United Kingdom
Debt Management
Office

Official Operations in the Gilt Market

An Operational Notice

16 March 2016

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This Notice (the "Operational Notice") sets out the objectives and procedures for the DMO's operations in the gilt market, acting as the Government's debt manager. It replaces all earlier such notices, the most recent of which was published in March 2015, and will come into effect from 1 April 2016.

The Notice sets out the normal market operations which the DMO undertakes in the gilt market. In exceptional circumstances, the DMO may on occasion undertake other operations at its discretion. The DMO may also announce variations in these arrangements, or new forms of market operation, either by special announcement or by means of a supplement or revision to this Operational Notice.

The DMO's cash management operations are outlined separately in the "Exchequer Cash Management Operational Notice".

This Operational Notice should be read in conjunction with the "Information Memorandum on the Issue, Stripping and Reconstitution of British Government Stock", most recently issued in November 2015, and the "Guide to the roles of the DMO and Primary Dealers in the UK government bond market", also re-issued in March 2016. All of these publications are available on the DMO website at: www.dmo.gov.uk.

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1. Framework for Gilt Operations

1. The framework for gilt operations is set out in the Report of the Debt Management Review produced jointly by HM Treasury and the Bank of England in July 1995[1]. With the transition in debt management responsibilities from the Bank to the DMO from 1 April 1998, this framework has since applied to the DMO's operations. A full description of all the DMO's responsibilities, objectives and lines of accountability is also set out in its Framework Document, first published in March 1998, and most recently revised in April 2005.

2. The objective of debt management, as stated in the Debt Management Report, is "to minimise over the long term the cost of meeting the Government's financing needs, taking into account risk, whilst ensuring that debt management policy is consistent with the aims of monetary policy".

3. Alongside the Budget each year (usually in March), the Government publishes a Debt Management Report, including a debt management Remit to the DMO, setting out advance details of the annual issuance programme. This includes a planned maturity structure for the issuance of conventional gilts for the year and an indication of the likely scale of the issuance of index-linked gilts. Within that published framework, the Government aims each year to sell sufficient gilts, Treasury Bills and National Savings and Investments products to finance the Central Government Net Cash Requirement (plus maturing debt and any net change in financing of the foreign exchange reserves).

4. This Notice describes the arrangements for the primary and secondary market operations which the DMO undertakes in implementing the debt management Remit. It covers conventional and index-linked auctions, syndicated offerings, switch auctions, reverse auctions, tenders, conversions, sales to and from official portfolios, and other secondary market operations. In all sections, references to Gilt-edged Market Makers (GEMMs) should be read as applying to those GEMMs recognised by the DMO as specialists in that particular sector of the wholesale and/or retail market – conventional gilts, index-linked or both. Any timings mentioned refer to London time (GMT/BST as relevant).

5. Throughout this document, in respect of index-linked gilts, all references to clean prices relate to real clean prices for 3-month lag and 'uplifted' clean prices for 8-month lag index-linked gilts respectively.

6. Any changes to the arrangements described below will be published through updates to the relevant sections of this Operational Notice.

[1] Copies are available from the Publishing Unit, HM Treasury, 1 Horse Guards Road, London, SW1A 2HQ, and on the DMO website.

2. The Primary Market

2.1 Policy and the Financing Remit

7. Since 1995[2], auctions have constituted the primary means of issuance for both conventional and index-linked gilts, as the government regards such operations as the most transparent and most cost-effective way of issuing gilts over the long term. However, the DMO may issue gilts via other means (e.g. a syndicated offering or gilt tender).

8. The DMO remit is usually published alongside the Budget, in the Debt Management Report (DMR), every spring, which is released after the Chancellor of the Exchequer has delivered the Budget speech. An indicative annual calendar of gilt auctions is also published as part of the DMO's Remit announcement.

9. The DMO's remit is set by HM Treasury following consultation with the DMO, primary dealers, investors and other market participants. Primary dealer firms and other market investors are invited to send a representative to annual meetings, chaired by the responsible Minister, in order to state their recommendations on the content of the forthcoming year's remit, the perceived needs and demands of the market, and any other topical issues of the time.

10. The financing remit for each financial year will indicate the target amounts of cash to be raised in conventional gilts and index-linked gilts, and within conventional gilts the amounts to be raised in each maturity band[3], as well as the planned split by method of issue. Further operational details (such as the planned dates for auctions) are published in a parallel remit announcement by the DMO.

11. The issuance programme may be varied during the year in the light of any substantial changes to any of the following: (a) the CGNCR, (b) the level and/or shape of the yield curve, market expectations of future interest and/or inflation rates, (c) market volatility, or (d) any other criteria specified in the relevant annual Remit. In practice, variations are most likely to occur in regular quarterly issuance announcements, or at the time of publication of the outturn of the previous year's CGNCR in late April, and/or at the time of the in-year revision to the public finance forecasts, usually in November or December. Any revisions will be announced by the DMO.

12. Decisions by the Chancellor over the timing of the Budget, and other announcements which revise the public finance forecasts, may result in the re-scheduling of previously-announced gilt operations, given the market sensitivity of these events.

