Appendix F2: Capital Strategy Report 2024/25

1. Introduction

1.1. This capital strategy report 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.

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

1.3. The introduction of IFRS16: Leases from 1 April 2024 will have an impact on the Council's prudential indicators. A report will be presented to members at a subsequent date with amounts for the IFRS16 impact.

2. Capital Expenditure and Financing

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

2.2. In 2024/25, the Authority is planning capital expenditure of £1,157.736m over the 10-year budgeting period as summarised below:

Table 1: Prudential Indicator: Estimates of Capital Expenditure (£m)

	2022/23 actual	2023/24 forecast	2024/25 budget	2025/26 budget	2026/27 budget	Total 3 Year Budget	2027/28-2033/24 budget	Total 10 Year Budget
General Fund services	33.494	68.084	91.669	75.045	78.452	**245.166**	85.606	**330.772**
Council Housing (HRA)	119.411	167.574	238.741	109.637	97.336	**445.714**	381.250	**826.964**
TOTAL	**152.905**	**235.658**	**330.409**	**184.682**	**175.788**	**690.880**	**466.857**	**1157.736**

Table 2: Capital Expenditure 2024/25 to 2033/34 summarised by Strategic Priority

Strategic Priority	2024/25 £m	2025/26 £m	2026/27 £m	2024/25 - 2026/27 Total £m	2027/28 - 2033/34 £m	Total 10 Year Plan £m
A Safe Place to Call Home	260.375	154.266	137.878	552.519	388.067	940.585
Child-Friendly Islington	11.573	3.862	3.628	19.063	8.400	27.463
Community Wealth Building	15.943	16.703	21.519	54.165	21.690	75.855
Fairer Together	1.000	1.000	1.150	3.150	0.000	3.150
Greener, Healthier Islington	41.518	8.851	11.614	61.983	48.700	110.683
Total	**330.409**	**184.682**	**175.788**	**690.880**	**466.857**	**1157.736**

2.3. The bullet points below detail some of the key projects in the capital programme with their 10-year budget and strategic priority:

Safe Place to Call Home

- Finsbury Leisure Centre New Build - £56.208m: delivering new affordable housing alongside the wider redevelopment of Finsbury Leisure Centre.
- Thriving Neighbourhoods Scheme - £12.015m: investment to improve local areas based on ideas put forward by local people to improve shared spaces on estates.
- HRA Major Works and Improvement - £583.771m: ongoing investment in council homes and estates, including cyclical improvements, mechanical and electrical works, fire safety and energy efficiency improvements to maintain safe homes for residents.

Child Friendly Islington

- Schools Condition Schemes - £16.369m: investment to ensure the Borough's schools remain in a good and safe condition for children to attend.

Community Wealth Building

- Compliance and Modernisation - £17.033m: continuous investment in the Council's non-housing estate to ensure and maintain compliance with the appropriate statutory, regulatory and corporate standards.
- Highways - £17.179m: investment in the structural maintenance of highway infrastructure including carriageways, footways and drainage to fulfil the statutory duty to maintain the highway in a fit state to accommodate the ordinary expected to pass along them.

Greener, Healthier Islington

- Energy Decarbonisation Schemes - £21.384m: ongoing investment to enhance assets and deliver the Council's strategy 'Vision 2030 Building a Net Zero Carbon Islington by 2030' by reducing emissions and improving energy efficiency. This includes £12.852m to be used as match funding to accept decarbonisation grant offers. If grant funding offers are not received or accepted, the budget will be subject to review.
- People Friendly Streets - £25.793m: investment to improve the environmental impact of the highway network through development of liveable neighbourhoods, low traffic neighbourhoods and school streets.
- Vehicle Replacement - £29.867m: investment to replace vehicles with newer Euro 6/ULEZ compliant and electric vehicles.
- Sobell Leisure Centre - £7.000m: investment at the site following a flood which will be covered by insurance. These works are expected to be completed in 2024/25.
- Ironmonger Row Baths - £7.000m: investment following a fire at the site which will be covered by insurance. These works are expected to be completed in 2023/24.

2.4. The Housing Revenue Account (HRA) is a ring-fenced account which ensures that council housing does not subsidise, or is itself subsidised, by other local services. HRA capital expenditure is therefore recorded separately and includes the building of 956 new homes over the forecast period.

Governance:

2.5. Oversight and governance of the capital programme is supported by a comprehensive framework of advisory boards with member and officer involvement:

- The Corporate Asset Delivery Board (CADB), comprised of officers and members, is accountable for the overall delivery of the corporate asset strategy, with oversight of all material asset and capital related decisions. It reviews the 10-year capital strategy and supporting annual programmes, subject to formal budget approval.

