

North East Derbyshire District Council

Council

30 January 2023

Treasury Strategy Reports 2023/24 - 2026/27

Report of the Portfolio Holder for Economy, Transformation and Climate Change

Classification: This report is public

Report By: Jayne Dethick, Director of Finance and Resources (S151 Officer)

Contact Officer: Jayne Dethick

PURPOSE/SUMMARY

The purpose of this report is to provide Council with the necessary information to approve the Council's suite of Treasury Strategies for 2023/24 to 2026/27.

RECOMMENDATIONS

1. That Council approve the Treasury Management Strategy at **Appendix 1** and in particular:
 - a) Approve the Borrowing Strategy
 - b) Approve the Investment Strategy
 - c) Approve the use of the external treasury management advisors Counterparty Weekly List (or similar) to determine the latest assessment of the counterparties that meet the Council's Criteria before any investment is undertaken.
 - d) Approve the Prudential Indicators
2. That Council approve the Capital Strategy as set out in **Appendix 2** and in particular:
 - a) Approve the Capital Financing Requirement
 - b) Approve the Minimum Revenue Provision Statement for 2023/24
 - c) Approve the Prudential Indicators for 2023/24, in particular:

Authorised Borrowing Limit £217.5m

Operational Boundary £212.5m

3. That Council approve the Investment Strategy as set out in **Appendix 3**.
4. That Council approve the Flexible Use of Capital Receipts Strategy at **Appendix 4**

Approved by the Portfolio Holder

IMPLICATIONS

Finance and Risk

Yes ✓ No

These are considered throughout the report.

On Behalf of the Section 151 Officer

Legal including Data Protection

Yes ✓ No

As part of the requirements of the CIPFA Treasury Management Code of Practice the Council is required to produce every year a Treasury Management Strategy and Capital Strategy which requires approval by full Council prior to the commencement of each financial year. This report is prepared in order to comply with these obligations.

There are no Data Protection issues arising directly from this report.

On Behalf of the Solicitor to the Council

Staffing

Yes No ✓

There are no staffing issues arising directly from this report.

On Behalf of the Head of Paid Service

DECISION INFORMATION

<p>Is the decision a Key Decision? A Key Decision is an executive decision which has a significant impact on two or more District wards or which results in income or expenditure to the Council above the following thresholds:</p> <p>NEDDC: Revenue - £100,000 <input checked="" type="checkbox"/> Capital - £250,000 <input checked="" type="checkbox"/> <input checked="" type="checkbox"/> <i>Please indicate which threshold applies</i></p>	<p>No</p>
<p>Is the decision subject to Call-In? (Only Key Decisions are subject to Call-In)</p>	<p>No</p>
<p>District Wards Significantly Affected</p>	<p>None</p>
<p>Consultation:</p>	<p>Yes</p>

Leader / Deputy Leader <input type="checkbox"/> Cabinet <input type="checkbox"/> SMT <input checked="" type="checkbox"/> Relevant Service Manager <input checked="" type="checkbox"/> Members <input checked="" type="checkbox"/> Public <input type="checkbox"/> Other <input type="checkbox"/>	Details: Audit and Corporate Governance Scrutiny Committee 18 January 2023
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Links to Council Plan priorities, including Climate Change, Equalities, and Economics and Health implications.
All

REPORT DETAILS

- 1.1 Treasury risk management at the Council is conducted in compliance with the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice 2021 Edition* (the CIPFA Code) which requires the Council to approve a treasury management strategy before the start of each financial year. This report fulfils the Council's legal obligation under the *Local Government Act 2003* to have regard to the CIPFA Code.
- 1.2 The CIPFA Code requires that a Capital Strategy be produced alongside the Treasury Management Strategy along with a Flexible Use of Capital Receipts Strategy. In addition, the 2018 Investment Guidance issued by the Department for Levelling Up, Housing and Communities also requires local authorities to produce an investment Strategy. So there is now a requirement to produce four separate treasury strategies for Council to approve.
- 1.3 The Council's Treasury Management Strategy provides the framework for managing the Council's cash flows, borrowing and investments, and the associated risks for the years 2023/24 to 2026/27. The Strategy also sets out the parameters for all borrowing and lending as well as listing all approved borrowing and investment sources. Prudential indicators aimed at monitoring risk are also included. **(Appendix 1)**.
- 1.4 The Capital Strategy is intended to provide a high level, concise overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of the Council's services. The report provides an overview of the associated risk, its management and the implications for future financial sustainability. The Capital Strategy also sets out the capital expenditure plans for the period and how they will be financed. It includes information of the minimum revenue provision, capital financing requirement and prudential indicators aimed at monitoring risk **(Appendix 2)**.
- 1.5 The Investment Strategy focuses on investments made for service purposes and commercial reasons, rather than those made for treasury management. Investments covered by this strategy include earning income through commercial investments or by supporting local services by lending to or buying shares in other organisations **(Appendix 3)**.
- 1.6 The Flexible Use of Capital Receipts Strategy focuses on the Council's plans to utilise capital receipts for service reform in strict adherence of S15 (1) of the Local Government Act 2003 **(Appendix 4)**.

2 Reasons for Recommendation

2.1 This report outlines the Council's proposed suite of Treasury Strategies for the period 2023/24 to 2026/27 for consideration and approval by Council. It contains:

- The Treasury Management Strategy which provides the framework for managing the Council's cash flows, borrowing and investments for the period.
- The Capital Strategy which is intended to provide a high level, concise overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of the Council's services.
- The Investment Strategy which focuses on investments made for service purposes and commercial reasons, rather than those made for treasury management.
- The Flexible Use of Capital Receipts Strategy which details plans to utilise capital receipts for service reform in strict adherence with S15 (1) of the Local Government Act 2003.

The above strategies provide an approved framework within which the officers undertake the day to day capital and treasury activities.

3 Alternative Options and Reasons for Rejection

3.1 Alternative options are considered throughout the report.

DOCUMENT INFORMATION

Appendix No	Title
1	Treasury Management Strategy 2023/24 – 2026/27
2	Capital Strategy 2023/24 – 2026/27
3	Investment Strategy 2023/24 – 2026/27
4	Flexible Use of Capital Receipts Strategy 2023/24 – 2024/25
Background Papers	



North East Derbyshire District Council

Treasury Management Strategy 2023/24 – 2026/27

Introduction

- 1.1 Treasury Management is the management of the Council's cash flows, borrowing and investments, and the associated risks. The Council has borrowed and invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of financial risk are therefore central to the Council's prudent financial management.
- 1.2 Treasury risk management at the Council is conducted within the framework of the *Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2021 Edition* (the CIPFA Code) which requires the Council to approve a treasury management strategy before the start of each financial year. This report fulfils the Council's legal obligation under the *Local Government Act 2003* to have regard to the CIPFA code.
- 1.3 Investments held for service purposes or for commercial profit are considered in a different report, the Investment Strategy.

External Context

- 1.4 **Economic background:** The ongoing impact on the UK from the war in Ukraine, together with higher inflation, higher interest rates and a deteriorating economic outlook, will be major influences on the Council's treasury management strategy for 2023/24.
- 1.5 The Bank of England (BoE) increased Bank Rate by 0.5% to 3.5% in December 2022. This followed a 0.75% rise in November which was the largest single rate hike since 1989 and the ninth successive rise since December 2021. The December decision was voted for by a 6-3 majority of the Monetary Policy Committee (MPC), with two dissenters voting for a no-change at 3% and one for a larger rise of 0.75%.
- 1.6 The November quarterly Monetary Policy Report (MPR) forecast a shallow recession in the UK with CPI inflation remaining elevated at over 10% in the near-term. While

the projected peak of inflation is lower than in the August report, due in part to the government's support package for household energy costs, inflation is expected remain higher for longer over the forecast horizon and the economic outlook remains weak, with unemployment projected to start rising.

- 1.7 The UK economy grew by 0.3% between July and September 2022 according to the Office for National Statistics, and the BoE forecasts Gross Domestic Product (GDP) will decline 0.75% in the second half of the calendar year due to the squeeze on household income from higher energy costs and goods prices. Growth is then expected to continue to fall throughout 2023 and the first half of 2024.
- 1.8 CPI inflation is expected to peak at around 11% in the last calendar quarter of 2022 and then fall sharply to 1.4%, below the 2% target, in two years' time and to 0% in three years' time if Bank Rate follows the path implied by financial markets at the time of the November MPR (a peak of 5.25%). However the BoE stated it considered this path to be too high, suggesting that the peak in interest rates will be lower, reducing the risk of inflation falling too far below target. Market rates have fallen since the time of the November MPR.
- 1.9 The labour market remains tight for now, with the most recent statistics showing the unemployment rate was 3.7%. Earnings were up strongly in nominal terms by 6.1% for both total pay and for regular pay but factoring in inflation means real pay for both measures was -2.7%. Looking forward, the November MPR shows the labour market weakening in response to the deteriorating outlook for growth, leading to the unemployment rate rising to around 6.5% in 2025.
- 1.10 Interest rates have also been rising sharply in the US, with the Federal Reserve increasing the range on its key interest rate by 0.5% in December 2022 to 4.25%-4.5%. This rise follows four successive 0.75% rises in a pace of tightening that has seen rates increase from 0.25%-0.50% in March 2022. Annual inflation has been slowing in the US but remains above 7%. GDP grew at an annualised rate of 3.2% (revised up from 2.9%) between July and September 2022, but with official interest rates expected to rise even further in the coming months, a recession in the region is widely expected at some point during 2023.
- 1.11 Inflation rose consistently in the Euro Zone since the start of the year, hitting a peak annual rate of 10.6% in October 2022, before declining to 10.1% in November. Economic growth has been weakening with an upwardly revised expansion of 0.3% (from 0.2%) in the three months to September 2022. As with the UK and US, the European Central Bank has been on an interest rate tightening cycle, pushing up its three key interest rates by 0.50% in December, following two consecutive 0.75% rises, taking its main refinancing rate to 2.5% and deposit facility rate to 2.0%.
- 1.12 **Credit outlook:** Credit default swap (CDS) prices have generally followed an upward trend throughout 2022, indicating higher credit risk. They have been boosted by the war in Ukraine, increasing economic and political uncertainty and a weaker global

and UK outlook, but remain well below the levels seen at the beginning of the Covid-19 pandemic.

