

Presentation to the Treasury Borrowing Advisory Committee



UNITED STATES
DEPARTMENT OF
THE TREASURY

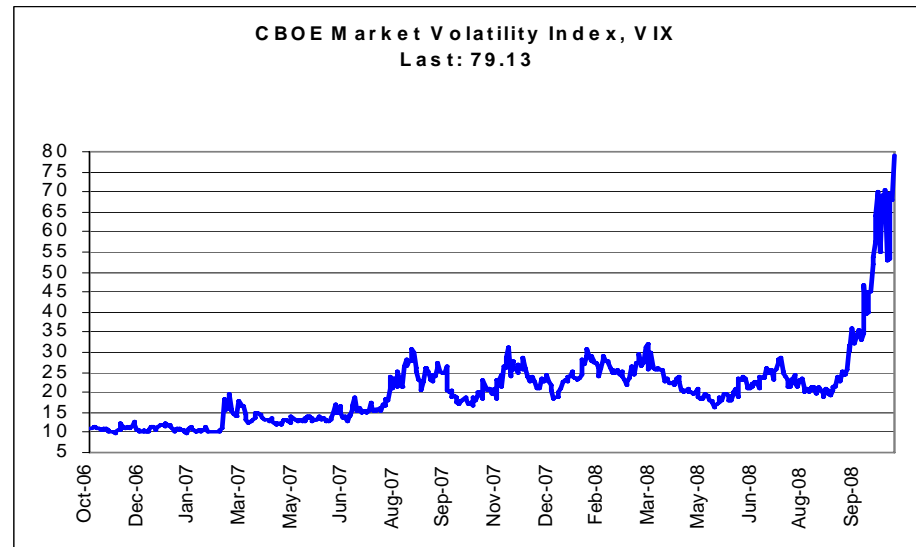
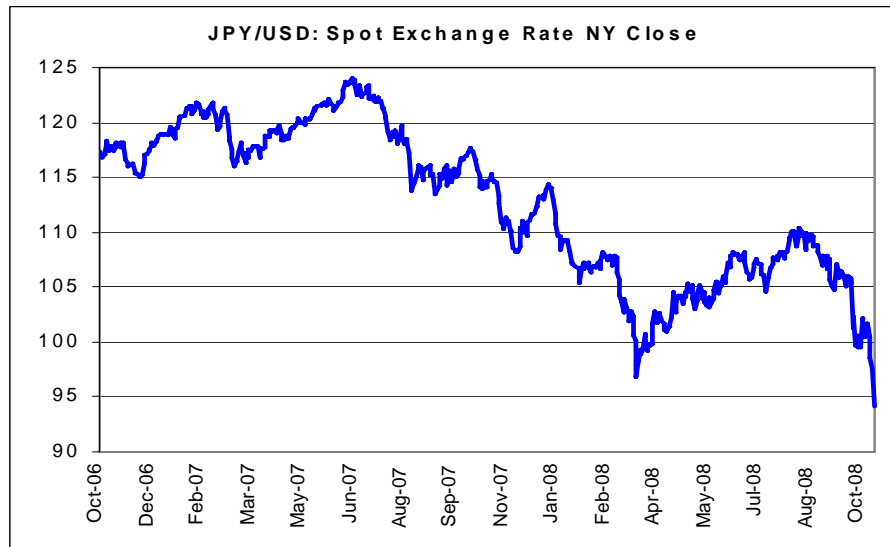
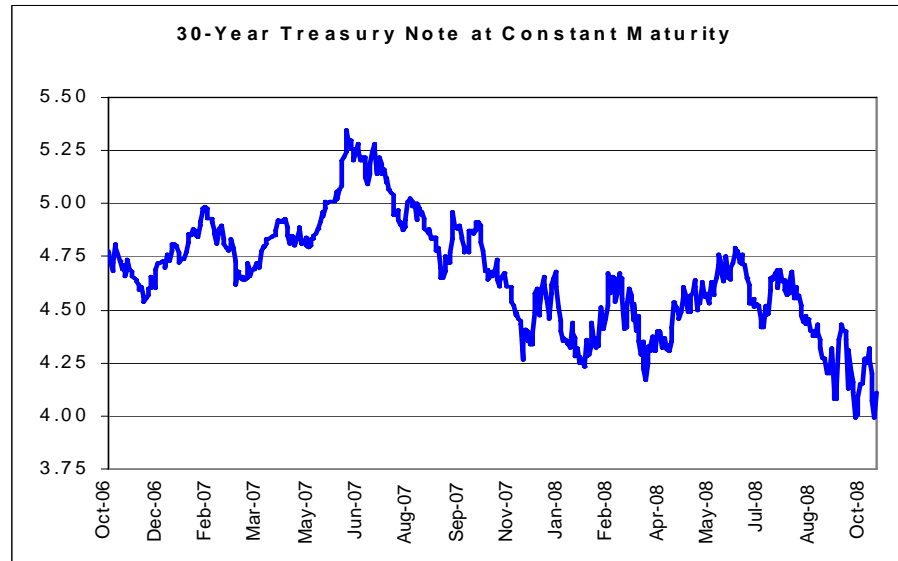
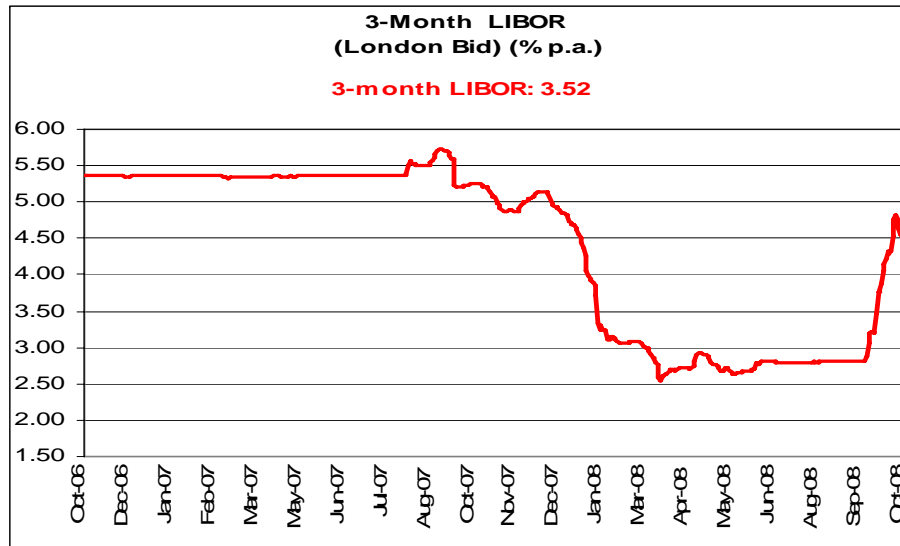


U.S. Department of the Treasury
Office of Debt Management
November 4, 2008

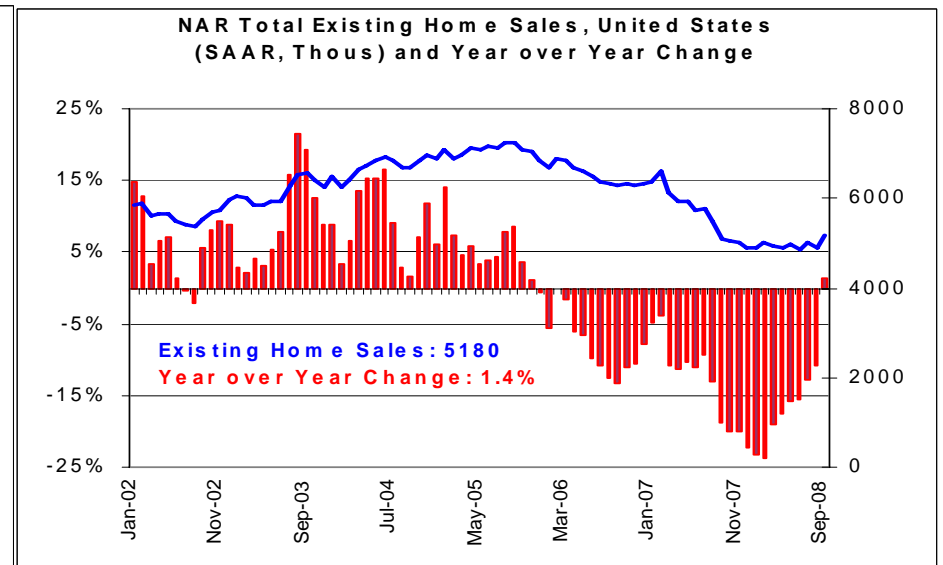
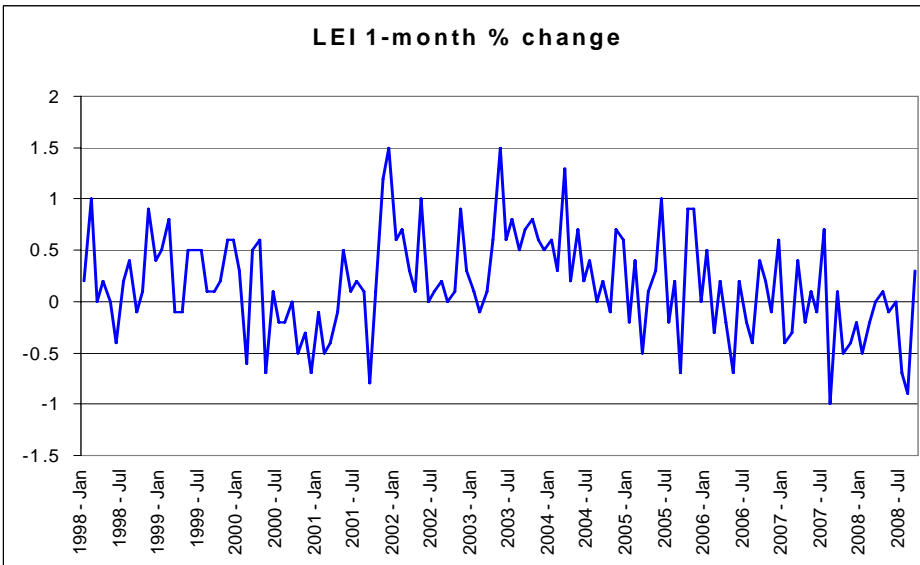
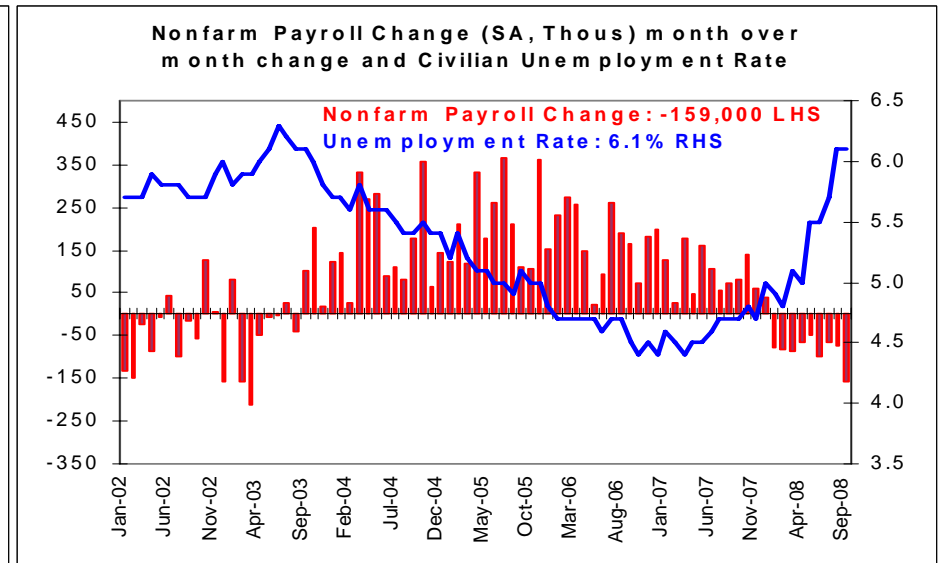
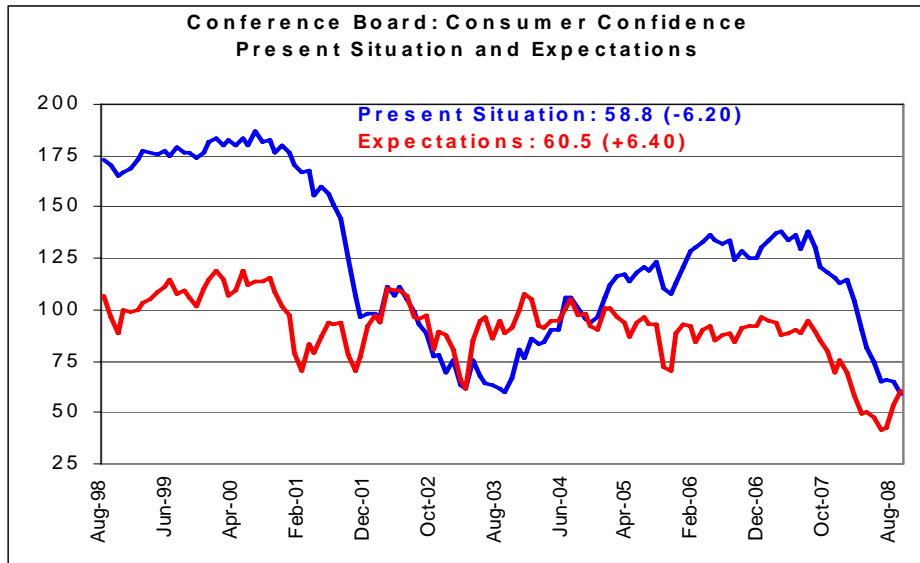
Fiscal Outlook



