6 December 2023
By the Director of Resources
DECISION REQUIRED

Not exempt

Horsham District Council

Capital Strategy 2024/25 incorporating Investment and Treasury Management Strategy

Executive Summary

This report combines an overview of how capital expenditure, capital financing, treasury and other investment activity contribute to the provision of local public services, how the associated risks are managed and the implications for future financial sustainability.

The strategies set limits and indicators that embody the risk appetite that the Council believes to be prudent. The strategies are set against the Council's own mid-term financial strategy, the context of the UK economy and projected interest rates.

Treasury investment criteria and limits which are unchanged except for the limits for long term investments that have been increased by £4m to give more leeway for medium term investing. Details are in Appendix B paragraph 36.

The investment strategy in paragraphs 4.11 to 4.18 and appendix C pulls together information on service loans and commercial property to demonstrate the Council's risk management approach in that area. The overall strategy is unchanged. The commercial property portfolio is projected to maintain income levels but risks to income persist especially in the retail part of the portfolio.

Recommendations

The Committee is asked to:

i) approve this Capital Strategy as an appropriate overarching strategy for the Council while leaving full Council to approve the updated Capital Strategy that will accompany the 2024/25 budget to Council.

ii) recommend that full Council approve the Treasury Management Strategy for 2024/25 and the associated limits and specific indicators included in section 4 and appendix B of this report.

iii) recommend that full Council approve the Investment Strategy for 2024/25 and the associated limits and specific indicators included in section 4 and appendix C of this report.

Reasons for Recommendations

i) The Council is required to have regard to the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice and Prudential Code for Capital Finance that require the Council to approve a Capital Strategy, Investment Strategy and Treasury Management Strategy before the start of each financial year.

ii) The Department for Levelling Up, Housing and Communities (DLUHC) issued revised guidance on local authority investments in 2018 that the Council is required to have regard to.

Background Paper

"Update of the Council's Financial Position in 2023/24" – Cabinet 23 November 2023

Consultation: Arlingclose Limited

Wards affected: All

Contact: Julian Olszowka, Group Accountant, Technical, 01403 215310

Background Information

1 Introduction

The purpose of this report

1.1 This report covers the requirements of CIPFA Codes and guidance that the Council must, by statute, have regard to. Section 3 gives an overview of:

- how capital expenditure, capital financing and treasury management activity contribute to the provision of local public services
- how associated risk is managed and;
- the implications for future financial sustainability.

1.2 The Treasury Management Strategy in section 4 covers the aspects of investments that this Committee has historically considered. It covers management of the Council's cash flows, borrowing and investments, and the associated risks.

1.3 The Investment Strategy starting in paragraph 4.11 covers investments held for service purposes or for commercial yield.

1.4 The guidance requires the Capital and Investment Strategies to be approved by full Council while the Treasury Management Strategy can now be approved by a subcommittee of the Council. However, here we follow the Council's own practice that this Committee recommends the Treasury Management Strategy be approved by full Council.

2 Background

Economic background

2.1 The Council's strategies must take account of expectations for the economy and specifically the finance sector. The Council receives advice on this from its advisors Arlingclose Ltd. Appendix A is a commentary by them on the current economic background, the outlook for creditworthiness and interest rates.

2.2 For the purpose of the interest budget, any new investments are estimated to be on or about the Bank Rate.

2.3 The treasury management environment has changed radically over last year or so. The very low yields that had seemed to be the new normal have been replaced by rising rates and rate volatility. Although this has brought challenges of interpreting how rates would develop, the rising rates have significantly increased the Council's investment income. The next movement in rates is expected to be a slow downward trajectory, however, recent experience has underlined the risk of relying too much on expert economic predictions.

Statutory background

2.4 This report is part of the Council's legal obligation under the Local Government Act 2003 to have regard to both the CIPFA Codes and the Department For

Levelling Up, Housing and Communities Guidance. 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.

2.5 Next year will be the second year of fully implementing the 2021 revised Codes. Those revisions were a tightening of previous versions of the Codes after concerns from CIPFA and Central Government that some councils were able to take unsustainable commercial risks under the previous Codes.

Relevant Council policy

2.6 The Council's constitution requires that the Council approve Prudential Code indicators and Treasury Management Strategy. The Investment Strategy covering commercial property has been split from the traditional Treasury Management Strategy here for ease of understanding as it deals with a different type of investment, but it can be considered to be encompassed in the definition of the Treasury Management Strategy as used by the Constitution.

2.7 The existing strategies and Prudential indicators were approved by the Council on 22 February 2023; having been recommended for adoption by this Committee on 7 December 2022.

3 Capital Expenditure and Financing

3.1 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. 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 or leasing).

3.2 Service managers bid annually in October to include projects in the Council's capital programme. Bids are collated by Finance who calculate the financing cost (which can be nil if the project is fully externally financed). The Senior Leadership Team appraises all bids based on a comparison of service priorities against financing costs and makes recommendations to the informal cabinet. The final capital programme is then presented to Cabinet in January and to Council in February each year.

3.3 The current projected capital programme and financing is shown below. It includes current estimates for capital bids for 2024/25 and beyond. It will be revised, if necessary, as the 2024/25 budget process develops and the final figures that appear alongside the final budget report in 2024 will constitute the prudential indicators required by the CIPFA Prudential Code.

3.4 The £2.4m of 'debt' financing in 2024/25 is the effect of an accounting change following the implementation of the accounting standard IFRS16 by UK councils. Leased assets will be recognised as though they are an asset on the balance sheet from April 2024 which leads to an increase in the necessary capital finance. This creates a ‘notional’ financing requirement as though the asset were purchased. The actual cash payments for leases remains the same so there is no change to the financial transactions of the Council only its presentation in the accounts.

