Cabinet

11 February 2021

Warwickshire Recovery and Investment Fund

Recommendations

That Cabinet:

1. Supports the Business Case at Appendix A to establish the Warwickshire Recovery and Investment Fund.

2. Approves in principle the establishment of a Warwickshire Recovery and Investment Fund (WRIF) and authorises the Strategic Director for Resources to finalise the proposals and the fund allocations and to develop the Year 1 Business Plan based on the principles set out in Section 1.11 of this report for further consideration by Cabinet.

3. Supports the proposed WRIF governance arrangements and approves the establishment of a Member Oversight Group and an Officer Investment Panel as more fully described in Section 7 of this report.

4. Notes that a further report will be brought back to Cabinet to approve the final arrangements, including the 2021-22 Business Plan and to ask Cabinet to consider making the recommendations to Council in respect of the changes considered necessary to the Treasury Management Strategy and the Investment Strategy and to add the WRIF loan facility to the capital programme.

1. Executive Summary

1.1 Following the Cabinet decision on 8th October 2020, officers have progressed consideration of the options related to the creation of a Warwickshire Recovery & Investment Fund (WRIF) to support the Council's strategic place shaping agenda and its recovery and regeneration strategies, particularly in light of very significant economic impacts brought to the fore by the COVID-19 pandemic. This report seeks the approval in principle of Cabinet to the establishment of the WRIF as recommended in the WRIF business case at Appendix A and the further development of the operational arrangements which will be brought back to Cabinet for consideration.

1.2 The proposal is that the WRIF operates as a 'closed fund', time limited for 5 years, after which there will be no further investments made unless it is decided by the Council that the WRIF is operating successfully and there is demand for it to continue. Any external contractual arrangements will not go beyond the 5 years (unless agreed in advance) and will have adequate break clauses to end the contract at stages before this.

Rationale for establishing the WRIF

1.3 The Council commissioned the economic and social development research and advisory company SQW to undertake research into the potential impact of Covid on the local economy and to forecast the potential impact by sector and into job losses and the recovery timescale of both. Their report (August 2020) which was considered by Cabinet on 8th October 2020 indicated that, in Warwickshire:

- There could be an increase in the number of unemployed people from 7,000 before the pandemic, to around 26,500, with potential further growth in subsequent phases of the pandemic response. When the second wave scenario was applied to the model, it resulted in a forecast of between 19,500 and 23,500 additional people out of work. Further waves will increase this number.
- Tourism is worth over £1 billion to the local economy and it employs over 20,000 people – approximately 6% of all employment in Warwickshire. VisitBritain's central scenario for inbound tourism to the UK in 2020, as of June 3rd, is for a decline of 59% in visits - to 16.8m - and 63% in spend - to £10.6bn. The pre-COVID forecast was for 25.3m visits and £19.7bn spend.[1]
- Sectors reliant upon in-person service delivery, such as retail, hospitality, leisure and recreation are particularly exposed as a result of the pandemic.
- Modelling demonstrates that potentially a third of the additional jobs lost in 2020 could be in food and beverage services, retail and accommodation, sectors that employ a large proportion of younger people, with the effects spread across the entire County.
- Alongside this, the number of jobs lost in manufacturing is also likely to be high. The model suggests there could be 1,700 – 1,800 job losses in automotive manufacturing.
- The model indicates a potential 12% loss in GVA for Warwickshire when the second wave scenario was applied.
- The results are particularly sensitive to the impacts on the automotive manufacturing sector and its supply chain. A significant drop in activity in this sector in 2020 is one of the reasons that GVA and employment in Warwickshire is expected to be hit harder than in the UK as a whole.

1.4 This SQW analysis has formed the foundation for the proposals for a WRIF, strengthened by the fact that the outlook for the local economy has, in all likelihood, worsened since the August 2020 report as a result of the extended period of national restrictions. A Business Case has therefore been developed by 31Ten, external specialists, setting out the case for the establishment of the WRIF. As a part of the Business Case development process, the options to establish a WRIF, or 'do nothing' (which includes investing through alternative Council initiatives or letting the market fill the gap), were assessed against the following criteria:

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[1] VisitBritain's 2020 tourism forecasts (last updated June 3rd 2020)

- ability to deliver the Council's Strategic Objectives;
- ability to support Warwickshire's post-COVID economic recovery in a targeted way;
- ability to support businesses, social enterprises and create jobs; and
- ability to generate financial returns that, as a minimum, cover cost but also provide a small return across the whole fund.

1.5 In recent years other Local Authorities have undertaken similar initiatives to further achievement of their organisational objectives. Examples include:

- Cardiff Capital Region Wider Investment Fund, which deploys £495m to achieve the core objectives of the Cardiff Region City Deal, including leveraging in £4bn of additional investment to create 25,000 jobs and a 5% uplift in Gross Value Added (GVA).

- Greater Manchester Investment Fund, which has invested £123m into over 110 businesses in Greater Manchester, creating/safeguarding over 7,450 jobs. The fund has leveraged private sector funds of approximately £1.1 billion.

- Kent County Council, which operates a Property Investment Fund, capped at £17m, which is aimed at supporting regeneration and the economy in the county.

1.6 The WRIF is closely aligned to the Council's strategic objectives; its establishment will provide a direct way of supporting delivery of the Council's strategic outcome 'Warwickshire's economy is vibrant and supported by the right jobs, training, skills and infrastructure' which will in turn help the Council deliver its second outcome relating to supporting Warwickshire's communities, while also making best use of resources. In a 'Do Nothing' option the delivery of strategic outcomes would be via other council initiatives, but some may be challenging to deliver in the context of the forecast impact of the pandemic on the local economy.

1.7 The existing investment market will support Warwickshire-based businesses but there is anticipated to be a growing and unmet demand for finance which may limit or delay economic recovery.

1.8 The WRIF has a specific focus on supporting Warwickshire based businesses, social enterprises and on creating jobs in the county. Existing funds within the regional market will have wider objectives than the Council's specific objectives and the WRIF will have a focussed commitment to providing funding specifically within Warwickshire. Economic forecasting indicates that WRIF will have a significant positive impact on the county's Gross Value Added (GVA) and employment and therefore there is a strong policy rationale for a direct and targeted approach, via the WRIF, to realise this positive impact.

1.9 The mechanism of the WRIF has been developed on the basis that it is intended to generate financial returns that as a minimum cover costs (principal, interest and overheads) and therefore is not exposing the Council to additional financial burden.

1.10 The WRIF business case, prepared by 31Ten on behalf of Warwickshire County Council, utilises the HM Treasury ‘Five Case’ model, which derives a full business case from separate component sections, comprising:

- Economic Case;
- Strategic Case;
- Commercial Case;
- Financial Case; and
- Management Case.

1.11 The WRIF business case sets out the full detail; however, in summary, the conclusions reached following the options appraisal are set out below. These form the principles on which the further work necessary to move to implementation of the WRIF will be developed:

a. there is a viable business case and clear policy rationale for the establishment of WRIF, using the Council’s strong balance sheet to make non-treasury investments in the county, which is preferable to a “do nothing” option;

b. the evidence of demand and the gap in the market supports the establishment of a flexible WRIF, targeting priority sectors for the county’s future, leveraging further external investment into Warwickshire, and driving social value, comprising three pillars aimed at:
   i. Growing existing businesses;
   ii. Supporting the creation of new and SME businesses; and
   iii. Property and infrastructure.

c. WRIF should be managed via a ‘mixed-economy’ of in-house and externally sourced expertise;

d. Robust governance and risk management arrangements should be put in place to secure the Council’s objectives whilst at the same time ensuring due diligence in relation to the Council’s investments, protecting the taxpayer and making appropriate use of public funds that reflects the Council’s fiduciary duties; and

e. The Council should consider investing up to £140m into WRIF over the 5 year period of the MTFS, with annual business plans setting the levels of investment for each individual year based on an assessment of the risk profile performance of the Fund during preceding years and setting the indicative allocations between the pillars. This is in addition to the £160m already proposed to be allocated to WPDC. If approved, this would bring the Council’s investment in place shaping and economic recovery to approximately £300m over a five year period, as set out in the Table below:

