Item: 6

Investments Sub-committee: 28 August 2019.

Temporary Loans.

Report by Head of Finance.

1. Purpose of Report

To advise of the status of the temporary loan portfolio as at 30 June 2019.

2. Recommendations

The Sub-committee is invited to note:

2.1.

The status of the temporary loan portfolio as at 30 June 2019, as detailed in section 3 of this report.

2.2.

That, for the period 1 April to 30 June 2019, the temporary loans portfolio made a return of £76,275.47 at an average interest rate of 1.00%.

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 30 June 2019 totalled £27,414,192.36. 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 30 June 2019:

- £4,000,000 matured from National Westminster Bank Plc.
- £2,000,000 invested with Bank of Scotland at a rate of 1.25%
- £5,200,000 recalled from Aberdeen Standard Investments Liquidity Fund.
- £4,200,000 invested with Aberdeen Standard Investments Liquidity Fund, with an average net yield of 0.74%.

3.3.

The value of the temporary loans stood at £24,178,891.11 as at 31 July 2019.

4. Rate of Return

4.1.

For the period 1 April to 30 June 2019, the temporary loans returned an average interest rate of 1.00%. This equates to a return of £76,275.47 on the temporary loans for the three months to 30 June 2019.

4.2.

By comparison, the equivalent 90-day London Inter-Bank Offered Rate of 0.77% is considered to be the target.

4.3.

With inflation quoted at 2.0% for June 2019 based on Consumer Price Index (2.9% Retail Price Index), the return on temporary loans equates to a relative decline in value of 1.00% 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 June 2019.

Appendix 1

Orkney Islands Council

Monthly Investment Analysis Review

June 2019

Monthly Economic Summary

General Economy

June’s economic data began with the May Markit/CIPS Manufacturing PMI figure. This fell to 49.4 from 53.1 the previous month, which was the steepest contraction since February 2013. The drivers of the decline were firms continuing to run down their excess inventory after stockpiling for a no-deal Brexit and the impact of the global economic slowdown. This was then compounded by Construction PMI also dropping into contraction territory (ie a reading below 50), falling to 48.6 from 50.5. The Services PMI figure provided a small saving grace, rising to 51 from 50.4. This left the Composite figure at 50.9, which indicated minimal levels of growth in the UK economy.

The UK trade deficit narrowed to £2.74bn in April, falling from an upwardly revised £6.15bn the previous month. Exports declined 4.3% to £53.47bn, but imports declined at a faster rate of 9.3% to £56.21bn, causing the lowest trade deficit since last September. Meanwhile, the UK’s economy’s growth rate fell; the 3m/3m rolling average GDP growth figure fell from 0.5% to 0.3% in the 3 months to April. The economy slowed in April mainly due to a large fall in car production, with Brexit uncertainty leading to planned shutdowns in automotive factories.

The Bank of England’s Monetary Policy Committee (MPC) voted unanimously to keep interest rates on hold at 0.75% in June. The tone of the meeting was far more dovish than in May, as the Bank slashed its growth forecast for the three months to June to zero, amid a broader deterioration in the domestic economy allied with weaker overall global conditions.

Unemployment maintained its 3.8% rate in the three months to April, its lowest level since 1974. Meanwhile, the nominal employment figure increased by 32,000 to a record high of 32.75 million. The tight labour market showed in wage growth figures, as average earnings excluding bonuses came in at 3.4%, up from 3.3% previously. However, when bonuses were accounted for, the figure dropped to 3.1%.

CPI inflation was in line with the Bank of England’s 2% target in May, decreasing from 2.1 % y/y previously. Cost pressures in factories fell to a three-year low and travel prices fell back after their Easter highs in April. The data added to market views that the Bank of England has no urgency to pursue its stated policy of gradually raising interest rates. The Core CPI figure (which strips out the more volatile components of inflation) fell to 1.7%, the lowest annual rate since January 2017, signalling that underlying inflationary pressures are contained at present. The m/m CPI figure fell to 0.3% from 0.6% in the previous month.