- The Housing Delivery Board, comprised of officers and members, integrates governance of new homes delivery and major works across the council's existing stock.
- The Borough Investment Panel, comprised of officers and members, is accountable for recommending approval of all CIL/s106 investment decisions and spend oversight.
- A series of Directorate level programme delivery boards, comprised of officers, are accountable for all other asset development and capital programme activity and linked to wider Directorate governance arrangements.

2.6. In relation to the annual capital programme, service managers submit capital submission bid requests annually to include projects in the authority's capital programme. Bids are collated by corporate finance who calculate the financing cost (which can be nil if the project is fully externally financed) and assess the overall affordability of the capital programme. This includes an assessment of the revenue implications of the projects as part of the revenue budget setting process.

2.7. An assurance and prioritisation exercise is then undertaken, assessing capital projects against their contribution to council priorities and their deliverability. The prioritisation process supports the council in making decisions about which project to progress, especially in an environment of challenging financial resources. All bids are appraised at Corporate Management Board who then make recommendations to members. The final capital programme is then presented to the Executive in January and to council in February/March each year.

2.8. For full details of the Authority's capital programme, see Capital Programme 2024/25 to 2033/34 **(Appendix F1)**.

Risks:

2.9. Inflation rates provide a risk to the delivery of the capital programme to budget. If inflation rises, the cost of materials and labour will increase which can lead to overspends within the capital programme. This risk will be mitigated to some extent by contingency built into scheme budgets.

2.10. Increasing interest rates in turn increase the revenue impact of borrowing to fund the capital programme. **Table 3** below provides sensitivity analysis to model the impact of a 1% change in interest rates.

Table 3: Impact of 1% Interest Rate Change

1% Interest Rate Change	2024/25 £m	2025/26 £m	2026/27 £m	2027/28 – 2033/24 £m	Total £m
General Fund	0.552	0.376	0.291	0.497	**1.716**
HRA	1.420	0.797	0.352	0.327	**2.897**
Total	**1.972**	**1.173**	**0.643**	**0.825**	**4.613**

2.11. The funding of some capital schemes is linked to delivery of the scheme's asset. There are risks in the assumptions made around this funding. There may be timing differences between expenditure being incurred and receipt of the funding, particularly regarding housing open market sale properties. In these instances, alternative interim funding will be applied such as short-term borrowing, with additional short-term revenue cost implications to cover interest costs and MRP, or the use of HRA reserves. There may also be differences in the value of receipt assumed and actual receipt. Receipts in excess of the assumed amount can be applied elsewhere by the Council, including to reduce external borrowing requirements. Receipts less than the assumed amount will increase the borrowing requirement and the associated revenue costs. Over the next 10 years, £118.609m of General Fund capital financing is assumed to come from the open market sales of completed housing projects.

2.12. Another commercial risk is the supply chain. The financial health of our current suppliers needs to be assessed regularly to minimise the risk of supplier insolvency which will have significant impact on the delivery and affordability of the projects. Due to cost-of-living crisis, many suppliers are in difficult situations, and it is important that robust contract management strategies are in place to highlight any potential issues. To mitigate the risk of supplier insolvency, all current and future contracts are being reviewed by the Assurance Team and Finance and the correct indexation is applied, ensuring value for money but also supporting the supplier. All new tenders are subject to financial appraisal, making sure companies certify the ‘Going Concern’ requirement.

2.13. To set the capital programme, budget holders and project managers have informed the profiling of budgets based on their expectation of project delivery timescales. It is typical for there to be slippage in the capital programme where works delivered, and so spend incurred, fall below what is expected at budget setting. Robust budget monitoring in-year will identify where these slippages are occurring and with timely raising and reporting, management actions can be taken to manage capital financing, including adjusting the borrowing requirements and associated revenue charges.

Financing:

2.14. All capital expenditure must be financed, either from external sources (government grants and other contributions), the Authority’s own resources (revenue, reserves and capital receipts) or debt (borrowing, leasing and Private Finance Initiative).

