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OXFORD CITY COUNCIL

To: City Executive Board

Date: 10 September 2015

Report of: Finance Panel (Panel of the Scrutiny Committee)

Title of Report: Municipal Bonds

Summary and Recommendations

Purpose of report: To present recommendations from the Finance Panel following an item on municipal bonds

Scrutiny Lead Member: Councillor Simmons

Executive lead member: Councillor Ed Turner, Executive Member for Finance, Asset Management and Public Health

Recommendation of the Finance Panel to the City Executive Board

That the City Executive Board states whether it agrees or disagrees with the following recommendations:

1. That the City Council welcomes the establishment of the Municipal Bonds Agency as a worthwhile social investment vehicle and source of capital financing.

2. That the City Council doesn't make significant investments in the Municipal Bonds Agency or borrow from it at this stage but keeps a watching brief on the Agency and considers it as a future source of prudential borrowing.

3. That the Executive Member for Finance, in consultation with the Head of Financial Services, considers the case for the City Council making a £10k capital investment to become a minimum shareholder in the Municipal Bonds Agency before its first bond issuance, which is expected to take place in September 2015. This investment would be made with no guarantee of a return but it would secure preferential interest rates on any future Council borrowing. The Executive Member for Finance is asked to report on the outcome of his deliberations at the September City Executive Board meeting.

4. That in considering whether to make a minimal investment (Recommendation 3), the Head of Financial Services speaks with one or more District Councils that have already signed up as shareholders in the Agency.

Appendices

Appendix 1 – Suggested executive response provided by the Board Member

Introduction

1. The Finance Panel convened a discussion on municipal bonds at its public meeting on 2 July 2015. The Panel is grateful to Christian Wall from the Municipal Bonds Agency for attending this meeting to provide a presentation and answer the Panel's questions. The Panel would also like to thank Nigel Kennedy and Anna Winship for contributing to this discussion.

2. This meeting followed on from a previous Finance Panel item on 8 October 2014, where the Panel reviewed documentation on the establishment of the Municipal Bonds Agency and a briefing note from the Head of Financial Services.

Summary of the discussion

3. Christian Wall from the Municipal Bonds Agency provided a presentation which set out the vision, model, credit structure and governance of the Agency, together with an overview of the market for local authority borrowing.

4. The Panel asked how much capital the Agency had raised and heard that it has raised £5.8m against an original target of £8-10m, which would include a buffer to ensure that the Agency was sufficiently capitalised to cover the worst case scenario. The Agency would obtain credit ratings from two agencies once it had secured £6m of capital. It expected to do so imminently and issue bonds in September 2015. The agency would break even once it had issued 1.6-2bn worth of bonds and expected to pay dividends from year 5.

5. In response to a question, the Panel heard that 54 local authorities had signed up to the Agency. The Local Government Association was the largest shareholder, having invested £0.5m and a County Council was the next largest shareholder at £350k. About 12 District Councils had invested the minimum shareholding amount of £10k. Investments were made with no guarantee of a return but they would secure a preferential interest rate on future borrowing.

6. The Panel heard that local authorities that had expressed an interest in the Agency but opted not to sign up had done so because they didn't need to borrow, not because they had a problem with the concept.

7. The Panel asked how long local authorities needed to hold shares for in order to obtain a preferential interest rate. The Panel heard that the preferential rate was not dependent on the amount invested or how long shares were held for, so long as the investment was made before the first bond issuance.

8. The Agency's directors were still to agree the level of the premium on borrowing for local authorities that joined later. The Agency aimed to provide preferential and non-preferential interest rates that were both lower than that offered by the Public Works Loan Board (PWLB) (currently 80 basis points). The Agency expected its rates to track the PWLB rate over time, as Transport for London had done, so there would still be an incentive for non-shareholding local authorities to borrow from the Agency rather than the PWLB, even if the PWLB lowered their rate.

9. The Panel noted that Council's Housing Revenue Account (HRA) included borrowing in future years. In recent years, the Council's borrowing requirements had been met through internal borrowing. However, it was possible that recent national policy changes would result in substantial changes to the Council's HRA business plan and potentially, the Council's future borrowing requirements.

Recommendations:

1. That the City Council welcomes the establishment of the Municipal Bonds Agency as a worthwhile social investment vehicle and source of capital financing.

