RESPONSE OF THE BANK OF ENGLAND TO THE THREE COURT-COMMISSIONED REVIEWS

Presented to the Court of the Bank of England

March 2013

Response of the Bank of England to the Three Court-Commissioned Reviews

1. In May 2012, the Court of the Bank of England commissioned a set of three Reviews into areas of the Bank's performance and existing capabilities. Each Review was led by an independent, internationally respected expert. The Reviews were published in November 2012.

2. The three Reviews covered:

   - The provision of Emergency Liquidity Assistance in 2008/9.
   - The Bank's framework for providing liquidity to the banking system as a whole.
   - The Monetary Policy Committee's forecasting capability.

3. This document sets out the proposed response of the Bank's Executive to each of the 71 recommendations or options and suggestions for change made in the three reviews. That response, which has been endorsed by the Court of the Bank, is very positive. Having consulted, where appropriate, the Court, the Monetary Policy Committee and the Financial Policy Committee, the Bank is minded to take forward almost all of them.

4. Even though, overall, the Reviews did not find the Bank's frameworks and processes to be at fault, they did identify a range of potential improvements, some of them modest, others more fundamental and far-reaching. The result of the proposed changes will include: an enhanced readiness for future provision of Emergency Liquidity Assistance; changes to the Sterling Monetary Framework in respect of providing liquidity insurance to the banking system; and a new forecast process that includes more consideration of alternative policy options and greater transparency.

5. This document provides a summary of the proposed changes to be made in response to each of the three reviews and detailed tables describing the responses to each of the 71 specific recommendations or options. The response to each is categorised into one of the following four groups: (1) The Bank has already implemented or will implement the recommendation forthwith; (2) The Bank intends to implement, but to do so will require further planning; (3) Before implementing, further analysis is required to assess the merits and drawbacks of the recommendation; (4) The Bank does not intend to implement the recommendation.

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Plenderleith Review of Emergency Liquidity Assistance in 2008/9

1. The remit of the Plenderleith Review was to examine how the Bank discharged its responsibilities as Lender of Last Resort in 2008-9 and to make recommendations for the conduct of Emergency Liquidity Assistance operations (ELA) in the future. Specifically, the Review examined: (a) the basis of the Bank's decisions to provide ELA; (b) governance arrangements for making those decisions; (c) the structure and terms of each ELA operation; (d) the effects of ELA on its recipients and on overall financial stability; and (e) the capability of the Bank to plan, implement and manage ELA operations. The report covered the 2008-9 ELA operations for HBOS and RBS but not for Northern Rock (2007), which was covered in the Treasury Select Committee's report *The run on the Rock.*[1]

2. The overall assessment of the Review was positive, commending the manner in which ELA was conducted and noting the improvements made to the ELA framework and preparedness since 2008-9. Plenderleith wrote, "*the Bank has built on its experience of 2008 and is as fully prepared as could reasonably be expected*", and that there has been a "*significant enhancement of the authorities' ability to scan the horizon for impending financial stresses*" since 2008.

3. Nevertheless, the Review raised 28 recommendations in relation to ELA. A number of the recommendations were aimed at **improving processes**; others emphasised the need to ensure that the Bank's **collateral management** capabilities evolve in line with changes in the structure of commercial banks' balance sheets. The Bank will implement almost all of these.

4. Over and above this, Plenderleith emphasised the challenges that any institution would face in **maintaining the heightened level of readiness and horizon scanning** for rare and high impact events which the Bank has developed over the course of the financial crisis. He recommended that the Bank takes steps to ensure that it mitigates the risk that this capacity will erode over time. In response to the Review, the Bank is reflecting on what additional

[1] The House of Commons Treasury Committee's report, *The run on the Rock*, Fifth Report of Session 2007–08, HC56-I, January 2008, available at http://www.publications.parliament.uk/pa/cm200708/cmselect/cmtreasy/56/56i.pdf.

steps or processes it should put in place to manage this risk, especially when calmer financial conditions return.

Summary of responses to Plenderleith Review

Category descriptions: **1)** Implemented or implemented forthwith; **2)** Intend to implement but will require further planning; **3)** Further analysis is required to assess the merits and drawbacks of the recommendation; **4)** Do not intend to implement, with reasons explaining the difference of view.

