

Item: 4

Investments Sub-committee: 12 June 2019.

Temporary Loans.

Report by Head of Finance.

1. Purpose of Report

To advise of the status of the temporary loan portfolio as at 31 March 2019.

2. Recommendations

The Sub-committee is invited to note:

2.1.

The status of the temporary loan portfolio as at 31 March 2019, as detailed in section 3 of this report.

2.2.

That, for the period 1 April 2018 to 31 March 2019, the temporary loans portfolio made a return of £288,788.47 at an average interest rate of 0.85%.

2.3.

That the Treasury Policy Statement is being adhered to by the Finance Service and is producing an acceptable rate of return.

3. Temporary Loan Portfolio

3.1.

The temporary loan portfolio as at 31 March 2019 totalled £34,141,904.47. Further details are provided in the Monthly Investment Analysis Review that is prepared by Link Asset Services, attached as Appendix 1 to this report.

3.2.

The following transactions have taken place since 31 March 2019:

- £3,000,000 matured from Dumfries and Galloway Council.
- £2,000,000 matured from Bank of Scotland.
- £1,900,000 recalled from Aberdeen Standard Investments Liquidity Fund.
- £5,300,000 invested with Aberdeen Standard Investments Liquidity Fund, with an average net yield of 0.78%.

- £1,000,000 invested with Insight Liquidity Fund, with an average net yet yield of 0.76%.
- £400,000 recalled from Insight Liquidity Fund.

3.3.

The value of the temporary loans stood at £33,650,360.19 as at 30 April 2019.

4. Rate of Return

4.1.

For the period 1 April 2018 to 31 March 2019, the temporary loans returned an average interest rate of 0.85%. This equates to a return of £288,788.47 on the temporary loans for the twelve months to 31 March 2019.

4.2.

By comparison, the equivalent 90-day London Inter-Bank Offered Rate of 0.80% is considered to be the target.

4.3.

With inflation quoted at 1.9% for March 2019 based on Consumer Price Index (2.4% Retail Price Index), the return on temporary loans equates to a relative decline in value of 1.05% in real terms.

5. Corporate Governance

This report relates to the Council complying with its treasury management policies and procedures and therefore does not directly support and contribute to improved outcomes for communities as outlined in the Council Plan and the Local Outcomes Improvement Plan.

6. Financial Implications

6.1.

The Treasury Policy Statement is being adhered to by the Finance Service and is producing an acceptable rate of return.

6.2.

The effective management and control of risk are prime objectives of the Council's treasury management activities, with priority given to security and liquidity when investing funds.

7. Legal Aspects

Section 69 of the Local Government (Scotland) Act 1973 empowers a local authority to lend and invest surplus funds on a temporary basis where it is calculated to facilitate, or is conducive or incidental to the discharge of any of their functions.

8. Contact Officers

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9. Appendix

Appendix 1: Link Asset Services Monthly Investment Analysis Review for March 2019.



Orkney Islands Council

Monthly Investment Analysis Review

March 2019

Monthly Economic Summary

General Economy

March began with Manufacturing PMI which fell to 52 in February, from 52.6 the previous month. Construction PMI dropped into negative figures, falling to 49.5 from 50.6 the month before, caused by Brexit uncertainty and the slowing housing market delaying new building projects. Services PMI rounded the figures off with a rising score of 51.3 in February, from a previous 50.1. This left the Composite figure at 50.3 from 51.5.

The UK's trade deficit continued to rise in January; the trade deficit in goods rose to £13.08bn, and the overall deficit rose to £3.83bn, well above the forecasted £2.6bn.

One of the key economic indicators, CPI inflation, rose slightly in February to 1.9% y/y from 1.8% the previous month, moving closer to the Bank of England's 2% target. However, core inflation, which strips out the more volatile components, edged down to 1.8%. Month-on-month, CPI rose to 0.5% from -0.8% previously, marginally below forecasts.

The UK's labour market continued to defy forecasts; the unemployment rate fell to 3.9%, with employment increasing by 220,000, above expectations of 150,000. Meanwhile, wage growth excluding bonuses maintained its 3.4% y/y figure, with the overall figure falling from 3.5% to 3.4%. British consumers are currently enjoying a period of relief as "real wages" continue to be maintained, as wage growth is well above inflation.

A warm month of February caused retail sales figures to unexpectedly keep up their good start to 2019; retail sales y/y growth slowed slightly to 4% from January's 4.1% figure, well above forecasts of 3.3%, and showing that consumer spending continues to be a source of strength for the British economy at a time when Brexit uncertainty is looming over the nation. Prospects for retail sales continue to look strong as wage growth continues to exceed the pace of inflation. In another measure of nationwide consumer sentiment, GfK Consumer Confidence remained at -13.

