

Cambridgeshire and Peterborough Combined Authority Investment Strategy Report 2020/21

Introduction

The Authority invests its money for three broad purposes:

- because it has surplus cash as a result of its day-to-day activities, for example when income is received in advance of expenditure (known as **treasury management investments**),
- to support local public services, skills or economic growth by lending to or buying shares in other organisations (**service investments**), and
- to earn investment income (known as **commercial investments** where this is the main purpose).

This investment strategy meets the requirements of statutory guidance issued by the government in January 2018 and focuses on the second and third of these categories.

Treasury Management Investments

The Authority typically receives its income in cash (e.g. from grants) before it pays for its expenditure in cash (e.g. through payroll, invoices and grants). It also holds reserves for future expenditure. These activities, plus the timing of borrowing decisions, lead to a cash surplus which is invested in accordance with guidance from the Chartered Institute of Public Finance and Accountancy. The balance of treasury management investments is expected to fluctuate between £150m and £300m during the 2020/21 financial year.

Contribution: The contribution that these investments make to the objectives of the Authority is to support effective treasury management activities.

Further details: Full details of the Authority's policies and its plan for 2020/21 for treasury management investments are covered in a separate document, the treasury management strategy.

Service Investments: Loans

Contribution: The Council lends money to its subsidiaries and local businesses to support local public services, to support the provision of affordable housing and to stimulate local economic growth and skills development.

Revolving Housing Fund

In September 2018, the Combined Authority Board approved the creation of a £40m revolving fund from the £100m fund receivable from central government to bring forward 2,000 affordable homes by March 2022.

The £40m fund will gradually grow over time through financial investment, including the provision of loans to re-invest into more housing schemes.

Key objectives and principles in the service investments within the Housing Strategy include the following:

- To accelerate housing delivery to support Economic Growth.
- To create Prosperous Places where people want to live.
- To expand housing choices and opportunity through promotion of steps to promote home ownership using alternative tenure structures, potential starter homes and more shared ownership schemes.
- Promoting all Housing (not just affordable) that is in addition to the existing development pipeline and encourage accelerated delivery within adopted local plans.
- Be creative, in using a range of financial delivery mechanisms that have not traditionally been a method through which public sector organisations have supported and delivered housing. This aims to create a revolving fund that will outlast the £170m programme that will help to meet the longer term target of an additional 100,000 homes by 2037.
- An ambition to deliver 40,000 affordable homes within the same time period, to help address the affordability of housing, particularly for key workers, first time buyers and those in low and medium paid employment who cannot easily access the home ownership market without family or other third party support. This will support more sustainable communities.
- To support the spread of Community Land Trusts (CLT's) which support their local communities.
- Ensuring that housing supports the most vulnerable by offering increased choice and affordability for those requiring specialist care.
- Supporting infrastructure to enable new housing schemes through a co-ordinated approach, particularly regarding transport by making strong links across strategies and projects within the Combined Authority.
- Encouraging best use of all property assets, bringing homes that are currently excluded from the market back into market use and supporting the creation of new homes from existing built assets not currently in residential use.
- To consider using the combined authorities borrowing powers to help to accelerate schemes using financial mechanisms, where it aligns to the overall Combined Authority Investment strategy.

Local Growth Fund Loans

The CPCA offers capital loans to local companies, and other Local Authorities, on the advice of the Business Board, where the projects are considered to achieve value for money and fit with the strategic direction set out in the Local Industrial

Strategy. In 2020-21 the value of loans made available via this programme is estimated to stand at £6.6m

Security: The main risk when making service loans is that the borrower will be unable to repay the principal lent and/or the interest due. In order to limit this risk, and ensure that total exposure to service loans remains proportionate to the size of the Authority, upper limits on the outstanding loans to each category of borrower have been set as follows:

Table 1: Loans for service purposes in £ millions

Category of borrower	31.3.2019 actual			2020/21
	Balance owing	Loss allowance	Net figure in accounts	Approved Limit
Subsidiaries	0.000	0.000	0.000	20.000
Local businesses	7.227	0.000	7.227	90.000
TOTAL	7.227	0.000	7.227	110.000

Accounting standards require the Authority to set aside loss allowance for loans, reflecting the likelihood of non-payment. The figures for loans in the Authority's statement of accounts are shown net of this loss allowance. However, the Authority makes every reasonable effort to collect the full sum lent and has appropriate credit control arrangements in place to recover overdue repayments.

