Capital and Investment Strategy 2024/25 to 2026/27

This strategy document is presented in three sections and requires approval by the County Council.

- **Section A: Capital Strategy**

  This gives a high-level overview of how capital expenditure, capital financing, treasury management and investment activity contribute to the provision of local public services. It also provides an overview of how associated risk is managed and the implications for future financial sustainability.

- **Section B: Minimum Revenue Provision (MRP) Statement**

  This is a statement that the County Council is required to prepare and approve each year setting out its policy on making MRP for the repayment of borrowing in respect of the upcoming financial year. The statement sets out how the County Council proposes to discharge its duty to make prudent MRP charges to the revenue budget.

- **Section C: Non-treasury Investment Strategy**

  This focuses on investments that are not made for treasury management purposes and supports transparent reporting and democratic accountability for any such non-treasury investments.

The requirement for this strategy document stems from the:

- Local Government Act 2003, Section 15(1)
- Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 [SI 3146]

As a result, the Authority is required to have regard to:

- MHCLG Statutory Guidance on Local Government Investments
- MHCLG Statutory Guidance on Minimum Revenue Provision (MRP)
- CIPFA's Prudential Code (last updated 2021)
- CIPFA's Treasury Management Code (last updated 2021)

Where a local authority prepares a Capital Strategy in line with the requirements of the Prudential Code, and a Treasury Management Strategy (TMS) in line with the requirements of the Treasury Management Code, the Investment Strategy can be published in those documents instead of as a separate document. The County Council includes its non-treasury management Investment Strategy with the Capital Strategy. The TMS is a separate document and includes the investment strategy for treasury management investments.

Section A: Capital Strategy

1. Introduction

1.1 This Strategy gives a high-level overview of how capital expenditure, capital financing, treasury management and investment activity contribute to the provision of local public services. It also provides an overview of how associated risk is managed and the implications for future financial sustainability.

2. Governance arrangements for capital investment

2.1 The County Council's Medium Term Financial Strategy (MTFS) ensures that it continues to invest appropriately in its existing assets and to deliver a programme of new ones in line with overall priorities, need and affordability. This is kept under review by the Corporate Management Team and reported through Cabinet for approval by the County Council. The MTFS is closely linked to the 'Serving Hampshire – Strategic Plan 2021 – 2025' the Hampshire 2050 Vision and directorate service plans.

2.2 Risk management is an integral part of determining and delivering a capital programme. Given the impact of high inflation alongside wider economic uncertainty within the UK, in planning and monitoring the capital programme and MTFS, the County Council has introduced additional measures to mitigate risk. This includes additional detailed analysis of financial exposure for projects most sensitive to price uncertainty. The County Council also created a capital inflation risk reserve in 2022.

2.3 In accordance with the MTFS, each year the Cabinet sets cash limit guidelines for a three-year capital programme funded by local resources. The current MTFS assumes continuing revenue contributions to capital schemes throughout the forecast period. In order to allow the County Council time to continue to consider the evolving MTFS position, the capital cash limit guidelines approved by Cabinet in December 2023 only allocated the funding from these revenue based contributions to directorates for 2024/25, with the amounts for 2025/26 and 2026/27 to be held centrally pending further review.

2.4 Executive Members propose capital programmes within these cash limits together with schemes funded by government grants and other external sources. The proposed programmes are scrutinised by the relevant Select Committee. The final Capital Programme is then presented to Cabinet and to County Council in February each year as part of the formal budget approval. Once a defined scheme has been included in the approved capital programme, approval to spend must be granted either by the relevant Chief Officer in consultation with the Executive Member for schemes up to £500,000 or by the Executive Member for schemes of higher values, in line with the County Council's financial regulations.

2.5 Before a major capital project can be committed, the relevant Chief Officer must ensure it has undergone an appropriate project appraisal. This appraisal should be proportionate to scheme value and complexity including the options considered, appropriate financial analysis of capital and revenue implications, and conclusions setting out why the option proposed is the best use of available resources.

2.6 The County Council utilises two decision-making tools to assess the carbon emissions and resilience of its projects and decisions. These tools provide a clear, robust, and transparent way of assessing how projects, policies and initiatives contribute towards the County Council's climate change targets of being carbon neutral and resilient to the impacts of a 2℃ temperature rise by 2050. This process ensures that climate change considerations are built into everything the Authority does.

3. Capital expenditure, capital financing and asset management

3.1 Capital expenditure is spending by the County Council on assets, such as land, property, the highway network, or vehicles, that will be used for more than one year. In local government this includes relevant spending on assets owned by other bodies, and loans and grants to other bodies enabling them to buy or enhance assets.

3.2 The County Council considers estimates for the timing of capital expenditure and the availability of financial resources when determining the capital programme.