- 1.13 CDS price volatility was higher in 2022 compared to 2021 and the divergence in prices between ringfenced (retail) and non-ringfenced (investment) banking entities has emerged once again.
- 1.14 The weakening economic picture during 2022 led the credit rating agencies to reflect this in their assessment of the outlook for the UK sovereign as well as several local authorities and financial institutions, revising them from to negative from stable.
- 1.15 There are competing tensions in the banking sector which could impact bank balance sheet strength going forward. The weakening economic outlook and likely recessions in many regions increase the possibility of a deterioration in the quality of banks' assets, while higher interest rates provide a boost to net income and profitability.
- 1.16 However, the institutions on our adviser Arlingclose's counterparty list remain well-capitalised and their counterparty advice on both recommended institutions and maximum duration remain under constant review and will continue to reflect economic conditions and the credit outlook.
- 1.17 **Interest rate forecast:** The Council's treasury management adviser Arlingclose forecasts that Bank Rate will continue to rise in 2022 and 2023 as the Bank of England attempts to subdue inflation which is significantly above its 2% target.
- 1.18 While interest rate expectations reduced during October and November 2022, multiple interest rate rises are still expected over the forecast horizon. Arlingclose expects Bank Rate to rise to 4.25% by June 2023 under its central case, with the risks in the near- and medium-term to the upside should inflation not evolve as the Bank forecasts and remains persistently higher.
- 1.19 Yields are expected to remain broadly at current levels over the medium-term, with 5-, 10- and 20-year gilt yields expected to average around 3.6%, 3.7%, and 3.9% respectively over the 3-year period to September 2025. The risks for short, medium and longer-term yields are judged to be broadly balanced over the forecast horizon. As ever, there will undoubtedly be short-term volatility due to economic and political uncertainty and events.
- 1.20 A more detailed economic and interest rate forecast provided by Arlingclose is attached at **Appendix A**.
- 1.21 For the purpose of setting the budget, it has been assumed that new treasury management investments will be made at an average rate of around 2.42%, and that new long-term loans will be borrowed at an average rate of 4.33%.

Local Context

1.22 On 30th November 2022, the Council held £147.0m of borrowing and £33.5m of investments. This is set out in further detail at **Appendix B**. Forecast changes in these sums are shown in the balance sheet analysis in **Table 1** below.

Table 1: Balance sheet summary and forecast

	31/3/22 Actual £m	31/3/23 Estimate £m	31/3/24 Forecast £m	31/3/25 Forecast £m	31/3/26 Forecast £m	31/3/27 Forecast £m
General Fund CFR	16.7	21.3	25.8	32.0	28.2	26.2
HRA CFR	170.7	172.7	181.7	189.3	189.9	190.5
Total CFR	187.4	194.0	207.5	221.3	218.1	216.7
Less: Other debt liabilities *	(0)	(0.3)	(0.2)	(0.7)	(0.5)	(0.3)
Loans CFR	187.4	193.7	207.3	220.6	217.6	216.4
Less: External borrowing **	(147.0)	(146.9)	(150.8)	(157.0)	(156.0)	(155.0)
Internal borrowing	40.4	46.8	56.5	63.6	61.6	61.4
Less: Balance sheet reserves	(77.4)	(67.3)	(68.2)	(73.6)	(71.6)	(71.4)
Investments	37.0	20.5	11.7	10.0	10.0	10.0

* Leases that form part of the Council's total debt.

** shows only loans to which the Council is committed and excludes optional refinancing

1.23 The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while balance sheet resources are the underlying sums available for investment. The Council's current strategy is to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing.

1.24 The Council has an increasing CFR due to commitments within the capital programme and also loans for Northwood Group Ltd and Rykneld Homes Ltd. The forecast level of reserves means that the majority of borrowing throughout this period is likely to be from internal resources.

1.25 CIPFA's Prudential Code for Capital Finance in Local Authorities recommends that the Council's total debt should be lower than its highest forecast CFR over the next three years. Table 1 shows that the Council expects to comply with this recommendation during 2023/24.

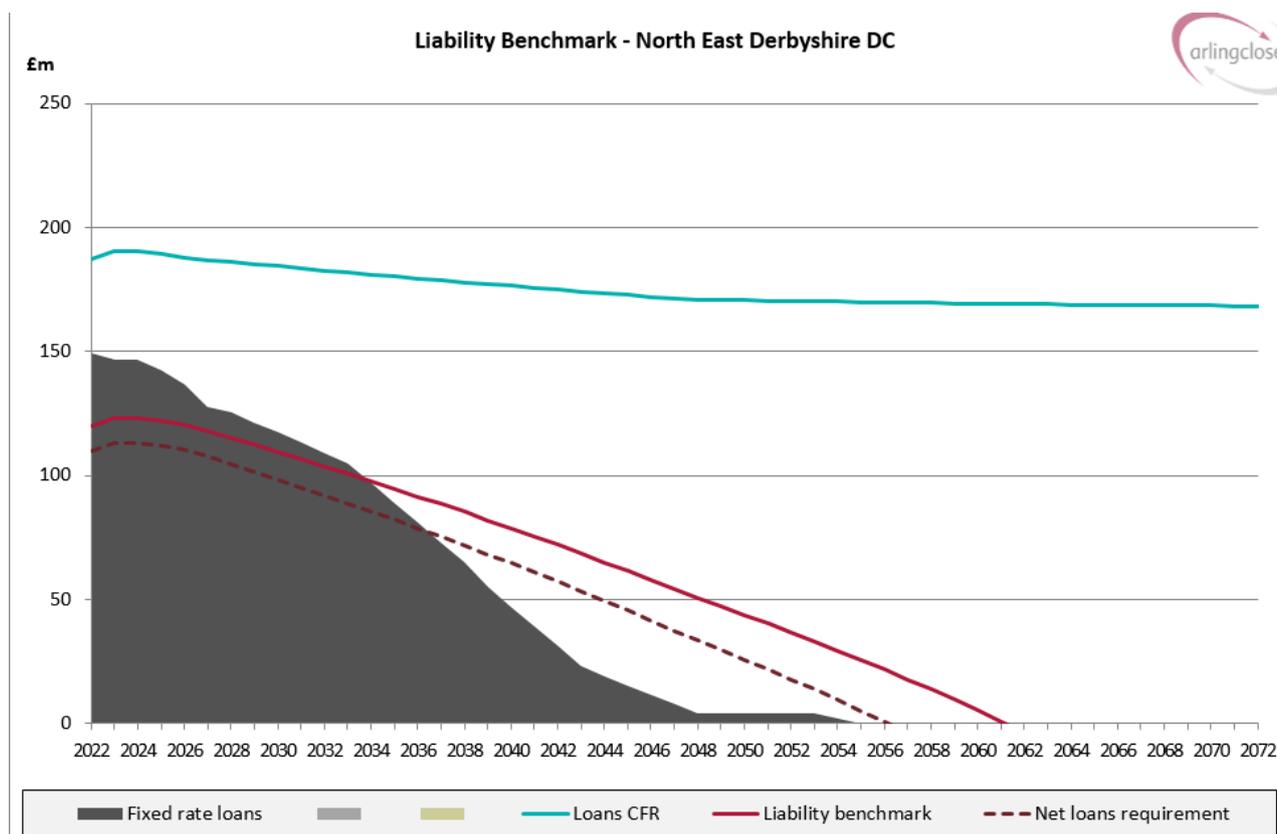
1.26 **Liability benchmark:** To compare the Council's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing. This assumes the same forecasts as **Table 1** above, but that cash and investment balances are kept to a minimum level of £10m at each year-end to maintain sufficient liquidity but minimise credit risk.

1.27 The liability benchmark is an important tool to help establish whether the Council is likely to be a long-term borrower or long-term investor in the future, and so shape its strategic focus and decision making. The liability benchmark itself represents an estimate of the cumulative amount of external borrowing the Council must hold to fund its current capital and revenue plans while keeping treasury investments at the minimum level required to manage day to day cash flow.

Table 2: Prudential Indicator: Liability benchmark

	31/3/22	31/3/23	31/3/24	31/3/25	31/3/26	31/3/27
	Actual	Estimate	Forecast	Forecast	Forecast	Forecast
	£m	£m	£m	£m	£m	£m
CFR	187.4	194.0	207.5	221.3	218.1	216.7
Less: Balance sheet reserves	(77.4)	(67.3)	(68.2)	(73.6)	(71.6)	(71.4)
Net loans requirement	110.0	126.7	139.3	147.7	146.5	145.3
Plus: Liquidity allowance	10.0	10.0	10.0	10.0	10.0	10.0
Liability Benchmark	120.0	136.7	149.3	157.7	156.5	155.3

1.28 Following on from the medium-term forecasts in table 2 above, the long-term liability benchmark assumes capital expenditure funded by borrowing of £36.895m over the term of the report, minimum revenue provision on new capital expenditure based on a 50 year asset life and income, expenditure and reserves all decreasing slightly over the period of the report. This is shown in the chart below together with the maturity profile of the Authority's existing borrowing:



- 1.29 The minimum requirement is to show forecasts for loans CFR, net loans requirement and liability benchmark against actual borrowing for ten years. CIPFA recommends a longer period covering the current debt maturity profile with borrowing split into fixed rate, variable rate and LOBO.
- 1.30 The liability benchmark is a projection of the amount of loan debt outstanding that the Council needs each year into the future to fund its existing debt liabilities, planned prudential borrowing and other cash flows. The liability benchmark identifies the maturities needed for new borrowing in order to match future liabilities. It therefore avoids borrowing for too long or too short. The liability benchmark acts as a mechanism for preventing future over-borrowing. Once the benchmark has been established, new borrowing decisions that take the level of borrowing over the benchmark, or increase any existing over-benchmark positions, should be considered very carefully.
- 1.31 The graph provided above shows how the CFR remains constant at a level of approximately £160m but the fixed rate loans are reducing once they meet their maturity dates. The graph, however, doesn't take account of any potential reborrowing of the current fixed rate loans as they mature.

