2 June 2021
Investment Solutions & Products
Global

CREDIT SUISSE

Credit Suisse Economics

Global Money Dispatch

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Are you concerned about the Hoover Dam cracking?

Then neither should you be concerned about repo and bill yields going negative under "pressure" from the wall of money that's building in the o/n RRP facility. The RRP facility is doing what it was designed to do – absorbing excess cash – and the money funds that we talk to aren't about to gate inflows to their funds. Why would they? If one fund were to gate inflows, another would grow instead, and there are no marginal costs involved in taking an extra $1 trillion of cash even if the marginal asset that they invest in – o/n RRPs at the Fed – pays zero. If money funds gating inflows is not a risk, neither is the Hoover Dam cracking.

Should the Fed adjust the rate on the o/n RRP facility to a positive number?

Ask money funds and they'll say yes. Their argument is that the Fed is able to defend the zero lower bound with the RRP facility *only* because money funds are willing to intermediate between cash lenders and the Fed. In other words, because money funds aren't gating inflows (see above). Services ain't for free, so why should money funds' "policing services" at the zero bound be for free? FRBNY should pay for "services rendered" and pay at least a few bps on the o/n RRP facility. Yes, but the Fed isn't in the business of paying money funds, unless their policy stance requires so. The Fed sets the target range for o/n interest rates and has facilities to enforce that range. If the o/n RRP facility serves as well as the Hoover Dam, there is no policy reason for a higher RRP rate.

Should the Fed just sell its short-dated Treasuries to money funds?

It should. The Fed holds $1 trillion in Treasuries that mature within one year, $325 billion of which are bills. These holdings provide interest income to the Fed, but the RRP facility pays zero to money funds. The Fed is "eating" all the carry. Those asking for a higher rate paid by the o/n RRP facility effectively are asking for a few bps of carry from the Fed's short-dated Treasury portfolio. The Fed should sell a portion of that portfolio and shrink its balance sheet – they wouldn't be selling duration or draining reserves, as reserves have been drained already – but it's not about what *should* happen, but what *will* happen, and unfortunately, the Fed never mentioned bill sales as an option, which means it won't happen.

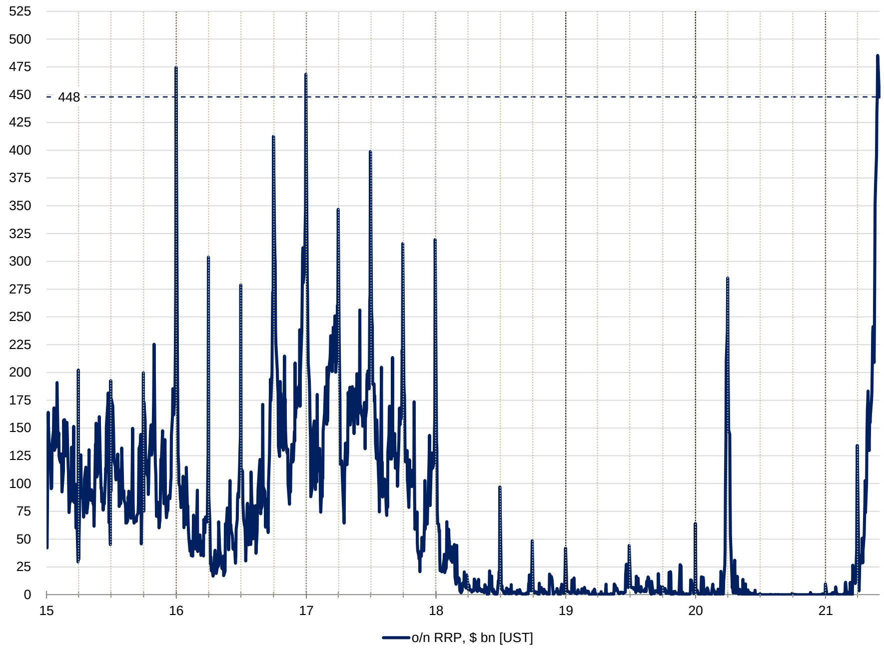
Is there "undue" pressure on the fed funds rate?

