

U.S. Banks and Global Liquidity^{*}

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Abstract

We show that ample bank reserves are critical for the well-functioning of short-term funding markets in the new post-crisis monetary policy and regulatory environment. Using daily supervisory data, we find that large U.S. banks use their excess reserves at the Federal Reserve to finance a modest increase in dollar lending in the repo and foreign exchange swap markets in response to dollar funding shortages. Intra-firm transfers between depository institutions and broker-dealer subsidiaries within the same bank holding company are crucial to this type of reserve-based intermediation. Our results highlight the importance of a large Fed balance sheet even when interest rates are above the zero-lower bound in the post-crisis era.

Keywords: Liquidity, Global Banks, Repos, Reserves, Covered Interest Rate Parity

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1 Introduction

The post-Global Financial Crisis (GFC) period features two fundamental changes to the monetary policy and regulatory policy environments. First, central banks quantitative easing (QE) programs led to an expansion of central banks' asset holdings. As a result, banks' cash piles at central banks (known as bank reverses) materially increased beyond the statutorily required levels. Second, post-GFC regulatory reforms increase costs for large global banks to engage in traditional intermediation activities that heavily rely on balance sheet space (for example, [Duffie \(2017\)](#) and [Du, Tepper and Verdelhan \(2018a\)](#)). These two fundamental changes prompted large global banks to use existing bank reserves to support liquidity provision. In this environment, we show reserves play a key role in supporting the well-functioning of short-term funding markets, and thus the transmission of monetary policy. Our results highlight that central bank balance sheets and interest rate policies are intricately linked, as large bank reserves balances and expanded central bank balance sheets have become necessary for the successful implementation of interest rate policy.

We define a new intermediation method, called "reserve-draining intermediation", in which banks finance additional short-term dollar lending by using their reserve holdings, while leaving the overall size of their balance sheets unchanged. This method sharply contrasts with traditional "matched-book intermediation" transactions ([CGFS \(2017\)](#)), in which banks borrow more in order to lend more, expanding the size of their balance sheet and making the Basel III leverage ratio (LR) requirement more binding. Using information on the daily balance sheets of U.S. globally systemically important banks (GSIBs), we show that reserve-draining intermediation is key for U.S. GSIBs' liquidity provision in short-term funding markets during periods of dollar funding shortages. In addition, we also show that intra-firm liquidity sharing between depository institutions

that hold reserves and the affiliated broker-dealers that do most of the short-term dollar lending, are critical to support these reserve-draining intermediation transactions.

Our paper provides a forensic account of U.S. GSIBs’ short-term dollar intermediation activities, which are crucial for monetary policy implementation. This empirical exercise could not be performed in the past due to the absence of high-frequency balance sheet data broken down by currencies and instruments. As part of the regulatory effort to calculate the Basel III liquidity coverage ratio (LCR), the Federal Reserve started to collect detailed daily consolidated bank balance sheet information (and for material entities) by currency for the largest U.S. banks in the FR2052a *Complex Institution Liquidity Monitoring Report*, starting in December 2015. We use aggregated data from the FR2052a report for six GSIBs headquartered in the United States: Bank of America, Citigroup, Goldman Sachs, JP Morgan, Morgan Stanley, and Wells Fargo to shed light on the global dollar intermediation activities of the largest U.S. banks.¹

We focus on the two most important types of short-term dollar lending: dollar lending via repurchase agreements (known as repos) and dollar lending via the foreign exchange (FX) swap market. We estimate that these two types of lending total about \$1.6 trillion in our sample banks. In a repo agreement, a cash loan is collateralized by securities such as Treasury securities. Dollar lending via FX swaps can also be viewed as a form of secured lending collateralized by foreign currency — the borrower receives dollars and posts foreign currency at the spot exchange rate at the inception of the trade and promises to repurchase the foreign currency with dollars at the forward exchange rate at maturity.

We analyze the U.S. GSIBs’ balance sheet responses to three types of dollar funding shortages: on quarter-ends, on days with increases in Treasury General Account (TGA) balances ([Hamilton \(1997\)](#)), and on days with reductions in the Federal Reserve’s System Open Market Account (SOMA) portfolio. We show that repo spreads and FX swap

¹There are currently eight GSIBs in the United States. We exclude the Bank of New York Mellon and State Street from our sample due to their specialization in the custodian business.

spreads are significantly wider on these days. First, quarter-ends are associated with tight dollar funding conditions because non-U.S. banks reduce their low-margin balance-sheet-intensive arbitrage and intermediation activities to "window-dress" the Basel III leverage ratio (LR) on regulatory-reporting dates.² Second, an increase in the Treasury's TGA balance at the Federal Reserve, either due to an increase in the net issuance of Treasury securities or higher tax payments (or lower expenses), reduces reserves from the banking system. Third, a decrease in the Federal Reserve's SOMA portfolio also reduces the level of reserves in the banking system.

We show that U.S. GSIBs modestly increase their short-term dollar lending in repo and FX swap markets during these three types of dollar-shortage events. Importantly, reserve-draining intermediation is the dominant channel for U.S. GSIBs to increase their dollar liquidity provision in our sample period. In other words, the additional short-term lending from U.S. GSIBs is largely financed by a reduction in reserve balances at the Fed rather than additional repo borrowing or deposit inflows.

In terms of economic magnitudes, focusing on quarter-ends, we find that U.S. GSIBs reduce their reserve balances by about \$60 billion, and increase their net repo lending by \$40 billion and dollar lending in the FX swap market by \$20 billion. The increase in the net repo lending is primarily driven by a reduction in the gross repo borrowing while holding the gross repo lending steady. Using a multivariate regression controlling for quarter-ends, daily fluctuations in the TGA balance and the SOMA portfolio, we find that in response to a one-standard-deviation change in the daily TGA balance (about \$20 billion), U.S. GSIBs significantly reduce their reserve balances by about \$3.6 billion, while increasing their net repo lending by \$7.4 billion and FX lending by \$6.2 billion. The impact of daily changes in the SOMA holdings is also significant for intermediation

²In most non-U.S. jurisdictions, the Basel III leverage ratio is calculated using quarter-end snapshots of bank balance sheets. For U.S. banks, the LR is calculated based on the daily average of bank assets. The quarter-end effects in repo and FX swap rates have been documented in [Munyan \(2017\)](#) and [Du, Tepper and Verdelhan \(2018a\)](#).

activities and generally affect spreads and bank balance sheets in the opposite direction as the TGA fluctuations.

We find additional evidence for the reserve-draining intermediation channel by studying the direction and intensity of intra-firm liquidity flows within bank holding companies (BHCs). Given that most of the short-term liquidity provision is done by broker-dealers, but only depository institutions can hold reserves, intra-firm transfers between broker-dealers and depository institutions are crucial. To keep the reverse repo lending position steady and to expand dollar lending in the FX swap market, the broker-dealer arm increases internal repo borrowing from the non-broker dealer arm of the bank. The non-broker dealer arm of the bank (largely depository institutions), in turn, finances the intra-firm transfer through a reduction in reserve balances.³ The internal liquidity sharing between depository institutions and broker dealers adds a new dimension to banks' internal liquidity management documented in [Campello \(2002\)](#) and [Cetorelli and Goldberg \(2012\)](#).

Furthermore, we show that the distribution of reserves among U.S. GSIBs, foreign banks, and other U.S. banks react strongly to dollar funding conditions. Holding the size of the Fed's assets constant, a reduction in the reserve balance of U.S. GSIBs must translate into an increase in the reserve balance of other banks in the system or an increase in non-reserve liabilities of the Federal Reserve.⁴ Using daily data on reserve balances for all banks, we find that U.S. GSIBs and foreign banks significantly reduce their reserve balances during dollar funding shortage episodes, while other smaller U.S. banks and the overnight reverse repurchase agreement (ON RRP) facility become the recipients of these reserve outflows, particularly at quarter-ends. Our results suggest that large non-

³We note that intra-firm transfers that are used to accommodate cash demands at the entity level are mainly achieved through internal repo transactions, as such transactions protect individual entities from a resolution planning standpoint. Additionally, this type of transaction is exempted under certain circumstance from the Regulation W quantitative limits on transactions between depository institutions and affiliates within a BHC.

⁴The three most important non-reserve liability items are currency in circulation, reverse repo positions of non-banks at the Fed, and the TGA.

U.S. global banks are also potentially conducting significant amounts of reserve-draining intermediation in dollar funding markets.

