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Accepted that there are  
residual needs for it  
but think we should  
phase out cheaper  
loans, and long term  
loans at fixed interest

PRIME MINISTER

THE PUBLIC WORKS LOAN BOARD

Pie Anika  
Your query arose in the context of  
the recent changes to restrict LAs access  
to the PwLB for their marginal funds.  
Content to accept the Chancellor's case  
for keeping the PwLB in being?

You asked for my views on whether it is necessary to retain an  
organisation like the Public Works Loan Board.

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I have a great deal of sympathy with your question: at first sight the PwLB, with its antique-sounding name, really does seem a curious and anachronistic operation. But it does in fact perform a useful, if not indispensable, function; it is cheap to run; at present it is more than self-financing from fees from the local authorities; and although we could certainly abolish it if we wished to, it would require legislation and would, I think, cause unnecessary difficulties with the local authorities at an awkward time.

There are certainly arguments for saying that central Government should not be in the business of lending to local authorities at all. There is much to be said for exposing them to the disciplines of the market. Those who are acting imprudently would find it harder to raise funds, and those funds would cost more at the margin, giving the authority a clear message about the consequence of its behaviour for its creditworthiness. I hope that one useful by-product of the announcement I made on 15 February will be that high spending authorities may find their marginal cost of funds sharply increased because they have to raise the balance of their money from the markets. But such a



change would increase local authorities' debt service costs and their public expenditure. Authorities have been used to getting the bulk of their funds cheaply from the PWLB for many years, and there is a limit to how rapidly we can add to their costs by pushing them substantially into the market for more than their marginal funds. The time may come again, moreover, when it may prove useful to be able to channel local authorities' borrowing through the central Government accounts either for monetary policy reasons or as a way of under-pinning the control of local authorities' borrowing.

The PWLB also performs three other functions which it would be difficult to provide in any other way. It lends to small authorities who only borrow intermittently and who would find it awkward to have to go to the market for such funds. It provides long term finance - up to 25 years if needed - at fixed interest rates, which the market does not provide. And it acts as lender of last resort for authorities who try and fail to raise money on the markets. The latter has only happened very rarely, but I would want to think very carefully before disturbing this long established lender of last resort facility.

For all these reasons, it would be very difficult for central Government to withdraw rapidly, or completely, from providing loan finance to the local authorities. It is certainly possible to contemplate winding up the PWLB as such, and for either Treasury or for the DOE, Scottish Office and Welsh Office to provide the funds instead. But the local authorities would regard such a move with the deepest suspicion. Moreover, it has proved convenient to us, at times, to have the PWLB as an independent buffer between central Government and the individual authorities. When Liverpool was close to the brink, there was considerable presentational advantage in the fact that they were having to satisfy twelve independent Commissioners of the legality of their action, and it would have been those twelve independent Commissioners who

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would finally have refused further loan finance, rather than the Government itself. Similarly it was only possible to tighten up the lending quotas in the fairly arbitrary way I announced last month because the PWLB Commissioners can exercise discretion in individual cases in a way which a Government department would find difficult. The authorities accept their judgement because they are independent and known to be so, and include some ex-local authority officials whom the authorities trust to understand their problems.

We are, as you are aware, about to appoint a new Chairman for the PWLB. We have agreed that Robin Dent will replace James Guinness when he retires at the end of next month. My office will be in touch with yours very shortly about the necessary consultation for the issue of the Royal Warrant.

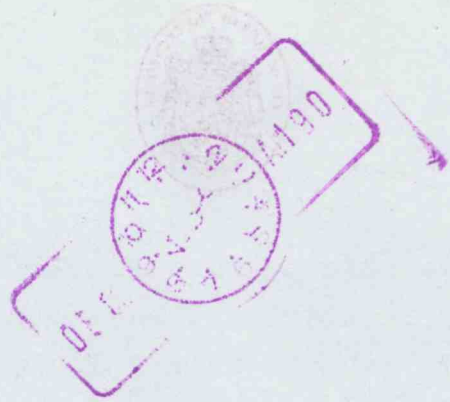
I am copying this minute to the Governor.

[J.M.]

7 March 1990

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