

**BANK OF ENGLAND STERLING MONEY MARKETS LIAISON  
GROUP  
MEETING AT 2:30PM ON FRIDAY 5 OCTOBER**

Ian Plenderleith (Chairman)	Bank of England
Bill Allen	Bank of England
Martin Brooke	Bank of England
Paul Mikhailoff (Secretary)	Bank of England
John Rippon	Bank of England
Alastair Wilson	Bank of England

<b>Ian Firth</b>	Lloyds Bank
<b>Gerard Fitzpatrick</b>	Financial Services Authority
<b>Barry Holland</b>	London Investment Banking Association
<b>Richard Inglis</b>	BHF-Bank
<b>Alice Keegan</b>	CRESTCo
<b>Antony Littleton</b>	Association for Payment Clearing Services
<b>Ian Mair</b>	London Money Market Association
<b>Richard Pattinson</b>	Barclays
<b>Michael Beales</b>	WMBA
<b>Lesley Poltock</b>	J P Morgan
<b>Amanda Sudworth</b>	LIFFE
<b>Jo Whelan</b>	UK Debt Management Office
<b>Jonathan Wood</b>	HSBC
<b>Roger Woodbridge</b>	Halifax

Guests

<b>Pelham Temple</b>	Prebon Marshall Yamane
<b>Gavin Matthews</b>	Prebon Marshall Yamane
<b>Alan Brown</b>	ICAP

**Agenda Item 1 – Introduction**

- 1 Ian Plenderleith referred to the postponement of the meeting originally scheduled for the second week in September. He then ran through the

agenda mentioning that, additionally, Jo Whelan would describe developments in the Treasury bill market. The guests accompanying Mike Beales were welcomed.

## **Agenda Item 2 – Current developments in sterling money markets**

- 2 Martin Brooke described market developments beyond the period covered by the Autumn Bulletin, the meeting having been delayed. He referred to recent reductions in growth forecasts and to the heavy falls in equity markets which were still 30% to 40% off their highs despite a partial recovery. Implied volatility, derived from options on interest rate futures contracts, had also risen sharply. Expectations of official rates likely to prevail at the end of 2001 had fallen since MMLG last met; rates implied by short sterling futures were about 140 basis points lower and eurodollar futures were about 180 basis points lower. The trough in expectations of the Bank's repo rate seemed to be 4 ¼%. The recent rise in long yields could have been because of anticipated government and corporate issuance, revival of EMU entry trades following Mr Blair's recent speech and relaxation of resilience and other regulatory requirements for pension funds and insurance companies.
- 3 Martin Brooke then referred to recent trends in the amounts outstanding of the various sterling money market instruments, CDs contracting while interbank deposits expanded in Q2. He referred to daily broked turnover in the overnight interbank market which was volatile day to day around a figure of some £10 bn.
- 4 The group was asked for its views on the expected floor of 4 ¼% for the Bank's repo rate, whether it thought high implied volatilities arose from uncertainty about growth and inflation and why in Q2 the CD market had contracted while interbank deposits had expanded.
- 5 Members of the group stressed that there were now great uncertainties for the global and domestic economy and it was not easy for the market to anticipate how policy would or should be set. High volatilities reflected these developments, as well as being influenced by the hedging of mortgage products. Markets had also been thin with a preponderance of long positions. One member of the group felt that the recent rise in long yields reflected fears of inflation down the road perhaps exacerbated by fiscal expansion in the US. Liquidation of assets by insurance companies was also said to be a factor behind the rise in long yields. It was stressed that in these times it was impossible to be scientific about the rationale

behind expectations. It was pointed out that the consumer was keeping the economy going at this point; so continuing confidence was essential.

### **Agenda Item 3 – Calculation of SONIA**

- 6 Paul Mikhailoff introduced the Bank's paper to MMLG members in which the history of SONIA was described along with similar products in other markets. The paper explained that the that the Bank had from time to time heard suggestions from some in the market that the calculation of the daily rate could be improved. The Bank, which was neutral on the matter, thought that it was an appropriate topic for MMLG to consider. Were there to be change, options included making the cut-off of 3.30 pm later in the day so that more trades were embraced, taking rates from a panel of banks as opposed to using overnight transactions put through the brokers and including tom/next or even spot/next trades. MMLG were also asked if more data on SONIA swaps would be helpful, amounts outstanding by maturity for example.
  
- 7 Mike Beales spoke for WMBA saying that the cut-off had been extended two years ago, from 3 pm to 3.30 pm, and that WMBA already had it in mind to extend the cut-off again to 4 pm. It had also to be decided how to define trades to be included in the SONIA calculation following the obsolescence of the definition of Section 43 banks at the end of the year. The inclusion of corporate trades would, he thought, have an affect on the SONIA rate. Ian Plenderleith invited others' views. The consensus was clearly that delaying the cut-off was the important change: some 20% of the day's business was thought to be done after 3.30 pm and importantly it was nearly all through the brokers because at that time of day it was far quicker to use the brokers' services rather than ring around. There was agreement that the cut-off should be 4.15 pm which, Mike Beales thought, need not delay the posting of the daily rate too much after 5 pm. The view was to make one change at a time and see the result so that the inclusion of tom/next trades could wait. The establishment of a working group had been suggested but it seemed, Ian Plenderleith said in summarising, that the consensus was clear. There was no wish for a panel, let WMBA change the cut-off to 4.15 pm (which could be done in two weeks) and review again next time. The Bank will help WMBA decide how to redefine the institutions whose trades will be used for the calculation of the daily rate. No wish for more data was expressed.

#### **Agenda Item 4 – Bank of England deposit facility three months on**

- 8 Paul Mikhailoff described the effectiveness of the facility in moderating undue softness in the overnight rate and how the market, having used it only five times in any size and soon after its introduction, had not needed to use it since 22 August. Since then, as had been intended, the existence of the facility had moderated undue softness and put the Bank's operations towards the close of the business day on a symmetrical basis.

#### **Agenda Item 5 – Continuous Link Settlement Bank**

- 9 Alastair Wilson gave an update on progress, summarising the reasons for the delay to the planned start date from October this year to Q2 2002 and explaining the steps being taken to address the problems experienced with the test system earlier in the year. He noted that IBM had allocated significant resources to addressing any remaining problems, with extended testing in "live mode" now planned. Reports from CLS gave grounds for optimism. He also explained the regulatory timetable. MMLG members involved with the project were cautiously optimistic, pointing out that financial penalties were always good incentives.

#### **Agenda Item 6 – Possible Quarterly Bulletin Article on the Work of MMLG**

- 10 Paul Mikhailoff told the group that an article for inclusion in the Winter Bulletin was proposed describing the work and composition of MMLG with mention made of the topics MMLG had covered, including planning for the millennium change, the Non-Investment Products Code, the Money Markets Instruments Review and work on stock lending and repo agreements. The MMLG welcomed this. The MMLG was asked if it saw any objections to minutes of its meetings appearing on the Bank's markets website: this was agreed

#### **Agenda Item 7 - Development of the Treasury Bill Market**

- 11 Jo Whelan said that, in line with the Government's plans to expand the total of bills outstanding to £8 bn by the end of the year, the DMO had made some changes to encourage the expansion of the investor base including a list of Primary Participants (bidding on behalf of customers and giving dealing levels in the bills); the production of an Information Memorandum about the Treasury bill programme; and moving to an earlier closing time for tenders of 11 am. Full details and other information are available on DMO's website ([www.dmo.gov.uk](http://www.dmo.gov.uk)).

## **Agenda Item 7 – Any Other Business**

12 In the absence of other business Ian Plenderleith concluded the meeting and thanked attendees.

Bank of England  
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