Draft Investment Profile

£m	2021/22	2022/23	2023/24	2024/25	2025/26	Cumulative
Business Growth Pillar - Capital	10.100	19.950	19.950	20.000	20.000	90.000
Local Communities Enterprise Pillar - Capital Loans	0.900	1.825	1.825	0.450	0.000	5.000
Local Communities Enterprise Pillar - Revenue Loans	0.900	1.825	1.825	0.450	0.000	5.000
Sub Total - BGIF and LCEF	11.900	23.600	23.600	20.900	20.000	100.000
Property - Non WPDC Investment	0.000	10.000	10.000	10.000	10.000	40.000
In Year Total - WRIF	11.900	33.600	33.600	30.900	30.000	140.000
£m	2021/22	2022/23	2023/24	2024/25	2025/26	Cumulative
Property - WPDC Equity	14.128	4.130	0.000	2.117	9.029	29.404
Property - WPDC Capital Loans	0.000	13.716	27.216	41.153	38.015	120.100
Property - WPDC Revenue Loans	0.556	1.007	0.718	1.813	4.382	8.476
In Year Total - WPDC	14.684	18.853	27.934	45.083	51.426	157.980
Split between Capital and Revenue (£m)	2021/22	2022/23	2023/24	2024/25	2025/26	Cumulative
Capital	25.128	49.621	58.991	73.720	77.044	284.504
Revenue	1.456	2.832	2.543	2.263	4.382	13.476
Total - WPDC and WRIF	26.584	52.453	61.534	75.983	81.426	297.980
£m	2021/22	2022/23	2023/24	2024/25	2025/26	
Cumulative Total Investment	26.584	79.037	140.571	216.554	297.980	

1.12 The £140m figure for investment in the WRIF is the upper limit set as affordable and reasonable to invest through the Treasury Management Strategy and the Investment Strategy. Together, the Treasury Management and Investment Strategies set the control limits for WRIF. They must be complied with in order to ensure that there is authority for the WRIF investments and that the operation of the WRIF is in compliance with all legal and financial requirements. Full Council will need to approve any required amendments to these Strategies before any WRIF business plan, approved by Cabinet can be implemented. This can happen as part of the annual approval of the strategies or in-year, if required. The modelling in the 31 Ten Business case has tested different funding profiles, which will be re-run when a final profile is recommended to Cabinet to consider prior to making a final decision on the business plan.

1.13 These and the other proposals made by the Business Case were tested by engagement with the market (see section 3 of this report) and evaluated by the Economy & Skills team based on their knowledge and experience of the current and anticipated economic landscape in light of the Covid pandemic.

1.14 There are significant benefits anticipated from that creation of the WRIF that align with the Council's priorities. These will:

- stimulate and accelerate economic growth/recovery by filling identified gaps and demand for finance by businesses;
- drive growth and productivity gains, with an estimated uplift in Gross Value Added of four times WCC's initial investment;
- unlock and secure new and additional private sector investment (c. £98m);
- generate a direct positive net return on the value invested;
- create new jobs in the county (c. 2,200+) and safeguard thousands (c. 4,000) more from redundancies;
- increase attractiveness of Warwickshire to new inward investment and business relocation; and
- safeguard and increase Business Rates and Council Tax base.

1.15 A performance framework will be developed and finalised for use by the proposed governance arrangements (see section 7 of this report) to monitor the WRIF and ensure that the potential benefits of it are realised to the maximum possible extent. The Business Case includes the following for consideration:

Benefit	Measures & Quantification
Support business and grow the economy; create the conditions for business innovation and investment to support business growth in growing sectors and drive economic growth.	Annual GVA / Value of GVA uplift to the County Number of new start-up businesses / businesses supported Business rates income Council Tax income County-wide equitable distribution of funding
Increase the rate of employment; investment stimulates job creation with an increase of skilled or entry level jobs in the County	Number of jobs created/ filled by unemployed Number of jobs safeguarded
Provides employment land and premises; investment addresses the lack of appropriate employment land and premises in the County	Sq ft of employment land and number of premises created
Creates Housing Growth; investment supports housing growth and infrastructure	Number of new homes, split by type
Enables Carbon reduction; investment in environmentally and/or economically sustainable businesses that are driving	An increase in the use of/public support for low and zero carbon technologies Number of responsible investments

Benefit	Measures & Quantification
climate change benefits, carbon neutral and low carbon initiatives	
Increases Social Value; investment brings benefits to local residents by promoting initiatives that increase skills and capabilities, remove barriers to employment, improve health and wellbeing, protect and enhance the natural environment, create better places to live and maximise opportunities to strengthen community capacity and resilience.	Poverty premium how many people's lives have they touched and households helped
Attracts inward investment; investment attracts new employers, increases employment and brings wealth into the local economy	Value of third party/private sector investment leverage
Enables development: investment unlocks the development potential of sites or kick starts stalled developments to quicken the pace of housing delivery and creation of employment land to support jobs	Number of brownfield sites remediated Sq ft of development
Improves connectivity; improves the county's infrastructure and connectivity to break down barriers to digital inclusivity	Increased network capacity

1.16 The remainder of this report provides context and key points from the business case document, to enable informed decision making and is structured as follows:

- background, including policy context and previous Cabinet decision making on the subject;
- business case development, including the market engagement exercises undertaken;
- the WRIF Business Case and WRIF configuration, including key features of the three proposed investment themes/sub-funds within the WRIF;
- the WRIF management;
- proposed WRIF governance;
- decision making and considerations of fiduciary duty;
- financial implications and risk mitigations of WRIF establishment;
- environmental implications of WRIF establishment; and
- Appendices, including WRIF Business Case full document.

1.17 Subject to Cabinet's decision on the recommendations before it today, a WRIF business plan for 2021-22, with more detailed proposals, will be presented to Cabinet for decision at the next appropriate meeting and thereafter to Council to approve the funding arrangements (the addition of the WRIF loan facility to the capital programme) and the changes that will be required to the Investment Strategy and the Treasury Management Strategy prior to the WRIF being launched.

2 Background

2.1 Further to a detailed report on the Council's Place Shaping programme in June 2020, Cabinet approved the investigation of the establishment of a recovery and investment fund for Warwickshire (the WRIF). In October 2020, Cabinet approved the principles, objectives and fund structure for WRIF based on independent economic research and requested a further report to Cabinet setting out a full business case confirming the proposals and viability of such a fund.

2.2 A Project Team consisting of Council officers and external advisors has since been working to build the business case that is included at Appendix A of this report.

2.3 It should be noted that changes to the Treasury and Investment Management Strategies and any additions to the capital programme which will require full Council approval are key enablers in the setup of the WRIF and, subject to Cabinet approval of the recommendations in this report, these changes will follow alongside the detailed Year 1 business plan and before any launch of the WRIF.

3.0 Business Case Development

Approach to development

3.1 The Business Case (at Appendix A) follows the Treasury 'Five Case' Model, which is structured under the following sections:

- **The Strategic Case**: makes the case for change, its context and outlines how the proposal fits with the wider policy and strategic objectives of the Council. This includes clarification of the WRIF objectives, structures, principles and strategic fit.

- **The Economic Case**: sets out the critical success factors and demonstrates that a range of potential options have been considered for achieving the strategic goals of the proposal and recommends a preferred option to deliver the proposal. This section includes market analysis and engagement, options appraisal, measurement of success and benefit realisation, WRIF investment criteria, economic risks.

- **The Commercial Case**: addresses commercial feasibility and seeks to answer the question "can the proposed solution be effectively delivered through a workable commercial deal or deals?"; it sets out the opportunity, the route to investment, the commercial terms and considerations that must be addressed in taking forward the preferred option.

- **The Financial Case**: presents financial data and the financial parameters set for the fund(s) and demonstrates the affordability of the proposal alongside funding sources. This section includes consideration of the fund size, funding sources, affordability, modelling, sensitivity analysis, accounting and risks.

- **The Management Case**: demonstrates whether the proposal is deliverable by setting out the governance structure, project planning, risk management and communication & engagement arrangements required to ensure successful delivery of a proposal. This section includes the proposal for the most appropriate model for fund management, governance, project planning and communication.

Market engagement

3.2 To complement and inform the business case development, market engagement was undertaken. The approach was to establish how the WRIF might align with existing investment funds in the region and the extent to which there is existing or potentially unmet demand for finance within the County. The market was also asked for its views on how the fund should be structured. This builds on research previously undertaken by Warwickshire County Council around the lack of availability of finance for businesses in the county, and the findings from the Midlands Engine Independent Economic Review which found that access to finance was a major barrier to growth for businesses in this region.

3.3 The first stage of market engagement involved informal conversations with the following organisations that operate in or have experience of the region:

- British Business Bank;
- Coventry & Warwickshire Reinvestment Trust;
- Mercia;
- Maven CP;
- BCRS;
- Ascension Ventures; and
- Finance Birmingham/Frontier Development Capital (FDC).

