APPENDIX 1

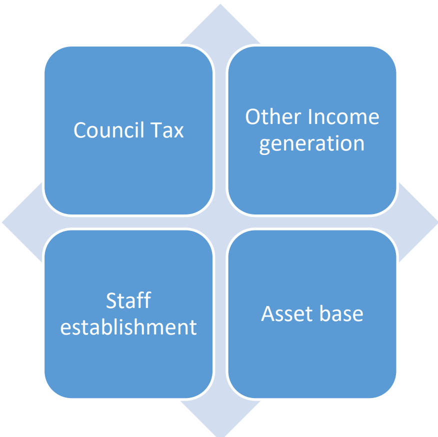
Medium to Long Term Financial Strategy

1. Background

1.1 On 1 March 2023 the Council set a balanced one year revenue budget for 2023/24. In doing so, it was acknowledged that based on current assumptions at that time, significant funding gaps existed in future years. In order to balance the budget the total anticipated savings required were £19.84m in 2024/25 and £1.06m in 2025/26.

1.2 Significant use of reserves was planned to balance the budget in 2023/24. This is not a sustainable position. Using reserves to avoid cuts in the short-term will only provide temporary relief. The Council faces two challenges: to remove the reliance on reserves (the structural or underlying deficit in funding) and to contain budget pressures from increased demand in services and/or inflation.

1.3 The Short to Medium Term Financial Strategy, approved by Council on 27 September 2023, sets out a strategy to remove the structural deficit by 2025/26. It includes the financial levers in the diagram below. - These levers are the key to both the short to medium and medium to long term financial strategies of the Council. The movement from each of these levers impacts on the required movement from the others in order to get a sustainable, balanced budget.



1.4 This Medium to Long Term Financial Strategy builds on the Short to Medium Term Financial Strategy and extends the financial planning time frame to 10 years. Characteristics of financial planning horizons in the Short, Medium and Long term are set out in the table below.

	Short Term	**Medium Term**	**Long Term**
Nature	Budget	Financial Plan	Financial Strategy
Timeframe	Annual	2-5 years	3-10 years +
Focus	Accountability	Performance	Transformation
Unpredictability	Risk	Risk/Uncertainty	Uncertainty
Financial Techniques	Estimating	Forecasting	Scenario Planning
Level of Detail	High	Medium	Low

1.5 The Medium to Long Term Financial Strategy (MLTFS) is an important part of the financial planning process. It reinforces the longer term sustainability of the Council by ensuring that the financial commitments required for good quality services are sustainable within a changing economic outlook over the next 3-10 years.

1.6 The strategy makes a number of key assumptions and, while it is recognised that future projections covering a 10 year period will contain some degree of uncertainty, these assumptions are clearly laid out below. In doing this, the Council has reviewed a range of possible outcomes with an optimistic (i.e. a positive for the Council budget), pessimistic (negative position for the Council) and mid-range scenario. It is assumed that the mid-range scenario will be taken as the most likely outcome.

1.7 The strategy places a lot of weight on achieving strategic and significant cost-cutting/savings proposals, concurrent with the Council's priorities within the Corporate Plan. The intended outcome of the financial strategy is a sustainable financial plan, with planned revenue expenditure met by budgeted revenue income, with use of reserves to balance the budget kept to a minimum and targeted towards transformation of council services.

1.8 The strategy covers the period 2024/25 to 2033/34 with 2023/24 as base year. The main focus is on 2026 onwards as the Short to Medium Term Financial Strategy covers years 1 and 2 and is more detailed than this high level Strategy. It will:

- Highlight the key influences, risks and cost drivers for the Council's service delivery
- Outline the Council's high level position over the years 2024/25 to 2033/34
- Facilitate planning ahead to enable the impact of change to be managed more proactively and effectively
- Plan for a sustainable revenue budget and capital investment programme which will support the Council's priorities and address the key issues for Moray
- Assist in increasing the people of Moray's understanding of the Council's financial position and the challenges facing it over the next ten years.

1.9 This Strategy sets out the financial roadmap for the Council for the medium to long term and gives background to the various financial pressures and drivers that will impact on the wider economy, and the communities in Moray. It will be reviewed no less than annually as part of the Council's financial planning process, with updates of the short-medium term position reported to Corporate Management Team and Corporate Committee on a regular basis. The inclusion of information in the Strategy does not imply approval. All financial estimates are subject to approval by Council as part of the budget setting process.

1.10 The scope of this Financial Strategy is the Council's General Fund. The Council's Housing Revenue Account (HRA) is ring-fenced, according to statutory requirements, and consequently financial planning for the HRA is a separate exercise.

1.11 The Medium to Long Term Financial Strategy forms part of a suite of documents used in the Council's financial planning, alongside:

- the Council's Corporate Plan

- the three year budget reported when the budget for the year is set and regularly updated in reports to the Council
- the indicative 10 year Capital Plan, underpinned by the Council's Capital Strategy
- the Council's Reserves Policy
- the Council's Charging Policy
- the Treasury Management Policy
- the Short to Medium Term Financial Strategy

2. Key Influences

2.1 In May 2023 the Scottish Government published its updated Medium-Term Financial Strategy. While this does not replace the Scottish Budget, it addresses Scotland's economic outlook for the period 2023/24 to 2027/28 and provides a useful awareness of estimated future funding and spending priorities at national level. A key point from the document is that "Economic conditions in Scotland and the UK continue to remain challenging as inflationary pressures continue to create a cost of living crisis for households and businesses across the country and increase pressures on public services." The Council's MLTFS will take on board some of the key influences and risks included in the Scottish Government's strategy and apply to its own position.

