Appendix 2

Capital Expenditure Plans and Prudential Indicators: 2019/20 to 2022/23

Indicator 1 - Capital expenditure estimates
The table below summarises the SCR Group's capital investment plans for the forthcoming year and indicative estimates for the following two years.

The estimates are based on known commitments at this point in time and where grant funding streams have already been secured or there is reasonable assurance that they will be, for example, Transforming Cities Fund Tranche 2.

An assumption has also been made that the recent decision to progress on conducting a consultation on the powers to be delegated to the SCR / elected mayor will lead to the Devolution Deal being unlocked and Gainshare flowing to the SCR from 2020/21.

No assumption has been built in at this stage for successor funding for Local Growth deal funding beyond the end of the current Growth Deal in 2020/21 pending clarification from Government on the arrangements and potential allocation to the SCR.

1. Capital Expenditure Estimates	2019/20	2020/21	2021/22	2022/23
	Forecast	Proposed	Indicative	Indicative
	£'000	£'000	£'000	£'000
South Yorkshire Transport Programmes:				
SCR Group:				
SYPTE	£10,326	£9,250	£6,056	£4,179
SCR	£1,420			
Grants to third parties:				
Highways Capital Maintenance	£13,668	£12,219	£0	£0
Integrated Transport Block	£9,619	£8,428	£0	£0
Transport Capital Pot	£2,036	£1,043	£0	£0
Pothole Fund	£723	£0	£0	£0
Transforming Cities Fund - Tranche 1	£4,244	£0	£0	£0
Transforming Cities Fund - Tranche 2	£0	£30,400	£109,000	£90,100
DfT Local Major - Parkway widening	£0	£0	£0	£0
	£42,036	**£61,340**	**£115,056**	**£94,279**
LEP				
Local Growth Fund Programme	£35,458	£42,400	£0	£0
Gainshare	£0	£18,000	£18,000	£18,000
LGF 2 / Shared Prosperity Fund	£0	£0	£0	£0
	£35,458	**£60,400**	**£18,000**	**£18,000**
Corporate				
SCR operational assets	£0	£0	£0	£0
Investment property portfolio	£0	£0	£0	£0
	£0	**£0**	**£0**	**£0**
Total Capital Investment	**£77,494**	**£121,740**	**£133,056**	**£112,279**

The great majority of the SCR Group's capital programme represents grants to stakeholders and third parties in furtherance of the SCR Group's transport and economic development objectives.

The SCR Group does however, have its own capital investment plans to renew or develop assets held by the Group, principally those for which SYPTE is responsible.

Indicator 2 – Capital Financing Requirement (CFR) estimates

The table below shows how the planned capital expenditure is expected to be financed. Any capital expenditure not funded by capital grants, capital receipts, or revenue contributions, results in a need for borrowing.

2. Capital Financing Requirement Estimates	2019/20	2020/21	2021/22	2022/23
	Forecast	Proposed	Indicative	Indicative
	£'000	£'000	£'000	£'000
South Yorkshire Transport Programmes:				
Government Grants	£33,345	£54,809	£115,056	£94,279
Borrowing	£5,719	£5,279	£0	£0
Capital Receipts	£1,464	£0	£0	£0
Earmarked reserves	£1,508	£664	£0	£0
Revenue contributions	£0	£588	£0	£0
	£42,036	**£61,340**	**£115,056**	**£94,279**
Local Growth Fund Programme:				
Government Grant	£35,458	£60,400	£18,000	£18,000
	£35,458	**£60,400**	**£18,000**	**£18,000**
Corporate	£0	£0	£0	£0
	£0	**£0**	**£0**	**£0**
Net borrowing needed for the year	**£5,719**	**£5,279**	**£0**	**£0**

The borrowing need stems from the decision taken in 2018/19 to borrow up to £23.3m over the 3-year period 2018/19 to 2020/21 to support capital investment on South Yorkshire transport schemes (Rotherham Interchange, re-railing and the transport capital pot). The borrowing need forecast for 2019/20 and proposed for 2020/21 together with the actual borrowing need in 2018/19 of £12.087m is within the overall amount approved. The revenue implications of this borrowing has been factored into the South Yorkshire transport 2020/21 annual budget and medium term forecast approved by the MCA at its meeting on 27 January 2020.

