

UK TREASURY BILLS



INFORMATION MEMORANDUM

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Introduction

The UK Debt Management Office (“DMO”) expects Treasury bills to play a growing role in its Exchequer cash management operations in the future and to represent an increasingly important component in the UK Government’s stock of marketable debt instruments, alongside gilts. HM Treasury’s remit to the DMO for 2001-02 includes plans for a £5.0 billion increase in the stock of Treasury bills over the financial year (to £8.3 billion).

This information memorandum sets out the main features of Treasury bills as a financial instrument, how they can be bought, settled and traded and through whom. The arrangements set out in this memorandum come into force with effect from the Treasury bill tender to be held on **Friday 5 October 2001**.

This memorandum is to be read alongside the DMO’s revised cash management Operational Notice dated 21 September 2001. This memorandum is repeated as Appendix 1 of the Operational Notice which is available on the DMO web site www.dmo.gov.uk (and is available from the DMO).

The Government’s Treasury bill programme is continuously kept under review. If interested parties have any comments or suggestions on the programme, or wish to express an interest in becoming a Treasury bill primary participant (see Annex A) or would like more information on Treasury bills generally, see Annex B for DMO contact/information details.

1. Description of the instrument

- 1.1. Treasury bills are sterling denominated unconditional obligations of the UK Government with recourse to the National Loans Fund and the Consolidated Fund. They are issued from, and are liabilities of, the Debt Management Account. Treasury bills are negotiable, bearer, zero-coupon instruments.
- 1.2. In credit risk terms Treasury bills have the same standing as gilt-edged securities (“gilts”)¹. They qualify as zero risk-weighted instruments for the purposes of determining capital adequacy under the 1988 Basel Capital Accord.
- 1.3. Treasury bills can be issued with maturities of 1 month (approximately 28 days), 3 months (approximately 91 days), 6 months (approximately 182 days) and 12 months (up to 364 days). However, the DMO expects to give priority to establishing the shorter maturities more fully before introducing the longer maturity instruments.
- 1.4. Treasury bills issued on and after the tender on Friday 5 October 2001 will have a minimum denomination at issue of £25,000 nominal.
- 1.5. Treasury bills can be held in the following depository systems – CMO and Euroclear (see section 3).
- 1.6. Treasury bills can be used as collateral in the Bank of England’s open market operations and in RTGS² and can be used by the DMO as part of its Exchequer cash management operations.

¹ Gilts and Treasury bills are both unconditional liabilities of the UK Government, which is AAA rated by Standard & Poor’s and Fitch IBCA, and Aaa by Moody’s.

² Real-Time Gross Settlement payment system.

Pricing

- 1.7. Treasury bills are issued at tenders (see below) on a money market yield basis, with the quotation of yield being up to three decimal places. They will be settled according to the following price/yield formula:

$$P = \frac{N}{\left(1 + \frac{y \times n}{36500}\right)}$$

where: P = Settlement proceeds in pounds

N = Nominal value in pounds

y = Yield, quoted as a percentage and up to three decimal places

n = Number of calendar days from the settlement date to the maturity date

The settlement proceeds P will be rounded to the nearest penny for each transaction (0.5 pence is rounded up).

2. Treasury bill tenders

- 2.1. Treasury bills are issued at weekly tenders, held by the DMO on the last business day of each week (ie usually on Fridays). The DMO announces the size of the following week's tender and the maturity of bills on offer at the preceding week's tender. These announcements are made on the DMO's wire service pages³.
- 2.2. The DMO may also issue Treasury bills to assist the Bank of England in its management of the sterling money markets. If requested by the Bank, the DMO would consider adding an additional amount of bills to a tender and in which case it would identify, in its usual announcements, any amount being issued for the Bank.

Participation

- 2.3. Direct bidding by telephone in Treasury bill tenders is open to the following eligible participants:
 - DMO cash management counterparties – who may make bids on existing direct dealing telephone lines.
 - Treasury bill primary participants – (see Annex A).
 - A limited range of wholesale market participants who have established a dealing relationship⁴ with the DMO.
- 2.4. Primary participants have indicated that, subject to their own due diligence controls, they are willing to bid at tenders on behalf of other parties.
- 2.5. Eligible participants may bid in tenders in their own name and/or on behalf of clients; it will be the responsibility of the client and the eligible participant to agree bilaterally the payment and custody arrangements for any Treasury bill holdings acquired in a tender.

