National Loans Fund Account 2017-18

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CONTENTS

Performance Report

Overview

Purpose and activities of the National Loans Fund

The National Loans Fund (NLF) was established on 1 April 1968 by the National Loans Act 1968 to account for government borrowing and lending which were until then accounted for as part of the Consolidated Fund (CF). The CF was first set up in 1787 as 'one fund into which shall flow every stream of public revenue and from which shall come the supply for every service'. The NLF was set up in order to separate government revenue and expenditure on the one hand and government borrowing and lending on the other. The accounts for the CF and NLF are now published separately.

Both the CF and NLF are administered by the Treasury with the bank accounts maintained at the Bank of England. The CF can therefore be regarded as central government's current account whereas the NLF can be regarded as central government's main borrowing and lending account. Most of the NLF's borrowing needs are now met indirectly through borrowing on its behalf by the Debt Management Office (DMO) and National Savings and Investments (NS&I).

The DMO was established as an executive agency of the Treasury on 1 April 1998. Its remit is 'to carry out the Government's debt management policy of minimising financing costs over the long term, taking account of risk, and to minimise the cost of offsetting the Government's net cash flows over time, while operating in a risk appetite approved by Ministers in both cases'. Its operations are managed through the Debt Management Account (DMA) which is a bank account at the Bank of England linked closely with the NLF. As the Government's debt manager, the DMO has a key role in the issue of gilt-edged securities on behalf of the Treasury. Gilt-edged securities, or gilts, are UK Government sterling-denominated listed bonds. There are two main types: conventional (i.e. fixed rate) gilts and index-linked gilts on which the return is linked to movements in the Retail Prices Index (RPI). They are issued from the NLF and sold into the market by the DMO. In addition, the DMO issues Treasury Bills from the DMA and undertakes other money market operations to meet the Government's daily cash requirements. Further details on these operations can be found in the Debt management report 2018-19[1] published by the Treasury in March 2018.

The Exchange Equalisation Account (EEA) was established in 1932 to provide a fund that could be used when necessary to regulate the exchange value of sterling. It holds the UK's reserves of gold, foreign currency assets and International Monetary Fund (IMF) Special Drawing Rights. Combined with the UK's Reserve Tranche Position (RTP) with the IMF, these assets comprise the UK's official holdings of international reserves. The RTP is an asset of the NLF. The Bank of England acts as the Treasury's agent in the day-to-day management of the EEA.

The NLF's main role is to meet the finance needs of the CF to the extent that taxation and other receipts are insufficient to meet the CF's outgoings. To this end the NLF undertakes borrowing and uses the proceeds to meet any deficits on the CF; conversely, any net surpluses on the CF are passed to the NLF to reduce the latter's need to borrow or to increase the amount that it can lend. The NLF finishes every day with a nil balance on its bank account because any cash surpluses or deficits are offset by transfers to or from the DMA.

The NLF's borrowing operations include the temporary borrowing of balances in various government bank accounts that are surplus to immediate requirements. Such borrowing minimises the amount that the NLF needs to borrow from other sources. Where the money borrowed in this way already counts as Exchequer money, interest is not paid. For the rest of its borrowing however the NLF normally has to pay interest. If the NLF's interest income is less than the interest it pays on its borrowings, which it generally is, the shortfall is met by a transfer from the CF.

The NLF provides finance for both the DMA and EEA so surpluses and deficits of the DMA and EEA are income and expenditure of the NLF and their net assets are assets of the NLF. It also makes loans to various statutory

[1] https://www.gov.uk/government/publications/debt-management-report-2018-to-2019

public sector bodies and provides the finance needed by the Public Works Loan Board (PWLB) for its loans to prescribed bodies, mainly local authorities. The profits of the Issue Department of the Bank of England are also paid to the NLF under section 9(1) of the National Loans Act 1968. The Issue Department is solely concerned with the issue of banknotes and the assets backing them. NS&I's savings products are liabilities of the NLF.

As the vast majority of the assets of the NLF comprise the advances to and net assets of the DMA and EEA and advances to the PWLB, the NLF is not exposed to significant credit risk. Further detail on how credit risk is managed is included in note 15 to the accounts. By virtue of section 19(1) of the National Loans Act 1968, the net liabilities of the NLF are a liability of the CF. The servicing of the NLF's liabilities is expected to be mainly met through future tax revenue receipts. There is no reason to believe that tax revenues will not be forthcoming and therefore, in accordance with the Government Financial Reporting Manual, it has been concluded as appropriate to adopt the going concern basis of preparation for the NLF Accounts.

Key issues and risks

The key issues and risks facing the NLF are considered in the governance statement on pages 9 to 13. In addition, the financial risks related to the NLF are separately disclosed in note 15 on page 34 to 40.

Performance summary

The total comprehensive net expenditure of the NLF increased by £20.9 billion from £33.7 billion in 2016-17 to £54.6 billion in 2017-18 primarily due a decrease in Other income of £13.5 billion from £14.2 billion in 2016-17 to £0.7 billion in 2017-18, an increase in Financing costs of borrowing of £5.3 billion from £51.5 billion in 2016-17 to £56.8 billion in 2017-18 and an increase in Other expenditure of £1.3 billion from £0.2 billion in 2016-17 to £1.5 billion in 2017-18.

The NLF's total gross assets decreased by £36.2 billion from £344.3 billion in 2016-17 to £308.1 billion in 2017-18. Total gross liabilities increased by £19.7 billion from £1,888.0 billion in 2016-17 to £1,907.7 billion in 2017-18. As a result, net liabilities increased by £55.9 billion from £1,543.7 billion in 2016-17 to £1,599.6 billion in 2017-18. Further details can be found in the Performance analysis.

Performance analysis

International Support

The UK has continued to support the International Monetary Fund (IMF) through the NLF in 2017-18 in line with our commitments as an IMF member. The UK has provided such support through its quota subscription and other lending to the Fund. The IMF's 14th General Quota Review, which involved a package of reforms of the Fund's governance and quota, became effective on 26 January 2016. As part of this reform package the UK's quota increased to SDR 20.2bn (£20.8bn). The UK's 2012 bilateral loan agreement (BLA) to the IMF worth SDR 9,178.0 million (£9,488 million) also became effective when the UK's quota was increased and the size of the UK's commitment under the New Arrangements to Borrow (NAB) was reduced by the amount of the BLA to SDR 9,479.0 million (£9,799 million). The 2012 BLA expired without being used at the end of 2016. The UK agreed to a third bilateral loan facility (2016 bilateral loan) to the IMF again worth SDR 9,178.0 (£9,488 million) in October 2016. The NLF's net exposure to the IMF of £4.1 billion at 31 March 2018 (2016-17: £5.3 billion) is described in note 9 and comprises the reserve tranche position of £3.1 billion (2016-17: £4.0 billion) and loans of £1.0 billion (2016-17: £1.3 billion). The IMF maintains precautionary balances of retained earnings to absorb any losses it may incur. As at 31 March 2018, any losses that may be incurred by the IMF on loans to its member countries are not expected to result in losses to the NLF.

The UK's bilateral loan facility to Ireland has been funded by HM Treasury's Vote which is funded through the normal Supply procedures. Details can be found on the GOV.UK website[2]. The UK has a contingent liability in respect of European Union (EU) mechanisms that provide financial assistance to EU Member States and Third Countries including loans from the European Financial Stabilisation Mechanism, European Balance of Payments Facility, Macro Financial Assistance and the European Investment Bank. The CF is responsible for this contingent liability and details can be found in the Consolidated Fund Account 2017-18. The NLF is not party to either the bilateral loan to Ireland or the EU financial assistance arrangements.

Asset Purchase Facility

The Asset Purchase Facility was set up in 2008-09 at the Bank of England and is authorised to purchase assets financed by the issuance of central bank reserves (a process known as 'quantitative easing'). As at 31 March 2018, on an amortised cost basis, £380.6 billion (2016-17: £387.8 billion) of gilts from the NLF were held by the Bank of England for quantitative easing. Excess cash held in the facility, which arises largely from coupons on these gilts, is transferred to the Exchequer via HM Treasury from where it is paid to the CF as Extra Receipts. More information on the scheme can be found on the Bank of England's website[3].

Funding for Lending Scheme (FLS)

The FLS is designed to incentivise banks and building societies to boost their lending to the UK real economy. It was launched in July 2012 and subsequently extended to allow participants to borrow from the FLS until January 2018. The NLF issues Treasury Bills for sale to the DMA which makes them available to be borrowed by the Bank of England. Banks and building societies participating in the FLS can then borrow Treasury Bills from the Bank of England in exchange for eligible collateral. As at 31 March 2018, on an amortised cost basis, £39.2 billion (2016-17: £75.1 billion) of Treasury Bills issued to the DMA by the NLF for the FLS are outstanding. More information can be found on the Bank of England's website[4].

Outturn for 2017-18

The total comprehensive net expenditure of the NLF increased by £20.9 billion from £33.7 billion in 2016-17 to £54.6 billion in 2017-18 primarily due a decrease in Other income of £13.5 billion from £14.2 billion in 2016-17 to £0.7 billion in 2017-18, an increase in Financing costs of borrowing of £5.3 billion from £51.5 billion in 2016-17 to £56.8 billion in 2017-18 and increase in Other expenditure of £1.3 billion from £0.2 billion in 2016-17 to £1.5 billion in 2017-18.

[2] https://www.gov.uk/government/publications/bilateral-loan-to-ireland
[3] http://www.bankofengland.co.uk/markets/Pages/apf/default.aspx
[4] http://www.bankofengland.co.uk/markets/pages/fls/default.aspx

The decrease in Other income and increase in Other expenditure are mainly due to £9.6 billion reduction in DMA's total comprehensive income, a gain of £0.5 billion in the current year compared to a gain of £10.1 billion in 2016-17 and £5.0 billion change in EEA's total comprehensive income/expenditure, a loss of £1.3 billion in the current year compared to gain of £3.7 billion in 2016-17 while the increase in Financing costs of borrowing was mainly as a result of £5.3 billion higher financing costs of gilts.

The total comprehensive net income from the DMA was £0.5 billion in 2017-18 and is reported against Other income in the Statement of Comprehensive Net Expenditure; this compares to net income of £10.1 billion in 2016-17 (reported against Other income). The £9.6 billion difference is primarily due to £3.8 billion loss on the fair value of DMA gilt holdings compared to a gain of £5.8 billion in 2016-17. The total comprehensive net expenditure to the EEA was £1.3 billion in 2017-18 (reported against Other expenditure) compared to a net income of £3.7 billion in 2016-17 (reported against Other income). The £5.0 billion difference was largely due to £3.1 billion decrease in net trading income and £1.9 billion decreased fair value changes in gold as a result of a decrease in the price of gold during 2017-18. Further information on the DMA and EEA can be found in their respective accounts which are published separately.

