APPENDIX A

MEDIUM TERM FINANCIAL STRATEGY 2016/2020

Introduction

The purpose of the Medium Term Financial Strategy (MTFS) sets out the strategic direction for the financial management of the Council, providing the financial framework that supports delivery of the priorities set out in the Council Plan. The MTFS outlines the principles and key assumptions that direct the construction of the City Council's Medium Term Financial Plan (MTFP). The MTFS is underpinned by a range of financial principles and practices that are contained within the budget guidelines and financial management handbook. This document is regularly reviewed to ensure that they are fit for purpose and to ensure that councillors have a sound basis for planning and decision making.

As part of the 2016/17 budget process the MTFP is presenting a four year view in response to the Government's offer of four year funding settlement to 2019/20 for any council that wishes to take up the offer.

The sub-sections of the MTFS are set out below:-
1 – Policy Framework
2 – Economic and Financial Context
3 – Financial Framework
4 – Summary MTFP

1. POLICY FRAMEWORK

The Council's service planning and MTFS are aligned to ensure that the MTFP reflects the priorities of the Council, and that service plans explain how priorities will be delivered with the resources available. The MTFS creates the framework for resource allocation decisions that will support the delivery of the Council Plan.

Council Plan

The plan sets out how the City Council aims to make Nottingham a great city with citizens at the heart of everything we do.
The latest Council Plan, approved by Full Council on 9 November 2015, sets out the Council's ambitions for the city over the next four years up to 2019. The Plan underpins the council's wider Good to Great journey, with a continued emphasis on placing citizens at the heart of everything we do to shape our service delivery going forward. This includes 5 key objectives for the Council to deliver:

- Ensure that every child in Nottingham is taught in a school that is judged good or outstanding by Ofsted
- Build 2,500 new homes that Nottingham people can afford to rent or buy
- Cut the number of victims of crime by a fifth and continue to reduce anti-social behaviour
- Tackle fuel poverty by setting up a not for profit energy company, to sell energy at the lowest possible price to Nottingham people
- Guarantee a job, training place or further education plan for every 18-24 year old

Citizens at the Heart

This strategy ensures that all areas of the City Council's work have the 'Citizen at the Heart', this strategy has four elements to it being:

- Great City - Shared Prosperity – Reduced Poverty
- Great Workforce - Working Together
- Great Services – The Nottingham Way
- Great Council – Delivering on Promises

2. ECONOMIC AND FINANCIAL CONTEXT

National Context

Economic background: Domestic demand has grown robustly, supported by sustained real income growth and a gradual decline in private sector savings. Low oil and commodity prices were a notable feature of 2015, and contributed to annual CPI inflation falling to 0.1% in November. Consumer confidence has been boosted by wages growing at 2.4% a year, and the unemployment rate falling to 5.2%. This has helped to underpin retail spending and hence GDP growth, which was 2.1% a year in the third quarter of 2015.

The Bank of England's Monetary Policy Committee (MPC) has held policy rates at 0.5% for the 82nd consecutive month at its meeting in December 2015. Quantitative Easing (QE) has been maintained at £375bn since July 2012.

Uncertainty over the outcome of the forthcoming EU referendum is expected to put downward pressure on UK GDP growth and interest rates.

China's growth has slowed and its economy is performing below expectations, reducing global demand for commodities and contributing to emerging market weakness. Financial markets have reacted negatively on concerns that the Chinese slowdown will present a significant drag on global growth. US domestic growth has accelerated but the globally sensitive sectors of the US economy have slowed. Strong US labour market data and other economic indicators suggested recent global turbulence has not knocked the American recovery off course, although activity has weakened a little. The Federal Reserve raised policy rates at its meeting in December as expected, but accompanying statements suggested that the tightening cycle will be gradual and very much data dependent. In contrast, the European Central Bank finally embarked on QE in 2015 to counter the perils of deflation and undertook further monetary easing late in the year.

Public spending: The Chancellor's Autumn Statement announced that policing, health, international aid and defence budgets would be protected from further funding reductions, requiring the remaining unprotected public services, including local government to deliver significant further savings. By 2020 unprotected Government departments will have their funding reduced by a total of £20bn.

The November 2015 Spending Review forecast that core central government funding will fall by **24%** in real terms or **£4.1bn** over the Spending Review period. Taking into account Office of Budget Responsibility (OBR) forecasts of income raised locally by councils, the overall position is a **6.7%** real terms reduction.

The Local Government Association (LGA) also predicts that councils will have **£3.6bn** of budget pressures by 2019/20 this is in addition to the **£6.3bn** of pressures as a result of previous Government decisions.

The Autumn Statement also confirmed the planned reforms to Business Rate Retention, which will allow local authorities to retain all Business Rates by 2020. At a national level the intention is that this will be financially neutral, with additional responsibilities being passed to local government to be financed from the additional income passed through. The impact and transfer of risk to Nottingham will only become clear later.