2. That the City Council doesn't make significant investments in the Municipal Bonds Agency or borrow from it at this stage but keeps a watching brief on the Agency and considers it as a future source of prudential borrowing.

3. That the Executive Member for Finance, in consultation with the Head of Financial Services, considers the case for the City Council making a £10k capital investment to become a minimum shareholder in the Municipal Bonds Agency before its first bond issuance, which is expected to take place in September 2015. This investment would be made with no guarantee of a return but it would secure preferential interest rates on any future Council borrowing. The Executive Member for Finance is asked to report on the outcome of his deliberations at the September City Executive Board meeting.

4. That in considering whether to make a minimal investment (Recommendation 3), the Head of Financial Services speaks with one or more District Councils that have already signed up as shareholders in the Agency.

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List of background papers: None
Version number: 2.0

Suggested executive response provided by the Board Member for Finance, Asset Management and Public Health

Recommendation	***Agreed? (Y / N / In part)***	***Comment***	***Board Member / Lead Officer***
1. That the City Council welcomes the establishment of the Municipal Bonds Agency as a worthwhile social investment vehicle and source of capital financing.	Y	Agreed. The City Council welcomes the establishment as an alternative source of financing to PWLB	Cllr Ed Turner / Nigel Kennedy
2. That the City Council doesn’t make significant investments in the Municipal Bonds Agency or borrow from it at this stage but keeps a watching brief on the Agency and considers it as a future source of prudential borrowing.	Y	Agreed. There is still some uncertainty about the rate of return any investor would get from investing in the Municipal Bond Agency if indeed there would be any at all. There are no plans to undertake prudential borrowing in the immediate future to fund capital expenditure and given latest announcements from the Chancellors Budget in July the authority will be looking to reassess all its future spending plans. When and if the authority has a requirement to borrow then it will consider all sources of finance.	Cllr Ed Turner / Nigel Kennedy
3. That the Executive Member for Finance, in consultation with the Head of Financial Services, considers the case for the City Council making a £10k capital investment to become a minimum shareholder in the Municipal Bonds Agency before its first bond issuance, which is expected to take place in September 2015. This investment would be made with no guarantee of a return but it would secure preferential interest rates on any future Council borrowing.	In Part	There still remains uncertainty as to the rationale behind investing in the MBA since the Council currently has no requirement to borrow in the immediate future. The preferential rate referred to (and mentioned at the Finance Panel by the representative of the MBA) is not referred to in any of the documentation submitted to the Council and therefore cannot be validated. Information obtained from the Council Treasury advisors, Capita suggest that there remains a number of unanswered questions • Early paperwork from the MBA referred to a ‘new issue premium’ in the first year or two, it is uncertain whether early joiner borrowing authorities would voluntarily pay a higher interest rate	Cllr Ed Turner / Nigel Kennedy

		• There is a joint and several guarantee for investors, whilst this would presumably be in proportion to holding there may be a risk to the authority • How flexible can the agency be around bond maturities and how will ensure that its meets the requirements of its customers in terms of size, duration and interest rate. • The MBA representative mentioned that the preferential rate for investors would be 2 or 3 basis points below the preferential bond rate for other investors (although this is by no means certain). Additionally rates move quickly and this differential could be wiped out quickly even before the overall costs of the bond are taken into consideration. Due to the level of uncertainties although a £10k 'hedge' may be seen as relatively small in the scale of the Council's overall finances there are a number of important questions which need to be answered before such funds should be committed. Officers will undertake to investigate answers to these questions and either commit £10k if the answers suggest investment would be in the interests of the Council, or report back to CEB and Scrutiny within the next three months with the outcome of the investigation.	
4. That in considering whether to make a minimal investment (Recommendation 3), the Head of Financial Services speaks with one or more District Councils that have already signed up as shareholders in the Agency.	In part	The MBA advise that there are 10 authorities who have invested £10k with the fund although it is not known who they are. To some extent it is irrelevant as to the reason why other authorities have invested in the fund since it is a matter of judgement for the Section 151 Officer of this authority in consultation with the Finance and Asset Portfolio Holder to decide whether to invest.	Cllr Ed Turner / Nigel Kennedy

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