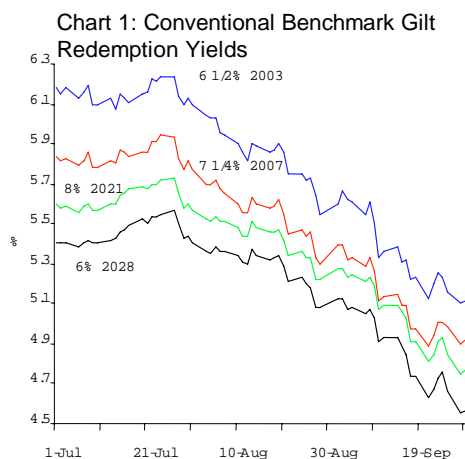


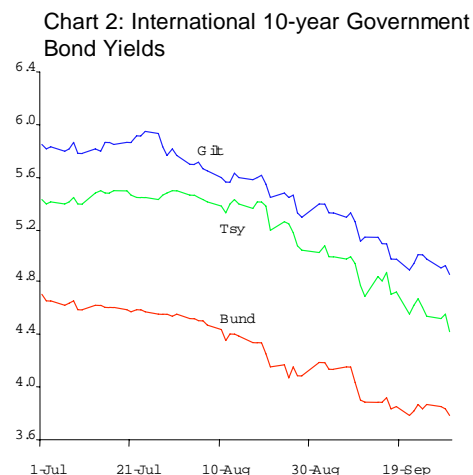
Gilts REVIEW

3rd Quarter 1998 July-September

The third quarter saw a decline in gilt yields, in line with other major government bond yields (see charts 1 and 2). Yield movements were dominated by international events. Deterioration in Russia and prolonged difficulties in Asia caused an intensification of emerging market crises and a growth in deflationary pressures. Investors sought financial safe-havens. The quarter began with speculation of base rate increases in the UK and US. The quarter ended with base rate cuts in Japan and the US and speculation of a repo rate cut by the MPC in the UK.



Source: DMO

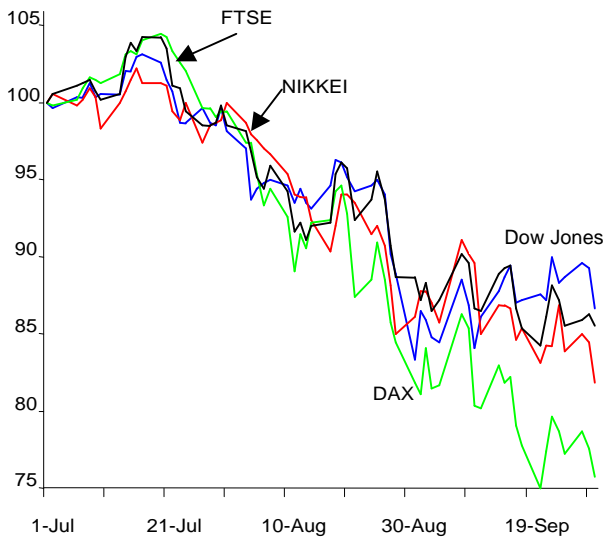


The fall in yields was driven by four factors:

- The continuing crisis in Asia which continued to generate global deflationary pressure. The market expected the new Japanese cabinet to introduce a new fiscal stimulus; but the eventual cut in income tax of ¥4tr was less than expected. Political pressures hindered the proposed reform of the Japanese financial sector.
- Russia also caused disruption to the market. An economic aid package, organised by the IMF and World Bank, had eased market fears of a rouble devaluation. But, on 17 August the Russian Government devalued the rouble and declared a 90 day moratorium on its debt. This weighed heaviest on the



Chart 3: Equity Indices

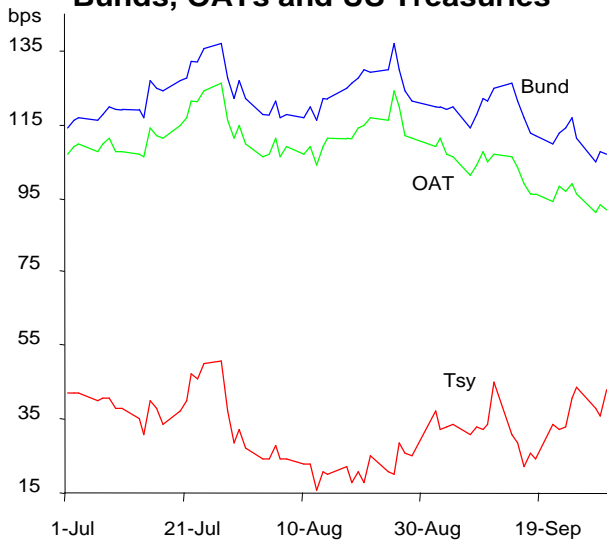


Source: Reuters. 1 July 1998=100

German market over fears of German banks' exposure to Russia.

