

Capital Strategy Report 2023/24

1.0 Introduction

- 1.1 This Capital Strategy Report gives a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of local public services along with an overview of how associated risk is managed and the implications for future financial sustainability. It has been written in an accessible style to enhance members' understanding of these sometimes technical areas.
- 1.2 Decisions made this year on capital and treasury management will have financial consequences for the Council for many years into the future. They are therefore subject to both a national regulatory framework and to local policy framework, summarised in this report.

2.0 Capital Expenditure and Financing

- 2.1 Capital expenditure is where the Council spends money on assets, such as property, vehicles or other assets that will be used for more than one year. In local government this includes spending on assets owned by other bodies, and loans and grants to other bodies enabling them to buy assets. The Council has some limited discretion on what counts as capital expenditure, for example assets costing below £5,000 are generally not capitalised and are charged to revenue in year. Details of the Council's policy on capitalisation is set out in the annual Statement of Accounts.
- 2.2 In 2023/24, the Council is planning capital expenditure of £461.4m as summarised below:

Table 1: Prudential Indicator: Estimates of Capital Expenditure in £ millions

£M	2022/23 forecast	2023/24 budget	2024/25 budget	2025/26 budget	2026/27 budget	2027/28 budget
General Fund services	173.0	304.4	213.8	85.7	41.0	42.0
Council housing (HRA)	59.4	156.9	113.3	37.0	22.6	-
Capital investments	-	-	-	-	-	-
TOTAL	232.4	461.4	327.1	122.7	63.7	42.0

- 2.3 The Capital Programme comprises of projects approved by Cabinet from previous year budget setting, new projects approved in year and being brought forward including those promoted from the pipeline provision.

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- 2.4 The main General Fund capital projects include the new Council Homes Programme £143.2m, i4B Street Properties Purchase £58.2m, NAIL (Supported Living) £18.1m and Morland Gardens Regeneration £43.5m. The Council also plans to incur capital expenditure on investments, which are discussed in more detail within the Investment Strategy for 2023/24.
- 2.5 The Housing Revenue Account (HRA) is a ring-fenced account which ensures that council housing does not subsidise, or is itself subsidised, by other local services. HRA capital expenditure is therefore recorded separately, and includes the building of new homes as well as expenditure on improving and maintaining council homes over the planning period.
- 2.6 Capital investments include loans and shares made for service purposes and property to be held primarily for financial return in line with the definition in the CIPFA Treasury Management Code.
- 2.7 **Governance:** Full details of the Council's capital programme, including the project appraisals undertaken can be found within the capital programme and capital pipeline proposals 2023/24 presented to Cabinet in February 2023.
- 2.8 All capital expenditure must be financed, either from external sources (government grants and other contributions), the Council's own resources (revenue, reserves and capital receipts) or debt (borrowing, leasing and Private Finance Initiative). The planned financing of the above expenditure is as follows:

Table 2: Capital financing in £ millions

£M	2022/23 forecast	2023/24 budget	2024/25 budget	2025/26 budget	2026/27 budget	2027/28 budget
External resources	56.2	124.1	39.2	20.4	0.0	0.0
Revenue resources	34.3	60.6	57.8	30.6	11.4	7.1
Debt	141.9	276.6	230.1	71.8	52.3	34.9
TOTAL	232.4	364.8	327.1	122.7	63.7	42.0

- 2.9 Excluding external grants and other resources most assets are funded from debt. As with any debt, it must be repaid over time, and for a local authority there is a statutory requirement to set aside "minimum revenue provision" (MRP) in each year's budget for debt repayment. Planned MRP to 2026/27 is as set out in the table below.

