

Treasury Committee

Oral evidence: Autumn 2022 Fiscal Events, HC 740

Wednesday 26 October 2022

Ordered by the House of Commons to be published on 26 October 2022.

[Watch the meeting](#)

Members present: Dame Angela Eagle (Chair); Rushanara Ali; Harriett Baldwin; Anthony Browne; Emma Hardy; Kevin Hollinrake; Julie Marson; Alison Thewliss.

Questions 134 - 231

Witnesses

I: Sir Robert Stheeman, Chief Executive, Debt Management Office; Jim Juffs, Chief Operating Officer, Debt Management Office; Jessica Pulay, Co-Head of Policy and Markets, Debt Management Office.

Examination of witnesses

Witnesses: Sir Robert Stheeman, Jim Juffs and Jessica Pulay.

Q134 **Chair:** Thank you very much. It is a pleasure to welcome you all to this Treasury Committee hearing on the Debt Management Office. We are going to be discussing the autumn 2022 fiscal events, which we are all too familiar with. Sir Robert, I wonder if you would introduce yourself first and then let's introduce the rest of your team.

Sir Robert Stheeman: I am Robert Stheeman. I am the chief executive of the Debt Management Office.

Jessica Pulay: I am Jessica Pulay. I am co-head of policy and markets at the Debt Management Office.

Jim Juffs: I am Jim Juffs. I am the chief operating officer at the Debt Management Office.

Q135 **Chair:** Thank you very much for agreeing to come and give us evidence at quite a precipitous time for the DMO. A revision to your debt remit was issued on 23 September, after what I am going to call the mini-Budget; although it called itself the growth statement, everybody recognises it was actually a Budget. Alongside that, you had a revision to your debt remit. Was the process in the run-up to that revised remit similar to that for other fiscal events that have implications for the Debt Management Office?



HOUSE OF COMMONS

Sir Robert Stheeman: It was slightly different. It was the same in as much as the key aspect of any remit revision for us is the quantum of financing that the Treasury asks us to raise. In this case, we were given a very different quantum of finance for the rest of this financial year compared to what we had received back in March and then, when it was revised, in April.

The timetable was actually quite compressed. Normally, if these measures or these statements—we call them fiscal events—of whatever description occur, we have a little more warning. There are various iterations that occur between the Treasury and the OBR, in terms of working out exactly what the costings of any measures are. The number that we are given is derived from those discussions. In this case, we were given a specific number, but, as I recall, the entire timetable, in terms of our trying to design what was, in effect, a significantly different remit, was quite compressed.

Q136 **Chair:** Was it a few days?

Sir Robert Stheeman: It was a bit more than that. It often happens that the absolute final figure that is then published changes over a period of at least a few weeks, depending on how various measures are costed. I am trying to think when we first had a rough indication of the overall size. In this case, I would say the whole thing was compressed into approximately 10 days to a fortnight.

Q137 **Chair:** This was to have an increase in financing of £72.4 billion.

Sir Robert Stheeman: That is correct. That is the cash amount. For us in the DMO, the key issue is always the cash amount that we have to raise. That was the increase compared to the most recent revision, which occurred in April. Our overall financing requirement went up from just over £160 billion to £234 billion.

Q138 **Chair:** They are not insubstantial amounts, are they?

Sir Robert Stheeman: It is not an insubstantial amount, no. To give you a bit more colour, the decision was then taken, ultimately by Ministers, that that additional requirement should be met by approximately £62 billion more in gilt issuance between then and the end of the financial year and an additional £10 billion on to the overall level of the Treasury bill stock.

Q139 **Chair:** Do you get a chance in any of these discussions, normally less truncated than this one, to feed back your expertise and views on whether this is possible, or do you simply get given your remit and have to go off and try to fulfil it?

Sir Robert Stheeman: We get a chance. It is important to stress that. Also, we got a chance at the time. Ultimately, of course, it is the number that counts and we are tasked with delivering that overall requirement. To give a bit of context, we always, and we did at this time, provide



HOUSE OF COMMONS

advice on market conditions, in particular advice on why we found it necessary to change the overall shape of the remit. By that, I mean what we might be doing in particular maturities, the balance between short-dated issuance and long-dated issuance, or inflation-linked issuance as well. We had a chance to feed that in. We also made sure, as we are supposed to do, that we fed back as much colour, as we would describe it, about market conditions at the time, which were, inevitably, challenging.

Q140 Chair: Parts of the mini-Budget were being discussed publicly before the actual event and quite a lot of it, although not the grim detail, had been available if one was watching the leadership election going on over the summer. The market was watching the leadership election going on over the summer, so what commentary from the market were you getting on the general noise around what was going to be in the Budget?

Sir Robert Stheeman: The market is usually very good at both anticipating events, even before they have been formally announced, and, in particular, discounting the impact of those events in the actual pricing of what is going on. It is fair to say that there were expectations that grew throughout the summer period, in particular during August and into September, about an increased financing requirement. That went hand in hand with speculation around the energy package, because that was clearly deemed by the market to be a very significant potential cost to the Exchequer. As a result, the market already began to factor in what it estimated the potential impact would be.

It is fair to say that it was really only in the immediate run-up and the last two weeks or so prior to the mini-Budget, fiscal event or whatever that the numbers, and the speculation in the market around what those numbers might be, began to increase in the market. Originally we heard something in the region of £10 billion to £15 billion, maybe about two to three weeks before. Then there were some very large numbers, also in terms of their potential impact next year, that were being bandied around in the immediate run-up to the 23rd.

Q141 Chair: We had a circumstance where there was not a lot of information given, but the announcements about the energy support package were made first, in a discrete way but with no detail on costs. Then we had the period of mourning for the Queen, before we went into the rest of the mini-Budget. What effect do you think that had on the way that the market was responding?

Sir Robert Stheeman: Because the precise amount or the precise cost of the energy support package was not exactly known, you saw a lot of speculation in the market, a lot of analysts, bank analysts in particular, trying to anticipate what they thought it might cost. I would add that, in general, you always have this speculation and how it might translate into our financing requirement ahead of any fiscal event. In this case, it was quite marked and it varied enormously depending on people's views of what that cost would be.



Q142 **Chair:** And depending on what is happening to energy prices.

Sir Robert Stheeman: Absolutely, but it seemed to increase constantly in this period, in the run-up to that. It is fair to say that some of the other measures that were then announced might not have been anticipated.

Q143 **Chair:** Do you think that it would have calmed things down a bit ahead of the mini-Budget if there had been some attempt at least to cost a potential range of what the energy support package might cost? There were literally no costings of any kind, which left the field completely open to the speculations that you are talking about among bank analysts and others.

Sir Robert Stheeman: Potentially, yes, but I am also trying to be fair. The precise nature or precise cost of the energy package in particular was not known and I would almost say even now is not known. You can make a costing but, as you have indicated, ultimately, that is subject to what energy markets themselves are doing. It was quite hard and the danger with any number that is based on any kind of estimate is that it ultimately gets proven wrong.

Q144 **Chair:** The £75 billion of unfunded tax cuts that were there in the mini-Budget would have seen an additional borrowing requirement that we have talked about. Do you think that you would have been able to meet that requirement without yields becoming untenable?

Sir Robert Stheeman: I should say that our present financing requirement, as of today, is still very much the financing requirement that was announced on 23 September. I am confident that we will meet that. I am not saying it is necessarily going to be easy. Regardless of what might have happened very recently, the market overall is clearly, to use a popular word, volatile. It is stressed and we should not pretend otherwise.

Inevitably, we will look at things through the lens of the United Kingdom, but all of the developments we have seen in the market, here in the UK but also elsewhere, have to be viewed against the backdrop of, since the beginning of the year, rising interest rates on the back of tighter monetary policy, all of which makes this quite a challenging and difficult backdrop. To answer your question directly, we will meet that financing requirement.

