STRATEGY & RESOURCES COMMITTEE - 3RD FEBRUARY 2020 - AGENDA ITEM 7

INVESTMENT SUB-COMMITTEE

Minutes of the meeting of the Sub-Committee held in the Lyndsay Narcisi Room, Council Offices, Station Road East, Oxted on the 24th January 2020 at 10.00 a.m.

PRESENT: Councillors Elias (Chair), Bourne, Farr, Jecks and Jones.

APOLOGY FOR ABSENCE: Councillor Davies.

1. MINUTES

The minutes of the meeting held on the 25th October 2019 were approved as a correct record.

2. DECLARATIONS OF INTEREST

Councillor Jecks declared that:

- he is a non-executive director of UBS Asset Management UK Limited; and
- chairs two other committees regarding investments for which CCLA is the fund manager

These did not amount to disclosable pecuniary interests under the Members' code of conduct and Councillor Jecks remained in the meeting.

COUNCIL DECISION
(subject to ratification by Council)

3. INVESTMENT STRATEGIES FOR 2020/21

Proposed updated investment strategies for capital, treasury management and commercial property were presented. The main purposes of the strategies were to explain:

<u>Capital and Investment Strategy 2020/21 to 2022/23</u>

- the Council's capital expenditure plans, together with funding sources (i.e. external / internal sources or borrowing)
- the Council's policy of adopting the 'asset life / annuity method' for charging a prudent Minimum Revenue Provision (MRP) to the general fund revenue budget to account for the cost of debt
- the Council's approach to asset management, treasury management and investments

<u>Treasury Management Strategy 2020/21</u>

- cashflow planning for meeting expenditure demands
- the approach to investing surplus monies and to fund the capital programme
- the approach to borrowing in relation to the limits imposed by prudential indicators

Commercial Property Investment Strategy 2020/21

- the process for identifying and evaluating commercial property investment opportunities

- the objectives of such investments, namely to achieve financial returns that contribute towards savings targets and budgets to enable the continued delivery and investment in key services and/or to enable redevelopment and regeneration

- clarification that the 'reasonable economic area limit' (for property investments) is within 30 miles of the District's boundary.

R E C O M M E N D E D – that the following strategies be adopted:

(i) the capital and investment strategy for 2020/21 to 2022/23 at Appendix A (page 4)
(ii) the treasury management strategy for 2020/21 at Appendix B (page 31)
(iii) the commercial property investment strategy for 2020/21 at Appendix C (page 48).

SUB-COMMITTEE DECISIONS
(under powers delegated to the Sub-Committee)

4. SUMMARY INVESTMENT AND BORROWING POSITION

The investment analysis at Appendices D and E was considered, together with fact sheets for the four funds within the Council's treasury investment portfolio. Discussion focused on the £2 million investment with Funding Circle's 'peer to peer' retail lending platform. This followed the decision at the previous meeting to review the investment, pending consideration of:

(i) the viability of the investment being re-profiled on a more conservative basis; and

(ii) the question of whether the investment could be switched to a Funding Circle institutional fund.

The Sub-Committee concluded that nether options (i) or (ii) above were likely to be more advantageous than switching to one, or a combination of, the CCLA (x2), Schroders or UBS funds. It was therefore agreed that the redemption proceeds of Funding Circle loans should not be automatically re-invested in further Funding Circle loans but should, instead, be regularly withdrawn from Funding Circle and invested in the other four funds equally.

Officers also undertook to provide an analysis of Gryllus property investments at future Sub-Committee meetings, including rental income streams; costs being incurred by the company; and relevant information about the various tenancies.

R E S O L V E D – that

A. the Council's investment and borrowing position at 31st December 2019, as set out at Appendices D and E (pages 61 to 63) be noted;

B. upon redemption of the Council's current Funding Circle loans, the monies be invested elsewhere within the Council's portfolio (in equal portions), namely 25% to each of the following funds:

- CCLA (diversification fund)
- CCLA (property fund)
- Schroders bond fund
- UBS multi-asset fund

C. the individual factsheets for the CCLA, Schroders and UBS funds be noted; and

D. the current Statement of Investment Beliefs (Appendix F on page 64) be noted.

5. EXCLUSION OF THE PUBLIC

R E S O L V E D – that members of the press and public be excluded from the meeting for the consideration of the item covered by Minute 6 below because:

(i) it involves the likely disclosure of exempt information as defined in Paragraph 3 of Schedule 12A to the Local Government Act 1972 (i.e. information relating to the financial or business affairs of any particular person); and

(ii) the public interest in maintaining the exemption outweighs the public interest in disclosing the information.

6. PROPERTY INVESTMENT UPDATE

The Sub-Committee considered a report about current property investment activity, including an update about recent acquisitions, on-going due diligence about another proposed purchase and other opportunities that continued to be tracked.

R E S O L V E D – that

A. the Council's property investment activity be noted;

B. officers' continued investigations into potentially suitable investment sites be supported; and

C. officers be supported in their efforts to bid to purchase properties that align with the Council's property investment strategy and which offer a relatively low-risk income stream (all bids would be subject to contract and full due diligence and in line with the requirements of Financial Regulation 17).

7. DATE OF NEXT MEETING

This was scheduled for Friday, 17th April 2020 at 10.00am (Lyndsay Narcisi Room).

Rising: 11.13 a.m.

CAPITAL AND INVESTMENT STRATEGY 2020/21 to 2022/23

1. Introduction

1.1 This capital strategy gives a high-level overview of how capital expenditure, capital financing and other investments contribute to the delivery of the Council’s Vision along with an overview of how associated risk is managed and the implications for future financial sustainability. It has been written in an accessible style to enhance members’ understanding of these sometimes technical areas.

1.2 The overarching aim of the 2019/20 to 2022/23 Capital Strategy is to provide a framework within which the Council’s capital investment plans will be delivered. It has been prepared to cover a four year time-frame from 2019/20 to 2022/23. Recognising that there is some uncertainty, especially in relation to funding in later years, the Strategy therefore focuses on 2019/20 and 2020/21.

1.3 Capital investment plans are driven by the Council’s Key Objectives. The Key Objectives form the Council’s key strategic document and outlines the Council’s contribution to achieving the vision and outcomes detailed in the Council’s Vision, as well as priority areas of focus and delivery aimed at taking forward our vision of a co-operative future where everyone contributes to create a confident and ambitious district.

1.4 The Council’s key objectives and priorities have been agreed by Strategy and Resources Committee. These are reviewed annually and these will be considered as part of the Council’s review of the Corporate Plan in 2020/21. The current key objectives and key priorities are set out below

2. Council’s Vision, Key Objectives and Key Priorities

2.1 The Council's Vision is to make Tandridge ‘aspirational for our people, our place and ourselves’.

2.2 The Council’s Key Objectives to achieve the Vision are:

- Providing high quality, customer focused services.
- Making a difference in our community by supporting those who need it most.
- Creating a thriving economy while protecting the local environment.
- Working in partnership with the community and other public services to create opportunities for all.
- Improving the quality of our residents’ lives, including enabling access to decent and affordable homes.
- Being a proactive, flexible learning environment.

2.3 The top five priorities for achieving this are to:

- Implement the Customer First Strategy.
- Implement a strategy for investing in land and property in order for the Council to remain financially viable and to create more affordable housing.
- Progress the Local Plan process to adoption (i.e. to the Secretary of State for Examination).
- Enhance the vitality and viability of our town centres, including the adoption and implementation of regeneration schemes in Caterham and Oxted.
- Engage with multi-agency partners to facilitate flood prevention measures in Caterham, Smallfield and Whyteleafe.

2.4 The key objectives reflect the on-going commitment to ensure the Council works to serve the people of Tandridge in all that it does and provides strong leadership for the district. Such leadership is essential if the district is to be able to meet the immediate challenges faced in a way that means it is stronger and able to make the most of opportunities in the future.

2.5 Aligned to corporate and service priorities, individual scheme proposals are included within approved capital spending plans or are to be considered for a resource allocation over the period of the Capital Strategy having regard to the Commercial Property Investment Strategy.

2.6 The Capital Strategy therefore aligns to the Commercial Property Investment Strategy. The Commercial Property Investment Strategy presents a framework for strategic management of the Council's land and property portfolio, reflecting the Council's key priorities and driving transformational change in service delivery.

2.7 The Commercial Property Investment Strategy incorporates the statutory requirements and aligns to the Council's Key Priorities. The Commercial Investment Strategy will align with Council's wider priorities for revenue generation, site acquisition, site development, release of assets for disposal, affordable housing and regeneration within the District.

2.8 The Council is continuing to develop the Commercial Property Investment Strategy and this will regularly be refreshed to improve the way in which Commercial Property Investment objectives can be delivered. This will enable the Council to accelerate progress and realise benefits within a shorter timeframe, whilst maximising regeneration and investment opportunities.

2.9 The Council's intention in relation to capital investment is to take a strategic approach so capital investment can be directed to make a real and demonstrable impact on the economy of Tandridge by:

- Regenerating the district, by attracting and securing significant amounts of external investment to supplement Council resources and deliver an enhanced district-wide regeneration offer.
- Prioritising the regeneration investment to develop the local economy and to support job creation and promote local employment within the District.
- Using the regeneration investment to drive up the yield from business rates This will provide additional resources which can either be used to support the Council's budget or to pursue opportunities for further investment in Tandridge.

2.10 The Council will also:

- Work with Surrey County Council, Parish Councils, Health, Police and Fire as a co-operative and commissioning district particularly with regard to the integration of health and social care to promote joint investment opportunities, co-location and the release of surplus assets.
- Instigate further transformational approaches to the delivery of services with and by communities and staff, that maximise involvement and delivery at a more local level, working with residents to reset priorities, manage expectations and promote self-help.
- Get the basics right, drive improved business performance with more flexible customer focused ICT systems which enable web based self service and instigate new delivery models.
- Focus on effective service delivery, achieving social value and maximising the impact of the resources invested.

2.11 The Capital Strategy is focused on the achievement of the Council's Key Objectives and Key Priorities in order to deliver maximum benefit from the use of capital resources. A set of overarching principles, which apply to the Council's 2019/22 Capital Strategy, are set out in Annex 1.

3. Key Priorities for Capital Investment

3.1 Priority investment areas for 2019/20 onwards will be taken forward subject to the availability of resources and the approval of a full business case. The priority investment areas identified for the 2019/20 to 2022/23 period are set out in Annexes 2 and 7.

4. Capital Expenditure and Financing

4.1 Capital expenditure investment is where the Council spends money on assets, such as property or vehicles, that will be used for more than one year. In local government this includes spending on assets owned by other bodies and providing loans and grants to other bodies to enable them to buy assets.

4.2 The Council capitalises expenditure on the acquisition or creation of a *tangible and intangible assets,* where the expenditure adds to and not merely maintains the value of the asset.

4.3 In 2019/20, the Council is planning capital expenditure investment totalling over 4 years of £248.2m as summarised below:

Table 1: Prudential Indicator: Estimates of Capital Expenditure in £ millions

	2018/19 Actual £m	**2019/20 Forecast £m**	**2020/21 Budget £m**	**2021/22 Budget £m**	**2022/23 Budget £m**
General Fund services	4.671	5.930	2.928	1.426	1.176
Council Housing (HRA)	9.832	10.378	14.045	12.595	4.436
Capital Investments	5.565	66.000	65.000	64.375	0
TOTAL	**20.068**	**82.308**	**81.973**	**78.396**	**5.612**

4.4 The main General Fund capital projects in 2019/20 and 2020/21 includes the replacement of Waste Vehicles (£3.5m), the purchase for wheeled refuse bins (£0.6m) and the refurbishment of public conveniences (£0.55m). The Council also plans to incur £195.4m of capital expenditure on property investment as part of the Council's Commercial Property Investment Strategy.

4.5 The Housing Revenue Account (HRA) is a ring-fenced account which ensures that council housing does not subsidise, or is itself subsidised, by other local services. HRA capital expenditure is therefore recorded separately. Details of the draft Capital Programme 2019-23 are attached at Annex 7.

4.6 All capital expenditure must be financed, either from external resources (government grants and other contributions), the Council's own resources (revenue, reserves and capital receipts) or debt (borrowing, leasing and Private Finance Initiative).

The planned financing of the above expenditure is as follows:

Table 2: Capital financing in £ millions

	2018/19 Actual £m	2019/20 Forecast £m	2020/21 Budget £m	2021/22 Budget £m	2022/23 Budget £m
External resources	0.596	0.744	1.191	0.676	0.725
Internal resources	7.607	10.768	10.194	7.465	4.446
Borrowing	11.865	70.796	70.588	70.255	0.441
TOTAL	**20.068**	**82.308**	**81.973**	**78.396**	**5.612**

4.7 Further details on the different funding sources for funding capital expenditure as set out in Annexes 3 & 8

4.8 Borrowing is only a temporary source of finance, since loans and leases must be repaid, and this is therefore replaced over time by other financing, usually from revenue which is known as minimum revenue provision (MRP). Alternatively, proceeds from selling capital assets (known as capital receipts) may be used to replace debt finance. Planned MRP, Repayments and use of capital receipts are as follows:

Table 3: Replacement of debt finance in £ millions

	2018/19 Actual £m	2019/20 Forecast £m	2020/21 Budget £m	2021/22 Budget £m	2022/23 Budget £m
Minimum Revenue Provision	0.035	0.213	0.295	0.359	0.368
Refinancing of HRA Debt	3.850	4.050	4.250	2.350	2.850

Minimum Revenue Provision (MRP)

4.9 Under regulations 27 and 28 of the 2003 Regulations, local authorities are required to charge a prudent MRP to their revenue account for each financial year to account for the cost of their debt in that financial year. The prudent amount should be determined with the broad aim of ensuring that debt is repaid over a period reasonably commensurate with that over which the capital expenditure provides benefit. The Secretary of State recommends that full Council should approve an MRP policy in respect of the financial year ahead.

4.10 The guidance issued gives four options for making MRP which the Secretary of State considers prudent provision. The option chosen can be altered annually.

4.11 Tandridge District Council's MRP policy is follow the Asset Life – annuity method of calculating MRP. The Asset Life - annuity method allows MRP to increase gradually over the asset life, which better reflects the profile of the Council's borrowing requirement for its capital assets (and their benefits), rather than the equal instalment method which, simply provides MRP in equal instalments and is less accurate. The Council's full minimum revenue provision policy statement is attached at Annex 5.

Borrowing

4.12 The Council will investigate opportunities to resource capital projects using prudential borrowing where plans are sustainable, affordable and prudent. Full appraisal will take place to ensure that, where appropriate, sufficient revenue returns are generated to cover the cost of borrowing. This will be especially important when undertaking property acquisitions under the Commercial Property Investment Strategy (CPIS) where, in addition, a revenue income stream is required to support the revenue budget.

4.13 Where it is considered that Prudential Borrowing is the appropriate method of funding it will require additional revenue budget to finance the interest and minimum revenue provision.,

4.14 Strategy and Resources Committee will review the detailed capital expenditure plans before allocations of resources are committed to ensure that the costs of prudential borrowing are understood and affordable.

4.15 The Council is able to take advantage of the Public Works Loans Board (PWLB) certainty rate, whereby there is a 20 basis points discount on standard loans from the PWLB under the prudential borrowing regime for authorities which provide improved information on their long term borrowing and associated capital spending plans. The obvious benefit to the Council of the certainty rate is reflected in reduced Treasury Management borrowing costs in relation to any PWLB borrowing undertaken.

5. Capital Financing Requirement

5.1 The Council's cumulative outstanding amount of debt finance is measured by the capital financing requirement (CFR). This increases with new debt-financed capital expenditure and reduces with MRP and capital receipts used to replace debt. The CFR is anticipated to increase by £135.2m during 2019/20. Based on the above figures for expenditure and financing, the Council's estimated CFR is as follows:

Table 4: Prudential Indicator: Estimates of Capital Financing Requirement in £ millions

	31.3.2019 actual	31.3.2020 forecast	31.3.2021 budget	31.3.2022 budget	31.3.2023 budget
General Fund services	3.653	9.583	12.511	13.937	15.113
Council housing (HRA)	61.308	71.686	85.731	98.326	102.762
Commercial Investment	8.832	74.832	139.832	204.207	204.207
TOTAL CFR	**73.793**	**156.101**	**238.074**	**316.470**	**322.082**

6. Capital Programme Governance

6.1 The Council has specific arrangements for the management of capital expenditure. The principles for governance of the Capital Programme are detailed in in Annex 4. The separate approval process for the acquisition of commercial investments in property is contained within the CPIS.

7. Asset Management & Asset Disposals

7.1 To ensure that the Council's capital assets continue to be of long-term use, the Asset Management Team is developing an asset management plan for the assets owned by the Council. When a capital asset is no longer needed for council purposes and surplus to requirements, it may be sold so that the proceeds, known as Capital Receipts, can be used to finance the acquisition of new assets or used to repay debt. The Council does not currently have a land disposal programme for the General Fund identifying assets for disposal, as the Council's current policy is to use any surplus land and property which is identified, for Housing purposes. Therefore it is unlikely that any General Fund Capital Receipts will be received in the future.

7.2 There are specific regulations about the extent to which Capital Receipts from sales of Council Houses can be used to finance new capital expenditure. Repayments of capital grants, loans and investments also generate capital receipts. The Council does not anticipate any General Fund capital receipts in the coming financial year. The estimate of Capital Receipts is set out below:

Table 5: Capital receipts in £ millions

	2018/19 Actual £m	**2019/20 Forecast £m**	**2020/21 Budget £m**	**2021/22 Budget £m**	**2022/23 Budget £m**
HRA Disposals	1.843	1.325	1.429	1.461	1.493
GF Disposals	0.973	0	0	0	0
Loans repaid	0.318	0.634	0.329	0.318	0.318
TOTAL	**3,134**	**1.959**	**1.758**	**1.779**	**1.811**

8. Treasury Management

8.1 Treasury management is concerned with keeping sufficient but not excessive cash available to meet the Council's spending needs, while managing the risks involved. Surplus cash is invested until required, while a shortage of cash will be met by borrowing, to avoid excessive credit balances or overdrafts in the bank current account. The Council is typically cash rich in the short-term as revenue income is received before it is spent, but cash poor in the long-term as capital expenditure is incurred before being financed. The revenue cash surpluses are offset against capital cash shortfalls to reduce overall borrowing.

8.2 Due to decisions taken in the past, the Council currently has borrowing of £105m at an average interest rate of 2.7 % and treasury investments totalling £26.1m at an average rate of 2.4%.

