

Investment Strategy Report 2019/20 (DRAFT)

Cotswold District Council

Introduction

The Authority 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 other organisations (**service investments**), and
- to earn investment income (known as **commercial investments** where this is the main purpose).

This investment strategy is a new report for 2019/20, meeting the requirements of statutory guidance issued by the government in January 2018, and focuses on the second and third of these categories.

Treasury Management Investments

The Authority 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. These activities lead to a cash surplus at various points of the year 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 £34.0m and £23m during the 2019/20 financial year.

Contribution: The contribution that these investments make to the objectives of the Authority is to support effective treasury management activities. *(This sentence may look odd but it is a requirement of the guidance [paragraph 21])*

Further details: Full details of the Authority's policies and its plan for 2019/20 for treasury management investments are covered in a separate document - the treasury management strategy - which is available via the Council's website.

Service Investments: Loans

Contribution: The Council lends money to support local public services and stimulate local economic growth. These include loans to organisations and residents within the district which support the priorities of the Council.

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

Table 1: Loans for service purposes in £

| Category of borrower | 31.3.2018 actual £ | | | 2019/20 |
|--|--------------------|----------------|------------------------|------------------|
| | Balance owing | Loss allowance | Net figure in accounts | Approved Limit |
| Charities | 379,270 | 0 | 379,270 | 457,270 |
| Housing associations | 31,500 | 0 | 31,500 | 31,500 |
| Local Authority Mortgage Scheme (LAMS) | 1,000,000 | 0 | 1,000,000 | 1,000,000 |
| Local residents (equity loans) | 174,288 | 0 | 174,288 | 174,288 |
| Employees (car loans) | 68,973 | 0 | 68,973 | 78,973 |
| TOTAL | 1,654,031 | 0 | 1,654,031 | 1,742,031 |

Accounting standards require the Authority to set aside loss allowance for loans, reflecting the likelihood of non-payment. The loans that the Council has made are limited to specific service areas and the likelihood of non-payment is minimal. There is no history of non-payment and no evidence to suggest that there will be any default against the loans granted. As a result, no allowance for loss has been included against the loan balances. Should any indication be given that there is a risk of default then the risk will be assessed and a provision established at that time. Should a loan default, the Authority will make every reasonable effort to collect the full sum lent and recover any overdue repayments.

In addition to the loans granted the Council has included provision in its Treasury Management Strategy to loan up to £500,000 to both Ubico Limited and Publica Group (Support) Limited, should either company require support. The Council is a shareholder in Ubico and a shared owner in Publica. In both cases, the loan facility is to enable the Council to be able to provide a loan for short-term cash flow purposes.

Risk assessment: The Authority assesses the risk of loss before entering into and whilst holding service loans by undertaking credit checks and ensuring that appropriate legal documentation is in place to secure the Council's money.

The Council also receives independent financial advice on its financial dealings from Arlingclose.

Service Investments: Shares

Contribution: The Council has a £1 shareholding in Ubico Ltd. Ubico Ltd is wholly-owned by seven local authorities and operates as a not for profit enterprise. Ubico Ltd is an environmental services company which provides household and commercial refuse collection, recycling, street cleansing, grounds maintenance and fleet maintenance services to the Council.

Security: One of the risks of investing in shares is that they fall in value meaning that the initial outlay may not be recovered. The Council has no other shareholdings.

Table 2: Shares held for service purposes in £

| Category of company | 31.3.2018 actual £ | | | 2019/20 |
|-------------------------------|--------------------|-----------------|-------------------|----------------|
| | Amounts invested | Gains or losses | Value in accounts | Approved Limit |
| Local authority-owned company | 1 | - | 1 | 1 |
| TOTAL | 1 | - | 1 | 1 |

Risk assessment: the Council has not invested into Ubico to generate a financial return. The Council has invested purely to support service provision. Ubico is a cost sharing company - any surplus generated within Ubico is returned to the partner Councils [shareholders] similarly with any deficit met by the Councils. Through regular budget monitoring and sound financial management by Ubico and transparency within calculation of contract sums, the risk of any financial loss is mitigated.

Liquidity: the Council has not invested into Ubico to generate a financial return. The Council has invested purely to support service provision. The Council has no intention to dispose of its investment in the foreseeable future.

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

Commercial Investments: Property

Investment Property is defined in the CIPFA code of practice on Local Authority Accounting as property (land or buildings, or both) held solely to earn rentals or for capital appreciation, or both. The Council holds a number of assets which it classifies as Investment Properties.