2.2 Prior Notice of Gilt Auctions

13. The DMO hosts quarterly consultation meetings with representatives of GEMMs and end investors. These meetings are normally held towards the middle of March, May, August and November, and are intended to inform the DMO of the market's preferences for the issuance of individual gilts in forthcoming quarters (April-June, July-September, October-December and January-March), within the constraints of the published remit. Summary minutes of these meetings are published on the DMO's wire services and web pages as soon as practicable the following day.

14. On a quarterly basis, the DMO will announce its plans for auctions to be held over the following one to four months, typically at 3:30pm on the last business days of March, May, August and November. These announcements will normally indicate the identity of the individual

[2] See: http://www.dmo.gov.uk/documentview.aspx?docname=remit/report95.pdf.
[3] The DMO defines maturity bands as follows: shorts 1-7 years to maturity, mediums 7-15 years, and longs 15+ years.

existing gilt(s) or, if relevant, the launch of any new one(s), although coupons on new gilts are usually fixed closer to the auction date itself.

15. At 3:30pm on the Tuesday in the week preceding a scheduled auction, the DMO will publish the final terms and conditions of an auction, including the nominal amount of the gilt on offer, ISIN and SEDOL codes etc., and, where the gilt is a new one, the coupon, which will normally be set at current market yields for the relevant maturity, where possible rounded to the nearest 1/4% for conventional bonds, 1/8% for index-linked. Further issues of already existing gilts will usually be fungible with the parent issue from the settlement date of the auction.

2.3 Auction Mechanics

16. With the exception of small retail bids from members of the DMO's Approved Group scheme (see below), all bids at gilt auctions must be submitted by, or through, a recognised primary dealer firm, via the Bloomberg Auction System (BAS), or, in emergency circumstances only, by electronic mail or by direct telephone line to the DMO's dealing desk, whichever is specified by the DMO. All other investors wishing to participate in the auction process must submit their bid to a GEMM firm of their choosing, which is in turn obliged to submit that bid to the DMO, via BAS, without charge or discount.

17. Bids may be submitted at any time from the opening of the bidding window (usually 8:00am on the morning of an auction), up until the published deadline (usually 10:30am), after which no further bids can be accepted.

18. Unless otherwise notified, each competitive bid, from a GEMM or a client bidder, must be for one amount and at one clean price, expressed as a multiple of 0.001[4] of £1, for at least £1 million nominal and round multiples thereof.

19. Dealers bidding on behalf of clients, or other non-GEMM dealers in their firm, must enter a client code in the relevant field on their bid input screen. Client codes are allocated and maintained by the DMO dealers, and any client institution intending to participate in the auction should apply directly to DMO dealers for allocation of a code. Applications may be made by e-mail, Bloomberg message or headed letter. Such codes are unique, and will be retained for use in future auctions. However, the assignation of such a code should not be taken as a signal that the DMO has verified the legitimacy of the client institution, and GEMM firms are expected to conduct their own due diligence validations. GEMM dealers or salespeople may not apply to the DMO on behalf of a client, but the latter is expected to reveal its code when submitting a bid to a GEMM. New applications for codes should be made to the DMO by the close of business on the evening before any auction.

20. Client institutions that are part of the same parent organisation as a GEMM firm (e.g. a bank's Treasury operation) may also apply for the assignation of a client code, but in such cases the DMO will seek additional assurances around the independence and segregation of the two entities.

21. Primary dealers are also offered a non-competitive allowance at each conventional or index-linked auction. The DMO sets aside a total of 15% of the nominal amount on offer to provide the GEMM community with the assurance of a guaranteed minimum allocation, in order that they are more willing to carry short positions into the auction itself. In conventional gilt auctions, the 15% allowance is divided equally amongst wholesale GEMM firms, while in index-linked auctions individual firms' allowances, within the 15% aggregate total, are determined by reference to that firm's successful competitive bidding results in the three previous index-linked auctions. Allowances are calculated to the nearest £100,000 nominal. Note that non-competitive

[4] From April 2014. Prior to this date, in multiples of 0.01 (ie. two decimal places).

allowances are not automatic – GEMMs must request an allocation each time, in one single non-competitive bid, for a size that is a multiple of £100,000, up to the stated maximum. Non-competitive bids are filled at the average accepted price in conventional gilt auctions, and at the strike price in index-linked auctions.

22. Other applicants, who are members of the DMO's Approved Group of Investors[5], may bid non-competitively by delivering a completed application form to the DMO by either of the following means: (a) to arrive at the Registrar[6], not later than 10:00am on the day of the auction; or (b) to be lodged at the DMO's office at Eastcheap Court not later than 10:00am on the day of the auction. Approved Group bidders can make a non-competitive bid for up to £500,000 nominal in both conventional and index-linked gilt auctions, subject to a minimum application of £1,000 nominal and a limit of one bid per applicant, in £1,000 multiples.

