

Shropshire County Council  
Monthly Investment Analysis Review  
June 2016



## Shropshire County Council

### Monthly Economic Summary

#### General Economy

During some of the most dramatic days in UK politics of post-war history, the shock of Britain's vote to leave the European Union, followed by the Prime Minister's announcement that he will step down by October, saw financial markets experience material levels of volatility. Bond yields tumbled to record lows in major markets, while equity prices whipsawed and the value of sterling tumbled.

In the lead-up to the much-anticipated EU referendum, markets were firstly seeing the bias in voting polls shift to the "Leave" campaign in the early stages of the month, before the "Remain" vote made a late surge in the days leading up to the vote itself. Such mood swings ensured that, data aside, markets were already skittish for much of the month.

On the data front, the month kicked off with some disappointing Purchasing Managers' Index (PMI) figures. Commencing with manufacturing, activity appeared fairly stagnant in May, only slightly rising to 50.1 last month from April's upwardly revised 49.4, itself the lowest reading since early 2013. Gloomy news continued through the construction sector, with orders falling for the first time in over three years, following concerns regarding the EU referendum. Financial data company, Markit, said construction's PMI dropped to 51.2, from April's 52. More encouraging was news that activity in the dominant service sector picked up last month to 53.5, from 52.3 the previous month. However, details of the report indicated that respondents were still weighed down by the build up to the EU vote.

UK inflation remained wedged near record lows in May as cheaper clothes, food and entertainment offset the effects of rising fuel costs. Consumer Price Inflation (CPI) elevated 0.3% over the year, unchanged from April's figure. Core inflation, which strips out the most volatile goods, was also steady at 1.2% in May. Following Britain's vote to leave the European Union, pressure was immediately heaped on the value of Sterling, causing it to plummet. While beneficial to our exporters, analysts suggested that this is likely to cause inflation to increase over the coming months faster than originally anticipated as our cost of goods increases.

Slightly more buoyant data followed for the UK, by way of the unemployment rate falling to its lowest level in 11 years, as EU referendum fears and the introduction of the National Minimum Wage failed to hold back UK firms. Reaching a low of 5% in the three months to April, this marked the lowest the unemployment rate has stood at since the autumn of 2005, and is now in line with the Bank of England's estimates of full employment. In contrast to inflation running around the 0.3% mark, real wage growth came in at around 1.7%, one of the strongest levels since the onset of the financial crisis.

Further afield, US non-farm payrolls crumbled in May, with the economy adding just 38,000 positions through the month, the lowest figure in six years, and far below market expectations of 160,000. When adjusted for the striking Verizon workers, payrolls still only stood at 73,000, suggesting any speculation of a near-term hike should be put to bed. The unemployment rate did drop to a nine-year low of 4.7%; however this was mainly a result of people leaving the workforce. This feeble news and its implications for rate prospects caused the Dollar to plummet 1.25% against the Euro. On a slightly more upbeat note, GDP in the US economy was revised up on the back of strong exports and investment numbers. The rate was pushed up to 1.1% on an annualised basis in the first quarter of the year, up from the previous reading of 0.8% reported last month. In normal circumstances, higher growth would have put the spotlight back on the Federal Reserve over the timing of the next rate hike; however following the weak payrolls data print and the UK's vote to leave the EU, markets have almost discounted any expectation of interest rates being raised before the end of the year.

Following polls signalling a victory for "Remain" in the lead up to the Referendum day, Sterling climbed to \$1.50 amid optimism over the result, however soon lost ground and dropped sharply to \$1.34 as markets were wrong-footed after UK voters defied polls to leave the European Union in a historic referendum. The final result gave the "Leave" campaign a lead by 52%, while "Remain" took 48%. On the political side of things, shortly after the results were announced, Prime Minister David Cameron took to the stage to declare he would step down by October. This almost immediate declaration was not necessarily a surprise, but did come somewhat sooner than many had expected. With a decision to be made on the scheduling of Article 50 of the Lisbon Treaty, the timing of the UK's eventual exit from the European Union remains up in the air. However, this did not stop the main credit ratings agencies, Moody's, Fitch, and S&P, from acting on the UK sovereign rating. Two out of the three cut the rating, while one, Moody's lowered the Outlook, as well as those for a number of UK financial entities, on heightened uncertainty and the potential for weaker economic prospects that Brexit may entail.

