United Kingdom
Debt Management
Office

DMO Annual Review

2015-16

The United Kingdom
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Contents

Foreword by the DMO Chief Executive

2015-16 saw the DMO successfully deliver its gilt financing programme in financial market conditions that continued to be challenging with market observations of deteriorating liquidity and diminished risk appetite.

The DMO raised £127.7 billion from gilt sales in 2015-16, the eighth consecutive financial year in which gilt sales have exceeded £100 billion and have averaged £162 billion annually over that period. These sales have tripled the size of the gilt portfolio. At the end of 2007-08, at the start of the financial crisis, the overall size of the gilt portfolio was £479 billion, whilst at the end of 2015-16, it was £1,462 billion.

Over the same period, the gilt market has developed significantly in terms of the diversity of its investor base and the primary dealer community – although two primary dealers resigned in 2015-16, reflecting the challenging market conditions in which they, and the DMO, operate.

Auctions remain HM Government's primary and most important means of distributing gilts and they raised £99.5 billion, or 78% of the gilt sales programme in 2015-16. The use of supplementary distribution methods, principally syndications, again facilitated the issuance of long-dated conventional and index-linked gilts, and allowed the DMO to continue targeting its core domestic investor base more directly.

Six syndications were held in 2015-16, raising £26.6 billion. Such was the strength of demand that five of these operations were increased in size above initial planning assumptions and £2.4 billion of funding that had initially been unallocated was moved into the syndication programme to accommodate these increases. Only two gilt mini-tenders were held in 2015-16, raising £1.6 billion. In all, the DMO held 47 gilt financing operations (including 39 auctions), which was one more than in 2014-15.

Despite the challenging backdrop I continue to be impressed by the effectiveness of the gilt market in absorbing these levels of gilt supply. A deep and well functioning gilt market is vitally important for the DMO's delivery of its financing remit.

The DMO again performed strongly in 2015-16 in carrying out its cash management function, with all related objectives met, despite difficult money market conditions in particular affecting liquidity in the repo market.

Strong demand continued for Treasury bills. As with gilts, Treasury bills continued to attract significant overseas investor interest, with 49% of the market being held by such investors at the end of December 2015.

The DMO again successfully provided a cost-effective service to its clients through the fund management operations of the Commissioners for the Reduction of the National Debt. The market value of these funds was £30.2 billion at 31 March 2016.

Looking ahead, the DMO's remit for 2016-17 was published on 16 March 2016; gross gilt sales plans of £129.4 billion were announced, an increase of £1.7 billion compared with 2015-16. No net contribution to financing from Treasury bills is planned for 2016-17. Planned gilt sales rose to £131.5 billion as a result of the publication of the outturn Central Government Net Cash Requirement for 2015-16 on 21 April 2016.

2016-17 also sees the introduction of a package of measures into the financing remit designed to support the delivery of the gilt sales programme by easing pressures on the primary dealer distribution mechanism.

Sir Robert Stheeman
August 2016

Chapter 1: The Economy and Financial Markets

Macroeconomic developments

Global growth was subdued during the financial year despite continued accommodative monetary policy. Following robust domestic GDP growth policymakers in the US increased the upper band of the target federal funds rate 25 basis points (bps) to 50bps in December 2015, but hopes of a sustained and robust global recovery were undermined by renewed concerns over slowing economic growth in China and other emerging economies at the start of 2016. In the euro area, very low/negative inflation coupled with subdued growth led the European Central Bank (ECB) Governing Council to cut its main interest rate by 5bps to 0.0% and expand its programme of asset purchases in March 2016.

As in 2014-15 the falling price of oil was a key factor in global economic activity; this and the downward pressure from lower energy prices resulted in continuing low or negative inflation in many countries. In early May 2015 Brent crude stood at the in-year high of just over $70 per barrel. In January 2016 the level fell below $30 before trending steadily higher to the end of the financial year, finishing around $40.

In the UK, real Gross Domestic Product (GDP) growth was 0.4% in Q1 and Q2 of the financial year, before increasing to a relatively robust rate of 0.7% in Q3. The rate eased back to 0.4% in the final quarter of the financial year. The UK grew by 2.0% in the financial year 2015-16, making the UK the second fastest growing G7 economy behind only the US (2.2%).

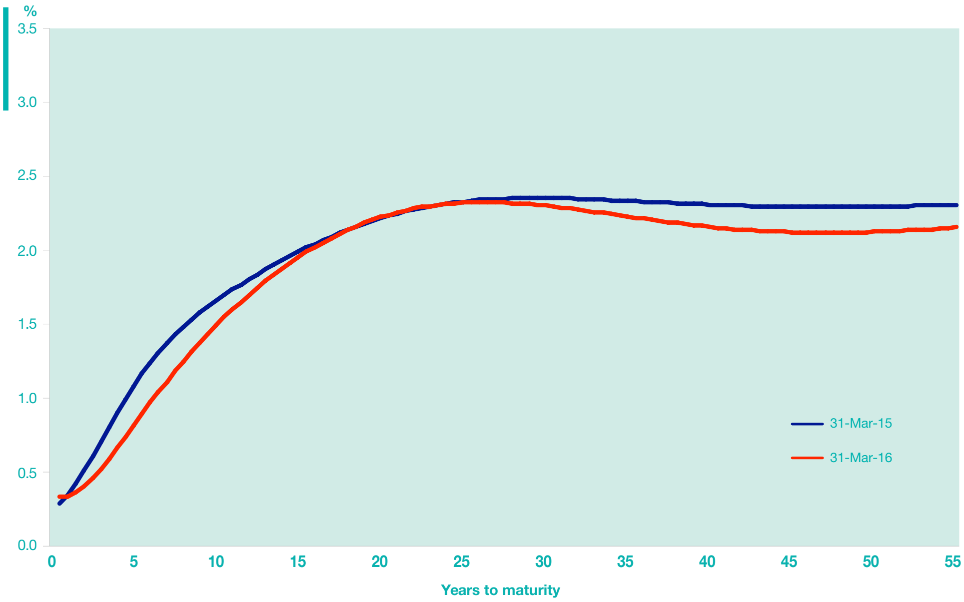
Consumer Prices Index (CPI) inflation was significantly below the Bank of England’s target growth rate of 2.0% year-on-year (y-o-y) throughout the financial year (even falling to a negative level) as falling fuel and food prices depressed overall price growth. Starting at a record low level of -0.1% the rate edged marginally positive in May 2015 before falling back to -0.1% in September and October. From this point the rate rose steadily to a financial year peak of 0.5% in March 2016. The Retail Prices Index (RPI) measure of inflation, which is used to set the cash flows on index-linked gilts, started the financial year at 0.9% y-o-y in April 2015, rising slowly to 1.1% in August before falling back to a financial year low of 0.7% in October. From this point the rate rose steadily to a financial year peak of 1.6% in March 2016.

Gilt market developments

Par gilt yields

Nominal gilt yields fell slightly at the short and long end of the curve in 2015-16, with yields in the 15-30 year area ending the financial year broadly unchanged. Over 2015-16, 2-year yields fell by 10bps to 0.38%, 5-year yields by 27bps to 0.80%, 10-year yields by 17bps to 1.47%, 30-year yields by 5bps to 2.28% and 50-year yields by 17bps to 2.11% (see Chart 1).

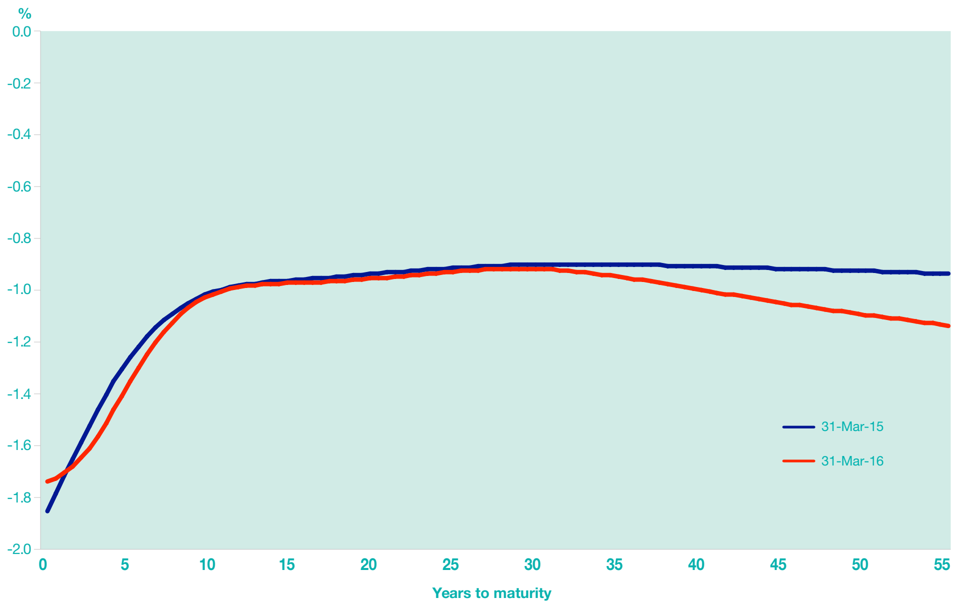
Chart 1: Nominal par yields



Source: DMO

Similarly, real yields were slightly lower y-o-y at the short and longer ends of the curve in 2015-16 with yields in the 10 to 30 year maturity area staying at similar levels. The real yield par curve began to slope downwards at the long end, as yields in the longest maturities fell most. 5-year real par yields fell by 10bps to -1.40%, 10-year real par yields by 1bp to -1.02%, 30-year real par yields by 2bps to -0.91% and 50-year real par yields by 17bps to -1.08%.

Chart 2: Real par yields



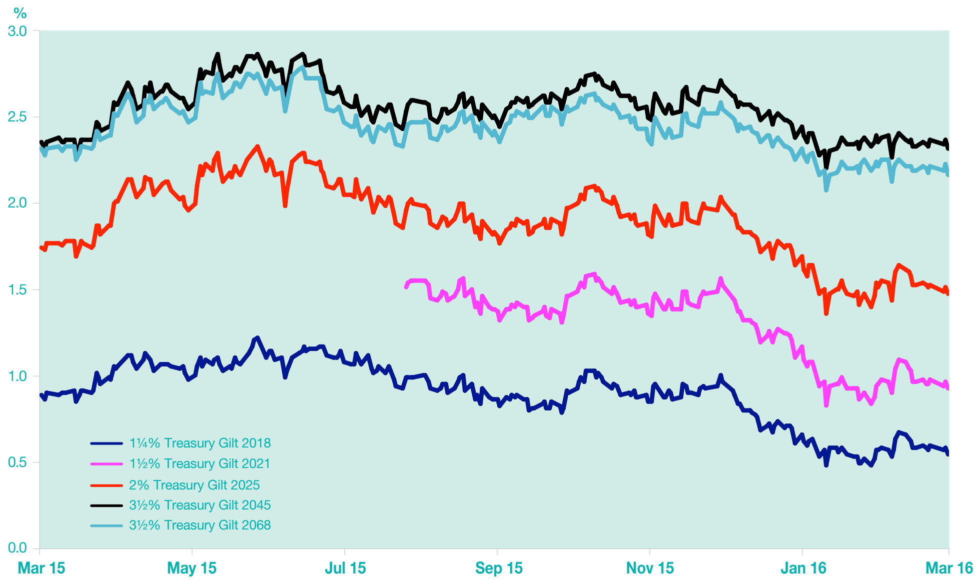
Source: DMO

Nominal yields

Gilt yields began the financial year on an upward trajectory until market volatility caused investors to seek safe havens. The response to the perceived readjustment by China to a more consumer orientated economy, and concerns over corresponding effects on global growth, led gilt and other major bond markets to rally. Renewed reports of slowing rates of growth in China, decade lows in oil prices, other falling commodity prices and disappointing economic data from the US coupled with the announcement of a UK referendum on EU membership further sustained this rally in early 2016.

Gilts were not significantly affected by the Federal Reserve decision to increase the US policy rate by 25bps to 0.50% in December 2015. Shortly after this, renewed concerns over external shocks to growth from China and elsewhere muted market expectations for another rise in the near future. The ECB lowered their policy rate to a historic low of 0.00% towards the end of the financial year.

Chart 3: Nominal yields

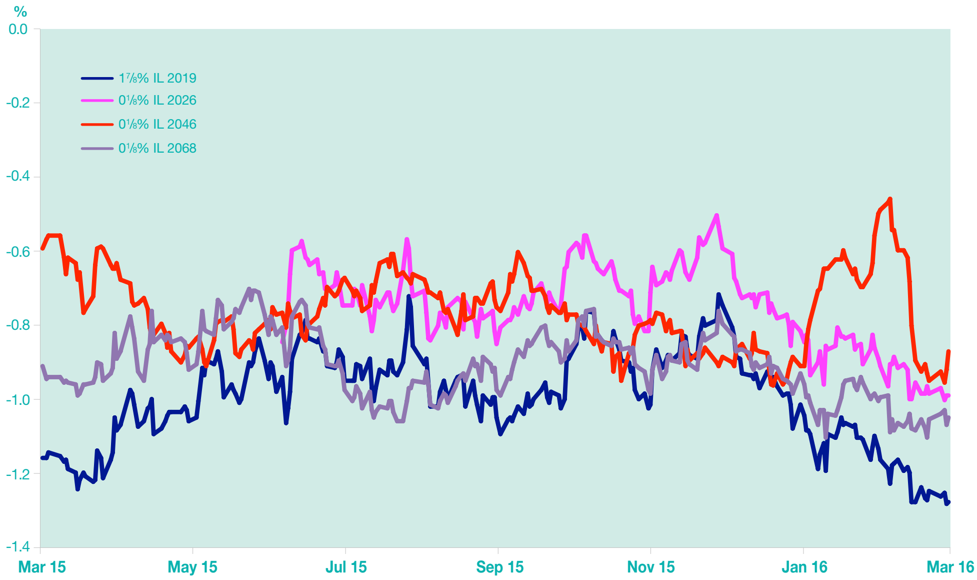


Source: DMO

Real yields

Chart 4 shows the real yields on selected index-linked gilts in 2015-16, all of which fell over the financial year. The real yield on 0% Index-linked Treasury Gilt 2019 fell by 12bps to -1.28%. The real yield on 0% Index-linked Treasury Gilt 2026 fell by 15bps since launch to -1.00%, whilst the real yield on 0% Index-linked Treasury Gilt 2046 fell by 28bps to -0.88% and that on 0% Index-linked Treasury Gilt 2068 by 14bps to -1.05% over 2015-16.

