**Economic Update (provided by CAS Treasury Solutions)**

**Quarter Ended 31st December 2016**

1. Economic growth appears to have barely lost pace, despite the vote for Brexit. Indeed, quarterly GDP growth in Q3 of 2016 is now estimated to have been 0.6%, up from the initial estimate of 0.5%: Q2's growth rate was also nudged down from 0.7% to 0.6%. Moreover, the average level of the Markit/CIPS all-sector PMI in October and November was 54.8, compared to an average of 51.4 in Q3. On the basis of past form, this is consistent with quarterly GDP growth of about 0.5%. And the sharp rise in the manufacturing PMI in December suggests the sector ended the year solidly.
2. Consumer spending continued to be the key driver of growth in Q4. Admittedly, retail sales only rose by a monthly 0.2% in November. But this followed a whopping 1.8% monthly increase in October. As a result, even if sales volumes were flat in December, they would have risen by 2.1% over Q4 as a whole, the largest increase since Q2 2014 and up from Q3's 1.9% rise.
3. This does not look sustainable though. Q3's National Accounts revealed a fall in households' real disposable incomes, and as a result the 0.7% rise in overall household spending was funded entirely through a fall in the household saving ratio. With inflation having picked up and employment growth having slowed in Q4, it looks likely that the saving ratio may have fallen further.
4. The labour market's recent strength seems to be waning. Employment actually fell in the three months to October, the first fall since Q2 2015. Annual growth in employment remained positive, albeit weak, at 1.1%. Granted, the unemployment rate held steady at its post-crisis low of 4.8%. But note that this was due to people moving into inactivity rather than employment.
5. Note that some slowdown in employment growth was inevitable, regardless of the outcome of the referendum, as labour market slack has diminished. Indeed the unemployment rate is now around the level often thought to be its "natural" rate. Looking ahead, we doubt that any job losses will be particularly severe or sustained. Survey measures of firms' employment intentions are consistent with annual growth in private sector employment of about 1% over the coming months.
6. Meanwhile, perhaps in response to past tightening in the labour market, there have been some more optimistic signs on the wages front, with annual growth in average weekly earnings (including bonuses) holding broadly stable at 2.5% in the three months to October, following a 2.4% rise in Q3.
7. At the current time, this is enough to outpace inflation. CPI inflation picked up from 0.7% in Q3 to average 1.1% in October and November. The 1.2% level reached in November was the highest since October 2014, although this still remains low by historical standards. However, inflation is on a steep upward trajectory. Components of inflation that typically respond quite quickly to exchange rate movements, such as petrol and food prices, have had big upward influences on the headline rate recently, and will continue to do so as the drop in the pound makes its way through the inflation pipeline.

