U.S. DEPARTMENT OF THE TREASURY

Minutes of the Meeting of the Treasury Borrowing Advisory Committee of the Securities Industry and Financial Markets Association February 2, 2021

February 3, 2021

The Committee convened in a closed session via teleconference at 9:00 a.m. All members were present, except for Christine Hurtsellers. Deputy Assistant Secretary for Federal Finance Brian Smith, Director of the Office of Debt Management Fred Pietrangeli, and Deputy Director of the Office of Debt Management Nick Steele welcomed the Committee, including the newest member to the Committee, Mohit Mittal. Other members of Treasury staff present were Bobby Bishop, Chris Cameron, Dave Chung, David Copenhaver, Tammy Didier, Christian Furey, Christine Graffunder, Timothy Gribben, Tom Katzenbach, Chris Kubeluis, David Lebryk, Nellie Liang, Brett Solimine, Renee Tang, Brandon Taylor, Gregory Till, and Tom Vannoy. Federal Reserve Bank of New York staff members Kyle Lee, Susan McLaughlin, Linsey Molloy, Rania Perry, Julie Remache, and Nathaniel Wuerffel were also present.

Fiscal Assistant Secretary David Lebryk began the discussion and emphasized the importance of the Committee in providing advice to the Treasury on debt management.

Director Pietrangeli then provided brief highlights of Q1 FY2021 changes in receipts and outlays. Receipts were largely unchanged, declining by $3 billion (-0.4%) year-over-year. Outlays increased by $190 billion (17%), largely driven by payments related to the federal government's response to the COVID-19 outbreak, including increased unemployment, Medicare, Medicaid, food stamp, and financial assistance payments. Looking over the next two quarters, Pietrangeli noted that Treasury's Office of Fiscal Projections estimates privately-held net marketable borrowing of $274 billion and $95 billion, assuming cash balance of $800 billion for the end of March and $500 billion for the end of June. These borrowing estimates made no assumptions about future fiscal stimulus and assume coupon auction sizes remain unchanged.

Pietrangeli highlighted that deficit and privately-held net marketable borrowing projections by the primary dealers remain elevated with a median deficit estimate of $3.200 trillion for FY2021 and $1.743 trillion for FY2022. The median estimate for privately-held net marketable borrowing for FY 2021 was $2.600 trillion, which was lower than the deficit estimate in part due to expectations for Treasury to decrease its cash balance over the period. Primary dealers included an estimate for FY2021 fiscal stimulus in their deficit and borrowing estimates, with most dealers anticipating a package of about $1 trillion to be passed over the next few months. However, primary dealers also expressed uncertainty around both the size and timing of fiscal stimulus and the continued economic impact of COVID-19, with some risk that FY2021 borrowing needs could be biased to the upside. Pietrangeli next discussed the financing gap, commenting that Treasury appears well financed for FY2021 based on existing coupon auction sizes and the currently elevated cash balance.

Next, Debt Manager Taylor summarized primary dealer expectations for Treasury issuance over the coming months. Given the increases in nominal coupon auction sizes introduced over the course of CY2020, Treasury's elevated cash balance, and estimates for future fiscal stimulus, most primary dealers anticipated that Treasury is adequately financed for FY2021. As such, most primary dealers expected no change to nominal coupon auction sizes for the upcoming quarter. In addition, primary dealers largely anticipated slight increases in TIPS issuance sizes in CY2021, in line with the guidance provided at the November refunding.

Debt Manager Katzenbach then reviewed primary dealer views on the pace that Treasury could decrease bill supply to the Committee's recommended range of 15-20% of marketable debt outstanding. Primary dealers prefaced their views on the fiscal outlook but generally forecasted that the share could reasonably decline below 20% in the next 1-2 years. Within this context, primary dealers broadly noted that consideration should be given to the outlook for money market mutual fund assets under management, as well as the availability of investment substitutes. Some primary dealers suggested that eliminating one or two of the regular cash management bills could ease the impact of broader reductions in bill supply.

Next, Deputy Director Steele summarized responses from the primary dealers indicating a wide range of experience as Treasury market intermediaries in March and April 2020, with most citing internal risk limits as the primary source of constraints when facilitating the sudden, unprecedented demands for cash from all counterparty types. External factors were also cited with a focus on margin requirements, haircuts, and regulatory ratios. In terms of what could help in the future, the main theme was anything that could improve the flexibility of dealer balance sheets to better absorb the massive flows that customers abruptly demanded. Some dealers noted that the temporary supplemental leverage ratio (SLR) exemptions were helpful in subsequent months but that they were not as effective as they could have been due to being temporary and not including repo. Other suggestions included a standing repo facility with broad access or additional central clearing to allow for more netting down of the balance sheet. While these suggestions were viewed as potentially beneficial, dealers did not expect them to be sufficient to prevent similar challenges to intermediation in a future crisis.