£millions	2022/23 Actual £000	2023/24 Estimate £000	2024/25 Estimate £000	2025/26 Estimate £000	2026/27 Estimate £000
Services spend	4.3	14.6	10.9*	11.6	14.8
Capital Investments	0.9	0.2	0.1	0.1	0.1
Financed by:					
External resources	2.7	4.9	2.0	1.8	5.3
Internal Resources	2.5	9.9	6.6	9.9	9.6
Debt	0.0	0.0	2.4*	0.0	0.0
Total Financing	5.2	14.8	11.0	11.7	14.9

*Spend and debt have £2.4m added due to lease accounting change which does not represent cash expenditure

3.4 Capital spend is broken down into spend which directly provides services and spend on capital investments, which covers equity and loans provided to the Council’s Housing companies or required improvements to existing investment properties.

3.5 The term ‘Debt’ used above does not automatically lead to external borrowing as the Council may be able to use cash it holds in reserves and as working capital which is usually termed ‘internal borrowing’.

3.6 Over time, all debt, whether it be internal or external borrowing, must be repaid, and this is therefore replaced over time by other financing, usually from revenue which is known as minimum revenue provision (MRP). The Council is required to make an annual MRP statement and this will be included in the Budget report in January 2024 and the methodology will be on the same basis as 2023/24. The current planned MRP payments are set out below. The increase in 2024/25 is due to the accounting change mentioned above and again does not affect the Council’s overall budget.

£millions	2022/23 actual	2023/24 forecast	2024/25 budget	2025/26 budget	2026/27 budget
MRP	0.9	0.9	1.2	1.2	1.2

3.7 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 any capital receipts used to replace debt. The CFR is gradually decreasing as MRP is paid and no new unfinanced spend is planned. The increase 2024/25 is again due to the change in lease accounting. The Council’s estimated CFR is projected as follows:

£millions	31.3.2023 actual	31.3.2024 forecast	31.3.2025 budget	31.3.2026 budget	31.3.2027 budget
CFR	32.7	31.8	33.0	31.8	30.7

3.8 **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. Repayments of capital grants, loans and investments also generate capital receipts. Loans repaid below are estimates of those from the Council's Housing Company. The Council projects capital receipts as follows:

£millions	**2022/23 actual**	**2023/24 forecast**	**2024/25 estimate**	**2025/26 estimate**	**2026/27 estimate**
Asset sales	0.4	0.4	0.4	0.4	0.4
Loans repaid	0.3	0.0	0.0	0.0	0.0
TOTAL	**0.7**	**0.4**	**0.4**	**0.4**	**0.4**

4 Treasury Management

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

4.2 **Borrowing strategy**: The Council has no plans to borrow but could find itself in a position which calls for borrowing. In that circumstance, the main objectives when borrowing would be to achieve a low but certain cost of finance while retaining flexibility. These objectives are often conflicting, and the Council therefore would seek to strike a balance between short-term loans (currently available at about 5.4%) and long-term fixed rate loans where the future cost is known (currently about 5%).

4.3 Projected levels of the Council's total outstanding debt are shown below, compared with the Capital Financing Requirement. Statutory guidance is that debt should remain below the Capital Financing Requirement, except in the short-term. As can be seen from the table the Council expects to comply with this in the medium term.

£millions	**31.3.2023 actual**	**31.3.2024 forecast**	**31.3.2025 budget**	**31.3.2026 budget**	**31.3.2027 budget**
Debt	0	0	2.4*	2.1*	1.9*
CFR	32.7	31.8	33.0	31.8	30.7

*Debt is again purely due to accounting change and not actual unfinanced spend

4.4 The table above demonstrates that the Council is relying on internal borrowing i.e. using reserves and other cash resources that it holds rather than borrowing from external sources. From projections of the capital programme and use of reserves this strategy is seen as sustainable in the medium term although the Director of Resources will monitor the actual position against the projections in order to be ready to respond should external borrowing become advisable.

4.5 **Liability benchmark:** This is an indicator in the CIPFA Prudential Code designed to compare a Council's actual borrowing against a benchmark showing the lowest risk level of borrowing. The Council has no current or forecast need to borrow and therefore has a liability benchmark of zero. The table in paragraph 4.8 below shows a projection of investments based on long-term cash flow forecasts and this acts as a general envelope for the long-term treasury management strategy.

4.6 **Affordable borrowing limit**: Irrespective of plans to borrow or not the Council is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt) each year. In line with statutory guidance, a lower "operational boundary" is also set as a warning level should debt approach the limit. Although no borrowing is planned, limits are set in case a need develops. Further details on borrowing are in appendix B.

£millions	**2023/24 limit**	**2024/25 limit**	**2025/26 limit**	**2026/27 limit**
Authorised limit – borrowing	15	15	15	15
Authorised limit – leases	6	6	6	6
Authorised limit – total external debt	21	21	21	21
Operational boundary – borrowing	0	0	0	0
Operational boundary – leases	0	2.5	2.5	2.5
Operational boundary – total external debt	0	2.5	2.5	2.5

4.7 **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 dealt with in the Investment Strategy in paragraph 4.11 onwards and Appendix C.

4.8 The Council's policy on treasury investments is to prioritise security and liquidity over yield, that is to focus on minimising risk rather than maximising returns. Cash that is likely to be spent in the near term is invested securely, for example with the government, other local authorities or selected high-quality banks, to minimise the risk of loss. Money that will be held for longer terms is invested more widely, including in bonds, shares and property, to balance the risk of loss against the risk of receiving returns below inflation. Both 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. The future longer-term investments in the table below include strategic pooled funds that the Council intends to hold for the longer term, although they can be sold if required.

	31.3.2023 actual	**31.3.2024 forecast**	**31.3.2025 estimate**	**31.3.2026 estimate**	**31.3.2027 estimate**
Near-term investments	33	27	23	19	16
Longer-term investments	42	42	42	37	28
TOTAL	**75**	**69**	**65**	**56**	**44**

4.9 The projections show cash balances at year-end, which is a cash low point, in the region of £40m in the medium term. The Capital programme is expected to include some major projects in the medium term which will start to eat into cash balances. The position around developers' contributions is uncertain because of strategic planning issues so their contribution to cash balances is hard to quantify. Further detail on treasury investments are in Appendix B including limits and indicators which the Committee is asked to consider. The significant changes compared to last year's limits are an increase in limits on long term investments.

