PERFORMANCE SCRUTINY COMMITTEE **14 NOVEMBER 2024**

SUBJECT:	**TREASURY MANAGEMENT AND PRUDENTIAL CODE UPDATE MID YEAR REPORT – 30 SEPTEMBER 2024**
DIRECTORATE:	**CHIEF EXECUTIVE & TOWN CLERK**
REPORT AUTHOR:	**LAURA SHIPLEY, FINANCIAL SERVICES MANAGER**

1. Purpose of Report

1.1 This report summarises the Council's treasury management activity and the actual prudential indicators for the period 1st April 2024 to 30th September 2024.

2. Executive Summary

2.1 The Treasury Management Strategy for 2024/25 approved by council on 27th February 2024 outlines the Council's capital and investment priorities as follows;

- **Liquidity** of investments
- **Security** of capital / investments
- **Yield** earned on investments

2.2 The strategy includes indicators that help ensure that the Council's capital investment plans are affordable, prudent and sustainable. Setting an integrated Capital and Treasury Management Strategy is a requirement of the CIPFA Code of Practice.

2.3 The position and performance for the 6 months ended 30th September 2024 are set out in the body of this report.

2.4 Officers can confirm that the approved limits within the Annual Treasury Management Strategy were not breached during the quarter ended 30th September 2024.

3. Background

3.1 The prudential system for capital expenditure is well established. One of the requirements of the Prudential Code is to ensure adequate monitoring of the capital expenditure plans, prudential indicators (PIs) and treasury management response to these plans. This report fulfils that requirement and includes a review of compliance with Treasury and Prudential Limits and the Prudential Indicators at 30th September 2024. The Treasury Management Strategy and Prudential Indicators were previously reported to and approved by Council on 27th February 2024.

3.2 This Council has adopted the CIPFA Code of Practice for Treasury Management in the Public Sector and operates its treasury management service in compliance with this Code and the above requirements. These require that the prime objective of treasury management activity is the effective management of risk, and that its borrowing activities are undertaken in a prudent, affordable and sustainable basis.

3.3 This report highlights the changes to the key prudential indicators, to enable an overview of the current status of the capital expenditure plans. It incorporates any new or revised schemes previously reported to Members. Changes required to the residual prudential indicators and other related treasury management issues are also included.

4. Investment portfolio

4.1 The Council held £29.355m of investments as at 30th September 2024. (as set out in paragraph 4.8).

4.2 Forecast interest income for the year is £0.961m (£0.354m General Fund & £0.606m HRA), an overachievement of income of £0.300m against the £0.661m budget.

4.3 Of this investment portfolio 100% was held in low risk specified investments, the requirement for the year being a minimum of 25% of the portfolio to be specified investments. During the 6 months to 30th September on average 93% of the portfolio was held in low risk specified investments and an average of 7% of the portfolio was held in non-specified investments (with other local authorities).

4.4 Where possible the council seeks sustainable investments and are working with our advisors on the best way to score banks and funds ESG ratings, whilst balancing this against generating returns that are in the best interest of the taxpayer.

4.5 Liquidity – The Council seeks to maintain liquid short-term deposits of at least £5m available with a week's notice. At 30th September 2024 the Council held liquid short term deposits of £20.355m and the WAL of the investment portfolio was 0.082 years (30 days). The WAL of the investment portfolio is higher than expected.

4.6 Security - The Council's maximum security risk benchmark for the portfolio as at 30th September 2024 was 0.012%. Based on the historic risk of default of the counterparties and types of accounts in which the council's funds are place – this equates to a potential loss of £0.004m on an investment portfolio of £29m. This represents a very low risk investment portfolio.

4.7 Yield – The Council achieved an average return of 5.25% on its investment portfolio for the 6 months ended 30th September 2024. This compares favourably with both the prior year's equivalent figure of 4.73% and average SONIA rate over the period of 5.12%.

