

CABINET
21 December 2021

***PART 1 – PUBLIC DOCUMENT**

TITLE OF REPORT: SECOND QUARTER INVESTMENT STRATEGY (CAPITAL AND TREASURY) REVIEW 2021/22

REPORT OF: SERVICE DIRECTOR - RESOURCES

EXECUTIVE MEMBER: FINANCE AND I.T.

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 2021/22, as at the end of September 2021.
- 1.2 To update Cabinet on the impact upon the approved capital programme for 2021/22 – 2030/31. The current estimate is a decrease in spend in 2021/22 of £13.124million and a decrease in spend in future years of £10.661million. The most significant change is the removal from the capital programme of the Acquisition of Property Investments capital scheme, for reasons detailed in table 2 and paragraph 8.11. A total of £20m had been earmarked in the programme (£8m in 2021/22 and £4m in each of the next three financial years). The £2.649M Provide Housing at Market Rents scheme is also being removed from the capital programme, while the £1.193M Museum Storage Solution is being withdrawn and replaced with a new capital bid in 2022/23.
- 1.3 To inform Cabinet of the Treasury Management activities in the first six months of 2021/22. The current forecast is that the amount of investment interest expected to be generated during the year is £0.050million. This is an increase of £0.010million on the working estimate reported at 1st quarter.

2 RECOMMENDATIONS

- 2.1 That Cabinet notes the forecast expenditure of £3.045million in 2021/22 on the capital programme, paragraph 8.3 refers.
- 2.2 That Cabinet approves the adjustments to the capital programme for 2021/22 onwards, as a result of the revised timetable of schemes detailed in table 2 and 3, decreasing the estimated spend in 2022/23 by £2.661million.
- 2.3 That Cabinet notes the position of the availability of capital resources, as detailed in table 4 paragraph 8.6 and the requirement to keep the capital programme under review for affordability.

- 2.4 That Cabinet recommends to Council that it notes the position of Treasury Management activity as at the end of September 2021.

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 20th August 2021.

7. BACKGROUND

- 7.1 In February 2021, Council approved the Integrated Capital and Treasury Strategy for 2021/22 to 2030/31. To be consistent with the strategy, the monitoring reports for Capital and Treasury are also integrated.

- 7.2 The Medium Term Financial Strategy for 2021 to 2026 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. 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 2021/22

- 8.2 The full capital programme is detailed in Appendix A and shows the revised costs to date, together with the expected spend from 2021/22 to 2030/31 and the funding source for each capital scheme.
- 8.3 Capital expenditure for 2021/22 is estimated to be **£3.045million**. This is a reduction of **£13.124million** on the forecast in the 1st quarter report (reported to Cabinet on 21st September 2021). The decrease in spend in 2021/22 is largely due to removing projects from the Capital Programme (see paragraph 8.11). Table 1 below details changes to capital programme.

Table 1- Current Capital Estimates

	2021/22 £M	2022/23 £M	2023/24 to 2030/31 £M
Original Estimates approved by Full Council February 2021	14.718	7.919	21.114
Changes approved by Cabinet in 3rd Qrt 2020/21	1.102	0.537	0
Changes approved by Cabinet in 2020/21 Capital Outturn report	0.473	0	0
Revised Capital estimates at start of 2021/22	16.293	8.456	21.114
Executive Member – Finance and I.T. approved additional Expenditure – Financial System upgrade	0.082	0	0

	2021/22 £M	2022/23 £M	2023/24 to 2030/31 £M
Executive Member – Finance and I.T. approved additional Expenditure – Installation of high-definition cameras in the Council Chamber	0.018	0	0
Changes at Q1	-0.224	0.312	0
Executive Member – Finance and I.T. approved additional Expenditure on Careline Servers	0.015	0	0
Changes at Q2	-13.139	-2.661	-8.000
Current Capital Estimates	3.045	6.107	13.114

8.4 Table 2 lists the schemes in the 2021/22 Capital Programme that will start or continue in 2022/23:

Table 2: Scheme Timetable Revision:

(Key: - = reduction in capital expenditure, + = increase in capital expenditure)

