# Fifteenth Report of Session 2023-24

## HM Treasury

## Managing government borrowing

**Introduction from the Committee**

Government borrows when its spending exceeds its income, which has been the case in all but five of the last 53 years. Borrowing allows government to continue to deliver important public services when tax receipts fall, or spending requirements increase. Government needs to pay interest on the money it borrows, and government's overall debt increases when it borrows more than it repays. Public sector net debt excluding the Bank of England (PSND ex BoE) is government's preferred measure for reporting on public finances. PSND ex BoE, which is the amount by which total government spending exceeds its total receipts, excluding assets and liabilities held by the Bank of England, was an estimated £2,251 billion at the end of 2022–23, equivalent to 86.1% of the UK's gross domestic product (GDP). Interest payments on this debt totalled an estimated £112 billion. The government's debt stock is forecast to continue rising through to 2028–29.

The Treasury is responsible for the government's fiscal and debt management policy, and for delivering the government's overall debt management objective which is "to minimise, over the long term, the costs of meeting the government's financing needs, taking into account risk, while ensuring that debt management policy is consistent with the aims of monetary policy". Ministers make judgements about taxation, spending and the total amount of borrowing required. Government borrows by issuing bonds, known as gilts, through the UK Debt Management Office (DMO) to large investors in the capital markets, or by encouraging savers to invest in National Savings & Investments (NS&I) retail products such as Premium Bonds. In 2023–24, the DMO was tasked with raising £232.3 billion, while NS&I was required to raise £7.5 billion. The Treasury's Debt and Reserves Management (DRM) team is responsible for stress-testing and challenging any analysis the DMO and NS&I provides during the preparation of the annual borrowing requirement known as the "remit". The Office for Budget Responsibility (OBR), which is independent of government, examines and reports on the sustainability of the public finances, in addition to forecasting the government's borrowing needs.

Since 2009, the Bank of England's quantitative easing (QE) programme has acted as a guaranteed buyer of government gilts, purchasing just under £900 billion, thereby indirectly helping the DMO sell the gilts it needed. However, QE is now unwinding, meaning for the first time the DMO will be selling gilts at the same time as the Bank of England. With interest rates having risen to levels not seen since 2008, the government is forecast to make a £126 billion loss on the QE programme, further increasing the government's borrowing needs. These higher interest rates, together with inflation-linked debt, lead to higher debt interest payments for government, which risks eroding government choices for public spending.

Based on a report by the National Audit Office (NAO), the Committee took evidence on 7 December 2023 from HM Treasury, the Debt Management Office, National Savings & Investments, and the Office for Budget Responsibility. The Committee published its report on 5 March 2024. This is the government's response to the Committee's report.

**Relevant reports**

- NAO report: Managing government borrowing – Session 2022-23 (HC 1658)
- PAC report: Managing government borrowing – Session 2023-24 (HC 74)

**Government response to the Committee**

***1. PAC conclusion: The Treasury is not able to fully monitor performance in meeting its debt management objective owing to a lack of quantifiable measures.***

***1. PAC recommendation: The Treasury, together with the DMO and NS&I, should set out, as part of the Treasury Minute response, how they plan to improve performance measurement against the debt management objective, including their analysis of international approaches and possible new metrics that could be introduced.***

1.1 The government agrees with the Committee's recommendation.

**Target implementation date: Spring 2025**

1.2 To better improve performance measurement against the debt management objective, the government will look to examine international best practice and what it can apply from other countries. Alongside this, it plans to thoroughly assess any prospective quantitative and qualitative measures it could consider, and how it can systematically report performance further in the future.

1.3 Currently, the government closely monitors the UK's debt portfolio and reports on it in the annual Debt Management Report (DMR), which was last published in March 2024. A detailed assessment of the costs and risks associated with debt issuance in 2024-25 (including yields and risk premia, demand from investors, and various risks – such as inflation and refinancing risk) is set out in Annex B of this publication.

1.4 The Debt Management Office (DMO) also reports on its performance against its objectives and operational targets in its Annual Report and Accounts, whilst National Savings & Investments (NS&I) report on performance against its Service Delivery Measures (SDMs) in its Annual Reports and Accounts. The Economic Secretary sets targets for SDMs, which are also published annually.

