Public
Key Decision – Yes

HUNTINGDONSHIRE DISTRICT COUNCIL

Title:	Commercial Investment Strategy: Business Plan
Meeting/Date:	Overview & Scrutiny Panel (Economic Well-Being) – 8th December 2015 Cabinet – 10th December 2015
Executive Portfolio:	Resources – Cllr Jonathan A Gray
Report by:	Head of Resources – Clive Mason
Ward(s) affected:	All Wards

Executive Summary:

The Government's austerity programme continues and the Council is aiming to still provide cost effective services to its local population. However, with the potential for increased cuts in Government funding, the Council is endeavouring to meet this challenge by undertaking a number of innovative approaches to service delivery. One of the key approaches to supporting Council services is the development of new sources of income generation and the introduction of the Commercial Investment Strategy (CIS) is such an approach. The CIS itself was approved in October 2015; it is now necessary to approve the CIS Business Plan (BP) (**Appendix 2**). Although the CIS covers a period of 9 years and has three distinct phases of development, the Business Plan being recommended here will be for Phase 1 and cover the period from now until the 31st March 2019.

The Council currently has existing investment assets (property) totalling £20.9m and it is proposing to invest a further £50.0m in commercial assets. The primary aim of the CIS is to generate a future income stream with a secondary objective of capital growth. After the payment of £2.2m in asset completion costs, the Councils total commercial asset portfolio at the end of the BP period will be £68.7m and split as follows:

Type 1: Existing Assets:	£20.9m
Type 2 and 3: Investment Fund and Property Shares:	£14.7m
Type 4: Direct Assets (Local Acquisitions):	£18.9m
Type 4: Direct Assets (National Acquisitions):	£14.2m

For the investments:

- up to the end of this financial year, it is proposed that these investments should not be financed from external borrowing, so a transfer is required from the Councils General Fund of £6.8m to the Capital Investment Earmarked Reserve. By making investments directly from in-house resources will mean that the Council can maximise returns and will not have to set-aside revenue funding in respect of the Minimum Revenue Provision.

- in subsequent years the Council will plan to externally borrow up to £35.0m. As the Council will be externally borrowing there will be the requirement to set-aside an amount for Minimum Revenue Provision (MRP); this will be equal to the annual loan repayment and a specific MRP policy is required (which will need to be approved by Council).

Where assets are being effectively managed, there will be occasions when assets will be sold and proceeds reinvested, it is proposed that capital receipts are ring-fenced in line with the Reserves Strategy (elsewhere on the agenda).

Recommendation(s):

That Cabinet approve the:

1. CIS Business Plan (**Appendix 2)**.
2. Transfer of £6.8m from the Councils General Fund balance to the Capital Investment Earmarked Reserve.
3. Potential to borrow up to £35.0m from 2016/17 onwards to support the CIS. However, there will still be “head-room” to borrow a further £25.0m if commercial opportunities arise.
4. MRP policy noted below and refer this to Council for approval:

   “For each capital investment undertaken under the requirements of the Councils Commercial Investment Strategy, Minimum Revenue Provision will be made that is equal to the principal repayment for any loan finance supporting the investment.”

1. WHAT IS THIS REPORT ABOUT?

1.1 The Council, along with all of local government, continues to face ongoing cuts in direct government grant as part of the government's austerity programme. However the pressure on services continues, and in some areas is increasing, so the Council is following a programme of service change to ensure that it is providing its services in the most cost-effective way possible.

1.2 Members will be aware that the Council is currently forecasting reductions of 37.6% by 2019/20, as detailed in the "Plan on a Page" (copy attached at **Appendix 1**). The "Plan on a Page" shows 6 strands that are being followed across the Council to assist in achieving the required budget reductions. One of these strands relates to "Income Generation" and a key constituent of this strand is the development of a Commercial Investment Strategy (CIS). The CIS itself was approved by Cabinet on the 17th September 2015 (Minute 35). What is now required is the approval of a Business Plan (BP) that will support the CIS.

2. BACKGROUND

2.1 Early in 2015 the Council started working with an external consultancy, EC Harris, in the development of the CIS, and then the BP. The CIS will incorporate the BP so the Strategy is one coherent document.

2.2 In the development of both the CIS and the BP, the Leader, Deputy Leader and the Executive Portfolio Holder for Resources have been consulted, including a meeting of the Treasury & Capital Management Group (TCMG) in mid-November and follow-up communications with the Executive Portfolio Holder for Resources. With regard to the development of the BP, at the TCMG meeting the following was undertaken:

- the BP model was reviewed so the investment schedule could be examined as well as both the revenue and capital propositions,
- potential investment opportunities were discussed to gauge member appetite; these included both commercial assets and property funds.

Further, TCMG also discussed proposals for the reallocation of the General Fund balance.

3. THE BUSINESS PLAN

3.1 The BP itself is shown at **Appendix 2**, in addition to the Councils existing investment portfolio (£20.9m) the Council will aim to invest up to £50.0m between Quarter 3 of 2015/16 and the end of 2019, a summarised profile of investments is shown at **Appendix 3** and estimated revenue returns are shown in **Table 1** below.

Estimated Revenue Returns from the Commercial Investment Strategy						**Table 1**
	2015/16 **£000**	**2016/17** **£000**	**2017/18** **£000**	**2018/19** **£000**	**Increase in Investments (2015/16 to 2018/19)** **£000**	
EXISTING INVESTMENTS						
Costs	371	379	386	394		
Income	(1,869)	(2,047)	(2,241)	(2,454)		
Net Income	**(1,498)**	**(1,668)**	**(1,855)**	**(2,060)**	562	38%
NEW PROPOSITIONS						
Revenue Propositions						
Costs	0	0	0	0		
Income	(27)	(114)	(236)	(265)		
Net Income	**(27)**	**(114)**	**(236)**	**(265)**		
Capital Propositions						
Costs	1	14	40	51		
Income	(56)	(875)	(2,120)	(2,825)		
Income before debt charges	**(55)**	**(860)**	**(2,081)**	**(2,774)**		
Debt Service/MRP	69	885	1,949	2,369		
Net Income	**14**	**25**	**(132)**	**(405)**		
CIS OVERHEADS	103	130	182	238		
TOTAL NET REVENUE	**(1,408)**	**(1,627)**	**(2,041)**	**(2,492)**	1,084	77%
Revenue Contribution to Equity (*1)	6.1%	7.1%	7.8%	9.0%		

Key:
Equity – the difference between total asset values and debt

Existing Investment Portfolio

3.2 The BP includes the Councils current commercial estate, valued at £20.9m and for 2014/15 gave a return of 7.2%.

Revenue Propositions

3.3 Local government is only permitted to invest in one revenue property investment fund; this is operated by CCLA Investment Management Limited and the BP proposes investing a total of £4.7m by the end of 2016/17.