3.4 Feedback from the market engagement concluded that:

a) There is demand for finance from Warwickshire businesses: £12m of £85m invested by the MEIF (Midlands Engine Investment Fund) has been in Coventry & Warwickshire businesses. Fund managers all felt that additional capital targeted within Warwickshire would be beneficial.

b) Gaps exist in the regional market, as companies struggle to secure loans between £1.5m and £5m and other forms of capital and financing.

c) There is a need to keep the WRIF flexible and a need to avoid prescriptive lending and repayment terms. It was also considered important by the market to be able to flex the targeting of the fund, based on gaps and opportunities arising. Also, there was a sense that the fund should look at more innovative investment products, for example loan repayment holidays or debts converting to equity.

d) The WRIF proposals would be attractive to the existing market of fund managers. Several of them already have operations that they could utilise for the WRIF. Each fund manager had specific niche areas of operation, for example: start-ups; equity; loans; property; and mid-market SMEs. None of the fund managers spoken to had expertise in social enterprises.

e) All fund managers consulted were familiar with seeking investments that bring wider social benefits, such as job creation. However, for start-up businesses the view was that it is important to concentrate on achieving viability and then job creation will follow.

f) Most of the fund managers highlighted the need for additional support to businesses pre-investment. Suggestions varied but included: signposting and liaison across different funds; accelerator programmes; and incubator arrangements. This is recognised, and consideration is being given as to how the Council can support businesses in their applications for funding before applying for investment through existing teams, existing business support initiatives such as the Business Ready Programme, and through further investment in specialist advisors.

3.5 The outputs from the market engagement and the internal intelligence have been factored into the Business Case which has followed the Treasury Model in its approach. The development of the Business Case also reflects the requirements that a Local Authority establishing such a fund must consider and these aspects are set out in more detail in the sections which follow.

3.6 Informal conversations about WRIF have also been undertaken with key local business intermediary organisations, such as the Coventry & Warwickshire Chamber of Commerce, CWLEP and C&W Growth Hub; who have all endorsed the need for the WRIF and supported the concept given known current and expected future issues around the availability of finance for businesses.

4.0 The WRIF Business Case

4.1 The WRIF Business Case attached at Appendix A follows the Treasury ‘Five Case’ Model however this section provides a summary. At a headline level the Fund is intended to use Council cash funds to invest in Warwickshire businesses and developments by means of loans initially, but with the option to consider alternative types of funding products as the WRIF becomes more established and there is assurance that the Fund is delivering its strategic goals whilst at the same time delivering within the investment parameters set out in the Council’s Investment Strategy and Treasury Management Strategy.

4.2 The Business Case was developed against the strategic objectives and principles identified for the Fund and is based on the fund structure, all of which were approved by Cabinet in October 2020 and set out below:

Objectives

- Provide access to finance that helps businesses start, grow and scale up;

- Leverage additional resources or funding for the county through the investment and support of key growth businesses;
- Secure an ongoing financial return, commensurate with risk, for reinvestment to continue to deliver the benefits and outcomes sought from the Fund or other permitted activities;
- Make investments that deliver benefits in both in the short term (12 months) and medium term (1-5 years);and
- Support the delivery of the Council's strategic goals and priorities as set out in the Warwickshire Council Plan 2025, COVID-19 Recovery Plan, Economic Strategy, Commercial Strategy and Place Shaping Programme.

Principles

- Support County based businesses;
- Create a diversified and balanced portfolio of risk-based investments that protect the public purse, support business, create new jobs and protect existing ones;
- Manage risk and target full recovery of investments;
- Generating permitted financial returns for reinvestment into the Council and/or to continue to deliver benefits and outcomes set out in the WRIF objectives subject to a further business case;
- Provide a flexible tool to consider and enable a range of opportunities for supporting business;
- Provide targeted business support through investments based on agreed investment criteria and priorities that are developed from analysis of the economy and strategic sectors; investments will support key sectors and growth, rather than weaker sectors;
- A consistent and streamlined approach to considering investment opportunities and ensure all investment decisions are made against agreed investment criteria and align with Council priorities and outcomes; and
- Complement the existing investment landscape and other recovery packages.

Fund Structure

The Fund will be structured around three pillars as below:

- The business investment growth pillar – to focus on providing finance to growing businesses with sound prospects;
- The local communities and enterprise pillar – to focus on meeting local, smaller scale requirements for access to finance with the aim of maintaining social capital in communities, supporting new local small businesses and creating entry level jobs; and
- The property and infrastructure pillar – to enable development in the County, facilitating new employment land and commercial premises and which could also include investing in commercial sites and premises consistent with the needs of key sectors and/or wider ambitions for economic recovery.

WRIF Strategic Case

4.3 The Strategic Case situates the WRIF project within the broader strategic context faced by the Council. It references the following key policy and strategy documents of the Council, including:

- Council Plan;
- COVID 19 Recovery Plan;
- Economic Growth Strategy 2020 – 25;
- Emerging Capital Strategy 2020 – 2030 (draft);
- MTFS;
- Commercial Strategy;
- Voluntary and Community Sector Strategy;
- Local Industrial Strategy (West Midlands); and
- Coventry & West Midlands LEP Strategic Economic Plan (updated).

4.4 In particular the specific policy objectives / outcomes which the proposed WRIF is designed to support and deliver are as set out below (with further detail set out in Section 3 of the Business Case and supported by the SQW report):

- ‘Warwickshire’s economy is vibrant and supported by the right jobs, training, skills and infrastructure’ (Council Plan);

- ‘Support business and grow the economy: Build confidence in local businesses. Re-purpose town centres and create the conditions for business innovation and investment to drive economic growth’. (Recovery Plan);

- ‘Stimulate job creation and skills: Work with our partners in the Local Enterprise Partnership and higher and further education, to invest in getting people back into employment, or starting their careers, supporting skills, training and re-learning’ (Recovery Plan);

- ‘Invest in regeneration and a sustainable future: Invest in the regeneration of local areas, support housing growth, a fit for the future digital infrastructure and sustainable transport’ (Recovery Plan);

- ‘Make sustainability and tackling climate change central to our recovery so that we lay the foundations for a sustainable long-term future’ (Recovery Plan); and

- ‘Our ambition is for strong economic growth, with seven strategic priorities and particular focus given to four sectors: automotive technology, advanced manufacturing, digital creative/video game development, and tourism’ (Economic Growth Strategy).

WRIF Economic Case

4.5 The Economic Case assessed the way in which the WRIF could be delivered to best achieve the strategic goals of the Council Plan and Covid-19 Recovery Plan. It considered the following three elements in sequence:

- whether to continue with current approach (which includes a mix of WCC support, external financial markets and current investment framework to access public sector financial support) or establish a WRIF;
- how should the fund be structured – as a single fund or two or three funds; and
- how should the fund be managed – in-house, outsourced or mixed economy.

4.6 The primary issue to address is whether to establish a WRIF to support economic recovery or whether to continue with the Council's current approach to supporting local businesses, assessed against the policy objectives that the Council is seeking to deliver (set out at paragraph 4.2). The Business Case concludes that establishing a WRIF to complement the current approach is the preferred option. Section 4 (in particular the table at paragraph 142) of the Business Case sets out the analysis in more detail; however, a summary of the alternative options for delivery and why the establishment of a WRIF is considered the most appropriate solution to deliver the Council's policy objectives is set out below:

Options to deliver policy objectives	**Analysis**	
	Pros	**Cons**
Continue the Council's current approach and let market / other funds fill the gap	The Council is not exposed to risks arising from investment in gaps in the market.	Gaps for the provision of funding have been highlighted by market engagement and these gaps have not yet been addressed by market forces alone. Scale of economic challenge arising from pandemic would go unaddressed.
Scale up the Council's investments in the existing funds (CWRT, Coronavirus Business Interruption Loan Scheme (CBILS))	Existing arrangements in place and well established. Well understood and relatively low risk. Existing skills and expertise within the Council to enable this.	Missed opportunity to use alternative forms of investment to achieve a better return for the Council. Inability to apply the Council's own risk/reward criteria and controls to specific investments. Initiatives such as CBILS and CWRT are time-limited.

Deliver support through alternative/ new grant funding arrangements	Skills and expertise to achieve this delivery support are already available within the Council but may need additional resources. There is no need to secure additional internal and/or external expertise to achieve this.	Limited budgets to support grant programmes. Grants are 100% loss, whereas WRIF aims to recover its costs (the principa, interest and overheads) plus an overall small return. Missed opportunities to use alternative forms of investment to achieve a better return for the Council.
Establish WRIF	Existing funds do not offer direct alignment to WCC-specific policy objectives and investment principles (see para. 4.2). The WRIF will enable investment to be targeted at businesses in Warwickshire, support job creation and retention in a way that the current investment market is not supporting.	Set-up costs and heightened exposure to risk arising from use of new forms of investment.

