Capital Strategy Report

2025/26

Contents

Strategic Implications

This report relates to all the objectives in the Council's Corporate Plan 2023-2026 as it supports the Council's ability to fund capital and revenue projects and services.

Background

This strategy gives 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.

Decisions made this year on capital and treasury management will have financial consequences for the Council for many years into the future. They are therefore subject to both a national regulatory framework and to a local policy framework, summarised in this report.

Capital Expenditure

Capital expenditure is where the Council spends money on assets, such as property or vehicles, that have a usable life of more than one year. In local government this includes spending on assets owned by the Council, by other bodies, as well as loans and grants to other bodies enabling them to buy or improve assets.

In 2025/26 the Council is planning to incur capital expenditure of £81M as summarised below:

Table 1 – Prudential Indicator - Estimates of Capital Expenditure

Programme Area	2023/24 Actual £'000	2024/25 Forecast £'000	2025/26 Budget £'000	2026/27 Budget £'000	2027/28 Budget £'000
Climate and Environmental	1,742	0	11	200	0
Housing	33,102	50,931	73,127	144,493	56,759
Infrastructure	18,255	1,612	1,815	50	25
IT	131	312	219	0	0
LACs	3,694	3,915	3,372	0	0
Leisure	310	1,194	68	0	0
Urban Regeneration	1,588	349	2,252	0	0
Total Capital Expenditure	**58,822**	**58,313**	**80,864**	**144,743**	**56,784**

Governance of Capital Expenditure

The current Community Investment Programme (CIP) is attached at Appendix 1A. The CIP consists of capital schemes identified by councillors as being of benefit to the community. Schemes are approved in year by Cabinet, or if it is a scheme that falls under a Local Area remit, then approval can be given by the relevant Local Area Committee (LAC).

All projects are monitored by the Project Management Office (PMO), ensuring that projects are initiated in a controlled and planned way and are reported upon regularly and in a standardised format.

For each proposed scheme, alignment to Corporate Strategic aims is confirmed before further work is carried out on the full feasibility of any project. This initial confirmation is achieved using a Project Initiation Matrix (PIM) which turns a proposal into a clear concept. When a project is authorised by Cabinet or the relevant LAC, this is after the submission and approval of a PID (Project Initiation Document) to the appropriate Strategic Programme Board. A consistent project methodology is used to control and deliver each project and report on progress through to the appropriate Strategic Programme Board. This monitoring is reported in summary form to Policy and Performance Scrutiny Committee and Cabinet as part of the quarterly performance monitoring process. A process map of the project initiation process is shown at Appendix 1B.

All Strategic Capital Projects are monitored through project boards with a senior officer designated as the Project Sponsor. Each project is also reported to regular Programme Board meetings which are chaired by a member of the Corporate Leadership Board. These Boards comprise Councillors, including a member of Cabinet, alongside key members of staff who are involved in the implementation and delivery of capital schemes including a member of the Project Management Office. The aim of Programme Boards is to ensure that schemes are managed efficiently and effectively, whilst considering the Council's priorities and aligning capital expenditure and Council resources to meet these priorities. For smaller capital spend, these items are monitored either through Local Area Committees or through the Council's regular performance monitoring process.

Financing of Capital Expenditure

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

Table 2 - Capital financing

Financing	2023/24 Actual £'000	2024/25 Forecast £'000	2025/26 Budget £'000	2026/27 Budget £'000	2027/28 Budget £'000
External sources	7,845	6,902	13,969	0	2,368
Own resources	11,049	4,526	10,874	25,426	29,458
Borrowing	39,928	46,885	56,021	119,317	24,958
Total	**58,822**	**58,313**	**80,864**	**144,743**	**56,784**

The core financing of capital expenditure continues to be borrowing. The Council continues to borrow under the guidance of CIPFA's Prudential Code for Capital Finance in Local Authorities, which gives the Council the power to borrow.