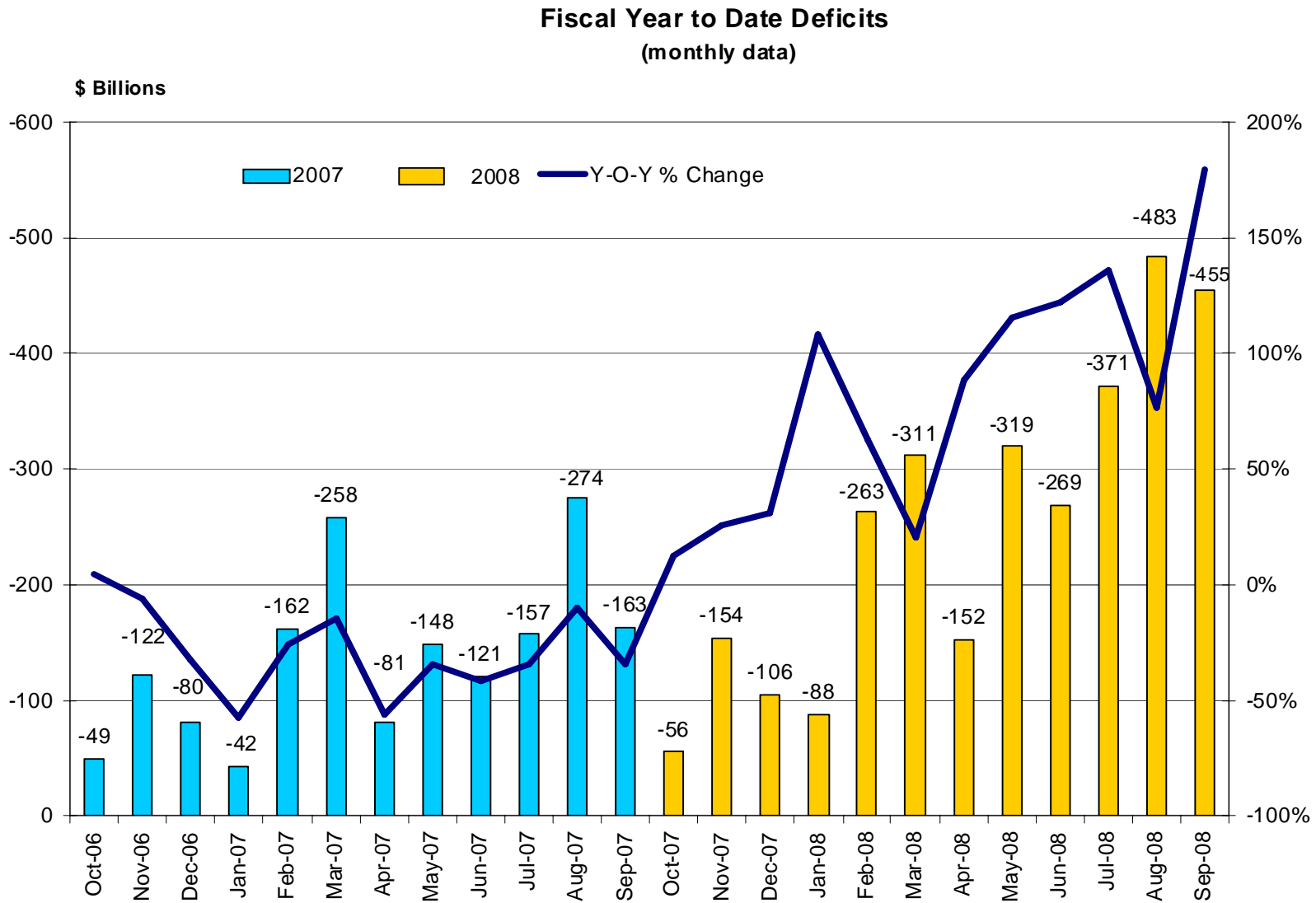
Volatility across credit markets remains though there have been signs of pressures easing



The economic outlook continues to present challenges

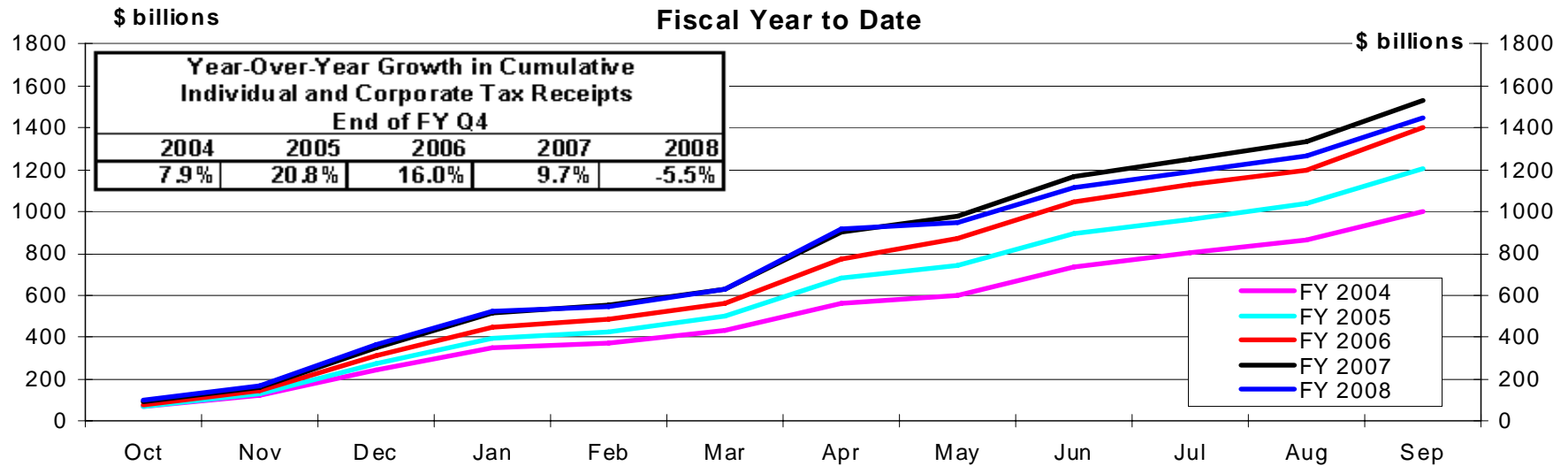


From a fiscal perspective, borrowing requirements have steadily increased

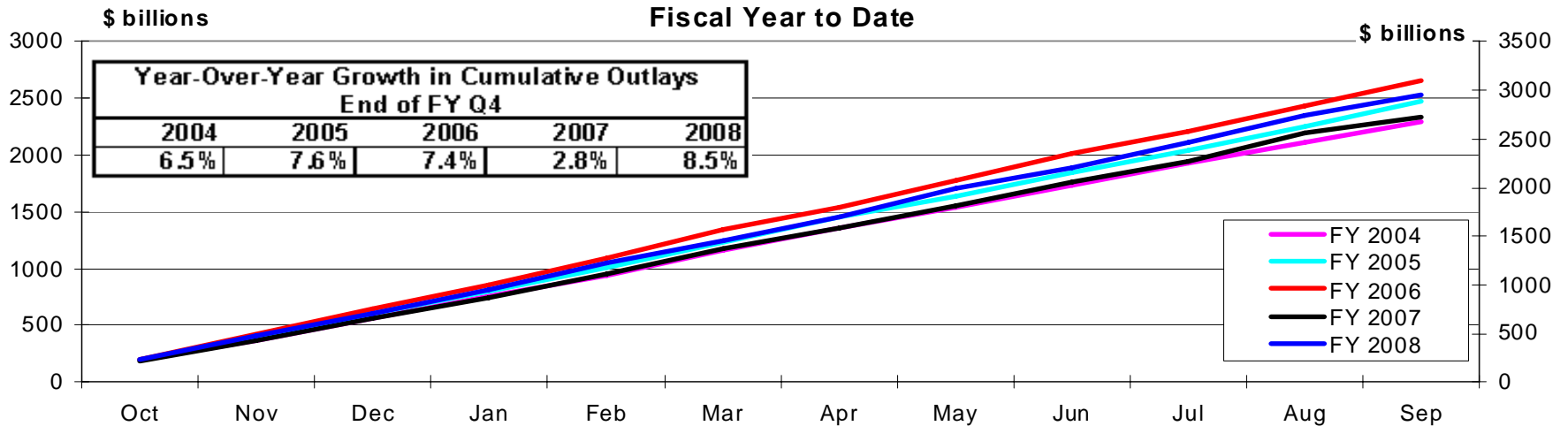


In FY08, growth in receipts was negative for the first time since FY03, and growth in outlays accelerated to its highest pace since FY06

