United Kingdom
Debt Management
Office

The role of inflation-linked bonds - UK experience

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Index-linked gilt issuance – rationale

- The UK Government first issued index-linked (IL) gilts in 1981. It was the first G7 country to do so

Original rationale for issuing government bonds linked to inflation

- ✓ Reinforce the UK Government's anti-inflationary credibility
- ✓ Increase the flexibility of the issuer, allowing the Government to borrow even in times of high inflation uncertainty without the need to raise nominal interest rates
- ✓ Reduce debt servicing costs – it was anticipated that investors would accept a lower real return in exchange for inflation protection
- ✓ Benefit the pensions industry – providing additional flexibility in tailoring the benefits on offer

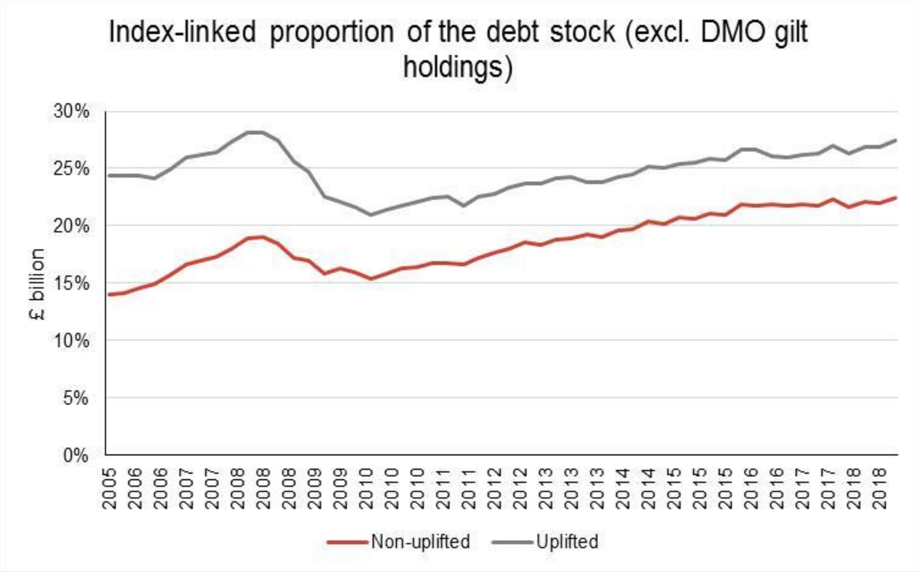
HM Treasury, Economic Progress Report, May 1981

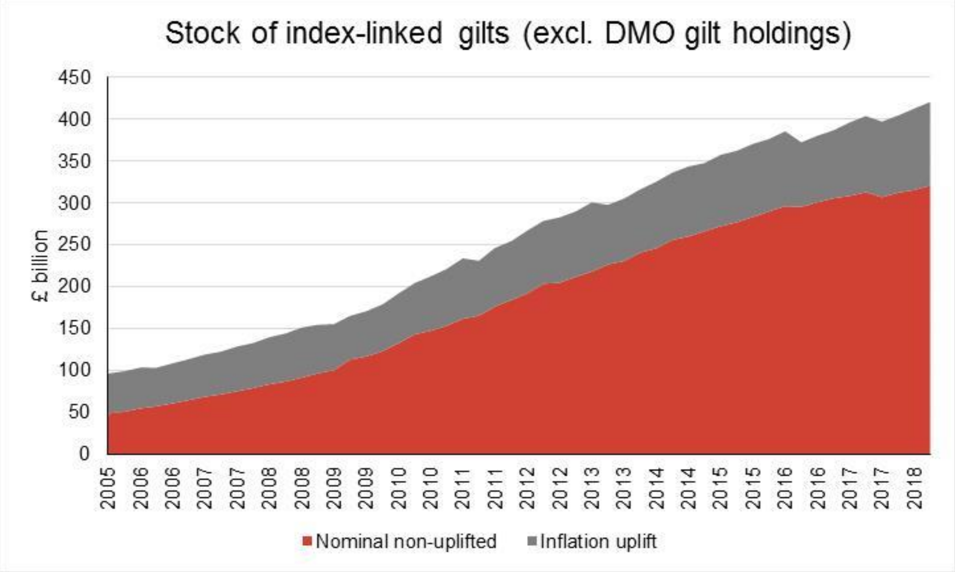
- Both the principal and interest payments are linked to the Retail Prices Index (RPI)

