

## AGENDA

A meeting of the **Board of Directors** of **North Lanarkshire Municipal Bank Ltd** will be held remotely on **11 March 2021**.

1. Present
2. Apologies
3. Minutes of meeting held on the 23 October 2020
4. Interest rate review
5. AOB : Sponsorship (verbal update)

**NORTH LANARKSHIRE MUNICIPAL BANK LTD**  
**MINUTES OF BOARD OF DIRECTORS MEETING**  
**HELD 23 OCTOBER 2020 AT 10.15AM**  
**VIRTUAL MEETING BY WEBINAR SESSION**

1. Present:

Councillors - R Burrows, T Castles, J Hume, S Watson - Directors

In Attendance:

E Kemp, Head of Finance for Business Solutions, J Quinn, Finance Manager, Treasury

2. Apologies:

I McNeil, J Ashraf N Pettigrew - Directors

3. Approval of Minutes of Previous Meeting:

The minutes of the meeting held on 12 March 2020 were tabled with point to note per item 6 (ii) it was agreed due to the pandemic to suspend

- a) planned developments around the long term marketing strategy
- b) considerations regarding the community hub model and the integration of the Municipal Bank

4. Letter of Representation, Report and Financial Statements year ended 31 March 2020

A set of audited accounts were tabled and circulated. It was noted that the draft accounts had previously been circulated. A brief summary of the main items was presented by J Quinn, with points raised regarding a "typo" in terms of interest paid to customers plus changes to data held on website page. Following this the directors unanimously agreed to the signing of the accounts and letter of representation and that they should be presented to all shareholders at the annual general meeting to be held in March 2021.

5. Resolution to re-appoint Auditors

BDO LLP offered themselves for reappointment in accordance with S385 of the Companies Act 1985. The directors unanimously agreed to the reappointment.

6. Interest Rate Review

J Quinn presented a review of the interest rates which considered the interest rates currently being offered to other financial institutions, the inter-lending relationship between the bank and the Council, and the outlook for interest rates.

In summary an interest rate reduction of the interest from 0.20% to a negative rate of -0.21% is required to re-establish the equilibrium in the borrowing and investment relationship between the bank and NLC. This reflects the current market interest rates being paid on the investment/borrowing of funds in the financial markets. It was noted by all directors that the Council, as shown within Appendix 2, is now providing temporary financial support to the bank of almost £90k based on current rates, level of depositor balances, overhead costs and alternative rates available from other markets. To mitigate this there was a general discussion around potentially reducing the rate to 0.10% but in light of the uncertainties around the pandemic it was unanimously agreed to retain current rates at 0.20%. It was highlighted by Councillor Watson that if current temporary financial support by the Council was to continue over a longer period this may adversely impact on the longer term sustainability of the bank. It was also requested that the next interest rate review include additional details regarding the overhead recharge and how service delivery and availability, as a result of the pandemic, may have impacted the amounts chargeable per transactional activity.

To: Board of Directors North Lanarkshire Municipal Bank Ltd		Subject: Interest Rate Review
From: Company Secretary		
Date: 11 March 2021	Ref: EK/JQ	

## 1. Purpose

1.1 The purpose of this report is to provide an update following the previous interest rate review in October 2020. To review the interest rates currently being offered, in comparison to other financial institutions, whilst managing the inter-lending relationship between the bank and the Council and the outlook for interest rates and the impact of COVID19 (the pandemic).

## 2. Background

2.1 Since 19 March 2020 the Bank of England has retained the base rate at 0.10% with the following table showing the comparative North Lanarkshire Municipal Bank (NLMB) interest rate over the same period:-

Bank of England Base Rate	Interest Rate Bandings	NLMB Ltd Interest Rate
0.10%	£1+	0.20%

