

Bank of England Report and accounts 1994



1 March 1994

Report and accounts for the year ended 28 February 1994

Issued by Order of the Court of Directors 12 May 1994

Edward Adam John George, Governor
(First appointed to the Court 1 March 1991
and appointed Deputy Governor 1 March 1992)

Rupert Lavallias Penant-Ross, Deputy Governor

Sir David James Scott Cooksey
(Chairman, Adams Ltd)

Sir Colin Ross Cursons
(Chairman, Redland plc)

Frances Anne Heslop
(Director, Leased Assets & Co., Ltd)

Sir Christopher Anthony Hogg
(Chairman, Economy Holdings plc)

Sir Martin Watfield Joo'ah
(Chairman, P&O/F&L Assurance Management)

Pendrell Hugh Knox
(Executive Director)

Sir John Chipworth, Lindley Kesteven
(Chairman, Bankers' Bank Ltd)

Mervyn Alistair King
(Executive Director)

Sir David Bryan Lees
(Chairman, GKN plc)

Sheila Valerie Maston
(Partner, KPMG Peat Marwick)

Sir Christopher Jeremy Maurice FRCR
(Former Chairman, British Petroleum)

Ian Pinderleith
(Executive Director)

Brian Quinn
(Executive Director)

Sir David Donald Scholey CBE
(Chairman, J D Wadsworth Group plc)

Professor Sir Ronald Smith
(Chairman, Biscuits plc)

Sir Colin Orlove Southwood
(Chairman, THORN plc)

Andrew Crockett resigned on 31 December 1993 and the Bank was represented until 1 January 1994

Sir Adrian Cuddeby, Tony Clarke and Dennis Hill CBE resigned on 28 February 1994 on completing their terms of office. The Governor and the Court of Directors have agreed that Sir Pinderleith will continue until 31 May 1994.

The term of office of Sir David Scholey CBE expired on 28 February 1994. He will be appointed for a further period of one year.

Associate Director

Hugh Christopher Rindley Heald

Secretary of the Bank: G A C. Williams

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Bank of England

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Court of Directors

1 March 1994

	Date of first appointment	Expiry date of current appointment
Edward Alan John George, <i>Governor</i> (First appointed to the Court 1 March 1982 and appointed Deputy Governor 1 March 1990)	1 July 1993	30 June 1998
Rupert Lascelles Pennant-Rea, <i>Deputy Governor</i>	1 July 1993	30 June 1998
Sir David James Scott Cooksey (Chairman, Advent Ltd)	1 March 1994	28 February 1998
Sir Colin Ross Corness (Chairman, Redland plc)	1 March 1987	28 February 1995
Frances Anne Heaton (Director, Lazard Brothers & Co., Ltd)	1 March 1993	28 February 1997
Sir Christopher Anthony Hogg (Chairman, Reuters Holdings plc)	1 March 1992	29 February 1996
Sir Martin Wakefield Jacomb (Chairman, POSTEL Investment Management Ltd)	19 May 1986	28 February 1995
Pendarell Hugh Kent (Executive Director)	1 January 1994	28 February 1997
Sir John Chippendale Lindley Keswick (Chairman, Hambros Bank Ltd)	1 March 1993	28 February 1997
Mervyn Allister King (Executive Director)	1 March 1990	29 February 1996
Sir David Bryan Lees (Chairman, GKN plc)	1 March 1991	28 February 1995
Sheila Valerie Masters (Partner, KPMG Peat Marwick)	1 March 1994	28 February 1998
Sir Christopher Jeremy Morse KCMG (Former Chairman, Lloyds Bank plc)	1 March 1993	28 February 1997
Ian Plenderleith (Executive Director)	1 March 1994	28 February 1998
Brian Quinn (Executive Director)	1 April 1988	29 February 1996
Sir David Gerald Scholey CBE (Chairman, S G Warburg Group plc)	1 March 1981	28 February 1998
Professor Sir Roland Smith (Chairman, Hepworth plc)	1 March 1991	29 February 1996
Sir Colin Grieve Southgate (Chairman, THORN EMI plc)	1 March 1991	28 February 1995

Andrew Crockett resigned on 31 December 1993 and Pen Kent was appointed with effect from 1 January 1994.

Sir Adrian Cadbury, Tony Coleby and Gavin Laird CBE retired on 28 February 1994 on completing their terms of office. Sir David Cooksey, Sheila Masters and Ian Plenderleith were appointed with effect from 1 March 1994.

The term of office of Sir David Scholey CBE expired on 28 February 1994; he was re-appointed for a further period of four years.

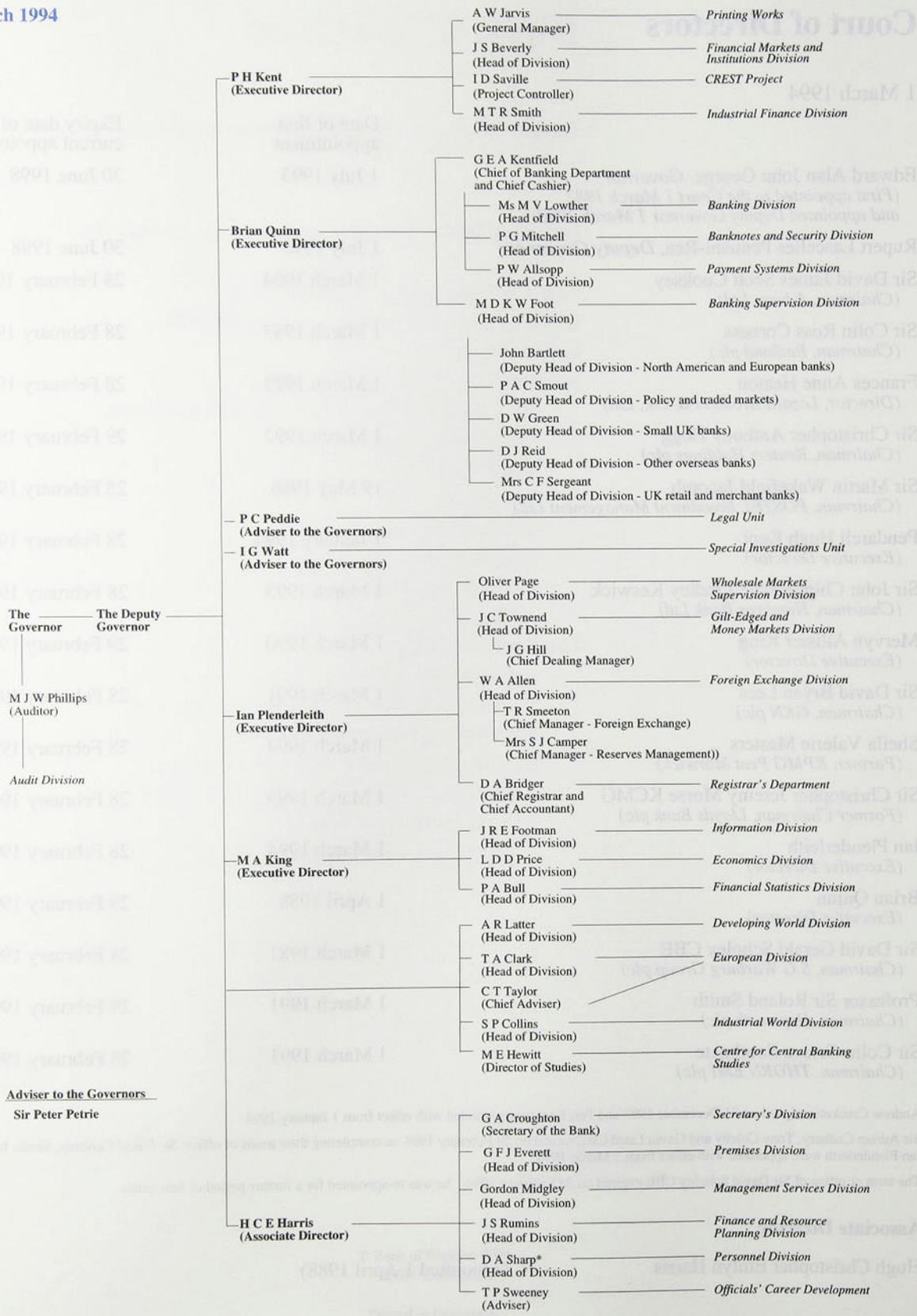
Associate Director

Hugh Christopher Emlyn Harris (appointed 1 April 1988)

Secretary of the Bank G A Croughton

Organisation of the Bank

March 1994



* David Sharp died on 24 March 1994

Foreword

This is my first report as Governor of the Bank, and I am pleased to be able to describe a year of very considerable progress in all of the fields in which the Bank is engaged. That I am in a position to do so is a reflection on the immense contribution of my predecessor, Lord Kingsdown, on my colleagues on the Court of the Bank, and on the staff of the Bank at all levels.

I have also the privilege of being Governor during the Bank's tercentenary year. The celebrations culminate on 27 July 1994, when Her Majesty The Queen will attend a service of thanksgiving at St Paul's Cathedral, and will afterwards visit the Bank. Before that, in June, I am looking forward to welcoming some 150 central bank governors and heads of international financial institutions from around the world to a tercentenary symposium in London, the theme of which will be the evolution and future of central banking. This will underline the Bank's long-standing commitment to promoting co-operation between central banks in the pursuit of monetary and financial stability.

That commitment is reflected also in our continuing active participation in international monetary discussions within the framework of the G7, the G10, the IMF, the BIS and now, the newly established European Monetary Institute (EMI), which took over the role of the EC Governors' Committee from 1 January 1994 in accordance with the Maastricht Treaty. The structural problems within the EU and the strains associated with German unification contributed to further turbulence within the ERM during the year, leading to the widening of margins, to 15%, last autumn. Despite the subsequent relative exchange market calm, there has been a growing recognition that the reintroduction of tight exchange rate constraints would involve considerable risks while the underlying economic imbalances persist. In the meantime, there is general agreement that the EU member states should each individually continue to pursue economic convergence, including domestic monetary stability, while at the same time preparing the infrastructure for an eventual move to Stage III of EMU. The Bank will play a positive part in this, through my own involvement in the EMI Council and through our involvement at all levels in the various EMI Committees and Working Groups.

Our core purposes, as the central bank of the United Kingdom, are to maintain the integrity and the value of the currency (monetary stability), and the integrity of the financial system (financial stability) - related to which is promoting the efficiency of our key financial markets. In the monetary field, we have now 18 months' experience of the monetary framework which was established after we left the ERM in 1992. That has as its main element an explicit inflation target of 1-4%, with an intention to be in the lower part of that range by the end of the present Parliament. It is supplemented by a greater openness in policy-making, including the publication by the Bank of a quarterly Inflation Report,

which provides an objective and entirely independent assessment of the progress being made towards achieving the target. In addition, the papers for (and more recently the minutes of) my monthly policy meeting with the Chancellor are now published.

The objective of policy, and the means by which we intend to achieve it, have never been clearer, and there has been solid and encouraging progress towards our objective. The underlying rate of inflation had fallen to less than 3% by the early part of 1994; at the same time, a steadily rising trend in demand and output seems to have become more firmly established. The foundations are thus laid for steady, non-inflationary growth, and we will achieve that more swiftly, and at less cost, the faster expectations in the economy at large adjust to the low-inflation environment which is now becoming a reality.

I welcome the growing evidence of support for price stability as the primary objective of monetary policy, including from the House of Commons Treasury and Civil Service Committee, which in effect recognised, in its Report last December, that there is no trade-off, in other than the short term, between growth and employment on the one hand, and control of inflation on the other. In this context, while the Government has not accepted the TCSC's recommendation for institutional change, the Chancellor has accepted its proposal for greater openness in the policy-making process by agreeing that the minutes of our monthly monetary meetings should now be published.

The TCSC also endorsed the changes we have made in supervision since the Bingham Report. The Special Investigations Unit has now become fully established, and together with the Legal Unit has provided a valuable additional resource for the supervisors, who have themselves been taking steps to increase their awareness of, and sensitivity to, indications of financial fraud. These changes are reported in more detail in our Annual Report under the Banking Act, which also notes the recovery among the major UK banks from the damage inflicted by the recession, and the significant improvement in the position of the smaller banks, many of which were the subject of intensive monitoring three years ago.

As business conditions improve, companies are likely to turn again to external finance for investment and working capital. The relationship between finance and business has long been an interest of the Bank's, and during the year we have paid especially close attention to the relationship between smaller companies and their bankers. This has for some time been an area of difficulty, amounting on occasions to mutual hostility; and during the year we held discussions with lenders and representatives of small businesses to see what areas of common ground could be identified. The outcome, summarised in a paper issued by the Bank in January 1994, was encouraging. Both the banks and the small firms recognised that there were failings on both sides, and could agree

on many of the changes necessary to improve the relationship. This is an important area of the economy - small firms have accounted for a very large part of employment growth in recent years - and the Bank is continuing to monitor progress and will review the subject again later this year.

We continue to place great emphasis on improving the security of payments and settlements arrangements which are a vital, if often under-appreciated, element in the stability of the financial system. The initiative to convert our large value payment systems to a real-time gross settlement basis has made further progress, and is on track to be completed by 1996. This will reduce risk and increase efficiency in our domestic payments, and also open the way to the reduction of risk in international payments, where simultaneous exchange of value would eliminate the risk of counterparty default. It will also open the way to genuine real-time delivery-versus-payment in securities settlement.

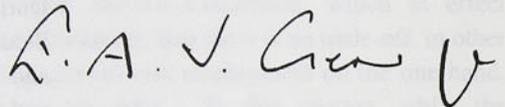
During the year the Bank started Ecu settlement through the European Settlements Office, building on the success of our Central Gilts Office and Central Moneymarkets Office. The Bank's experience in building and operating settlement systems has stood it in good stead for the major challenge of managing the CREST project for equity settlement, which we took on after the report of the Securities Settlement Task Force in June 1993. The design specification was completed on time, in May 1994, and the Bank is now managing the building of CREST which will be owned by a broadly-based consortium of market participants. All of these initiatives will improve the efficiency of London as a financial centre.

Towards the end of 1993 the Directors reviewed the organisation of the Bank and decided to make changes so that our structure could more accurately match our main policy functions. The present organisation chart (page 4) is descriptive more of the Bank's history than of its present responsibilities. The intention is to group together those working on each of our core functions: thus there will be a monetary stability wing, extending from economic analysis through to the dealing desks and their back-offices; and a financial stability wing extending from day-to-day supervision, through supervisory and regulatory policy, and including our work on the financial infrastructure. Several working parties have been refining the new structure, and the changes will be put in place shortly.

I have mentioned already my debt to the staff and to my colleagues on Court. During the year Lord Kingsdown retired after ten years as Governor, during which he served with great distinction and courage, doing much to maintain the Bank's high reputation both at home and abroad. Andrew Crockett has left the Bank to become General Manager of the BIS, having served as the Bank's international Director for nearly five years. Tony Coleby has retired after 33 years in the Bank, having spent much of that period as the Bank's leading official on monetary

affairs. Among our Non-Executive Directors, Sir Adrian Cadbury has retired after nearly a quarter of a century's service to the Bank. Gavin Laird, who served as a Director for eight years, has also retired. Both have made outstanding contributions to the working of Court and will be sadly missed. We welcome in their places Sir David Cooksey and Sheila Masters, who have wide experience of business and government.

As the Bank starts its fourth century we are, as a nation, on the brink of achieving a breakthrough to low and stable inflation. There is a consensus about economic management, and in particular about the risks of inflation. The target is set, and is clear. The instruments of policy are well understood and the way in which policy is set is more open to public scrutiny than ever before. Price stability and sustained growth of output and employment are within reach, and this time we must not let the prize slip from our grasp.



Governor of the Bank of England

Report of the Court of Directors

The Court of Directors is pleased to present its Report together with the audited accounts for the Banking and Issue Departments for the year ended 28 February 1994.

Financial background to the Bank's operations

The Bank of England is the central bank of the United Kingdom. Its core purposes are to maintain the value of the currency and the integrity of the financial system, and to promote the efficiency of financial markets. The Bank does not have as a principal objective the making of profit. Nevertheless it requires income and capital to enable it to meet the costs of carrying out its functions, the majority of which do not in themselves directly generate revenue. The Bank has a responsibility to manage its resources and activities in such a way as not to impose an unnecessary burden on the banking community, whilst satisfying our shareholder, HM Treasury, that we make effective use of our capital, and provide, through payments in lieu of dividend, an appropriate return.

Since 1844, the Bank has, for accounting purposes, been divided into "Issue" and "Banking". The Issue Department is solely concerned with the note issue, the assets backing the issue, the income generated by those assets and the costs incurred by the Bank in printing, issuing and destroying notes. The entire profits of the note issue are paid over to HM Treasury. The Bank does not make a profit on its management of the note issue.

The Banking Department's income derives principally from investments in British government securities, Treasury and commercial bills and advances to customers. The main source of funds is Cash Ratio Deposits (CRDs), which banks in the UK place interest-free with the Bank. The sum each bank deposits is calculated on the basis of the size of its eligible liabilities. These deposits are adjusted twice a year. The investment of these funds, and of the accumulated capital and reserves, produced approximately 70% of the Bank's income in 1993/94. The remaining income is derived mainly from charges to HM Government matching the cost of services provided to them.

The Bank's income is dependent, therefore, on two principal factors - interest rates and the amount of CRDs. In recent years the liabilities on which CRDs are calculated have grown faster than the rate of inflation; and this, together with tight budgetary controls, enabled the Bank, without risk to the security of its income and capital, to reduce the percentage rate for CRDs: first from 0.45% to 0.4% in January 1991, and then to 0.35% in January 1992. The latter was stated to be a temporary reduction; the Bank indicated that it would raise the rate if it became

necessary to do so, and that the rate would revert to 0.4% in 1996 unless the Bank decided otherwise. It has not been necessary to raise the rate in 1993/94.

About 50% of the Bank's costs are staff-related. The Bank therefore attaches considerable importance to ensuring that its personnel are deployed effectively and are properly trained. In recent years the Bank has managed to reduce its staff in total whilst taking on new or increased responsibilities in the areas of supervision, provision of market settlement systems and training for overseas central bankers.

Payment in lieu of dividend to HM Treasury

The Bank of England Act 1946 requires the Bank to pay to HM Treasury, in lieu of dividend on the Bank's capital, a sum agreed between the Bank and HM Treasury. The dividend is paid in two parts. An interim dividend is paid on 5 April, based on provisional figures for the profit for the year. The final dividend is payable on 5 October.

Presentation of the accounts

Banking Department

Although the Bank is not governed by the Companies Acts, the Court of Directors has, since 1971, presented the annual accounts of the Banking Department so as to follow, as far as is appropriate for a central bank, the accounting requirements for banks as laid down in the legislation or in accounting standards and practice. New requirements for the published accounts of banks take effect this year and the Court of Directors has taken the opportunity to review the form in which the Department's accounts are presented. It has decided to continue to follow the requirements for banks in general with the following exception.

In exceptional circumstances, as part of its central banking responsibilities, the Bank may act as "lender of last resort" to financial institutions in difficulty in order to prevent a loss of confidence spreading through the financial system as a whole. In some cases confidence can best be sustained if the Bank's support is disclosed only when the conditions giving rise to potentially systemic disturbance have improved. Accordingly, although the financial effects of such operations will be included in the Department's financial statements in the year in which they occur, these financial statements may not explicitly identify the existence of such support. However, the existence of such support will be disclosed in the Annual Report when the need for secrecy or confidentiality has ceased.

As a result the Department's financial statements disclose less detail than would be required under the Companies Acts of the constituent elements of the profit and loss account, particularly of interest income and expense

and any provisions for bad and doubtful debts, together with consequential restrictions in detailed disclosures in the balance sheet, cash flow statement and the notes to the financial statements.

Issue Department

The accounts of the Issue Department, which are prepared in accordance with the requirements of the Currency and Bank Notes Act 1928 and the National Loans Act 1968, have been revised by giving more detail in the notes to the accounts to assist the reader.

Financial results

The Banking Department accounts for the year ended 28 February 1994 are given on pages 29 - 43 and show a profit after provisions and before tax of £120.2 million, compared with £88.3 million in 1992/93.

The average interest rate during the year was approximately 3 percentage points lower than in the previous year. The value of the CRDs, which remained fairly constant throughout the year, failed to offset the lower interest rates, with the result that net interest income fell by about 16% compared with 1992/93. This re-inforces the need for tight control on costs. Owing to the nature of its activities, the Bank cannot readily adjust its cost base in line with fluctuations in its income. However, as explained on page 23, in the Administration section of this Report, the Bank has maintained tight control over staff budgets in recent years, and aggregate staff remuneration fell once again in 1993/94. The new and increased responsibilities described in the Activities section of the Report have led to modest increases in other items of expenditure. The combined effect of these factors has resulted in operating profit, before exceptional items, being £68 million (38%) lower than in 1992/93.

This year's profit benefits, as an exceptional item, from a release of £10 million of provisions made in previous years in respect of support operations. Last year provisions totalling £90 million were charged against profit, as an exceptional item, in respect of these support operations. The circumstances behind these movements in provisions are discussed below.

After a payment in lieu of dividend to HM Treasury of £48.4 million (compared with £38.1 million in the previous year) and a tax charge of £24.4 million (1992/93 £12.1 million), the profit transferred to reserves amounts to £47.4 million which compares with £38.1 million last year.

The accounts for the Issue Department (which are given on pages 44 to 46) show that the profits of the note issue were £1,117.0 million compared with £1,555.5 million in 1992/93. These profits are all payable to HM Treasury. In accordance with the Currency and Bank Notes Act

1928, the assets of the Issue Department comprise securities of an amount in value sufficient to cover the fiduciary note issue.

Minorities Finance Limited, formerly Johnson Matthey Bankers Limited, which was acquired by the Bank in October 1984, has continued to realise its remaining assets and has declared dividends of £3.0 million, equivalent to its surplus for the year to 31 December 1993. This brings the total dividends to date to £80.6 million, enabling the Bank both to repay the £20.7 million contributed by others under the indemnity arrangements (as reported in previous years) and substantially to cover its own costs.

EBS Investments Ltd, which was acquired as a result of a support operation in the 1970s, was wound up during the year.

Provisions for support operations

As reported last year, the Bank had made provisions amounting to £115 million at 28 February 1993 in respect of indemnities given to lenders to a number of small authorised banks. Of these provisions, £90 million had been charged against profit in 1992/93, and £25 million in 1991/92. These indemnities arose out of arrangements that the Bank put in place in 1991 to support the liquidity of a few small authorised banking institutions, which drew their funds largely from the wholesale markets. As explained in last year's Report, this support was designed to avert the possibility of widespread difficulties in the banking system and in the economy, and was successful in containing the potential problem.

Over the past year, the institutions involved have either successfully re-ordered their affairs and no longer require support, or are winding down their activities in an orderly manner. In the case of the institution which necessitated the major part of the provision, the Bank has taken over the financing from commercial banks - it already, of course, bore the risk. This factor, in conjunction with a modest improvement in the underlying position of the institution, has enabled the Bank to release £10 million of the provisions made in the previous years.

3i Group plc

3i Group plc, in which the Bank has a 14.47% shareholding, has recently announced its intention to seek a Stock Exchange listing during 1994. It is currently intended that this flotation should take place in the summer. The Bank fully endorses this intention.

Premises

The Directors have revalued the Bank's property portfolio and reflected this in the Bank's accounts. This valuation, which has been made by the Directors, having taken professional advice, is in addition to the regular

five-yearly professional valuation which was carried out as at 28 February 1992.

Activities

The Bank's monetary policy operations are described fully in successive issues of the *Quarterly Bulletin*, and the basis of policy is explained in the Bank's *Inflation Report*. A full account of banking supervision is given in the Annual Report under the Banking Act, published alongside this Report. This section of the Directors' Report mainly covers those activities of the Bank that are not otherwise reported on a regular basis.

The note issue

The value of the note issue was £17,163 million at the end of February 1994, £198 million (1.2%) larger than a year earlier.

Value of notes in circulation

£ Millions	End-February	1991	1992	1993	1994
£1 (a)		61	59	58	57
£5		1,373	1,166	1,163	1,135
£10		5,810	5,743	5,348	5,245
£20		4,847	5,288	6,101	6,818
£50		2,375	2,515	2,732	2,884
Other notes (b)		909	1,350	1,563	1,024
Total		15,375	16,121	16,965	17,163

(a) No £1 notes have been issued since 1984.

(b) Includes higher value notes used internally in the Bank, eg as cover for the note issues of banks of issue in Scotland and Northern Ireland in excess of their permitted issues.

Number of new notes issued each year, by denomination

Millions	Year to end-February	1991	1992	1993	1994
£5		507	355	318	325
£10		619	638	752	622
£20		252	489	329	339
£50		24	21	23	22
Total		1,402	1,503	1,422	1,308

The £10 note remains the most commonly issued denomination.

In response to public comment on the new Series E notes, the Bank announced in February 1993 that denomination numerals on these notes would be enhanced. A new variant £5 note was issued from 1 March 1993, and new £20 and £10 notes followed on 27 September 1993 and 22 November 1993 respectively. The Series E £50 note, the last in the Series, was issued on 20 April 1994.

Legal tender status was withdrawn from the Series D £10 note on 20 May 1994.

With the investment in new printing machinery and equipment largely completed, a major programme of retrenchment and refurbishment has been started at the Printing Works. This will allow economies in site utilisation to be achieved, so continuing the trend towards lower staff numbers (shown on page 23) and reduced unit cost.

In April 1994, the Bank's action in relation to the theft of used notes at the Bank of England Printing Works was heard in the High Court and resulted in orders against three former members of staff and their spouses to repay to the Bank sums amounting to £510,000. Costs were also awarded to the Bank. This was additional to the recovery of £170,000 secured from another former employee following criminal proceedings.

Management of the money markets

The Bank's money market operations have continued to be directed to establishing and maintaining short-term interest rates at the officially desired level. These operations are conducted daily, for the most part in the bill market and with the discount houses. Additional techniques are used when the Bank needs to operate on a particularly large scale. From September 1992 to January 1994 the Bank offered a series of temporary facilities to the largest banks and building societies and to the gilt-edged market makers, for the sale and repurchase of gilt-edged stocks and for loans against promissory notes related to Government-guaranteed export credit and ship-building paper. In December 1993 the Bank announced its intention to put these facilities on to a permanent basis, to be offered regularly, twice a month. The facilities were extended to the discount houses, and the rates of interest applied match those in the Bank's bill operations. The first operation on the new basis was conducted on 19 January 1994, with funds passing the following day. The Bank also discussed with the market a Master Agreement to govern sale and repurchase transactions in these operations. This was introduced on 20 April 1994, when the Bank offered to undertake such transactions with all banks in the United Kingdom and for the sale and repurchase of HM Government's non-sterling marketable debt as well as of gilt-edged stocks.

Management of government debt

The large PSBR in 1993/94, originally forecast at some £51 billion, meant the Bank was very active in managing a substantial programme of sales of gilt-edged stock. Gross sales during the year totalled £53 billion, including £1 billion of calls tied up for the 1994/95 financial year.

As in previous years, the Bank established large benchmark stocks, and as yields fell during the course of the year, notably at the long end, new current coupon stocks were created. Ten auctions were held, at broadly monthly intervals, accounting for over half of the funds raised; tap sales accounted for the remainder. The flexibility of this mixed approach to

funding proved valuable: auctions provided the backbone of the funding programme and allowed for the issue of large amounts of stock, while tap sales enabled the Bank to respond quickly to market rallies, notably over the summer.

Early in the year the Bank published two information booklets on the gilt market, targeted at personal and professional investors. The former was widely publicised, and the number of retail bids at auctions has subsequently increased substantially. Over the year there was a notable increase in demand from overseas investors, and net purchases by the monetary sector - which since March 1993 have counted as funding - were also sizeable.

On 17 March 1994 HM Treasury published a Funding Remit. This set both a gilt funding target for 1994/95 and broad parameters within which the funding operations are to be carried out. This initiative by the Chancellor is aimed at clarifying the respective responsibilities of the Treasury and the Bank in the funding programme.

On 20 December 1993, the Chancellor announced that the Government intended to repay, in advance of final maturity, the ECU 5 billion revolving credit taken out in September 1992. Tranches of the credit, which was fully drawn, were repaid over the following four months at their respective rollover dates. Of the Government's other foreign currency debt, both the D-Mark and eurodollar bonds have performed well since launch and have continued to be actively traded.

Turnover and new issues in the Ecu bond and money markets increased towards the end of 1993. In part, this reflected the composite character of Ecu securities offering exposure to a range of European markets with reduced currency risk. As confidence returned to the Ecu market, the Bank reverted, in May 1993, to the normal procedures for the regular monthly tender for ECU 1 billion Treasury Bills, explained in last year's Report; tenders have been oversubscribed, with turnover averaging around ECU 1½ billion per month in the first quarter of 1994, down from the high levels in early 1992. The January 1994 tender launching ECU 1 billion 1997 Treasury Notes (the third three-year Note in the programme) was oversubscribed and tightly priced. It has traded well and was re-opened by tender in an auction held on 19 April 1994 and may be re-opened again in July and October 1994. Turnover in the outstanding Notes has remained steady, averaging ECU 1-2 billion per month.

Management of the stock registers

1,041,684 transfers of stock were registered in 1993/94, a decrease of almost 8% on 1992/93. 532,813 transfers were effected through the Central Gilts Office, representing 51% of the total.

Transfers registered

Thousands	Year to end-February	1991	1992	1993	1994
Stock transfer forms		578	474	609	509
Electronic transfers through					
Central Gilts Office		473	433	523	533
Total		1,051	907	1,132	1,042

The nominal value of British government securities managed by the Bank rose by over 30% to £193,656 million; but the total of other securities under management fell by almost 5% to £3,322 million. The number of accounts fell by almost 7% to 1,165,973, of which 1,155,155 related to British government securities.

Securities in issue under management at the Bank of England

£ millions nominal

	End-February	1992	1993	1994
British government securities:				
Registered stock		124,538	148,343	193,630
<i>of which index-linked</i>		13,348	16,362	21,395
Bearer bonds		37	32	26
		124,575	148,375	193,656
Other securities:				
Government-guaranteed		428	257	224
Commonwealth and overseas		3,262	3,027	2,990
Local authorities		41	41	41
The Agricultural Mortgage Corporation plc		131	121	22
Other		45	45	45
		3,907	3,491	3,322
Total		128,482	151,866	196,978

Payment and settlement systems

(i) Large value payments

Last year's Report noted that, in discussing ways to eliminate risks in London's wholesale payments systems, the Bank and the Association for Payment Clearing Services (APACS) had reached agreement in principle to develop the present Clearing House Automated Payment System (CHAPS) into a real-time gross settlement system (RTGS), and that work had begun on drawing up the detailed system specification. This activity culminated in the issue of a Statement of User Requirements and Procedures in November 1993 and the production of an outline plan for

subsequent stages of work. The proposals set out in these documents were widely supported. Work has therefore started on the build stage of the RTGS programme by the Bank and the CHAPS and Town Clearing Co Ltd (co-ordinated by APACS). This stage is expected to be completed by Spring 1995. This will then lead to the implementation stage, with a phased implementation planned to start before the end of 1995.

(ii) European Settlements Office

The book-entry transfer system for Ecu-denominated securities, development of which was announced by the Bank in August 1992, was inaugurated, as planned, in August 1993. The new service, the European Settlements Office, provides same-day settlement facilities which are expected to be of benefit in particular to the wholesale end of the market, and is linked to the Euroclear and CEDEL settlement system in continental Europe. By Spring 1994, the system covered 130 securities and had 25 members.

(iii) CREST

Following the decision by the Stock Exchange to abandon TAURUS in March 1993, the Bank established, at the Stock Exchange's request, a Securities Settlement Task Force to make proposals on the way forward for equity settlement in the UK. The Task Force, chaired by Mr Kent, recommended in June 1993 that the UK equity market should move to rolling settlement, beginning with a ten-day cycle in July 1994 and moving to a five-day cycle in early 1995; the Stock Exchange has since chosen 18 July 1994 for the start of rolling settlement. The Task Force further proposed that the Bank should prepare a design for a replacement settlement system to be known as CREST. This will provide an electronic book-entry transfer system which will reduce cost and risk by enabling members to hold stock in dematerialised form and by allowing delivery versus payment. Investors will, however, still be able to hold stock in paper form if they wish. CREST can be introduced with relatively little change to the law, since it will continue to rely on the company register for full legal title; it will, however, as a corollary require major improvements to registrars' systems, so that full legal title can normally follow within two hours of the movement of equitable title in CREST.

The Bank set up a project team, reporting to Mr Kent and to a widely based Steering Committee from the equity industry. As well as working on the design of CREST, the team has been assisting the Stock Exchange in delivering its rolling settlement objectives.

The Bank has undertaken a significant campaign of consultation and discussion, issuing newsletters and consultative documents and participating in roadshows, conferences and bilateral meetings with a

large number of participants from all sectors of the equity industry. The culmination of this process was the publication of several papers setting out the basis for the development of CREST. The final business requirements for CREST were issued in February 1994, after intensive consultation on a draft issued (in parts) in November 1993 and January 1994; a paper (by HM Treasury) on the legal issues was issued in May 1994; and details of the computer plans, including estimates of the time and cost to build the system and an independent audit, were issued in April and May 1994.

Following extensive consultation, the team delivered a complete design specification for CREST on 3 May 1994, with a recommendation that the building of the system start immediately. This recommendation was accepted by the Governor. CREST will be built by the Bank, which will continue to act as project manager during this phase. It will eventually be owned by CRESTCO, a separate company to be set up early in the build phase by a widely-based group of equity market participants. The Bank had received, by end-April, advance commitments from a sufficient number of potential owners (and users) to secure funding and make CREST viable: further commitments are expected before the ownership group is finalised on 31 May. Once the ownership structure is in place, the Bank will recover its costs for the design and build phases from the owners. The owners will also be responsible for choosing an operator to administer the system, making CREST operational and determining pricing policy and future development plans. CREST is expected to begin operations in late 1996.

European Community developments

During July 1993 there was renewed and intensified pressure on the Exchange Rate Mechanism (ERM) which led to the decision on 2 August to substitute 15% fluctuation margins for the previous margins of 2¼% and 6%. Although sterling left the ERM in September 1992, the UK - represented by HM Treasury and the Bank - participated fully in the discussion leading up to this decision, both in the Monetary Committee and in the subsequent meetings of Ministers and Governors.

The other main European development of significance for the Bank was the ratification, on 1 November 1993, of the Maastricht Treaty and the subsequent coming into effect, on 1 January 1994, of Stage Two of Economic and Monetary Union. Stage Two has several implications for central banks and for the public finances. It forbids central banks from lending to the public sector and prohibits measures which give the public sector privileged access to private savings. Stage Two also involves the setting up of the European Monetary Institute (EMI). The role and functioning of the EMI were described in an article in the February 1994 edition of the Bank's *Quarterly Bulletin*. The Bank will be engaged in the EMI's work at all levels, from the Governor's participation in the EMI Council (the EMI's senior decision-making body) to the various

sub-committees and working groups dealing with particular subjects. Like its predecessor, the Committee of EC Central Bank Governors, the EMI will provide a forum for central banks to discuss and review exchange rates and the operation of monetary policies; responsibility for those policies remains, however, clearly in the hands of the national authorities. The EMI is also charged with undertaking a range of preparatory work for a move to the third stage of monetary union. Several members of the Bank's staff are already on secondment to the EMI, and others are likely to go there during 1994.

Administration of financial sanctions

The Bank has continued to administer on behalf of HM Treasury the restrictions on Iraqi assets and on those of Serbia and Montenegro. In addition, the Bank took on responsibility for administering sanctions on certain assets of the military authorities in Haiti, and on assets of the Government of Libya.

Money laundering

The Bank has continued to play a full part in developing measures to combat money laundering. In October 1993, the Joint Money Laundering Steering Group, chaired by the Chief Cashier, published revised Guidance Notes to assist financial institutions by providing a practical interpretation of the Money Laundering Regulations 1993 (which came into effect on 1 April 1994). These Regulations, together with the Criminal Justice Act 1993, implement in UK law the provisions of the EC Directive on Money Laundering.

Financial Fraud Information Network

The Financial Fraud Information Network (FFIN) has been increasingly active throughout the year in the exchange of information which may point to financial fraud or other criminal activity in the UK financial system, and in identifying appropriate courses of action. The members of FFIN are drawn from UK regulatory and supervisory bodies, government departments and investigatory and prosecutory agencies. Mr Watt, Head of the Bank's Special Investigations Unit, is the present Chairman, supported by a Secretariat provided by the Securities and Investments Board.

Industrial finance

The Bank has continued to promote the London Approach as a flexible framework enabling banks collectively to reach orderly and well-founded decisions about their continued support for companies facing financial difficulty. As the economy has emerged from recession, there have been fewer calls on the Bank to assist in smoothing the path to eventual agreement on the terms of a workout. The London Approach is kept

under review to ensure that its effectiveness is not impeded by financial innovation or market practice. The Bank has taken an active part in discussions throughout the year on a number of issues, including the high level of fees associated with workouts and the impact of the emerging secondary market in impaired debt on restructuring negotiations. Discussions with the banking community disclosed no support for a moratorium on the secondary trading of impaired debt during a company restructuring, but it was nevertheless felt to be helpful if the spirit of the London Approach was embraced by new investors.

During the year the financing of small firms has been much debated. The Governor held a series of discussions involving the banks, the CBI, small firms' representatives, government departments and academic specialists to clarify the availability of appropriate finance for small firms. The Bank presented the main themes to emerge from the discussions in January 1994, in its paper entitled Finance for Small Firms.

PRONED

In January 1994 the sponsors of PRONED announced the sale of the company to its management in partnership with an executive search firm, Egon Zehnder International. The Bank, together with the other sponsors, had earlier decided that it was in PRONED's best interest to go into commercial ownership. This partly reflected the fact that the original aim of the sponsors in setting up PRONED in 1982 - to increase the awareness of the importance of non-executive directors - had been largely met.

Training and technical assistance in central banking

There has been continued strong demand from other central banks for training and technical assistance from the Bank of England during the past year. Much of the Bank's effort has been directed at Central and Eastern Europe and the former Soviet Union. In these countries, the movement towards a market-based economy has imposed on central bank officials a steep learning curve in developing market techniques and good supervisory practice. The Bank has contributed by providing training and advice reflecting the importance it attaches to the promotion of international monetary and financial stability.

The Bank's international training and technical assistance are co-ordinated by its Centre for Central Banking Studies. 23 courses were run here in 1993/94, of which 9 were short, specialist programmes for up to 6 participants. In total 326 foreign central bankers attended courses held in London. Of equal and growing importance are the courses which the Bank has run abroad, where 607 participants attended a total of 24 courses. The Bank has recognised the need to alter course content progressively to reflect the rapidly developing expertise in many countries. The key areas where training is most needed remain those

associated with the operation of monetary policy, banking supervision and payments systems, but the range of subjects and the content of courses are becoming increasingly specialist. To date, over 2,000 foreign central bankers and others from over 100 different countries have attended our courses or seminars.

The Bank continues to provide technical assistance to foreign central banks by way of short-term, often recurring, assignments and longer-term secondments. Over the past year some 40 short-term visits have been made to give advice on subjects such as public debt management, monetary operations, banking supervision, financial statistics, human resources management, security arrangements and even the design of central bank buildings. On many of these short-term assignments, Bank officials have acted as expert members of IMF technical assistance missions.

Public accountability

The Bank recognises the need to account for its actions to Parliament and to the wider public. This Report, and the Annual Report under the Banking Act, provide us with opportunities to explain our policies and actions. Evidence given to Parliamentary Committees provides another opportunity. During the past year the Governors and other officials have appeared four times before the Treasury and Civil Service Committee of the House of Commons, and written evidence was submitted to the European Communities Committee of the House of Lords. In addition, through membership of the Industry and Parliament Trust and through other means, the Bank has sought opportunities for briefing Members of Parliament about its activities.

The greatly increased openness of the monetary policy process, including the publication of an independent, quarterly *Inflation Report* and the publication of the minutes of the Governor's monthly meetings with the Chancellor, also helps the Bank to explain its policies more fully.

The Bank endorses the principles underlying the Citizen's Charter and seeks to apply its principles in its dealings with customers and the public. During the year guidelines have been issued within the Bank requiring prompt and full responses to all public letters and telephone calls received, and arrangements for monitoring performance have been established.

Each year the Bank deals with over 40,000 requests for information from the public; several free fact sheets are available to answer the most frequently asked questions. In November 1993, the Bank published "Money in the Bank", a leaflet alerting the public to the risks of unauthorised deposit-taking and explaining how to check whether those soliciting deposits are properly authorised. This was widely distributed,

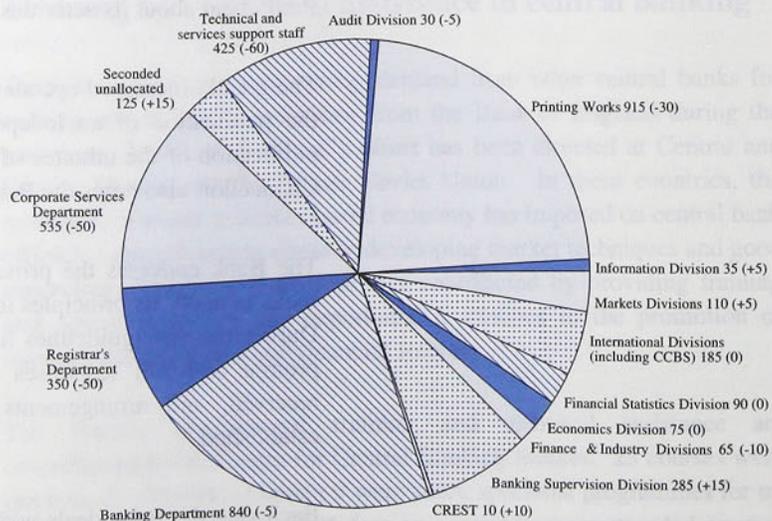
including through the Post Office, as was the guide to the gilts market referred to above.

Many people learn about the Bank by visiting the Museum. At 104,000, the number of visitors during the year held up well against the decline in museum attendances generally, with the result that it ranks 25th out of the 950 or so independent museums. For groups who book in advance the Bank offers a range of presentations in the Museum cinema which can be tailored to suit requirements. Three special exhibitions were held during the year.

Administration

The average number of people employed by the Bank and its subsidiaries during the year was 4,440, of whom 4,287 were employed by the Bank itself. The aggregate remuneration was £99 million. In 1992/93 the average was 4,570 (of whom 4,416 were employed by the Bank). The aggregate remuneration was £101 million. At 28 February 1994 the Bank employed 3,905 full-time staff, 290 permanent part-time staff and 50 staff temporarily working part time upon return from maternity leave; of these, 300 full-time and 80 part-time staff were engaged on fixed-term contracts. The distribution at the year-end is shown in the following chart; staff not working on a full-time basis are included pro rata.

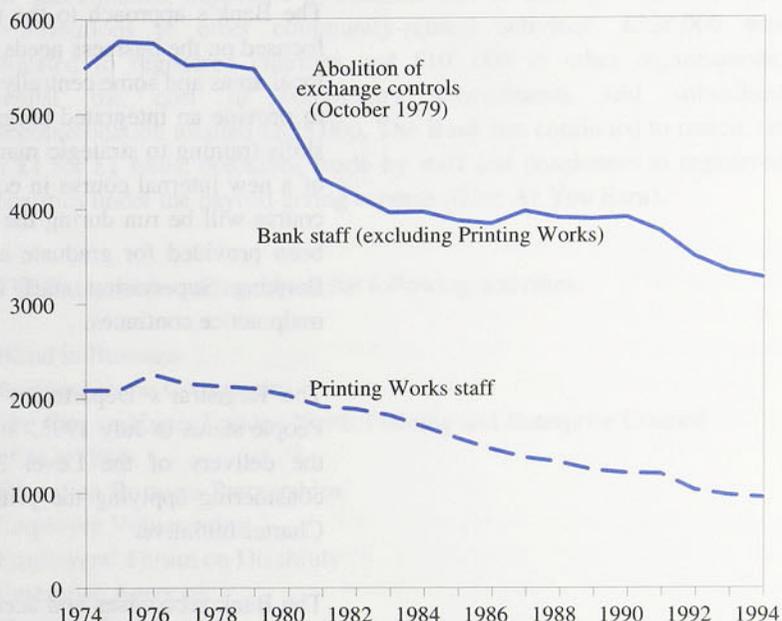
Staff numbers at end-February 1994



Banking Supervision Division figures include the Special Investigations and Legal Units. Figures in brackets are changes against 28 February 1993.

The Bank remains determined to ensure tight budgetary control over all its functions. Since staff account for a large proportion of the Bank's expenditure, staff budgets have been tightly controlled in recent years. The chart below shows the extent to which the Bank's staff has fallen since the peak of 1976. Part of the fall is accounted for by the abolition of exchange controls in 1979; but most by the continuing search for greater efficiency and economy in the use of staff.

Numbers of staff employed by the Bank at end-February



At 28 February 1994, 21 members of the Bank's staff were on secondment overseas with other central banks, governments, international institutions and UK missions. Another 22 staff were with UK organisations such as the Panel on Takeovers and Mergers, government departments and banks. These are additional to the community secondments referred to on page 25. The number of inward secondees to the Bank from UK and overseas organisations was 21.

Employment policies

The Bank attaches great importance to the implementation of its equal opportunities policy: this seeks to ensure that job applicants and members of staff receive equal treatment, regardless of sex, ethnic origin or disability. Annual statistical monitoring is in place which will indicate how effectively this policy is working. Equal opportunities training is provided to staff via workshops and seminars; in 1993 this was supplemented by the launch of inter-active computer training for 1,000 staff in operational and shift-working areas. The Bank participates in the

Windsor Fellowship scheme, and has so far sponsored 7 ethnic minority students. Action for disabled staff includes improved access to premises and the use of sheltered placement schemes: in addition, the Bank continues to be used as an example of best practice, and was invited last year to make a presentation to the European Commission on integrating disabled staff. The Bank's goals under Opportunity 2000 include a commitment to develop wider flexible working practices: local areas are in the process of identifying jobs suitable for flexible working across the Bank. There are currently 27 women on a career break.

The Bank's approach to the training and development of staff remains focused on the business needs of the Bank. Some training is delivered by local areas and some centrally by the Training Centre, the intention being to provide an integrated programme ranging from technical, job-related skills training to strategic management for senior managers. The design of a new internal course in economics has been completed, and the first course will be run during the summer of 1994. New courses have also been provided for graduate entrants and their managers. Training for Banking Supervision staff in the detection of financial fraud and malpractice continues.

The Registrar's Department in Gloucester was awarded Investors in People status in July 1993. It has since become an accredited centre for the delivery of the Level 2 Business Administration NVQ, and is considering applying the principles recommended by the Management Charter Initiative.

The Bank recognises and accepts its responsibilities as an employer for ensuring the health, safety and welfare of all its staff, members of the public, visitors and contractors working on its premises. As required by current legislation, the Bank is undertaking continuing risk assessment supported by a training programme. The Bank's Health and Safety Policy is reviewed and revised on a regular basis to reflect changes in legislation. Health and safety is regarded as a prime management responsibility.

The Houlton-Norman Fund

To mark the Bank's tercentenary, the Directors have approved an endowment of £500,000 to increase the resources of the Houlton-Norman Fund. The Fund, which was established at the time of the Bank's 250th anniversary in 1944, finances academic research into subjects relevant to central banking. Since 1981 fellowships have been tenable at the Bank, encouraging interaction between the Houlton-Norman Fellows and the staff economists. The increase approved by Court has doubled the resources available to the trustees, and, for 1993/94, three fellowships have been granted: to Professor John Campbell to undertake research on "index-bonds, inflationary expectations, asset pricing and monetary policy"; to Professor Richard

Dale to conduct research into "the prudential regulation of securities firms within the single European market"; and to Professor Gary Gorton on "bank loan pricing and the monetary transmission mechanism".

Community involvement

In addition to the extra contribution of £500,000 made to the Houblon-Norman Fund as described above, the Bank contributed a further £1,266,000 in support of its community programme. This covers the cost of secondments, donations to charities and to academic research, and contributions to other community-related activities. £328,000 was donated to registered charities and £103,000 to other organisations, whilst the cost of community secondments and subsidised accommodation totalled £835,000. The Bank has continued to match, on a £1 for £1 basis, donations made by staff and pensioners to registered charities under the payroll giving scheme (Give As You Earn).

The Bank continues to support the following activities:

- Blind in Business
- Business in the Community
- The City and Inner London North Training and Enterprise Council (CILNTEC)
- Education Business Partnerships
- Employee Volunteering
- Employers' Forum on Disability
- Enterprise Agencies
- Hackney Task Force
- The Industrial Society
- The Local Recruitment Brokerage
- Making Training Work
- The Meningitis Trust
- National Star Centre for Disabled Youth
- North Peckham Task Force
- Opportunities for People with Disabilities
- Prince's Trust Volunteers
- Project Fullemploy (within GrandMet Trust)
- The Spastics Society's Fast Track Programme
- Spitalfields Community Job Link
- The Trident Trust
- The Willow Trust
- Windsor Fellowship
- Workwise
- Youth Training

As at 28 February 1994 there were 14 members of staff on community secondments. Staff are also given time off to serve their local communities, for example as school governors and as magistrates.

No donations have been made for political purposes.

Governance of the Bank

Under the Bank of England Act 1946 and the Charters of the Bank of England, the Court of Directors is responsible for the affairs of the Bank. The Governor, the Deputy Governor and the sixteen other members of the Court of Directors are appointed by the Crown. Up to four Directors may serve as Executive Directors.

The names of the members of Court are given on page 3, together with the dates of their first appointment and expiry of their current terms. The principal outside appointment of each Non-Executive Director is also given. The areas of responsibility of the Executive and Associate Directors at 1 March 1994 are set out on page 4.

The day-to-day management of the Bank is the responsibility of the Executive members of Court. Their main forum for discussion and decision-making is the Executive Committee, comprising the Executive and Associate Directors under the Chairmanship of the Governor or Deputy Governor.

The Court of Directors meets weekly to review and examine major issues of policy and strategy proposed by the Executive members of Court. Meetings vary in length, with one monthly meeting set aside for substantive discussion on policy and strategic issues relating to one of the Bank's core functions. In future, more emphasis will be put on these longer meetings.

During the past year there has been a re-examination of the role of the Court committees, with the result that the Debden Committee, which was responsible for advising management at the Printing Works, and the Committee to consider the Securities of Certain Funds, have been stood down: in future, the General Manager of the Printing Works will report to Court through an Executive Director. The role of the Securities Committee will in future be assumed by the Trustees of the Staff Pension Fund, who will report directly to Court. The role of the Charitable Appeals Committee has been combined with that of the Community Affairs Unit under the administration of the Director responsible for Corporate Services.

The continuing committees are the Remuneration Committee, which makes recommendations to Court on the salaries of the Governors and the Executive members of Court, and the Audit Committee. The current members of the Remuneration Committee are Sir David Scholey (Chairman), Sir Martin Jacomb, Sir Colin Corness, Sir David Lees and Professor Sir Roland Smith. The current members of the Audit Committee are Sir David Lees (Chairman), Sir Colin Southgate, Sir Jeremy Morse, Sir David Cooksey and Ms Sheila Masters.

Statement of Directors' responsibilities

The Bank of England is not formally governed by the Companies Act 1985 but has chosen, for the accounts of the Banking Department, to comply with the accounting provisions of the Act, as applicable to banks, modified as set out in Note 1 of the accounts. The Court of Directors is responsible for ensuring that these accounts, on the basis set out in the accounts, present fairly the state of affairs of the Banking Department as at 28 February 1994 and of the profit for the year to that date. The accounts of the Issue Department are drawn up in accordance with provisions agreed between the Bank and HM Treasury to implement the requirements of the Currency and Bank Notes Act 1928 and the National Loans Act 1968. The Court of Directors is responsible for ensuring that the accounts are drawn up in accordance with these requirements.

The Court of Directors is responsible for keeping proper accounting records, which disclose at any time the financial position of the Bank and enable the Court to ensure that the accounts comply with the requirements set out in Note 1 thereto. The Court of Directors is also responsible for safeguarding the assets of the Bank and its subsidiaries, and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Court of Directors confirms that suitable accounting policies, consistently applied and supported by reasonable and prudent judgement and estimates, have been used in the preparation of the accounts of the Banking Department. Accounting standards applicable in the United Kingdom have been followed in preparing the accounts of the Banking Department in so far as they are appropriate to the basis of accounting set out in the notes to the accounts.

Auditors

Coopers & Lybrand will continue as auditors of the Bank.