Warwickshire County Council

# Warwickshire Recovery Investment Fund (WRIF)

Business Case

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# 1. Executive Summary

## INTRODUCTION & CONTEXT

1. Warwickshire County Council's ('the Council') Council Plan and other key strategic documents place a focus on supporting Warwickshire's economy to ensure it remains vibrant and is supported by the right jobs, training, skills and infrastructure.
2. The COVID-19 Pandemic has had profound impacts, globally and locally, for public health, the economy, society and the environment, highlighting and compounding existing known challenges. Like the rest of the UK, these impacts are being directly experienced in Warwickshire where GVA and employment is expected to be significantly adversely affected.
3. Economic analysis was commissioned and undertaken by SQW, (a provider of research, analysis and advice in economic and social development). Its research assessed the potential impact of COVID-19 in the local economy and endeavoured to forecast this impact by sector and indicate potential job losses and the recovery timescale of both.
4. The SQW report recommended the establishment of a Warwickshire Recovery and Investment Fund (WRIF). The WRIF could access funds and provide further provision of finance to enable investments that can help support local businesses in key growth sectors that in turn create jobs, underpin social enterprise and unlock land.
5. The Council now wishes to test the business case for the WRIF to be established and to outline how this proposal will need to be delivered. To do this the Council has commissioned a Business Case, based on a proportional approach to the Treasury Green Book, 5 Cases Model that will look to support the Council's decision-making process.

## STRATEGIC CASE

6. The purpose of the Strategic Case is to outline how the proposal fits with the wider policy and strategic objectives of the Council.

### The Proposal

7. The Council is seeking to test the establishment of the Warwickshire Recovery and Investment Fund (WRIF) to support the economic recovery of the County. Its aim is to provide access to finance for businesses and through this access to provide a platform to support social and financial investment in key growth sectors.
8. The WRIF is proposed as a mechanism for implementing a programme of interventions and investment within the County. Its governance is such that it will enable a range of targeted support across a variety of different needs based on their key financial and growth characteristics.

9. It will use a variety of potential sources to finance a range of investments; with each investment being assessed on a consistent basis against a number of pre-agreed objectives. This approach will allow the Council to choose the best form of investment given the known financial parameters; whilst paying regard to the commercial and wider economic conditions at the time.

10. Economic analysis undertaken by SQW suggested that a Fund focused on three themes for investment might best support the economic recovery in the County. The three themes were:

- Business Growth;
- New Business, Local Communities & Enterprise; and
- Property & Infrastructure.

11. The three themes or pillars upon which the WRIF will be based as an overarching portfolio are:

- Business Improvement Growth;
- Local Communities & Enterprise; and
- Property & Infrastructure.

12. Each Pillar of investment is proposed to have a different focus, different investment criteria, different types of investment, different management arrangements and different target beneficiaries and outcomes.

13. The recent approval of the formation of the Warwickshire Property Development Company (WPDC) will also contribute towards the Property & Infrastructure Pillar. WPDC has its own separate Business Case and Business Plan and does not therefore form part of this Business case for the WRIF.

The Case for Change

14. There is clear strategic alignment of the Fund with delivering Council priorities. Specifically, establishment of the Fund will support delivery of the Council Plan, Recovery Plan and other key strategies by promoting investments and setting investment criteria that are aligned with strategic priorities and will help enable the delivery of priority outcomes.

15. The SQW report and subsequent economic analysis has indicated there will be a significant impact of COVID 19 on the local economy, resulting in a significant increase in the number of unemployed and a drop in GVA.

16. Changes in banking terms as a result of COVID-19 meaning there is less capacity to engage with higher risk or more innovative funding requests, coupled with an existing unmet demand for finance within the County indicates a growing demand for investment to support Warwickshire based businesses and the local economy.

17. Without the WRIF, the contributions to economic recovery will be limited to those from the existing investment market and the broader County and government response to the pandemic. This could delay recovery and restrict economic growth into the longer term.

18. There is therefore a clear rationale for action to be taken by the Council to mitigate the impact to the County, aid the economic recovery from COVID 19 and help support businesses in key growth sectors to continue to grow. This fund, if created, will be one of the Council's significant directly

controlled contributions to the economic recovery of Warwickshire amongst the much larger and broader county and government response.

## THE ECONOMIC CASE

19. The purpose of the Economic Case is to assess the range of potential options for best achieving the strategic goals of the project.

20. A total of seven options are being considered by the Council, which can be categorised into three main decisions:

- Decision 1: WRIF or "Do Nothing";
- Decision 2: The Structure of the Fund or Funds; and
- Decision 3: The future management arrangements for the Fund or Funds (based on the preferred fund structure determined in Decision 2)

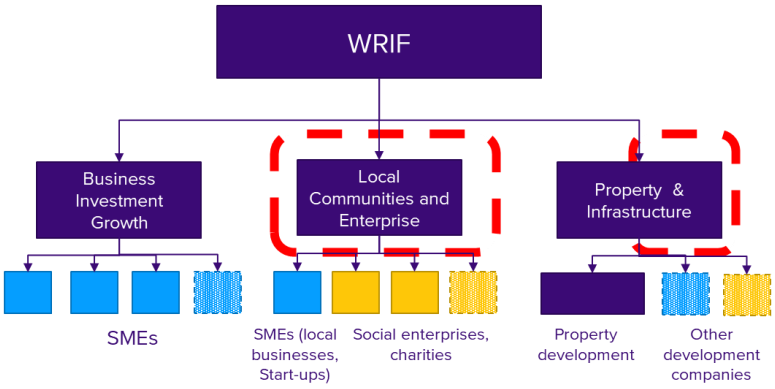
21. A market engagement exercise was undertaken to help shape and develop the focus of the WRIF and to provide a gap analysis to understand the current investment market and how the WRIF might align, complement, or enhance existing investment funds and the extent to which there is existing or potential unmet demand for finance in the region.

22. In line with HM Treasury guidance and methodologies, decision criteria have been used for appraising the options, alongside feedback from the market engagement.

### The preferred option

23. Using the decision criteria it has been determined that **Option 7 – Establishing a WRIF based around three-pillars and a mixed economy of fund management is the preferred option**. A visual of this option is shown in the diagram below:

**Option 7: WRIF mixed economy**




Mix of in house and outsourced. This is illustrative and actual mix to be determined by market engagement

24. The red boxes in the above diagram are indicative only to illustrate the parts of the fund which may be managed externally.

Conclusion – the preferred approach

25. The preferred approach, and the approach to be taken forward as part of this Business Case, is the option to establish the WRIF to support the identified three-pillar structure and a mixed economy of fund management.

26. This option is the preferred approach because:

- Establishment of the WRIF is aligned with strategic priorities and will enable the Council to have a dedicated fund and a targeted approach to support the economic recovery of the County.
- A do-nothing option, that relies on contributions from the existing investment market and broader government response to the pandemic, has been discounted for not directly contributing towards the Council's aims and objectives or strategic priorities and not supporting a targeted approach to the economic recovery of Warwickshire.
- The Fund will manage investments by monitoring outcomes, be set up to best meet WCC's objectives and will use investment criteria to support its outcomes around increased GVA, business growth and the creation of new jobs.
- The three-pillar structure reflects that the proposed elements of the WRIF are sufficiently different to require a fund structure that allows different recipients and different benefits to be targeted.
- A three-pillar structure is also expected to be more attractive to the market by allowing specific gaps in the market to be targeted and the skill set for Fund Management to be able to be tailored to the specific requirements.
- A three-pillar structure also ensures that the investment criteria, governance and decision making can be tailored to the scale, type and risk of investment which is expected to differ across each of the funds.
- A mixed economy of fund management secures the advantages of external expertise, resource, capacity, and knowledge of sectors and the investment market but which provides some involvement and control for the Council plus the opportunity for skills transfer too.

## COMMERCIAL CASE

27. The purpose of the Commercial Case is to address any issues of commercial feasibility and seeks to answer the question "can the proposed solution be effectively delivered through a workable commercial deal or deals?" In the case of the WRIF this section outlines the types of investment, commercial terms and decision-making process by which all investment opportunities for the

WRIF will be assessed together with the fiduciary and commercial considerations the investment opportunities progressed by the WRIF must satisfy.

Summary of the Pillars of Investment

28. A total portfolio of c.£140m is proposed across the three pillars,

29. A proposed breakdown of the total WRIF portfolio is as follows:

- £90m for the Business Investment Growth Pillar
- £10m for the Local Communities & Enterprise Pillar
- £40m for the Property & Infrastructure Pillar

30. The WRIF as a Fund is flexible to respond to market need and changing economic and financial climates, as such, the proposed governance structure allows the proposed allocation to each pillar to change provided it stays within the £140M envelope.

31. It is suggested that the WRIF operate as a closed Fund, meaning that a period of investment decision making for the Fund would initially be limited to up to 5 years.

32. The following tables summarise the key features and proposed terms for each individual pillar of investments operating within the WRIF.

*Table 1 -Investment Priorities*

| Name | Description | Priorities |
|---|---|---|
| **Business Investment Growth** | Finance for growing businesses with sound prospects | Priority industries<br>• automotive technology,<br>• advanced manufacturing and engineering,<br>• digital creative/video game development<br>• tourism and hospitality<br>• logistics<br>• house building/ modern methods of construction (MMC)<br>• 'green' /sustainable technologies or industries<br>• rural industry and enterprise<br>• social care or other supply markets of the Council<br>• Any new sector that creates skilled or entry level jobs |
| **Local Communities & Enterprise** | Aimed at addressing local challenges and the economic and social consequences of the pandemic | Priority business types<br>• New and growing SMEs<br>• Small, local businesses that support social capital<br>• Start ups<br>• Social enterprises<br>• Environmentally and/or economically sustainable businesses that are driving climate change benefits, cardon neutral and low carbon initiatives |

| Name | Description | Priorities |
|---|---|---|
| | | • Those businesses that create entry level jobs and/or increase skills<br>• Those businesses where investment will improve high streets and town centres |
| **Property & Infrastructure** | Provide loans to invest in commercial sites, premises and infrastructure. Support viable developments to underpin economic recovery | Priority is on enabling development:<br>• Supporting viable external led schemes where they fit the investment strategy |

*Table 2 -Key Investment Features*

| Name | Indicative fund size | Investment size & volume | Investment term | Investment type |
|---|---|---|---|---|
| Business Investment Growth | [£90m] | <£10m (Approx. 2-5 per annum. Low number of high value loans) | Up to 10 years | • Predominantly commercial loans<br>• Management Buy Outs/ Acquisitions / Refinancing |
| Local Communities & Enterprise | [£10m] | <£1m (Approx. 10-30 per year. Higher volume, lower value loans) | Up to 5 years | • Commercial loans<br>• Equity investment<br>• Co-investment with social investment partners<br>• Other more innovative products |
| Property & Infrastructure | [£40m] For investments that sit outside WPDC | <£40m | Up to 10 years | • Commercial loans<br>• Equity investment<br>• Corporate guarantees<br>• Joint Ventures |

Benefits

33. Using metrics from other Funds it is possible to illustrate the scale of direct benefits that the WRIF may be able to deliver according to the proposed size of the fund. The table below indicates the potential range of benefits the WRIF as a portfolio fund at £140m could deliver:

**WRIF at £140m**

| Projected outcomes | Summary |
|---|---|

| | |
|---|---|
| Jobs created | 2,500 - 3,400 |
| Jobs safeguarded | 2,700 - 3,900 |
| Annual regional GVA (£m) | 110 - 160 |
| Number of Businesses supported | 118 |
| Private sector leverage (£m) | £78 - 104m |
| Public sector leverage (£m) | £26 - 35m |
| Land remediated (hectares) | 15-23 ha |

Approach

34. A WRIF Strategy that sets out the objectives, priorities, type of investment and criteria for assessing investment opportunities is to be approved.

35. It is proposed that an Investment Panel (an officer body) is established to monitor the performance of the WRIF at a portfolio level and also to guide and make recommendations on any investment decisions that are to be managed in house, with Cabinet making the final decision to invest.

36. It is proposed that the WRIF is to have a mixed economy of Fund Management with some elements of the Fund managed in-house, with the support of advisors, and some outsourced to external Fund Managers. A procurement exercise will be undertaken to secure Fund Management services to support delivery of elements of the WRIF where it is considered that the type of investment, volume of opportunities, due diligence and/or resource and skills required justify the costs for external management.

37. The WRIF Strategy will form the basis of the criteria for all investment decisions but there will be an alternative set of arrangements and approach to decision making depending on the management arrangements for each Fund/element of the WRIF.

38. A robust Sift and Business Case approach to support investment decision making for those elements of the Fund that will be managed in house.

39. The Council will establish an in-house team for the WRIF that will operate alongside the existing Business & Economy Team and the Business Support Programme that is already established and being operated by the Council. The in-house team will be responsible for managing investments that relate to the Business Improvement Growth Pillar and any other elements of the WRIF that are to be internally managed and will report into the Investment Panel that will be established for decision making and management and monitoring of the WRIF.

40. It is anticipated that a large proportion of the potential investment opportunities available to the Fund will be gained by directly engaging with the local market. Where external Fund Management is in place it will be the role of the Fund Manager to source opportunities using their network. In addition to this a detailed marketing strategy and associated website will be

developed that sets out the nature of the fund(s), its focus and priority areas and the nature of the investment it is likely to make. This will promote the fund locally and be used to source investment opportunities.

41. Each year Full Council and Cabinet (as appropriate to the decision being made) will approve:
    - the relevant annual budgeted amount for each WRIF pillar of investment;
    - set out the WRIF's authority to operate the fund via the Investment Panel for the next year; and
    - the key priorities and themes for investment, should these have changed from the prior year.

42. A Member Oversight Group will be established for the scrutiny of investment decisions where quarterly monitoring reports will be referred and any individual investments or investment decisions can be referred in for further scrutiny.

Commercial Considerations

43. In addition to the practical mechanisms of investment decision making, including counterparty risk and profile and of return there are four key factors that the commercial case of any investment made by the WRIF must satisfy:
    - The Council has sufficient powers to makes the investment (known as vires);
    - The Council's fiduciary duties;
    - There is no State Aid associated with the investment; and
    - There are clear exit arrangements.

44. The Council's legal advisors have provided an advisory report to provide guidance on these matters. Specific advice has been given regarding the Powers to set up WRIF and the legal advisors have concluded that *"The Council, in principle, has the powers to create WRIF and the related funds for the broad purposes set out in the Strategic and Economic Cases"*.

45. The Council must however keep the activities of the WRIF under review to check vires, ongoing compliance with its fiduciary duties, and ensure the structure of the fund (and their activities) remain (for capital spending) within the PWLB's guidance's 'permitted activities' and related conditions.

Conclusion

46. All the key factors that the commercial case must satisfy have been considered and legal advice has confirmed that the Council has sufficient powers to create the WRIF.

47. The approval of a WRIF Strategy will form the basis of the decision-making process for the WRIF and ensure that investment decisions are aligned with strategic priorities but also commercially robust as a viable investment opportunity.

48. A robust governance and accountability process, through establishment of an Investment Panel and Member Oversight Group, is proposed for adoption whereby all investment opportunities will be assessed via a consistent decision-making process that will ensure that all the commercial considerations are assessed for the investments progressed by the WRIF.

49. Specific advice will be required on key investment points to ensure that legal requirements such as appropriate security, financial strength of each entity and the impact each of these has on matters such as State Aid (it's replacement) or any legacy matters, have been factored in the decision.

50. Assessing a portfolio of investments through the establishment of the WRIF will allow the Council to manage risk and give it the ability to invest in some moderately higher risk activities, where these risks are offset against some lower risk opportunities. A commercial investment case will also be made for all individual investment opportunities that are progressed to business case stage.

51. Establishment and resourcing of robust monitoring and reporting of investments and appropriate exit strategies will also ensure that the Fund remains affordable to the Council throughout the duration of an investment. Affordability will be considered in the finance case, but there is a requirement that there is a constant feedback loop between robust monitoring, investment criteria and affordability to ensure investments meet the objectives of the WRIF.

## FINANCIAL CASE

52. The Financial Case is used to consider the affordability of the proposed project. In the case of the WRIF, the finance case assesses the affordability of the Fund as the preferred approach and how each investment will be considered with reference to the financial parameters set out in the WRIF Strategy.

### Funding

53. The WRIF approach enables the Council to directly invest in a wide range of interventions; introducing a diverse range of returns both in terms of size, timing, and nature of receipts.

54. The potential sources of finance are Borrowing, Guarantees, Reinvestment of surplus balances from the WRIF and Co-investment/ Partnerships.

55. The most appropriate source of finance for each individual investment will be determined and recorded at the time of the investment decision making when the individual opportunity is being reviewed by the Investment Panel via consideration of a Business Case. Where external borrowing is used the business case will need to state which of the permitted activities the investment falls under and a positive confirmation with appropriate evidence that is it complies with new PWLB lending arrangements will be required

### Affordability

56. Affordability will be a key constraint, and the Council will need to understand the programme of investment at a portfolio level as well as the return profile of each intervention.

57. The fund will operate on a commercial basis and should not therefore be investing into financially unviable schemes or providing grants.

58. Running and operating costs of the Fund will need to be accounted for and monitored in relation to the performance of the Fund.

59. It is proposed that the Fund will cover all internal costs for resources and external costs for management as well as any transaction fees and charges. The aim is to make the Fund run as efficiently as possible, seeking to pass costs on to borrowers wherever appropriate. This will be generally achieved through a market normal transaction charge for any investment.

Financial Modelling

60. Financial modelling and financial scenario testing has been undertaken to understand the financial impact and affordability of the WRIF based on a "typical" level of investment across the three pillars of investment over a 5 year profile of investment.

**Overall Financial Performance of the WRIF**

| Item | Total £M |
|---|---|
| Gross Funding | 140 |
| Peak Funding | 76 |
| | |
| PWLB Interest payable | (9.5) |
| Potential Loss through default | (2.7) |
| Running Cost | (2.8) |
| Arrangement Fee | 0.5 |
| Interest Repayment | 21.0 |
| **Net Revenue** | **6.5** |
| **Net Revenue (NPV)** | **4.9** |

61. The modelling indicates the total financial return from the WRIF over its investment cycle lies in the region of £6.5m, (£4.9m NPV).

62. Sensitivity and scenario analysis was conducted to determine the predicted range for how the WRIF returns could vary. Based on the results there is a "near certain" probability that the WRIF will produce a net return. However, due to the varied nature of investments and market needs across the three pillars the risks and returns vary. More detailed analysis of each of the pillars has been conducted in the Finance Case.

Conclusion

63. The Financial Case concludes that proposals for the WRIF, as a whole, are affordable as the Fund has been designed as a flexible tool to enable investment in a wide range of different opportunities to manage and diversify risk and ensure that all costs are contained within the Fund.

64. Risks will need to be managed at a Portfolio level and will form part of the performance and monitoring measures put in place by the Investment Panel.

## MANAGEMENT CASE

65. The purpose of the Management Case is to assess whether a proposal is deliverable by setting out the governance structure, project planning, risk management and communication & engagement arrangements required to ensure successful delivery of a project.

Management arrangements

66. The Council will establish an in-house team for the WRIF that will operate alongside the existing Business & Economy Team and the Business Support Programme that is already established by the Council. The in-house team will be supported by a team of external advisors that will need to appropriately procured.

67. The in-house team will report into the Investment Panel that will be established for decision making and management and monitoring of the Fund.

68. A procurement exercise will be undertaken to secure Fund Management services (and any other external advice required) to support delivery of elements of the WRIF where it is considered that the type of investment, volume of opportunities, due diligence, risk, skills and resource require external involvement. It is anticipated that there will be a requirement for more than one external Fund Manager across the WRIF in order to support operation of investments relating to both the Local Communities & Enterprise and the Property & Infrastructure pillars.

69. It is proposed that an Investment Panel is established to monitor the performance of the WRIF at a portfolio level and also to guide and make recommendations on any investment decisions for any investments that are to be managed in house.

70. Each year Full Council and Cabinet will approve the relevant annual budgeted amount for each WRIF fund and set out the WRIF's authority to operate the fund(s) via the Investment Panel for the next year.

71. All individual investments will be referred to Cabinet to approve within a total investment portfolio size of £140M and in line with the criteria set by the WRIF Strategy. The Panel will report to Cabinet to whom it will also refer investment decisions that fall outside of the parameters of the WRIF Strategy and delegations that will be considered as part of the future business plan, subject to approval of this business case, in due course..

72. A high-level Project Plan will be prepared to cover all significant activities, events and milestones involved in the setting up and running of the WRIF. The Project Plan will be regularly updated and included in regular Progress Reports.

73. The Council's risk management strategy will be embedded by the Investment Panel into its management of the WRIF and robust monitoring process of individual investments as well as the portfolio as a whole. Performance of the WRIF will be monitored by the Investment Panel and reported through the highlight reports and the use of a risk log or register and as part of the Quarterly reporting to Cabinet.

74. The Member Oversight Group will have the opportunity to consider any investments where the risk of investment requires further scrutiny, or the risk of default has increased following the original investment decision.

Communication & Engagement

75. The purpose, scope, and operation of the WRIF will need to be clearly communicated across the Council. Effective operation of the WRIF will also require communication and engagement with stakeholders outside of the Council who may introduce potential investment opportunities.

76. A detailed marketing strategy will be developed that sets out the nature of the fund(s), its focus and priority areas and the nature of the investment it is likely to make. This will promote the fund locally and be used to source investment opportunities.

Conclusion

77. The Management Case concludes that the Council intends to resource and manage the WRIF using robust governance and decision-making arrangements and by sourcing resources internally and externally to the Council.

## WAY FORWARD & NEXT STEPS

78. The Business Case confirms the preferred approach to establish the Warwickshire Recovery & Investment Fund. It describes the structure of the Fund, how it will be funded, resourced, managed and monitored.

79. The Council will seek approval of the Business Case from Cabinet to establish the WRIF, agree the WRIF Strategy, agree governance arrangements and seek the approval of Full Council where required.

80. Approval will also be requested to commence procurement activities needed to support the management and delivery of the WRIF and the set up and running costs associated with this.

# 2. Introduction

## CONTEXT FOR THE PROPOSAL

81. Warwickshire County Council's ('the Council') Council Plan and other key strategic documents place a focus on supporting Warwickshire's economy to ensure it remains vibrant and is supported by the right jobs, training, skills and infrastructure.

82. The COVID-19 Pandemic has had profound impacts, globally and locally, for public health, the economy, society and the environment, highlighting and compounding existing known challenges.

83. Like the rest of the UK, these impacts are being directly experienced in Warwickshire where GVA and employment is expected to be significantly adversely affected.

84. In response to the pandemic, the Council has developed a Recovery Plan setting out its priority actions for recovery from COVID-19. The Recovery Plan sets out 10 priorities aligned to the long-term vision and outcomes the Council has already set out in their Council Plan to 2025. Three of these priorities focus on Warwickshire's economy to ensure it is vibrant and supported by the right jobs, training, skills and infrastructure.

85. During the Recovery Plan development, Member Working Groups considered the key challenges and solutions which could be used to support recovery in terms of Economy, Place and Climate Change. One potential solution was an Investment Fund and accordingly it was requested that the Council commission work to investigate whether a fund should be set up by the Council, and potentially partners, given the economic downturn and extreme challenges business and residents would face caused primarily by the pandemic.

