**Public**

**Agenda Item No 4(d)**

**DERBYSHIRE COUNTY COUNCIL**

**CABINET**

**21 January 2021**

**Report of the Director of Finance & ICT**

# CAPITAL PROGRAMME APPROVALS, TREASURY MANAGEMENT AND CAPITAL STRATEGY

(CORPORATE SERVICES)

## 1 Purpose of the Report

To obtain approval for proposals for submission to Council relating to the capital starts programme for 2021-22 and the Treasury Management, Investment and Capital Strategies.

This report should be read alongside the following reports to this Cabinet Meeting: the Reserves Position Report, the Budget Consultation Results Report for 2021-22 and the Revenue Budget Report 2021-22.

## 2 Information and Analysis

In line with previous years, the proposed new Capital Starts Programme for 2021-22 has been evaluated and it is recommended to proceed with new borrowing of £32.121m (excluding invest to save schemes). The detailed proposals are set out in Appendix One of this report.

The Treasury Management Strategy Report for 2021-22 (Appendix Two) sets out the Council's management of its cash flow, borrowing and investments and the management of its associated risks.

The Investment Strategy Report for 2021-22 (Appendix Three) deals with the management of the Council's balances and reserves, managing the balance between risk and return.

The Capital Strategy (Appendix Four) for 2021-22 provides a high-level overview of how capital expenditure and capital financing contribute to the provision of local public services.

## 3 Considerations

In preparing the report the relevance of the following factors has been considered: financial, legal, human resources, environmental, social value, property and transport.

## 4 Background Papers

Local Government Act 2003; Prudential Code 2017; Treasury Management in the Public Services; Capital Accounting Working Papers.

## 5 Key Decision

No.

## 6 Is it necessary to waive the call-in period?

No.

## 7 Officer's Recommendations

That Cabinet recommends to Council that it:

7.1 Approves the 2021-22 Capital Starts Programme set out in Appendix One;

7.2 adopts the Treasury Management Policy set out in Appendix Two;

7.3 adopts the Investment Strategy set out in Appendix Three; and

7.4 adopts the Capital Strategy set out in Appendix Four.

PETER HANDFORD

Director of Finance & ICT

## CAPITAL PROGRAMME 2021-22

The proposed new starts programme for 2021-22, along with funding streams, as shown in Table 1, has been evaluated and it is recommended to proceed with new borrowing of £32.121m (excluding invest to save schemes). More details on each individual scheme are set out below.

Schemes are usually funded from a combination of Government grants, capital receipts, borrowing, use of reserves and contributions from revenue budgets. Capital receipts are normally used to support the overall programme and have in recent years been in the region of £2-£3m per year. However, with the Council reviewing its approach to property and asset management this has the potential to increase capital receipts and assist with funding of current and future programmes. In cases where a new project is directly dependent on the disposal of an existing asset, for example, the replacement of a school, or where it is a statutory regulation that sales proceeds must be used to improve sports or educational facilities, then the receipt from the disposal of the ‘old’ asset can be earmarked to fund the replacement.

The Capital Programme remains affected by the downward pressure on the Council’s finances. The main limiting factor on the Council’s ability to undertake capital expenditure is whether the revenue resource is available to support in full the implications of capital expenditure, both borrowing costs and running costs, after allowing for any support provided by Government, which is now mainly through capital grants. Because of this, there has been a limit on new borrowing of no more than £15m. However, it is recognised that due to the increasing pressures being placed on school places and infrastructure, borrowing has been increased to ensure that the Council meets its statutory obligations and in turn assists in delivering the Strategic Plan.

The Council will receive estimated Government grants of just under £40m to address key issues in highways and maintenance, develop integrated transport schemes and address the most immediate condition problems in schools. Funding is requested to cover the funding gaps to assist in the building of new schools in response to major housing developments and also schools that have ageing buildings and are high on the buildings at risk register. There are also bids to assist in the refurbishment of Children’s Homes, along with planned refurbishment works at the Council’s Homes for Older People, to address high priority requirements.

To address some of the backlog on other Council properties and reduce the burden on revenue funding of Capital works, a Corporate bid has been submitted as part of a long-term strategy to target the Council’s backlog.

As in previous years, and in line with the Council's ICT Strategy, a full capital replacement programme is being developed, to ensure that all capital related ICT hardware and software will be replaced over a five-year cycle. This envisaged borrowing of £2m per year, however, due to the significant infrastructure upgrades required for 2021-22, partly due to end of life equipment, this will mean that bids for future years will be less than the £2m originally envisaged, to enable the overall plan to remain within the allocated five year plan of £10m.

**Table 1 Capital Programme Bids 2021-22**

**Funding Streams**

| | Grant | Council Reserves | Borrowing | Invest to Save | Total |
|---|---|---|---|---|---|
| | £m | £m | £m | £m | £m |
| **Children's Services** | | | | | |
| Basic Need | 2.000 | | | | 2.000 |
| Harrington Junior School | 1.284 | 1.000 | 3.216 | | 5.500 |
| Brampton Primary - Modernisation | | | 1.750 | | 1.750 |
| Childrens Home Capital Improvements | | | 0.250 | | 0.250 |
| School Condition Allowance | 7.153 | | | | 7.153 |
| Bramley Vale Primary School | | | 5.500 | | 5.500 |
| Children's Home Refurbishment | | | 2.740 | | 2.740 |
| Mickley Infant School | | | 1.250 | | 1.250 |
| | | | | | |
| **Adult Social Care & Health** | | | | | |
| Disabled Facilities Grant Adaptations | 6.960 | | 4.000 | | 10.960 |
| HOPS Planned Programme | | | 1.410 | | 1.410 |
| | | | | | |
| **Communities, Commissioning and Policy** | | | | | |
| Oil Storage and Distribution | | | 0.800 | | 0.800 |
| Kitchen Ventilation Schemes | | | 1.400 | | 1.400 |
| Corporate Buildings CIP | | | 2.000 | | 2.000 |
| Replacement of ICT Hardware | | | 3.220 | | 3.220 |
| Risk Mitigation Measures | | | 0.130 | | 0.130 |
| | | | | | |
| **Environment, Transport and Economy** | | | | | |
| Glossop HWTS | | | 3.285 | | 3.285 |
| Closed Landfill Replacement Programme | | | 0.165 | | 0.165 |
| Derelict Land and Reclamation | 0.377 | | 0.120 | | 0.497 |
| Elvaston Castle Drive Lodge | | | | 0.350 | 0.350 |
| Elvaston Castle Operational Compound | | | 0.700 | | 0.700 |
| Loscoe Closed Landfill Infrastructure Improvements | | | 0.185 | | 0.185 |
| Local Transport Plan | 22.098 | | | | 22.098 |
| **TOTAL** | **39.872** | **1.000** | **32.121** | **0.350** | **73.343** |

## Summary of Individual Schemes

## Childrens Services

### Basic Need £2.000m

The Department for Education (DfE) grant allocation for Basic Need schemes is to provide additional school places in areas of population growth. Feasibility studies have been undertaken, based on an analysis of pupil projections. Funding will be allocated from a priority list of potential projects once a grant figure is known.

### Harrington Junior School £5.500m

Harrington Junior School suffered a major fire in May 2020 which destroyed the main building, leaving only a two-classroom block and an old one classroom temporary block. The new school, unlike the old school which was built in the 1970s and was not fitted with any sprinklers, will be built to modern standards of insulation and energy efficiencies, which will result in potential revenue savings. The project is partially funded under an insurance claim and through the risk management budget, however, the £3.216m shortfall is to be covered by the Council.

### Brampton Primary £1.750m

The £1.750m scheme is to replace a building at risk and re-use former Children's Centre accommodation. There are significant condition issues with the building, in particular the roof, which is currently being propped. The proposed scheme offers extensive benefits at significantly less cost than a like for like replacement - doubling the nursery places to allow local need for 30 hours to be met, creating a coherent Enhanced Resource Schools (ERS) unit, relocating the kitchen into the main building removing health and safety issues, and providing a playing field which the school currently lacks, as well as avoiding the potential DfE claw-back of £0.156m if the children's centre building is not used for children under 5 years old.

### Childrens Home Capital Improvements £0.250m

The Council is a Corporate Parent to children in care and is required to provide suitable and homely accommodation for children in the Council's Children's Homes. The Homes are subject to inspection by Ofsted and should the accommodation not meet the quality standards, there is a risk of the Homes failing inspection and even closing, which would be disruptive to the young people living there. The money is to fund improvements to both the Council's Children's Homes and Disabled Children's Centres to meet the Council's duty to maintain the Homes and Centres to the standards required by Ofsted.

## School Condition Allowance £7.153m

DfE Grant funding to cover the cost of upgrading and maintaining the condition of school accommodation to suit the needs of education in Derbyshire. School Condition Allowance allows for only the most serious condition related issues to be addressed given that the Council has a backlog of school condition expenditure of £150m. Projects funded on school buildings where the condition is poor, include re-roofing, replacement windows and doors, re-heating and re-wiring. A priority list of potential projects will be finalised once the actual grant figure is known.

