Rushcliffe Borough Council	**Governance Scrutiny Group** **Thursday, 23 November 2023** **Capital and Investment Strategy – Mid-Year Report 2023/24**

Report of the Director - Finance and Corporate Services

1.1. The purpose of this report is to summarise the capital and investment activities of the Council for the period 1 April to 30 September 2023.

1.2. The Capital and Investment Strategy for 2023/24, approved by Council on 3 March 2023, outlines the Council's capital and investment priorities as follows:

- Security of capital
- Liquidity of investments; and
- Optimising yield earned on investments (cash and property).

1.3. The strategy includes indicators that help ensure that the Council's capital investment plans are affordable, prudent and sustainable. Setting an integrated Capital and Investment Strategy is a requirement of the CIPFA Code of Practice.

1.4. As from 1 November the Council have a new Treasury Management Advisor. Arlingclose Financial Advisors replace Link Treasury Services for the next three years.

2. Recommendations

It is RECOMMENDED that the Governance Scrutiny Group considers the Capital and Investment Strategy up-date position as of 30 September 2023.

3. Reasons for Recommendation

3.1 CIPFA's updated Code of Practice for Treasury Management (2021) recommends that Councillors should be informed of Treasury Management activities quarterly. This report ensures that the Council is embracing best practice for the scrutiny of capital and investment activity in accordance with the CIPFA code of Practice.

4. Supporting Information

Economic Forecast

4.1. The UK economy could struggle to keep its head above water the second half of 2023 with real Gross Domestic Product (GDP) growth slowing to just 0.4%. Inflation (CPI) has fallen from 7.9% in June to 6.3% in the 12 months to September 2023 and is forecast to fall further.

4.2. The UK unemployment rate is currently 4.2% and is projected to trend around 5% in 2024 and 5.2% in 2025.

4.3. The Bank of England base rate remains at 5.25%. Analysts are predicting UK interest rates are likely to remain between 5.25% and 5.50% in 2023 before falling to 4.75% by the end of 2024.The Council's Treasury Advisors' forecasts concur with this.

4.4. Overall, the economy is looking on course to avoid a technical recession with a growth rate of 0.3% expected for the whole of 2023 and 0.8% in 2024. The Bank of England base rates are expected to remain around the current base rate.

Investment Income

4.5. Based on Link's base rate forecast of 4.5%, the Council budgeted to receive £1,359,300 in investment income in 2023/24 (compared with £673,300 in 2022/23). Actual interest earned to 30 September 2023 totalled £571,600 (see paragraph 4.8). Whilst base rates have been rising the pooled funds have not been as positively affected but we are expecting to slightly exceed the budget target. Currently we are projecting to receive £1.438m for the year (net of Section 106 and CIL interest discussed in paragraph 4.9).

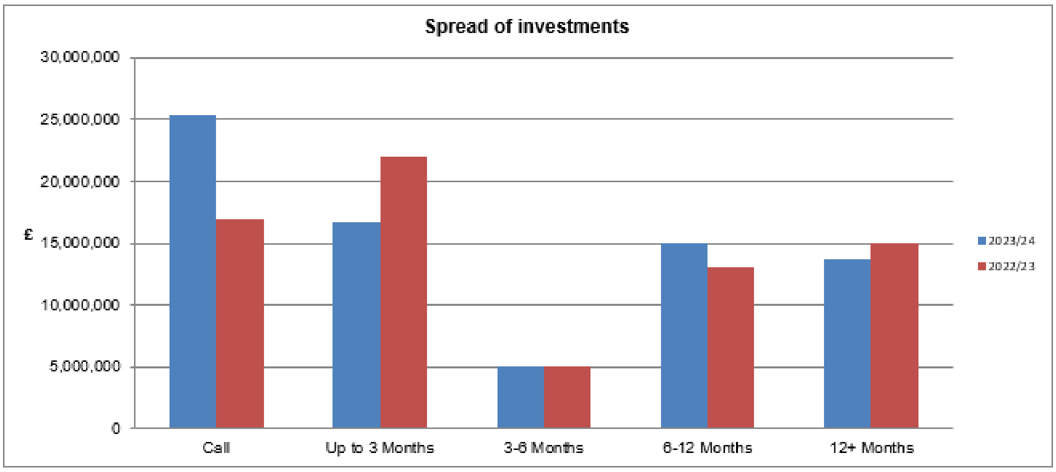
4.6. The average level of funds available for investment purposes during the first 6 months was £55.78m. These funds were available on a temporary basis and the level of funds available was mainly dependent on the timing of precept payments, receipt of grants and progress on the capital programme. The Council holds £13.766m core cash balances for investment purposes (i.e., funds available for more than one year).

