

Audit Committee

29 September 2025

Part 1 - Public

Recommendation to Council



Cabinet Member	Martin Coffin – Cabinet Member for Finance, Waste and Technical Services
Responsible Officer	Paul Worden – Head of Finance
Report Author	Donna Riley – Principal Accountant

Treasury Management Performance Update and Mid-Year Review for 2025/26

1 Summary and Purpose of Report

- 1.1 The report provides details of investments undertaken during April to July of the current financial year, and a mid-year review of the Treasury Management and Annual Investment Strategy for 2025/26.

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 **RECOMMEND** that Council:
- Endorse the action taken by officers in respect of Treasury Management activity for April to July 2025.
 - Endorse the inclusion of Ethical Investments to the existing parameters intended to limit the Council's exposure to investment risks as per paragraph 9.2.
 - Note the current position 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 and include a mid-year review of the Treasury Management and Annual Investment Strategy. This report, therefore, ensures this Council is implementing best practice in accordance with the Code.
- 4.2 The primary requirements of the Code are as follows:
- The creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.
 - The creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.
 - Receipt by Full Council of an Annual Treasury Management Strategy Statement, including the Annual Investment Strategy, for the year ahead; a mid-year Review Report (this report) and an Annual Report (stewardship report) covering activities during the previous year.
 - Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.
 - Delegation by the Council of the role of scrutiny of the treasury management strategy and policies to a specific named body. For this Council, the delegated body is the Audit Committee.
- 4.3 This mid-year report has been prepared in compliance with the Code and covers the following:
- An economic update and interest rate forecast.
 - Investment performance for April to July for the 2025/26 financial year including recent benchmarking data.
 - Compliance with Treasury and Prudential Limits for 2025/26.
 - A review of the risk parameters contained in the 2025/26 Treasury Management and Annual Investment Strategy.

5 Investment Performance

- 5.1 In accordance with the CIPFA Code, the Council's priorities, in order of importance, are to ensure security of capital; liquidity; and having satisfied both, to obtain an appropriate level of return which is consistent with the Council's risk appetite.
- 5.2 The Council's investments are derived from cash flow surpluses, core cash balances and other long term cash balances.
- 5.3 Cash flow surpluses are available on a temporary basis and the amount is mainly dependent on the timing of council tax and business rates collected and their payment to precept authorities and government. Less significant cash flows relate to receipt of grants, payments to housing benefit recipients, suppliers and staff. Cash flow surpluses build up during a financial year and are spent by financial year end. Thus far in 2025/26 cash flow surpluses have averaged £20.19m.
- 5.4 The Authority also has £33m of core cash balances. These funds are for the most part available to invest for more than one year, albeit a proportion is usually transferred to cash flow towards the end of the financial year to top-up daily cash balances. Core cash includes the Council's capital and revenue reserves which are being consumed over time to meet capital expenditure and 'buy time' to enable the authority to deliver its revenue savings targets.
- 5.5 Cash flow and core cash balances also include sums to meet business rate appeals which are expected to be resolved in 2025/26 and future years.
- 5.6 Long term investments at the end of July 2025 comprised of £3.68m in property fund investments.
- 5.7 Medium term investments at the end of July 2025 comprised £4.25m in multi-asset fund investments.
- 5.8 A full list of investments held on 31 July 2025 is provided at **[Annex 1]** and a copy of our lending list of 31 July 2025 at **[Annex 2]**. The table below provides a summary of funds invested and interest / dividends earned at the end of July.

	Funds invested on 31 July 2025	Average duration to maturity	Weighted average rate of return	SONIA benchmark July 2025	Interest / dividends earned	Gross annualised return
	£m	Days	1 April to 31 July 2025 %	%	1 April to 31 July 2025 £	%
Cash flow	20.19	5	4.24	4.26	368,900	4.37
Core cash	33.00	74	4.41	4.18	471,300	4.62
Long term	3.00				28,730	4.04
Long term (LPT)	0.68				1,715	--
Medium term	4.25				56,830	4.00
Total	61.12				927,475	--

Table 1

Property funds pay dividends quarterly. The return quoted above is based on dividends received for the quarter April to June 2025.

- 5.9 **Cash flow and core cash investments.** Interest earned of £840,200 from surplus cash flow and core cash balances to the end of July 2025 represent a positive variance of £116,220 against the original 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.
- 5.10 Market sentiment around future rate cuts is reflected in the investment opportunities being offered by financial institutions. Meanwhile, money market funds continue to yield near the bank rate level (5-10 bps higher at the time of writing), providing investors with a low risk, enhanced liquidity option.
- 5.11 The Council takes advantage of MUFG's 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 30 June 2025, the Council's return was 4.43% (purple diamond) in-line with the local benchmarking group average of 4.36%. 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.
- 5.12 **Long term investment.** £5m was originally 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.