4.10 **Governance:** Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Director of Resources and staff, who must act in line with the Treasury Management Strategy as approved by the Council following this committee's scrutiny and recommendation. The Audit Committee currently receives quarterly reports and is responsible for scrutinising treasury management decisions.

Investment Strategy (loans, shares and property)

4.11 This section is the disclosure required by CIPFA and the Department for Levelling Up, Housing and Communities guidance, which has been tightened in recent years as concerns over the perceived increasing risks in Local Authority sector as councils have become more commercial and made large commercial property purchases.

Investments for Service Purposes

4.12 The Council has the ability to make investments to assist local public services, including making loans to local service providers and buying shares and making loans to any Council subsidiaries that provide services. In light of the public service objective, the Council is willing to take more risk than with treasury investments. However, it still plans for such investments to generate a return after all costs to offset risk. Further details on service investments are in appendix C. The overall limits are £4m on the total exposure to loans for service purposes. The limit to exposure permitted for shares is £0.5m.

4.13 **Governance:** Decisions on service investments are made by full Council after the relevant Head of Service has submitted a comprehensive analysis in consultation with the Director of Resources and must meet the criteria and limits. Most loans and shares are capital expenditure and will therefore also be approved as part of the capital programme in the Budget report or by full Council.

Commercial Activities

4.14 With central government financial support for local public services declining, the Council invests in commercial property within the district purely or mainly for financial gain. Total commercial investments were valued at £58m on 31 March 2023. These provide a net return after direct costs of 6.4% based on the last set of final accounts which value the assets at market value rather than historical value.

4.15 As financial return is the main objective, the Council recognises the higher risk on commercial investment compared with treasury investments. The principal risk exposures include individual voids, falls in market value, and changes in economic activity. Individual property risks are constantly monitored and managed by the Head of Property and Facilities. Should income not meet expectations the Council holds at least £6m of general reserves available to balance the revenue budget in the short term while the Head of Property and Facilities reviews the performance of the portfolio.

4.16 In order that commercial investments remain proportionate to the financial capacity of the Council, these are currently subject to an overall maximum investment limit which is set at £70m.

4.17 **Governance:** Decisions on new commercial investments are made by the Cabinet after consideration by the Policy Development Advisory Groups for Finance and Resources, and Local Economy and Place in line with the criteria and limits approved by the Council in this strategy. Property and most other commercial investments are also capital expenditure and purchases will therefore also be approved as part of the capital programme. Further details on commercial investments and associated limits and benchmarks are in appendix C.

4.18 **Net income from commercial and service investments to net revenue stream:** the latest iteration of the Code requires the reporting of a prudential indicator that shows the proportion that commercial and service net income forms of the whole Council's net revenue stream.

	2022/23 actual	2023/24 forecast	2024/25 budget	2025/26 budget	2026/27 budget
Total net income from service and commercial investments	£3.7m	£3.5m	£3.8m	£3.8m	£3.8m
Proportion of net revenue stream	29%	26%	27%	26%	27%

Other Liabilities

4.19 The Council has set aside £0.9m to cover risks of Business Rates Appeals. The Council is also at risk of having to pay for historic insurance claims but has not put aside any money because there is no reasonable assessment of the amount required.

4.20 **Governance:** Decisions on incurring new discretionary liabilities are taken by the relevant director in consultation with the Director of Resources. If significant, these would be discussed at the quarterly corporate risk management meeting and final decisions as to recognition taken by the Director of Resources. New liabilities exceeding £1m are reported to full Council for approval or notification as appropriate. Further details on liabilities are in note 18 of the 2022/23 statement of accounts.

Revenue Budget Implications

4.21 Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP are charged to revenue. This 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 to produce a required prudential indicator. As the Council does not borrow the financing costs are purely the MRP which is stable apart from the increase due to the lease accounting change as no new unfinanced spend is envisaged.

	2022/23 actual	2023/24 forecast	2024/25 budget	2025/26 budget	2026/27 budget
Financing costs (£m)	0.9	0.9	1.2*	1.2*	1.2*
Proportion of net revenue stream	7%	7%	8%	8%	8%

*The increase in 2024/25 is the one-off effect of the IFRS16 lease accounting change

4.22 **Sustainability:** Due to the 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 40 years into the future. The Director of Resources is satisfied that the proposed capital programme is prudent, affordable and sustainable because the net budget demand on the Council and the risks in the programme have been reviewed and fall within the Council's tolerances.

Knowledge and Skills

4.23 The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. For example, the Director of Resources and S151 Officer is a qualified accountant with over 15 years' finance experience and the Head of Property and Facilities is a member of RICS with over 35 years' experience in commercial property. The Council continues to support junior staff to study towards relevant professional qualifications.

4.24 Where Council staff do not have the knowledge and skills required, use is made of external advisers that are specialists in their field. The Council currently employs Arlingclose Limited as treasury management advisers and for any significant property investment would use property consultants with specialist knowledge of the appropriate property sector. This approach ensures access to right knowledge and skills and can be more cost effective than employing such staff directly. The overarching requirement is that the Council has access to knowledge and skills commensurate with its risk appetite.

5 Outcome of Consultations

5.1 Externally the Council's adviser Arlingclose was consulted. Internally the Head of Property and Facilities was consulted.

6 Other courses of action considered but rejected

6.1 The Department for Levelling Up, Housing and Communities' Investment Guidance and the CIPFA Codes of Practice do not prescribe any particular strategies for local authorities to adopt. 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 will 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 will be smaller
Borrow additional sums at long-term fixed interest rates using less internal funds	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
Invest more in service loans	Interest income will be higher and service benefits will accrue	Increased risk of losses from credit related defaults or service body being unable to pay loan and provide service
Reduce investment in property	Income will be lower	Lower chance of losses from non-paying tenants or falling property values.
Invest additional sums in property	Income will be higher	Increased chance of losses from vacancies or falling property values. Reputational and regulatory risk if Council incurs large loss

7 Resource consequences

7.1 The budgeted treasury investment income in 2024/25 is £3.6m (2023/24 £2.4m), which is equivalent to an average investment portfolio of £81m at an interest rate of 4.5%. The increase is due to the general increase in the rates available. There is no budget for debt interest as no borrowing, even on a short-term basis, is envisaged. The budget for commercial property net income is £3.8m which is a yield of 6.5% from an investment portfolio of £58m.

