REPORT TO:	East Lothian Council
MEETING DATE:	23 February 2016
BY:	Depute Chief Executive (Resources & People Services)
SUBJECT:	Treasury Management Strategy 2016/17 to 2018/19

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1 PURPOSE

1.1 To seek the approval of the Council of the Treasury Management and Investment Strategies for 2016/17 to 2018/19.

2 RECOMMENDATIONS

2.1 The Council is recommended to :

i. Note the Treasury Management Strategy referenced within sections 3.4–3.18.

ii. Note the Investment Strategy referenced in sections 3.19–3.20.

iii. Approve Authorised Limits for external debt as detailed in section 3.13.

iv. Approve Operational Boundaries for external debt as detailed in section 3.15.

v. Approve the delegation of authority to the Head of Council Resources to effect movement between external borrowing and other long-term liabilities as detailed in section 3.16.

vi. Approve the detailed Treasury Management Strategy Statement which has been submitted to the Members Library (Ref: 32/16, February 2016 Bulletin).

3 BACKGROUND

3.1 It is a statutory requirement under Section 93 of the Local Government Finance Act 1992, that the Council produces a balanced budget. In particular, a local authority must calculate its budget for each financial year to include the revenue costs that flow from capital financing decisions. This, therefore, means that increases in capital expenditure must be limited to a level whereby any increases in charges to revenue arising from:

- Increases in interest charges caused by increased borrowing to finance additional capital expenditure, and
- Any additional running costs from new capital projects

are limited to a level that is affordable and within the projected income of the Council for the foreseeable future.

3.2 The Treasury Management Code of Practice, updated by CIPFA in 2011, requires the Council to approve a Treasury Management Strategy and an Investment Strategy in advance of each financial year:

3.3 A detailed document more fully covering both the Treasury Management and Investment strategies for 2016/17 to 2018/19 has been placed in the Members' Library. This report outlines the key points from those strategies. The figures used are based on those reflected within setting the Council Tax, HRA rents and supporting budgets on 9 February 2016.

Treasury Management Strategy

3.4 Actual capital expenditure incurred in 2014/15 and the estimates of total gross capital expenditure to be incurred for 2015/16 and future years are detailed below in Table 1:

Table 1: Capital Expenditure					
	2014/15 £'000 actual	2015/16 £'000 outturn	2016/17 £'000 estimate	2017/18 £'000 estimate	2018/19 £'000 estimate
General Services	19,781	32,436	23,555	44,179	32,915
HRA	20,798	25,450	22,509	25,933	23,845
TOTAL	**40,579**	**57,886**	**46,064**	**70,112**	**56,760**

3.5 Not all of this spending will be funded by borrowing. The table below details the actual and planned capital expenditure over the period.

Table 2: Net Financing Need for the Year					
	2014/15 £'000 actual	2015/16 £'000 outturn	2016/17 £'000 estimate	2017/18 £'000 estimate	2018/19 £'000 estimate
General Services Gross Capital Spend	19,781	32,436	23,555	44,179	32,915
HRA Gross Capital Spend	20,798	25,450	22,509	25,933	23,845
Sub-total	**40,579**	**57,886**	**46,064**	**70,112**	**56,760**
Financed by;					
Capital grants	(18,611)	(15,401)	(10,152)	(12,783)	(12,687)
Capital receipts/contributions	(4,878)	(6,957)	(8,244)	(21,067)	(10,000)
Capital Reserves	-	-	-	-	-
Revenue Contributions	(1,966)	(1,825)	(4,059)	(717)	(1,226)
Sub-total	**(25,455)**	**(24,183)**	**(22,455)**	**(34,567)**	**(23,913)**
Net Financing Need for the Year	**15,124**	**33,703**	**23,610**	**35,546**	**32,847**

3.6 Estimates of the ratio of financing costs to net revenue stream for the current and future years, and the actual figures for 2014/15 are:

Table 3: Ratio of financing costs to revenue stream					
	2014/15 % actual	2015/16 % outturn	2016/17 % estimate	2017/18 % estimate	2018/19 % estimate
General Services	8.44%	8.09%	8.56%	8.83%	9.20%
HRA	30.42%	33.46%	36.52%	37.31%	39.54%

3.7 The gradual increase in the General Services ratio largely reflects the standstill in corporate income against a background of continuing capital spend although it is now likely that capital investment plans will increase to support the infrastructure requirements associated with demographic growth. The increase in the HRA ratio reflects the large planned investment in new affordable housing, which is mainly financed through borrowing. This borrowing has to be repaid with interest and this leads to increased financing costs.