No.	Recommendation	Category	Next steps
	HORIZON SCANNING AND PLANNING FOR EMERGENCY LIQUIDITY ASISTANCE (ELA)		
1	In situations where the Bank is aware of a bank experiencing escalating liquidity strains, the Bank could consider whether it might act pre-emptively to provide bilateral liquidity support before the need definitively crystallises.	2 (2013 H2)	The Discount Window Facility (DWF) is the most likely mechanism to address this issue of earlier access to liquidity provision. The Bank will also ensure that it can provide pre-emptive liquidity support when appropriate.
2	It will be important that the Bank continues to develop and monitor processes to enable sufficient and intelligent filtering of the formidable amount of raw data and information now being collected and analysed within the Bank, such that senior staff receive timely notification of key developments, without being overwhelmed with data and analysis.	2 (2013 H2)	Agreed. A review will be undertaken to identify whether there is more that could helpfully be done in this regard.
3	It will be important for the Bank to maintain its strengthened capacity to scan the horizon for impending financial stresses even when financial conditions return to relative calm. It will be a challenge not to allow the functions within the Bank that have been built up as a response to the crisis to deteriorate when the immediate need for them is less intense.	2 (2013 H2)	Agreed. The implementation of statutory changes to the regulatory architecture will help to ensure that advances in the Bank's ability to horizon-scan are not lost. A specific review of horizon-scanning will be undertaken. In addition, to guard against this risk, Court will receive periodic reports on the issue.

No.	Recommendation	Category	Next steps
4	The Bank needs to be able to identify impending systemic shocks emanating from, or impacting on, non-bank financial institutions.	2 (2013 H2)	Agreed. The Financial Policy Committee will have a statutory responsibility for monitoring systemic risks, including those emanating from outside the scope of microprudential supervision. The horizon-scanning review (see recommendation 3 above) will also cover this finding.
5	The Bank's foreign currency swap lines with overseas central banks are currently due to be renewed on 1 February 2013. It would be a sensible contingency for the Bank to maintain these swap lines in case of need.	1	Agreed. The existing swap lines have been extended for a further year.
6	The Bank should continue to explore the options of funding the provision of foreign currency ELA through swaps undertaken in the market, or by using the Bank's or Government's foreign exchange reserves, in order to ensure that it is adequately prepared to extend foreign currency ELA if swap lines with other central banks were for some reason not available for that purpose.	2	Contingency plans are being developed and will be revisited annually.
7	Notwithstanding the Bank's improved ability to identify impending financial stresses, some shocks, such as the impact of rogue traders, or events like 9/11, are, by their nature, inherently unforeseeable. The Bank needs to maintain its capacity to manage the consequences of unforeseen, as well as foreseeable, events.	2 (2013 H2)	Agreed. An annual internal test of ELA will be introduced to assess the Bank's capacity to manage shocks.
8	The Bank should consider what expertise—for example in risk management and collateral valuation—it needs to have in-house for crisis scenarios if it is unlikely to be able to call on external expertise, either because an operation needs to be implemented at short notice or because the Bank has concerns about secrecy.	2 (2013 H2)	Agreed. In-house expertise available to manage collateral risk has been increased. A further review will be undertaken, following the first annual test of ELA processes planned in response to recommendation 7 (see recommendation 9 of the Winters Review).

No.	Recommendation	Category	Next steps
9	In some instances the Bank's normal external legal advisers may not be able to be used because they are already representing the counterparty to which ELA is being extended. The Bank is aware of this possibility and should continue to make contingency plans for engaging alternative legal advisers if needed.	1	Agreed. The Legal Directorate is alert to the issue and has contingency plans.
	LENDING DECISIONS AND TERMS		
10	It will be important to ensure that the more structured framework which is now in place for assessing whether the criteria are met for extending ELA can be made to work effectively in practice, so that the Bank, including in future the Prudential Regulation Authority, can marshal information internally in an efficient manner and, in conjunction with HMT, reach and implement decisions on whether or not to extend ELA without delay.	1	Agreed. The *Memorandum of Understanding on Crisis Management* between the Bank and HM Treasury will come into force on 1 April when the Prudential Regulation Authority becomes part of the Bank. The Memorandum specifies the decision-making responsibilities to advance ELA.
11	The Bank may need to give more detailed consideration to how it would accept, value and determine appropriate haircuts for collateral outside that eligible in operations within its published framework. As a consequence, the Bank will need to ensure that its risk management function continues to develop in response to the evolving balance sheets of banks.	2 (2013 H2)	The Bank will ensure that its collateral risk management function evolves over time in response to the changing composition of balance sheets of financial institutions. Regular monitoring of assets on the balance sheets of Sterling Monetary Framework (SMF) eligible institutions will be undertaken in response to a recommendation of the Winters Review.
12	The task of managing and realising collateral, particularly portfolios of unsecuritised loans, in the event that an ELA recipient defaulted would be a formidable administrative challenge. The Bank needs to have a fully developed plan to manage this process.	2 (2013 H2)	Agreed. A project to determine what actions would be necessary to risk-manage certain types of collateral has been initiated and an implementation plan will be prepared (see recommendation 9 of the Winters Review).

