Attachment 2

Watford Borough Council

Capital Strategy

2024/25

WATFORD BOROUGH COUNCIL

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1. **Introduction**

1.1 The purpose of the capital strategy (the Strategy) is to set out a clear and concise view of how the council determines it priorities for capital investment, decides how much it can afford to borrow and sets its risk appetite. It is intended to give a high level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services along with an overview of how associated risk is managed and the implications for future financial sustainability.

1.2 The framework the government uses to control how much councils can afford to spend on capital investment is known as the Prudential Framework. The objectives of the Prudential Code, which sets out how this framework is to be applied, are to ensure that local authorities' capital investment plans are:

- affordable, prudent and sustainable;
- that treasury management decisions are taken in accordance with good professional practice; and
- that local strategic planning, asset management planning and proper option appraisal are supported.

1.3 This capital strategy sets out how Watford Borough Council will achieve the objectives set out above. It is supported by the following policies which are included as appendices to the strategy:

Appendix 1: Treasury Management Strategy Statement
Appendix 2: Property Investment Strategy
Appendix 3: Minimum Revenue Provision Policy

2. **Capital Investment Programme**

Capital Investment Programme - Expenditure

2.1 Capital Investment is the term used to cover all expenditure by the council that can be classified as capital under legislation and proper accounting practice. This includes expenditure on:

- property, plant and equipment,
- intangible assets,
- heritage assets,
- investment properties, and
- loans to subsidiaries and joint ventures.

2.2 Property plant and equipment includes assets that have physical substance and are held for use in the production or supply of goods and services, for rental to others, or for administrative purposes. They are expected to be used during more than one financial year. Expenditure on the acquisition, creation or enhancement of these assets is capitalised on an accruals basis, provided that the Council is likely to benefit from the future economic benefits or service potential and the cost of the item can be measured reliably. Expenditure on repairs and maintenance is charged to the revenue account when it is incurred.

2.3 Intangible assets are assets that are not physical in nature but still deliver value to the organisation over a period of time such as ICT software.

2.4 Heritage Assets are held with the objective of increasing knowledge, understanding and the appreciation of the Council's history and local area.

2.5 Investment properties are those that are used solely to earn rentals and/or for increases in value. The definition is not met if the property is used in any way for the delivery of services or production of goods or is held for sale.

2.6 The Council does not capitalise borrowing costs for assets under construction with the exception of development undertaken by joint ventures. The council has a number of joint ventures for development where borrowing costs in relation to assets under construction are routinely capitalised and repaid from the proceeds of sale.

2.7 Detailed accounting policies in relation to assets and capital expenditure may be found in the annual statement of accounts.

2.8 A summary of the proposed capital programme is set in the table below. New major schemes will be subject to individual business cases, including identification of resources and an assessment of affordability. A detailed breakdown of the Capital Programme is set out in Attachment 3 Directorate Budget Book 2024/25 to 2026/27. The monitoring of the capital investment programme is reported to the Budget Report and reported on a quarterly basis to Finance Scrutiny Committee and Cabinet.

Capital Investment Programme	Actual Investment 2022/23 £m	Forecast Year End 2023/24 £m	Proposed Budget 2024/25 £m	Proposed Budget 2025/26 £m	Proposed Budget 2026/27 £m
Corporate, Housing & Wellbeing	10.615	10.762	12.041	1.202	0.810
Place	12.610	21.936	17.068	8.631	2.977
Corporate Strategy & Comms	-	-	-	-	0.065
Strategic Finance	10.132	1.188	3.807	0.677	0.677
Total Capital Investment	**33.356**	**33.885**	**32.916**	**10.510**	**4.528**

Capital Investment Programme - Funding

2.9 The Capital Investment Programme can be funded from the following sources:

2.10 Government Grants & Other Contributions: These are grants for specific purposes which may be available from the Government, e.g. Disabled Facility Grants. The Council can also attract partnership funding from other local authorities and agencies e.g. Local Enterprise

Partnership (LEP). The Council has also benefited in the past from other funding such as lottery grants.

2.11 Section 106 Contributions and Community Infrastructure Levy: These are contributions from developers secured through the planning process to the public services, amenities and infrastructure required for the development.

2.12 Capital Receipts: Capital receipts are derived when selling assets such as land.

2.13 Revenue Contributions: Revenue balances from the General Fund may be used to directly fund capital expenditure.

2.14 Capital Expenditure Reserves: The Council has reserves which it has put aside for capital expenditure.

2.15 Borrowing: The Council is allowed to borrow to support its capital expenditure as long as this is prudent, sustainable, and affordable.

2.16 The capital programme includes an assessment of likely available resources to finance capital expenditure. The funding for the latest capital programme is set out in the table below:

Funding Type	2022/23 Actual Funding £m	2023/24 Year End Forecast £m	2024/25 Proposed Budget £m	2025/26 Proposed Budget £m	2026/27 Proposed Budget £m
Grants & Contributions	8.305	1.919	8.613	0.055	0.057
Reserves	0.008	0.113	0.194	0.054	-
Capital Receipts	2.487	7.602	1.085	-	-
Section 106 & CIL Contributions	0.464	2.762	0.600	0.466	0.500
Land Transfer	-	3.830	5.626	6.900	0.227
Borrowing (Internal and External)	22.094	17.659	16.799	3.035	3.744
Total Funding Applied	**33.356**	**33.885**	**32.916**	**10.510**	**4.528**

Property investment

2.17 Lambert Smith Hampton (LSH) were commissioned by the Council in 2014 to undertake a strategic property review. The outcome of this process was reported to the March 2015 Cabinet which resulted in a number of decisions on the general aims of the Council, including establishing a Property Investment Board.

2.18 The overarching Property Investment Strategy is included at Appendix 2. The strategy objectives have been updated to reflect the latest PWLB lending terms and conditions (revised November 2020) and PWLB Guidance (issued August 2021). The primary aim of the revision to the terms and conditions was to prevent the use of PWLB borrowing to finance investments made on a debt for yield basis; specifically the purchase of investment assets. Access to the PWLB will be restricted for authorities planning to acquire investment assets in the current or following three years, including active portfolio management where the acquisition of a new asset is funded by the sale of an existing asset. However, the Prudential

Code for Capital Finance confirms that authorities with commercial property may continue to invest in the repair, renewal and updating of their existing commercial properties. Authorities can also continue to invest in regeneration projects within their local area.

2.19 The Portfolio Holder for Property Resources and Customer Service has delegated powers to agree to acquisitions and disposals up to £10,000,000 and the Executive Director of Place and Associate Director for Property and Asset Management and Property Team Manager (investment assets) have delegated powers to agree to acquisitions and disposals up to £3,000,000. Both of these subject to a full written business case being prepared and signed off by Finance and Legal and the acquisition/disposal being in line with the Property Investment Board Investment Strategy.

