

**FINANCE, AUDIT AND RISK COMMITTEE**  
**29 JULY 2019**

**PUBLIC DOCUMENT**

**TITLE OF REPORT: FIRST QUARTER INVESTMENT STRATEGY (CAPITAL AND TREASURY) REVIEW 2019/20**

REPORT OF THE SERVICE DIRECTOR - RESOURCES

EXECUTIVE MEMBER FOR FINANCE AND I.T.

COUNCIL PRIORITY : RESPONSIVE AND EFFICIENT

**1. EXECUTIVE SUMMARY**

- 1.1 To update Cabinet on progress with delivering the capital and treasury strategy for 2019/20, as at the end of May 2019 and updated for significant events during June.
- 1.2 To update Cabinet on the impact upon the approved capital programme for 2020/21 – 2023/24. The current estimate is a decrease in spend in 2019/20 of £1.398million and an increase in spend in future years of £1.408million. The most significant individual change relates to the reprofiling of the John Barker Place budget into 2020/21.
- 1.3 To inform Cabinet of the Treasury Management activities in the first two months of 2019/20. The current forecast is that the amount of investment interest expected to be generated during the year is £0.372million. This is an increase of £0.072million on the working budget.

**2. Recommendations**

- 2.1 That Cabinet notes the forecast expenditure of **£7.822million** in 2019/20 on the capital programme, paragraph 8.2 refers.
- 2.2 That Cabinet approves the adjustments to the capital programme for 2019/20 onwards as a result of the revised timetable of schemes detailed in table 2, increasing the estimated spend in 2020/21 by **£1.408million**.
- 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 Cabinet is asked to note the position of Treasury Management activity as at the end of May 2019.

### **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 decision that was first notified to the public in the Forward Plan on the 7th June 2019.

### **7. BACKGROUND**

- 7.1 In February 2019, Council approved the Integrated Capital and Treasury Strategy for 2019/20 to 2022/23. This was a change from having a separate Capital Programme and Treasury Strategy. The change was in response to guidance from the Ministry for Housing, Communities and Local Government (MHCLG) and the Chartered Institute of Public Finance and Accountancy (CIPFA). To be consistent with the strategy (and the guidance), the monitoring reports for Capital and Treasury are also integrated.
- 7.2 The Medium Term Financial Strategy for 2019 to 2024 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 2019/20. 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 £114.5 million of capital assets that it currently owns. This value of these assets has increased since the Investment Strategy was set to reflect the property valuations that are required for the Statement of Accounts and the capital spend at the end of the financial year. The most significant addition is the capitalisation of the vehicles used in the waste contract. A summary of the assets owned and the changes in valuation are shown in Appendix A. 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 changes in relation to these since the Strategy was set.

### Capital Programme 2019/20

8.2 The full capital programme is detailed in Appendix B and shows the revised costs to date, together with the expected spend from 2019/20 to 2022/23 and the funding source for each capital scheme.

8.3 Capital expenditure for 2019/20 is estimated to be **£7.822million**. This is a reduction of **£1.398million** on the forecast in the 2018/19 Capital Programme Outturn report (reported to Cabinet on 11<sup>th</sup> June 2019). The decrease in spend in 2019/20 is largely due to the reprofiling the John Barker Place. Table 1 below details changes to capital programme.

**Table 1- Current Capital Estimates**

	2019/20 £M	2020/21 £M	2021/22 to 2023/24 £M
Original Estimates approved by Full Council February 2019	8.213	0.962	2.128
Changes approved by Cabinet in 2018/19 Capital Outturn report	1.007	0	0
Revised Capital estimates at start of 2019/20	9.220	0.962	2.128
Changes at Q1 detailed in this report	-1.398	1.408	0
Current Capital Estimates	7.822	2.370	2.128

8.4 Table 2 lists the schemes in the 2019/20 Capital Programme that will start or continue in 2020/21:

**Table 2: Scheme Timetable Revision:**

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

Scheme	2019/20 Working Budget £'000	2019/20 Forecast Spend £'000	Difference £'000	Reason for Difference	Estimated impact on 2020/21 onwards £'000
John Barker Place, Hitchin	1,096	0	-1,096	Settle have submitted revised plans for pre-application advice and are waiting for confirmation from their Board to proceed with the revised application.	1,096
Property Improvements	278	100	-178	A review of the Condition Survey will be undertaken during the year.	178
Letchworth Multistorey Parapet / Soffit / Decoration	134	0	-134	On hold until the Parking review is complete.	134
<b>Total Revision to Budget Profile</b>			<b>-1,408</b>		<b>1,408</b>

8.5 There is just one minor change to the overall costs of schemes in 2019/20 being an increase of £0.01million.

### Capital Programme 2019/20 Funding onwards

8.6 Table 3 below shows how the Council will fund the 2019/20 capital programme.

**Table 3: Funding the Capital Programme:**

	2019/20 Balance at start of year £M	2019/20 Estimated Additions £M	2019/20 Funding Used £M	2019/20 Balance at end of year £M
Useable Capital Receipts and Set-aside Receipts	8.490	4.950	(6.667)	6.773
S106 receipts			(0.219)	
Other third party grants and contributions			(0.936)	
<b>Total</b>	<b>8.490</b>		<b>(7.822)</b>	

- 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 at 31<sup>st</sup> March 2019 was negative £5.9 million. Based on current forecasts it is expected to remain negative during 2019/20, which means that the Council does not have a need to borrow to fund capital spend.

