

Mid-Year Treasury Management Review 2024/25

Cambridgeshire and Peterborough Fire Authority

(This report is written with material taken from Link Group's Quarterly Treasury Report, their latest report available at time of writing was to 30th September 2024. Data specific to the Authority is to 31 December 2024).

Quarter Ended 31 December 2024

1. Introduction

1.1 This report has been written in accordance with the requirements of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised 2021).

The primary requirements of the Code are as follows:

- Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Authority's treasury management activities.
- Creation and maintenance of Treasury Management Practices which set out the manner in which the Authority will seek to achieve those policies and objectives.
- Receipt by the Authority of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead, a Mid-year Review Report and an Annual Report, covering activities during the previous year.
- Delegation by the Authority of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.
- Delegation by the Authority of the role of scrutiny of treasury management strategy and policies to a specific named body. For this Authority, the delegated body is the Policy and Resources Committee:

1.2 This mid-year report has been prepared in compliance with CIPFA's Code of Practice on Treasury Management, and covers the following;

- An economic update for the first half of the 2024/25 financial year,
- A review of the Treasury Management Strategy Statement and Annual Investment Strategy,
- The Authority's capital expenditure, as set out in the Capital Strategy, and prudential indicators,
- A review of the Authority's investment portfolio for 2024/25,
- A review of the Authority's borrowing strategy for 2024/25,
- A review of any debt rescheduling undertaken during 2024/25,
- A review of compliance with Treasury and Prudential Limits for 2024/25.

2. Annual Investment Strategy Update

2.1 The Treasury Management Strategy Statement (TMSS) for 2024/25, which includes the Annual Investment Strategy, was approved by the Authority on 15th February 2024. In accordance with the CIPFA Treasury Management Code of Practice, it sets out the Authority's investment priorities as being:

- Security of capital
- Liquidity
- Yield

2.2 The Authority will aim to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity and with the Authority's risk appetite. In the current economic climate, it is considered appropriate to keep investments short term to cover cash flow needs, but also to seek out value available in periods up to 12 months with high credit quality financial institutions, using the Link suggested creditworthiness approach, including a minimum sovereign credit rating and Credit Default Swap (CDS) overlay information.

Creditworthiness

2.3 The UK's sovereign rating has proven robust through the first half of 2024/25.

Investment Counterparty Criteria

2.4 The current investment counterparty criteria selection approved in the TMSS is meeting the requirement of the treasury management function.

CDS Prices

2.5 It is noted that sentiment in the current economic climate can easily shift, so it remains important to undertake continual monitoring of all aspects of risk and return in the current circumstances.

Investment Balances

2.6 The average level of funds available for investment purposes up to 31 December 2024 was £12,197m. These funds were available on a temporary basis, and the level of funds available was mainly dependent on the timing of precept payments, receipt of grants and progress on the capital programme.

2.7 The Authority received funding from Central Government in July 2024 to help the Authority manage its cashflows settling payments in relation to the Fire fighters pension remedy's. It is relatively unknown as to when payments will be required to be made so the Authority is monitoring its Treasury activities on a continual basis and have prioritised short term investments over longer term investments until there is greater certainty over future cashflows.

