Appendix G4

Investment Strategy Report 2020/21

Introduction

The Council invests its money for three broad purposes:

- because it has surplus cash as a result of its day-to-day activities, for example when income is received in advance of expenditure (known as **treasury management investments**),
- to support local public services by lending to or buying shares in other organisations (**service investments**), and
- to earn investment income (known as **commercial investments** where this is the main purpose).

This investment strategy meets the requirements of statutory guidance issued by the government in January 2018, and focuses on the second and third of these categories.

Treasury Management Investments

The Council typically receives its income in cash (e.g. from taxes and grants) before it pays for its expenditure in cash (e.g. through payroll and invoices). It also holds reserves for future expenditure and collects local taxes on behalf of other local authorities and central government. These activities, plus the timing of borrowing decisions, lead to a cash surplus which is invested in accordance with guidance from the Chartered Institute of Public Finance and Accountancy. The balance of treasury management investments is expected to average £75m during the 2020/21 financial year.

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

Further details: Full details of the Council's policies and its plan for 2020/21 for treasury management investments are covered in a separate document, the treasury management strategy (**Appendices G1-G3**).

Service Investments: Loans

Contribution:

The Council has lent £50k to its wholly owned subsidiary, Islington Limited (iCo), at an interest rate of 5% per annum. iCo provides local services and raises revenue for the Council. The loan serves to support the working capital of iCo where the timings of its payments and receipts do not coincide. In addition, as at 31.03.2019, the Council had lent £717k (including accrued interest) to three private companies responsible for managing schools under the Building Schools for the Future programme (Transform Islington Phase 1 Holdings Limited, Transform Islington Phase 2 Holdings Limited and Transform Islington Limited). All loans were issued at market rates.

Where loans are advanced at below market rates they are classed as 'Soft Loans'. As at 31.03.2019 the council had also issued around £0.9m of soft loans, mainly to employees (e.g. travel season ticket, gym membership, home computer loans).

Security: The main risk when making service loans is that the borrower will be unable to repay the principal lent and/or the interest due. In order to limit this risk, the Council ensures its exposure to service loans remains proportionate to the size of the Council. The value of the iCo loan does not expose the Council to undue risk, and the Council regularly monitors the performance of iCo to ensure it remains capable of repaying the loan. The Building Schools for the Future loans are long standing and part of the overall agreed funding model of the programme. The various soft loans, mainly to staff, are repaid through deductions from salaries.

Accounting standards require the Council to set aside loss allowance for loans, reflecting the likelihood of non-payment. The figures for loans in the Council's Statement of Accounts from 2018/19 onwards are shown net of this loss allowance. However, the Council makes every reasonable effort to collect the full sum lent and has appropriate credit control arrangements in place to recover overdue repayments.

Risk assessment: The Council assesses the risk of loss before entering into and whilst holding service loans. In relation to iCo, the Council has representation (2 councillors and 2 senior officers) on the board and regularly monitors performance and financial risks.

Service Investments: Shares

Contribution: The Council holds equity investments in Islington Limited (iCo), a wholly owned subsidiary providing local services, and minority (10%) equity investments in three private companies responsible for managing schools under the Building Schools for the Future programme (Transform Islington Phase 1 Holdings Limited, Transform Islington Phase 2 Holdings Limited and Transform Islington Limited). The fair value of these shares is nil and the shares are not traded in an active market. The Council has no current plans to dispose any of these shareholdings.

Security: One of the risks of investing in shares is that they fall in value meaning that the initial outlay may not be recovered. Normally, in order to limit this upper limits on the sum invested in each category of shares would be set. However, this is not considered applicable by the Council due to the nature of the shares held, their low value in the 2018/19 Statement of the Accounts (£83.7k for Transform Islington Limited and nil for all others) and the fact that there are no current plans to increase shareholdings.

Risk assessment: The Council assesses the risk of loss before entering into and whilst holding shares, but has no current plans to purchase any new shareholdings.

Liquidity: Liquidity risk is considered low due to the nature of the shares held, their low value in the 2018/19 Statement of the Accounts (£83.7k for Transform Islington Limited and nil for all others) and the service reasons for holding the shares over the long term.

Non-specified Investments: Shares are the only investment type that the Council has identified that meets the definition of a non-specified investment in the government guidance. The Council has not adopted any procedures for determining further categories of non-specified investment since none are likely to meet the definition.

Commercial Investments: Property

Contribution: The Council holds a long-held portfolio of investment properties (mainly retail and office space) with the intention of generating a net income stream to fund local services. The market value of all such properties as at 31.03.2019 was £32.7m. The Council has not purchased new commercial properties in recent years nor does it have any plans to do so over the medium term. In 2018/19, rental income from investment property was £2.5m against direct operating expenditure arising from investment property of £1.1m.

Additionally, although not strictly investment properties, the Council's housing new build programme includes the building of private dwellings to sell on the open market. The upfront costs of building these private dwellings is funded by temporary borrowing for cash flow purposes, to be recouped by the capital receipts when the completed units are sold. These capital receipts also contribute to the funding of the wider new build programme of social housing.

