

## Capital Strategy Report 2023/24

### 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 Council 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 Council 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.

In 2023/24, the Council is planning capital expenditure of £49.9 as summarised below:

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

	2021/22 actual	2022/23 forecast	2023/24 budget	2024/25 budget	2025/26 budget
General Fund services	36.5	15.0	19.3	14.3	1.1
Council housing (HRA)	21.7	21.8	30.6	20.1	22.5
<b>TOTAL</b>	<b>58.2</b>	<b>36.8</b>	<b>49.9</b>	<b>34.4</b>	<b>23.6</b>

The main General Fund capital projects for 23/24 include Stephenson Memorial Hall (£8.9m), Revitalising the Heart of Chesterfield (£2.8m), Staveley Town Deal schemes (£5.4m) and Disabled Facilities Grants (£2.2m).

The Housing Revenue Account (HRA) is a ring-fenced account which ensures that council housing does not subsidise, or is itself subsidised, by other local services. HRA capital expenditure is therefore recorded separately, and includes the building of new homes, as well as enhancements to current housing stock.

**Governance:** The Finance and Performance Board appraises all requests for capital growth based on a comparison of service priorities against financing costs and ongoing revenue commitments. Approval at Finance and Performance Board allows new schemes to be added to the latest version of the capital programme which is presented to Council for approval. Copies of all Council reports can be found on the Authority's website.

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

*Table 2: Capital financing in £ millions*

	2021/22 actual	2022/23 forecast	2023/24 budget	2024/25 budget	2025/26 budget
External sources	2.7	10.3	16.9	9.3	1.0
Capital receipts	4.7	4.9	4.7	4.2	3.9
Revenue resources	17.7	17.6	16.5	15.2	15.0
Debt	33.1	4.0	11.8	5.7	3.7
<b>TOTAL</b>	<b>58.2</b>	<b>36.8</b>	<b>49.9</b>	<b>34.4</b>	<b>23.6</b>

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 prior years' debt finance in £ millions*

	2021/22 actual	2022/23 forecast	2023/24 budget	2024/25 budget	2025/26 budget
General Fund	0.3	0.7	1.4	1.5	1.8
HRA	1.9	1.9	1.8	2.0	2.0

The Council's full minimum revenue provision statement can be found at Appendix D to this report.

The Council's cumulative outstanding amount of debt finance is measured by the capital financing requirement (CFR). This increases with new debt-financed capital expenditure and reduces with MRP and capital receipts used to replace debt. The General Fund CFR is expected to decrease by £100k during 2023/24 and the HRA CFR is expected to increase by £8.6m during the same period. Based on the above figures for expenditure and financing, the Council's estimated CFR is as follows:

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

	31.3.2022 actual	31.3.2023 forecast	31.3.2024 budget	31.3.2025 budget	31.3.2026 budget
General Fund services	56.6	59.9	59.8	62.1	60.4
Council housing (HRA)	124.5	122.7	131.3	131.2	132.9
<b>TOTAL CFR</b>	<b>181.1</b>	<b>182.6</b>	<b>191.1</b>	<b>193.3</b>	<b>193.3</b>

**Asset disposals:** When a capital asset is no longer needed, it may be sold so that the proceeds, known as capital receipts, can be spent on new assets or to repay debt. The Authority is currently also permitted to spend capital receipts "flexibly" on service transformation projects until 2023/24. Repayments of capital grants, loans and investments also generate capital receipts. The Council plans to receive £5.9m of capital receipts in the 2023/24 financial year as follows:

Table 5: Capital receipts in £ millions

	2021/22 actual	2022/23 forecast	2023/24 budget	2024/25 budget	2025/26 budget
General Fund Asset sales	0.5	2.0	2.5	1.5	1.5
Right to Buy Receipts	5.8	3.9	2.6	2.1	1.6
Other HRA Asset sales	0	0.8	0.8	0.8	0.8
<b>TOTAL</b>	<b>6.3</b>	<b>6.7</b>	<b>5.9</b>	<b>4.4</b>	<b>3.9</b>

### Treasury Management

Treasury management is concerned with keeping sufficient but not excessive cash available to meet the Council's spending needs, while managing the risks involved. Surplus cash is invested until required, while a shortage of cash will be met by borrowing, to avoid excessive credit balances or overdrafts in the bank current account.

Due to decisions taken in the past, the Council currently has £138m borrowing at an average interest rate of 3.45% and £31m treasury investments at an average rate of 3.20%.

