REPORT CONSIDERED BY CABINET AT THE MEETING HELD ON 29 JUNE 2021

TITLE OF REPORT: INVESTMENT STRATEGY (CAPITAL AND TREASURY) END OF YEAR REVIEW 2020/21

REPORT OF THE SERVICE DIRECTOR - RESOURCES

EXECUTIVE MEMBER: FINANCE AND I.T.

COUNCIL PRIORITY: ENABLE AN ENTERPRISING AND CO-OPERATIVE ECONOMY

1 EXECUTIVE SUMMARY

1.1 As at the end of financial year 2020/21, there is a reduction in Capital spend compared to quarter 3 of **£0.521million**. The majority of this change is due to revisions to the profile of planned project spend, with **£0.527million** that will now instead be incurred in 2021/22.

1.2 During the year the Council has generated **£0.184million** of interest from its investments. This is slightly below the budgeted total of £0.185million. The Council continued to invest in smaller Building Societies (subject to checks that compare the size of the Society with that of the investment).

1.3 The Council has repaid £0.018million of borrowing during the year as it has matured. The Council has £0.405million of remaining borrowing. This borrowing is at a fixed rate for a fixed period. The premium incurred from repaying this borrowing early means that it is not worthwhile to do so.

1.4 The Council complied with its legislative and regulatory requirements throughout the year.

1.5 The forecast for 2021/22 is that investment income will continue to reduce due to market conditions and the use of cash balances to fund the capital programme. To attempt to offset the reduction in interest received from short fixed term investments, the Council is looking at options to diversify its portfolio by investing in longer term, Property Funds and Multi Asset Income Funds. Paragraph 8.20 refers.

2. RECOMMENDATIONS

2.1 That Cabinet notes expenditure of **£1.883million** in 2020/21 on the capital programme, paragraph 8.3 refers, and in particular the changes detailed in table 3 which resulted in a net increase on the working estimate of **£0.001million**.

2.2 That Cabinet approves the adjustments to the capital programme for 2020/21 as a result of the revised timetable of schemes detailed in table 2, increasing the estimated spend in 2021/22 by **£0.522million** (£0.527milion re-profiled from 2020/21 and £0.005million from 2021/22 re-profiled into 2020/21).

2.3 That Cabinet notes the position of the availability of capital resources, as detailed in table 4 paragraph 8.8 and the requirement to keep the capital programme under review for affordability.

2.4 That Cabinet approves the application of **£1.224million** of capital receipts towards the 2020/21 capital programme and the drawdown of £0.417million from set aside receipts, paragraph 8.8 refers.

2.5 Cabinet is asked to note the position of Treasury Management activity as at the end of March 2021.

2.6 Cabinet is asked to recommend this report to Council and ask Council to:

1) Approve the actual 2020/21 prudential and treasury indicators.
2) Note the annual Treasury Report for 2020/21.

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.

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 £129.0 million of capital assets that it currently owns. This has increased from £117.0 million as at 31 March 2020.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 actual spend from 2020/21 to 2030/31 and the funding source for each capital scheme.

8.3 The Outturn Capital expenditure for 2020/21 is **£1.883million**. This is a reduction of **£0.521million** on that reported at the end of the third quarter. The decrease in spend is largely due to re-profiling spend into future years and underspend on projects. Table 1 below details the changes from what was reported at Quarter 3.

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
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 11/02/21	0.071	0.283	1.287
Changes at Q3	-1.604	1.052	0.537
Changes since Q3 (as detailed in this report)	-0.521	0.522	0
Outturn 2021/21	**1.883**	**16.293**	**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 Outtrun £'000	Difference £'000	Reason for Difference	Estimated impact on 2021/22 onwards £'000
Provide Hsg at Market Rents	350	225	-125	Due to the refurbishment of Harkness Court taking longer than originally anticipated, the remaining money will be spent in 2021/22. The	125

