FINANCE, AUDIT AND RISK COMMITTEE
8 MARCH 2021

***PART 1 – PUBLIC DOCUMENT**

TITLE OF REPORT: THIRD QUARTER INVESTMENT STRATEGY (CAPITAL AND TREASURY) REVIEW 2020/21

REPORT OF THE SERVICE DIRECTOR - RESOURCES

EXECUTIVE MEMBER: FINANCE AND I.T.

CURRENT COUNCIL PRIORITY: RESPONSIVE AND EFFICIENT

NEW COUNCIL PRIORITY: ENABLE AN ENTERPRISING AND CO-OPERATIVE ECONOMY

1 EXECUTIVE SUMMARY

1.1 To update Cabinet on progress with delivering the capital and treasury strategy for 2020/21, as at the end of December 2020.

1.2 To update Cabinet on the impact upon the approved capital programme for 2020/21 – 2030/31. The current estimate is a decrease in spend in 2020/21 of £1.6million and an increase in spend in future years of £2.0million. The most significant individual changes relate to £0.397M Property Improvements, £0.352M Lairage Lift Refurbishment, £0.350M Resurface Lairage Car Park and £0.265M Community Facilities Refurbishment. These are being reprofiled into future years. In addition, £0.320M from the Provide Housing at Market Rents budget has been reprofiled into 2020/21 from 2021/22.

1.3 To inform Cabinet of the Treasury Management activities in the first nine months of 2020/21. The current forecast is that the amount of investment interest expected to be generated during the year is £0.185million. This remains unchanged from the estimate reported in the second quarter monitoring report.

2. RECOMMENDATIONS

2.1 That Cabinet notes the forecast expenditure of **£2.354million** in 2020/21 on the capital programme, paragraph 8.3 refers.

2.2 That Cabinet approves the adjustments to the capital programme for 2020/21 onwards as a result of the revised timetable of schemes detailed in table 2, increasing the estimated spend in 2021/22 by **£1.102million.**

2.3 That Cabinet notes the position of the availability of capital resources, as detailed in table 3 paragraph 8.6 and the requirement to keep the capital programme under review for affordability.

2.4 That Cabinet approve the £0.050million budget to refurbish the Gym Floor at the North Herts Leisure Centre be reprofiled into 2020/21. The budget has been approved to spend in 2021/22 but with the Leisure Centre closed due to Covic-19 there's an opportunity to bring this work forward and avoid closing the gym once Covid-19 restrictions have been lifted.

3. REASONS FOR RECOMMENDATIONS

3.1 Cabinet is required to approve adjustments to the capital programme and ensure the capital programme is fully funded.

3.2 To ensure the Council's continued compliance with CIPFA's code of practice on Treasury Management and the Local Government Act 2003 and that the Council manages its exposure to interest and capital risk.

4. ALTERNATIVE OPTIONS CONSIDERED

4.1 Options for capital investment are considered as part of the Corporate Business Planning process.

4.2 The primary principles governing the Council's investment criteria are the security of its investments (ensuring that it gets the capital invested back) and liquidity of investments (being able to get the funds back when needed).

After this the return (or yield) is then considered, which provides an income source for the Council. In relation to this the Council could take a different view on its appetite for risk, which would be reflected in the Investment Strategy. In general, greater returns can be achieved by taking on greater risk. Once the Strategy has been set for the year, there is limited scope for alternative options as Officers will seek the best return that is in accordance with the Investment Strategy.

5. CONSULTATION WITH RELEVANT MEMBERS AND EXTERNAL ORGANISATIONS

5.1 Consultation on the capital expenditure report is not required. Members will be aware that consultation is incorporated into project plans of individual capital schemes as they are progressed.

5.2 There are quarterly updates with the Authority's Cash Manager, Tradition and regular meetings with Treasury advisors (Link).

6. FORWARD PLAN

6.1 This report contains a recommendation on a key Executive decision that was first notified to the public in the Forward Plan on the 5th February 2021.

7. BACKGROUND

7.1 In February 2020, Council approved the Integrated Capital and Treasury Strategy for 2020/21 to 2029/30. To be consistent with the strategy, the monitoring reports for Capital and Treasury are also integrated.