Further changes to specific grants were included in the Local Government Financial Settlement and are reflected in the MTFP.

Interest rate forecast: The Authority's treasury advisor Arlingclose projects the first 0.25% increase in the UK Bank Rate in the third quarter of 2016, rising by 0.5% a year thereafter, finally settling at or below 2% in several years time. Persistently low inflation, subdued global growth and potential concerns over the UK's position in Europe mean that the risks to this forecast are weighted towards the downside. Arlingclose projects the 10 year gilt yield to rise from its current 1.8% level by around 0.3% a year.

Public Sector Pay: Public sector pay was subject to a pay freeze in 2011/12 and 2012/13, but increased on average by 1% in 2013/14. The nationally agreed pay award for 2014/15 included a 15 month (covering January 2015 to March 2016) increase of 2.2%, with some specific non-consolidated increases at a lower level. The national Government announced in the Emergency Budget of June 2015, that public sector pay would be capped at 1% for the next four years.

Local Context

Population: The population of Nottingham has increased in the last decade and in 2013 was **310,800**. This is predicted to continue to grow, with the largest predicted growth being in the 70-74 age group. Due to the large student population in the City the largest age band is 20-24. Nottingham is a diverse city in terms of ethnicity, with over a third of the population being non-white British. The 2011 census reported **18.1%** of Nottingham's population having health problems or disabilities which limit their day to day activity, this is slightly above the national average (**17.6%**).

Local economy: Greater Nottingham's economy has seen steady growth since 2012. In 2012 the Greater Nottingham economy was worth £12.91bn. Provisional figures for 2014 show that this has increased to £13.66bn, growth over the period of 5.8%, lower than the average 9% achieved in England over the same period. The growth has been lower than the national averages, largely due to a lack of growth in the Public Sector, which dominates the local economy.

Forecast overall employment growth for Nottinghamshire (including Nottingham City) to 2022 is 4.5% which is equivalent to 22,000 jobs, a total workforce of 755,000. There are also expected to be around 170,000 which will arise due to replacement demand, mainly due to retirement.

The City Council and partners remain focused on improving education and skill levels, investing in modern infrastructure, supporting (new) business formation and growth in key sectors, raising productivity, and strengthening place marketing in order to grow the visitor economy and attract inward investment. In all these areas the City Council remains committed to economic and social inclusion and tackling the underlying causes of poverty and disadvantage.

City Council finances: The Council, like all other local authorities across the country, has seen a substantial reduction in government funding as a consequence of the Government's policies to tackle the national fiscal deficit.

Over the last 5 years Nottingham has had to make annual savings to the total of **£152m**. This has been driven by the reduction in settlement funding and grant income over this period, whilst at the same time there has been increased demand for a number of services, most notably Adult Social Care and Children in Care which already account for **50%** of the Council's net budget. These increasing care pressures, alongside continuing funding cuts, will continue to have a significant impact on the Council's ability to fund other local services.

Table 1 summarises the **£152m** annual savings already delivered by the Council over the last five years (i.e. between 2011/12 and 2015/16) and the currently projected **£78m** savings that will be required to deliver balanced budgets between 2016/17 and 2019/20.

TABLE 1: BUDGET SAVINGS					
Financial Year	**New budgeted savings [A] £m**	**Continuing profile of previous savings £m**	**Projected MTFO gap £m**	**Annual total savings £m**	**Cumulative savings £m**
2011/12	(38.404)	(6.903)		(45.307)	
2012/13	(19.596)	(7.165)		(26.761)	
2013/14	(19.171)	(7.881)		(27.052)	
2014/15	(22.619)	(1.084)		(23.702)	
2015/16	(25.033)	(3.734)		(28.768)	**(151.589)**
2016/17	(20.826)	(8.016)	balanced budget	(28.841)	
2017/18		(3.777)	(23.347)	(27.124)	
2018/19		(3.370)	(10.793)	(14.163)	
2019/20		0.216	(7.927)	(7.710)	**(77.838)**

[A] as reported in the appropriate February Executive Board budget reports

In response to the current financial climate the Council continues to work with council networks including the LGA and the Special Interest Group of Municipal Authorities (SIGOMA) to campaign for a fairer funding settlement from central government for cities like Nottingham. As one of the ten Core Cities in the UK, the Council is campaigning for control over funding, programmes and policy to be devolved to cities to give us more freedom to grow our economy and reform our public services to get better outcomes for citizens.

Nationally and locally the economy has continued to show signs of a steady recovery in the past year, with an increase in the employment rate and significant fall in the number of people claiming out of work benefits, and whilst these continue to lag behind the national average the gap is narrowing. The most recent data shows higher than average growth in both the economy and wages in Nottingham in 2014 and 2015 although economic productivity, both locally and nationally, is yet to recover to pre-recession levels.

