

# TONBRIDGE & MALLING BOROUGH COUNCIL

## AUDIT COMMITTEE

17 April 2023

### Report of the Director of Finance and Transformation

#### Part 1- Public

#### Matters for Information

#### 1 TREASURY MANAGEMENT PERFORMANCE UPDATE

The report provides details of investments undertaken and the return achieved in the first eleven months of the current financial year.

##### 1.1 Introduction

1.1.1 The Council's investments are derived from cash flow surpluses, core cash balances and other medium term and long term cash balances.

##### 1.2 Performance 1 April 2022 to 28 February 2023

1.2.1 A full list of investments held on 28 February 2023 is provided at **[Annex 1]** and copy of our lending list is provided at **[Annex 2]**. The table below provides a summary of funds invested and income earned at the end of February 2023.

	Funds invested on 28 February 2023	Average duration to maturity	Weighted average rate of return	SONIA benchmark (average)	Interest / dividends earned	Gross annualised return
	£m	Days	%	1 April to 28 February 2023 %	1 April to 28 February 2023 £	%
Cash flow	25.97	8	3.92	3.91	658,070	2.03
Core cash	28.00	167	4.25	4.08	576,530	2.43
<b>Sub-total</b>	<b>53.97</b>	<b>90</b>	<b>4.09</b>	<b>4.00</b>	<b>1,234,600</b>	<b>2.20</b>
Long term	5.00				130,420	3.46
Medium term	4.25				163,520	4.20
<b>Total</b>	<b>63.22</b>				<b>1,528,540</b>	<b>2.39</b>

Table 1

*Property funds pay dividends quarterly. The return quoted above is based on dividends received for the period April to December 2022 and on the return achieved since inception.*

- 1.2.2 **Cash flow and core cash investments.** Interest earned of £1,234,600 from cash flow surpluses and core cash balances to the end of February has exceeded the expectations of the revised estimate for the same period. This is due to the upward movement in interest rates over the past year and in particular the 0.75bps increase in November followed by a further 0.50bps in both December and February moving the bank rate from 2.25% to 4.0% in quick succession. This has provided the authority with the opportunity to invest excess funds at favourable rates, providing a higher than anticipated return.
- 1.2.3 The benchmarking service provided by the Council's treasury advisor enables our performance to be gauged against Link's other local authority clients. An extract from the latest benchmarking data is provided at **[Annex 3]**. The graph shows the return (vertical scale) vs. the credit / duration risk (horizontal scale) associated with an authority's investments. On 31 December 2022 the Council's return at 3.43% (purple diamond) was higher than the local authority average of 2.90%. Based on the Council's exposure to credit / duration risk the return was above Link's predicted return (between the green and red diagonal lines). The Council's risk exposure remained in-line with the local authority average.
- 1.2.4 **Long term investment.** £5m of the Council's expected long term cash balances together with new money derived from the sale of assets and other windfalls is invested in externally managed property funds. These investments generate an annual income stream and an expectation of capital appreciation over time sufficient to at least recoup the fund entry and exit costs circa 8%.
- 1.2.5 Income from property funds of £130,400 has been generated thus far in 2022/23 (quarter ending December 2022) which represents an annualised return of 3.46%. Income is in line with the original budget for the same period.
- 1.2.6 Capital appreciation / depreciation is recorded in the table below. Commercial property values having momentarily recovered from the impact suffered from Covid-19, has faced new challenges including rising inflation . All the property fund investments recorded capital depreciation in the period April 2022 to February 2023.

<b>Property fund</b>	Purchase price	Sale value at date of purchase	Sale value 28 February 2023	28 February 23 sale value above (below) purchase price (c-a) £
(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)	a	b	C	
	£	£	£	
LAPF (Primary, July 2017)	1,000,000	922,200	918,600	(81,400)
Lothbury (Primary, July 2017)	1,000,000	927,700	822,400	(177,600)
Hermes (Secondary, Oct 2017)	1,000,000	939,000	953,600	(46,400)
LAPF (Primary, June 2018)	1,000,000	922,200	880,700	(119,300)
Lothbury (Secondary, July 2018)	1,000,000	973,000	806,500	(193,500)
<b>Total change in principal</b>	5,000,000	4,684,100	4,381,800	<b>(618,200)</b>
			<b>Total dividends received to December 2022</b>	<b>868,500</b>
			<b>Net benefit since inception</b>	<b>250,300</b>

Table 2

### 1.3 Medium-term Investment

- 1.3.1 £4.25m of the Council's expected medium term cash balances together with new money derived from the sale of asset has been invested in externally managed diversified income funds. These investments will generate an annual income stream and will provide capital appreciation over time.
- 1.3.2 The diversified income funds have generated £163,520 up to 28 February 2023 which represents an annualised return of 4.2%. Income is some £23,270 higher than anticipated against the revised budget for the same period.

### 1.4 Legal Implications

- 1.4.1 Under Section 151 of the Local Government Act 1972, the Section 151 Officer has statutory duties in relation to the financial administration and stewardship of the authority including securing effective arrangements for treasury management. In addition, Link Asset Services are employed to provide independent advice on legislative and professional changes that impact on the treasury management function.

## **1.5 Financial and Value for Money Considerations**

- 1.5.1 Our investment income estimates for 2022/23 were increased by £554,800 when they were revised in January 2023. The final position for the investment income for 2022/23 is expected to be favourable variance circa £730,000 when compared to the revised income total of £951,900. The increase reflects the continued upward movement of interest rates that markets were offering at the time of preparing the revised estimates.
- 1.5.2 Performance is monitored against a benchmark return and against other local authorities in Kent and the broader local authority pool via Link's benchmarking service.
- 1.5.3 Whilst the annual income stream from the externally managed property funds and diversified income funds exhibits stability (circa 4% per annum net of management fees) capital values rise and fall with the cyclical nature of economic activity. During a downturn in the economy capital values may fall significantly. The duration of a property fund or diversified income fund investment may need to be extended to avoid crystalizing a loss and as a consequence the investment's duration cannot be determined with certainty.
- 1.5.4 Buying and selling property involves significant costs making property unsuitable for short term investment. Buying and selling costs are reflected in the entry fees (circa 6%) and exit fees (circa 2%) a property fund will charge unit holders. These fees are expected to be recouped overtime through capital appreciation.
- 1.5.5 The money being applied to the property fund investment from existing resources is expected to be available in perpetuity. Nevertheless, the Council's cash balances will continue to be monitored and due regard had to the potential for a fund to delay payment of redemption requests by up to 12 months. Funds will seek to minimise their own cash balances in favour of holding property and therefore manage redemption requests for the benefit of all fund participants. The Council is only likely to seek redemption to pursue a higher yielding income opportunity should one be identified.
- 1.5.6 Diversified income funds aim to limit risk by spreading investment across a broad range of asset classes (equities, bonds, property and cash). Nevertheless, the principal sum invested may fall or rise with the cyclical nature of economic activity or because of adverse economic conditions or market events.

## **1.6 Risk Assessment**

- 1.6.1 The application of best practice, including the regular reporting and scrutiny of treasury management activity, as identified by the CIPFA Code is considered to be an effective way of mitigating the risks associated with treasury management.

Background papers:

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Link Asset Services - benchmarking data.

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