7.2 The Medium Term Financial Strategy for 2020 to 2025 confirmed that the Council will seek opportunities to utilise capital funding (including set aside receipts) for 'invest to save' schemes and proposals that generate higher rates of return than standard treasury investments. This is one way the Council will allocate resources to support organisational transformation that will reduce revenue expenditure.

7.3 Link Asset Services Ltd were first contracted to provide Treasury advice for the financial year 2012/13 and this arrangement has been extended until 2022/23. The service includes:

- Regular updates on economic and political changes which may impact on the Council's borrowing and investment strategies
- Information on investment counterparty creditworthiness
- Technical updates
- Access to a Technical Advisory Group.

8. RELEVANT CONSIDERATIONS

8.1 The Council has £117.0 million of capital assets that it currently owns. The Investment Strategy set out the reasons for owning assets that are not for service delivery, including an assessment of Security, Liquidity, Yield and Fair Value. There have been no significant changes in relation to these since the Strategy was set.

Capital Programme 2020/21

8.2 The full capital programme is detailed in Appendix A and shows the revised costs to date, together with the expected spend from 2020/21 to 2030/31 and the funding source for each capital scheme.

8.3 Capital expenditure for 2020/21 is estimated to be **£2.354million**. This is a reduction of **£1.583million** on the forecast in the 2nd quarter report (reported to Cabinet on 15th December 2020). The decrease in spend in 2020/21 is largely due to the reprofiling of projects into 21/22.Table 1 below details changes to capital programme.

Table 1- Current Capital Estimates

	2020/21 £M	2021/22 £M	2022/23 to 2030/31 £M
Original Estimates approved by Full Council February 2020	**9.357**	**5.405**	**26.650**
Changes approved by Cabinet in 3rd Qrt 2019/20	3.801	0	**0**
Changes approved by Cabinet in 2019/20 Capital Outturn report	0.277	0	**0**
Revised Capital estimates at start of (2020/21)	**13.435**	**5.405**	**26.650**
Changes approved by Cabinet in Covid-19 Financial Impacts report 21/07/20	-2.809	1.713	1.096
Executive Member – Finance and I.T. approved additional Expenditure on 4 schemes	0.180	0	0
Changes at Q1	-0.287	0.296	0
Executive Member – Finance and I.T. approved additional Expenditure on 3 schemes	0.108	0	0

	2020/21 £M	2021/22 £M	2022/23 to 2030/31 £M
Changes approved by Council in Covid-19 Financial Impacts report 24/09/20	0.350	0	0
Changes at Q2	-7.040	7.022	0
Changes approved by Council	0.071	0.283	1.287
Changes at Q3	-1.654	1.102	0.537
Current Capital Estimates	**2.354**	**15.821**	**29.570**

8.4 Table 2 lists the schemes in the 2020/21 Capital Programme that will start or continue in 2021/22:

Table 2: Scheme Timetable Revision:
(Key: - = reduction in capital expenditure, + = increase in capital expenditure)

Scheme	2020/21 Working Budget £'000	2020/21 Forecast £'000	Difference £'000	Reason for Difference	Estimated impact on 2021/22 onwards £'000
Property Improvements	472	75	-397	Some capital works have been completed this year, but limited staff resource have been focused on reactive repairs, compliance and additional COVID-19 related compliance works. These capital improvements will be completed in 2021/22 (or later).	397
Lairage Lifts Refurbishment	352	0	-352	A review of the multi-storey car parks meant that there was a hold put on non urgent works . This delayed the start of the project. A specification and tender exercise has now been completed and a contractor appointed, with an anticipated start in late May 2021.	352
Resurface Lairage Car Park	350	0	-350	Options for surface treatments were put forward	350

Scheme	2020/21 Working Budget £'000	2020/21 Forecast £'000	Difference £'000	Reason for Difference	Estimated impact on 2021/22 onwards £'000
				and a budget approved. However there has been insufficient time to specify, tender and complete the works before the winter of 2020. Works are planned for summer 2021.	
Community Facilities Refurb	523	258	-265	The Community Facilities Capital Grant fund is demand lead. There has been a reduction in applications, which is probably related to Covid-19. It is expected that further applications will be received in 2021/22.	265
Letchworth Multi Storey Parapet / Soffit / Decoration	134	0	-134	Delays with the tender exercise have resulted in works now planned for summer 2021.	134
Museum Storage Solution	100	17	-83	Having explored the initial feasibility and put together a draft layout of the museum storage facility required, we are currently exploring what to do with the rest of the site to make the overall plot and development as financially viable as possible. As a result, this project is on pause until we decide what next steps to take.	83
Leisure Condition Survey	87	5	-82	Due to Covid-19 it has not been possible to carry out the majority of items included in the condition survey for 2020 which will now commence in 2021/22	82

