Committee: Investment Committee	**Dated:** 21 May 2024
Subject: Treasury Management Update as at 31 March 2024	**Public**
Which outcomes in the City Corporation's Corporate Plan does this proposal aim to impact directly?	**All**
Does this proposal require extra revenue and/or capital spending?	**No**
If so, how much?	**£N/A**
What is the source of Funding?	**N/A**
Has this Funding Source been agreed with the Chamberlain's Department?	**N/A**
Report of: The Chamberlain	**For Discussion**
Report author: Adam Buckley – Chamberlain's Department	

Summary

This report provides a summary of the City of London Corporation's treasury management portfolio (investments) as at 31 March 2024. The report includes an update on the current asset allocation of the short-term investment portfolio and its performance. A monthly investment review report produced by the Corporation's treasury management consultants, Link Treasury Services, is included at Appendix 3.

The treasury position was last reviewed by the Investment Committee at the meeting on 12 February 2024, when they received a report outlining the treasury position as at 31 December 2023.

The treasury management investment portfolio had a market value of £901.2m as at 31 March 2024, which is a decrease of £103.9m from the balance previously reported as at as at 31 December 2023 (£1,005.1m).

The annual consumer price inflation rate in the UK rose by 3.2% in the 12 months to March 2024, down from 3.4% in February and 4.0% in January 2024. The Bank of England's Monetary Policy Committee (MPC) maintained the Bank Rate at 5.25% for a fifth consecutive time at its meeting on 21 March 2024, after the rate was also unchanged at the previous four meetings in February 2024, and December, November and September 2023. The markets view is that the rate has now peaked at 5.25%, with no cuts expected to materialise until Q3 of 2024. However, this sentiment remains volatile and may change in the near-term on the back of fresh central bank speakers, as well as both domestic and international data releases.

The increase in rates throughout 2023 allowed the Corporation to obtain higher yields across its asset allocations, though officers expect interest income to begin to decrease over 2024/25 if the MPC's current restrictive policy stance begins to loosen.

Recommendation

Members are asked to note the report.

Main Report

Background

1. The Investment Committee will receive an update on the treasury management portfolio at each meeting. Officers have compiled this report to provide additional context to the short-term investment portfolio as at 31 March 2024.

Current Position

2. The treasury management investment portfolio had a market value of £901.2m as at 31 March 2024, which is a decrease of £103.9m from the balance previously reported as at as at 31 December 2023 (£1,005.1m). This decrease is principally due to:-

   - business rates payments to central government (£315.8m);
   - business rates refunds (£35.6m);
   - expenditure on Major Projects (£19.9m); and
   - a property premium insurance payment (£17.0m); offset by
   - business rates income of £182.2m;
   - financial Investment drawdowns totalling £120.4m; and
   - receipts from lease premiums (£19.4m).

Asset Allocation

3. In accordance with the current Treasury Management Strategy Statement 2024/25, surplus cash is invested first and foremost with the aim of securing the Corporation's financial assets and secondly in line with the organisation's liquidity requirements (i.e. ensuring the cash is available when needed to meet the Corporation's spending obligations). Once these two objectives have been satisfied, the Corporation targets the best returns available in the sterling money markets.

4. A summary of the asset allocation by instrument type as at 31 March 2024, 31 December 2023 and 31 March 2023 is set out in Table 1.

Table 1: Asset allocation as at 31 March 2024

	31-Mar-2023		**31-Dec-2023**		**31-Mar-2024**	
	£m	**%**	**£m**	**%**	**£m**	**%**
Fixed Term Deposit	535.0	51%	490.0	49%	350.0	39%
Notice accounts	140.0	13%	90.0	9%	90.0	10%
Short Dated Bond Funds	151.0	15%	159.8	16%	159.0	18%
Ultra Short Dated Bond Funds	139.2	13%	145.1	14%	147.0	16%
Liquidity Fund	82.5	8%	120.2	12%	155.2	17%
Total	**1,047.7**	**100%**	**1,005.1**	**100%**	**901.2**	**100%**

5. As at 31 March 2024, most of the Corporation's cash balances are invested on a short term (under one year) basis with eligible banks, with the highest allocation via fixed term deposits (39%); a reduction of £140m from the previous reporting date, due to the decrease in the portfolio total as detailed at paragraph 2 above, and the increase in funds invested in Liquidity funds. Liquidity funds now make up around 17% of the portfolio; these balances are very liquid and can be accessed on the day. There have been no changes in the amount of funds that are invested in notice accounts, which make up 10% of the portfolio.