23. Further details on all aspects of auction bidding, including operational aspects of BAS and contingency arrangements, can be found in the GEMM Handbook "A guide to the roles of the DMO and Primary Dealers in the UK Government bond market" and the user guide ""Bloomberg Auction System – User guide for gilt primary market operations conducted by the UK Debt Management Office"", issued to all GEMMs, and available to primary dealers upon request to the DMO.

24. In processing auction results and allocations, the DMO may, at its own discretion, decline to allot some or all of the stock bid for to an individual institution, if it is deemed likely that a large allocation may lead to post-auction market distortion. In conventional auctions, the maximum permitted allocation for any single bidding institution is set at 25% of the nominal amount on offer, and in index-linked auctions the figure is 40%. In the case of GEMMs, the DMO will take account of any formally notified net short position already accumulated in the stock, thus raising their potential maximum allowance proportionally. Should there be a need to scale back any allocations, the DMO will discard the lowest competitive bid(s) first, up to the relevant cut-off point. Non-competitive bids and bids on behalf of unrelated clients will be unaffected by this measure. The maximum allocation limit for client bidders is absolute, and any client bidding for more than 25%/40% may be scaled back by the same method (i.e. lowest priced successful bids first) and, if necessary on a pro-rata basis per GEMM, where multiple bids are at the same price. The DMO also retains the right to refuse or amend bids in the case of any other error or irregularity in the bidding process, and any bid is not legally deemed to be accepted unless/until the auction results are published.

25. Allocations at the lowest accepted price are scaled pro rata, rounded down to the nearest 0.0001%, and all such allocations are in multiples of £1,000 nominal of gilts. Any small rounding residual amount is retained by the DMO on its own portfolio.

26. Results of the auction will be released on the DMO's wire services pages and in a press notice, simultaneously to all market participants, as soon as all the necessary calculations, allocations and checks have been performed internally by the DMO.

27. Gilt auctions will normally settle on the following business day, in accordance with the T+1 convention in the gilt market. For auction settlement purposes, accrued interest is rounded to 6 decimal places per £100 nominal.

[5] The Approved Group of Investors is a group of investors who have satisfied the evidentiary requirements of the DMO regarding the identity of any applicant for Stock or of any person for whom an applicant is acting as agent. Requests to be admitted to the Approved Group can be made at any time but failure to provide satisfactory evidence of identity will result in an applicant being refused admission to the Approved Group.

[6] HM Treasury's designated Registrar, currently Computershare Investor Services plc, The Pavilions, Bridgwater Road, Bristol, BS99 7NH, tel no. 0870 702 0003, website www.computershare.com.

28. All successful primary dealer bidders are expected to match the DMO's settlement instructions, and to meet their commitments on the day and in good time.

29. The target cash raising amounts for conventional and index-linked auctions are set out each financial year in the annual Debt Management Report, published by HM Treasury at the time of the Budget. As a general rule, the DMO will aim for even-paced funding in each sector and will tailor the sizes of individual auctions to take account of the amount of risk being offered to the market in each operation. This means that auctions for shorter-dated gilts will generally be for larger nominal sizes than those for longer-dated gilts, although there is no formulaic correlation. In determining the size of individual auctions, the DMO may also take into account specific market events (e.g. index changes, redemptions, coupon flows etc.), perceived levels of demand, and any portfolio considerations of its own.

30. The procedures described above apply commonly to all conventional and index-linked gilt auctions conducted by the DMO. The following paragraphs identify areas where procedures and regulations may differ from one type of auction to another:

2.4 Conventional Gilt Auctions

31. Conventional gilt auctions are held on a bid price basis (i.e. successful bidders pay the price that they bid), with non-competitive bids allocated at the weighted average accepted price.

32. Direct bidding is open to all primary dealers, wholesale or retail, recognised as a GEMM in conventional gilts, and permissioned as such in BAS.

33. The published results of a conventional gilt auction will include details of the highest, average and lowest accepted prices (with the pro rata scaling rate at the lowest accepted price); the gross redemption yields equivalent to these prices; the total nominal value of accepted non-competitive bids (split between GEMMs and non-GEMMs); the total value of all bids received, including those rejected in whole or in part on account of price; and the ratio of this total to the amount on offer (the 'cover').

2.5 Index-linked Gilt Auctions

34. Index-linked gilt auctions are held on a single price basis (i.e. all successful bidders pay the lowest accepted price), with non-competitive bids also allocated at this lowest accepted price.

35. Direct bidding is open to those primary dealers, wholesale or retail, recognised as an index-linked GEMM, and permissioned as such in BAS.

36. The published results of an index-linked gilt auction will include details of the common allotment price (with the pro rata scaling rate at this lowest accepted price); the real yield equivalent to that price (and any inflation assumption contained therein); the total nominal value of accepted non-competitive bids (split between GEMMs and non-GEMMs); the total value of all bids received, including those rejected in whole or in part on account of price; and the ratio of this total to the amount on offer (the 'cover').

2.6 Post Auction Option Facility (PAOF)

37. Since 1 June 2009, all UK gilt auctions – conventional and index-linked – have included an additional Post Auction Option Facility (PAOF), whereby all successful direct bidders – GEMMs and clients – are offered the right to purchase up to an additional percentage (15% from 1 April 2016) of the gilt they were allotted at the relevant auction, at the published average accepted price in multiple price format auctions, or at the published strike price in auctions of uniform price format.

