

B) Exchequer cash management remit

Objective

1. The DMO's primary objective in carrying out its Exchequer cash management operations will be to offset, through its market operations, the expected cash flow into or out of the National Loans Funds on every business day; and to do so in a cost-effective manner. In doing so the DMO should:

- balance cost and risk in its choice of strategies; and
- manage cash flows without influencing the level of short-term interest rates.

2. The DMO should also take account of:

- the operational requirements for the Bank of England for implementation of its monetary policy objectives; and
- its impact on the efficiency of the sterling money market.

3. The DMO will carry out its objective primarily by a combination of:

- structured weekly Treasury bill tenders;
- bilateral market operations with DMO counterparties; and
- ad hoc tenders of Treasury bills (and repo or reverse repo transactions).

4. The DMO and the Bank of England will work together to avoid clashes in the delivery of their respective objectives in the money markets. The DMO will not take speculative positions on interest rate decisions by the Bank nor hold operations which by their nature or timing in the day could be perceived to clash with the Bank's open market operations.

D) Structured Treasury bill tenders

Timing and schedule of announcements

5. The DMO will hold structured Treasury bill tenders on the last business day of each week. When

announcing the results, the DMO will also announce the quantity and maturity of Treasury bills on offer in the structured tender in the following week and may give the maturity and indicative size of any ad hoc tenders in the following week.

6. Following the final structured tender at the end of each quarter, the DMO will issue a notice outlining the maturities of Treasury bills likely to be available via structured tenders over the following quarter.

Maturities

7. The DMO's structured Treasury bill tenders in 2001-02 may be of the following maturities:

- one month (approximately 28 days);
- three months (approximately 91 days);
- six months (approximately 182 days); and
- twelve months (approximately 364 days).

8. The DMO expects to give priority to establishing fully the shorter maturities before introducing the longer maturity instruments.

Level of stocks

9. The DMO will manage Treasury bill transactions with a view to running down the stock of bills in months of positive cash flows and increasing it in months of higher net expenditure. The DMO will aim to build up the stock of Treasury bills in market hands to £8.5 billion by the end of March 2002.

Interaction with Bank of England's money market operations

10. The DMO may also issue Treasury bills to the market to assist the Bank of England in its management of the sterling money markets. In response to a request from the Bank, the DMO will add a specified amount to the size(s) of the next structured 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 structured bill tender announcement. Treasury bill issues at the request of the Bank will be identical in most respects with the rest of the stock of Treasury bills outstanding.

Ad hoc tenders

11. The DMO may also issue short maturity Treasury bills (up to 28 days) at ad hoc tenders. The objective of such tenders will be to provide additional flexibility for the DMO in smoothing Exchequer cash flows. Treasury bills issued in ad hoc tenders will be identical in every respect with those issued by structural tenders.

12. In addition to issuing Treasury bills, the DMO may also execute repo or reverse repo transactions at ad hoc tenders. For such transactions, collateral used would either be gilts or Treasury bills.

13. The DMO may also hold ad hoc tenders for buying in gilts (or gilt strips) with a residual maturity of less than six months.

Timing of ad hoc tenders

14. The DMO will usually announce its intention to hold ad hoc tenders in the weekly announcement of the structured tender result. Such announcements will indicate the day(s) of the following week on which ad hoc tender(s) are expected to be held, together with a guide to the expected maturity and size.

15. The precise details of the maturity and nominal amount on offer will be announced at the opening of the offer on the morning of the tender (usually at either 8:30 a.m. or 10:00 a.m.).

II) Bilateral operations with the market

16. In pursuit of its cash management objectives, the DMO expects to continue to trade on a daily basis with its counterparties across a range of instruments.

17. The DMO's bilateral operations may comprise of:

- purchase from the market for future resale (reverse repo);
- sale to the market for future repurchase (repo);
- outright sale and purchase of gilts, Treasury bills and eligible bank bills, certificates of deposit, commercial paper, selected bank bills and other short-term debt issued by high quality issuers, including supnationals and foreign governments;
- unsecured cash borrowing and lending with its counterparties; and
- short-term foreign currency swaps, Forward Rate Agreements (FRAs) and interest rate futures may also be used to manage foreign currency and interest rate exposures. All foreign currency exposure will be hedged back into sterling.

18. The DMO would give prior notice to the market if it planned to introduce additional instruments for use in its bilateral operations.

19. Other than gilts and Treasury bills, collateral used in the repo and reverse repo transactions may include selected euro-denominated government securities, eligible bank bills, and supranational sterling and euro-denominated securities. In carrying out these transactions, the DMO may make use of those of its own holdings of marketable gilts, and of funds managed by the National Investment and Loans Office (NILO), for collateral purposes. If required, in exceptional circumstances, HM Treasury may issue gilts or Treasury bills, to the DMO for collateral purposes.