Rushcliffe Borough Council

Governance Scrutiny Group

Thursday, 22 February 2024

Capital and Investment Strategy – Quarter Report 3 2023/24

Report of the Director - Finance and Corporate Services

1. Purpose of report

1.1. The purpose of this report is to summarise the capital and investment activities of the Council for the period 1 April to 31 December 2023.

1.2. The Capital and Investment Strategy for 2023/24, approved by Council on 2 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.

2. Recommendations

It is RECOMMENDED that the Governance Scrutiny Group considers the Capital and Investment Strategy update position as of 31 December 2023.

3. Reasons for Recommendation

CIPFA's Code of Practice for Treasury Management (2021) recommends that Councillors should be informed of Treasury Management activities quarterly. This report, therefore, ensures this 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 is currently facing a weakening economic outlook with a prolonged period of weak Gross Domestic Product (hovering close to zero), inflation (CPI) easing from a peak of 11.1% in October 2022 but unlikely to be back to normal levels of around 2% until the end of 2025 and an uncertain political climate due to an upcoming general election.

4.2. At its meeting in August 2023, the Bank of England Monetary Policy Committee (MPC) increased the base rate to 5.25%, it remained at this level for the rest of 2023.

4.3. The Council's treasury management adviser, Arlingclose, forecasts the Bank Rate has peaked at 5.25% and rates will start to reduce in 2024 with the first cuts anticipated in Q3 2024 to a low of around 3% early-mid 2026.

4.4. Overall, UK economic activity has outperformed expectations, but the outlook remains weak and vulnerable to shocks. Risks to the outlook are skewed to the downside, and stem from more persistent inflation, delayed impact of monetary policy, labour supply and geopolitical risks.

Investment Income

4.5. Based on Link's (the Council's Treasury Advisors at the time) 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 31 December 2023 totalled £640,919 with total receipts for the year expected to be approximately £1.442m. Interest receipts are slightly higher than estimated due to investment balances and interest rates being higher than budgeted for. The Council achieved an average interest rate of 5.11%, compared to the average SONIA rate of 4.94%.

4.6. The average level of funds available for investment purposes during the quarter was £83.32m. 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 £14.015m 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. 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.

4.8. The Council ensures investments are secure and that liquidity is achieved whilst at the same time it is proactively looking to maximise its rate of return. A full list of investments at 31 December 2023 can be found at Appendix A.

4.9. 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.

4.10. The fair value of the Council's diversified funds can fluctuate. These can be seen in Appendix B. Funds are still volatile, but values are starting to pick up after a long downward trend. 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 for a further two years. The risk of any impact on the accounts is mitigated by appropriations to the Treasury Capital Depreciation Reserve which has a current balance of £1.173m which is in excess of current requirement. The revenue returns from these funds make up a significant proportion of the overall returns on investments (32% in 2022/23) and have returned £2.9m since these investments were purchased. The Council will continue to monitor the position and take advice from the treasury advisors.

Capital Expenditure and Financing

4.11. The original Capital Programme for 2023/24 was £9.576m, with £5.426m carry forwards and other adjustments reducing the budget by £2.585m giving a current budget of £12.417m. The projected outturn is £8.537m, resulting in an estimated underspend of £3.880m arising from realisable savings on Bingham Arena and Crematorium and reprofiling the provision for support for Registered Housing Providers to future years,

4.12. The Council undertakes capital expenditure on both its own long-term assets and on grants that can be capitalised under statute (capital payments to third parties). These activities may either be:

- Financed immediately through the application of capital or revenue resources (capital receipts, capital grants, revenue contributions etc.) which has no resulting impact on the Council's borrowing need; or
- If insufficient financing is available or a decision is taken not to apply resources, the capital expenditure will give rise to a borrowing need.

4.13. The actual capital expenditure forms one of the required prudential indicators. Table 1 below shows actual capital expenditure and how this will be financed. There is currently no need to borrow in the current financial year or over the medium term:

Table 1

	2023/24 Current £000	2023/24 Projection £000	Variance
Capital Expenditure	12,417	8,537	(3,880)
Less Financed by:			
Capital Receipts	(6,115)	(3,906)	2,209
Capital Grants	(3,139)	(3,112)	27
Reserves	(842)	(710)	132
Section 106 Monies	(2,321)	(809)	1,512
Increase in Borrowing Need	**0**	**0**	**0**

4.14. The Council's underlying need to 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.

4.15. The Council's CFR for 2023/24 represents a Key Prudential Indicator and is shown below in Table 2. The table shows a forecast net reduction in the CFR with no additional internal borrowing in the year and after deducting the Minimum Revenue Provision (MRP) of £1.255m and capital receipts applied of £2.5m.

Table 2

	2023/24 Current £000	2023/24 Projection £000
Opening CFR	15,516	13,266
CFR in year	1,000	0
Less: MRP etc	(1,311)	(1,255)
Less: Capital Receipts Applied	(2,600)	(2,500)
Closing CFR	**12,605**	**9,511**

Borrowing and Prudential Indicators

4.16. 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 C.

4.17. The Liability Benchmark (also sometimes referred to as the Asset Benchmark) reflects the real need to borrow. A credit balance shows that the Council has no need to borrow over the medium term.

4.18. Net Income from Commercial and Service Investments to Net Revenue Streams reflects the Council's dependence on income from investments. The projected figure is lower than estimated due changes in the operational start dates for the Crematorium and Bingham Hub, rising utility costs and favourable net revenue streams.

Commercial Investments

4.19. The Council must 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.

4.20. The Council's target is that this should not exceed 30% with the current actual around 15% (see Appendix D), leaving it less exposed to risks surrounding commercial property.

