Inflation Briefing Session

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HILLINGDON
LONDON

Doom & Gloom!

It is hard to predict the future, but we think it's likely to reach around 10% this year and go down next year. We expect it to be close to 2% in around two years – *Bank of England*

Rising prices will add to already-significant UK inflation – now expected to peak at a forty-year high of 8.5% in April, up from the 7.2% peak predicted by the *Winter Forecast*. The EY ITEM Club expects inflation to still be close to 6% by the end of 2022, and to not fall back in line with the Bank of England's 2% target until late-2023

Higher global energy prices will feed through to higher domestic prices over the course of 2022, with CPI inflation now forecast to peak at close to 9 per cent in the fourth quarter of this year – *Office for Budget Responsibility*

Economic escalation scenario: UK inflation hits a 40 year high of around 11% in Q4 2022, with the energy price cap to increase by around 75% - *PWC*

Highways Term Contract - annual contracted uplift request of 25.3% average

Social Care - 67 requests received with an average of 14.1% being requested

GoodShape Absence Management Service 20% Uplift request as part of contract re-award

Gas price up 134% and Electricity up 64% from April 1st

Tree Maintenance 55% Uplift request on contract extension

Diesel fuel – up over 30% in the last 12 months

What it means for LBH & its finances

- 2022/23 budget built around assumption of 5% CPI with £12m inflationary uplifts (up from less than £5m in 2021/22), higher and longer "spike" will increase this requirement
- Of the Council's £251m budget for the year, funding is already locked in – with Council Tax having been raised by 1.9% and grant funding set for the year
- With an £11m Savings Programme already in place to deliver balanced budget for the year, and core funding locked in for the year, any additional costs will represent a call on the Council's balances (a finite resource)
- Over the medium term, planning for inflationary pressures to increase the £31m savings required by 2026/27, with any measures we can implement to curtail cost increases contributing towards securing balanced budgets
- Note that budgets are held for particular purpose and that these new inflationary pressures represent a step change from approved budgets which will need to be funded

What do we do about it?

Understand what is being requested and why? Knowledge of your suppliers, the markets they operate in and their cost chain will all help you navigate any fee uplift requests.

Challenge any supplier uplift requests. Depending on the size of the request, the validity of the justification, the evidence they have shared, the nature of our relationship with them will all be factors in how hard you push back against their request.

Manage the requests. You have the detail and challenged the supplier, but the next step is about understanding what you are going to do about it. Are you going to ‘pay up’ or try and mitigate some of the increase by reviewing how and what you’re are buying.

Track what is being agreed. If you are agreeing to an increase or specific mitigation that has operational or governance impact, you need to make sure you have the relevant approval.

Core Principles

We acknowledge that price pressures on our suppliers are increasing and inevitably they will want to try and shift those pressures to their customers – ie LB Hillingdon

Whilst we want to resist proposed increases, we also need our suppliers to remain viable. The risk of supplier failure could be substantially more costly and resource intensive than an increase with the incumbent supplier.

The pressures on Council finances are also significant and we receive no additional monies to manage inflationary pressures. Although provision has been made for inflation within budgets, the current situation and forecast levels have not been accounted for and will need to come out of other budgets.

Fee uplifts are for Budget Holders to manage. Procurement and Finance colleagues will support in challenging suppliers, considering alternatives / mitigations and tracking any increases.

Every situation will be governed by very different factors and needs an individual approach – e.g. nature of relationship (transactional v strategic) balance of power (will we be able to push back against the supplier) nature of uplift (commodity driven and trackable or general) alternative options (can we walk away or retender or are we tied in to a supplier) when the last increase was requested and granted. (Recently or not for several years)

Any increase request needs to be justified to LBH in writing - setting out what the increase is and supporting narrative of why. The request for uplift cannot be general and should be specific linked to the contract. For example;

- *15% of our contract spend is on fuel and these prices have risen 'x' percent in the last 'x' months.*
- *We employ 'x' people on your contract and their pay has increase in line with National Living contributing to an 'x' % increase in overall costs*
- *40% of our costs are building material costs and based on Construction Building Material Index they have risen on average 'x' percent since the start of the contract*

Core Principles

Subject to the exact wording, uplift requests embedded in contracts will likely have to be honoured although the relevant uplift clause needs to be fully understood. If it is not considered reasonable, then challenge can still be issued, and alternative options should be considered.

Working with colleagues in Finance and Procurement, Budget Managers then need to substantiate the reasoning provided and consider if it is viable – i.e. is it still affordable? What pressure does it put on your budget?

There are a number of strategies you could consider as either short or longer term mitigations:

a. *Change your specification – e.g. components, frequency, service levels etc*
b. *Retender to seek better pricing – perhaps even the threat of a retender may cause uplift requests to be moderated.*
c. *Lock in for longer period at better price*
d. *Can you deliver the service differently in the short term?*
e. *If components of the price pressures are potentially short term (i.e. fuel / energy etc) then these should be identified clearly and should be dealt with on a one off basis to avoid baselining at a higher price.*
f. *Consider what is contributing to demand and take steps to reduce demand*
g. *In longer-term contracts or supplier relationships explore opportunities for "sharing" inflationary pressures between the Council and supplier.*
h. *Defer decision to proceed with contracts and wait for some stability in prices. This might result in more short-term extensions or a decision to defer entirely.*

In order for the Council to manage its overall budget position all requests for uplift need to be approved and managed through the correct process.

Any Questions?