Central Government Funding

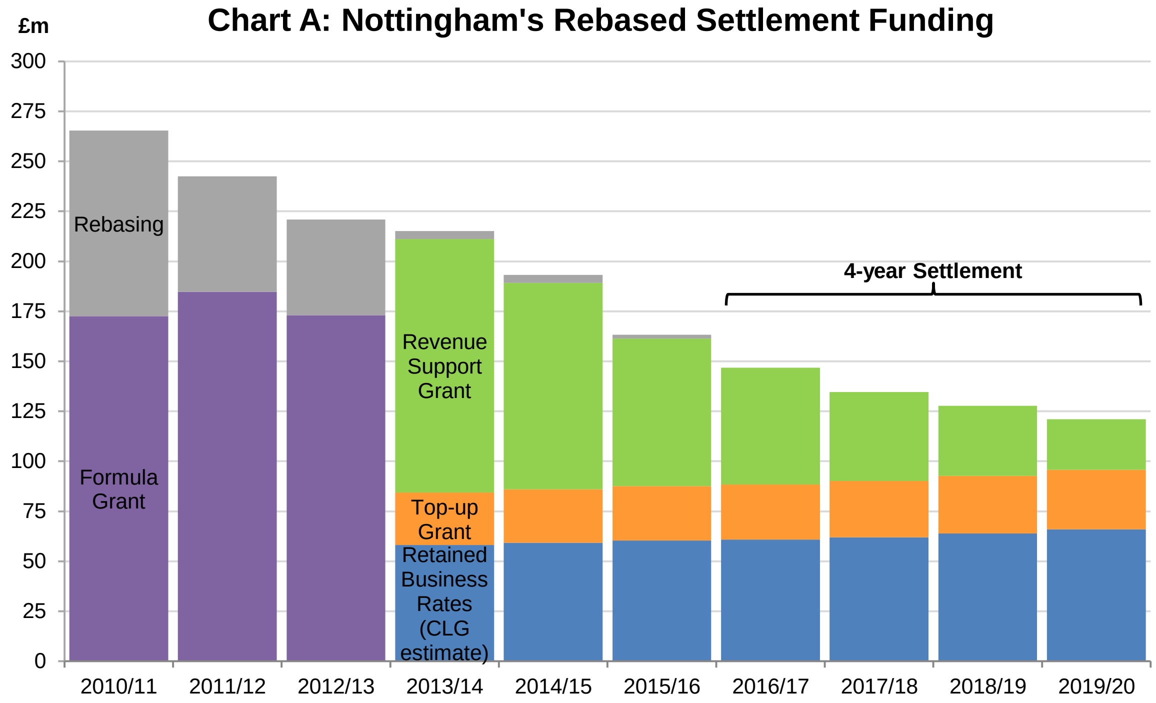
Between 2010/11 and 2016/17 the overall settlement funding for the Council, after taking account of transfers in funding and new burdens, has been reduced by the equivalent of **£119m** or **45%** with further significant cuts expected for 2017/18 and beyond as illustrated in **Chart A**.

Since 2013/14 and the introduction of the current settlement system of 50% locally retained business rates, Nottingham's Revenue Support Grant (RSG) has fallen **£68m** or **54%** by 2016/17.

The Government is offering a four year funding settlement to 2019/20 for any council that wishes to take it up. Their expectation is that the future funding certainty will enable more proactive planning of service delivery and will support strategic collaboration with local partners. Authorities will be required to publish an 'efficiency plan' setting out what further collaborative saving opportunities have been created with the acceptance of a multi-year settlement. Further details of the offer and the process for acceptance are expected from DCLG in the near future with a response deadline of 14 October 2016.

The proposed four year settlement assumes that RSG will continue to fall a further **£33m** or **57%** by 2019/20. This steep reduction in RSG will only be partially compensated by increasing retained business rates and council tax income.

By 2019/20 the assumed reduction in overall settlement funding since 2010/11 will be **£144m** or **54%**.

