BANK OF ENGLAND

Quarterly Bulletin

2017 Q2

Recent economic and financial developments

Markets and operations

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Markets and operations

This is the final Markets and operations *Quarterly Bulletin* article. Historically, the first section of this article covered developments in financial market asset prices over the preceding quarter. Please refer to the *Inflation Report* and *Financial Stability Report* for this information. The second section provides an update on Sterling Monetary Framework (SMF) operations. This is included in this article. In future, please refer to the SMF Annual Report for this information.

SMF operations

Operational Standing Facilities

Since 5 March 2009, the rate paid on the Operational Standing Deposit Facility has been zero, while all reserves account balances have been remunerated at Bank Rate. As a consequence, there is little incentive for reserves account holders to use the deposit facility. Reflecting this, the average use of the deposit facility was £0 million in the three months to 10 May 2017.[1]

The rate charged on the Operational Standing Lending Facility remained at 25 basis points above Bank Rate. However, given the large aggregate supply of reserves, there was no demand from market participants to use the lending facility. The average use of the lending facility was also £0 million over the quarter to 10 May 2017.

Indexed Long-Term Repo operations

The Bank conducts regular Indexed Long-Term Repo (ILTR) operations as part of its provision of liquidity insurance to banks, building societies and broker-dealers. The total amount allocated in each operation remained well below the minimum £5 billion on offer (**Table A**).

The stock of outstanding ILTR drawings increased over the review period. A total of £2,235 million of ILTRs matured and £6,265 million of new ILTRs were allocated (**Chart 1**), resulting in a net increase of central bank reserves of around £4,030 million from ILTR operations.

Contingent Term Repo Facility

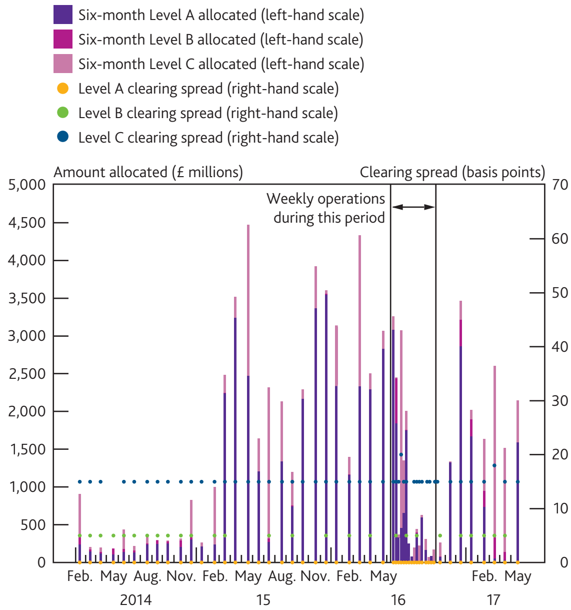
The Contingent Term Repo Facility (CTRF) is a contingent liquidity facility that the Bank can activate in response to actual or prospective market-wide stress of an exceptional nature. The Bank reserves the right to activate the facility as it deems appropriate. In light of market conditions throughout the review period, the Bank judged that CTRF auctions were not required.

Table A Indexed long-term repo operations[(a)]

	Total	Collateral set summary		
		Level A	Level B	Level C
7 March 2017 (six-month maturity)				
Minimum on offer (£ millions)	5,000			
Total bids received (£ millions)	3,560	55	275	3,230
Amount allocated (£ millions)	2,600	55	275	2,270
Clearing spread (basis points)		0	5	18
4 April 2017 (six-month maturity)				
Minimum on offer (£ millions)	5,000			
Total bids received (£ millions)	1,520	40	105	1,375
Amount allocated (£ millions)	1,520	40	105	1,375
Clearing spread (basis points)		0	5	15
9 May 2017 (six-month maturity)				
Minimum on offer (£ millions)	5,000			
Total bids received (£ millions)	2,145	1,590	0	555
Amount allocated (£ millions)	2,145	1,590	0	555
Clearing spread (basis points)		0	–	15

(a) The minimum amount on offer is the size of the operation that the Bank is willing to allocate, in aggregate, across all collateral sets at the minimum clearing spreads.

