Classification: Public
Key Decision: No

Gravesham Borough Council

Report to:	Finance and Audit Committee
Date:	8 November 2023
Reporting officer:	Director (Corporate Services)
Subject:	Treasury Management Mid-Year Review 2023/24

Purpose and summary of report:

To provide a mid-year review update report to Members of the Finance and Audit Committee on treasury management activity undertaken during the period April to September 2023.

Recommendations:

1. The Finance and Audit Committee note the contents of this report

Key Implications:	
Item	**Implications**
Legal	As per section 1.13B.67 of the Council's Constitution, the Chief Finance officer has delegated responsibility from Cabinet. "in respect of borrowing and investments to arrange such loans as are legally permitted to meet the Council's borrowing requirements"
Finance and Value for Money	A summary of the perceived risks associated with Treasury Management were identified in the Treasury Management Strategy approved by Council on 21 February 2023. Officers continue to monitor the risks on a day to day basis and identify mitigating actions to minimise risks. In order to achieve a balanced budget, the authority relies upon generating maximum interest from its investments whilst minimising the exposure to risk. In order to achieve this, investments are only placed with institutions which meet the criteria set out within this report. Investment durations do not exceed those as advised by Capita Asset Services credit ratings which are associated with the specific institutions. Where the authority is required to borrow to meet the needs of the authority, officers will seek advice from Capita Asset Services on timings and options in order to ensure the best deal for the authority.

Corporate Plan	Strategic Objective #3 Progress; Sound Financial Management & Successfully Managing Key Business Risks.
Climate Change	Climate Change implications are one consideration of ESG investments which are covered in Section 11 of this report.

1. BACKGROUND

1.1 **Capital Strategy:** In December 2021, the Chartered Institute of Public Finance and Accountancy, (CIPFA), issued revised Prudential and Treasury Management Codes. These require all local authorities to prepare a Capital Strategy which is to provide the following : -

- a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services;
- an overview of how the associated risk is managed;
- the implications for future financial sustainability.

1.2 **Treasury management** The Council operates a balanced budget, which broadly means cash raised during the year will meet its cash expenditure. Part of the treasury management operations ensure this cash flow is adequately planned, with surplus monies being invested in low risk counterparties, providing adequate liquidity initially before considering optimising investment return.

1.3 The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer term cash flow planning to ensure the Council can meet its capital spending operations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses, and on occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

1.4 Accordingly, treasury management is defined as:

"The management of the local authority's borrowing, investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

2. INTRODUCTION

2.1 This report has been written in accordance with the requirements of the Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice on Treasury Management (revised 2021). The primary requirements of the Code are as follows:

- Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.
- 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 the Full Council of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum

Revenue Provision Policy - for the year ahead, a **Mid-year Review Report** and an Annual Report (stewardship report) covering activities during the previous year. (Quarterly reports are also required for the periods ending April to June and October to December but may be assigned to a designated committee or panel as deemed appropriate to meet the Treasury Management governance and scrutiny aspects of the Council).

- 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 treasury management strategy and policies to a specific named body. For this Council the delegated body is the Finance and Audit Committee.

2.2 This mid-year report has been prepared in compliance with CIPFA's Code of Practice on Treasury Management, and covers the following:

- An economic update for the first half of the 2023/24 financial year;
- A review of the Treasury Management Strategy Statement and Annual Investment Strategy;
- The Council's capital expenditure, as set out in the Capital Strategy, and prudential indicators;
- A review of the Council's investment portfolio for 2023/24;
- A review of the Council's borrowing strategy for 2023/24;
- A review of any debt rescheduling undertaken during 2023/24;
- A review of compliance with Treasury and Prudential Limits for 2023/24.

3. ECONOMIC BACKGROUND

3.1 The following economic performance update has been provided by Link Asset Services – Treasury Solutions as at 4 October 2023.

3.2 The first half of 2023/24 saw:

- Interest rates rise by a further 100bps, taking Bank Rate from 4.25% to 5.25% and, possibly, the peak in the tightening cycle.
- Short, medium and long-dated gilts remain elevated as inflation remained high.
- A decline in real GDP in July, mainly due to more strikes.
- CPI inflation falling from 8.7% in April to 6.7% in August, its lowest rate since February 2022, but still the highest in the G7.
- Core CPI inflation declining to 6.2% in August from 7.1% in April and May, a then 31 years high.