There is none whatsoever. What changed since the April meeting? Nothing: repo and bills trade at zero, supported by the o/n RRP facility; o/n fed funds went from trading at 7 bps to 6 bps, but with so much excess liquidity around, that's not an "undue" move lower; the bottom percentiles of fed funds flows haven't done anything they haven't done before; fed funds volumes are robust.

Why should the Fed then adjust the IOR or o/n RRP rates at the June meeting?

[Daily]: Use of the Fed's o/n RRP Facility

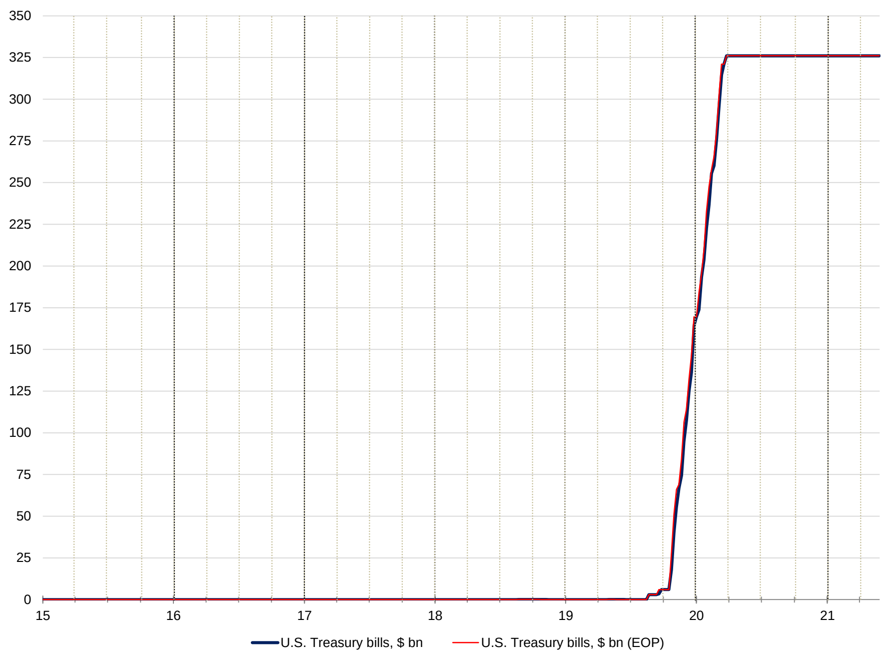
$ billion



Source: FRBNY, Credit Suisse

[Weekly]: The Fed's Holdings of U.S. Treasury Bills

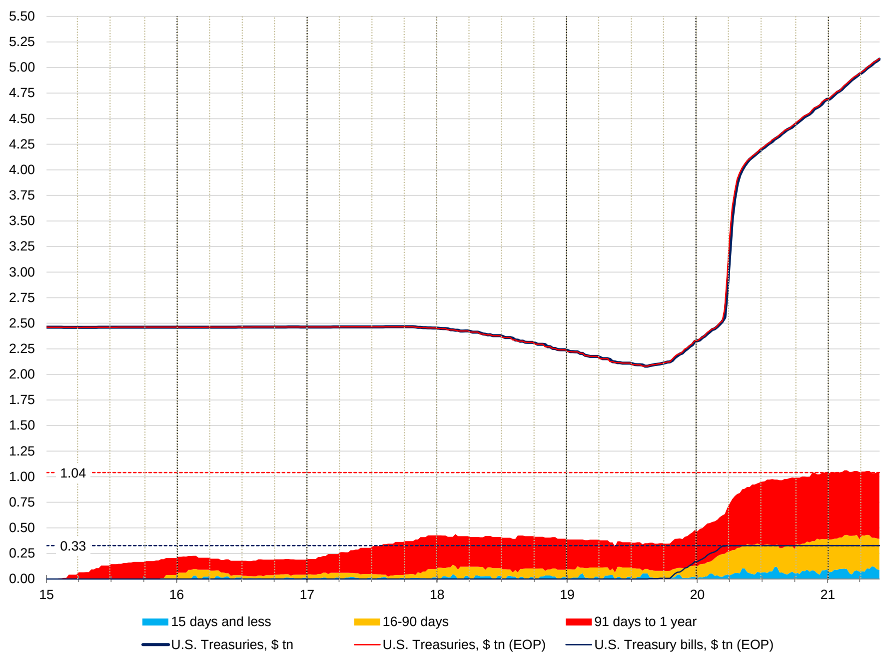
$ billion



Source: Federal Reserve, Credit Suisse

[Weekly]: The Fed's Holdings of U.S. Treasury Securities (1)

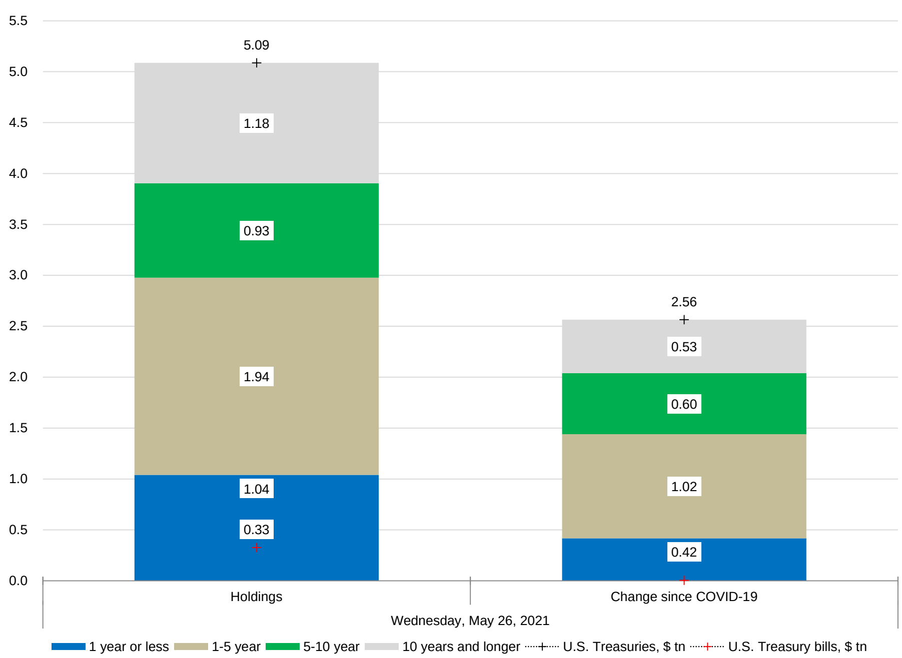
$ trillion



Source: Federal Reserve, Credit Suisse

[Weekly]: The Fed's Holdings of U.S. Treasury Securities (2)