4.7 In terms of the fund structure and fund management the Economic Case preferred options are set out below:

Fund structure

To establish a fund which comprises three pillars and allows maximum flexibility in its operations with the ability, on an annual basis, to flex the indicative fund allocations to meet demand. The rationale for this decision is:

- the three pillars match the findings of the economic analysis undertaken by SQW;
- the three pillars are sufficiently different in focus to allow different recipients/beneficiaries and different benefits to be targeted;
- investment criteria, governance and decision making can be tailored across the three-pillar structure in accordance with respective scale, type and risk of investment; this also allows for more effective risk management;
- a three-pillar structure allows specific gaps in the market to be targeted and also allows market differentiation, making the proposition more

attractive to Fund Managers with specific skills and experience in the Fund areas; and
  - a three-pillar structure, including a specific focus on enabling development via the Property & Infrastructure component, which enables accelerated development in the County.

Fund Management

- To establish a WRIF which adopts a mixed economy for fund management –the rationale for this is given in summary in Section 6 of this report and in detail in section 4 of the Business Case; and
- Further work will be undertaken by officers on the split of internal/ external fund management across the three pillars and how the arrangement would work in practice. This detailed work will be presented to Cabinet in the next report on the establishment of the WRIF.

<u>WRIF Commercial Case</u>

4.8 The Commercial Case recommends that there should be a blended approach to the management of the WRIF, utilising a combination of WCC internal resource and external resource. A mixed economy of fund management secures the advantages of external expertise, resource, capacity, and knowledge of sectors and the investment market but also provides the opportunity for involvement and control for the Council (in respect of internally managed funds), plus the opportunity for skills transfer.

4.9 It is proposed that a newly created internal team be established, operating alongside the existing business support programmes being delivered through the Council's Economy & Skills Team in the Communities Directorate, although it should be noted that resourcing of the WRIF is subject to further consideration before bringing a recommendation to Cabinet. The role of the newly created team, comprising Investment Manager(s) (IMs) and Business Advisor(s) (BAs), would potentially be as follows:

- promoting the programme to businesses and intermediary organisations, and as a vehicle to facilitate and encourage inward investment into the county within our key priority sectors;
- signposting appropriate potential applicants to the WRIF and supporting investor readiness;
- identifying investment opportunities that are in line with the WRIF Investment Strategy;
- developing sift documentation for investment opportunities;
- undertaking initial appraisal of the business, the investment opportunity, and an assessment of the leadership team within the business and their motivations and abilities
- being represented on the Investment Panel and presenting sift documents and applications for Investment Panel consideration;
- reporting on the financial and non-financial performance of individual investments of Funds under internal management;
- contract management and monitoring of External Fund Manager(s); and

- reporting on performance of WRIF portfolio overall.

4.10 The proposed in-house team would potentially be supported by a team of external advisors that will need to be sourced and/or recruited externally to the Council. Scope exists to appoint specialist external advisors either following a procurement process (using frameworks or stand-alone procurement exercise(s)) or alternatively via direct recruitment. It should be noted that resourcing of the WRIF is subject to further consideration before bringing a recommendation to Cabinet.

WRIF Financial Case

4.11 The Financial Case for the WRIF is set out in more detail in Section 9 of this report and has not been repeated in full here. However, the Financial Case concludes that proposals for the WRIF are affordable within the parameters of the Council's Treasury Management Strategy and Investment Strategy due to its annual business planning cycle and its flexibility that enables investment in various opportunities to manage and diversify risk and ensure that all costs are contained within the Fund. The WRIF Investment Strategy will ensure that the investment is aligned with strategic priorities and other agreed criteria.

WRIF Management Case

4.12 The key considerations in the Management Case include:
- The proposed WRIF governance structure – this is set out in more detail in section 7 below;
- Resourcing of the proposed internal team – see section 6, below; and
- The sourcing of external advisers and ICT solutions, where required.

4.13 Other considerations included in the Business Case that are not described elsewhere in this report include project planning (including indicative timescales), communication and engagement, indicative set up costs and the risk management strategy, all of which are subject to further consideration and development following Cabinet decision. The following table derived from the Business Case gives a summary of many of the key risks:

Risk	Mitigation
The public finance environment Changes to PWLB and other recent guidance from central government, particularly the Cipfa Prudential Code, is that Local Authorities are expected to be more considered when making investment decisions than previously permitted. This represents a risk to a purely commercial investment approach.	A business case is to be prepared for each individual investment decision (for internally managed funds) and a framework for investments will be developed (for externally managed funds) to demonstrate the economic, social and environmental benefits to be delivered via the investment in order to meet the current guidance, and consider compliance with the Prudential Code. This will need to be kept under close review.

HMT **Public Works Loan Board** – future lending terms November 2020 sets out that local authorities should not borrow primarily for yield or other speculative purposes.	The WRIF Strategy includes both financial and non-financial criteria for the assessment of investment opportunities and the business case will seek to show alignment with both to demonstrate that any borrowing is policy-driven and will not be solely for the purpose of yield
The restrictions in place on **access to PWLB**.	To be monitored and considered by the Investment Panel in relation to each investment opportunity on a case-by-case basis and in relation to the externally managed portfolio to ensure that the Council's wider borrowing power is not compromised.
Resources and Skills – A lack of available or suitable resources could result in delays to the establishment of the Investment Panel / procurement of external Fund Management services and consequently the sourcing of investment opportunities.	The marketing strategy and promotion of the opportunities of the Fund via the Council's own network will widen the potential pool of resources available to the Council. The Council can scale up the WRIF over time as resources are procured.
Benefit Realisation – the WRIF is unable to finance the number of investments anticipated or investments perform more poorly than anticipated and consequently the complete realisation of benefits is not achieved.	Regular monitoring of performance and benefit realisation by the Investment Panel through the life of the investment and at portfolio level. A clear exit strategy will be put in place to ensure that investments only remain live when delivering against the investment criteria agreed and future year's investments will taking into account previous performance.
Reputation - concerning liability surrounding investments, public perception of investments made and adhering to responsible and sustainable practice. Perception if funds underperform or the Council seeks to enforce against assets etc.	The marketing, communication & engagement strategy will be key to managing the public perception of the Fund. The contract for external fund managers will set the parameters for investment to mitigate this risk. The robust decision-making process for internal fund management will help mitigate this risk.
Investment performance - Higher levels of bad debt, higher default levels, lower levels of return and /or low market interest results in under	Sensitivity testing analysis has been undertaken to model the WRIF to demonstrate that overall investment performance can be achieved in a range of

performance of the WRIF and the Council losing money.	scenarios and via a diverse portfolio of investments. A number of crystallisation events will be created as milestones in the management of the WRIF that will ensure the Council covers its costs as a minimum. The flexibility of the WRIF with a portfolio approach will ensure a diversification of investments with a range of risk, return and types of investments to mitigate against underperformance.
Market Interest in the Fund is lower than expected causing a lower number of investment opportunities.	The focus and priority areas of the Fund are based on economic analysis of the likely needs of the local market. The bespoke forecasting tool should continue to be used to shape and update the WRIF Strategy to ensure it continues to reflect the market. The WRIF will only continue to operate if it has sufficient resource, expertise and experience to manage it.

5.0 The Proposed Fund Configuration

5.1 The proposal is that the WRIF is focussed on three pillars for investment:

- The business investment growth pillar – to focus on providing finance to growing businesses with sound prospects;
- The local communities and enterprise pillar – to focus on meeting local, smaller scale requirements for access to finance with the aim of maintaining social capital in communities, supporting new local small businesses and creating entry level jobs; and
- The property and infrastructure pillar – to utilise a range of possible property investments to deliver the Council's policy objectives with examples including commercial sites and premises to deliver new business premises to deliver and safeguard jobs, consistent with the needs of key sectors and the wider ambitions for economic recovery.

5.2 This configuration is in accordance with the recommendation of the SQW report and the fund structure proposals approved by Cabinet in October 2020 which identified demand for additional investment funding into these sectors to stimulate economic growth post Covid.

5.3 A table allowing comparison of the key features of each of the themes is included in the Business Case at Appendix A and the following sections summarise the proposed focus and priorities for each of the respective themes.

Business Investment Growth pillar

5.4 The pillar is focussed upon providing finance for growing businesses with sound prospects, operating in sectors where Warwickshire has particular strengths. The pillar will make investments <£10m per investment application, numbering approx. 2-5 per annum. Projects and investments that help implement greener operations will be a priority and there will be an overall focus on growth, rather than addressing the short-term effects of the pandemic; the intention is that this approach will help underpin medium and longer-term recovery. These requirements will be factored into the fund documentation and loan conditions.

