WARWICK DISTRICT COUNCIL	**Finance and Audit Scrutiny Committee. 12 November 2019.**	**Agenda Item No. 6**

Title	Treasury Management Activity Report for the period 1 April 2019 to 30 September 2019.
For further information about this report please contact	Karen Allison, Assistant Accountant 01926 456334 karen.allison@warwickdc.gov.uk
Wards of the District directly affected	All
Is the report private and confidential and not for publication by virtue of a paragraph of schedule 12A of the Local Government Act 1972, following the Local Government (Access to Information) (Variation) Order 2006?	No
Date and meeting when issue was last considered and relevant minute number	N/a
Background Papers	Treasury Management File L2/9 Treasury Management Information via External Advisers, Brokers, External Investment Agents etc.

Contrary to the policy framework:	No
Contrary to the budgetary framework:	No
Key Decision?	No
Included within the Forward Plan? (If yes include reference number)	No
Equality Impact Assessment Undertaken	No-not relevant.

Officer/Councillor Approval		
Officer Approval	**Date**	**Name**
Chief Executive/Deputy Chief Executive	30.10.2019	Andrew Jones
Head of Service	30.10.2019	Mike Snow
CMT		
Section 151 Officer	30.10.2019	Mike Snow
Monitoring Officer	30.10.2019	Andrew Jones
Finance	29.10.2019	Karen Allison/Richard Wilson
Portfolio Holder(s)	29.10.2019	Cllr Richard Hales
Consultation & Community Engagement		
None.		
Final Decision?		Yes
Suggested next steps (if not final decision please set out below)		

1. **Summary**

1.1 This report details the Council's Treasury Management performance for the period 1 April 2019 to 30 September 2019.

2. **Recommendations**

2.1 That Finance and Audit Scrutiny Committee notes the contents of this report.

2.2 That Finance and Audit Scrutiny Committee approves the changes to the Prudential Indicators for 2019/20 at Appendix E.

3. **Reasons for the Recommendation**

3.1 The Council's 2019/20 Treasury Management Strategy and Treasury Management Practices (TMP's) require the performance of the Treasury Management Function to be reported to Members on a half yearly basis in accordance with the Treasury Management Code of Practice.

3.2 One of the Council's 2019/20 Prudential Indicators requires an amendment to provide sufficient flexibility to the Council's future long-term borrowing and future-proof the Council's Prudential Indicators against any change in accounting practice relating to internal borrowing.

4. **Policy Framework**

4.1 **Fit for the Future (FFF)**

The Council's FFF Strategy is designed to deliver the Vision for the District of making it a Great Place to Live, Work and Visit. To that end amongst other things the FFF Strategy contains several Key projects. This report shows the way forward for implementing a significant part of one of the Council's Key projects.

The FFF Strategy has 3 strands – People, Services and Money and each has an external and internal element to it. The table below illustrates the impact of this proposal if any in relation to the Council's FFF Strategy.

FFF Strands		
People	**Services**	**Money**
External		
Health, Homes, Communities	**Green, Clean, Safe**	**Infrastructure, Enterprise, Employment**
<u>Intended outcomes:</u> Improved health for all Housing needs for all met Impressive cultural and sports activities Cohesive and active communities	<u>Intended outcomes:</u> Area has well looked after public spaces All communities have access to decent open space Improved air quality Low levels of crime and ASB	<u>Intended outcomes:</u> Dynamic and diverse local economy Vibrant town centres Improved performance/ productivity of local economy Increased employment and income levels
Impacts of Proposal		

The Treasury Management function enables the Council to meet its vision.	The Treasury Management function enables the Council to meet its vision.	The Treasury Management function enables the Council to meet its vision.
Internal		
Effective Staff	**Maintain or Improve Services**	**Firm Financial Footing over the Longer Term**
<u>Intended outcomes:</u> All staff are properly trained All staff have the appropriate tools All staff are engaged, empowered and supported The right people are in the right job with the right skills and right behaviours	<u>Intended outcomes:</u> Focusing on our customers' needs Continuously improve our processes Increase the digital provision of services	<u>Intended outcomes:</u> Better return/use of our assets Full Cost accounting Continued cost management Maximise income earning opportunities Seek best value for money
Impacts of Proposal		
The Treasury Management function enables the Council to meet its vision.	The Treasury Management function enables the Council to meet its vision.	The Treasury Management function enables the Council to meet its vision.

4.2 **Supporting Strategies**

Each strand of the FFF Strategy has several supporting strategies. The Treasury Management function is consistent with the relevant supporting strategies.

4.3 **Changes to Existing Policies**

The Treasury Management function is in accordance with existing policies.

4.4 **Impact Assessments** – No impacts of new or significant policy changes proposed in respect of Equalities.

5. **Budgetary Framework**

5.1 Treasury Management has a potentially significant impact on the Council's budget through its ability to maximise its investment interest income and minimize borrowing interest payable whilst ensuring the security of the capital. The Council is reliant upon interest received to help fund the services it provides. The current estimate for investment interest in 2019/20 is shown in the following table:

	Latest 2019/20 Budget £'000	**Original 2019/20 Budget £'000**	**Actual 2018/19 £'000**
Gross Investment Interest	1,091	1,096	937
less HRA allocation	-422	-624	-335
Net interest to General Fund	**669**	**472**	**602**

*Note- the 2019/20 figure for net interest to General Fund includes £20,600 of deferred capital receipts interest.

The latest estimate is being revised during the budget setting process. The main differences between the original and latest 2019/20 budgets are shown in the table below:

Differences:	£'000
Reduction in HRA recharge	202
Reduction in investment interest	-239
Increase in 3rd party loan interest	235
Increase in net interest to GF	**198**

The interest paid to the HRA is based on the HRA's equated balances for the year and the interest rate earned on relevant investments. The reduction from the original budget is mainly due to increased capital spending reducing the equated balances, with a smaller impact of the Base Rate not increasing, as had been expected, on interest rates.

6. Risks

6.1 Investing the Council's funds inevitably creates risk and the Treasury Management function effectively manages this risk through the application of the SLY principle. Security(S) ranks uppermost followed by Liquidity (L) and finally Yield(Y). It's accepted that longer duration investments increase the security risk within the portfolio, however this is inevitable in order to achieve the best possible return and still comply with the SLY principle which is a cornerstone of treasury management within local authorities.