In 2020/21 there is forecast capital expenditure of £12.1m on the building of such private dwellings, of which £10.9m will be funded from temporary borrowing (on top of £6.1m such temporary borrowing forecast to be brought forward from previous years). This cumulative temporary borrowing of £17.0m is currently forecast to be repaid in full by the end of 2021/22 from the estimated capital receipts.

Security: In accordance with government guidance, the Council considers a property investment to be secure if its accounting valuation is at or higher than its purchase cost including taxes and transaction costs.

A fair value assessment of the Council's investment property portfolio has been made within the past twelve months, and the underlying assets provide security for capital investment. Should the 2019/20 year end accounts preparation and audit process value these properties below their purchase cost, then an updated investment strategy will be presented to full council detailing the impact of the loss on the security of investments and any revenue consequences arising therefrom.

Liquidity: Compared with other investment types, property is relatively difficult to sell and convert to cash at short notice, and can take a considerable period to sell in certain market conditions. To ensure that the invested funds can be accessed when they are needed, for example to repay capital borrowed, the Council ensures dwellings are of a type and location that is marketable and has proven demand. The Council also has scope to continue to generate an income stream whilst they are being marketed.

Risk assessment: The Council assesses the risk of loss before entering into and whilst holding property investments. The Council has no current plans to purchase new investment properties.

Loan Commitments and Financial Guarantees

Although not strictly counted as investments, since no money has exchanged hands yet, loan commitments and financial guarantees carry similar risks to the Council and are included here for completeness.

The Council has provided a guarantee to its wholly owned subsidiary, Islington Limited (iCo), should it request it. There is currently no indication that this is likely to happen. The net current liabilities of iCo as at 31.03.2019 were £0.2m.

Proportionality

Whilst the Council is dependent on some profit generating investment activity from treasury management and commercial property investments to achieve a balanced revenue budget, this amounts to less than 0.5% of the overall gross revenue budget and therefore is considered proportionate. The assumptions around profit generating investment activity are reviewed as part of the annual budget monitoring process and, if necessary, revised as part of the following year's budget setting process.

In particular, commercial property income target assumptions are currently being reviewed to ensure that they reflect latest known plans over the MTFS period. This will feed into the next refresh of budget assumptions at the outset of the 2020/21 budget setting process.

The 2020/21 revenue budget includes a corporate contingency budget of £5.4m to mitigate against budget risks.

Capacity, Skills and Culture

Elected members and statutory officers: There are a number of procedures and processes that enable elected members and statutory officers to make appropriate investment decisions, including:

- All elected members and statutory officers are aware of the Council's strategic objectives.
- Training on treasury management is available and can be tailored to needs.
- The Council's constitution and financial regulations determine the authorisations required for investment decisions.
- Financial and legal implications (including statutory and regulatory frameworks) are required as part of all decision-making reports.
- The Council has a multi-disciplinary governance process for reviewing budget proposals, including any future commercial investment proposals.
- Specialist external advice is sought and considered where it is deemed necessary.
- The Council has an embedded risk management and reporting framework.

Commercial deals: Financial and legal implications (including statutory and regulatory frameworks) are required as part of all decision-making reports. Specialist external advice is sought where appropriate to advise on commercial transactions. The Council ensures external advisors are fully aware of the prudential framework and of the regulatory regime within which it operates.

Investment Indicators

The Council has set the following indicators to allow elected members and the public to assess the Council's total risk exposure as a result of its investment decisions.

Total risk exposure: The first indicator shows the Council's total exposure to potential investment losses. This includes amounts the Council is contractually committed to lend but have yet to be drawn down and guarantees the Council has issued over third party loans. In the absence of other information, it is assumed that non treasury management investments remain at the same value as in the 2018/19 Statement of Accounts given that there are no current plans to increase/decrease these investments. The future investment exposure will however be affected by valuations in the Statement of Accounts, particularly in relation to investment properties.

Total investment exposure in £millions

Total investment exposure	31.03.2019 Actual	31.03.2020 Forecast	31.03.2021 Forecast
Treasury management investments	96.2	75.0	75.0

Service investments: Loans	1.7	1.7	1.7
Service investments: Shares	0.1	0.1	0.1
Commercial investments: Property	32.7	32.7	32.7
TOTAL INVESTMENTS	130.7	109.5	109.5
Commitments to lend	0.2	0.2	0.2
TOTAL EXPOSURE	130.9	109.7	109.7

How investments are funded: Government guidance is that these indicators should include how investments are funded. Since the Council does not normally associate particular assets with particular liabilities, this guidance is difficult to comply with. It is assumed that the Council's investments are funded by usable reserves and income received in advance of expenditure.

Rate of return received: This indicator shows the investment income received less the associated costs, including the cost of borrowing where appropriate, as a proportion of the sum initially invested. Only the rate of return on treasury investments and commercial property investments are included in the table below. The rate of return on all other investments (e.g. service loans/shares) is considered immaterial. For consistency, fair value revaluation gains have been excluded as estimated valuations gains are currently not available for 2019/20 and 2020/21.

Investment rate of return

Investments net rate of return	**2018/19 Actual**	**2019/20 Forecast**	**2020/21 Forecast**
Treasury management investments	0.62%	1.01%	1.25%
Commercial investments: property	4.30%	4.30%	5.20%