Alternative Views on Isssuance Modeling

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Introduction

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- Model uncertainty is a problem.
- Models have difficulty pinning down long-run expectation of short rates.
- Incorporating information from surveys helps.

Expected 10-Year Borrowing Costs from Term Structure Model: 9/2015

3-month	2.03
2-year	2.16
5-year	2.38
10-year	2.14

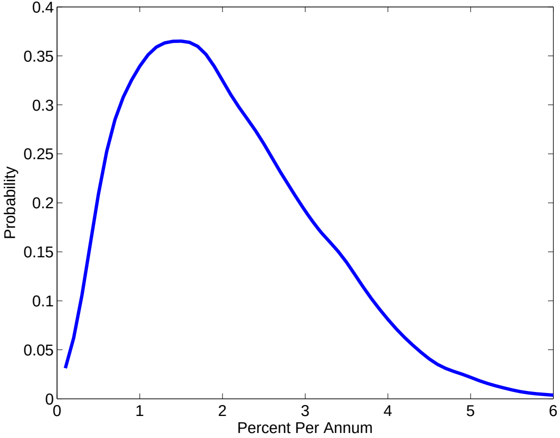
Expected 10-Year Borrowing Costs from Term Structure Model: 12/1999

3-month	5.11
2-year	5.71
5-year	6.06
10-year	6.70

Complications

- Treasury wants stable issuance.
- Issuance affects yields.
- Not a one-shot decision.
  - Short issuance gives option value of reoptimizing.
- Rollover risk.

PDF of 10-year average of 3 month rates from Term Structure Model: 9/2015



Nominal v. TIPS Issuance

- Treasury minimizing expected cost should issue TIPS if breakeven is greater than expected inflation.
- Irrelevant whether difference reflects inflation risk premium or TIPS liquidity premium.

Are TIPS a good deal for Treasury?