Chart 4:
Real yields

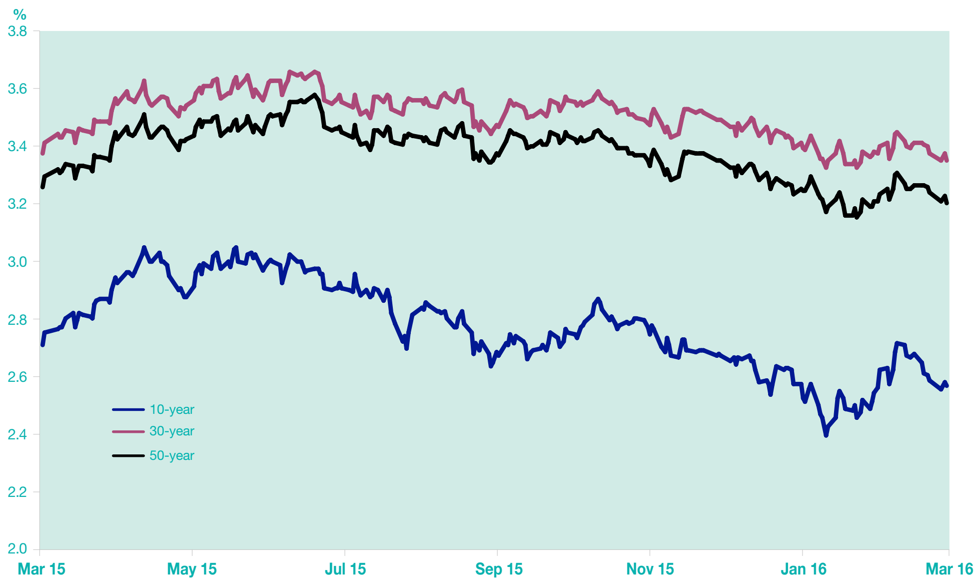


Source: DMO

Break-even inflation rates

For most of 2015-16, index-linked gilts, as measured by break-even inflation rates (BEIRs), underperformed relative to their conventional gilt counterparts, reflecting market expectations that inflation would not pick up again in the near term due to low food and energy prices. This underperformance began to reverse as inflation marginally increased in the final quarter of the year. Over the financial year 10-year BEIRs fell by 14bps (to 2.57%) while 30-year and 50-year BEIRs fell by 3bps (to 3.35%) and 6bps (to 3.20%) respectively (see Chart 5).

Chart 5:
10-, 30- and 50-year break-even inflation rates

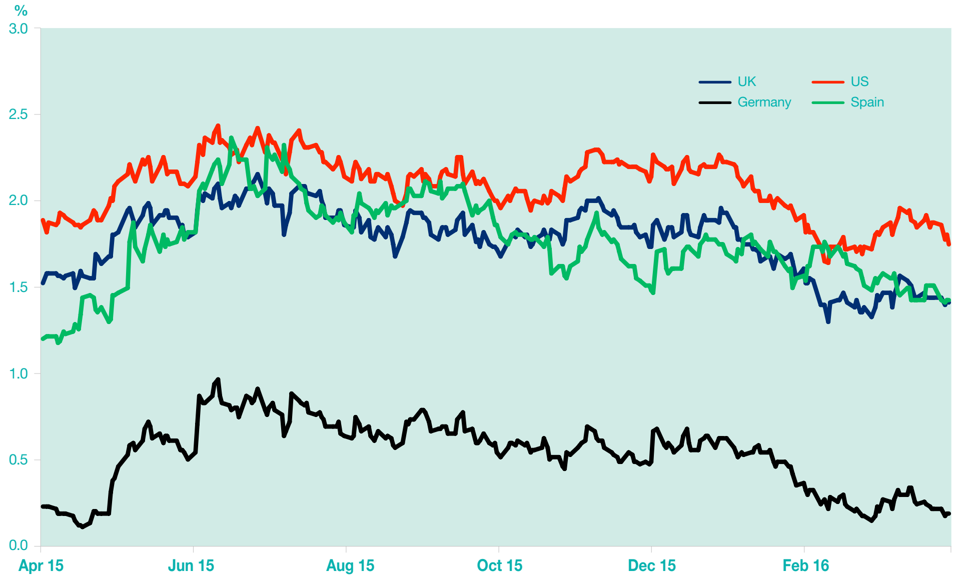


Source: DMO

International comparisons

Yields on 10-year UK, US, German and Spanish government bonds ended the financial year approximately where they started, although all were slightly lower with the exception of Spain. 10-year yields in the UK fell by 13bps relative to the start of the financial year, while in the US they fell by 14bps and in Germany by 4bps. By contrast, 10-year yields in Spain rose by 23bps.

Chart 6: Selected international 10-year benchmark bond yields

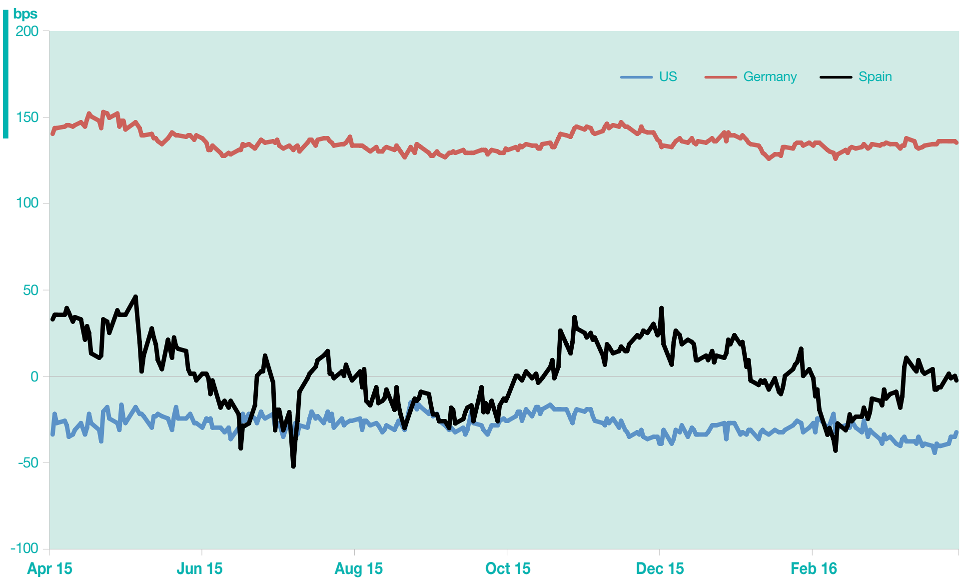


Source: Bloomberg

The spread between 10-year gilt and US treasury yields was relatively stable in 2015-16. At the beginning of the financial year, the spread was -37bps and it had increased marginally to -35bps by the end of the year.

The spread between 10-year gilt and German government bond (Bund) yields also remained range-bound in 2015-16, beginning at +135bps and ending the financial year at +126bps. The comparable spread to Spanish government bonds (obligaciones) behaved similarly, beginning the financial year at +33bps and ending it at -2.2bps.

Chart 7: Selected international 10-year benchmark bond spreads to gilts

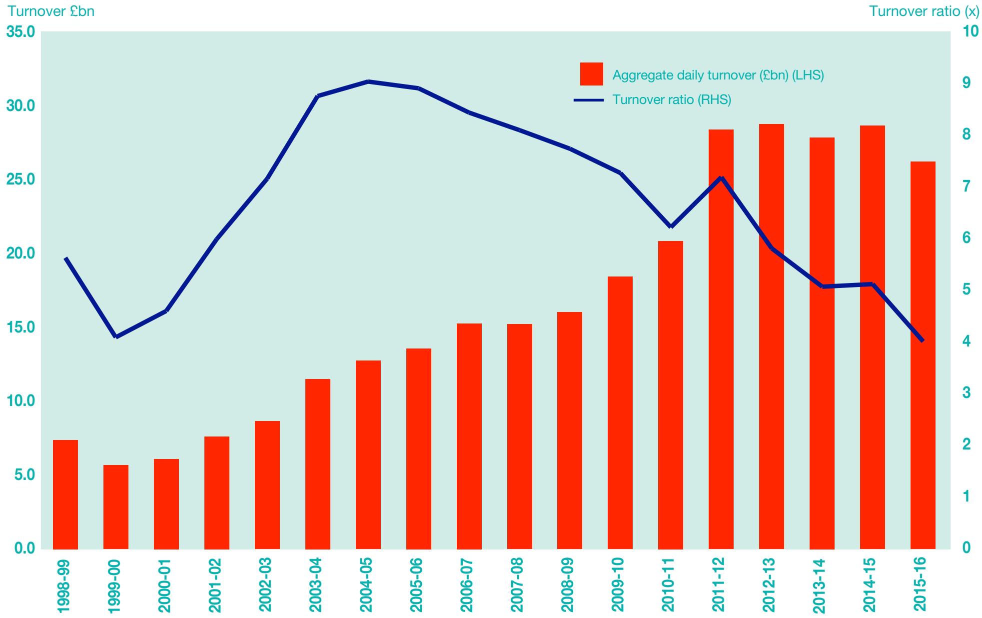


Source: Bloomberg

Gilt market turnover

Aggregate daily turnover in 2015-16 fell by £2.4 billion in 2015-16 compared with the previous financial year (from £28.7 billion to £26.2 billion). Relative to 2014-15, trading intensity (as measured by the turnover ratio[1]) declined significantly from 5.13x to 4.02x (see Chart 8). A number of factors, including evolving regulatory pressures and correspondingly reduced risk appetite from primary dealers could explain this phenomenon.

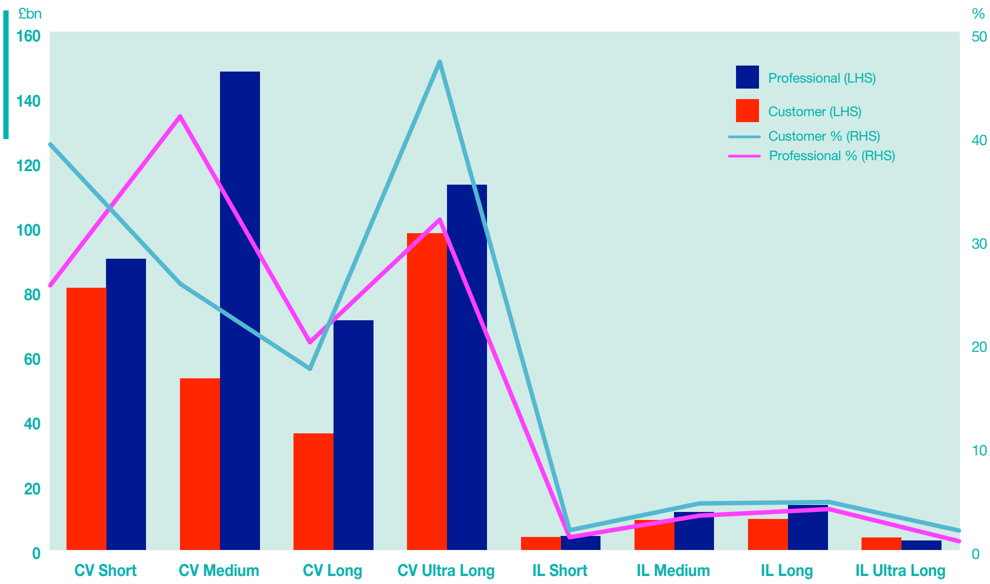
Chart 8: Gilt market turnover



Source: Gilt-edged Market Makers (GEMMs)

As usual, gilt market turnover was heavily weighted towards the short and medium maturity sectors with over 30% in the short and 36% in the medium sectors. Index-linked gilts as a whole accounted for 10.6% of trading.

Chart 9: Gilt market turnover by maturity and type in 2015-16 (nominal)



Source: GEMMs

[1] The turnover ratio for a given year is the aggregate turnover in that financial year relative to the market value of the gilt portfolio at the start of the year.

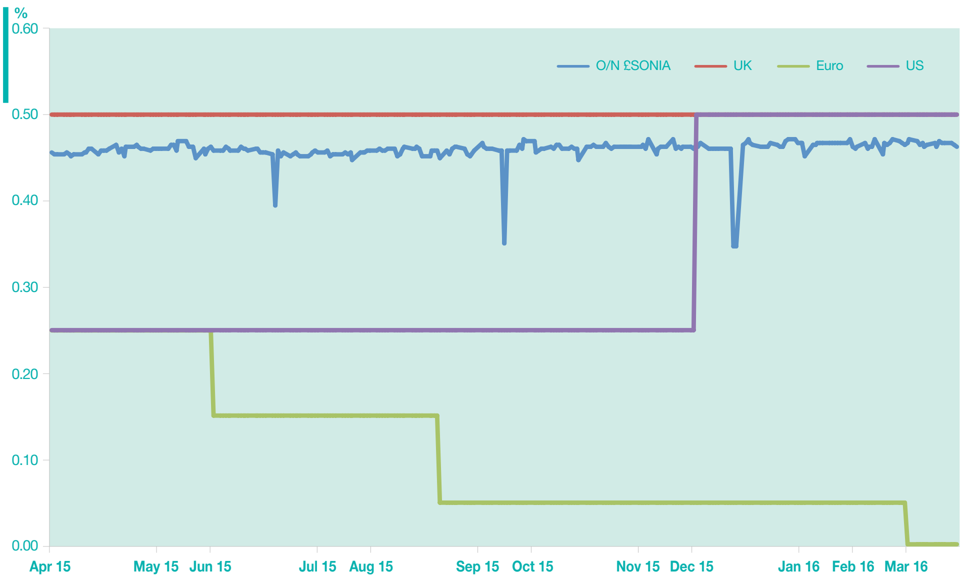
Money market developments

In the UK, the Monetary Policy Committee (MPC) voted to maintain the Bank Rate at 0.50%. It also voted to maintain the stock of asset purchases, financed by the creation of central bank reserves, at £375 billion throughout the financial year. CPI inflation was below the 2% target throughout the financial year, moving around the 0% level in the first half of the financial year before marginally increasing to 0.5% by March 2016. Weakness in inflation continued due to subdued energy and food prices.

The ECB maintained an accommodative monetary policy stance during 2015-16, cutting its policy rate to a historic low of 0% in March 2016 in an effort to stimulate economic activity. The ECB also announced that it will increase the permitted amount of central bank asset purchases from €60 billion to €80 billion per month late in the financial year. These and other measures were intended to incentivise bank lending. The Bank of Japan also unexpectedly introduced a negative official interest rate in January 2016.

By contrast, the Federal Reserve increased the US policy rate by 25bps to 50bps as it judged that signs of recovery in the US economy were sufficient to justify an increase. The Federal Reserve commented that any path to higher rates will be gradual and dependent on economic conditions.

