Treasury Management and Investment Sub-Committee Agenda

22 June 2020 at 7pm

Remote Meeting

Membership

Councillor C.K. Davidson (Chair)

and Councillors

M.W. Bracken, D.J.R. Clark, P.H. Clark, J. Galley, A.B. Sosin and R.T. Whitehead

Local people are welcome to attend this meeting, where your elected Councillors take decisions affecting YOU and your City. There will also be an opportunity to ask your Councillors questions or make a statement. These have to be submitted in advance and details are on the agenda page. If you would like to find out more, please telephone Daniel Bird in the Democracy Team on Chelmsford (01245) 606523 email Daniel.bird@chelmsford.gov.uk

Treasury Management and Investment Sub Committee

22 June 2020

AGENDA

1. Apologies for Absence and substitutions

2. Minutes

To consider the minutes of the meeting held on 16 December 2019

3. Declaration of Interests

All Members are reminded that they must disclose any interests they know they have in items of business on the meeting's agenda and that they must do so at this point on the agenda or as soon as they become aware of the interest. If the interest is a Disclosable Pecuniary Interest they are also obliged to notify the Monitoring Officer within 28 days of the meeting.

4. Public Question Time

Any member of the public may ask a question or make a statement at this point in the meeting. Each person has two minutes and a maximum of 15 minutes is allotted to public questions/statements, which must be about matters for which the Committee is responsible.

The Chair may disallow a question if it is offensive, substantially the same as another question or requires disclosure of exempt or confidential information. If the question cannot be answered at the meeting a written response will be provided after the meeting.

Any member of the public who wishes to submit a question or statement to this meeting should email it to committees@chelmsford.gov.uk 24 hours before the start time of the meeting. All valid questions and statements will be published with the agenda on the website at least six hours before the start time and will be responded to at the meeting. Those who have submitted a valid question or statement will be entitled to put it in person at the meeting, provided they have indicated that they wish to do so and have submitted an email address to which an invitation to join the meeting and participate in it can be sent.

5. Treasury Management Outturn Report 2019/20

6. Non-Treasury Investment Strategy – Monitoring and Strategy Development

7. Urgent Business

To consider any other matter which, in the opinion of the Chair, should be considered by reason of special circumstances (to be specified) as a matter of urgency.

MINUTES

of the

TREASURY MANAGEMENT SUB-COMMITTEE

held on 16 December 2019 at 7pm

Present:

Councillor C.K. Davidson (Chair), Councillors M.W. Bracken, D.J.R. Clark, P.H. Clark and M.D. Watson

1. **Apologies for Absence and Substitutions**

   Apologies for absence were received from Councillor Raven. Councillor Watson was his substitute.

2. **Minutes**

   The minutes of the meeting held on 21 October 2019 were confirmed as a correct record and signed by the Chair.

3. **Declaration of Interests**

   All Members were reminded to declare any Disclosable Pecuniary interests or other registerable interests where appropriate in any items of business on the meeting's agenda. None were made.

4. **Public Question Time**

   There were no questions from members of the public.

5. **Treasury Management Strategy 2020/21**

   The Sub-Committee considered a draft report to the Cabinet on 28th January 2020 regarding the proposed Treasury Management Strategy for 2020/21. Members were asked to review the draft report and recommend a Treasury Management Strategy for 2020/21 to Cabinet on 28th January 2020 and then Full Council on 26th February 2020.

   The Sub-Committee were informed that the proposed strategy did not include any major changes and followed similar limits to the current one. Members were informed that the strategy would allow the Director of Finance to manage investments and borrowing with the flexibility required. The Sub-Committee were directed to page 10 which summarised that if borrowing was undertaken there would be a smaller sum available to invest. It was noted that this was difficult to forecast at the moment and would become clearer with the new capital programme. Members were informed that the issue of internal borrowing was covered in more detail in this year's strategy.

   In response to questions from the Sub-Committee, officers confirmed that;

   - There was a £10m limit on investments with other local authorities but any decisions were taken on a case by case basis, using local knowledge and advice from Arlingclose.

- Initial income projections had been cautious, therefore even with less money potentially available to invest, the projected forecasts were still positive.
- Further information on the possibility of investing in multi asset funds would be provided after the meeting to Cllr Watson.
- Any funds not invested were kept short and placed in the best money market fund available.
- The rate applied to any internal borrowing was 0.9%.

Councillor P. Clark raised a concern that yield was being prioritised over security by continuing to invest in the CCLA property fund. He raised concerns that whilst the fund had been successful that might not always be the case, and that the Council should realise their profits rather than continue with the investment. Therefore, Cllr P. Clark did not agree with the conclusion detailed at paragraph 4.1 of the report. In response officers stated that it needed to be read in conjunction with paragraph 4.2 which clarified that the council's methods could not remove all risk of losses but balanced the need to make an appropriate return within reasonable risk parameters.

Councillor P. Clark put forward a proposal that the strategy be amended, to be clear that there would be no further investment in the property sector outside of Chelmsford. He felt that the Council should be looking at more diverse investments rather than property which was already well invested in. Officers clarified that direct investment in individual commercial properties (whether inside or outside of Chelmsford) was not covered within the Treasury Management Strategy but would be included in the Capital and Investment Strategy due to be considered at Cabinet on 28th January 2020 and Council on 26th February 2020. The Sub-Committee agreed that the strategy be amended to clarify that no further investments would be made in property funds. It was also noted that the £8m limit was to allow headroom in case of an increase in values rather than additional investment.

Members of the Sub-Committee also clarified that the three objectives were security of capital, liquidity and yield. It was stated that the strategy and future work would look to achieve an appropriate balance across the three, with most weight to security and then liquidity. The Sub-Committee also made it clear that their role was to set a strategy, but that decisions on induvial investments were still for officers to make in line with the strategy. The majority of the Sub-Committee confirmed they were happy with the proposed strategy, but Cllr P. Clark asked for his objections to be noted.

RESOLVED that;

1. the draft Treasury Management Strategy for 2020/21, set out in the report before the Sub-Committee, be endorsed and recommended to Cabinet and Council for approval with the following amendments to be added to the draft by officers;
2. no further investments to take place in property funds and;
3. at paragraph 1.5 it be made clear that the priorities are balanced with the security of capital being first.

(7pm to 7.54pm)

6. **<u>Urgent Business</u>**

There were no matters of urgent business brought before the Sub-Committee.

The meeting closed at 7.54pm.

