**CABINET – 20 FEBRUARY 2017** **PORTFOLIO: FINANCE AND EFFICENCY**

# ASSET INVESTMENT STRATEGY

## 1. INTRODUCTION

1.1. Cabinet, at its meeting of 4 January 2017 agreed in principle to implement a new strategy to invest in commercial property either for the purpose of economic redevelopment and regeneration within the district, or for the purpose of income generation or a mixture of both and requested that a commercial property investment strategy be developed for further consideration by the Cabinet.

1.2. The proposed Asset Investment Strategy is attached to this report.

## 2. BACKGROUND

2.1. A Council priority set out in its Corporate Plan 2016 – 2020 is to help local businesses grow and to boost the economic viability of the District. In addition, the Corporate Plan states that the Council continually reviews activities and services to identify opportunities for savings and opportunities to generate income to address significant reductions in government funding, whilst at the same time maintaining services that are important to our customers.

2.2. The purpose of the Asset Investment Strategy is to make commercial property investments either for economic redevelopment or regeneration in the District, or for the purpose of income generation for the provision of services, or a mixture of both.

2.3. The February Medium Term Financial report covering the period 2017/18 – 2019/20 shows that, over that period, the Council has a projected cumulative budget shortfall of £496k, (or £896k excluding £400k savings currently allowed for but not yet identified). It is considered that a meaningful contribution towards ensuring continued delivery of the Council's key services can be achieved through investment in good quality income producing commercial property. The strategy is supplemental to other strategies being adopted by the Council that also aim to help close the Council's funding gap.

2.4. The Council already owns a limited number of investment properties. The management of these properties is undertaken by the Estates and Valuation Department in accordance with the Council's Asset Management Strategy. The Council's existing income from commercial property is generated from 23 properties with a total capital value of £9.6m. The gross rental income is £673k PA representing a gross yield of approximately 7%.

2.5. Other authorities, including many in Hampshire, make significant investments in commercial property. Investments could be funded either from the Council's own resources or by taking advantage of its ability to borrow at relatively low rates of interest from the Public Works Loan Board (PWLB) compared to the return on property assets.

2.6. Cabinet requested that a Task and Finish Group be constituted to draw up the draft Asset Investment Strategy. The Task and Finish Group has reviewed the proposed Strategy and has approved it.

## 3. FINANCIAL IMPLICATIONS

3.1. Full details of the Financial Implications are set out in the Strategy.

3.2. The management of the Council's cash is dictated within the Council's Treasury Management Strategy and is held within a variety of investment types. The average yield achieved as at December 2016 from these investments was 0.85%. The investment portfolio currently includes a modest sum (£4.4m) in pooled property and equity funds which are higher earning (5.35% achieved), with the majority of other funds being held with less than 1 year to maturity.

3.3. Local authorities are seeking to become more self-sufficient and not reliant on grant funding. An important issue when implementing the Asset Investment Strategy is the value of the property portfolio and the expected target net yield. It is recommended that a target for investment return aims to make a significant contribution towards the current forecast budget deficit mentioned in 2.3.

3.4. The experience of other local authorities indicates a gross yield of between 5% - 7% on the value of the investment is achievable on the types of commercial property likely to be of interest to a local authority. The resultant net revenue income would be compared against the cost of capital (i.e. either the cost of a loan or investment interest foregone, or a combination of both)

3.5. Although the Council's cash balances ranged between £54.7m and £86.1m to the 12 months to December 2016, they are forecast to decrease over the next few years. The level of usable General Fund reserves is currently around £18m. It is envisaged that an internal borrowing arrangement would take place to initially finance any property purchase, until such a time when either the cost of external borrowing hits a threshold or when the time comes for the internal funds to be utilised for their originally intended purpose (in essence whichever comes first).

3.6. Officers believe that the Council could currently potentially borrow funds with the PWLB at a rate of around 2.5% - 3.00%. The PWLB fixed interest rates are based on gilt yields and are published twice a day. The PWLB needs to be satisfied the Council is acting lawfully when borrowing funds.

3.7. NFDC already has substantial loans of c£144M following the Housing Revenue Account resettlement. The Council's prudential indicators, which are agreed as part of the Treasury Management Strategy and Annual Budget 2017/18, include for example, a limit on external debt to £30m on top of the HRA resettlement figure. The agreed size, funding mix and anticipated timing of the acquisitions of the investment portfolio would need to be taken into account in the prudential indicators, to include an increase in the overall external debt limit.

3.8. It is necessary for the Council to take a prudent approach to the management of its financial affairs. When assessing investments taking a prudent approach, the Council will need to consider such factors as the security against loss, the liquidity of the investment, the yield, affordability of the loan repayments, change in interest rates and property values.

3.9. An investment portfolio in the region of £30m is deemed as reasonable in the balance of risk verses reward, and is sought as a supplementary estimate to the Council's Capital budget. The Strategy will require an additional revenue resource budget of £100,000 PA and is forecast to achieve a net income in the region of £650k PA, in line with the projections set out in the Strategy.

3.10. There are a number of risks the Council should consider, all of which could have an impact on the net return to the Council as set out in section 4 of the Strategy.

3.11. The overall investment value and range of properties being acquired needs to represent a good mix and spread of risk across differing sectors. If the size of the investment is too small, then an adequate mix cannot be established.

3.12. It is important that the Council maintains an adequate level of reserves and balances to ensure it can manage any down turn in the property market and limit the impact it will have on revenue income. There is a risk that substantial expansion of the asset portfolio may result in a lower credit rating.

## 4. HUMAN RESOURCE IMPLICATIONS

4.1. Increasing the Council's investment property portfolio will have an impact on workloads within the Estates and Valuation team. Officers recommend that initially one additional full time equivalent post be created (funded within the £100,000 as per para 3.9) to help develop and manage the portfolio and its expansion. There may be additional staffing requirements within the Estates and Valuation team depending on the nature of the properties acquired.

## 5. PORTFOLIO HOLDERS COMMENTS

5.1. I am pleased to see the Council has developed an asset investment strategy that will promote economic development and regeneration in the District as well as giving the opportunity to derive financial benefit to the Council.

## 6. ENVIRONMENTAL IMPLICATIONS

6.1. There may be environmental benefits where commercial property is acquired for redevelopment or regeneration purposes.

## 7. EQUALITY AND DIVERSITY IMPLICATIONS

7.1. There are no equality and diversity implications arising from this report.

## 8. CRIME AND DISORDER IMPLICATIONS

8.1. There are no existing crime and disorder implications arising from this report.

## 9. RECOMMENDATION

9.1. That the Council:

9.1.1. Approves the Asset Investment Strategy attached to this Report.

9.1.2. Approves the proposed level of investment and the additional budgetary and staffing requirements as set out in the Strategy and this Report.

9.1.3. Delegates authority to make purchases and investments in accordance with the provisions of the Strategy as follows:

(a) The Chief Executive, the Executive Head Governance & Regulation, and the S151 Officer, in consultation with the Portfolio Holder for Finance & Efficiency and the Chairman of the Corporate Overview & Scrutiny Panel, shall have authority to make asset purchases and investments up to £5million;

(b) The Cabinet shall have authority to make asset purchases and investments above £5 million.

9.1.4. Constitutes a Property Investment Panel consisting of the Portfolio Holder – Finance & Efficiency, the Chairman of the Corporate Overview & Scrutiny Panel, the Chief Executive, the Executive Head Governance & Regulation, and the S151 Officer, for the purposes set out in the Report.

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**Background Papers:**

Asset Investment Strategy

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