Adding to Brexit uncertainty is the UK's current account deficit, which continues to run at a near record high. The deficit came in at £32.6bn in Q1, equating to 6.9% of GDP, the second largest figure for any quarter on record. Alongside this release, figures revealed that growth in the first quarter of the year slowed to 0.4%. This updated figure was a drop from an upwardly revised 0.7% in the last quarter of 2015. Downward revisions to growth during the start of 2015 have led to annual growth unrevised at 2% for Q1. Looking ahead, market participants and analysts alike believe that the decision to leave the EU is likely to hinder growth for at least the remainder of this year.

In a further effort to calm market concerns, Bank of England's Mark Carney spoke out on the last day of the month. He reaffirmed that the Bank would do all that was necessary to support the economy in this uncertain time, hinting at the likelihood of an interest rate cut and an increase in quantitative easing. The prospect of rates being cut from their historic low of 0.5% sent the Pound tumbling once more; however stock markets in the UK and beyond rebounded from the weakness seen in the immediate aftermath of the Brexit result.

### Housing

Nationwide figures revealed that British house price growth was unchanged in June, rising at 0.2% on the month. However, house price acceleration on an annual basis sped up to 5.1% from 4.7% in May. Halifax reported houses prices rose 0.6% in May, following a 0.8% dip the previous month. On an annual basis, house prices grew 9.2%.

### Forecast

Capita Asset Services did not alter its forecast this month. Capita Asset Services expects the first rate hike to come in the first quarter of 2017. Capital Economics left their forecast unchanged in May. They expect the first Bank Rate increase to come in Q4 2016.

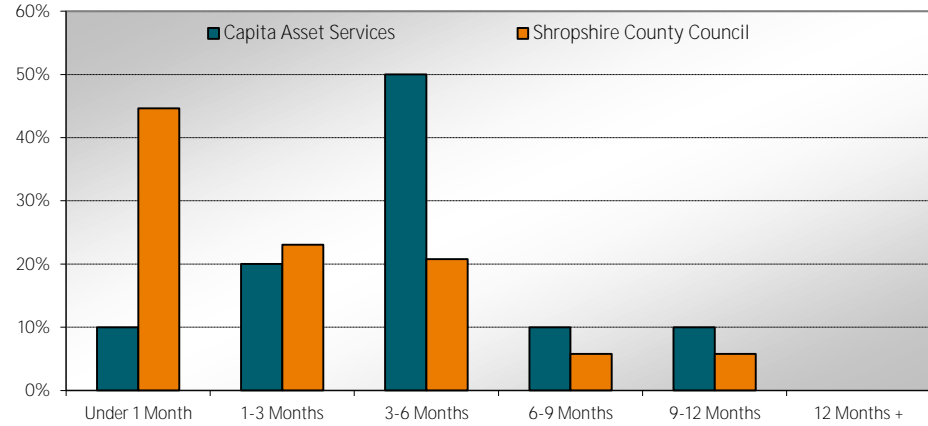
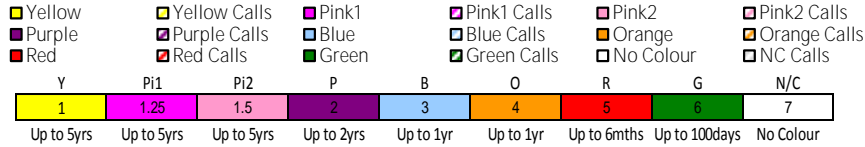
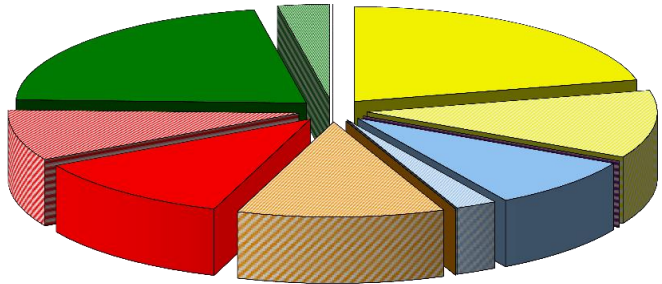
Bank Rate	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17
Capita Asset Services	0.50%	0.50%	0.75%	0.75%	1.00%
Capital Economics	0.50%	0.75%	0.75%	1.00%	1.00%