3.3 The fall in GDP in July suggests that underlying growth has lost momentum since earlier in the year. Some of the weakness in July was due to there being almost twice as many working days lost to strikes in July (281,000) than in June (160,000). But with output falling in 10 out of the 17 sectors, there is an air of underlying weakness.

3.4 The fall in the composite Purchasing Managers Index in September left it at its lowest level since COVID-19 lockdowns reduced activity in January 2021. At face value, it is consistent with the 0.2% q/q rise in real GDP in the period April to June, being followed by a contraction of up to 1% in the second half of 2023.

3.5 The 0.4% m/m rebound in retail sales volumes in August is not as good as it looks as it partly reflected a pickup in sales after the unusually wet weather in July. Sales volumes in August were 0.2% below their level in May, suggesting much of the resilience in retail activity in the first half of the year has faded.

3.6 As the growing drag from higher interest rates intensifies over the next six months, the economy is likely to continue to lose momentum and soon fall into a mild recession. Strong labour demand, fast wage growth and government handouts have all supported household incomes over the past year. And with CPI inflation past its peak and expected to decline further, the economy has got through the cost-of- living crisis without recession. But even though the worst of the falls in real household disposable incomes are behind us, the phasing out of financial support packages provided by the government during the energy crisis means real incomes are unlikely to grow strongly. Higher interest rates will soon bite harder too. With the Bank of England expected to keep interest rates at the probable peak of 5.25% until the second half of 2024. Mortgage rates are likely to stay above 5.0% for around a year.

3.7 The tightness of the labour market continued to ease, with employment in the three months to July falling by 207,000. The further decline in the number of job vacancies from 1.017m in July to 0.989m in August suggests that the labour market has loosened a bit further since July. That is the first time it has fallen below 1m since July 2021. At 3.0% in July, and likely to have fallen to 2.9% in August, the job vacancy rate is getting closer to 2.5%, which would be consistent with slower wage growth. Meanwhile, the 48,000 decline in the supply of workers in the three months to July offset some of the loosening in the tightness of the labour market. That was due to a 63,000 increase in inactivity in the three months to July as more people left the labour market due to long term sickness or to enter education. The supply of labour is still 0.3% below its pre-pandemic February 2020 level.

3.8 But the cooling in labour market conditions still has not fed through to an easing in wage growth. While the monthly rate of earnings growth eased sharply, a lot of that was due to the one-off bonus payments for NHS staff in June not being repeated in July. The headline 3myy rate rose which meant UK wage growth remains much faster than in the US and in the Euro-zone. Moreover, while the Bank of England’s closely watched measure of regular private sector wage growth eased a touch in July, it is still well above the Bank of England’s prediction for it to fall in September.

3.9 CPI inflation declined from 6.8% in July to 6.7% in August, the lowest rate since February 2022. The biggest positive surprise was the drop in core CPI inflation, which declined from 6.9% to 6.2%. That reverses all the rise since March and means the gap between the UK and elsewhere has shrunk (US core inflation is 4.4% and in the Euro-zone it is 5.3%). Core goods inflation fell from 5.9% to 5.2% and the further easing in core goods producer price inflation, from 2.2% in July to a 29-month low of 1.5% in August, suggests it will eventually fall close to zero. But the really positive development was the fall in services inflation from 7.4% to 6.8%. That also reverses most of the rise since March and takes it below the forecast of 7.2% the Bank of England published in early August.

3.10 In its latest monetary policy meeting on 20 September, the Bank of England left interest rates unchanged at 5.25%. The weak August CPI inflation release, the recent loosening in the labour market and the downbeat activity surveys appear to have convinced the Bank of England that it has already raised rates far enough. The minutes show the decision was “finely balanced”. Five MPC members (Bailey, Broadbent, Dhingra, Pill and Ramsden) voted for no change and the other four (Cunliffe, Greene, Haskel and Mann) voted for a 25bps hike.

3.11 The Bank of England wants the markets to believe in the higher for longer narrative. The statement did not say that rates have peaked and once again said if there was evidence of more persistent inflation pressures “further tightening in policy would be required”.

