

SECTOR

An overview of Local Authority borrowing activity in a low interest rate environment

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June 2011

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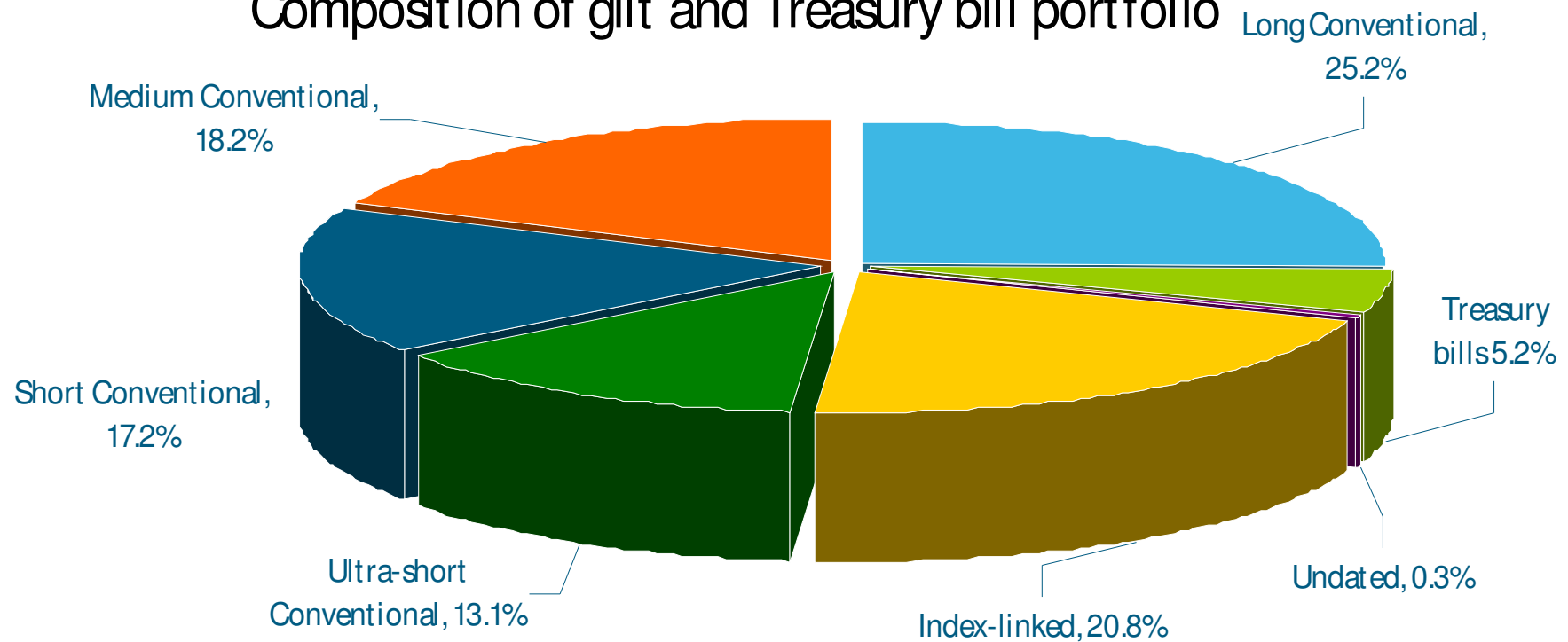
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7. Summary

1. Government debt

Government debt stands at £960bn at 31/12/2010
(net of government holdings, as per DMO Quarterly Report)

