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iFlow

SHORT THOUGHTS

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Debt Ceiling And Taxes

Tax revenues lift TGA - we think it is enough to last through June

No usual "kink" in the bills curve; very front end richening instead

iFlow data shows significant demand for short-end paper

Tax Collections So Far

Between Wednesday April 12 and Thursday April 20, the Treasury's General Account increased from a paltry $86.5bn to a more comfortable $280bn, thanks to income tax collections during that week. This could move the so-called X-date, when the Treasury would effectively be out of funds to pay its obligations, beyond June, particularly if the Treasury can stay flush through the June 15 quarterly corporate tax collection deadline.

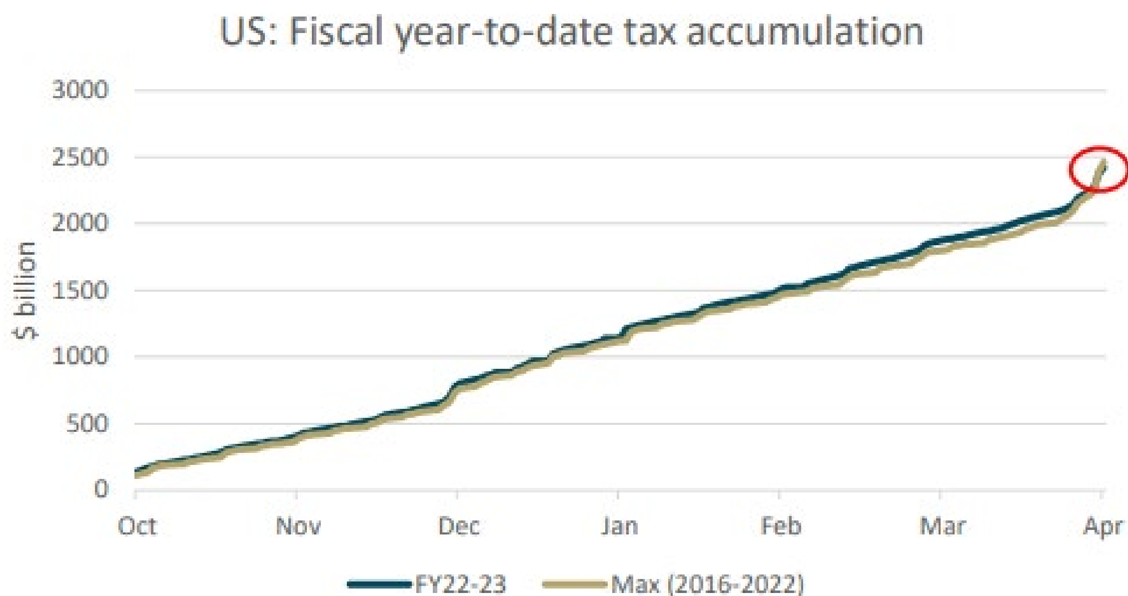
As the graph below shows, since the Oct. 1 beginning of the Federal fiscal year, US tax revenues accumulated through April 20 total $2.42trn, not far off the maximum amount of taxes collected through that date for the last six years. Despite concern of lower capital gains receipts thanks to weak markets in 2022, it appears that so far at least, nominal incomes have been high enough to offset these lower capital gains.

> **X-date projections still could land in June, depending on incoming tax revenue**

At this point, estimates of the X-date still range from early June (which we think is too conservative) through the summer, out to mid- or even late-August. Markets are awaiting the Treasury Department's next announcement of its fiscal position relative to the X-date, which should be coming some time this week or next. That announcement will increase focus on the debt ceiling even more than currently. A tangible deadline tends to focus minds, after all.

Dealings in Washington are slowly heating up. This week it is expected that the House will take up initial legislation, proposed by leadership, to raise the debt limit by $1.5trn – which would extend to approximately March 31, 2023, in return for $4.5trn in spending cuts over the next decade. While reports from DC say this is a political nonstarter for Democrats, it does represent the first attempt to concretely address the issue. In broader terms, it seems that the fate of the debt limit is now in the hands of Washington's protagonists.