No.	Recommendation	Category	Next steps
13	In any future ELA, the Bank as both lender and the supervisory authority will need to be closely involved in monitoring the progress of the ELA recipient in returning to a more liquid position and in repaying the outstanding ELA. The Bank should consider what monitoring might be necessary in future and how legal agreements should be structured to ensure that the banks in receipt of ELA are obliged to facilitate that monitoring.	2 (2013 H2)	Agreed. The Bank will consider what can be done in addition to its existing arrangements.
14	Since ELA operations require authorisation by the Chancellor, it would in principle be logical for the Bank to seek an indemnity from HMT for the full amount of ELA from the outset of any operation.	2 (2013 H1)	Agreed.
	GOVERNANCE AND DECISION MAKING		
15	In view of the scale of risk to which the Bank's balance sheet may be exposed by any ELA lending, a more structured process of reporting on the progress of ELA operations by the Executive to the relevant committee of the Bank's Court of Directors might assist that committee in discharging its oversight responsibilities—for example, a daily teleconference and weekly monitoring reports, covering in particular the risk management policies being put in place by the Bank to manage the increased exposure.	2 (2013 H1)	Agreed. A reporting structure will be agreed with Court.
16	It is recommended that the Bank's formal statement, approved by Court, setting out how Court operates, *Governance of the Bank Including Matters Reserved to Court,* be reviewed to specify more clearly and precisely Court's role as regards the Bank's balance sheet and its financial risk exposure.	1	Agreed. *Matters Reserved to Court* is being updated to reflect this recommendation.

No.	Recommendation	Category	Next steps
17	It is appropriate, given the need for meetings to be called at short notice in a crisis and the need to maintain secrecy, for the requirement to consult Court about ELA to be fulfilled by a smaller group of Non-Executives. Any sub-committee constituted for this purpose should, however, have substantial representation of non-conflicted Non-Executive Directors.	1	Agreed. Terms of reference for sub-committees of Court will reflect this recommendation.
18	In order to minimise the scope for confusion, it might be logical to manage any future ELA from the Markets Directorate, particularly if any future ELA is likely to be similar in mechanism to the Discount Window Facility, which is managed within that Directorate. Equally, other management structures would be possible and it is recommended that the Bank reviews whether the present dispersion of responsibilities remains appropriate in light of the significant extension in recent years of its framework for liquidity insurance.	4	The organisational structure of the Bank needs to support the effective provision of ELA. The most important aspect – that risk management should be undertaken in the Markets Directorate where there is relevant specialist expertise – already applies. The Bank will, however, keep these structures under review.
19	Separation at the Divisional level of the responsibility for initiation, risk management and settlement of any ELA between front, middle and back office is an appropriate step to strengthen risk management safeguards.	1	Agreed.
20	The current reporting lines of the Markets and Banking Services Directorates to their respective Deputy Governors may leave scope for uncertainty. A more structured approach of each Directorate reporting to the relevant Deputy Governor for the latter's area of responsibility could be considered. The structure of responsibilities might appropriately be addressed when the third Deputy Governor, responsible for the Prudential Regulation Authority, joins the Bank.	4	In practice Executive Directors currently liaise closely with both Deputy Governors and report to the relevant Deputy Governor. The Bank will keep these structures under review.

No.	Recommendation	Category	Next steps
21	Consideration will need to be given to what role the new Financial Policy Committee, which will have a statutory responsibility for monitoring systemic risk and initiating policy actions in that area, would appropriately play in establishing the framework within which ELA decisions would be made.	1	The FPC, with its objective of financial stability, has a limited role in relation to decisions on ELA to individual firms. The Governors will ensure that the FPC is informed about any matters relevant to its functions and decisions on the system as a whole. A protocol for this has been agreed between the Executive and the FPC.
	DISCLOSURE		
22	The Bank still publishes the weekly Bank Return, despite no longer being required to, following the enactment of the Banking Act 2009. It should consider ceasing to do so at an appropriate time, in order to improve its ability to provide covert liquidity assistance in future.	3 (2014 H1)	Further analysis is required. The Bank agrees with the objective of this recommendation that it should not inadvertently disclose a covert ELA operation.
23	It is important that remaining uncertainties in some areas of the legal and regulatory framework for disclosure are resolved so that to the extent possible the standard requirements for disclosure do not, in a crisis, counterproductively compromise the wider public interest in financial stability.	2 (2013 H1)	The Bank is engaging with relevant external parties to seek to minimise risks to its operations being disclosed when that would be counterproductive for stability.
24	It would be helpful, in terms of enabling ELA to be undertaken covertly, if there were fuller implementation of the regulatory rule requiring banks periodically to realise a proportion of their liquid assets through repo or outright sale in the market, such that banks undertook this periodic realisation on sufficient scale to provide a degree of cover for any ELA support extended by the Bank.	2	Agreed.
25	It would be appropriate for a process of quarterly review on the timing of disclosure to be followed within the Bank in relation to any ELA that is not indemnified by HMT.	1	Agreed. A quarterly review will be undertaken.

