

**REPORT TO:** East Lothian Council

**MEETING DATE:** 3 March 2020

**BY:** Depute Chief Executive (Resources & People Services)

**SUBJECT:** Treasury Management Strategy 2020-21 to 2024-25

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## **1 PURPOSE**

1.1 To seek the approval of the Council of the Treasury Management and Investment Strategies for 2020-21 to 2024-25.

## **2 RECOMMENDATIONS**

2.1 The Council is recommended to :

- i. Note that the General Services Capital investment plans for 2020-2025 are subject to consideration and approval by the previous budget item considered Council on 3 March. Should there be any change to these approved figures, there will be a need to update the specific Boundaries and Limits set out below.
- ii. Approve the Treasury Management Strategy referenced within sections 3.5-3.18.
- iii. Approve the Investment Strategy referenced in sections 3.19-3.21.
- iv. Approve the repayment of loans fund advances using the methodology detailed in section 3.6.
- v. Approve the Operational Boundaries for external debt as detailed in section 3.14.
- vi. Approve the Authorised Limits for external debt as detailed in section 3.15.
- vii. 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 3.18.

- viii. Note the detailed Treasury Management Strategy Statement which has been submitted to the Members Library (Members' Library Service Ref: 25/20, February 2020 Bulletin).

### **3 BACKGROUND**

- 3.1 Each year a local authority must calculate 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 the elements reflected below are limited to a level that is affordable and within the projected income of the Council for the foreseeable future. These elements include:
- Increases in interest charges caused by increased borrowing to finance additional capital expenditure, and
  - Any additional running costs from new capital projects
- 3.2 The Treasury Management Code of Practice, requires the Council to approve a Treasury Management Strategy and an Investment Strategy in advance of each financial year.
- 3.3 As from 2019-20, all local authorities were required to prepare a Capital Strategy report, which is intended to firmly place decisions around borrowing in the context of the overall longer-term financial position of the authority and to provide improved links between the revenue and capital budgets. The Capital Strategy was approved by Council on 17 December 2019.
- 3.4 The full Treasury Management and Investment Strategy for the period 2020-21 to 2024-25 has been lodged in the Members Library (Members' Library Service Ref: 25/20, February 2020 Bulletin). This report outlines the key points from those strategies. The figures used are based on those reflected within setting the HRA budget approved by Council on 25 February 2020, and in the draft General Services supporting budget amendment to be considered by Council at this meeting.

### **TREASURY MANAGEMENT STRATEGY**

- 3.5 The table below provides details setting out the capital investment plans for 2020– 2025, in line with the approved HRA capital budget and draft General Services capital budget. As a reminder, the actual capital expenditure incurred in 2018-19 and provisional estimates of total gross capital expenditure plans and how these are to be financed for 2019-20 are also detailed below. Not all of this spending will be funded by borrowing, with any shortfall of resources results in a borrowing need.

**Table 1**

Capital expenditure £'000	2018/19 Actual	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
General Services	37,519	34,572	96,199	81,480	76,824	72,038	28,966
HRA	22,410	33,429	33,540	37,248	36,747	32,752	33,801
<b>Total</b>	<b>59,929</b>	<b>68,001</b>	<b>129,739</b>	<b>118,728</b>	<b>113,571</b>	<b>104,790</b>	<b>62,767</b>

Financing of capital expenditure £'000	2018/19 Actual	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
<b>General Services</b>							
Capital receipts	(3,404)	(9,051)	(28,174)	(16,110)	(21,137)	(23,698)	(9,037)
Capital grants	(12,615)	(11,797)	(19,293)	(17,558)	(24,888)	(30,883)	(14,091)
CFCR	(224)						
<b>General Services Total</b>	<b>(16,243)</b>	<b>(20,848)</b>	<b>(47,468)</b>	<b>(33,668)</b>	<b>(46,025)</b>	<b>(54,581)</b>	<b>(23,128)</b>
<b>HRA</b>							
Capital receipts	(352)	(2,347)	(3,726)				
Capital grants	(7,374)	(7,542)	(3,991)	(4,696)	(4,696)	(4,696)	(2,696)
CFCR	(3,200)	(6,700)	(3,500)	(3,700)	(4,200)	(3,900)	(4,600)
<b>HRA Total</b>	<b>(10,926)</b>	<b>(16,589)</b>	<b>(11,217)</b>	<b>(8,396)</b>	<b>(8,896)</b>	<b>(8,596)</b>	<b>(7,296)</b>
<b>Net financing need for the year</b>	<b>32,760</b>	<b>30,565</b>	<b>71,055</b>	<b>76,664</b>	<b>58,651</b>	<b>41,613</b>	<b>32,342</b>