- The pressures in Russia and Asia led to an increase in concern about emerging markets. Capital left Latin America as investors feared contagion leading to collapse. Brazil and Venezuela were particularly affected.
- Stock markets around the world began to fall in mid-July (see chart 3). This continued throughout August but steadied in September on growing expectations of base rate cuts.

Chart 4: Spread of 10-year Gilts against Bunds, OATs and US Treasuries

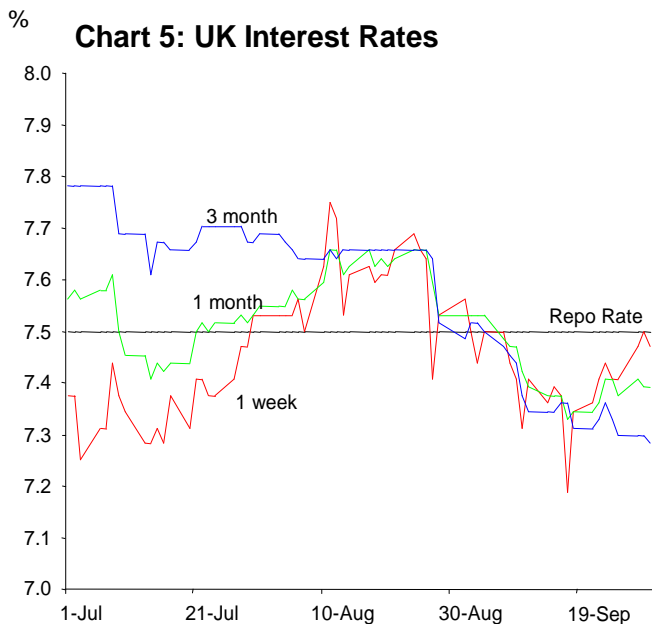


Source: DMO

A statement made by the Federal Reserve's Greenspan on 4 September led markets to infer a more relaxed base rate policy. The Bank of Japan cut base rates by 25 basis points to 0.25% on 9 September. The Bundesbank's Tietmeyer made a statement ruling out a rate cut as this would burden the EMU convergence process. The Federal Reserve cut rates by 25 basis points to 5.25% on 29 September, less than market expectations.

Gilt yields lagged the falls in international government bond yields at points in July and August (see chart 4). This was due to domestic concern that the Monetary Policy Committee (MPC) would increase repo rates. Market views of repo rate movements changed at the beginning of September, as they began to anticipate a rate cut. This was a result of data becoming available that more clearly suggested domestic and global economic slow downs. Chart 5 shows interest rates increasing until the end of August. The perceived removal of upside risk to UK interest rates allowed the gilt yield on the ten year benchmark to rally against bunds and to average its lowest monthly value in September since December 1963.

Chart 5: UK Interest Rates

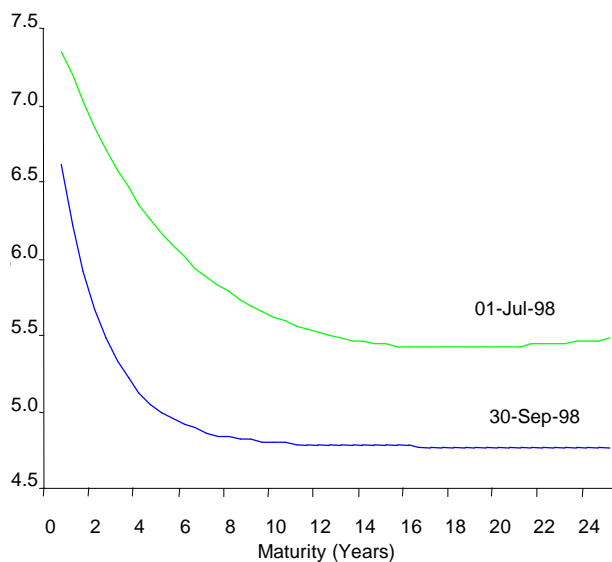


Source: Bank of England

Over the quarter, the DMO converted £2.9bn nominal of 11¾% 2002-7 into £3.4bn 6½% 2003 on 22 July. The DMO also auctioned £2.5bn nominal of a new ten year benchmark, 5¾% 2009, on 29 July. On 7 August the DMO successfully tapped £150 mn of 4 3/8% 2004.

