Part B

Financial Performance Q2 2020/21

1.0 General Fund

1.1 General Fund performance of the quarter is shown in the table below:

Department	**Current Budget £'000**	**Profiled Budget £'000**	**Actual to 30th Sept 2020 £'000**	**Variance to date £'000**	**Q1 £'000**
SUMMARY					
Corporate Services	3,337	3,219	3,548	329	34
Service Delivery	5,876	3,195	4,203	1,008	439
Regeneration & Planning	(37)	(248)	222	470	43
Tourism & Enterprise	2,659	1,369	4,159	2,790	743
Total Service Expenditure	**11,835**	**7,535**	**12,132**	**4,597**	**1,259**
Covid-19	0	0	(177)	(177)	(413)
Contingencies & Corporate Savings	(599)	(375)	0	375	0
Capital Financing and Interest	2,286	1,141	1,141	0	5
Net Expenditure	**13,522**	**8,301**	**13,096**	**4,795**	**851**
			Income Recovery Claims Due*	***(1,500)***	
			Quarter 2 Variance	**3,295**	
			Quarter 1 Variance	*851*	
			Increase	***2,444***	

* *Note that the income recovery claim has been based on a prudent view of the amounts recoverable at this stage. Further work is required to ensure all current net losses are eligible for recovery in line with the guidance prior to the return being completed in December.*

1.2 The position at the end of September shows an initial deficit of £4.795m. However, the Council is still due money back from Government in respect of the Income Recovery Scheme (£1.5m), which would reduce the deficit down to £3.295m (Q1 £851k) on net expenditure. The main variances as at the end of September include:

Corporate Services		
Additional IT costs – software licences, network & equipment costs		£326k
Service Delivery		
Account & Case Management – mainly salary savings	(£78k)	
Housing Benefit Payments and Subsidy - mainly a shortfall in subsidy on emergency accommodation	£457k	
Waste Contract – delay in Trade Waste savings being achieved	£114k	
Revenues – no summons cost income	£244k	
Crematorium – reduction in income	£116k	
Car parks – mainly reduction in income	£166k	£1,019k

Regeneration & Planning Housing Delivery Team – feasibility work Corporate Landlord – mainly reduced rental income	 £155k £328k	 £483k
Tourism & Enterprise Redundancy costs Net income losses on facilities and events	 £508k £2,282k	 £2,790k
Covid-19: Direct costs incurred to date (food parcels, staffing, PPE etc) Emergency Grant received to date	 £1,104k (£1,281k)	 (£177k)
Contingencies & Savings – 6 months of corporate savings target relating to vacancy savings and staff reductions. The actual savings are contained within the relevant service areas.		£375k

1.3 Overall, the deficit has increased by just over £2.4m since Q1 to the current £3.3m position. This will inevitably increase as a result of the latest lockdown which will further impact on the recovery.

1.4 The Government announced a fourth tranche of emergency Covid-19 grant monies at the end of October, of which Eastbourne was allocated £474k. This is in addition to the £1.281m shown in the table above. This has not been included in the above figures as it is anticipated that it will be needed to cover future costs relating to homelessness and temporary accommodation.

1.5 In September, it was reported that the deficit was expected to be in the region of £8m for the current financial year and whilst this is a snapshot at the end of quarter 2 the position will worsen. If the current trajectory of losses continues into the second half of the year then the deficit could increase to £8.2m. Mainly as a result of the second lockdown and the impact this will have on income losses and continued cost pressures. Detailed 2020/21 revised and draft 2021/22 budgets are currently being prepared which will give a clearer picture.

2.0 HRA

2.1 HRA performance of the quarter is as follows:

	Full Year Budget **£'000**	**Profiled Budget** **£'000**	**Actual to 30 June 2020** **£'000**	**Variance to date** **£'000**
HRA				
Income	(15,473)	(7,737)	(7,737)	-
Expenditure	13,501	6,804	6,703	(101)
Capital Financing & Interest	1,897	949	949	-
Contribution to Reserves	3,656	1,828	1,828	-
Total HRA	**3,581**	**1,844**	**1,743**	**(101)**

There is a positive variance of £101,000 at the end of quarter 2 (Q1 £33k). The main variance relates to a £70k underspend on the management fee. A further breakdown is shown at **Appendix 2**.