3.12 This narrative makes sense as the Bank of England does not want the markets to decide that a peak in rates will be soon followed by rate cuts, which would loosen financial conditions and undermine its attempts to quash inflation. The language also gives the Bank of England the flexibility to respond to new developments. A rebound in services inflation, another surge in wage growth and/or a further leap in oil prices could conceivably force it to raise rates at the next meeting on 2nd November, or even pause in November and raise rates in December.

4. INTEREST RATE FORECASTS

4.1 The Council's treasury advisor, Link Asset Services, has provided the following interest rate forecast. The PWLB rate forecasts below are based on the Certainty Rate (standard rate minus 20 bps) which the Council can access.

Link Group Interest Rate View	25.09.23												
	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26
BANK RATE	5.25	5.25	5.25	5.00	4.50	4.00	3.50	3.00	2.75	2.75	2.75	2.75	2.75
3 month ave earnings	5.30	5.30	5.30	5.00	4.50	4.00	3.50	3.00	2.80	2.80	2.80	2.80	2.80
6 month ave earnings	5.60	5.50	5.40	5.10	4.60	4.10	3.60	3.10	2.90	2.90	2.90	2.90	2.90
12 month ave earnings	5.80	5.70	5.50	5.20	4.70	4.20	3.70	3.20	3.00	3.00	3.00	3.00	3.00
5 yr PWLB	5.10	5.00	4.90	4.70	4.40	4.20	4.00	3.90	3.70	3.70	3.60	3.60	3.50
10 yr PWLB	5.00	4.90	4.80	4.60	4.40	4.20	4.00	3.80	3.70	3.60	3.60	3.50	3.50
25 yr PWLB	5.40	5.20	5.10	4.90	4.70	4.40	4.30	4.10	4.00	3.90	3.80	3.80	3.80
50 yr PWLB	5.20	5.00	4.90	4.70	4.50	4.20	4.10	3.90	3.80	3.70	3.60	3.60	3.60

4.2 The latest forecast on 25 September sets out a view that short and long-dated interest rates will be elevated for some little while, as the Bank of England seeks to squeeze inflation out of the economy.

5. TREASURY MANAGEMENT STRATEGY STATEMENT AND ANNUAL INVESTMENT STRATEGY UPDATE

5.1 The Treasury Management Strategy Statement (TMSS) for 2023/24 was approved by Full Council on 21 February 2023.

5.2 There are no policy changes to the TMSS; the details in this report update the position in the light of the updated economic position and budgetary changes already approved.

6. THE ST GEORGE'S SHOPPING CENTRE TRANSACTION

6.1 On 16 October 2023, the Council exited the legal arrangements with Aviva Investors relating to the St Georges Shopping Centre and replaced the financing with external borrowing which it sourced from the Public Works Loans Board (PWLB).

6.2 Given the transaction date fell after the end of the mid-year period, the current position figures detailed within this report include the existing financial arrangement with Aviva Investors with the replacement PWLB loans incorporated into the revised estimate figures, where applicable.

6.3 This transaction was subject to a report to Cabinet on 11 September 2023 entitled "Interests in land and assets belonging to the council" and a decision notice published on 10 October, to report the decision of the Director (Corporate Services), in consultation with the Leader of the Executive, Chief Executive and Deputy Monitoring Officer in accordance with the delegations approved by the Cabinet.

7. THE COUNCIL'S CAPITAL POSITION (PRUDENTIAL INDICATORS)

7.1 This part of the report is structured to update:

- The Council's capital expenditure plans
- How these plans are being financed
- The impact of changes in the capital expenditure plans on the prudential indicators and the underlying need to borrow; and
- Compliance with the limits in place for borrowing activity.

7.2 **Prudential Indicator for Capital Expenditure -** The table below shows the revised estimates for capital expenditure and the changes since the capital programme was agreed by Council as part of the budget.

Capital Expenditure	2023/24 Original Estimate £m	2023/24 Current Position £m	2023/24 Revised Estimate £m
Non HRA	74.196	7.624	29.670
HRA	20.594	9.343	23.106
Total	94.790	16.967	52.776

7.3 The revised estimate for Non HRA and HRA capital schemes reflects both the carried forward items from 2022/23 along with the forecast spend reported within the Quarter 2 Budget Monitoring reports.

