Appendix 1 - Thurrock Council

Capital Strategy Report 2022/23

Introduction

This capital strategy is a refreshed report for 2022/23, giving 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.

Capital Expenditure and Financing

Capital expenditure is where the Council spends money on assets 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 or build assets. The Council has some limited discretion on what counts as capital expenditure, for example assets costing below £10k are not capitalised and are charged to revenue in year.

In 2022/23, the Council is planning capital project expenditure of £120.047m as summarised below:

Table 1a: Prudential Indicator: Estimates of Capital Expenditure in £m – Capital Projects

	2020/21 actual	2021/22 forecast	2022/23 forecast	2023/24 forecast	2024/25 forecast
General Fund services	73.262	117.595	81.496	69.782	56.546
Council housing (HRA)	18.934	54.775	39.051	16.260	18.410
TOTAL	**92.196**	**172.370**	**120.547**	**86.042**	**74.956**

The main General Fund capital projects include the Stanford Le Hope Interchange, Purfleet and Grays redevelopment, Highways Infrastructure Improvements, Provision of Care Home, Integrated Medical Centres, school expansions, and ICT improvements.

The Housing Revenue Account (HRA) is a ring-fenced account that ensures that council housing does not subsidise, or is itself subsidised, by other local services. HRA capital expenditure is therefore recorded separately, and includes expenditure over the following 3 years of £86m including £32.9m for transforming homes and £29.4m for tower block refurbishments.

Table 1b: Prudential Indicator: Estimates of Capital Expenditure in £m – New investment activity

	2020/21 actual	**2021/22 forecast**	**2022/23 forecast**	**2023/24 forecast**	**2024/25 forecast**
Capital investments	15.302	0	0	0	0

There are no planned capital investments from 2022/23 onwards following an agreed pause to the investment strategy.

Governance: Service managers bid annually in September to include projects in the Council's capital programme. Bids are collated by Corporate Finance who calculate the financing cost (which can be nil if the project is fully externally financed). The bids are then collated and prioritised by either Property Board, Digital Board or the Service Review Board. The proposed programme is then considered by Directors' Board. This includes a final appraisal of all bids including final consideration of service priorities and financing costs. The final proposed capital programme is then collated and reported with recommendations to the Corporate Overview and Scrutiny committee. The final capital programme is then presented to Cabinet and to Council in February each year as part of the overall budget setting process.

All capital expenditure must be financed, from either 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 sources in £m

	2020/21 actual	**2021/22 forecast**	**2022/23 forecast**	**2023/24 forecast**	**2024/25 forecast**
External sources	54.790	25.711	23.691	23.790	29.000
Own resources	15.805	20.907	10.790	11.046	11.307
Debt	36.903	125.752	86.066	51.206	34.649
TOTAL	**107.498**	**172.370**	**120.547**	**86.042**	**74.956**

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 that is known as the Minimum Revenue Provision (MRP). Alternatively, proceeds from selling capital assets (known as capital receipts) may be used to replace debt finance and repayments of investments on maturity will repay the associated debt. Planned MRP and use of capital receipts are as follows:

Table 3: Minimum Revenue Provision in £m

	2020/21 actual	2021/22 forecast	2022/23 forecast	2023/24 forecast	2024/25 forecast
Own resources	5.189	6.675	9.024	10.756	12.796

The Council's full MRP statement is included in the treasury management statement appended as an annex to this document.

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 CFR is expected to increase by £83.945m during 2022/23 to reflect capital project programme changes. 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 £m

	31.3.2021 actual	31.3.2022 forecast	31.3.2023 forecast	31.3.2024 forecast	31.3.2025 forecast
General Fund services	207.612	291.979	340.761	375.996	390.746
Council housing (HRA)	195.263	229.972	258.233	263.447	270.550
Capital investments	915.759	915.759	915.759	872.759	872.759
TRL Investments	29.632	28.632	35.532	78.782	71.882
TOTAL CFR	**1,348.266**	**1,466.342**	**1,550.285**	**1,590.984**	**1,605.937**

Asset management: To ensure that capital assets continue to be of long-term use, the Council has undertaken a detailed asset review in 2021/22 and the use and future of assets is being considered alongside the delivery of corporate priorities.

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 capital borrowing. The Council is currently also permitted to spend capital receipts on service transformation projects until 2024/25. Repayments of capital grants, loans and investments also generate capital receipts. The Council plans to receive capital receipts (total includes both GF and HRA receipts) in the coming financial year as follows:

Table 5: Capital (asset) receipts in £m

	2020/21 actual	2021/22 forecast	2022/23 forecast	2023/24 forecast	2024/25 forecast
Asset sales	6.931	15.000	10.000	10.000	10.000
Loans repaid	0.041	0.043	0.045	0.047	0.049
TOTAL	**6.972**	**15.043**	**10.045**	**10.047**	**10.049**

Treasury Management

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

The Council is projecting £1.460bn of borrowing at the end of 2022/23 at an average interest rate of 2.4% including £21m treasury investments at an average rate of 0.11%

- £550.581m for the capital programme (General Fund, HRA and TRL combined) and
- £915.759m for investments. In terms of the latter, the approach has generated an 11.5% return after all costs and interest are paid.

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 cheap short-term loans (currently available at around 0.30%) and long-term fixed rate loans where the future cost is known but higher (currently 0.95% to 1.37%).