4.7. In order to maintain returns and mitigate risks, the Council has continued to diversify its investments mix. As a result, the Council is currently placing deposits in Money Market Funds (MMFs), Call Accounts, CCLA Property Fund, UK Local Authorities and Diversified Funds. A full list of investments at 30 September can be found in Appendix A. Investments totalled £75.914m compared with £72.471m in 2022/23. Investments were made in line with Link's approved counterparty list.

4.8. As part of the Council's diversification strategy, short term investments are, where suitable, made to other local authorities. LA's do not have a credit rating in the same way as other organisations and therefore the Council undertakes its own due diligence before making such investments. Although the sector has in general seen an increase in the issuing S114 notices or declaration of significant budget deficits, investments in these organisations are low risk as Government support remains likely. Arlingclose advise on investment in counterparties without credit ratings in sectors such as local authorities and building societies providing other indicators which will support the Council's investment decisions in such sectors.

4.9. It should be noted that £49.1 million of the above investments relate to funds held in relation to Section 106 and CIL Agreements that are yet to be released by the Council. As part of the agreement, interest has to be paid over once funds are released. The budget assumes interest amounts on these monies will be approximately £1.78m although with higher balances and higher interest rates current projections could change.

4.10. The graph below depicts our investment spread showing the range of investments over the different time periods, balancing both cash flow risk and counterparty risk. The spread of investments is very similar to this time last year. To ensure liquidity, the Council continues to hold considerable sums over the short term, with a greater number of institutions. This is compliant with the Council's Capital and Investment Strategy and recommended action by the Council's Treasury advisors.



4.11. The average interest rates achieved so far this year on the Council's investments are compared to the Sterling Overnight Index Average (SONIA) rates. £25.4m of RBC's investments are held in MMF/Call accounts. Interest rates earned on these accounts tend to lag behind movements in the base rate, although the trend tends to be the same. The Council also holds £37m in temporary investments which vary in duration. These earn a fixed rate of interest set at commencement of the investment so again do not immediately reflect changes in interest rates. RBC also holds just over £13.7m in diversified income and property accounts which are held long term (12 Months +). These are normally higher earning accounts, although with base rates currently high they are only marginally higher than the Bank of England base rate. They are earning an average a rate of 5.57% in interest but are subject to fluctuations in capital value as discussed below in paragraph 4.12.

Benchmark	SONIA (September 2023)	Council Performance
1 Month	5.29%	5.18%
3 Months	5.40%	4.85%
6 Months	5.51%	4.83%
12 Months +	5.59%	5.57%

4.12. The fair value of the Council's diversified funds can fluctuate. In total £15m has been invested in these funds. The table below shows the current position at the end of September. Funds are still volatile with the downward trend experienced by the political turmoil last year continuing, largely mitigated by appropriations to the Pooled Funds reserve which has a current balance of £1.234m. Currently there is a statutory override preventing any accounting loss impacting on the revenue accounts. This is due to end 31 March 2025 having recently been extended a further two years. Whilst the value of this type of investment can fluctuate, the revenue returns make up a significant proportion of the overall returns on investment (32% in 2022/23) The Council will continue to monitor and take advice from our treasury advisors.