Borrowing is only a temporary source of finance, since loans and leases must be repaid and this is therefore replaced over time by other sources of finance, 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 repay borrowing. Planned MRP repayments are shown in the table below:

Table 3 – Repayment of borrowing

Repayment of Borrowing	2023/24 Actual £'000	2024/25 Forecast £'000	2025/26 Budget £'000	2026/27 Budget £'000	2027/28 Budget £'000
MRP	6,204	6,468	6,649	6,709	6,696

The Council's full MRP Policy is approved by Council as part of the Treasury Management Strategy report. The MRP policy ensures that over the life of any asset the full borrowing is repaid.

The Council's cumulative outstanding amount of borrowing is measured by the Capital Financing Requirement (CFR). This increases with new borrowing-financed capital expenditure and reduces with MRP and capital receipts used to repay borrowing. The CFR is expected to rise to £693M in 2025/26. Based on current projections for capital expenditure and financing, the Council's estimated CFR is as follows:

Table 4 – Prudential Indicator - Estimates of Capital Financing Requirement

	2023/24 Actual £'000	2024/25 Forecast £'000	2025/26 Budget £'000	2026/27 Budget £'000	2027/28 Budget £'000
Capital Financing Requirement	602,474	642,892	692,264	804,872	823,134

Asset Management

To ensure that capital assets continue to be of long-term use, the Council has an Asset Management Strategy 2020-2025 that was approved by Cabinet in 2020. This Strategy sets out the key future objectives and how the Council will effectively manage and utilise the assets of the Council. The Strategy will be refreshed and an Asset Management Strategy for 2025 – 2030 will be drafted during early 2025. This will enable the Council to examine the portfolio and assess whether long term use remains relevant in terms of sustaining the core net rental income, as well as the identification of strategic disposals and the repurposing of assets for alternative use or development opportunities.

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 used to repay borrowing.

The current Strategy reflects the flexible use of capital receipts for 2024/25 for services transformation projects. This flexibility has also been applied in previous years. The Flexible use of capital receipts has been revised during 2024/25 to take account of updated efficiencies, and therefore if approval from Council is received then details will be submitted to the Secretary of State as required by the relevant direction. Further details are contained within Appendix 1C.

Treasury Management

Treasury Management is concerned with keeping sufficient, but not excessive cash available to meet the Council's spending needs, while managing the risks involved. Surplus cash is invested until required, whilst a shortage of cash will be met by borrowing. 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, also known as internal borrowing.

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 has struck a balance between cheaper variable rate short-term loans and long-term fixed rate loans where the future cost is known but often higher. The Council continues to weigh up this balance and evaluates the market to maintain affordability, certainty, and flexibility in its borrowing. The Council takes external professional advice on interest rates and Treasury Management from advisors Arlingclose to help inform this Strategy.

Projected levels of the Council's total outstanding net borrowing are shown below, compared with the CFR. The difference between the two being the level of internal borrowing used by the Council. This represents the use of reserves, working capital and revenue financing to offset the need to borrow.

Table 5 – Prudential Indicator – Gross Borrowing and the Capital Financing Requirement

Gross Borrowing & the Capital Financing Requirement	2023/24 Actual £'000	2024/25 Forecast £'000	2025/26 Budget £'000	2026/27 Budget £'000	2027/28 Budget £'000
Gross Borrowing	577,051	617,468	666,840	779,448	797,710
CFR	602,474	642,892	692,264	804,872	823,134

Statutory guidance is that gross borrowing should remain below the CFR, except in the short term. Table 5 demonstrates that the Council expects to comply with this into the medium term.

To compare the Council's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing. This assumes that treasury investments are kept to a minimum level of £16.4M to maintain liquidity at each year end. This benchmark is forecast to be £667M for 2025/26 and is forecast to rise over the following three years as capital expenditure is incurred.

Table 6 – Liability Benchmark

Liability Benchmark	2023/24 Actual £'000	2024/25 Forecast £'000	2025/26 Budget £'000	2026/27 Budget £'000	2027/28 Budget £'000
Secured Borrowing	583,006	580,000	350,000	290,000	230,000
Liability Benchmark	583,006	612,321	667,308	782,490	813,134
Borrowing Required	n/a	32,321	317,308	492,490	583,134

The table shows that the Council expects to borrow below its liability benchmark, representing a need to borrow as short-term loans become due for renewal in the future. This strategy should maintain a lower cost of borrowing through the financing of short-term loans but does show the refinancing risk this introduces the Council to. This risk is mitigated by the Council's ongoing access to the PWLB, and the liquid short term local authority to local authority borrowing market, allowing access to refinance borrowing as it becomes repayable.