3.0 Capital Expenditure

3.1 The detailed capital programme at **Appendix 3,** provides a summary of spend for quarter 2 compared to the revised allocation for 2020/21 and the total spend for each scheme as at 30 September. Current spend totals £3.465m against an overall budget of £54.830m. Comments are provided for each scheme in the appendix.

4.0 Collection Fund

4.1 The Collection Fund records all the income from Council Tax and Non-Domestic Rates and its allocation to precepting authorities.

4.2 The Collection fund for the year is as follows:

	Council Tax £'000	**Business Rates £'000**
(Surplus)/Deficit Brought Forward 01 April 2020	**(208)**	**331**
Total Collectable Income for year*	(70,975)	(11,095)
Payments to Preceptors	71,543	37,467
Write offs, provisions for bad debts and appeals	673	585
Additional Business Rate Reliefs – as a result of Covid-19	-	(23,728)
Estimated Balance 31 March 2021 – (Surplus) / Deficit	**1,033**	**3,560**
Allocated to:		
Government	-	1,780
East Sussex County Council	756	320
Eastbourne Borough Council	127	1,424
Sussex Police	101	-
East Sussex Fire & Rescue	49	36
	1,033	**3,560**

* *This represents the latest total amount of income due for the year and allows for changes as a result of discounts, exemptions and reliefs, as well as increases in the Council Tax and Business Rate bases.*

4.3 The allocation to preceptors reflects the operation of the Collection Fund for Council Tax and Business Rates which are distributed on different bases under regulations. The distributions for the estimated balance calculated at quarter 3 will be made in 2021/22.

4.4 Council Tax is showing a deficit of £1.033m for the quarter (Qtr1 £1.792m), which is an improvement of £759k. However, this still represents an in-year deficit of £1.241m as there was a surplus of £208k brought forward from the previous year. The Council's share of the overall forecast deficit is £127k. The position continues to be monitored on a monthly basis and the final surplus or deficit will be formally set in January 2021. It should be noted that, should the position change, under new accounting regulations brought in by Government in response to Covid-19, deficits can be spread over three financial years from 2021-2024.

4.5 There is a Business Rates deficit of £3.560m at the end of September (Q1 £1.511m), which is an increase of £2m. This represents an in-year deficit of £3.229m as there was a deficit of £331k brought forward from the previous year. There continues to be a significant risk associated with business rate income, despite the additional business rate reliefs (£24m) that have been given by Government. The latest deficit would be split between the relevant preceptors with Eastbourne's share equating to £1.424m. This would be spread over the following three financial years. The exact surplus or deficit position will be determined in January 2021.

5.0 Treasury Management

5.1 The Annual Treasury Management and Prudential Indicators were approved by Cabinet and Council in February.

5.2 Annual Investment Strategy

The Treasury Management Strategy Statement (TMSS) for 2020/21 which includes the Annual Investment strategy, was approved by the Full Council on Wednesday, 19th February. It sets out the Council's investment priorities as being:

- Security of Capital;
- Liquidity;
- Yield.

There were no short term investments held as at 30 September. Approved limits within the Annual Investment Strategy were not breached during the quarter ending 30 September 2020, except for the balance held with Lloyds Bank, which exceeded the £5m limit for 9 days during the quarter. Investment rates available in the market have continued at historically low levels. Investment funds are available on a temporary basis and arise mainly from the timing of the precept payments, receipts of grants and the progress of the capital programme.

As shown by the interest rate forecasts, it is now impossible to earn the level of interest rates commonly seen in previous decades as all investment rates are barely above zero now that Bank Rate is at 0.10%, while some entities, including more recently the Debt Management Account Deposit Facility (DMADF), are offering negative rates of return in some shorter time periods. Given this risk environment and the fact that increases in Bank Rate are unlikely to occur before the end of the current forecast horizon of 31st March 2023, investment returns are expected to remain low.

5.3 Negative investment rates

While the Bank of England has said that it is unlikely to introduce a negative Bank Rate, at least in the next 6 -12 months, some deposit accounts are already offering negative rates for shorter periods. As part of the response to the pandemic and lockdown, the Bank and the Government have provided financial markets and businesses with plentiful access to credit, either directly or through commercial banks. In addition, the Government has provided large sums of grants to local authorities to help deal with the

Covid crisis; this has caused some local authorities to have sudden large increases in investment balances searching for an investment home, some of which was only very short-term until those sums were able to be passed on.