Fair Value	31.03.23	30.06.23	30.09.23	Difference	Difference in valuation from initial investment
Aegon-Previously Kames	4,364,956	4,383,672	4,291,918	(73,038)	(708,082)
Ninety One-Previously Inves	4,559,707	4,488,899	4,420,550	(139,156)	(579,450)
RLAM	983,676	980,687	992,726	9,051	(7,274)
CCLA Property	2,018,374	2,015,601	2,015,601	(2,774)	15,601
CCLA Divesified	1,839,164	1,829,781	1,810,885	(28,279)	(189,115)
	13,765,876	**13,698,640**	**13,531,680**	**(234,197)**	**(1,468,320)**

4.13. The Council agreed on the 19 September 2019 to consider its carbon footprint and over the longer-term aim to divest from fossil fuel investments. Currently 18% (21% in 2022) of our portfolio is invested in diversified funds which invest in equities and, therefore, carry a small risk of fossil fuel investments. Security, Liquidity and Yield are the Council's main priority (in accordance with the CIPFA Code for treasury investments). We also have a sustainable fixed term deposit with Standard Chartered and have an ESG liquidity account with HSBC and continue to consider 'green' investments that are compliant with the Council's strategy.

Borrowing

4.14. In accordance with the Local Government Act 2003, the Council has a statutory duty to determine and keep under review how much it can afford to borrow. Therefore, the Council establishes 'Affordable Borrowing Limits' (or Authorised Limit) as part of the Prudential Indicators within the approved Capital and Investment Strategy Statement.

4.15. The authorised limit represents the limit beyond which external borrowing is prohibited and is set as part of the Treasury Strategy, whereas as the operational boundary is the expected borrowing position of the Council based on the CFR and a buffer.

4.16. In light of cash balances in 4.6, the Council continues to internally borrow to fund capital expenditure and does not envisage externally borrowing during the medium term.

4.17. The Council's underlying need to internally or externally borrow for capital expenditure is called the Capital Financing Requirement (CFR). The CFR represents the net capital expenditure in 2023/24 and prior years that has not yet been paid for by revenue or other resources. The Councils CFR is a key Prudential Indicator. The need to internally borrow is now anticipated to be £12.011m in 2023/24 compared to the £13.266m in 2022/23. This is due repayment of MRP of £1.255m. The Operational Boundary set for the year is £20m (see Appendix B). The authorised limit is set at £25m and any change in this would require Full Council approval.

4.18. The Liability (or Asset) Benchmark reflects the real need to borrow. This benchmark, at £37.873m illustrates that the Council has no need to borrow over the medium term (i.e., existing resources exceed the underlying need to borrow). Working capital is projected to be more and hence higher than the expected outturn figure due to reprofiling of expenditure in the capital program (see paragraph 4.19 (a))

£'000	2023/24 Budget	2023/24 Projection	2024/25 £'000	2025/26 £'000	2026/27 £'000	2027/28 £'000
Closing CFR	12,605	12,011	9,385	8,116	7,281	7,012
Less:						
Usable Reserves	(21,853)	(21,377)	(22,632)	(20,451)	(18,665)	(18,281)
Working Capital	(38,625)	(43,010)	(35,750)	(33,750)	(31,750)	(29,750)
Plus minimum investments	10,000	10,000	10,000	10,000	10,000	10,000
LIABILITY BENCHMARK	(37,873)	(42,376)	(38,997)	(36,085)	(33,134)	(31,019)

4.19. As part of the Capital and Investment Strategy, the Council established a range of Prudential Indicators (which also accords with professional practice) to monitor both Treasury and Capital as the two are intrinsically linked. Details of the performance against the Prudential Indicators can be found at Appendix B. Key comments to note are as follows:

(a) Capital Expenditure – The original budget for 2023/24 was £9.576m, with £5.426m carry forwards and other adjustments of £2.681 giving a current budget of £17.683m. The projected outturn is £8.391m, resulting in an estimated underspend of £9.292m arising from projected savings on Bingham Arena and Crematorium (final account is yet to be agreed and may result in some savings); and requested re-profiling of expenditure on other operational land and buildings £7.070m (£6.070m to 2024-25 and £1m to 2025-26). £1.131m is to be accelerated from the 2024-25 programme to support the vehicle replacement programme, this will give a net programme reduction of £5.939m in 2023/24, this position is reported to both Cabinet and Corporate Overview Group.