Borrowing Strategy

- 1.32 The Council currently holds £147.0m of loans, a decrease of £2.2m on the previous year, as part of its strategy for funding previous years' capital programmes. The balance sheet forecast in **Table 1** shows that the Council does not expect to need to borrow in 2023/24. The Council may however, borrow to pre-fund future years'

requirements, providing this does not exceed the authorised limit for borrowing of £217.5m.

- 1.33 **Objectives:** The Council's chief objective when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving certainty of those costs over the period for which funds are required. The flexibility to renegotiate loans should the Council's long-term plans change is a secondary objective.
- 1.34 **Strategy:** 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. With short-term interest rates currently much lower than long-term rates, it is likely to be more cost effective currently to borrow short-term loans or use internal resources.
- 1.35 By doing so, the Council is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of internal borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise modestly. Arlingclose will assist the Council with this 'cost of carry' and breakeven analysis. Its output may determine whether the Council borrows additional sums at long-term fixed rates in 2023/24 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.
- 1.36 The Council has previously raised all of its long-term borrowing from the PWLB but will consider long-term loans from other sources including banks, pensions and local authorities, and will investigate the possibility of issuing bonds and similar instruments, in order to lower interest costs and reduce over-reliance on one source of funding in line with the CIPFA Code. PWLB loans are no longer available to local authorities planning to buy investment assets primarily for yield; the Council intends to avoid this activity in order to retain its access to PWLB loans.
- 1.37 Alternatively, the Council may arrange forward starting loans, where the interest rate is fixed in advance, but the cash is received in later years. This would enable certainty of cost to be achieved without suffering a cost of carry in the intervening period.
- 1.38 In addition, the Council may borrow short-term loans to cover unplanned cash flow shortages.
- 1.39 **Sources of borrowing:** The approved sources of long-term and short-term borrowing are:
- HM Treasury's PWLB lending facility (formerly the Public Works Loan Board)
 - any institution approved for investments (see below)

- any other bank or building society authorised to operate in the UK
- any other UK public sector body
- UK public and private sector pension funds (except Derbyshire County Council Pension Fund)
- capital market bond investors
- UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues

1.40 **Other sources of debt finance:** In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:

- leasing
- hire purchase
- Private Finance Initiative
- sale and leaseback

1.41 **Municipal Bonds Agency:** UK Municipal Bonds Agency plc was established in 2014 by the Local Government Association as an alternative to the PWLB. It issues bonds on the capital markets and lends the proceeds to local authorities. This is a more complicated source of finance than the PWLB for two reasons: borrowing authorities will be required to provide bond investors with a guarantee to refund their investment in the event that the agency is unable to for any reason; and there will be a lead time of several months between committing to borrow and knowing the interest rate payable. Any decision to borrow from the Agency will therefore be the subject of a separate report to Council.

1.42 **LOBOs:** The Council doesn't hold or intend to hold any LOBO (Lender's Option Borrower's Option) loans.

1.43 **Short-term and variable rate loans:** These loans leave the Council exposed to the risk of short-term interest rate rises and are therefore subject to the interest rate exposure limits in the treasury management indicators below. Financial derivatives may be used to manage this interest rate risk (see section below).

1.44 **Debt rescheduling:** The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. Other lenders may also be prepared to negotiate premature redemption terms. The Council may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall cost saving or a reduction in risk. The recent rise in interest rates means that more favourable debt rescheduling opportunities should arise than in previous years.

Treasury Investment Strategy

- 1.45 The Council holds invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Council's treasury investment balance has ranged between £27.0m and £44.0m, however these levels are predicted to decrease due to the works on the replacement of Sharley Park Leisure Centre.
- 1.46 **Objectives:** The CIPFA Code requires the Council to invest its treasury funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.
- 1.47 Where balances are expected to be invested for more than one year, the Council will aim to achieve a total return that is equal or higher than the prevailing rate of inflation, in order to maintain the spending power of the sum invested. The Council aims to be a responsible investor and will consider environmental, social and governance (ESG) issues when investing.
- 1.48 **Strategy:** As demonstrated by the liability benchmark above, the Council expects to be a long-term borrower and new treasury investments will therefore be made primarily to manage day-to-day cash flows using short-term low risk instruments. The existing portfolio of strategic pooled funds will be maintained to diversify risk into different sectors and boost investment income.
- 1.49 The CIPFA Code does not permit local authorities to both borrow and invest long-term for cash flow management. But the Council may make long-term investments for treasury risk management purposes, including to manage interest rate risk by investing sums borrowed in advance for the capital programme for up to three years; to manage inflation risk by investing usable reserves in instruments whose value rises with inflation; and to manage price risk by adding diversification to the strategic pooled fund portfolio.
- 1.50 **ESG policy:** Environmental, social and governance (ESG) considerations are increasingly a factor in global investors' decision making, but the framework for evaluating investment opportunities is still developing and therefore the Council's strategy does not currently include ESG scoring or other real-time ESG criteria at an individual investment level. When investing in banks and funds, the Council will prioritise banks that are signatories to the UN Principles for Responsible Banking and funds operated by managers that are signatories to the UN Principles for Responsible Investment, the Net Zero Asset Managers Alliance and/or the UK Stewardship Code.

- 1.51 **Business models:** Under the new IFRS 9 standard, the accounting for certain investments depends on the Council's "business model" for managing them. The Council 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.
- 1.52 **Approved counterparties:** The Council may invest its surplus funds with any of the counterparty types in **Table 3** below, subject to the cash limits (per counterparty) and the time limits shown.

Table 3: Approved investment counterparties and limits

Sector	Time limit	Counterparty limit	Sector limit
The UK Government	50 years	Unlimited	n/a
Local authorities & other government entities	25 years	£5m	Unlimited
Secured investments *	25 years	£5m	Unlimited
Banks (unsecured) *	13 months	£5m	Unlimited
Building societies (unsecured) *	13 months	£5m	£20m
Registered providers (unsecured) *	5 years	£5m	£20m
Money market funds *	n/a	£5m	Unlimited
Strategic pooled funds	n/a	£5m	£20m
Real estate investment trusts	n/a	£5m	£20m
Other investments *	5 years	£5m	£20m

- 1.53 * **Minimum credit rating:** Treasury investments in the sectors marked with an asterisk will only be made with entities whose lowest published long-term credit rating is no lower than A-. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used. However, investment decisions are never made solely based on credit ratings, and all other relevant factors including external advice will be taken into account.
- 1.54 For entities without published credit ratings, investments may be made either (a) where external advice indicates the entity to be of similar credit quality; or (b) to a maximum of £5m per counterparty as part of a diversified pool e.g. via a peer-to-peer platform.

- 1.55 **Government:** Loans to, and bonds and bills issued or guaranteed by, national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is generally a lower risk of insolvency, although they are not zero risk. Investments with the UK Government are deemed to be zero credit risk due to its ability to create additional currency and therefore may be made in unlimited amounts for up to 50 years.
- 1.56 **Secured Investments:** Investments secured on the borrower's assets, which limits the potential losses in the event of insolvency. The amount and quality of the security will be a key factor in the investment decision. Covered bonds and reverse repurchase agreements with banks and building societies are exempt from bail-in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the higher of the collateral credit rating and the counterparty credit rating will be used. The combined secured and unsecured investments with any one counterparty will not exceed the cash limit for secured investments.
- 1.57 **Banks and building societies (unsecured):** Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail. See below for arrangements relating to operational bank accounts.
- 1.58 **Registered providers (unsecured):** Loans to, and bonds issued or guaranteed by, registered providers of social housing or registered social landlords, formerly known as housing associations. These bodies are regulated by the Regulator of Social Housing (in England), the Scottish Housing Regulator, the Welsh Government and the Department for Communities (in Northern Ireland). As providers of public services, they retain the likelihood of receiving government support if needed.
- 1.59 **Money market funds:** Pooled funds that offer same-day or short notice liquidity and very low or no price volatility by investing in short-term money markets. They have the advantage over bank accounts of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a small fee. Although no sector limit applies to money market funds, the Council will take care to diversify its liquid investments over a variety of providers to ensure access to cash at all times.
- 1.60 **Strategic pooled funds:** Bond, equity and property funds that offer enhanced returns over the longer term but are more volatile in the short term. These allow the Council to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Council's investment objectives will be monitored regularly.

