

## Enterprise M3 Board meeting

30 January 2020

### EM3 2020/21 Outline Revenue Budget and 2019-2023 Medium Term Financial Forecast - Item 8

#### The Enterprise M3 Board is asked to:

**ENDORSE** – The proposed outline budget for the 2020/21 financial year, subject to a full detailed budget being brought to the Board in March 2020. (Section 4)

**NOTE** – The expected 2019/20 out-turn position at the end of Quarter 3 (Section 3)

**NOTE** – The key financial risks associated with the proposed outline budget and medium-term forecast (Section 2)

**NOTE** – The 2019/20 to 2022/23 medium-term forecast and impact on reserves (Section 5)

#### 1. Executive Summary

- 1.1. The purpose of this report is to provide the Board with Enterprise M3's (EM3) outline revenue budget for 2020/21, in conjunction with the updated financial forecast to the end of 2022/23. The budget is set to enable delivery of the Strategic Economic Plan objectives, drive implementation of the Local Industrial Strategy and deliver the Local Growth Fund Programme.
- 1.2. The Resources, Finance and Audit Committee (RFAC) reviewed the 2020/21 outline budget on 16<sup>th</sup> January 2020. The group's recommendation is that it be endorsed by the Board, subject to a detailed budget being brought to the March 2020 Board meeting for approval. At that point we will have more detailed information relating to government spending and funding plans, which impact our revenue income and activity. This report summaries the key constituents of the budget and the matters discussed by RFAC.
- 1.3. The report sets out
  - The key financial risks associated with the proposed outline budget
  - The forecast 2019/20 out-turn position at the end of Quarter 3
  - The 2020/21 outline budget
  - The 2019/20 to 2022/23 medium-term forecast and impact on reserves
- 1.4. The Board should be aware of the **key financial risks** associated with the proposed outline budget and medium term-financial plan. The key risks relate to the uncertainty of Government funding, both in relation to a future growth deal and ongoing operational funding for EM3 and Growth Hub activities. In addition, the interest receivable on balances held by Hampshire County Council, are linked to the Bank of England's base rates, which market commentators expect to rise or fall in response to Government yet unknown economic policy. **Section 2** sets out the potential implications and mitigation of these risks. We will consider different scenarios and options for the medium term and bring a paper to the Board for discussion at the March 2020 meeting.

## 1.5. Key Messages

- **2019/20 Forecast Out-turn:** As reported to the Board last year, we are forecasting a surplus position for 2019/20, and are expecting to end the financial year with net income about £0.7m above budget. **Section 3** expands further.
- **2020/21 Outline Budget:** Our focus for 2020/21 will be on implementing our developed Local Industrial Strategy (LIS), alongside a final push on getting remaining projects up and running; meeting funding targets; and continuing to deliver careers activity, Enterprise Zone and the Growth Hub service. This will involve cross-sector engagement with business and other stakeholders to ensure delivery is in line with our LIS. We anticipate expenditure of **£3.2m** (19/20 £3.4m) will exceed in year income of **£3.1m** (19/20 £3.8m). **Section 4** expands further.
- **2019-2023 Medium Term Financial Plan:** We have updated our medium-term financial plan (MTFP), reviewing our costs and activities to ensure we delivery our plans in the most effective and efficient way. The forecast demonstrates that we can fund expenditure required to support our plans to the end of 2022/23, by using **£0.9m** from existing reserves, bringing the reserves level to **£1.9m**. This is in keeping within the minimum reserves level set in our Reserves Policy. However, the Board should note that, if we continue the current trend in using our reserves to fund ongoing activity, our reserves are likely to fall below the minimum required level in the following year (2023/24). **Section 5** expands further.

## 2. Key Financial Risks

2.1. With minimal clarification from Government at this stage, assumptions include expectations that:

- Government revenue funding for LEPs will continue at the current basic rate of £500k p.a.
- Further Growth Deals, of £30m per annum, are in place beyond March 2021
- The Bank of England base rate remains at the current level
- We continue to receive contributions from our major partners, and
- Current services will be maintained, and, where necessary, funded from existing revenue reserves.

2.2. Table 1 considers the key financial risks associated with the assumptions in the 2020/21 budget and the three-year medium-term-financial plan.