The central role of reserves to absorb large dollar funding shocks helps us better understand the money market turmoil in September 2019, during which the repo rate increased by nearly 10 percent and the FX swap market rate increased by 6 percent. Before the rate spikes, the total amount of reserves in the banking system reached multi-year lows as a result of Fed balance sheet normalization. A low level of reserves impairs reserve-draining intermediation. In the aftermath of the repo rate spike in September 2019, the Fed re-established the repo facility to allow primary dealers to borrow directly from the Fed. We find that liquidity from the Fed partly substituted broker-dealers' intra-firm borrowing from depository institutions as part of their reserve-draining intermediation transactions, while helping to boost U.S. GSIBs' dollar lending in the repo and FX swap markets.⁵

Reserve-based intermediation became dominant in the context of fundamental changes to the monetary policy regime and regulatory environment post-GFC. First, prior to the GFC, total drainable reserves for the banking sector were zero. Banks financed their immediate cash needs by either borrowing from each other in an actively traded federal funds market or by accessing Fed intraday credit in the form of overdrafts. Post-GFC, drainable reserves were created as a result of the Fed's QE programs, which provides a pre-condition for the reserve-based intermediation to take place. Second, in the post-GFC regulatory environment, banks face higher balance sheet costs to intermediate in global

⁵The money market turmoil in September 2019 prompted many commentary pieces from policymakers and market observers. [Pozsar \(2017, 2019\)](#) voiced concerns with excess balance sheet normalization prior to the repo market turmoil and detailed potential liquidity concerns associated with Treasury settlements. [Gagnon and Sack \(2019\)](#) have made several suggestions focusing on the Federal Reserve's operational framework including the setting of a standing repo facility, higher reserve levels, and explicit directives to control the repo rate. [Tarullo \(2019\)](#) highlights several questions yet to be addressed with the current monetary policy and regulatory frameworks. [Avalos, Ehlers and Eren \(2019\)](#) attributes part of the repo turmoil to hedge funds' use of repo. [Afonso, Cipriani, Copeland, Kovner, La Spada and Martin \(2020\)](#) provides a detailed account of the event and highlights the role of reserves and interbank market frictions. [Anbil, Anderson and Senyuz \(2020\)](#) emphasizes trading relationships in the repo market turmoil.

dollar funding markets. Reserve-based intermediation is often preferred as it is ex-post neutral to key Basel III regulatory ratios, such as the LR and the LCR.

Nevertheless, reserve-based intermediation faces different and new types of balance sheet constraints. In particular, banks are reluctant to use existing reserves to lend in higher-yielding repo and FX swap markets due to constraints on intraday liquidity needs and the required distribution of liquidity across entities and jurisdictions for resolution planning purposes. These new balance sheet considerations partly explain why U.S. GSIBs' additional reserve-draining liquidity provision appears to be modest during periods of funding shortages and why various intermediation spreads persist even when total reserves appear to be abundant. In closely related recent papers, [Copeland, Duffie and Yang \(2020\)](#) provides a detailed empirical account at the intraday frequency to highlight the crucial role of reserves in alleviating intraday repo payment timing stress. [D'Avernas and Vandeweyer \(2020\)](#) and [Yang \(2020\)](#) explicitly model the impact of intraday liquidity constraints on money market dislocations. The non-linearities in the model are able to generate large spikes in repo rates. Beyond the intraday liquidity constraint, the distribution of liquidity across entities and jurisdictions is also a particularly important concern for dollar lending in the FX swap market, as it requires draining reserves in the U.S. and moving the liquidity to non-U.S. jurisdictions. Together, these balance sheet considerations add a new perspective to the large growing literature on arbitrage and intermediary asset pricing, which primarily focuses on the intermediary size and leverage constraints.⁶ The positive profits associated with reserve-based intermediation shed light on the shadow cost of other types of balance sheet constraints beyond size and leverage.

The crucial role of reserves in supporting short-term market functioning adds an important dimension to the effect of unconventional monetary policy. As recently summarized in [Carlson, D'Amico, Fuentes-Albero, Schlusche and Wood \(2020\)](#), the effects of the Fed

⁶For example, [Brunnermeier and Pedersen \(2008\)](#); [He and Krishnamurthy \(2013\)](#); [Adrian, Etula and Muir \(2014\)](#); [Adrian and Shin \(2010\)](#); [He, Kelly and Manela \(2017\)](#); [Andersen, Duffie and Song \(2019\)](#); [Du, Hébert and Huber \(2019\)](#)

balance sheet policies have largely been examined in the context of providing accommodation to the real economy through the signaling channel, the duration-risk channel, and the portfolio rebalancing channel. In addition, [Greenwood, Hanson and Stein \(2016\)](#) also discuss the role of balance sheet policy as a financial stability tool. As money markets are heavily intermediated by global banks subject to various balance sheet constraints, our results imply that a large Fed balance sheet may need to stay even when short-term interest rates are above the zero-lower bound, because ample reserves are required to maintain control over short-term interest rates.

In addition, our paper provides new insights into the role of global banks in providing liquidity by exploiting synergies between the traditional banking and "shadow banking" arms within BHCs. The role of traditional banks in supplying liquidity through their issuance of demand deposits has been widely recognized in earlier studies that emphasize liquidity transformation ([Diamond and Dybvig \(1983\)](#)), information-insensitive claims ([Gorton and Pennacchi \(1990\)](#)), connections between loans and deposits ([Kashyap, Rajan and Stein \(2002\)](#)), and market power in the deposit markets ([Drechsler, Savov and Schnabl \(2017\)](#)). The GFC has led to a separate line of inquiry into the role of non-depository financial institutions, generally referred to as "shadow banks", that engage in repo financing and liquidity transformation ([Gorton and Metrick \(2012\)](#); [Krishnamurthy, Nagel and Orlov \(2014\)](#)). While the literature has articulated important differences between traditional commercial banks and shadow banks (for example, [Hanson, Shleifer, Stein and Vishny \(2015\)](#)), the two types of entities are often studied in silos and their linkages are little understood. The shared usage of reserves and internal liquidity between depository institutions and the affiliated dealers documented in our paper, highlight the importance of having both traditional banks and broker-dealers organized under the same BHC structure.

From an international finance perspective, given the predominant role of the U.S. dollar in global trade and financial transactions (for example, [Bruno and Shin \(2015\)](#), [Maggiore](#),

Neiman and Schreger (Forthcoming), Gopinath et al. (2020), and Bank for International Settlements (2020)), short-term dollar funding is the lifeblood of the modern financial system.⁷ Covered interest rate parity (CIP) deviations capture a picture of some recurrent strains in global dollar funding conditions post-GFC. On the pricing side, we meticulously construct overnight CIP deviations based on central bank deposit rates, which provide a clean measure of riskless profits that large global banks can make by engaging in reserve-based CIP arbitrage.⁸ On the quantity side, our paper provides the first granular account of balance sheet adjustments of U.S. GSIBs in response to fluctuations in CIP deviations, and quantify the amount of CIP arbitrage.

The rest of the paper is organized as follows. Section 2 provides an overview of the data. Section 3 discusses types of short-term dollar lending and intermediation. Section 4 presents main results on U.S. GSIBs’ response to dollar funding shortages. Section 5 discusses the money market turmoil in September 2019. Section 6 provide additional discussions on the advantages and constraints of reserve-draining intermediation for global banks. Section 7 concludes.

2 Data Description and Summary Statistics

2.1 Daily Bank Balance Sheets for U.S. GSIBs

We construct detailed bank balance sheets at the daily frequency using data collected by the Federal Reserve using form FR2052a, *Complex Institution Liquidity Monitoring Report*. These data are used for the calculation of the Basel III LCR, which requires that banks hold enough high quality liquid assets to fund net expected cash outflows

⁷Liquidity and safety of dollar-denominated assets are the bedrock of international financial systems, such as in Farhi and Maggiori (2018), Gopinath and Stein (2018), He, Krishnamurthy and Milbradt (2019) and Jiang, Krishnamurthy and Lustig (2020).

⁸This is different from the large literature on CIP deviations based on bank rates, Treasury and corporate bond yields (for example, Du, Tepper and Verdelhan (2018a); Du, Im and Schreger (2018b); Jiang, Krishnamurthy and Lustig (2018, 2019); Anderson, Du and Schlusche (2019); Liao (2020); Liao and Zhang (2020))

for 30 days. These bank-level data contain a detailed breakdown of individual banks’ asset inflows and liability outflows on a consolidated basis, as well as by material legal entities. Banks with \$700 billion or more in total consolidated assets or \$10 trillion or more in assets under custody are required to report this information on each business day beginning in December 2015.

Our analysis focuses on the aggregate data for six U.S. GSIBs: Bank of America, Citigroup, Goldman Sachs, JP Morgan, Morgan Stanley, and Wells Fargo. As the data collection is designed for LCR assessment rather than balance sheet reporting, we perform a manual mapping of the inflow and outflow product categories collected in FR2052a to asset and liability line items in the quarterly call reports collected through FR Y-9C forms at the consolidated bank holding company level. The balance sheet assembly and matching process is meticulous and achieved through iterative comparison with FR Y-9C.⁹

There are several novel aspects of the LCR assessment data that relates to our analysis. First, the data capture the global activities of reporting U.S. banks, which allows for a comprehensive analysis of these institutions’ exposure in different currencies and locations. Second, the data is collected daily and as such, offers a look into the high-frequency changes that these institutions make to their balance sheets. Third, the data allows us to assess the intermediation activities at the consolidated level and the material legal entity level. This allows us to assess whether banks move funds across material entities to manage their liquidity, as a result of specific events. Last, the granularity of the inflow and outflow data also provides a view into hard to find details about bank balance sheet items, including the remaining maturity and the collateral type used, when it is applicable.