1.5 Making decisions on borrowing involves balancing a range of cost and risk considerations. The International Monetary Fund (IMF) Public Debt Management Network's 2014 Revised Guidelines for Public Debt Management sets out the key features that are essential for optimal debt management, all of which are in the line with the UK's approach.

1.6 Since the National Audit Office (NAO) published its report, the government has developed further its evidence base to assess performance after having welcomed its recommendations. The following analyses have been conducted and published:

- Analysis conducted by the DMO on the value of issuing index-linked gilts over time, demonstrated that, for index-linked gilts that had matured since their introduction in 1981 but prior to August 2023, the government had generated direct savings of around £77 billion in total from the issuance of index-linked gilts if valued at maturity, or £158 billion in 2023 terms.
- HM Treasury (HMT) furthered its analysis of the UK's exposure to refinancing risk (published in the DMR annually), to account for the impacts of quantitative easing (QE). This demonstrated that the average effective maturity of the UK's debt stock remains longer than peers even after accounting for QE (at 11 years), leaving it relatively more insulated from interest rate rises.

1.7 Regarding retail financing, HMT and NS&I routinely use the 'Value Indicator' (VI) in setting NS&I's annual Net Financing target and rates on products, monitoring how it evolves throughout the year. Alongside this, in 2024-25 NS&I will utilise additional measures of cost effectiveness of raising finance to sit alongside the VI. More broadly, NS&I's SDMs include an 'efficient administration of funds ratio' that measures the costs of managing each £100 of funds held. For 2023-24, NS&I is forecasting to achieve the SDM with a figure of 6.8p (beneath a target of 7.2p).

1.8 The challenges around providing a definitive metric to measure performance against a qualitative objective are recognised in the NAO's report and across international issuers. For example, in the US, its quarterly refunding reports concentrates on financing needs and recommended issuance skews but does not attempt to quantify past performance – in a similar vein to the UK's annual DMR. In France, the Agence France Trésor publishes an annual report, which contains qualitative analysis on its performance against the debt management objective over the past year – the form and content of the report is similar in nature to the UK DMO's quarterly reviews.

1.9 Despite these challenges, the government recognises the need to continually review and improve on how it manages the costs and risks associated with debt management. It will therefore seek to continue improving its evidence base in the coming months, including through examining international best practice, and how it can systematically report performance further in the future (as set out fully above).

1.10 The government will write to the Committee when this analysis is concluded.

***2. PAC conclusion: We are concerned that the Treasury, DMO and NS&I will not have the necessary skills, experience, and institutional knowledge needed to overcome the challenges they face now, and in the years to come.***

***2. PAC recommendation: The Treasury should set out, as part of the Treasury Minute response, its overarching plan for building and retaining skills and experience, which should include, but not limited to, the following:***

- ***How NS&I is upskilling its workforce to deliver its Rainbow Programme;***
- ***Details of the DMO's succession planning, in particular an assessment of the merits of a minimum term or equivalent for the new CEO; and***
- ***How the Treasury builds and retains institutional knowledge.***

2.1 The government agrees with the Committee's recommendation.

**Recommendation implemented**

2.2 It is important for HMT, DMO, and NS&I, to have the right skills and resources to execute their duties effectively, given the critical role played in delivering value for money for the taxpayer.

2.3 To support delivery of the transformation programme (formally known as Rainbow), NS&I has plans in place to upskill the organisation by insourcing functional skills in IT and service integration, alongside growth in its commercial and contract management expertise. In the context of a wider Civil Service Headcount cap, NS&I has retained the ability to grow their headcount to support core transformation activity whilst using external contractors and consultants where needed to provide additional short-term support.

2.4 The DMO has a developed resourcing strategy to maintain skills and capacity, and enhance resilience for its operations, including to identify where there is greater potential for the loss of critical skills. It has examined the key person risk for all direct reports of its Executive Committee, considering mitigation measures for each person or skill set, the route to hire suitable skills, and to capture and retain knowledge within the team. The DMO has developed an action plan for both short and longer term by role, and is now expanding knowledge and providing further training across the organisation to help develop specialist skills.