Q145 **Chair:** There was significant volatility in the UK gilt market after the mini-Budget on 23 September. To what extent do you think that was caused by the mini-Budget itself, rather than the background that you have just talked about, which is general volatility. We have the very illustrative chart showing UK gilt yields, which Sir Jon Cunliffe sent in a letter to the Treasury Committee, which indicates there was clearly a UK-only effect. What is the feedback you have had from your engagement with the markets about that? Are we really the wildebeest that has now fallen behind the herd that the wolf pack are after, or have we managed



to somehow get back into the herd and acquire the safety that there is in a herd of wildebeests?

Sir Robert Stheeman: You are absolutely right to put your finger on the issue, which is how you untangle what is UK-specific, based on what has happened here, and what is going on elsewhere. That is quite hard. Having said that, we have to admit or acknowledge that, quite clearly, UK influences were prevalent, especially in this period, immediately in the run-up to the 23rd and afterward, without a shadow of doubt.

You saw that because the volatility that we were seeing in yields—and this is absolutely borne out by Sir Jon's letter—exceeded by a very large margin the volatility that you would have seen, for instance, in the US Treasury market or in the European Government bond market. Clearly, there were UK factors at play. I am loathe to put an absolute figure on how much you can ascribe to one or the other, but I want to be very clear that what we saw in the gilt market was clearly the impact of a UK-specific situation. One has to acknowledge that.

Q146 **Chair:** To what extent have we managed to get back to the herd, to use my earlier analogy? The wolves are at our heels.

Sir Robert Stheeman: The wolves are at our heels. I am thinking of one of those David Attenborough films.

Chair: They do not always end well.

Sir Robert Stheeman: Occasionally they do. I point to two things and I want to do so without suggesting that everything is absolutely fine either. First, it is notable that actually 10-year gilt yields are now back to where they were prior to 23 September.

More importantly, to your question, the underperformance that was also noticeable, the higher risk premium that the market was demanding for gilts compared to US Treasuries or European Government bonds, but US Treasuries in particular, now seems to have reversed. There was a period, and that period had started in early September already, but was very prevalent after the 23rd, where 10-year yields in the United Kingdom rose above those in the US. That is unusual. That was, I believe, the first time since 2014. I am trying to extract that.

The best way to try to determine the actual UK-specific element is to also look at what is happening elsewhere. You cannot do that completely scientifically, if only because in so-called normal times you would expect the biggest determinants of yield to be expectations around monetary policy. Clearly, in as much as the measures that were announced on the 23rd also fed into the market's expectations around monetary policy, that was also reflected in yields.

Q147 **Chair:** We would have a higher rate of interest as a result of the Budget than we would have without.

Sir Robert Stheeman: Indeed, yes.



HOUSE OF COMMONS

Q148 **Kevin Hollinrake:** I am happy to bring in your colleagues if they would like to contribute to give you a bit of a break. Can I go back to something you said, giving evidence to the Chair? I think you said that 10 days before the mini-Budget you expected a borrowing requirement of £10 billion to £15 billion.

Sir Robert Stheeman: I said that the market expected that.

Q149 **Kevin Hollinrake:** The market expected that. What were you expecting at that point? Were you at that point aware that it was going to be more like £70 billion?

Sir Robert Stheeman: I do not want to be tied down exactly on which date we were informed about the amount, but it is fair to say that—I am turning to Jessica at this point—we were informed by the Treasury about a week or so beforehand that the number was going to be considerably larger. Is that correct?

Jessica Pulay: We were informed that it was going to be larger. It was also complicated by the Queen's funeral and that period. That is why it was concertinaed so much. If you remember, the official date of the fiscal event was only confirmed quite late because of that as well.

Q150 **Kevin Hollinrake:** Yes, I am not directing any criticism at you. Why were the markets so far off? Most of the things had been mooted and there were things that were reversed subsequently. You are saying now that the borrowing requirement is pretty much the same anyway, even despite the reversals, which I will ask you about in a second. Was it the energy price guarantee that was the biggest factor in terms of that increasing level of debt requirement?

Sir Robert Stheeman: We are not responsible for exactly working out what is behind the numbers, but it is absolutely my understanding that that was by far the biggest single factor. We are not responsible for that. I cannot say X billion pounds of the overall £72 billion is down to this or that particular measure. I simply do not know. The Treasury would be able to answer that question.

Jessica Pulay: I will just add one tiny point. As the date drew closer, so market expectations grew more in line with what actually transpired, for various reasons. The final number was more or less in the range.

Q151 **Kevin Hollinrake:** Is it your role, when Treasury indicates the likely borrowing requirement, to say, "That is going to cause some problems in the market. You might get a spike in the bond yield on that basis"?

Sir Robert Stheeman: I will have a quick stab at that. To an extent, yes, but we need to be clear about what our role is. Our role is about, ultimately, advising Ministers on how best to design the remit, based on whatever number we are asked to raise. That means, as I say, advising on market conditions. I do not want to go into too much detail of what advice was offered, when and how, but I can assure you that we were in



HOUSE OF COMMONS

close contact with colleagues in the Treasury, officials, on exactly these sorts of points, on the fact that this was likely to result, potentially, in higher borrowing costs. That was what you would expect us to do.

Q152 **Kevin Hollinrake:** This is not a small increase in borrowing costs. It was 100 basis points, and 150 basis points at one point.

Sir Robert Stheeman: We certainly did not try to put that sort of a figure on. We would never try to do that because, ultimately, we do not know better than the market does. The fact that markets were already stressed and already pricing in projected bank rate rises and monetary policy tightening was a key part of what we were monitoring and feeding back.

Q153 **Kevin Hollinrake:** A rise of 150 basis points over that period of a few days was not a surprise to you.

Sir Robert Stheeman: I would happily say it was a surprise and I would guess that it was a surprise to virtually every market participant as well. Otherwise every market participant would have been able to make rather a lot of money, because they know exactly what is going to happen. No one knows that. This very large rise was a sign of the extreme volatility and hence, at that particular time also, illiquidity in the market.

Q154 **Kevin Hollinrake:** You said earlier that the borrowing requirement would be roughly similar now to what it was on 23 September.

Sir Robert Stheeman: The point I was trying to make is that it has not been changed yet.

Q155 **Kevin Hollinrake:** The Chancellor's reversals amount to about £32 billion. The difference in in corporation tax will be down the line, of course. You would expect, on that basis, that there would be some change to the borrowing requirement.

Sir Robert Stheeman: As I understand it, it was also announced today that what I believe is now going to be an Autumn Statement on 17 November will be accompanied by an OBR forecast. That OBR forecast will also produce a specific forecast for the CGNCR, the central Government net cash requirement, which forms the basis of our financing requirements. We will have to wait to see exactly how these measures are costed. That will all be announced and any change to our financing remit will be announced at that time.

Q156 **Kevin Hollinrake:** I think you said before that the bond yields now are back to where they were before 23 September. On the basis that there is a direct relationship between bond yields and certainly fixed rate mortgages, likely to be fixed rate mortgages, is everything back to where it was, so there has been no impact on the likely borrowing costs in terms of mortgages and the like?

Sir Robert Stheeman: No. I am not a mortgage expert, but clearly this feeds through and these things take a long time to play out properly. The



fact remains that further monetary policy tightening seems to be priced into the market. That clearly has a consequence across the entire economy. 10-year yields, or 30-year yields as well, might be now roughly back to where they were then, but—I get this also from reading or listening to the media—all the press suggests that mortgage costs are higher now than they were a month ago.

Q157 Kevin Hollinrake: That is partially due to the risk premium people are attaching to the UK?

Sir Robert Stheeman: I do not quite know how each and every mortgage is priced by every lender, but I would say it is just the wider environment and we are now in a much higher rate environment than we used to be.

Q158 Kevin Hollinrake: In terms of those factors and others relating to people who might consider increasing the risk premium on the UK right now, once we get to 17 November and there is a full fiscal forecast and an OBR forecast as well, do you think those things will wash out of the system at that point, all being well?

Sir Robert Stheeman: I would very much hope so, but I am not predicting anything. I said earlier that I think that it will be challenging certainly for the rest of this financial year. We should not pretend otherwise. If I think back a little bit over the last 10 to 15 years, and I have been at the DMO now for a fair bit of time, we have always had a number of unique advantages in the UK, also around the whole institutional credibility set-up.