Table 1: NLMB Interest Rate applicable since 1 December 2019

## 3. Customer Balances

3.1 Table 2 below highlights the movements in customer balances since 30 September 2020.

Month Ended	No of Accounts	Monthly Movement in Number of Accounts	Customer Balances (£)	Monthly Movement in Customer Balances	% Monthly Movement in Customer Balances
30-Sep-20	5,070		21,775,850		
31-Oct-20	5,054	-16	21,771,233	-4,617	-0.02
30-Nov-20	5,051	-3	21,599,464	-171,769	-0.79
31-Dec-20	5,036	-15	21,519,016	-80,448	-0.37
31-Jan-21	5,029	-7	21,636,712	117,696	+0.55
28-Feb-21	5,012	-17	21,723,027	86,315	+0.40
<b>Cumulative Movement</b>		<b>-58</b>		<b>-52,823</b>	

Table 2: Movement in Customer Balances

3.2 Since 30 September 2020, there has been a decrease of £52,823 (0.24%) in customer balances and a decrease of 58 (1.15%) in customer accounts.

## 4. Interest Rate review

4.1 In carrying out an interest rate review, the bank considers the following:

- interest rates for comparable accounts being offered by other financial institutions;
- the inter-lending relationship between the Council and the Bank;

## 5. Comparable Accounts & Competitor rates

5.1 The interest rates for a range of accounts of other financial institutions are compared to the bank's rates. The comparator range is the closest account type identified when compared to the services available within the bank.

5.2 Per Table 3 below, this demonstrates that NLMB interest rates are comparatively more attractive, as other financial institutions have reduced their interest rates significantly, reflecting the impact of Covid19 and are now marginally above zero. This comparison does not include internet based accounts, which generally offer higher interest rates, however, the account terms and conditions vary significantly from those offered by the NLMB. The comparator range being the closest account type identified when compared to the services available within the NLMB.

Deposit Balance	North Lanarkshire Municipal Bank Ltd	Lloyds/ Bank of Scotland	Santander UK	Royal Bank of Scotland	Barclays
+£1	0.20%	0.01%	0.01%	0.01%	0.01%

**Table 3: Comparator Interest Rates**

## **6. Lending Relationship between the Bank and North Lanarkshire Council**

- 6.1 As part of the interest rate review, the bank considers the relationship for investing customer balances with North Lanarkshire Council (the Council) per the legislation governing municipal banks, which requires that all funds are lent to the Council.
- 6.2 These funds provide the Council with an alternative to borrowing from other sources, maintaining an interest rate profile that facilitates the bank charging the Council a competitive rate which is attractive to both parties.
- 6.3 This arrangement enables the bank to cover its costs and manage its investment, interest rate and liquidity risks, whilst the Council achieves value for money and manages associated treasury management risks, including the underlying guarantee.
- 6.4 Appendix 1 shows, that if current customer balances are maintained and interest rates kept on hold, including overheads, the estimated average annual charge to the Council would equate to 0.98% for sourcing the bank's balances throughout the year.
- 6.5 This charge is currently higher than the 6 month to 1 year London Interbank Offer rate (LIBOR) of 0.43%, which is the average daily rates for period 1 April to 28 February 2021 and considered an acceptable benchmark for comparison purposes, based on the behaviour patterns for withdrawals and deposits by customers. (See Appendix 1)
- 6.6 NLC is currently incurring higher charges than if it obtains similar funds from alternative sources. This situation primarily arising due to the aforementioned Bank of England base rate being retained at 0.10% to manage the impact of the pandemic and the correlational impact upon short term interest rates offered by financial institutions, with speculation surrounding moving to negative interest territory.
- 6.7 To re-establish the equilibrium in the borrowing and investment relationship between the bank and NLC, a reduction in the interest rate payable to customers is required from a positive 0.20% to a negative interest rate of 0.34%, with further detail provided within Appendix 1. This would mean a charge being imposed on customers to deposit their monies, which given the customer base, status and services offered by the bank and potential reputational damage, would not be deemed a realistic option.
- 6.8 To close the interest rate gap, a reduction in the 2020/21 Council overhead recharge given the reduced branch opening hours to implement Scottish Government health and safety guidance for Covid19 at the start of the pandemic was considered, with almost normal business opening hours being restored since August 2020 once offices made Covid secure.
- 6.9 However the review identified the banks share of the counter service costs, based on the percentage of bank transactions to the total transactional activity, had altered significantly, given the significant changes to the counter services provided within the branch locations by shared Council and NLMB staff since March 2020.
- 6.10 In 2019/20 the estimated counter service element of the total overhead charge was approximately £64,645, for 2020/21, if the current fixed overhead charge was adjusted to reflect the impact of the pandemic on the counter service recharge, adopting, the same transactional basis, this would be £151,646, excluding any uplift for NLMB transactional activity taking longer and VAT. As per Appendix 2, an increase of £86,901, as opposed to a decrease, in the charge from NLC for counter services would be applicable.
- 6.11 Notwithstanding the above, it is recognised in these extra-ordinary times, that the functioning interest rate relationship between the Council and the municipal bank has become skewed and therefore the Directors are requested to consider two options:

### Option 1

- 6.12 No change to the current interest rate, with the Council, reflecting the close business relationship, managing the impact of the higher interest costs currently incurred, for utilising municipal bank balances, by achieving other Treasury Management efficiencies from other short term borrowing sources.

### Option 2

- 6.13 Reduce the interest rate from 0.20% to 0.10%, which represents a reduction of 0.10%, to reduce the gap between the interest rate the Council is currently paying and the interest rate incurred to source funding from alternative sources available. The proposed interest rate would still retain the bank rate above the interest rates currently offered by other financial institutions, which as mentioned above, have reduced their interest rates significantly, and are now marginally above zero.
- 6.14 The financial impact of Option 2 compared to Option 1, based on the current average customer balances of £21.8m over a twelve month period, would result in a saving in the interest payable by the Council to the NLMB of £21,830. However, it should be noted that this may have an impact upon the customer balances, which is uncertain, recognising if customer balances were to fall further, the sustainability of the bank in meeting its overhead costs and paying an attractive interest rate to customers becomes increasingly challenging.
- 6.15 Both options are consistent with the approach agreed and confirmed by the Council, in its letter of support to the NLMB. This letter stating that the Council will continue to provide financial support for a period of at least 12 months from the date of approval of the financial statements to 31 March 2020, which is 23 October 2021, as the bank relies upon the support of its parent, North Lanarkshire Council.

## **7. Outlook for Interest Rates**

- 7.1 The medium-term global economic outlook has improved with the rollout of vaccination programmes, of which the UK is at the forefront. However, the current imposition of lockdowns and ongoing social distancing measures will increase the economic damage caused by the pandemic.
- 7.2 The Bank of England will therefore maintain loose monetary conditions for the foreseeable future with this central bank stance mirrored across most developed economies, albeit some, like the Federal Reserve, are closer to monetary tightening than others. Current economic consensus amongst forecasters is the bank rate will remain stable at 0.10% with the risks of a bank rate cut over the medium term having reduced with savings rates trends remaining weighted to the downside.

## **8. Conclusion**

- 8.1 Table 3 above shows that the bank is offering competitive rates when compared to the other financial institutions, therefore scope currently exists for a reduction in interest rates.
- 8.2 Under normal business operating conditions, an interest rate reduction would be required to re-establish the equilibrium in the borrowing and investment relationship between the bank and NLC and to reflect the current market interest rates being paid on the investment/borrowing of funds in the financial markets, which are at historically low levels as markets react to the pandemic.
- 8.3 However, to achieve the optimum position, a reduction in the interest rate payable to customers is required from a positive 0.20%, to a negative interest rate of 0.34%, which would mean a charge being imposed on customers to deposit their monies.
- 8.4 Given the customer base, status and limited services offered by the bank and potential reputational damage, negative interest rates would not be a viable option for the bank and therefore the Council, as parent company, has agreed to provide temporary financial support, which will allow the existing interest rate to be retained or a proposed reduction of 0.10% in the interest rate.

## 9. Recommendation

9.1 The Board is asked to consider the report and agree to either

Option 1: No change to the current interest rate

Option 2: Reduce the interest rate from 0.20% to 0.10% with effect from 1 June 2021.

