

Performance and Resources Scrutiny Programme 2019/20

Report to: the Office of the Police, Fire and Crime Commissioner for Essex

Title of Report:	Half Year Treasury Management Review 2019/20
Classification:	Official
Chief Officer	Abbey Gough, Acting Treasurer to the PFCC for Essex
Report from:	Corporate Finance
Date of Meeting:	31st October 2019
Author on behalf of Chief Officer:	Matt Tokley, Corporate Accounting Manager
Date of Approval:	22nd October 2019

1.0 Purpose of Report

1.1 To present the half-year treasury review for 2019/20. The Chartered Institute of Public Finance and Accountancy (CIPFA) definition of treasury management:

‘The management of the organisation’s cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks’.

1.2 To present an update regarding investments and borrowings with both UK and, where appropriate, non-UK financial institutions.

2.0 Recommendations

2.1 The PFCC is recommended to:-

- (i) Note the half-year treasury review for 2019/20.
- (ii) Approve the recommendations set out in respect of amendments for the use of money market funds in paragraphs 6.4/6.5.
- (ii) Maintain the treasury investment limits shown in appendix B.

3.0 **Executive Summary**

3.1 This report provides the PFCC with a half-yearly review of treasury management activity as well as the economic backdrop which we are currently operating in.

4.0 **Introduction/Background**

4.1 The OPFCC has adopted the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice* (the CIPFA Code) which requires the OPFCC to approve treasury management semi-annual and annual reports.

4.2 The OPFCC's Treasury Management Strategy for 2019/20 was approved at the 14th March 2019 Strategic Board by the PFCC. The OPFCC invests substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to the OPFCC's treasury management strategy.

4.3 The 2017 Prudential Code includes a requirement for the OPFCC to provide a Capital Strategy, a summary document approved by the PFCC covering capital expenditure and financing, treasury management and non-treasury investments. This document, complying with CIPFA's requirement, was also approved at the 14th March 2019 Strategic Board.

5.0 **Current Work and Performance**

5.1 On 31st March 2019, the OPFCC had net investments of £16.42m (£14.13m, 31st March 2018) arising from revenue and capital income and expenditure. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. These elements are presented in table 1 below.

Table 1: Balance Sheet Summary

	31/3/19 Actual £m
Capital financing requirement	6.57
Less: usable reserves	(22.81)
Less: working capital deficit	(0.18)
Net (borrowing)/investments	16.42

5.2 The treasury management cashbook position as at the 30th September 2019 and the change over the period is shown in table 2 below.

Table 2: Treasury Management Summary

	31/3/19 Balance £m	Movement £m	30/9/19 Balance £m
Long/short-term borrowing	0.00	0.00	0.00
Total borrowing	0.00	0.00	0.00
Long-term investments	0.00	0.00	0.00

Short-term investments	8.52	10.96	19.48
Cash and cash equivalents	7.90	(0.08)	7.82
Total investments	16.42	10.88	27.30
Total net investments	16.42	10.88	27.30

5.3 Investments

The OPFCC holds invested funds, representing income received in advance of expenditure plus balances and reserves held. During the year to date the OPFCC's investment balances have ranged between £1.5m and £54m due to timing differences between income and expenditure.

5.4 Both the CIPFA Code and government guidance require the OPFCC to invest its funds prudently, and to have regard to the security and liquidity of its treasury investments before seeking the optimum rate of return, or yield. The OPFCC's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

5.5 The table below summarises the actual investments held at the 31st March 2019 and the 30th September 2019 (excluding accrued interest and other adjustments). Please refer to Appendix A for full details of these investments.

