Notable items since May 2007

- OMB released its Mid-Session Review in mid-July:
  - Revised down its FY 2007 budget deficit forecast from $244 billion to $205 billion
  - Marginally revised up its FY 2008 budget deficit forecast to $258 billion
  - Continues to forecast a budget surplus in 2012

- SLGS issuance has slowed from very high levels

- Discontinued issuance of the 3-year note

- Experienced another strong April tax season
Year to date tax receipts continue to grow

FY07 Revenue YTD on pace to surpass last year's total fiscal year revenues
YTD outlay growth continues at slower pace than in recent years

Total Outlays
Fiscal Year to Date

FY07 Outlays YTD smallest year-over-year growth rate in recent years
OMB expects improvement to budget deficits after FY 2008

Projected Budget Results
(+ Deficit/- Surplus)

$ billions

-50 0 50 100 150 200 250 300

2006 2007 2008 2009 2010 2011 2012

Office of Debt Management
Net SLGS Issuance in FY 2007 has been very high, but slowed recently
Marketable Debt Net Issuance Historically Low

*2007 Net marketable Borrowing includes $73 billion estimated for Q4. 2007 Budget Deficit from OMB’s Mid Session Review.
Leading to Decline in Bills Outstanding
And Reduced Coupon Issuance

Net Coupon Issuance

Net financing projections for FY 2007 are based on internal FY 2007 deficit estimate. Future residual financing needs are spread proportionally across auctioned securities, based on coupon auction sizes in the prior quarter and September 30, 2006 bills outstanding.
Future Financing and Portfolio Considerations

- Market participants suggest that current auction sizes of benchmark coupon securities are at or near minimum sizes to ensure liquidity.

- The deficit has been cut in half ahead of schedule, and the OMB forecasts a balanced budget by 2012.

- From February to July, the deficit forecast has dropped by almost $40 billion.

- We aim to preserve flexibility to address a range of fiscal outcomes.
In light of intermediate and longer-term fiscal trends as well as recent economic and market conditions, what advice would the Committee give in terms of Treasury’s debt issuance?
The Costs of Inaction Regarding Entitlement Reform: Potential Implications for Treasury Debt Issuance, Interest Costs, and Overall Market Dynamics

Treasury Borrowing Advisory Committee Presentation to the US Treasury
July 31, 2007
Executive Summary

• A long run Treasury financing model has been used to attempt to quantify the potential implications of rising entitlement spending.

• The output is based on three alternative baseline budget scenarios originally developed by the Congressional Budget Office.

• The findings imply a very large future financing need under each of CBO’s scenarios.
  • For example, even under the most optimistic budget outlook, 2-year note issuance will be nearly $380 billion per month by 2050.
  • In the most pessimistic scenario, 2-year note issuance reaches $1.9 trillion per month.

• In relation to the size of the economy, it is estimated that gross coupon issuance will need to be between four and fifteen times as large as at present by 2050.

• The sharp elevation in the financing needs starts to become apparent as early as 2020.
Long Run Treasury Financing Model Assumptions

1) Budget deficit forecast of $170 billion in FY 2007.

2) CBO long range alternative budget scenarios A, B and C for FY 2012 to FY 2050 (an interpolation was used for the FY 2008-2011 period). A description of these scenarios appears on the next page.

3) Hold Treasury bills at 25% of debt outstanding.

4) Increase coupon sizes in proportion to their current share of gross issuance.

5) End of FY cash balance target remains at $45 billion.

6) Net Non-marketable issuance and Miscellaneous Means of Financing are set equal to zero after FY 2008.

7) **No** Entitlement Reform

Source: CBO, The Long Term Budget Outlook, December 2005
Scenario Analysis based on CBO Assumptions

**Scenario A (Intermediate Spending/High Revenue)**

<table>
<thead>
<tr>
<th>Category</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Medicare &amp; Medicare Spending</td>
<td>Excess cost growth of 1 percentage point</td>
</tr>
<tr>
<td>Defense</td>
<td>Gradual phase down through 2024, then grow at CPI</td>
</tr>
<tr>
<td>Individual Income Taxes</td>
<td>Current law (i.e., higher rates after 2010)</td>
</tr>
</tbody>
</table>