Chair

Chelmsford City Council Treasury Management and Investment Sub-Committee

22 June 2020

Treasury Management Outturn Report 2019/20

Report by:
Director of Financial Services

Officer Contact:
[Phil Reeves, Accountancy Services Manager, phil.reeves@chelmsford.gov.uk, 01245 606562]

Purpose

Under statute and the CIPFA Code of Practice on Treasury Management ("the Code"), Members are required to receive a report on the Treasury Management activities that took place in 2019/20.

Recommendations

Recommend the Treasury Management Outturn Report 2019/20 to Cabinet or amend as appropriate.

1. Introduction

1.1. The CIPFA Code of Practice for treasury management sets out the requirements for oversight by the Council of its treasury management operations. As part of the Code, the Council is required to receive an annual report on the performance of the treasury management function which highlights the effects of decisions taken and the circumstances of any non-compliance with the Code and the Council's Treasury Management Strategy.

2. Background

2.1. The Council can expect to have cash to invest arising from its revenue and capital balances, and collection of Council Tax. This cash can be usefully invested to produce a return to help support services and Council Tax. The activities around the management of this cash are known as 'Treasury Management'.

2.2. Treasury Management is defined by the Chartered Institute of Public Finance and Accountancy (CIPFA) as:

"The management of the local authority's 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"

2.3. CIPFA produce a framework for managing treasury activities, called a 'Code'. Councils are legally required to have regard to this Code and members of CIPFA are expected to comply with its requirements. This report fulfils the Authority's legal obligation under the Local Government Act 2003 to have regard to both the CIPFA Code and the MHCLG Guidance.

2.4. The Council's investment priorities as required by Government regulations are in order of priority:
(a) The security of Capital
(b) The liquidity of its investments; and
When these are satisfied
(c) Yield

The regulations and CIPFA both advise that absolute certainty of security of capital and liquidity does not have to be achieved before seeking yield from investments. An appropriate balance of all three should be sought and that balance is determined by the Council in its Treasury Strategy.

2.5. The operation of Treasury Management is not without risk and the Council could suffer losses if one of its counterparties had financial difficulties.

2.6. The Council formally reviews its investment holdings in the following ways:

- Treasury Management Strategy report in February
- Treasury Outturn report in July
- A half year update in November

- Treasury Management sub-committee to monitor Treasury Activity during the financial year.

The review of the year's activities is set out in the following appendices:

Appendix A – Economic Environment Update

Appendix B – Borrowing and Actual Investment Activity compared to the Approved 2019/20 Strategy

Appendix C – Treasury Performance Indicators for 2019/20

3. Summary of Review

3.1. During the financial year, there was one breach against the Treasury Management Strategy which resulted in a negligible risk to Council funds as previously reported. This was rectified as soon as operationally possible and did not result in any losses. Other than this the Council has operated within its Treasury Management Framework.

3.2. The CCLA fund dropped in capital value by £240k but is still valued at £1.5m over the initial investment made by the Council. As previously identified in the strategy, there will be short-term fluctuations in capital value but the Fund Manager expects there to be some recovery during 2021.

3.3. The Council's investment holdings on the 31st March 2019 were £47.0m and £50.4m on 31st March 2020. The average investment balance during the year was slightly higher than allowed for in the budget due to re-phasing of the capital programme and additional CIL contributions.

3.4. Interest earnings from investments were some £0.77m, which was above the budget of £0.54m mainly because of a higher average cash balance than expected.

3.5. The return on investments in 2019/20 was 1.25% compared to the budgeted rate of 1.01%.

4. Conclusion

4.1. It should be noted that apart from one breach during the year, the Council's Treasury Management has operated within approved parameters, has resulted in no realised losses and interest earnings of £0.77m which have helped to support Council services.

List of appendices:

Appendix A – Economic Environment Update

Appendix B – Borrowing and Actual Investment Activity compared to the Approved 2019/20 Strategy

Appendix C – Treasury Performance Indicators for 2019/20

Background papers:

None

Corporate Implications

Legal/Constitutional: None

Financial: As detailed in report.

Potential impact on climate change and the environment: The Council's Climate and Ecological Emergency Action Plan as agreed at Cabinet 28th January 2020 included review of the Council's investment strategy in light of the Climate and Ecological Emergency Declaration.

Contribution toward achieving a net zero carbon position by 2030: As above

Personnel: None

Risk Management: All treasury management activity requires a careful consideration of risk and reward.

Equality and Diversity: None

Health and Safety: None

Digital: None

Other: None

Consultees: None

Relevant Policies and Strategies:

Treasury Management Strategy 2019/20

Appendix A – Economic Environment Update

Introduction

The amount of interest the Council earns on its balances is a function of the mix of fixed and variable rate investments made by the authority, together with the performance of the shares it holds in pooled investment funds such as the CCLA and Money Market Funds.

Therefore, the interplay of various economic factors including interest rate expectations, property prices and economic growth all affect the performance of the Council's investments.

Economic factors

Uncertainty surrounding Brexit and the impact of Coronavirus had the most significant effects on the UK economy in 2019/20 and are expected to continue to impact further going into 2020/21.

The UK Bank of England base interest rate started the year at 0.75% before the impact of Coronavirus resulted in two cuts to the rate in March 2020 with a year-end interest rate of 0.10%. Inflation year to March was 1.5% (CPI). Low levels of unemployment continued, but are likely to increase in 2020/21 with the impact of Coronavirus playing out. It is now very unlikely that interest rate increases will happen in the short to medium term due to the impact of Coronavirus with some forecasters suggesting a negative Bank of England base rate could be introduced.

This has led to the Council's fixed and variable rate investments continuing to earn historically low levels of interest, with this expected to continue into 2020/21. The Council have locked into a number of Local Authority deals at favourable fixed rates due to the uncertainty surrounding Coronavirus.

The retail property sector in particular has been impacted significantly by Coronavirus at the end of the year, even before the lockdown was enforced. The valuation of the Council's investment in the CCLA Property Fund decreased by £0.2m in the year, leaving the Council's unrealised gain at £1.5m on its initial investment. The income yield for the year was 4.48%, as measured against the current £6.5m market value. Capital values in the Fund are down by a further £0.2m as at the end of May, but the Manager believes these are not expected to fall much further with recovery predicted moving into 2021. The Fund is currently closed for redemptions and purchases as identifying a fair value for transactions is currently difficult. The fund will only be paying investors on the basis of income collected and is aiming to pay between 70-75% of the normal dividend during 2020/21. The income returns are again expected to recover moving into 2021/22 and further information about the shape of the Fund is given below.