3.3 There are a number of ways that capital expenditure can be funded:

- A large proportion of the programme is typically funded from **external sources**, predominantly capital grants and contributions from the Government and other bodies, including developers.
- **Capital receipts** secured through the sale of assets owned by the County Council are also used to fund expenditure, although capital receipts can vary significantly from year to year and each asset can only be sold once.
- The remaining expenditure is funded through the County Council's own **local resources**, comprising prudential borrowing, contributions from the revenue budget, and the use of reserves. **Reserves** can only be spent once, and **prudential borrowing** creates a future pressure on the revenue budget through interest and repayment of principal (Minimum Revenue Provision) costs. Similarly, pressures on the revenue budget limit the extent to which **planned revenue contributions** can be used as a source of funding.

Capital expenditure

3.4 Table 1 provides details of the County Council's capital programme. As parts of the capital programme are managed on a 'starts' basis, the programme years do not fully reflect when capital expenditure is expected to take place. This is therefore shown separately in the second half of the table and is one of the required Prudential Indicators.

3.5 Some of the most significant areas in which the County Council is investing in its assets include:

- investment to safeguard the long-term viability of the Older Adult care estate
- the investment in new and extended school buildings to ensure there is a school place for every child in Hampshire
- structural maintenance and improvement of roads and bridges;
- Integrated Transport Plan schemes including schemes specifically focused on walking and cycling improvements
- condition improvements to the schools' estate

Table 1 – Capital programme

Prior years starts*		**Revised 2023/24**	**2024/25**	**2025/26**	**2026/27**	**Total**
£'000		**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
20,260	Adults' Health & Care	49,154	187,733	14,252	14,252	285,651
15,282	Children's Services	47,332	121,056	80,338	41,208	305,206
2,997	Hampshire 2050	4,445	62,990	100	1,776	72,308
250,837	Universal Services	207,077	137,547	107,583	84,467	787,511
0	Centrally held	0	0	13,669	13,669	27,338
289,376	**Total**	**307,998**	**509,326**	**215,942**	**155,372**	**1,478,014**

** schemes started in prior years that have not yet completed*

880,640

Forecast timing of capital expenditure flows (Prudential Indicator 1)

	2023/24	2024/25	2025/26	2026/27	Future years	Total
	£'000	£'000	£'000	£'000	£'000	£'000
Expenditure	247,672	331,401	319,049	349,924	229,968	1,478,014

3.6 Further details can be found in the February 2024 Capital Programme Report.

Capital financing

3.7 All capital expenditure must be financed, either from external sources, the Authority's own resources, or debt. Debt is only a temporary source of funding and is replaced over time by other financing, usually from revenue through annual Minimum Revenue Provision (MRP) charges. External debt will also incur interest costs. The County Council's borrowing strategy is summarised in Section 6 and forms part of its Treasury Management Strategy.

3.8 The resources to fund the capital expenditure flows set out in Table 1 are shown in Table 2.

Table 2 – capital financing

	2023/24	2024/25	2025/26	2026/27	Future
	£'000	£'000	£'000	£'000	£'000
Prudential borrowing	19,305	28,514	56,467	139,966	103,143
less repayments from capital	(6,422)	(21,418)	(8,929)	(23,072)	(58,731)
Capital grants	130,818	159,513	141,216	132,853	94,731
Contributions from other bodies*	61,944	75,174	83,857	53,647	47,437
Capital receipts	465	19,316	810	24,030	6,982
Revenue contributions to capital	17,847	14,677	14,322	14,380	30,705
Use of the capital reserve	21,984	53,925	30,206	8,120	5,701
Use of revenue reserves	1,731	1,700	1,100	0	0
Total planned use of resources	**247,672**	**331,401**	**319,049**	**349,924**	**229,968**

** including developers*

Asset management and disposals

3.9 The 5-year Strategic Asset Management Plan (SAMP) for the **County Council's estate** was presented to Cabinet on 13 December 2022. This followed previous SAMPs published in 2011 and 2015.

3.10 The report sets out the context and drivers for the SAMP, its structure, and the key themes providing direction to the management of the County Council's property assets through a set of strategic actions. The SAMP itself was included as an appendix to the report and is a key enabler of the County Council's corporate strategy to ensure that its large and diverse estate continues to meet corporate priorities and objectives, providing a strategic framework for decision making based on a clear set of principles and mechanisms through which the future use of land and property assets will be considered, together with a high-level action plan to enable the effective management and re-shaping of the estate.

3.11 The SAMP sets out the vision to achieve the optimal financial return and commercial opportunities from the rationalisation and disposal of surplus land and buildings. The plan includes the objective to rationalise the operational estate, achieving reduction through co-location, new ways of working and maintenance optimisation, with an action plan for disposals to:

- Promote appropriate land assets as strategic development sites
- Identify and dispose of strategic sites where multiple benefits can be achieved
- Rationalise and reduce the overall size of the County Council's built estate, starting with office accommodation.