4.8 The table below highlights the level of investment activity, and the rates obtained as at 30th September 2024. Investments were made in line with Link's approved counterparty list.

INVESTMENTS	PRINCIPAL £	RATE %	PERIOD DAYS
Lloyds Bank Corporate Market NRFB	2,000,000	5.24	92
Lloyds Bank Corporate Market NRFB	2,000,000	5.12	185
SMBC Bank International Plc	2,000,000	4.95	92
SMBC Bank International Plc	3,000,000	4.77	181
Total Fixed Short term Investments	**9,000,000**		

Aberdeen Standard Liquidity Fund	7,000,000	5.01	Call
BlackRock Institutional Sterling Liquidity	605,000	4.97	Call
BNP Paribas Insticash Sterling	5,750,000	4.96	Call
Federated Short-Term Sterling Prime Fund	7,000,000	5.03	Call
Total Money Market Fund Investments	**20,355,000**		
Total Investments / Average Rate	**29,355,000**	5.01	

5. Borrowing

5.1 In accordance with the Local Government Act 2003, the Council has a statutory duty to determine and keep under review how much it can afford to borrow. Therefore, the Council establishes 'Affordable Borrowing Limits' (or Authorised Limit) as part of the Prudential Indicators within the approved treasury management strategy.

5.2 The 'authorised limit' and 'operational boundary' indicators govern the maximum level of external borrowing to fund the capital programme and short-term cash flow. See Appendix A.

5.3 The Council's capital financing requirement (CFR) for 2024/25 is £154.944m. The CFR denotes the Council's underlying need to borrow for capital purposes. If the CFR is positive the Council may borrow from the PWLB or the market (external borrowing), or from internal balances on a temporary basis (internal borrowing). The balance of external and internal borrowing is generally driven by market conditions. The Council has projected borrowing at the end of 2024/25 of £105.068m and is forecasting to utilise £49.876m of cash flow funds in lieu of borrowing towards capital expenditure. This is a prudent and cost-effective approach in the current economic climate but will require ongoing monitoring if further upside risk to gilt yields prevails.

5.4 As at 30th September 2024, the average rate of interest paid during the first half of the financial year on external borrowing was 3.26%. This is lower than the budgeted rate set in the MTFS 2024-29 of 3.65% due to the repayment of a loan in the prior year which was not anticipated in the MTFS, and the new borrowing forecast at budget setting has not yet been required.

5.5 As at 30th September 2024, the Council held £107.406m of external borrowing, of which 100% were fixed rate loans (See table below).

Borrowing Type	Lender	Outstanding Loans (£)	No Of Loans	Ave Rate %
PWLB	PWLB	95,405,738	32	3.55
LA Borrowing	North Kesteven District Council	2,000,000	1	2.05
Market Loans	Barclays	10,000,000	4	4.24
Total/ Ave Rate		**107,405,738**	**37**	**3.59***

* Note the average rate in the table above differs from the actual average rate of interest paid in **5.4** as it relates to all loans and doesn't take into account size of loans / weighting.

5.6 It is anticipated that no additional borrowing will be undertaken during this financial year. A loan of £2m is due to mature in February 2025, the need to replace this will be assessed closer to the time in-line with cashflow forecasts and interest rates at the time.

5.7 The capital programme is being kept under regular review due to the effects of inflationary pressures and shortages of materials and labour. The borrowing strategy will therefore also be regularly reviewed and revised, to achieve optimum value and risk exposure in the long-term.

6. Capital Expenditure and Financing

6.1 Capital expenditure forms one of the required prudential indicators. The Council must ensure that capital expenditure is affordable, approved and monitored.

6.2 The table below shows the forecast capital expenditure as at Q2 against budgets set as part of the Medium Term Financial Strategy (OE), and revised budgets adjusted at 2023/24 year end due to reprofiling etc, and how these are to be financed.

