THE UK DEBT MANAGEMENT OFFICE'S REMIT 2011-12: MINUTE OF CONSULTATION MEETINGS WITH GEMMs AND INVESTORS, HELD AT HM TREASURY, ON 11 JANUARY 2011

The Commercial Secretary to the Treasury chaired the regular annual meetings with representatives of the Gilt-edged Market Makers (GEMMs) and of UK-based gilt investors on 11 January 2011. Officials from HM Treasury and the UK Debt Management Office (DMO) were also present. These meetings are designed to provide gilt market participants with the opportunity to inform HM Treasury's decisions regarding the debt financing remit for 2011-12.

The forecast in the Economic and Fiscal Outlook (November 2010), published by the Office for Budget Responsibility (OBR), for the Central Government Net Cash Requirement (CGNCR) for 2011-12 is £120 billion. Gilt redemptions in 2011-12 are forecast to be £49 billion. On this basis, the gross financing requirement for 2011-12 would be around £169 billion (compared to £162.7 billion forecast for 2010-11). It is expected that most of the financing requirement will be met by the sale of gilts. The DMO's financing remit for 2011-12 will be published alongside Budget 2011 on 23 March 2011.

The Commercial Secretary opened the meeting by welcoming attendees and thanking them for their professionalism and commitment to the gilt market in 2010-11.

The main points discussed at the meetings are summarised below.

Investors: Strong support was expressed for an increase in index-linked gilt sales in 2011-12 (including sales of shorter-dated maturities). Ongoing strong expected demand from the pension sector was seen as supportive for the index-linked sector (although some thought that this might be sensitive to the level of yields), as were a couple of technical factors occurring in 2011-12[1]. A number of attendees also reported demand for short-dated conventional gilts, while other attendees reported demand for long-dated conventional gilts; there was less clear support for high issuance of medium-dated conventional gilts.

Investors' views were mixed on the case for fewer, larger auctions compared to the status quo, with some supporting this case, but others expressing a preference for more frequent but smaller auctions in 2011-12.

The structure of the supplementary programme was judged to have been successful in 2010-11 – in particular the use of syndications for index-linked gilts – and investors called for supplementary methods of gilt issuance to be deployed again in 2011-12.

The prospect of a specific consultation on CPI-linked gilts, led by the DMO at some stage in 2011-12, was welcomed, with some attendees mentioning that some

[1] Namely the reinvestment of the proceeds from the redemption of 2½% IL 2011, and, reflecting the shortening of its maturity, the exit of 2½% IL 2016 from the over 5-year index which would lead to demand for long-dated index-linked gilts from those funds tracking this index.

clients had already moved to use the CPI to uprate private pension benefits. As a result, demand for CPI-linked gilts was likely to develop.

In terms of other instruments, there were some calls for the issuance of Floating Rate Notes and longer-maturity Treasury bills, and a small number of calls for issuance of “green gilts”.

GEMMs: Demand was reported to be high for conventional and index-linked gilts across all maturity sectors. There were widespread calls to increase overall index-linked gilt issuance in 2011-12, and that increased issuance of shorter-dated index-linked maturities alongside longer maturities would be welcome. A number of GEMMs cited technical factors occurring in 2011-12, which would also lead to demand for index-linked gilts (see footnote 1). High demand for index-linked gilts was also seen as being underpinned by a positive environment for clients undertaking Liability Driven Investments (LDI).

Demand for short-dated gilts was projected to remain high in 2011-12, including from overseas investors such as central banks. Some GEMMs recommended the launch of a programme of two-year ‘ultra short’ gilt sales to meet that demand, although others disagreed with this suggestion on the grounds that it would increase pressure on the redemption profile. Some attendees suggested that, following the relatively large reduction in medium-maturity gilt issuance in 2010-11, sales of these gilts could be increased, citing the banking sector’s demand for gilts as increasingly extending to the medium maturity gilt sector. Significant expected LDI by the pension and insurance sectors was seen as likely to underpin demand for long-dated conventionals, and, in particular, index-linked gilts.

A large number of GEMMs advocated holding fewer but larger auctions in 2011-12 on the grounds that a smaller number of relatively large auctions would aid liquidity management, although others expressed satisfaction with the current structure.

There was general support for the continuation of the supplementary programme, and, in particular, syndication. Views were, however, mixed on use of mini-tenders in 2011-12. Some GEMMs valued the flexibility provided by mini-tenders; moreover, there were some calls for the use of mini-tenders to be extended to shorter gilts than is currently the case. Others suggested that mini-tenders were no longer necessary and that the use of mini-tenders detracted from the principles of transparency and predictability. If mini-tenders were discontinued, it was suggested that the sales could be absorbed within the syndication or auction programmes.

A number of other innovations were proposed by some attendees, with potential demand for Floating Rate Notes cited. The prospect of a consultation on the issuance of CPI-linked gilts, led by the DMO at some stage in 2011-12, was also welcomed, although it was noted that any such consultation would await the publication of the Government’s response to the Department for Work and Pensions’ consultation on the arrangements for the uprating of private pension benefits that was currently underway.

Other business – issuance of sovereign sukuk

The Government had reviewed the case for the issuance of sovereign sukuk. The Government had decided not to issue sovereign sukuk because it was judged not to provide value for money for the Exchequer but it would keep the situation under review.