2.8 Currently shorter-term investments are providing the Authority with greater yield over longer-term investments.

3. Treasury Position as at 31 December 2024

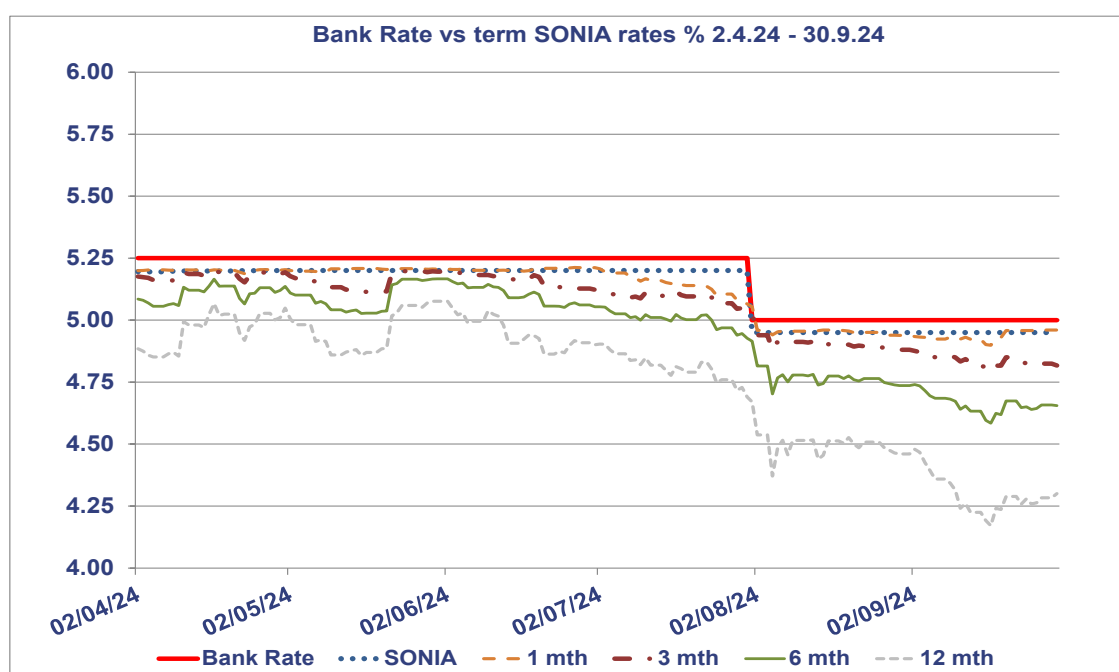
Approved Limits

3.1 Officers can confirm that the approved limits within the Annual Investment Strategy were not breached during the period ended 31 December 2024. The movement in reserves relate to planned movements from the previous year's budget to the current revenue budget (order carry forwards and requested carry forwards

(Paragraph 4.2 within Appendix 3). Currently the Authority uses its capital receipts to fund capital expenditure each year.

DEBT	31 March 2024 Principal	Rate/Return	Average Life yrs	31 December 2024 Principal	Rate/Return	Average Life yrs
Total Debt	£5.700m	3.56%	35	£5.700m	3.56%	34
Capital Financing Requirement (CFR)	£9.688m			£9.688m		
Over / (under) Borrowing	(£3. 988)m			(£3. 988)m		
Total Investments	£4.444m	5.04%		£13.364m	4.56%	
Net Investments	(£1.256)m			£7.664m		

3.2 Investment Performance April to September 2024 (provided by Link Group)



**Investment performance year to date as of end-September 2024. The graph uses the Sterling Overnight Index Averages. It is based on a backward-looking benchmark which reflects where the market was positioned when investments were placed.*

	Bank Rate	SONIA	7 day	30 day	90 day	180 day	365 day
High	5.25	5.20	5.20	5.21	5.23	5.26	5.33
High Date	02/04/2024	03/05/2024	13/05/2024	26/06/2024	26/07/2024	26/07/2024	01/08/2024
Low	5.00	4.95	4.95	4.96	5.06	5.18	5.09
Low Date	01/08/2024	01/08/2024	27/08/2024	04/09/2024	30/09/2024	30/09/2024	02/04/2024
Average	5.17	5.12	5.12	5.15	5.20	5.25	5.26
Spread	0.25	0.25	0.25	0.25	0.17	0.08	0.24

Interest Rate Forecast

3.3 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.

3.4 Link Group's latest forecast below sets out a view that short, medium and long-dated interest rates will fall back over the next year or two.