8.3 <u>Borrowing Strategy-</u> the Council's main objectives when borrowing are to achieve a low but certain cost of finance while retaining flexibility should plans change in future. These objectives are often conflicting, and the Council therefore will aim to strike a balance between cheap short-term loans (currently available at around 0.70%) and long-term fixed rate loans where the future cost is known but higher (currently 2.0 to 3.0%).

Table 6: Prudential Indicator: Forecast Gross Debt and the Capital Financing Requirement in £ millions

	31.3.2019 Actual £m	**31.3.2020 Forecast £m**	**31.3.2021 Budget £m**	**31.3.2022 Budget £m**	**31.3.2023 Budget £m**
HRA Debt	61.189	61.189	64.803	69.953	69.953
General Fund Debt	26.099	81,555	148.529	213.633	214.075
Total Debt	**87.288**	**142.744**	**213.332**	**283.586**	**284.028**
Capital Financing Requirement	73.793	156.101	238.074	316.470	322,082
CFR not funded by Borrowing	(13,495)	13.357	24.742	32.884	38.054

8.4 Statutory guidance is that debt should remain below the capital financing requirement, except in the short-term. As can be seen from table 6, the Council expects to comply with this. The CFR not funded by Borrowing is funded principally from the HRA Revenue Budget, HRA Capital Receipts and DFG Grant.

8.5 Borrowing in advance of need

8.5.1 Government Guidance is that local authorities must not borrow in advance of their needs purely in order to profit from the investment of the extra sums borrowed. The Authority has chosen not to follow this guidance and has plans to borrow to invest in property assets to support the economic development of the District and to deliver a financial return to support the provision of services.

8.6 Affordable borrowing limit: The Council is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt) each year. In line with statutory guidance, a lower "operational boundary" is also set as a warning level should debt approach the limit. In order to determine whether the proposed borrowing as set out in the CFR is affordable. The Council has considered the extent to which borrowing can be funded by the General Fund and HRA revenues as determined by the Medium Term Financial Strategy and HRA Business Plan. The Council has also assessed the anticipated commercial property investment income which directly offsets the cost of borrowing. The Council will only engage in borrowing to support commercial property investment where the target return receivable significantly exceeds the cost of borrowing. Future returns are secured on the appropriate use of fixed rate borrowing.

Table 7: Prudential Indicators: Authorised limit and operational boundary for external debt in £m

	2019/20 limit £m	**2020/21 limit £m**	**2021/22 limit £m**	**2022/23 limit £m**
Authorised limit – borrowing	201	215	285	285
Authorised limit – PFI and leases	0	0	0	0
Authorised limit – total external debt	201	215	285	285
Operational boundary – borrowing	196	210	280	280
Operational boundary – PFI and leases	0	0	0	0
Operational boundary – total external debt	196	210	280	280

8.7 Further details on borrowing are set out in Para 5.5 of the Treasury Management Strategy

8.8 Investment strategy- Treasury investments arise from receiving cash before it is paid out again. Investments made for service reasons or for pure financial gain are not generally considered to be part of treasury management.

8.9 The Council's policy on treasury investments is to prioritise security and liquidity over yield, that is to focus on minimising risk rather than maximising returns. Cash that is likely to be spent in the near term is invested securely, for example with the government, other local authorities or selected high-quality banks, to minimise the risk of loss. Money that will be held for longer terms is invested more widely, including in bonds, shares and property, to balance the risk of loss against the risk of receiving returns below inflation. Both short term and medium term investments may be held in pooled funds, where an external fund manager makes decisions on which particular investments to buy and the Council may request its money back at short notice.

Table 8: Treasury management investments in £millions

	31.3.2019 Actual £m	31.3.2020 Forecast £m	31.3.2021 Budget £m	31.3.2022 Budget £m	31.3.2023 Budget £m
Short Term Investments*	20.0	6.0	6.0	6.0	6.0
Medium Term investments	5.8	5.8	5.8	5.8	5.8
Long Term Investments	11.6	28.5	45.0	45.0	45.0
TOTAL	**37.4**	**40.3**	**56.8**	**56.8**	**56.8**

* 31.3.19 actual includes a PWLB loan of £15.34m for the purchase of Quadrant House which was purchased in the following financial year

8.10 Further details on treasury investments are contained within the Treasury Management Strategy.

8.11 Governance- Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Director of Finance and staff, who must act in line with the treasury management strategy approved by Council. Regular reports on treasury management activity are presented to the Finance Committee.

9. Service Investments-Loans and Shares

9.1 Loans- the Council makes investments to assist local public services; including making loans to local service providers, local small businesses to promote economic growth and the Council's subsidiaries that provide services. In light of the public service objective, the Council is willing to take more risk than with treasury investments, however it still plans for such investments to generate a profit after all costs.

9.2 Security- the main risk when making service loans is that the borrower will be unable to repay the principal lent and/or the interest due. In order to limit this risk, and ensure that total exposure to service loans remains proportionate to the size of the Authority, upper limits on the outstanding loans to each category of borrower have been set as follows:

Table 9: Loans for service purposes in £ millions

Category of borrower	31.3.2020 Forecast			2020/21
	Balance owing	Loss allowance	Net figure in accounts	Approved Limit
Subsidiaries	19.293	0	19.293	19.3
Suppliers	1.589	0	1.589	2.6
TOTAL	**20.882**	**0**	**20.882**	**21.9**

9.3 Accounting standards require the Authority to set aside loss allowance for loans, reflecting the likelihood of non-payment. The figures for loans in the Authority's statement of accounts from 2018/19 onwards are shown net of this loss allowance. However, the Authority makes every reasonable effort to collect the full sum lent and has appropriate credit control arrangements in place to recover overdue repayments. At the end of 2017/18 there were no reasons to make a provision this will be kept under review in 2018/19

9.4 Risk assessment- The Council assesses the risks of loans before entering into and whilst holding service loans. The loan to the supplier is partly secured on a fixed asset and the balance is secured against a cash deposit.

Shares

9.5 Security- One of the risks of investing in shares is that they fall in value meaning that the initial outlay may not be recovered. In order to limit this risk, upper limits on the sum invested in each category of shares have been set as follows:

Table 10: Shares held for service purposes in £ millions

Category of company	31.3.2020 Forecast			2020/21
	Amounts invested £m	Gains or losses £m	Value in accounts £m	Approved Limit £m
Subsidiaries	5.318	0	5.318	11.000
TOTAL	**5.318**	**0**	**5.318**	**11.000**

9.6 The Council has provided two Service Loans one to a supplier (Freedom Leisure £2.225m) who provides the Council's outsourced leisure services. The other loan £15.002m is favour of the Council's subsidiary Gryllus Property Ltd. The Council plans to set aside a reserve of £150,000 to finance any diminution in value of the investment and loan to Gryllus or any non-repayment of the Freedom Leisure Loan in 2019/20. The provision for loss will be reviewed annually.

9.7 Risk assessment- The investment in shares totalling £5.318m is within the Council's subsidiary Gryllus Property Ltd. The Authority assesses the risk of loss before entering into and whilst holding shares by assessing the current and future return achievable and the level of security provided by the assets of the company, and the level of control which the Council can exert over the strategy of the company. Gryllus is 100% owned and controlled by the Council. The Council also takes independent financial advice on investments. The Council plans to set aside a reserve of £150,000 to finance any diminution in value of the investment and loan to Gryllus or any non-repayment of the Freedom Leisure Loan in 2019/20. The provision for loss will be reviewed annually.

9.8 Liquidity- The funding of long term investments in the Council's subsidiary are financed by fixed long term borrowing, so that there is no short or medium term risk to the liquidity of the Council, which would require the Council to be forced to liquidate its asset in the company.

9.9 Non-specified Investments- Shares are the only investment type that the Authority has identified that meets the definition of a non-specified investment in the government guidance. The limits above on share investments are therefore also the Authority's upper limits on non-specified investments. The Authority has not adopted any procedures for determining further categories of non-specified investment since none are likely to meet the definition.

9.10 Governance- Decisions on service investments are agreed by Corporate Management Team led by the Chief Executive in consultation with the Director of Finance and must meet the criteria and limits laid down in the Commercial Property investment strategy. Most loans and shares are capital expenditure and purchases will therefore also be approved as part of the capital programme.

10. Commercial Property Investment

10.1 With central government financial support for local public services declining, the Council invests in commercial and residential property principally within the local area in pursuit of economic development objectives and financial gain and also lends to its subsidiary Gryllus Property Ltd.

Table 11: Property held for investment purposes in £ millions

Property	**Actual**	**31.3.2019 Actual**		**31.3.2020 expected**	
	Purchase cost £m	**Gains or (losses) £m**	**Value in accounts £m**	**Gains or (losses) £m**	**Value in accounts £m**
Redstone House	0.120	0.350	0.470	0.036	0.506
Linden House	4.434	0	4.434	0.155	4.589
Village Health Cub	0.860	0.064	0.924	0.010	0.937
Quadrant House	15.164	-	-	0	15.164
TOTAL	**20.578**	**0.414**	**5.828**	**0.201**	**21.196**

10.2 Security- In accordance with government guidance, the Authority considers a property investment to be secure if its accounting valuation is at or higher than its purchase cost including taxes and transaction costs.

10.3 A fair value assessment of the Authority's investment property portfolio has been made within the past twelve months, and the underlying assets provide security for capital investment. Should the 2019/20 year end accounts preparation and audit process value these properties below their purchase cost, then an updated investment strategy will be presented to full council detailing the impact of the loss on the security of investments and any revenue consequences arising therefrom.

10.4 **Risk assessment:** With financial return being a core objective, the Council accepts higher risk on commercial investment than with treasury investments. The principal risk exposures include near-term and longer-term risks, e.g. vacancies, fall in capital value, etc. These risks are managed by ensuring leases are with tenants of good financial standing and there is considerable before break clauses apply and the properties are of good quality in good locations. A varied portfolio will be acquired in diverse sectors thus spreading the risk. In order that commercial investments remain proportionate to the size of the authority, the Council has set an overall maximum investment limit of £200m. The Authority assesses the risk of loss before entering into and whilst holding property investments through independent advice sought from advisers. The Council has a risk matrix for assessing the quality of the investment to measure the suitability and risk of the investment, this is contained within the CPIS. To further mitigate risk, a provision will be set aside from rental income to mitigate the risks of voids and only properties with a significant period before the next break clause.

10.5 Liquidity- Compared with other investment types, property is relatively difficult to sell and convert to cash at short notice, and can take a considerable period to sell in certain market conditions. The funding of long term investments in the Council's subsidiary are financed by fixed long term borrowing, so that there is no short or medium term risk to the liquidity of the Council, which would require the Council to be forced to liquidate its asset and suffer a loss nor impact upon the Council's provision of services. As these long term investments are matched by long term borrowing, it will not be necessary to access the invested funds in an emergency. Investments in property are not undertaken unless they are secure over the medium term and the target rate of return significantly exceeds the annual cost of borrowing.

10.6 The Council's strategy for these Commercial Property Investments is covered by the Commercial Property Investment Strategy.

10.7 Governance- Decisions on commercial investments are made by the Chief Executive and Strategy and Resources Committee in line with the criteria and limits approved by Council in the CPIS. Property and most other commercial investments are also capital expenditure and purchases will therefore also be approved as part of the capital programme.

10.8 Further details on commercial property investments and limits on their use are set out in the CPIS.

11. Liabilities

11.1 In addition to debt of £67.8m at 31st March 2018 detailed above, the Council is committed to making future payments to cover its pension fund deficit (valued at £45.8m). This is revalued on a triennial basis, with the next valuation due in 2019. Payments are made based on a calculated contribution rate. The initial report of the actuary indicates that the current contribution rates will be maintained until the next valuation in 2022.

11.2 Governance- Decisions on incurring new discretional liabilities are taken by Corporate Management Team in consultation with the Acting Section 151 Officer. The risk of liabilities crystallising and requiring payment is monitored by Corporate Finance and reported as and when they are identified as part of regular financial monitoring.

11.3 Loan Commitments and Financial Guarantees

Although not strictly counted as investments, since no money has changed hands yet, loan commitments and financial guarantees carry similar risks. The Council has given no further formal loan commitments or guarantees to Gryllus Property Limited, Freedom Leisure or any other organisation. However the Council would consider any request for funding from its Gryllus Property Limited if required, subject to a suitable business case.

12. Proportionality

12.1 The Authority does not plan to be dependent on profit generating investment activity to achieve a balanced revenue budget. Table 4 below shows the extent to which the expenditure planned to meet the service delivery objectives and/or place making role of the Authority is dependent on achieving the expected net profit from investments over the lifecycle of the Medium Term Financial Plan. Should it fail to achieve the expected net profit, the Authority's contingency plans for continuing to provide these services will be to set side rental income in an income equalisation reserve and income will only be released from the reserve when earned. Income will only be used to support expenditure initiatives which by nature represent one off spending or are easily curtailed. Income from rental income will not be used to support statutory responsibilities.

Table 12: Proportionality of Investments

	2018/19 Actual £m	**2019/20 Forecast £m**	**2020/21 Budget £m**	**2021/22 Budget £m**
Net service expenditure	9.917	11.642	10.589	10.802
Investment rental income	0.216	1.143	1.143	1.143
Proportion	2.2 %	9.8%	10.8%	10.6%

13. Revenue Budget Implications

13.1 Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP are charged to revenue, offset by any investment income receivable. The net annual charge is known as financing costs; this is compared to the net revenue stream i.e. the amount funded from Council Tax, business rates and general government grants.

Table 13: Prudential Indicator: Proportion of financing costs to net revenue stream

	2018/19 Actual £m	2019/20 Forecast £m	2020/21 Budget £m	2021/22 Budget £m
Net service expenditure	9.917	11.642	10.589	10.802
General Fund- Financing costs	0.191	0.583	0.665	0.831
Proportion of General Fund net revenue stream	1.9%	5.0%	6.3%	7.7%

13.2 Further details on the revenue implications of capital expenditure are set out in the 2019/20 revenue budget.

13.3 Sustainability- Due to the very long-term nature of capital expenditure and financing, the revenue budget implications of expenditure incurred in the next few years will extend for up to 50 years into the future. The Acting Section 151 Officer is satisfied that the proposed capital programme is prudent, affordable and sustainable. The proportion that financing costs represent of the General Fund net revenue stream is negative. The most significant investments in waste vehicles and Ellice Road car park deliver a return equal to the financing costs. Property investments are determined on the basis of return. Unless the target rate of return is achieved Property Investments are not undertaken. The financing costs above exclude the cost of borrowing for property investments as these generate a return greater than the financing costs.

14. Knowledge, Skills, Capacity and Culture

14.1 The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. For example, the Interim Section 151 Officer is a qualified accountant with 20 years' experience, The Council pays for junior staff to study towards relevant professional qualifications including CIPFA, ACT (Treasury), where required.

14.2 Where Council staff do not have the knowledge and skills required, use is made of external advisers and consultants that are specialists in their field. The Council currently employs Link Asset Services as treasury management advisers and property advisers, this approach is more cost effective than employing such staff directly, and ensures that the Council has access to knowledge and skills commensurate with its risk appetite. Senior staff maintain their skills and knowledge up to date by attending technical briefings, circulars from treasury advisers and CIPFA treasury workshops. The Council also provides training for Councillors who are involved with Treasury and Pension matters.

Annex 1 to the capital and investment strategy 2020/21 to 2022/23

CAPITAL STRATEGY PRINCIPLES

Corporate Management Team led by the Chief Executive lead the strategic direction of capital investment for the Council.

All schemes already approved in the 2018/21 Continuing Capital Programme or contractually committed will be supported and sufficient resources will be provided to enable them to proceed or complete. These schemes are presented in Annex 3, Current Capital Priorities.

A capital project sponsor for a new bid must also be able to demonstrate that a rigorous process of options appraisal has been followed, requiring evidence of need, cost, risk, outcomes and methods of financing. Capital investment proposals which will result in a revenue cost saving, income generation or efficiency are encouraged. The Corporate Management Team has a clear role in ensuring that all the key questions have been asked at the initiation stage of a project.

All capital investment decisions will be made with reference to Council objectives and regional strategies and, only after a positive contribution to one or more of the objectives has been demonstrated, is a project to be considered for resource allocation. There will be no ring-fencing of capital receipts to specific projects.

The capital strategy will support the implementation of the approved Commercial Property Investment Strategy (CPIS) by the allocation of resources and facilitating the introduction of activities required to promote the objectives of the strategy which include providing a sustainable income stream to support the Council's revenue budget from the acquisition of property assets.

For the purposes of preparing the Capital Strategy and Capital Programme for 2019/20, an assumption has been made that any funding relating to slippage in capital projects at the end of 2018/19 will be carried forward into 2019/20 to fund the completion of the projects. Where an underspend occurs this will be returned to the Council Capital resources and will be used to fund new capital priorities. Funding for any overspends will be taken from the Council's uncommitted capital resources.

As well as using traditional funding mechanisms to finance capital schemes, the Council will also consider the use of new initiatives and develop these options if it is considered financially advantageous in the context of the Council achieving its capital investment objectives.

The Council is conscious that the Government could in the future introduce a range of grant funding opportunities for which bids must be submitted at short notice, some of which may have a matched funding requirement. The Council will respond as it considers appropriate to bidding opportunities, ensuring that bids are submitted which align with its objectives and capital investment priorities and that matched funding requirements are considered on a scheme by scheme basis with resource requirements prioritised accordingly.

The Council will work in a collaborative manner with Surrey County Council, Surrey Police & NHS.

Regard will be given during the appraisal process to ensure that the Council's Key Objectives and capital investment priorities are achieved.

- The Council will seek to make best use of opportunities offered by the Government to invigorate the housing market, empower first time buyers and to reduce homelessness by a comprehensive package of new policies to raise housing supply.

- The Council will have a number of capital investment priorities. Whilst these are initially set on an annual basis, it will review and update the priorities in accordance with in-year developments, responding to local and national emerging issues. The draft Capital Programme 2018-2022 set out at Annex 7 reflects the Council's current Strategies and Priorities.

