South Cambridgeshire District Council

Report To:	Cabinet	2 October 2019
Lead Cabinet Member(s):	Councillor John Williams, Lead Cabinet Member for Finance	
Lead Officer:	Trevor Roff, Interim Director of Finance	

SUBJECT: INVESTMENT STRATEGY

PURPOSE

1. To consider a refreshed version of the Investment Strategy for consideration and adoption by the Council.

2. This is a key decision as the report seeks to establish a strategy that is designed to target economy, efficiency and effectiveness in the allocation of capital resources to achieve the investment priorities of the Council.

RECOMMENDATIONS

3. **That Cabinet is requested to consider the report and, if satisfied, recommend to Full Council:**

   (a) The updated Investment Strategy attached at Appendix A which includes (i) a range of investment indicators to comply with the Statutory Guidance on Local Government Investments and (ii) the governance arrangements that enable the Council to seek approval for priority investments in a timely manner in response to market conditions.

   (b) The consequent changes to the Scheme of Delegation to enable the Head of Commercial Development & Investment to progress investment opportunities, including due diligence checks, and to authorise the S151 Officer to submit non-binding offers in line with market practice.

REASON FOR RECOMMENDATION

4. To establish and approve an updated Investment Strategy that complies with CIPFA's revised Prudential Code for Capital Finance in Local Authorities (2017 edition) and Prudential Code Guidance Notes for Practitioners (2018 edition), CIPFA's Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes (2017 edition), and revised Statutory Guidance on Local Government Investments (3rd Edition) issued in February 2018.

BACKGROUND INFORMATION

Statutory Guidance on Local Government Investments

5. The Local Government Act 2003 (the Act) and supporting regulations requires the Council to 'have regard to' the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code, the CIPFA Treasury Management Code of Practice (the Code) and Investment Guidance (the Guidance) issued by The Ministry of Housing Communities and Local Government (MHCLG) in order to ensure that the Council's capital investment plans are affordable, prudent and sustainable.

6. The revised Statutory Guidance in relation to Local Government Investments, issued in February 2018, widened the definition of an investment to include all the financial assets of a local authority as well as other non-financial assets held primarily or partially to generate a profit. This wider definition includes investment property portfolios as well as loans made to wholly owned companies or associates, joint ventures or third parties. The Guidance applies for financial years commencing on or after 1 April 2018 and was reflected in the new Investment Strategy that was considered and approved by Council at its meeting on 21 February 2019.

7. Previous editions of the Guidance covered treasury investments only, but the current edition focuses on non-treasury investments including:

   - Loans made for service purposes e.g. to wholly owned companies, suppliers, local businesses, to support local public services and stimulate local economic growth;

   - Shares in companies bought for service purposes;

   - Debt Instruments (Loans) and Equity in subsidiaries;

   - Non-financial assets (e.g. property) held primarily or partially to generate profit.

8. The Guidance requires the Strategy to be approved by Full Council on an annual basis and sets out the disclosure and reporting requirements. Any mid-year material changes to the Strategy must also be subject to Full Council approval. The Strategy should also be publicly available on the local authority's website.

Investment Strategy

9. The approved Investment Strategy seeks to ensure compliance with the Government's requirements, including the need for an Investment Strategy to include:

   - the contribution that investments make towards the service delivery objectives and/or place making role of the authority, recognising that each investment can make more than one type of contribution. This could include:

     - Yield/Profit
     - Regeneration;
     - Economic benefit/business rates growth;
     - Responding to local market failure;
     - Treasury management;

     and, where the authority, classifies an investment as contributing to regeneration or local economic growth, it should be able to demonstrate that the investment forms part of a project in its Local Plan;

   - quantitative indicators that allow Councillors and the public to assess a local authority's total risk exposure as a result of its investment decisions;

   - how investments are funded and the rate of return and, where investment decisions are funded by borrowing, the indicators should reflect the additional debt servicing costs taken on;

- indicators to assess the risks and opportunities of the investment;

- the security of the investment as a paramount consideration to protect the capital sum invested from loss. Treasury management investments should consider security, liquidity and yield in that order of importance whilst other types of investment (such as property investments) should consider the balance between security, liquidity and yield based upon the risk appetite and the contribution the investment activity makes;

- demonstration that total financial exposure to loans (e.g. to local enterprises, local charities, wholly owned companies and joint ventures as part of a wider strategy for local economic growth) is proportionate and formally setting out limits on the total level of loans;

- for investment property, with a fair value above cost, the Strategy should include a statement that a fair value assessment has been made within the past twelve months, and that the underlying assets provide security for the capital investment;

- for investment property, with a fair value below cost, the Strategy should detail of the mitigating actions that the local authority is taking or proposes to take to protect the capital invested;

- how the authority has assessed the market that it is/will be competing in, the nature and level of competition, how it thinks that the market/customer needs will evolve over time, barriers to entry and exit and any ongoing investment requirements;

- whether and, if so how, a local authority uses external advisors be they treasury management advisors, property investment advisors or any other relevant persons; and how it monitors and maintains the quality of advice provided by external advisers;

- the sources of information used to assess and monitor risk;

- for financial investments that are not treasury management investments or loans (e.g. equity investments) the Strategy should set out procedures for determining the maximum periods for which funds may prudently be committed; what those maximum periods are; and how the local authority will stay within its stated investment limits;

- for non-financial investments (e.g. property) the Strategy should set out the procedures for ensuring that the funds can be accessed when they are needed, for example to repay capital borrowed, and the local authority's view of the liquidity of the investments that it holds, recognising that assets can take a considerable period to sell in certain market conditions;

- the extent to which funding expenditure to meet the service delivery objectives and/or place making role of the local authority is dependent on achieving the expected net profit from investments and the local authority's contingency plans should it fail to achieve the expected net profit;

- the commitment not to borrow more than, or in advance of needs, purely in order to profit from the investment of the extra sums borrowed and, where the authority plans to borrow or has borrowed purely to profit from the investment of the extra sums borrowed, why the local authority has decided not to have regard to the Guidance and the local authority's policies for investing the money borrowed, including management of the risks, for example, of not achieving the desired profit or borrowing costs increasing;

- the steps taken to ensure that those elected members and statutory officers involved in the investments decision making process have appropriate capacity, skills and information to enable them to take informed decisions as to whether to enter into a specific investment, to assess individual assessments in the context of the strategic objectives and risk profile of the local authority and to enable them to understand how the quantum of these decisions have changed the overall risk exposure of the local authority;

- the steps taken to ensure that those negotiating commercial deals are aware of the core principles of the prudential framework and of the regulatory regime within which local authorities operate;

- the corporate governance arrangements that have been put in place to ensure accountability, responsibility and authority for decision making on investment activities within the context of the local authority's corporate values.

10. It is appropriate to consider the Investment Strategy in the context of other relevant Council Plans and Strategies that are being refreshed in line with Business Plan objectives and priorities. This includes the Corporate Asset Plan (for non-Housing Revenue Account properties) that is also scheduled to be considered by Cabinet at this meeting and the Economic Growth Strategy which will be considered by Cabinet on 6 November 2019. There is also a need to have regard to more recent advice proffered by the Chartered Institute of Public Finance & Accountancy (CIPFA), including the outcome and learning from the Member and Officer training held on 24 April 2019 and, moreover, the need to ensure effective governance arrangements. This aspect of the review includes the consideration of the following:

    - The need to ensure that the governance framework provides effective control and enables the Council to seek approval for priority investments in a timely manner in response to market conditions;

    - The need to ensure that the Investment Strategy accords with the Scheme of Delegations, including the appropriate delegation to Officers to make non-binding offers and incur potentially abortive due diligence and feasibility costs;

    - The need to review all Corporate policies and plans to ensure consistency with the aims and objectives of the Investment Strategy;

    - The specific need to assess the Commercial estate against a comprehensive and agreed asset list, expected performance criteria and asset requirements using the Investment Strategy as a guide as to whether to hold, dispose or invest in specific assets.

11. An updated version of the Investment Strategy is attached at **Appendix A** which seeks to meet the requirements of the statutory investment guidance and effective governance arrangements. Proposed changes to the current version of the Strategy, approved on 21 February 2019, are identified in red and crossed through text.

12. The analysis at **Appendix B** sets out the issues and options arising from the CIPFA training held on 24 April 2019, and further consideration of the original draft document and guidance, together with the proposed actions.

13. The Council has a separate Treasury Management Strategy covering treasury investments and borrowing and this is subject to review on an annual basis. The Council typically receives its income (e.g. from taxes and grants) before it pays for expenditure incurred (e.g. through payroll and invoices). It also holds Reserves for future expenditure and collects local taxes on behalf of other local authorities and central government. 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 Councils borrowing and investment involves substantial sums of money and, therefore, there is a potential exposure to financial risks including the loss of invested funds and the effect of changing interest rates. The successful identification, monitoring and control of risk, is therefore central to the Council's Treasury Management Strategy.

14. In addition, investments are held for service purposes. In this regard, the Council has a wholly owned housing development company called South Cambs Limited trading as Ermine Street Housing. The Council's main objective for creating the company is to generate a financial return by operating a commercial entity to develop underutilised and surplus assets to generate value. Instead of disposing of assets and giving up future increases in value through asset sales Ermine Street Housing offers a way for the Council to retain control of these assets through its ownership of the company and, in this way, secure an additional return from development and potentially long term value in the form of rental income.

OPTIONS

15. The option of not reviewing the Investment Strategy is not considered to be appropriate. Local authorities are required to have regard to guidance issued in relation to investments and are accountable to their communities for the performance of them. Local politicians and officers operate within local governance frameworks of checks and balances to ensure that decision-making is lawful, informed by objective advice, transparent and consultative. Good governance means that proper arrangements are in place to ensure that an authority's intended objectives are achieved, and the security, liquidity and yield of investments are paramount commitments. The Council is required to obtain approval for the Investment Strategy each financial year and, where the Council proposed to make a material change to its Strategy during the year, a revised Strategy must be presented to Council for approval before the change is implemented.

IMPLICATIONS

16. In the writing of this report, taking into account the financial, legal, staffing, risk management, equality and diversity, climate change, community safety and any other key issues, the following implications have been considered:

Policy

17. The Investment Strategy has been developed to fulfil the requirements of the revised Statutory Investment Guidance, and provides the framework for:

- governance of service loans, equity investments and commercial property investment;
- assessing risk of providing loans, equity investments and investing in commercial property;
- borrowing in advance of need;
- income generating investment activities.

Legal

18. The Local Authorities (Capital Finance and Accounting) Regulations 2003 provides operational detail and specifically states that Authorities must have regard to CIPFA's Prudential Code when setting and reviewing borrowing limits. Local Authorities must also have regard to the Investment Guidance issued by Secretary of State under section 15(1)(a) of the Local Government Act 2003.

Financial

19. The Investment Strategy sets out how the Council determines its capital investment priorities in particular in relation to corporate priorities taking into account the capital resources available including borrowing in line with the Council's approved Prudential Indicators. There are no additional resource requirements as a result of the refreshed Investment Strategy, but it does provide the framework for determining investment priorities for the Council from allocated capital resources.