The unlocking of the Devolution Deal will lead, subject to consultation, to the SCR Group acquiring borrowing powers for economic development activity. At this stage, there are no plans to exercise these powers.

Based on the above capital investment plans and capital financing proposals, the SCR Group's overall forecast underlying need to borrow or Capital Financing Requirement (CFR) is forecast to change as shown in the table below. In future CFR will be increased from changes that will be brought about from the introduction of IFRS 16 in production of SCR Financial Accounts. Work has started on this and the implications will be reported to a future meeting on the implications of the introduction.

2. Capital Financing Requirement	2019/20	2020/21	2021/22	2022/23
	Forecast	Proposed	Indicative	Indicative
	£'000	£'000	£'000	£'000
Opening CFR	£113,045	£115,603	£116,860	£112,645
movement in CFR				
Additional borrowing requirement	£5,719	£5,279	£0	£0
MRP	-£3,161	-£4,022	-£4,215	-£4,171
Capital receipts set aside for the repayment of debt	£0	£0	£0	£0
Other adjustments	£0	£0	£0	£0
Closing CFR	**£115,603**	**£116,860**	**£112,645**	**£108,474**

Indicator 3 - Amount of external debt against the Capital Financing Requirement (CFR)

The purpose of this indicator is to assess the extent to which borrowing is only being used in the medium to longer term to finance capital expenditure.

CURRENT BORROWING POSITION	2019/20	2020/21	2021/22	2022/23
	Forecast	Proposed	Indicative	Indicative
	£'000	£'000	£'000	£'000
External Debt				
-MCA Loans at 1st April	£25,660	£25,660	£25,660	£25,660
-Expected change in MCA Loans	£0	£0	£0	£0
-SYPTE Debt at 1st April	£161,375	£161,375	£108,375	£100,400
-Expected change in SYPTE Loans	£0	-£53,000	-£7,975	-£8,000
Gross Debt	**£187,035**	**£134,035**	**£126,060**	**£118,060**
The Capital Financing Requirement	£115,603	£116,860	£112,645	£108,474
Debt in excess of CFR	**£71,432**	**£17,175**	**£13,415**	**£9,586**

The benchmark recommended by CIPFA is that the estimated amount of gross debt should not exceed the estimated CFR for the current and following two years.

The reason why gross debt is in excess of CFR for the SCR Group is a legacy of previous capital financing regulations that applied to PTEs which required amounts set aside for the repayment of debt to be held in cash. This is one of the reasons for the high level of treasury investments held by the MCA as illustrated in Indicator 8.

The excess will be eliminated as the amount set aside in cash is used to repay debt as it matures. Hence, in 2023/24 the SCR Group is due to repay another significant tranche of debt amounting to £50.4m which will bring gross debt below the CFR.

The level of gross debt assumes that there will be a continuation of the current borrowing strategy whereby the borrowing need for the year is met internally from treasury investments rather than taking out externally borrowing. This is in the expectation that the cost of new borrowing will continue to exceed likely investment returns. This scenario is more likely following the Governments decision on 9 October 2019 to suddenly increased PWLB rates by 1% with immediate effect taking them up to the range 2.2% to 3%. Returns in investments by contrast currently are in the region of 1% although the proposed new investment strategy will consider options for looking to increase returns.

Indicator 4 - Ratio of Financing Costs to Net Revenue Stream

This indicator is a measure of the affordability of decisions taken to finance capital investment borrowing in the context of the SCR Group's overall financial sustainability.