3.12 The County Council also applies asset management principles in relation to its **infrastructure assets** in developing a needs based programme of structural maintenance for its highways assets, developed based on various factors including condition, remaining life and lifecycle planning including whole life costs.

Capital receipts

3.13 The County Council's capital programme is supported by the appropriate use of capital receipts. These receipts vary from year to year, for example in 2021/22 they accounted for about 5% of the funding applied to capital expenditure, rising to 12.5% in 2022/23.

3.14 Capital receipts are generated when a capital asset is identified as surplus to requirements and is then sold. The proceeds from these asset sales may be used to fund new capital assets or to repay debt. The repayment of capital grants, loans and investments will also count as capital receipts, with the same restrictions on future use of the proceeds.

3.15 Capital receipts are fully retained to fund corporately agreed priorities, except where an appropriate business case for alternative use is agreed in advance.

4. Prudence and affordability

4.1 The County Council is required to ensure that capital expenditure, investment and borrowing decisions are prudent, sustainable and affordable. There are a number of prudential indicators that must be set and monitored to help with this requirement, which are set out in the Prudential Code. Actual figures for the prudential indicators at the end of each quarter will be included in regular reporting to Members. The prudential indicators cover:

- Capital expenditure (Tables 1 and 3)
- External debt (Tables 3 and 5)
- Affordability (Tables 6 and 7).

4.2 The Prudential Code sets out that certain acts and practices are not prudent activity for a local authority and incur risk to the affordability of local authority investment. The County Council will not therefore:

- Borrow to invest primarily for financial return
- Make investment or spending decisions that increase the Capital Financing Requirement (CFR) unless directly and primarily related to the functions of the authority (any financial returns should either be related to the financial viability of the project or incidental to the primary purpose).

Prudential borrowing

4.3 Capital financing costs associated with prudential borrowing must be financed by the County Council from its own resources. It is therefore important that the use of prudential borrowing is very closely controlled and monitored. The County Council will only use prudential borrowing where there is a clear financial case to support doing so, although it will not borrow to invest primarily for financial return and therefore retains full access to the Public Works Loan Board (PWLB).

4.4 The County Council operates within a framework for the use of prudential borrowing,. This includes:

- Borrowing for which loan charges are financed by virement from the Executive Member’s revenue budget, including invest-to-save schemes that will generate revenue savings or additional revenue income.

- 'Bridging' finance that will be repaid by eventual capital receipts, capital grants or contributions, provided that the cost of interest and the statutory minimum revenue provision is met by services in the years that such costs are incurred.
- Capital investment by business units, to be funded by business unit reserves.
- Temporary borrowing to accommodate shortfalls in general capital resources.

Ensuring borrowing is only for capital purposes

4.5 The Capital Financing Requirement (CFR) is the cumulative outstanding amount of debt finance. The CFR increases with new debt-funded capital expenditure and reduces through annual Minimum Revenue Provision (MRP) charges to the revenue budget and any capital receipts or other contributions used to replace debt.

4.6 The Prudential Code states that a local authority must ensure that gross debt is only for capital purposes over the medium term, which means that gross external debt must not exceed the total of the CFR from the preceding year plus the estimates of any additional CFR for the current and next two financial years, except in the short term. This is a key indicator of prudence and is shown in Table 3.

Table 3: Ensuring Borrowing is Only for Capital Purposes (Prudential Indicator 2)

	31/03/24 Revised £M	31/03/25 Estimate £M	31/03/26 Estimate £M	31/03/27 Estimate £M
CFR	**731**	**721**	**735**	**819**
Debt				
Borrowing	222	212	213	193
PFI Liabilities	113	104	95	85
Leases		15	13	12
Total Debt	**335**	**331**	**321**	**290**

4.7 Total debt is expected to remain below the CFR during the forecast period. External debt is expected to remain below the CFR because of the County Council's borrowing strategy, whereby it has used internal borrowing (the temporary use of internal cash balances) to fund capital expenditure in place of borrowing money from external sources. Further details are in the Treasury Management Strategy.

Affordable borrowing limit

4.8 The County Council is legally obliged to set an Authorised Limit for the maximum affordable amount of external debt. In line with statutory guidance, a lower 'Operational Boundary' is also set as a warning level should debt approach the limit. The Operational Boundary is based on the County Council's estimate of the most likely (i.e. prudent but not worst case) scenario for external debt. It links directly to the County Council's estimates of capital expenditure, the CFR and cash flow requirements, and is a key management tool for in-year monitoring.