7.2 There are no staffing consequences apart from the need for appropriate training.

8 Legal Considerations and Implications

8 .1 This report is part of the Council's legal obligation under the Local Government Act 2003 to have regard to both the relevant CIPFA Codes and the guidance issued by the Department for Levelling Up, Housing and Communities.

9 Risk assessment

9.1 Risks such as security of funds, liquidity, and interest rate risk are considered in the report. The limits and indicators chosen effectively set the Council's risk appetite.

10 Procurement implications

10.1 There are no procurement implications arising from this report.

11. Equalities and Human Rights implications / Public Sector Equality Duty

11.1 There are no direct equality or human rights implications arising from this report. However, it is recognised that the Council's investment choices may have an indirect effect on social issues. The investment management industry has begun to add social issues such as human rights and equality to its criteria for selecting investments and although this is at an early stage officers will work with its advisers as to how it can positively contribute in this area.

12 Environmental Implications

12.1 There are no direct environmental implications attributable to the recommended strategies. However, it is recognised that the Council's investment choices may have an indirect effect on the environment. Officers will work with its advisers as to how it can positively and constructively use its investments to reduce impact on the environment.

13 Other Considerations

13.1 There are no other considerations to take into account.

Appendix A Economic background and interest rate forecast

Economic background

The impact on the UK from higher interest rates and inflation, a weakening economic outlook, an uncertain political climate due to an upcoming general election, together with war in Ukraine and the Middle East, will be major influences on the economic background to the Council's treasury management strategy for 2024/25.

The Bank of England (BoE) increased Bank Rate to 5.25% in August 2023, before maintaining this level in September and then again in November. Members of the BoE's Monetary Policy Committee voted 6-3 in favour of keeping Bank Rate at 5.25%. The three dissenters wanted to increase rates by another 0.25%.

The November quarterly Monetary Policy Report (MPR) forecast a prolonged period of weak Gross Domestic Product (GDP) growth with the potential for a mild contraction due to ongoing weak economic activity. The outlook for CPI inflation was deemed to be highly uncertain, with near-term risks to CPI falling to the 2% target coming from potential energy price increases, strong domestic wage growth and persistence in price-setting.

Office for National Statistics (ONS) figures showed CPI inflation was 4.6% in October a fall from the September 2023 figure of 6.7%. Core CPI inflation fell to 5.7% from 6.1%. Although these figures fell more than expected inflation is still well above the Government's 2% target.

ONS figures showed the UK economy grew by 0.2% between April and June 2023. The BoE forecasts GDP will likely stagnate in Q3 but increase modestly by 0.1% in Q4, a deterioration in the outlook compared to the August MPR. The BoE forecasts that higher interest rates will constrain GDP growth, which will remain weak over the entire forecast horizon.

The labour market appears to be loosening, but only very slowly. The unemployment rate remained at 4.2% in the second and third quarters of 2023. Earnings growth remained strong, with regular pay (excluding bonuses) up 7.7% over the third quarter. The unemployment rate has remained at 4.2% in the last two quarters while vacancies fell from August to October 2023 58,000 to 957,000.

Credit outlook

Credit Default Swap (CDS) prices were volatile during 2023, spiking in March on the back of banking sector contagion concerns following the major events of Silicon Valley Bank becoming insolvent and the takeover of Credit Suisse by UBS. After then falling back in Q2 of calendar 2023, in the second half of the year, higher interest rates and inflation, the ongoing war in Ukraine, and now the Middle East, have led to CDS prices increasing steadily.

On an annual basis, CDS price volatility has so far been lower in 2023 compared to 2022, but this year has seen more of a divergence in prices between ringfenced (retail) and non-ringfenced (investment) banking entities once again.

Moody's revised its outlook on the UK sovereign to stable from negative to reflect its view of restored political predictability following the volatility after the 2022 mini-budget.

Moody's also affirmed the Aa3 rating in recognition of the UK's economic resilience and strong institutional framework.

Following its rating action on the UK sovereign, Moody's revised the outlook on five UK banks to stable from negative and then followed this by the same action on five rated local authorities. However, within the same update the long-term ratings of those five local authorities were downgraded.

There remain competing tensions in the banking sector, on one side from higher interest rates boosting net income and profitability against another of a weakening economic outlook and likely recessions that increase the possibility of a deterioration in the quality of banks' assets.

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.

Interest rate forecast:

Although UK inflation and wage growth remain high, the Council's adviser Arlingclose forecasts that Bank Rate has peaked at 5.25%. The BoE's Monetary Policy Committee will cut rates in the medium term to stimulate the UK economy but will be reluctant to do so until it is sure there will be no lingering second-round effects. Arlingclose sees rate cuts from Q3 2024 to a low of around 3% by early-mid 2026.

Arlingclose expects long-term gilt yields to eventually fall from current levels (amid continued volatility) reflecting the lower medium-term path for Bank Rate. However, yields will remain relatively higher than in the past, due to quantitative tightening and significant bond supply. As ever, there will undoubtedly be short-term volatility due to economic and political uncertainty and events.

Like the BoE, the Federal Reserve and other central banks see persistently high policy rates through 2023 and 2024 as key to dampening domestic inflationary pressure. Bond markets will need to absorb significant new supply, particularly from the US government.

