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THE DEBT MANAGEMENT OFFICE'S FINANCING REMIT FOR 2006-07

Objectives

5.1 The UK Debt Management Office (DMO), an Executive Agency of HM Treasury, has been given the following objectives in respect of Government debt management:

- to meet the annual remit set by HM Treasury Ministers for the sale of gilts, with due regard to long-term cost minimisation taking account of risk;
- to advise Ministers on setting the remit to meet the Government's debt management objectives and to report to Ministers on the DMO's performance against its remit, objectives and targets;
- to develop policy on and promote advances in new instruments, issuance techniques and structural changes to the debt markets that will help to lower the cost of debt financing, liaising as appropriate with the Bank of England, Financial Services Authority, London Stock Exchange, and other bodies and to provide policy advice to HM Treasury Ministers and senior officials accordingly;
- to conduct its market operations, liaising as necessary with regulatory and other bodies, with a view to maintaining orderly and efficient markets and promoting a liquid market for gilts;
- to provide, including in liaison with Computershare Investor Services plc and CRESTCo, a high quality efficient service to investors in government debt, and to deal fairly and professionally with market participants in the gilt and money markets, consistent with achieving low cost issuance;
- to contribute to HM Treasury's work on the development of the medium-term strategy for the debt portfolio; and
- to make information publicly available on the debt markets and DMO policies where that contributes through openness and predictability to efficient markets and lower costs of debt issuance.

Quantity of gilt sales

5.2 The DMO, on behalf of the Government, will aim for gilt sales of £63.0 billion (cash)⁹ in 2006-07.

Pre-commitment to gilt issuance

5.3 Within the total of £63.0 billion a minimum gilt sales programme of £53.0 billion is pre-allocated from the start of the financial year between short (maturity of 1-7 years), medium (maturity of 7 to 15 years), and long (maturity of 15 years and over) conventional gilts, and regular auctions of index-linked gilts. This core issuance programme aims at ensuring regular issuance across the maturity spectrum throughout the year and at building up benchmarks at key maturities (e.g. 5-year and 10-year for conventional gilt issuance).

⁹ Figures in Chapter 5 are in cash terms unless otherwise stated.

5.4 The remaining unallocated amount of £10.0 billion will be allocated on a quarterly basis throughout the year in a broadly even-flow manner (i.e. approximately £2.5 billion will be allocated each quarter). This is intended to increase the ability of the Government to respond to substantial changes in market conditions and in the pattern of demand for gilts throughout the year. The allocation in the first quarter of the financial year is announced as part of the publication of the DMO's annual remit. From the second quarter of the financial year, decisions on the allocation of these supplementary amounts of issuance will be made following regular consultation meetings with Gilt-edged Market Makers (GEMMs) and representatives of investors (see paragraphs 5.5 and 5.6 below).

5.5 Supplementary issuance in any one quarter may be achieved by increasing the size of scheduled auctions and/or adding auctions. The dates of any additional auction(s) will be the subject of discussion at the regular quarterly consultation meetings of the DMO with gilt market participants and will be communicated in the quarterly issuance announcement.

5.6 The March consultation meetings to discuss the calendar for the first quarter of the financial year will continue to take place with the next meeting scheduled for Monday 27 March 2006. In order to improve further the degree of transparency and predictability in the delivery of the remit within the financial year, the quarterly consultation meetings for the remaining quarters of the year will take place in the penultimate month of each quarter and the issuance calendar for the following quarter will be announced at the end of that month. For example, the issuance calendar for July-September 2006 will be announced at 3.30pm on Wednesday 31 May 2006. This, and subsequent quarterly announcements, will also specify that part of the unallocated tranche to be allocated in the forthcoming quarter.

5.7 The allocation of the £2.5 billion supplementary issuance planned for the first quarter of 2006-07 is as follows:

- £2.5 billion (cash) in long conventional gilts.

This amount has been taken into account in the maturity mix of conventional gilt issuance provided below and in the auction calendar provided in Table 5.1.

Minimum amount and maturity mix of conventional gilt issuance

5.8 A minimum of 17 auctions of conventional gilts are planned in 2006-07:

- a minimum of 4 in the short (1-7 years) maturity area, aiming to raise at least £10.0 billion cash;
- a minimum of 4 in the medium (7-15 years) maturity area, aiming to raise at least £10.0 billion cash; and
- a minimum of 9 in the long (15 years and over) maturity area, aiming to raise at least £19.5 billion cash.