5.5 The main drivers of this pillar will be:

- Supporting business and growing the economy;
- Increasing productivity and development of new market opportunities
- maximising the rate of employment;
- enabling carbon reduction; and
- improving social value, including employment, skills and protection of the natural environment.

5.6 The investment case for this pillar is derived from the market engagement with existing Funds which identified a gap in the market based on existing fund operations. The gaps this fund would be addressing as identified by the market engagement are:

- A scarcity of funding for Warwickshire businesses in the range of £1.5m to £5m debt that was highlighted by those we spoke to as part of the market engagement exercise;
- The problem of companies securing capital finance with a longer-term pay back in industries such as advanced manufacturing. The Council is able to take a wider and longer-term view of the impact of debt finance than a commercial organisation;
- Management Buy Out, acquisitions or refinancing options;
- The market engagement exercise confirmed that there is demand for a fund of this nature. However, it has not been possible to quantify this demand or assess the scale of finance that is required by Warwickshire-specific businesses as other current investment vehicles have a wider geographic remit; and
- The proposed size of the pillar has been determined based on the likely value of investments (£), considering market feedback, and the volume (number) of loans anticipated per annum over the 5-year life of the WRIF.

5.7 The priorities for investment in this pillar are intended to focus on investment opportunities that both stimulate job creation or retention of skilled or entry level jobs in the County and can/will leverage additional resources or funding into the county.

5.8 The priority sectors are those growing sectors where Warwickshire has particular strengths. Those sectors outlined in the Economic Strategy as priorities for economic growth in the County include;

- automotive technology;
- advanced manufacturing;

- digital creative/video game development;
- tourism;
- logistics;
- house building/modern methods of construction;
- ‘green’ /sustainable technologies or industries;
- rural industry and enterprise; and
- social care or other supply markets of the Council.

5.9 The priority sectors are not exclusive, and any sector will be considered if it meets the fund objectives and creates or retains skilled or entry level jobs.

Local Communities & Enterprise pillar

5.10 This pillar is aimed at directly addressing the local challenges, economic and social consequences of the pandemic, focusing on new business funding and meeting local smaller scale requirements for access to finance. The pillar will make investments <£1m, numbering approx. 10-30 or greater per annum. Due to the higher risk and specialist requirements associated with the proposed investments to be made by this pillar, we anticipate a need to procure external expertise to manage this fund. However, further consideration will be given to fund management and the detailed arrangements and will brought back to Cabinet in the next report on the WRIF. The fund has additional aims to maintain and build social capital in communities and to create entry level jobs, particularly for young people in Warwickshire.

5.11 The main drivers of this pillar will be:

- Promotion of additional employment by stimulating job creation and increasing skills;
- Supporting new business starts and early phase growth of small businesses;
- maintaining some of the County’s key social capital assets;
- improving town centers and high streets in Warwickshire; and
- the delivery of benefits in relation to climate change.

5.12 The investment case for this pillar is derived from market engagement which identified that within the space of the Local Communities & Enterprise Fund there is a gap in the market for some product types including:
- Debt finance for micro-businesses (<10 employees) and new start-ups;
- Start-up equity[2]; and
- Mezzanine finance[3].

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[2] Equity investment refers to buying shares in a company and thereafter holding those shares in order to gain an ownership interest that can be sold later to generate returns. Equity investments are a classic example of taking on higher risk of loss in return for potentially higher reward.
[3] Mezzanine financing is a hybrid of debt and equity financing that gives the lender the right to convert debt to an equity interest in the company

5.13 In addition, engagement also identified that the current supply of funding is considered insufficient to meet the high demands brought about by the current pandemic.

5.14 Whilst the market engagement exercise confirmed that there is demand in these areas, it has not been possible to quantify this demand or assess the scale of finance that is required by Warwickshire-specific businesses as other current investment vehicles have a wider geographic remit.

5.15 The market engagement did not identify any insights on the social enterprise space as the existing providers have no previous experience in it. This aspect of the fund is to be further tested during the second stage of the market engagement and included in the subsequent report to Cabinet.

5.16 The priorities for investment for this pillar are investment opportunities that:

- Stimulate job creation or retention of skilled or entry level jobs in the County;
- Support the development of new enterprises and business opportunities
- can leverage additional resources or funding; and
- increase social value.

5.17 It is not proposed that this pillar will operate on the basis of a priority sector focus. Instead focus will be given to investment opportunities that relate to Council policy priorities. Particular focus will be given to support the following priority business types:

- new and growing small and medium sized businesses;
- small, local businesses that support social capital;
- start-ups;
- social enterprises;
- environmentally and/or economically sustainable businesses that are driving climate change benefits, carbon neutral and low carbon initiatives;
- businesses that create entry level jobs and/or increase skills; and
- businesses where investment will improve high streets and town centres.

5.18 The priority business types are not exclusive, and all business types will be considered if the proposal meets the fund's objectives and creates or retains skilled or entry level jobs.

Property & Infrastructure pillar

5.19 The fund will provide loans to invest in commercial sites, premises and infrastructure, addressing the needs of key sectors and wider ambitions for economic recovery. The pillar aims for investment in viable developments that underpin medium and longer-term recovery, supporting growing business, rather than addressing the short-term effects of the pandemic. There is also scope for this pillar to support any future business cases brought forward by the Council or its Warwickshire Property and Development Company (WPDC) such as a ‘support to buy’ initiative , for example for key workers, however that would be subject to separate consideration and appropriate member approval; any such initiative would require further development before being considered for investment under this pillar.

5.20 The main drivers for this pillar will be:

- additional housing;
- additional employment land/premises and enhanced or accelerated infrastructure to support housing and employment growth, potentially through forward funding infrastructure schemes, investment in commercial sites and premises and by seeking to unlock stalled sites and development schemes;
- addressing the requirements of place making and regeneration; and
- unlocking employment land that will enable business growth.

5.21 The investment case for this pillar is derived from engagement with existing Funds which identified a gap in the market and indicated that this could be one of the fastest growing spaces for investment with a direct link to growth. There is an existing market for this type of finance; however, companies still struggle to get traditional finance for speculative developments i.e. land which is developed with no formal commitment from end users. However, no information was available on the demand for investment in this area from Warwickshire specific businesses.

5.22 The priority focus is on enabling development. The investment focus and beneficiaries of this fund are likely to be:

- developers, contractors and buyers of houses;
- developers of employment land;
- developers of office space;
- developers of operational business buildings;
- infrastructure projects; and
- occupiers of existing businesses.

6.0 The Proposed Fund Management arrangements

6.1 As set out above, the Economic Case recommended a hybrid approach to fund management. This means that some elements of the fund would be managed by the in-house team and some by externally appointed fund managers who have the necessary experience and expertise in managing a particular area of investment activity.

6.2 At this stage in the development of the proposals it has not yet been determined whether a single fund manager could deliver the Council’s strategic objectives or whether more than one fund manager would be required to provide sufficient coverage of the three investment pillars identified and to effectively manage risk.

6.3 At this stage the following gives an indication of how the different pillars of the fund are expected to be managed. However further work on this will be undertaken by officers and brought back to Cabinet for a decision at a subsequent Cabinet meeting, which will also consider the WRIF Year 1 business plan.

Pillar	Proposed Fund Management Arrangement
Business Growth	More likely to have internal management with option for external management at any later stage; and likely to have relationships with the existing British Business Bank and Midlands Engine Investment Fund.
Local Communities & Enterprise	Likely to be externally managed due to volume of work/administration; and likely to have a relationship with the existing Coventry & Warwickshire Investment Trust.
Property and Infrastructure	Likely to be internally managed with option to move to external management to get wider expertise, leverage private sector finance, etc.

6.4 External fund managers would be appointed following a procurement process(es). Members needs to recognise that where a fund is externally managed, the Council will be able to set investment parameters (the criteria, limits and requirements as based on the WRIF Investment Strategy) through the procurement process and those could be enshrined in the contract between the Council and the external fund managers. However, day to day investment decisions would be made by the external fund manager in line with the framework and criteria laid down by the Council.

7.0 Proposed WRIF Governance

Member decision making

7.1 The business case proposes that each year Cabinet considers and recommends to Council approval of the relevant annual budgeted amount for each WRIF pillar and sets out the authority within which to operate them, supported by an officer-led WRIF Investment Panel for the next year.

7.2 It is also envisaged that a specific WRIF Investment Strategy, containing objectives, priorities and investment criteria, is agreed by Cabinet on an annual basis, to ensure that funding is allocated within the parameters of appropriate criteria and in accordance with the agreed purposes. Whilst the intention is to run this scheme for the full 5 year period, a review at least on an annual basis as part of the MTFS and budget setting process will consider the continuation of the WRIF. This will incorporate a review of performance for the year just ended (and previous years), and in this way provides an annual continue/stop decision point. As such, this arrangement provides a crucial risk management control in that each new year will be planned in light of the experience and performance of previous years. There will be a ‘tail’ of investments to manage after any decision to stop further investments.