Projected levels of the Council'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 £m

	31.3.2022 forecast	31.3.2023 forecast	31.3.2024 forecast	31.3.2025 forecast
Debt (incl. PFI & leases)	1,460.385	1,533.932	1,552.237	1,502.237
Capital Financing Requirement	1,466.340	1,550.285	1,633.984	1,605.937

Statutory guidance is that debt should remain below the capital financing requirement over the medium to long term but can be over for the short term recognising borrowing requirements ahead of need for future capital expenditure. As can be seen from table 6, the Council complies with this requirement.

Affordable borrowing limit: The Council is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt) each year. 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

	2021/22 Forecast	2022/23 limit	2023/24 limit	2024/25 limit
Authorised limit – borrowing	1,570.385	1,633.932	1,652.137	1,602.237
Authorised limit – PFI and leases	0.000	0.000	0.000	0.000
Authorised limit – total external debt	1,570.385	1,633.932	1,652.137	1,602.237
Operational boundary – borrowing	1,470.385	1,533.932	1,552.137	1,502.237
Operational boundary – PFI and leases	0.000	0.000	0.000	0.000
Operational boundary – total external debt	1,470.385	1,533.932	1,552.137	1,502.237

Further details on borrowing are contained in the treasury management strategy as annex 1 on this report.

Investment strategy:

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. Historical activity that will conclude as investments complete over the next several years were always based on low-risk activity, for lesser return; prioritising safety over risk. The approach has endured during the COVID-pandemic, contributing to a return of circa £115m of additional income over the last five years. 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. Both short-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.

Further details on treasury investments are contained in the treasury management strategy as annex 1 to this report.

Governance: Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Corporate Director of Resources and Place Delivery and staff, who must act in line with the treasury management strategy approved by elected members of Full Council.

Maturity structure of borrowing: This indicator is set to control the Authority's exposure to refinancing risk. The upper and lower limits on the maturity structure of borrowing will be:

Refinancing rate risk indicator	Upper limit	Lower limit
Under 12 months	100%	0%
12 months and within 24 months	60%	0%
24 months and within 5 years	60%	0%
5 years and within 10 years	60%	0%
10 years and within 40 years	60%	0%
Over 40 years	100%	0%

Time periods start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment.

Investments for Service Purposes

The Council can make investments to assist local public services, including making loans to and buying shares in local service providers, local small businesses to promote economic growth, the Council's subsidiaries that provide services. In light of the public service objective, the Council is willing to take more risk than it would with other treasury-related investments, however it still plans for such investments to break even after all costs.

Governance: Decisions on service investments are made by the relevant service manager in consultation with the Corporate Director of Resources and Place Delivery and must meet the criteria and limits laid down in the investment strategy. Most loans and shares are capital expenditure and purchases will therefore be approved as part of the capital programme.

Further details on service investments are contained in the treasury management strategy in annex 1 to this report.

Commercial Activities

With central government financial support to local public services declining, the Council decided to investigate various options to increase income and has subsequently made investments in line with the principles set out in the Council's Investment Strategy. The approach started in 2010, and its first larger investment occurred in 2016. Members then supported a move to an investment approach in 2017. In 2020, the decision was made to pause the approach.

On 20 November 2018, a Long Term Investment Strategy was taken to the Corporate Overview and Scrutiny Committee outlining the Council's approach to Service/Non-Treasury/Commercial Investments rather than the standard treasury investments. The report outlined the key principles involved, governance arrangements and the considerations required to ensure investments are thoroughly scrutinised before completion.

In 2020/21, the investment strategy was paused and following changes in the Prudential code and PWLB borrowing regulations the strategy has now been stopped with no further investments to be undertaken.

Liabilities

In addition to debt detailed above, the Council is committed to making future payments to cover its pension fund deficit (valued at £195.941m at 31 March 2021). It has also set aside £10.164m to cover risks including business rates appeals and insurance claims.

Governance: Decisions on incurring new discretional liabilities are taken by service managers in consultation with Corporate Finance and, where appropriate, the Corporate Director of Finance, Governance and Property. The risk of liabilities crystallising and requiring payment is monitored by Corporate Finance.

Revenue Budget Implications

Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP are charged to revenue, offset by any investment income receivable. The net annual charge is known as financing income; this is compared to the net revenue stream i.e. the amount funded from Council Tax, business rates and general government grants.

This shows the net financing income that is in addition to the core funding streams of the Council.

Table 9 (i): Prudential Indicator: Proportion of net financing costs to net revenue stream

	2021/22 forecast	2022/23 budget	2023/24 budget	2024/25 budget
Net financing income (£m)	(17.430)	(10.676)	(7.728)	(4.360)
Proportion of net revenue stream	14.64%	8.67%	6.04%	3.25%

For wider context, the table below shows the financing costs (Interest payable plus MRP) as a percentage of the revenue stream, excluding the investment income generated from the investment strategy. This demonstrates how this income is providing additional funding to meet service priorities including the delivery of the capital programme.

Table 9 (ii): Prudential Indicator: Proportion of financing costs to net revenue stream

	2021/22 forecast	2022/23 budget	2023/24 budget	2024/25 budget
Financing costs (£m)	27.731	32.513	35.578	36.578
Proportion of net revenue stream	23.29%	26.41%	27.81%	27.30%

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 into the future. The Corporate Director of Finance, Governance and Property is satisfied that the proposed capital programme is prudent, affordable and sustainable as set out annually in the s25 statement accompanying the setting of the annual budget.

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 Corporate Director of Resources and Place Delivery is a qualified accountant with 35 years' experience. The Council pays junior staff to study towards relevant professional qualifications including CIPFA, ACT (treasury), AAT & ACCA.

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. 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.