

Audit Committee

14 April 2025

Part 1 - Public

Delegated



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Cabinet Member	Kim Tanner – Cabinet Member for Finance and Housing
Responsible Officer	Sharon Shelton – Director of Finance and Transformation
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Treasury Management Performance Update

1 Summary and Purpose of Report

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

2 Corporate Strategy Priority Area

- 2.1 Efficient services for all our residents, maintaining an effective council.
- 2.2 Prudent financial management of Council's investments will generate a yield to assist with the Council's overall budget objectives.

3 Recommendations

- 3.1 Members are asked to **NOTE**:
- The Treasury Management position as at 28 February 2025.
 - The current positions in respect of the Lothbury and Hermes Property Investment Funds.

4 Introduction and Background

- 4.1 The CIPFA (Chartered Institute of Public Finance and Accountancy) Code of Practice for Treasury Management 2021 recommends that Members be updated on treasury management activities at least quarterly. This report, therefore, ensures this Council is implementing best practice in accordance with the Code.
- 4.2 The Council's investments are derived from cash flow surpluses, core cash balances and other medium term and long term cash balances.

5 Investment Performance

- 5.1 A full list of investments held on 28 February 2025 is provided at **[Annex 1]** and a copy of our lending list of 28 February 2025 is provided at **[Annex 2]**. The table below provides a summary of funds invested and income earned at the end of February 2025.

	Funds invested on 28 February 2025	Average duration to maturity	Weighted average rate of return	SONIA benchmark February 2025	Interest / dividends earned	Gross annualised return
	£m	Days	1 April to 28 February 2025 %	%	1 April to 28 February 2025 £	%
Cash flow	26.02	6	4.54	4.47	1,330,890	4.56
Core cash	33.14	151	4.78	4.55	1,478,080	5.20
Long term	3.72				118,040	4.21
Medium term	4.25				192,750	4.96
Total	67.13				3,119,760	--

Table 1

Property funds pay dividends quarterly. The return quoted above is based on dividends received for the period April to December 2024.

- 5.2 **Cash flow and core cash investments.** Interest earned of £2,808,970 from surplus cash flow and core cash balances to the end of February has exceeded expectation when compared to the revised estimate for the same period. This positive variance is primarily driven by the slower-than-anticipated reduction in the Bank Rate, which has resulted in sustained higher interest yields on deposits.
- 5.3 The revised budget has been updated to incorporate the sustained higher bank rate, ensuring that future investment interest income projections are aligned with the current market expectations.
- 5.4 The Council takes advantage of MUFG's (formerly Link Asset Services) benchmarking service which enables performance to be gauged against MUFG's other local authority clients. An extract from the latest benchmarking data is provided in the form of a scatter graph at **[Annex 3]**. The graph shows the return (vertical scale) vs. the credit / duration risk (horizontal scale) associated with an authority's investments. As at 31 December 2024 the Council's return was 4.76% (purple diamond) in-line with the local benchmarking group average of 4.75%. MUFG's predicted return is between the upper and lower boundary indicated by the diagonal lines. The Council's risk exposure remains consistent with the local authority average.

- 5.5 Only cash flow and core cash returns form part of the benchmarking data. The additional return the Council makes from its property fund, and diversified income fund investments are not included. The data also excludes any short-term borrowing costs authorities may have incurred to meet payment obligations; however, no such costs have been incurred to date, and none are anticipated during the remainder of 2024/25.
- 5.6 **Long term investment.** £5m was invested in property investment funds, spread across three funds to ensure, as far as is possible, stability of annual income and capital growth over time.
- 5.7 During the period 1 April 2024 to 31 December 2024, as property funds are reported quarterly, the £3.72m investment in property funds generated dividends of £118,040 which represents an annualised return of 4.21% (3.65% in 2023/24).
- 5.8 The long-term investment figure set out in Table 2 concentrates on the LAPF and Hermes Property Funds. Lothbury Property Fund is shown separately in Table 3 to provide details of the repayment of capital investment from the sale of assets due to the termination of the Fund on 30 May 2024.
- 5.9 As part of the current year budget review, income projections from property funds have been adjusted downward to reflect changes in shareholdings and their capacity to generate future dividends. While it was anticipated that investment income from the Lothbury portfolio would be removed due to uncertainty, an unbudgeted dividend income of circa £32,270 has been received in 2024/25.
- 5.10 The overall income from all property funds is now expected to exceed the revised budget for the 2024/25 financial year by circa £39k.
- 5.11 Sale values at the end of February 2025 vs initial purchase prices are as follows:

Property fund	Purchase price	Sale value at date of purchase	Sale value 28 February 2025	28 February 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	price (c-a)
	£	£	£	£
LAPF (Primary, July 2017)	1,000,000	922,200	888,430	(111,570)
Hermes (Secondary, Oct 2017)	1,000,000	939,000	909,740	(90,260)
LAPF (Primary, June 2018)	1,000,000	922,200	851,830	(148,170)
Total change in principal	3,000,000	2,783,400	2,650,000	(350,000)
			Total dividends received to December 2024	834,450
			Net benefit since inception	484,450

Table 2

- 5.12 Since inception, the Council have received dividends from the above property fund investments totalling £834,450.
- 5.13 Investment institutes continue to diversify their portfolios to optimise returns while considering prevailing market conditions. Between April 2024 and December 2024, all property fund investments recorded capital depreciation. Despite this, property funds have continued to distribute dividends, with £118,040 received in the first nine months of the financial year.
- 5.14 Following the withdrawal of several investors, Lothbury Property Trust were unable to secure a viable path forward and was officially terminated on 30 May 2024.
- 5.15 As shown in Table 3 below, we have, to date, received five payments totalling £1,276,520 of our initial investment. The remaining assets are now expected to be sold by June 2025, with distributions made as asset sales are finalised and dividends paid from income-generating assets.
- 5.16 Taking into account the dividends received since the fund's inception, the breakeven point would be achieved with the recovery of £379,040 from the outstanding assets.