	2024/25 Original Estimate (OE) £'000	2024/25 OE inc. Year End Adj 's £'000	2024/25 Q2 Revised Estimate £'000
General Fund Capital Expenditure	**17,527**	**23,151**	**27,894**
Financed By -			
Capital Grants	4,550	6,806	14,601
Capital Receipts	1,112	1,133	74
Revenue Contributions	121	161	149
REFCUS Grants	5,468	8,270	8,376
Prudential Borrowing	6,276	6,781	4,694

6.3 The General Fund Investment Programme was adjusted post 2023/24 year end to take into account reprofiling of schemes and known changes at the time. The programme has since seen an increase in forecast expenditure in Q2, mainly due to the approval and inclusion of the Western Growth Corridor Levelling Up Fund bridge works.

	2024/25 Original Estimate (OE) £'000	2024/25 OE inc. Year End Adj 's £'000	2024/25 Q2 Revised Estimate £'000
Housing Revenue Account Capital Expenditure	**21,043**	**22,763**	**17,432**
Financed By -			
Capital Receipts	1,119	2,213	1,677
Capital Grants	0	0	1,155
MRR Revenue Contributions	5,721	5,855	4,235
MRR Depreciation	13,603	13,352	8,969
Prudential Borrowing	600	1,343	1,396

6.4 The Housing Investment Programme original was adjusted post 2023/24 year end to take into account reprofiling of schemes and known changes at the time. In addition, the original estimates, set as part of the Medium-Term Financial Strategy, were based on a stock condition survey of properties and the required levels of work. The forecast expenditure has now been adjusted to better reflect what the council's internal workforce and current contractors have capacity to complete in year.

6.5 The Capital Financing Requirement (CFR), the councils underlying need to borrow, and the movement in year can be seen below. (See also 5.3 & 7.2)

Capital Financing Requirement (CFR)	2024/25 Original Estimate (OE) £'000	2024/25 OE inc. Year End Adj 's £'000	2024/25 Q2 Revised Estimate £'000
Capital Financing Requirement (CFR) - General Fund	76,810	76,701	74,614
Capital Financing Requirement (CFR) - HRA	79,913	80,278	80,330
Capital Financing Requirement Total	**156,723**	**156,979**	**154,944**
Net movement in CFR (Capital borrowing need less MRP & VRP)	5,949	7,197	5,163

* Note that although the CFR total doesn't change significantly between the Original Estimate and the OE including year end adjustments, the net movement figures look greater due to the reprofiling of capital expenditure at year end and the 2023/24 CFR carried forward figure being adjusted accordingly.

7. Prudential Indicators

7.1 As part of the Treasury Management Strategy, the Council established a range of Prudential Indicators (in accordance with professional practice) to monitor both Treasury and Capital as the two are intrinsically linked.

7.2 Details of the performance against the Prudential Indicators can be found at Appendix A. See comments below.

1. Capital Expenditure General Fund – see section **6.2**
2. Capital Expenditure HRA – see section **6.2**.
3. Capital Financing Requirement (CFR) General Fund – The Capital Financing Requirement is the Council's underlying need to borrow for a capital purpose. The GF CFR is currently less than anticipated at budget setting due to the reprofiling of WGC Housing element, in line with revised build schedule.
4. Capital Financing Requirement (CFR) HRA – As above. The HRA CFR remains very close to the original estimate (including year-end adjustments) with minimal additional borrowing expected, pushing the CFR up only slightly.
5. Actual External Debt – Currently forecasting actual external debt at year end to be less than original anticipated at budget setting due to the council utilising internal funds rather than borrowing whilst interest rates are still high. The need for borrowing will be continuously monitored in-line with the councils cashflow and spending requirements.

6. Gross debt to the CFR – Under Borrowing –. The council is currently under borrowing against the CFR, meaning the council is utilising internal resources (£46m) rather than borrowing.

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

8. Operational Boundary for External Debt - This indicator is based on the probable external debt during the course of the year; it is not a limit and actual borrowing could vary around this boundary for short times during the year. CIPFA anticipate that this should act as an indicator to ensure the authorised limit is not breached.