On the 21st March, the Bank of England's Monetary Policy Committee (MPC) voted unanimously to keep the base rate on hold at 0.75%. Governor Mark Carney has remained dovish due to the prospect of Brexit, but did imply in his press conference that in case of a long Brexit extension, the MPC may move to raise rates in the summer.

The UK's public finances were once again stronger than expected, as the resilient labour market boosted income tax revenue. Public borrowing for February fell to £0.2bn from £1.2bn a year earlier, below forecasts of £0.6bn. With just one month remaining of the financial year, government borrowing totals £21.3bn, down 44% from the same point in the previous tax year, and the government is broadly on track to meet its fiscal targets. Alongside this, Chancellor Hammond suggested in his Spring Statement that spending on public services will be increased if an orderly Brexit can be achieved. The Confederation of British Industry (CBI) data for the month was weaker than expected; the CBI Distributive Trades survey fell from 0 in February to -18 in March, despite being expected to rise to 5. The Industrial Trends survey also suffered a drop, from 6 in February to 1 in March.

To end the month, the final estimate of Q4 GDP growth showed a fall to 1.4% y/y from 1.6% in Q3, however this is higher than

the 1.3% earlier estimated. On the quarter, the UK achieved a final estimate of 0.2% growth, a fall from Q3's 0.7%.

In the USA, February's Nonfarm Payrolls figure came in at just 20,000, a massive drop from 311,000 in January, and below forecasts of 190,000. These numbers were amid a contraction in payrolls in construction among other sectors, raising concerns about a sharp slowdown in activity. This was also reflected in the final Q4 GDP estimate, which came in at 2.2%, a further downward revision and down from 3.4% in Q3. The Federal Reserve's Open Market Committee (FOMC) chose to keep rates on hold, as signs of a global slowdown start to take hold.

The Eurozone's unemployment rate remained at 7.8% in January, below predictions of a rise to 7.9%. In terms of growth, the 3rd estimate of Eurozone Q4 GDP growth came in at 1.1% y/y, a sharp drop from Q3's 1.6% figure, partly caused by the largest economy in the bloc, Germany, falling to nearly zero growth.

Housing

According to Nationwide's index, house prices rose 0.4% y/y in February, up from 0.1% in January, however they fell 0.1% m/m, down from 0.2%. Halifax's index showed a 2.8% rise in house prices y/y, well above forecasts of 1.1% and above the 0.8% previous figure. Meanwhile, prices rose 5.9% m/m, up markedly from January's -3% figure.

Currency

Sterling began February at \$1.33 and €1.14 against the dollar and euro respectively, and finished the month at \$1.30 and €1.16.

Forecast

Link Asset Services suggest that the next interest rate rise will be in the third quarter of 2019, followed by further hikes in Q2 2020 and Q1 2021, reaching 2.00% in Q1 2022. Capital Economics also expect the next rate rise will be in Q3 2019, followed by further regular rises, reaching 1.50% in Q4 2020.

Bank Rate	Now	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20
Link Asset Services	0.75%	0.75%	1.00%	1.00%	1.00%	1.25%	1.25%	1.25%
Capital Economics	0.75%	0.75%	1.00%	1.00%	1.00%	1.00%	1.25%	1.50%