9.2 Over the coming months, movement in customer balances will be monitored, with the comparator market/competitor interest rates and any changes required to the interest rate agreed to restore the equilibrium position and the removal of the financial support currently being provided by the Council on a temporary basis.



**E Kemp**  
Company Secretary

**Interest Rate Relationship: North Lanarkshire Municipal Bank (NLMB) and North Lanarkshire Council**

The tables below reflect the inter-relationship between the NLMB rate to customers, the average interest rate cost to NLC for using NLMB balances in accordance with legislative requirements and the alternative Money Market interest rate available to the Council if borrowing from other external sources. These interest rates are monitored to ensure an equilibrium between the council's external borrowing rate, the interest rate it incurs borrowing from the NLMB, whilst endeavouring to offer a competitive interest rate to customers.

**Table 1: Current position:** 12 month projection based on average balances held since 1 April – 28 February 2021 at existing 0.20% interest rate; and no change to NLC estimated borrowing costs.

NLMB Income & Expenditure					NLC Loan Charge Analysis			
Average Customer Balances since 31/03/2020	Current NLMB Interest Rate to Customers	Total Annual Interest Payable to Customers	Total NLMB Annual Overheads	Income Receivable from NLC for Use of Balances	Average Interest Rate Cost to NLC in accessing NLMB balances	Money Market Comparable Interest Rate (since 01.04.20) Average 6 – 12 month term	NLC Interest Rate Saving / (Cost) (£)	Estimated Saving / (Cost) to NLC (£)
21,830,395	0.20%	£43,661	£169,534	£213,195	0.98%	0.43%	-0.54%	(£118,703)
<b>Based on the above, over a 12 month period, NLC would incur an additional cost of £118,703 by borrowing from the NLMB compared to external sources. This indicates that the lending /borrowing relationship between NLC and the Municipal Bank is operating sub-optimally and under normal operating conditions there would be a requirement to reduce the interest rates currently on offer to customers. This assumes overhead costs remain the same and there is no movement in the money market rates available from external sources.</b>								

**Table 2: Required change to NLMB customer interest rate (based on current average customer balances) to offer an interest charge to NLC to match equivalent Money Market Rate**

Breakeven interest rate is a negative interest rate 0.34% (charge customers to deposit their monies) based on current average customer balances since 1 April 2020 and to match Money Market interest rates available to NLC.

NLMB Income & Expenditure					NLC Loan Charge Analysis			
Average Customer Balances since 31/03/2020	Breakeven NLMB Interest Rate to Customers	Total Annual Interest Payable by Customers	Total NLMB Annual Overheads	Income Receivable from NLC for Use of Balances	Average Interest Rate Cost to NLC in accessing NLMB balances	Money Market Comparable Interest Rate (since 01.04.20) Average 6 – 12 month term	NLC Interest Rate Saving / (Cost)	Estimated Cost to NLC (£)
21,830,395	-0.34%	-75,042	£169,534	£94,492	0.43%	0.43%	0.00%	£0.00

## Counter Services Recharge: North Lanarkshire Council to North Lanarkshire Municipal Bank (NLMB)

	(1)	(2)	(3)	(3)	(4)	(5)	(6)
Counter Service Area	Estimated No of Transactions Processed 19/20	% of Transactions attributed to each service 19/20	Counter Services Recharge 19/20	Estimated Annual No of Transactions Processed based on 20/21 activity to date	Estimated Annual % of Transactions attributed to each service 20/21	Estimated Counter Service Recharge 20/21	Year on Year Movement in Counter Services Recharge
<b>Approximate Total Budgeted Cost</b>			£1,417,640			£1,417,640	
Cash Receipting/First Stop Shop queries	502,585	95.44%	£1,352,995	108,251	89.31%	£1,266,094	£86,901
NLMB (excl VAT)	23,998	4.56%	£64,645	12,946	10.69%	£151,546	+£86,901
<b>Total</b>	<b>526,583</b>	<b>100.00%</b>	<b>£1,417,640</b>	<b>121,197</b>	<b>100.00%</b>	<b>£1,417,640</b>	