Appendix 7

Denbighshire County Council

Capital Strategy Report 2019/20 to 2021/22

Contents

Capital Strategy Report 2019/20 to 2021/22

1 Introduction

1.1 This capital strategy is a new report for 2019/20, giving a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of local public services along with an overview of how associated risk is managed and the implications for future financial sustainability. It has been written in an accessible style to enhance members' understanding of these sometimes technical areas.

2 Capital Expenditure and Financing

2.1 Capital expenditure is where the Council spends money on assets, such as property or vehicles that will be used for more than one year. In local government this includes spending on assets owned by other bodies, and loans and grants to other bodies enabling them to buy assets.

In 2019/20, the Council is planning capital expenditure of £52.2m as summarised below:

Table 1: Prudential Indicator: Estimates of Capital Expenditure

Capital Expenditure	2018/19 Approved £000	2018/19 Revised £000	2019/20 Estimate £000	2020/21 Estimate £000	2021/22 Estimate £000
Council Fund	51,137	54,269	37,249	15,333	6,296
Corporate Plan	0	0	685	3,914	16,661
HRA	10,233	11,579	14,270	15,688	13,605
Total	**61,370**	**65,848**	**52,204**	**34,935**	**36,562**

2.2 For details of the capital projects please refer to Appendix 2-4 in the Capital Plan report. These give details of the capital plan by service, scheme estimates and major capital project updates.

2.3 The Housing Revenue Account (HRA) is a ring-fenced account which ensures that council housing does not subsidise, or is itself subsidised, by other local services. HRA capital expenditure is therefore recorded separately. Details of the Housing Capital Budgets can be found in the Housing Rent Setting and Housing Revenue and Capital Budgets Report to Cabinet on 22 January 2019.

2.4 **Governance**:

The Strategic Investment Group (SIG) provides an independent review of all business case proposals for capital investment regardless of value and has delegated authority to approve bids to the value of £1 million. It will also recommend schemes to either Cabinet or the full Council if the value of the Application is above £1m or if for other reasons, it is more appropriate for Cabinet or the full Council to approve.

Annually SIG invite bids from the Heads of Service and meet to review the bids and recommend the proposed allocation of the funding to Cabinet and Council. The recommendations for 2019/20 are included in Appendix 5 of the Capital Plan Report.

A Summary of the Council's Capital Plan is included in the monthly Finance Report to Cabinet. It shows the approved Capital Plan against spend to date. Also an update on the major projects is included in the overall Capital Plan.

2.5 All capital expenditure must be financed, either from external sources (government grants and other contributions), the Council's own resources (revenue, reserves and capital receipts) or debt (borrowing, leasing). The planned financing of the above expenditure is as follows:

Table 2: Capital Financing

Capital Financing	**2018/19 Approved £000**	**2018/19 Revised £000**	**2019/20 Estimate £000**	**2020/21 Estimate £000**	**2021/22 Estimate £000**
Council Fund					
Capital Receipts	648	4,911	330	0	0
Grants & Contributions	11,201	17,245	12,345	5,713	1,814
Revenue Contributions & Reserves	5,418	5,134	1,601	893	0
Supported Borrowing	6,388	953	7,314	2,982	2,982
Prudential Borrowing	27,482	26,026	15,659	5,745	1,500
	51,137	**54,269**	**37,249**	**15,333**	**6,296**
Corporate Plan 2					
Capital Receipts	0	0	0	0	0
Grants & Contributions	0	0	229	883	8,914
Revenue Contributions & Reserves	0	0	0	0	0
Supported Borrowing	0	0	0	0	0
Prudential Borrowing	0	0	456	3,031	7,747
	0	**0**	**685**	**3,914**	**16,661**
Total	**51,137**	**54,269**	**37,744**	**19,813**	**22,957**
HRA					
Capital Receipts	0	71	1,820	1,200	2,150
Grants & Contributions	2,409	2,412	2,412	2,412	2,412
Revenue Contributions & Reserves	2,050	2,395	1,944	809	405
Supported Borrowing	0	0	0	0	0
Prudential Borrowing	5,774	6,701	8,094	11,267	8,638
Total	**10,233**	**11,579**	**14,270**	**15,688**	**13,605**

2.6 Debt is only a temporary source of finance, since loans and leases must be repaid, and this is therefore replaced over time by other financing, usually from revenue which is known as Minimum Revenue Provision (MRP). Alternatively, proceeds from selling capital assets (known as capital receipts) may be used to replace debt finance. The Council's full MRP statement is included within the Treasury Management Strategy Statement (TMSS) 2019/20.

2.7 The Council's cumulative outstanding amount of debt finance is measured by the capital financing requirement (CFR). This increases with new debt-financed capital expenditure and reduces with MRP and capital receipts used to replace debt. The CFR is expected to increase by £20m during 2019/20. Based on the above figures for expenditure and financing, the Council's estimated CFR is as follows:

Table 3: Prudential Indicator: Estimates of Capital Financing Requirement

Capital Financing Requirement	31/03/19 Approved £000	31/03/19 Revised £000	31/03/20 Estimate £000	31/03/21 Estimate £000	31/03/22 Estimate £000
Council Fund	208,906	201,640	216,762	219,119	220,052
HRA	74,271	73,593	78,508	86,212	90,726
Total CFR	**283,177**	**275,233**	**295,270**	**305,331**	**310,778**

2.8 **Asset management:** To ensure that capital assets continue to be of long-term use, the Council has an asset management strategy in place. The Asset Management Group (AMG) meets quarterly and its purpose is to provide strategic direction for all matters relating to the effective use of Council owned land and building assets within the County, including (but not exclusively):

Land and Property disposal

Land and property acquisition

Strategic property planning (including consideration of Asset Management Plans)

Innovative land and property usage / utilisation.