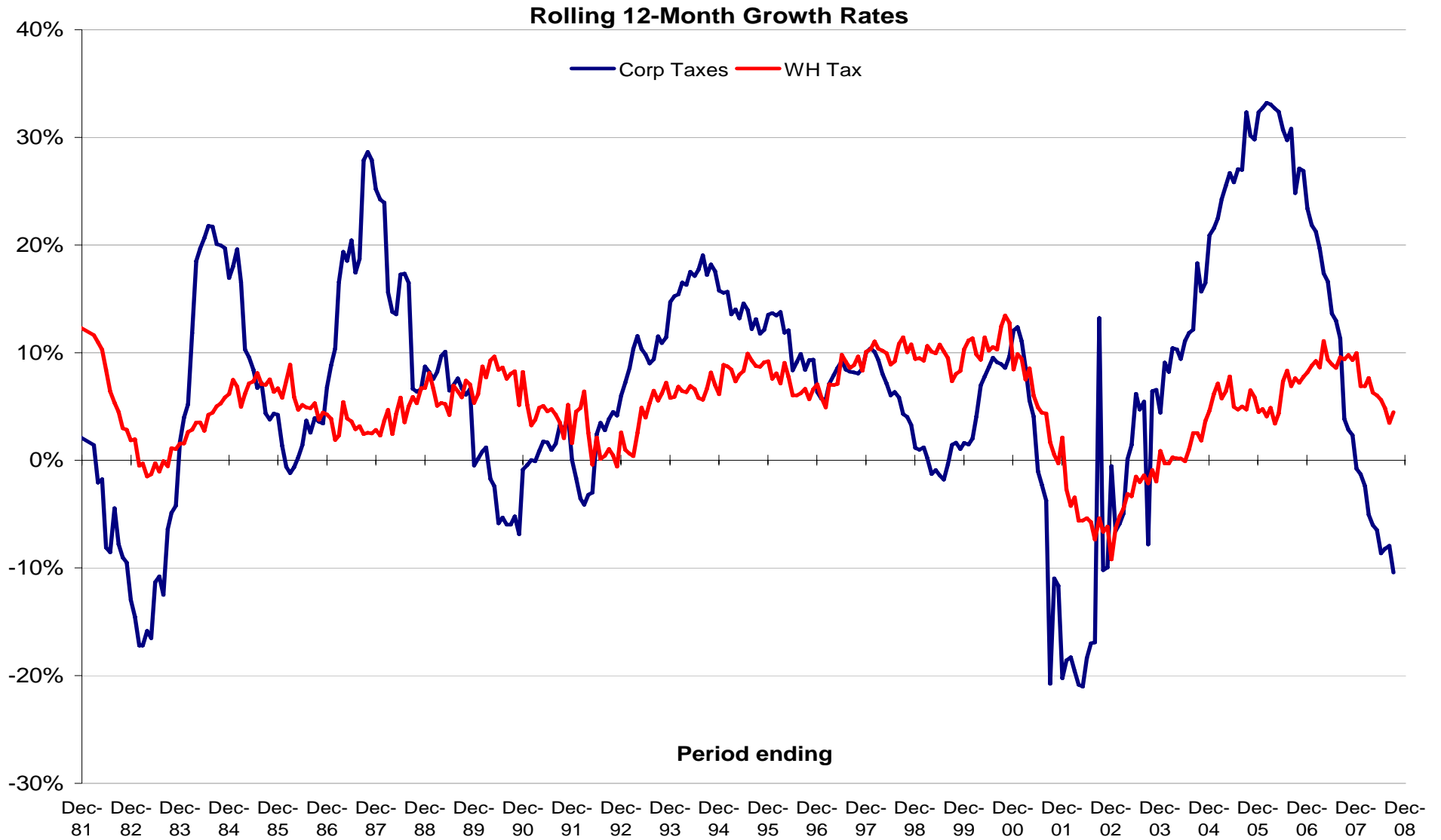
Individual and Corporate Tax Receipts



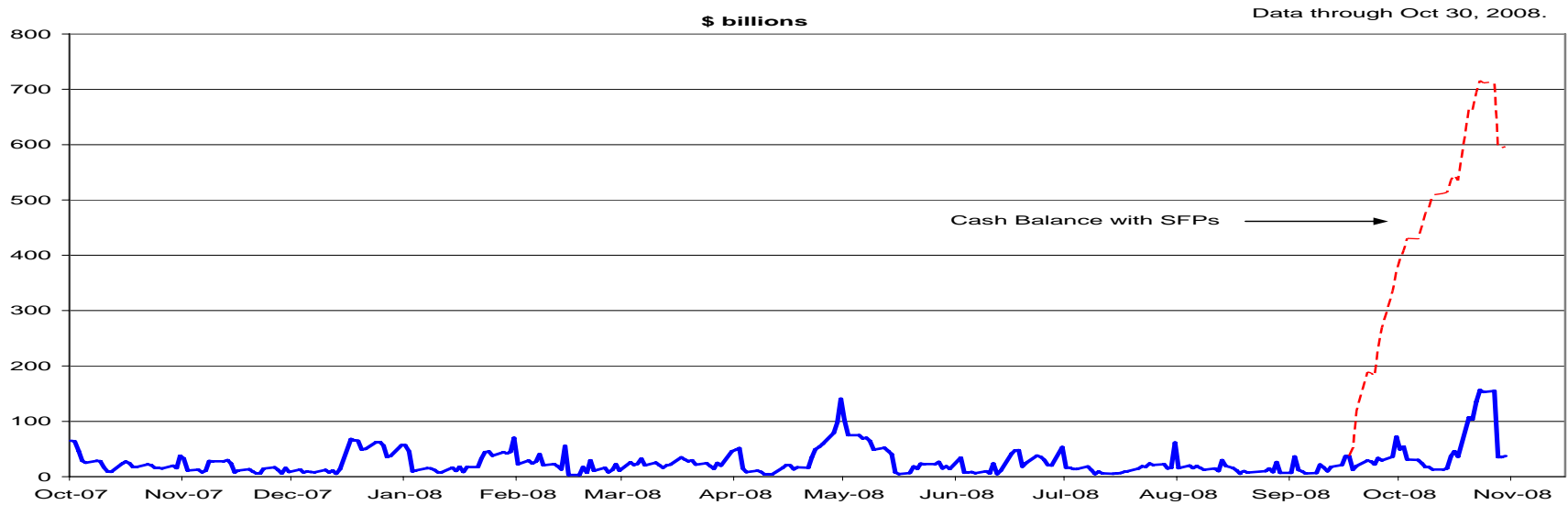
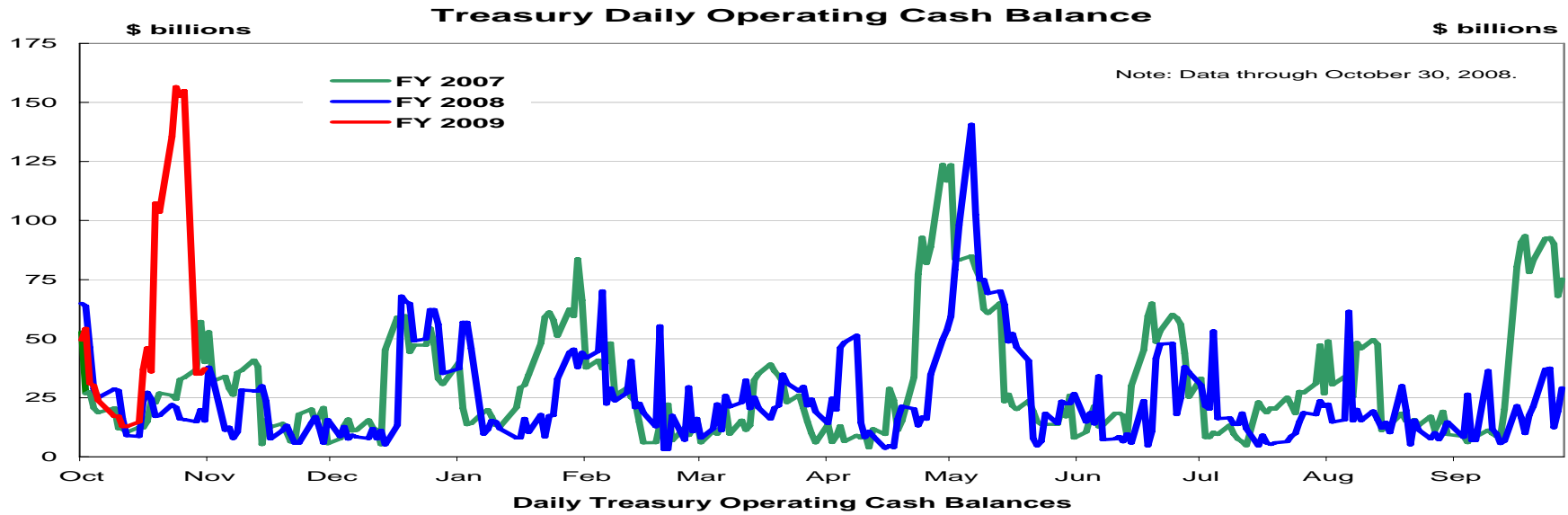
Total Outlays



Withheld and corporate tax receipts continue to decelerate



Mitigating volatility in cash balances remains challenging



Primary dealer estimates of the FY 2009 deficit rose to \$988 billion, and marketable borrowing estimates range between \$1.1 trillion and \$2.1 trillion

FY 09 Deficit Estimates

\$ billions

	Primary Dealers*	CBO	OMB
Current:	988	438	482
Range based on average absolute forecast error**	863 - 1,113	338 - 538	391 - 573
FY 2009 Marketable Borrowing***	1,400	-	-
FY 2009 Marketable Borrowing Range***	1,100 - 2,100	-	-
Estimates as of:	October 08	September 08	July 08