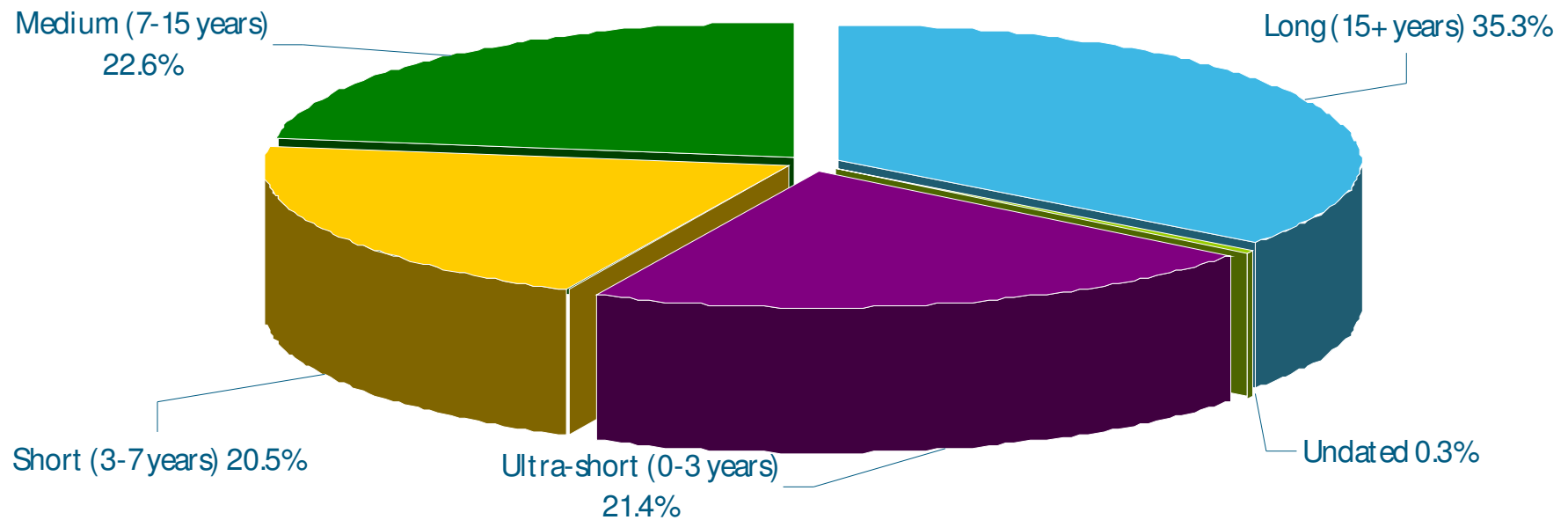
Composition of gilt and Treasury bill portfolio



1. Government debt

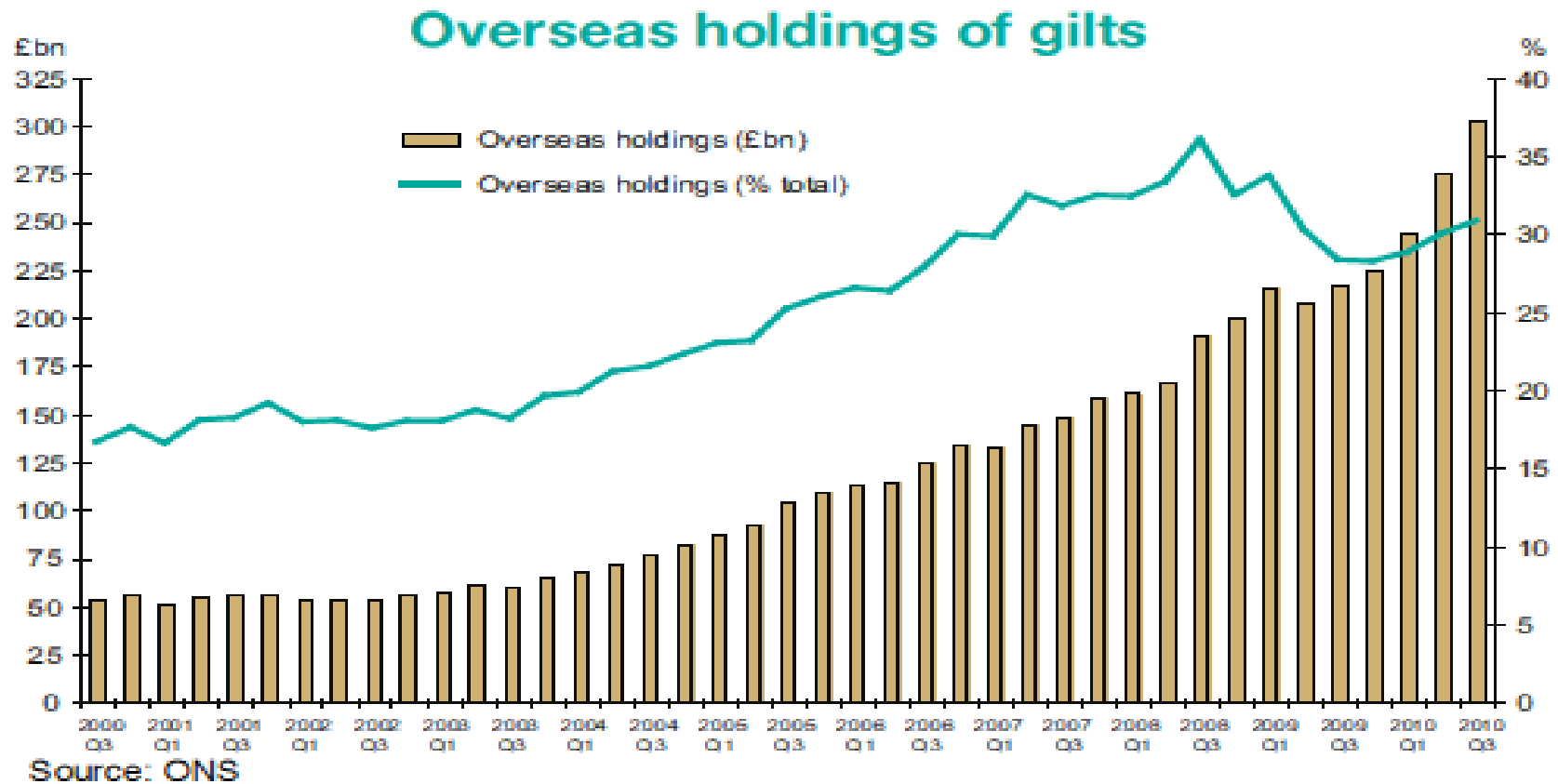
Government debt averages 13.4 years
(including Treasury Bills)

