Bank of England

Thirteen days in October: how central bank balance sheets can support monetary <u>and</u> financial stability

Andrew Hauser (ECB Money Markets Conference 2022)

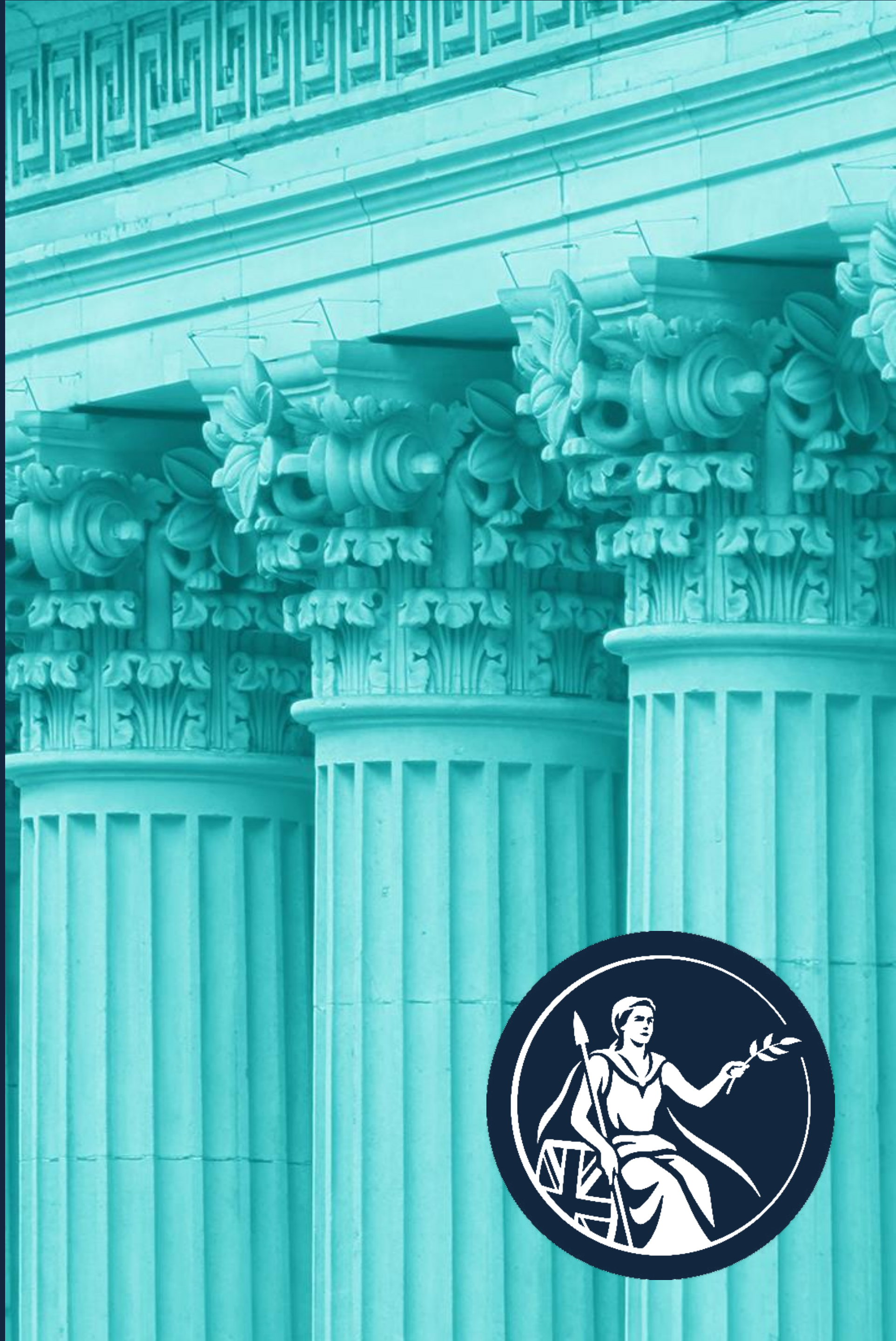


Chart 1: Yield moves and Bank operations

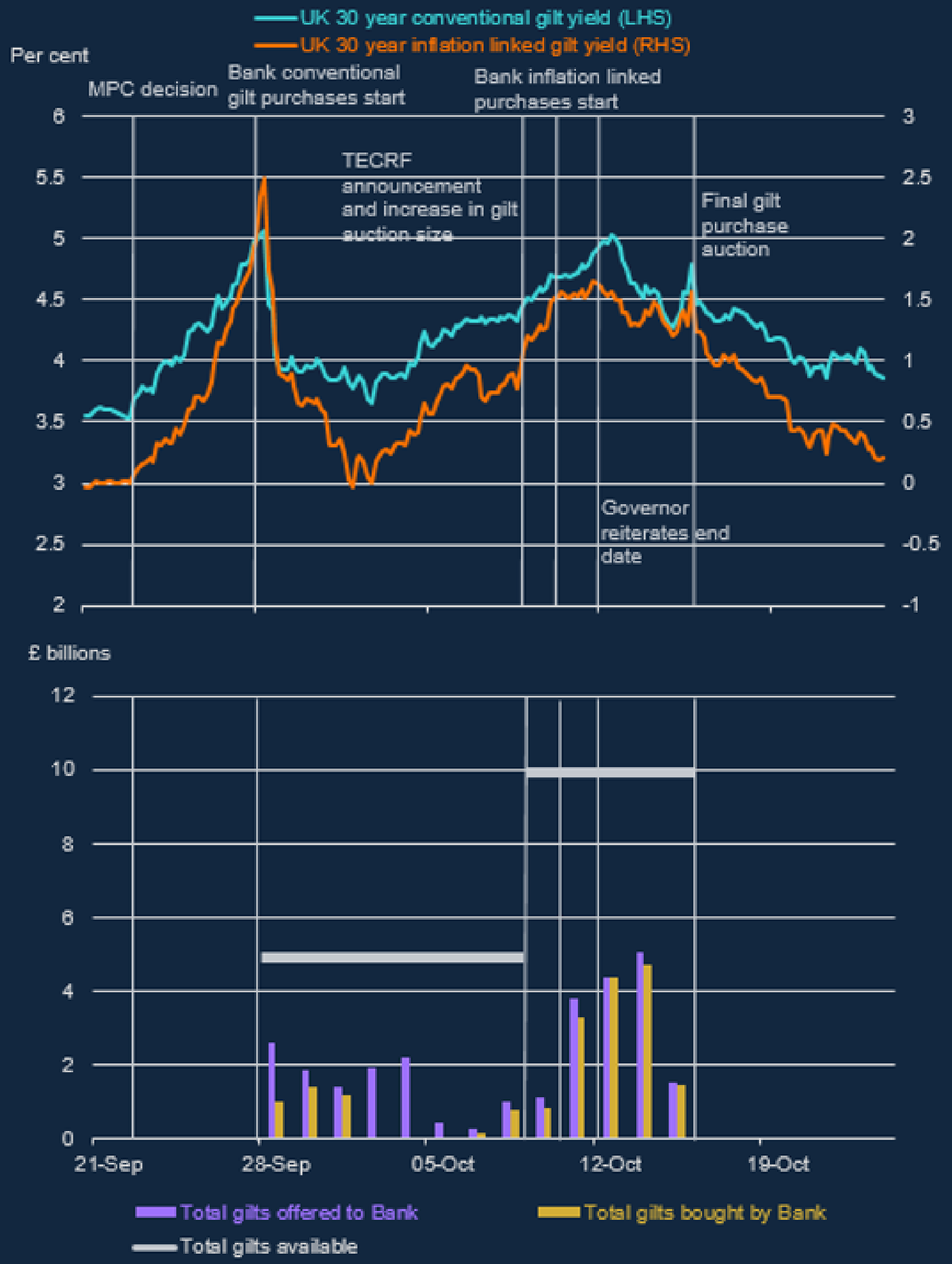
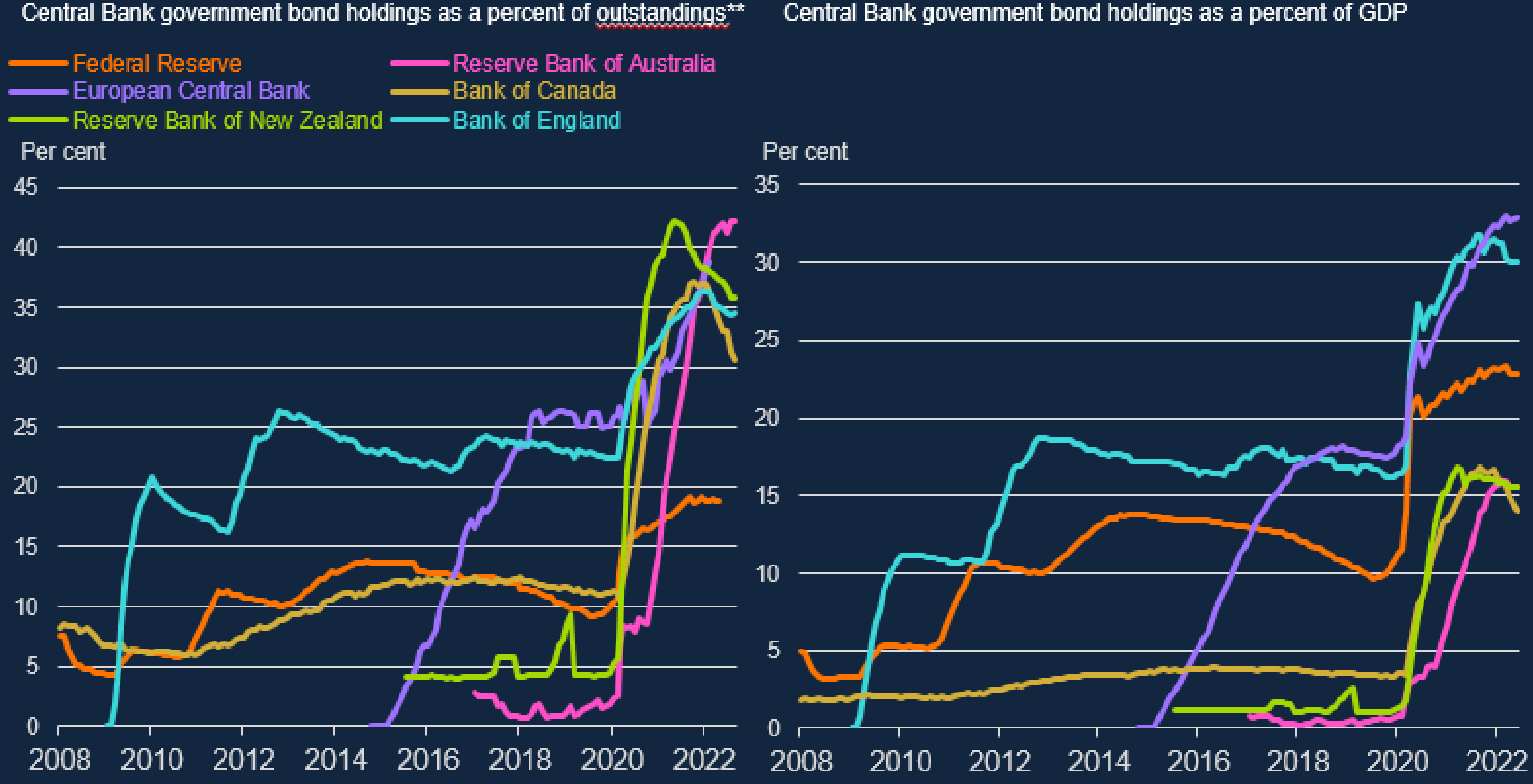


