BANK OF ENGLAND

Mario Draghi
Chair of ESRB General Board
Kaiserstrasse 29
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Germany

Mark Carney
Governor

17 December 2014

Dear Mario Mark

In accordance with Article 136 of Directive 2013/36/EU (CRD IV), I am writing to notify the European Systemic Risk Board that the UK countercyclical capital buffer (CCB) rate has been set at 0 per cent, as announced in the Financial Policy Committee's *Financial Stability Report* published on 16 December. More information on the UK's approach to setting the CCB rate is provided in the annex to this letter.

Yours sincerely

Annex: Further information on setting of the UK CCB rate

Information required to be published under CRDIV	Latest data*
Applicable countercyclical buffer rate	0%
Credit-to-GDP ratio	150%
Deviation of credit-to-GDP from long-term trend	-25.5%
Buffer guide	0%

* As of 16 December

Justification for the buffer rate on UK exposures (source: December 2014 *Financial Stability Report*)

As part of its discussions in December, the Committee considered both the 'buffer guide' — a simple metric identified in legislation which provides a guide for the CCB based on the size of the credit-to-GDP gap — and its core indicators, which look at aspects of balance sheet stretch in banks and other sectors and terms and conditions in markets.

Indicators of bank resilience — such as capital, leverage ratios, and dependence on short-term wholesale funding — have improved during 2014. Levels of resilience are markedly higher than before the crisis and are expected to improve further as banks continue to transition to Basel III. The Committee's view on capital adequacy has been supported by the stress-testing exercise and its assessment of the risk outlook.

Aggregate private sector credit in the United Kingdom has continued to fall relative to GDP, though the level of debt — particularly for the household sector — remains high. As a result of weak net credit growth, the gap between the ratio of credit-to-GDP and its long-term trend has been strongly negative and falling in recent years. Reflecting this, the 'buffer guide' suggests that the CCB should be set at 0%. But this is only one indicator that the Committee considers.

Other imbalances in the UK economy have persisted. The UK current account deficit — at 5.2% of GDP in 2014 Q2 — remains close to historical highs. And the official estimate of the UK net foreign asset position has deteriorated over the past few years, to around -20%. As discussed in Box 2, however, the United Kingdom's external balance sheet position is likely to be healthier than implied by official estimates. And to the extent that fiscal policy is credible and investors are confident in the policy framework and its continuing openness, current account deficits are easier to finance. At a sectoral level, other financial institutions have become more reliant on net short-term foreign currency funding recently. But banks appear to be in a better position on this measure than before the crisis.

The modest increase in market volatility in Autumn 2014 has been associated with a slight tightening in terms and conditions in financial markets, following a period of easing over the past couple of years. Market intelligence also suggests that yield-seeking behaviour has eased a little. But long-term real interest rates remain very low.

Taking these indicators into its overall assessment of risks, at its December meeting the Committee agreed to set the CCB rate for UK exposures at 0%, unchanged from September.