



BANK OF ENGLAND

The state of the markets

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Delivered at the Institutional Investor Institute

29 June 2011

BoE Core Purposes

- CP1: Maintaining monetary stability
 - achieving stable prices as defined by the Government and ensuring confidence in the currency
- CP2: Maintaining financial stability
 - identifying, monitoring, and taking action to remove or reduce systemic risks with a view to enhancing the resilience of the UK financial system

The contribution of Market Intelligence (MI)

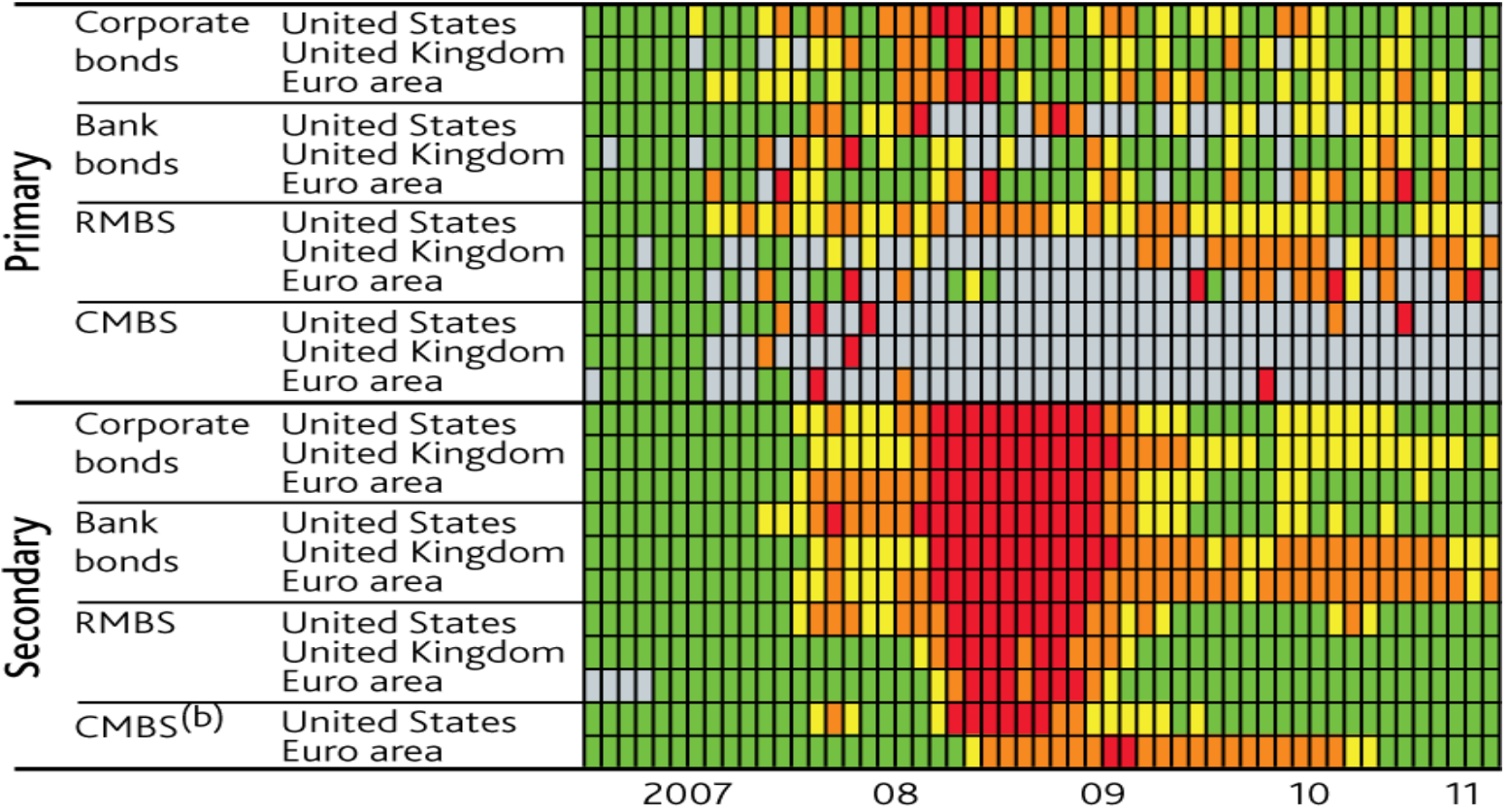
- BoE uniquely positioned to collect MI, given its public policy objectives, its location and its own operations.
- Helps make up for missing data.
- Crucially it helps us to understand better the behavioural patterns that underlie movements in financial variables.
- Helps us spot stress and new developments/risks that might introduce potential vulnerabilities into parts of the system.