	Current	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26
Official Bank Rate													
Upside risk	0.00	0.25	0.50	0.50	0.75	0.75	0.75	0.75	0.75	0.75	0.75	1.00	1.00
Central Case	5.25	5.25	5.25	5.25	5.00	4.75	4.25	4.00	3.75	3.50	3.25	3.00	3.00
Downside risk	0.00	0.00	-0.25	-0.50	-0.75	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
3-month money market rate													
Upside risk	0.00	0.25	0.50	0.50	0.75	0.75	0.75	0.75	0.75	0.75	0.75	1.00	1.00
Central Case	5.40	5.40	5.40	5.30	5.15	4.80	4.30	4.10	3.80	3.50	3.25	3.05	3.05
Downside risk	0.00	0.00	-0.25	-0.50	-0.75	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
5yr gilt yield													
Upside risk	0.00	0.50	0.70	0.70	0.85	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Central Case	4.28	4.35	4.30	4.25	4.10	4.00	3.75	3.50	3.40	3.30	3.30	3.30	3.35
Downside risk	0.00	-0.55	-0.75	-0.85	-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	0.50	0.70	0.70	0.80	0.90	1.00	1.10	1.20	1.20	1.20	1.20	1.20
Central Case	4.32	4.40	4.35	4.30	4.25	4.15	4.00	3.80	3.75	3.65	3.60	3.65	3.70
Downside risk	0.00	-0.55	-0.75	-0.85	-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	0.50	0.70	0.70	0.80	0.90	1.00	1.10	1.20	1.20	1.20	1.20	1.20
Central Case	4.78	4.70	4.65	4.55	4.45	4.35	4.25	4.25	4.25	4.25	4.25	4.25	4.25
Downside risk	0.00	-0.55	-0.75	-0.85	-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	0.50	0.70	0.70	0.80	0.90	1.00	1.10	1.20	1.20	1.20	1.20	1.20
Central Case	4.38	4.30	4.25	4.20	4.15	4.15	4.10	4.10	4.10	4.10	4.10	4.10	4.10
Downside risk	0.00	-0.55	-0.75	-0.85	-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%; Certainty Rate = Gilt yield + 0.80%

Appendix B Treasury Management Strategy

Mid-year position and forecast

1 On 30 September 2023 the Council held no borrowing and £84.6m of investments at market value; broken down as follows:

	Principal £m	Interest Rate %
Banks & building societies (unsecured)	0.4	1.5
Covered bonds (secured)	20	4.6
Local authorities & govt entities	12	5.3
Money Market Funds – call	10.5	5.3
Money Market Funds – cash plus or short bonds	13.2	2.9
Pooled Funds - Property	4.6	3.8
Pooled Funds – Multi-Asset	8.2	4.9
Pooled Funds – Equity	8.4	4.5
Pooled Funds – Bonds	5.3	3.5
REIT	2.0	2.7
Net Investments	**84.6**	**4.5**

2 Taking the forecasts within the capital strategy, the balance sheet of the Council can be projected to estimate the amounts available for investments. Below is the current projected analysis of the balance sheet to illustrate the trajectory of the Council's funds. The notional external borrowing is again a consequence of lease accounting change and is not true borrowing.

All figures at year-end £m	**Actual 2022/23**	**Estimate 2023/24**	**Estimate 2024/25**	**Estimate 2025/26**	**Estimate 2026/27**
CFR	32.7	31.8	33.0	31.8	30.7
Less notional lease borrowing	0	0	2.3	2.1	1.9
Internal borrowing	32.7	31.8	30.7	29.7	28.8
Useable reserves, receipts, contributions held	96.0	89.6	83.6	73.9	61.0
Working capital/other balances	11.7	11.7	11.7	11.8	11.8
Estimated Investments	75.0	69.5	64.6	56.0	44.0

3 The Council's strategy has been to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing. In spite of the continuation of this, the Council is projected to hold significant investment balances even at the end of the financial year, which is the low point for cash. Investments levels are expected to fall over the period as reserves are used to finance capital spend and developer contributions flow out.

Borrowing Strategy

4 As shown above the Council is not expecting to borrow long term funds although it may need short-term borrowing if short term cash flow issues require it.

5 **Sources of borrowing:** The approved sources of long-term and short-term borrowing are:

- Public Works Loan Board (PWLB)
- Any institution approved for investments (see below)
- Any other bank or building society authorised to operate in the UK
- UK public and private sector pension funds (except West Sussex County Council Pension Fund)
- Capital market bond investors
- UK Municipal Bond Agency and other special purpose companies created to enable joint local authority bond issues.
- UK Infrastructure Bank Ltd

6 In addition, capital finance may be raised by the use of leases and hire purchase that are not borrowing, but may be classed as other debt liabilities.

7 The Council has historically raised its long-term borrowing from the PWLB. Changes to PWLB lending rules have added restrictions on local authorities planning to buy investment assets primarily for yield. Although the Council has no plans to borrow it will review its capital plans against the PWLB rules so it does not restrict access to PWLB in the future. In the event longer term borrowing is required the Council would consider long-term loans from all possible sources in order to lower interest costs and avoid over-reliance on one source of funding.

Investment Strategy

8 The Council holds significant funds, representing income received in advance of expenditure plus balances and reserves held. In the past year, the Council's total investments have ranged between £108m and £74m and although the level of reserves is expected to reduce in the longer term, there will still be significant short to medium-term cash flow surpluses leading to larger sums being held than the core reserves of the Council would indicate. The current projections show year-end balances over £44m for the next three years.

9 Both the CIPFA Code and the Department For Levelling Up, Housing And Communities Guidance require the Council to invest its 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. Where balances are expected to be invested for more than one year, the Council's long-term aim is 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. This may not be possible in the high inflation environment of today but remains the long-term objective.

10 The Council aims to be a responsible investor and will consider environmental, social and governance (ESG) issues when investing. However, realistically the Council does not have the resources to analyse all its investments for ESG considerations as it is a complex area with no clear and easily followed standards or ESG scoring mechanisms to follow. The Council will work with its advisers and its fund managers in order to maximise its impact in this area and develop its approach over the medium term.

11 The Council expects to be a long-term investor and treasury investments will therefore include both short-term low risk instruments to manage day-to-day cash flows and longer-term instruments where limited additional risk is accepted in return for higher investment income. The existing portfolio of strategic pooled funds will be maintained to diversify risk into different sectors and maintain investment income. The Council will also explore the use of secured bonds and other ways to diversify its portfolio.

