



ASSET MANAGEMENT

IS IT TIME FOR THE BANK OF ENGLAND TO SELL CORPORATE BONDS BACK TO THE MARKET?

3 August 2017

In recent days there has been speculation about the possible sale of corporate bonds bought by the Bank of England (BoE) as part of its post-referendum emergency measures, back to the private sector. RLAM would be fully supportive of an early commencement of such sales; we believe it would be in the long-term interests of the sterling credit market if the BoE was to exit its position in an orderly manner and take advantage of current benign conditions.

Why do RLAM advocate an early exit?

There are several reasons why we think the BoE should sell now. First, the purchases were part of a set of emergency measures that are no longer required. Indeed, we were always sceptical about the need for corporate bond buying in the first place, as the market was not “broken” at the time of intervention.

Second, the buying programme distorted the market by favouring global companies at the expense of more UK focused issuers. In our opinion, it made little sense to lower the cost of capital for global companies who were simultaneously buying back equity. The sooner market forces determine the pricing of credit, the better it is for the long-term health of the market.

Third, the programme has increased the price at which investors buy new and existing securities, thereby lowering their long-term returns. It is apparent, looking at the degree of over subscription for recent new credit bond issues, that there is latent private sector demand for non-government bonds; an orderly sale of existing bonds would help bring the demand / supply balance more into equilibrium.

Therefore, it was disappointing to hear today that the BoE, instead of preparing an early exit, is planning to reinvest coupon and maturity proceeds back into the sterling credit market from the second half of 2019; this is in our opinion, neither necessary nor desirable.

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