Excluding the profits and total comprehensive net income/expenditure of other entities, the NLF's total comprehensive net expenditure was £6.2 billion higher at £53.9 billion in 2017-18 compared to £47.7 billion in 2016-17, primarily as a result of higher financing costs of gilts:

	Note	**2017-18 £m**	2016-17 £m
Total comprehensive net expenditure		**54,595**	33,674
Removal of EEA total comprehensive net (expenditure) / income	5	**(1,338)**	3,649
Removal of DMA total comprehensive net income	5	**473**	10,154
Removal of Profits of the Bank of England Issue Department	5	**196**	241
		53,926	47,718

Assets

The NLF's total gross assets decreased by £36.2 billion from £344.3 billion in 2016-17 to £308.1 billion in 2017-18. This was primarily due to decreases in advances of £34.9 billion (consisting of a decrease in advance to the DMA of £45.0 billion, an increase in advance to the EEA of £6.3 billion and an increase in advance to the PWLB of £3.8 billion) and a decrease in the IMF Quota Subscription & Lending of £1.3 billion (consisting of a £1.1 billion exchange rate losses relating to the Quota subscription and a decrease of £0.2 billion on net IMF Lending including related exchange rate losses).

Liabilities

Total gross liabilities increased by £19.7 billion from £1,888.0 billion in 2016-17 to £1,907.7 billion in 2017-18. This is largely a result of gilt-edged stock increasing by £30.2 billion from £1,602.8 billion to £1,633.0 billion, liabilities to other public sector increasing by £15.8 billion from £45.2 billion to £61.0 billion and NS&I liabilities increasing by £9.8 billion from £146.9 billion in 2016-17 to £156.7 billion in 2017-18 (reflecting significant inflows from Premium bonds and Guaranteed Bonds) partly offset by Treasury Bill issuance for the Funding for Lending scheme decreasing by £35.9 billion from £75.1 billion to £39.2 billion.

Public Sector Net Debt

As a result of these changes, the net liabilities of the Fund increased by £55.9 billion from £1,543.7 billion to £1,599.6 billion. This is matched by a corresponding claim on the CF. The NLF lends to and borrows from other parts of the public sector. For example, it makes advances to the PWLB and borrows directly from a range of public sector bodies (as described in note 12). In addition, some of the gilts it has issued are held in the public sector, including by the DMA which retains a portfolio of gilts for use as collateral for its money market activities and by the Bank of England under the Asset Purchase Facility. The DMA also has large advances to and from the NLF. Therefore, the NLF's net liabilities do not equate to the Public Sector Net Debt ("PSND"), which is a calculation of the net debt of the whole of the public sector after eliminating intra-public sector balances. Figures for PSND are published jointly by HM Treasury and the Office for National Statistics in the monthly *Public Sector Finances Statistical Bulletin* which can be found on the Office for National Statistics and GOV.UK websites.

Forward Look

Net financing requirement

The Debt management report which included the financing remit for 2018-19 was published by the Treasury with the Spring Statement in March 2018 and subsequently revised following publication of the 2017-18 Central Government Net Cash Requirement (CGNCR) Outturn: Revision to the DMO's Financing Remit 2018-19[5]. On the basis of a CGNCR forecast for 2018-19 of £40.6 billion (excluding NRAM plc, Bradford and Bingley and Network Rail), the revised Net Financing Requirement to be met by the DMO is £106.0 billion (following upward adjustments including £66.7 billion for gilt redemptions and planned financing for the reserves of £6 billion and downward adjustments including £6 billion for the net contribution from National Savings & Investments). The DMO will meet this requirement by gross gilt sales of £106.0 billion (gilts issued by the NLF).

PWLB

Following a review of the role of the Public Works Loan Commissioners, the Infrastructure Act 2015 introduced a provision to enable HM Government to abolish the PWLB using the Public Bodies Act 2011. In May 2016, a consultation was launched on the transfer of functions from the PWLB to another entity. The results of this consultation were published in November 2016, concluding that the PWLB should be abolished and its powers transferred to HM Treasury. The reforms only affect the governance arrangements and do not change any of the policy or operational aspects of lending to local authorities, the existing lending or loan repayment arrangements for borrowers or the arrangements with the NLF. The government is exploring the ways it can deliver the reform given the current constraints within the legislative process.

Section 4 (1) of the National Loans Act 1968 limits the aggregate amount that may be outstanding in respect of commitments entered into by the Public Works Loan Commissioners. Section 300 of the Finance Act 2014 came into force on 1 December 2017 and replaced the limits of £55 billion and £70 billion in Section 4(1) of the 1968 Act with new limits of £85 billion and £95 billion respectively. It also revoked the Local Loans (Increase of Limit) Order 2008.

Long-term expenditure trends

Since the function of the NLF is to account for government borrowing and lending, it has no long-term expenditure trends.

Tom Scholar
Accounting Officer
HM Treasury

10 July 2018

[5] https://www.dmo.gov.uk/media/15447/sa240418.pdf

Accountability Report

The accountability report contains a Corporate governance report and a Parliamentary accountability and audit report. The purpose of the corporate governance report is to explain the composition and organisation of the National Loans Fund's governance structures and how they support the achievement of the National Loans Fund's objectives. It includes the Statement of Accounting Officer's responsibilities and the Governance statement. The Parliamentary accountability and audit report includes key Parliamentary accountability information on regularity of expenditure and remote contingent liabilities as well as the Certificate and Report of the Comptroller and Auditor General to the House of Commons.

Corporate governance report

Directors' report

Operationally, the NLF is part of HM Treasury and its staff are employees of HM Treasury. The NLF itself therefore has no employees of its own.

Directors' conflicts of interest

In 2017-2018, no material conflicts of interest have been noted by the senior management overseeing the NLF.

Personal data related incidents

The NLF does not hold any protected personal data.

Statement of Accounting Officer's responsibilities

Under section 21(1) of the National Loans Act 1968 HM Treasury is required to prepare an account relating to the National Loans Fund for each financial year in the form and on the basis considered appropriate by the Treasury. The Account is prepared on an accruals basis and must give a true and fair view of the state of affairs of the Fund and of its Comprehensive Net Expenditure and cash flows for the financial year.

In preparing the Account the Accounting Officer is required to:

- observe the relevant accounting and disclosure requirements of the Government Financial Reporting Manual in so far as they are relevant to the Account and apply suitable accounting policies on a consistent basis;
- make judgements and estimates on a reasonable basis; and
- prepare the accounts on a going concern basis as defined in the Government Financial Reporting Manual.

The Treasury has appointed its Permanent Secretary, Tom Scholar, as Accounting Officer of the National Loans Fund.

The responsibilities of an Accounting Officer, including responsibility for the propriety and regularity of the public finances for which the Accounting Officer is answerable and for keeping proper records, are set out in Managing Public Money published by the Treasury.

The Accounting Officer confirms that, as far as he is aware, there is no relevant audit information of which the NLF's auditors are unaware, and that he has taken all the steps that he ought to have taken as Accounting Officer to make himself aware of any relevant audit information and to establish that the NLF's auditors are aware of that information.

The Accounting Officer confirms that the annual report and accounts as a whole is fair, balanced and understandable and that he takes personal responsibility for the annual report and accounts and the judgments required for determining that it is fair, balanced and understandable.

Audit arrangements

The NLF accounts are audited by the Comptroller and Auditor General (C&AG) under the requirements of the National Loans Act 1968. The National Audit Office (NAO) bears the cost of all external audit work performed on the NLF. No non-audit work was undertaken by the NAO in relation to the NLF in 2017-18.

Governance Statement

1. Governance Framework

1.1 The NLF is managed within the Treasury's overall risk and governance framework as set out in the Treasury's Annual Report and Accounts 2017-18. This includes the Treasury Board's assessment of its compliance with the *Corporate Governance Code for Central Government Departments*.

1.2 The Chancellor of the Exchequer, as Minister in charge of the Treasury, is responsible and answerable to Parliament on all the policies, decisions and actions of the Treasury, and ultimately of the NLF.

1.3 As Accounting Officer for the NLF, I am personally responsible and accountable to Parliament for the organisation and quality of management of the NLF, including its use of public money and the stewardship of its assets, in line with those responsibilities assigned to me in *Managing Public Money*.

Audit and Risk Committee

1.4 The Treasury Group Audit and Risk Committee is a subcommittee of the Treasury Board, and is tasked with supporting me in my role as Principal Accounting Officer, and the Treasury's Additional Accounting Officers in their responsibilities for managing risk, internal control and governance related to the Treasury Group's Annual Report and Accounts, the Central Funds (Consolidated Fund, National Loans Fund, Contingencies Fund and Exchange Equalisation Account) and the Whole of Government Accounts. Details on the overall risk and governance structure of HM Treasury can be found in the Governance Statement in the Treasury's Annual Report and Accounts.

1.5 I appoint members of the Audit and Risk Committee for periods up to three years, extendable by one additional three-year period. The Chair of the Audit and Risk Committee (Richard Meddings) reports directly to me and is also a non-executive Member of the Treasury Board. The membership of the Audit and Risk Committee at the close of 2017-18 was:

- Richard Meddings (reappointed 1 July 2017 for a second term) – Non-executive Director TSB (September 2017 - present) and Chairman from 1 February 2018; Non-executive Director, Deutsche Bank AG (October 2015 - present); Non-executive Director JLT plc (September 2017 - present); Non-executive Director Teach First (February 2016 - present); Financial Reporting Review Panel in FRC (2008 - 2018); Board member of International Chambers of Commerce UK (2007 - present); Non-executive Director, Legal & General plc (December 2014 to May 2017); Non-executive Director and Senior Independent Director of 3i Group plc (2008-2014) and chair of Audit and Risk Committee; Main Board Director (2002-2014) and Group Finance Director (2006–2014) Standard Chartered plc.

- Tim Score - Member of the Board of Trustees of Royal National Theatre; Chair of the Audit Committee of the Football Association; Non-executive director and Chair of Audit Committee at Pearson plc; Non-executive director and Chair of Audit Committee at The British Land Company plc; Chief Financial Officer of ARM Holdings plc (2002 to 2015); Senior independent director, Chair of Audit and Interim Chairman at National Express Group (2005 to 2014); CFO of Rebus Group and William Baird plc; Group Financial Controller at BTR plc and LucasVarity plc.

- Peter Estlin - Alderman, City of London; Senior Advisor, Barclays plc, (previously Group Financial Controller and acting Group CFO); Governor, Bridewell Royal Hospital; Board Member, Trust for London; Trustee, Morden College.

- Zarin Patel – formerly Chief Operating Officer of The Grass Roots plc; previously Chief Financial Officer at the BBC and a member of its Executive Board; Non-Executive Director of John Lewis Partnership and member of its Audit and Risk Committee.

- Jacinda Humphry - Director of Government Finance Transformation – central finance function; previously Finance Director, Department for Communities and Local Government (now Ministry of Housing, Communities and Local Government).