Capital Propositions

3.4 The Capital Propositions include the following investment opportunities (amounts shown are net of completion costs):

i. Property Shares
These are investments in property funds, similar in nature to Unit Trusts. The BP proposes investing £10.0m by mid-2016/17. Further property funds and shares (such as Real Estate Investment Trusts) are being investigated and their suitability is being assessed,

ii. Direct Assets (Local Area)
These are investments in commercial property assets that are within the Councils local area. The BP proposes investing £18.9m by mid-2017/18. The “local area” is deemed to be Cambridgeshire and the area covered by the Local Enterprise Partnership.

iii. Direct Assets (Regional Cities)
These are investments in commercial property assets that are outside of the Councils local area. The BP proposes investing £14.2m by the end of 2017/18.

Governance and Reporting

3.7 The BP includes a number of key performance indicators (KPI’s). It is proposed that these KPI’s are included within the Councils overall Treasury Management Strategy and reported to management in line with that key Strategy.

3.8 In addition, the performance of the BP and proposed investment opportunities and future borrowing requirements will be reported on a quarterly basis to the Treasury and Capital Management Group (TCMS). The TCMS included the Leader, Deputy Leader and the Executive Portfolio Holder for Resources along with the Head of Resources (as the Councils S.151 officer).

4. FINANCING

4.1 In total, the Council is looking to have a commercial asset portfolio of £71.0m; £68.7m once completion costs are excluded (based on current values). This is shown in **Table 2** below:

Funding of CIS Portfolio			**Table 2**
Funding	**Asset £m**	**Completion Costs £m**	**Total £m**
Existing Assets	20.9	0.0	20.9
Revenue Funding (2015/16)	12.1	0.4	12.5
Revenue Funding (2016/17)	2.4	0.1	2.5
Borrowing	33.3	1.8	35.1
Total	**68.7**	**2.3**	**71.0**

Reserves

4.2 The forecast:

- General Fund (GF) balance will have increased to £9.8m by the end of 2015/16 (**Appendix 4**). At the Cabinet meeting held in February 2015, the minimum level of GF Reserves was set at £3.0m. At this time, this is contributing to a short-term investment income return of 0.2% which is considerably less than the Revenue Returns noted in **Table 1** (3.1). Therefore, to maximise the return from our balances it is proposed that £6.8m is transferred from the GF Reserve to the Capital Investment Earmarked Reserve (CIER).

- CIER balance will have increased to £5.7m by the end of 2015/16 (**Appendix 4**). With the inclusion of the £6.8m from the GF, this would give a total of £12.5m available for immediate investment. A significant advantage of transferring this balance is that by using internal resources this will mitigate the need to borrow; thus the need to finance a Minimum Revenue Provision.

Borrowing

4.3 Borrowing is expected to be from the Public Works Loans Board (PWLB). For the investments within the BP, repayment loans are expected to be the preferred form of loan finance.

4.4 If however, loan rates are found to be cheaper at other financial institutions then the Council will take appropriate advantage, providing that the institutions are included within the Councils Treasury Management Strategy.

Minimum Revenue Provision (MRP)

4.5 Where the Council externally "borrows" for capital purposes, the Council is required:

- to set aside an amount in respect of MRP.
- have in place an approved MPR policy.

4.7 The capital propositions included within the BP that are to be financed from external borrowing are modelled on being financed by repayment loans (4.4), consequently the annual principal repayment will equate to the MRP requirement. As this is a new approach to MRP a new Policy is required to be approved by Full Council. Therefore the proposed MRP Policy for the CIS is shown below:

"For each capital investment undertaken under the requirements of the Councils Commercial Investment Strategy, Minimum Revenue Provision will be made that is equal to the principal repayment for any loan finance supporting the investment."

4.8 Through the operation of the CIS, there may be occasions when investment assets are sold; it is recommended in the Reserve Review report elsewhere on the agenda, such capital receipts will be ringfenced for future CIS reinvestment in line with the Reserves Strategy.

5 RISKS AND BUSINESS PLAN ASSUMPTIONS

5.1 The Council has a very good track record of managing commercial assets; however what is proposed by the CIS is a step change in approach and therefore will attract a unique set of risks. A detailed analysis of the risks and mitigations is shown in **Appendix 5** along with the key assumptions of the Business Plan.

6. COMMENTS OF OVERVIEW & SCRUTINY PANEL

6.1 Due to the date of the Overview and Scrutiny (Economic Well-Being) Panel meeting and the date of the agenda dispatch of the Cabinet Agenda the comments will be circulated subsequent to the Panel meeting on the 8th December 2015.

7. TIMETABLE FOR IMPLEMENTATION

7.1 The CIS Business Plan (Appendix 2) illustrates the proposed investment plan.

8. LINK TO THE CORPORATE PLAN

8.1 Supports "ensuring we are a customer focused and service led council" by delivering value for money services.

9. CONSULTATION

9.1 Detailed discussions with the Leader and Executive Portfolio Holder for Resources as key members of the Treasury & Capital Management Group.

10. LEGAL IMPLICATIONS

10.1 The Council has the relevant broad legal powers to undertake the activities proposed. Each specific decision taken will need to be assessed for any legal implications and requirements to ensure the Council acts lawfully and in accordance with the decision making process set out in the Constitution. As such, regard will need to be given to the Constitution and the scheme of delegations which may require amendments to allow this process to be workable.

11. RESOURCE IMPLICATIONS

11.1 The direct resource implications are noted within the report.

12 REASONS FOR THE RECOMMENDED DECISIONS

12.1 The recommended decisions will enable the Council to commence the acquisition of commercial assets, this in turn will generate revenue funding that will assist the Council in devliering cost effective services.

13. LIST OF APPENDICES INCLUDED

Appendix 1 – Plan on a Page.
Appendix 2 – Commercial Investment Strategy: Business Plan.
Appendix 3 – Summarised Profile of Investments
Appendix 4 – Extract of Forecast Outturn and General Fund Reserve as at September 2015 (reported to Cabinet, November 2015)
Appendix 5 – CIS Risks, Mitigations and Key Assumptions

BACKGROUND PAPERS

If stated need to be made available for publication for Cabinet meetings.

CONTACT OFFICER

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Plan on a Page

Appendix 1

VISION

To improve the quality of life for the people of Huntingdonshire and work towards sustainable economic growth whilst providing value for money services

STRATEGIC PRIORITIES

- A strong local economy
- Enabling sustainable growth
- Working with our communities
- Ensuring we are customer focused and service led council

CURRENT SERVICES

- Customer Service Strategy / Service Standards
- Lean
- Shared Services
- Zero Basing
- Income Generation
- Facing the Future

CLICK arrow for details

FINANCIAL

Financial ambitions

To reduce the Council's reliance on Central Government Funding and in so doing create a sustainable financial platform

	2015/16	2016/17	2017/18	2018/19	2019/20
Approved MTFS	£18.881m	£19.870m	£20.671m	£21.259m	£21.721m
% cut from MTFS	0% (-£0m)	19.2% (-£3.8m)	28.6% (-£5.9m)	35.1% (-£7.5m)	37.6% (-£8.2m)
Modified budget	£18.881m	£16.059m	£14.750m	£13.805m	£13.553m

Appendix 2

Commercial Investment Strategy
Resources - Estates

BUSINESS PLAN
(Q3 2015/16 TO Q4 2018/19))

Author: Clive Mason

Owner: Clive Mason Head of Resources

Client: HDC

Revision History:-

Version	Date	Status	Summary of Changes	Author
1	23/11/2015	Current	CIS Business Plan reviewed by Corporate Management Team	Clive Mason
1	08/12/2015	Current	CIS Business Plan reviewed by Overview & Scrutiny (Economic Well-Being) Panel	Clive Mason
1	10/12/2015	Current	CIS Business Plan reviewed/approved by Cabinet	Clive Mason

Distribution:-

This document has been distributed to:

Name	Role	S/R/I*
Cllr Jonathan Gray	Executive Portfolio Holder for Resources	S & R
CMT	Corporate	S & R

** S = SIGN-OFF, R = REVIEW, I = Information*

1. Business Rationale

1.1. **Description and Objectives**

The Council faces considerable “revenue” financial challenges over the medium term; as shown in the Medium Term Financial Strategy (MTFS) the Council will have a budget gap of £2.4m by 2019/20 and between the end of 2016 and 2020 there will be a general reduction in general fund balances of £6.3m; such use of reserves does not represent financial sustainability.

