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iFlow

SHORT THOUGHTS

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Refilling The Coffers

So Far, So Good...

The US Treasury's General Account (TGA), has increased from a low of $23bn on June 1, during the final stages of the debt-ceiling impasse, to $250.4bn this past Thursday, the latest date for which we have information. Much of the rebuild, expected to total $425bn by the end of this month, has been accomplished by $180bn in net T-bill issuance from the fiscal authorities. Approximately an additional $40bn (estimated) in net Treasury revenues has also helped out with the replenishment of the government’s coffers over that period of time.

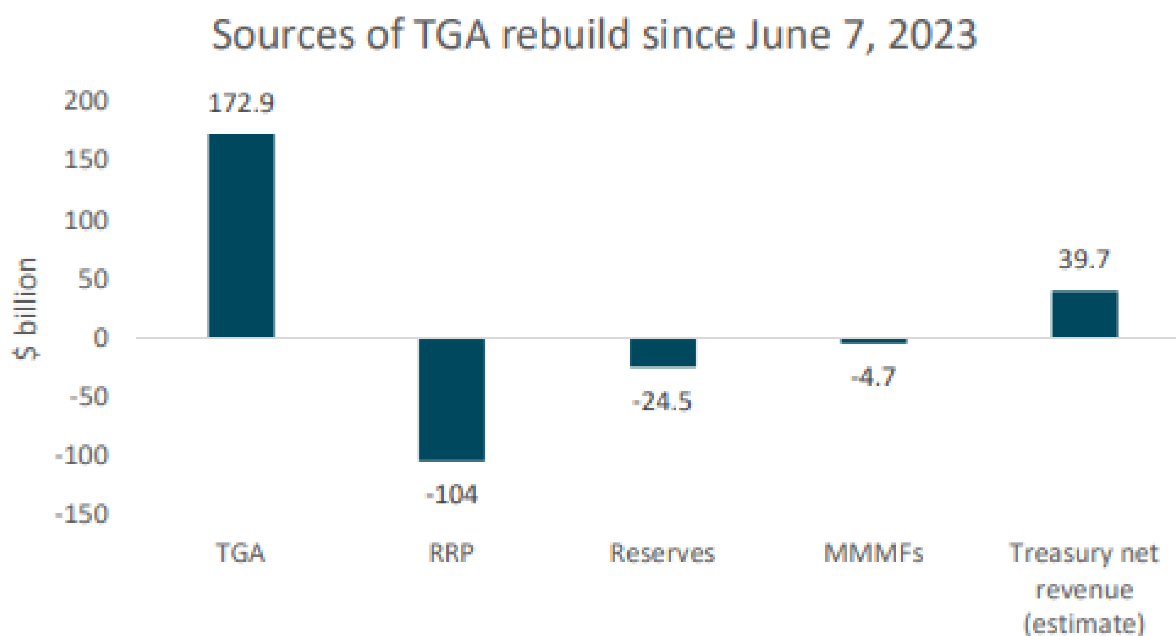
The question had always been how much of the TGA refill would come from the transformation of near-record money market mutual fund (MMMF) monies coming from the overnight reverse repo facility (RRP) at the NY Fed, which would entail no reduction in bank reserves, and how much would come out of reserves themselves. The RRP facility is down $104bn since June 7, suggesting that over half of the TGA rebuild was indeed financed by this transformation of MMMF assets. June 15 was a federal corporate tax payment date. Given that much of the monies to pay corporate tax came out of corporations’ MMMF holdings and flowed into the Treasury, we should not read too much into the data from June 15, the latest date for which we have data. RRP takeup last Thursday was just $1.9trn, the lowest level in over a year. Indeed, on Friday last week, RRP rebounded to $2.01trn.