20. The sum of £100 million has been identified in the approved capital programme to enable investment of £20 million in each financial year until 2023/2024. Variations to these allocations are identified in the revised Investment Strategy and will require consideration and approval by Council. A full review of capital programme allocations will also be required as part of the butting determination process and this will be included as part of the budget setting report to Council on 5 February 2020.

21. It is appropriate to reconsider the level of investment given the opportunities that exist in the market to support business plan objectives and to generate income to help support and sustain the ongoing delivery of priority services to the community. There is a balance of only £6.26 million available in 2019/2020 following the initial investment of prime commercial real estate at the Cambridge Science Park (a defined "Stream 1" investment in the approved Investment Strategy).

22. Further similar prime and close to prime commercial real estate investments are currently available that are let on long leases to good covenants, but the Council does not have the financial allocation to proceed with many of these opportunities. There are also several investments that can generate regeneration or economic development benefits as well as positive financial returns for the Council (i.e. "Stream 2" investments in the approved Investment Strategy) but further consideration of the level of allocated funding will be required to enable these to proceed.

23. It is also relevant that the Council is now appointing, following procurement processes, Framework Suppliers for the pursuance of carefully assessed development opportunities that support key priorities of the Council and that can deliver positive financial returns. This investment specifically relates to Stream 3 investment [Investment Partnerships] in accordance with the Investment Strategy and, in accordance with procurement limits, these arrangements enable works up to a value of £340 million to be delivered, equally funded by the parties (i.e. up to £42.5 million per annum from the Council and a similar amount by the joint venture contractor). This is the maximum limit prescribed in the procurement framework and does not impose a requirement on the Council to commit to this level of investment. Each investment opportunity would be subject to a business case justification and appropriate due diligence before being considered for investment. This level of investment exceeds the level specified in the current Investment Strategy.

24. The revised Investment Strategy identifies the sum of £340 million for potential investment that provides (i) an allocation for Stream 1 investments in line with the potential investment pipeline, (ii) a £10 million per annum allocation in Stream 2 investments (e.g. energy storage projects or investments with regeneration benefits) and (iii) the capacity to deliver the level of investment with the two framework suppliers (subject to completion of the Members Agreements). The projection of likely investments in all three streams as follows:

Funding Allocation	2019/2020 £'000	2020/2021 £'000	2021/2022 £'000	2022/2023 £'000	2023/2024 £'000
Stream 1	40,000	60,000	80,000	100,000	120,000
Stream 2	10,000	20,000	30,000	40,000	50,000
Stream 3	-	42,500	85,000	127,500	170,000
Totals	**50,000**	**122,500**	**195,000**	**267,500**	**340,000**

Risk

25. The Investment Strategy is a key financial planning and resource management tool for the Council. An effective strategy for capital investment provides the framework for eliminating the risk of approving schemes which:

- are not affordable in either capital or ongoing revenue terms;
- do not meet legal obligations or the Council's key stated priorities.

Environmental

26. There are no environmental implications arising directly from the report. The environmental impacts of each capital investment opportunity will need to be considered as part of the feasibility assessments and evaluations.

Equality Analysis

27. In preparing this report, due consideration has been given to the District Council's statutory Equality Duty to eliminate unlawful discrimination, advance equality of opportunity and foster good relations, as set out in Section 149(1) of the Equality Act 2010. It is considered that the report has no relevance to South Cambridgeshire District Council's statutory equality duty to eliminate unlawful discrimination, advance equality of opportunity and foster good relation.

28. An equality analysis is not needed. Individual capital investments may, however, have specific equality impacts that need to be considered and evaluated.

BACKGROUND PAPERS

Where the Local Authorities (Executive Arrangements) (Meetings and Access to Information) (England) Regulations 2012 require documents to be open to inspection by members of the public, they must be available for inspection:

(a) at all reasonable hours at the offices of South Cambridgeshire District Council;
(b) on the Council's website; and
(c) in the case of documents to be available for inspection pursuant to regulation 15, on payment of a reasonable fee required by the Council by the person seeking to inspect the documents at the offices of South Cambridgeshire District Council.

The following documents are relevant to this report:

- General Fund Medium Term Financial Strategy – Report to Cabinet: 7 November 2018
- Budget Report – Report to Cabinet: 6 February 2019
- Business Plan 2019 - 2014 – Report to Council: 21 February 2019
- Medium Term Financial Strategy and General Fund Budget – Report to Council: 21 February 2019

APPENDICES

A Investment Strategy

B Investment Strategy – Summary of Key Revisions

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APPENDIX A

INVESTMENT STRATEGY

OCTOBER 2019 [REVISED]

1. INTRODUCTION

The Local Government Act 2003 (the Act) and supporting regulations requires the Council to ‘have regard to’ the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code, the CIPFA Treasury Management Code of Practice (the Code) and Investment Guidance (the Guidance) issued by The Ministry of Housing Communities and Local Government (MHCLG) to ensure that the Council’s capital investment plans are affordable, prudent and sustainable.

In February 2018 the Secretary of State issued new guidance on Local Government Investments (the Guidance), which widened the definition of an investment to include all the financial assets of a local authority as well as other non-financial assets held primarily or partially to generate a profit. This wider definition includes investment property portfolios as well as loans made to wholly owned companies or associates, joint ventures or third parties. The Guidance applies for financial years commencing on or after 1 April 2018.

The Guidance requires the Investment Strategy to be approved by Full Council on an annual basis and sets out the disclosure and reporting requirements. Any mid-year material changes to the Strategy will also need to be subject to Full Council approval.

The Council has set out within this Strategy its approach to risk and risk mitigation, including the requirement for fully tested and scrutinised business cases, sound due diligence indicators and the need for regular and formal reporting and the effective scrutiny of investment decisions and performance.

2. THE INVESTMENT STRATEGY

2.1 South Cambridgeshire is located centrally in the East of England region at the junction of the M11/A14 roads and with direct rail access to London and to Stansted Airport. It is a largely rural district which surrounds the city of Cambridge and comprises over 100 villages and 1 town, none currently larger than 8,000 persons. It is surrounded by a ring of market towns just beyond its borders, which are generally 10–15 miles from Cambridge. Together, Cambridge, South Cambridgeshire and the Market Towns form the Cambridge Sub-Region. South Cambridgeshire has long been a fast growing district and in 2011 had a population of 146,800 persons (bigger than Cambridge itself) and has become home to many of the clusters of high technology research and development in the Cambridge Sub-Region.

2.2 The Council recognises that it faces a unique set of challenges to deliver the services and infrastructure required to support the new communities on the strategic growth sites within the Greater Cambridge area, where the District will see the majority of the 22,000 jobs and 19,500 homes to be delivered between 2011 to 2031. To meet this challenge, against further funding uncertainty from central government to deliver essential services, the Council has recognised the need to make investments to ensure it has the capacity to continue to grow and deliver essential services.

2.3 The Council has taken independent advice during the development of the Strategy and continues to engage with commercial advisors and regulators to ensure that its officers and members are engaged in continual professional development in relation to property investment activities by local authorities.

2.4 **Aims:** The Investment Strategy aims to provide a robust and viable framework for the acquisition of commercial property investments and the pursuance of redevelopment and regeneration opportunities that contribute to Business Plan objectives and can deliver positive financial returns for the Council.

2.5 **Value:** The Investment Strategy identifies the sum of £340 million for prime and close to prime commercial real estate investment, investment which can generate regeneration or economic development benefits as well as positive financial returns for the Council and for investment partnerships with third party developers to deliver new homes. These streams of investment are outlined in more detail at Section 7. The Strategy also covers the existing portfolio of investments comprising of the following loans to third parties:

(a) A loan to Cambridge Ice Arena with a value of £2.5 million for a term of 25 years at a rate of 4.31%. The interest cost for the loan is based on a PWLB rate of 2.56% plus a margin of 1.75%;

(b) Loans to South Cambs Ltd (Trading as Ermine Street Housing) with a value of £63.317 million (at September 2019) at a rate of 3.78% (reviewed annually). The Council earmarked a total investment of £100 million to Ermine Street in its capital programme to enable the supply of 500 private rented housing stock; loans are based on an opportunity cost of 1% plus a margin of 2.78%.

2.6 **Contribution:** The Council invests in local commercial property with the intention that profits will be spent on local public services. The following table provides details of the current portfolio:

Category	Fair Value £000
Commercial	13,000
Offices	0
Retail	0
Industrial	0
Ground Lease	0
Agriculture	0
Other	0
TOTAL	**13,000**

2.7 **Security:** In accordance with government guidance, the Council considers a property investment to be secure if its accounting valuation is at or higher than its purchase cost including taxes and transaction costs. A fair value assessment of the Council's investment property portfolio has been made within the past twelve months, and the underlying assets provide security for the capital investment. Should year end accounts preparation and audit processes value these properties below their purchase cost, then an updated Investment Strategy will be presented to Council detailing the impact of the loss on the security of investments and any revenue consequences arising therefrom.

2.8 **Financing the Strategy:** The Council will fund the investment property acquisitions by utilising the most appropriate and efficient funding strategy available at the time of purchase. The Council has the option of utilising prudential borrowing, capital receipts, and reserves and may consider other structures such as joint ventures with pensions and insurance funds. Financing decisions will link to the Council's Medium Term Financial Strategy and Treasury Management Strategy.

2.9 **Risk Assessment:** The Council assesses the risk of loss before entering into and whilst holding property investments. The Council is engaged in the market through the proactive management of the investment portfolio, the asset valuation exercise and the economic growth activity and, through this, gaps/opportunities in the market are identified. Each asset is reviewed on an annual basis in order to review its performance, investment requirements and whether it should remain in the portfolio.

The Council intends to adopt a risk spread profile but its commercial portfolio is, at this stage, limited and not diversified (see table at 2.6 above). It is recognised, therefore, that the Council is potentially exposed to greater risk in the early period of the Investment Strategy through the absence of diversification. As the portfolio develops, there will be a need to assess the continuing appeal of the Council's property investments in the market. In some property investment classes this could be more significant than others, for example functional obsolescence in the industrial sector may have less impact on market appeal and rental growth than in the office sector. Economic obsolescence risk may be higher in markets which are more susceptible to social change and popular culture.

The Head of Commercial Development & Investment is responsible for ensuring that each investment decision is measured against the investment criteria set out in the Investment Strategy, which includes an assessment of risk. Asset investment advice is provided by retained agents and, where necessary, additional specialist advice is procured from suitably experienced external advisers. This will include the provision of pre-purchase reports and building surveys and other due diligence required to support the business case. The advice by the retained agents will include an assessment of the market and how it will evolve over time, the nature and level of competition and the impact that any asset acquisition or disposal could have on the projected income generated. The retained agent advice is monitored against the specification of requirements detailed in the invitation to tender and contract.

2.10 **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. The Council has no immediate plans or needs to sell any of the property investment assets. However, lower yielding assets may be sold and replaced with higher yielding assets within manageable risk tolerances.

2.11 **Loan Commitments:** Although not strictly counted as investments, since no money has exchanged, loan commitments and financial guarantees carry similar risks to the Council. The Council has no such loan commitments or financial guarantees.