Table 3: Investments

Investments	31/3/19 £m	30/9/19 £m
Call accounts & money market funds	10.62	13.15
Fixed term deposits	8.50	9.50
Treasury Bills	0.00	9.98
Lloyds current account	0.71	0.62
Total	19.83	33.25

5.6 The increase in investments between the two dates is mainly due to the receipt of £34.63m Police Pensions Top-Up Grant in July 2019. Whilst a large proportion of this income has subsequently been required to cover cashflow commitments, a significant element has also been able to be invested in various instruments. Investments will steadily decrease over the second half of the year, mainly due to the OPFCC's capital programme outgoings as well as the standard revenue budget outgoings. The OPFCC does not have a significant amount of capital receipts expected during 2019/20 to cushion the cashflow position in the same way as 2018/19. The total cash and investments balance as at the 31 March 2020 is forecast to be in the region of £10m.

5.7 The average level of investments over the first six month period of 2019/20 was £27.50m. Interest earnings for the period (including the accrued element) were £0.088m, representing an average return of 0.64%. This average rate was an increase of 19 basis points over the figure at the same point last year. It should be noted that these figures do not include interest in subsequent months for deals already placed at the 30th September. The forecast investment income for the year is £0.160m, broadly in line with the 2018/19 outturn position. It is proposed that the

historic budget level of £0.080m is increased as part of the 2020/21 budget setting process.

5.8 Approved financial institutions

The 2019/20 treasury management strategy defines the country, duration and monetary limits for investments and this criteria is set out in Appendix B.

- 5.9 The PFCC's treasury advisors, Arlingclose, maintain a recommended lending list of UK banks and building societies, the UK Counterparty List. Arlingclose issue the list each month. The version issued on the 30th September 2019 includes the following counterparties:-

Table 4: Approved financial institutions

Arlingclose Recommended UK Counterparty List 30th September 2019	
Banks	Building Societies
Barclays Bank plc and Barclays Bank UK plc	Coventry Building Society
Close Brothers Limited	Leeds Building Society
Goldman Sachs International Bank	Nationwide Building Society
Handelsbanken plc	
HSBC Bank plc and HSBC UK Bank plc	
Lloyds Bank plc & Bank of Scotland plc	
NatWest Bank plc, RBS plc and Ulster Bank Ltd	
Santander UK plc	
Standard Chartered Bank	

- 5.10 In addition to the UK counterparties listed above Arlingclose also issue a list of non-UK counterparties on a monthly basis. These counterparties have not been listed in this report as whilst the 2019/20 Treasury Management Strategy includes non-UK entities they have not been used by the OPFCC in this year to date. Unrated building societies are also omitted from the above table as the OPFCC would not consider these as an investment option.
- 5.11 The OPFCC is currently in the process of setting up an account with Handelsbanken plc for additional investment options.
- 5.12 Any proposed investments would have to meet the criteria as set out in Appendix B before any deal is made with a counterparty on the Arlingclose list. Other factors which need to be considered are parent-subsidiary relationships (e.g. essentially exposure to the same counterparty) as well as which counterparties are actively willing to deal in the local authority/public sector market.
- 5.13 Borrowings
The OPFCC's chief objective when borrowing has been to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required. Where the cashflow has fallen into a minor deficit on certain dates the OPFCC has considered it to be more cost effective in the

short term to use internal resources and/or the current account bank overdraft.

- 5.14 There were no long-term borrowings during the period. There has been one instance of short-term borrowing during the first six month period of 2019/20. This was necessary to fund a temporary peak in cash outflows, notably supplier payments and payroll costs. The details of the borrowing is shown in the table below:-

Table 5: Borrowings

Borrowings – 2019/20	£m	Duration	Interest Rate
Northern Ireland Housing Executive	5.00	7 days	0.75%

- 5.15 It is doubtful that further short-term borrowing will be required for the remainder of 2019/20 although if this is required to meet further short-term cashflow deficits this will most likely be through the local authority market, particularly following the announcement that the PWLB certainty rate is rising by 100 basis points. The decision for which option we choose would be based on the term of the loan and the most favourable rate available at the time monies are required.