2.15. The main sources of capital funding the council uses are summarised below:

- Capital Grants: predominantly government grants and are usually provided to the council for the specific use of funding capital expenditure for certain schemes and programmes (e.g. Department for Education funding for schools’ condition works).
- Section 106/CIL: developer contributions towards infrastructure; Section 106 contributions relate to specific projects and outcomes.
- Capital receipts: when a capital asset is no longer needed, it may be sold so that the proceeds, known as capital receipts, can be spent on new assets or to repay debt. The council primarily generates capital receipts from the open market sale homes used to finance the building of the council homes.
- Other capital contributions: specific contributions received for projects from third parties who may have a specific output or benefit achieved through the capital works the council is providing (e.g. landlord/tenant contributions to modernisation works).
- Revenue contributions: direct revenue contributions towards capital expenditure, a minimal source of funding due to pressures on the revenue budget.
- HRA Reserves: direct funding from the HRA to support its capital programme through the use of the Major Repairs Reserve and revenue contribution to capital works.
- Borrowing: typically, Public Works Loan Board (PWLB) loans to support capital expenditure. This form of capital funding has revenue implications (i.e. interest and provision to pay back loan) which are accounted for as part of the budget setting process.

The planned financing of the above expenditure is as follows:

Table 4: Capital financing (£m)

	2022/23 actual	2023/24 forecast	2024/25 budget	2025/26 budget	2026/27 budget	Total 3 Year Budget	2027/28-2033/34 budget	Total 10 Year Budget
General Fund								
Grants	4.374	10.203	13.140	4.142	4.141	21.423	11.104	32.527
S106/CIL	2.477	11.034	3.542	0.000	1.276	4.818	0.600	5.418
Capital Receipts	15.682	7.942	20.081	44.629	40.541	105.251	5.416	110.667
Revenue Contributions and Other	0.000	8.422	5.470	0.560	0.000	6.030	1.500	7.530
Borrowing	10.961	30.483	49.436	25.714	32.494	107.644	66.986	174.630
Total General Fund	**33.494**	**68.084**	**91.669**	**75.045**	**78.452**	**245.166**	**85.606**	**330.772**
HRA								
Grants	24.961	31.706	57.801	0.000	0.000	57.801	0.000	57.801
S106/CIL	5.476	5.391	7.652	3.200	0.000	10.852	0.000	10.852
Capital Receipts	9.376	28.231	26.060	46.588	25.423	98.071	21.315	119.386
Revenue Contributions and Other	58.266	24.559	18.590	29.033	32.326	79.949	334.056	414.005
Borrowing	21.332	77.687	128.638	30.816	39.587	199.041	25.880	224.920
Total HRA	**119.411**	**167.574**	**238.741**	**109.637**	**97.336**	**445.714**	**381.251**	**826.964**
TOTAL	**152.905**	**235.658**	**330.410**	**184.682**	**175.788**	**690.880**	**466.857**	**1157.736**

2.16. Debt is only a temporary source of finance, since loans and leases must be repaid, and this is therefore replaced over time by other financing, usually from revenue which is known as minimum revenue provision (MRP). Alternatively, proceeds from selling capital assets (known as capital receipts) may be used to replace debt finance. Planned MRP and use of capital receipts are as follows:

Table 5: Replacement of prior years' debt finance (£m)

	2022/23 actual	2023/24 forecast	2024/25 budget	2025/26 budget	2026/27 budget
Minimum revenue provision (MRP)	3.767	4.731	6.266	8.721	9.511
Repayment of PFI/ Leases	3.472	4.454	4.872	5.272	5.587
TOTAL	**7.239**	**9.185**	**11.138**	**13.993**	**15.098**

2.17. For the Authority's full Minimum Revenue Provision Statement see MRP Policy Statement **(Appendix F5).**

2.18. The Authority's cumulative outstanding amount of debt finance is measured by the capital financing requirement (CFR). This increases with new debt-financed capital expenditure and reduces with MRP and capital receipts used to replace debt. The CFR is expected to increase by £155.052m during 2024/25. Based on the above figures for expenditure and financing, the Authority's estimated CFR is as follows:

Table 6: Prudential Indicator: Estimates of Capital Financing Requirement (£m)

	31/03/2023 actual	31/03/2024 forecast	31/03/2025 budget *	31/03/2026 budget	31/03/2027 budget
General Fund services	190.702	216.454	259.625	276.618	299.600
Housing Revenue Account	463.593	541.280	669.918	700.734	740.321
PFI Liabilities	80.552	76.098	71.226	65.954	60.367
TOTAL CFR	**734.847**	**833.832**	**1000.769**	**1043.306**	**1100.288**

Asset Management:

2.19. To ensure that capital assets continue to be of long-term use, the Authority has a Strategic Asset Management Strategy (SAMP). The SAMP is currently being updated and is scheduled to be re-published in Summer 2024.