CCLA are expecting the property sector to return to a more normal position by next year. The asset shape of the CCLA's holdings should also protect returns moving forwards as they have less retail property than many other property funds in the sector.

The significant proportion of the CCLA's investments are in industrial and high-quality office accommodation, which have both held up well in the current situation with the Coronavirus.

The impact of Coronavirus affected Treasury Management in 2019/20 and will continue to do so in 2020/21. The April 2020 CIPFA Treasury and Capital Management Update Bulletin said the following about the impact of Coronavirus:

"The Panel would recommend that day-to-day cash flow management is prioritised during and immediately after the Covid-19 period. Forecasted cash flows are likely to be on a downward trend for the medium to long term."

As such the Council will endeavour to keep more of its cash than usual at shorter durations in order to account for the uncertainty explained above. This in turn, is likely to impact on interest income returns moving into 2020/21.

Appendix B – Borrowing and Actual Investment Activity compared to the Approved Strategy for 2019/20

External borrowing

1. The Council became effectively debt free on the 16th September 2002, when it repaid all its PWLB debt. The Council therefore only has the freedom to borrow in the following circumstances:

- Short term borrowing to manage liquidity
- Long term borrowing only to fund capital expenditure if no other capital resources exist e.g. the Council has spent its capital receipts or expects to do so imminently

The Council did not need to borrow in 2019/20.

2. Finance leases are deemed by Government to be a type of borrowing in the Council's Accounts and Treasury reporting must identify that the Council has borrowed money when they are used. At 31st March 2020, the Council had outstanding finance lease liabilities of £738,000.

Investments

3. Officers with appropriate knowledge and training invest the Council's cash balances. Arlingclose are used as advisers on treasury management to help inform the decision-making process.

4. The Council's funds are invested in the following priority order, in accordance with statutory guidance:

i) Security – protecting the capital sum invested from loss

ii) Liquidity – ensuring the funds invested are available for expenditure when needed

iii) Yield – subject to achieving proper security and liquidity, to pursue a yield on investments to support service provision

The regulations and CIPFA both advise that absolute certainty of security of capital and liquidity does not have to be achieved before seeking yield from investments. An appropriate balance of all three should be sought and that balance is determined by the Council in its Treasury Strategy.

5. The Council uses cash-flow planning methods in order to manage its in-house investments. This allows officers to separate in-house funds in to two categories:

- Shorter term, lower yielding investments – these investments are invested for relatively short durations, normally 3-6 months, in order to ensure that the maturity profile of investments matches the peaks and troughs in the Council's liquidity needs – particularly for the final 2 months of the year where council tax income falls significantly due to the 10 monthly instalments most residents choose to pay in.

- Longer term, higher yielding investments – these are investments of ‘core cash’ which the Council does not require for operational purposes within the short to medium term. These funds can be invested for a year or more in appropriate counterparties in order to generate higher yields without causing liquidity issues.

6. During 2019/20 the Council’s investment portfolio has remained relatively similar in size from £47.0m to £50.4m. The increase in balance reflects re-phasing of capital schemes from 2019/20 into later years and higher than anticipated levels of CIL income.

Compliance with Treasury Management Strategy

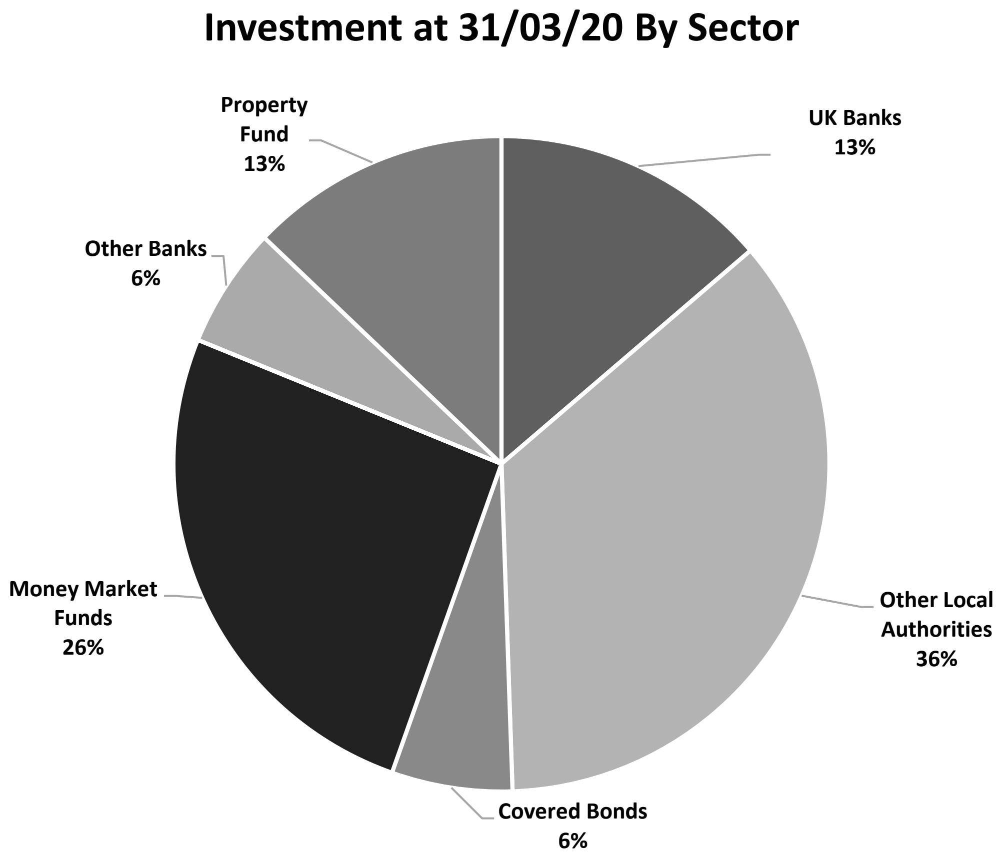
7. A summary of the approved treasury management strategy, together with actual outcomes is presented below:

a. **To ensure that there are no breaches of the approved counterparty limits or durations**	One breach occurred to counterparty limits in 2019/20 as previously reported.
b. **The option to invest further sums in pooled funds**	No additional investments in longer term funds took place in 2019/20.
c. **To continue holding up to £8m (£5m initial investment plus a generous allowance for unrealised capital growth) investment in the CCLA Local Authority Property Fund**	The CCLA depreciated in value during 2019/20, largely due to the impact of Coronavirus. However, £291k in dividend income was still realised. The Council’s investment was valued at £6.48m as at 31st March 2020.
d. **Limit investments over 365 days in duration to £18m**	Investments with a duration in excess of 365 days did not exceed £18m in the year.
e. **Ensure that no more than 75% of the Council’s Portfolio is invested for periods of greater than 3 months at any one time**	No breach occurred.
f. **In exceptional circumstances allow short borrowing on occasions to cover any liquidity shortfalls caused by the unexpected timing of payments or to avoid the opportunity costs of liquidating certain investments**	No exceptional borrowing was required in 2019/20.

