

## Notice of KEY Executive Decision

<b>Subject Heading:</b>	£121m New Fixed Rate Long Term debt for the General Fund Capital Programme from the Public Works Loan Board.
<b>Cabinet Member:</b>	Councillor Roger Ramsey – Cabinet member for Finance and Property
<b>SLT Lead:</b>	Jane West
<b>Report Author and contact details:</b>	Stephen Wild, Mob: 07791 33 5337, Stephen.wild@onesource.co.uk
<b>Policy context:</b>	This decision is in accordance with the Treasury Management Strategy Statement (TMSS) 2021/22 approved by Cabinet on 17 February 2021.
<b>Financial summary:</b>	The 2021/22 interest payable budget is £12.4m and 2020/21 provisional outturn existing long term debt is forecast at £8.304m. It is anticipated that the £121m will be drawn down over the year so expected outturn is c. £11m.
<b>Reason decision is Key</b>	This decision will result in interest payable expenditure increasing by more than £500k. This increase is provided for in the interest payable budget so no adjustment is being proposed.
<b>Date notice given of intended decision:</b>	19 June 2021

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<b>Relevant OSC:</b>	Overview and Scrutiny Board
<b>Is it an urgent decision?</b>	No
<b>Is this decision exempt from being called-in?</b>	No

**The subject matter of this report deals with the following Council Objectives**

Communities making Havering	<input type="checkbox"/>
Places making Havering	<input type="checkbox"/>
Opportunities making Havering	<input type="checkbox"/>
Connections making Havering	<input type="checkbox"/>

***Place an X in the [] as appropriate***

## Part A – Report seeking decision

### DETAIL OF THE DECISION REQUESTED AND RECOMMENDED ACTION

- 1.1 The authority's Treasury Management Strategy Statement (TMSS) ensures the capital programme is affordable and sustainable, updated annually and approved by Full Council. A key consideration in minimising capital financing costs and protecting the Budget Strategy is the timing and execution of long term borrowing toward the funding of long life assets.
- 1.2 Unlike the HRA, General Fund (GF) long term borrowing has not kept pace with the growth in its capital programme's capital financing requirement (CFR) over a number of years culminating in £121m being funded from the authority's cash balances as at 31/3/20, otherwise described as internal borrowing – see **appendix 1**. Treasury officers have taken advantage of the lower PWLB HRA rate to borrow £65m in the past two years – the General Fund PWLB Certainty rate had until November 2020 been one percentage higher than the PWLB HRA rate. This report recommends that it is timely to re-balance the funding of the General Fund capital programme with long term debt and lock in new borrowing while long term fixed rates remain at historically low levels.
- 1.3 The TMSS borrowing strategy sets out the circumstances when internal borrowing takes place. Officers have taken advantage of the differential between budgeted long term rate (3.5%) and cheaper short term rates to release significant revenue savings to the Budget Strategy - £3m in 2020/21 alone. It should be noted cash investment returns have fallen sharply due to the bank rate plunging to 0.1% while inflation has jumped to 2% thus eroding the real value of cash. Internal borrowing, however can only be a short term initiative as it must ultimately be replaced with long term borrowing typically linked to the life of the assets it is financing - the bulk of the authority's cash being ring-fenced for a specific purpose and not to be locked up permanently to fund the capital programme.
- 1.4 Moreover faced with a significant increase in prudential borrowing requirement over the medium term (£705m over the next 4 years) it is anticipated later this year the authority's cash investment balances will drop to the minimum level (£30m-£50m) necessary to protect the authority against any liquidity shocks. In the absence of drawing long term debt the authority will be forced to raise temporary debt through the financial markets thereby adding complexity and increasing the risk of short term interest rate volatility and refinancing risk.
- 1.5 The approved 2021/22 TMSS suggests that if long term rates are likely to increase then it is necessary to start taking down long term fixed rate debt to protect the Budget Strategy from short term interest rate volatility.
- 1.6 Long term Interest rates have moved significantly higher than what was forecast in the 2021/22 approved TMSS where the 25Y PWLB rate (1.60%) and the 50Y PWLB rate (1.40%) were expected to remain unchanged until March 2022. The authority's treasury adviser's (Link) latest interest rate outlook (10/05/21) expect Bank rate to remain at 0.1% to March 2023 and the longer term rates to show a