Ratio of financing costs to net revenue streams	2019/20	2020/21	2021/22	2022/23
	Forecast	Proposed	Indicative	Indicative
	£'000	£'000	£'000	£'000
Interest	£13,136	£9,541	£8,359	£7,742
MRP	£3,161	£4,022	£4,215	£4,171
Less Investment Income	-£2,000	-£1,274	-£1,032	-£952
Net Financing Costs	**£14,297**	**£12,289**	**£11,542**	**£10,961**
Income - transport levy	£54,365	£54,365	£54,365	£54,365
Finance Costs/Unrestricted Revenue Income %	26.3%	22.6%	21.2%	20.2%

Interest payable is principally fixed rate PWLB borrowing. The reduction in the amount of interest payable is therefore a function of PWLB debt being repaid as it matures. A significant amount of PWLB debt is scheduled to be repaid over the 3-year period 2020/21 to 2022/23 as illustrated in Indicator 3. The return on investments is a function of the average level of treasury investments and target returns which are expected to be achieved. The reduction in investment income reflects the fact that investments are being used to settle loan repayments as they fall due reducing the level of core funds. This is in accordance with the borrowing strategy set out in Appendix 3. The modest increases in the expected returns on investments are as set out in the investment strategy in Appendix 1.

External Debt – borrowing limits – Indicators 5 and 6

There are two indicators on borrowing limits: the authorised limit and operational boundary
The **authorised limit** represents a control on the maximum amount of debt the SCR Group can borrow for capital investment and temporary cash flow purposes. Under Section 3 of the Local Government Act 2003 this limit is agreed by the MCA and cannot be revised without that body's agreement.

The authorised limit reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the long term.

The **operational boundary** is the maximum amount of money the MCA group expects to borrow during the financial year. It acts as a useful warning if breached during the year that underlying spend may be higher than expected or income lower than budgeted.

Authorised Limit	2019/20	2020/21	2021/22	2022/23
	Forecast	Indicative	indicative	indicative
	£'000	£'000	£'000	£'000
Loans	£228,500	£228,500	£175,500	£167,500
Other Long Term Liabilities	£11,500	£11,500	£11,000	£11,000
Total	**£240,000**	**£240,000**	**£186,500**	**£178,500**
Operational Boundary	**2019/20**	**2020/21**	**2021/22**	**2022/23**
	Forecast	**Indicative**	**Indicative**	**Indicative**
	£'000	**£'000**	**£'000**	**£'000**
Loans	£213,500	£213,500	£160,500	£152,500
Other Long-Term Liabilities	£11,500	£11,500	£11,000	£11,000
Total	**£225,000**	**£225,000**	**£171,500**	**£163,500**

The authorised limit allows £40m headroom over the maximum expected amount of gross debt in the year.

The operational boundary allows for £25m headroom.

This is considered affordable in the short term in the current low interest rate environment where short term borrowing rates are around 1%.

Having this headroom serves the purpose of covering short term timing differences between significant cash outflows, for example, the repayment of debt, and receipt of significant funds, without compromising the new investment strategy's aim of optimising returns through having longer term investments rather than highly liquid short-term investments. Should there be a need to borrow on a temporary basis the MCA has ready access to such funds through local authority to local authority lending.

The Other Long-Term Liabilities set out in the table below represents the PFI liability in respect of Doncaster Interchange. There is a major change to local authority accounting rules in respect of accounting for leasing which comes into effect for the 2020/21 financial year. This may lead to "right of use" leased assets being brought on balance sheet which would increase the value of Other Long-Term Liabilities. The impact of the accounting changes is still being evaluated. Should it lead to the recognition of significant additional "right of use" liabilities the authorised limit and operational boundary will be adjusted to take account of them in due course and the treasury management strategy revised accordingly.

Managing exposure to the risk of interest rate changes

<u>Borrowing</u>
All of the SCR Group's PWLB debt of £166.375m is fixed rate. As such there is no risk to the amount of interest payable from interest rate fluctuations.
There is in addition £20m of market loans where the lender has an option to change the interest rate periodically on specified call dates. As explained in the borrowing strategy in Appendix 3 it is considered highly unlikely that the lender would exercise the option in the current low interest rate environment.

<u>Investments</u>
The investment portfolio is currently weighted to short term non specified investments.
The expectations are that returns on short term investments will rise only slightly in the next 3 years.
Accordingly, there is a benefit in locking a higher proportion of investments longer term with high quality counterparties in order to enjoy the higher returns that longer term investments typically bring.