Chart 10: Official interest rates

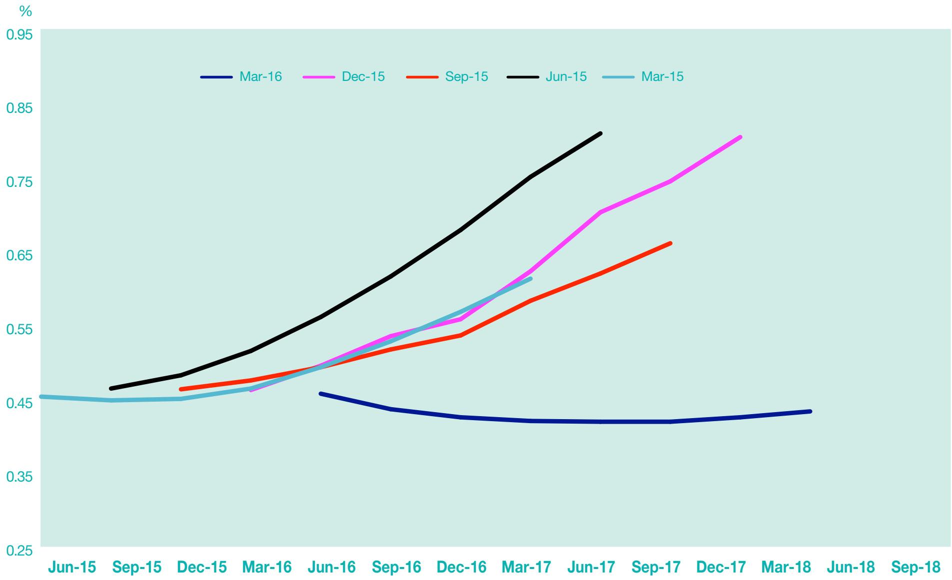


Source: Bloomberg/British Bankers'Association (BBA)

Chart 10 shows the path of the Sterling Overnight Index Average (SONIA) rate in 2015-16. In the UK the spread between SONIA and Bank Rate ranged between -3bps and -15bps (i.e. SONIA remained slightly below Bank Rate) with the spread typically widening at quarter-end when demand for overnight liquidity among UK banks is significantly reduced.

The changing path of future interest rate expectations over the financial year can be seen in the implied yields of short Sterling contracts shown in Chart 11. All the curves ahead of the March 2016 contract show a rise in interest rates was expected in the next financial year; however, the March 2016 contract rates implied no expectation of an increase in rates in the near term.

Chart 11: Implied curves from short Sterling contracts



Source: Bloomberg

Chapter 2: Government Debt Management

Debt management responsibilities and objectives

Objectives of debt management

The UK Government's debt management policy objective is:

"to minimise, over the long term, the costs of meeting the government's financing needs, taking into account risk, while ensuring that debt management policy is consistent with the aims of monetary policy."

The objective is achieved by:

- meeting the principles of openness, transparency and predictability;
- developing a liquid and efficient gilt market;
- issuing gilts that achieve a benchmark premium;
- adjusting the maturity and nature of the government's debt portfolio; and
- offering cost-effective savings instruments to the retail sector through National Savings & Investments (NS&I).

Maturity and composition of debt issuance

In order to determine the maturity and composition of debt issuance, the government needs to take account of a number of factors including:

- the government's own appetite for risk, both nominal and real;
- the shape of both the nominal and real yield curves;
- investors' demand for gilts; and
- changes to the stock of Treasury bills and other short-term debt instruments.

The DMO's financing remit for 2015-16

Budget March 2015

The DMO's financing remit for 2015-16 was published alongside Budget 2015 on 18 March 2015. The DMO's Net Financing Requirement (NFR) was forecast to be £140.4 billion (cash)[2]; this was planned to be financed as follows:

- Outright gilt sales: £133.4 billion
- Net Treasury bill sales (via tenders): £7.0 billion

The gilt financing remit structure

The remit provided that gilt sales were to be split as follows:

- £105.2 billion via 39 auctions
- A minimum of £24.2 billion via six syndications
- £4.0 billion of additional supplementary gilt issuance which could be directed at syndications or mini-tenders, subject to demand.[3]

A breakdown of the initially planned split of gilt issuance in 2015-16 compared with the plans for 2014-15 announced at Budget 2014 are shown in Table 1 below. An initially unallocated portion of supplementary gilt sales was set aside to be used either to increase the size of the syndication programme and/or for sale via mini-tender (subject to demand).

Table 1: The structure of gilt financing remits in 2014-15 and 2015-16 (as initially announced)

	2014-15		2015-16	
	£bn	%	£bn	%
Total	**128.4**		**133.4**	
Short	32.4	25.2%	33.9	25.4%
Medium	26.9	21.0%	26.7	20.0%
Long	33.1	25.8%	37.4	28.0%
Index-linked	31.0	24.1%	31.4	23.5%
Unallocated	5.0	3.9%	4.0	3.0%
Auctions	**106.4**	**82.9%**	**105.2**	**78.9%**
of which				
Short	32.4		33.9	
Medium	26.9		26.7	
Long	24.6		28.1	
Index-linked	22.5		16.5	
Syndications*	**17.0**	**13.2%**	**24.2**	**18.1%**
Long	8.5		9.3	
Index-linked	8.5		14.9	
*Minimum				
Figures may not sum due to rounding				

[2] All reported values are in cash terms unless specified otherwise.
[3] Sales via syndications could only be of long conventional or index-linked gilts; sales via mini-tenders could be of any type or maturity of gilt.

Other operations

There were no plans to hold any switch auctions, reverse auctions or conversion offers in 2015-16 (and none were held).

The 2015-16 remit also provided for the continuation of the Post Auction Option Facility (PAOF), under which successful bidders (GEMMs and investors) at each auction have the option to purchase additional stock of up to 10% of the amount allocated to them at the auction within a two hour window from noon to 2.00pm on the day of the auction.

Outturn of the 2014-15 CGNCR: 22 April 2015

Planned gilt sales were reduced by £2.5 billion to £130.9 billion following the publication of the outturn of the Central Government Net Cash Requirement (CGNCR) on 22 April 2015. There were no changes to planned sales of Treasury bills, which remained at £7.0 billion. The reduction in planned gilt sales was accommodated entirely via the auction programme, resulting in slightly lower average (cash) auction sizes.

The reductions were split as shown in Table 2.

Table 2: Reductions in average auction sales announced at CGNCR outturn

Auctions (£bn)	Reduction	New plans
Short	0.7	33.2
Medium	0.5	26.2
Long	0.7	27.4
Index-linked	0.6	15.9
Totals	**2.5**	**102.7**

The impact on the average (cash) sizes of auctions is shown in Table 3.

Table 3: Reductions in average auction sizes announced at CGNCR outturn

Auction sizes (£bn)	Pre-outturn	Post-outturn
Short	4.25	4.15
Medium	3.34	3.28
Long	2.34	2.27
Index-linked	1.43	1.37

Budget July 2015

Following the change of Government after the 2015 General Election, a Summer Budget was held on 8 July 2015. The DMO's NFR fell by £14.0 billion. Planned gilt sales were reduced by £3.5 billion to £127.4 billion and planned net sales of Treasury bills fell by £10.5 billion to -£3.5 billion. The reduction in planned gilt sales was again accommodated entirely via the auction programme, resulting in further reductions to average (cash) auction sizes.

The revised splits of planned gilt issuance announced at the July Budget remit revision, compared with the plans announced in April 2015 are shown in Table 4.

Table 4:
Planned gilt sales splits April 2015 and July 2015

(£bn)	April	July
Short	33.2	32.3
Medium	26.2	25.4
Long*	36.7	36.8
Index-linked*	30.8	30.2
Unallocated	4.0	2.7
	130.9	127.4
(£bn)	**April**	**July**
Short	25.4%	25.4%
Medium	20.0%	19.9%
Long	28.0%	28.9%
Index-linked	23.5%	23.7%
Unallocated	3.1%	2.1%

*The long and index-linked totals for July include transfers from the initially unallocated programme. £1.0 billion was allocated to a long conventional mini-tender and £0.3 billion was allocated to an index-linked syndication.

The reductions in planned gilt auction totals and the resultant impact on average auction sizes are shown in Table 5.

Table 5:
Reductions in auction sales and average auction sizes announced at the July Budget

Auctions (£bn)	Reduction	New plans
Short	0.9	32.3
Medium	0.8	25.4
Long	0.9	26.5
Index-linked	0.9	15.0
Totals	**3.5**	**99.2**

Autumn Statement (AS) 2015

At AS 2015 on 25 November, the NFR for the DMO rose by £4.5 billion, but there was no change to planned gilt sales. The DMO announced plans to finance the increase entirely by higher Treasury bill sales; consequently planned net Treasury bill sales were revised to +£1.0 billion for 2015-16.

Budget March 2016

The DMO's NFR for 2015-16 fell by £2.1 billion at Budget 2016 compared with AS 2015, reflecting a correspondingly higher contribution to financing by National Savings & Investments (NS&I). In addition, forecast gilt sales for 2015-16, at £127.7 billion, were £0.3 billion higher than forecast at AS 2015. As a result, the forecast size of the DMO's net cash position at end-March 2016 rose by £2.5 billion to £3.0 billion. It was assumed that this £2.5 billion increase will be unwound in 2016-17, correspondingly reducing the NFR in that financial year.

Outturn CGNCR for 2015-16 and the financing outturn

The DMO's NFR for 2015-16 rose by £2.2 billion compared to Budget 2016 primarily reflecting a £2.9 billion increase in the CGNCR and a £0.9 higher contribution to financing from other financing items[4]. As a result, the DMO cash position at end March 2016 fell to £0.9 billion, £2.1 billion lower than forecast at Budget 2016. The DMO cash position will be reduced by £0.4 billion to its planned level of £0.5 billion in 2016-17, reducing the NFR for 2016-17 accordingly.

The developments in the 2015-16 financing arithmetic are shown in Table 6.

Table 6: Updates to the financing arithmetic 2015-16

£ billion	Budget March 2015	2014-15 Outturn	Budget July 2015	Autumn Statement 2015	Budget March 2016	2015-16 Outturn
CGNCR (ex NRAM, B&B and NR)	85.6	85.6	71.6	75.5	75.5	78.4
Gilt redemptions	70.2	70.2	70.2	70.2	70.2	70.2
Planned financing for the reserves	6.0	5.3	5.3	5.3	5.3	5.2
Financing adjustment carried forward from previous financial years	-11.3	-13.1	-13.1	-13.1	-13.1	-13.1
Gross Financing Requirement	**150.6**	**148.1**	**134.1**	**137.9**	**138.0**	**140.8**
Less:						
Contribution from National Savings & Investments	10.0	10.0	10.0	9.3	11.5	11.3
Other financing*	0.2	0.2	0.2	0.2	0.2	1.1
Net Financing Requirement (NFR) for the DMO	**140.4**	**137.9**	**123.9**	**128.4**	**126.2**	**128.4**
Financed by debt issuance:						
a) Gilt sales	**133.4**	**130.9**	**127.4**	**127.4**	**127.7**	**127.7**
of which:						
– Short conventional	33.9	33.2	32.3	32.3	32.6	32.6
– Medium conventional	26.7	26.2	25.4	25.4	25.0	25.0
– Long conventional	37.4	36.7	36.8	37.0	37.2	37.2
– Index-linked	31.4	30.8	30.2	30.7	32.2	32.8
– Unallocated supplementary sales	4.0	4.0	2.7	2.0	0.6	0.0
b) Planned net contribution to financing from Treasury bills	**7.0**	**7.0**	**-3.5**	**1.0**	**1.0**	**1.0**
Total financing	**140.4**	**137.9**	**123.9**	**128.4**	**128.7**	**128.7**
DMO net cash position	0.5	0.5	0.5	0.5	3.0	0.9

Figures may not sum due to rounding.

[4] Other financing items include revenue from coinage, non-governmental deposits, certificates of tax deposit and foreign exchange transactions. There were other minor adjustments to the contribution from NS&I and financing the reserves. Prior to the outturn this item comprises estimated revenue from coinage only.

The DMO's gilt financing operations in 2015-16

New gilts issued

The DMO issued seven new gilts in 2015-16, three conventional and four index-linked gilts. Three of these (the index-linked 2046 and 2065 maturities and a conventional 2065 maturity) were launched via syndication, and the four shorter maturities via auction. The first issue dates of the new gilts are shown in Table 7.

Table 7: New gilts issued in 2015-16

First issue date	Gilt
24-Jun-15	0⅛% Index-linked Treasury Gilt 2046
16-Jul-15	0⅛% Index-linked Treasury Gilt 2026
3-Sep-15	1½% Treasury Gilt 2021
21-Oct-15	2½% Treasury Gilt 2065
18-Feb-16	1½% Treasury Gilt 2026
24-Feb-16	0⅛% Index-linked Treasury Gilt 2065
11-Mar-16	0⅛% Index-linked Treasury Gilt 2036

Implementing the 2015-16 remit

a) Auctions

Auctions continued to be the core of the DMO's gilt sales programme in 2015-16 and, together with associated proceeds from the PAOF, raised £99.5 billion, accounting for 77.9% of overall gilt sales. The auction calendar for the financial year as a whole is usually announced before the start of each financial year, but the choice of gilts to be sold on each date is made quarter-by-quarter following the regular quarterly cycle of consultation meetings with representatives of the GEMMs and end investors. In 2015-16 these meetings also considered the interaction between choices over gilts to be issued via auctions and those at syndicated offerings.

The consultation meetings were held in March 2015 (to discuss issuance in April-June), May 2015 (to discuss issuance in July-September), August 2015 (to discuss issuance in October-December) and December 2015 (to discuss issuance in January-March 2016).

Ahead of the consultation meetings the DMO published an agenda on its wire service screens and website to steer the discussion. The morning after each meeting, summary minutes were published recording the main areas of discussion. The quarterly operations calendars, which specify the particular bonds to be sold at each auction together with advance notice of some of the details of forthcoming syndicated offerings, were published on the last business day of March, May and August and on 4 December 2015 respectively.

39 gilt auctions were held, eight each of short and medium conventional gilts, 12 of long conventional gilts and 11 of index-linked gilts. The results of gilt auctions and other operations are available on the DMO's website at:

http://www.dmo.gov.uk/index.aspx?page=Gilts/Operations_Results

The average cover ratio at gilt auctions in 2015-16 was 1.63x, 12% lower than the average of 1.86x in 2014-15.

The average concentration of bidding at conventional gilt auctions, as measured by the tail[5], remained high, at an average of 0.5 bps, although this represented a marginal deterioration compared with the previous year. Details are shown in Table 8.