Annex 2 to the capital and investment strategy 2020/21 to 2022/23

CAPITAL STRATEGIC PRIORITIES

Existing Programmes 2019/20

There is a requirement for continued funding of existing programmes of work on:

Council Offices Maintenance Programme this covers; Corporate Major Repairs, Disability Discrimination Act (DDA) Adaptations, Legionella and Health and Safety projects (Corporate Landlord Function)
Council Houses - Works to maintain dwellings to a Decent Homes Standard
Council House Building Programme
Housing Management Software
Disabled Facilities Improvements
Affordable Housing/Housing Enabling
Children's Playgrounds
Parks, Pavilions & Open Spaces
Vehicle Fleet Renewals
Waste Collection Containers
Information Technology
Car Parks
Commercial Property Investment Fund

Additions to existing Programmes and New Projects 2019/20-2021/22

In addition to the projects specifically referred to above, the following is a list of additions to funding to extending existing programmes or new projects for which funding may be required:

Extension to the Council House Building Programme
Extension to HRA Business Plan works to maintain dwellings to a Decent Homes Standard
Extension to the Disabled Facilities Improvements
Extension to the Affordable Housing Programme
Extension to the Playground Improvements Programme
Extension to the Parks, Pavilions & Open Spaces Programme
Extension to Vehicle Fleet Renewals
Extension to Car Park Equipment
Extension to Commercial Property Investment Fund
Public Conveniences
Litter Bins
Cemetery-Roads & Paths
Land Drainage
Plant & Machinery Replacement Programme
Replacement of Waste Vehicles
Garden Waste Bins
IT – Hardware, Infrastructure. Customer First Projects

Annex 3 to the capital and investment strategy 2020/21 to 2022/23

SOURCES OF CAPITAL FUNDING

External Resources

External resources from Central Government and other public sector bodies can be split into two categories:

Un ring-fenced – resources which are delivered through grant that can be utilised on any project (albeit that there may be an expectation of use for a specific purpose). This now encompasses the vast majority of Government grant funding.

Ring-fenced – resources which are ring-fenced to particular areas and therefore have restricted uses. e.g. Disabled Facilities Grant

Where there is a requirement to make an application to an external agency for external funding and, when appropriate, to commit Council resources as matched funding to any bid for external resources, a business case must be presented to the Corporate Management Team for approval. This must justify the bid for external resources and any Council matched funding prior to submission of the bid.

Examples of ring-fenced grants for which the Council can bid for capital projects include Arts Council Grants and Heritage Lottery Grants.

Additional Government grant funding notifications and these will be incorporated into the programme as appropriate.

Own Resources

Capital Receipts

Section 9 (1) of the Local Government Act 2003 defines a capital receipt as ‘’a sum received by the authority in respect of the disposal by it of an interest in a capital asset’’.
Section 9 (2) of the Act defines a capital asset as ‘’an asset is a capital asset if, at the time of the disposal, expenditure on the acquisition of the asset would be capital expenditure’’.

Capital receipts are usually restricted to use for:
i) Financing new capital investment.
ii) Reducing borrowing under the Prudential Framework.
iii) Paying a premium charged in relation to any amounts borrowed.
iv) Meeting any liability in respect of credit arrangements.
v) Meeting disposal costs (not exceeding 4% of the receipt).

Following the 2015 Spending Review, the DCLG published statutory guidance on the flexible use of capital receipts for a three year period covering 2016/17 to 2018/19. The guidance allows Local Authorities to use capital receipts to offset the revenue cost of transformational projects which are expected to deliver future ongoing revenue savings. As part of 2018/19 Provisional Local Government Finance Settlement, the Secretary of State announced an extension of this flexibility for a further three years to 2022.

In 2018/19, the Council intends to use up to £0.589m of capital receipts to fund elements of Tandridge’s Capital Programme, specifically:

- the Customer First programme;
- Investment in the modernisation of IT systems;

In general capital receipts arising from the disposal of housing assets and for which account is made in the Housing Revenue Account (HRA), are governed by the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003. In summary the regulations require that receipts arising from:

Right to Buy (and similar) sales may be retained to cover the cost of transacting the sales and to cover the debt on the properties sold, but a proportion of the remainder must be surrendered to Central Government;

However exemptions from the regulations were published in 2012 which enable the Council to use Housing Capital receipts to part finance the replacement of homes for rent sold under the renewed Right to Buy, including purchasing, remodelling and new build

HRA disposals may be retained in full provided they are spent on affordable housing, regeneration or the paying of housing debt.

Ring-fencing of Capital Receipts

The Council will not ring-fence or earmark capital receipts to specific projects, projects will be considered on the costs and benefits of the individual project.

Capital Receipts will be retained to support the Capital Programme as a corporate resource.

Availability of Capital Receipts

In considering the 2018/19 capital programme, and given the position with regard to capital receipts, a prudent approach has been taken and there has been no assumption of any additional capital receipts to finance new expenditure over and above those already known amounts underpinning the programme.

No additional capital receipts have been anticipated in 2019/20 and 2020/21. However as advised above, the Council anticipates using up to £0.589m of capital receipts in 2018/19 to support projects.

The level of receipts upon which the programme relies to fund existing and new commitments has in the past been affected by the property market which has impacted on the:

i) Ability of the Council to sell assets within the timescale anticipated.

ii) Level of receipt actually generated, which has sometimes been less than originally expected.

Monitoring of capital receipts is undertaken through the CMT and the Corporate Property Board (CPB); follow-up actions are initiated to address any comments raised.

Revenue Contributions

A service or the Council may wish to offer some of its revenue budget or reserves to support the financing of a capital project.

Leasing

Some of the assets used by the Council are financed by a lease arrangement, for example vehicles. With the advent of Prudential Borrowing this source of financing is less attractive. As it is usually generally a more expensive form of borrowing and there are usually costs which arise when vehicles, plant and equipment is returned in poor condition. Therefore it is the Councils policy not to lease unless it can be demonstrated that leasing will offer value for money, when options are appraised.

Section 106 Agreements

In considering an application for planning permission, the Council may seek to secure benefits to an area or restrict uses or activities related to a proposed development through the negotiation of a 'planning obligation' with the developer. Such obligations, authorised by Section 106 of the Town and Country Planning Act 1990, generally either improve the quality of the development, or overcome difficulties which would otherwise result in planning permission being refused. A planning obligation must be:

i) Necessary to make the development acceptable in planning terms;

ii) Directly related to the development; and

iii) Fairly and reasonably related in scale and kind to the development.

As such, therefore, the Council may in some instances receive funds to enable it to undertake works arising from these planning obligations. Examples of the use of planning obligations are the:

i) Provision of affordable housing.

ii) Improvement to community facilities - Public open space/play areas, educational facilities.

iii) Improved transport facilities - contributions have previously been used towards Oldham bus station, park and ride and provision of cycle lanes.

iv) Public art.

v) Renewable energy measures.

vi) Specific measures to mitigate impact on a local area - parking restrictions, landscaping or noise insulation.

The use of any Section 106 funding will be presented to the CMT for review.

Community Infrastructure Levy

The Community Infrastructure Levy (CIL) is a planning charge based on legislation that came into force on 6 April 2010. When adopted, a CIL levy allows the Council to raise contributions from new development to help pay for infrastructure that is needed to support planned growth. CIL contributions can be used to supplement other funding streams and can wholly or partly fund a variety of strategic infrastructure projects ranging from transport, green infrastructure, flood defences, education and health, subject to pooling restrictions.
Where a CIL charging schedule is in place, it largely replaces Section 106 Obligations in delivering strategic infrastructure. However, S106 would still be used for affordable housing and site development-related infrastructure requirements that are deemed necessary to make a development acceptable. Some developments would pay both Section 106 and CIL, but they would fund different types of infrastructure. Contributions may also be sought for Section 278 of the Highways Act where modifications are required to the highways network.

UK Municipal Bonds Agency Plc formerly Local Capital Finance Company

The Local Government Association (LGA) has now set up the Local Capital Finance Company (formerly known as the UK Municipal Bonds Agency) the aim of which is to seek to provide Councils with a cheaper source of long term borrowing and to introduce sector owned diversity into the Local Government lending market. The Council will keep under review the availability and cost of funds from the Company as an alternative source of finance with a view to borrowing at an appropriate time if terms are preferential.

Borrowing

The Council will investigate opportunities to resource capital projects using prudential borrowing where plans are sustainable, affordable and prudent. Full appraisal will take place to ensure that, where appropriate, sufficient revenue returns are generated to cover the cost of borrowing. This will be especially important when undertaking property acquisitions under the Commercial Property Investment Strategy (CPIS) where, in addition, a revenue income stream is required to support the revenue budget.

Where it is considered that Prudential Borrowing is the appropriate method of funding it will require additional revenue budget to finance the interest and minimum revenue provision.

Strategy and Resources Committee will review the detailed capital expenditure plans before allocations of resources are committed to ensure that the costs of prudential borrowing are understood and affordable.

The Council is able to take advantage of the Public Works Loans Board (PWLB) certainty rate, whereby there is a 20 basis points discount on standard loans from the PWLB under the prudential borrowing regime for authorities which provide improved information on their long term borrowing and associated capital spending plans. The obvious benefit to the Council of the certainty rate is reflected in reduced Treasury Management borrowing costs in relation to any PWLB borrowing undertaken.

Annex 4 to the capital and investment strategy 2020/21 to 2022/23

CORPORATE GOVERNANCE

Corporate Management Team

Corporate Management Team, which comprises the Directors of each Department lead by the Chief Executive, is the officer body for Capital Investment development and planning and is charged with bringing forward funded capital expenditure plans for approval by the Strategy and Resources Committee. Strategy and Resources Committee considers capital expenditure and funding plans and for monitoring performance through a series of regular capital monitoring reports and recommends the annual Capital Programme to Council for approval.

All Directorates are represented at Director Level on CMT supported by the Interim Chief Finance Officer.

All capital investment will be commissioned on the recommendation of the CMT which will enable any expenditure and it’s funding to be aligned with the Council’s Key Capital Priorities and funding sources. Partners, from both the public and private sector will be at regional and local levels as well as at a district level.

Approval of Capital Investment

Within the Council, a concept for a potential capital project will originate from, or at least be ‘owned’ by the Director. The ‘owner’ should prepare, or direct the preparation of a Strategic Business Case (SBC) for the proposed project. The Strategic Business Case outlining the initial idea or ‘concept’ for a project and should be submitted to CMT for consideration.

If CMT is satisfied that the proposal meets investment criteria, it will be given approval to progress to Stage 2 of the process – the completion of an Outline Business Case (OBC).

The OBC builds on the SBC providing more detailed information including the benefits that could be realised focusing on the links to the Council’s Capital Investment Priorities and the proposed outcomes and may include a number of options to deliver the proposed benefits. The OBC will be submitted to the CMT for consideration, and if it is satisfied with the proposal will give guidance for the development of a preferred option.

Stage 3 of the process entails the completion of a Final Business Case (FBC) which will then be submitted to the CMT for final consideration. Again, building on the OBC, the FBC will contain evidence of a:

- Full option appraisal
- Detailed financial analysis of all costs/income including how the project is financially sustainable and that any adverse revenue implications can be dealt with within existing budgets.
- Robust delivery plan including how the chosen option delivers the highest impact in achieving the required outcomes with identified key project milestones enabling progress review. Included within the delivery plan should be proposed consultation arrangements, value for money assessment equality and environmental impact assessments.
- Risk assessment and that appropriate actions to negate these risks have been identified.
- Full exit strategy where the project involves a disposal.
- Method of procurement that represents value for money.

Depending on the circumstances of the bid for resources, CMT has the discretion to vary the three stage review process and omit one or more of the stages.

Once Final Business Cases have been agreed for bids, these bids will be prioritised using the following criteria (it should be noted that these bids will be ranked in the following order):

The criteria examine whether the proposal is:

- Fully-funded from external resources.
- Related to mandatory, contractual or legislative service delivery requirements.
- Required to achieve the delivery of a specific revenue budget saving within the revenue budget setting process.
- Providing general revenue saving or offering the delivery of a more efficient service.
- Enables and supports the implementation of the Commercial Property Investment Strategy
- Supporting regeneration and economic growth, particularly in the town centre and district centres.
- Required to support Service Plan priorities.
- Bringing in substantial external resources for which Council matched funding is required.
- Delivers the aim of local jobs for local people.
- Supporting integrated working with NHS partners
- Linked into other regional objectives.
- Enhancing the asset management/estate management agenda.
- Makes a contribution to carbon reduction targets and renewable energy initiatives

The results of this process will be presented to Members each year as part of the capital budget setting process, or during the year if projects come forward outside the normal timeframe.

Service Challenge & Review, Efficient Use of Assets

With regard to the review of operational assets, the Asset Management Team and services continue to work closely with service managers alongside wider public and third sector partners to ensure that portfolios are best fit for purpose and efficient usage is maximised.

The Chief Executive and CMT will oversee any acquisition and disposal of land and property assets and monitors the progress of any corporate disposals and performance of the investment portfolio.

In terms of acquisition of Commercial Property Investment there is a specific process for this under Financial Regulation 17 to enable proposals to progress in year. Details of this are set out in the Commercial Property Investment Strategy.

Performance Monitoring of Capital Programme

The capital expenditure investment approach above is supported by a strong programme management process in order to ensure a coordinated corporate approach. This will ensure that investments are planned, managed and delivered prudently.

CMT has a remit to review the financial performance of the capital programme and it receives a monthly monitoring report. In addition financial monitoring reports will be considered by Strategy and Resources Committee at months 3, 6, 8 and 9, together with a capital outturn report. Issues that have been considered and agreed at CMT can be reported to Strategy and Resources as necessary via the regular financial monitoring reports.

The undertaking of the detailed annual review of the capital programme provides the opportunity to review all schemes or focus on specific areas of concern.

Where a potential cost overrun has been identified, CMT will explore possible solutions in detail. It will also consider any under spending or identified surplus resources which can be added to the central pool of resources. CMT may also suggest a reallocation of resources to other projects.

Where there is a delay in the commitment of programme/project resources, the CMT will require project managers to report the reasons for the delay and consider whether it would be appropriate to recommend the decommissioning of the project and the reallocation of un-ring-fenced resources to other projects.

The performance of the capital programme is also measured by the prudential indicators which are reported Council as part of the Treasury Management Strategy, the Treasury Management half-yearly review, and the annual review.

Annex 5 to the capital and investment strategy 2020/21 to 2022/23

ANNUAL MINIMUM REVENUE PROVISION POLICY STATEMENT 2019/20

Where the Council finances capital expenditure by debt, it must put aside resources to repay that debt in later years. The amount charged to the revenue budget for the repayment of debt is known as Minimum Revenue Provision (MRP), although there has been no statutory minimum previous to 2017/18. The Local Government Act 2003 requires the Council to have regard to the Department for Housing, Communities and Local Government's Guidance on Minimum Revenue Provision (the CLG Guidance) most recently issued in 2018.

The broad aim of the MHCLG Guidance is to ensure that debt is repaid over a period that is either reasonably commensurate with that over which the capital expenditure provides benefits, or, in the case of borrowing supported by Revenue Grant, reasonably commensurate with the period implicit in the determination of that grant.

The CLG Guidance requires the Council to approve an Annual MRP Statement each year and recommends a number of options for calculating a prudent amount of MRP. The following statement incorporates options recommended in the Guidance.

The Council expects that its Capital Financing Requirement will be a maximum of £238.074m (General Fund £149.429m) at 31st March 2020 and in line with the MHCLG Guidance it will therefore charge MRP on an asset life basis. This basis is subject to review and changes in line with the Councils Treasury Management Strategy and approved Prudential Indicators which are revised annually.

Capital expenditure incurred during 2019/20 will be fully subject to a MRP charge from 2020/21 onwards. Capital expenditure incurred during 2020/21 will be subject to a MRP charge from 2021/22 onwards. This ensures that MRP is only charged to the full first operational year of the assets life.

The Council is recommended to approve the following MRP Statement:-

For all unsupported borrowing (General Fund) the MRP Policy will be; Asset Life Method.

Under this method MRP will be based on the estimated life of the assets, in accordance with the regulations. This option provides for a reduction in the borrowing need over approximately the estimated assets life.

There are two methods of calculating charges under this option; equal instalment method (equal payments over asset life) and the annuity method (gradually increases over asset life).

Both methods allow costs to be spread over the full life of the asset.

The Council will utilise the annuity method.

Annex 6 to the capital and investment strategy 2020/21 to 2022/23

Investment Indicators

The Authority has set the following quantitative indicators to allow elected members and the public to assess the Authority's total risk exposure as a result of its investment decisions.

Total risk exposure: The first indicator shows the Authority's total exposure to potential investment losses. This includes amounts the Authority is contractually committed to lend but have yet to be drawn down and guarantees the Authority has issued over third party loans.

Table 5: Total investment exposure in £millions

Total investment exposure	31.03.2019 Actual £m	31.03.2020 Forecast £m	31.03.2021 Forecast £m
Treasury Management Investments	33.933	26.400	26.400
Service Investments: Loans	4.627	16.700	33.200
Service Investments: Shares	1.026	5.300	10.800
Commercial Investments: Property	5.828	21.200	43.200
TOTAL INVESTMENTS	**45.414**	**69.600**	**113.600**
Commitments to lend	0	0	0
Guarantees issued on loans	0	0	0
TOTAL EXPOSURE	**45.414**	**69.600**	**113.600**

How investments are funded: Government guidance is that these indicators should include how investments are funded. Since the Authority does not normally associate particular assets with particular liabilities, this guidance is difficult to comply with. However, the following investments could be described as being funded by borrowing. The remainder of the Authority's investments are funded by usable reserves and income received in advance of expenditure.

Table 6: Investments funded by borrowing in £millions

Investments funded by borrowing	31.03.2019 Actual £m	31.03.2020 Forecast £m	31.03.2021 Forecast £m
Treasury management investments	0	0	0
Service Investments: Loans	4.627	16.700	33.200
Service Investments: Shares	1.026	5.300	10.800
Commercial investments: Property	5.332	20.694	42.694
TOTAL FUNDED BY BORROWING	**10.985**	**42.694**	**86.694**

Rate of return received: This indicator shows the investment income received less the associated costs, including the cost of borrowing where appropriate, as a proportion of the sum initially invested. Note that due to the complex local government accounting framework, not all recorded gains and losses affect the revenue account in the year they are incurred.