86. Against this backdrop, the Council first wanted to explore how the economy of Warwickshire might change over the next period of 5 years given the effects of the pandemic and the process of EU transition, (commonly referred to as "Brexit"). Secondly, the Council wanted to understand the difference it could make by using its financial strength to set up a Fund that could support Warwickshire based businesses and the jobs of its residents.

87. Economic analysis was commissioned and undertaken by SQW, (a provider of research, analysis and advice in economic and social development). Its research assessed the potential impact of COVID-19 in the local economy and endeavoured to forecast this impact by sector and indicate potential job losses and the recovery timescale of both. SQW also developed an economic forecasting model to enable the Council to review and update the potential impacts on the local economy over time.

88. As further context to the current impact of COVID-19, other research suggests access to bank finance becomes more problematic for SMEs during crisis episodes. This is a combination of reduced supply of lending by banks and reduced demand from SMEs who face chronic

uncertainty. Managing finances is likely to become hugely important for small companies. This is on top of a recognised shortage of finance availability for businesses in Warwickshire pre-COVID, particularly with respect to mezzanine and equity finance options.

89. In this context the SQW report recommended the establishment of a Warwickshire Recovery and Investment Fund (WRIF). The Council, through the WRIF, could access funds and provide further provision of finance to enable investments that can help support local businesses in key growth sectors that in turn create jobs, underpin social enterprise and unlock land. The WRIF could aim to provide access to finance for businesses and for social investment, but also provide a return commensurate with risk to cover costs that can be reinvested over time to continue to deliver benefits and outcomes sought from the Fund.

90. In light of these reports, the Council now wishes to test the business case for the WRIF to be established and to outline how this proposal will need to be delivered.

91. To do this the Council has commissioned a Business Case, based on a proportional approach to the Treasury Green Book, 5 Cases Model that will look to support the Council's decision-making process.

92. The structure of the business case will include key information under each of 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;
- **The Economic Case-** demonstrates that a range of potential options have been considered and compared against the existing landscape. and that a preferred option is able to better achieve the strategic goals of the Council whilst complementing the current offer;
- **The Commercial Case** – sets out the opportunity, the route to investment, the commercial terms and legal considerations, including both internal and external constraints that must be addressed in taking forward the preferred option;
- **The Financial Case -** presents financial data the financial parameters set for the fund(s) and demonstrates the affordability of the proposal; and
- **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.

# 3. Strategic Case

93. The purpose of the Strategic Case is to outline how the proposal fits with the wider policy and strategic objectives of the Council.

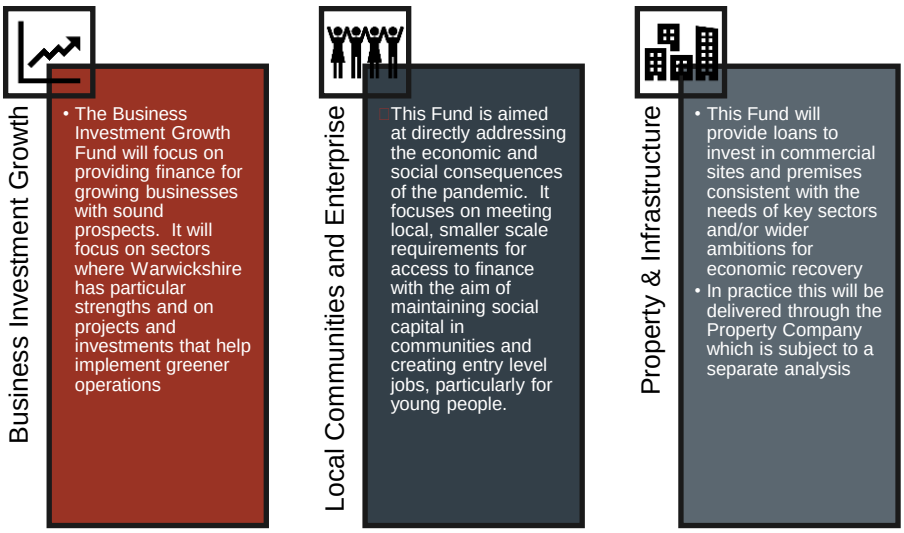
## THE PROPOSAL AND APPROACH

94. The Council is seeking to test the establishment of the Warwickshire Recovery and Investment Fund (WRIF) to support the economic recovery of the county by providing access to finance for businesses and for social investment in key growth sectors. The expected outcome of this support is that it will support existing business, create new business and create jobs in Warwickshire and in delivering these policy driven Council objectives also provide a relatively small return, commensurate with risk, that can be reinvested into the Council over time to support future service delivery and or investments and continue to deliver benefits and outcomes for the residents of Warwickshire.

95. In October 2020, Cabinet agreed to investigate the establishment of a WRIF and requested a further report to Cabinet by February 2021 setting out a full business case. If approved, officers have been working on a report, potentially for consideration in March, on the WRIF delivery business plan, with a view to set-up the WRIF thereafter recognising the economic impact being experienced by residents and business now.

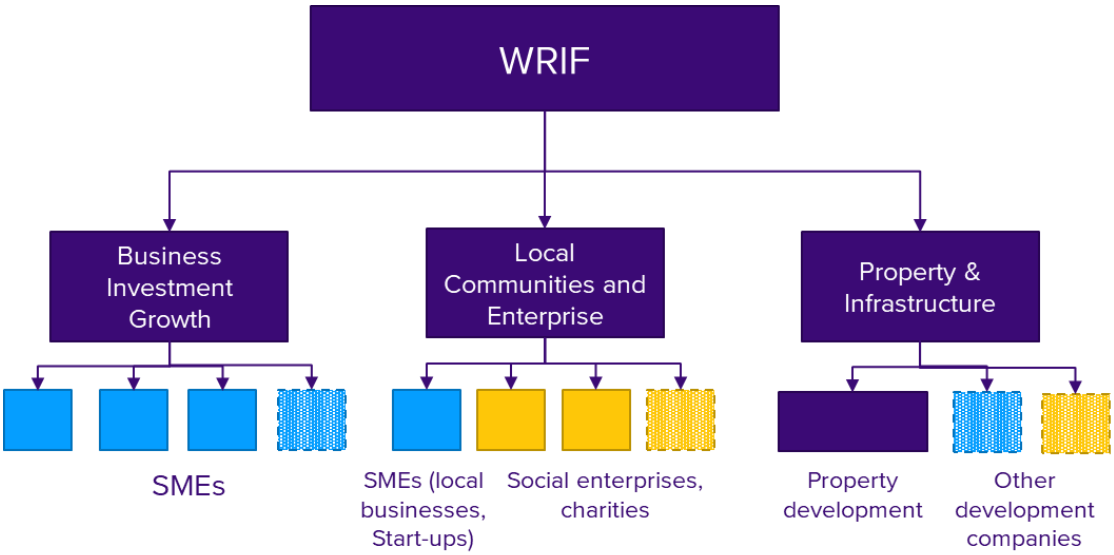
### The Structure

96. The SQW report, commissioned by the Council to assess the impact of the current pandemic on the Warwickshire Economy put forward a Fund that focused on the following three themes or pillars for investment that might best support the economic recovery in the County:




97. These proposals form the broad basis for the WRIF which has then been shaped through market engagement and more detailed understanding of demand and the priority focus and subsequent beneficiaries of the Fund. A more detailed description of the WRIF is set out in subsequent sections of this document.

98. An initial structure for the WRIF, using the three main themes to establish three pillars or focused areas of investment, was suggested (as shown below).




Objectives

99. An initial set of objectives and principles were set out by SQW and then subsequently agreed by Cabinet.

100. The objectives have been revisited in more detail and have been updated to set out what the Fund is aiming to achieve. The proposed objectives for the WRIF are to:

- 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 (c. 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

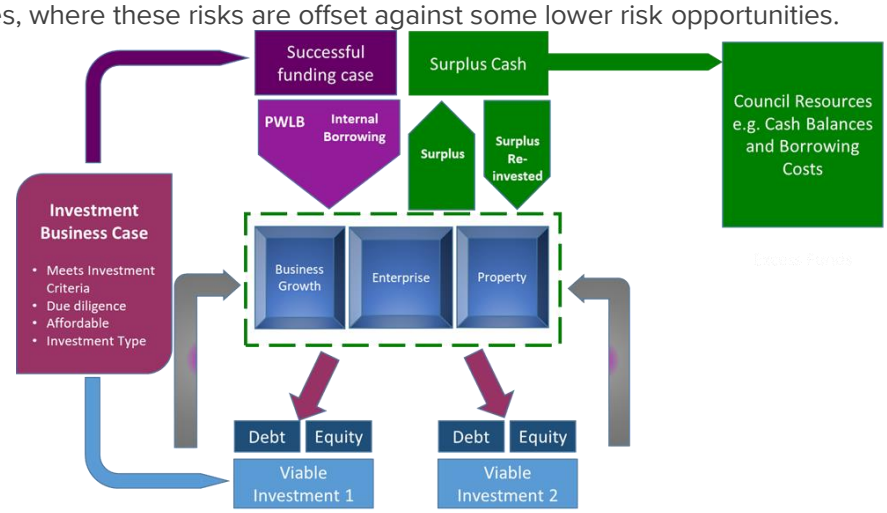
101. The main principles of how a Fund might operate have also been revisited and have now been established to be:

- Support County based business;
- Create a diversified and balanced portfolio of risk-based investments that protect the public purse and support business and create new and protect existing jobs;
- 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.
- Support business through investments based on agreed investment criteria and priorities that are developed from analysis of the economy and strategic sectors and 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

102. The WRIF is proposed to act as a mechanism for implementing a programme of investment and a process for enabling a range of investment opportunities with a variety of different needs based on their key investment characteristics.

103. It will use a variety of potential sources to fund a range of investments that can be assessed on a consistent basis against a number of pre-agreed objectives. This approach will allow the Council to choose the best form of investment given the known financial parameters; whilst paying regard to the commercial and wider economic conditions at the time.

104. The WRIF will provide a clear and consistent methodology to assess each request to the Council for investment support. By establishing this structure and assessing a portfolio of support it will allow the Council to manage risk and give it the ability to invest in some moderately higher risk activities, where these risks are offset against some lower risk opportunities.




## THE STRATEGIC FIT

105. The Council has defined its strategic priorities and ambition for Warwickshire over the next five years in its Council Plan 2020 – 25. The Plan has a clear vision 'To make Warwickshire the best it can be, sustainable now and for future generations' by making best use of its resources by focusing on:

1. Warwickshire's communities and individuals are supported to be safe, healthy and independent; and
2. Warwickshire's economy is vibrant and supported by the right jobs, training, skills and infrastructure;

106. By establishing a Fund, the Council is able to directly support delivery of the Council Plan and more specifically create a vibrant economy and the associated priority to 'attract economic investment and maximise the rate of employment, business growth and skill levels in Warwickshire'. The Fund will provide access to finance to support businesses and leverage additional funding for the County, both of which will support the economic recovery of Warwickshire.

107. The COVID 19 Recovery Plan sets out 10 priorities aligned to the long-term vision and outcomes the Council has already set out in their Council Plan to 2025. Three of these priorities focus on Warwickshire's economy to ensure it is vibrant and supported by the right jobs training, skills and infrastructure:

- 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.

- 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
- 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.

108. The Council has declared a climate change emergency and has also indicated that recovery from COVID-19 must be a green recovery that helps to address the serious long-term challenge of climate change. One of the priorities set in the Recovery Plan focuses on Climate Change and indicates that:

- Sustainability and tackling climate change should be made central to our recovery so that we lay the foundations for a sustainable long-term future

109. The WRIF will support delivery of the Recovery Plan by promoting investments and setting investment criteria that are aligned with these priorities, including those that are focused on sustainability.

110. The WRIF will also support the Economic Growth Strategy which outlined seven strategic priorities for economic growth in the county, with particular attention given to four sectors: **automotive technology, advanced manufacturing and engineering, digital creative/video game development, tourism and hospitality**. These sectors will be included as priority sectors for investment by the Fund to ensure that investment is focused in strong sectors to enable continued growth.

111. The WRIF will also support a number of the Council's other key Strategies, including the Commercial Strategy, Capital Strategy, Property Strategy, Local Industrial Strategy (West Midlands) and Coventry & West Midlands LEP Strategic Economic Plan (updated) by providing access to finance, supporting Warwickshire based businesses and mitigating some of the impact of COVID-19 on the local economy which in turn will enable the Council to continue to deliver on the key outcomes set out in these Strategies.

## THE CASE FOR CHANGE

112. There is clear strategic alignment of the Fund with delivering Council priorities. Specifically, establishment of the Fund will support delivery of the Council Plan, Recovery Plan and other key strategies by promoting investments and setting investment criteria that are aligned with strategic priorities and will help enable the delivery of priority outcomes.

113. The SQW report and subsequent economic analysis has indicated there will be a significant impact of COVID 19 on the local economy, resulting in an increase in the number of unemployed and a drop in GVA.

114. Changes in banking terms as a result of COVID-19 meaning there is less capacity to engage with higher risk or more innovative funding requests, coupled with an existing unmet demand for

finance within the County indicates a growing demand for investment to support Warwickshire based businesses and the local economy.

115. Without the WRIF, the contributions to economic recovery will be limited to those from the existing investment market and the broader County and government response to the pandemic. This could delay recovery and restrict economic growth into the longer term.

116. There is therefore a clear rationale for action to be taken by the Council to mitigate the impact to the County, aid the economic recovery from COVID 19 and help support businesses in key growth sectors to continue to grow. This fund, if created, will be one of the Council's significant directly controlled contributions to the economic recovery of Warwickshire amongst the much larger and broader county and government response.

117. The fund, if successful, will have several beneficial financial impacts for Warwickshire County Council, will leverage additional funding for the county through opportunities to collaborate funding streams and secure match funding and support the long-term financial sustainability of the Council.

## CONCLUSION

118. There is a clear rationale and a robust case for the establishment of the WRIF as:

- Without the WRIF, the contributions to economic recovery will be limited to those from the existing investment market and the broader County and government response to the pandemic. This contribution is not expected to be sufficient to mitigate the impact of COVID-19 or support the economic recovery of the county in a short time frame.
- The market engagement has confirmed there is an existing and growing demand for finance in the county, but existing sources of funding are limited and there are increasing barriers to businesses being able to access finance they need to continue to thrive and grow.
- Establishment of the WRIF provides an opportunity for the Council to directly contribute to the economic recovery of the County rather than businesses relying on the current investment market and external financial markets to access finance and support which is now more limited.
- There is clear strategic alignment of the proposed WRIF with delivering Council priorities. Specifically, the Fund will:
    - help meet the priority to 'attract economic investment and maximise the rate of employment, business growth and skill levels in Warwickshire';
    - support delivery of the Economic Growth strategy by investing in priority sectors;
    - support delivery of the COVID-19 Recovery Plan by supporting business and stimulating job creation and skills with a direct positive impact on business rates and council tax payments.

- The Fund will offer the Council a flexible tool and act as a mechanism for implementing a programme of investment and a process for enabling a range of investment opportunities with a variety of different needs based on their key investment characteristics.
- The Fund will provide support to the County in both the short, medium, and longer term and, whilst not the primary objective, has the potential to generate financial returns from the investments to reinvest into the Fund, to continue to deliver benefits and outcomes in jobs over the longer term.

# 4. Economic Case

119. The purpose of the Economic Case is to assess the range of potential options for best achieving the strategic goals of the project.

120. A range of options have been developed to test how the WRIF could be structured and delivered. The Economic Case will:

- Set out the options;
- Set out the basis on which these options will be assessed;
- Establish the decision criteria against which these options will be assessed;
- Outline the market engagement exercise to be and already undertaken and the results of this engagement;
- Complete an assessment of the options to determine the **preferred approach** – this will be a qualitative assessment against the agreed criteria;
- Outline the anticipated benefits of the WRIF; and
- Set out key risk and considerations to be taken into the Commercial assessment

## THE OPTIONS

121. A total of seven options are being considered by the Council, which can be categorised into three main decisions:

- Decision 1: WRIF or "Do Nothing";
- Decision 2: The Structure of the Fund; and
- Decision 3: The future management arrangements for the Fund or Funds (based on the preferred fund structure determined in Decision 2)

122. The options under consideration and how they relate to each of the three main decisions are set out in the table and diagram below:

| Decision 1: WRIF or "Do Nothing" | Decision 2: The Fund Structure | Decision 3: The Fund Management |
|---|---|---|
| Option 1: WRIF or Do Nothing | Option 2: WRIF operates as a single fund<br>Option 3: WRIF operates with 2 pillars<br>Option 4: WRIF operates as 3 pillars | Option 5: WRIF in house fund management*<br>Option 6: WRIF outsourced fund management<br>Option 7: WRIF mixed economy |

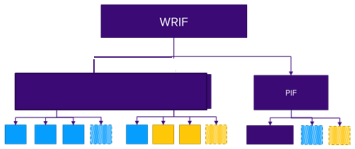
*In house fund management is where the Council, supported by external consultants and advisors, manages the fund. They are responsible for sourcing investments, investment decision making, governance, performance monitoring and management.

**Decision 1: WRIF or Do Nothing** Option 1: Do Nothing

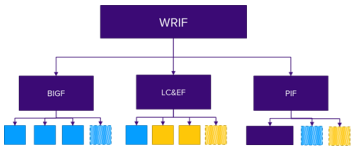
**Decision 2: Fund structure**

Option 2: WRIF operates as a single fund


Option 3: WRIF operates with 2 pillars

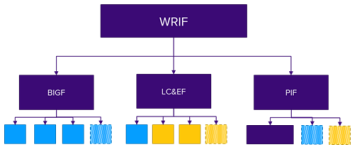



Option 4: WRIF operates with 3 pillars



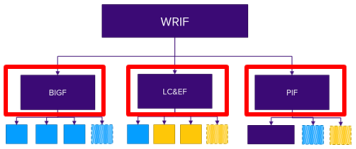

**Decision 3: Sourcing fund management.** Based on preferred fund structure – indicative only below

Option 5: WRIF inhouse fund management



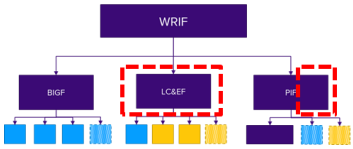

Each fund managed inhouse

Option 6: WRIF outsourced




Each separate fund outsourced

Option 7: WRIF mixed economy




Mix of in house and outsourced. This is illustrative and actual mix determined by market engagement

## MARKET ANALYSIS

123. Economic analysis has been undertaken by SQW for the Council to understand the economic impact of COVID-19 and an economic forecasting model has been used to assess the potential impact of the EU exit on Warwickshire's economy.

124. Overall, the model suggested the following economic impact for Warwickshire:

- That there could be an increase in the number of unemployed people from 7,000 before the pandemic, to around 26,500 albeit this could grow with further phases. When the second wave scenario was applied to the model this equates to a forecast of between 19,500 and 23,415 additional people out of work.
- Like the rest of the UK, the challenges are facing sectors that rely on in-person service delivery, such as retail, hospitality, leisure and recreation
- The model shows that perhaps a third of the additional jobs lost in 2020 could be in food and beverage services, retail and accommodation
- These sectors employ a large proportion of younger people, on lower wages and lower productivity, and the effects will be spread across all County. It points to some clear priorities for a recovery plan.
- 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.

125. The longer-term outlook for the UK economy remains highly uncertain. It is dependent on the evolution of the pandemic and the measures taken to protect public health. It will also depend on how governments, households, businesses, and financial markets respond to those developments.

126. In November 2020, the Bank of England published its Monetary Policy Report, which outlined 'The economic outlook', 'recent developments' along with 'projections and risks'. In the Bank of England's projections, the economy is expected to start to recover in 2021, although GDP is not expected to not exceed its level in 2019 Q4 until 2022.

127. The process of economic recovery is often described in relation to 'bounce back curves' which come in four distinct shapes—L, U, W, and V. The exact curve of recovery the U.K will follow is still unknown, due to ongoing policy changes around COVID-19 restrictions and the impact of the current trade deal with the EU. Initial expectations were for a V- shape recovery for the UK, the best-case outcome, where there is an initial sharp downturn fall, bottoms out and economic recovery quickly follows. This was based on assumptions for a full reopening of the economy and removal/reducing COVID-19 restrictions occurring all at once (September 2020). This has not happened due to the second wave of the pandemic, the discovery of the new variant virus and the need for implementation of Tiers with differing rules (and the majority of the country continuing under some form of restrictions affecting economic sectors to a greater degree than originally anticipated). The current position may lead to a further dip and accordingly a more U-shape recovery, where the recession lasts longer with a slow return to the level of growth seen before the original downturn. The impact of the virus mutation and the success of the vaccine rollout and community testing will also impact on the recovery curve in ways that have yet to be determined.

128. In consideration of the broader economic outlook, the rationale for the WRIF to be established and to have a direct and targeted impact to help support economic recovery for Warwickshire is well made. However, this case must now be considered as part of this process to ensure governance, legal and financial risks are known and considered before commencement of the Fund.

## MARKET ENGAGEMENT

129. A market engagement exercise in two stages was proposed to help shape and develop the focus of the WRIF. The first stage was intended to provide a gap analysis to understand the current investment market and determine:

- How the WRIF might align/complement or enhance existing investment funds in the region
- The extent to which there is existing or potential unmet demand for finance within the County
- How the fund should be structured from a market perspective

130. The second stage is to test the preferred option in the market in order to refine the details of the Fund. Further details on this soft market testing exercise is included in the Commercial Case.

131. For the first stage of market engagement informal verbal conversations were held with the following organisations that operate in or have experience in the region:

- **British Business Bank –** a government owned business development bank who run the Midlands Engine Investment Fund (MEIF) as well as other regional investment programmes
- **Coventry & Warwickshire Reinvestment Trust** - a not-for profit, FCA accredited, specialist finance provider who provide business loans on behalf of WCC and other local public sector bodies to businesses and individuals looking to start a business
- **Mercia** – an asset manager with a focus on regional businesses seeking venture capital, private equity or debt finance to scale their business. Mercia operate the proof-of-concept equity finance up to £750k for the MEIF
- **Maven CP** – provides debt finance between £150k and £1.5m on behalf of the MEIF and also similar finance for other regional and local government partners
- **BCRS** – a non-profit distributing lender providing small business loans between £25k to £150k on behalf on the MEIF
- **Ascension Ventures** – an early-stage venture capitalist who have advised WCC and other regional funds and operates Fair by Design, a fund dedicated to ending the poverty premium
- **Finance Birmingham/Frontier Development Capital (FDC)** – sister companies with a strong relationship with Birmingham City Council (BCC). Finance Birmingham is owned by BCC and manages targeted funds that are largely now closed to new opportunities. BCC also has a small shareholding in FDC that provides long term debt between £1m and £10m to mid-market SME business and property developers in the UK.