2.5 In December 2023, HMT launched a campaign to recruit a new DMO Chief Executive. HMT announced the successful candidate on 16 April 2024, after undertaking a full and open recruitment. The DMO Chief Executive is a vitally important and high-profile leadership role, which is further reflected in the recent upgrade to Director General, with an increase in the salary. The role has been offered on a permanent basis. HMT launched the campaign with plenty of notice to find the right candidate to take on this critical public role, and to allow for a handover period before the incumbent retires. This approach will ensure a smooth transition in leadership at the DMO, which is now underway.

2.6 The Treasury also places great weight on knowledge management within the department, ensuring policy decisions and key stakeholder engagements are adequately captured and shared over time. The department invests in its people to develop the skills and capabilities required to undertake varied and complex work and to respond flexibly to the evolving needs of the department. Throughout 2023-24 a range of corporate learning and development initiatives were delivered, including for example: People Management workshops and a Policy Leadership Programme, as well as offering a range of external qualifications in policy, economics, tax, and analytics.

2.7 In recognition of some of the key challenges around retention and skills shortage, HM Treasury has recently undertaken a programme of work to de-merge one of its grades, which provides a pay uplift to approximately a third of its largest cohort of staff. This brings the department's grading structure in line with the rest of the Civil Service, which will help to respond to issues it has experienced attracting and retaining staff at this grade.

***3. PAC conclusion: The Treasury and the DMO lack the information needed to better identify unlawful activity and understand the risks posed by overseas investors, potentially reducing the value for money from future gilt sales.***

***3a. PAC recommendation: The Treasury, together with the DMO, should write to us, within two months of the conclusion of the CMA's investigation, outlining what steps they will take to address the information gaps around identifying potentially unlawful activity, including:***

- ***The changes the Treasury will make to its gilt selling process in response to the CMA's investigation;***
- ***Undertaking a formal review of the DMO's gilt selling process to identify any additional changes that could further limit the possibility of collusion, including the information it collects to help monitor unlawful activity; and ….***

3.1 The government agrees with the Committee's recommendation.

**Target implementation date: To be advised**

3.2 As requested, HMT, together with the DMO, will write to the Committee with this information within two months of the conclusion of the Competition and Market Authority's (CMA) investigation. There is currently no statutory deadline for when the CMA will issue a final decision on the case. The government will therefore look to inform the Committee with more information on timing in the future, subject to this being made available by the CMA.

***3b. PAC recommendation: The Treasury should, as part of its Treasury Minute response, set out its assessment of how increasing foreign ownership is affecting the stability of the UK gilt market, and the steps the Treasury and the DMO can take to gain more information on the foreign holders of UK debt.***

3.3 The government agrees with the Committee's recommendation.

**Recommendation implemented**

3.4 Overseas investors play an important role in maintaining the diversity of the gilt investor base, ensuring that underlying demand for UK debt remains strong, changes in gilt supply can be met smoothly, and borrowing costs can be minimised in line with the debt management objective. A diverse investor base ensures that government is not overly reliant on any one type of investor.

3.5 Overseas investors include a range of different types of investors, who each have different incentives to buy and trade gilts. This includes foreign central banks, where the role of sterling as a reserve currency has increased. It also includes funds which may originate from the UK but are domiciled abroad. It is therefore not the case that appetite for gilts from all overseas investors will be perfectly correlated or that they are all inherently riskier than domestic investors.

3.6 The gilt market is a large and liquid market with an independent rate setting body. There is no reason to believe that global investors' strategic allocation will change while the underlying instruments continue to represent diversification and meet liquidity requirements.

3.7 While UK gilts are registered instruments, they are mostly held in nominee accounts, with intermediaries passing on any gilt principal or coupon payments to the underlying beneficial holder who may be domiciled elsewhere. The government currently has no visibility of the underlying beneficial owners of gilts.

3.8 This data limitation is not uncommon across jurisdictions; however, the department will review the sovereign bond ownership data available to other countries to consider if there is anything it can learn from their approaches.

***4. PAC conclusion: We are concerned that significant problems with NS&I's procurement of its Rainbow Programme could leave limited flexibility or room for further delays.***

***4. PAC recommendation: NS&I should set out, as part of its Treasury Minute response, the following:***

- ***A list of the key project milestone between now and the Rainbow Programme launch date (thereafter NS&I should provide 6 monthly progress updates against these milestones);***
- ***The expected costs of extending the Atos contract beyond March 2025 and the contingency plans should Atos not wish to extend contract; and***
- ***Details on how it will avoid further delays to Rainbow Programme.***

4.1 The government agrees with the Committee's recommendation.

**Recommendation implemented**

4.2 Developing a transition plan is a complex process reflecting the technical and cultural complexity of changing a structure that has been in place for 25 years. This involves NS&I balancing a range of factors, some of which stem from the historical structure of NS&I. Others relate to commercially sensitive matters (relating to providers) that add complexity to the development of the integrated plan.

