

## North East Derbyshire District Council

### Investment Strategy 2019/20 – 2022/23

#### Introduction

- 1.1 The Council invests its money for three broad purposes:
- because it has surplus cash as a result of its day-to-day activities, for example when income is received in advance of expenditure (**treasury management investments**),
  - to support local public services by lending to or buying shares in other organisations (**service investments**), and
  - to earn investment income (**commercial investments**).
- 1.2 This investment strategy is a new report for 2019/20, meeting the requirements of the 2018 Ministry of Housing, Communities and Local Government (MHCLG) Investment Guidance, and focuses on the second and third of these categories.

#### Treasury Management Investments

- 1.3 The Council typically receives its income in cash (e.g. from taxes and grants) before it pays for its expenditure in cash (e.g. through payroll and invoices). It also holds reserves for future expenditure and collects local taxes on behalf of other local authorities and central government. These activities, plus the timing of borrowing decisions, lead to a cash surplus which is invested in accordance with guidance from the Chartered Institute of Public Finance and Accountancy. The balance of treasury management investments is expected to fluctuate between £11.8m and £24.5m during the 2019/20 financial year.
- 1.4 **Contribution:** The contribution that these investments make to the objectives of the Council is to support effective treasury management activities.
- 1.5 **Further details:** Full details of the Council's policies and its plan for 2019/20 for treasury management investments are covered in the Treasury Management Strategy.

### **Service Investments: Loans**

- 1.6 **Contribution:** The Council lends money to assist local public services, including making loans to local service providers and businesses to stimulate local economic growth. This includes loans to the Council's ALMO, Rykneld Homes Ltd to allow development of social housing. Rykneld Homes Ltd is a wholly owned subsidiary of the Council, limited by guarantee.
- 1.7 **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 Council, upper limits on the outstanding loans to each category of borrower have been set as follows:

**Table 1: Loans for service purposes**

Category of borrower	31/3/2018 actual			2019/20
	Balance owing £m	Loss allowance £m	Net figure in accounts £m	Approved Limit £m
Rykneld Homes Ltd	5.5	0	5.5	13.0
Northwood Group Ltd	0	0	0	7.7
<b>TOTAL</b>	<b>5.5</b>	<b>0</b>	<b>5.5</b>	<b>20.7</b>

- 1.8 Accounting standards require the Council to set aside loss allowance for loans, reflecting the likelihood of non-payment. The figures for loans in the Council's statement of accounts from 2018/19 onwards will be shown net of this loss allowance. However, the Council makes every reasonable effort to collect the full sum lent and has appropriate credit control arrangements in place to recover overdue repayments.
- 1.9 **Risk assessment:** The Council assesses the risk of loss before entering into and whilst holding service loans by requiring a fully costed business case in all instances that includes any investment/loan requirements and financial/risk implications. A significant amount of due diligence work is undertaken in each case to ensure the business case is robust. Regards loans to Rykneld Homes Ltd, the strength of the partnership between the company and the Council helps to mitigate any risk associated with non-payment of the loan.

### **Service Investments: Shares**

- 1.10 **Contribution:** The Council has invested £0.15m to date in the shares of Northwood Group Ltd to support local public services and stimulate local economic growth by delivering housing developments whilst generating income for the Council.

- 1.11 **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 2: Shares held for service purposes**

Category of company	31/3/2018 actual			2019/20
	Amounts invested £m	Gains or losses £m	Value in accounts £m	Approved Limit £m
Northwood Group Ltd	0.15	0	0.15	1.11
<b>TOTAL</b>	<b>0.15</b>	<b>0</b>	<b>0.15</b>	<b>1.11</b>

- 1.12 **Risk assessment:** The Council assesses the risk of loss before entering into and whilst holding shares by working with experienced professionals who have extensive knowledge of the projects and the local markets. In order that commercial investments remain proportionate to the size of the Council, these are subject to overall maximum investment limits and contingency plans are in place should expected yields not materialise.
- 1.13 **Liquidity:** the viability models for each project the Council considers take account of the maximum periods for which funds may prudently be committed and states what those maximum periods are within approved contracts. This will assist the Council to stay within its stated investment limits.
- 1.14 **Non-specified Investments:** Shares are the only investment type that the Council has identified that meets the definition of a non-specified investment in the government guidance. The Council has not adopted any procedures for determining further categories of non-specified investment since none are likely to meet the definition.

**Commercial Investments: Property**

- 1.15 MHCLG defines property to be an investment if it is held primarily or partially to generate a profit.
- 1.16 **Contribution:** The Council invests in local, commercial and residential property with the intention of making a profit that will be spent on local public services. This includes the industrial units across the district as well as residential property development through Northwood Group Ltd.