The Committee then reviewed a presentation on the implications of the current abundant reserves environment for Treasury issuance. The presenting member highlighted that, as reserve balances continue to grow over the course of CY2021, given ongoing asset purchases by the Federal Reserve and an expected drawdown in Treasury's cash balance, bank deposit levels will grow and bank demand for Treasury securities should rise. With loan growth likely to remain low, banks would deploy excess liquidity in Treasury securities, with demand focused on banks' preferred habitat in the short and intermediate sectors. However, increased reserve levels risk constraining bank balance sheet capacity as leverage and capital ratio thresholds are approached, which could put pressure on the pricing of deposits and repurchase agreements. Lower bank balance sheet capacity for deposits could result in additional liquidity flowing into money market mutual funds, further bolstering demand for short-dated Treasury securities.

Next, the Committee reviewed a presentation on swap spreads and the information they may provide in understanding government borrowing costs. The presenting member noted that swap spreads can provide information about Treasury supply effects, but there are unique dynamics impacting the relative yield in swaps at different times and different maturities, including bank funding costs, regulatory effects, and idiosyncratic demand dynamics from different investor types. For example, front-end swap spreads have been primarily driven by bank funding costs. Moreover, narrower long-end swap spreads may indicate long-end Treasury securities are relatively expensive, but they could also represent a structural increase in the relative demand from investors to receive fixed rates in long maturity swaps. The Committee also discussed how regulations have affected swap spreads, including the effects of SLR, making on-balance-sheet holdings of Treasury securities more expensive than off-balance-sheet swaps. Finally, the presenting member highlighted that as the London Interbank Offered Rate (LIBOR) transition progresses, liquidity will migrate from LIBOR-based swaps to swaps linked to the Secured Overnight Financing Rate (SOFR), which could facilitate more direct comparison between Treasury securities and swaps. The Committee noted the widening of swap spreads amid increased coupon supply over the last year suggests that factors other than Treasury supply may have prevailed recently.

The Committee then turned to its financing recommendation for the upcoming quarters and recommended that Treasury maintain nominal coupon auction sizes at current levels. The Committee noted that prior increases to coupon issuance had generated significant financing capacity and that making no further changes in February would provide the most flexibility, given the current fiscal uncertainty. The Committee also recommended that Treasury continue to increase TIPS auction sizes at a pace consistent with the $10-20 billion increase in gross issuance for CY2021 that was forecast at the November 2020 refunding.

The Committee adjourned at 1:15 p.m.

The Committee reconvened at 4:30 p.m. The Chair reviewed recent Committee recommendations, summarized key elements of the Committee report for Secretary Yellen, and followed with a brief discussion of recent market developments.

The Committee adjourned at 5:00 p.m.

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Brian Smith

Deputy Assistant Secretary for Federal Finance

United States Department of the Treasury

February 2, 2021

Certified by:

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Elizabeth Hammack, Chair

Treasury Borrowing Advisory Committee

Of The Securities Industry and Financial Markets Association

February 2, 2021

TREASURY BORROWING ADVISORY COMMITTEE QUARTERLY MEETING

COMMITTEE CHARGE – FEBRUARY 2, 2021

Fiscal Outlook

Taking into consideration Treasury's short, intermediate, and long-term financing requirements, as well as the variability in financing needs from quarter to quarter, what changes, if any, do you recommend to Treasury issuance? Please also provide perspectives regarding market expectations for Treasury issuance, the effects of SOMA investments, the evolution of Treasury holdings by different types of investors, as well as auction calendar construction.

Abundant Reserves

What are the implications of the current abundant reserve environment for Treasury issuance? Are there significant differences between the current abundant reserve environment compared to previous periods of abundant reserves that Treasury should consider? How does an abundant reserve environment affect private demand for Treasuries at different maturities?

Swap Spreads

Discuss the movements in swap spreads in both recent months as well as the long-term. What are the benefits and limitations of comparing fixed rates on fixed-to-float interest rates swaps to interest rates on Treasury securities? To what extent can swap spreads provide relevant context for understanding government borrowing costs? What types of interest rate swaps are most relevant for comparison across Treasury maturities and security types? How do the demand dynamics for interest rate swaps differ from that of Treasury securities and what are the differences in the investor base for each product? How does the transition away from LIBOR affect the information content derived from swap spreads?

Financing this Quarter

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

- The composition of Treasury notes and bonds to refund approximately $62.9 billion of privately-held notes and bonds maturing on February 15, 2021.
- The composition of Treasury marketable financing for the remainder of the January-March 2021 quarter.

- The composition of Treasury marketable financing for the April-June 2021 quarter.