Inflation expectations also fell over the quarter.

Chart 6: Zero-coupon UK Yield Curve

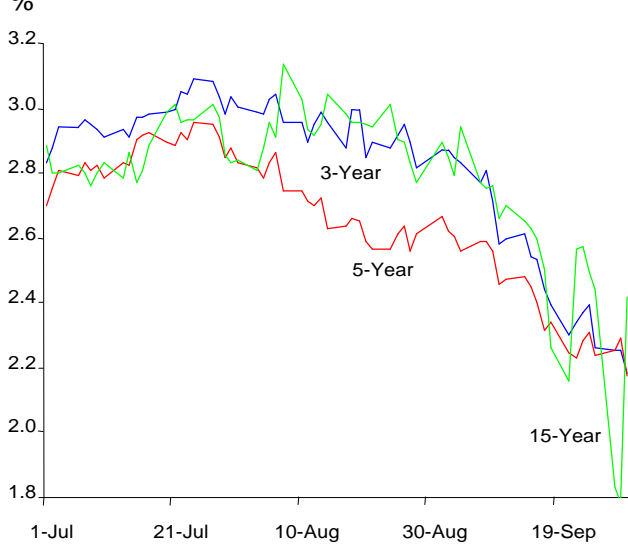


Source: Bank of England

This can be seen in chart 7, showing a fall in implied inflation expectations 3, 5 and 15 years out. Signs of a UK slowdown in both the service and manufacturing sectors, increased global deflationary pressures and constant UK repo rates all contributed to the fall.

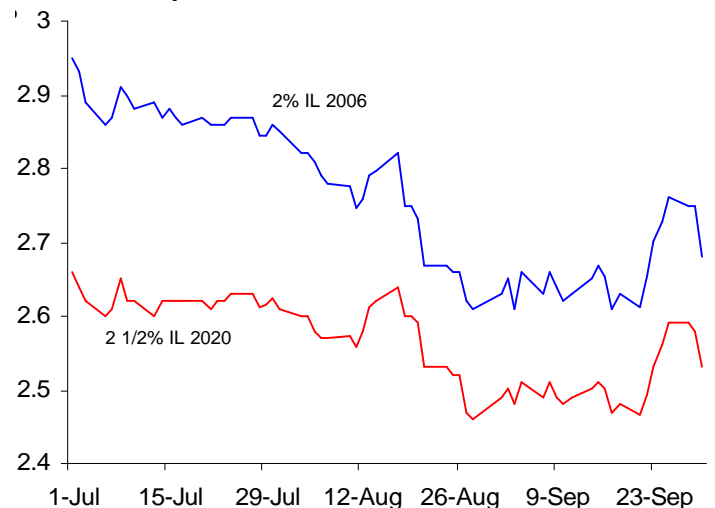
Index-linked gilt yields fell across the quarter (see chart 8). This reflected strong institutional demand and interest in financial safe-havens. The continual decline in inflation expectations created a floor for index-linked gilt yields. Relatively stable yields in early September rose towards the end of the month as lower inflation expectations reduced demand for index-linked gilts.

Chart 7: Implied Forward Inflation Rates*



* In 3, 5 and 15 years time - derived from the inflation term structure.
Source: DMO

Chart 8: Index-linked Gilt Real Redemption Yields



3% RPI assumption.
Source: DMO

1998-99 Financing Requirement

	DMR (1) March 1998	EFSR (2) June 1998	Sales to end of September	Remaining
CGNCR Forecast	3.7	3.5	-	-
Gilt Redemptions	16.7	16.8	-	-
Gilt Sales Residual from 1997-98	-5.1	-8.2	-	-
Financing Requirement	15.2	12.1	-	-
<i>Less net financing from:</i>				
National Savings	1.0	0.5	-	-
Gross Gilt Sales Required	14.2	11.6	-	-
<i>of which</i>				
Ultra-short conventionals (1-3 years)				
Short conventionals (3-7 years)	2.7	2.5	0.07	2.43
Medium conventionals (7-15 years)	2.7	2.5	2.49	0.01
Long conventionals (>15 years)	5.3	3.1	3.07	0.03
Index-linked gilts	3.6	3.5	0.76	2.74
Total	14.3	11.6	6.36	5.24