2.2 External influences outwith the Council's control include economic changes, such as:

- Rate of Inflation
- Interest rate fluctuations
- Level of grant funding from the Scottish Government
- Pay agreements

2.3 Climate related issues:

- Climate change – Council's policy
- Flooding
- Storm damage
- Winter maintenance

2.4 Internal Influences

- Corporate priorities
- Transformation of services
- Asset Management of the Council's schools and other properties
- Participatory Budgeting, commitment to giving communities the influence on decisions for 1% of the Council's budget
- Affordability and sustainability of the Council's revenue and capital programme

2.5 These are key variables that influence the financial planning of the Council and, while not an exhaustive list, these will be measured using a scenario basis that can be routinely updated to keep assumptions in line with the economic outlook. In doing so this ensures that the Council continues to meet its statutory obligations in line with its corporate policies. The key variables to be used are:

- Inflation, including pay awards
- Anticipated Scottish Government funding

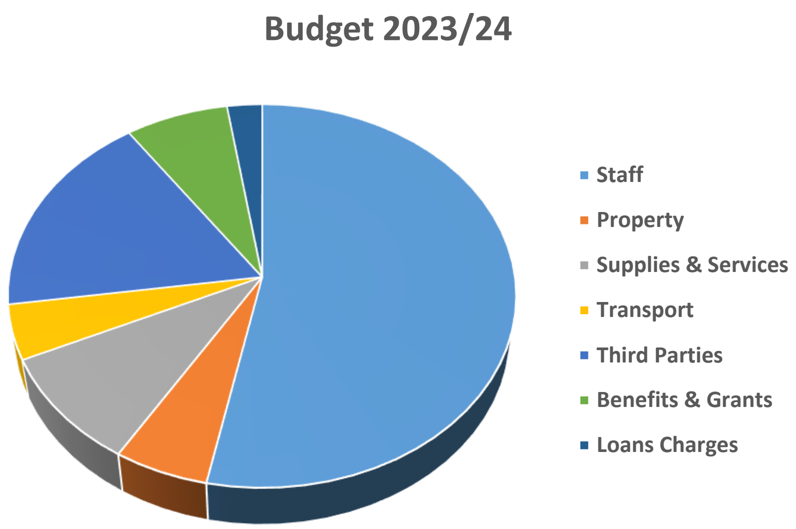
- Council Tax income
- Interest Rates and Loans Charges
- Increased demand for services
- Savings from Transformational change

3. Cost Drivers

3.1 The Council's budget of £348 million gross revenue expenditure for 2023/24 includes £185 million for staff. Pay awards and pension costs are key cost drivers for the Council. Pay awards for 2023/24 have not yet been agreed for non-teaching staff, and with the most recent negotiations at higher than the Council has budgeted for this year, any further increases will have a substantial effect on current and future years financial planning.

3.2 A significant proportion of the Council's services are out-sourced, with 18% of the Council's expenditure being on services delivered by third parties. The procurement process therefore has a strong influence on the costs borne by the Council and significant savings have been made by procurement on the purchase of supplies and services as well as on out-sourced services.

3.3 The split of the Council budget is shown below.



Medium to Long Term Financial Strategy

4. Sensitivity Analysis and Budget Assumptions

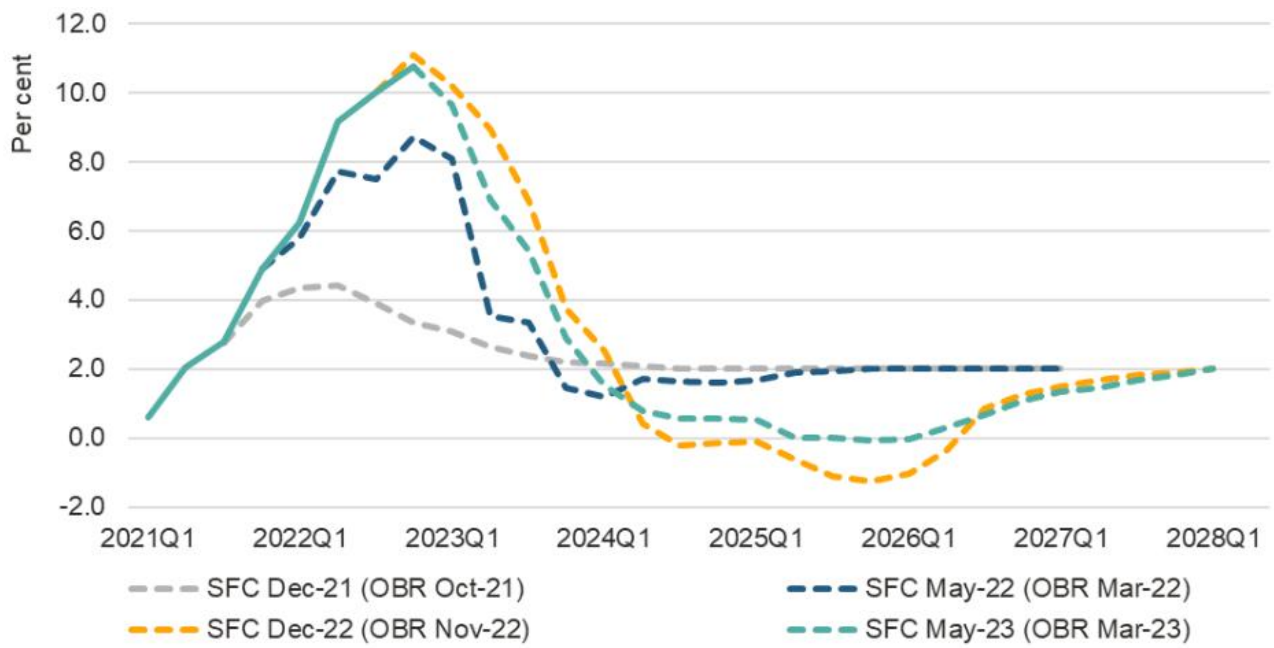
4.1 Key budget assumptions are set out below, showing the scenario and what impact that variation has on budget projections for each of the next three years, as well as years 4 to 10 together.

5. Inflation

5.1 Cost pressures arise from the Council's contractual obligations which are uplifted for inflation. Such inflationary uplifts are difficult to forecast as a result of uncertainties in the economy and how effective attempts by the Bank of England at reducing inflation will be, especially within the projected timescales. Inflation affects a small number of significant contracts – in particular the PPP schools contract – and also covers potential increases in utilities; energy prices have been one of the main forces in driving inflation levels in recent years. The cost of utilities and fuel has been volatile over the past couple of years, with additional budget pressures identified for these areas.