Gilt and Treasury bill portfolio maturity split



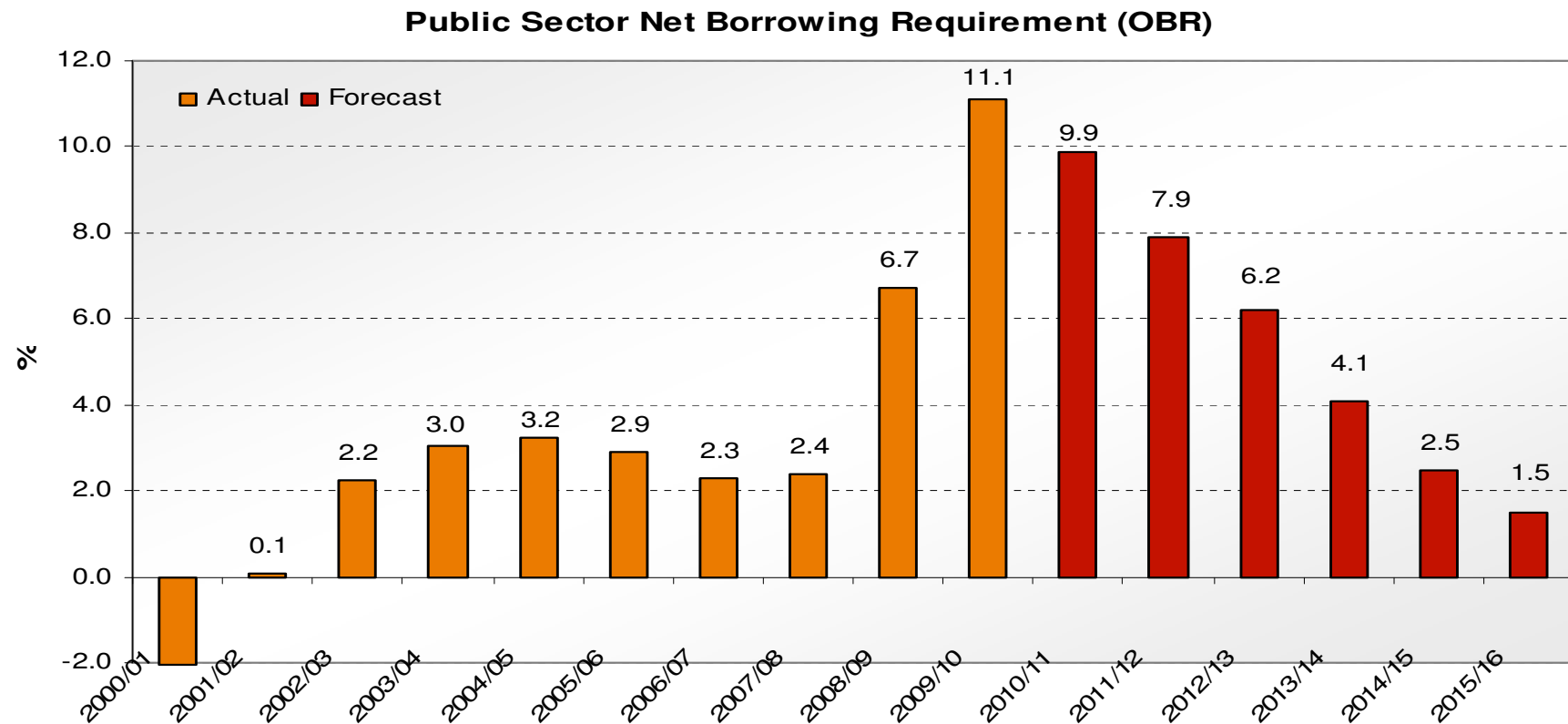
1. Government debt

Government debt susceptible to a change in foreign investor sentiment...so CPI needs to be kept on target



1. Government debt

Government debt borrowing requirement 2011/12



1. Government debt

Government debt borrowing requirement as a % of GDP

Summary of intended gilt issuance 2011/12:

£57.4bn short dated

£34.7bn medium dated

£37.4bn long dated

£38.0bn index linked gilts

£167.5bn total

Funded by:

£131.3bn gilt auctions

£31.6bn gilt syndication

£4.6bn mini tenders

£167.5bn total

2. Local Authority debt

Local Authority borrowing from Public Work Loans Board (March 2011)

Summary of LA PWLB borrowing by
£42.5bn England
£8.0bn Scotland
£2.7bn Wales
£53.2bn total

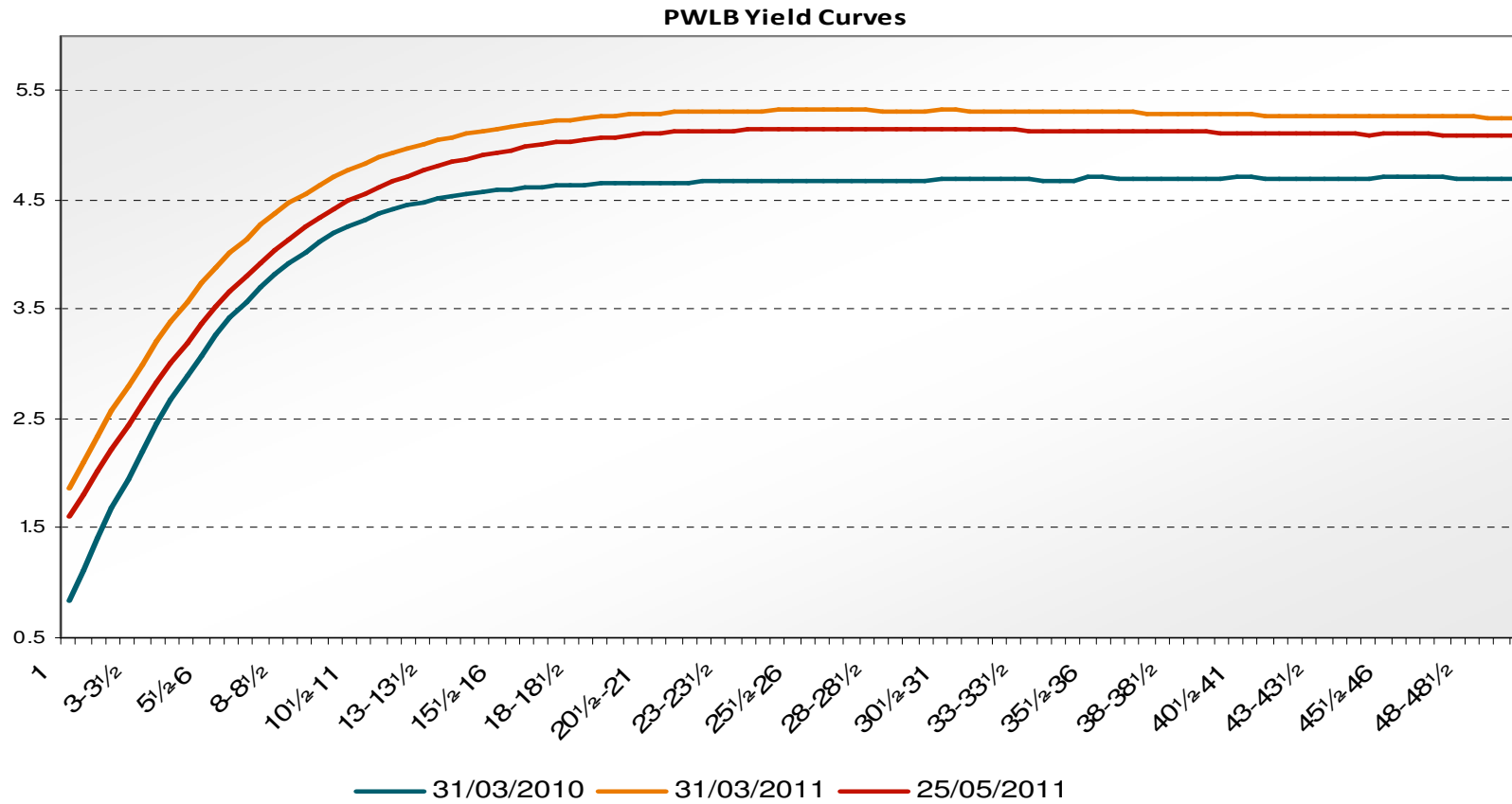
Pretty much
unchanged since
March 2010...why?