Other investments

2.20 Watford Borough Council has established a commercial trading company, Watford Commercial Services Ltd, of which it has 100% ownership. At present the only activity carried out through the company is Watford's investment in Hart Homes Development LLP, of which it has a 50% share. This is a joint venture with Watford Community Housing, set up to deliver housing development within the area. In addition, Watford Borough Council has a direct 50% share in Hart Homes (Watford) Ltd which was set up for the ongoing management of rental properties developed by Hart Homes Development LLP.

2.21 Watford Borough Council has set up a Local Asset Backed Vehicle (LABV) (the Watford Health Campus Partnership LLP) with Kier to develop Watford Health Campus, known as Watford Riverwell. Under the LABV model, the public sector transfers land and funding when required into the partnership and the private sector matches the value of the public sector assets to deliver the joint venture's objectives, empowering the joint venture (by way of land and money) to deliver the regeneration and transformation activities agreed between the parties.

2.22 In July 2019, the Council acquired Croxley Park (a local business park) through a finance lease. Under proper accounting practice for finance lease arrangements, both the asset and lease liability are recognised on the Council's balance sheet. The finance lease is a debt instrument and forms part of the Council's total external debt. The external debt in relation to the finance lease is disclosed separately within the Council's authorised limit and operational boundary for borrowing to distinguish this from external borrowing in the form of loans.

2.23 All investment activity in relation to other investments is managed through the capital programme and revenue budget process. The activity of the joint ventures, investments in partnerships and companies is included within the Group Accounts which are prepared as part of the Annual Statement of Accounts.

Future Investment

2.24 Future Investment Schemes will be assessed on the basis of a full business case which will include full resourcing for the project and an assessment of affordability. Priority areas for future capital investment are:

- Schemes through the joint ventures that generate a surplus and increase the supply of housing locally.

- Schemes that generate revenue budget savings or income.
- Schemes that allow the council to benefit from future economic regeneration potential within the local area.

2.25 The Council will continue to seek opportunities to work in partnership with others to promote economic development and the provision of housing within Watford's wider economic area. This will include continuing to work with current partners including Kier for the Riverwell project and Watford Community Housing as the main local registered social provider.

2.26 Where appropriate, the Council will utilise Watford Commercial Services Ltd to allow it to work more closely with providers and exploit future commercial opportunities.

3. Treasury Management

3.1 The Council is required to operate a balanced budget over the medium term which, after allowing for contributions to and from reserves, broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's low risk appetite, providing the requisite liquidity before considering investment return.

3.2 The Treasury Management Strategy Statement (Appendix 1), details the policies, practices, objectives and approaches to risk management of its treasury management activities, which is to be monitored by the Audit Committee. The Council's investment strategy's primary objectives are safeguarding the repayment of the principal and interest of its investments on time, and then ensuring adequate liquidity, with the investment return being the final objective. The strategy allows the Chief Finance Officer, in consultation with the Portfolio Holder for Property, Resources and Customer Service, the delegated authority to approve any variation to the Treasury Management Strategy during the year with the objective of maximising the Council's returns without significantly increasing risk. This could include use of other investment instruments such as Government bonds or Gilts.

3.3 The Council's Treasury Management advisors, Link Group have provided the following interest rate forecast for the medium term:

Link Group Interest Rate View	07.11.23												
	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26
BANK RATE	5.25	5.25	5.25	5.00	4.50	4.00	3.50	3.25	3.00	3.00	3.00	3.00	3.00
3 month ave earnings	5.30	5.30	5.30	5.00	4.50	4.00	3.50	3.30	3.00	3.00	3.00	3.00	3.00
6 month ave earnings	5.60	5.50	5.40	5.10	4.60	4.10	3.60	3.40	3.10	3.10	3.10	3.10	3.10
12 month ave earnings	5.80	5.70	5.50	5.20	4.70	4.20	3.70	3.50	3.30	3.30	3.30	3.30	3.30
5yr PWLB	5.00	4.90	4.80	4.70	4.40	4.20	4.00	3.80	3.70	3.60	3.50	3.50	3.50
10 yr PWLB	5.10	5.00	4.80	4.70	4.40	4.20	4.00	3.80	3.70	3.70	3.60	3.60	3.50
25 yr PWLB	5.50	5.30	5.10	4.90	4.70	4.50	4.30	4.20	4.10	4.10	4.00	4.00	4.00
50 yr PWLB	5.30	5.10	4.90	4.70	4.50	4.30	4.10	4.00	3.90	3.90	3.80	3.80	3.80

4. Prudential Indicators

4.1 All local authorities are required to set prudential indicators for the forthcoming year and following years before the beginning of the forthcoming year. The indicators must be set by full Council.

4.2 The prudential indicators fall into two main categories of 'Prudence' and 'Affordability'. The indicators for Prudence are further separated between those relating to the Council's capital expenditure plans and those relating to levels of external debt.

Prudence – Capital Expenditure

4.3 The table below sets out the Council's estimates of capital expenditure over the medium term financial planning period and the estimated impact on the Council's Capital Financing Requirement (CFR). The table also includes the actual capital expenditure for 2022/23 and the actual CFR as at 31 March 2023.

	2022/23 Actual £m	2023/24 Forecast £m	2024/25 Estimate £m	2025/26 Estimate £m	2026/27 Estimate £m
CFR relating to Capital programme					
Opening CFR		85.033	97.145	111.197	109.376
Proposed Capital Expenditure		33.885	32.916	10.510	4.528
Capital Financing:					
Grants		(1.919)	(8.613)	(0.055)	(0.057)
Reserves		(0.113)	(0.194)	(0.054)	0.000
Capital Receipts		(7.602)	(1.085)	0.000	0.000
Section 106 and CIL		(2.762)	(0.600)	(0.466)	(0.500)
Land Transfer		(3.830)	(5.626)	(6.900)	(0.227)
Total Financing		(16.226)	(16.117)	(7.475)	(0.784)
MRP		(2.068)	(2.666)	(3.472)	(3.662)
Repayment of loans from JVs		(3.478)	(0.081)	(1.384)	(1.088)
Closing CFR relating to Capital programme*	**85.033**	**97.145**	**111.197**	**109.376**	**108.370**
CFR relating to Croxley Park Finance Lease					
Opening CFR		225.046	221.098	217.150	213.202
MRP on Finance Lease		(3.948)	(3.948)	(3.948)	(3.948)
Closing CFR relating to Finance Lease	**225.046**	**221.098**	**217.150**	**213.202**	**209.254**
Total Opening CFR		**310.079**	**318.243**	**328.347**	**322.578**
Total Closing CFR	**310.079**	**318.243**	**328.347**	**322.578**	**317.624**
Movement in the CFR		8.164	10.104	(5.769)	(4.954)

*Note the CFR is subject to restatement following the conclusion of the external audits 2020/21 to 2022/23

4.4 The CFR is the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's underlying borrowing need. Any capital expenditure, which has not immediately been paid for, will increase the CFR. An increase in the CFR does not necessarily mean that the council will borrow externally to fund the increase. The Council manages its cash balances as a whole and may choose to use internal cash (generated by holding reserves and through timing differences between income and expenditure).