12 **Business models:** Under the IFRS9 accounting 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 rather than buying and selling investments and therefore, where other criteria are also met, these investments will continue to be accounted for at amortised cost.

13 **Approved counterparties**: The Council may invest with any of the counterparty types in the table below; subject to the cash limits (per counterparty) and the time limits shown. There are no changes from the 2023/24 limits.

Sector	Time limit	Counterparty limit	Sector limit
The UK Government	50 years	Unlimited	n/a
Local authorities	10 years	£5m	Unlimited
Governments and government entities rated A- and above	10 years	£5m	Unlimited
Secured investments rated AA and above	10 years	£5m	Unlimited
Secured investments rated A- to A+	13 months	£5m	Unlimited
Banks (unsecured) rated A and above	13 months	£3m	Unlimited
Banks (unsecured) rated A-	6 months	£3m	Unlimited
Building societies (unsecured)	13 months	£1.25m	£10m
Registered providers (unsecured) Rated A-and above	5 years	£5m	£10m
Registered providers unrated(unsecured)	3 years	£4m	
Money market funds	n/a	£6m	£50m
Strategic pooled funds – Property, Equity, Bond and Diversified assets	n/a	£6m	£30m
Real estate investment trusts	n/a	£5m	£5m
Other Corporates rated A- and above	1 year	£3m	£5m
Unrated corporates	5 years	£50,000	£2m

This table must be read in conjunction with the notes below.

14 **Credit Rating**: Investment limits are set with reference to the lowest published long-term credit rating from Fitch, Moody's or Standard & Poor's. 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.

15 **Government**: Loans, 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 an insignificant risk of insolvency. Investments with the UK Central Government may be made in unlimited amounts for up to 50 years.

16 **UK Local Authority:** The Council will consider investments with a UK local government body up to £5m for up to 10 years. The Council is confident that as a sector, local authorities are secure investments in the context of support from Central Government and the legal surcharging framework that guarantees debts will be paid. However, for any investment over six months the financial resilience of the relevant council will be checked with the Council's advisor.

17 **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.

18 **Banks 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.

19 **Building Societies:** Although the regulation of building societies is no longer any different to that of banks the Council takes additional comfort from building societies' business model. The Council will therefore consider investing with unrated building societies where independent credit analysis shows them to be suitably creditworthy. A minimum asset size of £250m applies and limits of £1.25m per Society and £10m in total apply for unrated societies.

20 **Registered Providers:** Loans and bonds issued by, guaranteed by or secured on the assets of Registered Providers of Social Housing, formerly known as Housing Associations. These bodies are tightly regulated by the Regulator of Social Housing and, as providers of public services; they retain the likelihood of receiving government support if needed.

21 **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.

22 **Strategic pooled funds:** Bond, equity and property funds 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.

23 **Real estate investment trusts (REIT):** 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. The Council will carry out a detailed appraisal and take expert advice before any investment.

24 **Corporates**: Loans, bonds and commercial paper issued by companies other than banks and registered providers. Non-bank companies cannot be bailed-in but can become insolvent placing the Council's investment at risk. Loans to unrated companies will only be made either following an external credit assessment or to a maximum of £50,000 per company as part of a diversified pool in order to spread the risk widely.

25 **Operational bank accounts:** The Council may incur exposure through its current accounts 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 still subject to the risk of a bank bail-in and balances will therefore be kept below £3m. 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. The Council currently banks with NatWest rated A.

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

- no new investments will be made,
- any existing investments that can be ended 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

27 Where a credit rating agency announces that a rating is on review for possible downgrade (also known as "rating watch negative" or "credit watch negative") so that it may fall below the approved rating criteria, then no investments other than call investments 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.

28 **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 and reports in the quality financial press. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may meet the Council's credit rating criteria.

29 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 those 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. This may reduce investment income earned, but will protect the principal sum invested.

30 **Investment limits**: The Council's revenue reserves available to cover investment losses were in the region of £26m on 31 March 2023, well above the stated minimum long-term target of £6m. In order that available reserves will cover the case of a single default, the maximum that will be lent to any one organisation (other than the UK Government or Local Authority) will be £5m. A group of banks under the same ownership will be treated as a single organisation for limit purposes. Limits will also be 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.

Category	**Cash limit**
Any group of organisations under the same ownership	£5m per group
Any group of pooled funds under the same management	£12m per manager
Negotiable instruments held in a broker's nominee account	£22m per broker
Foreign countries	£12m per country

Cash flow management

31 The Council's officers maintain a detailed cash flow forecast for each coming year revising it as more information is available. This informs the short-term investments such as those to cover precept payments. The forecast is compiled on a prudent basis, with receipts under-estimated and payments over-estimated to minimise the risk of the Council being forced to borrow on unfavourable terms to meet its

financial commitments. Long term investment strategy is based on the Council's medium term financial strategy.

Treasury Management Indicators

32 **Security benchmark: average credit rating** 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. The benchmark for 2024/25 will be an average credit rating of A unchanged from 2023/24.

33 **Liquidity benchmark:** 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. For 2024/25 the benchmark amount available will be £3m unchanged from 2023/24.

Interest rate exposures

34 This indicator is set to control the Council's exposure to interest rate risk. Although no longer part of the formal CIPFA code this indicator is retained for local use. It is an upper limit on the one year revenue impact of a 1% rise or fall in interest rates. The impact of a change in interest rates is calculated on the assumption that maturing loans and investments will be replaced at current rates.

	Limit
Upper limit on one-year revenue impact of a 1% rise in interest rates	-£300,000
Upper limit on one-year revenue impact of a 1% fall in interest rates	£300,000

Maturity structure of borrowing

35 This indicator is set to control exposure to refinancing risk for councils with a portfolio of loans. The upper and lower limits on the maturity structure of fixed rate borrowing are shown below. The Council is not planning to borrow but will set limits to allow flexibility of term and maturity date for any new borrowing.

