Report No
FSD22037

London Borough of Bromley

PART 1 - PUBLIC

Decision Maker:	**Resources, Commissioning and Contracts Management Portfolio Holder**
Date:	**For pre-decision scrutiny by Executive, Resources and Contracts PDS Committee on 22 June 2022 and to be reported to Council on 18 July 2022**
Decision Type:	Non-Urgent Executive Non-Key
Title:	**TREASURY MANAGEMENT - ANNUAL REPORT 2021/22**
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Ward:	All Wards

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1. Reason for report

1.1. This report summarises treasury management activity during the fourth quarter and includes the Treasury Management Annual Report for 2021/22, which is required to be reported to Full Council. The report ensures that the Council is implementing best practice in accordance with the CIPFA Code of Practice for Treasury Management.

1.2. Investments as at 31st March 2022 totalled £377.7m and there was no external borrowing. For information and comparison, the balance of investments stood at £442.9m as at 31st December 2021 and £380.1m as at 31st March 2021.

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2. RECOMMENDATION(S)

2.1. The Resources, Commissioning and Contracts Management Portfolio Holder and Council are requested to:

(a) Note the Treasury Management Annual Report for 2021/22;

(b) Approve the actual prudential indicators within the report

(c) Note the publication of the revised Treasury Management and Prudential Codes, with formal adoption required in 2023/24

Impact on Vulnerable Adults and Children

1. Summary of Impact: None

Corporate Policy

1. Policy Status: Existing policy. To maintain appropriate levels of risk, particularly security and liquidity, whilst seeking to achieve the highest rate of return on investments.

2. BBB Priority: Excellent Council .

Financial

1. Cost of proposal: N/A

2. Ongoing costs: N/A

3. Budget head/performance centre: Interest on balances

4. Total current budget for this head: Provisional net interest earnings of £4,202k achieved against a budget of £3,591k for 2021/22 (surplus of £611k). Budget for 2022/23 is £2,841k.

5. Source of funding: Net investment income

Personnel

1. Number of staff (current and additional): 0.25 fte

2. If from existing staff resources, number of staff hours: 9 hours per week

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Legal

1. Legal Requirement: Non-statutory - Government guidance.

2. Call-in: Call-in is applicable

Procurement

1. Summary of Procurement Implications: N/A

Customer Impact

1. Estimated number of users/beneficiaries (current and projected): N/A

Ward Councillor Views

1. Have Ward Councillors been asked for comments? N/A

2. Summary of Ward Councillors comments: N/A

3. COMMENTARY

3.1 Under the requirements of the CIPFA Code of Practice on Treasury Management, the Council is required, as a minimum, to approve an annual treasury strategy in advance of the year, a mid-year review report and an annual report following the year comparing actual activity to the strategy. In practice, the Director of Finance has reported quarterly on treasury management activity for many years, as well as reporting the annual strategy before the year and the annual report after the year-end. This report includes details of investment performance in the final quarter of 2021/22 and the annual report for the whole of the 2021/22 financial year.

3.2 The 2021/22 Annual Treasury Strategy, including the Minimum Revenue Provision (MRP) policy statement and prudential indicators, was originally approved by Council in March 2021.

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

3.4 The Council has monies available for Treasury Management investment as a result of the following:

- Positive cash flow;
- Receipts (mainly from Government) received in advance of payments being made;
- Capital receipts not yet utilised to fund capital expenditure;
- Provisions made in the accounts for liabilities e.g. provision for outstanding legal cases which have not yet materialised;
- General and earmarked reserves retained by the Council.

3.5 Some of the monies identified above are short term and investment of these needs to be highly 'liquid', particularly if it relates to a positive cash flow position which can change in the future. Future monies available for Treasury Management investment will depend on the budget position of the Council and whether the Council will need to substantially run-down capital receipts and reserves. Against a backdrop of unprecedented cuts in Government funding, which will require the Council to make revenue savings to balance the budget in future years, there is a likelihood that such actions may be required in the medium term which will reduce the monies available for investment.

3.6 The Council has also identified an alternative investment strategy relating to property investment. To date, this has resulted in actual and planned acquisitions which generated £4.6m in 2016/17, £5.6m in 2017/18, £5.5m in 2018/19, £5.4m in 2019/20, £5.3m in 2020/21, £5.2m in 2021/22 and £5.4m in 2022/23. This is based on a longer-term investment timeframe of at least 3 to 5 years and ensures that the monies available can attract higher yields over the longer term.

