Agenda Item 13

To:	**Cabinet**
Date:	**13 July 2022**
Report of:	**Head of Financial Services**
Title of Report:	**Medium Term Financial Strategy 2023-24 to 2026-27**

Summary and recommendations	
Purpose of report:	To agree the budget setting strategy for the forthcoming Medium Term Financial Plan 2023-24 to 2026-27
Key decision:	Yes
Cabinet Member:	Councillor Ed Turner, Deputy Leader (Statutory) – Finance and Asset Management
Corporate Priority:	All
Policy Framework:	Council Strategy 2020 – 2024, Budget 2022 – 2023

Recommendation: That Cabinet resolves to:	
1.	**Approve** the budget setting strategy for the Medium Term Financial Plan 2023-24 to 2026-27.

Introduction

1. The purpose of the Medium Term Financial Strategy is to pull together in one place all known factors affecting the financial position and financial sustainability of an organisation over the medium term. A number of plans are integral to the overall strategy, including:

- Council Corporate Plan 2020-24 and Business Plan 2022-23
- 2023/24 to 2026/27 General Fund Revenue Budget and Medium Term Financial Plan
- 2023/24 to 2026/27 Capital Strategy and Capital Programme
- Housing Revenue Account 30 year Business Plan
- Oxford Direct Services Ltd Business Plan
- Oxford City Housing Ltd 40 year business plan
- Treasury Management Strategy
- Asset Management Plan
- Procurement Strategy

- Risk Management Strategy

2. The MTFS balances the financial implications of objectives and policies against constraints in resources and provides the basis for decision making. As a living document the process of producing and updating the MTFS is as important as the output in giving a focus to the future implications of decisions as well as discussion of priorities and external influences.

3. It is intended to support the council in:

    - Becoming more financially sustainable and resilient;
    - Aligning resources to deliver council plan priorities;
    - Driving value for money; and
    - Safeguarding public money.

Background

4. An effective MTFS requires the organisation to be aware of its overall financial position by being more inclusive and widening the ownership of the MTFS to ensure its success. Whilst much of the development is undertaken within Finance, the wider ownership and engagement of the organisation, particularly from those responsible for decision making is critical and the council priorities ensuring that decisions required to achieve strategic outcomes are made within the context of a robust, timely and relevant MTFS given constraints in funding.

Key Pillars of the Financial Strategy

5. A robust MTFS will ensure:

    a. A balanced budget is achieved in all four years of the MTFS

    b. An alignment of expenditure to the Councils core priorities contained in the Councils Corporate Plan:

        i. Enable an inclusive economy
        ii. Deliver more, affordable housing
        iii. Support thriving communities
        iv. Pursue a zero carbon Oxford

    c. The making of suitable provisions for general reserves and known liabilities

    d. Building sufficient risk / contingency allocations into budget plans

    e. Making plans for capital spend that are appropriate, timely, cost effective and affordable across the life of the asset.

Budget Setting Strategy

6. Given the significant financial challenge the Budget Setting process is being started earlier than in previous years and improvements will be made to ensure the integration of Service and Financial Planning.

7. With increases in interest rates and inflation and continued uncertainty around many of our key income streams such as retained business rates, external income and company dividends, this year's budget setting process is unlikely to be any less problematic than previous years. Unlike previous years there is limited scope for one off use of reserves and balances to balance the budget. There is a sense that the usual due diligence of savings and efficiencies has already been undertaken and consequently the Council may need to reduce spend and potentially services if it is to fulfil its statutory duty to provide a balanced budget over the four year period. This will only be exacerbated should any of the assumptions previously made in the MTFS begin to change adversely.

8. The City Council is not alone in facing such a challenging situation. As a consequence, it will lobby both individually, and collectively with other local authorities so far as there is appetite to do so, to press for a fair settlement on local government funding for all authorities who are affected by the current situation, with dramatically increased energy costs and construction costs, rising interest rates, and reduced income due to the Covid pandemic. The Deputy Leader of the Council has written to the Secretary of State for Levelling Up, Housing and Communities pressing these points.