## Bramley Vale Primary School £5.500m

The project at Bramley Vale Primary School is for the replacement of all of the school, with the exception of the Foundation Unit and a single block. The main school has been at the top of the Buildings at Risk register for many years and has a condition backlog of £1.1m. The project would be carried out in phases, to allow the school to be rebuilt on its current site, whilst remaining open, to limit disruption to the pupils. The school is at the heart of its small community and it would provide buildings that meet current standards and enhance the education of its pupils.

## Children’s Home Refurbishment £2.740m

The Council has a legal obligation to provide children's home accommodation which is fully compliant to current statutory requirements. Residential accommodation with sleeping accommodation is the highest risk category of accommodation. Refurbishment works are required at four children’s homes, in order to bring them up to current standards, with sprinklers being installed in two homes. The four homes are Spring Cottage Grinlow, Glenholme, Fairview and Solomon House Buxton. The scope of works for each home has been defined as the result of feasibility studies in 2019-20. The works are programmed to take place on site between June 2021 and February 2024. The homes will be vacated in turn to allow the works to take place. The projects are planned to be undertaken consecutively, in order to minimise the requirements for alternative accommodation.

## Mickley Infant School £1.250m

Consultation is currently underway to consider the conversion of Mickley Infant School into a primary school. There is considerable parental support for the proposal in this isolated community where access to public transport is limited and unreliable. Parents currently have difficulty ensuring that their key stage 2 children can travel to the nearest primary school, particularly if they have children at both the Infant and Primary schools. This project is to build two classrooms, toilets, a staffroom and library, that would allow the delivery of education to all nursery and primary aged children on the one site, which is within walking distance of the estate on which the school is based. The projections for Mickley Infant School and the primaries in the area indicate that the conversion of the Infant school would not have any effect on the surrounding schools.

## Adult Social Care and Health

### Disabled Facilities Grant £10.960m

Disabled people requiring major adaptations to their accommodation are able to apply for a Disabled Facilities Grant (DFG) administered by District Councils. The DFG is mandatory if the applicant is unable to access essential facilities within their home. The County Council has a duty to identify suitable works based upon an assessment of individual needs: however, the decision to approve the grant lies with the relevant District Council.

The DFG process is prescribed by legislation and regulations and requires that applicants are subject to a Test of Resources (means test). The Test of Resources only looks at an applicant's income and does not take account of their outgoings or personal circumstances. There are three possible outcomes for applicants: a grant to cover the cost of the work (up to a maximum of £30,000), a grant to cover part of the work, or the grant application is deemed to be able to meet all the costs of the work.

The decision on DFG funding is the responsibility of the relevant District Council. However, the County Council, as part of its legal duties under the Chronically Sick and Disabled Peoples Act 1970, is required to consider providing financial assistance where the applicant cannot meet some or all of the cost of the adaptation.

### HOPS Planned Programme £1.410m

The Council has a statutory duty to maintain Homes for Older People (HOPS) to provide a safe environment. A programme of planned maintenance and refurbishment works is required to maintain HOPS in a safe and secure condition. This programme is intended to ensure that for two years the buildings will be secure and watertight; will have compliant fire alarm and detection; compliant kitchen ventilation; fully functional hot water and heating systems; and all external areas will be made safe with the removal of trip hazards and so on.

If it is intended to extend the use of these buildings beyond two years, then this will require a re-wire and major refurbishment. Therefore, in parallel with this programme of essential work, it is also necessary to also undertake feasibility studies (funded by revenue) to assess budget costs. A subsequent capital strategy bid will be required in 12 months to secure the necessary funding for the additional major refurbishments as necessary. The budget cost of 7 refurbishments is likely to be approximately £30m. The total of this programme of works is for £3.410m however £2.000m is currently being utilised from a previous year's approved allocation.

**Commissioning, Communities and Policy**

**Oil Storage and Distribution £0.800m**

Funding is required to replace oil storage and pipework distribution systems across a range of corporate and school buildings across the County.

The Council has a legal duty to ensure the safety of staff occupying corporate buildings, together with staff and pupils occupying local authority school buildings. There is also a duty on the Council to ensure it meets its statutory responsibility in complying with The Control of Pollution (Oil Storage) (England) Regulations 2001. Funding pressures and limited availability of parts and equipment, coupled with deteriorating and aged oil storage systems, have contributed to increased defects and risk of system failure, leading to potential leakage and ground contamination.

The risk to the Council is deemed high due to the high likelihood of an oil spillage or leakage leading to the polluting of environmental waterways, drainage and sewer systems, with the presence of open drains and gullies in close proximity of the storage facility.

It is envisaged that this will result in the replacement of out of date equipment across all sites and the introduction of additional equipment or an alternative fuel source, to provide greater monitoring and safety controls at each site and provide greater resilience in performance of the systems.

An estimated cost of £0.800m has been determined for the proposed works based on the knowledge of Property professionals; however, detailed costs will be developed as part of the specialist report and the individual items of work of which may require phasing.

**Kitchen Ventilation Schemes £1.400m**

Funding is required to replace kitchen ventilation and extraction systems across a range of corporate and school buildings across the County. The systems are past the end of their useful life and difficulties are occurring in maintaining, managing and monitoring the systems to provide robust and safe ventilation systems to the respective buildings.

Funding is required to ensure that the Council meets its statutory responsibilities to The Gas (installation & use) Regulations 1998.

The risk to the Council is deemed high due to the high likelihood of system failure, leading to risk to staff and the closure of kitchens providing meals to vulnerable adults and children, which could in turn lead to increased costs to the Council by transporting meals from alternative locations.

Detailed surveys are required to inform and become the basis of a new priority-based strategy for ventilation and extraction systems across the County.

It is envisaged that this will result in the replacement of out of date equipment across all sites and the introduction of additional equipment or an alternative delivery system to provide greater monitoring.

An initial estimated cost of £5.600m has been determined for the proposed works based on the knowledge of Property professionals; however, until detailed costs have been developed as part of a specialist report, funding for the first phase will be required of £1.400m.

**Corporate Buildings Capital Investment Programme £2.000m**

The Council's quinquennial (every five years) building condition surveys have highlighted significant building improvements that require redress to ensure the continued use of buildings and safety to building occupants and members of the public.  The Corporate Building Capital Investment Programme has been developed to reduce the burden placed upon the Corporate Maintenance Budget which covers both reactive maintenance and repairs and funds the Planned Maintenance Programme for Capital works.

The Planned Maintenance Programme has only been able to fund a limited amount of the highest priority work.  In the meantime, the reactive day to day maintenance has had stringent emergency-only repairs applied as the budget is insufficient to meet demand.  The Corporate Building Capital Investment Programme is designed to target essential capital improvements to address building suitability and condition in line with the Asset Management Framework.

The Planned Maintenance Programme can only address the highest priority works identified from condition surveys and is deemed insufficient. The future vision of this strategy is to identify a long-term capital investment strategy for the Council's Corporate Building and to incorporate preventative work through capital investment, which in turn will reduce the Council's maintenance liabilities and reduce the Council's maintenance deficit.

**Replacement of ICT Hardware £3.220m**

The ICT Service maintains a 5-year plan which details the desktop equipment and other major ICT infrastructure components that need replacing.  This includes users’ laptops and PCs, components and utilities that support the Data Centre and Converged Infrastructure, Core Virtual Switching System

(VSS) Network and Network Cabinet replacement, to maintain a physically secure network.

Laptops and PCs are replaced on a 5-year cycle, to ensure they are capable of running the latest software and meet the demands of service users. All other components are centralised and represent critical elements of the Council's ICT Infrastructure. The ICT infrastructure underpins the delivery of front line services through the direct provision of ICT, such as IT equipment and connectivity in libraries and the ICT backbone to support large systems for practitioners, such as the Adult Care and Children Services case management system and the SAP platform that provides the Council's core financial systems.

SAP has recently announced that after 31 December 2027 support for all its systems used by the Council will expire, although it has committed to consider to support these systems beyond that date for a further three year period at an additional support cost premium. This funding will allow the SAP system to operate in a manner that is consistent and supportive of the Council s ICT Strategy and upgrade its core business systems (SAP) to SAP Intelligent suite. In addition, DCC’s current SAP systems are hosted in the Data Centre at County Hall. Support for the current database (DB) and operating system (OS) expire in 2022 and 2023 respectively. This means that all the systems would need to be migrated to the latest versions of the Microsoft OS and DB. This upgrade is complex and is likely to take approximately 42 weeks, with involvement from across the ICT and SAP support community.

The Council also relies heavily on its own data centre ICT hardware infrastructure and services and has identified a range of major infrastructure components that will need replacing over the next five years.

**Risk Mitigation Measures £0.130m**

To provide funding that will actively reduce risk and to increase the understanding of risk across all departments within the Council and therefore provide a long term cost saving by reducing the risk of injury; improve staff absence following incidents; reduce the risk of damage to our properties; assist with risk related improvements that impact upon Adult Care and Childrens homes that impact upon their classification; support risk reduction methodologies that will minimise reputational damage to Derbyshire and therefore support visitor growth.