1.6 The Audit and Risk Committee met five times during 2017-18, taking the opportunity for pre-committee discussions with the National Audit Office (NAO) on each occasion. Attendance is outlined in the table below:

	Eligible to attend	**Attended**
Richard Meddings (Chair)	5	5
Tim Score	5	4
Peter Estlin	5	5
Zarin Patel	5	5
Jacinda Humphry	5	2

1.7 The Audit and Risk Committee has a robust Conflicts of Interest Policy, which requires members to excuse themselves from discussions where potential conflicts may occur. Members are required to inform me about any potential conflicts and highlight these at the start of each meeting as appropriate.

1.8 In addition to the independent members, the appropriate Accounting Officers, HM Treasury's Group Director of Finance and the Treasury Accountant (or, in her absence, the Head of Exchequer Accounts or Exchequer Accounts Manager) also attend Audit and Risk Committee meetings. Members have the opportunity for a pre-committee discussion with the NAO, Group Head of Internal Audit for HM Treasury and Head of Exchequer Funds Internal Audit (EFIA).

1.9 Over the course of the year, as well as scrutinising the Treasury's financial management and balance sheet risks, the Audit and Risk Committee considered a wide range of issues relating to the department's framework of governance, risk management and control. The Audit and Risk Committee challenged and approved the Internal Audit work programme throughout the year and followed up on management action to address audit recommendations.

1.10 Outside the planned Audit and Risk Committee meetings individual members have shared their commercial and professional expertise with key officials across the Treasury.

1.11 The external auditor is the Comptroller and Auditor General and the NAO attend all Audit and Risk Committee meetings on his behalf.

1.12 The Audit and Risk Committee receives all NAO reports and a summary of EFIA reports relating to the NLF plus underlying reports on internal audits where issues are identified leading to Red or Amber assessments (no such report in 2017-18 and one such report in 2016-17).

Exchequer Funds Internal Audit (EFIA)

1.13 Internal Audit for the NLF is provided by EFIA which reports directly to both me and the Audit and Risk Committee on audit reporting matters.

1.14 For the NLF, an annual risk-based internal audit programme is agreed with the Treasury Accountant (or, in her absence, one of her managers) in advance of the Audit and Risk Committee's approval. The work programme always includes a review of the receipts and payments process, due to the very high value of payments made by the NLF. The Audit and Risk Committee reviews the work programme and is kept informed of progress and amendments.

Management of the National Loans Fund

1.15 The NLF is managed by the Treasury Accountant and her managers within the Exchequer Funds and Accounts (EFA) Team of HM Treasury. The EFA team reports any matters concerning the NLF directly to me.

2. Risk management

Treasury Risk management and reporting to the Treasury's Boards

2.1 The department has a sound system in place to consider the risks faced by the Treasury, challenge the assumptions made about these risks and, where appropriate, offer advice on how best to mitigate risk.

2.2 A newly formed Operating Committee (OpCo) was established this year as a sub-committee of the Executive Management Board (EMB) to oversee the financial, planning, operational and risk management issues of the Treasury including responsibility for identifying, assessing and reporting against operational risks. OpCo meets monthly and is chaired by the Second Permanent Secretary.

2.3 To strengthen the Treasury's governance and oversight across the Treasury, the department introduced a new risk management framework which covers, amongst other areas, the National Loans Fund. The process seeks to improve the effective identification, assessment and management of operational risks, ensuring that they can be escalated as appropriate. The framework was formally introduced in November 2017 following consideration by OpCo and the Audit and Risk Committee. On a quarterly basis, a risk summary for the National Loans Fund together with information on its governance arrangements is submitted to a central Treasury team. The risk summary looks at the likelihood, probable impact and potential mitigation of risks to delivery of objectives. The central Treasury team collate the various returns received and present their analysis to OpCo. This analysis is also fed into a Quarterly Performance and Risks report which includes a range of risks, not just operational. This report is discussed by EMB and the Treasury Board Sub-committee on a quarterly basis.

2.4 EFA also feeds a summary of key risks into a separate Quarterly Performance and Risks report return which is then discussed by EMB and the Treasury Board Sub-committee on a quarterly basis. This covers broader areas such as Cyber Risk across the entirety of EFA's operations. This enables EMB, Treasury Board Sub-committee and senior managers to take action where appropriate.

2.5 The Chair of the Audit and Risk Committee is invited to report concerns or issues to the Treasury Board (Sub-committee), and is a non-executive member of the Treasury Board.

National Loans Fund Risk management

2.6 EFA is managed within the Treasury's risk management framework as set out in the Treasury's Annual Report and Accounts. The Treasury Accountant and her managers have overall responsibility on a day-to-day basis for risk management of those Funds managed by EFA, and for ensuring that my financial, regularity and propriety responsibilities as Accounting Officer of the NLF are discharged appropriately. She is supported by members of EFA management who are responsible for ensuring that the tasks in their areas are compliant with operational policies and procedures, and legislation. EFA management provide me with a quarterly update report on changes to the control environment and changes in risk exposure.

2.7 Risk management is key to all processes within EFA, including business continuity resilience planning for those public funds for which EFA is responsible. Business continuity resilience is regularly tested locally and with business partners, and lessons learned feed into improved business continuity processes. The risk management strategy includes periodic horizon scanning to identify any changes in risk exposure, to evaluate the change and to identify appropriate mitigating actions. Significant risk issues are recorded in a risk register and are assessed by likelihood and impact. A risk owner, who is responsible for managing the risk, is assigned to each risk. The risk register is reviewed quarterly by EFA management, and is circulated to me alongside the quarterly risks and controls report.

2.8 There are sufficient experienced staff in the EFA team with an appropriate range and breadth of knowledge to manage the NLF, covering absences as necessary and maintaining resilience. EFA management ensures that staff members working on the NLF are trained and equipped to manage risk in a way appropriate to their authority and duties. Training on risk awareness and management is provided as required, either by management or by attending appropriate courses. Training is also provided to staff to build the team's capability and to increase its resilience. EFA team members are encouraged to obtain professional qualifications in areas that are relevant to their roles.

3. The system of internal control

3.1 As Accounting Officer, I am responsible for maintaining a sound system of internal control that supports the achievement of the NLF's policies, aims and objectives, whilst safeguarding the public funds and assets, for which I am personally responsible, in accordance with the responsibilities assigned to me in Managing Public Money.

3.2 The system of internal control is designed to manage risk to an acceptable level, balancing the impact of potential risks with the resources required to manage them, rather than eliminate all risk. It can therefore only provide reasonable and not absolute assurance of effectiveness. The system of internal control is based on an ongoing process designed to identify and prioritise the risks to the achievement of the NLF's policies, aims, and objectives; to evaluate the likelihood of those risks being realised and the impact should they be realised; and to manage them efficiently, effectively and economically.

3.3 The system of internal control has been in place throughout the year ended 31 March 2018 and up to the date of approval of the financial statements, and accords with Treasury guidance. During the year, there were no significant changes to the control environment.

4. Risk profile

4.1 The NLF is managed generally within the framework of the Treasury's system of internal control. This framework includes resourcing the administration of the NLF, security and the management of risks across the Treasury's business.

4.2 The key risks in managing the NLF and their associated controls are:

- **Irregularity of transactions, including fraudulent or erroneous payments:** Clear separation of duties is enforced by appropriate user permissions within the accounting system and payment approval panels. Up-to-date policy and procedures manuals including job instructions are readily accessible to all operational staff. Payment instructions are computer-generated and are derived from underlying transaction records. This minimises the risk of keying errors. Separately, the Comptroller and Auditor General, through the NAO Exchequer Section approves NLF payments in advance and reconciles NLF transactions on a daily basis. There is also a clear and comprehensive audit trail in the IT system, to which the NAO Exchequer Section has real-time access.

- **Incorrect accounting:** Application controls exist within the IT system used to manage financial transactions and account for receipts and payments on the NLF. Interest and amortisation are generated automatically by the accounting system at month end using pre-defined rules. New general ledger accounts are authorised by the Treasury Accountant or one of her managers before being set up. Gilts issuances are reported to senior management and key operational staff. EFA reconciles the dividend claims received from the gilts registrar with its own records prior to each interest payment. The Debt Management Office reconciles principal amounts twice a year. Monthly management accounts for the NLF are also produced and reviewed by the Treasury Accountant or the Head of Exchequer Accounts, and are provided to me. The accounting for any unusual transactions is suitably considered.

- **Failure of IT systems:** The Nippon Telegraph and Telephone Corporation (NTT) data centre offers high levels of resilience with the data centre platform availability set to 99.9% and the network connectivity availability set to 99.99%. NTT has dual centres which provides a high level of resilience. As part of disaster recovery measures, there is an Active/Active configuration across the two data centres, which ensures a superior level of availability across both sites with near instant failover. EFA also has its own contingency plans in place.

- **Failure to provide an effective service in adverse circumstances, including disaster situations:** To ensure operational resilience in key areas in the event of a threat to business continuity, staff within EFA are trained to provide cover for times when other staff members are absent. Measures are in place to facilitate the NAO Exchequer Section's normal payments approval process in the event of disruption to enable the essential payments business to continue. The risks that impact upon EFA's key stakeholders are managed by their involvement in business continuity planning and testing. Business continuity arrangements are regularly reviewed and tested within the framework of the Treasury's corporate Business Continuity Plan facilities.

- **Failure of principal counterparties to provide agreed services:** Well-developed Service Level Agreements (SLAs) for the provision of services from all principal counterparties are in place. They cover details of the monitoring and control arrangements that both parties are expected to observe. Bi-annual meetings are held with managers at the Bank of England where service levels are discussed. A monthly report of any failure to meet the service requirements is also sent to the Bank of England by EFA. A monthly meeting is held with Government Banking management where service levels are discussed.

- **Information risk:** Data and information risk are managed in accordance with the Treasury's policies, which involve a range of controls to prevent unauthorised disclosures. These include encryption and physical and IT security. HM Treasury adheres to Cabinet Office guidelines available at https://www.gov.uk/government/publications/security-policy-framework. Further guidance on information security and assurance is available to all Treasury staff on the intranet. EFA's own Data Handling Policy identifies risks specific to EFA. This policy is reviewed as required.

- **Financial risk:** Adverse results of the Debt Management Account and the Exchange Equalisation Account will affect the NLF's results; therefore all financial risks inherent in these accounts are also inherent in the NLF. Responsibility for risk management and the system of internal control is clearly delegated to the Accounting Officers of those accounts, which have their own control frameworks in place.

5. Review of effectiveness

5.1 In line with HM Government guidance, set out within the Corporate Governance Code of Good Practice for central government departments, I have reviewed the effectiveness of the system of internal control. My review is informed by the work of EFIA who provided positive assurance as to the management and control of the NLF in 2017-18, and the executive managers within EFA who have responsibility for the development and maintenance of the internal control framework, as well as comments made by external auditors in their management letter and other reports. I have been supported by the Treasury Group Audit and Risk Committee, and risk owners in addressing weaknesses and ensuring continuous improvement of the system is in place. Information about the effectiveness of the Treasury's overall system of governance including board effectiveness, attendance, compliance with the Corporate Governance Code and quality of management information reviewed, is reported in the Treasury's Annual Report and Accounts.