8. Price pressures at the beginning of the pipeline are already building rapidly. Producer input price inflation rose from 6.5% in Q3 to an average of 12.6% in October and November. There is typically quite a long lag between producer prices and CPI inflation, but we should start to see this feed through to higher prices on the high street over the course of 2017. Indeed, CPI inflation is still on track to breach the 2% inflation target in spring 2017, and should peak at around 3% by spring 2018.
9. For now at least, the MPC doesn’t appear to be too fazed by this overshoot of the 2% inflation target: it left interest rates unchanged at 0.25% during Q4. Given the uncertainty about the economic outlook, and especially the impact from the two year window for Brexit negotiations from March 2017, interest rates look set to remain on hold for a long while yet.
10. By contrast, the US Fed pressed ahead and raised interest rates by 25bp in December, as expected, taking the Fed funds target range to between 0.50% and 0.75%. At the same time, the ECB announced that it would slow the pace of its asset purchases from April 2017, but committed to extending the purchases by another nine months (to December 2017). This highlights the unusual divergence in western monetary policy set to occur over the next year or so.
11. Meanwhile, the latest data suggests that the public finances are broadly on track to meet the recently revised OBR’s near-term forecasts. Borrowing on the PSNB ex measure in the first eight months of the fiscal year so far was about 11% lower than last year. This compares to the OBR’s expectations of a 10% fall for the fiscal year as a whole.
12. But hopes of a complete “reset” of fiscal policy were dashed in November’s Autumn Statement. Chancellor Philip Hammond did lessen the fiscal squeeze a bit, but the UK still faces another bout of austerity over the coming years. Of course, the new fiscal rules – which include achieving a cyclically-adjusted budget deficit of below 2% by 2020/21 – do offer the Chancellor a bit of room for manoeuvre if the economy were to turn out much weaker. On the basis of the OBR’s new forecasts, the deficit will be about 0.8% on this measure by that point, leaving him about 1.2% of GDP to play with.
13. Ongoing deficit reduction in the UK is in contrast to the US, where we expect a major fiscal stimulus on the back of Trump’s victory. Indeed, we have revised up our US GDP growth forecast for 2017 from 2% to 2.7%.
14. Meanwhile, in financial markets, the FTSE 100 rose by 2.4% between Q3 and Q4 of 2016, taking it to a record high. This partly reflected the 3.5% drop in the trade-weighted value of sterling, (which boosts the sterling value of UK firms’ overseas profits), but also the generally positive market reaction to Trump’s victory in the US election. That said, Brexit worries are still lingering, with the FTSE UK Local Index, which only includes firms of which more than 70% of their sales are generated in the UK, falling by 5.4%. Meanwhile, reflecting a combination of rising US Treasury yields on the back of Trump’s victory, as well as fears about the sterling-driven rise in inflation over the next few years in the UK, 10-year UK government bond yields rose by close to 50bp during Q4.

15. Finally, the UK government still plans to trigger Article 50 and begin Brexit negotiations by the end of March, and has promised to lay out its plans before it does so. A soft(ish) form of Brexit still looks in prospect. Granted, controlling immigration and ending the influence of the European Court of Justice appear to be key priorities, but the government has stated it wants to retain a very close trading relationship, and that a transitional deal may be considered in order to smooth the process.

**Appendix 2**

**Prudential and Treasury Indicators at 31st December 2016**

**Monitoring of Prudential and Treasury Indicators: approved by Council in February 2016.**

1. Has the Council adopted CIPFA Code of Practice for Treasury Management in the Public Services?

   The Council has adopted CIPFA's Treasury Management in the Public Services: Code of Practice and Cross Sectoral Guidance Notes. This is a key element of the Treasury Strategy 2016-17 which was approved by Council in February 2016.

2. **Limits for exposure to fixed and variable rate net borrowing (Borrowing less investments)**

| | Limits | Actual |
|---|---|---|
| Fixed rate | 150% to 35% | 79% |
| Variable rate | 65% to -50% | 21% |
| Total | | 100% |

The Interest rate exposure is calculated as a percentage of the net debt figure. The formula is shown below:

$$\frac{\textit{Total Fixed (or Variable) rate exposure}}{\textit{Total borrowing – short term investments}}$$

3. **Total principal sums invested for periods longer than 364 days**

| | 2016-17 Limit £m | Actual £m |
|---|---|---|
| Investment longer than 364 days to run | 80.0 | 0.0 |

Notes: This indicator is calculated by adding together all investments that have greater than 364 days to run to maturity at this point in time.

4. **Limits for maturity structure of borrowing**

| | Upper Limit | Actual |
|---|---|---|
| under 12 months | 80% | 35% |
| 12 months and within 24 months | 50% | 2% |
| 24 months and within 5 years | 50% | 9% |
| 5 years and within 10 years | 50% | 1% |
| 10 years and above | 100% | 53% |

**Note:** The guidance for this indicator requires that LOBO loans are shown as maturing at the next possible call date rather than at final maturity.