## Economy, Transport and Environment

### Glossop Household Waste Transfer Station £3.285m

Redevelopment of the Glossop Household Waste Recycling Centre (HWRC) and Transfer Station. The waste transfer station is currently being demolished due to its unsafe structure. The land vacated by the demolished transfer station creates an area of land within the HWRC that is a health and safety hazard to the public and staff. The Transfer Station receives residual household waste from High Peak Borough Council, which is then disposed of by the County Council under its waste disposal duties. The HWRC receives household waste from householders in the northern half of the High Peak borough.

This bid relates to two phases. The first phase seeks funding of £0.385m to reinstate the transfer station land, drainage and landscape to ensure that it is operating in a safe and lawful manner, which will enable legal compliance with the Environment Permit so that the HWRC can remain open. The second phase of this bid for £2.900m, following a full technical review of the need for a transfer station in 2021, proposes the development and construction of suitable transfer station facilities at this site, along with modifications to the household waste recycling centre.

**Closed Landfill Replacement Programme £0.165m**

Following the replacement of six flares in 2018, the Council now has five gas flares that are out of the recommended 10-year replacement programme, with their ages ranging from 10 years to 30 years. A Programme (prioritisation list) for the replacement has been developed, taking account of age, condition and local environment. By experience it has proved necessary to replace the flares every nine or ten years as parts become unavailable, general wear and tear take its toll and they become “old” technology.

Prior to the capital investment in 2018 to replace six flares, no flares have been replaced since 2010-11. This has had an impact on the service, as the flares have broken down more frequently, which has necessitated a slight increase in expenditure on maintenance and more Technician time to carry out repairs. This has been managed within the Service but is not sustainable, so a replacement programme now needs to be put in place and investment made. The typical cost of replacement per flare is £0.033m.

**Derelict Land and Reclamation £0.497m**

Funding for the land reclamation programme is predominantly provided through capital grants secured from a variety of external funding organisations, with the Council providing some pump-prime investment. The funding may be used to match other funding from outside bodies and will continue to do so with further bids, working together with the Countryside team. It also assists with early scheme development on proposed works. The funding is also required to enable the Council to meet statutory obligations on land in its ownership, particularly around physical and environmental work on mines, tips and quarries to deal with hazards and contamination. The work on Chesterfield Canal also supports many hours of volunteer time through partnership working and the Memorandum of Understanding which, together with significant capital investment from the Chesterfield Canal Trust, all contributes to the ongoing restoration programme.

**Elvaston Castle Drive Lodge £0.350m**

Drive Lodge is a residential property on the edge of Elvaston Castle Country Park, directly adjacent to the area used for weddings and inside what would once have been the natural boundary of the estate. The property is likely to come onto the market very soon. The acquisition of the land currently forming the garden of the property would facilitate improved access to the Nursery garden/Old English Garden and bothy buildings which currently presents difficulties with access for wedding related deliveries and so on. Once the property has been acquired and the land that is required for the access has been sectioned off, an "invest to save" options appraisal/business case will be developed to identify whether the residential property should be sold; renovated then sold; or renovated and kept for income generation purposes.

**Elvaston Castle Operational Compound £0.700m**

To facilitate the conversion of the Coach House and Clock Tower range at Elvaston, part of a planned major project bid to regenerate the historic core buildings at Elvaston Castle to create a Visitor Hub, staff will need to be relocated from this building to a new operational/staff base to include storage facilities. The major bid includes the creation of retail, catering, hospitality, office and workshop facilities in repaired historic buildings which will, when converted, generate revenue for further repairs and operational costs towards providing a sustainable future for Elvaston Castle and Country Park. As repairs are completed and buildings appropriately converted, revenue streams will develop and allow the phased transfer of the estate from the Council to Elvaston Castle & Gardens Trust, thus relieving the Council of repair and operational costs of up to £0.900m per annum.

**Loscoe Closed Landfill Infrastructure Improvements £0.185m**

There is a need to upgrade the gas extraction system in 2021 to ensure that the site remains well managed and safe, noting that there is an active business on the site, the pubic have access to the site and there are many properties that sit on the boundary to this site. The Council has a health and safety duty to keep people safe and it is therefore essential that the Council extracts the landfill gas from the ground efficiently to minimise the risk of explosion.

This bid is to upgrade a number of the gas extraction wells and replace the gas flare on the site. This will ensure legal compliance with environmental legislation, notably the Environment Act 1995 (Section 57) and the Landfill Regulations (England and Wales) 2002, made under the Pollution Prevention Control Act 1999. The Council also has an obligation to ensure best practice through a series of Waste Management Papers (WMP) i.e. WMP27 Landfill Gas (1989 and 1991) and Environment Agency Guidance.

**Local Transport Plan £22.098m**

The Local Transport Plan capital programme supports a number of Council plan priorities, but is fundamental to the maintenance of the highway, towards which the majorly of the available capital funding is dedicated. The programme also supports preparation and local contributions towards major projects including the A61 Growth Corridor, a programme of road safety and traffic management engineering schemes, and others to provide infrastructure, encouraging the use of public transport, walking and cycling.

**Appendix Two**

# Treasury Management Strategy Report 2021-22

## 1) Introduction

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 is therefore central to the Council's prudent financial management.

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 2017 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.

Investments held for service purposes or for commercial profit are considered in the Investment Strategy (Appendix Three).

## 2) External Context

**Economic background:** The impact on the UK of the Covid-19 pandemic and the UK's exit from the European Union (EU), together with its trading arrangements, will continue to be a major influence on the Council's Treasury Management Strategy for 2021-22.

The Bank of England (BoE) maintained its Bank Rate at 0.1% in November 2020 and extended its Quantitative Easing (QE) programme by £150 billion, to £895 billion. The Monetary Policy Committee voted unanimously for both, but no mention was made of the potential future use of negative interest rates. Within the latest forecasts, the BoE expects the UK economy to contract by 2% in the last quarter of 2020, before growing by over 7% in 2021. The BoE also forecasts that the economy will now take until the first quarter of 2022 to reach its pre-pandemic level.

UK Consumer Price Inflation (CPI) was 0.5% year on year in September 2020, up from 0.2% in the previous month. In the three months to August 2020, the unemployment rate increased to 4.5%, whilst wages fell 0.8% for total pay in real terms (0.1% increase for regular pay).

UK Gross Domestic Product (GDP) growth decreased by -19.8% in the second quarter of 2020, with the annual rate falling by -21.5%. Monthly GDP estimates have shown the economy is recovering but remains well below its pre-Covid-19 pandemic peak.

Growth in Europe increased by 12.7% in Q3 2020 after contracting by -11.8% in Q2. Headline inflation remains extremely weak, registering -0.3% year-on-year in October 2020. The European Central Bank (ECB) is expected to continue holding its main interest rate at 0% and deposit facility rate at -0.5% for some time, with further monetary stimulus expected later in 2020.

The US economy contracted at an annualised rate of 31.7% in Q2 2020 and then rebounded by 33.1% in Q3. The Federal Reserve (Fed) maintained the Fed Funds rate at between 0% and 0.25%. The Fed also provided strong indications that interest rates are unlikely to change over the next three years from current levels.

**Credit outlook:** The UK's credit rating was downgraded in late March 2020, as a result of the Covid-19 pandemic. This led to a downgrade of individual UK banking institutions.

**Interest rate forecast:** The Council's Treasury Management Adviser, Arlingclose, is forecasting that BoE Bank Rate will remain at 0.1% until at least the end of 2023. It is thought that this forecast could potentially prove to be higher than the actual (known as downside risk), as the BoE and UK Government continue to react to the Covid-19 pandemic and the Brexit transition period ends. The BoE extended its asset purchase programme to £895 billion in November, whilst not changing the Bank Rate. However, further interest rate cuts to zero, or possibly negative, cannot yet be ruled out. Gilt yields are expected to remain very low in the medium-term, whilst short-term yields are likely remain below, or at zero, until such time as the BoE expressly rules out the chance of negative interest rates or growth and/or inflation prospects improve.

A more detailed economic and interest rate forecast provided by Arlingclose is attached at Appendix A.

For the purpose of setting the budget, it has been assumed that new treasury investments will be made at an average rate of 0.25%, and that new long-term loans will be borrowed at an average rate of 1.50%, based upon an average term of 18 years.

### 3) Local Context

On 31 December 2020, the Council held £487.778m of borrowing and £340.746m 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**

| | 31.3.20 Actual £m | 31.3.21 Forecast £m | 31.3.22 Forecast £m | 31.3.23 Forecast £m | 31.3.24 Forecast £m |
|---|---|---|---|---|---|
| General Fund CFR | 525.169 | 572.709 | 642.699 | 679.939 | 688.939 |
| Less: Other debt liabilities* | -68.879 | -64.548 | -59.981 | - 62.186 | -56.532 |
| **Loans CFR** | **456.290** | **508.161** | **582.718** | **617.753** | **632.407** |
| Less: External borrowing** | -329.974 | -378.899 | -287.899 | -265.579 | -259.174 |
| **Internal borrowing** | **126.316** | **129.262** | **294.819** | **352.174** | **373.233** |
| Less: Usable reserves | -305.525 | -244.032 | -191.462 | -156.603 | -149.213 |
| Less: Working capital | -47.671 | -47.671 | -47.671 | -47.671 | -47.671 |
| **New borrowing (or Treasury investments)** | **-226.880** | **-162.441** | **55.686** | **147.900** | **176.349** |

* finance leases, PFI liabilities and transferred debt that form part of the Council's total debt. The new accounting standard IFRS 16 Leases is due to be adopted in 2022-23. The liabilities relating to leases which were previously treated as operating leases will be recognised on the Council's balance sheet. An estimate has been made of the impact of this change and included in the balance sheet summary and forecast. This change increases the General Fund CFR and other debt liabilities by an equal amount, therefore Loans CFR is unaffected.