Table 4: Affordable Borrowing Limits (Prudential Indicators 3 and 4)

	2023/24 Revised £M	2024/25 Estimate £M	2025/26 Estimate £M	2026/27 Estimate £M
Authorised Limit:				
Borrowing	780	760	790	880
PFI and Leases	150	150	140	130
Authorised Limit	**930**	**910**	**930**	**1,010**
Operational boundary:				
Borrowing	700	680	710	800
PFI and Leases	120	120	110	100
Operational Boundary	**820**	**800**	**820**	**900**

Affordability of financing costs

4.9 Capital expenditure is not charged directly to the revenue budget, however the interest payable on loans and the annual MRP are charged to revenue, as are other financing costs. The impact of these costs needs to be well understood prior to making capital investment decisions and then closely monitored.

4.10 Table 5 shows the proportion of the County Council's net revenue stream (Council Tax, business rates and general government grants) required to meet financing costs. This is an indicator of the affordability of the County Council's capital programme.

Table 5: Ratio of Capital Financing Costs to Net Revenue Stream (Prudential Indicator 5)

	2023/24 Revised	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate
Ratio	5.2%	4.8%	4.5%	4.6%

4.11 A low proportion is forecast, demonstrating that the cost of financing is minimised and the proportion of the revenue budget available for delivering services is maximised.

Reliance on income from commercial and service investments

4.12 The update to the Prudential Code in 2021 introduced a new prudential indicator intended to show how reliant a local authority is on income from commercial and service investments, and therefore how exposed the authority is to the loss of this income. Table 6 compares the income from these investments with the net revenue stream (Council Tax, business rates and general government grants) and demonstrates the County Council does not place a significant reliance on this income to balance its revenue budget.

Table 6: Net Income from Commercial and Service Investments to Net Revenue Stream (Prudential Indicator 6)

	2023/24 Revised	2024/25 Estimate	2025/26 Estimate	2026/27 Estimate
Ratio	0.2%	0.2%	0.3%	0.3%

5. Treasury Management

5.1 The Treasury Management Strategy Statement (TMSS) supports the Capital and Investment Strategy in setting out the arrangements for the management of the County Council's cash flows, borrowing and investments, and the associated risks.

5.2 The County Council has potentially large exposures to financial risks through its investment and borrowing activity, including the loss of invested funds and the effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to the Council's Treasury Management Strategy (TMS).

5.3 The County Council's TMS, included as Appendix 8 to this report, is scrutinised by the Audit Committee and approved by the County Council each year. Actual performance is reviewed by the Audit Committee and reported to Cabinet and County Council.

Treasury management borrowing strategy

5.4 The County Council's chief objective when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving certainty of those costs over the period for which funds are required. The flexibility to renegotiate loans, should the County Council's long-term plans change, is a secondary objective.

5.5 The County Council expects to continue its approach of internally borrowing instead of taking on additional external borrowing with the aim of reducing both net costs and overall treasury risk. Arlingclose assist the County Council in regularly monitoring this approach.

Treasury management investment strategy

5.6 The CIPFA Code requires the County Council to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The County Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income. The County Council aims to be a responsible investor and will consider environmental, social and governance (ESG) issues when investing.

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

5.8 The County Council's actual and forecast treasury management investment balances are shown in Table 7 with further detail in the TMS. The large reduction in total balances in the year to 31/3/24 is related to the County Council paying its Local Government Pension Scheme employer pension contributions in advance for the 3 year period from April 2023.

Table 7 – Treasury Management Investments

	31/3/23 actual £m	31/3/24 forecast £m	31/3/25 forecast £m	31/3/26 forecast £m
Short term investments	501	69	74	60
Long term investments	225	239	103	20
Thames Basin Heaths pooled fund investments	14	15	15	15
Total**	**740**	**323***	**192***	**95**

*reduction in investments reflects the decision to pre-pay employer pension contributions for three years on 1 April 2023 as well as the forecast reduction to reserves and the impact of the increasing DSG deficit.

Pooled fund investments

5.9 The County Council holds reserves for a number of purposes, which are explained in more detail in the Reserves Strategy (Appendix 5). In previous years the County Council earmarked an amount of its cash balances for investments targeting higher yields; these were made from its most stable core balances with the intention that they would be held for at least the medium term, and it was targeted that these investments would achieve a return of at least 4%. This was a successful approach through the period of very low interest rates, as this portfolio achieved higher percentage income returns that was being achieved by cash investments and significantly increased the annualised average income return for the total investment portfolio.

5.10 Following the increases in UK Bank Rate there is no longer a significant difference between the interest rates being achieved by these investments and cash. The County Council will however continue to make use of long-term balances by making investments to mitigate the risk of low interest rates if the UK Bank Rate reduces in the future as expected.