Table 7: Investment rate of return (net of all costs)

Investments net rate of return	**2018/19 Actual**	**2019/20 Forecast**	**2020/21 Forecast**
Long Term Treasury Management investments	4.1%	4.1%	4.1%
Service Investments: Loans	3.1%	2.9%	2.4%
Service Investments: Shares	0%	0%	0%
Commercial Investments: Property	4.0%	3.3%	3.0%

Table 8: Other investment indicators

Indicator	**2018/19 Actual**	**2019/20 Forecast**	**2020/21 Forecast**
Debt to net service expenditure ratio	263%	700%	1,403%
Commercial income to net service expenditure ratio	2.25%	9.8%	10.8%

Proposed Capital Programme 2020-2023

Annex 7 to the capital and investment strategy 2020/21 to 2022/23

Current Continuing Capital Schemes	Revised Capital Programme reflecting 2018/19 Slippage (S&R Committee 26/11/19) and Housing Committee Changes 19th Sept 2019: Current Budget 2019/20	Revised Budget 2020/21	Revised Budget 2021/22	Revised Budget 2022/23	Total Budget 2019/20-2021/22	New Bids/ Revisions 2019/20	New Bids/ Revisions 2020/21	New Bids/ Revisions 2021/22	New Bids/ Revisions 2022/23	New Bids/ Total	Current Budget 2019/20	Proposed Budget 2020/21	Proposed Budget 2021/22	Proposed Budget 2022/23	Proposed Budget Total 2019-2023
Housing HRA															
Structural Works	755,000	480,000	795,000		2,030,000		225,000	40,000	855,000	1,120,000	755,000	705,000	835,000	855,000	3,150,000
Modernisation & Improvements	654,000	800,000	392,000		1,846,000		(34,500)	47,000	752,000	764,500	654,000	765,500	439,000	752,000	2,610,500
Energy Efficiency Works	393,000	448,000	481,000		1,322,000		93,500	189,500	679,500	962,500	393,000	541,500	670,500	679,500	2,284,500
Service Renewals	628,000	620,000	445,000		1,693,000		(9,000)	240,000	712,500	943,500	628,000	611,000	685,000	712,500	2,636,500
Void Works	490,000	450,000	395,000		1,335,000		(25,000)	30,000	425,000	430,000	490,000	425,000	425,000	425,000	1,765,000
Health & Safety	175,000	175,000	200,000		550,000		(85,000)	(105,000)	95,000	(95,000)	175,000	90,000	95,000	95,000	455,000
Adaptations for the Disabled	232,500	225,000	225,000		682,500		0	0	225,000	225,000	232,500	225,000	225,000	225,000	907,500
Essential Structural Works	175,000	135,000	125,000		435,000		(75,000)	(65,000)	60,000	(80,000)	175,000	60,000	60,000	60,000	355,000
Communal Services	75,000	90,000	70,000		235,000		95,000	115,000	185,000	395,000	75,000	185,000	185,000	185,000	630,000
Council House Building	8,345,600	14,351,300	3,660,000		26,356,900	(1,626,300)	(3,934,100)	5,295,400	447,200	182,200	6,719,300	10,417,200	8,955,400	447,200	26,539,100
Housing Management Software	81,100	20,000	20,000		121,100						81,100	20,000	20,000	0	121,100
Total- Housing HRA	**12,004,200**	**17,794,300**	**6,808,000**	**0**	**36,606,500**	**(1,626,300)**	**(3,749,100)**	**5,786,900**	**4,436,200**	**4,847,700**	**10,377,900**	**14,045,200**	**12,594,900**	**4,436,200**	**41,454,200**
Housing GF															
Disabled Facilities Grant	439,100	426,000	426,000		1,291,100	0	0	0	460,000	460,000	439,100	426,000	426,000	460,000	1,751,100
Housing Enabling - General	274,400	100,000	100,000		474,400	(274,400)	0	0	0	(274,400)	0	100,000	100,000	0	200,000
Total- Housing GF	**713,500**	**526,000**	**526,000**	**0**	**1,765,500**	**(274,400)**	**0**	**0**	**460,000**	**185,600**	**439,100**	**526,000**	**526,000**	**460,000**	**1,951,100**
Community Services															
Children's Playground Improvements	116,600	75,000	75,000		266,600	0	190,000	75,000	165,000	430,000	116,600	265,000	150,000	165,000	696,600
Parks, Pavilions & Open Spaces	188,400	100,000	100,000		388,400	0	0	0	100,000	100,000	188,400	100,000	100,000	100,000	488,400
Vehicle Fleet Renewals	59,900	40,000	40,000		139,900	0	444,000	270,000	163,000	877,000	59,900	484,000	310,000	163,000	1,016,900
Collection / Containerisation	600,000	0	0		600,000						600,000	0	0	0	600,000
Car Park Equipment/Maintenance	58,200	30,000	0		88,200						58,200	30,000	0	0	88,200
Ellice Road Car Park Decking	4,325,100	0	0		4,325,100	(4,225,100)				(4,225,100)	100,000	0	0	0	100,000
Public Conveniences	275,000	275,000	0		550,000						275,000	275,000	0	0	550,000
Litter Bins	20,000	2,000	2,000		24,000	0	0	0	2,000	2,000	20,000	2,000	2,000	2,000	26,000
Roads&Paths at St.Mary's Church Cemetery	20,000	0	0		20,000						20,000	0	0	0	20,000
Land Drainage	10,000	10,000	10,000		30,000						10,000	10,000	10,000	0	30,000
Plant & Machinery Replacement Programme	8,000	8,000	8,000		24,000	0	43,000	0	8,000	51,000	8,000	51,000	8,000	8,000	75,000
Waste Vehicles	3,500,000	0	0		3,500,000						3,500,000	0	0	0	3,500,000
Garden Waste Bins	96,000	15,000	15,000		126,000	(96,000)	96,000	0	15,000	15,000	0	111,000	15,000	15,000	141,000
Recycling, food waste and refuse bins	0	0	0		0	0	100,000	100,000	100,000	300,000	0	100,000	100,000	100,000	300,000
Playground Improvements (Match Funding Pot)	50,000	0	0		50,000						50,000	0	0	0	50,000
Total- Community Services	**9,327,200**	**555,000**	**250,000**	**0**	**10,132,200**	**(4,321,100)**	**873,000**	**445,000**	**553,000**	**(2,450,100)**	**5,006,100**	**1,428,000**	**695,000**	**553,000**	**7,682,100**
Resources															
Council Offices Major Maintenance Programme	182,300	100,000	0		282,300						182,300	100,000	0	0	282,300
Customer First/IT	150,000	150,000	50,000		350,000						150,000	150,000	50,000	0	350,000
IT - Hardware/infrastructure/Customer First Projects					0		723,600	154,800	163,400	1,041,800	0	723,600	154,800	163,400	1,041,800
Investment & Development Fund	130,374,900	65,000,000	0		195,374,900	(64,374,900)		64,374,900		0	66,000,000	65,000,000	64,374,900	0	195,374,900
Land / Asset Development	153,000	0	0		153,000					0	153,000	0	0	0	153,000
Total- Resources	**130,860,200**	**65,250,000**	**50,000**	**0**	**196,160,200**	**(64,374,900)**	**723,600**	**64,529,700**	**163,400**	**1,041,800**	**66,485,300**	**65,973,600**	**64,579,700**	**163,400**	**197,202,000**
Total Capital Programme	**152,905,100**	**84,125,300**	**7,634,000**	**0**	**244,664,400**	**(70,596,700)**	**(2,152,500)**	**70,761,600**	**5,612,600**	**3,625,000**	**82,308,400**	**81,972,800**	**78,395,600**	**5,612,600**	**248,289,400**

Proposed Capital Programme 2020-2023 - Financing

Annex 8 to the capital and investment strategy 2020/21 to 2022/23

Current Continuing Capital Schemes	Current Budget 2019/20	Proposed Budget 2020/21	Proposed Budget 2021/22	Proposed Budget 2022/23	Proposed Budget Total 2019-2023	HRA Reserves	DFG Grant	CIL/S106 Contributions	GF Cap Receipts/Reserves	Hsg Capital Receipts	Housing Developer Contribution	Borrowing	Total Financing
Housing HRA													
Structural Works	755,000	705,000	835,000	855,000	3,150,000	3,150,000							3,150,000
Modernisation & Improvements	654,000	765,500	439,000	752,000	2,610,500	2,610,500							2,610,500
Energy Efficiency Works	393,000	541,500	670,500	679,500	2,284,500	2,284,500							2,284,500
Service Renewals	628,000	611,000	685,000	712,500	2,636,500	2,636,500							2,636,500
Void Works	490,000	425,000	425,000	425,000	1,765,000	1,765,000							1,765,000
Health & Safety	175,000	90,000	95,000	95,000	455,000	455,000							455,000
Adaptations for the Disabled	232,500	225,000	225,000	225,000	907,500	907,500							907,500
Essential Structural Works	175,000	60,000	60,000	60,000	355,000	355,000							355,000
Communal Services	75,000	185,000	185,000	185,000	630,000	630,000							630,000
Council House Building	6,719,300	10,417,200	8,955,400	447,200	26,539,100	11,948,100				5,227,000	400,000	8,964,000	26,539,100
Housing Management Software	81,100	20,000	20,000	0	121,100	121,100							121,100
Total- Housing HRA	**10,377,900**	**14,045,200**	**12,594,900**	**4,436,200**	**41,454,200**	**26,863,200**	**0**	**0**	**0**	**5,227,000**	**400,000**	**8,964,000**	**41,454,200**
Housing GF													
Disabled Facilities Grant	439,100	426,000	426,000	460,000	1,751,100		1,751,100						1,751,100
Housing Enabling - General	0	100,000	100,000	0	200,000					200,000			200,000
Total- Housing GF	**439,100**	**526,000**	**526,000**	**460,000**	**1,951,100**	**0**	**1,751,100**	**0**	**0**	**200,000**	**0**	**0**	**1,951,100**
Community Services													
Children's Playground Improvements	116,600	265,000	150,000	165,000	696,600			696,600					696,600
Parks, Pavilions & Open Spaces	188,400	100,000	100,000	100,000	488,400			488,400					488,400
Vehicle Fleet Renewals	59,900	484,000	310,000	163,000	1,016,900							1,016,900	1,016,900
Collection / Containerisation	600,000	0	0	0	600,000							600,000	600,000
Car Park Equipment/Maintenance	58,200	30,000	0	0	88,200							88,200	88,200
Ellice Road Car Park Decking	100,000	0	0	0	100,000				100,000				100,000
Public Conveniences	275,000	275,000	0	0	550,000							550,000	550,000
Litter Bins	20,000	2,000	2,000	2,000	26,000				26,000				26,000
Roads&Paths at St.Mary's Church Cemetery	20,000	0	0	0	20,000				20,000				20,000
Land Drainage	10,000	10,000	10,000	0	30,000				30,000				30,000
Plant & Machinery Replacement Programme	8,000	51,000	8,000	8,000	75,000				75,000				75,000
Waste Vehicles	3,500,000	0	0	0	3,500,000							3,500,000	3,500,000
Garden Waste Bins	0	111,000	15,000	15,000	141,000							141,000	141,000
Recycling, food waste and refuse bins	0	100,000	100,000	100,000	300,000							300,000	300,000
Playground Improvements (Match Funding Pot)	50,000	0	0	0	50,000				50,000				50,000
Total- Community Services	**5,006,100**	**1,428,000**	**695,000**	**553,000**	**7,682,100**	**0**	**0**	**1,185,000**	**301,000**	**0**	**0**	**6,196,100**	**7,682,100**
Resources													
Council Offices Major Maintenance Programme	182,300	100,000	0	0	282,300				282,300				282,300
Customer First/IT	150,000	150,000	50,000	0	350,000							350,000	350,000
IT - Hardware/infrastructure/Customer First Projects	0	723,600	154,800	163,400	1,041,800							1,041,800	1,041,800
Investment & Development Fund	66,000,000	65,000,000	64,374,900	0	195,374,900							195,374,900	195,374,900
Land / Asset Development	153,000	0	0	0	153,000							153,000	153,000
Total- Resources	**66,485,300**	**65,973,600**	**64,579,700**	**163,400**	**197,202,000**	**0**	**0**	**0**	**282,300**	**0**	**0**	**196,919,700**	**197,202,000**
Total Capital Programme	**82,308,400**	**81,972,800**	**78,395,600**	**5,612,600**	**248,289,400**	**26,863,200**	**1,751,100**	**1,185,000**	**583,300**	**5,427,000**	**400,000**	**212,079,800**	**248,289,400**

Capital Financing	2019/20 £	2020/21 £	2021/22 £	2022/23 £	Total £
HRA Reserves	9,007,900	7,605,200	6,272,900	3,977,200	26,863,200
DFG Grant	439,100	426,000	426,000	460,000	1,751,100
CIL/S106 Contributions	305,000	365,000	250,000	265,000	1,185,000
General Fund Capital Receipts/Reserves	390,300	163,000	20,000	10,000	583,300
Housing Capital Receipts	1,370,000	2,426,000	1,172,000	459,000	5,427,000
Hosuing Debeloper Contribution		400,000			400,000
Borrowing	70,796,100	70,587,600	70,254,700	441,400	212,079,800
Total Capital Funding	**82,308,400**	**81,972,800**	**78,395,600**	**5,612,600**	**248,289,400**

APPENDIX 'B' **APPENDIX 'B'**

TREASURY MANAGEMENT STRATEGY STATEMENT 2020/21

1. Background

1.1 The Council is required to operate a balanced budget which broadly means that income raised during the year will meet planned expenditure. Part of the treasury management operation is to ensure that the cashflow for this is adequately planned, with cash being available when it is needed. Where surplus monies are available these are invested with counterparties or in instruments commensurate with the Council's low risk appetite, providing security and adequate liquidity initially before considering investment return.

1.2 The second main function of the treasury management service is the funding of the Council's capital plans. These plans provide a guide to borrowing need, essentially the longer term cash flow planning, to ensure that the Council can meet its capital spending obligations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses. On occasion, when it is prudent and economic, any loan debt may be restructured to meet Council risk or cost objectives.

2. Treasury Management Strategy 2020/21

2.1 The proposed strategy for 2020/21 covers borrowing and investment issues. This includes the requirements of the Local Government Act 2003 and the CIPFA Treasury Management Code. The requirements of the CIPFA Prudential for Capital Finance Code 2017 are covered by the Capital Strategy.

3. Economic Background

3.1 Economic Outlook-The UK's progress negotiating its exit from the European Union, together with its future trading arrangements, will continue to be a major influence on the Authority's treasury management strategy for 2020/21.The stated position of the UK Government to leave the EU by the 31st December 2020 continues the uncertainty facing the UK economy. A more detailed economic and interest rate forecast provided is attached at **Annex 1**.

3.2 UK Consumer Price Inflation (CPI) for December was 1.5% year on year. The BoE forecasts inflation for 2020 as 1.5% and 2% for 2021. The most recent labour market data for October 2019 showed the unemployment rate edged up slightly to 3.8%. The average annual growth rate for pay excluding bonuses in October was 3.5% as and provide some pull on general inflation. Adjusted for inflation, real wages grew by 2.0%., a level likely to have little effect on consumer spending. Unemployment in October 2019 was 3.8%, 0.3% lower than October 2018.

3.3 Looking ahead, the BoE, in its November Monetary Policy Report, expects GDP growth to average around 1% for 2020, providing the UK's exit from the EU is relatively smooth.

3.4 Interest Rate Forecast- Following the Bank of England's decision to increase Bank Rate to 0.75% in August, no changes to monetary policy has been made since. The short term outlook for increases in interest rate increases is soft with the risks on the downside. The Monetary Policy Committee continues to reiterate that any further increases will be at a gradual pace and limited in extent. For the purpose of setting the budget, it has been assumed that new investments will be made at an average rate of 0.75%, and that new long-term loans will be borrowed at an average rate of 2.7%. A more detailed economic background and interest rate forecast provided is attached at **Annex 1.**

4. Current Treasury Portfolio

4.1 The Council's current treasury portfolio, as at 31 December 2019 is shown below at Table 1 and highlights the average interest rate return in 2019/20 compared to 2018/19 :-

Table 1	2019/20 Principal Amount £m	2019/20 Avg. Interest Rate %	2018/19 Avg. Interest Rate %
Notice Accounts & Cash Plus Funds	4.0	0.8	0.8
Money Market Funds	8.1	0.7	0.7
Short-term Deposits	0	0	0.7
CCLA Property Fund	4.0	4.3	5.0
Funding Circle	2.0	3.9	6.0
Schroders Bond Fund	3.0	4.6	4.4
UBS Multi-Asset Fund	3.0	3.9	4.0
CCLA Diversification Fund	2.0	3.2	3.0
Total Treasury Investments	**26.1**	**2.4**	**2.0**
Long-term PWLB loans (HRA)	61.2	2.7	2.7
Long-term PWLB loans (GF)	43.4	2.6	2.5
Total Borrowing	**104.6**	**2.7**	**2.7**
Net Borrowing	**78.5**		

5. Capital Strategy and Capital Investment Planning

5.1 The Council's Capital Strategy is shown as a separate document. This covers the following capital expenditure.

5.2 Physical capital assets owned by the Council and used in the delivery of services, and, where appropriate:

(i) Capital Loans to specific service providers e.g Loans to Gryllus Property Ltd and Freedom Leisure ; and

(ii) Loans and shareholdings in limited companies, joint ventures and other non-financial investments in property.

5.3 Such investments will be treated as capital expenditure for treasury management and prudential borrowing purposes even though they do not create physical assets in the Council's accounts. Appropriate budgets in respect of these activities are agreed as part of the Council's budget setting and ongoing monitoring processes and considered as part of the Investment Strategy.

5.4 Capital Financing Requirement (CFR) -The CFR measures the Council's underlying borrowing need for the capital strategy. Each year, the CFR will increase by the amounts of new capital expenditure not immediately financed and reduces by the resources set aside for financing capital expenditure incurred in earlier years. e.g MRP. The Capital Strategy sets out the Councils Capital Financing Requirement

5.5 Table 2 below shows that the CFR will increase over the medium term. Consequently, the capital financing charge to revenue will increase, reflecting the capital spending plans.

Capital Financing Requirement	Actual 2018/19	Estimate 2019/20	Estimate 2020/21	Estimate 2021/22	Estimate 2022/23
	£m	**£m**	**£m**	**£m**	**£m**
General Fund CFR	12.485	84.415	152.343	218.144	219.320
HRA CFR	61.308	71.686	85.731	98.326	102.762
Capital Financing Requirement	**73.793**	**156.101**	**238.074**	**316.470**	**322.082**
Movement in CFR		**82.308**	**81.973**	**78.396**	**5.612**

Table 3 below shows a forecast of borrowing requirement over the period

Forecast of Borrowing	Actual 2018/19	Estimate 2019/20	Estimate 2020/21	Estimate 2021/22	Estimate 2022/23
	£m	£m	£m	£m	£m
General Fund Borrowing	26.099	81.555	148.529	213.633	214.075
HRA Borrowing	61.189	61.189	64.803	69.953	69.953
Forecast Borrowing	**87.288**	**142.744**	**213.332**	**283.586**	**284.028**
CFR not funded by Borrowing	**0**	**13.357**	**24.742**	**32.884**	**38.054**

It should be noted that the estimated General Fund borrowing in Table 3 is based on the financing of the Council’s planned Capital Programme, however if capital expenditure is does not occur in line with the profiled spend then borrowing will not be undertaken.

