APPENDIX 4 TO REPORT 32/22

CAPITAL AFFORDABILITY ASSESSMENT

Starting with an update of the 2021/22 position, the HRA Business Plan has been projected forward over a 30-year period (i.e. 2021/22 to 2050/51), with particular emphasis on the following:

- Potential future rent levels
- Existing loan charges commitments (unavoidable costs);
- Estimated levels of HRA capital expenditure for each year; and
- Estimated levels of borrowing.

This has involved estimates and assumptions that will change over time, but which are considered reasonable and robust based on known information at this time. A summary of the assumptions made is provided later in this appendix.

AFFORDABILITY ASSESSMENT OUTCOME

The following table summarises the key outcomes from the affordability assessment for the current year plus 4 forward years of the capital plan, as well as snapshots at 5 years intervals thereafter.

	21/22 £m	22/23 £m	23/24 £m	24/25 £m	25/26 £m	30/31 £m	35/36 £m	40/41 £m	45/46 £m	50/51 £m
Capital Expenditure	21.004	16.089	19.654	15.003	18.187	13.449	11.540	10.607	11.328	12.551
Estimated Borrowing	11.193	8.338	12.067	6.194	9.661	6.000	4.000	2.000	2.000	2.000
Affordability %	11%	14%	16%	13%	14%	18%	19%	19%	19%	19%

The affordability % in the above table represents the ratio of projected loan charges costs to projected rental income in each year.

The affordability of the HRA capital plan is assessed against a parameter, as set out in the assumptions section below. In line with those assumptions, it is currently our view that the affordability % should not exceed 25%. However, if there are particular circumstances in which it may be desirable to increase borrowing to achieve specific business objectives, this level will be reviewed.

The assessment of the current position confirms that the affordability % is not breached in any of the 30 years of the assessment.

On the basis of the assessment therefore, the Director of Finance believes that the HRA Business Plan can be regarded as affordable, prudent and sustainable.

ASSUMPTIONS

The following key assumptions have been made.

<u>Loan Charges Costs</u>
In line with previously approved parameters, the assessment is based on the presumption that overall loan charges costs should not exceed 25% of the projected rental income in any single year.

<u>Interest and Expenses Rates</u>
Costs in respect of principal repayments for existing borrowing are known with certainty from the Council’s fixed asset management system, however assumptions have to be made in respect of future interest and debt management expenses rates. Based on current interest rate expectations, it’s considered that rates will rise very gradually over the first few years but will rise more sharply in the later part of the assessment period.

The following interest rates have therefore been assumed:

- 4.50% - 2021/22;
- 4.60% - 2022/23;
- 4.70% - 2023/24 to 2027/28;
- 4.95% - 2028/29 to 2032/33;
- 5.20% - 2033/34 to 2037/38; and
- 5.45% - 2038/39 for each year thereafter.

For context, the actual interest rate for 2020/21 was 4.50%.

A rate of 0.08% has been assumed in each year for debt management expenses based on recent history.

<u>Capital Expenditure</u>
The draft capital plan 2021/22 to 2025/26 (per Appendix 3 to this report) has been used in respect of the early years of the affordability assessment. Thereafter, the following average levels of future capital expenditure have been assumed for the purposes of this assessment:

- £13.501 million per annum – 2026/27 to 2030/31; and
- £11.286 million per annum – average for each year thereafter.

These average spend levels reflect the capital investment proposals per this report. These may of course require to be revisited over time to take account of the future actual positions in respect of the assumptions made in this assessment.

<u>Capital Receipts</u>
As noted in section 8 of the monitoring report also on the agenda of this meeting, capital receipts accumulated prior to 2021/22 (£0.188 million at 31 March 2021) are to be used in the funding of the 2021/22 capital programme.

As also noted in the monitoring report, capital receipts generated in the current financial year are projected to be £0.499 million and will be utilised in funding the 2022/23 capital programme. It is expected that capital receipts in future years will be relatively minimal. It is considered prudent therefore for the purposes of this affordability assessment to assume no capital receipts for future years. Any receipts that are received in future years will be applied to reduce any borrowing requirement in the following year.

The following receipts assumptions have therefore been made in terms of this affordability assessment:

- 2021/22 - £0.188 million;
- 2022/23 - £0.499 million; and
- Zero thereafter.

<u>Other Funding</u>
Other funding has only been included where it is already confirmed or where conditional approval has been received (e.g. Scottish Government Affordable Housing Grant or Affordable Housing Revenue Account).

Should any additional “other” funding be secured into the future, this will either be utilised to reduce borrowing or to enhance the capital programme as appropriate, taking on board updated long term affordability assessments, capital requirements or grant conditions.

<u>Capital Financed from Current Revenue (CFCR)</u>
The HRA revenue budget provides for a significant level of resources each year for funding of capital expenditure directly from revenue resources – known as Capital Financed from Current Revenue. The following average levels of CFCR have been assumed for the purposes of this affordability assessment:

- £7.185 million per annum – 2021/22 to 2025/26
- £7.201 million per annum – 2026/27 to 2030/31; and
- £8.786 million per annum – average for each year thereafter.

Inclusion of such sums in the capital expenditure funding package allows for the prudent management of borrowing over the HRA Business Plan period, ensuring that the HRA does not become overstretched by over borrowing.

The above CFCR levels have been projected after allowing for the currently evident significant inflation affecting underlying costs.

New Borrowing
It is the level of new borrowing required to fund capital expenditure which determines future commitments in relation to loan charges costs.

The affordability assessment therefore estimates the level of new borrowing required in each year after taking account of all the other assumptions about capital expenditure, capital funding sources, etc. and this in turn has been used to calculate estimated loan charges costs into the future using the interest and expenses rates assumed above. The following average levels of borrowing have been assumed for the purposes of this affordability assessment:

- £9.490 million per annum –2021/22 to 2025/26
- £6.000 million per annum – 2026/27 to 2030/31; and
- £2.500 million per annum – average for each year thereafter.

Expenditure Slippage
Slippage in the capital programme does not represent a capital funding source but merely a change in the phasing of when expenditure is incurred. As such no slippage assumptions have been included in this affordability assessment.