



THE INVESTMENT STRATEGY (NON-TREASURY) for 2020/21

1 **Background Information**

- 1.1 For the purposes of this Strategy “Investment” mean all financial assets and also non-financial assets held primarily to generate income (i.e. investment property).
- 1.2 This Investment Strategy has been produced in accordance with The Government Department guidance on local government investments which requires the production of an Annual Investment Strategy for non-treasury management investments to include risk indicators to allow the level of risk to be assessed.
- 1.3 The Council’s Investment Strategy is undertaken within the following context:
 - i) The level of the Council’s non-treasury investments is one of the highest of all district authorities and has been for some time.
 - ii) The income generated from non-treasury investments is significant to the Council and supports the cost of services.
- 1.4 The Council invests its money for three board purposes:
 - i) Because it has surplus cash as a result of its day to day activities or cash that it holds pending the Council’s spending plans (known as Treasury Management investments).
 - ii) To support local public services by lending to other organisations (known as service based investments).
 - iii) To earn investment income (known as commercial investments where this is the main purpose).
- 1.5 Details of the Council’s treasury management investments are contained in the Council’s Treasury Management Strategy and are therefore not included in this strategy.

2 Total Non-Treasury Investment Exposure

- 1.1 The Council's total exposure to non-treasury investments is estimated at £289.97M as at 31/03/20 and is forecast to increase as set out in Table 1:

Table 1 – Non-Treasury Investments

Estimate 31/3/20 £M		Estimate 31/3/21 £M	Estimate 31/3/22 £M	Estimate 31/3/23 £M	Estimate 31/3/24 £M
	Investment Property				
260.16	Existing Investment Property	260.16	260.16	260.16	260.16
23.61	Property Investment Strategy	32.51	32.51	32.51	32.51
	Service Based Investments				
0.20	Manydown	1.15	3.29	3.91	3.91
6.00	Service Based Loans	5.00	4.00	3.00	2.00
289.97		298.82	299.96	299.58	298.58

- 1.2 The government guidance requires the Council to indicate how the investments are funded. Although local authorities do not normally associate individual sources of funding to specific investments it is possible to say that none of the above investments have been funded from borrowing.
- 1.3 This is a key indicator of the level of risk the Council is taking as borrowing to invest is deemed to be extremely risky and is discouraged.

2 Expected Rates of Return Indicator

- 2.1 This indicator shows the investment income receivable as a proportion of the sum invested for the non-treasury investments and can be seen in Table 2.

Table 2 – Average Returns on Non-Treasury Investments

	2018/19 Actual %	2019/20 Forecast %	2020/21 Forecast %
Investment Property			
Existing Investment Property	5.77	5.77	5.77
Property Investment Strategy Investments	6.40	7.40	7.10
Service Based Investments			
Manydown Investments	0.00	0.00	3.20
Service Based Loans	0.00	0.00	0.00

- 2.2 The returns above do not include valuation gains and losses or property running costs.

3 Investment Property

- 3.1 The Council has a very large Investment Property Portfolio valued in the accounts at £285.70M. A summary of the portfolio is shown in Table 3.

Table 3 – Investment Property Portfolio

<u>Investment Property</u>	Value 31/03/2019 £M
Houndmills Industrial Estate	49.70
Daneshill Industrial Estate	46.70
Viables	38.00
Basing View	27.90
The Malls	19.10
Festival Place	12.50
Manydown Land	21.70
Other Industrial and Commercial Property	44.50
Property Investment Strategy Properties	25.60
	285.70

- 3.2 For the Council's historically held Investment Property Portfolio it is not possible to identify the initial sums invested and therefore the actual returns from these properties. It is possible to calculate a simple return based on the value of the properties in the balance sheet and the income generated.
- 3.3 The historically held property portfolio generates £15.54M of rent income on properties valued at £260.10M which is a gross return of 5.97%. After maintenance and running costs of £5.20M the net income is £10.34M which is a net return of 3.98%.