132. We also contacted Midven as a MEIF fund manager but the contact was reluctant to engage at this stage.

133. The following scope of questions formed the basis of the informal discussions:

- Extent of investment in Warwickshire-based businesses & type of businesses/organisations that are prioritised
- Types of finance offered

- Types of businesses/organisations supported
- Gap for investment/support – areas of unmet demand, areas of weakness in proposals/applicants, reasons unable to support some current applicants
- Attractiveness of the proposed WRIF funds to fund managers
- Consideration of social benefits in investments
- Any lessons specific to Warwickshire based businesses or that WCC should take into account when setting up its fund and using external fund managers for example balancing financial return with economic benefits, additional support for businesses prior to coming to the fund

134. The main themes of feedback from the discussions were as follows:

- **Demand -** there is clear demand for finance from businesses located in Warwickshire: £12m of £85m invested by the MEIF has been in Coventry & Warwickshire businesses. Whilst fund managers do not specifically measure or record investments in Warwickshire as distinct from Coventry, they all felt that additional capital targeted at Warwickshire would be beneficial and could be utilised
- **Gaps –** there are some identified gaps in the regional market where companies struggle to secure finance for example: loans between £1.5m and £5m; start-up capital; equity/mezzanine finance; management buy-out or refinancing; capital financing with longer term payback. These gaps are generally as a result of changes in banking terms as a result of COVID-19 meaning there is less capacity to engage with higher risk or more innovative funding requests.
- **Flexibility** – a key area of learning raised by a number of the funds was the need to keep the WRIF flexible and to avoid prescriptive lending and repayment terms. It was considered important to be able to flex where the fund is targeted based on the gaps and opportunities at the time. 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 and that links between different types of fund managers through the lifecycle of companies could be better managed and indeed bult into contracts.
- **Attractiveness to the market –** the WRIF proposals are attractive to the existing market of fund managers. A number of them already have operations on the ground that they could utilise for the WRIF. Each fund manager had specific niche areas for example start-ups; equity; loans; property; mid-market SMEs. None of the fund managers we spoke to had expertise in social enterprises, however this will be tested via broader range of participants in the engagement with the market in early 2021.
- **Wider social benefits –** all fund managers were familiar with seeking investments that bring wider social benefits such as job creation. That said, for start-ups the view was that it is important to concentrate on getting the business viable and the jobs will follow.

- **Business support** – most of the fund managers we spoke with highlighted the need for additional support to businesses pre-investment. This took the form of different suggestions but included: signposting and liaison across different funds; accelerator programmes; and incubator arrangements.

135. This feedback from the market has been used to shape and refine the terms of the WRIF to ensure that the Fund is designed to meet the needs of the market but also complement and enhance the existing investment landscape rather than compete against it. Some specific aspects of the fund, such as lending and repayment terms, measuring and evidencing benefits, attractiveness to the market in terms of fund management will be tested further via soft market testing in the early part of 2021.

## ASSESSMENT OF THE OPTIONS

136. In line with HM Treasury guidance and methodologies, decision criteria have been used for appraising the options.

137. A workshop with officers of the Council was used to determine the objectives of the Fund and accordingly the decision criteria that could guide a decision on the preferred approach. It was agreed that there were three main decisions required;

- Decision 1 - firstly, whether or not there was a rationale for the Fund;
- Decision 2 - secondly, how the fund should be structured; and
- Decision 3 - thirdly, how the fund could be managed.

138. The table below sets out the decision criteria that were used in a staged, three decision, approach:

| Decision 1: WRIF or Do Nothing | Decision 2: Fund structure | Decision 3: Sourcing |
|---|---|---|
| 1. Ability to deliver Strategic Objectives of WCC<br>2. Ability to support the post-COVID economic recovery of Warwickshire in a targeted way<br>3. Ability to support businesses, social enterprises and create jobs<br>4. Ability to generate financial returns from investment for the Council | 1. Similarity of objectives<br>2. Reflective of economic analysis & main themes for investment<br>3. Similarity of recipients<br>4. Similarity of types of finance<br>5. Similarity of benefits (financial return, social benefits) | 1. Level of specialist knowledge and skills needed to operate<br>2. Existing market to utilise<br>3. Attractiveness to the market<br>4. Requirement for regulated advice<br>5. Legal Powers<br>6. Ability to leverage additional investment finance |

139. The options were then qualitatively assessed against the appropriate criteria for Decision 1, 2 and 3 in order to determine the preferred option. A matrix, using the following scoring key, is provided below to demonstrate the extent to which an option meets the decision criteria:

| Scoring Key | Description |
|---|---|
| Y | Yes - The option fully meets the criteria by enabling the Council to support, deliver and generate the objectives and outcomes for the Fund and/or best meets the decision criteria |

| Scoring Key | Description |
|---|---|
| P | Partially – The option meets the criteria to some extent but is not the best option for delivering the Council's objectives or meeting the decision criteria |
| N | No – The option does not meet the criteria, provides minimal support to delivering the Council's objectives and/or does not adequately reflect the decision criteria |

Decision 1: WRIF or "Do Nothing"

140. Decision 1 first gives consideration whether there is a clear rationale for the establishment of the WRIF in comparison to a "do nothing" option.

141. Do nothing is defined as continuing to rely on the contributions from the existing investment market and the broader county and government response to the pandemic that will support the economic recovery of Warwickshire, for example:

- The county Council continues with its current approach to supporting the local economy;
- Businesses rely on the current external financial markets to access finance and support;
- Businesses access public sector support through the current investment framework that includes, but is not limited to:
  - Midlands Engine;
  - Central Government schemes
  - Investment Trusts, including CWRT and BCIT; and
  - Current County initiatives.

142. The table below compares these two options against the decision criteria.

| Decision criteria | Do Nothing Option 1 | WRIF All other options | Comments |
|---|---|---|---|
| Ability to deliver Strategic Objectives of WCC | P | Y | In a Do-Nothing option, delivery of Council priorities will be via other council initiatives and without a targeted approach may take longer to deliver<br>The WRIF supports the delivery of a number of priorities in the Council's key strategy documents |
| Ability to support the post-COVID economic recovery of Warwickshire in a targeted way | P | Y | In a Do Nothing Option the existing investment market will contribute to the economic recovery of Warwickshire and thus the criteria is only partially met.<br>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. |
| Ability to support businesses, social enterprises and create jobs | P | Y | In a Do-Nothing option, the council will have to support and finance businesses, social enterprises and create jobs via other council initiatives and thus the criteria is only partially met<br>The WRIF has a specific focus on supporting business, social enterprises and creating jobs, increasing GVA and will generate investment returns commensurate with risk |

| Decision criteria | Do Nothing Option 1 | WRIF All other options | Comments |
|---|---|---|---|
| | | | that can be reinvested to continue support into the medium and longer term. |
| Ability to generate financial returns that as a minimum cover cost and provide a return commensurate with the risk taken by the Council | N | Y | As a portfolio the WRIF will generate a financial return commensurate with the risk for reinvestment into the Fund. The risk associated with individual investments can be mitigated across the portfolio. |

143. The matrix table above demonstrates that establishing a WRIF is the best option to fully meet all the decision criteria for Decision 1. The main rationale for establishing the WRIF is set out below:

- The WRIF is clearly aligned with strategic objectives and through its establishment will provide a direct way of supporting delivery of strategic outcomes. In a Do Nothing option the delivery of strategic outcomes will 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.
- 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.
- The WRIF has a specific focus on supporting Warwickshire based businesses, social enterprises and on creating jobs. The economic forecasting is indicating a significant impact on GVA and employment to the County and therefore there is a rationale for a direct and targeted approach to mitigate this impact.
- The mechanism of the WRIF will generate financial returns that as a minimum cover costs and therefore are not exposing the Council to additional financial burden.

144. A "Do Nothing" option has been discounted for not meeting the strategic objectives of the Council and not providing the ability to support the economic recovery of the County in a targeted and more timely manner.

Decision 2: The Structure of the single Fund with 3 flexible component fund parts (pillars)

| Decision criteria | 2 Single Fund (under WRIF umbrella) | 3 – Two pillars (Merge Business Investment & Local Communities & Enterprise) | 4 Three pillars | Comments |
|---|---|---|---|---|
| Are the objectives sufficiently similar across the fund(s)? | Y | Y | Y | All 3 proposed pillars have similar objectives around economic recovery |

| Decision criteria | 2 Single Fund (under WRIF umbrella) | 3 – Two pillars (Merge Business Investment & Local Communities & Enterprise) | 4 Three pillars | Comments |
|---|---|---|---|---|
| Ability to target investment against the three themes highlighted from economic analysis? | P | P | Y | Only the three-pillar structure enables targeted investment to reflect the themes from the economic analysis. A single fund or two fund structure can target investment against the broad objectives but will not allow a priority focus on different outcomes and thus only partially meets the criteria |
| Ability to target specific recipients/beneficiaries? | N | Y | Y | There is some cross over of recipients between the Business Investment Growth Fund and the Local Communities and Enterprise Fund (SMEs, business) but the recipients of the Property Investment Fund are quite different. |
| Will the fund(s) offer similar types of finance? | Y | Y | Y | Both the Business Investment Growth pillar and the Local Communities and Enterprise pillar will have the ability to provide debt and equity. The Property & Infrastructure pillar might offer a wider array of intervention including supporting other financial structures e.g. corporate guarantees and local help to buy |
| Will the fund(s) deliver similar benefits? | P | P | P | The financial and non-financial benefits are likely to be different across the 3 pillars |
| Will the fund(s) be appealing to the market? | P | P | Y | The potential market for each pillar is different and it is unlikely that a fund manager would have the knowledge and experience to operate across the 3 areas |
| Ability to set different investment criteria/due diligence requirements? | N | P | Y | The scale of investment and level of risk is likely to differ and the criteria and decision-making process needs to be tailored accordingly. A two-pillar fund structure provides some additional flexibility to tailor the investment criteria and decision making and thus partially meets the criteria whereas a three fund structure provides the most amount of flexibility |
| Will the costs/resources to the Council to set up be similar? | Y | N | N | There will be additional resource and costs associated with setting up more than one single fund |
| Ability to enable/ | P | Y | Y | A single fund partially meets the criteria in that some investment can enable |

| Decision criteria | 2 Single Fund (under WRIF umbrella) | 3 – Two pillars (Merge Business Investment & Local Communities & Enterprise) | 4 Three pillars | Comments |
|---|---|---|---|---|
| accelerate developments? | | | | development. Separate pillars for property & infrastructure however will enable a focus on and prioritisation of enabling developments. |
| Will the risks be more easily managed/ mitigated? | N | Y | Y | Separate pillars enable due diligence and investment criteria to be tailored to the risk |

145. The economic analysis highlighted three themes for investment and thus proposed a structure of three flexible pillars of investment aligned with each theme. Decision 2 compares this three-pillar structure with a single or two pillars which would see the Business Investment and Local Communities & Enterprise pillars merged. A matrix, using the same scoring key, is provided above to demonstrate the extent to which an option meets the decision criteria.

146. Decision 2 assesses the most appropriate structure for the Funds by giving consideration to the objectives, types/scale/size of investment, ability to target different recipients and benefits and appeal to the market. The table above compares three options against the decision criteria:

147. The matrix table above demonstrates that **Option 4** – the option to have three pillars within the WRIF is the best option to meet all the decision criteria. The rationale for a three-pillar structure is set out below:

a) All three pillars have similar objectives around economic recovery.

b) The three pillars have been defined to reflect the three main themes of investment from the economic analysis.

c) The focus of each of the three pillars are sufficiently different to indicate that a fund structure that allows different recipients/beneficiaries and different benefits to be targeted is most suitable.

d) A three-pillar structure, with a focus on enabling development via the Property & Infrastructure Fund allows the opportunity to accelerate development

e) A three-pillar structure will enable different investment criteria, governance and decision making to be tailored to the scale, type and risk of investment. It also allows for more effective risk management. This arrangement gives the Council more flexibility in terms of the structure and repayment terms of the investment.

f) The investment market is distinct, and a three-pillar structure will allow more specific gaps in the market to be targeted.

g) A three-pillar structure will allow market differentiation and make it a more attractive option for potential Fund Managers that have specific skills and experience in each area.

148. The management of a three-pillar structure will now be considered further via Decision 3.

Decision 3: The future management arrangements for the Fund or Funds

149. Based on the preferred fund structure determined by Decision 2, Decision 3 considers the options for:

- The Council to manage all three pillars in-house using their own (or appointed) resources (Option 5 – Insource all)
- The Council to outsource all three pillars and use external fund management (Option 6 – Outsource all)
- The Council establish a mixed economy option where they internally manage some aspects and outsource others (Option 7 -Mixed Economy)

150. The matrix table below sets out how the three options relating to the future management arrangements for the Fund(s) meet the decision criteria. The same scoring key is used to assess each option.

| Decision criteria | 5 Insource all | 6 Outsource all | 7 Mixed economy | Comments |
|---|---|---|---|---|
| Is there sufficient knowledge, experience, skills and resources to operate the funds? | N | Y | Y | The Council are unlikely to have the resource capacity, skills and experience to internally manage all 3 of the Pillars. Outsourcing or a mixed economy option allows the market to respond and tailor the offer against the fund management requirements. |
| Is there an existing market to utilise? | N/A | P | Y | There is a clear market for the Business investment and potentially the Property Investment Pillars but it is less well defined for the Local Communities & Enterprise. The Council could outsource all three pillars but there is likely to be less market interest or capability to manage all three and thus the criteria is only partially met. |
| Is the offer likely to be attractive to the market? | N/A | P | Y | The Council are likely to want the flexibility to have a mixed economy of management support which is tailored to where knowledge, resource and skills are required.<br>The potential market for each pillar is different and it is unlikely that a fund manager would have the knowledge and experience to operate across the 3 |

| Decision criteria | 5 Insource all | 6 Outsource all | 7 Mixed economy | Comments |
|---|---|---|---|---|
| | | | | areas and therefore the criteria is only partially met. |
| Financial regulation (through FCA) advice is required | Y | Y | Y | Some FCA regulated management is recommended for some of the higher risk type of investment. This would need to be sourced as required |
| Does the Council have legal powers for this Fund Management arrangement? | Y | Y | Y | Yes, with adequate support from advisors. |
| Will this arrangement attract or leverage additional investment or finance? | N | Y | Y | Outsourcing options provide the opportunity to leverage private sector finance |
| Will the costs/resources to operate be lower to the Council? | N | P | Y | The Fund will cover all costs for resources as well as any transaction fees and charges. The aim is to make the Fund run as efficiently as possible, seeking to pass costs on to borrowers wherever appropriate.<br>The Council are unlikely to be able to run the Fund in the most efficient way and therefore Option 5 is a No. The size and activities of the fund are different, and it will take time to scale up from the initial set up – this may mean there isn't justification for the costs of procuring and setting up an external fund for the entire WRIF from day one and therefore option 6 only partially meets the criteria. |
| Will the risks be more easily managed/mitigated? | N | Y | Y | Outsourcing and mixed economy options ensure that market knowledge, experience and expertise is a key part of investment decision making, management and monitoring |

151. The matrix table above demonstrates that **Option 7 – the option of having a mixed economy for Fund Management** is the option that best meets all the decision criteria. The rationale for a mixed economy being the preferred option is set out below:

a) From discussions with officers, the Council do not currently have the resource capacity, knowledge, skills or experience to manage the WRIF all in house.

b) Outsourcing all of the pillars may not be the most attractive option to the market as the types of proposed investment and scale of businesses to be supported is varied and the market engagement completed to date indicated that multiple fund managers or specialist would be required. Outsourcing all may also not be justified in terms of costs – the size and activities of each proposed pillar are different, and the volume of potential investment opportunities is expected to differ also. It is also anticipated that the scale of the WRIF will take time to build up and on this basis, there may not be justification for the costs of procuring and setting up an external fund for its initial operation. The potential market for each pillar is also different and it is unlikely that a single fund manager would have the knowledge and experience to operate across the 3 areas.

c) The Council are likely to want the flexibility to have a mixed economy of management support that secures the advantages of external expertise, resource, capacity, and knowledge of sectors and the investment market but which provides some involvement and control for the Council plus the opportunity for skills transfer too. A mixed economy option is also tailored to where knowledge, resource and skills are required to ensure the due diligence and management of risk is effective and appropriate to the scale and associated risk of investment.

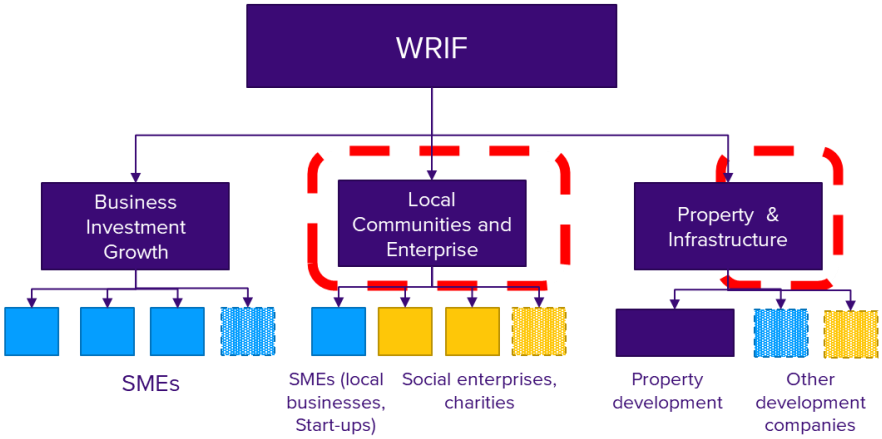
d) A mixed economy option provides the option of scaling up the management arrangements – starting with internal management and then moving to external management to get wider expertise where and when appropriate.

e) A mixed economy option provides the opportunity to leverage private sector finance when funds are delivered externally or in partnership.

## THE PREFERRED OPTION

152. Using the decision criteria across a three-decision staged approach it has been determined that **Option 7 – Establishing a WRIF with a three-pillar structure and a mixed economy of fund management is the preferred option**. A visual of this option is shown in the diagram below:

## Option 7: WRIF mixed economy




Mix of in house and outsourced. This is illustrative and actual mix to be determined by market engagement

153. The red boxes in the above diagram are indicative only to illustrate the parts of the fund which may be managed externally.

### WRIF INVESTMENT CRITERIA

154. All investment decisions that are to form part of the WRIF will be assessed against a set of predetermined criteria that covers both its strategic alignment with the Fund objectives and whether it meets financial, economic, and social value, and environmental criteria that will be set differently for each of the three funds.

155. Across the three pillars, particular focus will be given to investment opportunities that:

- Stimulate job creation of skilled or entry level jobs in the county
- Can or will leverage additional resources or funding
- Increase social value – where the investment brings benefits to local residents, removes barriers to employment, supports health and well-being, protects and enhances the natural environment, creates better places to live and/or maximises opportunities to strengthen community capacity and resilience.

Investment Priorities

156. The WRIF will also be used to accelerate and promote investments in **priority sectors** (those sectors considered as important for economic growth) and for **priority business** types (the size, scale and type of business activity it is engaged in) and for investments that **enable development**. Separate Priorities will be set for each element or pillar of the WRIF with a focus on:

**The Business Investment Growth Pillar** (BIGP)will focus on growth in order to underpin medium- and longer-term recovery rather than addressing the short-term effects of the pandemic. The

priorities for investment will be **priority sectors** where Warwickshire already has particular strengths and are growing sectors.

**The Local Communities & Enterprise Pillar (LC&EP)** will focus on investment opportunities that address the local challenges and economic and social consequences of the pandemic in the short term. The priorities for investment will be **priority business types** such as new and growing small and medium sized businesses. It will be a closed fund extending no longer than 5 years.

**The Property & Infrastructure Pillar (PIP)** will focus on enabling developments that underpin medium- and longer-term recovery. The priority focus will be on **enabling development** .

157. These criteria are outlined in more detail in the Commercial Case and in full in the WRIF Strategy at Appendix A.

## MEASURING SUCCESS & BENEFIT REALISATION

158. The WRIF will manage all investments by monitoring outcomes against different performance measures. The Fund will be set up to best meet WCC's objectives and support its outcomes around increased GVA, business growth and the creation of new jobs.

159. Initial work has indicated that it is desired for the fund to deliver the following direct benefits (delivered through the WRIF rather than other measures) – these are to be quantified and informed by the market engagement

| 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<br>Number of new start-up businesses / businesses supported<br>Business rates income<br>Council Tax income<br>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<br>Number of jobs safeguarded |
| **Provides employment land and premises;** investment addresses the lack of appropriate employment land and premises in the County | Creation of employment land and premises |
| **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 climate change benefits, carbon neutral and low carbon initiatives | An increase in the use of/public support for low and zero carbon technologies<br>Number of responsible investments |
| **Increases Social Value;** investment brings benefits to local residents by promoting initiatives that increase skills and capabilities, removes barriers to | Poverty premium how may people's lives have they |

| Benefit | Measures & Quantification |
|---|---|
| employment, improves health and wellbeing, protects and enhances the natural environment, creates better places to live and maximises opportunities to strengthen community capacity and resilience. | 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<br>Sq ft of development |
| **Improves connectivity;** improves the county's infrastructure and connectivity to break down barriers to digital inclusivity | Increased network capacity |

160. Further work will be completed and collated within the WRIF Investment Strategy to set out the full set of benefits, measures and quantification.

161. Further detail on the scale of benefits is included in the Commercial Case to help understand the benefits that can be delivered from varying levels of Council investment.

## ECONOMIC RISKS

162. The key economic risks are:

- The Council, via the Fund, is unable to cover the costs of investments and therefore cannot sustain WRIF to deliver benefits in the medium to longer term;
- The Council loses money on investments and this directly impacts on its future ability to meet its MTFS;
- The Fund does not deliver the range of benefits or to the targets that have been set;
- Increasing economic issues/recession require more finance/a larger Fund to support economic recovery;
- Political support for the Fund reduces or changes significantly;
- The current investment market changes and therefore the gap/rationale/focus of the Fund is no longer relevant.

163. These risks will be taken into consideration in the Commercial Case and Financial Case, together with commercial and financial risks, to ensure the preferred option is defined and targets set that give the Council the best opportunity to meet its objectives and deliver against the benefits and outcomes it is aiming to achieve.

## CONCLUSION – PREFERRED APPROACH

164. The preferred approach, and the approach to be taken forward as part of this Business Case, is the option to establish the WRIF with a three-pillar structure and a mixed economy of fund management.

165. This option is the preferred approach because:

- Establishment of the WRIF is aligned with strategic priorities and will enable the Council to have a dedicated fund and a targeted approach to support the economic recovery of the County.
- A do-nothing option, that relies on contributions from the existing investment market and broader government response to the pandemic, has been discounted for not directly contributing towards the Council's aims and objectives or strategic priorities and not supporting a targeted approach to the economic recovery of Warwickshire.
- The Fund will manage investments by monitoring outcomes, be set up to best meet WCC's objectives and will use investment criteria to support its outcomes around increased GVA, business growth and the creation of new jobs.
- The three-pillar structure reflects that the proposed three funds are sufficiently different to require a fund structure that allows different recipients and different benefits to be targeted.
- A three-pillar structure is also expected to be more attractive to the market by allowing specific gaps in the market to be targeted and the skill set for Fund Management to be able to be tailored to the specific requirements.
- A three-pillar structure also ensures that the investment criteria, governance and decision making can be tailored to the scale, type and risk of investment which is expected to differ across each of the funds.
- A mixed economy of fund management secures the advantages of external expertise, resource, capacity, and knowledge of sectors and the investment market but which provides some involvement and control for the Council plus the opportunity for skills transfer too.
- A mixed economy option is also tailored to where knowledge, resource and skills are required to ensure the due diligence and management of risk is effective and appropriate to the scale and associated risk of investment.
- A mixed economy option provides the option of starting incrementally and then scaling up the management arrangements – starting with internal management and then moving to external management to get wider expertise where and when appropriate.
- A mixed economy option provides the opportunity to leverage private sector finance when funds are delivered externally or in partnership.