6.0 Implications (Issues)

- 6.1 Readiness for EI Exit & Proposed Amendment to Treasury Management Strategy
The scheduled leave date for the UK to leave the EU is now 31st October 2019 and there remains little political clarity as to whether a deal will be agreed by this date and there is the possibility that the exit date is pushed back yet again. As 31st October approaches the OPFCC will ensure there are enough accounts open at UK-domiciled banks and money market funds to hold sufficient liquidity required in the near term and that its account with the Debt Management Account Deposit Facility (DMADF) remains available for use in an emergency.
- 6.2 Whilst the OPFCC is in a sound position in terms of the liquidity and financial security of its investment portfolio, the criteria specified in paragraph 6.1 (as recommended by our advisors Arlingclose) does highlight that we do not currently have any accounts with UK-domiciled money market funds (MMF's). In order to achieve this we will need to amend our current limits as set out in the 2019/20 Treasury Management Strategy. This states the following limits apply:-

Money market funds	£5m per fund (minimum AAA rated), see paragraph 4.17 of 2019/20 Treasury Management Strategy for further details
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Money market funds (MMF): the guideline exposure for these funds will be as follows:-

- i) Investment exposure of no more than 0.5% of the total MMF (if a government MMF then this can be 2%)
- ii) Assuming condition i) is initially met, investments in each MMF are then limited to £5m maximum
- iii) Overall exposure to MMF's as a whole to £10m maximum

6.3 The current advice from Arlingclose sets out the following guidance in respect of money market funds. This is as follows:-

- i) Investment exposure of no more than 0.5% of the total MMF (if a government MMF then this can be 2%). Unchanged from current strategy document.
- ii) Assuming condition i) is initially met, investments in each MMF are limited to 10% of total investments held at any time. It is recommended to adopt this amendment.
- iii) Overall exposure to MMF's as a whole is limited to 50% of total investments held at any one time. It is recommended to adopt this amendment.
- iv) Investment exposure diversified, as far as practicable, over multiple MMF's, with broadly equal exposure to each fund. It is recommended to adopt this amendment.

6.4. In accordance with the guidance set out in paragraph 6.2 it is proposed to set up a minimum of two UK-domiciled money market funds to make the proposals set out in paragraph 6.3 workable and realistic from a cashflow and treasury management perspective. These funds will have to meet the minimum AAA-rated criteria.

6.5 Non-Treasury Investments

The definition of investments in CIPFA's revised Treasury Management Code now covers all the financial assets of the OPFCC as well as other non-financial assets which the OPFCC holds primarily for financial return. This is replicated in MHCLG's Investment Guidance, in which the definition of investments is further broadened to also include all such assets held partially for financial return.

6.6 As expected in the Investment Strategy 2019/20 the OPFCC has not held any non-treasury investments in the year to date.

6.7 Compliance

All treasury management activities undertaken during the first half of 2019/20 have complied fully with the CIPFA Code of Practice and the OPFCC's approved Treasury Management Strategy.

6.8 Compliance with the authorised limit and operational boundary for external debt is demonstrated in table 6 below.

Table 6: Debt Limits

	2019/20 Maximum (to date)	30.9.19 Actual	2019/20 Operational Boundary	2019/20 Authorised Limit	Complied? Yes/No
Borrowing	£5m	£0m	£10m	£20m	Yes

6.9 It should be noted that since the operational boundary is a management tool for in-year monitoring it is not significant if the operational boundary is breached on occasions due to variations in cash flow, and this is not counted as a compliance failure. For 2019/20 however there have been no instances to date when total debt was above the operational boundary.

6.10 Compliance with the approved investment counterparties list is demonstrated in table 7 below.

Table 7: Investment Counterparties

	2019/20 Maximum (to date)	30.9.19 Actual	2019/20 Guideline Limit	Complied?
UK central government (including Debt Management Office & Treasury Bills)	£43.0m	£15.0m	£ unlimited (50 years)	Yes
UK local government	£5.0m	£0.0m	£5.0m per authority (5 years)	Yes
Lloyds Bank account plc (operational bank account) <i>based on credit rating being A- or above during 2019/20 to date</i>	£4m	£0.6m / 1.9%	Higher of 5% or £1.0m (1 year), or up to £5.0m (overnight only)	Yes
UK financial institutions (between A and AAA, liquid investments) – Barclays Bank	£1.5m / 19.5% (max % where > £1m)	£1.5m / 4.5%	Higher of 5% or £1.0m (unlimited)	Yes*
UK financial institutions (between A and AAA, liquid investments) – Santander	£1.7m / 5.0 % (max % where > £1m)	£1.7m / 5.0%	Higher of 5% or £1.0m (unlimited)	Yes*
UK financial institutions (between A and AAA, fixed term deposits) – Coventry BS	£1.5m / 4.5%	£1.5m / 4.5%	Higher of 5% or £1.0m (1 year)	Yes**
UK financial institutions (between A and AAA, fixed term deposits) – Nationwide BS	£1.5m / 4.5%	£1.5m / 4.5%	Higher of 5% or £1.0m (1 year)	Yes**
UK financial institutions (between A and AAA, fixed term deposits) – Goldman Sachs Bank	£1.5m / 4.5%	£1.5m / 4.5%	Higher of 5% or £1.0m (1 year)	Yes**
Money market funds (AAA rated) - Aberdeen	£5.0m	£5.0m	£5.0m	Yes
Money market funds (AAA rated) - Insight	£5.0m	£5.0m	£5.0m	Yes
Money market funds (AAA rated) - Total	£10.0m	£10.0m	£10.0m	Yes

*Limits with call or notice accounts (e.g. Barclays and Santander) are calculated at the point that monies are invested or withdrawn. Whilst there were some instances when the balances of Barclays subsequently exceeded the recommended counterparty limit of 5% (e.g. not within the guidelines of the 19/20 strategy) it was nevertheless viewed as low-risk as the monies were either accessible on a same-day basis or, in respect of the Notice account, within a short timescale.

** Limits for counterparties with fixed term deposits are calculated only at the point that monies are invested e.g. by their nature the OPFCC cannot call back these investments during the term specified and therefore the OPFCC cannot legislate against the counterparty's % increasing during this period.

- 6.11 Performance in respect of UK entities with a credit rating of A- or below, all non-UK entities, corporates and registered providers have been omitted from the above table as these have not been used to date during 2019/20.

7.0 Treasury Management Indicators

- 7.1 The OPFCC measures and manages its exposure to treasury management risks using the following indicators.

- 7.2 **Interest rate exposure:** This indicator is set to control the OPFCC's exposure to interest rate risk. The upper limits on the one year revenue impact of a 1% rise or fall in interest rates was:-

Table 8: Interest rate exposure

	30/9/19 Actual	2019/20 Limit	Complied?
Upper limit on one year revenue impact of a 1% <u>rise</u> in interest rates	n/a	£300,000	✓
Upper limit on one year revenue impact of a 1% <u>fall</u> in interest rates	n/a	(£80,000)	✓

- 7.3 **Security:** The OPFCC has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average of its investment portfolio.

Table 9: Security

	30/9/19 Actual	2019/20 Target	Complied?
Portfolio average credit rating	A	A	✓

- 7.4 **Liquidity:** The OPFCC has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments on a daily basis, without the need for additional borrowing.

Table 10: Liquidity

	30/9/19 Availability	2019/20 Target	Complied?
OPFCC bank account overdraft facility available	£1m	£1m	✓

- 7.5 **Principal sums invested for periods longer than a year:** The purpose of this indicator is to control the PFCC's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the total principal sum invested to final maturities longer than one year were:

Table 11: Investments longer than one year

	30/9/19 Actual	2019/20 Target	Complied?
Principal invested beyond one year in duration	£0m	£0m	✓

8.0 **Equality and/or Human Rights Implications**

- 8.1 There is no impact on equality, diversity or human rights.

9.0 **Health and Safety Implications**

- 9.1 There are no health and safety implications for this report.

10.0 **Consultation/Engagement**

- 10.1 This paper has been prepared in consultation with Arlingclose, the OPFCC's treasury management advisers.

11.0 **Actions for Improvement**

- 11.1 These are noted in paragraphs 6.3 and 6.4.

12.0 **Future Work/Development**

- 12.1 A wider review of the use of strategic pooled funds is currently being undertaken, with a proposal that if approved, these will be included within the 2020/21 Treasury Management Strategy.

13.0 **Decisions Required by the Police, Fire and Crime Commissioner**

- 13.1 Please see recommendations section in paragraph 2.0.

Investment position at 31st March and 30th September 2019

31st March 2019

	31/3/19 £000	Start date	Maturity date	Approx. Rate %
Call/notice accounts				
Santander UK PLC	1,120			0.85%
Barclays Bank PLC	1,500			0.75%
Total	2,600			
Money market funds				
Aberdeen	5,000			0.79%
Insight	3,000			0.75%
Total	8,000			
Fixed term deposits				
Bank of England DMO	3,500	29/03/19	01/04/19	0.50%
Rotherham Council	5,000	24/10/18	23/04/19	0.90%
Total	8,500			
Other				
Lloyds current account	711			0.40%
Total	711			
Total treasury investments	19,811			

Appendix A (continued)

30th September 2019

	31/3/19 £000	Start date	Maturity date	Approx. Rate %
Call/notice accounts				
Santander UK PLC	1,650			0.70%
Barclays Bank PLC	1,499			0.50%
Total	3,149			
Money market funds				
Aberdeen	5,000			0.74%
Insight	5,000			0.71%
Total	10,000			
Fixed term deposits				
Bank of England DMO	3,500	25/09/19	01/10/19	0.50%
Bank of England DMO	1,500	30/09/19	07/10/19	0.50%
Nationwide BS	1,500	15/07/19	15/01/20	0.81%
Coventry BS	1,500	15/07/19	15/01/20	0.86%
Goldman Sachs	1,500	15/07/19	15/01/20	0.85%
Total	9,500			
Treasury Bills				
Bank of England DMO	4,991	08/07/19	07/10/19	0.69%
Bank of England DMO	4,991	15/07/19	14/10/19	0.72%
Total	9,982			
Other				
Lloyds current account	618			0.40%
Total	618			
Total cash & investments	33,249			

Counterparty criteria – Treasury Management Strategy 2019/20

Credit rating	Banks unsecured	Banks secured	Government	Corporates	Registered Providers
UK central government (including Debt Management Office)	n/a	n/a	£ unlimited (50 years)	n/a	n/a
UK local government	n/a	n/a	£5m per authority (5 years)	n/a	n/a
Lloyds Bank plc (operational bank account) where credit rating is A- or above	Higher of £1m or 5%* (1 year) An exception applies where planned cash outflows (e.g. salaries or creditor payments) necessitate additional funds being held:- £5m (overnight)	n/a	n/a	n/a	n/a
Lloyds Bank plc (operational bank account) where credit rating is below A-	£1m (overnight)	n/a	n/a	n/a	n/a
Between AA- and AAA (fixed-term duration)	UK financial institutions: Higher of £1m or 5%* (1 year) Non-UK financial institutions: Higher of £1m or 5%* (6 months)	UK financial institutions: Higher of £1m or 5%* (1 year) Non-UK financial institutions: Higher of £1m or 5%* (6 months)	Higher of £1m or 5%* (1 year) Longer exposure - under review	UK financial institutions: Higher of £1m or 5%* (1 year) Non-UK financial institutions: Higher of £1m or 5%* (6 months) Longer exposure - under review	UK financial institutions: Higher of £1m or 5%* (1 year) Non-UK financial institutions: Higher of £1m or 5%* (6 months) Longer exposure - under review

Appendix B (continued)

Credit rating	Banks unsecured	Banks secured	Government	Corporates	Registered Providers
Between A and A+ (fixed term duration)	UK financial institutions: Higher of £1m or 5%* (1 year) Non-UK financial institutions: Higher of £1m or 5%* (3 months)	UK financial institutions: Higher of £1m or 5%* (1 year) Non-UK financial institutions: Higher of £1m or 5%* (3 months)	Higher of £1m or 5%* (1 year) Longer exposure - under review	UK financial institutions: Higher of £1m or 5%* (1 year) Non-UK financial institutions: Higher of £1m or 5%* (3 months) Longer exposure - under review	UK financial institutions: Higher of £1m or 5%* (1 year) Non-UK financial institutions: Higher of £1m or 5%* (3 months) Longer exposure - under review
A- (fixed term duration)	UK financial institutions: Higher of £1m or 5%* (6 months) Non-UK financial institutions: n/a	UK financial institutions: Higher of £1m or 5%* (6 months) Non-UK financial institutions: n/a	Higher of £1m or 5%* (1 year) Longer exposure - under review	UK financial institutions: Higher of £1m or 5%* (6 months) Non-UK financial institutions: n/a Longer exposure - under review	UK financial institutions: Higher of £1m or 5%* (6 months) Non-UK financial institutions: n/a Longer exposure - under review
Between A- and AAA (with same day access to funds e.g. call accounts or notice accounts)	Higher of £1m or 5%* (unlimited)	Higher of £1m or 5%* (unlimited)	Higher of £1m or 5%* (unlimited)	Higher of £1m or 5%* (unlimited)	Higher of £1m or 5%* (unlimited)
No published rating	n/a	n/a	n/a	n/a	n/a
Money market funds	£5m per fund (minimum AAA rated), see paragraph 4.17 of 2019/20 Treasury Management Strategy for further details				
Other pooled funds (including estates trusts, property funds and equity shares)	Under review (no investments permitted in these funds at the current time, see paragraph 4.14 of the Treasury Management Strategy for further details)				

External Context

Economic background:

UK Consumer Price Inflation (CPIH) fell to 1.7% year/year in August 2019 from 2.0% in July, weaker than the consensus forecast of 1.9% and below the Bank of England's target. The most recent labour market data for the three months to July 2019 showed the unemployment rate edged back down to 3.8% while the employment rate remained at 76.1%, the joint highest since records began in 1971. Nominal annual wage growth measured by the 3-month average excluding bonuses was 3.8% and 4.0% including bonuses. Adjusting for inflation, real wages were up 1.9% excluding bonuses and 2.1% including.

The Quarterly National Accounts for Q2 GDP confirmed the UK economy contracted by 0.2% following the 0.5% gain in Q1 which was distorted by stockpiling ahead of Brexit. Only the services sector registered an increase in growth, a very modest 0.1%, with both production and construction falling and the former registering its largest drop since Q4 2012. Business investment fell by 0.4% (revised from -0.5% in the first estimate) as Brexit uncertainties impacted on business planning and decision-making.

Politics, both home and abroad, continued to be a big driver of financial markets over the last quarter. Boris Johnson won the Conservative Party leadership contest and has committed to leaving the EU on 31st October regardless of whether a deal is reached with the EU. Mr Johnson prorogued Parliament which led some MPs to put forward a bill requiring him to seek a Brexit extension if no deal is in place by 19th October. The move was successful and, having been approved by the House of Lords, was passed into law. The Supreme Court subsequently ruled Mr Johnson's suspension of Parliament unlawful.

Tensions continued between the US and China with no trade agreement in sight and both countries imposing further tariffs on each other's goods. The US Federal Reserve cut its target Federal Funds rates by 0.25% in September to a range of 1.75% - 2%, a pre-emptive move to maintain economic growth amid escalating concerns over the trade war and a weaker economic environment leading to more pronounced global slowdown. The euro area Purchasing Manager Indices (PMIs) pointed to a deepening slowdown in the Eurozone. These elevated concerns have caused key government yield curves to invert, something seen by many commentators as a predictor of a global recession. Market expectations are for further interest rate cuts from the Fed and in September the European Central Bank reduced its deposit rate to -0.5% and announced the recommencement of quantitative easing from 1st November.