⁹The FR2052 data is mainly composed of inflow items that correspond generally to assets and outflow items that correspond generally to liabilities. However, there are caveats to these generalizations. We exclude a number of the inflow and outflow categories in the LCR assessment that are off-balance sheet or contingency facilities, e.g. loan or liquidity facilities on which either the banks or their clients can draw on. For some inflow and outflow LCR items, we rely additionally on the collateral type reported for the proper assembly of the balance sheet snapshots. We discuss the comparison between FR2052a and FR Y-9C in greater detail in Appendix A. Appendix Figure A1 shows that the key balance sheet items from the two data sources are broadly in line.

2.2 Summary Statistics of Balance Sheets by Currency

Figure 1 shows the balance sheet of dollar-denominated assets and liabilities aggregated across the six banks in our sample. We can see that the overall assets and liabilities of U.S. banks are broadly equivalent in size, with the assets averaging to \$7.4 trillion and liabilities averaging to \$7.2 trillion. The gap in dollar-denominated assets and liabilities only averages to 4% of total assets. Loans represent the largest asset category and deposits represent the largest dollar-denominated liability. The short-term liquid component of the balance sheet, such as reverse repos (and repos), cash and reserves, and Treasury securities account average to about \$2 trillion.

Figure 2 shows the evolution of assets and liabilities denominated in euros (EUR), yen (JPY), sterling (GBP), and Australian (AUD) dollars, respectively. The size of all foreign-currency-denominated assets is about \$1.7 trillion and the average size of all foreign currency denominated liabilities is about \$1.4 trillion. The foreign currency funding gap, or the difference between assets and liabilities denominated in foreign currencies, is about to \$300 billion, or 17% of the size of total foreign currency assets. In contrast to the dollar-denominated balance sheet items, the foreign currency balance sheets have a markedly lower fraction of loans in total assets and a lower fraction of deposits in total liabilities. Reverse repos and repos represent the largest balance sheet items denominated in foreign currency.

3 Dollar Lending in Repo and FX Swap Markets

In this section, we first describe two types of dollar liquidity provision in repo and FX swap markets. We then introduce two types of intermediation methods: matched-book and reserve-draining intermediation, which are used to finance the provision of short-term dollar liquidity.

3.1 Definition and Measurement

We focus on the two most important types of collateralized short-term lending done by U.S. GSIBs: dollar lending in the repo market and dollar lending in the FX swap market. These two types of lending are the most liquid and scalable components of bank’s overall dollar lending. As opposed to traditional bank loans to businesses and households, banks can easily change the scale of these positions on a daily basis.

Figure 4 shows schematically these two types of dollar lending. As shown in Panel A, at the inception of a dollar repo loan, a bank (e.g., JP Morgan) lends dollars against some collateral, most commonly U.S. Treasury securities. At maturity, the bank receives the principal and interest payment in dollars and returns the collateral. Repo lending is referred to as a reverse repo position on the bank’s balance sheets. We can directly observe the amount of reverse repo positions denominated in dollars from our constructed balance sheet.¹⁰

Panel B of Figure 4 shows the mechanics of dollar lending in the FX swap market, which is a form of collateralized lending in the sense that the foreign currency is posted as collateral against U.S. dollar lending. To lend dollars in the FX swap market (e.g., the dollar-yen swap market), at the inception of the trade, the bank lends dollars through an FX swap dealer, receives yen in exchange at the spot exchange rate, and on-lends the yen. The bank has the option to on-lend the yen without credit risk, for example, by depositing the yen at the Bank of Japan’s deposit facility or lending it in the Japanese repo market backed by Japanese government bonds. In addition, the bank promises to buy dollars for yen at the forward exchange rate. At maturity, the bank receives the yen principal and interest payment and fulfills the terms of the forward contract by exchanging yen for dollars.

¹⁰We also consider fixed income security lending and borrowing positions that are much smaller in size relative to repo and reverse repo positions but are functionally similar in our analyses.

The challenge to measure dollar lending via the FX swap market is that the position is off balance sheets and not directly observable. However, given that dollar lending via the FX swap market is accompanied by foreign-currency on-lending on balance sheets, we can construct an empirical proxy for FX lending positions based on balance-sheet items. Our benchmark measure for short-term FX swap lending (*Short-Term FX Swap Lend*) is equal to the sum of net repo lending in foreign currency and excess reserve balances in foreign currency:

$$\textit{Short-Term FX Swap Lend} = \textit{FC Reverse Repo} - \textit{FC Repo} + \textit{FC Excess Reserve}. \quad (1)$$

The assumption behind this measure is that banks choose secured foreign currency on-lending to minimize their credit risk so that an increase in the short-term dollar lending in the FX swap market (e.g. for the dollar-yen FX swap) is associated with an increase in the reverse repo position in yen (not matched by an increase in the repo position in yen) or an increase in the reserve balances at the Bank of Japan. While the high-frequency variation in our *Short-Term FX Swap Lend* measure provides relevant information about the fluctuations in short-term dollar lending in the FX swap market, the level of *Short-Term FX Swap Lending* could overstate the amount of FX swap lending. This is because banks may hold excess reserves in foreign currency for reasons other than supporting dollar lending in the FX swap market. In Section 4.5.1, we present robustness checks for our main results using an alternative proxy of FX swap lending that takes the difference between total foreign currency assets and foreign currency liabilities.

Figure 3 shows the amount of reverse repo positions, our proxy for short-term dollar lending in the FX swap market, along with the total reserve balances at the Federal Reserve for our sample of U.S. GISBs. We can see that reverse repo positions is the largest item totaling over \$1 trillion. Our proxy for FX swap lending is significantly lower and averages to about \$300 billion in our sample period. It is worth noting that since

late 2017, when the Federal Reserve started reducing the size of its balance sheet, the decline in reserves balances has been associated with a significant increase in the reverse repo position.

3.2 Matched-Book and Reserve-Draining Intermediation

How do U.S. GSIBs finance their short-term dollar liquidity provision? We now discuss two types of intermediation methods, matched-book and reserve-draining, which allow banks to scale up or down short-term dollar lending in the repo and FX swap markets at a high frequency. We illustrate these two intermediation methods in Figure 5.

To start, Panel A of Figure 5 presents the baseline balance sheet that consists of dollar-denominated short-term scalable assets, namely reverse repos (RRP), short-term FX swap lending (FX Lend), and drainable excess reserve balances.¹¹ The last item, drainable excess reserves, measures excess reserves that the bank holds at the Federal Reserve beyond those determined by reserve requirements and other regulatory demands. Post-crisis liquidity regulations have increased banks' demand for reserves, over those usually maintained for reserve requirement purposes. However, the exact amount of drainable reserves is unknown, but is certainly lower than total excess reserve balances, as shown in Figure 3. On the liability side of our scalable balance sheet, we have repos and deposits, which fund reverse repo, FX swap lending, and drainable excess reserve positions.¹²

The first intermediation method, matched-book intermediation, is illustrated by Panel B of Figure 5, which features simultaneous changes in the bank's assets and liabilities. For example, if the bank wants to lend additional dollars in the repo market, it needs to

¹¹By combining the foreign currency on-lending and an FX swap, we treat synthetic dollar lending in the FX swap market as an on-balance-sheet item.

¹²We purposely exclude unsecured wholesale funding instruments (such as fed funds, eurodollars, commercial paper and certificate of deposits) from the liabilities because U.S. GSIBs' reliance on these sources of unsecured wholesale funding is small during our sample period based our data. This fact is also separately documented in [Anderson, Du and Schlusche \(2019\)](#). As presented in Figure 1, U.S. GSIBs have smaller repo positions compared to their reverse repo positions, so a certain amount of deposits is needed to support the short-term dollar liquidity provision. However, since deposits are rather sticky, the bank cannot rely on deposits to scale their liquidity provision at a high frequency.

borrow additional dollars in the repo market. On the bank's balance sheet, we can see that an increase in the reverse repo position is matched by the same increase in the repo position. Any matched-book intermediation transactions result in a larger balance sheet for the bank.

The second intermediation method, reserve-draining intermediation, is illustrated by Panel C of Figure 5. It features a change in the composition of assets while maintaining the overall size of the balance sheet unchanged. In this case, the bank can "drain" reserves to finance an expansion of repo lending, without additional borrowing. On the bank's balance sheet, we can see that the increase in the reverse repo position is matched by a reduction in the drainable reserve balance by the same amount. There are no changes to banks' liabilities.

Intra-firm transfers between depository institutions and broker-dealers within the BHC play a central role in reserve-draining intermediation. As shown in Figure 6, only depository institutions have reserve accounts at the Federal Reserve, but most of the reverse repo and repo positions are booked on the broker-dealers' balance sheet. The mechanics of the reserve-draining intermediation is that the depository institutions reduce their reserve balance and lend the cash to a broker-dealer within the same BHC through an internal repo position, the broker-dealer then uses the internal repo from the depository institution to finance its additional external repo lending. After netting out internal repo positions, the overall size of the BHC's balance sheet remains unchanged after additional reserve-draining intermediation.¹³

Matched-book intermediation and reserve-draining intermediation have different regulatory implications. The most important difference is that additional matched-book intermediation increases the overall size of the bank balance sheet, but additional reserve-

¹³Regulation W, which implements sections 23A and 23B of the Federal Reserve Act, establishes restrictions on transactions between depository institutions and its affiliates. The regulation sets quantitative limits on transactions that are covered by the rules. Importantly, transactions that are collateralized by U.S. government securities are not subject to the quantitative limits (equivalent to 10% of capital stock and surplus).

draining intermediation leaves the overall balance sheet size unchanged at the BHC level.¹⁴ However, reserve-draining intermediation can be constrained by additional regulatory and internal risk management practices, especially regarding intraday liquidity and how liquidity can be allocated across material entities and jurisdictions.