## Shropshire County Council

### Current Investment List

Borrower	Principal (£)	Interest Rate	Start Date	Maturity Date	Lowest Long Term Rating	Historic Risk of Default
HSBC Bank Plc	20,000,000	0.80%		Call	AA-	0.000%
National Westminster Bank Plc	4,000,000	0.25%		Call	BBB+	0.000%
MMF Standard Life	10,000,000	0.50%		MMF	AAA	0.000%
MMF Insight	10,000,000	0.50%		MMF	AAA	0.000%
Lloyds Bank Plc	3,260,000	0.57%	31/03/2016	01/07/2016	A	0.000%
Lloyds Bank Plc	1,520,000	0.75%	04/01/2016	04/07/2016	A	0.001%
Lloyds Bank Plc	5,000,000	0.57%	07/04/2016	05/07/2016	A	0.001%
Barclays Bank Plc	1,750,000	0.48%	06/04/2016	06/07/2016	A-	0.001%
Lloyds Bank Plc	4,320,000	0.75%	07/01/2016	07/07/2016	A	0.001%
Lloyds Bank Plc	3,600,000	0.75%	08/01/2016	08/07/2016	A	0.001%
Leeds Building Society	2,000,000	0.63%	11/01/2016	11/07/2016	A-	0.002%
Lloyds Bank Plc	5,000,000	0.57%	14/04/2016	14/07/2016	A	0.002%
National Westminster Bank Plc	5,000,000	0.92%	22/07/2015	21/07/2016	BBB+	0.009%
Mid Suffolk District Council	2,000,000	0.45%	21/04/2016	21/07/2016	AA	0.000%
Nationwide Building Society	2,900,000	0.71%	04/02/2016	04/08/2016	A	0.006%
Barclays Bank Plc	5,000,000	0.56%		Call35	A-	0.006%
Barclays Bank Plc	3,250,000	0.69%	05/02/2016	05/08/2016	A-	0.006%
Lloyds Bank Plc	1,400,000	0.65%	11/05/2016	11/08/2016	A	0.007%
Coventry Building Society	5,000,000	0.60%	16/02/2016	16/08/2016	A	0.008%
Middlesborough Council	5,000,000	0.48%	16/05/2016	16/08/2016	AA	0.001%
Eastleigh Borough Council	2,000,000	0.57%	22/02/2016	22/08/2016	AA	0.001%
Leeds Building Society	2,000,000	0.67%	14/03/2016	14/09/2016	A-	0.013%
Reading Borough Council	5,000,000	0.50%	15/06/2016	15/09/2016	AA	0.001%
Barclays Bank Plc	5,000,000	0.47%	15/06/2016	15/09/2016	A-	0.013%
Lloyds Bank Plc	2,420,000	0.75%	16/03/2016	16/09/2016	A	0.013%
Leeds Building Society	1,000,000	0.67%	30/03/2016	30/09/2016	A-	0.016%
Telford & Wrekin Council	3,000,000	0.50%	23/06/2016	03/10/2016	AA	0.002%
Santander UK Plc	15,000,000	0.90%		Call95	A	0.016%
Nationwide Building Society	2,100,000	0.71%	12/04/2016	12/10/2016	A	0.018%
Birmingham City Council	10,000,000	0.60%	13/04/2016	13/10/2016	AA	0.002%
Nationwide Building Society	3,000,000	0.66%	20/06/2016	20/12/2016	A	0.029%
Lloyds Bank Plc	900,000	0.80%	21/06/2016	21/12/2016	A	0.030%
Nationwide Building Society	2,000,000	0.66%	22/06/2016	22/12/2016	A	0.030%
Lancashire County Council	10,000,000	0.60%	27/05/2016	27/02/2017	AA	0.004%
National Westminster Bank Plc	10,000,000	0.75%	15/06/2016	14/06/2017	BBB+	0.144%
<b>Total Investments</b>	<b>£173,420,000</b>	<b>0.65%</b>				<b>0.013%</b>