³ Reuters/Bridge/ADP, DMO/CASH11, Telerate, 15710 to 15711, Topic 44670 to 44671, Bloomberg, DMO9<GO>.

⁴ In accordance with the arrangements set out under "Cash management counterparty selection" in the Operational Notice. When arranging for a telephone bidding facility, allowance should be made for the timescale involved in setting up such arrangements.

Bidding at Treasury bill tenders

2.6. The key features of the Treasury bill tender process are:

- Tenders are held on a competitive bid yield basis.
- All bids must specify the maturity of bills being bid for, and must be made on a percentage money market yield basis⁵. Bids may be made up to three decimal places, and must include the nominal amount bid for at each yield.
- Bids must be for a minimum of £500,000 nominal of bills. Above this minimum, bids must be made in multiples of £50,000. There is no limit to the number of bids that may be submitted by each tenderer.
- All bids must be received by 11.00 am (London time) on the day of the tender.

Processing of bids

2.7. On receipt of bids from eligible participants the DMO will:

- rank bids for each maturity on offer by yield. Bills will then be allotted to those bids that are at, or below, the yield deemed by the DMO to be the highest accepted yield. Bids at the highest accepted yield may only receive a proportion of the nominal amount of bills bid for;
- reserve the right not to allot the total amount of bills on offer, to cancel any tender and not allot any bills (although it would consider this only in exceptional circumstances), and to reject and scale bids. At the cut-off point a scaling ratio will be calculated and applied to bids at the highest accepted yield. These amounts will be rounded down to the nearest minimum denomination of £25,000. Any residual amount will then be split in tranches of the minimum denomination and allocated to tenderers firstly in order of size of bid (with larger bids taking precedence) and then time of bid (with earlier⁶ bids taking precedence);

⁵ See the section on pricing for the settlement convention the DMO uses for these purposes.

⁶ Based on the time a bid is input to the DMO's tender processing system.

- publish the results of the tender on its wire services pages and on its web site www.dmo.gov.uk as soon after 11.00 am (London time) as possible⁷. The results set out the amounts applied for and allotted respectively at each maturity, the lowest, average and highest accepted yields together with a weighted average percentage allotted at the highest accepted yield (ie, weighted by the amount bid)⁸; and
- announce, at the same time, the amounts on offer at each maturity at the next tender, together with an outline of any ad hoc tenders to be held in the following week.

Maturity of bills issued

- 2.8. Bills issued at tenders currently mature on the first business day of the week, four weeks, thirteen weeks, twenty six weeks or fifty two weeks respectively following the issue date, which will be the first business day of the week following the tender.
- 2.9. If Treasury bills are due to be issued or to settle in weeks including bank holidays, the exact maturity of the bills at issue will be adjusted to ensure repayment on the first business day of the relevant week.

Announcements of future tenders

- 2.10. Following the final tender at the end of each calendar quarter, the DMO will issue a notice outlining the maturities of Treasury bills available in each week of the following quarter.

⁷ The results of the 52 tenders held in 2000-01 were made available on average within 13 minutes of the close of the tender.

⁸ For example, 2 bids are successful at the highest accepted yield and there is £100m to allot. If bid X was for £200m and bid Y was for £1m, X would receive about 49.8% (£99.525m) of its amount bid and Y would receive 47.5% (£0.475m); the weighted average percentage at the highest accepted yield would be $((200 \times 49.7625) + (1 \times 47.5)) / 201 =$ about 50%.