As we will see in Sections 4 and 5 that reserve-draining intermediation plays a dominant role during episodes of dollar funding shortages. Then will discuss in greater detail in Section 6 why global banks choose reserve-draining over matched-book intermediation on the difficult days, and specific factors that constrain the magnitude of reserve-draining activities.

4 Dollar Funding Shortages and Response of U.S. GSIBs

In this section, we assess the response of U.S. GSIBs to high-frequency fluctuations in dollar funding and cash liquidity demand. In particular, we examine three types of events: first, contraction of dollar intermediation by foreign banks on period-end regulatory reporting dates, second, large fluctuations in TGA balances, and third, changes in the Fed SOMA portfolio holdings. We find that all three types of fluctuations have a substantial impact on the scarcity value of the dollar and elicit responses from the U.S. GSIBs as they optimize their balance sheets. We first introduce the three types of dollar funding events and demonstrate their effects on the intermediation spreads. We then discuss U.S. GSIBs' balance sheet response. Finally, we also describe changes in the distribution of reserves across different types of banks. All the analyses are based on the sample from December 15, 2015, to August 31, 2019, prior to the repo rate spike in September 2019.

¹⁴For the Basel III LCR, matched-book intermediation is LCR-neutral if the change in the repo and reverse positions have the same maturity and collateral. Reserve-draining intermediation is also LCR-neutral if the increase in the reverse repo position is collateralized by U.S. Treasury securities, as reserves and Treasury securities both count towards Level 1 high quality liquidity assets.

4.1 Three Types of Dollar Funding Shortage

We now describe three types of dollar funding shortages examined in our paper. First, dollar funding conditions are particularly tight on quarter-ends. The quarter-end liquidity premium predominately arises due to a significant contraction in foreign banks' dollar intermediation activities to meet regulatory requirements in their own jurisdictions [Du, Tepper and Verdelhan \(2018a\)](#); [Cenedese, Della Corte and Wang \(2019\)](#); [Egelhof, Martin and Zinsmeister \(2017\)](#). Of particular importance, in most non-U.S. jurisdictions the Basel III LR is assessed using banks' balance sheet size on quarter-ends.¹⁵ This reporting requirement incentivizes foreign banks to significantly reduce matched-book dollar intermediation activities on quarter-ends in order to have better reported LRs, contributing to spikes in short-term intermediation spreads. In contrast to the foreign banks, U.S. banks calculate the leverage ratio based on the daily-average of assets in each quarter. Therefore, U.S. banks have considerably more balance sheet space for dollar intermediation activities on quarter-ends compared to foreign banks.

Second, fluctuations in the TGA account balance are also significantly correlated with dollar funding conditions. The TGA contains cash balances that the U.S. Treasury holds at the Federal Reserve. Other things being equal, an increase in the TGA balance corresponds to a reduction in the overall cash for the entire banking system, making dollar liquidity more scarce.¹⁶ Similarly, [Hamilton \(1997\)](#) has used Treasury cash balances in commercial banks to identify liquidity shocks.¹⁷ Since May 2015, the TGA balance has been particularly volatile, ranging from a minimum of \$23 billion to a high of \$440 billion.

¹⁵In addition to quarter-end reporting, banks in some jurisdictions follow Basel III guidelines for calculating the LR using month-end averages of banks' assets within a quarter. U.K. banks switched from three month-end-averaging for the LR calculation to daily-averaging beginning in 2018.

¹⁶This is because a higher TGA balance, either due to higher net Treasury issuance or higher taxes correspond to a transfer of cash from the bank account of the buyer of the Treasury or the taxpayer to the U.S. treasury's account at the Fed.

¹⁷The methodology in [Hamilton \(1997\)](#) exploits the forecasting error in Treasury cash holdings in private banks, a setup specific to the pre-GFC regime in which the Federal Reserve conducted daily open market operations to control the Fed Funds rate based on forecasts of banking reserves.

The weekly changes in the TGA balance have a standard deviation of \$40 billion, with a maximum weekly change exceeding \$100 billion. Appendix Figure A2 presents the time series of the TGA balance.¹⁸

Third, fluctuations in the Fed SOMA portfolio also affect dollar funding conditions. In our sample, between October 2017 and August 2019, the Federal Reserve reduced its Treasury holdings at the rate of \$35 to \$50 billion a month, a process known as the balance sheet normalization or taper. A reduction in the SOMA's Treasury holdings corresponds to a reduction in the overall reserve balance for the banking system and an increase in the Treasury securities held by financial market participants, likely increasing financing needs and tightening funding conditions.

4.2 Impact on the Intermediation Spreads

Banks engage in dollar intermediation activities because they earn an intermediation spread, and these intermediation spreads increase during episodes of dollar funding shortage. The exact intermediation spread depends on the intermediation method and funding markets. We show that all these intermediation spreads increase during the three types of dollar funding shortages described in the previous subsection.

In the repo market, the spread on the matched-book intermediation that the bank can earn is determined by the difference between the U.S. GSIBs' funding cost in the repo market and its lending rate in the reverse repo market. We use the triparty Treasury repo spread as the proxy for GSIBs' repo funding rate and the General Collateral Financing (GCF) repo rate as the proxy for their lending rate in the reverse repo market.¹⁹

¹⁸Prior to 2009, the Treasury held most of its cash balances in commercial bank deposit accounts through the Treasury Tax and Loan program. The Treasury shifted to holding cash balances at the Federal Reserve in the fall of 2008 to facilitate the Fed's large expansion of lending to financial firms (Santoro, 2012). In May 2015, the Treasury expanded its TGA balance to protect against "a potential interruption in market access," with a minimum balance of \$150 billion (Treasury Quarterly Refunding Statement, May 2015).

¹⁹The triparty repo market is where large, high-quality, dealers borrow from U.S. money market funds, and the GCF repo market is where large dealers lend to smaller dealers. As a result, the GCF-triparty repo spread measures the compensation that large dealers earn when providing matched book intermediation.

Alternatively, for the reserve-draining intermediation, the bank earns an intermediation spread captured by the difference between the reverse repo lending rate and the opportunity cost of not holding reserves, which equals the foregone interests on reserves (IOR). We use the GCF-IOR spread as the repo spread for reserve-draining intermediation.²⁰ Panel (A) of Figure 7 shows these two repo intermediation spreads. We can see that the GCF-triparty spread is almost always positive. Outside the large spikes on period ends, the GCF-triparty spread is on average about 10 basis points in our sample period. In contrast, the GCF-IOR spread was negative until early 2018 and then became positive and of similar magnitude compared to the GCF-triparty repo spread. The sign-switch for the GCF-IOR spread likely reflects the fact that as the amount of drainable reserves declined for large banks, constraints on reserve-draining activities became more binding, and as a result, banks started to charge a positive intermediation spread between the reverse repo rate and the IOR.

In the FX swap market, we measure the intermediation spread for lending dollars as the *overnight* CIP deviations between overnight central bank deposit rates.²¹ We conduct a meticulous calculation for the overnight FX swap rate following a strict set of market conventions, the first time in the literature to our knowledge, in order to be as analogous as possible to an overnight dollar reverse repo.²² Panel (B) of Figure 7 shows the spread

²⁰We also present results on an additional spread measure using SOFR minus IOR to show the impact on the benchmark rate that is set to replace LIBOR.

²¹This is the spread on the reserve-draining intermediate in the FX swap market, and the matched-book FX swap spreads are similar in levels.

²²To calculate overnight FX-implied dollar funding rate, we use the following formula:

$$r_{implied} = ((1 + r^* * N/d) * (S - \phi_{TN}/D)) / (S - \phi_{TN}/D - \phi_{ON}/D - 1) * (d/N),$$

where $r_{implied}$ is the FX-implied dollar rate, r^* is the non-dollar interest rate on reserve, S is the spot exchange rate, ϕ_{TN} and ϕ_{ON} are the forward points on the overnight and tomorrow next contracts, $d = 360$ is the day count convention, D is the forward point multiplier, and N is the number of calendar days from valuation to settlement date following FX holiday calendar conventions. This formula is more involved than the textbook forward and spot relation since the market convention in FX is that the spot exchange rate is quoted to settle on $T + 2$, effectively making spot contracts a two-day forward exchange rate. To obtain the overnight implied rate, it is important to adjust the spot exchange rate to a hypothetical contract that settles at T rather than $T + 2$.

between the swapped BOJ and ECB deposit rates in dollars and the IOR paid by the Federal Reserve. Excluding the large period-end spikes, the average FX swap spreads are 15 and 25 basis points for the yen and the euro, respectively, despite the BOJ's and the ECB's negative deposit rates. Once we swap these negative deposit rates into dollars overnight, they are more attractive than the IOR paid by the Federal Reserve. Unlike the GCF-IOR spread, the FX swap spread based on central bank deposit rates is largely positive throughout our sample, including in the earlier sample when the drainable excess reserves at the Federal Reserve were more abundant. Lending dollars in the FX swap market is on average more profitable than lending dollars in the repo market.

