



## **POLICY AND RESOURCES COMMITTEE**

**Tuesday, 15 February 2022**

<b>REPORT TITLE:</b>	<b>INVESTMENT STRATEGY 2022/23</b>
<b>REPORT OF:</b>	<b>DIRECTOR OF RESOURCES (S151 OFFICER)</b>

### **REPORT SUMMARY**

In February 2018, the former Ministry for Housing, Communities and Local Government (MHCLG), (now Department for Levelling Up, Housing and Communities (DLUHC)) published updated 'Guidance on Local Government Investments'. The previous edition covered only Treasury Management investments. In recent years local authorities have had an increasing focus on commercial activities including but not exclusive to property. Such activity has the potential to bring both increased returns and increased positive and negative risk. The revised Guidance on Local Authority Investments requires that a separate Investment Strategy focusing on non-treasury investments is produced and approved annually by Council.

This report fulfils the requirement of the DLUHC to produce an investment strategy that covers non-treasury activities.

This matter affects all Wards within the Borough.

The decisions in this report are key decisions.

### **RECOMMENDATIONS**

The Policy and Resources Committee is requested to recommend to Council the approval of the Investment Strategy for 2022/2023 which includes potential investment in the following activity areas:

1. Commercial Property
2. Service Investments: Loans
3. Service Investment: Shares (non-currently held)
4. Loan Commitments and Financial Guarantees

## SUPPORTING INFORMATION

### 1.0 REASON FOR RECOMMENDATIONS

- 1.1 To fulfil the requirement of the DLUHC to produce an investment strategy that covers non-treasury activities.

### 2.0 OTHER OPTIONS CONSIDERED

- 2.1 This report fulfils the requirement of the DLUHC to produce an investment strategy that covers non-treasury activities. Should the Council not produce a strategy this would conflict against DLUHC guidance. The guidance on investments is issued under section 15(1) of the 2003 Local Government Act and authorities are therefore required to have regard to it. An annual strategy is standard practice and should it become appropriate to amend any key elements of this strategy during the period covered, a revised report will be produced.

### 3.0 BACKGROUND INFORMATION

- 3.1 The Authority invests its money for three broad purposes:
- there is surplus cash as a result of its day-to-day activities, for example when income is received in advance of expenditure (known as **treasury management investments**),
  - to support local public services by lending to or buying shares in other organisations (**service investments**), and
  - to earn investment income (known as **commercial investments** where this is the main purpose)
- 3.2 This investment strategy report meets the requirements of statutory guidance issued by the Government in January 2018 and focuses on the second and third of these categories. DLUHC have acknowledged the increase in commercial activities local authorities are engaged in. The revised guidance requires local authorities to clearly define their approaches and risk appetite for such activity and to gain approval from Council on an annual basis.
- 3.3 A separate report covering the Treasury Management Strategy will also be produced that fulfils the Authority's legal obligation under the Local Government Act 2003 to have regard to both the Chartered Institute of Public Finance and Accountancy (CIPFA) Code and the DLUHC guidance.
- 3.4 A Commercial Strategy was approved by Cabinet on 26<sup>th</sup> November 2018. This strategy takes a commercial approach to service design, management, and decisions, encouraging innovation whilst optimising assets and services to exploit opportunities to generate income surplus for reinvestment, and reduce costs.

## Treasury Management Investments

- 3.5 The Authority typically receives its income in cash (e.g., from taxes and grants) before it pays for its expenditure in cash (e.g., through payroll and invoices). It also holds reserves for future expenditure and collects local taxes on behalf of other local authorities and Central Government. These activities, plus the timing of borrowing decisions, may lead to a cash flow surplus which is invested in accordance with guidance from CIPFA. The daily balance of treasury management investments is expected to fluctuate between £20m and £50m during the 2022/23 financial year.
- 3.6 Wirral Council defines its treasury management activities as:
- “the management of the organisation’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.”*
- 3.7 **Contribution:** The contribution that these investments make to the objectives of the Authority is to support effective treasury management activities. Investment returns contribute towards funding services, whilst reduced borrowing costs allow resources to be allocated elsewhere.
- 3.8 **Further details:** Full details of the Authority’s policies and its plan for 2022/23 for treasury management investments are covered in a separate document, the Treasury Management Strategy.

