CAPITAL STRATEGY 2024-25 – 2033-34

Introduction and background

1. This capital strategy is an overarching document which sets the policy framework for the development, management and monitoring of capital investment. The strategy focuses on core principles that underpin the council's capital programme; its short, medium and long-term objectives; the key issues and risks that will impact the delivery of the programme and the governance framework required to ensure the capital programme is delivered providing value for money for residents of Southwark.

2. The capital strategy aligns with the priorities set out in the Council Delivery Plan and other key council strategies. The strategy is integrated with the medium-term financial strategy (MTFS) and treasury management strategy.

Core principles that underpin the capital programme

3. The key principles for the capital programme are summarised below:

   - Capital investment decisions reflect the aspirations and priorities included within the Council Delivery Plan and supporting strategies;
   - Schemes to be added to the capital programme will be subject to a gateway process, prioritised according to availability of resources and scheme specific funding, council priorities and commitments and factors such as legal obligations, health and safety considerations and the longer term impact on the council's financial position;
   - The cost of financing capital schemes, net of revenue benefits, are profiled over the lifetime of each scheme and incorporated into the annual policy and resources strategy and budget;
   - Commissioning and procuring for capital schemes will comply with the requirements set out in the council's constitution, financial regulations and contract standing orders.

4. Risk review is an important aspect of the consideration of any proposed capital or investment proposal. The risks will be considered in line with the council's risk management strategy and commensurate with the council's low risk appetite. Subject to careful due diligence, the council may consider a moderately higher level of risk for strategic initiatives, where there is a direct gain to the council's revenues or the ability to deliver its statutory duties more effectively and efficiently.

Governance framework

5. The council's constitution requires council assembly to agree the capital strategy and programme at least once every four years (last one was in 2022) and in the event of a significant change in circumstances. The reports from the chief finance officer will consider the compliance of proposed schemes in the programme with the medium term financial strategy, the capital resources

available to the council, the revenue implications of the proposed capital expenditure, and any other relevant information.

6. Democratic decision-making and scrutiny processes provide overall political direction and ensure accountability for investment in the capital programme. These processes include:

- Council assembly approves the Council Delivery Plan which sets out the strategic priorities for the council;
- Council assembly is ultimately responsible for approving the capital strategy, treasury management strategy and capital programme;
- Cabinet receives regular capital monitoring reports, approves variations to the programme and considers new bids for inclusion in the capital programme;
- Portfolio holders are assigned projects in line with their responsibilities;
- Scrutiny committees can call in cabinet reports, receive and scrutinise reports;
- All projects progressing to the capital programme follow the constitution, and financial regulations;
- The capital programme and capital expenditure is subject to internal and external audit.

7. Cabinet agreed in October 2023 to develop a refreshed set of governance proposals to ensure that all future capital bids remain affordable and in alignment with key council objectives.

8. The approach taken each year will be to assess the overall funding envelope, the affordability criteria, which will be determined by the estimated capital funding available and within a predetermined and prudent limit on borrowing.

9. New capital bids from council departments will require a business case with ‘sign off’ from the respective member of the Corporate Management Team (CMT). A newly established capital board will prioritise the bids and ensure that they can be funded within the pre-defined funding envelope. It is expected that the panel will meet at least twice a year.

10. The final list of bids will be considered by the Corporate Management Team (CMT) ahead of cabinet approval.

11. Approval to spend on individual capital schemes will only be given once procedural guidelines have been complied with and assessed to the satisfaction of the Strategic Director of Finance.

12. Senior officer teams exist within directorates to monitor the delivery of the directorate capital programme. Directorate management teams must consider and recommend all additions, variations to their directorate capital programme before being agreed by the Strategic Director of Finance, and then by cabinet.

Capital investment priorities and plans

13. The capital programme for the council is a long-term ambition, with the lifetime of new and existing assets stretching far into the future. The obligation for maintaining and improving council dwellings and operational buildings is very long-term and as such will be considered accordingly in financial and asset management planning.

14. Capital investment plans are driven by the council delivery plan the council's key strategic document that sets out the council's vision, ambitions, values and priorities. Cabinet approved the 2022-2026 '*Fairer Greener Safer Southwark – Council Delivery Plan*' in September 2022, and that it would be referred to as the council delivery plan.