6. The ultra-short dated bond funds account for 16% of the treasury portfolio. These instruments are also very liquid (funds can be redeemed with two to three days' notice) but their market value is more volatile than liquidity funds. Ultra-short dated bond funds are suitable for surplus cash balances with an investment horizon of six months or more. The remaining portion of the portfolio (18%) continues to be invested in short dated bond funds. These funds are invested in investment grade credit instruments and currently have a duration (weighted average time to maturity) of around 3 years. The value of the short dated bond funds can be volatile in the short term and should only be used for surplus cash balances with an investment horizon of at least three years (In light of this volatility, the Treasury Management Strategy Statement (TMSS) was amended with effect from 1 April 2022, so that only City Fund would maintain exposure to the short dated bond funds).

7. Further analysis on the composition of the portfolio as at 31 March 2024 is provided in the Monthly Investment Report at Appendix 3. A summary of counterparty exposure is also included at Appendix 1, as well an *Economic, Social, & Governance (ESG)* checklist of Treasury Management Counterparties (excluding local authorities) at Appendix 2.

Performance

8. The Bank of England's Monetary Policy Committee (MPC) maintained the Bank Rate at 5.25% for a fifth consecutive time at its meeting on 21 March 2024, after the rate was also unchanged at the previous four meetings in February 2024, and December, November, and September 2023. The decision was passed with a vote of 8-1, with the one dissenting vote favouring a reduction in the Bank Rate by 0.25 percentage points, to 5%. This was the first time since September 2021 that no one on the Bank's committee, which decides rates, voted for an increase. The accompanying policy statement from the March MPC meeting maintained that rates will remain *"restrictive for sufficiently long*" and restrictive for an "*extended period"* until the risk of inflation becoming embedded above the 2% target dissipates.

9. As previously reported, the market expectation is that rates have peaked at 5.25%. Current market expectations for cuts remain somewhat volatile since the recent round of central bank policy meetings and subsequent key data releases. This has seen market expectations for the first cut push out from June (as expected prior to the February MPC meeting) to either August or September, with a following cut to 4.75% now expected in Q4 or Q1 2025. LINK, our investment consultants, are currently forecasting no further changes in the rate until a decrease in Q3 of 2024 to 4.75%, reaching 4.25% by the end of the year, followed by further rate cuts through 2025 reaching 3.00% by September 2025 where it is assumed to plateau.