Index-linked gilts and the investor base

- Strong domestic demand for RPI-linked gilts especially from a major part of the pension fund industry where RPI indexation remains widespread
- Pension fund demand tends to be at the long-end of the real yield curve (20-year maturity and longer)
- Index-linked gilt issuance results in cost-effective financing in accordance with the debt management objective
- Contractual commitment to make RPI-linked payments as long as the RPI continues to be published
- No current plans to issue gilts linked to any other prices index

Proportion and stock of IL gilts since 2005

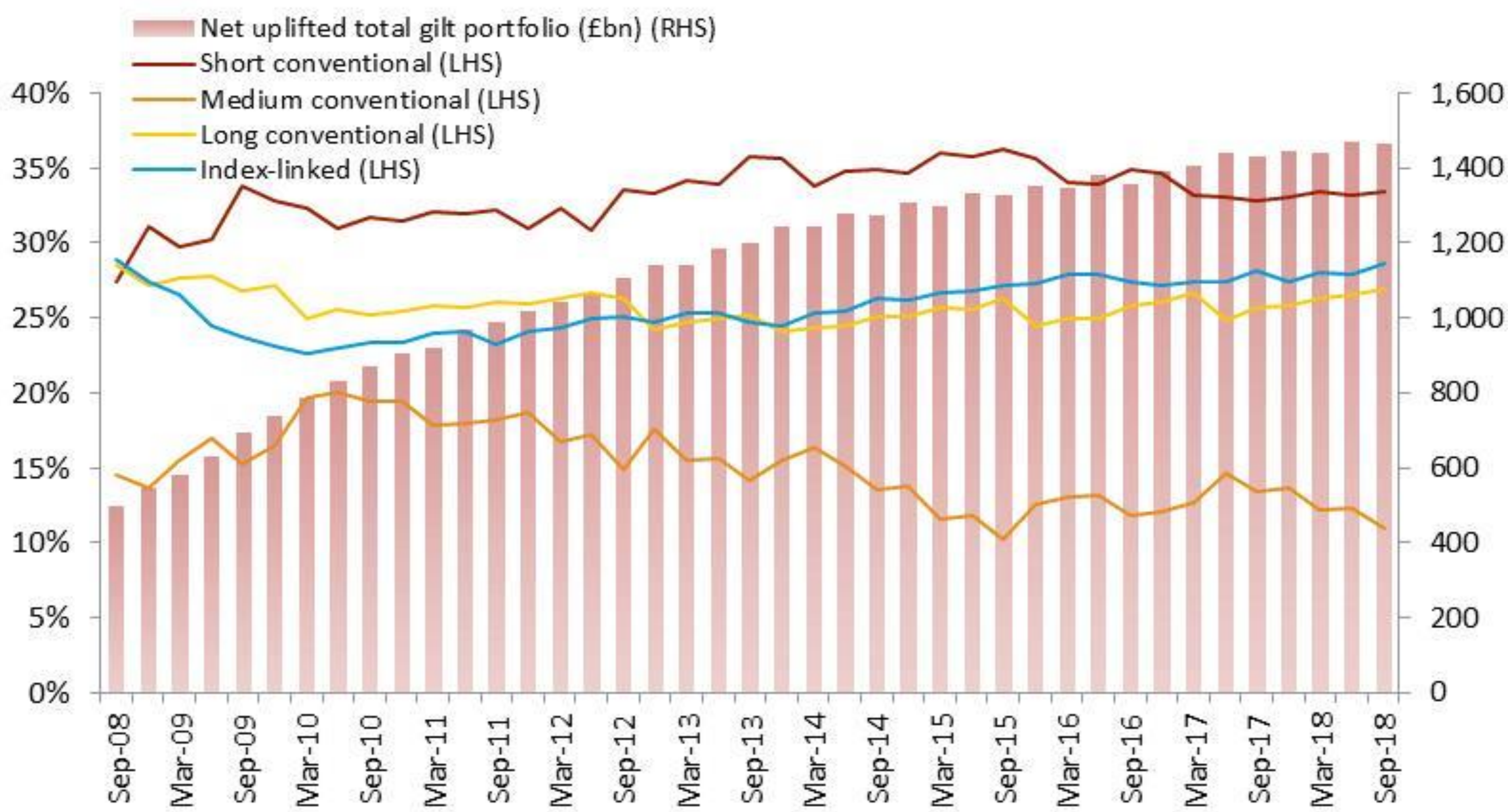




- At 27.5%, the UK has the highest proportion of IL debt of any major economy
- As at end-September 2018, the uplifted nominal amount of IL gilts was £420bn