5.2 The outlook for inflation remains a key source of uncertainty yet has a crucial influence in long term financial planning, particularly around pay and core contract inflations increases that are often linked to, or kept as closely aligned as possible, to inflation.

5.3 The Scottish Fiscal Commissions (SFC) are a non-Ministerial Office who produce Scotland's official, independent economic and fiscal forecasts to accompany the Scottish Government's Budget cycle, and who are accountable to the Scottish Parliament for their functions (set out in the Scottish Fiscal Commission Act 2016), reporting twice a year. The Office for Budget Responsibility (OBR), an official independent fiscal watchdog that produces detailed forecasts for the economy and public finances, also provide UK Government with forecast data. Both bodies expected Consumer Price Index (CPI) inflation to have peaked in the fourth quarter of 2022 before beginning its descent. The SFCs most recent forecast in May 2023 indicates a sharp decline in the rate of inflation in 2023. Inflation is expected to fall rapidly, reaching 0% from mid-2024 to mid-2026 as energy bills fall back and supply issues reverse. Inflation is then expected to return to the Treasury's 2% target thereafter for the remainder of the ten year outlook as the diagram below shows.



Solid lines refer to outturn available at time of publication and dashed lines refer to forecasts.
Source: [Scottish Fiscal Commission]
Office for Budget Responsibility (OBR) "Long term economic determinants – March 2023 Economic and fiscal outlook" published in June 2023 https://obr.uk/data/

Forecasts for Inflation (CPI, year on year)

5.4 The latest published CPI inflation forecasts from the OBR are:

	2023/24	2024/25	2025/26	2026/27	2027/28	2028/29	2029/30	2030/31	2031/32	2032/33	2033/34
Inflation (Consumer Price Index (CPI))	4.1%	0.6%	0.0%	0.8%	1.7%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%

5.5 When the budget for 2023/24 was approved, indicative figures for 2024/25 and 2025/26 were based on the forecast assumption at that time that inflation, having peaked at over 11% in October 2022, would rapidly return to the Treasury target of 2%. Events in recent months have seen inflation dropping at a far slower rate than forecast at the beginning of the calendar year. A base budgeted provision of £3.3m was included in the 2023/24 budget for expected inflationary increases, including pay awards, with an additional £5million included as a budget pressure for additional budget pressures that were more than probable.

5.6 The provision for inflation needs re-evaluating in terms of the short-medium and medium-long term financial planning of the Council as, although inflation has begun to fall and is continuing to show signs of reducing, uncertainty remains high, particularly for the economy with expectations of how inflation and interest rates will go forward together. The Council's Treasury Advisors, Arlingclose, provide regular economic updates including inflation measures. CPI inflation in August 2023 was 6.7%, therefore it is proposed to assume a slower rate of recovery than the forecast rates suggested in the table above, in order to be more prudent and err on the side of caution in such a volatile situation.

5.7 Key contracts receive an uplift in line with inflation for the prior 12 month period. For scenario planning, the mid-range scenario will apply a more cautious rate of the forecast inflation rate in the table +2% before stabilising at 2% in 2028/29 as forecasts suggest, thus removing the drop to 0% in assumptions, which even at that is still a positive outlook to come back to Treasury targets in a relatively short space of time, and assumes no fluctuations. The optimistic scenario will be 1% less (until assuming the 2% target from 2028/29) and the pessimistic at 1% higher than mid-range.

5.8 The areas of cost pressures for inflation provisions are:

- Contracts – service contracts
- Contracts – PPP, Energy
- Pay

<u>Contract inflation</u>

5.9 In summary, cost pressures arising with service contract inflation (excluding pay awards, energy and PPP contract uplifts which are shown separately) are as follows:

	Optimistic	Mid-range	Pessimistic
Assumption	*Mid-range -1%*	*CPI forecast +2%*	*Mid-range +1%*
Year 1	£0.510m	£0.610m	£0.710m
Year 2	£0.168m	£0.276m	£0.386m
Year 3	£0.107m	£0.218m	£0.333m
Years 4-10	£0.191m - £0.227m	£0.303m - £0.234m	£0.420m - £0.369m

Energy Contracts

5.10 Energy costs includes oil, gas, electricity, water and street lighting and unmetered electricity. The nature of these costs is such that inflation is not the only influencing factor; markets are volatile and affected by the national and global economy. As such, to predict with any level of accuracy the long term position on energy costs is impossible and current forecasts available to the Energy Team only go to 2025/26. Updated prices and consumption along with forecast are reported each year in the annual Energy Report. The scenarios have been calculated using 2022/23 full year consumption as a basis. However, energy efficiency measures as part of the Council's Road Map to Net Zero may go some way to reduce energy consumption.

5.11 Scenarios for energy costs have been calculated on the same basis as contract inflation above but with a wider range given the volatility of the energy market: the mid-range adopts forecast CPI +2% until levelling at 2% in 2028/29, the optimistic scenario will be 4% less and the pessimistic at 4% higher than mid-range.

5.12 In summary, inflation pressures associated with Energy costs are as follows:

	Optimistic	Mid-range	Pessimistic
Assumption	*Mid-range -4%*	*CPI forecast +2%*	*Mid-range +4%*
Year 1	£0.121m	£0.353m	£0.584m
Year 2	(£0.083m)	£0.160m	£0.420m
Year 3	(£0.116m)	£0.126m	£0.407m
Years 4-10	(£0.068m) – (£0.104m)	£0.180m - £0.148m	£0.489m - £0.627m

PPP

5.13 The Council's PPP schools contract is a significant contract that attracts an annual inflationary increase for the payments. The level of uplift applicable to the contract is the value of the Retail Price Index (RPI) for the month of February immediately preceding the indexation review date (1 April) compared to the value of RPI at the base date. As with the above scenarios for service contract and energy costs, the PPP assumptions will follow the same reasoning: the mid-range scenario will apply the forecast RPI rate +2% before stabilising at 2% in 2030/31 (two years behind CPI), the optimistic scenario will be 1% less (until assuming the 2% target from 2030/31) and the pessimistic at 1% higher than mid-range.