To achieve financial sustainability, the Council is required to bridge a funding gap of £8.2m, as shown on the “Plan on a Page” and a key business activity to meet this gap is “income generation”, with the generation of revenue income via investment in Commercial Assets being a key component. The Council approved the Commercial Investment Strategy (CIS) in September 2015 and the CIS covers a 9 year period. This Business Plan is the vehicle through which the Council will aim to achieve additional revenue income between now and the end of 2019.

This approach will be a key thread in securing a sustainable financial future for the Council, as endorsed by Cllr Jonathan Gray, Executive Portfolio Holder for Resources:

> *“The Council faces an unprecedented decline in government funding and consequently, the Council needs to deliver services and generate income in new and innovative ways. The Commercial Investment Strategy will be a key driver to ensuring that the Council will have a sustainable financial future in the medium to long term. By investing in commercial assets, the Council aims to generate a revenue stream that will, over the medium term, support the delivery of cost effective services to the local community and over the next 10 years, to develop a healthy growth in invested capital resources”.*

1.2 **Strategic Objectives**

The overall objective of the CIS is to undertake commercial activity to support the Council’s General Fund in the cost effective delivery of services.

Consequently, the strategic objectives of the CIS are as follows, to:

i. generate sustainable revenue returns from investments in commercial assets that will support the general fund over the medium term.
ii. develop a long-term commercial asset portfolio that will generate capital returns for immediate reinvestment.

1.3 Business Background

1.3.1 **CIS**

The CIS portfolio model covers a 9 year period, broken down into 3 distinct, but not equal phases:

Phase 1 – this will focus on the development of revenue returns.
Phase 2 – this will consolidate Phase 1 and commence pool funding to invest in capital assets that will generate future capital growth.
Phase 3 – this will be an extension of Phase 2 so there is further investment in capital generating assets with a concentration on ensuring that the developed capital assets continue to develop revenue returns.

This approach to the commercial investment portfolio will aim to appropriately balance risk and reward with flexibility and the over-riding objective of revenue generation.

This first business plan will cover Phase 1, from now until 31st March 2019. The delivery options that the business plan will concentrate on include:

- Existing assets,
- Property Shares and Investment Funds
- Direct Assets (local and national)

1.3.2 Existing Asset

The Councils existing asset portfolio, as reported in the Councils Annual Financial Report 2014/15 is shown in **Table 1** below:

Current Investment Assets (31st March 2015)		**Table 1**
		£m
Revenue	Rental Income Direct Costs **Net revenue**	(1.9) 0.4 **1.5**
Capital	**Valuation**	**20.9**

The current portfolio generates a net return of 7.2%.

1.3.3 CIS Investments

It is intended that by the end 2017/18 the Council will seek to invest a further £50.1m, with the Councils existing asset portfolio this gives a total commercial estate of £71.0m.

The capital investment will permit the purchase of new assets totalling £47.8m with associated completion costs of £2.3m (see **Table 2** below). When the existing portfolio is included, this would give a total commercial investment portfolio of £68.7m. The completion costs of £2.3m are allowable capital expenditure and as such capital resources can be used to finance these costs.

CIS Investment Portfolio			**Table 2**
Funding	**Asset £m**	**Completion Costs £m**	**Total £m**
Existing Assets	20.9	0.0	20.9
Revenue Proposition			
• Investment Fund	4.7	0.3	5.0
Capital Proposition:			
• Property Shares	10.0	0.1	10.1
• Direct Assets (Local Area)	18.9	1.0	20.0
• Direct Assets (Regional Cities)	14.2	0.8	15.0
Total	**68.7**	**2.2**	**71.0**

1.3.4 **Funding of CIS**

The business plan proposes that the £71.0m CIS portfolio is to be funded as shown in **Table 3** below:

Funding of CIS Portfolio			**Table 3**
Funding	**Asset £m**	**Completion Costs £m**	**Total £m**
Existing Assets	20.9	0.0	20.9
Revenue Funding (2015/16)	12.1	0.4	12.5
Revenue Funding (2016/17)	2.4	0.1	2.5
Borrowing	33.3	1.8	35.1
Total	**68.7**	**2.3**	**71.0**

1.3.5 **Revenue Funding**

The CIS is not a “capital only” investment strategy; to spread risk and maximise investment opportunities it is beneficial for the investment portfolio to be as broad as possible. Therefore, by investing in revenue only investments (1.3.3) as well as using revenue funds to finance capital investment, the Council is able to maximise its portfolio but in the most cost effective way possible.

As at the 31st March 2015, the Council’s General Fund Balance stood at £9.3m and had earmarked £4.7m in a Capital Investment Earmarked Reserve (CIER).

The September 2015 Budget Monitoring information, as reported to Cabinet in November 2015, forecast that by the end of 2015/16 a further contribution to the:

- General Fund balance of £0.5m would be made, giving a balance of £9.8m.
- CIER of £1.0m would be made, giving a balance of £5.7m.

Considering that the Council has approved a minimum level of General Fund reserves of £3.0m, it is proposed that the Council will transfer £6.8m from the General Fund balance to the CIER, thereby giving the Council £12.5m to invest in its Commercial portfolio. The benefits of utilising the General Fund balance in this way will be to:

i. Minimise the need to borrow, and therefore reduce statutory costs relating to the Minimum Revenue Provision, and
ii. Maximise returns from amounts invested.

1.3.6 **Treasury Management Strategy - borrowing**

The current Treasury Management Strategy (TMS), approved by Council in February 2015, permits the Council to long-term borrowing of up to £60.0m for “capital investments delivering a commercial yield”. With the investment portfolio proposed within the BP (Phase 1 of the CIS) a total of £35.1m is estimated to be borrowed by 2018/19, the profile of borrowing is shown in **Table 3** below:

Estimated Borrowing Profile for CIS	Table 3 £m
Now until 31st March 2016	0.0
2016/17	20.0
2017/18	15.1
2018/19	0.0
Total	**35.1**

However, this leaves the Council with a further £24.9m available to borrow and invest in commercial activity. If an opportunity presents itself, the Council will be free to invest further within the CIS governance arrangements and the thresholds allowed within the TMS.

