

US Rates Watch

BTFP final days: cash tracking

BTFP to close to new loans next week

The BTFP is set to close to new loans next week with banks still able to request advances under the program until Monday March 11th. We expect to have the final level of BTFP take-up in next week's Fed balance sheet data with the potential for several borrowers to re-extend their loans to 1 year. We have observed a slight tick-up in the maturity distribution of Fed loans in the 91 to 1y bucket, implying some modest BTFP extension has already begun (Exhibit 1).

BTFP background: emergency liquidity tool

The BTFP was created as an emergency funding measure after the bank stress in March '23. The facility provided loans up to 1y for open market eligible paper (USTs, agency MBS, agency debt) at par and funded at 1Y OIS +10bps. The Fed later adjusted the rate to the greater of 1Y OIS + 10bps or IORB to discourage arbitrage. The facility is an emergency measure under the Fed's 13-3 clause, which requires UST Secretary approval.

BTFP loan expiration & cash tracking

The BTFP provided roughly \$165b in liquidity, offsetting some of the drain from QT. Depending on whether banks replace the funding or not will have implications on reserve and ON RRP drain, and therefore could impact our expectations for the end of QT.

Borrowers who have gone to the BTFP will either need to (1) re-extend their loan ahead of the expiration, (2) find another source of funding to replace the BTFP or (3) allow the loan to rolloff without borrowing elsewhere. The first two options are unlikely to result in any near-term change in reserve balances. We may see ON RRP deplete if banks bid up for other sources of funding. Conversely, if most banks do not need to replace this funding source, it will likely be a drain on reserve balances. Recent growth in reserve balances suggest banks are resisting any decline in their cash levels (Exhibit 2).

BTFP expiry could drive higher FHLB advances

We expect that most of the BTFP borrowers who need the cash will simply rollover their loans ahead of the expiry. However, banks may also consider replacing their lost funding with the Federal Home Loan Bank (FHLB) system. FHLB debt issuance has increased \$12b over Jan and Feb, implying that demand for advances has increased YTD after several months of paydowns in the 2H of '23. The limited growth in FHLB debt outstanding implies that there has been limited pre-funding for BTFP expiration.

Bottom line: watching BTFP loan extension & FHLB issuance will be key to determine how comfortable banks are with their liquidity positions. The recent increase in Fed loan maturity & ongoing increase in bank reserves suggest banks are still demanding elevated liquidity buffers. FHLB issuance may grow with BTFP loan expirations.

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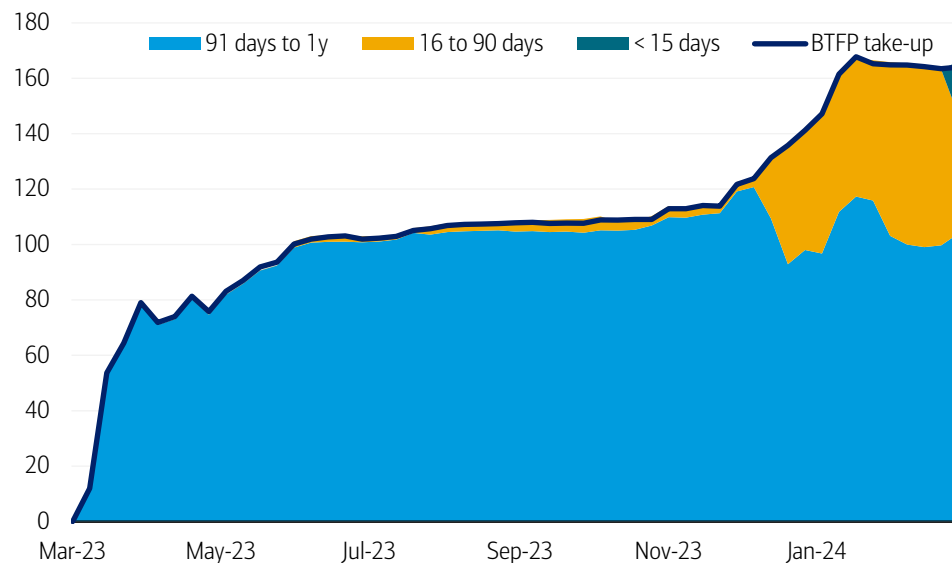
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Exhibit 1: Fed Bank Term Funding Program (BTFP) use with Fed loan maturity breakdown (\$bn)

Recent data implies some banks have already re-extended loans up to 1 year



Source: Bloomberg, BofA Global Research

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Exhibit 2: Fed reserve balances (\$bn)

Reserve balances remain elevated and continue to rise



Source: Federal Reserve

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Exhibit 3: Cumulative FHLB debt issuance since March 1 2023 (\$bn)

FHLB issuance was ramping up to start the year but has come down quickly in March



Source: BofA Global Research, Bloomberg, FHLB OF

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