Table 1 shows regression results capturing the relation between quarter-ends, fluctuations in the TGA balance, and SOMA portfolios and the intermediation spreads. The first four columns show effects on daily changes in various repo spreads, and the last two columns show the effects on daily changes in the FX swap spreads. The independent variables are $Qend_t$ and $Qstart_t$ indicator variables, which denote the last and the first business day of the quarter, daily changes in the TGA balance, ΔTGA_t , and daily changes in the SOMA holding of Treasury securities, $\Delta SOMA_t$.

We can see clear quarter-end effects on intermediation spreads, as captured by the coefficients on the quarter-end and quarter-start indicator variables. On the last day of the quarter, repo spreads increase between 8 to 30 basis points. FX swap spreads increase over 100 basis points and 400 basis points for the dollar-euro and the dollar-yen swap, respectively. These quarter-end spikes quickly normalize after the end of the quarter, as indicated by negative coefficients on $Qstart_t$ of similar magnitude compared to the coefficients on $Qend_t$.²³ Furthermore, fluctuations in the TGA balance, ΔTGA_t are also significantly positively correlated with intermediation spreads. In particular, a 100 billion increase in the TGA balance increase the repo spreads between 4 and 7 basis points, and

²³Standard event-study style charts showing the effect of period-ends on intermediation spreads are shown in Appendix Figure A3.

FX swap spreads by 25 and 41 basis points. Finally, changes in the SOMA portfolio, captured by the coefficient on $\Delta SOMA_t$, are generally negatively correlated with dollar intermediation spreads. Therefore, as the Fed decreased the size of its SOMA portfolio (negative $\Delta SOMA_t$), intermediation spreads increased.

4.3 U.S. GSIBs' Response to Dollar Funding Shortages

Having documented the price response to dollar funding shortages, we now examine the response of the U.S. GSIBs through their intermediation activities. We first discuss balance sheet adjustments of U.S. GSIBs on quarter-ends based on event-study analysis, and then we discuss multivariate regression analysis of balance sheet items on three types of funding shortages.

4.3.1 Quarter-end Event Study

We begin by describing the quarter-end dynamics since their well-defined timing allow us to visualize the impact of funding shortage on U.S. GSIBs' activities using an event study approach.²⁴

Reserves play a key role in supporting liquidity provision of U.S. GSIBs on quarter-ends. Figure 8 presents changes in U.S. GSIBs' scalable balance sheet items near quarter-ends. The horizontal axis indicates the number of business days from the adjacent quarter-end. In terms of short-term dollar lending, we can see the U.S. GSIBs maintain their dollar reverse repo position steady, and increase their dollar lending in the FX swap market by \$20 billion on quarter-ends. This modest increase in the overall short-term dollar lending is financed entirely via draining reserves, as opposed to additional borrowing in the repo

²⁴We show similar patterns for the year-end and month-end dynamics in the Appendix Figures A4 and A5. Month-ends are special because the Basel III LR is calculated as the average of the past three month-ends in some jurisdictions. Year-ends are associated with worse funding conditions than quarter-ends because in addition to the LR, global banks also face the GSIB capital surcharge, largely based on the year-end balance sheet. In addition, European banks also face some additional capital levy based on the-year balance sheet.

market. Repo borrowing of U.S. GSIBs actually declined by \$40 billion on quarter-ends, but reserves declined by \$60 billion. The overall draining in reserves is enough to fully offset the \$40 billion decline in repo borrowing, and to support a steady amount of repo lending and \$20 billion increase in the FX swap lending on quarter-ends. The higher amount of lending in the FX swap market by U.S. GSIBs on quarter-ends likely reflects the higher intermediation fees earned in the FX swap market.²⁵

Using the limited daily data reported from the U.S. operations of four foreign banks in 2052a, we also find that reserves play a similarly important role in supporting an increase in the *net* liquidity provision of foreign banks, despite a significant contraction in foreign banks' gross lending on quarter-ends. Figure 9 shows the U.S.-based entities of the four foreign banks contracted their repo lending by \$60 billion on quarter-ends, in a direct contrast to a steady reverse repo position of the U.S. GSIBs. Meanwhile, repo borrowing of these foreign banks contract by \$80 billion. We can see that reserves declined by about \$20 billion, which is equal to the \$20 billion increase in the net repo lending by foreign banks.²⁶

As illustrated in Figure 6, since depository institutions hold reserves and broker-dealers do most of the short-term lending in the repo and FX swap market, the quarter-end reserve-draining should be accompanied by an internal liquidity sharing between broker-dealers non-broker-dealer affiliates. Figure 10 shows that this is indeed the case. On quarter-ends, the broker-dealer arm of the U.S. GSIBs reduces its external repo borrowing by about \$30 billion (left panel), which accounts for almost the entire decline in the total repo borrowing of the BHC. To replace the lost external funding, broker-dealers turn to internal funding from non-broker-dealer entities in the same BHC (right panel). Broker-dealers' net internal repo borrowing increases by \$30 billion. Again, this internal

²⁵Standard event-study style charts showing the effect of period-ends on intermediation spreads are shown in Appendix Figure A3.

²⁶Note that we only observe the U.S. operations of these foreign banks, so we cannot construct our measure of the dollar lending in the FX swap market

transfer is made possible by the non-broker-dealer entities (e.g. depository institutions) draining reserves from their Federal Reserve accounts. Market observers have previously hypothesized that such use of reserves by banks to finance short-term lending, termed "fracking", amounted to sterilization in FX swaps (Pozsar, 2017). Our findings provide micro-evidence that is consistent with "reserve fracking" on quarter-ends. Meanwhile, our results highlight the important role of liquidity management within BHCs to absorb high-frequency liquidity shortages ((Cetorelli and Goldberg, 2012)).

4.3.2 Regression Analysis with Quarter-Ends, TGA and SOMA Variations

Table 2 presents quantity regressions for intermediation activities with respect to quarter-ends, and variations in the TGA balance and SOMA holdings. We first quantify the quarter-end effects in the multivariate regression. The last day of the quarter, as indicated by the dummy variable $Qend_t$, is associated with a \$26 billion contraction in aggregate U.S. GSIB reserve balances (column 1). Similar to the event study, reverse repo lending is largely unchanged (column 2) while repo borrowing by these banks declines by around \$30 billion (column 2), resulting in a net increase in reverse repo lending (gross reverse repo minus repo, column 4). FX lending activities also increase by around \$10 billion (column 5). These coefficients have smaller magnitudes than the multi-day responses shown in Figure 8. This is in part due to the fact that the adjustment for short-term intermediation activities with maturities greater than overnight can take place a few days before the quarter-ends.²⁷ The last two columns (columns 6 and 7) show two additional

²⁷It is also possible that large banks have some difficulty in fully adjusting their balance sheets in just a single day. The inability of banks to adjust their balance sheet despite their natural role in intermediation and arbitrage activities in response to large increases in funding spreads speak to papers on slow-moving capital and asset price dynamics (Duffie, 2010; Greenwood et al., 2018).

balance sheet items that exhibit some frequent variations — deposit and outright treasury holdings. Both of these are relatively stable on quarter-ends.²⁸

The impact of increases in the TGA balance on U.S. GSIBs’ intermediation activities follows similar patterns compared to their quarter-end response. U.S. GSIBs draw down reserves to fund reverse repo and FX swap lending as the TGA balance sheet increases. The regression coefficient on ΔTGA_t for reserves (column 1) indicates that each dollar of TGA balance increases is funded with around 18 cents of reserve drainage for our sample of U.S. GSIBs, controlling for other factors (the unconditional univariate coefficient is around 0.30). Both repo and reverse repo positions are reduced, but the decline in repo borrowing is larger, leading to a small increase in net reverse repo lending (columns 2-4). Similar to the quarter-end results, the coefficients suggest that U.S. GSIBs prefer to maintain lending at the higher intermediation spreads but reduce their financing costs by shrinking their repo borrowings. Instead of repo market financing, the banks rely on reserves drainage to make up for the reduced repo borrowing. Additionally, the banks also lend out more dollars through FX swaps as indicated by column 5. Concurrently, U.S. GSIBs experiences small deposit outflows (column 6), which likely reflect a transfer from depositors’ account to the TGA account to finance the increase in the TGA balance. Finally, U.S. GSIBs increase their outright Treasury holdings (column 7), partly in response to the rising net Treasury issuance associated with the TGA increase.

Comparing the responses across balance sheet items due to TGA fluctuations reveals two additional insights. First, the amount of reserve drainage roughly matches the cash used to provide short-term funding and outflows due to deposit and Treasury holdings. This finding confirms that we are capturing the most scalable components of the balance sheet. Second, the relative coefficients of dollar deposits and reserves reveal the active

²⁸The quarter-start variable, $Qstart_t$, exhibits changes that are largely the reverse of $Qend_t$, with the exception that deposit flow is positive and significant while repo borrowing shows little sign of reversing the quarter-end decline. This is likely related to periodic payroll-related deposit inflows occurring at the beginning of the month, which reduces the banks’ need for repo financing.

role that U.S. GSIBs play in providing short-term funding intermediation. Absent these intermediation activities, the reduction in reserves should match the outflow of deposits that goes towards an increase in the TGA balance.

