

Shropshire Council

Monthly Investment Analysis Review

March 2020

Monthly Economic Summary

General Economy

The Flash Manufacturing PMI for March fell to 48.0 from 51.7 in February, pointing to a contraction in the sector, as output dropped at the sharpest pace since 2012 as factories shut down across the world in response to the Covid-19 outbreak. March's Flash Services PMI figure, meanwhile, slumped to a record-low of 35.7 from 53.2 in February. With measures to halt the spread of the Covid-19 causing footfall to slump, hotels, restaurants and gyms recorded particularly steep downturns in activity. As a result, the Flash Composite PMI tumbled to 37.1 in March, signalling the fastest downturn in private sector business activity since the series began in 1998. The Construction PMI, which is now released on a different timescale to the main services and manufacturing reports, rose to 52.6 in February from 48.4 in January, easily beating market expectations of 48.8 – but this survey was taken before the Covid-19 outbreak began to severely impact businesses.

GDP data showed that the UK economy stagnated in January prior to the Covid-19 outbreak, as growth in the service sector was offset by falls in production and construction. Year-on-year GDP growth fell to +0.6% from +1.2% in December and missed market expectations of a 0.9% rise.

The UK's unemployment rate edged up to 3.9% in the three months to January from its lowest level since 1975 and above market expectations of 3.8%. The number of people out of work rose by 63,000 to 1.34 million, which was the biggest increase since 2011, while the number of employed people rose by 184,000 to a record high of 32.99 million. Average earnings including bonuses grew 3.1% in the three months to January, up from 2.9% in the previous period. Excluding bonuses, average earnings also grew 3.1%, a slight fall from 3.2% in December.

Consumer Price Inflation (CPI) fell to 1.7% in February, from 1.8% in the previous month, in line with market expectations and remaining below the Bank of England's 2% target. In monthly terms, CPI increased by 0.4% in February following January's 0.3% fall. The core CPI rate (which strips out the more volatile components), rose to 1.7% y/y in February, up from 1.6% y/y in January.

February's retail sales fell by 0.3% m/m following an upwardly revised 1.1% gain in January. This missed market expectations of a 0.2% m/m rise, with a number of retailers noting that sales were hampered by extreme rainfall. Year-on-year sales stagnated, down from the upwardly revised 0.9% y/y growth recorded in January. March's Confederation of British Industry's monthly retail sales index dropped to -3 from +1 in February, but still beat market expectations of -12. The survey revealed that the Covid-19 outbreak hit demand for most products, with sales of clothing and furniture falling the most in the year to March. The GfK Consumer Confidence index, meanwhile, dropped 2 points to -9 in March, falling for the first time in four months as coronavirus anxiety took its toll.

As evident in the Flash PMI reports noted above, March saw the Covid-19 outbreak significantly impact both the UK and global economy. The FTSE 100 index fell from 7021 to 5645 during the month, evidencing the sharp deterioration in the outlook for business profitability. In response to the deteriorating economic conditions, the Bank of England cut Bank Rate twice during the month - firstly cutting by 50bps to 0.25%, and then again by a further 15bps to a record low of 0.1%. The central bank also

announced that it would resume quantitative easing, buying up to £200 billion of UK government and corporate bonds to improve liquidity in both financial markets and the broader economy. The UK government also announced a range of measures to support the economy including a £330 billion package of loan guarantees for domestic businesses - equivalent to 15% of UK GDP – and a commitment to pay 80% of an employee's salary (capped at £2,500 a month) if they are unable to work during the coronavirus crisis and are furloughed by their employer.

Although Q4 2019 US GDP growth was confirmed at 2.1%, this is expected to fall dramatically in Q1 and Q2 as the impact of Covid-19 sweeps through the US economy. One sign of what could be to come was the extraordinary jump in the number of people filing for unemployment benefits to 3.283 million from 282,000 previously as businesses were ordered to shut. In response, the US Fed cut official policy rates twice during the month – firstly from 1.75% to 1.25% and then again to just 0.25%. It also resumed quantitative easing, committing to buy at least \$700 billion of bonds to support the financial system and the US economy. The US Government also passed a \$2 trillion coronavirus relief package designed to help the US weather the outbreak.