The chart below shows cash movements among the TGA, RRP, bank reserves and

MMMFs since June 7. On that date (data are reported weekly for every Wednesday by the Investment Company Institute), MMMFs held a record $5.46trn. By the following week (June 14) that was down by $4bn. The lion's share of the TGA rebuild indeed appears to have come from the asset transformation described above, out of RRP and into T-bills.

Given that Treasury's initial target for the TGA by the end of the month is only about $50bn away, this should be accomplished relatively smoothly, without any stresses so far in money markets. Indeed, this operation has been minimally disruptive to date, post the debt-ceiling event. Ultimately, Treasury has indicated that it wishes to achieve a TGA of around $600bn by the end of the summer, meaning more issuance will need to be absorbed by the market.

From RRP Into TGA



Source: BNY Mellon Markets, Bloomberg

..But What Happens After Summer Is Over?

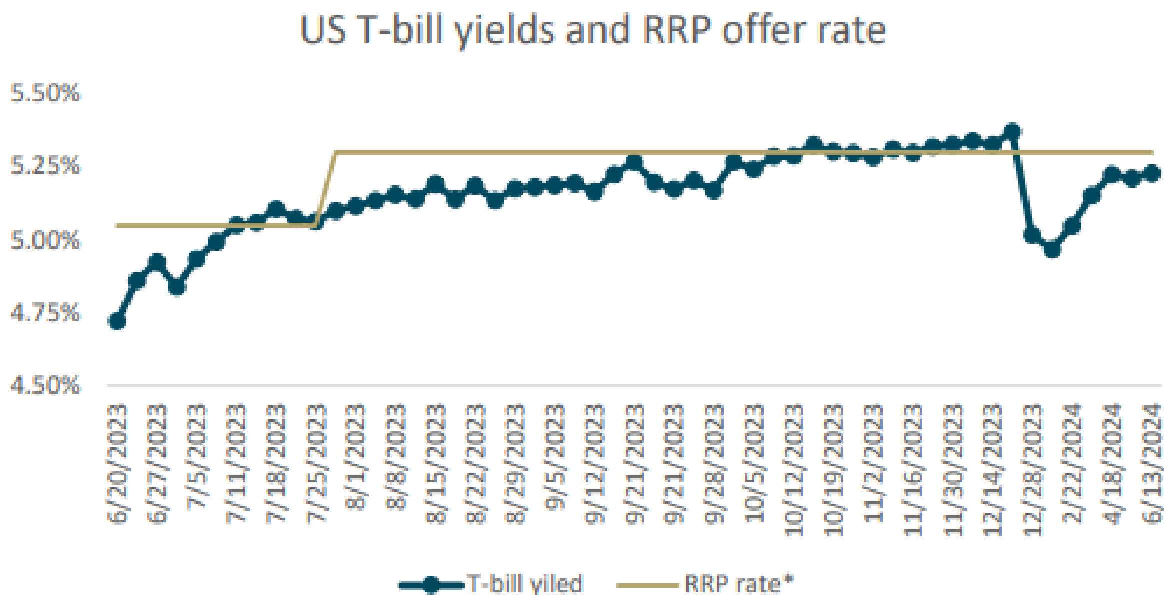
Given that the RRP facility has drained significantly over the last week or so, to the tune of over $100bn, we might be tempted to think that the additional issuance to come over the rest of the year (which is estimated to be over $1 trillion) will be easily financed by this transformation of RRP into bills. However, we caution – and we don't yet know the Treasury's borrowing plans in detail for Q3 and Q4 – that this might not be the case after the summer, or even in July and August.

With uncertainty over the Fed's next move(s), we aren't convinced that money funds will be tempted to snap up bills with summer maturities. Why buy an August bill yielding less than 5.30% when there is a good chance that there will be a July 26 rate hike, which would presumably bring the RRP offer rate to 5.3%. While we think that the Fed may only have one more rate hike in store, in July, that the latest Summary of Economic Projections sees at least two more 25bp moves is enough to engender caution on the post-July bills.