9. Financing costs to net revenue stream (General Fund)– improved position anticipated due to re-profiling of forecast borrowing (planned borrowing for Western Growth Corridor £6m) and utilising internal funds.

10. Financing costs to net revenue stream (HRA) – Slight improvement due to forecasting holding off on reborrowing to replace a maturing loan.

7.3 Due to changes in accounting practice and the implementation of IFRS16 (leases) this year, the CFR will include lease liabilities that are currently not recognised on the balance sheet. As IFRS16 implications have not been fully calculated at the date of this report no changes to the CFR forecast have been made yet. The council is currently establishing the impact of the change in accounting for these liabilities (previously treated as operating leases and treated as rental expenditure) and estimates will be reflected in the 2024/25 Statement of Accounts.

7.4 The Chief Finance Officer reports that no difficulties are envisaged for the current or future years. This view takes into account current commitments, existing plans, and the proposals in the budget report.

8. Economic Update

8.1 The current economic update from the Council's treasury advisors (LINK) can be found in Appendix B.

8.2 Interest Rate Forecast - Current medium term interest rate forecasts are shown below. Economists have now forecast a more gradual / slower reduction of rates so

Link Group forecasts are likely to be adjusted to reflect the Capital Economics forecast.

Bank Rate	NOW	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27
Link Group	5.00%	4.50%	4.00%	3.50%	3.25%	3.25%	3.25%	3.25%	3.00%	3.00%	3.00%
Capital Economics	5.00%	4.75%	4.50%	4.25%	3.75%	3.25%	3.00%	3.00%	3.00%	3.00%	-
5yr PWLB Rate	**NOW**	**Dec-24**	**Mar-25**	**Jun-25**	**Sep-25**	**Dec-25**	**Mar-26**	**Jun-26**	**Sep-26**	**Dec-26**	**Mar-27**
Link Group	4.75%	4.50%	4.30%	4.10%	4.00%	3.90%	3.90%	3.90%	3.90%	3.90%	3.80%
Capital Economics	4.75%	4.70%	4.60%	4.40%	4.30%	4.10%	4.10%	4.00%	4.00%	4.00%	-
10yr PWLB Rate	**NOW**	**Dec-24**	**Mar-25**	**Jun-25**	**Sep-25**	**Dec-25**	**Mar-26**	**Jun-26**	**Sep-26**	**Dec-26**	**Mar-27**
Link Group	5.01%	4.60%	4.40%	4.30%	4.10%	4.10%	4.10%	4.00%	4.00%	4.00%	3.90%
Capital Economics	5.01%	4.80%	4.70%	4.60%	4.50%	4.30%	4.30%	4.20%	4.10%	4.10%	-
25yr PWLB Rate	**NOW**	**Dec-24**	**Mar-25**	**Jun-25**	**Sep-25**	**Dec-25**	**Mar-26**	**Jun-26**	**Sep-26**	**Dec-26**	**Mar-27**
Link Group	5.51%	5.00%	4.80%	4.70%	4.50%	4.50%	4.40%	4.40%	4.40%	4.30%	4.30%
Capital Economics	5.51%	5.10%	4.90%	4.80%	4.70%	4.50%	4.50%	4.40%	4.30%	4.20%	-
50yr PWLB Rate	**NOW**	**Dec-24**	**Mar-25**	**Jun-25**	**Sep-25**	**Dec-25**	**Mar-26**	**Jun-26**	**Sep-26**	**Dec-26**	**Mar-27**
Link Group	5.29%	4.80%	4.60%	4.50%	4.30%	4.30%	4.20%	4.20%	4.20%	4.10%	4.10%
Capital Economics	5.29%	5.10%	5.00%	4.80%	4.70%	4.60%	4.50%	4.40%	4.40%	4.30%	-

9. Strategic Priorities

9.1 One Council

Through its Treasury Management Strategy the Council seeks to reduce the amount of interest it pays on its external borrowing and maximise the interest it achieves on its investments.

