

The Rt Hon Kwasi Kwarteng
Chancellor of the Exchequer
HM Treasury
1 Horse Guards Road
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SW1A 2HQ

22 September 2022

Dear Kwasi

At its meeting ending on 21 September 2022, the Monetary Policy Committee (MPC) voted to reduce the stock of purchased UK government bonds (gilts) held in the Asset Purchase Facility (APF) by £80 billion over the next twelve months. Details of this decision and the approach to reducing the stock of gilts, including liaison with the UK Debt Management Office, are set out below.

The use of the APF for monetary policy

Consistent with its guidance set out in the August 2021 Monetary Policy Report, in February 2022 the MPC voted to begin to reduce the stocks of gilts and sterling non-financial investment-grade corporate bonds held in the APF, by ceasing to reinvest any future maturities falling due and initiating a programme of corporate bond sales to be completed no earlier than towards the end of 2023. Since February, a total of £37.1bn of gilts has matured, reducing the outstanding gilt stock from £875.0bn at the end of 2021 to £837.9bn. In addition, a total of £1.1bn of corporate bonds has matured, reducing the stock from £20.0bn to £18.9bn; sales of the remaining stock will begin on 27 September. That leaves the total size of the APF at £856.8bn, as of 21 September 2022.

At this week's September meeting, the MPC voted to reduce the stock of purchased UK government bonds, financed by the issuance of central bank reserves, by £80 billion over the next twelve months, to a total of £758bn, in line with the strategy set out in the minutes of the August MPC meeting. At its August meeting, the MPC had communicated that it was provisionally minded to commence gilt sales shortly after its September meeting, subject to economic and market conditions being appropriate. At the September meeting, the Committee agreed that the conditions were appropriate and voted to begin the sale of UK government bonds held in the Asset Purchase Facility shortly after this policy meeting.

The Committee has also reaffirmed its preference in most circumstances to use Bank Rate as its active policy tool when adjusting the stance of monetary policy. If potential movements in Bank Rate are judged insufficient to achieve the inflation target, or if prevailing conditions are ones in which asset purchases might be particularly effective, the reductions in the stock of purchased assets could be amended or reversed. Looking ahead, the overall stance of monetary policy will, as required by the Committee's remit, continue to be set to meet the 2% inflation target, and in a way that helps to support the government's economic policy objective of strong, sustainable and balanced growth.

Approach to gilt sales

The Bank will deliver the reduction in the stock of APF gilts set by the MPC via gilt maturities over the twelve-month period, and a programme of gilt sales over the same period. As set out in the Market Notice published by the Bank on 1 September 2022, the Bank will set its gilt sale auction schedule on a quarterly basis. Accordingly, we have today set out the details and schedule for the Bank's planned gilt sale operations in Q4 2022, starting from the week commencing 3 October 2022.

As set out in my letter dated 3 February 2022, and explained further in the Bank's Market Notice published on 4 August 2022, in designing a strategy for gilt sales the Bank has liaised with the UK Debt Management Office (DMO) in order to minimise interference with the DMO's own issuance programme and considered the views of market participants as to how best to minimise disruption in private asset markets.

The Committee reaffirmed that, as a matter of course, it would not continue to vote at each meeting on propositions regarding the stock of purchased assets outside a scheduled annual review. The Committee also reaffirmed that, as set out in the minutes of its August meeting, there would be a high bar for amending the planned reduction in the stock of purchased gilts outside such a review. In judging whether that bar was met, the Financial Policy Committee would also have a role through its assessment of financial stability.

Additional operational arrangements

As you are aware, the Bank and HMT agreed in 2012 to transfer gilt coupon payments received by the APF, net of interest costs and other expenses, to the Exchequer in order to facilitate more efficient cash management across the public sector as a whole. It was recognised that this arrangement would result initially in payments from the APF to the Government, and indeed to date a cumulative total of over £120bn of cash transfers have been made from the APF to HMT. It was also agreed that reverse payments from the Government to the APF were likely to be needed in the future as Bank Rate increases and as the APF's gilt holdings are unwound by the MPC, and that these reverse payments would be met by the Government on a timely basis. Our officials will continue to discuss the size and direction of future cashflows regularly as the portfolio begins to shrink.

In order to streamline its operational processes in the context of asset sales, repayments from the APF to the Bank on the loan used to fund its asset purchases will now move to a quarterly basis, aligned with the timing of the relevant cashflows.

As the size of APF holdings reduces, we have also agreed that authorised maximum size of the APF should be adjusted to reflect the size of portfolio every six months, confirmed through an exchange of letters between us. I will therefore write to you again during Q4, alongside the next APF Quarterly Report and every second report thereafter. As announced by the Bank in May, the APF Quarterly Reports will also include updated projections of the expected cashflow profile to support transparency.

Should the MPC deem it necessary to recommence asset purchases in the future, I would expect to notify you and – if necessary – to request a corresponding increase to the maximum size of the APF via a public exchange of letters between ourselves, as was the case in November 2020.

Yours sincerely,

A handwritten signature in black ink that reads "Andrew Bailey". The signature is written in a cursive style with a small dot above the 'i' in Bailey.

cc: The Rt Hon Mel Stride MP, Chair of the Treasury Committee