6.2 In addition to credit ratings themselves, the Council will also have regard to any ratings watch notices issued by the 3 agencies as well as articles in the Financial press, market data and intelligence from Link Asset Services benchmarking groups. It will also use Credit Default Swap (CDS) data as supplied by Link Asset Services – Treasury Solutions to determine the suitability of investing with counterparties.

6.3 Corporate Bonds and Floating Rate Notes (FRN's) introduce counterparty credit risk into the portfolio by virtue of the fact that it is possible that the institution invested in could become bankrupt leading to the loss of all or part of the Council's investment. This is mitigated by only investing in Corporate Bonds or FRN's with a strong Fitch credit rating, in this case A and issued as Senior Unsecured debt which ranks above all other debt in the case of a bankruptcy.

6.4 Covered Bonds also reduce risk in the portfolio as the bond is "backed" by high quality assets such as prime residential mortgages thus ensuring that if the bond issuer defaults there are sufficient assets that can be realised in order to repay the bond in full.

6.5 While Corporate Equity Funds can help to ensure capital security in real (as opposed to nominal) terms, they consequently introduce the risk of capital loss due to market price fluctuations. This is mitigated by ensuring the investments are held for a sufficiently long period. In addition, mitigation is achieved by having a spread of funds with differing risk appetites. "Stop loss" limits (whereby if the value in the fund goes below a defined limit, the holdings in that fund will be sold) reduce risk by limiting losses. Finally, a volatility reserve has been created - a proportion of the annual return on the funds will be credited to this reserve and then when required can be released to revenue either to cover or at least mitigate the impact of any deficits.

7. Alternative Option(s) considered

7.1 This report retrospectively looks at what has happened during the last 6 months. It is a statement of fact. The Treasury Management Strategy for 2020/21 will consider the options available to the Council.

8. Background

8.1 A detailed commentary by our Treasury Consultants, Link Asset Services, of the economic background surrounding this report appears as Appendix C.

9. Interest Rate Environment

9.1 The major influence on the Council's investments is the Bank Rate. The Monetary Policy Committee (MPC) voted to keep the bank rate of 0.75% on 19 September 2019 but the potential impact of Brexit has meant that the MPC has considered scenarios where the Bank Rate could rise or fall after Brexit. The Council's Treasury Management Advisors, Link Asset Services, provided the following forecast as at October 2019 for future Bank Rates (based on a central assumption that there will be some form of orderly exit from the EU based on an agreement that has passed through Parliament).

Qtr End-ing	Sept 2019	Dec 2019	Mar 2020	June 2020	Sept 2020	Dec 2020	Mar 2021	Jun 2021	Sept 2021	Dec 2021	Mar 2022
Current Forecast, as at October 2019:											
Bank Rate %	0.75	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.00	1.25
Forecast, as at January 2019, (when Original Budgets were set):											
Bank Rate %	1.00	1.00	1.25	1.25	1.25	1.50	1.50	1.75	1.75	1.75	2.00

The forecast as at January 2019 is shown for comparison purposes as this forecast was used in calculating the original budgets.

9.2 The Council aims to achieve the optimum return on investments commensurate with the proper levels of security and liquidity. The Annual Investment Strategy 2019/20 was approved by Council on 20 February 2019. This approved the current lending criteria which reflect the level of risk appetite of the Council. However, the Council continues to review its Standard Lending List as a result of frequent changes to Banking Institutions' credit ratings, to ensure that it does not lend to those institutions identified as being at risk. A copy of the current lending list is shown as Appendix D.

10 INVESTMENT PERFORMANCE

Core Investments

10.1. During 2019/20, the in house function has invested core cash funds in fixed term deposits, bonds, notice accounts, and certificates of deposits in the Money Markets. Table 1 in Appendix A illustrates the performance of the in house function during this first half year for each category normally invested in.

10.2 All the LIBID rates in the table and referred to below include a margin of 0.0625% to give the Benchmark.

10.3 During April to September eleven core investments matured. In all of the periods up to 365 days the Council out-performed against the Benchmark.

10.4 In September 2019 the Council took out PWLB borrowing of £12 million at a rate of 1.84% over 40 years (further details are in 14.2). £2 million was invested in the Santander 95-day notice account, £4 million in a 6 month fixed deposit with DBS Bank and £6 million in a 364 day fixed deposit with Helaba Bank.

10.5 Given that Bank Rate remains at 0.75% and counterparty security is of the utmost importance over return of yield, the level of performance achieved in this first half year continues to be satisfactory.

Cash Flow Derived Funds & Accounts

10.6 The in house function utilises Money Market Funds and Call Accounts to assist in managing its short term liquidity needs. Performance in this period is shown in table 2 of Appendix A.

10.7 During the half year, the Council’s cash flow investments were mainly into the Money Market Funds.

10.8 As with the Money Market investments in paragraph 10.1, the LIBID benchmark which in this case is the 7-day rate, has been increased by a margin of 0.0625% and it can be seen from table 2 in Appendix A that the total interest out performance of the benchmark remains satisfactory.

10.9 The Council continued to concentrate its investments in the highest performing funds Federated (variable and low volatility net asset value funds), Aberdeen Standard, Invesco and Royal London Cash Plus.

10.10 During the first half of 2019/20 the Council earned £145,900 realised interest on its Money Market Fund investments at an average rate of 0.85% and the average balance in the funds during the period was £34,506,400.

Call Accounts

10.11 As with the Money Market investments in paragraph 10.1, the LIBID benchmark, which in this case is the 7-day rate for HSBC and 1 month for Svenska Handelsbanken, has been increased by a margin of 0.0625%.

10.12 The Council earned £2,300 interest on its call accounts in the first half year at an average rate of 0.62% and the average balance in the funds during the period was £760,500.

10.13 The following table brings together the investments made in the various investment vehicles during the first half year to give an overall picture of the investment return:

Vehicle	Return (Annualised) £	Benchmark (Annualised) £	Performance £
Money Markets	165,700	145,600	20,100
Money Market Funds	145,900	108,700	37,200
Call A/c's	2,300	2,400	-100
Total	**313,900**	**256,700**	**57,200**

It should be noted that the total investment return of £313,900 shown in the table above will not all be received in 2019/20 as it is an annualised figure and will include interest relating to 2018/19 and 2020/21.