**Table 3:** Property held for investment purposes

Property	Actual	31/3/2018 actual		31/3/2019 expected	
	Purchase cost	Gains or (losses)	Value in accounts	Gains or (losses)	Value in accounts
Industrial Units	4.5	0.2	4.7	0	4.7
Land	2.2	6.2	8.4	0	8.4
Commercial Properties	1.1	(0.1)	1.0	0	1.0
Shared Ownership Properties	1.0	0	1.0	0	1.0
Northwood Group Ltd	0	0	0	0	0
<b>TOTAL</b>	<b>8.8</b>	<b>6.3</b>	<b>15.1</b>	<b>0</b>	<b>15.1</b>

- 1.17 **Security:** In accordance with government guidance, the Council considers a property investment to be secure if its accounting valuation is at or higher than its purchase cost including taxes and transaction costs.
- 1.18 A fair value assessment of the Council's investment property portfolio has been made within the past twelve months, and the underlying assets provide security for capital investment.
- 1.19 On revaluation the commercial properties decreased by £0.1m as a result of a general fall in market valuations of properties of this nature. This has no material impact on the security of the investment and the revenue implication was £0.1m, accounted for in 2017/18.
- 1.20 **Risk assessment:** The Council assesses the risk of loss before entering into and whilst holding property investments by working with experienced professionals who have extensive knowledge of the projects, properties and local markets. In order that commercial investments remain proportionate to the size of the Council, these are subject to overall maximum investment limits and contingency plans are in place should expected yields not materialise.
- 1.21 **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 Council's Treasury Management Strategy provides assurances through limits on long-term investments to ensure that the invested funds or suitable alternatives can be accessed when they are needed, for example to repay capital borrowed.

## **Loan Commitments and Financial Guarantees**

- 1.22 Although not strictly counted as investments, since no money has exchanged hands yet, loan commitments and financial guarantees carry similar risks to the Council and are included here for completeness.
- 1.22 The Council has contractually committed to make up to £7.7m of loans to Northwood Group Ltd should it request it. The Council has also guaranteed loans of £8.1m to Rykneld Homes Ltd.

## **Borrowing in Advance of Need**

- 1.23 Government guidance is that local authorities must not borrow more than or in advance of their needs purely in order to profit from the investment of the extra sums borrowed.

## **Capacity, Skills and Culture**

- 1.24 **Elected members and statutory officers:** The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. Suitably qualified and experienced officers are employed throughout the Council to perform such functions.
- 1.25 Where Council officers 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 Arlingclose Limited as treasury management 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.
- 1.26 Members receive individual training and development through the Member Development Programme and are periodically required to attend seminars held by the external treasury management advisors.
- 1.27 **Commercial deals:** All Officers involved in negotiating such arrangements are aware of the core principles of the prudential framework and of the regulatory regime within which local authorities operate and considerable due diligence is undertaken in all instances.
- 1.28 **Corporate governance:** All decisions regards new loans or investments of this nature are considered by the Council's Cabinet before being recommended for approval at Council. Any presentation to members will have been through a fully costed business case that includes any investment/loan requirements and financial/risk implications. A significant amount of due diligence work is undertaken in each case to ensure the business case is robust before reporting to Cabinet.

## Investment Indicators

- 1.29 The Council has set the following quantitative indicators to assess the total risk exposure as a result of its investment decisions.
- 1.30 **Total risk exposure:** The first indicator shows the Council's total exposure to potential investment losses. This includes amounts the Council is contractually committed to lend but have yet to be drawn down and guarantees the Council has issued over third party loans.

**Table 5:** Total investment exposure

<b>Total investment exposure</b>	<b>31/03/2018 Actual £m</b>	<b>31/03/2019 Forecast £m</b>	<b>31/03/2020 Forecast £m</b>
Treasury management investments	13.80	10.60	10.00
Service investments: Loans – Rykneld Homes Ltd	5.50	13.00	13.00
Service investments: Loans – Northwood Group Ltd	0	0	7.70
Service investments: Shares – Northwood Group Ltd	0.15	0.15	1.11
Commercial investments: Property	15.10	15.10	15.10
<b>TOTAL INVESTMENTS</b>	<b>34.55</b>	<b>38.85</b>	<b>46.91</b>
Commitments to lend	0	8.66	0
<b>TOTAL EXPOSURE</b>	<b>34.55</b>	<b>47.51</b>	<b>46.91</b>

- 1.31 **How investments are funded:** Government guidance is that these indicators should include how investments are funded. Since the Council does not normally associate particular assets with particular liabilities, this guidance is difficult to comply with. To date these investments have been funded by usable reserves and income received in advance of expenditure. It is planned that this approach will continue in the medium term as internal resources allow.
- 1.32 **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 6: Investment rate of return (net of all costs)**

<b>Investments net rate of return</b>	<b>2017/18 Actual £m</b>	<b>2018/19 Forecast £m</b>	<b>2019/20 Forecast £m</b>
Treasury management investments	0.27%	0.36%	0.28%
Service investments: Loans – Rykneld Homes Ltd	3.26%	2.50%	3.42%
Service investments: Loans – Northwood Group Ltd	0.00%	0.00%	6.00%
Service investments: Shares – Northwood Group Ltd	0.00%	0.00%	0.00%
Commercial investments: Property	4.08%	2.39%	2.78%

- 1.33 The indicators used to report on the risks and opportunities associated with investment decisions will be kept under review as the Council's Investment Strategy and activities evolve over time.