As for money market funds (MMFs), yields have continued to drift lower. Some managers have suggested that they might resort to trimming fee levels to ensure that net yields for investors remain in positive territory where possible and practical. Investor cash flow uncertainty, and the need to maintain liquidity in these unprecedented times, has meant there is a glut of money swilling around at the very short end of the market. Inter-local authority lending and borrowing rates have also declined due to the surge in the levels of cash seeking a short-term home at a time when many local authorities are probably having difficulties over accurately forecasting when disbursements of funds received will occur or when further large receipts will be received from the Government.

5.4 Investment performance for the quarter ending 30 September is as follows:

Benchmark	Benchmark Return	Council Performance	Interest Earning
7 day LIBID	-0.06%	0.03%	£1,096.22

The Council outperformed the benchmark by 0.09%. The budgeted investment return for 2020/21 is £50,000. Due to cash flow requirements and current low interest rates, investments held are at minimum and it is unlikely that this budget will be achieved, but this will be offset by reduced borrowing.

The continuous use of internal balances is in line with the Council’s strategy and reduces the amount of interest payable on loans and investment income.

5.5 **Borrowing**

The following loan was taken during the quarter:

New Short Term Borrowing – there was no new borrowing for quarter 2				
Start Date	Counterparty	Amount	Interest Rate %	End Date
Total		**0.0**	**-**	**-**
Less Short Term Borrowing Repaid				
Repayment Date	Counterparty	Amount	Interest Rate	No of Days
07-07-20	East Riding of Yorkshire Pension Fund	10.0	0.95	113
Total		**10.0**	**-**	**-**
Net New Short Term Borrowing during quarter		**(10.0)**	**-**	**-**

Cash flow predictions indicate that further borrowing will be required in the next quarter, depending on the timing of capital expenditure. The exact timing and nature of this borrowing will be considered at that time in light of prevailing interest rates.

5.6 **Interest Rate Forecast**

The Council's treasury advisor, Link Group, provided the following forecasts on 11 August 2020:

Link Group Interest Rate View 11.8.20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23
Bank Rate View	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
3 month average earnings	0.05	0.05	0.05	0.05	0.05	0.05	-	-	-	-	-
6 month average earnings	0.10	0.10	0.10	0.10	0.10	0.10	-	-	-	-	-
12 month average earnings	0.15	0.15	0.15	0.15	0.15	0.15	-	-	-	-	-
5yr PWLB Rate	1.90	1.90	2.00	2.00	2.00	2.00	2.00	2.10	2.10	2.10	2.10
10yr PWLB Rate	2.10	2.10	2.10	2.10	2.10	2.20	2.20	2.20	2.30	2.30	2.30
25yr PWLB Rate	2.50	2.50	2.50	2.50	2.60	2.60	2.60	2.70	2.70	2.70	2.70
50yr PWLB Rate	2.30	2.30	2.30	2.30	2.40	2.40	2.40	2.50	2.50	2.50	2.50

The above table is based on PWLB certainty rates – gilt yields plus 180bps.

The coronavirus outbreak has done huge economic damage to the UK and to economies around the world. After the Bank of England took emergency action in March to cut Bank Rate to first 0.25%, and then to 0.10%, it left Bank Rate unchanged at its last meeting, although some forecasters had suggested that a cut into negative territory could happen. However, the Governor of the Bank of England has made it clear that he currently thinks that such a move would do more damage than good and that more quantitative easing is the favoured tool if further action becomes necessary. As shown in the forecast table above, no increase in Bank Rate is expected within the forecast horizon ending on 31st March 2023 as economic recovery is expected to be only gradual and, therefore, prolonged.

While inflation targeting by the major central banks has been successful over the last 30 years in lowering inflation expectations, the real equilibrium rate for central rates has fallen considerably due to the high level of borrowing by consumers. This means that central banks do not need to raise rates as much now to have a major impact on consumer spending, inflation, etc. The consequence of this has been the gradual lowering of the overall level of interest rates and bond yields in financial markets. Over the year prior to the coronavirus crisis, this has seen many bond yields up to 10 years turn negative in the Eurozone. In addition, there has, at times, been an inversion of bond yields in the US whereby 10 year yields have fallen below shorter term yields. In the past, this has been a precursor of a recession. The other side of this coin is that bond prices are elevated as investors would be expected to be moving out of riskier assets i.e. shares, in anticipation of a downturn in corporate earnings and so selling out of equities.