Table 8: Auction cover and tail 2014-15 and 2015-16

Gilt auctions	Cover ratio		Tail (bps)	
	2014-15	**2015-16**	2014-15	**2015-16**
Short conventional	1.54	**1.44**	0.4	**1.0**
Medium conventional	1.68	**1.47**	0.3	**0.3**
Long conventional	1.74	**1.62**	0.2	**0.4**
Index-linked	2.20	**1.92**	N/A	**N/A**
All	**1.86**	**1.63**	**0.3**	**0.5**

b) Syndicated offerings

The DMO again used syndications as an integral part of the remit in 2015-16 to supplement auctions and facilitate the primary gilt distribution process. Continued usage of syndications reflected the ongoing historically high level of the financing requirement. In particular, syndications enable the DMO to issue more long conventional and index-linked gilts than it judges would be practicable via auctions alone.

The DMO stated in its remit announcement alongside Budget 2015 that it planned to use the syndication programme to launch new gilts and for re-openings of high duration gilts, with an upfront planning assumption that it would raise a minimum of £24.2 billion via syndication (£9.3 billion of long conventional and £14.9 billion of index-linked gilts).

Subject to market feedback the DMO said that it envisaged holding approximately six syndications (four index-linked and two long conventional), with at least one per quarter. The remit allowed the DMO to vary the size of each syndicated sale having regard to the size and quality of end investor demand in the order book[6].

An outline pattern for the approximate timing of syndications and the scheduling of gilt sales by type in the quarter ahead was discussed at the quarterly consultation meetings in 2015-16 and planning assumptions about the syndication programme were published in the quarterly operations calendar announcements. A greater level of precision is typically given in the announcement about the type and maturity of those sales by syndication planned closest to the date of the calendar announcement. Around two weeks in advance of the anticipated operation, a series of further DMO announcements begin, including the announcement of the appointment of the Lead Managers and the specific maturity of the bond to be sold.

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[5] The tail is the difference in basis points between the yield at the average and lowest accepted prices at multiple price auctions (conventional gilts only).

[6] In the event that proceeds from syndications varied from plan, the mini-tender programme was designed to act as a buffer, with the size of that programme capable of being reduced if syndication sales were higher than plan or increased if syndication sales fell short of plan. In addition, in the event that the balance of sales required to meet either the long conventional or index-linked syndication targets was deemed too small to permit a viably sized final offer (despite any offsetting adjustments to the mini-tender programme), the sizes of the sales targets for long conventional and index-linked gilts could be increased in total by up to 10% of the size of the respective programmes.

£26.6 billion was raised through six syndications in 2015-16 (£9.5 billion of long conventional and £17.0 billion of index-linked gilts). The total raised by the programme was £2.4 billion more than the original plan, reflecting re-allocations into the syndication programme from the mini-tender programme. Five of the six transactions were increased above initial planning (even-flow sized) assumptions to take account of the size and quality of demand received in each case.

The results of the syndication programme in 2015-16 are summarised in Table 9.

Table 9: Syndications in 2015-16

Date	Gilt	Size (£mn nom)	Issue Price (£)	Issue Yield (%)	Proceeds (£mn cash)
23-Jun-2015	0⅛% Index-linked Treasury Gilt 2046	3,250	123.840	-0.582	4,018
21-Jul-2015	3½% Treasury Gilt 2068	4,000	121.310	2.736	4,844
22-Sep-2015	0⅛% Index-linked Treasury Gilt 2068	2,500	166.002	-0.866	4,294
20-Oct-2015	2½% Treasury Gilt 2065	4,750	98.403	2.557	4,663
01-Dec-2015	0⅛% Index-linked Treasury Gilt 2046	3,250	129.738	-0.748	4,240
23 Feb 2016	0⅛% Index-linked Treasury Gilt 2065	2,750	163.728	-0.891	4,496
Figures may not sum due to rounding					**26,557**

As in the previous financial years, strong domestic order books were a feature throughout the 2015-16 syndication programme, with the domestic investor base taking an average of 93% of each sale (marginally up on the 91% figure for 2014-15). Domestic investor orders were largely from asset managers, pension funds and insurance companies, reflecting their structural demand for liability-matching long-dated fixed income assets.

c) Mini-tenders

As in the previous three financial years, all types and maturities of gilt were eligible for sales via the mini-tender programme in 2015-16[7].

Mini-tenders had originally been introduced in 2008-09 to target pockets of demand in specific (long conventional and index-linked) gilts as they emerged in-year. However, over the successive financial years the mini-tender programme evolved so that it increasingly played a supporting role to the syndication programme, with the outturn size of the mini-tender programme being altered to accommodate variances in syndication proceeds. In practice, syndication proceeds in recent years have tended to exceed initial plans and the size of mini-tender programmes has been reduced accordingly.

The 2015-16 remit formalised this arrangement with the scheduling of mini-tenders taking place depending on market demand and the progress of the syndication programme and with the DMO re-stating the prevailing planning assumption of the respective sizes of the syndication and mini-tender programmes after each syndicated offer.

[7] From their introduction in 2008-09 the use of mini-tenders had been confined to sales of long conventional and index-linked gilts. From 2012-13, their potential use was extended to all maturities and types of gilt.

The initial planned size of the mini-tender programme in 2015-16 was £4.0 billion, but this was progressively reduced during the year reflecting re-allocations of sales to the syndication programme. Only two mini-tenders were held in 2015-16 raising £1.7 billion (cash). The results of the two transactions are summarised in Table 10 below.

Table 10: Mini-tenders in 2015-16

Date	Gilt Name	Size (£mn nom)	Cover	Price (£)	Yield (%)	Proceeds (£mn)
4-Jun-15	4¼% Treasury Gilt 2055	750	1.22	136.01	2.766	1,020.0
23-Mar-16	0⅛% Index-linked Treasury Gilt 2068	350	1.44	184.05	-1.077	668.9
						1,688.9

Gilt sales outturn for 2015-16

The outturn for gilt sales in 2015-16 is shown in Table 11. Total gilt sales were £127.7 billion relative to the plan of £127.4 billion.

Table 11: Gilt sales outturns by maturity, type and method of sale

(£mn)	Conventional gilts			Index-linked gilts	Total
	Short	Medium	Long		
Auction proceeds	31,098	24,619	25,277	14,514	95,508
PAOF proceeds	1,512	403	1,438	605	3,957
Auction and PAOF proceeds	**32,610**	**25,022**	**26,715**	**15,119**	**99,465**
Syndication proceeds	0	0	9,508	17,049	26,557
Mini-tender proceeds	0	0	1,020	669	1,689
Total Gilt sales outturn	**32,610**	**25,022**	**37,243**	**32,837**	**127,711**

The outturn for gilt sales against the various remit targets are summarised in Table 12.

Table 12:
Gilt sales outturns relative to remit targets

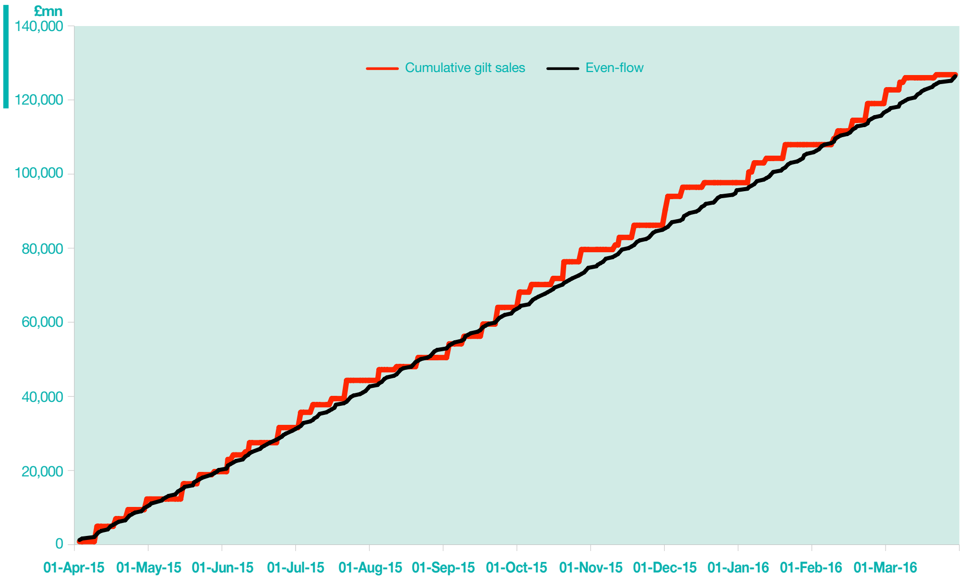
(£mn)	Target	Outturn	Relative to target (£mn)	Relative to target (%)
Total gilt sales	**127,400**	**127,711**	**311**	**0.2%**
Auctions*	**99,200**	**99,465**	**265**	**0.3%**
Short	32,300	32,610	310	1.0%
Medium	25,400	25,022	-378	-1.5%
Long	26,500	26,715	215	0.8%
Index-linked	15,000	15,119	119	0.8%
Syndications**	**26,550**	**26,557**	**7**	**0.0%**
Long	9,500	9,508	8	0.1%
Index-linked	17,050	17,089		0.0%
Mini-tenders**	**1,650**	**1,698**	**39**	**2.4%**

*Auction sales include PAOF proceeds

** Syndication and mini-tender targets are final totals as revised in-year

Gilt sales proceeds were received on a broadly even-flow basis throughout the year as illustrated in Chart 12, which shows cumulative proceeds from all operations including proceeds from the PAOF.

Chart 12:
Gilt sales proceeds even-flow



Source: DMO

Future provision of gilt and Treasury bill reference prices

On 21 January 2015, the DMO announced its strategic intention to withdraw, in due course, from the provision of gilt and Treasury bill reference prices. The DMO held an initial phase of engagement with the market, reporting its findings in two update documents published on 12 March 2015 and 29 May 2015.

On 31 July 2015 it was announced that the government was considering the establishment of a formal and independent process to review the provision of prices and to facilitate the transition to a successor arrangement. Professor David Miles CBE, professor at Imperial College London and former member of the Bank of England's MPC, was appointed on 8 January 2016 to lead the Independent Reference Prices Review ('the Review').

The Review team began meeting with key stakeholders in March 2016, including end users from buy-side firms, GEMMA, trade associations, the Financial Conduct Authority and the Bank of England. The Review team have also met with the firms who had already informed the DMO that they are interested in providing the successor arrangements.

To ensure the whole market has an opportunity to feed into the Review, a consultation document was published on the DMO website on 19 May 2016. The consultation closed on 19 June 2016.

The Review intends to publish an open invitation for potential providers to submit business proposals which the Review team will evaluate over the summer. Taking into account the responses from the consultation, the Review will make clear in the invitation any necessary features of the successor arrangements. The way in which the proposals are assessed will reflect the responses to the consultation.

It is expected that the Review will conclude in September 2016 after delivering its recommendations to HM Treasury ministers.

DMO remit 2016-17 (March 2016 Budget)

The DMO's financing remit for 2016-17 was published alongside the Budget on 16 March 2016. The DMO's NFR for 2016-17 was forecast to be £129.4 billion, to be financed entirely by gilt sales.

The structure of the gilt financing remit

The planned split of gilt issuance was very similar to that in the 2015-16 remit, as announced at Budget 2015 with small downward adjustments to the planned proportion of short and medium sales. The major change was the increase in the size and proportion of unallocated issuance, which was introduced in the context of a wider package of operational changes implemented for the 2016-17 remit – these are summarised in the box on page 24.

The structure of the remits for 2015-16 and 2016-17 both as regards the split of issuance and by type of operation is shown in Table 13. Auctions remain the primary means of sale, accounting for 74% of total planned sales.

Table 13: The structure of financing remits in 2015-16 and 2016-17 (as initially announced)

	2015-16		2016-17	
	£bn	%	£bn	%
Total	**133.4**		**129.4**	
Short	33.9	25.4%	30.4	23.5%
Medium	26.7	20.0%	24.8	19.2%
Long	37.4	28.0%	36.2	28.0%
Index-linked	31.4	23.5%	30.0	23.2%
Unallocated	4.0	3.0%	8.0	6.2%
Auctions	**105.2**	**78.9%**	**95.9**	**74.1%**
of which				
Short	33.9		30.4	
Medium	26.7		24.8	
Long	28.1		26.7	
Index-linked	16.5		14.0	
Syndications*	**24.2**	**18.1%**	**25.5**	**19.7%**
Long	9.3		9.5	
Index-linked	14.9		16.0	
*Minimum				
Figures may not sum due to rounding				

Post Auction Option Facility (PAOF)

In 2016-17 the remit continued to include the facility whereby successful bidders (both primary dealers and investors) have the option to purchase additional stock via the PAOF. In 2016-17, the option was increased from 10% to 15%[8] of the nominal amount allocated to bidders at the average accepted price at conventional gilt auctions and at the clearing (or strike) price at index-linked gilt auctions. The increase in the size of the option was introduced as part of a wider package of measures designed to facilitate remit delivery – see the box on page 24.

The PAOF is available between midday and 2.00pm on the day of an auction and any proceeds raised via the PAOF will count towards remit auction targets and be factored into auction size calculations on an auction-by-auction basis throughout the financial year. All else equal, PAOF proceeds will be used progressively to reduce implied average auction sizes throughout the year. Average auction sizes are re-stated after every auction.

The supplementary distribution programme

- ### Syndications

The remit specified that six syndications were envisaged for 2016-17, aiming to raise a minimum of £25.5 billion (£9.5 billion via two syndications of long conventional gilts and £16.0 billion via four syndications of index-linked gilts).

- ### Gilt tenders

Gilt tenders (for any type and maturity of gilt) may be scheduled after consultation with the market in response to evolving market and demand conditions during the financial year and can be added to the gilt operations calendar with at least seven business days' notice, but can be scheduled at shorter notice as required.

- ### Initially unallocated issuance

A £8.0 billion portion of issuance was initially unallocated regarding type and maturity of gilt and means of sale. This unallocated portion can be used to increase sales of gilts via syndication, to be sold via gilt tenders or to increase the targets for sales via auction. Any such re-allocations will be announced.

Other operations

The remit specified that the DMO has no current plans for a programme of reverse or switch auctions, or conversion offers in 2016-17.

New gilt instruments

The remit specified that there were no current plans to introduce new types of gilt instruments in 2016-17.

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[8] Since the introduction of the facility in June 2010 the option had been for 10% of the amount allocated.