38. Following each auction, the DMO calculates each GEMM's option entitlement, based on that firm's successful bids – non-competitive, own account and/or those on behalf of clients.

39. The option take-up window is currently open from 12:00 noon until 2:00pm on the day of the auction and GEMMs have until the cut-off time to inform the DMO electronically via BAS whether they wish to take-up some or all of their entitlement. Dealers may cancel or amend these 'bids' as they wish, and only those 'live' at the cut-off time shall be counted.

40. GEMMs are under an obligation to pass on the right to the option to any client bidder(s) that submitted successful bids in the auction through their firm, and, as a result, dealers should factor client take-ups into the single amount of options that they 'bid' for during the take-up window. However, in the event that a client does not wish to take up his/her allowance, the GEMM may opt to take up that allowance.

41. After the designated take-up deadline has passed, the DMO calculates the total take-up of the option facility across all GEMMs, and publish this total as soon as practicable, on its wire services pages and website. This announcement also contains the revised total nominal amount in issue of the relevant gilt.

42. The DMO only creates an additional amount of the gilt equal to the nominal amount of options taken up.

43. Settlement will normally take place on the following day, in line with the T+1 convention in gilts. GEMM dealers taking up option entitlements should book a single purchase trade as a normal secondary market transaction with the DMO, at the option strike price and separate from any instructions relating to the auction, and, where relevant, sales ticket(s) to clients who have exercised their options to purchase stock, at the same price.

44. The PAOF will not be offered in the event that the auction itself is uncovered. For the avoidance of doubt, 'uncovered' in this respect means cases where either (i) insufficient bids were received, or (ii) where the DMO has exercised its discretion not to accept bids that it judged to have been at an unacceptably deep discount to the prevalent market level (see below).

2.7 Uncovered Auctions

45. The DMO reserves the right not to allot all of the gilts on offer at a conventional or index-linked auction, although it would consider this only in exceptional circumstances, where it judges bids to be at an unacceptably deep discount to the prevailing market level. This is particularly, but not exclusively, pertinent to the index-linked sector, where the nature of the single price auction format means that the entire auction is allocated at the same low price, rather than individual outlier bids. In some circumstances, this could even mean that allocating a larger nominal amount of stock would actually lead to a lower amount of revenue being raised. In such cases, the DMO is likely to reject the lower bids. In other circumstances, an auction may still not be 100% covered, even if all bids submitted are accepted.

46. Where a regular conventional or index-linked auction is uncovered, for whatever reason, it is likely that the remaining gilts will still be created from the National Loans Fund, although the DMO does have the option to cancel the residual amount immediately. The unsold balance will then be held by the DMO on an official portfolio for a certain period of 'purdah' in order to allow market conditions to stabilise. The DMO may then offer the balance for re-sale at a time of its choosing, but no sooner than three business days after the original auction. These arrangements will be detailed in a screen announcement to be published immediately after the

results of an uncovered auction. Depending upon the amount of gilts involved, the re-sale of the unsold balance may be via a tender (see below).

2.8 Switch Auctions

47. Switch auctions were designed to allow the DMO, and the market, to execute large-scale switches out of one gilt into another. This process involves the cancellation of the relevant amount of the source gilt and the creation of an extra corresponding amount of the destination gilt. Switch auctions may be employed in various circumstances – (a) to maintain a supply of current benchmark gilts in a low issuance environment, or (b) to allow the DMO to smooth the immediate gilt redemption profile. Note that switch auctions are no longer employed as a means of facilitating market events, such as index extensions. The decision on whether or not to offer a switch auction is entirely at the discretion of HM Treasury and the DMO, but any planned operations (date of auction and gilts involved) will be announced in the regular quarterly auction calendar announcement.

48. The bidding mechanics of a switch auction are similar to those of regular auctions, in terms of who may bid directly (i.e. GEMMs only), utilisation of BAS, timings, bid denominations etc. Conventional switch auctions are held on a competitive bid price basis, index-linked switch auctions are single price format.

49. The differences are as follows:

- The DMO will fix its bid price for the source gilt 15 minutes before the bidding deadline, at the prevalent mid-market price, and publish this price on its wire services pages,
- GEMMs, either for their own account or on behalf of clients, submit 'bids' in terms of the amount of the source gilt that they are offering and the clean price at which they are willing to buy the destination gilt,
- There is no non-competitive bidding facility,
- Maximum bidding and/or allocation limits are discretionary – any limitations would be pre-announced by the DMO on the preceding Tuesday.

50. The DMO will not set a minimum bidding price, but, before accepting any bids, it will be mindful of fair value in the market, and reserves the right to reject any bids it judges to be at an excessive discount. Any shortfall from the pre-announced maximum simply means that less of the destination gilt will be created.

