

Medium Term Financial Outlook

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Summary

<p>Financial outlook remains highly uncertain</p>	<p>The pandemic and economic recession have resulted in a more uncertain medium term outlook. In particular there is only a one-year funding settlement from government and spending growth and income will be significantly impacted by pace of recovery from the pandemic.</p>
<p>The range of potential gaps between spending forecasts and available funding remain excessively large</p>	<p>The original outlook resulted in range of potential gaps of between £20m to £120m. The first update to the outlook has not significantly reduced the potential range although we have identified are narrower range for the most probable outcome of between £40m to £60m although at this early stage this should not be assumed as the most likely outcome.</p>
<p>The impact of economic recovery on inflation and levels of employment are likely to have a significant impact on 2022-23</p>	<p>The economic recovery, and in particular levels of employment, will be vital to recovery of council tax base and retained business rates. The Council is also exposed if rates of inflation increase as the impact of inflation on council contracted services is only partially reflected in grant settlement if these continue to be a rollover as has been the case in the one-year settlements for 2020-21 and 2021-22</p>
<p>2020-21 outturn provides an opportunity to strengthen the council's financial resilience</p>	<p>Due to the uncertainties and risks it is essential that the council has sufficient reserves to manage unforeseeable circumstances. This includes general reserves and earmarked reserves for specific eventualities e.g. ongoing impact of Covid-19 pandemic in 2021-22. If the council does not have adequate reserves there is a heightened risk of overspends in 2021-22 which in turn could increase the potential gaps for 2022-23 and beyond.</p>
<p>Further updates to the medium term outlook will be provided during the autumn</p>	<p>The spending growth and savings plan estimates will be updated over the course of summer and autumn. Consultation on the budget strategy for 2022-23 will be undertaken earlier than in recent years to inform the updates in the autumn</p>

2.1 The County Council budget report for 2021-22 on 11th February 2021 included a high-level medium term financial outlook. This outlook acknowledged that the financial environment for local authorities remains highly uncertain. Since this outlook was published progress on the national roadmap for easing restrictions has until recently been largely positive although the lasting impact of the Covid-19 pandemic and the economic recession on council spending and income remains unclear. This means that forecast spending, income levels and council tax/business rates yields are considerably less reliable than we have been used to in previous years. Added to this uncertainty we only have a one-year settlement for local government from central government.

2.2 The medium-term outlook is based around three potential scenarios. These include a central case (not necessarily the most likely scenario) together with upside scenarios (based on a rapid recovery) and downside scenarios (based on a slower recovery with lasting impact of Covid-19 pandemic). This is consistent with the approach adopted by the Office for Budget Responsibility (OBR) in their Economic and Fiscal Outlook reports.

2.3 The scenarios encompass spending growth forecasts, existing savings plans and funding forecasts, and result in a wide range for future budget gaps. The gaps make no assumptions about the Council agreeing further savings although do include the full year effect of 2021-22 savings in 2022-23 plus any annual savings/income from continuation of existing policies e.g. fees and charges.

2.4 Each scenario assumes future 2%+2% council tax increases, and that one-off spending and funding from one-off sources included in the 2021-22 are not repeated. At this stage none of the scenarios assume recovery of collection losses in 2020-21 through higher future collection fund balances although this would not help to resolve the budget gaps assuming we continue with the approach that recurring spending should not be supported from insecure funding sources.

2.5 All the scenarios are based on high level assumptions to give an indication of the potential scale of the challenge and are not predictions. We are likely to maintain forecasts based on these scenarios for the immediate short-term future until uncertainties are resolved.

2.6 Ultimately, we anticipate that 2022-23 budget will be honed into a single scenario (as this is essential to comply with requirements for a balanced budget) albeit with the enhanced financial resilience arising from 2020-21 outturn if agreed providing scope to mitigate outstanding uncertainties and risks. These uncertainties include the one-year funding settlement for 2021-22 and several possible trajectories for future spending including ongoing impact of Covid-19.

2.7 The one-year settlement means that the council tax referendum principles and grant settlements are not known for 2022-23, although it seems likely that the Fair Funding reforms and reforms to business rate retention will be further delayed. We had hoped these would address long standing concerns with the redistribution of funding between different classes of authority.

2.8 Due to ongoing uncertainties we anticipate that future years' projections will continue to include alternative scenarios until government has set out detailed government medium-term financial strategy to put public finances and accumulated debt on a sustainable path. The original summary of the scenarios as presented to County Council is shown in table 1.

Table 1 – Original Forecast February 2021

	Upside Scenario		Central Case		Downside Scenario	
	2022-23 £m	2023-24 £m	2022-23 £m	2023-24 £m	2022-23 £m	2023-24 £m
Spending Growth Forecasts						
Business as usual	57.0	57.0	68.0	68.0	79.0	79.0
Covid-19	0.0	0.0	14.0	7.0	21.0	21.0
Replace one-offs from insecure sources in 2021-22	13.0		13.0		13.0	
Remove One-off spending in 2021-22	-10.0		-10.0		-10.0	
Existing savings and policy	-27.0	-20.0	-27.0	-20.0	-27.0	-20.0
Total Spending Growth	33.0	37.0	58.0	55.0	76.0	80.0
Funding Change Forecasts						
Council Tax Base	15.6	16.5	7.8	8.2	-15.6	7.9
Assumed 2%+2% Tax Increases	31.8	33.7	31.5	33.0	30.5	30.5
Government Core Grants	12.5	13.1	0.8	0.8	-12.5	-13.1
Covid-19 Grants	-46.7		-46.7		-46.7	
Total Funding Change	13.1	63.3	-6.6	42.0	-44.2	25.4
Gap	19.9	-26.3	64.6	13.0	120.2	54.6

3.1 The three planning scenarios are based on the assumptions set out below. It is important that these are not considered as a best/worst case as they are based upon assumed possible trajectory for spending and income rather than predictions of final levels.