Although Eurozone economic growth was confirmed at 0.1%/q in Q4 of 2019, easing from an upwardly revised 0.3% expansion in Q3, the fall in March's Composite PMI to an all-time low of 31.4 from 51.6 in February suggests that growth looks set to fall appreciably, as elsewhere. In response, the ECB announced they would expand their existing quantitative easing programme by purchasing up to €750 billion of securities to help counter the risks posed to the Eurozone by the Covid-19 outbreak.

Housing

Halifax reported that house prices in the UK rose by 2.8% y/y in February, well below both the 4.1% gain reported in January and market expectations of 4%. On a monthly basis, house prices increased by 0.3%, easing from the 0.4% gain posted in January, but higher than the consensus forecast of a 0.2% rise.

Currency

Safe haven buying of other currencies (especially the dollar) in the wake of the coronavirus outbreak and the oil price war saw Sterling fall significantly last month against both the US Dollar and the Euro.

February	Start	End	High	Low
GBP/USD	\$1.2933	\$1.1872	\$1.3142	\$1.1541
GBP/EUR	€1.1817	€1.0809	€1.1817	€1.0611

Forecast

Following the coronavirus outbreak, both LAS and Capital Economics have revised their interest rate forecasts - and now forecast that the base rate will remain unchanged at 0.1% throughout 2020 and 2021.

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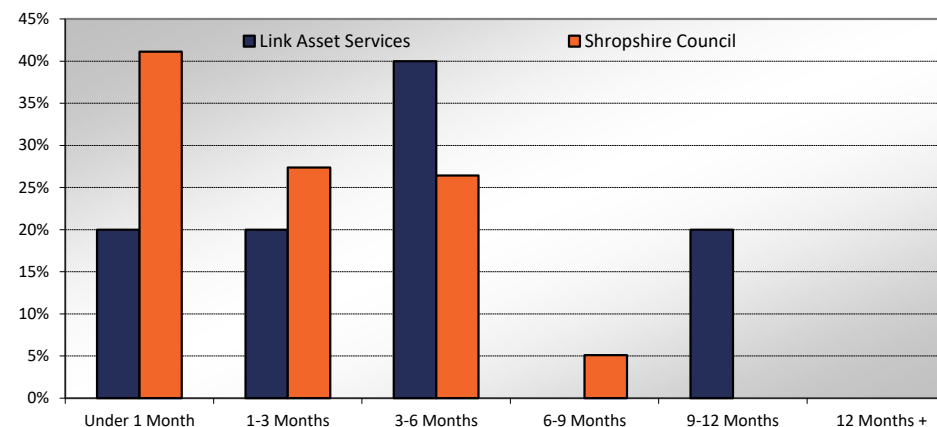
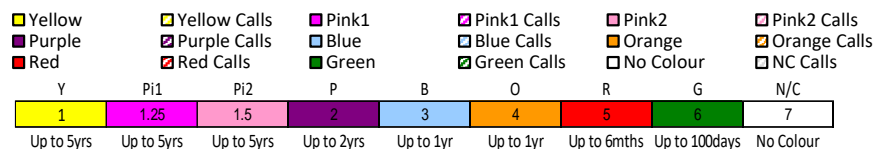
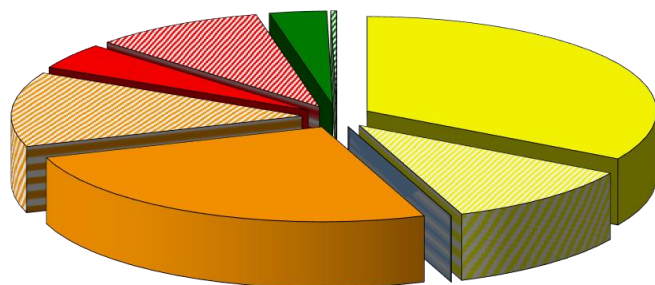
Current Investment List