Risk assessment: The Authority would assess the risk of loss before entering into and whilst holding service loans. The Combined Authority approved its first loan in May 2018 and used this agreement as a 'proof of concept'. All future loans would be subject to the following risk assessment and mitigating actions:

- 1) An appropriate level of due diligence, to include the use of external advisors where appropriate.
- 2) An appropriate loan period and timing of repayments
- 3) The calculation of an interest rate that would represent 'value for money' be of 'no detriment' to the Combined Authority and to minimise the risk of State Aid challenge
- 4) Approval being subject to a business case, due diligence and loan agreement to the satisfaction of the Chief Executive, Monitoring Officer and Chief Finance Officer.
- 5) The business case would be reviewed to include focus on:
 - a. Impact of existing loans and charges on assets
 - b. Accuracy and reasonableness of Cashflow and profit forecasts
 - c. Ambition of future sales targets and income to repay loan
 - d. Provisions/allowances for contingency, inflation

- e. Review of credit worthiness of business and collateralisation of loan
- 6) First legal charge over land and assets
- 7) Regular review and valuation of the assets
- 8) Drawdown subject to a gateway process
- 9) Consideration of options of parent company guarantees
- 10) Consideration of obligations of S106 agreements

All loans are subject to approval by the Combined Authority Board.

‘Top Up’ Fund

The Treasury Management Strategy sets out provision for the Combined Authority to make ‘service investments’ from Treasury balances. Whilst the revolving £40m fund derives from the £100m grant funding for affordable housing, the ‘top up’ fund is ‘treasury’ cash, being earmarked for other projects within the Medium Term Financial Plan (MTFP), but available for investment until such time as they are required to be drawn down to fund delivery. The availability of these balances is identified within the Authority’s cashflow forecast. The criteria for the use of these balances will be consistent with the fundamental treasury management concepts of ‘Security’ first, then ‘Liquidity’ and then ‘Return’.

Service Investments: Shares

Contribution: The Council invests in the shares of its subsidiaries and local businesses to support local public services and stimulate local economic growth. Currently the CPCA owns shares in its wholly owned subsidiaries (Angle Holdings Ltd and Angle Developments East Ltd) and in the Med-tech accelerator which provides loans to SMEs in the bio-medical field to develop novel services and products, promoting GVA growth and job creation in the area.

The CPCA has approved a number of further service equity investments as part of its Business and Skills agenda, the shareholding agreements for these had not been finalised at the end of March 2020 however they are expected within the 2020-21 financial year and thus are accounted for in our indicators as set out below:

University of Peterborough Phase 1

Equity investment into a JV along with Peterborough City Council total of £23.5m.

The Growth Service

Approved by CPCA and involves equity investment of up to £7.7m of CPCA and LGF funding.

Other LGF equity investments

There are a number of smaller equity investments made within the Local Growth Fund programme, these total £5.7m currently awarded with a further pipeline of up to £5.5m.

Capital Growth Scheme Investments

In November 2019, the Combined Authority Board approved the creation of a £12m partially revolving fund of which £5.46m is earmarked for small scale equity investments into SMEs or larger companies who require investment at the higher level from £150k to £250k. These provide working capital to fund growth projects which unlock growth in jobs or scale a company to secure more income generation and jobs at a level where private sector equity finance is lacking due to its focus on high-tech, Intellectual Property (IP) based start-ups and much higher growth rates, which typically favour much higher value equity investments of at least £250k up to £2m and higher.

For this scheme, the following phases of administration apply:

1. Establish evaluation panel – create a panel of representatives who will appraise the applications and ensure there are sufficient funds available and that projects are prioritised according to outcomes and need
2. Receiving Applications – administrative support to receive and check applications.
3. Reviewing Applications – administrative support to check applications are complete and all associated documentation supporting the application is included
4. Financial due diligence check – carry out checks that the funds will be utilised correctly, the business is viable, the project is as described in the application, there is no potential for reputational damage and the project will deliver the outcomes as set out
5. State aid check – that there has been independent legal advice sought by the applicant and the grant administrator has checked this
6. Financial processes for payments and repayments – establish the routines for financially managing the share-holding and repayment requirements
7. Legal agreements/contracts - develop shareholding agreements– ensure legal advice is in place to agree contracts with applicants
8. Audit arrangements – establish mechanism for financial audit of accounts

Security: One of the risks of investing in shares is that they fall in value meaning that the initial outlay may not be recovered. In order to limit this risk, upper limits on the sum invested in each category of shares have been set as follows:

Table 2: Shares held for service purposes in £ millions

Category of company	31.3.2019 actual			2020/21
	Amounts invested	Gains or losses	Value in accounts	Approved Limit
Subsidiaries	0.000	0.000	0.000	40.000
Local businesses	0.341	0.132	0.209	7.000
TOTAL	0.341	0.132	0.209	47.000

Risk assessment: The Authority would assess the risk of loss before entering into and whilst holding shares. The approach followed would be to consider:

- 1) an assessment of the market that the Authority would be competing in, the nature and level of competition, how market/customer needs will evolve over time, barriers to entry and exit and any ongoing investment requirements;
- 2) whether to use external advisors;
- 3) risk assessment based on credit ratings and the use of credit rating agencies;
- 4) the monitoring of risk in accordance with the Combined Authority's risk management policy.