Treasury bill financing

The remit assumes that net Treasury bill sales will not contribute to debt financing in 2016-17, with the implication that the stock of Treasury bills in issue for debt management purposes at the end of March 2017 will be £66.0 billion. Any changes to that assumption will be announced as part of any future remit revision (for example at Autumn Statement 2016). The outturn net contribution of Treasury bills to debt financing in 2016-17 will be reported by the DMO in April 2017.

Package of measures introduced for the 2016-17 Remit

In the 2016-17 remit announcement the DMO set out a package of operational measures, summarised below. The package is intended to support a smooth delivery of the remit in changing market conditions. Individually the changes are relatively minor but, taken together, the package was designed to have an important positive effect on the primary dealer system while remaining in accordance with the DMO's long-standing principles of predictability and transparency.

1. Smaller auctions: The DMO is holding smaller auctions in 2016-17 compared with 2015-16, particularly in short and medium conventional gilts, which were initially some 35% and 26% smaller respectively compared with 2015-16. The objective is to reduce the amount of gilts the market is asked to absorb at each individual auction in order to ease the pressure on intermediation.

2. A larger unallocated portion of issuance: The remit sets out an initially unallocated portion of issuance of £8.0 billion, which may be allocated during the year to any maturity or type of gilt and sold via any issuance method. The primary intention is to support a more active programme of gilt tenders (see below), as well as potentially increasing the syndication programme, but it can also be used to top-up gilt auction targets. The unallocated portion of issuance is intended to permit more responsiveness to changing market and demand conditions during the year. Depending on the allocation of this portion during the year, the outturn split of gilt issuance may differ at the margin from initial planning assumptions.

3. The introduction of gilt tenders: Gilt tenders have replaced mini-tenders and will also encompass the role of the tap facility for market management purposes. In their role as replacement for mini-tenders, gilt tenders will be used for issuance alongside the auction programme, although they will be scheduled with less notice than auctions. Gilt tenders may be for any maturity and type of gilt and will generally be smaller than auctions of comparable gilts; they may also be used for market management purposes. Full terms are set out in the Gilt Market Operational Notice[9].

4. A more flexible syndication programme: The initial planning assumption for the 2016-17 syndication programme is that it will be used to issue long conventional and index-linked gilts. However, should the DMO judge that market and demand conditions so warrant, it may schedule syndications of short and/or medium conventional gilts.

[9] The DMO's gilt market operational notice can be found at:
http://www.dmo.gov.uk/index.aspx?page=Gilts/Operational_Rules

5. A more responsive auction calendar: The planned gilt auction calendar may also be changed on a quarterly basis, if deemed necessary, following consultation with the market. Any change(s) to the planned auction calendar for the forthcoming quarter would be set out as part of the quarterly issuance announcement. The reasons for any change(s) to the auction calendar may include an alteration to the assumed mix of issuance methods to deliver the planned financing in the relevant quarter.

6. The Post Auction Option Facility (PAOF) rate increased from 10% to 15%: All successful direct bidders are offered the right to purchase up to 15% of the nominal amount of gilts they were allotted at the relevant auction at the published average accepted price in multiple price format auctions, or, in auctions of uniform price format, at the published strike price.

7. GEMM non-competitive bid allowance increased from 10% to 15%: GEMMs are entitled to a share of a non-competitive allowance of 15% of the total nominal amount of the gilts on offer at auctions, at the average accepted/strike price of the auction.

Future gross financing projections

The Budget in March 2016 included new projections for the CGNCR as a percentage of GDP to the financial year 2020-21. Table 14 sets out the resulting CGNCR projections in cash terms together with current redemption totals to produce illustrative gross financing projections. Note that these are not gilt sales forecasts, as they take no account of possible contributions to financing by NS&I or net Treasury bill sales for debt management purposes.

Table 14: 2016 Budget: illustrative gross financing requirement projections

(£bn)	2017-18	2018-19	2019-20	2020-21
CGNCR (ex NRAM, B&B and NR)	41.0	32.3	3.0	17.0
Gilt redemptions	79.5	67.3	93.2	85.2
Planned financing for the reserves	6.0	6.0	6.0	0.0
Illustrative gross financing requirement	**126.5**	**105.5**	**102.2**	**102.3**

Figures may not sum due to rounding.

In-year revisions to the remit

There are two main events which may routinely be expected to trigger revisions to the remit in any financial year:

- the publication, usually in the third week of April, of an outturn CGNCR for the previous financial year, if the outturn differs from the forecast published in the Budget; and/or
- the publication, in the Autumn Statement (usually in the November-December period), of a different forecast financing requirement for the prevailing financial year.

2015-16 CGNCR outturn revision to the 2016-17 financing remit

The outturn CGNCR for 2015-16 was published on 21 April 2016 and, as a consequence, the NFR for the DMO in 2016-17 rose by £2.1 billion to £131.5 billion (to be financed exclusively by gilt sales). The increase was financed by additional planned gilt sales at auctions – split as shown in Table 15 below:

Table 15: Increases to gilt sales at auctions announced on 21 April 2016

Gilt auctions (£mn)	New totals	Increase
Short	31,000	600
Medium	25,200	400
Long	27,300	600
Index-linked	14,500	500
	98,000	**2,100**

Chapter 3: Exchequer Cash Management

Exchequer cash management remit 2015-16

The DMO's cash management remit for 2015-16, published alongside the Budget on 18 March 2015, specified that the government's cash management objective is:

> "to ensure that sufficient funds are always available to meet any net daily central government cash shortfall and, on any day when there is a net cash surplus, to ensure this is used to best advantage".

HM Treasury and the DMO work together to achieve this, with HM Treasury providing information to the DMO about flows into and out of the National Loans Fund (NLF) and the DMO making arrangements for funding and for placing net cash positions, primarily by carrying out market operations on the basis of HM Treasury forecasts.

The DMO's cash management objective

The remit specifies that the DMO's cash management objective is:

> "to minimise the cost of offsetting the government's net cash flows over time, while operating to a risk appetite approved by ministers. In so doing, the DMO will seek to avoid actions or arrangements that would:
>
> - undermine the efficient functioning of the Sterling money markets; or
> - conflict with the operational requirements of the Bank of England for monetary policy implementation"

Instruments and operations used in Exchequer cash management

In 2015-16 the DMO carried out its cash management objective primarily through a combination of:

- bilateral market operations with DMO counterparties; and
- Treasury bill sales.

The average accepted yields achieved at the weekly Treasury bill tenders are assessed against the SONIA rates for the relevant maturities. These are reported in Annex B.

Variations in the stock of Treasury bills sold to market participants serve as a financing instrument within short-term debt sales. In 2015-16, Treasury bill sales contributed £1.0 billion to debt financing. Table 10 shows the split of issuance of Treasury bills by maturity at tenders over the course of the financial year.

Bilateral Treasury bill facility

Since November 2007, the DMO has had access to a facility which allows it to re-open existing Treasury bills and issue them on a bilateral basis, on request from its cash management counterparties (provided that such issuance is consistent with the DMO's cash management operational requirements). In particular, Treasury bills sold through the bilateral facility can contribute to smoothing cumulative cash positions. Monthly issuance of Treasury bills via the bilateral facility is shown in the "Other issuance" category in Table 16[10].

Table 16: Treasury bill issuance (gross value) in 2015-16

Month	One month (£mn)	Three month (£mn)	Six month (£mn)	Other issuance (£mn)	Total issuance (£mn)	Total stock outstanding (£mn)
Apr-15	2,000	5,000	6,000	255	13,255	62,072
May-15	4,500	6,000	8,000	416	18,916	66,651
Jun-15	9,500	6,500	10,000	1,257	27,257	71,290
Jul-15	2,000	6,000	8,000	393	16,393	68,094
Aug-15	4,500	5,000	8,000	164	17,664	71,171
Sep-15	10,000	3,500	10,000	1,544	25,044	73,614
Oct-15	2,750	7,000	8,000	291	18,041	70,512
Nov-15	2,000	12,500	9,000	848	24,348	76,156
Dec-15	4,500	9,000	6,500	953	20,953	82,765
Jan-16	6,750	5,750	4,750	1,949	19,199	81,695
Feb-16	5,500	10,000	9,500	2,278	27,278	76,545
Mar-16	4,500	6,000	7,500	5,809	23,809	78,317

The breakdown of the Treasury bill portfolio (including amounts issued bilaterally) at end-March 2016 is shown in Table 17.

Table 17: Treasury bills outstanding at 31 March 2016

Maturity date	Size (£mn)	Maturity date	Size (£mn)
4-Apr-16	5,670	4-Jul-16	256
11-Apr-16	5,891	11-Jul-16	1,500
18-Apr-16	8,943	18-Jul-16	1,523
25-Apr-16	4,300	25-Jul-16	1,500
3-May-16	3,500	1-Aug-16	1,500
9-May-16	3,500	8-Aug-16	2,000
16-May-16	4,000	15-Aug-16	2,003
23-May-16	4,100	22-Aug-16	2,000
31-May-16	4,000	30-Aug-16	2,000
6-Jun-16	3,500	5-Sep-16	1,501
13-Jun-16	3,010	12-Sep-16	2,000
20-Jun-16	3,121	19-Sep-16	2,000
27-Jun-16	3,000	26-Sep-16	2,000
Total			**78,317**

[10] From 2013-14 onwards Treasury bills sold bilaterally (i.e. for cash management purposes), are excluded from the end-year stock of Treasury bills reported in the financial arithmetic and thus are excluded from the contribution of Treasury bills to financing.

Bilateral cash management operations

In practice, a significant portion of cash management operations in 2015-16, as in previous years, were negotiated bilaterally by the DMO with market counterparties. To ensure competitive pricing, the DMO maintains relations with a wide range of money market counterparties with whom it transacts both directly and via voice and electronic brokers.

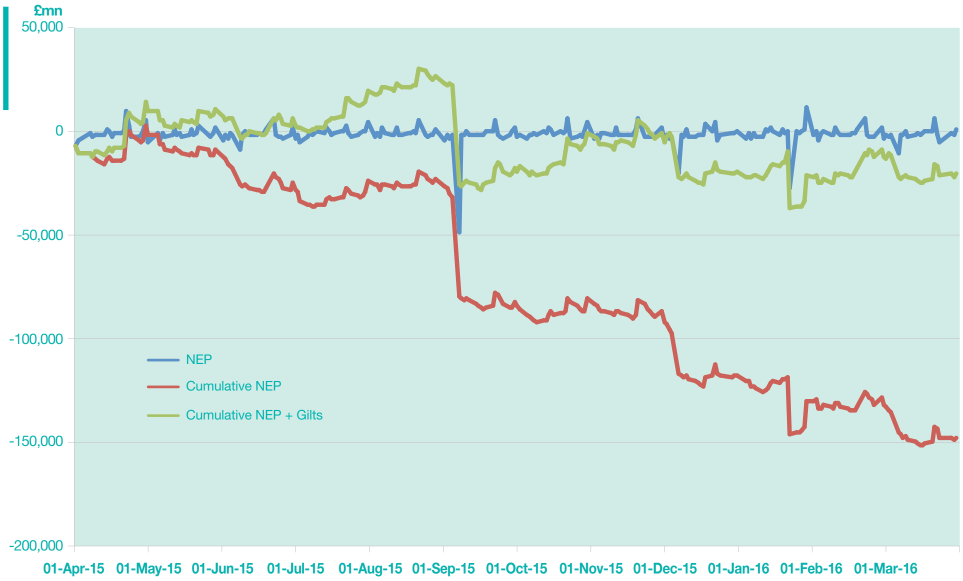
Cash management is conducted using market instruments in order to minimise cost whilst operating within agreed risk limits. Sterling-denominated repurchase agreements (repo) and reverse repurchase agreements currently dominate these transactions, though short-dated cash bonds, certificates of deposit, commercial paper, reverse repo of foreign currency bonds swapped into Sterling, and unsecured loans and deposits can also be used.

The DMO's money market dealers borrow from or lend to the market on each business day to balance the position on the NLF. In order to do so the DMO receives from HM Treasury forecasts of each business day's significant cash flows into and out of central government. Additionally, the DMO obtains up-to-date intra-day monitoring of cash flows as they occur. The DMO trades only with the purpose of offsetting current and forecast future government cash flows, subject to the agreed risk limits. The DMO does not take interest rate positions, except in so far as that is necessary to offset forecast future cash flows.

Over the course of a financial year, the Exchequer's cash flow has typically had a fairly regular and predictable pattern associated with the tax receipts and expenditure cycles. Outflows associated with gilt coupons and redemptions are also known in advance.

Chart 13 shows the scale of daily cash flows measured in terms of the Net Exchequer Position (NEP) in 2015-16 on a daily and cumulative basis. The NEP excludes the effects of gilt sales, Treasury bill issuance and NS&I's overall net contribution to financing, and therefore shows the cumulative in-year deficit which has to be financed. The chart also shows the net effect including gilt sales demonstrating how the timing of these make a significant contribution to reducing the in-year financing required by Exchequer cash management operations.

Chart 13: Exchequer cash flows 2015–16



Source: HM Treasury/DMO

Active cash management performance framework

Since 2000, the in-year cash needs of the government have been managed actively by HM Treasury and the DMO with HM Treasury providing short and medium-term forecasts of daily net cash surpluses and deficits and the DMO transacting with its market counterparties in a variety of instruments at a range of different maturities to offset the current and forecast future cumulative net cash position.

This active cash management framework is designed to allow specialist cash managers to select appropriate counterparties, instruments and maturities with which to deliver the cash management remit at minimum cost subject to the agreed risk limits. Formal performance reporting is in place as a means of enhancing effectiveness and ensuring accountability and the results for 2015-16 are presented in Annex B. HM Treasury and the DMO recognise that performance measurement needs to capture the wider policy objectives the government sets the DMO as its cash manager as well as the cost minimisation objective and for this reason a number of key performance indicators are used including a quantifiable measure of net interest saving which is shown under key performance indicator (KPI) 1.4.

HM Treasury and the DMO equally recognise that to measure performance solely in terms of net interest savings is a somewhat narrow interpretation that does not fully capture the ethos or the wider policy objectives the government sets the DMO as its cash manager. Exchequer cash management differs from that of a commercial entity in that it does not seek to maximise profits, but rather to minimise costs subject to risk while playing no role in the determination of Sterling interest rates. Consequently the DMO and HM Treasury monitor and assess overall performance in meeting the government's objectives using a number of quantitative and qualitative KPIs and controls. A full report on performance in 2015-16 is presented in Annex B.

Chapter 4: Fund Management

Fund management

The origins of the Commissioners for the Reduction of the National Debt (CRND) date back to the passing of the National Debt Reduction Act of 1786. From their earliest days the Commissioners also had associations with the stock market and this led to a diversification of CRND operations, including in particular responsibility for the investment of major government funds. This now constitutes the main function of CRND, which since 2002 has been carried out under the auspices of the DMO.

