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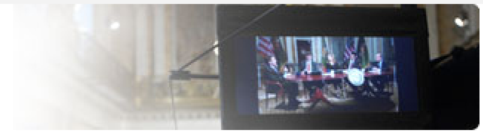

Minutes of the Meeting of the Treasury Borrowing Advisory Committee of the Securities Industry and Financial Markets Association November 4th

11/5/2014

The Committee convened in closed session at the Hay Adams Hotel at 11:30 a.m. All members were present. Acting Under Secretary for Financial Markets Matthew S. Rutherford, Senior Advisor Seth Carpenter, Deputy Assistant Secretary for Federal Finance James G. Clark, and Director of the Office of Debt Management Fred Pietrangeli welcomed the Committee, including the Committee's newest member Brian Sack. Other members of Treasury staff present were Deputy Director Amar Reganti, Deputy Director Allen Zhang, John Dolan, Laura Lipscomb, and Tom Katzenbach. Federal Reserve Bank of New York staff members Nathaniel Wuerffel and Lorie Logan were also present.

Deputy Assistant Secretary Clark and Director Pietrangeli quickly reviewed the Treasury presentation to the Borrowing Advisory Committee. Clark noted that budget deficits forecasts have declined, and that Treasury is likely to be over-financed in FY2015. Clark specifically noted that Treasury's current auction schedule would raise $100 and $200 billion more than the current FY2015 forecasted borrowing estimates from primary dealers and the CBO, respectively.

Clark also noted that Treasury's borrowing needs would increase again in 2016 if the Federal Reserve decides not to reinvest at least some of the maturing Treasury securities held in the System Open Market Account (SOMA), despite the projected overfunding in 2015 with the current auction schedule. Clark noted that while Treasury would normally address a short-term decline in borrowing needs by reducing bill issuance, he suggested that Treasury and the Committee should instead consider the possibility of cuts to coupon security issue sizes. He explained that this consideration is warranted as Treasury bills comprise just 11 percent of marketable debt outstanding and that further large reductions could have implications for the functioning of short-term markets, given investors' persistent and strong structural demand for short-term high-quality liquid assets.

A member asked about the status of Treasury's cash balance policy. Clark began by noting that at the August 2014 Treasury Quarterly refunding meeting, the TBAC recommended that Treasury hold a $500 billion cash balance, or 10-days of liquidity, to ensure that all government obligations could be met in the event that Treasury lost market access. Clark stated that Treasury believes that a maintaining a higher cash balance is prudent and that the Department continues to refine its approach on this matter. Clark noted that Treasury's ability to run higher cash balances in FY2015, however, may be somewhat constrained by debt limit considerations.

Following Clark's comments a robust discussion ensued about financing options. One member noted that Treasury should be careful to avoid negative rates in bill markets, as this can create a number of unintended consequences. Another member noted that Treasury has more flexibility in coupon reductions, given progress made in recent years toward extending the weighted-average maturity (WAM) of the Treasury portfolio. Several members suggested that the Committee should continue to discuss the pace of further WAM extension at future meetings.

Based upon better-than-expected deficits and near-term fiscal projections for FY2015, the Committee recommended that Treasury initiate $1 billion cuts to both the 2- and 3-year coupon auction sizes beginning in November.

Clark then asked the Committee for their views regarding the significant volatility in Treasury cash and futures markets that occurred on October 15, 2014. Committee members expressed a wide variety of views regarding the potential drivers of the intra-day volatility. Many noted, however, that no firm conclusions could be drawn without further analysis and better data regarding the transactions that took place that day. The Committee suggested that Treasury analyze this event more, given the importance of secondary markets to Treasury auctions.

The Committee adjourned at 12:30 p.m. for lunch. The Committee reconvened after lunch at 1:30 p.m. to review the final charge regarding student loans.

