Annex 4

Tonbridge and Malling Borough Council

Treasury Management Annual Report 2021/22

1.1 Introduction

1.1.1 This Council is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management review of activity and the actual prudential and treasury indicators for 2021/22. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).

1.1.2 During 2021/22 the minimum reporting requirements were that full Council should receive the following treasury reports:

- an annual strategy in advance of the year;
- a mid-year review; and
- an annual review following the end of the year describing the activity compared to the strategy (this report).

In addition, treasury management updates have been presented to each meeting of the Audit Committee throughout the 2021/22 financial year. Treasury performance was also considered at the Finance, Innovation and Property Advisory Board through the regular Financial Planning and Control reports.

1.1.3 Changes in the regulatory environment place a much greater onus on Members for the review and scrutiny of treasury management policy and activities. This report is important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by Members.

1.1.4 This Council also confirms that it has complied with the requirement under the Code to give prior scrutiny to all of the above treasury management reports by the Audit Committee before they were reported to full Council.

1.2 Treasury Position 31 March 2022

1.2.1 At the beginning and the end of 2021/22 the Council's debt and investment position was as follows:

	31 March 2021 £m	Rate / Return %	Average duration Days	31 March 2022 £m	Rate / Return %	Average duration Days
Variable rate debt:						
Overdraft	0.0	-	-	0.0	-	-
Total debt	**0.0**	-	-	**0.0**	-	-
Fixed rate investments:						
Cash flow surpluses	0.0	-	-	0.0	-	-
Core cash	8.0	0.38	134	21.0	0.69	120
Variable rate investments:						
Cash flow surpluses	15.8	0.04	7	22.1	0.52	5
Core cash	8.0	0.41	90	3.0	0.15	95
Sub-total	31.8	0.22	70	46.1	0.62	63
Medium term investments:						
Multi-Asset Income Funds	-	-	-	4.3	3.87	-
Long term investments:						
Property Funds	5.0	3.51	-	5.0	3.17	-
Total investments	**36.8**	**0.67**	-	**55.4**	**0.82**	-

1.2.2 The increase in investment balances can be attributed to a number of factors including surpluses / deficits on the council tax and business rates collection funds due to be paid / recovered in 2022/23; unspent provisions for business rate appeals which are yet to be determined by the Valuation Office during the financial year; receipt of energy relief grant for distribution; and changes in the level of year-end debtor and creditor provisions.