5.9 Both the planned total and maturity breakdown of planned conventional gilt issuance, and the number of auctions may be increased in-year as part of the allocation of the supplementary gilt issuance referred to in paragraph 5.4 above.

Minimum amount and maturity mix of index-linked gilt issuance

5.10 The Government has an ongoing commitment to the index-linked gilt market. In 2006-07, the DMO aims to sell a minimum of £16.0 billion (cash) in index-linked gilts.

5.11 A minimum of 16 auctions of index-linked gilts are planned in 2006-07 and it is intended that this will include at least monthly issuance at long maturities.

5.12 Both the planned total of index-linked gilt issuance and the number of auctions may be increased during the year as part of the allocation of the supplementary gilt issuance referred to in paragraph 5.4 above.

Sizing of gilt auctions

5.13 The gilt sales targets in paragraphs 5.2 to 5.10 above are specified in cash terms, but the gilt auctions are sized in nominal terms, typically in £0.25 billion increments for conventional gilts and £0.025 billion increments for index-linked gilts. Therefore all gilt sales targets are expressed in approximate terms.

Method of issuance of gilts

5.14 Auctions will constitute the primary means of issuance of all gilts (conventional and index-linked). All auctions will be single auctions held on the day indicated.

5.15 Each outright auction of conventional gilts is planned to be for between £1.5 billion and £4.0 billion (cash) on a competitive bid-price basis. Each outright auction of index-linked gilts will be for between £0.5 billion and £1.5 billion (cash) on a uniform price basis.

5.16 The expected timing of gilt sales comprising the £53.0 billion core programme and the £2.5 billion supplementary issuance for Q1 2006-07 is set out in the auction calendar in Table 5.1 below. These dates are subject to revision in the light of decisions by the Chancellor of the Exchequer on the Budgetary timetable and on new information about the publication date of key economic data, in particular RPI release dates.

5.17 A more detailed auction calendar for the first quarter of the financial year, including the gilts to be auctioned on each date, will be announced by the DMO at 3.30pm on Tuesday 28 March 2006. For the rest of 2006-07 the quarterly calendar announcements will be made at 3.30pm on 31 May, 31 August and 30 November – and these will include the dates of any auctions added as part of the supplementary sales programme. Full details of all auctions will normally be announced at 3.30pm on the Tuesday of the week preceding the auction.

Table 5.1: Gilt auction calendar 2006-07

Date	Type
2006	
4 April	Conventional
11 April	Index-linked
25 April	Index-linked
11 May	Conventional
23 May	Index-linked
25 May	Conventional
7 June	Conventional
22 June	Conventional
27 June	Index-linked
4 July	Conventional
11 July	Index-linked
25 July	Index-linked
1 August	Conventional
23 August	Index-linked
5 September	Conventional
21 September	Conventional
27 September	Index-linked
3 October	Conventional
12 October	Index-linked
24 October	Index-linked
23 November ¹	Conventional
28 November ¹	Index-linked
5 December ¹	Conventional
6 December ¹	Conventional
14 December ¹	Index-linked
2007	
9 January	Conventional
18 January	Index-linked
25 January	Index-linked
20 February ¹	Index-linked
22 February ¹	Conventional
6 March ¹	Conventional
15 March ¹	Conventional
27 March ¹	Index-linked

1. Subject to confirmation following the Chancellor's decisions on the Budgetary timetable.

5.18 The above programme of conventional and index-linked gilt auctions and any others that may be added in-year may be supplemented between auctions by official sales of gilts by the DMO "on tap". Taps of gilts will be used only as a market management instrument in conditions of temporary excess demand in a particular gilt or sector. The DMO would only contemplate taps in exceptional circumstances.

5.19 The DMO has no plans to issue gilts by syndicated offering in 2006-07.

5.20 After an auction, the DMO will generally refrain from issuing gilts of a similar type or maturity to the auctioned gilt for a reasonable period, unless already pre-announced, or if there is a clear market management case for doing so.

5.21 For the purposes of market management, the DMO may create and repo out gilts in accordance with the provisions of its Standing Repo Facility launched on 1 June 2000.

Reverse auctions

5.22 The DMO has no plans for a programme of reverse auctions in 2006-07.

Conversions and switch auctions

5.23 The DMO has no plans to conduct conversion offers or switch auctions in 2006-07.

Coupons

5.24 As far as possible, coupons on new issues will be set to price the gilt close to par at the time of issue.

Buy-ins of short maturity debt

5.25 The DMO will have responsibility for buying in gilts close to maturity to manage Exchequer cash flows.

Revisions to the remit

5.26 Any aspect of this remit may be revised during the year, in the light of exceptional circumstances and/or substantial changes in the following:

- the Government's forecast of the gilt sales requirement;
- the level and shape of the gilt yield curve;
- market expectations of future interest and inflation rates; and
- market volatility.