9. The budget setting strategy for this year through a series of service review meetings over the coming months will:

    a) Avoid incremental cuts to services

    b) Challenge managers to identify additional efficiencies and income whilst providing the existing level of service

    c) Request managers to identify changes to service delivery perhaps from additional investment in staffing or ICT or look at alternative delivery models which could result in additional savings or income

    d) Look at the minimum level of service that could be provided

    e) Look at whether the service can be removed altogether.

10. Service Reviews will be undertaken using a set of principles put forward by the Corporate Management Team as follows:

    A. Create a leaner, more efficient, organisation, reducing head count to enable a more progressive pay structure in the medium term

    B. Drive *and profile* additional income from assets and services within the next four-year MTFP, balanced against an assessment of risk and resource

    C. Right size service delivery, where structural changes following the pandemic, have led to reduced (or increased?) demand

    D. Identify new cost reductions, or additional income, which can be achieved through:

        a. planned, or new, investment in ICT
        b. reductions in energy costs
        c. any other area of the council's business

    E. Create alternative ways of wholly, or partially, delivering (or funding) services, including those of a non-statutory nature

F. Reduce service delivery to the minimum viable proposition possible to meet statutory or other requirements, in order to realise a saving

G. Drive financial returns from our wholly owned companies and joint ventures whilst recognising the risks

H. Mitigate the potential impact of not achieving income currently planned within the MTFP.

11. The information below outlines the starting position for the budget review together with an update on assumptions previously made which will need to be incorporated into the forthcoming budget setting process.

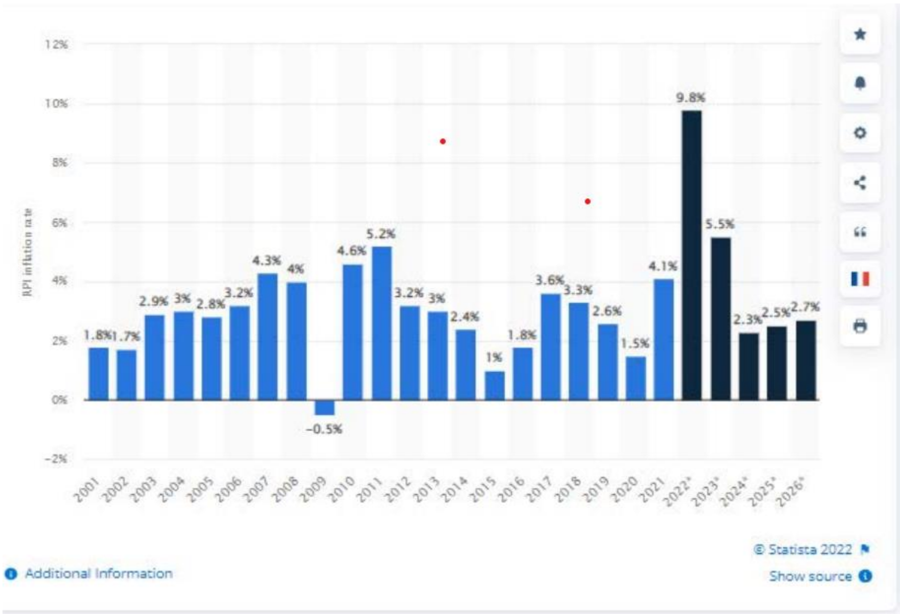
12. The Consultation Budget will be presented to Cabinet on 14th December and once agreed will be subject to the usual 6 weeks consultation process with residents, businesses and other groups, returning to Cabinet In February 2023 for sign off by Cabinet and Council.

National Economic Position

Inflation Rate Forecasts

13. Prices were already on the increase due to increases in utilities prior to recent events in Ukraine and these will continue to drive inflation upwards from its latest forecast level in March 2022 of 6.1% to a forecast 9.8% by the end of the year. This is widely forecast to fall back in future years although how much by is still uncertain. Suffice to say that this is likely to lead to budgetary pressures for the council and its wholly owned companies for the purchase of supplies and services.