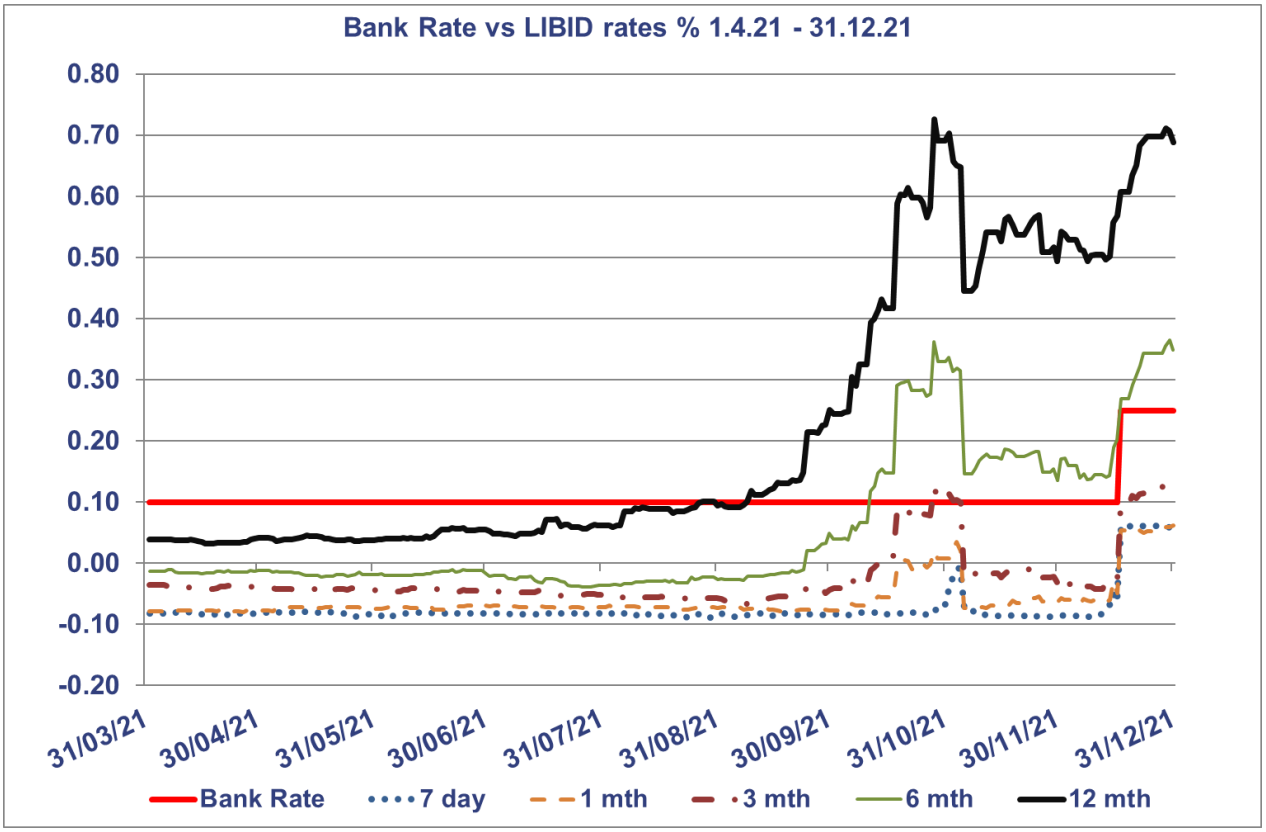
1.3 The Strategy for 2021/22

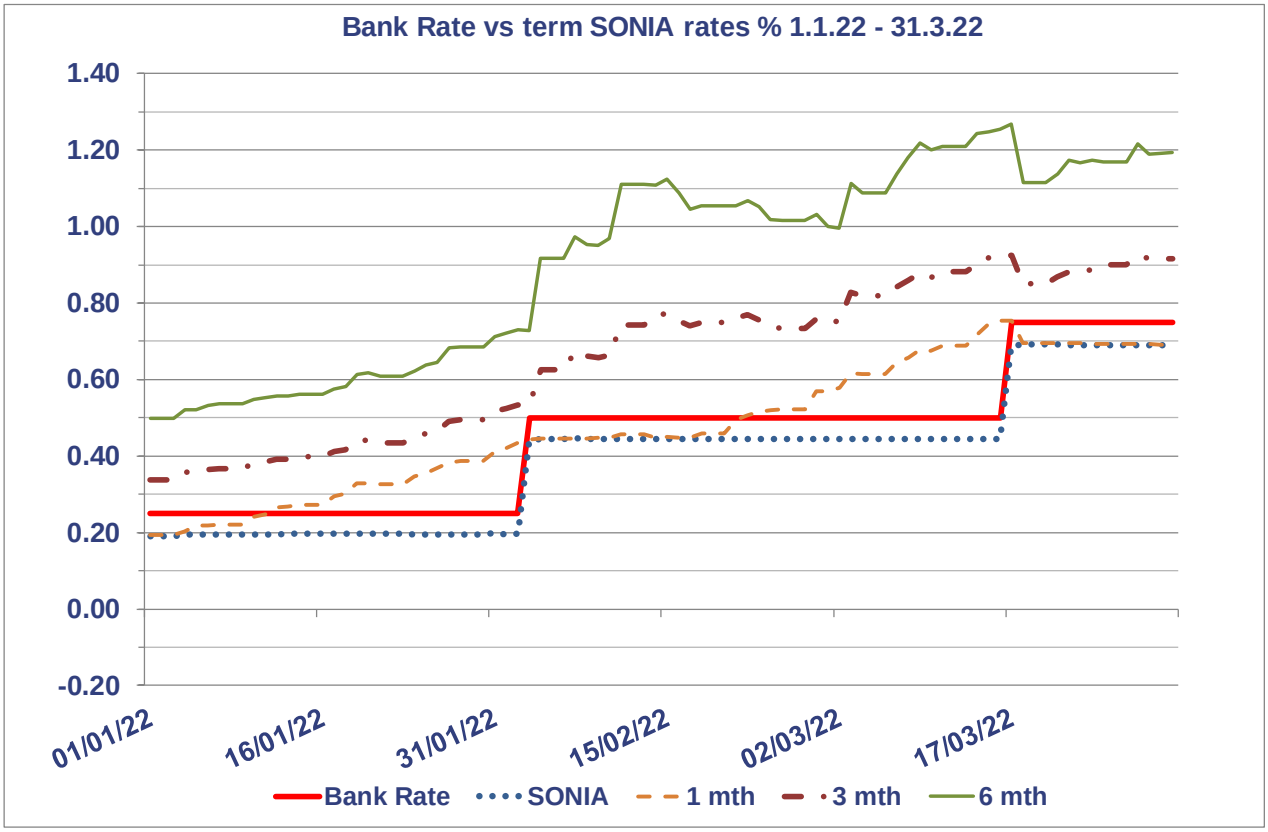
1.3.1 The treasury management strategy for 2021/22 was based on the November 2020 forecast and assumed a trade deal would be agreed with the EU; no further national lockdowns or sever regional restrictions were imposed; inflation was unlikely to pose a threat and bank rates would remain at 0.10% for the next three years. In actuality, energy costs sit at unprecedented levels; the conflict in Ukraine took place in February 2022 and inflation is at the highest level in three decades. Upward inflationary pressures have seen the Bank of England opting to increase the Bank Rate in December 2021 with additional increases in February and March 2022 in an attempt to suppress soaring inflation. Bank Rate is expected to continue to rise over the next two years.

1.3.2 While the Council has taken a cautious approach to investing, it is also fully appreciative of changes to regulatory requirements for financial institutions in terms of additional capital and liquidity that came about in the aftermath of the financial crisis. These requirements have provided a far stronger basis for financial institutions, with annual stress tests by regulators evidencing how institutions are now far more able to cope with extreme market stress and economic conditions.

1.4 Investment Rates in 2021/22

1.4.1 Bank rate and investment returns across durations up to 12 months are depicted in the graphs below. LIBID rates were phased out at the end of December 2021 with SONIA rates being considered as the industry accepted alternative. Since November 2021 Bank Rates have increased to 0.75% taking the rates back to the pre-virus and post-Global Financial Crisis high of 0.75% at 31 March 2022. Deposit rates made available towards the end of the financial year showed significant improvement and market expectation is for further increases in 2022/23.





1.5 Investment Outturn for 2021/22

1.5.1 The Council's investment policy sets out the approach for choosing investment counterparties and is based on credit ratings provided by the three main credit rating agencies. This is supplemented by additional market information including credit rating outlooks and credit default swap data (CDS). The 2021/22 Annual Investment Strategy was approved by Council in February 2021 and was subjected to a mid-year review in September 2021. In undertaking the review, no changes were made to the Council's minimum counter-party credit requirement (typically Fitch A-, F1 unless UK state owned) or counter-party exposure limits (maximum of 20% of funds per financial institution). Subject to constraints, discretion to extend investment duration for UK regulated financial institutions by up to six months over the Council's external treasury advisor's suggested duration was also retained.