1.3.7 **Use of Debt**

Debt will be used to both increase the size of the CIS portfolio and to enhance returns. It is imperative that the use of debt as a form of financing is carefully monitored to ensure that the Council is not overly leveraged and the credit liability inherent in debt financing, and the cost of financing, is managed within the permitted limits of the Councils Treasury Management Strategy.

The overall amount of debt used in the CIS will be monitored in two ways:

i. Interest Cover Ratio (ICR)

This ratio determines the amount of total net income from property investments (after operating costs and any applicable taxes) compared with the interest expense of the debt. This is important so the amount of interest payable compared to income generated is proportionate.

Because debt commences later in the Phase 1 cycle, the profile of the ICR is shown in **Table 4** below. It is suggested that these are initial indices reflecting the maximum debt interest to revenue at the commencement of the BP. If investments profiles change, the ICR ratio will change.

Initial Interest Cover Ratio (at start of CIS Business Plan)			Table 4
Year	Estimated		ICR
	Revenue cash flow £000	Cost of Interest £000	
2015/16	183	11	16.6
2016/17	292	55	5.3
2017/18	403	87	4.6
2018/19	463	95	4.9

ii. Loan to Value Ratio (LTV)

This ratio determines the amount of total debt (compared to the total value of the underlying property assets as valued from time to time. Debt in this respect is both internal and external debt, i.e. revenue financing and borrowing from the market that is used to finance the capital propositions. Although it is recognised that the primary form of finance for the CIS portfolio is debt, it is important to ensure that the proportion of debt to asset value is actively managed to ensure that the debt burden is within acceptable limits

In a similar way to the ICR, the LTV rations, as shown in **Table 5** below reflect that debt commences later in the BP cycle. It is suggested that these are initial indices reflecting the maximum debt asset value at the commencement of the BP. If investments profiles change, the ICR ratio will change.

Loan to Value Ratio (at start of CIS Business Plan)			Table 5
Year	Estimated		ICR
	Loan Value £000	Asset Value £000	
2015/16	10.0	32.9	30
2016/17	29.5	52.3	56
2017/18	43.5	69.5	63
2018/19	42.3	70.1	60

It is recognised that while the LTV is an important indices when having regard to debt repayment obligations, the ICR is the more important indices when monitoring the CIS on an on-going basis because it provides performance information that will enable the Council to determine its ability to:

- Make revenue contributions that will support the delivery of Council services.
- Meet its interest payments commitments on the debt within the CIS.

1.4. Portfolio Approach

The CIS will be viewed on a portfolio basis, in that the CIS's performance will be monitored "as a whole". This reflects the fact that the portfolio is made up of different investment propositions that themselves have different risks and rewards.

The current Estates team will be restructured so it will be able to proactively monitor and report to management on individual assets, relevant subsets or sectors of assets also the total portfolio; this shall include the Council's current commercial portfolio. In addition, the CIS will be actively reported to the Treasury & Capital Management Group.

In this way the Council will be able to:

- Make decisions about and review the CIS on an integrated and holistic basis
- Target and achieve diversification of investments and risk styles
- Benchmark performance
- Better manage risk

1.5. Delivery Options

There are a variety of ways in which the Council can invest in property; these are detailed in **Annex 1** and summarised below:

1. Type 1: Existing Assets
2. Type 2: Investment Funds
3. Type 3: Listed Property Shares
4. Type 4.1: Direct Asset (Local Area)
5. Type 4.2: Direct Asset (Regional Cities)
6. Type 5.1: Risk Share Development – Forward Purchase/Funding
7. Type 5.2: Risk Share Development – Joint Venture
8. Type 6: Self Develop

The approach to all these options at the start of the investment programme should be to start the CIS investment approach with a lower risk activity that can evolve over time as more experience is gained. Whilst the CIS would permit the delivery of all six delivery options, only Types 1 to 4 will be considered over the Phase 1 period of the BP.

With regard to a definition for “Direct Asset (Local Area)”, this is seen as anywhere within Cambridgeshire and the Local Enterprise Partnership area that the Council resides.

The capital value options (Types 5 & 6) are recognised as having higher risk and will be developed over Phase 2 and 3 (2019/20 onwards). It is recognised that risk may in fact be lower for Types 5-6 where they are within the Councils boundary given the specific knowledge that the Council may have in relation to those projects, the planning context, tenant requirements and general market knowledge. However, these investments are more complicated by their nature and consequently at this time will be left to a later period of the CIS.

1.6. Progressive Approach

It is understood that the desired portfolio mix, income profile and risk profile of the CIS is unlikely to be achieved in the first year of the business plan, and should be viewed as an evolutionary process that will take time to mature. Indeed, actual investments may not follow that indicated as such investments will be dependent on a host of variables, including but not limited to when the actual opportunity arises.

An indicative approach to the build-up of the portfolio, the appropriate delivery options over time and the reinvestment of capital is set out in the chart in **Annex 2**.

1.7. Approach to Risk

The strategic objectives of the CIS are designed to mitigate risk by:

- Having the fundamental aim of an income rather than capital return (although the latter is part of the strategy)
- Adopting a portfolio approach so as to avoid concentration of risk in any one property, tenant or risk type

In addition, CIS risk will be managed having regard to the following factors:

1. A robust acquisition due diligence process and subsequent approvals.
2. Asset management plans and on-going reviews.
3. Liability management (reviews of debt levels and terms).
4. Tenants (financial exposures, potential defaults, changing business plans).
5. Portfolio factors including occupancy levels, operating costs, etc.
6. Delivery partners (suitability, performance levels and financial stability).
7. Market factors (with periodic advice from appropriate professionals).
8. State Aid considerations.
9. Professional advisors.

1.8. Role of the Business Plan

The role of the Business Plan is to review on a periodic basis:

1. The strategic objectives of the CIS
2. The target income returns of the CIS
3. The target amount of capital invested in the CIS
4. The debt levels to be utilised in the CIS
5. The target portfolio composition of the CIS
6. The delivery models for achieving the CIS
7. The appropriate risk profile for the CIS

1.9 Key Assumptions

The key investment assumptions included with the BP are:

- Maximum Debt: £60.0m
  - The limit on Commercial Investments as approved in Treasury Management Strategy.

- PWLB Loan Rate: 2.75%, loans with a life of 20 years
  - The prevailing loan rate.

- Cost of funding capital propositions: a margin of 2% per annum and a management fee of 0.75% per annum.
  - The inherent cost of financing capital investments on an ongoing basis.

- CPI/General Inflation: 2.5%
  - Inflation on costs and income.

- Completion fees ranging from 0.50% to 5.75%
  - Each investment will incur costs to acquire. Such costs can be charged to capital.

- Revenue indexation/growth ranging from 2% and 3%
  - Estimates for revenue growth from the portfolio and capital value.

2. Financial Objectives

2.1. Target Income Returns

The primary indices for measuring returns on investment is the “return on equity” (ROE) indices. This is effectively the:

*Net Revenue Contribution (*1) / Equity (*2)*

**1* Revenue contributions shall be calculated as net i.e. income returns after taking into account all operating and management costs, interest expense, minimum revenue provision and relevant taxes.