- 1.61 **Real estate investment trusts:** Shares in companies that invest mainly in real estate and pay the majority of their rental income to investors in a similar manner to pooled property funds. As with property funds, REITs offer enhanced returns over the longer term, but are more volatile especially as the share price reflects changing demand for the shares as well as changes in the value of the underlying properties.
- 1.62 **Other investments:** This category covers treasury investments not listed above, for example unsecured corporate bonds and company loans. Non-bank companies cannot be bailed-in but can become insolvent placing the Council's investment at risk.
- 1.63 **Operational bank accounts:** The Council may incur operational exposures, for example through current accounts, collection accounts and merchant acquiring services, to any UK bank with credit ratings no lower than BBB- and with assets greater than £25 billion. These are not classed as investments, but are still subject to the risk of a bank bail-in, and balances will therefore be kept at £5m per bank. The Bank of England has stated that in the event of failure, banks with assets greater than £25 billion are more likely to be bailed-in than made insolvent, increasing the chance of the Council maintaining operational continuity.
- 1.64 **Risk assessment and credit ratings:** Credit ratings are obtained and monitored by the Council's treasury advisers, who will notify changes in ratings as they occur. The credit rating agencies in current use are listed in the Treasury Management Practices document. 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.
- 1.65 Where a credit rating agency announces that a credit rating is on review for possible downgrade (also known as "negative watch") so that it may fall below the approved rating criteria, then only investments that can be withdrawn on the next working day will be made with that organisation until the outcome of the review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.
- 1.66 **Other information on the security of investments:** 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, information on potential government support, reports in the quality financial press and analysis and advice from the Council's treasury management adviser. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may otherwise meet the above criteria.

- 1.67 When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2008 and 2020, this is not generally reflected in credit ratings, but can be seen in other market measures. In these circumstances, the Council will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. 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 the UK Government via the Debt Management Office or invested in government treasury bills for example, or with other local authorities. This may cause investment returns to fall, but will protect the principal sum invested.
- 1.68 **Investment limits:** The Council's revenue reserves available to cover investment losses are forecast to be £25.2 million on 31st March 2023 and £23.6 million on 31st March 2024. In order that no more than 19.8% of available reserves will be put at risk in the case of a single default, the maximum that will be lent to any one organisation (other than the UK Government) will be £5 million. A group of entities under the same ownership will be treated as a single organisation for limit purposes.
- 1.69 Credit risk exposures arising from non-treasury investments, financial derivatives and balances greater than £5 million in operational bank accounts count against the relevant investment limits.
- 1.70 Limits are also placed on fund managers, investments in brokers' nominee accounts and foreign countries as below. Investments in pooled funds and multilateral development banks do not count against the limit for any single foreign country, since the risk is diversified over many countries.

Table 4: Additional Investment limits

	Cash limit
Any group of pooled funds under the same management	£5m per manager
Negotiable instruments held in a broker's nominee account	£5m per broker
Foreign countries	£5m per country

- 1.71 **Liquidity management:** The Council uses its own cash flow forecasting techniques to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a prudent basis to minimise the risk of the Council being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Council's medium-term financial plan and cash flow forecast.

- 1.72 The Council will spread its liquid cash over a number of providers (e.g. bank accounts and money market funds) to ensure that access to cash is maintained in the event of operational difficulties at any one provider.

Treasury Management Prudential Indicators

- 1.73 The Council measures and manages its exposures to treasury management risks using the following indicators:

- 1.74 **Security:** The Council has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average credit rating of its investment portfolio. This is calculated by applying a score to each investment (AAA=1, AA+=2, etc.) and taking the arithmetic average, weighted by the size of each investment. Unrated investments are assigned a score based on their perceived risk.

Credit risk indicator	
Portfolio average credit rating	Target <3.0
Current portfolio average credit rating on investments	Actual 1.36

- 1.75 **Liquidity:** The Council has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments within a rolling three month period, without additional borrowing.

Liquidity risk indicator	Amount available
Total cash available within 3 months	£29.5m

- 1.76 **Interest rate exposures:** This indicator is set to control the Council's exposure to interest rate risk. The upper limits on the one-year revenue impact of a 1% rise or fall in interest rates will be:

Interest rate risk indicator	Limit each year
Upper limit on one-year revenue impact of a 1% <u>rise</u> in interest rates	£1.5m
Upper limit on one-year revenue impact of a 1% <u>fall</u> in interest rates	(£1.5m)

- 1.77 The impact of a change in interest rates is calculated on the assumption that maturing loans and investments will be replaced at new market rates.

- 1.78 **Maturity structure of borrowing:** This indicator is set to control the Council's exposure to refinancing risk. The upper and lower limits on the maturity structure of borrowing will be:

Refinancing rate risk indicator	Upper limit	Lower limit
Under 12 months	20%	0%
12 months and within 24 months	20%	0%
24 months and within 5 years	40%	0%
5 years and within 10 years	40%	0%
10 years and above	90%	0%

1.79 Time periods start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment.

1.80 **Long-term treasury management investments:** 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 prudential limits on the long-term treasury management investments will be:

Price risk indicator	2022/23	2023/24	2024/25	No fixed date
Limit on principal invested beyond year end	£20m	£20m	£20m	£20m

Related Matters

1.81 The CIPFA Code requires the Council to include the following in its treasury management strategy.

1.82 **Financial Derivatives:** Local authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk (e.g. interest rate collars and forward deals) and to reduce costs or increase income at the expense of greater risk (e.g. LOBO loans and callable deposits). The general power of competence in Section 1 of the *Localism Act 2011* removes much of the uncertainty over local authorities' use of standalone financial derivatives (i.e. those that are not embedded into a loan or investment).

1.83 The Council will only use standalone financial derivatives (such as swaps, forwards, futures and options) where they can be clearly demonstrated to reduce the overall level of the financial risks that the Council is exposed to. Additional risks presented, such as credit exposure to derivative counterparties, will be taken into account when determining the overall level of risk. Embedded derivatives, including those present in pooled funds and forward starting transactions, will not be subject to this policy, although the risks they present will be managed in line with the overall treasury risk management strategy.

1.84 Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria, assessed using the appropriate credit rating for

derivative exposures. An allowance for credit risk calculated using the methodology in the Treasury Management Practices document will count against the counterparty credit limit and the relevant foreign country limit.

- 1.85 In line with the CIPFA code, the Council will seek external advice and will consider that advice before entering into financial derivatives to ensure that it fully understands the implications.
- 1.86 **Markets in Financial Instruments Directive:** The Council has opted up to professional client status 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 Council's treasury management activities, the Chief Financial Officer believes this to be the most appropriate status.
- 1.87 **Financial Implications:** The General Fund budget for investment income in 2023/24 is £0.120m with the HRA budget for investment income in 2023/24 being £0.220m, based on an average investment portfolio of £22.8m at an average interest rate of 1.49%. The General Fund budget for debt interest paid in 2023/24 is £0.366m with the HRA budget for debt interest paid in 2023/24 being £4.864m, based on an average debt portfolio of £147.0m at an average interest rate of 3.60%. If actual levels of investments and borrowing, or actual interest rates, differ from those forecast, performance against budget will be correspondingly different.

Other Options Considered

- 1.88 The CIPFA Code does not prescribe any particular treasury management strategy for local authorities to adopt. The Chief Financial Officer, having consulted the Cabinet Member for Finance, believes that the above strategy represents an appropriate balance between risk management and cost effectiveness. Some alternative strategies, with their financial and risk management implications, are listed below.

Alternative	Impact on income and expenditure	Impact on risk management
Invest in a narrower range of counterparties and/or for shorter times	Interest income will be lower	Lower chance of losses from credit related defaults, but any such losses may be greater
Invest in a wider range of counterparties and/or for longer times	Interest income will be higher	Increased risk of losses from credit related defaults, but any such losses may be smaller

Borrow additional sums at long-term fixed interest rates	Debt interest costs will rise; this is unlikely to be offset by higher investment income	Higher investment balance leading to a higher impact in the event of a default; however long-term interest costs may be more certain
Borrow short-term or variable loans instead of long-term fixed rates	Debt interest costs will initially be lower	Increases in debt interest costs will be broadly offset by rising investment income in the medium term, but long-term costs may be less certain
Reduce level of borrowing	Saving on debt interest is likely to exceed lost investment income	Reduced investment balance leading to a lower impact in the event of a default; however long-term interest costs may be less certain

Appendix A

Arlingclose Economic & Interest Rate Forecast (November 2022)

Underlying assumptions:

- The influence of the mini-budget on rates and yields continues to wane following the more responsible approach shown by the new incumbents of Downing Street.
- Volatility in global markets continues, however, as investors seek the extent to which central banks are willing to tighten policy, as evidence of recessionary conditions builds. Investors have been more willing to price in the downturn in growth, easing financial conditions, to the displeasure of policymakers. This raises the risk that central banks will incur a policy error by tightening too much.
- The UK economy is already experiencing recessionary conditions and recent GDP and PMI data suggests the economy entered a technical recession in Q3 2022. The resilience shown by the economy has been surprising, despite the downturn in business activity and household spending. Lower demand should bear down on business pricing power – recent data suggests the UK has passed peak inflation.
- The lagged effect of the sharp tightening of monetary policy, and the lingering effects of the mini-budget on the housing market, widespread strike action, alongside high inflation, will continue to put pressure on household disposable income and wealth. The short- to medium-term outlook for the UK economy remains bleak.
- Demand for labour appears to be ebbing, but not quickly enough in the official data for most MPC policymakers. The labour market remains the bright spot in the economy and persisting employment strength may support activity, although there is a feeling of borrowed time. The MPC focus is on nominal wage growth, despite the huge real term pay cuts being experienced by the vast majority. Bank Rate will remain relatively high(er) until both inflation and wage growth declines.
- Global bond yields remain volatile as investors price in recessions even as central bankers push back on expectations for rate cuts in 2023. The US labour market remains tight and the Fed wants to see persistently higher policy rates, but the lagged effects of past hikes will depress activity more significantly to test the Fed's resolve.
- While the BoE appears to be somewhat more dovish given the weak outlook for the UK economy, the ECB seems to harbour (worryingly) few doubts about the short term direction of policy. Gilt yields will be broadly supported by both significant new bond supply and global rates expectations due to hawkish central bankers, offsetting the effects of declining inflation and growth.

