Summary Investment and Borrowing Position at 30 September 2022

Investment Sub Committee Friday, 4 November 2022

Report of: Chief Finance Officer (Section 151)

Purpose: For information

Publication status: Unrestricted

Wards affected: All

Executive summary:

This report updates the Investment Sub Committee on the Council's investment and borrowing position at 30th September 2022, provides an update on the Government's consultation regarding the IFRS 9 statutory override, and provides an update on the Council's projected cash balances and the strategy for the use of redeemed proceeds from Funding Circle loans, as discussed at the Investment Sub Committee meeting on the 17th June 2022.

This report supports the Council's priority of: Building a better Council/ Supporting economic recovery in Tandridge.

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Recommendation to Committee:

That the Sub Committee notes:

A. the Council's Investment and Borrowing position at 30th September 2022 as set out in Appendices A and B

B. the update on the future of the statutory override

C. the update on the Council's cash flow position and review of the use of redeemed proceeds from Funding Circle loans

D. the update on the Council's performance against its Prudential Indicators as set in the Capital, Investment and Treasury Management Strategy for 2022/23

Reason for recommendation:

This report will be reviewed by the Sub Committee, which provides an update on the Council's investment and borrowing position.

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1. Introduction and background

1.1 The Capital, Investment and Treasury Management Strategy for 2022/23 was reported to the Strategy and Resources Committee on 1st February 2022. This covered the borrowing and investment plans for the Council. As detailed in this strategy, part of the Treasury Management function is to ensure that the cashflow is adequately planned and surpluses are invested while allowing for cash to be available when needed. Additionally, the treasury management function ensures that the Council can meet its capital spending plans. This requires the management of longer-term cash which will involve the use of long or short-term loans, or cash flow surpluses.

1.2 Tandridge District Council's contract for expert Treasury Management Advice with Link Group came to an end on the 30th April 2022. The new contract, with Arlingclose Ltd began on 1st May 2022 and their comments on the management of the Council's cash flows are reflected in this report.

2. Summary Investment and Borrowing Position

2.1 A summary of the Council's investment and borrowing at 30th September 2022 is set out in Appendix A.

- Total long term financial investments (over 12 months) amount to £11.6m million. This represents a reduction in market value of £1.0m since the 31st March 2022, largely reflecting the volatile economic situation. The statutory override, as set out in section 3, prevents this fall in market value from impacting the revenue budget in the current financial year. A decision on the future of the override is expected imminently.

- Short term investments (less than 12 months) amount to £16.6 million.

- The Council also has £21.1 million in non-financial investments which is made up of capital loans to specific service providers and limited companies.

- The total amount of Public Works Loan Board (PWLB) loans at 30th September 2022 is £102.3 million. This is made up of £43.4 million General Fund loans and £58.9 million Housing Revenue Account loans.

3. Statutory Override Update

3.1 At its meeting on Friday 21st January 2022, Investment Sub Committee considered a report from officers and then-Treasury Management advisors, Link Group on the future of four long-term investments:

- CCLA Property Fund
- Schroeders Credit/Bond Fund
- UBS Multi Asset Fund
- CCLA Diversification Fund

3.2 The current regulatory environment means that the Council does not recognise annual gains and losses in the capital value of investments in the revenue budget, unless the investment is withdrawn. This is known as a statutory override, because it overrides usual accounting practice. The current override lasts until 31st March 2023. Government has not yet made a decision on whether to extend, amend or remove the override from that point.

3.3 The 17th June 2022 ISC report set out the potential implications of the removal or continuation of the override. A Government consultation was issued in August and officers responded on behalf of TDC in October. Officers expressed an opinion that the override should be made permanent as this represents the lowest risk to the revenue budget, and leaves options open to change the mix of the investment portfolio, should it be deemed appropriate.

3.4 The outcome of the consultation will determine a) the impact on the Council and b) actions to be taken by the Council as identified in the report to ISC on 17th June, repeated below for reference.

3.5 The Council's options in the two scenarios set out in the 17th June ISC report are as follows:

Scenario	Override continued	Override removed
Outline	General Fund continues to be insulated from gains and losses in fair value. The gain / loss on the asset would have a General Fund impact if the investment was withdrawn at greater than or lower than the initial investment.	General Fund is no longer insulated from gains and losses in fair value. The change in value at 31st March each year would be part of the Council's General Fund outturn against budget.

Scenario	Override continued	Override removed
Potential responses	• Maintain the current portfolio of investments if they still demonstrate strong in-year yield; or • Disinvest in current funds and then re-invest in funds that offer the strongest in-year yield but set aside surpluses into a reserve to manage volatility in funds that would be felt if the Council needed to disinvest from the asset; or • Reduce the investment portfolio in overall size.	• Maintain investment in the funds, and manage the year-to-year volatility through reserves; or • Disinvest in current funds and reinvest in funds that offer the best combination of asset value security and in-year yield; i.e. total return; or • Sell the investments and move into lower yielding deposits, causing a budget pressure; or • Sell the investments and move into higher risk alternatives where the override is not required; or • Reduce the investment portfolio in overall size
Preferred response	• **The portfolio of funds should be kept under review to maximise in-year yield whilst providing adequate long-term security of Council investments;** • An element of in-year yield could be credited to a reserve to guard against falls in value upon disinvestment – a target level of reserve for this purpose would be developed in consultation with Arlingclose	• When a decision is made by Government, funds currently below their market value should be withdrawn when their capital value recovers to at least the amount invested, or if it becomes clear that their value will not be recovered further; • Losses in these funds are partly mitigated by the gain in CCLA Property; • **Cash should then be reinvested in funds that offer the best total return (i.e. the combination of in-year yield and capital value)**

