Portsmouth
CITY COUNCIL

Agenda item:

Title of meeting:	Cabinet
Date of meeting:	25 September 2014
Subject:	Purchase of Equity Shares in Municipal Bonds Agency
Report by:	Head of Finance and Section 151 Officer
Wards affected:	All wards
Key decision:	No
Full Council decision:	No

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1. Purpose of report

To obtain the Cabinet's approval to subscribe for £150,000 of shares in the municipal bonds agency.

2. Recommendations

1) That the City Council subscribes for £150,000 of ordinary shares in the Local Capital Finance Company Limited which will operate the municipal bonds agency.
2) That the purchase of the shares be financed from a revenue contribution to capital outlay funded from the contingency provision in the revenue budget.

3. Background

Most local authority borrowing is undertaken with the Public Works Loans Board (PWLB). The PWLB accounts of 97% of the City Council's borrowing. PWLB rates are driven by gilt rates, ie. government borrowing, but include a margin to cover potential losses. PWLB rates were raised to 1% above gilts in 2010 (from 0.2% above gilts previously), subsequently reduced to 0.8% above gilts in 2012. This is an effective increase of 0.6%. The PWLB has a long history of changing the amount, and the rate at which it lends to local authorities.

The Local Government Association (LGA) has proposed to set up a municipal bonds agency. The municipal bonds agency will sell bonds in the capital markets. These are tradable debt instruments where by pension funds, financial institutions and other lenders will lend to the municipal bonds agency. The municipal bonds agency will then lend the funds raised to local authorities. This should increase competition in the market and reduce the cost of local authority borrowing. The LGA estimates the demand for borrowing by local authorities to be between £3bn and £5bn annually over the next 3 years. The LGA estimates that £8m to £10m will be required to cover the launch and early operating costs.

4. Reasons for recommendations

The reason for the recommendations is to help facilitate the establishment of a municipal bonds agency which would offer a number of long term benefits including:

- Cheaper access to borrowing for local authorities - expected to be between 20 to 25 basis points (or £20,000 p.a. to £25,000 p.a. per £10m borrowed or £600,00 to £750,000 over the life of a 30 year loan;
- Loans from the municipal bonds agency should be cheaper to reschedule (ie. redeem and replace);
- Increased opportunities for local authorities to lend to each other;
- The ordinary shares purchased in the Agency may provide a dividend in future years
- Insulate local authorities from future policy changes by the PWLB regarding interest rates.

5. Equality impact assessment (EIA)

The contents of this report do not have any relevant equalities impact and therefore an equalities assessment is not required.

6. Legal Implications

The Section 151 Officer is required by the Local Government Act 1972 and by the Accounts and Audit Regulations 2011 to ensure that the Council's budgeting, financial management, and accounting practices meet the relevant statutory and professional requirements. Members must have regard to and be aware of the wider duties placed on the Council by various statutes governing the conduct of its financial affairs.

7. Finance Comments

The purchase of shares in the municipal bonds agency will score as capital expenditure. This will need to be financed by revenue contributions to capital expenditure funded from the contingency provision.

The Council's investment should bring financial benefits as set out in paragraph 4, but it is not possible to quantify the returns on the Council's investment because the dividends generated by the ordinary shares purchased are not known. Indefinite long term savings on the Council's borrowing are possible, but these will not accrue until the Council needs to borrow.

There are a number of risks that may ultimately prevent the establishment of a municipal bonds agency including:

- Being unable to raise the required level of operating capital of £8m to £10m;
- Local authority demand for the agency may not materialise;
- The market pricing for the bond issuance may not be attractive;
- The agency may not be able to attract personnel of sufficient calibre on a timely basis.

If the municipal bonds agency does not come to fruition any funds that have been spent on establishing the agency will be lost. The extent of the loss will depend on the point at which the establishment of the agency is abandoned and the amount of expenditure incurred up until that point. Any unspent funds will be returned to the shareholders.

A further risk is that the PWLB may reduce its margin over gilts sufficiently to render the municipal bonds agency an unattractive choice for local authority borrowing. However, if the municipal bonds agency does not go ahead because it is priced out of the market by the PWLB, the Council will have achieved its objective of lower borrowing costs.

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Signed by Head of Financial Services and Section 151 Officer

Appendices:

Background list of documents: Section 100D of the Local Government Act 1972

The following documents disclose facts or matters, which have been relied upon to a material extent by the author in preparing this report:

Title of document	**Location**
Local Capital Finance Company Limited Information Memorandum	Financial Services

The recommendation(s) set out above were approved/ approved as amended/ deferred/ rejected by the Cabinet on 25 September 2014.

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Signed by the Leader