Table 1: Inflation Forecasts



Interest Rate Forecasts

14. On 16th June the Bank of England (BoE) increased the bank rate from 0.75% to 1.00%, marking the fourth successive rate hike. The Bank's decision was driven by the desire to rein in surging inflation and the prevailing weak economy

15. Link Asset Management predict the next base rate rise to be in September of this year with a peak of 2.75% in December 2023 but they also indicate that the rate could peak at a higher level than this if the economy continues at its current level. .

16. Forecast interest rates are shown below.

Link Group Interest Rate View 21.06.22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25
BANK RATE	1.75	2.25	2.75	2.75	2.75	2.75	2.50	2.50	2.25	2.25	2.25	2.25
3 month ave earnings	2.00	2.50	2.80	2.80	2.80	2.80	2.60	2.50	2.30	2.30	2.20	2.20
6 month ave earnings	2.50	2.80	3.00	3.00	2.90	2.90	2.80	2.70	2.60	2.50	2.40	2.30
12 month ave earnings	3.10	3.20	3.20	3.20	3.00	2.90	2.80	2.60	2.50	2.40	2.40	2.40
5 yr PWLB	3.20	3.30	3.30	3.30	3.30	3.20	3.10	3.00	3.00	3.00	2.90	2.90
10 yr PWLB	3.40	3.50	3.50	3.50	3.50	3.40	3.30	3.20	3.20	3.20	3.10	3.10
25 yr PWLB	3.70	3.70	3.70	3.70	3.70	3.70	3.60	3.50	3.50	3.40	3.40	3.30
50 yr PWLB	3.40	3.40	3.50	3.50	3.40	3.40	3.30	3.20	3.20	3.10	3.10	3.00

17. The Council currently makes use of internal borrowing from reserves and balances to fund new capital expenditure although the requirement to borrow (known as the Capital Financing Requirement) is set to increase by around £58 million and £155 million for the General Fund and HRA respectively over the next 4 years, putting pressure on the Council to take on Public Works Loans Board (PWLB) external debt. The increases in borrowing rates illustrated above are around 1.5% higher than those used in the MTFP in the earlier period moving to 0.75% higher in the later years. This could result in a slightly improved position in the earlier years due to higher investment interest returns but as balances are used for internal borrowing this could move to a broadly neutral position where borrowing costs changes and investment income changes equalise. Over the life of the MTFP. The Housing Company, OCHL, will equally be affected by interest rate rises possibly by as much as £750k over the life of the MTFP, which will impact dividend returns to the Council. These changes have yet to be factored into the MTFP assumptions below.

General Fund Revenue Forecasts

18. Based on the assumptions at the time the unpublished budget for 2026-27 indicated a budget pressure in the order of £5.5 million and extending this by another year 2027-28 would indicate that this may rise to around £6.2 million as indicated below.

Medium Term Financial Strategy 2023/24 - 2027/28	2023/24 £	2024/25 £	2025/26 £	2026/27 £
Base Budget	29,646,748	29,889,148	30,022,748	30,265,148
Efficiencies	(362,000)	(2,211,000)	(3,051,000)	(3,051,000)
Fees and Charges	(1,075,009)	(1,638,779)	(1,169,244)	(1,169,244)
New Investment	(315,000)	(1,367,000)	(1,427,000)	(1,427,000)
Inflation & other pressures	(367,653)	(258,053)	(240,053)	(240,053)
Revenue Contributions	1,163,200	963,200	963,200	963,200
Net interest	(7,118,936)	(10,802,249)	(11,045,276)	(5,881,171)
Depreciation reversal	(5,662,415)	(5,662,415)	(5,662,415)	(5,662,415)
Corporate costs including MRP, pay	7,662,956	10,535,214	12,213,795	13,252,375
Contingencies	554,593	731,593	661,594	661,594
Transfers to/ (from) reserves and working balances	(4,045,804)	589,466	211,112	55,200
Net Budget Requirement	20,080,679	20,769,125	21,477,461	27,766,634
FUNDING				
Council Tax	(15,201,715)	(15,659,272)	(16,130,600)	(16,616,115)
Retained Business Rates	(4,878,963)	(5,109,854)	(5,346,861)	(5,590,136)
New Homes Bonus	0	0	0	0
Total	(20,080,678)	(20,769,126)	(21,477,462)	(22,206,251)
(Surplus)/ Deficit	1	(0)	(0)	5,560,383