5.2 The Audit and Risk Committee considered the 2017-18 accounts in draft and provided me with its views before I formally signed the accounts.

5.3 No significant internal control issues, including data related incidents, have been identified in 2017-18, and no significant new risks have been identified in the year. No ministerial directions have been given in 2017-18.

5.4 In my opinion, the system of internal control was effective throughout the financial year and remains so on the date I sign this report.

Parliamentary accountability and audit report

Regularity of expenditure

The expenditure and income of the NLF were applied to the purposes intended by Parliament.

The borrowings, investments and lending of the NLF were applied to the purposes intended by Parliament.

The above statements have been audited.

Losses and special payments

Currency losses from transactions with the IMF and the issuance and redemption of the renminbi bond are disclosed within the financial statements.

The above statements have been audited.

Fees and charges

The NLF does not have any fees or charges.

The above statement has been audited.

Remote contingent liabilities

The NLF has two contingent liabilities which fall outside the scope of IAS 37 as the possibility of an outflow of resources is remote. Disclosure of these liabilities is necessary however under Parliamentary reporting requirements.

i) Under the National Loans Act 1968 section 9(3), the NLF has a contingent liability to the Bank of England Issue Department in respect of that part of the assets backing the note issue that is not represented by government securities. This liability would only crystallise if government securities were insufficient to meet demand from holders of notes to exchange them for another instrument. The contingent liability was £71,943 million at 31 March 2018 (£70,851 million at 31 March 2017). No obligations crystallised or expired in 2017-18 (2016-17: none).

ii) The NLF has a contingent liability to the Commissioners for the Reduction of the National Debt (CRND) in respect of unclaimed dividends received in previous years. This represents old uncleared amounts surrendered by the gilts registrar to CRND and then onto the NLF and stood at £30.2 million at 31 March 2018 (£29.9 million at 31 March 2017). This contingent liability would crystallise if holders of gilts requested amounts owed to them in excess of an amount for settlement retained by CRND. No obligations crystallised or expired in 2017-18 (2016-17: none).

The above statements have been audited.

Tom Scholar
Accounting Officer
HM Treasury

10 July 2018

The Certificate and Report of the Comptroller and Auditor General to the Houses of Parliament

Opinion on financial statements

I certify that I have audited the financial statements of the National Loans Fund for the year ended 31 March 2018 under the National Loans Act 1968. The financial statements comprise: the Statements of Comprehensive Net Expenditure, Financial Position, Cash Flows, Changes in the Liability of the Consolidated Fund to the National Loans Fund; and the related notes, including the significant accounting policies. These financial statements have been prepared under the accounting policies set out within them. I have also audited the information in the Accountability Report that is described in that report as having been audited.

In my opinion:

- the financial statements give a true and fair view of the state the National Loans Fund's affairs as at 31 March 2018 and of the total comprehensive net expenditure for the year then ended; and
- the financial statements have been properly prepared in accordance with the National Loans Act 1968 and in the form prescribed by HM Treasury.

Opinion on regularity

In my opinion, in all material respects the income and expenditure recorded in the financial statements have been applied to the purposes intended by Parliament and the financial transactions recorded in the financial statements conform to the authorities which govern them.

Basis of opinions

I conducted my audit in accordance with International Standards on Auditing (ISAs) (UK) and Practice Note 10 'Audit of Financial Statements of Public Sector Entities in the United Kingdom'. My responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of my certificate. Those standards require me and my staff to comply with the Financial Reporting Council's Revised Ethical Standard 2016. I am independent of the National Loans Fund in accordance with the ethical requirements that are relevant to my audit and the financial statements in the UK. My staff and I have fulfilled our other ethical responsibilities in accordance with these requirements. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Responsibilities of HM Treasury and the Accounting Officer for the financial statements

As explained more fully in the Statement of Accounting Officer's Responsibilities, HM Treasury and the Accounting Officer are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

Auditor's responsibilities for the audit of the financial statements

My responsibility is to audit, certify and report on the financial statements in accordance with the National Loans Act 1968.

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs (UK), I exercise professional judgment and maintain professional scepticism throughout the audit. I also:

- identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the National Loans Fund's internal control.
- evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the National Loans Fund's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my auditor's report. However, future events or conditions may cause the entity to cease to continue as a going concern.
- evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

I communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.

In addition, I am required to obtain evidence sufficient to give reasonable assurance that the income and expenditure reported in the financial statements have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them.

Other Information

The Accounting Officer is responsible for the other information. The other information comprises information included in the Performance Report and Accountability Report, other than the parts of the Accountability Report described in that report as having been audited, the financial statements and my auditor's report thereon. My opinion on the financial statements does not cover the other information and I do not express any form of assurance conclusion thereon. In connection with my audit of the financial statements, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or my knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work I have performed, I conclude that there is a material misstatement of this other information, I am required to report that fact. I have nothing to report in this regard.

Opinion on other matters

In my opinion:

- the parts of the Accountability Report to be audited have been properly prepared in accordance with applicable law;
- in the light of the knowledge and understanding of the National Loans Fund and its environment obtained in the course of the audit, I have not identified any material misstatements in the Performance Report or the Accountability Report; and
- the information given in the Performance Report and Accountability Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which I report by exception

I have nothing to report in respect of the following matters which I report to you if, in my opinion:

- adequate accounting records have not been kept or returns adequate for my audit have not been received from branches not visited by my staff; or
- the financial statements and the parts of the Accountability Report to be audited are not in agreement with the accounting records and returns; or
- I have not received all of the information and explanations I require for my audit; or
- the Governance Statement does not reflect compliance with HM Treasury's guidance.

Report

I have no observations to make on these financial statements.

Sir Amyas C E Morse
Comptroller and Auditor General

13 July 2018

National Audit Office
157-197 Buckingham Palace Road
Victoria
London SW1W 9SP

Statement of Comprehensive Net Expenditure for the year ended 31 March 2018

	Note	**2017-18 £m**	2016-17 £m
Finance costs of borrowing	2	**56,809**	51,525
Income from lending operations	3	**(3,294)**	(3,293)
Losses / (gains) on foreign exchange transactions	4	**245**	(548)
Other expenditure	5	**1,507**	174
Other income	5	**(672)**	(14,184)
Total comprehensive net expenditure		**54,595**	33,674

The notes on pages 22 to 40 form part of this Account.

Statement of Financial Position as at 31 March 2018

	Note	**At 31 March 2018 £m**	At 31 March 2017 £m
Assets			
Advances	6	**174,903**	209,843
Loans	7	**3,156**	2,858
Other assets	8	**108,155**	108,353
IMF Quota Subscription & Lending	9	**21,883**	23,223
Total assets		**308,097**	344,277
Liabilities			
Gilt-edged stock	10	**1,633,022**	1,602,816
National Savings and Investments products	11	**156,738**	146,942
Other debt:			
FLS Treasury Bills	12	**39,150**	75,069
Other	12	**60,965**	45,217
Liabilities to the IMF	9	**17,782**	17,946
Total liabilities		**1,907,657**	1,887,990
Net liabilities		**1,599,560**	1,543,713
Liability of the Consolidated Fund to the National Loans Fund		**1,599,560**	1,543,713

The notes on pages 22 to 40 form part of this Account.

Tom Scholar
Accounting Officer
HM Treasury

10 July 2018

Statement of Cash Flows for the year ended 31 March 2018

	2017-18 **£m**	2016-17 £m
Cash flows from operating activities		
Interest received	**3,045**	3,323
Other receipts	**30**	207
Interest paid	**(45,253)**	(45,788)
Other outflows	**(1,498)**	(605)
Transfer from the Consolidated Fund for the cost of debt servicing	**43,676**	42,863
Net cash flow from operating activities	**-**	-
Cash flows from investing activities		
Net decrease in advance to the Debt Management Account	**45,000**	5,000
Net increase in advance to the Public Works Loan Board	**(3,510)**	(1,773)
Net (increase) / decrease in loans	**(149)**	557
Net increase in advance to the Exchange Equalisation Account	**(6,300)**	(6,525)
Net cash inflow / (outflow) from investing activities	**35,041**	(2,741)
Cash flows from financing activities		
Net issuance of government stock	**20,261**	73,327
Net redemption of Treasury Bills for Funding for Lending	**(35,908)**	(11,204)
Net receipt of cash from National Savings	**7,519**	10,524
Net increase / (decrease) in other sterling borrowing	**16,083**	(6,276)
Net transfers of IMF non-interest bearing securities	**2,276**	458
Net Foreign currency borrowing	**(344)**	-
Net transfers to the Consolidated Fund	**(44,928)**	(64,088)
Net cash (outflow) / inflow from financing activities	**(35,041)**	2,741
Net change in cash and cash equivalents	**-**	-
Cash and cash equivalents at beginning and end of year	**-**	-

The notes on pages 22 to 40 form part of this Account.

Statement of Changes in the Liability of the Consolidated Fund to the National Loans Fund for the year ended 31 March 2018

	2017-18 £m	2016-17 £m
Liability of the Consolidated Fund to the National Loans Fund at 1 April	**1,543,713**	1,488,814
Net cash paid to the Consolidated Fund	**44,928**	64,088
Payment from the Consolidated Fund for the cost of debt servicing during the year	**(43,676)**	(42,863)
Total comprehensive net expenditure	**54,595**	33,674
Liability of the Consolidated Fund to the National Loans Fund at 31 March	**1,599,560**	1,543,713

The notes on pages 22 to 40 form part of this Account.

Notes to the Account

1 Accounting Policies

i Accounting convention

The National Loans Fund (NLF) was established on 1 April 1968 by the National Loans Act 1968 to account for government borrowing and lending which were until then accounted for as part of the Consolidated Fund (CF). The NLF Account has been prepared under the historical cost convention and in accordance with International Financial Reporting Standards (IFRSs) as adapted or interpreted for the public sector context in so far as they are relevant to transactions and balances within the NLF.

ii Applicable accounting standards and interpretations issued but not yet adopted

IFRS 9 'Financial Instruments', was issued in July 2014 and is set to replace IAS 39 'Financial Instruments: Recognition and Measurement'. It sets out requirements for recognition, measurement, impairment and de-recognition of financial instruments as a single IFRS framework for all financial instruments required or permitted by IFRS. IFRS 9 is effective for reporting periods beginning on or after 1 January 2018. It is expected that the application of IFRS 9 should not have a material impact upon the financial statements of the NLF.