1.5.2 **Cash flow investment**. In 2021/22 cash flow surpluses averaged £22.3m and earned an average rate of return of 0.14%. The benchmark used to compare performance, (LIBID/SONIA Hybrid) was 0.03%. Cash flow surpluses arise from the timing difference between the receipt of monies (from council tax, business rates, grants, etc.) and its subsequent payment (to Government, precepting authorities, housing benefit recipients, suppliers, staff, etc.). Cash flow surpluses are required to meet regular payment obligations and are invested in bank deposit accounts and money market funds which allow next day access. The opportunity to invest for longer durations and generate additional yield is taken when cash flow surpluses permit.

1.5.3 **Core cash investment**. In 2021/22 core cash averaged £20.3m and earned an average rate of return of 0.34%. The benchmark used to compare performance, (LIBID/SONIA Hybrid) was 0.03%. Core cash comprises the authority's revenue and capital reserves. Unlike cash flow, core cash is not required to meet regular payment obligations and is available to invest for longer durations including durations exceeding one year. This added flexibility allows core cash to generate a better return relative to cash flow surpluses.

1.5.4 **Medium-term investment**. In recent years multi asset (diversified income) funds have grown in popularity. Like property funds, multi asset funds aim to generate returns over and above inflation and thus preserve spending power.

1.5.5 A total of £3m was initially invested equally across three funds in July and August, with a further £1.25m invested in November 2021 across two of the funds with the proceeds from the sale of River Walk offices. Additional multi asset fund investments could be made in the future as resources become available from asset disposals and other windfalls.

1.5.6 During the period July 2021 to March 2022 the investment in multi asset funds generated dividends of £95,869 which represents an annualised return of 3.87%.

1.5.7 As at 31 March 2022, the capital investment has depreciated in value by £143,000. The value of multi asset diversified income funds at 31 March stood at £4.107m. Members are reminded that our muti asset diversified income funds are medium term investments (5+ years) and the funds applied to them are not required to meet day to day spending commitments.

1.5.8 **Long-term investment**. The availability of cash balances over the longer term (10 years) and the suitability of different types of long-term investment (equities, bonds, and commercial property) was explored in the report to Audit Committee, January 2017. Of the alternatives, investment in property funds was considered best suited to meet the Council's more immediate funding need: a sustainable, stable income stream.

1.5.9 This does not however, preclude consideration of an alternative investment opportunity that meets the Council's strategic priorities and objectives, achieves value for money and delivers a financial return commensurate with the Council's risk appetite. Each such opportunity to be considered on a case-by-case basis as appropriate.

1.5.10 At the start of the year £5m was invested in property investment funds and no further sums were invested during the year. Investment was spread across three funds to ensure, as far as is possible, stability of annual income and capital growth over time. Additional property fund investments may be made in the future as resources become available from asset disposals and other windfalls.

1.5.11 In 2021/22 investment in property funds generated dividends of £158,725 which represents an annualised return of 3.17%.

1.5.12 Property funds issue and redeem primary units at a buy and sell price with the difference between the two prices reflecting the costs associated with buying and selling property (legal and other fees, stamp duty, etc.). The price spread varies from fund to fund but is typically in the region of 8% (6% on entry to a fund and 2% on exit). Where units are traded on a secondary market the impact of the spread can be reduced and delays in the purchase or redemption of units avoided. The table below compares the sale value of each investment if sold to the fund manager with the initial purchase price.

Property fund (Primary = units in the fund purchased from the fund manager. Secondary = units purchased from another investor at a discount. Date = first month the investment attracted dividends)	Purchase price (a) £	Sale value at date of purchase (b) £	Sale value March 2022 (c) £	March sale value above (below) purchase price (c-a) £
LAPF (Primary, July 2017)	1,000,000	922,200	1,095,400	95,400
Lothbury (Primary, July 2017)	1,000,000	927,700	1,061,400	61,400
Hermes (Secondary, Oct 2017)	1,000,000	939,000	1,131,000	131,000
LAPF (Primary, June 2018)	1,000,000	922,200	1,050,300	50,300
Lothbury (Secondary, July 2018)	1,000,000	973,000	1,041,000	41,000
Total	5,000,000	4,684,100	5,379,100	379,100

1.5.13 As at 31 March 2022, the capital investment has appreciated in value by £379,100. Members are reminded that our property fund investments are long-term (10 years) and the funds applied to them are not required to meet day to day spending commitments.