3.6 The net financing need for the year is financed by Loans Fund advances. The operation of the loans fund is regulated by statute, with updated regulations: (The Local Authority (Capital Finance and Accounting) (Scotland) Regulations 2016 (the 2016 Regulations)) coming into force on 1 April 2016. The Council will apply the following strategy for loans fund advances:

- Any income/receipts applied in year are where possible aligned to shorter life assets or where appropriate to reduce loans fund advances. Any loans fund advances in year is matched to assets with longer economic lives.

#### **General Services**

- All capital expenditure incurred from 2001 has been reflected within the loans fund on an individual asset basis, rather than an overall pooled approach.
- All capital expenditure incurred between 2001 and 2016 has been aligned to the asset life which was given at the time capital expenditure had been incurred (i.e. in line with depreciation

charged through the Council's statutory accounts). These have been aligned to the asset lives provided for the rolling valuation programme as required by the Council's statutory accounting process.

- From 2016, in line with the statutory guidance, all asset lives have been reviewed and aligned to the estimated economic life of the asset.

## **HRA**

- All capital expenditure incurred from 2001 has been reflected within the loans fund and categorised as new council housing, modernisation expenditure on existing properties and open market acquisitions.
- All capital expenditure incurred between 2001 and 2012-13 has been aligned to the asset life which was given at the time capital expenditure has been incurred (i.e in line with depreciation charged through the Council's statutory accounts).
- From 2013-14, there was a change to the approach required to value Council dwellings through the statutory accounts. As a result, all of the Council dwellings have been depreciated using a pooled approach and given the same life, regardless of each asset's age.
- It is not considered prudent and commensurate with the economic benefit of the asset life to match loans fund advances in such a way. As such, from 2013-14, all of the asset lives have been reviewed, and all HRA loans fund advances are now aligned to the estimated economic life of the asset.

3.7 For illustrative purposes, assuming projected expenditure in line with approved plans and further extended to a 10 year period, the General Services and HRA expected loans fund balances are shown below in the tables 2 and 3 below.

**Table 2 - General Services**

<b>General Services £'000</b>	<b>Opening Balance</b>	<b>Advances</b>	<b>Repayments</b>	<b>Closing Balance</b>
Year 1	230,788	48,732	7,299	272,221
Year 2-5	272,221	101,906	21,020	353,107
Year 6-10	353,107	22,350	27,358	348,099
Year 11-15	348,099		34,809	313,290
Year 15-20	313,290		40,068	273,222
Year 21-30	273,222		74,976	198,246
Year 31-40	198,246		48,263	149,983
Year 41-50	149,983		50,690	99,293
Year 51-60	99,293		69,435	29,858
Year 61-70	29,858		29,858	0

**Table 3 - HRA**

<b>HRA £'000</b>	<b>Opening Balance</b>	<b>Advances</b>	<b>Repayments</b>	<b>Closing Balance</b>
Year 1	200,566	22,323	4,054	218,835
Year 2-5	218,835	107,363	21,530	304,668
Year 6-10	304,668	129,762	36,970	397,460
Year 11-15	397,460		43,123	354,337
Year 16-20	354,337		43,510	310,827
Year 21-30	310,827		71,946	238,881
Year 31-40	238,881		63,231	175,650
Year 41-50	175,650		64,433	111,217
Year 51-60	111,217		75,270	35,947
Year 61-70	35,947		35,947	0

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. 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 Table 4 below sets of the capital financing requirement (CFR) and the movement in CFR for the Council across the 5 year strategy period from 2020-2025. The table also includes a reminder of the actual CFR in 2018-19 and current projections for 2019-20.