5.6 CIPFA’s Prudential Code for Capital Finance in Local Authorities recommends that the Council’s total debt should be lower than its highest forecast capital expenditure over the next three years. This is confirmed by comparing the total forecast capital expenditure per year in to the movement in CFR in Table 2 with projected Table 3. This allows some flexibility for limited early borrowing for future years,but ensures that borrowing is not undertaken for revenue purposes or that the Council is in an over-borrowed position for its capital strategy and programme.

6. Borrowing Strategy

6.1 The Council's main objective when borrowing money is to strike an appropriate balance between securing low interest costs and achieving cost certainty over the period for which funds are required. Given the significant cuts to public expenditure and in particular to local government funding, the Council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. The key factors influencing the 2020/21 borrowing strategy are:

(i) forecast the borrowing requirement of the Council;

(ii) the current economic and market environment; and

(iii) interest rate forecast awareness.

6.2 The Council’s current strategy is to maintain borrowing and investments below their underlying full capital expenditure level. The Council is thus maintaining its an under-borrowed position, which means that capital expenditure has not been fully funded from loan debt as other funding streams (e.g. government grants, reserves or capital receipts) have also been used where available. This policy has served the Council well over the last few years while investment returns have been variable and counterparty risk has been relatively high.

6.3 However, the Council's borrowing position will still need to be kept under review to avoid incurring higher borrowing costs in future years when the Council may not be able to avoid new borrowing to finance capital expenditure and/or to refinance maturing debt.

6.4 As the overall financial climate still remains unsettled, the Treasury Management team will continue to monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances (within their approved remit). If it were considered that there was a significant risk of a sharp fall in long and short term rates (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), long term borrowings could be postponed, and potential rescheduling from fixed rate funding into short term borrowing could be considered. Further reports to the Investment Sub-Committee will be made as appropriate if a change in strategy is required.

7. Borrowing Limits

7.1 The Prudential Code requires the Council to set two limits on its total external debt, as set out in the table below. The limits have been adjusted as required for growth and slippage in the capital strategy. The limits are:

- Authorised Limit for External Debt (Prudential Indicator 7a).This is the limit prescribed by section 3(1) of the Local Government Act 2003 representing the maximum level of borrowing which the Council may incur. It reflects the level of external debt which, while not desired, could be afforded in the short term, but may not be sustainable in the longer term.

- Operational Boundary (Prudential Indicator 7b).This is the limit which external debt is not normally expected to exceed. The boundary is based on current debt plus anticipated net financing need for future years.

Overall Borrowing Limits	**Limit 2020/21**	**Limit 2020/22**	**Limit 2022/23**
Authorised Limit for External Borrowing	**£m**	**£m**	**£m**
Borrowing and Other Long Term Liabilities	215	285	285
Operational Boundary for External Debt			
Borrowing and Other Long Term Liabilities	210	280	280

7.2 Managing the profile of when debt matures is essential for ensuring that the Council is not exposed to large fixed rate sums falling due for re-financing within a short period, and thus potentially exposing the Council to additional cost. The table below sets out current upper limits for debt maturity.

Debt Maturity Profile Limits	Actual as at 31/12/19	Lower Limit 2020/21	Upper Limit 2020/21
	%		%
Under 1 year	3.9	5	15
1 to 2 years	6.3	5	15
2 to 5 years	9.1	10	25
5 years to 10 years	24.4	20	50
10 -20 years	11.2	20	50
Over 20 years	45.1	30	50
Total	**100%**		

7.3 In the event that there is a much sharper rise in long and short term rates than currently forecast, then the balance of the loan portfolio will be re-visited with a view to taking on longer term fixed rate borrowing in anticipation of future rate rises.

8. Debt Rescheduling

8.1 As short term borrowing rates will be considerably cheaper than longer term fixed interest rates, there may be opportunities to generate savings by switching from long term debt to short term debt. However, these savings will need to be considered in the light of the current treasury position and the cost of debt repayment (premiums can be incurred on premature redemption of PWLB debt).

9. Managing Cash Balances

9.1 The Council had accumulated reserves of £19.3m at the end of the financial 2018/19. This was supported by Short and Long Term Investments. The position is anticipated to be £18m at the end of the 2019/20 financial year. It is not anticipated that this position will alter significantly in 2020/21. In addition, the Council has significant inflows of cash and outflows each month, which require investment.

9.2 The Council’s policy is to set aside £4-5m to provide working capital to cover day to day contingencies. Therefore assuming a level of accumulated reserves of £18m plus a day to day working balance of £4-5m gives an average of £13-14m is available to be invested over the longer-term without impacting on the Council's need for liquidity.

9.3 As planned Capital Programme expenditure takes place in 2019/20, the Council will need to borrow to fund this investment in 2019/20 as cash balances will naturally reduce. The Council currently has £14m under long term investment., valued at £14.2m at the end of December 2019, which could be used to finance capital expenditure in the short term. However investment returns are currently higher than long term borrowing costs and it is not proposed therefore at this stage to use these investments.

10. Treasury Investment Strategy

10.1 The Council holds significant invested funds, representing income received in advance of expenditure, balances and reserves. During the first half of the current year, the Council's average investment balance has been around £25-30m and the cash flow projections shows this pattern is expected to continue in the forthcoming year. Investments are made with reference to the core balance, future cash flow requirements and the outlook for interest rates.

10.2 The Council's investment policy has regard to the CLG's Guidance on Local Government Investments ("the Investment Guidance") and the CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code"). The Council's investment priorities will be security first, liquidity second, and then return.

10.3 In accordance with the above guidance and to minimise the risk to investments, the Council applies minimum acceptable credit criteria to generate a list of highly creditworthy counterparties which will provide security of investments, enable diversification and minimise risk. The key ratings used to monitor counterparties are the Short Term and Long Term ratings.

10.4 An investment time limit has to be set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment. For the year 2020/21, the proposed limit of investments for over 1 year is £14m.

10.5 The Council's officers recognise that ratings should not be the sole determinant of the quality of an institution and that it is important to assess continually and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To this end the Council will engage with its advisors and monitor changes in market variables and pricing with the credit ratings in order to generate optimal returns.

10.6 Other information sources used will include the financial press, share price and other such information pertaining to the banking sector to establish the most robust scrutiny process on the suitability of potential investment counterparties.

10.7 The primary principle governing the Council's treasury investment criteria is the security of its investments, closely followed by liquidity (i.e. repayment of money) and then finally the actual return on the investment. These factors in that order are a key consideration. After this main principle, the Council will ensure that:

(i) It maintains a policy covering both the categories of investment types it will invest in, criteria for choosing investment counterparties with adequate security and monitoring their security; and

(ii) It has sufficient liquidity in its investments. For this purpose it will set out procedures for determining the maximum periods for which funds may prudently be committed. These procedures also apply to the Council's prudential indicators covering the maximum principal sums invested.

10.8 The Interim Chief Finance Officer (S151 Officer) will use the services of the Council's Treasury management adviser currently, Link Asset Services, to provide advice on an up to date counterparty list in compliance with the following criteria and will revise the criteria and submit them to Council for approval as necessary.

10.9 The Council takes into account the following relevant matters when proposing counterparties:

(i) the financial position and jurisdiction of the institution;

(ii) the market pricing of credit default swaps for the institution;

(iii) any implicit or explicit Government support for the institution;

(iv) the use of two of the major credit rating agencies external short and long term credit ratings to assess creditworthiness;

(v) Sovereign ratings to select counterparties from only the most creditworthy countries; and

(vi) core Tier 1 capital ratios.

NB- Definition of Credit Default Swap – CDS are a financial instrument for swapping the risk of debt default. Credit default swaps may be used for emerging market bonds, mortgage-backed securities, corporate bonds and local government bond. The buyer of a credit default swap pays a premium for effectively insuring against a debt default.

10.10 The MHCLG Guidance on Local Government Investments made under section 15(1) of the Local Government Act 2003, places restrictions on Local authorities in relation to investments. Investments fall in to one of the three categories; Specified Investments , Loans and Non Specified Investments

10.11 A specified investment is defined as an investment which satisfies all of the conditions below:

(i) the investment is denominated in sterling and any payments or repayments in respect of the investment are payable only in sterling;

(ii) the investment is not a long term investment. This means that the local authority has a contractual right to repayment within 12 months, either because that is the expiry term of the investment or through a non conditional option;

(iii) the making of the investment is not defined as capital expenditure under Regulation 25 of the Capital Finance regulations (2013); and

(iv) the investment is made with a body or in an investment scheme of high credit quality; or with the UK Government, a UK Local Authority or parish/community council.

10.12 Loans- Authorities may provide loans to local enterprises, local charities, wholly owned companies and joint ventures as part of a wider strategy for delivering economic growth and delivering services for the Council. This is covered within the Council's Capital Strategy in more detail.

10.13 A non-specified investment is any investment that is not a loan and does not meet the criteria to be treated as a specified investment. These principally relates to non–financial investments which an Authority holds primarily or partially to generate a profit. This is covered within the Council's Capital Strategy.

Credit Rating of Treasury Management Investments

10.14 The criteria for providing a pool of high quality short, medium and long-term, cash-based investment counterparties along with the time and monetary limits for institutions on the Council's counterparty list are in the table below. The Council defines the following as being of "high credit quality" for making specified investments, subject to the monetary and time limits shown.

High Credit Quality	Individual Monetary limit[1]	Aggregate Monetary Limit	Fitch Credit rating[3]
UK Central Government	No Limit	No Limit	Not applicable
UK Local Authorities including PCC's	£2m each	LT: £8m	Not applicable
Banks(1) operating in the UK(2)	£2m each	LT: £8m ST: None	LT:AA- ST: F1
Overseas Banks (subject to Sovereign Rating AAA or AA+)	£2m each	£8m	LT:AA- ST: F1
UK building societies with an asset base > £1bn	£2m each		LT: A ST:F1
UK building societies with an asset base < £1bn	£1m each		LT: A ST:F1
Money Market Funds	£4m each		ST: AAA
Pooled Funds*			
Bond Funds without credit ratings	£4m each	£8m	Not applicable
Property Funds without credit ratings	£4m each	£4m	Not applicable
Multi Asset Funds	£4m each	£8m	Not applicable
Long Term Loans to small business ranked no lower than average risk by independent credit analysis	£100,000	£6m	Not applicable
Company shares to participate in the UK Municipal Bonds Agency	£10,000	£10,000	Not applicable

[1] banks within the same group ownership are treated as one bank for limit purposes
[2] where the bank is used as a reserve account the criteria will exclude consideration of the long term credit rating
[3] Minimum Credit rating required, is expressed as a Fitch rating or the equivalent S&P or Moodys ratings etc
[4] The Council has placed an overall limit on pooled funds of £16m

10.15 The majority of the Council's investments will be made for relatively short periods and in highly credit rated investments, giving priority to security and liquidity ahead of yield. In order that the Council is not at risk of a large single default, the maximum that will be lent to any one organisation (other than the UK Government) will be £2 million or £4 million per pooled fund. A group of banks under the same ownership will be treated as a single organisation for limit purposes.

11. Money market Funds and Pooled Funds

11.1 Money market funds are pooled investment vehicles consisting of instruments similar to those used by the Council. They have the advantage of providing wide diversification of investment risks, coupled with the services of a professional fund manager. Fees of between 0.10% and 0.20% per annum are deducted from the interest paid to the Council.

11.2 Funds that offer same-day liquidity and a constant net asset value will be used as an alternative to instant access call accounts, while funds whose value changes with market prices and/or have a notice period will be used for longer investment periods.

12. Risk assessment and credit ratings

12.1 The Council uses long-term credit ratings from at least two of the main credit rating agencies to assess the risk of investment default. The lowest available credit rating will be used to determine credit quality.

12.2 Long-term ratings are expressed on a scale from AAA (the highest quality) through to D (indicating default). Ratings of BBB- and above are described as investment grade, while ratings of BB+ and below are described as speculative grade. The Council's credit rating criteria are set to ensure that it is unlikely that the Council will hold speculative grade investments directly, despite the risk of repeated downgrades. The Council may invest in bond funds that hold speculative grade bonds themselves, giving the Council an indirect exposure, but the risk is mitigated by the high level of diversification and the expert fund management.

12.3 Credit ratings are obtained and monitored by the Council's treasury advisers, who will notify changes in ratings as they occur. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:

- no new investments will be made;
- any existing investments that can be recalled or sold at no cost will be; and
- full consideration will be given to the recall or sale of all other existing investments with the affected counterparty.

13 Other information on the security of investments

13.1 The Council understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements and reports in the quality financial press. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may meet the above criteria.

13.2 If these restrictions mean that insufficient commercial organisations of "high credit quality" are available to invest the Council's cash balances, then the surplus will be deposited with Money Market Funds, the UK Government, via the Debt Management Office for example, or with other local authorities. This will cause a reduction in the level of investment income earned, but will protect the principal sum invested.

14. Foreign countries

14.1 Investments in foreign countries will be limited to those that hold an AAA or AA+ sovereign credit rating from two of the three major credit rating agencies, and to a maximum of £2 million per foreign country. Investments in countries whose lowest sovereign rating is not AAA will be limited to one year's duration. No country limit will apply to investments in the UK, irrespective of the sovereign credit rating.

14.2 Overseas subsidiaries of foreign banking groups will normally be assessed according to the country of domicile of the parent organisation. However, Santander UK plc (a subsidiary of Spain's Banco Santander) will be classed as a UK bank due to its substantial UK franchises and the arms-length nature of the parent-subsidiary relationships.

14.3 Sovereign credit rating criteria and foreign country limits will not apply to investments in multilateral development banks (e.g. the European Investment Bank and the World Bank) or other supranational organisations (e.g. the European Union).

15 Liquidity management

15.1 The Council uses financial systems to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a pessimistic basis, with receipts under-estimated and payments over-estimated to minimise the risk of the Council being forced to borrow on unfavourable terms to meet its financial commitments. Decisions on long-term investments are set by reference to the Council's medium term financial plan and cash flow forecast.

16. Interest rate exposures

16.1 This indicator is set to control the Council's exposure to interest rate risk. The upper limits on fixed and variable rate interest rate exposures, expressed as net principal borrowed will be:

	2020/21 £m	2021/22 £m	2022/23 £m
Upper limit on fixed interest rate exposures	215	285	285
Upper limit on variable interest rate exposures	50	60	60

16.2 Fixed rate investments and borrowings are those where the rate of interest is fixed for the whole financial year. Instruments that mature during the financial year are classed as variable rate.

17 Risk Implications - principal sums invested for periods longer than 364 days

17.1 The purpose of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments. The recommendation for the upper limit of principal sums maturing beyond the year end is £16m, as shown below:

	2020/21	2021/22	2022/23
Limit on principal invested beyond year end	£16m	£16m	£16m

18 Investment training

18.1 The needs of the Council's treasury management staff for training in investment management are assessed annually as part of the staff appraisal process, and additionally when the responsibilities of individual members of staff change.

18.2 Staff regularly attend training courses, seminars and conferences provided by treasury management advisors and CIPFA. Relevant staff are also encouraged to study professional qualifications from CIPFA, the Association of Corporate Treasurers and other appropriate organisations. A regular programme for the training of Members responsible for Treasury Management is being provided.

19 Other Financial Policies

19.1 Charging interest to the Housing Revenue Account- Following the reform of housing finance, the Council is free to adopt its own policy on sharing interest costs and income between the General Fund and Housing Revenue Account (HRA). The CIPFA Code recommends that Authorities state their policy on this matter each year in their treasury management strategy.

19.2 The Council is required to notionally split each of its existing long-term loans into General Fund and HRA pools. For TDC, the only borrowing relates to the £70.2m that was borrowed on 28th March 2012 which was assigned to the HRA pool. In the future, any new long-term loans borrowed will be assigned in their entirety to one pool or the other. Interest payable and other costs/income arising from long-term loans (e.g. premiums and discounts on early redemption) will be charged/credited to the respective revenue account. Transfers between the General Fund and HRA will be made at the Authority's average short term interest rate on investments, adjusted for credit risk.

19.3 Financial Derivatives- In the absence of any explicit legal power to do so, the Authority will not use standalone financial derivatives (such as swaps, forwards, futures and options). Derivatives embedded into loans and investments, including pooled funds and forward starting transactions, may be used, and the risks that they present will be managed in line with the overall treasury risk management strategy.

19.4 Markets in Financial Instruments Directive- The Authority has registered as a professional client with its providers of financial services, including advisers, banks, brokers and fund managers, allowing it access to a greater range of services but without the greater regulatory protections afforded to individuals and small companies. Given the size and range of the Authority's treasury management activities, the [Chief Financial Officer (Section 151 Officer) believes this to be the most appropriate status.

19.5 Business models- Under the new IFRS 9 standard, the accounting for certain investments depends on the Authority's "business model" for managing them. The Authority aims to achieve value from its internally managed treasury investments by a business model of collecting the contractual cash flows and therefore, where other criteria are also met, these investments will continue to be accounted for at amortised cost.

ANNEX 1 to the Treasury Management Strategy Statement 2020/21

ECONOMIC BACKGROUND

UK. Brexit. 2019 has been a year of upheaval on the political front as Theresa May resigned as Prime Minister to be replaced by Boris Johnson on a platform of the UK leaving the EU on 31 October 2019, with or without a deal. However, MPs blocked leaving on that date and the EU agreed an extension to 31 January 2020. In late October, MPs approved an outline of a Brexit deal to enable the UK to leave the EU on 31 January. Now that the Conservative Government has gained a large overall majority in the **general election** on 12 December, this outline deal will be passed by Parliament by that date. However, there will still be much uncertainty as the detail of a trade deal will need to be negotiated by the current end of the transition period in December 2020, which the Prime Minister has pledged he will not extend. This could prove to be an unrealistically short timetable for such major negotiations that leaves open two possibilities; one, the need for an extension of negotiations, probably two years, or, a no deal Brexit in December 2020.