On Track



Source: BNY Mellon Markets, Bloomberg, US Treasury

No Kink Yet, But A Plateau Now

Front-end dynamics in the T-bill market are beginning to reflect increased concern over an impeding, if still unidentified, X-date. Typically in previous debt-ceiling episodes, we have seen the bills curve develop a "kink" as it cheapens significantly for issues whose maturities fall during the expected likely window within which Treasury would be approaching default once the money runs out. This time around, there appears less

cheapening in the June-August maturities, and a significant bid for paper closer in and therefore unlikely to be due after the X-date. Note the chart below, which plots current yields for every T-bill on the curve between April 15 and Nov. 2. There is a notable plateau just under 5% for almost every issue after June 1. That 5% is consistent with, and reflects just a small premium to, a 5% terminal rate in the Fed's monetary policy. While the banking sector stresses in March pushed even the very front of the curve lower, we still think rates this summer of 5% to 5.25% are likely, and we see the FOMC pushing the upper end of the fed funds target range up to 5.25% in early May. Thus, we don't think T-bill yields around 5% are reflecting how much lower prices can go as X-date concerns grow.

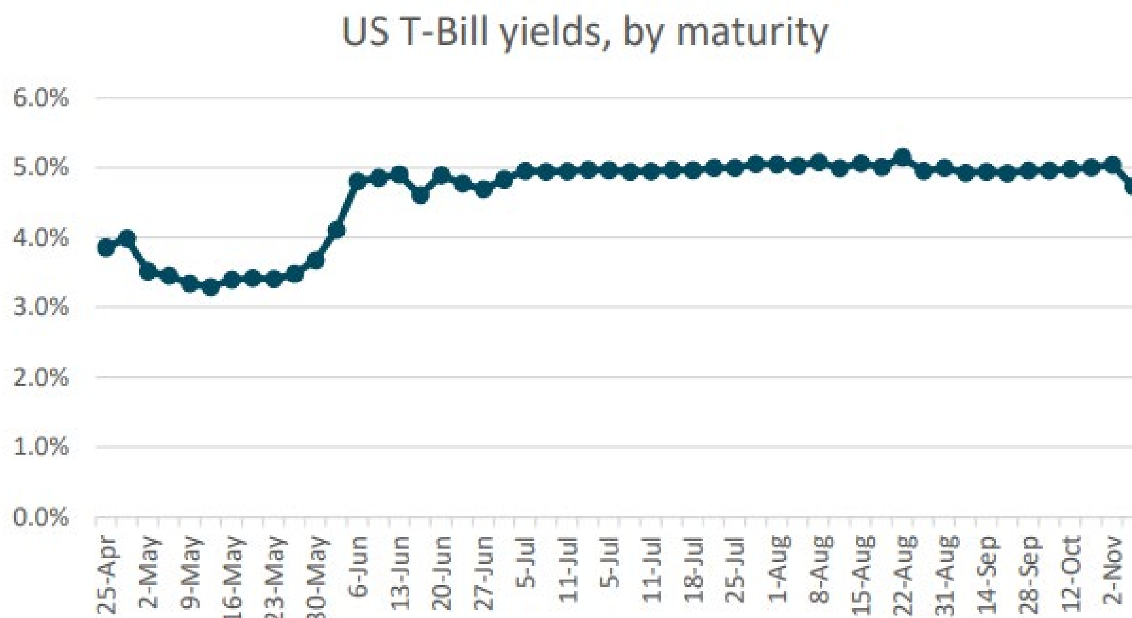
What's more significant to us is how expensive the very front-end has become: bills maturing in May now trade well below fed funds and most money market rates. The June 1 maturity is currently paying just 4.1%. The next, the June 6 maturity, pays 4.8% –- quite a jump. It seems that investors are not willing to tempt fate much beyond the beginning of June.

> **Summer maturities for bills are trading cheap, but yields still close to 5%**

Combined with lack of T-bill supply between now and whenever the debt ceiling gets resolved (after which we expect a flood of new bill issuance), the considerable uncertainty in policy and the debt ceiling itself, plus the persistent, pervasive glut of cash in the system, participation in the Fed's overnight reverse repurchase facility remains unbridled.