10. Organisational Impacts

10.1 Finance

The financial implications are covered in the main body of the report.

10.2 Legal Implications including Procurement Rules

The powers for a local authority to borrow and invest are governed by the Local Government Act 2003 (LGA 2003) and associated Regulations. A local authority may borrow or invest for any purpose relevant to its functions, under any enactment, or for the purpose of the prudent management of its financial affairs. The Regulations also specify that authorities should have regard to the CIPFA Treasury Management Code and the MHCLG Investment Guidance when carrying out their treasury management functions.

10.3 Equality, Diversity and Human Rights

The Public Sector Equality Duty means that the Council must consider all individuals when carrying out their day-to-day work, in shaping policy, delivering services and in relation to their own employees.

It requires that public bodies have due regard to the need to:

- Eliminate discrimination
- Advance equality of opportunity

- Foster good relations between different people when carrying out their activities

Due to the nature of the report, no specific Equality Impact Analysis required.

11. Risk Implications

The Local Government Act 2003, the Prudential Code and the Treasury Management Code of Practice include a key principal that an organisations appetite for risk is included in their annual Treasury Management Strategy and this should include any use of financial instruments for the prudent management of those risks, and should ensure that priority is given to security and liquidity when investing.

12. Recommendation

12.1 Members are asked to:

a) note the Prudential and Treasury Indicators and the actual performance against the Treasury Management Strategy 2024/25 for the mid-year ended 30th September 2024, and;

b) consider any specific recommendations to be referred to the Executive relating to the contents of this report.

Is this a key decision?	No
Do the exempt information categories apply?	No
Does Rule 15 of the Scrutiny Procedure Rules (call-in and urgency) apply?	No
How many appendices does the report contain?	Two
List of Background Papers:	Treasury Management Strategy 2024/25 (Approved by Council February 2024)
Lead Officer:	Laura Shipley, Financial Services Manager laura.shipley@lincoln.gov.uk

Updated Position on Prudential and Local Indicators

The table below summarised and provides an update of the main prudential indicators as at 30th September 2024 against budget.

Indicator No.	Indicator	2024/25 Original Estimate (OE) £'000	2024/25 OE inc. Year End Adj 's £'000	2024/25 Q2 Revised Estimate £'000
1 & 2	Capital Expenditure - General Fund	17,527	23,151	27,894
1 & 2	Capital Expenditure - HRA	21,043	22,763	17,432
	Capital Expenditure Total	**38,570**	**45,914**	**45,326**
3 & 4	Capital Financing Requirement (CFR) - General Fund	76,810	76,701	74,614
3 & 4	Capital Financing Requirement (CFR) - HRA	79,913	80,278	80,330
	Capital Financing Requirement Total	**156,723**	**156,979**	**154,944**
5	Estimated Actual External Debt (As at 31st March 2025)	113,017	113,017	105,068
6	Gross Debt and the CFR – Under Borrowing	(43,706)	(43,962)	(49,876)
7	Authorised Limit for External Debt	130,165	130,773	128,850
8	Operational Boundary for External Debt	124,217	124,217	116,268
9 &10	Financing Costs to Net Revenue Stream - General Fund	15.39%		13.51%
9 &10	Financing Costs to Net Revenue Stream - HRA	28.79%		28.34%
Local 5	Net Income from Commercial and Service Investments to Net Revenue Stream	10.45%		10.58%

Remaining Prudential Indicators

In addition to the 10 key Prudential Indicators covered in the main report are 4 further indicators, as set out below.

Treasury Management Prudential Indicators

The first treasury indicator requires the adoption of the CIPFA Code of practice on Treasury Management. This Council adopted the Code of Practice on Treasury Management on 1st March 2011 (revised 2021), and as a result adopted a Treasury Management Policy & Practices statement.

There are two further indicators:

These limits relate to funds invested for greater than 365 days.