Other accounting standards in issue or revised but not yet effective will not impact on the NLF.

iii Basis of presentation

The NLF Account is stated in millions of pounds sterling (£m). This Account presents the results and transactions of the NLF. The Statement of Financial Position is presented in order of liquidity. The NLF is the government's main borrowing and lending account. By the nature of government financing, it is expected that the NLF will show a net liability. By virtue of section 19(1) of the National Loans Act 1968, the net liabilities of the NLF are a liability of the CF. The servicing of the NLF's liabilities is expected to be mainly met through future tax revenue receipts. There is no reason to believe that tax revenues will not be forthcoming and therefore, in accordance with the Government Financial Reporting Manual, it has been concluded as appropriate to adopt the going concern basis of preparation for the NLF Accounts.

iv Recognition of finance income and costs

Premium Bond prizes are recognised in the period to which they relate. Other interest income and costs of financing are determined using the effective interest rate method. The effective interest rate method is a method of calculating the amortised cost of a financial asset or financial liability and of allocating the interest income or interest expense over the expected life of the asset or liability. The effective interest rate is the rate that exactly discounts estimated future cash flows to the instrument's initial carrying amount. The calculation takes into account premiums or discounts on acquisition or issue of financial assets and liabilities and all the contractual terms of the financial instrument.

The majority of the NLF's financial assets and liabilities have a fixed return. For those products that have a variable return, the current rate applicable to that product is used in the calculation of the finance income or cost. Gilts with the same maturity and coupon rate are sometimes issued in separate tranches. Because of market conditions each tranche may be issued with a different premium or discount and therefore a different effective interest rate. However, once issued, gilts with the same maturity and coupon rate are indistinguishable from each other and so are accounted for as one issue using a weighted average effective interest rate.

v Recognition of finance income – Special Drawing Rights (SDR)

The IMF remunerates the UK in SDRs on its Reserve Tranche Position (RTP) for balances in excess of SDR 700 million and on its bilateral loans. Under section 3(2) of the Exchange Equalisation Act 1979 any SDRs received by the Government must be treated as assets of the EEA, therefore all SDR income is accounted for in the EEA and not the NLF.

vi Financial assets and liabilities

The assets and liabilities of the NLF are all accounted for as financial assets and liabilities except for those arising from the net assets of the EEA and the DMA which are accounted for as explained in accounting policy ix. The NLF's financial assets are all designated as loans and receivables. In accordance with IAS 39, financial assets and liabilities are initially recognised at fair value. They are subsequently measured at amortised cost using the effective interest rate method. If gilts are issued by a syndication process, the syndication fees are borne by the NLF and are netted off from gross issuance proceeds as part of the calculation of amortised cost. Other directly related issue costs for assets and liabilities are negligible and are written off as incurred.

The distinction between loans and advances derives from the legislation that governs the operation of the NLF. On loans, interest must be charged at a rate that at least covers the cost that the Fund would have to bear if it were to borrow the same sum for the period of the loan, plus the Treasury's own administration costs. There is no such requirement for advances, although interest is charged at Bank Rate on advances to the DMA. No interest is charged on advances to the EEA. The NLF does not charge interest on its advances to PWLB but interest on loans by the PWLB to local authorities financed by NLF advances is paid to the NLF under section 3(3) of the National Loans Act 1968.

The fair values of the financial assets and liabilities are disclosed in note 13. They are calculated by reference to market prices where instruments are traded on an active quoted market or, where this is not the case, as the net present value of future cash flows.

Impairment of financial assets

Exchequer Funds and Accounts (EFA) assesses at the end of each reporting period whether there is any objective evidence that a financial asset measured at amortised cost is impaired. An asset is impaired if there is objective evidence of impairment as a result of one or more events that occurred after the recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset that can be reliably estimated. Objective evidence used in assessing whether a financial asset is impaired includes financial difficulties experienced by the borrower and breach of loan conditions such as a default or delinquency in interest or principal payments. No impairment losses have been recognised during the year.

vii Foreign currencies

The financial statements of the NLF are presented in sterling which is the Fund's functional currency, being the currency of the primary economic environment in which it operates. Transactions denominated in foreign currencies are recorded at the rate of exchange applicable to the transaction. Monetary assets and liabilities denominated in foreign currencies at the end of the reporting period are reported at the rates of exchange prevailing at that date. Liabilities to the IMF are denominated in sterling but are subject to a revaluation adjustment reflecting movement in the SDR to sterling exchange rate.

viii Administration expenditure

These financial statements reflect activity through, and the financial position of, the NLF. The costs of gilts registration, listing fees and foreign currency debt issuance are met by the NLF. Administration costs such as departmental staff costs and bank charges are borne by the appropriate body and accounted for through their respective accounts.

ix Exchange Equalisation Account and Debt Management Account

Under section 11 of Schedule 5A to the National Loans Act 1968, any excess of the assets of the DMA over its liabilities shall be a liability of the DMA to the NLF. Over time, the NLF has advanced sterling to the EEA in order to finance the UK's reserves of gold, foreign currency assets and IMF Special Drawing Rights. As a result, having been derived from initial NLF financing, the EEA's net assets are ultimately due to the NLF. Annual financial statements are prepared for both the DMA and the EEA. The net assets of the DMA and EEA are reported in Other Assets (note 8) and the total comprehensive net expenditure or income recognised in the Statement of Comprehensive Net Expenditure as Other Expenditure or Other Income (note 5). These NLF assets and net income or expenditure are the result of activity in the EEA and DMA during the year and the various accounting policies applied by them to that activity.

x Critical accounting judgements and key sources of estimation uncertainty

The NLF's accounting policy for impairment losses arising on financial assets is described in vi above. No impairment losses have been recognised in the year. There are no other areas of the financial statements which are reliant on management's judgement in the process of applying the Fund's accounting policies. Fair values are included for disclosure purposes only. Their calculation is described in note 13. As mentioned in accounting policy iv, the majority of the NLF's financial assets have a fixed return. For those products that have a variable return, the current rate applicable to that product is used in the calculation of the finance income or cost. Note 15 applies various assumptions to demonstrate the sensitivity of NLF's assets and liabilities to changes in interest rates, inflation and foreign currency exchange rates.

2 Finance costs of borrowing

	2017-18 £m	2016-17 £m
Gilt-edged stock	**53,922**	48,631
National Savings and Investments products	**2,487**	2,334
Treasury Bills (Funding for Lending)	**268**	429
Other finance costs	**132**	131
Total finance costs of borrowing	**56,809**	51,525

3 Income from lending operations

	2017-18 £m	2016-17 £m
Interest on loans advanced by the National Loans Fund to:		
Public corporations	**44**	45
Central government bodies	**72**	76
	116	121
Interest on loans by the Public Works Loan Board financed by National Loans Fund advances	**2,848**	2,837
Interest on funding advanced to the Debt Management Account	**330**	335
Total income from lending operations	**3,294**	3,293

4 Gains and losses on foreign exchange transactions

	Note	**2017-18 £m**	2016-17 £m
(Gain) / loss on foreign currency borrowing		**(5)**	26
Loss / (gain) on Reserve Tranche Position at the IMF	9	**185**	(389)
Loss / (gain) on lending to the IMF	9	**65**	(185)
Net loss / (gain) on foreign currency transactions		**245**	(548)

5 Other income and expenditure

	2017-18 £m	2016-17 £m
Other expenditure		
EEA total comprehensive net expenditure [1]	**1,338**	-
Expenditure in respect of depreciation of Issue Department Assets [2]	**166**	171
Miscellaneous expenditure	**3**	3
Total: Other expenditure	**1,507**	174
Other income		
EEA total comprehensive net income [1]	**-**	(3,649)
DMA total comprehensive net income	**(473)**	(10,154)
Profits of the Bank of England Issue Department [2]	**(196)**	(241)
Income in respect of appreciation of Issue Department Assets [2]	**-**	(137)
Miscellaneous receipts	**(3)**	(3)
Total: Other income	**(672)**	(14,184)
Net total	**835**	(14,010)

[1] The EEA made a loss of £1,338 million (2016-17: £3,649 million profit). Of the £1,338m net expenditure to the EEA, £27 million (2016-17: £7 million) relates to interest income from the IMF Reserve Tranche Position and bilateral loans to the IMF in line with accounting policy v.

[2] Under section 9 of the National Loans Act 1968, the profits of the Issue Department are paid into the NLF. In addition, the Bank of England Issue Department is required by the Currency and Bank Notes Act 1928 to hold investments equal to the value of bank notes in issue. These investments are revalued to market value quarterly. If the market value is less than the value of notes in issue, legislation requires the NLF to pay an amount equal to the deficiency to the Issue Department to finance the purchase of additional investments. Conversely, if the market value of the assets exceeds the value of notes in issue, the Issue Department sells investments to the value of the surplus and pays the proceeds to the NLF.

6 Advances

	Public Works Loan Board		Debt Management Account		Exchange Equalisation Account		Total	
	£m	£m	**£m**	£m	**£m**	£m	**£m**	£m
	2017-18	2016-17	**2017-18**	2016-17	**2017-18**	2016-17	**2017-18**	2016-17
Principal outstanding at 1 April	**66,602**	64,829	**93,000**	98,000	**49,697**	43,172	**209,299**	206,001
Advances	**5,162**	3,634	**75,000**	30,000	**9,500**	9,875	**89,662**	43,509
Advances repaid	**(1,652)**	(1,861)	**(120,000)**	(35,000)	**(3,200)**	(3,350)	**(124,852)**	(40,211)
Principal outstanding at 31 March	**70,112**	66,602	**48,000**	93,000	**55,997**	49,697	**174,109**	209,299
Accrued interest	**764**	524	**30**	20	**-**	-	**794**	544
Total advances outstanding	**70,876**	67,126	**48,030**	93,020	**55,997**	49,697	**174,903**	209,843

7 Loans and commitments to lend

Loans			**2017-18**			2016-17
	Public Corporations	**Central Government**	**Total**	Public Corporations	Central Government	Total
	£m	**£m**	**£m**	£m	£m	£m
Principal outstanding at 1 April	**684**	**2,153**	**2,837**	711	2,089	2,800
Loans advanced	**306**	**484**	**790**	319	214	533
Loans repaid	**(335)**	**(156)**	**(491)**	(346)	(150)	(496)
Principal outstanding at 31 March	**655**	**2,481**	**3,136**	684	2,153	2,837
Accrued interest	**9**	**11**	**20**	9	12	21
Total loans outstanding	**664**	**2,492**	**3,156**	693	2,165	2,858

Commitments to lend			**At 31 March 2018**			At 31 March 2017
	Public Corporations	**Central Government**	**Total**	Public Corporations	Central Government	Total
	£m	**£m**	**£m**	£m	£m	£m
Undrawn commitments to lend	**6**	**-**	**6**	8	-	8

Commitments to lend are agreements to lend to a customer in the future subject to certain conditions. Such commitments are made either for a fixed period or have no specific maturity but are cancellable by the lender. The NLF does not have any loans or commitments to lend to financial institutions classified as 'Public Financial Corporations' following the banking crisis. In addition to the above, the NLF has loans and a loan commitment to the IMF which is explained in note 9.