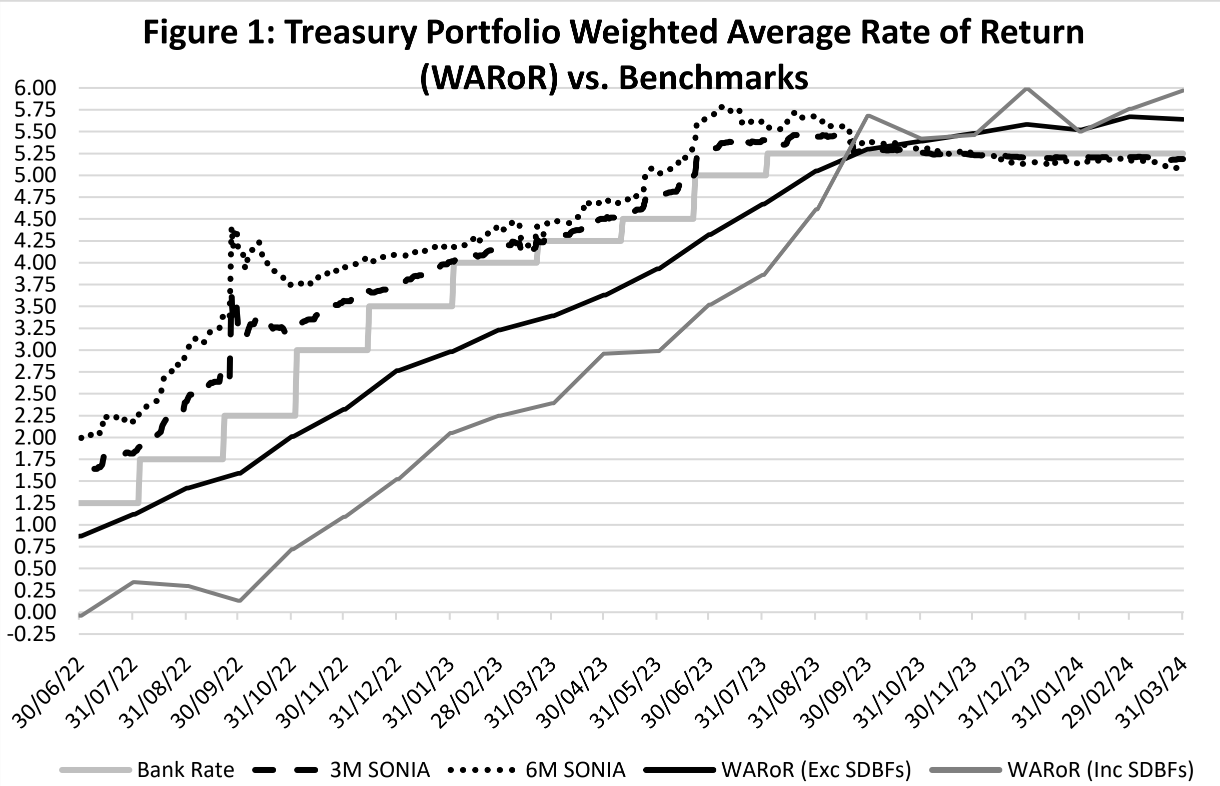
10. As the Bank Rate is the primary determinant of short-term interest rates in the UK, these changes impact the treasury investment portfolio, broadly in two ways:

    a. As yields increase, the capital value of the Corporation's bond fund investments decline (i.e. when interest rates increase, bond prices decrease and vice versa). These investments are exposed to interest rate risk which the Corporation manages by ensuring the allocations are consistent with a longer-term investment horizon for this minority portion of the portfolio.

    b. For the majority of the portfolio – which is invested in short term money market instruments – the increase in interest rates has meant that the

Corporation has benefitted from materially enhanced returns on new deposits and via the shorter term liquidity funds. A decrease in interest rates will result in reduced future returns from short term money market instruments.

11. These effects can be seen in the weighted average rate of return (WARoR) for the portfolio over the past 21 months and is shown in figure 1 below. In this chart, the two WARoR lines represent the level of returns achieved by the Corporation while the “dashed”, and solid Bank Rate, lines represent suitable performance comparators.



12. Sterling money market rates rose steadily in line with bank rate increases throughout most of 2022 and the first half of 2023, although they rose sharply at the end of September 2022 due to the Governments proposed fiscal stimulus plans, as investors demanded a higher risk premium and expected faster and higher interest rate rises to offset the perceived risk of the proposed significant tax cuts to the UK economy, as shown in figure 1 for 3-month and 6-month Sterling Overnight Index Average Rate (SONIA). Rates subsequently eased as the government reversed its plans and the Bank of England moved to quell market unease, though rates still trended upwards in line with expected bank rate increases in the first half of 2023 as the MPC moved to try and ease inflation. In the second half of 2023 Sterling money market rates began to ease, as the bank rate reached an assumed peak of 5.25% at the start of August 2023. Sterling money market rates began to decrease in the second half of 2023 as the market priced in a number of Bank Rate cuts over the next 12 months, though money market rates have steadied so far in 2024 as expectations on future price cuts have been pushed back further.