Gilt yields had, therefore, already been on a generally falling trend up until the coronavirus crisis hit western economies during March. At the close on 30th September, all gilt yields from 1 to 6 years were in negative territory, while even 25-year yields were only at 0.76% and the 50 year at 0.60%.

From the local authority borrowing perspective, HM Treasury imposed **two changes of margins over gilt yields for PWLB rates** in 2019-20 without any prior warning. The first took place on 9th October 2019, adding an additional 1% margin over gilts to all PWLB period rates. That increase was then, at least partially, reversed for some forms of borrowing on 11th March 2020, but not for mainstream non-HRA capital schemes. At the same time the Government announced in the Budget a programme of increased infrastructure expenditure.
It also announced that there would be a consultation with local authorities on possibly further amending these margins; the HM Treasury consultation was initially due to end on 4th June, but that date was subsequently put back to 31st July. To date, the outcomes of the consultation have yet to be announced but it is clear that HM Treasury will most likely no longer allow local authorities to borrow money from the PWLB to purchase commercial property if the primary aim is to generate an income stream (assets for yield).

Following the changes on 11th March 2020 in margins over gilt yields, the current situation is as follows: -

- **PWLB Standard Rate** is gilt plus 200 basis points (G+200bps)
- **PWLB Certainty Rate** is gilt plus 180 basis points (G+180bps)
- **PWLB HRA Standard Rate** is gilt plus 100 basis points (G+100bps)
- **PWLB HRA Certainty Rate** is gilt plus 80bps (G+80bps)
- **Local Infrastructure Rate** is gilt plus 60bps (G+60bps)

It is possible that the non-HRA Certainty Rate will be subject to revision downwards after the conclusion of the HM Treasury consultation; however, the timing of such a change is currently an unknown, although it would be likely to be within the current financial year.

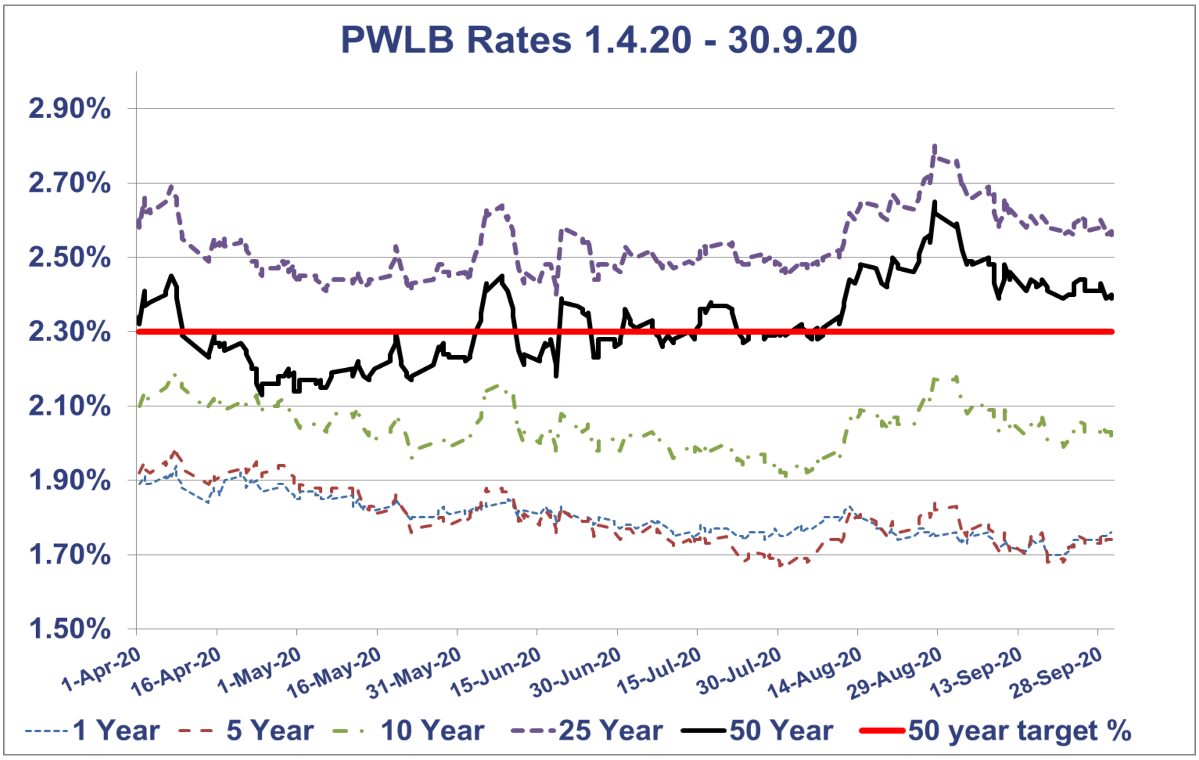
As the interest forecast table for PWLB certainty rates, (gilts plus 180bps), above shows, there is likely to be little upward movement in PWLB rates over the next two years as it will take economies, including the UK, a prolonged period to recover all the momentum they have lost in the sharp recession caused during the coronavirus shut down period. Inflation is also likely to be very low during this period and could even turn negative in some major western economies during 2020/21.