Contribution: The Council owns a number of Investment Properties within the Cotswold district and three significant assets outside of the district, with the intention of generating a revenue income to support the revenue budget.

Table 3: Property held for investment purposes in £

| Property | 01.4.17 | 31.3.2018 actual £ | | 31.3.2019 |
|---|-------------------|--------------------|-------------------|------------------|
| | Value in accounts | Gains or (losses) | Value in accounts | Expected value |
| Investment Property within Cotswold District | 1,185,375 | 40,025 | 1,225,400 | 1,225,400 |
| Investment Property outside of Cotswold District: Superdrug, Worcester | 1,200,000 | 0 | 1,200,000 | 1,200,000 |
| Investment Property outside of Cotswold District Wilkinsons, West Bromwich | 1,600,000 | 0 | 1,600,000 | 1,600,000 |
| Investment Property outside of Cotswold District Tesco, Seaford | 1,018,000 | 0 | 1,018,000 | 1,018,000 |
| Potential Investment Property purchase (within the district) | 0 | 0 | 0 | 2,500,000 |
| TOTAL | 5,003,375 | 40,025 | 5,043,400 | 7,543,400 |

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

A fair value assessment of the Authority's investment property portfolio is made each year as part of the final accounts process. Investment Property is valued at market value.

The fair value of the Authority's investment property portfolio is included in the Statement of Accounts, based upon 'market value'. The Council's Investment Property is held primarily to generate a stable income stream to support the revenue budget. Should a property be sold any profit/loss on disposal will be recognised at that point. The Council has no plans to dispose of any Investment Property in the near future.

Risk assessment: The Council aims to generate a revenue return from its Investment Property assets which is greater than the return generated by its Treasury Management activity. It is understood that the fair value of property will fluctuate. The Authority assesses the risk of movement in asset values before entering into and whilst holding property investments and aims wherever possible to mitigate the risk by purchasing property with secure tenants on long leases.

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. To ensure that the Council has cash funds that can be accessed when they are needed, the Treasury management policy includes the provision of liquid investments should the Council be in need of cash. It is not anticipated that the Council would need to sell any Investment Property at short notice.

Loan Commitments and Financial Guarantees

Although not strictly counted as investments, since no money has exchanged hands yet, loan commitments and financial guarantees carry similar risks to the Authority and are included here for completeness.

The Authority is a shareholder of Ubico Ltd and is a joint partner in Publica Group (Support) Limited (¼ owner). In both cases, should the company overspend the Council would be liable for its share of the additional costs. In both companies, sound financial management and budgetary control mitigate the risk that additional sums will be required without adequate notice.

Proportionality

The Authority is dependent on 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 of the Authority is dependent on achieving the expected income from treasury investments over the lifecycle of the Medium Term Financial Plan. Should it fail to achieve the expected income targets, the Authority will be required to draw additional balances from reserves, or generate savings elsewhere within the budget to continue to provide its services.

Table 4: Proportionality of Investments

| | 2017/18 Actual | 2018/19 Forecast | 2019/20 Budget | 2020/21 Budget | 2021/22 Budget |
|----------------------------|-------------------|---------------------|-------------------|-------------------|-------------------|
| Gross service expenditure* | 25,530,980 | 22,462,000 | 23,264,000 | 23,077,000 | 23,747,000 |
| Investment income | 259,019 | 368,270 | 391,270 | 430,395 | 430,395 |
| Proportion | 1.01% | 1.64% | 1.68% | 1.87% | 1.81% |

* Excluding Housing Benefit payments.

Borrowing in Advance of Need

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. The Authority has plans to borrow in 19/20 to invest in new capital schemes. Any funds borrowed will be in relation to specific schemes and based upon the cash required for the chosen schemes. There are no plans to borrow in advance of need.

Capacity, Skills and Culture

Summary of knowledge and skills available to the authority:

The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. For example, the Chief Finance Officer is a qualified accountant with over 20 years' experience of working in local government finance. The Deputy Chief Finance Officer is also a qualified accountant with 17 years' experience. The Council pays for junior staff to study towards relevant professional qualifications including Chartered Institute of Public Finance and Accountancy (CIPFA), Association of Certified Chartered Accountants (ACCA) and Association of Accounting Technicians.

Where Council staff do not have the knowledge and skills required, use is made of external advisers and consultants that are specialists in their field. The Council currently employs Arlingclose Limited as treasury management advisers. The Council employs other specialist advisers to advise upon specific, extra-ordinary transactions as required. Examples of such transactions include property acquisitions, and loans to third parties. 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.