7.4 **Changes to the Financing of the Capital Programme** - The following table draws together the main strategy elements of the capital expenditure plans (above), highlighting the original supported and unsupported elements of the capital programme, and the expected financing arrangements of this capital expenditure. The borrowing element of the table increased the underlying indebtedness of the Council by way of the Capital Financing Requirement (CFR), although this will be reduced in part by revenue charges for the repayment of debt (Minimum Revenue Provision). This direct borrowing need may also be supplemented by maturing debt and other treasury requirements.

Capital Financing	2023/24 Original Estimate £m	2023/24 Current Position £m	2023/24 Revised Estimate £m
Total	98.790	16.967	52.776
Financed by:			
Capital Receipts	8.056	0.646	5.797
Grants/Contributions	4.772	1.567	4.567
Revenue Grants not yet applied	0.251	0.049	0.902

Reserves	1.893	2.291	2.273
Revenue	3.809	0.128	5.067
Major Repairs Reserve	5.554	5.947	10.594
Total Financing	24.335	**10.178**	**29.200**
Borrowing Need	70.455	6.789	23.576

7.5 The borrowing need for 2022/23 currently stands at £23.576m, which is based on the forecast capital programme spend for the current year. External borrowing will be utilised for meet the full requirement.

7.6 **Changes to the Prudential Indicator for the Capital Financing Requirement (CFR), External Debt and the Operational Boundary** - The table below shows the CFR, which is the underlying external need to incur borrowing for a capital purpose. It also shows the expected debt position, which is termed the Operational Boundary.

	2023/24 Original Estimate £m	2023/24 Current Position £m	2023/24 Revised Estimate £m
Prudential Indicator – Capital Financing Requirement			
CFR – Non HRA	145.049	81.184	97.467
CFR – HRA	83.923	84.805	84.614
Total CFR	228.975	165.989	182.081
Net Movement in CFR (between years)	**69.790**	**6.789**	**22.881**
Prudential Indicator – the Operational Boundary for external debt			
Total	390.770	390.770	390.770

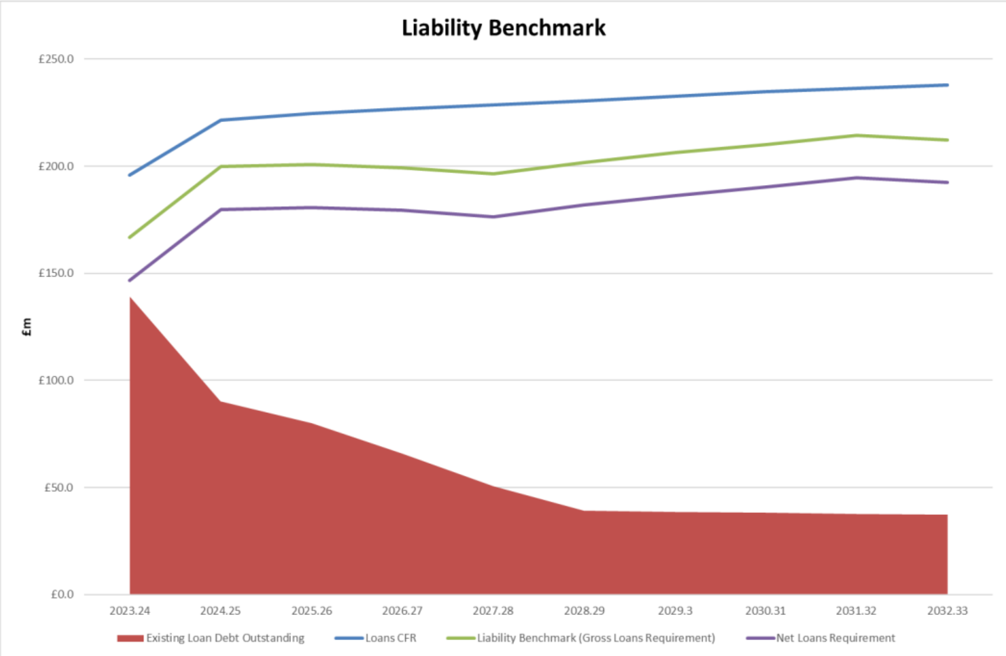
7.7 The operational boundary is the maximum amount of borrowing which the council is permitted to undertake on a day-to-day basis and must not be breached other than for temporary cash flow demand purposes. This level has not been breached during the first six months of 2023/24.

