Capital Strategy Report 2024/25

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. It has been written in an accessible style to enhance members' understanding of these sometimes-technical areas.

Decisions made this year on capital and treasury management will have financial consequences for the Authority for many years into the future. They are therefore subject to both a national regulatory framework and to local policy framework, summarised in this report.

Capital Expenditure and Financing

Capital expenditure is where the Authority spends money on assets, such as property or vehicles, that will be used for more than one year. In local government this includes spending on assets owned by other bodies, and loans and grants to other bodies enabling them to buy assets.

- For details of the Authority's policy on capitalisation, see Note 1.15 in the Financial Statements for the year ended 31 March 2023

In 2024/25, the Authority is planning capital expenditure of £4.58m as summarised below:

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

	2022/23 actual	2023/24 forecast	2024/25 budget *	2025/26 budget	2026/27 budget
General Fund services	2.77	3.27	4.58	2.71	1.29
TOTAL	2.77	3.27	4.58	2.71	1.29

The main General Fund capital projects include the replacement of the refuse and recycling fleet and payment of Disabled Facility Grants. Following a change in the Prudential Code, the Authority no longer incurs capital expenditure on investments.

Governance: Service managers must take a report to full Council in order to include projects in the Council's capital programme. Finance calculate the financing cost (which can be nil if the project is internally financed) and review any business case for the proposal to ensure it meets the council requirements over payback periods (if applicable). Council appraises all proposals based on a comparison of strategic priorities against financing costs and approves the use of capital resources. The final capital programme is then presented to Executive Committee and to Council in February each year.

All capital expenditure must be financed, either from external sources (government grants and other contributions), the Authority's own resources (revenue, reserves, and capital receipts) or debt (borrowing, leasing). The planned financing of the above expenditure is as follows:

Table 2: Capital financing in £ millions

	2022/23 actual	2023/24 forecast	2024/25 budget *	2025/26 budget	2026/27 budget
External sources	1.76	1.94	1.20	0.80	0.80
Capital receipts	0.16	0.8	0.13	0.22	0.13
Revenue resources	0.85	0.53	3.25	1.69	0.36
Debt	0	0	0	0	0
TOTAL	**2.77**	**3.27**	**4.58**	**2.71**	**1.29**

Debt is only a temporary source of finance, since loans and leases must be repaid, and this is therefore replaced over time by other financing, 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 and use of capital receipts are as follows:

Table 3: Replacement of debt finance in £ millions

	2022/23 actual	2023/24 forecast	2024/25 budget	2025/26 budget	2026/27 budget
Own resources	0.93	0.95	0.97	1	1.02
TOTAL	**0.93**	**0.95**	**0.97**	**1**	**1.02**

The Authority's cumulative outstanding amount of debt finance is measured by the capital financing requirement (CFR). This increases with new debt-financed capital expenditure and reduces with MRP and capital receipts used to replace debt. The CFR is expected to be £51.62m during 2024/25. Based on the above figures for expenditure and financing, the Authority's estimated CFR is as follows:

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

	31.3.2023 actual	31.3.2024 forecast	31.3.2025 budget *	31.3.2026 budget	31.3.2027 budget
Capital investments	53.54	52.59	51.62	50.62	49.61
TOTAL CFR	**53.54**	**52.59**	**51.62**	**50.62**	**49.61**

Asset management: To ensure that capital assets continue to be of long-term use, the Council has an asset management strategy in place. This plan is set in the wider context of ensuring a sustainable future for Council expenditure and revenue and aims to:

- Identify and explain the context and objectives of Asset Management at Tewkesbury Borough Council.
- Identify and explain how the plan links with our Corporate Plan and processes that will be followed to deliver Asset Management to Tewkesbury Borough Council.
- Identify the specific challenges and opportunities that currently affect Tewkesbury Borough Council's land and building assets and the ability of those assets to deliver the priorities, goals and promises set out in our Corporate Plan.
- Identify and recommended strategies to address and resolve issues and opportunities within the asset portfolio.

• Establish an annual Service Action Plan summarising the required actions arising from those recommendations.

The Council's asset management strategy can be found on our website.

Table 5: Capital receipts receivable in £'000

	2022/23 actual	2023/24 forecast	2024/25 budget	2025/26 budget	2026/27 budget
Right to buy receipts	421	250	250	250	250
Other	7	0	0	0	0
TOTAL	**428**	**250**	**250**	**250**	**250**

Treasury Management

Treasury management is concerned with keeping sufficient but not excessive cash available to meet the Authority'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 Authority 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 Authority does not borrow to invest for the primary purpose of financial return and therefore retains full access to the Public Works Loans Board.

Due to decisions taken in the past, the Authority currently has £20.07m borrowing at an average interest rate of 1.92% and £33.7m treasury investments at an average income rate of 4.63%.

Borrowing strategy: The Authority'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 Authority therefore seeks to strike a balance between cheaper short-term loans (currently available between 5.14% to 5.35%) and long-term fixed rate loans where the future cost is known but higher (currently 5% to 5.7%).

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

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

	31.3.2023 actual	31.3.2024 forecast	31.3.2025 budget	31.3.2026 budget	31.3.2027 budget
Debt	30.33	19.79	19.26	18.73	18.09
Capital Financing Requirement	53.54	52.59	51.62	50.62	49.61

Statutory guidance is that debt should remain below the capital financing requirement, except in the short-term. As can be seen from table 6, the Authority expects to comply with this in the medium term.