**Table 4 - CFR**

£'000	2018/19 Actual	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
<b>Capital Financing Requirement (including PPP &amp; Finance Leases)</b>							
CFR - General Services	264,048	267,686	307,574	347,703	371,753	382,752	382,207
CFR – HRA	187,528	200,567	218,836	243,023	265,699	284,171	304,670
<b>Total CFR</b>	<b>451,576</b>	<b>468,253</b>	<b>526,410</b>	<b>590,726</b>	<b>637,452</b>	<b>666,923</b>	<b>686,877</b>
<b>Movement in CFR</b>	<b>20,058</b>	<b>16,677</b>	<b>58,157</b>	<b>64,316</b>	<b>46,726</b>	<b>29,471</b>	<b>19,954</b>
<b>Movement in CFR represented by</b>							
Net financing need for the year	32,759	30,565	71,055	76,664	58,651	41,613	32,342
GS -Less loan fund repayments and other financing movements	(9,869)	(10,086)	(8,844)	(7,683)	(6,749)	(6,458)	(6,382)
HRA - Less loan fund repayments and other financing movements	(2,832)	(3,802)	(4,054)	(4,665)	(5,186)	(5,684)	(6,006)
<b>Movement in CFR</b>	<b>20,058</b>	<b>16,677</b>	<b>58,157</b>	<b>64,316</b>	<b>46,726</b>	<b>29,471</b>	<b>19,954</b>

3.10 Capital investment decisions should be made 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 and Rent levels
- 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

3.11 Prudential indicators are required to assess the affordability of the capital investment plans. These provide an indication of the impact of the capital investment plans on the councils overall finances. Some of these are set out in more detail below.

- One of the main prudential indicators is the ratio of financing costs to net revenue streams which identifies the trend in the cost of capital against income. Actual 2018-19 figures, and estimates of the ratio of financing costs to net revenue stream for the current and future years are set out in the table 5 below.

**Table 5 – Ratio of financing costs to net revenue streams**

£'000	2018/19 Actual	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
GS Revenue Stream	230,577	238,805	252,992	257,880	263,380	269,312	275,711
GS Financing Costs	16,000	16,000	15,250	15,250	15,500	16,000	16,000
General Services	6.94%	6.70%	6.03%	5.91%	5.89%	5.94%	5.80%
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HRA Revenue Stream	30,159	31,862	34,201	36,269	38,625	40,759	42,746
HRA Financing Costs *	9,000	10,190	10,915	12,082	13,403	14,663	15,524
HRA	29.84%	31.98%	31.92%	33.31%	34.71%	35.97%	36.32%

\* Note these have changed slightly from the approved HRA budget due to changes to the General Services capital budget

- The relative stability in the General Services ratio reflects the impact of the loans fund review carried out in 2019 although this is against a background of increased capital investment plans to support the infrastructure requirements associated with future growth plans and will rise in future. The increase in the HRA ratio reflects the large planned investment in new council housing programme, which is mainly financed through borrowing. This borrowing has to be repaid with interest and this leads to increased financing costs.
- Furthermore, the incremental impact of capital investment decisions on council tax and housing rent levels are set out in Tables 6 and 7 below.

**Table 6 - Impact on Council Tax**

	2018/19 Actual	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
General Services Debt £'000	225,804	230,789	272,222	313,928	339,544	352,070	353,108
Band D Equivalents	48,047	49,416	50,516	51,616	52,716	53,816	54,916
Debt per Band D Equivalent £	£4,670	£4,670	£5,389	£6,082	£6,441	£6,542	£6,430

**Table 7 - Impact on Rent**

	2018/19 Actual	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
HRA debt £'000	187,528	200,567	218,836	243,022	265,699	284,170	304,669
Number of HRA dwellings £m	8,740	8,850	8,941	9,116	9,207	9,388	9,546
Debt per dwelling £	£21,456	£22,663	£24,476	£26,659	£28,858	£30,270	£31,915

3.12 The Council's treasury portfolio position at 31 March 2019, with forward projections are summarised in Table 8 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 8 – Treasury Portfolio**