5.11 The County Council continues to invest in pooled funds, although this allocation has been reduced over the last 12 months, as well as other long-term investments. Diversification helps to mitigate the risk of overexposure to a single event affecting a specific asset class.

5.12 Pooled funds allow the County Council to invest in a diversified ‘basket’ of individual investments and to benefit from the expertise of specialist external investment managers rather than having to employ its own specialists. Pooled fund investments do however present a number of risks which must be carefully managed, including the risk of loss of capital, illiquidity, entry and exit fees, and volatility of returns. The selection of pooled funds is carefully managed to target funds with a strong performance track record and objectives that are well aligned to the County Council’s income return aims without putting its initial investment at undue risk over the longer term. Arlingclose supports the County Council in regularly reviewing the ongoing suitability of these investments.

5.13 At the current time, given the medium to long term nature of the investments, it is unlikely that a capital loss would ever be realised as the County Council would avoid selling investments that realised a capital loss.

5.14 The County Council is aware of the risks involved with investing in pooled funds and has an Investment Risk Reserve in place to mitigate the risk of an irrecoverable fall in the value of these investments. The balance held in this reserve is currently £10.15m. This helps to mitigate the risk of crystalising a loss on investments (although the medium to long term nature of these investments reduces this likelihood of selling at a loss) and risks related to the IFRS 9 statutory override.

6. Knowledge and skills

6.1 The County Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions in accordance with the approved strategies. This includes the Chief Executive, Director of Corporate Operations (S151 officer) and Deputy Director of Corporate Operations (Deputy S151 officer) all being longstanding members of the Chartered Institute of Public Finance and Accountancy (CIPFA). Performance against targets and learning and development needs are assessed annually as part of the staff appraisal process across the County Council, and additionally when the responsibilities of individual members of staff change.

6.2 Staff attend training courses, seminars and conferences provided by CIPFA, Arlingclose and other providers. Relevant staff are also encouraged to study professional qualifications from CIPFA, and other appropriate organisations.

6.3 CIPFA's Code of Practice requires that the County Council ensures that all members tasked with treasury management responsibilities, including scrutiny of the treasury management function, receive appropriate training relevant to their needs and understand fully their roles and responsibilities. All Members were invited to a workshop presented by Arlingclose in November 2023, which gave an update of treasury matters. A further Arlingclose workshop is planned for 2024.

Investment Advisers

6.4 The County Council has appointed Arlingclose Limited as treasury management advisers and receives specific advice on investment, debt and capital finance issues. The quality of this service is controlled through quarterly review meetings with the Director of Corporate Operations, their staff, and Arlingclose.

7. Chief Financial Officers Conclusion on the Affordability and Risk Associated with the Capital and Investment Strategy

7.1 This Capital and Investment Strategy has been developed alongside the TMS (Appendix 8) and the Reserves Strategy (Appendix 5). Together, they form an integrated approach adopted by the County Council to balance the need for capital investment to support service priorities with consideration of affordability and the consequent impact on the revenue budget, whilst recognising and managing risk to an acceptable level.

7.2 The forward planning of capital investment and its funding, including being in a position to maximise the use of external grants, contributions and capital receipts, together with the process of regular monitoring of actual income, expenditure, and project progress, provides assurance to the Director of Corporate Operations that the proposed Capital Programme is prudent, affordable and sustainable.

Section B: Minimum Revenue Provision Statement

8. Minimum Revenue Provision (MRP) Statement

8.1 Where the County Council finances capital expenditure by debt, statutory guidance requires it to put aside revenue resources to repay that debt in later years, known as MRP. There are four options provided by the MHCLG guidance on MRP, however other options may also be considered:

- Option 1: Regulatory Method
- Option 2: CFR Method (4% of the CFR)
- Option 3: Asset Life Method
- Option 4: Depreciation Method

8.2 **Supported borrowing:** Prior to 2015/16 the County Council calculated MRP for supported borrowing[1] on a 4% reducing balance basis (Option 2). It was agreed by Cabinet in December 2015 that the calculation of MRP from 2015/16 onwards would change to a straight-line basis over 50 years. This is Option 3 from the range provided by the guidance. To be more prudent the 50 years was assumed to have started from 2008, however had the County Council been applying the new policy of a 50-year straight line calculation starting in 2008 it would have made £67m less in MRP payments by 31 March 2016. As agreed in 2016/17 the County Council paused making MRP payments on supported borrowing until it had realigned with the total amount of MRP payments under the new policy, which was during 2021/22 when payments recommenced. No new supported borrowing has occurred since 2013/14 and all MRP payments on pre-existing supported borrowing will cease by 2063/64 when the outstanding CFR balance is fully exhausted.