Key General Fund Assumptions

Government Funding

19. The following are key assumptions on future Government funding, much of which is still uncertain:

- **The Final Finance Settlement** for local Government announced on 13th January 2022 did not deliver the longer term funding promises previously announced by Government and hence much uncertainty still exists in a number of areas as indicated below.

- **Business Rates** – The fairer funding allocation linked to business rates retention was eventually delayed from the original implementation date of 1ST April 2022 although no date has been confirmed when it will be brought in. Latest assumptions are that this will be 1st April 2023 and a £2.5 million reduction of business rates income has been assumed from the existing retained amount of ££7 million. Considerable uncertainty still exists around this figure.

- **New Homes Bonus** – It is widely believed that the final payments of New Homes Bonus to local authorities were made in 2022-23. The amount for Oxford was £200k, no confirmation of ongoing funding has been given or assumed in the MTFS

- **Lower Tier Services Grant** – Within the Finance Settlement a further year of lower tier services grant was given, with a total national value remaining unchanged at £111m. The Councils allocation was £266k and no further allocation has been assumed.

- **2022/23 Services Grant** – This new £822m grant was in respect of COVID pressures experienced by local authorities. The Councils allocation was £431k which has been assumed to be for one year only.

Corporate Planning Assumptions

20. The following assumptions are in relation to core areas of the MTFS:

    - **Council Tax Increase** – Assuming council tax referendum levels remain at below 2% for District Councils then council tax increases are assumed to be 1.99% each year of the MTFS period. A 1% increase would mean additional revenue of approximately £150k per annum.
    - **Pay Assumptions** – The Council recently agreed a pay deal for the 2 year period commencing 1-4-2022 of 2% for 2022-23 and 2.5% for 2023-24. Whilst some inflationary rise has been assumed for the later years of the MTFS it is worth noting that officers are working on a wider more structural review of pay going forward. The intention is to try and contain pay within the future budget envelopes although the ability to do so remains a challenge – and one which will become more acute with current levels of inflation.
    - **Capital Financing** - The Capital programme is largely funded by borrowing and any available capital receipts. The revenue implications for borrowing have been included of around 5% including Minimum Revenue Provision. Officers are encouraged to only submit capital bids to fund invest to save projects or that are predominantly externally funded.
    - **Contingencies** – Provision has been made for contingencies to cover unachieved efficiencies and other risks of around £600k per annum across the MTFS. The Council has had a good track record of delivering within budget over the past few years and contingencies held against high risk savings have usually been underspent.

21. **Utilities** – The Council has around 20 flexible electricity contracts, 50 flexible gas contracts and some 700 fixed term contracts at an estimated cost of around £1.6 million per annum. Fixed term contracts with the council’s current supplier end on 1St October. The current unprecedented global conditions and events are anticipated to lead to a significant step up in energy spend from 1St October based on current projections which could rise to between £2.4 million and £4.6 million per annum.

22. **Efficiencies** – Within the MTFS efficiencies aimed at achieving ongoing annual revenue savings of £3.9 million by the end of the 4 year period have been included arising from:

    a) **Reducing office space and remote working -** £630k per annum with effect from 1-4-2023. Officers will also examine options for a more ambitious project to let the entire building during this next budget setting round

    b) **Communities and Housing Integration –**£480k per annum from 2022-23

    c) **Community Grants –** £200k reduction from 2022-23

    d) **Housing Needs – £300k per annum –** A review of Housing Needs services to reduce cost of preventing homelessness, gain better access to private rented sector housing, reduce the cost of temporary accommodation, and reviewing the process for applications to the housing register

e) **Rough sleeping –** £189k on going from 2023-24 -County wide changes to the provision of the service to release efficiencies

f) **Revenues and Benefits system replacement –** £100k saving per annum from staffing and the resilience contract

g) **Data Centre and ICT storage-** a package of measures to release £300k of savings per annum

h) **Transformation**
   - Investing in ICT software and new technology - £496k per annum
   - Customer Services – reviewing processes and procedures that streamlines the customer experience in a number of service areas brought about by the introduction of new technology -£268k per annum
   - Procurement - review of contracts for supplies and services to reduce costs -£100k per annum