3. PROPORTIONALITY

3.1 In setting a balanced budget (as required by statute) the Council takes into account the contribution of income that is generated by its investment activity and, in doing this, it recognises that such investment activity meets wider economic and service objectives of the Council. The table below shows the extent to which expenditure planned to meet the service delivery objectives and/or place making role of the Authority is funded by the expected net income from investments over the lifecycle of the Medium Term Financial Strategy.

Investment Net Rate of Return	2019/2020 Budget £000	2020/2021 Budget £000	2021/2022 Budget £000	2022/2023 Budget £000	2023/2024 Budget £000
Net Revenue Stream	18,590	15,651	16,262	16,479	16,528
Net Investment Income	3,238	4,765	7,148	9,533	11,372
PROPORTION	**0.17**	**0.30**	**0.44**	**0.58**	**0.69**

Note: The Net Revenue Stream will need to be updated in line with future medium term financial forecasts.

3.2 An appropriate level of contingency within the General Fund Reserve is assessed annually as part of the outturn position each year. The Council also has a contingency revenue allocation of £75,000 to cover specified "precautionary" items. These contingencies cover any net reduction in income sources, including rental income from investment properties, compared to the levels estimated.

4. BORROWING IN ADVANCE OF NEED

4.1 Government guidance is that local authorities must not borrow more than, or in advance of their needs, purely in order to profit from the investment of the extra sums borrowed.

4.2 Where exceptionally the Council chooses to disregard the CIPFA Prudential Code and Government Guidance in respect of borrowing to fund investment activity, the rationale for this decision must be explained in the Strategy.

4.3 The Council has noted and has had regard to the Guidance and has no plans to borrow in advance of need and is, therefore, compliant with the CIPFA Prudential Code in respect of this matter. The Council will only depart from it in exceptional cases, within the parameters set out in this Strategy, for the purposes of delivering Business Plan objectives and maintaining a robust financial position. In these exceptional cases, the reasons for so doing will be fully explained, together with the Council policies for investing the money borrowed, including management of the risks, for example, of not achieving the desired profit or borrowing costs increasing.

5. CAPACITY, SKILLS AND USE OF EXTERNAL ADVISORS

5.1 The Guidance requires that elected members and officers involved in the investment decision making process have appropriate capacity, skills and information to enable them to take informed decisions as to whether to enter into a specific investment. In addition, it places a duty on the Council to ensure that advisors negotiating deals on behalf of the Council are aware of the core principles of the prudential framework and the regulatory regime in which the Council operates. This will be achieved by ensuring an adequate and effective training programme, obtaining appropriate advice to inform the decision making process and by ensuring that procurement arrangements provide relevant information to potential advisers of the specific principles, regulations and governance relevant to the local authority sector.

5.2 The Council will appoint specialist advisors to provide training to ensure that relevant Officers and Members have the required skills to make informed decisions and assess the associated risks. This training will take place before any investment decisions associated with the Strategy are considered and on a regular basis to ensure that Officers are engaged in continual professional development in relation to property investment activity and that Members, as decision makers, have the skills, knowledge and relevant information to effectively assist the decision making process. This will include training for new Members of the Council.

5.3 The Council recognises that investing in land and properties to achieve business objectives and to generate returns is a specialist and potentially complex area. The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. Where skills, or capacity are lacking, the Council will engage the services of professional property, legal and financial advisors, where appropriate, to access specialist skills and resources to inform the decision-making process associated with this Strategy. The Council measures the impact of investment decisions on borrowing and affordability through Investment Indicators to ensure that the overall risk exposure remains within acceptable levels.

6. GOVERNANCE ARRANGEMENTS

6.1 It is necessary to have a framework for determining which properties and development opportunities should be invested in.

6.2 The ~~PST~~ IST will advise a designated ~~Property~~ Investment Governance Board (IGB) on potential purchases and development opportunities that meet the pre-determined selection criteria contained within the Strategy. The ~~PST~~ IST will identify investment opportunities based on the selection criteria set out in this Strategy, will carry out all necessary due diligence and will present a full business case to the IGB for approval. The structure of the IGB is also outlined in **APPENDIX 4**. The purpose of the IGB is to challenge and scrutinise investment opportunities identified by the ~~PST~~ IST, ensuring that only credible options are progressed. It also provides the forum for the strategic management of the overall portfolio of investments, consistent with the aims of the Strategy.

6.3 A designated ~~Property~~ Investment Selection Team (~~PST~~ IST), structured as outlined in **APPENDIX 4,** provides the setting for senior property, finance, service and legal professionals to share details of investment proposals ensuring that the core principle of the CIPFA Prudential Framework and the regulatory regime within which the Council operate are adhered to.

6.4 Investment decisions ~~delegated to the Executive Director~~ taken by Cabinet will be subject to the fulfilment of the minimum criteria set out within the Strategy, satisfaction with the business case and risk assessment, and will have regard to the ~~approval~~ recommendation of the IGB. Acquisitions and development opportunities that do not meet the minimum criteria set out within the Strategy may still be considered, where they would bring other compelling benefits to the District, but would require Cabinet approval.

6.5 Cabinet is required to approve investment in new capital schemes prior to any expenditure being incurred (subject to 6.6 below) and Council approval will be required if additional, or the reprofiling of, funding is required. There may be occasions when an investment opportunity may be lost by the market need for speed; in these exceptional cases, decisions may be taken by the Leader after consultation with IGB and in accordance with the Access to Information Procedure Rules as set out in the Constitution and a full report will be prepared to inform the decision, fully outlining the opportunities and risks. The requirements relating to the giving of notice of the decision in the Forward Plan and for call-in of any decision shall apply unless the urgency procedures in the Council's Constitution are required to be used for urgent investment decisions.

6.6 To enable the timely and decisive decision making which is essential in this type of industry, to respond to opportunities as they arise, regular meetings of the IGB will be scheduled. The Council's Scheme of Delegations provides the basis for enabling Officers to progress investment opportunities, including due diligence checks and the submission of non-binding offers in line with market practice.

7. INVESTMENT STREAMS

7.1 Investments will be focussed within the District, the Greater Cambridge Partnership area and the Travel to Work Area as shown in **APPENDIX 5**.

7.2 The Investment Strategy identifies the sum of £340 million for potential commercial investments into three streams of activity outlined in 7.3 below. This provides (i) an allocation for Stream 1 investments in line with the potential investment pipeline, (ii) a £10 million per annum allocation in Stream 2 investments (e.g. energy storage projects or investments with regeneration benefits) and (iii) the capacity to deliver the level of investment with the two approved framework suppliers in line with Member Agreements. The projection of likely investments in all three streams as follows:

Funding Allocation	2019/2020 £'000	2020/2021 £'000	2021/2022 £'000	2022/2023 £'000	2023/2024 £'000
Stream 1	40,000	60,000	80,000	100,000	120,000
Stream 2	10,000	20,000	30,000	40,000	50,000
Stream 3	-	42,500	85,000	127,500	170,000
Totals	**50,000**	**122,500**	**195,000**	**267,500**	**340,000**

7.3 Investment relating to commercial premises will be directed towards three streams of activity:

7.3.1 **Stream 1**

Prime and close to prime commercial real estate investment let on long leases to good covenants which will provide a secure long-term income over and above their ability to pay back the purchase price debt. The minimum target yield for a stream 1 assessment is 5% per investment, excluding MRP and the cost of borrowing.

The contributions from Stream 1 investments will include:

- Yield / profit
- Long term capital uplift

Commercial lease arrangements in relation to the Council's portfolio are classed as operating leases. International Financial Reporting Standard (IFRS) 9 relates to treatment of various financial instruments. Sundry Debtor Balances are classed as a financial instrument and all financial instruments need to be subject to impairment when the expected recoverable amount is less than the actual amount outstanding. All outstanding amounts relating to leases will be recorded at the net recoverable amount after allowing for an appropriate provision for bad and doubtful debts (If any).

7.3.2 **Stream 2**

Investment which can generate regeneration or economic development benefits as well as positive financial returns for the Council. Financial returns for the Council may come in the form of increased business rates income, New Homes Bonus where the investment is within the District and residential letting income from Build to Rent developments. The minimum target yield for a stream 2 investment is 2.5%, excluding MRP and the cost of borrowing.

The contributions from Stream 2 investments will include positive financial returns for the Council, and may also include the following:

- Investment loans to 3rd parties
- Investing in climate and environmental initiatives
- Investing in Social Capital
- Redeveloping Council owned assets
- Building homes and commercial premises
- Using public land and buildings to achieve long-term socio-economic development within the District and wider Greater Cambridgeshire Area, as identified in the Local Plan and **APPENDIX 5**.

To provide a longer term perspective for Stream 2 investments, the Internal Rate of Return (IRR) may be an appropriate metric to assess the strength of an investment. The IRR is the interest rate at which the net present value of all cash flows arising from an investment is equal to zero.

7.3.3 **Stream 3**

Investment partnerships with third party developers to deliver new homes that will include:

- Acquisition of 3rd party land
- Include public sector and bank debt
- Incorporation of grants and other funding
- A sharing of risk and reward between partners

The investment assessment criteria for all three streams are shown in **APPENDIX 1 (1a)**. The minimum target yield for a stream 3 investment is 5%, excluding MRP and the cost of borrowing. IRR may also be appropriate as a measure of an investment's rate of return.

8. PRUDENTIAL INDICATORS

8.1 The Guidance requires local authorities to develop quantitative indicators that allow Councillors and the public to assess a local authority's total risk exposure as a result of commercial property investment decisions.

8.2 Local Authorities are required to charge to their revenue account each year a Minimum Revenue Provision (MRP) to make provision for the repayment of debt, as measured by the underlying need to borrow. The MRP should be prudent and, although it is for each authority to determine the amount, the published guidance by the Government is "local authorities should align the period over which they charge MRP to one that is commensurate with the period over which their capital expenditure provides benefits". Provision has, therefore, been made for MRP in the performance indicators in line with the approved Capital and Treasury Management Strategies and based on the equal instalment method, amortising expenditure equally over the estimated useful life of the asset for which borrowing is required.

8.3 The approved Treasury Management Strategy does, however, confirm that where a loan is made to a wholly owned subsidiary of the Council, the loan is deemed to be secured on the assets of the company. Evidence of the ability to repay the loan will be based on the company's business plan and asset valuation, and no MRP will be made. Exceptionally, where capital expenditure is part of a loan agreement to other than a wholly owned subsidiary – such as the loan to Cambridge Ice Arena – MRP will be applied in these cases.

8.4 The indicators associated with the Council's proposed Commercial Property Investment Strategy are detailed below.

8.4.1 Debt to Net Service Expenditure (NSE) Ratio

This indicator measures the gross debt (as cash or loan financing) associated with Commercial Property Investments and loans to third parties as a percentage of the Council's net service expenditure, where net service expenditure is a proxy for the size and financial strength of a local authority.