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

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

The Council has an increasing CFR as a result of its capital programme.

Investments are forecast to fall to £162.441m by March 2021 as the Council's use of internal borrowing to fund capital expenditure increases and after that new borrowing is required.

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 2021-22.

**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.

**Table 2: Liability benchmark**

| | **31.3.20 Actual £m** | **31.3.21 Estimate £m** | **31.3.22 Forecast £m** | **31.3.23 Forecast £m** | **31.3.24 Forecast £m** |
|---|---|---|---|---|---|
| Loans CFR | 456.290 | 508.161 | 582.718 | 617.753 | 632.407 |
| Less: Usable reserves | -305.525 | -244.032 | -191.462 | -156.603 | -149.213 |
| Less: Working capital | -47.671 | -47.671 | -47.671 | - 47.671 | -47.671 |
| Plus: Minimum investments | 10.000 | 10.000 | 10.000 | 10.000 | 10.000 |
| **Liability benchmark** | **113.094** | **226.458** | **353.585** | **423.479** | **445.523** |

Following on from the medium-term forecasts in Table 1 above, the long-term liability benchmark assumes capital expenditure funded by borrowing of £55.686m in 2021-22, £92.214m in 2022-23 and £28.449m in 2023.24. In reality, there is likely to be some slippage of the capital programme. Minimum revenue provision on new capital expenditure based on a 40-year asset life and income, expenditure and reserves all increasing by inflation of 2.5% a year.

## 4) Borrowing Strategy

The Council currently holds £378.899m of loans, an increase of £48.925m on the previous year, as part of its long term strategy for funding previous years' capital programmes and short term operational cash-flow management. The balance sheet forecast in Table 1 shows that the Council expects to borrow up to £55.686m in 2021-22. The Council may however borrow to pre-fund future years' requirements, providing this does not exceed the authorised limit for borrowing of £707.000m (General Fund CFR £642.699m x 110%).

**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.

**Strategy:** Given the continued uncertainty of future 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 in the short-term to either use internal resources, or to borrow short-term loans instead.
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 and short-term 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 2021-22 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.

The Council has previously raised the majority of its long-term borrowing from the Public Works Loan Board (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 HM Treasury's PWLB lending facility.

Alternatively, the Council may arrange forward starting loans during 2021-22, 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.

In addition, the Council may borrow further short-term loans to cover unplanned cash flow shortages.

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

- HM Treasury's PWLB lending facility (formerly the Public Loans Works Board, or PWLB);
- 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 Pension Fund);
- capital market bond investors;
- UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues; and
- D2N2 Local Economic Partnership

**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.

**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 Cabinet.

**LOBOs:** The Council holds £5m of LOBO (Lender's Option Borrower's Option) loans where the lender has the option to propose an increase in the interest rate at set dates, following which the Council has the option to either accept the new rate or to repay the loan at no additional cost. £5m of these LOBOs have options during 2021-22, and although the Council understands that lenders are unlikely to exercise their options in the current low interest rate environment, there remains an element of refinancing risk. The Council will take the option to repay LOBO loans at no cost if it has the opportunity to do so. Total borrowing via LOBO loans will be limited to £5m.

**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).

**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.

## 5) Treasury Investment Strategy

The Council holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past twelve months, the Council's investment balance has ranged between £233.726m and £427.536m and similar levels are expected to be maintained in the forthcoming year.

**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. 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.

**Negative interest rates:** The Covid-19 pandemic has increased the risk that the Bank of England will set its Bank Rate at or below zero, which is likely to feed through to negative interest rates on all low risk, short-term investment options. Since investments cannot pay negative income, negative rates would be applied by reducing the value of investments. In this event, security will be measured as receiving the contractually agreed amount at maturity, even though this may be less than the amount originally invested.

**Strategy:** Given the increasing risk and very low returns from short-term unsecured bank investments, the Council has diversified into higher yielding asset classes, with £70m currently invested in strategic pooled investments. This diversification will represent a continuation of this strategy first adopted in 2015-16.

The majority of the Council's surplus cash is currently invested in Local Authority loans, short-term unsecured bank deposits and money market funds.

**Business models:** Under the 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.

**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 (County Fund)**

| **Sector** | **Time Limit** | **Counterparty Limit** | **Sector Limit** |
|---|---|---|---|
| UK Government | 50 years | Unlimited | n/a |
| Local Authorities & Other Gov't Bodies | 25 years | £30m | Unlimited |
| Secured investments * | 25 years | £30m | Unlimited |
| Banks (unsecured) * | 13 months | £30m | Unlimited |
| Building societies (unsecured) * | 13 months | £30m | £50 million |
| Registered providers (Unsecured) * | 5 years | £10m | £50 million |
| Money market funds * | n/a | £30m | Unlimited |
| Strategic pooled funds | n/a | £30m | £100 million |
| Real estate investment trusts | n/a | £10m | £50 million |
| Other investments | Individual | Cabinet | Approval |

**County Fund**: It is requested that the limit for the Council's main operation bank (currently Lloyds) of £60 million is maintained (£30m overnight only and £30m up to 13 months in duration).

**D2N2**: It is requested the overnight limit of £10m (currently Lloyds) is maintained.

**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.

**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 generally a lower risk of insolvency, although they are not zero risk. Investments with the UK Central 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.

**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.

**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.

**Registered providers (unsecured):** Loans and bonds issued by, guaranteed by or secured on the assets of registered providers of social housing and registered social landlords, formerly known as housing associations. These bodies are regulated by the Regulator of Social Housing (in England). As providers of public services, they retain the likelihood of receiving government support if needed.

**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.

**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.

**Real Estate Investment Trusts (REITs):** 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.

**Other:** This category covers non-treasury investments. Loans to unrated companies will only be made following appropriate due diligence which may include an external credit assessment. Cabinet will consider approval on an individual case by case basis.

**Operational bank accounts:** The Council may incur operational exposures, for example though 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. BoE 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.

**Risk assessment and credit ratings**: Credit ratings are obtained and monitored by the Council's Treasury Management Adviser, who will notify changes in ratings as they occur. Where an entity has its credit rating downgraded so that it fails to meet the minimum 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.

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 minimum 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.

**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.

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 or with other Local Authorities. This will cause investment returns to fall but will protect the principal sum invested.

**Investment limits (County Fund)**: The Council's Total Useable Reserves available to cover investment losses are forecast to be £244.032m at 31 March 2021. In order to minimise risk in the case of a single default, the maximum that will be lent to any one organisation (other than the UK Government or Lloyds Bank (operational bank accounts)) will be £30 million and capitalised interest. A group of banks under the same ownership will be treated as a single organisation for limit purposes.

Credit risk exposures arising from non-treasury investments, financial derivatives and balances in operational bank accounts greater than £30 million count against the relevant investment limits.

Limits will also be placed on fund managers, investments in brokers' nominee accounts, foreign countries and industry sectors 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 | £30 million per manager |
| Negotiable instruments held in a broker's nominee account | £100 million per broker |
| Foreign countries | £30m per country |

**Liquidity management**: The Council uses purpose-built cash flow forecasting software and Excel spreadsheets 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.

## 6) Treasury Management Indicators

The Council measures and manages its exposures to Treasury Management risks using the following indicators.

**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. Unrated investments are assigned a score based on their perceived risk.

| Credit risk indicator | Target |
|---|---|
| Portfolio average credit rating | A |

**Liquidity (Option 1): –** 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 | Target |
|---|---|
| County Fund:<br>Total cash available within 1 month | £10m |

**Liquidity (Option 2) –:** The Council has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount it can borrow each quarter without giving prior notice.

| Liquidity risk indicator | Target |
|---|---|
| County Fund:<br>Total sum borrowed in past 3 months without prior notice | £30m |

The County Fund can use either Liquidity risk indicator (Option 1 or Option 2) as appropriate.