Market Intelligence (MI) at the Bank of England

- Frequent meetings and conversations with a wide range of external market contacts
- Up to 70 staff involved in collecting MI as part of their day-to-day responsibilities.
- Extensive and (internationally) diverse contact base, including banks, dealers, brokers, asset managers, pension funds, insurance companies, hedge funds, private equity funds.
- Cover a wide range of markets, from vanilla instruments such as gilts and equities through to all manner of derivatives

The path of financial markets during the crisis

Chart 1 - Market functioning 'heat map' based on issuance and spreads data

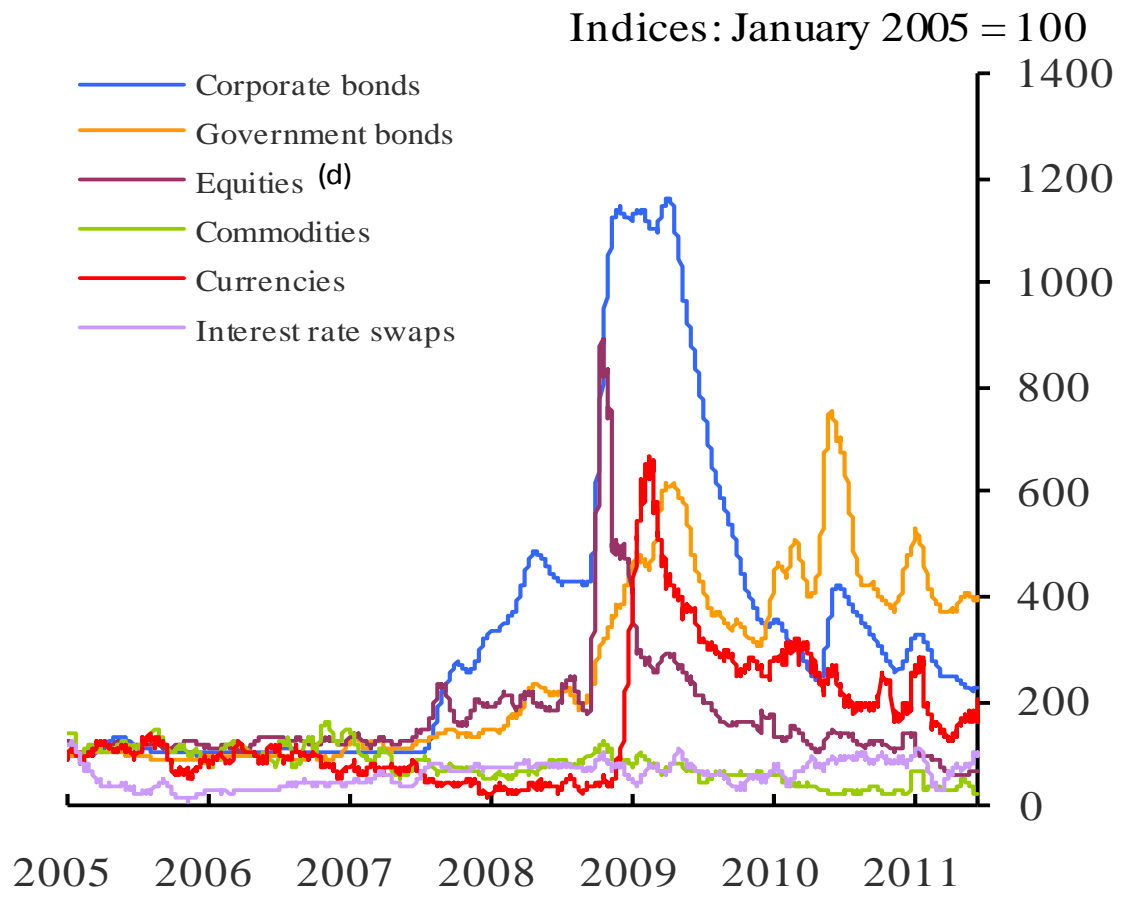


Sources: Bank of America Merrill Lynch Global Research, Bloomberg, Dealogic, JPMorgan Chase & Co. and Bank calculations.

(a) Shading is based on a score that reflects, for unguaranteed debt, both issuance (relative to GDP) and spreads in primary markets and secondary markets, expressed as a number of standard deviations from average, using as much data as was available from January 1998. Updated to end-May 2011; recent months use 2011 Q1 GDP.

(b) Insufficient data for UK CMBS secondary markets.