The word “credibility” is related to the word “credit”. Ultimately, behind your question is one around the perception of our credit. There was a real concern around that after the 23rd. That concern has, to a significant extent, receded. Whether that will be gone completely in the future is very hard to say. I need to stress this, and I am trying to be as objective as I possibly can. The market is doing its best at the moment to price in what it feels future not just fiscal or monetary policy but wider policy issues are going to be. There is perhaps a greater degree of confidence in the market now than there was a few weeks ago.

Q159 Kevin Hollinrake: This is my final question. As that feeds through to the gilt markets, are you confident you would be able to get your auctions of gilts away, given that greater confidence and more liquidity in the market?

Sir Robert Stheeman: That is a very fair question. I am confident that we will meet the remit requirements. I am very confident about that. Having said that, I first have to acknowledge that this has been, and will continue to be for some time yet, a challenging environment.

Secondly, it is important to say that every single one of our operations is what is described in the market terminology as a risk event. Arguably, it is a risk event for us and a risk event for the market. There is never any



guarantee that, for instance, a particular operation, such as an auction, will, on any given day, be sufficiently covered. There are always risks around that, even in good times. I cannot exclude that there might be the odd bump along the road on the way to 31 March. I cannot exclude that, but, in the end, I am confident that that requirement will be met.

Q160 Harriett Baldwin: Into this mix of rising global interest rates and a fiscal statement that surprised everyone with its size, we also need to add in the fact that the Bank of England has switched to quantitative tightening. I want to focus my questions on quantitative tightening. I was asking the deputy governor at the beginning of September about the impact that this switch could have on the gilt market, given that it was going to be coincident with a lot more issuance of gilts by the Government and the markets are pricing in rising rates around the world.

Sir Robert, you are on the record as having said in the past that you felt that, with quantitative easing, there was an equilibrium—I think you used the word “equilibrium”—in the market between the issuance that the DMO was doing and the purchasing by the big purchaser in the market, the Bank of England. That has now ended, so can you definitively say that equilibrium has ended in the gilt market?

Sir Robert Stheeman: Previously, especially when QE was active, when it was being carried out, in effect we had one big seller, which was us, and one big buyer, which was the Bank. That is what I meant by equilibrium.

Q161 Harriett Baldwin: We have two big sellers now.

Sir Robert Stheeman: We now have one very big seller and one somewhat smaller seller, in the Bank. Clearly, that is a very different dynamic. I want to acknowledge that. Net issuance is the way the market looks at this, net of purchases. The market is trying to anticipate what is supposed to be coming or what might be coming, in terms of supply to the market, and how that needs to be absorbed.

It is absolutely true to say that we now have a situation where, from now on—and the Bank intends to implement active sales of the asset purchase facility portfolio starting next week—net issuance to the market will be the highest in history. It will be even higher than during the coronavirus period when, while our nominal borrowing requirement was much higher, there was QE going on in the background. There will be an enormous amount of net issuance.

You would normally expect how that plays out to be a question of supply and demand. If there is a lot of supply, theoretically, we will need the price to fall, and yields potentially to rise, in order for that supply to be taken down by the market at a clearing level.

Q162 Harriett Baldwin: What I am trying to pin you down on, Sir Robert, and you are evading so masterfully, is whether we have found a new equilibrium, or whether we are in a period of disequilibrium in the gilt



HOUSE OF COMMONS

market.

Sir Robert Stheeman: I am being cautious because I am trying to imagine what disequilibrium actually looks like. If you mean the absence of one big buyer while we are selling an enormous amount of gilts, yes, there is an element of disequilibrium.

Q163 **Harriett Baldwin:** It would mean higher volatility, would it not?

Sir Robert Stheeman: It means higher volatility.

Q164 **Harriett Baldwin:** What are you seeing in terms of option prices on gilts then? What is volatility doing there?

Sir Robert Stheeman: Everything, theoretically, is priced in right now to the market. At any given point in time, the market has full knowledge of what we all know, in terms of expectations.

Q165 **Harriett Baldwin:** Is it expecting it to be more volatile?

Sir Robert Stheeman: Yes, clearly, and not only expecting it to be more volatile. You have actually seen that recently as well. That is another factor in terms of gilt movements over the last few weeks as well. It is just incredibly hard to disentangle one cause of volatility from another, whether one is QT or whether one is what we have just been discussing previously.

Q166 **Harriett Baldwin:** I am going to try to drill down in the independence of the Bank of England from your organisation, because presumably there is a formal independent relationship there. How much do you co-ordinate on a day-to-day basis now that the Bank has moved into quantitative tightening?

Sir Robert Stheeman: That is a very reasonable question. It has always been a key part, also, of our whole overall institutional credibility that monetary policy and debt management policy are kept separate, ever since QE was first initiated, back in 2009. Decisions around QE and QT are purely for the Bank.

On the question of co-ordination, the size and pace are not for us, in the DMO, to decide upon. We have had discussions—the Bank has been very clear that that was always its intention—together with the Bank, around, if you like, trying to minimise, as far as is possible, disruption to the market directly caused by the Bank's sales.

Q167 **Harriett Baldwin:** Jim, from an operational point of view, are you having ongoing operational discussions? The Bank has now switched away from long-end sales. It is concentrating on the short and medium end of the curve. How much ongoing operational discussion is there, despite the Bank of England's independent decision-making?

Jim Juffs: From the operational point of view, we have had operational discussions.



Q168 **Harriett Baldwin:** Are they daily?

Jim Juffs: They are not necessarily daily. For example, in the formulation of our own issuance plans, we will be looking to schedule our auction dates so they do not coincide with the Bank's own operations. As a general rule, our gilt auctions tend to be held in the morning and the Bank's operations would tend to be held in the afternoon.

Q169 **Harriett Baldwin:** Are you working together in terms of which maturities you are selling? Has the fact that it has avoided the long end changed your operational activities?

Jim Juffs: On the whole, from my side—I think also from the policy and markets side, Jessica—there is a regular and open dialogue between us and the Bank. Would that be fair?

Jessica Pulay: That is fair. To answer your question a little more, the decision to focus its sales on the shorter maturities is quite a recent one. It post-dated our own publication of our remit and was in response to the volatility that we had seen at the longer end.

Q170 **Harriett Baldwin:** You have not changed any of your plans in terms of the maturities that you will be issuing.

Jessica Pulay: Our maturities were announced publicly on 23 September, so we have not, at this point, changed anything, no.

Q171 **Harriett Baldwin:** Are you changing anything in terms of the number of green gilts that you are going to issue? Has the volatility changed in the green gilt market at all?

Jessica Pulay: That is a very good question. We committed at the beginning of this fiscal year to issue £10 billion worth of green gilts and that has not changed. That commitment stays. We have already done two operations in green gilts this year. We reopened the inaugural green gilt 2033 that we launched just over a year ago. We did that via auction in May. More recently, in September, we did a reopening of the green gilt 2053 that we launched last October. That commitment to the programme remains ongoing.

Is there more volatility in green gilts than in standard gilts? I would say not especially at this point, because the volatility affects the whole fixed income complex, if you like. The green gilts are obviously not immune from that.

Q172 **Harriett Baldwin:** Have any of your issuances had very worryingly low levels of cover?

Jessica Pulay: That is also a very good question. If you look at our auction cover ratios, even in the very volatile period, it is actually quite reassuring to see that cover ratios have been very robust. Even around the period where volatility levels got very high in late September, following the fiscal event, we had an index-linked auction that was well



HOUSE OF COMMONS

covered. The cover ratio on 27 September was slightly lower than some of the ones that we have seen, but not especially. In fact, the cover itself was quite in line.

We do not only look at cover. That is just one metric that we observe and it does not necessarily paint the whole picture, because the cover ratio is just a representation of the amount of appetite on that particular day. We also have to look at, for example, where that bond clears at auction relative to what the price is in the secondary market. That can move around. If you look at the overall picture since the beginning of September, our cover ratios have remained relatively robust, including this morning, by the way, because we did an auction this morning.