(b) Financing costs to net revenue stream – this indicator shows the proportion of net income used to pay for financing costs. The projected actual is close to zero, -0.01%, reflecting a breakeven position with investment income matching Minimum Revenue Provision (MRP).

(c) Expected investment position – is expected to be higher due to rephasing of the capital programme and additional S106 monies.

(d) Capital Financing Requirement (CFR) – the closing position will be considerably less than predicted, in the short-term. As a result of re-profiling capital expenditure in the current year there will be no need to increase borrowing in the current year. The CFR projected end of year position is £12.011m. This is a reduction of £1.255m after deducting MRP.

Commercial Investments

4.20. The Council has to disclose its dependence on commercial income and the contribution non-core investments make towards core functions. This covers assets purchase through the Council's Asset Investment Strategy, as well as pre-existing commercial investments.

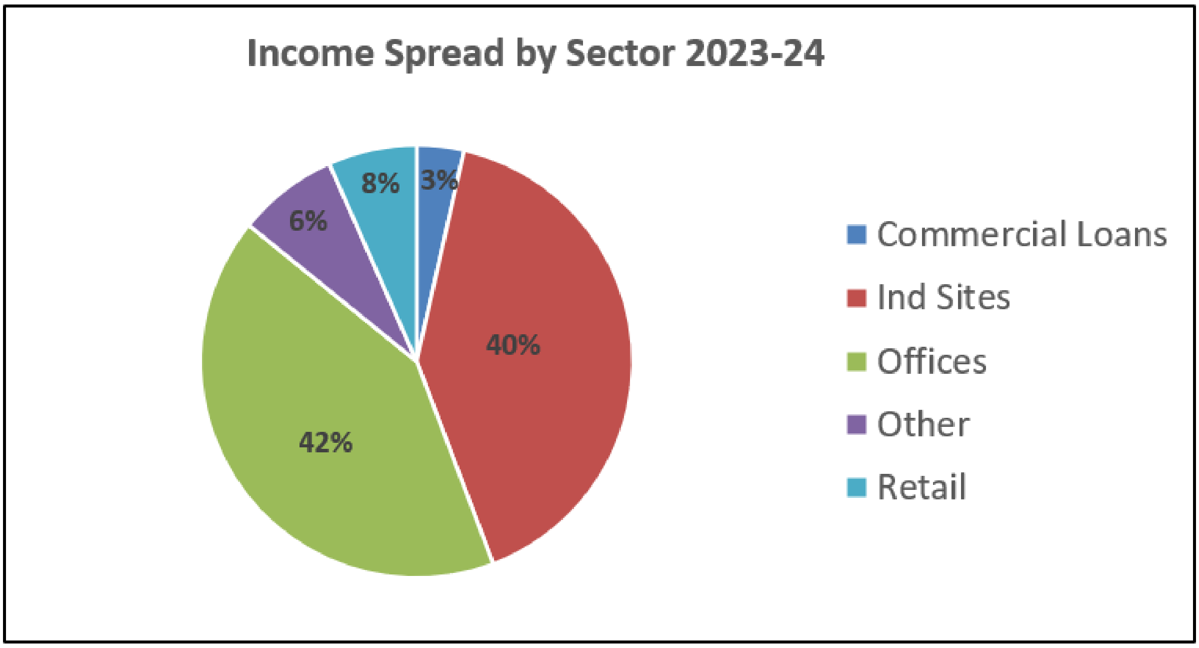
4.21. The expected contributions from commercial investments are shown below. In order to manage the risk to the Council's budget, income from commercial investments should not be a significant proportion of the Council's income. It is estimated to be around 16.4% in the current year, slightly above the current budget due to total income for the council projected to be below that currently budgeted for (in the main Crematorium start up and Planning Fee income). The Council set a target that this ratio should not exceed 30% in future years, subject to annual review.

