

**REPORT TO:** East Lothian Council

**MEETING DATE:** 2 March 2021

**BY:** Executive Director for Council Resources

**SUBJECT:** Treasury Management Strategy 2021-22 to 2025-26

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## **1 PURPOSE**

- 1.1 To seek the approval of the Council of the Treasury Management and Investment Strategies for 2021-22 to 2025-26.

## **2 RECOMMENDATIONS**

2.1 The Council is recommended to :

- i. Note that the General Services Capital investment plans for 2021-2026 are subject to consideration and approval by the previous budget item considered at Council on 2 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 Chief Financial Officer 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 lodged in the Members' Library Service Ref 29/21 (Feb 2021 Bulletin). [February 2021 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 principal and 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 This is also supported by the Financial and Capital Strategy, which was approved by Council on 15 December 2020, and 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.
- 3.4 The full Treasury Management and Investment Strategy for the period 2021-22 to 2025-26 has been lodged in the Members' Library Service Ref 29/21 (Feb 2021 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 23 February 2021, 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 2021– 2026, in line with the approved HRA capital budget and draft General Service's capital budget. As a reminder, the actual capital expenditure incurred in 2019-20 and provisional estimates of total gross capital expenditure plans and how these are to be financed for 2020-21 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	2019/20 Actual	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate	5 Year Total Estimate
General Services	42,261	44,629	91,506	77,439	97,699	57,300	42,844	366,788
HRA	29,929	21,371	29,676	45,340	37,468	36,877	35,698	185,059
<b>Total</b>	<b>72,190</b>	<b>66,000</b>	<b>121,182</b>	<b>122,779</b>	<b>135,167</b>	<b>94,177</b>	<b>78,542</b>	<b>551,847</b>

Financing of capital expenditure £'000	2019/20 Actual	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate	5 Year Total Estimate
<b>General Services</b>								
Capital receipts	(26,105)	(11,509)	(12,358)	(10,026)	(14,871)	(19,665)	(11,737)	(68,657)
Capital grants	(10,691)	(17,945)	(28,484)	(27,455)	(49,698)	(26,834)	(17,038)	(149,509)
CFCR	(732)							
<b>General Services Total</b>	<b>(37,528)</b>	<b>(29,454)</b>	<b>(40,842)</b>	<b>(37,481)</b>	<b>(64,569)</b>	<b>(46,499)</b>	<b>(28,775)</b>	<b>(218,166)</b>
<b>HRA</b>								
Capital receipts	(1,293)							
Capital grants	(6,141)	(5,046)	(4,196)	(4,196)	(4,196)	(4,196)	(4,196)	(20,980)
CFCR	(7,700)	(1,862)	(2,500)	(3,000)	(3,700)	(5,500)	(7,000)	(21,700)
<b>HRA Total</b>	<b>(15,134)</b>	<b>(6,908)</b>	<b>(6,696)</b>	<b>(7,196)</b>	<b>(7,896)</b>	<b>(9,696)</b>	<b>(11,196)</b>	<b>(42,680)</b>
<b>Net financing need for the year</b>	<b>19,528</b>	<b>29,638</b>	<b>73,644</b>	<b>78,102</b>	<b>62,702</b>	<b>37,982</b>	<b>38,571</b>	<b>291,001</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: (The Local Authority (Capital Finance and Accounting) (Scotland) Regulations 2016 (the 2016 Regulations)) which came into force on 1 April 2016. The Council will apply the following strategy for loans fund advances, and this remains consistent with the Loans Fund Review principles previously approved by Council in June 2019:

- 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. This table assumes the use of fiscal flexibilities for loans fund advance repayments for General Services in Year 1.

