North East Derbyshire District Council

Audit and Corporate Governance Scrutiny Committee

11 May 2022

Scrutiny of Treasury Management Investments

Report of the Assistant Director – Finance & Resources (S151 Officer)

Classification: This report is public

Report By: Jayne Dethick – Assistant Director – Finance & Resources (S151 Officer)

Contact Officer: as above

PURPOSE/SUMMARY

To provide information to the Audit and Corporate Governance Scrutiny Committee on the current portfolio of cash investments along with alternative options for scrutiny.

RECOMMENDATIONS

1. That the Audit and Corporate Governance Scrutiny Committee consider the information and options presented in the report and make any recommendations that they believe to be appropriate to the Cabinet.

IMPLICATIONS

Finance and Risk **Yes** ✓ **No**

Contained within the report

On Behalf of the Section 151 Officer

Legal including Data Protection **Yes** **No**✓

None arising

On Behalf of the Solicitor to the Council

Staffing **Yes** **No** ✓

There are no staffing issues arising directly from this report.

On Behalf of the Head of Paid Service

DECISION INFORMATION

Is the decision a Key Decision? A Key Decision is an executive decision which has a significant impact on two or more District wards or which results in income or expenditure to the Council above the following thresholds: *BDC: Revenue - £75,000* ☐ *Capital - £150,000* ☐ *NEDDC: Revenue - £100,000* ☐ *Capital - £250,000* ☐ ☑ *Please indicate which threshold applies*	N/A
Is the decision subject to Call-In? (Only Key Decisions are subject to Call-In)	N/A
Has the relevant Portfolio Holder been informed	N/A
District Wards Affected	All
Links to Corporate Plan priorities or Policy Framework	All

REPORT DETAILS

1 Scrutiny of Treasury Management Investments

1.1 Following scrutiny of the Treasury Management monitoring report at its last meeting (Appendix 1), the Committee asked for an update on the Council's treasury management investments for scrutiny. The policy that governs how the Council can invest its cash is encompassed within the Treasury Management suite of strategies which is approved at Council each year. This suite comprises three strategies:

- The Treasury Management Strategy which provides the framework for managing the Council's cash flows, borrowing and investments for the period.

- The Capital Strategy which is intended to provide a high level, concise overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of the Council's services.

- The Investment Strategy which focuses on investments made for service purposes and commercial reasons, rather than those made for treasury management

The purpose of this review is to consider the Council’s cash investments so the main focus in this report will be on the Treasury Management Strategy.

1.2 The Treasury Management Strategy (Appendix 2) sets out the parameters for all borrowing and lending as well as listing all approved borrowing and investment sources. Prudential indicators aimed at monitoring risk are also included. All transactions are conducted in accordance with this strategy and the CIPFA Treasury Management Code of Practice.

1.3 Over recent years, investment options for local authorities have become much more tightly controlled by regulation and borrowing purely for yield is now prohibited by the PWLB. This ban relates to all of a local authority’s borrowing requirements not just that planned for the investment. The revised Prudential Code requires much more robust metrics to demonstrate that risk management of investments is in place and there is a requirement to demonstrate that investment risk is proportionate to financial capacity – in effect plausible losses should be capable of being absorbed in budgets or reserves without unmanageable detriment to services.

1.4 Knowing when to invest or indeed borrow can be a challenge especially during periods of economic volatility like we are currently experiencing. Interest rates have been at all-time lows for a number of years now affecting investor returns. There have been a number of small incremental increases over recent months and these are forecast to continue until the middle of 2023 (1.5% predicted high) then level out again.

1.5 Interest rate increases are largely to counteract rising inflation which is expected to continue to rise to a peak of 7.25% in the coming months, reflecting the increase in global prices. The contribution to inflation from higher energy prices is currently expected to decline to zero by the start of 2023 but the ongoing unrest in the Ukraine may impact on this. Goods price inflation is also expected to fall over the next 18 months and current economic forecasts are for inflation to fall back to target by the end of 2023 then drop below target during 2024.

1.6 The Council has diversified its investment portfolio over the past 18 months, moving away from very low interest bank deposits to money market funds which not only have a better yield but also remove the risk of “bail in”. These are still short term, liquid investments though with low yield so investing with other local authorities and registered providers for a longer duration (2-5 years) has been undertaken which has increased the yield a little.

1.7 The current return at 0.7% however is still lower than the national average across local authorities of 1.95%. This is because the Council’s investment portfolio is almost entirely made up of short dated, liquid funds, carrying little risk or volatility. A move to higher returns will require a willingness to accept moderately more risk and commit to longer term investments, even if this means external borrowing will need to be undertaken as a result. Building a portfolio that diversifies investments where higher return/volatility is combined with lower risk helps to balance the overall risk.

Consideration of Options

1.8 Having considered the Council's current position and the desire to consider options to increase yield through a moderate increase in risk/duration, our treasury management advisors have recommended a number of investment options to consider that would be best suited to our investment needs and that can be undertaken within our existing Treasury Management Policy.

1.9 Detailed below are a range of investment options that have a good track record of performance over the medium term (5+ years). It is important to recognise when monitoring performance of these funds that they may appear to be under performing in the early years of the investment, there may be times when return is lower than expected or even negative during their life.

Multi Asset Income Bonds

- Recommended investment duration 3 – 5 years
- Aims to provide income return over the medium term
- Minimum investment £1m
- Indicative return after 5 years – 2.8% -4%

Property Funds

- Recommended investment duration 5 years
- Aims to provide income return over the medium term
- Minimum investment £1m
- Indicative return after 5 years – 3.7% - 4.3%

Real Estate Investment Trusts (REIT's)

- Recommended investment duration 5 years
- Aims to provide income return over the medium term
- Minimum investment £1m
- Indicative return after 5 years – up to 5%

1.10 Using the working assumption that investing whilst minimising the need to borrow externally, provides a sum of £5m to be invested initially. Further investment could then be considered on an ongoing basis as part of the treasury management monitoring processes in place.

2 Reasons for Recommendation

2.1 The Council's treasury management investment portfolio is almost entirely made up of short dated, liquid funds, carrying little risk or volatility. A move to higher returns is therefore an aim. This will require a willingness to accept moderately more risk and commit to longer term investments. Building a portfolio that diversifies investments where higher return/volatility is combined with lower risk helps to balance the overall risk.

4 Alternative Options and Reasons for Rejection

4.1 To maintain the current low risk, low yield strategy.

DOCUMENT INFORMATION

Appendix No	Title
1 2	Treasury Management Monitoring Treasury Management Strategy
Background Papers (These are unpublished works which have been relied on to a material extent when preparing the report. They must be listed in the section below. If the report is going to Cabinet (NEDDC) or Executive (BDC) you must provide copies of the background papers)	
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