8.3 **Unsupported borrowing:** The County Council will continue to apply the Asset Life Method (Option 3) in respect of unsupported capital expenditure funded from borrowing. MRP will therefore be determined by charging the expenditure in equal annual instalments over an appropriate useful life for the asset.

8.4 **Private Finance Initiatives:** MRP in respect of leases and Private Finance Initiative (PFI) schemes brought on Balance Sheet under the International Financial Reporting Standards (IFRS) based Accounting Code of Practice will match the annual principal repayment for the associated deferred liability i.e. the element of rent or charge that goes to write down the balance sheet liability.

[1] Borrowing or use other forms of credit to finance capital expenditure, for which central government historically provided a revenue stream to support repayment of principal and interest. This support ended in the late 1990s.

8.5 **Leases:** The mandatory adoption of the new accounting standard for leases (IFRS 16) is April 2024. When the standard is introduced, it will mean that former operating leases will be brought onto the balance sheet on 1 April 2024. Where this is the case annual MRP charges will be set so that the total charge to revenue remains unaffected by the new accounting standard. For assets acquired by leases, MRP will be determined as being equal to the element of the rent or charge that goes to write down the balance sheet liability.

8.6 **Capital loans:** For capital expenditure loans to third parties, the County Council will make nil MRP and apply the capital receipts arising from principal repayments to reduce the capital financing requirement unless (a) the loan is an investment for commercial purposes and no repayment was received in year or (b) an expected credit loss was recognised or increased in-year. In years where there is no principal repayment on loans that are investments for commercial purposes, MRP will be charged in accordance with the MRP policy for the assets funded by the loan. Sufficient MRP will be charged to ensure that the outstanding capital financing requirement (CFR) on the loan is no higher than the principal amount outstanding less the expected credit loss. This option was proposed by the government in its recent MRP consultation and in the County Council's view is consistent with the current regulations.

8.7 **Commencement of MRP:** MRP is not charged until the year after the capital expenditure takes place, e.g. capital expenditure incurred during 2024/25 will not be subject to an MRP charge until 2025/26.

MRP forecast

8.8 Based on the Authority's latest estimate of its CFR on 31 March 2024, the budget for MRP has been set as follows:

Table 8: MRP Budget

	31/03/2024 Estimated CFR £M	**2024/25 Estimated MRP £M**
Supported Capital Expenditure	428	11
Unsupported Capital Expenditure After 31/03/2008	165	12
Leases and PFI	113	11
Transferred Debt	25	1
Loans to other bodies	0	0
Total General Fund	**731**	**34**

Section C: Non-treasury Investment Strategy

9. Non-treasury Investment Strategy

9.1. Government issued statutory guidance on local government investments in 2018 and requires an investment strategy to be produced, which may be included alongside the capital strategy and/or treasury management strategy.

9.2. The County Council could decide to invest its money for three broad purposes:

- Because it holds surplus cash in advance of need (treasury management)
- To support local public services (service investments)
- To generate a financial return (commercial investments)

9.3. Investments are categorised in accordance with the primary purpose of the investment. The majority of the County Council's investments are defined as **treasury management investments** and therefore summarised in Section 5 of this document and in more detail in the Treasury Management Strategy. The contribution that these investments make to the objectives of the County Council is to support effective treasury management activities.

9.4. This Non-treasury Investment Strategy therefore focuses on **service and commercial investments.**

Definitions

9.5. The Government guidance defines investments as "all of the financial assets of a local authority as well as other non-financial assets that the organisation holds primarily or partially to generate a profit; for example, investment property portfolios."

9.6. The County Council interprets this to exclude (a) trade receivables which meet the accounting definition of financial assets but are not investments in the everyday sense of the word and (b) property held partially to generate a profit but primarily for the provision of local public services. This aligns the Authority's definition of an investment with that in the 2021 edition of the CIPFA Prudential Code, a more recent piece of statutory guidance.

9.7. The Government guidance states that assets that generate revenue income solely through fees and charges for discretionary services levied under Section 93 of the Local Government Act 2003 should not be classified as non-financial investments for this purpose.

Commercial strategy

9.8. The County Council operates a Corporate Land and Assets Board at officer level to consider the strategic development of its estate including commercial opportunities. Opportunities for investment are reported to the appropriate Member meetings and, if additional capital schemes are proposed, approval is sought to add them to the Capital Programme in accordance with the County Council's Financial Regulations.

9.9. The County Council's commercial strategy was summarised in the Medium Term Financial Strategy (MTFS) update to Cabinet and County Council in the autumn of 2023.