We think it's too early to worry about the flood of issuance that would presumably come once the debt ceiling is resolved, preferring instead to focus on what we think will be a tricky path between now and resolution. However, getting through to some sort of resolution/extension isn't likely to be the end of the distortion in the money markets. Renewed issuance at a fast clip would see the TGA rebuilt, putting pressure on liquidity and reserves, and the deposits that have "flown" out of large banks into money funds, might not rush back in as these funds would then have a plethora of Treasury securities in which to invest.

In Line With Fed Rate Expectations



Source: BNY Mellon Markets, Bloomberg

Elevated Front-End Demand Persists

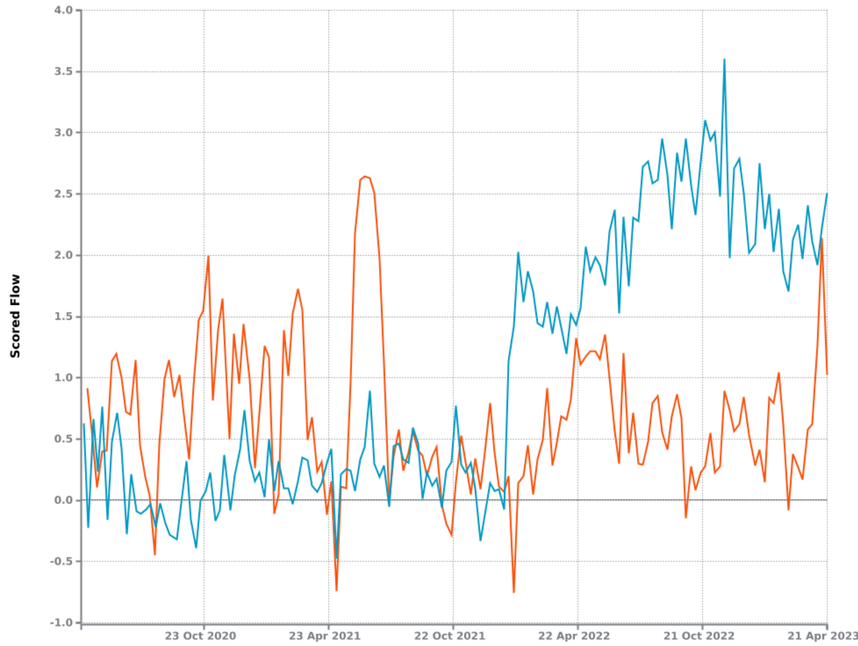
We have written a great deal about the glut of cash in money markets and have shown how our iFlow data can capture this activity. We can examine fixed income flows in US markets by their maturity, including paper coming due in less than one year, and break that down into cross-border and total activity. The chart below shows these data for last three years. Note that at around year-end 2022, there had been a substantial pickup in investor demand for this short-duration paper. By the end of last year, total flows were as high as 3 standard deviations above normal. These flows have only slightly relented and are still quite positive.

> **No let-up in demand for short maturity rates**

Foreign (i.e., cross border) inflows have also been evident since the end of 2022, but at a generally lower rate – even though they have remained positive. There was a noteworthy spike in foreign demand very recently, although that has moderated somewhat in the past week (note that we are showing weekly scored flows). We don’t see much to indicate that these flows into the short end of money markets will relent anytime soon, at least until uncertainty around the debt ceiling and Fed policy is resolved.

Staying In Short Maturities

FI Scored Flow



Scored Flow
INVESTOR BASE
CROSS BORDER

FI
SUBCLASS TOTAL | MATURITY < 1 YEAR

Averaged | Weekly

United States

Scored Flow
INVESTOR BASE
ALL

FI
SUBCLASS TOTAL | MATURITY < 1 YEAR

Averaged | Weekly

United States

DATE RANGE:
04.27.2020 — 04.21.2023

Source: BNY Mellon Markets, iFlow

Please direct questions or comments to: iFlow@BNYMellon.com

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