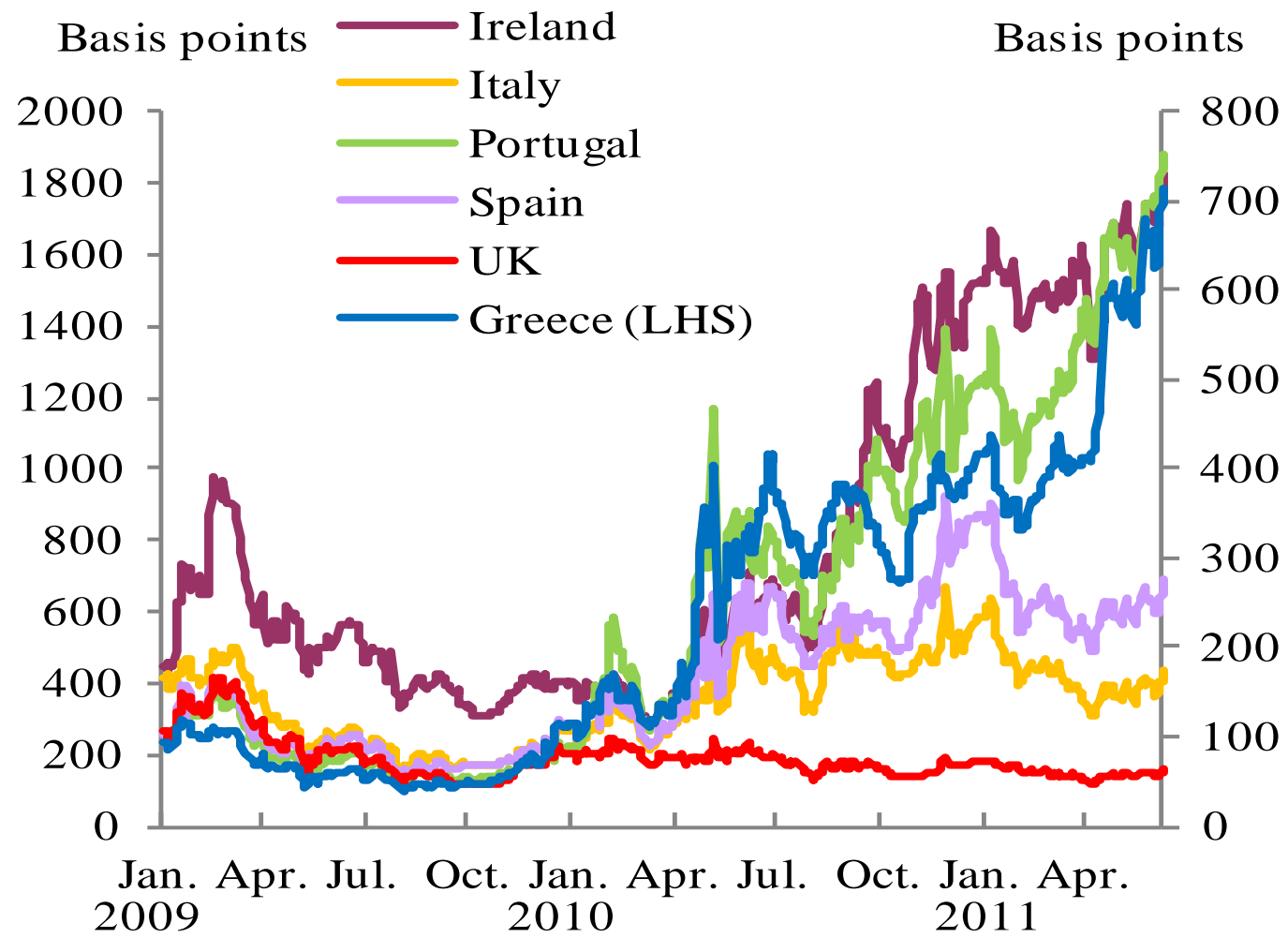
Chart 4 Bid-ask spreads on selected assets^{(a)(b)(c)}



Sources: Bloomberg, UBS Delta and Bank calculations.

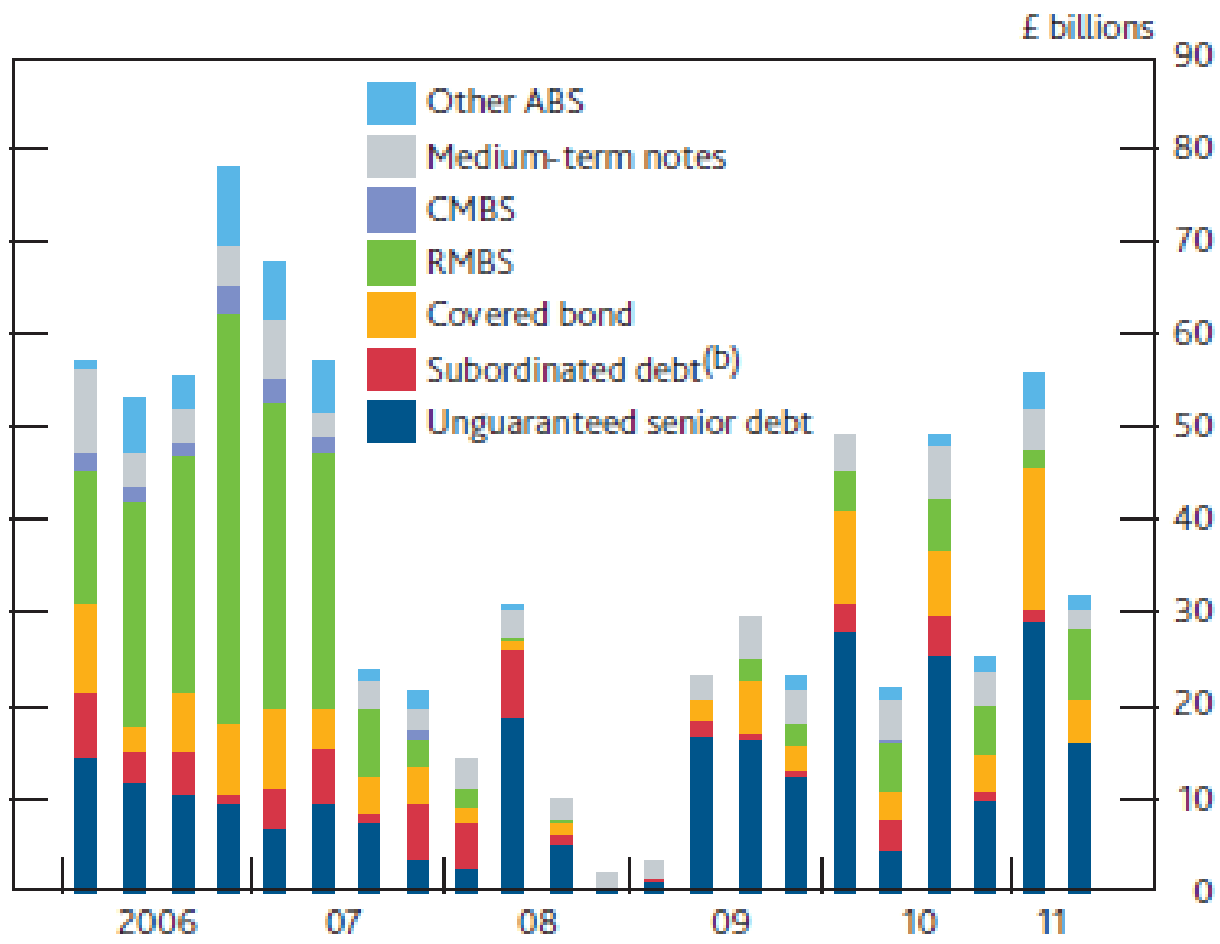
- (a) Monthly moving averages of daily bid-ask spreads.
- (b) iBoxx €Corporates for corporate bonds; S&P 500 for equities; iBoxx €Sovereigns for government bonds; sterling/dollar exchange rate for currencies; gold price for commodities; and euro five-year swaps for interest rate swaps.
- (c) Data to close of business on 10 June 2011.
- (d) End of day bid-ask spread until 1 May 2011, average intra-day bid-ask spread thereafter.