**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 |
|---|---|
| Upper limit on one-year revenue impact of a 1% <u>rise</u> in interest rates | £-3.00m |
| Upper limit on one-year revenue impact of a 1% <u>fall</u> in interest rates | £3.00m |

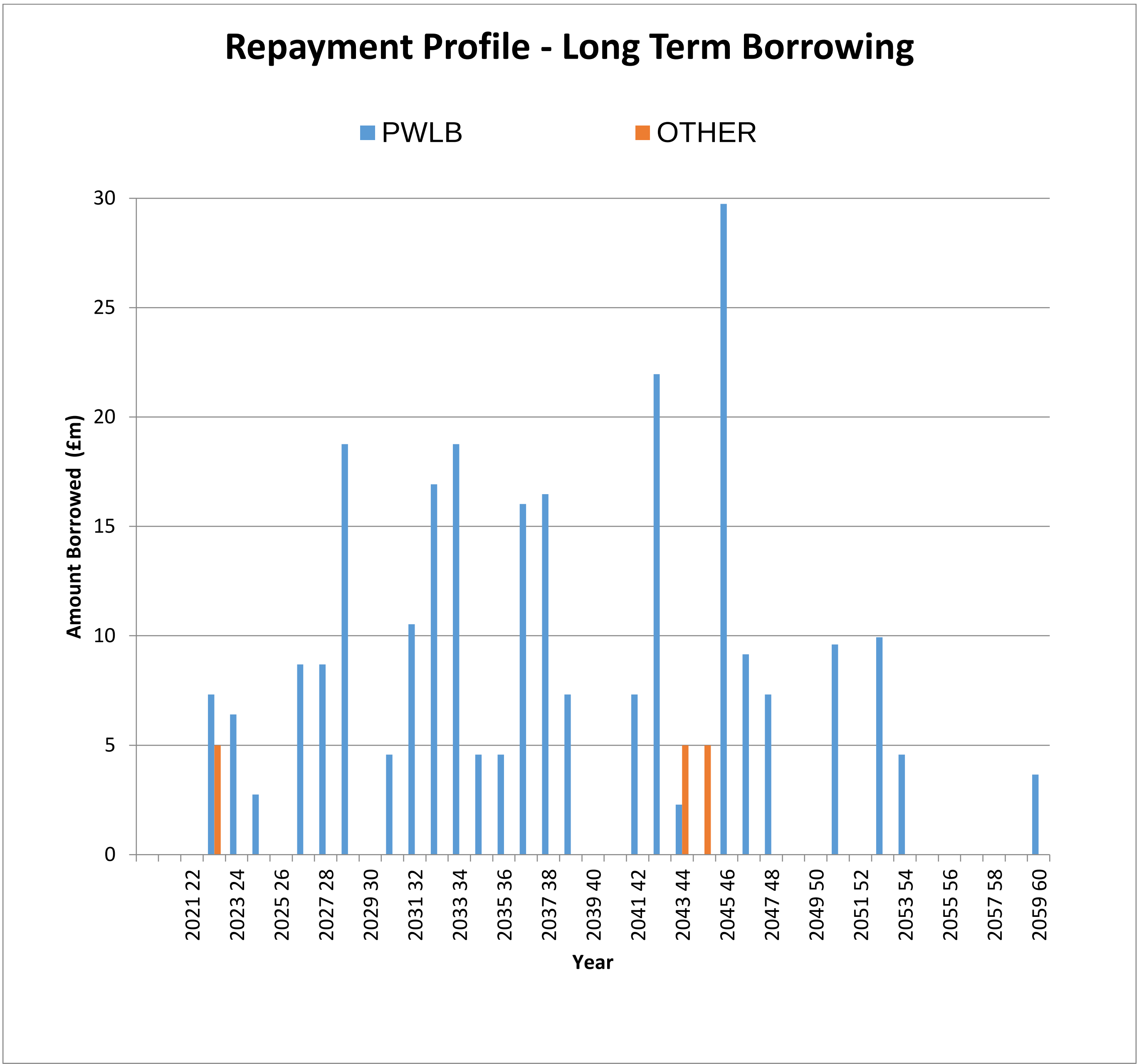
**Maturity structure of borrowing:** This indicator is set to control the Council's exposure to refinancing risk. The upper and lower limits on the maturity structure of borrowing will be:

| Refinancing rate risk indicator | Upper limit | Lower limit |
|---|---|---|
| Under 12 months | 60% | 0% |

| | | |
|---|---|---|
| 12 months and within 24 months | 20% | 0% |
| 24 months and within 5 years | 20% | 0% |
| 5 years and within 10 years | 20% | 0% |
| 10 years and within 20 years | 40% | 10% |
| 20 years and within 30 years | 40% | 10% |
| 30 years and above | 40% | 0% |

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. It should be noted that the LOBO option dates are potential repayment dates.

The Council's long term maturity repayment profile at 31 March 2021 is shown below. A good spread of maturities is desirable. The average redemption is £6.997m per year over the next 39 years. The maximum redemption is £29.738m in 2045-46. The average duration of all the Council's loans is approximately 18 years. Any new borrowing would be targeted for maturity in years with nil/low repayments.




**Principal sums invested for periods longer than a year:** 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 limits on the long-term principal sum invested to final maturities beyond the period end will be:

| Price risk indicator | 2021-22 | 2022-23 | 2023-24 |
|---|---|---|---|
| Limit on principal invested beyond each year end (including strategic pooled funds & non-treasury investments) | £150m | £125m | £100m |

**Related Matters**

The CIPFA Code requires the Council to include the following in its Treasury Management Strategy.

**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).

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.

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 will count against the counterparty credit limit and the relevant foreign country limit.

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.

**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 Director of Finance & ICT believes this to be the most appropriate status.

**Financial Implications**

The budget for investment income in 2021-22 is £4.016m, based on an average investment portfolio of £300m at an interest rate of 1.34%. The budget for long term external borrowing in 2021-22 is £12.292m, based on an average debt portfolio of £272.899m at an average interest rate of 4.50%. 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

The CIPFA Code does not prescribe any particular treasury management strategy for local authorities to adopt. The Director of Finance & ICT, having consulted the Cabinet Member for Council Services, 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 – Treasury Management Advisors' Economic & Interest Rate Forecast - December 2020

### Underlying assumptions:

- The medium-term global economic outlook has improved with the distribution of vaccines, but the recent upsurge in coronavirus cases has worsened economic prospects in the short term.
- Restrictive measures and further lockdowns are likely to continue in the UK and Europe until the majority of the population is vaccinated by the second half of 2021. The recovery period will be strong thereafter, but potentially longer than previously envisaged.
- Signs of slowing UK economic recovery were already evident in UK monthly GDP and PMI data, even before the second lockdown and Tier 4 restrictions. Employment is falling despite an extension to support packages.
- The need to support economic recoveries and use up spare capacity will result in central banks maintaining low interest rates in the medium term.
- The UK's secured a future trading arrangement with the EU at the eleventh hour. The combined effect of Brexit and the after effects of the pandemic will dampen growth relative to peers, maintain spare capacity and limit domestically generated inflation. The Bank of England (BoE) will therefore maintain loose monetary conditions for the foreseeable future.
- Longer-term yields will also remain depressed, anchored by low central bank policy rates, expectations for potentially even lower rates and insipid longer-term inflation expectations. There is a chance yields will follow a slightly different path in the medium term, depending on investor perceptions of growth and inflation and the deployment of vaccines.

### Forecast:

- The Treasury Management Advisors for the Council expect the BoE Bank Rate to remain at the current 0.10% level.
- Their central case for BoE Bank Rate is no change, but further cuts to zero, or perhaps even into negative territory, cannot be completely ruled out.
- Gilt yields will remain low in the medium term. Shorter term gilt yields are currently negative and will remain around zero or below until either the BoE expressly rules out negative BoE Bank Rate or growth/inflation prospects improve.
- Downside risks remain in the near term, as the Government continues to react to the escalation in infection rates and the Brexit transition period comes to an end.