Scheme	2020/21 Working Budget £'000	2020/21 Forecast £'000	Difference £'000	Reason for Difference	Estimated impact on 2021/22 onwards £'000
Sprung Floor Hitchin Town Hall	75	0	-75	Conditional Listed Building Consent has been awarded for this project and the contractor is preparing a submission to discharge the condition. The project will then be able to move forward and will take around 4 weeks. However, we have been asked to host a Covid-19 rapid testing site at HTH for the next 6 weeks, starting in February and as such, the project will not be completed within this financial year.	75
Mrs Howard Hall Boiler / Windows	63	0	-63	This funding is linked to the completion of a new lease. Due to various factors (particularly Covid-19 impacts) the lease will not be finalised until 2021/22.	63
Museum Services Development	48	0	-48	This budget was intended for a canopy to the Terrace Area. Professional advice has determined that the building structure was not strong enough for the proposed canopy design. Alternative options will now be investigated, and if possible will be implemented in 2021/22. It is possible that there will not be a practical solution. Unfortunately, this would mean loss of income in the winter and during poor weather.	48

Scheme	2020/21 Working Budget £'000	2020/21 Forecast £'000	Difference £'000	Reason for Difference	Estimated impact on 2021/22 onwards £'000
Hitchin Swim Centre Outdoor Boiler Replacement	40	0	-40	Due to Covid-19 the outdoor pool did not open in 2020 and the project to replace the boiler will be put on hold until 2021	40
Letchworth Outdoor Pool Boiler	40	0	-40	Due to Covid-19 the outdoor pool did not open in 2020 and the project to replace the boiler will be put on hold until 2021	40
Provide Housing at Market Rents	30	350	320	£2.947M of this budget was approved for reprofiling into 21/22 at the 2nd quarter. Work at Harkness Court has progressed a lot more quickly than previously anticipated, so increasing the spend in 2020/21 (rather than 2021/22).	-320
Total Minor (under £25k) slippage on other projects	130	88	-30		30
Total Revision to Budget Profile			**-1.639**		**1.639**

8.5 There are also minor changes to the overall forecast cost of schemes in 2020/21 with the revised estimate being a decrease of £0.015million

8.6 Table 3 below shows how the Council will fund the 2020/21 capital programme.

Table 3: Funding the Capital Programme:

	2020/21 Balance at start of year £M	2020/21 Forecast Additions £M	2020/21 Forecast Funding Used £M	2020/21 Balance at end of year £M
Useable Capital Receipts and Set-aside Receipts	7.455	1.105	(2.118)	6.442

	2020/21 Balance at start of year £M	2020/21 Forecast Additions £M	2020/21 Forecast Funding Used £M	2020/21 Balance at end of year £M
S106 receipts			(0.148)	
Other third party grants and contributions			(0.088)	
Planned Borrowing			0	
Total			**(2.354)**	

8.7 The availability of third party contributions and grants to fund capital investment is continuously sought in order to reduce pressure on the Council's available capital receipts and allow for further investment. Additional capital receipts are dependent on selling surplus land and buildings. Ensuring that the Council gets best value from the disposal of land and buildings can take a long time and therefore the amounts that might be received could be subject to change. This will be kept under review throughout the year.

8.8 The Council's Capital Financing Requirement (CFR) at 31st March 2020 was negative £5.60 million. Based on current forecasts it will remain negative during 2020/21, which means that the Council does not have a need to borrow to fund capital spend.

Treasury Management 2020/21

8.9 The Council invests its surplus cash in accordance with the Investment Strategy (see paragraph 4.2). This surplus cash is made up of capital funding balances, revenue general fund balance, revenue reserve and provisions balances and variations in cash due to the timing of receipts and payments. During the first nine months, the Council had an average investment balance of £44.4 million and invested this in accordance with the treasury and prudential indicators as set out in the Integrated Capital and Treasury Management Strategy and in compliance with the Treasury Management Practices. The approved investment limits within the Investment Strategy were breached during the quarter ended 31 December 2020.The limit on investments placed with Building Societies was exceeded by £2.0 million for 19 days in October. Measures have been put in place to ensure limits are not exceeded again.

