Fit for the future

creating a prosperous and healthy Torbay

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Investment Fund Strategy

Version 8

Torbay Council

Investment Fund Strategy

1. Background

As part of its efficiency plan and transformation programme the Council needs to increase its future local taxbase income (Council tax and NNDR) by investing capital resources within Torbay to stimulate growth. Capital resources could be a combination of asset purchase, co investment in projects or capital loans. The Council also seeks to contribute to regeneration within Torbay so as to support the local economy and the associated positive impacts upon deprivation.

As clarification the following descriptions have been used:

"Investments – Yield". These are property purchases where the objective is to increase rental income to the Council.

"Investments – Taxbase". These are property purchases where the objective is to increase NNDR or Council tax income to the Council.

"Investments – Loans or Co Investment". These are loans to business for capital expenditure where the objective is to increase rental income to the Council or to increase NNDR or Council tax income to the Council. Co Investment is where Council with another investor provides finance or jointly purchases.

"Property Purchase" – property to include purchase of land and/or buildings.

"Regeneration Investment" – These are property/land purchases or loans where the objective is to support regeneration projects within Torbay.

This Policy Framework document sets out the strategy for the management of the Investment Fund. The strategy reflects a suitable balance between the risks inherent in the types of investments to be made and the financial rewards or wider regeneration outcomes obtainable whilst limiting risks appropriately. In addition, the portfolio of investments should be diversified in order to spread risks via a balanced portfolio, such diversification principally being across geographical location and the use type of investments held. Existing investments that fall within the broad remit of the Investment Fund Strategy shall be included in the portfolio to assist in creating a balanced portfolio, as well as other suitable assets held by the Council.

Initial proposals to the Investment Committee can be made by the Elected Mayor, wider Members or Officers. Proposals will be developed by Officers in consultation with the Elected Mayor and Chairman of the Investment Committee.

2. Objective – Investment Fund

To make investments for the benefit, improvement or development of the area, through a balanced investment of acquisition, retention and management of good quality investments.

The improvement or development of the area will not be constrained by the strict boundaries of Torbay as there is an evidence base that demonstrates that investment within the South West Local Enterprise Partnership (LEP) Zone area has a positive impact on Torbay's economy. LEPs were established around functional economic boundaries which reflects both labour market and wider economic interdependence. This can be evidenced through the Heart of the South West Strategic Economic Plan (see http://heartofswlep.co.uk/wp-content/uploads/2016/09/SEP-Final-draft-31-03-14-website-1.pdf **)** and the Torbay Economic Strategy (see http://www.torbay.gov.uk/DemocraticServices/documents/s35783/Torbay%20Economic%20Strategy.pdf **).** However opportunities in any geographic location will be considered where it can be demonstrated that there is a benefit to, or improvement or development of Torbay. This will not prevent the Council investing in national opportunities which have a sufficient yield by the Council or through a wholly owned company of the Council, if supported by the Monitoring Officer and the Head of Finance.

3. Scope

The maximum total level of investment shall be £200m for the Investment Fund.

4. Strategy

This Policy Framework sets out that decisions to allocate monies in accordance with this policy are not Executive decisions, and the Council has previously delegated this to the Investment Committee who shall make all decisions up to £25m in respect of all proposals. The maximum individual investment to be approved by Investment Committee shall be £25m including any estimated purchasing costs, however Full Council approval is not restricted in terms of value.

The Strategy envisages proposals in two categories:

1. investment opportunities that deliver both a financial return to the Council and a benefit, improvement or development of the area – 'Investment Opportunities,'

2. regeneration investment opportunities that deliver significant regeneration benefits to the area – 'Regeneration Investment Opportunities.'

The Committee will be held in two distinct parts, dealing with Investment and Regeneration opportunities separately.

4.1 Investment Opportunities

To make investments for the benefit, improvement or development of the area, through a balanced investment of acquisition, retention and management of good quality investments, whilst also delivering an income return to the Council.

Achieving a spread of risk across a greater number of investments and by acquiring them across the range of different property asset classes, namely retail, leisure, office and industrial, is to be desired, however it has to be recognised that opportunities to do this may not arise, and ultimately if individual business cases are robust, groupings in any individual property class should not pose any increased risk to the Council.