- 5.13 During the period 1 April 2025 to 30 June 2025, the £3m investment in property funds generating dividends of £28,730 which represents an annualised return of 4.04%.
- 5.14 Of the initial £2m invested in Lothbury Property Fund, sales of assets and the return of capital monies, leaves an outstanding balance of £675,760. While unbudgeted dividends are being received, it is on an ad-hoc basis. Further information is set out in paragraphs 5.19 to 5.21.
- 5.15 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.
- 5.16 Sale values at the end of July 2025 vs initial purchase prices are as follows:

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	Sale value at date of purchase	Sale value 31 July 2025	31 July sale value above (below) purchase price (c-a)
	a	b	c	
	£	£	£	£
LAPF (Primary, July 2017)	1,000,000	922,200	897,810	(102,190)
Hermes (Secondary, Oct 2017)	1,000,000	939,000	908,350	(91,650)
LAPF (Primary, June 2018)	1,000,000	922,200	860,830	(139,170)
Total change in principal	3,000,000	2,783,400	2,666,990	(333,010)
Total dividends received to June 2025				863,175
Net benefit since inception				530,165

Table 2

- 5.17 Since inception, the Council have received dividends from the above property fund investments totalling £863,175.
- 5.18 Investment institutes continue to diversify their portfolios to optimise returns while considering prevailing market conditions. Between April and July 2025, all property fund investments recorded capital depreciation. Despite this, property funds have continued to distribute dividends of £30,445 for the first quarter of the financial year.
- 5.19 Lothbury Property Fund officially terminated on 30 May 2024 and commenced the sale of assets.
- 5.20 As shown in Table 3 below, the Council have, to date, received six payments totalling £1,324,240 of our initial investment. The remaining assets, valued at

£65.5m are currently under offer and sales are expected to conclude by August 2025. Distributions will be made as assets sales are completed.

- 5.21 Taking into account the dividends received since the fund's inception, the breakeven point would be achieved with the recovery of £295,000 from the outstanding assets.

Property fund <small>(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)</small>	Purchase price	Sale value at date of purchase	Principal Investment Returned	Principal Investment Balance Outstanding
	a £	b £	c £	£
Lothbury Property Trust	2,000,000	1,900,700	1,324,240	(675,760)
Total dividends received to July 2025				380,755
Net balance to breakeven point				(295,005)

Table 3

- 5.22 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. A subsequent EGM took place on 24 June 2025 and the resolution to proceed with the merger was successful. The expected completion date for the merger is 14 August 2025.
- 5.23 Federated Hermes announced that small-value investments will be excluded from the merger. Consequently, the Council, along with other minority stakeholders, will have its shares realised and paid out upon the successful completion of the merger.
- 5.24 The capital investment expected to be returned from Federated Hermes is in the region of £908,000.
- 5.25 This return represents the crystallisation of the investment rather than a discretionary decision to divest. The receipt will provide an opportunity to support cash flow, replenish reserves and will be considered for short-term reinvestment in line with the Council's Treasury Management Strategy.
- 5.26 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.
- 5.27 **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.

- 5.28 During the period April 2025 to July 2025 the £4.25m investment in multi asset funds generated dividends of £56,830 which represents an annualised return of 4.0%.

6 Compliance with the Annual Investment Strategy

- 6.1 Throughout the period April to July 2025, all the requirements contained in the 2025/26 Annual Investment Strategy intended to limit the Council's exposure to investment risks (minimum sovereign and counterparty credit rating; durational limits; exposure limits in respect of counterparties, groups of related counterparty and sovereigns; and specified and non-specified investment limits) have been complied with. No borrowing was undertaken during April to July 2025.
- 6.2 The Council has also operated within the treasury limits and prudential indicators set out in the Annual Investment Strategy, and in compliance with the Council's Treasury Management Practices. The Prudential and Treasury Indicators can be found in **[Annex 4]** to this report.

7 Interest Rate Forecast

- 7.1 MUFG reviewed and updated their interest rate forecast following the Bank of England's Monetary Policy Committee (MPC) meeting in August.

The table below sets out the revised rates which are broadly in-line with the assumptions reported to Committee in January 2025 as part of the Treasury Management and Annual Investment Strategy 2025/26. The Bank Rate is projected to undergo a managed reduction over the next two years, before stabilising at 3.25%.

MUFG - August 2025	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27	Jun-27	Sep-27	Dec-27	Mar-28
	%	%	%	%	%	%	%	%	%	%	%
Bank Rate	4.00	4.00	3.75	3.75	3.50	3.50	3.50	3.50	3.25	3.25	3.25
3 mth ave earnings	4.00	4.00	3.80	3.80	3.50	3.50	3.50	3.50	3.30	3.30	3.30
6 mth ave earnings	4.00	3.90	3.70	3.70	3.50	3.50	3.50	3.50	3.30	3.30	3.40
12 mth ave earnings	4.00	3.90	3.70	3.70	3.50	3.50	3.50	3.50	3.30	3.40	3.50
25yr PWLB	6.10	5.90	5.70	5.70	5.50	5.50	5.50	5.40	5.40	5.30	5.30

Table 4

8 Economic Background

- 8.1 CPI inflation rose from 3.6% in June to 3.8% (consensus 3.7%) and is expected to peak of 4% in September due to ongoing pressures in certain sectors such as services and domestically driven costs, as well as global agricultural commodity

prices. However, the inflation trajectory beyond the short-term is likely to fall below the BoE's 2% target by 2027, or earlier if the macroeconomic developments, such as the strengthening of the pound and declines in global energy prices, can be sustained.