Upside (rapid recovery)	Successful eradication of the virus with no lasting impact on spending or income levels; Rapid economic recovery for tax base with support discounts, collection rates and housing growth returning to pre-pandemic levels; Business as usual spending growth at lower end of forecast spectrum; Cash increases in government grant
Central (partial recovery)	Partial recovery from pandemic with some additional but reducing impact on spending and income; Partial economic recovery but with higher support discounts and lower collection rates and housing growth than pre-pandemic levels; Business as usual spending growth at the mid-range of forecast spectrum; Rollover grant settlement from government
Downside (ongoing restrictions)	Continuing and ongoing need to take measures to tackle spread of the virus; Continuing economic impact with further reduction in tax base and collection rates in 2022-23 followed by slower economic recovery; Business as usual spending growth at the upper end of forecast spectrum; Reductions in grant settlement from government

3.2 In all likelihood the final outcome for 2022-23 is likely to include aspects of each of the scenarios rather than ending up exactly equating to one of the scenarios. The purpose of medium-term planning based upon scenarios is to demonstrate the potential range of outcomes.

4.1 Since the original publication we have updated some of the forecasts. In particular we have revised the impact of one-off spending and funding within 2021-22 and separated out the impact of inflation uplifts to core grants under rollover arrangements and potential increases/decreases in government grants under the upside and downside scenarios. We have also included forecasts for 2024-25 based on rolling forward the scenario assumptions illustrating the continuing uncertainty. The further into the future we make forecasts the less reliable the estimates become. A summary of the updated forecast is shown in table 2.

Table 2 – Updated Forecast June 2021

	Upside Scenario			Central Case			Downside Scenario		
	2022-23 £m	2023-24 £m	2024-25 £m	2022-23 £m	2023-24 £m	2024-25 £m	2022-23 £m	2023-24 £m	2024-25 £m
Spending Growth Forecasts									
Business as usual	56.6	56.6	56.6	67.9	67.9	67.9	79.3	79.3	79.3
Covid-19	0.0	0.0	0.0	14.0	7.0	0.0	21.0	21.0	10.5
Replace one-offs from insecure sources in 2021-22	4.6			4.6			4.6		
Remove One-off spending in 2021-22	-8.0			-8.0			-8.0		
Existing savings and policy	-26.5	-20.2	-2.8	-26.5	-20.2	-2.8	-26.5	-20.2	-2.8
Total Spending Growth	26.8	36.4	53.8	52.1	54.7	65.1	70.4	80.1	87.0
Funding Change Forecasts									
Council Tax Base	15.6	16.5	17.5	7.8	8.2	8.6	-15.6	7.9	8.3
Assumed 2%+2% Tax Increases	31.8	33.7	35.8	31.5	33.0	34.7	30.5	32.1	33.7
Inflationary uplift	4.0	4.1	4.2	4.0	4.1	4.2	4.0	4.1	4.2
Government Core Grants	8.5	9.0	9.6	0.0	0.0	0.0	-16.5	-16.0	-15.5
Covid-19 Grants	-46.6	0.0	0.0	-46.6	0.0	0.0	-46.6	0.0	0.0
Removal of residual collection fund & S31 Balances	-1.0	0.0	3.4	-1.0	0.0	3.4	-1.0	0.0	3.4
Total Funding Change	12.2	63.4	70.5	-4.4	45.3	50.9	-45.2	28.1	34.1
Gap	14.6	-27.0	-16.7	56.5	9.4	14.3	115.6	51.9	52.8

4.2 Further updates will need to be sensitive to the emerging economic scenario particularly in relation to inflation and levels of employment as the economy recovers. Any increase in inflation will increase the budget gap as this will have a much greater impact on spending than uplifts in grants.

4.3 We are working on the probability of the likelihood of outcomes from the individual scenarios to refine them as far as is possible. Despite the positive progress on the national roadmap for easing restrictions this initial work indicates that the more likely outcome will be between the upside and central scenarios. This could result in a budget gap of between £40m to £60m but it is too early to assume that this is the most likely outcome.

4.4 The ongoing uncertainties for the medium term outlook emphasises the need for the Council to take every opportunity to strengthen financial resilience. Prior to 2020-21 we had assessed that KCC's overall resilience (as measured by accumulated debt and usable reserves) was around the lower quartile for all county councils. If we do not strengthen the council's reserves and some of the risks materialise this could result in an overspend on 2021-22 budget which in turn would reduce reserves at the end of that year, and subject to the level of the reduction

could require replenishment of reserves which would increase the potential gaps in the medium term.

4.5 We have embarked upon the first review of the existing savings plan and business as usual spending growth. This first review will be completed during the summer and the next updated outlook will be reported in September. In the meantime we are planning to launch consultation on the budget over the summer, earlier than in previous years. This will enable the responses to be evaluated to include with the updated forecast. We will undertake further reviews of spending growth and savings plans throughout the autumn as a clearer picture emerges.

4.6 As well as updating spending growth and savings we will also be closely monitoring changes to council tax and business rate collection over the coming months. As shown in the scenarios the possible trajectory for council tax base growth (assuming a rapid economic recovery) provides a significant contribution towards the smaller budget gap under the upside scenario if levels of council tax support discounts recover to pre-pandemic levels. As well increasing the tax base we will also need to monitor recovery of uncollected council tax from 2020-21 which has not been compensated by Tax Income Guarantee grant from government on the assumption that under collection of the collectable based will be recovered in subsequent years.