The presenting member began by providing some information on the growth of the student loan program and default rates. The member noted that the balance of outstanding student loans has grown from $1.0 trillion as of the end of 2011 to $1.3 trillion as of mid-2014. The member cited four key factors that continue to drive student loan growth. These included: students' broadly choosing to consume more years of higher education, in part reflecting demographic change with growth in the 20-34 year old cohort; a greater proportion of students utilizing the federal student loan program (48 percent as of 2012, up from 33 percent in 2002); increases in the cost of higher education exacerbated by reduced subsidies from state governments to in-state schools; and outstanding loan balances declining at a slower rate than originally anticipated due to both increased volume of loans in deferral and forbearance as well as longer loan tenors.

The presenting member stated that default rates are high and rising, with the two-year cohort default rate increasing to 10.0 percent as of 2011versus 8.8 percent in 2009. The member stated that "default" in the context of federal student loans is generally defined as 270 days without payment and that loans in default represent 9 percent of the stock of outstanding federal student loans.

The member suggested that students are taking out student loans because higher education has historically been correlated with upward economic mobility. However, the member noted an average of 40 percent of students at four-year institutions (and 68 percent of students in for-profit institutions) currently do not graduate within six years. As a result, they most likely do not benefit from higher incomes associated with education yet face the burden of student debt. The member also noted that unlike all other indebtedness, student debt cannot be extinguished in bankruptcy in almost all cases and the government can garnish income tax refunds, Social Security and other federal benefits.

The member next discussed the cost of the student loan program. The member noted that CBO calculations indicate that the student loan program will deliver a $135 billion profit to taxpayers over the next decade. However, it was observed that the estimate is based on the programs as legislated and does not factor in market risk or shifts in macroeconomic conditions, thereby ignoring the impact of potential defaults. The member further added that the estimate does not include the potential cost associated with recent proposals to redesign elements of the student lending program, including: reducing the interest rate on student loans; increasing repayment options; and addressing the pace of origination with a focus on qualifying institutions eligible for such programs. The member noted that under an alternative fair-value accounting approach used by CBO, the program results in an $88 billion cost to taxpayers.

The member concluded his presentation by noting that due to the relatively recent growth in both origination volume and default rates, it is premature to draw conclusions regarding the extent to which student lending is crowding out other forms of credit creation and thus acting as a drag on other parts of the economy.

A robust and spirited discussion followed the presentation. One member noted that it might be prudent for Treasury to consider some type of asset and liability management framework in conjunction with the optimal WAM discussion for large financial programs such as student loans.

The meeting adjourned at 2:20 p.m.

The Committee reconvened at the Department of the Treasury at 5:00 p.m. All Committee members were present. The Chair presented the Committee report to Secretary Lew.

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

The Committee then reviewed the financing for the remainder of the October through December quarter and the January through March 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
November 4, 2014

Certified by:

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Dana Emery, Chairman
Treasury Borrowing Advisory Committee
Of The Securities Industry and Financial Markets Association
November 4, 2014

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Curtis Arledge, Vice Chairman
Treasury Borrowing Advisory Committee
Of The Securities Industry and Financial Markets Association
November 4, 2014

Treasury Borrowing Advisory Committee Quarterly Meeting
Committee Charge – November 5, 2014

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?

Market Volatility on October 15, 2014

On October 15, 2014, there was significant volatility in Treasury cash and futures markets. We would like the Committee's views on the drivers of the October 15 volatility and the impact of this volatility on market participants. Was October 15th an idiosyncratic "perfect storm" event or have there been changes in the markets that increase the probability of similar events/volatility occurring in the future? What, if anything, can or should Treasury do with regard to this matter?

Student Loans

We would like the Committee to provide an update on the trends in the student loan market over the last several years. What issues, if any, should Treasury consider with regard to funding student loans?"

Financing this Quarter

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

- The composition of Treasury notes and bonds to refund approximately $59.8 billion of privately-held notes maturing on November 15, 2014.
- The composition of Treasury marketable financing for the remainder of the October-December 2014 quarter, including cash management bills.
- The composition of Treasury marketable financing for the January – March 2015 quarter, including cash management bills.

TBAC Recommended Financing Table Q1 2015 & TBAC Recommended Financing Table Q4 2014