- 8.2 It is expected that UK economic growth will remain subdued in the near-term after the first quarter's boost by 0.7% from tariff front-running (reported in July) GDP growth is forecast at 1.0% in 2025 and 1.2% in 2026.
- 8.3 The labour market continues to face pressures from rising costs, notably through increases to the minimum wage and employer's National Insurance contributions. These factors are weighing on business sentiment and recruitment intentions. Unemployment is forecast to rise, with rates expected to peak around 5.0% in Q4 2025, signalling a gradual softening in labour demand.
- 8.4 It is anticipated that the BoE will cut interest rates to 3.0% in 2026. Meanwhile, future fiscal tightening is expected, through increased taxation.
- 8.5 While the situation in the Middle East remains fluid, the economic ramifications are being monitored closely by markets, policymakers, and international institutions. The key channels of impact include energy markets, inflation, financial market volatility and regional economic stability.

9 Review of Risk Parameters

- 9.1 Members will recall the detailed consideration that was given to the 2025/26 Treasury Management and Annual Investment Strategy at Audit Committee in January. For ease of reference the parameters included in the Strategy that aim to limit the Council's exposure to investment risks are summarised in **[Annex 5]**.
- 9.2 In undertaking this review *a change to the current approved risk parameters to include Ethical Investments are being proposed at this time. Future consideration will be given to the inclusion of borrowing and debt rescheduling in anticipation of the future needs of the Council.* The Strategy ensures that the Council is investing in high credit quality counterparties and there are an adequate number of counterparties available to maintain a well-diversified portfolio. However, we will continue to look to expand the Council's lending list to include any UK banks and building societies that don't currently feature on our lending list but meet our minimum credit criteria. This will ensure that we can take advantage of all available opportunities as they arise.
- 9.3 There is a need to continue to explore alternative investment options to ensure the maximum return on investment for the Council. Subject to an understanding and acceptance of any associated risks with such investments, they may be offered for inclusion in next year's Annual Investment Strategy. Any investment will of course be dependent on the level of reserves and other balances available for such an investment.

10 Financial and Value for Money Considerations

- 10.1 **Short-Term Liquidity:** Ensuring sufficient cash is readily available to meet operational and unforeseen financial commitments.
- 10.2 **Longer-Term Investments:** Identifying opportunities to invest surplus cash (up to 1 year) at fixed higher rates before further interest rate reductions diminish returns.
- 10.3 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.
- 10.4 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 over time through capital appreciation.
- 10.5 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.
- 10.6 **Diversification:** Allocating funds across a range of investment vehicles to mitigate risk while maximising returns.
- 10.7 **Market Monitoring:** Regularly assessing economic conditions and interest rate forecasts to make informed investment decisions.
- 10.8 By adopting a proactive approach, the Council aims to optimise returns on its cash holdings while maintaining financial stability.
- 10.9 Performance is monitored against a benchmark return and against other local authorities in Kent and the broader local authority pool via MUFG's benchmarking service.

11 Risk Assessment

- 11.1 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.

- 11.2 MUFG 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.

12 Legal Implications

- 12.1 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 are employed to provide independent advice on legislative and professional changes that impact on the treasury management function.
- 12.2 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.

13 Cross Cutting Issues

- 13.1 Climate Change and Biodiversity
- 13.2 While the Treasury Management Code outlines the principle for investments as Security Liquidity and Yield as core, it recognises that environmental, social and governance (ESG) issues are increasingly significant for investors.
- 13.3 The Council's Treasury Management activities will continue to be guided by the primary principles of Security, Liquidity and Yield (SLY) as part of the Treasury Management Strategy Statement. In addition, consideration will be given to the incorporation of ethical investment criteria within the investment decision-making process.
- 13.4 Investment counterparties will be required to meet the Council's approved lending criteria to ensure the ongoing safeguarding of public funds. Where ethical investment opportunities are available and consistent with the Council's security and liquidity requirements, such options will be considered in the first instance.
- 13.5 The Council recognises that, while ethical considerations are an important element of its investment strategy, any decision to prioritise such opportunities will be assessed in the context of potential impacts on investment yield when compared to other suitable options.
- 13.6 Equalities and Diversity
- 13.7 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:	<ul style="list-style-type: none"> (1) TMBC Investment Summary July 2025 (2) TMBC Lending List July 2025 (3) TMBC Benchmarking June 2025 (4) TMBC Prudential and Treasury Indicators 2025/26 (5) TMBC Risk Parameters 2025/26