5.14 In summary, budget pressures associated with the PPP contact are as follows:

RPI	Optimistic	Mid-range	Pessimistic
Assumption	*Mid-range -1%*	*CPI forecast +2%*	*Mid-range +1%*
Year 1	£0.620m	£0.704m	£0.788m
Year 2	£0.198m	£0.291m	£0.385m
Year 3	£0.184m	£0.281m	£0.382m
Years 4-10	£0.291m - £0.224m	£0.396m - £0.238m	£0.507m - £0.389m

6. Pay

6.1 Pay accounts for over £185m of budgeted expenditure across the Council. Pay agreements for Council staff, including teachers, are negotiated at a national level. The 2022/23 budget process saw 2% included for the pay award however, as circumstances in the economy quickly changed with inflation rapidly increasing, and the cost of living crisis, pay awards actually averaged over 6% in the year, after agreements were reached for both the Scottish Negotiating Committee for Teachers (SNCT) and Scottish Joint Councils (SJC) pay deals. The Council must satisfy itself that the pay bill and pay awards for the workforce are affordable and sustainable and remain within existing budget allocations.

6.2 In response to high inflation, average pay growth accelerated in 2022/23 and continues to remain uncertain for 2023/24 for much of the Council's workforce with current negotiations for non-teaching staff ongoing at the time of preparing this strategy. The Council's financial planning requires to take a sensible approach to future pay settlements as it is such a significant portion of the budget that even a modest change in assumption can affect the decisions made regarding the other financial levers.

6.3 The Scottish Government's 2023/24 Public Sector Pay Strategy was published in March 2023, at a time when the pay awards for 2023/24 for much of the Scottish Public Sector were still in contest. Key features of the 2023/24 Public Sector Pay Strategy are:

- The implementation of the real Living Wage rate of £10.90 per hour, including internships and Modern Apprenticeships;
- A suggested cash underpin of £1,500 for public sector workers who earn £25,000 or less;
- Pay uplift for Chief Executives is capped at the same cash amount as the lowest paid;
- Setting a pay award floor of 2%; and
- Recommending a central metric of 3.5% and setting both an award ceiling and pay envelope maximum of 5% on business efficiencies and/or pay bill savings

Source Public Sector Pay Strategy 2023/24

6.4 The Council's Short to Medium Term Financial Strategy recognises that due to inflation currently running at an elevated level, the effects are a likelihood of a higher than budgeted increase in the Real Living Wage which then leads to higher contract inflation in 2024/25 than currently budgeted for as well as creating pressures for pay negotiations. Likewise, the outlook in the long term for pay awards is one of uncertainty.

6.5 For planning purposes, alternative scenarios setting out the best and pessimistic outlook are presented in the tables below. The Public Sector Pay Strategy says the Scottish Government sets a pay floor of 2%, therefore this is the optimistic scenario in the model. The pessimistic scenario, assuming a pay award to be fully funded by the Council, is 4%. The mid-point is 3%.

6.6 In summary, budget cost pressures arising from workforce pay increases are as follows:

	Optimistic	Mid-range	Pessimistic	
Assumption	*2%*	*3%*	*4%*	*CPI forecast +2%*
Year 1	£3.840m	£5.760m	£7.680m	£11.711m
Year 2	£3.917m	£5.932m	£7.987m	£5.296m
Year 3	£3.995m	£6.110m	£8.306m	£4.180m
Years 4-10	£4.075m - £4.589m	£6.294m - £7.515m	£8.638m - £10.930m	£5.969m - £4.920m

7. <u>Funding from the Scottish Government</u>

7.1 The main source of the Council's funding is from the Scottish Government, which provides around 80% of the Council's net revenue budget each year in the form of General Revenue Grant and Non Domestic Rates income.

7.2 The Scottish Government's Medium Term Financial Strategy in May 2023 addressed their funding outlook for the next five year period, recognising that the outlook has changed significantly since the previous year. The main movements relevant to local authorities were due to the Scottish Government allocating an additional £1 billion to the health and social care budget to provide a 10.1% inflationary increase to the level of social security benefits, along with an additional £900m reallocated towards the public sector pay awards. The impact of these moves changed the Scottish Governments 2022 spending and future funding baselines.

7.3 As is the case for the Council at a local level, demand-led expenditure is likely to lead to significant gaps at a national level as the Scottish Government focus on spending demands in areas like health and social care and education. Their strategy states "In order to prioritise the programmes that will have the greatest impact on delivery of our three missions, such as early learning and childcare, we will need to deprioritise programmes that make a less meaningful contribution to our central missions." This suggests that local government (except for these priority areas) will be viewed as lower priority and subject to further reductions in funding support.

7.4 The Scottish Government expect a decrease in real-terms funding in 2024/25 from 2023/24 after social security spending plans and ring-fenced Scottish local authority funding is taken into account. Inflationary pressures are expected to be greater than recent years but modest compared to 2022/23. It is anticipated that the Scottish Government will provide clarity on details of its budget plans in November 2023, and the Local Government Finance Settlement in December 2023.

7.5 Until the settlement is announced, non-protected budgets are expected to face reduced settlements in the medium to long term. The optimistic scenario assumes a 2% increase from 2024/25, mid-range assumes 1% increase for one year then flat cash for the remainder of the plan. The pessimistic scenario assumes a 1% reduction year on year. This translates to the cash movements detailed below.