Table 3: Replacement of debt finance in £ millions

£M	2022/23 forecast	2023/24 budget	2024/25 budget	2025/26 budget	2026/27 budget	2027/28 budget
MRP	13.6	13.3	15.8	18.1	20.5	21.6
TOTAL	13.6	13.3	15.8	18.1	20.5	21.6

- 2.10 The Council's full minimum revenue policy statement is presented as an Appendix to the annual Council Tax and Budget Setting Report.
- 2.11 The Council's cumulative outstanding amount of debt finance is measured by the capital financing requirement (CFR). This increases with new debt-financed capital expenditure and reduces with MRP and capital receipts used to replace debt. The CFR is expected to increase to £1.3bn during 2023/24 and to over £1.6bn by 2026/27. Based on the above figures for expenditure and financing, the Council's estimated CFR is as follows:

Table 4: Prudential Indicator: Estimates of Capital Financing Requirement in £ millions

£M	2022/23 forecast	2023/24 budget	2024/25 budget	2025/26 budget	2026/27 budget	2027/28 budget
Opening CFR	997.3	1,125.6	1,389.0	1,603.3	1,657.0	1,688.7
Capital Expenditure	232.4	461.4	327.1	122.7	63.7	42.0
External resources	(56.2)	(124.1)	(39.2)	(20.4)	0.0	0.0
Own Resources	(34.3)	(60.6)	(57.8)	(30.6)	(11.4)	(7.1)
MRP	(13.6)	(13.3)	(15.8)	(18.1)	(20.5)	(21.6)
Closing CFR	1,125.6	1,389.0	1,603.3	1,657.0	1,688.7	1,702.1

3.0 Capital Programme Governance and Prioritisation

- 3.1 The capital programme is updated annually for new schemes, revised profiling, slippage and changes in expenditure projections. The capital programme and capital pipeline proposals 2023/24 – report (included elsewhere on this agenda) sets out the indicative capital programme that will be presented to Council in February 2023 as part of the annual budget setting cycle.

Pipeline Schemes

- 3.2 During the year the individual capital sub-boards (led by Operational Directors) developed a comprehensive list of opportunities and proposals for future aspirational capital investment to meet the council's strategic objectives. These outline bids are then collated by the PMO (Programme Management Office). For 2023/24 this process has culminated in the assimilation of c24 individual outline capital proposals with a total value of c480m and a spend profile spanning 2 to 5 years. At this stage these strategic pipeline schemes are only indicative and do not yet form part of the main programme as there is a requirement that individually they will still go through the normal approval routes (i.e. CMT/Cabinet/Council). Furthermore, officers will be required to produce detailed business cases, undertake feasibility and consult appropriately before getting to this stage.

Capital Programme Board

- 3.3 This Board is the main forum for reviewing the financial viability of the new capital bids and monitoring of existing programme. The Board reviews all capital investment and new opportunities, oversees and maintains the list of pipeline schemes and ensures outcomes are aligned with Council's aspirations and reflective of the circumstances within Brent. The board also ensures that all projects have a viable business case and that value for money (VfM) will be delivered for the Council.

Prioritisation criteria

- 3.4 The general criteria for scoring proposals are summarised below, higher scores were applied based on the following criterion:
- **Strategic Alignment** - How the scheme meets the outcomes of a key service objective as stated in a strategy document, business plan or action plan.
 - **Statutory Obligations** - How the delivery of a scheme is essential to ensuring the Council meets the statutory need and without the project, the Council would otherwise be at risk of failing to meet.
 - **Risk** - Whether the success of the project is dependent on mitigating high associated risks
 - **Financial Return** - Whether the scheme generates ongoing revenue savings, a capital receipt or attract external funding (partial or fully).
 - **Demand and Demographic Changes** - whether the scheme is required following a change in demographic, economic or social change that impact the borough and will reduce the demand for services in the borough.

4.0 Asset management

- 4.1 To ensure that capital assets continue to be of long-term use, the Council has a Housing Asset Management strategy in place and a Property Asset Management Strategy under review. The strategies provide a planning tool which ensures the assets are well managed and maintained in order to maximise the benefits for local residents.