Prudence – External Debt

4.5 There are two limits on external debt: the ‘Operational Boundary’ and the ‘Authorised Limit’. Both are consistent with existing plans and the proposals in the budget report for capital expenditure and financing, and with approved treasury management policy statement and practices.

4.6 These prudential indicators ensure that over the medium term, net borrowing (borrowings less investments) will only be for a capital purpose. Gross external borrowing should not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional CFR for 2023/24 and next two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes.

4.7 The Operational Boundary is the limit beyond which external borrowing is not normally expected to exceed. In most cases this would link directly to the authority’s plans for capital expenditure, its estimates for CFR and its estimate of cashflow requirements for the year for all purposes. The Council may need to borrow, this limit represents a contingency should the need arise.

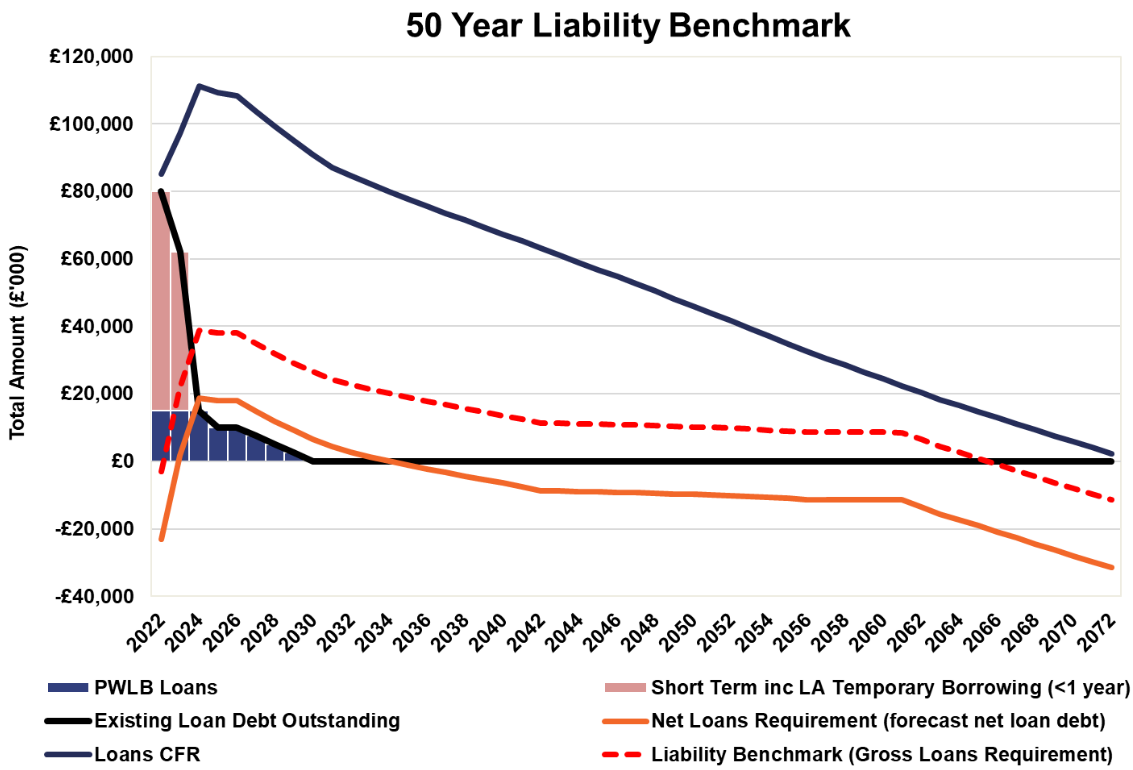
Operational Boundary	2023/24 £m	2024/25 £m	2025/26 £m	2026/27 £m
Borrowing - Capital Programme	50.000	30.000	40.000	40.000
Finance Lease – Croxley Park	222.000	218.000	214.000	210.000
Total	272.000	248.000	254.000	250.000

4.8 The Authorised Limit for External Borrowing controls the overall level of borrowing and represents the limit beyond which external long and short term borrowing is prohibited, and this limit needs to be set or revised by the Council. It reflects the level of borrowing which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. It is the expected maximum borrowing need with some headroom for unexpected movements. This is the statutory limit determined under section 3 (2) of the Local Government Act 2003.

Authorised Limit	2023/24 £m	2024/25 £m	2025/26 £m	2026/27 £m
Borrowing	64.500	105.000	115.000	115.000
Finance Lease – Croxley Park	227.000	223.000	218.000	213.000
Total	**291.500**	**328.000**	**333.000**	**328.000**

Treasury Management Indicator – The Liability Benchmark

4.9 The Treasury Management Code of Practice requires local authorities to calculate their Liability Benchmark. The benchmark includes a projection of external debt required over the long term to fund the organisation's approved budgets and plans compared to the Forecast of total borrowing outstanding. The benchmark should be used to evaluate the amount, timing and maturities needed for new borrowing in relation to the organisation's planned borrowing needs in order to avoid borrowing too much, too little, too long or too short.



Affordability

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

4.11 In considering the affordability of its capital plans, the authority is required to consider its forecast financial position, including all of the resources currently available to it and estimated for the future, together with the totality of its capital, borrowing and investment plans, income and expenditure forecasts and risks.

4.12 The following indicators provide an indication of the impact of the capital investment plans on the Council's overall finances.

Financing costs to net revenue stream

4.13 This indicator identifies the trend in the cost of capital, (borrowing and other long-term obligation costs net of investment income), against the net revenue stream. The net revenue stream is the Council's core funding of Council Tax, Business rates, and unringfenced central government grants. Investment income includes interest from Treasury Management activities and interest from loans to joint ventures and subsidiaries. The calculation for cost of capital excludes the financing costs in relation to Croxley Business

Park Finance Lease which are reflected in the net income from the Business Park in paragraph 4.15.

	2022/23 Actual £m	2023/24 Forecast £m	2024/25 Estimate £m	2025/26 Estimate £m	2026/27 Estimate £m
Cost of Capital	(0.026)	1.731	2.810	3.490	3.707
Net Revenue Stream	13.685	14.260	14.911	14.704	15.209
Ratio %	**-0.19%**	**12.14%**	**18.84%**	**23.74%**	**24.37%**

Net income from commercial investment to net revenue stream

4.14 This indicator is intended to show the financial exposure of the authority to the loss of income.

4.15 Net income from commercial investments comprises net income from financial investments (other than treasury management investments), together with net income from other assets held primarily for financial return, such as commercial property.

