Appendix 7c – Borrowing Strategy

1. Introduction

1.1 The Borrowing Strategy is prepared in accordance with a professional code of practice (the CIPFA Code of Practice and Cross-Sectoral Guidance Notes on Treasury Management – 2021 Edition). Revised reporting requirements from the newly published 2021 Edition of the guidance notes.

1.2 It includes the following:

- The Council's debt and investment projections (section 2).
- The expected movement in interest rates (section 3).
- The Council's borrowing strategy (section 4).
- The Council's policy on borrowing in advance of need (section 5).
- The Council's approach to debt rescheduling (section 6).
- The Council's Lender Option Buyer Option (LOBO) strategy (section 7).

2. Debt and Investment Projections 2023/24 – 2026/27

2.1 The borrowing requirement comprises the expected movement in the Capital Financing Requirement (CFR in the table below) and any maturing debt which will need to be re-financed. The table below shows this effect on the treasury position over the next three years. It also highlights the expected change in investment balances:

£'000s	2023/24 Revised	2024/25 Projection	2025/26 Projection	2026/27 Projection
External Debt				
Long-term debt at 1 April	200,286	183,773	229,594	248,671
Repaid Debt	(16,513)	(4,179)	(923)	(923)
Replacement of maturing debt	-	50,000	20,000	18,350
Additional long-term debt	-	-	-	-
Long-term debt at 31 March	**183,773**	**229,594**	**248,671**	**266,098**
Short-term debt at 31 March	273,900	282,907	312,259	306,634
PFI and Other Liabilities	95,725	77,005	72,410	67,365
Total external debt at 31 March	**553,399**	**589,506**	**633,340**	**640,097**
Annual change in debt	**61,427**	**36,107**	**43,834**	**6,757**
Investments	(21,728)	-	-	-
Total investments at 31 March	**(21,728)**	**-**	**-**	**-**
Investment change	**(21,728)**	**21,728**		
Change in debt less investment	39,699	57,835	43,834	6,757
Annual change in CFR (annex E 3.3.)	**68,876**	**48,143**	**38,360**	**1,748**

2.2 The additional long-term debt includes any borrowing in advance and catch-up borrowing. The related impact of the above movements on the revenue budget are:

£'000s	2023/24 Revised	2024/25 Projection	2025/26 Projection	2026/27 Projection
Revenue Budget				
Interest on long-term loans	6,790	10,992	10,128	10,761
Interest on short-term loans	7,684	13,448	11,916	13,099
Total Interest Costs	**14,474**	**24,440**	**22,044**	**23,860**
General Fund long-term borrowing cost	7,000	10,678	9,718	10,339
HRA long-term borrowing cost	318	314	409	422
Investment income/internal financing	(845)	(150)	(150)	(150)

3. Expected Movements in Interest Rates

3.1 The Bank of England Base Rate has been increasing rates from 4.25% at 1st April 2023 to 5.25% in December 2023. Rates are expected to stay at a similar level for the rest of the financial year 2023/24. The Bank Rate forecasts produced by the Office of Budget Responsibility in November 2023 are as follows:

- 2023/24 5.30%
- 2024/25 4.99%
- 2025/26 4.44%
- 2026/27 4.16%

3.2 Market expectations of Long Term Interest Rates are estimated to be:

PWLB Certainty Borrowing Rates				
Indicative %	**5 Year**	**10 Year**	**25 Year**	**50 Year**
2023/24 Actual (December 2022)	4.82%	4.47%	4.93%	5.27%
2024/25	4.56%	4.21%	4.67%	5.01%
2025/26	4.01%	3.66%	4.12%	4.46%
2026/27	3.73%	3.38%	3.84%	4.18%

The Treasury Management Panel attempt to keep Short-Term Borrowing and Long-Term Borrowing broadly at a 50/50 split, however due to the dramatic increase in interest rates in 23/24, the Treasury Management Panel have agreed that it would be more beneficial to borrow on a short-term basis in 24/25 with the hope to use Long-Term Borrowing in the future as interest rates are forecast to decline.

3.3 These assumptions have been used to determine the treasury management budget projections, included as part of the 2024/25 revenue budget and future year projections.

3.4 The Covid-19 pandemic, the war in Ukraine as well as global supply shortages have had a significant impact on the UK and global economy. In April 2022, the base rate stood at 0.75% and has subsequently been increased to 5.25% on 14th December 2023 in an effort to curb inflation. Some money market investment rates for temporary surplus cash balances have increased in line with the base rate increases, however it has been agreed by the Treasury Management Panel to repay the money market loans that increased their base rate. The current rate for three month fixed term deposit with the Debt Management Office is 5.18%

3.5 Long-term borrowing rates, influenced by gilt yields, have fluctuated over the year, peaking in September. Market expectations are that long-term rates will continually decrease throughout 2024 in line with forecast base rate falls.

4. Borrowing Strategy

4.1 The Council borrows for one of two purposes – to finance cash flow in the short-term or to fund capital investment over the longer term. The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully financed either with long-term loans or with temporary borrowing. This however is unlikely to be sustained in the future as the Council's reserves and cash balances have been significantly depleted over recent years.

4.2 A key aim of the Borrowing Strategy is to minimize the cost of the Council's loan portfolio whilst ensuring that the obligation to repay loans is matched with the benefit received from expenditure incurred on the capital programme.

