APPENDIX C

INVESTMENT STRATEGY

Background

1. The authority invests its money for three broad purposes:

   - The Council 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 by lending to or buying shares in other organisations (known as service investments);
   - to achieve a number of corporate objectives for Regeneration, Economic and Housing Development and achievement of the Council's Efficiency Strategy through the purchase and building of property (known as commercial investments) and

2. This Strategy focuses on the second and third of these investment categories, with the first, Treasury Management Investments being covered in more detail in the Treasury Management Strategy, Appendix B

Treasury Management Investments

3. The authority typically receives its income in cash (e.g. from taxes and grants) before it pays for its expenditure in cash (e.g. through payroll and invoices). 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 (CIPFA).

4. The balance of Treasury Management Investments is expected to fluctuate between £10m and £47.5m during the 2019/20 financial year. This is based on the authority having a constant £10m investment in the CCLA property fund, alongside having access to one current account and four money market funds, each with an internal limit of £7.5m.

5. The contribution that these investments make to the objectives of the Council is to support effective treasury management activities

Service Investments – Loans

6. The Council lends money to local residents, employees, businesses and local charities to support local public services and to help the Council achieve its Corporate Objectives, through stimulating local economic growth, regeneration of the local area, and increased provision of affordable Housing.

7. The largest loan currently forecast is to a Council Subsidiary to accelerate delivery of both housing and infrastructure and seek to increase the percentage of affordable housing on a development. Without this loan the additional community benefit desired by the Council would not have been

delivered by the private sector. By providing this loan the Council has helped to meet the corporate objective for an increased provision and a more diverse mix of housing as well as accelerating delivery.

8. 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 the risk, and ensure that the total exposure to service loans remains proportionate to both the size and aspirations of the Authority, upper limits on the outstanding loans to each category of borrower are detailed in the table on the next page:

Category of Borrower	31/03/2018 actual			2019/20
	Balance Outstanding	Loss Allowance	Net Figure in Accounts	Approved Limit
Subsidiaries	0	0	0	36,100,000
Businesses	0	0	2,500,000	8,000,000
Local Residents - Mortgages	13,000	0	13,000	13,000
Employees - Loans	99,000	-3,300	95,700	30% of employee salary
TOTAL	**112,000**	**-3,300**	**2,608,700**	

9. Due to the nature and timing of these loans, the limits will be monitored throughout the year, and should any new loans be identified for approval, limits will be adjusted accordingly and reported to Cabinet.

10. Accounting standards require the Authority to set aside loss allowance for loans, reflecting the likelihood of non-payment. The figures for loans in the Council's statement of accounts from 2018/19 onwards will be 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. Details of the recovery process are outlined in the Write Off of Irrecoverable Debts report, presented for approval to Cabinet annually.

11. The authority assesses the risk of loss before entering into and whilst holding service loans by:

- Assessing the markets in which the Council is looking to invest, in order to ascertain why the market is currently not delivering the outcomes the Council requires through its Corporate Objectives. If this is due to financial reasons the Council will then assess whether a service loan would provide the means to achieve the desired outcome.

- Upon determining that a service loan may be required, the Council will then seek external advice where necessary, this may include the use of external legal, financial and tax advice as appropriate.

- A credit check and analysis of the beneficiary's financial statements will also be carried out to determine their financial strength. Loans will only be entered into should the beneficiary be of a suitable strength, and

additional security may be sought, for instance, through a charge on land, should the Council require this.

- In order to ensure the objectives of the Council are delivered, the terms of the loan may oblige the borrower to meet certain criteria, for instance to deliver a new road to aid congestion before houses are built, or to seek to provide additional affordable housing on a housing development.

- Where possible, the Council will also place a staff member or one of its subsidiaries staff on the board of the project, in order to ensure effective ongoing monitoring of the project is maintained.

- Once the loan has been made, the Council will continue to monitor credit ratings and financial statements of the beneficiary half yearly to ensure loss adjustments can be made accurately and in a timely manner should the beneficiary's credit rating or financial performance decrease.

Commercial Investments – Property

12. The Council invests in regional commercial and residential property with the primary intention for regeneration, economic and housing development, either through the direct impact of investments within the borough, or through the indirect impact of investments within the wider region by providing additional income that is then spent on regeneration, economy and housing within the local area.

13. For example, during 2017/18 the Council purchased Link 1 & 2, two grade A office buildings in Chandler's Ford for £19.5m. This purchase enabled the Council to secure two of the best office blocks in the Borough, with high strength multinational tenants, ensuring the provision of employment in the Borough and also ensuring that when the lease expires, the Council can continue to ensure future employment in the Borough is in line with the Council's vision for making Eastleigh a prosperous place with high yet stable employment, and allowing business to thrive. Whilst these were the primary objectives of the purchase, the Council also ensured, through financial and legal due diligence, that the purchase represented sound value for money, by generating a sustainable surplus of £215k per annum. This surplus then goes towards meeting other Corporate Objectives.