# 5. Commercial Case

166. The purpose of the Commercial Case is to address any issues of commercial feasibility and seeks to answer the question "can the proposed solution be effectively delivered through a workable commercial deal or deals?"

167. In the case of the WRIF this section outlines the opportunity for, and route to, invest as well as the commercial issues that any decision to invest must address.

168. This section also outlines the types of investment, commercial terms and decision-making process by which all investment opportunities for the WRIF will be assessed together with the fiduciary and commercial considerations the investment opportunities progressed by the WRIF must satisfy.

## MARKET DEMAND

169. Market engagement was undertaken to explore the current investment activity that is supporting businesses in the county. The findings from the market engagement are being used to shape the proposals for the WRIF. It is intended that the WRIF will be designed to complement and enhance the existing investment landscape, to address the perceived gaps in the provision of finance, and not compete with or dilute the role of other Funds already operating in the County or wider region.

170. There appears to be clear demand for finance from Warwickshire businesses: £12m of £85m invested by the MEIF has been into businesses operating in Coventry & Warwickshire. Whilst fund managers do not specifically measure or record investments in Warwickshire as distinct from Coventry, they all indicated that there was a role for the WRIF to provide additional, unmet demand for finance and that additional targeted capital would be beneficial and could be utilised to support the Council's objectives.

171. On the basis of the conversations with fund managers, the main perceived gaps are:

- Business loans between £1.5m and £5m
- Start-up finance
- Capital with longer term payback than is traditionally granted by banks e.g. 3-5 years
- Equity/mezzanine finance
- Management buy-out or company refinancing.

## FUND STRUCTURE

172. The preferred approach determined in the Economic Case is to establish a three-pillar structure within which the WRIF which will act and be treated for governance purposes as an overarching Fund portfolio.

173. The three pillars proposed to operate within the WRIF are:

- Business Investment Growth Pillar
- Local Communities & Enterprise Pillar
- Property & Infrastructure Pillar

174. Each Pillar is proposed to have a different focus, different investment criteria, different types of investment, different management arrangements and different target beneficiaries and outcomes. Further detail on each of these Pillars is provided in the following sections.

175. Warwickshire Property Development Company (WPDC) will also contribute towards the Property & Infrastructure Pillar, however WPDC has its own separate Business Case and Business Plan and does not therefore form part of this Business case.

## SUMMARY OF THE FUNDS

176. A total fund size of c.£140m is proposed across the three pillars. The overall single fund is flexible, so these amounts are movable between funds based on market need and changes in economic and financial conditions.

177. A breakdown of the total portfolio is as follows:

- £90m for the Business Investment Growth Pillar
- £10m for the Local Communities & Enterprise Pillar
- £40m for the Property & Infrastructure Pillar

178. In reflection of the feedback from the market engagement, the following tables summarise the key features and proposed terms for each individual fund operating within the WRIF. Further detail on each individual fund is then provided in the paragraphs below.

*Table 1 -Investment Priorities*

| Name | Description | Priorities |
|---|---|---|
| **Business Investment Growth** | Finance for growing businesses with sound prospects | Priority industries<br>• automotive technology,<br>• advanced manufacturing and engineering,<br>• digital creative/video game development<br>• tourism and hospitality<br>• logistics<br>• house building/ modern methods of construction (MMC)<br>• 'green' /sustainable technologies or industries<br>• rural industry and enterprise<br>• social care or other supply markets of the Council<br>• Any new sector that creates skilled or entry level jobs |
| **Local Communities & Enterprise** | Aimed at addressing local challenges and the economic and social | Priority business types<br>• New and growing SMEs |

| Name | Description | Priorities |
|---|---|---|
| | consequences of the pandemic | • Small, local businesses that support social capital<br>• Start ups<br>• Social enterprises<br>• Environmentally and/or economically sustainable businesses that are driving climate change benefits, cardon neutral and low carbon initiatives<br>• Those businesses that create entry level jobs and/or increase skills<br>• Those businesses where investment will improve high streets and town centres |
| **Property & Infrastructure** | Provide loans to invest in commercial sites, premises and infrastructure. Support viable developments to underpin economic recovery | Priority is on enabling development:<br>• Supporting viable external led schemes where they fit the investment strategy |

*Table 2 -Key Investment Features*

| Name | Indicative fund size | Investment size & volume | Investment term | Investment type |
|---|---|---|---|---|
| Business Investment Growth | [£90m] | <£10m (Approx. 2-5 per annum. Low number of high value loans) | Up to 10 years | • Predominantly commercial loans<br>• Management Buy Outs/ Acquisitions / Refinancing |
| Local Communities & Enterprise | [£10m] | <£1m (Approx. 10-30 per year. Higher volume, lower value loans) | Up to 5 years | • Commercial loans<br>• Equity investment<br>• Co-investment with social investment partners<br>• Other more innovative products |
| Property & Infrastructure | [£40m] For investments that sit outside WPDC | <£40m | Up to 10 years | • Commercial loans<br>• Equity investment<br>• Corporate guarantees<br>• Joint Ventures |

## THE FUNDS IN DETAIL

Business Investment Growth Pillar

179. The Business Investment Growth Pillar will **focus on growth in order to underpin medium- and longer-term recovery** rather than addressing the short-term effects of the pandemic. The priorities for investment will be **priority sectors** where Warwickshire already has particular strengths and are growing sectors.

180. This Pillar is most closely aligned with the following in the current investment market:

- Debt finance between £100k and £1.5m offered through the MEIF by the Maven CP fund manager
- Frontier Development Capital for mid-market SME with debt finance up to £7.5m.

181. The gaps this pillar would be addressing as identified by the market engagement are:

- A scarcity of funding for Warwickshire businesses in the £1.5m to £5m debt space 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 are 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.

182. The market engagement exercise confirmed that there is demand for investment in this area. 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.

183. The proposed size for this 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.

184. The proposed size is £90m with individual investments up to a limit of £10m. The type of investments will be predominantly commercial loans with investment into sound and established businesses which require capital to grow and where Warwickshire already has particular strengths.

185. Considering the size of individual investments, it is anticipated that there will be a low number of higher value loans with approximately 2-5 successful investments approved per annum.

186. Due to the smaller volume of loans and the predominance of more straightforward commercial loans as a type of investment it is recommended, in the first instance, that this Pillar could be managed internally by the Council with the support of a range of legal, financial, commercial and technical external advisors as required. MBO and acquisitions require more specialist skills and if this is an area that the Council would like to provide support in further work should be done on how best to deliver this type of finance.

187. For the remaining finance options in this pillar there is an existing market for fund managers operating at the lower levels of investment (<£10m) and if the Council found there was a higher

level of demand or demand for more complex products, it is possible that an external fund manager could be engaged at a later stage.

**Local Communities & Enterprise Pillar**

188. The Local Communities & Enterprise Pillar will focus on investment opportunities that address the local challenges and **economic and social consequences of the pandemic in the short term**. The priorities for investment will be **priority business types** such as new and growing small and medium sized viable businesses.

189. This Pillar has similar characteristics to a number of other funds operating in the region, including those supported by the Council (through CWRT) and through the MEIF. These characteristics include:

- Capital loans up to £75k – operated by CWRT on behalf of the Council
- Proof of concept – early-stage equity finance up to £750k operated by Mercia as part of the MEIF
- Equity finance - later stage equity finance up to £2m operated by Midven as part of the MEIF
- Debt finance - business loans up to £1.5m operated by Maven CP as part of the MEIF
- Small business loans – up to £150k operated by BCRS as part of the MEIF.

190. However, market engagement identified that within the space of the Local Communities & Enterprise Pillar there remain some areas where there is believed to be unmet demand (definitions for these terms are included in the glossary):

- Debt finance for micro-businesses (<10 employees)
- Start-up equity
- Mezzanine finance

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

192. There is the potential opportunity for the Council to consider expanding the current arrangements and increasing the amount of finance allocated to the Coventry and Warwickshire Reinvestment Trust. This opportunity will be tested via further market engagement.

193. The market engagement did not identify any insights on the social enterprise space as the existing providers have no previous experience in this space. It is intended that this aspect of the fund be further tested during the second stage of the market engagement.

194. Whilst the 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.

195. The proposed size of £10m 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.

196. This pillar is intended to operate as a closed fund with a investment horizon limited to 5 years.

197. The proposed size is £10m with individual investments up to a limit of £1m. Investments are likely to be relatively small in size and given to a broad range of organisations which may include social enterprises and potentially individuals. There is also expected to be a broader range of types of investment to enable it to deliver the interventions that the market requires.

198. There is anticipated to be a higher volume of lower value loans in the region of approximately 10 -30 investments approved per annum, with an average size of c.£100,000.

199. Considering the focus on the short-term impact of the pandemic and drive for economic recovery, and due to the broader types of investment, higher volume of loans and objective to deliver finance in the short term it is recommended that this Pillar is externally managed. The types of finance proposed to be offered is quite wide, requiring different skills sets to operate and this would be difficult for the Council to manage. This approach will allow the Council to engage market specific advice and additional support to undertake the level of due diligence required for potentially higher risk investments.

200. The Council's legal advisors have also provided the following advice that provides additional rationale for the management to be external:

*The investment activities for WRIF that may move us close to the territory of consumer lending and these must be kept under close review to ensure that we do not stray across the lines. The most obvious area of risk is any lending to small businesses who may be sole traders and the most likely theme where this could arise is in relation to the Local Communities and Enterprise investments. Although there are specific exemptions to FSMA 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.*

201. In consideration of the above, it is recommended that the Council look to work with a regulated entity in order to administer the LC&EF pillar. This would enable the Council to contract with the third party in order to rely on their existing FCA authorisation and for the Council to indirectly fund regulated loans if required.

202. As such, it is clear that the appropriate approach would be to seek external FCA regulated advisors to manage this Fund who will be qualified to undertake the appropriate level of due diligence required.

203. Given this variety of skills and potential for regulated activities it is unlikely that any single fund manager would offer the full suite of financing offers proposed. Further work is required to

establish the exact market offer but it is likely that equity products would need to be offered to the fund management market separately to debt finance; and starts-up as well as social enterprises would each require a specific focus/fund manager. Fund managers felt that the minimum size of fund they would be interested in operating was around £20m unless it aligned with an existing fund with a team already on the ground. The Council will therefore need to consider:

- The size of this pillar given market demand, the higher risk profile, and the broader needs of the applicants;
- How/if to allocate investment across the components;
- Phasing the introduction of this pillar, perhaps focussing on a specific type of finance of business first whilst aiming to maintain as much flexibility as possible going forward;
- Collaborative (perhaps specific in the contract) or adviser/partnership arrangements across fund managers.

**Property & Infrastructure Pillar**

204. The Property & Infrastructure Investment Pillar will focus on enabling developments that underpin medium- and longer-term recovery including the provision of housing across a range of tenures. The primary focus will be on **enabling development**.

205. Market engagement has 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. Though, no information was available on the demand for investment in this area from Warwickshire specific businesses.

206. It is anticipated that this Pillar will initially be established and managed by the Council. However, it is accepted that Council may not have the in-house capacity, regulatory requirements or skill sets to undertake the work required to gain the most out of this Fund.

207. The Council may elect to procure fund management services for this Pillar. The nature of the likely investments and the potential to attract and leverage other investment means that a Fund Manager may need to be regulated by the Financial Conduct Authority (FCA); however, these requirements will be tested with the market.

208. This Pillar has a broader aspiration to enable development in the County beyond that of WPDC.

209. The Pillar is set up to target projects which are key to delivery of the County's growth, in support of innovation, business growth and regeneration. It will address funding market failures, accelerate and increase investment in private sector led development and site-specific infrastructure. The pillar provides the Council with the necessary finance to unlock projects, with the risk managed in accordance with a pre-approved Investment Strategy.

210. An amount of £40m has been identified through market engagement as a minimum amount that would provide a sufficiently robust fund to meet the wider needs of the county's Property Market. Evidence of similar Funds set up at a regional level suggest that this amount of resource could typically attract an external fund manager and leverage a similar amount of finance to provide greater reach.

211. As previously noted, the Council should consider further whether there is sufficient unmet demand to offer finance more widely to Warwickshire businesses undertaking development projects in the County and this may be more appropriately offered through an external fund manager.

## SCALE OF BENEFITS

212. Defining the potential benefits of the WRIF will, in part, depend on the level and nature of support given to specific businesses. However, it is possible to draw conclusions about the potential benefit the WRIF could bring to the county by assessing the impact of other regional funds.

213. The European Regional Development Fund (ERDF) focuses investment on a range of priority areas to redress the balance between richer and underdeveloped regions in the EU in order to allow those underdeveloped regions to attract private sector investments and create jobs on their own. ERDF have prepared a series of 'ready reckoner' (standard numerical calculations) that can be used to facilitate an assessment of the level of benefits investment can bring.

### Direct Benefits

214. Using 'ready reckoner' metrics from ERDF it is possible to illustrate an estimate of the scale of direct benefits that the WRIF may be able to deliver according to the proposed size of the fund and individual pillars of investment. The table below indicates the potential range of benefits the WRIF as a portfolio fund at £140m could deliver:

**WRIF - £140m**

| Projected outcomes | Summary |
|---|---|
| Jobs created | 2,500 - 3,400 |
| Jobs safeguarded | 2,700 - 3,900 |
| Annual regional GVA (£m) | 110 - 160 |
| Number of Businesses supported | 118 |
| Private sector leverage (£m) | £78 - 104m |
| Public sector leverage (£m) | £26 - 35m |
| Land remediated (hectares) | 15-23 ha |

215. These figures can be further broken down to demonstrate the scale of direct benefits that the WRIF could deliver between each of the individual pillars proposed as is shown in the tables below.

**Business Investment Growth (£90m)**

| Projected outcomes | Range |
|---|---|
| Jobs created | 1,800 – 2,400 |
| Jobs safeguarded | 2,200 – 3,200 |
| Annual regional GVA (£m) | 86 - 116 |
| Number of businesses supported | 18 |
| Private sector leverage (£m) | 70 – 95 |
| Public sector leverage (£m) | 23 - 32 |

**Local Communities and Enterprise (£10m)**

| Projected outcomes | Range |
|---|---|
| Jobs created | 207 – 263 |
| Jobs safeguarded | 247 - 350 |
| Annual regional GVA (£m) | 9.5 - 13 |
| Number of Businesses supported | 100 |
| Private sector leverage (£m) | 7.5 - 11 |
| Public sector leverage (£m) | 2.5 - 3 |

**Property & Infrastructure (£40m)**

| Projected outcomes | Range |
|---|---|
| Jobs created | 500 - 760 |
| Jobs safeguarded | 270 - 420 |
| Annual regional GVA (£m) | 20 -30 |
| Land remediated (hectares) | 15 - 23 |

Indirect Benefits

216. It is also important to recognise that the WRIF will support the delivery of a range of indirect, and non-cashable, benefits to the Council, the wider Public Sector, and the county as a whole.

217. As well as measuring the total number of jobs created by the fund, i.e. the cost per job created, it is also worth considering the costs avoided by safeguarding jobs that, if lost, could lead to an increase in subsequent unemployment. When a job is lost there is the potential for additional costs to be felt throughout the public sector purse, most obviously through unemployment support. However, costs can also increase as a result of the need for supported housing, deterioration in health standards and in some case a reduction in educational standards to name but a few. All of these can lead to higher whole life costs as a result of moving from employment to unemployment.

218. Although this metric does not offer the Council any direct return from the investment, it is delivering cost savings to the public purse from employment itself as well as improved health

outcomes and reductions in crime etc. Public Health England in their Moving into Employment Report conclude that employment 'has been shown to improve the wellbeing of individuals, their families, and their communities from both an economic and a quality-of-life standpoint' (Public Health England, Moving into Employment 2017)

219. This is particularly relevant in making the case for investment and accepting that there may be the potential for net loss from some elements of the fund. Any proposed net loss can be balanced by consideration of the cost per job saved (to the public purse) as well as the other wider social and economic benefits of people remaining or returning to employment.

## FUND MANAGEMENT

220. The preferred approach determined in the Economic Case is to set up a mixed economy model where the Council internally manage some aspects of the fund, with the support of external advisors, and outsource other parts of the fund to be managed by an external Fund Manager(s).

221. It is proposed that the Business Investment Growth pillar is managed inhouse by the Council with support from external advisors.

222. It is proposed that the Local Communities & Enterprise pillar and any investments that within the Property & Infrastructure pillar will be managed by an external Fund Manager(s).

223. Flexibility for the WRIF to adapt to respond to the market and scale up and down to reflect demand will be important and therefore the management arrangements may adjust as the scale of the Fund increases.

224. Further detail on the management of the WRIF is provided in the Management Case.

## TYPES OF INVESTMENT

225. The Council's legal advisors have recommended that the scope of the WRIF is kept as broad as possible to enable it to deliver the interventions that the market requires.

226. The types of investment that the WRIF will predominantly undertake are commercial loans to businesses within the County that are focused on the key priorities, or that support and enhance the overarching objectives of the Fund;

227. However, the Council will also consider opportunities that require the following types of investment and a decision will be made on a case-by-case basis considering the market, due diligence, assessment of risk and the potential reward/outcomes to be delivered from the investment (definitions for these terms are available in the Appendix):

- Mezzanine Finance;
- Investment in company equity, for example in start-up companies;
- Co-Investment – capital or equity – with other Funds or individual investors;

- Purchase of assets: Including housing, [residential] commercial/retail property, land or infrastructure where it can be shown to meet the funds objectives and is in line with PWLB lending requirements;
- Partnerships to leverage additional private sector resources (skills or finance);
- Management buy-outs/acquisitions;
- Corporate Guarantees; and
- Other more innovative products that allow start-ups to repay once they are successful e.g. debts convert to equity or loan repayment 'holidays' for 2 years

228. The type of investment to be undertaken is expected to differ between each individual pillar and has been determined using the feedback from the market engagement, legal advice and accounting considerations as well as from discussions with Council officers. The predominant (but not exclusive) types of investment for each individual pillar are expected to be:

| Business Investment Growth | Local Communities & Enterprise | Property & Infrastructure |
|---|---|---|
| • Commercial Loans<br>• Management buy/outs acquisitions/ refinancing | • Commercial Loans<br>• Equity Investment/Mezzanine Finance<br>• Co-Investment | • Commercial Loans<br>• Equity Investment<br>• Purchase of assets<br>• Corporate Guarantees<br>• Partnerships (Joint Venture) |

229. The most appropriate source of funding for each individual investment will be determined on a case-by-case basis at the time of the investment decision making when the individual opportunity is being reviewed by the Investment Panel via consideration of an Investment Business Case.

## COMMERCIAL TERMS

230. It is proposed that the WRIF will operate with a total investment portfolio size up to [£140m]. The portfolio size indicates the maximum expected exposure of the Council to the activities of the WRIF.

231. From the overall portfolio an allocation will be made to each individual Fund accordingly:

- Business Improvement Growth Fund [£90m]
- Local Communities & Enterprise Fund [£10m]
- Property & Infrastructure Fund [£40m]

232. The Fund, as a whole is designed to be flexible and responsive to market needs. If after an assessment of risk and affordability it is felt that these allocations should change to meet demand,

then this will be addressed by a recommendation of the Investment Panel to Cabinet as ultimate decision maker.

233. Each year Full Council and Cabinet will approve:

- the relevant annual budgeted amount for the WRIF;
- review and agree any allocation, if appropriate, across each of the three pillars;
- set out the WRIF's authority to operate the fund(s) via the Investment Panel for the next year; and
- the key priorities and themes for investment, should these have changed from the prior year.

234. There will be alignment between the operations of the WRIF and the statutory Investment Strategy and Treasury Management Strategy agreed by the Council.

235. For elements of the fund that are to be internally managed, the investment decision making will be referred to Cabinet with a recommendation from the Investment Panel for consideration.

236. For those pillars under the WRIF that are proposed to be externally managed, the investment decision making will be under the remit and control of the Fund Manager subject to the terms of the contractual arrangement between the Council and the Fund Manager. Authority will be given to the Fund Manager to make individual investment decisions up to the limit of that individual fund and performance against agreed targets will be set out in the contractual agreement.

237. The Fund will seek to operate on the following basis:

- Make investments where they meet the investment criteria and the objectives of the Fund and the financial return is commensurate with the level of risk taken
- Offer a flexible approach to financing designed to reduce the impact of market failures, increase economic resilience, and accelerate the delivery of projects
- Seek full recovery of costs
- Seek to generate financial returns (over and above costs) to continue to meet the overarching objectives of the Fund through reinvestment or on permitted uses
- Operate alongside other wider funding streams to accelerate economic recovery and/or the delivery of schemes
- Leverage private sector investment into priority areas of growth
- Manage risk at a portfolio level to give the Council the ability to invest in some moderately higher risk activities, where these risks are offset against some lower risk opportunities
- Use external Fund Management expertise where required to source investment opportunities, undertake due diligence to support decision making, allocate funding and manage and monitor the performance of the Fund in line with the investment criteria

238. The fund will operate on a commercial basis and should not be investing into financially unviable schemes or providing grant. It is envisaged that if a project requires grant to realise its benefits, these funds will be made available from a different source.

239. Investment proposals that the Council wishes to progress but that are considered to be outside the remit of the WRIF, to not meet the investment criteria or to exceed the financial delegation thresholds will be referred to Cabinet for a decision.

240. The duration of the Fund and closure of the Fund will form part of a recommendation by the Investment Panel to Cabinet. It is suggested that the period of investment decision making for the Fund would operate initially for up to 5 years, with annual performance reporting, at which point the Investment Panel would undertake an assessment of the effectiveness of the Fund as a tool to continue to support delivery of the Council's objectives.

241. The exit strategy for an individual investments, as well as closure of the Fund as a whole, will need to be clearly determined and the contractual ability for the Council to close the Fund enabled throughout all contractual specification and documents.

242. A Member Oversight Group will be established for the scrutiny of investment decisions where quarterly monitoring reports will be referred and any individual investments or investment decisions can be referred for further scrutiny.

## IDENTIFYING OPPORTUNITIES

243. It is anticipated that a large proportion of the potential investment opportunities available to the Fund will be gained by directly engaging with the local market. Where external Fund Management is in place it will be the role of the Fund Manager to source opportunities using their network. In addition to this a detailed marketing strategy and associated website will be developed that sets out the nature of the fund and pillars, its focus and priority areas and the nature of the investment it is likely to make. This will promote the fund locally and be used to source investment opportunities.

244. In addition to the in-house team that will be established for operation of the WRIF, the Council's Economy & Skills Group, Business and Economy Team and the Business Support Programme that is already established and operated by the Council will support the identification of opportunities by signposting local businesses to the Fund.

245. The Council may decide to establish 'invitation to bid' windows to ensure that a mix of investment opportunities are sourced together so they can be considered alongside each other and against the WRIF Strategy criteria rather than in a piecemeal fashion. This approach may also ensure more effective resourcing of the Sift and Business Case process.

246. There is also an aspiration from the Council plus feedback from the market engagement that an incubator and/or accelerator programme is desired to help start-ups develop a viable investment opportunity and advance the growth of existing companies. The Council will consider the opportunity to create an investor support programme. There is also an existing portfolio for Business Centres and the potential opportunity to combine this offer with incubator/accelerator

support will be explored further via the WRIF. If established this could also be a source for identifying opportunities.