Upper Limits On Variable Rate Exposure – This indicator identifies a maximum limit for variable interest rates based upon the debt position net of investments.

Upper Limits On Fixed Rate Exposure – Similar to the above indicator, this covers a maximum limit on fixed interest rates.

Indicator No	Indicator	2024/25 %
11	Upper Limit for Fixed Interest Rates	100%
12	Upper Limit for Variable Interest Rates	40%

Total Principal Funds Invested – These limits are set to reduce the need for early sale of an investment, and are based on the availability of investments after each year-end.

Indicator 14 - Maximum Principal Sums invested for longer than 365 days	2024/25 Limit £m	Actual as at 30/09/24	Forecast 31/03/25
	7	0	0

As at 30th September 2024, there were no principal funds invested for a duration invested greater than 1 year.

Maturity Structure of Borrowing

These gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing at the same time and are required for upper and lower limits.

The table below shows the maturity structure limits in places per the Treasury Management Strategy, maturity structure as at Q2 and the profile expected at year end.

Indicator 13 - Maturity structure of fixed borrowing	2024/25 Lower Limit	2024/25 Upper Limit	Actual at 30/09/24	Forecast at 31/03/25
Under 12 months	0%	40%	3%	2%
12 months to 2 years	0%	40%	1%	1%
2 years to 5 years	0%	60%	7%	9%
5 years to 10 years	0%	80%	14%	15%
10 years and above	10%	100%	75%	74%

Local Prudential Indicators

In addition to the statutory and local indicators listed above the Chief Finance Officer has set five additional local indicators aimed to add value and assist in the understanding of the main indicators. These are summarised in the table below.

Additional Local Indicator	2024/25 Target	2024/25 Actual as at 30/09/24
1. Borrowing rate achieved (i.e. temporary borrowing of loans less then 1 year)	Less than SONIA rate	No temporary loans taken
2. Investment rate achieved against the SONIA rate	Greater than SONIA rate (5.12% 6 month Ave)	5.25%
3. Average rate of interest paid on Council debt during the year	4.50%	3.26%
4. The amount of interest on debt as a percentage of gross revenue expenditure.	Reported at year end	
5. Net Income from Commercial and Service Investments to Net Revenue Stream	10.45%	10.58%

The interest rate achieved on investments compares favourably to the SONIA rate due to the use of fixed rate investments setup prior to Bank of England rate reduction forecasts. The council is also proactive with the use of money market funds and seeking best possible rates.

Average rate of interest paid on the Council's debt during the year - The council has benefitted from holding long term loans taken out prior to rates being as high as they have been over the last couple of years.

Net income from commercial and service investments has to Net revenue stream ratio being slightly higher due to rent reviews in excess of what was assumed at budget setting.

Appendix B

Economic Update from LINK (the Council's treasury advisors)
NOTE – THIS WAS PREPARED AHEAD OF THE 2024 AUTUMN BUDGET