7.3 For the internally managed element of the Fund, it is envisaged that all individual investments will be referred to Cabinet to approve within the total investment portfolio size and in line with the criteria set by the WRIF Investment Strategy (subject to any officer delegations that Cabinet approve). Cabinet will receive and decide on recommendations and will also decide on investments which fall outside of the parameters of the WRIF Investment Strategy. Any further detailed proposals in relation to internally managed elements of the Fund will be brough back to Cabinet as necessary.

Officer role in decision making

7.4 It is also proposed that an Investment Panel is established. It is proposed that Investment Panel membership would include representatives from the relevant services within the Council, including Finance, Legal, Business and Economy, Property and Regeneration, and Governance and Policy, with the Strategic Director for Communities as Chair. The Investment Panel would be supported by the appointment of specialist expertise to advise and inform its recommendations. Its proposed role would be:

- To oversee the governance and decision-making process for investments to ensure investment opportunities are thoroughly evaluated and appropriate due diligence undertaken;
- Review and update the WRIF Investment Strategy to reflect the current needs of local businesses, the local economy and investment market;
- Allocate appropriate resources to support the governance and decision-making process;
- To make recommendations to Cabinet on any individual investment decisions for Funds, in line with the criteria set by the WRIF Investment Strategy;
- To consider individual business case investment proposals, reviewing, challenging and making recommendations on individual investment decisions;
- Monitor the progress and performance of individual investments as well as the overall portfolio;
- Undertake effective risk management;
- Regularly review and take corrective action to ensure the returns on live investments meet the overall criteria and targets;
- Regularly review the effectiveness of decision-making tools and make changes to better achieve the Council’s investment strategy objectives; and
- Provide updates to Cabinet (and Member Oversight Group when required) on the performance of the Portfolio.

7.5 Where the fund is externally managed the role of the Panel is to:

- Review and update the WRIF Investment Strategy to reflect the current needs of local businesses, the local economy and investment market;

- Provide contract management of External Fund Managers/Management, ensuring their awareness of and alignment with the current Investment Strategy;
- Monitor the progress and performance of the overall portfolio; and
- Provide updates to Cabinet (and Member Oversight Group and the relevant Overview and Scrutiny Committee when required) on the performance of the Portfolio.

7.6 The Panel will also have an overarching role in relation to the overall Fund to make recommendations to Cabinet and Council on Fund priorities and allocations for the following year.

Member Oversight and Scrutiny

7.7 It is proposed to establish a cross-party standing Member Oversight Group chaired by the Deputy Leader to consider the direction, scope and extent of investment decisions and alignment to the Business Plan on internally managed elements of the Fund, and to consider any proposals for changes to the WRIF Investment Strategy prior to Cabinet being asked to approve them. There may be opportunities to align this group with the Member group overseeing WPDC activity. This will be confirmed in the next report to Cabinet as part of the confirmed proposals for the WRIF.

7.8 Monitoring the performance of funds (at an officer and member level) will also be a critical aspect of the arrangements to ensure robust governance and early alerts and corrective action if the investments are considered to be underperforming against the Council's strategic objectives and in terms of financial performance. This role would encompass active monitoring and scrutiny of the fund's performance on policy and financial grounds, assessing delivery of the annual business plan, identifying weaknesses and improvement actions. It would also include making recommendations for continuation, augmentation or exit depending on the Fund performance. Further detail around the global performance management arrangements and scrutiny of the fund will be developed and presented to the next Cabinet meeting.

7.9 The relevant Overview and Scrutiny Committee could also include in its work programme consideration of the overall performance of the Fund and make recommendations to Cabinet about its parameters and operations as it considered appropriate.

7.10 The Audit and Standards Committee will review the Council's accounts, WRIF investments, and the wider risk and assurance framework supporting the operation of the Fund.

8.0 Legal powers and fiduciary duties

8.1 The Council has sought external legal advice in developing the WRIF proposals. covering the questions of vires (does the Council have legal powers to set up the fund), what considerations must the Council consider before investing or offering products through the fund (including the Council's fiduciary duties in respect of public money and appropriate governance), changes to state aid rules post EU transition, and regulatory requirements. The full legal advice (confidential) is available to members on request however the key matters are set out below.

Legal Powers (vires)

8.2 The legal advice has confirmed that the Council has the necessary legal powers to establish the WRIF. These are contained in:

- The General Power of Competence (for lending, funding and other activities);
- Section 12 Local Government Act 2003 (power to invest);
- Local Authorities Land Act 1963 – acquiring, developing land and funding for certain third party developments;
- Section 120 Local Government Act 1972 (acquiring land – particularly for the benefit, improvement or development of its area); and
- The Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 – (treatment of receipts and capital treatment of certain loans).

8.3 The legal powers will need to be subject to ongoing review over time depending on the size and scale of its activities and to ensure that governance arrangements are robust, fiduciary duties are considered and that there is compliance with the requirements of any PWLB borrowing.

Fiduciary Duties

8.4 The issue of fiduciary duties has been considered in shaping the initial concept and design of the proposals and a summary is set out below. In making decisions about the establishment of the WRIF and approving the funds, the Council must have regard to its fiduciary duties. These can be summarised as the Council acting as 'a trustee' of tax and public sector income (and liabilities) on behalf of its local taxpayers and other residents. The Council in effect holds money but does not own it; rather, it spends money (and incurs liabilities) on behalf of its business rate and council taxpayers.

8.5 The potential quantum of funding involved in the WRIF proposals coupled with the potential risk of losses and the fact that a Council will be funding something different from typical local authority activities has required consideration of fiduciary duties throughout this project. This report highlights for members the key considerations in terms of fiduciary duties, and how risks and mitigations will manage/avoid losses arising from the proposed investments.

8.6 A summary of the Council's fiduciary duties and how they have been considered and are assessed in this report is set out below:

Considerations	How addressed
Clarity of the policy objectives/outcomes which WRIF (or its separate streams) are designed to support/deliver	Section 4 of this report covers the policy objectives / outcomes which the WRIF is designed to deliver. The evidence based for these objectives is the SQW report (August 2020) which set out the post Covid economic outlook for Warwickshire
Options Appraisal – assessment of WRIF versus alternative routes to deliver the policy/objectives. Why are the WRIF proposals best suited to deliver these?	The options appraisal is set out at paragraph 142 of the Business Case and summarised at paragraph 4.6 of this report, and concludes that WRIF is the most appropriate policy option for the Council to pursue
Financial impact (to the Council) of the proposals and the risks of non-recovery and steps to mitigate/manage such risks. If some of funding is expected to be non-recoverable, this should be identified.	This is set out in detail in Section 6 of the Business Case and covered at Section 9 of this report. The analysis includes the risks of non-recovery
Benefit of WRIF to target groups (who would benefit under WRIF) fairly balanced against the interests of Warwickshire's taxpayers/residents – i.e. the impact of the money being spent on WRIF (especially if a loss is projected or high level of risk is involved) on the Council's other activities/level of Council Tax.	The direct economic benefits of WRIF are estimated in paragraphs 214 and 215 of the Business Case. These show an annual contribution to the county's gross value-added of £110m – 160m. The direct financial benefit to the County Council in terms of the potential Net Present Value of the net revenue £4.9m (paragraph 367 of the Business Case).
Fiduciary Duty considerations are not a one-off exercise. They remain relevant throughout the life of the programme. Members and officers need to continue to consider the above points – i.e. act in an efficient 'business like' manner	This will be kept under review throughout the duration of the fund and any future Fund decisions taken

8.7 The Business Case projects that the LCEF will potentially make a loss given the profile of investments and the industries supported, However, the fact that not all funds, i.e. the LCE pillar within WRIF, are projected to be recovered does not, in itself, mean that the Council is failing in its fiduciary duties if it supports the WRIF. It does mean that the Council needs to recognise that there is a potential risk in relation to LCEF, and decision makers need to properly consider these issues (such as the quantum of loss; were other alternatives to deliver the policy objective considered and were these less likely to result in a loss; would other aspects of the WRIF programme compensate for this shortfall; was this approach better than a grant (100% loss) and how would the projected loss impact on the wider interests of the Council's taxpayers/residents) in reaching their decisions. These points are addressed in more detail in Section 9. This approach needs to be applied throughout the life of the WRIF as decisions are made on investments, and as new products or interventions are considered.

8.8 As highlighted in the table, consideration of fiduciary duties should also be applied to future decisions in relation to the activities of the Fund including:

- allocation of Council funding to WRIF funds;
- scoping and approving new products / initiatives;
- approving individual transactions – against criteria for the relevant product; and
- active management and monitoring of the WRIF funds' performance.

