Minutes of the Meeting of the Treasury Borrowing Advisory Committee May 4, 2021

May 5, 2021

The Committee convened in a closed session via teleconference at 10:45 a.m. All members were present. Fiscal Assistant Secretary David Lebryk, 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. Other members of Treasury staff present were Bobby Bishop, Chris Cameron, Dave Chung, David Copenhaver, Tammy Didier, Joshua Frost, Christine Graffunder, Timothy Gribben, Tom Katzenbach, Michael Kiley, Chris Kubeluis, Kyle Lee, Nellie Liang, Justin Reber, Jessie Smith, Brett Solimine, Renee Tang, Brandon Taylor, Gregory Till, and Tom Vannoy. Federal Reserve Bank of New York staff members Ellen Correia Golay, Matthew Lieber, Susan McLaughlin, Rania Perry, Monica Scheid, and Nathaniel Wuerffel were also present.

Fiscal Assistant Secretary Lebryk opened the meeting by emphasizing the importance of the Committee's work in providing advice to the Treasury on debt management.

Director Pietrangeli then provided brief highlights of changes in receipts and outlays fiscal-year-to-date. Receipts increased by $102 billion (6%) compared to the same period last year. Outlays increased by $1.06 trillion (45%), driven by payments related to the CARES Act of 2020, the Consolidated Appropriations Act of 2021 and the American Rescue Plan Act of 2021.

Over the next two quarters, Pietrangeli noted that Treasury's Office of Fiscal Projections estimates privately-held net marketable borrowing of $463 billion and $821 billion, respectively, assuming a cash balance of $800 billion for the end of June and $750 billion for the end of September. Pietrangeli noted that the September cash balance estimate assumes that Congress has taken actions to resolve the debt limit.

Pietrangeli also highlighted the May 3 financing estimates announcement, which notes that Treasury is assuming a cash balance of approximately $450 billion at the expiration of the debt limit suspension on July 31. This cash balance assumption is based on expected outflows under Treasury's cash management policies, is subject to variation based on changes to those outflows, and is consistent with Treasury's authorities and obligations, including the Bipartisan Budget Act of 2019.

Pietrangeli then turned to the primary dealer estimates, which show a median expected privately-held net marketable borrowing requirement in FY2021 of $2.6 trillion. This estimate is significantly below the median expected deficit for FY2021 of $3.3 trillion, largely due to assumptions about the use of cash as a source of financing. Despite these net marketable borrowing needs, primary dealers anticipate Treasury will be overfinanced in upcoming fiscal years and may need to consider coupon cuts either later this year or early next year. Primary dealers added that potential legislation associated with the American Jobs Plan and the American Families Plan introduced uncertainty to their financing outlooks. The dealers noted that the ultimate size of this spending was still unknown, and it was expected to be spread over a decade and offset by proposed higher tax revenues. They suggested Treasury should continue to evaluate the fiscal outlook before considering adjustments to coupon auction sizes.

Next, Debt Manager Lee described more details regarding primary dealers' expectations for Treasury issuance. Given the increases in coupon auction sizes over the past year, dealers expected Treasury to keep nominal coupon auction sizes unchanged for this quarter. As for Treasury Inflation-Protected Securities (TIPS), they expected Treasury to continue to gradually increase auction sizes over the calendar year and suggested that Treasury consider the higher-end of the previously announced $10-20 billion range of increases in TIPS gross issuance for CY2020 if demand remains robust. Dealers argued that for FY2022 and beyond, reductions in nominal coupon auction sizes could help avoid a significant decline in bill supply and were expected across the curve. In addition, some primary dealers suggested that Treasury could consider greater auction size reductions in tenors that appeared to have relatively less demand at auction or that were increased relatively more over the last year.

