County Council

1 July 2021

Warwickshire Recovery and Investment Fund Addition to the Capital Programme

Recommendation

That Council approves the addition of the Warwickshire Recovery and Investment Fund to the Capital Programme at a cost of up to £130 million, funded from additional borrowing and phased over the five years as set out in paragraph 4.3.

1. Purpose of the Report

1.1. In February 2021, Council approved that as a priority over the next 12 months an investment proposal should be brought forward for decision supporting business innovation, investment and inward investment through a Warwickshire Recovery and Investment Fund (WRIF), as part of our place shaping to help residents prosperity.

1.2. This resulted in a Cabinet decision approving, in principle, the establishment of a WRIF and authorising the Strategic Director for Resources to finalise the proposals and fund allocations and to develop the Year 1 Business Plan.

1.3. This work has now been completed and at its meeting on 17 June 2021, Cabinet approved a WRIF Business Plan for 2021/22 and the WRIF Investment Strategy. Full details of the WRIF Business Case and Business Plan can be found in supporting papers available via the Council's website.

1.4. This approval was subject to Council approving:

- the £130 million required to deliver the WRIF be added to the Council's 2021-26 capital programme; and
- the changes required to the Council's Treasury Management and Investment strategies to facilitate the delivery of the WRIF.

1.5. The latter report is elsewhere on today's agenda. The purpose of this report is to seek Council's approval for the required increase in the Council's capital programme.

2. Executive Summary

2.1. The WRIF is a significant Council policy initiative to support its strategic place shaping agenda and its recovery and regeneration strategies in response to the economic impact of the Covid 19 Pandemic.

2.2. WRIF is aligned to and will help deliver the Council's strategic objectives, providing direct support to delivery of the Council's strategic outcome "Warwickshire's economy is vibrant and supported by the right jobs, training, skills and infrastructure", which in turn helps the Council support Warwickshire communities and make the best use of resources.

2.3. The objectives for the WRIF are to:

- Fill a gap in access to finance that helps businesses in Warwickshire start, grow and scale up; or helps businesses locate to the county. Businesses located just outside of the county may be considered for finance, if there are clear benefits to Warwickshire subject to compliance with any applicable legal and/or financial frameworks;
- Leverage additional resources or funding for the county through the investment and support of key growth businesses;
- Make investments that deliver benefits and social value to the residents and communities of Warwickshire in both the short term (0-12 months) and medium term (1-5 years);
- Support investments that make a contribution towards meeting net zero carbon goals; 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.

2.4. In meeting these objectives, the main principles of how the WRIF should operate are:

- To increase the Council's ability to offer space tailored to meet the needs of existing businesses wanting to grow in Warwickshire and to attract new business to Warwickshire resulting in increased employment opportunities. The Council as a result will have a greater location incentive to keep and attract business to Warwickshire;
- To enable development in the County, facilitating new employment, land and commercial premises and which could also include investing in or building commercial sites and premises when the need is confirmed, and contract arrangements are in place with the organisation needing the premises;

- Support businesses based within Warwickshire and looking to grow or looking to re-locate in the county. Businesses located just outside of the county may be considered for finance, if there are clear benefits to Warwickshire in providing this support, subject to compliance with any applicable legal and/or financial frameworks;
- 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;
- Target priorities by promoting investment in priority sectors, business types and investments that enable development, and provide wider social value benefits across the Warwickshire economy;

2.5. It is intended that the WRIF will give a particular focus to investment opportunities that:

- Stimulate the creation of skilled and/or entry level jobs in the county;
- Can or will leverage additional resources or funding;
- Help meet the net zero carbon targets for the Council and County; and
- 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.

2.6. The financial nature of the WRIF is that it will provide access to funding, on a repayable basis. It has been modelled on the basis that the WRIF will be financially sustainable. Overall, the Business Plan demonstrates that, with a notional £140m investment in the WRIF and on the base assumptions, the WRIF would generate a net return of £4.6m. This equates to a net return on investment of 3.3%.

2.7. The WRIF is split into three “Pillars”, the Business Investment Growth pillar (BIG), the Property and Investment Fund pillar (PIF) and the Communities and Enterprise Pillar pillar (LCE). Each of these focusses on a different investment need in order to provide the coverage considered necessary to advance the funds objectives.