	2022/23 Actual £m	2023/24 Forecast £m	2024/25 Estimate £m	2025/26 Estimate £m	2026/27 Estimate £m
Commercial Investment	10.057	11.220	12.877	12.736	11.447
Net Revenue Stream	13.685	14.260	14.911	14.704	15.209
Ratio %	**73.49%**	**78.68%**	**86.36%**	**86.62%**	**75.26%**

5. **Minimum Revenue Provision (MRP) Strategy and Policy Statement**

5.1 The Minimum Revenue Provision (MRP) is designed to pay off an element of the capital spend which has not already been financed from existing revenue or capital resources. The Council is required to make prudent provision, by way of a charge to the revenue account, which means that the repayment of debt is enabled over a period that is reasonably commensurate with that over which the capital expenditure provides benefits.

5.2 The Council is also able to increase the rate it reduces its CFR by undertaking additional voluntary payments (voluntary revenue provision - VRP) in addition to any MRP; this is not currently the Council's policy.

5.3 Government Regulations require the Council to approve a MRP Statement in advance of each year. The MRP policy statement for 2024/25 is at Appendix 3.

5.4 Where the Council decides to borrow to fund capital expenditure the annual cost of borrowing is included within the revenue budget. All business cases for capital investment must set out the level of MRP proposed to ensure that the repayment of any debt can be made in a period commensurate with the period the expenditure provides benefit or makes returns. The business case must also set out the forecast cost of interest payments so that the full cost of delivering and financing the scheme is considered when assessing the value for money of the scheme.

6. Skills, Knowledge and Professional Advice

6.1 The Council has a shared service with Three Rivers District Council for the provision of the finance function allowing access to a greater range of professional skills than would otherwise be available if each council had a separate team.

6.2 Watford Borough Council uses Lambert Smith Hampton Investment Management (LSHIM) to provide advice on and management of its investment property portfolio. LSHIM also provide ad-hoc advice where required on other projects. The council procures external advisers on all major projects.

6.3 The Council contracts with Link Asset Services for the provision of Treasury Management advice. Link Asset Services provide non-regulated advice on the management of the council's cash flows, investments and borrowings and a markets information service. The Councils VAT advisers are PSTax.

7. Risk

7.1 Financial risks are closely monitored as a separately identifiable part of the corporate risk management framework.

7.2 The Council's risk appetite continues to evolve to respond to the wider economic and regulatory environment. Delivery of an ambitious capital programme and management of a commercial investment portfolio have inherent risks linked to external factors such as interest rates, inflation and the economy. These risks are understood and managed.

7.3 The Council takes advice from its professional advisers to both identify and mitigate the key risks it faces and ensures that all decisions are made with an understanding of the risks involved. The ongoing management of risk is a key function of the Council's Property Investment Board which routinely takes advice from LSHIM.

7.4 Whilst recognising the importance of generating income to support services, the Council will ensure that its external income is actively managed to safeguard the future financial sustainability of the council. In this respect it will continue to seek to balance income from its commercial investment activities against its overall level of risk and the amount of reserves available to mitigate this risk. The Council holds two reserves specifically to manage the risk on commercial and investment income. These are the Croxley Business Park Reserve and the Commercial Risk Reserve (formally Riverwell Reserve). These reserves can be used to protect the general fund from fluctuations in income.

7.5 In assessing the risk of its commercial investments, the Council will consider the level of risk inherent in the income stream, the security held, its ability to realise assets or other security should the need arise, and the level of income received from commercial investments compared to the total income of the council.

Appendix 1

Treasury Management Strategy Statement 2023/24

WATFORD BOROUGH COUNCIL

1. Overview

1.1. This document sets out the Council's Treasury Management Strategy Statement. The Strategy has been developed with reference to and is compliant with the Code of Practice for Treasury Management in the public services (2021 edition) published by The Chartered Institute of Public Finance and Accountancy (CIPFA).

1.2. This Council defines treasury management as: "the management of the local authority's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks".

1.3. The Treasury Management Strategy Statement supports the delivery of the Council's Capital Strategy and provides additional detail on how the Council manages its Treasury Management Activity.

1.4. The Treasury Management Strategy Statement details the policies, practices, objectives and approaches to risk management of its treasury management activities, which is to be monitored by the Audit Committee. The primary objectives of the Treasury Management Strategy Statement are:

- Security - Safeguard the repayment of the principal and interest of its investments on time
- Liquidity - Ensure adequate liquidity to meet obligations as they fall due
- Yield - Investment return is the final objective and is considered after the security and liquidity requirements have been satisfied.

1.5. This statement is reviewed and approved annually by Council alongside the Council's budget, Medium Term Financial Strategy (MTFS) and Capital Strategy.

1.6. This organisation regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation and any financial instruments entered into to manage these risks.

1.7. This organisation acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable, comprehensive performance measurement techniques within the context of effective risk management.

1.8. The Chief Finance Officer in consultation with the Portfolio Holder for Property, Resources and Customer Service has delegated authority to approve any variation to the Treasury Management Strategy Statement during the year with the objective of maximising the Council's returns without significantly increasing risk.

2. Risks

2.1 The key Treasury Management risks are set out in the CIPFA Treasury Management Code of Practice (the "TM Code"). The following paragraphs set out these risks and how they are managed:

Credit and Counterparty Risk - The risk of failure by a counterparty to meet its contractual obligations to the organisation under an investment, borrowing, derivative instrument, or capital, project or partnership financing, particularly as a result of the counterparty's diminished creditworthiness, and the resulting detrimental effect on the organisation's capital or current (revenue) resources.

This risk is managed through the maintenance of a list of authorised counterparties, with separate limits to ensure that the exposure to this risk is limited.

Liquidity Risk - The risk that cash will not be available when it is needed, that ineffective management of liquidity creates additional unbudgeted costs, compromising the organisation's business/service objectives.

This risk is managed through forecasting and the retention by the Council of an adequate working capital balance. In addition, through the Public Works Loan Board and other organisations, the Council is able to access short term borrowing, usually within 24 hours.

Interest Rate Risk - The risk that fluctuations in the levels of interest rates create an unexpected or unbudgeted burden on the organisation's finances against which the organisation has failed to adequately protect itself.

This risk is managed through the placing of different types and maturities of investments, within limits set for the amount of borrowing which may mature in a given time-period, the forecasting and monitoring of the interest budget (with assistance from the Council's retained advisors).

Exchange Rate Risk - The risk that fluctuations in foreign exchange rates create an unexpected or unbudgeted burden on the organisation's finances against which the organisation has failed to adequately protect itself.

The Council does not engage in any significant non-sterling transactions.

Inflation – also called purchasing power risk, is the chance that the cash flows from treasury instruments (such as investments) won't be worth as much in the future because of changes in purchasing power due to inflation.