3.8 The Capital Financing Requirement (CFR) measures the Council's underlying need to borrow for a capital purpose. The Council does not associate borrowing with particular items or types of expenditure. The authority has an integrated treasury management strategy and has adopted the CIPFA Code of Treasury Management in the Public Services. The Council has at any point in time a number of cash flows both positive and negative. In day-to-day cash management, no distinction is made between revenue cash and capital cash. External borrowing arises as a consequence of all the financial transactions of the Council and not simply those arising from capital spending. However, other than to manage short-term cash flows, the Council is not allowed to borrow for revenue purposes.

3.9 Estimates of the end of year capital financing requirement (CFR) for the Council for the current and future years, and the actual CFR at 31 March 2015 are detailed in Table 4 below:

Table 4: Capital Financing Requirement (CFR)

	2014/15 £'000 actual	2015/16 £'000 outturn	2016/17 £'000 estimate	2017/18 £'000 estimate	2018/19 £'000 estimate
Total CFR at start of year	365,802	368,195	388,957	398,508	419,417
Movement in CFR	2,393	20,762	9,551	20,909	16,994
Total CFR at end of the year	**368,195**	**388,957**	**398,508**	**419,417**	**436,411**
Movement in CFR represented by					
Net Financing Need for the year (above)	15,124	33,703	23,610	35,545	32,846
Less: Scheduled Debt Amortisation	(12,731)	(12,941)	(14,059)	(14,636)	(15,852)
Movement in CFR	**2,393**	**20,762**	**9,551**	**20,909**	**16,994**

3.10 The importance of the CFR lies in the way it measures the need to borrow for a capital purpose excluding the effect of revenue cash flows.

3.11 The key indicator of prudence is that external borrowing should not exceed the CFR for the preceding year plus additional CFR in the current and two following years. At the close of the 2014/15 financial year, the Council was well within this indicator, as the relevant CFR was £368.195 million and external borrowing was £334.930 million.

3.12 The Council's treasury portfolio position at 31 March 2015, with forward projections are summarised in Table 5 below. The table shows the actual external debt (the treasury management operations) against the underlying capital borrowing need (the Capital Financing Requirement – CFR) highlighting any over or under borrowing.

Table 5: Actual Debt and the Capital Financing Requirement (CFR)					
	2014/15 £'000 actual	**2015/16 £'000 outturn**	**2016/17 £'000 estimate**	**2017/18 £'000 estimate**	**2018/19 £'000 estimate**
Total External debt at start of year	339,286	334,930	361,309	379,297	409,220
Expected/Actual change in debt	(4,356)	26,379	17,988	29,923	17,886
Actual gross debt at 31 March	**334,930**	**361,309**	**379,297**	**409,220**	**427,106**
The Capital Financing Requirement	**368,195**	**388,957**	**398,508**	**419,417**	**436,411**
(Under)/Over borrowing	**(33,265)**	**(27,648)**	**(19,211)**	**(10,197)**	**(9,305)**

3.13 The Council is recommended to approve the following Authorised Limits for its gross external debt for the next three years. These limits separately identify borrowing from other long-term liabilities such as finance leases.

Table 6: Authorised Limit for External Debt				
	2015/16 £'000 estimate	**2016/17 £'000 estimate**	**2017/18 £'000 estimate**	**2018/19 £'000 estimate**
Borrowing	409,000	419,000	439,000	457,000
Other long term liabilities	52,000	51,000	50,000	48,000
Total	**461,000**	**470,000**	**489,000**	**505,000**

3.14 These authorised limits are consistent with the Council's current commitments, existing plans and the budget proposals for capital expenditure and financing, and with the approved treasury management policy. The limits are based on the estimate of the most likely, prudent but not worst-case scenario with, in addition, sufficient headroom over and above this to allow for the operational management of unusual cash flows, such as debt restructuring.