More detail on the liability benchmark can be found in the Treasury Management Strategy.

The Council is legally obliged to set an affordable borrowing limit each year. In line with statutory guidance, a lower operational boundary for borrowing is also set at £10M below the authorised limit, as a warning level should borrowing begin to approach the limit. As the Council approves capital schemes throughout the year, this limit is updated and reviewed regularly and reported to Cabinet for approval by Council alongside Community Investment Programme approvals.

Table 7 – Prudential Indicator - Authorised limit and Operational Boundary for External Borrowing

Authorised Limit for External Borrowing	2023/24 Actual £'000	2024/25 Forecast £'000	2025/26 Budget £'000	2026/27 Budget £'000	2027/28 Budget £'000
Borrowing	601,474	641,892	691,264	803,872	822,134
Other Long-Term Liabilities	1,000	1,000	1,000	1,000	1,000
Total Authorised Limit	**602,474**	**642,892**	**692,264**	**804,872**	**823,134**

Operational Boundary for External Borrowing	2023/24 Actual £'000	2024/25 Forecast £'000	2025/26 Budget £'000	2026/27 Budget £'000	2027/28 Budget £'000
Borrowing	591,474	631,892	681,264	793,872	812,134
Other Long-Term Liabilities	1,000	1,000	1,000	1,000	1,000
Total Operational Boundary	**592,474**	**632,892**	**682,264**	**794,872**	**813,134**

Investments

Treasury Investments arise from receiving cash before it is paid out again. Investments made for service reasons or for financial gain are not generally considered to be treasury investments.

The Council's policy on treasury investments is to prioritise security and liquidity over yield, focusing 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 high-quality banks, to minimise the risk of loss.

Money that will be held longer term is invested more widely, to balance the risk of loss against the risk of receiving returns below inflation. Both near-term and longer-term investments may be held in pooled funds. In this instance an external Fund Manager makes decisions on which particular investments to buy and the Council may request its money back at short notice.

Table 8 - Treasury management investments

Treasury Investments	2023/24 Actual £'000	2024/25 Forecast £'000	2025/26 Budget £'000	2026/27 Budget £'000	2027/28 Budget £'000
Near-term Investments	18,800	16,400	16,400	16,400	16,400
Longer-term Investments	10,000	10,000	10,000	10,000	10,000
Total	**28,800**	**26,400**	**26,400**	**26,400**	**26,400**

The effective management and control of risk are prime objectives of the Council's treasury management activities. The Treasury Management Strategy sets out various indicators and limits to constrain the risk of unexpected losses and details the extent to which financial derivatives may be used to manage treasury risks.

The Council delegates responsibility for the monitoring and scrutiny of its Treasury Management practices and activity to the Treasury Management Review Group (TMRG), which includes Councillors and the Chief Financial Officer, and delegates responsibility for the implementation and administration of Treasury Management policies, strategies, and practices to the Council's Chief Financial Officer. The Council also employs an external advisor, Arlingclose, to provide advice on how the Council can manage its investment and borrowing portfolio.

Investments for service purposes are where the Council may choose to assist local public services by making loans to, or purchasing shares in, local service providers, or businesses to promote economic growth, or to help enable Council objectives externally, such as by lending money to a housing developer to provide additional housing that would not be provided by the open market. Considering the public service objective, the Council is willing to take more risk than with treasury investments. However, it still plans for such investments to break-even or generate a surplus after all costs.

Decisions on service investments are made by the relevant Service Director in consultation with the Chief Financial Officer and must meet the criteria limits laid down in the Investment Strategy. Most loans and shares are capital expenditure and investments and purchases will therefore also need approval by Cabinet as part of the CIP.

Cabinet are requested to recommend that Council approve the Investment Strategy which is contained within the separate Investment Strategy report.

Investment Governance

With central government financial support for local public services declining, the Council has made investments in property and housing to meet corporate objectives for Regeneration, Economic, Environment, Service Delivery and Housing Development and achievement of income to support efficiencies, to enable it to continue to provide high quality local services.