Forecast:

- The MPC raised Bank Rate by 50bps to 3.5% in December as expected, with signs that some members believe that 3% is restrictive enough. However, a majority of members think further increases in Bank Rate might be required. Arlingclose continues to expect Bank Rate to peak at 4.25%, with further 25bps rises February, March and May 2023.
- The MPC will cut rates in the medium term to stimulate a stuttering UK economy, but will be reluctant to do so until wage growth eases. We see rate cuts in the first half of 2024.
- Arlingclose expects gilt yields to remain broadly steady over the medium term, although with continued volatility across shorter time periods.
- Gilt yields face pressures to both sides from hawkish US/EZ central bank policy on one hand to the weak global economic outlook on the other. BoE bond sales and high government borrowing will provide further underlying support for yields.

	Current	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25
Official Bank Rate													
Upside risk	0.00	0.50	0.75	1.00	1.00	1.00	1.25	1.50	1.75	1.50	1.25	1.25	1.25
Arlingclose Central Case	3.50	4.00	4.25	4.25	4.25	4.25	4.00	3.75	3.50	3.25	3.25	3.25	3.25
Downside risk	0.00	0.50	0.75	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.00	1.00
3-month money market rate													
Upside risk	0.00	0.50	0.75	1.00	1.00	1.00	1.25	1.50	1.75	1.50	1.25	1.25	1.25
Arlingclose Central Case	3.00	4.40	4.40	4.40	4.35	4.30	4.25	4.00	3.75	3.50	3.40	3.40	3.40
Downside risk	0.00	0.50	0.75	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.00	1.00
5yr gilt yield													
Upside risk	0.00	0.70	0.80	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Arlingclose Central Case	3.43	3.60	3.80	3.80	3.80	3.70	3.60	3.50	3.40	3.30	3.30	3.30	3.30
Downside risk	0.00	0.80	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
10yr gilt yield													
Upside risk	0.00	0.70	0.80	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Arlingclose Central Case	3.47	3.50	3.60	3.60	3.60	3.60	3.50	3.50	3.50	3.50	3.50	3.50	3.50
Downside risk	0.00	0.80	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
20yr gilt yield													
Upside risk	0.00	0.70	0.80	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Arlingclose Central Case	3.86	3.85	3.85	3.85	3.85	3.85	3.85	3.85	3.85	3.85	3.85	3.85	3.85
Downside risk	0.00	0.80	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
50yr gilt yield													
Upside risk	0.00	0.70	0.80	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Arlingclose Central Case	3.46	3.60	3.60	3.60	3.60	3.60	3.60	3.60	3.60	3.60	3.60	3.60	3.60
Downside risk	0.00	0.80	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00

PWLB Standard Rate (Maturity Loans) = Gilt yield + 1.00%

PWLB Certainty Rate (Maturity Loans) = Gilt yield + 0.80%

UKIB Rate (Maturity Loans) = Gilt yield + 0.60%

Appendix B**Existing Investment & Debt Portfolio Position**

	30/11/22 Actual Portfolio £m	30/11/22 Average Rate %
External borrowing:		
Public Works Loan Board	147.0	3.53
Total external borrowing	147.0	3.53
Total other long-term liabilities:	0	0
Total gross external debt	147.0	3.53
Treasury investments:		
The UK Government	0.0	0.00
Local authorities	10.0	1.13
Banks (unsecured)	0.0	0.00
Money Market Funds	23.5	3.11
Total treasury investments	33.5	4.24
Net debt	113.5	



North East Derbyshire District Council

Capital Strategy 2023/24 – 2026/27

Introduction

- 1.1 This capital strategy report, gives a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of local public services along with an overview of how associated risk is managed and the implications for future financial sustainability.
- 1.2 Decisions made this year on capital and treasury management will have financial consequences for the Council for many years into the future. They are therefore subject to both a national regulatory framework and to a local policy framework, summarised in this report.

Capital Expenditure and Financing

- 1.3 Capital expenditure 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 loans and grants to other bodies enabling them to buy assets. The Council has some limited discretion on what counts as capital expenditure, for example assets costing below £10,000 are not capitalised and are charged to revenue in year.

In 2023/24, the Council is planning capital expenditure of £48.4m as summarised below:

Table 1: Prudential Indicator: Estimates of Capital Expenditure

	2021/22 Actual £m	2022/23 Forecast £m	2023/24 Budget £m	2024/25 Budget £m	2025/26 Budget £m	2026/27 Budget £m
General Fund Services	5.4	17.0	18.5	19.8	5.1	1.7
Council Housing (HRA)	20.7	22.0	29.9	28.1	12.3	12.3
TOTAL	26.1	39.0	48.4	47.9	17.4	14.0

- 1.4 The main General Fund capital projects include replacement vehicles, asset refurbishment, ICT replacement, disabled facilities grant funded adaptations, Clay Cross Towns Fund programme and rebuilding of Sharley Park Leisure Centre. Following a change in the Prudential Code, the Council no longer incurs capital expenditure on investments.
- 1.5 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. The main HRA capital projects involve refurbishment of dwellings, North Wingfield new build project, stock purchase programme and improvement works to the energy efficiency of the Council's non-traditional housing stock.
- 1.7 **Governance:** Projects are included in the capital programme as part of the annual budget review or through ad hoc approval during the year. The capital programme is refreshed each year and the new requirements are presented to Cabinet and Council annually. Full details of the Council's Capital Programme can be seen at **Appendix A** to this report.
- 1.8 All capital expenditure must be financed, either from external sources (government grants and other contributions), the Council's own resources (revenue, reserves and capital receipts) or debt (borrowing and leasing). The planned financing of the above expenditure is as follows:

Table 2: Financing of Capital Programme (Appendix A)

	2021/22 Actual £m	2022/23 Forecast £m	2023/24 Budget £m	2024/25 Budget £m	2025/26 Budget £m	2026/27 Budget £m
External Sources	4.9	11.0	12.3	11.4	4.0	0.8
Capital Receipts	1.2	5.7	4.2	3.9	1.5	1.3
Own Resources	17.4	18.8	16.2	16.2	11.3	11.3
Debt	2.6	3.5	15.7	16.4	0.6	0.6
TOTAL	26.1	39.0	48.4	47.9	17.4	14.0

- 1.9 Debt 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 repay and/or replace debt finance. Planned MRP and use of capital receipts are as follows:

Table 3: Replacement of debt finance

	2021/22 Actual £m	2022/23 Forecast £m	2023/24 Budget £m	2024/25 Budget £m	2025/26 Budget £m	2026/27 Budget £m
Capital Resources	1.3	0	0	0	0	0
Minimum Revenue Provision (MRP)	0.6	0.1	0.2	0.3	0.7	0.7
Total	1.9	0.1	0.2	0.3	0.7	0.7

The Council's full minimum revenue provision statement is **Appendix B** to this report.

- 1.10 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 expected to increase by £13.5m during 2023/24. 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

	31/3/2022 Actual £m	31/3/2023 Forecast £m	31/3/2024 Budget £m	31/3/2025* Budget £m	31/3/2026 Budget £m	31/3/2027 Budget £m
General Fund Services	16.7	21.3	25.8	32.0	28.2	26.2
Council Housing (HRA)	170.7	172.7	181.7	189.3	189.9	190.5
TOTAL CFR	187.4	194.0	207.5	221.3	218.1	216.7

*£0.7m of the CFR increase in 2024/25 arises from a change in the accounting for leases.

- 1.11 **Asset management:** The Council's assets require regular maintenance to ensure they remain safe and fit for purpose. It is also important for income generation that assets remain in a good condition and so remain lettable. A planned approach yields savings in running costs and energy efficiency benefits over time as works are completed and asset conditions improve.
- 1.12 **Asset disposals:** When a capital asset is no longer needed, it may be sold so that the proceeds, known as capital receipts, can be spent on new assets or to repay debt.

The Council is currently also permitted to spend capital receipts “flexibly” on approved service reform projects until 2023/24 under the flexible use of capital receipts strategy. Repayments of capital grants, loans and investments also generate capital receipts. The Council plans to receive £5.8m of capital receipts in the coming financial year as follows:

Table 5: Capital receipts receivable

	2021/22 Actual £m	2022/23 Forecast £m	2023/24 Budget £m	2024/25 Budget £m	2025/26 Budget £m	2026/27 Budget £m
Asset Sales	5.18	4.92	5.80	4.70	4.20	4.20
Loans Repaid	0	0	0	0	0	0
TOTAL	5.18	4.92	5.80	4.70	4.20	4.20

Treasury Management

- 1.13 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.
- 1.14 Due to decisions taken in the past, the Council currently has £147.0m borrowing at an average interest rate of 3.53% and £33.5m treasury investments at an average rate of 2.42%.
- 1.15 **Borrowing strategy:** 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 seeks to strike a balance between cheap short-term loans (currently available at around 3.5%) and long-term fixed rate loans where the future cost is known but higher (currently 4.09%-4.57%).
- 1.16 The Council does not borrow to invest for the primary purpose of financial return and therefore retains full access to the Public Works Loans Board.
- 1.17 Projected levels of the Council’s total outstanding debt (which comprises borrowing and leases) are shown below, compared with the capital financing requirement (see above):

Table 6: Prudential Indicator: Gross Debt and the Capital Financing Requirement

	31/3/2022 Actual £m	31/3/2023 Forecast £m	31/3/2024 Budget £m	31/3/2025 Budget £m	31/3/2026 Budget £m	31/3/2027 Budget £m
Debt (incl. leases)	147.0	147.2	151.0	157.7	156.5	155.3
Capital Financing Requirement	187.4	194.0	207.5	221.3	218.1	216.7

1.18 Statutory guidance states 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 in the medium term.

1.19 **Liability benchmark:** To compare the Council's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing:

Table 7: Borrowing and the Liability Benchmark

	31/3/2022 Actual £m	31/3/2023 Forecast £m	31/3/2024 Budget £m	31/3/2025 Budget £m	31/3/2026 Budget £m	31/3/2027 Budget £m
Outstanding Borrowing	147.0	146.9	150.8	157.0	156.0	155.0
Liability Benchmark	120.0	136.7	149.3	157.7	156.5	155.3

1.20 The table above shows that the Council expects to remain borrowed above its liability benchmark in the short term but slightly below in the longer term. This is because a deliberate decision has been made to borrow additional sums for the rebuilding of Sharley Park Leisure Centre.

