

To: POLICY & RESOURCES (FINANCE) SUB-COMMITTEE		Subject: INVESTMENT CRITERIA RATINGS
From: DIRECTOR OF FINANCE		
Date: 10 January 2006	Ref: JV/KMH	

1. INTRODUCTION

- 1.1. The purpose of this report is to inform Committee of the criteria that the Council will refer to when selecting financial institutions for investment purposes.
- 1.2. Members approved the Annual Treasury Strategy for 2005/06 on 22 March 2005, which included details of the Council's investment strategy and the pre-determined list of financial institutions used when investing surplus cash funds, pending receipt of revised Investment Guidance from the Scottish Executive.
- 1.3. Although the Council's list of institutions, or Counterparty List as it is commonly known, has assisted the Council in making effective investment decisions, it has become evident that it is in need of revision to allow the flexibility required to maximise the use of surplus cash funds.

2. CREATION OF CREDIT CRITERIA LIST

- 2.1. The Council's Counterparty List was primarily a list of financial institutions that the Council deemed appropriate to lend funds to. Although the list was in accordance with the credit ratings provided by Fitch, Moody's and Standard & Poors (the world's foremost providers of independent credit ratings), it does not contain time limits for lending, and excluded a number of high quality financial institutions.
- 2.2. With the Counterparty List becoming too static to meet the Council's investment needs, the department in conjunction with its Treasury advisors Butlers have revised the list. This establishes a more flexible based approach in investment decision making, in terms of time limits and the expansion of the number of institutions used for this purpose.
- 2.3. The revised criteria-based list, as detailed in Appendix 1, improves the Council's flexibility for making prudent investment decisions. This list highlights those institutions i) currently in use ii) proposed new institutions meeting the revised criteria and iii) institutions now deleted that no longer meet the criteria.
- 2.4. In addition to detailing maximum time limits for investments, and therefore maximising security and liquidity, the revised list maximises the number of institutions in which the Council can invest surplus funds.

- 2.5. Previously, some overseas institutions e.g. Fortis Bank and Societe Generale (SG) had lower lending limits applied to them simply because they were outwith the UK. This often reduced the Council's flexibility when making investment decisions since its capacity to invest funds in overseas institutions was restricted. However, the introduction of the criteria-based list and an internationally comparable set of rating criteria result in all institutions now being viewed consistently, regardless of their country of origin.
- 2.6. Paragraph 2.1 makes reference to the fact that Fitch, Moody's and Standard & Poors are generally accepted as being the world's foremost providers of independent credit ratings. The ratings provided by these bodies define the likelihood of an investor receiving their money back on the terms in which it was invested. Given that the Council must always take a prudent approach towards its investments, the Council's criteria-based counterparty list has been formed on the basis of Fitch, Moody's and Standard & Poors (S&P) credit rating definitions.
- 2.7. By way of illustration, an institution with S&P short-term rating of A-1 (e.g. Abbey National plc) is deemed to have ***an extremely strong capacity to meet its financial commitments***. Given that such institutions have exceptionally strong credit quality and capacity for timely repayment of funds, maximum limits of 364 days and £15 million are applied because there is very little risk involved to the Council regarding such investments.

3. RECOMMENDATIONS

- 3.1. Committee is requested to note the contents of the report and endorse the introduction of the criteria-based counterparty list, as detailed in Appendix 1.
- 3.2. To note that a further report regarding the counterparty list may be brought to Committee during 2006/07 following the release of the Scottish Executive's Investment Guidance.