- Increase 2% - £3.9m
- Increase 1% for three years only
- Decrease 1% (£1.94m)

	Optimistic	Mid-range	Pessimistic
Assumption	+2%	1% then Flat cash	-1%
Year 1	£3.88m	£1.94m	(£1.94m)
Year 2	£3.96m	£1.96m	(£1.92m)
Year 3	£4.04m	£1.98m	(£1.90m)
Years 4-10	£4.12m - £4.64m	£0	(£1.88m) – (£1.77m)

7.6 In June 2023 a new agreement was signed between the Scottish Government and Local Government that is expected to support the Scottish Government's proposed new deal for Local Government. Known as 'The Verity House Agreement' (VHA) it will also see a Fiscal Framework introduced to re-establish joint-working in a partnership focussed on achieving shared objectives for all Local Government communities. There is a commitment towards three key priorities:

- Tackling poverty, especially child poverty
- Transforming our economy through a just transition to deliver net zero
- Delivering sustainable, person-centred public services

7.7 A keynote issue addressed in the VHA is the approach to ring-fenced funding by the Scottish Government and the limitations that increasing levels of such funding puts on councils. The benefits to the Scottish Government of ring fencing funding, where it can only be used for specific purposes, are that its priorities can be delivered at a local level and often within stipulated parameters and timescales. Ring-fenced funding has conditions attached and typically a clawback clause if the conditions aren't met. There are other forms of restriction on funding, where Scottish Government sets clear expectations as to the use of funding and frequently requires reporting on the use of such funding even when given as part of General Revenue Grant. There are drawbacks to the Council when receiving ring fenced and other funds with conditionality as part of the total revenue allocation: additional monitoring and reporting requirements require staff resources; lack of flexibility may impede development of local solutions; the emphasis is on input rather than outcomes. A recent update on the Agreement is that a review of ring-fenced or specific grants to Local Government is being undertaken with a view to baselining these, giving Councils more flexibility to address their priorities. The changes brought about by the VHA will hopefully give greater control to the Council over its budget, by giving the freedom to be resourceful and removing the administration that ring-fenced funding and specific grants often come with. However, truly ring-fenced grants form a relatively small part of funds given from Scottish Government with conditionality and it is unclear to what extent effective control by Scottish Government of much local authority spend will be reduced.

7.8 It is anticipated that some issues addressed in the VHA may be put into place as early as the 2024/25 settlement.

8. <u>Council Tax Income</u>

8.1 Council Tax income accounts for 20% of the Council's revenue and is the main fiscal lever that local authorities have. In setting Council Tax, estimated income is based on a combination of Band D equivalent numbers (the Council Tax base), householder base (single occupancy and other discounts) and the expected rate of collection.

8.2 The Council has discretion to increase tax levels however this has been capped in recent years through conditions set out by the Scottish Government in the annual local government settlement. The Council's Band D equivalent was £1,135 for 10 years between 2007/08 and 2016/17 when the Scottish Government's Council Tax freeze ended. The freeze was reinstated in 2021/22 during the Covid-19 pandemic.

8.3 Crucially, the rate of Council Tax must provide the Council with a degree of certainty around current and future funding levels. The system must therefore be stable and buoyant to provide this certainty, and must not expose the Council to an unmanageable degree of financial risk by reduced collection rates. The number of chargeable dwellings vary only relatively modestly year to year, reflecting new dwellings as well as properties removed.

8.4 There are general assumptions made when budgeting for Council Tax revenue raised: collection rates and the buoyancy of the tax base. The scenarios adopted in the long term planning are twofold: increases in Council tax and an assumption for an element of growth in the tax base.

8.5 For each 1% increase in Council Tax rates, at current 2023/24 rates, the Council could raise approximately £500,000 in additional revenue. For scenario planning the following key assumptions have been made in relation to Council Tax increases: all scenarios include a 0.6% increase in the number of chargeable dwellings each year, and maintain a stable collection rate of 98.5% (96.5% in year + 2% prior year recoveries) as these are not variables the Council has control over, although it is appreciated that as the % rate increases so does the risk of failure to pay resulting in a decrease in collection rate.

- the pessimistic scenario – from the Council's perspective – is based on a 2% increase in rates, which long term would be an inflationary increase only
- the mid-point scenario is based on the assumption that the Council will apply a 5% increase to Council Tax rates.
- the optimistic scenario assumes a 10% increase.
- An increase based on year on year inflation (CPI) is also shown but given some years are predicted to be 0% before stabilising at 2% this would be counter-productive in generating additional income to pay for services and would not be a recommended option.

8.6 In summary, additional revenue income generated from Council tax receipts year on year are as follows:

	Optimistic	Mid-range	Pessimistic	Inflation
Assumption	*10%*	*5%*	*2%*	*CPI%*
Year 1	£5.335m	£2.877m	£1.402m	£0.714m
Year 2	£5.806m	£2.940m	£1.339m	£0.323m
Year 3	£6.428m	£3.107m	£1.374m	£0.726m

Years 4-10	£7.117m-£13.105m	£3.283m-£4.572m	£1.411m-£1.650m	£1.195m-£1.572m

8.7 Other revenue-raising methods that may give rise to additional income depending on the extent of changes in legislation and development of Council policy are:

- Council Tax on second homes and empty properties
- NDR Empty Property Relief

Given the uncertainties about future proposals for Council Tax nationally and the need for Council to develop policy positions, no additional income is assumed at this stage in the Medium to Long Term Financial Strategy, although the potential for this is noted in the Short to Medium Term Strategy. It would not be prudent to import this into longer term calculations without a degree of certainty

8.8 There are also Council Tax reform measures currently out for consultation which would increase rates in Bands E to H on an increasing scale to generate additional funding. As this is not yet approved these potential increases have not been included in the scenarios below, on the same grounds of prudence as mentioned in paragraph 8.7 above..

9. The Cost of Capital Borrowing

9.1 The Council's revenue budget is interconnected to the financing of its capital expenditure and to the treasury management function that lies beneath the day to day transactions of the Council's service provision. When the Capital Programme is approved, the impact of debt and borrowing requirements that will arise from it are factored in to the revenue budget. The affordability of the recurring interest and principal debt repayments are a significant part of the Council budget and changes to interest rates can create unexpected budget pressures. When there is a pressure on the revenue budget, this in turn can put a strain on decision making within the capital programme.

9.2 It is a statutory requirement under Section 93 of the Local Government Finance Act 1992 for the Council to produce a balanced budget. The Act specifies that a local authority must calculate its budget requirement for each financial year to include the revenue costs incurred from capital financing decisions. The key objectives are to ensure the capital investment plans of the Council are affordable, prudent and sustainable.