<table>
<tr><th>Scenario</th><th>Override continued</th><th>Override removed</th></tr>
<tr><td></td><td>• The appropriate overall value of investments will continued to be gauged against cash requirements and the differential in interest rates on new borrowing and investment return</td><td>• An element of in-year surpluses should be held in reserves to cover future volatility of funds – a target level of reserve for this purpose would be developed in consultation with Arlingclose

• The appropriate overall value of investments will continued to be gauged against cash requirements and the differential in interest rates on new borrowing and investment return</td></tr>
<tr><td>Risks</td><td>The continuation of the override may be time-limited, or the prevailing financial position of the Council may require disinvestment from funds, potentially at a loss. The statutory override does not protect the General Fund in the event of disinvestment.</td><td>In-year volatility in the market value of investments may impact the delivery of the General Fund Budget.</td></tr>
<tr><td>Mitigations</td><td colspan="2">Although the risks differ in timing, ultimately the General Fund would bear the risk of falls in the value of investments. The potential mitigations are the same in both scenarios.

An element of surpluses should be credited to a specific reserve in order to manage the risk that losses in investment values will ultimately be a General Fund impact (either each year if the override is discontinued or on disinvestment if it is not).

The reserve may require a level of up-front funding. It is proposed that this is achieved through either a) from in-year surpluses in investment income (if achievable) or;
b) a contribution from the General Fund at a level to be determined through the 2023/24 budget process and in consultation with Arlingclose.

Any losses could also be mitigated by recognising the gain from a stronger-performing investment.</td></tr>
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4. Update on cash flow strategy and Funding Circle loans

4.1 At its meeting on Friday 17th June 2022, Investment Sub Committee resolved that the use of redeemed proceeds from Funding Circle would be reviewed at this meeting in light of the Council's cash flow requirements.

4.2 The Council has updated its cash flow projections to 30th September 2023, and a detailed 12-month cash flow will be circulated to members of the Sub-Committee separately. The position is under continual refinement now the Council has adopted a more robust, software-based approach to forecasting. The Council's current recommended approach is to use cash balances to offset the need to borrow, and to invest in Money Market Funds.

4.3 The advice from Arlingclose is that using cash to avoid or delay the need to borrow to fund the capital programme is the best approach for the use of balances, including redeemed Funding Circle proceeds. This will remain the case whilst PWLB loan rates are in the region of 5%, as it represents a positive yield on the cash balances whilst avoiding any uncertainty or risk involved in investing without certainty on the statutory environment.

5 Update on the Council's Prudential Indicators

5.1 It is good practice to update the ISC on performance against the Council's prudential indicators, as set in advance of each financial year. This has not happened previously. Appendix C sets out the latest estimate for the indicators.

Key implications

6. Comments of the Chief Finance Officer

6.1 The forecast position at 30 September 2022 is for investment income for the year to be £197k more than budgeted. This is mainly due to the performance of the Council's investments in Money Market Funds, as generally funds have reacted to the increases in the Bank of England base rate. The forecast for General Fund and HRA loan interest payable is in accordance with budget. As the year progresses, a decision will be required on whether to release any surplus against the Council's overall outturn position, or to transfer an element to reserve to mitigate changes in the Council's investment values. This will be contingent on a decision from Government on the future of the override.

6.2 With all investments there are risks attached. The Council manages these risks by holding diversified investments and through seeking expert advice from its Treasury Management Advisors and through the Finance Joint Working Agreement with the Orbis Centre of Expertise. The Council will continue to monitor the value of its investments in context of the regulatory environment.

6.3 The Council's internal auditors have recently reviewed the new arrangements for treasury management, including the joint working arrangement with Surrey County Council and Orbis. The review concluded that the Council's arrangements for Treasury Management were 'reasonable', which is a marked improvement on the 'limited' assurance provided in 2020/21's audit. The improvement areas identified related to the following points which have subsequently been addressed:

- Training for Members on treasury management; an initial session of which has now been provided.
- The regular updates to ISC did not included updates on the Prudential Indicators; to commence from November 2022 onwards.
- A more regular reconciliation of treasury management to the financial system; which is now underway through the joint working agreement.

Officers will continue to strengthen the arrangements for treasury management, including ongoing refinements of its cash flow forecasts and the instigation of more regular training.

7. Comments of the Head of Legal Services

7.1 The Council's Treasury Management Strategy Statement follows the latest codes of practice and the DLUHC and CIPFA guidance.

7.2 The Council has borrowed and invested sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of financial risk are therefore central to the Council's prudent financial management.

8. Equality

8.1 The proposals within this report do not have the potential to disadvantage or discriminate against different groups with protected characteristics in the community.

9. Climate change

9.1 There are no significant environmental/sustainability implications associated with the report. It is however recognised that some Council investments may be in companies that are considered to have a detrimental impact on the climate, for example oil companies. The Council will need to consider its strategy in respect of this. A consultation is under way on similar issues in Surrey Pension Fund, which closes on 6th November 2022, and officers are considering the response with Members.

Appendices

Appendix A – Summary of Investments and Borrowing

Appendix B – Market Value of Long-Term Investments

Appendix C – Prudential Indicators – performance and updated estimates

Background papers

Investment Sub-Committee Papers 17th June 2022

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