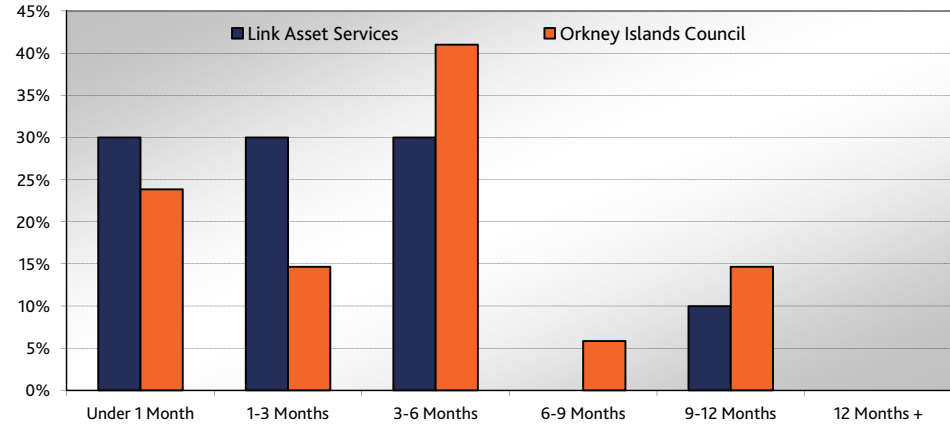
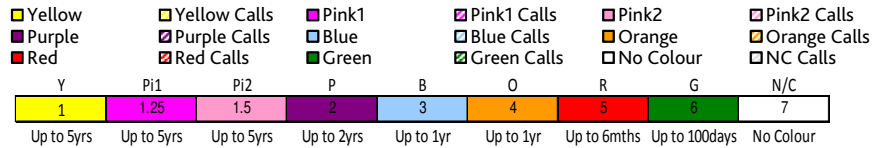
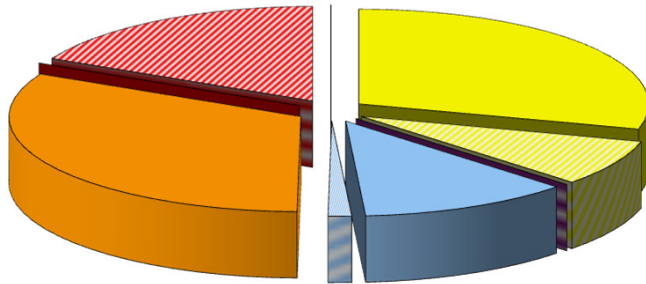
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Current Investment List

Borrower	Principal (£)	Interest Rate	Start Date	Maturity Date	Lowest Long Term Rating	Historic Risk of Default	Expected Credit Loss
MMF Aberdeen Standard Investments	2,300,000	0.79%		MMF	AAA	0.000%	2.55
MMF Insight	400,000	0.75%		MMF	AAA	0.000%	0.44
The Royal Bank of Scotland Plc (RFB)	441,904	0.20%		Call	A-	0.000%	0.64
Dumfries & Galloway Council	3,000,000	0.85%	01/03/2019	03/04/2019	AA	0.000%	0.00
Bank of Scotland Plc (RFB)	2,000,000	1.00%	04/01/2019	18/04/2019	A+	0.003%	51.98
Bank of Scotland Plc (RFB)	1,000,000	1.10%	08/02/2019	28/05/2019	A+	0.008%	83.74
Bank of Scotland Plc (RFB)	2,000,000	1.00%	13/06/2018	13/06/2019	A+	0.011%	213.69
Bank of Scotland Plc (RFB)	2,000,000	1.00%	22/06/2018	21/06/2019	A+	0.012%	236.79
Santander UK Plc	1,000,000	1.00%		Call95	A	0.014%	137.17
National Westminster Bank Plc (RFB)	2,000,000	1.01%	20/07/2018	19/07/2019	A-	0.016%	317.65
National Westminster Bank Plc (RFB)	2,000,000	1.04%	31/07/2018	29/07/2019	A-	0.017%	346.53
North Lanarkshire Council	2,000,000	1.00%	26/11/2018	27/08/2019	AA	0.010%	0.00
Santander UK Plc	2,000,000	1.10%		Call180	A	0.026%	519.79
Santander UK Plc	3,000,000	1.10%		Call180	A	0.026%	779.69
North Tyneside Metropolitan Borough Council	2,000,000	1.05%	02/10/2018	01/10/2019	AA	0.012%	0.00
Toronto Dominion Bank	2,000,000	1.08%	26/10/2018	25/10/2019	AA-	0.014%	274.88
Thurrock Borough Council	3,000,000	1.10%	18/01/2019	17/01/2020	AA	0.019%	0.00
Lloyds Bank Plc (RFB)	2,000,000	1.23%	28/01/2019	28/01/2020	A+	0.044%	874.98
Total Investments	£34,141,904	1.01%					£3,840.53

The Historic Risk of Default column is based on the lowest long term rating. If clients are using this % for their Expected Credit Loss calculation under IFRS 9, please be aware that the Code does not recognise a loss allowance where the counterparty is central government or a local authority since relevant statutory provisions prevent default. For these instruments, the Expected Credit Loss will be nil. Please note that we are currently using Historic Default Rates from 2009-2018 for Fitch, Moody's and S&P.