No.	Recommendation	Category	Next steps
	FUTURE ELA AND LOLR FUNCTION		
26	It will be important for the Bank to have the capacity, if necessary, to extend ELA to non-banks if strains on one or more were to precipitate a threat to systemic stability.	1	Agreed. There are no legal impediments to the Bank's ability to advance liquidity assistance to non-bank financial institutions, if warranted.
27	Given the fundamental changes in the nature of the Bank's lender of last resort function since 2008, it may be appropriate at some stage for the Bank to set out the principles under which it would contemplate activating this function in its widest sense, particularly in light of the greatly enhanced regulatory and statutory frameworks within which the financial system now operates.	2 (2014 H2)	The Bank will set out its policies once the remaining questions of principle raised by the Winters and Plenderleith Reviews have been resolved.
28	Some increase in the size of the Bank's capital may be appropriate, to enable the Bank to play an effective role in a financial crisis, where this can be done without public funds being put at risk, as envisaged in the draft Memorandum of Understanding on Crisis Management.	3 (2014 H1)	The amount of capital on the Bank's balance sheet is ultimately a matter for the Government as sole shareholder. The Bank will consider the issues in the light of changes to its operations generated by these Reviews and, if necessary, consult HM Treasury.

Winters Review of the Bank's Framework for Providing Liquidity to the Banking System

1. The Winters Review concluded that the Sterling Monetary Framework (SMF) had been consistently improved and functioned properly; the Bank had been responsive to changing conditions and the SMF was robust and broadly fit for purpose. It also identified in its recommendations a number of detailed aspects of the framework where further changes could be considered. In some cases, the issues raised were very substantial and were about what central banks should or should not do.

2. In most of the recommendations, the Review questioned whether the Bank should widen access to the SMF across a range of dimensions: price; collateral; maturity; and eligibility of firms. This in turn raises questions about moral hazard and the appropriate degree of official support for commercial institutions. Several of the recommendations are straightforward to accept and to implement, but some of the more complex issues go to the heart of central banking and, before any conclusions can be reached, need more thorough analysis and reflection.

2. Those recommendations which are broadly accepted can be divided into five work streams, each with some concrete deliverables in the first half of 2013:

3. **Mitigating stigma (recommendations 3–6).** The Review devotes considerable attention to how to mitigate perceptions of stigma in central bank facilities. The work programme will involve identifying the sources of stigma and identifying policy initiatives.

4. **Merger of Indexed Long-Term Repo (ILTR) and Extended Collateral Term Repo (ECTR) (recommendations 7, 8).** By the end of March 2013 the staff will have begun to identify practical options for regularising an ECTR-like operation while retaining the ability to respond to market-wide shocks outside the Bank's regular operations. Decisions on pricing will overlap somewhat with the work on stigma. Delivery of the chosen option will entail market consultation and systems development.

5. **Extending SMF access within banking groups (part of recommendation 11).** The statutory implementation of the 'ringfencing' recommendations of the Independent Commission on Banking will require a relaxation of the current policy of limiting the holding of a reserves account to a single entity within a banking group. During 2013 Q1 we will assess the case

for further relaxing this rule, identifying governing principles, and practical implementation.

6. **Collateral eligibility (part of recommendation 9).** The Bank accepts the principle of accepting as Discount Window Facility (DWF)-level collateral all assets that play a material role in supporting provision of core financial services to the UK real economy by SMF-eligible firms. Assuming that any obstacles to extending eligibility can be overcome, the Bank will design and implement a risk management framework for such collateral in 2013 H2. Over the longer term the Bank will continue to monitor the balance sheets of commercial banks and review its collateral eligibility framework in response.

7. **Governance (recommendations 15–22).** New governance arrangements setting out a framework for engagement between the Bank's Executive and both the MPC and FPC with regard to the Bank's SMF have been agreed. The possible shape of a process for an annual review by external stakeholders is also under consideration. Processes to clarify internal governance arrangements have been agreed and implemented where possible since the Review was published. For example, a new Operations Committee, chaired by a Deputy Governor, has been established. All of these structures will be subject to periodic review by Court.

8. Longer-term work in the following three areas will begin in the second half of 2013:

9. **Non-bank membership of SMF (part of recommendation 11).** Although the Bank agrees that it should have the capacity, if warranted, to extend ELA to individual non-bank institutions (see Plenderleith recommendation 26), it is not agreed that membership should be extensively widened in general. The Bank plans to assess the evolution of bank/non-bank financing to understand how the provision of finance to the economy is changing. It also plans to identify the main activities of different parts of the shadow banking system – and the extent to which they overlap with the three key banking services that Winters discusses in his Review, namely intermediation between savers and borrowers, providing payment services, and providing risk management services.

10. **Market maker of last resort (recommendation 12) and maturity transformation (recommendation 10).** These are the furthest removed from the the role of a central bank in normal conditions. While such operations can be desirable in particular circumstances – as demonstrated by the Bank acting as a backstop market maker in corporate bonds in 2009 – the expectation that a central bank will perform them can

create distortions in markets during normal times. The principles guiding such roles need therefore to be considered carefully.