4.3 NS&I is currently working with Atos, NS&I's incumbent provider and preferred bidder for its core banking system, along with IBM and Sopra Steria, as the providers of its new service packages, to formulate an integrated transition plan. The plan will provide key project milestones (e.g. the launch of a transactional customer mobile app), ensuring that the transition is orderly and does not disrupt services to customers.

4.4 NS&I will share this integrated transition plan with the Committee when it is finalised. As requested by the Committee, NS&I will also share updated plans on a six-monthly basis.

4.5 Transforming NS&I is a £2.2 billion programme. As set out in evidence to the Committee, an additional 12 months of termination assistance services was agreed with Atos to March 2025, the cost of which is encompassed in the total cost of the programme. The contract enables NS&I to utilise this provision for a further 12 months beyond March 2025 if needed. Commercial terms, which would then determine the subsequent costs, would be agreed at point of extension with Atos. Should Atos not agree to extend, NS&I would seek to ensure an orderly transition to a new supplier in a manner that does not disrupt services to customers. There are a range of approaches NS&I could take, all of which at this time are commercially sensitive.

4.6 NS&I's programme governance has been audited and assured by the Government Internal Audit Agency (GIAA) over the last year. A representative from GIAA's Project and Programme Management Assurance practice and a representative of the Infrastructure and Projects Authority are standing attendees at the Transformation Programme Board. NS&I is also in the process of adding a member of the executive team of another government department to the programme board to provide additional insights and experience from another public body. It is also working with the Cabinet Office's complex transaction team to provide additional expert support.

***5. PAC conclusion: We are not convinced that the Treasury, DMO and NS&I have adequately captured the lessons learned during the financial crisis and pandemic to prepare them to deal with the challenges to come.***

***5. PAC recommendation: The Treasury, DMO and NS&I should set out, as part of the Treasury Minute response, the lessons they have identified and learned from the financial crisis and pandemic, including the process whereby these lessons are captured and the changes that have been made to the borrowing process because of these lessons.***

5.1 The government agrees with the Committee's recommendation.

**Recommendation implemented**

5.2 Previous crisis episodes placed extraordinary demands on the government and capturing lessons learned have helped to improve its preparedness.

5.3 Following the Review of HM Treasury's management response to the financial crisis, the Professionalising Crisis Management project was established to ensure the department is ready to effectively respond to future financial stability events. It has expanded considerably since, and the department has developed a suite of manuals and resources to support the deployment of tools in crises.

5.4 More recently, the COVID-19 pandemic posed an unprecedented challenge that required the government to revise its financing requirement outside of the normal cycle. As discussed in the government's response to recommendation 4b of the Committee's Ninth Report of Session 2023-24, HMT remains committed to learning and sharing lessons from the response to the pandemic. In respect to borrowing, HMT has since agreed with the Office for Budget Responsibility (OBR) that it will consult the OBR on any future out-of-cycle internal fiscal projections (that, for example, might be used to inform a DMO financing update). In light of market challenges at the time, there was also an increase in the planned DMO end-financial year net cash position, to provide additional day-to-day liquidity.

5.5 Generally, setting the DMO's remit each year involves taking into account the market's feedback to design a programme that best meets the debt management objective. This serves as an annual lessons learned process, which remained robust during the pandemic.

5.6 NS&I's funding target was also increased materially at the time. NS&I met this by maintaining high rates on easy access variable products, which led to very high demand for their products and services. When these rates fell, customers moved quickly to withdraw funds creating further operational pressures, which, regrettably, negatively impacted customers experiences and public trust in NS&I.

5.7 The operational pressures from both high inflows and subsequent outflows were exacerbated by NS&I's older systems. NS&I's transformation programme will deliver the systems scalability needed to meet sudden spikes in demand and the robustness customer 'journeys' that enable customers to complete these online without further support.