5.27 Any revisions to this remit will be announced.

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THE DEBT MANAGEMENT OFFICE'S EXCHEQUER CASH MANAGEMENT REMIT FOR 2006-07

6.1 The Government's cash management objective is to ensure that sufficient funds are always available to meet any net daily central government cash shortfall and, on any day when there is a net cash surplus, to ensure this is used to best advantage. HM Treasury and the DMO work together to achieve this.

6.2 HM Treasury's role in this regard is to make arrangements for a forecast of the daily net flows into or out of the National Loans Fund (NLF); and its objective in so doing is to provide the DMO with timely and accurate forecasts of the expected net cash position over time.

6.3 The DMO's role is to make arrangements for funding and for placing the net cash positions, primarily by carrying out market transactions in the light of the forecast; and its objective in so doing is to minimise the costs of cash management while operating within a risk appetite approved by Ministers.

6.4 The Government's preferences in relation to the different types of risk-taking inherent in cash management will be defined by a set of explicit limits covering four types of risk¹⁰, which taken together, represent the Government's overall risk appetite. The risk appetite therefore defines objectively the bounds of appropriate Government cash manager behaviour determined in accordance with the Government's ethos for cash management as a cost minimising rather than profit maximising activity and playing no role in the determination of interest rates. The DMO may not exceed this boundary but within it the DMO will have discretion to take the actions it judges will best achieve the cost minimisation goal.

Exchequer cash management objective

6.5 The DMO's cash management objective is to minimise the cost of offsetting the Government's net cash flows over time, while operating within a risk appetite approved by Ministers. In so doing, the DMO will seek to avoid actions or arrangements that would:

- undermine the efficient functioning of the Sterling money markets; or
- conflict with the operational requirements of the Bank of England for monetary policy implementation.

Instruments and operations used in Exchequer cash management

6.6 The range of instruments and operations that the DMO may use for cash management purposes is set out in its Operational Notice¹¹. The arrangements for the issuance of T-bills and the management of the T-bill stock in market hands will be set out in and operated according to the DMO's Operational Notice.

¹⁰ The four types of risk are: liquidity risk; interest rate risk; foreign exchange risk; and credit risk. An explanation of these risks and the Government's cash management operations more generally is set out in Chapter 4 of the Debt Management Office's Annual Review 2004-05, which is available on the DMO's website at: www.dmo.gov.uk/gilts/public/annual/gar0405.pdf.

¹¹ The current edition of *Exchequer Cash Management Operational Notice and Treasury Bill Information Memorandum* is available on the DMO's website at: www.dmo.gov.uk/cash/cashops/10903.pdf.

6.7 One component of the debt sales planned to meet the Government's annual financing requirement is the year-on-year change in the outstanding stock of T-bills (excluding bills issued solely for collateral purposes). This change is announced as part of the financing remit given by HM Treasury to the DMO (see Chapter 5 above).

6.8 During the financial year the DMO will manage the level of the T-bill stock and may increase or reduce the stock vis-a-vis the end year target level, in order to support the implementation of Government cash management.

6.9 As a contingency measure, the DMO may also issue T-bills to the market to assist the Bank of England's operations in the sterling money market for the purpose of implementing monetary policy while meeting the liquidity needs of the banking sector as a whole. In response to a request from the Bank, the DMO may add a specified amount to the size(s) of the next bill tender(s) and deposit the proceeds with the Bank, remunerated at the weighted average yield(s) of the respective tenders. The amount being offered to accommodate the Bank's request will be identified in the DMO's weekly Treasury bill tender announcement. T-bill issues made at the request of the Bank will be identical in all respects to T-bills issued in the normal course of DMO business.

DMO collateral pool

6.10 To assist the DMO in the efficient execution of its cash management operations a combination of T-bills and gilts, which shall be chosen to have a negligible effect on relevant indices, may be issued to the DMO on the third Wednesday of April, July and October 2006 and January 2007. Any such issues to the DMO will only be used as collateral in the DMO's cash management operations and will not be available for outright sale. The precise details of any such issues to the DMO will be announced in advance. If no issue is to take place in a particular quarter, DMO will announce that this is the case in advance.