	Upper	Lower
Under 12 months	100%	0%
12 months and within 24 months	100%	0%
24 months and within five years	100%	0%
Five years and within 10 years	100%	0%
10 years and above	100%	0%

Principal sums invested for periods longer than a year

36 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. Although in the longer medium term the Council's cash balance are expected to track downwards in order to give some leeway in investing to secure longer term rates

it is proposed that these limits increase by £4m. Prior rates are shown in italics. The limits on the total long-term principal sum invested to final maturities beyond the period are:

	2024/25	2025/26	2026/27	No fixed date
Limit on principal invested beyond year end	£20m*(£16m)*	£18m*(£14m)*	£16m*(£12m)*	£35m

37 Long-term investments with no fixed maturity date include strategic pooled funds and real estate investment trusts but exclude money market funds and bank accounts with no fixed maturity date as these are considered short-term.

Other Treasury Management issues

38 **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).

39 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.

40 Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria, assessed using the appropriate credit rating for derivative exposures. The current value of any amount due from a derivative counterparty will count against the counterparty credit limit and the relevant foreign country limit.

41 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.

42 **Markets in Financial Instruments Directive**: The Council has opted up to professional client status with its providers of financial services allowing it access to a greater range of services but without the greater regulatory protections afforded to individuals and small companies. The Director of Resources believes this to be the most appropriate status.

Appendix C Investment Strategy

1. This Investment Strategy meets the requirements of statutory guidance widening the coverage beyond strict treasury investments. It focuses on the financial support of local public services by lending to or buying shares in other organisations or its own subsidiaries (service investments) and commercial property investment income.

Service Investments: Loans

2. The Council can lend money to local bodies or its subsidiaries to support local public services and stimulate local economic growth. Historically the Council has only lent to local bodies in very limited circumstances where a significant service outcome is expected. At present there is only one loan to a local community run leisure centre for it to develop a specific facility. The original loan was for £300,000 and there is currently £170,000 outstanding.

3. There is no intention to increase the use of loans to local bodies and they are expected to be infrequent. The Council will, however, be lending to a subsidiary in the guise of its housing company. 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 exposure has been set at £4m. This is set to cover the housing company's potential projects. The Council controls its subsidiary so is in a position to determine the level of risk it takes on.

4. 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 will be shown net of this loss allowance. However, the Council makes every reasonable effort to collect the full sum lent and has appropriate credit control arrangements in place to recover overdue repayments.

5. **Risk assessment**: The Council assesses the risk of loss before entering into service loans by assessing the counterparty's resilience, the service users' needs that the loan is designed to help meet and how these will evolve over time. During the life of the loan any change in original assumptions will be monitored. The Council will use external advisors if felt appropriate by the Director of Resources. All loans will be subject to contract agreed by Head of Legal and Democratic Services. All new classes of loans must be approved by full Council and will be monitored by Director of Resources.

Service Investments: Shares

6. The Council does not currently intend to invest in any shares except for in its own housing company where £0.5m has been invested. The overall limit for 2024/25 is £0.5m and no further equity funding is currently planned.

7. **Security:** One of the risks of investing in shares is that they potentially 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 subsidiaries will be set at the lowest practical level if and when exposure is allowed.

8. **Risk assessment:** The Council would assess the risk of loss before entering into and whilst holding shares by going through an extensive process of risk analysis. The risk analysis will include an assessment of the market that the subsidiary will be active in including the nature and level of competition, how the market will evolve over time, the barriers to entry and exit and any ongoing investment requirements. The Council will use external advisors as thought appropriate by Director of Resources.

9. **Liquidity:** Although this type of investment is fundamentally illiquid, in order to limit this the Council, when it sets a limit in this area, will initially set out the maximum periods for which funds may prudently be committed and how the Council will ensure it stays within its stated investment limits. The life of the housing companies has not been explicitly set but the invested equity will be reviewed at a five-year interval.

10. **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 limits above on share investments are therefore also the Council's required upper limits on non-specified investments. 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

11. The Council invests in commercial property within the District in order to make a return that will be spent on local public services. These include retail units, business centres, and healthcare facilities. They contributed £3.7m of income net of direct costs in 2022/23 providing a significant support to the Council's finances.

12. The table below lists the properties by major category and by whether they are 'legacy' properties, which is taken as having been on the Council's books on 31 March 2007, or the acquisitions and developments since then. The reason for the choice of 31 March 2007 is twofold: firstly, this was the date of the

implementation of asset accounting under the international financial reporting standard that required the Council to keep detail records of historic asset values and secondly it separates out the last decade or so when the recent purchases are reported. It is these more recent purchases which were made to provide commercial income to support the Council's budget which are of more concern to CIPFA and its latest guidance. For the recent purchases the cost records are available whereas the Council does not have comprehensive records of actual purchase costs so the 31 March 2007 values are used.

Property by type £millions	**Actual**	**31.3.2023 actual**		**31.3.2024 expected**	
	Purchase cost or 31 March 2007 value	**Gains or losses**	**Value in accounts**	**Gains or losses**	**Value in accounts**
Retail – legacy	2.7	1.9	4.6	1.7	4.4
Retail – Swan Walk	9.5	-7.5	2.0	-7.6	1.9
Light industrial - legacy	9.3	9.9	19.2	9.9	19.2
Healthcare – legacy	6.5	1.6	8.1	1.6	8.1
Office - legacy	1.3	0.6	1.9	0.6	1.9
Retail - recent	14.7	-6.1	8.6	-6.5	8.2
Light industrial – recent	6.3	3.8	10.1	3.8	10.1
Healthcare – recent	0.9	0.0	0.9	0.0	0.9
Education -recent	1.8	-0.1	1.7	-0.1	1.7
Leisure – recent	1.5	-0.6	0.9	-0.6	0.9
Total	**54.5**	**3.5**	**58**	**2.8**	**57.3**

13. In the table above the Swan Walk Centre has been taken out of the legacy retail category as it has a significant effect and has its own distinct history. The major loss in value is due to the movement of the valuation of the Council's equity share in Swan Walk. A true separable purchase price for the Swan Walk equity share is not available as the Swan Walk development was a complex set of multiparty arrangements rather than a simple purchase.

