non-domestic VAT	543
No tax on invoice	299
Supply not to Powys County Council	2,120
Over-accounting for VAT	63
Total	**3,025**

A breakdown by service is shown below

Service	Not A Tax Invoice	No Invoice Uploaded To BSM	Inv(s) Do Not Match Payment	Foreign VAT	No Tax On Invoice	Supply Not To PCC	Over-accounting For VAT
Revenue							
Schools Delegated Budgets	63	5,238	291		237	19	48
Schools Service	232	120		23	17		32
Adults		6					
Childrens		478			6		
Highways, Transport & Recycling	304	116	191				
Community Development		87					
Property, Planning & Public Protection		51			39		
Housing General Fund		787				2,101	
Housing Revenue Account		618					
Corporate Activities		196					-16
Workforce & Organisational Development		165					
Economy & Digital Services		1,004		504			
Transformation & Communications		70		17			
Capital							
Childrens	256						
Highways, Transport & Recycling	649						
Housing Revenue Account		109					
Total	**1,505**	**9,045**	**482**	**543**	**299**	**2,120**	**63**