Liquidity: Investments will be subject to the drawdown requirements of the Capital programme as set out in the Medium-Term Financial Plan and as monitored in the monthly cashflow forecast.

Non-specified Investments: Shares are the only investment type that the Authority has identified that meets the definition of a non-specified investment in the government guidance. The limits above on share investments are therefore also the Authority's upper limits on non-specified investments. The Authority has not adopted any procedures for determining further categories of non-specified investment since none are likely to meet the definition.

Commercial Investments: Property

The Authority currently does not invest in property with the intention of making a profit that will be spent on local public services and has no immediate plans to do so. In the event that commercial property investments would be held in future, the Authority would consider the following:

Security: In accordance with government guidance, the Authority considers a property investment to be secure if its accounting valuation is at or higher than its purchase cost including taxes and transaction costs.

Risk assessment: The Authority would assess the risk of loss before entering into and whilst holding property investments. The approach followed would be to consider:

- 1) A full due diligence exercise covering an assessment of: the property business plan, including sensitivity and scenario analysis; the credit quality of incumbent tenants (if any); the local property market, including demand, availability and voids in current similar commercial stock; the area's economic outlook and potential; how market/customer needs will evolve over time; barriers to entry and exit and any ongoing investment requirements;
- 2) Where in-house expertise does not cover the relevant investment opportunity, we will use external advisors for all/part of the due diligence and any other specialist areas;
- 3) External advice will be monitored by relevant officers, including adherence to deadlines, regular advisory meetings and adherence to project objectives;

- 4) The risk assessment will include credit ratings as part of the overall in-depth credit assessment of tenants. The creditworthiness of tenants will be monitored on a regular basis, using external expertise where necessary to give a credit view and an early warning of possible issues. As landlord, the Authority will maintain open dialogue with tenants, including discussion of financial stress;
- 5) The Authority will monitor the performance of the property asset against business plans throughout the life of the asset, assessing its performance and contribution of continued investment against the probable returns from sale.

Liquidity: 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. Each potential investment would be considered to ensure that the invested funds can be accessed when they are needed, for example to repay capital borrowed.

Loan Commitments and Financial Guarantees

Although not strictly counted as investments, since no money has exchanged hands yet, loan commitments and financial guarantees carry similar risks to the Authority and were the Authority to enter into any, a process in line with that taken for service loans, as set out above, would be followed, including a calculation of a loss allowance where appropriate.

Investment Indicators

The Authority has set the following quantitative indicators to allow elected members and the public to assess the Authority's total risk exposure as a result of its investment decisions.

Total risk exposure: The first indicator shows the Authority's total exposure to potential investment losses. This includes amounts the Authority is contractually committed to lend but have yet to be drawn down.

Table 3: Total investment exposure in £millions

Total investment exposure	31.03.2019 Actual	31.03.2020 Forecast	31.03.2021 Forecast
Treasury management investments	166.800	150.000	50.000
Service investments: Loans	7.227	50.000	110.000
Service investments: Shares	0.209	1.000	47.000
TOTAL INVESTMENTS	174.236	161.000	207.000
Commitments to lend	30.900	10.000	10.000
TOTAL EXPOSURE	205.136	201.000	217.000

How investments are funded:

To date, all investments are funded by the Authority's useable reserves and income received in advance of expenditure. There are no immediate plans to borrow.

Rate of return received: This indicator shows the investment income received less the associated costs, including the cost of borrowing where appropriate, as a proportion of the sum initially invested. Note that due to the complex local government accounting framework, not all recorded gains and losses affect the revenue account in the year they are incurred.

Table 4: Investment rate of return

Investments net rate of return	2018/19 Actual	2019/20 Forecast	2020/21 Forecast
Treasury management investments	0.790%	0.824%	0.600%
Service investments - Loans	0.000%	3.290%	4.000%
ALL INVESTMENTS	0.790%	1.200%	1.200%