Summary of responses to Winters Review

Category descriptions: **1)** Implemented or implemented forthwith; **2)** Intend to implement but will require further planning.; **3)** Further analysis is required to assess the merits and drawbacks of the recommendation; **4)** Do not intend to implement, with reasons explaining the difference of view.

No.	Recommendation	Category	Next steps
	MONETARY POLICY AND RESERVES		
1	The Bank should consider returning to a reserves averaging approach in future, but this is not critical. As monetary policy is normalised, Court should ensure the Executive evaluates the relevant factors in deciding whether to move away from the current floor regime.	2	Agreed. A return to reserves averaging is planned. But this will be reviewed when market prices suggest a rise in Bank Rate is expected in the near-term.
2	If the Bank decides to return to reserves averaging, it should maintain a system of voluntary reserves setting, that places a burden on the banks to assess the level of reserves required for the proper functioning of the payments and other interbank systems.	2	Agreed. If there is a return to reserves averaging.
11b	The Bank should also specifically consider whether the restriction of only one legal entity per group accessing the full range of Sterling Monetary Framework (SMF) facilities is reasonable. This will be particularly relevant in future in the case of non-ring fenced banks.	2	During 2013 Q1, the Bank will evaluate the case for changing this rule. It is already clear that the statutory implementation of the Independent Commission on Banking report is likely to require a change.
	LIQUIDITY INSURANCE		
3	The Bank should consider changes to its Discount Window Facility (DWF) to make it more accessible to banks. This could include: removing the on-the-day conditions to borrowing in favour of continuous assessment; increasing the certainty of available funds; and reducing pricing. In particular, the Bank should rely less on penal pricing as a means to manage moral hazard.	2	By the end of 2013 Q2, the Bank will: analyse the potential root causes of stigma; gather evidence for the relative importance of each potential cause; and assess the effectiveness of the possible reforms to the SMF in addressing those causes, including a review of pricing.

No.	Recommendation	Category	Next steps
4	The Bank should further consider concrete action to reduce any remaining reluctance of banks to use the DWF. The best way to accomplish this would be to regularise its use so that crisis usage is less visible and, hence, less stigmatised.	3	Any move to regularising use would depend on the results of the workstream under recommendation 3.
5	The Bank should also consider moving to a pricing structure for the DWF that incorporates payment of an upfront premium reflecting the value of the insurance being provided to the banks.	3	See response to recommendation 3 . The Bank will need to align with the work on the Liquidity Coverage Ratio by the Basel Committee on Banking Supervision, and its interaction with facilities of central banks generally.
6	In addition to the above changes, the Bank could consider having a second tier DWF, which would provide liquidity against pre-positioned collateral on less generous terms, to deal with cases where the Bank's Risk Management Division had determined that more rigorous monitoring of drawings was necessary.	3	See response to recommendation 3 – whether this is needed depends on decisions to be made on other options and the experience of other central banks that have tried this.
7	The Bank should consider regularising facilities such as the Extended Collateral Term Repo (ECTR) that are currently exceptional. It might do this by combining the ECTR with the Indexed Long-Term Repo (ILTR) Facility to create a regular auction facility allowing banks to access term funding against a wider collateral pool.	2	Agreed. The Bank will begin assessing alternative options during 2013 Q1.
8	There may be merit, nevertheless, in retaining an ECTR-type operation that could be used to respond to a market-wide shock from an external source (e.g. acts of God, disintegration of the Euro zone).	2	Agreed. The operational question is whether to deliver this within the ILTR framework (by adjusting pricing/term) or have a separate facility (as now). To be assessed on same timetable as recommendation 7.

No.	Recommendation	Category	Next steps
9	The Bank should continue to broaden the range of eligible collateral for its DWF and other facilities beyond the substantial portion of bank assets already allowed. Criteria for broader eligibility should focus on the Bank's policy objectives of financial stability and preventing disruptions to payment and settlement services provided to the wider economy, not merely the assets held by banks and, as such, might include allowing drawn revolving credit facilities as eligible collateral.	3	By the end of 2013 Q2, the Bank will establish what obstacles there are to risk-managing collateral taking the form of drawn revolving credit facilities, within the Bank's appetite for financial risk. Depending on whether any obstacles can be overcome, the Bank will implement a framework for such collateral in 2013 H2. The Bank will set up regular surveillance of non-eligible assets held by SMF members to identify candidates for further extensions to eligibility from 2014 onwards.
10	The SMF should be more explicit in its role in providing a maturity transformation backstop in extraordinary situations where banks appear likely to curtail their maturity transformation provision to their customers. In order to accomplish this, the Bank might consider whether it should extend the maturity of some of its current facilities or develop other facilities that would give banks the necessary confidence to maintain or extend the term of credit provision.	3	The explicit purpose of the Bank's liquidity insurance facilities, as set out in its 'Red Book', is to "reduce the cost of disruption to the liquidity and payment services supplied by banks to the UK economy". Its regular ILTR operations have a maturity of 6 months. Changing the permanent facilities to provide longer-term support would be a major change to the role of central banks. This is therefore for longer-term review, starting in 2013 H2. Meanwhile, the Bank already has the ability to introduce temporary facilities with long maturities, as it has through the Funding for Lending Scheme.
11a	The Bank should consider making certain liquidity facilities in the SMF available to non-banks, including for example central counterparties.	3	As with recommendation 10, this would be a major change in central banking and is therefore for longer-term review, starting in 2013 H2.
12	As an extension of the previous recommendations, the Bank should address more directly its role as a market maker of last resort (MMLR). Structural changes to the ways markets operate and the role of banks in markets may call for the Bank to make its MMLR actions more predictable and consistent.	3	The Bank has acted as MMLR in selected markets during the recent crisis and set out some principles for doing so.[2] But making this part of the permanent framework is for longer-term review, starting in 2013 H2.