3.7 A combination of lower risk investment relating to Treasury Management and a separate investment strategy in the form of property acquisitions (generating higher yields and risks) provides a balanced investment strategy. Any future investment decisions will also need to consider the likelihood that interest rates may continue to rise. The available resources for the medium term, given the ongoing reductions in Government funding, will need to be regularly reviewed.

Treasury Performance in the quarter ended 31st March 2022

3.8 The Council's healthy cashflow position continues and, other than some short-term borrowing at the end of 2015/16, no borrowing has been required for a number of years. The following table sets out details of investment activity during the fourth quarter and entire financial year:

	Qtr Ended 31/03/22		2022/23 Full Year	
	Deposits	Ave Rate	Deposits	Ave Rate
	£m	%	£m	%
Balance of "core" investments b/f	270.00	0.60	265.00	0.97
New investments made in period	30.00	0.85	225.00	0.40
Investments redeemed in period	-40.00	0.62	-230.00	0.72
"Core" investments at end of period	260.00	0.62	260.00	0.62
Money Market Funds	4.00	0.24	4.00	0.06
CCLA Property Fund*	40.00	24.57	40.00	21.12
Multi-Asset Income Funds*	40.00	-17.36	40.00	-0.87
Schroders Diversified Growth Fund	20.00	-17.39	20.00	-0.19
Project Beckenham Loan	3.75	6.00	3.75	6.00
Sovereign Bonds	10.00	1.84	10.00	1.84
"Alternative" investments at end of period	117.75	-0.15	117.75	7.19
Total Investments at end of Period	**377.75**	0.38	**377.75**	2.67

3.9 Details of the outstanding investments at 31st March 2022 are shown in maturity date order in Appendix B and by individual counterparty in Appendix C. The return on the new "core" investments placed during the fourth quarter of 2021/22 was 0.85% (0.48% during the third quarter).

3.10 Reports to previous meetings have highlighted the fact that options with regards to the reinvestment of maturing deposits have become seriously limited in recent years following bank credit rating downgrades and general low interest rate environment. Changes to lending limits and eligibility criteria, as well as the introduction of pooled funds and housing associations have alleviated this to some extent. More recently, increases in the Bank of England base rate have begun to feed through into improved lending rates with counterparties.

3.11 The chart in Appendix A shows total investments at quarter-end dates back to 1st April 2004 and shows how available funds have increased steadily over the years. This has been a significant contributor to the over-achievement of investment income against budgeted income in recent years.

Interest Rate Forecast (provided by Link Asset Services)

3.12 The current Bank of England base rate is 1%, following an increase at the May meeting of the Monetary Policy Committee. The market believes that further rises will follow, especially in the light of persistent inflationary pressures in the economy. Link's current interest rate view is shown in the table below.

Link Group Interest Rate View												
	Now	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24
Bank Rate	0.75%	1.00%	1.00%	1.25%	1.25%	1.25%	1.25%	1.25%	1.25%	1.25%	1.25%	1.25%
3 month ave. earnings	-	0.80%	1.00%	1.00%	1.20%	1.20%	1.20%	1.20%	1.20%	1.20%	1.20%	1.20%
6 month ave. earnings	-	1.00%	1.10%	1.20%	1.30%	1.30%	1.30%	1.30%	1.30%	1.30%	1.30%	1.30%
12 month ave. earnings	-	1.40%	1.50%	1.60%	1.70%	1.70%	1.60%	1.60%	1.50%	1.40%	1.40%	1.40%

Money Market Funds

3.13 The Council currently has 6 AAA-rated Money Market Fund accounts, with Federated Prime Rate, Aberdeen Standard (formerly known as Ignis), Insight, Blackrock, Fidelity and Legal & General, all of which have a maximum investment limit of £15m. In common with market rates for fixed-term investments, interest rates on money market funds have fallen considerably in recent years, though they have recently started to climb. The Funds currently offer rates in the range of 0.82% to 0.94%.

3.14 The total balance held in Money Market Funds has varied during the year to date moving from £23m as at 31st March 2021 to £35m as at 30th September 2021 to £60m as at 31st December 2021 and £4m at 31st March 2022. The Money Market Funds currently offer the lowest interest of all eligible investment vehicles with the exception of the Government Debt Management Account Deposit Facility; however, they are the most liquid, with funds able to be redeemed up until midday for same day settlement.

