

Cambridgeshire and Peterborough Combined Authority

Capital Strategy Report ~~2021/22~~2022/23

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 Authority for many years into the future. They are therefore subject to both a national regulatory framework and to a local policy framework, summarised in this report.

Capital Expenditure and Financing

Capital expenditure is where an Authority spends money on assets, such as property, shares in companies 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 ~~2021/22~~2022/23, the Authority is planning capital expenditure of £~~132.37m~~105.39m as summarised below.

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

	2019/20 <u>2020/21</u> actual	2020/21 <u>2021/22</u> forecast	2021/22 <u>2022/23</u> budget	2022/23 <u>2023/24</u> budget
Capital investments	86.39 <u>152.28</u>	182.34 <u>176.96</u>	132.37 <u>105.39</u>	144.86 <u>58.45</u>
TOTAL	86.39 <u>152.28</u>	182.34 <u>176.96</u>	132.37 <u>105.39</u>	144.86 <u>58.45</u>

The budget figures for ~~2021/22~~ and ~~2022/23~~ and ~~2023/24~~ are taken from the Approved Capital Expenditure Programme as set out and described in the Medium Term Financial Plan approved by the Board in January ~~2021~~2022.

Governance:

The Combined Authority's Assurance Framework sets out:

(a) How the seven principles of public life shape the culture within the Combined Authority in undertaking its roles and responsibilities in relation to the use and administration of the Cambridgeshire and Peterborough Investment, incorporating the Single Pot funding. This culture is developed and underpinned by processes, practices and procedures.

(b) Alongside the Combined Authority's constitution, sets out the respective roles and responsibilities of the Combined Authority, the Business Board (the Local Enterprise Partnership) and statutory officers.

(c) The key processes for ensuring accountability, including public engagement, probity, transparency, legal compliance and value for money.

(d) How potential investments to be funded through the Cambridgeshire and Peterborough Medium Term Financial Plan, incorporating the Single Pot, will be appraised, prioritised, approved, signed off and delivered.

(e) The processes for oversight of projects, programmes and portfolios and how the progress and impacts of these investments will be monitored and evaluated.

All capital expenditure must be financed, either from external sources (government grants and other contributions), the Authority'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

	<u>2019/2020/21</u> actual	<u>2020/21/22</u> forecast	<u>2021/22/23</u> budget	<u>2022/23/24</u> budget
Grant Funding	<u>86.01146.96</u>	<u>175.57155.09</u>	<u>104.8677.49</u>	<u>84.8448.02</u>
Usable Capital Receipts	<u>0.385.32</u>	<u>6.7421.87</u>	<u>27.5490</u>	<u>30.0210.43</u>
Debt	0	0	0	0
TOTAL	<u>86.39152.28</u>	<u>182.31176.96</u>	<u>132.37105.39</u>	<u>114.8658.45</u>

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.

The Combined Authority currently does not have any debt, but is considering debt funding schemes has the ability to borrow to facilitate delivery should it be needed. While there are no current projects within the Housing directorate, and significant work is being done to establish what the financing requirements will be for MTFP which fund delivery via borrowing, the Cambridge Autonomous Metro and whether role of the Combined Authority borrowing in future affordable housing and the sustainability agenda is still in development and debt may have a role in form part of this. A provision is included in role. While the budget and Combined Authority has an allowance built into it's MTFP from 2022/23 to service approximately £40m a small amount of debt costs (based on 25-year maturity rates from PWLB as at 20th January 2021) which would cover, it is anticipated that any charges incurred from future borrowing for the potential Housing directorate debt would have to be supported by future receipts from the project delivery it funded programme. n.

The Authority'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 Authority currently has no debt and therefore no CFR.

The Authority expects that its capital financing requirement will be nil on 31st March 2021/2022 and in line with the AMHCLGDLUHC Guidance expects to charge no MRP in 2021/22/2022/23.

For capital expenditure loans to third parties that are repaid in annual or more frequent instalments of principal, the Authority will make nil MRP, but will instead apply the capital receipts arising from principal repayments to reduce the capital financing requirement instead.

Where loans are made from grant funds, there will be no Capital Finance Requirement and therefore no MRP. Where loans are debt funded, where creditworthiness of the borrower decreases or the asset value drops below the loan value, MRP will be charged on the shortfall.

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. Repayments of capital grants, loans and investments also generate capital receipts.

Treasury Management

Treasury management is concerned with keeping sufficient, but not excessive, cash available to meet the Authority'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. The Authority is typically cash rich in the short-term as revenue grant income is received before it is spent.