9.3 Given the upward trend on interest rates recently, the Council is carefully monitoring the impact of current commitments and existing plans. A review of the Council's capital plan has commenced. Increased construction costs in recent years are also a pressure for the capital plan and that translates into increased borrowing costs also. The Treasury Management Team, in partnership with the Council's treasury advisors Arlingclose, will continue to monitor closely the situation around interest rates and take any necessary action on a day-to-day basis to avoid risk to the Council's finances. In the longer term the Council's approved Performance Indicator for the costs of borrowing – cost of borrowing as a percentage of the Council's net revenue budget – will continue to be used as a litmus test for affordability.

9.4 The Council has a revenue budget for debt charges and the increases in capital expenditure between 2024/25 and 2033/34 means that the revenue debt budget needs to be reviewed and increased. Current assumptions in respect of the debt charges are shown below along with optimistic and pessimistic scenarios:

- The capital expenditure in the mid-range is the approved capital programme. Optimistic spend is 80% of this and assumes underspends rather than carry forward to the following year. Pessimistic is a 2% overspend on the approved plan.
- Interest rates for the scenarios are the 20 year Gilt forecast from Arlingclose as at March 2024. These are different to the base rate and is tracked by the Public Works Loans Board (PWLB) so are more reflective of the borrowing rates the Council would get.
- Prudential borrowing levels are based on the capital expenditure of each scenario less the funding from capital grant and receipts. The loans charges are based on these borrowing requirements.

	Optimistic	Mid-range	Pessimistic
Assumption	80% of Capital Plan		+2% of Capital Plan
Year 1 – Loans Pool Rate 4.6% Prudential Borrowing Inc/(dec) in Loans Charges	£39.981m £2.839m	£49.976m £3.548m	£54.326m £3.857m
Year 2 – Loans Pool Rate 4.25% Prudential Borrowing Inc/(dec) in Loans Charges	£31.394m £2.119m	£42.971m £2.901m	£44.129m £2.979m
Year 3 – Loans Pool Rate 4.20% Prudential Borrowing Inc/(dec) in Loans Charges	£19.007m £1.273m	£27.952m £1.873m	£28.847m £1.933m
Year 4 - 10 – Loans Pool Rate 4.20% Prudential Borrowing Inc/(dec) in Loans Charges	£32.136m - £8.091m £2.153m - £0.542m	£44.045m - £12.668m £2.951m - £0.849m	£45.236m - £13.126 £3.031m - £0.879m

9.5 The Capital Plan is being reviewed and following that review, which is intended to be reported to Council in December, this section of the report will be updated and a revised report brought to Council prior to the budget being set, along with any other amendments for changes in assumptions.

10. Cost Pressures/Risks

Additional Financial Risks

10.1 There are several additional financial risks that cannot currently be quantified or classed as budget pressures, therefore they are categorised as risks that may or may not materialise during the period of time which the strategy covers. If and when this happens, officers will update the financial assumptions in the strategy and notify members. At this present time, these financial risks include:

- Moray Integration Joint Board (MIJB). The provision of health and social care is delivered by NHS Grampian and the Moray Council under the direction of the Moray Integration Joint Board (MIJB). The Council has no direct control over the strategic delivery of social care services and is currently liable for 37% of any overspend on health and social care by MIJB. Based on current levels of expenditure and future predicted demographic changes, MIJB may overspend on adult health and social care services. This presents a significant risk for the Council in terms of budget management. Children's Services have now also been delegated to MIJB. During 2023/24 financial responsibility for these sits entirely with the Council as specified in the revised Scheme of Integration.. Moving forward this will become part of the MIJB financial envelope and this will increase the proportion of funding provided by Moray Council to MIJB and thus the percentage by which the Council will be liable to fund any MIJB overspend.
- There is a growing demand for Additional Support within Early Years and school settings. The Council has allocated additional funding to this area – this may prove insufficient; some funding is one-off – this may require to be converted to recurring funding.
- The Council budgets for a mild winter in terms of winter maintenance but the actual cost will be higher if weather conditions are poorer.
- Other demand-led expenditure will vary according to the need for a particular service and can depend on social and economic factors at set points in time. For example, homelessness and the need for temporary accommodation must be managed within the service budget allocated yet are subject to unpredictable demand when linked to social and economic factors.
- The affordability of the capital plan and borrowing, particularly given forecast reductions in capital grant funding per the SG MTFS.
- A reduction in the Council's general revenue grant allocation, if demographic forecasts are accurate and affect the future allocation, as Moray's under 16 population is currently forecast to be decreasing at a greater rate than the Scottish average..

10.2 This medium to long term strategy includes known service specific cost pressures, either existing or anticipated to be new burdens. Other risks in the environment in which the Council operates are noted as above and any other emerging risks will be kept under review as part of the medium to long term financial planning process. Identification of these risks, monitoring and where possible mitigating them form part of the unquantifiable input into the financial planning process.

11. Participatory Budgeting

11.1 Participatory Budgeting (PB) is a democratic process in which members of the community decide how to spend part of a public budget. It gives the public influence in the decision-making over Council finances.

11.2 Scottish Local Authorities and the Scottish Government have a framework agreement with a target where at least 1% of Council budgets will be subject to PB. Currently the Council are actively engaged in a wide variety of PB projects and making every effort to reach the target, however, actual amounts allocated through PB fall far short of the target.

11.3 PB goes above and beyond budget consultations and requires facilitation between the sponsor (Council) to ensure openness and transparency and a vote on the actual outcome to determine that outcome.

11.4 The benefits of Participatory Budgeting are perceived to be:

- Improved democratic process
- Improved public awareness and understanding of the Council
- Strengthens the relationship between the community and the Council

11.5 There are also risks with PB:

- Unrealistic expectations from the community if not properly facilitated
- Limited scope where restrictions on budgets
- Needs public buy-in
- Voting risks (excluding minority or hard to reach groups)
- Very time consuming and requires significant officer input

11.6 An update to the Community Empowerment Act is expected and this will give direction as to future PB activity, along with other forms of community engagement.

12. Demographics

12.1 Population changes vary across Scotland, and between council areas from one year to the next. The National Records of Scotland most recent population estimates report (Mid-2021 Population Estimates, Scotland)

12.2 The population of Scotland has been increasing every year for the last 20 years and is projected to continue rising until around mid-2033 before beginning a gradual decline over the following two decades. Population change is driven by two main factors: natural change (number of births minus the number of deaths) and net migration (the number of people moving into an area minus the number of people leaving). Scotland's population is projected to age with an increase in the number of people aged 65 and over set to grow, while the number of children is projected to fall sharply, compared to those aged 16-64 only expected to fall slightly.