4.4 The approved sources of long-term and short-term borrowing will be:

- Public Works Loan Board
- UK Local Authorities
- Pension Funds
- Public Corporations
- UK Municipal Bond Agency (see paragraph 4.7 below for further details)
- Any institution approved for investments

4.5 As stated above in paragraph 3.4, the interest rate environment continues to be uncertain and the Bank of England expects that interest rates will start to decrease throughout the period covered by this report. The Treasury Management Panel, under delegated powers, will take the most appropriate form of borrowing in this uncertain economic environment depending on the prevailing interest rates at the time.

4.6 In order to borrow from the PWLB, the council must submit a high-level description of capital financing plans for the following three years. As part of this, to be granted a loan the Director of Resources must confirm there is no intention to buy investments primarily for yield at any point within the next three years regardless of whether the transaction would be notionally financed from a source other than the PWLB. To secure the lowest cost of borrowing Blackpool Council has agreed to disclose estimates of its capital transactions including new borrowing and planned capital to Her Majesty's Treasury. The disclosure of this information in summary format entitles the Council to receive a 20 basis point discount on all new loans borrowed from the Public Works Loan Board during the next 12 months. The information provided to Her Majesty's Treasury is updated annually.

4.7 Along with other local authorities the Council became a shareholder in the UK Municipal Bond Agency (UK MBA) and is part of the UK MBA Working Group. The council saw this as a viable alternative to borrowing from the PWLB. The UK MBA issued its first bond on 5th March 2020 on behalf of Lancashire County Council for a total of £350 million and then a further £250 million bond issuance was completed in August 2020.

5. Policy On Borrowing In Advance Of Need

5.1 The Council will not borrow more than or in advance of its needs, purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates, and will be considered carefully to ensure value for money can be demonstrated and that the Council can ensure the security of such funds.

5.2 In determining whether borrowing will be undertaken in advance of need the Council will:

- ensure that there is a clear link between the capital programme and maturity profile of the existing debt portfolio, which supports the need to take funding in advance of need;
- ensure the ongoing revenue liabilities created, and the implications for the future plans and budgets have been considered;
- evaluate the economic and market factors that might influence the manner and timing of any decision to borrow;
- consider the merits and demerits of alternative forms of funding;
- consider the alternative interest rate bases available, the most appropriate periods to fund and repayment profiles to use;
- consider the impact of borrowing in advance (until required to finance capital expenditure) increasing investment cash balances and the consequent increase in exposure to counterparty risk and the level of such risks given the controls in place to minimise them. Any risks arising will be reported via the mid-year or annual reporting mechanism.

6. Debt Rescheduling

6.1 The introduction by the PWLB in 2007 of a spread between the rates applied to new borrowing and repayment of debt (which has now been compounded since 20 October 2010 by a considerable further widening of the difference between new borrowing and repayment rates) has meant that PWLB to PWLB debt restructuring is now much less attractive than before these events. In particular, consideration would have to be given to the large premiums, which would be incurred by prematurely repaying existing PWLB loans and it is very unlikely that these could be justified on value for money grounds if using replacement PWLB refinancing. However, some interest savings may still be achievable through using other local authority loans and market loans in rescheduling exercises rather than using PWLB borrowing as the source of replacement financing.

6.2 As short-term borrowing rates are currently considerably cheaper than longer term fixed interest rates, there may be potential opportunities to generate savings by switching from long term debt to short term debt. However, these savings will need to be considered in the light of the current treasury position and the size of the cost of debt repayment (premiums incurred).

6.3 The reasons for any rescheduling to take place will include:

(a) The generation of cash savings and / or discounted cash flow savings;
(b) Help fulfil the borrowing strategy outlined above;
(c) Enhance the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

6.4 Consideration will also be given to identify if there is any residual potential for making savings by running down investment balances to repay debt prematurely as short term rates on investments are likely to be lower than rates paid on current debt.

6.5 Any decision taken on rescheduling existing long-term debt will be made by the Treasury Management Panel.

7. Lender Option Borrower Option debt (LOBOs)

7.1 LOBOs typically carry a cheaper initial rate of interest than new debt available from other sources. They are structured with an initial period in which a fixed rate of interest is paid, followed by a much longer 'variable' period. During this period at the agreed 'call' dates (typically between every six months to every five years) the Lender has the option to increase the interest rate. If the Lender exercises their Option to increase the rate, the Borrower has the Option to repay the debt.

7.2 When general interest rates are rising, the interest the Council pays on its LOBOs will tend to ratchet up at call dates, lagging just below other available market rates. The higher rate chosen by the lender is always likely to be enticingly below other immediately available market rates so that at the decision points when the borrower has the option to repay, it will be seduced into a longer relationship with the LOBO at higher rates. However, when general interest rates are falling, the interest the borrower pays on its LOBOs will remain fixed at the higher rates.

7.3 The Treasury Management Panel notes that whenever a lender calls an increase in the rate of a LOBO there will be a great temptation to accept the higher rate and remain tied into the LOBO (as the alternative borrowing is likely to be slightly more expensive in the short term). The Council will continue to take advantage of the beneficial rates available through LOBOs as part of a balanced portfolio of fixed and variable debt, especially through the early fixed period of the instrument.

7.4 The Council's policy is that on every occasion when a lender opts to increase the interest rate on one of its LOBOs there is a presumption that the Council will repay the LOBO.

7.5 In view of the recent bad press on LOBOs the Treasury Management Panel is looking for ways to redeem them whenever favourable opportunities arise. This opportunity has arisen a number of times in 2023/24 and £12m of the £26m LOBO outstanding balances have been paid in 23/24, leaving an outstanding LOBO balance of £14m. The Treasury Management Panel will seek to repay this as and when the opportunity arises.