**2* Equity being the difference between the value of assets and borrowing.

Following extensive modelling of the proposed investment opportunities, the expected revenue contribution to the Council will be £2.5m by the end of 2018/19; this gives a ROE of **9%.**

However, reflecting the income expected to be generated from the CIS will grow over time, it is best to have an ROE range for the period of the BP, this will be set between **6%** and **9%** per annum.

It is accepted that individual investments will contribute different levels of income return and that the target revenue contribution is an average across the CIS portfolio (1.4).

2.2. Allocations to Delivery Options (see 1.5 for definitions)

Immediate

At inception the CIS will consist of the Councils current Commercial Portfolio (Type 1: Existing Assets).

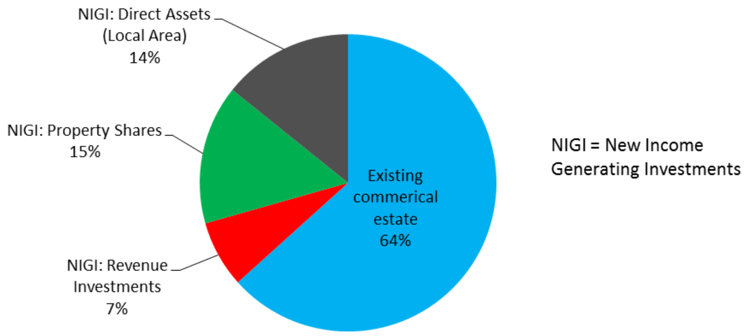
Year 1: Now until 31st March 2016

As well as the existing commercial estate, the Council will contribute £12.5m from in house resources to finance new commercial acquisitions, there will be no additional debt financing to the CIS. However, the £12.5m will used to meet estimated £12.1 in asset purchase costs and £0.4m in completion costs.

This additional investment will be allocated to immediate income generating investments:

i. Investment Funds (Type 2)
ii. Property Shares (Type 3)
iii. Direct Assets (Local Assets) (Type 4)

As a result it is intended that at the end of year 1 the capital invested (purchase price) in the CIS will be split as follows:



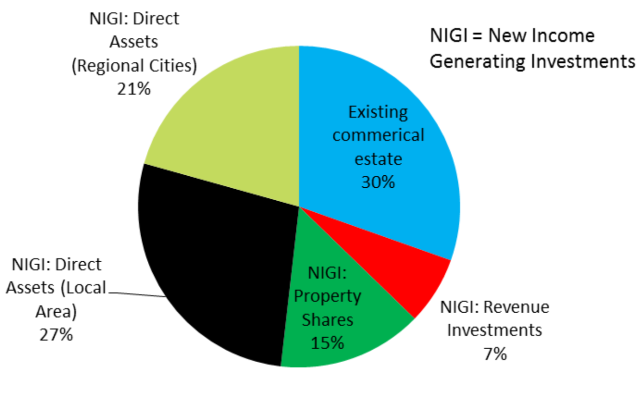
The net value of the Portfolio:	£32.9m
Debt within the Portfolio:	£10.1m

The net estimated revenue return by the 31st March 2016 is £1.4m, this is made-up of: £1.5m from the existing commercial estate, a marginal contribution from new investments of £27,000 and portfolio management costs of £100,000.

In this way the CIS can accommodate a blend of investments in year one between those that are immediately income producing and those that create capital returns and/or future income. As shown in the aforementioned paragraph, it should be noted that net returns are reduced in the initial period of investment as a consequence of initial purchase/sales fees – but as these fees are met, future year's returns start to increase.

Target Year 3: By 31st March 2019

By the end of the BP period, the value of the CIS portfolio will be £68.7m and split as follows



Some of the assets within the portfolio, such as revenue investments and property shares could be part of a wider asset product, similar to unit trusts. Consequently their liquidity is limited as the Council will not be able, on its own, to realise an investment quickly. However, such investments are not made for short-term capital gain and in reality the Council will be expected to invest in such assets for a minimum of 4 to 5 years. Because of the poor-liquidity of these investments, it is proposed that such assets will not exceed 25% of the CIS portfolio at any one time (the Illiquid Asset Ratio).

It is envisaged that investments made in future income producing investments (i.e. Direct Assets, either Local Area or Regional Cities i.e. delivery types 5 & 6) will either be sold and reinvested, or held as income producing assets. As such there will be a natural shift in the portfolio balance over time.

2.3. Borrowings

Borrowings will be the primary source of funding for the expansion of the CIS. As referred to in paragraph 1.3.7, there are two metrics that shall be used to monitor the debt position in the CIS, the Loan to Value ratio (LTV) and the Interest Coverage Ratio (ICR). As previously shown in **Tables 4** and **5**, there will be a range of indices as the BP matures up to the 31st March 2019, and the proposed range is shown below:

- LTV range shall be between of 5 and 17.
- ICR range shall be a between 30 and 65.

2.4 Future Capital Receipts

As the CIS develops, there may be occasions when assets are sold. All capital receipts will be ring-fenced to the CIS. Capital receipts will only be used for non-CIS investment when there has been separate agreement by Cabinet.

2.5. Section 151

As a consequence of the government's austerity programme, as well as the Council having to review both its direct and indirect service provision, it is also required to review the ways in which it manages and generates its corporate income. The current MTFS is forecasting savings required of in excess of £2.4m by 2019/20; however, with the continued pressure of ongoing austerity the Council is seeking to reduce its reliance on New Homes Bonus thereby becoming non-reliant on central government support. At this time this equates to savings of around 37.6% (£8.2m) by 2019/20.

Investing in commercial assets to generate an income stream is a relatively new and innovative way in which some Councils are seeking to bridge the gap in their budgets. This Councils Commercial Investment Strategy (and this Business Plan) is an ambitious plan to develop such a revenue stream. Expert advice has been sought from EC Harris, including the development of a financial business case which has allowed the Council to appropriately scenario plan different investment opportunities.

As mentioned, this Business Plan is ambitious but it is considered achievable. Obviously, returns are dependent on the market and the market remains "uncertain" even 7 years after the crash of 2008. However, the Council has not lost sight of the statutory requirement in respect of Treasury Management activity in that the primary driver must be to maintain the capital sum; consequently this plan represents a mix of investments and therefore a mix of risk to ensure the capital sum is fairly protected but allows for the generation of revenue income.

Firstly, the plan aims to invest in long-established property related investment funds (£15.0m), both of which are acceptable to the Councils Treasury Management advisors. Secondly, the plan then proposes to invest £35.0m in property assets; £20.0m in its local area (thereby clearly demonstrating the Councils commitment to its local area) and £15.0m on a wider geographical basis. It is therefore fair to say that the Plan takes a balanced view on risk, seeking to safeguard the capital invested but also to maximise the opportunity to generate fair revenue income returns.