10.14 An analysis of the overall in house investments held by the Council at the end of September 2019 is shown in the following table:
(The balance at 31 March 2019 is shown for comparison)

Type of Investment	Closing balance @ 30 Sept 2019 £'000	Closing balance @ 31 March 2019 £'000
Money Markets incl. CD's & Bonds	41,900	35,500
Money Market Funds	29,786	25,345
Business Reserve Accounts incl. call accounts	6,551	1,295
Total In House Investments	**78,237**	**62,140**
Corporate Equity Funds	6,000	6,000
Total Investments	**84,237**	**68,140**

11. CORPORATE EQUITY FUNDS

11.1 The equity income fund values for the first half year are as follows:

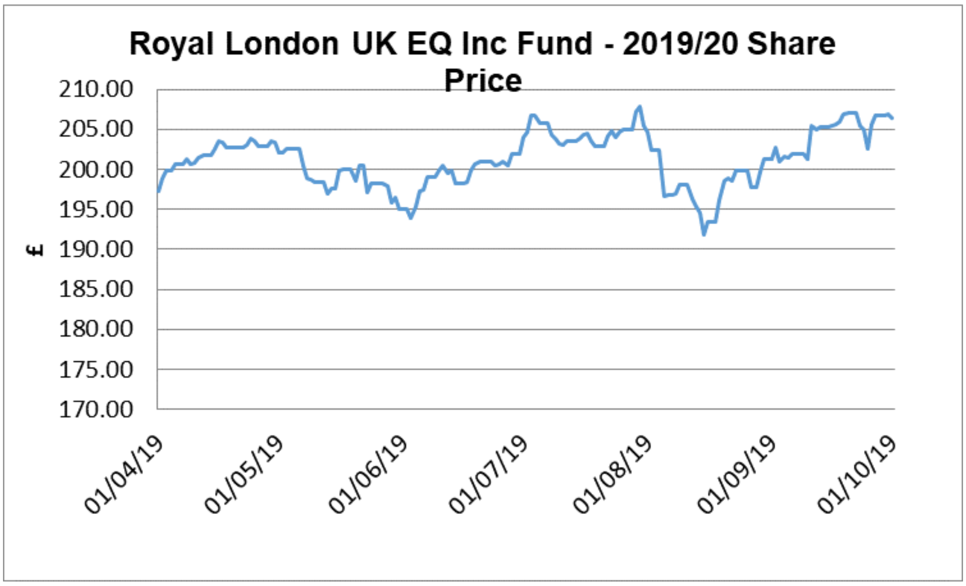
Fund	Value of Fund @ 30 Sept 2019 £'000	Value of Fund @ 31 March 2019 £'000	Variation in first half year £'000
Royal London UK Equity Fund	3,337	3,202	135
Columbia Threadneedle UK Equity Income Fund	3,203	3,031	172
TOTAL	**6,540**	**6,233**	**307**

11.2 It can be seen from the table above that both funds had a positive variation in value from April to September 2019.

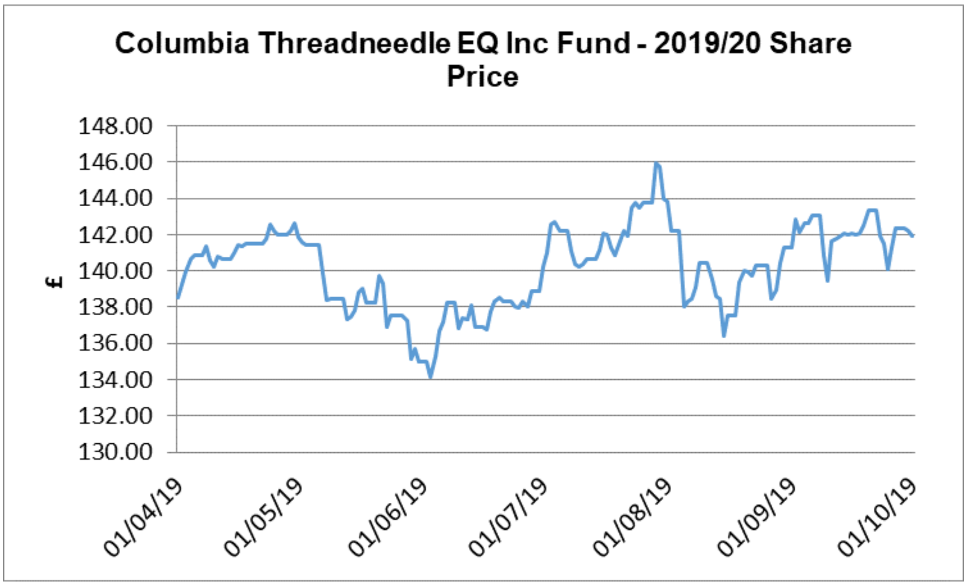
11.3 The table below gives a breakdown of income and capital elements of growth.

Period	Capital Element £'000	Income Element £'000	Total growth £'000	Capital Element %	Income Element %	Total growth %
Royal London Asset Management						
3 months (April 2019 to June 2019)	60.7	32.3	93	1.9	1.0	2.9
3 months (July 2019 to September 2019)	44.9	36.7	81.6	1.4	1.1	2.5
6 months (April 2019 to September 2019)	105.6	69.1	174.6	3.3	2.1	5.5
Since inception 04.04.2017	120.1	256.9	377	4.0	8.6	12.6
Columbia Threadneedle						
3 months (April 2019 to June 2019)	54	24.5	78.5	1.8	0.8	2.6
3 months (July 2019 to September 2019)	117.6	42.4	160	3.8	1.4	5.2
6 months (April 2019 to September 2019)	171.6	66.9	238.5	5.7	2.1	7.8
Since inception 13.04.2017	202.70	288.10	490.8	6.8	9.6	16.4

11.4 Royal London UK Equity Fund was ahead of competitor funds in the first quarter to June 2019 but behind the FTSE All Share index. Performance benefitted from a number of stocks including Dunelm, McCarthy & Stone, Marshalls and BBA Aviation. The fund's performance was negatively impacted by several stocks such as Saga, ITV, De La Rue, Intu Properties and Stobart Group. During the second quarter to September 2019 the fund was ahead of competitor funds and the FTSE All Share Index. The largest positive contributor to performance was Greene King. Stocks such as Investec, Intu Properties, Cineworld and Dunelm detracted from performance. For the full 6 months the Equity Fund out-performed the benchmark by 1.25%. It can be seen from the graph below that share prices dropped in May and August 2019 but had risen again by end of September 2019.