Retail sales fell by 0.5% in May m/m, following on from the flat reading of April. At the annual level, sales decreased to 2.3% y/y from 5.1% in April. Despite the decreasing trend, consumer spending has generally been a bright spot for the UK economy, contrasting with falling investment by businesses.

British banks approved 65,409 mortgages for new house purchases in May 2019, which was below the 66,045 figure seen in the previous month. In addition, approvals of loans secured on dwellings for re-mortgaging fell to 46,706 in May from 48,945 previously. Meanwhile, loans for other purposes increasing slightly to 14,748 from 14,425 previously.

May's Confederation for British Industry (CBI) and GfK surveys produced negative results; the CBI's Distributive Trades Survey (covering retailing) fell to -42 from a previous figure of -27, and its Industrial Trends survey also showed a drop, from -10 to -15. Following the trend of these releases, the GfK Consumer Confidence reading showed a fall from -10 to -13..

The government's public finances figures showed a deficit of £4.46bn in May, showing a surprisingly large difference to the figure for April of £6.15bn which was significantly revised from the initial reading of £4.97bn. Excluding state-controlled banks, the deficit came in at £5.1bn, a 23.1% increase from the previous year. The UK's government debt increased by £20.5bn to £1.8trn as at the end of May, equivalent to 82.9% of GDP.

In the USA, Nonfarm Payrolls came in at 75,000 in May, down from 224,000 in April, which suggests the labour market is slowing in the US economy, combined with earnings remaining at 3.1% y/y and 0.2% m/m. While the unemployment rate dropped to 3.6% from 3.8%, this was more related to a fall in the overall workforce rather than a product of job gains. Elsewhere, the second estimate of annualised US GDP growth was unrevised, at 3.1%, remaining above Q4 2018's 2.2% figure, but slightly short of forecasts. Meanwhile, in the Eurozone, GDP growth remained at 0.4% in Q1 and 1.2% year-on-year, as the effects of the global slowdown, particularly in China, have taken hold. Unemployment fell to 7.5% from 7.6% last month, the lowest jobless rate since August 2008.

Housing

According to Nationwide, house prices increased by 0.6% y/y in May but fell by 0.2% on the month, both figures were below estimates. Meanwhile, Halifax's 3-month y/y figure increased slightly to 5.2% from 5% previously, but below estimates of a 5.4% jump. On the month, prices decreased from a figure of +1.1% to +0.5%, which was above market expectations.

Currency

Over the month of June the pound slightly rose against the dollar, from $1.265 to $1.269. It was a different story against the euro, beginning at €1.13 and ending at €1.12.

Forecast

Link Asset Services currently forecast the next rate rise to come in Q3 2020. This forecast is scheduled to be reviewed following the release of the Bank of England Quarterly Inflation Report in August. Capital Economics have cut back their forecasts, not predicting a rate rise until Q4 2020.

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

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Current Investment List

Borrower	Principal (£)	Interest Rate	Start Date	Maturity Date	Lowest Long Term Rating	Historic Risk of Default
MMF Aberdeen Standard Investments	5,600,000	0.76%		MMF	AAA	0.000%
MMF Insight	1,500,000	0.73%		MMF	AAA	0.000%
The Royal Bank of Scotland Plc (RFB)	314,192	0.20%		Call	A	0.000%
National Westminster Bank Plc (RFB)	2,000,000	1.01%	20/07/2018	19/07/2019	A	0.003%
National Westminster Bank Plc (RFB)	2,000,000	1.04%	31/07/2018	29/07/2019	A	0.004%
North Lanarkshire Council	2,000,000	1.00%	26/11/2018	27/08/2019	AA	0.004%
Santander UK Plc	3,000,000	1.10%		Call75	A	0.011%
North Tyneside Metropolitan Borough Council	2,000,000	1.05%	02/10/2018	01/10/2019	AA	0.006%
Toronto Dominion Bank	2,000,000	1.08%	26/10/2018	25/10/2019	AA-	0.008%
Thurrock Borough Council	3,000,000	1.10%	18/01/2019	17/01/2020	AA	0.013%
Lloyds Bank Plc (RFB)	2,000,000	1.23%	28/01/2019	28/01/2020	A+	0.031%
Bank of Scotland Plc (RFB)	2,000,000	1.25%	21/06/2019	22/06/2020	A+	0.052%
Total Investments	**£27,414,192**	**1.00%**				0.010%

