

## Capital Strategy Report 2020/21

### 1.0 Introduction

1.1 The capital strategy is a requirement for authorities following the publication of the revised Prudential Code for Capital Finance in Local Authorities in 2017. Our Capital Strategy has been produced in accordance with the guidance.

1.2 The Capital Strategy provides:

- A high-level overview of how capital expenditure, capital financing and treasury management activity supports the provision of local public services;
- an overview of how associated risk is managed; and
- the implications for future years budget and financial sustainability.

### 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 2020/21, the Council is planning capital expenditure of £291M as summarised below:

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

£M	2019/20 forecast	2020/21 budget	2021/22 budget	2022/23 budget	2023/24 budget	2024/25 budget
Capital Expenditure	261.2	292.5	280.5	158.1	42.6	5.5
Financing:						
General Fund services	81.5	173.0	182.9	126.6	41.7	5.5
Council housing (HRA)	110.0	92.1	74.1	8.0	0.9	0
Capital investments	69.7	27.4	23.5	23.5	0	0
<b>TOTAL</b>	<b>261.2</b>	<b>292.5</b>	<b>280.5</b>	<b>158.1</b>	<b>42.6</b>	<b>5.5</b>

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2.3 The Capital Programme comprises of projects approved by Cabinet from previous year budget setting, new projects approved in year and bids promoted from the pipeline provision for Cabinet approval in February 2020.

The main General Fund capital projects include (South Kilburn Estate Regeneration £74.2M, i4B Street Properties Purchase £110M, Schools Expansion programme works £35.1M, NAIL (Supported Living) £19M and Morland Gardens Regeneration £43M). The Council also plans to incur capital expenditure on investments, which are detailed later in this report in paragraph 2.9.

2.4 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.

2.5 Full details of the Council's capital programme, including the project appraisals undertaken can be found within the capital programme and capital pipeline proposals 2020/21 presented to Cabinet in January 2020.

2.6 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	2019/20 forecast	2020/21 budget	2021/22 budget	2022/23 budget	2023/24 budget	2024/25 budget
External resources	52.0	64.5	67.2	29.7	2.1	0
Own Resources	65.9	69.7	36.2	23.5	9.9	5.5
Debt	143.3	158.3	177.1	104.9	30.6	0
<b>TOTAL</b>	<b>261.2</b>	<b>292.5</b>	<b>280.5</b>	<b>158.1</b>	<b>42.6</b>	<b>5.5</b>

2.7 Excluding external grants and other resources most assets are funded from debt. (The position in 2019/20 to 2021/22 is somewhat unusual as the council has accumulated capital receipts and other reserves planned to be used to fund capital expenditure). 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 2024/25 is as set out in the table below.

**Table 3: Replacement of debt finance in £ millions**

£M	2019/20 forecast	2020/21 budget	2021/22 budget	2022/23 budget	2023/24 budget	2024/25 budget
MRP	10.2	10.2	11.8	13.6	13.1	13.1
<b>TOTAL</b>	<b>10.2</b>	<b>10.2</b>	<b>11.8</b>	<b>13.6</b>	<b>13.1</b>	<b>13.1</b>

- 2.8 The Council's full minimum revenue policy statement is presented as an Appendix to the annual Council Tax and Budget Setting Report.
- 2.9 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 £970M during 2020/21, and to over £1bn, a 50% increase on the 2019/20 figure, by 2024/25. 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	2019/20 forecast	2020/21 budget	2021/22 budget	2022/23 budget	2023/24 budget	2023/24 budget
Opening CFR	688.7	821.8	969.9	1,135.2	1,226.4	1,243.8
Capital Expenditure	261.2	292.5	280.5	158.1	42.6	5.5
External resources	(52.0)	(64.5)	(67.2)	(29.7)	(2.1)	0
Own Resources	(65.9)	(69.7)	(36.2)	(23.5)	(9.9)	(5.5)
MRP	(10.2)	(10.2)	(11.8)	(13.6)	(13.1)	(13.1)
<b>Closing CFR</b>	<b>821.8</b>	<b>969.9</b>	<b>1,135.2</b>	<b>1,226.4</b>	<b>1,243.8</b>	<b>1,230.7</b>

### 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 2020/21 – report (included elsewhere on this agenda) sets out the indicative capital programme that will be presented to Council in February 2020 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 2020/21 this process has culminated in the assimilation of c50 individual outline capital proposals with a total value of c£545m 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 Investment Panel (CIP)

- 3.3 The main forum for reviewing the financial viability of the new capital bids is the **Capital Investment Panel (CIP)**. The panel reviews all new capital investment 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 panel also ensures that 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:
- **Statutory obligations** – higher scores are applied to schemes with a greater statutory need and the need is of significance.
  - **Financial return** – higher scores are applied to schemes that generate ongoing revenue savings or capital receipts.
  - **Local demand** – higher scores are applied where the proposal will enhance residents demand and satisfaction.
  - **Complexity** – proposals that are likely to be deliverable without slippage, complicated negotiations, lots of officer time are more likely to be approved.
  - **Economic growth** – higher score are applied where proposal would contribute towards economic growth (such as enhancement to residents' employment prospects, attract new business into the local economy) in the borough.
  - **Demand management** – higher scores are applied where proposal would reduce current demand for services or, to a lesser extent reduce future demand for services.

