US Treasury Issuance Resurgence

BOND AUCTION SIZE INCREASES BEGIN

As expected, following the US tax reform, sharply wider federal deficits are forecast for fiscal 2018 (FY18) through FY20 by primary dealers in the latest US Treasury *Quarterly Refunding Survey* (here). Relative to the 2017 Q4 survey, the median deficit in 2018 Q1 is $73 billion[1] wider for FY18 and more than $170 billion wider for FY19 and FY20, pushing up net marketable borrowing forecasts by somewhat larger amounts (charts 1 and 2). For the federal deficit forecasts, multiple sources of forecast uncertainty persist, including unresolved spending plans and the timing of tax remittances, but the overall direction appears clear.

Treasury discussions of rising borrowing requirements in recent months have indicated increased issuance across the curve, favouring bills plus 2-, 3-, and 5-year notes and keeping the Weighted Average Maturity (WAM) close to the present level of roughly 70 months. Expanding the funding gap is the redemption of SOMA Treasury holdings, starting in FY18 at an estimated $175 billion, according to the schedule currently laid out by the Federal Reserve.

Treasury anticipates the following auction size increases from February to April, raising an additional $42 billion:

- For 2- and 3-year notes, increases of $2 billion per month;
- For 5- and 7-year notes, a $1 billion rise in February sustained over the following two months; and
- For 2-year FRNs, a $2 billion increase, and for 10-year notes and 30-year bonds a $1 billion rise, applying to new issues and reopenings.

Borrowing over the past year has been complicated by the absence of a longer-term debt ceiling increase, resulting in a cycle of depleting and restoring cash balances. Treasury now expects current extraordinary measures to fund the government to the end of February, about a month earlier than the Congressional Budget Office projection last November that these measures could carry Washington to late March or early April.

Further expansion of note and bond auction sizes is anticipated. While Treasury will continue to rely upon significant Treasury bill financing, allocating more than one-third of net marketable borrowing to bills would lower WAM.

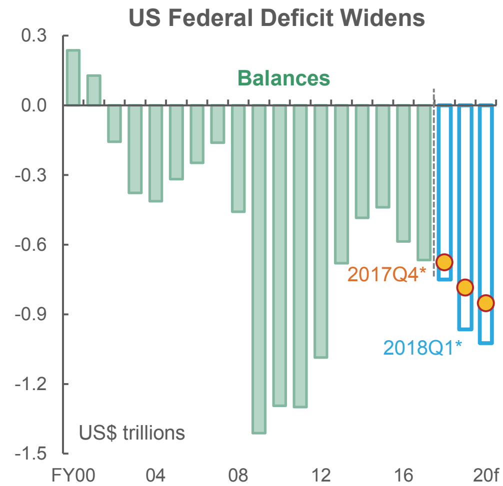
Introducing a two-month bill will likely be discussed at the April refunding. The primary dealer response to this proposed tenor indicated significant potential demand with minimal damage to other short-term instruments and it would limit the extent of surges in weekly auction sizes for 4-week and 3-month bills.

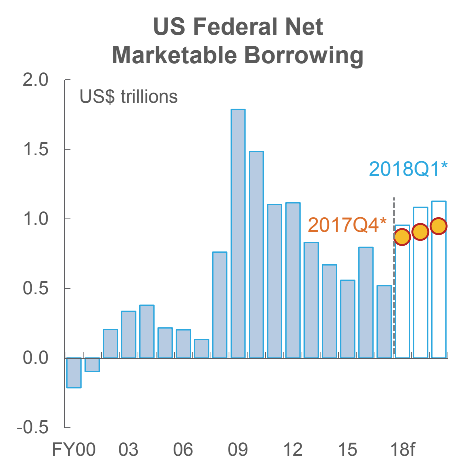
TIPS[2] auction sizes were not announced for February but are expected to be considered in the future. Supporting an increase in TIPS as nominal bonds outstanding climb are the expanding holdings of TIPS by non-resident investors and in domestic vehicles such as target-date funds.

[1] Fiscal 2018 ends September 30, 2018. All dollar data in US dollars.
[2] Treasury Inflation Protected Securities.

CONTACTS

Mary Webb
416.866.4202
Scotiabank Economics
mary.webb@scotiabank.com





* Median of primary dealer surveys. Sources for charts: US Treasury, Office of Management and Budget.