Scheme	2020/21 Working Budget £'000	2020/21 Outtrun £'000	Difference £'000	Reason for Difference	Estimated impact on 2021/22 onwards £'000
				estimate completion date is June 2021.	
Renovate Howard Park Play Area	75	0	-75	Delay was due to supply issues with the new equipment from Europe. If we had gone ahead it would have meant that the play area would be closed for the renovation at the potentially busiest part of the year as the splash pads open on the 1st May. We have therefore decided to hold back the works until September when the splash parks close and the schools have returned.	75
Email Encryption Software	45	4	-41	This piece of work has been delayed while alternative options for enhanced email encryption are explored, this will be reviewed in Q3/Q4 once our services have migrated to the cloud. As part of this review we are also seeking input from our auditors (BDO) on encrypting data in the cloud.	41
NH Museum Platform Lift	40	0	-40	A potential low cost solution has been found to repairing the lifts (revenue spend) before spending this budget on completely new lifts. We are exploring this option currently, but if this proves unsuccessful we will still require the budget to invest in new lifts.	40
Private Sector Grants	60	30	-30	Spend on this budget is demand led. Due to last year's lock down restrictions and the fact that those residents who qualify for these grants are in the main from the vulnerable groups, a number of cases were cancelled by the residents as they did not wish people	30

Scheme	2020/21 Working Budget £'000	2020/21 Outtrun £'000	Difference £'000	Reason for Difference	Estimated impact on 2021/22 onwards £'000
				inspecting their properties during the Covid crisis. As part of the process the required works and residents' financial situation must be diligently verified before a grant is approve. As a result of a number of cancellations we did not manage to process the projected number of cases	
Total Minor (under £25k) slippage on other projects	938	727	-211		211
Total Revision to Budget Profile			**-522**		**522**

8.5 The Council received £750k grant for improving the energy performance of park homes. The BEIS average cap per unit is £10k. Following Grenfell, the fire officer advice is we use a mineral core to external cladding rather than an expanded polystyrene core. This pushes the cost above £10k per unit so it is proposed that the £30K slippage form the Private Sector Grants is used to finance the expenditure that is not covered by the grant. This is covered by the proposed 2021/22 spend detailed in the table above.

8.6 There are also changes to the overall costs of schemes in 2020/21. These changes total a net increase of £0.001million and are detailed in Table 3.

<u>Table 3: Changes to Capital Schemes Commencing in 2020/21</u>:
(Key: - = reduction in capital expenditure, + = increase in capital expenditure)

Scheme	202/21 Working Budget £'000	2020/21 Spend £'000	Difference £'000	Comments
Section 106 Project – All weather Hockey pitch at Royston	129	0	-129	The £129K budget is for the provision of an All Weather Hockey Pitch on the Heath, Royston. As the Heath is a public open space permission will not be granted to create an enclosed area on the Heath. Officers are looking to see if the S106 funds can be used at an alternative location in Royston. Also in order for the scheme to go ahead

Scheme	202/21 Working Budget £'000	2020/21 Spend £'000	Difference £'000	Comments
				additional external funding is still to be secured.
Disabled Facilities Grants	50	82	32	In 2019/20 the Council spent 100% of its allocated Disabled Facilities Grant. In 2020/2021, a discretionary payment was made to allow a specific project to be undertaken in consultation with the Executive Member. There has also been continued pressure on the budget from high demand for adaptations such as stairlifts and accessible bathrooms. Additional funding was provided by the Council to the Herts Home Improvement Agency (HCC) to ensure these works were able to be undertaken within the financial year. This funding came from amounts set aside from previous underspends against the grant. On the face of it this level of overspend is a contravention of financial regulations, as prior approval should have been sought from Cabinet. However, the level of overspend should be viewed in the context of the overall funding available, the vast majority of which is the DFG (£840k) that is received directly by HCC on our behalf. Extra reporting will be put in place to monitor spend in 21/22 will be monitored as the Council's ability to further top up the grant is becoming limited and a policy approach to applications may be required.
Other minor changes			**98**	
Total revision to scheme spend			**1**	

8.7 The following capital schemes have been completed during 2020/21:

- NHLC Gym Members Changing Room
- NHLC Circulation Pipework
- Norton Common Wheeled Sports Facility

- Walsworth Common Pitch Improvements
- Bancroft Recreation MUGA
- Land Purchase adjacent to Grange Community Centre
- Various IT Projects

Capital Programme 2020/21 Funding onwards

8.8 Table 4 below shows how the Council will fund the 2020/21 capital programme.

Table 4: Funding the Capital Programme:

	2020/21 Balance at start of year £M	**2020/21 Additions £M**	**2020/21 Funding Used £M**	**2020/21 Balance at end of year £M**
Useable Capital Receipts and Set-aside Receipts	7.455	0.712	(1.641)	6.526
S106 receipts	[redacted]	[redacted]	(0.122)	[redacted]
Other third party grants and contributions	[redacted]	[redacted]	(0.120)	[redacted]
Planned Borrowing			0	
Total			**(1.883)**	

8.9 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.