| | Dec-20 | Mar-21 | Jun-21 | Sep-21 | Dec-21 | Mar-22 | Jun-22 | Sep-22 | Dec-22 | Mar-23 | Jun-23 | Sep-23 | Dec-23 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Official Bank Rate | | | | | | | | | | | | | |
| Upside risk | 0.00 | 0.00 | 0.00 | 0.15 | 0.15 | 0.15 | 0.15 | 0.30 | 0.30 | 0.30 | 0.30 | 0.30 | 0.30 |
| Arlingclose Central Case | 0.10 | 0.10 | 0.10 | 0.10 | 0.10 | 0.10 | 0.10 | 0.10 | 0.10 | 0.10 | 0.10 | 0.10 | 0.10 |
| Downside risk | -0.10 | -0.20 | -0.50 | -0.50 | -0.50 | -0.50 | -0.50 | -0.50 | -0.50 | -0.50 | -0.50 | -0.50 | -0.50 |
| | | | | | | | | | | | | | |
| 3-month money market rate | | | | | | | | | | | | | |
| Upside risk | 0.05 | 0.05 | 0.05 | 0.10 | 0.10 | 0.15 | 0.20 | 0.30 | 0.30 | 0.30 | 0.30 | 0.30 | 0.30 |
| Arlingclose Central Case | 0.10 | 0.10 | 0.15 | 0.20 | 0.20 | 0.20 | 0.20 | 0.20 | 0.20 | 0.20 | 0.20 | 0.20 | 0.20 |
| Downside risk | -0.40 | -0.40 | -0.45 | -0.50 | -0.50 | -0.50 | -0.50 | -0.50 | -0.50 | -0.50 | -0.50 | -0.50 | -0.50 |
| | | | | | | | | | | | | | |
| 5yr gilt yield | | | | | | | | | | | | | |
| Upside risk | 0.40 | 0.40 | 0.40 | 0.45 | 0.45 | 0.50 | 0.50 | 0.55 | 0.60 | 0.60 | 0.65 | 0.65 | 0.70 |
| Arlingclose Central Case | 0.00 | 0.00 | 0.05 | 0.10 | 0.15 | 0.15 | 0.20 | 0.20 | 0.25 | 0.25 | 0.25 | 0.25 | 0.25 |
| Downside risk | -0.30 | -0.40 | -0.50 | -0.55 | -0.60 | -0.60 | -0.60 | -0.60 | -0.60 | -0.60 | -0.60 | -0.60 | -0.60 |
| | | | | | | | | | | | | | |
| 10yr gilt yield | | | | | | | | | | | | | |
| Upside risk | 0.40 | 0.40 | 0.40 | 0.45 | 0.45 | 0.50 | 0.50 | 0.55 | 0.60 | 0.60 | 0.65 | 0.65 | 0.70 |
| Arlingclose Central Case | 0.30 | 0.30 | 0.35 | 0.40 | 0.40 | 0.45 | 0.45 | 0.50 | 0.50 | 0.55 | 0.55 | 0.55 | 0.55 |
| Downside risk | -0.30 | -0.40 | -0.50 | -0.55 | -0.50 | -0.50 | -0.50 | -0.50 | -0.50 | -0.50 | -0.50 | -0.50 | -0.50 |
| | | | | | | | | | | | | | |
| 20yr gilt yield | | | | | | | | | | | | | |
| Upside risk | 0.40 | 0.40 | 0.40 | 0.45 | 0.45 | 0.50 | 0.50 | 0.55 | 0.60 | 0.60 | 0.65 | 0.65 | 0.70 |
| Arlingclose Central Case | 0.70 | 0.70 | 0.70 | 0.75 | 0.75 | 0.75 | 0.80 | 0.80 | 0.85 | 0.85 | 0.85 | 0.85 | 0.85 |
| Downside risk | -0.20 | -0.20 | -0.25 | -0.30 | -0.30 | -0.30 | -0.30 | -0.30 | -0.30 | -0.30 | -0.30 | -0.30 | -0.30 |
| | | | | | | | | | | | | | |
| 50yr gilt yield | | | | | | | | | | | | | |
| Upside risk | 0.40 | 0.40 | 0.40 | 0.45 | 0.45 | 0.50 | 0.50 | 0.55 | 0.60 | 0.60 | 0.65 | 0.65 | 0.70 |
| Arlingclose Central Case | 0.60 | 0.60 | 0.60 | 0.65 | 0.65 | 0.65 | 0.70 | 0.70 | 0.75 | 0.75 | 0.75 | 0.75 | 0.75 |
| Downside risk | -0.20 | -0.20 | -0.25 | -0.30 | -0.30 | -0.30 | -0.30 | -0.30 | -0.30 | -0.30 | -0.30 | -0.30 | -0.30 |

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

## Appendix B – Existing Investment and Debt Portfolio Position

| | 31 Dec 2020 Actual Portfolio £m | 31 Dec 2020 Average Rate % |
|---|---|---|
| **External Borrowing:** | | |
| Public Works Loan Board | 257.899 | 4.50 |
| Local authorities | 74.000 | 0.23 |
| LOBO loans | 5.000 | 4.50 |
| Other Bank Loans | 10.000 | 4.69 |
| Other loans (D2N2) | 72.000 | 0.10 |
| **Total External Borrowing** | **418.899** | **2.99** |
| **Other long term liabilities** | | |
| PFI | 63.709 | |
| Finance Leases | 5.009 | |
| Transferred Debt | 0.161 | |
| **Total Other Long Term Liabilities** | **68.879** | |
| **Total Gross External Debt** | **487.778** | |
| **Treasury Investments:** | | |
| Local Authorities | 210.000 | 1.02 |
| Banks (unsecured) | 40.092 | 0.30 |
| Registered Providers (unsecured) | 5.000 | 2.15 |
| Money Market Funds | 20.000 | 0.01 |
| **Total Deposits:** | **275.092** | **0.86** |
| Bonds | 5.051 | 2.59 |
| Equities UK | 7.029 | 4.74 |
| Equities Global | 5.627 | 2.93 |
| Multi Asset | 24.995 | 3.40 |
| Property | 22.952 | 4.36 |
| **Total Strategic Pooled Funds** | **65.654** | **3.74** |
| **Total Treasury Investments** | **340.746** | **1.42** |
| **Net Debt** | **147.032** | |

**Appendix Three**

# Investment Strategy Report 2021-22

## Introduction

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).

This Investment Strategy meets the requirements of statutory guidance issued by Government in January 2018, and focuses on the second and third of these categories.

## Treasury Management Investments

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. These activities, plus the timing of borrowing decisions, leads to a cash surplus, which is invested in accordance with guidance from the Chartered Institute of Public Finance and Accountancy (CIPFA). The balance of Treasury Management investments is expected to fluctuate between £262m and £423m during the 2021-22 financial year.

**Contribution:** The contribution that these investments make to the objectives of the Council is to support effective Treasury Management activities.

**Further details:** Full details of the Council's policies and its plan for 2021-22 for Treasury Management investments are covered in the Treasury Management Strategy included at Appendix Two.

## Service Investments: Loans

**Contribution:** The Council lends money to its local regeneration partners to stimulate local economic growth. The Council also lends money to its local Community Trusts to support local public services.

£12.753m + capitalised interest and fees - Buxton Crescent Hotel Ltd – to regenerate Buxton Crescent by redeveloping a derelict Grade I listed building at Buxton Crescent into a spa hotel. This will boost the economy and tourism in Buxton and the High Peak area.  Contribution of £0.561m per annum with effect from 12 months after reopening.

£0.500m - Community Trusts – to Chesterfield Football Club Community Trust.  Contribution of £0.012m per annum.

**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:

Each loan requires individual Cabinet approval.

**Table 1: Loans for service purposes in £ millions**

| **Category of borrower** | **31 March 2020 actual** | | | **2021-22** |
|---|---|---|---|---|
| | **Balance owed £m** | **Loss allowance £m** | **Net figure in accounts £m** | **Approved Limit £m** |
| Local Regeneration Partners | 12.268 | 1.227 | 11.041 | 13.468 |
| Local Community Trusts | 0.000 | 0.000 | 0.000 | 0.500 |
| **TOTAL** | **12.268** | **1.227** | **11.041** | **13.968** |

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.

**Risk assessment:** The Council assesses the risk of loss before entering into and whilst holding service loans by:

Buxton Crescent Hotel Ltd – the Council agreed a development loan to renovate and refurbish the Grade 1 listed building at The Crescent Buxton into a 5* luxury hotel and spa.  The development would regenerate Buxton Crescent and provide a welcome boost to the local economy and tourism.

The Buxton Crescent Spa Hotel opened on 1 October 2020, however Derbyshire entered Tier 3 Covid-19 restrictions on 31 October 2020, which meant the hotel had to close. Under the circumstances the Directors may request an extension of the repayment holiday.

Buxton Crescent & Thermal Spa Co Ltd - The risk of loss based upon an Arlingclose non-rated corporate estimate of 10.0%, on the current loan amount outstanding of £12.268m, is £1.227m.

Chesterfield Football Club Community Trust – the Council agreed a loan to enable the football club to continue its services in the local community.

Chesterfield Football Club has suffered from Covid-19 restrictions, resulting in no income from fans attending home matches. The Council's borrowing is fully secured on the stadium.

## Capacity, Skills and Culture

**Elected members and statutory officers**: Elected members receive periodic training from the Director of Finance & ICT on Treasury Management (including non-treasury investments).

The Director of Finance & ICT holds semi-annual meeting with the Council's Treasury Management advisors to discuss Treasury Management Strategy options.

**Commercial deals:** The Director of Finance & ICT is aware of the core principles of the prudential framework and of the regulatory regime within which local authorities operate.

**Corporate governance:** The Council's corporate governance arrangements are fully detailed in the Treasury Management Manual.

## Investment Indicators

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.

**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 2: Total investment exposure**

| Total investment exposure | 31.03.2020 Actual £m | 31.03.2021 Forecast £m | 31.03.2022 Forecast £m |
|---|---|---|---|
| Treasury management investments | 226.881 | 335.959 | 264.607 |
| Service investments: Loans | 12.268 | 13.391 | 13.968 |
| **TOTAL INVESTMENTS** | **239.149** | **349.350** | **278.575** |
| Commitments to lend | 0.623 | 0.577 | 0.000 |
| **TOTAL EXPOSURE** | **239.772** | **349.927** | **278.575** |

**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. However, the following investments could be described as being funded by borrowing. The remainder of the Council's investments are funded by usable reserves and income received in advance of expenditure.