Source: DMO
Data at end September 2018

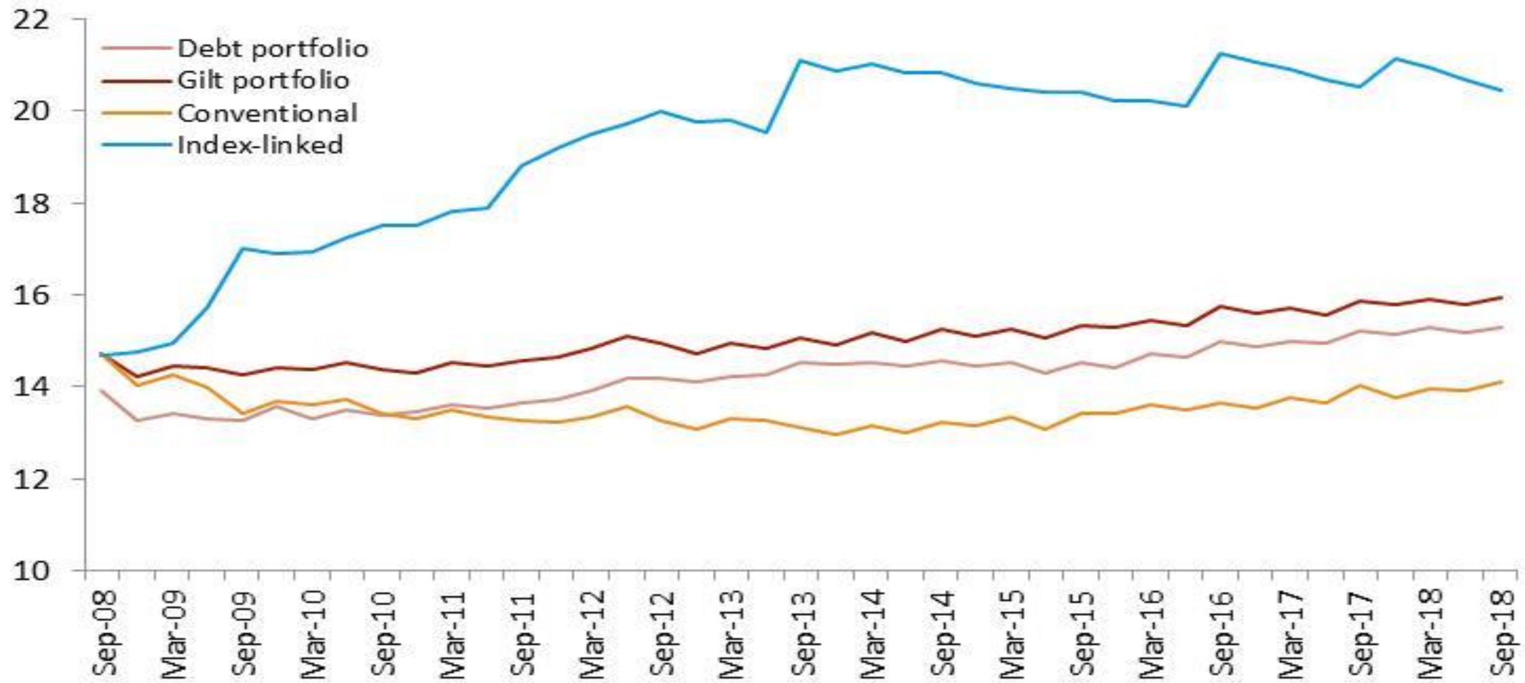
Gilt portfolio composition since September 2008: The stock of index-linked gilts has increased over time



Source: DMO
Data at end September 2018

Gilt portfolio average maturity since 2008: Average maturity of the index-linked portfolio has increased over time

- 30 ILGs currently in issue (2019 to 2068 maturity range)



Source: DMO
Data at end September 2018

Gilt market turnover since September 2008 (13-week moving average)

Source: DMO
Data at end September 2018

Index-linked gilt issuance and the Government's inflation exposure in its debt portfolio