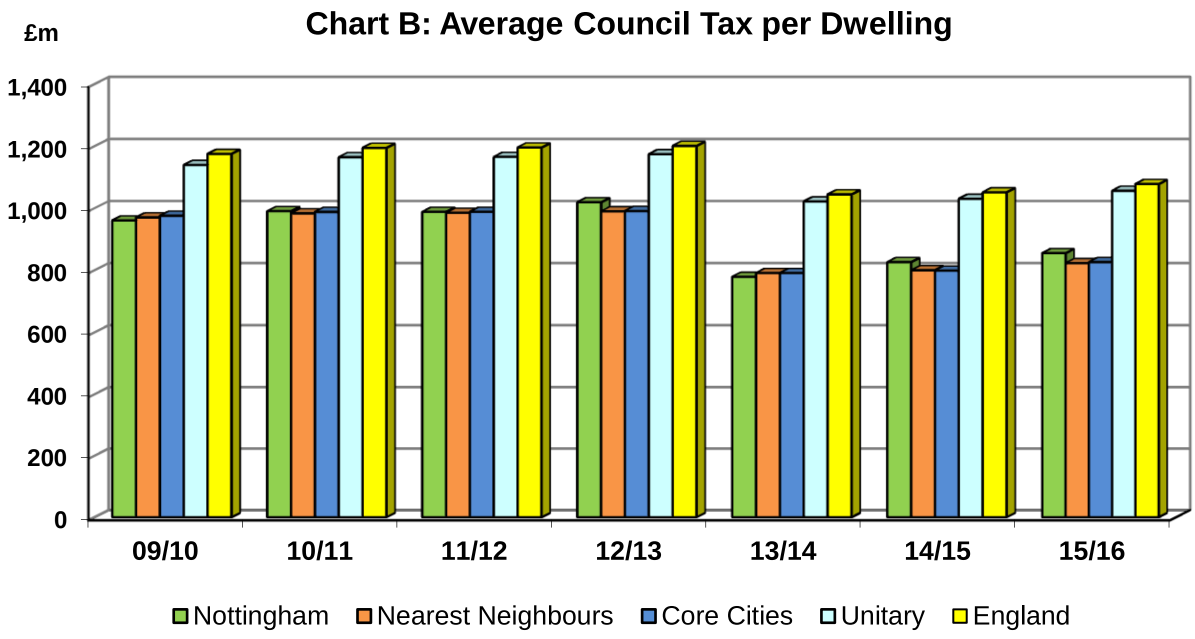


Council Tax

Council tax is a significant source of income. Decisions to make increases are based on a balanced consideration of the need to raise funds with the ability of local taxpayers to pay.
In recent years Nottingham's total Band D council tax (i.e. including all precepts) has consistently increased at a greater percentage rate than the average for its CIPFA classified nearest neighbours, other Core Cities and similar Unitary Authorities with the sole exception of 2011/12 when the Government introduced its Council Tax Freeze Grant (CTFG) to encourage authorities to freeze their council tax.

The benefit or dis-benefit of any increase or decrease in council tax impacts on the Council in perpetuity. For the last four years the Council has increased its Band D council tax and has not been in receipt of CTFG. Alternatively taking the available CTFG and freezing council tax over this period would have resulted in a requirement for an additional **£12.6m** cumulative savings.
Nottingham has a relatively high Band D due to its local tax base predominately consisting of properties in bands A and B (these make up **80.2%** of the **134,370** dwellings on the October 2015 valuation list) and the relatively high number of student properties excluded from council tax (**10,130** properties). As a consequence Nottingham has the 31st lowest average council per dwelling out of 326 billing authorities in England in 2015/16. **Chart B** illustrates the average council tax per dwelling against the key comparators.

The MTFS assumes that the City Council will continue to increase Council Tax within the referendum limits currently set by the Government (MTFP assumes 1.95% Council Tax increase per annum).



Cost of services

The City Council is budgeting to spend £837.5m on services in 2016/17 as shown in **Chart C**.