14. During 2017/18 the Council also purchased One City Park in Brighton, a grade A office building for £23m. Whilst this purchase did not directly help to fund the Council's Corporate Objectives, the investment secured a sustainable surplus of £384k per annum that has then be used to directly support the Council's corporate objectives.

15. Alongside property purchases, the Council has also entered into a design and build contract to provide a new car showroom for commercial purposes on the former civic site, alongside the proposed build of a new pre-let grade A office block on the adjoining civic site. Whilst the car showroom is currently under

construction and the Office site is going through the final stages of legal documentation, the site as a whole is forecast to provide the authority with an additional ongoing sustainable surplus of approximately £450k per annum that will not only bring jobs into Eastleigh but will also help fund the Council's Corporate Objectives.

16. The authority assesses the risk of loss before entering into and whilst holding property investments by:

- Assessing the tenants covenant strength, This includes, but is not limited to, credit checks on potential tenants, meetings with the senior management of potential tenants of large value transactions and a detailed review of their accounting statements.

- Assessing a thorough financial business case, costing not only the purchase price, but also long term costs associated with the purchase such as future maintenance and void costs. This includes setting aside provisions as follows:

  a) The Council charges an interest adjustment on each property. This is where, although the Council predominantly borrows at cheap variable rates, any financial business case is charged at higher long term rates. This ensures should interest rates rise in the future, the Council will still make a financial return. This adjustment is taken to the Interest Rate Reserve, an earmarked reserve used to mitigate the risk of future rate rises affecting the Councils ability to provide services.
  b) The Council also charges a void adjustment to each business case. This reserves a percentage of the income so that when the initial lease period expires, the Council has enough funds set aside to cover the loss of income and void costs such as empty rates for up to 12 months should that tenant decide not to renew a lease, leaving the Council having to find a new tenant. This adjustment is taken to the Property Reserve, an earmarked reserve used to ensure a future loss of tenant does not affect the Councils ability to provide services.
  c) The Council also has a similar maintenance reserve, where, depending on the age and condition of the building, between 5 and 10% of all income is put in reserve each year to cover future maintenance works to the buildings. This Maintenance Reserve is then used to fund the Repairs and Renewals Programme prepared by the Property Services Team.

- Decisions on property purchases are also subject to additional levels of scrutiny through staff meetings. Discussions will occur between members of Management Team, Asset Management, Planning, Legal Services and Financial Services to scrutinise the due diligence that has been carried out, and to scrutinise financial business cases to ensure potential purchases are sound.

- Once the property has been purchased, the Council will continue to

monitor credit ratings and financial statements of the tenant half yearly to ensure loss adjustments can be made accurately and in a timely manner should the tenant's credit rating or financial performance decrease.

Capacity, Skills and Culture

17. Staff within Treasury Management hold quarterly treasury meetings with the Treasury Management Review Group (TMRG). This is a Group consisting of the Leader of the Council, and containing members of the Cabinet, Councillors from the party in power and the opposition parties, alongside senior representation from the Finance Team. The basis of these meetings is for staff to give TMRG an update on the current borrowing and investment position of the Council, as well as to update on upcoming governance changes, legislation and accounting changes, or legal changes that may affect the Council and its investment decision making going forward. This is then followed by questions from the TRMG to further their understanding of the key areas surrounding both investment and borrowing decision making, and to enable them to make informed decisions surrounding Investments.

18. During 2017/18 and 2018/19 the Council has held training sessions on Treasury Management and the current borrowing and investment environment, led by our Treasury Advisers, Arlingclose, another of these sessions is planned for 2019/20. This is a formal training evening, where both staff and advisers brief all Councillors on the current investment position of the Council, future investment position and possible changes to governance that may impact future decisions. A questions and answers session is held after the briefing where Councillors are encouraged to ask questions to both staff and Arlingclose to further their understanding of the way the Council makes decisions on both investments and borrowing.

19. To ensure staff have the correct knowledge and skills to inform investment decisions, the team currently includes:

- A Finance Team with four CIPFA qualified accountants, including two with over fifteen years of experience in Local Government accounting.
- An Asset Management Team with six RICS qualified Surveyors including four with over ten years' experience, two of which are also Registered Valuers.
- A Legal Team with 6 qualified solicitors, including four with over 10 years' experience in Local Government and 3 with significant property transaction knowledge.

20. When negotiating commercial deals, there is mandatory representation from both the Council's finance and legal staff in all stages. This is to ensure that both the prudential and legal framework that local authorities operate within is considered. Once it is ensured the Council would be operating within its powers, Finance and Legal representation will stay at the forefront of any decision made, and commercial deals must be approved internally by the Chief Financial Officer (CFO) before being formally approved by Cabinet.

Investment Indicators

21. The authority has set investment indicators to monitor the future performance of Investments and allow elected councillors and the public to assess the Council's total risk exposure as a result of its investment decisions. Moving forward these indicators – Appendix C1 will be reported to Cabinet as part of the Prudential Indicators.