[2] See Tucker, P (2009) 'Speech at the Bank of Japan 2009 International Conference, Financial System and Monetary Policy: Implementation', Tokyo, 27-28 May 2009, available at http://www.bankofengland.co.uk/publications/Documents/speeches/2009/speech390.pdf.

No.	Recommendation	Category	Next steps
13	The Bank should coordinate policies closely with the Financial Services Authority (FSA) / Prudential Regulation Authority (PRA) and other domestic and international bodies to the greatest extent possible such that policy actions the Bank pursues to encourage acceptance of Bank liquidity facilities are not effectively offset or rendered redundant by the actions of others.	2	Agreed. See response to recommendation 3. The PRA will be part of the Bank making liaison between prudential supervisors and liquidity providers easier than in the past decade or so. The Bank stands ready to escalate issues with other authorities as necessary.
14	As an overarching recommendation, the Bank should avoid constructive ambiguity in its published framework. Specifically, it could provide even greater clarity upfront about the terms on which it would expect to provide liquidity insurance in a range of circumstances.	4	The Bank will make sure that the Sterling Monetary Framework remains one of most transparent regimes globally.
	GOVERNANCE		
15	The formal arrangements around internal governance could usefully be clarified. While the Governor must retain the final say, he should be required to formally seek the views of his Deputies and those Deputies should be required to record any dissenting views. Minutes should be taken and reviewed by Court, although not disclosed for some time. Court should assure that these consultative processes are carried out.	1	Agreed. A new Operations Committee began meeting in February 2013, comprising relevant members of the Executive and chaired by a Deputy Governor. Minutes and papers of this Committee will be made available to Court.
16	The Court should regularly assess the efficiency of decision-making around issues relating to the SMF to ensure that the right issues are raised to senior management for a decision, with a balanced set of views and options, and that appropriate accountability is in place throughout the organisation for decisions taken in the process leading up to this.	2	Agreed. An annual review process will be put in place with the first review during 2014.

No.	Recommendation	Category	Next steps
17	Consideration should be given to the establishment of a regular forum at which the Governors of the Bank meet key stakeholders in the Bank's liquidity operations. For example, the Governors, the Chancellor and/or senior HMT representative and the chair of Court might meet annually to discuss current issues around liquidity provision.	3	The Bank will need different processes for consulting different stakeholders. Options will be discussed in 2013 H1.
18	Some thought should be given to the appropriate level of capital for the Bank.	3 (2014 H1)	The amount of capital on the Bank's balance sheet is ultimately a matter for the Government as sole shareholder. The Bank will consider the issues in the light of changes to its operations generated by these Reviews and, if necessary, consult HM Treasury.
19	The roles of the MPC and the FPC in relation to the design and implementation of the Bank's SMF should be clarified.	1	Agreed. Implemented. Protocols have been agreed with each policy committee and will be reviewed annually.
20	The FPC and the MPC have clear interests in aspects of the Bank's liquidity operations. The Review suggests that it would be useful for the FPC to provide as much clarity as possible to the Executive over its views regarding the Bank's provision of liquidity insurance.	1	Agreed. A governance framework was established under recommendation 19.
21	The MPC should continue to have authority over any operations intended primarily to influence monetary conditions. And it should be informed of the implications for monetary conditions of other liquidity operations, and have the opportunity to express views on such operations if those implications were likely to be material.	1	Agreed. A governance framework was established under recommendation 19.
22	The processes described above will require a high level of communication and cooperation between the Executive, the MPC and the FPC regarding the Bank's liquidity operations. Court should be responsible for ensuring the proper communication and coordination channels are in place.	2	Agreed. An annual review process will be put in place with the first review during 2014.

Stockton Review of the Monetary Policy Committee's Forecasting Capability

1. The Stockton Review considered the forecasting capabilities of the Monetary Policy Committee (MPC), including the adequacy of the discussions and analysis that constitute its forecasting process, and the ways in which the Committee's forecasts are communicated externally. The Review concluded that the forecast process and associated forecasting tools were fundamentally sound. But it also suggested there was scope for improvement, particularly in terms of increasing the transparency with which key features of the MPC's forecasts are communicated to the public and in enhancing the role the forecast process plays in informing the Committee's monetary policy decisions.

