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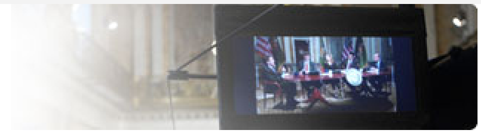

Minutes of the Meeting of the Treasury Borrowing Advisory Committee Of the Securities Industry and Financial Markets Association February 5, 2013

2/6/2013

The Committee convened in closed session at the Hay Adams Hotel at 11:31 a.m. All Committee members were present. Under Secretary for Domestic Finance Mary Miller, Assistant Secretary for Financial Markets Matthew S. Rutherford, Deputy Assistant Secretary for Federal Finance James G. Clark, and Director of the Office of Debt Management Colin Kim welcomed the Committee, including the newest Committee member Carey Lathrop. Other members of Treasury staff present were Fred Pietrangeli, Amar Reganti, John Dolan, Jamie Franco, and Tom Katzenbach. Federal Reserve Bank of New York staff Josh Frost and Lorie Logan were also present.

Deputy Assistant Secretary (DAS) Clark began by discussing the recent trends in receipts. Clark noted that withheld receipts in Q1 FY13 increased at the most rapid pace in 10 years, possibly reflecting the acceleration of performance payments by employers to employees from calendar year 2013 to calendar year 2012 in anticipation of changes in tax laws.

Clark then showed a chart with the ten largest outlays in the fiscal year to date. The chart showed that Treasury expenditures were $26 billion lower compared to the same period in FY12, largely reflecting the Department of Defense's change from accrual to cash accounting on its non-marketable investments. Clark also noted that the sizable increase in Health and Human Services (HHS) payments primarily resulted from a calendar effect, reflecting the timing of payments.

Clark noted that net issuance of State and Local Government Series (SLGS) securities increased in Q1 FY13. Clark explained that lower rates most likely prompted advance refunding activity by tax-exempt issuers, noting that it was too difficult to tell whether the increase could have also reflected state and local issuers moving deals into Q1 in anticipation of a protracted-debt limit related closure of the SLGS window.

Next, Clark noted that primary dealer deficit estimates for FY13 were $40 billion below CBO’s latest deficit estimate of about $971 billion, and about $60 billion below the Administration’s FY13 Mid-Session Review (MSR) of $991 billion released in late July 2012.

Finally, Clark commented on the cumulative budget deficit chart, noting that there was no change between November and December’s cumulative budget deficit in our current fiscal year. He noted that this reflected the elevated level of receipts in Q1 FY13.

DAS Clark then noted that some dealer estimates for net marketable borrowing were lower than their deficit estimates. Given the guidance given in prior TBACs regarding the federal direct lending programs such as student loans, net marketable borrowing estimates should generally run above deficit projections.

After DAS Clark completed his overview, Director Kim began by briefly reviewing sources of financing in Q1 and Q2 of FY13. He called attention to the projected implied increase in financing for Q2 FY13 of $142 billion. Kim stated that all of this projected increase in financing would be done with bills in normal seasonal fashion.

Director Kim then provided a brief overview of historical and projected net marketable borrowing. Assuming that end of December 2012 issuance levels remain constant throughout FY 13, Director Kim noted that Treasury appears to be underfunded by more than $129 billion in FY2013. He noted, however, that the number reflects financing need estimates from the August 2012 Mid-Session Review and that the funding gap is reduced to $21 billion if financing estimates are closer to market expectations of $950 billion.

Next, Director Kim reviewed current interest rate assumptions. Kim compared the OMB interest rate forecasts to those implied by market forward rates. Kim noted that there was sizable divergence between the two rate forecasts.

Next, Director Kim reviewed several debt metrics. As of December 31, 2012, the average maturity of the portfolio was approximately 64.8 months. In the chart presentation showing the projections for Treasury’s weighted average maturity, Kim adjusted future note and bond issuance on a pro-rata basis to match projected financing needs. The simulation showed that the average maturity continues to extend well above the 3-decade average of 58.1 months. By 2016, it could reach the upper end of the historical range.