Scheme	2021/22 Working Budget £'000	2021/22 Forecast £'000	Difference £'000	Reason for Difference	Estimated impact on 2022/23 onwards £'000
Resurface Lairage Car Park	350	0	-350	Due to delays in agreeing the specification there has been a delay in the procurement process	350
Cycle Strategy Implementation	278	0	-278	Currently working in partnership with HCC in preparing a Local Cycling Walking & Infrastructure Plan (LCWIP) due for completion in Jan 2022, which will then need to go through our Cabinet process for adoption in March. The LCWIP should identify possible schemes that could be part funded from this budget, but these are not likely to occur until 2022/23	278
Transport Plans Implementation	250	0	-250	This is subject to the Local Plan being adopted and the preparation of Supplementary Planning Documents.	250

Scheme	2021/22 Working Budget £'000	2021/22 Forecast £'000	Difference £'000	Reason for Difference	Estimated impact on 2022/23 onwards £'000
Green Infrastructure Improvements	185	0	-185	This is subject to the Local Plan being adopted and the preparation of Supplementary Planning Documents.	185
Letch Multi-Storey Parapet / Soffit / Decoration	129	0	-129	Due to delays in procurement and forming a contract the works have been delayed to commence in summer when the weather is better	129
Thomas Bellamy House Structure	65	0	-65	Project delayed whilst some unexpected preliminary works and investigations at the property are carried out. Completion of these works is necessary before embarking on the planned works. Completion is not expected until around June 2022.	65
Newark Close Road Replacement	65	0	-65	The road has recently undergone some essential repairs. The wholesale replacement is therefore to be deferred until 22/23.	65
Other minor changes			-17		17
Total Revision to Budget Profile			-1,339		1,339

8.5 There are also changes to the overall costs of schemes in 2021/22. These changes total a net decrease of £11.8million and are detailed in Table 3

Table 3: Changes to Capital Schemes Commencing in 2021/22:

(Key: - = reduction in capital expenditure, + = increase in capital expenditure)

Scheme	2021/22 Working Budget £'000	2021/22 Forecast Spend £'000	Difference £'000	Comments
Acquisition of Property Investments	8,000	0	-8,000	No suitable property acquisitions have been identified. This reflects the general economic conditions, as well as changes to Public Works Loan Board borrowing, and expected changes to the CIPFA prudential code. Both of these require that the primary reason for the investment is not a financial return. This therefore implies that the acquisition should be within the District and involve something like regeneration or

Scheme	2021/22 Working Budget £'000	2021/22 Forecast Spend £'000	Difference £'000	Comments
				service delivery. Whilst we will continue to look for opportunities, the budget has been removed from the capital programme for treasury management reasons (see paragraph 8.11).
Provide Housing at Market Rents	2,752	103	-2,649	The forecast spend against this budget is the works to complete the conversion of Harkness Court. As per the description above, the opportunities for further spend have been limited by the expected changes to the CIPFA prudential code. This would preclude the purchase of existing residential property, as generally that would be seen as primarily being purchased for a financial return (unless there was a clear redevelopment plan). Whilst we will continue to look for opportunities the budget will be removed at this stage.
Museum Storage Solution	1,193	0	-1,193	Further investigation with developers has indicated that the cost would be in excess of the available budget. As a result, a new capital proposal with a revised capital estimate is included in the proposed capital programme for 2022 - 2032. The existing budget can therefore be removed from the programme.
S106 Projects	30	75	+45	To date, a total of £75k of S106 funds have been released for community schemes.
Other minor changes			-3	
Total revision to scheme spend			-11,800	

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

Table 4: Funding the Capital Programme:

	2021/22 Balance at start of year £M	2021/22 Forecast Additions £M	2021/22 Forecast Funding Used £M	2021/22 Balance at end of year £M
Useable Capital Receipts and Set-aside Receipts	6.229	4.973	(2.750)	8.452
S106 receipts			(0.075)	
Other third party grants and contributions			(0.185)	
IT Reserve			(0.035)	
Planned Borrowing			0	
Total			(3.045)	

- 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 2021 was negative £5.18 million. Based on current forecasts it will remain negative during 2021/22

