CIPFA The Chartered Institute of Public Finance & Accountancy

Response to the Consultation on introducing the Local Infrastructure Rate

January 2017

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Local Infrastructure Rate Consultation
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Submitted electronically to localinfrastructurerate@hmtreasury.gsi.gov.uk

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Background

The Prudential Code provides a framework to ensure and demonstrate that local authorities' capital programmes are prudent, affordable and sustainable. The PWLB has been by far the largest source of borrowing for capital investment for local authorities for many years and therefore changes to its interest rate policies have the potential to impact on the sector and the capital market. Given that CIPFA is responsible for the Prudential Code we welcome the opportunity to respond to the consultation paper. The response has been discussed at a recent Treasury and Capital Management Panel meeting.

Responses to the specific consultation questions are detailed below along with associated issues.

Question 1: How would the introduction of the Local Infrastructure Rate at gilts + 60 basis points affect local authorities' infrastructure investment?

A total of £1.5bn was made available for the project rate, although PWLB records suggest that in 2014/5 £141m was advanced, in 2015/16 £417m was advanced, and in 2016/17 (to the end of December 2016), £107m had been advanced at the project rate. Whilst there are inevitably allocations which have yet to be drawn down, that drawn down to the end of December 2016 is less than 45% of the funding that was available. Given that the £1.5bn available at the project rate was only accessible through approved bids by Local Enterprise Partnerships (LEPs), the proposed Local Infrastructure Rate is potentially more accessible given that bids would be considered from principal authorities rather than through LEPs.

In order not to place undue additional burdens on local authorities, it is essential that any bidding process should not add unnecessary bureaucracy. The timing of the bidding process and subsequent decisions on bids should be scheduled in such a way as not to introduce unnecessary uncertainty into the financial planning process.

It would also be helpful to provide clarity on any potential process should a local authority subsequently no longer require their full allocation.

For many authorities, the repayment of borrowing poses more of a pressure than the annual interest costs. Given that the Local Infrastructure Rate is priced the same as the project rate (which will no longer be available), and is only 20bps less than the certainty rate, it is not likely that the availability of the discounted Local Infrastructure Rate will have a significant impact on the affordability of capital projects.

The Prudential Code identifies value for money as one of the factors which local authorities are required to take into account when setting or revising their prudential indicator. Especially in the current times of austerity, it is highly likely that local authorities are only proposing projects which are high value for money.

The proposals suggest that bids would only be considered for projects in the "transport, energy, flood defences, water, waste, and digital communications sectors". This may be restrictive and may exclude some local economic development schemes or public realm schemes which meet the policy objectives.

The current extended period of austerity faced by local authorities has led to the re-assessment of their capital plans. This, coupled with changes in the capital financing regime, such as the move away from supported borrowing to capital grant has led to a position whereby some local authorities have a mismatch between their existing long term borrowing and their current liability benchmark profile (which takes into account core cash requirements, such as the use of reserves). The current repayment margins make it prohibitively expensive for local authorities to repay or reschedule existing borrowing in order to better match their liability benchmark. The potential consequence is over borrowing and the build-up of cash which then leads to additional credit risk. At a time when interest rates were higher, the margin may have been more reasonable. Given the fall in interest rates it is suggested that the margin be reviewed, and in particular, consideration be given to differential rates for different loan periods.

Question 2: How would the introduction of the Local Infrastructure Rate at gilts + 60 basis points impact lenders in the local government debt market?

Given that the PWLB in 2015/16 advanced loans totalling £1,490m to English local authorities and that the £1bn proposed is over a period of 3 years, is the same as the project rate and only 20 basis points lower than the certainty rate, the impact on the local government debt market is likely to be negligible.

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