Chart 7 - Selected European sovereign CDS premia



Sources: Thomson Reuters DataStream.

Chart 8 - Major UK banks' unguaranteed term issuance in public markets^(a)



Sources: Bank of England, Dealogic and Bank calculations.

(a) 2011 Q2 is up to and including 15 June 2011. Term issuance refers here to securities with original contractual maturity or earliest call date of at least 18 months. This excludes debt issued under HM Treasury's Credit Guarantee Scheme.

(b) It includes subordinated lower Tier 2 and Tier 3 capital instruments with debt features.

Chart 9 - Aggregate SLS repayment profiles

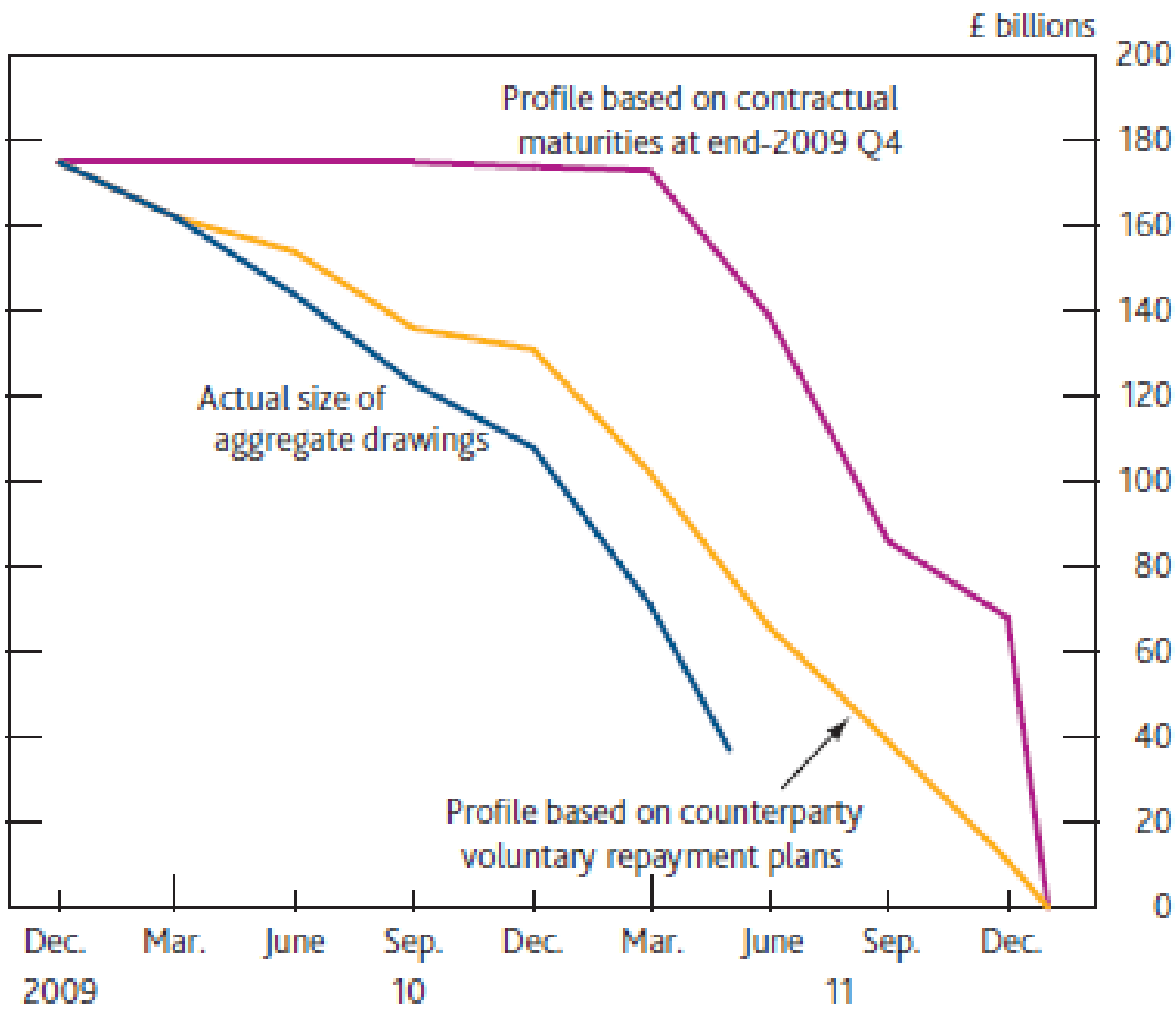
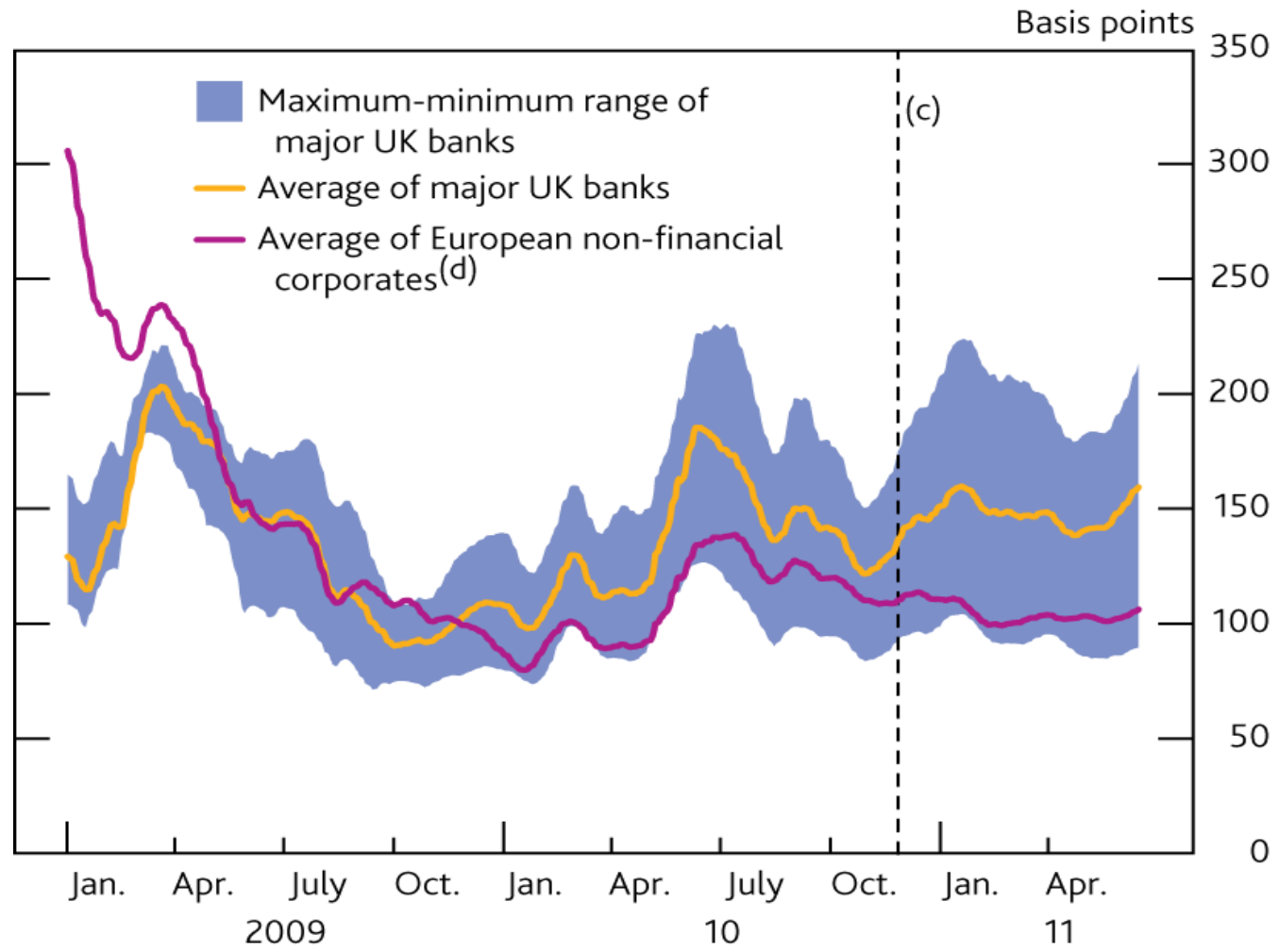


