

US Rates Watch

Fed balance sheet: tax date tweaks

Updated Fed balance sheet forecast

We update our Fed balance forecasts by tweaking our assumptions on (1) tax date liquidity drain (2) BTFP repayment. These tweaks push out the timing of when ON RRP will reach the \$200-250b threshold we believe the Fed considers “low”. We are not changing our QT slowdown timing call due to elevated uncertainty around these factors but acknowledge higher ON RRP could mean a later QT adjustment.

Fed balance sheet drain largely out of ON RRP

The Fed’s balance sheet has declined at a pace of roughly \$70-75b per month on average since QT reached peak redemption cap levels in Sept 2022 (Exhibit 1). Since the start of QT, the Fed’s balance sheet has declined nearly \$1.28tn, but \$1.47tn has come out of ON RRP (reserve balances have grown \$293b) (Exhibit 2). We expect this trend of QT draining 100% from ON RRP & 0% from reserves to continue. We also assume other non-reserve Fed liability growth will come out of ON RRP. We are less certain how BTFP repayment & the April tax date will impact reserves & ON RRP.

BTFP set to expire in March, drain ON RRP & reserves

Fed BTFP loans originated in March ’23 may soon be repaid. These loans could be extended before maturity, but this seems less likely given the recent increase in BTFP borrowing cost (base rate shifted from 1Y OIS to IORB). If the loans are not rolled over Fed H.4.1 suggests ~\$60b may be repaid by early April. Recall, Fed H.4.1 data provides the maturity structure of Fed loans & \$63b will mature in 16 to 90 days (Exhibit 3); most Fed loans are BTFP-related and an initial \$79b was borrowed from early Mar to early April. When BTFP loans mature we assign a 50/50 liquidity drain from reserves & ON RRP but have low confidence in this estimate. Risks are for a larger reserve drain.

April tax date will drain reserves and grow TGA

The April tax date is another uncertainty in our Fed balance sheet projection. The April tax date often coincides with a large increase in the TGA, lower bill supply, and lower reserve balances. Looking at post COVID tax-dates, we found that over 100% of the TGA increase over the month of April typically comes out of reserve balances. In our forecast, we assume 100% of the growth in TGA in April will come out of reserves while QT and growth in other liabilities will continue to drain out of ON RRP.

Debt limit could temporarily reverse effects of QT

A final wild card in our Fed balance sheet projection is debt limit, which will be relevant again in late ’24. The debt limit suspension period ends on Jan 1 ’25 & which we believe will require TGA to drop from \$750b to \$550b by end ’24 (\$550b = ~5D of TGA outflows). Lower TGA means less bill supply & easier funding. We assume the TGA drop will be 100% offset by higher ON RRP use, though reserves could also increase. ... see page 2 for more detail on risks to QT slowing if ON RRP higher than originally projected...

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Glossary

BTFP: Bank Term Funding Program**ON RRP:** Overnight reverse repurchase agreement facility**QT:** Quantitative tightening**TGA:** Treasury General Account

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QT winddown trigger to be “low” ON RRP take-up

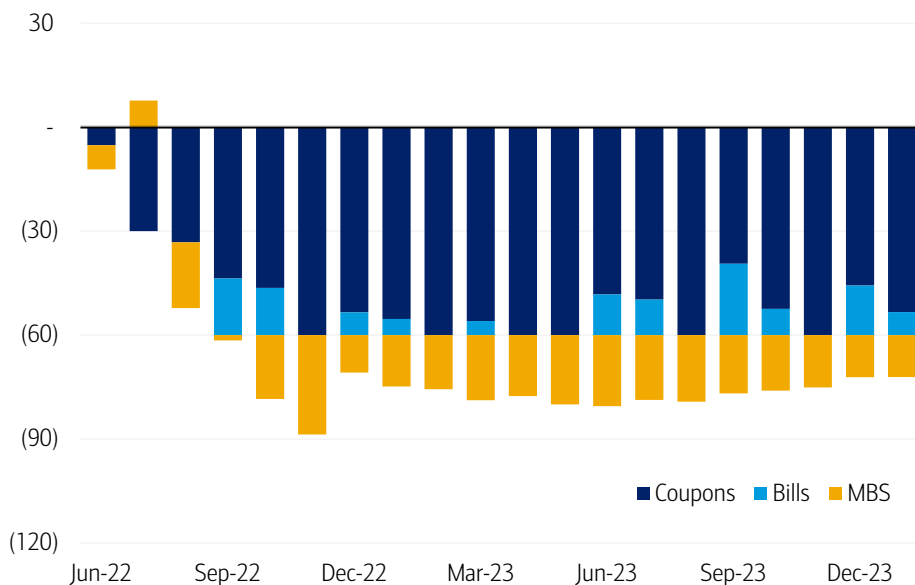
We have received limited guidance from the Fed on when and how they will slow QT. We agree with Dallas Fed President Logan that it will be prudent for the Fed to begin slowing QT once ON RRP, which we view as excess liquidity, is low. With these factors in mind, we estimate “low” ON RRP take-up to be roughly between \$200 and \$250b. Our base case previously saw ON RRP reaching these levels in April and thus expected QT slowdown to begin in May.

Our updated Fed balance sheet forecasts now see the \$200-250b ON RRP threshold first being breached in Q3 '24. The key driver of the slower ON RRP decline vs our prior forecast is the April tax date & TGA build coming from reserves (not ON RRP). We are not changing our QT slowdown timing call but see risks of a later QT moderation if ON RRP balances stay high. Tax date TGA growth & BTFP repayment drain + FOMC minutes guidance on QT preferences will be key to our QT slowdown timing.