Portfolio Composition by Link Asset Services' Suggested Lending Criteria



Portfolios weighted average risk number = **2.93**

WARoR = Weighted Average Rate of Return

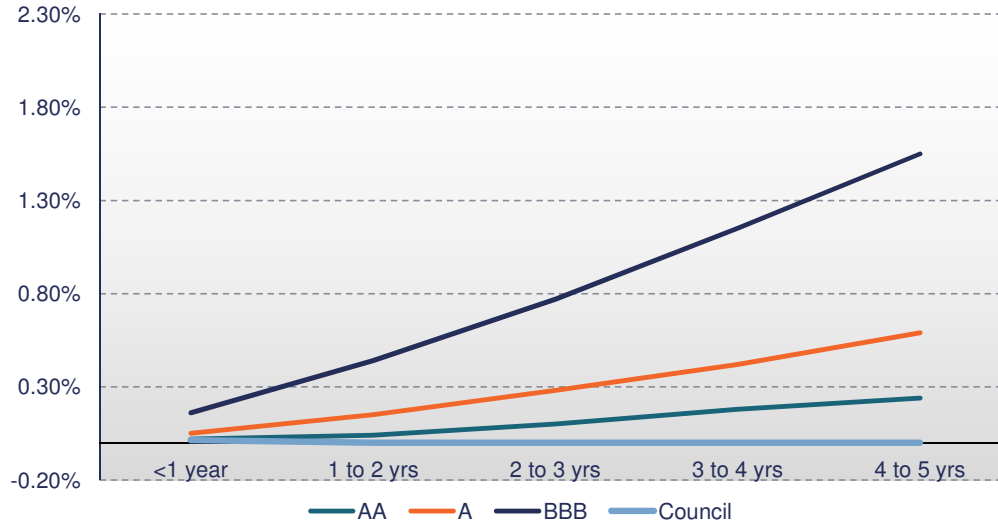
WAM = Weighted Average Time to Maturity

	% of Colour		Amount of		% of Call		Excluding Calls/MMFs/USDBFs			
	% of Portfolio	Amount	% in Calls	Colour in Calls	WARoR	WAM	WAM at Execution	WAM	WAM at Execution	
Yellow	37.20%	£12,700,000	21.26%	£2,700,000	7.91%	0.95%	122	194	155	247
Pink1	0.00%	£0	0.00%	£0	0.00%	0.00%	0	0	0	0
Pink2	0.00%	£0	0.00%	£0	0.00%	0.00%	0	0	0	0
Purple	0.00%	£0	0.00%	£0	0.00%	0.00%	0	0	0	0
Blue	13.01%	£4,441,904	9.95%	£441,904	1.29%	0.94%	104	327	115	364
Orange	32.22%	£11,000,000	0.00%	£0	0.00%	1.07%	130	294	130	294
Red	17.57%	£6,000,000	100.00%	£6,000,000	17.57%	1.08%	166	166	0	0
Green	0.00%	£0	0.00%	£0	0.00%	0.00%	0	0	0	0
No Colour	0.00%	£0	0.00%	£0	0.00%	0.00%	0	0	0	0
Total	100.00%	£34,141,904	26.78%	£9,141,904	26.78%	1.01%	130	239	138	286

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Investment Risk and Rating Exposure

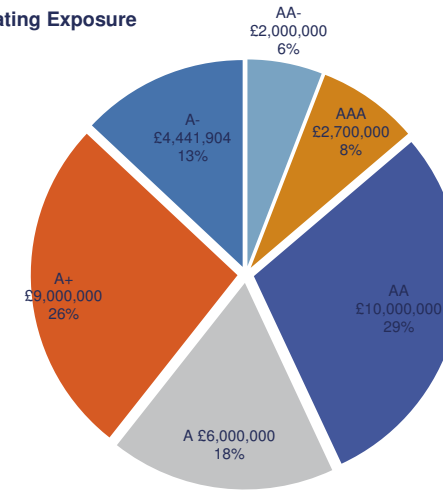
Investment Risk Vs. Rating Categories



Historic Risk of Default

Rating/Years	<1 year	1 to 2 yrs	2 to 3 yrs	3 to 4 yrs	4 to 5 yrs
AA	0.02%	0.04%	0.10%	0.18%	0.24%
A	0.05%	0.15%	0.28%	0.42%	0.59%
BBB	0.16%	0.44%	0.77%	1.15%	1.55%
Council	0.014%	0.000%	0.000%	0.000%	0.000%

Rating Exposure



Historic Risk of Default

This is a proxy for the average % risk for each investment based on over 30 years of data provided by Fitch, Moody's and S&P. It simply provides a calculation of the possibility of average default against the historical default rates, adjusted for the time period within each year according to the maturity of the investment.

Chart Relative Risk

This is the authority's risk weightings compared to the average % risk of default for "AA", "A" and "BBB" rated investments.

Rating Exposures

This pie chart provides a clear view of your investment exposures to particular ratings.