Chart 10 – Credit Default Swap premia^{(a)(b)}

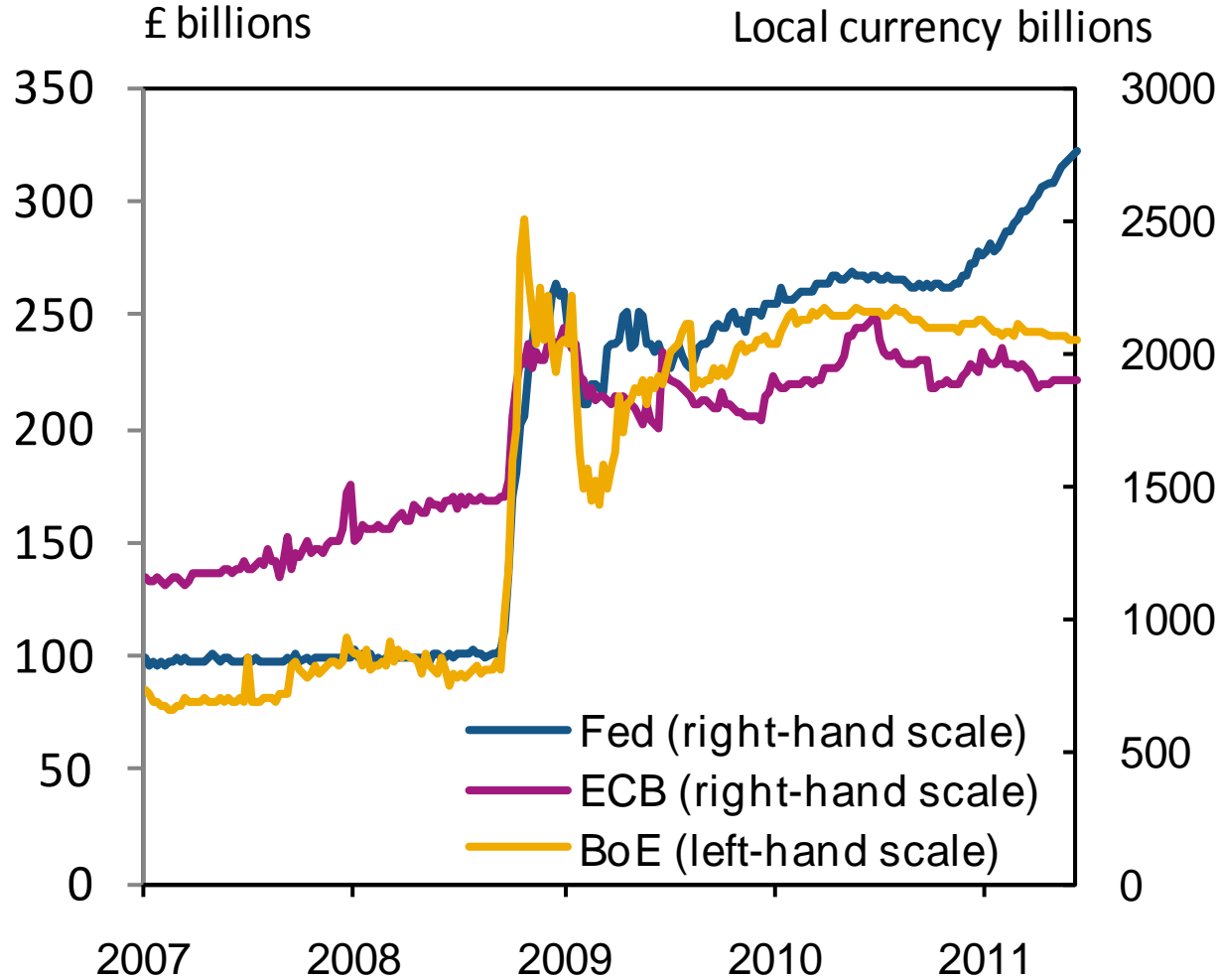


Sources: Bloomberg, Markit Group Limited and Bank calculations.

- (a) Five-year senior CDS premia. Data are presented as fifteen-day end-period moving averages.
- (b) Chart shows data for a subset of the major UK banks peer group — Barclays, HSBC, LBG and RBS.
- (c) December 2010 *Financial Stability Report*.
- (d) Average of the CDS premia of companies that were part of the iTraxx European non-financial corporates index (series 10) at the beginning of the time series in this chart.