The Council has experience of investing in commercial property in recent years. The Council's property service is provided through its strategic service provider Publica Group (Support) Ltd. The team of property officers have the following qualifications:

- BSc Hons Real Estate Management
- Associate Member Royal Institute Chartered Surveyors
- Member Royal Institute Chartered Surveyors
- Royal Institute Chartered Surveyors Registered Valuer
- Member institute welfare & facilities management
- Technical member for institute for occupational safety and health
- Member of chartered institute of marketing

The Council's legal team have experience of carrying out due diligence checks, particularly for commercial property acquisitions, and the legal officers have the following qualifications:

- Fellow of the Charter Institute of Legal Executives (FCIlex)
- Associate Member of the Charter Institute of Legal Executives (FCIlex)
- Graduate of the Charter Institute of Legal Executives (FCIlex)
- Para-Legals
- Solicitors

The Property and Legal teams work together with the Finance team to support the Council's Chief Finance Officer and the Publica Finance Director in developing investment proposals for the Council. External specialist advice is obtained when required to support these teams.

The Council has previously invested in a range of commercial properties which are delivering a sustainable revenue stream to the Council. Any further investment in non-treasury management transactions will be set out in this, or future iterations of this strategy.

Scrutiny Arrangements:

The Cabinet will make decisions or make recommendations to full Council on new investments that are not part of Treasury Management Activity.

Financial Performance is reported quarterly to the Council's scrutiny committee and to Cabinet. This will include the financial performance of the Treasury management function and any other revenue generating investments.

Treasury Management performance is reported at half-year and year-end the Council's Audit Committee and to full Council.

The Council's internal audit provider (South West Audit Partnership Ltd) regularly audits the Council's treasury management activity and its processes and procedures for approving investment and performance management. SWAP report to the Council's Audit Committee.

Investment Indicators

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

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

Table 5: Total investment exposure in £

| Total investment exposure | 31.03.2018 Actual | 31.03.2019 Forecast | 31.03.2020 Forecast |
|----------------------------------|----------------------|------------------------|------------------------|
| Treasury management investments | 33,800,000 | 29,885,000 | 24,712,000 |
| Service investments: Loans | 1,654,031 | 1,742,031 | 740,000 |
| Service investments: Shares | 1 | 1 | 1 |
| Commercial investments: Property | 5,043,400 | 7,543,400 | 7,543,400 |
| TOTAL INVESTMENTS | 40,497,432 | 39,170,432 | 32,995,401 |
| Commitments to lend ¹ | 0 | 0 | 0 |
| TOTAL EXPOSURE | 40,497,432 | 39,170,432 | 32,995,401 |

¹ This excludes the potential loan facility offered to Ubico Limited and Publica Group (Support) Limited for cash flow purposes.

How investments are funded: Government guidance is that these indicators should include how investments are funded. The Council's plans for borrowing are limited to a small number of schemes - which are primarily for service delivery - which do not form part of this report. As a result, investments funded by borrowing can be presented as follows:

Table 6: Investments funded by borrowing in £

| Investments funded by borrowing | 31.03.2018 Actual | 31.03.2019 Forecast | 31.03.2020 Forecast |
|----------------------------------|----------------------|------------------------|------------------------|
| Treasury management investments | 0 | 0 | 0 |
| Service investments: Loans | 0 | 0 | 0 |
| Service investments: Shares | 0 | 0 | 0 |
| Commercial investments: Property | 0 | 0 | 0 |
| TOTAL FUNDED BY BORROWING | 0 | 0 | 0 |

Planned borrowing for the coming years is solely investing in services and not any form of investment.

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 | 2017/18 Actual | 2018/19 Forecast | 2019/20 Forecast |
|--|-------------------|---------------------|---------------------|
| Treasury management investments | 0.6% | 1.2% | 1.9% |
| Service investments: Loans | | | |
| Charities ¹ | 2.8% | 2.8% | 3.0% |
| Housing association | 0.0% | 0.0% | 0.0% |
| Local Authority Mortgage Scheme ² | 3.0% | 3.0% | NA |
| Local residents (equity loans) | 0.0% | 0.0% | 0.0% |
| Employees (car loans) | 2.0% | 2.0% | 2.0% |
| Service investments: Shares | 0.0% | 0.0% | 0.0% |
| Commercial investments: Property | 9.9% | 9.9% | 8.9% |

¹ This represents an average return based upon loans ranging from 0% to 3.5%.

² The Local Authority Mortgage Scheme (LAMS) investment will end and be repaid in January 2019.