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News release

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The Framework for the Bank of England's Operations in the Sterling Money Markets (the 'Red Book')

The Bank is today publishing an updated version of its 'Red Book', which sets out the framework for the Bank's operations in the sterling money markets. This update builds on the framework first introduced in May 2006. The last update was in January 2008.

The Bank's operations in the sterling money markets are designed to:

- **Implement the Monetary Policy Committee's decisions in order to meet the inflation target**. The Bank usually does this by paying interest at Bank Rate on the reserves balances held by commercial banks and building societies. In exceptional circumstances, the Bank may choose to vary the structure of its remuneration on reserves and to supply whatever reserves it deems necessary to meet its monetary policy objectives, by changing the size or composition of its balance sheet.
- **Reduce the cost of disruption to the liquidity and payment services supplied by banks to the UK economy**. The Bank does this by balancing the provision of liquidity insurance against the costs of creating incentives for commercial banks and building societies to take greater risks and subject to the need to avoid taking risks onto its own balance sheet.

The Bank is able to undertake these tasks because it is the sole supplier of 'central bank money' in the United Kingdom - the banknotes used in everyday transactions and the balances ('reserves') that are held by commercial banks and building societies at the Bank.

This update divides the 'Red Book' into two parts. Part 1 describes how the framework supports the Bank's core purposes of monetary and financial stability. Part 2 describes the facilities in operation at each point in time as part of that framework. Part 2 will therefore be subject to future updates as the facilities are adjusted. This update reflects a number of changes to the Bank's framework since early 2008, including:

- the suspension of reserves averaging in March 2009, when the Bank began undertaking asset purchases financed by the creation of central bank reserves (so called 'Quantitative Easing') in line with MPC decisions. The Bank currently operates a 'floor system' whereby all reserves balances are remunerated at Bank Rate.
- the provision of Operational Standing Facilities that help keep money market rates close to Bank Rate, and provide a means for participating banks to manage unexpected payment shocks which may arise due to technical problems.
- the introduction and use of indexed long-term repos to provide liquidity insurance to the banking system. The facility has been designed to avoid distorting banks' incentives for prudent liquidity management, while minimising the risk being taken onto the Bank's own balance sheet.
- the introduction of the Discount Window Facility ('DWF'), which offers liquidity insurance for firm specific as well as system-wide shocks. It is a bilateral facility designed to be able to address short-term liquidity shocks without distorting banks' incentives for prudent liquidity management, and whilst minimising the risk being taken onto the Bank's balance sheet.

The changes to the Bank's operations have all been previously announced.

Notes to Editors

1. The 'Red Book' is available at:
http://www.bankofengland.co.uk/markets/sterlingoperations/redbook.htm

The legal terms and conditions and operating procedures for the framework are contained in the Bank's Documentation, which is available at:
http://www.bankofengland.co.uk/markets/money/documentation.htm