3. UK interest rate forecast

Bank Rate													
	NOW	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14
Sector's View	0.50%	0.50%	0.50%	0.75%	1.00%	1.25%	1.50%	1.75%	2.00%	2.25%	2.50%	2.75%	3.00%
UBS	0.50%	0.50%	0.75%	1.00%	1.25%	1.50%	1.75%	2.00%	2.25%	-	-	-	-
Capital Economics	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.75%	1.00%	-
5yr PWLB Rate													
	NOW	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14
Sector's View	3.19%	3.40%	3.55%	3.65%	3.75%	3.90%	4.00%	4.15%	4.25%	4.45%	4.60%	4.65%	4.75%
UBS	3.19%	-	-	-	-	-	-	-	-	-	-	-	-
Capital Economics	3.19%	3.20%	3.20%	3.00%	3.00%	3.00%	3.00%	3.20%	3.20%	3.20%	3.40%	3.60%	-
10yr PWLB Rate													
	NOW	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14
Sector's View	4.42%	4.60%	4.75%	4.75%	4.80%	4.95%	4.95%	5.00%	5.05%	5.15%	5.20%	5.25%	5.25%
UBS	4.42%	4.80%	4.90%	5.00%	5.10%	5.20%	5.30%	5.40%	-	-	-	-	-
Capital Economics	4.42%	4.50%	4.25%	3.75%	3.75%	3.75%	3.75%	3.75%	3.80%	3.80%	3.90%	4.00%	-
25yr PWLB Rate													
	NOW	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14
Sector's View	5.14%	5.30%	5.40%	5.40%	5.40%	5.40%	5.40%	5.45%	5.50%	5.50%	5.50%	5.60%	5.65%
UBS	5.14%	5.45%	5.50%	5.50%	5.55%	5.60%	5.65%	5.65%	-	-	-	-	-
Capital Economics	5.14%	5.20%	4.85%	4.65%	4.65%	4.65%	4.65%	4.65%	4.65%	4.65%	4.75%	4.85%	-
50yr PWLB Rate													
	NOW	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14
Sector's View	5.09%	5.30%	5.40%	5.40%	5.40%	5.40%	5.40%	5.45%	5.50%	5.50%	5.50%	5.60%	5.65%
UBS	5.09%	5.45%	5.60%	5.60%	5.65%	5.70%	5.75%	5.75%	-	-	-	-	-
Capital Economics	5.09%	5.20%	5.20%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.10%	5.20%	-

