BANK OF ENGLAND

Funding for Lending Scheme: worked examples of borrowing allowance and fee

The following examples illustrate the quantity and pricing of borrowing available from the Funding for Lending Scheme (FLS) under three hypothetical scenarios.

Borrowing Allowance and Fee

The quantity and price of borrowing available to banks and building societies in the FLS will be linked to their performance in lending to the UK non-financial sector, as described more fully in the FLS documentation available via the Bank's website.[1]

Borrowing Allowance

The Borrowing Allowance for each Participant will be 5% of its stock of existing applicable loans as at end-June 2012, plus any expansion of its lending during the 'Reference Period', which runs from that date to the end of 2013.

Fee

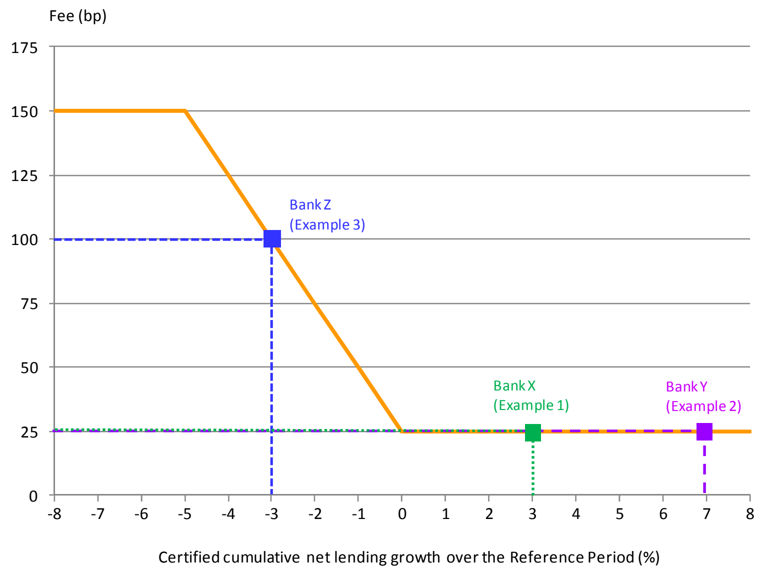
The fee on FLS borrowings is comprised of two parts:

i) The fee on borrowings up to the Borrowing Allowance is determined by the cumulative net lending growth over the Reference Period as a whole. The fee increases linearly from 25bp per annum for positive or stable net lending, up to 150bp pa if lending falls by 5% or more, as shown in Chart 1.

ii) Any 'excess' borrowings above the Borrowing Allowance attract a fee of 150bp pa.

Participants actually *pay* a flat fee of 25bp pa during the Drawdown Period, with any additional fee required on drawings during the Drawdown Period paid after the end of the period.

Chart 1: FLS fee on drawings up to the Borrowing Allowance



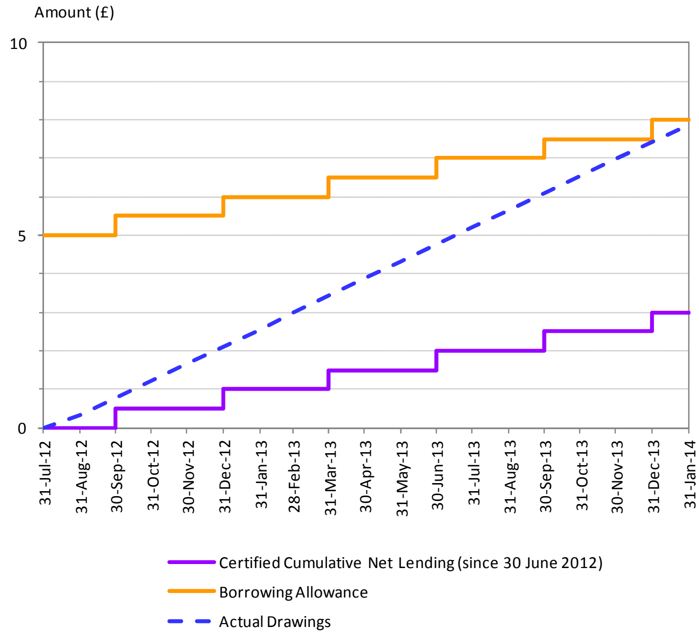
[1] www.bankofengland.co.uk/markets/Pages/FLS/default.aspx

Example 1 – A Participant increases its lending

Bank X certifies a Base Stock of applicable loans of £100 as at 30 June 2012. Bank X therefore has an initial Borrowing Allowance of £5 (5% of its Base Stock).

Bank X increases its net lending over the Reference Period, and certifies lending growth of £0.50 for each quarter during the period, as shown in Chart 2. This results in its Borrowing Allowance increasing by £0.50 each quarter, from £5 at the start of the Reference Period up to £8 at the end. Bank X steadily borrows from the FLS over the Drawdown Period, borrowing up to its maximum Borrowing Allowance by the end of the Drawdown Period on 31 January 2014.

Chart 2: FLS usage by Bank X



Over the Reference Period as a whole, Bank X increased its net lending by 3%, and therefore pays a fee of 25bp pa on all drawings up to its Borrowing Allowance on each day (see Chart 1). Bank X has no 'excess' drawings above its Borrowing Allowance at any point.

Since Bank X already paid 25bp pa on drawings during the Drawdown Period, it does not need to pay anything extra on drawings during the Drawdown Period. It will continue to pay 25bp pa on its outstanding drawings quarterly from the end of the Drawdown Period until its drawings are repaid.

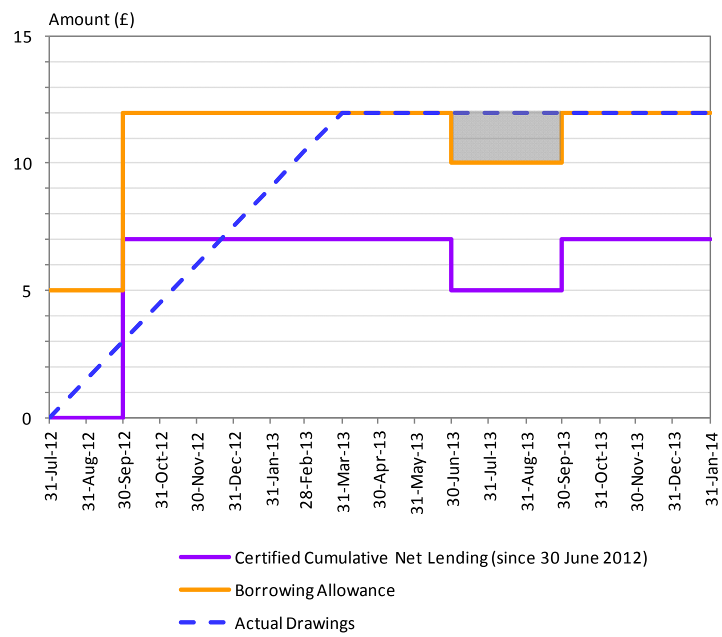
Example 2 – A Participant increases its lending and has a period of excess drawings

Bank Y certifies a Base Stock of applicable loans of £100 as at 30 June 2012. Bank Y therefore has an initial Borrowing Allowance of £5. Bank Y certifies that it had net positive lending flows of £7 during the quarter ending 30 September 2012. This results in its Borrowing Allowance increasing by £7 to £12, as shown in Chart 3. By March 2013, Bank Y had drawn up to this maximum allowance, and maintains this level of drawings for the remainder of the Drawdown Period.

Bank Y certifies that its net lending flows during Q2 2013 were -£2, reducing its Borrowing Allowance to £10. Bank Y does not have to repay its £2 of drawings in excess of its new Borrowing Allowance (represented by the shaded area of Chart 3), but does pay a higher fee on this excess.

Bank Y certifies that cumulative net lending to 30 September 2013 has risen back to £7, and remains at this level.

Chart 3: FLS usage by Bank Y



Over the Reference Period as a whole, Bank Y increased its net lending by 7%, and therefore pays a fee of 25bp pa on all drawings up to its Borrowing Allowance on each day (see Chart 1). Since it already paid 25bp pa on drawings during the Drawdown Period, Bank Y does not need to pay anything extra on drawings during the Drawdown Period up to its Borrowing Allowance. It will continue to pay 25bp pa on its outstanding drawings quarterly from the end of the Drawdown Period until its drawings are repaid.

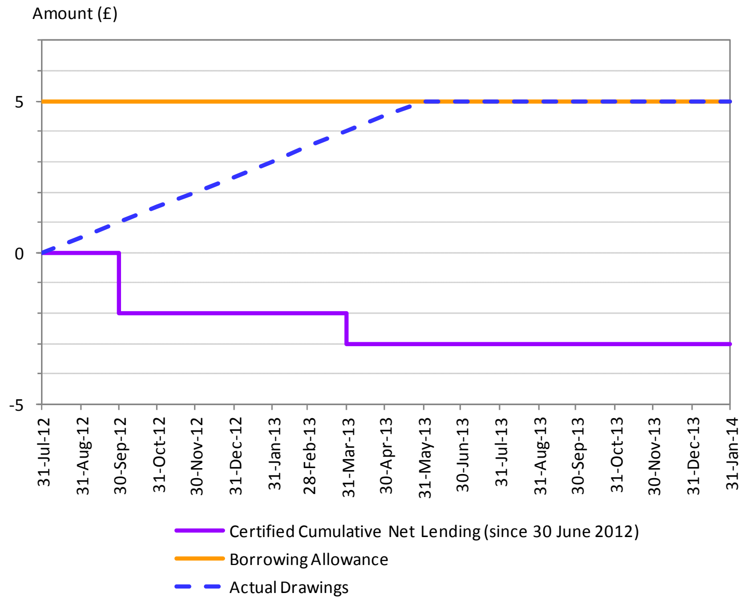
For the period 30 June 2013 - 30 September 2013, Bank Y had £2 of drawings in excess of its Borrowing Allowance. This excess attracts a fee of 150bp pa. Since Bank Y has already paid 25bp pa on these drawings, it will be charged an extra 125bp pa on the excess drawings of £2 for this period. This is paid as a lump sum after the end of the Drawdown Period.

Example 3 – A participant reduces its lending

Bank Z certifies a Base Stock of applicable loans of £100 as at 30 June 2012. Bank Z therefore has an initial Borrowing Allowance of £5. Over the course of the Reference Period, Bank Z certifies that its cumulative net lending is negative, decreasing by £2 over the quarter ending 30 September 2012 and by a further £1 over the quarter ending 31 March 2013.

Since the Borrowing Allowance of an FLS Group remains at 5% of its Base Stock even if net lending is negative, Bank Z's Borrowing Allowance remains £5 during the Drawdown Period. Bank Z draws up to this maximum allowance, as shown in Chart 4.

Chart 4: FLS usage by Bank Z



Over the Reference Period as a whole, Bank Z reduced its net lending by 3%. As illustrated in Chart 1, a 3% reduction in net lending equates to a 100bp pa fee, which is therefore the fee Bank Z is charged on all drawings up to its Borrowing Allowance on each day. Bank Z has no 'excess' drawings above its Borrowing Allowance at any point.

Since Bank Z already paid 25bp pa on drawings during the Drawdown Period, it is charged an additional 75bp pa on these drawings, which is paid as a lump sum after the end of the Drawdown Period. It pays 100bp pa on its outstanding drawings quarterly from the end of the Drawdown Period until its drawings are repaid.