REPORT TO:	East Lothian Council
MEETING DATE:	27 February 2018
BY:	Depute Chief Executive (Resources & People Services)
SUBJECT:	Treasury Management Strategy 2018/19 to 2020/21

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1 PURPOSE

1.1 To seek the approval of the Council of the Treasury Management and Investment Strategies for 2018/19 to 2020/21

2 RECOMMENDATIONS

2.1 The Council is recommended to :

i. note the Treasury Management Strategy referenced within sections 3.5-3.23

ii. note the Investment Strategy referenced in sections 3.24-3.27

iii. approve the repayment of loans fund advances by the statutory method before 1 April 2016 and after 1 April 2016 in sections 3.10-3.11

iv. approve operational boundaries for external debt as detailed in section 3.20

v. approve authorised limits for external debt as detailed in section 3.21

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 3.23

vii. approve the detailed Treasury Management Strategy Statement which has been submitted to the Members Library (Ref: 24/18, Feb 18 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 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 will be required to prepare an additional report, a Capital Strategy report, which is intended to provide the following:

- a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services
- an overview of how the associated risk is managed
- the implications for future financial sustainability

3.4 A detailed document more fully covering both the Treasury Management and Investment Strategies for 2018/19 to 2020/21 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 13 February 2018.

Treasury Management Strategy

3.5 Actual capital expenditure incurred in 2016/17 and the estimates of total gross capital expenditure to be incurred for 2017/18 and future years are detailed overleaf in Table 1:

Table 1

Capital expenditure £'000	**2016/17 Actual**	**2017/18 Estimate**	**2018/19 Estimate**	**2019/20 Estimate**	**2020/21 Estimate**
General Services	**18,559**	**32,152**	**44,974**	**46,097**	**52,639**
HRA	**23,343**	**23,421**	**24,364**	**37,683**	**33,754**
Total	**41,902**	**55,573**	**69,338**	**83,780**	**86,393**

3.6 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

Capital expenditure £'000	**2016/17 Actual**	**2017/18 Estimate**	**2018/19 Estimate**	**2019/20 Estimate**	**2020/21 Estimate**
Total Cap Ex	**41,902**	**55,573**	**69,338**	**83,780**	**86,393**
Financed by:					
Capital receipts	9,426	15,529	12,698	25,270	21,624
Capital Grants	13,472	15,545	15,464	18,947	19,870
Capital reserves	141				
Revenue	3200	2,500	1,700	2,600	3,500
Net financing need for the year	**15,663**	**21,999**	**39,476**	**36,963**	**41,399**

3.7 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.

3.8 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 2017 are detailed in Table 3 overleaf:

Table 3

£’000	2016/17 Actual	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate
Capital Financing Requirement					
CFR – General Services	217,559	212,810	221,399	217,495	221,574
PFI & Leasing	41,318	39,723	38,245	36,898	35,353
CFR – housing	169,092	181,171	196,403	220,541	239,906
Total Gross CFR	**427,969**	**433,704**	**456,047**	**474,934**	**496,833**
Movement in CFR	**405**	**5,735**	**22,343**	**18,887**	**21,899**

Movement in CFR represented by					
Net financing need for the year (above)	15,663	21,999	39,476	36,963	41,399
Less scheduled debt amortisation	15,258	16,264	17,133	18,076	19,500
Movement in CFR	**405**	**5,735**	**22,343**	**18,887**	**21,899**

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

3.10 For loans fund advances made before 1 April 2016, the policy will be to maintain the practice of previous years and apply the **Statutory Method** with all loans fund advances being repaid by the annuity method.

3.11 For loans fund advances made after 1 April 2016 (with regard to the Local Authority (Capital Finance and Accounting) (Scotland) Regulations 2016), the policy for repayment of loans will be the **Statutory Method** with all loans fund advances being repaid by the annuity method.

3.12 Assuming no further advances after year 5, the General Services expected loans fund balances are shown below in Table 4 and HRA expected loans fund balances are shown in Table 5.