The principle of being relatively risk-averse whilst maximizing the return to the Council will be taken in respect of investment opportunities.

The investment portfolio will include acquiring some properties to hold and some properties to dispose of depending on the anticipated lifespan of the asset, so as to ensure that the Council has a rolling stock of investments in order to achieve maximum benefit for the Council.

Minimum Yield Required for investment opportunities (before costs)	2% above estimated borrowing costs (interest and MRP or if capital loan prevailing borrowing rates + 2%)

Traditionally the highest returns come from the office and industrial sub-sectors. Currently offices can provide an income return of 5.5% in quality in-town areas and between 7.5% and 8.5% for reasonable quality offices in regional and sub-regional centres. Industrial income yields can range from 6.0% up to 7.5% for acceptable quality assets. The retail sub-sector for prime retail property is lower than comparable office/industrial assets with typical yields ranging between 5% and 7% for high quality in-town properties. On this evidence it is likely that predominantly office and industrial/warehouse will be targeted for acquisition with a lesser emphasis on retail. Leisure and mixed use investments will also be eligible under the strategy.

Residential property tends to be management intensive and requires specialist expertise, and the Council has established its Housing Company in this respect. It is therefore proposed that this sector is excluded from this element of the Investment Fund strategy.

Torbay would be the preferred location for fresh acquisitions of investment properties, so that reinvestment is directly retained within the local economy and any additional capital expenditure is made in the local area. However, there is a finite and limited supply of property within the local area, and of that supply only a small proportion may be available for purchase at any time that meet the requirements of the General Investment Fund. The wider South West Local Enterprise Partnership area should also be considered for fresh acquisitions as there is an evidence base that demonstrates that investment in this area has a positive impact on Torbay's economy. However opportunities in any geographic location will be considered where it can be demonstrated that there is a benefit to, or improvement or development of Torbay. This will not prevent the Council investing in national opportunities which have a sufficient yield by the Council or through a wholly owned company of the Council, if supported by the Monitoring Officer and the Head of Finance.

The strategy does permit opportunities for co investment with partner organisations of good financial and reputational standing.

Only opportunities in excess of £500,000 will be considered for this element of the Investment Fund Strategy, given the need to consider the number of smaller investments held by the Council, in pursuance of this Strategy and the burden of administering each investment before a decision is taken.

An assessment of all risks is required in each case of fresh investment in order firstly to value it and then to check its suitability for inclusion in the portfolio. The risks fall into two categories, firstly economic and property market risks in specific property market sub-sectors and locations and secondly asset-specific risks. These can be measured and an assessment made of the likely future performance of the investment carried out based on, for example, the ranges of likely future rental growth and voids of the property and also the projected disposal price or capital value at the end of the period over which the cash flow analysis is being measured.

Financial returns are modelled over a medium-term horizon of five years, based on proposed offer prices, to determine the acceptability of each investment, and can be compared against general market forecasts.

Minimum Revenue Provision (MRP) on all proposals will be assessed on a case by case basis by the Head of Finance in line with the Council's MRP Policy.

The Head of Finance reserves the right to refer any proposed investment decision (irrespective of value) to the Council for consideration where he deems this is in the best interest of the Council.

4.2 Regeneration Investment Opportunities

To make investments for the benefit, improvement or development of the area, through a balanced investment of acquisition, retention and management of good quality investments, whilst delivering regeneration outcomes for Torbay, inter alia through;

- Job creation;
- Business rate growth;
- Opportunities that have strategic importance within Torbay, such as those that will improve key locations or address issues such as deprivation and child poverty.

Minimum Yield required for Regeneration Investment opportunities (after costs)	0% - cost neutral after estimated borrowing costs (interest and MRP or if capital loan prevailing borrowing rates must be equal to the income due). In exceptional circumstances where the regeneration benefits are significant, there may be a cost to the fund of the project, however such costs to be met from other projects within the fund which provide a financial return to the Investment Fund. Such proposals will need the agreement of the Head of Finance.

In respect of Regeneration Investments, opportunities will be pursued where there is a clear business case demonstrating how it will contribute to the regeneration of Torbay. Any surplus income after operating, borrowing and MRP costs will be ring-fenced to support both wider regeneration within Torbay and any schemes in which there could be a cost to the Investment Fund.