3.15 Daily balances in the Money Market Funds will vary considerably and have been higher than usual during 2021/22 owing to the receipt of Covid related grant funding by the Council. Additionally, balances tend to be higher during February and March to provide a cashflow buffer when the Council's income from Council Tax and Business Rates is significantly lower than the rest of the year. Occasionally, these balances are also inflated to ensure that the Council has sufficient liquidity to cover any 'non-standard' expenditure such as investment property purchases.

Housing Associations

3.16 Deposit with Housing Associations have recently attracted favourable rates and most recently the Council's Treasury Management Strategy Statement was amended to increase the overall limit for investments with Housing Associations to £80m. Current investments in Housing Associations total £35m, with rates varying from 0.6% to 2.15%.

Loan to Project Beckenham

3.17 On 26th June 2017 Council approved the inclusion in the strategy of a secured loan to Project Beckenham relating to the provision of temporary accommodation for the homeless that had previously been agreed to be advanced from the Investment Fund. A loan of £2.3m was made in June 2017, at a rate of 6%, although that may increase to 7.5% if the loan to value ratio exceeds a specified value. As at 31st March 2021, the loan balance stood £2.1m and six fund advances totalling £1.65m have been made during 2021/22, and the loan balance as at 31st March 2022 was £3.7m.

Sovereign Bonds

3.18 During November 2021, it was agreed that the Council's Treasury Management Strategy be amended to allow investment in sterling denominated Sovereign Bonds, subject to a maximum duration of 3 years and an exposure limit of £25m. On 30th November 2021, an investment of £10m was made for two years at a rate of 1.84%.

Pooled Investment Schemes

3.19 In September 2013, the Portfolio Holder and subsequently Council approved the inclusion of collective (pooled) investment schemes as eligible investment vehicles in the Council's Investment Strategy with an overall limit of £25m and a maximum duration of 5 years. The limit was subsequently increased to £40m by Council in October 2015, £80m in June 2017 and £100m in December 2017. Such investments would require the approval of the Director of Finance in consultation with the Resources Portfolio Holder.

IFRS 9 and the Statutory Override

3.20 Until March 2018, accounting rules required that the change in capital value of these investments be held in the Available for Sale Financial Assets Reserve, and only recognised in revenue on the sale of the investment. In year projections for interest on balances therefore only reflected the dividends from these investments.

3.21 However, from 2018/19 onwards, local authorities have been required to account for financial instruments in accordance with IFRS 9. This required that changes in the capital value of pooled fund investments are recognised in revenue in-year. Subsequently, MHCLG (now DLUHC) issued regulations providing a statutory override to reverse the impact of IFRS 9 on the Council's General Fund – this came into force in December 2018. The regulations are currently only applicable for a period of five years to March 2023, when it is intended for movements in value to be recognised in year. It would, however, be advantageous for Bromley and other Council's if the override was extended or made permanent.

3.22 Due to the regulations being time limited and the potentially volatile nature of these investments, interest/dividend earnings above 2.5% for 2018/19 and 2019/20 (£1,509k and £1,196k respectively) and above 2% for 2020/21 and 2021/22 (£1,520k and £1,676k respectively) – have been set aside in an Income Equalisation earmarked reserve. This will protect the Council against unexpected variations in the capital value of these investments and any timing issues arising from the expiry of the statutory override.

CCLA Property Fund

3.23 Following consultation between the Director of Finance and the Resources Portfolio Holder, an account was opened in January 2014 with the CCLA Local Authorities' Property Fund and an initial deposit of £5m was made, followed by further deposits of £5m in July 2014, £5m in March 2015, £10m in October 2015, £5m in October 2016 and £10m in October 2017. The investment in the CCLA Fund is viewed as a medium to long-term investment and dividends are paid quarterly. A breakdown of the dividends earned and capital growth is provided in the table below.

Annualised Net Return	**Dividend %**	**Capital Growth %**	**Total Return**
01/02/14 – 31/3/14	4.29	-29.64	-25.35
01/04/14 – 31/03/15	5.03	3.44	8.47
01/04/15 – 31/03/16	5.02	1.63	6.65
01/04/16 – 31/03/17	4.55	-2.50	2.05
01/04/17 – 31/03/18	4.59	2.41	7.00
01/04/18 – 31/03/19	4.46	1.57	6.03
01/04/19 – 31/03/20	4.45	-3.68	0.77
01/04/20 – 31/03/21	4.30	-0.71	3.59
01/04/21 – 31/03/22	3.82	17.29	21.12
Cumulative Return	4.42	2.51	6.94

3.24 The annualised fund return for the year to 31st March 2022 was capital growth of 17.29% and dividends paid of 3.82% resulting in a total return of 21.12%.