7.8 **Liability Benchmark –** A new prudential indicator was introduced into the 2023/24 TMSS. There are four components to the Liability Benchmark:

- Existing loan debt outstanding: the Council's existing loans that are still outstanding in future years
- Loans CFR: this is calculated in accordance with the loans CFR definition in the prudential code and projected into the future based on approved prudential borrowing and planned MRP
- Net loans requirement: this will show the Council's gross loan debt less treasury management investments based on its approved prudential borrowing, planned MRP and other major cash flow forecast

- Liability benchmark: this equals net loans requirement plus short term liquidity allowance

7.9 A graphical representation of the Council's Liability Benchmark (post the Aviva transaction is shown below.



7.10 **Limits to Borrowing Activity** - The first key control over the treasury activity is a prudential indicator to ensure that over the medium term, net borrowing (borrowings less investments) will only be for a capital purpose. Gross external borrowing should not, except in the short term, exceed the total CFR in the preceding year plus the estimates of any additional CFR for 2023/24 and next two financial years. This allows some flexibility for limited early borrowing for future years. The Council has approved a policy for borrowing in advance of need which will be adhered to if this proves prudent.

Borrowing Activity	2023/24 Original Estimate £m	2023/24 Current Position £m	2023/24 Revised Estimate £m
Debt as at 1 April	150.121	150.124	150.124
Expected change in debt	66.890	6.986	40.288
Total Gross Debt	**217.011**	**157.110**	**190.412**
CFR (year-end position)	228.975		182.081

7.11 The revised estimate shows that the revised estimate for the year shows that the total gross debt exceeds the CFR year-end position and therefore the Council cannot demonstrate that it is complying with this prudential indicator. This position has principally arisen because of the St Georges transaction, detailed in section 6 of this report and was reference in section section 8 of the report to Cabinet on 11 September 2023.

7.12 The Council currently has £20m of its cash balances invested in Property and Multi Asset Funds. The capital values of these investments are currently below the value that the Council entered the funds and therefore disinvesting at this time would result in a capital loss. The Council will consider exiting these arrangements at such time as capital values have improved with a view to repaying debt, if debt rescheduling options are favourable.

7.13 **Prudential Indicator for the Authorised Limit** - A further prudential indicator controls the overall level of borrowing. This is the Authorised Limit which represents the limit beyond which borrowing is prohibited and needs to be set and revised by Members. It reflects the level of borrowing which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. It is the expected maximum borrowing need with some headroom for unexpected movements. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003.

	2023/24 Original Estimate £m	2023/24 Current Position £m	2023/24 Revised Estimate £m
Authorised limit for External Debt	405.770	405.770	405.770

8. BORROWING

8.1 The Council's forecast Capital Financing Requirement (CFR) for 2023/24 is £182.081m. The CFR denotes the Council's underlying need to borrow for capital purposes. If the CFR is positive the Council may borrow from the PWLB or the market (external borrowing) or from internal balances on a temporary basis (internal borrowing). The balance of external and internal borrowing is generally driven by market conditions. The Council has forecast borrowings of £190.412m and has utilised £21.664m of cashflow funds in lieu of borrowing. This is a prudent and cost-effective approach in the current economic climate but will require ongoing monitoring in the event that upside risk to gilt yields prevails.

8.2 Due to the overall financial position and the underlying need to borrow for capital purposes (the CFR), new external borrowing of £18m was undertaken (of which £9m to support new capital expenditure and £9m for refinancing purposes). The Council arranged and received PWLB loans totalling £41.425m in relation to the St Georges Shopping Centre transaction referenced in Section 6 on 16 October 2023. A further £51.035m arranged but not yet drawn (of which £14.576m to support new capital expenditure and £36.459m for refinancing purposes). The capital programme is being kept under regular review because of inflationary pressures, shortages of materials and labour. Our borrowing strategy will, therefore, also be regularly reviewed and then revised, if necessary, to achieve optimum value and risk exposure in the long-term.