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 six months, the Council had an average investment balance of £57.9 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.
- 8.10 During the quarter the Council has had higher than usual 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 in 2020/21. 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 the level in short-term investments with the Debt Management Office has remained high.
- 8.11 The Council generated £0.024M of interest during the first six months of 2021/22. The average interest rate on all outstanding investments at the 30th September was 0.10%. Interest rates have continued to remain low so consequently any new investments are yielding significantly less than the average interest rate on all outstanding investments at the 31st March which was 0.41%. 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 £0.050 million of interest over the whole of 2021/22. The investment strategy allows for investments in a Property Fund and Multi-Asset Fund. In July, Cabinet approved the use of a procurement waiver in relation to the selection of these funds. This selection process has subsequently been paused due to the changes that are expected in relation to the CIPFA prudential code. The current code effectively allows Council's to treat their revenue cash balances and capital borrowing requirement separately. This meant that a Council could borrow for capital (as long as it has a positive Capital Financing Requirement) even if it had revenue cash balances. It could choose to internalise that borrowing (i.e. borrow against revenue cash balances) or obtain external cash. The Council had planned to follow this approach and determined an investment strategy that invested some of its revenue cash balances on a longer-term basis (i.e. in a Property Fund and Multi-asset Fund). This would give the Council the potential benefit

of getting the improved returns from longer term investments, whilst maintaining its capital programme - even though elements of that programme are very uncertain. The revised CIPFA prudential code requires that Councils view their balances overall and only borrow externally when they have no cash remaining (subject to maintaining a buffer for cashflow purposes). The implication of this is that the Council should not embark on longer-term investments if during the expected period of that investment (i.e. 5 years+) the overall remaining cash balances would mean that the level of longer term investments would be imprudent. As a result we have been reviewing the capital forecasts for this year and future years (as part of the Corporate Business Planning process) to determine future cash balances, and whether it would be prudent to undertake longer-term investments. This has included removing capital budgets where there is not a specific plan in place (i.e. the acquisition of property investments and providing housing at market rents). These opportunities will still be investigated and if an opportunity is identified then approval will be sought from Council to add it in to the Capital Programme, and implications on the investment strategy will also be considered. Those implications could include a managed exit from any longer-term investments but ensuring that the exit point was at a time that was beneficial to the Council.

- 8.12 As at 30 September 2021 the split of investments was as shown in the table below. There were no investments with non-UK banks during the quarter due to the high Country rating that we have set for international investments.

Banks	18%
Building Societies	19%
Government	32%
Local Authorities	26%
Money Market Fund (MMF)	5%

- 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 30 September 2021. The most risky investment has a historic risk of default of 0.109%. 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 30 Sept	Historic Risk of Default %
Bank of Scotland	2.0	0.03	A+	Call	0.004
Lloyds	3.0	0.05	A+	Call	0.012
Public Sector Deposit Fund (MMF)	3.0	0.03	AAmmf	Call	0
DMO (Government)	11.0	0.01	AA-	5	0
DMO (Government)	7.0	0.01	AA-	7	0
Leeds Building Society	2.0	0.03	A-	18	0.002
Coventry Building Society	2.0	0.02	A-	19	0.002

Borrower	Principal Invested £M	Interest Rate %	Credit Rating	Days to Maturity at 30 Sept	Historic Risk of Default %
Santander UK	1.0	0.09	A+	29	0.004
Nationwide Building Society	2.0	0.07	A	47	0.006
Ashford Borough Council	3.0	0.04	AA-	55	0.004
Leeds Building Society	1.0	0.1	A-	61	0.008
Blackpool Council	2.0	0.32	AA-	74	0.005
North Lanarkshire Council	2.0	0.03	AA-	111	0.007
Nationwide Building Society	1.0	0.07	A	111	0.014
Santander UK	1.0	0.08	A+	139	0.018
Santander UK	1.0	0.08	A+	144	0.019
Barclays	2.0	0.02	A+	144	0.019
Newcastle Building Society	1.0	0.11	*	151	0.058
Slough Borough Council	2.0	0.1	AA-	152	0.001
Slough Borough Council	1.0	0.1	AA-	152	0.001
West Dunbartonshire Council	5.0	0.05	AA-	260	0.017
Marsden Building Society	1.5	0.25	*	284	0.109
	56.5	0.10			

* 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 around £3 million higher than the budgeted £22 million.

- 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 2021 was negative £5.18million.
- 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 2021/22 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/b8344/Items%20Referred%20from%20Other%20Committees%20-%206b%20-%20Investment%20Strategy%20Capital%20and%20Treasury%2011th-Feb-202.pdf?T=9>