Director of Finance

LIST OF APPROVED COUNTERPARTIES FOR LENDING

	<u>Fitch Ratings</u>				<u>Moody's Ratings</u>			<u>S and P</u>		<u>Limits</u>		<u>Status</u>
	<u>S.Term</u>	<u>L.Term</u>	<u>Indiv</u>	<u>Suprt</u>	<u>S.Term</u>	<u>L.Term</u>	<u>Fin Stgth</u>	<u>S.Term</u>	<u>L.Term</u>	<u>Time</u>	<u>Money</u>	
<u>UK BANKS</u>												
<u>ABBEY NATIONAL GROUP</u>												
Abbey National Plc	F1+	AA-	B	2	P - 1	Aa3	B	A-1	A+	364 days	15	Current
<u>ALLIANCE & LEICESTER GROUP</u>												
Alliance & Leicester	F1+	AA-	B	3	P - 1	Aa3	B	A-1	A+	364 days	15	Current
<u>BANK OF IRELAND</u>												
Bristol and West Plc	F1+	AA-	B	1	P - 1	Aa3	C +	A-1	-	364 days	15	New
<u>CITIGROUP</u>												
Citibank International Bank	F1+	AA+	NR	1	P - 1	Aa1	B -	A-1+	AA	364 days	15	New
<u>HBOS GROUP</u>												
* Bank of Scotland (Ireland)	-	-	-	-	-	-	-	-	-	6 months	5	New
Bank of Scotland Plc	F1+	AA+	A/B	1	P - 1	Aa2	B +	A-1+	AA	364 days	15	New
Halifax Plc	F1+	AA+	A/B	1	P - 1	Aa2	B +	A-1+	AA	364 days	15	New
<u>HSBC GROUP</u>												
HSBC Bank Plc	F1+	AA	A/B	1	P - 1	Aa2	B +	A-1+	AA -	364 days	15	Current
<u>LLOYDS TSB GROUP</u>												
Lloyds TSB Bank	F1+	AA+	A	1	P - 1	Aaa	A	A-1+	AA	364 days	15	Current
<u>NATIONAL AUSTRALIA BANK GROUP</u>												
Clydesdale Bank	-	-	-	-	P - 1	A1	B -	A-1	A +	364 days	10	Current
<u>ROYAL BANK OF SCOTLAND GROUP</u>												
* Adam & Co	-	-	-	-	-	-	-	-	-	6 months	5	Current
National Westminster Bank	F1+	AA+	A/B	1	P - 1	Aa1	A -	A-1+	AA	364 days	15	Current
Royal Bank of Scotland	F1+	AA+	A/B	1	P - 1	Aa1	A -	A-1+	AA	364 days	15	Current
Ulster Bank Ireland Ltd	F1+	AA	-	1	P - 1	Aa2	B	A-1+	AA	364 days	15	Current
Ulster Bank Ltd	F1+	AA	-	1	P - 1	Aa2	B	A-1+	AA	364 days	15	Current

* No Individual Ratings available but Time and Money limits set at appropriate level taking into account status of the parent group

	<u>Fitch Ratings</u>				<u>Moody's Ratings</u>			<u>S and P</u>		<u>Limits</u>		<u>Status</u>
	<u>S.Term</u>	<u>L.Term</u>	<u>Indiv</u>	<u>Suprt</u>	<u>S.Term</u>	<u>L.Term</u>	<u>Fin Stgth</u>	<u>S.Term</u>	<u>L.Term</u>	<u>Time</u>	<u>Money</u>	
<u>OTHER UK BANKS</u>												
Bank of Butterfield (UK) Limited	F1	A-	C	1	P - 2	A3	C	A-2	A -	364 days	10	New
Barclays Bank	F1+	AA+	A/B	1	P - 1	Aa1	A -	A-1+	AA	364 days	15	Current
Bradford & Bingley	F1	A	B	3	P - 1	A1	B -	A-2	-	364 days	10	Current
Co-Operative Bank Plc	F1	A	B	3	P - 1	A3	C	-	-	364 days	10	Current
Egg Banking Plc	F1	A+	C	1	P - 2	A3	D +	-	-	364 days	10	New
Lehman Brothers Holdings Plc	F1+	A+	B	1	-	A1	-	A-1	A+	364 days	10	New
MBNA Europe Bank Ltd	F1+	AA-	A/B	1	-	-	-	-	-	364 days	15	Current
Northern Rock Plc	F1	A+	A/B	3	P - 1	A1	B -	A-1	A	364 days	10	Current
Schroders Plc	F1	A+	B	5	-	-	-	A-1	A	364 days	10	New
Standard Life Bank Ltd	-	-	-	-	P - 1	A2	D +	A-2	A -	364 days	10	Deleted
<u>UK BUILDING SOCIETIES</u>												
Nationwide Building Society	F1+	AA-	A/B	2	P - 1	Aa3	B	A-1	A+	364 days	15	Current
Britannia Building Society	F1	A+	B	3	P - 1	A2	C +	A-1	A	364 days	10	Current
Portman Building Society	F1	A	B	3	P - 1	A2	C +	-	-	364 days	10	Current
Yorkshire Building Society	F1	A+	B	3	P - 1	A2	C +	A-1	A	364 days	10	Current
Coventry Building Society	F1	A	B	3	P - 1	A2	C +	-	-	364 days	10	Current
Chelsea Building Society	F1	A	B	3	P - 1	A3	C	-	-	364 days	10	Current
Skipton Building Society	F1	A	B	3	P - 1	A3	C	-	-	364 days	10	Current
Leeds & Holbeck Building Society	-	-	-	3	P - 1	A3	C	-	-	364 days	10	Current
West Bromwich Building Society	F1	A	B	3	P - 1	A3	C	-	-	364 days	10	New
Derbyshire Building Society	-	-	-	3	P - 1	A3	C	-	-	364 days	10	Current
Cheshire Building Society	-	-	-	3	P - 1	A3	C	-	-	364 days	10	Current
Principality Building Society	F1	A	B	3	P - 1	A2	C +	-	-	364 days	10	Current
Newcastle Building Society	F1	A	B	3	P - 1	A3	C	A-2	BBB+	364 days	10	Current
Norwich & Peterborough Building Society	-	-	-	3	P - 1	A3	C	-	-	364 days	10	Current
Dunfermline Building Society	-	-	-	-	P - 1	A3	C	-	-	364 days	10	Current
<u>OVERSEAS BUILDING SOCIETIES</u>												
<u>Ireland</u>												
EBS Building Society	-	-	-	-	P - 1	A2	C +	-	-	364 days	10	New