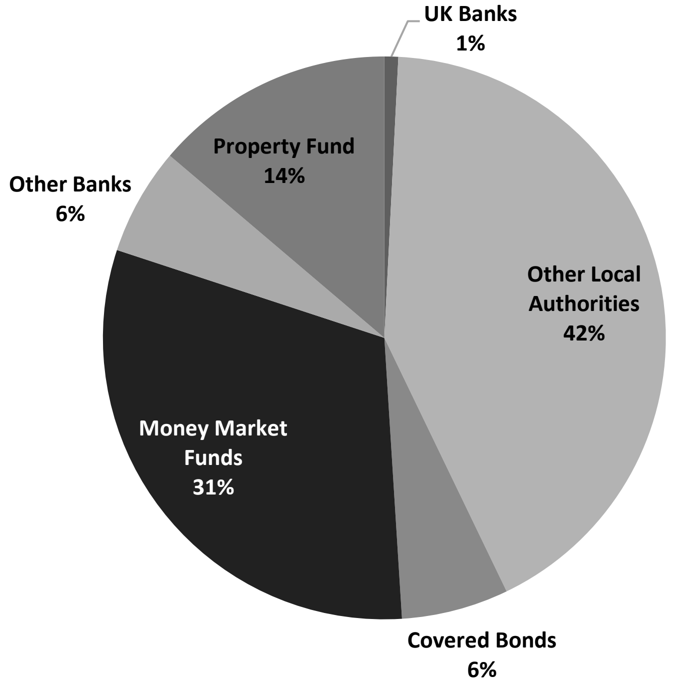
In 2019/20, the Council remained mindful of the risk of Bail-in losses from unsecured lending to banking counterparties.

As at 31st March the Council's exposure to Bail In risk (direct lending to banks and building societies) was 20%, against 7% at the end of the previous financial year. Year ending exposure tends to be lower than the average exposure because, where possible, the Council takes advantage of higher rates offered by other local authorities in the final quarter of the year. However, due to the uncertainty surrounding the impact of Covid-19, the Council chose to hold a higher proportion of its cash in liquid accounts in order to protect against potential cashflow problems. Two notice accounts were also set up in 2019/20 with HSBC and Lloyds to take advantage of the slightly higher interest rates on offer.

Exposure	**2017/18**	**2018/19**	**2019/20**
Bail In Risk -Direct investment	13%	7%	20%
Bail In Risk – Pooled Fund Managers and Money Market Funds	25%	31%	26%
Exempt from Bail In (including CCLA)	62%	62%	54%
Total	100%	100%	100%



Investment at 31/03/19 By Sector



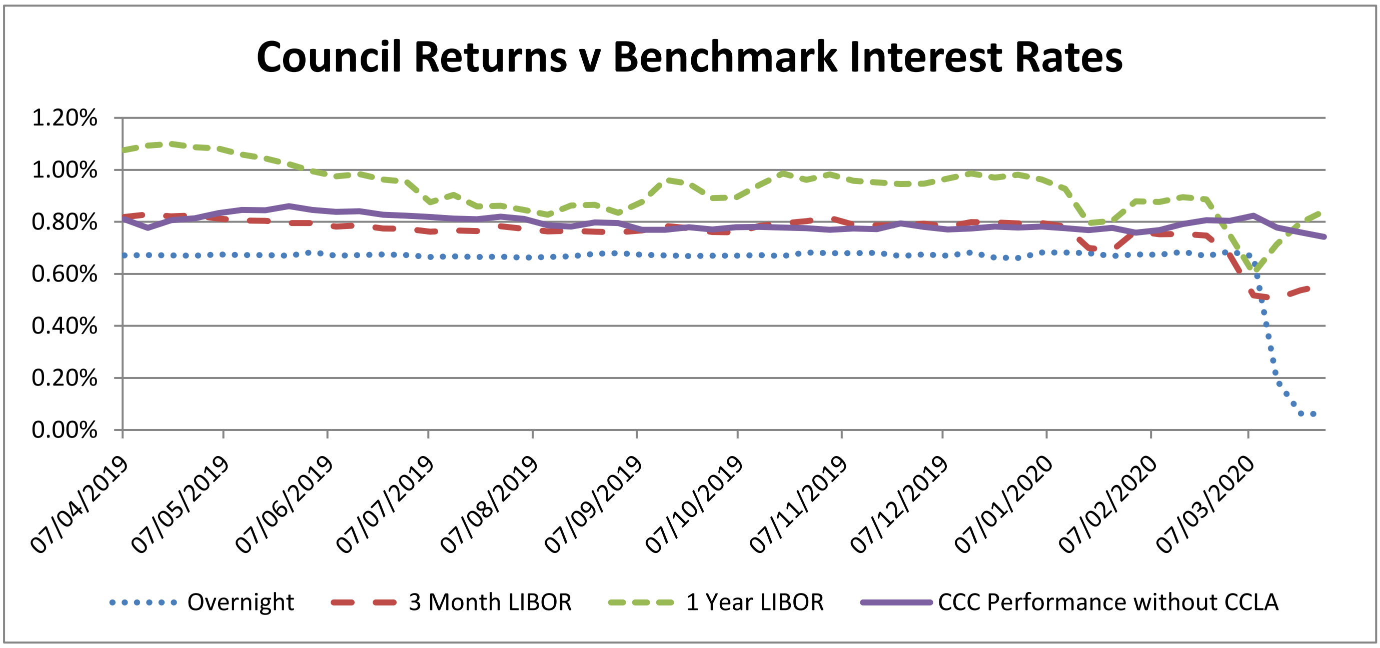
Counter Party	31/03/2020	Limits for 2019/20
Short-Term Money Market Instant Access Funds	£s	£s
BlackRock MMF	306,000	6,000,000
Aberdeen Constant Fund	5,925,000	6,000,000
Federated Money Market Fund	5,241,000	6,000,000
Invesco Money Market Fund	1,500,000	6,000,000
CCLA Property Fund	6,482,180	8,000,000
UK Treasury Bills	0	Unlimited
Banks		
Natwest	912,000	3,000,000
HSBC	3,000,000	3,000,000
Lloyds	3,000,000	3,000,000
DBS (Development Bank of Singapore)	3,000,000	3,000,000
Local Authorities		
Wirral Borough Council	5,000,000	20,000,000
Eastleigh Borough Council	2,000,000	20,000,000
London Borough of Croydon	5,000,000	20,000,000
West Dunbartonshire Council	3,000,000	20,000,000
Thurrock Borough Council	3,000,000	20,000,000
Fixed and Floating Bonds		
FRN – Barclays	3,000,000	6,000,000
	50,366,180	

Return on investments

8. Interest rates remained at very low levels throughout 2019/20, culminating in a drop of the Bank of England base rate in March to 0.25% and then 0.10%. Consequently, returns remain below the prevailing inflation rate, resulting in negative real rates of return on funds invested.