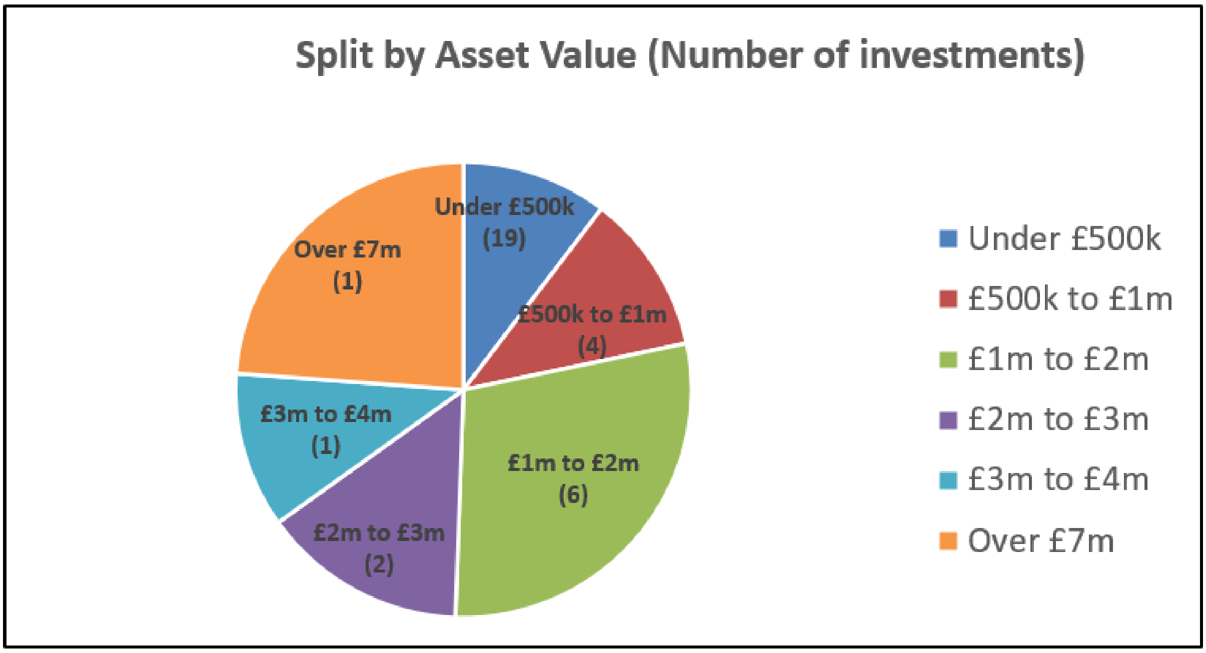
Commercial Investment income and costs

2023/24	Original £'000	Current £'000	Actual £'000	Projected £'000
Commercial Property Income	(1,832)	(1,832)	(950)	(1,864)
Running Costs	480	483	150	545
Net Contribution to core functions	(1,352)	(1,349)	(800)	(1,319)
Interest from Commercial Loans	(67)	(67)	(2)	(67)
Total Contribution	(1,419)	(1,416)	(802)	(1,386)
Sensitivity:				
+/- 10% Commercial Property Income	183	183	95	186
Indicator:				
Investment Income as a % of total Council Income	18.8%	15.7%	15.2%	16.4%
Total Income	10,117	12,105	6,260	11,753

Risk Exposure Indicators

4.22. The Council can minimise its exposure to risk by spreading investments across sectors and by avoiding single large-scale investments. Generally, there is a spread of investment across sectors. The Council's commitment to economic regeneration (not purely financial return) has meant that many of its investments have been in industrial units, which have been very successful. Fears that new ways of working in light of Covid would reduce demand for office accommodation have largely been unfounded, with workers returning to offices.