9.10. The County Council's approach to commercialisation takes account of the need to manage and mitigate risk. This is achieved through the pursuit of a range of initiatives targeting increased income generation but without overexposing the Council to excessive risk or considering radical changes that take the County Council into areas that are not its core business, or indeed pursuing more niche opportunities that simply do not offer with any confidence anything like the scale of income to merit the effort and upfront investment. In the light of difficulties experienced by other authorities regarding commercial investments (notably in Thurrock, Slough, Croydon and Woking) the County Council's approach has been proven to appropriately manage risk whilst contributing to the financial strategy.

9.11. Delivery of the commercial strategy focuses on three core components:

a. Business activity – selling, trading or receiving in come for operational delivery of goods and services.

b. Investment activity – externally investing money and/or using strategic assets to generate financial returns as part of our place shaping activity, for example the strategic land programme.

c. Commercial operating model – developing our future operating model under key principles to be "more business like" in how we behave and operate.

9.12. A good example of this approach operating in practice is the proposed future direction of the Older Adults' service portfolio and supporting capital investment strategy approved by Cabinet in July 2023. In the light of concerns about the rate at which market prices are increasing, increases in service demand and acuity, and future forecasts regarding the number of older adults with advanced dementia, maintaining the strongest market presence possible was agreed as this would enable consistently improved occupancy, strong value for money, and far greater assurance regarding the delivery of financial savings/efficiencies.

9.13. Another example is the place-shaping Manydown project, where the County Council has a Joint Venture arrangement in place with Basingstoke and Deane Borough Council named Manydown Garden Communities (MGC) LLP. In July 2020, MGC LLP formed a Joint Venture partnership with the development partner Urban & Civic and the Wellcome Trust known as the Manydown Development Vehicle (MDV) LLP. The programme is about bringing forward sustainable new communities at Manydown in western Basingstoke, with the vision to *“create communities of connected neighbourhoods developed in a well-planned and coordinated way, combining the best features from Hampshire villages and towns with a contemporary design.”*

Investments for commercial purposes

9.14. Investments for commercial purposes are undertaken primarily for financial return but without being linked to treasury management activity or being part of service delivery. They are therefore additional investments taken voluntarily with the primary objective of generating a net financial return or profit. They will usually constitute capital expenditure. The income generated helps the County Council to deliver its service objectives.

9.15. The County Council has a small number of legacy arrangements that generate income from commercial tenants that would be considered commercial investments under the definitions of the Government guidance. It also holds a number of further assets classified as investment properties within its Balance Sheet.

9.16. All investment properties included within Table 9 are revalued on an annual basis at fair value based on market conditions. In accordance with government guidance, the County Council considers property investments to be secure where the accounting value is higher than the purchase cost including taxes and transaction costs. The most recent valuations are significantly higher than the purchase cost meaning the underlying assets provide security for the original capital investment.

9.17. These commercial investments generated around £1m of income in 2022/23 and therefore covered less than 0.1% of the gross expenditure of the County Council. The strategic land holdings are primarily not held to generate income but to generate future financial benefits and the County Council is not heavily reliant on income from its commercial investments to balance its revenue budget.

Table 9 – investment properties at 31/3/23	**Purchase cost**	**Gain/(loss) in fair value**	**Value in accounts at 31/3/22**
	£'000	**£'000**	**£'000**
Legacy arrangements generating income from commercial tenants	13,777	2,107	15,884
Legacy arrangements generating income from residential (secure) tenants	304	586	890
Legacy arrangements generating income from other legal agreements	165	107	272
Strategic land holdings	16,619	102,229	118,849
Total investment properties in accounts	**30,865**	**105,030**	**135,895**

The Strategic Asset Management Plan (covered in more detail in Section 3) was updated in 2022. The vision and objectives identified in the SAMP reflect the role that land and property assets can play in achieving the strategic priorities of the County Council. This includes enabling and contributing to economic regeneration and growth in Hampshire, in line with the Hampshire 2050 strategy, as well as enabling the further transformation of County Council services and maximising the financial return from assets in the context of the significant financial challenges the County Council faces to 2025 and beyond.

9.18. The SAMP identifies a desire to explore **commercial opportunities** from assets, including through acquisition, with a change in the organisational risk appetite and an agile approach, to achieve commercial advantage. Any activity that constitutes commercial investments will be considered and reported appropriately in accordance with the requirements of the Prudential Code and the Government investment guidance. This will include consideration of the contribution the investment will make to the County Council, the security of the amount invested, an assessment of the risks involved, and an understanding of the impact of the potentially illiquid nature of the assets involved.

Investments for service purposes

9.19. Investments for service purposes are those undertaken primarily and directly for the delivery of public services or in support of joint working with others to deliver such services. They will normally constitute capital expenditure and it may be appropriate to borrow to finance these investments. They may or may not deliver financial returns, but this will not be the primary purpose of the investment. The County Council holds a limited number of service investments.