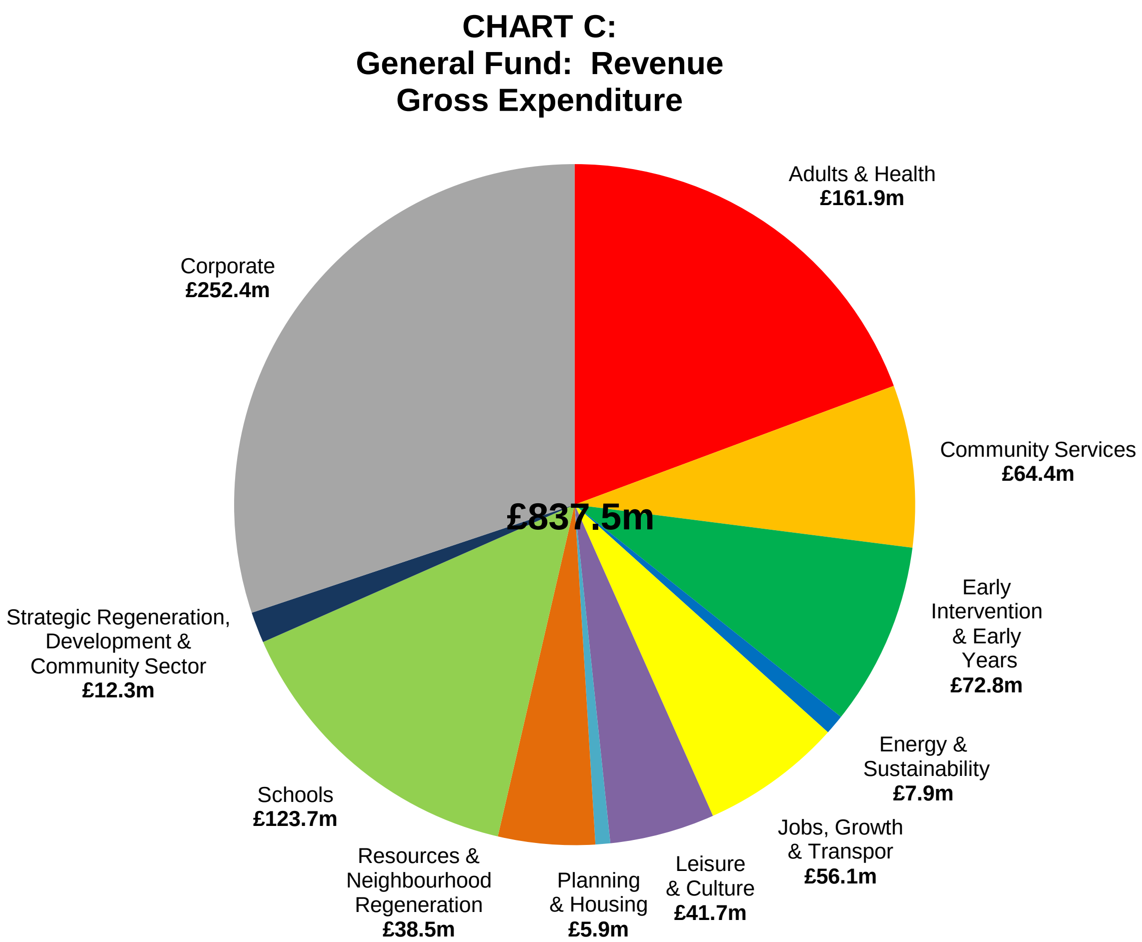
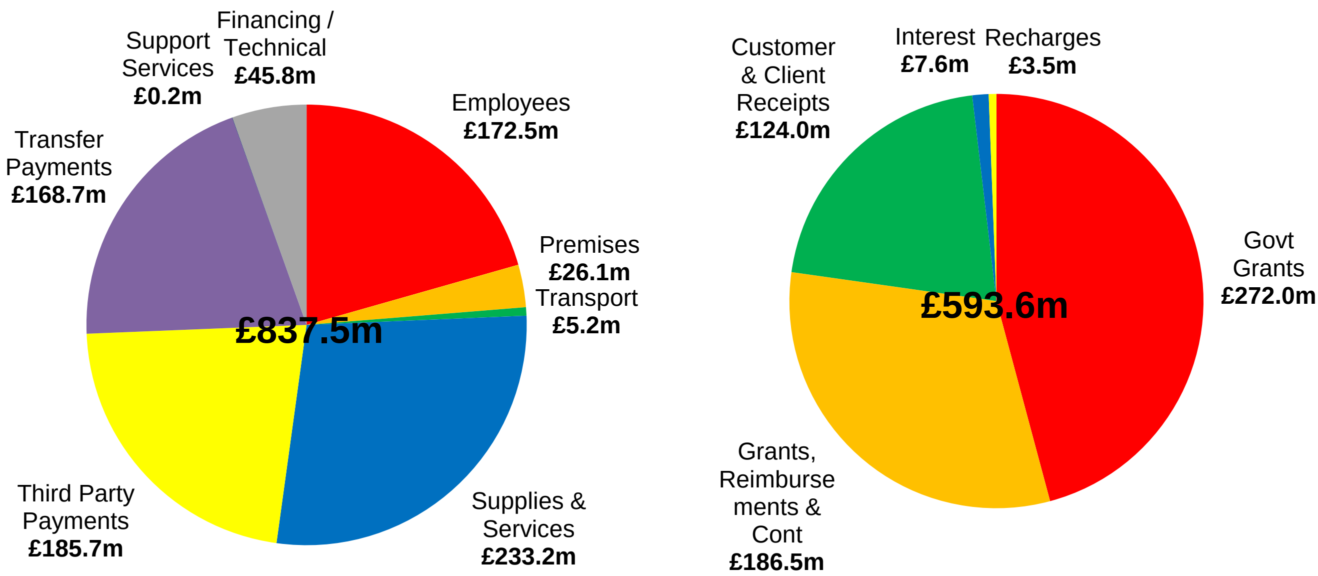


Chart D further shows how the gross expenditure is spent and the sources of income that fund these services. The net expenditure being financed through the Settlement funding and Council Tax.