Q173 Harriett Baldwin: Correct me if I am wrong, but I am hearing that, while the Bank itself has changed the length of the maturities that it is prepared to sell in its quantitative tightening, at the Debt Management Office you have not really made any big shifts. You are continuing with the remit that you had before. You are co-ordinating on a daily basis, in terms of the morning and the evening issuance, but you have not had to make any very big shifts in your plans. Is that right?

Sir Robert Stheeman: That is 100% correct. I will touch on exactly that point, because it is an important one. As early as March 2009, when QE was first implemented, the then Chancellor wrote to the then Governor and made clear that “the Government will not alter its issuance strategy as a result of the asset transactions undertaken by the Bank of England for monetary policy purposes”. That means that we, the Government’s issuer, are not trying to take advantage of, to use or to adapt our issuance strategy as a result of what might be decided for monetary policy reasons, in other words QE or now QT. That is a fundamental principle of this divide that we referred to.

Q174 Emma Hardy: Good afternoon, everyone. I want to drill down on whether the Bank of England’s policy interventions have distorted the price mechanisms of the gilt auctions. That is what I would like to explore. Sir Jon Cunliffe told us on 18 October that the gilt market operation “was not intended to prevent markets from making the necessary adjustment to changes in the fundamental determinants of gilt prices—including the Government’s changes to fiscal policy—which is a necessary part of gilt market functioning”. Did the Bank achieve this, or did the Bank’s intervention prevent the market from discovering what the true price of UK sovereign debt risk was?

Sir Robert Stheeman: My opinion is that, largely, the Bank was pretty successful in its operations in stabilising the gilt market at a time when there was a huge amount of volatility. There is one particular day that I think everybody is aware of, which was 28 September in particular, where intra-day movements I think were more than 1% at one point, which is utterly unprecedented. Part of that was a direct result of yields that had spiked higher coming all the way back down, following the Bank’s announcements.



HOUSE OF COMMONS

My sense is that the actions of the Bank, in terms of what it announced in terms of purchases of long-end gilts, time-limited purchases and the same also later on with inflation-linked gilts, went a very long way towards stabilising the market. As Jessica noted, it allowed us to continue with our issuance according to the plans that we have. It should be acknowledged that the Bank went a very long way towards stabilising the market, yes.

Q175 Emma Hardy: Does it concern you that the price of UK gilts may have been, in the previous weeks, more in part determined by the Bank of England than by actual market conditions?

Sir Robert Stheeman: The short answer to that is no, it does not. If the Bank is ultimately helping to achieve stability and allow better market function, giving market participants confidence to return to the market, to trade the market, to give the gilt-edged market makers confidence that they could take positions in that market without violent movements and the sort of volatility that we witnessed, that is, longer term, a much more reassuring note for the market. It demonstrates to the entire market and, arguably, to the entire outside world that the central bank is also fulfilling a financial stability objective.

Q176 Emma Hardy: If I have interpreted what you have said correctly—and tell me if I have not—you are saying that the actions the Bank of England took to stabilise our worth, if that is the right word, could have impacted on what might have been the correct price of UK gilts. Is that correct?

Sir Robert Stheeman: The point is that I am not sure that the extreme movements we saw as a result of the volatility around the end of September and into October themselves were reflective of what the true price should or should not have been. There are so many factors that go into determining gilt prices and yields. I do not think that it is possible to actually separate that out. If the market was dysfunctional, which it was at that point, restoring good market functioning, to me, seems a good way to restore proper price discovery.

Q177 Emma Hardy: The Bank will obviously be unwinding its interventions it made in the gilt market in response to the mini-Budget. Will that affect your auctions?

Sir Robert Stheeman: The short answer is that I do not know, because the Bank has not said anything about how or when it intends to do so. I would like to think that the Bank will try, as it is planning to do with QT, to be as circumspect as possible in terms of how it disposes of those holdings. It has not said anything at all about that yet, as far as I am aware.

Q178 Emma Hardy: Andrew Hauser from the Bank told us that “the differentiator between [the Bank’s recent operation] and monetary policy is that it should be temporary. That therefore means that we need to get out in a timely way. That does not mean a stupidly fast way, but a relatively rapid way, subject to not disturbing the market.” Have you



HOUSE OF COMMONS

taken that need for speed on board?

Sir Robert Stheeman: That is one for the Bank, because that is clearly its decision. It is the one that has acquired the bonds. I do not know whether I should be interpreting Andrew's comments, but I think he is trying to reassure that this was not a monetary policy operation. It does not want to sit on these holdings as part of its monetary policy operations. It wants to sell the bonds soon, but it will be very mindful of conditions and will not do it, as he says, in a stupidly fast way. I am sure that the Bank never does anything in a stupidly fast way.

Q179 **Emma Hardy:** I wonder, when it comes to making decisions about how the Bank acts, what is the level of communication? Does it have any communication with you about the decisions it is making?

Sir Robert Stheeman: As Jim noted, there is certainly a lot of discussion around, for instance, what I would describe as the boring operational matters, so timings of their operations, to try to avoid clashes with our own operations. These are, fundamentally, decisions for the Bank and it does not seek our input directly on them. It will say when it will decide that. In the case of, for instance, QT, in the case of what I would call monetary policy matters, it will be the MPC that will decide the timing, size and pace.

Q180 **Emma Hardy:** This is my final question. Do you think the Bank ending its participation on 14 October surprised the markets?

Sir Robert Stheeman: Probably it did, but it also reassured the market.

Q181 **Emma Hardy:** Could you elaborate on how it surprised and reassured?

Sir Robert Stheeman: Occasionally, if I may put it this way, the market can try to game the authorities. My view on things is that, in as much as it would have been an easy trade for the market to say, "Would it not be nice if the Bank keeps on buying this stuff, so we can continue selling it", the fact that the Bank made clear that it did not want to do that and it was setting a clear deadline was also a bit of a wake-up call, perhaps, in a positive way, to the market that it should not assume that the Bank was always going to be there as a backstop.

Some of these questions are probably better answered by the Bank than me, but having certainty is always incredibly important for the market. That is a little bit what I am trying to hint at, in terms of reassurance.

Chair: I suspect that the Governor's insistence on that hard date was not only a signal to the market. I suspect that it was also a signal to the Government, who are in control of fiscal policy.

Q182 **Rushanara Ali:** Good afternoon. Apologies if you have already covered this question and apologies for not being able to be here from the beginning. On that question about certainty, do you have a view on the change of date for the statement that was due to come on Halloween to 17 November and how that will affect the markets and, by implication,



affect you?

Sir Robert Stheeman: The question has not come up and it is a very valid one. I just mentioned the importance of certainty. On one level, the market might be a little disappointed that the certainty that they were anticipating as soon as this coming Monday is not going to be there. On another level, the market might also feel, given the fact that this is a full-blown Autumn Statement, that there will be much more certainty around everything, in terms of fiscal measures, that the Government are planning for the immediate future.

Actually, I do not think it is going to have too much effect—I hope I am right about this—on the market. Put it this way. I looked at screens before coming here. In the immediate aftermath of today's announcement, there was not much movement.

Q183 **Rushanara Ali:** Antoine Bouvet, who is the rates strategist at ING, said that delays were “bad news for gilts”. “Delaying the Budget statement until after the BoE meeting won't force the Bank to take it into account in its economic forecast and push back more forcefully against hikes priced on the curve”, he said. I do not know what time he said this, whether it was before you checked and arrived, but there seem to be some differences. Also, the point about what the Bank can do in line of sight is an important one, but we will have to wait and see. I wondered whether you wanted to comment on some of those observations.

Sir Robert Stheeman: He was highlighting my point about two and a bit more weeks of uncertainty. That is a valid point. At the same time, as I say, that is one view. Do not forget that the market is made up of lots of different views all at the same time. The other view is, “We will get greater certainty around fiscal measures and wider fiscal policy”. These balance themselves out.

Q184 **Rushanara Ali:** That is provided there is not any political instability in the next fortnight. Let us hope that there is not, for the sake of our economy. I have one other overarching question before I go into the specifics around market instability on 26 and 27 September. It is a wider point about the state of Britain's economic reputation, some of the interventions that have been made by external players over the recent period, including the IMF and so on.