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gradual increase – e.g. 50Y rate expected to rise to 2.10% in December 2021 and 2.2% in March 2022. Table 1 shows the movement in the last 6 months:

Table 1: PWLB New Long Term Fixed Rate Maturity loans (Certainty Rate)

	5Y	10Y	25Y	50Y
04/01/21	0.95	1.04	1.55	1.35
26/02/21	1.05	1.53	2.00	2.05
24/03/21	1.14	1.65	2.13	1.94
25/06/21	1.24	1.71	2.08	1.89

- 1.7 The main uplift occurred in February when the Bank of England (BoE) signalled a slowing down of their bond purchasing programme. CPI annual Inflation jumped from 0.4% in February to 2.1% in May, a much faster rise than the BoE expected. The BoE expected inflation to rise by 2.5% in December and then ease back to its target rate of 2% by mid-2022. With the unlocking of C19 restrictions there has been a sharp increase in economic activity that has stoked inflation.
- 1.8 The markets are sticking (for now) to that BoE view, but the risk the BoE is underestimating inflation and the uncertainty around how it might respond are increasing- there is a danger that the bond market on which PWLB rates are based will price in higher medium term inflation which has the potential to move longer term rates upwards.
- 1.9 The S151 is of the view that it is timely to take £121m fixed rate long term PWLB debt over the near term to fund the GF capital programme to mitigate changing economic circumstances and increased uncertainty. This borrowing amount reflects what has been spent rather than what is forecast. Link have advised that the S151 officer should have the flexibility to draw down long term debt quickly should the markets change suddenly.
- 1.10 Officers are undertaking more work to test the accuracy of the borrowing forecasts and cash flow forecasts – on completion a further report may be produced setting out a further borrowing proposal for the HRA/GF.
- 1.11 The S151 Officer has delegated powers to make this borrowing decision. and it is proposed that the following fixed rate borrowing takes place based on current PWLB interest rates – the duration and amount of loans within the overall £56m limit taken may change as PWLB interest rates across different periods change.

Table 2: Proposed new LT borrowing for the GF-Regen schemes

Period	Duration	Amount ( £)	PWLB rates*
2029-30	9 years	19,000,000	1.64
2031-32	10 years	0.00	1.71
2032-33	11 years	8,500,000	1.78
2033-34	12 years	... 8,500,000	1.83
2033-34	13 years	20,000,000	1.88
<b>Total</b>		<b>56,000,000</b>	

\* Rates at 25/06/21

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- 1.12 The loans are typically shorter in duration to reflect the fact that Regen' schemes may have a shorter life than those belonging to the main scheme. The durations selected above reflect the shape of the PWLB yield curve and the authority's debt maturity curve. It is proposed that officers will draw down above loans while rates remain below the budgeted rate of 3.50% and at a timing when market conditions are most favourable. This debt is likely to be drawn down before the financial year end 2021/22.
- 1.13 This decision will provide certainty with regard to the financing costs of existing regeneration schemes. In addition it will free up liquid capital that has been earmarked for a specific purpose and help maintain general cash reserves.
- 1.14 Based on the Authority's debt maturity profile and following consultation with Link it is recommended borrowing new fixed term loans from PWLB on maturity as follows

Table 3: Proposed LT borrowing for GF main schemes.

Period	Duration	Amount ( £)	PWLB rates
2072-73	50 years	40,000,000	1.89
2067-68	46 years	25,000,000	1.92
<b>Total</b>		<b>65,000,000</b>	

- 1.15 It is proposed that this borrowing takes place on a phased basis during 2021/22 to minimise carry costs while rates remain below the budgeted rate of 3.5%.
- 1.16 A key consideration on how much debt will be drawn down will be the impact it will have on level of future cash balances and the carry cost of holding debt pending application

### **Recommendation**

That the S151 Officers executes new long-term fixed rate PWLB borrowing of £121m (£56m on GF Regen schemes and £65m on GF main schemes) as market conditions permit.