### Service Investments: Loans

- 3.9 **Contribution:** The Council lends money to its subsidiaries e.g., Edsential Community Interest Company (by way of a credit facility), and local businesses to support local public services and stimulate local economic growth.
- 3.10 **Security:** The main risk when making service loans is that the borrower will be unable to repay the principal lent and/or the interest due. Appropriate due diligence is undertaken on loan applications and collateral sought to offset risk. To further limit this risk and ensure that total exposure to service loans remains proportionate to the size of the Authority, upper limits on the outstanding loans to each category of borrower have been set as per the table below. Loans should be self-financing with returns covering financing and administrative costs plus any return.

Table 1: Loans for service purposes.

Category of borrower	31.03.2022 Estimated			2022/23
	Balance Owing £000	Loss allowance £000	Estimated Net figure in accounts £000	Approved Limit £000
Subsidiaries	2,607	2,607	0	10,000
Local businesses	350	350	0	10,000
<b>TOTAL</b>	<b>2,957</b>	<b>2,957</b>	<b>0</b>	<b>20,000</b>

- 3.11 Accounting standards require the Authority to set aside a loss allowance (where appropriate) for loans, reflecting the likelihood of non-payment. The figures for loans in the Authority's Statement of Accounts are shown net of this loss allowance. However, the Authority makes every reasonable effort to collect the full sum lent and has appropriate credit control arrangements in place to recover overdue repayments.
- 3.12 **Risk assessment:** The Authority assesses the risk of loss before entering and whilst holding service loans. If in the future the authority actively markets itself as a provider of finance, it would need to assess the market that it would be competing in e.g., other local authorities and financial institutions. Prior to offering any loan facility, the following factors are considered:
- Financial appraisal based on evidence obtained from credit agencies.
  - Independent external advisor appointed in conjunction with procurement.
  - Analysis of business plans.
  - Appropriate interest rate calculation, including potential state aid implications; and
  - The availability of any securities/collateral.

### **Service Investments: Shares**

- 3.13 **Contribution:** The Council can invest in the shares of its subsidiaries, its suppliers, and local businesses to support local public services and stimulate local economic growth. At present there are no such investments in place.
- 3.14 **Security:** One of the risks of investing in shares is that they fall in value meaning that the initial outlay may not be recovered. In order to limit this risk, upper limits on the sum invested in each category will be determined as the need arises.
- 3.15 **Risk assessment:** The Authority will assess the risk of loss before entering and whilst holding shares by the approach referred to in paragraph 3.11.
- 3.16 **Liquidity:** The maximum period for non-subsidiaries which funds may prudently be committed would initially be 12 months, but this would be subject to an ongoing review to best avoid the likelihood of capital losses.
- 3.17 **Non-specified Investments:** Shares are the only investment type that the Authority has identified that meets the definition of a non-specified investment in the government guidance. The limits on share investments will therefore also be the Authority's upper limits on non-specified investments. The Authority has not adopted any procedures for determining further categories of non-specified investment since none are likely to meet the definition covered by this requirement.

### **Commercial Investments: Property**

- 3.18 **Contribution:** DLUHC defines property to be an investment if it is held primarily or partially to generate a profit. The Council invests in local commercial and residential property, with profits generated spent on local public services. Although there is increased national focus on property, councils have a long history of owning investment properties. Wirral's portfolio includes industrial estates, commercial and leisure properties.

Table 2: Property held for investment purposes

Property	Actual	31.3.2022 Estimate	
	Purchase cost £000	Gains or (losses) £000	Estimated Value in accounts £000
Europa Boulevard	8,400	(2,450)	5,950
Vue Cinema	6,800	(3,150)	3,650
Other Investment Properties	9,286	147	9,433
<b>TOTAL</b>	<b>24,486</b>	<b>(5,453)</b>	<b>19,033</b>