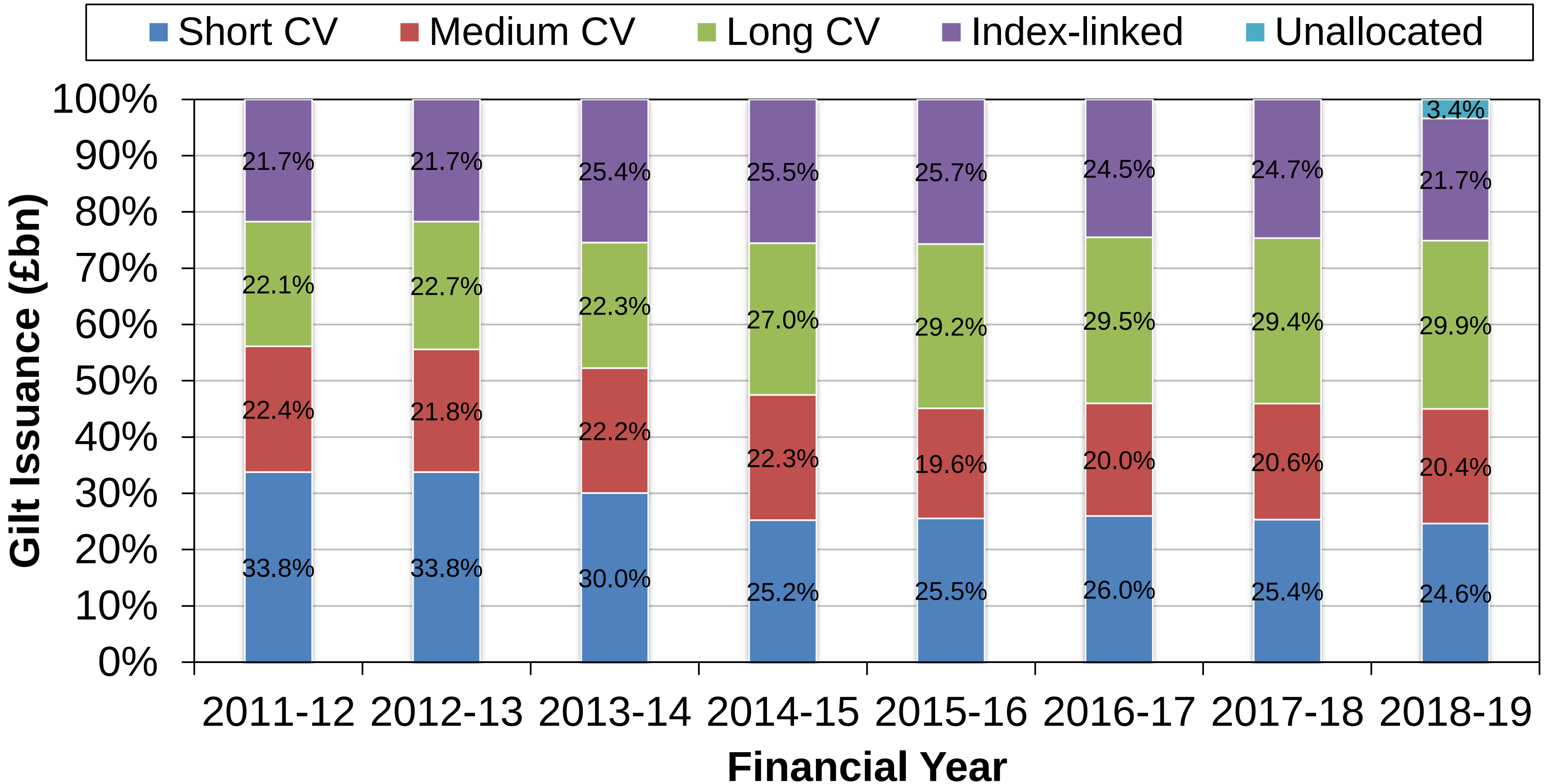
- The UK Government is aware that the significant volume of index-linked issuance in recent years has consequences for the long-term inflation exposure in the public finances

- Possible reduction in the level of maturity of demand for ILGs in future years – due to closure of defined benefit pension schemes to new members and contributions

- The UK Government is now considering the appropriate level of index-linked debt in the total debt portfolio in coming years

- Reflecting these considerations in 2018-19, the financing remit published in March 2018 reduced index-linked issuance by 2 percentage points relative to the 2017-18 initial plan

Spring Statement 2018 - reduction in initial IL gilt issuance by 2 percentage points



Source: DMO
Data at 10 October 2018

Further information

DMO website	www.dmo.gov.uk
HM Treasury website	www.gov.uk/hm-treasury
Reuters	DMO/INDEX
Bloomberg	DMO <GO>

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