11.5 Columbia Threadneedle Equity Fund had a similar pattern in share price. With the exception of May, it surpassed the FTSE All-Share benchmark and the peer group each month. The top performers during the six months included AstraZeneca, Cobham and Electrocomponents and much of May's underperformance was due to detraction from Imperial Brands.



11.6 These investments are classed as long term investments and share prices can fluctuate. Disposals of shares needs to be done over a phased period in order to minimise capital losses.

12. COUNTERPARTY CREDIT RATINGS

12.1 The investments made in the first half year and the long and short term credit ratings applicable to the counterparty at the point at which the investment was made is shown in Appendix B.

12.2 All investments made within the first half year were in accordance with the Council's credit rating criteria.

12.3 Also attached for the Committee's information as Appendix B is the Council's current 2019/20 Counterparty lending list.

13. BENCHMARKING

13.1 With regard to the Link Asset Services Treasury Management Benchmarking Club, the Council is part of a local group comprising both District and County Councils and the results are published quarterly. Analysis of the results for the first quarter show that the Council's Weighted Average Rate of Return (WARoR) on its investments at 0.91% was in-line with Link's model portfolio.

13.2 The result for the September quarter was 0.94% WARoR which was above Link's model portfolio band range.

13.3 A comparison between Warwick District Council and the benchmarking group reveals that during the first quarter the Council's WARoR was marginally higher and the weighted average risk was lower. In the second quarter the WARoR and the weighted average risk were in-line.

14. BORROWING

14.1 During the half year, there was long term borrowing activity of £12 million along with paying the first half year interest instalment on the £136.157 million PWLB borrowing for the HRA Self Financing settlement which amounted to £2.383 million.

14.2 The Council took out the £12 million PWLB loan on 12 September at a 1.84% discounted rate and a maturity date of 28 August 2059. This was taken to replenish the Council's liquid funds which were projecting to be exhausted by early 2020. It was always intended to replace the £12 million spent on the refurbishment of two leisure centres from internal borrowing to a PWLB loan. The Council's treasury advisors, Link Asset Services, indicated that the optimal time to take the loan had presented itself as rates were going to rise. On 9 October PWLB increased their certainty rate by 1% thereby saving the Council £4.8 million in interest over the life of the maturity loan by taking the decision to borrow in September.

14.3 During the half year it was not necessary to undertake any Money Market borrowing to fund cash flow deficits, with any deficits being managed within the Council's £50,000 overdraft facility. The interest rate on this facility is 2.85% above Bank Rate and is charged on the cleared balance at the end of each day when that balance is in debit i.e. overdrawn. In the half year there was a minimal amount of overdraft interest.

15 PRUDENTIAL INDICATORS

15.1 The 2019/20 Treasury Management Strategy included a number of Prudential Indicators within which the Council must operate. The two major ones are the Authorised Limit and Operational Boundary for borrowing purposes. It is confirmed that during the half year neither indicator has been exceeded.

15.2 Appendix E contains recommended revisions to a Prudential Indicator to make it more pertinent to the current treasury management position of internal borrowing.

16. 2020/21 Treasury Management Strategy.

16.1 Work is about to commence on preparing the 2020/21 Treasury Management and Investment Strategies. Whilst security of the funds will be paramount, it is intended that the Council will continue to achieve the best returns possible but within Environment, Social and Governance ("ESG" – aka "ethical") criteria, where possible. Details will be included within the forthcoming Treasury Management report in February.

APPENDIX A

Investment Performance Analysis

Table 1 – Summary Performance

Period	Investment Return (Annualised)	LIBID Benchmark (Annualised)	Out/(Under) Performance
Up to 7 days—no investments			
Over 7 days & Up to 3 months			
April to September 2019	0.88%	0.72%	0.16%
Interest earned first half year	£6,606	£5,451	£1,155
Over 3 months & Up to 6 months			
April to September 2019	0.90%	0.80%	0.10%
Interest earned first half year	£77,835	£68,835	£9,000
Over 6 months to 365 days			
April to September 2019	1.02%	0.89%	0.13%
Interest earned first half year	£81,245	£71,362	£9,883
1 year and over—no investments			
TOTAL INTEREST FIRST HALF YEAR	**£165,686**	**£145,648**	**£20,038**

Table 2 - Cash Flow Derived Funds & Accounts

Period	Investment Return (Annualised)	LIBID Benchmark (Annualised)	Out/(Under) Performance
Deutsche (CNAV)			
April to September 2019	0.68%	0.63%	0.05%
Interest earned first half year	£3,377	£3,127	£250
Goldman Sachs (CNAV)			
April to September 2019	0.92%	0.63%	0.29%
Interest earned first half year	£3,236	£2,220	£1,016
Invesco (CNAV)			
April to September 2019	0.74%	0.63%	0.11%
Interest earned first half year	£28,084	£24,049	£4,035
Aberdeen Standard (LVNAV)			
April to September 2019	0.75%	0.63%	0.12%
Interest earned first half year	£35,142	£29,509	£5,633
Federated Constant Net Asset Value (CNAV)			
April to September 2019	0.81%	0.63%	0.18%
Interest earned first half year	£15,074	£9,320	£5,754
Federated Variable Net Asset Value (VNAV)			
April to September 2019	0.88%	0.63%	0.25%
Interest earned first half year	£26,276	£19,002	£7,274
Royal London Cash Plus Account (VNAV)			
April to September 2019	0.58%	0.63%	-0.05%
Interest earned first half year	£34,672	£19,058	£15,614
TOTAL INTEREST FIRST HALF YEAR	**£145,861**	**£106,285**	**£39,576**

Table 3 – Call Accounts

Call Accounts-- Period	Investment Return (Annualised)	LIBID Benchmark (Annualised)	Out/(Under) Performance
HSBC Business Deposit Account			
April to September 2019	0.62%	0.63%	-0.01%
Interest earned 1st half year £	2,285	2,337	-52
Svenska Handelsbanken Account			
April to September 2019	0.57%	0.66%	-0.09%
Interest earned 1st half year £	60	69	-9
TOTAL INTEREST FIRST HALF YEAR £	**2,345**	**2,406**	**-61**

