

# Capital Strategy Report 2023/24

## 1. Introduction

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.

## 2. Capital Expenditure and Financing

Capital expenditure is where the Council spends money on assets, such as property or vehicles, which 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.

In 2023/24, the Council is planning capital expenditure of £35m as summarised below:

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

	<b>2022/23 forecast</b>	<b>2023/24 budget</b>	<b>2024/25 budget</b>	<b>2025/26 budget</b>
General Fund services	22,913	35,358	30,095	21,522

The capital expenditure forecast for 2023/24 continues to be monitored and reviewed, in terms of both project delivery and affordability. The Council is currently working on a long term capital expenditure forecast and will update the above table when this becomes available.

**Governance** – The Council’s Capital Programme is agreed on a yearly basis by the Strategic Policy & Resources Committee in its role as the Council’s investment decision maker. All capital projects must go through a 3-stage approval process and decisions on which projects are added to the Capital Programme and which projects progress are also taken by SP&R Committee. This provides assurance as to the level of financial control and allows Members to properly consider the opportunity costs of approving capital projects. The Physical Programmes Department and Financial Services calculate the financing cost of all proposals, including emerging proposals. As part of the final investment decision it must be confirmed that any project is within the affordability limits of the Council.

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 and leasing). The planned financing of the above expenditure is as follows:

*Table 2: Capital financing in £thousands*

	<b>2022/23 forecast</b>	<b>2023/24 budget</b>	<b>2024/25 budget</b>	<b>2025/26 budget</b>
External sources	0	0	0	0
Own resources	16,897	18,218	10,443	14,050
Debt	6,016	17,140	19,652	7,472
<b>TOTAL</b>	<b>22,913</b>	<b>35,358</b>	<b>30,095</b>	<b>21,522</b>

Debt is only a temporary source of finance, since loans and leases must be repaid, usually from revenue which is known as minimum revenue provision (MRP). Alternatively, proceeds from selling capital assets (known as capital receipts) may be used to replace debt finance. Planned MRP is as follows:

*Table 3: Repayment of debt finance in £thousands (MRP)*

	<b>2022/23 forecast</b>	<b>2023/24 budget</b>	<b>2024/25 budget</b>	<b>2025/26 budget</b>
Own resources	8,669	9,313	10,477	11,042

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 repay debt. The CFR is expected to increase by £8m during 2023/24. 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 £thousands*

	<b>31.3.2023 forecast</b>	<b>31.3.2024 budget</b>	<b>31.3.2025 budget</b>	<b>31.3.2026 budget</b>
General Fund services	132,480	140,307	149,482	145,912

**Asset Management** – The Council is committed to ensuring that all Capital projects contribute to the strategic direction of the city and continue to be of long term use. The Council is currently in the process of looking at its Asset Management Strategy and is implementing a new Asset Management System to support the strategic objectives of better financial management, information management, planning and performance and asset management

**Asset disposals:** When a capital asset is no longer needed, it may be sold so that the proceeds, known as capital receipts, can be spent on new assets or to repay debt. Repayments of capital grants, loans and investments also generate capital receipts. The Council plans to receive £5m of capital receipts in the coming financial year as follows:

Table 5: Capital receipts in £thousands

	<b>2022/23 forecast</b>	<b>2023/24 budget</b>	<b>2024/25 budget</b>	<b>2025/26 budget</b>
Asset sales	£375	£4,946	£3,200	£1,996
Loans repaid	0	0	0	0
<b>TOTAL</b>	<b>£375</b>	<b>£4,946</b>	<b>£3,200</b>	<b>£1,996</b>

### 3. Treasury Management

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.

The Council currently has £44m borrowing and due to legacy loans taken at higher rates in the past and transfers of debt under Local Government, the average interest rate of these loans is 7.87%. The council also has £21m treasury investments at current average rate of 2.67%.

**Borrowing strategy:** 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 4.5%) and long-term fixed rate loans where the future cost is known but higher (currently over 5%).

Projected levels of the Council's total outstanding debt (which comprises borrowing, leases and transfers from local government reorganisation) are shown below, compared with the capital financing requirement (see above).

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

	<b>31.3.2023 forecast</b>	<b>31.3.2024 budget</b>	<b>31.3.2025 budget</b>	<b>31.3.2026 budget</b>
Debt (incl. PFI & leases)	43,782	53,064	71,447	79,925
Capital Financing Requirement	132,480	140,307	149,482	145,912

Statutory guidance is that debt should remain below the capital financing requirement, as can be seen from table 6.