Multi-asset Income Fund

3.25 Following approval by Council in June 2017, the limit for pooled investment schemes was increased to £80m and an investment of £30m was made on 12th July 2017 in the Fidelity Multi-Asset Income Fund following the agreement of the Resources, Commissioning and Contracts Management Portfolio Holder. A subsequent investment of £10m was made on December 30th 2019. The annualised fund return for the year was capital reduction of 4.98% and dividends paid of 4.11% resulting in a total return of -0.87%.

Annualised Net Return	Dividend %	Capital Gain/Loss %	Total Return %
12/07/17 – 31/03/18	4.42	-6.27	-1.85
01/04/18 – 31/03/19	4.26	1.45	5.71
01/04/19 – 31/03/20	4.37	-11.81	-7.44
01/04/20 – 31/03/21	4.38	9.52	13.90
01/04/21 – 31/03/22	4.11	-4.98	-0.87
Cumulative Return	4.32	-0.65	3.67

Global Diversified Income Fund

3.26 During 2020/21 a new investment was made in the Global Diversified Income Fund managed by Schroders. The aim of this fund is to provide long-term capital growth and income of 3-5% per annum. An initial investment of £10m was made in March 2021, followed by a further £10m in April 2021. A breakdown of the dividends earned and capital growth is provided in the table below. The net fund return for the year was 0.02%.

Annualised Net Return	Dividend %	Capital Gain/Loss %	Total Return %
01/03/21 – 31/03/21	2.45	2.43	4.88
01/04/21 – 31/03/22	2.96	-3.15	-0.19
Cumulative return	2.94	-2.92	0.02

Property Acquisition Scheme (Meadowship Homes)

3.27 As agreed by the Executive during 2021, the Council will embark on a property acquisition scheme under a funding arrangement with Orchard & Shipman. This will involve the formation of an LLP which will be a joint venture between the Council and Orchard & Shipman. As part of this scheme, the Council will make a £20m loan (in tranches) for 50 years. Annual repayments will start from year 3 of 1.6% (£320k) per annum and increasing annually by CPI (collared at 0-4%), As the Effective Interest Rate on the loan is dependent on CPI, it is possible that this will be lower than the rate the Council might achieve through treasury management investments.

Actual prudential indicators for 2021/22

3.28 The old capital control system was replaced in April 2004 by a prudential system based largely on self-regulation by local authorities themselves. At the heart of the system is The Prudential Code for Capital Finance in Local Authorities, developed by CIPFA. The Code requires the Council to set a number of prudential indicators designed to monitor and control capital expenditure, financing and borrowing. The indicators for 2021/22 were approved by the Executive and the Council in February/March 2021. Appendix D sets out the actual performance in 2021/22 against those indicators.

Economic Background during 2021/22 (provided by Link Asset Services)

3.29 Further information on the economic background is included as Appendix E.

Revised Treasury Management and Prudential Codes

3.30 During December 2021 CIPFA published a revised Prudential Code (Prudential Code for Capital Finance in Local Authorities) and Treasury Management Code (Treasury Management in the Public Services Code of Practice and Cross-Sectoral Guidance Notes). It also stated that formal adoption is not required until the 2023/24 financial year. This Council is required to have regard to these codes of practice when it prepares the Treasury Management Strategy Statement and Annual Investment Strategy, and also related reports during the financial year, which are taken to Full Council for approval.

3.31 The revised codes will have the following implications:

- a requirement for the Council to adopt a new debt liability benchmark treasury indicator to support the financing risk management of the capital financing requirement
- clarify what CIPFA expects a local authority to borrow for and what they do not view as appropriate. This will include the requirement to set a proportionate approach to commercial and service capital investment
- address ESG issues within the Capital Strategy
- require implementation of a policy to review commercial property, with a view to divest where appropriate
- create new Investment Practices to manage risks associated with non-treasury investment (similar to the current Treasury Management Practices)
- ensure that any long-term treasury investment is supported by a business model
- a requirement to effectively manage liquidity and longer-term cash flow requirements
- amendment to TMP1 to address ESG policy within the treasury management risk framework
- amendment to the knowledge and skills register for individuals involved in the treasury management function - to be proportionate to the size and complexity of the treasury management conducted by each council
- a new requirement to clarify reporting requirements for service and commercial investment, (especially where supported by borrowing/leverage).