4 Property Investment Strategy

- 4.1 The Council approved the objectives and principles of the Property Investment Strategy in 2017 which was set up to aims to invest up to £35.00M (originally £30.00M) in new and existing Investment Properties in order to increase the Council's income.
- 4.2 In order that commercial investments remain proportionate the Council set a limit of £35.00M (originally £30.00M) for this type of investment.
- 4.3 A sum of £23.61M has been invested in new properties as part of this strategy with a further £8.90M committed in 2020/21.
- 4.4 The Property Investment Strategy was expected to generate returns in the 5% to 7% range.

4.5 The individual investments and the expected returns are shown in Table 4.

Table 4 – Property Investment Strategy Returns

	Investment Made £M	Return %	Additional Income £M
Units 1 to 4 Armstrong Road	4.56	9.6%	0.44
Units 1 to 2 Stroudley Road	4.99	6.0%	0.30
Units 1 to 2 Winchester Road	6.02	5.2%	0.31
Ringway House	0.47	16.8%	0.08
Lister Road (B&Q)	7.57	8.1%	0.61
	23.61	7.4%	1.74
Eli Lilly (2020/21)	8.90	6.3%	0.56
	32.51	7.1%	2.30

4.6 Although the primary objective of these investments is to generate additional rent income to balance the Council's future budgets they can also make other contributions such as regeneration, economic growth, increased business rates income and replacing local property market failure.

4.7 With financial return being the main objective, the Council accepts higher risk on commercial investment than with treasury investments. The principal risk exposures include vacancies, loss of capital value and increasing maintenance costs. The Council has had to strike a balance between security, liquidity and yield based on the contribution the investments make and the Council's risk appetite.

4.8 The target returns (%) and gross income (£) from these investments are government recommended indicators and will need to be monitored and reported throughout the year along with any costs associated with the investments (currently none) and the net income.

4.9 When looking at the security of capital for property investments the MHCLG guidance requires the Council to look at the fair value of the property and as long as the value does not fall below the price paid for the property then it is deemed to be secure.

4.10 If the value of a property investment drops below the purchase price (excluding costs) then the Council will need to determine what mitigation is required in order to maintain the Council's future financial stability. This may involve reviewing the property portfolio and identifying properties that are not performing well and if necessary disposing of them.

4.11 The investments made and the fair values can be seen in Table 5.

Table 5 – Value of Property Investment Strategy Investments

<u>Property</u>	Investment	Original	Value	Valuation
	Made	Value	31/03/19	Gain
	£M	£M	£M	£M
Units 1 to 4 Armstrong Road	4.56	3.25	11.20	3.39
Units 1 to 2 Stroudley Road	4.99	0.43	6.58	1.16
Units 1 to 2 Winchester Road	6.02	0.00	4.94	(1.08)
Ringway House, Bell Road	0.47	1.15	2.82	1.20
Lister Road (B&Q)	7.57	0.00	7.57	0.00
	23.61	4.83	33.11	4.67

4.12 As shown in Table 5, in 2018/19 the Property Investment Strategy Investments have an unrealised net gain of £4.67M (19.8%) as well as returning 7.1% per annum in income.

4.13 As these property acquisitions are very recent there are currently no additional costs associated with them that would reduce the net return.

4.14 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. The Council has accepted this liquidity risk because it has considerable cash investments within its treasury management investments that are highly liquid to ensure that it can assess sums when needed.

4.15 Further details on how the risks are managed and the process for ensuring effective due diligence for these investments can be found in the Council's Property Investment Strategy – Annual Property Plan.

4.16 The other main recommended indicators relate to the level of voids (currently none) and the Council's dependency on the income from these commercial investments of £1.74M (which equates to about 1.32% of its total income budget of £131.38M or 4.73% of the Council's net cost of services budget in 2020/21) which will also need to be monitored and reported during the year.