Guy Hands, who runs a private equity firm and is a Tory donor, said that the UK faces higher taxes, lower benefits and a possible International Monetary Fund bailout. We have had the last six years post Brexit, partly due to poor negotiation of a Brexit deal and so on. He talks about “mistakes they've made in the last six years which have frankly put this country on a path to be the sick man of Europe”. The context of that is of course about becoming indebted and a whole series of issues that are well rehearsed in recent weeks.

What do you make of that observation? Should we now be less concerned because we have a new Prime Minister and the markets seem,



temporarily anyway, a little calmer than they have been? Should we be concerned about these observations? We have not heard phrases like that in a very long time, but the recent episode in the Truss Government and the events of the 26th and the 27th have led even Tory donors, who are supportive of the Government, to make those observations. What is your view on that?

Sir Robert Stheeman: Because I am a markets hack, I just view these things from the perspective of the market. We can all look at the events of the last few weeks. If you look at them through this market prism, as I was saying earlier as well, clearly some of the concerns that, as you mentioned, Guy Hands expressed were being played out in the market. That is not great.

Q185 **Rushanara Ali:** It is a disaster, is it not? It is an embarrassment for our country. Even emerging markets were having a field day looking at the state of what had been done to our economy. Basically, it was political irresponsibility. What you are saying is an understatement, is it not? Is it not a total disaster and are we not a laughing stock to the rest of the world now?

Sir Robert Stheeman: I am prone to understatement, which is probably a very good thing.

Rushanara Ali: It is admirable under the circumstances.

Sir Robert Stheeman: I will try to continue being as understated as possible.

Chair: We do not want overstated people to be in charge of selling our gilts.

Sir Robert Stheeman: I am reassured. Thank you. I want to acknowledge an important point that you are making indirectly. This is a very markets view, but it is quite an important one. The UK gilt market, notwithstanding all our trials and tribulations, is and remains a very important global fixed income market. Fixed income markets globally are a matter of relative value and relative valuations. We always talk about the market as if it is a single thing, but it is not. The market will always look at how we are faring compared to, for instance, as I mentioned earlier, the United States, Germany or other jurisdictions.

To use Dame Angela's expression, we do not want to be that little wildebeest who strays too far away from the herd. If we can get back into the herd and if we can be viewed as anything but an outlier, that is obviously important. The comment that you quoted from Guy Hands was precisely a concern around us being an outlier and being viewed as an outlier. We have seen the consequence of that played out in the market. We have also seen played out in the market—and I really believe this—a much clearer acknowledgement and vote of confidence in terms of the subsequent direction that Government have taken.



Q186 **Rushanara Ali:** It is debatable whether the Government took—

Sir Robert Stheeman: I am only saying what you see in the market.

Q187 **Rushanara Ali:** The Government had to take that direction because of the reaction of the market and the actions of the Bank of England and the independent institutions, which have had to reassert their authority, ultimately. That is why it happened. I will move on. Thank you. I appreciate the response and the candidness, albeit with understated language.

In the revision to the DMO's financing remit published on 23 September, there was an offer to market participants to provide feedback on the provisional operations calendar by 26 September. What was the feedback like?

Sir Robert Stheeman: This is what we will almost always do after a fiscal event. The feedback was focused almost solely on what I would call operational matters for us. The direct consequence of the remit revision on the 23rd was that we had to operationally schedule 13 more auctions between then and the end of the financial year. The questions that we then ask the market, and, in particular, our gilt-edged market makers, are around the sequencing of that: which operations should be scheduled on which day? What are their views? What particular issues would they like us to see—shorts, mediums or longs?

It is all around the operational delivery. It is not a view on whether this is a good thing or a bad thing. The market, like we do, just takes for granted, ultimately, what our political masters will decide. They will see that borrowing number. The market will then give us feedback directly on the best way to deliver that financing.

Q188 **Rushanara Ali:** Feel free, others, to come in if you need or want to. How does this period compare with other times?

Jessica Pulay: One of the issues for us compared with the Covid period in 2021¹ is when the statement actually happened. In Covid times, we were given much longer. We had a huge financing remit, as you know, well in excess of what we are going to be issuing this year in terms of the DMO's issuance. It was announced in April, then it was extended into July and then extended again. We had a significant amount of time in which to deliver that.

Q189 **Rushanara Ali:** You knew it was coming.

Jessica Pulay: We did not know exactly what was coming.

Q190 **Rushanara Ali:** Once the pandemic hit, you knew the Government would have to take a series of unusual actions.

Jessica Pulay: Yes, exactly, and, as has already been discussed, there was already a big buyer in the market, which was helpful. The difference

¹ The witness later clarified that she meant to refer to the "Covid period in 2020".



HOUSE OF COMMONS

here is that we do have a very compressed amount of time in order to deliver the amount that was mentioned on 23 September.

Q191 **Rushanara Ali:** Would you say that was unprecedented?

Jessica Pulay: In terms of net supply, i.e. without a big buyer in the market, it was unprecedented.

Jim Juffs: I will just give a bit of context on the number of operations over the course of the rest of the year. We had the 13 plus one as an extra. Over the whole of the 12 months, we are delivering around 71 operations. That compares with 71 last year, but the pandemic year was around 159. There is only one year prior to then, in the almost 25 years of our history, that we did anything near that. That was close to the financial crisis, where we did 77 operations in a year. Just to recap, in 2022-23 we will be doing 71 operations. That is the same as last year. In the pandemic year, which was an exception, we were up at 159, where we were raising £40 billion a month. It is quite a large number.

Q192 **Rushanara Ali:** Andrew Hauser of the Bank of England recently provided the Committee with a graphic description of his increasingly worrying conversations with LDI funds before the Bank's gilt market intervention on 28 September. Can you describe to us what market participants were communicating to you across this period? By all means, feel free to use understated or colourful language, whichever takes your fancy. He used quite colourful language.

Sir Robert Stheeman: I have already warned you I try to avoid colourful language. Clearly, the market was extremely stressed. We were hearing directly from market participants just how stressed matters were. The Bank was obviously hearing it too. I even recall that Andrew Hauser sent me a message and asked for my views, wanting to know what we were hearing from the market in terms of linkers in particular. There was a real concern. I heard directly from one or two pension funds that operated LDI schemes saying what stress they were under. I know that they also made the same representations to the Bank of England. There was a lot of stress at that time, it is fair to say.

Sometimes terms are thrown around. There is a doom loop, which I do not particularly like because it also does not describe exactly what was going on. In my opinion, what you saw happen was actually a classic situation that occurs in finance where, arguably, existing risk management strategies were exposed as not having been adequate.

Q193 **Rushanara Ali:** Could you say a bit more about the risk management strategy? Who should have done that risk management strategy better? Are you saying that there are some things that the Bank should have done?

Sir Robert Stheeman: No, I am talking specifically about the pension funds.



HOUSE OF COMMONS

Q194 **Rushanara Ali:** Is that something that the regulator should have done more about? Is it that they did not factor in a set of decisions, such as unfunded Government tax cuts of the order that we saw without independent forecasts and so on? Should they have factored that in as part of the risk management strategy?

I asked an equivalent question to the Bank of England about whether stress testing now needs to extend to a set of fiscal policy decisions that Government make. If they do not make them in the normal way, with warnings and with independent assessments, then it is clearly a risk to financial stability, as stated by the Bank of England. Are we now saying the risk management in relation to the Pensions Regulator needs to factor in those sorts of scenarios? That is essentially what would have needed to be done in this scenario.

Sir Robert Stheeman: We are not a regulator. It is very important to say that. What is clear and has been clear to the entire market is that the extent of the margin calls that some of these funds faced was never anticipated, because they equally did not anticipate the sort of price movements that you saw occur in the gilt market and the movements in yields to that extent. This is what happens in any leveraged position. You will have heard, as we did, that supposedly the big issue was around liquidity rather than solvency. There is a clear lesson for everybody there, which is you always need to be in a position to meet your obligations.