Asset Disposals:

2.20. When a capital asset is no longer needed, it may be sold so that the proceeds, known as capital receipts, can be spent on new assets or to repay debt. The Authority is currently also permitted to spend capital receipts "flexibly" on service transformation projects until 2025/26. The Authority's Flexible Use of Capital Receipts Policy can be seen in **Appendix F6**. Repayments of capital grants, loans and investments also generate capital receipts. The Authority plans to receive £38.408m of capital receipts in the coming financial year as follows:

Table 7: Capital receipts receivable (£m)

	2022/23 actual	2023/24 forecast	2024/25 budget	2025/26 budget	2026/27 budget	Total 3 Year Budget	2027/28-2033/34 budget	Total 10 Year Budget
Right to Buy (Gross)	20.235	11.717	12.417	12.813	13.221	**38.451**	105.116	**143.567**
Open Market Sales	9.035	22.829	18.359	19.746	-	**38.105**	121.331	**159.436**
Non-Right to Buy Sales	1.931	7.632	7.632	7.632	7.632	**22.896**	-	**22.896**
TOTAL	**31.201**	**42.178**	**38.408**	**40.191**	**20.853**	**99.452**	**226.447**	**325.899**

3. Treasury Management

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

3.2. Due to decisions taken in the past, the Authority had £267.5m borrowing at an average interest rate of 4.05% and £74.2m treasury investments at an average rate of 4.56% as at 30.09.2024.

Borrowing Strategy:

3.3. The Authority'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 Authority therefore seeks to strike a balance between cheaper short-term loans and long-term fixed rate loans where the future cost is known but higher.

3.4. The Authority does not borrow to invest for the primary purpose of financial return and therefore retains full access to the Public Works Loans Board.

3.5. Projected levels of the Authority's total outstanding debt, which comprises borrowing, PFI liabilities, leases and transferred debt, are shown below, compared with the capital financing requirement shown in **Table 4**.

Table 8: Prudential Indicator: Gross Debt and the Capital Financing Requirement (£m)

	31.3.2023 actual	31.3.2024 forecast	31.3.2025 budget	31.3.2026 budget	31.3.2027 budget
Debt (incl. PFI & leases)	285.606	302.544	273.876	255.208	249.873
Capital Financing Requirement	734.847	833.832	1000.769	1043.306	1100.288

3.6. Statutory guidance is that debt should remain below the capital financing requirement, except in the short-term. The Authority expects to comply with this in the medium term.

Liability Benchmark:

3.7. To compare the Authority's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing. This assumes that cash and investment balances are kept to a minimum level of £10.000m at each year-end. This benchmark is currently forecast to be £373.369m at 31.03.2024 and is forecast to rise to £681.069m over the next three years.

Table 9: Borrowing and the Liability Benchmark (£m)

	31.3.2023 actual	31.3.2024 forecast	31.3.2025 budget	31.3.2026 budget	31.3.2027 budget
Outstanding borrowing	285.606	302.544	273.876	255.208	249.873
Liability benchmark	241.906	374.564	569.367	625.831	692.951

3.8. The table shows that the Authority expects to remain borrowed below its liability benchmark.

Affordable Borrowing Limit:

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

Table 10: Prudential Indicators: Authorised limit and operational boundary for external debt (£m)

	2023/24 limit	2024/25 limit	2025/26 limit	2026/27 limit
Authorised limit – borrowing	533.860	924.543	972.352	1034.921
Authorised limit – PFI and leases	74.973	76.226	70.954	65.367
Authorised limit – total external debt	**608.833**	**1000.769**	**1043.306**	**1100.288**
Operational boundary – borrowing	383.393	493.029	515.891	562.637
Operational boundary – PFI and leases	74.973	71.226	65.954	60.367
Operational boundary – total external debt	**458.366**	**564.255**	**581.845**	**623.004**

3.10. Further details on borrowing are available in the Treasury Management Strategy (**Appendix F4**)

Treasury Investment Strategy:

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

3.12. The Authority's policy on treasury investments is to prioritise security and liquidity over yield, that is to focus on minimising risk rather than maximising returns. Cash that is likely to be spent in the near term is invested securely, for example with the government, other local authorities or selected high-quality banks, to minimise the risk of loss. Money that will be held for longer terms is invested more widely, including in bonds, shares and property, 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, where an external fund manager makes decisions on which particular investments to buy and the Authority may request its money back at short notice.

Table 11: Treasury management investments (£m)

	31.3.2023 actual	31.3.2024 forecast	31.3.2025 budget	31.3.2026 budget	31.3.2027 budget
Near-term investments	43.700	72.020	295.491	370.623	443.078
Longer-term investments	10.000	10.000	10.000	10.000	10.000
TOTAL	**53.700**	**82.020**	**305.491**	**380.623**	**453.078**

3.13. Further details are available in the Treasury Management Strategy (**Appendix F4**).

Risk Management:

3.14. The effective management and control of risk are prime objectives of the Authority's treasury management activities. The treasury management strategy therefore 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.