The Council priorities security and liquidity over yield but where possible investment returns will aim to match inflation to preserve the capital value.

Refinancing Risk - The risk that maturing borrowings, capital, project or partnership financings cannot be refinanced on terms that reflect the provisions made by the organisation for those refinancings, both capital and current (revenue), and/or that the terms are inconsistent with prevailing market conditions at the time.

The timing of loan maturities is monitored along with interest rate forecasts. Officers ensure that due dates are monitored and seek advice from the Council's advisors about when to raise any finance needed.

Legal and Regulatory Risk - The risk that the organisation itself, or an organisation with which it is dealing in its treasury management activities, fails to act in accordance with its legal powers or regulatory requirements and that the organisation suffers losses accordingly.

This risk is managed through the Council's training and development of Officers involved in Treasury Management, the independent oversight of Internal and External Audit, and the advice (for example on the contents of this strategy) taken from the Council's Treasury advisors.

Operational Risk, including Fraud, Error and Corruption - The risk of direct or indirect loss resulting from inadequate or failed internal processes, people and systems or from external events. This includes the risk of fraud, error, corruption or other eventualities in treasury management dealings.

This is managed through the controls in the Council's financial procedures. For example, the segregation of duties between those making investment decisions and those transferring funds.

Price / Market Risk - The risk that through adverse market fluctuations in the value of the principal sums an organisation borrows and invests, its stated treasury management policies and objectives are compromised, against which effects it has failed to adequately protect itself.

The majority of the Council's investments are not traded, but where they are (e.g. Property investment portfolio) the main investments' value comes from the income they generate which is generally long term and secure.

3. Treasury Indicators: Limits to Borrowing Activity

3.1 There are two limits on external debt: the 'Operational Boundary' and the 'Authorised Limit'. Both are consistent with existing plans and the proposals in the budget report for capital expenditure and financing, and with approved treasury management policy statement and practices. These indicators are set out in the Capital Strategy.

3.2 The key difference is that the Authorised Limit cannot be breached without prior approval of the Council. The Operational Boundary is a more realistic indicator of the likely position. The difference between the authorised limit and operational boundary for borrowing is that the authorised limit includes a head room for borrowing for future known capital needs now. The Authorised Limit represents the limit beyond which borrowing is prohibited, and needs to be revised if necessary by members.

3.3 In addition to the limits controlling the total amount of borrowing, further limits are in place to control the Council's exposure to interest rate risk on refinancing. These limits are set out in the following table:

Maturity Structure of Borrowing		
	Lower	**Upper**
Under 12 months	0%	100%
12 months to 2 years	0%	100%
2 years to 5 years	0%	100%
5 years to 10 years	0%	50%
10 years to 20 years	0%	50%
20 years to 30 years	0%	50%
30 years to 40 years	0%	50%
40 years to 50 years	0%	50%

3.4 These limits range between 0% and 100% for loans out to 5 years where there is some degree of accuracy with the forecasts for interest rates. Then for the longer term, loans are limited to 50% of the overall borrowing portfolio maturing in each of the given timeframes. The 50% maximum limit protects the Council from being exposed to high levels of refinancing when interest rates may be substantially higher than they are now.

4. Borrowing Strategy

4.1 The Council's treasury team maintains a cashflow forecast and works its liquidity requirements within this forecast; it may, on rare occasions, be necessary to borrow short-term for cashflow purposes. This will be in the form of short term debt or overdraft facilities and is normally for small amounts for minimum durations. As this is based on need and has a defined repayment period it is not normally included within the limits set above.

4.2 The Council will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates, and will be considered carefully to ensure that value for money can be demonstrated (i.e. the cost of holding does not outweigh the benefits of early borrowing) and that the Council can ensure the security of such funds. Any associated risks will be approved and reported through the standard reporting method.

4.3 The Council's level of external borrowing is expected to fall in the first year of the MTFS and then increase across the remaining period of the MTFS. The Council will divest from investment in three pooled investment funds. This cash will be utilised as internal borrowing to remove the need to refinance maturing short term debt or take additional external borrowing for the Capital Investment Programme in 2024/25. This will reduce the Council's exposure to high interest rates in the short term.

4.4 In the longer-term it will be necessary to refinance internal borrowing with external debt as the Council utilises its revenue and capital earmarked reserves for their intended purposes.

4.5 Officers will monitor interest rate forecasts, and in conjunction with Treasury Management advisors determine the optimum timing and amount of future borrowing.

5. Annual Investment Strategy

5.1 The Council's investment strategy has regard to the Statutory Guidance on Local Government Investments and the TM Code. The Council's investment priorities are security first, liquidity second, then yield.

5.2 Investment instruments identified for use in the financial year and counter-party limits are listed in Annex A under the 'Specified' and 'Non-Specified' Investments categories.

5.3 As part of its diversification of investments, the Council has invested some of its core funds (i.e. funds not immediately required for cashflow reasons) in longer–term investment property instruments. These are in the form of individual assets directly owned by the council. All property investments are controlled through the Property Investment Board (PIB).

5.4 As the Council has an ongoing Capital Financing Requirement, consideration will be given to the sale of investment property as an alternative to external borrowing. The Council will take advice from the Council's appointed property advisors, Lambert Smith Hampton Investment Management (LSHIM). Decisions to divest will take into account property portfolio management best practices and the long term benefits and risks of holding the assets.

5.5 Although the Council has no current investments or plans to invest in pooled property funds, these are permitted under the policy and are an option that could be considered in the future if the Council had a long term cash surplus or an alternative to direct property holdings.

5.6 The Council will divest from the Royal London Asset Management Pooled Funds by 31 March 2025 to reduce the Council's exposure to Price risk, Refinancing Risk and high interest rates on external borrowing by utilising the cash for internal borrowing.

5.7 The 31 March 2025 target coincides with the end of the statutory override which protects authorities from having to recognise change in the fair value of investments (movements in market price) in the Council's budget. From 1 April 2025, gains and losses will need to be recognised in the Council's general fund. Although in the long term funds are expected to grow in value, the volatile nature of the bond and equity markets mean that there can be significant movements in value from year to year.

6. Creditworthiness policy

6.1 The Council will ensure:

- It maintains a policy covering both the categories of investment types it will invest in and the criteria for choosing investment counterparties with adequate security, and monitoring their security. This is set out in the Specified and Non-Specified investment schedule at Annex A.
- It has sufficient liquidity in its investments. For this purpose it will set out procedures for determining the maximum periods for which funds may prudently be committed. These procedures also apply to the Council's prudential indicators covering the maximum principal sums invested.

6.2 The Chief Finance Officer will maintain a counterparty list in compliance with the following criteria in section 7. The criteria will be reviewed regularly and proposed changes will be submitted to Council for approval as necessary in order to provide an overall pool of counterparties considered high quality.