4.21. 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 Asset Management review has been conducted and will be considered as a separate report on this agenda.

5. Conclusion

Treasury Management continues to be fraught with difficulty. The UK economy is recovering but risk of a recession remains with inflationary pressures and possible reductions in interest rates coupled with a general election pending. Cuts in interest rates will have a negative effect on returns that can be achieved from investments, uncertainty in the economy can also have a negative impact on the capital value of some of the Council's investments. Officers will continue to monitor the environment 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	No direct impact on quality of life
Efficient Services	Responsible income generation and maximising returns
Sustainable Growth	No direct impact on sustainable growth
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 Group notes the Capital and Investment Strategy update position as of 30 June 2023.

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Background papers available for inspection	Treasury Management Strategy 2023/24
List of Appendices:	Appendix A – Investments held at 31 December 2023 Appendix B – Pooled Funds Appendix C - Prudential and Treasury Indicators for 2023/24 position at 31 December 2023 Appendix D – Commercial Investment Income and Costs

APPENDIX A

Investments held at 31 December 2023

Financial Institution	Amount £	Length of Investment	Interest
Standard Chartered	3,000,000	183 days	5.50%
Standard Chartered	3,000,000	183 days	5.43%
Close Brothers	5,000,000	179 days	4.90%
HSBC ECG	5,216,233	Call	4.82%
Goldman Sachs International	5,000,000	Call	5.84%
Rushmoor Borough Council	5,000,000	364 days	4.50%
Moray Council	5,000,000	365 days	5.00%
North Lanarkshire	5,000,000	365 days	5.00%
Central Bedfordshire Council	5,000,000	92 Days	5.30%
Stockport Metro Borough Council	5,000,000	87 Days	5.30%
Residual MMF/Bank Balances	32,144	Call	5.24%
Blackrock	4,605,206	Call	5.33%
Ccla - Psdf	137,348	Call	2.26%
Federated Investors (Uk)	7,307,907	Call	5.36%
Goldman Sachs Asset Management	262,893	Call	5.23%
Hsbc Asset Management	2,563,940	Call	0.50%
Invesco Aim	7,819,708	Call	5.32%
Aberdeen Asset Management	2,794,276	Call	5.28%
Bank Of Scotland Plc	112,244	32 Days	2.75%
Barclays Bank Plc	4,568,889	32 Days	5.20%
Santander Uk Plc	167,440	Call	3.23%
Santander Uk Plc	85,189	35 Days	4.78%
Royal London Cash Plus Fund	983,676	On-going	3.96%
Ccla Property Fund	2,018,374	On-going	4.36%
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	6.20%
Total Investments/Average Interest F	**90,439,295**		**5.11%**

APPENDIX B

Fair Value of pooled fund investments

Fair Value	31.03.23	30.04.23	31.12.23	Amount Invested	Difference	Difference in valuation from initial investment
Aegon-Previously Kames	4,364,956	4,411,518	4,530,206	5,000,000	165,249	(469,794)
Ninety One-Previously Investec	4,559,707	4,560,198	4,558,231	5,000,000	(1,475)	(441,769)
RLAM	983,676	988,835	1,003,107	1,000,000	19,431	3,107
CCLA Property	2,018,374	2,018,374	2,005,610	2,000,000	(12,764)	5,610
CCLA Divesified	1,839,164	1,856,626	1,918,266	2,000,000	79,102	(81,734)
	13,765,876	**13,835,552**	**14,015,420**	15,000,000	**249,544**	**(984,580)**

APPENDIX C

Prudential and Treasury Indicators for 2023/24
Position at 31 December 2023

	2023/24 £'000 Original Estimate	2023/24 £'000 Projected
Prudential Indicators		
Capital Expenditure	9,576	8,537
Proportion of financing costs to net revenue streams	-0.37%	-1.41%
Expected Investment Position (at 31 March 2024)	48,149	54,876
Capital Financing requirement as at 31 March 2024	12,605	9,511
Net Income (from Commercial and Service Investments) to Net Revenue Streams	10.9%	8.8%
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	27,438
Liability/(Asset) Benchmark	(38,149)	(44,876)

APPENDIX D

Commercial Investment Income and Costs

2023/24	Original £'000	Current £'000	Actual £'000	Projected £'000
Commercial Property Income	(1,832)	(1,832)	(1,423)	(1,911)
Running Costs	480	483	372	593
Net Contribution to core functions	(1,352)	(1,349)	(1,051)	(1,318)
Interest from Commercial Loans	(67)	(67)	(4)	(67)
Total Contribution	(1,419)	(1,416)	(1,055)	(1,385)
Sensitivity:				
+/- 10% Commercial Property Income	183	183	142	191
Indicator:				
Investment Income as a % of total Council Income	18.1%	14.6%	15.3%	15.6%
Total Income	10,117	12,550	9,293	12,250

Glossary of Terms

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.

Covered Bonds – these investments are secured on the bank's assets, which limits the potential losses in the unlikely event of insolvency, and means they are exempt from bail-in.

LIBID – London Inter Bank Bid Rate. The rate at which banks are willing to borrow from other banks.

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.

MRP – Minimum Revenue Provision – is the minimum amount which a Council must charge to its revenue budget each year, to set aside a provision for repaying external borrowing. This is an annual revenue expense in a Council's budget.

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.

SONIA – Sterling Over Night Indexed Average – is an overnight rate, set in arrears and based on actual transactions in overnight indexed swaps for unsecured transactions in the Sterling market.

ESG – Environmental, Social and Governance – a set of practices (policies, procedure etc.) that organisations implement to limit negative impact or enhance positive impact on the environment, society and governance bodies.