14. The values at year-end are uncertain so no significant movement in values is predicted. Values were recovering well after the pandemic but higher interest rates have in general weighed on property values. The estimates for the end of 2023/24 above assume values broadly hold their value apart from retail, where a weak consumer demand may have an effect, so a reduction of 5% has been applied.

15. **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.

16. The fair value assessment of the Council's investment property portfolio is above the 'purchase' cost which means that the whole portfolio does provide 'security' in terms of the government guidance.

17. The Head of Property and Facilities has considered the prospects for the overall value of the portfolio and bearing in mind it is normal for assets within the portfolio to perform differently depending on market conditions concludes that the best course of action is to hold the assets for the long term as they are sound assets with dependable income streams.

18. The commercial properties are revalued each year-end by an external valuer so should the audited values at the end of 2023/24 fall below their purchase price the Head of Property and Facilities will consider whether the current course of action of holding the assets is appropriate and bring any alternative actions to Council in an update to the Investment Strategy. This is in line with the current government guidance.

19. **Risk assessment:** The Council has no budgeted plans to expand its portfolio in 2024/25 but should there be a change the Council would assess the risk of loss before entering into and whilst holding property investments by :
    - assessing any plans against the CIPFA Code and Government guidance
    - assessing the relevant market including the level of competition, the barriers to entry and exit and future market prospects;
    - using advisors if thought appropriate by the Director of Resources;
    - consulting Policy Development Advisory Groups for Finance & Resources and Local Economy and Place
    - taking final comprehensive report on all new investments to Cabinet
    - continually monitoring risk in the whole portfolio and any specific assets

20. **Liquidity:** Clearly property is relatively difficult to sell at short notice, and can take a considerable period to sell in certain market conditions. To ensure that the invested funds can be accessed when they are needed the Head of Property and Facilities ensures that at least £5m of commercial property could be sold as a going concern within a six-month period.

Loan Commitments and Financial Guarantees

21 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. The Council plans to provide loan commitments up to £4m to its Housing Company subsidiary. It does not plan to provide any guarantees in the near future.

Proportionality

22 The Council is dependent on profit generating investment activity to achieve a balanced revenue budget. The table 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 Strategy. The figures are best estimates bearing in mind the uncertainty due to the challenging economic position. They assume a reasonably robust level of rents, which may be threatened by a prolonged and deep recession.

Proportionality of Investments £m	**2022/23 Actual**	**2023/24 Forecast**	**2024/25 Budget**	**2025/26 Budget**	**2026/27 Budget**
Gross service expenditure	40	43	43	43	43
Investment income	3.7	3.5	3.8	3.8	4.0
Proportion	9%	8%	9%	9%	9%

23 **Capacity, Skills and Culture**

Elected Members and statutory officers: The Council recognises that those elected Members and statutory officers involved in the investments decision making process must have appropriate capacity, skills and information to enable them to:

- take informed decisions as to whether to enter into a specific investment;
- assess individual assessments in the context of the strategic objectives and risk profile of the Council; and
- understand how new decisions have changed the overall risk exposure of the Council.

The Council will ensure that the relevant officers and the Members of Audit Committee and Policy Development Advisory Groups for Finance & Resources, and Local Economy and Place have appropriate skills, providing training and advisor support where there is a skills gap.

24 **Commercial deals:** The Council will ensure that the Audit Committee, Policy Development Advisory Groups for Finance & Resources and Local Economy and Place, Cabinet, and officers negotiating commercial deals are aware of the core principles of the prudential framework and of the regulatory regime within which local authorities operate.

25 **Corporate governance:** Any investment decisions will be scrutinised by Senior Leadership Team, Policy Development Advisory Groups for Finance &

Resources and Local Economy and Place and Cabinet before final approval. The Overview and Scrutiny committee review all decisions made by the Cabinet. Although after the event, the Committee can make any recommendations to the Council if it sees fit.

Investment Indicators

26 The Council has set the following quantitative indicators to allow elected Members and the public to assess its total risk exposure as a result of its investment decisions.

27 **Total risk exposure:** The first indicator shows the total exposure to potential investment losses.

Total investment exposure £m	31.03.2023 Actual	31.03.2024 Forecast	31.03.2025 Forecast
Treasury management investments	75	69	65
Service investments: Loans	0.0	0.0	0.0
Service investments: Shares	0.5	0.5	0.5
Commercial investments: Property	58	57	57
TOTAL INVESTMENTS	133.5	126.5	122.5
Commitments to lend	0	0	0
Guarantees issued on loans	0	0	0
TOTAL EXPOSURE	133.5	126.5	122.5

28 **How investments are funded:** Government guidance is that these indicators should include how investments are funded. Since the Council does not have any borrowing the Council's investments are funded by usable reserves and income received in advance of expenditure.

29 **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.

Investments net rate of return	2022/23 Actual	2023/24 Forecast	2024/25 Forecast
Treasury management investments	2.6%	4.5%	4.5%
Service investments: Loans	0%	0%	0%
Service investments: Shares	0%	0%	0%

Commercial investments: Property	6.4%	6.2%	6.5%
ALL INVESTMENTS	4.2%	5.2%	5.4%

30 **Other indicators:** The Department for Levelling Up, Housing and Communities guidance lists other indicators and the Council has selected the indicators below as appropriate.

Indicator	**2022/23 Actual**	**2023/24 Forecast**	**2024/25 Forecast**
Income net of direct cost return target	6.4%	6.2%	6.5%
Operating overheads of property section attributable to commercial property as a proportion of net property income	6.1%	6%	6%
Average Vacancy levels	4%	3%	3%
Tenant over 5% of net property income	5	5	5
Weighted Average Unexpired Lease Term (WAULT)	14yr	14yr	14yr
Bad debts written off	£82,000	£100,000	£200,000