Comparisons by Arlingclose out of 127 authorities (143 last year) show the City Council's returns remained in the second quartile for authorities in March 2020 (50th highest) compared to March 2019 (49th highest). This shows that comparative performance remains significantly lower in terms of total return ranking than its high point early in 2016 (22nd highest), and December 2015 (10th highest). Over this period many authorities have invested more extensively in property funds, bond funds, equity funds and mixed asset funds. Consequently, Chelmsford has moved further down the total return curve.

The LIBOR (London Inter Bank Offered Rate) rates below show the interest levels that London based banks charge each other. These highlight the historically low levels of interest rates and provide context for the Council's own investment returns.



	Market investments (excluding CCLA)	CCLA Investment Yield	All Investments
	Year ending 31/03/2020		
Average yield	0.86%	4.48%	1.25%

Security

The CCLA fund dropped in capital value by £240k but is still valued at £1.5m over the initial investment made by the Council. As previously identified in the strategy, there will be short-term fluctuations in capital values but the Fund Manager expects there to be some recovery during 2021.

Conclusion

The Council had one breach during the year through investing above agreed Counterparty Limits. This was rectified as soon as operationally possible and did not result in any losses.

Other than this the Council has operated within its Treasury Management Framework. This has enabled the Council to safeguard its financial assets and produce a good level of return relative to the prevailing market interest rates.

Treasury Management Performance Indicators

Chelmsford City Council

Period Ending: 31/03/2020

Security

	Year 2019/20	Projected as at Nov 19	Target for year	Target for year	Target for year	Target for year
	31/03/2020	*31/03/2020*	*31/03/2020*	*2021/22*	*2022/23*	*2023/24*
Require - Only to invest with approved counterparties	No breach	No breach	No breach	No breach	No breach	No breach
Require - Only to invest up to approved limits	One breach	One breach	No breach	No breach	No breach	No breach
Target - Bail in exposure to not exceed portfolio	45.40%	50.00%	50.00%	50.00%	50.00%	50.00%

Liquidity

	Year 2019/20	Projected as at Nov 19	Target for year	Target for year	Target for year	Target for year
	31/03/2020	*31/03/2020*	*31/03/2020*	*2021/22*	*2022/23*	*2023/24*
Target - At least £10m maturing in 100 days or less	£ 35,884,000	£ 30,000,000	£ 10,000,000	£ 8,000,000	£ 8,000,000	£ 8,000,000
Require - Investments maturing in more than 365 days not to exceed target	£ 14,482,180	£ -	£ 18,000,000	£ 10,000,000	£ 10,000,000	£ 10,000,000
	£ 50,366,180	**£ 30,000,000**				

	Actual Borrowing 2019/20	Projected as at Nov 19	Target for year	Target for year	Target for year	Target for year
	31/03/2020	*31/03/2020*	*31/03/2020*	*2021/22*	*2022/23*	*2023/24*
Requirement - Authorised Limit of Borrowing	£ Nil	£ Nil	£ 45,000,000	£ 45,000,000	£ 45,000,000	£ 45,000,000
Target - Operational Boundary of Borrowing (excluding finance leases)	£ Nil	£ Nil	£ 25,000,000	£ 25,000,000	£ 25,000,000	£ 25,000,000

Yield

	Year 2019/20	Projected as at Nov 19
	31/03/2020	*31/03/2020*
Average yield on cash portfolio	0.86%	0.72%
3 month Libor benchmark	0.56%	0.63%
Average yield on CCLA	4.48%	4.14%
Average yield on total portfolio	1.25%	1.20%
1 year Libor benchmark	0.84%	0.85%

APPENDIX C

Chelmsford City Council Treasury Management and Investment Sub-Committee

22 June 2020

Non-Treasury Investments - Monitoring and Strategy Development

Report by:
Director of Financial Services

Officer Contact:
[Joe Reidy, Corporate Property Services Manager, Joe.Reidy@chelmsford.gov.uk, 01245 606311]

Purpose
To consider the work programme for the Treasury Management Sub-Committee in order to give effect to the recent changes to its Terms of Reference, in respect of non-cash investments. This report and appendices are designed to facilitate an initial discussion to establish what information will be required by the sub-committee at future meetings to enable it to carry out its expanded role to:

(i) monitor non-cash investments in the same way that it is does for cash investments, and
(ii) to comment on and make recommendations to Cabinet on the Investment Strategy

Recommendations
It is recommended that the Treasury Management Sub-Committee considers the report and appendices, and the information requirements for future meetings, and agrees the next steps/programme of work set out in the report.

1. Background

1.1. On 13 May 2020, the Council considered, and approved, changes to the Terms of Reference for the Treasury Management Sub-Committee (TMSC), recommended by the Governance Committee. As the TMSC is a sub-committee of the Audit and Risk Committee, it was appropriate to consult with the Committee about the changes and the report attached at Appendix 1 was circulated to Audit and Risk Committee Members alongside the proposed changes to the Terms of Reference. Comments received were fed back via the Chair of Audit and Risk, to the Chair of Governance Committee. The new Terms of Reference are included at Appendix 2.

1.2. The key change to the TMSC's Terms of Reference was to expand the remit of the Sub-Committee to include non-cash investments such as commercial property, in addition to the cash investments already considered by the Sub-Committee under the Treasury Management Strategy. The Sub-Committee would then be able to comment on both the Treasury Management and the Investment Strategy moving forward and make recommendations to Cabinet on these Strategies.

1.3. The reasons for bringing consideration of both cash and non-cash investments together were set out in the report and included reference to investment guidance and increasing the understanding of the risk profile of the Council's investment portfolio. This was summed up in the conclusion as follows:

"The current system of strategy development and monitoring of cash investments by the Sub-Committee works well and it would be appropriate to extend this to other forms of non-cash investment. The overlap between the Treasury Management Strategy and the Investment Strategy, and the knowledge and skills required to develop them, would also support bringing these two strategies together. In addition, developing a suite of indicators to monitor property investment returns will add a robust level of scrutiny to the performance of the Council's investment portfolio."