As at 31 December ~~2020~~2021, the Authority had no borrowing and ~~£187.5m~~£345.6m treasury investments at an average rate of ~~0.34~~12%

Borrowing strategy: The Authority's main objectives when borrowing ~~are~~would be to achieve a low but certain cost of finance while retaining flexibility should plans change in future. These objectives are often conflicting, and the Authority would therefore ~~seek~~seeks to strike a balance between cheap short-term loans (currently available at around 0.10%) and long-term fixed rate loans where the future cost is known but higher (currently 1.5 to 2.5%).

Projected levels of the Authority's total outstanding debt (which comprises borrowing, PFI liabilities, leases are shown below, compared with the capital financing requirement (see above).

Table 3: Prudential Indicator: Gross Debt and the Capital Financing Requirement in £ millions

	31.3. 2020 <u>2021</u> actual	31.3. 2021 <u>2022</u> forecast	31.3. 2022 <u>2023</u> budget	31.3. 2023 <u>2024</u> budget
Debt (incl. PFI & leases)	0	0	0	0
Capital Financing Requirement	0	0	0	0

Statutory guidance is that debt should remain below the capital financing requirement, except in the short-term. The Authority expects to comply with this in the medium term.

Liability benchmark: To compare the Authority's actual borrowing against an alternative strategy, a liability benchmark is calculated showing the lowest risk level of borrowing. Given that there are no current plans to borrow, this benchmark is currently set at the existing debt cap level to allow a small level of borrowing to facilitate delivery should it be needed, but will be kept under review.

Table 4: Borrowing and the Liability Benchmark in £ millions

	31.3. 2020 <u>2021</u> actual	31.3. 2021 <u>2022</u> forecast	31.3. 2022 <u>2023</u> budget	31.3. 2023 <u>2024</u> budget
Outstanding borrowing	0	0	0	0
Liability benchmark	0	0	<u>84.618.50</u>	<u>84.618.50</u>

Affordable borrowing limit: The Authority 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 5: Prudential Indicators: Authorised limit and operational boundary for external debt in £m

	<u>2020/21</u> <u>2021/22</u> limit	<u>2021/22</u> <u>2022/23</u> limit	<u>2022/23</u> <u>2023/24</u> limit
Authorised limit - total external debt	84.61	84.61	84.61
Operational boundary - total external debt	74.61	74.61	74.61

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 Authority'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 is 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 Authority may request its money back at short notice.

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 Head of Chief Finance Officer and staff, who must act in line with the treasury management strategy approved by the Board. Regular reports on treasury management activity are presented to the Audit and Governance Committee who are responsible for ensuring effective scrutiny of the treasury management strategy and policies in accordance with CIPFA's Code of Practice.

Investments for Service Purposes

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

Governance: Decisions on service investments are made by the relevant service manager in consultation with the Head of Chief Finance Officer and must meet the criteria and limits laid down in the investment strategy. Most loans and shares are capital expenditure and purchases and will therefore also be approved as part of the capital programme.

Commercial Activities

The Combined Authority currently does not invest in hold any commercial property for financial gain

investments.

Liabilities

The Authority is committed to making future payments to cover its pension fund deficit (valued at ~~£1.55m~~~~3.64m~~). There are currently no commitments to make future payments in relation to debt or other major liabilities. There is currently no requirement to cover risks of other provisions, financial guarantees or major contingent liabilities.

Governance: Decisions on incurring new discretionary liabilities are taken by Directors in consultation with the ~~Head of~~Chief Finance ~~Officer~~. The risk of liabilities crystallising and requiring payment is monitored by the Finance team and reported to the Audit and Governance committee. New liabilities/loans are reported to the Board for approval/notification as appropriate.

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 costs; this is compared to the net revenue stream i.e. the amount funded from general government grants.

Table 6: Prudential Indicator: Proportion of financing costs to net revenue stream

	31.3.2020/21 actual	31.3.2021/22 forecast	31.3.2022/23 budget	31.3.2023/24 budget
Financing costs (£m)	0	0	£0.43m	£0.73m 49m
Proportion of net revenue stream	0%	0%	02.7%	4.13.3%

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 into the future. The ~~Head of~~Chief Finance ~~Officer~~ is satisfied that the proposed capital programme is prudent, affordable and sustainable as demonstrated in the Medium-Term Financial Plan.

Knowledge and Skills

The Authority employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. For example, the ~~Head of~~Chief Finance ~~Officer~~ is a qualified accountant with ~~over~~ 25 years post qualification experience. The Authority pays for staff to study towards relevant professional qualifications and for all qualified staff to keep up to date with relevant 'continuing professional development'.

Where Authority staff do not have the knowledge and skills required, use is made of external advisers and consultants that are specialists in their field. The Authority currently employs Arlingclose Limited as treasury management advisers. This approach is more cost effective than employing such staff directly and ensures that the Authority has access to knowledge and skills commensurate with its risk appetite.