The search for yield/assets

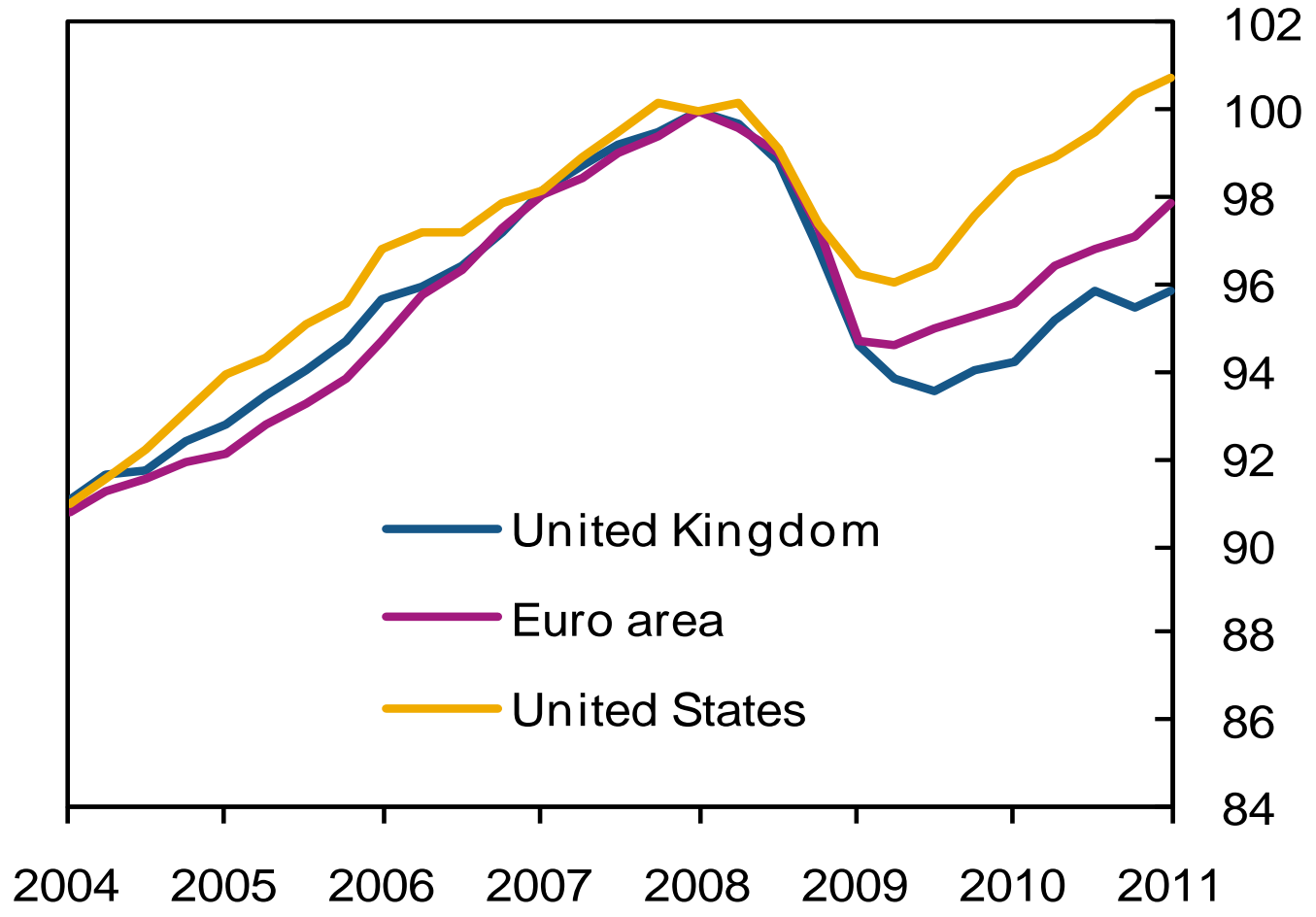
Chart 11: Central bank balance sheets



Sources: Bloomberg and Bank of England.

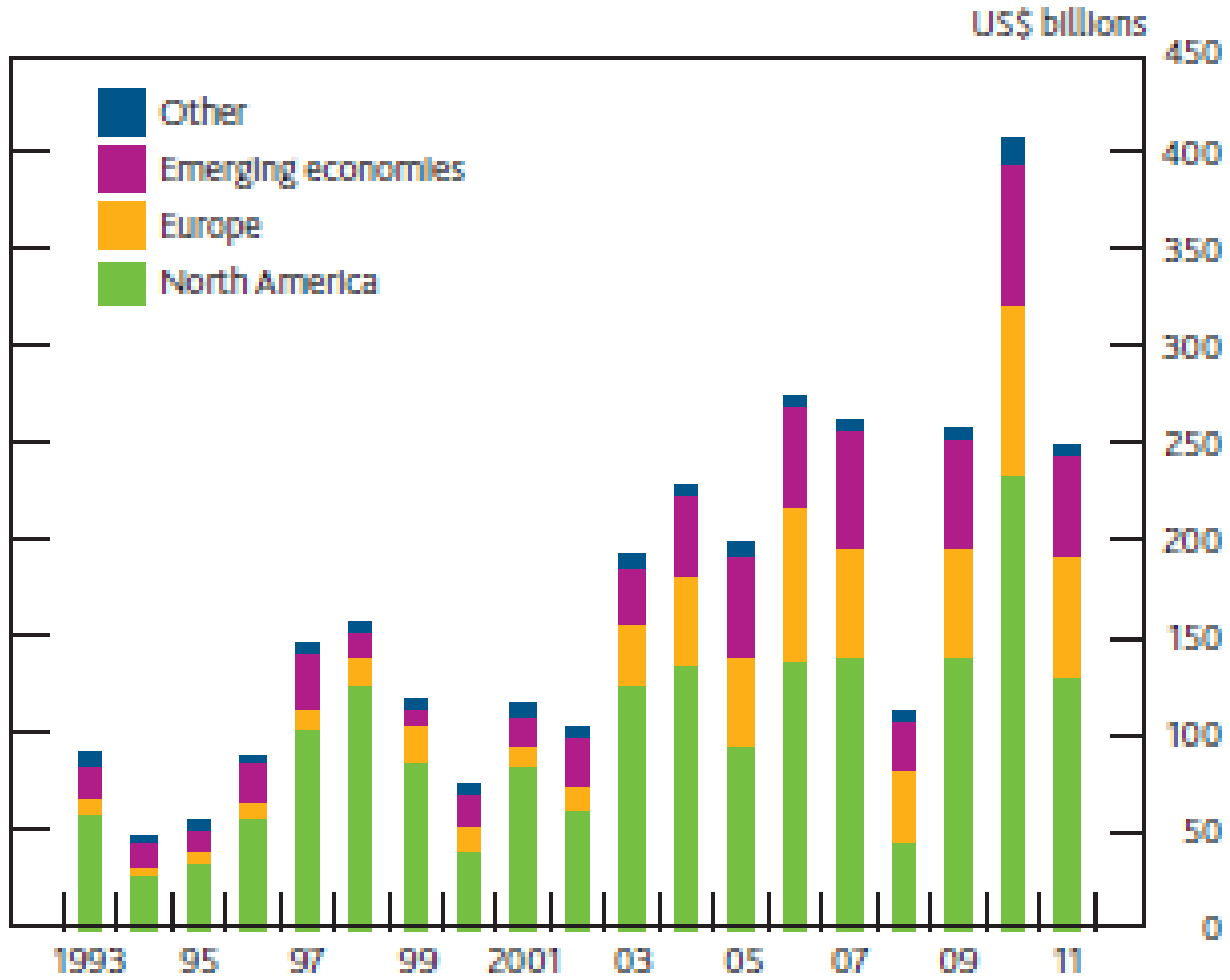
Chart 12: US, UK and Euro area GDP

Indices: 2008 Q1 = 100



Sources: ONS, Eurostat and Bureau of economic analysis.