3.15 The Council is also asked to approve in Table 7 the operational boundaries for gross external debt. This is the limit beyond which external debt is not normally expected to exceed and is based on the authorised limits but excluding headroom.

Table 7: Operational Boundary for External Debt				
	2015/16 £'000 estimate	2016/17 £'000 estimate	2017/18 £'000 estimate	2018/19 £'000 estimate
Borrowing	388,957	398,508	419,417	436,411
Other long term liabilities	42,490	41,306	39,712	38,232
Total	**431,447**	**439,814**	**459,129**	**474,643**

3.16 The Council has delegated authority to the Head of Council Resources to effect movement between borrowing and long-term liabilities within the total authorised limits and operational boundaries approved. Any such movement would be reported to Cabinet via the Members' Library as part of Treasury Management update reports.

3.17 Within the limits set by the indicators above, the Council will make capital investment decisions in accordance with the following fundamental principles of the Prudential Code:

- Service objectives, e.g. achieving the Council Plan objectives
- Stewardship of assets, e.g. asset management planning
- Affordability, e.g. implications for Council Tax
- Value for money, e.g. option appraisal
- Prudence and sustainability, e.g. implications for external borrowing
- Practicality, e.g. is the investment proposal practical given other competing pressures on the service involved

3.18 A key measure of affordability is the incremental impact of capital investment decisions on the Council Tax and Council House rents. The impacts of the expenditure plans are:

Table 8: Incremental impact of capital investment decisions			
	2016/17 £'000 estimate	2017/18 £'000 estimate	2018/19 £'000 estimate
Increase in Council Tax (band D) per annum	£15.69	£17.57	£23.36
Increase in average housing rent per week	£2.51	£1.82	£2.89

Investment Strategy

3.19 The Council's Investment Strategy for 2016/19 has been prepared in accordance with the Local Government Investments (Scotland) Regulations 2010 and the CIPFA Treasury Management Code.

3.20 The Investment Strategy details the approach which the Council will take to minimise the risk to investments and lists the investments which the Council will be permitted to use.

3.21 Common Good and Charitable Trust funds are managed on behalf of the Council by an external investment management firm. The strategy details the Council's policy on the investment of these funds.

3.22 The indicator below sets a limit on the total level of investments held for longer than 364 days.

Maximum principal sums invested > 364 days			
£m	**2016/17**	**2017/18**	**2018/19**
Principal sums invested > 364 days	£m 30	£m 30	£m 30

4 POLICY IMPLICATIONS

4.1 Implementation of Council policy will require capital expenditure. The policy effect of a proposed capital expenditure will be assessed as part of the project appraisal.

4.2 The limited resources available form an important constraint on the development of policy, which requires to be managed through the development of a sustainable corporate plan associated with a corporate asset management plan.

5 EQUALITIES IMPACT ASSESSMENT

5.1 This report is not applicable to the wellbeing of equalities groups and an Equalities Impact Assessment is not required.

6 RESOURCE IMPLICATIONS

6.1 Financial – these strategies are interwoven with the revenue and capital budgets. The expenditure and debt limits are implicit within the revenue budgets approved by the Council on 9 February 2016.

6.2 Personnel - none directly from this report although there may be implications arising from capital investment decisions.

6.3 Other – capital investment choices made have a major impact on the property, equipment and IT resources available for the delivery of services.

7 BACKGROUND PAPERS

7.1 CIPFA (2011) – “Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes”

7.2 CIPFA (2011) – “The Prudential Code for Capital Finance in Local Authorities”

7.3 The Local Government (Scotland) Regulations 2010

7.4 Capital Investment & Treasury Management Strategy 2016/17 to 2018/19 (lodged in Members Library Service)

7.5 Council Meeting of 9 February 2016 – all papers

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