## RESOURCES

247. The Council will establish an in-house team for the WRIF that will operate alongside the existing Business & Economy Team and the Business Support Programme that is already established and being operated by the Council. The in-house team will be responsible for managing the Business Investment Growth pillar and any other elements of the WRIF that are to be internally managed and will report into the Investment Panel that will be established for decision making and management and monitoring of the WRIF.

248. There is anticipated to be one main role of Investment Manager that will be responsible for identifying investment opportunities and developing the business cases for these investments for Investment Panel consideration. This role will need to be resourced appropriately for the WRIF to operate effectively and as the Fund scales up in size there may need to be more than one of this role in the team.

249. To support the initial assessment of bids it is recommended that an IT solution is developed or procured to allow potential investment opportunities to be submitted through a portal; allowing for consistency of information at an early stage.

250. The Investment Manager would be a member of the Investment Panel and will present the investment business case for all investment opportunities that are seeking approval and will report on the financial and non-financial performance of individual investments and the WRIF portfolio overall.

251. The in-house team would also include Business Advisor roles that would signpost potential applicants to the fund, support investor readiness via incubator/accelerator programmes and spend time with investees to fully understand the business proposition prior to business case stage. These support programmes will be part of the remit of the Fund as a whole and will be funded via the operating costs of the Fund.

252. The in-house team will be supported by a team of external legal, banking, and technical specialist advisors that will need to be sourced externally to the Council. The Council has access to a number of panels and frameworks that may be suitable to source these resources from as well as the option to secure additional resources via direct recruitment.

253. Further detail on these roles and the external advisors required is set out in the Management Case.

## INVESTMENT CRITERIA

254. A WRIF Strategy that sets out the objectives, priorities, type of investment and criteria for assessing investment opportunities is to be approved. This document is included at Appendix A.

255. These investment criteria are to be tested with the market as part of the next stage of market engagement.

## DECISION MAKING PROCESS

256. It is proposed that the WRIF is to have a mixed economy of Fund Management with some elements of the Fund managed in-house, with the support of advisors, and some outsourced to external Fund Managers. The WRIF Strategy will form the basis of the criteria for all investment decisions but there will be an alternative set of arrangements as options for consideration in the business plan, and approach to decision making depending on the management arrangements for each Fund/element of the WRIF.

257. The Council's legal advisors have confirmed that the Cabinet and Council have wide scope to delegate most of their respective functions (relating to the operation of WRIF) to officers and/or relevant sub-committees should it wish to do so.

258. It is proposed that an Investment Panel (an officer body) is established to monitor the performance of the WRIF at a portfolio level and also to guide and make recommendations on any investment decisions that are to be managed in house, with Cabinet making the final decision to invest.

259. The Investment Panel will refer all investment decision making to Cabinet together with a recommendation that reflects the due diligence undertaken and investment business case made. All investment decision making is to be aligned with the WRIF Strategy.

260. A Member Oversight Group will be established for the scrutiny of investment decisions where quarterly monitoring reports will be referred and any individual investments or investment decisions can be referred for further scrutiny.

### Existing Governance arrangements

261. The WRIF will need to operate alongside existing Council governance, particularly the Business and Economy Team but will also seek to complement the governance arrangements and proposed to be put in place for WPDC.

262. The WRIF and WPDC Member Oversight Group could operate as one governance forum, established to monitor performance, achievement against objectives and to scrutinise any decision making as required.

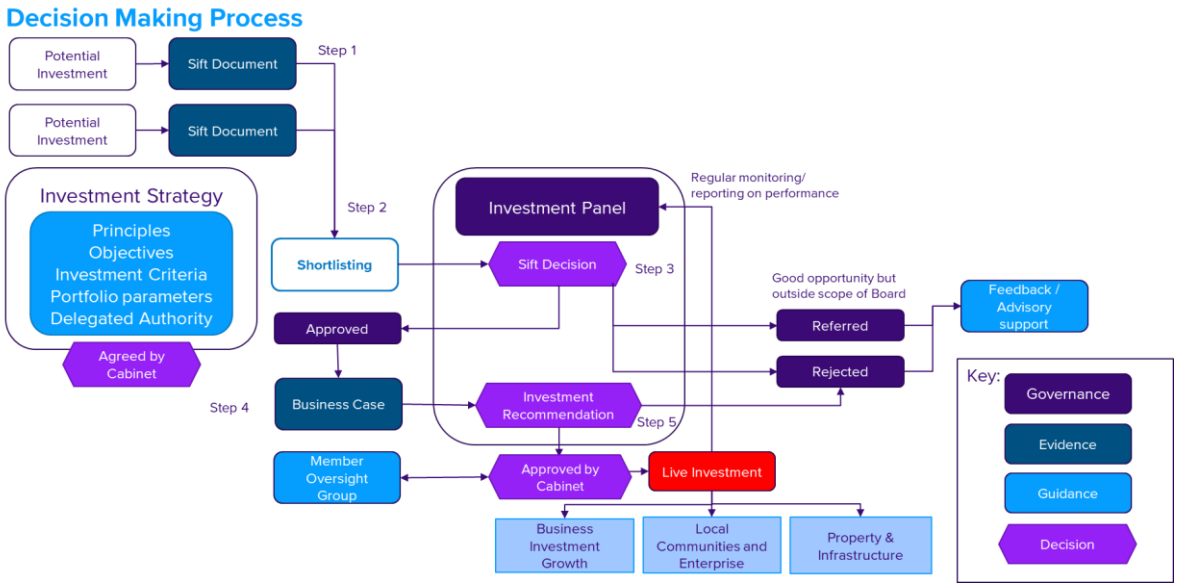
### Decision making - Internal Fund Management

263. The Council's Legal advisors have indicated that Members (and reports to them) should address not only the potential benefits of the proposed fund but also the Council's objectives in relation

to them (e.g. support local economic development); potentially why other options to secure these objectives have been discounted and also the risks of adopting this approach (together with any strategies to manage such risks). This is fundamental to ensure that the Council properly fulfils its fiduciary responsibilities as regards its budget and the money proposed to be invested. Members must have sufficient information to make appropriate and rational investment decisions.

264. In consideration of this advice, we are recommending a robust Sift and Business Case approach to support investment decision making for those elements of the Fund that will be managed in house.

265. The process for making investment decisions is outlined in the diagram below:




266. Each step is described further here:

1. **Step 1 – Prepare a SIFT Document:** a short Sift Document should be completed to outline the potential opportunity at a high level
2. **Step 2 – Sifting process:** The Investment Manager reviews all Sift Documents against the WRIF Strategy and provides a shortlist of potential investments to the Investment Board
3. **Step 3 – Investment Panel Review**: Investment Panel reviews the shortlisted Sift Documents and rejects or approves them to move to Business Case stage
4. **Step 4 - Prepare Business Case:** An investment Business Case is prepared by managers of potential investments in conjunction with the Investment Manager
5. **Step 5 - Investment Panel Decision Making:** Business Case presented to Investment Panel and if appropriate criteria are met, a recommendation is made and the investment is then referred to Cabinet to then approves or reject it for funding. If approved, the investment becomes part of the WRIF.
6. Any individual investment decisions can also be referred to the Member Oversight Group for further scrutiny if required.

267. The key information that should be included within the Investment Business Case is:

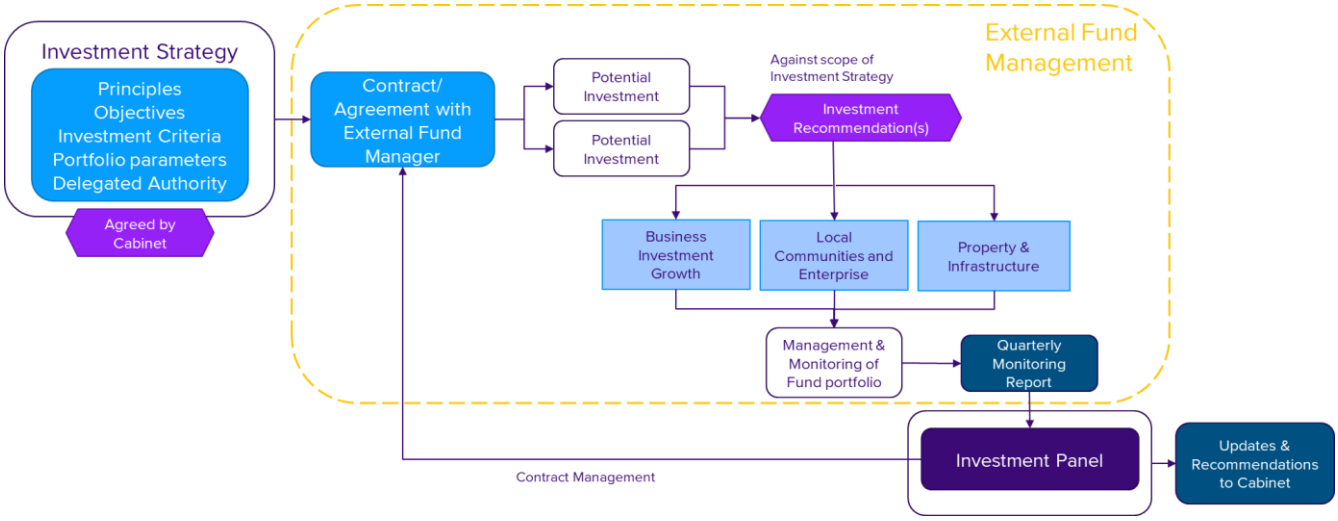
- Outline of investment opportunity, including total value, investment proposer, date of submission, overview of opportunity, etc;
- assessment of strategic fit;
- assessment against Investment Criteria (as set in WRIF Strategy), including quantifiable metrics and how the investment meets Council objectives and PWLB lending criteria;
- proposed source(s) of funding;
- financial model of investment, including cash flow, peak debt, etc;
- investment duration;
- exit strategy;
- commercial considerations (vires, state aid, etc.);
- risks and risk management arrangements split into (1) risks to the borrower and (2) risks to the lender;
- management and monitoring arrangements; and
- recommendation and key considerations.

Decision making - External Fund Management

268. The involvement of the Council in investment decision making will be reduced where the management of pillar or elements therein is outsourced via an External Fund Manager(s).

269. The process for making investment decisions under an outsourced fund is outlined in the diagram overleaf:

270. A key issue for further consideration is whether to give an external fund manager delegations to a set level and then reporting into the Council or require all decisions to be brought by a fund manager to the investment panel for onward recommendation to Council.



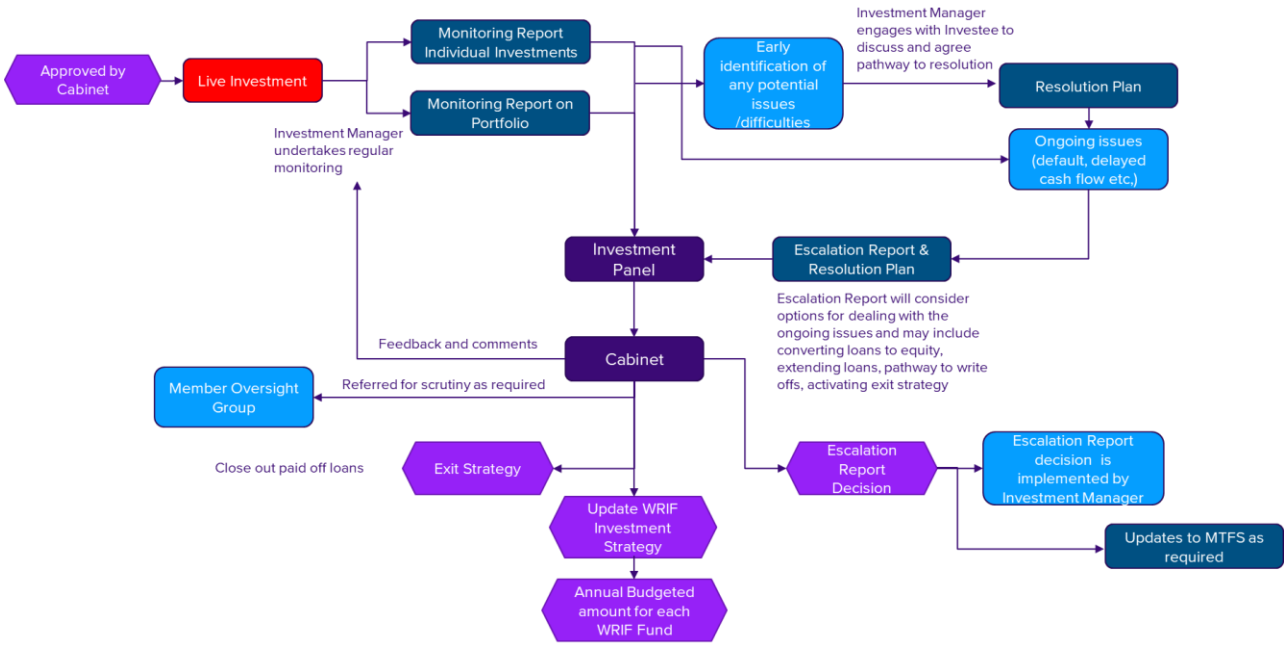

Unsuccessful Investments - Feedback/Advisory support

271. The Council are very keen to support potential investees where their investment proposal is closely aligned with the objectives of the Fund but perhaps doesn't meet the investment criteria. There is an opportunity for those investment opportunities that are rejected to be provided:

- Feedback on the proposal and perhaps the opportunity to resubmit following some additional advisory support
- Access to Advisory support via incubator/accelerator programmes or for example the LEP growth hub, to provide the following:
    - Support preparing revised proposal
    - Guidance and signposting to other potential sources of funding
    - Other advice on business resilience

Managing Investments

272. The following flow chart indicates the type of process that would be undertaken by the Council in managing investments once they have been approved.



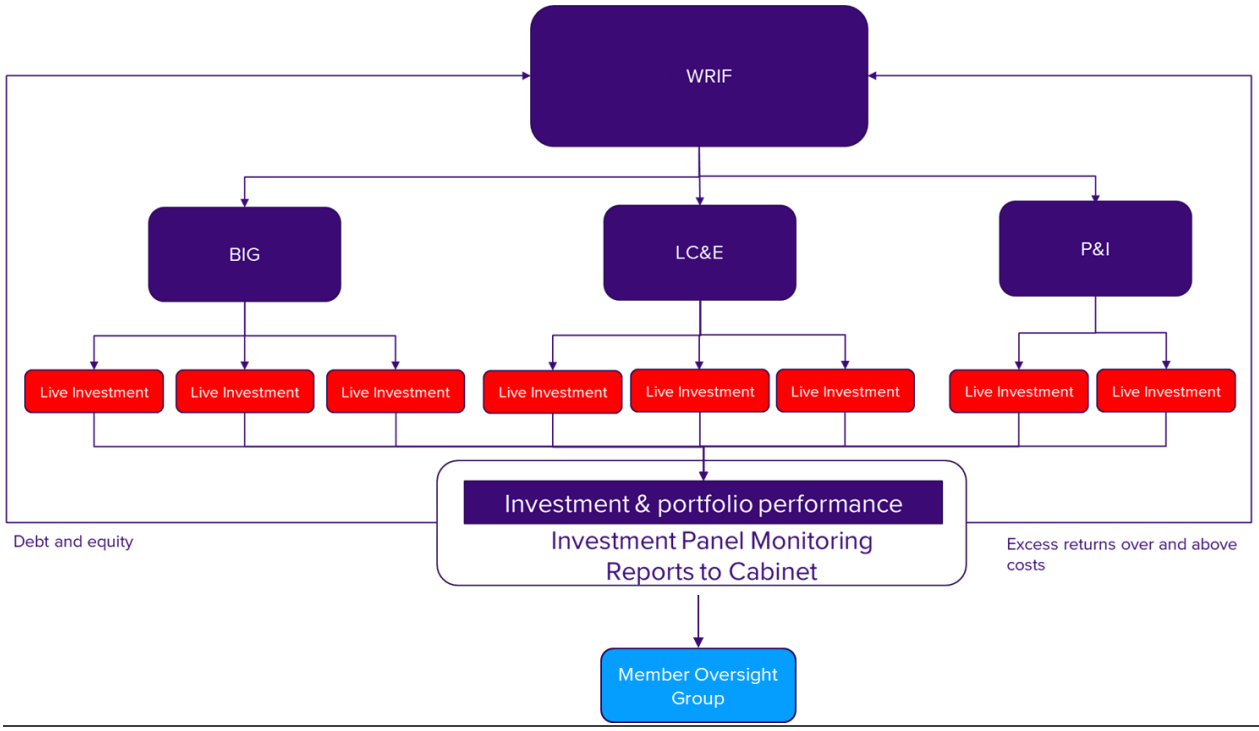

273. The Investment Manager will be responsible for monitoring all live investments and providing monitoring reports to Investment Panel, Cabinet and Member Oversight Panel as required. Challenge to the investment arm and advice to the Investment Panel will be provided via the finance team through a risk focussed role(s).

274. For any instances where potential issues/difficulties have been identified by the Investment Manager in the performance of a live investment they will engage with the investee in the first instance to understand the potential cause of the issues and to agree a Resolution Plan to resolve them.

275. Where there are ongoing issues with a live investment and the potential for default/delayed cash flow etc and Escalation Report and Resolution Plan will be reported to Investment Panel, Cabinet and Member Oversight Panel as required.

Performance monitoring

276. Once the investment has been made, the following governance process applies for monitoring the performance of individual investments and the fund as a portfolio:




277. Once an investment is agreed and live, the progress is monitored regularly by the Investment Manager and external Fund Managers with regular reports to the Investment Panel and quarterly performance reports to Cabinet and Member Oversight Group.

278. Debt or equity funding is repaid back into the WRIF at the level of return and cash flow specified. After the costs are repaid, returns generated are fed back into the WRIF and any excess retained for reinvestment into the fund.

279. In both internally managed and externally managed arrangements, individual investment performance will be regularly monitored to ensure it continues to meet or deliver the WRIF objectives.

Exit Strategy

280. Establishment of robust monitoring and appropriate exit strategies will also ensure that the Fund remains affordable to the Council throughout the duration of an investment.

281. For all elements of the fund where the management is in-house, Cabinet will have the authority to exit any individual investment subject to the implications of that exit. The exit strategy could

be executed at the end of the investment period or due to a non-performing investment - for example if, following performance monitoring, the investment is determined to not be performing in line with the expected Return on Investment or other key indicators. An exit strategy may also be executed when an investment has met or exceeded its profit target or return on investment if it is deemed commercially advantageous to do so.

282. For all elements of the fund with external management, the authority will be granted to the Fund Manager to determine the appropriate exit strategy for individual investments and to exit any investments at the most opportune and appropriate stage.

283. In any instances where the exit of an investment has potential negative consequences, reputational risk or adverse impact on the financial sustainability of the Fund as a whole, the decision to execute the exit strategy will be considered by Cabinet for a decision.

284. The annual review (or more frequent) provides an opportunity for the Cabinet to consider whether to continue with the fund in future years. This would not only take into account the performance of the pillars but also whether market conditions continued to support the need for the WRIF in part or full.

## PROCUREMENT

285. A procurement exercise will be undertaken to secure Fund Management services to support delivery of elements of the WRIF where it is considered that the type of investment, volume of opportunities, due diligence and/or resource and skills required justify the costs for external management. Consideration as to the structure of this procurement exercise is being undertaken.

286. The broad services expected from external Fund Management are:

- Sourcing investment opportunities
- Support to businesses in developing viable business/investment propositions
- Evaluating applications
- Due Diligence & Business Case preparation
- Investment appraisal
- Investment decision making & allocating funds
- Valuation services (tbc)
- Fund Management
- Performance Monitoring

287. It is anticipated that there will be a requirement for more than one external Fund Manager across the WRIF in order to support operation of the Local Communities & Enterprise pillar and the Property & Infrastructure pillar although this element may not operate from day one.

288. In consideration of the feedback from the market engagement there is the possibility of separate Fund Managers being required for operation of the Local Communities & Enterprise pillar where

there is a broader range of recipients, outcomes, and types of investment. The different management could be with a focus on:

- Start-ups;
- Micro Businesses; and
- Social Enterprise.

289. A soft market testing exercise will be undertaken to refine the details of the Fund, shape the procurement strategy, determine the role of the Fund Manager and the scope and services that can be procured externally. This exercise will also help to provide challenge to the Council's investment criteria and performance and provide some insight into the most appropriate method for incentivising Fund Managers to deliver the priorities of the WRIF. An updated version of the WRIF Strategy will then be brought to Cabinet for approval.

290. The soft market testing will also assist the Council to determine the number of different lots to be procured to reflect the number of external Fund Managers required to support different elements of the Fund in consideration of experience and expertise.

291. It is also anticipated that a procurement exercise(s) may be required to procure some of the advisory resources required to support delivery of the WRIF that will need to be sourced and recruited externally to the Council. The Council has access to a number of panels and frameworks that may be suitable to source these resources from as well as the option to secure additional resources via direct recruitment. However, a procurement exercise may be required to broaden the range of skills available from current existing frameworks.

292. In addition, the Council may decide that an IT solution should be procured to allow potential investment opportunities to be submitted through a portal, allowing for consistency of information at an early stage.

## COMMERCIAL CONSIDERATIONS

293. In addition to the practical mechanisms of investment decision making, including counterparty risk and profile and of return there are four key factors that the commercial case of any investment made by the WRIF must satisfy:

- The Council has sufficient powers to makes the investment (known as vires);
- The Council's fiduciary duties;
- There is no State Aid (replacement regulations) associated with the investment; and
- There are clear exit arrangements.

294. The Council's legal advisors have provided an advisory report at Appendix D to provide guidance on these matters.

295. Specific advice has been given regarding the Powers to set up WRIF and the legal advisors have concluded that:

*"The Council, in principle, has the powers to create WRIF and the related funds for the broad purposes set out in the Strategic and Economic Cases"*

296. This advice is subject to:

- The Council continuing to check vires as the terms of the fund are refined and as particular 'products' or interventions are developed;
- Compliance with the Council's fiduciary duties – which, in view of the potential size of the funds, should address in some depth the risks of (and mitigations) to manage/avoid council losses;
- Adoption of robust governance and accountability processes;
- Ensuring that revenue funding to recipients (of the WRIF funds) is not financed from Council borrowing;
- Ensuring that the use of PWLB funding for the WRIF does not contravene PWLB lending criteria. In particular that it does not amount to borrowing in advance of need nor buying investment assets for yield

297. In consideration of the recently issued PWLB lending criteria and the final bullet point above, the Council must ensure the structure of the funds (and their activities) remain (for capital spending) within the PWLB's guidance's 'permitted activities' and related conditions. Details are included at Appendix E and a positive statement regarding these points will be required where PWLB debt is used to support investments.

298. The legal advisors also highlight that the legal and financial obligations which apply to the Council would to the extent they were relevant also apply to the funds even where they are externally managed. This would include not only distributing the original funding, but also how repayments/receipts are treated.

Subsidy Control

299. The UK-EU Free Trade Agreement reached on 24 December 2020 and published on 26 December 2020, contains extensive provisions around subsidy control that must be adhered to and are directly enforceable in UK law as a consequence of the EU (Future Relationship) Act 2020 (unlike the World Trade Organisation (WTO) rules). These arrangements effectively replace the EU state aid laws.