2.9 **Asset disposals:** When a capital asset is no longer needed, it may be sold so that the proceeds, known as capital receipts, can be spent on new assets or to repay debt. The Council has received £2.394m of capital receipts in 2018/19 and has a programme of potential disposals which is reported to the Asset Management Group.

3 Treasury Management

3.1 Treasury management is concerned with keeping sufficient but not excessive cash available to meet the Council's spending needs, while managing the risks. Surplus cash is invested until required, while a shortage of cash will be met by borrowing, to avoid excessive credit balances or overdrafts in the bank current account. The Council is typically cash rich in the short-term as revenue income is received before it is spent, but cash poor in the long-term as capital expenditure is incurred before being financed. The revenue cash surpluses are offset against capital cash shortfalls to reduce overall borrowing.

3.2 Due to decisions taken in the past, the Council currently has £224.6m borrowing at an average interest rate of 4.25% and £19.6m treasury investments at an average rate of 0.5%.

3.3 **Borrowing strategy:** The Council's main objectives when borrowing are to achieve a low but certain cost of finance while retaining flexibility should plans change in future. These objectives are often conflicting, and the Council therefore seeks to strike a balance between cheap short-term loans (currently available at around 0.75%) and long-term fixed rate loans where the future cost is known but higher (currently 2.0 to 3.0%).

Projected levels of the Council's total outstanding debt are shown below, compared with the capital financing requirement (see above).

Table 4: Prudential Indicator: Gross Debt and the Capital Financing Requirement

Capital Financing Requirement	31/03/19 Approved £000	31/03/19 Revised £000	31/03/20 Estimate £000	31/03/21 Estimate £000	31/03/22 Estimate £000
CFR	283,177	275,233	295,270	305,331	310,778
Debt	220,802	223,135	248,763	258,172	265,371

3.4 Statutory guidance is that debt should remain below the capital financing requirement, except in the short-term. As can be seen from table 6, the Council expects to comply with this in the medium term.

3.5 **Affordable borrowing limit:** The Council is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt) each year and to keep it under review. In line with statutory guidance, a lower "operational boundary" is also set as a warning level should debt approach the limit.

Table 5: Prudential Indicators: Authorised Limit and Operational Boundary for External Debt

	2018/19 Approved £000	2018/19 Revised £000	2019/20 Proposed £000	2020/21 Proposed £000	2021/22 Proposed £000
Authorised Limit	250,000	250,000	295,000	300,000	300,000
Operational Boundary	245,000	245,000	290,000	295,000	295,000

Further details on borrowing are included in the treasury management strategy.

3.6 **Investment strategy:** Treasury investments arise from receiving cash before it is paid out again. Investments made for service reasons or for pure financial gain are not generally considered to be part of treasury management.

3.7 The Council's policy on treasury investments is to prioritise security and liquidity over yield that is to focus on minimising risk rather than maximising returns. Cash that is likely to be spent in the near term is invested securely, for example with the government, other local authorities or selected high-quality banks, to minimise the risk of loss.

Table 6: Treasury Management Investments

	31/03/18 Actual £000	31/03/19 Estimate £000	31/03/20 Estimate £000	31/03/21 Estimate £000	31/03/22 Estimate £000
Investments	12,600	5,000	5,000	5,000	5,000

Further details on treasury investments are included in the treasury management strategy.

3.8 **Governance:** Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Director of Finance and staff, who must act in line with the treasury management strategy approved by Council. Semi-annual reports on treasury management activity are presented to the Corporate Governance Committee. The Corporate Governance Committee is responsible for scrutinising treasury management decisions.

4 Revenue Budget Implications

4.1 Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP are charged to revenue, offset by any investment income receivable. The net annual charge is known as financing costs; this is compared to the net revenue stream i.e. the amount funded from Council Tax, business rates and general government grants.

Table 7: Prudential Indicator: Proportion of Financing Costs to Net Revenue Stream

Ratio of Financing Costs to Net Revenue Stream	2018/19 Approved £000	2018/19 Revised £000	2019/20 Estimate £000	2020/21 Estimate £000	2021/22 Estimate £000
Financing Costs	11,005	11,361	11,361	11,361	11,361
Net Revenue Stream	194,418	194,418	198,538	196,685	196,962
Council Fund Ratio	**5.66%**	**5.84%**	**5.72%**	**5.78%**	**5.77%**
Financing Costs	6,757	6,473	6,992	7,690	8,558
Net Revenue Stream	15,535	15,739	16,456	16,817	17,491
HRA Ratio	**43.50%**	**41.13%**	**42.49%**	**45.73%**	**48.93%**

4.2 **Sustainability:** Due to the very long-term nature of capital expenditure and financing, the revenue budget implications of expenditure incurred in the next few years will extend for up to 50 years into the future. The Head of Finance is satisfied that the proposed capital programme is prudent, affordable and sustainable.

5 Knowledge and Skills

5.1 The Council's approach to ensuring that the requisite knowledge and skills are held and demonstrated when making capital, borrowing and investment decisions is three fold.

- Employment of professionally qualified and experienced staff with responsibility for making decisions.
- Continuous and extensive training for Council members to aid informed decision making and effective scrutiny.
- Employment of Treasury Management advisors, Arlingclose to provide specialist advice in requisite areas.