## **AUTHORITY UNDER WHICH DECISION IS MADE**

### **Extract from Joint Committee Scheme of Delegations:**

The Chief Operating Officer (Classified as Level A) has delegated responsibility for the Council's treasury management activities as noted below:

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B10: Manage the participating Authority's' loan debt (including borrowing, investing or lending money on the behalf of the Authority), investments, and temporary investments, and pension fund, insurance fund, act as registrar of loan instruments. Manage all banking arrangements including numbers and types of accounts at all times subject to compliance to the financial procedures, Treasury Management Policy Statement and borrowing limits and Prudential Code.

B11; Approve all loans in accordance with the participating Authority's financial regulations and procedures.

B12: Prepare, propose and implement a treasury management policy statement, annual strategies pursuant to the participating Authority's financial regulations and procedures.

## **STATEMENT OF THE REASONS FOR THE DECISION**

By taking new fixed rate long-term borrowing to fund the capital programme the authority is able to bring a measure of certainty to its debt financing costs and the authority's Budget Strategy. Link have recommended that given the heightened volatility in the bond and the PWLB market that officers be given the flexibility to move quickly on drawing down long term fixed rate PWLB debt as the market changes. The amount of long term fixed rate borrowing £121m is limited to the amount of internal borrowing used on historical General Funding capital expenditure that has already been through an assessment process and approved under the Authorities governance procedures.

The Authority's approved 2021/22 TMSS stated that officers be given authority to draw down long term debt if there was a reasonable likelihood that the outlook on long term interest rates might rise above what was planned. The recommendations in this report are a measured response to that market outlook.

It is not proposed to take down long term debt against future capital expenditure until there is more certainty about the profile of the capital programme.

## **OTHER OPTIONS CONSIDERED AND REJECTED**

PWLB is the cheapest (Gilt+ 80Bps) and quickest method of raising capital finance to fund historical capital expenditure as detailed in the table below.

Repayment of debt on maturity is preferred over other PWLB options as that is will have the lowest impact on the Authorities revenue account.

<b>Borrowin g Type</b>	<b>Partner</b>	<b>Pro's</b>	<b>Con's</b>	<b>Costs</b>
<b>PWLB</b>	N/A – LA calls/email	• Simple process/application	• Cannot defer drawdown of	• PWLB brokerage fees apply (0.035%)

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	DMO directly	<ul style="list-style-type: none"> <li>• Money arrives in 2 working days</li> <li>• Minimal paperwork</li> <li>• Can borrow between 1-50 years on Maturity, Annuity or Equal Instalments of Principal</li> <li>• Rates for new loans and premature repayment published twice a day</li> <li>• Low costs</li> </ul>	<ul style="list-style-type: none"> <li>• principal to a future date</li> <li>• Structure of loans limited to Maturity, Annuity or Equal Instalments of Principal</li> <li>• PWLB applications are subject to scrutiny by DMO and HM Treasury</li> </ul>	<ul style="list-style-type: none"> <li>• No credit rating required.</li> </ul>
<b>Private placement (bond)</b>	Placement agent/or debt arrangement advisor	<ul style="list-style-type: none"> <li>• Differing maturities. (10-50 years but weighted average life is likely to be between 10-35 years)</li> <li>• Drawdown deferrable (1-4 years subject to lender appetite). Help with savings in respect of the cost of carry.</li> <li>• Repayment profiles can be flexible and tailored to requirements. Include options available under PWLB but also hybrids of maturity and annuity/EIP structures or inflation linked.</li> <li>• Diversification of funding</li> <li>• Access to wide range of long term institutional investors</li> <li>• Deferred drawdown will be priced over the forward gilt and a margin above the spot rate. While higher, will provide future certainty (rate locked in today for drawdown in the future) and help save on the cost of carry</li> <li>• Allows Council to build relationship with investors to utilise for future borrowing requirements.</li> <li>• Can arrange an ESG issue which could reduce the margin/rate on loan</li> </ul>	<ul style="list-style-type: none"> <li>• Transaction costs high but can be spread over life of instrument.</li> <li>• Material arrangement fees which are higher than PWLB</li> <li>• Documentation may need to be negotiated and will need external legal counsel for both borrower and investor</li> <li>• Spot rate likely to be between Gilt + 95-110bps subject to lenders credit assessment so higher than PWLB</li> </ul>	<ul style="list-style-type: none"> <li>• Placement agent/debt arrangement advisor fees</li> <li>• Private credit rating may be required (not published) by credit rating agency</li> <li>• Legal fees for documentation (borrower and investor)</li> </ul>
<b>Public Bond</b>	Bookrunner and debt arrangement advisor	<ul style="list-style-type: none"> <li>• Differing maturities</li> <li>• Diversification of funding</li> <li>• Access to widest range of investors</li> <li>• Indicatively at Gilt + 85-95bps but subject to credit rating and appetite from investor/marketing from Bookrunner.</li> <li>• Allows Council to come back in the future for further funding</li> </ul>	<ul style="list-style-type: none"> <li>• Transaction costs high but can be spread over life of instrument (issuing costs in relation to bond)</li> <li>• High amount needed upfront on day 1 (minimum of £250m needed to be eligible for listing on stock exchange which provides liquidity</li> </ul>	<ul style="list-style-type: none"> <li>• Bookrunner fees apply for successful raising of loan</li> <li>• Public credit rating and ongoing maintenance costs apply</li> <li>• Legal fees for documentation (borrower and bookrunner)</li> </ul>