12.3 In Moray, the population grew by 10.8% from 2001 to 2021, with an increase of 0.7% in the one year to June 2021. The population is currently expected to decrease by 0.1% in the 10 year period between 2018 and 2028. Moray's population is ageing, with life expectancy and healthy life expectancy for both men and women above the Scottish average. The age structure of the population in Moray in mid-2021 was: 0-15 years 17%, 16-64 years 61% and 65 years and over 22%. The percentage change in each of those age groups from ten years previous, in mid-2011, were: 0-15 years -6%, 16-64 years 0% and 65 years and over +24%. This trend indicates a reducing number of children with an even greater level of ageing population settling in Moray. Between 2018 and 2028 the age group 90 years and over is projected to see a +50.9% increase. The number of households in Moray has increased by 22.7% since 2001, at a more rapid change than the Scotland level for the same period (+16.2%). The level is projected to increase even further by 4.9% up to 2028, the same as Scotland as a whole. Likewise, the number of dwellings had steadily increased in the period from 2001 to 2022. In Moray, Council Tax band A was most common (25.6%) in 2022, followed by Council tax band B (22.7%), with Council Tax band H the least common (0.2%). (Source National Records of Scotland, Household Estimates, July 2022)

12.4 These projections will be updated based on the 2022 census during 2024.

12.5 Primary and secondary school rolls are projecting to increase in the short term, with a slight decrease in the interim period 2027 and 2028. This will impact on demand for services and also on grant support from Scottish Government under the present method of allocating general revenue grant. (data from the School Census data, September 2022 – due to be updated for September 2023 figures and will be published towards the end of this calendar year and updated annually)

12.6 A significant element of Scottish Government grant funding allocated through Grant Aided Expenditure (GAE). GAE uses statistical measures to apportion funding across local authorities. Over 30% of GAE is linked to the number of school pupils in primary and secondary education. A further 15% is linked to population, either of a certain age group, working age population or the total population. The impact of demographic changes; migration, population growth may lead to funding changes for specific services particularly Education, and will fall within the timescale of this strategy. When population projections are updated in 2024 these will be reviewed to estimate the likely impact on income for the Council and to assist in financial planning for services likely to be impacted by changing population numbers.

13. Other revenue-raising methods

Charging for Services

13.1 Under the Council's Charging for Services Policy, an annual revision of charges is required and charges within the control of the council are generally inflated annually. A default freeze of charges was approved for 2022/23 at 2021/22 levels. When setting Charges services should consider the scope for full cost recovery, with benchmarking against other local authorities a good test of reasonableness. It is intended to bring forward proposals in December 2023 to apply a multi year approach.

13.2 Not all charges are within the Council's control, some are levied by statute and are excluded from the scenarios below.

13.3 Charging for discretionary services with a flat rate increase could generate additional income, assuming the demand is still there for the service. It is accepted that there will be an element of decline in the demand for services if the charges are increased too much. Assumptions used are:

- Optimistic – 10%
- Mid-range – 5%
- Pessimistic – 2%

	Optimistic	Mid-range	Pessimistic
Assumption	*10%*	*5%*	*2%*
Year 1	£0.216m	£0.108m	£0.043m

Year 2	£0.238m	£0.114m	£0.044m
Year 3	£0.262m	£0.119m	£0.045m
Year 4-10	£0.288m - £0.510m	£0.125m - £0.168m	£0.046m - £0.052m

14 Key assumptions within the financial strategy

14.1 The impact of all the main assumptions listed above and the different scenarios outlined are summarised below. The actions to balance 2024/25 and 2025/26 are driven by the Short to Medium Term Financial Strategy and are included here as illustrative information only. The main consideration within the Short to Medium Term Financial Strategy has been to remove the structural deficit. On the assumption that this has been achieved, the table below identifies the main influences on the budget from 2026/27 going forward . The key consideration for the Medium to Long Term is that from 2026/27 onwards a budget gap of £5 million on average is anticipated to be created by inflationary pressures and the cost of borrowing, even after increase in Council Tax and charges for services. This Strategy therefore identifies how that ongoing gap could be bridged.

	Note	2024/25	2025/26	2026/27	2027/28 – 2033/34
Pay Award (all staff, average %)	**1**	2% - £3.840m 3% - £5.760m 4% - £7.680m	£3.917m £5.932m £7.987m	£3.995m £6.110m £8.306m	£4.075m - £4.589m £6.294m - £7.515m £8.638m - £10.930m
Contract inflation – general	**2**	Opt – Mid-1% £0.510m Mid CPI+2% - £0.610m Pess – Mid+1% £0.710m	£0.168m £0.276m £0.386m	£0.107m £0.218m £0.333m	£0.191m - £0.227m £0.303m - £0.234m £0.420m - £0.369m
Contract inflation - Energy (tariff changes)	**3**	Opt – Mid-4% £0.121m Mid CPI+2% - £0.353m Pess – Mid+4% £0.584m	(£0.083m) £0.160m £0.420m	(£0.116m) £0.126m £0.407m	(£0.068m) – (£0.104m) £0.180m - £0.148m £0.489m - £0.627m
Contract inflation – PPP	**4**	Opt – Mid-1% £0.620m Mid CPI+2% - £0.704m Pess – Mid+1% £0.788m	£0.198m £0.291m £0.385m	£0.184m £0.281m £0.382m	£0.291m - £0.224m £0.396m - £0.238m £0.507m - £0.389m
Loans Charges - borrowing for capital programme		Opt – £2.839m Mid – £3.548m Pess - £3.857m	£2.119m £2.901m £2.979m	£1.273m £1.873m £1.933m	£2.153m - £0.542m £2.951m - £0.849m £3.031m - £0.879m
Council Tax (rate)		2% - £1.402m 5% - £2.877m 10% - £5.335m CPI - £0.714m	£1.339m £2.940m £5.806m £0.323m	£1.374m £3.107m £6.428m £0.726m	£1.411m - £1.650m £3.283m – £4.572m £7.117m - £13.105m £1.195m - £1.572m
Government Grant core funding	**5**	+2% - £3.88m +1%/flat cash - £1.94m -1% - (£1.94m)	£3.96m £0 (£1.92m)	£4.04m £0 (£1.90m)	£4.12m - £4.64m £0 (£1.88m) – (£1.77m)