External Income

23. Our key income streams continue to be under significant pressure. In some areas income streams are not bouncing back as quickly as previously thought. Income levels for 3 key income streams is as follows:

			Actual 2019-20 £000's	Actual 2020-21 £000's	Actual 2021-22 £000's	Budget 2022-23 £000's	Budget 2023-24 £000's	Budget 2024-25 £000's	Budget 2025-26 £000's
Car parking			**7,426**	**2,968**	**5,683**	**6,724**	**6,800**	**6,877**	**6,955**
Commercial rents base rentals			9,097	11,707	10,536	10,380	10,361	10,697	10,697
Additional from regeneration					1,117	2,028	993	1,651	2,377
Provision for bad debt				-3,973	-2,400				
	Sub total		**9,097**	**7,734**	**9,253**	**12,408**	**11,354**	**12,348**	**13,074**
Town Hall lettings			**899**	**209**	**614**	**808**	**1,058**	**1,058**	**1,058**
Total			**17,422**	**10,911**	**15,549**	**19,940**	**19,212**	**20,283**	**21,087**

24. **Town Hall and lettings–** The pre-pandemic base budget in 2019-20 was around £0.9 million. Actual income dropped to around £614k in 2021-22. In 2022-23 the current assumption is an increase to pre-pandemic levels with further increased income of £250k ongoing.

25. **Commercial Property Income** – The pre-pandemic budgeted income in 2019-20 was £11.7 million. Whilst income continues to be charged at this level, the level of arrears continues to increase, with a provision for bad debt set aside at £3.9 million and £2.4 million for 2020-21 and 2021-22 respectively. Base income from the existing portfolio of property for 2022-23 and onwards continues to be budgeted at around £10.3 million - £10.6 million which is £1.4 million to £1million less than pre-pandemic levels per annum. This reduced amount of income has been offset by increased income from regeneration activity including the leasing of Boswells and Cave Street as approved by Cabinet and Council.

26. **Car parking income-** Car parking income was around £3.8 million down in comparison to the budgeted income in 2020-21. The current assumption is a return to pre-Covid levels in 2023-24, a projection which still gives cause for concern based on current usage and one which is likely to be pushed back.

Wholly Owned Companies and Joint Ventures

Oxford Direct Services Ltd

27. Difficult trading conditions and rising costs, which have been compounded by the issues in relation to QL, previously reported, have delayed any return of dividend back to the Council in the last few years. Additional growth and additional efficiencies are required if previous years' unpaid dividends totalling circa £1.9 million are to be paid together with future dividends of £12 million already included within the MTFS over the next 4 years.

28. The revised Company Business Plan will be presented to shareholders in September 2022, the updated dividends from which will be incorporated within the Council's MTFS.

Housing Company- Oxford City Housing Ltd

29. The company makes financial returns to the Council in three primary ways:

    a) A 3.2% margin on loan interest on borrowing
    b) Support service agreement charges payable to the council inclusive of a 5% uplift to cover transfer pricing
    c) Dividend payments out of surpluses generated by the Company from housing developments.

30. The housing company is equally experiencing issues that affect the development programme including, rising supply costs, increases in capital gains tax and borrowing costs and slippages all of which will impinge on the dividend. The revision of the OCHL Business Plan in May 2022 may show an adverse financial impact on company from rising costs of development which will impact on surpluses and potentially the £12 million dividend payment to the Council over the next 4 years, which is also reliant on the planning authority granting planning approval for the schemes in the programme. The ability of the company to deliver additional dividend in future years will depend on a continuous pipeline of schemes and remains uncertain.

