

Bolsover District Council

Executive

18th February 2019

<p>Commercial Property Investment Strategy</p>

Report of the Leader

This report is public.

Purpose of report

- To provide Executive with a draft Commercial Property Investment Strategy for consideration and approval.

1. Report Details

- 1.1 At its meeting on 5th November 2018, Executive considered a report detailing the financial pressures facing the Council including a summary of the measures being taken to maximise income, reduce costs and redesign services in line with the Transformation Programme. It was agreed that a further report would be provided to a future meeting setting out a draft commercial property investment strategy for approval.
- 1.2 In addition, on 3rd December 2018, Executive considered a report which contained a detailed analysis of the Council's existing non-housing property stock; setting out details of occupancy levels, voids, return rates and percentages, maintenance and capital depreciation costs, debt write offs, trends and demands.
- 1.3 Given the financial challenges faced, Executive have indicated a will to progress the development of an investment strategy for commercial property based around expanding its existing non-housing property portfolio. This is in order to develop revenue streams that provide a required level of return to offset the forecast budget deficits for forthcoming years. This approach can also support economic development and regeneration in the District through targeted investment.
- 1.4 It was agreed that, given the importance of ensuring that investment decisions to generate income are sound, it is important that the mechanisms for management of the Council's future budget deficit are properly understood. This is in order to ensure the extent and level of risk arising from any additional investment properly reflects the budget deficit that income generation is aiming to help address. Executive has, therefore been provided with the financial details required in order to make informed decisions in relation to future investments.

- 1.5 During the development of the draft Commercial Property Investment Strategy, a number of key factors were considered in order to shape an approach that ensures due diligence is undertaken. The strategy reflects the requirements within the ‘**Statutory Guidance on Local Government Investments**’ issued under Section 15(1) (a) of the Local Government Act 2003’, which came into force April 2018. Further details of this statutory guidance are available at:

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/678866/Guidance_on_local_government_investments.pdf

- 1.6 Table 2 below sets out a summary of the statutory guidance requirements to be covered in an investment strategy:

Table 2

Requirement	Considerations
Clearly show how investments contribute to Council’s objectives	<ul style="list-style-type: none"> • Need to align with Corporate Plan priorities • Clarify purpose and extent to which it supports deficit reduction and /or economic regeneration in the District
Strategy must include indicators to show how Councillors have assessed the total risk exposure on decision	<ul style="list-style-type: none"> • How is it funded • Rate of return expected and why (benchmarked) • Show additional debt costs • Risks over the repayment period • Extent of support for deficit gap • Mitigation if returns fail and / or borrowing increases • Assessment of capital depreciation
Clearly consider and demonstrate how the investment is proportionate to the overall financial position of the Council	<ul style="list-style-type: none"> • Loan corresponds in size or degree (terms/rate/returns) • Risk exposure is reasonable and accepted • Within agreed and defined ‘affordability’ limit
Risk assessment should be robust	<ul style="list-style-type: none"> • Market assessment (competition, demand, trends) • Proper quality external advice and expertise • Credit ratings
Contingency	<ul style="list-style-type: none"> • Loss of investment return / Increase in loan repayments • Capital depreciation • Extra costs and budget impact • Loss of revenue stream - service delivery impact

1.7 In developing the strategy, consideration has also been given to a number of essential elements which will inform acceptable investment choices, specifically:

- Ethical investment (for instance, prohibiting investment in alcohol and tobacco production or sale, animal exploitation, gambling, sex establishments, arms trade or environmentally damaging practices)
- Geographic spread of investments
- Limits of individual and cumulative risk
- Timescales for the achievement of objectives
- The level of losses that can be tolerated
- The degree to which the Council can realistically become reliant on the income stream to provide services

1.8 In addition to reflecting the statutory requirements and the essential elements to inform acceptable investment choices, the strategy should show how property investment choices will be considered. Therefore the strategy sets out the need to consider key factors such as:

- **Location** – location of the property is critical to ensure it is an attractive position, so that in the long term it optimises its ability to re-let/re-sell if capital is required, or is strategically located for re-development. The location of the property will affect the ability of the Council to undertake inspections and to deal with management issues without the need to employ specialist agents. It will also affect income to the Council from Business rates, Council Tax and New Homes Bonus, depending on the type of investment.
- **Covenant Strength** - the quality of the tenant and, more importantly, their ability to pay the rent on time and in full is essential. This is particularly important where the Council has borrowed against the investment, and minimum acceptable financial strength for any given tenant will be determined through a financial appraisal of company accounts and the use of appropriate methods of risk assessment and credit scoring. It is however worth noting that the Council, as a public body, may not wish to invest in properties where the occupiers are generally seen to be undertaking business which is contrary to its corporate values.
- **Lease length** - the unexpired length of the term of the lease is of key importance in ensuring that the landlord's revenue stream is secure and uninterrupted. The Council will take into consideration the risks associated with a tenant vacating and the potential to attract good quality replacements tenants at acceptable rental levels.

1.9 In order to assist with the decision making process and the assessment and appraisal of property investment opportunities the strategy includes a matrix to 'score' investment opportunities through an established criteria. This criteria has been weighted in order to score an opportunity on its 'acceptability' providing a first stage in determining if it should be further progressed. The matrix is included within the draft Commercial Property Investment Strategy at Appendix 1.