Borrower	Principal (£)	Interest Rate	Start Date	Maturity Date	Lowest Long Term Rating	Historic Risk of Default	Expected Credit Loss (£)
MMF Insight	3,900,000	0.51%		MMF	AAA	0.000%	4
MMF Aberdeen Standard Investments	13,160,000	0.46%		MMF	AAA	0.000%	14
Barclays Bank Plc (NRFB)	500,000	0.82%		Call	A	0.000%	1
Santander UK Plc	15,000,000	0.85%		Call	A	0.000%	20
Handelsbanken Plc	20,000,000	0.53%		Call	AA-	0.000%	13
Nationwide Building Society	2,000,000	0.72%	15/10/2019	14/04/2020	A	0.002%	37
Rugby Borough Council	5,000,000	0.90%	25/02/2020	17/04/2020	AA-	0.001%	0
East Dunbartonshire Council	5,000,000	0.90%	24/02/2020	24/04/2020	AA-	0.002%	0
Plymouth City Council	5,000,000	0.80%	03/02/2020	04/05/2020	AA-	0.002%	0
Lloyds Bank Plc (RFB)	5,000,000	1.25%	05/06/2019	05/06/2020	A+	0.009%	438
Goldman Sachs International Bank	5,000,000	0.93%	06/12/2019	05/06/2020	A	0.009%	438
Blaenau Gwent County Borough Council	3,000,000	0.84%	06/12/2019	08/06/2020	AA-	0.004%	0
Flintshire County Council	5,000,000	1.30%	13/03/2020	12/06/2020	AA-	0.005%	0
HSBC UK Bank Plc (RFB)	20,000,000	1.13%	25/06/2019	25/06/2020	A+	0.011%	2285
Nationwide Building Society	5,000,000	0.79%	08/01/2020	08/07/2020	A	0.013%	657
Lloyds Bank Plc (RFB)	5,000,000	1.25%	12/07/2019	10/07/2020	A+	0.013%	671
Thurrock Borough Council	5,000,000	0.92%	12/08/2019	10/07/2020	AA-	0.007%	0
Lloyds Bank Plc (RFB)	5,000,000	1.25%	15/07/2019	13/07/2020	A+	0.014%	691
Blaenau Gwent County Borough Council	1,500,000	0.90%	21/01/2020	21/07/2020	AA-	0.007%	0
Lloyds Bank Plc (RFB)	5,000,000	1.25%	25/07/2019	24/07/2020	A+	0.015%	764
Calderdale Metropolitan Borough Council	2,000,000	1.00%	14/02/2020	17/08/2020	AA-	0.009%	0
Surrey Heath Borough Council	4,000,000	0.90%	17/02/2020	17/08/2020	AA-	0.009%	0
Kingston Upon Hull City Council	4,000,000	0.93%	25/02/2020	25/08/2020	AA-	0.010%	0
falkirk Council	5,000,000	1.00%	02/03/2020	02/09/2020	AA-	0.010%	0
Plymouth City Council	5,000,000	0.97%	14/02/2020	14/10/2020	AA-	0.013%	0
North Tyneside Metropolitan Borough Council	3,000,000	0.95%	25/11/2019	23/11/2020	AA-	0.015%	0
Total Investments	£157,060,000	0.89%					£6,033

The Historic Risk of Default column is based on the lowest long term rating. If clients are using this % for their Expected Credit Loss calculation under IFRS 9, please be aware that the Code does not recognise a loss allowance where the counterparty is central government or a local authority since relevant statutory provisions prevent default. For these instruments, the Expected Credit Loss will be nil. Please note that we are currently using Historic Default Rates from 1990-2019 for Fitch, 1983-2019 for Moody's and 1981-2019 for S&P.