- The third quarter of 2024 (July to September) saw:
  - GDP growth stagnating in July following downwardly revised Q2 figures (0.5% q/q)
  - A further easing in wage growth as the headline 3myy rate (including bonuses) fell from 4.6% in June to 4.0% in July;
  - CPI inflation hitting its target in June before edging above it to 2.2% in July and August;
  - Core CPI inflation increasing from 3.3% in July to 3.6% in August;
  - The Bank of England initiating its easing cycle by lowering interest rates from 5.25% to 5.0% in August and holding them steady in its September meeting;
  - 10-year gilt yields falling to 4.0% in September.
- The economy's stagnation in June and July points more to a mild slowdown in GDP growth than a sudden drop back into a recession. Moreover, the drop in September's composite activity Purchasing Managers Index, from 53.8 in August to 52.9, was still consistent with GDP growth of 0.3%-0.4% for the summer months. This is in line with the Bank of England's view, and it was encouraging that an improvement in manufacturing output growth could be detected, whilst the services PMI balance suggests non-retail services output grew by 0.5% q/q in Q3. Additionally, the services PMI future activity balance showed an uptick in September, although readings after the Chancellor's announcements at the Budget on 30th October will be more meaningful.
- The 1.0% m/m jump in retail sales in August was stronger than the consensus forecast for a 0.4% m/m increase. The rise was reasonably broad based, with six of the seven main sub sectors recording monthly increases, though the biggest gains came from clothing stores and supermarkets, which the ONS reported was driven by the warmer-than-usual weather and end of season sales. As a result, some of that strength is probably temporary.
- The government's plans to raise public spending by around £16bn a year (0.6% GDP) have caused concerns that a big rise in taxes will be announced in the Budget, which could weaken GDP growth in the medium-term. However, if taxes are raised in line with spending (i.e., by £16bn) that would mean the overall stance of fiscal policy would be similar to the previous government's plan to reduce the budget deficit. Additionally, rises in public spending tend to boost GDP by more than increases in taxes reduce it. Our colleagues at Capital Economics suggest GDP growth will hit 1.2% in 2024 before reaching 1.5% for both 2025 and 2026.
- The further easing in wage growth will be welcomed by the Bank of England as a sign that labour market conditions are continuing to cool. The 3myy growth rate of average earnings fell from 4.6% in June to 4.0% in July. On a three-month annualised basis, average earnings growth eased from 3.0% to 1.8%, its lowest rate since December 2023. Excluding bonuses, the 3myy rate fell from 5.4% to 5.1%.
- Other labour market indicators also point to a further loosening in the labour market. The 59,000 fall in the alternative PAYE measure of the number of employees in August marked the fourth fall in the past five months. And the 77,000 decline in the three months to August was the biggest drop since November 2020. Moreover, the number of workforce jobs fell by 28,000 in Q2. The downward trend in job vacancies continued too. The number of job

vacancies fell from 872,000 in the three months to July to 857,000 in the three months to August. That leaves it 34% below its peak in May 2022, and just 5% above its pre-pandemic level. Nonetheless, the Bank of England is still more concerned about the inflationary influence of the labour market rather than the risk of a major slowdown in labour market activity.

- CPI inflation stayed at 2.2% in August, but services inflation rose from a two-year low of 5.2% in July to 5.6%, significantly above its long-run average of 3.5%. Food and fuel price inflation exerted some downward pressure on CPI inflation, but these were offset by the upward effects from rising furniture/household equipment inflation, recreation/culture inflation and a surprisingly large rise in airfares inflation from -10.4% in July to +11.9% in August. As a result, core inflation crept back up from 3.3% to 3.6%. CPI inflation is also expected to rise in the coming months, potentially reaching 2.9% in November, before declining to around 2.0% by mid-2025.

- The Bank initiated its loosening cycle in August with a 25bps rate cut, lowering rates from 5.25% to 5.0%. In its September meeting, the Bank, resembling the ECB more than the Fed, opted to hold rates steady at 5.0%, signalling a preference for a more gradual approach to rate cuts. Notably, one Monetary Policy Committee (MPC) member (Swati Dhingra) voted for a consecutive 25bps cut, while four members swung back to voting to leave rates unchanged. That meant the slim 5-4 vote in favour of a cut in August shifted to a solid 8-1 vote in favour of no change.

- Looking ahead, CPI inflation will likely rise in the coming months before it falls back to its target of 2.0% in mid-2025. The increasing uncertainties of the Middle East may also exert an upward pressure on inflation, with oil prices rising in the aftermath of Iran's missile attack on Israel on 1 October. China's recent outpouring of new fiscal support measures in the latter stages of September has also added to the upshift in broader commodity prices, which, in turn, may impact on global inflation levels and thus monetary policy decisions. Despite these recent developments, our central forecast is still for rates to fall to 4.5% by the end of 2024 with further cuts likely throughout 2025. This is in line with market expectations, however, although a November rate cut still looks likely, December may be more problematic for the Bank if CPI inflation spikes towards 3%. In the second half of 2025, though, we think a more marked easing in inflation will prompt the Bank to speed up, resulting in rates eventually reaching 3.0%, rather than the 3.25-3.50% currently priced in by financial markets.