13. Returns on the Corporation’s short term investment portfolio excluding short dated funds trended upwards in 2023, as lower yielding deposits have matured and been replaced with new investments at a higher yield, as the Corporation capitalised on

the increase in interest rates. This is visible in the weighted average return excluding short dated bond funds above (which omits the two longer-term short dated bond fund investments in the portfolio). Rates were maintained at the end of 2023/24 as the restrictive monetary policy continued; however officers expect the current rate of return on the portfolio to decrease slightly over the start of 2024/25, as maturing deposits are likely to be reinvested at rates below those achieved in 2023/24, reflecting the market expectation that the MPC's current restrictive policy stance begins to loosen in 2024.

14. As month-to-month returns from the ultra-short and short dated bond fund investments can be volatile, for these instruments, officers have used the trailing 12 month total return to 31 March 2024 in calculating the portfolio returns displayed in figure 1 (i.e. the WARoR (Weighted Average Rate of Return)). Returns on these investments faced somewhat of a reality check at the start of 2024 following their historic end to 2023. Throughout most of 2023 bond prices weakened amid concerns that major central banks would keep increasing interest rates in order to quell inflation. This sentiment changed in November 2023, with growing optimism that inflation was cooling and interest rates would be lowered, and hence investors piled into bonds which drove up prices and triggered a powerfully rally at the end of 2023. However, in a partial reversal of the positive performance experienced over the final quarter of 2023, bond yields rose in Q1 2024 (meaning prices fell) as the likelihood of interest rate cuts as soon as March were pushed out until later in the year. Whilst inflationary pressures look to be subsiding, non-committal statements from central banks on the future trajectory of interest rates was enough to "spook" investors and hence some of the earlier gains have been given back.

15. To aid an effective assessment of performance, table 2 shows the historical return of the ultra-short and short dated bond fund investments on a total return basis over various time horizons under one year.

Table 2: Bond Fund Total Returns as at 31 March 2024

Fund	1 Month Return (29/02/2024 to 31/03/2024)	3 Month Return (31/12/2023 to 31/03/2024)	12 Month Return (31/03/2023 to 31/03/2024)
Federated Hermes Sterling Cash Plus Fund	0.40%	1.29%	5.19%
Aberdeen Standard Liquidity Fund Ultra Short Duration Sterling	0.50%	1.38%	5.57%
Payden Sterling Reserve Fund	0.63%	1.13%	5.63%
L&G Short Dated Sterling Corporate Bond Index Fund	1.47%	-0.94%	7.16%
Royal London Investment Grade Short Dated Credit Fund	1.49%	0.04%	7.78%

16. The most conservative fund (Federated) is listed first in table 2 and the longer-term investments (L&G and Royal London) are listed at the bottom to the table. The steadying in interest rates rises, especially since the end of July 2023,

compared to the sharp rise in September 2022, has had a positive effect on these short dated bond funds total returns over the last 12 months.

17. As noted above, the capital values of the bond funds – particularly the short-dated bond funds – can be volatile over the short term but they are expected to produce higher returns over the longer term. The Corporation deliberately allocates a small portion of the overall portfolio to these investments - an amount that can sustainably be invested over the medium term.

18. It should also be noted that fluctuations in the market value of investments do not impact the City Fund's revenue position owing to the existence of the IFRS 9 statutory override, which has been extended for a further 2 years until 31 March 2025, which English local authorities are required to implement, and which requires unrealised capital gains and losses to be charged to an unusable reserve on the balance sheet rather than reported via income and expenditure.

19. As interest rates rise the bond managers are able to reinvest the maturing bonds at a higher yield, thus raising the level of income in the portfolio, that is, income, rather than capital gains, has generally made up a greater part of the total return generated by these funds. The income (distribution) yield on the bond funds with Royal London and L&G are 4.62% and 3.80% respectively as at the end of March 2024.

