

REPORT TO: East Lothian Council

MEETING DATE: 26 February 2019

BY: Depute Chief Executive (Resources & People Services)

SUBJECT: Treasury Management Strategy 2019-20 to 2023-24

1 PURPOSE

- 1.1 To seek the approval of the Council of the Treasury Management and Investment Strategies for 2019-20 to 2023-24.

2 RECOMMENDATIONS

- 2.1 The Council is recommended to :
- i. Approve the Treasury Management Strategy referenced within sections 3.5-3.18.
 - ii. Approve the Investment Strategy referenced in Sections 3.19-3.21.
 - iii. Approve the repayment of loans fund advances by the statutory method before 1 April 2016 and by the asset life method after 1 April 2016 in Section 3.6, and agree that this may need to be reviewed subject to the outcome of the promised legislative changes at a national level.
 - iv. Approve the Operational Boundaries for external debt as detailed in Section 3.14.
 - v. Approve the Authorised Limits for external debt as detailed in Section 3.15.
 - vi. 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.
 - vii. Note the detailed Treasury Management Strategy Statement which has been submitted to the Members Library (Ref: 19/19, February 2019 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 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, updated by CIPFA in 2017, 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 are 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 11 December 2018.
- 3.4 The full Treasury Management and Investment Strategy for the period 2019-20 to 2023-24 has been lodged 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 12 February 2019.

Treasury Management Strategy

- 3.5 The actual capital expenditure incurred in 2017-18 and the estimates of total gross capital expenditure plans and how these are to be financed for 2018-19 and future five years in line with approved capital budgets are detailed below in Table 1 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	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
General Services	29,536	44,361	52,074	74,932	68,374	60,887	56,295
HRA	21,302	22,321	32,890	31,499	35,305	35,291	35,856
Total	50,838	66,682	84,964	106,431	103,679	96,178	92,151

Financing of capital expenditure £'000	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
General Services							
Capital receipts	(13,825)	(9,585)	(27,112)	(26,082)	(18,778)	(28,005)	(19,137)
Capital grants	(11,990)	(11,429)	(9,465)	(12,156)	(13,602)	(11,146)	(11,278)
CFCR	(113)						
General Services Total	(25,928)	(21,014)	(36,577)	(38,238)	(32,380)	(39,151)	(30,415)
HRA							
Capital receipts	(2,111)						
Capital grants	(3,905)	(5,304)	(6,222)	(5,619)	(6,401)	(5,479)	(2,534)
CFCR	(2,500)	(1,700)	(6,700)	(3,350)	(3,200)	(5,400)	(5,400)
HRA Total	(8,516)	(7,004)	(12,922)	(8,969)	(9,601)	(10,879)	(7,934)
Net financing need for the year	16,394	38,664	35,465	59,224	61,698	46,148	53,802

- 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 current regulations state that the statutory method for loans fund advances made after 31 March 2021 is not available. However, as highlighted in the Budget report to Council on 12 February 2019, the Cabinet Secretary for Finance has formally announced his intention to bring forward legislative changes for Council's to vary loans fund advances made prior to 1 April 2016.
- 3.7 The Council will apply the following strategy for loans fund advances, but this may change subject to the outcome of the wider review, detail of which will be reported to Council in due course.
- For loans fund advances made before 1 April 2016, the Council's policy has been to maintain the practice of previous years and apply the **Statutory Method** with all loans fund advances being repaid by the annuity method.
 - For loans fund advances made after 1 April 2016 (with regard to the Local Authority (Capital Finance and Accounting) (Scotland) Regulations 2016), the Council's policy for repayment of loans will be to move to the **Asset Life Method** with all loans fund advances continue to be repaid by the annuity method.
- 3.8 For illustrative purposes, assuming no further advances are made after year 5, the General Services and HRA expected loans fund balances are shown below in the tables 2 and 3 below.

Table 2 - General Services

General Services £'000	Opening Balance	Advances	Repayments	Closing Balance
Year 1	220,643	15,258	12,352	223,548
Year 2-5	223,548	119,258	64,357	278,450
Year 6-10	278,450		79,241	196,143
Year 11-15	196,143		41,434	154,709
Year 15-20	154,709		24,968	129,740
Year 21-30	129,740		22,073	107,667
Year 31-40	107,667		21,784	85,883
Year 41-50	85,883		27,760	58,122
Year 51-60	58,122		40,979	17,144
Year 61-70	17,144		17,144	

Table 3 - HRA

HRA £'000	Opening Balance	Advances	Repayments	Closing Balance
Year 1	191,264	19,968	3,728	207,504
Year 2-5	207,504	100,568	18,202	289,869
Year 6-10	289,869		30,189	259,681
Year 11-15	259,681		36,079	223,602
Year 16-20	223,602		38,446	185,156
Year 21-30	185,156		78,839	106,317
Year 31-40	106,317		36,058	70,259
Year 41-50	70,259		28,223	42,036
Year 51-60	42,036		29,696	12,340
Year 61-70	12,340		12,340	

3.9 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.