Table 4

General Services £’000

Years	Opening balance	Advances	Repayments	Closing Balance
1	212,809	20,847	12,258	221,398
2-5	221,398	58,965	55,536	224,827
5-10	224,827		73,240	151,587
10-15	151,587		52,450	99,137
15-20	99,137		37,119	62,018
21-30	62,018		50,872	11,146
31-40	11,146		11,146	0
41-50	0		0	0

Table 5

HRA
£'000

Years	Opening balance	Advances	Repayments	Closing Balance
1	181,171	18,628	3,398	196,403
2-5	196,403	101,445	19,408	278,440
5-10	278,440		35,267	243,173
10-15	243,173		42,562	200,611
15-20	200,611		47,349	153,262
21-30	153,262		109,886	43,376
31-40	43,376		38,369	5,007
41-50	5,007		5,007	0

3.13 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 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

3.14 Prudential indicators are therefore 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.

3.15 The ratio of financing costs to net revenue streams identifies the trend in the cost of capital against the net revenue stream. Estimates of the ratio of financing costs to net revenue stream for the current and future years, and the actual figures for 2017/18 are:

Table 6

£'000	2016/17 Actual	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate
GS Revenue Stream	217,047	223,131	224,635	226,196	229,084
HRA Revenue Stream	26,956	28,673	29,760	32,066	34,781
GS Financing Costs	18,505	18,998	19,711	20,257	20,752
HRA Financing Costs	9,104	9,124	10,045	11,044	12,389
General Services	8.53%	8.51%	8.77%	8.96%	9.06%
HRA	33.77%	31.82%	33.75%	34.44%	35.62%

3.16 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 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.

3.17 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 three-year capital budget compared to the councils previously agreed commitments and plans.

Table 7 Impact on Council Tax

£	2016/17 Actual	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate
General Services Debt £'000	**217,559**	**212,809**	**221,399**	**217,495**	**221,574**
Band D Equivalents	**43,877**	**47,369**	**48,253**	**49,142**	**50,030**
Debt per Band D Equivalent £	**4,958**	**4,493**	**4,588**	**4,425**	**4,429**

Table 8 Impact on Rent

£	2016/17 Actual	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate
HRA debt £'000	**169,092**	**181,171**	**196,403**	**220,541**	**239,906**
Number of HRA dwellings £m	**8649**	**8693**	**8735**	**8920**	**9090**
Debt per dwelling £	**19,550**	**20,841**	**22,485**	**24,724**	**26,392**

3.18 The Council's treasury portfolio position at 31 March 2017, with forward projections are summarised in Table 9 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 9

£'000	**2016/17 Actual**	**2017/18 Estimate**	**2018/19 Estimate**	**2019/20 Estimate**	**2020/21 Estimate**
External Debt					
Debt at 1 April	337,160	344,247	358,084	380,248	399,707
Expected change in Debt	7,087	13,837	22,164	19,459	24,121
Other long-term liabilities (OLTL)	42,506	41,318	39,723	38,245	36,898
Expected change in OLTL	-1,188	-1,595	-1,478	-1,347	-1,545
Actual gross debt at 31 March	**385,565**	**397,807**	**418,493**	**436,605**	**459,181**
The Capital Financing Requirement	**427,970**	**433,704**	**456,047**	**474,934**	**496,833**
Under / (over) borrowing	**42,405**	**35,897**	**37,554**	**38,329**	**37,652**

3.18 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 £398m and CFR £475m (£428m + £6m + £22m + £19m). At the close of the 2016/17 financial year, the Council was well within this indicator, as the CFR for the actual year was £428 million and external borrowing was £386 million.

3.19 The Council is asked to approve in Table10 the operational boundaries for gross external debt. This is the limit beyond which external debt is not normally expected to exceed.

Table 10

Operational boundary £'000	**2017/18 Estimate**	**2018/19 Estimate**	**2019/20 Estimate**	**2020/21 Estimate**
Debt	393,980	417,801	438,035	461,479
Other long term liabilities	39,723	38,245	36,898	35,353
Total	433,703	456,046	474,933	496,832

3.20 A further key indicator represents a control on the maximum level of borrowing. 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.