1.5.14 **Summary**. Investment performance for the year 2021/22 is summarised in the table below:

	2021/22 Average balance £m	Return % 	2021/22 Interest/ dividends earned £	2021/22 Revised Estimate £	Variance Better (worse) £
Cash flow surpluses	22.3	0.14	30,581	9,200	21,381
Core cash	20.3	0.34	69,874	55,000	14,874
Medium term investment	4.3	3.87	95,869	61,900	33,969
Long term investment	5.0	3.17	158,725	170,000	(11,275)
Total	51.9	0.82	355,049	296,100	58,949

1.5.15 The overall performance of the Authority's investments bettered the revised estimates by £58,949 (£105,049 when compared to the 2021/22 original estimates).

1.5.16 In finalising the Council's revised estimates, the income estimate for cash flow was reduced from £31,000 to £9,200; the return from core cash was increased from £49,000 to £55,000; and income from property funds held at £170,000.

1.6 Compliance with the Annual Investment Strategy

1.6.1 The Annual Investment Strategy aims to limit the Council's exposure to investment risks by prescribing: minimum counterparty credit criteria; maximum exposure limits in respect of sovereigns, counterparties, and groups of related counterparties; the type of investment instrument that can be used; and investment duration limits. Throughout the period April 2021 to March 2022 the requirements set out in the Annual Investment Strategy for 2021/22, as approved by Council in February 2021, were complied with. No liquidity issues were experienced resulting in nil borrowing throughout 2021/22.

1.7 Treasury and Prudential Codes of Practice

1.7.1 Updates to both the Prudential Code and Treasury Management Code were published by the Chartered Institute of Public Finance and Accountancy (CIPFA) in December 2021 and uphold a key principle that borrowing primarily for return on investment is not permissible.

1.7.2 Also re-emphasised that the risks associated with investment in '**non-financial assets** which are held primarily for financial returns' are properly evaluated, reported, subject to scrutiny and managed over time. The Council has no material non-financial investments.

1.7.3 The requirements of both the Treasury Management and Prudential Codes of Practice published by CIPFA have been considered and reflected as appropriate in this annual review.

Financial Services
May 2022

Annex 4

Prudential and Treasury Indicators

1 Prudential Indicators	2020/21 Actual £'000	2021/22 Original £'000	2021/22 Actual £'000
Capital expenditure	2,064	4,693	2,251
Ratio of financing costs to net revenue stream	-1.96%	-4.89%	-6.91%
Net borrowing requirement: Brought forward 1 April Carried forward 31 March In year borrowing requirement	 nil nil nil	 nil nil nil	 nil nil nil
Capital financing requirement as at 31 March	nil	nil	nil
Annual change in capital financing requirement	nil	nil	nil
Incremental impact of capital investment decisions: Increase in Council Tax (Band D) per Annum	-£1.03	£0.05	£0.05

2 Treasury Management Indicators	2020/21 Actual £'000	2021/22 Original £'000	2021/22 Actual £'000
Authorised limit for external debt: Borrowing Other long-term liabilities Total	 nil nil nil	 7,000 nil 7,000	 nil nil nil
Operational boundary for external debt: Borrowing Other long-term liabilities Total	 nil nil nil	 4,000 nil 4,000	 nil nil nil
Actual external debt	nil	nil	nil
Upper limit for fixed rate exposure over one year at year end	nil	0 – 60%	nil
Upper limit for variable rate exposure under one year at the year end	23,794 (64.7%)	40 – 100%	22,131 (40.0%)
Upper limit for total principal sums invested for over 365 days	5,000 (13.6%)	60%	9,250 (16.7%)

3 Maturity structure of new fixed rate borrowing during 2021/22	Upper limit %	Lower limit %
Under 12 months	100	nil
Over 12 months	nil	nil