Cabinet
30 July 2015 **Agenda item:**

Amendment to Treasury Management Strategy 2015/16

Cabinet Member: Councillor Peter Hare-Scott
Responsible Officer: Head of Finance

Reason for Report: To agree an amendment to the lending criteria included in the 2015/16 Treasury Management Strategy.

RECOMMENDATION(S):

1. **To agree the inclusion of the ability to deposit medium term cash balances of no more than £2.5m in to the CCLA commercial property fund.**

Relationship to the Corporate Plan: Maximising our return from all associated treasury activities enables the Council to support current levels of spending in accordance with our Corporate Plan.

Financial Implications: Good financial management and administration underpins the entire strategy.

Legal Implications: Compliance with the Local Government Finance Act 1992 and the Local Government Act 2003 is a legal requirement.

Risk Assessment: The S151 Officer is responsible for the administration of the financial affairs of the Council. Implementing this strategy and the CIPFA Code of Practice on Treasury Management manages the risk associated with the Council's treasury management activity.

1.0 Introduction

1.1 When the Cabinet agreed the overarching Treasury Management Strategy for 2015/16 Members were advised of the extremely low level of investment return being delivered over the last 2-3 years of around 0.5-0.6%. On the basis that many market commentators are expecting the base rate to remain at relatively low levels for the foreseeable future the Cabinet agreed for the Head of Finance to investigate a property investment fund specifically tailored to Local Authority deposits, such as the CCLA.

2.0 Background

2.1 The Head of Finance has had a few meetings with a representative from the CCLA, which stands for Churches, Charities and Local Authorities, the only bodies this Fund will transact with. On the 12 June 2015 the Head of Finance and the Accountant who deals with the day to day cash deposits and treasury planning at the Council had a further more detailed meeting with CCLA to establish a number of pertinent issues relating to a potential investment in the Fund, i.e. security, deposit lengths/amounts, return, access to funds, properties invested in, etc., in order to provide an update to the Cabinet prior to any decisions being reached.

3.0 The CCLA Commercial Property Fund

3.1 At the aforementioned meeting the Head of Finance and the Accountant asked a number of specific questions. These questions and the answers from CCLA are detailed below:

1 - Are there minimum investment periods/amounts?

No - but as this is a property investment fund it should be seen as a medium to long term investment decision. As the Fund is dealing in property acquisition, management and ultimately to sales, any investor would need to remain in the Fund for a reasonable period as there are one-off upfront costs associated with property purchasing – e.g. stamp duty and legal fees. However, the investor will get a share of the rental return from day one.

Minimum deposit of £25k initially and £10k for subsequent amounts.

2 - What rate of return has been delivered in the past few years?

Gross dividend yield at March 2015 was 4.86% net of fees – which are 0.65%. For information purposes the return in the previous 2 years was at March 2014 4.65% and March 2013 6.18%. Dividends are paid quarterly. Their independent financial specialist BNP Paribas indicates commercial capital appreciation of between 7-8% over the next 5 years.

3 - When can you make deposits/withdrawals?

Deposits/withdrawals are done at end of calendar month. Dividend payment dates are quarters ending January, April, July and October.

4 - How does the investment work?

When a Council makes a deposit it effectively buys a number of shares in the fund based on an initial “offer” price and any subsequent withdrawals will be valued at a bid “selling” price based on the prevailing market/property prices at that time.
This Fund can only be used by Councils in England, Wales, Scotland and NI. It now has 110 Councils who have invested circa £385m as at the 31 March 2015.

5 - How much notice is required and what penalties are applied for urgent withdrawals?

No penalties – withdrawals can be instant if enough cash is available to the Fund – they prefer a reasonable amount of notice as majority of fund tied up in properties earning a return.

6 - Is the return consistent – i.e. if you put £50k or £5m do you still receive the same level of annual return?

Yes – every investment will receive the same level of return irrelevant of the volume of investment made.

7 - Does everyone share in capital appreciation as well as a share of the rental income and how does this work?

Yes and is based on the “selling” price when the Council chooses to withdraw its investment.

8 - Who decides what properties you invest in?

CCLA have a specialist small property team of 3 chartered surveyors, who decide which properties, where, when and who to focus on: high quality, well diversified commercial and industrial property portfolio, delivering attractive income which is actively managed to “add value”. Strategic oversight is provided by the Chief Investment Officer, who was previously head of asset management at the Abbey. Any purchase needs to be ratified by the Fund’s trustee, the Local Authorities Mutual Investment Trust (LAMIT) a body controlled by the Local Government Association (LGA).

The current Commercial property portfolio currently stands at £326m – 32 units – spanning shops 9.4%, offices 35.6%, industrial/warehouses 26.2%, retail warehouses 18.0%, indirect 1.5% and cash 9.3%

Top ten property holdings – which total 53.6% of the Fund

- Beckton Retail Park, London
- Torrington Avenue, Coventry
- Science Park, Cambridge
- Stockley Park, London
- Fenchurch Street, London
- Iceni Centre, Warwick
- The Arena, Bracknell
- Magna Park, Lutterworth
- Albion Mills Retail Park, Wakefield
- Castle Boulevard, Nottingham

Vacancy rates currently 5.1% far better than industry average (and most of these voids are due to substantial refurbishment prior to new let). Also highly pro-active regarding which tenants they choose for their premises. A high percentage of tenants are from blue chip companies.
They get Dunn & Bradstreet to perform company searches/reports to grade all tenants.
All property values are carried out by an independent Valuer (currently this is carried out by BNP Paribas Real Estate).

9 - What would you need from us before we could start making investment(s)?

It is appreciated that a new or additional investor gives a few months notice (where possible/practical) of a decision to invest with an approximate amount and date of deposit so that the property team can build it into property purchasing decisions.