Security and Liquidity

4.23. Commercial investments are held for longer term asset appreciation as well as yield. Investments or sales decisions will normally be planned as part of the consideration of the five year capital strategy to maximise the potential return. Nevertheless, the local and national markets are monitored to ensure any gains are maximised or losses minimised.

4.24. To help ensure asset values are maintained the assets are given quarterly inspections, together with a condition survey every three years. Any works required to maintain the value of the property will then form part of Council's spending plans.

4.25. The liquidity of the assets is also dependent on the condition of the property, the strength of the tenants and the remaining lease lengths. The Council keeps these items under review with a view to maximising the potential liquidity and value of the property wherever possible. The last Asset Management review was reported to this group 25 November 2021 with the next review planned for spring 2024.

4.26. The liquidity considerations for commercial investments are intrinsically linked to the level of cash and short-term investments, which help manage and mitigate the Council's liquidity risk.

Training and Development

4.27. The Council's previous Treasury Management Advisors, Link Asset Services held a presentation and training session to Councillors on 17 January 2023. The next scheduled training session will be held by our new Treasury Management advisers, Arlingclose. A date is yet to be confirmed but is anticipated to be in January 2024.

5. Conclusion

5.1. Treasury Management continues to be fraught with difficulty. The UK economy is recovering but risk of a slight recession remains. Inflationary pressures are reducing, and although interest rates are currently stable, they are forecast to fall over the longer term. The latter will have a negative effect on returns that can be achieved from investments, and uncertainty in the economy continues to have a negative impact on the capital value of some of the Council's investments. As normality returns then it is expected a positive impact on asset values will materialise. Changes in accounting codes will restrict what local authorities can do coupled with the threat of borrowing caps. Officers will continue to be vigilant and report any significant issues to the Governance Scrutiny Group.

6. Risk and Uncertainties

6.1. The report covers both counterparty, interest rate and property related risks.

7. Implications

7.1. Financial implications

Financial Implications are covered in the body of the report.

7.2. Legal Implications

There are no specific legal implications identified in this report. The report demonstrates the Council's good practice in following CIPFA's Code of Practice for Treasury Management (2021) recommends by informing Councillors of Treasury Management activities quarterly. Adoption of the best practice ensures scrutiny of capital and investment activity undertaken during the relevant period.

7.3. Equalities Implications

There are no equalities implications identified for this report.

7.4. **Section 17 of the Crime and Disorder Act 1998 Implications**

There are no Section 17 implications identified for this report.

7.5. **Biodiversity Net Gain Implications**

There are no Biodiversity Net Gain implications identified for this report.

8 Link to Corporate Priorities

Quality of Life	Good Treasury Management enables the Council to continue to deliver services that contribute to the quality of life of Rushcliffe residents.
Efficient Services	Responsible income generation and maximising returns and minimising exposure to borrowing costs.
Sustainable Growth	The recommendations in this report do not impact on or contribute to the Council's Sustainable Growth priority.
The Environment	Helping to protect the environment by consideration of carbon footprint and fossil-based investments as part of the Capital and Investment Strategy.

9 Recommendations

It is recommended that the Governance Scrutiny Group considers the Capital and Investment Strategy update position at 30 September 2023.