- 3.19 The estimated values in the table above, specifically Europa Boulevard and Vue Cinema, represent the latest valuations as per the Statement of Accounts (as at 31.03.2021), and reflect the specific circumstances at that time, directly attributable to pressures arising due to the COVID-19 pandemic. These valuations are to be reviewed again this year and the prevailing market conditions factored in.
- 3.20 It is prudent to note that whilst these properties are held as investment properties in the Council's asset register, the properties were not acquired specifically for income generation. Most of these investment assets are owned for historic reasons, but subsequent acquisitions (Europa Boulevard and Vue Cinema) are linked to regeneration opportunities.
- 3.21 Discussions with real estate services and investment firm, CBRE, have taken place with the aim of commencing a review of the existing properties held by the Council. This will result in a rolling review of council assets, the outcomes from which will be supported by property disposal and investment strategies, which evidence due consideration of the recommendations contained within the CIPFA/DLUHC Local Government Finance Review (November 2021).
- 3.22 The Council's 'Strategic Asset Management Plan' sets out how the council will make the best use of its buildings and land in the future. This will be linked to future property purchase or consideration.
- 3.23 The Council is currently engaged in a joint venture agreement with Muse Developments to create the Wirral Growth Company. The anticipated benefits to the Authority of this agreement are inward investment, regeneration, job creation, and income generation. These growth priorities are reflected within the Wirral Plan 2021-2026, which highlights ambitions to drive forward sustainable economic growth.
- 3.24 **Security:** In accordance with government guidance, the Authority considers a property investment to be secure if its accounting valuation is at or higher than its purchase cost including taxes and transaction costs.
- 3.25 Where value in the accounts is at or above purchase cost: an annual fair value assessment of the Authority's investment property portfolio is undertaken, and the underlying assets provide security for capital investment. Should the 2021/22 year-end accounts preparation and audit process value these properties significantly below their purchase cost, then an updated investment strategy will be presented to

full council detailing the impact of the loss on the security of investments and any revenue consequences arising therefrom.

- 3.26 Where value in accounts is below purchase cost: the fair value of the Authority's investment property portfolio is no longer sufficient to provide security against loss, and in these circumstances the Authority will take mitigating actions to protect the capital invested.
- 3.27 **Risk assessment:** The Authority assesses the risk of loss before entering and whilst holding property investments. Refer to measures outlined in paragraph 3.11.
- 3.28 **Liquidity:** Compared with other investment types, property is relatively difficult to sell and convert to cash at short notice and can take a considerable period to sell in certain market conditions.

### **Loan Commitments and Financial Guarantees**

- 3.29 Although not strictly counted as investments, since no money has exchanged hands yet, loan commitments and financial guarantees carry similar risks to the Authority and are included here for completeness.
- 3.30 The Authority has committed itself to make available a credit facility of £2 million to Edsential Community Interest Co. To date £1.75 million has been advanced. Under the terms of the existing agreement Edsential has until March 2026 to call upon the balance. Interest is earned by the Council on any sums advanced and is charged at an appropriate market rate.
- 3.31 In addition to the credit facility of £2m, a request for financial assistance was made to the two shareholders of Edsential - Wirral Council, and Cheshire West and Chester Council, to assist Edsential manage their financial pressures because of the COVID-19 pandemic. Both shareholders agreed to provide an additional £857k to Edsential (£1.74m total). Wirral Council agreed to provide the funding at a meeting of Shareholder Board in October 2021. It should be noted that this loan is separate from the credit facility, and as such, has individual terms and conditions.

### **Proportionality**

- 3.32 The table below shows the extent to which the expenditure planned to meet the service delivery objectives and/or place making role of the Authority is dependent on achieving the expected net profit from investments over the lifecycle of the Medium-Term Financial Plan. It is important to note, that the Authority plans to reinvest any profit earned on investment activity into regeneration initiatives. Regular budget monitoring and review of income to be achieved will highlight if expected net profit is in any doubt and if so that corrective budgetary action needs to be taken to minimise any potential impact on services.