£'000	2018/19 Actual	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
<b>External Debt</b>							
Debt at 1 April	358,025	360,440	373,710	430,487	487,136	532,522	562,889
Expected change in Debt	2,415	13,270	56,776	56,649	45,416	30,337	4,186
Other long-term liabilities (OLTL)	39,723	36,898	36,897	35,352	33,775	32,209	30,682
Expected change in OLTL	(1,479)	(1,347)	(1,545)	(1,577)	(1,566)	(1,473)	(1,583)
Actual gross debt at 31 March	<b>398,684</b>	<b>409,262</b>	<b>465,839</b>	<b>520,911</b>	<b>564,761</b>	<b>593,626</b>	<b>596,174</b>
The Capital Financing Requirement	<b>451,575</b>	<b>466,906</b>	<b>526,409</b>	<b>590,726</b>	<b>637,452</b>	<b>666,976</b>	<b>686,877</b>
Under / (over) borrowing	<b>52,891</b>	<b>57,644</b>	<b>60,570</b>	<b>69,815</b>	<b>72,691</b>	<b>73,350</b>	<b>90,703</b>



3.13 The key treasury management indicator of prudence is that external borrowing should not exceed the CFR for the preceding year (2018/19) plus additional CFR in the current (2019/20) and two following years (2020/21 and 2021/22). This year is projected to be within this indicator - External Debt £409m and CFR £590m (£451m+£17m+£58m+£64m). At the close of the 2018/19 financial year, the Council was well within this indicator, as the CFR for the actual year was £451 million and external borrowing was £398 million.

### Boundaries for Debt

3.14 In line with the requirements, the Council is asked to approve limits beyond which external debt is not normally expected to exceed in the proceeding 5 years of the strategy. The operational boundaries for gross external debt are set out in Table 9 below.

**Table 9 – Operational Boundary**

Operational boundary £'000	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
Debt	431,355	491,056	556,950	605,243	636,240	657,777
Other long term liabilities	36,897	35,352	33,775	32,209	30,682	29,099
<b>Total</b>	<b>468,252</b>	<b>526,409</b>	<b>590,725</b>	<b>637,452</b>	<b>666,922</b>	<b>686,876</b>

3.15 Furthermore, the Council must set maximum levels of borrowing by way setting Authorised Limits for its gross external debt for the strategy period. Table 10 below sets out the maximum authorised limits for the next five years. These limits separately identify borrowing from other long-term liabilities such as finance leases.

**Table 10 – Authorised Limits**

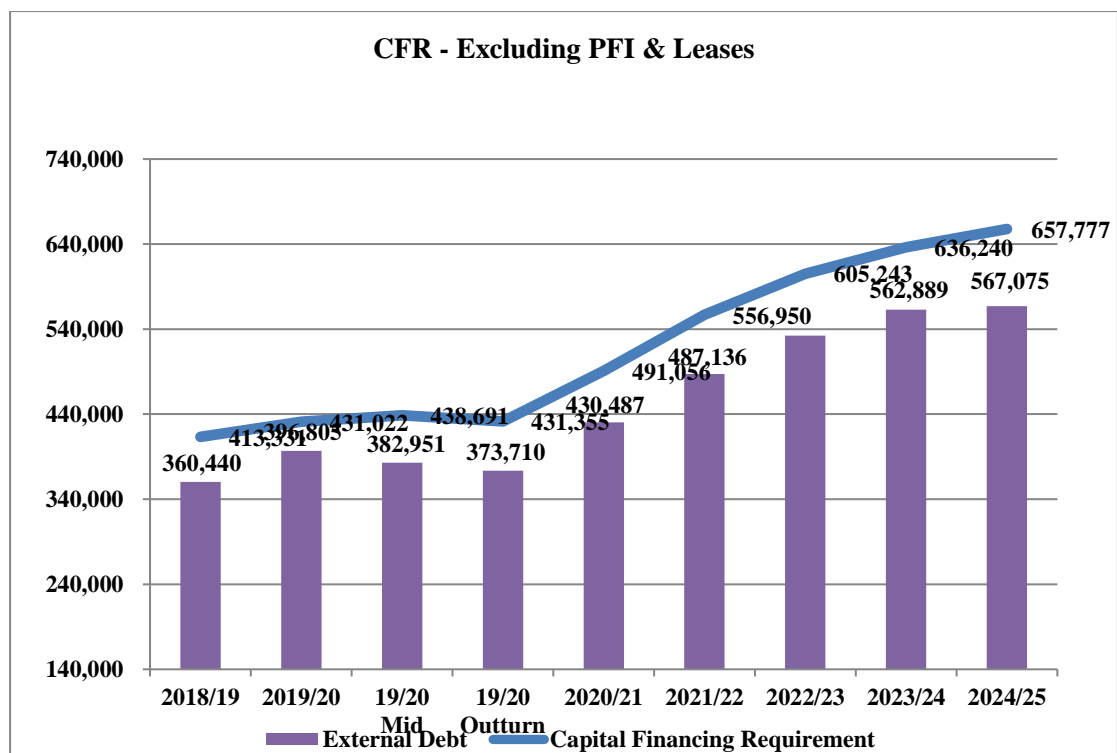
Authorised limit £'000	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate
Debt	481,000	550,000	600,000	660,000	700,000	689,000
Other long term liabilities	37,000	36,000	34,000	33,000	31,000	30,000
<b>Total</b>	<b>518,000</b>	<b>586,000</b>	<b>634,000</b>	<b>693,000</b>	<b>731,000</b>	<b>719,000</b>