Due to the nature of these transactions, there is a higher risk, bringing with it a higher return. To mitigate the risk, the Council has developed a governance structure to allow it to carry out additional due diligence on these investments.

The governance of investments is split into two main areas, considering current investments that may be deemed surplus to requirements, and considering new investment.

In respect of current investments, a continual review of properties owned by the Council that are no longer of use, or coming towards the end of their lease period, is carried out. To facilitate this, the Council will carry out best value options appraisals on each asset to determine the next course of action. Within these options will be the option to sell the asset to realise a capital receipt, which would be used to repay borrowing, and therefore reduce financing costs. This will be balanced against the outstanding borrowing attributed to the property, to allow a comparison to be made between capital gains or losses that could be realised or utilised to reduce borrowing upon sale, versus foregone future revenue income that could be achieved should the property be refurbished, redeveloped, or re-let.

After this stage, governance is as follows:

The first stage of assessing the business case for ongoing ownership or investment into an existing or new commercial property is to understand the tenant covenant strength of any potential or current tenant, i.e. their ability to pay rent as it becomes due. This will be assessed through the internal knowledge of the Asset Management Team, external use of agents to assess the market, and credit checks on potential tenants. Meetings are held with the senior management of potential tenants of large value properties alongside a detailed review of their accounting statements.

Similarly with a housing scheme, the Council will look at areas such as underlying land and property values, to determine, should there be complications with a scheme, whether the Council would still be able to sell or develop the land in a different way to achieve the same objectives. For example, with the One Horton Heath development, there are options both to sell land parcels to developers, and to self-deliver the site, to ensure financial flexibility on the scheme, whilst continuing to deliver desired outcomes.

In addition to security of the investment is the consideration of the financial business case. The Council has the ability to borrow for property investments, as long as this is not solely for yield, i.e. regeneration, and also for housing investments; therefore, the Council ensures that the rental income from the tenants exceeds the borrowing costs and repayment of borrowing (MRP) applicable to the investment, or similarly the sale of the completed assets will be higher than the capital outlay should the assets be sold prior to being used by the Council.

To ensure that the financial business case is resilient and as low risk as possible, the Council sets aside three additional costs for assets it will keep in its portfolio: an interest rate adjustment, a void adjustment, and a maintenance adjustment. As the Council borrows at a variable rate for its commercial activity, the Council charges an interest adjustment on each property. This is where, although the Council predominantly borrows at cheaper variable rates, any financial business case is charged at higher long-term rates. This ensures should interest rates rise in the future, the Council has factored in the risk of higher future borrowing costs within the business case.

The Council also charges a void adjustment to each business case. This reserves a percentage of the income from each property so that when the initial lease period expires, the Council has funds set aside to mitigate the loss of income and void costs such as Business Rates or Council Tax for up to 12 months should a tenant decide not to renew a lease, leaving the Council having to find a new tenant. For housing developments, this is an allowance to cover the possibility of a void period between tenancy agreements. This adjustment is transferred to the property or housing reserve which are earmarked reserves held to ensure a future loss of tenant does not affect the Council's ability to provide services.

The Council also has a similar maintenance reserve, where, depending on the age and condition of the building, between 5% and 10% of all income is reserved each year to cover future maintenance works to the buildings. This Maintenance Reserve can then be used to fund the Repairs and Renewals Programme managed by the Property Team. For Housing schemes, this will again be transferred to a similar Housing Reserve and will be calculated accordingly to ensure regular maintenance and major repairs can be funded from this reserve.

In the case of affordable housing assets being transferred to the Housing Revenue Account (HRA) in the future, arrangements will be put in place within the HRA to cover these elements.

Decisions on property investments are also subject to additional levels of officer scrutiny, through meetings between members of the Corporate Leadership Board, Asset Management, Project Delivery, Housing, Development Management, Legal Services, the Monitoring Officer and Financial Services. These meetings consider the due diligence that has been carried out, and scrutinise financial business cases to ensure potential investments deliver value for money and will deliver against Council priorities.

For both housing and commercial schemes, there is an additional board structure in place which has councillor attendance, for final scrutiny.