APPENDIX B

Warwick District Council Counterparty Lending List

Counterparty	Investment Amount £	Credit Rating		Duration of Investment (days)
		Long Term	Short Term	
WDC Minimum	(Fitch)	**A+**	**F1**	
Banks				
Lloyds Bank	£1,000,000	A+	F1	92
Lloyds Bank	£1,000,000	A+	F1	183
Lloyds Bank	£2,000,000	A+	F1	365
DBS Bank Ltd	£5,000,000	AA-	F1+	182
Standard Charter-CD	£2,000,000	A+	F1	182
Helaba	£6,000,000	A+	F1	364
Santander 95 day Notice Account	£2,500,000	A+	F1	61 days to end Sept 2019
Santander 95 day Notice Account	£2,000,000	A+	F1	55 days to end Sept 2019
Santander 95 day Notice Account	£2,000,000	A+	F1	11 days to end Sept 2019
Building Societies		**n/a**	**n/a**	
West Bromwich	£1,000,000	n/a	n/a	91
National Counties	£1,000,000	n/a	n/a	92
WDC Minimum	(Fitch)	**A**	**n/a**	
London Stock Exchange-Bond	£1,900,000	A	n/a	147
Local Authority		**n/a**	**n/a**	
Surrey Heath Council	£3,000,000	n/a	n/a	183
Surrey Heath Council	£1,000,000	n/a	n/a	183
Thurrock Council	£2,000,000	n/a	n/a	103
Thurrock Council	£2,000,000	n/a	n/a	98
Money Market Funds (Investment amount is average principal in fund during half year)				
WDC Minimum	Fitch AAA & Volatility rating VR1+ or S & P AAAm or Moodys AAA & Volatility Rating MR1+			
Deutsche	£989,808	Fund retained its rating throughout half year		liquid
Goldman Sachs	£702,724	Fund retained its rating throughout half year		liquid
Invesco	£7,611,357	Fund retained its rating throughout half year		liquid
Federated	£9,786,424	Fund retained its rating throughout half year		liquid
Aberdeen Standard	£9,000,000	Fund retained its rating throughout half year		liquid
Royal London Asset Management	£6,000,000	Fund retained its rating throughout half year		liquid
Call Accounts				
WDC Minimum	(Fitch)	**A+**		**F1**
HSBC Business Deposit Account	£739,528	Counterparty retained its rating throughout period AA- long term,F1+ short term.		liquid
Svenska Handelsbanken	£0	Counterparty retained its rating throughout period of AA- long term, F1+ short term,		liquid

APPENDIX C

Link Asset Services Commentary on the Current Economic Background

1.1 UK

This first half year has been a time of upheaval on the political front as Theresa May resigned as Prime Minister to be replaced by Boris Johnson on a platform of the UK leaving the EU on or 31 October, with or without a deal. However, in September, his proroguing of Parliament was overturned by the Supreme Court and Parliament carried a bill to delay Brexit until 31 January 2020 if there is no deal by 31 October. MPs also voted down holding a general election before 31 October, though one is likely before the end of 2019. So far, there has been no majority of MPs for any one option to move forward on enabling Brexit to be implemented. At the time of writing the whole Brexit situation is highly fluid and could change radically by the day. Given these circumstances and the likelihood of an imminent general election, any interest rate forecasts are subject to material change as the situation evolves. If the UK does soon achieve a deal on Brexit agreed with the EU then it is possible that growth could recover relatively quickly. The MPC could then need to address the issue of whether to raise Bank Rate at some point in the coming year when there is little slack left in the labour market; this could cause wage inflation to accelerate which would then feed through into general inflation. On the other hand, if there was a no deal Brexit and there was a significant level of disruption to the economy, then growth could weaken even further than currently and the MPC would be likely to cut Bank Rate in order to support growth. However, with Bank Rate still only at 0.75%, it has relatively little room to make a big impact and the MPC would probably suggest that it would be up to the Chancellor to provide help to support growth by way of a fiscal boost by e.g. tax cuts, increases in the annual expenditure budgets of government departments and services and expenditure on infrastructure projects, to boost the economy.

The first half of 2019/20 has seen UK **economic growth** fall as Brexit uncertainty took a toll. In its Inflation Report of 1 August, the Bank of England was notably downbeat about the outlook for both the UK and major world economies. The MPC meeting of 19 September reemphasised their concern about the downturn in world growth and also expressed concern that prolonged Brexit uncertainty would contribute to a build-up of spare capacity in the UK economy, especially in the context of a downturn in world growth. This mirrored investor concerns around the world which are now expecting a significant downturn or possibly even a recession in some major developed economies. It was therefore no surprise that the Monetary Policy Committee (MPC) left Bank Rate unchanged at 0.75% throughout 2019, so far, and is expected to hold off on changes until there is some clarity on what is going to happen over Brexit. However, it is also worth noting that the new Prime Minister is making some significant promises on various spending commitments and a relaxation in the austerity programme. This will provide some support to the economy and, conversely, take some pressure off the MPC to cut Bank Rate to support growth.

As for **inflation** itself, CPI has been hovering around the Bank of England's target of 2% during 2019, but fell to 1.7% in August. It is likely to remain close to 2% over the next two years and so it does not pose any immediate concern to the MPC at the current time. However, if there was a no deal Brexit, inflation could rise towards 4%, primarily as a result of imported inflation on the back of a weakening pound.

With regard to the **labour market**, despite the contraction in quarterly GDP growth of -0.2% q/q, (+1.3% y/y), in quarter 2, employment continued to rise, but at only a muted rate of 31,000 in the three months to July after having risen by no less than 115,000 in quarter 2 itself: the latter figure, in particular, suggests that firms are preparing to expand output and suggests there could be a return to positive growth in quarter 3. Unemployment continued at a 44 year low of 3.8% on the Independent Labour Organisation measure in July and the participation rate of 76.1% achieved a new all-time high. Job vacancies fell for a seventh consecutive month after having previously hit record levels. However, with unemployment continuing to fall, this month by 11,000, employers will still be having difficulty filling job vacancies with suitable staff. It was therefore unsurprising that wage inflation picked up to a high point of 3.9% in June before easing back slightly to 3.8% in July, (3 month average regular pay, excluding bonuses). This meant that in real terms, (i.e. wage rates higher than CPI inflation), earnings grew by about 2.1%. As the UK economy is very much services sector driven, an increase in household spending power is likely to feed through into providing some support to the overall rate of economic growth in the coming months. The latest GDP statistics also included a revision of the savings ratio from 4.1% to 6.4% which provides reassurance that consumers' balance sheets are not over stretched and so will be able to support growth going forward. This would then mean that the MPC will need to consider carefully at what point to take action to raise Bank Rate if there is an agreed Brexit deal, as the recent pick-up in wage costs is consistent with a rise in core services inflation to more than 4% in 2020.