Chart 1 ILTR reserves allocation and clearing spreads[(a)]



(a) Where there has not been any allocation to a collateral set, no clearing spread is marked.

Discount Window Facility

The Discount Window Facility (DWF) is a bilateral on-demand facility provided to institutions experiencing a firm-specific or

(1) Operational Standing Facility usage data are released with a lag.

market-wide liquidity shock. It allows participants to borrow highly liquid assets in return for less liquid collateral in potentially large size and for a variable term. The Bank publishes quarterly data of DWF usage with a lag. The average daily amount outstanding in the DWF in the three months to 30 December 2015 was £0 million.

Asset Purchase Facility operations

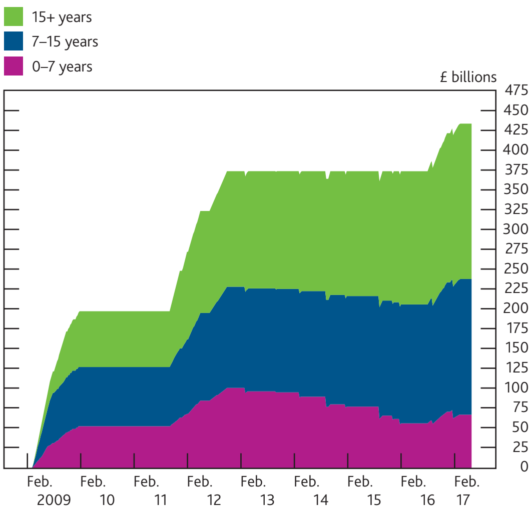
In the publication of the *Inflation Report* on 11 May 2017, the Monetary Policy Committee (MPC) agreed that it remained appropriate to maintain the asset purchase programmes announced on 4 August 2016, financed by the issuance of central bank reserves.

Gilt purchases

On 4 August 2016, the MPC announced an expansion of the asset purchase scheme for UK government bonds of £60 billion, taking the total stock of asset purchases to £435 billion.

Over the review period, the total stock of gilts outstanding in the Asset Purchase Facility (APF), measured as proceeds paid to sellers on a trade date basis, increased from £432.6 billion on 1 March 2017 to £435 billion. The stock of gilts comprised of £67.8 billion (an increase of £0.8 billion) of purchases in the 3–7 years residual maturity range, £171.2 billion (an increase of £0.8 billion) in the 7–15 years residual maturity range and £196 billion (an increase of £0.8 billion) with a residual maturity of greater than fifteen years (**Chart 2**).

Chart 2 Cumulative gilt purchases by maturity[(a)(b)]



(a) Proceeds paid to counterparties on a settled basis.
(b) Residual maturity as at the date of purchase.

In the Market Notice of 2 February 2017, the Bank announced £11.6 billion of gilt purchases to reinvest the cash flows associated with the maturities of outstanding assets. Gilts were purchased in smaller operation sizes, but otherwise in the same format as previous operations. The Bank completed these operations in the review period. All APF gilt purchases over the review period were fully covered.

Gilt lending facility

The Bank continued to offer to lend gilts held in the APF via the Debt Management Office (DMO) in return for other UK government collateral. In the three months to 31 March 2017, the daily average value of gilts lent, as part of the gilt lending facility, was £1,081 million. This was similar to the previous quarter at £1,117 million but higher than the same quarter the previous year at £202 million. This is in part because following the cut in Bank Rate on 4 August 2016, the DMO reduced the cost of its Standing Repo Facility from 40 basis points to 25 basis points, thus reducing the cost of this facility for market participants.