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Portfolio Composition by Link Asset Services' Suggested Lending Criteria



Portfolios weighted average risk number = **2.88**

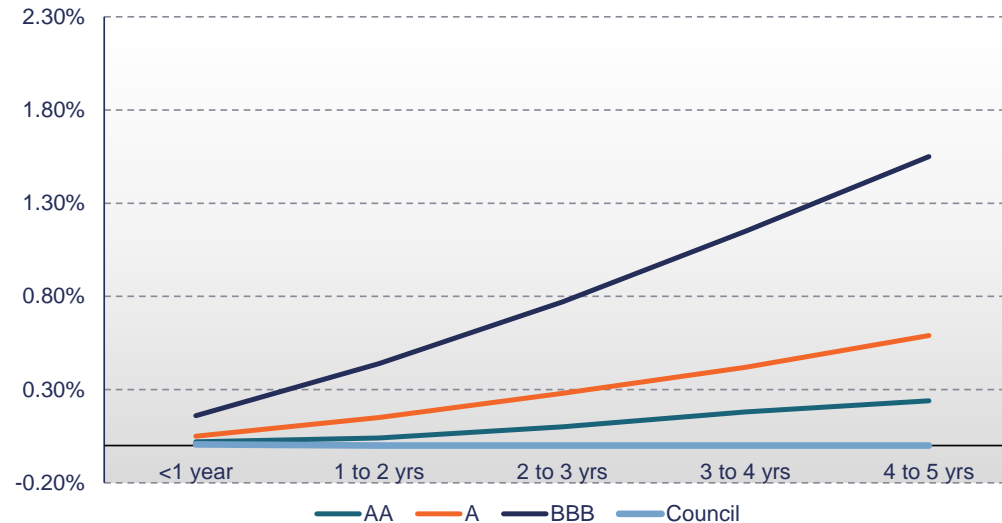
WARoR = Weighted Average Rate of Return
WAM = Weighted Average Time to Maturity

	% of Portfolio	Amount	% of Colour in Calls	Amount of Colour in Calls	% of Call in Portfolio	WARoR	WAM	WAM at Execution	Excluding Calls/MMFs/USDBFs	
									WAM	WAM at Execution
Yellow	44.29%	£69,560,000	24.53%	£17,060,000	10.86%	0.83%	79	130	105	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	0.00%	£0	0.00%	£0	0.00%	0.00%	0	0	0	0
Orange	38.20%	£60,000,000	33.33%	£20,000,000	12.73%	0.97%	61	244	91	365
Red	14.01%	£22,000,000	68.18%	£15,000,000	9.55%	0.82%	24	58	75	182
Green	3.50%	£5,500,000	9.09%	£500,000	0.32%	0.92%	60	165	66	182
No Colour	0.00%	£0	0.00%	£0	0.00%	0.00%	0	0	0	0
Total	100.00%	£157,060,000	33.46%	£52,560,000	33.46%	0.89%	64	164	96	247

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Investment Risk and Rating Exposure

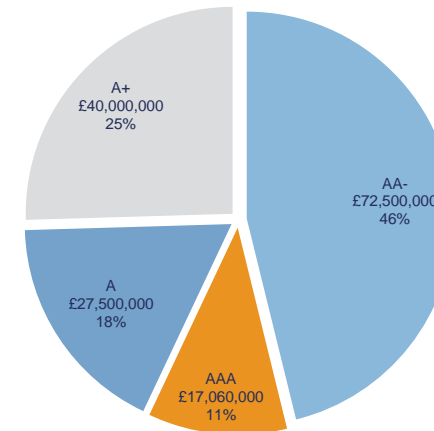
Investment Risk Vs. Rating Categories



Historic Risk of Default

Rating/Years	<1 year	1 to 2 yrs	2 to 3 yrs	3 to 4 yrs	4 to 5 yrs
AA	0.02%	0.04%	0.10%	0.18%	0.24%
A	0.05%	0.15%	0.28%	0.42%	0.59%
BBB	0.16%	0.44%	0.77%	1.15%	1.55%
Council	0.006%	0.000%	0.000%	0.000%	0.000%

Rating Exposure



Historic Risk of Default

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

Chart Relative Risk

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

Rating Exposures

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

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Monthly Credit Rating Changes FITCH

