MEETING OF THE COURT OF DIRECTORS

Friday, 4 November 2016

Present:
Anthony Habgood, Chairman
The Governor
Mr Broadbent, Deputy Governor – Monetary Policy
Sir Jon Cunliffe, Deputy Governor – Financial Stability
Dame Minouche Shafik, Deputy Governor – Markets & Banking
Mr Woods, Deputy Governor – Prudential Regulation
Mr Fried
Mr Frost
Baroness Harding
Mr Prentis
Mr Robert
Ms Thompson

Ms Hogg, Chief Operating Officer

Secretary:
Mr Footman

Court joined Mr Habgood in welcoming the Governor's decision, announced earlier in the week, to continue in office until the end of June 2019, so as to provide continuity over the period of the Brexit negotiations. Mr Habgood added that this would be a difficult period, requiring clear heads and objectivity but also experience and context. On behalf of the Bank he thanked the Governor for making that decision despite some personal inconvenience.

1. **Minutes**

The minutes of the meeting held on 21 September 2016 were approved.

2. **Report from ARCO**

Mr Fried reported on the ARCO meeting on the 6th October. The meeting was now run with two separate agendas, for Risk and Audit respectively.

On the Risk side, clearly a significant amount of thinking and work had gone into the development of the Risk Reports, which had been transformed, enabling robust discussion of risk levels, exceptions and outliers. The Committee had reviewed the management environment for the new Term Funding and Corporate Bond Purchase schemes, systems and processes having had to be developed from scratch. Although subject to Treasury indemnity, risks were reviewed no differently than if they were directly on the Bank's own balance sheet.

3. **Report from Remco**

Baroness Harding said that Remco had reviewed the flexible pension contribution rates for the following year. It was clear that the reforms agreed in 2015 were working as intended, and with the lower basic accrual rate for new joiners the overall cost of the pension scheme was coming down. In the short term these gains had been obscured by the sharp fall in discount rates, which were reflected in the funding contribution, and also in the flex rates, which allowed staff to choose more or less pension accrual at actuarially fair prices. To ensure fairness to the Bank as well as employees the Committee had decided make an allowance in the rates for changes in Employers' NI; and it had also capped the compensation for those who opted out of pension accrual altogether. The scheme was due for review in 2018 and Remco had agreed that preliminary work should start in 2017.

The Committee had also reviewed the "Employment Deal" concept that was being developed in the context of the new Strategic Plan. This stressed the Bank's commitment to development, training (including the new Central Banking Qualification), corporate social responsibility, diversity and wellbeing – as well as the reward strategy. It would be tested against elements of the strategic plan and would provide the context for the review of the remuneration framework. Members had particularly welcomed the commitment to diversity, which went beyond the normal "protected characteristics" and would continue to be set out in detail in the Annual Report.

Court members noted that although the pension scheme was fully funded with assets that matched the Fund's liabilities, contribution rates would be affected in the accounting valuation by the decline in credit spreads. Ms Hogg noted that this would be the case whatever the investment strategy of the Fund itself. The Bank had moved to a low basic accrual rate and charged actuarially fair contribution rates to those who wanted more. In this it differed to other public sector schemes, which were often unfunded and not valued on a market-consistent basis.

4. Future Forum

The Governor summarised the outcome of the Future Forum which had been held, drawing on the Agency network, at a number of centres in the East and West Midlands and had involved all of the Bank Governors. It culminated in a plenary session in Birmingham Town Hall, where Governors discussed what they had heard and considered actions for the Bank to take forward. The aim had been to hear from a wide range of stakeholders – large corporates, SMEs, Fintech and IT, Education, Charity and the Third Sector as well as the general public – and to encourage a continuing dialogue between the Bank and the general public. Discussion ranged across the full range of the Bank's objectives and the quality was generally very high. Among the conclusions drawn by the Bank team were that the Bank could play more of a role in basic economic and financial education – which would involve an overhaul of its communications approach, explaining ourselves in terms people can understand, through a wide range of channels, and visually wherever possible – covering such areas as the growth/inflation trade-off, access to finance, the risks and the opportunities of Brexit, and the impact of monetary policy on saving and pensions.

5. Investigations

Ms Hogg updated Court on current Investigations.

6. IEO Report on FMI Supervision: Discussion

(Lea Paterson, David Bailey, Anne Wetherilt and Alexander Justham)

Ms Paterson said that the IEO was finishing their evaluation of the Bank's FMI supervision, and was preparing a full report. There was no doubt that the FMI team's supervisory outputs were seen as high quality by stakeholders internally and externally, and held in high regard internationally, as evidenced for example by the IMF FSAP report. The investments made in FMI supervision by the Bank at time of the Strategic Plan were having a positive effect. However the FMI sector was growing in scale and complexity and demands on FM Supervision were likely to increase. Opportunities should be taken to leverage and share expertise with other parts of the Bank, particularly in areas of operational risk. It was also worth considering introducing some external specialist expertise into the governance process.