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		<p>after building relationship with investors</p> <ul style="list-style-type: none"> <li>• Can arrange an ESG issue</li> </ul>	<p>(see retained bond below))</p> <ul style="list-style-type: none"> <li>• Material arrangement fees for which are higher than PWLB</li> <li>• Legal counsel (externally appointed) will be needed for both borrower and bookrunner, Costs picked up by Council</li> <li>• More regulatory reporting as part of a public bond (providing statement of accounts and other documents)</li> <li>• Need to maintain public credit rating during the life of the bond as part of raising the funds</li> <li>• Execution and pricing risk</li> </ul>	
<b>Retained Public Bond</b>	Bookrunner and debt arrangement advisor	<ul style="list-style-type: none"> <li>• As per public bond above</li> <li>• If £250m for example is not needed on day 1, an bond issue can be structured where £250m or more is announced to the market but only £100m is issued to the market and drawdown. The remaining balance of £150m or more is retained for future issue when needed. The retained element can be retained for up to 4 years before it expires. The retained bond allows a quick access to the market with the margin locked in meaning any future issue will be based on the underlying gilt and margin agreed from the initial issue.</li> <li>• Can arrange on a ESG basis.</li> </ul>	<ul style="list-style-type: none"> <li>• Transaction costs high but spread over life of instrument (issuing costs in relation to bond)</li> <li>• Material arrangement fees for which are higher than PWLB</li> <li>• Further fees such as retaining the bond (cost to retain the bond) and potential costs for issuing bonds in the future (bookrunner/advisor fees and any other fees in relation to issuance)</li> <li>• Legal counsel (externally appointed) will be needed for both borrower and bookrunner, Costs picked up by Council</li> <li>• More execution and pricing risk</li> </ul>	<ul style="list-style-type: none"> <li>• Public credit rating and ongoing maintenance costs apply</li> <li>• Legal fees for documentation (borrower and bookrunner)</li> <li>• Other fees from retaining bond (eg Custodian fees)</li> <li>• Further issuance costs if retained element of bond is issued at a future date</li> </ul>
<b>UKMBA</b>	UKMBA and	<ul style="list-style-type: none"> <li>• As per public bond above</li> <li>• Diversification of funding</li> </ul>	<ul style="list-style-type: none"> <li>• Cost of issuing via UKMBA</li> </ul>	A credit rating will be assigned by the