	<u>Fitch Ratings</u>				<u>Moody's Ratings</u>			<u>S and P</u>		<u>Limits</u>		<u>Status</u>
	<u>S.Term</u>	<u>L.Term</u>	<u>Indiv</u>	<u>Suprt</u>	<u>S.Term</u>	<u>L.Term</u>	<u>Fin Stgth</u>	<u>S.Term</u>	<u>L.Term</u>	<u>Time</u>	<u>Money</u>	
<u>OVERSEAS BANKS</u>												
<u>AUSTRALIA</u>												
National Australia Bank	F1+	AA	A/B	2	P-1	Aa3	B	A-1+	AA -	364 days	15	New
Australia & New Zealand Banking Group	F1+	AA-	B	2	P-1	Aa3	B	A-1+	AA -	364 days	15	New
Commonwealth Bank of Australia	F1+	AA	A/B	2	P-1	Aa3	B	A-1+	AA -	364 days	15	New
Westpac Banking Corporation	F1+	AA-	B	2	P-1	Aa3	B	A-1+	AA -	364 days	15	New
<u>BELGIUM</u>												
KBC Bank	F1+	AA-	B	2	P-1	Aa3	B	A-1	A+	364 days	15	Current
Fortis Bank	F1+	AA-	B	1	P-1	Aa3	B	A-1+	AA-	364 days	15	Current
<u>CANADA</u>												
Canadian Imperial Bank of Commerce	F1+	AA-	B	1	P-1	Aa3	B -	A-1	A+	364 days	15	New
Bank of Montreal	F1+	AA-	B	1	P-1	Aa3	B	A-1+	AA -	364 days	15	New
Bank of Nova Scotia	F1+	AA-	B	1	P-1	Aa3	B	A-1+	AA -	364 days	15	New
National Bank of Canada	F1	A+	B	2	P-1	A1	B -	A-1	A	364 days	10	Current
Royal Bank of Canada	F1+	AA	A/B	1	P-1	Aa2	B +	A-1+	AA -	364 days	15	New
Toronto-Dominion Bank	F1+	AA-	B	1	P-1	Aa3	B	A-1	A +	364 days	15	New
<u>DENMARK</u>												
Danske Bank	F1+	AA-	B	1	P-1	Aa1	A -	A-1+	AA -	364 days	15	New
<u>FINLAND</u>												
Nordca Bank Finland	F1+	AA-	B	1	P-1	Aa3	B	A-1+	AA -	364 days	15	New
<u>FRANCE</u>												
Calyon	F1+	AA	NR	1	P-1	Aa2	C	A-1+	AA-	364 days	15	New
Credit Agricole	F1+	AA	B	1	P-1	Aa2	B +	A-1+	AA-	364 days	15	New
BNP Paribas	F1+	AA	A/B	1	P-1	Aa2	B +	A-1+	AA	364 days	15	New
Credit Industriel et Commercial	F1+	AA-	B/C	1	P-1	A1	C	A-1	A +	364 days	15	New
Credit Lyonnais	F1+	AA	B/C	1	P-1	Aa2	B -	A-1+	AA-	364 days	15	New
Dexia Credit Local	F1+	AA+	A/B	1	P-1	Aa2	B +	A-1+	AA	364 days	15	New
Societe Generale (SG)	F1+	AA-	B	1	P-1	Aa2	B +	A-1+	AA-	364 days	15	New