20. Previously, interest generated from short-dated bond funds was automatically reinvested, either by accumulating more shares or by increasing the price of the shares already held. The interest from these investments is now distributed – in the 7 month period ended 31 March 2024 the interest distributed from these funds totalled £3.2m (Royal London: £1.78m and L&G: £1.42m).

<u>Interest on cash balances</u>

21. A summary of the interest on *average cash balances* (i.e. the returns on the treasury management investment portfolio) for the 2023/24 financial year (1 April 2023 to 31 March 2024) as applicable to City Fund and City's Estate is shown in Table 3 below.

Table 3: Interest on Cash Balances as at 31 March 2024

	2023/24 Original Budget	**2023/24 Actual**	**2023/24 Better / (Worse)**
	£'000	**£'000**	**£'000**
City Fund	**27,026**	**54,048**	**27,022**
City's Estate	**5,507**	**(714)**	**(6,221)**
Total City Fund & City's Estate Interest on average cash Balances	**32,533**	**53,334**	**20,801**

22. Income from interest on *average cash balances* exceeded the original budget by £20.8m principally due to higher than anticipated interest rates. The Bank of England base rate has increased from 3% in November 2022, when the original budget was set as part of the City of London Corporation's Medium term financial plan (MTFP), to 5.25% in August 2023 where it has remained.

23. As noted above in accordance with the Treasury Management Strategy Statement (TMSS) for 2023/24, due to the volatility of the income and capital returns of the 2 non-specified investments (i.e. the two short dated bond funds (SDBF's)), only City Fund maintains exposure to these, including the interest earned – overall, in 2023/24 City Fund received an interest allocation of 4.82% on *average cash balances* held totalling £54.0m.

24. For all other funds, including City's Estate (i.e. those excluding the two SDBF's) an interest allocation of 4.29% on *average cash balances* held was made for 2023/24. However, due to some re-phasing of City's Estate capital expenditure, the cash position was overdrawn for part of the year resulting in an interest charge of some £0.7m.

25. Going forward, the cashflow position of the individual funds (i.e. City's Estate, and City Fund) will be reviewed on a monthly basis to ensure that the planned drawdowns from either the sale of property (City Fund and City's Estate) or financial assets (City's Estate only) are sufficient to cover the liquidity requirements, and the funds remain in surplus. A separate paper is on the agenda today in relation to the proposed drawdowns.

<u>Cash Flow Forecast</u>

26. The City Fund's medium-term cash flow forecast is currently being reviewed along with all the capital projects, including the major projects, to develop a detailed forecast and appropriate funding strategy. Stanhope Capital LLP has been appointed to provide a strategic investment advisory function working alongside the City's in-house Corporate Treasury and Investment Property teams, to provide expert advice on the investment strategy/allocation advice between property and financial investments; and advice on how to secure the best rates of return for the differing requirements for City Find and City's Estate - a separate paper is on the agenda today in relation to this.

Conclusion

27. This report has provided a summary of the City of London Corporation's treasury management portfolio (investments) as at 31 March 2024. Cash is invested across a range of counterparties and instruments in accordance with the Corporation's current Treasury Management Strategy Statement 2024/25.

28. Since the Investment Committee last reviewed the treasury position as at 31 December 2023, the Bank of England's Monetary Policy Committee (MPC) maintained its Bank Rate at 5.25% at its meeting in March 2024. The markets view is that the rate has now peaked at 5.25%, with no cuts expected to materialise until Q3 of 2024.

29. The accompanying policy statement from the March MPC meeting maintained that rates will remain *"restrictive for sufficiently long"* and restrictive for an *"extended period"* until the risk of inflation becoming embedded above the 2% target dissipates.

30. The increase in sterling money market rates in 2023 allowed the Corporation to obtain higher yields, though officers expect the current rate of return on the portfolio to begin to decrease over 2024/25, reflecting the market expectation that the MPC's current restrictive policy stance begins to loosen in 2024.