These aspects will need to be kept under continual review throughout the Fund's existence and will need to be covered in any future reports to Members as necessary.

Subsidy Control, Regulatory Requirements and Governance

8.9 The position on subsidy control (State Aid's replacement) is that broadly speaking the same considerations apply. The new subsidy control principles are broad and are focused on subsidy being policy-driven, proportionate, and necessary, designed to incentivise policy-conducive economic behaviour. Given that the proposals for WRIF primarily involve the offer of loans at market rates, it is not considered that subsidy control will have a significant impact on the proposals however this will be kept under review as the detail of the products available is developed and defined.

8.10 In terms of regulatory requirements, the proposals in the main involve relationships which are classed as business-to-business lending. Provided the Council keeps within the framework of such relationships and avoids any activity which could be classed as consumer lending (Council lending to private individuals) then the requirements of the FCA regulations do not need to be considered.

8.11 The most obvious area of risk comes with the LCEF interventions. Here, although lending will be business to business in the sense that it is funding intended to support small business, there is an added risk in any lending to small businesses who may be sole traders and thus "individuals" for the purposes of the regulatory framework. Although there are specific exemptions which can be used for lending to individuals for business purposes, the requirements of the exemption (which include a declaration by the individual as to the purpose of the loan) need to be closely followed to ensure that the parties do not inadvertently create a regulated loan. There may also be some situations where the fund may potentially be dealing with individuals which do not readily fit within the available exemptions. For this reason, officers are continuing to explore the balance of internally versus externally managed funds. Contracting with a third-party external fund manager who has an existing FCA authorisation, would enable the Council to indirectly fund regulated loans without being at risk of a Regulatory infringement. An entity with an existing FCA authorisation to provide smaller regulated loans should also have available loan documentation in the correct format and existing policies to incorporate the required FCA regulations.

8.12 Section 7 of this report contains the detailed Governance proposals for the establishment and operation of the WRIF.

9.0 Financial Implications and Risk Management

Level of investment

9.1 The £140m figure for investment in the WRIF over five years is considered to be the upper limit of what is affordable and reasonable to invest. Changes to the Treasury Management & Investment Strategies will be needed to accommodate this level of investment and these changes will be brought forward at the point at which Cabinet will be asked to approve the Year 1 Business Plan (noting that changes to the Treasury Management & Investment strategies will require Council approval). Council will also be required to approve the addition of a loan facility for the element of the WRIF spend that is capital in nature. Within this overall £140m figure for WRIF, a cap of £90m has been allocated for the Business Investment Growth pillar which has the lowest risk and strongest return, with a much lower £10m cap set for the higher risk Local Communities and Enterprise Pillar to minimise the risk of 'losses' on that pillar and ensure the overall WRIF makes a positive return, is affordable and takes account of the Council's fiduciary duties. There is a £40m cap for Property Investment.

9.2 £140m is the maximum investment, and repayment profiles will mean that peak debt is significantly below this level. The financial modelling behind the Business Case has demonstrated a peak funding level of £76m over the 5 year investment cycle. The Monte Carlo simulation[4] in the financial model has also indicated a high probability that the WRIF will produce a net positive return. The Council is also able to manage risk based on the overall economic and market conditions at the time. If losses start to increase then the Council may wish to slow or stop future investments or invest in more secure counter parties.

Analysis of Investment and Returns

9.3 The following table represents the potential returns to the Council over a 5 year period from the WRIF including recovery of principal and interest and any estimated losses arising from default. In overall terms the WRIF is expected to return a net revenue over 10 years of £6.5m (NPV £4.9m). These are modelled numbers, and the Council will target the recovery of all investments to avoid

[4] A model used to predict the probability of different outcomes

default losses across all 3 pillars and in particular to avoid the LCE potential losses.

	Total WRIF	Business Growth	Communities & Enterprise	Property & Infrastructure
Gross Funding	£140m	£90m	£10.0m	£40m
Peak Funding[5]	£76m	£50m	£3.4m	£25m
PWLB Interest	-£9.5m	-£6.3m	-£0.4m	-£2.8m
Potential Loss	-£2.8m	-£0.5m	-£2.3m	£0.0m
Running Cost	-£2.8m	-£1.8m	-£0.2m	-£0.8m
Arrangement Fee	£0.5m	£0.45m	£0.05m	£0.0m
Interest Repayment	£21.0m	£12.6m	£1.2m	£7.2m
Net Revenue	**£6.5m**	**£4.4m**	**-£1.5m**	**£3.6m**
Net Revenue (NPV)	**£4.9m**	**£3.5m**	**-£1.3m**	**£2.7m**

9.4 The table below from the Business Case is a breakdown of the potential loss arising from defaults across all 3 pillars, which are already included in the 'potential loss' figures within all three pillars of the table above.

Financial Year	Potential Loss
20/21	£0k
21/22	£94k
22/23	£351k
23/24	£495k
24/25	£422k
25/26	£419k
26/27	£477k
27/28	£327k
28/29	£147k
29/30	£24k
10-Year Total	£2,755k

9.5 The following table from the Business Case summarises the key financial risks (not exhaustively) and actions that can be taken to mitigate them.

Risk	Potential Management & Mitigations
Governance	

[5] Peak Funding is the maximum exposure of each of the pillars and its impact on the WRIF as a whole. Timing is an important control for the Council, as the peak funding of one pillar may not occur at the same point as another, and this can be used as a tool to manage risk. As the peak funding for each pillar occurs at a different time in the cycle, the calculation is not merely the sum of the peak of each pillar.

Risk	Potential Management & Mitigations
Insufficient resource and expertise is committed to the business case process that supports any investment decision (for internally managed funds) and as such investment decisions are poor and increase the likelihood of loss. The Council is slow in making corrective actions where investments are performing below expectations Recent coverage of Local Authorities getting into difficulty when making loans to third party entities has highlighted the need for a robust understanding of the risks, governance arrangements and the need to quickly identify and act on any financial issues. Appropriate training, sufficient understanding of investment and purpose, timing of returns and robust reporting against issues where all identified as key areas to Council wishing to undertake these activities.	The Council must identify sufficiently qualified resource to ensure business cases are robust and any investment decisions properly understood. Reporting should be sufficiently regular and detailed to ensure that issues are identified and addressed in a timely manner. The Council should pay regard to recent Public Interest reports in this area and ensure that lessons learnt are embedded in the governance of the WRIF. A key element highlighted in the reports was the need to challenge optimism bias and for appropriate training and skills for officers and also training for members to enable members to adequately scrutinise and challenge the information they receive.
Finance and Funding Risks Finance rates are currently at historically low levels, with some commentators believing that the current market outlook may push these rates lower. As such, debt is currently relatively cheap, although this could be considered the new norm when looking at the current Government Bond Market. There is a risk that the future success of the programme could be impacted by an interest rate rise.	The Council has a corporate Treasury Management strategy that allows rises in interest rates to be managed across a range of financial instruments thereby lower the impact of future rate increases.
Debt monitoring and recovery Where an element of a fund is internally managed there is insufficient resource applied to monitor and recover debts once the initial investment has been made.	Sufficient resource must be identified to monitor and report on the performance of the funds. Market Testing has indicated the total costs of the Fund to be in the region of 2% of the total sums invested, which is in line with industry norms.

Risk	Potential Management & Mitigations
Default levels exceed Fund estimates Default rates have been estimated based on the financial strength of the counterparties. However, as the Fund is focused on Growth and Recovery losses may exceed those expected and there may be insufficient set aside to cover Fund losses.	The creation of the commercial risk reserve (£7.5m) proposed as part of the 2021/22 MTFS provides additional financial cover in the short term should the level of loan repayment defaults be higher than those expected in the business case until such time as corrective action to the operational arrangements for the WRIF or the next MTFS refresh can be put in place. The value of the reserve could be assessed each year for prudence and adjustments made accordingly. Where losses exceed expectations, this should be fed back to the Investment Panel and consideration given to a tightening of investment criteria.
Investment Objectives Investment objectives are unclear, not consistently applied or don’t adapt to meet changing market conditions or the needs of the Council.	Regular review of the relevance of the investment objectives, including their rationale, is vital in keeping the programme and investment decision making responsive.
Local Government Regulation There is currently heightened scrutiny in the Sector, where authorities are looking to support their financial positions through the use of commercial investments. This increases the risk of changes to Local Government Regulation that may inhibit the ability of the Council to invest in such activities or increase the cost of doing so. Failing to meet the current PWLB rules would have an adverse impact on the Council’s ability to borrow for future activities. For instance, regulation around MRP has been adapted to respond to current market activity and borrowing requirements from PWLB have recently changed.	The Council must identify key individuals responsible for the regular review of all legislation and financial requirements. The Council must have the flexibility to alter investments if those changes would adversely impact the ability to borrow/fund statutory services. The WRIF proposals are policy-driven non-treasury investments and therefore are considered to comply with the current regulatory framework.