He emphasized that the average maturity projections and the associated underlying assumptions for future issuance were hypothetical and not meant to convey future debt management policy or an average maturity target. He also reiterated that Treasury will remain flexible in the conduct of debt management policy.

Director Kim then quickly reviewed the demand characteristics within the primary market for Treasury securities over Q1 FY13. Director Kim noted that bid-to-cover ratios remained high relative to historical levels across all securities.

Director Kim concluded with a brief review of investor trends in auctions, noting that investment funds increased their portion of short- and long-coupon awards as well as TIPS in Q1 FY13.

Next, the Committee considered the charge question concerning potential changes in coupon auction sizes given the fiscal outlook over the short, intermediate and long term. It was the consensus view of the Committee that coupon sizes should remain unchanged and that any residual funding needs could be met with adjustments to bill issuance.

A Committee member asked about the status of floating rate notes. Assistant Secretary Rutherford noted that Treasury staff received 15 comment letters in response to the Advanced Notice of Proposed Rule Making and was currently in the process of reviewing the comments. Rutherford noted that there was a fairly even split among the comment letters regarding the index choice, with about half of the respondents advocating the use of 13-week T-bills and the other half recommending the use of a Treasury general collateral repo rate. Rutherford noted that Treasury was hoping to issue a final rule in the coming months and that the first FRN auction was estimated to be about a year away.

Another member asked about the debt limit and the restoration of extraordinary measures. Specifically, the member asked whether Treasury would have the ability to utilize the restored extraordinary measures at the expiry of the debt limit suspension in May. Rutherford indicated that Treasury believed that it could use these fully restored extraordinary measures in their entirety, if needed.

The Committee then turned its attention to the third charge about whether Treasury should consider more rapidly extending the weighted average maturity (WAM) of its debt and if so, what strategies might best assist Treasury in achieving such a goal, while remaining consistent with our broader debt management principles.

The presenting member noted that the Committee had periodically addressed this question in the past, concluding each time that the reasons for extending the WAM more rapidly had not been compelling. Historically, borrowing at the short end of the curve had been a cost saving strategy based on the level of rates and the presence of positive term premia. However, the fact that interest rates were near historic lows and term premia was currently negative suggested that the Committee should reconsider this question.

The member suggested that one strategy for extending WAM would be for Treasury to reduce bills issuance from current levels. In fact, maintaining the current nominal stock of bills outstanding implied that these securities would decline as a share of the outstanding debt and decline as a share of GDP.

The member then proceeded to discuss three purely hypothetical alternative strategies for increasing the pace of maturity extension. The member began by noting that given the current maturity structure of new issuance, WAM will naturally extend to about 80 months by 2022. The member stated that this status quo strategy could be considered a "base case" for comparing alternative strategies. The member outlined three hypothetical debt issuance strategies that would extend the WAM to 80 months by 2017.

The first hypothetical alternative strategy maintained the current auction schedule but reduced both 2- and 3-year issuance sizes and increased 10- and 30-year issuance sizes. The second hypothetical alternative introduced a new 50-year bond. In this strategy, 2- and 3-year note issuance sizes were reduced and a 50-year was introduced. The third hypothetical alternative reintroduced a 20-year bond. In this strategy, Treasury reduced both 2-year and 3-year issuance and raised commensurate funds through the issuance of a 20-year bond.

The presenting member then estimated the potential impact on the debt portfolio associated with each of these three strategies, noting that in all three hypothetical cases, investors would be required to absorb significantly greater amounts of long-end debt compared to the base case. The member further noted that even under the base case, long-term debt was expected to double over the next 5 years.

The presenting member then turned to potential demand for long-duration debt and an assessment of whether the markets had the capacity to absorb the increases in long-term debt associated with the alternative strategies. The member noted that the pension & liability-driven investment (LDI) community was expected to provide the most domestic demand for duration.