31. The 12 month returns on the Corporation's Short dated bond fund investments remain strong, following a partial reversal in Q1 of 2024 of the positive

performance experienced over the final quarter of 2023, which witnessed a rise in bond yields (meaning prices fell) as the likelihood of interest rate cuts as soon as March were pushed out until later in the year. These investments are appropriate for surplus cash balances that can be invested sustainably over the medium term given the expectation for higher returns over this time horizon, and they continue to generate strong income returns. The interest from these investments is distributed, quarterly for RLAM and twice yearly for L&G.

Appendices

Appendix 1: Counterparty Exposure as at 31 March 2024
Appendix 2: Treasury Management Counterparties 2024/25: Economic, Social & Governance (ESG) Checklist
Appendix 3: Monthly Investment Analysis Review March 2024

Sarah Port
Group Accountant – Treasury & Investments
E: sarah.port@cityoflondon.gov.uk

Adam Buckley
Senior Accountant - Treasury
adam.buckley@cityoflondon.gov.uk

APPENDIX 1: COUNTERPARTY EXPOSURE AS AT 31 MARCH 2024

	Counter-party Limit £M	Total Invested as at 31 March 2024 £M	Average Rate of Return %
TOTAL INVESTED		**901.2**	**5.97%**
FIXED TERM DEPOSITS			
UK BANKS			
Goldman Sachs	100.0	70.0	5.89%
Santander	100.0	20.0	5.90%
NatWest	100.0	70.0	5.69%
		160.0	
FOREIGN BANKS			
Australia & New Zealand	100.0	30.0	5.57%
DBS Bank	100.0	10.0	5.33%
Toronto Dominion Bank	100.0	80.0	6.02%
United Overseas Bank	100.0	20.0	5.23%
		140.0	
LOCAL AUTHORITIES			
Central Bedfordshire Council	25.0	10.0	6.25%
Stockport Council	25.0	20.0	6.25%
Surrey County Council	25.0	20.0	6.50%
		50.0	
LIQUIDITY FUNDS			
Aberdeen SLI Liquidity Fund	100.0	25.0	5.26%
CCLA - Public Sector Deposit Fund	100.0	25.0	5.26%
Deutsche Global Liquidity Fund	100.0	30.0	5.25%
Federated Prime Liquidity Fund	100.0	35.0	5.29%
Invesco Sterling Liquidity Fund	100.0	40.2	5.31%
		155.2	
ULTRA SHORT DATED BOND FUNDS			
Payden Sterling Reserve Fund	100.0	65.3	5.63%
Aberdeen SLI Short Duration Fund	100.0	54.4	5.57%
Federated Sterling Cash Plus Fund	100.0	27.3	5.19%
		147.0	
SHORT DATED BOND FUNDS			
L&G	100.0	79.4	7.16%
Royal London	100.0	79.6	7.78%
		159.0	
NOTICE ACCOUNTS			
Australia and New Zealand 185 Days Account	100.0	45.0	5.43%
Santander 95 Days Account*	100.0	45.0	5.80%
		90.0	
TOTAL		**901.2**	