8 Other assets

	At 31 March 2018 £m	At 31 March 2017 £m
Exchange Equalisation Account net assets	**31,719**	33,057
Debt Management Account net assets	**74,817**	74,344
Cash held by National Savings and Investments	**1,566**	897
Sterling balances at Bank of England advanced to IMF	**53**	55
Total other assets	**108,155**	108,353

9 IMF Reserve Tranche Position and Lending to the IMF

The United Kingdom's relationship with the International Monetary Fund (IMF) is accounted for in the NLF and the EEA. The UK's quota subscription to the IMF, 20,155 million Special Drawing Rights (SDRs) - equivalent to £20,836 million[6] at 31 March 2018 (£21,961 million at 31 March 2017) - was paid from the NLF and is recognised as an NLF asset. Part of the subscription is deposited by the IMF in the NLF in return for sterling non-interest-bearing securities (NIBS) which totalled £18,171 million at 31 March 2018 (£15,895 million at 31 March 2017). NIBS represent a liability of the NLF to the IMF. There is a remaining small liability of £53 million (£55 million at 31 March 2017) against which an equal amount of sterling cash is made available in an account at the Bank of England for drawdown by the IMF.

The difference between the gross quota subscription and the NLF's sterling liability to the IMF is the UK's reserve tranche position (RTP). Under the arrangements for membership of the Fund, valuation adjustments are made between the IMF and NLF annually to reflect any changes in value in SDR terms of the NLF's sterling liability to the IMF. An annual settlement payment is made between the NLF and the IMF, normally in May. The cumulative valuation adjustment at 31 March 2018 was £442 million gain (£1,996 million loss at 31 March 2017). The table below sets out the composition of the RTP and the make-up of changes over the year.

[6] The GBP/SDR exchange rate at 31 March 2018 was 0.967313 (31 March 2017: 0.917752)

NLF Assets and Liabilities: Composition of the Reserve Tranche Position and Lending[7] to the IMF

	Asset	Liabilities				Reserve Tranche Position
	IMF Quota Subscription	Non-interest-bearing securities	Other quota liability	Valuation adjustment	Total liabilities	
	£m	£m	£m	£m	£m	£m
Balances at 31 March 2017	21,961	(15,895)	(55)	(1,996)	(17,946)	4,015
Exchange rate losses for the year on the Quota subscription	(1,125)				-	(1,125)
Change in year-end valuation adjustment				2,438	2,438	2,438
Change in loan notes as a result of the valuation settlement		(1,498)			(1,498)	(1,498)
Change in cash on No 1 account			2		2	2
Cash subscribed to the IMF	-				-	-
Net increase in loan notes		(778)			(778)	(778)
Balances at 31 March 2018	**20,836**	**(18,171)**	**(53)**	**442**	**(17,782)**	**3,054**

Lending to the IMF	**£m**
Lending as at 31 March 2017	1,262
Loans advanced in 2017-18	200
Loans repaid in 2017-18	(350)
Loss on foreign exchange	(65)
Lending as at 31 March 2018	**1,047**
IMF Quota Subscription and Lending	**21,883**

The RTP is a net asset of the NLF. It represents an SDR asset that can be drawn on by the UK if needed and is considered part of the UK's foreign exchange reserves. Sterling transactions by the IMF impact on the level of non-interest-bearing securities (NIBS) and hence on the RTP. Under current policy, changes in the RTP lead to adjustments in the composition of other reserve assets (held in the EEA) in order to keep the portfolio composition of the reserves in line with plan. Interest is payable by the IMF on the RTP balance in excess of SDR 700 million. This interest is retained in the EEA.

[7] Lending includes both loans made under the New Arrangements to Borrow (NAB) and the bilateral loan facility

Separately, the EEA also holds the UK's allocation of SDRs (SDR 10,134 million at 31 March 2018) as a liability to the IMF and retains an asset in the form of the UK's holdings of SDRs (SDR 8,322 million at 31 March 2018).

During 2017-18 the IMF deposited a net amount of £778 million into the NLF in return for NIBs, representing a net repayment of amounts provided from the UK quota subscription in support of IMF funding programmes (a net payment to the IMF of £147 million was made in 2016-17).

During 2009-10 the UK agreed to provide a bilateral loan facility (2009 bilateral loans) to the IMF for an amount up to the equivalent of SDR 9,920 million (£10,255 million at the 31 March 2018 exchange rate). In March 2011, all outstanding claims under the 2009 bilateral loan agreement were folded into the New Arrangements to Borrow (NAB) (see below). The total drawn loans represent a claim on the IMF and are therefore an asset of the NLF and the undrawn loans are a commitment of the NLF. Interest is payable by the IMF on the loan balance and is retained in the EEA in line with accounting policy v.

In April 2012, a G20-led agreement to a temporary increase in IMF resources was reached. As part of this, the UK agreed to provide a new bilateral loan facility (2012 bilateral loans) worth SDR 9,178 million (£9,488 million). This loan facility expired without being used in October 2016.

The UK agreed to a third bilateral loan to the IMF, again worth SDR 9,178 million (£9,488 million), in October 2016 (2016 bilateral loans). The 2016 bilateral loan facility has not been used yet.

On 1 April 2011 IMF members agreed to the first activation of the expanded New Arrangements to Borrow (NAB), the IMF's main backstop over and above quota resources. The UK's commitment to the expanded NAB is SDR 18,657 million (£19,287 million at the 31 March 2018 exchange rate). The new NAB however can only be used to finance drawings under IMF commitments approved during its activation periods. Most recently, the NAB was re-activated during 2015-16 for further six month periods on 1 April and 1 October 2015. The expanded NAB was reduced and deactivated in February 2016 when the Fourteenth General Review of Quotas (GRQ – see below) was implemented. Accordingly, the UK's NAB commitment was reduced to SDR 9,479 million (£9,799 million).

On 26 January 2016, the IMF's Fourteenth GRQ, agreed in November 2010, took effect. As a result, the UK's quota subscription increased from SDR 10,739 million to SDR 20,155 million, an increase of SDR 9,416 million. Related transactions were completed on 23 February 2016, as approved by Parliament in July 2011.

UK's total commitment to the IMF

	At 31 March 2018			At 31 March 2017		
	Total commitment	**Total drawn**	**Total undrawn**	Total commitment	Total drawn	Total undrawn
Quota (SDRm)	**20,155**	**2,953**	**17,202**	20,155	3,685	16,470
Loans (SDRm)	**18,657**	**1,013**	**17,644**	18,657	1,158	17,499
Total (SDRm)	**38,812**	**3,966**	**34,846**	38,812	4,843	33,969
Quota (£m)	**20,836**	**3,054**	**17,782**	21,961	4,015	17,946
Loans (£m)	**19,287**	**1,047**	**18,240**	20,329	1,262	19,067
Total (£m)	**40,123**	**4,101**	**36,022**	42,290	5,277	37,013

All anticipated changes to the UK's quota subscription and loans to the IMF are reflected within current limits approved by Parliament.

10 Gilt-edged stock

	Conventional £m	Index-Linked £m	Total £m
At 31 March 2017	1,173,632	429,184	1,602,816
Receipts from gilt issuance	87,007	28,520	115,527
Payments for gilt redemption	(67,409)	(16,372)	(83,781)
Net redemption of DMA gilts	(11,003)	(482)	(11,485)
Amortisation of premiums and discounts	(3,663)	2,573	(1,090)
Change in accrued interest	(35)	11,070	11,035
At 31 March 2018	**1,178,529**	**454,493**	**1,633,022**

The NLF issues gilts directly to the DMA for use by the Debt Management Office in its money market activities managing the Exchequer's daily cash requirement. These gilts do not contribute directly to Exchequer financing. All other gilts are sold into the primary gilt market to meet government financing needs.

The analysis below shows two large holdings of the gilt liability by UK public sector entities, the DMA and Bank of England.

	At 31 March 2018 £m	At 31 March 2017 £m
Debt Management Account (DMA)	**112,592**	123,814
Bank of England (for quantitative easing)	**380,619**	387,756
Other investors	**1,139,811**	1,091,246
Total gilt-edged stock	**1,633,022**	1,602,816

Syndication fees are borne by the NLF and are netted off from gross issuance proceeds as part of the calculation of amortised cost. Other directly related issue costs for assets and liabilities are negligible and are written off as incurred. Total syndication fees for the year were £34 million (2016-17: £48 million).

11 National Savings and Investments (NS&I) products

	2017-18 £m	2016-17 £m
Principal outstanding at 1 April	**146,229**	134,597
Cash repayments from the National Loans Fund	**(33,845)**	(23,658)
Principal cash received in the National Loans Fund	**41,364**	34,182
Capitalised interest and other returns to savers	**1,586**	1,373
Change in cash holdings for principal	**665**	(265)
Principal outstanding at 31 March	**155,999**	146,229
Accrued interest and other returns to savers	**739**	713
Total principal and accrued interest outstanding	**156,738**	146,942

NS&I provides more detail on this liability in a set of Product Accounts which are published with the NS&I resource accounts on the NS&I website[8].

12 Other debt

	At 31 March 2018 £m	At 31 March 2017 £m
FLS Treasury Bills	**39,150**	75,069
Other:		
Debt Management Account	**27,616**	13,061
Bank of England Issue Department	**370**	370
Balances from government accounts at the Government Banking Service	**23,615**	21,490
Deposits from public sector bodies	**8,193**	8,587
Foreign currency debt	**-**	353
Other	**1,171**	1,356
	60,965	45,217
Total other debt payable	**100,115**	120,286

Treasury Bills have been issued by the NLF to the DMA in connection with the Bank of England's Funding for Lending Scheme (FLS). Further information on the scheme is provided in the Performance report.

[8] http://nsandi-corporate.com/about-nsi/our-performance/our-annual-report-and-accounts/

The next two items reflect deficit funding from the DMA and the Issue Department of the Bank of England. The fourth item reflects the transfer to the NLF of any temporary cash surpluses on other government accounts held at Government Banking. Deposits from public sector bodies represents deposits by public sector bodies which are directly held with the NLF. "Other" comprises mostly certificates of tax deposit held by the NLF. From 23 Nov 2017, the CTD scheme has been closed for new purchases, but existing certificates will continue to be honoured until 23 November 2023.

At 31 March 2018, there was no foreign currency debt outstanding in the NLF as the renminbi issuance in October 2014 matured in October 2017.