Note: figures may not sum due to rounding
(1) Debt Management Report
(2) Economic and Financial Strategy Report

Auction Results 1998-99

Auction Date	Issue Amount	Stock	Cover	Tail Price	Lowest Accepted Price	Yield at Lowest
20 May 1998	£3bn	6% 2028	2.26	0	£102.30	5.79%
29 July 1998	£2.5bn	5 3/4% 2009	2.93	0	£100.05	5.73%

Taps of Index Linked Gilts 1998-99

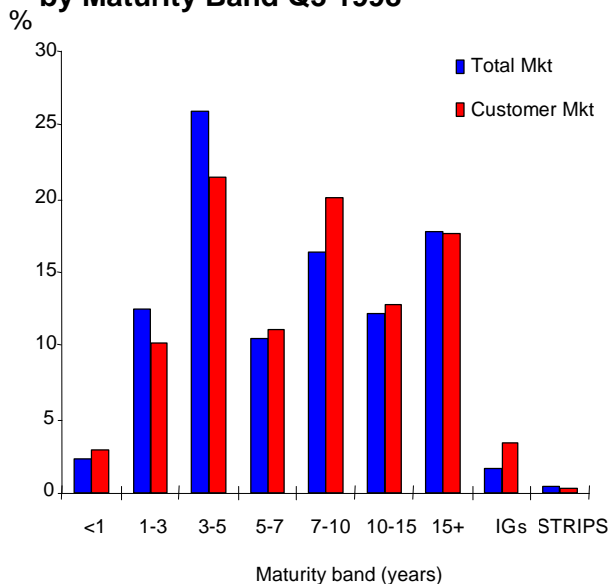
Date of Tap	Issue amount £m	Stock	Price at Issue	Price when exhausted	Yield when exhausted
3 April 1998	150	2 1/2% IL 2024	£160.75	£160.75	2.842
22 May 1998	150	2 1/2% IL 2016	£185.25	£185.25	2.880
12 June 1998	150	4 1/8% IL 2030	£151.38	£151.38	2.530
7 August 1998	150	4 3/8% IL 2004	£128.31	£128.31	2.918

Conversions 1998-99

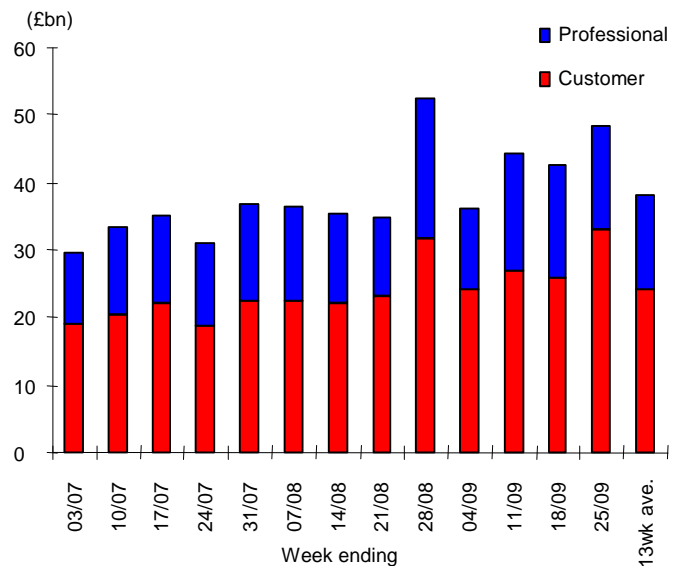
Date	Source Stock	Nominal Converted	Destination Stock	Nominal Converted into
22 July 1998	11 3/4% 2003-07	£2.9bn	6 1/2% 2003	£3.4bn