5.0 Asset disposals

- 5.1 When a capital asset is no longer needed, it may be sold so that the proceeds, known as capital receipts, can be spent on new assets or to repay debt. The Council is currently also permitted to spend capital receipts on service transformation projects until 2023/24. Repayments of capital grants, loans and investments also generate capital receipts.
- 5.2 The Council plans to receive £7.1m of capital receipts in the current financial year. A significant proportion of these arise from asset disposals on the South Kilburn site as well as housing sold under the right to buy (RTB) scheme. The capital receipts expected in future financial years are as follows:

Table 5: Capital receipts in £ millions

£M	2022/23 forecast	2023/24 budget	2024/25 budget	2025/26 budget	2026/27 budget	2027/28 budget
Asset Sales	3.0	16.2	6.0	0.0	13.8	0.0
Loans Repaid	7.4	6.9	20.7	34.5	77.0	51.9
TOTAL	10.4	23.1	26.7	34.5	90.8	51.9

6.0 Treasury Management

- 6.1 Treasury management is concerned with keeping sufficient but not excessive cash available to meet the Council's spending needs, while managing the risks involved. Surplus cash is invested until required, while a shortage of cash will be met by borrowing, to avoid excessive credit balances or overdrafts in the bank current account.
- 6.2 The Council is typically cash rich in the short-term as revenue income is received before it is spent, but cash poor in the long-term as capital expenditure is incurred before being financed. The revenue cash surpluses are offset against capital cash shortfalls to reduce overall borrowing.
- 6.2 On 31st December 2022, the Authority held £761.9m of borrowing (£686.9m long term and £75.0m short term) at an average rate of 3.3% and £142.0m of investments at an average rate of 2.7%.

7.0 Borrowing strategy

- 7.1 The Council's main objectives when borrowing are to achieve a low but certain cost of finance while retaining flexibility should plans change in future. These objectives are often conflicting, and the Council therefore seeks to strike a balance between cheap short-term loans (currently available at around 3.5-4%) and long-term fixed rate loans where the future cost is known but higher (currently around 4.2-4.8%).

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- 7.2 Projected levels of the Council’s total outstanding debt (which comprises borrowing, PFI liabilities and leases) are shown below, compared with the capital financing requirement (see above).

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

£M	2022/23 forecast	2023/24 budget	2024/25 budget	2025/26 budget	2026/27 budget	2027/28 budget
Debt (incl. PFI & leases)	700.5	689.0	726.6	716.9	707.5	697.7
Capital Financing Requirement	1,125.6	1,389.0	1,603.3	1,657.0	1,688.7	1,702.1

- 7.3 Statutory guidance prescribes that debt should remain below the capital financing requirement, except in the short-term. As can be seen from Table 6, the Council expects to comply with this regulation.

8.0 Affordable borrowing limit

- 8.1 The Council is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt) each year. In line with statutory guidance, a lower “operational boundary” is also set as a warning level should debt approach the limit.

Table 7: Prudential Indicators: Authorised limit and operational boundary for external debt in £ millions

£M	2022/23 budget	2023/24 budget	2024/25 budget	2025/26 budget	2026/27 budget	2027/28 budget
Authorised Limit	1,400.0	1,700.0	1,800.0	1,800.0	1,900.0	2,000.0
Operational Boundary	1,200.0	1,500.0	1,600.0	1,600.0	1,700.0	1,800.0

- 8.3 Further details on borrowing are contained within the Council’s treasury management strategy.

9.0 Investment strategy

9.1 Treasury investments balances arise from receiving cash before it is required to be paid out again. Investments made for service reasons or for pure financial gain are not generally considered to be part of treasury management.

9.2 The Council’s policy on treasury investments is to prioritise security and liquidity over yield and to focus on minimising risk rather than maximising returns. Cash that is likely to be spent in the near term is invested securely, for example with the government, other local authorities or selected high-quality banks, to minimise the risk of loss. Money that will be held for longer terms is invested more widely, including in bonds, shares and property, to balance the risk of loss against the risk of receiving returns below inflation. Both near-term and longer-term investments may be held in pooled funds, where an external fund manager makes decisions on which particular investments to buy and the Council may request its money back at short notice.

Table 8: Treasury management investments in £millions

£M	2022/23 forecast	2023/24 budget	2024/25 budget	2025/26 budget	2026/27 budget	2027/28 budget
Short term investments	30.0	30.0	30.0	30.0	30.0	30.0
Long term investments	0.0	0.0	0.0	0.0	0.0	0.0

9.3 Further details on treasury investments are contained within the Council’s treasury management strategy.

9.4 Risk management: The effective management and control of risk are prime objectives of the Council’s treasury management activities. The treasury management strategy therefore sets out various indicators and limits to constrain the risk of unexpected losses.