2. Current Strategy

2.1. The Capital and Investment Strategy approved at Council in February 2020 set out some high-level data in respect of the Council's commercial property portfolio including segmental analysis, acquisitions and disposal in year and valuations. It also set out the principal risk of holding these investments such as:

- Investments funded from borrowing expose the Council to risk that the income generation from schemes is less than the cost of repaying the borrowing.
- Such investments must be proportional and do not concentrate risk in one particular sector or activity.
- Capital appreciation may not occur, and the value of the investment could fall in real terms.

2.2. Other key points raised in the Strategy were that:

- the Council would monitor the value of its investment property and the security of the related income
- that commercial investments should remain proportionate to the size of the authority
- compared to other forms of investment, and depending on the prevailing market conditions, investment in property can take time to sell and therefore the Council undertakes these investments on the basis that they are medium to long term in nature

2.3. It should be noted that the investments to be included in the monitoring arrangements do not include the development of land holdings by the Council or purchase of assets to support service delivery such as temporary or affordable housing. The investments to be covered here are direct commercial investments entered into for financial return. Some of these commercial property investments have a dual purpose in that they also support local economic objectives, such as supporting SMEs, but it is still important to monitor the financial performance of such assets.

3. Proposal

3.1. The current Strategy will be required to be reviewed by Council in February 2021. For the TMSC to feed into that Strategy development, it needs to be provided with sufficient information to enable it to understand the Council's investment property portfolio and associated risks.

3.2. Appendix 3 provides some initial information to provoke discussion on the potential criteria to be set within the Strategy and suggests key data that may assist the Sub-Committee in its monitoring of investments. The aim will be to build these into a framework of reporting so that the TMSC receives a draft Strategy ahead of the new financial year, a mid-year report and an outturn report, just as it does for cash investments.

3.3. Members are asked to consider the suggested criteria and information requirements set out in Appendix 3 and determine what data officers need to provide to subsequent meetings in order for the Sub-Committee to be able to robustly scrutinise non-cash investments, and make recommendations on the draft strategy to be presented to the Sub-Committee later in the financial year.

4. Conclusion

4.1. The aim of the report is to establish what information will be required by the sub-committee at future meetings to enable it to carry out its expanded role.

4.2. The proposed work programme for TMSC in relation to monitoring non-cash investments and strategy development is as follows:

Date:	Activity/Objective:
Initial preparatory work culminating in draft Strategy 2021/22:	
Jun 2020	Review suggested data and confirm requirements for next meeting
Oct 2020	Receive monitoring data, agree indicators/data/criteria to be included in Investment Strategy 2021/22
Dec 2020	Consider draft Investment Strategy 2021/22 and make recommendations to Cabinet
On-going reporting pattern:	
June	Consider outturn report for recommendation to Cabinet
Oct	Consider mid-year report for recommendation to Cabinet
Dec	Consider draft Investment Strategy and make recommendations to Cabinet

List of appendices:

Appendix 1 – Consultation report circulated to Audit and Risk Committee 24 April 2020

Appendix 2 – Treasury Management Sub-Committee Terms of Reference

Appendix 3 – Discussion document – example investment criteria and data sets

Background papers:

None

Corporate Implications

Legal/Constitutional: The Council is required to produce an annual Investment Strategy and have due regard to investment guidance

Financial: The setting of performance indicators or monitoring criteria will enable robust monitoring of the financial performance of non-cash investments

Potential impact on climate change and the environment: The Council's Climate and Ecological Emergency Action Plan as agreed at Cabinet 28th January 2020 included review of the Council's investment strategy in light of the Climate and Ecological Emergency Declaration.

Contribution toward achieving a net zero carbon position by 2030: As above

Personnel: None

Risk Management: The Investment Strategy should be set taking account of the risk appetite of the Council. Risk mitigation is provided by on-going monitoring of investment returns.

Equality and Diversity: None

Health and Safety: None

Digital: None

Other: None

Consultees: None

Relevant Policies and Strategies:
Capital and Investment Strategy 2020/21

APPENDIX 1

AUDIT AND RISK COMMITTEE
24th April 2020

Subject	TREASURY MANAGEMENT SUB-COMMITTEE TERMS OF REFERENCE
Report by	DIRECTOR OF FINANCIAL SERVICES

Enquiries contact: Amanda Fahey, 01245 606401, amanda.fahey@chelmsford.gov.uk

Purpose

To consider expanding the remit of the Treasury Management Sub-Committee of the Audit and Risk Committee, to include the monitoring of "non-cash" investments such as commercial property and to update the Terms of Reference of the Sub-Committee in respect of membership.

Recommendation(s)

1.	The Audit and Risk Committee recommend to Council the expansion of the remit of the Treasury Management Sub-Committee and the revised Terms of Reference as set out at Appendix 1 [*the agreed TOR are now shown at Appendix 2*]

Corporate Implications	
Legal:	The Council is required to produce an Investment Strategy under the Ministry for Housing, Communities and Local Government's (MHCLG) *Statutory Guidance on Local Government Investments.* Councils are also required to have regard to the Chartered Institute of Public Finance and Accountancy (CIPFA) publications *The Prudential Code for Capital Finance in Local Authorities* and *Treasury Management in the Public Services.*
Financial:	A robust investment strategy is essential in the delivery of the Council's objectives over the medium-term, and in managing the risks and opportunities inherent in investment transactions. Monitoring should be undertaken to ensure delivery of the strategy.
Personnel:	None
Potential impact on climate change and the environment	The Council's Climate and Ecological Emergency Action Plan as agreed at Cabinet 28th January 2020 included review of the Council's investment strategy in light of the Climate and Ecological Emergency Declaration.
Contribution towards achieving a net zero carbon position by 2030:	As above

Risk Management:	The Investment Strategy should be set taking account of the risk appetite of the Council. Risk mitigation is provided by on-going monitoring of investment returns.
Equalities and Diversity:	N/a
Health and Safety:	None
IT:	None
Other:	None

Consultees	Cabinet Member for Fairer Chelmsford

Policies and Strategies
The report takes into account the following policies and strategies of the Council:

- Capital and Investment Strategy
- Treasury Management Strategy

1. Background

1.1 The recent rapid expansion of commercial property purchases by local authorities has prompted concern from Government, Cipfa and others particularly in regard to borrowing to fund such investment.

