HM Treasury, 1 Horse Guards Road, London, SW1A 2HQ

Andrew Bailey
Governor
Bank of England
Threadneedle Street
London
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17 September 2026

Dear Andrew,

Asset Purchase Facility

Thank you for your letter of 17 September 2026, setting out the changes announced by the Bank of England that relate to the Asset Purchase Facility's (APF) stock of purchased assets, and for the progress made over the course of the year by officials from the Bank and HM Treasury to review the Bank executive's implementation of QT, to ensure it continues to maximise value for money by minimising cost and risk over the lifetime of the APF, continues to support gilt market functioning and predictability of sales, whilst continuing to align with the Monetary Policy Committee's (MPC) QT principles.

The APF has been authorised by my predecessors to hold assets, primarily for monetary policy purposes. In addition, and as set out below, I am today authorising a segregated portfolio of APF gilts to be held for non-monetary policy purposes. Under the terms of the existing APF indemnity, HM Treasury will continue to indemnify the Bank and the Bank of England Asset Purchase Facility Fund (BEAPFF), so that any gains or losses arising out of, or in connection with, the APF, including in relation to this segregated portfolio of APF gilts, are borne by HM Treasury.

The MPC's multi-year path for QT

I acknowledge the decision taken by the MPC to unwind the APF through an annual sales pace of £20bn in purchase proceeds terms until gilts held for monetary policy purposes are fully unwound by the end of 2034. Taking the maturity profile into account, this is equivalent to an average annual stock reduction of £46bn. The MPC has statutory independence to set monetary policy to pursue its objectives, as set out in law and specified by the government. I would like to reiterate that the separation of fiscal and monetary policy is a key feature of the UK's economic framework and is essential for the effective delivery of monetary policy. I welcome that the APF continues to be unwound in a way that maximises value for money by minimising cost and risk over the lifetime of the APF, subject to achieving the MPC's objectives.

Unwind of the APF is an important aspect of the future design of the Bank of England's balance sheet, and the Treasury continues to engage with the Bank on these issues. As you and Bank officials have set out in several speeches, the Bank's plans for a demand-driven operating framework for reserves backed by repo and the transition away from gilts held in the APF, will further reduce the public sector's interest rate risk exposure. Dependent on the evolution of demand for reserves and the design of the Bank's repo facilities, the transition to repo is expected to generate income for the Bank and broader public sector. The Treasury and the Bank will continue to engage to understand both the short- and long- term implications arising from balance sheet transition, via existing governance and information sharing channels set out in the Financial Relationship MoU.

The Bank Executive's strategy for backing banknotes

Thank you for providing detail in your letter on the Bank Executive's strategy for backing current and future banknote issuance. The Bank is legally required to ensure notes in circulation have sufficient backing assets. Currently, the Issue Department holds a deposit with the Banking Department as part of the assets backing the notes liability. The Banking Department in turn holds assets against that deposit, which are ultimately backed by the gilts held within the APF. As a result, the APF gilts indirectly back notes. This means that absent any changes, as the APF's monetary policy holdings wind down toward zero, the current arrangement would no longer work. As you note, the Bank Executive judges that gilts remain the appropriate asset to back such liabilities.

Given that the APF already holds gilts, and that the MPC intends to run its portfolio of APF gilts held for monetary policy purposes to zero, I agree that it is appropriate for the Bank Executive to set aside and retain a portion of the APF's existing holdings to reflect anticipated banknotes in circulation. This will avoid incurring the unnecessary cost and risk of buying gilts for note-backing purposes at the same time as selling gilts as part of QT, which is the best outcome for the taxpayer. I also note that this arrangement formalises the existing balance sheet arrangement, and welcome that this avoids crystallising the upfront costs associated with transferring the gilts across the Bank's own balance sheet. £120bn of the longest-dated gilts will therefore no longer be held for monetary policy purposes and so will not be unwound as part of QT. Additional gilts that are needed to back banknotes once those in the APF mature will be purchased by the Bank Executive from the secondary market directly onto the Issue Department.

I am writing to agree to these proposed changes. Setting these long-dated gilts aside for indirect note-backing maintains an orderly transition as the APF winds down, ensuring continuity in the assets held within the existing note-backing framework and delivering value for money for the taxpayer.

The implementation of QT

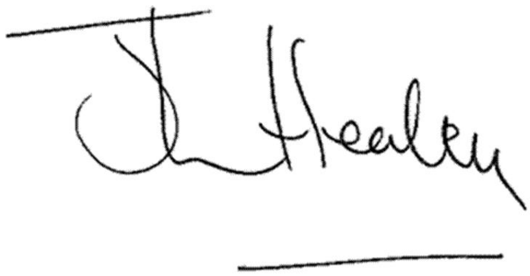
As you note in your letter, officials have been developing a model whereby all APF active gilt sales are conducted to the government and not to the market. HM Treasury would instruct the DMO via the Debt Management Account to purchase the APF gilts that the Bank Executive is selling in its implementation of the MPC's multi-year plan. Sales would be conducted at market prices and in a pre-defined manner, pre-announced by the Bank Executive, with the remaining gilts continuing to be held by the APF to maturity. The DMO would subsequently on-sell the gilts to the National Loans Fund for cancellation. The indemnity arrangements between HM Treasury and the Bank would continue unchanged. HM Treasury would in due course instruct the DMO to issue a corresponding amount of debt to finance such APF purchases through the annual financing remit.

This sales model, whilst leaving the overall supply of gilts to the market from the public sector unchanged, would see a return to a single public sector supplier of gilts to the market. Such an arrangement, along with the MPC's multi-year path of QT and the confirmation that the longest-dated APF gilts will be held in the APF to indirectly back banknotes, would also support the principle of predictability, whilst continuing to uphold the independence of the MPC.

We will review progress before April 2027 such that, subject to a final decision to proceed, implementation could begin in a way that allows this to be incorporated into the DMO's annual financing remit, as set by HMT. Further operational details would be announced in due course. Regardless of the final decision, the Bank will be announcing by April 2027 the operational details through which it will be implementing the MPC's multi-year plan.

I am copying this letter to the chairs of the Treasury Committee and the Public Accounts Committee and depositing it in the libraries of both Houses of Parliament and on the HM Treasury website.

Yours ever,



RT HON JOHN HEALEY MP
Chancellor of the Exchequer