1.21 **Affordable borrowing limit:** The Council is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt) each year and to keep it under review. In line with statutory guidance, a lower "operational boundary" is also set as a warning level should debt approach the limit.

Table 8: Prudential Indicators: Authorised limit and operational boundary for external debt

	2022/23 limit £m	2023/24 limit £m	2024/25 limit £m	2025/26 limit £m	2026/27 limit £m
Authorised Limit – Borrowing	203.7	217.3	230.6	227.6	226.4
Authorised Limit – Leases	0.3	0.2	0.7	0.5	0.3
Authorised Limit – Total External Debt	204.0	217.5	231.3	228.1	226.7
Operational Boundary – Borrowing	198.7	212.3	225.6	222.6	221.4
Operational Boundary – Leases	0.3	0.2	0.7	0.5	0.3
Operational Boundary – Total External Debt	199.0	212.5	226.3	223.1	221.7

1.22 **Treasury 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.

1.23 The Council's policy on treasury investments is to prioritise security and liquidity over yield, which 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 near-term and longer-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 9: Treasury Management investments

	31/3/2022 Actual £m	31/3/2023 Forecast £m	31/3/2024 Budget £m	31/3/2025 Budget £m	31/3/2026 Budget £m	31/3/2027 Budget £m
Near-Term Investments	37.0	20.5	11.7	10.0	10.0	10.0
Longer-Term Investments	0	0	0	0	0	0
TOTAL	37.0	20.5	11.7	10.0	10.0	10.0

1.24 **Risk management:** The effective management and control of risk are prime objectives of the Council's treasury management activities. The treasury management strategy therefore sets out various indicators and limits to constrain the

risk of unexpected losses and details the extent to which financial derivatives may be used to manage treasury risks.

- 1.25 **Governance:** Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Chief Finance Officer and staff, who must act in line with the treasury management strategy approved by Council. Quarterly reports on treasury management activity are presented to the Audit and Corporate Governance Scrutiny Committee who are responsible for scrutinising treasury management decisions. Six monthly updates are provided for Council.

Investments for Service Purposes

- 1.26 The Council can make investments to assist local public services, including making loans to local service providers and businesses to promote economic growth.
- 1.27 **Risk Management:** 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 at least break even after all costs. The risk of incurring unexpected losses is managed by the use of estimated credit losses. Provisions for expected credit losses are made to ensure that the Council can finance any sums due to the Council which are deemed to be irrecoverable after all recovery measures have been exhausted. A limit of £14.5m is placed on total investments for service purposes to ensure that plausible losses could be absorbed in budgets or reserves without unmanageable detriment to local services. This includes loans to the Rykneld Homes Ltd to allow development of social housing. Rykneld Homes Ltd is a wholly owned subsidiary of the Council, limited by guarantee.
- 1.28 **Governance:** Decisions on service investments are made by the relevant service manager and submitted to Cabinet then Council in consultation with the Chief Finance Officer and must meet the criteria and limits laid down in the Investment Strategy. Most loans and shares are capital expenditure and purchases will therefore also be approved as part of the capital programme. The relevant service director is responsible for ensuring that adequate due diligence is carried out before investment is made.

Commercial Activities

- 1.29 With central government financial support for local public services declining, the Council has invested in developing residential property through Northwood Group Ltd. Currently, an investment of £7.813m has been made into Northwood Group Ltd and further future investment of £0.850m is approved to provide a total investment of £8.663m.
- 1.30 The Council has investment properties generating between £0.449m and £0.474m in net income a year after all costs, before exposing it to normal commercial risks. These

risks are managed by maintaining the properties in good order and advertising vacant properties as soon as possible over a wide area to generate interest in letting the vacant properties.

- 1.31 **Risk Management:** With financial return being the main objective, the Council accepts higher risk on commercial investment than with treasury investments. The principal risk exposures include build cost estimates, sales values estimates and demand. These risks are mitigated by working with experienced builders and professionals who have knowledge of the local market. In order that commercial investments remain proportionate to the size of the Council, and to ensure that plausible losses could be absorbed in budgets or reserves without unmanageable detriment to local services. Contingency plans are in place should expected yields not materialise.
- 1.32 **Governance:** Decisions on commercial investments are made by Council in line with the criteria and limits approved in the Investment Strategy. Property and most other commercial investments are also capital expenditure and purchases will therefore also be approved as part of the capital programme. The Chief Financial Officer is responsible for ensuring that adequate due diligence is carried out before investment is made.

Table 10 – Prudential Indicator: Net income from commercials & service investments to net revenue scheme.

	2021/22 Actual £m	2022/23 Forecast £m	2023/24 Budget £m	2024/25 Budget £m	2025/26 Budget £m	2026/27 Budget £m
Net income from commercial investments	0.474	0.458	0.450	0.451	0.450	0.449
Net income from service investments	0.440	0.624	0.614	0.493	0.343	0.259
Total net income from service and commercial investments	0.914	1.082	1.064	0.944	0.793	0.708
Proportion of net revenue stream	5.85%	6.79%	6.30%	5.86%	5.67%	5.04%
Proportion of usable revenue reserves	3.49%	4.30%	4.50%	4.09%	3.85%	3.93%

Liabilities

- 1.33 In addition to debt of £147.0m detailed above, the Council is committed to making future payments to cover its net pension fund deficit (valued at £42.8m). It has also set aside £1.0m to cover risks of business rates appeals and £1.1m to cover risks of water claims.
- 1.34 **Governance:** Decisions on incurring new discretionary liabilities are taken to Council for approval. The risk of liabilities occurring and requiring payment are monitored as part of the year-end process.

Revenue Budget Implications

- 1.35 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 11: Prudential Indicator: Proportion of financing costs to net revenue stream

	2021/22 Actual £m	2022/23 Forecast £m	2023/24 Budget £m	2024/25 Budget £m	2025/26 Budget £m	2026/27 Budget £m
Financing Costs	0.5	(0.3)	(0.2)	(0.1)	0.4	0.5
Proportion of Net Revenue Stream	3.30%	(1.58%)	(1.33%)	(0.52%)	2.75%	3.37%

1.36 **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 Chief Finance Officer is satisfied that the proposed capital programme is prudent, affordable and sustainable.

Knowledge and Skills

1.37 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.

1.38 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.

1.39 Members receive individual training and development through the Member Development Programme and are periodically required to attend seminars held by the external treasury management advisers.

Treasury Management Operations

1.40 As mentioned above the Council uses external treasury management advisers. The company provides a range of services which include:

- Technical support on treasury matters, capital finance issues and the drafting of Member reports;
- Economic and interest rate analysis;
- Debt services which includes advice on the timing of borrowing;
- Debt rescheduling advice surrounding the existing portfolio;
- Generic investment advice on interest rates, timing and investment instruments;

- A number of places at training events offered on a regular basis.
 - Credit ratings/market information service comprising the three main credit rating agencies;
 -
- 1.41 Whilst the advisers provide support to the internal treasury function, under current market rules and the CIPFA Code of Practice the final decision on treasury matters remains with the Council. This service is subject to regular review. It should be noted that the Council has Arlingclose Ltd as external treasury management advisors, for a period of up to 3 years commencing October 2022.

Banking Contract

- 1.42 The contract with the Councils banking provider Lloyds Bank was extended on the 10th February 2022 for a period of up to 7 years.

Business Continuity Arrangements

- 1.43 As part of the Councils business continuity arrangements officers have sought to set up and provide alternative banking arrangements for the Council should they be required at short notice. These arrangements effectively mean a separate bank account is in place with the required security controls and appropriate officer access to undertake transactions. This account is with Barclays Bank and will only be utilised should a business continuity need or similar issue arise. Officers will continue to review this arrangement.