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

**The PWLB rate forecasts above 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.*

4. The Authority's Capital Position

4.1 This part of the report is structured to update:

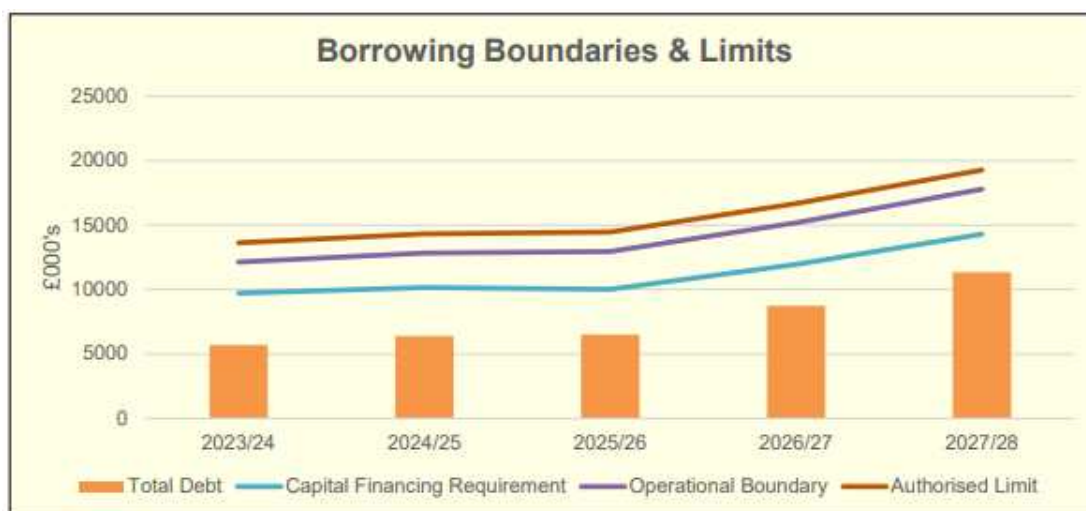
- The Authority's capital expenditure plans;
- How these plans are being financed;
- The impact of the changes in the capital expenditure plans on the prudential indicators and the underlying need to borrow; and
- Compliance with the limits in place for borrowing activity.

Changes to the Financing of the Capital Programme (see also Appendix 2 to main report)

4.2 The table draws together the main strategy elements of the capital expenditure plans and the expected financing arrangements of this capital expenditure. The borrowing element of the table increases the underlying indebtedness of the Authority by way of the Capital Financing Requirement (CFR), although this will be reduced in part by revenue charges for the repayment of debt (the Minimum Revenue Provision). This direct borrowing need may also be supplemented by maturing debt and other treasury requirements.

Changes to the Prudential Indicators for the Capital Financing Requirement (CFR), External Debt and the Operational Boundary

4.3 Currently no changes have been made to the prudential indicators.



	2024/25 £.m	2025/26 £.m	2026/27 £.m
Capital financing requirement	10.150	10.018	11.965
Operational boundary	12.826	12.955	15.176
Authorised limit	14.326	14.455	16.676
Upper limit for fixed rate interest exposure	100%	100%	100%
Upper limit for variable rate interest exposure	100%	100%	100%

5. Borrowing Strategy

5.1 No borrowing has been undertaken up to and including the quarter ending 31 December 2024. The Authority continues to maintain an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement) is not fully funded with loan debt, as cash supporting the Authority's reserves, balances and cash flows was used as an interim measure. This strategy was prudent as investment returns have previously been very low and minimising counterparty risk on placing investments also needed to be considered.

5.2 The Authority has not taken out any borrowing as there continues to be a cost to revenue on any new long-term borrowing that is not immediately used to finance capital expenditure, although this would have caused a temporary increase in cash balances, it would have incurred a revenue cost – the difference between (higher) borrowing costs and (lower) investment returns.

5.3 The policy of avoiding new borrowing by running down spare cash balances has served well over the last few years. However, this was kept under review to avoid incurring higher borrowing costs in the future when this authority may not be able to avoid new borrowing to finance capital expenditure and/or the refinancing of maturing debt.

PWLB Rates (taken from Link Group's Treasury Report to 30 September 2024)

5.4 The yield curve movements have become less volatile and PWLB 5 to 50 years Certainty Rates are, generally, in the range of 4.10% to 4.80%. Link 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.

PWLB Maturity Certainty Rates Year to Date to 30 September 2024

5.5 Gilt yields and PWLB certainty rates were less volatile than at this time last year. Overall, the 10, 25 and 50-year part of the curve endured a little volatility but finished September very much as it started in April.