Risk	Description	Impact	Likelihood	Mitigation
<b>Capital Funding uncertainty</b>	The current Growth Deal funding ends in 2020/21. Government have yet to announce their spending and funding plans. The main funding assumption in the proposed 2020/21 outline budget and the medium-term financial forecast is that a further Growth Deal of £30m will be in place each year from 2021/22.	<b>Medium</b> Around £1.1m of our annual revenue activity is funded from application fees and interest receivable - funding sources dependant on our capital funds. In 2020/21 over £0.3m of this is dependent on the assumed new Growth Deal. In 2021/22 and 2022/23 this figure is around £0.8m p.a. If the assumed new Growth Deal was reduced or removed, we would need to secure funding/cost-savings, in order to cover the proposed activity for the three years to the end of 2022/23. The focus of the LEP would change.	<b>Medium</b>	For 2020/21 we have enough reserves to cover the potential gap in funding in our budget. We expect Government to announce their funding plans by November 2020. We will consider different scenarios and options for the medium term and bring a paper to the Board for discussion at the March 2020 meeting.

Risk	Description	Impact	Likelihood	Mitigation
<b>Revenue Funding uncertainty</b>	The assumptions in the 2020/21 and the medium-term budgets are that both EM3's operational activity and Growth Hub will continue to be funded at same level as in 2019/20 (£500k and £287k p.a. respectively). In December we received confirmation that Government will continue to fund the Growth Hub for a further year. We have had unofficial indications that our core activity funding will be extended for a further year but have not yet received formal confirmation.	<b>Medium</b> Without this continued funding, in order to maintain the same level of activity, we would need to reduce costs or draw an additional £500k from reserves in 2020/21, and then secure further funding/cost-savings of £1.57m to cover the next two years to the end of 2022/23.	<b>Low</b>	For 2020/21 we have enough reserves to cover the potential gap in funding in our budget. We expect Government to announce their core funding plans for 2020/21 by March 2020. We will consider different scenarios and options for the medium term and bring a paper to the Board for discussion at the March 2020 meeting.
<b>Interest rate uncertainty</b>	We receive interest on our balances held by HCC, as our accountable body, at the Bank of England base rate. Our forecasting assumes that rates remain at the current level of 0.75%.	<b>Low</b> A small change in the level will impact reserves. For example, a change of 0.25% in the base rate would affect income by approximately £145k in 2020/21, adjusting overall reserves by £0.4m by the end of 2022/23.	<b>High</b>	For 2020/21 we have enough reserves to cover the potential gap in funding in our budget. Most impact when capital funds are high. We will consider different scenarios and options for the medium term and bring a paper to the Board for discussion at the March 2020 meeting.

- 2.3. The combination of declining reserves and possible reductions in Government funding means we must continue to secure further funding to enable delivery of our plans or identify possible cost savings. We continue to work with RFAC to explore alternative funding scenarios, how we secure financial stability, and will bring a discussion paper to the Board in March 2020.

### 3. 2019/20 Forecast Outturn

- 3.1. EM3's forecast income and expenditure at the end of Quarter 3 (December 2019) across all revenue funds is summarised below in **Table 2**:

2018/19 Audited Outturn £'000	Table 2: EM3 Revenue Income and Expenditure	2019/20 Approved Budget £'000	2019/20 Forecast Quarter 3 £'000	2019/20 Budget variance* £'000
		<b>A</b>	<b>B</b>	<b>C</b>
<b>2,229</b>	<b>REVENUE RESERVES Brought Forward</b>		<b>2,477</b>	
2,876	Income	3,203	3,810	607
(2,628)	Expenditure	(3,522)	(3,451)	71
<b>248</b>	(Deficit)/Excess Income over expenditure	<b>(319)</b>	<b>359</b>	<b>678</b>
<b>2,477</b>	<b>TOTAL REVENUE RESERVES</b>		<b>2,836</b>	

\* Variance is positive when 2019/20 forecast income is higher / expenditure is lower, than budgeted

- 3.2. The year began with **£2.477m** in overall revenue reserves. At the end of Quarter 3, we are forecasting the 2019/20 year to end with **£2.836m** in overall reserves, adding **£359k** to the balance (*column B*). This is **£678k** (*column C*) higher than the approved budget approved in March 2019, when we expected to draw **£319k** from reserves (*column A*).
- 3.3. These **£678k** net additional funds, arose due to several variances, detailed in **Table 3**:

Event	Net income variation £	Impact / Benefit	Planned/ Unplanned	Description	S-T / L-T
Expansion of our project pipeline	 £404k	Additional application fee	Planned	By the end of 2019/20 we expect to have approved the allocation for all our current Growth Fund, and for expected loan repayments over the next three years.	Short-term
Pause in recruitment	 £118k	Net staffing costs underspend	Planned	Pause in recruiting until the planned new organisation is in place	Short-term
Difficulty in recruitment	 £131k	Net staffing costs underspend	Unplanned	Continued difficulties in recruiting staff in a tight labour market	Short-term
Additional government funding	 £75k	Net staffing costs underspend	Unplanned	Additional government funding provided to help businesses across a cluster of four LEPS to prepare for EU Exit and for intelligence gathering. Part of this will cover EM3 staff costs, as staff focus on business readiness activities and must put on hold normal day to day activities	Short-term
Other	 (£50k)	Net additional income	Unplanned	Various over and underspends, including additional partner funding for joint events; decrease in interest receivable due to issuing a lower than planned level of interest-bearing loans; minor changes in working patterns.	Mainly long-term

**Total £678k**

#### 4. 2020/21 Outline Budget

- 4.1. In 2020/21 income is expected to be lower than in 2019/20, mainly due to the potential of lower Government funding. Expenditure is also expected to be below the 2019/20 level, mainly due to completion of the LIS development work carried out in 2019/20, as we move into LIS implementation.
- 4.2. EM3's budget across all revenue funds is summarised below in **Table 4**:

Table 4: EM3 Revenue Income and Expenditure	2020/21 Budget	2019/20 Forecast (Quarter 3)
	A	B
	£'000	£'000
<b>INCOME</b>	<b>3,116</b>	<b>3,810</b>
<b>EXPENDITURE</b>	<b>(3,239)</b>	<b>(3,451)</b>
<b>(Excess) expenditure over income</b>	<b>(123)</b>	<b>359</b>
<b>TOTAL REVENUE RESERVES (C)</b>	<b>2,713</b>	<b>2,836</b>

- 4.3. The 2020/21 budget (*column A*) shows expenditure (£3.2m) exceeding income (£3.1m), and we therefore expect to draw on retained reserves, by £123k.
- 4.4. **Total revenue reserves:** Our reserves at the end of 2019/20 are expected to stand at £2.8m (*Column B, Row C*), £359k above last year (*Column B*). We plan to use reserves to cover the 2020/21 excess expenditure of £123k (*Column A*) from our retained reserves brought forward, leaving £2.7m in the balance carried forward (*Column A, Row C*).

4.5. 2020/21 budgeted income is approximately **£694k** below the 2019/20 forecast income. **Table 5** identifies the main differences:

<b>Table 5: 2020/21 Budgeted income variation from 19/20 forecast income</b>				
<b>Income</b>	<b>Net income variation £</b>	<b>Impact / Benefit</b>	<b>Description</b>	<b>S-T / L-T</b>
EU Exit Government Funding	 <b>(£427k)</b>	Reduction in Government funding	One-off Government funding provided in 2019/20 to help businesses prepare for EU Exit and for intelligence gathering. As lead partner, EM3 received the income on behalf of a four LEP cluster.	Short-term
LIS development Government Funding	 <b>(£275)</b>	Reduction in Government funding	One-off Government funding provided in 2019/20 as additional capacity funding in 2019/20 to aid implementation of the LEP review requirements and to develop our LIS. We have assumed that only the basic £500k capacity funding will be provided by Government in 2020/21, as it is yet to be confirmed.	Short-term
Application Fees	 <b>(£250k)</b>	Reduction in Application Fees	Application fees were exceptionally high in 2019/20 arising from escalated new project calls. At £400k, we have based the 2020/21 figure on the assumption that a Growth Deal of £30m will be announced for 2021/22.	Long-term
Loan interest	 <b>£158k</b>	Increase in interest receivable	Due to increased loans issued towards the end of 2019/20 and a high proportion of our current Growth Fund allocation (£42m) being received at the start of the year.	Mainly short-term
Partner Contributions	 <b>£150k</b>	Additional partner income	Local Authority partners agreed to increase their contributions to the LEP in 2019/20, However, due to careful budget management and some additional government income, we postponed increase to 2020/21.	Mainly long-term
Other	 <b>(£50k)</b>	Reduction in net income	Various movements including a reduction in EU income funding our ERDF Technical Assistance post, as we reach the end of the programme.	Mainly long-term

4.6. 2020/21 budgeted expenditure is approximately **£212k** below the 2019/20 forecast expenditure. **Table 6** identifies the main differences:

<b>Table 6: 2020/21 Budgeted expenditure variation from 19/20 forecast expenditure</b>				
<b>Expenditure</b>	<b>Net expenditure variation £</b>	<b>Impact / Benefit</b>	<b>Description</b>	<b>S-T / L-T</b>
EU Exit Business Readiness	 <b>(£427k)</b>	Reduction in expenditure	One-off Government funding provided in 2019/20 to help businesses prepare for EU Exit and for intelligence gathering. As lead partner, the funding was received by EM3 to be spent in conjunction with, and on behalf of, the four-LEP cluster, by the end of the year.	Short-term
Staff Costs	 <b>£388k</b>	Increase in staff costs	2020/21 reflects a full year of costs for those staff recruited mid-way through 2019/20, which saw a delay in recruitment to vacant posts due to the tight labour market. Additionally, our organisation review has identified staffing requirements required to increase activity around sectors and trade/international focus. A 15% vacancy rate has been applied to reflect vacancies and staff turnover.	Short-term
Research/Studies/Consultancy	 <b>(£156k)</b>	Reduction Research/Studies /Consultancy costs	Costs were higher in 2019/20 due to additional activity around development of our LIS. However, in 2020/21 there will be activity and costs relating to LIS implementation/case building.	Long-term
Other	 <b>(£17k)</b>	Reduction in net expenditure	Various movements	Mainly long-term

**Total £212k**

## 5. Medium-Term forecast and impact on reserves

- 5.1. We have updated our 2019-2023 Medium Term Financial Forecast, reviewing our costs and activities to ensure we deliver our plans in the most effective and efficient way.
- 5.2. The Board approved several financial measures in April 2018, which would provide around £2m additional funding to use on future operational activity. These incorporated a combination of increasing application fees, partner contributions, and the proportion of capital allocated to interest-bearing loans; and using excess overall reserves to maintain them at a prudent level of 50% of annual expenditure. The increased income allows Enterprise M3 to expand operations to drive forward our Strategic Economic Plan, Local Industrial Strategy and meet the objectives of Government.
- 5.3. Table 7 summarises our position to 2022/23. The proposed organisational structure and plans for management of our Growth Hub, as agreed at the November 2019 Board meeting, are incorporated in this forecast.

2019/20 Forecast	Table 7: EM3 Revenue Reserves: Medium-term financial forecast	2020/21 Budget A	2021/22 Estimate B	2022/23 Estimate C	
£'000		£'000	£'000	£'000	
2,477	<b>TOTAL RESERVES AT START OF YEAR</b>	2,836	2,713	2,371	
3,810	<i>Income</i>	3,116	3,031	2,917	
(3,451)	<i>Expenditure</i>	(3,239)	(3,373)	(3,365)	<b>TOTAL</b>
359	<b>Use of reserves</b>	(123)	(342)	(448)	<b>(913)</b>
2,836	<b>TOTAL RESERVES AT END OF YEAR (D)</b>	2,713	2,371	1,923	
1,784	Minimum Revenue Reserves Level (E)	1,685	1,747	1,738	
1,053	<b>RESERVES AVAILABE FOR USE</b>	1,028	624	185	

- 5.4. The forecast demonstrates our plan to use retained reserves to continue our operations over the next three years in line with discussions with Board members. It shows that we can fund our planned activities to support the economy over the next three years, by using **£0.913m** from existing revenue reserves, reducing the total to **£1.9m** (*Column C, Row D*), which is in line with our Reserves Policy.
- 5.5. Our reserves policy dictates that reserves should be maintained at a level which covers 50% of annual operational expenditure (excluding EZ<sup>3</sup> activity) i.e. around £1.7m (*Row E*). However, the Board should note that, if the current trend continues, we are likely to breach the minimum reserve level in the subsequent year (2023/24).

## 6. Ongoing monitoring

- 6.1. RFAC will continue to play a key role in overseeing the budget, managing risks and keeping the Board informed. This includes monitoring 2020/21 income and expenditure and the medium-term-financial forecast, on an ongoing basis, adjusting the forecast, accordingly, challenging spend and championing future sustainability through increased income and expenditure savings. We are working with RFAC to model alternative assumptions, identify pressure/decision points, and further explore how we secure financial stability, and will report to the Board in March 2020

**Aleks Bennett - EM3 Finance Manager**  
30 January 2020