51. The published results of a switch auction will include, where applicable, details of the highest, average and lowest accepted prices of the destination gilt (and the dirty price ratios relating to these prices); the nominal amounts of the source gilt offered and accepted; the nominal quantity of the destination gilt created; the new amounts outstanding following the switch auction; any pro-rata scaling percentage for bids submitted at the lowest accepted price; and the ratio of bids received to the amount on offer (the 'cover').

52. Switch auctions are cash neutral operations, hence successful bidders will be allocated nominal amounts of the destination stock calculated as the ratio of the dirty prices of the two gilts, rounded to the nearest 4^{th} decimal place. Source gilts that were successfully switched will be cancelled at the same time as the new stock is created. The DMO expects all successful bidders to be able to deliver their commitment of the source gilt on the settlement date.

2.9 Reverse Auctions

53. In times of low financing requirements, or for other market management reasons, the DMO's financing remit, set out in the annual Debt Management Report, may include provisions for reverse auctions, whereby the DMO, on behalf of HM Treasury, will make an offer to buy

back, and subsequently cancel, pre-announced amounts of one or more gilts. The scheduling of any reverse auction(s) would be announced as part of the usual quarterly funding announcement.

54. Where offers in multiple gilts are invited, the gilts involved will normally be of a similar duration and/or maturity. The DMO will not hold a reverse auction in any gilt that is, or has a reasonable likelihood of becoming, the cheapest-to-deliver gilt in any active gilt futures contract. The maximum size of such an operation will be limited to the same upper constraints as on regular auctions, as specified in the relevant year's remit – the actual size(s) and gilt(s) involved would be announced at 3:30pm on the Tuesday in the week preceding the operation.

55. The mechanics of a reverse auction are again similar to those of regular auctions, in terms of who may offer directly (i.e. GEMMs only), use of BAS, timings, denominations, price increments etc. Conventional reverse auctions are held on a competitive offer price basis, index-linked reverse auctions are single price format.

56. As with switch auctions, there is no non-competitive facility and the DMO will not set a maximum price, but, before accepting any offers, it will be mindful of fair value in the market, and reserves the right to reject any offers it judges to be at an excessive premium. Any shortfall from the pre-announced maximum simply means that less stock is purchased, and subsequently cancelled.

57. In determining the results of a multiple gilt operation, the DMO will convert prices offered to yield equivalents, subtract from these values the theoretical yield for each gilt, as calculated by the DMO's own yield curve model, and allot acceptances to the highest relative yields offered. Allotment continues until the maximum pre-announced cash amount of stock is purchased. There are no limits on allocation of purchases to particular gilts or bidders.

58. Acceptances at the highest accepted price will be in multiples of £1,000 nominal of each gilt.

59. The published results of a reverse auction will include details of the highest, average and lowest accepted prices of each of the gilts involved; the nominal amounts offered, purchased and remaining in each; any pro rata scaling percentages at the highest accepted price in each; and the ratio of the cash value of offers received to the cash the DMO offered to bid for (the 'cover').

60. Any gilt purchased by the DMO in such an operation will normally be cancelled on the settlement date. The DMO expects all successful sellers to be able to deliver their commitment on that date.

3. Gilt Tenders

3.1 Policy and Mechanics

61. The conventional and index-linked gilt auction programme in any year may be supplemented between auctions by official sales of gilts by the DMO via gilt tenders. Gilt tenders will typically be for existing gilts and for a lower size (in cash terms) than conventional and index-linked gilt auctions of equivalent maturity. The DMO's annual remit may specify any plans for sales by gilt tender, and may also set out any rules concerning notice periods, amounts and/or maturities of such operations.

62. Demand for gilt tenders (including views on preferred timing and/or choice of gilt) may be communicated to the DMO via the quarterly consultation process or at other times during the year. Advance notice will be given of the specific details of the gilt tenders via an announcement(s) that will detail the identity of the gilt(s) involved; the intended size of the operation; any applicable limitations on participation (e.g. minimum acceptable prices, number of bids permissible, and allocation limits); and other operational details. Tenders in index-linked gilts will normally be held on a single price basis, and those in conventional gilts may be either single price or multiple price format, with bids at the striking/clearing price subject to the usual pro rata scaling. There are no non-competitive or post auction option facilities in respect of gilt tenders.

63. GEMMs will be invited to submit bids via BAS, either for their own account or on behalf of clients, in the usual denominations, within the timetable outlined in the screen announcement. Results of the operation, including new amounts outstanding, will be published as soon as possible, with settlement and, where appropriate, creation of the relevant gilt(s) taking place on the following business day. The DMO expects all counterparties to be able to honour their commitments on that day.

3.2 Other operations

64. The DMO may also use the gilt tender process described here for other larger-scale market operations, such as the subsequent sale of the unsold portion of gilts following an uncovered auction, or the acquisition or disposal of gilts on behalf of other government funds, under the management of the Commissioners for the Reduction of the National Debt (CRND) or others. These may be sales or purchases.

4. Syndication

65. Although auctions constitute the primary means of gilt issuance, the annual debt management Remit (contained in the Debt Management Report) may include provision for syndicated issues of debt, including the target maturity bands or sector(s) of the market, expected size and number of operations in such a programme.