Table 3: Proportionality of Investments

	2021/22 Forecast £000	2022/23 Budget £000	2023/24 Budget £000	2024/25 Budget £000
Gross service expenditure	587,000	588,000	593,000	595,000
Investment income	2,000	2,000	2,000	3,000
Proportion	0.34%	0.34%	0.34%	0.51%

*The proportion is the investment income divided by the gross service expenditure.*

### **Borrowing in Advance of Need**

- 3.33 Government guidance is that local authorities must not borrow more than, or in advance of their needs, solely to profit from the investment of the extra sums borrowed. The Authority may, from time to time, borrow in advance of need, where this is expected to provide the best long-term value for money. Since amounts borrowed will be invested until spent, the Authority is aware that it will be exposed to the risk of loss of the borrowed sums, and the risk that investment and borrowing interest rates may change in the intervening period. At present, any borrowing arrangements in place have been made solely to meet cashflow requirements, and not to profit from the investment of the extra sums borrowed. Furthermore, all borrowing is undertaken once an analysis of approved lending counterparties has taken place. These risks will be managed as part of the Authority's overall management of its treasury risks, in addition to the consideration of the recommendations contained within the CIPFA/DLUHC Local Government Finance Review (November 2021).

### **Capacity, Skills and Culture**

- 3.34 **Elected members and statutory officers:** The Council has a dedicated 'Policy & Resources Committee' to review key financial matters. The Committee meets regularly with officer support from the Director of Resources to review and approve reports; raise questions; and receive briefings on latest developments. Financial training has been provided to all Members to aid decision making. Regular reporting and discussion of financial matters occurs with frequent meetings of the Policy and Resources Finance Sub-Committee via weekly workshops and with the Strategic Leadership Team. Formal reporting is provided to Council via the Policy and Resources Committee and to the Policy and Services committees. Reports undergo extensive review to ensure content is detailed and appropriate for the circumstance, and relevant implications have been identified. As part of the External Assurance Reviews commissioned by DLUHC, the newly established Independent Panel also review and comment on reports in advance of Policy and Resources Committee.

- 3.35 Decisions which have a financial impact must be approved by the Director of Resources (Section 151 Officer) or one of their authorised officers. Finance Officers are members of appropriate professional bodies such as the Chartered Institute of Public Finance and Accountancy (or equivalent). Membership requires officers undergo continuous professional development and are subject to compliance with the regulatory frameworks laid down by the professional institute. Officers are supported by properly regulated advisors and have access to the latest guidance and best practice. Strategies and policies are approved to provide a framework for investment decisions to be made within.
- 3.36 **Commercial agreements:** Commercial agreements require initial approval from the Director of Resources. Governance arrangements include oversight from the Investment and Change Board (ICB), chaired by the Director of Resources. ICB membership includes senior officers from a range of disciplines including legal services. Decisions are also subject to member approval with governance arrangements in place to ensure reports contain appropriate detail to enable decisions to be made. Where appropriate, external advice will be sought from experienced and suitably qualified experts.
- 3.37 **Corporate governance:** The Director of Resources has statutory responsibility for overseeing the Council's financial affairs and ensuring that robust controls are in place. The Director is supported by officers within and without the directorate. The Investment and Change Board assists with ensuring governance and oversight is in place. At member level there is a Policy & Resources Committee with responsibility for financial matters. The Council maintains appropriate risk registers and an Internal Audit function is maintained to provide appropriate challenge and review.

### **Investment Indicators**

- 3.38 The Authority has set the following quantitative indicators to allow elected members and the public to assess the Authority's total risk exposure as a result of its investment decisions.
- 3.39 **Total risk exposure:** The first indicator shows the Authority's total exposure to potential investment losses. This includes amounts the Authority is contractually committed to lend but have yet to be drawn down and guarantees the Authority has issued over third-party loans.

*Table 4: Total investment exposure*

<b>Total investment exposure</b>	<b>31.03.2021 Actual £000</b>	<b>31.03.2022 Forecast £000</b>	<b>31.03.2023 Forecast £000</b>
Treasury management investments	47,833	30,000	30,000
Service investments: Loans	1,325	2,607	2,607
Commercial investments: Property	19,033	19,033	19,033
<b>TOTAL INVESTMENTS</b>	<b>68,191</b>	<b>51,640</b>	<b>51,640</b>
Commitments to lend	1,025	250	250
Guarantees issued on loans	0	5,330	5,330
<b>TOTAL EXPOSURE</b>	<b>69,216</b>	<b>57,220</b>	<b>57,220</b>

- 3.40 **How investments are funded:** Government guidance is that these indicators should include how investments are funded. Since the Authority does not normally associate particular assets with particular liabilities, this guidance is difficult to comply with. However, the following investments could be described as being funded by borrowing. The remainder of the Authority’s investments are funded by usable reserves and income received in advance of expenditure.