CHART D: 2016/17 GENERAL FUND GROSS BUDGET AND INCOME



Devolution

Recognising devolution as a historic opportunity for the areas 2.2m citizens, Councils across Nottinghamshire and Derbyshire, along with the private sector led by D2N2, have come together as the 'North Midlands' to seek ground-breaking local control over powers and budgets that are currently held at the national level. The North Midlands is working hard to establish a brand new Combined Authority that will be amongst the largest in England with an economy larger than Northern Ireland.

The proposed governance for the new arrangements would result in:

- A single combined authority for Nottinghamshire and Derbyshire
- A single elected Mayor – first elections planned to be held in May 2017

In February 2016 the draft North Midlands Devolution Agreement was published. It includes proposals put forward by local councils for key areas where control and funding is to be transferred from central government to the new Mayor and combined authority covering:-

- Skills, apprenticeships and employment
- Housing and planning
- Transport

3. FINANCIAL FRAMEWORK

The financial framework is an integral part of the wider planning framework, and comprises a series of documents and processes which together facilitate our strategic financial planning and operational financial management. The financial framework has clear links to the various levels of service planning, risk management and performance management.

The financial framework is shown in **Table 2** includes four strands – strategies, guidance, plans and governance. Nottingham City Council has adopted the CIPFA / SOLACE Code of

Practice on governance and is committed to ensuring high standards are embraced by the organisation.

<table>
<tr><th colspan="6">TABLE 2: FINANCIAL FRAMEWORK</th></tr>
<tr><th>Category</th><th>Revenue</th><th>Capital</th><th>Treasury Management</th><th>Procurement</th><th>Risk Management</th></tr>
<tr><td rowspan="2">Strategies</td><td colspan="5">Medium Term Financial Strategy</td></tr>
<tr><td>Income and Debt Management Strategies</td><td>Capital and Asset Management Strategies</td><td>Treasury Management Strategy</td><td>Procurement Strategy</td><td>Risk Management Strategy</td></tr>
<tr><td rowspan="2">Guidance</td><td colspan="5">CIPFA and Technical Guidance</td></tr>
<tr><td colspan="2">Budget guidelines and Financial Management handbook</td><td>CIPFA Treasury Management Code</td><td>Procurement Toolkit</td><td>Risk Management Guides</td></tr>
<tr><td rowspan="2">Plans</td><td colspan="5">Medium Term Financial Plan</td></tr>
<tr><td>Annual Budget</td><td>Capital Programme & AMP</td><td>TM Plan</td><td>Procurement Plans</td><td>Risk Management Action Plans</td></tr>
<tr><td rowspan="5">Governance</td><td colspan="5">Constitution</td></tr>
<tr><td colspan="5">Financial Regulations and Standing Orders Relating to Contracts</td></tr>
<tr><td colspan="5">Annual Governance Statement</td></tr>
<tr><td colspan="5">Internal and External Audit Plans</td></tr>
<tr><td colspan="5">Professional advice and support from colleagues</td></tr>
</table>

The MTFS seeks to weave together the key components of the framework in order to fully understand the prevailing context and use that to develop a strategy for the short, medium and long term. The MTFP translates that strategy, as an integral part of the service planning process, into the financial plan that will support delivery of the Council’s objectives for the next four years.

The financial framework is supported by financial policies and practices that are key to ensuring robust financial decision making and strong governance. These policies and practices are contained within the Budget Guidelines and Financial Management Handbook. These policies are subject to regular review and any changes will be presented to Council for consideration.

Development of the MTFP

Revenue Budgets

The revenue element of the budget has been driven by the following:

- take account of the Council’s priorities within the Council Plan 2015/2019 agreed by City Council on 9 November 2015;
- address demographic and service pressures through investment;
- reflect the significant reductions in external funding (especially general and specific Government grants) by reducing expenditure on those activities;
- support the Council’s determination to be efficient, improve performance and modernise the organisation;

- recognise the very challenging financial landscape and future outlook and the impact on all sectors, including the Public Sector.

In addition, the Council's approach to setting recent budgets has, where possible, been guided by the following principles:

- to pursue commercialisation opportunities to generate income for the Council; and help offset a proportion of the impact of grant reductions;
- reducing demand and reviewing the way we commission our services;
- redesigning and modernising our service provision / identifying efficiencies;
- to protect frontline services and minimise the impact of service reductions and changes on vulnerable citizens

<u>Commercialism</u>

In recent years the Council has taken a more commercial perspective. The aim is to ensure all services are more 'business-like' in terms of the rigour and thought processes going into spending and pricing decisions. The aim is to understand and challenge what outcomes are being achieved for the inputs being put in and how the service is being delivered. This will mean different things for different service areas. For some areas this will mean breaking even or making a 'profit', for others it will mean clarity of the benefits for the level of spending and the impact of changing to other levels of spending. However, for all it will involve challenging why and how things are done, if they are needed on an ongoing basis, and if there are different, better ways of doing them in the future.