9.5 Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Director of Finance, who must act in line with the treasury management strategy approved by Council. Reports on treasury management activity are presented to Cabinet and Full Council, whilst the Audit & Standards Advisory Committee is responsible for scrutinising treasury management decisions.

10.0 Investments for Service Purposes

10.1 The Council makes investments to assist local public services, including making loans to council subsidiaries to promote economic growth. In light of the public service objective, the Council is willing to take more risk than with treasury investments, however it still plans for such investments to break-even after all costs.

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10.2 Decisions on service investments are either made by Cabinet or under delegated authority, or set down in the approved investment strategy. Most loans and shares are capital expenditure and purchases will therefore also be approved as part of the capital programme. Further details on service investments are contained within the investment strategy.

10.3 The proposed budget includes sums for investment in the Council's subsidiary i4B for the acquisition of street properties as part of the Council's temporary accommodation reform plan. These schemes aim to alleviate affordable housing pressures. A development finance loan to United College's Group to assist with cashflow pressures around their campus redevelopment has also been included.

11.0 Commercial Activities

11.1 The Council has previously invested in property locally to support regeneration whilst also securing a financial return. Total commercial investments are currently valued at £20.7m consisting of 40 individual property assets generating £3.1m PA, or a yield of 15%. Over time the use of these assets may change as new priorities are confirmed and assets are repurposed to contribute to the delivery of new strategic priorities.

Table 9: Property asset types and income generated in £millions

ASSET TYPES	No. of Assets	Value £M	Income PA £M
Operational	47	186.4	0.0
Commercial	40	20.7	3.1
Community Groups	63	28.3	0.0
Education	70	486.8	0.0
Regeneration	101	6.5	0.0
Non HRA Housing	533	280.5	0.0
TOTAL	853	1,009.2	3.1

11.2 With a higher financial return, the Council accepts higher risk on commercial investment than with treasury investments. The principal risk exposures include voids, diminution of capital values, etc. These risks are managed by the existing risk management framework. In order that commercial investments remain proportionate to the size of the authority they are under constant review and contingency plans are in place should expected yields not materialise. The Corporate Director for Finance and Resources is responsible for governance and due diligence on these investments.

12.0 Liabilities

- 12.1 In addition to debt of £700.5m detailed above, the Council is committed to making future payments to cover its pension fund deficit (valued at £163m – Report March 2022).
- 12.2 The Council will be making appropriate adjustments to its bad debt provision due to the impact of global pandemic on local businesses, residents and suppliers with more details to be provided in the 2022/23 statement of accounts.

13.0 Revenue Budget Implications

- 13.1 Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP payments are charged to revenue, offset by any investment income receivable. The net annual charge is known as financing costs; this is compared to the net revenue stream i.e. the amount funded from Council Tax, business rates and general government grants.

Table 10: Prudential Indicator: Proportion of net revenue stream to financing costs

£M	2022/23 forecast	2023/24 budget	2024/25 budget	2025/26 budget	2026/27 budget	2027/28 budget
Financing costs	36.5	57.3	78.5	101.8	109.7	112.1
Proportion of net revenue stream %	12.6%	18.7%	24.3%	31.0%	33.4%	34.1%

- 13.2 Due to the very long-term nature of capital expenditure and financing, the revenue budget implications of expenditure incurred in the next few years will extend for up to 50 years into the future. The detailed information contained within the treasury management strategy and the Budget & Council Tax Report 2023/24, as well as the prudential indicators included above demonstrates how this is prudent, affordable and sustainable.

14.0 Knowledge and Skills

- 14.1 The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. The Council also pays for junior staff to study towards relevant professional qualifications including CIPFA and AAT for example.
- 14.2 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 can be

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more cost effective than employing such staff directly, and ensures that the Council has access to knowledge and skills commensurate with its risk appetite.