Date	Update Number	Institution	Country	Rating Action
30/03/2020	1724	United Kingdom Sovereign Rating	United Kingdom	The Sovereign Rating was downgraded to 'AA-' from 'AA'.
30/03/2020	1725	Deutsche Bank AG	Germany	The Outlook on the Long Term Rating was removed from Evolving Outlook and placed on Negative Watch.
30/03/2020	1725	Landesbank Hessen-Thuringen Girozentrale	Germany	The Outlook on the Long Term Rating was changed to Negative from Stable.
30/03/2020	1725	Commerzbank AG	Germany	The Long Term Rating was downgraded to 'BBB' from 'BBB+'. The Short Term Rating was downgraded to 'F2' from 'F1' and the Viability Rating was downgraded to bbb from bbb+.
30/03/2020	1726	DZ BANK AG Deutsche Zentral-Genossenschaftsbank	Germany	The Outlook on the Long Term Rating was changed to Negative from Stable.
31/03/2020	1727	BNP Paribas	France	The Outlook on Long Term Rating was removed from Stable Outlook. The Long Term and Viability Ratings were placed on Negative Watch.
31/03/2020	1727	Credit Agricole Corporate and Investment Bank	France	The Outlook on the Long Term Rating was changed to Negative from Stable.
31/03/2020	1727	Credit Agricole S.A.	France	The Outlook on the Long Term Rating was changed to Negative from Stable.
31/03/2020	1727	Credit Industriel et Commercial	France	The Outlook on the Long Term Rating was changed to Negative from Stable.
31/03/2020	1727	Societe Generale	France	The Outlook on Long Term Rating was removed from Stable Outlook. The Long Term and Viability Ratings were placed on Negative Watch.
31/03/2020	1728	KBC Bank N.V.	Belgium	The Outlook the Long Term Rating was changed to Negative from Stable.
31/03/2020	1729	Credit Suisse AG	Switzerland	The Outlook on the Long Term Rating was changed to Negative from Positive.

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Monthly Credit Rating Changes FITCH

Date	Update Number	Institution	Country	Rating Action
31/03/2020	1729	UBS AG	Switzerland	The Outlook on the Long Term Rating was changed to Negative from Stable.
31/03/2020	1730	Nordea Bank Abp	Finland	The Outlook on the Long Term Rating was removed from Stable Outlook and placed on Negative Watch. The Short Term and Viability Ratings were also placed on Negative Watch.
31/03/2020	1730	Handelsbanken Plc	United Kingdom	The Outlook on the Long Term Rating was removed from Stable Outlook and placed on Negative Watch.
31/03/2020	1730	Svenska Handelsbanken AB	Sweden	The Outlook on the Long Term Rating was removed from Stable Outlook. The Long Term and Viability Rating were placed on Negative Watch.
31/03/2020	1730	Skandinaviska Enskilda Banken AB	Sweden	The Outlook on the Long Term Rating was removed from Stable Outlook placed on Negative Watch. The bank's Short Term and Viability Ratings were also placed on Negative Watch.
31/03/2020	1730	Danske A/S	Denmark	The Outlook on the Long Term Rating was removed from Negative Outlook and placed on Negative Watch. The bank's Viability Rating was also placed on Negative Watch.
31/03/2020	1731	Bank of Scotland Plc (RFB)	United Kingdom	The Outlook on the Long Term Rating was changed to Negative from Stable.
31/03/2020	1731	Lloyds Bank Corporate Markets Plc (NRFB)	United Kingdom	The Long Term Rating was upgraded to 'A+' from 'A' and the Outlook on the Long Term Rating was changed to Negative from Stable.
31/03/2020	1731	Lloyds Bank Plc (RFB)	United Kingdom	The Outlook on the Long Term Rating was changed to Negative from Stable.

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Monthly Credit Rating Changes MOODY'S

Date	Update Number	Institution	Country	Rating Action
				No Rating Changes to Report.

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Monthly Credit Rating Changes S&P

Date	Update Number	Institution	Country	Rating Action
27/03/2020	1723	Swedbank AB	Sweden	The Long Term Rating was downgraded to 'A+' from 'AA-' and the Short Term Rating was downgraded to 'A-1' from 'A-1+'. The Outlook on the Long Term Rating was changed to Stable from Negative.

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