3.15. The treasury management prudential indicators are available in the Treasury Management Strategy (**Appendix F4**).

Governance:

3.16. Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Director of Finance and staff, who must act in line with the Treasury

Management Strategy approved by Council. Reports on treasury management activity are presented to the Executive and Full Council.

4. Investments for Service Purposes

4.1. The Authority makes investments to assist local public services, including making loans to and buying shares in local service providers, local small businesses to promote economic growth, the Authority's subsidiaries that provide services.

4.2. Total investments for service purposes are currently valued at £2m with the largest being soft loans to employees of £1.202m providing a net return after all costs of 0%. There is also loans to and equity investments in:

- Three private companies responsible for managing schools under the Building Schools for the Future programme (a loan of £0.639m);
- A local charity (a loan of £0.078m);
- Equity investment in a private company responsible for managing schools under the Building Schools for the Future programme (fair value of £0.081m)

Governance:

4.3. Decisions on service investments are made by the relevant service manager in consultation with the Director of Finance and must meet the criteria and limits laid down in the investment strategy. Most loans and shares are capital expenditure and purchases will therefore also be approved as part of the capital programme.

4.4. Further details on service investments are available in the Investment Strategy (**Appendix F3**).

5. Commercial Activities

5.1. The council hold investment property (with a value of £43.648m as at 31/03/2023) in order to generate income to spend on services in Islington. The council has consistently taken a prudent approach to this – no new commercial properties have been purchased in recent years and there are no current plans to invest in commercial properties over the medium term. In November 2020 PWLB guidance was updated and PWLB loans are no longer available to local authorities planning to buy investment assets primarily for yield. The authority intends to avoid this activity in order to retain its access to PWLB loans.

5.2. The council also has a wholly owned subsidiary – Islington Limited (iCo), the purpose of which is to trade for profit with public bodies, private organisations and members of the public to provide a return to the council. The service provided by iCo where activities relate to municipal functions in which relevant expertise is held.

5.3. Decisions on commercial investments are to be made by senior officers in line with the criteria and limits approved by council in the Investment Strategy. Property and most other commercial investments are also capital expenditure.

5.4. Further details on commercial investments, limits on their use and the risk management are available in the Investment Strategy (**Appendix F3**).

6. Other Liabilities

6.1. In addition to forecast 31.03.2024 debt of £302.544m detailed above, the Authority is committed to making future payments to cover its pension fund deficit, £249m as at the last valuation setting contributions – 31st March 2019. The Council has also set aside provisions to cover probable liabilities that can be measured reliably. The most significant of these are the NNDR appeals provision, £11.522m as at 31/03/2023, and the insurance fund provision of £16.345m as at 31/03/2023. The insurance fund provision covers anticipated liabilities for

Errors and Omissions, Libel and Slander, Motor (Third Party), Employers' Liability, Public Liability, Fire and other risks – up to a specific limit for any one claim. External policies cover claims in excess of these limits.

Governance:

6.2. Decisions on incurring new discretional liabilities are taken by service managers in consultation with the Director of Finance and Director of Resources/Section 151 Officer. The risk of liabilities crystallising and requiring payment is monitored by corporate finance and reported as part of the annual closing of accounts process and as appropriate during the financial year. Corporate risks and risk management are also reported to Executive.

6.3. Further details on liabilities and guarantees are available in the 2022/23 Statement of Accounts.

7. Revenue Budget Implications

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

Table 12: Prudential Indicator: Proportion of financing costs to net revenue stream

	2023/24 forecast	2024/25 budget *	2025/26 budget	2026/27 budget
Financing costs (£m)	14.032	17.575	21.891	24.050
Proportion of net revenue stream	5.4%	6.5%	7.1%	7.2%

Sustainability:

7.2. 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 many years into the future. The Section 151 Officer is satisfied that the proposed capital programme is prudent, affordable and sustainable because revenue costs of borrowing have been fully incorporated in the 2024/25 revenue budget and MTFS. Additionally, the council is moving towards the development of a ten-year capital programme, and indicative requirements to 2033/34 are known. This enhanced long term budgetary planning will continue to be developed.

8. Knowledge and Skills

8.1. The Authority employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. The Authority pays for junior staff to study towards relevant professional qualifications including CIPFA (Chartered Institute of Public Finance and Accountancy).

8.2. Where Authority staff do not have the knowledge and skills required, use is made of external advisers and consultants that are specialists in their field. The Authority currently employs Arlingclose Limited as treasury management advisers. This approach is more cost effective than employing such staff directly and ensures that the Authority has access to knowledge and skills commensurate with its risk appetite.