Estimate £'000	2019/20	2020/21	2021/22	2022/23	2023/24	Limit
Third Party Loans	78,568	91,257	90,827	90,396	89,902	
Commercial Investments	50,000	122,500	195,000	267,500	340,000	
Funding Allocation	~~20,000~~ 128,568	~~40,000~~ 213,757	~~60,000~~ 285,827	~~80,000~~ 357,896	~~100,000~~ 429,902	
NSE	20,701	22,089	21,627	21,086	20,701	
Debt to NSE Ratio	**~~97%~~ 621%**	**~~181%~~ 968%**	**~~277%~~ 1,322%**	**~~379%~~ 1,697%**	**~~483%~~ 2,077%**	**~~500%~~ 2,100%**

The indicator shows that the debt level proposed by the Strategy will be approximately ~~up to 5 times~~ 21 times the level of the Council's net revenue budget if the proposed investment in the Strategy is funded solely from ~~borrowing~~ cash or loan financing.

Given that the Strategy will take the risk profile of investments into account in the decision-making process and the Council sees property investments as a long-term investment this ratio is reasonable. A maximum limit of ~~500%~~ 2,100% has been set for this indicator.

8.4.2 Net Commercial Income to NSE Ratio

This indicator measures the Council's dependence on the income from commercial property investments to deliver core services.

The commercial income will be the gross income from all investments made through the strategy less all operational costs, including the operational costs shown in indicator 8.4.7. All income forecasts should allow for void periods where applicable. The table below identifies gross income:

Estimate £'000	2019/20	2020/21	2021/22	2022/23	2023/24	Limit
Third Party Loans	2,132	2,511	2,499	2,487	2,474	
Commercial income	~~2,600~~ 1,107	~~3,200~~ 3,350	~~3,800~~ 7,195	~~4,400~~ 11,042	~~5,000~~ 14,344	
Total Net Income (less MRP)	3,239	4,765	7,148	9,533	11,372	
NSE	20,701	~~22,180~~ 22,089	~~21,718~~ 21,627	~~21,177~~ 21,086	~~20,786~~ 20,701	
Net Commercial income to NSE Ratio	**~~12.6%~~** 15.6%	**~~14.4%~~** 21.6%	**~~17.5%~~** 33.1%	**~~20.8%~~** 45.2%	**~~24.1%~~** 54.9%	**~~30%~~** 55%

The additional income generated from the investments set out within this Strategy will be equivalent to 54.9% of the Council's Net Service Expenditure by 2023/2024. This ratio is considered reasonable and a maximum limit of 55% has been set for this indicator.

The indicator allows for MRP in accordance with the approved Treasury Management Strategy with the following allowance for each year:

Estimate £'000	**2019/20**	**2020/21**	**2021/22**	**2022/23**	**2023/24**
Minimum Revenue Provision	0	1,096	2,546	3,996	5,446

8.4.3 **Investment Cover Ratio**

This indicator measures the total net income from property investments compared to interest expense:

Estimate £'000	2019/20	2020/21	2021/22	2022/23	2023/24
Net Commercial income	~~2,600~~ 3,239	~~3,200~~ 4,765	~~3,800~~ 7,148	~~4,400~~ 9,533	~~5,000~~ 11,372
Interest cost	~~594~~ 1,219	~~1,188~~ 3,105	~~1,782~~ 4,961	~~2,376~~ 6,817	~~2,970~~ 8,673
Investment cover Ratio	~~4.38~~ 2.66	~~2.69~~ 1.53	~~2.13~~ 1.44	~~1.85~~ 1.40	~~1.68~~ 1.31

For commercial investments within Streams 1 to 3, the rate of 2.56% (reflecting current medium to long term PWLB rates) is used to determine the interest expense in the above ratio through to 2023/2024. The interest rates on loans to third parties range from 4.31% to 3.78%. These assumptions will be revised in future years as the size of the portfolio develops. ~~The indicator shows that the net income from property investments is expected to be at least 1.68 times higher than anticipated interest expense.~~

8.4.4 **Loan to Value (LTV) Ratio**

This indicator measures the amount of debt compared to the total asset value. In the period immediately after purchase it is normal for the directly attributable costs of purchasing commercial property investments to be greater than the realisable value of the asset (e.g. because of non-value adding costs such as stamp duty). ~~A decrease in the loan to value ratio from 2020/21 reflects that debt finance will be raised through Public Works Loan Board borrowings and~~ Current market advice indicates that commercial property values are expected to remain constant for the foreseeable future, however, borrowings will be repaid.

Estimate £'000	2019/20	2020/21	2021/22	2022/23	2023/24
Funding Allocation	~~20,000~~ 128,568	~~40,000~~ 213,757	~~60,000~~ 285,827	~~80,000~~ 357,896	~~100,000~~ 429,902
Total asset values	~~86,597~~ 128,298	~~128,478~~ 217,622	~~153,509~~ 292,817	~~177,559~~ 368,011	~~201,715~~ 443,142

LTV Ratio	~~4.33~~ 1.00	~~3.21~~ 1.02	~~2.56~~ 1.02	~~2.22~~ 1.03	~~2.02~~ 1.03

Each year the Council will assess whether assets purchased via the Strategy retain sufficient value to provide security of investment using the fair value model in International Accounting Standard 40: Investment Property. If the fair value of assets is not sufficient to provide security for the capital investment the Strategy will provide detail of the mitigating actions that are being taken, or are proposed to be taken, to protect capital investment. The IST will also provide a liquidity assessment of the portfolio when undertaking the Fair Value assessment.

8.4.5 Target Income Returns (Yield)

This indicator shows the target gross yield for each stream of investment activity ~~net revenue income compared to equity~~ and is a measure of the minimum expected return for ~~achievement of~~ the property investment portfolio. ~~The net return is shown after making allowance for financing and borrowing costs.~~

Target income returns	2019/20	2020/21	2021/22	2022/23	2023/24
Stream 1	5%	5%	5%	5%	5%
Stream 2	2.5%	2.5%	2.5%	2.5%	2.5%
Stream 3	5%	5%	5%	5%	5%

8.4.6 Gross and Net Income

Estimate £'000	2019/20	2020/21	2021/22	2022/23	2023/24
Gross Income:	~~5,046~~ 4,324	~~6,509~~ 7,217	~~8,690~~ 11,182	~~9,397~~ 15,126	~~10,107~~ 18,523
Net Income	~~2,600~~ 3,239	~~3,200~~ 4,765	~~3,800~~ 7,148	~~4,400~~ 9,533	~~5,000~~ 11,372

~~The net income target of £2.6 million in 2019/2020 to £5 million by 2023/2024 from Commercial Property Investments is not currently incorporated into the Council's financial projections for the period up to 2023/2024. This income will need to be delivered if current service delivery is to be maintained by the Council.~~

~~The non-achievement of this income will require the identification of alternative savings proposals, which may result in cuts in service.~~

The achievement of the target income required from the Investment Strategy will be closely monitored as part of the Council's budget monitoring process.

8.4.7 Operating Costs

Estimate £'000	2019/20	2020/21	2021/22	2022/23	2023/24
Operating Costs	~~233~~	~~259~~	~~260~~	~~260~~	~~260~~

	261	404	541	654	767

The above operating costs relate to the cost of ~~the Council's~~ ~~PST~~ acquiring and maintaining the investments made through the Strategy. The costs shown reflect the estimated cost of internal staff, external asset management and a budget for feasibility work to conduct due diligence prior to investment ~~managing the procurement of assets under this Commercial Property Investment Strategy and developing the future pipeline of investments~~.

~~Additional operating costs have been allowed as a result of the purchase of Commercial Investment Properties. These costs will be factored into the financial appraisals as part of the purchase assessment to ensure that target net rates of return are achieved. This indicator may, therefore, need to be revised once investments are made.~~

8.4.8 **Vacancy Levels and Tenant Exposures**

Estimate £'000	2019/20	2020/21	2021/22	2022/23	2023/24
Operating Costs	~~0%~~ 3%	~~0%~~ 3%	~~0%~~ 3%	~~0%~~ 3%	~~0%~~ 3%

This indicator measures and sets targets for the void periods within the property portfolio.

The target of 3% reflects the strong tenant covenant strengths that will be required under the Stream 1 investment criteria. Void periods will be factored into the financial appraisals as part of the assessment criteria where relevant, therefore this indicator may be revised once investments are made.

APPENDIX 1: PROPERTY INVESTMENT STREAM 1

1. Objective

The objective of the Stream 1 investment criteria is to establish a framework for the identification of commercial property investments which, if acquired, would contribute to established Business Plan priorities and provide the Council with a positive rental return and capital growth.

The investment criteria are designed to ensure that funds are invested in properties that deliver yield and security commensurate with the Council's risk appetite.

Each potential investment will be evaluated to ensure the income received is sufficient to provide an acceptable rate of return following the payment of borrowing costs, acquisition costs, management fees and any running costs.

Purchases will take regard of the need to diversify the Council's property portfolio to manage risks across the entire portfolio.

The Council will procure external advisors to act on its behalf for the acquisition of investments, who will provide pre-purchase reports and building surveys to support the business case. These consultants will be managed by the Commercial Development & Investment Team, who will be responsible for monitoring the service that is provided.

2. Market Analysis and Background

As with other forms of investment at their most basic level, property investment is a trade-off between risk and return. A traditional well diversified property portfolio (spread across different property sectors and geographical regions) will deliver long term rental and capital growth with relatively low risk. Prime property in the target regions covered by this Strategy will typically provide an initial yield of between 5-7% with the additional prospect of capital growth leading to a higher total return to the Council.

The Strategy will adopt the same underlying principle of diversification in acquiring property investments offering a similar return profile. The three main property sectors will be included (industrial, office and retail) and in turn, these will be additionally diversified on criteria including location, the lease term and lot size. When added to the existing portfolio this will assist in protecting the Councils overall risk and return profile should an individual property investment cease to be income producing (for example, it is undergoing refurbishment or awaiting a new tenant).

3. Property Acquisition Methodology

Identification, consideration and recommendation of assets suitable for acquisition will be undertaken by the ~~Property Selection Team (PST)~~ IST in conjunction with outside specialist guidance and professional support, procured in accordance with the Council's established Contract Procedure Rules.

The ~~PST~~ IST, through the designated Head of Commercial Development & Investment and appointed agents, will undertake a search of the market which will include approaches and introductions of opportunities direct from the sellers, their agents and third parties. Introductions from third party agents will be accepted on a first come first served basis by verbal or written communication to the ~~PST~~ Head of Commercial Development & Investment.

Investment opportunities will initially be submitted to IST for consideration and subsequently to the Investment Governance Board (IGB). If after the introduction is made, the Council wishes to pursue the purchase further written agreement on the "basis of engagement" and fees will be required.

The use of independent consultants will be required to assess properties prior to bidding and any purchase will be subject to due diligence on all physical, financial and legal aspects of the property to address its suitability as an asset for long term security and growth.

All investments considered for purchase that meet pre-determined criteria and strategy aims (see section 4 below) will undergo qualitative and quantitative appraisal to establish portfolio suitability which will consider rental levels, location, property type, rent review and lease expiry pattern, tenant(s), industry sector, tenure, lease covenants, market exit constraints and physical and environmental factors. In addition, 3rd party advice will be called upon where specialist market knowledge is required. It is recognised that some of the cost of feasibility work and technical appraisal and assessment will be abortive.