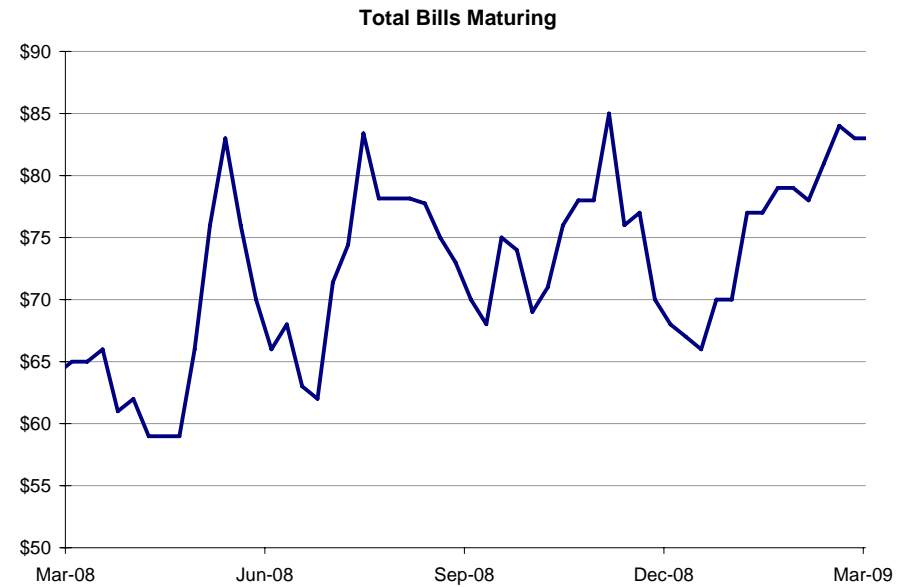
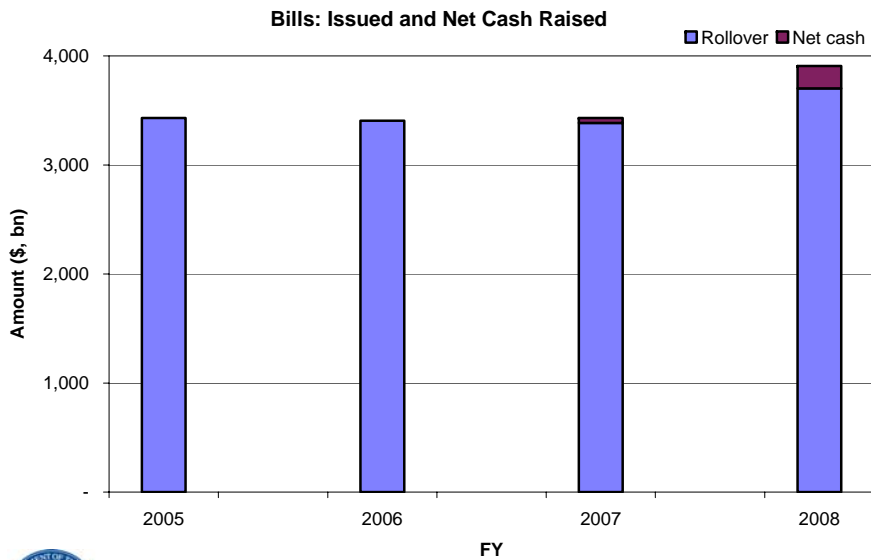
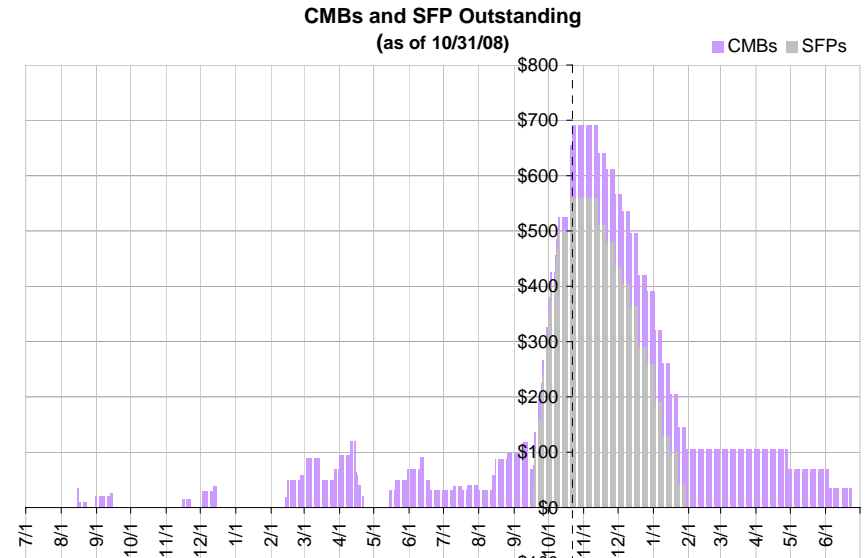
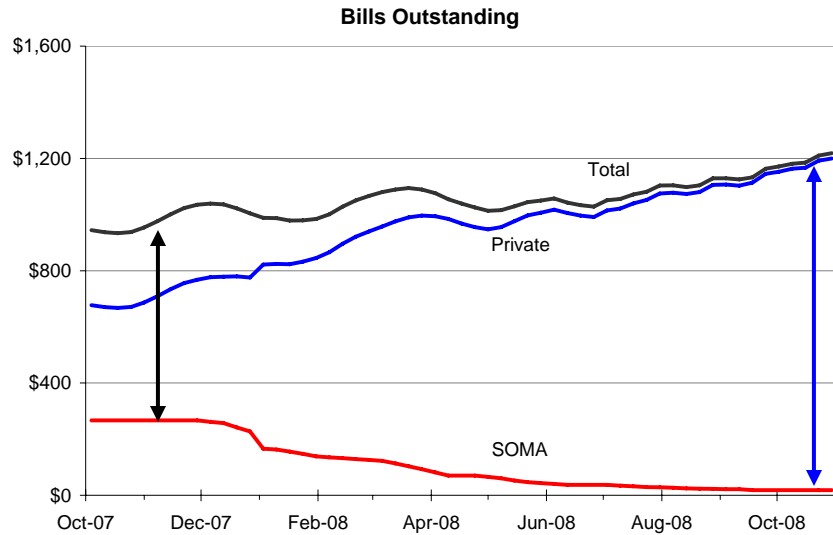
* Primary Dealers reflect average estimate.

** Ranges based on errors from 2004-2008.

*** Based on Primary Dealer feedback on October 30, 2008.

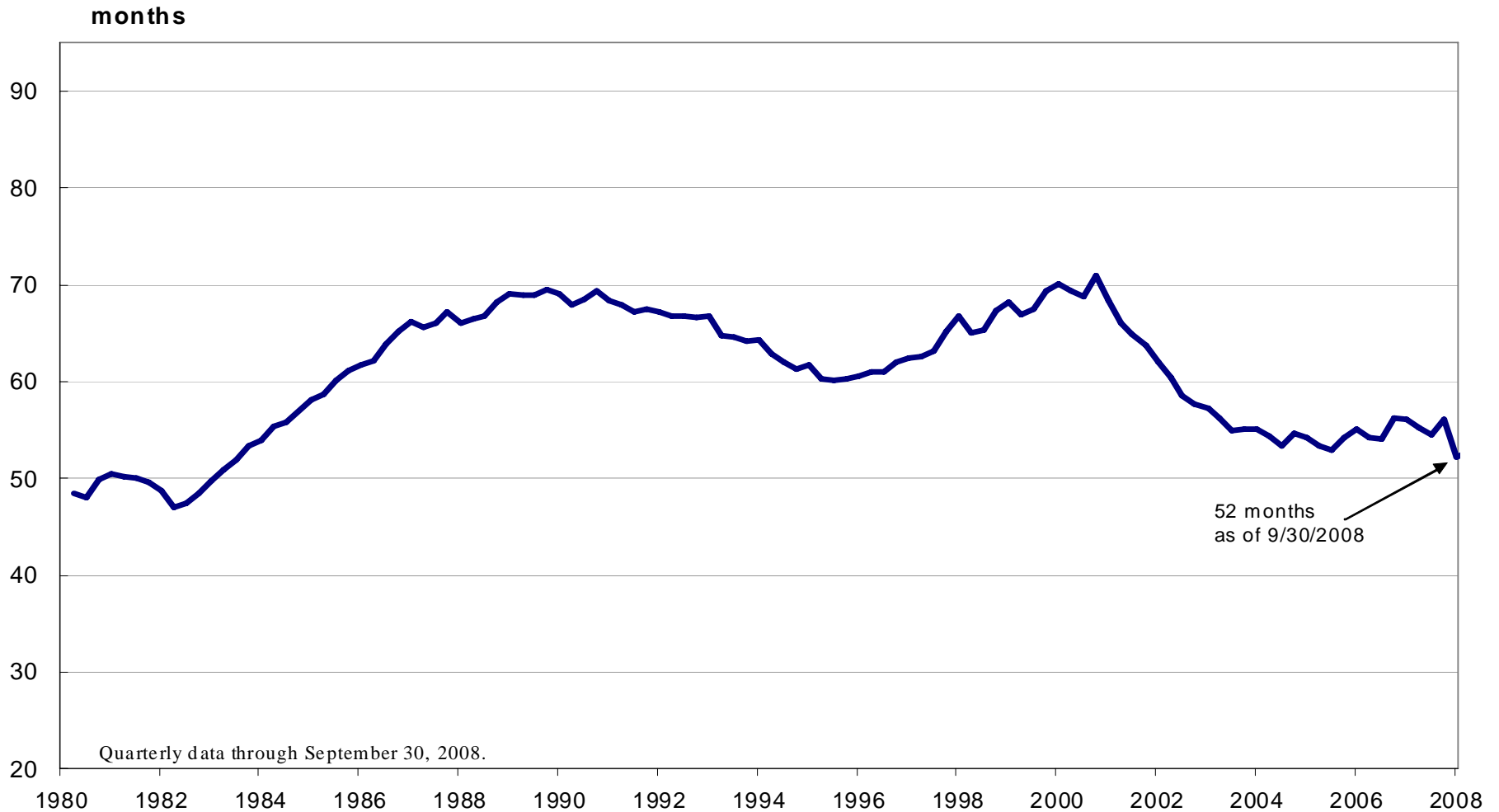


The decline in SOMA bill holdings, SFP related financing, and funding needs, have led to higher bill issuance, including cash management bills



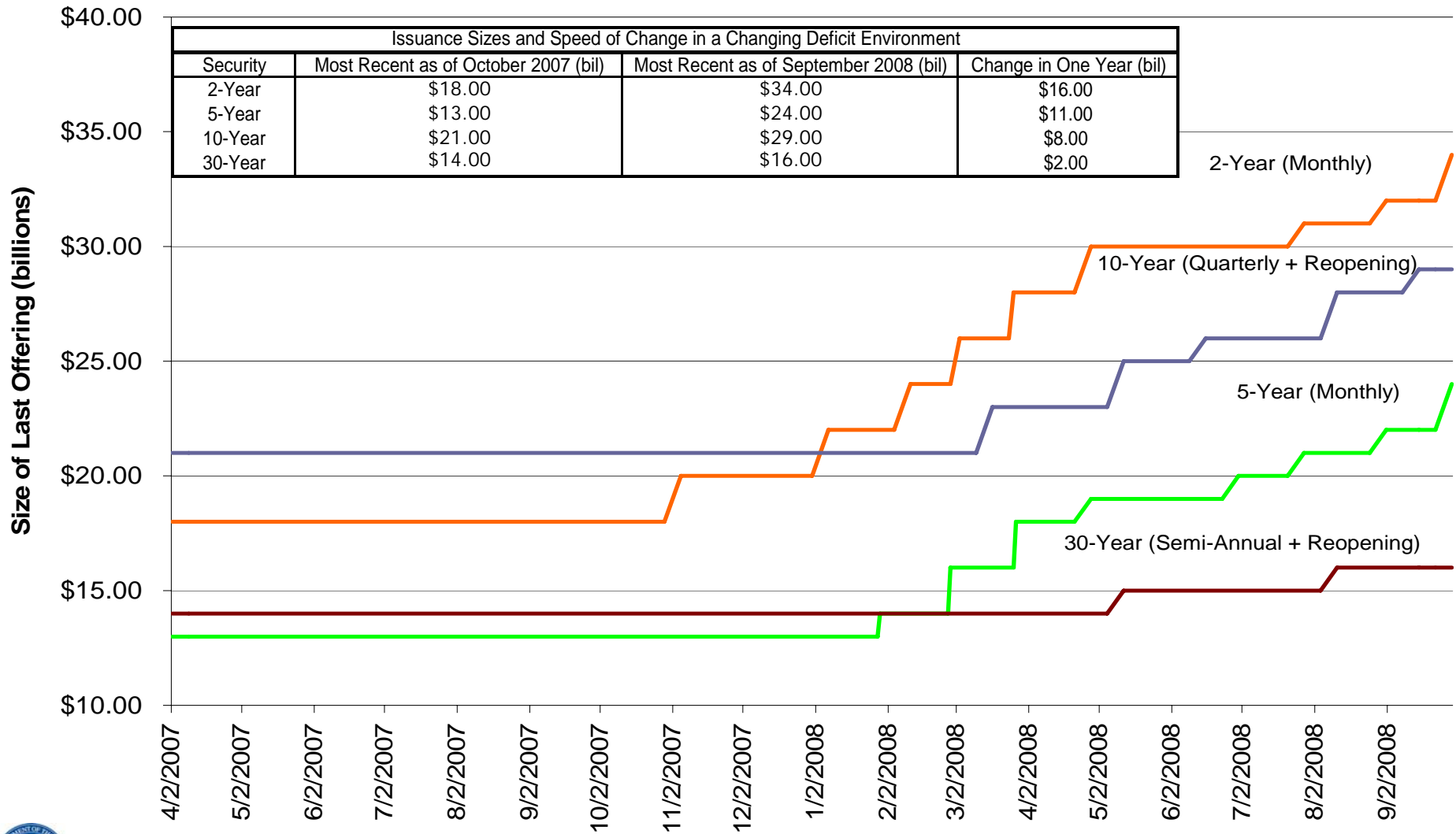
The average maturity of marketable debt outstanding fell between August 31 and September 30 as short-term issuance increased

