

# Why the government bonds owned by the Bank of England are not a debt burden

<https://www.uk/2021/04/03/why-the-government-bonds-owned-by-the-bank-of-england-are-not-a-debt-burden>

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I received this email very recently, and share it with the author's permission:

*Hi Richard,*

*Hope you're well. After reading some of your articles and watching one of your videos, I'm left with a question that I hoped you could answer.*

*The Bank of England holds lots of government debt. What happens when the bonds they hold mature? Doesn't the treasury need to pay the bank?*

*From what I understand, any interest earned on the bonds makes its way back to the treasury but what about the payment for the bond when it matures? Isn't that used to fund more purchases of bonds?*

*If the above is correct, isn't it right to say the debt remains a burden until the Bank of England forgive the treasury for the debt they hold and do not claim payments when the bonds mature?*

*I hope you don't mind me disturbing you over the bank holiday weekend and there's obviously no rush to reply.*

*All the best,*

*Etc.*

Since this seems to be a recurring question I thought it worth replying on the blog.

First, it is true that interest is still paid on these bonds. This is deliberate. It is intended to perpetuate the deficit narrative. The claim is that the country is over-burdened by debt and that as a result the country cannot afford things like education.

What the government never makes clear in its own accounting is that this money

comes straight back to it from the Bank of England, which it owns. The cost is not real as a result. Good accounting would require that the income and expense be offset against each other and that only the net cost of interest be shown. But that would not play into the hands of the debt fetishists so that does not happen.

Let's deal with the second issue then, of debt repayment when a bond comes to the end of its life, and most especially with regard to those bonds notionally held by the Bank of England. Note I say notionally, because actually they are entirely beneficially owned by the Treasury, but we can ignore that in what follows.

To make things easier let's assume the bond is for a total of £10 billion and lets assume the entire bond issue is held by the Bank. That does not happen in practice, but making the assumption just let's me ignore third party repayment in what follows, and does not alter the key explanation.

It's important to recall that the Treasury has no money as such. That is hardly surprising. The only tangible representations of money that we have are notes and coin, and these are not used to repay bonds. So, in other words all the Treasury does have are electronic bank balances, which are held with the Bank of England, the government's wholly owned bank.

In that case, when redemption is due to the Bank of England the Treasury asks the Bank to pay the Bank's subsidiary that owns the bonds £10 billion. And given that the Bank has to make any payment the Treasury asks it to do under the terms of the [1866 Exchequer and Audit Departments Act](#) (last revised in 2000) that is exactly what the Treasury will do.

So now what has happened is that the Treasury no longer owes the Bank of England subsidiary in respect of a bond. It instead owes the Bank itself the same sum, but on its bank account. In other words, all that happened is that there has been an asset swap by the Bank and a liability swap by the Treasury.

The Bank's subsidiary did have a bond. Now the Bank itself has £10 billion owing to it on a bank account. The Treasury did owe the Bank's subsidiary for a bond. Now it owes the Bank on an overdraft. So, in effect, repayment means that nothing has changed. The Treasury stills owes its own bank exactly the same amount of money as it did before repayment was made. And the Bank is also no better off. Nor is it owed by anyone different to whom it was owed money before this swap took place.

But, as we know, the Treasury won't now run an overdraft with the Bank of England even though it is allowed to, and did so regularly until 2008. That means that in practice it will now issue a new bond for £10bn so that it can clear the overdraft. And since under current QE arrangements the Bank of England is effectively matching new bond issues by the Treasury with pound for pound new bond purchases this means that the Bank will, in effect (it's indirect, but the substance is what I am suggesting) buy that

new bond issue. In the case of QE bond redemptions this has, incidentally, been true since 2009, so nothing has changed in 2020, just to avoid the suggestion that there is something unusual about this current arrangement.

The result is that the Bank will now pay the Treasury £10bn, whether directly or via the money markets, to buy that bond. In effect, the Bank will clear the Treasury's overdraft and say that it now owns a bond again in its place. The Treasury is entirely happy with this arrangement, however it is organised, because that is precisely what it intended should happen.

What this means is that we have now had a reverse asset and liability swap that puts both parties back in the position they were in when they both started. The Bank of England subsidiary now owns a bond again, the Treasury owes for it, and there is no overdraft. It is as if nothing happened.

So the question is, might this be onerous? My answer is straightforward. It is only onerous if doing the little bit of double entry book-keeping within the government's accounts that this requires is onerous, because that is all that really happens.

Throughout these transactions there is no real change to the economic substance of the relationship between the parties. The Treasury always appears to owe the Bank of England £10 billion at all times, but since the government controls them both this is anyway meaningless debt because in reality no third party is involved. There is no burden then.

So, how was that burden of debt that once existed to third parties removed? The answer is, of course, through quantitative easing (QE). QE creates new money. That new money cleared the government's debt when QE took place, replacing it with what is called 'base money'. Unless you can figure out a way that base money can be repaid without the government deciding to cancel it, and no one has yet, that debt has been cancelled in that case by QE. The obligation to pay has gone.

So, there is no burden left after QE is my summary, and the notional maturing, repayment and reissue of debt between the Bank of England and Treasury is just economic game playing of no consequence at all in the real economy.

I hope that helps.

*NB: I am open to answering questions, but I don't guarantee to do so.*