Finally, the change in SOMA Treasury holdings is also significantly associated with intermediation activities. An increase in $\Delta SOMA_t$ generally works in the opposite way as an increase in the TGA balance, as an increase in $\Delta SOMA_t$ increases overall bank reserves and eases overall funding condition. U.S. banks provide less dollar intermediation in response to an increase in $\Delta SOMA_t$ through an increase in reserve holdings and a reduction in net reverse repo lending and FX swap lending.²⁹

The intra-firm flows for TGA- and SOMA-related cash liquidity shortage again qualitatively mirror the findings from the quarter-end study. Table 3 shows that broker-dealers reduce their external repo borrowing from unrelated parties on quarter-ends, when the TGA balance increases and SOMA holdings decline. To make up for the loss of funding on these days, the broker-dealers increase their net internal repo borrowing non-broker-dealer affiliates (depository institutions) within the BHC. Non-broker-dealers finance the intra-office transfer by draining their excess reserve balances.

4.4 Reserve Distribution among U.S. GSIBs, Foreign and Other U.S. Banks

The previous subsection highlights the crucial role of reserves in the U.S. GSIBs' dollar intermediation strategy. These institutions substitute excess reserves at the Fed for repo or FX lending as intermediation spreads increase. However, from an aggregate financial-system-perspective, the overall level of bank reserves is determined by the size of Federal Reserve's assets, holding other non-reserve liability items of the Federal Reserve constant.³⁰ Any decrease in the reserve holdings of some institutions has to end up in other

²⁹We note that in our sample, the Fed reduced its balance sheet only on Treasury auction dates by not fully rolling over the maturing debt in its existing holdings. The coefficients on $\Delta SOMA_t$ are rather imprecisely estimated because $\Delta SOMA_t$ are equal to zero for most of the sample dates.

³⁰Appendix Figure A6 shows the evolution of the Federal Reserve balance sheet post-GFC.

institutions' balance sheets. The distribution of reserves across institutions in the system may have implications for the level of aggregate financial intermediation activities. Moreover, data on reserve holdings can also shed light on whether other institutions conduct reserve-dependent intermediation strategies similar to those followed by the six U.S. GSIBs.

To conduct our tests, we use information collected by the Federal Reserve on daily reserve balances at financial institutions. Besides the six U.S. GSIBs, we create two additional groups composed of foreign financial institutions and other domestic institutions.³¹ As shown in Figure 11, reserve balances for the U.S. GSIBs and the foreign banks have trended down in the last couple of years, consistent with the normalization process of the Federal Reserve's balance sheet. This trend is less pronounced for the domestic banks, which have held relatively stable balances of reserves in recent years.

We also collect information on balances at the overnight reverse repurchase agreement facility (ON RRP). This facility is used by the Federal Reserve to control the federal funds rate by selling securities to eligible non-bank counterparties with an agreement to repurchase them the next day. Thus, an increase in ON RRP transactions drains reserves from the system, which should mirror the change in reserves at the three groups of banks previously described.

In Table 4, we estimate the same specifications as in Table 2, using the change in the reserve balances of financial institutions and the change in the ON RRP as the dependent variables.³² Focusing on the coefficients on the quarter-end ($Qend_t$) and quarter start ($Qstart_t$) dummies, we find that at quarter ends, both reserves at the U.S. GSIBs and foreign banks decrease substantially, with most of those balances moving to the domestic

³¹We include Bank of New York Mellon and State Street in the group of other domestic institutions. We also note that only foreign BHCs with U.S. branches and subsidiaries can hold reserves at the Federal Reserve, and these branches and subsidiaries hold reserves for their ultimate parent BHCs.

³²The results in column 1 are nearly identical to those presented in column 1 of Table 2. As this data on daily reserve holdings is collected separately from the FR2052a, the sample size differs slightly. Nonetheless, these data validates the result on the reserve holdings of the six U.S. GSIBs from the FR2052a report.

banks or the ON RRP. As noted previously, the drop in reserves balances at the U.S. GSIBs is driven by their reserve-draining intermediation strategy, where they substitute reserves for repo and FX lending.

In the case of the foreign banks, the drop in reserves on quarter-ends is larger, which is likely driven by at least two factors. First, foreign banks could also be conducting some reserve-draining intermediation as is the case for the U.S. GSIBs. Second, as noted previously, regulations that govern the disclosure of banks' leverage ratios incentivize foreign banks to shrink the size of their balance sheets at quarter ends. In particular, [Anderson, Du and Schlusche \(2019\)](#) show that foreign banks are actively engaged in the IOR arbitrage and significantly contract their IOR arbitrage positions on quarter-ends. U.S. banks do not engage in much IOR arbitrage.³³ The scale-back in the IOER arbitrage accounts for the additional quarter-end effects in the reserve holdings for foreign banks.

The shift of reserves from large U.S. GSIBs and foreign banks to smaller U.S. banks and the ON RRP facility at quarter ends reduces the level of aggregate financial intermediation. As the smaller banks participate less in lending via the wholesale funding markets and the ON RRP absorbs cash from the banking system, the effective amount of dollar cash lent out by banks declines. This reserve redistribution can have implications on the aggregate pricing of funding, as evidenced by the significant effects on funding spreads observed on quarter ends.

The two additional types of events that we noted in the previous sections are the changes in TGA balances and in the Federal Reserve's SOMA portfolio. In Table 4, we observe that the coefficient on the foreign and smaller domestic banks is each about negative 0.4 and the coefficient on U.S. GSIBs is around negative 0.2.³⁴ As discussed in Section

³³The IOR arbitrage involves borrowing in the overnight private money markets, such as the federal funds or eurodollar markets, and then depositing the proceeds at the Federal Reserve, earning the IOR rate. U.S. banks face additional regulatory costs, such as the insurance premium charged by the Federal Deposit Insurance Corporations, which disincentives this activity.

³⁴We note that the sum of the coefficients on TGA across the three types of banks adds up to around negative one, which suggests that the TGA variations are generally uncorrelated with changes in other non-reserve liability items of the Federal Reserve.

4.3.2, a larger reduction in reserves than the deposit outflows for U.S. GSIBs is a signal for reserve-draining intermediation activities. For foreign banks and smaller domestic banks, we do not have direct daily data on their dollar deposits. However, given that foreign banks in the U.S. do not have a significant deposit base, and that most of the smaller domestic banks are primarily funded with deposits, the very negative coefficients on TGA for foreign banks and smaller domestic banks likely reflect different drivers: foreign banks might also engage in reserve-draining intermediation, whereas other smaller domestic banks passively accommodate deposit outflows to pay for TGA increases.³⁵ Lastly, in response to a reduction in the SOMA portfolio holdings ($\Delta SOMA_t < 0$), we find that only U.S. GSIBs and foreign banks reduce their reserve balances, with the effect larger and more statistically significant for foreign banks. Smaller domestic banks increase their reserve holdings.³⁶

In sum, beyond the six U.S. GSIBs, it appears that foreign banks also conduct reserve-based intermediation activities, as shown by similar patterns in the changes of reserve balances. In contrast, smaller domestic banks that are less involved in these markets are at the receiving end of those reserves. A similar pattern is observed for the ON RRP facility. The redistribution of reserves has implications for the overall level of financial intermediation and therefore various dollar funding spreads. We will return to these distributional issues in our analysis of the repo rate spike in September 2019 in Section 5.

4.5 Robustness Checks

We now discuss three main robustness checks for our core results on U.S. GSIBs' balance sheet adjustments. First, we construct an alternative measure of the dollar lending in the

³⁵As businesses or households use their deposits to, for example, pay their taxes, banks use reserves to credit the government while debiting the deposit accounts.

³⁶We note that the take-up at the ON RRP facility has a negative coefficient on $\Delta SOMA_t$. However, this negative coefficient largely captures some period-end dynamics not fully absorbed by the quarter-end dummies. Once we control for the month-end and month-start dummies, the coefficient $\Delta SOMA_t$ on the ON RRP becomes positive and significant, consistent with the notion that the Fed taper reduces the spare cash parked in the ON RRP facility.

FX swap market. Second, we decompose the TGA fluctuations into two components, one related to the net Treasury issuance, and the other related to taxes and expenditures. Third, we differentiate outright and repo-financed Treasury holdings.

4.5.1 Alternative Measure of FX Swap Lending

As a robustness check, we use an alternative proxy for FX swap lending (*Total FX Swap Lend*), which takes the difference between foreign currency assets and foreign currency liabilities:

$$Total\ FX\ Swap\ Lend = FC\ Total\ Assets - FC\ Total\ Liabilities. \quad (2)$$

Assuming that U.S. GSIBs fully hedge the currency risk of its assets and liabilities, then the gap between foreign currency assets and liabilities on balance sheets must be matched by dollar lending in the FX swap market off-balance sheets. Similar measures have been used in the literature to measure non-US banks' dollar borrowing in the FX swap market (for example, [McGuire and Von Peter \(2009\)](#) and [Fender and McGuire \(2010\)](#)). Compared to *Short-Term FX Swap Lend*, *Total FX Swap Lend* also capture long-term dollar lending in the FX swap market. Table [A3](#) shows that the regression results based on the alternative FX lend measure are very similar to those based on our benchmark short-term FX-lending measure.