3. Settlement and depository arrangements

3.1. The main features of the settlement and depository arrangements relating to Treasury bills are:

Settlement

- Successful tenderers will be contacted by the DMO following the publication of the results of the tender to which their allotments relate. The DMO will confirm the nominal amount of Treasury bills allotted, the purchase consideration bearing in mind the accepted bids and the purchasers' settlement instructions. The DMO will also ask the purchaser for their preferred bill denominations. As noted above the minimum denomination of Treasury bills at issue is £25,000 nominal.
- An exchange of confirmations will follow. Treasury bill allocations resulting from tenders will be settled on the first business day of the following week; this will also be the issue date of the Treasury bills purchased.
- A CHAPS payment for the full consideration must be received by the Bank of England, from a European Economic Area regulated credit institution, **for credit of the DMO's account at Sort Code 10-18-00, by 1.30pm (London time) on the settlement date**⁹. The purchased Treasury bills will only be released to, or made available for withdrawal from, the purchaser's account at the CMO¹⁰ (or its equivalent) once this payment has been received.
- Treasury bills may be split into smaller denominations or reconstituted into larger denominations on request to the Bank of England, Custodial Services Group, Treasury bills section (020 7601 3302). Currently, the minimum denomination for such splits is £5,000; to bring it into line with the minimum denomination at issue, the DMO intends to increase the minimum split denomination to £25,000 as from 2 January 2002.
- Transactions in Treasury bills can also be settled across Euroclear.

⁹ Unless in any particular case the DMO agrees a different method of settlement.

¹⁰ Central Moneymarkets Office.

Depository

- 3.2. Treasury bills can be held in the CMO, which is operated by the Bank of England on behalf of CRESTCo. The CMO is the central depository for Treasury bills.
- 3.3. It is also possible to hold Treasury bills through Euroclear through the relevant specialised depository.

4. Withholding tax

- 4.1. All payments to holders of Treasury bills will be made without withholding or deduction for or on account of any taxes of whatever nature imposed or levied by or on behalf of the United Kingdom or by any political sub-division of or taxing authority in the United Kingdom unless required by law.

5. Treasury bill primary participants

- 5.1. Annex A contains a list of banks that have agreed, subject to their own due diligence, to bid at Treasury bill tenders on behalf of investors; they will also provide secondary dealing levels for Treasury bills.
- 5.2. All participants at Treasury bill tenders must be registered financial institutions, regulated by the FSA and subject to its rules and guidance in their activities.

Annex A:

Treasury bill primary participants (at 21 September 2001)¹¹

The primary participants listed below are banks that have agreed, subject to their own due diligence, to bid at Treasury bill tenders on behalf of investors; they will also provide secondary dealing levels for Treasury bills.

Barclays Bank plc	020 7773 9650
Cater Allen International Ltd	020 7383 9520
Credit Lyonnais	020 7782 0106
Deutsche Bank	020 7547 0009
Halifax Group Treasury & Wholesale Banking	020 7374 0484
JP Morgan Securities Ltd	020 7779 3180
The Royal Bank of Scotland plc	020 7256 5471
Salomon Brothers International Ltd	020 7986 9535
UBS Warburg	020 7328 0203

¹¹ The DMO will update this list as necessary – a current version will appear on its web site www.dmo.gov.uk

Annex B: Contacts/information

Cash dealing unit – participation/dealing issues

020 7862 6522

020 7862 6518

020 7862 6527

Settlements team – settlement, custody and depository issues

020 7862 6542

Risk management unit – legal/compliance issues

020 7862 6523

Press/media issues

020 7862 6532

Further information on the Treasury bill programme can be accessed on the DMO web site www.dmo.gov.uk (in the money markets pages) and in the DMO's Quarterly Reviews published each January, April, July and October (and which are also available on the DMO web site in the publications pages).

The DMO also publishes information on its Treasury bill and money markets activities on the following wire services:

Information	Reuters/Bridge/ADP	Telerate	Topic	Bloomberg
Money market announcements	DMO/CASH 01	15700 to 15709	44660 to 44669	DMO9<GO>
Treasury bill tenders	DMO/CASH 11	15710 to 15711	44670 to 44671	DMO9<GO>
Ad hoc tenders	DMO/CASH 16	15715 to 15716	44675 to 44676	DMO9<GO>

United Kingdom
**Debt
Management
Office**

*Eastcheap Court
11 Philpot Lane
London EC3M 8UD*