Appendix A

Capital Programme 2022-2027

Capital Expenditure	Revised Budget 2022/23 £	Original Budget 2023/24 £	Original Budget 2024/25 £	Original Budget 2025/26 £	Original Budget 2026/27 £
Housing Revenue Account					
HRA Capital Works	12,272,000	11,485,100	11,485,100	10,441,000	10,441,000
HRA Capital Works - Non Traditional Properties	4,600,000	9,743,000	9,743,000	500,000	500,000
Green Homes EWI - Mickley	333,000	0	0	0	0
Pine View, Danesmoor	832,000	0	0	0	0
Stock Purchase Programme (1-4-1)	2,500,000	1,000,000	1,000,000	1,000,000	1,000,000
Acquisitions and Disposals (RHL)	500,000	0	0	0	0
North Wingfield New Build Project	215,000	7,325,000	5,555,000	0	0
Garage Demolitions	60,000	23,000	23,000	23,000	23,000
Concrete Balconies	111,000	0	0	0	0
Parking Solutions	573,000	288,000	288,000	288,000	288,000
HRA - Capital Expenditure	21,996,000	29,864,100	28,094,100	12,252,000	12,252,000
General Fund					
Private Sector Housing Grants (DFG's)	820,000	820,000	820,000	820,000	820,000
ICT Schemes	460,000	198,500	108,000	100,000	129,000
Clay Cross Football Pitch	9,000	0	0	0	0
Asset Refurbishment - General	609,000	500,000	500,000	500,000	500,000
Asset Refurbishment - Eckington Depot	732,000	0	0	0	0
Roller Shutter Doors	86,000	0	0	0	0
Eckington Pool Carbon Efficiencies Programme	266,000	0	0	0	0
Dronfield Sports Centre Carbon Efficiencies Programme	1,680,000	0	0	0	0
Replacement of Vehicles	2,292,500	2,210,000	1,914,500	484,000	260,000
Wingerworth Lido	150,000	0	0	0	0
Contaminated Land	42,000	0	0	0	0
Killamarsh Leisure Centre	1,060,000	0	0	0	0
Sharley Park 3G pitch	0	0	1,000,000	0	0
CX Town Market Street Regeneration	0	1,999,000	2,000,000	0	0
CX Town Bridge Street Regeneration	0	0	2,500,000	2,500,000	0
CX Town Clay Cross Creative (inc LC Energy Network)	150,000	850,000	0	0	0
CX Town Clay Cross Skills and Enterprise Hub	0	1,500,000	500,000	0	0
CX Town Sharley Park Active Community Hub	7,145,000	8,100,000	8,605,000	0	0
CX Town Clay Cross Connections	0	1,500,000	1,000,000	500,000	0
CX Town Low Carbon Housing Challenge Fund	650,000	650,000	650,000	0	0
CX Town Rail Station Feasibility	150,000	0	0	0	0
CX Town Programme Management	415,000	241,000	241,000	241,000	0
CX Acc Fund Old Constabulary	0	0	0	0	0
CX Acc Fund School Demolition	158,000	0	0	0	0
CX Acc Fund CX Depot Demolition	86,000	0	0	0	0
CX Acc Fund Public Art Work	32,000	0	0	0	0
CX Acc Fund Land Assembly	3,000	0	0	0	0
CX Acc Fund Other	2,000	0	0	0	0
General Fund Capital Expenditure	16,997,500	18,568,500	19,838,500	5,145,000	1,709,000
Total Capital Expenditure	38,993,500	48,432,600	47,932,600	17,397,000	13,961,000

Capital Financing	2022/23	2023/24	2024/25	2025/26	2026/27
Housing Revenue Account					
Major Repairs Reserve	(17,125,000)	(15,855,100)	(15,855,100)	(10,941,000)	(10,941,000)
Prudential Borrowing - HRA	(2,015,000)	(8,973,000)	(7,593,000)	(600,000)	(600,000)
Development Reserve	(1,596,000)	(311,000)	(311,000)	(311,000)	(311,000)
Grants	0	(3,395,000)	(3,005,000)	0	0
1-4-1 Receipts	(1,260,000)	(1,330,000)	(1,330,000)	(400,000)	(400,000)
HRA Capital Financing	(21,996,000)	(29,864,100)	(28,094,100)	(12,252,000)	(12,252,000)
General Fund					
Disabled Facilities Grant	(820,000)	(820,000)	(820,000)	(820,000)	(820,000)
External Grant - Lottery Funded Schemes	(9,000)	0	0	0	0
External Grant - Contaminated Land	(42,000)	0	0	0	0
External Grant - Clay Cross Towns Fund	(8,791,000)	(6,595,000)	(6,891,000)	(3,241,000)	0
External Grant - Sharley Park Rebuild (Sport E)	0	(1,500,000)	0	0	0
External Grant - Dronfield Sports Centre Carbon Efficiencies	(1,347,000)	0	0	0	0
External Grant - Sharley Park 3G pitch	0	0	(750,000)	0	0
Prudential Borrowing - Eckington Depot	(454,000)	0	0	0	0
Prudential Borrowing - Killamarsh Leisure Centre	(1,060,000)	0	0	0	0
Prudential Borrowing - Sharley Park Leisure Centre	0	(6,745,000)	(8,605,000)	0	0
Prudential Borrowing - Sharley Park Leisure Centre 3G pitch	0	0	(250,000)	0	0
RCCO - Roller Shutter Doors	(86,000)	0	0	0	0
Useable Capital Receipts	(4,388,500)	(2,908,500)	(2,522,500)	(1,084,000)	(889,000)
General Fund Capital Financing	(16,997,500)	(18,568,500)	(19,838,500)	(5,145,000)	(1,709,000)
HRA Development Reserve					
Opening Balance	(2,551,185)	(955,185)	(1,197,015)	(1,337,851)	(1,478,686)
Amount due in year	0	(552,830)	(451,836)	(451,835)	(441,780)
Amount used in year	1,596,000	311,000	311,000	311,000	311,000
Closing Balance	(955,185)	(1,197,015)	(1,337,851)	(1,478,686)	(1,609,466)
Major Repairs Reserve					
Opening Balance	(2,238,257)	(536,757)	(536,757)	(536,757)	(536,757)
Amount due in year	(15,423,500)	(15,855,100)	(15,855,100)	(10,941,000)	(10,941,000)
Amount used in year	17,125,000	15,855,100	15,855,100	10,941,000	10,941,000
Closing Balance	(536,757)	(536,757)	(536,757)	(536,757)	(536,757)
Capital Receipts Reserve					
Opening Balance	(2,340,168)	(51,668)	(143,168)	(120,668)	(1,036,668)
Income expected in year	(3,100,000)	(4,000,000)	(3,500,000)	(3,000,000)	(3,000,000)
Allowable Debt/Pooling Expenses	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000
Amount used in year	4,388,500	2,908,500	2,522,500	1,084,000	889,000
Closing Balance	(51,668)	(143,168)	(120,668)	(1,036,668)	(2,147,668)
Capital Receipts Reserve 1-4-1 receipts					
Opening Balance	(762,969)	(1,322,969)	(1,792,969)	(1,662,969)	(1,662,969)
Income expected in year	(1,820,000)	(1,800,000)	(1,200,000)	(1,200,000)	(1,200,000)
Amount used in year	1,260,000	1,330,000	1,330,000	400,000	400,000
Closing Balance	(1,322,969)	(1,792,969)	(1,662,969)	(2,462,969)	(2,462,969)
Total Capital Financing	(38,993,500)	(48,432,600)	(47,932,600)	(17,397,000)	(13,961,000)

Appendix B

Annual Minimum Revenue Provision Statement 2023/24

Where the Council finances General Fund 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 since 2008. The Local Government Act 2003 requires the Authority to have regard to the former Ministry of Housing, Communities and Local Government's *Guidance on Minimum Revenue Provision* (the MHCLG Guidance) most recently issued in 2018.

The broad aim of the MHCLG Guidance is to ensure that capital expenditure is financed 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 Government, Revenue Support Grant, reasonably commensurate with the period implicit in the determination of that grant.

The MHCLG Guidance requires the Council, to approve an Annual MRP Statement each year, and includes recommendations for calculating a prudent amount of MRP. In line with this guidance the Council has adopted the following approach:

- For capital expenditure incurred after 31st March 2008, MRP will be determined by charging the expenditure over the expected useful life of the relevant asset in equal instalments, starting in the year after the asset becomes operational. MRP on purchases of freehold land will be charged over 50 years. MRP on expenditure not related to fixed assets but which has been capitalised by regulation or direction will be charged over 20 years.
- For assets acquired by leases, MRP will be determined as being equal to the element of the rent or charge that goes to write down the balance sheet liability.
- Where former operating leases have been brought onto the balance sheet due to the adoption of the *IFRS 16 Leases* accounting standard, and the asset values have been adjusted for accruals, prepayments, premiums and/or incentives, then the annual MRP charges will be adjusted so that the total charge to revenue remains unaffected by the new standard.
- For capital expenditure loans to third parties that are repaid in annual or more frequent instalments of principal, the Council will make nil MRP, but will instead apply the capital receipts arising from principal repayments to reduce the capital financing requirement instead. In years where there is no principal repayment, MRP will be charged in accordance with the MRP policy for the assets funded by the loan, including where appropriate, delaying MRP until the year after the assets become operational. While this is not one of the options in the MHCLG Guidance, it is thought

to be a prudent approach since it ensures that the capital expenditure incurred in the loan is fully funded over the life of the assets.

- No MRP will be charged in respect of assets held within the Housing Revenue Account.

Capital expenditure incurred during 2023/24 will not be subject to a MRP charge until 2024/25 or later.

Based on the Council's latest estimate of its Capital Financing Requirement on 31st March 2023, the budget for MRP has been set as follows:

	31/03/23 Estimated CFR £m	2023/24 Estimated MRP £m
Supported Capital Expenditure after 31.03.2008	0	0
Unsupported Capital Expenditure after 31.03.2008	21.0	0.16
Leases	0.3	0.07
Total General Fund	21.3	0.23
Assets in the Housing Revenue Account	45.6	0
HRA Subsidy Reform Payment	127.1	0
Total Housing Revenue Account	172.7	0
Total	194.0	0.23

Revenue Account (HRA)

Following the budget on 30 October 2018, the legislation that capped the amount of HRA debt a local housing authority could hold was revoked with immediate effect. The capital financing requirements relating to the HRA will remain the same so there will still be no requirement for an MRP and levels of debt will be managed through prudential borrowing limits controlled by the Treasury Management Strategy.