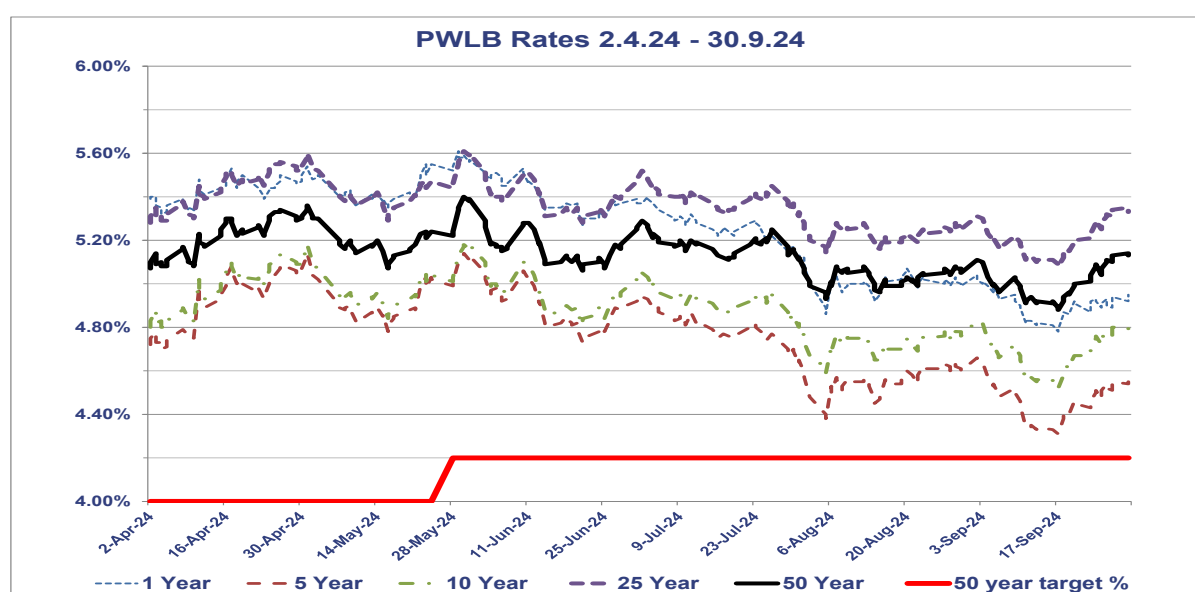
5.6 Where there was some movement downwards, this came in the shorter part of the curve as markets positioned themselves for Bank Rate cuts in the second half of 2024 and into 2025, although the continued stickiness of inflation and the prevailing tight labour market is a concern for those looking for more sizeable falls ahead.

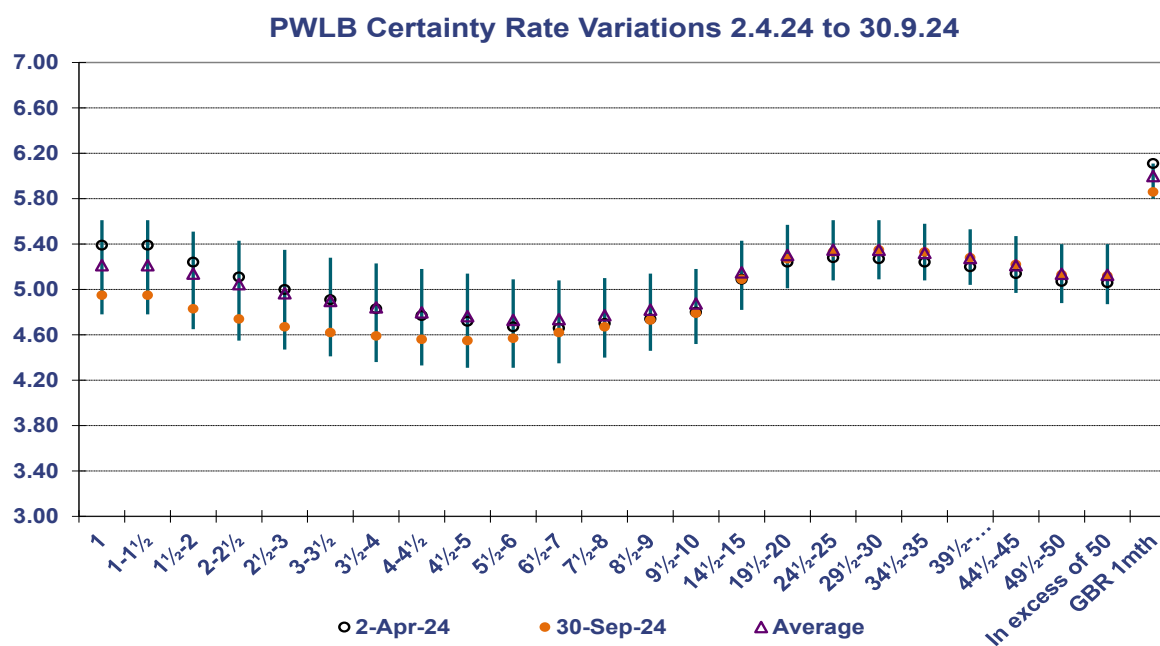
5.7 At the beginning of April, the 5-year certainty rate was the cheapest part of the curve at 4.72% whilst the 25-year rate was relatively expensive at 5.28%. May saw yields at their highest across the whole curve.