2. The MPC has discussed the options identified in the Stockton Review and this response reflects those discussions. There is considerable enthusiasm to take forward many of the options and ideas contained in the Review and the Bank is committed to implementing material changes both to the internal forecast process and to the way in which the forecast (and policy considerations) are communicated externally, primarily through the MPC's quarterly *Inflation Report*.

3. Many of these intended changes are grouped around three broad themes. Some of these improvements will take some time to implement and more details on the individual changes will be provided as the preparatory work develops.

4. **Providing greater transparency about the MPC's forecasts (options 6, 12, 13, 14, 16, 19-21).** The *Inflation Report* will provide greater transparency about the MPC's forecasts. In particular, it will contain more detailed information about the key judgements and assumptions underlying the Committee's economic forecasts. Wherever possible, these judgements will be quantified and accompanied by sensitivity (scenario) analysis, illustrating the possible implications if the economy evolves differently from that implied by these central judgements. These judgements will be assessed retrospectively as part of an enhanced forecast performance evaluation process. In addition, a number of changes will be made to the way in which information about the MPC's forecast distributions is communicated.

5. **Enhancing the role of monetary policy analysis in the forecast process (options 10, 12 and 16).** The forecast process will be adjusted to give greater weight and attention to the various monetary policy issues raised by the evolving economic outlook. This, for example,

includes policy issues such as: how quickly should the MPC try to bring inflation back to target in different economic circumstances; and what are the relative risks of providing too little versus too much monetary stimulus in a given environment? Initially, this change will have most impact on the Committee's internal discussions but, over time, it is likely to be reflected in the *Inflation Report* and in other forms of external communications.

6. **Exposing MPC's forecasts to increased challenge (options 4, 7, 9 and 18).** The forecast process will be adjusted such that the Committee's judgements and forecasts are exposed to greater challenge, both from within and from outside the Bank. There will be an enhanced role for Bank staff who are expert in particular topics to challenge the Committee's thinking. And the forecast process will be adjusted to give greater weight to external forecasts and views.

7. The one area in which the broad thrust of the Stockton Review will not be followed is **increasing the weight and attention given to individual MPC members' views (options 5, 15, 17).** Individual members' views are already fully taken into account and are a key part of deciding on the MPC's collective forecast. As was stressed in the Stockton Review, the deliberative nature of the forecast discussions used to generate the MPC's collective forecast has significant value. And there are considerable benefits to the quarterly *Inflation Report* and the projections continuing to focus on the best collective judgement of the MPC, rather than highlighting relatively small differences between individual members.

Summary of responses to Stockton Review

Category descriptions: **1)** Implemented or implemented forthwith; **2)** Intend to implement but will require further planning; **3)** Further analysis is required to assess the merits and drawbacks of the recommendation; **4)** Do not intend to implement, with reasons explaining the difference of view.

No.	Option	Category	Next steps
	PROVIDING GREATER TRANSPARENCY ABOUT THE MPC'S FORECASTS		
5	At some point in the forecast process, canvass individual MPC members for their forecasts of real GDP growth and inflation.	4	No change from current practice is planned. Individual members' views are already fully taken into account and are the key determinant of the Committee's collective forecast. There are considerable advantages in continuing to focus on the best collective judgement of the Committee as a whole.
6	Develop richer and more systematic internal processes for evaluating outturns against the forecast.	2 (2013 H2)	An enhanced forecast evaluation process will be developed, linked to a retrospective evaluation of the (quantified) central judgements shaping the forecast. Some progress should be possible in time for the annual forecast evaluation exercise, which will be published in the August 2013 *Inflation Report*.
12	Consider publishing some alternative scenarios.	2 (2013 H2)	This will be implemented in conjunction with the change to provide more information about the key central judgements underlying the Committee's forecasts and an analysis of the possible implications if the economy evolves differently to those central judgements.
13	Provide greater detail about the consensus forecast.	2 (2013 H2)	This will be implemented as part of the change to provide quantified information about the key central judgements underlying the Committee's forecasts.