GDP growth has taken a hit from Brexit uncertainty during 2019; quarter three 2019 surprised on the upside by coming in at +0.4% q/q, +1.1% y/y. However, the peak of Brexit uncertainty during the final quarter appears to have suppressed quarterly growth to probably around zero. The economy is likely to tread water in 2020, with tepid growth around about 1% until there is more certainty after the trade deal deadline is passed.

While the Bank of England went through the routine of producing another **quarterly Inflation Report,** (now renamed the Monetary Policy Report), on 7 November, it is very questionable how much all the writing and numbers were worth when faced with the uncertainties of where the UK will be after the general election. The Bank made a change in their Brexit assumptions to now include a deal being eventually passed. Possibly the biggest message that was worth taking note of from the Monetary Policy Report, was an increase in concerns among MPC members around weak global economic growth and the potential for Brexit uncertainties to become entrenched and so delay UK economic recovery. Consequently, the MPC voted 7-2 to maintain Bank Rate at 0.75% but two members were sufficiently concerned to vote for an immediate Bank Rate cut to 0.5%. The MPC warned that if global growth does not pick up or Brexit uncertainties intensify, then a rate cut was now more likely. Conversely, if risks do recede, then a more rapid recovery of growth will require gradual and limited rate rises. The speed of recovery will depend on the extent to which uncertainty dissipates over the final terms for trade between the UK and EU and by how much global growth rates pick up. The Bank revised its inflation forecasts down – to 1.25% in 2019, 1.5% in 2020, and 2.0% in 2021; hence, the MPC views inflation as causing little concern in the near future.

The **MPC meeting of 19 December** repeated the previous month's vote of 7-2 to keep Bank Rate on hold. Their key view was that there was currently 'no evidence about the extent to which policy uncertainties among companies and households had declined' i.e. they were going to sit on their hands and see how the economy goes in the next few months. The two members who voted for a cut were concerned that the labour market was faltering. On the other hand, there was a clear warning in the minutes that the MPC were concerned that "domestic unit labour costs have continued to grow at rates above those consistent with meeting the inflation target in the medium term".

If economic growth were to weaken considerably, the MPC has relatively little room to make a big impact with Bank Rate still only at 0.75%. It would therefore, probably suggest that it would be up to the Chancellor to provide help to support growth by way of a **fiscal boost** by e.g. tax cuts, increases in the annual expenditure budgets of government departments and services and expenditure on infrastructure projects, to boost the economy. The Government has already made moves in this direction and it made significant promises in its election manifesto to increase government spending by up to £20bn p.a., (this would add about 1% to GDP growth rates), by investing primarily in infrastructure. This is likely to be announced in the next Budget, probably in February 2020. The Chancellor has also amended the fiscal rules in November to allow for an increase in government expenditure.

As for **inflation** itself, CPI has been hovering around the Bank of England's target of 2% during 2019, but fell again in both October and November to a three-year low of 1.5%. It is likely to remain close to or under 2% over the next two years and so, it does not pose any immediate concern to the MPC at the current time. However, if there was a hard or no deal Brexit, inflation could rise towards 4%, primarily because of imported inflation on the back of a weakening pound.

With regard to the **labour market,** growth in numbers employed has been quite resilient through 2019 until the three months to September where it fell by 58,000. However, there was an encouraging pick up again in the three months to October to growth of 24,000, which showed that the labour market was not about to head into a major downturn. The unemployment rate held steady at a 44-year low of 3.8% on the Independent Labour Organisation measure in October. Wage inflation has been steadily falling from a high point of 3.9% in July to 3.5% in October (3-month average regular pay, excluding bonuses). This meant that in real terms, (i.e. wage rates higher than CPI inflation), earnings grew by about 2.0%. As the UK economy is very much services sector driven, an increase in household spending power is likely to feed through into providing some support to the overall rate of economic growth in the coming months. The other message from the fall in wage growth is that employers are beginning to find it easier to hire suitable staff, indicating that supply pressure in the labour market is easing.

USA. President Trump's massive easing of fiscal policy in 2018 fuelled a temporary boost in consumption in that year which generated an upturn in the rate of growth to a robust 2.9% y/y. **Growth** in 2019 has been falling after a strong start in quarter 1 at 3.1%, (annualised rate), to 2.0% in quarter 2 and then 2.1% in quarter 3. The economy looks likely to have maintained a growth rate similar to quarter 3 into quarter 4; fears of a recession have largely dissipated. The strong growth in employment numbers during 2018 has weakened during 2019, indicating that the economy had been cooling, while inflationary pressures were also weakening. However, CPI inflation rose from 1.8% to 2.1% in November, a one year high, but this was singularly caused by a rise in gasoline prices.

The Fed finished its series of increases in rates to 2.25 – 2.50% in December 2018. In July 2019, it cut rates by 0.25% as a 'midterm adjustment' but flagged up that this was not intended to be seen as the start of a series of cuts to ward off a downturn in growth. It also ended its programme of quantitative tightening in August, (reducing its holdings of treasuries etc.). It then cut rates by 0.25% again in September and by another 0.25% in its October meeting to 1.50 – 1.75%.. At its September meeting it also said it was going to **start buying Treasuries again**, although this was not to be seen as a resumption of quantitative easing but rather an exercise to relieve liquidity pressures in the repo market. Despite those protestations, this still means that the Fed is again expanding its balance sheet holdings of government debt. In the first month, it will buy $60bn, whereas it had been reducing its balance sheet by $50bn per month during 2019. As it will be buying only short-term (under 12 months) Treasury bills, it is technically correct that this is not quantitative easing (which is purchase of long term debt). The Fed left rates unchanged in December. However, the accompanying statement was more optimistic about the future course of the economy so this would indicate that further cuts are unlikely.

Investor confidence has been badly rattled by the progressive ramping up of increases in tariffs President Trump has made on Chinese imports and China has responded with increases in tariffs on American imports. This **trade war** is seen as depressing US, Chinese and world growth. In the EU, it is also particularly impacting Germany as exports of goods and services are equivalent to 46% of total GDP. It will also impact developing countries dependent on exporting commodities to China. However, in November / December, progress has been made on agreeing a phase one deal between the US and China to roll back some of the tariffs; this gives some hope of resolving this dispute.

EUROZONE. Growth has been slowing from +1.8 % during 2018 to around half of that in 2019. Growth was +0.4% q/q (+1.2% y/y) in quarter 1, +0.2% q/q (+1.2% y/y) in quarter 2 and then +0.2% q/q, +1.1% in quarter 3; there appears to be little upside potential in the near future. German GDP growth has been struggling to stay in positive territory in 2019 and fell by -0.1% in quarter 2; industrial production was down 4% y/y in June with car production down 10% y/y. Germany would be particularly vulnerable to a no deal Brexit depressing exports further and if President Trump imposes tariffs on EU produced cars.

The European Central Bank (ECB) ended its programme of quantitative easing purchases of debt in December 2018, which then meant that the central banks in the US, UK and EU had all ended the phase of post financial crisis expansion of liquidity supporting world financial markets by quantitative easing purchases of debt. However, the downturn in EZ growth in the second half of 2018 and into 2019, together with inflation falling well under the upper limit of its target range of 0 to 2%, (but it aims to keep it near to 2%), has prompted the ECB to take new measures to stimulate growth. At its March meeting it said that it expected to leave interest rates at their present levels "at least through the end of 2019", but that was of little help to boosting growth in the near term. Consequently, it announced a **third round of TLTROs**; this provides banks with cheap borrowing every three months from September 2019 until March 2021 that means that, although they will have only a two-year maturity, the Bank was making funds available until 2023, two years later than under its previous policy. As with the last round, the new TLTROs will include an incentive to encourage bank lending, and they will be capped at 30% of a bank's eligible loans. However, since then, the downturn in EZ and world growth has gathered momentum; at its meeting on 12 September it cut its deposit rate further into negative territory, from -0.4% to -0.5%, and announced a **resumption of quantitative easing purchases of debt for an unlimited period.** At its October meeting it said these purchases would start in November at €20bn per month - a relatively small amount compared to the previous buying programme. It also increased the maturity of the third round of TLTROs from two to three years. However, it is doubtful whether this loosening of monetary policy will have much impact on growth and, unsurprisingly, the ECB stated that governments would need to help stimulate growth by 'growth friendly' fiscal policy.

There were no policy changes in the December meeting, which was chaired for the first time by the new President of the ECB, Christine Lagarde. However, the outlook continued to be down beat about the economy; this makes it likely there will be further monetary policy stimulus to come in 2020. She did also announce a thorough review of how the ECB conducts monetary policy, including the price stability target. This review is likely to take all of 2020.

On the political front, Austria, Spain and Italy have been in the throes of **forming coalition governments** with some unlikely combinations of parties i.e. this raises questions around their likely endurance. The latest results of German state elections has put further pressure on the frail German CDU/SDP coalition government and on the current leadership of the CDU. The results of the Spanish general election in November have not helped the prospects of forming a stable coalition.

CHINA. Economic growth has been weakening over successive years, despite repeated rounds of central bank stimulus; medium term risks are increasing. Major progress still needs to be made to eliminate excess industrial capacity and the stock of unsold property, and to address the level of non-performing loans in the banking and shadow banking systems. In addition, there still needs to be a greater switch from investment in industrial capacity, property construction and infrastructure to consumer goods production.

JAPAN - has been struggling to stimulate consistent significant GDP growth and to get inflation up to its target of 2%, despite huge monetary and fiscal stimulus. It is also making little progress on fundamental reform of the economy.

WORLD GROWTH. Until recent years, world growth has been boosted by increasing **globalisation** i.e. countries specialising in producing goods and commodities in which they have an economic advantage and which they then trade with the rest of the world. This has boosted worldwide productivity and growth, and, by lowering costs, has also depressed inflation. However, the rise of China as an economic superpower over the last thirty years, which now accounts for nearly 20% of total world GDP, has unbalanced the world economy. The Chinese government has targeted achieving major world positions in specific key sectors and products, especially high tech areas and production of rare earth minerals used in high tech products. It is achieving this by massive financial support, (i.e. subsidies), to state owned firms, government directions to other firms, technology theft, restrictions on market access by foreign firms and informal targets for the domestic market share of Chinese producers in the selected sectors. This is regarded as being unfair competition that is putting western firms at an unfair disadvantage or even putting some out of business. It is also regarded with suspicion on the political front as China is an authoritarian country that is not averse to using economic and military power for political advantage. The current trade war between the US and China therefore needs to be seen against that backdrop. It is, therefore, likely that we are heading into a period where there will be a **reversal of world globalisation and a decoupling of western countries** from dependence on China to supply products. This is likely to produce a backdrop in the coming years of weak global growth and so weak inflation. **Central banks are, therefore, likely to come under more pressure to support growth by looser monetary policy measures and this will militate against central banks increasing interest rates**.

The trade war between the US and China is a major concern to **financial markets** due to the synchronised general weakening of growth in the major economies of the world, compounded by fears that there could even be a recession looming up in the US, though this is probably overblown. These concerns resulted in **government bond yields** in the developed world falling significantly during 2019. If there were a major worldwide downturn in growth, central banks in most of the major economies will have limited ammunition available, in terms of monetary policy measures, when rates are already very low in most countries, (apart from the US). There are also concerns about how much distortion of financial markets has already occurred with the current levels of quantitative easing purchases of debt by central banks and the use of negative central bank rates in some countries. The latest PMI survey statistics of economic health for the US, UK, EU and China have all been predicting a downturn in growth; this confirms investor sentiment that the outlook for growth during the year ahead is weak.

INTEREST RATE FORECASTS

The interest rate forecast are **predicated on an assumption of an agreement being reached on Brexit between the UK and the EU.** On this basis, while GDP growth is likely to be subdued in 2019 and 2020 due to all the uncertainties around Brexit depressing consumer and business confidence, an agreement on the detailed terms of a trade deal is likely to lead to a boost to the rate of growth in subsequent years. This could, in turn, increase inflationary pressures in the economy and so cause the Bank of England to resume a series of gentle increases in Bank Rate. Just how fast, and how far, those increases will occur and rise to, will be data dependent. The forecasts in this report assume a modest recovery in the rate and timing of stronger growth and in the corresponding response by the Bank in raising rates.

- In the event of an **orderly non-agreement exit in December 2020**, it is likely that the Bank of England would take action to cut Bank Rate from 0.75% in order to help economic growth deal with the adverse effects of this situation. This is also likely to cause short to medium term gilt yields to fall.
- If there were a **disorderly Brexit**, then any cut in Bank Rate would be likely to last for a longer period and also depress short and medium gilt yields correspondingly. Quantitative easing could also be restarted by the Bank of England. It is also possible that the government could act to protect economic growth by implementing fiscal stimulus.

The balance of risks to the UK

- The overall balance of risks to economic growth in the UK is probably even, but dependent on a successful outcome of negotiations on a trade deal.
- The balance of risks to increases in Bank Rate and shorter term PWLB rates are broadly similarly to the downside.
- In the event that a Brexit deal was agreed with the EU and approved by Parliament, the balance of risks to economic growth and to increases in Bank Rate is likely to change to the upside.

One risk that is both an upside and downside risk, is that all central banks are now working in very different economic conditions than before the 2008 financial crash as there has been a major increase in consumer and other debt due to the exceptionally low levels of borrowing rates that have prevailed since 2008. This means that the neutral rate of interest in an economy, (i.e. the rate that is neither expansionary nor deflationary), is difficult to determine definitively in this new environment, although central banks have made statements that they expect it to be much lower than before 2008. Central banks could therefore either over or under do increases in central interest rates.

Downside risks to current forecasts for UK gilt yields and PWLB rates currently include:

- **Brexit** – if it were to cause significant economic disruption and a major downturn in the rate of growth.
- **Bank of England** takes action too quickly, or too far, over the next three years to raise Bank Rate and causes UK economic growth, and increases in inflation, to be weaker than we currently anticipate.
- A resurgence of the **Eurozone sovereign debt crisis.** In 2018, Italy was a major concern due to having a populist coalition government which made a lot of anti-austerity and anti-EU noise. However, in September 2019 there was a major change in the coalition governing Italy which has brought to power a much more EU friendly government; this has eased the pressure on Italian bonds. Only time will tell whether this new coalition based on an unlikely alliance of two very different parties will endure.
- Weak capitalisation of some **European banks**, particularly Italian banks.
- **German minority government.** In the German general election of September 2017, Angela Merkel's CDU party was left in a vulnerable minority position dependent on the fractious support of the SPD party, as a result of the rise in popularity of the anti-immigration AfD party. The CDU has done badly in recent state elections but the SPD has done particularly badly and this has raised a major question mark over continuing to support the CDU. Angela Merkel has stepped down from being the CDU party leader but she intends to remain as Chancellor until 2021.
- **Other minority EU governments.** Austria, Finland, Sweden, Spain, Portugal, Netherlands and Belgium also have vulnerable minority governments dependent on coalitions which could prove fragile.
- **Austria, the Czech Republic, Poland and Hungary** now form a strongly anti-immigration bloc within the EU. There has also been rising anti-immigration sentiment in Germany and France.
- In October 2019, the IMF issued a report on the World Economic Outlook which flagged up a synchronised slowdown in world growth. However, it also flagged up that there was **potential for a rerun of the 2008 financial crisis**, but his time centred on the huge debt binge accumulated by corporations during the decade of low interest rates. This now means that there are corporates who would be unable to cover basic interest costs on **some $19trn of corporate debt in major western economies,** if world growth was to dip further than just a minor cooling. This debt is mainly held by the shadow banking sector i.e. pension funds, insurers, hedge funds, asset managers etc., who, when there is $15trn of corporate and government debt now yielding negative interest rates, have been searching for higher returns in riskier assets. Much of this debt is only marginally above investment grade so any rating downgrade could force some holders into a fire sale, which would then depress prices further and so set off a spiral down. The IMF's answer is to suggest imposing higher capital charges on lending to corporates and for central banks to regulate the investment operations of the shadow banking sector. In October 2019, the deputy Governor of the Bank of England also flagged up the dangers of banks and the shadow banking sector lending to corporates, especially highly leveraged corporates, which had risen back up to near pre-2008 levels.

- **Geopolitical risks,** for example in North Korea, but also in Europe and the Middle East, which could lead to increasing safe haven flows.

Upside risks to current forecasts for UK gilt yields and PWLB rates

- **Brexit** – if agreement was reached all round that removed all threats of economic and political disruption between the EU and the UK.
- The **Bank of England is too slow** in its pace and strength of increases in Bank Rate and, therefore, allows inflationary pressures to build up too strongly within the UK economy, which then necessitates a later rapid series of increases in Bank Rate faster than we currently expect.
- **UK inflation,** whether domestically generated or imported, returning to sustained significantly higher levels causing an increase in the inflation premium inherent to gilt yields.

APPENDIX ‘C’

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COMMERCIAL PROPERTY INVESTMENT STRATEGY 2020/2021

Introduction

1. As a result of significant reductions in funding from Government grants, Tandridge District Council has identified the aim to significantly increase the income earned from property through a focused approach towards the acquisition and management of commercial property that meets the criteria for inclusion in a portfolio of investment properties.

2. The Commercial Property Investment Strategy will be part of Tandridge District Council’s overall Capital & Investment Strategy and be included with the fund performance monitoring and reporting procedures.

3. The returns from the commercial property investment strategy (the Strategy) will contribute positively towards the achievement of savings targets *and budgets* to enable the continued delivery and investment in key frontline services whilst achieving a balanced budget.

4. The Strategy aims to provide a robust and viable framework for the acquisition of commercial property investments and the pursuance of redevelopment and regeneration opportunities that can deliver positive financial returns for the Council.

5. The strategy is to set out how the Investment Property Portfolio will be managed and covers the following matters:

    - Objectives and strategic priorities for Investment Property
    - Governance and performance reporting arrangements
    - Risks
    - Portfolio Mix
    - Funding, Performance monitoring and Financial Indicators for Investment Property
    - Investment evaluation criteria
    - Acquisition procedure
    - Disposal Procedure

Background

6. The Local Government Act 2003 (the Act) and supporting regulations requires the Council to have regard to the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code and MHCLG Investment Guidance (the Guidance) to ensure that the Council’s capital investment plans are affordable, prudent and sustainable.

7. The Local Government Act 1972 – Section 120 of the Local Government Act 1972 empowers local authorities to acquire by agreement “any land whether situated inside or outside their area for the purpose of any of their functions under this or any other enactment, or for the benefit, improvement or development of their area”.