Removing the debt cap and not having a statutory requirement to make a provision to repay debt presents a significant risk to the HRA. Very careful treasury management is needed to ensure that the Council's HRA borrowing remains affordable, prudent and reasonable and that the HRA remains sustainable over the long term.



**North East
Derbyshire**
District Council

North East Derbyshire District Council

Investment Strategy 2023/24 – 2026/27

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 (known as **treasury management investments**),
 - to support local public services by lending to or buying shares in other organisations (**service investments**), and
 - to earn investment income (known as **commercial investments** where this is the main purpose).
- 1.2 This investment strategy meets the requirements of the statutory guidance issued by the Government in January 2018, 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 £11.7m and £30.0m during the 2023/24 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 2023/24 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 Rykneld Homes Ltd to allow development of social housing. Rykneld Homes Ltd is a wholly owned subsidiary of the Council, limited by guarantee. It also includes a loan to Northwood Group Ltd for a mixed tenure housing development scheme in the district.
- 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	31/3/2022 actual			2023/24
	Balance owing £m	Loss allowance £m	Net figure in accounts £m	Approved limit £m
Rykneld Homes Ltd	7.029	0	7.029	13.500
Northwood Group Ltd	4.929	0	4.929	8.663
Total	11.958	0	11.958	22.163

- 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 are 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. The strength of the partnership between Rykneld Homes company and the Council and Northwood group Ltd and the Council helps to mitigate any risk associated with non-payment.

Service Investments: Shares

- 1.10 **Contribution:** The Council has invested £0.150m 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	31/3/2022 actual			2023/24
	Amounts invested £m	Gains or (losses) £m	Value in accounts £m	Approved Limit £m
Northwood Group Ltd	0.150	(0.016)	0.134	0.150
TOTAL	0.150	(0.016)	0.134	0.150

- 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. These are mainly industrial units owned across the district.

Table 3: Property held for investment purposes

Property	Actual	31/3/2022 actual		31/3/2023 expected	
	Purchase cost £m	Gains or (losses) £m	Value in accounts £m	Gains or (losses) £m	Value in accounts £m
Industrial Units	4.1	5.7	9.8	0	9.8
Land	1.7	7.3	9.0	0	9.0
Commercial Properties	1.1	0.1	1.2	0	1.2
Shared Ownership Properties	1.0	0.4	1.4	0	1.4
TOTAL	7.9	13.5	21.4	0	21.4

- 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. Should the 2022/23 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.
- 1.19 Where value in the accounts is below purchase cost, the fair value of the Council's investment property portfolio would no longer be sufficient to provide security against loss, and the Council would therefore need to take mitigating actions to protect the capital invested. These actions could include maintaining the investment properties to a required standard and once vacant, advertising any empty investment properties quickly and with professional advertising agencies.
- 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.
- 1.23 The Council has contractually committed to make up to £8.663m of loans to Northwood Group Ltd should it request it.

Proportionality

- 1.24 The Council is to some extent dependent on income 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 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 Council's contingency plans for continuing to provide these services are to meet the shortfalls from other efficiencies generated within the general fund revenue budget or utilise reserves set aside for this purpose.

Table 4: Proportionality of investments

	2021/22 Actual £m	2022/23 Forecast £m	2023/24 Budget £m	2024/25 Budget £m	2025/26 Budget £m	2026/27 Budget £m
Net Service Expenditure	10.431	13.272	14.805	13.978	13.646	13.815
Net Investment Income	0.474	0.458	0.450	0.451	0.450	0.449
Proportion	4.5%	3.5%	3.0%	3.2%	3.3%	3.3%

Borrowing in Advance of Need

- 1.25 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

- 1.26 **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.
- 1.27 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.
- 1.28 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.
- 1.29 **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.
- 1.30 **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

- 1.31 The Council has set the following quantitative indicators to allow elected members and the public to assess the Council's total risk exposure as a result of its investment decisions.
- 1.32 **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

Total investment exposure	31/03/2022 Actual £m	31/03/2023 Forecast £m	31/03/2024 Forecast £m
Treasury management investments	37.00	20.50	11.70
Service investments: Loans – Rykneld Homes Ltd	7.03	6.77	6.50
Service investments: Loans – Northwood Group Ltd	4.93	8.11	6.41
Service investments: Shares – Northwood Group Ltd	0.15	0.15	0.15
Commercial investments: Property	21.40	21.40	21.40
TOTAL INVESTMENTS	70.51	56.93	46.16
Commitments to lend	10.20	7.28	9.25
TOTAL EXPOSURE	80.71	64.21	55.41

- 1.33 **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.

Table 6: Investments funded by borrowing

Investments funded by borrowing	31/03/2022 Actual £m	31/03/2023 Forecast £m	31/03/2024 Forecast £m
Treasury management investments	0	0	0
Service investments: Loans – Rykneld Homes Ltd	7.03	6.77	6.50
Service investments: Loans – Northwood Group Ltd	4.93	8.11	6.41
Service investments: Shares – Northwood Group Ltd	0	0	0
Commercial investments: Property	0	0	0
TOTAL FUNDED BY BORROWING	11.96	14.88	12.91

- 1.34 **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	2021/22 Actual £m	2022/23 Forecast £m	2023/24 Forecast £m
Treasury management investments	0.08%	1.06%	1.49%
Service investments: Loans – Rykneld Homes Ltd	3.50%	3.53%	3.52%
Service investments: Loans – Northwood Group Ltd	5.09%	5.09%	5.09%
Service investments: Shares – Northwood Group Ltd	0.00%	0.00%	0.00%
Commercial investments: Property	2.22%	2.15%	2.11%

- 1.35 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.



North East Derbyshire District Council

Flexible Use of Capital Receipts Strategy 2023/24 – 2024/25

Introduction

- 1.1 As part of the November 2015 Spending Review, the Government announced that it would introduce flexibility for the period of the Spending Review for local authorities to use capital receipts from the sale of assets to fund the revenue costs of service reform and transformation.

The Guidance

- 1.2 The guidance issued by the Secretary of State under section 15(1)(a) of the Local Government Act 2003 specified that:
- Local authorities will only be able to use capital receipts from the sale of property, plant and equipment received in the years in which this flexibility is offered. They may not use their existing stock of capital receipts to finance the revenue costs of reform.
 - Local authorities cannot borrow to finance the revenue costs of the service reforms.
 - The expenditure for which the flexibility can be applied should be the up-front (set up or implementation) costs that will generate future ongoing savings and/or transform service delivery to reduce costs or to improve the quality of service delivery in future years. The ongoing revenue costs of the new processes or arrangements cannot be classified as qualifying expenditure.
 - The key determining criteria to use when deciding whether expenditure can be funded by the new capital receipts flexibility is that it is forecast to generate ongoing savings to an authority's net service expenditure.
 - In using the flexibility, the Council will have due regard to the requirements of the Prudential Code, the CIPFA Local Authority Accounting Code of Practice and the current edition of the Treasury Management in Public Services Code of Practice.

- 1.3 The Council is also required to prepare a “Flexible use of capital receipts strategy” before the start of the year to be approved by Council which can be part of the budget report to Council. This Strategy therefore applies to the financial years 2023/24 to 2024/25.

Examples of qualifying expenditure

- 1.4 There are a wide range of projects that could generate qualifying expenditure and the list below is not prescriptive. Examples of projects include:

- Sharing back-office and administrative services with one or more other council or public sector bodies;
- Investment in service reform feasibility work, e.g. setting up pilot schemes;
- Collaboration between local authorities and central government departments to free up land for economic use;
- Funding the cost of service reconfiguration, restructuring or rationalisation (staff or non-staff), where this leads to ongoing efficiency savings or service transformation;
- Sharing Chief Executives, management teams or staffing structures;
- Driving a digital approach to the delivery of more efficient public services and how the public interacts with constituent authorities where possible;
- Aggregating procurement on common goods and services where possible, either as part of local arrangements or using Crown Commercial Services or regional procurement hubs or Professional Buying Organisations;
- Improving systems and processes to tackle fraud and corruption in line with the Local Government Fraud and Corruption Strategy – this could include an element of staff training;
- Setting up commercial or alternative delivery models to deliver services more efficiently and bring in revenue (e.g. through selling services to others);
- Integrating public facing services across two or more public sector bodies (e.g. children’s social care, trading standards) to generate savings or to transform service delivery.

The Council's Proposals

- 1.5 Government has provided a definition of expenditure which qualifies to be funded from capital receipts. This is: "Qualifying expenditure is expenditure on any project that is designed to generate ongoing revenue savings in the delivery of public services and/or transform service delivery to reduce costs and/or transform service delivery in a way that reduces costs or demand for services in future years for any public sector delivery partners. Within this definition, it is for individual local authorities to decide whether or not a project qualifies for the flexibility."
- 1.6 The Government's use of flexible capital receipts directive has been extended until 31st March 2025.
- 1.7 The Council currently has no plans to utilise the use of flexible capital receipts during the period of the Medium Term Financial Plan 2023/24 to 2026/27.

Impact on Prudential Indicators

- 1.8 The guidance requires that the impact on the Council's Prudential Indicators should be considered when preparing a Flexible Use of Capital Receipts Strategy. The Council's current capital programme does not utilise the capital receipts that will be generated to fund the above proposal. Therefore, there will be no change to the Council's Prudential Indicators that are contained in the Treasury Management Strategy Statement.
- 1.9 This strategy has been produced to fulfil the requirements of the DELTA return for the flexible use of capital receipts. As the Council is not utilising the flexible use of capital receipts within its current medium term financial plan this strategy was not needed and not taken through the usual Council committee, it will, in future be added to the normal Treasury Management Strategy Statement approval process