Average Maturity of Marketable Debt Outstanding

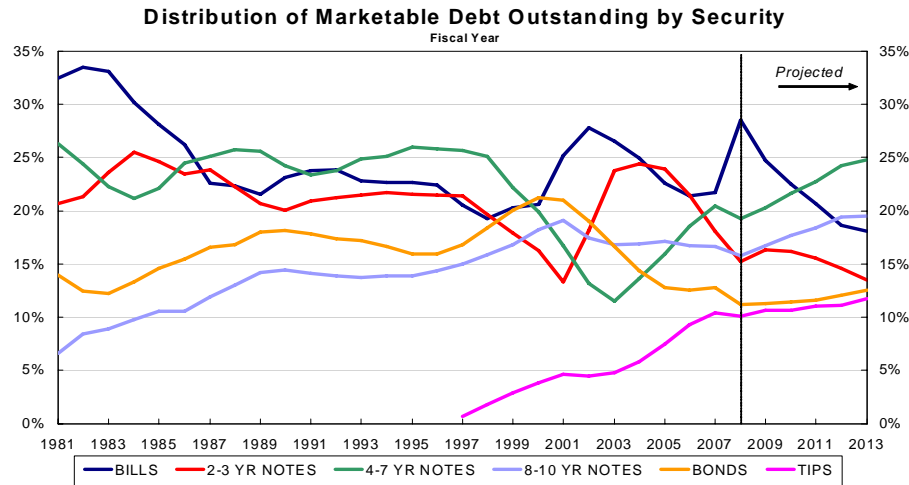
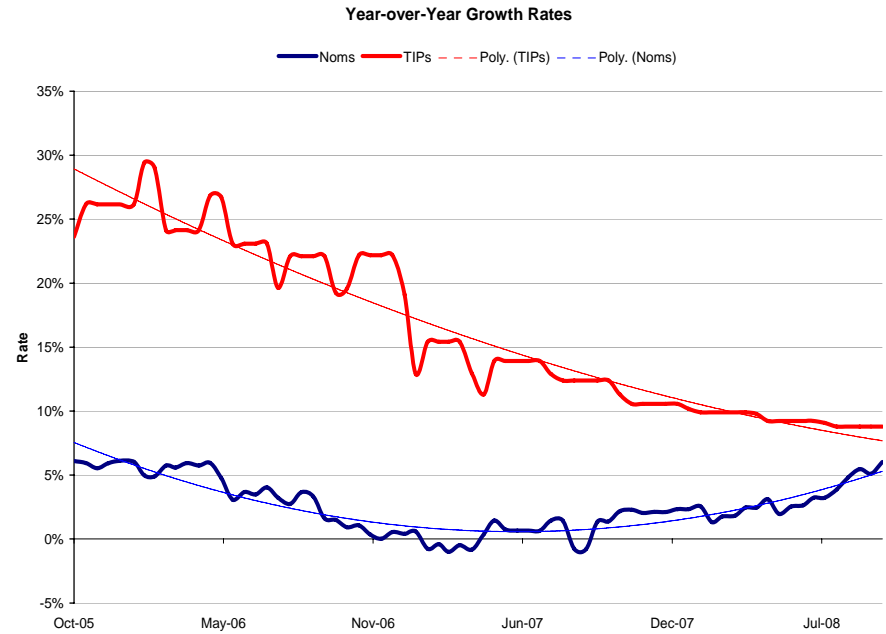
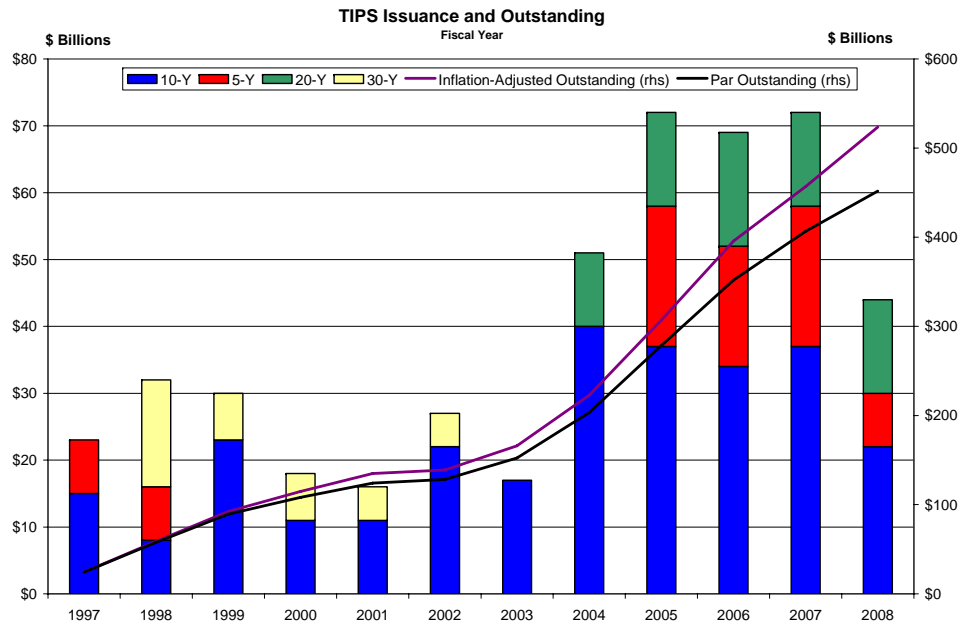


Nominal coupon security issuance has also been increased in response to borrowing needs

Coupon Issuance in 2007-2008



TIPS' share of the outstanding portfolio has stabilized at 10%



Net financing projections for FY 2009-2013 are based on OMB 2009 MSR Budget estimates. Future residual financing needs are spread proportionally across auctioned securities and are derived from hypothetical auction sizes. Initial sizes are based on announced coupon amounts as of September 30, 2008 and assume the outstanding level of bills on September 30, 2008. All projections exclude CMB issuance and maturing amounts.



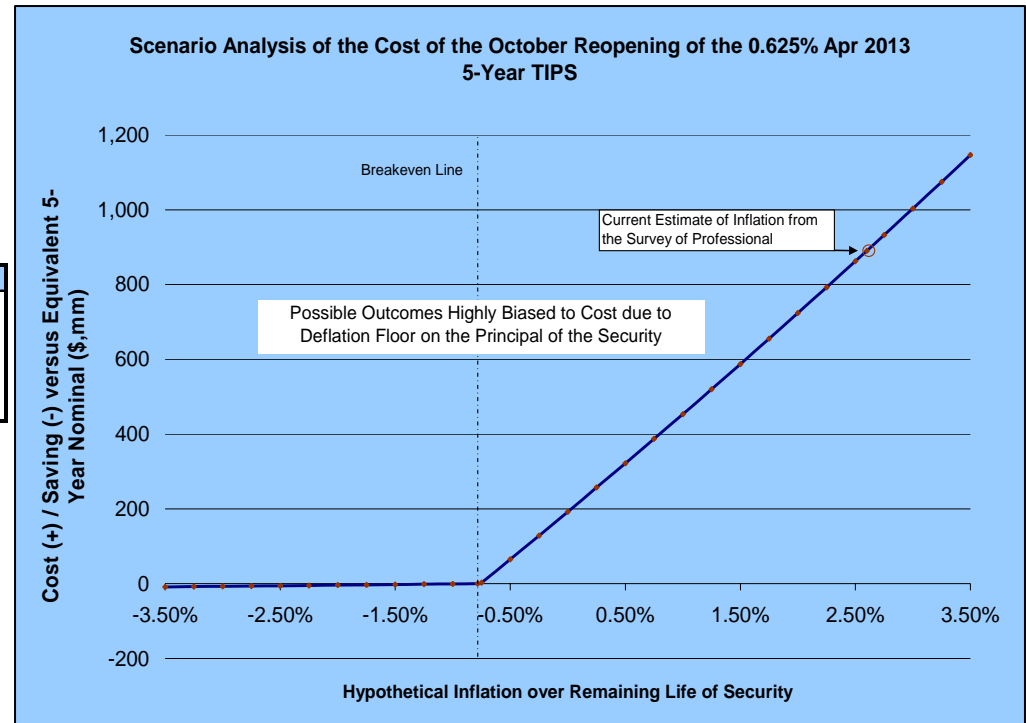
Several estimates indicate that shorter dated TIPS are less beneficial from an issuer and investor perspective

Investor Class at Auction Breakdown by Security since 2001

Security	Depository Institutions	Individuals	Dealers & Brokers	Pension & Retirement funds & Ins.	Investment Funds	Foreign and International	Other	Auctions
Average	1%	2%	56%	1%	32%	8%	0%	45
5	0%	1%	62%	2%	26%	10%	0%	8
10	1%	2%	58%	1%	29%	8%	0%	28
20	0%	1%	45%	1%	46%	6%	0%	9

TIPS Program Cost Estimates

Study	Cost Estimate (bn, \$)	Date of Estimate	Study Type
Sack/Elsasser	2.8	Through June 2003	Ex Post
Sack/Elsasser	12.3	Through June 2003	Ex Post + Extrapolation
Roush	5 - 8	Through February 2007	Ex Post
Roush	8 - 17	Through February 2007	Ex Post + Extrapolation
TBAC	30	Through July 15, 2008	Ex Post