**Table 3: Investments funded by borrowing**

| Investments funded by borrowing | 31.03.2020 Actual £m | 31.03.2021 Forecast £m | 31.03.2022 Forecast £m |
|---|---|---|---|
| **TOTAL FUNDED BY BORROWING** | **0.000** | **0.000** | **0.000** |

**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 4: Investment rate of return**

| Investments net rate of return | 2019-20 Actual % | 2020-21 Forecast % | 2021-22 Forecast % |
|---|---|---|---|
| Treasury management investments (excluding *) | 1.24 | 0.80 | 0.49 |
| *Strategic Pooled Funds | 4.32 | 3.74 | 3.74 |
| Service Investments: Loans | 4.65 | 4.32 | 4.32 |
| **ALL INVESTMENTS** | **2.19** | **1.45** | **1.47** |

**Table 5: Other investment indicators**

| Indicator | 2019-20 Actual | 2020-21 Forecast | 2021-22 Forecast |
|---|---|---|---|
| Debt to net service expenditure ratio | 1:1.28 | 1:1.27 | 1:1.50 |
| Service Loans income to net service expenditure ratio | 1:998 | 1:819 | 1:903 |

**Appendix Four**

# Capital Strategy

## 1 Purpose and Aims

The Prudential Code for Capital Finance in Local Authorities was updated by the Chartered Institute of Public Finance and Accountancy (CIPFA) in December 2017. The framework established by the Prudential Code supports local strategic planning, local asset management planning and proper option appraisal.

The objectives of the Prudential Code are to ensure that the capital expenditure plans of local authorities are affordable, prudent and sustainable and that treasury management decisions are taken in accordance with good professional practice and in full understanding of the risks involved.

The Prudential Code requires authorities to look at capital expenditure and investment plans in the light of overall organisational strategy and resources and ensure that decisions are made with sufficient regard to the long term financing implications and potential risks to the authority.

The Prudential Code sets out that in order to demonstrate that the authority takes capital expenditure and investment decisions in line with service objectives and properly takes account of stewardship, value for money, prudence, sustainability and affordability, the capital strategy should set out the long term context in which capital expenditure and investment decisions are made and gives due consideration to both risk and reward and impact on the achievement of priority outcomes.

This capital strategy sets out a framework for the self-management of capital finance and examines the following areas:

- Capital expenditure and investment plans;
- Prudential Indicators;
- External debt; and
- Treasury Management

## 2 Objectives of the Strategy

**T**he capital budgets should support the key priorities laid out in the Council's Council Plan. Each capital proposal is required to clearly demonstrate the project links to the Council's priorities, which are:

1. Work efficiently and effectively
2. Unlock economic growth and access to economic opportunities
3. Invest in employment and skill
4. Repair and improve the condition of Derbyshire roads
5. Improve accessibility in rural and vulnerable communities
6. Improve social care
7. Transform services for people with learning difficulties
8. Keeping children and adults safe

9. Be a good corporate parent for children in our care
10. Help children and young people get the best start
11. Encourage healthy lifestyles
12. Champion local communities
13. Support local library services
14. Protect local people and communities
15. Promote Derbyshire as a global cultural and tourist destination
16. Protect and enhance the natural environment

## 3 Key Projects

Within the Council Plan are a number of key projects which are, or will have an impact on the Council's Capital Programme:

- Delivered the Information and Communications Technology Strategy 2018-23 to streamline service delivery and embed modern working practices
- Increased fibre enabled broadband coverage across Derbyshire for homes and business
- Invested in well maintained roads and highways infrastructure
- Supported the development of a network of electric vehicle charging points across the county
- Created an innovation park on the former Coalite site in Bolsover
- Developed, agreed and begun to implement the Older People's Housing, Accommodation and Support Strategy
- Ensure all Council run adult care homes have Quality of Care graded as good or outstanding

In addition to this, the Council's Asset Management Framework identifies additional activities which are property specific including:

- Develop a model for the community management of Council property assets under the Thriving Communities agenda
- One Public Estate projects
- Delivery of major regeneration projects including Buxton Crescent
- Delivery of the schools capital programme
- Smarter working projects

## 4 Approach to Capital Investment

Derbyshire County Council's Capital Strategy defines and outlines the Council's approach to capital investment and is fundamental to the Council's financial planning processes. It aims to ensure that:

- An affordable and sustainable capital programme is delivered.
- Use of resources and value for money is maximised.

- A clear framework for making capital expenditure decisions is provided.
- A corporate approach to generating capital resources is established.
- Access to sufficient long term assets to provide services are acquired and retained
- Invest to save initiatives to make efficiencies within the Council's revenue budget are encouraged
- An appraisal and prioritisation process for new schemes is robust.
- Capital expenditure contributes to the achievement of the Council's strategic plan.

## 5 Commercial Activity and Investment Property

The CIPFA Code defines investment property as property held solely to earn rentals or for capital appreciation or both. Returns from property ownership can be both income driven (through the receipt of rent) and by way of appreciation of the underlying asset value (capital growth). The combination of these is a consideration in assessing the attractiveness of a property for acquisition.

The Council does not currently borrow to fund these type of activities.

## 6 Loans

The Council has discretion to make loans for a number of reasons, primarily for economic development. These loans are treated as capital expenditure.

In making loans the Council is exposing itself to the risk that the borrower defaults on repayments. The Council, in making these loans, must therefore ensure they are prudent and has fully considered the risk implications, with regard to both the individual loan and that the cumulative exposure of the Council is proportionate and prudent.

The Council will ensure that a full due diligence exercise is undertaken and adequate security is in place. The business case will balance the benefits and risks. All loans are agreed by Cabinet. All loans are subject to close, regular monitoring.

For further details, refer to the Investment Strategy above.

## 7 Governance Arrangements

### Capital Programme Approvals

The Council's constitution and financial regulations govern the capital programme as set out below:

- All capital expenditure must be carried out in accordance with the Financial Regulations and the Council's Constitution.

- The expenditure must comply with the statutory definition of capital purposes as defined within this document and wider financial standards.
- The Capital Programme approved by Full Council as part of the Council's annual budget report sets the capital funding availability for the Council.
- Prioritisation of funding and the schemes receiving entry into the Capital Programme.
- Each scheme must be under the control of a responsible person/project manager.
- Any agreements (such as section 106) which contractually commit to procure capital schemes will need to follow the same approval process as other capital expenditure before it can be formally be incorporated into the capital programme.

**Capital Programme Bodies**

The main internal bodies that are responsible for the governance and management of the capital programme are the Full Council, Cabinet, Cabinet Member and the Capital Strategy Group.

- **Full Council:**
  Approves the Capital Programme as part of the Annual Budget Report within the strategic boundaries set by the Council.

- **Cabinet/Cabinet Member:**
  Approves additional schemes into the Capital Programme and cost variations to various schemes

  Cabinet also receives the capital monitoring reports.

- **Capital Strategy Group:**
  This is a cross-service group of officers with a finance, service and property management background.

  It is responsible for ensuring that the Council has a clear and cohesive strategy for managing its physical assets and to oversee the development and delivery of the Council's Capital Programme in support of that strategy.

## 8 Funding Streams

The Council's Capital Programme is funded from a mix of sources including:-

- **Prudential Borrowing**
  The introduction of the Prudential Code in 2004 allowed the Council to undertake unsupported borrowing itself. This borrowing is subject to the requirements of the Prudential Code for Capital Expenditure for Local Authorities. The Council must ensure that unsupported borrowing is affordable, prudent and cost effective. This has provided the Council with the flexibility to raise capital funding as demand and business need have dictated. This type of borrowing has revenue implications for the Council in the form of financing costs.

- **External Grants**
  The largest form of capital funding comes through as external grant allocations from Central Government departments, such as the Department for Transport and Department for Education.

- **Section 106 and External Contributions**
  Elements of the Capital Programme are funded by contributions from private sector developers and partners. Growth in Derbyshire has resulted in Section 106 contributions from developers accounting for significant elements of funding of the Capital Programme in recent years.

- **Revenue Funding**
  The Council can use revenue resources to fund capital projects on a direct basis and this funding avenue has been used in the past. However, the impact of austerity on the Council's revenue budget has reduced options in this area and therefore the preference is for Invest to Save options to be adopted where feasible.

- **Capital Receipts**
  The Council is able to generate capital receipts through the sale of surplus assets such as land and buildings. The Council seeks to maximise the level of these resources which will be available to support the Council's plans.

The size of the Capital Programme will be influenced by funding sources and financing costs. The main limiting factor on the Council's ability to undertake capital investment is whether the revenue resource is available to support in full the implications of capital expenditure, both borrowing costs and running costs, after allowing for any support provided by central government, now mainly through capital grants.

## 9 Key strategies impacting on the Council's Capital Strategy

The three key strategies in place that will significantly influence the Council's Capital Programme over the medium term:

### (a) Property Asset Management Framework

The strategic aim of the Property Asset Management Framework is to ensure that the Council has appropriate, cost effective buildings from which to deliver services.

The aim of the strategy is to give clarity to the way we manage our assets, including:

- The organisational arrangements for asset management including polices and protocols.
- The corporate processes for decision making in relation to our assets – Corporate Governance.
- The performance measures and monitoring.
- How we manage and maintain our data on land and buildings.

