



THE INVESTMENT STRATEGY (NON-TREASURY) for 2022/23

1 Background Information

- 1.1 For the purposes of this Strategy, “Investment” means 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 (HMT) guidance on local government investments and the Prudential Code 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 broad 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 to be £324.43M as at 31/03/22 and is forecast to increase as set out in Table 1:

Table 1 – Non-Treasury Investments

Estimate 31/3/22 £M		Estimate 31/3/23 £M	Estimate 31/3/24 £M	Estimate 31/3/25 £M	Estimate 31/3/26 £M
	Investment Property				
316.60	Existing Investment Property	316.60	306.60	296.60	286.60
0.00	Property Investment Strategy	10.00	20.00	30.00	40.00
	Service Based Investments				
2.62	Manydown Loan Notes	4.07	4.35	4.15	2.75
0.00	Manydown Infrastructure Funding	5.59	14.41	25.00	25.00
5.21	Service Based Loans	4.57	3.93	2.89	1.62
324.43		340.83	349.29	358.64	355.97

- 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 external 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. As noted in section 9 of the Capital Investment Strategy, this is now actively discouraged, with restrictions being put in place on PWLB borrowing for this purpose, and by the explicit provisions of CIPFA's Prudential Code which prohibit borrowing primarily for yield (i.e. financial return).

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

	2020/21 Actual %	2021/22 Forecast %	2022/23 Forecast %
Investment Property			
Existing Investment Property	5.12	5.68	5.60
Property Investment Strategy *	0.00	0.00	0.00
*The expected level of return is between 4 & 7% (blended average 5.5%)			
Service Based Investments			
Manydown Loan Notes	6.09	8.06	4.71
Manydown Infrastructure Funding	0.00	0.00	2.60
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 £316.60M at the previous balance sheet date (i.e. 31/03/2021). A summary of the portfolio is shown in Table 3.

Table 3 – Investment Property Portfolio

	Value 31/03/2021 £M
<u>Investment Property</u>	
Houndmills Industrial Estate	50.00
Daneshill Industrial Estate	49.20
Viabes	42.70
Basing View	41.12
The Malls	11.50
Festival Place	11.70
Manydown Land	24.60
Other Industrial and Commercial Property	46.60
Property Investment Strategy Properties	39.18
	316.60

- 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 £15.30M of rent income on properties valued at £277.42M which is a gross return of 5.51%. After maintenance and running costs of £6.05M the net income is £9.25M which is a net return of 3.33%.

Property Investment Strategy 2022/23 to 2025/26

- 3.4 In 2017 Council approved specific further investment in property and set a limit of £35M (initially £30M) to invest in new and existing properties to increase the overall investment property income. These investments generate an income of £2.43M (7.48%).
- 3.5 The individual investments and the expected returns are shown in Table 4 and the current capital values shown in Table 5.

Table 4 – Property Investment Returns

	Investment		Additional
	Made	Return	Income
	£M	%	2022/23
			£M
Units 1 to 4 Armstrong Road	4.55	13.0%	0.59
Units 1 to 2 Stroudley Road	4.99	7.2%	0.36
Units 1 to 2 Winchester Road	6.01	5.3%	0.32
Veolia, Bell Road	0.47	17.0%	0.08
Lister Road (B&Q)	7.57	8.1%	0.61
Eli Lilly	8.90	5.3%	0.47
	32.49	7.4%	2.43

Table 5 – Valuations of Property Investments

	Investment	Original	Value	Valuation
	Made	Value	31/03/21	Gain
	£M	£M	£M	£M
<u>Property</u>				
Units 1 to 4 Armstrong Road	4.55	3.25	11.27	3.47
Units 1 to 2 Stroudley Road	4.99	0.43	6.51	1.09
Units 1 to 2 Winchester Road	6.01	0.00	3.50	(2.51)
Veolia, Bell Road	0.47	1.15	2.86	1.24
Lister Road (B&Q)	7.57	0.00	6.65	(0.92)
Eli Lilly	8.90	0.00	8.39	(0.51)
	32.49	4.83	39.18	1.86

- 3.6 These properties now form part of the commercial property investment income and are monitored and reported as part of the overall position.
- 3.7 Further to this the council appointed new property advisers in 2020 who have been working alongside officers to develop a new Strategic Asset Management Plan (SAMP) 2022/23 to 2025/26. Approval for the SAMP will be sought from Council in February 2022. As part of this plan, a new Property Investment Strategy is proposed which seeks to consider the council's property investment portfolio and land holdings from 2022/23 for the next 4 years to 2025/26 and expands on the portfolio's relationship with key regeneration projects.
- 3.8 The objective of the strategy is to ensure a stable long-term income with the ability to grow that income to negate the effects of inflation and obtain real term growth, inflation is seen as a risk in the medium term. The strategy will also aim to preserve and enhance capital value.
- 3.9 Central government expects local councils to be more self-sufficient in the way they fund residents' services and low interest rates means returns on council investments are lower whilst demand for services has increased.
- 3.10 Current predictions are that interest rates will remain at historically low levels for as long as government can manage as they face the challenge of addressing the exceptional level of national debt incurred as a result of the Covid – 19 pandemic and encouraging investment throughout the economy. Accordingly, levels of return from cash investments will remain at minimal levels in a likely inflationary environment.
- 3.11 This proposed strategy will address these challenges and will include active asset management strategies of the commercial property portfolio to optimise income and rebalance the portfolio in terms of use, tenure and to take account of changing legislation around sustainability which is likely to have a negative effect on some property values and portfolio performance if buildings don't meet appropriate standards in the future.
- 3.12 The current overall level of property investment (including the 2017 additional investment of £32.49M) is expected to be maintained. This in the main will therefore require the disposal of current assets with capital receipts reinvested in line with Investment Strategy.
- 3.13 The work undertaken by JLL has identified the need to reinvest circa £35M to rebalance the existing portfolio. A scheme with spend of up to £40M has been added to the Capital Programme to facilitate this to cover the period of activity to 2025/2026. The Executive Director of Corporate Services (S151 Officer) has delegation under approved Financial Regulations to rephase spend within to overall total value of the scheme following a recommendation of the Council Capital Board.