300. The position in relation to subsidy control is of particular relevance to the WRIF as the new regime will govern relationships with third parties. The UK-EU Free Trade Agreement has agreed to maintain a system of control in relation to subsidies and sets out a series of principles that must be adhered to when (in the Council's case) the local authority is transacting with borrowers. The principles governing the agreed regime are essentially based on the EU state aid regime. There are also new obligations around publication of information relating to the grant of subsidies and

different remedies for breach. We are expecting Central Government to provide more legislation and guidance in the forthcoming months.

301. It is anticipated that the WRIF agreements will be on commercial terms which will negate the need to consider the issue of subsidies. However, the detailed compliance requirements will be considered in due course to ensure that the new regime is adhered to and that the risks to the Council of unlawful aid under the new regime are minimised.

Regulatory position

302. The legal advisors have indicated that FCA regulation needs to be considered where bodies are lending to individuals who are acting as consumers. The majority of the activities proposed to be funded WRIF are likely therefore be outside of the scope of FSMA and will not require FCA regulation. However, although business to business lending is not caught by the scope of the Financial Services and Markets Act 2000 (FSMA) which details the activities which are subject to regulation by either the Financial Conduct Authority or the Prudential Regulation Authority, there are some instances where the type of business or the activity concerns means regulation is required and it is important to keep the activities under review to ensure that they do not extend to consumer lending. The most obvious area of risk is any lending to small businesses who may be sole traders. In consideration of this, and in particular in relation to the type of activities expected under the Local Communities & Enterprise pillar, the Council may be best seeking the support of external fund management with FCA authorisation for that element of investment.

## CONCLUSION

303. The economic analysis has assessed the potential impact of COVID-19 on the local economy and determined that there is a role and rationale for the WRIF to be established to support the economic recovery of the County.

304. Engagement with the market has indicated an ongoing and unmet demand for the provision of financial support for Warwickshire businesses for different investment types. There is therefore a clear opportunity for the WRIF to provide investment which is tailored to meet demand.

305. In addition, it was identified that the current level of provision where insufficient to meet overall requirements, as such there is also a clear opportunity for the WRIF to supplement current supply.

306. All the key factors that the commercial case must satisfy have been considered and legal advice has confirmed that the Council has sufficient powers to create the WRIF.

307. The Council must however keep the activities of the WRIF under review to check vires, ongoing compliance with its fiduciary duties, and ensure the structure of the funds (and their activities) remain (for capital spending) within the PWLB's guidance's 'permitted activities' and related conditions.

308. The approval of a WRIF Strategy with associated objectives, scope, priorities, type of investment and criteria for assessing investment opportunities will form the basis of the decision-making process for the WRIF and ensure that investment decisions are aligned with strategic priorities but also commercially robust as a viable investment opportunity. It is recommended that this document is regularly reviewed to ensure that it meets the overarching objectives of the Council, whilst still providing a relevant market facing initiative.

309. A robust governance and accountability process, through establishment of an Investment Panel and Member Oversight Group, is proposed for adoption whereby all investment opportunities will be assessed via a consistent decision-making process that will ensure that all the commercial considerations are assessed for the investments progressed by the WRIF.

310. Specific advice will be required on key investment points to ensure that legal requirements such as appropriate security, financial strength of each entity and the impact each of these has on matters such as State Aid or any legacy matters, have been factored in the decision.

311. Assessing a portfolio of investments through the establishment of the WRIF will allow the Council to manage risk and give it the ability to invest in some moderately higher risk activities, where these risks are offset against some lower risk opportunities. A commercial investment case will also be made for all individual investment opportunities that are progressed to business case stage.

312. Establishment and resourcing of robust monitoring and reporting of investments and appropriate exit strategies will also ensure that the Fund remains affordable to the Council throughout the duration of an investment. Affordability will be considered in the finance case, but there is a requirement that there is a constant feedback loop between robust monitoring, investment criteria and affordability to ensure investments meet the objectives of the WRIF.

# 6. Financial Case

313. The Financial Case is used to consider the affordability of the proposed project. In the case of the WRIF, the finance case assesses the affordability of the Fund as the preferred approach and how each investment will be considered with reference to the financial parameters set out in the WRIF Strategy.

314. The focus of the Financial Case is on the affordability of the Business Investment Growth Fund [£90m], Local Communities & Enterprise Fund [£10m] and Property & Infrastructure Fund [£40m] at a total portfolio size of £140m.

## THE PREFERRED APPROACH

315. The Preferred Approach provides the Council with a governance process for addressing a range of key interventions that support a variety of different needs based on their key characteristics. It allows the Council to choose the best possible approach to support, given the known financial, commercial, and wider economic conditions prevalent at the time.

316. As set out in the WRIF Strategy, it can be location specific, focusing on investment within the county, aimed at key sectors and business types that will drive growth and be responsive to market forces and local level needs. For instance, it recognises that an intervention in one business type may require a substantially different investment to a similar opportunity in a different sector.

317. This is an important control for the Council as it recognises that no "one size" fits all approach would be appropriate. This flexibility allows the Council greater control when addressing the market, growth, and the specific needs of the area.

318. This flexible approach also enables the Council a much greater control over defining the risks it is willing to take and the potential commensurate rewards it is likely to receive in return, especially when investing in a wide range of business and growth opportunities.

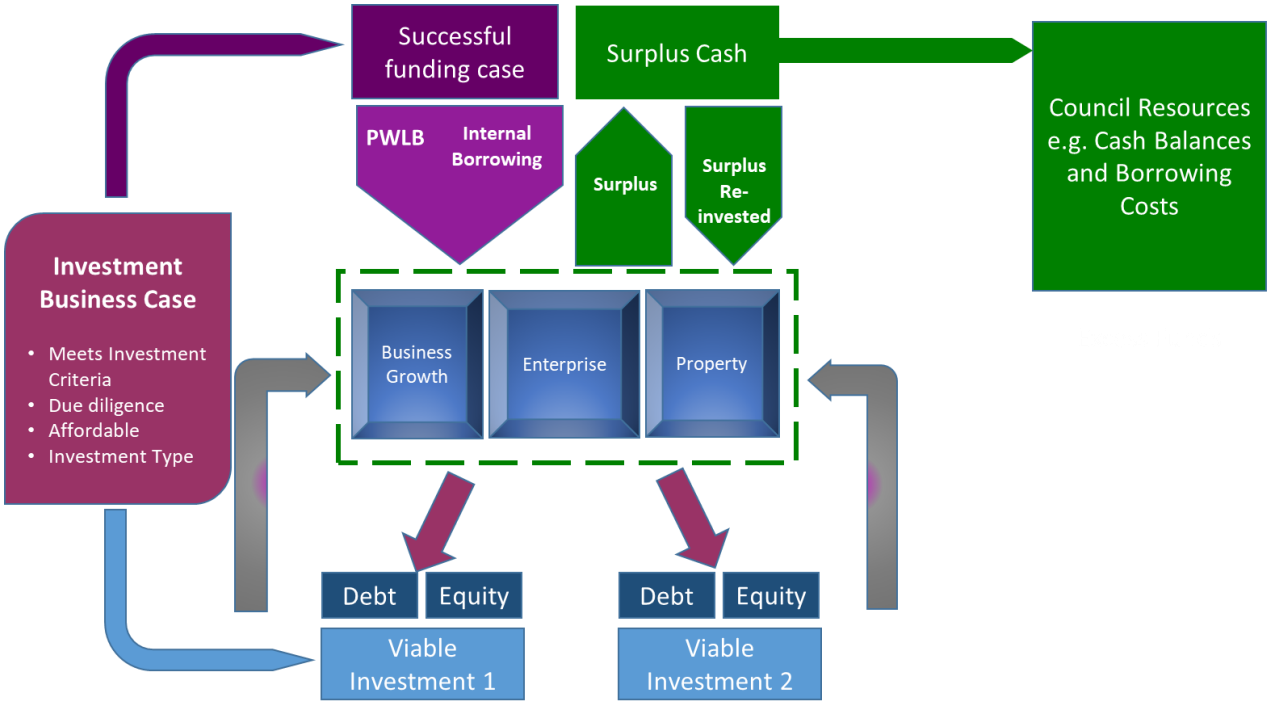
319. The approach has been designed in such a way that should an investment opportunity result in too high a risk profile, or the potential returns are not commensurate with the risks taken, or do not fit in with the Council's appetite for risk at the time of delivery, then another delivery route can be sought – or indeed the Council can delay or decline any investment until market conditions change.

320. This as an approach enables a range of opportunities to be brought forward and to be considered at the earliest possible stage in terms of viability. The structure defrays risk across a range of investments, the Council is able to manage risk on a portfolio level, rather than on an investment-by-investment basis.

321. By assessing the proposal at a portfolio level as well as on an individual case by case basis suitable plans can be put in place to protect the Council and support its financial sustainability. It

enables the Council to take on more risk with these risks being offset elsewhere in the portfolio should there be a robust service imperative to invest.

322. The diagram below sets out, at a high level, the process for assessing investment opportunities allowing a range of different delivery approaches that best suits the Council's risk, return and control objectives.




323. Once categorised as a viable investment, the Scheme Investment Business Case will be made to ensure that each intervention addresses the objectives of the Council's stated WRIF Strategy.

324. The Approach is also designed to recognise that as Business Cases are put forward the approach to investment can be adjusted to best meet changing needs and varied investment requirements. It is an iterative process where approaches can adapt over time based on improving assumptions, changes in market conditions and requirements and changes in the financial standing of the Council.

325. Using this approach, the Council will extract returns from a number of sources, for example:

- Capital receipts;
- Financing returns e.g. return on loans issues to third parties;
- Development profit;
- Revenue and profit from assets held for the purposes set out in the WRIF objectives e.g. housing, commercial/retail units;
- Returns from sustainable energy investments;
- Other payments for financial support e.g. Loan guarantees, income strips; and
- Return on equity (company).

326. Each of the above relies on a different investment approach by the Council, and each has a different risk profile and provides a combination of short, medium, and long term returns that go beyond the current approach.

## INVESTMENT FUND SIZE

327. The Council has identified a maximum investment pot of c.£140m to support the objectives of the WRIF over a 5-year time horizon. This is the maximum anticipated size of the Fund for this period and represents the maximum exposure of the Council in cash terms.

328. The split of the total quantum of WRIF Funds will be allocated against individual Pillar accordingly:

| Fund | Size<br>£m | Rationale for size |
|---|---|---|
| Business Investment Growth Pillar | 90 | • Market demand<br>• Risk profile<br>• Size of interventions |
| Local Communities & Enterprise Pillar | 10 | • Market demand<br>• Risk profile<br>• Size of interventions |
| Property & Infrastructure Pillar | 40 | • Market demand for leveraged fund (£40m)<br>• Smaller number of strategic interventions;<br>• Externally managed to enable key sites |

329. However, the Fund, as a whole is designed to be flexible and responsive to market needs. If after an assessment of risk and affordability it is felt that these allocations should change to meet demand, then this will be addressed by a recommendation from the Investment Panel to Cabinet as required.

330. Given the nature of the Fund any returns over and above those repaying the original cash balances will be used to support the ongoing priorities set out in the WRIF investment strategy. These could form part of the WRIF or be delivered through other Council programmes.

331. This overall size of the WRIF investment portfolio and the allocation to each separate Fund are considered appropriate for the following reasons:

- Market engagement has indicated there is a strong level of demand for support across these three areas. As such, when considered with the risks associated with investment and the availability of resource and the Council's wider fiduciary duties, a bigger fund would have more impact;

- The Fund needs to have sufficient critical mass to enable to the Fund to support a wide array of schemes. The size of the Fund will provide market credibility amongst the investor, business and developer community;
- Any smaller is unlikely to attract the inward investment desired or be sufficient to support, accelerate and unlock regeneration and economic growth;
- The economics and resources of running a smaller Investment Fund may be out of proportion with the gains;
- The WPDC Business Plan has been used to determine the funding allocation for the Property & Infrastructure Fund;
- The maximum possible exposure of the Council of the WRIF will be limited to a maximum of £140m in cash, and therefore, revenue exposure will be tied to the opportunity costs of using this cash elsewhere or the cost of borrowing this money at the time of investment and;
- Where £140m is the maximum exposure, repayment profiles will mean that peak debt is significantly below this level.

332. Whilst the Fund may invest in the purchase of physical assets, when this purchase meets the strict criteria of the funds, there is no intention to transfer physical assets currently held by the Council for investment purposes into the Fund.

## FUNDING SOURCES

333. The WRIF approach enables the Council to directly invest in a wide range of interventions; introducing a diverse range of returns both in terms of size, timing, and nature of receipts.

334. The approach to investment will be dictated by the individual projects and may include debt and equity investment (see glossary in Appendix for more information). However, the investment will need to be monitored at a portfolio level to ensure that affordability, and risk, is managed through the diversification of investment approaches.

335. Based on the diverse potential for investments, there are a number of considerations that will influence the source of funding and the nature of the investment. For example, all investments made by the WRIF will utilise the Council's resources, with each investment judged on its own merits. However, in practice this means that the Council will use internal cash balances; external borrowing taken under its Prudential Powers; or use its covenant (financial strength) to support initiatives.

336. Where investments are not classified as capital expenditure or activities that would be classed as capital expenditure where they to be undertaken by a Local Authority, (as set out in the Code of Practice on Local Authority Accounting), then the Council is unable to borrow to support this investment, and it must be funded by internal resources.

337. When using external borrowing to support investments, it must be minded of recent changes to the Lending Arrangements for PWLB Loans, provided by HM Treasury[1]

**New Guidance – Lending Arrangements for the Public Works Loan Board**

338. New lending arrangements put in place in December 2020 mean that Local Authorities are required to warrant HM Treasury that:

- it has the power to enter into, perform and deliver, and has taken all necessary action to authorise its entry into, performance and delivery of:
    - the PWLB Loan Conditional Confirmation Letter and relevant Operational Circular, which set out the terms of the PWLB loan for which the borrower is applying; and
    - the intended use of that loan once granted (as set out by the borrower in its application for the PWLB loan); and
- no limit on its powers will be exceeded as a result of the borrowing contemplated by the terms of the PWLB.

339. Of particular relevance to the Council of the new lending arrangements is the requirement that the Section 151 officer must certify that the relevant council is not borrowing in advance of need and does not intend to buy investment assets primarily for yield/income.

340. When local authorities borrow, they must have regard to the Prudential Framework as set out by Chartered Institute of Public Finance and Accountancy (CIPFA), and by the Ministry of Housing, Communities and Local Government (MHCLG).

341. Recently legislation has changed to broadly stop Council taking on debt to generate a yield off these amounts. This is in response to a number of local authorities who have looked to support their medium to long term financial sustainability by borrowing to invest in income generative assets.

342. Changes to legislation mean that if the sole purpose of the investment is to generate a yield then this is contrary to the Prudential Code. Guidance confirms that the PWLB is intended to offer long-term, affordable loans to support local authority investment in service delivery, housing, economic regeneration, [treasury management], and occasionally preventative action, not to enable local authorities to purchase income generating assets with no wider public purpose.

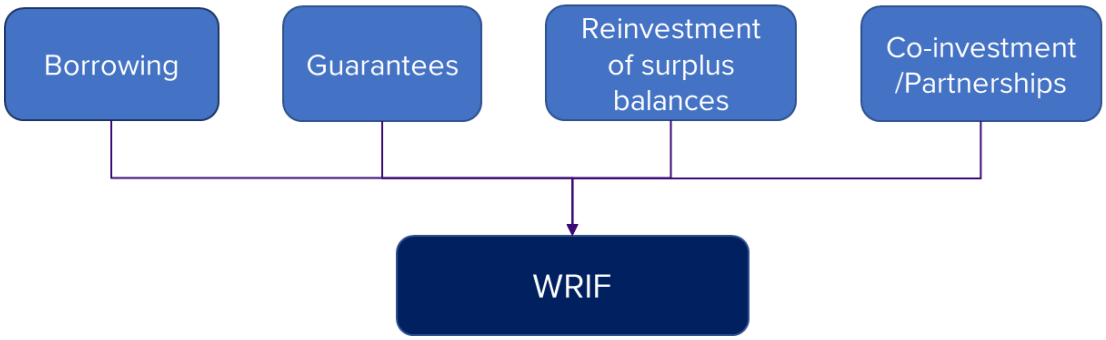
343. It will be necessary for the Council to ensure the structure of the fund (and their activities) remain (for capital spending) within the PWLB's guidance's 'permitted activities' and related conditions. Details of the Councils approach to PWLB's revised lending objectives are included in the Council's Annual Investment Strategy and included at Appendix E.

344. Should the Council though the use of the WRIF contravene PWLB lending criteria, then the ultimate sanction would be that it would be unable to borrow from the PWLB for a three-year

[1] Circular 162 – 26 November 2020

period. As such, each opportunity will be assessed to confirm a permitted use when the Council uses its Prudential powers.

345. The potential sources of finance are as follows:




346. The most appropriate source of finance for each individual investment will be determined and recorded at the time of the investment decision making when the individual opportunity is being reviewed by the Investment Panel via consideration of a Business Case. Where external borrowing is used the business case will need to state which of the permitted activities the investment falls under and a positive confirmation with appropriate evidence that is it complies with new PWLB lending arrangements will be required

## AFFORDABILITY

347. Affordability will be a key constraint, and the Council will need to understand the programme of investment at a portfolio level as well as the return profile of each intervention. For instance, significant levels of upfront investment will be required with returns to the Funds varying against a number of different factors.

348. When considering the operation of the fund, the full impact of any investment must be clear with the following aspects for consideration:

| | |
|---|---|
| Source of investment / funding | • Internal cash balances<br>• External borrowing (PWLB, third party banks, pension funds)<br>• Private sector / public sector partners (Property Fund)<br>• Accessing Grants |
| Revenue Costs (borrowing) | • Finance (interest) costs<br>• Minimum Revenue Provision<br>• Indexation |
| Opportunity / Other Costs | • Investing internal resources<br>• Providing corporate guarantees<br>• Impact on the MTFP<br>• Running costs |

349. The fund will operate on a commercial basis and should not therefore be investing into financially unviable schemes or providing grants. However, it may look to provide affordable loans that use the flexibilities afforded to some SMEs by recently updated State Aid Guidance.

350. The Council will set out its expected returns based on Market normative and State Aid compliant lending rates, peak debt levels, payback period, hurdle and default rates to provide a consistent comparison for investment purposes. As the programme progresses, these rates can be flexed to better reflect market dynamics, the relative investment risk of each proposal and the Council's appetite for risk based on affordability and prevailing economic conditions.

351. Affordability is built into the governance of the WRIF by assessing the affordability of each investment and the impact of these on the overall portfolio.

## RUNNING & OPERATING COSTS

352. Running and operating costs of the Fund will need to be accounted for and monitored in relation to the performance of the Fund.

353. It is proposed that the Fund will cover all internal costs for resources and external costs for management as well as any transaction fees and charges. The aim is to make the Fund run as efficiently as possible, seeking to pass costs on to borrowers wherever appropriate. This will be generally achieved through a market normal transaction charge for any investment.

354. The total running/operating costs for a Fund are expected to account for in the region of 2% of the total Capital invested based on market feedback this being £140m invested over 5 years; this gives a total estimated running cost of the WRIF of £2.8m.

355. The net return on investment (including for all costs, fees and charges in making the investment and its ongoing monitoring) will be clearly set out as part of the investment decision making and monitoring of the investment performance by the Investment Panel.

356. There may be an increase in costs in the early years of the Fund as the Council looks to market its objectives, to attract opportunities and as it prepares standard documentation e.g., Loan Agreements. This increase is to be offset by savings later in the programme and as such the 2% overall cost is appropriate.

357. For the purposes of modelling running cost it must also be recognised that costs may be incurred after the final investment, with monitoring and reporting requirements until the investments are repaid.

358. To ensure all costs are accounted for the financial model allocates 80% of the total running costs to Years 1 -5, with the remaining 20% of costs allocated to Years 5 – 12.

359. The Year 1 Budget for running the Fund has been calculated based on eighty percent of the 2% of the total capital invested. This will be funded from [Commercial Fund] and approval given in the normal way for that fund.

## FINANCIAL MODELLING

360. Financial modelling and financial scenario testing has been undertaken to understand the financial impact and affordability of the WRIF based on a "typical" level of investment across the three pillars. The financial model assumes that an appropriate level of due diligence is undertaken by the Council to support any investment decision and that robust monitoring is in place to identify any issues as they occur.

361. The financial model seeks to provide the Council with a view of a typical portfolio of investments, setting out a 5-year profile of investment.

362. The financial model focuses on the affordability of the WRIF as a total Fund and then looks at the proposals for the Business Investment Growth pillar [£90m], Local Communities & Enterprise pillar [£10m] and Property & Infrastructure pillar [£40m].

Key Assumptions

363. The following assumptions have been made across the three Funds:

| Key Assumption | Business Investment Growth Pillar | Local Communities & Enterprise Pillar | Property & Infrastructure PIllar |
|---|---|---|---|
| **Size/ £M** | 90 | 10 | 40 |
| **Average Size of Investment**[2] | £5,000,000 | £100,000 | £10,000,000 |
| **Average investment Return** | 5.0% | 8.0% | 6.5% |
| **Arrangement Fee** | 0.5% of capital employed | 0.5% of capital employed | 2% Determined by Fund |
| **Default rate** | 3.0% | 30.0% | 0% |
| **Recovery on Default** | 80% | 25% | 100% |
| **Total Running Costs** | 2.0% of capital employed | 2.0% of capital employed | 0% (contained in Fund) |
| **Council cost of Funds** | 2.5% | 2.5% | 2.5% |

Note: The Property and Infrastructure pillar has drawn figures from market testing and will need to be tested further during any procurement of an external advisor. Running costs and arrangement fees are included within the Fund with returns to the Council net of these costs.

364. In an attempt to reflect "typical" activity across the funds a number of loans have been modelled, with a varying amount invested over a 5-year time horizon, with varying repayment periods,

[2] For modelling purposes

reflecting the broad objectives of the funds. The constant is the requirement not to breach the Peak Fund Size allocated to each Fund.

**Financial Modelling Results**

365. The table below sets out the potential return of the WRIF:

| Item | Total £M |
|---|---|
| Gross Funding | 140 |
| Peak Funding | 76 |
| | |
| PWLB Interest payable | (9.5) |
| Potential Loss through default | (2.7) |
| Running Cost | (2.8) |
| Arrangement Fee | 0.5 |
| Interest Repayment | 21.0 |
| **Net Revenue** | **6.5** |
| **Net Revenue (NPV)** | **4.9** |

366. The financial modelling indicates the total financial return from the WRIF over its investment cycle lies in the region of £6.5m, (£4.9m NPV). This is a positive return to the Council and demonstrates, given the baseline assumptions used that the WRIF is viable and affordable.

367. Further work has been completed to assess the viability of the three-pillars within the WRIF. The Table below sets out the performance of each pillar given the baseline assumptions.

**Performance of the WRIF across the three-pillars**

| | Total WRIF | Business Growth | Communities & Enterprise | Property & Infrastructure |
|---|---|---|---|---|
| Gross Funding | £140m | £90m | £10.0m | £40m |
| Peak Funding | £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 | | | |
| 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** |

368. 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 can be used as a to manage risk. The modelling demonstrates that whilst the Business Growth and Investment and Property and Infrastructure pillars produce a strong positive contribution to the financial viability of the WRIF, given the nature of the Local Communities and Enterprise Fund, a number of risks will need to be managed, to ensure any support and intervention given is carefully managed to ensure the overall viability of the WRIF.