13 Fair Values

Carrying Value and Fair Value of NLF assets and liabilities

	At 31 March 2018		At 31 March 2017	
	Carrying Value	**Fair Value**	Carrying Value	Fair Value
Assets	**£m**	**£m**	£m	£m
Advances:				
Public Works Loan Board	**70,112**	**102,249**	66,602	99,669
Debt Management Account	**48,000**	**48,000**	93,000	93,000
Exchange Equalisation Account	**55,997**	**55,997**	49,697	49,697
Accrued interest	**794**	**794**	544	544
Loans:				
Principal	**3,136**	**3,636**	2,837	3,456
Accrued interest	**20**	**20**	21	21
Other assets	**108,155**	**108,155**	108,353	108,353
IMF quota subscription & lending	**21,883**	**21,883**	23,223	23,223
Total assets	**308,097**	**340,734**	344,277	377,963
Liabilities				
Gilts	**1,633,022**	**2,077,136**	1,602,816	2,090,128
National Savings & Investments:				
Principal	**155,999**	**156,496**	146,229	146,858
Accrued interest	**739**	**747**	713	719
IMF liabilities	**17,782**	**17,782**	17,946	17,946
Other debt:				
Treasury Bills (Funding for Lending)	**39,150**	**39,165**	75,069	75,088
Debt Management Account	**27,616**	**27,616**	13,061	13,061
Issue Department of Bank of England	**370**	**370**	370	370
Government balances	**23,615**	**23,615**	21,490	21,490
Deposits from public sector bodies	**8,193**	**8,193**	8,587	8,587
Foreign currency debt	**-**	**-**	353	353
Other	**1,171**	**1,171**	1,356	1,356
Total liabilities	**1,907,657**	**2,352,291**	1,887,990	2,375,956

The NLF's assets are classified as financial assets except for the net assets of the EEA (£31,719 million, 2016-17: £33,057 million) and DMA (£74,817 million, 2016-17: £74,344 million), reported in Other Assets (note 8). The carrying value of financial assets (all of which are designated as loans and receivables) is £201,561 million (2016-17: £236,876 million) and their fair value is £234,198 million (2016-17: £270,562 million). All the NLF's liabilities are financial liabilities. In instances where the fair value differs from the carrying value, the fair value has been calculated by reference to market prices where instruments are traded on an active quoted market or, where this is not the case, as the net present value of future cash flows.

The fair value of advances to the PWLB is calculated as the net present value of future cash flows. Loans by the PWLB are usually at a fixed rate of interest and so their fair value increases or decreases according to changes in the difference between the fixed rate of interest earned on the loan and current market values. Differences between the fair and book value will not be realised as the PWLB loans are not traded by the NLF.

The fair value of gilts and Treasury Bills are calculated by reference to their market prices. They will generally be redeemed at their book values so any difference between their fair value and book value will not normally be realised in the NLF accounts.

14 Maturity of assets and liabilities

The following table shows the split between current and non-current assets and liabilities based on contract date of maturity or expected maturity if there is no contract date.

		At 31 March 2018			At 31 March 2017	
	Current	**Non-current**	**Total**	Current	Non-current	Total
	£m	**£m**	**£m**	£m	£m	£m
Assets						
Advances	**2,653**	**172,250**	**174,903**	2,261	207,582	209,843
Loans	**244**	**2,912**	**3,156**	236	2,622	2,858
Other assets	**1,620**	**106,535**	**108,155**	952	107,401	108,353
IMF quota subscription (SDR) & lending	**-**	**21,883**	**21,883**	-	23,223	23,223
Total assets	**4,517**	**303,580**	**308,097**	3,449	340,828	344,277
Liabilities						
Gilts						
Conventional	**78,777**	**1,099,752**	**1,178,529**	86,108	1,087,524	1,173,632
Index-linked	**1,033**	**453,460**	**454,493**	17,298	411,886	429,184
Gilt-edged stock	**79,810**	**1,553,212**	**1,633,022**	103,406	1,499,410	1,602,816
National Savings and Investments	**156,738**	**-**	**156,738**	146,942	-	146,942
IMF liabilities	**-**	**17,782**	**17,782**	-	17,946	17,946
Treasury Bills for FLS	**39,150**	**-**	**39,150**	75,069	-	75,069
Other debt payable	**60,765**	**200**	**60,965**	45,017	200	45,217
Total liabilities	**336,463**	**1,571,194**	**1,907,657**	370,434	1,517,556	1,887,990

All National Savings and Investments products are payable on demand and therefore classified as current liabilities.

The following table shows an analysis of current and non-current assets and liabilities by type of counterparty.

	At 31 March 2018			At 31 March 2017		
	Current	**Non-current**	**Total**	Current	Non-current	Total
	£m	**£m**	**£m**	£m	£m	£m
Assets						
Balances with:						
Other central government bodies	**4,393**	**281,104**	**285,497**	3,325	316,980	320,305
Public corporations and trading funds	**124**	**593**	**717**	124	625	749
Total intra government balances	**4,517**	**281,697**	**286,214**	3,449	317,605	321,054
Balances with bodies external to government	**-**	**21,883**	**21,883**	-	23,223	23,223
Total assets	**4,517**	**303,580**	**308,097**	3,449	340,828	344,277
Liabilities						
Balances with:						
Other central government bodies	**98,208**	**107,181**	**205,389**	125,707	111,264	236,971
NHS Trusts	**4,745**	**-**	**4,745**	4,077	-	4,077
Public corporations and trading funds	**25,454**	**365,038**	**390,492**	32,837	364,701	397,538
Total intra government balances	**128,407**	**472,219**	**600,626**	162,621	475,965	638,586
Balances with bodies external to government	**208,056**	**1,098,975**	**1,307,031**	207,813	1,041,591	1,249,404
Total liabilities	**336,463**	**1,571,194**	**1,907,657**	370,434	1,517,556	1,887,990

15 Financial risks related to the NLF

The Government's debt management objective is set out in the annual Debt and Reserves Management Report:

> *to minimise, over the long term, the costs of meeting the Government's financing needs, taking into account risk, whilst ensuring that debt management policy is consistent with the aims of monetary policy.*

This is achieved by:

- meeting the principles of openness, transparency and predictability;
- developing a liquid and efficient gilt market;
- issuing gilts that achieve a benchmark premium;
- adjusting the maturity and nature of the Government's debt portfolio, primarily by means of the maturity and composition of debt issuance and potentially by other market operations including switch auctions, conversion offers and buy-backs; and

- offering cost-effective savings instruments to the retail sector through National Savings & Investments.

For cash management, the aggregate balance on government accounts is swept daily to the National Loans Fund and then to the DMA. The Debt Management Office deals with the financial markets to manage the daily cash surplus or deficit on the DMA relative to its target overnight balance, lending when there is a surplus and borrowing when there is a deficit.

The NLF's liabilities include conventional and index-linked gilt-edged securities, NS&I product liabilities, certificates of tax deposit, Treasury Bills issued to the DMA for the Funding for Lending scheme, deposits from other public sector accounts and liabilities to the IMF. During the year NLF liabilities also included foreign currency debt denominated in Renminbi which matured in October 2017. There is a wide spread of maturities.

NLF assets include advances to the DMA, PWLB and EEA, loans to UK public bodies, net assets of the DMA and EEA, NS&I product-related cash holdings and the UK's gross Quota Subscription and lending to the IMF, denominated in SDRs.

Set out below are certain risk factors that could affect the NLF's operations.

Interest rate and inflation risk

The NLF is exposed to cash flow interest rate risk on its floating rate borrowing and lending due to the risk that future interest rates will fluctuate. It is not exposed to fair value interest rate risk as its financial assets and liabilities are measured at amortised cost and not fair value. Some of the NLF's assets and liabilities have no associated interest income or expense (are "zero-rated") and are therefore not exposed to changes in interest rates.

Inflation risk arises because interest and redemption amounts paid on index-linked gilts vary monthly in line with changes in the UK Retail Prices Index (RPI) since the initial issue of each stock.

The table below analyses the NLF's interest rate and inflation risk. Assets and liabilities are included at carrying amount and are shown at the earlier of contractual re-pricing or maturity dates.

Interest rate and inflation risk analysis as at 31 March 2018

	Up to 1 month/ repayable on demand £m	**1-12 months £m**	**1-5 years £m**	**Over 5 years £m**	**Zero-rated £m**	**Total carrying value £m**	**Fixed rate £m**	**Floating rate £m**
Assets								
Advances	48,394	2,027	7,658	60,023	56,801	**174,903**	69,496	48,606
Loans	30	193	768	2,145	20	**3,156**	3,136	-
Other assets	-	-	-	-	108,155	**108,155**	-	-
IMF quota subscription	-	-	-	-	20,836	**20,836**	-	-
IMF loans	-	-	-	-	1,047	**1,047**	-	-
Total	**48,424**	**2,220**	**8,426**	**62,168**	**186,859**	**308,097**	**72,632**	**48,606**
Liabilities								
Gilts								
Conventional	-	71,673	340,171	759,582	7,103	**1,178,529**	1,171,426	-
Index-linked	453,475	-	-	-	1,018	**454,493**	-	453,475
Gilt-edged stock	453,475	71,673	340,171	759,582	8,121	**1,633,022**	1,171,426	453,475
National Savings and Investments	133,709	6,767	15,439	-	823	**156,738**	23,558	132,357
IMF liabilities	-	-	-	-	17,782	**17,782**	-	-

Treasury Bills for FLS	5,380	33,770	-	-	-	**39,150**	39,150	-
Other debt payable	36,768	6,501	200	-	17,496	**60,965**	8,185	35,284
Total	**629,332**	**118,711**	**355,810**	**759,582**	**44,222**	**1,907,657**	**1,242,319**	**621,116**
Period gap	**580,908**	**116,491**	**347,384**	**697,414**	**(142,637)**	**1,599,560**		
Cumulative gap	**580,908**	**697,399**	**1,044,783**	**1,742,197**	**1,599,560**			

Interest rate and inflation risk analysis as at 31 March 2017

	Up to 1 month/ repayable on demand £m	1-12 months £m	1-5 years £m	Over 5 years £m	Zero-rated £m	**Total carrying value £m**	Fixed rate £m	Floating rate £m
Assets								
Advances	93,216	2,098	6,990	57,288	50,251	**209,843**	65,976	93,616
Loans	28	187	724	1,898	21	**2,858**	2,837	-
Other assets	-	-	-	-	108,353	**108,353**	-	-
IMF quota subscription	-	-	-	-	21,961	**21,961**	-	-
IMF loans	-	-	-	-	1,262	**1,262**	-	-
Total	**93,244**	**2,285**	**7,714**	**59,186**	**181,848**	**344,277**	**68,813**	**93,616**
Liabilities								
Gilts								
Conventional	-	78,969	353,200	734,325	7,138	**1,173,632**	1,166,494	-
Index-linked	428,137				1,047	**429,184**		428,137
Gilt-edged stock	428,137	78,969	353,200	734,325	8,185	**1,602,816**	1,166,494	428,137
National Savings and Investments	126,756	12,554	6,851	-	781	**146,942**	19,798	126,363
IMF liabilities					17,946	**17,946**		
Treasury Bills for FLS	9,730	65,339	-	-	-	**75,069**	75,069	-
Other debt payable	28,159	784	200	-	16,074	**45,217**	8,935	20,208
Total	**592,782**	**157,646**	**360,251**	**734,325**	**42,986**	**1,887,990**	**1,270,296**	**574,708**
Period gap	**499,538**	**155,361**	**352,537**	**675,139**	**(138,862)**	**1,543,713**		
Cumulative gap	**499,538**	**654,899**	**1,007,436**	**1,682,575**	**1,543,713**			

Foreign currency risk

The NLF is exposed to foreign exchange risk through transactions with the IMF as the reserve tranche position (quota subscription less UK liability) and lending to the IMF are denominated in SDRs (note 9). In addition to the risk of unrealised revaluations of the assets and liability, foreign exchange gains and losses are realised as the NLF transacts with the IMF on the UK liability and loans. As it is not possible to predict the size and timing of these transactions with any certainty it has not been deemed cost-effective to attempt to mitigate this risk through hedging arrangements.