3.16 These authorised limits are consistent with the Council's current commitments, and approved budget for capital expenditure and financing. The limits are based on the estimate of the most likely, but prudent but not worst-case scenario with, and includes sufficient headroom over and above this to allow for the operational management of unusual cash flows, such as debt restructuring, or timing issues with expected capital income.

3.17 A summary of the CFR against the planned external debt is set out in Table 11 and the graph shown below.

**Table 11**

	2018/19	2019/20	19/20 Mid	19/20 Outturn	2020/21	2021/22	2022/23	2023/24	2024/25
Authorised Limit	441,000	481,000	481,000	481,000	550,000	600,000	660,000	700,000	689,000
Operational Boundary	413,331	431,022	431,022	431,022	491,056	556,950	605,243	636,240	657,777
Capital Financing Requirement	413,331	431,022	438,691	431,355	491,056	556,950	605,243	636,240	657,777
External Debt	360,440	396,805	382,951	373,710	430,487	487,136	532,552	562,889	567,075



3.18 In line with the approved standing orders, 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 Council / Cabinet via the Members Library and as part of Treasury Management update reports.

## Investment Strategy

- 3.19 The Council's Investment strategy is developed in line with Local Government Investments (Scotland) Regulations 2010, (and accompanying Finance Circular 5/2010), and the CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2017, ("the CIPFA TM 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. The regulations and guidance place a high priority on the management of risk. **The Council's investment priorities will be security first, liquidity second and then return.**
- 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. The indicator below sets a limit on the total level of investments held for longer than 365 days.

Maximum principal sums invested > 364 & 365 days			
£m	2020/21	2021/22	2022/23
Principal sums invested > 365 days	£m 10	£m 10	£m 10

## 4 POLICY IMPLICATIONS

- 4.1 There are no direct policy implications associated with this report although clearly, the report provides a strategic context and direction within which all future financial plans should be considered. On-going monitoring and reporting of the Council's financial performance is a key part of the approved Treasury Management Strategy.

## 5 INTEGRATED IMPACT ASSESSMENT

- 5.1 The subject of this report has been considered and given there is no direct change in policy direction, there is no immediate requirement to undertake any further impact assessment.

## 6 RESOURCE IMPLICATIONS

- 6.1 Financial – these strategies are consistent with the HRA budget approved on 25 February and the draft General Services budget considered by Council on 3 March 2020.
- 6.2 Personnel - none
- 6.3 Other – none

## **7 BACKGROUND PAPERS**

- 7.1 CIPFA (2017) – “Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes”
- 7.2 CIPFA (2017) – “The Prudential Code for Capital Finance in Local Authorities”
- 7.3 The Local Government (Scotland) Regulations 2010
- 7.4 The Local Authority (Capital Financing and Accounting) (Scotland) Regulations 2016
- 7.5 Treasury Management Strategy Statement and Annual Investment Strategy 2020 - 2025 (Members’ Library Service Ref: 25/20, February 2020 Bulletin)
- 7.6 Council 25 February 2020 – Rent Proposals 2020/21 – 2024/25 – Amendment Submitted by the Administration
- 7.7 Council 3 March 2020 – Budget Proposals on General Services – Amendment Submitted by the Administration

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