2.6. Portfolio & Risk Metrics

A series of metrics will be used to examine the current performance and assist in planning the future profile of the CIS. The primary performances indices highlighted earlier in the BP include:

- Interest Cover Ratio (1.3.7i)
- Loan to Value Ratio (1.3.7ii)
- Return on Equity (2.1)
- Illiquid Asset Ratio (2.2)

Over-and-above these indices, there are other indicators that would be useful to monitor the CIS, however most of these will come into play as the CIS matures. These include:

- Historic and forecast income and total returns
  As the CIS matures, different assets will be purchased within the same asset type. It will be useful to monitor the performance of the assets to assist in informing future assets acquisitions.

- Benchmarking of returns (IPD)
  It would be useful to benchmark returns against the market and against other Councils.

- Gross & net income
  Gross and Net income of the CIS itself will be useful to determine the overall cost envelope and the efficiency of the portfolio.

- Operating costs
  This indices will be useful to determine the cost efficiency of the overheads within the Portfolio.

- Vacancy levels and Tenant exposures
  These two indices will be useful to determine how effectively tenancies within the property investments are being managed. Would also be useful to review the types of tenant and their relevant industry to see if certain industries are better tenants.

3. Reporting

3.1 Reporting to Council

The CIS will be an intrinsic part of the Councils Treasury Management Strategy (TMS) and as such will be reported to Council in line with the TMS and the other TMS related reports.

The performance reporting specifically related to the CIS will include the basket of indicators noted within the business plan.

3.2 In-year Performance Reporting

The Cabinet has established a “Treasury and Capital Management Group” (TCMG), its purpose to meet on a quarterly basis to review the Councils Treasury Management activity and the performance and approval of the Councils capital programme. As the CIS will become a key element of the Councils TMS, the TCMG will take a member lead in supporting and guiding the operation of the CIS.

4. Risk Management

Risk will be managed as envisaged in section 1.7 above and having regard to the portfolio and risk metrics referred to in section 2.5 above.

Appropriate reporting formats will be developed and reviewed in line with 5.

5. Other Matters for Consideration

5.1 Governance

The CIS is intended to be managed within the Councils current governance structures. Day-to-day management will be within the Resources Team with quarterly review by the Treasury and Capital Management Group, including relevant performance reporting as noted in 3.2 above. In addition, as the CIS will be a key element of the Councils TMS, it will be included within the TMS statutory reporting requirements.

5.2 Resourcing Plan

The current Estates Team will be reviewed following approval of the CIS Business Plan to ensure that the Council will have in place appropriate resources to ensure the effective and successful operation of the business plan.

5.3 Audit Requirements

The CIS and the Business Plane will be subject to both Internal and External Audit as agreed by the Corporate Governance Panel and the External Auditors Code of Audit Practice respectively.

5.4 Timescales for the Commencement of the Business Plan

Target Start Date	Cabinet – December 2015
Target End Date	31/03/2019
Business Plan review due	Annually, or more frequently if required.

Delivery Options for the Commercial Investment Strategy

Annex 1

1. Existing Assets

WHAT IS IT?

- This is the Councils current commercial portfolio.

HOW DOES IT WORK?

- The Council will continue to manage the estate based.
- After deciding on price and clearing appropriate internal approvals, bid for assets.
- Using appropriate advisors (legal, surveying, valuation) undertake due diligence and complete legal acquisition documentation.
- Ongoing management arrangements (internal).
- Regular asset reviews to determine business plan and exit strategy.
- Process required on an asset by asset basis.

BENEFITS

Financial Objective	Depending on property type, is capable of delivering market level income return
Revenue Delivery	Generates revenue from the time of the property acquisitions
Risk	Low risk option with the appropriate due diligence
Control	High level of control
Liquidity	Reasonable liquidity, subject to usual property market timings
Management Oversight	Assuming management is outsourced - relatively light requirement - high involvement at key decision points (buying and selling)

LIMITATIONS

Performance	Low return option and no competition in the market for the Council.
Diversification	Maintain and develop as required.

2. Investment Funds

WHAT IS IT?

- The Council invests in an unlisted property fund which owns a range of diversified property investments.

HOW DOES IT WORK?

- The Council will undertake a process of reviewing available fund options and the track record of the fund managers.
- Once capital is invested the entire responsibility for acquiring and managing the investments is delegated to and the responsibility of the fund manager.
- The fund manager will report and pay distributions to the Council on a regular basis, usually quarterly.
- The fund documentation will set out the rights of the Council to redeem its investment and/or to sell it on the secondary market. The nature of these rights will vary depending on the type of fund.

BENEFITS

Financial Objective	Depending on property type, is capable of delivering market level of income return
Revenue Delivery	Generates revenue from the time of the fund investment - generally a shorter time than investing in direct property
Risk	Risk is determined by the nature of the fund. Additional risks relate to the fund structure, principally the performance of the fund manager
Performance	Returns are related to the specific investment strategy of the fund and manager performance.
Diversification	Fund investment can spread risk over a large number of underlying assets.
Control	High level of control of fund interest
Management Oversight	Very light requirement

LIMITATIONS

Liquidity	Unlisted investment funds generally have a low level of liquidity, particularly in market downturns.

3. Listed Property Shares

WHAT IS IT?

- The Council invests in listed property shares in a fund or a separate account mandate managed by a specialist fund manager.

HOW DOES IT WORK?

- The Council will undertake a process of reviewing managers and available fund options and selecting an appropriate investment strategy.
- Once capital is invested the entire responsibility for acquiring and managing the investments is delegated to and the responsibility of the fund manager.
- The fund manager will report and pay distributions to the Council on a regular basis, usually quarterly.
- The mandate with the fund manager can be structured to allow an immediate liquidation of the investment portfolio if required.

BENEFITS

Revenue Delivery	Generates revenue from the day the property shares are acquired - share transactions can be effected in a short time period
Liquidity	The highest level of liquidity
Risk	The risk and return level is flexible and can be altered over time by reference to the agreed investment strategy
Diversification	Risk can be spread over a large number of underlying property companies/assets.
Control	High level of control
Management Oversight	Very light requirement

LIMITATIONS

Performance	Higher volatility than direct property. Longer term performance correlates to property but short term can correlate to general equity markets
Financial Objective	Dividend yields generally lower that direct property yields.

4.1 and 4.2 Direct Assets – Local and National Acquisitions

WHAT IS IT?

- The Council acquires and manages freehold or leasehold properties in either the Local area (defined as within Cambridgeshire and the Local Enterprise area) or Nationally.

HOW DOES IT WORK?

- The Council uses property professionals to identify market opportunities.
- After deciding on price and clearing appropriate internal approvals, bid for assets.
- Using appropriate advisors (legal, surveying, valuation) undertake due diligence and complete legal acquisition documentation.
- Establish ongoing management arrangements (internal or outsourced).
- Regular asset reviews to determine business plan and exit strategy.
- Process required on an asset by asset basis.

BENEFITS

Financial Objective	Depending on property type, is capable of delivering market level income return
Revenue Delivery	Generates revenue from the time of the property acquisitions
Risk	Low risk option with the appropriate due diligence
Control	High level of control
Liquidity	Reasonable liquidity, subject to usual property market timings
Management Oversight	Assuming management is outsourced - relatively light requirement - high involvement at key decision points (buying and selling)

LIMITATIONS

Performance	Low return option and no competitive e market position for HOC
Diversification	Circa 20 investments required to deliver portfolio diversification

5.1 Risk Share Development - Forward Purchase / Funding

WHAT IS IT?