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	appointed book runner(s)	<ul style="list-style-type: none"><li>• Access to wide range of investors</li><li>• Can do single name issue (in LA's own name) like Lancashire CC but may need minimum £250m issue (potential to retain bond for future issuance)</li></ul>	<ul style="list-style-type: none"><li>• Council ability to control events is relinquished to a degree</li><li>• If part of a joint issue, would need to agree period of loan (tenor) and assess implications of the underlying credit assessment of the other joint parties.</li><li>• More execution and pricing risk</li></ul>	UKMBA, the council's ability to influence will be limited. Arrangement and ongoing costs as part of the issue
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### **PRE-DECISION CONSULTATION**

This paper is the culmination of detailed discussions held with the Triangulation Finance group on 15 December 2020 and 10 March 2021 and at the (Link) quarterly strategy meeting held on the 12 January 2021. The S151 called a further meeting with Triangulation Finance Group and Link on 14 May 2021 to discuss the draft borrowing report.

The 20/21 TMSS approved by Cabinet and Full Council provides the strategic context for this report

### **NAME AND JOB TITLE OF STAFF MEMBER ADVISING THE DECISION-MAKER**

Name: Stephen Wild

Designation: Head of Pensions and Treasury

Signature:

Date:

## **Part B - Assessment of implications and risks**

### **LEGAL IMPLICATIONS AND RISKS**

The prudential capital finance system relies on the provisions of Part 1 of the Local Government Act 2003. Under this system, local authorities are allowed to borrow funds for capital investment as long as the borrowing remains within prudential limits.

Regulation 2 of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003/3146 requires the Authority to have regard to the code of practice entitled the “Prudential Code for Capital Finance in Local Authorities” published by CIPFA when considering its duty to keep under review the amount of money the Authority can afford to borrow.

### **FINANCIAL IMPLICATIONS AND RISKS**

The 2021/22 interest payable budget is £12.4m. It is anticipated that the £121m will be drawn down over the year so the expected outturn for 2021/22 is c. £11m, a potential in-year saving of c £1.4m. The planned borrowing is shown in the body of the report at Tables 2 and 3.

The risk from not agreeing the proposal is that long term rates increase and remain at that level imposing additional borrowing costs in future generations. Rates are currently at a historically low level. The proposal will lock in the authority's borrowing costs on regeneration schemes.

The proposals included in the report are compliant with the Council's Treasury Management Strategy for 2021/22 as approved by Council.

### **HUMAN RESOURCES IMPLICATIONS AND RISKS (AND ACCOMMODATION IMPLICATIONS WHERE RELEVANT)**

Non specific

### **EQUALITIES AND SOCIAL INCLUSION IMPLICATIONS AND RISKS**

The Public Sector Equality Duty (PSED) under section 149 of the Equality Act 2010 requires the Council, when exercising its functions, to have ‘due regard’ to:

- (i) The need to eliminate discrimination, harassment, victimisation and any other conduct that is prohibited by or under the Equality Act 2010;
- (ii) The need to advance equality of opportunity between persons who share protected characteristics and those who do not, and;

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(iii) Foster good relations between those who have protected characteristics and those who do not.

Note: 'Protected characteristics' are age, disability, gender reassignment, marriage and civil partnerships, pregnancy and maternity, race, religion or belief, sex/gender, and sexual orientation.

The Council is committed to all of the above in the provision, procurement and commissioning of its services, and the employment of its workforce. In addition, the Council is also committed to improving the quality of life and wellbeing for all Havering residents in respect of socio-economics and health determinants.

## **HEALTH AND WELLBEING IMPLICATIONS AND RISKS**

As stated in paragraph 1.13 the recommendation of this report supports the delivery of existing regenerations schemes that have increased the provision of new and affordable housing. This in-turn provides good standard accommodation in the Borough that has positive health benefits. Moreover it will lock in the gains from regeneration schemes that form part of the authority's budget strategy and are important in helping to deliver and shape services on which the most vulnerable members of the community rely upon. The benefits are detailed more explicitly in the authority's Capital Strategy.

Securing debt at historically low levels may provide cost benefits to the budget for several generations should long term fixed rates return to their higher historical norm. This in turn, is expected to be beneficial in securing long term planned developments which are likely to improve health of the local population.