**Notice has been given on this account, with the full £45m returning on 07/06/2024*

APPENDIX 2: TREASURY MANAGEMENT COUNTERPARTIES 2024/25: ESG CHECKLIST

	Counterparty Name	UK (UK) or Foreign (f)	Net Zero Target Y/N	Date Net Zero Target	Interim Target	Signatory to PRI/TCFD	Which ones(s)?	Do they Publish ESG data? Y/N
	UK Banks and their wholly owned subsidiaries							
1	Barclays Bank PLC (NRFB)	UK	Y	2050	50% by 2030	Y	Both	Y
2	Barclays Bank UK PLC (RFB) - **Same as parent company above**							
3	Goldman Sachs International Bank	UK	Y	2050	N/A	Y	Both	Y
4	Handelsbanken PLC	Foreign	Y	2040	50% by 2030	Y	Both	Y
5	HSBC	UK	Y	2050	N/A	Y	Both	Y
6	HSBC Bank PLC (NRFB) - **Same as parent company above**							
7	Lloyds Bank Corporate Markets PLC (NRFB)	UK	Y	2050	50% by 2030	Y	TCFD	Y
8	Lloyds Bank PLC (RFB) - **Same as parent company above**							
9	Bank of Scotland	UK	Y	2050	50% by 2030	Y	TCFD	Y
10	NatWest Markets PLC (NRFB)	UK	Y	2050	50% by 2030	Y	TCFD	Y
11	National Westminster Bank PLC (RFB) - **Same as parent company above**							
12	The Royal Bank of Scotland PLC (RFB) - **Same as parent company above**							
13	Santander	UK	Y	2050	N/A	Y	Both	Y
	Building Societies							
14	Nationwide	UK	Y	2050	Separated by Scope	Y	TCFD	Y
15	Yorkshire	UK	Y	2050	Separated by Scope	Y	TCFD	Y
16	Coventry	UK	Y	2040	Separated by Scope	Y	TCFD	Y
17	Skipton	UK	Y	2050	Separated by Scope	Y	TCFD	Y
18	Leeds	UK	Y	2050	N/A	N	N/A	Y
	Foreign Banks							
19	Australia and New Zealand Banking Group	Foreign	Y	2050	N/A	Y	Both	Y
20	National Australia Bank Ltd	Foreign	Y	2050	N/A	Y	TCFD	Y
21	Bank of Montreal	Foreign	Y	2050	N/A	Y	TCFD	Y
22	Royal Bank of Canada	Foreign	Y	2050	N/A	Y	TCFD	Y

	Counterparty Name	UK (UK) or Foreign (f)	Net Zero Target Y/N	Date Net Zero Target	Interim Target	Signatory to PRI/TCFD	Which ones(s)?	Do they Publish ESG data?
23	Toronto-Dominion Bank	Foreign	Y	2050	N/A	Y	TCFD	Y
24	Landesbank Hessen-Thueringen Girozentrale (Helaba)	Foreign	N	NA	N/A	N		N
25	Cooperatieve Rabobank U.A.	Foreign	N	NA	N/A	N		N
26	DBS Bank Ltd	Foreign	Y	2050	N/A	Y	TCFD	Y
27	United Overseas Bank Ltd.	Foreign	Y	2050	N/A	Y	TCFD	Y
28	Skandinaviska Enskilda Banken AB	Foreign	Y	2050	N/A	Y	TCFD	Y
29	Swedbank AB	Foreign	Y	2050	N/A	Y	TCFD	Y
	Svenska Handelsbanken AB - Same a parent company (4)							
	Money Market Funds - Parent Companies Used (MMFs don't have net-zero targets)							
30	CCLA - Public Sector Deposit Fund	UK	N					
31	Federated Hermes Short-Term Sterling Prime Fund*	Foreign	Y	2050	N/A	Y	Both	Y
32	Aberdeen Sterling Liquidity Fund	UK	Y	2050	N/A	Y	Both	Y
33	Invesco Liquidity Funds Plc - Sterling Liquidity Portfolio	Foreign	N	2050	N/A	Y	Both	Y
34	DWS Deutsche Global Liquidity Series Plc – Sterling Fund	Foreign	Y	2050	N/A	Y	Both	Y
	Ultra Short Dates Bonds							
35	Payden Sterling Reserve Fund	UK	Y	2050	Based on engagement and other factors	Y	Both	Y
36	Federated Hermes Sterling Cash Plus Fund* - **Same as Parent company (31)**							
37	Aberdeen Standard Investments Short Duration Managed Liquidity Fund** **- Same as parent company (32)**							
	Short Dated Bond Funds							
38	Legal and General Short Dated Sterling Corporate Bond Index Fund	UK	Y	2050	50% by 2030	Y	Both	Y
39	Royal London Investment Grade Short Dated Credit Fund	UK	Y	2050	50% by 2030	Y	Both	Y