Oxwed LLP and Grenoble Road

31. The Council has a number of other joint venture/ limited liability partnerships on which it is currently working. With the exception of interest payable by Oxwed for loans to the company made by the council, there are no other revenues from these scheme, included within the MTFS. During the current budget setting process the ability to introduce such income within the next 4 year period will be a challenge.

Use of Working Balances and Transfers from Reserves

32. The Council has around £11 million in a COVID Emergency Reserve and over the 4 year period of the MTFS assuming delivery as planned around £5.588 million will be drawn from this reserve in addition to around £5 million which is planned to be drawn from reserves in 2021-22. Earmarked reserves at 31-3-2021 stood at around £67million although only around £22 million which includes the COVID Reserve) is usable. No further additional draw on reserves will be planned over the next 4 year period.

Housing Revenue Account Budget

33. The Council continues to operate an ambitious programme of investment both in the maintenance and refurbishment of its existing stock of 7,664 council dwellings, regeneration of its council estates and also investment in new social housing dwellings constructed by the Councils wholly owned company Oxford City Housing Limited (OCHL). The Capital programme budgeted for £366 million of capital works over the next four years with £274 million of this being spent on purchases of 759 new build social houses. The commitment to OCHL was for the purchase of 1114 dwellings over a 10 year period for approximately £370 million.

34. In managing future risks that will inevitably start to rise as more debt is taken on to facilitate new build housing and regeneration the consultants recommended that as well as managing net income per dwelling that more use is made of Prudential indicators to manage these risks

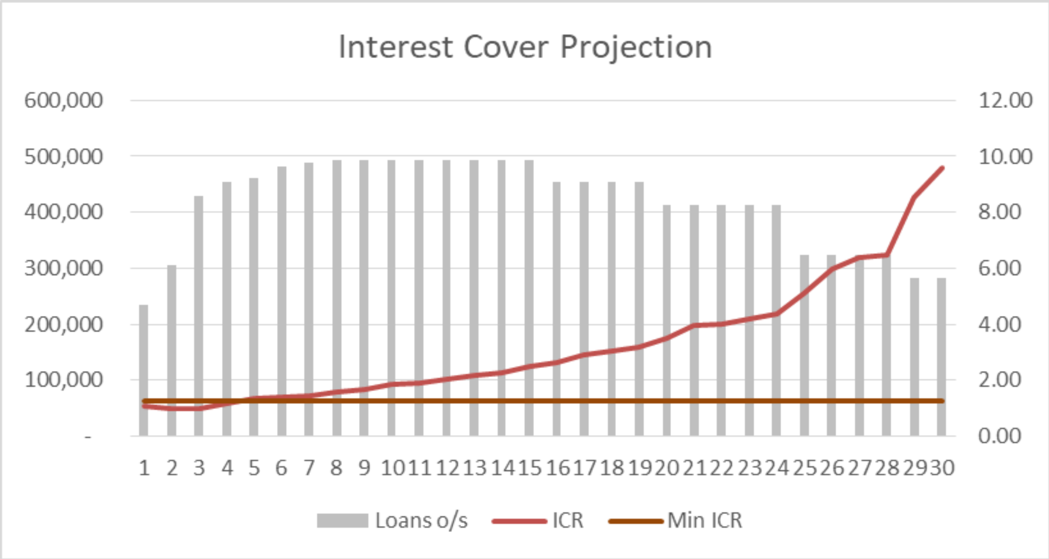
35. Prudential indicators are used in the Treasury Management Strategy to control the level of borrowing being undertaken to one which is financially prudent and affordable and are a matter of judgement by the Section 151 Officer but those typically used by banks and building societies to assist management would be:

    a) Interest cover ratio – ratio of operating surplus divided by interest cost i.e. how many times interest can be paid from surpluses
    b) Loan to value ratio- outstanding debt/ fixed asset value at year end
    c) Debt to income ration – Turnover / debt

36. The most widely used ratio is interest cover and typically Registered Providers would operate on a ratio of 1.72:1 and 2.1:1. As a golden rule 1.25:1 would be acceptable especially given the significant housing development being undertaken by the Council.

