	WEST OXFORDSHIRE DISTRICT COUNCIL
Name and date of Committee	**Finance and Management Overview and Scrutiny Committee: Wednesday 7 October 2020**
Report Number	**Agenda Item No. 8**
Subject	**Treasury Management Activity and Performance 2020/21**
Wards affected	All
Accountable member	Cllr Derek Cotterill Chairman Finance and Management Overview and Scrutiny Committee Email: derek.cotterill@westoxon.gov.uk
Accountable officer	Elizabeth Griffiths, Chief Finance Officer Tel: 01993 861188 Email: elizabeth.griffiths@westoxon.gov.uk
Summary/Purpose	To advise members of treasury management activity and the performance of internal and external fund managers for the period 1 April 2020 – 31 August 2020.
Annexes	Annex A – Schedule of Investments
Recommendation	That treasury management and the performance of in-house and external Pooled Funds' activity for the period 1 April 2020 – 31 August 2020 be noted.
Corporate priorities	
Key Decision	No
Exempt	No
Consultees/ Consultation	None

1. BACKGROUND

1.1. This report is submitted as one of the regular updates provided for this Committee in relation to Treasury Management activity and performance.

2. MAIN POINTS

2.1. Historically, West Oxfordshire District Council has been in a positive cash position, financing its capital programme from a mixture of capital receipts and working capital and investing the positive cash-flows in a range of instruments that gave a balanced approach to security, liquidity and returns.

2.2. Over recent years officers have advised the Council that it was moving towards a position where it would need to borrow to support future investment in the capital programme and have both external debt and investments.

2.3. To date officers have managed the financing of the capital programme by effectively using the positive cash-flows of the Council (typically April – Feb) to avoid external borrowing as this has been the most cost efficient form of capital financing with regard to prevailing interest rates. However, given the ongoing scale of the capital programme (£7m in 2019/20 and £18m in 2020/21) it is now clear that the Council will need to supplement this 'internal borrowing' with external borrowing or recalling pooled investment funds. As at 31 March 2020 the Council's accounts stated that the Capital Financing Requirement (the level of capital requiring financing via internal or external sources) was £16.3m and to date this has all been financed through internal borrowing.

2.4. WODC have been in discussion with the Council's Treasury Management advisors, Arlingclose, to review the current portfolio of investments and have sought their recommendations on any that should be liquidated from a risk perspective or any underperforming funds that should be recalled ahead of external borrowing. Their assessment was that nothing needed to be immediately recalled but that where investments had lost large capital values, these should be monitored to ensure that if they persist downwards, consideration is given to closing them.

2.5. Cash-flow estimates by the Treasury Officer show that the Council will experience a large cash shortfall of circa £21m by the end of the financial year 2020-21 due to funding large capital expenditure transactions in 2019/20 and 2020/21.

2.6. Borrowing from external sources remains an option for West Oxfordshire. There are two main sources for accessing loans with relative simplicity - other local authorities and the Public Works Loans Board (PWLB) but all available sources of financing will be considered.

2.7. The Covid-19 outbreak and the ensuing market concern saw economic growth forecasts reverse steeply as countries closed borders and imposed lockdowns. Equity markets delivered the fastest bear markets in history in Q1 2020 with the UK and Europe faring worst, losing 25% and 24.7% respectively. This impacted the capital values of Schroders Income Maximiser Fund and the Columbia Threadneedle UK Equity Fund. The capital values in August have shown some recovery since March 2020 but equity prices are expected to remain volatile over the forthcoming 12-18 month period. Currently these two funds are valued at £438k less than the amounts originally invested. Arlingclose's advice was not to sell now as that would crystallise the losses but to monitor in the hope that the recovery continues.

2.8. The returns on the portfolio generally are down with a forecast of £608K against a budget of £680K.

3. INVESTMENT PERFORMANCE

3.1. Performance Achieved for the period (excluding outstanding Icelandic investments) is shown below:-

Performance of Fund 1 April 2020 to 31 August 2020 (annualised returns)	**In-House**	**Bonds**
Net Return	0.29%	4.75%

3.2. The current In-house investments have achieved a net return of 0.29% which is 0.09% above the 3 month LIBID rate. As the extent of the losses that banks and building societies will suffer due to the impact from the coronavirus epidemic remains uncertain but is expected to be substantial, in early June following Arlingclose's stress testing of the institutions on the counterparty list using bail-in analysis, a number of UK banks and building societies were suspended from the counterparty list for unsecured deposits. Although much better capitalised than before the 2007-09 financial crisis, under the current economic circumstances these entities were suspended for reasons of prudence. For those remaining on the list, the duration advice remains up to 35 days.

3.3. The table below shows the current valuations of the Pooled Funds portfolio at the end of August 2020 compared with the values at the close of the 2019/20 financial year. In the first five months of the year we have seen a capital gain of £729,363 however dividend returns have seen a drop of over £19k compared with this time last year. The table below shows the current valuations of the Pooled Funds portfolio at the end of August 2020 compared with the values at the close of the 2019/20 financial year.