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Monthly Credit Rating Changes FITCH

Date	Update Number	Institution	Country	Rating Action
04/03/2019	1671	Abbey National Treasury Services PLC	United Kingdom	The Long Term Rating was removed from Stable Outlook and placed on Negative Watch.
04/03/2019	1671	Bank of Scotland PLC (RFB)	United Kingdom	The Long Term Rating was removed from Stable Outlook and placed on Negative Watch.
04/03/2019	1671	Barclays Bank PLC (NRFB)	United Kingdom	The Long Term Rating was removed from Stable Outlook and placed on Negative Watch.
04/03/2019	1671	Barclays Bank UK PLC (RFB)	United Kingdom	The Long Term Rating was removed from Stable Outlook and placed on Negative Watch.
04/03/2019	1671	Close Brothers Ltd	United Kingdom	The Long Term Rating was removed from Stable Outlook and placed on Negative Watch.
04/03/2019	1671	Clydesdale Bank PLC	United Kingdom	The Long Term Rating was removed from Stable Outlook and placed on Negative Watch.
04/03/2019	1671	Co-operative Bank PLC (The)	United Kingdom	The Long Term Rating was removed from Stable Outlook and placed on Negative Watch.
04/03/2019	1671	HSBC Bank PLC (NRFB)	United Kingdom	The Long Term Rating was removed from Stable Outlook and placed on Negative Watch.
04/03/2019	1671	HSBC UK Bank PLC (RFB)	United Kingdom	The Long Term Rating was removed from Stable Outlook and placed on Negative Watch.
04/03/2019	1671	Lloyds Bank Corporate Markets PLC (NRFB)	United Kingdom	The Long Term Rating was removed from Stable Outlook and placed on Negative Watch.
04/03/2019	1671	Lloyds Bank PLC (RFB)	United Kingdom	The Long Term Rating was removed from Stable Outlook and placed on Negative Watch.
04/03/2019	1671	NatWest Markets PLC (NRFB)	United Kingdom	The Long Term Rating was removed from Stable Outlook and placed on Negative Watch.
04/03/2019	1671	Santander UK PLC	United Kingdom	The Long Term Rating was removed from Stable Outlook and placed on Negative Watch.
04/03/2019	1671	National Westminster Bank PLC (RFB)	United Kingdom	The Long Term Rating was removed from Stable Outlook and placed on Negative Watch.
04/03/2019	1671	The Royal Bank of Scotland PLC (RFB)	United Kingdom	The Long Term Rating was removed from Stable Outlook and placed on Negative Watch.
04/03/2019	1672	Coventry Building Society	United Kingdom	The Long Term Rating was removed from Stable Outlook and placed on Negative Watch.
04/03/2019	1672	Leeds Building Society	United Kingdom	The Long Term Rating was removed from Stable Outlook and placed on Negative Watch.
04/03/2019	1672	Nationwide Building Society	United Kingdom	The Long Term Rating was removed from Stable Outlook and placed on Negative Watch.

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Monthly Credit Rating Changes FITCH

Date	Update Number	Institution	Country	Rating Action
04/03/2019	1672	Principality Building Society	United Kingdom	The Long Term Rating was removed from Stable Outlook and placed on Negative Watch.
04/03/2019	1672	Skipton Building Society	United Kingdom	The Long Term Rating was removed from Stable Outlook and placed on Negative Watch.
04/03/2019	1672	Yorkshire Building Society	United Kingdom	The Long Term Rating was removed from Stable Outlook and placed on Negative Watch.
04/03/2019	1673	UBS Ltd.	United Kingdom	Ratings withdrawn as a result of changes to the UBS banking group.

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Monthly Credit Rating Changes MOODY'S

Date	Update Number	Institution	Country	Rating Action
04/03/2019	1673	UBS Ltd.	United Kingdom	Ratings withdrawn as result of changes to the UBS banking group.
07/03/2019	1674	Bank of America N.A.	United States	The Long Term Rating was upgraded to 'Aa2' from 'Aa3' and the Short Term Rating was affirmed. At the same time, the Long Term Rating was removed from Positive Watch and placed on Stable Outlook.
28/03/2019	1675	Bank Nederlandse Gemeenten N.V.	Netherlands	The Long Term Rating was upgraded to 'AAA' from 'AA+'. At the same time, the Short Term Rating and Viability Rating were affirmed.

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Monthly Credit Rating Changes S&P

Date	Update Number	Institution	Country	Rating Action
04/03/2019	1673	UBS Ltd.	United Kingdom	Ratings withdrawn as result of changes to the UBS banking group.