	<u>Fitch Ratings</u>				<u>Moody's Ratings</u>			<u>S and P</u>		<u>Limits</u>		<u>Status</u>
	<u>S.Term</u>	<u>L.Term</u>	<u>Indiv</u>	<u>Suprt</u>	<u>S.Term</u>	<u>L.Term</u>	<u>Fin Stgth</u>	<u>S.Term</u>	<u>L.Term</u>	<u>Time</u>	<u>Money</u>	
<u>OVERSEAS BANKS</u>												
<u>GERMANY</u>												
Bayerische Hypo- und Vereinsbank AG	F1	A	C/D	1	P-1	A2	D+	A-1	A	364 days	10	New
Bayerische Landesbank Girozentrale	F1+	A+	C/D	1	P-1	Aaa	D+	A-1	A	364 days	10	New
Deutsche Bank AG	F1+	AA-	B	1	P-1	Aa3	B-	A-1+	AA-	364 days	15	Current
Dresdner Bank, AG	F1	A	C	1	P-1	A1	C-	A-1	A	364 days	10	Current
HSN Nordbank AG	F1	A	C	1	P-1	A1	C	A-1	A	364 days	10	Current
Landesbank Baden-Wuerttemberg	F1+	A+	B/C	1	P-1	Aaa	B-	A-1	A+	364 days	15	Current
Landesbank Hessen-Thuringen Girozentrale	F1+	A+	-	1	-	Aaa	C	A-1	A	364 days	10	Current
Norddeutsche Landesbank Girozentrale	F1	A	C	1	P-1	Aa2	C-	A-1	A	364 days	10	New
<u>ICELAND</u>												
Landsbanki Islands HF	F1	A	B/C	2	P-1	A2	C	-	-	364 days	10	New
<u>IRELAND</u>												
DEPFA Bank Plc	F1+	AA-	B	3	P-1	Aa3	B-	A-1+	AA-	364 days	15	Current
IIB Bank Limited	F1	A+	B	1	P-1	A1	C	A-1	A	364 days	10	Current
Allied Irish Banks, Plc	F1+	AA-	B	1	P-1	Aa3	B	A-1	A+	364 days	15	Current
Anglo Irish Bank Corporation	F1	A	B	3	P-1	A2	C+	-	-	364 days	10	Current
Bank of Ireland	F1+	AA-	B	1	P-1	Aa3	B	A-1	A+	364 days	15	Current
Irish Permanent Plc	-	-	-	-	P-1	A1	B-	A-1	A+	364 days	10	Current
<u>ITALY</u>												
Banca Monte dei Paschi di Siena	F1	A+	B/C	2	P-1	A1	B-	A-1	A	364 days	10	New
Sanpaolo IMI	F1+	AA-	B	2	P-1	Aa3	B	A-1	A+	364 days	15	New
Unicredito Italiano	F1	A+	B/C	1	P-1	A1	B-	A-1	A+	364 days	10	Current
<u>LUXEMBOURG</u>												
Dexia Banque Internationale a Luxembourg	F1+	AA+	A/B	1	P-1	Aa2	B	A-1+	AA	364 days	15	Current
<u>NETHERLANDS</u>												
Internationale Nederlanden Bank / ING Bank	F1+	AA-	B	1	P-1	Aa2	B+	A-1+	AA	364 days	15	New
ABN AMRO Bank	F1+	AA-	B	1	P-1	Aa3	B	A-1+	AA-	364 days	15	New
Rabobank	F1+	AA+	A	1	P-1	Aaa	A	A-1+	AAA	364 days	15	New
<u>PORTUGAL</u>												
Banco Comercial Portugues	F1	A+	B	2	P-1	A1	B-	A-2	A-	364 days	10	New
Banco Espirito Santo	F1	A+	B	2	P-1	A1	B-	A-2	A-	364 days	10	New