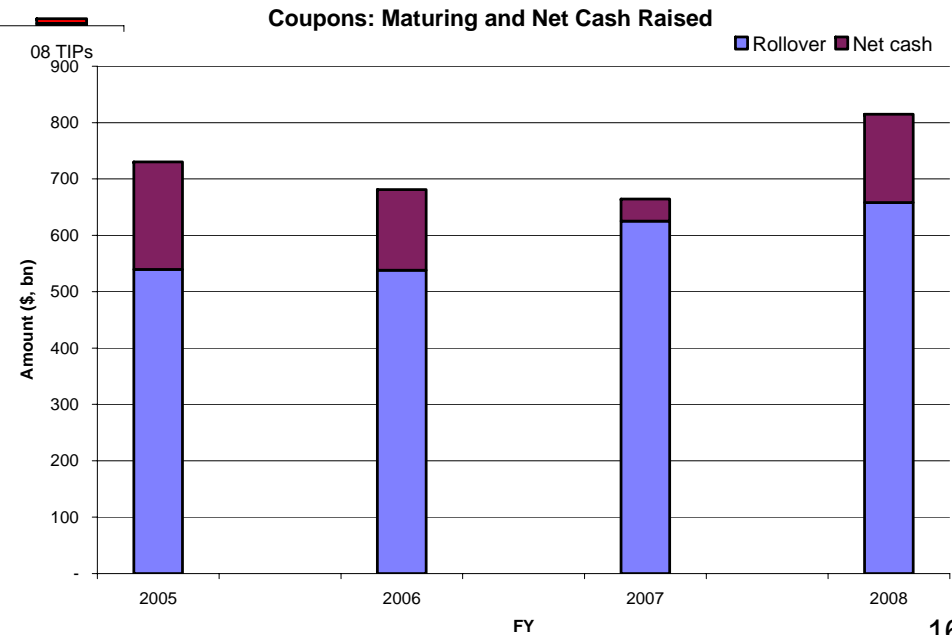
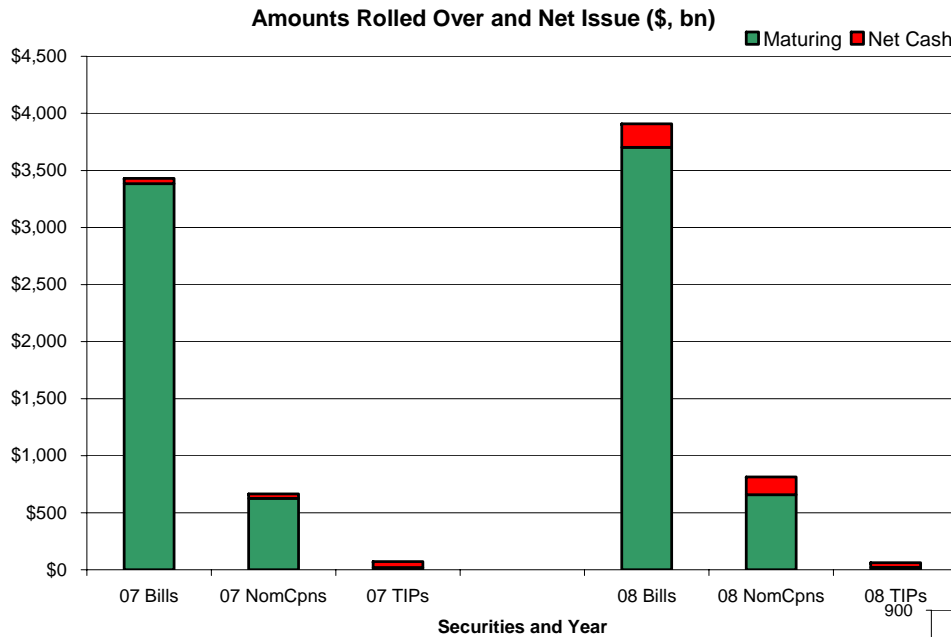


Adjusting the auction calendar should be considered to address borrowing needs while minimizing costs

<u>Security</u>	<u>Recent Size, \$ Billions</u>
4-week, 13-week, and 26-week bills	34, 27, 27
52-week bills	21 per month
2-year note	34 per month
5-year note	24 per month
10-year note	29 (17 initial + 12 reopening)
30-year bond	16 (10 initial + 6 reopening)
5-year TIPS	14 (8 initial + 6 reopening)
10-year TIPS	14 (8 initial + 6 reopening)
20-year TIPS	14 (8 initial + 6 reopening)
Cash Management Bills (including SFP)	37 (average size in FY 2008 thru Nov. 5)



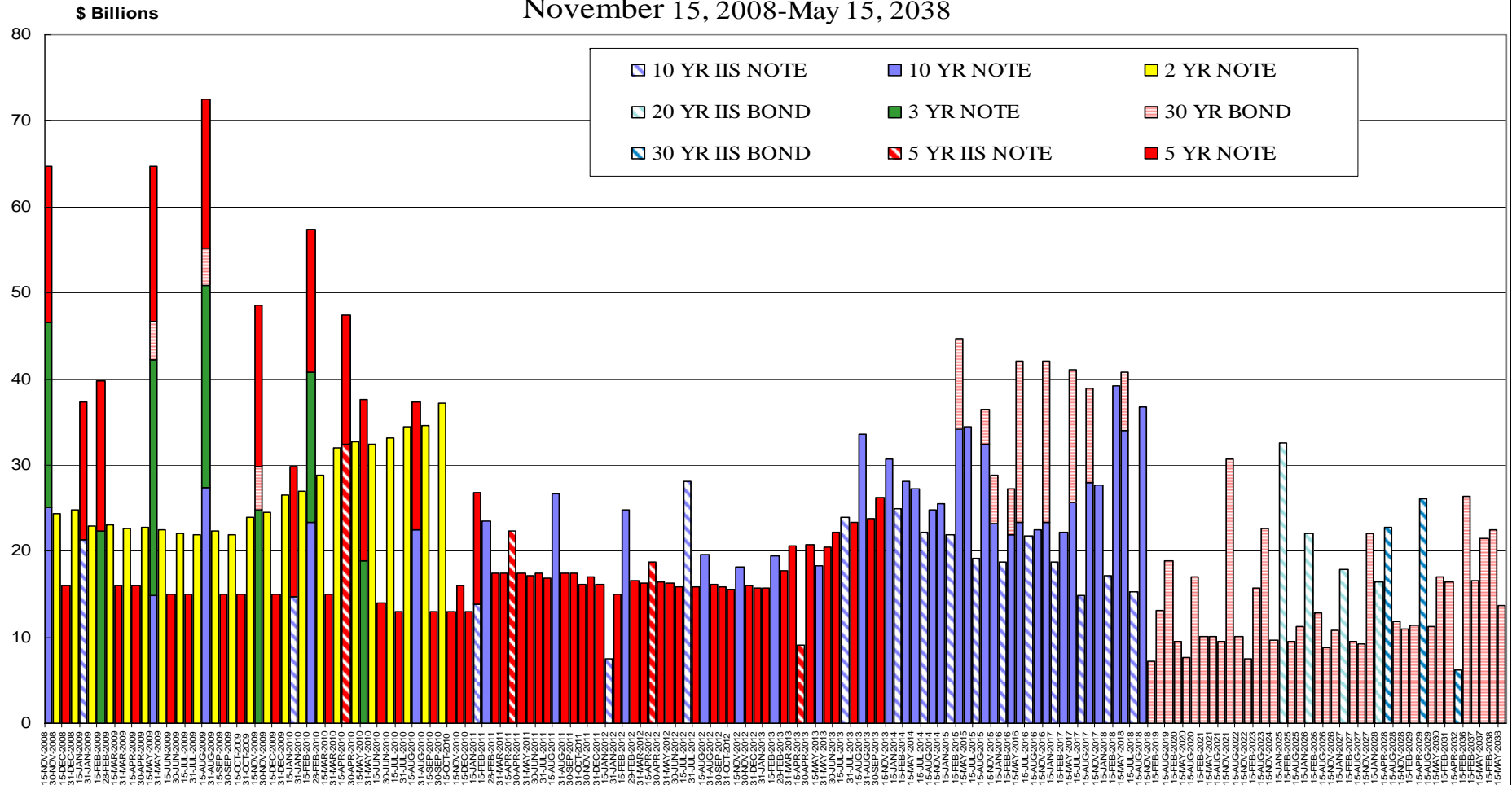
Coupons can be adjusted to raise additional cash



In FY 2009, maturing securities add to financing needs

Coupons Maturing*

November 15, 2008-May 15, 2038



*Based on coupon securities outstanding as of October 15, 2008.



Given Treasury's financing needs in the coming years as well as current and medium-term trends in the fiscal and economic outlooks, what are the Committee's thoughts on Treasury's debt issuance?

What changes to the auction calendar do you recommend Treasury make at this time?



Treasury Cash and Debt Management Tools



Existing Cash and Debt Management Tools

Cash Management Tools

- Treasury Tax and Loan (TT&L)
- Treasury's Term Investment Option (TIO)
- Repurchase Agreement Program

Debt Management Tools

- Auction schedule
 - Amount
 - Frequency
 - Adding/Discontinuing Securities
- Treasury Debt Repurchases



Private sector solutions need to be implemented to prevent a reoccurrence

Treasury has repeatedly requested as part of its quarterly refundings that the private sector address the fails-to-deliver :

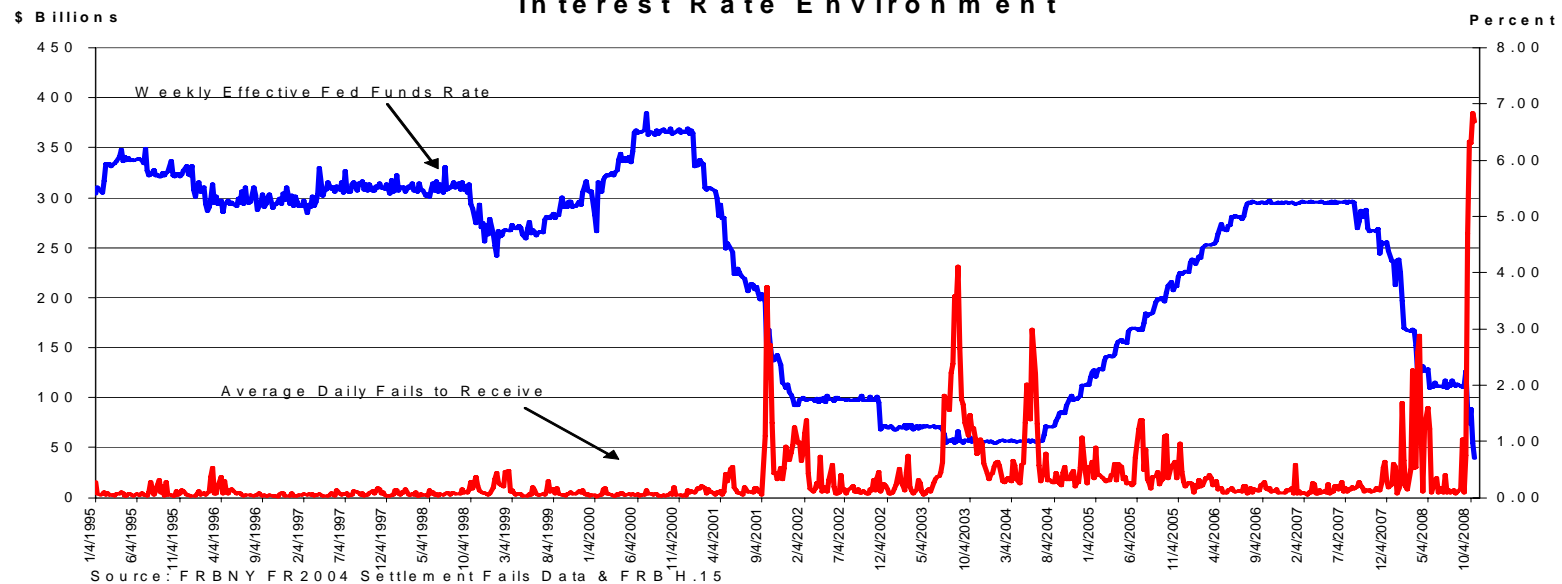
- Feb 2008
- May 2008
- Aug 2008
- Nov 2006
- Aug 2006
- May 2006
- Feb 2006
- Nov 2005
- Aug 2005
- Nov 2003

The private sector has repeatedly stated that they would implement their own solutions rather than involving governmental intervention.