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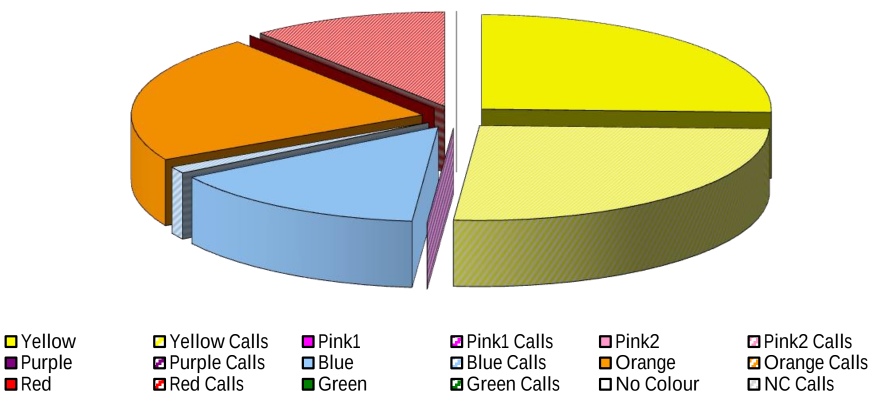
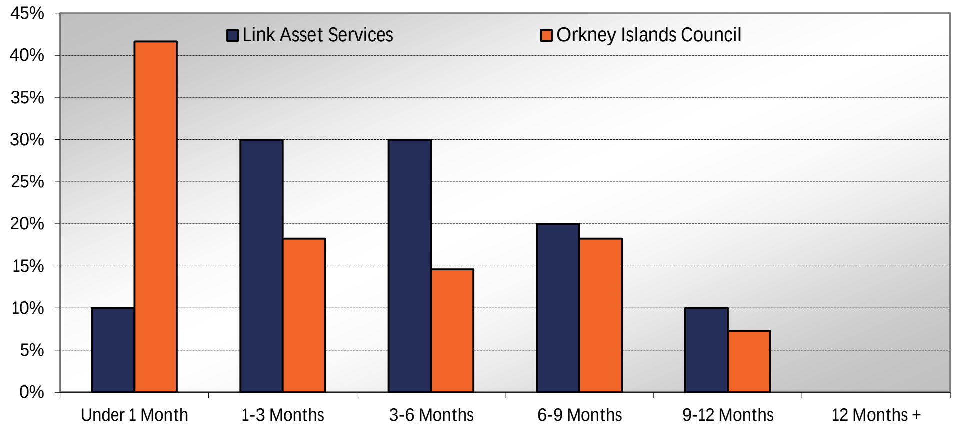
Portfolio Composition by Link Asset Services' Suggested Lending Criteria



Y	Pi1	Pi2	P	B	O	R	G	N/C
1	1.25	1.5	2	3	4	5	6	7
Up to 5yrs	Up to 5yrs	Up to 5yrs	Up to 2yrs	Up to 1yr	Up to 1yr	Up to 6mths	Up to 100days	No Colour



Portfolios weighted average risk number = 2.41

WARoR = Weighted Average Rate of Return
WAM = Weighted Average Time to Maturity

	% of Portfolio	Amount	% of Colour in Calls	Amount of Colour in Calls	% of Call in Portfolio	WARoR	WAM	WAM at Execution	Excluding Calls/MMFs/USDBFs WAM	Excluding Calls/MMFs/USDBFs WAM at Execution
Yellow	51.43%	£14,100,000	50.35%	£7,100,000	25.90%	0.90%	64	168	129	338
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	15.74%	£4,314,192	7.28%	£314,192	1.15%	0.96%	22	337	24	364
Orange	21.89%	£6,000,000	0.00%	£0	0.00%	1.19%	229	365	229	365
Red	10.94%	£3,000,000	100.00%	£3,000,000	10.94%	1.10%	75	75	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
	100.00%	**£27,414,192**	**37.99%**	**£10,414,192**	**37.99%**	**1.00%**	**95**	**228**	**140**	**354**