- The Council enters into an agreement with a developer to fund part of the development cost and/or acquire a development on completion.

HOW DOES IT WORK?

- The Developer will identify a market opportunity (although it may come from the Council) and carry out the development functions
- The Council will be able to determine the risk profile it wishes to take on in entering the arrangement with the developer (e.g. after planning permission has been secured and construction packages have been tendered).
- During the construction stage the Council will likely require monitoring rights.
- Post development completion (as per direct investment):
  - Establish ongoing management arrangements (internal or outsourced).
  - Regular asset reviews to determine business plan and exit strategy.

BENEFITS

Financial Objective	Should deliver a premium to pure investment activity, so at least a market level income return dependent on property type
Performance	A higher level of performance than investment activity
Risk	The risk of development is highly mitigated by the forward purchase/funding arrangements
Control	High level of control
Management Oversight	Moderate level once the transaction is agreed

LIMITATIONS

Revenue Generation	Revenue can accrue to the investment when funded, but this will only occur during or at the end of the development period
Diversification	Circa 20 investments required to deliver portfolio diversification
Liquidity	Low liquidity during the development period, thereafter as per the general property market

5.2 Risk Share Development - Joint Venture

WHAT IS IT?

- The Council enters into a JV agreement with a developer to carry out a specific development

HOW DOES IT WORK?

- The Developer will identify a market opportunity (although it may come from the Council) and carry out the development functions.
- The risk of the development will be shared 50/50 between the Council and the Developer.
- The Council will be involved in key decisions during the development period.
- Post development completion (as per direct investment):
  - Establish ongoing management arrangements (internal or outsourced).
  - Regular asset reviews to determine business plan and exit strategy.

BENEFITS

Financial Objective	Should deliver a premium to pure investment and forward purchase/funding, so at least a market level return dependent on property type
Performance	A higher level of performance than investment and forward purchase/fund development activity
Risk	The risk of development is mitigated by careful partner selection and development stage oversight
Control	Strong level of control through JV documentation
Management Oversight	Meaningful level of oversight required

LIMITATIONS

Revenue Generation	Revenue will only accrue once the development is completed and leased (or sold).
Diversification	Diversification improved given Developer 50% capital contribution. Circa 20 investments required to deliver portfolio diversification
Liquidity	low liquidity during the development period, thereafter as per the general property market

6. Self Development

WHAT IS IT?

- The Council undertakes a development itself, appointing a development manager.

HOW DOES IT WORK?

- The Development Manager will identify a market opportunity (although it may come from the Council) and carry out the development functions.
- The risk of the development will be taken 100% by the Council.
- The Council will be involved in key decisions during the development period.
- Post development completion (as per direct investment):
  - Establish ongoing management arrangements (internal or outsourced).
  - Regular asset reviews to determine business plan and exit strategy.

BENEFITS

Financial Objective	Should deliver a premium to pure investment and forward purchase/funding, so at least a market level return dependent on property type
Performance	The highest level of performance- the Council retains all development profit
Risk	The risk of development is mitigated by appointment of expert development manager and adoption of thorough risk management strategy
Control	Complete control with the Council

LIMITATIONS

Management Oversight	Complete control with the Council
Revenue Generation	High level of oversight required
Diversification	Revenue will only accrue once the development is completed and leased (or sold).
Liquidity	Circa 20 investments required to deliver portfolio diversification
	low liquidity during the development period, thereafter as per the general property market

A Portfolio Model for the Commercial Investment Strategy

Annex 2

Developing a Portfolio Model

It is understood that HDC is intending to plan for a growing shortfall in Central Government resulting in a desire to achieve a growing revenue return over time. This can potentially be achieved in two ways. First by increasing the amount of CIS investment and secondly by taking greater risk in the investment strategy.

A potential model for taking progressively, and measured, increased risk over time is shown below. The intention is that a blend of risk profiles are employed and that the proceeds of higher risk (and shorter term) activities are partly redeployed back into the lower risk, long term sustainable "core" investment strategy.

EC HARRIS
BUILT ASSET CONSULTANCY
AN ARCADIS COMPANY

Appendix 3

"Proposed" Investment Schedule		2015/16 Year 1		2016/17 Year 2				2017/18 Year 3				2018/19 Year 4				TOTAL
		End of		End of				End of				End of				
		Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	
	Life	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Type 2: Revenue Proposition (use of ER)												Consolidation and development of "Risk Shared Development" Options				
- Asset Purchase Cost		2,364					2,364									4,728
- Asset Completion Cost		136					136									272
		2,500	**0**	**0**	**0**	**0**	**2,500**	**0**	**0**	**0**	**0**					**5,000**
Capital Proposition																
Type 3: Property Shares	20															
- Asset Purchase Cost		4,975			4,975											9,950
- Asset Completion Cost		25			25											50
																10,000
Type 4.1: Direct Assets (Local Are)	20															
- Asset Purchase Cost			4,728		4,728		4,728		4,728							18,912
- Asset Completion Cost			272		272		272		272							1,088
																20,000
Type 4.2: Direct Assets (Regional Cities)	20															
- Asset Purchase Cost						4,728		4,728			4,728					14,184
- Asset Completion Cost						272		272			272					816
																15,000
		5,000	**5,000**	**0**	**10,000**	**5,000**	**5,000**	**5,000**	**5,000**	**0**	**5,000**					**45,000**
Total per Quarter		**7,500**	**5,000**	**0**	**10,000**	**5,000**	**7,500**	**5,000**	**5,000**	**0**	**5,000**					**50,000**
Total per Annum		**12,500**		**22,500**				**15,000**								**50,000**

	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	TOTAL
By Quarter: Total Asset Purchase Cost	7,339	4,728	0	9,703	4,728	7,092	4,728	4,728	0	4,728	47,774
Total Completion Cost	161	272	0	297	272	408	272	272	0	272	2,226
	7,500	**5,000**	0	**10,000**	**5,000**	**7,500**	**5,000**	5000	**0**	**5,000**	**50,000**

	2015/16	2016/17	2017/18	TOTAL
By Year: Total Asset Purchase Cost	12,067	21,523	14,184	47,774
Total Completion Cost	433	977	816	2,226
	12,500	22,500	15,000	**50,000**

Forecast Outturn and General Fund Reserve as at September 2015 (as reported to Cabinet, November 2015)