2.8. At this point in time the £140m figure for investment in the WRIF over five years is considered to be the upper limit of what is affordable and reasonable to invest. Within this overall £140m figure for WRIF, a cap of £90m has been allocated for the Business Investment Growth pillar which has the lowest risk and strongest return. There is a £40m cap for Property and Infrastructure Investment Fund. Together these two pillars total £130m meeting the definition of capital necessitating the addition to the capital programme. The Communities and Enterprise Pillar has a much lower £10m cap, funded from internal resources, set for this higher risk area to minimise the risk of ‘losses’ on that pillar and ensure the overall WRIF makes a positive return, is affordable and takes account of the Council’s fiduciary duties.

2.9. The net financial return from the potential £140m investment makes it critical that the operational requirements within which the WRIF operates are set at levels which support a positive financial outcome and minimise the risk to the Council’s investment, whether this be through investment returns, the level of default risk the Council is prepared to accept or the level of security over loans required. These requirements have been a focus of attention in the development of the business plan, the drafting of the WRIF Investment Strategy and in the development of the operational arrangements for the WRIF.

2.10. Given the modelled levels of return and in order to ensure that the Council meets its fiduciary duty to taxpayers, the outcomes in terms of the service and wider economic benefits to the residents of Warwickshire from the WRIF and individual investments should demonstrably outweigh the potential financial risks at both Fund and individual project level. The spreading of investment over 5 years provides the opportunity to assess risk experience and adjust investment amounts or investment protocols in later years. Financial monitoring and taking appropriate action in the light of experience will be a critical feature of risk management.

2.11. The overhead and administrative costs of running the WRIF will be recovered through the use of application fees and from the interest paid on any loans. As a result, there is a minimum level of activity that the WRIF will need to undertake to ensure it meets the financial objective of at least breaking even. This is currently estimated to be £77.0m. Any under recovery of the operating costs will be an additional cost that will need to be met from future MTFS allocations.

2.12. Given the nature of the Fund any returns over and above those repaying the original loans and funding the WRIF running costs will be available to support the ongoing priorities set out in the WRIF investment strategy or to invest in other Council priorities. The options and affordability will form part of the annual MTFS refresh, Treasury Management Strategy and Council Investment Strategy refreshes to be approved by Council and then built into the WRIF Investment Strategy to be approved by Cabinet.

3. Fiduciary Duties

3.1 In making decisions about approving the funds, the Council must have regard to its fiduciary duties. These can be summarised as the Council acting as trustee over the tax and public sector income (and liabilities) on behalf of its local taxpayers and other residents. The Council in effect holds money but does not own it; rather, it spends money (and incurs liabilities) on behalf of its business rate and council taxpayers.

3.2 Due to the size of the proposed investments going via the WRIF together with the risk of losses which attach to any investment and the fact that the Council will be funding something different from typical local authority activities, has resulted in careful consideration being given to the Council's fiduciary duties in relation to this project. A summary of this position is set out below.

Considerations	How addressed
Clarity of the policy objectives/outcomes which WRIF (or its separate streams) are designed to support/deliver	The WRIF is a key component of the Council's Covid-19 Recovery Plan. The economic case for the WRIF was initially developed last year, and the forecasting was updated in light of the likely impacts of the second national lockdown and again in light of the extension of the various Government support schemes (particularly job furloughing, business rates and tax holidays), and the successful movement along the roadmap out of lockdown and the rollout of vaccinations. While the revised forecasts suggest an improved picture and a faster recovery than initially thought, this is clearly not guaranteed, and it is vital that Warwickshire seeks to maximise the opportunities for recovery and future investment that could otherwise occur elsewhere. In summary, the implementation of the WRIF aligns with the Council's objective to promote economic recovery, the economic outlook remains challenging and the introduction of the WRIF coincides with the current planned phasing out of central government support, including the various Business Intervention Loan Schemes.
Options Appraisal – assessment of WRIF versus alternative routes to deliver the	The options appraisal is set out at paragraph 142 of the WRIF Business Case (received