5.7 **Debt Rescheduling**

Debt rescheduling opportunities have been limited in the current economic climate and following the various increases in the margins added to gilt yields which has impacted PWLB new borrowing rates. During the quarter ended 30 September 2020, no debt rescheduling was undertaken.

5.8 **PWLB maturity certainty rates (gilts plus 180bps) year to date to 30th September 2020**
There has not been a great deal of volatility in PWLB rates since the start of the financial year, apart from a more significant spike up during the second half of August into early September. The 50 year PWLB target rate for new long term borrowing was unchanged at 2.30%.

Year to 30th September 2020



	1 Year	5 Year	10 Year	25 Year	50 Year
Low	1.70%	1.67%	1.91%	2.40%	2.13%
Date	18/09/2020	30/07/2020	31/07/2020	18/06/2020	24/04/2020
High	1.94%	1.99%	2.19%	2.80%	2.65%
Date	08/04/2020	08/04/2020	08/04/2020	28/08/2020	28/08/2020
Average	1.80%	1.80%	2.04%	2.54%	2.33%

5.9 **Compliance with Treasury and Prudential Limits**

It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. The Council's approved Treasury and Prudential Indicators (affordability limits) are included in the approved TMSS.

During the quarter to 30 September the Council has operated within the treasury limits and Prudential Indicators set out in the Council's Treasury Management Strategy Statement and in compliance with the Council's Treasury Management Practices, except for temporary balances exceeding limits with Lloyds Bank.

5.10 **Climate change and environmental implications**

Treasury management is a Council-wide function and its climate change, environmental and sustainability implications are the same as for the Council itself. The Council and its TM Advisors will have regard to the environmental activities of its Counterparties (where reported) but: -

Prioritises Security, Liquidity and Yield,

Recognises that as large, global institutions our high-quality counterparties operate across the full range of marketplaces in which they are legally able to, and as a result climate change considerations are an increasingly important and heavily-scrutinised part of their overall business.

Excluding any one counterparty will likely mean others will similarly have to be avoided and thus impact the Council's capacity to mitigate risk through diversification.

5.11 **Covid-19 crisis**

As the Council's borrowing rates are directly linked to market expectations this gives rise to the potential that our borrowing rates will remain close to all-time lows for some time. With the Council's Capital Programme and re-financing commitments over the next few years, our ability to secure good value in our borrowing has significant implications for the spending plans of Council as a whole. This ability will be affected by the outcome of the current consultation by Public Works Loan Board (PWLB) on how it offers debt to the sector. Potentially this may mean some reversal of the PWLB's 1% margin hike imposed in October 2019. At the time of writing any such reversal is by no means certain and so our central borrowing strategy remains one of undertaking regular transactions in order to lock in current rates to fulfil our long-term borrowing requirement. Timing will be managed through a portfolio of short-term debt and we will seek to add new sources of borrowing while PWLB's margin remains competitive.

5.12 **Economic Background**

As expected, the Bank of England's Monetary Policy Committee kept Bank Rate unchanged on 6th August (and subsequently 16th September). It also kept unchanged the level of quantitative easing at £745bn. Its forecasts were optimistic in terms of three areas:

- The fall in **GDP** in the first half of 2020 was revised from 28% to 23% (subsequently revised to -21.8%). This is still one of the largest falls in output of any developed nation. However, it is only to be expected as the UK economy is heavily skewed towards consumer-facing services – an area which was particularly vulnerable to being damaged by lockdown.
- The peak in the **unemployment rate** was revised down from 9% in Q2 to 7½% by Q4 2020.
- It forecast that there would be excess demand in the economy by Q3 2022 causing CPI **inflation** to rise above the 2% target in Q3 2022, (based on market interest rate expectations for a further loosening in policy). Nevertheless, even if the Bank were to leave policy unchanged, inflation was still projected to be above 2% in 2023.