In the **political arena**, if there is a general election soon, this could result in a potential loosening of monetary policy and therefore medium to longer dated gilt yields could rise on the expectation of a weak pound and concerns around inflation picking up although, conversely, a weak international backdrop could provide further support for low yielding government bonds and gilts.

1.2 USA

President Trump's massive easing of fiscal policy in 2018 fuelled a temporary boost in consumption in that year which generated an upturn in the rate of strong growth to 2.9% y/y. Growth in 2019 has been falling back after a strong start in quarter 1 at 3.1%, (annualised rate), to 2.0% in quarter 2. Quarter 3 is expected to fall further. The strong growth in employment numbers during 2018 has reversed into a falling trend during 2019, indicating that the economy is cooling, while inflationary pressures are also weakening The Fed finished its series of increases in rates to 2.25 – 2.50% in December 2018. In July 2019, it cut rates by 0.25% as a 'midterm adjustment' but flagged up that this was not to be seen as the start of a series of cuts to ward off a downturn in growth. It also ended its programme of quantitative tightening in August, (reducing its holdings of treasuries etc). It then cut rates again in September to 1.75% - 2.00% and is thought likely to cut another 25 bps in December. Investor confidence has been badly rattled by the progressive ramping up of increases in tariffs President Trump has made on Chinese imports and China has responded with increases in tariffs on American imports. This trade war is seen as depressing US, Chinese and world growth. In the EU, it is also particularly impacting Germany as exports of goods and services are equivalent to 46% of total GDP. It will also impact developing countries dependent on exporting commodities to China.

1.3 EUROZONE

Growth has been slowing from +1.8 % during 2018 to around half of that in 2019. Growth was +0.4% q/q (+1.2% y/y) in quarter 1 and then fell to +0.2% q/q (+1.0% y/y) in quarter 2; there appears to be little upside potential to the growth rate in the rest of 2019. German GDP growth fell to -0.1% in quarter 2; industrial production was down 4% y/y in June with car production down 10% y/y. Germany would be particularly vulnerable to a no deal Brexit depressing exports further and if President Trump imposes tariffs on EU produced cars. The European Central Bank (ECB) ended its programme of quantitative easing purchases of debt in December 2018, which meant that the central banks in the US, UK and EU had all ended the phase of post financial crisis expansion of liquidity supporting world financial markets by purchases of debt. However, the downturn in EZ growth in the second half of 2018 and into 2019, together with inflation falling well under the upper limit of its target range of 0 to 2%, (but it aims to keep it near to 2%), has prompted the ECB to take new measures to stimulate growth. At its March meeting it said that it expected to leave interest rates at their present levels "at least through the end of 2019", but that was of little help to boosting growth in the near term. Consequently, it announced a third round of TLTROs; this provides banks with cheap borrowing every three months from September 2019 until March 2021 which means that, although they will have only a two-year maturity, the Bank is making funds available until 2023, two years later than under its previous policy. As with the last round, the new TLTROs will include an incentive to encourage bank lending, and they will be capped at 30% of a bank's eligible loans. However, since then, the downturn in EZ and world growth has gathered momentum so at its meeting on 12 September, it cut its deposit rate further into negative territory, from -0.4% to -0.5%, and announced a resumption of quantitative easing purchases of debt. It also increased the maturity of the third round of TLTROs from two to three years. However, it is doubtful whether this loosening of monetary policy will have much impact on growth and unsurprisingly, the ECB stated that governments will need to help stimulate growth by fiscal policy. On the political front, Austria, Spain and Italy are in the throes of forming coalition governments with some unlikely combinations of parties i.e. this raises questions around their likely endurance. The recent results of two German state elections will put further pressure on the frail German CDU/SDP coalition government.

1.4 CHINA

Economic growth has been weakening over successive years, despite repeated rounds of central bank stimulus; medium term risks are increasing. Major progress still needs to be made to eliminate excess industrial capacity and the stock of unsold property, and to address the level of non-performing loans in the banking and credit systems. Progress also still needs to be made to eliminate excess industrial capacity and to switch investment from property construction and infrastructure to consumer goods production. The trade war with the US does not appear currently to have had a significant effect on GDP growth as some of the impact of tariffs has been offset by falls in the exchange rate and by transhipping exports through other countries, rather than directly to the US.

1.5 JAPAN

Japan has been struggling to stimulate consistent significant GDP growth and to get inflation up to its target of 2%, despite huge monetary and fiscal stimulus. It is also making little progress on fundamental reform of the economy.

1.6 WORLD GROWTH

The trade war between the US and China is a major concern to financial markets and is depressing worldwide growth, as any downturn in China will spill over into impacting countries supplying raw materials to China. Concerns are focused on the synchronised general weakening of growth in the major economies of the world compounded by fears that there could even be a recession looming up in the US, though this is probably overblown. These concerns have resulted in government bond yields in the developed world falling significantly during 2019. If there were a major worldwide downturn in growth, central banks in most of the major economies will have limited ammunition available, in terms of monetary policy measures, when rates are already very low in most countries, (apart from the US), and there are concerns about how much distortion of financial markets has already occurred with the current levels of quantitative easing purchases of debt by central banks. The latest PMI survey statistics of economic health for the US, UK, EU and China have all been sub 50 which gives a forward indication of a downturn in growth; this confirms investor sentiment that the outlook for growth during the rest of this financial year is weak.

Warwick District Council Standard Lending List as at October 2019

Banks

Investments up to 365 days (3 months for explicitly guaranteed subsidiaries)

Investment / Counterparty type:	S/term	L/term minimum	Security / Min credit rating	Max limit per counterparty	Max. Maturity period	Use
Bank deposits	F1	A	UK Sovereign	£8m AA- & above, £6m if L/term rating minimum A+,£4m if L/Term rating A.	365 days	In House +Advice & EFM*
Bank - part nationalised UK	F1	A	UK Sovereign	£9m	365 days	In House +Advice & EFM*
Bank subsidiaries of UK Banks	Unrated	Unrated	Explicit Parent Guarantee	£5m	3 months	In House +Advice & EFM*

NB. Includes Business Call Reserve Accounts and special tranches and any other form of investment with that institution e.g. Certificate of Deposits, Corporate Bonds and Repo’s except where the Repo collateral is more highly credit rated than the counterparty in which case the counterparty limit is increased by £3m with a maximum in Repo's of £3m.