policy/objectives. Why are the WRIF proposals best suited to deliver these?	by the meeting of Cabinet on 11/2/21) and concludes that WRIF is the most appropriate policy option for the Council to pursue
Financial impact (to the Council) of the proposals and the risks of non-recovery and steps to mitigate/manage such risks. If some of funding is expected to be non-recoverable, this should be identified.	Overall, the Business Plan demonstrates that, with a notional £140m investment in the WRIF and on the base assumptions, the WRIF would generate a net return of £4.6m. This equates to a net return on investment of 3.3%. This gain is the aggregate of an estimated net return on the BIG of £3.1m, on the PIF of £2.7m offset by an estimated net loss on the LCE of £1.2m. However, the estimated losses with the LCE need to be considered in conjunction with the potential indirect benefits generated by supporting small business and the associated jobs. Applications will be assessed against set criteria which support a positive financial outcome and minimise the risk to the Council's investment. Further, using external expertise to manage the LCE will assist in mitigating the risks associated with it. Any returns over and above those repaying the original loans and funding WRIF running costs will be available to support the ongoing priorities set in the WRIF investments strategy or to invest in other council priorities. There is a process for an annual review of WRIF performance which will inform the Council's financial commitments for the following year, helping to manage and mitigate risk
Benefit of WRIF to target groups (who would benefit under WRIF) fairly balanced against the interests of Warwickshire's taxpayers/residents i.e. the impact of the money being spent on WRIF (especially if a loss is projected or high level of risk is involved) on the Council's other activities/level of Council Tax.	The direct economic benefits of WRIF are estimated in paragraphs 214 and 215 of the WRIF Business Case (received by the meeting of Cabinet on 11/2/21). These show an annual contribution to the county's gross value-added of £110m – 160m

Fiduciary Duty considerations are not a one-off exercise. They remain relevant throughout the life of the programme. Members and officers need to continue to consider the above points i.e. act in an efficient 'business like' manner	This will be kept under review throughout the duration of the fund and any future Fund decisions taken

3.3 The WRIF Business Plan anticipates that "the security taken by the Council through the loan agreement will be at least sufficient to allow the WRIF to recoup a significant, if not all, of the initial investment". For clarity, this is likely to be the case for the investments in the BIG and PIF pillars. However, due to the nature of the loans made through the LCE pillar, these loans are much less likely to be backed by security and therefore it is unlikely that loans made through this, currently much smaller, pillar will be recoverable in the event of default by the borrower. The risk of non-recovery for LCE loans is therefore higher than for the BIG and PIF loans.

3.4 However, the fact that there is a fund that is not projected to be recovered in full does not, in itself, mean that the Council is failing in its fiduciary duties if it supports the WRIF. It does mean that the Council needs to recognise that there is a potential risk, and decision makers need to properly consider the issues and considerations discussed above (and in the Business Case) before reaching their decisions.

3.5 The Council has sought external legal advice in developing the WRIF proposals. This covers the Council's powers to set up the fund, relevant considerations prior to investing or offering products through the fund (including the Council's fiduciary duties in respect of public money and appropriate governance), changes to state aid rules post EU transition, and regulatory requirements. The full legal advice is available to members on a confidential basis if required

4. Financial Implications

4.1. From a local authority accounting perspective, the majority of the potential activities of the WRIF are defined as capital expenditure. This includes the provision of loan finance for the creation/development of a fixed asset (whether or not the asset is owned by the Council) and the purchase of shares/equity investment. The financial model underpinning the WRIF assumes that £130m of the £140m investment will meet the definition of capital expenditure. It is for this reason that Council is requested to add a capital facility of £130 million to the Capital Programme.

4.2. The ability to draw down funding will be subject to further separate decisions as set out in the governance arrangements for the WRIF. The Capital Programme facility will be reviewed and/or updated via the Budget Resolution approved by Council in February each year.

4.3. The initial phasing of the Council's investment in WRIF will be phased across the 2021-26 capital programme set out in Table below.

	Addition to the Capital Programme £m
2021/22	20.0
2022/23	30.0
2023/24	30.0
2024/25	30.0
2025/26	20.0
Total	**130.0**

4.4. At the end of March 2021, the Council's level of outstanding debt was £321m with a further £200m of financing forecast to be required over the period of the 2021-26 MTFS as the financing approved for the Council's own Capital Programme (including the Capital Investment Fund) and the investment required to support the delivery of the Warwickshire Property and Development Group (WPDG) business plan.

