

Discussion of “Who Moves the Long End? The Dynamics of Bond Market Segmentation”

by Sitong Ding (LSE) and Robert Czech (Bank of England)

Discussant: Egemen Eren (BIS)

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Disclaimer: Views are those of the author and should not be attributed to the BIS.

What does monetary policy do to the long end?

- A 20-year puzzle: long real rates over-react to MP news.
- Far more than the expectations hypothesis (or long-run neutrality) would predict.

Recent term-premia explanations rely on **segmented bond markets**:

- **HLW (2021)**: habitat investors with rate-amplifying demand.
- **KLM (2024)**: tighter MP $\rightarrow$ arbitrageur wealth $\downarrow \rightarrow$ risk aversion $\uparrow \rightarrow$ term premia widen.

These predict **opposite quantity responses**. Quantity data have been missing.

This paper

- **Data:** MiFID II — near-universe of UK gilt trades, 2018–2025, LEI-level, daily.
- **Identification:** proxy-SVAR with HF external instruments.
 - Baseline (MP news): Braun–Miranda–Agrippino–Saha (BMAS, 2025) target factor. $F = 9.6$ baseline / 20.2 full sample.
 - Novel (inflation news): *inflation-swap surprises*, $F > 200$.
- **Headline:** long rates over-react persistently (hump-shape, $> 1\text{yr}$). To a MP tightening: GEMMs **sell** ($-\text{£}20\text{bn}$), PFs/insurers **buy** ($+\text{£}25\text{bn}$). Quasi-permanent.
- **Model:** NK + segmented markets + Blanchard–Yaari arbitrageurs with adjustment costs.
- **Counterfactual:** MP is more powerful when markets are segmented.

The discriminating moment. Quantity responses to a monetary *tightening*:

	KLM (intermediary wealth)	HLW (rate-amplifying demand)
Habitat (PFs, insurers)	BUY	SELL
Arbitrageurs (GEMMs)	SELL	BUY
Paper's empirical IRF	✓ matches	× contradicted

Roadmap for this discussion

Four comments:

1. BoE balance sheet policy.

Instrument defensible; but the model has no CB balance sheet, and Fn 38 is an identity, not a test.

2. ESX (2025) find rate-amplifying demand for UK ICPFs on balance-sheet shocks.

Independent UK evidence on the balance-sheet-shock dimension.

3. Regulatory regime shifts within the sample.

LDI 2022, Solvency UK, Basel III phase-in — non-stationarity in demand parameters.

4. The marginal trader: global capital and foreign investors.

Largest elastic UK holder; absent from the closed-economy framework.

Comment 1. BoE Balance Sheet Policy

BMAS factors are clean: QE and QT load on the balance-sheet factor, orthogonal to Target. Supply news acts through the curve; the rotation orthogonalizes Target in curve space. **The instrument is defensible.**

But the model has no central-bank balance sheet.

- QE peaked $\sim$ £895bn; QT $>$ £100bn by mid-2025.
- Counterfactual (“MP more powerful under segmentation”) read off a model where the balance sheet is absent.

And Fn 38 is an identity, not a test.

- “GEMM buys $\approx$ long-term-investor sells $\Rightarrow$ gross supply fixed” holds mechanically whenever the BoE sits outside both investor groups.
- A BoE $\rightarrow$ GEMM $\rightarrow$ PF passthrough gives the same equality while gross supply rises — the identity can’t tell them apart.
- Discriminating needs APF holdings + primary issuance — invisible to MiFID II.

Suggestions: add cumulative APF holdings (+ issuance) to the VAR; CB balance sheet as a state variable.

Comment 2. ESX (2025) find rate-amplifying demand in UK ICPFs

Eren–Schrimpf–Xia (*Management Science*, 2025) estimate UK ICPF demand using the BMAS **QE-surprise** instrument — a long-end balance-sheet-policy shock, different from the paper's target factor (short-end MP).

Finding: upward-sloping demand in prices for UK ICPFs. They call this “shock amplifiers” and link it explicitly to the LDI 2022 crisis.

Different shocks, different conditional responses:

- Paper (short-end MP shock) → ICPF demand downward-sloping; rate-amplifying ruled out.
- ESX (long-end balance-sheet shock) → ICPF demand upward-sloping; rate-amplifying alive.

ESX identify off long-end balance-sheet shocks — a different dimension from the paper's target factor. On that dimension, UK ICPF demand looks rate-amplifying. The two findings can coexist; together they say demand is shock-conditional.

Comment 3. Regulatory regime shifts within the sample

UK gilt demand is regulation-driven: PFs (The Pensions Regulator [TPR], LDI mandates), insurers (Solvency II MA), banks (Basel III LCR, leverage).

Regimes within the sample (Jan 2018 – Feb 2025):

- **Pre-Sept 2022:** old regime. $\sim 67\%$ of sample.
- **Sept 2022 LDI crisis:** TPR pushes LDI leverage $\downarrow$, cash buffers $\uparrow$. $\sim 19\%$.
- **2024 onwards:** Solvency II $\rightarrow$ Solvency UK (MA reform). $\sim 14\%$.

$\sim$ Two-thirds of identifying variation: a regulatory regime that no longer exists.

Testable: split at Sept 2022. Read the policy-relevant counterfactual off the current sub-sample.

Comment 4. The marginal trader?

UK gilt ownership (DMO/BoE data, end-2024, approximate):

Bank of England	~30%
Foreign / overseas investors	~28%
UK PFs, insurers, LDI	~25%
UK banks, building societies	~6%
Households and other	~11%

ESX (2025): foreign investors are the most elastic UK holder (significant, downward-sloping); ICPFs/OFls go the other way; banks and households insignificant.

⇒ Foreign capital — largest *elastic* holder — a strong candidate for marginal price-setter.

MP shocks move the US-UK 10Y spread → shift foreign demand for gilts → a channel the closed-economy framework can't capture.

The paper's model has one local arbitrageur, no foreign investor. MiFID II LEI ≠ ultimate domicile (US HF via London PB looks domestic).

Suggestion: use LEI to identify foreign counterparties; add sterling NEER + US-UK 10Y spread as endogenous in the VAR.