### 4.0 Asset management

- 4.1 To ensure that capital assets continue to be of long-term use, the Council has an asset management strategy in place. The Property and Asset Strategy 2015-19 was approved by cabinet on 1 June 2015.

## 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 2021/22. Repayments of capital grants, loans and investments also generate capital receipts. The Council plans to receive £28.8M of capital receipts, a significant proportion of which stems from asset disposals on the South Kilburn site as well as housing sold under the right to buy (RTB) scheme. The capital receipts in the coming financial year as follows:

**Table 5: Capital receipts in £ millions**

£M	2019/20 forecast	2020/21 budget	2021/22 budget	2022/23 budget	2023/24 budget	2023/24 budget
Asset Sales	15.8	28.8	15.2	19.5	5.9	5.5
Loans Repaid	10.4	3.7	5.6	1.4	0.9	0.9
<b>TOTAL</b>	<b>26.2</b>	<b>32.5</b>	<b>20.8</b>	<b>20.9</b>	<b>6.8</b>	<b>6.4</b>

## 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. 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 31<sup>st</sup> December 2019, the Authority held £491.5m of borrowing (£386.5m long term and £105m short term) at an average rate of 4.1% and £86.3m of investments at an average rate of 0.70%.

## 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 0.9%) and long-term fixed rate loans where the future cost is known but higher (currently around 3.3%).

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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	2019/20 forecast	2020/21 budget	2021/22 budget	2022/23 budget	2023/24 budget	2024/25 budget
Debt (incl. PFI & Leases)	369.8	341.1	316.1	304.7	303.8	303.9
Capital Financing Requirement	821.8	969.9	1,135.2	1,224.0	1,241.6	1,228.5

- 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	2019/20 forecast	2020/21 budget	2021/22 budget	2022/23 budget	2023/24 budget	2024/25 budget
Authorised Limit	1,200.0	1,200.0	1,300.0	1,400.0	1,500.0	1,600.0
Operational Boundary	1,000.0	1,000.0	1,100.0	1,200.0	1,300.0	1,400.0

- 8.2 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.

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- 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	2019/20 forecast	2020/21 budget	2021/22 budget	2022/23 budget	2023/24 budget	2024/25 budget
Short term investments	110.0	90.0	70.0	50.0	50.0	50.0
Long term investments	102.9	130.3	153.8	177.3	177.3	177.3

- 9.3 Further details on treasury investments are contained within the Council's treasury management strategy.
- 9.4 Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Chief Finance Officer, 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 and local businesses / service providers 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 / generate a profit after all costs.
- 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 key worker units and street properties. These schemes aim to alleviate affordable housing pressures.

**11.0 Commercial Activities**

11.1 The Council can invest in commercial property purely or mainly for financial gain. Total commercial investments are currently valued at £9.0M consisting of 34 individual property assets generating £0.55M PA, or a yield of 6.1%.

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

<b>ASSET TYPES</b>	<b>No. of Assets</b>	<b>Value £M</b>	<b>Income PA £M</b>
Operational	48	173.0	0.86
Commercial	34	9.0	0.55
Community Groups	40	15.8	0.18
Education	48	294.0	0
Regeneration	35	26.3	0.12
Non HRA Housing	7	4.1	0.1
<b>TOTAL</b>	<b>212</b>	<b>522.4</b>	<b>1.81</b>

11.2 With financial return being the main objective, 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.

**12.0 Liabilities**

12.1 In addition to debt of £369.8M detailed above, the Council is committed to making future payments to cover its pension fund deficit (valued at £248M – Draft Report March 2020).

**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 financing costs to net revenue stream**

£M	2019/20 forecasts	2020/21 budget	2021/22 budget	2022/23 budget	2023/24 budget	2024/25 budget
Financing costs	12.2	11.2	12.5	15.1	17.0	25.1
Proportion of net revenue stream %	4.6%	3.9%	4.2%	5.0%	5.6%	8.3%

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 2020/21, 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 pays for junior staff to study towards relevant professional qualifications including CIPFA, ACT (treasury) & 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 more cost effective than employing such staff directly, and ensures that the Council has access to knowledge and skills commensurate with its risk appetite.