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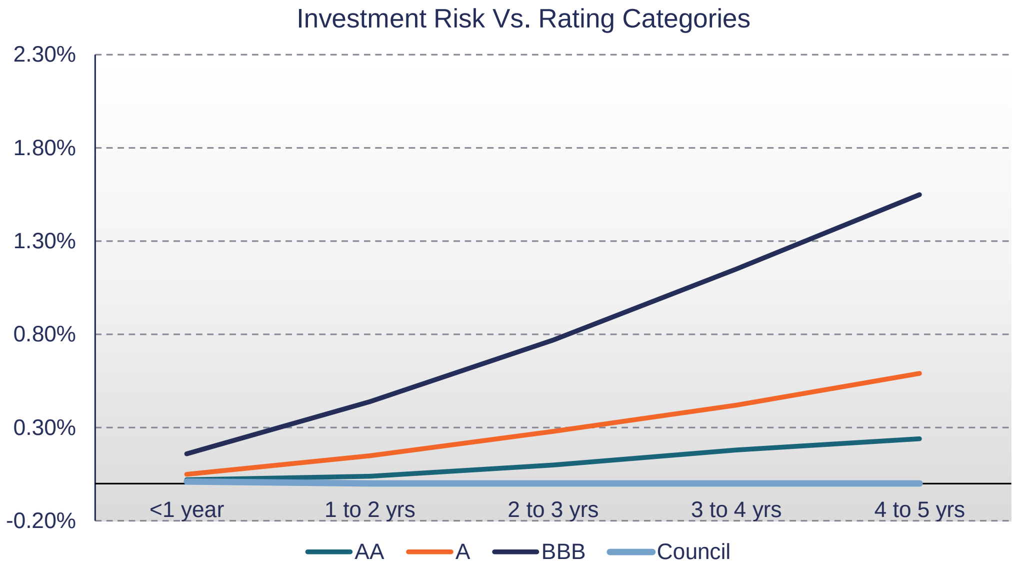
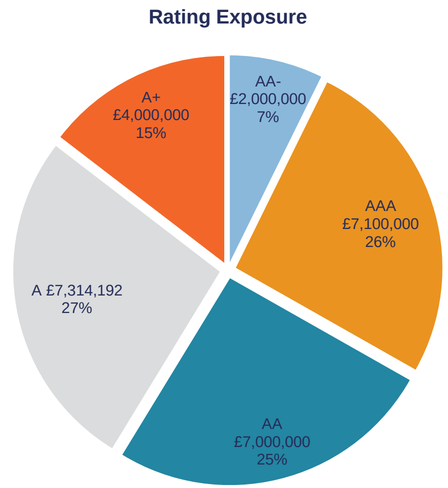
Investment Risk and Rating Exposure





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	0.010%	0.000%	0.000%	0.000%	0.000%

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
03/06/2019	1685	Clydesdale Bank Plc	United Kingdom	The Long Term Rating was upgraded to 'A-' from 'BBB+' and maintained on Negative Watch.
10/06/2019	1686	Deutsche Bank AG	Germany	The Long Term Rating was downgraded to 'BBB' from 'BBB+' and the Viability Rating was downgraded to 'bbb' from 'bbb+'. The Outlook on the Long Term Rating was changed to Evolving from Negative.

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Monthly Credit Rating Changes
MOODY'S

Date	Update Number	Institution	Country	Rating Action
28/06/2019	1687	Co-operative Bank PLC (The)	United Kingdom	The Long Term Rating was upgraded to 'B3' from 'Caa1' and the Outlook was changed to Positive from Stable.

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Monthly Credit Rating Changes
S&P

Date	Update Number	Institution	Country	Rating Action
28/06/2019	1688	ABN AMRO Bank N.V.	Netherlands	The Outlook on the Long Term Rating was changed to Stable from Positive.
28/06/2019	1688	Cooperatieve Rabobank U.A.	Netherlands	The Outlook on the Long Term Rating was changed to Stable from Positive.