APPENDIX C

Risk Environment 2018/19	
Credit Background	**Local Context**
Credit Default Swap (CDS) spreads drifted up towards the end of 2018 on the back of Brexit uncertainty before declining again in 2019 and continuing to remain low in historical terms. After hitting around 129 basis points in December 2018, the spread on non-ring-fenced bank NatWest Markets plc fell back to around 96bps at the end of March, while for the ring-fenced entity, National Westminster Bank plc, the CDS spread held relatively steady around 40bps. The other main UK banks, as yet not separated into ring-fenced and non-ring-fenced from a CDS perspective, traded between 33 and 79bps at the end of the period. The ring-fencing of the big four UK banks (Barclays, Bank of Scotland/Lloyds, HSBC and RBS/Natwest Bank plc) transferred their business lines into retail (ring-fenced) and investment banking (non-ring-fenced) entities.	The Council receives monthly updates from its advisors on changes to credit ratings. Whilst the Council maintains deposits on a short-term or available on an instant basis the risk is reduced from failures, as the Council will be able to withdraw funds as soon as there is an indication of a credit problem. The CDS spreads declining indicates that the financial market feels that the overall credit risk (of failure) has reduced.
Equities	**Local Context**
December was a month to forget in terms of performance of riskier asset classes, most notably equities. The FTSE 100 (a good indicator of global corporate sentiment) returned -8.8% assuming dividends were reinvested; in pure price terms it fell around 13%. However, since the beginning of 2019 markets have rallied, and the FTSE 100 and FTSE All share indices were both around 10% higher than at the end of 2018.	Whilst the Council is not directly investing in equities, the upturn on the FTSE 100 is likely to have a positive impact on the financial returns available on investments and economic growth. As long as the FTSE growth continues into the medium term.
Gilt Yields	**Local Context**
Gilt yields continued to display significant volatility over the period on the back of ongoing economic and political uncertainty in the UK and Europe. After rising in October, gilts regained their safe-haven status throughout December and into the new year - the 5-year benchmark gilt yield fell as low as 0.80% and there were similar falls in the 10-year and 20-year	Gilt yield are used by HM Treasury to set PWLB lending rates. While the Gilt rates remain low, borrowing for the CIS or the general capital programme will remain affordable.

gilts over the same period dropping from 1.73% to 1.08% and from 1.90% to 1.55%. The increase in Bank Rate pushed up money markets rates over the year and 1-month, 3-month and 12-month LIBID (London Interbank Bid) rates averaged 0.53%, 0.67% and 0.94% respectively over the period.	
Global Credit Background	
Recent activity in the bond markets and PWLB interest rates highlight that weaker economic growth is not just a UK phenomenon but a global risk. During March the US yield curve inverted (10-year Treasury yields were lower than US 3 month money market rates) and German 10-year Bund yields turned negative. The drivers are a significant shift in global economic growth prospects and subsequent official interest rate expectations given its impact on inflation expectations. Further to this is world trade growth which collapsed at the end of 2018 falling by 1.8% year-on-year. A large proportion of this downturn in trade can be ascribed to the ongoing trade tensions between the US and China which despite some moderation in January does suggest that the International Monetary Fund's (IMF) and Organisation for Economic Co-Operation & Development's (OECD) forecasts for global growth in 2019 of 3.5% might need to be revised downwards.	Indicators for the economy (inflation, wages, growth) are reasonable. Indicators for the credit environment (interest rates, CDS, Gilt Rates) are stable. But any change in the global economy as a result of the risk and shifts indicated could have a significant impact on the UK credit and economic environment which seems to be finely poised.