3. UK interest rate forecast

Prevailing PWLB borrowing rates



4. Determining a debt management strategy



4. Determining a debt management strategy

No universal correct answer

Flattish yield curve – rates to rise

- Consider locking out medium/long term

Flattish yield curve – rates to fall

- Consider holding off fixed borrowing

Inverse yield curve

- Preferential to lock out fixed

Positive yield curve

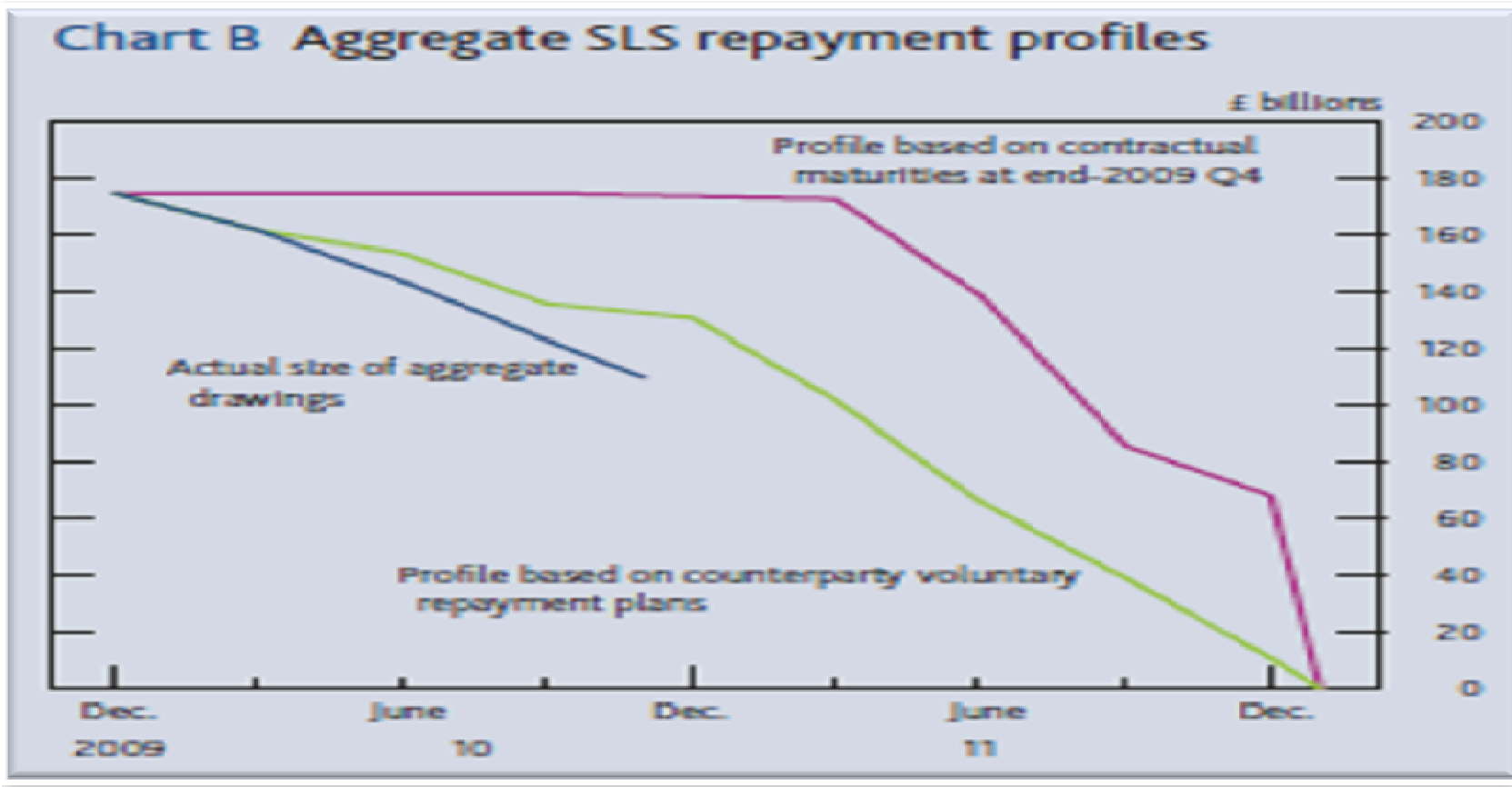
- Preferential to hold short

Don't know!

- Take 1/12 of requirement per month!

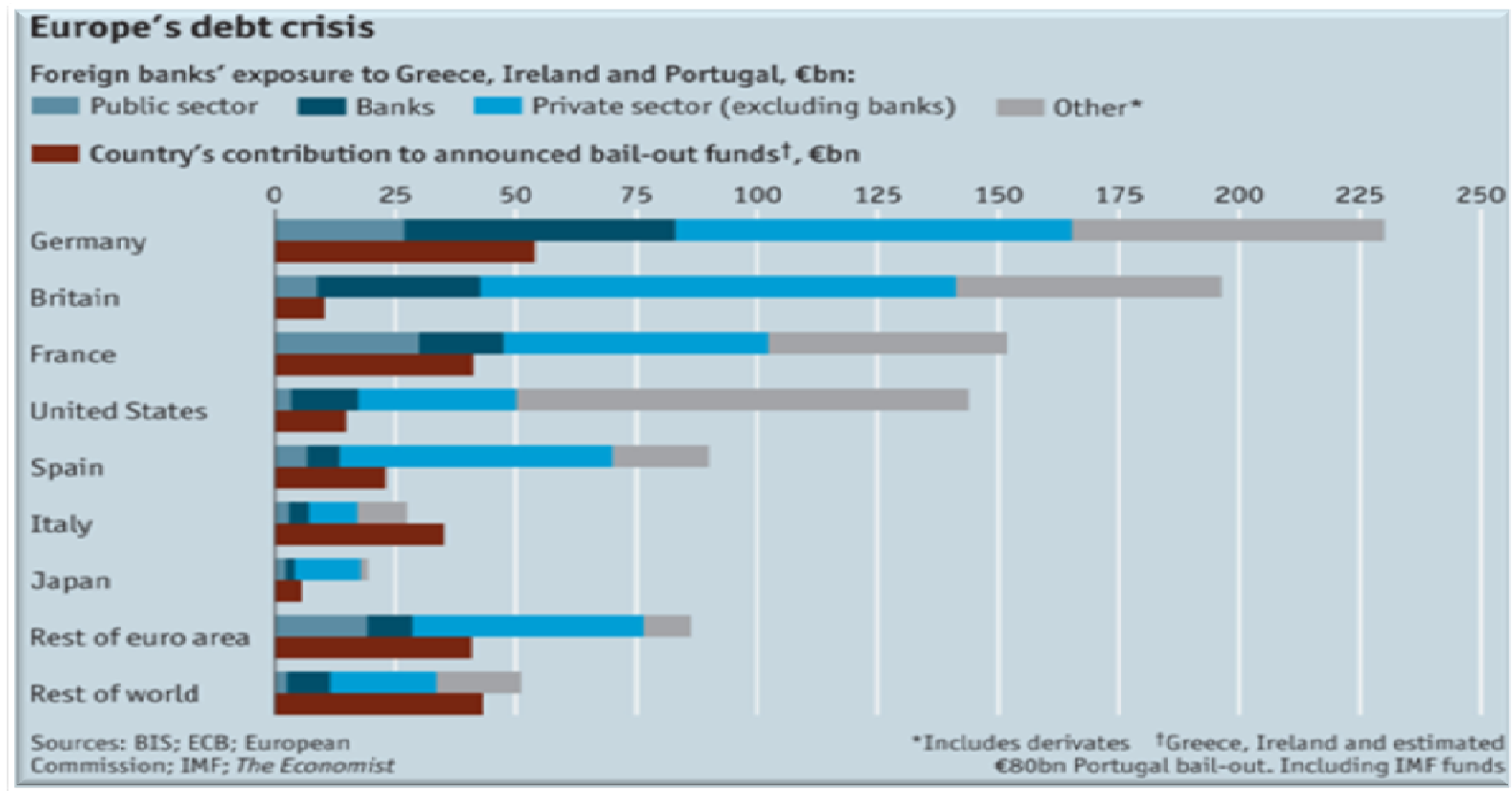
5. Why banks aren't lending very much long-term