	<u>Fitch Ratings</u>				<u>Moody's Ratings</u>			<u>S and P</u>		<u>Limits</u>		<u>Status</u>
	S.Term	L.Term	Indiv	Suprt	S.Term	L.Term	Fin Stgth	S.Term	L.Term	Time	Money	
<u>OVERSEAS BANKS</u>												
<u>SINGAPORE</u>												
Development Bank of Singapore	F1+	AA-	B	2	P-1	Aa2	B -	A-1+	AA -	364 days	15	New
<u>SPAIN</u>												
Banco Santander Central Hispano	F1+	AA-	B	1	P-1	Aa3	B	A-1	A +	364 days	15	New
Banco Bilbao Vizcaya Argentaria	F1+	AA-	B	1	P-1	Aa2	B +	A-1+	AA -	364 days	15	New
<u>SWEDEN</u>												
ForeningsSparBanken (Swedbank)	F1	A+	B	1	P-1	Aa3	B	A-1	A	364 days	15	New
Skandinaviska Enskilda Banken	F1	A+	B	1	P-1	Aa3	B	A-1	A	364 days	15	New
Svenska Handelsbanken	F1+	AA-	B	1	P-1	Aa1	A -	A-1+	AA -	364 days	15	New
<u>SWITZERLAND</u>												
UBS AG	F1+	AA+	A/B	1	P-1	Aa2	B +	A-1+	AA +	364 days	15	New
<u>UNITED STATES</u>												
Bank of America, N.A.	F1+	AA-	A/B	1	P-1	Aa1	A -	A-1+	AA	364 days	15	New
Bank of New York	F1+	AA-	A/B	2	P-1	Aa2	B +	A-1+	AA -	364 days	15	New
Citibank, N.A.	F1+	AA+	A	1	P-1	Aa1	A -	A-1+	AA	364 days	15	New
CIT Group Inc	F1	A	-	-	P-1	A2	-	A-1	A	364 days	10	New
JP Morgan Chase Bank	F1+	A+	B	1	P-1	Aa2	B +	A-1+	AA -	364 days	15	New
State Street Bank & Trust Company	F1+	AA-	A/B	2	P-1	Aa2	B +	A-1+	AA	364 days	15	New
Wachovia Bank, N.A.	F1+	AA-	B	3	P-1	Aa2	B +	A-1+	AA -	364 days	15	New
<u>OTHERS</u>												
<u>UNITED KINGDOM</u>												
Bank of England	-	-	-	-	-	-	-	A-1+	AAA	364 days	15	New
Local Authorities	-	-	-	-	-	-	-	-	-	364 days	10	Current

RATING DEFINITIONS

Fitch - Short Term Ratings

F-1 Indicates the strongest capacity for timely payment of financial commitments; may have an added "+" to denote any exceptionally strong credit feature.

F-2 A satisfactory capacity for timely payment of financial commitments, but the margin of safety is not as great as in the case of the higher ratings.

Fitch - Long Term Ratings

AAA Highest credit quality.

AAA ratings denote the lowest expectation of credit risk. They are assigned only in case of exceptionally strong capacity for timely payment of financial commitments. This capacity is highly unlikely to be adversely affected by foreseeable events.

AA Very high credit quality.

AA ratings denote a very low expectation of credit risk. They indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.

A High credit quality.

A ratings denote a low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be more vulnerable to changes in circumstances or in economic conditions than is the case for higher ratings.

Note: Plus (+) or minus (-) may be appended to a rating to denote relative status within major rating categories. Such suffixes are not added to the AAA Long-term rating.

Fitch - Individual Rating

A A very strong bank. Characteristics may include outstanding profitability and balance sheet integrity, franchise, management, operating environment, or prospects.