The Bank of England maintained Bank Rate at 0.75% and in its August Inflation Report noted the deterioration in global activity and sentiment and confirmed that monetary policy decisions related to Brexit could be in either direction depending on whether or not a deal is ultimately reached by 31st October.

Appendix C (continued)**Financial markets:**

After rallying early in 2019, financial markets have been adopting a more risk-off approach in the following period as equities saw greater volatility and bonds rallied (prices up, yields down) in a flight to quality and anticipation of more monetary stimulus from central banks. The Dow Jones, FTSE 100 and FTSE 250 are broadly back at the same levels seen in March/April.

Gilt yields remained volatile over the period on the back of ongoing economic and political uncertainty. From a yield of 0.63% at the end of June, the 5-year benchmark gilt yield fell to 0.32% by the end of September. There were falls in the 10-year and 20-year gilts over the same period, with the former dropping from 0.83% to 0.55% and the latter falling from 1.35% to 0.88%. 1-month, 3-month and 12-month LIBID (London Interbank Bid) rates averaged 0.65%, 0.75% and 1.00% respectively over the period.

Recent activity in the bond markets and PWLB interest rates highlight that weaker economic growth remains a global risk. The US yield curve remains inverted with 10-year Treasury yields lower than US 3-month bills. History has shown that a recession hasn't been far behind a yield curve inversion. Following the sale of 10-year Bunds at -0.24% in June, yields on German government securities continue to remain negative in the secondary market with 2 and 5-year securities currently both trading around -0.77%.

Credit background:

Credit Default Swap (CDS) spreads rose and then fell again during the quarter, continuing to remain low in historical terms. After rising to almost 120bps in May, the spread on non-ringfenced bank NatWest Markets plc fell back to around 80bps by the end of September, while for the ringfenced entity, National Westminster Bank plc, the spread remained around 40bps. The other main UK banks, as yet not separated into ringfenced and non-ringfenced from a CDS perspective, traded between 34 and 76bps at the end of the period.

There were minimal credit rating changes during the period. Moody's upgraded The Co-operative Bank's long-term rating to B3 and Fitch upgraded Clydesdale Bank and Virgin Money to A-.

Outlook for the remainder of 2019/20:

The global economy is entering a period of slower growth in response to political issues, primarily the trade policy stance of the US. The UK economy has displayed a marked slowdown in growth due to both Brexit uncertainty and the downturn in global activity. In response, global and UK interest rate expectations have eased dramatically.

There appears no near-term resolution to the trade dispute between China and the US, a dispute that the US appears comfortable exacerbating further. With the 2020 presidential election a year away, Donald Trump is unlikely to change his stance.

Appendix C (continued)

Parliament appears to have frustrated UK Prime Minister Boris Johnson's desire to exit the EU on 31st October. The probability of a no-deal EU exit in the immediate term has decreased, although a no-deal Brexit cannot be entirely ruled out for 2019 and the risk of this event remains for 2020. The risk of a general election in the near term has, however, increased.

Central bank actions and geopolitical risks will continue to produce significant volatility in financial markets, including bond markets.

Our treasury advisor Arlingclose expects Bank Rate to remain at 0.75% for the foreseeable future but there remain substantial risks to this forecast, dependant on Brexit outcomes and the evolution of the global economy. Arlingclose also expects gilt yields to remain at low levels for the foreseeable future and judge the risks to be weighted to the downside and that volatility will continue to offer longer-term borrowing opportunities

	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22
Official Bank Rate													
Upside risk	0.00	0.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
Arlingclose Central Cas	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75
Downside risk	0.50	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75