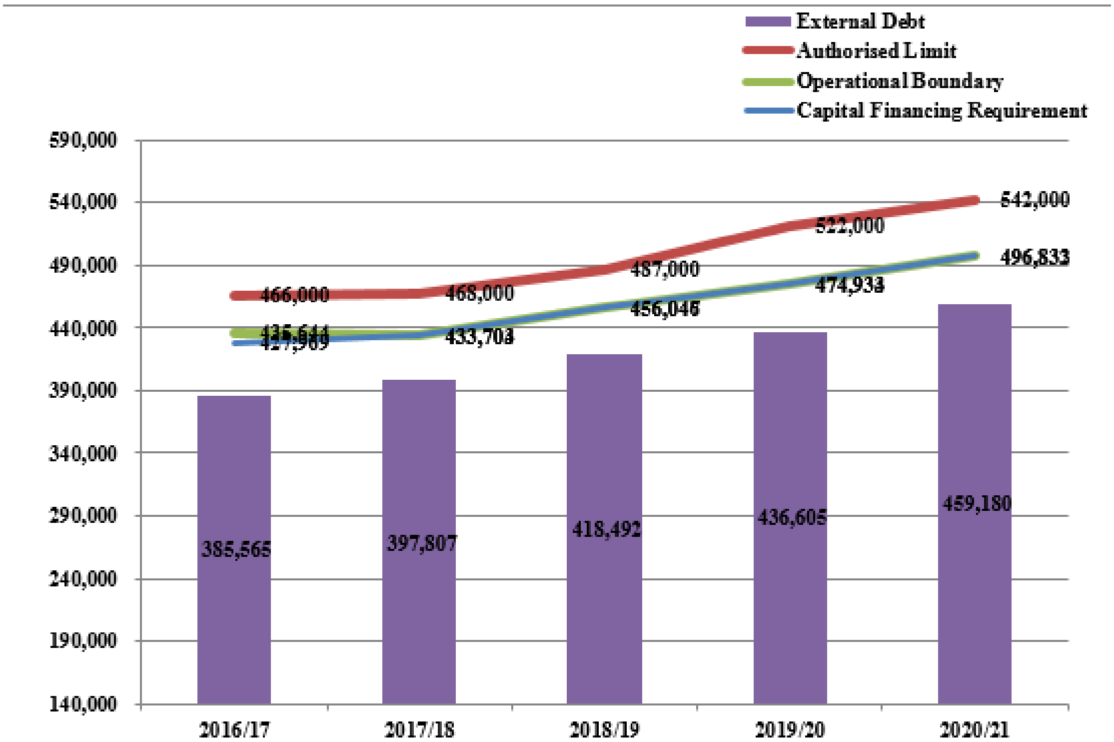
Table 11

Authorised limit £'000	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate
Debt	428,000	448,000	485,000	506000
Other long term liabilities	40,000	39,000	37,000	36,000
Total	**468,000**	**487,000**	**522,000**	**542,000**

3.21 These authorised limits are consistent with the Council's current commitments, existing plans and the approved budget 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, or timing issues with expected capital income.

Capital Financing Requirement

Including PFI & Leasing	2016/17	2017/18	2018/19	2019/20	2020/21
	£'000	£'000	£'000	£'000	£'000
Authorised Limit	466,000	468,000	487,000	522,000	542,000
Operational Boundary	435,644	433,703	456,046	474,933	496,832
Capital Financing Requirement	427,969	433,704	456,047	474,934	496,833
External Debt	385,565	397,807	418,492	436,605	459,180



3.22 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.

Investment Strategy

3.23 The Council's Investment Strategy for 2017/18 has been prepared in accordance with the Local Government Investments (Scotland) Regulations 2010 and the CIPFA Treasury Management Code.

3.24 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.

3.25 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.

3.26 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	**2018/19**	**2019/20**	**2020/21**
Principal sums invested > 364 & 365 days	£m 10	£m 10	£m 10

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 Council Plan associated with a Council Asset Management Plan.

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 13 February 2018.

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 2018/19 to 2020/21 (lodged in Members Library Service)

7.6 Council 13 February 2018 – all papers

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