Sensitivity analysis

The following analysis, required by IFRS 7, is intended to illustrate the sensitivity of the NLF's financial assets and liabilities to changes in UK interest rates, the UK Retail Prices Index and the SDR to sterling and Renminbi to sterling exchange rates. The sensitivity analysis has been calculated on the basis that the components of financial assets and liabilities, the amount of instruments held at fixed, floating and zero interest rates and the amount of instruments held in SDRs are all constant and are as at the end of the reporting period.

The following assumptions have been made in calculating sensitivity:

- All sensitivities impact the Statement of Comprehensive Net Expenditure and thereby the net liability of the CF to the NLF.
- Finance income and costs and the net liability of the CF to the NLF will be affected by changes in interest rates on floating rate instruments.
- All instruments are held at amortised cost and are therefore not subject to changes in fair value as a result of interest rate changes.
- No sensitivity is provided for interest accruals where these are based on pre-agreed interest rates and are therefore not susceptible to further rate changes.
- 100 basis points and 10 percent are management's assessment of the reasonably possible change in interest, RPI and FX rates at the end of the reporting period. This is not a forecast.

Using the above assumptions, the following table shows the illustrative impact on the Statement of Comprehensive Net Expenditure that would result from an increase in UK interest rates and the UK Retail Prices Index and if the SDR and Renminbi to sterling exchange rates were to strengthen.

	2017-18 Statement of Comprehensive Net Expenditure	2016-17 Statement of Comprehensive Net Expenditure
	£m	£m
UK interest rates + 100bp expense	**1,190**	530
UK Retail Prices Index + 100bp expense	**4,535**	4,281
SDR exchange rate + 10% income	**(410)**	(528)
Renminbi exchange rate + 10% expense	**-**	35

An equal, but opposite effect would result if there were a decrease in UK interest rates and the UK Retail Prices Index, and if the SDR and Renminbi to sterling exchange rates were to weaken.

Liquidity risk

Liquidity risk is the risk that the NLF will encounter difficulty in meeting obligations associated with financial liabilities. Its exposure to liquidity risk arises because of its fundamental purpose of being the Government's main borrowing account. NLF liabilities carry a wide range of maturities, spreading funding requirements for redemption payments, and thus liquidity risk, across a wide time period into the future. The longest stock in existence at 31 March 2018 matures in 2068. Deposits in the NLF have a shorter maturity profile since they can change on demand. However, in practice, balances change only slowly due to re-investment. By virtue of section 19(1) of the National Loans Act 1968, the net liabilities of the NLF are a liability of the Consolidated Fund. The servicing of the NLF's liabilities is expected to be mainly met through future tax revenue receipts. There is no reason to believe that tax revenues will not be forthcoming and therefore, in accordance with the Government Financial Reporting Manual, it has been concluded as appropriate to adopt the going concern basis of preparation for the NLF Accounts. Most of the NLF's borrowing needs are met through borrowing on its behalf by the DMO and NS&I.

Contractual undiscounted cash flows of financial liabilities

The following table shows the contractual undiscounted cash flows of the NLF's liabilities. The amounts shown are the cash flows arising from the NLF's financial liabilities during the period up to and including maturity. This is in contrast to the basis on which the Statement of Financial Position amounts are calculated. As described in note 1, items on the Statement of Financial Position are valued at fair value upon initial recognition and subsequently held at amortised cost. Therefore, totals in the following table will not agree to the Statement of Financial Position.

The treatment of coupon payments is of particular significance. The table includes contractual coupon payments for the period to maturity based on coupon rates and, in the case of index-linked gilts, the Retail Prices Index at 31 March 2018. Because of the many coupon payments to be made for longer dated gilts the table below reports coupon cash flows of £630,833 million (£647,116 million at 31 March 2017) whereas the gilts liability in the Statement of Financial Position contains coupon accruals to the end of the reporting period of £8,137 million (£8,200 million at 31 March 2017).

The cash flows reported in the table will be funded by replacement debt issues, the proceeds of assets or by finance from the Consolidated Fund.

At 31 March 2018

	0-12 months	1-2 years	2-5 years	Over 5 years	Undated	Total
Liabilities	£m	£m	£m	£m	£m	£m
Conventional Gilts:						
Principal	71,194	98,553	237,285	728,917	-	1,135,949
Coupons	38,164	35,453	87,821	415,398	-	576,836
Index-Linked Gilts:						
Principal	-	9,043	42,773	359,520	-	411,336
Coupons	3,762	3,762	9,899	36,574	-	53,997
Total Gilts	113,120	146,811	377,778	1,540,409	-	2,178,118
National Savings and Investments	156,653	-	-	-	84	156,737
IMF	17,783	-	-	-	-	17,783
Treasury Bills For FLS	39,229	-	-	-	-	39,229
Temporary Deposits	8,002	-	-	-	-	8,002
Other debt payable	52,776	202	-	-	-	52,978
	387,563	147,013	377,778	1,540,409	84	2,452,847

The cash flow analysis after five years is:

	5-10 years	10-20 years	20-30 years	30-40 years	Over 40 years	Total
	£m	£m	£m	£m	£m	£m
Conventional Gilts:						
Principal	218,784	164,604	201,686	81,421	62,422	728,917
Coupons	115,547	161,881	87,695	37,601	12,674	415,398
Index-Linked Gilts:						
Principal	70,960	102,404	82,162	67,769	36,225	359,520
Coupons	12,276	14,780	6,255	2,793	470	36,574
	417,567	443,669	377,798	189,584	111,791	1,540,409

At 31 March 2017

	0-12 months	1-2 years	2-5 years	Over 5 years	Undated	Total
Liabilities	£m	£m	£m	£m	£m	£m

Conventional Gilts:						
Principal	78,412	71,194	275,187	703,664	-	1,128,457
Coupons	39,653	37,026	93,862	421,443	-	591,984
Index-Linked Gilts:						
Principal	16,237	-	29,586	348,087	-	393,910
Coupons	3,800	3,597	9,986	37,749	-	55,132
Total Gilts	138,102	111,817	408,621	1,510,943	-	2,169,483
National Savings and Investments	146,871	-	-	-	69	146,940
IMF	17,946	-	-	-	-	17,946
Treasury Bills For FLS	75,186	-	-	-	-	75,186
Temporary Deposits	8,388	-	-	-	-	8,388
Other debt payable	36,638	4	202	-	-	36,844
	423,131	111,821	408,823	1,510,943	69	2,454,787

The cash flow analysis after five years is:

	5-10 years	10-20 years	20-30 years	30-40 years	Over 40 years	Total
	£m	£m	£m	£m	£m	£m
Conventional Gilts:						
Principal	195,679	183,217	182,564	81,408	60,796	703,664
Coupons	115,478	164,250	90,445	37,712	13,558	421,443
Index-Linked Gilts:						
Principal	65,145	97,158	79,555	60,017	46,212	348,087
Coupons	12,571	15,280	6,306	3,048	544	37,749
	388,873	459,905	358,870	182,185	121,110	1,510,943

Credit risk

The NLF makes loans to UK public corporations and central government entities, advances to other UK central Exchequer Funds and subscribes to the IMF. The NLF also lends to the IMF. As a result, the NLF is not exposed to significant credit risk. Details of this can be found in notes 6, 7 and 9. Total loans and advances stand at £178,059 million (2016-17: £212,701 million) and gross IMF exposure stands at £21,883 million (2016-17: £23,223 million).

In respect of loans financed by the NLF, the financial relationship with the borrower is managed by the department responsible for the relevant public corporation. The sponsoring department performs due diligence on the borrower and proposes the loan. The Treasury reviews the proposal and, if the proposal is approved, the NLF will make the loan. The NLF is not allowed to accept losses on its loans. Any such losses can only be written off by primary legislation; however, in 1990 the Treasury gave an undertaking to the Public Accounts Committee that it would not seek Parliament's approval to such a course except as part of a reconstruction of the borrower's finances prior to privatisation. In other cases, the Treasury would look to the borrower's sponsor department to cover any losses from its resource account.

In the case of advances to the PWLB for loans to Local Authorities, the PWLB manages the financial relationship with the borrower though the credit risk is borne by the NLF.

In the context of NLF loans issued to trading organisations at market rates, under the Treasury's Commercial Lending policy, the terms and interest rates are designed to reflect the terms on which a private sector lender, such as a commercial bank would lend to the borrower if the borrower were a wholly private sector body rather than a government body.

Ceilings on total lending from the NLF to specific bodies are prescribed in the statutes governing each loan. The PWLB is allowed to lend up to an aggregate amount of £95 billion (2016-17: £70 billion). For short-term lending to public bodies, the maximum exposure of the NLF is determined by prescribed credit ceilings appropriate for the circumstances of the body.

The IMF maintains precautionary balances (comprising retained earnings) as prudential cover in order to ensure the continued security and liquidity of its members' claims. Other factors that help safeguard the Fund's resources include the conditionality associated with lending by the IMF and the IMF's status as a creditor with preferential right to receive payment.

None of the NLF's financial assets are past due or impaired.

Derivatives and hedging

The NLF itself does not use derivatives or undertake hedging. However some of the risks on the NLF are offset by the activities of the EEA. The Exchange Equalisation Account Act 1979 constrains how the EEA may borrow from outside government. Where the EEA's foreign currency reserves are financed by foreign currency borrowing, the debt is issued by and is an obligation of the NLF. The foreign currency raised is sold by the NLF to the EEA for sterling. While the NLF remains exposed to the interest and exchange rate risks from the foreign currency debt it has issued, in practice these risks are offset through the EEA's programme of asset management and swaps. There was no foreign currency debt outstanding in the NLF at 31 March 2018 as the 3 billion Renminbi bond matured in October 2017 (£349.0 million principal amount outstanding excluding accrued interest as at 31 March 2017. See note 12 for total outstanding including accrued interest at 31 March 2017).

16 Related Parties

The Treasury is the ultimate controlling party of the NLF. There have been no direct transactions between the Treasury and the NLF in 2017-18. As at 31 March 2018 £200 million proceeds of debt issuance from Treasury Group is deposited with the NLF.

The main related parties of the NLF are the CF, DMA, EEA, PWLB, Bank of England and NS&I. The relationship between the NLF and CF is explained in the Overview within the Performance report. The NLF has provided finance in the year to the DMA, EEA, PWLB and to various statutory public sector bodies. The NLF has also transacted with the Bank of England and NS&I. Transactions with these bodies are all disclosed in these accounts. The NLF has also had a significant number of transactions with other government bodies via its temporary borrowing of balances in various Government Banking bank accounts.

During the year, there have been no transactions between key management personnel at the Treasury and the NLF.

17 Events after the Reporting Period

There are no events after the reporting period to report.

18 Date of Authorisation for Issue of Account

The Accounting Officer authorised these financial statements for issue on 13 July 2018.

HM Treasury contacts

This document can be downloaded from www.gov.uk

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