8.10 The Council's Capital Financing Requirement (CFR) at 31st March 2021 was negative £5.180 million (negative £5.60 million 31st March 2020). As the CFR is negative the Council does not have a need to borrow to fund capital spend. However, should the Capital programme be fully spent in 21/22 there will be a potential need to borrow £5.2M, which will have an impact on the General Fund by way of a Minimum Revenue Provision (MRP) and interest payments. This need to borrow will mainly be dependent on spend in line with the property acquisition and development strategy. It is expected that any such spend will generate income that will exceed the cost of capital.

Treasury Management 2020/21

8.11 The Council has operated both within the treasury and prudential indicators set out in the Treasury Management Strategy Statement and in compliance with the Treasury Management Practices. The £5 million limit on the Council's current account was exceeded during the 1st quarter to ensure the Council had sufficient funds to pay Business Support Grants and to ensure that cash was available to respond more generally to the implications of Covid-19. The Chief Executive made an urgent decision on the 9th April to temporarily remove the limit on amounts held in the Council's current account to facilitate the grant payments. The current account limit of £5m has since been reinstated. The approved investment limits within the Investment Strategy were breached during October 2020.The limit on investments placed with Building Societies was exceeded by £2.0 million for 19 days in October and was reported to Members in the Third Quarter report.

8.12 The Council generated £0.184M of interest during 2020/21. The average interest rate agreed on new deals during the year was 0.17%. The average interest rate on all outstanding investments at the 31st March was 0.41%.

8.13 The Council's activities expose it to a variety of risks (credit, liquidity and market). The Treasury Strategy sets out the Authority's appetite for the level of exposure to these risks.

8.14 **Security Risk** – The possibility that other parties fail to pay amounts due to the Authority.

The Council's counterparty list comprises UK building societies and UK banks with a Fitch (a credit rating agency) credit rating greater than BBB, non-UK banks with a credit rating greater than AA- with a AAA Country rating, other Local Authorities and Public Corporations. It also includes smaller Building Societies that do not have a credit rating.

8.15 **Liquidity Risk –** the possibility that the Authority may not have funds available to meet its commitments to make payments.

8.16 **Market Risk** - the possibility that financial loss might arise as a result of changes in interest rates.

Investing long term (greater than one year) currently achieves higher interest rates than short term deals. The risks of long term deals are:

(i) The longer the time period the longer the investment is exposed to default.
(ii) If the investment has a fixed interest rate, interest rates could rise and the potential to invest at a higher rate will be lost until the investment matures.

8.17 Members have indicated that they are prepared to accept this risk within the limits expressed in the Treasury Strategy, which allows no more than £12M of outstanding investments to be invested for longer than 365 days at any one time. At the end of the year the Council didn't have any investments invested for longer than 365 days.

8.18 **Interest (Yield)** - This year has continued to prove challenging to find counterparties willing to pay a reasonable return on cash investments, either long or short term. The uncertainty around interest rate changes has continued in 20/21, with the latest predictions indicating that there will be no increase in base rate during 2021/22.

8.19 The investments outstanding at the 31 March 2021 were £42.5million. This compares to a balance of £29.5million at 31 March 2020. Investment in capital projects will continue during 2021/22 and combined with declining returns for new investments, means that the estimated investment interest for 2021/22 was set at £0.103million.

8.20 To try and limit the reduction of investment income from short fixed term investments in 2021/22, the Council will seek to invest in Property Funds and Multi Asset Income Funds. These type of funds are most effective over the longer term with a minimum investment period of five years. A maximum of £4.0M will be invested across the two investment types. Work has begun in collaboration with the Council's Treasury advisors, Link, to select the most appropriate funds for the Council to invest in.

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 £4.113million higher than the budgeted £45.833million.

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 (0.1%). 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 2021 was negative £5.18million. 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).

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.

16.2 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