**Borrowing strategy:** The Council's main objectives when borrowing are to achieve a low but certain cost of finance while retaining flexibility should plans change in future. These objectives are often conflicting, and the Council therefore seeks to strike a balance between short-term loans (currently available at around 4.0%) and long-term fixed rate loans where the future cost is known but higher (currently 4.5 to 5.0%).

The Council does not borrow to invest for the primary purpose of financial return and therefore retains full access to the Public Works Loans Board.

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

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

	31.3.2022 actual	31.3.2023 forecast	31.3.2024 budget	31.3.2025 budget	31.3.2026 budget
Debt	143.5	145.7	155.6	159.3	158.5
Capital Financing Requirement	181.1	182.6	191.1	193.3	193.3

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 Council expects to comply with this in the medium term.

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

*Table 7: Prudential Indicators: Authorised limit and operational boundary for external debt in £m*

	2022/23 limit	2023/24 limit	2024/25 limit	2025/26 limit
Authorised limit	180.7	181.9	185.9	187.9
Operational boundary	164.3	165.3	169.0	170.8

**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 Council’s policy on treasury investments is to prioritise security and liquidity over yield, that is to focus on minimising risk rather than maximising returns. Cash that is likely to be spent in the near term is invested securely, for example with the government, other local authorities or selected high-quality banks, to minimise the risk of loss. Money that will be held for longer terms can be invested more widely, including in bonds, shares and property, to balance the risk of loss against the risk of receiving returns below inflation. Both near-term and longer-term investments may be held in pooled funds, where an external fund manager makes decisions on which particular investments to buy and the Council may request its money back at short notice.

*Table 8: Treasury management investments in £millions*

	31.3.2022 actual	31.3.2023 forecast	31.3.2024 budget	31.3.2025 budget	31.3.2026 budget
Near-term investments	27.3	10.0	0	0	0
Longer-term investments	0	0	10.0	10.0	10.0
<b>TOTAL</b>	<b>27.3</b>	<b>10.0</b>	<b>10.0</b>	<b>10.0</b>	<b>10.0</b>

**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.

**Governance:** Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Service Director - Finance and staff, who must act in line with the treasury management strategy approved by Council. Regular reports on treasury management activity are presented to Council. The Standards and Audit Committee is responsible for scrutinising treasury management decisions.

### Investments for Service Purposes

The Council may from time to time make investments to assist local public services, including making loans to local service providers and local small businesses to promote economic growth. In light of the public service objective, the Authority is willing to take more risk than with treasury investments, however it still plans for such investments to generate a profit after all costs.

**Governance:** Decisions on service investments are made by the Service Director - Finance in consultation with the relevant Executive Directors, and must meet the criteria and limits laid down in the investment strategy. Most loans and shares are capital expenditure and purchases will therefore also be approved as part of the capital programme.

## Commercial Activities

The Council invests in commercial properties which are held primarily for service purposes such as economic regeneration, but which in addition generate a profit that will be spent on local public services. With central government financial support for local public services declining, the Council may in the future decide to invest in commercial property purely or mainly for financial gain.

With financial return being the main objective, the Council would accept higher risk on commercial investment than with treasury investments. Further details can be found in the Investment Strategy at Appendix C to this report.

*Table 9: Prudential indicator: Net income from commercial and service investments to net revenue stream in £millions*

	2021/22 actual	2022/23 forecast	2023/24 budget	2024/25 budget	2025/26 budget
Total net income from service and commercial investments	2.4	2.4	2.4	2.4	2.4
Proportion of net revenue stream	17.0%	21.6%	19.6%	21.3%	20.8%

## Liabilities

In addition to debt of £144m detailed above, the Council is committed to making future payments to cover its pension fund deficit (valued at £72.4m) This deficit is planned to be reduced to a break-even position over the next 18 years.

## 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 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. As a result of the 2021 changes to the Prudential Code interest and investment income has been removed from the definition of financing costs.

*Table 9: Prudential Indicator: Proportion of financing costs to net revenue stream*

	2021/22 actual	2022/23 forecast	2023/24 budget	2024/25 budget	2025/26 budget
Financing costs General Fund (£000)	433	801	1,479	1,520	1,868
Financing costs HRA (£000)	6,431	5,993	5,755	6,372	6,389
Proportion of net revenue stream General Fund	3.1%	7.3%	12.3%	13.7%	16.4%
Proportion of net revenue stream HRA	12.1%	11.3%	10.2%	10.4%	10.3%

**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 Service Director - Finance is satisfied that the proposed capital programme is prudent, affordable and sustainable.

### **Knowledge and Skills**

The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. The Council pays for 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. 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.