Sector spread will not be applicable for Regeneration Investment opportunities, as these will be focused on delivering regeneration within Torbay, which will be site specific so as to drive economic regeneration. Only proposals within Torbay will be considered for Regeneration Investment opportunities.

The strategy for Regeneration Investment opportunities does not expressly exclude residential property, although it does envisage that any residential opportunities are more likely to come forward as part of enabling development or hybrid schemes, for wider regeneration purposes.

The Strategy does permit opportunities for co investment with partner organisations of good financial and reputational standing.

Opportunities of any value will be considered for Regeneration Investments, although consideration will always need to be given to the number of smaller investments held by the Council, in pursuance of this Strategy and the burden of administering each investment before a decision is taken.

An assessment of all risks is required in each case of fresh investment in order firstly to value it and then to check its suitability for inclusion in the portfolio. Wider risks and benefits need to be considered in respect of opportunities for Regeneration Investment. It is envisaged that an outline appraisal will be prepared for consideration. Following approval of the outline appraisal, a full appraisal will be undertaken before a decision on the opportunity is made. It is however recognised that there may be some situations in which a regeneration opportunity arises at short notice, for example through auction. In these circumstances as full an appraisal as possible will need to be undertaken, and the Committee will have to consider whether it has sufficient information upon which to make a robust decision.

Financial returns are modelled over a medium-term horizon of five years, based on proposed offer prices, to determine the acceptability of each investment, and can be compared against general market forecasts.

MRP on all proposals will be assessed on a case by case basis by the Head of Finance in line with the Council's MRP Policy.

The Head of Finance reserves the right to refer any proposed investment decision (irrespective of value) to the Council for consideration where he deems this is in the best interest of the Council.

5. Financial Assumptions

	Investment - Yield	Investment - Taxbase	Investment- loans & co investment	Regeneration Investment Opportunities
MRP (Minimum Revenue Provision)	50 years land and 40 years buildings or life of asset	50 years land and 40 years buildings or life of asset	As applicable	Life of asset
Interest Costs used in appraisal	New Borrowing Rates	New Borrowing Rates	New Borrowing Rates	New Borrowing rates
SDLT & other purchase costs	Part of purchase price	Part of purchase price	-	Part of purchase price
*Fund Management Costs & ongoing client costs	0.25% of purchase price	0.25% of purchase price	0.25% of loan or investment	To be determined dependent upon project under consideration
"Green Book" Financial profile over life of asset (IRR)	Yes	Yes	Yes	Yes
**VRP (Voluntary Revenue Provision)	0.5% of purchase price	0.5% of purchase price	0.5% of purchase price - co-investment only	0.5% of purchase price

*Normally for each investment an annual payment of 0.25% of the purchase price or loan or investment, subject to a case by case evaluation and decision by the Head of Finance, will be held in a central fund to cover the following:

- external advice for future investments;
- known or expected one off future costs, such as costs associated with future negotiation or renegotiation of leases;
- bad debt provision;
- irrecoverable estate costs;

- management of assets; and
- maintenance or redevelopment costs associated with future leases.

**Consideration will be given in respect of each asset of a VRP (Voluntary Revenue Provision) of 0.5% of the cost of the purchase price before costs, which will be funded from the surplus income generated and placed in a reserve to contribute towards deminuation of the value of the asset etc. Reports will also include details in respect of paying off or writing off the purchase costs.

***The Chief Executive, in consultation with the Executive Lead for Finance, the Investment Committee and Head of Finance is authorised to amend the Fund Management and VRP percentage parameters from time to time to ensure an adequate and prudent asset management strategy is maintained.

6. Oversight

Following a decision to proceed with a proposal, whether an Investment proposal or a Regeneration Investment proposal, the Investment Committee will maintain an oversight of their progress, in the context of;

1. the overall fund;
2. Individual proposals for the Investment Fund, and
3. Individual proposals for Regeneration Investment opportunities, including monitoring their delivery and regeneration benefits (including existing investments that fall within the broad remit of the Investment Strategy which shall be included in this oversight, as well as other suitable assets held by the Council).

Investment Committee will keep under review the classification of investments, and will be able to transfer investments between the Investment and Regeneration as appropriate, as long as the relevant criteria is met.

The Chairman of the Investment Committee will determine in consultation with Officers how he wants such oversight to be presented, and the frequency of the same.