3.10 Table 4 below sets of the capital financing requirement (CFR) and the movement in CFR for the Council setting out the 2017-18 actual, forecast 2018-19 position, and the forecast CFR based on approved budget plans from 2019-2024.

Table 4 - CFR

£'000	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
Capital Financing Requirement (including PFI & Finance Leases)							
CFR – General Services	249,223	258,889	260,447	282,608	303,522	299,586	309,096
CFR – HRA	178,877	191,264	207,504	226,026	247,394	267,063	289,869
Total CFR	428,100	450,153	467,951	508,634	550,916	566,649	598,965
Movement in CFR	130	22,053	17,798	40,683	42,282	15,733	32,316
Movement in CFR represented by							
Net financing need for the year (above)	16,394	38,664	35,465	59,224	61,698	46,148	53,802
GS -Less loan fund repayments and other financing movements-	(13,263)	(13,681)	(13,939)	(14,534)	(15,079)	(25,672)	(16,370)
HRA - Less loan fund repayments and other financing movements	(3,001)	(2,930)	(3,728)	(4,007)	(4,337)	(4,743)	(5,116)
Movement in CFR	130	22,053	17,798	40,683	42,282	15,733	32,316

3.11 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

3.12 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 2017-18 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	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
GS Revenue Stream	226,773	229,902	238,805	246,519	249,655	249,655	249,655
GS Financing Costs	19,069	29,729	19,802	20,651	21,250	23,541	24,833
General Services	8.41%	8.30%	8.29%	8.38%	8.51%	9.43%	9.95%
HRA Revenue Stream	27,896	29,729	31,862	34,139	36,590	39,109	41,524
HRA Financing Costs	8,971	9,388	10,763	11,627	13,583	14,169	15,926
HRA	32.16%	31.58%	33.78%	34.06%	37.12%	36.23%	38.35%

- The gradual increase in the General Services ratio largely reflects the standstill in corporate income against a background of increased capital investment plans to support the infrastructure requirements associated with future growth plans. 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.
- Furthermore, the incremental impact of capital investment decisions on council tax and housing rent levels identify the revenue costs associated with the approved changes to the five year capital budget compared to the councils previously agreed commitments and plans, as set out in Tables 6 and 7 below.

Table 6 - Impact on Council Tax

£	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
General Services Debt £'000	209,500	220,644	223,549	247,254	269,745	267,376	278,451
Band D Equivalents	47,174	48,200	48,501	49,391	50,281	51,000	51,800
Debt per Band D Equivalent £	£4,601	£4,578	£4,609	£5,006	£5,365	£5,243	£5,375

Table 7 - Impact on Rent

£	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
HRA debt £m	178,877	191,264	207,504	226,027	247,394	267,063	289,869
Number of HRA dwellings	8,698	8,738	8,835	8,947	9,094	9,188	9,351
Debt per dwelling £	£20,565	£21,889	£23,487	£25,263	£27,204	£29,066	£30,999

3.13 The Council's treasury portfolio position at 31 March 2018, 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	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
External Debt							
Debt at 1 April	344,247	358,026	379,084	396,806	438,504	479,239	511,577
Expected change in Debt	13,779	21,058	17,722	41,698	40,735	32,338	42,251
Other long-term liabilities (OLTL)	41,319	39,724	38,246	36,899	35,354	33,777	32,211
Expected change in OLTL	(1,595)	(1,478)	(1,347)	(1,545)	(1,577)	(1,566)	(1,566)
Actual gross debt at 31 March	397,750	417,330	433,705	473,858	513,016	543,788	584,473
The Capital Financing Requirement	428,100	450,153	467,951	508,634	550,916	566,649	598,965
Under / (over) borrowing	30,350	32,823	34,246	34,776	37,900	22,861	14,492

3.14 The key treasury management 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. This year is projected to be within this indicator - External Debt £417m and CFR £509m (£428m+£22m+£18m+£41m). At the close of the 2017/18 financial year, the Council was well within this indicator, as the CFR for the actual year was £428 million and external borrowing was £398 million.