*Table 5: Investments funded by borrowing*

<b>Investments funded by borrowing</b>	<b>31.03.2021 Actual</b>	<b>31.03.2022 Forecast</b>	<b>31.03.2023 Forecast</b>
Service investments: Loans	1,325	2,607	2,607
Commercial investments: Property	19,033	19,033	19,033
<b>TOTAL FUNDED BY BORROWING</b>	<b>20,358</b>	<b>21,640</b>	<b>21,640</b>

- 3.41 **Rate of return received:** This indicator shows the investment income received less the associated costs, including the cost of borrowing where appropriate, as a proportion of the sum initially invested. Note that due to the complex local government accounting framework, not all recorded gains and losses affect the revenue account in the year they are incurred.

*Table 6: Investment rate of return (net of all costs)*

<b>Investments net rate of return</b>	<b>2020/21 Actual %</b>	<b>2021/22 Forecast %</b>	<b>2022/23 Forecast %</b>
Treasury management investments	0.85	0.43	0.43
Service investments: Loans	7.39	3.20	4.03
Commercial investments: Property	7.09	9.11	8.66
<b>ALL INVESTMENTS</b>	<b>2.72</b>	<b>3.76</b>	<b>3.65</b>

## **4.0 FINANCIAL IMPLICATIONS**

- 4.1 Approval and implementation of this strategy will limit financial risks, while helping to minimise financing costs and maximise investment returns.

## **5.0 LEGAL IMPLICATIONS**

- 5.1 The Department for Levelling Up, Housing and Communities guidance is issued by the Secretary of State under section 15(1)(a) of the Local Government Act 2003. Under that section local authorities are required to “have regard” to “such guidance as the Secretary of State may issue”. The Council has adopted the requirement of the DLUHC to produce an investment strategy that covers non-treasury activities. This requires the annual production of Investment Indicators and an Investment Strategy Statement.

## **6.0 RESOURCE IMPLICATIONS: STAFFING, ICT AND ASSETS**

- 6.1 There are none arising out of this report.

## 7.0 RELEVANT RISKS

7.1 The Council is responsible for investment decisions and activity and none of these decisions are without risk. The successful identification, monitoring and control of risk are important, and the main risks and mitigations are:

<b>Risk</b>	<b>Mitigation</b>
Fluctuations in interest rate levels	Borrowing and investment profiles are balanced both in terms of maturity (utilising short- and long-term instruments) and in terms of the nature of the interest rate of the portfolio (fixed rate and variable interest rate products).
Exposure to inflation	Wherever possible, investments are entered into at inflation equalling levels of interest. This depends entirely on the nature and purpose of the proposed investment.
Legal and Regulatory Risk	Appropriate legal advice is sought on new opportunities to ensure adherence to relevant legislation and regulation.
Credit and Counterparty Risk (Security of investments)	Any potential counterparty is subjected to suitable due diligence to ascertain appropriateness for investment and investment criteria.

## 8.0 ENGAGEMENT/CONSULTATION

8.1 There has been no consultation undertaken or proposed for this strategy report.

## 9.0 EQUALITY IMPLICATIONS

9.1 There are none arising directly from this report.

## 10.0 ENVIRONMENT AND CLIMATE IMPLICATIONS

10.1 As part of future investment strategy, consideration will be given to potential opportunities to invest in environmentally focussed instruments or organisations. 'Ethical, Social and Governance' (ESG) investment criteria will be considered and, where viable in adherence to the policies laid out in this strategy, will only be entered into following satisfactory assessment of the instrument and/or organisation.

## 11.0 COMMUNITY WEALTH IMPLICATIONS

11.1 There are none arising directly from this report.

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### BACKGROUND PAPERS

International Financial Reporting Standards – IFRS9 Financial Instruments  
Strategic Asset Management Plan  
Department for Levelling Up, Housing and Communities Investment Guidance

### SUBJECT HISTORY (last 3 years)

<b>Council Meeting</b>	<b>Date</b>
Investment Strategy Statement 2019-20	18 <sup>th</sup> February 2019
Investment Strategy Statement 2020-21	17 <sup>th</sup> February 2020
Investment Strategy Statement 2021-22	17 <sup>th</sup> February 2021