Property investment markets are, in general, controlled by national and regional commercial property agencies and establishing links and relationships with several such property agents is the best method of sourcing suitable properties for acquisition. Staffing resources will need to be made available to source suitable property assets for acquisition that match the criteria set under the Strategy. This can be done by both recruitment into the ~~PST~~ IST team and by employing additional external expertise as required.

All commercially based investments involve risk and, at each stage of the process, the commitments made will be at risk as there can be no guarantee that a fully successful development will be achieved. The terms of the agreement between the parties will seek to mitigate the inherent risks. Moreover, the timing of the exercise can also be a critical factor in achieving optimum success, particularly in terms of market conditions, the state of the national economy and levels of investment confidence within the development industry.

4. Minimum Investment Criteria

For a Stream 1 property investment to be considered by the ~~Property Investment Governance Board~~ IGB for recommendation to ~~the Executive Director~~ Cabinet for approval it must:

4.1. Achieve a minimum weighted score of 100 from the investment criteria matrix shown in **APPENDIX 1 (1a)**;

4.2. Have a Net Initial Yield of 5% after making allowance for purchase~~rs~~ costs;

4.3. Be accompanied by a full business case prepared by the ~~PST~~ IST.

Each potential property investment will undergo a qualitative and quantitative appraisal, together with a risk assessment, to establish portfolio suitability and the legal and financial implications of the purchase.

The findings of these appraisals will be reported to the IGB as part of the business case. **APPENDIX 1 (1b)** details the specific areas that will be included in the business case as a minimum.

All acquisitions, where relevant, will be subject to building and plant survey, independent advice and valuation.

An investment opportunity that does not meet the minimum criteria under investment stream 1 may have separate investment or regeneration benefits and, therefore, may be considered separately under Stream 2 of the strategy.

5. Risk Management

5.1. Financing Risk: As with all investments, there are risks that capital values and rental values can fall as well as rise. To mitigate against future unfavourable market forces, Stream 1 acquisitions will be made on the basis that the Council is willing and capable of holding property investments for the long term i.e. 35 years +. This will ensure income and capital returns are considered over the long term thereby smoothing out any cyclical economic/property downturns.

Where the purchase of a property is reliant on increases in borrowing the business case will factor in fixed rate borrowing costs. By utilising fixed rate borrowing options the Council will be protected from future increases in financing costs. The Council can mitigate the limitations that come with the term commitment characteristic of fixed rate options through using a portfolio of loans of different terms at different rates, as part of its wider Treasury Management Strategy, thereby creating options to ‘recycle’ loans for other purposes, should net disposals of assets held within the Investment Strategy exceed the value of net acquisitions.

5.2. Portfolio Risk – void periods: To mitigate the risk of void periods where the property is either partially or fully vacant, or a tenant has defaulted on its rental obligations, the investment portfolio will be actively managed. The investment criteria specified in the scoring matrix will tend to favour secure property investments i.e. high-quality buildings in prime locations, thus mitigating the risk of void periods on re-letting.

Void periods for commercial investment properties acquired under this Strategy will be monitored and vacancy levels will be reported to the IGB throughout the year so that they can be actively managed.

6. Portfolio Management

Newly purchased property acquired under this Strategy would be added to the existing portfolio and the Commercial Development & Investment Team (currently comprising the Head of Commercial Development & Investment, the Delivery & Innovations Officer and the Green Energy Investment Officer), would undertake asset and property management to maintain and improve the performance of an investment property; with established core staff supplemented, as required, by external commercial asset investment/management advisors from approved budgets ~~or additional specialist resources may need to be bought in as necessary~~. This would include ensuring statutory and regulatory compliance, tenant compliance, landlord responsibilities, securing receipt of rents, dealing with voids and insurance matters. The costs associated with these areas would be considered in the financial appraisal for the property acquisition.

The property asset management will be subject to an annual review and incorporated within the Asset Management Plan (Housing Revenue Account) and Corporate Asset Plan (General Fund) which are presented to Full Council annually.

APPENDIX 1 (1a) – Investment Criteria Matrix

The ~~PST~~ IST will score the property against the scoring criteria shown below in order of priority. The minimum score for Stream 1 at least 100 out of a maximum score of 184; this is equivalent to at least the 54th percentile of the maximum. There will however be a trade-off between the level of return and the score. For example, a high return would reflect higher risk and consequently a lower score; conversely, a lower level of return would reflect a lower level of risk and a higher score. The Investment Criteria Matrix is comparable with methods used by other local authorities, such as New Forest, Kettering and Redditch, which all broadly follow a format recommended by CIPFA.

The table below shows the suggested scoring criteria to be applied when considering an investment property.

Score		**4**	**3**	**2**	**1**	**0**
Scoring Criteria	**Weighting Factor**	**Excellent / very good**	**Good**	**Acceptable**	**Marginal**	**Unacceptable**
Location	12	Major Prime	Micro Prime	Major Secondary	Micro Secondary	Tertiary
Tenancy Strength	10	Single tenant with strong financial covenant	Single tenant with good financial covenant	Multiple tenants with strong financial covenant	Multiple tenants with good financial covenant	Tenants with poor financial covenant strength / vacant
Tenure	9	Freehold	Lease 125 years plus	Lease between 50 & 125 years	Lease between 20 & 50 years	Lease less than 20 years
Occupiers remaining lease length	5	Greater than 10 years	Between 7 and 10 years	Between 4 and 7 years	Between 2 and 4 years	Less than 2 years; vacant
Building Quality / obsolescence	4	Newly Built (useful life 50+ years)	Recently refurbished (within the past 5 years)	Average condition and likely to continue to be fit for current use for 25+ years	Aged property with redevelopment potential	Nearing end of useful life / unlikely to continue when lease expires
Repairing obligations	4	Full repairing and insuring	Internal repairing – 100% recoverable	Internal repairing – partially recoverable	Internal repairing – no recoverable	Landlord
Lot size	2	Between £6m and £12m	Between £4m & £6m or £12m and £18m	Between £2m & £4m or £18m and £20m	Between £1m & £2m or £20m & £25m	Less than £1m or more than £25m

INVESTMENT CRITERIA DEFINITIONS

Location - property is categorised as prime, secondary or tertiary in terms of its location desirability. For example, a shop located in the best trading position in a town would be prime, whereas a unit on a peripheral neighbourhood shopping parade would be considered tertiary.

Tenancy Strength – the financial strength and risk of failure of a tenant determines the security of the property's rental income. A financially weak tenant increases the likelihood that the property will fall vacant. Rating agencies, such as Dun & Bradstreet are often used to evaluate covenant strength, ranging from "5A" to "HH" to reflect company size based upon worth or equity, and a Composite Credit Appraisal from 1 to 4 to reflect the assessment of the firm's creditworthiness. The minimum acceptable financial strength for any given tenant will be determined through financial appraisal of company accounts and the use of appropriate methods of risk assessment and credit scoring. To minimise management and risk, the preference will be for single occupancy investments wherever possible.

Tenure – anything less than a freehold acquisition will need to be appropriately reflected in the price**.** If leasehold, is the lease free from unencumbered/onerous terms? Is the rent periodically reviewed to take into account inflation and upward market movement?

Occupational Lease Length – the lease term will determine the duration of the tenant's contractual obligation to pay rent. The most attractive investments offer a long lease with a strong tenant covenant. The lease term will reflect any tenant break clauses. The optimum lease length will depend on the sector, with commercial B1 offices typically 7+years and 10+ years for industrial. Retained agents will be expected to qualify the quality of the length lease in their pre-acquisition report.

Building Quality – a brand new or recently refurbished building with an anticipated life of at least 40 years will not usually require capital expenditure for at least 15 years. This is attractive for income investors requiring long term rental income with the minimum of ongoing capital expenditure.

Repairing Obligations – under a Full Repairing & Insuring Lease (FRI), the tenant is responsible for the building's interior and exterior maintenance / repair. The obligation is limited to the building's interior under an Internal Repairing & Insuring Lease (IRI). The preference will be to favour FRI terms (or FRI by way of service charge i.e. all costs relating to occupation and repairs are borne by the tenants and administered through a service charge).

Lot Size – to maintain portfolio balance the preference will be for no single property investment to exceed £12m for a single let property.

In addition to the above criteria the IGB ~~and the Executive Director~~ should, when assessing the merits of an investment, specifically consider compatibility with all SCDC policies on matters relating to use such as: -

- Alcohol or tobacco production or sale;
- Animal exploitation;
- Environmentally damaging practices;
- Gambling;
- Pornography.

APPENDIX 1 (1b) – Stream 1 Business Case

The ~~PST~~ IST will prepare a business case for Stream 1 investments where the minimum weighted score target has been met. The business case will include as a minimum:

a) Financial Appraisal

A detailed financial appraisal setting out the projected income and costs associated with a potential acquisition along with an assessment of the proposed financing options and associated risks and considerations. This will include an assessment of the net yield over various scenarios up to a 50 year period, and include the following inputs:

- anticipated void periods at the end of the initial and subsequent occupiers lease(s);
- anticipated Capital Expenditure required by the Landlord, taking into account the age and condition of the premises and Landlords repairing obligations;
- assumptions in the approved Capital and Treasury Management Strategies.

b) Lease Classification

A lease should be classified, for accounting purposes, as an operating lease rather than finance lease, to ensure that all rental income can be treated as revenue income (rather than a mix of capital receipt and revenue income). Operating leases are those where the risks and rewards of ownership are retained by the lessor (the Council) and must meet certain criteria. The main criteria being that the lease term should not be for the major part of the property's economic life and at the start of the lease, the total value of minimum lease payments (rents) should not amount to a significant proportion of the value of the property.

c) Risk Management Assessment

A detailed risk assessment of the potential purchase, including but not limited to:

- Specific risks associated with individual assets;
- Tenant default on rental payment (covenant risk);
- Risk of failure to re-let (void risks);
- Costs of ownership and management;
- Differing lease structures (e.g. rent review structure, lease breaks);
- Sector risk (portfolio spread);
- Provide an exit strategy financial assessment as a 'worse case' scenario;
- Liquidity assessment;
- LTV ratio assessment.

Market Risks, including risks of structural change or market failure, which may affect the market as a whole or particular subsectors or groups of property:

- Illiquidity upon sale (e.g. lot size, transaction times, availability of finance);
- Failure to meet market rental expectations (forecast rental growth);
- Failure to meet market yield expectations (forecast yield shift);
- Risk of locational, economic, physical and functional depreciation through structural change;
- Risks associated with legislative change (e.g. planning or changes in fiscal policy).

d) Portfolio Assessment

An assessment to establish suitability against the Council's existing property portfolio which will consider rental levels, location, property type, rent review and lease expiry patterns, industry sector, tenure, lease covenants, market exit constraints and physical and environmental factors.

e) Report on Title

To confirm ownership.

APPENDIX 2: PROPERTY INVESTMENT STREAM 2

1. Objective

The objective of the Stream 2 investment criteria is to establish a framework for the identification of properties or land for redevelopment. These opportunities may deliver placemaking or economic development benefits, as defined in the Councils Business Plan, as well as positive financial returns for the Council in the form of future revenue income streams or capital uplifts. Future revenue income streams could include increases in retained business rates income and New Homes Bonus.