Boundaries for Debt

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

Table 9 – Operational Boundaries

Operational boundary £'000	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
Debt	411,907	431,052	473,280	517,139	534,438	568,320
Other long term liabilities	38,246	36,899	35,354	33,777	32,211	30,645
Total	450,153	467,951	508,634	550,916	566,649	598,965

3.16 Furthermore the Council must set maximum levels of borrowing by way setting Authorised Limits for its gross external debt. 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

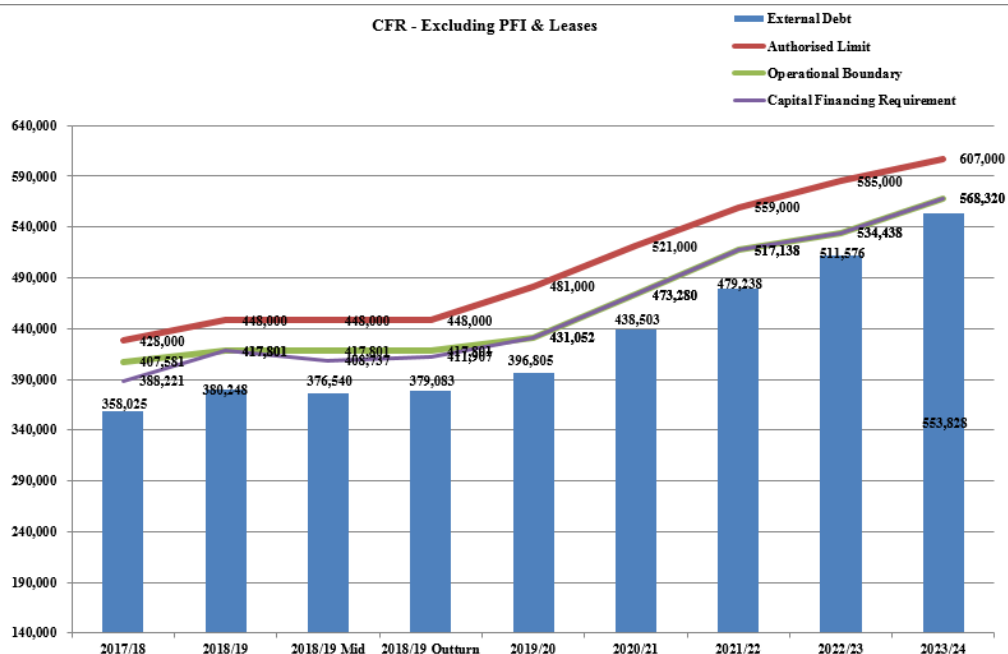
Authorised limit £'000	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate	2023/24 Estimate
Debt	448,000	481,000	521,000	559,000	585,000	607,000
Other long term liabilities	39,000	37,000	36,000	34,000	33,000	31,000
Total	487,000	518,000	557,000	593,000	618,000	638,000

3.17 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.

3.18 A summary of the CFR against the planned external debt is set out in Table 11 and the further graph set out overleaf.

Table 11

Excluding PFI & Leases	2017/18	2018/19	2018/19 Mid	2018/19 Outturn	2019/20	2020/21	2021/22	2022/23	2023/24
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Authorised Limit	428,000	448,000	448,000	448,000	481,000	521,000	559,000	585,000	607,000
Operational Boundary	407,581	417,801	417,801	417,801	431,052	473,280	517,138	534,438	568,320
Capital Financing Requirement	388,221	417,801	408,737	411,907	431,052	473,280	517,138	534,438	568,320
External Debt	358,025	380,248	376,540	379,083	396,805	438,503	479,238	511,576	553,828



3.19 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

3.20 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").

3.21 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.**

- 3.22 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 364 days.

Maximum principal sums invested > 364 & 365 days			
£m	2019/20	2020/21	2021/22
Principal sums invested > 364 & 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 does not directly affect the wellbeing of the community or have a significant impact on equality, the environment or economy.

6 RESOURCE IMPLICATIONS

- 6.1 Financial – these strategies are interwoven with the revenue and capital budgets. The expenditure and debt limits are consistent with the revenue budgets approved by the Council on 12 February 2019.
- 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 (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 Capital Investment & Treasury Management Strategy 2019-20 to 2023-24 (lodged in Members Library Service, Ref: 19/19, February 2019 Bulletin)
- 7.6 Council 12 February 2019 – Administration budget papers – General Services and HRA

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