66. The DMO will give sufficient notice of its intentions regarding syndicated offerings to allow the market to be suitably prepared for the event(s), but the degree of precision announced on the type (conventional or index-linked), maturity/maturity area or timing of each sale will vary according to the proximity of the intended syndication, to allow the DMO to react to market demand at the time.

67. Market feedback on syndication candidate bonds will be sought at quarterly consultation meetings with GEMMs and investors, and bilaterally on an on-going basis. Around two weeks in advance of an intended syndication, the DMO will announce further details relating to the operation, on its wire services pages and subsequently on the DMO's website.

68. In allocating lead management and other roles in syndicated issues under such a programme, the DMO will offer all relevant GEMMs the opportunity to present their advice and credentials on a regular, fair and equal basis. Factors such as: active participation in the primary market (including regular bidding participation in auctions), as well as the secondary market, expertise in the relevant market sector, timely provision of good quality market intelligence and responses to DMO requests for feedback and consultation exercises will be taken into account in the final selection decision, which shall be merit-based, although no specific targets, selection criteria or league tables will be published. However, the DMO will operate the selection process within a general design that, where possible, allows for most wholesale GEMM firms to have the opportunity to act as a lead manager in a syndicate during the life of the programme, subject to performance. The aforementioned factors are those most likely to lead to a GEMM being considered for a lead management role. The DMO would also not normally expect to appoint any non-GEMM institution to any role in the managerial group. Equally, newly-appointed GEMM firms and/or retail GEMM firms will not normally be eligible to participate in such a group, but may be invited at the DMO's sole discretion, for example, in cases where specific or smaller investors are targeted.

69. Lead managers are likely to be formally appointed and announced to the market around a week in advance of the intended issue date. Individual roles within the lead management group may be assigned nearer to the time of sale.

70. The precise structure of the group and method of sale may vary from issue to issue. The DMO will take such decisions based on its own policy and portfolio preferences at the time and advice from GEMM firms on prevalent best practices and their recommendations for the particular issue.

71. The DMO will endeavour, via screen and web announcements, press notices and/or communiqués from lead managers, to keep all market participants informed of developments in the syndication process at all key stages of the operation.

5. Conversion Offers

72. Exceptionally, the DMO may announce a conversion offer, usually with the aim of building up the size of a new gilt benchmark and/or retiring an old, 'off-the-run' one.

73. In determining which gilts might be candidates for conversion, the DMO will not consider any conventional gilt that is or has a reasonable likelihood of becoming, cheapest-to-deliver into any active[7] gilt futures contract. The DMO will not normally schedule offers so that fixed conversion terms on any two offers run concurrently. Moreover, a conversion offer will not be scheduled to coincide with a gilt auction in the same maturity area.

74. Conversions may be announced on any day, normally at 3:30pm, on the DMO's wire services pages, in a press notice and on the web site. This announcement will contain details of the source and destination gilts, the fixed price terms of the offer, and the timetable and method of acceptance. The price terms of the offer will be decided by the DMO, using its own yield curve model to provide a benchmark (dirty price) ratio and, where necessary, adjusting this ratio to take account of any observed cheap/dear characteristics in the market for the relevant gilts.

75. Holders have until the pre-announced prescribed time on the closing date to notify the Registrar, Computershare, via CREST, of their intention to 'assent' to the conversion. Non-CREST holders should notify the Registrar directly if they intend to assent. Notice to assent, once given, is irrevocable.

76. Any holder who is the beneficial owner of source gilt, but who has lent it out in the repo market or elsewhere, still has the right to choose whether or not to accept the offer (and, if the term of the repo/loan goes over the closing date, to receive the destination gilt instead), but the holder must communicate his intention to the borrower in sufficient time for the latter to be able to assent the gilt on behalf of the owner.

77. The DMO will usually announce the results of a conversion offer at 8:30am on the first business day following the closing date of the offer. This announcement will include the nominal amount of source gilts assented, the percentage rate of take up and any amount remaining unconverted. It will also detail the nominal amount of new destination gilts created, and the revised total nominal outstanding in that gilt. If appropriate, the DMO may also announce whether the source gilt has been assigned 'rump' status (i.e. a bond in which the amount remaining in issue is deemed too small to for market makers to be obliged to quote a two-way price on demand).

[7] 'Active' means a contract that already has outstanding open interest.

6. Other Official Operations

78. The DMO undertakes a number of other official operations in the secondary market, with the GEMMs, in its role as debt manager or to assist cash management. These include:

- trading in near maturity gilts;
- offsetting larger positions accumulated as a result of its dealings for the retail Purchase and Sale Service;
- purchases and sales of gilts for other official portfolios;
- activity in other exceptional circumstances;
- creating gilts for repo purposes.