Details of GEMM Market Turnover 3rd Quarter 1998

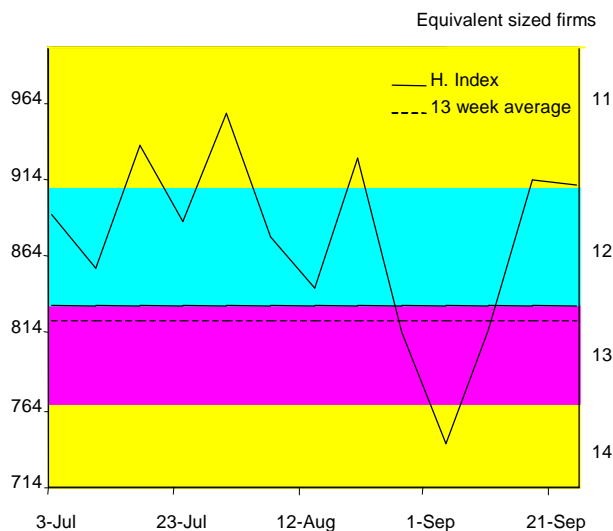
Percentage GEMM Market Turnover by Maturity Band Q3 1998



Total GEMM Market Turnover



Herfindhal Index of Total GEMM Market Turnover



Explanatory Notes:

A Herfindahl Index is a statistical measure of concentration. The HI is calculated as the sum of firms' market share squared. It is compared against numbers of equal sized firms' market shares e.g. five equal sized firms have a Herfindahl number of 2,000, sixteen have 625.

Professional Trades are defined as GEMM trades with IDBs, other GEMMs, DMO and Bank of England

Charts are based on data reported to DMO by GEMMs for the period starting 29 June and ending 25 September.

Index-linked Gilt-Edged Market Makers.

The DMO announced on 10 September, that as from 14 September it would recognise the following firms as specialist index-linked Gilt-Edged Market Makers (IG GEMMs)-

Barclays Bank plc (trading as Barclays Capital)
Dresdner Bank AG (London Branch)
Greenwich Nat West Gilts Ltd
Midland Bank plc (trading as HSBC Greenwell)
Lehman Brothers International (Europe)
Merrill Lynch International
Morgan Stanley & Co. International Limited
Winterflood Gilts Limited

The IG GEMMs have undertaken to provide liquidity to support secondary market trading in index-linked gilts ("IGs"). GEMMs which are not IG GEMMs will no longer have an obligation to make markets in IGs. Further information, including wire service information, can be found in the Press Notice 10 of September. This is available on the DMO website or from the DMO direct (contact numbers page 8).

Index-linked Auction Announcement

On 30 September 1998 the Debt Management Office announced that the auction of the index-linked stock, 2½% IL 2013, would take place on 25 November 1998. This auction date replaced that previously scheduled for 28 October 1998.

The change was made after a shift in the Parliamentary timetable meant that the Pre-Budget Report (PBR) might be published in the previously planned auction week. The move of the auction to 25 November will ensure that there will be at least a week between it and the PBR. The DMO recognised that the change in schedule would be disruptive, but concluded that it was the least potentially damaging course of action.

The date of the Pre-Budget Report will be announced after Parliament returns on 19 October.

The DMO will continue to reserve the right to tap index-linked gilts in line with the Remit and operational notice in light of market circumstances. This continues to preclude three weeks either side of the auction date.

The amount of stock to be auctioned and the terms of the auction will be announced by the DMO at 3.30pm on Tuesday 17 November.

DMO Website

The DMO consulted the GEMMs over the summer on the provision of information by the DMO. The lack of a DMO website was the main concern of those consulted. The following details the DMO's plans for the provision of website services.

The DMO have recently launched a temporary website, courtesy of the Bank of England. The temporary website can be found on the Bank of England's website at the following address:

<http://www.bankofengland.co.uk/dmo>

The website currently contains all DMO Press Releases and Publications, including this one. However, the DMO will shortly be establishing its own website. This will be found at the following address:

<http://www.dmo.gov.uk>

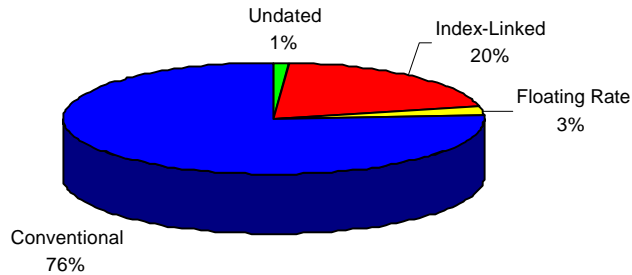
The DMO will announce when this website is operational, but it will be before the end of the year and probably in November.