The chart below shows the yield on every T-bill currently in the market well past this summer. We also superimpose our estimate of the RRP offer rate, under the assumption of a Fed move at the end of July. There are not a lot of attractively priced issues out there. We therefore don't share the opinion of many in the market who foresee significant declines in RRP usage over the summer. Not until Fed policy uncertainty is behind should we expect to see any further big moves out of the overnight facility.

This suggests there will be pressure on reserves going forward – and does not even include any views on how much the rest of the existing funding needs of the government will be addressed by bills and/or coupons. We also, relatedly, see pressure on coupon yields in the second half of the year, certainly by the autumn months.

Bills Curve Still Below Expected RRP Rates



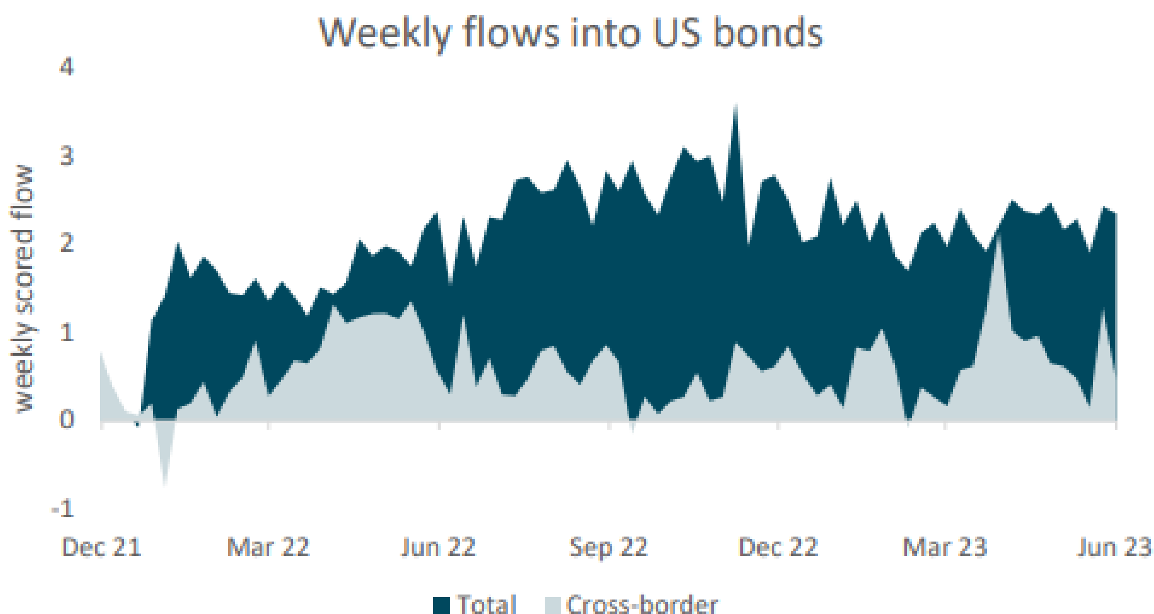
Source: BNY Mellon Markets, Bloomberg
** Estimated after July 26, assuming a 25bp federal funds rate hike*

Cash Ready To Go?

We have frequently commented on heavy cross-border selling of US Treasury bonds, but have also mentioned that foreign investors remain engaged in short-term paper. Indeed, both total flows (including the domestic and cross-border components) remain quite high.

The chart below shows both total and cross-border flows (per our iFlow data) into all US bonds less than 1y in maturity. Total flows are and have been very strong since early 2022. The pervasive and persistent loading up on cash-like instruments has been a consistent feature of our iFlow data. In the context of what we discussed above, this is important. How much of these cash-like holdings (which in our data do not represent MMMF flow) will be transformed into bills and/or coupons will be crucial as we look for which players will have sufficient appetite and funds to take down roughly $1 trillion more in issuance.

Piling Into The Front End, Still



Source: BNY Mellon Markets, iFlow

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

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