A. Dealing in near-maturity gilts

79. For purposes of smoothing redemption cash flows, the DMO is prepared, when requested by a GEMM, to bid a price of its own choosing for any gilt, including any strip, that has less than twelve months left before its maturity As these are essentially money market instruments by this stage, the price bid will be dictated by the DMO's cash management operations at the time of the request. Since August 2003, the DMO, with the consent of the Gilt-edged Market Makers' Association (GEMMA), has been a recognised gilt market counterparty of gilt Inter-dealer Brokers (IDBs), in order to help preserve its anonymity when trading in near-maturity gilts only.

B. Gilt Purchase and Sale Service

80. Since December 2004, the DMO has been responsible for the transaction of orders received from members of the public under the Gilt Purchase and Sale Service[8]. This is a low-cost, execution-only service in gilts offered through Computershare Investor Services PLC (the Gilt Registrar) to smaller investors who have registered on the DMO's Approved Group.

81. Under normal circumstances, the DMO will transact these orders over its own portfolio, but in times of heightened demand to purchase or sell a particular gilt or gilts, DMO dealers may choose to offset the effect on its portfolio by buying or selling gilts from GEMM counterparties.

82. In the interests of transparency to investors, the DMO will publish on its website, on a daily basis, prices at which Purchase and Sale transactions have been executed on that day. This will take the form of a 'snapshot' of bid and offer prices in all gilts taken at the time that prices were confirmed to Computershare, regardless of whether or not an order was actually received in each gilt. The exact timing of the snapshot will vary from day to day, but will usually be at around midday.

C. Dealing on behalf of other Government entities

83. From time to time, the DMO may be asked to execute market transactions in gilts on behalf of funds under the management of CRND or other UK Government entities. These may be purchases or sales. In such circumstances, the DMO will request bids or offers as relevant from three randomly chosen GEMMs, either electronically or by telephone, and deal on the best price received, provided that the order is for 'normal' market size. Where the size is smaller-than-average, the DMO may ask for prices from 'retail' GEMMs only, and where the size is deemed larger-than-average, the DMO may run a (reverse) tender, following the process described in Chapter 3 above.

[8] Prior to December 2004 this was a responsibility of the Bank of England.

D. Purchases or sales of conventional and index-linked gilts in exceptional circumstances for market management reasons

84. The DMO reserves the right to purchase or sell conventional and index-linked gilts offered by (or to) GEMM firms, but would do so only in exceptional circumstances.

85. In such exceptional circumstances, the procedure would be as detailed in the section on (reverse) tenders (Chapter 3 above).

E. Standing repo facility

86. The DMO operates an automatic, non-discretionary standing repo facility, whereby any GEMM, or other DMO counterparty, who has signed the relevant documentation, may request that the DMO repos out any gilt for repo purposes, which may involve temporary creation of the relevant gilt. The facility exists in order to ensure that market makers can be assured of being able to access and deliver any gilt at any time, albeit at a price, hence maintaining their ability to make two-way prices in the secondary market and avoiding the prospect of delivery failures. The facility is available from 12:30pm on the previous day up until 11:30am on the same day of settlement. Participants may roll the facility on a day-to-day basis, but the DMO does not anticipate accommodating a continuous roll for a period of more than two weeks. The minimum size of such a request is £5 million nominal per gilt, and the DMO will charge a penal overnight rate, usually expressed as a discount to the Bank Rate. At the same time, the DMO will normally insist on a back-to-back reverse repo of gilt collateral (GC) at the Bank's official rate, in order to neutralise the effect of the standing repo on funding requirements and its own cash management operations. The full Terms and Conditions of the Facility are published separately on the DMO website, and may be revised from time to time according to market conditions and the prevailing Bank Rate. Any changes will be announced. Details of the amount and terms of any standing repo trigger will be published on the DMO's dedicated wire services pages and website as soon as possible after 11:30am on the relevant day, and the DMO will also publish the return of the gilt(s) on the following day or later, as appropriate. The counterparty(ies) involved will remain anonymous to the market, although the DMO reserves the right to share such information with other official regulatory bodies in appropriate circumstances. In the event that gilts are created for such purposes, the DMO understands that none of such gilt(s) will be eligible for inclusion, temporary or otherwise, in the calculation of FTSE or iBoxx gilt indices.

G. Special repo facility

87. If the DMO considers that there is sufficient evidence of severe market dislocation or disruption, it may offer gilt(s) for repo-ing to any GEMM that has signed the required legal agreements with the DMO on different terms to those of the Standing Repo Facility. Again, this may involve temporary creation of the relevant gilts. Such circumstances will need to have been persistent and are not likely to be tied to any single event (e.g. delivery of a cheapest-to-deliver gilt into a single futures contract) or difficulties encountered by a single market participant. The terms and conditions of the facility, including any rate of repo, which may or may not be penal, and the amount of gilt(s) available for creation, will be announced on the DMO's wire services pages and the website. Any subsequent cancellations or withdrawal of the facility will be also announced in a similar fashion. As with the standing repo facility, such operations will usually involve a back-to-back, cash-for-cash reverse repo of gilt collateral with the same counterparty(ies) at the Bank of England's prevailing Bank Rate. Where gilts have been created, the DMO understands that none of such gilt(s) will be eligible for inclusion, temporary or otherwise, in the calculation of FTSE or iBoxx gilt indices.