**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 that cash and investment balances are kept to a minimum level of £10m at each year-end. This benchmark is currently £40m and is forecast to rise to £80m over the next three years.

*Table 7: Prudential Indicator: Borrowing and the liability benchmark £thousands*

	<b>31.3.2023 forecast</b>	<b>31.3.2024 budget</b>	<b>31.3.2025 budget</b>	<b>31.3.2026 budget</b>
Outstanding borrowing	43,782	53,064	71,447	79,925
Liability Benchmark	39,619	54,946	73,422	80,351

The table shows that the Council's borrowing is currently above its liability benchmark. The Council is projecting to borrow over the next few years to meet capital expenditure requirements. This external borrowing is currently projected to be slightly lower than the estimated liability benchmark over the next three years, based on current forecasts. Work is progressing on the long term capital expenditure forecasts and when finalised the budget figures in the above table will be reviewed and amended accordingly.

**Affordable borrowing limit:** The Council is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt) each year and to keep it under review. In line with statutory guidance, a lower "operational boundary" is also set as a warning level should debt approach the limit.

*Table 8: Prudential Indicators: Authorised limit and operational boundary for external debt in £thousands*

	<b>2023/24 limit</b>	<b>2024/25 limit</b>	<b>2025/26 limit</b>
Authorised limit – borrowing	140,307	149,482	145,912
Authorised limit – PFI and leases	0	0	0
Authorised limit – total external debt	140,307	149,482	145,912
Operational boundary – borrowing	124,307	133,482	129,912
Operational boundary – PFI and leases	0	0	0
Operational boundary – total external debt	124,307	133,482	129,912

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

The Council's policy on treasury investments is to prioritise security and liquidity over yield, that is to focus on minimising risk rather than maximising returns. Cash that is likely to be spent in the near term is invested securely, for example with the government, other local authorities or selected high-quality banks, to minimise the risk of loss. 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 9: Treasury management investments in £thousands*

	<b>31.3.2023 forecast</b>	<b>31.3.2024 budget</b>	<b>31.3.2025 budget</b>	<b>31.3.2026 budget</b>
Near-term investments	15,000	12,000	12,000	12,000
Longer-term investments	0	0	0	0
<b>TOTAL</b>	<b>15,000</b>	<b>12,000</b>	<b>12,000</b>	<b>12,000</b>

**Governance:** Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Director of Finance and staff, who must act in line with the treasury management strategy approved by Strategic Policy and Resources Committee (SP&R). Tri-annual reports on treasury management activity are currently presented to SP&R. From 1 April 2023, the frequency of these reports will be reviewed in light of the recent changes to the CIPFA Prudential Code. Reports may be presented on a quarterly basis, where the SP&R committee is responsible for scrutinising treasury management decisions.

### **Liabilities**

In addition to debt of £44m detailed above, the Council is making payments to cover its pension fund liability. It has also set aside £5.4m to cover risks of insurance claims and Landfill Closure. The Council is also at risk of having to pay for its share of the ARC 21 Joint Committee contingent liability but has not put aside any money.

**Governance:** Decisions on incurring new discretionary liabilities are taken by departmental Chief Officers in consultation with the Director of Finance. The risk of liabilities crystallising and requiring payment is monitored by central finance and reported quarterly to the Director of Finance. New liabilities exceeding £1m are reported to Strategic Policy and Resources Committee for approval/notification as appropriate.

## **4. Revenue Budget Implications**

Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP are charged to revenue. The net annual charge is known

as financing costs; this is compared to the net revenue stream i.e. the amount funded from the District Rate and general government grants.

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

	<b>2022/23 forecast</b>	<b>2023/24 budget</b>	<b>2024/25 budget</b>	<b>2025/26 budget</b>
Financing costs (£'000)	9,731	10,978	13,204	14,288
Proportion of net revenue stream	5.44%	5.69%	6.85%	7.41%

**Sustainability:** Due to the very long-term nature of capital expenditure and financing, the revenue budget implications of expenditure incurred in the next few years may extend for up to 50 years into the future. The Director of Finance is satisfied that the proposed capital programme is prudent, affordable and sustainable due to the processes in place to scrutinise any plans coming forward and are designed to highlight not only the ongoing financing costs but also the recurring running costs to ensure they remain within the affordability limits identified and agreed by the Council.

## **5. Knowledge and Skills**

The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. For example, the Director of Finance is a qualified accountant with over 25 years' experience. The Council pays for junior staff to study towards relevant professional qualifications including CIPFA, ACT (treasury), ACCA, etc.

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.