Developed properties may be retained for the benefit of their long-term rental income and will become an investment asset after completion. The decision on whether or not these investments would meet the overall objectives of this Strategy will be informed by a financial appraisal as described in Appendix 1.

The Stream 2 investment criteria will be designed to ensure that the financial returns delivered from investments are commensurate with the deemed levels of associated risk. A higher risk investment will therefore require the delivery of greater financial returns.

2. Market Analysis and Background

Stream 2 investment opportunities could come in a diverse range of forms. Examples include, but are not limited to:

- Investing in climate and environmental initiatives, further exploiting and supporting green energy generation and maximising energy efficiency
- Investing in Social Capital
- Redeveloping Council owned assets;
- Building homes and commercial premises;
- Using public land and buildings to achieve long-term socio-economic development within the District and wider Greater Cambridgeshire Area, as identified in the Local Plan and Appendix 4 of this Strategy;

As with other forms of investment there is a trade-off between risk and return. Given the more speculative nature of this type of investment activity the risks associated with this type of investment may, in some cases, be higher than those associated with Stream 1 activity. It may be possible to share risks and rewards of Stream 2 activities with adjoining councils and other public sector and private sector partners.

The assessment criteria for Stream 2 activities needs to be agile enough to allow significantly different schemes to be assessed using the same overarching principles.

For a Stream 2 property investment to be considered by the IGB ~~and the Executive Director~~ it must:

a) Deliver a rate of return commensurate with the deemed level of risk associated with the investment;

b) Be accompanied by a full business case prepared by the ~~PST~~ IST, and other officers where relevant.

The investment opportunities considered under Stream 2 could vary significantly and, due to the speculative nature of some schemes, there will be higher risks attached to some investment opportunities.

Each potential Stream 2 investment will undergo a qualitative and quantitative appraisal and risk assessment to establish the financial returns, financial and legal implications and risks associated with the purchase. The findings of these appraisals will be reported to the IGB as part of the business case.

An investment opportunity that does not meet the minimum criteria under investment stream 2 may have separate investment or regeneration benefits and, therefore, may still be considered for progression, however, decision making in this case is to be reserved to the Cabinet. For investments where there is a variable revenue stream, such as some energy projects, or a long time gap between investment and first revenue, such as development projects, alternative valuation options, such as the Internal Rate of Return (IRR) may be appropriate as a measure of an investment's rate of return.

3. Property Acquisition/Development Methodology

Identification, consideration and recommendation of assets suitable for acquisition and/or development will be undertaken by the ~~PST~~ designated Head of Commercial Development & Investment in conjunction with internal resource and outside specialist guidance and professional support, as required, procured in accordance with the Council's established Contract Procedure Rules. These investment opportunities will initially be submitted to IST for consideration and subsequently to the IGB.

All investments considered for purchase will undergo qualitative and quantitative appraisal to establish portfolio suitability and risks. In addition, 3rd party advice will be called upon where specialist market knowledge is required. It is recognised that some of the cost of feasibility work and technical appraisal and assessment will be abortive.

All commercially based investments and/or developments involve risk and, at each stage of the process, the commitments made will be at risk as there can be no guarantee that the investment will be secured or a fully successful development will be achieved. The terms of the agreement between the parties will seek to mitigate the inherent risks. Moreover, the timing of the exercise can also be a critical factor in achieving optimum success, particularly in terms of market conditions, the state of the national economy and levels of investment confidence within the development industry.

4. Green Energy Projects

The approved Business Plan 2019-2024 identifies the following Focus, Actions and Measures which relate to green energy investments within the 'Green to our core' priority:

Focus	Action	Measures
We will become a Zero Carbon Council	In recognition of the global climate and health emergency, develop an action plan to deliver a zero-carbon future for South Cambridgeshire	• Gather evidence to establish a carbon baseline by December 2019. • Establish the resources and budget needed to address the zero-carbon pledge for the end of March 2021 budget. • Run a zero-carbon conference to develop scenarios and learn from best practice to drive decarbonisation by 2050. • Commit to a medium-term carbon action plan by April 2020.

We will increase green energy generation and promote environmentally friendly energy consumption	Explore opportunities for renewable energy generation and maximise the energy efficiency of the Council offices and estate. Provide support and guidance to community groups for projects that will reduce reliance on fossil fuels and promote behaviour change to help achieve the zero-carbon target. Look into how electric vehicle charging points can be delivered in the district.	• Complete an assessment of investment opportunities at our Cambourne office and Waterbeach Depot by June 2019. • Commission green energy project(s) to fully invest the Renewable Energy Fund by end of March 2021. • Reduction in grid energy usage • Renewable energy generated onsite • Reenergise the Sustainable Parish Energy Partnership and investigate opportunities for helping local groups secure grant funding to kick start projects by the end of April 2019.

The Investment Strategy will develop projects identified in the Green Energy Programme, which is responsible for co-ordinating transformation activities within the South Cambridgeshire District Council commercial estate and assess these using the same criteria as other Stream 2 investments.

5. Minimum Investment Criteria

In addition to the investment criteria matrix in **APPENDIX 1 (1a)**, Stream 2 investments will be assessed for their strategic fit against the Objectives and Focus Areas contained within the 2019-2024 Business Plan.

5.1. Business Plan Objectives

The IGB will from time to time advise the target scores for the business plan objectives, and the weighting to be given to individual focus areas within each business plan area

6. Risk Management

6.1. Financing Risk: As with all investments, there are risks that capital values, rental values and development values can fall as well as rise. Where the acquisition or development is reliant on increases in borrowing the business case will factor in fixed rate borrowing costs commensurate with the anticipated holding period of the asset. By utilising fixed rate borrowing options the Council will be protected from future increases in financing costs.

Financial returns from Stream 2 activities may come in the form of capital receipts either in place of or in addition to revenue returns. This would need to be considered carefully as part of the overall Strategy given the requirement to achieve net revenue returns of 2.5% from the investment strategy overall.

7. Business Case

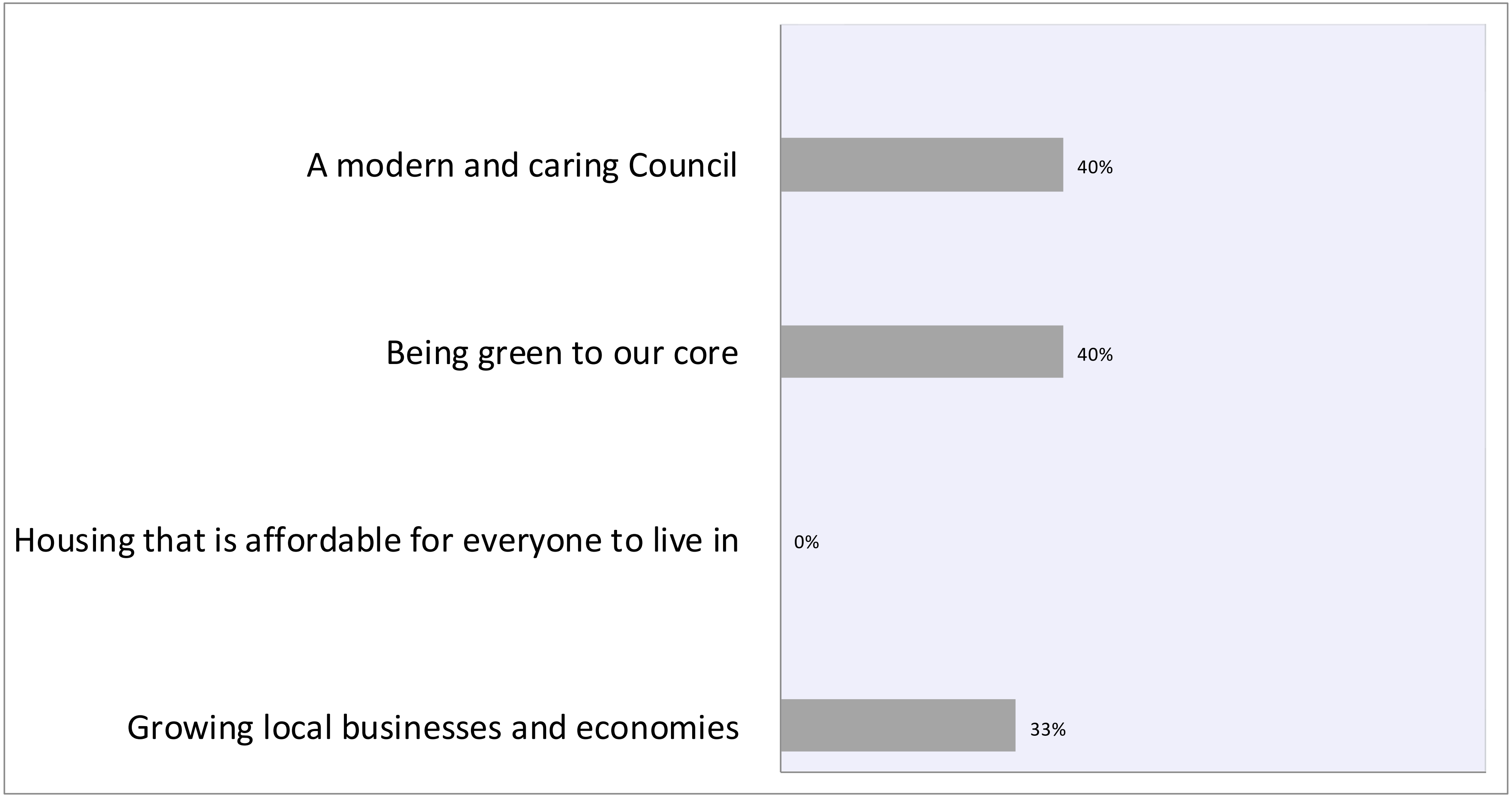
The ~~PST~~ IST will prepare a business case for Stream 2 investments where the minimum weighted score target has been met (**APPENDIX 6**).

The minimum score target will be determined by the ~~Interim Executive Director~~ Head of Commercial Development & Investment and their Team, in consultation with the Lead Member for Finance, once Business Plan objectives and focus areas have been finalised.