4.5. As stated above, the WRIF business plan estimates up to £130m additional capital spend through the WRIF, with £10m to be funded from internal resources. This borrowing would be additional to our current plans.

4.6. Whilst £130m is the maximum gross exposure to external debt within the WRIF, repayment profiles will mean that peak debt is significantly below this level. The business plan estimates that the maximum peak debt will be £67m in 2025/26. The financial modelling behind the Business Plan has demonstrated a peak funding level of £70.6m over the 5-year investment cycle. The Council is also able to manage risk based on the overall economic and market conditions at the time. If losses start to increase, then the Council has the ability to slow or stop future investments or adjust lending criteria/parameters and invest in more secure counter parties.

4.7. Any request from WRIF for loan/equity finance will need to be considered in the context of the wider County Council borrowing profile. Our total borrowing profile is driven by the sum of Capital Programme plus WPDG plus the WRIF.

Any assessment of affordability and risk from a treasury management and investment perspective will need to consider all of these in the round. It also needs to be recognised that this wider context will change over time and therefore the assessment needs to be “live” at the point the decision is made.

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

4.9. The use of borrowing to fund any WRIF activity means the Council will need to be able to justify to PWLB (and therefore HM Treasury) that the Council is taking out the borrowing primarily for service reasons rather than to generate a commercial return. The Investment Strategy approved by Council in February 2021 and the refresh being considered today make it Council policy to ensure our investment activity does not fall foul of the PWLB lending criteria that could exclude the Council from using this source of borrowing for the entirety of our capital programme for three years.

4.10. As a local authority, the Council is required to make sure it acts prudently in setting aside resources to repay the principal of any loans taken out to fund capital expenditure, which is the nature of the loans/equity investment it would be providing through the WRIF. The recent public interest reports on local authority owned companies determined that not setting aside resources because of an assumption that income would be received to repay the loans before they were due was not a prudent approach. Therefore, the County Council will make provision for MRP (the provision for the repayment of principal) in its revenue budget.

4.11. The repayment of loans made through the WRIF will be structured in such a way as to ensure sufficient levels of repayment to offset the costs of financing our PWLB loan/s and hence creating no additional call on the Council’s revenue budget.

4.12. The creation of the commercial risk reserve (£7.5m) as part of the 2021/22 MTFS provides additional financial cover in the short term should the level of loan repayment defaults be higher than those expected in the business plan until such time as corrective action to the operational arrangements for the WRIF can be put in place or the next MTFS refresh.

5. Environmental Implications

5.1. Whilst there are no direct environmental implications of an addition to the capital programme, the modelled benefits of the WRIF itself include enabling carbon reduction through investment in environmentally and/or economically sustainable businesses that are driving climate change benefits, carbon neutral and low carbon initiatives, and an increase in the use of/public support for zero carbon technologies.

6. Supporting Information

6.1. Arising from the work under the Council's Covid-19 Recovery Plan, WRIF is a direct support for the Council's objectives and outcomes. Subject to Council approval of the changes to the Treasury Management Strategy and Investment Strategy also before this Council meeting, the addition of the Warwickshire Recovery and Investment Fund to the Capital Programme 2021/22 at cost of up to £130 million is recommended.

Background Papers

None

Supporting Papers

1. Cabinet Report 17 June 2021
2. Cabinet Report 11 February 2021

	Name	**Contact Information**
Report Author	Virginia Rennie, Strategic Finance Nichola Vine, Legal & Democratic	vrennie@warwickshire.gov.uk, nicholavine@warwickshire.gov.uk
Assistant Director	Andy Felton Assistant Director Finance Sarah Duxbury Assistant Director Governance and Policy	andrewfelton@warwickshire.gov.uk sarahduxbury@warwickshire.gov.uk
Lead Director	Rob Powell Strategic Director for Resources	robpowell@warwickshire.gov.uk
Lead Member	Peter Butlin Portfolio Holder for Finance and Property	peterbutlin@warwickshire.gov.uk

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