Appendix 4

Revenue Forecast Outturn September 2015	2014/15 Provisional Outturn £'000	2015/16 Original Budget £'000	Updated Budget £'000	Forecast £'000	Forecast Variation Compared to :- Original Budget £'000	%	Updated Budget £'000	%	
Revenue by Service:									
Community	2,487	2,130	2,136	2,033	(97)	-4.6	(103)	-4.8	1
Customer Services	4,160	4,488	4,719	4,377	(111)	-2.5	(342)	-7.2	2
Development	1,268	1,691	1,700	1,388	(303)	-17.9	(312)	-18.4	3
Leisure & Health	320	58	60	(27)	(85)	-146.6	(87)	-145	4
Operations	4,546	4,593	4,593	4,587	(6)	-0.1	(6)	-0.1	5
Resources	2,997	3,930	3,929	3,901	(29)	-0.7	(28)	-0.7	
Directors and Corporate	2,845	2,377	2,392	2,265	(112)	-4.7	(127)	-5.3	6
Technical Adjustments	(452)	(386)	(386)	0	386	-100	386	-100	
Net Revenue Expenditure	**18,171**	**18,881**	**19,143**	**18,524**	**(357)**	**-1.9**	**(619)**	**-3.2**	
Contribution to Reserves	1,693	797	535	1,154	357	44.8	619	115.7	
Budget Requirement (Services)	**19,864**	**19,678**	**19,678**	**19,678**					
Financing:-									
NDR & Council Tax surplus	(6,222)	(4,242)	(4,242)	(4,902)	(660)	15.6	(660)	15.6	7
Government Grant (Non-specific)	(8,022)	(7,668)	(7,668)	(7,668)	0	0	0	0	
Contribution to Reserves (additional Funding)	2,018	0	0	660					
Council Tax for Huntingdonshire DC	**7,638**	**7,768**	**7,768**	**7,768**					
General Fund Reserve									
Balance as at 1st April	**8,684**	**8,537**	**8,537**	**9,287** A	750	8.8	750	8.8	
Contribution to Service Expenditure	603	797	535	535	(262)	-32.9	0	0	
Outturn forecast as at 31 March	**9,287**	**9,334**	**9,072**	**9,822**	488	5.2	750	8.3	

Earmarked Reserves	2014/15 Provisional Outturn £'000	Forecast £'000	Movement in Earmarked Reserves	
S106 agreements	1,141	1,141		
Commuted S106 payments	1,762	1,762		
Repairs and Renewals Funds	1,300	1,300		
Delayed Projects	262	262		
Collection Fund	2,768	2,768		
Capital Investment	4,737	5,716	979	Additional saving in excess of the contribution to General Fund Reserves
NDR Reliefs		300	300	S31 New Burdens grant - Forecast repayment to DCLG
Special Reserve	2,500	2,500		
Other Reserves	1,227	1,227		
Total Earmarked Reserves	**15,697**	**16,976**	**1,279**	

Definitions

Original Budget	As approved by Council, February 2015
Updated Budget	The Original Budget including approved carry forwards from 2014/15
Provisional Outturn	Provisional Outturn reported to Cabinet in June 2015.
(A)	Actual General Fund Balance as at 31st March 2015

CIS Risks, Mitigations and Financial Modelling Assumptions

Appendix 5

RISK	COMMENTARY	MITIGATION
Management		
• Unable to recruit necessary internal expertise to manage portfolio.	The current Estates service is not structured to be able to support the requirements of the CIS.	Skills analysis and recruitment planning, including visiting other Councils undertaking a similar CIS approach to establish skills needed. Then a full restructure of the Estates service will be undertaken.
• Internal support structure does not meet service requirements	Although the current estate is commercial centric in approach, the introduction of the CIS will require a faster approval process for investment decisions.	A Disposals & Acquisitions Policy (and a related Code of Practice) has been approved. Further the performance of the CIS is a key reporting requirement of the Treasury and Capital Management Group. Further, with a restructure of the Estates service will embed the structures needed to support the CIS.
Funding		
• Funds at 31 March 2016 not as high as currently estimated, therefore have to borrow earlier.	Possibility that the forecast underspend changes from that predicted, thereby reducing the amount available to be spent on asset acquisition from internal resources.	Ongoing monitoring of 2015/16 service delivery, ensuring that the ZBB programme and in-year savings are secured. Also, identifying as early as possible cost pressures so alternative action can be undertaken.
Investment		
• Reduced revenue streams because profile of investments changes due to investment opportunities not identified as quickly as possible.	No comment.	Early intervention with local and national estate agents (and similar brokerages) to identify opportunities as early as possible. Robust but pragmatic due diligence processes to review investment opportunities.

• Loss of capital investment	This could be the result of reduce asset values due to various forms of impairment (i.e. catastrophic disaster or local/national economy).	Pre-acquisition due diligence of assets and the market the assets are in. Ongoing monitoring of capital values and asset market to quickly identify and action where stresses are identified so asset disposal actions can be followed as quickly as possible.
• Investments in unfamiliar sector or regions may be time consuming with poor advice and low returns.	This would be the result of poor market research or over ambitious acquisitions.	Preservation of capital is paramount, thereby Council would need to follow appropriate due diligence of investment opportunities, to ensure that asset particulars are robust.
• Pressure to constrain investment to District only leading to limited opportunities and over reliance on local market conditions.	This could result to non-adherence to the CIS Business Case or political pressure to invest local rather than national.	The CIS Business Case clearly demonstrates the balance between investment types. The portfolio is balanced and shows that early property investment will centre on the local area, with a broadening in due course.
• Non-commercial activity within HDC slows investment progress	Due to poor management and or governance.	The CIS and its development is a key constituent of the “Income Generation” thread within the “Plan on a Page” and a service priority within the Resources service. An Estates service restructures will be undertaken and the CIS will be a centre of this services delivery plans.
Governance and Economics		
• Change in government regulations/legislation	The 2011 Act allows a Council to undertake “what an individual” would do; consequently investing activity of the sort included within the CIS is permissible; providing any borrowing is prudent and meets the requirements of the Prudential Code and relevant capital regulations.	By acting within current legislation requirements, the actions of the Council are not “ultra-vires”. Any future changes in government and or legislation would have to be dealt with as they occur. The worse that could happen is that the Council was required to sell its investments and repay supporting borrowing. Providing capital values are maintained at or above acquisition values, and as borrowings will be on a repayment

		basis, the Council should be able to meet any potential future obligations.
• Downturn in the National and Local economy.	This could affect capital values and rental incomes if tenant businesses fail.	Ongoing monitoring of the national and local economy and remedial action to protect capital investments (including sales/moth balling etc) and proactive reviews of rents.
• Procurement regulations make property development uneconomic without a JV and shared profit	Procurement regulations change that make current governance structures uneconomic.	Ongoing review of governance structures to ensure that tax and other economic factors are mitigated so the Council can maximise its returns.
Political Commitment		
• Political change forces change in direction.	CIS is no longer seen as a key deliverable to support ongoing service delivery.	The CIS is not a political vehicle; it is a means by which the Council can support ongoing service delivery.

CIS Financial Modelling Assumptions

The key investment assumptions included with the BP are:

- Maximum Debt: £60.0m
  - The limit on Commercial Investments as approved in Treasury Management Strategy.
- PWLB Loan Rate: 2.75%, loans with a life of 20 years
  - The prevailing loan rate
- Cost of funding capital propositions: a margin of 2% per annum and a management fee of 0.75% per annum.
  - The inherent cost of financing capital investments on an ongoing basis.
- CPI/General Inflation: 2.5%
  - Inflation on costs and income.
- Completion fees ranging from 0.50% to 5.75%
  - Each investment will incur costs to acquire. Such costs can be charged to capital.
- Revenue indexation/growth ranging from 2% and 3%
  - Esimtates for revenue growth from the portfolio and capital value.