8.10 During the year the Council has had higher than expected cash balances due to the various grant funding that it has been given by Government to pass on to businesses. Even though every effort has been made to pass the money on to businesses as quickly as possible, there has inevitably been a delay between receipt and payment. There have also been tranches of grant where the amount received has exceeded the amounts eligible for payment. Balances have also been higher due to the delays in capital spend.

These have both been partially off-set by revenue costs and reduced income related to Covid-19. It has been necessary to keep the business grant funding very liquid, and therefore there has been an increase in short-term investments with the Debt Management Office.

8.11 The Council generated £0.161M of interest during the first nine months of 2020/21. The average interest rate on all outstanding investments at the 31st December was 0.54%. Interest rates have continued to decline since the second quarter report with some banks offering 0%. The Government's Debt Management Office (DMO) has recently been offering negative rates for very short term deposits. Consequently any new investments are yielding significantly less than 0.54%, usually 0.1% or less. Based on current investments and forecasts of interest rates and cash balances for the remainder of the year, it is forecast that the Council will generate £0.185 million of interest over the whole of 2020/21.

8.12 As at 31 December 2020 the split of investments was as shown in the table below. There were no investments with non-UK banks during the quarter. There has been a general downgrading of banks which has meant a couple of non-UK banks have been temporarily removed from the Council's approved counter party list:

Banks	19%
Building Societies	27%
Government	12%
Local Authorities	36%
Money Market Fund (MMF)	6%

8.13 The level of risk of any investment will be affected by the riskiness of the institution where it is invested and the period that it is invested for. Where an institution has a credit rating this can be used to measure its riskiness. This can be combined with the period remaining on the investment to give a historic risk of default percentage measure. The table below shows the Historic Risk of Default for outstanding investments at 31 December 2020. The most risky investment has a historic risk of default of 0.178%. It should also be noted that in general the interest rate received is correlated to the risk, so the interest income received would be less if it took on less risk.

Borrower	Principal Invested £M	Interest Rate %	Credit Rating	Days to Maturity at 31 Dec	Historic Risk of Default %
Public Sector Deposit Fund (MMF)	3.0	0.09	AAA	Call	0
Santander UK	2.5	0.03	A	4	0.001
DMO (Government)	6.0	-0.01	AA-	4	0
Barclays Bank	1.5	0.01	A	15	0.002
West Brom Bldg Sob	1.0	0.08	*	18	0.032
Barclays Bank	1.5	0.01	A	19	0.003
Principality Bldg Soc	1.0	0.06	BBB+	19	0.008
Principality Bldg Soc	1.0	0.06	BBB+	21	0.009
Skipton Bldg Soc	2.0	0.1	A-	21	0.009
Marsden Bldg Society	1.5	1.6	*	22	0.010
Liverpool City Council	2.0	0.35	AA-	27	0.002
Fife Council	1.0	0.4	AA-	29	0.002
Principality Bldg Soc	1.0	0.16	BBB+	39	0.016
Surrey Heath Borough Council	3.0	0.18	AA-	53	0.003
Lloyds Bank	2.0	0.1	A+	67	0.013
Skipton Bldg Soc	1.0	0.2	A-	76	0.031
Bank of Scotland	1.0	0.1	A+	81	0.013
Lloyds Bank	1.0	0.05	A+	81	0.004
Leeds Bldg Soc	2.0	0.14	A-	82	0.011
Conwyn County Borough Council	2.0	0.08	AA-	110	0.007
Eastleigh Borough Council	2.0	0.05	AA-	137	0.009
Slough Borough Council	2.0	1.0	AA-	148	0.010
Monmouthshire Bldg Soc	1.0	1.5	*	148	0.178
Slough Borough Council	1.0	0.1	AA-	152	0.010
Monmouthshire County Council	1.0	0.25	AA-	169	0.011
Darlington Bldg Soc	1.0	0.35	*	189	0.083
London Borough of Southwark	2.0	0.2	AA-	217	0.014
Newcastle Bldg Soc	1.0	0.2	*	239	0.105
Blackpool Council	2.0	0.32	AA-	347	0.023
	50.0	0.54			

* Unrated Building Societies Historic Risk of Default is based on a Fitch (a credit rating agency) rating of BBB.
DMO and Local Authority credit ratings are the UK credit rating.