It also squashed any idea of using **negative interest rates**, at least in the next six months or so. It suggested that while negative rates can work in some circumstances, it would be "less effective as a tool to stimulate the economy" at this time when banks are worried about future loan losses. It also has "other instruments available", including QE and the use of forward guidance. The MPC expected the £300bn of **quantitative**

easing purchases announced between its March and June meetings to continue until the "turn of the year". This implies that the pace of purchases will slow further to about £4bn a week, down from £14bn a week at the height of the crisis and £7bn more recently.

In conclusion, this would indicate that the Bank could now just sit on its hands as the economy was recovering better than expected. However, the MPC acknowledged that the "medium-term projections were a less informative guide than usual" and the minutes had multiple references to **downside risks,** which were judged to persist both in the short and medium term. One has only to look at the way in which second waves of the virus are now impacting many countries including Britain, to see the dangers.

However, rather than a national lockdown, as in March, any spikes in virus infections are now likely to be dealt with by localised measures and this should limit the amount of economic damage caused. In addition, Brexit uncertainties ahead of the year-end deadline are likely to be a drag on recovery. The wind down of the initial generous furlough scheme through to the end of October is another development that could cause the Bank to review the need for more support for the economy later in the year. Admittedly, the Chancellor announced in late September a second six month package from 1 November of government support for jobs whereby it will pay up to 22% of the costs of retaining an employee working a minimum of one third of their normal hours.

There was further help for the self-employed, freelancers and the hospitality industry. However, this is a much less generous scheme than the furlough package and will inevitably mean there will be further job losses from the 11% of the workforce still on furlough in mid-September.

Overall, **the pace of recovery** is not expected to be in the form of a rapid V shape, but a more elongated and prolonged one after a sharp recovery in June through to August which left the economy 11.7% smaller than in February. The last three months of 2020 are now likely to show no growth as consumers will probably remain cautious in spending and uncertainty over the outcome of the UK/EU trade negotiations concluding at the end of the year will also be a headwind. If the Bank felt it did need to provide further support to recovery, then it is likely that the tool of choice would be more QE.

There will be some **painful longer term adjustments** as e.g. office space and travel by planes, trains and buses may not recover to their previous level of use for several years, or possibly ever. There is also likely to be a reversal of globalisation as this crisis has shown up how vulnerable long-distance supply chains are. On the other hand, digital services are one area that has already seen huge growth.

One key addition to **the Bank's forward guidance** was a new phrase in the policy statement, namely that "it does not intend to tighten monetary policy until there is clear evidence that significant progress is being made in eliminating spare capacity and achieving the 2% target sustainably". That seems designed to say, in effect, that even if inflation rises to 2% in a couple of years' time, do not expect any action from the MPC to raise Bank Rate – until they can clearly see that level of inflation is going to be persistently above target if it takes no action to raise Bank Rate

The **Financial Policy Committee** (FPC) report on 6th August revised down their expected credit losses for the banking sector to "somewhat less than £80bn". It stated that in its assessment "banks have buffers of capital more than sufficient to absorb the losses that are likely to arise under the MPC's central projection". The FPC stated that for real stress in the sector, the economic output would need to be twice as bad as the MPC's projection, with unemployment rising to above 15%.

EU. The economy was recovering well towards the end of Q2 after a sharp drop in GDP, (e.g. France 18.9%, Italy 17.6%). However, the second wave of the virus affecting some countries could cause a significant slowdown in the pace of recovery, especially in countries more dependent on tourism. The fiscal support package, eventually agreed by the EU after prolonged disagreement between various countries, is unlikely to provide significant support and quickly enough to make an appreciable difference in weaker countries. The ECB has been struggling to get inflation up to its 2% target and it is therefore expected that it will have to provide more monetary policy support through more quantitative easing purchases of bonds in the absence of sufficient fiscal support.

World growth. Latin America and India are currently hotspots for virus infections. World growth will be in recession this year. Inflation is unlikely to be a problem for some years due to the creation of excess production capacity and depressed demand caused by the coronavirus crisis.