Jessica Pulay: Just to add one tiny point to that, market conditions were already fragile, even before 23 September. They had been throughout a lot of the summer, including particularly in the gilt market as well. Therefore, it was against that backdrop. It was partly the magnitude of the moves. Remember that there was also a bank rate decision on the 22nd as well. It was also the velocity of the moves that were problematic, probably from a stress testing point of view.

Q195 **Alison Thewliss:** I just have a couple of questions around how you operate when there is volatility in the gilts markets. I heard you say earlier, Sir Robert, there are no guarantees for any of your auctions. When you are facing volatility as we have seen in recent weeks, would you consider postponing auctions?

Sir Robert Stheeman: Generally, we would not consider doing that unless there was an extremely strong reason to do so. The reason for that is the market sets great store in knowing that once we announce plans, unless there is a very strong reason, usually outside our control and not to do with markets, we will not deviate from announced plans. That allows market participants to factor whatever it is that we have announced previously into their own decision-making process.

For instance, were we to decide to move an auction because we are concerned about demand on the day, the market would also have to try to factor that in. Then we start to become a source of uncertainty ourselves in the market. That is not helpful to the market. What the



HOUSE OF COMMONS

market values from us is consistency as well. We try as much as possible to maintain that.

I always take a view around auctions. I am not saying it is likely, but there is always a possibility that there may be an uncovered auction. We have to take the rough with the smooth. We have to say that, if there is uncovered auction, we will deal with it. We have processes. Those are tried and tested, and the market knows all of this. The market does not suddenly want us to become unpredictable in what we are doing.

Q196 Alison Thewliss: What would an extremely strong reason look like? Could you give an example of what exactly that might be?

Sir Robert Stheeman: Usually—this is where we have moved operations—it is to do with, for instance, an announcement around a fiscal statement of some description. I am not giving anything away. We will have to think quite carefully about the implications of this morning's announcements, because the auction calendar has already been published. This happens, unfortunately. From our parochial DMO perspective, after you have set out a wonderful calendar that you think is perfectly designed for the market, these things are always frustrating, but that has always been the case. There is nothing new there. This is the point I need to make: we will rarely move anything because we are worried about the market. For us to move an auction, that is different.

The one difference here is perhaps when it comes to so-called syndications. Syndications are by definition much more flexible tools for issuance. They are not a formal part of the calendar where we announce in advance a very specific date or a very specific size. They are deliberately designed to be flexible. Occasionally, we have adjusted syndication dates to make way for certain things. We are planning a syndication. We have been planning a syndication in a couple of weeks. I am not saying it is not going to happen, but we will need to carefully consider the implications of today's announcement. That is where we have to work with the market.

Q197 Alison Thewliss: Looking at the issuance calendar, you would have had a bit of a gap if it was Monday, on either side.

Sir Robert Stheeman: There was a reason for that.

Q198 Alison Thewliss: You have some down for Tuesday 15 November and Wednesday 16 November. Is that correct?

Sir Robert Stheeman: Indeed, it is 15 and 16 November. I am not saying right now that we will definitely not move these. We will have to think very carefully and very quickly about whether it would be appropriate. It would not be unprecedented in that situation to change something, such as just changing the dates or trying to adapt.

Q199 Alison Thewliss: Would you be more likely to move that forward or move that back?



HOUSE OF COMMONS

Sir Robert Stheeman: At this stage, I would not want to say. You are right to note that there are gaps. Those gaps are also there by design. Very often they are there because we target a specific week for syndications. Of course, if various announcements happen, we find ourselves having to rearrange things on an operational side. This has happened not just today but also in the last weeks. That probably drives the operational side of the office nuts, but it has always done that.

Q200 **Alison Thewliss:** What are the wider implications of those movements that you have to make? What impact does that have? What impact does that have more widely when you have to move things about?

Sir Robert Stheeman: It is more a scheduling thing. We also need to consider what that means for our cash management operations in particular.

One thing to note, which is perhaps not so apparent, is that everyone assumes, correctly, that we are the issuer of gilts, but, in terms of the actual activities of the DMO in volume terms, when we carry out Government cash management, that has a far greater scale than just the debt management side of things. Because each gilt auction or syndication is associated with cash flows into Government, if we were to move any then we are not receiving funds on the day that we would expect to receive them. We have to take that into account in our cash management operations as well. It feeds through the whole system.

Q201 **Alison Thewliss:** That is useful to know. If things were more positive or more favourable, is there any argument for bringing things forward? Do you just feel it is more important to keep it stuck in the one place?

Sir Robert Stheeman: It is exactly that. We prefer very strongly to stick with the published calendar, if we can. As I indicated earlier, we really try to avoid giving the market any sense that we are being opportunistic, which is a dreaded word in debt management circles, or that we are trying to take advantage of what is going on in the market. We try to be predictable, transparent and reasonably boring.

Q202 **Julie Marson:** I would like to bring in the role of rating agencies. In the aftermath of the fiscal event, we saw the UK's fiscal output downgraded by a couple of rating agencies. What is the impact of that on the UK gilt market? Amongst the myriad other things that the market is looking at, how important is that to buyers?

Sir Robert Stheeman: Jessica, can I ask you to come in there?

Jessica Pulay: Yes, absolutely. That is a very good question. Ultimately, any decline in the credit rating for the UK, for obvious reasons, would not come as a welcome development. That is absolutely not to say that we would necessarily expect or do not expect any type of downgrade. It is really important to underscore that we have a very strong track record built over decades in coming through volatile times, adapting to new information, including changes in the credit rating. I believe that there



HOUSE OF COMMONS

was a downgrade in 2013, by both Moody's and Fitch. At that time, there was very little reaction in the gilt market, in fact.

Perhaps it might be helpful for Committee members just to recap where we are with the credit rating agencies at the moment. The three leading ones, Fitch, Moody's and S&P, have made announcements over the last month or so. The UK has been affirmed at AA by S&P, AA- on 5 October by Fitch, and Aa3 on 21 October by Moody's. Each of them has revised the outlook to negative.

One thing that is very important to note is that rating agency decisions are essentially retrospective, in the sense that they tend to be lagging indicators in the market rather than leading indicators. That has been something that we have learnt throughout the financial crisis. Quite often, by the time a rating agency actually downgrades any issuer, particularly a sovereign, the market will typically have already responded in terms of the pricing dynamics.

It is also the case that some of the underlying factors that could prompt a downgrade are affecting many countries. The high levels of indebtedness prompted by the Covid interventions affect a lot of countries, of course. In addition to that, there are the uncertainties around growth, inflation and monetary policy, which have been cited in respect of other countries as well.

On the other hand, from our perspective at the DMO, we need to acknowledge that a downgrade could potentially lead to higher yields and therefore potentially to higher borrowing costs. It could potentially be, for want of a better term, unhelpful to the market. It is not a desirable thing. However, we continue to focus on cost minimisation, subject to risk. As I mentioned earlier, during this period, during the rating agency pronouncements, our auction results have been very robust and totally in line with the kind of results that we would have expected to see absent these kind of announcements. That is reassuring.

One additional thing to flag, which you saw to a certain extent in the LDI situation that we have just witnessed, is the increasing importance of collateral in the financial ecosystem. That is something that has become more enshrined since the financial crisis. Collateral is predicated and quite often used, but sovereign bonds in general, and gilts in our case, are important components of that collateral use within the financial system. They are used both in bilateral trading and also by central clearing counterparties. They have a vital role to play in this. That is something that is important to note, because if there were a downgrade it could affect how collateral might be accepted within the system, depending on the level.

Some tactical overseas buyers or more short-term buyers could perhaps be affected by any type of downgrade. Investors who take a longer-term, more strategic approach to the market are unlikely to be deterred by this, I suspect. I have said it would not be welcome. There could be



HOUSE OF COMMONS

reverberations across the wider economy from a downgrade. It is important to note that. In fact, Moody's this morning made the same pronouncement regarding certain banks in the UK: that they would be affected. It does not just affect our own borrowing costs but ultimately other users of the capital markets within the wider UK economy and also some international financial institutions where the UK is a shareholder. It is a wider perspective there.