Court agreed to hold a further discussion in February against the background of the full Report.

7. **IEO forward planner**

(Lea Paterson and Kate Stratford)

Ms Paterson said that the current expectation remained that the IEO would undertake two reviews each year, using a mix of permanent staff, staff seconded from other parts of the Bank for specific reviews, and external expertise. That model had worked for the review of forecasting performance, the review of the PRA's Competition Objective, and the two current reviews of FMI supervision and Insurance Supervision. The fully-loaded cost of each review was in the region of £250,000.

Court agreed, in principle, that the 2017 Reviews should cover the Resolution Directorate's work and the Sterling Market Framework (SMF). It was important that the scope of an SMF evaluation was broad enough to cover liquidity provision and governance: this could be discussed at the next Court meeting. For future years, possible topics were: the stress testing framework; the impact of the FLS; operational resilience and possibly other aspects of the Brexit process.

8. **MPC Report**

Mr Haldane noted that sterling had depreciated by a further 6½% since the August Inflation Report. Since early October, some UK asset prices had underperformed international equivalents and some borrowing costs had risen. Output growth in Q3 had slowed much less markedly than expected at the time of the August Report and the near term outlook was also stronger. Consumer spending had remained strong and housing market conditions remained resilient. Largely as a result of the impact of exchange rate movement, the MPC expected inflation to rise to 2¾% in 2018 before falling back towards the target. The MPC's remit required it to balance the speed with which inflation is returned to target with support for growth. The MPC had kept policy unchanged in November despite a more adverse trade-off. Attempting to offset the exchange rate change with higher rates would be costly to output and employment; but the MPC had made it clear that the "there are limits to the extent to which above-target inflation can be tolerated".

9. **Report from the PRA**

Mr Woods briefed Court on recent issues relating to individual banks.

10. **Quarterly Financials**

(Rommel Pereira)

Mr Pereira presented the results from the first half of the financial year, to August 2016. Income was above budget and costs below; and for the full year to February, costs were expected to remain slightly below budget, due mainly to recruiting delays and rephasing of investment projects.

11. **Risk Report**

(Andrew Hauser, Julia Rangasamy and Nat Benjamin)

Court reviewed the six-monthly risk update. This suggested that the Bank's overall risk profile had heightened in the wake of the Referendum result; operational risk because of the expansion of the Asset Purchase Facility; and reputational risk as reflected in the volume of unfavourable media coverage. However polling across key metrics continued to indicate a high level of public trust in the Bank. Other issues included people risk and the continuing close attention being paid to information security risk.

12. **Viewpoint Survey 2016 Bank-wide Actions**

(Jo Place, David Bailey, Victoria Cleland and Gareth Ramsay)

The Viewpoint steering group summarised the steps taken in response to the latest (largely favourable) staff survey, in particular in relation to the office environment, performance management, career development and work/life balance issues, and noted particularly the timeline of deliverables. Deputy Governors had agreed new delegation frameworks that would pass decision-taking and responsibility in their areas down the management chain. Court welcomed these initiatives.

13. **Banknote Transformation Programme**

(Victoria Cleland, Andrew Baker)

Ms Cleland outlined progress of two separate tenders under EU procurement regulations for the polymer and security feature components for the next “G” series £20 banknote.

14. **Matters Reserved to Court**

Court reviewed “Matters Reserved for Court”, setting out its delegations to the Executive and the matters reserved for Court decision. The document had been updated to reflect the provisions of the Bank of England and Financial Services Act 2016 including the provisions relating to the PRC, even though these would not come into force before early 2017. Several amendments were suggested and the final document, including terms of reference of the Court Committees, would be presented for approval in December.

15. **FPC Report**

(Alex Brazier)

Mr Brazier summarised the FPC discussion on the Q3 round. The FPC’s assessment was that the current outlook for UK financial stability remained challenging, driven by uncertainty about the near-term macroeconomic outlook and the United Kingdom’s future relationship with the EU. The FPC had reviewed each of the channels of risk it had outlined in the July 2016 *Financial Stability Report*. The FPC judged that the risks of a sharp adjustment in the commercial real estate market were crystallising. The risk remained of a fall in overseas investors’ appetite to invest in the United Kingdom. The FPC had discussed its approach to meeting its statutory responsibility following the referendum. It would remain committed to a level of resilience that is at least as great as that currently planned, which itself exceeds that required by international baseline standards. It had also noted the importance of macroprudential flexibility to align the resilience of the financial system to the risks that the system faced.

The meeting of Court was closed.