8.3 It is anticipated that further borrowing will be undertaken during this financial year.

8.4 Gilt yields and PWLB certainty rates were on a generally rising trend throughout the first half of 2023/24. At the beginning of April, the 5-year rate was the cheapest part of the curve and touched 4.14% whilst the 25-year rate was relatively expensive at 4.58%.

8.5 July saw short-dated rates peak at their most expensive. The 1-year rate spiked to 6.36% and the 5-year rate to 5.93%. Although, in due course, short-dated rate expectations fell, the medium dates shifted higher through August and the 10-

year rate pushed higher to 5.51% and the 25-year rate to 5.73%. The 50-year rate was 4.27% on 5th April but rose to 5.45% on 28th September.

8.6 Link forecast rates to fall back over the next two to three years as inflation dampens. The CPI measure of inflation is expected to fall below 2% in the second half of 2024, and the forecast 50-year rates to stand at 3.90% by the end of September 2025. However, there is considerable gilt issuance to be digested by the market over the next couple of years, as a minimum, so there is a high degree of uncertainty as to whether rates will fall that far.

9. DEBT RESCHEDULING

9.1 Debt rescheduling opportunities have increased over the past six months and will be considered if giving rise to long-term savings. However, no debt rescheduling has therefore been undertaken to date in the current financial year.

10. COMPLIANCE WITH TREASURY AND PRUDENTIAL LIMITS

10.1 It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. During the half year ended 30 September 2023, the Council has operated within the treasury and prudential indicators set out in the Council's Treasury Management Strategy Statement for 2023/24. The Director Corporate Services reports that no difficulties are envisaged for the current or future years in complying with these indicators with the exception of the Council's gross debt position compared to the CFR as referenced in para 7.9.

10.2 All treasury management operations have also been conducted in full compliance with the Council's Treasury Management Practices.

11. ANNUAL INVESTMENT STRATEGY

11.1 The Treasury Management Strategy Statement (TMSS) for 2023/24, which includes the Annual Investment Strategy, was approved by the Council on 21 February 2023. In accordance with the CIPFA Treasury Management Code, it is the Council's priority to ensure

- security of capital
- liquidity, and
- yield

11.2 The Council will aim to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity and with Council's risk appetite. In the current economic climate it is considered appropriate to keep investments short term to cover cash flow needs, but also to see out value available in periods up to 12 months with high credit rated financial institutions, using the Link suggested creditworthiness approach, including a minimum sovereign credit rating and Credit Default Swap (CDS) overlay information.

11.3 **Creditworthiness** – Following the Government's fiscal event on 23 September 2022, both S&P and Fitch have placed the UK sovereign debt rating on Negative Outlook reflecting a downside bias to the current ratings in light of expectations of weaker finances and the economic outlook. Nothing further has evolved in the first half of 2023/24.

11.4 **Investment Counterparty Criteria –** The current investment counterparty criteria selection approved in the TMSS is meeting the requirement of the treasury management function.

11.5 **CDS Prices –** It is noted that sentiment in the current economic climate can easily shift, so it remains important to undertake continual monitoring of all aspects of risk and return in the current circumstances.

11.6 **Investment Balances –** The average levels of funds available for investment purposes during the first half of the year to 30 September 2023 was £30.702m. These funds are available on a temporary basis, and the level of funds available was mainly dependent on the timing of precept payments, receipt of grants and progress on the capital programme. The Council also holds £20m core cash balances for investment purposes (ie funds available for more than one year).

11.7 Appendix 1 provides full list of investments held as at 30 September 2023.

11.8 **Investment Performance on Internal Investments**

Period	Average SONIA benchmark	Council Performance	Investment Income Forecast
April - Sept	4.74%	4.68%	£1,488,830

11.9 As illustrated, the Council underperformed the benchmark by 6 bps on its internally managed investments. As fixed term investments have matured, the money has been placed in money market funds whilst the Council negotiated its exit from the legal arrangement with Aviva Investors. This was to ensure that the Council had the flexibility to secure the most cost-effective ongoing financial arrangements. Following the completion of the deal, the team will be assessing the Council's liquidity requirements for the remainder of the financial year and consider the available investment options.