**Property Policies and Protocols**

There are a number of policies and protocols that need to be in place to deliver strategic asset management effectively:

- Property Acquisition Protocol
- Property Disposal Protocol
- Community Asset Transfer Protocol
- Lettings Protocol
- Process for departments to follow when they have a property need
- Process for departments to follow when they wish to vacate a property
- Decommissioning Process
- Property Review Process

### (b) ICT Strategy

The Council recognises that ICT is a key enabler of service delivery. The strategy outlines how ICT will deliver new technologies to support the ambitions and outcomes of the Council Plan and Derbyshire's approach to becoming an Enterprising Council. In order to achieve this, a five year replacement capital programme will be developed, and initial requirements over this period are likely to be around £10m:

**Summary of Strategy Deliverables**

- Changing Service Models
- ICT Governance Structure
- Mobile and Agile Workforce
- Digital by Default
- Workforce ICT Competencies
- Corporate and Business systems
- ICT Infrastructure Delivery
- Responsible Data management

## (c) Highways Infrastructure Asset Management Strategy

Highway infrastructure is the largest and most visible asset the Council is responsible for. With a gross replacement cost of £11.0bn, it is fundamental to the delivery of the Council Plan. It includes over 5,000km of road network, as well as supporting public transport through cycle routes, public rights of ways, canals, bus stations and shelters, on-street parking, school buses and vehicle fleet. It reflects the character and quality of the local areas that it serves and makes an important contribution to the wider Council priorities, including regeneration, social inclusion, education, employment, recreation and health. In order to deliver these aims and strengthen local communities, it is crucial that it is maintained to enable safe, reliable and sustainable journeys.

There are a variety of factors that need to be taken into consideration when determining the Council's expectations for the highway service:

- Meeting national policy, guidance and codes of practice.
- Delivering Council goals – including maintenance policy and Local Transport Plan.
- Supporting Council Vision.
- Complying with legal duties, including Highways Act 1980, Traffic Management Act 2004 and The Equalities Act 2010.
- Enabling effective whole Government accounts and local financial reporting.
- Managing Stakeholder expectations – the Council readily engages with stakeholders through Elected Members, the National Transport and Public Satisfaction Survey, the DCC website, officer workshops and Midland Service Improvement Group (MSIG).
- Understanding future demands of the highway infrastructure assets.
- Making the best of financially constrained budgets.
- Delivering efficiency and value for money.
- Delivering long term improvements to the condition of the network.
- Providing a safe and reliable network.

The major groups of assets covered by the Strategy are:

- Carriageways
- Footways and Cycleways
- Structures (Bridges/retaining walls)
- Drainage
- Street Lighting
- Electronic Traffic Management
- Street Furniture (Traffic Signs/Vehicle Restraint Systems etc)

The major source of capital funding for the network is from the Local Transport Plan grant from central government which is approximately £22m per annum.

## 10 2021-22 Prudential Indicators for Capital Finance

This section of the Capital Strategy sets out the prudential indicators and outlines how expenditure will be financed by borrowing in an affordable, prudent and sustainable way.

### Information and Advice

The Local Government Act 2003 enables local authorities to determine their programmes for capital investment and associated borrowing requirements, provided they have regard to the Prudential Code for Capital Finance in Local Authorities developed by CIPFA and also take advice from the Section 151 Officer.

The Executive Summary of the Code states that "The framework established by the Prudential Code should support local strategic planning, local asset management planning and proper option appraisal. The objectives of the Prudential Code are to ensure, within a clear framework, that the capital investment plans of local authorities are affordable, prudent and sustainable, and that treasury management decisions are taken in accordance with good professional practice."

The Code sets out a number of prudential indicators designed to support and record local decision making and it is the duty of the Chief Financial Officer (the Council's Section 151 Officer) to ensure that this information is available to Members when they take decisions on the Council's capital expenditure plans and annual budget. Key issues to be considered are:

- Affordability (e.g. implications for Council Tax).
- Prudence and sustainability (e.g. implications for external borrowing and whole life costing).
- Value for money.
- Stewardship of assets (Service objectives (e.g. alignment with the Council's Strategic Plan).

- Practicality (e.g. whether the capital plans are achievable).

**Affordability**

The fundamental objective in the consideration of the affordability of the Council's capital plans is to ensure that the level of investment in capital assets proposed means that the total capital investment of the Council remains within sustainable limits.

In considering the affordability of its capital plans, the Council is required to consider all of the resources currently available to it and estimated for the future, together with the totality of its capital plans, income and expenditure forecasts.

The costs of financing capital expenditure are:

- Interest payable to external lenders less interest earned on investments.
- Amounts set aside for repayments of amounts borrowed (including repayments of amounts relating to PFI schemes and other finance lease liabilities).

**Table 1 – Actual and Estimates of financing costs to net revenue stream**

This indicator identifies the trend in the cost of capital against the net revenue stream, based on the Capital Programme.

| | **2019-20 Actual £m** | **2020-21 Estimate £m** | **2021-22 Estimate £m** | **2022-23 Estimate £m** | **2023-24 Estimate £m** |
|---|---|---|---|---|---|
| Financing costs of CFR | 40.850 | 44.760 | 49.970 | 56.906 | 59.480 |
| Net Revenue stream inc DSG | 898.088 | 910.570 | 915.579 | 929.725 | 1044.335 |
| **Percentage** | **4.55%** | **4.92%** | **5.46%** | **6.12%** | **5.70%** |
| Net Revenue stream excluding DSG | 539.126 | 545.395 | 550.404 | 564.550 | 679.160 |
| **Percentage** | **7.58%** | **8.21%** | **9.08%** | **10.08%** | **8.76%** |

## Prudence and Sustainability

The Prudential Code requires that the Council shall ensure that all of its capital expenditure, investments and borrowing decisions are prudent and sustainable.

In doing so it will take into account its arrangements for the repayment of debt and consideration of risk and the impact on the Council's overall fiscal sustainability.

The Council is required to make reasonable estimates of the total capital expenditure that it plans to incur in the forthcoming financial year and at least the following two financial years.

As part of the Prudential Code arrangements the authority needs to calculate the Capital Financing Requirement. This figure covers capital expenditure which has not yet been permanently financed through the revenue account.

The Code also states that "In order to ensure that over the medium term net debt will only be for a capital purpose, the local authority should ensure that net debt does not, except in the short term, exceed the total of the capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years." This is a key indicator of prudence.

**Table 2 – Estimates of Capital Expenditure and Capital Financing Requirement**

| | **2019-20 Actual £m** | **2020-21 Estimate £m** | **2021-22 Estimate £m** | **2022-23 Estimate £m** | **2023-24 Estimate £m** |
|---|---|---|---|---|---|
| **Capital Expenditure** | **103.249** | **155.630** | **172.370** | **102.460** | **70.310** |
| **Funding Sources:** | | | | | |
| Borrowing | 48.900 | 61.220 | 82.400 | 60.250 | 33.710 |
| Capital receipts | 7.833 | 9.240 | 12.100 | 3.970 | 0.140 |
| Capital grants | 46.516 | 74.950 | 73.240 | 26.990 | 36.330 |
| Revenue | 0.000 | 10.220 | 4.630 | 11.250 | 0.120 |
| | | | | | |
| **Total CFR at year end** | **525.169** | **572.709** | **642.699** | **679.939** | **688.939** |
| Net movement in CFR | 37.954 | 47.540 | 69.990 | 37.240 | 9.000 |
| Minimum Revenue Provision | 10.947 | 13.680 | 12.410 | 23.010 | 24.720 |
| | | | | | |
| PFI & Leases in CFR | 68.718 | 64.393 | 59.832 | 62.045 | 56.399 |
| PFI & Leases in MRP | 4.102 | 4.326 | 4.560 | 4.787 | 5.046 |

As such there is a requirement to ensure that net debt (the sum of borrowing and other long-term liabilities, net of investments) in 2021-22 does not, except in the short term, exceed £642.699m (i.e. the estimated CFR for 2021-22).

**External Debt**

The Local Government Act 2003 requires the Council to set two borrowing limits for next year and the following two years with respect to external borrowing.

Operational Boundary –have to be set for both borrowing and long term liabilities.

This measure encompasses all borrowing and is used in-year as a tool for monitoring the Council's prudent borrowing requirements. The operational boundary is calculated by taking account of existing borrowing and long term liabilities, planned new borrowing, net change in long term liabilities and any amounts set aside for repayment of debt.

Authorised Limit – this higher measure, is the upper limit on the level of gross indebtedness which must not be breached without Council approval.

The Operational Boundary for external debt for the next three years is built up from the existing level of external borrowing, which was £329.974m, and the level of relevant liabilities (including finance lease liabilities), which was £68.879m, on the Balance Sheet at 31 March 2020.

The Authorised Limit for 2021-22 is to be £707m and the Operational Boundary is to be £675m.

**Table 3 – Authorised Limit for External Debt**

| | **2019-20 Actual £m** | **2020-21 Estimate £m** | **2021-22 Estimate £m** | **2022-23 Estimate £m** |
|---|---|---|---|---|
| **Authorised limit for external debt** | **578** | **630** | **707** | **748** |
| **Operational boundary for external debt** | **551** | **601** | **675** | **714** |
| | | | | |
| **Borrowing** | 330 | 379 | 288 | 266 |
| **Other debt liabilities** | 69 | 65 | 60 | 62 |
| **Total** | **399** | **444** | **348** | **328** |

## 11 Knowledge and Skills

The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. 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. 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.