No.	Option	Category	Next steps
14	Expand the forecast evaluation exercise currently published in the *Inflation Report* to include a fuller discussion of how outturns have differed from expectations.	2 (2013 H2)	See response to option 6. An enhanced forecast evaluation process will be developed, linked to a retrospective evaluation of the (quantified) central judgements shaping the forecast.
15	Consider publishing a summary of the individual forecasts of the MPC members as a supplement to the fan charts in the *Inflation Report*.	4	See response to option 5: no change from current practice is planned. Individual members' views are already fully taken into account and are the key determinant of the Committee's collective forecast.
16	Consider increasing communication about the outlook for policy as part of the forecast process.	3 (2013 H2)	No firm decision has been reached at this stage on the provision of information concerning the possible future path of monetary policy. This recommendation will be reviewed as part of the changes intended to support the forecast process giving greater weight and attention to the monetary policy issues raised by the evolving economic outlook.
17	Consider publishing a vote by MPC members on the forecast in addition to a vote on the policy decision.	4	See response to option 5.
19	Consider changes to the fan charts. The Bank could reduce the fine gradations of the fan chart and add a line for the mean and/or modal forecast. And, some consideration should be given to moving away from a continuous quarterly projection and providing projections for half years or years.	2 (2013 H2)	The way in which information about the MPC's forecast distributions is communicated will be reviewed. The review will seek to increase the transparency and usefulness of the information provided, while preserving the importance that economic forecasts should be viewed as probability distributions rather than point projections. Some initial incremental improvements will be evident in the May and August *Inflation Reports*.

No.	Option	Category	Next steps
20	Consider the creation and publication of cumulative density functions for inflation, the growth rate of real GDP, and the level of real GDP for a couple or few specified dates.	1	Cumulative distribution functions were included for the first time in the February 2013 *Inflation Report*. The precise role and format of these charts will be considered over coming forecast rounds.
21	Publish the supplementary data with the quarterly detail and the probability distribution parameters underlying the fan charts at the time of the release of the *Inflation Report* rather than a week later.	1	These data will be published on the Bank's website at the time of the release of the *Inflation Report,* with effect from the May *Report*.
	THE ROLE OF MONETARY POLICY ANALYSIS		
10	Analysis of monetary policy options and strategies could be included routinely in the background materials and briefings prepared by the staff for every forecast round.	2 (2013 H2)	The forecast process will be altered to give greater weight and attention to the monetary policy issues raised by the evolving economic outlook. A particular focus will be on any short-run trade-offs faced by the Committee between, on the one hand, keeping inflation close to the target and, on the other, avoiding unnecessary volatility in output and employment.
12	Consider publishing some alternative scenarios.	2 (2013 H2)	As above.
16	Consider increasing communication about the outlook for policy as part of the forecast process.	3 (2013 H2)	As above.
	INCREASING CHALLENGE		
4	Produce a staff forecast and present it to the MPC prior to each *Inflation Report*.	4	No change from current practice is planned. Producing a staff forecast in addition to the MPC's own forecast risks confusing external communication. But the forecast process will be adjusted to provide an enhanced role for Bank staff who are expert in particular topics to challenge the Committee.
7	To promote a more assertive and experienced staff, increase the participation and influence of specialists within [the Monetary Analysis area of the Bank] in the forecast process.	2 (2013 H2)	See response to option 4.
9	Contemplate encouraging longer [staff] tenure in positions and less rotation.	2 (2013 H2)	The Bank is concerned to increase staff tenure in a wide range of its activities and will be reviewing its internal processes and career offer accordingly.

No.	Option	Category	Next steps
18	Outsource the responsibility to organise once- or twice-a-year meetings of the MPC with leading researchers and scholars, focused on difficult or controversial issues. This outside group would set an agenda based on what they think the MPC should hear, including views that would challenge prevailing conventional wisdom at the Bank.	3 (2013 H2)	The Bank (jointly with the Centre for Economic Policy Research) currently organises two seminars a year (Monetary Policy Roundtables) which bring together academics, private sector economists and MPC members to discuss topical economic issues. Further thought will be given to developing additional fora through which researchers and academics are able to inform and challenge MPC thinking on key economic issues.
	OTHER		
1	Further expand efforts to increase the detail with which the financial sector is incorporated into the forecast and the models that support the forecast.	2 (2013 H1)	This issue will be addressed in a Bank of England Working Paper on COMPASS, the central organising model for the MPC's forecast, due to be published in May 2013. A seminar with outside commentators and academics has been arranged for May. The MPC will also be able to draw upon briefing provided to the FPC and the FPC's analysis.
2	Support even greater engagement with the academic community on forecast technology.	1	A range of activities with outside academics on this topic has been organised.
3	Hold four "Special Issues" meetings each year that would be used to explore topics relevant, directly or indirectly, to the forecast but that need greater attention than can be devoted under the meeting constraints of the forecast round. To create time for MPC members to attend, these meetings could replace four pre-MPC meetings.	3 (2013 H1)	The Committee will devote more time outside of the forecast round to discussing key economic issues. But these additional discussions will not be at the expense of Pre-MPC meetings on developments in the economy, which play an important role in briefing the Committee ahead of its monthly policy meetings.
8	Consider increasing the number of staff allowed to witness forecast presentations.	1	This will be implemented in time for the May forecast round.
11	Consider creating a forecast with an extended horizon beyond the current three-year period—a horizon of sufficient length to allow consideration of the development and likely unwinding of major economic and financial imbalances.	3 (2013 H2)	The MPC will devote more time to discussing longer-term issues and risks, but in the first instance these discussions will take place outside of the formal forecast round.