11.10 **Investment Returns –** The Council's budgeted investment return for both internally and externally managed investments for 2022/23 is £832k. A favourable variance of £375k is included with the Quarter 2 Budget Monitoring Report, which reflects the impact of rising interest rates.

11.11 **PROPERTY FUNDS AND MULTI ASSET FUNDS**

11.12 In the 2016/17, £10m was placed in three Externally Managed Property Funds. In 2017/18, a further £10m was placed in three Multi Asset Funds.

11.13 The table shows the Net Asset Value (NAV) for each of the Property Funds and Multi Asset Funds as at end of September compared to the Purchase Price, along with the average gross return on investment to date.

	Purchase Price	Sept NAV	% Change NAV	Return on Investment
Property Funds				
CCLA	£1,873,530	£1,805,370	-3.64%	-3.59%
Lothbury	£4,949,650	£4,281,240	-13.50%	-10.47%

Hermes	£2,883,820	£3,061,050	6.15%	9.99%
Multi Asset Funds				
JP Morgan	£5,000,000	£4,231,100	-15.38%	-15.34%
Jupiter	£3,000,000	£2,425,320	-19.16%	-19.13%
Aberdeen	£2,000,000	£1,658,980	-17.05%	-17.01%
Total	**£19,707,000**	**£17,563,060**		

Note – The average gross return is based on the 12 months to 30 September.

11.14 **Property Funds** - The % change in capital values above are based on movement from the original investment in 2016. Since 2016 the capital values have fluctuated in response to domestic, and global events. Capital values peaked in June 2022 as asset prices increased significantly but they have fallen in recent months given current economic uncertainties.

11.15 The Return on investment (ROI) for both CCLA and Lothbury is currently negative, due to the fall in in the capital values. Only Hermes is showing a positive ROI which is due to the September NAV being higher than the value when the investment was initial made.

11.16 Despite the falling capital values of the funds, the dividend returns have been maintained and as at 30 September the annual return was 4.31%.

11.17 **Lothbury Property Fund –** The Council initially invested just under £5m in the fund in July 2016. Dividend income totalling £1,041,540 has been paid to the Council (net of fees) since the initial investment was made and the capital valuation has gone up as well as down during the investment period. At its peak the capital value was £5,912,900 (June 2022) but it had fallen to £4,421,000 by May 2023.

11.18 By early June 2023, Lothbury had received redemption requests from its investors totalling almost £700m. All property funds have seen an increase in redemption requests given the current economic position but the level of redemption requests for Lothbury was a significant proportion of its total fund size (£1.086bn as at 31 March 2023), primarily due to pension funds wishing to exit the fund.

11.19 Given the scale of redemption requests, Lothbury notified all investors that it was suspending redemptions in the fund for a period of 12 months. This is common practice as it allows for the fund to manage the sale of assets effectively to repay investors wishing to exit the fund whilst protecting remaining investors from assets being sold quickly and below market value. Given the level of redemptions the Council needed to determine whether it too wanted to submit a redemption request in order to protect its position. After carefully considering the options and following consultation with Link, the Council submitted a redemption request to Lothbury on 13 June 2023.

11.20 Lothbury commenced with an asset plan sale and notified all investors that it was looking to restructure the fund and presented a proposal to continue as a smaller refocused fund. Investors were asked to consider the proposal and consider if they would withdraw redemption requests.

11.21 An Investor meeting was held on 14 September at which it became apparent that there was very little appetite from investors for a smaller restructured fund. However, Lothbury were tasked with exploring the options of merging with another fund. This is currently being explored by Lothbury but in the meantime the Council's redemption request continues to be in place.

11.22 On 17 October, the Council received notification from Lothbury that, if no other option has been identified for the continuation of the fund by 31 December 2023, the fund will terminate. The outcome is now out of the Council's hands. If the fund terminates, all investors are treated equally and will receive repayments as and when assets are sold. There is a target to sell all assets by the end of 2024, but it is ultimately dependent upon market conditions. Distributions will continue to be made on the remaining assets until such time as all assets are sold.