**Business Investment Growth Pillar**

369. This Pillar supports larger investments in specific growth businesses. It is likely that the majority of the investments will be capital in nature with a focus on Business Loans. As such, the WRIF would look to secure suitable security over the assets of the business or new venture. Where security is diluted by other debt or erosion of financial strength then an interest rate/return will reflect this increased level of risk.

370. It is anticipated that the financial strength of the businesses will be above a moderate level, with a comparable Moody rating of at least Baa[3], although each investment will be judged based on its own merits.

371. Default rates on this Pillar are likely to be relatively low, with Standard and Poor's suggesting that a default rate on this class of investment is around c.1.5%. To ensure a prudent loss provision, commensurate with the Council's requirements to safeguard Public money, this has been increased to 3% for the purposes of the model.

372. In addition, it is expected that strong security will be available to support these investments and if a default position is reached the WRIF could expect to recover as a minimum 80% of the principle amount invested.

373. Set out in the table above, over the 18 specified investments, the BIGP could expect to see a return of £4.9m with a potential loss of £0.5m, giving a net return of £4.4m.

**Local Communities and Enterprise Pillar**

374. The Local Communities and Enterprise Pillar will address more recovery than growth, although it will look to support start up and SME/Micro organisations. As such the risk profile for these investments will be significantly higher than the BGIF.

375. The expected default rate, based on current market analysis, is estimated to be as high at 30%. The level of security that the WRIF will be able to take against these investments is expected to be low with recovery rates at c.25% of the investment value.

[3] www.moodys.com/sites/products/AboutMoodysRatingsAttachments/MoodysRatingSymbolsandDefinitions.pdf

376. Work is continuing to be undertaken by the Council and the wider market to assess how this default rate could be reduced or the level of recovery increased.

377. As a result of the high default rate on and the low Recover Value (25%) the current financial model would suggest that a net loss the on Local Communities & Enterprise pillar could be £1.6m, (based on a gross return of £0.7m and losses of £2.3m). This loss demonstrates the higher risks associated with investment in this pillar and justifies the relatively high return rate of these investments.

378. The Council could manage the impact of these losses in a number of ways, including:

- Set up a specific annual reserve against these predicted losses;
- Focus on specific investments that do not have such a high rate of default;
- Consider the range of ways to secure the investment in the event of default
- Increase the rates on return on particularly high risk interventions;
- If losses do start to occur amend or adjust the investment tolerance or activity to reduce these amounts; and
- Cross subsidise any losses from unallocated surplus achieved on the other two pillars.

379. In addition, the table shows that, although at a gross level the pillar is investing up to the size of the fund, repayments mean that actual peak debt is less – allowing the Council to better manage its core cash requirements or allowing the ability to invest in additional opportunities.

**The Property & Infrastructure Pillar**

380. The Property and Infrastructure Pillar will likely be externally managed that will provide support for strategically important sites across the County. As such, it is likely that this pillar will focus on larger strategic interventions.

381. The external Fund Manager will be responsible for sourcing the opportunities, ensuring viability, recommending to the Council, through the approved governance process, where investment should be made and monitoring and reporting on the ongoing performance of these investments.

382. Returns to the Council will be net of all external Fund Manager fees and any other running costs of the fund. Market testing has been conducted on this Fund and as a result of the additional due diligence and the strategic nature of the Fund, losses are minimal and contained within the fees payable to the Fund Manager.

383. Based on this analysis, the Council could expect a net return of c.£3.1m from this pillar.

**Sensitivity Analysis**

384. The base case gives the following net return to the WRIF:

| Total WRIF | Business Investment Growth [£90m] | Local Communities & Enterprise [£10m] | Property & Infrastructure [£40m] |
|---|---|---|---|

| | | | | |
|---|---|---|---|---|
| **Net Revenue** | **£6.5m** | **£4.4m** | **-£1.5m** | **£3.6m** |
| **Net Revenue (NPV)** | **£4.9m** | **£3.5m** | **-£1.3m** | **£2.7m** |

385. To assess the potential movement in this baseline figures sensitivity and scenario analysis was conducted by varying the key drivers within defined ranges.

386. Monte Carlo Simulation (MCS) is a method which employs a distribution/range-based approach to input assumption as opposed to the singular assumption used in base case modelling. This figures in the base case are predicated on calculated projections and backed by researched market evidence, however, it is not guaranteed to hold true. Errors in assumption projection, changing market conditions and many other factors could deviate the true values from those used in the model. To account for this uncertainty and inherent risk, the MCS method assumes a weighted range as opposed to an individual figure.

387. In one MCS simulation a value is drawn from each assumption distribution with the chances of each value in line with the % chance it was assigned. These randomly selected values are then run in the financial appraisal and the results are logged. This process is repeated a 1,000 times which yields 1,000 unique simulation results. These results are then analysed to determine the % chance of certain events happening.

388. The table below sets out how, using the MCS analysis, the predicted range for the WRIF returns could vary when the WRIF is considered as a whole (less risk) and when it is split across each pillar:

| | **Total WRIF** | **Business Investment Growth** | **Local Communities & Enterprise** | **Property & Infrastructure** |
|---|---|---|---|---|
| **Downside Risk (NPV)** | £3.2m | £2.3m | -£2.5m | £2.7m |
| **Upside Potential (NPV)** | £6.3m | £3.9m | -£0.1m | £2.7m |

389. In addition, the MCS was used to assess % chance of a positive return against each pillar, this information is set out in the table below:

| | **Total WRIF** | **Business Investment Growth** | **Local Communities & Enterprise** | **Property & Infrastructure** |
|---|---|---|---|---|
| **% Chance of Positive NPV** | **99%** | 99% | 0% | 99% |

390. Based on the results there is a “near certain” probability that the WRIF will produce a net return.

391. However, as previously identified, significant risks have been noted in the provision of the Local Community & Enterprise pillar. In order to assess the viability of this pillar a sensitivity testing has been completed to assess by how much some of the key drivers would have to change to create a net breakeven position. The table below sets out these key metrics:

| Key driver | Base Case % | Adjusted value to breakeven % |
|---|---|---|
| Investment Return | 8.0 | 18.0 |
| Default Rate | 30.0 | 9.1 |
| Recovery on default | 25.0 | 77.0 |

392. There is significant risk that despite the Council's desire to ensure that all costs are covered within each pillar, there may be a requirement to operate a cross subsidy model to support the viability of the Local Communities and Enterprise Pillar.

393. Further analysis has been done to assess the impact on the WRIF of varying the allocation between the Business Investment Growth and the Local Communities and Enterprise Pillar.

**£80M BGIF & £20M LC&EF**

| | Base Case | Total WRIF | Business Investment Growth | Local Communities & Enterprise | Property & Infrastructure |
|---|---|---|---|---|---|
| **Net Revenue** | £6.5m | 4.3m | 3.8m | (3.1m) | 3.6m |
| **Net Revenue (NPV)** | £4.9m | 3.3m | 3.1m | (2.5m) | 2.7m |

394. If the Council looked to increase the size of the LC&EP from £10m to £20m, (reducing the BIGP to £80m to maintain within the £100m total envelope), the potential return on the WRIF decreases.

## ACCOUNTING CONSIDERATIONS

395. The pillars are designed to be flexible and responsive to market requirements and, as such, there are a range of financial interventions that the WRIF could provide to support its objectives.

396. As each request is assessed it will be judged on its own merits, with the accounting implications of each considered within the round. However, below are a number of considerations that the Council must assess when making investment decisions:

*Source of Funding*

The Capital Accounting Regime is prescriptive about expenditure that is allowed for capital purposes. Indeed, when making an investment the Council must consider the activities

undertaken with or by its investment. If the activity is Capital in nature and, where it to be done by the Council it would be classed as capital, then the Council can use its powers under the Prudential Code to raise its Capital Financing Requirement by this amount and borrow from a suitable source. However, if the activities are materially revenue in nature then the Council cannot borrow for these purposes and resources must be made available from other sources e.g. internal cash balances.

*Minimum Revenue Provision*

A prudent provision (the Minimum Revenue Provision) is the calculated annual charge to the revenue account of provision to repay debt incurred in respect of capital expenditure financed by borrowing or other long term credit arrangements. MRP should normally commence in the financial year following the one in which the expenditure was incurred. The Council's current methodology for the provision for MRP is to charge a flat rate of 4% against its outstanding CFR and must be considered when assessing the affordability of the WRIF as a whole. There is a recognition that the 4% charge, when considered against the repayment of short-term capital loans, may cause a mismatch, and therefore it is important to ensure that capital repayments are used to reduce the CFR or the need for future borrowing.

*Financial Instruments*

Where an investment is made under its powers to invest, then the Council will be required, under IFRS 9 to disclose the fair value of any investments on an annual basis. As such, when making any investments, the Council must consider the valuation methodology and apply this consistently. In addition, where an investment falls outside of the Capital Finance Regime, the Council must recognise, through a charge to the I&E Account, any gain or loss in fair value.

*Requirements to prepare Group Accounts*

Where the Council purchase shares, equity in an entity or provides loans that convert to equity at a prescribed event it must consider the need to show the performance of this entity in its own financial statements. The general rules around whether it is necessary to prepare Group Accounts relate to level of ownership or the ability of the Council to exert significant positive control.

*Financial Returns*

The Council must consider the correct treatment of any financial returns from any investments. This is especially important as any surpluses are now required to be used to support similar activities either within or outside of the WRIF. Returns will generally take the form of principal repayments, financing payments e.g. interest payments, equity returns, lease premiums or

overage payments. The Council must consider the powers used to make each investment when assessing the nature of the returns i.e. capital or revenue.

*Recognition of Losses*

The financial model for the WRIF recognises, through a default rate and a recovery on default rate the risk of loss on a proportion of the loans. As part of the IFRS 9 disclosure the Council will have to recognise losses within its accounts. However, it may be prudent for the Council consider a set-aside for expected losses to minimise the in year impact of any defaults. The table below sets out (using the information from the financial model) the annual potential loss calculated from the default rates.

| 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** |

## FINANCIAL RISKS

397. The table below sets out a number of financial risks that the council must consider, together with some suggested management and mitigating actions.

398. The table is not exhaustive but reflects a collection of the key risks.

| Risk | Potential Management & Mitigations |
|---|---|
| **Governance**<br>Insufficient resource and expertise is committed to the business case process that supports any investment decision and as such investment decisions are poor and increase the likelihood of loss. | The Council must identify sufficiently qualified resource to ensure business cases are robust and any investment decisions properly understood. |

| Risk | Potential Management & Mitigations |
|---|---|
| The Council is slow in making corrective actions where investments are performing below expectations<br><br>Recent coverage of Local Authorities getting into difficultly when making loans to third party entities has highlighted the need for a robust understanding 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. | Reporting should be sufficiently regular and detailed to ensure that issues are identified and addressed in a timely manner.<br><br>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 optimum 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**<br><br>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**<br><br>Where an element of a funds 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 |
| **Default levels exceed Fund estimates**<br><br>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 Council may wish to consider setting aside an annual reserve to cover expected losses. 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**<br><br>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**<br><br>There is currently heightened scrutiny in the Sector, where authorities are looking to support their | |

| Risk | Potential Management & Mitigations |
|---|---|
| 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.<br><br>The Council must have the flexibility to alter investments if those changes would adversely impact the ability to borrow/fund statutory services? |

## CONCLUSION

399. The Financial Case concludes that proposals for the WRIF, as a whole, are affordable as the Fund has been designed as a flexible tool to enable investment in a wide range of different opportunities to manage and diversify risk and ensure that all costs are contained within the Fund. However, the estimated losses with the LC&EP needs to be considered in conjunction with the potential costs savings generated by supporting small business and the associated jobs.

400. The WRIF Strategy will ensure that the investment is aligned with strategic priorities and meets economic, social value and financial criteria. These criteria will also form the basis of all contractual obligations for external fund management.

401. The establishment of the Investment Panel will ensure that suitable and sufficient due diligence is undertaken to SIFT and consider investment opportunities before any decision making or investment takes place. Decisions will be taken by Cabinet and the establishment of robust monitoring and appropriate exit strategies will also ensure that the Fund remains affordable to the Council throughout the duration of an investment.

402. Risks will need to be managed at a Portfolio level and will form part of the performance and monitoring measures put in place by the Investment Panel.

# 7. Management Case

403. The purpose of the Management Case is to assess whether a proposal is deliverable by setting out the governance structure, project planning, risk management and communication & engagement arrangements required to ensure successful delivery of a project.

404. This section sets out the resources, governance arrangement and project management processes that will be put in place to ensure successful implementation and ongoing operation of the WRIF.

## FUND MANAGEMENT

405. The preferred approach determined in the Economic Case is to set up a mixed economy model where the Council internally manage some aspects of the fund, with the support of external advisors, and outsource other parts of the fund to be managed by an external Fund Manager(s).

406. The first stage of market engagement has indicated there is clear demand for finance from Warwickshire businesses and that there are Fund Managers already operating in the region whose skills and experience are aligned with different elements of the Fund. For example, Coventry & Warwickshire Reinvestment Trust and the Black Country Investment Fund are specialist finance providers who provide business loans to small businesses and individuals and already operate on behalf of the Council and the MEIF. Maven CP who provides debt finance on behalf of the MEIF and BCRS who provide small business loans behalf on the MEIF but also provide a property fund and work closely with local authorities who have established a PropCo, similar to the proposals for WPDC.

407. In consideration of this feedback and in understanding the regulatory framework, the current resource availability, skills, and capacity of the Council as well as their appetite for involvement and consideration of risk in terms of the management of the Fund, the following management arrangements are proposed:

### Internal Management

408. The Council will establish an in-house team for the WRIF that will operate alongside the existing Business & Economy Team and the Business Support Programme that is already established by the Council.

409. The in-house team will report into the Investment Panel that will be established for decision making and management and monitoring of the Fund. The exact details

410. The main roles that could be established in the in-house team are:

- **Investment Manager** that will be responsible for:
    - Identifying investment opportunities that are in line with the WRIF Strategy

- Developing the sift documents and business cases for these investment opportunities
- Being a member of the Investment Panel and presenting sift documents and business cases for Investment Panel consideration and the Cabinet's subsequent approval.
- 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)
- Reporting on performance of WRIF portfolio overall

- This role will need to be resourced appropriately for the WRIF to operate effectively and as the Fund scales up in size there may need to be more than one of this role in the team.
- **Business Advisor(s)** (numbers to be based on the activity of the Fund) that will be responsible for:
  - signposting potential applicants to the fund(s),
  - support investor readiness via incubator/accelerator programmes
  - spending time with investees to fully understand the business proposition prior to business case stage
  - supporting the Investment Manager in the preparation of Sift Documents and Business Cases

411. The in-house team could be supported by a team of external advisors that will need to appropriately procured. The Council has access to a number of panels and frameworks via the DPS (Dynamic Procurement System) that may be suitable to source these resources from as well as the option to secure additional resources via direct recruitment.

412. We set out below the types of skills we anticipate that may be required to support the internal team:

| Area of expertise | Role/requirement | Route to secure resources |
|---|---|---|
| Legal advisers | • Advice on the structuring of an investment<br>• Advice on State Aid implications of the investment<br>• Advice on Powers required to make investments and to enter into commercial partnerships. | Internal advice with support from external providers appointed pursuant to Standing Orders where needed. |
| Financial advisers | • Financial due diligence of companies involved with investments<br>• Financial implications of State Aid rules (e.g. minimum interest rate on loan to avoid state | Internal Finance team with some supplementary ad hoc external support |

| Area of expertise | Role/requirement | Route to secure resources |
|---|---|---|
| | aid, or quantification of state aid within the transaction, comparison again state aid thresholds)<br>• Financial viability assessments<br>• Financial accounting to understand the impact of any investment on the Council's statutory financial statements. | |
| Tax advice | Advice on Tax, included but not limited to:<br>• Stamp Duty Land Tax<br>• Value Added Tax<br>• Corporation Tax<br>• Capital Allowances. | External advisor as required |
| Property Valuation | Advice on and validation of property/asset valuations<br>Advice on housing development/management | Valuer (internal) or external advisor |
| Technical advisors/ Industry specialists | The requirement here will vary depending on the nature of the investment. We anticipate that you will likely need:<br>• Industry specialists<br>• Technical advisors with experience working with priority business types<br>• Incubator/Accelerator programme support | External Panel of Advisors to be available via call off |
| Peer review, Business Leaders, Private Sector representative | • Challenge function (akin to a NED) | Via existing Council networks and or OSC and Audit Committee as appropriate |

External Fund Management

413. A procurement exercise will be undertaken to secure Fund Management services (and any other external advice required) to support delivery of elements of the WRIF where it is considered that the type of investment, volume of opportunities, due diligence, risk, skills and resource require external involvement.

414. The broad services expected from external Fund Management are:

- Sourcing investment opportunities
- Support to businesses in developing viable business/investment propositions
- Evaluating applications
- Due Diligence & Business Case preparation
- Investment appraisal
- Investment decision making & allocating funds
- Valuation services (tbc)
- Fund Management
- Performance Monitoring

415. It is anticipated that there will be a requirement for more than one external Fund Manager across the WRIF in order to support operation of both the Local Communities & Enterprise Pillar and the Property & Infrastructure Pillar

416. In consideration of the feedback from the market engagement there is the possibility of separate Fund Managers also being required for operation of the Local Communities & Enterprise Pillar where there is a broader range of recipients, outcomes, and types of investment. The different management could be with a focus on:

- Start-ups;
- Micro Businesses; and
- Social Enterprise.

417. In addition, it may be appropriate for elements of the Property and Infrastructure Fund to be managed externally.

418. Although it is anticipated that this will not be a Day 1 activity, the benefits of this approach include securing leveraged finance, having a dedicated pillar to encourage developers to engage with experts and setting a ring-fenced block of finance to accelerate and increase investment in private sector led development and site-specific infrastructure across Warwickshire which maximises the impact of the WRIFS's intervention to deliver economic growth

419. Prior to the procurement exercise to secure the services of an external Fund Manager, a soft market testing exercise will be undertaken to refine the details of the Fund, shape the procurement strategy, determine the role of the Fund Manager and the scope and services that can be procured externally. This exercise will also test the proposed investment criteria and performance and the most appropriate method for incentivising Fund Managers to deliver the priorities of the WRIF.

420. The soft market testing will also assist in determining the number of different lots to be procured to reflect the number of external Fund Managers required to support different elements of the Fund in consideration of experience and expertise.

## GOVERNANCE

421. It is proposed that an Investment Panel is established to monitor the performance of the WRIF at a portfolio level and also to guide and make recommendations on any investment decisions for any of the three proposed Funds that are to be managed in house.

422. Each year Full Council and Cabinet will approve the relevant annual budgeted amount for each WRIF fund and set out the WRIF's authority to operate the fund(s) via the Investment Panel for the next year.

423. All individual investments will be referred to Cabinet to approve within a total investment portfolio size of £140M and in line with the criteria set by the WRIF Strategy. The Panel will report to Cabinet to whom it will also refer investment decisions that fall outside of the parameters of the WRIF Strategy.

424. Where an element of the Fund is internally managed, the role of the Investment Panel is to:

- Review and update the WRIF 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.
- Oversee the governance and decision-making process for investments to ensure investment opportunities are thoroughly evaluated and appropriate due diligence undertaken
- Consider Business Case proposals - Review, challenge and make 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
- Provide updates to Cabinet (and Member Oversight Group when required) on the performance of the Portfolio

425. Where an element of the Fund is externally managed the role of the Investment Panel is to:

- Review and update the WRIF Strategy to reflect the current needs of local businesses, the local economy and investment market.
- Provide contract management of External Fund Managers/Management
- Monitor the progress and performance of the overall portfolio

- Provide updates to Cabinet (and Member Oversight Group when required) on the performance of the Portfolio

Where an element of a fund is externally managed, the role of the Council will be to robust challenge of performance should the council delegate decision making to the fund manager, and the only control will be via the procurement exercise to appoint and by specifying the criteria, limits and requirements as based on the WRIF Strategy.

426. The membership of the Investment Panel is proposed as:

- Strategic Director for Resources (optional)
- Business & Economy & Growth/Regeneration representation - Assistant Director: Communities / Strategy & Commissioning Manager: Economy & Skills
- Governance & Policy Assistant Director: Governance & Policy / Strategy & Commissioning Manager: Legal and Democratic
- Property/Housing representation
- Finance Team Assistant Director: Finance (Deputy S151) / Strategy & Commissioning Manager: Strategic Finance] / Strategy & Commissioning Manager: Treasury, Pension, Audit & Risk

427. The Terms of Reference for the Investment Panel are set out at Appendix B.

428. It is recommended that the membership of the Investment Panel is made up of officers from within the Council covering Finance, Legal, Business and Economy, Property and Regeneration, and Governance and Policy. These officers will be advisors to Cabinet as the key decision maker on whether to invest or not. However, it is anticipated that officers may need to supplement their experience with specialist expertise to inform their recommendations.

429. A Member Oversight Group will be established for the scrutiny of investment decisions where quarterly monitoring reports will be referred and any individual investments or investment decisions can be referred for scrutiny. This will be a cross party, standing working group chaired by the Deputy Leader.

430. The Member Oversight Group will be tasked with monitoring:

- The achievement of WRIF objectives
- The financial performance of the fund
- The governance, decision making and management arrangements of the fund

431. The Member Oversight Group will receive a report from the Investment Panel on a quarterly basis that will capture a summary of investment decisions made in that quarter and reporting on delivery and performance of the fund.

432. The WRIF will utilise the relevant Overview and Scrutiny Committee and also the Audit and Risk Committee as required.

## PROJECT PLAN

433. A high-level Project Plan will be prepared to cover all significant activities, events and milestones involved in the setting up and running of the WRIF.

434. The Project Plan will be regularly updated and included in regular Progress Reports. All key stakeholders from the Investment Panel will have a responsibility to comment on and agree the Project Plan. Key Tasks together with target milestone dates are set out in the table below:

| Task Name | Target Milestone Date |
|---|---|
| Business Case Approval | February 2021 |
| WRIF Strategy agreed | February 2021 |
| Investment Panel established | April 2021 |
| Procurement exercise to source External Fund Management services<br>- Soft Market Testing<br>- Procurement Exercise | January – February 2021<br>March – April/May/June 2021 |
| Procurement to secure framework/panel of advisors<br>Procurement of external advisor for Property and Infrastructure Fund | February – April 2021<br>April 2021 – onwards |
| Sourcing/Recruiting of additional in-house Resources | March – June 2021 |
| Launch of WRIF | Spring/Summer 2021 |
| First Investment Panel Meeting | Spring 2021 |

435. On approval of the Business case a more detailed Project Plan will be prepared to set out all the key activities for the set up and Year 1 operation of the WRIF.

## COMMUNICATION & ENGAGEMENT

436. The purpose, scope, and operation of the WRIF will need to be clearly communicated across the Council. Effective operation of the WRIF will also require communication and engagement with stakeholders outside of the Council who may introduce potential investment opportunities.