**Affordability:**

5. **Ratio of financing costs to net revenue stream**

| 2016-17 Original Estimate (%) | 2016-17 Revised Estimate (%) | Difference % |
|---|---|---|
| 7.4 | 6.2 | -1.2 |

6. **Estimated incremental impact of capital investment decisions on band D council tax**

| 2016-17 Original Estimate (£) | 2016-17 Revised Estimate (£) | Difference (£) |
|---|---|---|
| -0.93 | -27.42 | -28.35 |

**Prudence:**

7. **Gross borrowing and the Capital Financing Requirement (estimated borrowing liability excluding PFI)**

| Original 2016-17 Capital Financing Requirement (CFR) £m | 2016-17 CFR (based on latest capital information) £m | Actual Gross Borrowing £m | Difference between actual borrowing and original CFR £m | Difference between actual borrowing and latest CFR £m |
|---|---|---|---|---|
| 668.7 | 662.2 | 513.3 | 155.4 | 148.8 |

**Capital Expenditure:**

8. **Estimates of capital expenditure**

For details of capital expenditure and funding please refer to the Monthly Capital Report.

**External Debt:**

9. **Authorised limit for external debt**

| 2016-17 Authorised Limit £m | Actual Borrowing £m | Headroom £m |
|---|---|---|
| 728.7 | 513.3 | 215.4 |

The Authorised limit is the statutory limit on the Councils level of debt and must not be breached. This is the absolute maximum amount of debt the Council may have in the year.

10. **Operational boundary for external debt:**

| 2016-17 Operational Boundary £m | Actual Borrowing £m | Headroom £m |
|---|---|---|
| 698.7 | 513.3 | 185.4 |

The operational boundary is set as a warning signal that debt has reached a level nearing the Authorised limit and must be monitored carefully.

**Appendix 3**

## Investment Portfolio as at 31st December 2016

| Class | Type | Deal Ref | Start / Purchase Date | Maturity Date | Counterparty | Profile | Rate | Principal O/S (£) |
|---|---|---|---|---|---|---|---|---|
| Deposit | Call (3 months notice) | NCC/6 | - | - | HSBC Bank plc | Maturity | 0.48% | 6,700,000.00 |
| Deposit | Call (3 months notice) | NCC/7 | - | - | HSBC Bank plc | Maturity | 0.48% | 3,300,000.00 |
| Deposit | Call (instant access) | NCC/11 | - | - | Barclays Bank plc | Maturity | 0.30% | 4,849,000.00 |
| **Call Total** | | | | | | | | **14,849,000.00** |
| Deposit | Money Market Fund | NCC/19 | - | - | Deutsche Managed Sterling Platinum | Maturity | 0.28% | 14,065,000 |
| **Money Market Fund Total** | | | | | | | | **14,065,000.00** |
| Deposit | 3rd Party Loan | NCC/150 | 10/03/2016 | 10/03/1956 | University of Northampton | Annuity | 2.92% | 13,906,603.39 |
| Deposit | Share Capital | NCC/110 | 25/09/2014 | | The UK Municipal Bonds Agency | - | - | 200,000.00 |
| Deposit | 3rd Party Loan | NCC/113 | 23/10/2014 | 22/10/2020 | Northamptonshire County Cricket Club Ltd | Maturity | 4.44% | 922,800.92 |
| Deposit | 3rd Party Loan | NCC/124 | 20/04/2015 | notice | LGSS Law | Maturity | 1.64% | 950,000.00 |
| Deposit | 3rd Party Loan | NCC/79 | 11/07/2013 | 30/06/2018 | Adrenaline Alley | EIP | 3.82% | 25,570.00 |
| Deposit | 3rd Party Loan | NCC/80 | 10/01/2014 | 14/02/2019 | Northamptonshire County Cricket Club Ltd | Maturity | 3.02% | 1,000,000.00 |
| Deposit | 3rd Party Loan | NCC/81 | 20/01/2014 | 20/07/2017 | MOLA- Museum of London Archaeology | EIP | 3.75% | 41,665.00 |
| **Third Party Loans & Share Capital Total** | | | | | | | | **17,046,639.31** |
| **Deposit Total** | | | | | | | | **45,960,639.31** |