### **Treasury Management 2019/20**

- 8.9 Whilst the Council does not have a need to borrow for capital spend, it still holds historic borrowing that is uneconomical to repay early. Borrowing can also be used for short-term cashflow purposes. During April and May no borrowing was taken out and no historic borrowing became due for repayment.
- 8.10 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 balances and variations in cash due to the timing of receipts and payments. During April and May the Council had an average investment balance of £34.4 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.
- 8.11 The Council generated £0.062 million of interest during the first two months of 2019/20. The average interest rate on all outstanding investments at the 31 May was 1.17%. 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 £0.372 million of interest over the whole of 2019/20.
- 8.12 As at 31 May the split of investments was as shown in the table below. Due to the time it takes to open investment accounts with non-UK banks, the Council currently still has all of its investments with UK institutions:

Banks	33%
Building Societies	42%
Local Authorities	22%
Money Market Funds	3%

- 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<sup>st</sup> May. The most risky investment still has a historic risk of default of below 1%. 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. As stated in paragraph 8.10, all investments have been made in accordance with the Investment Strategy.

Borrower	Principal Invested £M	Interest Rate %	Credit Rating	Days to Maturity at 31 <sup>st</sup> May	Historic Risk of Default %
Public Sector Deposit Fund	1.0	0.77	AAA	1	0.000
Lloyds Bank	1.0	1.00	A+	3	0.001
National Counties Bldg Soc	1.0	1.00	*	3	0.001
Dumfries & Galloway Council	1.0	0.85	AA	19	0.001
Santander UK Bank	1.5	0.85	A+	30	0.004
Barclays Bank	0.5	0.90	A	44	0.006
Lloyds Bank	0.5	1.00	A+	44	0.006
Yorkshire Bldg Soc	2.0	0.94	A-	46	0.007
Lloyds Bank	0.5	0.90	A+	51	0.008
Slough Borough Council	3.0	0.98	AA	58	0.004
Principality Bldg Soc	1.0	1.00	BBB+	58	0.025
Nottingham Bldg Soc	0.5	1.05	*	74	0.032
Barclay Bank	0.5	0.64	A	75	0.011
Lancashire County Council	2.0	1.10	AA	89	0.006
Santander UK Bank	1.0	0.97	A+	104	0.015
Principality Bldg Soc	1.0	0.99	BBB+	109	0.046
Lloyds Bank	1.0	1.15	A+	157	0.023
North Lanarkshire Council	1.0	0.80	AA	167	0.019
Barclays Bank	2.0	1.00	A	177	0.026
Cambridge Bldg Soc	1.0	1.25	*	181	0.079
Darlington Blsg Soc	1.0	1.30	*	223	0.098
Coventry Bldg Soc	1.0	0.99	A-	261	0.038
Yorkshire Bldg Soc	1.0	0.96	A-	261	0.038
Lancashire County Council	1.0	1.1	AA	292	0.019
Hinckley & Rugby Bldg Soc	2.0	1.35	*	328	0.144
Dudley Bldg Soc	1.0	1.3	*	341	0.561
Marsden Bldg Soc	1.5	1.6	*	601	0.724
Monmouthshire Bld Soc	1.0	1.5	*	727	0.876
	32.5	1.17			

\* Unrated Building Societies Historic Risk of Default is based on a Fitch (a credit rating agency) rating of BBB.

## 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.

## **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 duration of the programme it should be anticipated that the total spend over the period could be around £1.731million higher than the estimated budget of £12.320million.
- 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 £12k a 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 2019 was negative £6million.
- 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 dependant 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 2018/19 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” policy do not apply to this report.

## **14. HUMAN RESOURCE IMPLICATIONS**

- 14.1 There are no direct human resource implications.

## **15. APPENDICES**

- 15.1 Appendix A - Capital Assets as at 31 March 2019.
- 15.2 Appendix B - Capital Programme Detail including Funding 2018/19 onwards.
- 15.3 Appendix C - Treasury Management Update

## **16. CONTACT OFFICERS**

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## **17. BACKGROUND PAPERS**

- 17.1 Investment Strategy (Integrated Capital and Treasury Strategy)  
<https://democracy.north-herts.gov.uk/documents/s4263/Appendix%20A-%20Investment%20Strategy.pdf>