Ahead of schedule for repaying Special Liquidity Scheme loans (£185bn by Jan 2012), as referenced by BoE Quarterly Bulletin Dec 2010



5. Why banks aren't lending very much long-term

Heightened credit risk in parts of Europe



5. Why banks aren't lending very much long-term

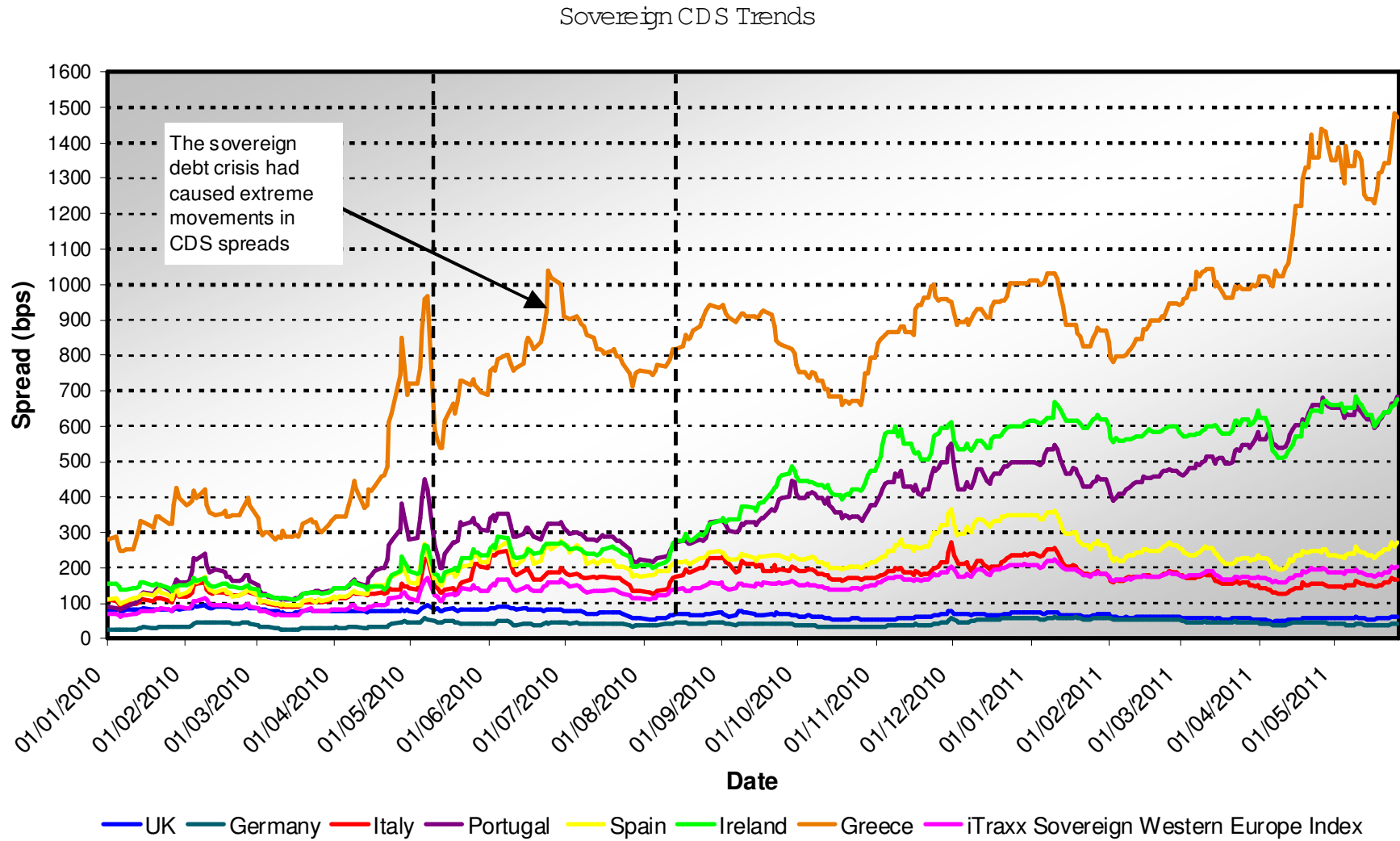
Greece, Ireland and Portugal have run into trouble financially
(NB the figures below reflect "public debt")