CRND had £30.2 billion under management at end-March 2016, representing the assets of the various investment accounts. The Commissioners themselves had not officially met in this capacity since 1860, but, in February 2016, the Chancellor of the Exchequer hosted a meeting, at which the DMO's Chief Executive was officially appointed as the Government Broker, a formal title, which was up until 1986 conferred on the senior partner of the stockbrokers Mullens & Co.

The investment powers differ to some extent from fund to fund, depending upon the provisions of the relevant Acts of Parliament or risk profiles agreed with fund owners, but essentially investments are restricted to cash deposits or government-issued and government-guaranteed securities. Currently, the largest funds are the National Insurance Fund Investment Account, the Court Funds Investment Account and the National Lottery Distribution Fund Investment Account. The main funds under CRND management at end-March 2016 were as follows:

- National Insurance Fund Investment Account
- Court Funds Investment Account
- National Lottery Distribution Fund Investment Account
- Northern Ireland National Insurance Fund Investment Account
- Insolvency Services Investment Account
- Northern Ireland Court Service Investment Account
- Various smaller legacy administrative accounts, including the Donations and Bequests Account, which processes any gifts to the nation for the purpose of debt reduction.

CRND continues to provide an efficient, value for money service, with the main investment objectives being to maintain sufficient liquidity to meet withdrawals and to protect the capital value of the funds under management.

Annexes:

A) List of GEMMs and Inter Dealer Brokers (IDBs) at 31 March 2016

B) Debt and cash management performance

C) The gilt portfolio

ANNEX A: List of GEMMs and IDBs at 31 March 2016

All are market-makers in both conventional and index-linked gilts.

Gilt-edged Market Makers

Website

BofA Merrill Lynch
Financial Centre
2 King Edward Street
London
EC1A 1HQ
www.baml.com

Barclays Bank plc^
5 The North Colonnade
Canary Wharf
London
E14 4BB
www.barclays.com

BNP Paribas (London Branch)
10 Harewood Avenue
London
NW1 6AA
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Citigroup Global Markets Limited
Citigroup Centre
33 Canada Square
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E14 5LB
www.citigroup.com

Deutsche Bank AG (London Branch)
Winchester House
1 Great Winchester Street
London
EC2N 2DB
https://gm-secure.db.com

Goldman Sachs International Bank
Peterborough Court
133 Fleet Street
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EC4A 2BB
www.gs.com

HSBC Bank PLC^
8 Canada Square
London
E14 5HQ
www.hsbcgroup.com

Jefferies International Limited*
Vintners Place
68 Upper Thames Street
London
EC4V 3BJ
www.jefferies.com

JP Morgan Securities PLC
25 Bank Street
Canary Wharf
London
E14 5JP
www.jpmorgan.com

Lloyds Bank plc
25 Gresham Street
London
EC2V 7AE
www.lloydsbankcommercial.com

Morgan Stanley & Co. International plc
20 Cabot Square
Canary Wharf
London
E14 4QW
www.morganstanley.com

Nomura International plc
One Angel Lane
London
EC4R 3AB
www.nomura.com

Royal Bank of Canada Europe Limited
Thames Court
One Queenhithe
London
EC4V 4DE
www.rbccm.com

Royal Bank of Scotland^
135 Bishopsgate
London
EC2M 3UR
www.rbsmarkets.com

Santander Global Banking & Markets UK
2 Triton Square
Regent's Place
London
NW1 3AN
www.santander.com

Scotiabank Europe plc
201 Bishopsgate
London
EC2M 3NS
www.scotiabank.com

The Toronto-Dominion Bank (London Branch)*
60 Threadneedle Street
London
EC2R 8AP
www.td.com

UBS Limited
1 Finsbury Avenue
London
EC2M 2PP
www.ubs.com/investmentbank/

Winterflood Securities Limited*^ www.wins.co.uk
The Atrium Building
Cannon Bridge
25 Dowgate Hill
London EC4R 2GA

* Retail GEMM
^ Strips market participant

Inter Dealer Brokers

BGC Brokers L.P. www.bgcpartners.com
One Churchill Place
Canary Wharf
London
E14 5RD

BrokerTec Europe Limited www.icap.com
2 Broadgate
London
EC2M 7UR

Dowgate www.ksbb.com
6th Floor
Candlewick House
120 Cannon Street
London
EC4N 6AS

GFI Securities www.gfigroup.com
1 Snowden Street
London
EC2A 2DQ

ICAP WCLK Limited www.icap.com
2 Broadgate
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EC2M 7UR

Tullett Prebon Gilts www.tulletprebon.com
155 Bishopsgate
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ANNEX B: Debt and cash management performance

This Annex includes data on the DMO's performance in execution of the gilt financing and Exchequer cash management remits in 2015-16.

The gilt data compare the actual cost of gilt issuance (measured by the average yield at which gilts were sold in accordance with the DMO's financing remit) with illustrative counterfactual costs of different patterns of gilt financing. It also looks at the performance of gilt auctions by comparing the average accepted/strike price of an auction with prevailing secondary market price levels.

Table 8 on page 18 of this Review reports on the average cover ratios at all gilt auctions in 2015-16 and on the concentration of bidding (the tail) at conventional gilt auctions.

The cash management material comprises a formal report on compliance with the DMO's published Key Performance Indicators (KPIs) in respect of Exchequer cash management and a comparison of the average yields achieved at weekly Treasury bill tenders with the prevailing SONIA rate for comparable maturities.

Other aspects of the DMO's performance each financial year are reported in the DMO's Annual Report and Accounts[11]. These comprise (page references refer to the 2015-16 Accounts published on 13 July 2016):

- A review of the DMO's main activities (pages 16-19);
- A report on achievements against agency objectives as set by HM Treasury (pages 22-23);
- A report on performance against agency targets (pages 24-27), including:
  - Compliance with the financing remit
  - Gilt and Treasury bill operation results – release times
  - Accuracy of the recording of transactions through the Debt Management Account
  - Compliance with the Freedom of Information Act 2000
  - Avoidance of breaches of operational notices
  - Compliance with the schedule for reporting cash management operational balances
  - Accurate and timely administration of settlement procedures
  - Accuracy of publications and timeliness of announcements
  - Timeliness of processing of local authority loan and early repayment applications
  - Appropriate operation of the DMO (retail) gilt purchase and sales service
  - Appropriate administration of the National Loan Guarantee Scheme.

[11] The Annual Report and Accounts for 2015-16 are available at: http://www.dmo.gov.uk/documentview.aspx?docname=publications/annualreports/dmodmarep2016.pdf&page=Annual_Report

a) Gilt issuance counterfactuals

Since 2001 the DMO has published in its Annual Reviews the results of its measurement of relative performance of outright issuance in each financial year against counterfactuals. Although the UK's debt management objective is concerned with minimising the cost of issuance "over the long term" rather than in any one year, the intention here is to illustrate whether different non-discretionary issuance patterns during a particular year could have resulted in higher or lower costs of financing.

The calculations compare the cash weighted yield of actual issuance with the yield on various counterfactual issuance patterns but on the basis of a key assumption that the different issuance patterns modelled would not have impacted the levels of yields relative to those achieved in practice (see below).

There are a number of limitations to this analysis. In particular, a major assumption that is unlikely to hold in practice is that the shape of the yield curve remains fixed over time. This is particularly relevant when considering the refinancing timeframes associated with different maturities of debt (i.e. short issuance needs to be refinanced much more frequently than long issuance) so this analysis is not comparing like-for-like in this regard. In principle, therefore, if yields evolve as reflected by the forward yield curve it would be too simplistic to say that in any one year one issuance pattern has outperformed another.

Another relevant assumption is that the counterfactual issuance patterns themselves would not have had any impact on yields. This is unlikely to hold in practice particularly where the gilt issuance pattern under the counterfactual is significantly different from actual issuance (e.g. a heavy skew to a certain maturity). Whilst it is likely, certainly over the medium to longer-term, that the greatest influences on the level of yields will be macro-economic conditions, market expectations of interest rates, and other external factors over which the debt manager has no control, establishing the extent to which changes in volumes and patterns of supply might affect yields is more difficult.

The underlying rationale for considering issuance performance against counterfactuals is that it provides one means by which to analyse the performance of the debt management authorities in achieving the debt management objective, in particular regarding the decisions on the split between maturities/types of gilt sold in a given year. It is worth noting in this context that measuring performance against the primary debt management objective is not straightforward, a fact widely acknowledged by many other sovereign debt managers. Hence, presentation of annual counterfactuals should not be interpreted as a complete or authoritative means by which to test achievement against the debt management objective – which as noted above is a long-term test.

For these reasons, caution is required when interpreting the yield impact of counterfactual issuance patterns set out in this annex in comparison with the actual issuance yield. The cash weighted average yield of actual issuance at the gilt auctions, syndicated offerings and mini-tenders in 2015-16 was 1.978%[12] (42.9bps lower than the 2.407% in the previous financial year). The cash weighted average yield of issuance by type of gilt and maturity is shown in Table B1.

[12] Index-linked real yields have been converted to nominal equivalents, assuming 3% RPI inflation.

Table B1: Average issuance yield by type and maturity of gilt 2015-16

	Cash (£mn)	Yield (%)
All issuance	**127,711**	**1.978**
Conventional		
Short	32,610	1.290
Medium	25,022	1.888
Long	37,243	2.506
Total conventional	**94,874**	**1.925**
Index-linked		
Medium	5,936	2.200
Long	26,901	2.159
Total Index-linked	**32,837**	**2.167**

The actual yield of 1.978% can be compared with yields derived by applying the actual annual cash weighted yield of different maturities/types of gilt to different gilt issuance patterns. Table B2 contrasts the actual average issuance yield in 2015-16 with three counterfactuals which assume the same yields by maturity and type as shown above, but with alternative issuance skews, namely:

- a significantly greater skew towards short issuance;
- a completely even-distribution approach to financing; and
- a significantly greater skew towards long issuance.

Table B2: Illustrative average issuance yields assuming different issuance patterns

Issuance splits	Actual	Skew short	Neutral	Skew long
Short	25.5%	50.0%	25.0%	12.5%
Medium	19.6%	15.0%	25.0%	12.5%
Long	29.2%	15.0%	25.0%	50.0%
Index-linked	25.7%	20.0%	25.0%	25.0%
Average yield (%)	**1.978**	**1.737**	**1.936**	**2.192**
Difference v actual (bps)		**-24.05**	**-1.53**	**21.40**

The neutral approach to financing by maturity produces an average yield of issuance very close to actual (just 1.5bps lower). The skews much longer and shorter both produce implied yields significantly different from the actual (-24.1bps in the case of the shorter option and +21.4bps in the case of the longer). This is to be as expected, given that the yield curve was upward sloping yield curve in the period.

The results from counterfactual modelling of this kind need to be considered in the context of an objective that requires the DMO (and many other sovereign issuers with similar objectives) to pursue policies designed to minimise long-term cost whilst taking account of the risks to which debt issuance exposes the Exchequer – i.e. the DMO does not seek exclusively to minimise yield at the expense of other considerations. In order to determine the maturity and composition of debt issuance, the government takes into account a number of factors including:

- the government's own appetite for risk, both nominal and real;
- the shape of both the nominal and real yield curves; and
- investors' demand for gilts.

b) Auction concession analysis

There are a number of ways to measure auction concessions. The method presented in Table B3 shows the extent of any concession/premium at auctions by measuring the difference between the actual proceeds received and those that would have been generated had each gilt at auction been priced at the secondary market price at the close of bidding.

Table B3: Concession (-) and premium (+) at gilt auctions in 2015-16

Date	Gilt	£ million
8-Apr-15	2% Treasury 2020	0.72
16-Apr-15	0⅝% IL 2040	-1.72
21-Apr-15	3½% Treasury 2045	2.28
29-Apr-15	2% Treasury 2025	0.99
14-May-15	2% Treasury 2020	0.94
21-May-15	4¾% Treasury 2030	1.26
27-May-15	0⅛% IL 2058	7.14
2-Jun-15	2% Treasury 2025	0.03
9-Jun-15	0⅛% IL 2024	2.70
11-Jun-15	3½% Treasury 2045	2.26
2-Jul-15	2% Treasury 2020	1.13
7-Jul-15	3½% Treasury 2045	1.12
15-Jul-15	0⅛% IL 2026	2.87
4-Aug-15	2% Treasury 2025	1.17
11-Aug-15	0⅛% IL 2058	-0.90
20-Aug-15	4¼%Treasury 2036	2.61
2-Sep-15	1½% Treasury 2021	0.71
8-Sep-15	3½% Treasury 2045	2.14
16-Sep-15	2% Treasury 2025	0.97
1-Oct-15	1½% Treasury 2021	1.32
6-Oct-15	4½% 2034	2.58
15-Oct-15	0⅛% IL 2026	2.30
27-Oct-15	2% Treasury 2025	0.69
10-Nov-15	0⅛% IL 2058	3.15
12-Nov-15	4¼% Treasury 2039	1.23
18-Nov-15	2% Treasury 2025	0.42
2-Dec-15	1½% Treasury 2021	0.97
8-Dec-15	3½% Treasury 2045	2.12
17-Dec-15	1¼% IL 2032	2.38
5-Jan-16	2% Treasury 2025	1.23
7-Jan-16	4% Treasury 2060	0.66
12-Jan-16	0⅛% IL 2046	3.79
20-Jan-16	3½% Treasury 2045	-0.48
9-Feb-16	0⅛% IL 2026	3.63
11-Feb-16	3½% Treasury 2045	0.00
17-Feb-16	1½% Treasury 2026	0.00
2-Mar-16	3½% Treasury 2045	0.70
8-Mar-16	3¾% Treasury 2052	1.90
10-Mar-16	0⅛% IL 2036	6.00
	Aggregate all auctions	**63.0**
	Average all auctions	**1.6**
	Average conventional auctions	**1.1**
	Short-dated conventional auctions	0.8
	Medium-dated conventional auctions	0.7
	Long-dated conventional auctions	1.7
	Average Index-linked auctions	**2.8**

A total premium of £63.0 million occurred across all 39 auctions in 2015-16 (an average premium of £1.6 million per auction – the same as in 2014-15). The average premium at conventional auctions was £1.1 million, while that at index-linked auctions was higher at £2.8 million. Concessions were only recorded at three auctions.

The largest premium was £7.14 million at the auction of 0% Index-linked Treasury gilt 2058 on 27 May 2015 and the largest concession was -£1.72 million at the auction of 0% index-linked Treasury Gilt 2040 on 16 April 2015.

c) The DMO's cash management objective: performance report

The DMO's high level cash management objective as set out in Chapter 3 has been subdivided into a series of objectives, to each of which has been attached a Key Performance Indicator (KPI). The following section explains how performance was delivered against these objectives in 2015-16.