9. LEGAL IMPLICATIONS

9.1 Cabinet's terms of reference under 5.6.7 specifically includes "to monitor expenditure on the capital programme and agree adjustments within the overall budgetary framework". The Cabinet also has a responsibility to keep under review the budget of the Council and any other matter having substantial implications for the financial resources of the Council. By considering monitoring reports throughout the financial year Cabinet is able to make informed recommendations on the budget to Council. The Council is under a duty to maintain a balanced budget.

9.2 Section 151 of the Local Government Act 1972 states that:
"every local authority shall make arrangements for the proper administration of their financial affairs and shall secure that one of their officers has responsibility for the administration of those affairs."

9.3 Asset disposals must be handled in accordance with the Council's Contract Procurement Rules.

9.4 The Prudential Indicators comply with the Local Government Act 2003.

10. FINANCIAL IMPLICATIONS

10.1 The main financial implications are covered in section 8 of the report.

10.2 The Authority operates a tolerance limit on capital projects that depends on the value of the scheme and on this basis over the next ten-year programme it should be anticipated that the total spend over the period could be £4.393million higher than the budgeted £47.745million.

10.3 The capital programme will need to remain under close review due to the limited availability of capital resources and the affordability in the general fund of the cost of using the Council's capital receipts. When capital receipts are used and not replaced the availability of cash for investment reduces. Consequently interest income from investments reduces. £1.0million currently earns the Authority approximately £1k per year in interest. The general fund estimates are routinely updated to reflect the reduced income from investments. When the Capital Financing Requirement (CFR) reaches zero the Council will need to start charging a minimum revenue provision to the general fund for the cost of capital and will need to consider external borrowing for further capital spend. The CFR at the 31 March 2020 was negative £5.6million. This may turn positive next year if the capital programme is fully spent.

10.4 The Council also aims to ensure that the level of planned capital spending in any one year matches the capacity of the organisation to deliver the schemes to ensure that the impact on the revenue budget of loss of cash-flow investment income is minimised.

11. RISK IMPLICATIONS

11.1 The inherent risks in undertaking a capital project are managed by the project manager of each individual scheme. These are recorded on a project risk log which will be considered by the Project Board (if applicable). The key risks arising from the project may be recorded on Pentana (the Council's Performance & Risk management software). Some of the major capital projects have been included in the Council's Corporate Risks (such as the new North Hertfordshire Museum). The Corporate Risks are monitored by the Finance, Audit and Risk Committee and Cabinet.

11.2 Risks associated with treasury management and procedures to minimise risk are outlined in the Treasury Management Practices document, TMP1, which was adopted by Cabinet in July 2003 and is revisited annually as part of the Treasury Strategy review. The risk on the General Fund of a fall of investment interest below the budgeted level is dependent on banks and building societies need for borrowing.

12. EQUALITIES IMPLICATIONS

12.1. In line with the Public Sector Equality Duty, public bodies must, in the exercise of their functions, give due regard to the need to eliminate discrimination, harassment, victimisation, to advance equality of opportunity and foster good relations between those who share a protected characteristic and those who do not.

12.2 There are no direct equalities implications directly arising from the adoption of the Capital Programme for 2020/21 onwards. For any individual new capital investment proposal of £50k or more, or affecting more than two wards, an equality analysis is required to be carried out. This will take place following agreement of the investment proposal.

13. SOCIAL VALUE IMPLICATIONS

13.1. The Social Value Act and "go local" requirements do not apply to this report.

14. ENVIRONMENTAL IMPLICATIONS

14.1. There are no known Environmental impacts or requirements that apply to recommendations of this report. The projects at section 8.4 may have impacts that contribute to an adverse impact. As these projects go forward, an assessment will be made where necessary.

15. HUMAN RESOURCE IMPLICATIONS

15.1 There are no direct human resource implications.

16. APPENDICES

16.1 Appendix A - Capital Programme Detail including Funding 2020/21 onwards.
Appendix B - Treasury Management Update.

17. CONTACT OFFICERS

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18. BACKGROUND PAPERS

18.1 Investment Strategy (Integrated Capital and Treasury Strategy)
https://democracy.north-herts.gov.uk/documents/s9835/Appendix%20A%20-%20Investment%20Strategy.pdf