It is important to flag that some of the factors that have historically underpinned the UK's credit rating are still there. The agencies cite these in their reports. They are things like the long maturity profile, which we benefit from relative to our G7 peers, and the independence of our policy-making institutions, which has been discussed here. The fact that sterling has reserve currency status, again, is very important. As Robert noted in another context, credit ratings are also about relativities. They do not just operate in isolation. It is about how a country is relative to its peer group. Quite often these decisions are made across the piece because, as I mentioned, to an extent they are part of a wider economic environment.

Q203 Julie Marson: That is a really useful assessment, thank you. Can I just press you? Would it be fair of me to characterise your response as overall saying it is one factor, an important factor, but you are not overly concerned by the recent downgrading of the outlook?

Jessica Pulay: It is important because there are symbolic issues and there are also, potentially, real issues. It is the magnitude that would cause a concern.

Q204 Julie Marson: You mentioned the reserve currency status and you said that is important. What kind of advantages does that bring us? How does that fit into the overall mix in terms of importance?

Jessica Pulay: It is important for different reasons. It is particularly important because to have that status clearly means that central banks, in particular internationally, value sterling as an asset for diversification purposes and it forms a part of their portfolios, which in terms of overall gilt demand, is extremely welcome.

Q205 Julie Marson: Do you have interactions with the rating agencies?

Jessica Pulay: Most of the rating agency interaction is conducted by the Treasury, as you might expect, given the comments on the overall economic policies and so on. Where they specifically want comments on the gilt market and the financing remit and so on, then we may have interactions.

Q206 Julie Marson: Have you had interactions in the last few weeks on that?

Jessica Pulay: No, we have not directly.

Sir Robert Stheeman: We have not directly.

Q207 Julie Marson: If I take Fitch, for example, with the overall credit rating



of AA-, we are on par with Estonia and Qatar. Do you think the risk profiles are comparable?

Jessica Pulay: I am not sure if it is helpful to make comparisons with other countries. When you look at other comparators, you also have to look at the overall sizes of the economies and, in particular, the sizes of the capital market. The gilt market remains one of the most liquid and tradeable markets in the world, albeit with some stresses that we have been discussing. From that perspective, we can take some reassurance from that.

Q208 **Julie Marson:** Who would you say were better comparators?

Jessica Pulay: That is a good question. Within the G7 community, there are some countries that are rated higher than us and there are some countries that are rated lower than us. Those are the comparators that perhaps one needs to look at.

Sir Robert Stheeman: Can I perhaps just come in there? You are touching on something that is quite interesting, because you are talking specifically about the perception of individual countries, also compared to each other, and then the associated ratings. What is significant is that the international investor community does not look only at ratings in making their assessments about whether or not to invest in sovereign debt of any particular country. Everything gets thrown into the mix, including, as Jessica says, the size of the economy, the institutional framework and the political system. Everything gets thrown in there.

The other point I would make as an observation in terms of rating agencies is they have an important and valuable role to fill, but they probably do not have, in the sovereign space, quite the same influence that they might have done 10 years ago or so, at the height of the financial crisis. My sense is that the market has slightly moved on from that. I am not saying that they are unimportant. Their influence is perhaps not as great as it once was.

Q209 **Julie Marson:** There is something that occurred to me on that. Does the rating prevent some buyers from buying gilts, depending on the credit rating? Does that have an actual stopping impact?

Sir Robert Stheeman: It could, if a particular investor has certain minimum criteria in terms of a rating. Generally, those criteria apply to lower ratings than what the UK currently has.

Q210 **Harriett Baldwin:** I have just a few mop-up questions on liability-driven investing. We have heard earlier about how we are in a market where rates are rising globally. We had the fiscal surprise of 23 September and then we have the Bank of England quantitative tightening. There was this somewhat unexploded bomb, if I may use that term, which was the fact that a lot of pension funds were fully invested in higher-yielding assets and were using leverage to neutralise their liabilities through liability-driven investing.



HOUSE OF COMMONS

We know that the Bank of England did a stress test on liability-driven investing back in 2018. They were aware it was out there. They knew that it had potential stresses for the gilt market if rates went up by 100 basis points, which they stressed as a maximum immediate shift. I just wondered how much you were involved in those discussions about the potential stresses that could occur if you had a sudden forced seller of gilts from liability-driven investing.

Sir Robert Stheeman: It is fair to say we were not involved in those discussions at all.

Q211 **Harriett Baldwin:** Were you wholly unaware that there was this unexploded bomb out there in the gilt market?

Sir Robert Stheeman: This goes back to what I was saying earlier about the scale of any participant's specific leverage. We do not have insight into the level of leverage that a particular pension fund or even financial institution might have as part of their strategy. We are not a regulator. We do not receive direct information in terms of that. It is important to understand that we have no regulatory function there.

Q212 **Harriett Baldwin:** The Bank had published this. They say they published their stress test of these particular liability-driven investment strategies on their website back in 2018. I just wondered operationally, Jim, whether you had noticed that report and it had fed into the thinking that potentially there could come a day when there would have to be a very big liquidation activity of those leverage strategies.

Jim Juffs: We had not looked in any detail at that, Harriett, to be honest. I have seen certainly in the transcript of previous evidence the levels of dysfunction or dislocation that might occur and how it has been tested before. However, as Sir Jon Cunliffe said, the levels that actually transpired were a multiple of the original.

Q213 **Harriett Baldwin:** They were much more than that. Andrew Hauser in his testimony said that he got calls suddenly late on the Friday that this was happening and there was a bit of panic setting in. Jim, at what point operationally were you brought into that conversation?

Jim Juffs: The DMO as a whole was brought in. Mainly the contact came through at a senior level. Would that be fair, Robert?

Sir Robert Stheeman: It did. I cannot remember exactly which day it was, but at that time Andrew Hauser specifically asked me what we were seeing in terms of linkers stress. That went beyond just the price action and also covered some of the feedback that we were getting. We were passing that feedback on also to the Treasury in terms of concerns around that.

Q214 **Harriett Baldwin:** Would it be possible, Sir Robert, to check your notes and your diary from the time and write to the Committee about the exact timings that you heard from Andrew Hauser on that?



Sir Robert Stheeman: I will do that.

Q215 **Harriett Baldwin:** That would be really helpful. I know that the DMO does a lot of work in terms of trying to broaden and widen the holdings of gilts, because you clearly would not want a situation where you had one investor, particularly an investment strategy that is very concentrated and leveraged, as in the case of LDI, holding a lot of exposure to gilts. Could you update the Committee on how that effort is going to make sure you have very widely held securities?

Sir Robert Stheeman: You are absolutely right; we do. Like any major sovereign debt manager, we value a diverse investor base that gives us greater resilience, especially in times such as this. If you think of the composition of the investor base at the moment, for instance, the three largest groups of investors and gilts are the overseas, the international investor base, which as of the end of September accounts for about 30% or 31% of all gilt holdings; the pension industry, in the wider sense—also life insurance companies—which were just over a quarter at about 26.3%; and then there is the Bank itself, which we do not view as necessarily a diverse investor, but it gives you a sense. These things are spread out quite a lot.

Q216 **Harriett Baldwin:** You are not agnostic about who holds gilts. You would rather they were more broadly spread, is what I just heard you say.

Sir Robert Stheeman: Yes, we would like them broadly spread, but we are agnostic in as much as we cannot control who owns gilts.

Q217 **Harriett Baldwin:** You cannot control, but you do proactively go out and inform investors about gilts, to try to widen the range of different investors who hold them.

Sir Robert Stheeman: Absolutely, we do that and we speak regularly. Also, as necessary, sometimes together with Treasury colleagues, I will actually go and visit what I would call internationally very important investors, official institutions, sovereign wealth funds and those sorts of people. In our view, that all helps in terms of having a widely diverse investor base. We very much want to encourage that, but of course ultimately these are choices that those investors themselves will make.

Jessica referenced the reserve currency aspect, which is an important part of this as well. The small percentage—and it is a small percentage; we are not the US dollar—that you will find in major central bank holdings invested in gilts is an additional source of stability for the gilt market.