Country	Gross Debt as a % of GDP est. 2010	Deficit as a % of GDP est. 2010
Greece	142.8	10.5
Ireland	96.2	32.4
Portugal	93.0	9.1
France	81.7	7.0
UK	76.5	10.4
Spain	60.1	9.2

Source: Eurostat

6. More about credit risk issues

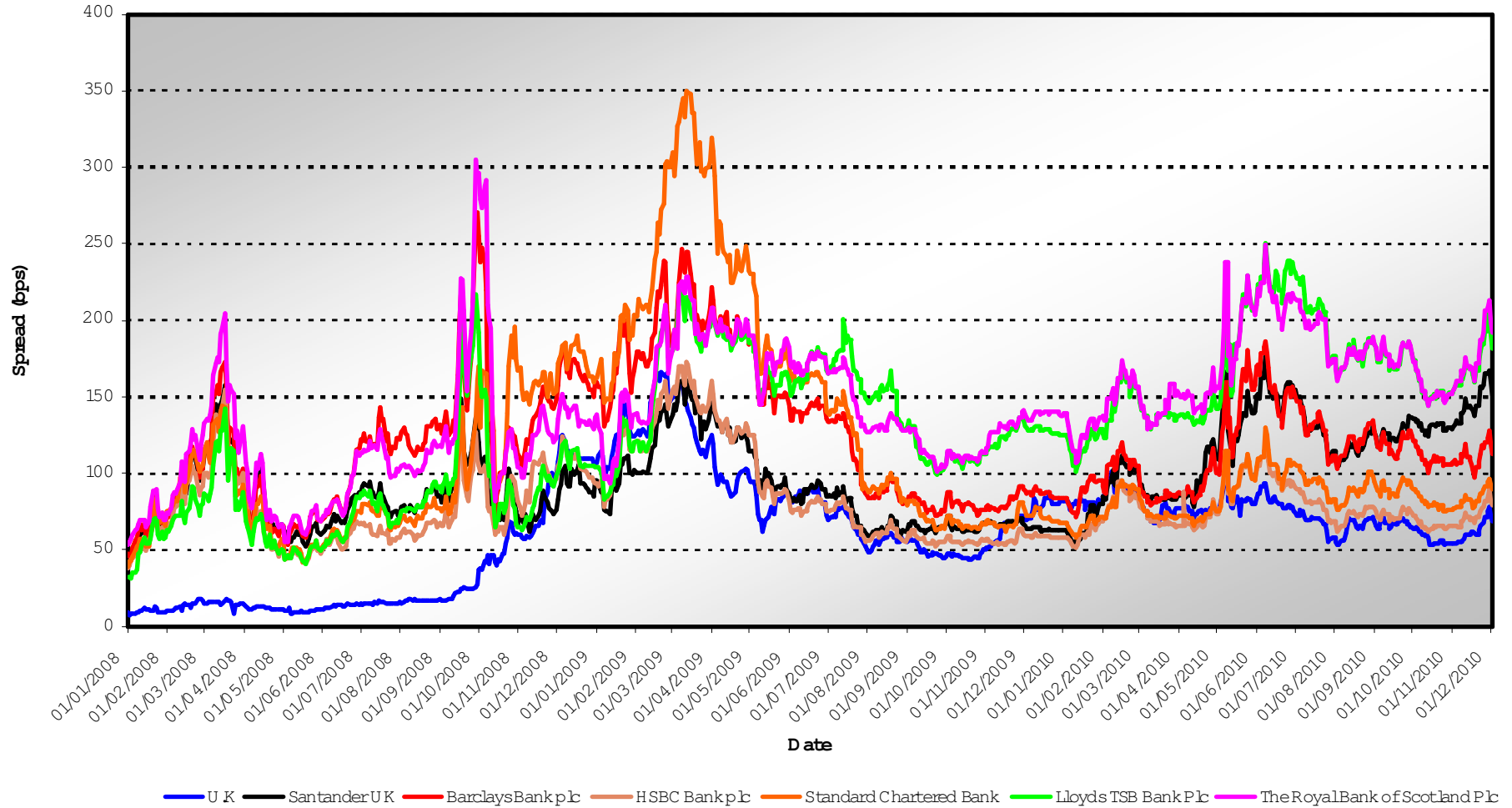
CDS Spreads emphasise increased risk in part of Europe (PIGS)



6. More about credit risk issues

The position with regard to the UK High Street

UK Bank's 5 Year Senior Debt Credit Default Swap Spreads



7. Summary

UK has a mountain of public debt

Local authorities are running down surplus cash and not borrowing for capital purposes unless really necessary

“Internal borrowing” mitigates credit and interest rate risk

Concerns in respect of other countries’ public debt continues, particularly Ireland

Next chapter in the debt story is likely to concern Spain, US or Japan