9.20. **Manydown:** The County Council together with Basingstoke and Deane Borough Council (BDBC) each hold an equal leasehold interest in land at Manydown with the option to purchase that land for future development. To undertake this purchase jointly, the Councils set up and operate a separate company called Manydown Garden Communities LLP. Both Councils entered into a joint venture arrangement (Manydown Development Vehicle LLP) with a development company called Urban and Civic (U&C) and it is hoped that a deal with the freeholder, The Manydown Company, for the purchase of the land can be agreed in the near future. Under the contractual arrangements, the County Council has some financial obligations and had financial opportunities as part of the overall funding for the development. The council has already made some loans totalling £3.7m under approvals within its Treasury Management Strategy however, given the heightened scrutiny on local authority investments and companies, our treasury advisers have suggested that all of these items should now be treated as service-based loans to reflect the wider benefits that the County Council and BDBC are aiming to achieve in terms of economic development, regeneration, place shaping and affordable housing.

9.21. **Farnborough International Ltd:** With the primary aim of improving economic prosperity and related infrastructure within Hampshire, the County Council has granted loans totalling £4.5m at market rates of interest to Farnborough International Ltd.

9.22. **EM3 Local Enterprise Partnership:** The loan to Farnborough International Ltd is part of a total of £9.5m including £5m from the Enterprise M3 Local Enterprise Partnership (EM3 LEP), where the County Council is the accountable body. A further £7.15m of loans for other projects have also been granted by the EM3 LEP. From April 2024 the central government sponsorship and funding of LEPs will cease and instead the government will "*support local and combined authorities to take on the functions currently delivered by LEPs."* Any future investments pursued by the County Council in taking on the functions of the EM3 LEP are likely to meet the qualification criteria for service investments given the purpose of the functions carried out by the LEP.

9.23. **Revolving Community Energy Fund:** In May 2022, the County Council approved the creation of a £250,000 Revolving Community Energy Fund

(RCEF) from the Climate Change budget. This RCEF will invest in community energy projects with the primary objectives of helping to meet the County Council's climate change target and enabling the County Council to provide leadership and support to communities. Individual investments made through the RCEF will be of a value of up to £25,000 and will typically be made through direct investments in share offerings of small local entities. These investments will bring a greater degree of risk than the County Council would accept for treasury management investments, but it understands and accepts these risks given the way that these investments will help achieve the County Council's service objectives on climate change. Risk is mitigated by the RCEF being a very small proportion of the County Council's overall budget and by a defined due diligence process.

9.24. Accounting standards require local authorities to set aside loss allowances for loans, with a greater percentage loss allowance for loans with a greater chance of not being repaid. The loss allowances calculated are not material to the County Council.

9.25. The details of the County Council's service loans at the time of writing are set out in Table 10.

Table 10 – investments for service purposes	**Amount approved £'000**	**Amount invested £'000**	**Loss allowance £'000**	**Approved amount as % of net revenue stream**
Manydown (Loans)	53,700	3,700	40	5.0%
Farnborough International Ltd (Loan)	4,500	4,500	10	0.4%
Community energy projects through RCEF (Equity)	250	0	0	0.0%
On behalf of EM3 LEP (Loans)	12,153	12,153	224	1.1%
Total	70,603	20,525	274	6.6%

Investment indicators

In addition to setting Prudential Indicators required by the Prudential Code, the County Council has also set the following quantitative investment indicators in accordance with the requirements of the Government investment guidance. Note that this table does not include short term treasury management investments.

Table 11 – Total Investment Exposure (£m) and net rate of return (%)	31.03.2023 Actual		31.03.2024 Forecast		31.03.2025 Forecast	
	Invested £m	Return %	Invested £m	Return %	Invested £m	Return %
Treasury management (long term)	225	4.2%	239	4.0%	103	4.0%
Service investments (loans)	20	4.7%	18	6.5%	36	6.9%
Service investments (equity)	0.0	n/a	0	5.0%	0	5.0%
Commercial investments	31	3.4%	31	3.4%	31	3.4%
Total investments	275	4.1%	288	4.1%	170	4.5%

9.26. This shows that the County Council expects the majority of its investments to continue to be for treasury management purposes, although potential future investments related to Manydown would increase the proportion of service based loans.

9.27. The commercial investments will continue to be legacy arrangements and strategic land holdings and in the table are forecast to be unchanged, although this position may evolve as set out in the recent Strategic Asset Management Plan update. None of these investments are funded by borrowing.

9.28. Figures shown are the amounts invested not the current market value where these amounts vary.

9.29. The figures above exclude invested on behalf the Thames Basin Heaths Joint Strategic Partnership Board (£10.7m) where these investments are held on the County Council's balance sheet due to operational arrangements but where risks associated with these investments do not belong to the County Council.