**Table 2 - General Services**

General Services £'000	Opening Balance	Advances	Repayments	Closing Balance
Year 1	229,778	50,663	236	280,205
Year 2-5	280,205	97,958	29,599	348,564
Year 6-10	348,564	45,605	31,257	362,912
Year 11-15	362,912		39,136	323,776
Year 15-20	323,776		48,625	275,153
Year 21-30	275,153		76,692	198,460
Year 31-40	198,460		46,998	151,462
Year 41-50	151,462		51,079	100,383
Year 51-60	100,383		68,844	31,540
Year 61-70	31,540		31,540	0

**Table 3 - HRA**

HRA £'000	Opening Balance	Advances	Repayments	Closing Balance
Year 1	208,930	22,980	4,480	227,429
Year 2-5	227,429	119,398	23,751	323,076
Year 6-10	323,076	133,536	39,952	416,660
Year 11-15	416,660		46,408	370,252
Year 16-20	370,252		46,509	323,743
Year 21-30	323,743		75,705	248,038
Year 31-40	248,038		66,416	181,622
Year 41-50	181,622		67,007	114,615
Year 51-60	114,615		76,778	37,837
Year 61-70	37,837		37,837	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 2021-2026. The table also includes a reminder of the actual CFR in 2019-20 and current projections for 2020-21.

**Table 4 - CFR**

£'000	2019/20 Actual	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate
<b>Capital Financing Requirement (including PPP &amp; Finance Leases)</b>							
CFR - General Services	258,767	265,131	313,981	344,884	368,904	370,726	375,805
CFR – HRA	198,521	208,930	227,430	260,449	284,225	305,197	323,078
<b>Total CFR</b>	<b>457,288</b>	<b>474,061</b>	<b>541,411</b>	<b>605,333</b>	<b>653,129</b>	<b>675,923</b>	<b>698,883</b>
<b>Movement in CFR</b>	<b>5,712</b>	<b>16,773</b>	<b>67,350</b>	<b>63,922</b>	<b>47,796</b>	<b>22,794</b>	<b>22,960</b>
<b>Movement in CFR represented by</b>							
Net financing need for the year	19,528	29,638	73,644	78,102	62,702	37,982	38,571
GS -Less loan fund repayments and other financing movements	(10,014)	(8,811)	(1,814)	(9,055)	(9,110)	(8,979)	(8,990)
HRA - Less loan fund repayments and other financing movements	(3,802)	(4,054)	(4,480)	(5,125)	(5,796)	(6,209)	(6,621)
<b>Movement in CFR</b>	<b>5,712</b>	<b>16,773</b>	<b>67,350</b>	<b>63,922</b>	<b>47,796</b>	<b>22,794</b>	<b>22,960</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 2019-20 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	2019/20 Actual	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate
GS Revenue Stream	244,262	249,526	260,511	267,248	274,797	278,490	282,247
GS Financing Costs	16,000	14,250	7,577	15,500	16,000	15,839	15,847
General Services	6.55%	5.71%	2.91%	5.80%	5.82%	5.69%	5.61%
<b>HRA</b>							
HRA Revenue Stream	31,638	34,201	34,641	37,051	39,861	42,728	45,702
HRA Financing Costs	10,197	10,572	11,091	11,884	13,042	13,709	14,755
HRA	32.23%	30.91%	32.02%	32.07%	32.72%	32.08%	32.29%

- The reduction in the General Services ratio in 2021-22 directly reflects the impact of the use of fiscal flexibilities in relation to loans fund principal repayments. The relative stability from 2022-23 in the 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 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**

	2019/20 Actual	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate
General Services Debt £'000	221,870	229,778	280,205	312,674	338,222	341,626	348,566
Band D Equivalents	49,069	54,972	55,983	57,471	59,094	60,571	62,086
Debt per Band D Equivalent £	£4,522	£4,180	£5,005	£5,440	£5,723	£5,640	£5,614

**Table 7 - Impact on Rent**

	2019/20 Actual	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate
HRA debt £'000	198,521	208,930	227,430	260,449	284,225	305,197	323,078
Number of HRA dwellings	8,636	8,718	8,938	9,119	9,303	9,437	9,512
Debt per dwelling £	£22,432	£23,965	£25,445	£28,561	£30,552	£32,340	£33,965