9.6 The appropriate source of finance for each investment will be considered during investment decision making, when the opportunity is being reviewed, by the Investment Panel prior to making investment recommendations to Cabinet (in respect of internally managed funds) and by the external fund manager in other cases.

9.7 Returns potentially come from several sources, for example:

- capital receipts;
- financing returns, e.g. return on loans issues to third parties;
- other payments for financial support e.g. Loan guarantees, income strips; and
- return on equity.

9.8 However, each of the above relies on a different investment approach by the Council and a different risk profile, providing a combination of short, medium- and long-term returns that go beyond the current approach.

9.9 Sensitivity analysis demonstrates a strong likelihood of a positive return across the total WRIF,[6] but demonstrates that the Local Communities & Enterprise pillar, taken in isolation, provides only a low chance of a positive NPV, as per the below table from the Financial Case:

	Business Investment Growth	Local Communities & Enterprise	Property & Infrastructure
% Chance of Positive NPV	High	Low	High

9.10 For the Local Communities & Enterprise pillar to break even, there would have to be significant adjustments made to assumed rates of investment return, loan default rate and recovery on default. It is therefore stated that a cross subsidy model between the funds may need to operate, in order to support the viability of the Local Communities & Enterprise pillar.

9.11 In isolation, the Local Communities & Enterprise pillar has a low likelihood of a positive NPV, but it has a potentially vital role in delivering positive policy outcomes across the county, including job creation, increasing skills, supporting new businesses and maintenance of some of the County's environment and key social capital assets.

9.12 Using external expertise to manage the Local Communities & Enterprise pillar will assist in mitigating the risks associated with it, as described above. In

[6] I.e. all three funds (Business Investment Growth, Local Communities & Enterprise, and Property & Infrastructure) considered together.

procuring the expertise we will look for appropriate targets and incentives to form part of the contractual arrangements. In summary, these risks arise from the nature of the target market of the pillar and the types of product it is likely to offer.

Financial Implications for the Council

9.13 Potential sources of finance for WRIF activities are:

- external borrowing (for example PWLB);
- internal borrowing (temporary use of our cash balances); and
- co-investment/partner funding.

9.14 The Financial Case also references recent changes to the Lending Arrangements for PWLB Loans. Government concerns about excessive investment risk taking by some Local Authorities have led to the requirement that the Section 151 officer must certify that the Council is not borrowing in advance of need and does not intend to buy investment assets primarily for yield/income. This will impact on the amount of borrowing available for WRIF in that not all types of activity will be capable of attracting PWLB borrowing. It is critical that the PWLB criteria are not breached as failing to meet the criteria could see a council prevented from using the PWLB for any purpose during that financial period – this would impact on the availability of funds to provide services or undertake capital projects.

9.15 Running and operating costs, including all internal costs for resources and external costs for management as well as any transaction fees and charges, are expected to be covered by the borrowers wherever appropriate. This will be generally achieved through a normal market transaction charge for any investment.

9.16 There is likely to be a minimum level of activity that the WRIF will need to undertake to recover the overhead and administration costs of operating the Fund, whether it is run internally or commissioned externally. This will need to be explored further through the development of the WRIF business plan and operational arrangements.

External borrowing

9.17 At the end of March 2020, the Council’s level of outstanding debt was £321m with a further £327m forecast over the period of the 2021-26 MTFS as the financing for the Capital Investment Fund (CIF)/WPDC. Any loans/purchase of shares through the WRIF would be additional to our current plans or could utilise some of the capacity for additional borrowing already built into the MTFS for the CIF. The business case estimates up to £130m additional capital spend through the WRIF, with £10m to be funded from internal resources. Borrowing of this magnitude would suggest it will need to be additional to our current plans, and brought back to Council for approval to be added to the capital programme.

9.18 Where £130m is the maximum exposure to external debt within the WRIF, investment and repayment profiles will mean that peak debt is significantly below this level.

9.19 Any borrowing the County takes out and then provides onwards through the WRIF as a loan/purchase of equity is proposed to be taken out on the basis that the financial returns from the investment more than cover both the interest and principal repayments to the Council that arise from taking out the borrowing plus any costs of the WRIF administration and decision-making arrangements.

9.20 As has been highlighted in the report and business case, as a local authority, the Council is required to make sure it acts prudently in setting aside resources to repay the principal of any loans taken out to fund capital expenditure, which is the nature of the loans/equity investment it would be providing through the WRIF. The recent public interest reports on local authority owned companies determined that not setting aside resources because of an assumption that income would be received to repay the loans before they were due was not a prudent approach. Therefore, the County Council will need to make provision for Minimum Revenue Provision (the provision for the repayment of principal) in its revenue budget. The repayment of loans made through the WRIF would need to be structured in such a way as to ensure sufficient levels of repayment to offset the costs of financing our PWLB loan/s and hence creating no additional call on the Council's revenue budget.

Internal borrowing

9.21 The Council currently has a significant level of cash balances. However, these cash balances are not unencumbered. They represent income we have received/collected in advance of the spend planned for using the reserve taking place e.g. reserves and borrowing deferred as the result of slippage in the capital programme. We are able to 'lend' these cash resources through our Investment Strategy provided we are confident that the cash will be returned and available by the time the future commitments to its use materialise.

9.22 Any revenue loans made through the WRIF would need to be financed from this source, if there is not to be an immediate cost to the MTFS. Therefore, the detailed operational arrangements of the WRIF will need to ensure timely repayment of any such loans.

9.23 The Investment Strategy seeks to manage the overall financial risk to the Authority through the use of our cash balances in this way. It sets an overall maximum limit for such loans that should ensure we do not reach the position of having insufficient available cash to meet our commitments. Current commitments against this limit include the working capital loans to Educaterers and WPDC, and the contribution to the CBILs. There will be an ongoing need to monitor the net level of outstanding debt in its entirety to ensure these limits are not breached and our financial standing impaired.

Risk and Risk Management

9.24 The following table summarises the key risks and proposed mitigations involved in setting up and operating the WRIF.

Risk	Mitigation
Fiduciary duties (PWLB, Prudential Code)	• Annual Cabinet review and decision making • Legal and specialist Treasury Management advice supports creation of Fund • Engagement with external auditors • Member Oversight Group and role of other member bodies (eg Audit and Standards Committee/OSC)
Default/loss, bad debts, interest rates	• Securitisation of loans and use of specific points enabling WCC to recover its investments • Investment Panel, chaired by the Strategic Director for Communities, due diligence to inform investment recommendations • Diversified and balanced portfolio of investments to mitigate risk • External advice to support sound running of WRIF, including to manage impact of changes in interest rates • Provision of business support to ensure strong, investment-ready proposals come forward
Impact on MTFS	• Ability to start small and build the fund up slowly with ongoing review of impact on MTFS of external/internal borrowing • Prudent accounting by including default assumptions in the business case and plan • Annual review and annual business plan approval by Cabinet, effectively an annual ‘continue/stop’ decision • Creation of £7.5m commercial reserve to cover any losses from WRIF, WPDC and other commercial activity
Reputational	• Policy-driven objectives underpin WRIF, with clear strategic priorities to drive investment decisions • Annual review and approval of business plan • Clear performance framework and benefits to track impact of WRIF • Member Oversight Group meets quarterly to review performance and operation of the WRIF • Annual Cabinet review/continue decision point
Skills and capability	• Likely mix of internal/external provision to run the WRIF • Appointment of specialist staff in Finance and Communities teams

Regulatory	• Where any products are likely to require FCA registration (most probably products within the LCEF) external fund management will be sourced

10.0 Environmental Implications

There are no direct environmental implications arising from the setup of the WRIF. Environmental implications arising from bids to the WRIF can be considered on a case-by-case basis as the respective funds become operational. Investing in new technologies and low carbon opportunities will be priorities and there may be scope to include some monitoring/evaluation around environmental impact. There may also be scope to have restrictions on use of funding that would have a direct negative environmental impact.

11.0 Supporting Information

Supporting information is included in the appendices to this report.

12.0 Timescales associated with the decision and next steps

A further report will be brought back Cabinet in due course and to Council thereafter prior to establishment and launch of the WRIF.

Appendices

Appendix A: WRIF Business Case
Appendix B: Equality Impact Assessment
Appendix C: SQW report

Background Papers

None

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