B A strong bank. There are no major concerns regarding the bank. Characteristics may include strong profitability and balance sheet integrity, franchise, management, operating environment, or prospects.

C An adequate bank which, however, possesses one or more troublesome aspects. There may be some concerns regarding its profitability and balance sheet integrity, franchise, management, operating environment, or prospects.

Note: In addition, we use gradations among these five ratings, i.e. A/B, B/C, C/D, and D/E.

Fitch - Support Rating

1 A bank for which there is an extremely high probability of external support. The potential provider of support is very highly rated in its own right and has a very high propensity to support the bank in question. This probability of support indicates a minimum Long-term Rating floor of A-.

2 A bank for which there is a high probability of external support. The potential provider of support is highly rated in its own right and has a high propensity to provide support to the bank in question. This probability of support indicates a minimum Long-term Rating floor of BBB-.

3 A bank for which there is a moderate probability of support because of uncertainties about the ability or propensity of the potential provider to do so. This probability of support indicates a minimum Long-term Rating floor of BB-.

Moody's - Short Term Ratings

P-1 Banks rated P-1 for deposits offer superior credit quality and a very strong capacity for timely payment of short-term deposit obligations.

P-2 Banks rated P-2 for deposits offer strong credit quality and a strong capacity for timely payment of short-term deposit obligations.

RATING DEFINITIONS cont.**Moody's - Long Term Ratings**

Aaa Banks rated Aaa for deposits offer exceptional credit quality and have the smallest degree of risk. While the credit quality of these banks may change, such changes as can be visualized are most unlikely to materially impair the banks' strong position.

Aa Banks rated Aa for deposits offer excellent credit quality, but are rated lower than Aaa banks because their susceptibility to long-term risks appear somewhat greater. The margins of protection may not be as great as with Aaa-rated banks, or fluctuations of protective elements may be of greater amplitude.

A Banks rated A for deposits offer good credit quality. However, elements may be present that suggest a susceptibility to impairment over the long term.

Note: Moody's applies the numerical modifiers 1,2 and 3 in each generic rating category from Aa to Caa. The modifier 1 indicates that the bank is in the higher end of its letter-rating category; the modifier 2 indicates a mid-range ranking; and the modifier 3 indicates that the bank is in the lower end of its letter-rating category.

Moody's - Financial Strength Rating

A Banks rated A possess superior intrinsic financial strength. Typically, they will be institutions with highly valuable and defensible business franchises, strong financial fundamentals, and a very predictable and stable operating environment.

B Banks rated B possess strong intrinsic financial strength. Typically, they will be institutions with valuable and defensible business franchises, good financial fundamentals, and a predictable and stable operating environment.

C Banks rated C possess adequate intrinsic financial strength. Typically, they will be institutions with more limited but still valuable business franchises. The banks will display either acceptable financial fundamentals within a predictable and stable operating environment, or good financial fundamentals within a less predictable and stable operating environment.

Note: The definitions for Moody's Bank Financial Strength Ratings employ the alphabetic notation A through E as well as the symbols + and - to indicate gradation.

Standard & Poors - Short Term Ratings

A-1 An obligor rated A-1 has strong capacity to meet its financial commitments. It is rated in the highest category by Standard & Poor's. Within this category, certain obligors are designated with a plus sign (+). This indicates that the obligor's capacity to meet its financial commitments is extremely strong.

A-2 An obligor rated A-2 has satisfactory capacity to meet its financial commitments. However, it is somewhat more susceptible to the adverse effects of changes in circumstances and economic conditions than obligors in the highest rating category.

Standard & Poors - Long Term Ratings

AAA An obligor rated AAA has extremely strong capacity to meet its financial commitments. AAA is the highest Issuer Credit Rating assigned by Standard & Poor's.

AA An obligor rated AA has very strong capacity to meet its financial commitments. It differs from the highest rated obligors only to a smaller degree.

A An obligor rated A has strong capacity to meet its financial commitments but is somewhat more susceptible to the adverse effects of changes in circumstances and economic conditions than obligors in higher-rated categories.

Note: Plus (+) or minus (-) The ratings from AA to CCC may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories.