Lars M. Andersson and Nicholas Anderson argue that Local Government Funding Agencies are a necessary tool for the efficient financing of local infrastructure projects.

Nordic know-how

Local authorities in New Zealand have recently formed their own Local Government Funding Agency (LGFA). French local authorities worked with the same question for a couple of years and are close to the start-up of their agency. Now, the formation of a Local Government Funding Agency is being discussed in the UK. In all these projects the Nordic LGFA experience has been used.

LGFAs are found in all of the four Nordic countries. They finance most of the infrastructure of public basic services. All operate in a cost efficient manner as AAA-issuers in the domestic and international bond markets on a sustainable basis. They replicate the efficiencies of government bond markets and were a haven of security for their beneficiaries, regional government, during the financial crisis of 2009.

The financial benefits are significant even when based on conservative assumptions. LGFAs are cost effective because they replicate the government bond market and create competition to loans provided by the banking system. This solution allows the easy replication of knowledge and good implementation practices.This solution is also based on cooperation between the private and public sectors.

The Nordic LGFAs are able to fund themselves at the same or nearly at the same costs as their own governments. They can do this because of two main reasons: they are sufficiently large to operate efficiently on the bond markets; and they enjoy the same ratings as their respective governments because they only operate for the benefit of their clients, the regional government.

Their diversified sources of funding with many different maturities allows them to offer their clients, regional government entities, the loans that best match their funding requirements to finance the construction and maintenance of their infrastructure investments.

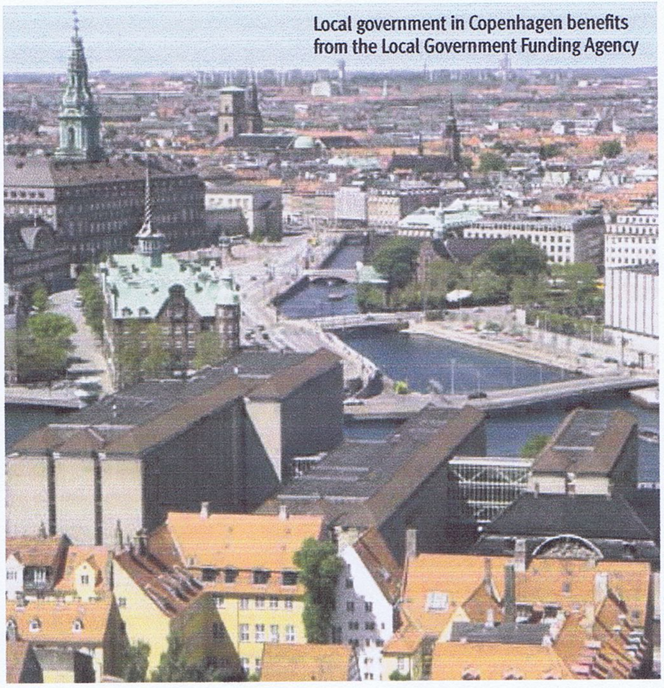
The Nordic experience has shown that the following minimum prerequisites are necessary for the continued success of a LGFA:

1. It is essential to have strong support from large groups of municipalities to form a joint funding system. This could be challenging to achieve especially with political, social and geographical differences.

   Naturally central government must also support this endeavour either by ensuring appropriate legislation or by becoming a shareholder in the LGFA.

   - The existence of a LGFA usually leads to better financial management in the municipal sector. All LGFAs must retain a high credit rating. This means that there is significant peer pressure between municipalities, exercised through a LGFA, to ensure budget discipline
   - Central governments can reduce their own contributions for infrastructure investment costs since local governments and local residents shoulder most of the costs locally.

2. LGFAs should operate without having to maximize profits since the basic infrastructure is there for the public good. It should seek to attain a result that enables growth of the balance sheet in the same fashion as other cooperative business models.



Local government in Copenhagen benefits from the Local Government Funding Agency

3. It is important to have market professionals appointed to the management of a LGFA who enjoy excellent relationships with banks and institutional investors on the global markets.
4. Finally the activities of all the companies are restricted to providing credit exclusively for the municipal sector. They are not allowed to finance business in the competitive markets outside the remit of the municipal sector.

The Nordic LGFAs have had a significant impact of the domestic municipal credit market and the whole area of financial management in municipalities. It has lowered funding costs for all Nordic municipalities, by bringing an alternative to the market and hence tough competition for the banks. It also opens up the markets to fair and transparent competitive bidding for all loans at market prices. All loan procurements are subject to negotiated bidding processes in accordance with EU competition law.

In the Nordic countries, LFGAs do not seek to maximize profits but to remain profitable and sustainable over the long term. They have the same rating as the sovereign, have professional staff and maintain healthy competition. LGFAs now provide local government a secure source of long term financing for basic infrastructure. Such a system has also been a key factor in permitting governments to stimulate the economy with new infrastructure projects.

The Nordic model is in one sense a virtuous circle that has created social and economic structures that reinforce one another. Cost efficiencies in procurement of public infrastructure in close cooperation with the corporate sector have produced excellent results.

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