Portfolio Composition by Capita Asset Services' Suggested Lending Criteria



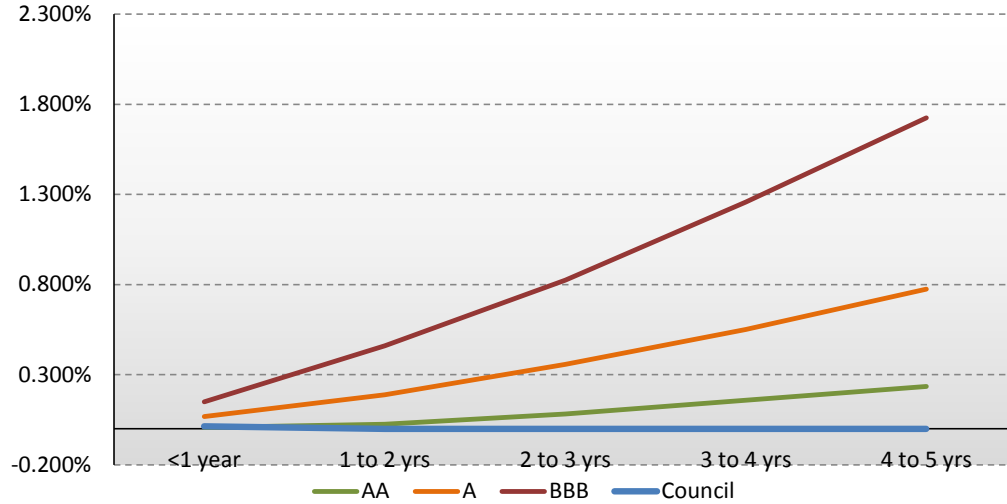
Portfolios weighted average risk number = **3.60**

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/EMMFs	
									WAM	WAM at Execution
Yellow	32.87%	£57,000,000	35.09%	£20,000,000	11.53%	0.53%	79	112	122	172
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	10.96%	£19,000,000	21.05%	£4,000,000	2.31%	0.69%	189	288	240	364
Orange	11.53%	£20,000,000	100.00%	£20,000,000	11.53%	0.80%	0	0	0	0
Red	20.18%	£35,000,000	42.86%	£15,000,000	8.65%	0.76%	89	145	84	183
Green	24.46%	£42,420,000	11.79%	£5,000,000	2.88%	0.62%	30	119	29	130
No Colour	0.00%	£0	0.00%	£0	0.00%	0.00%	0	0	0	0
<b>Total</b>	<b>100.00%</b>	<b>£173,420,000</b>	<b>36.90%</b>	<b>£64,000,000</b>	<b>36.90%</b>	<b>0.65%</b>	<b>72</b>	<b>127</b>	<b>100</b>	<b>186</b>

Investment Risk and Rating Exposure

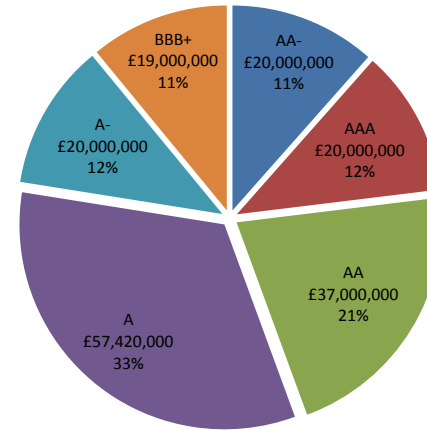
Investment Risk Vs. Rating Categories



Historic Risk of Default

Rating/Years	<1 year	1 to 2 yrs	2 to 3 yrs	3 to 4 yrs	4 to 5 yrs
AA	0.007%	0.024%	0.081%	0.158%	0.234%
A	0.067%	0.189%	0.356%	0.551%	0.775%
BBB	0.150%	0.460%	0.824%	1.257%	1.726%
Council	0.013%	0.000%	0.000%	0.000%	0.000%