Commercialism does not presuppose a best way of working, however, different ways of working and their costs and benefits should be considered as part of the overall decision of service provision. Alternatives include:

- 'Traditional' budgeted provision
- Shared services
- Partnership working
- Trading units
- Arms-length companies
- Outsourcing (or purchasing from another public sector body)
- Insourcing (bringing procured services back in-house)
- Selling services to other public sector organisations (via any of the methods above) or to others

This approach has been successful and has been a key driver in preserving other services which may otherwise have been under increasing pressure to reduce costs given the reduction in overall Council funding. The commercialism agenda is an integral part of the future direction for the Council.

<u>Capital Budgets</u>

The Council has an ambitious approach to capital investment and consequently the programme includes substantial investments. The following key principles are adopted in managing the capital programme:

- where new projects are added to the programme that will not cover their costs, an existing project will be removed or amended;

- all projects must have a robust and viable business case, which considers and includes whole life costing and revenue implications (including rate of return);
- all schemes will be subject to robust and deliverable business plans and models which demonstrate the necessary return on investment required;
- all future schemes will need to address the consequences of cash flow shortfalls in the early years, and available funding must be identified and approved prior to the commencement of projects;
- the decision to progress schemes will be dependent on securing the stated level of external funding or grant as appropriate;
- new projects will be considered where the Council can make a return on investment;
- where new sources of external funding/grants become available, the programme will be revisited;
- all schemes will be subject to an independent internal 'Gateway Review Process'.

With respect to funding the capital programme the following considerations will be made with respect to this funding:

- the Council will endeavour to maximise grant funding for schemes which will assist in the delivery of the corporate priorities, part/full grant funded bids will be subject to the same prioritisation process;
- prudential or unsupported borrowing can be used where it can be demonstrated that it is affordable and sustainable in the medium term. Borrowing must be within approved limits and in accordance with the prevailing guidance in the Treasury Management Strategy;
- capital receipts generated from the sale of land, buildings and other assets will be a non-earmarked, council–wide resource, to be allocated according to Council priorities only after a thorough and objective options appraisal and consideration of opportunity costs, and not earmarked to a particular project, scheme, service, directorate and/or geographical area.

<u>HRA</u>

The HRA is the Council's landlord account, which provides for the management and maintenance of the Council's Housing stock. Legislation requires this account to be ring-fenced from the Council's other financial transactions. The budget has been set under the HRA self-financing system whereby the HRA is sustained from the rental income. The legislative framework is a key driver to the strategy around the HRA.

<u>Reserves</u>

A corporate financial risk assessment is undertaken to determine the key risks and their impact on the budget. This is used to inform the level of unearmarked reserves held within the overall context of the financial policy for reserves. Regular reviews are undertaken of all reserve balances to ensure that the purpose is still required.

4. SUMMARY MTFP

Medium Term Financial Plan (MTFP)

The MTFP projections, taking into account the 2016/17 and previously agreed saving proposals, confirm the need for on-going significant cost reductions in the short to medium

term to meet the continuing challenging budget position. Government funding to provide services will continue to decline while there are increasing demands on services. This will be the focus of budget planning in 2016.
If Nottingham chooses to follow the process towards accepting the Government's four year funding settlement the Council will be required to produce an 'efficiency plan' by 14 October 2016 setting out what further collaborative saving opportunities would be created with the acceptance of a multi-year settlement and the MTFP will be the starting point for this process.

Based on current best estimates it is projected that at least a further £42.1m savings will have to be identified by 2019/20, as shown in **Table 2**.

TABLE 2: MEDIUM TERM FINANCIAL PLAN				
DESCRIPTION	**2016/17 £m**	**2017/18 £m**	**2018/19 £m**	**2019/20 £m**
2015/16 Net Budget Requirement	255.814	255.814	255.814	255.814
Budget Refresh	4.564	12.288	18.032	21.454
New Pressures	4.325	10.039	15.686	18.460
SUB-TOTAL	**264.703**	**278.142**	**289.533**	**295.728**
Portfolio Proposals	(19.826)	(20.038)	(22.749)	(22.749)
Corporate Proposals	(1.000)	0.000	0.000	0.000
ASSUMED NET BUDGET	**243.878**	**258.104**	**266.783**	**272.979**
Retained Business Rates, Top-up & RSG	(148.201)	(136.063)	(129.261)	(122.625)
Council Tax	(94.212)	(98.694)	(103.383)	(108.288)
Collection Funds	(1.465)	0.000	0.000	0.000
ASSUMED FUNDING	**(243.878)**	**(234.757)**	**(232.644)**	**(230.913)**
NET MTFP POSITION	**0.000**	**23.347**	**34.139**	**42.066**

The MTFP projections assume the following key parameters:

- Band D council tax increases of 1.95% plus an additional 2.0% social care precept for all years
- Revenue Support Grant as announced in the Government's four year settlement offer
- No significant underlying growth in retained business rates over the immediate future years
- 1% pay award and appropriate general inflation for all years
- No further budget increases to meet demographic or service demand pressures beyond those already agreed
- New Homes Bonus estimates reduced to match key proposals proposed by Government for the reformed grant scheme
- If specific grant funding reduces then the associated expenditure and activity will reduce accordingly
- All existing saving proposals will be fully delivered

All these budget assumptions will be subject to ongoing review in light of changing circumstances. In particular funding projections will be updated to reflect the final results of the Government consultations on the New Homes Bonus grant and the proposed implementation of 100% locally retained business rates by 2019/20.
The MTFP projections can also be represented graphically as shown in **Chart E**.

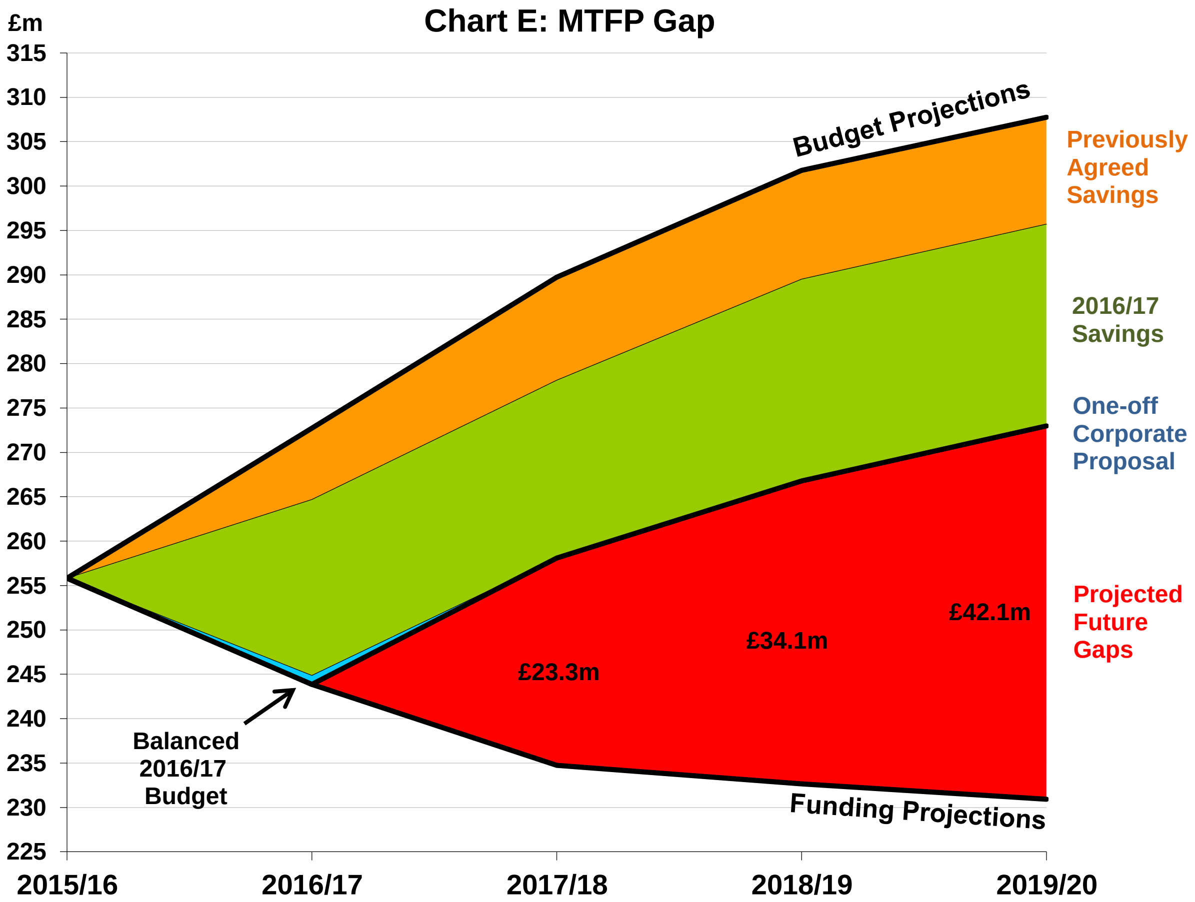


Chart E: MTFP Gap
£m
315
310
305
300
295
290
285
280
275
270
265
260
255
250
245
240
235
230
225
2015/16
2016/17
2017/18
2018/19
2019/20
Budget Projections
Funding Projections
Previously Agreed Savings
2016/17 Savings
One-off Corporate Proposal
Projected Future Gaps
£23.3m
£34.1m
£42.1m
Balanced 2016/17 Budget