The use of external advisers is also utilised at all stages where appropriate.

After all due diligence has been completed, property purchases are then treated as capital expenditure, and will therefore be put forward for approval as part of the CIP.

Table 9 – Prudential Indicator – Estimates of net income from commercial and service investments compared to budgeted net revenue stream

Income from non-treasury investments to net revenue stream	2023/24 Actual £'000	2024/25 Forecast £'000	2025/26 Budget £'000	2026/27 Budget £'000	2027/28 Budget £'000
Income/Savings generated by schemes funded by borrowing	20,374	20,685	19,459	20,751	20,646
Proportion of net revenue stream	**115%**	**137%**	**125%**	**139%**	**144%**

Further information on investments is covered in more detail within the Investment Strategy.

Revenue Budget Implications

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 of revenue spend funded by Council Tax, Business Rates and general Government Grants.

Table 10 – Prudential Indicator - Proportion of financing costs to net revenue stream

Financing costs compared to net revenue stream	2023/24 Actual £'000	2024/25 Forecast £'000	2025/26 Budget £'000	2026/27 Budget £'000	2027/28 Budget £'000
Financing Costs	18,878	23,071	21,073	21,500	22,409
Proportion of net revenue stream	**106%**	**153%**	**135%**	**144%**	**156%**

The table above shows that the Council is forecast to spend more on financing costs than on revenue spend net of financing costs by the end of the forecast period, this does not reflect the annual income that these investments have bought into the Council to spend on services, as can be seen in Table 11 below.

Table 11 – Revenue Surplus from Capital Financing

Financing costs compared to income generated	2023/24 Actual £'000	2024/25 Forecast £'000	2025/26 Budget £'000	2026/27 Budget £'000	2027/28 Budget £'000
Financing Costs	18,878	23,071	21,073	21,500	22,410
Income/Savings generated by schemes funded by borrowing	20,374	20,685	19,459	20,751	20,646

Annual Surplus	**1,496**	**(2,386)**	**(1,614)**	**(749)**	**(1,764)**

The surplus from income reduces to a deficit from 2024/25 which is predominantly due to an increase in interest costs in these years, and reductions in property income. Both of these are funded from reserve, either via the General Fund or the Investment Property Reserve. Active treasury management, as discussed in the Treasury Management Strategy looks to mitigate and reduce interest costs where possible, whereas the upcoming asset management strategy will look to address the performance of commercial assets to reduce the impact of any void buildings on the income being received by the Council.

Further details on the revenue implications of capital expenditure are discussed in the 2025/26 Revenue Budget.

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 CFO is satisfied that subject to continued effective Treasury Management, the effective monitoring of business plans and the successful implementation of the revised asset strategy, the proposed capital programme is prudent, affordable and sustainable. The process of effectively managing assets through monitoring approved business plans and utilising earmarked reserves where appropriate mitigates impacts of economic viability and is integral to the ongoing success of this Strategy.

Knowledge and Skills

The Council employs qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. The team includes:

- A Finance Team with five CIPFA qualified accountants, all with over ten years of experience in Local Government accounting, two CIMA and one ACCA qualified Accountant.

- An Asset Management Team including a number of Chartered Surveyors with over 10 years' experience who are members of the Royal Institution of Chartered Surveyors (RICS). They are regulated by their professional body (RICS) and comply with the RICS rules in relation to conduct and Continuing Professional Development. They maintain their knowledge and skills through regular technical updates from appropriate bodies.

- A Legal Team with one qualified barrister, two qualified solicitors, one trainee legal executive, and two solicitor apprentices. This includes three people with over 10 years in Local Government, two with extensive planning experience and two with substantial regulatory and governance backgrounds.

Where Council staff do not have the knowledge and skills required, use is made of external advisers and consultants that are specialists in their field. The Council currently employs Arlingclose Limited as Treasury Management Advisers and takes advice from external property and legal advisors where appropriate. This approach is often more cost effective than employing such staff directly and ensures that the Council has access to knowledge and skills commensurate with its risk appetite.

Further details on staff skills and knowledge, as well as external advisers can be found in the Investment Strategy report.