Objective 1.1: DMO must supply sufficient cash each day to enable government to meet its payment obligations. This is fundamental and unconditional.

The core requirement of Exchequer cash management is to secure the day to day funding of Exchequer cash needs. This objective is supported by HM Treasury's daily net cash flow forecasts for 19 weeks ahead and intraday updates of same-day scheduled expenditure and revenue flows. The DMO cash dealers raise and place current and future anticipated net daily balances in the DMA with counterparties in the Sterling money markets, transacting in a range of instruments and at a range of different maturities to smooth the profile of the forecast cumulative net cash position.

Table B4: Components of the cash management objective

CASH MANAGEMENT OBJECTIVE	KEY PERFORMANCE INDICATORS AND CONTROLS
The DMO must supply sufficient cash each day to enable government to meet its payment obligations. This is fundamental and unconditional.	Ways and Means transfers must be avoided for cash management purposes by ensuring that there is always a positive DMA balance. (NB: HM Treasury is responsible for monitoring and reporting performance of the forecasting function against outturns).
Cash management operations and arrangements should be conducted in a way that does not interfere with monetary policy operations.	The DMO will conduct market operations with a view to achieving, within a very small range, the weekly cumulative target balance for the DMA at the Bank of England. The DMO will maintain formal and informal channels of communication with the Bank on conditions in the Sterling money markets. The DMO will seek to avoid holding weekly or ad hoc Treasury bill tenders when the Bank conducts its weekly open market operations.
Cash management operations and arrangements should be conducted without impeding the efficient working of the Sterling money markets.	The DMO will advise HM Treasury as appropriate on the impact of Exchequer cash flows on liquidity conditions in the Sterling money markets.
The DMO should maintain a system in which the costs and risks are transparent, measured and monitored and the performance of government cash management is assessed. The DMO maintains an ethos of cost minimisation rather than profit maximisation.	The DMO will report to HM Treasury on a quarterly basis the details of its cash management activity, its active management performance against the government's marginal cost of funds and the market and credit risks incurred. Performance may also be reported in the DMO Annual Review.

CASH MANAGEMENT OBJECTIVE	KEY PERFORMANCE INDICATORS AND CONTROLS
The DMO should maintain a credible reputation in the market that leads to lower costs in the long term and a cash management system that is sustainable.	The DMO should maintain channels of communication with money market participants and Treasury bill counterparties both formally and informally to explain, as far as possible, the nature and intent of its operations in the money markets. The DMO should monitor compliance with its operational notices; provide complete, accurate and timely instructions to counterparties, agents, external systems and operators; and achieve the successful settlement of agreed trades on the due date.

The DMA is used to manage the Exchequer's net cash position. Balances in central government accounts contained within the Exchequer pyramid are swept on a daily basis into the NLF and the DMA is required to offset the resultant NLF balance through its borrowing and lending in the money markets. The DMA is held at the Bank of England and a positive end of day balance must be maintained at all times; it cannot be overdrawn. Automatic transfers from the government Ways and Means (II) account at the Bank of England would offset any negative end of day balances, though it is an objective to minimise such transfers. Thus, evidence of meeting this objective is provided by reference to the number of occasions the DMA goes overdrawn.

KPI 1.1: Ways and Means end of day transfers for cash management purposes must be avoided by ensuring that there is always a positive DMA balance.

- The DMO ensured a positive end of day DMA balance for all of 2015-16.

Objective 1.2: Cash management operations and arrangements should be conducted in a way that does not conflict with the operational requirements of the Bank of England for monetary policy implementation.

The DMA target balance at the Bank of England serves solely as a buffer against unexpected payments that occur after the wholesale money markets have closed for same-day settlement. It serves to mitigate the risk of going overdrawn. All changes to the daily net cash forecast that occur before markets are closed should be transacted by DMO cash dealers with market counterparties. The DMO cash forecasters are required to notify the Bank of England, in advance of its weekly round of open market operations, of the weekly target balance on the DMA for the week ahead. This contributes to the forecast money market shortage and hence it is important that actual cumulative end of day balances do not differ significantly from target.

KPI 1.2: The DMO will conduct market operations with a view to achieving, within a very small range, the weekly cumulative target balance for the DMA at the Bank of England. The DMO will maintain formal and informal channels of communication with the Bank on conditions in the Sterling money markets. The DMO will seek to avoid holding weekly or ad hoc Treasury bill tenders when the Bank conducts its weekly open market operations.

- The DMO achieved its target weekly cumulative balance for the DMA within a very small range (+/-2% of its weekly cumulative target) in 26 out of 52 weeks in 2015 -16. All significant known daily and forecast cumulative weekly variations from target were notified to the Bank of England in a timely fashion. The DMO and the Bank held regular meetings to review the operation of these arrangements.

- No cash management operations were undertaken that by their nature or timing could be perceived as clashing with the Bank's open market operations.

Objective 1.3: Cash management operations and arrangements should be conducted to avoid undermining the efficient functioning of the Sterling money markets.

While this objective is difficult to capture in a KPI, the DMO interprets this as a responsibility to seek to minimise the impact of individual daily flows on the Sterling money markets while ensuring it deals at competitive prices. The DMO operates as a customer at the core of the money markets, seeking to ensure the widest possible access to maturities, instruments, trading arrangements and counterparties across which to diversify its cash management operations. Limits have been set on the amount of dealing with individual counterparties and in individual instruments; exposure to Sterling overnight liquidity and Sterling interest rates are also subject to limits. In accordance with objective 1.3, limits and controls are intended to avoid concentration of exposures and are reviewed regularly to ensure consistency with market trends and developments; they find their expression in KPI 1.3.

KPI 1.3: The DMO will advise HM Treasury as appropriate on the impact of Exchequer cash flows on liquidity conditions in the Sterling money markets.

- Throughout 2015-16, the DMO undertook regular formal and informal communication with the Bank of England, money market counterparties, and industry groups to assess liquidity in the Sterling money markets. It also maintained frequent and regular dialogue to update HM Treasury on market liquidity and, working with HM Treasury, reviewed its trading policies and risk controls to respond to significant Sterling liquidity trends and developments.

Objective 1.4: The DMO should maintain a system in which the costs and risks are transparent, measured and monitored and the performance of government cash management is assessed. The DMO maintains an ethos of cost minimisation rather than profit maximisation.

The active cash management framework encompasses a series of quantitative liquidity, interest rate, foreign exchange and credit risk limits that together reflect the government's risk preferences and are designed to be consistent with the wider policy objectives the government sets its cash manager.

Under the current approach active cash performance is measured and evaluated directly by comparing actual net interest paid and received with cost of funds (i.e. deducting net interest on daily balances at the Bank of England repo rate and deducting transaction and management costs).

KPI 1.4: The DMO will report to HM Treasury on a quarterly basis the details of its cash management activity, including active cash management performance after cost of funds and the liquidity, interest rate, foreign exchange and credit risks incurred. Performance may also be reported in the DMO Annual Review.

- The DMO reports to the Treasury on a quarterly cycle the details of its cash management activity, including active cash management performance and usage of liquidity, interest rate, foreign exchange and credit risk limits.

- Net returns (over cost of funds) will be affected by market conditions and the size and volatility of the Exchequer's cumulative cash position, both of which will vary significantly over time.

- Results should be interpreted in the context of the government's ethos of cost minimisation and not profit maximisation: cash transactions are solely intended to smooth a given cash flow profile over time and across products and instruments, within agreed risk parameters, and are not intended to seek opportunities to generate excess return.

- Active cash management earned positive net interest after cost of funds, but before transaction and management costs, of £25.8 million for 2015-16 compared with £12.0 million for 2014-15. The DMO's estimated transaction and management costs during 2015-16 were £9.5 million.

- Positive net interest after cost of funds has been earned by virtue of funding the Exchequer's daily cash needs in the wholesale money markets at rates that have been on average significantly below the prevailing Bank of England Bank Rate and from investing surpluses at market rates that were on average marginally below Bank Rate.

- There were no breaches of the credit, interest rate, foreign exchange or liquidity risk limits in 2015-16.

Objective 1.5: The DMO should maintain a credible reputation in the market that leads to lower costs in the long term and a system that is sustainable.

The DMO seeks to maintain and enhance its reputation in the market by being open, transparent and consistent about the aims and intentions of its operations and transactions. This has allowed it to continue to widen its market and counterparty access and to deal at fair and competitive rates.

In addition, DMO personnel, processes and internal systems have to be capable of complying with market standards and following market practice in respect of speed and accuracy in negotiation, clearing and settlement of trades.

KPI 1.5: The DMO should maintain channels of communication with money market participants and Treasury bill counterparties both formally and informally to explain, as far as possible, the nature and intent of its operations in the money markets. The DMO should monitor compliance with its operational notices; provide complete, accurate and timely instructions to counterparties, agents, external systems and operators; and achieve the successful settlement of agreed trades on the due date.

- As stated in the report on KPI 1.3 above, in 2015-16 the DMO maintained an active and open dialogue with cash counterparties and other market stakeholders to explain its cash management approach and strategy and to explain the context for and receive feedback on Treasury bill tenders and other market operations.

- There were no breaches of cash management operational targets for trade settlement (percentage by value on the due date[13]) or the timing of the announcement of Treasury bill tender results[14]. There were no breaches of the cash management operational notice in 2015-16.

[13] The target is to settle at least 99% of trades by value on the due date: the level achieved was 99.8%.
[14] The target is to release tender results within 15 minutes: the average release time was 6.2 minutes.

d) Treasury bill tender performance

Table B5 and Charts B1-3 compare the results (in terms of the average accepted yield) of all Treasury bill tenders held in 2015-16 with the corresponding SONIA rates. Over the financial year the average accepted yields at one month tenders outperformed the corresponding SONIA rates by 3.6bps, but narrowly underperformed (by 0.4bps) in the case of three month tenders. There was a more significant underperformance (by 5.9bps) in the case of six month tenders – see Table B5.

The range of relative performances may in part reflect the range of average tender sizes. The average size of six-month Treasury bill tenders was some 60% larger than the average for one-month tenders. The average cover ratios were, however, more consistent across the three maturities – see Table B6.

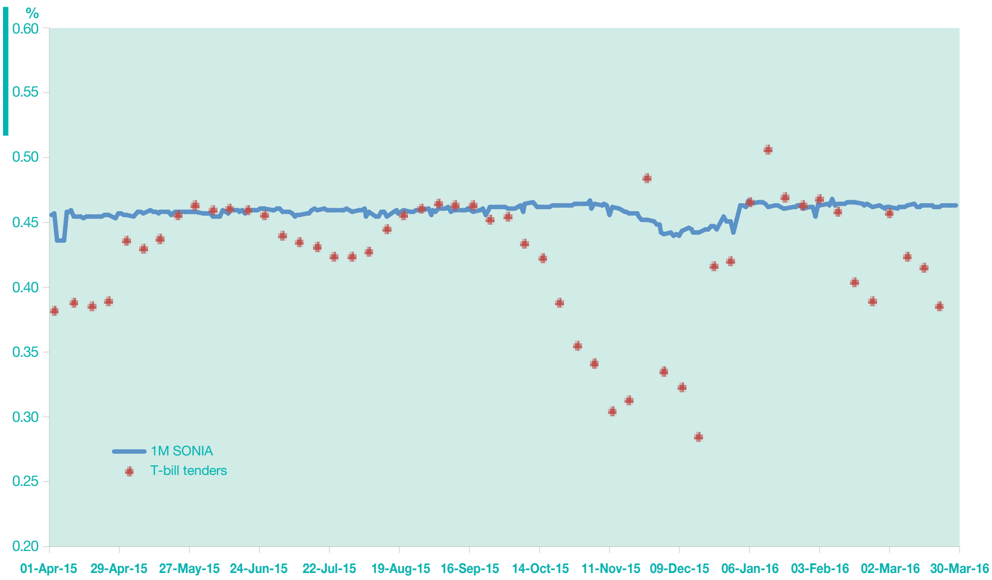
Table B5: Comparison of average tender yields with SONIA rates in 2015-16

	Average tender yield (%)	Average SONIA rate (%)	Difference (bps)
One-month	0.423	0.459	-3.6
Three-month	0.466	0.462	0.4
Six-month	0.530	0.470	5.9
Average	**0.473**	**0.464**	**0.9**

Table B6: Comparison of average tender sizes and cover ratios

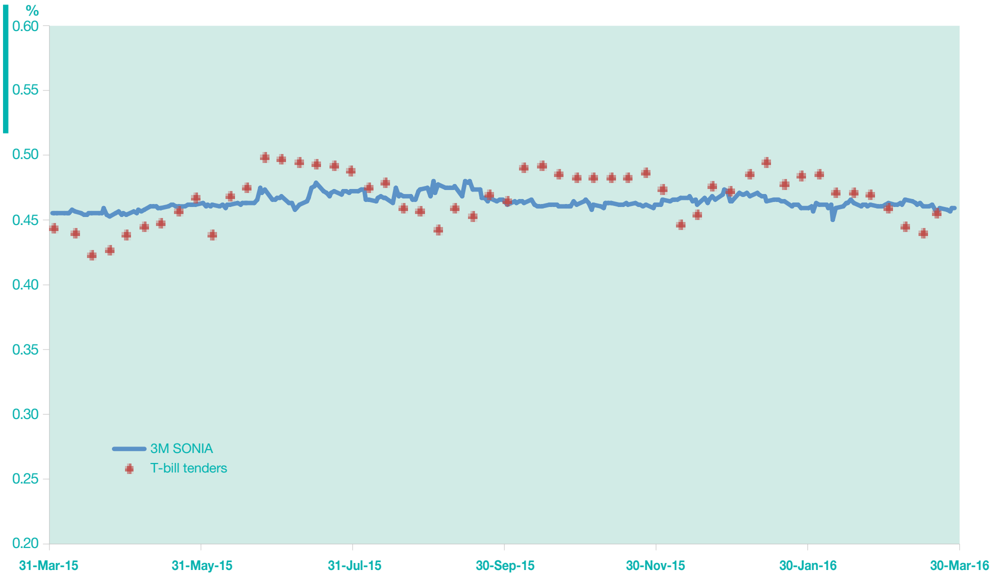
	Average tender size (£mn)	Average cover ratio (x)
One-month	1,125.0	3.67
Three-month	1,581.7	2.85
Six-month	1,831.7	3.09