	Note	2024/25	2025/26	2026/27	2027/28 – 2033/34
Income – discretionary charges		2% - £0.043m 5% - £0.108m 10% - £0.216m	£0.044m £0.114m £0.238m	£0.045m £0.119m £0.262m	£0.046m - £0.052m £0.125m - £0.168m £0.288m – £0.510m
BUDGET GAP – Mid Case Scenario	**6**	**£6.050m**	**£6.476m**	**£5.382m**	**£6.716m - £4.244m**

Note 1 – pay awards in recent years have been on a scale and capped at a limit for higher earners/Chief Officers. The methodology for calculating the impact of the assumptions has been done using an average position in light of previous year's averages.

Note 2 – this sum is allocated to a range of uplifts including School/community transportation, Children's Services and Waste contracts and fees.

Note 3 – Future years figures remain subject to considerable variations, given the moves within the Smarter Working policy, and possible reduction of office space, but until these are realised the current inflation assumptions have been based on 2022/23 full year consumptions.

Note 4 – the level of uplift applicable to the Council's PPP contract is RPI index rate in the February of the preceding financial year.

Note 5 – General Revenue Grant and Non-Domestic Rates

Note 6 – 2024/25 and 2025/26 budget gap already encompassed in Short to Medium Term Financial Strategy workings.

15 Transformation / Council of the Future

15.1 Work has commenced on identifying and developing a future operating model for the Council aligned with the shared priorities set out in the Verity House Agreement and looking forward to delivery of Council priorities within a sustainable balanced revenue budget and an affordable capital plan. Various models have been given preliminary scrutiny. The models themselves are unlikely to deliver financial savings but will help to determine where and how the Council invests in the change programme.

15.2 Looking forward beyond the current Improvement and Modernisation Programme (IMP), to areas of work which could deliver a financially more sustainable Council, the following are being scoped:

Asset Management

15.3 Various strands of work are encompassed under this theme. The Smarter Working project is already in delivery. The Depot review is at Outline Business Case stage. At this stage potential revenue savings of £200,000 to £400,000 have been provisionally estimated. The strategic review of the Learning Estate has commenced and again has potential to result in reduced running costs. With further investment there is scope to accelerate the pace of this review. Part of the Route Map to Net Zero involves a reduction is the Council's energy use. Preliminary estimates are for financial savings of £100,000 to £200,000 resulting from this. Development work will also be progressed on generating income from renewables and options to reduce costs through a Property Asset Trust. A desktop review of the Council's asset base will form part of the review of the capital plan. As can be seen from the table at 14.1 a significant element of the budget gap is generated from planned capital spend. In common with other local authorities the Council needs to reduce its planned capital spend. This needs to be followed up by service reviews to determine the pattern of service delivery from a reduced asset base. A combination of reduced capital spend and a reduced asset base has the potential to reduce costs to the order of £1,000,000.

Place Based Approach

15.4 In considering what the Council's future asset base might look like, consideration must be given to the optimal basis on which to meet place based needs and other sources of service support including through partner organisations and services delivered by communities themselves. The rural nature and geography of Moray requires to be factored into the distribution of service bases in order to meet the needs of Moray's population. This is an emerging aspect of the Transformation Programme. Future distribution of service bases will be reviewed taking account of factors such as operating cost, local population, service usage, travel (time/distance), geography (ease of access)and asset condition. In some cases a service base may not be proposed in every area where residents can access that service in a neighbouring or central area.

Service redesign / review of processes

15.5 A Lean review of processes has been part of IMP2 for some time but work has been delayed. This needs to be progressed to facilitate digitisation of Council processes. Lean as a tool in itself and as a facilitator for digitisation is anticipated to generate significant savings. Linked to such a micro review of service delivery needs to be a macro review, considering management and governance arrangements, to ensure a more streamlined approach. Estimated savings are included in the current financial plan at £250,000 and since those savings were estimated further areas for consideration have been identified.

15.6 As can be seen from the table at paragraph 14.1 the biggest single contributor to the projected future budget gap is from pay awards. Service redesign resulting in a streamlined council with consequent reduced head count over time will mitigate this pressure.

Demographics

15.7 As the Council reviews its asset base and likely demand for services it needs to use the best available information on demographic projections to predict the demand for services and to identify what a strategic asset base for different asset types would be to serve the future needs of the communities in Moray. Shrinking population numbers – eg of under 16s – should imply a reduced demand for services and if grant support is reduced then service reduction is imperative. Growing population numbers eg over 65 dictate a need to review how services are delivered as it is not sustainable in terms of financial cost or ability to recruit staff to continue to expand services on the current model. As these services are delegated to MIJB this will not form part of the detailed planning which the Council undertakes, however, Council services may be called upon to facilitate service redesign e.g. use of digital tools.

15.8 In parallel to the work being carried out under the Short to Medium Term Financial Plan, investment in the three strands of work identified in paragraphs 15.3 to 15.7 above needs to be made so that work can commence in order that savings become available to support the budget from 2026/27 onwards.

16 Conclusion

16.1 The Medium to Long Term Financial Strategy for a financially sustainable Council is to take work along three main strands of service development.

16.2 The Council will take a strategic approach to asset management, seeking to develop a strategically located asset base using a Place Based Approach to serve local communities from energy efficient facilities.

16.3 The Council will aim to be a more streamlined organisation, using recognised techniques to improve efficiency and taking advantage of technology to support service delivery.

16.4 The Council will seek to future proof its services, using the most up-to-date information of population to inform planning for future service delivery.

16.5 Work is on-going to develop workstreams to support the Council of the Future and reports will be brought to members as plans are developed. As approval is given for these developments the Medium to Long Tern Financial Strategy will be updated to appropriately reflect them.