Rating Exposure



**Historic Risk of Default**

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

**Chart Relative Risk**

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

**Rating Exposures**

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

## Shropshire County Council

### Monthly Credit Rating Changes

FITCH

Date	Update Number	Institution	Country	Rating Action
15/06/2016	1454	UBS AG	Switzerland	Long Term Rating upgraded to 'A+' from 'A', Outlook changed to 'Stable' from 'Positive'. Short Term Rating affirmed at 'F1'.
15/06/2016	1454	UBS Ltd	Switzerland	Long Term Rating upgraded to 'A+' from 'A', Outlook changed to 'Stable' from 'Positive'. Short Term Rating affirmed at 'F1'.
28/06/2016	1456	UK Sovereign Rating	UK	Sovereign Rating downgraded to 'AA' from 'AA+', Outlook changed to 'Negative' from 'Stable'

## Shropshire County Council

### Monthly Credit Rating Changes MOODY'S

Date	Update Number	Institution	Country	Rating Action
02/06/2016	1449	Norddeutsche Landesbank Girozentrale	Germany	Long Term Rating affirmed at 'A2', removed from 'Negative Outlook' and placed on 'Negative Watch' . Short Term rating affirmed at 'P-1' placed on 'Negative Watch'
06/06/2016	1450	Finland Sovereign Rating	Finland	Sovereign Rating was downgraded to 'Aa1' from 'Aaa', Outlook changed from 'Stable' to 'Negative'
27/06/2016	1455	UK Sovereign Rating	UK	Sovereign Rating was affirmed at 'Aa1', Outlook changed to 'Negative' from 'Stable'
29/06/2016	1459	Coventry Building Society	UK	Long Term Rating affirmed at 'A2', Outlook changed to 'Negative' from 'Stable'. Short Term Rating affirmed at 'P-1'
29/06/2016	1459	Leeds Building Society	UK	Long Term Rating affirmed at 'A2', Outlook changed to 'Negative' from 'Stable'. Short Term Rating affirmed at 'P-1'
29/06/2016	1459	Nationwide Building Society	UK	Long Term Rating affirmed at 'Aa3', Outlook changed to 'Negative' from 'Stable'. Short Term Rating affirmed at 'P-1'
29/06/2016	1459	Nottingham Building Society	UK	Long Term Rating affirmed at 'Baa1', Outlook changed to 'Negative' from 'Stable'. Short Term Rating affirmed at 'P-2'
29/06/2016	1459	Principality Building Society	UK	Long Term Rating affirmed at 'Baa3', Outlook changed to 'Stable' from 'Positive'. Short Term Rating affirmed at 'P-3'.
29/06/2016	1458	Abbey National Treasury Services Plc	UK	Long Term Rating affirmed at 'Aa3', Outlook changed to 'Negative' from 'Stable'. Short Term Rating affirmed at 'P-1'
29/06/2016	1458	Bank of Scotland Plc	UK	Long Term Rating affirmed at 'A1', Outlook changed to 'Stable' from 'Positive'. Short Term Rating affirmed at 'P-1'
29/06/2016	1458	Barclays Bank Plc	UK	Long Term Rating affirmed at 'A2', Outlook changed to 'Negative' from 'Stable'. Short Term Rating affirmed at 'P-1'
29/06/2016	1458	HSBC Bank plc	UK	Long Term Rating affirmed at 'A2', Outlook changed to 'Negative' from 'Stable'. Short Term Rating affirmed at 'P-1'
29/06/2016	1458	Lloyds Bank plc	UK	Long Term Rating affirmed at 'A1', Outlook changed to 'Stable' from 'Positive'. Short Term Rating affirmed at 'P-1'
29/06/2016	1458	Santander UK Plc	UK	Long Term Rating affirmed at 'Aa3', Outlook changed to 'Negative' from 'Stable'. Short Term Rating affirmed at 'P-1'