    In preparation of the revised HRA Business Plan the Section 151 Officer has agreed a trajectory of interest cover ratio from the existing level of 1.10:1 to 1.25: 1 over the first 4 years of the Business Plan and thereafter budgeted spend is approved which seeks to ensure that this ratio is maintained at a level of at least 1.25:1.

37. The chart below shows this ratio graphically:



Year	22/23	23/24	24/25	25/26	26/27	27/28	28/29	29/30	30/31
Year in BP	2	3	4	5	6	7	8	9	10
Interest Cover Achieved	1.00	1.00	1.18	1.35	1.38	1.43	1.60	1.69	1.87

38. Using this financial indicator when the budget was agreed in February 2022 the HRA Business indicated that there would be no capacity within the HRA to accommodate any further spend until 2025-26. Since then there have been a number of changes to the plans which will be incorporated into the next budget refresh.

Key Assumptions in the HRA Business Plan

39. The HRA Business Plan assumes that it will continue to purchase the affordable housing from OCHL's 10 year development programme 1,114 properties within an overall budget envelope of £367 m before grant and share ownership sales, £289 m when these are taken into account.

40. **Social Dwelling Purchases -**The HRA purchases such social dwellings from OCHL based on a set of 'financial viability indicators agreed with the Councils Section 151 Officer as follows:

a) Net present value (NPV)– positive over a 70 year period
b) Payback – 70 years or under
c) Internal rate of return IRR -(the discount rate which equates the Net Present Value to zero) of 3%

41. **Debt –** The closing HRA loan balance at 31-3-2023 is forecast to rise to around £306 million with peak debt rising to £494 million by 2028-29. The HRA business plan will to accommodate loan charges for this amount of debt with future interest currently estimated at 3%.

42. **Rent Increase -** Under the Governments rent standard from 1st April 2020 rent may only be increased by up to CPI +1% for a period of five years for local authority and

housing association social rents. 2022/23 is the third year of the rent standard and rent was increased by CPI + 1% i.e. 4.1% with 3% increases estimated for future years. With CPI currently at around 6.2% consideration will need to be given to affordability as well as prudent financial planning for future rises.

43. **Working Balance -** The working balance levels allow sufficient monies for the funding of future years' Capital Programme, the repayment of the debt, as well as an amount of £3.5 million as being the minimum required to cover unexpected events such as falling investment income or increased costs.

Financial Implications

44. These are covered within the main body of the report.

Legal Implications

45. Section 151 of the Local Government Act 1972 places a general duty on local authorities to make arrangements for 'the proper administration of their financial affairs' with the assistance of the Chief financial officer.

46. Section 30(6) of the Local Government Finance Act 1992 provides that the Council is required to set a budget before the 11th March in the financial year preceding the one in respect of which the budget is set, taking account of working balances and any other available reserves. Good practice would equally require the preparation of a Medium Term Financial Plan for the proceeding 3 years.

47. The Local Government Act 2000 states that it is the responsibility of the full council, on the recommendation of the executive to approve the budget and related council tax demand.

48. Section 114 (2) of the Local Government Finance Act 1988 requires the Chief Finance Officer of the authority to make a report to Council if it appears that the authority is about to take a decision which is 'unlawful'.

49. Failure to set a legal budget may lead to intervention from the Secretary of State under section 15 of the Local Government Act 1999.

Equality and Diversity

50. Specific budget proposals will be subject to an equality and impact assessment when it is presented to Cabinet in December.

Risk Implications

51. The forecast projections for the General Fund would indicate that the forthcoming budget process will require additional efficiencies to be delivered, delivery methods to be reviewed and potentially some services reduced if the Council is to fulfil its statutory requirement to provide a balanced budget next year and a balanced plan over the proceeding 3 years.

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Background papers: None

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