Counterparty Limit is also the Group Limit where investments are with different but related institutions.

Investments over 365 days

Investment/ Counterparty type:	S/term	L/term Min	Security/ Min credit rating	Max limit per counterparty	Max. Maturity period	Use
Bank deposits	F1	A	UK Sovereign	£8m AA- & above, £6m if L/term rating minimum A+,£4m if L/Term rating A.	2 years	In House +Advice & EFM*
Bank - part nationalised UK	F1	A	UK Sovereign	£9m	2 years	In House +Advice & EFM*

NB. Includes Business Call Reserve Accounts and special tranches and any other form of investment with that institution e.g. Certificate of Deposits, Corporate Bonds and Repo's.

Counterparty limit is also the Group Limit where investments are with different but related institutions.

£15m overall limit for Corporate Bond / Property Funds & £20m limit for all counterparties.

£20m over 365 day limit only applies to those investments where at 1 April the remaining term is greater than 365 days. Any over 365 day investment with 365 days or less to maturity at 1 April is deemed to be short term.

BANK NAME	OTHER BANKS IN GROUP (*= Not on list but included for information re potential problems etc.)	GROUP LIMIT APPLIES
AUSTRALIA (AAA)		
Australia & New Zealand Banking Group Ltd		
Commonwealth Bank of Australia		
Macquarie Bank Ltd		
National Australia Bank Ltd	Bank of New Zealand* Yorkshire Bank *(Trading name of Clydesdale) Clydesdale Bank*	Yes
Westpac Banking Corporation		
BELGIUM (AA)		
BNP Paribas Fortis		
KBC Bank NV		
CANADA (AAA)		
Bank of Montreal	Bank of Montreal Ireland plc*	
Bank of Nova Scotia	Scotia Bank* Scotia Bank (Ireland) Ltd* Scotia Bank Capital Trust (United States)* Scotia Bank Europe plc*	
Canadian Imperial Bank of Commerce	Canadian Imperial Holdings Inc New York* CIBC World Markets Holdings Inc*	
National Bank of Canada	National Bank of Canada New York Branch*	
Royal Bank of Canada-negative outlook	Royal Trust Company* Royal Bank of Canada Europe* Royal Bank of Canada Suisse* RBC Centura Banks Inc*	
Toronto Dominion Bank	TD Banknorth Inc*	
DENMARK (AAA)		
Danske Bank		
FINLAND (AA+)		
Nordea Bank Finland	Nordea Bank Denmark* Nordea Bank AB Nordea Bank Norge* Nordea Bank North America*	Yes
FRANCE (AA)		
BNP Paribas		
Credit Agricole Corporate & Investment Bank		
Credit Industriel et Commercial		
Credit Agricole SA		
Societe Generale		
GERMANY (AAA)		
DZ Bank AG (Deutsche Zentral-genossenscaftsbank)		
Landesbanken Hessen-Thueringen Girozentrale (Helaba)		
Landwirtschaftliche Rentenbank		
NRW Bank		

BANK NAME	OTHER BANKS IN GROUP (*= Not on list but included for information re potential problems etc.)	GROUP LIMIT APPLIES
HONG KONG (AA+) –		
The Hong Kong & Shanghai Banking Corporation Ltd		
LUXEMBOURG (AAA)		
Clearstream Banking		
NETHERLANDS (AAA)		
ABN AMRO Bank N.V		
Bank Nederlandse Gemeenten		
Cooperatieve Centrale Raiffeisen Boerenleenbank BA (Rabobank Nederland)		
ING Bank NV		
QATAR (AA)OUT OF RANGE—negative watch		
Qatar National Bank-monitoring		
SINGAPORE (AAA)		
DBS Bank Ltd	DBS Bank (Hong Kong)*	
Oversea Chinese Banking Corporation Ltd		
United Overseas Bank Ltd		
SWEDEN (AAA)		
Skandinaviska Enskilde Banken AB	SEB Bolan*	
Svenska Handelsbanken AB	Stadtshypotek* Svenska Handelsbanken Inc USA*	
Swedbank AB		
SWITZERLAND (AAA)		
Credit Suisse AG		
UBS AG		
UNITED ARAB EMIRATES (AA)- out of range		
First Abu Dhabi Bank PJSC		
UNITED KINGDOM (AA)negative outlook		
Abbey National Treasury Services plc		
Barclays Bank plc- LT Watch		
Close Brothers		
Goldman Sachs International Bank		
Handelsbanken Plc		
HSBC Bank plc	HSBC AM* HFC Bank Ltd* Hong Kong & Shanghai Banking Corporation* HSBC Finance Corp* HSBC Finance* HSBC USA	Yes

BANK NAME	OTHER BANKS IN GROUP (*= Not on list but included for information re potential problems etc.)	GROUP LIMIT APPLIES
	Hang Seng Bank*	
Lloyds Banking Group :- Lloyds TSB Bank of Scotland	Halifax plc* Bank of Western Australia Ltd*. Cheltenham & Gloucester* Scottish Widows Investment Partnership* Scottish Widows plc*	Yes
National Westminster Bank PLC (RFB)		
NatWest Markets Plc (NRFB)		
Royal Bank Of Scotland (RFB)		
Santander UK plc		
Standard Chartered Bank		
Sumitomo Mitsui Banking Corporation Europe Ltd		
UBS Ltd		
UNITED STATES OF AMERICA (AAA) MONITORING		
Bank Of America		
Bank of New York Mellon	Bank of New York (Delaware USA)* Bank of New York (New York USA)* Bank of New York Trust Company*	
Citibank		
JP Morgan Chase Bank NA	Bank One Corp* Bank One Financial LLC* Bank One NA * First USA Inc* NDB Bank NA* Chemical Bank * Chemical Banking Corp* JP Morgan & Co Inc* Chase Bank USA* Robert Fleming Ltd*	
Wells Fargo Bank NA	Wachovia Bank* Wachovia Bank NA North Carolina USA*	

<u>Building Societies</u>

Investments up to 365 days

Investment/ Counterparty type:	S/term	L/term	Security/ Min credit rating	Max limit per counter-party	Max. Maturity period
Building Societies - category A	F1	A	UK Sovereign	£4m	365 days
Building Societies - category B • Coventry • Nationwide	F1		UK Sovereign	£2m	365 days
Building societies – assets > £500m (Category C) • Yorkshire • Skipton • Leeds • Principality				£1m	3 months

Investment/ Counterparty type:	S/term	L/term	Security/ Min credit rating	Max limit per counter-party	Max. Maturity period
• West Bromwich • Newcastle (Fitch removed ratings 7.9.16) • Nottingham • Progressive • Cumberland • National Counties • Saffron • Cambridge • Monmouthshire • Furness • Leek United • Newbury • Hinckley & Rugby • Ipswich					

Investments over 365 days

Investment/ Counterparty type:	S/term	L/term	Security/ Min credit rating	Max limit per counter-party	Max. Maturity period
Building societies Category A & B (see above)	F1	A	UK Sovereign	£1m	2 years

NB. Group limit of £8m.