1.2 Guidance comes in the form of the Prudential Code, MHCLG Guidance on Local Investments, Guidance on Minimum Revenue Provision (MRP) and most recently Cipfa's informal guidance on "Prudential Property Investment".

1.3 Since 2019/20, Councils have been required to produce a Capital and Investment Strategy, which is expected to provide some detail around the governance and monitoring arrangements for non-cash investments (such as property) and Chelmsford's 2020/21 Strategy mentions a proposed review of governance and monitoring arrangements for the coming year.

2. Why do we need to respond?

2.1 Many local authorities have undertaken investment in commercial property to supplement their revenue budgets, especially given the perceived need to act "more commercially" and become more self-reliant in the face of central funding cuts. Concerns have stemmed from the increased use of borrowing to fund such purchases, given the Prudential Code's statement that local authorities must not borrow more than, or in advance of, their needs purely in order to profit from the investment of the extra sums borrowed.

2.2 Key areas for the Council to consider are:

- whether the Council is having due regard to the regulatory and advisory framework and is acting under the correct legal powers
- whether the risks are understood, in terms of incurring borrowing costs in exchange for potentially uncertain returns
- whether the increasing use of borrowing to fund such investment could provoke statutory intervention rather than continued reliance on the self-regulatory prudential code (and therefore usher in a more restrictive regime)

2.3 Clarifying the framework for decision-making and improving the reporting of non-cash investments, will support the Council in demonstrating that it has considered the risks inherent in these transactions, and set an Investment Strategy commensurate with its risk appetite. It will demonstrate decision-making based on relevant data and provide an opportunity for scrutiny of the investments, in the same way that cash investments are currently scrutinised by the Treasury Management Sub-Committee of the Audit and Risk Committee.

3. The proposal

3.1 It is proposed to extend the Terms of Reference of the Treasury Management Sub-Committee to encompass both cash and non-cash investments. The Sub-Committee currently reviews the Council's Treasury Management Strategy annually and makes recommendations to Cabinet, for onward approval at Council. The Council has appointed it as the designated body which considers treasury matters under Cipfa's Treasury Management Code of Practice.

3.2 In addition to reviewing the annual strategy, the Committee receives both a mid-year and end of year report prior to consideration by Cabinet and Council. These reports contain Treasury Management indicators which set limits for cash investments both in terms of monetary amounts and strength of counterparties, and the monitoring of these indicators ensures adherence to the approved strategy and provides opportunity for an appropriate level of scrutiny. As commercial investment increases, it is notable that this area of investment, whilst being subject to the Capital and Investment Strategy annual approval process, does not have the same level of scrutiny during the year to ensure it is meeting the Strategy requirements.

3.3 Bringing together the Investment Strategy and the Treasury Management Strategy and taking them through the same route, provides some consistency in method of scrutiny, utilises a similar knowledge and skillset as required for Treasury matters and improves transparency. A key part of this role could be to help determine the indicators that the Council wishes to use to monitor its investment property portfolio, having regard to the suggested range of indicators included in the Investment guidance while ensuring these are the right measures to use locally. As commercial property income is a key source of revenue income for the Council, supporting its core service delivery, it is important that there is some focus on the risks arising from this, and that the Council's Strategy is formed in light of both the risk and returns, in the same way that the Treasury Management Strategy seeks to find a balance between risk and return, taking into account the security, liquidity and yield available.

3.4 Minor adjustments may be made to the Constitution under delegation to the Monitoring Officer, while more significant changes are required to go through the Governance Committee before ultimate approval by full Council. For this reason, and due to timing of meetings, the proposed changes have already been considered by the Governance Committee meeting of 11th March and are scheduled to be presented to the full Council meeting of 13th May for final approval. The Governance Committee report however, included a delegation to the Chair to make any amendments to the onward report, following consideration of the changes to the Terms of Reference for the Treasury Management Sub-Committee by the Audit and Risk Committee. This report therefore seeks the views of the Committee on the proposed Terms of Reference so that any feedback can be supplied to the Chair of Governance ahead of the Council meeting.

3.5 If these changes to the Treasury Management Sub-Committee's Terms of Reference are approved by Council, the Director of Financial Services will then schedule work into the meetings to prepare indicators and meet reporting requirements.

3.6 In addition to expanding the remit to cover a wider definition of investments, the Terms of Reference as set out in the current Constitution require updating to reflect current practice and political balance. It is therefore recommended to amend the membership from three to five, with three Members being drawn from the Audit and Risk Committee.

4. Conclusions

4.1 The current system of strategy development and monitoring of cash investments by the Sub-Committee works well and it would be appropriate to extend this to other forms of non-cash investment. The overlap between the Treasury Management Strategy and the Investment Strategy, and the knowledge and skills required to develop them, would also support bringing these two strategies together. In addition, developing a suite of indicators to monitor property investment returns will add a robust level of scrutiny to the performance of the Council's investment portfolio.

<table>
<tr><td colspan="4">Treasury Management and Investment Sub-Committee
Terms of Reference</td></tr>
<tr><td colspan="4">Membership: Seven Members</td></tr>
<tr><td>Quorum

THREE</td><td>Substitutes

YES</td><td>Politically Balanced

YES</td><td>Frequency of meetings

THREE PER YEAR</td></tr>
<tr><td colspan="2">Functions/Purpose</td><td colspan="2">Delegations</td></tr>
<tr><td colspan="2">1. To comment on the draft Treasury Management and Investment Strategies and make recommendations to Cabinet on those Strategies.
2. To receive reports on Treasury Management and Investment activities and performance three times per year.
3. To report to the Audit and Risk Committee on any breaches of Treasury Strategy, Investment Strategy or Treasury Management Procedures.
4. On occasion of urgent matters to agree changes to the Treasury Management or Investment Strategy without reference to Full Council.
5. In the light of performance and market conditions recommend changes to either strategy going forward.
6. The sub-committee is not intended to be a consultee to individual investment decisions.</td><td colspan="2">N/A</td></tr>
<tr><td>Procedures</td><td colspan="3">Part 4.2 – Cabinet and Committee Procedure Rules
Part 4.9 – Financial Rules</td></tr>
<tr><td>Codes</td><td colspan="3">Part 5.1 – Code of Conduct for Councillors</td></tr>
</table>

Discussion Document for developing Chelmsford City Council investment strategy.