11.23 Officers are closely monitoring capital values and remain in regular contact with the Property Fund Managers of CCLA and Hermes, to ensure they are aware of the latest developments and how the funds are positioned in the current economic conditions.

11.24 **Multi Asset Funds** - The effect of the current economic pressures has been much more obvious on the Multi Asset funds, as can clearly be seen in the table above.

11.25 The fund capital values peeked in December 2021 but have since fallen. Markets fell initially following the invasion of Ukraine but have continued to fall in the wake of the current economic pressures. Dividend returns for two of the funds have held up reasonably well, albeit slightly below the pre-pandemic returns. However, the dividend return for Jupiter has been much harder hit, which is in part due to a change in direction of the fund. As with the Property Funds, officers are closely monitoring capital values and remain in regular contact with Fund Managers, to ensure they are aware of the latest developments.

11.26 Given the fall in capital values the ROI is currently negative for all three funds, however as at 30 September, the dividend return across all three funds is 3.39%.

11.27 It must be remembered that investment in Property Funds and Multi Asset Funds need to be viewed as a long-term investment as capital values can go up as well as down and that past performance is not a guarantee of future returns.

11.28 This is particularly relevant following the introduction of International Financial Reporting Standard 9 (IFRS9) which came into effect from 1 April 2018. A statutory override was introduced for a five-year period which runs till 31 March 2023. Following a consultation carried out by Government, it was announced that the statutory override would be grant a temporary extension to extend the override for a further two years to 31 March 2025.

12. Environmental, Social and Governance (ESG) Investments

12.1 When placing an investment, the Council's investment priorities are security, liquidity and yield and therefore it does not have a set of ESG standards to screen potential internally managed investments at this time. However, these factors are extremely important to the Council and opportunities will be explored as and when they arise.

12.2 However, ESG factors are an important consideration for the Council's external fund managers who administer both the Property Funds and Multi Asset Funds and therefore a significant proportion of the Council's investment portfolio is managed with these considerations in mind. Whilst we cannot stipulate what is and is not acceptable for these Funds to consider, Officers do discuss and receive briefings from Fund Managers as to the ESG credentials of the funds on a regular basis.

13. OTHER

13.1 In February 2015 the Authority became a shareholder in the Municipal Bonds Agency (MBA), with an investment of £20,000. The MBA was established by the Local Government Association (LGA) in the belief that it would provide councils with the opportunity to raise funds at significantly lower rates that those offered by the Public Works Loan Board (PWLB).

13.2 The MBA is now issuing bonds and officers will consider the appropriateness of any borrowing offer when the need to borrow arises.

14. APPENDICIES

14.1 Appendix 1 provides full list of investments held as at 30 September 2023.

15. BACKGROUND DOCUMENTS

15.1 There are no background documents

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Secondary Implications	
Risk Assessment	The risks associated with Treasury Management and capital expenditure are detailed within this report.
Data Protection Impact Assessment	*A data protection impact assessment (DPIA) should be carried out at the start of any major project involving the use of personal data or if you are making a significant change to an existing process.*
	a. Does the project/change being recommended through this paper involve the processing of personal data or special category data or criminal offence data? A definition of each type of data can be found on the Information Commissioner's Office website via the above links. No
	b. If yes to question a, have you completed and attached a DPIA including Data Protection Officer advice? N/A
	c. If no to question b, please seek advice from your nominated DPIA assessor or the Information Governance Team at gdpr@medway.gov.uk. N/A
Equality Impact Assessment	a. Does the decision being made or recommended through this paper have potential to cause adverse impact or discriminate against different groups in the community? If yes, please explain answer. No
	b. Does the decision being made or recommended through this paper make a positive contribution to promoting equality? If yes, please explain answer. No
	In submitting this report, the Chief Officer doing so is confirming that they have given due regard to the equality impacts of the decision being considered, as noted in the table above
Crime and Disorder	Treasury Management activities are carried out in accordance with the Treasury Management Strategy and Annual Investment Strategy which minimises the risk of criminal activities. The arrangements to ensure appropriate governance around capital expenditure are set out in the Capital Strategy.
Digital and website implications	N/A
Safeguarding children and vulnerable adults	N/A