6.3 Credit rating information is supplied by our treasury consultants on all active counterparties that comply with the Council's criteria. Any counterparty failing to meet the criteria would be omitted from the counterparty (dealing) list. Any rating changes, rating watches (notification of a likely change), rating outlooks (notification of a possible longer term change) are provided to officers almost immediately after they occur and this information is considered before dealing.

7. Counterparty Categories

7.1 The Council uses the following criteria in choosing the categories of institutions in which to invest:

- **Banks 1 - Good Credit Quality**
  The Council will only use UK banks or foreign banks trading in the UK in sterling denomination and which meet the Rating criteria.
- **Banks 2 – The Council's Own Banker**
  For transactional purposes, if the bank falls below the above criteria, it will be included, although in this case balances will be minimised as far as possible in both monetary size and time within operational constraints.
- **Bank Subsidiary and Treasury Operations**
  The Council will use these where the parent bank has the necessary ratings outlined above and the parent has provided an indemnity guarantee.
- **Building Societies**
  The Council will use all Societies which meet the ratings for banks outlined above.
- **Specific Public Bodies**
  The Council may lend to Public Bodies other than Local Authorities. The criterion for lending to these bodies is that the loan has been approved by Council.
- **Money Market Funds AAA Rated**
  The Council may lend to Money Market Funds in order to spread its investment risk.
- **Local Authorities**
  A limit of £5m per authority will be applied.
- **Debt Management Deposit Account Facility**
  A Government body which accepts local authority deposits.
- **Council Subsidiaries (non-specified)**
  The Council will lend to its subsidiaries subject to approval of a business case by the Chief Finance Officer in consultation with the Portfolio Holder for Property, Resources and Customer Services. Business cases must be accompanied by an independent assessment of viability, and be subjected to regular monitoring by the Chief Finance Officer.

7.2 The Council will also consider investment in property in accordance with its Property Investment Strategy. All property investments will be dependent on a standalone business case being proven. Further details of counterparty categories and limits are set out Annex A Schedule of Specified and Non-Specified Investments.

8. The Monitoring of Investment Counterparties

8.1 The credit rating of counterparties is monitored regularly. The main rating agencies (Fitch, Moody's and Standard & Poor's) provide credit ratings for financial institutions. The Council receives credit rating information (changes, rating watches and rating outlooks) from Link Asset Services as and when ratings change, and counterparties are checked promptly. The Council considers minimum short term ratings as key criteria in the choice of creditworthy investment counterparties; F1+, P-1 and A-1+ are the highest short term credit ratings of Fitch, Moody's and Standard & Poor's respectively. Minimum Short Term

Ratings, where given, must be met for all categories. On occasion ratings may be downgraded when an investment has already been made. The criteria used are such that a minor downgrading should not affect the full receipt of the principal and interest. Any counterparty failing to meet the criteria will be removed from the list immediately by the Chief Finance Officer, and if required new counterparties which meet the criteria will be added to the list.

8.2 For non-specified investments the progress of the entity against the approved, independently verified business case will be monitored by the Chief Finance Officer.

9. Use of Additional Information Other Than Credit Ratings

9.1 Additional requirements under the TM Code require the Council to supplement credit rating information. Whilst the above criteria rely primarily on the application of credit ratings to provide a pool of appropriate counterparties for officers to use, additional operational market information will be applied before making any specific investment decision from the agreed pool of counterparties. This additional market information (for example Credit Default Swaps, negative rating watches/outlooks) will be applied to compare the relative security of differing investment counterparties.

10. Time and Monetary Limits Applying to Investments

10.1 The time and monetary limits for institutions on the Council's Counterparty List summarised in the table below at paragraph 11.2, are driven by the criteria set out in sections 7 and 8. These limits will cover both Specified and Non-Specified Investments.

11. Exceptional Circumstances

11.1 The criteria for choosing counterparties set out above provide a sound approach to investment in "normal" market circumstances. Whilst Members are asked to approve this base criteria above, under the exceptional current market conditions Chief Finance Officer may temporarily restrict further investment activity to those counterparties considered of higher credit quality than the minimum criteria set out for approval. These restrictions will remain in place until the banking system returns to "normal" conditions. Similarly, the time periods for investments will be restricted.

11.2 Examples of these restrictions would be the greater use of the Debt Management Office Account Deposit Facility (DMADF) – a government body which accepts local authority deposits - money Market Funds, and strongly rated institutions. The credit criteria have been amended to reflect these facilities.

12. Investment Strategy

12.1 In-House Funds - investments will be made with reference to the core balance and cashflow requirements and the outlook for short-term interest rates (i.e. rates for investments up to 12 months).

12.2 Investment Treasury Indicator and Limit - total principal funds invested for greater than one year. These limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment, and are based on the availability of funds after each year-end. The table below provides details of these limits.

Treasury Indicator & Limit	2023/24	2024/25	2025/26	2026/27
Maximum amount invested for periods over one year (Property investment and loans to Council subsidiaries).	£5m	£20m	£20m	£20m

13. Investment Risk & Security Benchmarking

13.1 The Council sets benchmarks for security, liquidity and yield. These benchmarks are simple guides to maximum risk and so may be breached from time to time, depending on movements in interest rates and counterparty criteria. The purpose of the benchmarks is that officers will monitor the current and trend position and amend the operational strategy to manage risk as conditions change. Any breach of the benchmarks will be reported, with supporting reasons in the Mid-Year or Annual Report. The benchmarks are as follows:

Security:
Security of the investments is measured by credit ratings, which is supplied by the three main credit rating agencies (Fitch, Moodys and Standard & Poors). Where investments are made to Council subsidiaries (non-listed), the security is measured through a business case with independent viability assessment.

Liquidity:
The Council sets the following liquidity facilities/benchmarks to maintain:

- Authorised bank overdraft - nil.
- Liquid short term deposits of at least £1.0m available with a week's notice.

The Council has the benefit of instant access to its funds on the general account with Lloyds.

Yield:
The Council benchmarks the yield on its operational cash against SONIA (the Sterling Overnight Index Average). This is a measure of market rates for actual returns on overnight cash deposits. Performance against this indicator is monitored throughout the year.

14. Policy on Environment, Social and Governance (ESG) considerations

14.1 This Council is supportive of the Principles for Responsible Investment (www.unpri.org) and will seek to bring ESG (environmental, social and governance) factors into the decision-making process for investments. Within this, the Council is also appreciative of the Statement on ESG in Credit Risk and Ratings which commits signatories to incorporating ESG into credit ratings and analysis in a systemic and transparent way. The Council uses ratings from Fitch, Moody's and Standard & Poor's to support its assessment of suitable counterparties. Each of these rating agencies is a signatory to the ESG in credit risk and ratings statement, which is as follows:

"We, the undersigned, recognise that environmental, social and governance (ESG) factors can affect borrowers' cash flows and the likelihood that they will default on their debt obligations. ESG factors are therefore important elements in assessing the creditworthiness of borrowers. For corporates, concerns such as stranded assets linked to climate change, labour relations challenges or lack of transparency around accounting practices can cause unexpected losses, expenditure, inefficiencies, litigation, regulatory pressure and reputational impacts.