The website will initially contain the same information as the current temporary website, that is Press Releases and Publications. The DMO plan to increase this service by providing background information on: the DMO itself, gilts and gilt market operation and a supporting database. The DMO database will contain information relevant to the gilt market, in order to reduce the search cost of gathering gilt market data. The DMO has also agreed with the GEMMs to hold on the website some previously unpublished market share data. If market participants have views on the database content please contact David Page or Robert Scott at the DMO (contact numbers on page 8).

Details of the Gilts Portfolio as of 30 September 1998

The following charts are based on nominal values. Index-linked gilts are uplifted to account for inflation.

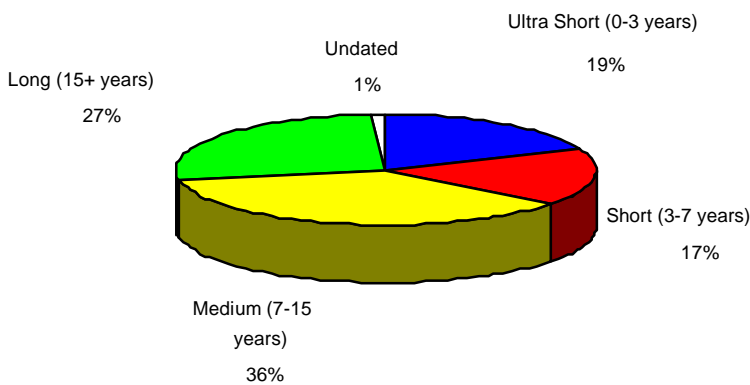
Composition of Gilts Stock



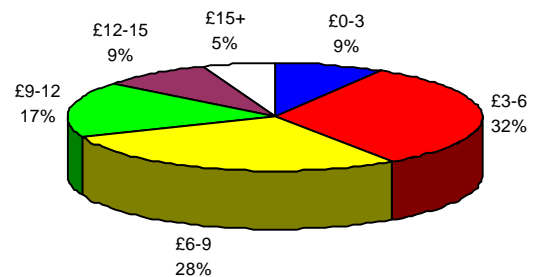
Portfolio Summary Statistics

Portfolio Average Maturity: 9.4 years
 Portfolio Average Modified Duration: 7.115 years
 Portfolio Average Convexity: 96.492
 Average Amount Issued of largest 20 Gilts: £9.056bn

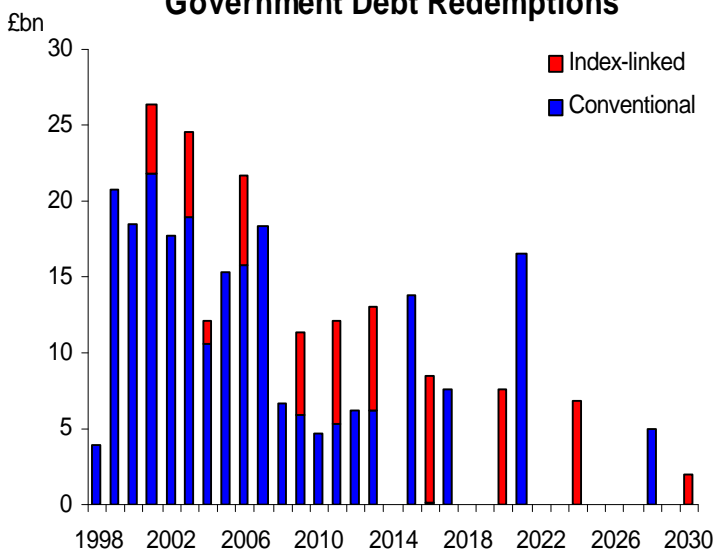
Gilt Portfolio's Maturity Split



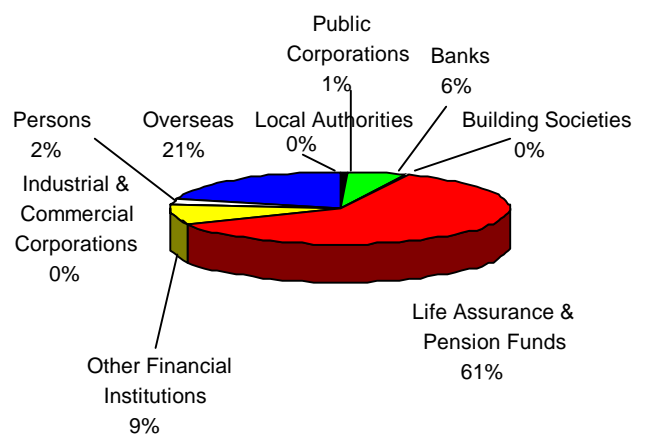
Size of Issues in £ bn of Portfolio



Government Debt Redemptions



Distribution of Holdings of Gilts in Market Hands Q1 1998



Assumes everything above par will be called at earliest maturity.