Deputy Director Steele then summarized responses from the primary dealers regarding the performance of the 20-year bond since its reintroduction in May 2020. Dealers broadly noted that issuance of the 20-year has been well received, but that relative liquidity in the secondary market has been challenged at times, particularly during periods of broader market volatility. Some attributed this to larger issuance sizes than had been expected for the security, while recognizing that the security provided substantial long-term financing capacity for the federal government to respond to the COVID-19 outbreak. Primary dealers were split on whether Treasury should maintain the current sizes of 20-year bond auctions in the near-term or introduce slight reductions in future quarters. Among the primary dealers that supported maintaining the current size of the issue, many noted that liquidity in the tenor is continuing to build over time, and would be bolstered by increased corporate issuance benchmarked to the 20-year bond yield and a potential shift toward higher Federal Reserve System Open Market Account (SOMA) purchases in the sector. Most who supported near-term reductions in the 20-year bond size still suggested making cuts in conjunction with other coupons based on structural financing needs. On the timing of the monthly auctions, a large majority of dealers noted that no change should be made, while a few argued that moving the calendar placement of the 20-year bond auction to later in the month could be beneficial.

Next, Debt Manager Katzenbach reviewed primary dealer views on how the expiration of the debt limit suspension could affect short-term financial markets, as well as their expectations for Treasury bill supply over the next three months. Primary dealers broadly anticipated continued reductions in T-bill supply during between May and July 2021, which several respondents argued could exacerbate any shortage in cash-like investment options. As a result, Treasury bill yields might trade at very low levels in the secondary market. Several primary dealers expected that Treasury could make use of ad-hoc cash management bills around the debt limit reinstatement date as needed.

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 the historically large issuance sizes in recent quarters had generated sufficient financing capacity at this time, and that coupon sizes could likely be reduced later this year or early next year. The Committee debated whether it would be beneficial to make near-term cuts for specific maturity points, such as the 20-year bond, or to hold off on recommending any cuts until it becomes clearer that Treasury should begin more broad-based cuts. After a discussion, the Committee recommended that Treasury maintain current nominal coupon issuance sizes and continue to evaluate borrowing needs over the coming quarters. 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 announced at the November 2020 quarterly refunding, and suggested considering the high-end of the range by increasing the size of 5-year TIPS auctions by slightly more than the increases in other TIPS securities based on relatively high demand.

The Committee then reviewed a presentation on lessons learned from recent episodes of market volatility and stressed liquidity conditions in the Treasury market, examining market structure, dynamics in the non-bank financial sector, and potential ways to improve market functioning during periods of heightened uncertainty. The presenting member began by discussing a few episodes of stress in the Treasury market in recent years. Liquidity across Treasury securities can vary during episodes of stress, and such events do not have easily anticipated drivers, complicating the design of potential policy responses. Given this, the presenting member suggested potential solutions designed to assist Treasury market participants in navigating periods of heightened volatility, rather than attempting to prevent these episodes.

The presenting member concluded by noting that when considering proposed solutions, it is critical to consider the impact in both normal and stressed market environments. The presenting member argued that introducing countercyclical tools could benefit the market in times of stress without material disadvantage to the normal market environment. The presenting member stated that most promising policy proposals were the adjustments to the leverage ratio and the standing repo facility. The Committee discussed the presentation and agreed that several of the solutions were worth further study to improve the resilience of the Treasury market.

The Committee adjourned at 2:00 p.m.

The Committee reconvened at 5:00 p.m. The Chair summarized key elements of the Committee report for Secretary Yellen and followed with a brief discussion of recent market developments.

The Committee adjourned at 5:30 p.m.

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Brian Smith

Deputy Assistant Secretary for Federal Finance

United States Department of the Treasury

May 4, 2021

Certified by:

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Beth Hammack, Chair

Treasury Borrowing Advisory Committee

May 4, 2021

TREASURY BORROWING ADVISORY COMMITTEE QUARTERLY MEETING

COMMITTEE CHARGE – MAY 4, 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.

Treasury Market Functioning

Treasury market liquidity has, at times, been strained during recent episodes of broader market stress. What lessons have been learned in recent years regarding Treasury market structure and vulnerabilities in the non-bank financial sector, and what efforts should be considered to improve market functioning and reduce the need for public sector interventions during future episodes of heightened uncertainty?

Financing this Quarter

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

- The composition of Treasury notes and bonds to refund approximately $47.7 billion of privately-held notes and bonds maturing on May 15, 2021.

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