10 - How is your company structured/financed – i.e. are your losses underwritten by anyone? Or would we all share in the financial pain if you made an annual loss?

Losses are not underwritten but they have LAMIT as their trustee which is controlled by the LGA. The Fund is an unregulated collective investment scheme established under a Scheme approved by HM Treasury under Section 11 of the Trustee Investments Act 1961 and is subject to the provisions of a Trust Deed dated 6 April 1972 and a supplemental Trust Deed dated 13 September 1978. The Fund is an AIF and is managed as an AIFM in accordance with the FCA Rules and the AIFMD Legislation.

Note – AIFMD = Alternative Investment Fund Managers Directive.

CCLA Investment Management Ltd as a group currently manages more than £5bn on behalf of its charity, church and public sector clients. LAMIT owns 14% of the share capital with the remainder owned by charities, the church and executive directors.

11 - Any accounting issues with investment?

No - deposits are not treated as Capital and therefore any return can be directly credited to the General Fund or HRA depending on which account invested in the Fund. The investment will be treated as an available for sale financial asset in the Accounts under International Accounting Standard (IAS) 39 and the current CIPFA Code of Practice. Dividends paid will be recognised as “other investment income” within the Financing & Investment part of the Income & Expenditure Account.

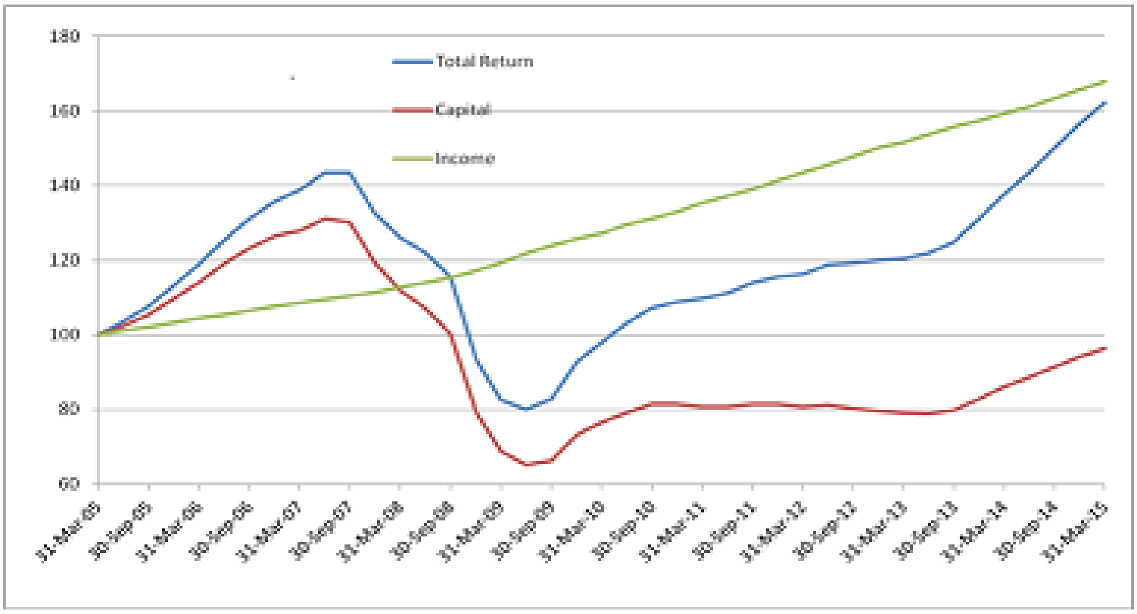
12 - Could you supply a reference of any SW Councils who are investing in the Fund?

A number of Councils in the South West have investments in the Fund – e.g. Plymouth, South Somerset DC, Taunton Deane BC, South Molton TC, etc.

4.0 Use of CCLA Commercial Property Fund

4.1 As eluded to earlier in the report, investing in any property fund is not for the short term and like any investment is not completely risk free. Clearly, property values go up and down and there will be periods of time when units are unoccupied and hence not generating a rental return. Due to the longer term nature of this kind of investment this is not an option that would be sensible if the Council didn't have some surplus funds that are potentially not required in the short term. However, upon reviewing both the rental return and capital appreciation that this Fund has delivered over the past 10 years (see graph/table below) it is recommended that an initial sum of £2.5m is deposited with this Fund on the 31 August 2015.

Graph showing last 10 years (return & capital appreciation).



4.2 If this investment is compared against our current level of return (4.86% vs 0.6%) then an additional £106.5k (excluding capital appreciation returns) per annum would be available to support current levels of service provision.

e.g £2.5m *4.86% = £121,500
£2.5m * 0.6% = £15,000

A difference of £106.5k per annum.

4.3 For Members information, an initial deposit of £2.5m has been recommended based on an examination of our existing Medium Term Financial Plan (MTFP) and after considering other longer term strategic goals/objectives (depot rationalisation/relocation, HRA property building programme, uncertainty around some major future capital receipts, etc.). Half yearly Treasury

Management reports show that the Council currently holds around £15m on deposit with various UK financial institutions at any one time. The Finance team have assessed that circa £3m of this amount could be invested for periods in excess of 1 year due to the nature of some of the Ear Marked Reserves that we hold for future funding commitments.

5.0 Conclusion

5.1 With the ever reducing level of funding settlements to all Councils which is likely to continue for at least the next 4 years coupled to historic low levels of UK base rates Mid Devon must look at alternative investment options that can increase its return, but as always remain cautious. It is considered that any investment in the CCLA commercial property fund is made for at least 3-5 years and based on the surplus cash balances currently held this is a financially viable proposition.

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Background Papers:

Circulation of the Report: Cllr Peter Hare-Scott, Management Team