The risk is that short term rates on investment balances or temporary borrowing remain as they are for much longer and the authority ends up paying higher interest on its debt as a consequence – reducing the level of cost savings on its budget that could be used now to deal with budget pressures. In mitigation this recommendation is a measured response to changing economic circumstances and does not cover the substantial increase in borrowing requirement projected over the next four years in the capital programme.

## **BACKGROUND PAPERS**

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**Part C – Record of decision**

I have made this executive decision in accordance with authority delegated to me by the Leader of the Council and in compliance with the requirements of the Constitution.

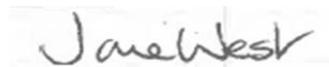
**Decision**

Proposal agreed

*Delete as applicable*

**Details of decision maker**

Signed



Name: Jane West,

Cabinet Portfolio held:

CMT Member title:

Head of Service title

Other manager title: Chief 151 Officer

Date: 22.07.21

**Lodging this notice**

The signed decision notice must be delivered to the proper officer, Debra Marlow, Principal Committee Officer in Democratic Services, in the Town Hall.

**For use by Committee Administration**

This notice was lodged with me on 22<sup>nd</sup> July 2021

Signed:



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### Appendix 1

Table 1: LB Havering Balance Sheet Projections as at 9 June 2021

	31/2/20 £m	31/3/21 £m	31/3/22 £m	31/3/23 £m	31/3/24 £m	31/3/25 £m
	Act	Act*	Est	Est	Est	Est
GF: Main	100	126	157	173	179	175
Regeneration	56	64	136	207	235	243
HRA	197	212	379	499	618	741
<b>Total CFR</b>	<b>353</b>	<b>402</b>	<b>673</b>	<b>879</b>	<b>1,032</b>	<b>1,159</b>
Financed by:						
Cash balances	81	127	179	179	179	179
External: Temp'Debt	38	10	229	435	588	715
LT Debt HRA	200	230	230	230	230	230
LT Debt GF Main	35	35	35	35	35	35

\* Provisional outturn

- 1.2 The GF CFR £156m at 31/3/20 was financed by internal borrowing of £121m. Based on provisional outturn figures at 31/03/21 the GF CFR is £190m financed by internal borrowing of £155m.
- 1.3 Total (CFR), debt is forecast to increase over the next 4 years, from £275m at 31/3/21 to £980m at 31/3/25. In the absence of further long term borrowing then available cash balances will be exhausted and Treasury will need to fund the capital programme from temporary borrowing. :
- 1.4 Looking at the component parts of the (CFR) in detail over the forecast horizon, (4 years) the general fund (GF) main programme increases by £49m, the GF regeneration fund by £179m and finally the HRA account by £529m
- 1.5 The current external debt £265.6m, (£258.2m, PWLB & £7.4m, Market counterparties) has an average fixed rate of 3.412% and an average life of 23.19 years, current PWLB rates for this maturity are 2.35%. PWLB debt repayments peak between 2027 and 2034 averaging approx. £17m p.a. rising to £30m in 2042. This represents 64% of the current total PWLB loans outstanding. Similarly in 2069/2070 a further £55m or 21% of the current external PWLB debt matures.
- 1.6 Considering debt capacity, the (CFR), represents as a percentage of the (Authorised limit) 87.9% in (2020/21), 71.8% in (2021/22), 81.5% in (2022/23), 84.9% in (2023/24) and finally 94.7% in (2024/25).
- 1.7 The authority's cash balances have been steadily declining from £210m at 31/3/20 to £100m (net of temporary debt) at 31 March 2021.
- 1.8 Cash balance investments totalled £140.5m at 02/06/21 – typically high at the start of the year due to front loading of c/tax, business rates, and Government grants, £65m in short term council loans, £35m in liquid Money Market Funds, £40m bank call accounts and short term loans, all maturities < 1year with 25%, £10m < 1 month.

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- 1.9 The authority will need to maintain a liquidity buffer of c. £30m-50m to protect against liquidity shocks and unexpected credit tightening