Recommendations:

- Amend master repo agreements
- Establish a standard cash trading agreement
- Margining of aged settlement fails
- Negative rate trading
- Bilateral cash settlement of aged fails
- Multi-lateral netting facility

**Primary Dealer Treasury Security Settlement Fails
Interest Rate Environment**



Unscheduled Reopenings

On October 8, Treasury announced that it was reopening \$10 billion in each of the following original issue 10-year note securities:

- 3.5% of February 15, 2018
- 4.25% of August 15, 2015
- 4.125% of May 15 2015
- 4.0% of February 15, 2015

The actions were undertaken to:

- Address upcoming borrowing needs
- Provide additional liquidity given the extraordinary dislocations in the Treasury market

Since then:

- Fails have declined by more than half of their mid-October peak
- Treasury 2-year and 5-year auctions performed well

Market participants should not anticipate regular unscheduled reopenings because they:

- Are contrary to Treasury's policy of transparency, regularity, and predictability
- Permanently increase outstanding supply for what may be a temporary shortage
- Increase supply uncertainty and raise borrowing costs
- Act as a disincentive to private sector solutions



Given the benefits of a liquid Treasury market and broad investor participation, what steps should be pursued to ensure continued efficient market functioning?

Are there any other approaches to auctions, cash and debt management tools, and/or instruments that Treasury should consider?



Treasury Borrowing Advisory Committee Presentation to the U.S. Treasury

Credit Market Conditions

November 4, 2008

Treasury Borrowing Advisory Committee

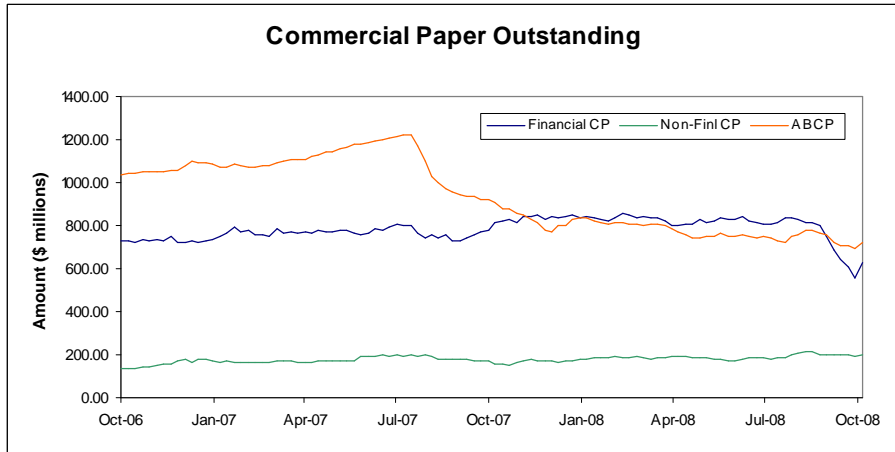
Credit Market Conditions

November 4, 2008

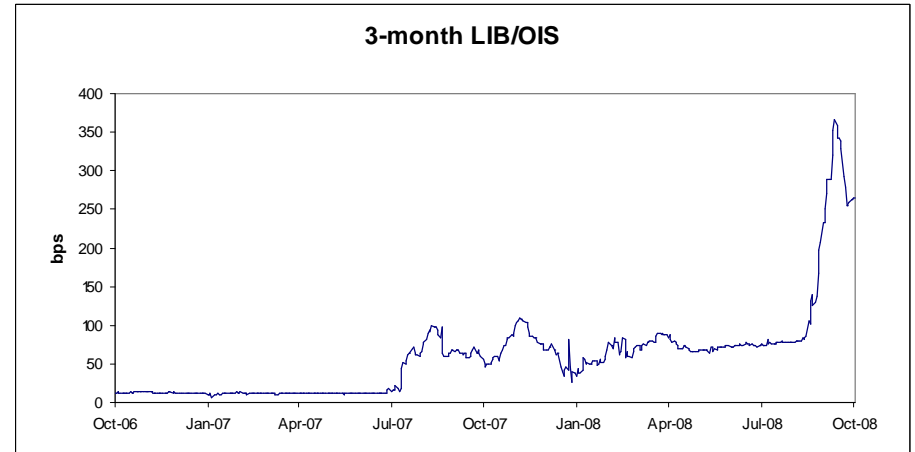
Executive Summary

- Healing phase started globally
 - Swap spreads 
 - CP tenure 
 - Monetary base 
- Risk aversion in all markets
 - Credit spreads 
 - Defaults 
 - VIX 
- Headwinds
 - Treasury fails
 - Credit deterioration in consumer
 - Lending attitudes
 - Investors asset allocations

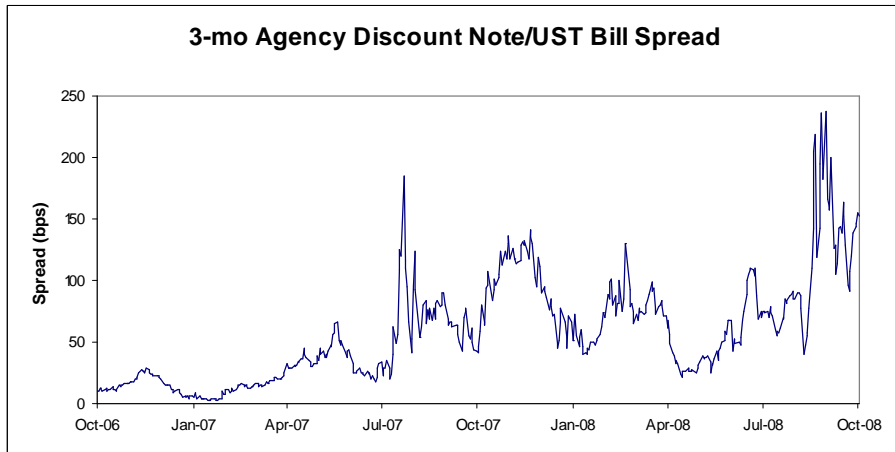
Credit Trends



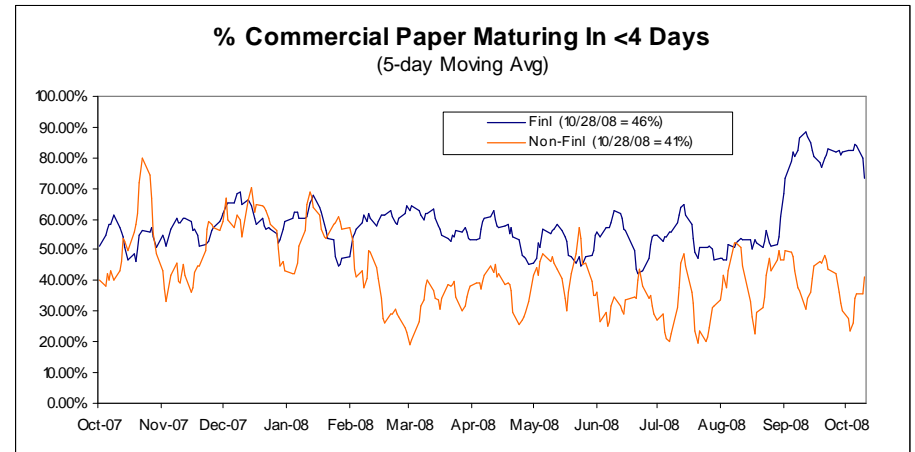
Source: Bloomberg



Source: Bloomberg



Source: Bloomberg



Source: Federal Reserve Bank

Swap Spreads

U.S. 2 yr



Euro 2 yr



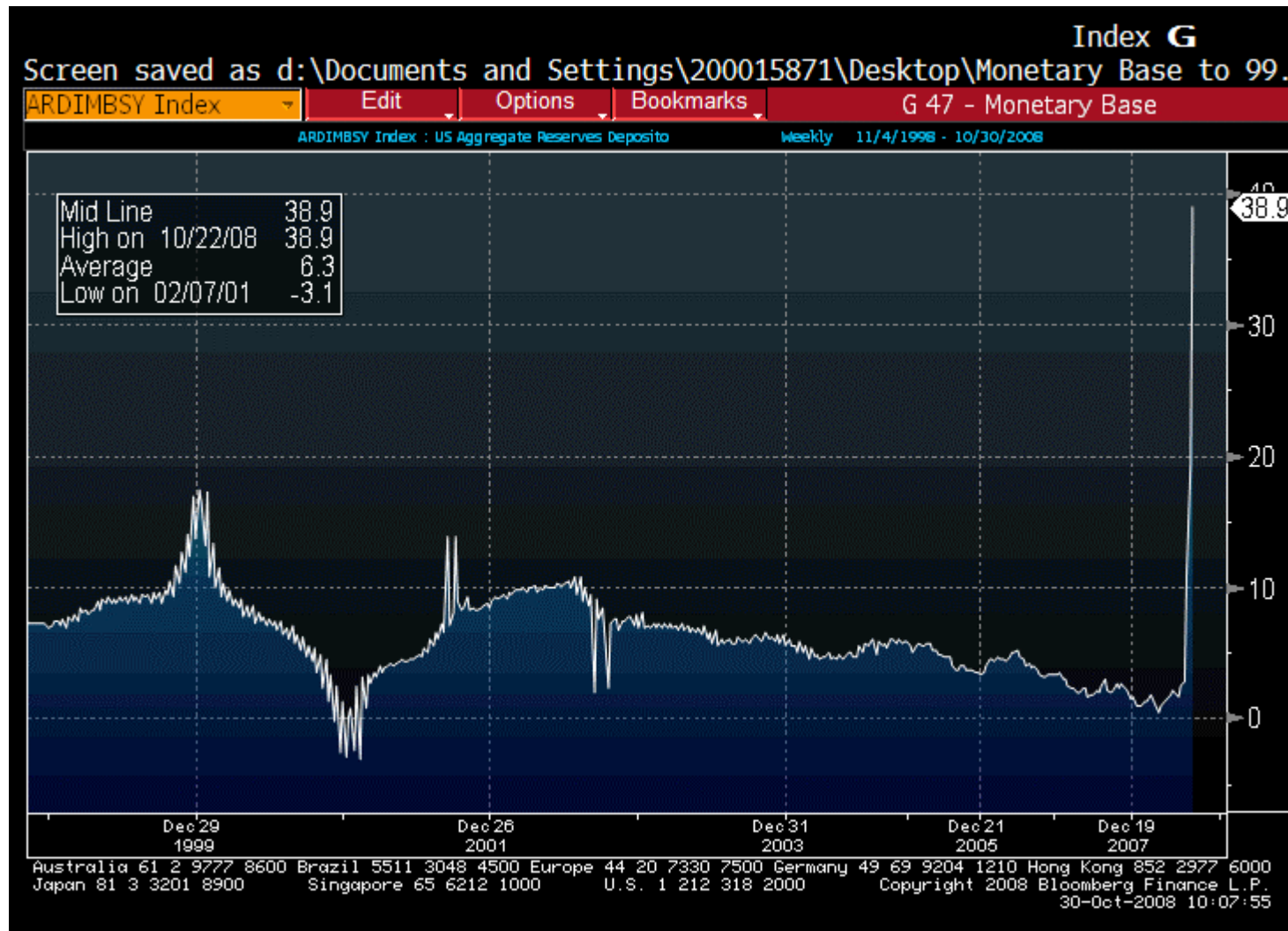
Sterling 2 yr



Yen 2 yr



The Monetary Base

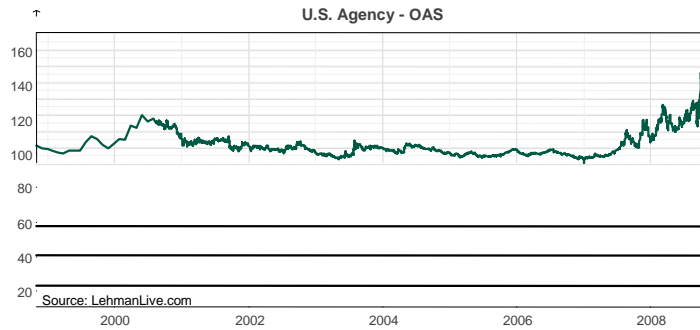


Source: Bloomberg

The Fed Has Expanded The Monetary Base By Nearly 39%.