Property fund	Purchase price	Sale value at date of purchase	Principal Investment Returned	Principal Investment Balance Outstanding
(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	
	£	£	£	£
Lothbury Property Trust	2,000,000	1,900,700	1,276,520	(723,480)
Total dividends received to February 2025				379,040
Net balance to breakeven point				(344,440)

Table 3

- 5.17 On 13 February 2025, Hermes Property Trust held an Extraordinary General Meeting (EGM) following a redemption request for approximately 22% of the fund. The meeting included a vote on proceeding with potential merger options, which required 75% approval to pass. The resolution was successful, and discussions are now moving forward.
- 5.18 However, it has been announced that small-value investments will not be eligible to form part of the merger. As a result, the Council, along with many other smaller stakeholders, will have their shares realised and paid out upon the successful completion of the merger.
- 5.19 Members are reminded that higher yielding investments (e.g. property, equities) have the potential to fluctuate in value, both up and down. It is this feature which makes them unsuitable for short term investment where certainty over value at maturity is a key criteria. The Council's property fund investments are not

required to meet day to day spending commitments and will only be realised should a higher yielding opportunity be identified.

5.20 **Medium term investment.** £4.25m of the Council's expected medium term cash balances together with new money derived from the sale of assets has been invested in externally managed diversified income funds. These investments will generate an annual income stream and will provide capital appreciation over time.

5.21 During the period April 2024 to February 2025 the £4.25m investment in multi asset funds generated dividends of £192,750 which represents an annualised return of 4.96%.

6 Financial and Value for Money Considerations

6.1 The Bank Rate is currently 4.50%. MUFG's current forecast (February 2025) anticipates Bank Rate will fall back to 3.75% by March 2026. Longer term, the rates are expected to fall back to 3.50% and remain there for the foreseeable future.

6.2 While the Council has benefited from higher-for-longer interest rates, the Bank of England initiated its rate cut cycle in August 2024, gradually reducing the Bank Rate from 5.25% to 4.5% over several months. In response, the Council has carefully considered its cash management strategy, aiming to balance liquidity needs with the opportunity to secure higher investment returns. Key considerations include:

6.2.1 **Short-Term Liquidity:** Ensuring sufficient cash is readily available to meet operational and unforeseen financial commitments.

6.2.2 **Longer-Term Investments:** Identifying opportunities to invest surplus cash (up to 1 year) at fixed higher rates before further interest rate reductions diminish returns.

6.2.3 **Diversification:** Allocating funds across a range of investment vehicles to mitigate risk while maximising returns.

6.2.4 **Market Monitoring:** Regularly assessing economic conditions and interest rate forecasts to make informed investment decisions.

6.3 By adopting a proactive approach, the Council aims to optimise returns on its cash holdings while maintaining financial stability.

6.4 Performance is monitored against a benchmark return and against other local authorities in Kent and the broader local authority pool via MUFG's (formerly Link Asset Services) benchmarking service.

6.5 Whilst the annual income stream from a property fund 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 investment may need to be extended to avoid crystallising a loss and as a consequence the investment's duration cannot be determined with certainty.

- 6.6 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 over time through capital appreciation.
- 6.7 The money being applied to 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.
- 6.8 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 as a consequence of adverse economic or market events. Short term bond values are linked to interest rate expectations and long-term bond values are linked to inflation expectations. Funds aim to minimise the risk of issuer default by investing in a broad spread of issuers and across different sectors and geographic regions. Nevertheless, the principal sum invested may fall as a consequence of adverse economic or market events.

7 Risk Assessment

- 7.1 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.
- 7.2 MUFG (formerly Link Asset Services) are employed to provide advice on the content of the Treasury Management and Annual Investment Strategy and this, coupled with a regular audit of treasury activities (balance sheet reviews, benchmarking and general support) ensures that the requirements of the Strategy and the Treasury Policy Statement adopted by this Council are complied with.

8 Legal Implications

- 8.1 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, MUFG (formerly Link Asset Services) are employed to provide

independent advice on legislative and professional changes that impact on the treasury management function.

- 8.2 This report fulfils the requirements of the Chartered Institute of Public Finance & Accountancy's Treasury Management and Prudential Codes of Practice 2021 and the 2018 Statutory Guidance on Local Government Investments.

9 Cross Cutting Issues

9.1 Climate Change and Biodiversity

- 9.2 While the Treasury Management Code outlines the principle for investments as Security Liquidity and Yield is core, it recognises that ESG issues are increasingly significant for investors.

- 9.3 Consideration will be given to how we can formalise ESG as part of the Treasury Management Strategy Statement, while appreciating it is better developed in the equity and bond markets, than the short-term cash deposits, where the majority of the Council's portfolio is held.

9.4 Equalities and Diversity

- 9.4.1 The decisions recommended through this paper have a remote or low relevance to the substance of the Equality Act. There is no perceived impact on end users.

Background Papers	Benchmarking data.
Annexes:	(1) TMBC Investment Summary February 2025 (2) TMBC Lending List February 2025 (3) TMBC Benchmarking December 2024