EXAMPLE: ENTERPRISE ZONE INVESTMENT / DEVELOPMENT – STREAM 2 SCHEME FIT AGAINST DRAFT BUSINESS PLAN

	Draft Business Plan areas	score	focus area	actions	measures
1	**Growing local businesses and economies**	33%	We will make it easy to do business in South Cambridgeshire	Deliver support to start-ups and small businesses that is not available elsewhere to help them grow, create new local jobs and deal with the impacts of Brexit	Number of new start-ups and small business growth by 2024
			We will improve environmentally friendly transport links	Improve walking, cycling and public transport links between existing villages and employment sites	Successful delivery of new or improved travel routes
2	**Housing that is affordable for everyone to live in**	0%			
3	**Being green to our core**	40%	We will increase green energy generation and promote environmentally friendly energy consumption	Explore opportunities for renewable energy generation and maximise the energy efficiency of the Council offices and estate.	Renewable energy generated onsite
			We will maintain and improve air quality across the district	Reduce carbon footprint and impact on air quality of the Council's activities	Install electric vehicle charging points at our Cambourne and Waterbeach offices for staff, members and visitors
4	**A modern and caring Council**	40%	We will generate new and innovative sources of income to invest in services for local people	Develop options to generate income by investing in the district in line with the criteria set out in the Council's investment strategy	Income generated from investments
			We will reduce costs and improve customer service	Develop and support Councillors to ensure that they can best serve their communities	Carry out a programme of Member development and training as part of the Organisational Development strategy

EXAMPLE: ENTERPRISE ZONE INVESTMENT / DEVELOPMENT – STREAM 2 SCHEME FIT AGAINST DRAFT BUSINESS PLAN


A modern and caring Council
40%
Being green to our core
40%
Housing that is affordable for everyone to live in
0%
Growing local businesses and economies
33%

APPENDIX 3: PROPERTY INVESTMENT STREAM 3 – INVESTMENT PARTNERSHIPS

1. Objective

The objective of the Stream 3 investment criteria is to establish a framework for the identification of properties or land for development of new homes through Investment Partnerships. These opportunities may deliver regeneration or economic development benefits as well as positive financial returns for the Council in the form of future revenue income streams or capital uplifts. Future income streams may include:

- Rental income from Council Housing (HRA Affordable Homes);
- Rental income from Private Rented Sector Housing (PRS) through Ermine Street Housing;
- Capital receipts from Intermediate Home Ownership staircasing;
- Capital receipts from Right to Buy;
- Increases in retained business rates;
- New Homes Bonus.

Developed properties may be retained for the benefit of their long-term rental income and will become an investment asset after completion. The decision on whether or not these investments would meet the overall objectives of this Strategy will be informed by a financial appraisal as described in Appendix 1.

The Stream 3 investment criteria will be designed to ensure that the financial returns delivered from investments are commensurate with the deemed levels of associated risk. A higher risk investment will therefore require the delivery of greater financial returns.

2. Market Analysis and Background

Stream 3 Investment Partnerships could come in a diverse range of forms. Examples include, but are not limited to:

- Building homes and commercial premises;
- Using public land and buildings to achieve long-term socio-economic sustainability for the District and wider Greater Cambridgeshire Area, as identified in the Local Plan and Appendix A4 of this strategy.

As with other forms of investment there is a trade-off between risk and return. Given the more speculative nature of this type of investment activity the risks associated with this type of investment may, in some cases, be higher than those associated with Stream 1 activity. However, these risks and rewards would be shared with the investment partner.

The assessment criteria for Stream 3 activities needs to be agile enough to allow significantly different schemes to be assessed using the same overarching principles.

3. Minimum Investment Criteria

For a Stream 3 property investment to be considered by the IGB it must:

- Deliver a rate of return commensurate with the deemed level of risk associated with the investment;
- Be accompanied by a full business case prepared by the ~~PST~~ IST, and other officers where relevant.

The scoring matrix for Stream 3 investments will be based on the targets for Stream 2 investments. Schemes with higher risks will be expected to deliver higher levels of return to cover the risk considerations, and only schemes that deliver the assessed rate of return will pass the minimum assessment criteria.

Each potential Stream 3 investment will undergo a qualitative and quantitative appraisal and risk assessment to establish the financial returns, financial and legal implications and risks associated with the purchase. The findings of these appraisals will be reported to the IGB as part of the business case.

An investment opportunity that does not meet the minimum criteria under investment stream 3 may have separate investment or regeneration benefits and, therefore, may still be considered for progression, however, decision making in this case is to be reserved to the Cabinet rather than the IGB. For investments where there is a variable revenue stream, such as some energy projects, or a long time gap between investment and first revenue, such as development projects, alternative valuation options, such as the Internal Rate of Return (IRR) may be appropriate as a measure of an investment's rate of return.

4. Acquisition/Development Methodology

Identification, consideration and recommendation of assets suitable for acquisition and/or development will be undertaken by the ~~PST~~ designated Head of Commercial Development & Investment in conjunction with internal resource and outside specialist guidance and professional support, as required, procured in accordance with the Council's established Contract Procedure Rules. These investment opportunities will initially be submitted to IST for consideration and subsequently to the IGB.

All investments considered for purchase will undergo qualitative and quantitative appraisal to establish portfolio suitability and risks. In addition, 3rd party advice will be called upon where specialist market knowledge is required. It is recognised that some of the cost of feasibility work and technical appraisal and assessment will be abortive.

All commercially based investments and/or developments involve risk and, at each stage of the process, the commitments made will be at risk as there can be no guarantee that the investment will be secured or a fully successful development will be achieved. The terms of the agreement between the parties will seek to mitigate the inherent risks. Moreover, the timing of the exercise can also be a critical factor in achieving optimum success, particularly in terms of market conditions, the state of the national economy and levels of investment confidence within the development industry.

In addition to the investment criteria matrix in **APPENDIX 1 (1a)**, Stream 3 investments will be assessed for their strategic fit against the Objectives and Focus Areas contained within the 2019-2024 Business Plan.

The IGB will from time to time advise the target scores for the business plan objectives, and the weighting to be given to individual focus areas within each business plan area.

5. Risk Management

5.1. Financing Risk: As with all investments, there are risks that capital values, rental values and development values can fall as well as rise. Where the acquisition or development is reliant on increases in borrowing the business case will factor in fixed rate borrowing costs commensurate with the anticipated holding period of the asset. By utilising fixed rate borrowing options the Council will be protected from future increases in financing costs.

Financial returns from Stream 3 activities may come in the form of capital receipts either in place of or in addition to revenue returns. This would need to be considered carefully as part of the overall Strategy given the requirement to achieve net revenue returns of 2.5% from the investment strategy overall.

6. Business Case

The ~~PST~~ IST will prepare a business case for Stream 2 investments where the minimum weighted score target has been met (**APPENDIX 6**).

The minimum score target will be determined by the ~~Interim Executive Director~~ Head of Commercial Development & Investment and their Team, in consultation with the Lead Member for Finance, once the Business Plan objectives and focus areas have been finalised.

APPENDIX 4: GOVERNANCE

Full Council

Scrutiny & Overview

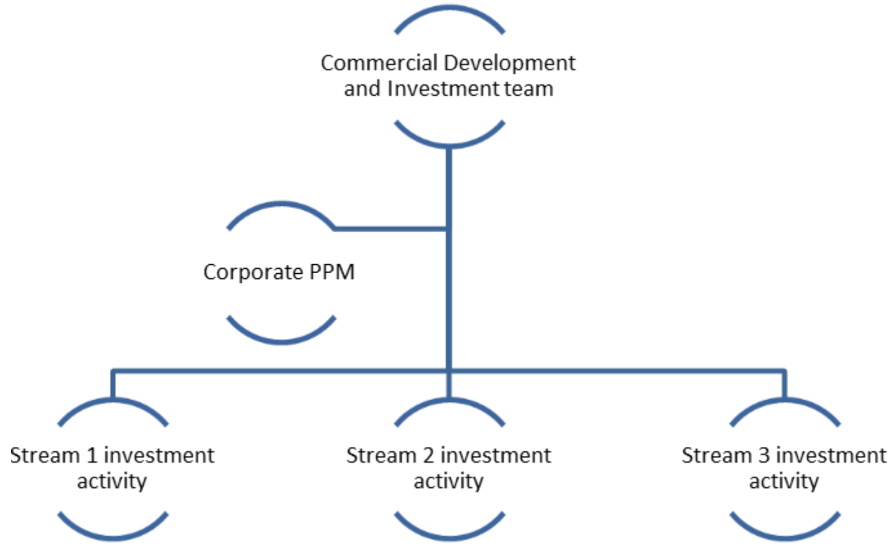
Cabinet

Investment Governing Board – approves recommendations within approved scheme of delegations, with recommendations to Council as appropriate

Chief Executive Officer	S151 Officer	Leader	Deputy Leader/ Lead Cabinet Member for Finance

Investment Selection Team – develops Stream 1, 2 & 3 investment recommendations for IGB approval

Chief Executive Officer	S151 Officer	Head of Commercial Development & Investment	Director	Monitoring Officer

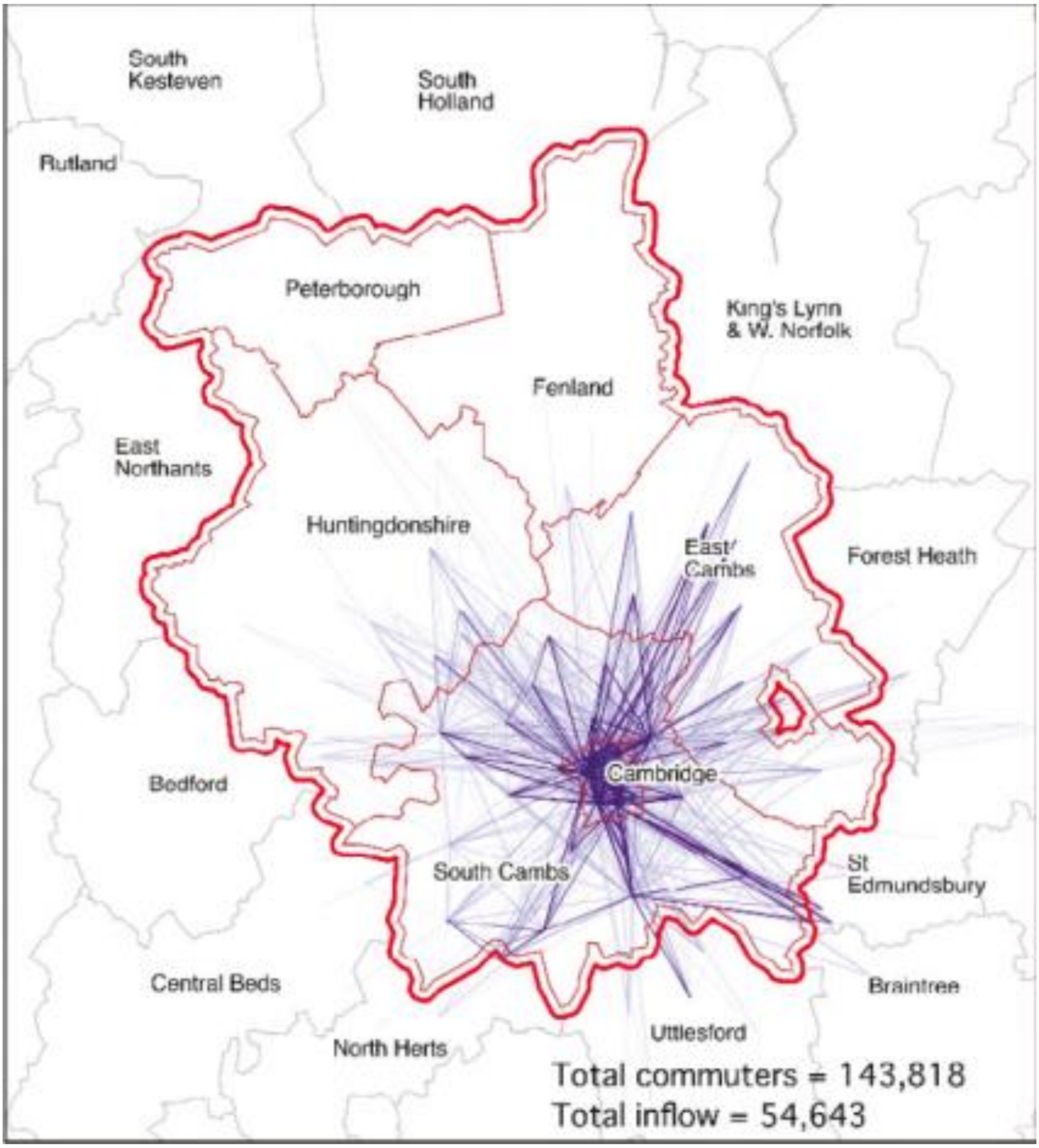


Delivery

APPENDIX 5: INVESTMENT AREA

Investment Target Area

The investment target area outside of the Local Plan boundary follows the definition of the Greater Cambridge commuting pattern, as identified in the Cambridgeshire and Peterborough Independent Economic Review (September 2018):



APPENDIX 6: STREAM 2 AND 3 BUSINESS CASE OUTLINE

The business case will include the following as a minimum:

Reasons - Why is the investment needed?

