

24 April 2013

The Rt Hon George Osborne
Chancellor of the Exchequer
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

Dear George,

The Funding for Lending Scheme (FLS), launched jointly by the Bank and HM Treasury, has contributed to a sharp reduction in funding costs for UK banks and building societies since the middle of last year. The Scheme has given banks confidence that they will be able to access funding on reasonable terms throughout 2013. That in turn has led to a reduction in borrowing costs and an increase in credit availability, especially for households and large companies.

We have recently discussed ways in which we can build on the success of the existing Scheme. Working together, Bank and Treasury officials have now finalised plans to extend the Scheme for one year, so that drawings can be made until January 2015. I believe such an extension is valuable as it gives banks continued assurance against the risk that market funding rates increase, especially in the light of continued uncertainty in the euro area.

The extended Scheme will differ from the original in two ways. First, in determining the amount that participants can borrow in the extended Scheme, more weight will be put on banks' lending to small and medium sized enterprises (SMEs) than on lending to large businesses and households. The aim is to increase the incentives for banks to lend to SMEs, as they have experienced a less marked easing in credit conditions since the original Scheme was launched. Second, banks' lending to certain categories of financial companies, which in turn lend to the real economy, will be included as part of the extended Scheme. That will help to support the supply of credit from these 'non-bank credit providers' to the real economy. The extended Scheme is described in more detail in the attached note.

As the FLS is designed to affect credit conditions and hence aggregate demand, these plans have been discussed with the Monetary Policy Committee, who support the extension of the Scheme. Financial Policy Committee members have also been briefed ahead of today's announcement. I would be grateful if you would confirm that you approve the extension to the FLS, and agree that it lies within the remit of the Bank. So that you can remain satisfied that the extended Scheme is within the remit of the Bank and that it is meeting its objectives, the FLS will continue to be overseen by a joint Bank / HM Treasury Oversight Board.

The extension of the FLS will help to maintain easier funding conditions for banks into 2015, and thereby help to support credit conditions and the recovery in our economy. Today's announcement is, however, a complement to, not a substitute for, ensuring that our banks are adequately capitalised. Banks that are short of capital cannot increase lending. That is why in March the Financial Policy Committee made a series of recommendations to the Prudential Regulation Authority (PRA) designed to ensure that UK banks are well capitalised, and that banks meet that requirement in a way that does not hinder lending to the economy. You may be assured that we are determined that the newly-formed PRA follows through on those recommendations.

With all best wishes.

The image shows a handwritten signature and several scribbles. The signature is written in black ink and appears to be 'M. C. B.' or similar, with a large, sweeping flourish underneath. There are also some smaller, less distinct scribbles above and to the right of the main signature.