4.17 The Council's dependency on the income from all of its investment property (including the existing property portfolio) is much higher at £17.45M in 2020/21 or 13.48% of the total income budget or 47.44% of the Council's net cost of services.

4.18 Once established, any significant changes in the indicators between years would need to be explained in the annual strategy.

- 4.19 The government recommend that benchmarking is undertaken for commercial investments against other Councils and other types of investment. The property management team have plans to carry out this type of benchmarking now that all the investments under the strategy are in place.
- 4.20 In terms of the governance arrangements for these investments, the Council has a specific strategy that was approved by Council and it has an asset management plan. The approved strategy set out the criteria, and limits on this type of investment and officers are required to operate within these criteria and limits.
- 4.21 Decisions on commercial investments are made by the Executive Director of Finance and Resources, after consultation with the Portfolio Holder for Property and Development, within the limits and criteria approved in the strategy.
- 4.22 Property and most other commercial investments are also deemed to be capital expenditure and therefore will also be approved as part of the capital programme.
- 4.23 Quarterly monitoring reports on property investment activity under the strategy are presented to the Audit and Accounts Committee and half yearly to Cabinet.

5 Invest to Grow Fund

- 5.1 The Council had an Invest to Grow Fund Strategy that had allocated £25.00M to be invested in future years via loans to development companies. The primary purpose of the Invest to Grow Strategy is economic development rather than income and therefore the investments will be treated as service based investments once they are made.
- 5.2 The fund has made one short term investment of £8.90M which will be repaid. The fund has now been closed and no further investment will be made.

6 Manydown Investments

- 6.1 The Council currently has budget provision of £35.00M for investment in the Manydown Project. The scale and timing of the investment was always dependent on the terms of the final development agreement with the Council's private sector partner.

- 6.2 It is now likely that the level of investment will be significantly lower than allowed for. This means that £31.09M is no longer required for this purpose.

7 Service Based Loans

- 7.1 The Council has a number of loans that it has made for operational purposes to other organisations and individuals. The main loans are £2.30M lent to Sentinel Housing Association as part of an existing house purchase scheme linked to homelessness prevention and £5.10M lent to SERCO (balance outstanding of £4.44M as at 31 March 2019) as part of the arrangements for the newly let waste management service.
- 7.2 The contribution these loans make relate to the direct provision of Council priority services and therefore this has been taken into consideration when assessing the risks involved with making these types of loan.
- 7.3 The Council's total exposure to this type of loan is currently £6.74M and all of these loans have been capitalised and have been funded from the Council's own resources which mean that there is no requirement to set aside allowances for expected credit losses.
- 7.4 In nearly all cases with service based loans the Council has a claim on the underlying assets should the organisation default on the loan.

8 Investment Performance Monitoring and Reporting

- 8.1 The Council has delegated responsibility for the monitoring and scrutiny of its investment strategies and activity to the Audit and Accounts Committee.
- 8.2 The execution and administration of the Property Investment Strategy is delegated to the Executive Director of Finance and Resources (S151 Officer).
- 8.3 Performance of the Council's Property Investment Strategy and associated investments are monitored and scrutinised quarterly by the Audit and Accounts Committee and half yearly by Cabinet.
- 8.4 Performance of the Council's investment property portfolio is reported in summary form quarterly to the Audit and Accounts Committee and the income from investment property is monitored and reported as part of the Council's revenue budget monitoring.
- 8.5 There is currently no formal monitoring and reporting of the service based investments.

9 Capacity, Knowledge, Skills and Culture

- 9.1 The Council employees professionally qualified and experienced staff in senior positions with responsibility for making commercial and service based investment decisions.

- 9.2 Prior to all major investments the Council will seek independent advice from external advisors and consultants that are specialists in their field as necessary. This approach ensures that the Council has access to knowledge and skill commensurate with its risk appetite.
- 9.3 For property investments the Council currently uses Cushman and Wakefield International and Knight Frank.