- 3.14 Property investment activity will only be undertaken once an appropriate capital receipt has been made from an asset disposal. This scheme will therefore be funded from disposal capital receipts.
- 3.15 It is however, recognised that it may be necessary to forward fund activity to make strategic purchases prior to an appropriate disposal being actioned. Therefore, a maximum sum of £10M has been allocated and funded from existing capital receipts to fund the programme spend as needed, to be reimbursed from disposal income and held as a rolling available sum.
- 3.16 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.
- 3.17 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. The returns from future property investments is expected to be in the range of 4 – 7% with a blended return of 5.5%.
- 3.18 When looking at the security of capital for property investments the DLUHC 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.
- 3.19 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.
- 3.20 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.
- 3.21 Further details on how the risks are managed and the process for ensuring effective due diligence for these investments can be found in the SAMP and Annual Property Plan 2022/23.
- 3.22 The government recommend that benchmarking is undertaken for commercial investments against other Councils and other types of investment. This activity is being undertaken by the Council's property advisers, JLL.

- 3.23 In terms of the governance arrangements for these investments, these are detailed in the Strategic Asset Management Plan 2022/23 to 2025/26 which includes the Property Investment Strategy (PIS) and the Annual Property Plan (APP) 2022/23. The approved strategy sets out the criteria, and limits on this type of investment and officers are required to operate within these criteria and limits.
- 3.24 Decisions on commercial investments are made by the Executive Director of Corporate Services (S151 Officer), after consultation with the Portfolio Holders for Property and Finance, within the limits and criteria set out in the PIS and APP.
- 3.25 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.
- 3.26 Quarterly monitoring reports on property investment activity under the strategy are presented to the Audit and Accounts Committee and half yearly to Cabinet.

4 Manydown Investments

- 4.1 The Council currently has provision of £18.06M 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.

5 Manydown North Infrastructure Funding

- 5.1 On behalf of the Manydown Development Company, Urban & Civic (U&C) have been in discussions with Homes England (HE) to secure a loan to meet the cost of accelerated infrastructure funding for Manydown North.
- 5.2 Both Hampshire County Council (HCC) and Basingstoke and Deane Borough Council (BDBC) have the opportunity to undertake this lending directly. The investment opportunity for BDBC on a 50:50 basis with HCC, has been considered with a loan of up to £25M from each authority.
- 5.3 A review of the current treasury management investment holdings has identified two funds that would benefit redemption and reinvestment currently only achieving overall marginal returns. Investment in these two funds totals £30M.
- 5.4 A similarly long term alternative investment (forming part of Treasury Management activity) would be to invest in this loan facility achieving an expected minimum interest rate of circa 2.6%.
- 5.5 Funding will only be provided once the Overarching Business Plan for the development has been agreed and will not be drawn down in one lump sum.

- 5.6 A new scheme has been added to the Capital Programme for approval in February 2022 for £25M to be funded from the redemption of the two funds noted in paragraph 6.3. These funds will be redeemed in stages to meet the draw down requirements on the £25M.
- 5.7 This alternative investment route will give a more secure return than that of the current treasury management activity, however, the investment will be significantly less liquid than current investments. This essentially will tie up the funding for a predetermined period which may require other funding sources for the councils capital spend to be considered.

6 Service Based Loans

- 6.1 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 £5.05M lent to SERCO (balance outstanding of £3.48M as at 31 March 2021) as part of the arrangements for the waste management service.
- 6.2 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.
- 6.3 The Council's total exposure to this type of loan is currently £5.84M 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.
- 6.4 In nearly all cases with service based loans the Council has a claim on the underlying assets should the organisation default on the loan.

7 Investment Performance Monitoring and Reporting

- 7.1 The Council has delegated responsibility for the monitoring and scrutiny of its investment strategies and activity to the Audit and Accounts Committee.
- 7.2 The execution and administration of the Property Investment Strategy is delegated to the Executive Director of Corporate Services (S151 Officer).
- 7.3 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.
- 7.4 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.

7.5 There is currently no formal monitoring and reporting of the service based investments.

8 Capacity, Knowledge, Skills and Culture

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

8.2 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.

8.3 For property investments the Council currently uses Jones Lang LaSalle (JLL).