1.10 In addition to the application of the matrix and weighting mechanism there are a range of other factors which should be considered when appraising an investment opportunity and therefore have been reflected in the strategy. These are:

- **Risk** – any borrowing needs to balance against the risk of the return. In general, the higher the sought level of return from an investment, the higher level of risk that it carries. The intention of an investment strategy is to minimise the risk to the Council on any investment.
- **Growth** – property investments have the potential for both revenue and capital growth. The Council will take into account that potential when assessing the strength of the investment opportunity. However Property values can fall as well as rise and mechanisms to minimise revenue reductions should be identified. Monitoring and review of the portfolio and any anticipated trends, will be required given how the market can change over time.
- **Sector and trends** - information as to the sector of use of the property (e.g. office, retail, retail, warehousing, industrial, and leisure) and trends in demand will assist in deciding on the risks associated with specific properties and the mix of sectors within the portfolio.

2. Conclusions and recommendations

- 2.1 Understanding the performance of the Council's existing budget pressures and the performance of its existing non-housing property is essential in determining how future property investment opportunities should be approached. This information was, therefore, provided to Executive during its meetings on 5th November 2018 and 3rd December 2018 to enable it to give full consideration to areas of risk and reward within the management of existing stock and to determine and how well placed the Council is to expand its commercial property portfolio activity.
- 2.2 As set out in this report, the development of the strategy has required the consideration of a number of key issues to ensure it reflects the requirements of the statutory guidance and enables Councillors to make informed 'risk based' decisions. The draft Commercial Property Investment Strategy is attached at Appendix 1.

3. Consultation and Equality Impact

- 3.1 Budget Scrutiny considered the draft Commercial Property Investment Strategy at their meeting on 30th January 2019. A table of their comments and responses is attached at Appendix 3.
- 3.2 In addition, it should be noted that all future investment decisions will require consultation proportionate with the extent and nature of the proposal. Any investment decisions will require consideration by the Council of its legal duties to eliminate unlawful discrimination, advance equal opportunities and promote good relations between people. The Council will also need to ensure

when making financial investment decisions, that it considers the needs of all members of the community.

4. Alternative Options and Reasons for Rejection

- 4.1 An alternative option would be to not progress the development of a commercial property investment strategy and not consider other high level investment opportunities. Whilst this approach would limit any risks associated with the use of Council resources or additional borrowing for investment, it could restrict the ability to generate additional income or deliver key corporate priorities.

5. Implications

5.1 Financial and Risk implications

- 5.1.1 None directly from the report, however given the Council's financial position, future pressures and uncertainties, it is essential any investment decisions are fully and properly considered. The proposed strategy will help to ensure that when making decisions the Council can demonstrate compliance with the statutory expectations and evidence awareness of the risks and rewards.

5.2 Legal Implications including Data Protection

- 5.2.1 As set out the development of the Council's Commercial Property Investment Strategy will need to give due regard to the provisions contained within the Statutory Guidance on Local Government Investments issued under Section 15(1) (a) of the Local Government Act 2003. Legal and financial advice will be taken to ensure the strategy aligns with the requirements to prepare and publish an Annual Investment Strategy consistent with the Treasury Management Code principles. This advice will also ensure the strategy sufficiently reflects the importance of risk, ensuring gross debt is proportionate to net service expenditure, in order to prevent over-extension of investment activities.
- 5.2.2 Furthermore any future property investment decisions will need to be taken in line with the Council's established governance structure and provide a sufficiently robust evidence based business case.

5.3 Human Resource Implications

- 5.3.1 None directly from the report.

6. Recommendation

- 6.1 That Executive considers the draft Commercial Property Investment Strategy for approval.

7. Decision Information

<p>Is the decision a Key Decision? A Key Decision is an executive decision which has a significant impact on two or more District wards or which results in income or expenditure to the Council above the following thresholds: <i>BDC: Revenue - £75,000</i> <input type="checkbox"/> <i>Capital - £150,000</i> <input type="checkbox"/> <i>NEDDC: Revenue - £100,000</i> <input type="checkbox"/> <i>Capital - £250,000</i> <input type="checkbox"/> <input checked="" type="checkbox"/> <i>Please indicate which threshold applies</i></p>	No
<p>Is the decision subject to Call-In? (Only Key Decisions are subject to Call-In)</p>	No
<p>Has the relevant Portfolio Holder been informed</p>	Yes
<p>District Wards Affected</p>	All
<p>Links to Corporate Plan priorities or Policy Framework</p>	All

8 Document Information

Appendix No	Title
Appendix 1 Appendix 2 Appendix 3	Draft Commercial Property Investment Strategy includes Statutory Guidance on Local Government Investments Property Investment Matrix Budget Scrutiny comments 30/1/19
<p>Background Papers (These are unpublished works which have been relied on to a material extent when preparing the report. They must be listed in the section below. If the report is going to Cabinet (NEDDC) or Executive (BDC) you must provide copies of the background papers)</p>	
Statutory Guidance on Local Government Investments issued under Section 15(1) (a) of the Local Government Act 2003	
Report Author	Contact Number
Karen Hanson	7053