8. The Localism Act 2011 – Part 1, Section 1 of the Localism Act 2011 introduced a new “general power of competence” for local authorities who now have power to do anything that an individual may do, rather than be limited to those things which are related to or necessary for the discharge of an existing function of the authority. Section 1 continues to allow a local authority to express views and beliefs on a wide range of matters – as an individual generally might do. Local authorities are allowed to confer powers for a commercial purpose or for the benefit of the authority, its area or residents.

Government Guidance

9. In February 2018 the Secretary of State issued new guidance on Local Government Investments (the Guidance) which widened the definition of an investment to include all the financial assets of a local authority as well as non-financial assets held primarily of partially to generate a profit. This wider definition includes investment property portfolios as well as loans made to wholly owned companies or associates, joint ventures or third parties. This guidance applies for financial years commencing on or after 1 April 2018.

10. The Guidance requires the Strategy to be approved by Full Council on an annual basis and sets out the disclosure and reporting requirements. Any midyear material changes will also be subject to Full Council approval.

11. *Further CIPFA guidance was issued in November 2019 reinforces the need for a comprehensive Investment Strategy which covers the need for an Authority to have the competence in terms of expertise and experience to take effective decisions.*

Objectives and Strategic priorities for the Investment Property Portfolio

12. The objective of the Property Investment Strategy is to establish a framework for the identification of commercial property investments which, if acquired, would provide the council with a positive rental return and capital growth.

13. Each potential investment will be evaluated to ensure the income received is sufficient to provide an acceptable rate of return following the payment of current costs, acquisition costs, management fees and any running costs.

14. In delivering the strategy over the next year the following priorities are to be used to guide the growth of the Investment Property Portfolio:

    a) A major driver for acquisition of new investment property will be income generation.
    b) Properties that have a development potential will also be considered for their long term benefits.
    c) A target is included to increase the gross income from property investments as required in the Medium Term Financial Strategy.

15. Investments will be mainly focussed within the District boundary. A secondary priority will be for property outside of the District as long as this is within accepted guidelines for Local Council property investments. *The revised Guidance appreciates that if authorities only acquire properties in their own area geographical inequity will arise in terms of the opportunities for returns to be made. It is for this reason that an economic area of within 30 miles of the Council Boundary has been selected as a reasonable economic area limit.*

16. When making Investments the Strategy & Resources Committee will have regard to other economic and social benefits for the residents of Tandridge District.

17. Investment relating to the Strategy will be directed towards two areas of activity:-

    Investment Property Opportunities

    Prime and close to prime commercial real estate investment let on long leases to good covenants which will provide a secure long-term income over and above their ability to pay back the purchase price debt.

    The contributions from property investments will include

    - Income
    - Long Term Capital Growth

    Regeneration and Development Opportunities

    Investment which can facilitate/generate regeneration or economic development benefits as well as positive financial returns for the Council. Financial returns for the Council may come in the form of increased business rates or New Homes Bonus where the Investment is within the District.

    The Contributions from Regeneration and Development Investments will include positive financial returns for the Council and may also include the following:

    - Regeneration benefits for the area including employment opportunities
    - Economic benefits for the area

Governance and Performance

18. The Strategy and Resources Committee will be responsible for approving the strategic priorities and the arrangements set out in this policy. There will be an annual report to the Committee that will set out performance over the previous year and plans for the next.

19. Operational management, including acquisitions is to be delegated to officers acting within Financial Regulation 17 of the Council Constitution

    a) The Chief Executive in consultation with the Leader or deputy Leader and the Chair or vice chair of the Strategy & Resources Committee has delegated authority for acquisitions up to £10m

b) The Committee process will be used for acquisitions above £10m

20. The Council recognises that investing in land and properties to generate yield and capital returns is a specialist and potentially complex area. The council are going to require the services of professional property, legal and financial advisers, where appropriate in order to access specialist skills and resources to inform the decision-making process associated with the strategy.

21. The Head of Strategic Asset Management shall lead on potential purchases and development opportunities that meet the pre-determined selection criteria contained within the strategy. The criteria to evaluate potential acquisitions is attached as Annex 1. The Asset Management team will identify investment opportunities based on the selection criteria, will co-ordinate all necessary due diligence in accordance with the Acquisition Procedure (Annex 2) and will present a business case for challenge and scrutiny to the relevant Committee or Chief Executive as required under Financial Regulation 17.

22. The Guidance requires that elected members and officers involved in the investment decision-making process have appropriate capacity, skills and information to enable them to take informed decisions as to whether to enter into a specific investment. In addition, it places a duty on the council to ensure that advisors negotiating deals on behalf of the council are aware of the core principles of the prudential framework and the regulatory regime in which the council operates.

23. The council recognises that it is responsible for property investment decisions at all times and will ensure that undue reliance is not placed upon our external service providers.

24. The Head of Strategic Asset Management is to be accountable for the performance of the Investment Property Portfolio and will be charged with making recommendations to the Chief Executive for acquisitions.

25. Disposal of Investment Property assets are to be undertaken in accordance with the Council's Financial Regulations and delegated Authorities. The Head of Strategic Asset Management will make recommendations to the Strategy & Resources Committee and in accordance with officer delegated powers.

26. The Finance Committee delegates the Freehold Disposal of assets in the General Fund worth less than £250,000 to the Chief Executive in consultation with the Chair of the Strategy & Resources Committee. Leasehold disposals of General Fund assets of up to 16 years and with an annual rental valuation of up to £75,000 are also delegated to the Chief Executive, in consultation with the Chair of the Committee.

Risk Assessment

27. Property investment has its own specific risks, the principal ones being property risks, financial risks and corporate risks

    a) Property Risks – the property market is cyclical and is affected by the wider economic environment. There are also property risks that are specific to a building due to its location, condition and quality of the tenants. Mitigation proposed in this policy for these risks include diversifying the portfolio (portfolio mix) to include investments that perform during different cycles of the economic cycle. The evaluation criteria, diversity of location, due diligence tests, approval processes and accountability for implementation are also proposed to address property specific risks.

    b) Financial Risks – the primary financial risks are borrowing levels, interest rate movement, ongoing ability to service debts, the general investment market conditions and its effect on rental income. Proposals have included the creation of a fully owned subsidiary property investment company, Gryllus Property Ltd and a funding strategy that allocates debt and all associated costs to the investment property portfolio so that the net revenue benefits to the Council is transparent and can be benchmarked.

    c) Corporate Risks – effective delivery of the Strategy requires staff with the requisite expertise, effective arrangements for asset management and the recognition of the reputational risks that can come from inappropriate tenants and from legal and environmental breaches. In accordance with the Statement of Investment beliefs as we are investing public money we will be sensitive to the ethical considerations of local residents.

28. The Council assesses the risk of loss before entering into and whilst holding property. The approach is laid out in Annex 1 – Investment Evaluation Criteria.

Liquidity

29. Compared with other investment types, property is relatively difficult to sell and convert to cash at short notice and can take a considerable period to sell in certain market conditions. The funding of long term investments is financed by fixed long term borrowing, so that there is no short or medium term risk to the liquidity of the Council, which would require the Council to be forced to liquidate its asset and suffer a loss nor impact upon the Council's provision of services. As these long term investments are matched by long term borrowing, it will not be necessary to access the invested funds in an emergency. Investments in property are not undertaken unless they are secure over the medium term and the target rate of return significantly exceeds the annual cost of borrowing.

Portfolio Mix

30. The Strategy will have the medium and long term aim to:

a) Invest in property within the District Boundary, a secondary priority will be for property outside the District as long as this is within accepted guidelines for Local Council property investments. *The revised CIPFA Guidance appreciates that if authorities only acquire properties in their own area geographical inequity will arise in terms of the opportunities for returns to be made. It is for this reason that an economic area of within 30 miles of the Council Boundary has been selected as a reasonable economic area limit.*

b) Acquire properties mainly within the District in areas with strong sustainable economic activity i.e. areas with the environmental and business activities capable of providing an economy whereby capital and rental growth over the mid to long term was possible.

c) When making investments the Strategy and Resources Committee will have regard to other economic and social benefits for the residents of Tandridge.

d) Achieve a balanced portfolio where after 4 years no single class of property, ie retail, industrial, office and leisure is larger than 60% and none smaller than 10%, other than retail or leisure.

Contribution

31. The Council invests in commercial property with the intention of making a surplus that will be spent on local services. The portfolio is at an early stage of development.

32. Table 1 shows the properties currently held by Tandridge District Council for Investment Purposes in type

Property in Type	Type	Value in Accounts 31st March 2019	Value in Accounts 31st March 2020 (expected)
Offices	Offices	£4,645,000	£20,259,000
Leisure	Leisure	£0	£937,000
		£4,645,000	
VHC purchased Feb 2019		£924,000	
Total		**£5,569,000**	**£21,196,000**

33. Investments held under Gryllus Holdings are reported separately.

34. Income from Investment Property

	31st March 2019	31st March 2020 (expected)
Income	£225,500	£1,143,000

Funding and Financial Performance of the portfolio

35. The Council will fund investment property acquisitions by utilising the most appropriate and efficient funding strategy available at the time of purchase. The Council has the option of utilising long term prudential borrowing, capital receipts or reserves. Financing decisions will link to the Council's Capital & Investment Strategy and Treasury Management Strategy.

36. All new acquisitions are to achieve an appropriate positive return net of borrowing and other costs associated with the acquisition.

37. Separate accounts are to be kept for income and expenditure in connection with investment property and are to be included in the annual report to the Strategy & Resources Committee.

38. Key Indicators have been adopted to monitor performance of the portfolio. Performance will be reported against the following indicators along with a property market narrative:

    A) Total Return – the annual increase in capital value plus income expressed as a percentage of the previous year's capital value (adjusted to include purchases).
    B) Effective Return – total return receivable less costs expressed as a percentage of the previous year's capital value
    C) Growth in Asset Value – Percentage increase per year
    D) Income Growth – Percentage increase in gross income per year.
    E) Vacancy Rate – Expressed as a percentage and number of vacant units compared with total number of units. This will also be expressed in terms of lost rental. Void periods are factored into financial appraisals as part of the assessment criteria.

	2018/19	2019/20
A) Total Return	N/A	6.42%
B) Effective Return	N/A	3.31%
C) Growth in Asset Value	N/A	281%
D) Income Growth	N/A	407%
E) Vacancy Rate	N/A	No Vacant buildings. Quadrant House is 33% vacant

39. In addition to property specific performance indicators are quantitative indicators that will be reported within the Council's Capital & Investment Strategy and Treasury Management Strategy to allow Councillors and the Public to assess a local authority's total risk exposure as a result of commercial property investment decisions.

40. *The operating cost of the Council's internal Strategic Asset Management Team excluding the Housing Development Specialists is projected to be £201,823 for the year 2019/20. (£149,948 - 2018/19).* The costs reflect the cost of managing the Council's entire property portfolio and *functions*, not just the assets acquired under this Commercial Property Investment Strategy. Additional costs may be incurred as a result of the purchase of Commercial Investment Properties. Any such costs will be factored into the financial appraisals as part of the purchase assessment to ensure that anticipated net rates of return are achieved.

Commercial Property Investment Strategy – Annex A

Investment Evaluation Criteria

1. As with other forms of investment at the most basic level, property investment is a trade-off between risk and return. A traditional well diversified property portfolio (spread across different property sectors and geographical regions) will deliver long-term rental and capital growth with relatively low risk.

2. Prime property in the target region covered by this strategy will typically provide an initial yield of between 4.5 –7% with the additional prospect of capital growth leading to a higher total return to the Council. Equivalent /Income yields over longer periods will also be reported.

3. The four main property sectors will be included (industrial, office, retail and leisure) and in turn, these will be additionally diversified on criteria including location, the lease term and lot size. This will assist in protecting the councils overall risk return profile should an individual property investment cease to be income producing (for example, it is undergoing refurbishment or awaiting a new tenant)

4. The following Criteria are to be used to make decisions on acquiring new investment properties:

    a. **Location** – Property is categorised as prime, secondary or tertiary in terms of its location desirability. For example, a shop located in the best trading position in the town would be prime, where as a unit on a peripheral neighbourhood shopping parade would be considered tertiary.
    b. **Tenant covenant** – the financial strength of a tenant determines the security of the property is rental income. A financially weak tenant increases the likelihood that the property will fall vacant. The minimum acceptable financial strength for any given tenant will be determined through financial appraisal of company accounts and the use of appropriate methods of risk assessment and credit scoring. To minimise management and risk, the preference will be for single occupancy investments wherever possible.
    c. **Lease terms** – the lease is to be free from unencumbered/onerous terms. The lease must have mechanisms for the rent to be periodically reviewed to take into account inflation and upward market movement.
    d. **Occupational lease length** – the lease term will determine the duration of the tenant's contractual obligation to pay rent. The most attractive investments offer a long lease with a strong tenant covenant. The lease term will reflect any tenant break clause.
    e. **Building quality** – a brand-new or recently refurbished building will not usually require capital expenditure for at least 15 years. This is attractive for income investors requiring long-term rental income with a minimum of ongoing capital expenditure.
    f. **Tenure and Title** anything less than a freehold acquisition will need to be appropriately reflected in the price. The legal title is required to be clean and free from any onerous conditions.
    g. **Tenant repairing obligations**. – Under a full repairing and insuring lease (FRI), the tenant is responsible for the building's interior and exterior

maintenance/repair. The obligation is limited to the building's interior under an internal repairing and insuring lease (IRI). The preference will be to favour FRI terms (or FRI by way of service charge i.e. all costs relating to occupation repairs are born by the tenants administered through a service charge.

h. **Lot size** – to maintain portfolio balance the preference will be for no single property to exceed *£25 million* for a single let property.

In addition it must -

a. Have passed a **building and plant survey**
b. Show a **positive return** after making allowance for financing costs, borrowing repayments and other associated costs.
c. Be supported by an Independent **RICS Red Book Valuation**
d. Be accompanied by a **full business case report** prepared by the Head of Strategic Asset Management and other officers where relevant.

Each potential property investment will undergo a quantitative and qualitative appraisal and risk assessment to establish portfolio suitability and the legal and financial implications of the purchase.

All due diligence findings will be included in the reporting procedure. The business case is to include reference to all areas above, the financial modelling, a risk assessment matrix and SWOT analysis.

An investment opportunity that does not meet the minimum criteria and investment criteria may have separate investment or regeneration benefits and therefore may be considered separately under the regeneration and development stream of the strategy.

For a regeneration or development opportunity to be considered by the council it must:-

a. Deliver a rate of return commensurate with the deemed level of risk associated with the investment. The financial returns from regeneration activities may be capital rather than revenue. If the returns are capital all the full costs will be capitalised.
b. Be accompanied by a full business case prepared by the Head of Strategic Asset Management and other officers where relevant.

5. Some of the above criteria may be relaxed if the property is of strategic value to the Council and or it has gained Strategy & Resources Committee Approval.

Commercial Property Investment Strategy - Annex B

Acquisition and Disposal Procedure

Acquisition Procedure

1. Acquisition of new investment properties is to follow the following process:

Activity	**Acquisition Stage and Timeline Guide**
a) Property identified as a potential investment by Asset Management or by Agents *b) Property to be discussed with in house Legal team for initial review* c) Head of Strategic Asset Management to notify Chief Executive and the Investment Property Group (includes Head of Legal & Head of Finance) of potentially suitable property and summarise to seek views d) If possible obtain desktop valuation from suitably qualified and experienced Valuer e) Review the valuation against the cost of Borrowing with Finance f) Finance to undertake search of tenant to ascertain the company's current financial status g) Finance to produce initial financial appraisal ~~h) Head of Strategic Asset Management to Instruct / appoint external agent to carry out RICS Red Book valuation~~	Initial Review 2 to 3 weeks
i) Make offer for property, subject where appropriate to any of the following: • Contract • Approval by Chief Executive, or relevant Committee • *RICS Red Book valuation carried out by external Registered Valuer (independent of introducing Agent)* • Searches • Legal due diligence to include receipt and analysis of all leases to determine landlord's financial obligations • Disclosure of freehold title and review to ensure clear of any onerous restrictions. • Pre-acquisition survey by chartered building surveyor to include, if appropriate, structural, mechanical and electrical survey • Internal inspection • Energy Performance Certificate • Disability Discrimination Assessment if appropriate	Under Offer 3 to 4 weeks

- Environmental desktop study if search suggests one is appropriate - Asbestos Survey - Resolution of any TUPE transfer implications - VAT - Insurance requirements - Tax implications j) Instruct legal services to deal with contract documentation k) If appropriate based on any of the above, propose adjustment to purchase price to reflect the monetary value of any issues discovered.	
l) Complete any outstanding surveys/ M&E reports and resolve all contractual matters before exchange m) Complete TDC Strategic Asset Management Acquisition Checklist n) Complete full Business Case for approval in accordance with Financial Regulation 17. o) Following agreement of terms and before instructing exchange of contract prepare Record of Officer Delegated Decision Notice and advise Leader of the Opposition and Ward Councillors if located in the District prior to publication date p) Arrange for transfer of funds q) Arrange Insurance Cover r) Exchange Contracts, if not simultaneous with Completion	Exchange 1-2 weeks
s) Complete purchase. All Documents and Management handed over to Asset Management to take forward as appropriate.	Completion 1 day

2. Newly purchased property acquired under this strategy would be added to the existing portfolio. The Asset Management Team would undertake management to maintain and improve the performance of an investment property; or additional specialist resources may need to be brought in as required.

Disposal Procedure

3. Properties will be considered for sale based on their performance and fit for the portfolio.

4. Any property considered for sale should be appropriately marketed. If an off-market approach is made and considered the property would not be sold unless in excess of an independent Red Book Valuation to support such a decision

5. A property will be disposed of in accordance with the Financial Regulations of the Council's Constitution and in line with the Delegated Authority provisions in place. The Head of Strategic Asset Management will make recommendations to the Strategy & Resources Committee and in accordance with officer delegated powers.