U.S. Spreads

Agencies



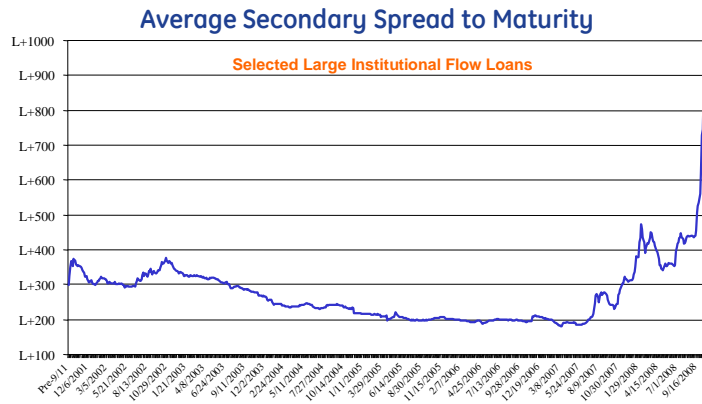
Key	Axis Name	Last	Minimum	Maximum	Mean	SD	SD Change
Left	U.S. Agency - OAS	157.914	18.095	163.962	40.106	17.288	2.015

Corporates



Key	Axis Name	Last	Minimum	Maximum	Mean	SD	SD Change
Left	U.S. Corporate Investment Grade - OAS	304.52	75.757	570.728	146.322	270.601	2.880

Loans



Source: Standard and Poor's

High Yield



Key	Axis Name	Last	Minimum	Maximum	Mean	SD	SD Change
Left	U.S. Corporate High Yield - OAS	9479.068	232.645	1516.719	1027.203	838.912	25.145

Credit Spreads Generally Wider

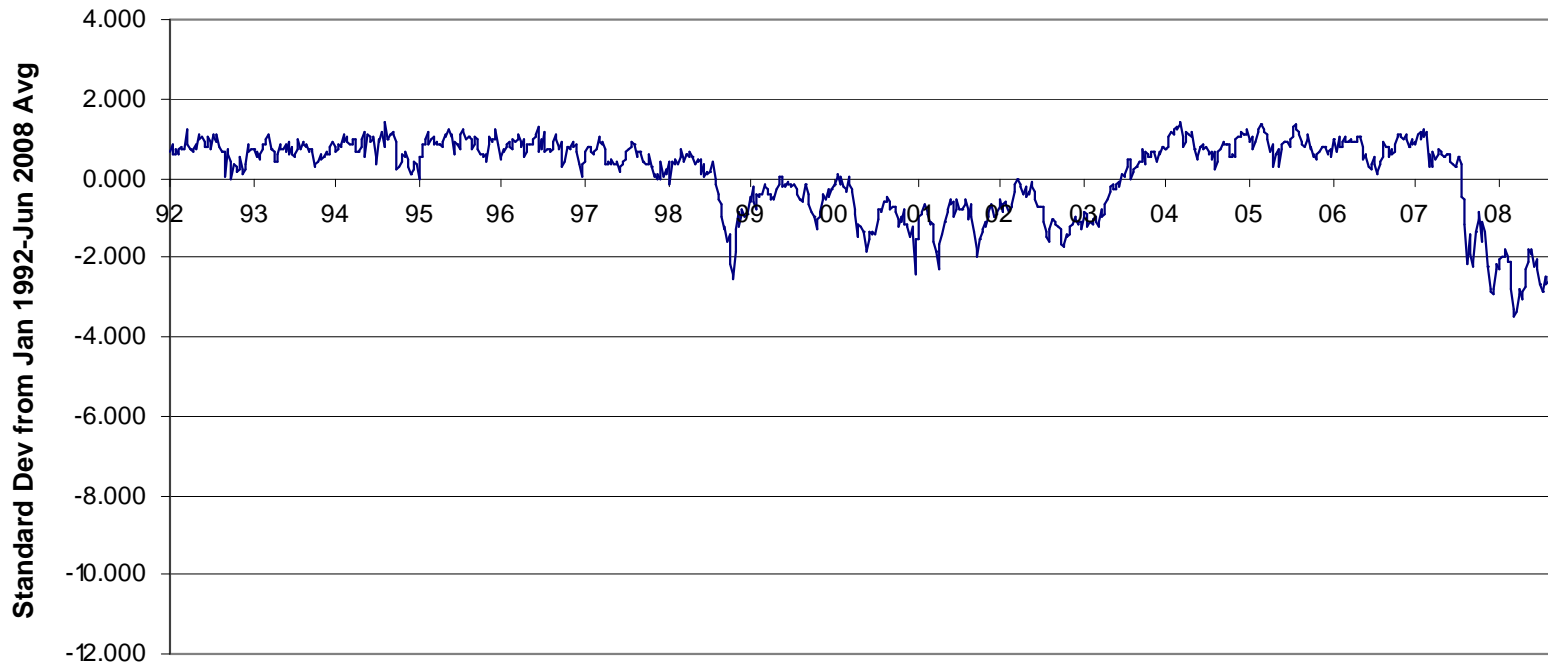
The VIX



Source: Bloomberg

Stock Market Volatility Hitting Thirteen Year Highs

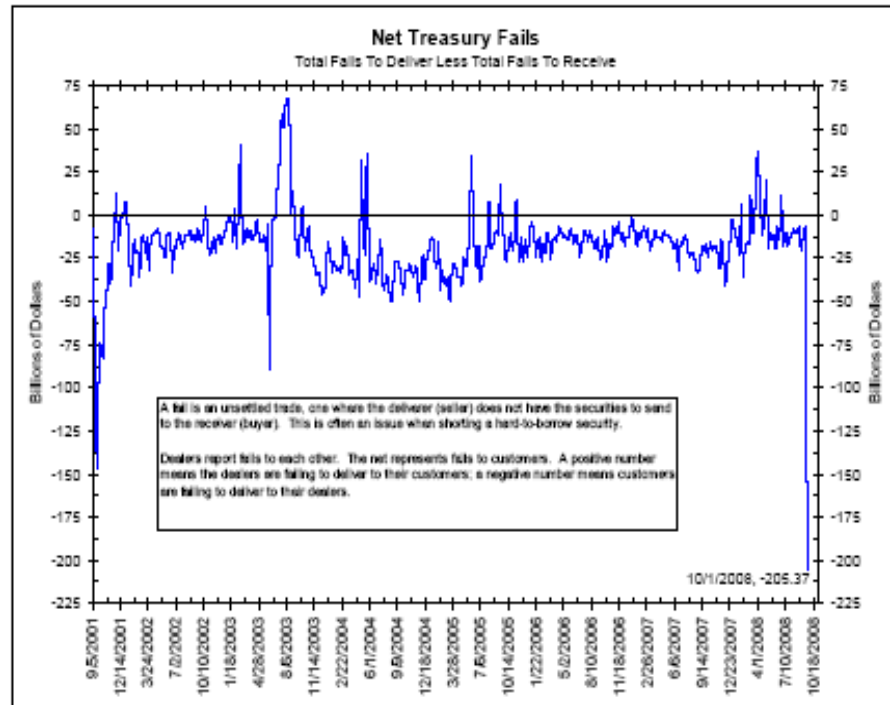
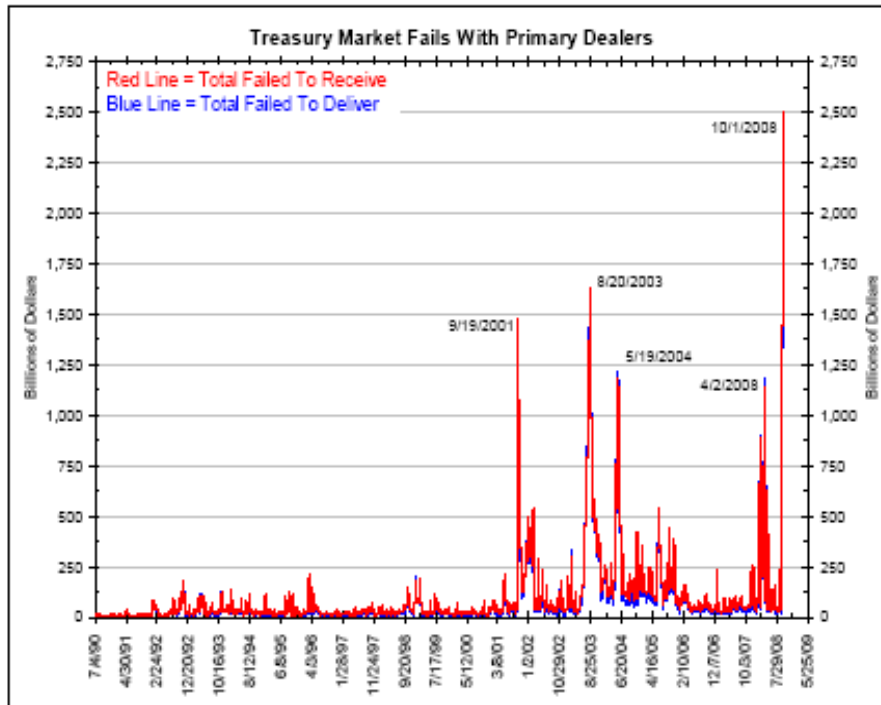
Bloomberg Financial Conditions Index



Bloomberg's U.S. Financial Conditions Index Components and Weights

<u>Money Market</u>	<u>Index Weight</u>	<u>Bond Market</u>	<u>Index Weight</u>	<u>Equity Market</u>	<u>Index Weight</u>
TED Spread	11.1%	Investment-Grade Corp/Tsy Spread	6.7%	S&P 500 Share Prices	16.7%
Commercial Paper/T-Bill Spread	11.1%	Muni/Treasury Spread	6.7%	VIX Index	16.7%
LIBOR-OIS Spread	11.1%	Swaps/Treasury Spread	6.7%		33.3%
	33.3%	High Yield/Treasury Spread	6.7%		
		Agency/Treasury Spread	6.7%		
			33.3%		
				Total	100.0%

Treasury System Fails



Source: Bianco Research, L.L.C

But Banks are Hoarding Cash



Sources: The Federal Reserve Board , The Bloomberg, and Merrill Lynch

Bank Cash Holdings at are above the levels of Sept 2001