Options - What are the options available?

Benefits - What would be the benefits of the investment? How would it help deliver the Business Plan objectives?

Investment Appraisal - A detailed financial appraisal setting out the projected income and costs associated with a potential acquisition along with an assessment of the proposed financing options and associated risks and considerations.

Risk Management Assessment - A detailed risk assessment of the potential investment, including mitigation measures that can be employed:

- Specific risks associated with the proposed investment:
- Risk of failure (sales / letting void risks)
- Costs of ownership and management
- Differing ownership structures (e.g. wholly owned subsidiaries).
- Sector risk (portfolio spread)
- Provide an exit strategy financial assessment as a 'worse case' scenario
- Liquidity assessment
- LTV ratio assessment

Market Risks, including risks of structural change or market failure, which may affect the market as a whole or particular subsectors or groups of property:

- Illiquidity upon sale (e.g. lot size, transaction times, availability of finance)
- Failure to meet market value expectations (forecast value growth)
- Failure to meet market yield expectations (forecast yield shift)
- Risk of locational, economic, physical and functional depreciation through structural change
- Risks associated with legislative change (e.g. planning or changes in fiscal policy)

Portfolio Assessment - An assessment to establish suitability against the Council's existing property portfolio which will consider rental levels, location, property type, rent review and lease expiry patterns, industry sector, tenure, lease covenants, market exit constraints and physical and environmental factors.

Legal

- Report on title (to confirm ownership)
- Options for legal structures (e.g. use of wholly owned subsidiaries)
- Advice on SDLT and VAT linked to use of legal structure options

Estimated Timescale

- Proposed start date
- Estimated end date
- Duration

Estimated project resources

- Identify role and name of officers
- Estimate the demand on officer time
- Identify resource gaps and whether these can be met
- Identify external resources required and estimated budget cost

APPENDIX B

INVESTMENT STRATEGY – SUMMARY OF KEY REVISIONS

ISSUE	OPTIONS	ACTION
1) Publication of Investment Strategy. Currently this is difficult to find on the website. A list of council policies and strategies would aid transparency.	Improve accessibility on the Councils website	**Note** that Head of Commercial Development & Investment is currently working with the Comms team to present the Strategy on a separate and fully accessible version on the website
2) Loans to 3rd parties. IGB should consider that any loans made to 3rd parties (i.e. Ice Rink) should be explained within the Investment Strategy, and not within other Capital Strategies. The rates of return on such loans need to be explained.	Amend Investment Strategy to include loans to 3rd parties within 'stream 2' investments	**Agree** to modify the Investment Strategy within the *Acquisition / Development methodology* section to include: <u>*investments via loans to 3rd parties*</u> as an area of activity within stream 2
3) Fair value assessment. Should IGB consider requiring this to be done as part of the annual strategy / review for inclusion within the MTFS?	To require the IST to undertake an annual Fair Value assessment of the portfolio of investments made through the Investment Strategy	**No action needed**. Paragraph 8.2.4 of the Investment Strategy states that: *Each year the Council will assess whether assets purchased via the Strategy retain sufficient value to provide security of investment using the fair value model in International Accounting Standard 40: Investment Property. If the fair value of assets is not sufficient to provide security for the capital investment the Strategy will provide detail of the mitigating actions that are being taken, or are proposed to be taken, to protect capital investment*
4) Dependency on yield bearing investment to fund NSE. Investment Strategy should set out extent of dependency and contingency plans if expected yields are not realised. IGB should consider the requirement for each investment proposal to provide an exit strategy financial assessment as a 'worse case' scenario, in order that members can appreciate the level of risk associated with each investment.	To require the IST to include an exit strategy financial assessment within each investment business case for the worst case scenario	**Agree** to modify the Investment Strategy under APPENDIX 1 (1b) - Stream 1 Business Case item c) Risk Management Assessment, and APPENDIX 6 Stream 2 & 3 Business Case outline, under Risk Management Assessment to include the wording: <u>*provide an exit strategy financial assessment as a 'worse case' scenario*</u>

ISSUE	OPTIONS	ACTION
5) Liquidity. What procedures exist to ensure funds can be accessed when they are needed? What is the liquidity associated with each asset class?	To require the IST to assess the liquidity of each investment and to maintain a register of the same in the Asset Management Plan for the investment portfolio	**Agree** to modify the Investment Strategy to include the wording: *liquidity assessment* under APPENDIX 1 (1b) - Stream 1 Business Case item c) Risk Management Assessment, and APPENDIX 6 Stream 2 & 3 Business Case outline, under Risk Management Assessment **Agree** to require the IST to provide a *liquidity assessment* when undertaking the annual Fair Value Assessment (as described in paragraph 8.2.4 of the Investment Strategy)
6) Use of cash as opposed to borrowing. The Investment Strategy assumes all investments would be made through PWLB borrowing, however as the Council has cash available. The indicator Debt:NSE (Net Service Expenditure) only records the amount borrowed. MHCLG guidance requires that the Investment Strategy needs to cover all assets not being used to deliver council services (i.e. cash as well as borrowing). Is a separate indicator required to record use of cash, or should the existing indicator be modified?	a) to modify the existing indicator to include cash and debt within the Debt:NSE indicator (i.e. £20m per annum including cash and debt financing) b) to add an additional indicator determining the amount of cash that can be invested each year (as a proportion of Net Service Expenditure)	**Agree** to modify the Investment Strategy to include cash within the Debt:NSE ratio by adding the words *(as cash or loan financing)* after the words 'gross debt' in paragraph 8.2.1 Debt to Net Service Expenditure (NSE) Ratio, **OR** **Agree** to *create an additional indicator* after paragraph 8.2.1 of the Investment Strategy to measure the amount of cash associated with Commercial Property Investments
7) b. Debt:NSE ratio. IGB should consider whether the limits set are reasonable, given the Council's business plan objectives and the growth agenda generally across the District. Consideration should be given as to whether the Council should target specific investment limits for each stream. Note that Investment Partnerships (Stream 3) could deliver schemes up to a total investment value of £340m over 4 years (£85m per annum), but that these investment swill also deliver capital returns at the completion of the developments when the properties are sold.	To modify to the level of investment from a fixed £20m per annum to a range from £20m up to £120m per annum.	**Agree** to modify the level of investment (as expressed through the Debt:NSE ratio and any additional cash indicators) from a fixed £20m per annum to a range from £20m to £120m per annum

ISSUE	OPTIONS	ACTION
8) Income:NSE ratio. IGB should consider refining this to reflect the different levels of financial return that each investment stream can deliver	a) Stream 1 - generally 5% minimum yield – what is the target level of income form this stream? b) Stream 2– Investment Strategy states minimum level return of 2.5% - what level of investment is the target? c) Stream 3 – could require significant levels of investment (exceeding current Debt:NSE limits) but will deliver capital receipts rather than annual revenue stream over the long term.	**Agree** target yield for Stream 1 investments at least 5% **Agree** target yield for stream 2 investment at least 2.5% **Agree** each project within stream 3 to be individually assessed with a minimum yield required of 5%
9) LTV ratio. Is it appropriate to have a fixed indicator for each year, given that cash inflows and outflows (especially from stream 3) will fluctuate within year? Should IGB consider setting an LTV limit no lower than 2.0 as a prudent indicator, including the requirement to calculate LTV of all investments within the Investment Strategy portfolio prior to any investment decision being made (as values can go down within year as well as up).	To modify the LTV ratio to require limit of 2.0 and require the ratio to be assessed prior to any investment being made when preparing the business case	**Agree** to modify the Investment Strategy to include the wording: *LTV ratio assessment* under APPENDIX 1 (1b) - Stream 1 Business Case item c) Risk Management Assessment, and APPENDIX 6 Stream 2 & 3 Business Case outline, under Risk Management Assessment
10) Consideration should be given as to a statement of how net revenue is calculated	Annual Net Revenue = Income – acquisition costs - operational costs – loan interest (or where cash is used, the loss of interest), divided by the Total amount invested	**Agree** to require the IST to agree the formula to calculate net revenue for each investment, and report this to IGB meetings within the Asset Management update
11) Gross and net income and Operating Costs. IGB should consider requiring the Investment Strategy to provide further detail of the operational costs. Going forward each year the Investment Strategy should provide out-turn costs and revenues compared against budgets set the previous year	Operational costs to include staff time and the following: i. Repairs, ii. Sinking fund, iii. Running costs (other than those recoverable from tenant) iv. Business rates (if not recoverable for tenants) v. Voids vi. Finance costs vii. Asset management costs, including: insurance; inspections; surveys; lease events; invoicing and arrears management; covenant enforcement, and service charge management.	**Agree** to amend the indicator at para 8.2.2. of the Investment Strategy (Commercial Income to NSE Ratio) to include all operational costs, thereby reporting the net income from investments

ISSUE	OPTIONS	ACTION
12) Vacancy levels. Currently set at zero, but what are acceptable parameters for ongoing portfolio management? What allowance should be made of void periods and capital expenditure during investment lifecycle? Is there an asset / portfolio management plan in place and who is responsible for this?	To include an allowance for voids or not	**Agree** to include an allowance for voids based on the anticipated 25 year cash flow for each investment and include the void costs within the Commercial Income to NSE ratio above
13) Strengthen the Strategy to ensure that it covers all requirements of the CIPFA guidance and statutory guidance.	To review the coverage in relation to contribution, security, risk assessment, liquidity, proportionality and borrowing in advance of need.	Agree to include further clarification if the requirements in relation to contribution, security, risk assessment, liquidity, proportionality and borrowing in advance of need.
14) Clarify governance arrangements, including arrangements for the approval of priority investments	To make appropriate amendments to the Investment Strategy to confirm the role of Council in capital funding allocations and the profiling of expenditure. To make appropriate amendments to the Scheme of Delegations to enable Officers to progress investment opportunities, including undertaking essential due diligence checks and the submission of non-binding offers in line with market practice.	Agree to clarify governance arrangements in the Investment Strategy, including amendments to the Scheme of Delegations to Officers.

South Cambridgeshire
District Council