<u>Other Counterparties</u>

Investment/ Counterparty type:	S/term	L/term	Security/ Min credit rating	Max limit per counter-party	Max. Maturity period
DMADF	n/a	n/a	UK Sovereign	£12m	365 days
UK Govt. (includes Gilt Edged Securities & Treasury Bills), Local Authorities / Public Corporations /Nationalised Industries.	n/a	n/a	High viability/support	£9m	365 days
Money Market Fund(CNAV)	AAAm / Aaa-mf/AAAmmf			£10m	liquid
Money Market Fund (VNAV)	AAAf S1 / Aaa-bf/ AAA/V1			£6m	liquid
Corporate bonds - category 1		A	UK Sovereign	£4m	2 years
		A+		£5m	
		AA - & ABOVE		£6m	
Corporate bonds - category 2		A		£9m	2 years
Corporate bonds - category 3		A	UK Sovereign	£4m	2 years
		A+		£5m	
		AA - & ABOVE		£6m	
Covered bonds - category 1		A	UK Sovereign	£4m	2 years
		A+		£5m	
		AA - &		£6m	

Investment/ Counterparty type:	S/term	L/term	Security/ Min credit rating	Max limit per counter-party	Max. Maturity period
		ABOVE			
Covered bonds - category 2		A		£9m	2 years
Covered bonds - category 3		A	UK Sovereign	£4m	2 years
		A+		£5m	
		AA - & ABOVE		£6m	
Bonds - Supranational / Multi Lateral Development Banks European Community European Investment Bank African Development Bank Asian Development Bank Council of Europe Development Bank European Bank for Reconstruction & Development Inter-American Development Bank International Bank of Reconstruction & Development *Or* any other Supranational/Multi-Lateral Development Bank meeting criteria.	AAA / Govt Guarantee			£5m	365 days
Floating Rate Notes - category 1		A		£4m	364 days
		A+		£6m	
		AA - & ABOVE		£7m	
Floating Rate Notes - category 2		A		£9m	364 days
Floating Rate Notes - category 3		A		£4m	364 days
		A+		£5m	
		AA - & ABOVE		£6m	
Eligible Bank Bills	n/a		Determined by EFM	£5m	364 days
Sterling Securities guaranteed by HM Government	n/a		UK Sovereign	£9m	Not defined
Local Authorities	n/a	Viability/support= High £15m overall limit for Corporate Bond/Property Funds & £20m limit for all counterparties.		£9m	5 years
Corporate Equity Funds - low risk (UK Equity Income Funds)	n/a	Maximum investment limit subject to 10% capital growth i.e. maximum is 110% of original investment.		£4m	10 years
Corporate Equity Funds - medium risk (UK Capital Growth Funds)	n/a	Maximum investment limit subject to 10% capital growth i.e. maximum is 110% of original investment.		£2m	10 years
Corporate Bond Funds	BBB	£15m overall limit for Corporate Bond/Property Funds & £20m limit for all counterparties.		£5m	10 years
Pooled property fund eg: REITS	£15m overall limit for Corporate Bond/Property Funds & £20m limit for all counterparties.			£5m	10 years

Investment/ Counterparty type:		S/term	L/term	Security/ Min credit rating	Max limit per counter-party	Max. Maturity period
CCLA property funds	n/a	Security of Trustee of fund (LAMIT) controlled by LGA, COSLA who appoint the members and officers of LAMIT. £15m overall limit for Corporate Bond/Property Funds & £20m limit for all counterparties.			£5m	10 years

Categories for Covered Bonds, Corporate Bonds (must be Senior Unsecured), Floating Rate Notes:

Category 1: Issued by private sector Financial Institutions
Category 2: Issued by Financial institutions wholly owned or part owned by the UK Government
Category 3: Issued by Corporates

Prudential Indicators

1.1 The Prudential Indicators for 2019/20 were presented to the Executive on 6 February 2019 and ratified by the Council on 20 February 2019. This is a statutory duty under Section 3 of the Local Government Act 2003 and supporting regulations, for the Council to determine and keep under review how much it can afford to borrow each financial year.

1.2 The Council has been using its reserves and balances to support capital expenditure as 'internal borrowing' for a couple of years, rather than taking external long-term loans. This was primarily because this was a cheaper option while long-term borrowing rates were expected to remain low. Internal borrowing was £11 Million at 31 March 2018 and £22 million at 31 March 2019.

1.3 CIPFA is reviewing how the increasing trend for councils to utilise internal borrowing needs to be reflected in accounting standards, as these are currently 'silent' in this matter.

1.4 In order to provide sufficient flexibility to the Council's future long-term borrowing and future-proof the Council's Prudential Indicators against any change in practice relating to internal borrowing, it is recommended that the indicator below is revised, increasing the limit for longer-terms loan (i.e. 10 years and above) to 100%:

Upper and Lower Limits respectively for the Maturity Structure of Fixed Interest Rate Borrowing – mid-year revision

Period	**Upper**		**Lower**
	Current	**Revised**	**Current**
Under 12 months	4%	20%	0%
12 months and within 24 months	20%	20%	0%
24 months and within 5 years	20%	20%	0%
5 years and within 10 years	20%	20%	0%
10 years and above	96%	100%	0%

1.5 This will enable any future loans - in addition to the £136 million HRA loans from 2011/12 and the £12 million taken in September 2019 for the General Fund - to take advantage of an interest rate yield curve that may favour longer-term loans, which match the pool of underlying new assets.

1.6 Increasing the 'Under 12 months' limit to 20% would allow for circa £32 million of internal borrowing. Although the Prudential Code does not specifically identify internal borrowing, it would be good practice to allow for this position in the Council's indicators, to reflect this element of borrowing.