Central Government has responded to the rise of property investment transactions undertaken by local authorities, particularly regarding borrowing for such investments. MHCLG and CIPFA have both published guidance notes on this matter which has since 2019/20 required Local Authorities to produce an investment strategy which should provide guidance and details of governance and monitoring arrangements for non-cash investments such as property.

Chelmsford City Council has for many years held and managed a range of commercial property. In recent years this has been extended to provide a revenue stream to support the Council's budget and to aid economic development in the City. The decision to invest has been based on assessment of the opportunities as they arise, and the purpose of this document is to outline suggested investment criteria for Chelmsford City Council's property purchases together with the details that will be included in a half yearly monitoring report.

Investment Criteria

Set out below are some suggested core strategy objectives for the Council's direct commercial property investments.

- Assets should be located within the City and support or further the development of economic activity.

- Commercial property investments should generate an immediate income, secured through legal agreements let on commercial terms, or from properties which are contracted to be let.

- Assets should provide an income yield (return) with a clear margin over the cost of capital, in a form which is sustainable, and has the potential to increase through future rental growth.

- Assets will be selected to achieve an even balance of risk and return through portfolio diversification.

- The aim will be to acquire investment grade properties where possible that possess characteristics that retain liquidity and preserve capital (notwithstanding market movement)

- Lot size should be between £3m and £10m.

- Single occupancy investments let to institutional tenants will be preferred in order to minimise management expense and risk. Multi-let properties or multi-unit schemes may be considered if all other criteria are met.

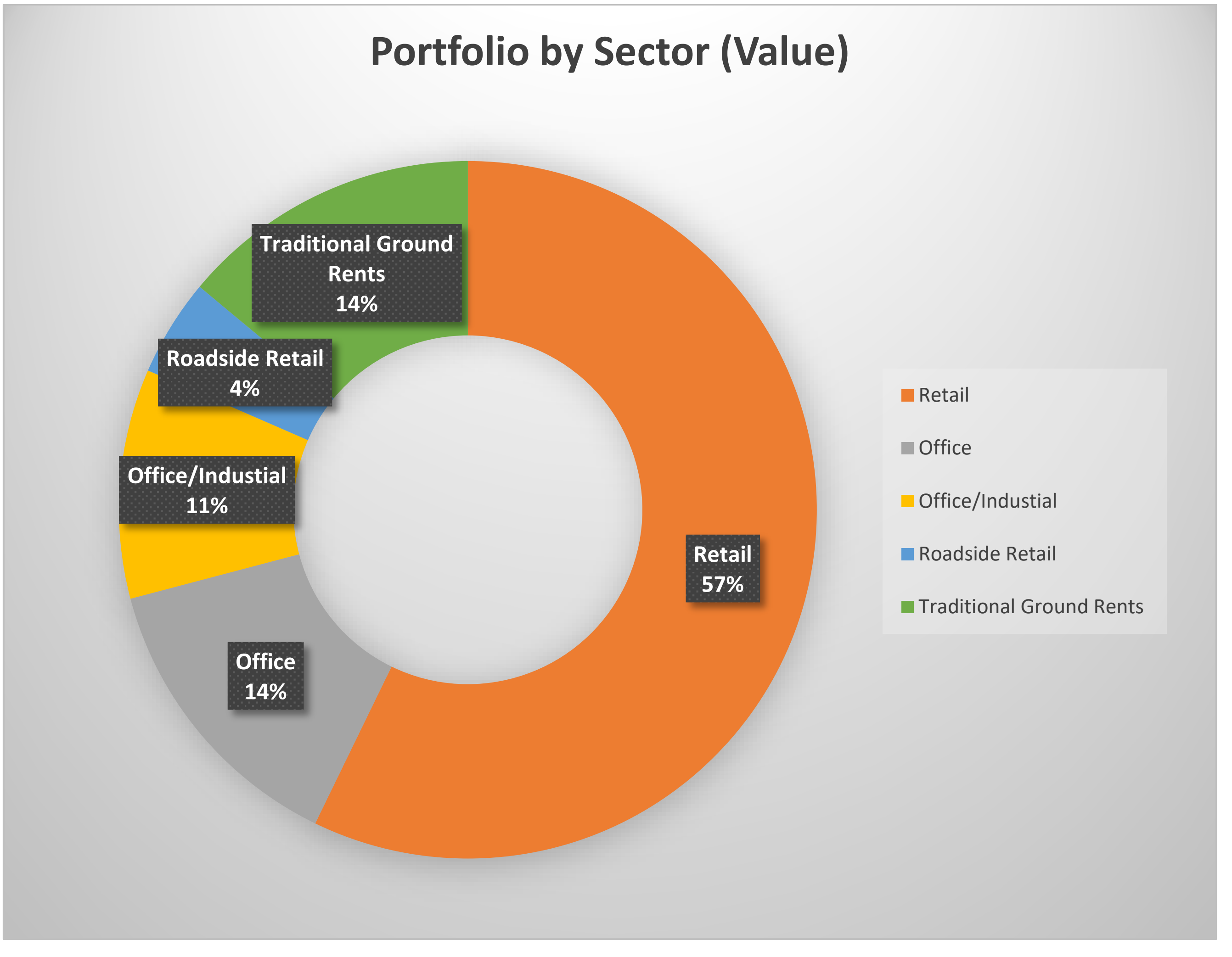
- Investments will be considered if the income is secured by existing tenants with a low-risk or medium-risk financial profile. The financial strength of existing tenants will be analysed considering company accounts and the use of appropriate methods of risk assessment and credit scoring such as Dun & Bradstreet reports.

- Assets that offer opportunities to increase value and income through asset management initiatives should be considered provided that all other criteria are meet.

The Current Portfolio

The Council's property investment portfolio consists of 15 income-producing assets that provide an annual income of over £5m. The assets that make up this holding may have been purchased for other purposes such as to support small and local business rather than as investments, but the characteristics of these assets are such that we believe that they should be reported here. Internally we have assessed the portfolio's value to be £82.1m following our latest acquisition of the Aquarium earlier this year.

The single largest asset held by the Council is High Chelmer Shopping Centre which accounts for over half of the investment income and value. Naturally, this distorts the sector analysis shown below and makes it is difficult to show a balanced sector split.



Investment Portfolio Reporting Criteria.

Performance reporting will be undertaken twice a year and the Estates Team will produce a performance report for the portfolio to include details of:

- any changes in the portfolio in the period (acquisitions and sales)
- all charges and receipts, indicating any arrears.
- capital expenditure, planned or reactive.
- performance against budgets both expenditure and income.
- any potential changes to the income through lease renewals and rent reviews.
- any changes to Dunn and Bradstreet rating of tenants.