At a sovereign level, risks related to, inter alia, natural resource management, public health standards and corruption can all affect tax revenues, trade balance and foreign investment. The same is true for local governments and special purpose vehicles issuing project bonds. Such events can result in bond price volatility and increase the risk of defaults.

In order to more fully address major market and idiosyncratic risk in debt capital markets, underwriters, credit rating agencies and investors should consider the potential financial materiality of ESG factors in a strategic and systematic way. Transparency on which ESG factors are considered, how these are integrated, and the extent to which they are deemed material in credit assessments will enable better alignment of key stakeholders.

In doing this the stakeholders should recognise that credit ratings reflect exclusively an assessment of an issuer's creditworthiness. Credit rating agencies must be allowed to maintain full independence in determining which criteria may be material to their ratings. While issuer ESG analysis may be considered an important part of a credit rating, the two assessments should not be confused or seen as interchangeable.

With this in mind, we share a common vision to enhance systematic and transparent consideration of ESG factors in the assessment of creditworthiness."

14.2 The assessment of creditworthiness undertaken by Fitch, Moody's and Standard & Poor's includes analysis of the following ESG factors when assigning ratings:

- ***Environmental:*** *Emissions and air quality, energy and waste management, waste and hazardous material, exposure to environmental impact.*

- ***Social:*** *Human rights, community relations, customer welfare, labour relations, employee wellbeing, exposure to social impacts.*

- ***Governance:*** *Management structure, governance structure, group structure, financial transparency.*

14.3 The Council will continue to evaluate additional ESG-related metrics and assessment processes that it could incorporate into its investment process and will update accordingly.

14.4 The Council does not invest directly in company bonds or equity. However, the Council is exposed to these investment instruments through the use of externally managed pooled investment funds.

14.5 This Council will not invest in pooled funds that invest in companies whose core activities pose a risk of serious harm to individuals or groups, or whose activities are inconsistent with the Council's mission and values e.g.:

a. Human rights abuse (e.g., slave or child labour, political oppression)
b. Activities that damage the environment by extraction of fossil fuels, destruction of habitat, or creation of pollutants
c. Socially harmful activities (e.g., tobacco, gambling)
d. Manufacture of weapons

15. Reporting Requirements

15.1 The Audit Committee has the responsibility for the scrutiny of Treasury Management policies and practices and receives the Treasury Management Strategy Statement for review prior to approval by Council.

15.2 An annual report on the performance of the Treasury Management function, including the effects of the decisions taken and the transactions executed in the past year, and on any circumstances of non-compliance with the organisation's treasury management Strategy Statement is considered by Council following the end of the financial year.

15.3 Council also receives a Mid-Year Treasury Management Report setting out activity to 30 September.

16. Policy on the Use of External Service Providers

16.1 The contract for external treasury management advisors is carried out by Link Asset Services. The Council recognises that responsibility for treasury management decisions remains with the Council at all times and will ensure that undue reliance is not placed upon our external service providers. It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review.

16.2 The Council will also, from time to time, procure specialist advice for ad-hoc pieces of work; this will be procured in accordance with the Council's normal contract procedure rules.

17. Member and Officer Training

17.1 In order to ensure that Members and Officers are sufficiently trained and qualified to monitor and manage the Council's Treasury Management activity, the following measures are in place:

- Ensuring that officers attend suitable courses and seminars to keep their technical knowledge up to date.
- Keeping up to date with CIPFA publications on Treasury Management.
- Regular briefings both by email and face to face with the Council's Treasury advisors.
- Reports and briefing sessions to Members on major changes to Treasury policies and strategies.

Annex A

Schedule of Specified and Non-Specified Investments

Specified Investments

These investments are sterling investments of not more than one-year maturity, or those which could be for a longer period but where the Council has the right to be repaid within 12 months if it wishes. These are considered low risk assets where the possibility of loss of principal or investment income is small. These would include sterling investments with:

- The UK Government (such as the Debt Management Account deposit facility, UK Treasury Bills or a Gilt with less than one year to maturity).
- A local authority, parish council or community council.
- A body that is considered of a high credit quality (such as a bank or building society) with a minimum short term rating of F-1 (or the equivalent) as rated by Standard and Poor's, Moody's or Fitch rating agencies or a Building Society with assets over £1,000m. Non rated Building Societies are non-specified investments.
- Money Market Funds (triple AAA rated only).

Within these bodies, and in accordance with the TM Code, the Council has set additional criteria to set the time and amount of monies which will be invested in these bodies. These criteria are defined in the Treasury Management Strategy.

The ratings criteria and exposure limits are detailed at Schedule 1.

Non-Specified Investments

Non-specified investments are any other type of investment (i.e. not defined as Specified above). The identification and rationale supporting the selection of these other investments and the maximum limits to be applied are set out on the following page.

Non Specified Investment Category	Limit (£ or %)
Any bank or building society that has a minimum long term credit rating of A (or equivalent), for deposits with a maturity of greater than one year (including forward deals in excess of one year from inception to repayment).	£5m
The Council's own banker if it fails to meet the basic credit criteria.	In this instance balances will be minimised as much as possible
Building Societies not meeting the basic security requirements under the specified investments. The operation of some building societies does not require a credit rating, although in every other respect the security of the society would match similarly sized societies with ratings. The Council may use such building societies which were originally considered Eligible Institutions and have a minimum asset size of £5,000m, but will restrict these types of investments to £2m for up to six months.	£2m
Specific Public Bodies The Council can seek Member approval to make loans to other public bodies for periods of more than one year.	£10m
Loans to Council Subsidiaries The Council will lend to its subsidiaries subject to approval of a business case by the Chief Finance Officer in consultation with the Portfolio Holder (Property, Resources and Customer Services). Business cases must be accompanied by an independent assessment of viability, and be subjected to regular monitoring by the Chief Finance Officer.	£10m limit for any single loan
Money Market Funds Appointed through competitive process for the investment of the Croxley Park Reserve	£100m
Other unspecified investments The strategy allows the Chief Finance Officer, in consultation with the Portfolio Holder (Property, Resources and Customer Services), the delegated authority to approve any variation to the Treasury Management Strategy during the year which may be brought about by investigating the opportunity to invest for greater than one year and also to invest in other investment instruments i.e Government bonds, Gilts and investment property with a view of to maximising the Council's returns without significantly increasing risk. This allows the addition of further unspecified investments, subject to conditions which will be generally similar to (e).	£10m