Q218 **Harriett Baldwin:** Given that you were not directly involved in the stress tests that were done by the Bank back in 2018, it sounds as though you were alerted to the impact on the gilt market when you got the call from Andrew Hauser. Before that you were not really focusing on the build-up of these positions in the liability-driven investing side of the pensions industry. Is that something you are going to be focused on much more in the future as a potential source of forced selling in the market or how will



you incorporate it?

Sir Robert Stheeman: We are aware, and the events of the last weeks have shown that unfortunately this sort of thing can happen. I repeat that we do not really have precise insight into risk management strategies that individual institutions will implement. That makes it very difficult for us. This is where we need to be careful, not because I do not want us to do it, but it is simply not within our gift. We cannot and should not be straying into areas that are, correctly, reserved for the regulators.

Q219 **Anthony Browne:** My questions are going to be about who we actually owe the money to, over what maturity and, indeed, whether it matters. According to figures from the ONS—I am sure they come from you—around a third of our gilts are owned by foreign investors or overseas, and about 40% or 50% of T-bills are owned overseas. Presumably you know who actually owns them. Are they sovereign wealth funds? I know you touched on your marketing earlier. Are they foreign pension funds?

Sir Robert Stheeman: We have a rough idea. Unfortunately, I have to say it is a rough idea. I have perhaps mentioned this previously to the Committee. We have never had a precise overview of who exactly owns gilts.

Q220 **Anthony Browne:** You do not follow the secondary market. You do not know.

Sir Robert Stheeman: We do.

Q221 **Anthony Browne:** You do not know who sells them.

Sir Robert Stheeman: We do not know, exactly. A large part of that secondary market activity is simply not visible. The other point, which I have made previously but is worth repeating, is that the vast majority of gilts are held in nominee accounts. We do not have knowledge of the ultimate beneficial holder, unfortunately.

Q222 **Anthony Browne:** Do you know the geographic spread, for example?

Sir Robert Stheeman: We can speculate and we do. One of the reasons why we do this outreach that I referred to earlier to international investors is to just get a sense of what particular international investor groups might be doing, which countries might be more active depending on exchange rate movements at a particular time. We have a sense of that, but this is not hard information.

Q223 **Anthony Browne:** Does it make any difference who owns it or is it a preference from the DMO's point of view about who actually ends up buying the debt?

Sir Robert Stheeman: That is a really good question. On one very general level, I would say no. It does not matter, because the market will determine that. We cannot say, "We want this particular gilt to go to that particular investor". Having the diverse investor base, where you have an element of buy and hold, provides stability. We have that in particular



with the domestic UK investor base. Also having major foreign central banks being active in the shorter maturities and being active in the gilt market helps provide the market with liquidity. Liquidity is important for the whole market. There are advantages in having different types of investors.

Q224 Anthony Browne: One entity that has huge assets is the Russian Government and the Russian central bank. Do they own a lot of gilts, as far as you know? Have the sanctions had any impact? There is a risk there that, if they do own a lot of gilts, they might end up selling them off or not being able to sell them because of sanctions.

Sir Robert Stheeman: First of all, the straight answer is that I do not know. If they do, they hold them through nominee accounts.

Secondly, these sanctions that were introduced earlier in the year are pretty hard and they will bite. We do not see that point at which they bite, which is presumably with the custodian banks where they hold it. As you suggested, my sense is that if they do and were they inclined to sell, they might find that rather difficult. I do not know.

Q225 Anthony Browne: There has been no noticeable impact in terms of the liquidity of the markets in gilts.

Sir Robert Stheeman: There has not that we have been able to observe, nor have we heard, "There has been particular selling from Russia". We have not heard that.

Q226 Anthony Browne: In terms of maturity, again from the figures that I have seen from the ONS, the average debt maturity in the UK is 15 years, which is twice the G7 average and three times the US, which is five years. What is the explanation for that? Is that actually a sign of strength or weakness? It depends on which rates you are buying into.

Sir Robert Stheeman: It does. In general, it is a good thing. I am also honest enough to admit that it is not just because of brilliant debt management strategy on our part. It is the result of the requirement, in particular by the domestic pension industry in this country, to hold long-term assets to meet their long-term liabilities. That has been the case for the better part of more than 30 years. That has allowed us to issue long-dated debt, long-dated gilts, at attractive rates, cost-effective for the taxpayer over time. That is the main reason why we have such a long average maturity in the portfolio.

Q227 Anthony Browne: Does that not apply to other countries as well then?

Sir Robert Stheeman: No, because they tend not to have such a developed pension market in the way that we do. I am often asked by our peers in other countries how it is possible that we have got to this situation. You have to go back to see the whole evolution of pension funds in the United Kingdom since the 1980s, and also the associated regulation, which has required them to match as closely as possible their



HOUSE OF COMMONS

liabilities with long-dated assets. There really is only one large source of long-dated assets on that scale and that is us.

Q228 Anthony Browne: Finally, in terms of the households and retail buyers, it is miniscule; it is 0.2% of the total debt, whereas in other countries like Italy, famously, households buy their national Government debt. We did during wartime, with war bonds and so on. People did their patriotic duty. Is there any benefit in having a strong retail sector buying national Government debt? Is that something you want to see more of or not?

Sir Robert Stheeman: There is benefit, in the same way as I indicated earlier that it is valuable to have a diverse investor base. The answer to that is yes. I would not assume that households only own this tiny percentage. Those are direct holdings. A large number of retail savings are what I would call mutualised, through investment funds and mutual funds. The retail sector is probably going to be quite a bit larger than that.

Q229 Emma Hardy: Sir Robert, when you last spoke to us in June 2020, you said you were extremely confident there was enough demand for UK Government debt. Since then, of course we have seen increased inflation, higher interest payments on debt, the energy price guarantee and the response of the market to the Government's fiscal plans. Given the Government's continuing funding needs, are you still confident there is sufficient demand for our debt at reasonable prices?

Sir Robert Stheeman: I am confident that there is sufficient demand for our debt. As I indicated earlier, I cannot guarantee that the process of raising that debt, which is what we have to do, is always going to be smooth. These are very challenging circumstances. We see volatility in the gilt market, very noticeably in the last few weeks but also globally. It would be imprudent of me to suggest that it is going to be plain sailing.

Having said that, am I confident? Yes, because we still have an extraordinarily well-functioning market, which is supported by a group of primary dealers who often do not get acknowledged but should get acknowledged. These are the gilt-edge market makers, with whom we are in very close dialogue, who turn up every time we hold an auction, like today, fulfil their roles as liquidity providers to the wider market, to the investor base, day in and day out. Without them, our job would be much harder. I really want to emphasise that, because they are in many respects absolutely key to what we do in the mainstay of the market.

Q230 Emma Hardy: What would it take to shake your confidence?

Sir Robert Stheeman: What would shake my confidence would be market confidence being so undermined that we find that we cannot conduct our operations, our issuance programme in the way they we intended to do so. We find that we have to constantly alter our plans because of changed market circumstances. I am glad to say that has not happened, even during the period of the last few weeks and all the associated volatility, which is I am still confident.



HOUSE OF COMMONS

Q231 **Emma Hardy:** To meet the winter fuel crisis and because of recent events, the UK will be selling more debt in 2022-23, we are expecting. Will this simultaneous international expansion in the supply of sovereign debt cause demand problems for the Debt Management Office?

Sir Robert Stheeman: What it will cause is a repricing of the debt. Demand is never finite. Ultimately, the price if necessary will have to adjust in order to take down our supply in a smooth fashion. I am not predicting, therefore, that we are definitely going to see higher yields, because this is where the whole aspect of monetary policy expectations comes into the pricing in the market. As long as the market can adjust smoothly and efficiently, we will be successful in what we do.

Chair: Sir Robert and colleagues you have been saved by the bell, because there is going to be a little bit of voting going on now and I do not want to keep you here on the off chance that we might return in an hour. Thank you very much for your very interesting evidence today and the fact that you have managed to shine a light on an area of Government operations that more people need to understand because of how vital it is. Thank you very much.