3.12 The Council's treasury portfolio position at 31 March 2020, 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	2019/20 Actual	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate
<b>External Debt</b>							
Debt at 1 April	360,440	382,831	398,266	469,365	526,609	578,165	577,199
Expected change in Debt	22,391	15,435	71,099	57,244	51,556	(966)	38,029
Other long-term liabilities (OLTL)	38,244	36,897	35,352	33,775	32,209	30,682	29,099
Expected change in OLTL	(1,347)	(1,545)	(1,577)	(1,566)	(1,527)	(1,583)	(1,860)
Actual gross debt at 31 March	<b>419,728</b>	<b>433,618</b>	<b>503,140</b>	<b>558,818</b>	<b>608,847</b>	<b>606,298</b>	<b>642,467</b>
The Capital Financing Requirement	<b>457,288</b>	<b>474,061</b>	<b>541,411</b>	<b>605,333</b>	<b>653,129</b>	<b>675,923</b>	<b>698,883</b>
Under / (over) borrowing	<b>37,560</b>	<b>40,443</b>	<b>38,271</b>	<b>46,515</b>	<b>44,282</b>	<b>69,625</b>	<b>56,416</b>



3.13 The key treasury management indicator of prudence is that external borrowing should not exceed the CFR for the preceding year (2019/20) plus additional CFR in the current (2020/21) and two following years (2021/22 and 2022/23). This year is projected to be within this indicator - External Debt £434m and CFR £605m (£457m+£17m+£67m+£64m). At the close of the 2019/20 financial year, the Council was well within this indicator, as the CFR for the actual year was £457 million and external borrowing was £419 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	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate
Debt	438,708	507,635	573,123	622,446	646,823	671,643
Other long term liabilities	35,352	33,775	32,209	30,682	29,099	27,240
<b>Total</b>	<b>474,060</b>	<b>541,410</b>	<b>605,332</b>	<b>653,128</b>	<b>675,922</b>	<b>698,883</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**