Term Funding Scheme

The Term Funding Scheme (TFS) is designed to reinforce the transmission of Bank Rate cuts to those interest rates faced by households and businesses by providing term funding to banks at rates close to Bank Rate. The TFS is a monetary policy tool of the MPC and is operated as part of the APF.

The Bank began accepting applications to join the TFS on 22 August 2016. During the drawdown period, which runs from 19 September 2016 to 28 February 2018, participants can borrow reserves for four years in exchange for eligible collateral. The quantity and price of funding available from the TFS is based on the amount of eligible lending undertaken by a participant's TFS group. Participants in the FLS will be permitted to repay FLS drawings in order to redraw in the TFS, subject to having sufficient borrowing allowance in the TFS.

As of 31 May 2017, £63,301 million of loans had been made through the TFS.

Corporate Bond Purchase Scheme

The Corporate Bond Purchase Scheme (CBPS) was designed to impart monetary stimulus by: lowering the yields on corporate bonds, thereby reducing the cost of borrowing for companies; triggering portfolio rebalancing; and stimulating new issuance of corporate bonds.

Purchases of sterling corporate bonds, financed by the creation of central bank reserves, are undertaken via the APF.

The Bank purchased, via the CBPS, £10 billion of sterling non-financial investment-grade bonds, representative of issuance, by firms making a material contribution to the UK economy, in order to impart broad economic stimulus.

During the review period, the Bank completed the operations necessary to complete £10 billion of corporate bond purchases. **Table B** shows the representative share for each of

Table B Representative share of each sector of the CBPS and the Bank's holdings in each

Sector	CBPS holdings as at close of business 3 May 2017 (per cent portfolio)	CBPS target sector share (per cent of eligble list)
Electricity	19	19
Consumer, non-cyclical	15	15
Communications	12	12
Industrial and transport	13	13
Water	11	12
Consumer, cyclical	11	11
Gas	8	8
Property and finance	6	6
Energy	3	3
Total	100	100

the nine sectors of the Corporate Bond Purchase Scheme and the Bank's holdings in each of these sectors.(1)

Other operations

Funding for Lending Scheme

The Funding for Lending Scheme (FLS) was launched by the Bank and HM Treasury on 13 July 2012. The initial drawdown period for the FLS ran from 1 August 2012 until 31 January 2014. The drawdown period for the FLS extension opened on 3 February 2014 and will run until 31 January 2018, following the extension beyond January 2016 announced on 30 November 2015.(2) The quantity current participants can borrow in the FLS is linked to their lending to the UK real economy from 2013 Q2 to 2015 Q4, with the incentives skewed towards supporting lending to small and medium-sized businesses. On 1 August 2016, participants' borrowing allowances were reduced by 25% and have been reduced by the same amount every six months thereafter, this continues to phase the scheme out gradually by 31 January 2018.

US dollar repo operations

On 23 April 2014, in co-ordination with other central banks and in view of the improvement in US dollar funding conditions, the Bank ceased the monthly 84-day US dollar liquidity-providing operations. The seven-day US dollar operations will continue until further notice. The network of bilateral central bank liquidity swap arrangements provides a framework for the reintroduction of further US liquidity operations if warranted by market conditions. There was no use of the Bank's US dollar facilities throughout the review period.

Capital portfolio

The Bank holds an investment portfolio that is approximately the same size as its capital and reserves (net of equity holdings, for example in the Bank for International Settlements, and the Bank's physical assets) and aggregate cash ratio deposits. The portfolio consists of sterling-denominated securities. Securities purchased by the Bank for this portfolio are normally held to maturity, though sales may be made from time to time, reflecting, for example, risk or liquidity management needs or changes in investment policy. At the end of the review period the portfolio included around £6 billion of gilts and £0.1 billion of other debt securities.

(1) www.bankofengland.co.uk/markets/Pages/apf/results.aspx.
(2) For more details, see www.bankofengland.co.uk/publications/Pages/news/2015/096.aspx.