Chart 13: Issuance of sub-investment grade corporate debt by region^{(a)(b)}



Sources: Dealogic and Bank calculations.

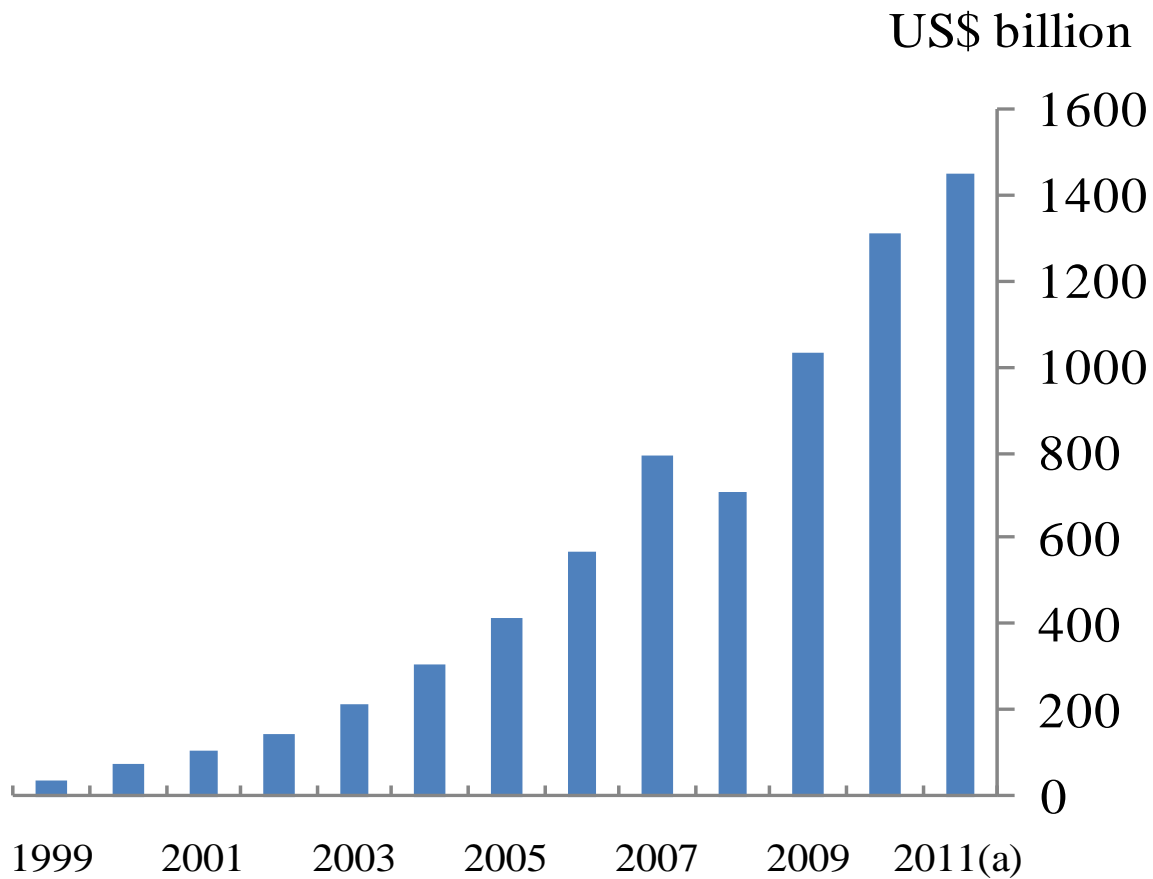
(a) Emerging economies includes Africa, Caribbean, Indian subcontinent, Latin America, Middle East, North Asia and South East Asia. 'Other' includes Australasia and Japan. Includes issuance in all currencies.

(b) 2011 data are to 3 June 2011.

Financial innovation

- Innovation is a fundamentally good thing – leads to a more efficient allocation of capital (helps sustain economic growth)
- A continuous and rapid process
- Recent innovations include:
 - putable CDs;
 - evergreen repos;
 - long-term collateral swaps;
 - Exchange Traded Funds (ETFs).

Chart 15 – Global ETF assets under management



Source: Blackrock Global ETF Research and Implementations Strategy Team.

(a) Data to end May 2011

Impact of the regulatory agenda

- Financial crisis exposed weaknesses in regulatory regimes, and triggered a wholesale overhaul.
- Cornerstone of that is to solve the “too big to fail” problem.
- Authorities, domestically and internationally, are still working on the design and precise calibration of these regulations.
- Getting those right will take time, but it is crucial. Meanwhile the uncertainty is impacting on market functioning.
- Once decided, there should be improvements arising from:
(a) more certainty, (b) a safer financial system.



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