3.4. Performance of other pooled funds is shown in the following table:

	Initial Investment	**1 April Fund Value**	**31 August Fund Value**	**Dividends paid out in 2020/21 as at 31 August**	**Gain / (Loss) for 2020/21**	**Gain / (Loss) to Initial Principal**
	£	**£**	**£**	**£**	**£**	**£**
Payden & Rygel –Cash+	2,000,000	2,005,540	2,047,795	3,871	42,255	47,795
UBS – Bond / Equity	2,000,000	1,665,187	1,830,567	44,389	165,380	(169,433)
M&G Strategic – Bond	2,000,000	1,865,992	2,062,593	16,886	196,601	62,593
Royal London Cash + (original investment)	2,000,000					
Royal London Short Dated Credit –Cash (additional investment)		1,933,013	1,995,086	11,612	62,073	(4,914)
Schroders – Equity	1,000,000	687,135	708,073	13,139	20,938	(291,927)

	Initial Investment	1 April Fund Value	31 August Fund Value	Dividends paid out in 2020/21 as at 31 August	Gain / (Loss) for 2020/21	Gain / (Loss) to Initial Principal
CCLA Diversified – All	1,000,000	911,541	989,044	9,914	77,503	(10,956)
Threadneedle - UK Equity	1,000,000	778,854	853,033	14,341	74,179	(146,967)
Kames Diversified-All	1,000,000	843,371	933,805	18,774	90,434	(66,195)
August 2020 Total	**£12,000,000**	**10,690,633**	**11,419,996**	**132,926**	**729,363**	**(580,004)**

3.5. **Payden Sterling Reserve Fund** – The fund invests in a diversified range of sterling-denominated, highly-rated and very liquid government agency securities and corporate fixed – and floating-rate and covered bonds. The Fund is currently returning 0.77% annualised and is one of the few funds which is valued at above the amount originally invested. Current gain is just under £48k.

3.6. **UBS Multi-Asset Income Fund** – The fund seeks to provide an income, through a diversified portfolio of investments in bonds and equities. The fund is expected, and is currently returning, income of around 4% for the year however the fund is valued at circa £169k less than the amount invested.

3.7. **M&G Strategic Corporate Bond Fund** - The aim of the Fund is to provide income and capital growth, through a top-down approach of the fund manager's economic outlook determining the fund duration, the sector allocation and stock concentration. It invests primarily in investment grade corporate bonds. Returns are likely to be around 3.4% against a budgeted return of 3.5%. The capital value has reduced by over £62.5k against the invested amount.

3.8. **Royal London Short Dated Credit Fund** – The Fund aims to offer income and capital growth by investing in a diversified portfolio of investment grade short dated bonds (issued by companies and organisations which meet the Fund's predefined ethical criteria). These bonds will include corporate bonds, asset backed securities, floating rate notes, UK government bonds and supranational and agency bonds. Income return is estimated at around 2.3% against a budgeted 2% return. The value of the fund is just over £5k less than originally invested.

3.9. **Schroder Income Maximiser Fund** – The Fund's investment objective is to provide income with potential for capital growth primarily through investment in equity and equity related securities of UK companies. The fund aims to deliver a target yield of 7% per year and in its first quarter returned 5.4% annualised. This fund has seen a £290k fall in capital value since its original investment.

3.10. **CCLA Diversified Income Fund** – The aim of the fund is to provide a balanced return from income and capital growth over time. The portfolio invests with UK and overseas equities, property, bonds and cash. The fund aims to achieve a 3% annual return. Current returns for the first quarter annualised are 3.96%. This fund has seen just under £11k fall in capital value against the amount invested.

3.11. **Threadneedle UK Equity Income Fund -** The aim of the Fund is to provide income with the potential to grow the amount invested. The Fund invests at least two-thirds of its assets in shares of UK companies. The Fund aims to achieve slow returns of income but also growth on the capital invested. The fund aims to return between 2.5% and 3.5% and is currently achieving 2.68%. The capital value of this fund is just under £147k less than the amount invested.

3.12. **Kames Diversified Monthly Income Fund -** The investment objective is to generate income with a target yield of approximately 3% per annum, with the potential for capital growth over the medium term (being any 5 year period). The fund is currently achieving 5.4% to date but is £66k down in capital value against the original amount invested.

4. FUNDAMENTUM SOCIAL HOUSING REIT

4.1. Following the implementation of changes to pooled funds the sum of £1 million was made available to be reinvested as supported by members of FMOS. The Council's Treasury Management Advisors, Arlingclose identified an opportunity to invest in a Real Estate Investment Trust, Fundamentum Property, investment advisors with a track record in the UK social housing market.