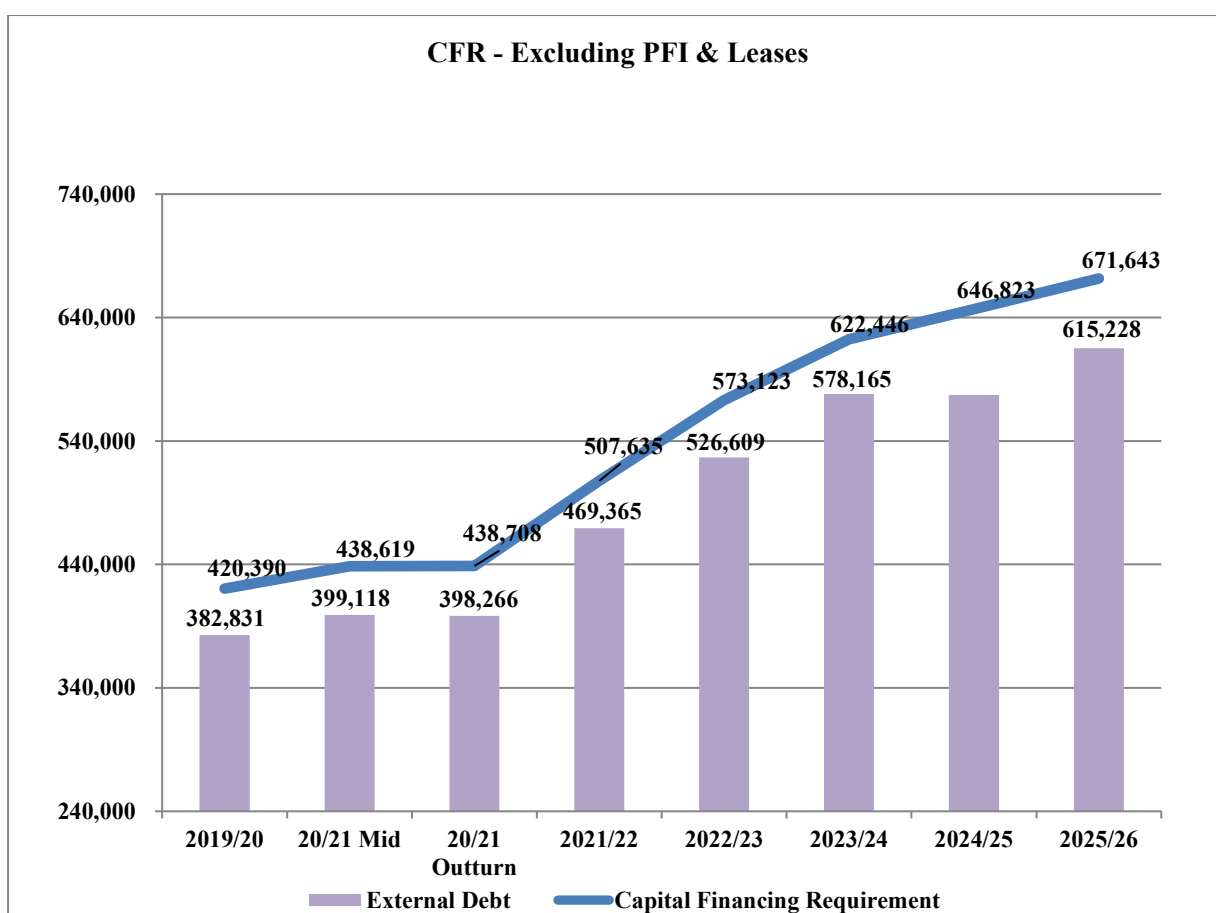
Authorised limit £'000	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate	2024/25 Estimate	2025/26 Estimate
Debt	550,000	556,000	618,000	695,000	704,000	712,000
Other long term liabilities	36,000	34,000	33,000	31,000	30,000	28,000
<b>Total</b>	<b>586,000</b>	<b>590,000</b>	<b>651,000</b>	<b>726,000</b>	<b>734,000</b>	<b>740,000</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 excluding PFI and leases against the planned external debt is set out in Table 11 and the graph shown below.

**Table 11**

	2019/20	2020/21	20/21 Mid	20/21 Outturn	2021/22	2022/23	2023/24	2024/25	2025/26
Authorised Limit	481,000	550,000	550,000	550,000	556,000	618,000	695,000	704,000	712,000
Operational Boundary	420,390	491,056	491,056	491,056	507,635	573,123	622,446	646,823	671,643
Capital Financing Requirement	420,390	491,056	438,619	438,708	507,635	573,123	622,446	646,823	671,643
External Debt	382,831	430,487	399,118	398,266	469,365	526,609	578,165	577,199	615,228



3.18 In line with existing financial regulations, the Council has delegated authority to the Chief Financial Officer 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 Service 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.

Upper limit for principal sums invested for longer than 365 days			
£m	2021/22	2022/23	2023/24
Principal sums invested for longer than 365 days	£10m	£10m	£10m

## 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 23 February and the draft General Service's budget being considered by Council on 2 March 2021.
- 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 Investments (Scotland) Regulations 2010
- 7.4 The Local Authority (Capital Financing and Accounting) (Scotland) Regulations 2016
- 7.5 Financial and Capital Strategy 2021-26 - Council 15 December 2020
- 7.6 Capital Investment & Treasury Management Strategy 2021-22 to 2025-26 which has been lodged in the Members’ Library Service Ref 29/21 (Feb 2021 Bulletin) [February 2021 Bulletin](#)
- 7.7 Council 23 February 2021 – Administration budget papers – HRA

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