3.32 In addition, all investments and investment income must be attributed to one of the following three purposes:

(i) **Treasury Management.** Arising from the organisation's cash flows or treasury risk management activity, this type of investment represents balances which are only held until the cash is required for use. Treasury investments may also arise from other treasury risk management activity which seeks to prudently manage the risks, costs or income relating to existing or forecast debt or treasury investments.

(ii) **Service Delivery.** Investments held primarily and directly for the delivery of public services including housing, regeneration and local infrastructure. Returns on this category of investment which are funded by borrowing are permitted only in cases where the income is "either related to the financial viability of the project in question or otherwise incidental to the primary purpose".

(iii) **Commercial Return.** Investments held primarily for financial return with no treasury management or direct service provision purpose. Risks on such investments should be proportionate to a council's financial capacity – i.e., that 'plausible losses' could be absorbed in budgets or reserves without unmanageable detriment to local services. An authority must not borrow to invest primarily for financial return.

3.33 Members will be updated on how all these changes will impact our current approach and any changes required will be formally adopted within the 2023/24 Treasury Management Strategy.

Regulatory Framework, Risk and Performance .

3.34 The Council's treasury management activities are regulated by a variety of professional codes, statutes and guidance:

- The Local Government Act 2003 (the Act) which provides the powers to borrow and invest as well as providing controls and limits on this activity
- The Act permits the Secretary of State to set limits either on the Council or nationally on all local authorities restricting the amount of borrowing that may be undertaken (although no restrictions have been made to date)
- Statutory Instrument (SI) 3146 2003, as amended, develops the controls and powers within the Act
- The SI requires the Council to undertake any borrowing activity with regard to the CIPFA Prudential Code for Capital Finance in Local Authorities
- The SI also requires the Council to operate the overall treasury function with regard to the CIPFA Code of Practice for Treasury Management in the Public Services
- Under the Act, the MHCLG (now DLUHC) issued Investment Guidance to structure and regulate the Council's investment activities
- Under section 238(2) of the Local Government and Public Involvement in Health Act 2007, the Secretary of State has taken powers to issue guidance on accounting practices. Guidance on Minimum Revenue Provision was issued under this section on 8th November 2007.

3.35 The Council has complied with all of the above relevant statutory and regulatory requirements, which limit the levels of risk associated with its treasury management activities. In particular, its adoption and implementation of both the Prudential Code and the Code of Practice for Treasury Management means that its capital expenditure is prudent, affordable and sustainable and its treasury practices demonstrate a low-risk approach.

4. POLICY IMPLICATIONS

4.1 In line with government guidance, the Council's policy is to seek to achieve the highest rate of return on investments whilst maintaining appropriate levels of risk, particularly security and liquidity.

5. FINANCIAL IMPLICATIONS

5.1 The provisional outturn for net interest on investments in 2021/22 was £4,202k compared to the budget of £3,591k, mainly due to the continued high level of balances available for investment as well as the high level of interest earned on the pooled funds, housing association deposits and the Project Beckenham loan.

5.2 The draft budget for 2022/23 has been set at £2,841k. This reflects an expected reduction in balances available for investment as a result of the utilisation of capital receipts and grants/contributions as well as earmarked revenue reserves. Whilst the Bank of England base rate is expected to continue to rise and this has started to improve counterparty rates, the Council anticipates a lag before this translates into investment opportunities that will provide a sustainable return in excess of what is currently being achieved on the entire portfolio.

6. LEGAL IMPLICATIONS

6.1 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.

6.2 This report fulfils the requirements of the Chartered Institute of Public Finance & Accountancy's Treasury Management and Prudential Codes of Practice 2017 and the 2018 Statutory Guidance on Local Government Investments.

Non-Applicable Sections:	Impact on Vulnerable Adults and Children, Personnel, Legal and Procurement Implications
Background Documents: (Access via Contact Officer)	CIPFA Code of Practice on Treasury Management CIPFA Prudential Code for Capital Finance in Local Authorities CLG/ MHCLG/ DLUHC Guidance on Investments External advice from Link Asset Services