6. ~~*The Strategy & Resources Committee delegates the Freehold Disposal of assets in the General Fund worth less than £250,000 to the Chief Executive in consultation with the Chair of the Finance Committee. Leasehold disposals between 16 and 99 years at a rental of up to £75,000 per annum and to a maximum lease length of 16 years if the rental is above £75,000 are also delegated to the Chief Executive Officer and Chair of the Strategy & Resources Committee (Part E Finance Committee, section 2(ii) and (iii) and 3(vi) and (vii)).*~~

Summary of Investments and Borrowing **Appendix D**

Investment	Investment Amount at 30/09/2019	Net Asset Value at 30/09/19	Yield Rate Note 1	Yield to 30/09/19 Note 2	Estimated Annual Return 2019/20 at 30/09/2019	2018/19 Actual
	£	£	%	£	£	£
Non - Specified (Financial Investments)- Long Term (over 12 mths)						
CCLA Property Fund	4,000,000	4,302,769	4.23	45,930	182,000	183,989
Schroders Bond Fund	3,000,000	2,873,584	4.50	30,838	129,300	120,508
UBS Multi Asset Fund	3,000,000	2,927,623	3.93	33,712	115,100	116,513
Funding Circle	2,000,000	1,995,299	3.40	34,114	67,800	98,171
CCLA Diversification Fund	2,000,000	2,049,420	3.20	34,329	65,600	67,030
Sub Total Non-specified (Financial Investments)	**14,000,000**	**14,148,695**		**178,923**	**559,800**	**586,211**
Non - Specified (Non-Financial Investments)- Long Term (over 12 mths)						
Gryllus Property Company Junior	342,000	342,000	10.47	0	35,800	35,807
Gryllus Property Company Senior	2,052,000	2,052,000	5.03	0	103,200	103,216
Gryllus Property Company Share Capital Note 3	1,026,000	0		0	0	0
Tandridge Leisure Ltd- Refurbishment Loan (TTLC)	33,750	33,750	3.75	940	1,300	1,222
Freedom Leisure- Loan (TLP)	1,065,429	1,065,429	5.50	31,963	58,600	74,580
Freedom Leisure- Loan (de Stafford)	682,786	682,786	7.58	28,230	51,800	65,870
Caterham Barracks Note 4	257,813	257,813	7.58	10,070	10,300	9,627
Gryllus Property Company Loan	945,000	945,000	5.81	0	54,900	0
Gryllus Property Company Share Capital	405,000	405,000		0	0	0
Sub Total Non-specified (Non-Financial Investments)	**6,809,777**	**5,783,777**		**71,203**	**315,900**	**290,322**
Total Non-Specified Investments	**20,809,777**	**19,932,473**		**250,125**	**875,700**	**876,533**
Specified Investments-Short Term (less than 12 mths)						
Banks/Building Societies Deposits	0	-	1.03	6,381	6,000	19,779
Notice Accounts	2,000,000	2,027,982	0.84	9,320	18,300	19,895
Money Market Funds	9,355,000	8,823,529	0.68	30,389	60,000	44,483
Total Specified Investments	**11,355,000**	**10,851,512**		**46,091**	**84,300**	**84,157**
Total Non- Specified and Specified Investments	**32,164,777**	**30,783,985**		**296,216**	**960,000**	**960,690**
Total Investment Income Budget 2019/20					975,900	
Over/(under) budget					**(15,900)**	

Borrowing	Loan Amount	Estimated Average Borrowing	Interest	Expenditure to 30/09/19	Estimated Cost 2019/20 at 30/09/2019
	£	£	%	£	£
General Fund Borrowing					
Gryllus-PWLB	3,420,000	3,420,000	2.46	42,066	84,100
Freedom Leisure-PWLB	2,225,000	2,225,000	2.45	27,256	54,500
Village Health Club	938,678	938,678	2.38	11,170	22,300
Linden House	4,175,000	4,175,000	2.69	56,154	112,300
Linden House	254,000	249,100	2.42	3,073	6,000
Quadrant House	15,340,000	15,340,000	2.41	184,847	369,700
Quadrant House	800,000	784,700	2.28	9,120	17,900
80-84 Station Road	724,400	710,500	2.28	8,258	16,200
Sub Total General Fund Borrowing	**27,877,078**	**27,842,978**		**341,945**	**683,000**
HRA Borrowing					
Public Works Loan Board	61,189,000	61,189,000	2.76	844,316	1,688,600
Sub Total HRA Borrowing	**61,189,000**	**61,189,000**		**844,316**	**1,688,600**
Total Borrowing	**89,066,078**	**89,031,978**		**1,186,261**	**2,371,600**

Notes

1. Yield Rate
CCLA Property Fund dividend yield Sept 19 Est provided by CCLA
Schroders Strategic Credit Fund Fact sheet on Schroders.com distribution yield as at 30 Aug 2019
UBS underlying yield latest per UBS Fact Sheet (Aug 19)
CCLA Diversified Fund dividend yield Aug 19 provided by CCLA
Funding Circle yield based on net earnings to date per Funding Circle statement

2. Yield to 30/09/19 include actuals received or notified of at this date - CCLA Property Fund, Schroders & UBS all only have the first quarter

3. No dividend will be paid in the current year

4. Caterham Barracks Community Trust have requested to repay their loan at the end of October 2019. These figures reflect this

Market Value of Long Term Investments

Prepared on 16/10/19

Appendix E

Carrying Value	Carrying Value 31.3.2017	Carrying Value 31.3.2018	Carrying Value 30.6.2018	Carrying Value 30.9.2018	Carrying Value 31.12.2018	Carrying Value 31.3.2019	Carrying Value 30.6.2019	Carrying Value 30.9.2019
	£	£	£	£	£	£	£	£
CCLA Property Fund	4,000,000	4,000,000	4,000,000	4,000,000	4,000,000	4,000,000	4,000,000	4,000,000
Schroders Bond Fund	3,000,000	3,000,000	3,000,000	3,000,000	3,000,000	3,000,000	3,000,000	3,000,000
UBS Multi Asset Fund	3,000,000	3,000,000	3,000,000	3,000,000	3,000,000	3,000,000	3,000,000	3,000,000
CCLA Diversification Fund	n/a	2,000,000	2,000,000	2,000,000	2,000,000	2,000,000	2,000,000	2,000,000
Total	10,000,000	12,000,000	12,000,000	12,000,000	12,000,000	12,000,000	12,000,000	12,000,000

Market Value	Market Value 31.3.2017	Market Value 31.3.2018	Market Value 30.6.2018	Market Value 30.9.2018	Market Value 31.12.2018	Market Value 31.3.2019	Market Value 30.6.2019	Market Value 30.9.2019
	£	£	£	£	£	£	£	£
CCLA Property Fund(mid-market value)	4,082,986	4,276,854	4,299,512	4,300,362	4,369,186	4,276,005	4,346,669	4,302,769
Schroders Bond Fund	2,963,563	2,912,837	2,908,609	2,891,399	2,825,575	2,865,130	2,910,421	2,873,584
UBS Multi Asset Fund	3,018,705	2,918,160	2,895,094	2,905,148	2,777,398	2,868,479	2,916,977	2,927,623
CCLA Diversification Fund(indicative market value)	n/a	1,921,257	1,972,126	1,990,756	1,913,197	1,982,167	2,032,111	2,049,420
Total	10,065,254	12,029,108	12,075,341	12,087,665	11,885,356	11,991,781	12,206,179	12,153,396

Surplus/(Deficit)	Surplus/ (Deficit) 31.3.2017	Surplus/ (Deficit) 31.3.2018	Surplus/ (Deficit) 30.6.2018	Surplus/ (Deficit) 30.9.2018	Surplus/ (Deficit) 31.12.2018	Surplus/ (Deficit) 31.3.2019	Surplus/ (Deficit) 30.6.2019	Surplus/ (Deficit) 30.9.2019
	£	£	£	£	£	£	£	£
CCLA Property Fund	82,986	276,854	299,512	300,362	369,186	276,005	346,669	302,769
Schroders Bond Fund	(36,437)	(87,163)	(91,391)	(108,601)	(174,425)	(134,870)	(89,579)	(126,416)
UBS Multi Asset Fund	18,705	(81,840)	(104,906)	(94,852)	(222,602)	(131,521)	(83,023)	(72,377)
CCLA Diversification Fund	n/a	(78,743)	(27,874)	(9,244)	(86,803)	(17,833)	32,111	49,420
Total	65,254	29,108	75,341	87,665	(114,644)	(8,219)	206,179	153,396

N/R = Data not available from fund manager

Gross Revenue Yield	Yield 2016/17	Yield 2016/17	Yield 2017/18	Yield 2017/18	Yield 2018/19	Yield 2018/19
	£	%	£	%	£	%
CCLA Property Fund	164,434	4.03%	193,758	4.53%	183,989	4.30%
Schroders Bond Fund	127,340	4.30%	105,413	3.62%	120,508	4.21%
UBS Multi Asset Fund	100,600	3.33%	146,788	5.03%	116,513	4.06%
CCLA Diversification Fund	n/a	n/a	62,732	3.27%	67,030	3.38%
Total	392,375		508,691		488,040	

Surplus/(Deficit)- Capital Value	Surplus/ (Deficit) 2016/17	Surplus/ (Deficit) 2016/17	Surplus/ (Deficit) 2017/18	Surplus/ (Deficit) 2017/18	Surplus/ (Deficit) 2018/19	Surplus/ (Deficit) 2018/19
	£	%	£	%	£	%
CCLA Property Fund	(92,996)	-2.28%	193,868	4.53%	(849)	-0.02%
Schroders Bond Fund	16,634	0.56%	(50,726)	-1.74%	(47,707)	-1.67%
UBS Multi Asset Fund	36,559	1.21%	(100,545)	-3.45%	(49,681)	-1.73%
CCLA Diversification Fund	n/a	n/a	(78,743)	-4.10%	60,910	3.07%
Total	(39,803)		(36,146)		(37,327)	

Net Yield	Net Yield 2016/17	Net Yield 2016/17	Net Yield 2017/18	Net Yield 2017/18	Net Yield 2018/19	Net Yield 2018/19
	£	%	£	%	£	%
CCLA Property Fund	71,438	1.75%	387,626	9.06%	183,140	4.28%
Schroders Bond Fund	143,974	4.86%	54,687	1.88%	72,801	2.54%
UBS Multi Asset Fund	137,159	4.54%	46,243	1.58%	66,832	2.33%
CCLA Diversification Fund	n/a	n/a	(16,011)	-0.83%	127,940	6.45%
Total	352,572		472,545		450,713	

Peer to Peer Investment

							Half Year	
	2016/17	2016/17	2017/18	2017/18	2018/19	2018/19	2019/20	2019/20
Funding Circle	£	%	£	%	£	%	£	%
Carrying Value	**2,004,525**		**2,003,498**		**1,971,379**		**1,995,299**	
Interest Paid by Borrowers	219,299		181,591		212,877		95,730	
Less FC Service fee	(36,267)		(19,669)		(19,707)		(9,896)	
Bad Debts	(89,587)		(61,288)		(100,515)		(63,911)	
Amounts Recovered on principal in prior years (since 06.04.15)	9,869		14,780		15,513		12,191	
Amounts Recovered on principal in prior years (prior to 06.04.15)	0		0		2			
Net Yield	**103,315**	**5.15%**	**115,415**	**5.76%**	**108,171**	**5.49%**	**34,114**	**1.71%**
Provisions for future losses	**0**		**0**		**(10,000)**			

APPENDIX F **APPENDIX F**

1. Tandridge District Council's Statement of investment beliefs

Assets

1.1 There are 3 pools of assets which have different objectives and constraints -

- *Short-term Pool*: short-term cash management, representing monies that need to be available for immediate funding needs of the Council, typically up to a period of 1 year.

- *Medium-term Pool*: where funds are not immediately required but may be required over a 1 to 5 year period. These investments will achieve a return of approximately cash base rate plus 2% as an indicative target.

- *Strategic Investment Pool*: where funds can be invested for the long term (greater than 3 years), to deliver returns in real terms, aiming to achieve additional revenue to support front line services of the council. These investments will seek to achieve the prevailing consumer price inflation (CPI) rate plus 3%.

Aims

1.2 The 3 pools have different aims. In the list above –

- *Short-term pool:* represents short-term liquid assets, which are invested to provide immediate liquidity. To manage risk, these assets are held in a way that achieves a measure of diversification. Where appropriate and after member input, the officers will from time to time investigate whether there is any possibility to move some of these funds into the medium term pool in the search for additional returns.

- *Medium-term pool:* is aimed at preserving the value of the funds in real terms in the medium term, assumed to be 1 to 5 years. Pure equity investment would generally not be an appropriate form of investment for the medium-term pool, but balanced portfolios incorporating an equity element may be appropriate.

- *Strategic Investment pool:* is aimed at preserving the value of funds in real terms in the medium to long term, while achieving revenue well in excess of the borrowing costs for the council. These investments will mainly be financed through external borrowing. Such investments may be very long term in nature and it is recognised that liquidity will be restricted. Timing of purchases and disposals is vital to preserve fund value.

Key beliefs

1.3 *The aims for each pool are the key drivers for asset allocation*

1.3.1 Of the three pools of assets referred to above:

- *The Short-term pool* is roughly matched to immediate or very short-term cash requirements. Therefore, the nominal value and liquidity must be preserved.

- *Medium-term pool* has no specifically defined liabilities. The prime aim is capital preservation in real terms to achieve an enhanced return over 1–5 years.

- *Strategic Investment pool* represents long-term assets and any investment strategy must seek at least to maintain the value of these assets after allowing for inflation, as well as to generate revenue in excess of the loan interest cost plus the minimum revenue provision (MRP). It is acknowledged that this cannot be achieved without accepting some risk. Where there is some conflict between any of these aims, the need to generate income exceeding the loan rate plus Minimum Revenue Provision (MRP) for the specific investment will be paramount.

1.4 *Asset allocation is the main driver of performance*

1.4.1 We believe that the performance of investment markets is the dominant aspect of investment.

1.4.2 Attempting to "time" markets is rarely successful as market timing introduces risk, without the expectation of return, so variations in asset allocation will be driven by other considerations rather than tactical return generation. These considerations as determined in the over-arching Treasury Management Strategy includes factors such as; credit risk, counter-party strength, security, liquidity and yield as well as interest rate risk and inflation. Asset allocation in multiple classes will also be a factor.

1.5 *<u>Costs matter and need to be managed in order to achieve value for money</u>*

1.5.1 Costs can materially impact the long-term value of the investment portfolio and are an important component in assessing different investment strategies and the managers appointed to invest Council assets. This does not necessarily imply that costs need to be minimised: there are often circumstances when paying extra costs will be more than compensated by rewards.

1.5.2 Careful management of costs is important in achieving the highest quality of returns on all our portfolios.

1.6 *<u>Investment decisions should reflect wider stakeholder views</u>*

1.6.1 Our stakeholders, including local residents, expect the Council to follow the highest ethical standards in all its activities. Strategy & Resources Committee members will therefore act in accordance with the Committee on Standards in Public Life's seven principles of public life, namely selflessness, integrity, objectivity, accountability, openness, honesty and leadership. We expect the investment professionals we deal with to act in a similar manner.

1.6.2 We are always conscious that we are investing public money and we will be sensitive to the ethical considerations of local residents.

1.7 *<u>Investment goals and performance measures need to be clearly articulated to ensure accountability</u>*

1.7.1 A key measure of success is the delivery of investment performance. It is important that the investment goal and the performance measures used are clearly set out to ensure full accountability, in accordance with the aims of each pool, which are respectively liquidity, capital preservation in capital terms and capital preservation in real terms with yields in excess of borrowing costs including MRP as appropriate.

1.8 *<u>Risk is multi-faceted and complex</u>*

1.8.1 The only investment opportunities that provide no "risk" in the sense of no possibility of unexpected negative outcomes are those that will provide negative inflation-adjusted returns. It is therefore necessary to accept some risk if positive inflation-adjusted returns are to be achieved.

1.8.2 A selection of appropriate performance measures will allow visibility that adequate compensation for risk taken has been achieved.

1.9 *<u>A long-term investment horizon is an advantage and a responsibility</u>*

1.9.1 The long-term horizon for the Strategic Investment pool brings with it the responsibility to take an appropriately long-term approach to assessing the success or otherwise of investment strategies and the advisers hired to implement our strategies.

1.9.2 The Strategic Investment pool and (to a lesser extent) medium-term pool have long to medium horizons which provide additional investment opportunity. This potentially allows the acceptance of less liquidity on a portion of assets. This may include extended periods of underperformance due to the long term nature of investments in the context of the aims described at 1.2.

1.10 *The Strategic Investment pool will mainly invest in property*

1.10.1 Given the constraints that apply to Local Councils, most of the Strategic Investment pool will be invested in property.

1.10.2 The first priority for investment will be property within the District boundary, a secondary priority will be for property outside of the District as long as this is within accepted guidelines for Local Council property investments.

1.10.3 When making investments the Strategy & Resources Committee will have regard to other economic and social benefits for the residents of Tandridge District.

1.11 *Investment strategies and complexity need to be consistent with the governance resources available*

1.11.1 One of the most significant constraints on investment strategy is the level of governance resources available. The complexity of strategies employed needs to be consistent with the resources available to manage them. In practice, this will normally mean that simple solutions will be preferred to complex ones unless there is a compelling reason to contemplate the complexity: this will normally be driven by a conviction that there are significant additional returns to be achieved and obtaining suitable outside professional advice to support this conviction.

2 What funds are available for investing?

2.1 In determining the allocation of funds to each of the 3 pools (short, medium-term and Strategic Investment pool), the Strategy & Resources Committee will, on a regular basis, consider relevant budgets, cash flow forecasts and other medium term financial projections. The main allocation will be the annual budget setting process.

2.2 Allocation of funds on this basis will normally be reviewed on at least, an annual basis, to tie in with relevant financial projections and quarterly reports from external investment advisers.

2.3 In terms of the allocation process for the medium term pool, the Strategy & Resources Committee will have the authority to select investments in line with our investment beliefs. For investments through Gryllus, these will be in accordance with the company's individual investment objectives as an entity.

3 Risk Management

3.1 We will be proactive in looking at risk including assessing this in terms of the risk framework set out in both the Asset (Capital) Investment and the Treasury Management Strategy. These strategies will be approved annually by Council and will be updated as necessary to cover risk including credit risk, counter-party risk, timing risks around purchasing and disposing of strategic assets; and the over-riding public sector investment principle of security and liquidity over yield.

3.2 Counter parties will only be selected with acceptable credit ratings from the three main rating agencies: Fitch Ratings Ltd, Moody's Investor Service inc and Standard and Poor's Financial Services LLC.

3.3 In respect of actual investment performance and having taken any external advice considered appropriate, the Council will monitor and review performance benchmarks relevant to each investment pool and in accordance with the recommended CIPFA Investment Code of Practice.

3.4 The Council will approve an annual Treasury Management Strategy (TMS) which will be approved annually by Council and incorporated within the Budget Book and Medium Term Financial Strategy (MTFS).