$ trillion



Source: Federal Reserve, Credit Suisse

[Daily]: U.S. Treasury Bill Yields Are Well Anchored at Zero

percent

Source: the BLOOMBERG PROFESSIONAL™ service, Credit Suisse

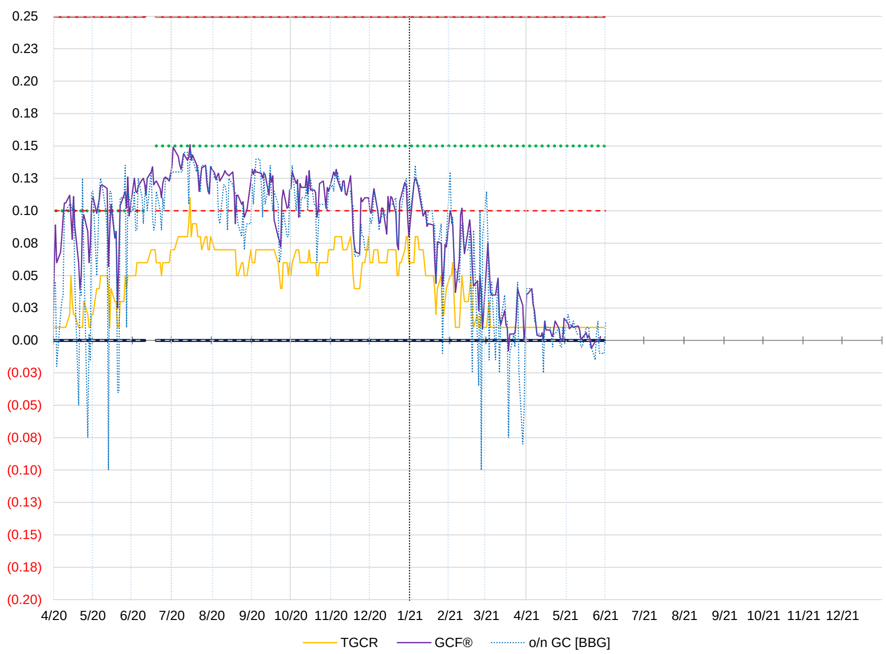
[Daily]: o/n Tri-Party Repo Rates Follow Bill Yields Hand-in-Hand