Source: ONS, Financial Statistics.

Stock in Issue at 30 September 1998*

Conventional Gilts

Stock	Redemption Date	Amount in Issue (£mn)	Amount held in Stripped form (£mn)	Central Government Holdings (end-June)+
12% Exchequer 1998	20-Nov-98	3,909	-	36
9 1/2% Treasury 1999	15-Jan-99	1,900	-	341
Floating Rate 1999	11-Mar-99	5,700	-	225
12 1/4% Exchequer 1999	26-Mar-99	3,050	-	67
10 1/2% Treasury 1999	19-May-99	1,252	-	15
6% Treasury 1999	10-Aug-99	6,950	-	476
10 1/4% Conversion 1999	22-Nov-99	1,798	-	7
9% Conversion 2000	03-Mar-00	5,358	-	42
13% Treasury 2000	14-Jul-00	3,171	-	96
8% Treasury 2000	07-Dec-00	9,800	276	219
10% Treasury 2001	26-Feb-01	4,406	-	15
Floating Rate 2001	10-Jul-01	3,000	-	16
7% Treasury 2001	06-Nov-01	12,750	-	692
11 1/2% Treasury 2001-04	19-Mar-01	1,620	-	142
7% Treasury 2002	07-Jun-02	9,000	75	76
9 3/4% Treasury 2002	27-Aug-02	6,527	-	12
8% Treasury 2002-06	05-Oct-02	2,050	-	65
8% Treasury 2003	10-Jun-03	8,600	-	418
11 3/4% Treasury 2003-07	22-Jan-03	234	-	69
10% Treasury 2003	08-Sep-03	2,506	-	-
12 1/2% Treasury 2003-05	21-Nov-03	2,200	-	-
6 1/2% Treasury 2003	07-Dec-03	5,446	351	21
3 1/2% Funding 1999-2004	14-Jul-04	543	-	32
9 1/2% Conversion 2004	25-Oct-04	3,412	-	-
6 3/4% Treasury 2004	26-Nov-04	6,500	-	363
9 1/2% Conversion 2005	18-Apr-05	4,842	-	-
8 1/2% Treasury 2005	07-Dec-05	10,373	670	188
7 3/4% Treasury 2006	08-Sep-06	4,000	-	261
7 1/2% Treasury 2006	07-Dec-06	11,700	130	32
8 1/2% Treasury 2007	16-Jul-07	7,397	-	216
7 1/4% Treasury 2007	07-Dec-07	11,000	110	94
5 1/2% Treasury 2008-12	10-Sep-08	1,000	-	49
9% Treasury 2008	13-Oct-08	5,621	-	-
8% Treasury 2009	25-Sep-09	3,450	-	160
5 3/4% Treasury 2009	07-Dec-09	2,500	222	-
6 1/4% Treasury 2010	25-Nov-10	4,750	-	256
9% Conversion 2011	12-Jul-11	5,273	-	110
7 3/4% Treasury 2012-15	26-Jan-12	800	-	148
8% Treasury 2013	27-Sep-13	6,100	-	330
8% Treasury 2015	07-Dec-15	13,787	64	86
8 3/4% Treasury 2017	25-Aug-17	7,550	-	18
8% Treasury 2021	07-Jun-21	16,500	629	127
6% Treasury 2028	07-Dec-28	5,000	61	43
2 1/2% Treasury	Undated	474	-	-
3 1/2% War	Undated	1,909	-	-
2 1/2% Consolidated	Undated	275	-	-
4% Consolidated	Undated	358	-	-