For more information contact:	Peter Linfield Director - Finance and Corporate Services 0115 914 8439 plinfield@rushcliffe.gov.uk
Background papers available for inspection	Capital and Investment Strategy 2023/24 Governance Scrutiny Group 28 September 2023 – Capital and Investment Strategy Q1
List of Appendices (if any):	Appendix A – Investment Balances at 30 September 2023 Appendix B – Prudential and Treasury Indicators for 2023/24 position at 30 September 2023

APPENDIX A

Financial Institution	Amount £	Length of Investment	Interest
Standard Chartered	4,000,000	183 days	5.22%
Standard Chartered	3,000,000	183 days	5.50%
Close Brothers	5,000,000	184 days	4.90%
HSBC ECG	5,148,198	Call	4.82%
Goldman Sachs International	5,000,000	184 days	5.84%
Rushmoor Borough Council	5,000,000	364 days	4.50%
Cornwall Council	5,000,000	184 days	4.35%
Moray Council	5,000,000	365 days	5.00%
North Lanarkshire	5,000,000	365 days	5.00%
Blackrock	427,464	Call	5.23%
CCLA -Public Sector Deposit Fund	133,523	Call	5.20%
Federated	6,876,927	Call	5.35%
Goldman Sachs Asset Management	259,509	Call	5.22%
HSBC	674,579	Call	0.05%
Invesco	6,159,429	Call	5.33%
Aberdeen Asset Management	546,464	Call	5.29%
Bank of Scotland	111,508	32 Days	2.75%
Barclays Bank	4,528,860	32 Days	5.20%
Santander UK	166,093	Call	3.23%
Santander UK	84,182	35 Days	4.53%
Residual MMF/Call Account balances	32,022	Call	3.61%
Royal London Cash Plus Fund	983,676	On-going	4.53%
CCLA Property Fund	2,018,374	On-going	3.96%
CCLA Diversified Income Fund	1,839,164	On-going	3.25%
Aegon Diversified Income Fund	4,364,956	On-going	6.80%
Ninety One Diversified Income Fund	4,559,707	On-going	6.02%
Total Investments/Average Interest Rate	**75,914,635**		**5.09%**

APPENDIX B

Prudential and Treasury Indicators for 2023/24
Position at 30 September 2023

	2023/24 £'000 Original Estimate	2023/24 £'000 Current Projections
Prudential Indicators		
Capital Expenditure – see paragraph 4.19	17,683	8,391
Proportion of financing costs to net revenue streams	-0.37%	-0.01%
Expected Investment Position (at 31 March 2024)	48,149	67,500
Capital Financing requirement as at 31 March 2024	13,266	12,011
Net Income (from Commercial and Service Investments) to Net Revenue Streams	11.3%	8.12%
Treasury Management Indicators		
Authorised Limit for external debt Borrowing and other long-term liabilities	25,000	25,000
Operational Boundary for external debt Borrowing and other long-term liabilities	20,000	20,000
Upper limit for fixed interest rate exposure on investments up to 1 year	50%	50%
Upper limit for variable rate exposure (investments)	100%	100%
Upper limit for total principal sums invested over 1 year	24,100	33,750
Liability Benchmark	(37,873)	(42,376)

Glossary of Terms

Money Market Funds – these funds are pooled investment vehicles consisting of money market deposits and similar instruments. They have the advantage of providing wide diversification of investment risks.

CCLA Property Fund - this a local authority property investment fund. The property fund is designed to achieve long term capital growth and a rising income from investments in the commercial property sector.

Pooled Funds – shares in diversified investment vehicles consisting of different investment types including banks, equity shares and property, these funds have the advantage of providing wide diversification of investment risks.

Pooled Funds Reserve – monies set aside (appropriated) from revenue efficiencies and underspends which will be used to offset any future accounting or actual loss incurred in the revenue accounts.

SONIA (Sterling Overnight Index Average) – Average interest rates that banks pay to borrow sterling overnight from other financial institutions in circumstances where credit, liquidity and other risks are minimal.

CPI – (Consumer Price Index) – a measure of the average change over time in the prices paid by consumers for a representative basket of consumer goods and services.

GDP – (Gross Domestic Product) – measures the monetary value of final goods and services produced in a country in a given period of time.