Chart B1: One-month tender yields compared with SONIA rates in 2015–16



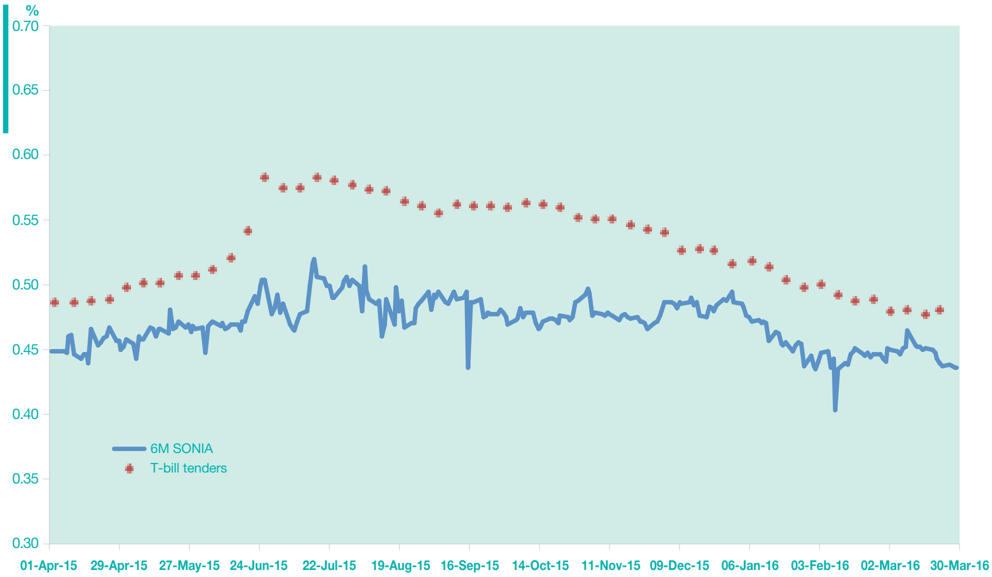
Source: DMO/Bloomberg

Chart B2: Three-month tender yields compared with SONIA rates in 2015–16



Source: DMO/Bloomberg

Chart B3: Six-month tender yields compared with SONIA rates in 2015–16



Source: DMO/Bloomberg

Annex C: The gilt portfolio

The gilt portfolio

The key statistics of the gilt portfolio at end-March 2016 compared with the position at the end of the previous financial year are shown in Table C1 below. Figures in the 'Net' columns next to the nominal and market values of the gilt portfolio are the corresponding totals excluding central government holdings.

Table C1: Key gilt portfolio statistics

	End-March 2015		End-March 2016	
	Gross	Net	Gross	Net
Nominal value of the portfolio – inc T-bills (£bn)	1,493.12	1,365.85	1,540.48	1,424.65
Nominal value of the gilt portfolio (£bn)	1,427.66	1,300.40	1,462.17	1,346.34
– conventional gilts	1,069.88	953.40	1,075.65	970.72
– index-linked gilts	357.78	347.00	386.52	375.62
Market value of the portfolio – inc T-bills (£bn)	1,875.90	1,710.57	1,941.65	1,789.47
Market value of the gilt portfolio (£bn)	1,810.51	1,645.18	1,863.40	1,711.22
– conventional gilts (£bn)	1,310.45	1,159.34	1,324.91	1,186.80
– index-linked gilts (£bn)	500.06	485.84	538.49	524.41
Weighted average market yields				
– conventional gilts	1.50	1.50	1.37	1.36
– index-linked gilts	-1.03	-1.02	-1.05	-1.05
Portfolio average maturity – inc Tbills (years)	16.24	16.39	16.47	16.59
Portfolio average maturity – exc Tbills (years)	16.82	17.03	17.15	17.34
– conventional gilts (years)	14.77	14.72	15.09	15.04
– index-linked gilts (years)	22.21	22.54	22.21	22.54
Average modified duration				
– conventional gilts (years)	10.16	10.41	10.24	10.20
– index-linked gilts (years)	20.81	21.14	22.00	22.24

A list of gilts, including first issue and coupon dates and nominal amounts outstanding (updated daily) is available on the DMO website at: http://www.dmo.gov.uk/index.aspx?page=Gilts/Gilts_In_Issue

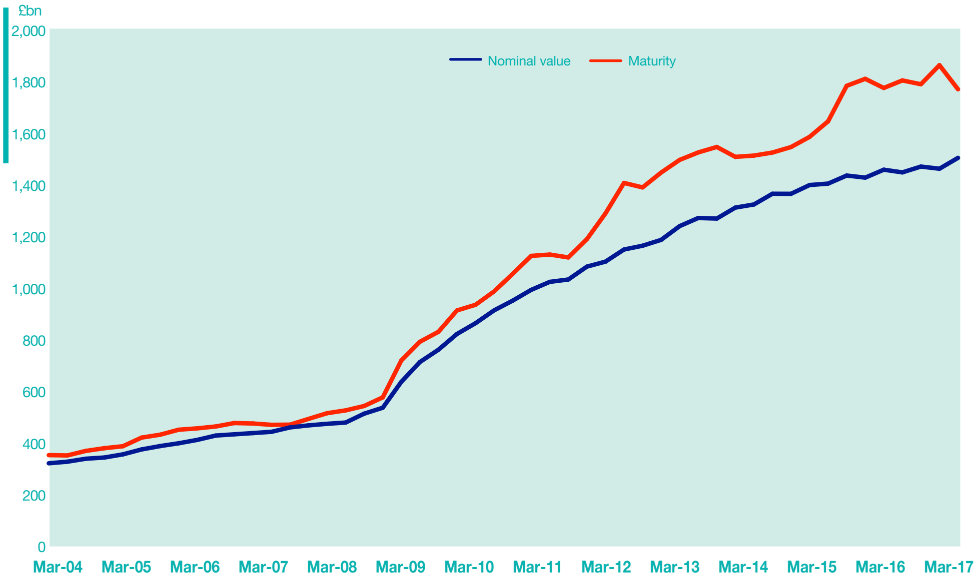
The nominal value[15] of the gilt portfolio rose by 2.4% to £1,462.2 billion as gross gilt issuance exceeded gilt redemptions. The market value of the portfolio also rose but by 2.9% to £1,863.4 billion, reflecting a fall in yields over the course of the year.

The size of the gross gilt portfolio is larger as a result of the creation (since 2008-09) of £115.8 billion (cash) of gilt collateral for the DMO's Exchequer cash management operations and the Bank of England's Discount Window Facility. The gilt collateral is held on the DMA and the net data above exclude these holdings.

[15] Including inflation uplift on index-linked gilts.

Chart C1 shows the nominal and market values of the gilt portfolio at end-March in each year since 2005 and projected to end-March 2017 (based on the DMO's financing remit for 2016-17).

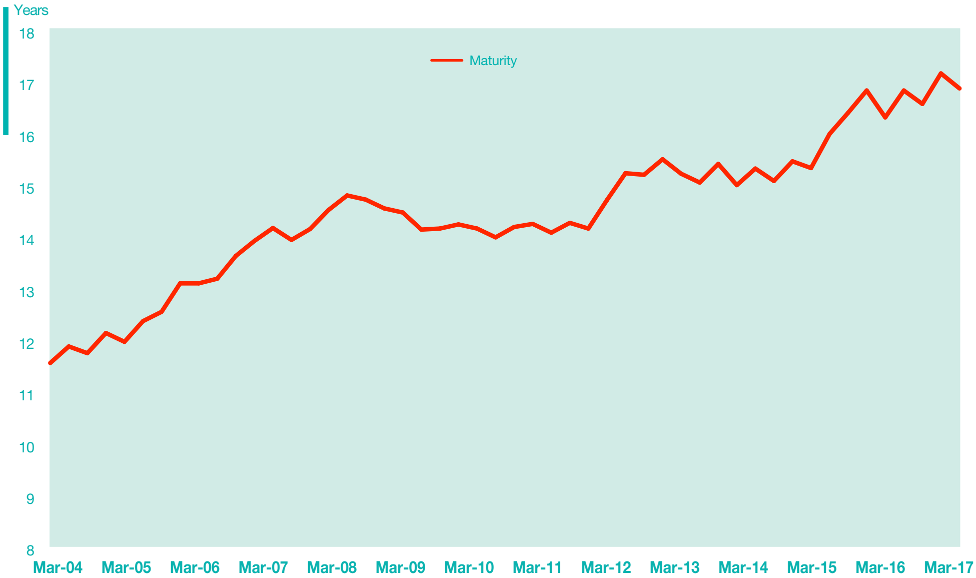
Chart C1: Nominal and market values of the gross gilt portfolio (projected to end-March 2017)



Source: DMO

Chart C2 shows the maturity of the gilt portfolio at end-March each year since 1998 and projected to end-March 2017 (on the basis of the DMO's 2016-17 financing remit). Average maturity is projected to fall marginally in 2016-17 from 17.15 to 16.68 years.

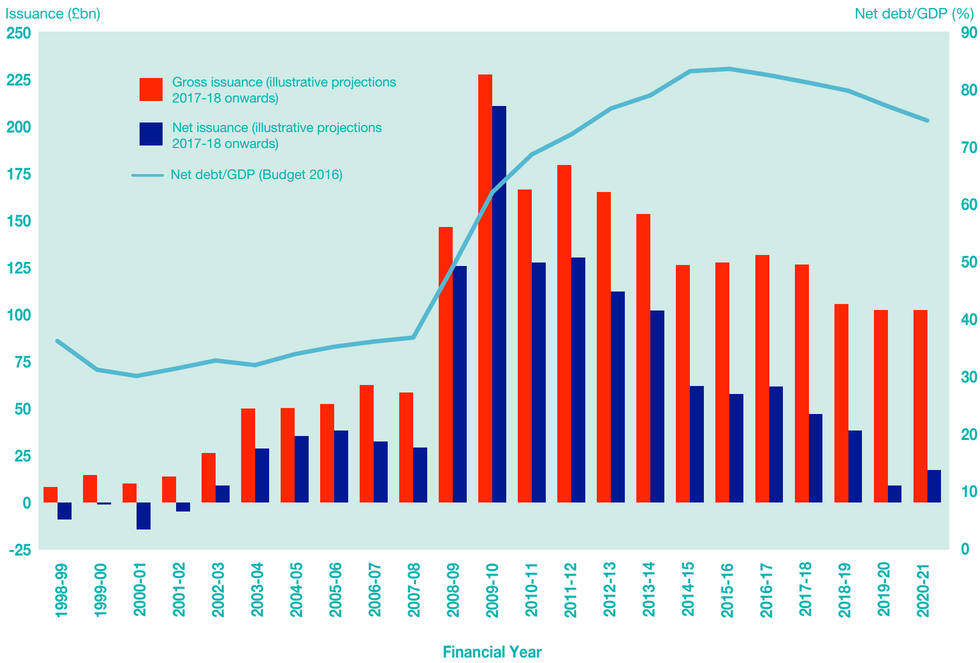
Chart C2: Maturity of the gilt portfolio (projected to end-March 2017)



Source: DMO

Chart C3 shows past and projected gross and net gilt issuance levels (and net debt/GDP ratio) as published at the Budget on 16 March 2016.

Chart C3: Gross and net gilt issuance history and projections



Source: DMO/Office for Budget Responsibility (OBR)

Breakdown of the gilt portfolio by type and maturity

Table C2 and Chart C4 below show the evolution of the gilt portfolio by type and maturity since March 1999. They show a steadily rising proportion of long conventional gilts (from 15% to 29% of the portfolio at the peak in March 2009), although it has fallen back a little since then, reflecting the subsequent large absolute increase in short-conventional issuance. The proportion of medium conventional gilts fell to a low of 12% in March 2015, due to reduced issuance in the sector and because of the effect of shorter-dated medium gilts rolling down into the short sector.

The proportion accounted for by index-linked gilts also rose significantly (from 21% to a peak of 30% at end-March 2008), although this too has fallen back since then in the wake of record high gilt sales requirements that necessitated significant absolute increases in conventional gilt sales.

Table C2:
Portfolio composition 1999-2016

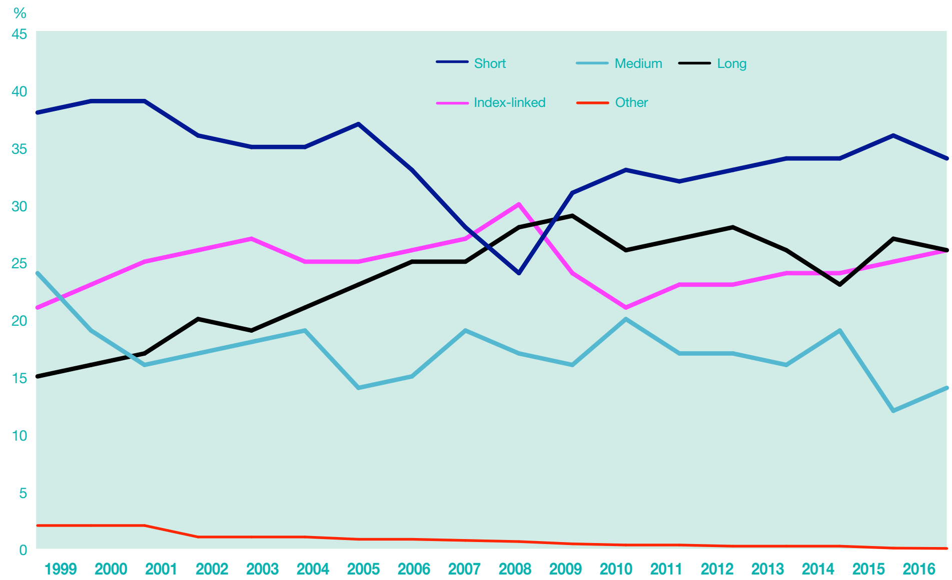
(%)	Short	Medium	Long	Index-linked	Other*
1999	38	24	15	21	2
2000	39	19	16	23	2
2001	39	16	17	25	2
2002	36	17	20	26	1
2003	35	18	19	27	1
2004	35	19	21	25	1
2005	37	14	23	25	0.8
2006	33	15	25	26	0.8
2007	28	19	25	27	0.7
2008	24	17	28	30	0.6
2009	31	16	29	24	0.4
2010	33	20	26	21	0.3
2011	32	17	27	23	0.3
2012	33	17	28	23	0.2
2013	34	16	26	24	0.2
2014	34	19	23	24	0.2
2015	36	12	27	25	0
2016	34	14	26	26	0

Data as at end-March. Figures may not sum due to rounding.

*Includes undated and floating rate gilts to 2001; undated gilts only thereafter.

Source: DMO

Chart C4:
Gilt portfolio – proportionate breakdown by maturity and type



Source: DMO

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