Index-linked Gilts

2 1/2% I-L Treasury 2001	24-Sep-01	2,150	-	17
2 1/2% I-L Treasury 2003	20-May-03	2,700	-	12
4 3/8% I-L Treasury 2004	21-Oct-04	1,300	-	-
2% I-L Treasury 2006	19-Jul-06	2,500	-	-
2 1/2% I-L Treasury 2009	20-May-09	2,625	-	37
2 1/2% I-L Treasury 2011	23-Aug-11	3,100	-	6
2 1/2% I-L Treasury 2013	16-Aug-13	3,750	-	5
2 1/2% I-L Treasury 2016	26-Jul-16	4,125	-	40
2 1/2% I-L Treasury 2020	16-Apr-20	3,800	-	8
2 1/2% I-L Treasury 2024	17-Jul-24	4,000	-	-
4 1/8% I-L Treasury 2030	22-Jul-30	1,650	-	1

* Stock of liquid issues. "Rump" stocks are excluded; a full list is obtainable from the DMO. Double-dated issues currently above par are assumed to be called at first maturity.

+ Includes holdings by National Investments and Loans Office (NILO) and DMO. Excludes local authority, public corporation and Bank of England holdings.

Announcements, Events and Contacts

Date	Notice	Title
30 June	Press Notice	Gilt-Edged Auctions: July to September 1998
13 July	Press Notice	Gilt-Edged Conversion from 11 3/4% 2003-7 into 6 1/2% 2003: Provisional Results
21 July	Press Notice	Sale by Auction of £2,500m of 5 3/4% 2009
22 July	Press Notice	Gilt-Edged Conversion from 11 3/4% 2003-7 into 6 1/2% 2003: Final Results
29 July	Press Notice	Result of Auction of £2,500m of 5 3/4% Treasury Stock 2009
3 August	Publication	Gilt Review 1997-8
5 August	Policy Paper	Gilt-Edged Stock Conversion Offers: Rationale and Methodology*
7 August	Press Notice	Additional issue of Government Stock: 4 3/8% IL 2004
10 Sept	Press Notice	Index-linked Gilt-Edged Market Makers
30 Sept	Press Notice	Gilt-Edged Auctions: October to December 1998

* The DMO would welcome comments on this paper to Paul Mills by 30 October.

Date	Event	Name	Position	Telephone No.
Autumn	Statement on Cash Management Progress	Mike Williams	Chief Executive	0171 862 6533
		Paul Mills	Head of Primary Issuance	0171 862 6521
November	DMO Website operational.	Hamish Watson	Chief Dealer	0171 862 6530
25 November	Index-linked auction	Jo Whelan	Manager Secondary Market	0171 862 6531
14 December	GEMM quarterly consultations.	Jim Juffs	Press Officer	0171 862 6520
15 December	End-Investors quarterly consultations.	Robert Scott	Assistant Press Officer	0171 862 6527
27 January	Index-linked auction	David Page	Economic Analyst	0171 862 6524
24 March	Conventional auction	Steve Whiting	Financing Remit	0171 862 6532
		Martin Duffell	Market Liaison Officer	0171 862 6517
		Mark Deacon	Quantitative Analyst	0171 862 6516
		Donna Russell	Primary Issuance Secretary	0171 862 6526

Information	Reuters/Bridge/ADP	Telerate	Bloomberg	Topic3/ASCII Broadcast	Stock ID	ISIN code
Index		DMO/INDEX	DBTM			
Announcements	DMO/GILTS1 to 7	22550 to 2256	44700 to 44714	44715		
Shop window general info	DMOGILTS8	6615	44715	44715		
Shop window 1	DMO/GILTS9	6516	44716	44716		
Shop window 2	DMO/GILTS10	6517	44717	44717		
Shop window 3	DMO/GILTS11	6518	44718	44718		
GEMMA ref prices (Conventionals)	GEMMA01 to 06	47216 to 47221	44800 to 44805	44800 to 44894	44806 to 44809	
GEMMA ref prices (Index-linked)	GEMMA08	47223	44807	44805	44811	
GEMMA ref prices (STRIPS)	GEMMA13 to 19	21291 to 21297	21291 to 21297	44850 to 44856	44850 to 44854	

DMO temporary website: <http://www.bankofengland.co.uk/dmo>

The UK DMO can be found at

Cheapside House,
138, Cheapside,
London.
EC2V 6BB.

Switchboard no. (0171) 862 6501
Fax no. (0171) 862 6509

If readers have any comments on this review, please contact David Page on 0171 862 6524.