15. The plan is centred on seven separate themes:

- transforming the borough,
- a thriving and inclusive economy,
- a healthy environment,
- quality, affordable homes,
- keeping residents safe,
- investing in communities,
- supporting families.

16. The application and planning for capital expenditure obligations and objectives should be considered over short, medium and long-term time horizons. Long term forecasts are not easily predicted and the accuracy of all financial estimates will be limited. However, long term forecasting is critical to informing strategic plans taking account of the sustainability and affordability of existing and planned investment, which will need to be repaid over future periods.

17. For all projects and investments, the funding and financial implications need to be planned well in advance. The council maintains an approved capital programme that covers a ten-year period. Prudential indicators for capital expenditure and financing are set out in Appendix E.

Treasury management

18. 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, while a shortage of resources will be met by prudential 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.

19. Each year the council assembly agrees an annual treasury management strategy covering the management of council's debt and cash investments (Appendix B).

Asset management planning

20. Cabinet approved the current asset management plan in January 2021. The plan sets out the council's ambitions for existing stock and future investment decision-making. It was developed from the priorities set out in the council delivery plan and how the decisions that the council take around property can help to achieve these, prioritising climate change and recognising the hugely important role in providing and building stable communities.

21. The council's future asset management decision-making will follow a clear and robust process, ensuring that plans are affordable and decisions are aligned to corporate ambitions and are in the best interests of the Borough as a whole.

Commercial activity and investment property

22. Returns from property ownership can both be income driven (through the receipt of rent) and by way of appreciation of the underlying asset value (capital growth). The combination of these is considered in assessing the attractiveness of a property for acquisition. However, yield is rarely the sole or primary objective of property acquisitions.

23. Historically, property has provided strong investment returns in terms of capital growth and generation of stable income. However, property investment is not without risk as property values can fall as well as rise and changing economic conditions could cause tenants to leave with properties remaining vacant. The investment appraisal, external professional advice, local strategic knowledge (ensuring all investments are in Southwark) and risk assessment ensure that commercial investments remain proportionate to the size of the council and that the revenue impact can be managed, should expected yields not arise.

24. The strategy makes it clear that the council will continue to invest prudently to take advantage of opportunities as they present themselves, supported by our robust governance process.

25. The council is mindful that Public Works Loan Board (PWLB) loans are not available to local authorities planning to buy investment assets primarily for yield.

Loans and other liabilities

26. The council has discretion to make loans for a number of reasons, primarily for economic development. These loans are treated as capital expenditure.

27. By advancing loans to other bodies, the council is exposing itself to the risk that the borrower defaults on repayments. The council must therefore ensure that these loans are prudent and that the risk implications have been fully considered, and that the cumulative exposure of the council is proportionate and prudent.

28. The council will ensure that a full due diligence exercise is undertaken and adequate security is in place. The business case will balance the benefits and risks. All loans are agreed by cabinet and will be subject to close, regular monitoring.

29. In addition to debt liabilities set out in the treasury management strategy, the council is committed to making future payments to cover any pension deficit. The pension fund is subject to a triennial valuation and the revenue implications are built into the MTFS.

Revenue budget implications

30. Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and the Minimum Revenue Provision (MRP) or voluntary debt repayment in Housing Revenue Account (HRA) are charged to revenue as financing costs. This is then compared to the net revenue stream (Appendix E).

31. 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 up to 50 years into the future. Capital investment decision-making is not only about ensuring that the initial allocation of capital funds meets corporate and service priorities but also ensuring that the asset is fully utilised, sustainable and affordable throughout its whole life.

32. This overarching commitment to long- term affordability is a key principle in any capital investment-appraisal decision. In approving the inclusion of schemes and projects within the capital programme, the Strategic Director of Finance must be satisfied that the proposed capital programme is prudent, affordable and sustainable.

Knowledge and skills

33. The council has professionally qualified staff across a range of disciplines including finance, legal and property that follow continuous professional development (CPD) and attend courses on an ongoing basis to keep abreast of new developments and skills.

34. The council establishes project teams from all the professional disciplines across the council as and when required. External professional advice is taken

where required and will always be sought in consideration of any major commercial property investment decision.

35. Internal and external training is provided for members to ensure they have up-to- date knowledge and expertise to understand and challenge capital and treasury decisions taken by the Strategic Director of Finance.