percent

Source: the BLOOMBERG PROFESSIONAL™ service, Credit Suisse

[Daily]: o/n GCF® Repo Rates Follow Tri-Party Repo Rates

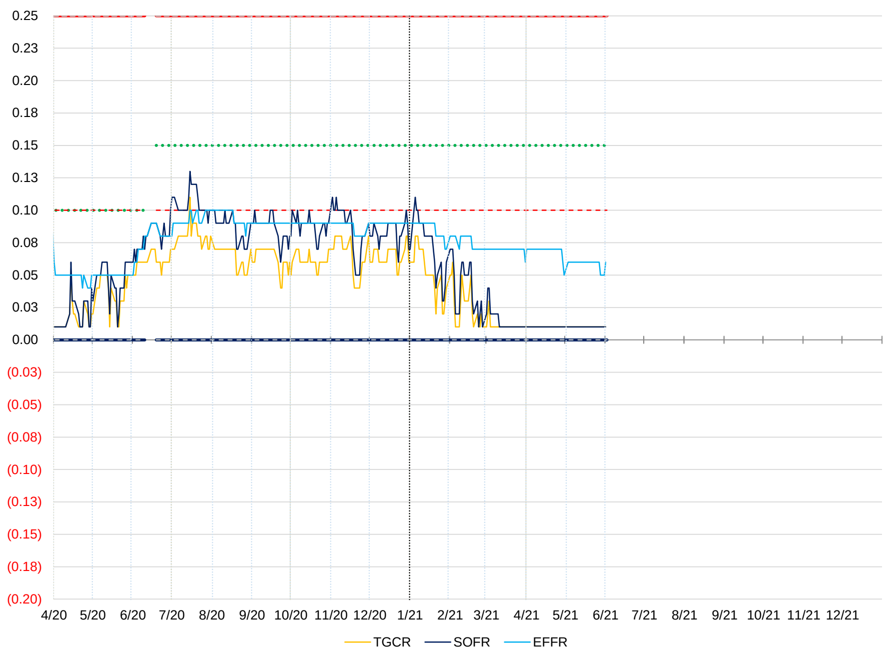
percent



Source: the BLOOMBERG PROFESSIONAL™ service, Credit Suisse

[Daily]: o/n EFFR Is Not Subject to "Undue" Pressure

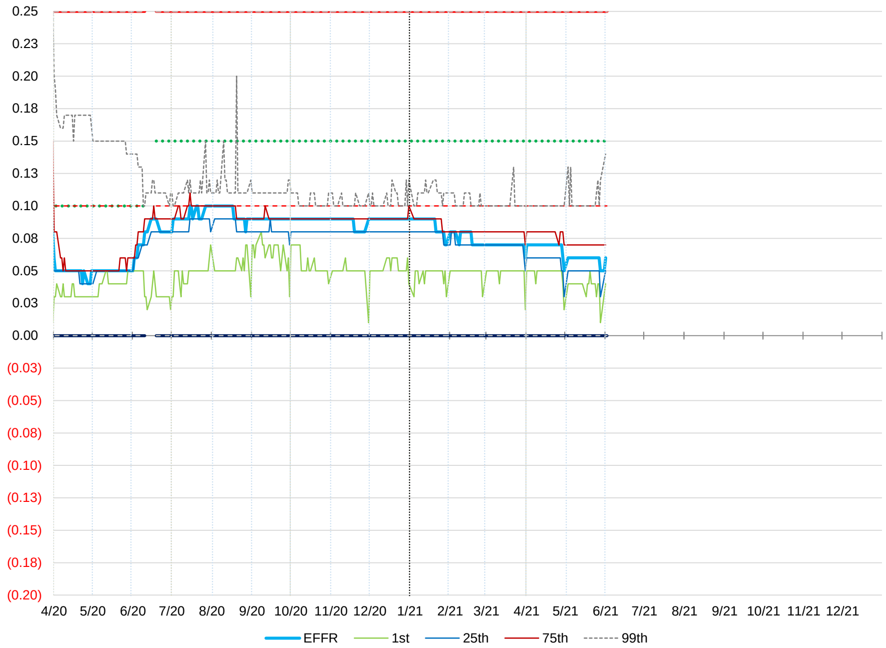
percent



Source: the BLOOMBERG PROFESSIONAL™ service, Credit Suisse

[Daily]: o/n EFFR Won't Trade Lower than 4 Basis Points

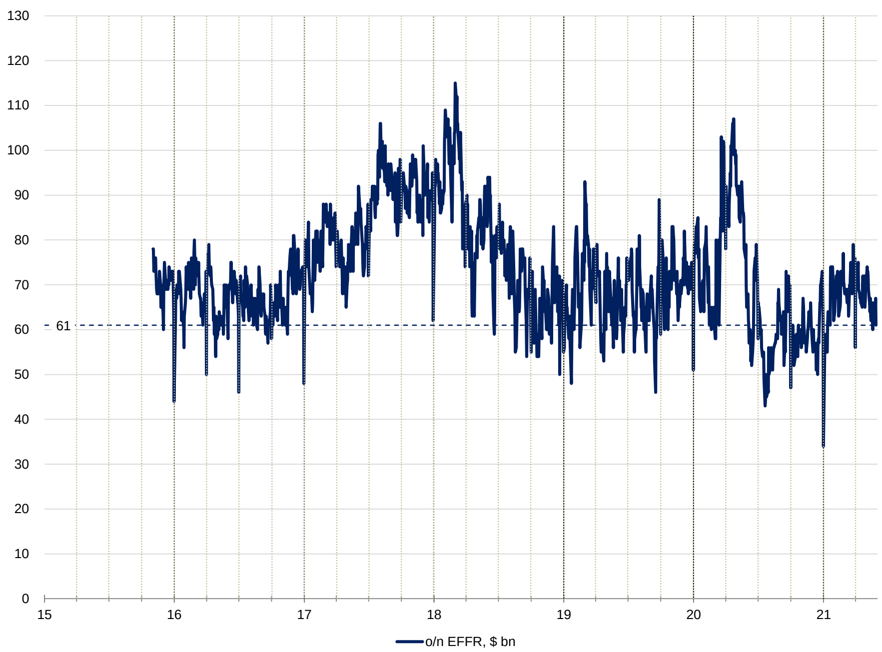
percent



Source: the BLOOMBERG PROFESSIONAL™ service, Credit Suisse

[Daily]: o/n Fed Funds Volumes Remain Robust

$ billion



Source: FRBNY, Credit Suisse

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