4.2. Following the launch in November 2019 the Council invested £1m into the new Fundamentum Social Housing REIT which purchases property and holds long term leases with Housing Associations who house vulnerable adults. Since the launch of the Fundamentum Social Housing REIT, the Investment Advisor has overseen 11 transactions up to the end of August 2020 and dividends of £6.5k have been received to date achieving a return of 1.30%. Returns of 5% are expected when the full portfolios of properties have been purchased and a full annual rental income is received.

5. ECONOMIC AND INTEREST RATE FORECAST

5.1. The UK's exit from the European Union took a back seat during the first quarter of 2020/21 as the global economic impact from coronavirus took centre stage. Part of the measures taken to stop the spread of the pandemic included the government implementing a nationwide lockdown in late March which effectively shut down almost the entire UK economy. These measures continued throughout most of the quarter with only some easing of restrictions at the end of May and into June.

5.2. Bank Rate was maintained at 0.1% despite some speculation that the Bank of England's Monetary Policy Committee (MPC) might cut further and some MPC members also suggesting that negative rates are part of the Bank's policy tools. In June the Bank increased the asset purchase scheme by £100 billion, taking the recent round of QE to £300bn and total QE to £745 billion.

5.3. As can be seen from the table below Arlingclose's view on interest rates is that they remain at 0.10% for the unforeseeable future.

	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23
Official Bank Rate												
Upside risk	0.00	0.00	0.00	0.00	0.00	0.15	0.15	0.15	0.15	0.30	0.30	0.30
Central case	**0.10**	**0.10**	**0.10**	**0.10**	**0.10**	**0.10**	**0.10**	**0.10**	**0.10**	**0.10**	**0.10**	**0.10**
Downside risk	0.00	0.35	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50

6. FINANCIAL IMPLICATIONS

6.1. Investment income in the Authority's 2020/21 budget was set against a very different economic backdrop. Bank Rate, which was 0.75% in January/February 2020 now stands at 0.10%. Interest earned from short-dated money market investments will be significantly lower. In relation to income from the Authority's externally managed strategic funds, dividends and income distributions will ultimately depend on many factors including but not limited to the duration of COVID-19 and the extent of its economic impact, the fund's sectoral asset allocation, securities held/bought/sold and, in the case of equities, the enforced or voluntary dividend cuts or deferral.

6.2. The original investment interest budget for 2020/21 was set at £680,000 which was based on an average balance of £32.626 million from all the different type of investments (e.g. fixed term deposits, pooled funds, bonds) achieving an overall average return of 2.18%.

6.3. The breakdown of the budget and estimated performance for the year is as follows:

	2020/21 Budget	2020/21 Estimate Outturn
Pooled Funds	360,000	339,000
In-House Investments	161,200	125,000
Housing REIT	40,000	25,000
Bonds	118,800	118,800
Total	**680,000**	**607,800**

7. BACKGROUND PAPERS

7.1. Valuation 31 August 2020 – Pooled Funds & Bonds

7.2. In – House investment as at 31 August 2020

Annex A

SCHEDULE OF CASH INVESTMENTS OUTSTANDING AT 31 AUGUST 2020

NAME OF COUNTERPARTY	VALUE DATE	NOMINAL AMOUNT (£)	MATURITY DATE	RATE OF INTEREST	Fitch Credit Rating Long Term	Fitch Credit Rating Short Term
IN HOUSE MANAGEMENT						
Thurrock Council	17.10.19	1,000,000	16.10.20	1.02%	AA-	
Federated MMF	31.08.20	5,000,000		0.08%	AAAmmf	
Invesco AIM MMF	31.08.20	3,680,000		0.06%	AAAmmf	
Deutsche Asset & Wealth MMF	31.08.20	5,000,000		0.05%	AAAmmf	
TOTAL IN-HOUSE INVESTMENTS		**14,680,000**				

BONDS

COUNTERPARTY	Book Cost (£)	Market Value (£)
A2D Bond (4.75%)	2,500,000	2,661,725

HOUSING REAL ESTATE INVESTMENT TRUST

COUNTERPARTY	Book Cost (£)	Market Value (£)
Fundamentum REIT	1,000,000	970,000

MANAGED FUNDS

COUNTERPARTY	As at:	NOMINAL VALUE (£)	MARKET VALUE (£)
Royal London Shortdated Credit Fund	31.08.20	2,000,000	1,995,086
Payden Sterling Reserve Fund	31.08.20	2,000,000	2,047,795
M&G Strategic Corporate Bond Fund	31.08.20	2,000,000	2,062,593
Threadneedle UK Equity Fund	31.08.20	1,000,000	853,033
Kames Diversified Monthly Income Fund	31.08.20	1,000,000	933,805
UBS Multi-Asset Income Fund	31.08.20	2,000,000	1,830,567
Schroders Income Maximiser Fund	31.08.20	1,000,000	708,073
CCLA Diversified Income Fund	31.08.20	1,000,000	989,044
TOTAL VALUE OF FUND		**12,000,000**	**11,419,996**