To assess whether U.S. GSIBs indeed hedge the foreign currency funding gap, we note that U.S. bank supervisors do not systematically collect data on the FX derivatives exposure by currency for banks' banking book. However, the FX swap exposure on banks' trading book can be inferred from the FR Y14Q *Capital Assessment and Stress Testing* form. In [Appendix D](#), we show that the foreign currency funding gap is directionally in line with the estimated FX swap exposure for long dollar positions in banks' trading books.

4.5.2 Decomposition of TGA fluctuations

In this subsection, we decompose daily fluctuations in the TGA balance, ΔTGA_t , into two components. The first component summarizes daily changes in the net issuance of Treasury securities, denoted by ΔTSY_t^{Issue} . The second component reflects daily changes in the TGA account unrelated to the net Treasury issuance, denoted by ΔTGA_t^{Other} . Therefore, we have that

$$\Delta TGA_t = \Delta TSY_t^{Issue} + \Delta TGA_t^{Other}.$$

Since the six banks in our sample have broker-dealer subsidiaries that are designated primary dealers for Treasury securities, we might expect ΔTGA_t^{Issue} and ΔTGA_t^{Other} to have different impacts on their dollar intermediation activities.

Table A4 shows regression results for intermediation spreads. We can see that TGA increases unrelated to Treasury issuance, ΔTGA_t^{Other} , raise the repo and FX swap intermediation spreads, with larger and more significant impact on the FX swap spreads. An increase in the overall Treasury net issuance, ΔTSY_t^{Issue} , significantly increases repo intermediation spreads. The effect of ΔTSY_t^{Issue} on the FX swap spread is not statistically significant.

Table A5 shows the analogous quantity regressions for intermediation activities. In response to an increase in ΔTGA_t^{Other} , U.S. GSIBs contract both repo and reverse repo positions by a similar magnitude, leaving the net reverse repo position roughly unchanged (columns 2-4). However, U.S. GSIBs increase their dollar liquidity provision in the FX swap market significantly (column 5). Similar to the results in Table 2, this increase in the FX swap lending is mainly financed via reserve-draining (column 1). Meanwhile, U.S. GSIBs experience deposit outflows (column 6) in these episodes, which likely reflect a transfer from depositors' accounts to the TGA account to finance the increase in the

TGA balance. However, the magnitude of the deposit outflow is significantly smaller than the reduction in the reserve balance, suggesting that reserves fall beyond a simple passive cash transfer between depositors and the TGA. Finally, U.S. GSIBs increase their unencumbered Treasury holdings (column 7). We find a few different results when assessing the relationship between the net issuance of Treasuries, ΔTSY_t^{Issue} , and U.S. GSIBs' intermediation activities. In contrast to ΔTGA_t^{Other} , an increase in ΔTSY_t^{Issue} significantly increases U.S. bank reverse repo lending, leaves the repo position largely unchanged, and thus results in a significant increase in the net reverse repo lending (columns 2-4). The Treasury net issuance has little effect on FX lending (column 5).

Taking stock of these pricing and quantity results in Tables A4 and A5, we can determine that an increase in both components of the TGA balance tighten funding conditions, with the TGA_t^{Other} affecting the FX swap market and TSY_t^{Issue} affecting the repo market more significantly. In response, U.S. GSIBs moderately increase their dollar liquidity provision. In particular, reserve-draining intermediation is used to finance an increase in TGA_t^{Other} .

4.5.3 Outright Treasury holdings vs. repo-financed Treasury holdings

As noted previously, the six U.S. GSIBs in our sample have broker-dealer subsidiaries that are designated primary dealers for Treasury securities. Primary dealers are required to participate in all Treasury auctions and are the direct counterparties of the Fed to purchase Treasury securities during the Fed balance sheet taper. In this subsection, we provide a closer look at Treasury holdings' of the U.S. GSIBs.

In our previous analysis, we examined the response of outright holdings of Treasury securities in the dollar funding shortage. In addition, U.S. GSIBs can also change their Treasury holdings financed via repos. We measure the amount of repo-financed Treasury holdings as the amount of "non-rehypothecated" repo positions backed by U.S. Treasury

collateral.³⁷ More details on the stylized facts and drivers of collateral-reuse based on FR 2052a data are discussed in [Infante et al. \(2020\)](#) and [Infante and Saravay \(2020\)](#).

Table [A6](#) shows the regression results for repo-financed Treasury holdings. We find that U.S. GSIBs' repo-financed Treasury holdings increase with the net issuance of Treasury securities and decrease with Fed SOMA portfolio holdings. Together with the outright Treasury holdings, for each \$100 billion increase in the Treasury net issuance, U.S. GSIBs increase their total Treasury holdings by \$7 billion, half of which is through outright holdings and the other half is through repo-financing. The effect of Fed's balance sheet taper on U.S. GSIBs' Treasury holdings is significantly larger. For each \$100 billion taper of the SOMA portfolio, U.S. GSIBs increase Treasury holdings by \$30 billion, \$12 billion of which is through outright holdings and \$18 billion of which is through repo-financing. The amount of U.S. GSIBs' own Treasury financing needs could help explain the large price effects of $\Delta SOMA$ on various repo spreads in Tables [1](#) and [A4](#).

5 Repo Spike in September, 2019 and U.S. GSIBs' Response to Fed Liquidity Support

Using insights from the previous section, we examine the funding crunch that took place in mid-September 2019 and the immediate aftermath, when the Federal Reserve re-established its repo facility and increased its purchases of Treasury bills. These actions were first intended to improve conditions in money markets and to maintain the federal funds rate within the target range following the mid-September event, but were then maintained to provide an extraordinary amount of liquidity support to the economy during the COVID-19 pandemic.

³⁷In contrast, if the Treasury-backed repo position is "rehypothecated", the bank re-pledges the Treasury collateral and no longer possesses the Treasury securities.

5.1 September 2019 repo rate spike

The September 2019 funding crunch occurred when the TGA balance increased over \$100 billion, as corporate tax payment coincided with large Treasury issuance settlements. This funding crunch happened against the backdrop of declining aggregate reserve levels as the Fed normalized the size of its balance sheet by, as noted previously, reducing the size of its SOMA holdings. Reserves across all banks reached their multi-year lows. On Monday, September 16, the TGA balance increased by \$83 billion, and the benchmark SOFR-IOR spread ended the day 23 basis point higher — a four-standard deviation increase. On September 17, the overnight repo rate spiked to a high of 10% and the volume-weighted SOFR benchmark settled at 5.25% — 3.15% above the interest paid on reserves. The repo market stress also strongly spilled over to the FX swap market, which priced the implied dollar funding rates at above 5% intraday. Figure 12 shows the intraday movements in the overnight repo rate and the implied dollar funding rates from the FX swap market. A detailed discussion of intraday movements in these rates is provided in Appendix Section B.

The price of secured dollar funding reacted strongly to the TGA balance increase compared to previous episodes. Figure 13 shows that the SOFR-IOR spread typically increases on days when there are large positive movements in the TGA balance and declines on days with large TGA balance reductions. The changes in SOFR-IOR on both September 16 and 17 were outsized relative to the TGA increase.³⁸

Using information for the GSIBs in our sample, we find that the one-day response of these institutions to the large TGA increase on September 16 was generally consistent

³⁸Furthermore, the multivariate comparison of the predicted versus actual spread changes based on coefficients estimated in Table 1 shows that the changes in SOFR-IOR were 20 basis points higher than the estimated fit on September 16 and 282 basis points higher than the fit on September 17. This outsized price reaction raises questions on the activities of intermediaries.

with their typical reaction to TGA shocks.³⁹ Panel A of Figure 14 shows the one-day changes in select balance sheet items on September 16 compared to the predicted range of response based on coefficient estimates in Table 2. The actual response is within the 95% confidence interval of the predicted response for most balance sheet items. Reserves declined around \$22 billion, which is slightly lower than the predicted decline. Dollar lending against foreign cash collateral, FX Lend, increased slightly above the top of the predicted range while net repo lending against security collateral remained roughly constant. The difference in the willingness of U.S. GSIBs to lend against foreign cash collateral and security collateral possibly speaks to the abundance of Treasury collateral due to new issuance.

While we cannot expand our analysis to non-U.S. GSIBs due to the lack of FR2052a reporting for these institutions, our reserve-based intermediation channel nonetheless helps us shed light on the likely culprit of the September 2019 funding crunch. Panel B of Figure 14 presents the estimated versus actual changes in reserve holdings at the Federal Reserve for the same three groups of banks described in Section 4.4: our sample of U.S. GSIBs, foreign banks, and other smaller domestic banks. The predicted changes are based on Table 4. The results show that in contrast to U.S. GSIBs, which drained reserves slightly more than predicted, foreign banks significantly under-reacted to the TGA increase on the 16th. Foreign banks reduced their total reserve balance by \$14 billion on the 16th, compared to a predicted change of \$40 billion. Other smaller domestic banks' reserve behavior on the day is quite in line with our prediction. Furthermore, on September 17, 2019, foreign banks increased their reserves by \$58 billion, an amount that is roughly on par with the total draw on the Fed repo facility reinstated for the first time since the GFC on that same day. In contrast, U.S. GSIBs drained their reserves further by \$14 billion.