**Scenario B (High Spending/High Revenue)**

<table>
<thead>
<tr>
<th>Category</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Medicare &amp; Medicare Spending</td>
<td>Excess cost growth of 2.5 percentage points</td>
</tr>
<tr>
<td>Defense</td>
<td>FYDP¹ through 2024, then grow at CPI</td>
</tr>
<tr>
<td>Individual Income Taxes</td>
<td>Current law (i.e., higher rates after 2010)</td>
</tr>
</tbody>
</table>

**Scenario C (High Spending/Low Revenue)**

<table>
<thead>
<tr>
<th>Category</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Medicare &amp; Medicare Spending</td>
<td>Excess cost growth of 2.5 percentage points</td>
</tr>
<tr>
<td>Defense</td>
<td>FYDP¹ through 2024, then grow at CPI</td>
</tr>
<tr>
<td>Individual Income Taxes</td>
<td>Hold at long run average (18.3% of GDP)</td>
</tr>
</tbody>
</table>

**Common Assumptions for All Scenarios**

- **No Entitlement Reform**
- **Social Security** Benefits paid as scheduled under current law
- **Other Nondiscretionary Spending** Hold at 2005 level as % of GDP
- **Other Discretionary Spending** Hold at historical share of GDP (3.6%)
- **Payroll Taxes** Current law
- **Other Taxes** Hold at 2014 level as share of GDP

1. FYDP - Future Years Defense Program (with allowances for cost risks and additional spending to support the war on terrorism).

Scenario A - Intermediate Spending/High Revenue
Debt/GDP Implications

Treasury Debt/GDP

%
Scenario A - Intermediate Spending/High Revenue
Gross Coupon Issuance/GDP Implications

Gross Coupon Issuance/ GDP

%
Scenario A - Intermediate Spending/High Revenue
Average Maturity of Debt Outstanding Implications

Years

Average Debt Maturity

0 1 2 3 4 5 6 7

93 96 99 02 05 08 11 14 17 20 23 26 29 32 35 38 41 44 47 50
Scenario A - Intermediate Spending/High Revenue
Potential Interest Cost as a Percent of GDP

Interest Expense/GDP
Scenario A - Intermediate Spending/High Revenue
Potential Size of Average Monthly 2-Year and Quarterly 10-Year Note
Scenario A - Intermediate Spending/High Revenue
Potential Annual DV01 of Issuance

Scenario A (Intermediate Spending/High Revenue) - Total Annual DV01 Takedown
Scenario B - High Spending/High Revenue
Debt/GDP Implications
Scenario B - High Spending/High Revenue
Gross Coupon Issuance/GDP Implications
Scenario B - High Spending/High Revenue
Average Maturity of Debt Outstanding Implications
Scenario B - High Spending/High Revenue
Potential Interest Expense as a Percent of GDP
Scenario B - High Spending/High Revenue
Potential Size of Average Monthly 2-Year and Quarterly 10-Year Note

$ Billions

- Average Monthly 2-Year Issuance
- Average Quarterly 10-Year Issuance

07 10 13 16 19 22 25 28 31 34 37 40 43 46 49
Scenario B - High Spending/High Revenue
Potential Annual DV01 of Issuance

Scenario B (High Spending/High Revenue) - Total Annual DV01 Takedown
Scenario C - High Spending/Low Revenue
Debt/GDP Implications
Scenario C - High Spending/Low Revenue
Gross Coupon Issuance/GDP Implications
Scenario C - High Spending/High Revenue
Average Maturity of Debt Outstanding Implications

![Graph showing average debt maturity over years. The x-axis represents years from 1993 to 2048, and the y-axis represents average debt maturity in years. The graph displays a downward trend in average debt maturity over time.]
Scenario C - High Spending/Low Revenue
Potential Interest Cost as a Percent of GDP
Scenario C - High Spending/Low Revenue
Potential Size of Average Monthly 2-Year and Quarterly 10-Year Note

$ Billions

Average Monthly 2-Year Issuance
Average Quarterly 10-Year Issuance
Scenario C - High Spending/Low Revenue
Potential Annual DV01 of Issuance

Scenario C (High Spending/Low Revenue) - Total Annual DV01 Takedown

Year

DV01 in $ millions