5.8 Conversely, 17 September saw the low point for the whole curve, with the 5-year certainty rate falling to 4.31% before rebounding to 4.55% by the end of the month. Similarly, the 50-year certainty rate fell to 4.88% but finished the month at 5.13%, slightly higher than at the start of April.

5.9 At this juncture, we still forecast rates to fall back over the next two to three years as inflation dampens, although there is upside risk to our Bank Rate forecast at present. The CPI measure of inflation is expected to fall below 2% in the second half of 2025, however, and we forecast 50-year rates to stand at 4.20% by the end of September 2026. The major caveats are that there is considerable gilt issuance to be digested by the market over the next couple of years, and geo-political uncertainties – which are generally negative for inflation prospects – abound in Eastern Europe and the Middle East, in particular.

PWLB Rates 2 April to 30 September 2024





High/Low/Average PWLB Rates for 2 April to 30 September 2024

	1 Year	5 Year	10 Year	25 Year	50 Year
02/04/2024	5.39%	4.72%	4.80%	5.28%	5.07%
30/09/2024	4.95%	4.55%	4.79%	5.33%	5.13%
Low	4.78%	4.31%	4.52%	5.08%	4.88%
Low date	17/09/2024	17/09/2024	17/09/2024	17/09/2024	17/09/2024
High	5.61%	5.14%	5.18%	5.61%	5.40%
High date	29/05/2024	01/05/2024	01/05/2024	01/05/2024	01/05/2024
Average	5.21%	4.76%	4.88%	5.35%	5.14%
Spread	0.83%	0.83%	0.66%	0.53%	0.52%

Debt Rescheduling

5.10 Debt repayment and rescheduling opportunities have increased over the course of the past six months and will be considered if giving rise to long-term savings. However, no debt repayments or rescheduling have been undertaken to date in the current financial year.

Compliance with Treasury and Prudential Limits

5.11 It is a statutory duty for the Authority to determine and keep under review the affordable borrowing limits. Up to the 31 December 2024, the Authority has operated within the treasury and prudential indicators set out in the Authority's Treasury Management Strategy Statement for 2024/25. The Authority reports that no difficulties are envisaged for the current or future years in complying with these indicators.

5.12 All treasury management operations have also been conducted in full compliance with the Authority's Treasury Management Practices.

6. Additional Information - Link Group's Economics Update as of 30 September 2024

6.1 The quarter July to September 2024 saw;

- GDP growth stagnating in July following downwardly revised quarter 2 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.

6.2 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 quarter 3. 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.

6.3 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.

6.4 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.

6.5 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%.

6.6 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 quarter 2. 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.

6.7 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.

6.8 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.

6.9 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.

6.10 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.

6.11 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%.

6.12 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.