Bottom line: we adjust our Fed balance sheet forecasts accounting for the April tax date liquidity drain, BTFP repayment, & end '24 debt limit dynamics. These factors could see ON RRP remain higher than the \$200-250b threshold we believe is important to the Fed. A slower pace of ON RRP depletion would mean a later timing of QT slowdown vs our base case in May.

Exhibit 1: Monthly reduction in Fed balance sheet assets

Fed QT has averaged a pace of roughly \$72b per month since reaching peak redemption caps



Source: BofA Global Research, Bloomberg

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Exhibit 2: Change in Fed balance sheet since the start of QT (\$bn)

Most of the drain the Fed's liabilities since the start of QT has been out of ON RRP

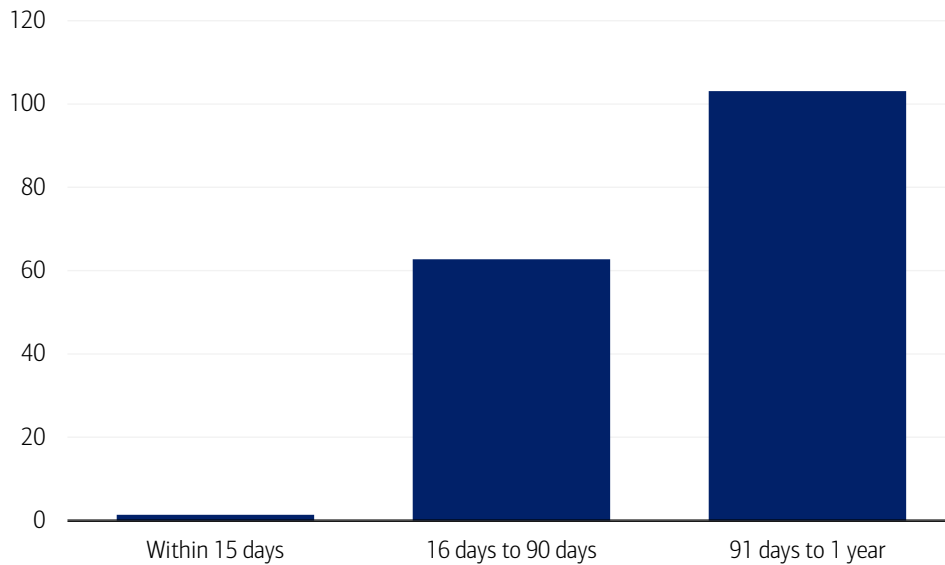
	Total	Assets			Reserves	Liabilities			
		USTs	Agy MBS	Other		UST Cash Balance	ON RRP	Currency	Other
5/25/2022	8964	5769	2707	487	3306	822	1996	2276	564
2/7/2024	7682	4693	2417	572	3599	802	526	2327	427
QT start	-1281	-1077	-290	86	293	-19	-1470	51	-136

Source: BofA Global Research, Bloomberg

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Exhibit 3: Fed loan maturity profile (\$bn)

We use the Fed's loan maturity profile to estimate when BTFP take-up will be wound down



Source: Federal Reserve H.4.1.

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Exhibit 4: Change in TGA, ON RRP and reserves around April Tax Date (\$bn)

Reserves offset most of the growth in TGA in April in all periods around the April tax dates

		ON RRP	Reserves	TGA	RRP % of TGA	Reserves % of TGA
April Change	3/30/22-5/4/22	30	-459	408	-7%	113%
	3/29/23-5/3/23	-7	-236	26	26%	922%
T-7 to T+7	4/13/22-4/27/22	-12	-466	414	3%	113%
	4/12/23-4/26/23	-24	-215	210	12%	103%
T-14 to T+14	4/6/22-5/4/22	84	-536	419	-20%	128%
	4/5/23-5/3/23	15	-215	48	-32%	452%

Source: BofA Global Research, Federal Reserve. Note: In both 2022 and 2023, the tax date in April was on the 18th

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Exhibit 5: Fed balance sheet forecast (\$bn)

We forecast QT to slowdown in May and end in December

	Asset							Liabilities						
	UST	MBS	CMBS	Repo	DW	BTFP	Other	Currency	TGA	Foreign RRP	ON RRP	Other	Reserves	Total
Jan-24	4716	2417	8	0	3	167	376	2327	842	346	578	87	3526	7706
Feb-24	4656	2401	8	0	3	165	377	2340	800	347	510	88	3525	7611
Mar-24	4596	2384	8	0	3	124	378	2352	775	348	423	89	3505	7493
Apr-24	4536	2364	8	0	3	116	379	2365	975	350	326	90	3301	7407
May-24	4506	2346	8	0	3	116	380	2378	800	351	439	91	3301	7359
Jun-24	4476	2326	8	0	3	106	381	2391	750	352	420	92	3296	7301
Jul-24	4446	2306	8	0	3	104	382	2404	750	353	355	93	3295	7249
Aug-24	4416	2290	8	0	3	102	383	2417	750	354	293	94	3294	7202
Sep-24	4386	2273	8	0	3	102	384	2430	750	356	232	95	3294	7156
Oct-24	4356	2259	8	0	3	100	385	2443	700	357	223	96	3293	7111
Nov-24	4326	2244	8	0	3	96	386	2456	650	358	211	97	3291	7063
Dec-24	4296	2232	8	0	3	51	387	2470	550	359	232	98	3268	6977

Source: BofA Global Research, Federal Reserve

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