However, the presenting member also observed that there were many sources of duration currently available to these investors and that this demand could be filled by credit, mortgages, and current expected Treasury supply.

The presenter concluded that the benefits from a more rapid WAM extension were relatively small. For example, using the assumptions contained in the analysis, a more rapid extension would only result in a two percent decline in the amount of debt maturing each year, and would not create any net interest-cost savings (assuming CBO interest rate forecast is realized).

The presenting member further noted that a more rapid extension of WAM had the potential to increase interest rates and term premia. Demand for longer-dated debt in excess of that which was already anticipated was uncertain, absent changes in the accounting or regulatory environment.

A discussion followed the presentation with some members contending that the current glide path of WAM was appropriate, while others argued for more aggressive extension. The proponents of the current glide path stated that Treasury should adhere to its model of “regular and predictable” issuance, which provides sufficient tailwind for WAM extension with the least disruption to the market.

Proponents of more aggressive extension cited the low cost of term premium in the market. The discussion concluded with a recommendation to do more work on the cost and benefits of extension strategies.

Due to time constraints, the Committee did not have an in-depth discussion regarding the charge relating to primary and secondary housing markets. However, the participants were keenly interested to hear the presenter's conclusions that secondary market liquidity was strong in MBS markets and that prices had increased in response to recent actions undertaken by the Federal Reserve. In addition, the presentation noted that there were a number of promising conditions in the primary market, including loosening lending standards, rising home prices, and historically low mortgage rates. Hurdles that remain include GSE reform, changes in loan servicing, regulatory capital changes, ongoing and future legal exposures and the availability of credit.

The meeting adjourned at 1:00 p.m.

The Committee reconvened at the Department of the Treasury at 5:00 p.m. All Committee members were present. The Chairman presented the Committee report to Acting Secy. Wolin.

A brief discussion followed the Chairman's presentation but did not raise significant questions regarding the report's content.

The Committee then reviewed the financing for the remainder of the January through March quarter and the April through June quarter (see attached).

The meeting adjourned at 6:00 p.m.

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James G. Clark
Deputy Assistant Secretary for Federal Finance
United States Department of the Treasury
February 5, 2013

Certified by:

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Matthew E. Zames, Chairman
Treasury Borrowing Advisory Committee
Of The Securities Industry and Financial Markets Association
February 5, 2013

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Ashok Varadhan, Vice Chairman
Treasury Borrowing Advisory Committee
Of The Securities Industry and Financial Markets Association
February 5, 2013

Treasury Borrowing Advisory Committee Quarterly Meeting
Committee Charge – February 5, 2013

Fiscal Outlook

Taking into consideration Treasury's short, intermediate, and long-term financing requirements, as well as uncertainties about the economy and revenue outlook for the next few quarters, what changes to Treasury's coupon auctions do you recommend at this time, if any?

Mortgage and Housing Market Conditions

We would like the Committee to comment on current conditions in the primary and secondary financing markets for housing credit. Please identify and discuss any barriers or hurdles that impede the availability of credit within these markets. What steps can the banking industry, regulators, and/or policy makers take to assure that the availability of credit to this market continues to improve?

More Rapid Extension of the Average Maturity of Debt

For the past several years, Treasury has been pursuing a policy of extending the average maturity of its debt. Should Treasury consider even more rapidly extending the weighted average maturity of its debt? If Treasury were to do so, what strategies might best assist us in achieving that goalwhile remaining consistent with ourbroader debt management principles?

Financing this Quarter

We would like the Committee's advice on the following:

- The composition of Treasury notes and bonds to refund approximately $64 billion of privately-held notes maturing on February 15, 2013.
- The composition of Treasury marketable financing for the remainder of the January-March quarter, including cash management bills.
- The composition of Treasury marketable financing for the April - June quarter, including cash management bills.

TBAC Recommended Financing Table Q1 2013 and TBAC Recommended Financing Table Q2 2013