Table 1: Comparing gilt purchases for financial stability & monetary stability purposes

	Financial Stability purchases (October 2022)	Monetary Stability purchases (QE)
Purpose and governance[11]	Aimed at reducing the risk of a self-reinforcing downward price spiral triggered by LDI vulnerabilities. FPC recommended action to tackle financial stability risk; MPC informed, in line with the Concordat regarding balance sheet operations;[12] Bank executive implemented.	QE aimed at easing monetary conditions in pursuit of the inflation target. MPC voted on quantity targets; Bank executive implemented.
Duration of purchases and exit plan	**Temporary**: purchases took place for only as long as required by financial stability issue. Unwind of those purchases to occur in a timely and orderly way.	High level targets for purchase, unwind and sales programmes voted on by MPC as part of its monetary policy process.
Asset selection	**Targeted**: at assets most affected by financial stability issue.	Appropriately broad based to achieve monetary policy goals.
Pricing	**Backstop pricing**: to ensure the facility did not unduly interfere with price discovery or substitute for the need for market participants to manage their own risks over the medium term.	Priced to deliver MPC-determined quantity targets.

Chart 2: Government bond holdings by country*



*Government bond holdings measured at nominal value. Recent temporary and targeted gilt purchases for financial stability purposes are excluded for simplicity

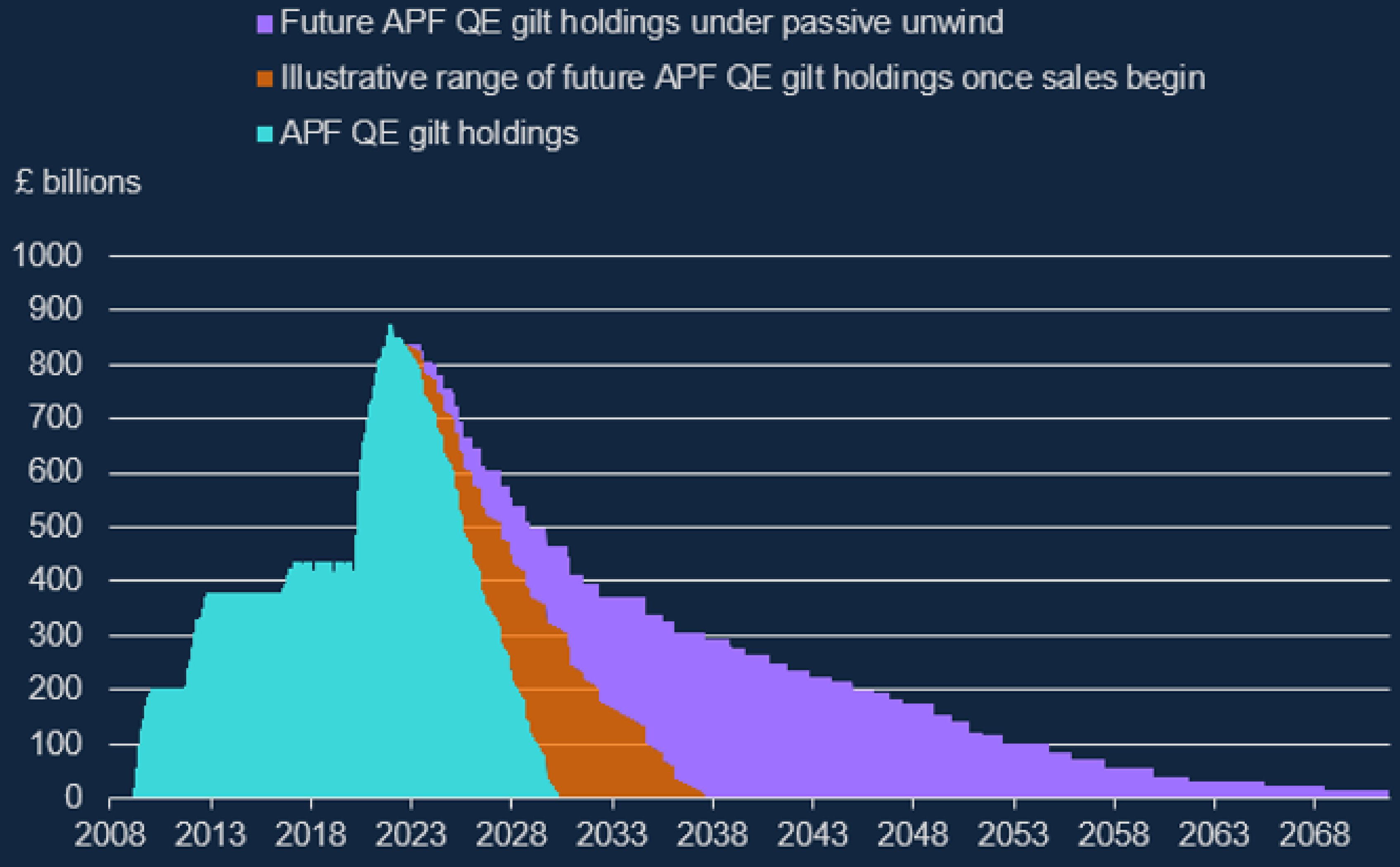
**Share of government debt securities issued by central governments.

Table 2: APF QE maturities over 12 month periods*

£ billions	Gilts	Corporate Bonds
2022/23	35	1
2023/24	49	1
2024/25	87	1
2025/26	52	1
2026/27	38	1
2027/28	36	1
2028/29	41	2
2029/30	54	1

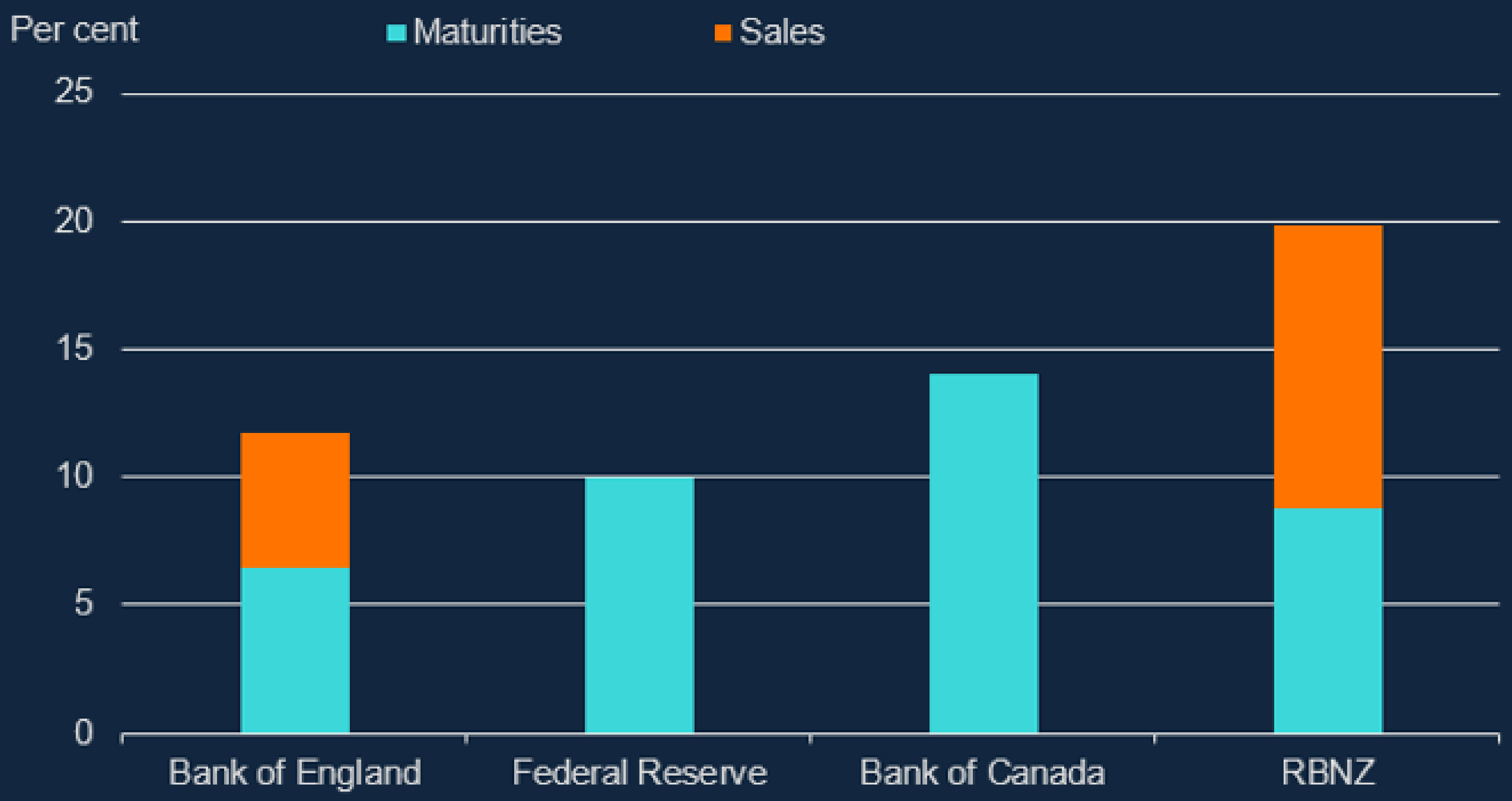
*Data reflect current APF QE holdings; 12 month periods run from 22nd September.

Chart 3: Comparing QE unwind pace under passive and active unwind*



* Range of active sales of between £20 billion and £60 billion per year

Chart 4: Illustrative average annual reduction in QE government debt holdings*



*Shows the average annual rate of respective bond purchase programmes' unwind over the next five years from programme commencement based on latest guidance regarding pace. Where sales are included, the current announced pace is assumed to stay constant for 5 years for illustrative purposes.

Chart 5: Market expectations for QE gilt unwind

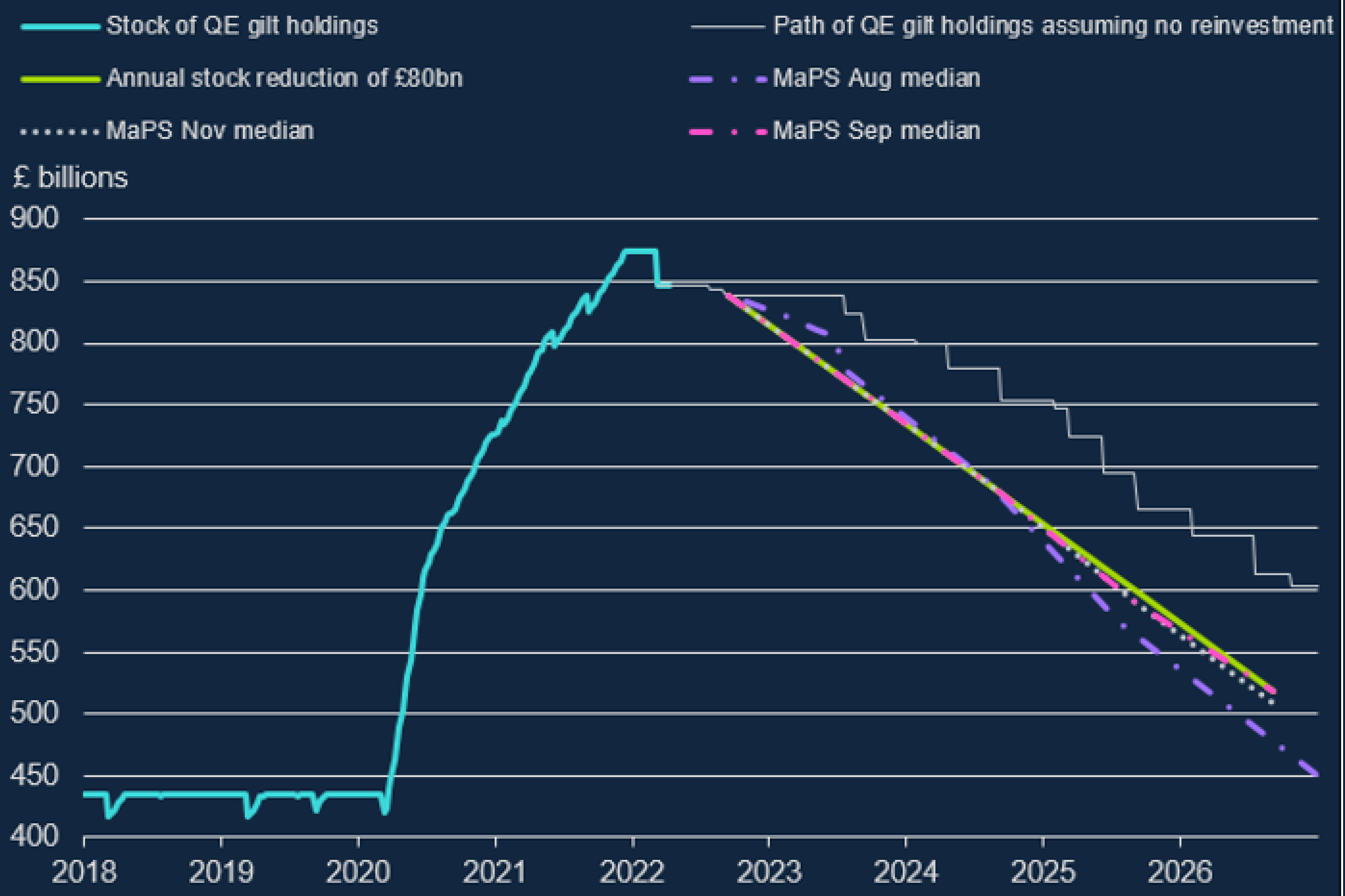


Table 3: Contingency planning during unwind

	Markets volatile but functioning	Market functioning impaired independent of QE unwind	QE unwind judged to be materially impairing market functioning	Bank Rate judged insufficient to meet inflation target
MPC	No change to QE unwind – high bar for changing outside annual review		MPC considers whether to halt or amend sales programme	MPC considers whether to amend sales programme and or recommence reinvestments/ purchases
Bank Executive	Heightened market monitoring	Consider how to adjust timing/design of auctions to respond to conditions	Implements any requested change to MPC strategy	
FPC	Monitor market functioning for potential financial stability risks, judging appropriate actions if such risks crystallise			

Chart 6: Daily indicators of market functioning

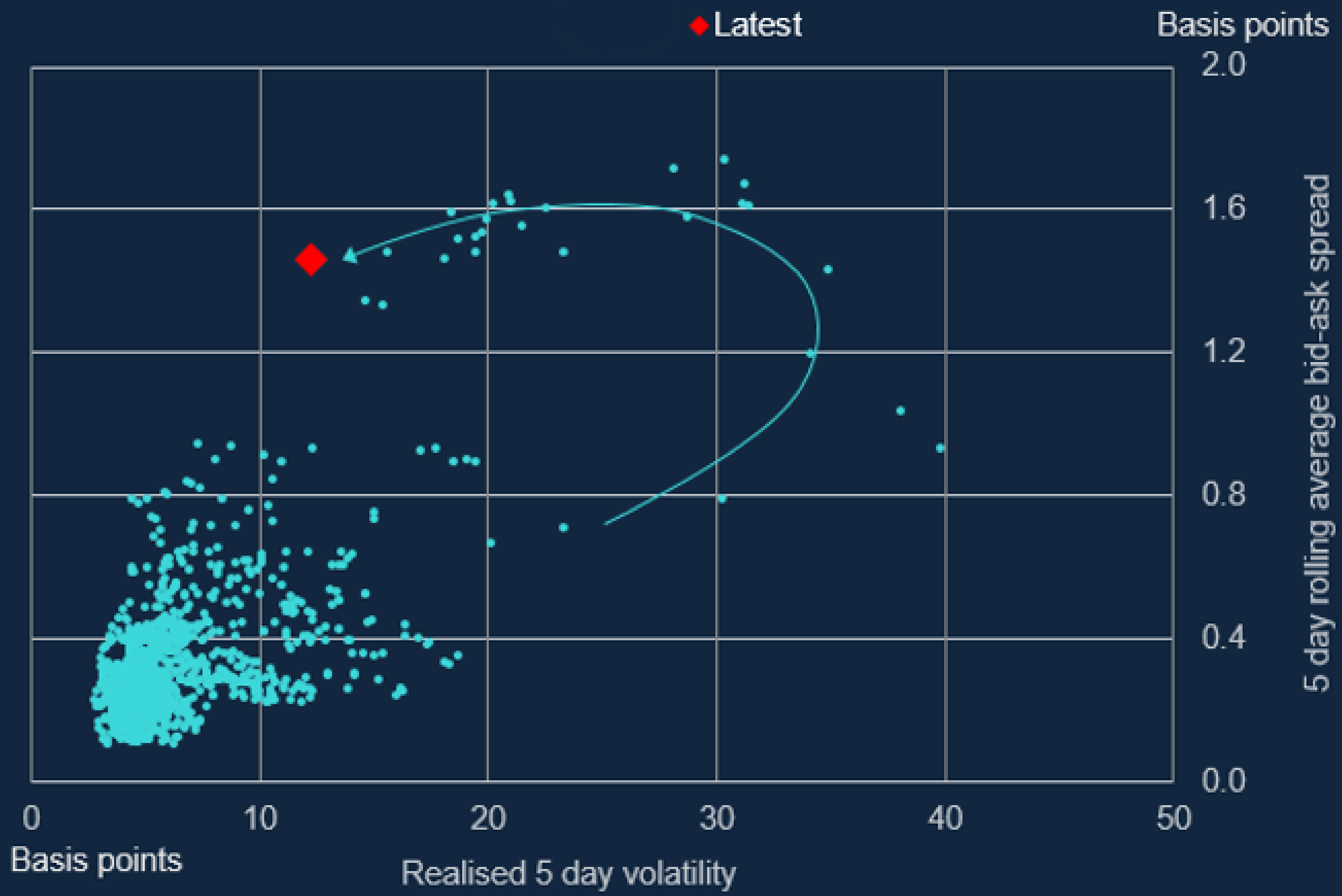
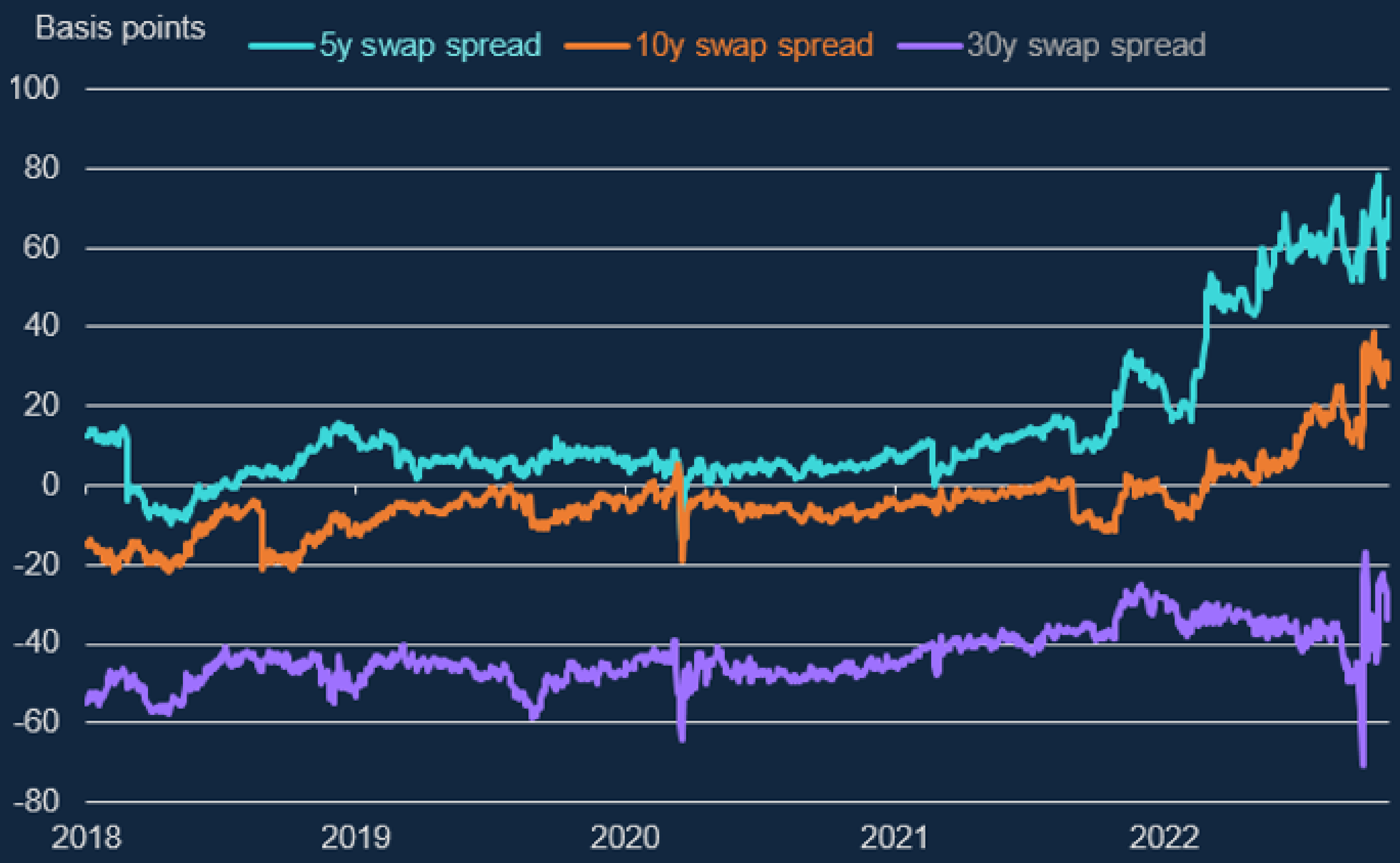


Chart 7: Gilt swap spreads over time



The swap spread is calculated as the difference between the fixed rate on an overnight-indexed swap and the yield on a gilt of an equivalent maturity

Chart 8: Demand for reserves and QE unwind

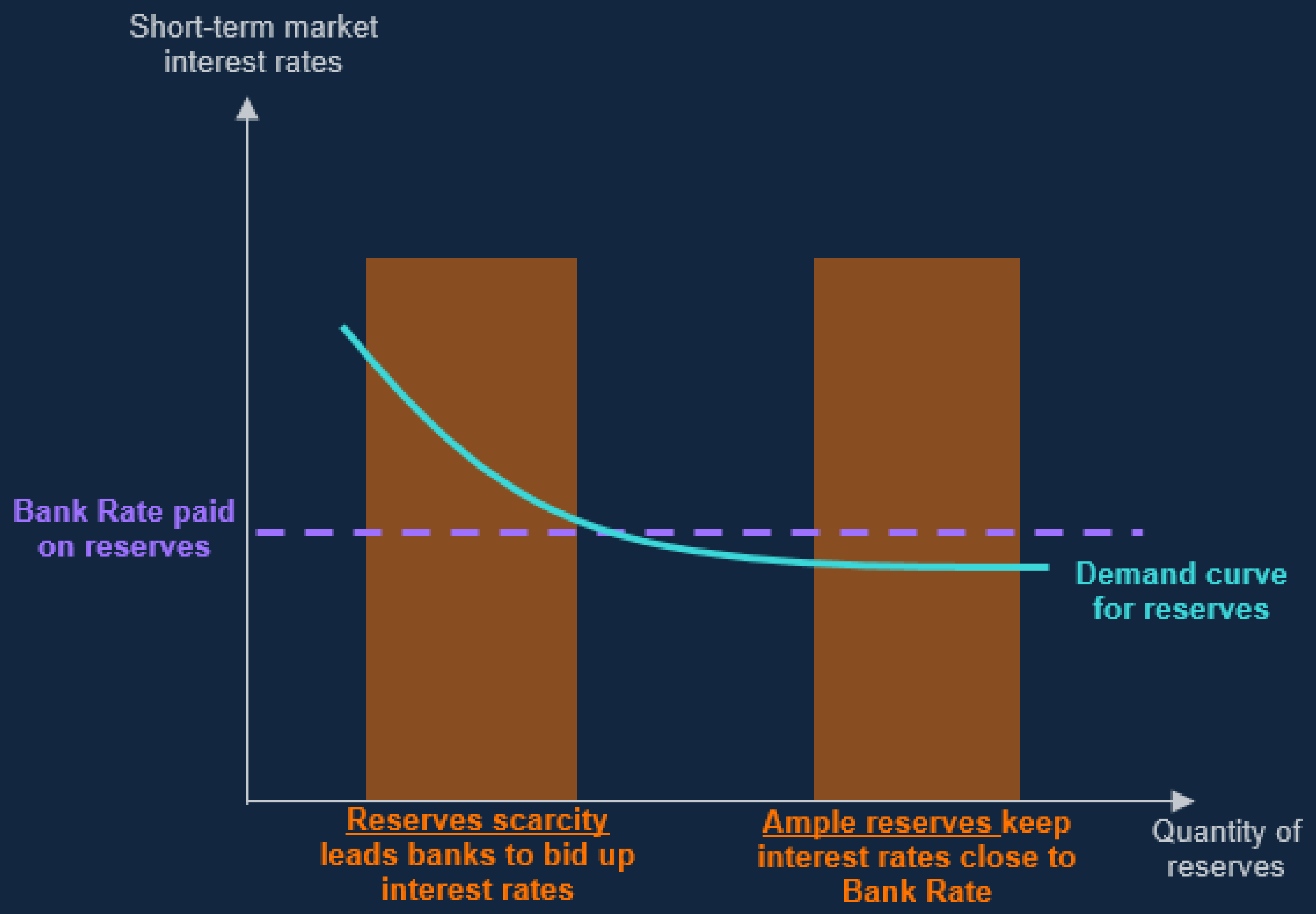


Chart 9: Illustrative projection of aggregate reserves*

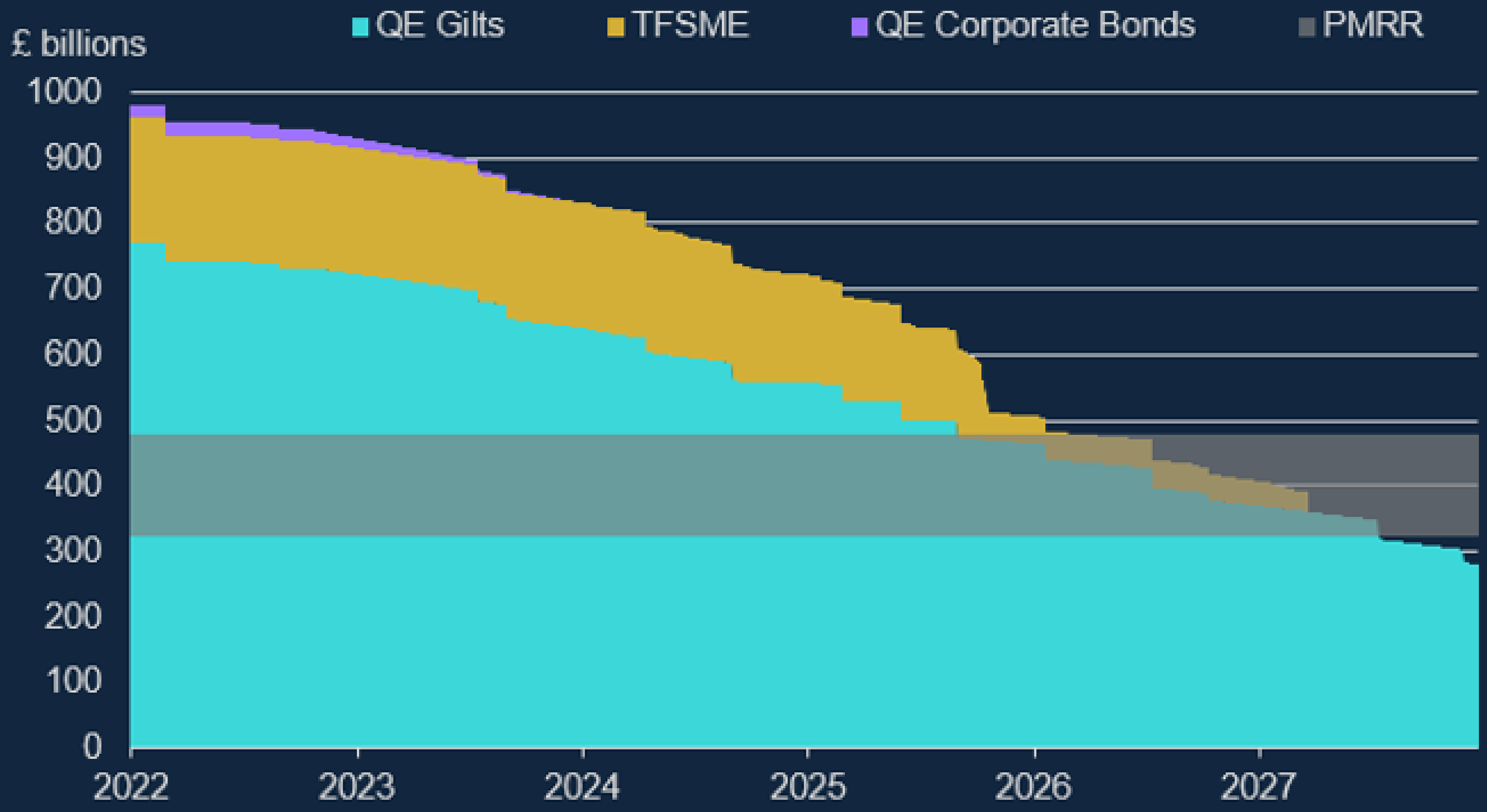


*Chart subtracts asset unwind based on latest guidance from reserve levels as at January 2022. QE Gilt and Corporate Bond unwind pace in line with latest MPC guidance. Assumes no early TFSME repayments, and holds other liabilities on the Bank's balance sheet constant. Recent temporary and targeted gilt purchases for financial stability purposes are excluded for simplicity

Chart 10: 2019 US repo spike