437. A detailed marketing strategy, recognising FCA regulation, will be developed that sets out the nature of the fund, its focus and priority areas and the nature of the investment it is likely to make. This will promote the fund locally and be used to source investment opportunities.

438. The marketing strategy may consider a launch event for the Fund, advertisement, and the establishment of an online web presence to promote and support the sourcing of investment opportunities.

439. A communication & engagement strategy will also be developed that will set out the types of communication and engagement required to support the WRIF to ensure ongoing sourcing of opportunities remains effective.

## SET UP COSTS

440. Indicative costs have been prepared to indicate all the costs to set up the WRIF.

441. The indicative costs for information at this stage to set up the WRIF, following and subject to Business Case approval, is estimated to be as follows:

| Cost Item | £ Estimate |
|---|---|
| Procurement of External Fund Managers | £60,000 |
| Procurement of Framework for External Advisors | Broadening of existing procurement so no cost to WRIF |
| Marketing, Communication & Engagement (including website) | £50,000 Budget |
| IT portal for fund applications | £20,000 |
| Legal/Tax Advice for standard documentation e.g. loan agreements | £50,000 |
| External support to produce WRIF Business Plan | £60,000 |
| **Total** | **£240,000 estimate** |

442. In addition to the external costs identified in the table above, the Council must make an allowance for officer time required to make the WRIF operational. Short term roles could include:

- Use of an investment manager to set up systems
- Business Advisors support
- Administrative function

443. As stated, there will be a call on senior management time to ensure that the WRIF is fit for purpose and is aligned with the Council's objectives.

444. The costs in the above table are subject to further review and testing and an updated analysis will then be included in the operational plan for the WRIF.

445. The overall role details and split between the Communities and Commissioning and Finance directorates will form part of the business plan report. This will include the costs of running the WRIF and will be considered in more detail as part of the overall business plan.

Running and Operating Costs

446. Running and operating costs of the Fund will need to be accounted for and monitored in relation to the performance of the Fund. It is proposed that the Fund will cover all internal costs for resources and external costs for management as well as any transaction fees and charges. The aim is to make the Fund run as efficiently as possible, seeking to pass costs on to borrowers wherever appropriate. This will be generally achieved through a market normal transaction charge for any investment. The total running/operating costs for the WRIF are expected to account for in the region of 2% of the total Capital invested, including estimates based on market feedback. In the financial model detailed in the Finance Case…

## RISK MANAGEMENT STRATEGY

447. The Council's risk management strategy will be embedded by the Investment Panel into its management of the WRIF and robust monitoring process of individual investments as well as the portfolio as a whole. Performance of the WRIF will be monitored by the Investment Panel and reported through the highlight reports and the use of a risk log or register and as part of the Quarterly reporting to Cabinet.

448. The Member Oversight Group will have the opportunity to request further input into 'any investments where the risk of investment requires further scrutiny, or the risk of default has increased following the original investment decision.

449. There are a number of risks that the Council should note that could impact on the delivery of this scheme and progression to establish the WRIF. The table below is not exhaustive, but reflects a collection of the key risks:

| Risk | Mitigation |
|---|---|
| **The public finance environment**<br>Changes to PWLB and other recent guidance from central government 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 to demonstrate the economic, social and environmental benefits to be delivered via the investment in order to meet the current guidance. 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 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.<br><br>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.<br><br>A clear exit strategy should be in place to ensure that investments only remain live when delivering against the investment criteria agreed. |
| **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.<br><br>The contract for external fund managers will set the parameters for investment to mitigate this risk.<br><br>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 performance of the WRIF and the Council losing money. | Sensitivity testing analysis has been undertaken to model the WRIF to demonstrate that overall investment performance can be achieved in a range of 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.<br><br>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. |

## CONCLUSION

450. The Management Case concludes that the Council intends to resource and manage the WRIF using robust governance and decision-making arrangements and by sourcing resources internally and externally to the Council.

451. It is intended that the WRIF and the progress of investments will be managed and monitored using established project management processes, regular reporting and effective risk management including:

- A clear resourcing proposal has been made that indicates the type and range of resources required to manage the WRIF effectively;
- A clear management approach has been described that will see the Council put in place a mixed economy model whereby external resources are sourced and procured to support the WRIF in a tailored way to provide skills, experience and expertise where required.
- A clear methodology is proposed for consideration of investment opportunities via a SIFT and Business Case approach that will ensure that resources are allocated appropriately to undertake due diligence only on those investments that are strategically aligned with the objectives of the Fund;
- An Investment Panel is to be established that will have responsibility for considering investment opportunities, making recommendations to Cabinet, managing, and monitoring performance of the WRIF and reporting to Cabinet on performance at portfolio level.

- A Member Oversight Group will be established for the scrutiny of investment decisions where quarterly monitoring reports will be referred and any individual investments or investment decisions can be referred for further scrutiny.
- Once investments have been approved by Cabinet, the governance arrangements are sufficiently robust to ensure effective management, monitoring and measurement of performance of the Fund;
- A detailed project plan will be put in place to drive an efficient process for set up of the WRIF and to determine the key milestones and activities required in the first year of operation;
- A marketing strategy and communication & engagement strategy will be developed and put in place to communicate the role of the WRIF and support the sourcing of investment opportunities.
- High level summary of Risks have already been identified with appropriate mitigating strategies and these can form the basis of a more detailed and effective risk management plan and approach to be taken forward by the Council once the Fund is in operation.

452. Considering the above, there are appropriate management and governance arrangements proposed to ensure the effective set up and ongoing management of the WRIF.

# 8. Way Forward

453. The Business Case confirms the preferred approach to establish the Warwickshire Recovery & Investment Fund. It describes the structure of the Fund, how it will be funded, resourced, managed and monitored.

454. The Council will seek approval of the Business Case from Cabinet to establish the WRIF, agree the WRIF Strategy, agree governance arrangements and seek the approval of Full Council where required.

455. Approval will also be requested to commence procurement activities needed to support the management and delivery of the WRIF and the set up and running costs associated with this.

## NEXT STEPS

456. The next steps to establish the WRIF are as follows:

| Item | Next Steps | Timescale |
|---|---|---|
| **WRIF Strategy** | Approval of Strategy with necessary delegated authority.<br>Pathway agreed for annual approval by Cabinet | Short Term 3-6 months |
| **Investment Panel** | Terms of Reference agreed<br>Decision Making process approved<br>Membership agreed and set up<br>Resources secured<br>Commence regular meetings | Short Term 3-6 months<br>Short Term 3-6 months |
| **Project Plan** | Prepare detailed Project Plan for approval | Short Term 3-6 months |
| **Procurement** | Specification for External Fund Management agreed<br>Soft Market Testing exercise to refine WRIF terms<br>Procurement exercise to secure services of Fund Manager(s)<br>Procurement exercise to establish framework for advisors for call off from to support the in-house management team | Short Term 3-6 months<br>Short Term 3-6 months<br>Short Term 3-6 months<br>Short Term 3-6 months |

| Item | Next Steps | Timescale |
|---|---|---|
| **Resources** | Recruitment of resources to form in-house team | Short Term 3-6 months |
| **Marketing/ Communication & Engagement Strategy** | Prepare strategy and seek approval to implement | Short Term 3-6 months |
| **Sourcing of Opportunities** | Start to source/ identify investment opportunities<br><br>Develop pipeline of investment opportunities | Medium Term 6-12 months<br><br>Long Term 12 months + |

# Appendix A – WRIF Strategy

# Appendix B – Investment Panel Terms of Reference

## Warwickshire County Council

## Warwickshire Recovery & Investment Fund –

## Investment Panel Terms of Reference - Draft

### Introduction

1. The Warwickshire Recovery & Investment Fund (WRIF) is to be established to mitigate the impact to the County and aid the economic recovery from COVID 19. This fund will be one of the Council's significant directly controlled contributions to the economic recovery of Warwickshire amongst the much larger and broader county and government response.

2. The WRIF will provide access to finance to support businesses and leverage additional funding for the County, both of which will support the economic recovery of Warwickshire.

3. The scope and range of investments, as well as the financial criteria for individual investments and the portfolio of investments are set out in the WRIF Strategy. This WRIF Strategy, and all the parameters within it, should be agreed by Cabinet on an annual basis.

4. A robust governance and accountability process, through establishment of an Investment Panel, is proposed for adoption whereby all investment opportunities will be assessed via a consistent decision-making process that will ensure that all the commercial considerations are assessed for the investments progressed by the WRIF. The Investment Panel will monitor the performance of the WRIF at a portfolio level and also guide and make recommendations on any investment decisions for any aspect of the Fund that are to be managed in house for final decision by Cabinet.

5. The Investment Panel is proposed to be an officer body which does not have any collective decision-making powers. The purpose of the Investment Panel is to provide a consistent decision-making process for the investments progressed by the WRIF. The Investment Panel will also monitor the performance of the WRIF at a portfolio level and make recommendations [to Cabinet in respect of proposed investments].

6. Cabinet will approve individual investment decisions for all aspects of the Fund that are to be internally managed within a total investment portfolio size of £140M and in line with the criteria set by the WRIF Strategy.

7. The Panel will report to Cabinet to whom it will also refer investment decisions that fall outside of the parameters of the WRIF Strategy.

8. A Member oversight group will be established for the scrutiny of investment decisions where quarterly monitoring reports will be referred and any individual investments or investment decisions can be referred for scrutiny.

**The role of the Investment Panel**

9. Where elements of a Fund are internally managed by the Council (with the support of external advisors), the role of the Investment Panel is to:

- Review and update the WRIF 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.
- Oversee the governance and decision-making process for investments to ensure investment opportunities are thoroughly evaluated and appropriate due diligence undertaken
- Consider Business Case proposals - Review, challenge and make 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
- Provide updates to Cabinet (and Member Oversight Group) on the performance of the Portfolio

10. Where elements of a Fund are externally managed the role of the Investment Panel is to:

- Review and update the WRIF Strategy to reflect the current needs of local businesses, the local economy and investment market.
- Provide contract management of External Fund Managers/Management
- Monitor the progress and performance of the overall portfolio
- Provide updates to Cabinet (and Member Oversight Group) on the performance of the Portfolio

Where elements of a fundare externally managed, the role of the Council will be limited and the only control will be via the procurement exercise to appoint and by specifying the criteria, limits and requirements as based on the WRIF Strategy.

11. The Panel will receive SIFT Documents and Business Cases setting out investment opportunities that are strategically aligned with the WRIF objectives for recommendations to Cabinet for approval, rejection, or referral. The Investment Manager will present the investment opportunity and the Panel will make a recommendation that will be referred to Cabinet to then agree or reject an investment opportunity.

12. The Panel will report regularly to Cabinet to whom it will also refer investment decisions that fall outside of the parameters of the WRIF Strategy or the delegated financial limits.

13. The Panel will monitor the progress and performance of individual investments and the overall portfolio and make decisions to execute exit strategies where and when appropriate. The Panel will provide regular updates to Cabinet on the performance of the WRIF portfolio.

**Membership**

14. The membership of the Investment Panel is proposed as:

- Strategic Director for Communities (Chair)
- Strategic Director for Resources (optional)
- Business & Economy
- Governance & Policy
- Growth/Regeneration
- Property/Housing
- Finance Team
- Legal
- Independent Advisor
- External Advisors (as required)

15. The Investment Panel will be supported by other officers who will attend or present but not be formal members.

16. In addition, the Panel will be supported by a team of external advisors that will be available via frameworks to call off as required, including:

- Legal advisors
- Financial advisors
- Tax advisors
- Property valuation
- Independent advisors
- Technical advisors/industry specialists
- Peer Review/Business Leader/Private sector representative.

**Quorum**

17. A minimum of 4 Investment Panel members is required to meet quorum with the Chair plus minimum representation from Finance, Legal and Business & Economy.

**Frequency**

18. The Panel will meet monthly or when an investment decision is required.

**Agenda items, Meeting Papers & Reporting**

19. The Investment Panel Agenda, Highlight Reports and papers should be distributed to Panel members at least five (5) working days before the Panel meeting. Exception reports may be sent out from time to time by the Board Chair as thought appropriate.

20. Formal minutes will be recorded from every meeting including a record of any recommendations/ decisions for audit trail and transparency.

# Appendix C – Scale of Benefits

**Business Investment Growth (£90m)**

| Projected outcomes | Lower | Middle | Upper |
|---|---|---|---|
| Jobs created/safeguarded | 4,081 | 4,801 | 5,521 |
| Annual regional GVA (£m) | 85.9 | 101.0 | 116.2 |
| Businesses created | 2,160 | 2,541 | 2,922 |
| Private sector leverage (£m) | 70.4 | 82.8 | 95.2 |
| Public sector leverage (£m) | 23.5 | 27.7 | 31.9 |
| No of successful innovation initiatives | 2,008 | 2,363 | 2,717 |
| No of successful environmental initiatives | 2,705 | 3,183 | 3,660 |
| No of businesses integrating new products, processes or services | 3,613 | 4,250 | 4,888 |

**Local communities and enterprise (£10m)**

| Projected outcomes | Lower | Medium | Upper |
|---|---|---|---|
| Jobs created/safeguarded | 453 | 533 | 613 |
| Annual regional GVA (£m) | 9.6 | 11.3 | 13.0 |
| Businesses created | 240 | 282 | 325 |
| Private sector leverage (£m) | 7.8 | 9.2 | 10.6 |
| Public sector leverage (£m) | 2.6 | 3.1 | 3.6 |
| No of successful innovation initiatives | 223 | 263 | 302 |
| No of successful environmental initiatives | 301 | 354 | 407 |
| No of businesses integrating new products, processes or services | 401 | 472 | 543 |

**Property & Infrastructure £40m)**

| Projected outcomes | Lower | Medium | Upper |
|---|---|---|---|
| Jobs created | 506 | 632 | 759 |
| Jobs safeguarded | 278 | 348 | 417 |
| Annual regional GVA (£m) | 20 | 25 | 29 |
| Businesses created | 18 | 22 | 27 |
| Land remediated (hectares) | 15 | 19 | 23 |

# Appendix D - Legal Advisors Report

**Legally Privileged and Confidential**

# Appendix D – Public Works Loan Board – Lending Objectives

| Type | Description |
|---|---|
| Service | Normal local authority capital spending, for example education, highways, transport, social care, public health, cultural services, environmental services, regulatory services, and Fire and Rescue Services, as would be captured in the MHCLG Capital Outturn Return. |
| Housing | Normal local authority general fund or housing revenue account activity, as would be captured in the housing sections of the MHCLG Capital Outturn Return. In principle this includes land release, housing delivery, and subsidising affordable housing. |
| Regeneration | • Addressing economic or social market failure by providing services, facilities, or other amenities of value to local people which would not otherwise be provided by the private sector<br>• Preventing negative outcomes including through buying and conserving assets of community value that would otherwise fall into disrepair<br>• Investing significantly in assets beyond the purchase price, developing assets to improve them and/or change their use<br>• Generating significant additional activity that would not otherwise happen without the local authority's intervention, for example creating jobs and/or social or economic value<br>• Investments that recycle income to related projects with similar objectives rather than income being applied to wider services |
| Treasury Management | Restructuring or extending existing debt from any source, including the restructuring of internal financing |
| Prevention of Social or Economic Decline | • Investments that prevent a negative outcome, for example conserving assets of community value that would otherwise fall into disrepair, or providing support to maintain economic activity that would otherwise cease<br>• Investment where there is no realistic prospect of support from any other source<br>• investments with a defined exit strategy so that investments are not held for any longer than is necessary to achieve their objective |

MHCLG issued guidance following the 2020 PWLB consultation stating that authorities that invest make Non-Treasury investments for the above reasons will have access to PWLB lending.

Local authorities that choose to invest for other reasons, or who choose to invest purely or primarily for yield will not be allowed to access PWLB lending for a period of time. In these cases, lending will be available from other sources, however it is foreseeable that the credit rating and risk profile of a local authority will be adversely impacted where is been refused access to the PWLB, and this would foreseeably impact on the lending rates and terms made available to the local authority.

# Appendix E – Financial Model

**Property & Infrastrucutre Pillar**

| | |
|---|---|
| Max. Fund Size | £40.0m |
| # Loans | 4 |
| Average Loan Size | £10,000k |
| Interest Rate | 6.5% |
| Arrangement Fee | 0.0% |
| Loan Period (25%) | 3 Yrs |
| Loan Period (50%) | 5 Yrs |
| Loan Period (25%) | 7 Yrs |
| Default Rate | 0.0% |
| Recovery on Default | 100% |

Business Investment Growth Pillar

| | |
|---|---|
| Max. Fund Size | £90.0m |
| # Loans | 18 |
| Average Loan Size | £5,000k |
| Interest Rate | 5.0% |
| Arrangement Fee | 0.5% |
| Loan Period (25%) | 3 Yrs |
| Loan Period (50%) | 5 Yrs |
| Loan Period (25%) | 7 Yrs |
| Default Rate | 3.0% |
| Recovery on Default | 80% |

**Communities & Enterprise Pillar**

| | |
|---|---|
| Max. Fund Size | £10.0m |
| # Loans | 100 |
| Average Loan Size | £100k |
| Interest Rate | 8.0% |
| Arrangement Fee | 0.5% |
| Loan Period (25%) | 2 Yrs |
| Loan Period (50%) | 3 Yrs |
| Loan Period (25%) | 5 Yrs |
| Default Rate | 30.0% |
| Recovery on Default | 25% |

| | Total WRIF | Business Growth | Communities & Enterprise | Property & Infrastructure |
|---|---|---|---|---|
| Gross Funding | £140m | £90m | £10.0m | £40m |
| Peak Funding | £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** |

## Sensitivity Analysis

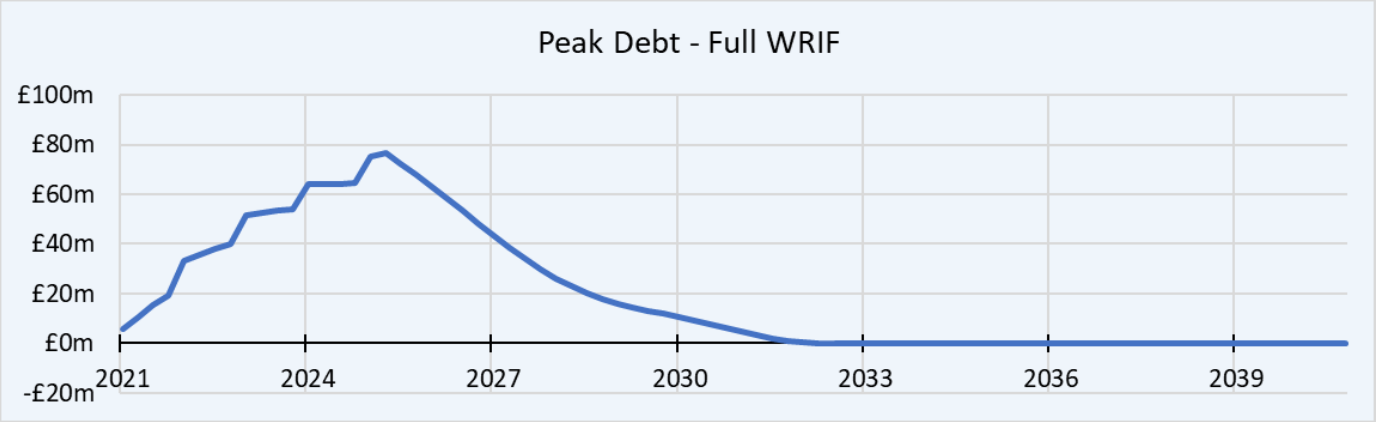
### Monte Carlo Confidence Range

| | | | | |
|---|---|---|---|---|
| **Downside Risk (NPV)** | **£3.2m** | **£2.2m** | **-£2.4m** | **£2.7m** |
| **Upside Potential (NPV)** | **£6.2m** | **£3.9m** | **-£0.1m** | **£2.7m** |

### Monte Carlo Risk Analysis

| | | | | |
|---|---|---|---|---|
| % Chance of Positive NPV | **99%** | 99% | 0% | 99% |

Peak Debt




**ANNUAL CASH FLOW**

| Council (Full WRIF) | Gross | NPV | 20/21 | 21/22 | 22/23 | 23/24 | 24/25 | 25/26 | 26/27 | 27/28 | 28/29 | 29/30 | 30/31 | 31/32 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| PWLB Interest | -£9.5m | -£7.2m | £0k | -£196k | -£789k | -£1,235k | -£1,536k | -£1,803k | -£1,516k | -£1,028k | -£622k | -£383k | -£244k | -£104k |
| MRP | -£2.8m | -£2.2m | £0k | -£94k | -£351k | -£495k | -£422k | -£419k | -£477k | -£327k | -£147k | -£24k | -£24k | -£21k |
| Running Costs | -£2.8m | -£2.1m | £0k | -£448k | -£448k | -£448k | -£448k | -£448k | -£80k | -£80k | -£80k | -£80k | -£80k | -£80k |
| Arrangment Fee | £0.5m | £0.4m | £0k | £110k | £110k | £110k | £110k | £60k | £0k | £0k | £0k | £0k | £0k | £0k |
| Interest Repayment | £21.0m | £15.9m | £0k | £413k | £1,741k | £2,744k | £3,425k | £4,026k | £3,395k | £2,292k | £1,375k | £837k | £534k | £230k |
| **Net Council Position** | **£6.5m** | **£4.9m** | **£0k** | **-£215k** | **£263k** | **£677k** | **£1,129k** | **£1,416k** | **£1,323k** | **£858k** | **£525k** | **£351k** | **£187k** | **£25k** |

# Glossary

This section contains some of the key terms used in the business case.

| Term | Definition |
|---|---|
| **COVID-19** | Coronavirus disease 2019 (COVID-19) is a contagious disease caused by severe acute respiratory syndrome coronavirus 2 (SARS-CoV-2). |
| **SME** | Small Medium Sized Enterprises |
| **Mixed Economy** | Delivery of the Fund's objectives lie with both internal and external fund managers |
| **Mezzanine Finance** | Mezzanine financing is a hybrid of debt and equity financing that gives the lender the right to convert to an equity interest in the company |
| **Corporate Guarantee** | Where the Council uses its corporate strength to provide security for a financial liability |
| **Interest Cover Ratio** | Net Income / Interest Expenditure in a given year |
| **Debt Service Cover Ratio** | Net Income / (Interest Expenditure + Principal Repayment) in a given year |
| **Net Present Value** | The sum of the discounted cash flow. If discount rate = x% than the discount factor for Year 1 = 1 / (1 + x)^1 , Year 2 = 1 / (1 + x)^2, Year 3 = 1 / (1 + x)^3, Year n = 1 / (1 + x)^n |
| **Internal Rate of Return** | Rate of return in a given cash flow. Another definition is the discount rate at which the NPV = 0. |
| **Yield on Cost:** | Net Income / Total Capital Expenditure |
| **Profit on Cost:** | Profit / all investment cost |
| **Loan to value/loan to cost ratios** | LTV: Outstanding Debt Principal (Debt Amount) / Asset |
| **Value LTC:** | Outstanding Debt Principal (Debt Amount) / Total Capital Expenditure |
| **Debt investment** | A debt investment involves the loan of money in exchange for the promise of a return of the principal loan plus interest. Debt investments tend to be less risky than equity investments but usually offer a lower but more consistent return |
| **Equity investment** | Equity investment refers to buying shares in a company and thereafter holding those shares in order to gain 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. |