7. Provision of Reference Prices

A. Intra-day composite prices

88. Between the hours of 8:00am and 4:15pm London time, on a best endeavours basis, the DMO collates and publishes a composite page of reference mid-prices in conventional and index-linked gilts. These prices represent the average of contributions from GEMMs to the wire services, after discarding any stale contributions and the highest and lowest outlier quotes for eachgilt. The DMO's composite pages will therefore update every time a new GEMM contribution in any single gilt is sufficient to change the overall average price. Note that these reference prices do not constitute an offer from the DMO to buy or sell securities, nor are they in any way intended to be binding on GEMMs dealing with other market participants, and no liability is assumed by the DMO. Ownership of the input data remains with the contributing GEMMs, the output with the DMO, and no GEMM or third party may re-distribute them, in any format, on a chargeable basis. The composite reference prices are published to various wire services providers and are available to all subscribers to those services, without additional charge and without discrimination over access. A list of the relevant wire services pages is attached in the Annex.

B. End-of-day GEMMA reference prices

89. The DMO, on behalf of the Gilt-edged Market Makers Association (GEMMA), currently collates and publishes end-of-day reference mid-prices in every gilt – conventional, index-linked and STRIPS[9]. In 2015, the DMO announced its strategic intention to withdraw from the provision of these prices in due course, following a period of stakeholder engagement, review and transition process to a potential alternative provider or providers. An Independent Reference Prices Review is taking this forward, under the leadership of Professor David Miles.

90. At 4:15pm every day, each GEMM is currently required to provide a mid-market clean price for every gilt (conventionals and index-linked) in which they make a market. Theoretical reference prices for STRIPS are calculated by the DMO's own yield curve model, but using the GEMMs' contributions in conventional gilts as its price source. These prices are collated by the DMO and then published on its dedicated wire services pages, usually at 5:00pm, and later in the evening on the DMO website, all on a best endeavours basis, with no liabilities assumed by the DMO. For further details of the precise method of calculation, please see the relevant section of the DMO website[10]. These prices are for reference purposes only, and do not constitute an offer to buy or sell securities.

[9] In the case of strips, the DMO publishes indicative prices based on its internal yield curve.
[10] "GEMMA Reference Prices: Calculation Methodology" June 1999 (and as updated thereafter) available on the DMO website.

8. Announcements to the Market

91. In the interests of transparency and predictability, the DMO strives to release announcements at a set time of the day. For gilt auctions and tenders this will usually be shortly after 10.30am. Unless otherwise mentioned, announcements to all market participants are generally released at 3:30pm, and occasionally at 7:30am or 8:00am, simultaneously on all recognised wire services and as soon as possible thereafter via a DMO Press Office e-mail and on the DMO website, although the DMO does reserve the right to make an announcement at any time, in relevant circumstances – for example, remit-related announcements made in the wake of the Chancellor's Budget speech and any other public revisions of the public finance forecasts.

92. The interest and redemption payments for all index-linked gilts with first issue dates before 2002 are fixed by the Bank of England. The Bank aims to announce details of these payments by 2:30pm on the day that the relevant value of the General Index of Retail Prices (RPI) is published. The DMO is responsible for fixing and announcing the interest and redemption payments for index-linked gilts first issued from 2002 onwards, and aims to announce details of these payments by 3:30pm on the day that the relevant RPI value is published. On days on which both the Bank and the DMO publish details of index-linked gilt interest or redemption payments, the DMO's announcement will also incorporate details of the payments published by the Bank. In every case, all fixings are published on the DMO website.

9. Freedom of Information

93. Since 1 January 2005, the DMO is, as a 'public authority', subject to the provisions of the Freedom of Information Act 2000, under which any person may make a request seeking information held by the DMO. Upon receipt of such a request, the DMO must balance the legitimate interests of all parties involved against public expectations of accountability, openness and transparency. Legitimate business interests of primary dealers and other third parties may be protected by a series of exemptions within the Act. Whilst the decision to disclose or not rests solely with the DMO, every effort will be made to consult with the source prior to a decision being taken, where third party information is involved. Further information on Freedom of Information may be obtained from the DMO's Dealing Desk or its Information Manager.

Annex. List of DMO information pages

Website

www.dmo.gov.uk

Index and market announcements pages

Thomson Reuters – DMO/INDEX, DMO/GILTS1 *et seq*
Bloomberg – DMO <GO>, DMO1 <GO>

GEMMA reference price pages

Thomson Reuters – 0#GBTSY=GEMM, 0#GBTSYIL=GEMM, 0#GBSTRIP=GEMM
Bloomberg – DMO4 <GO>, DMO5 <GO>, DMO6 <GO>, DMO7 <GO>

Intra-day composite price pages

Thomson Reuters – 0#GBTSY=DMO (conventionals), 0#GBTSYIL=DMO (index-linked),
Bloomberg – DMO2 <GO> (conventionals), DMO3 <GO> (index-linked),

Standing & Special Repos

Thomson Reuters – DMO/REPO01,
Bloomberg – DMO17 <GO>