- Our forecast is next due to be updated around mid-November following the 30 October Budget, 5 November US presidential election and the 7 November MPC meeting and the release of the Bank of England Quarterly Monetary Policy Report.

- Looking at gilt movements in the first half of 2024/25, and you will note the 10-year gilt yield declined from 4.32% in May to 4.02% in August as the Bank's August rate cut signalled the start of its loosening cycle. Following the decision to hold the Bank Rate at 5.0% in September, the market response was muted, with the 10-year yield rising by only 5bps after the announcement. This likely reflected the fact that money markets had priced in a 25% chance of a rate cut prior to the meeting. The yield had already increased by about 10bps in the days leading up to the meeting, driven in part by the Fed's "hawkish cut" on 18 September. There is a possibility that gilt yields will rise near-term as UK policymakers remain cautious due to persistent inflation concerns, before declining in the longer term as rates fall to 3.0%.

- The FTSE 100 reached a peak of 8,380 in the third quarter of 2024, but its performance is firmly in the shade of the US S&P500, which has breached the 5,700 threshold on several occasions recently. Its progress, however, may pause for the time being whilst investors wait to see who is elected the next US President, and how events in the Middle East (and Ukraine) unfold. The catalyst for any further rally (or not) is likely to be the degree of investors' faith in AI.

MPC meetings: 9 May, 20 June, 1 August, 19 September 2024

- On 9 May, the Bank of England's Monetary Policy Committee (MPC) voted 7-2 to keep Bank Rate at 5.25%. This outcome was repeated on 20th June.
- However, by the time of the August meeting, there was a 5-4 vote in place for rates to be cut by 25bps to 5%. However, subsequent speeches from MPC members have supported Governor Bailey's tone with its emphasis on "gradual" reductions over time.
- Markets thought there may be an outside chance of a further Bank Rate reduction in September, following the 50bps cut by the FOMC, but this came to nothing.
- Nonetheless, November still looks most likely to be the next month to see a rate cut to 4.75% but, thereafter, inflation and employment data releases, as well as geo-political events, are likely to be the determinant for what happens in the remainder of 2024/25 and into 2025/26.

Interest Rate Forecasts

The Authority has appointed Link Group as its treasury advisors and part of their service is to assist the Authority 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 1 November 2012.

Our latest forecast on 28 May sets out a view that short, medium and long-dated interest rates will fall back over the next year or two, although there are upside risks in respect of the stickiness of inflation and a continuing tight labour market, as well as the size of gilt issuance. Our PWLB rate forecasts below are based on the Certainty Rate (the standard rate minus 20 bps, calculated as gilts plus 80bps) which has been accessible to most authorities since 1 November 2012.

Link Group Interest Rate View	28.05.24									
	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27
BANK RATE	4.50	4.00	3.50	3.25	3.25	3.25	3.25	3.00	3.00	3.00
3 month ave earnings	4.50	4.00	3.50	3.30	3.30	3.30	3.30	3.00	3.00	3.00
6 month ave earnings	4.40	3.90	3.50	3.30	3.30	3.30	3.30	3.10	3.10	3.20
12 month ave earnings	4.30	3.80	3.50	3.40	3.40	3.40	3.40	3.20	3.30	3.40
5 yr PWLB	4.50	4.30	4.10	4.00	3.90	3.90	3.90	3.90	3.90	3.80
10 yr PWLB	4.60	4.40	4.30	4.10	4.10	4.10	4.00	4.00	4.00	3.90
25 yr PWLB	5.00	4.80	4.70	4.50	4.50	4.40	4.40	4.40	4.30	4.30
50 yr PWLB	4.80	4.60	4.50	4.30	4.30	4.20	4.20	4.20	4.10	4.10