Schedule 1 (A) – UK BANKS

	Minimum Short Term Ratings						
Institution	**Fitch**	**Moody's**	**S&P**				
The Council's own Bankers	F1m	P-1	A-1	If Council's own bankers fall below the minimum long term criteria for UK banks, cash balances will be managed within operational liquidity constraints and balances will be minimised as much as possible.			
Wholly Owned Subsidiaries of UK Clearing Banks Parent Ratings	F1	P-1	A-1	Long Term Credit Rating: AA(F), Aa2(M), AA(S&P)	Long Term Credit Rating: Single A (All agencies)	Long Term Crediting Rating: Lower than A (All Agencies)	Long Term Crediting Rating: Lower than A
Partially Owned Subsidiaries of UK Clearing Banks Parent Ratings	F1	P-1	A-1	Long Term credit Rating: AA(F), Aa2(M), AA(S&P)	Long Term Crediting Rating: Single A (All agencies)	Long Term Credit Rating: Lower than A (All Agencies)	Long Term Credit Rating: Lower than A
	Max Amount / Length:			**£10m** **364 Days**	**£10m** **6 Months**	**£10m** **3 Months**	**£10m** **1 Month**

	Minimum Short Term Ratings			Schedule 1 (B) – Building Societies			
Institution	Fitch	Moody's	S&P				
Building Societies – By Credit Rating	F1	P-1	A-1	Long Term Credit Rating: AA(F), Aa2(M), AA(S&P)	Long Term Credit Rating: Single A (all agencies)	Long Term CreditRating: Lower than A (All Agencies)	Long Term Crediting Rating: Lower than A
Building Societies – by Total Assets				Assets over £15bn	Assets over £5bn	Assets of £2.5bn	Assets of £1bn
	Max Amount / Length:			**£10m** **364 Days**	**£10m** **6 Months**	**£10m** **3 Months**	**£10m** **1 Month**

Schedule 1 (C) – Other Entities	
1. Specific Public Bodies	As approved by Members – up to £10m for up to 10 years
2. Debt Management Deposit Facility (UK Government)	Unlimited – this is the Council's Safe-Haven Deposit facility with the UK Government
3. Money Market Funds (Fixed NAV) (AAA Rated)	£5m per fund
4. Municipal Bond Agency	As approved by Members
5. UK Local Authorities	A Maximum of £5m Applies per Authority. The Council can invest in all UK Local Authorities whether rated or not. The Council will not lend to an authority which is subject to a s.114 notice *without member approval.*

Notes:-

1. F1+, P-1 and A-1+ are the highest short term credit ratings of Fitch, Moody's and Standard and Poor's respectively.
2. Minimum Short Term Ratings - Where given, these must be met, for all categories (except RBS Group).
3. Building Societies - A Building Society has to meet either the ratings criteria or the assets criterion to be included in the category, not both.
4. Maximum amount is the maximum, in total, over all investments, with any one institution (with the exception of RBS Group).

Appendix 2

PROPERTY INVESTMENT STRATEGY

Property Investment Policy

The council's Commercial Property Portfolio was established prior to the changes to the PWLB lending terms (November 2020) and revisions to the Prudential Code of Practice (November 2021) which restrict the ability of local authorities to invest in assets purely for yield. This strategy has been updated to reflect the move from an acquisition strategy to a strategy for maintaining the existing portfolio and income levels.

Objectives

- Maintain income levels within the core portfolio, enhancing where possible without impacting on future income potential.
- Preserve, and where possible increase, the capital value of the portfolio but not at the expense of losing income
- Maintain, and where possible improve the net rental position for Croxley Park as detailed in line with the original purchase objectives
- Rebalance the portfolio by reducing the historic weighting towards Retail and Indirect investments
- Implement a capital expenditure programme and work with tenants to ensure that all assets meet the new Minimum Energy Efficiency Standards (MEES) regulations.
- Target and identify opportunities that meet the Councils sustainability and regeneration objectives
- Consider investment in the residential / PRS sectors through existing land holdings using an appropriate vehicle

How much is invested?

Approximately £145m is currently held in the property portfolio as at the latest valuation date of 31 March 2023.

What type of property?

There are different types of property investment as follows:

- Retail
- Office
- Industrial
- Residential
- Alternatives including Leisure

For risk management purposes it is recommended that no single asset should comprise more than 10% of the whole portfolio and locations should be diverse as should property types. The mix helps to protect the fund against movements that might adversely affect one specific sector which would otherwise have a disproportionate impact.

The current target mix* for the portfolio is as follows:

- Retail 15 - 25%
- Office 15 - 25%
- Industrial 35 - 45%
- Alternatives including hotels, car parks, leisure 10 - 20%

*These allocations are expressed as a % of capital value

What level of financial return?

In general, property can be categorised as prime, secondary or tertiary in terms of its desirability. Yield derives from both capital and rent. Lower yields can indicate that the investment attracts a lower degree of risk due to the ratio of rent to capital and other factors such as location, security and regularity of income.

Property investment returns will differ depending upon the market and the nature of the asset.

Risks:

- There are management costs, risk of rent default and failure to honour maintenance agreements.
- Poor asset management strategy or poor execution of an asset management strategy leads to a fall in asset values (generally property tends to appreciate in value over time, although this will vary by length of lease, covenant status, type and area; however, in most cases, without active asset management the values will go down).
- Property can become functionally obsolete necessitating major refurbishment.
- Without regular repair and maintenance the condition will deteriorate and the responsibility for repairs/maintenance may not always rest with the tenant leading to additional revenue and capital expenditure.
- Certain types of property may become less desirable as time goes by; this can make re-letting difficult or attract a lower calibre of tenant.
- Regulatory risks eg. impact of Minimum Energy Efficiency Standards (MEES) imposing additional cost burden on landlords.

Appendix 3

Minimum revenue provision (MRP) policy statement for 2024/25

The Council is required to pay off an element of the accumulated General Fund capital spend each year (the CFR) through a revenue charge (the minimum revenue provision - MRP), although it is also allowed to undertake additional voluntary payments if required (voluntary revenue provision - VRP).

DLUHC regulations have been issued which require the full Council to approve **an MRP Statement** in advance of each year. A variety of options are provided to councils, so long as there is a prudent provision. The Council is recommended to approve the following MRP statement*:*

From 1 April 2008 for all unsupported borrowing (including PFI and finance leases) the MRP policy will be:

- **Asset life method** – MRP will be based on the estimated life of the assets, in accordance with the regulations (this option must be applied for any expenditure capitalised under a Capitalisation Direction) (option 3);

This option provides for a reduction in the borrowing need over approximately the asset's life.

No MRP provision is made in respect of investments or payments into the Council's wholly owned subsidiary, Watford Commercial Services Ltd, or the Council's joint ventures as these investments are intended to be time-limited and arrangements allow for the repayment of debt at the end of the investment period.

For finance leases the council will charge MRP to its General Fund each year dependant on the life of the underlying asset.