Liability benchmark: To compare the Authority'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.

Table 7: Borrowing and the Liability Benchmark in £ millions

	31.3.2023 actual	31.3.2024 forecast	31.3.2025 budget	31.3.2026 budget	31.3.2027 budget
Outstanding borrowing	30.33	19.79	19.26	18.73	18.09
Liability benchmark	10.56	11.19	9.22	7.22	6.21

The table shows that the Authority expects to remain borrowed above its liability benchmark. This is because a deliberate decision has been made to borrow additional sums due to the volatility of the Council's cash flows.

Affordable borrowing limit: The Authority 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 £m

	2023/24 limit	2024/25 limit	2025/26 limit	2026/27 limit
Authorised limit – borrowing	50	50	50	50
Operational boundary – borrowing	40	40	40	40

Further details on borrowing are in the treasury management strategy.

Treasury 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 Authority'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. Money that will be held for longer terms is invested more widely, including in bonds, shares and property, to balance the risk of loss against the risk of receiving returns below inflation. Both near-term and longer-term investments may be held in pooled funds, where an external fund manager makes decisions on which particular investments to buy and the Authority may request its money back at short notice.

Table 9: Treasury management investments in £millions

	31.3.2023 actual	31.3.2024 forecast	31.3.2025 budget	31.3.2026 budget	31.3.2027 budget
Near-term investments	19.34	8.35	11.79	13.25	13.73
Longer-term investments	10.43	10.30	8.30	8.30	8.30
TOTAL	**29.77**	**18.65**	**20.09**	**22.55**	**22.03**

Further details on treasury investments are in the treasury management strategy.

Risk management: The effective management and control of risk are prime objectives of the Authority's treasury management activities. The treasury management strategy therefore sets out various indicators and limits to constrain the risk of unexpected losses and details the extent to which financial derivatives may be used to manage treasury risks.

- The treasury management prudential indicators are in the treasury management strategy.

Governance: Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Executive Director of Resources and staff, who must act in line with the treasury management strategy approved by Council. The in-year review and management of our treasury and capital activities are actioned by the Executive Committee in line with the Terms of Reference set out within the Council's constitution. These Terms of Reference for the Executive Committee include:

- to 'review and monitor the operation of the policy framework' and
- to 'monitor the Council's performance.'.

The Audit and Governance Committee is responsible for scrutinising treasury management decisions.

Commercial Activities

- With central government financial support for local public services declining and uncertainty around future funding sources (e.g. New Homes Bonus), the Council had no choice in previous years but to invest in commercial property purely or mainly for financial gain. Total commercial investments are currently valued at £59.28m as at 31.03.23 (with a cost value of £60.76m) providing a net return after all costs of 5.29%.
- With financial return being the main objective, the Council accepts higher risk on commercial investment than with treasury investments. The principal risk exposures include voids, fall in capital value and high asset management costs. These risks are managed by using professional property advisers who are used to analyse the risk of voids, advice on alternative uses or exit strategies for investment properties. In order that commercial investments remain proportionate to the size of the authority, and to ensure that plausible losses could be absorbed in budgets or reserves without unmanageable detriment to local services, we have decided not to continue acquiring further properties and contingency plans are in place (including a contingency reserve) should expected yields not materialise.
- Only direct costs such as property management are netted off gross income. Interest and minimum revenue provision costs are excluded from this indicator.

Table 10: Prudential indicator: Net income from commercial and service investments to net revenue stream

	2022/23 actual	**2023/24 forecast**	**2024/25 budget**	**2025/26 budget**	**2026/27 budget**
Total net income from service and commercial investments	3,135	3,428	2,773	2,060	1,869
Proportion of net revenue stream	22.27%	26.27%	19.86%	14%	12.24%
Proportion of usable revenue reserves	7.75%	8.82%	6.96%	5.04%	4.58%

Other Liabilities

In addition to forecast debt of £19.26m detailed above, the Council is committed to making future payments to cover its pension fund deficit (valued at £2.3m as at 31 March 2023). It has also set aside £3.47m to cover risks of provisions (of which £2.64m relates to business rates appeals).

Governance: Decisions on incurring new discretional liabilities are taken in line with the Financial Procedure Rules by service managers in consultation with Executive Director of Resources and the Monitoring Officer.

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 Council Tax, business rates and general government grants.

Table 11: Prudential Indicator: Proportion of financing costs to net revenue stream

	2022/23 actual	**2023/24 forecast**	**2024/25 budget ***	**2025/26 budget**	**2026/27 budget**
Financing costs (£m)	1.390	1.367	1.383	1.400	1.414
Proportion of net revenue stream	9.88%	10.48%	9.90%	9.51%	9.26%

Further details on the revenue implications of capital expenditure are in the 2024/25 revenue budget.

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 will extend for up to 40 years into the future. The Executive Director of Resources is satisfied that the proposed capital programme is prudent, affordable and sustainable because it has all been full costed and the full revenue implications have been included within the Medium-Term Finance Strategy (MTFS).

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 Executive Director of Resources is a qualified accountant with over 25 years' experience, the Asset Manager has many years' experience and is supported by an expert team including engineers and building surveyors. The Council pays for staff to study towards relevant professional qualifications including CIPFA and AAT.

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, Lambert Smith Hampton as property consultants and appoints legal specialists as necessary. 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.