³⁹We focus on the one-day change from Friday, September 13 to Monday, September 16, despite the fact that the largest price action occurred on September 17. This is because the Fed intervened in the morning of September 17 and our balance sheet numbers as of the end of day on September 17 already reflect the Fed's intervention.

This provides an additional signal that foreign banks might have hit the limit of drainable reserves and contracted their dollar intermediation on the 16th.

In addition to the likely breakdown of reserve-based intermediation to absorb a large TGA shock due to the lack of drainable reserves, structural shifts in the broker-dealers' own Treasury financing needs might have also contributed to the dollar funding shortage. In particular, against the backdrop of the Federal Reserve's balance sheet normalization process and gradual reserve declines in banking entities, the broker-dealer arms of the banks transitioned from net lending to net borrowing in the repo market. Their extra financing needs were used to support accumulation of Treasury holdings in an environment with a flat to negative yield curve that reduced end-buyers' demand for Treasury securities. Moreover, the dealers' repo financing was increasingly reliant on posting lower-quality collateral and shortening the maturity of borrowing, characteristics that are indicative of a funding crunch. We discuss these developments in more details in [Appendix C](#).

5.2 The Fed Repo Facility and post-September 2019 events

The acute funding shortage in September 2019 prompted the Federal Reserve to reinstate its repo lending facility that had been inactive since the GFC. As the repo rate spiked to a high of 10% on September 17, 2019, the Fed established a repo facility with up to \$75 billion in initial drawing capacity. After this event, the Fed carried out daily overnight and term repo auctions through year-end 2019 and into 2020. The onset of the COVID-19 market turmoil in March 2020 led to another funding crunch with the GCF-IOR spread increasing to a high of 76 basis points and FX overnight funding spreads increasing by as much as 6%. [Appendix Figure A7](#) shows the evolution of funding spreads since September 2019.

Primary dealers are the only private sector counterparties that are allowed to borrow at the Fed repo facility.⁴⁰ The red line in Figure 15 plots the U.S. GSIBs’ take-up at the Fed repo facility (through their primary dealer subsidiaries). The repo facility take-up is high when the funding condition is tight. We see solid take-up reaching around \$80 billion in the immediate aftermath of the September 2019 repo spike. The take-up reached a pre-COVID peak at \$120 billion on December 31, 2019, and later peaked at \$170 billion during the COVID-related market turmoil in March 2020. Furthermore, the Fed repo facility possibly reduced the need for broker-dealers to draw on the BHC’s internal liquidity from affiliated depository entities and supported a substitution away from reserve-based intermediation to matched-book intermediation. The blue line in Figure 15 plots the broker-dealers’ net internal borrowing from depository institutions. Increases in the usage of the Fed repo facility tend to match declines in repo borrowing from internal sources within the BHC.

The repo facility was effective in enabling banks to on-lend official liquidity support through matched-book intermediation. Table 5 shows regression results of daily changes in the U.S. GSIBs’ dollar intermediation activities on changes in Fed repo take-up. Each dollar increase in the bank’s Fed repo facility use is correlated with a net increase in repo lending of around 75 cents and FX-swap-based dollar lending of around 25 cents. Consistent with our baseline result, the net increase in repo lending is predominantly driven by the bank’s reduction of borrowing from cash lenders and a somewhat smaller increase in reverse repo lending to other counterparties.⁴¹

Lastly, recent events have heightened financial institutions’ cash demand uncertainties because of the rapid increase in the TGA balance, which reached over a \$1.8 trillion dollars

⁴⁰On March 31, 2020, the Fed established an additional repo facility for foreign and international monetary authorities.

⁴¹Besides the repo facility, in response to the COVID-19 induced market turmoil in March 2020, the Federal Reserve launched a host of other liquidity facilities to restore liquidity in the short-term funding markets. Most notably, the central bank dollar swap line reached its peak usage around \$440 trillion, mainly drawn by foreign banks.

in July 2020. The COVID-19 fiscal measures led to a surge in cash flowing through the TGA as a result of asynchronous debt issuance and fiscal payouts. We find that despite the ample Fed liquidity support, unprecedented TGA balance changes continue to impact funding spreads and large bank’s intermediation activities. We present results for our baseline price and balance sheet regressions in the post-September 2019 sample period in Appendix Tables [A1](#) and [A2](#). In particular, we see that fluctuations in the TGA balance remain significantly correlated with the repo spreads and dollar intermediation activities.

6 Discussion

In previous sections, we show that reserve-draining intermediation has become the dominant intermediation strategy for U.S. GSIBs in response to dollar funding shortages. However, the modest increase in dollar liquidity provision by U.S. GSIBs is clearly not sufficient to smooth out large and frequent spikes in dollar funding rates. Recurrent and acute dollar shortages challenge the effectiveness of U.S. monetary policy implementation and pose considerable financial stability risk. In this section, we discuss why global banks favor reserve-draining intermediation and the constraints in scaling up this type of intermediation.

6.1 Why reserve-draining intermediation?

Against the backdrop of fundamental shifts in the monetary policy regime and regulatory environment, reserve-draining intermediation became a new type of intermediation activity conducted by global banks post-GFC.

First, the GFC triggered a rapid and fundamental change to the conduct of monetary policy. Large scales asset purchases by the Fed financed by reserves created an ample reserve environment for global banks, which is a pre-condition for reserve-draining intermediation. In the pre-GFC period, the Federal Reserve operated in a monetary policy

framework with scarce reserves ([Kroeger, McGowan and Sarkar \(2018\)](#)), with banks relying on the interbank market to satisfy their daily reserve requirements ([Kim, Martin and Nosal, 2018](#)) and tap into the Fed overdraft facility to manage intraday liquidity needs. The amount of drainable excess reserves in the financial system was zero, and reserve-draining intermediation was not feasible.

Second, under the post-GFC regulatory environment, leverage-constrained global banks have preferred reserve-draining intermediation over matched-book intermediation in part due to the stronger capital regulations that increase the cost of balance sheet expansions. In particular, the LR requirement under Basel III requires banks to maintain 3% capital against all assets, regardless of their risk characteristics. The U.S. implementation of the Basel III LR took the form of the enhanced supplementary leverage ratio (eSLR), which set the LR requirement for U.S. GSIBs at 5-6%. In addition, large global banks also face a GSIB surcharge applied on top of the other risk-based capital requirements. The GSIB surcharge calculation depends on several factors, but the size of the balance sheet is an important component.

The preference for reserve-draining intermediation could be potentially traced to the binding nature of the LR and the GSIB surcharge requirements.⁴² In response to a funding demand shock, reserve-draining intermediation does not change the size of a bank's balance sheet, whereas matched-book intermediation expands the balance sheet size and make the LR and GSIB surcharge requirement more binding. However, it is worth noting that reserve-draining intermediation requires banks to devote more balance sheet space to holding more reserves in normal times in lieu of engaging in more profitable business activities. However, the ultimate liquidity and safety of reserves and the attractiveness of the IOR relative to other overnight money market rates under the ample reserve environment incentivize banks to hold reserves in normal times. The exemption of reserves

⁴²Compared to the risk-weighted capital requirement, the eSLR under the stress test scenarios have become the more binding regulatory constraint ([Duffie \(2017\)](#)).

and Treasury securities from the eSLR calculation in April 2020 further reduces the cost of reserve-draining intermediation, as it reduces the ex-ante balance sheet cost of holding reserves.

6.2 Constraints facing reserve-draining intermediation

In an ample reserve environment, banks are likely to have a large amount of excess reserves on their balance sheets, beyond the traditionally required reserve ratio requirement against deposits. However, not all these excess reserves are drainable. Banks face new regulatory constraints in terms of intraday liquidity and the need to maintain liquid assets across entities and jurisdictions, as part of the post-GFC resolution framework. Furthermore, banks' own business models and internal risk management practices may also affect their own preference for holding reserves versus other high-quality liquid assets such as Treasury securities. These factors affect the degree of reserve-draining that banks can conduct conditional on the level of overall reserves in the system.

In particular, liquidity requirements associated with the new resolution framework have important implications for reserve-draining intermediation. As part of section 165(d) of the Dodd-Frank Act, large banks are now required to submit annual plans for resolution proceedings under a hypothetical bankruptcy. These plans are assessed on qualitative and quantitative bases. The latter set of rules has led to the creation of Resolution Liquidity Adequacy Positioning (RLAP). Under RLAP, banks are subject to the expectation that they have enough liquidity in material entities to meet potential stress-induced outflows during the BHC's resolution process.

The requirement of sufficient liquidity *at the time* of resolution under RLAP effectively generates an intraday liquidity requirement. Compared to Treasury securities and overnight repo agreements, reserves have the best intraday liquidity (or the highest monetization ratio), as reserves can be used for any type of transactions. The importance of reserves in facilitating intraday payment flows is documented in detail by [Copeland, Duffie](#)

and Yang (2020). The intraday liquidity constraint facing reserve-draining intermediation was summarized by Jamie Dimon, Chairman and Chief Executive Officer of JP Morgan, during the bank’s third quarter earnings call in 2019:

We have a checking account at the Fed with a certain amount of cash in it. Last year, we had more cash than we needed for regulatory requirements. So repo rates went up, we went with the checking account which paid IOER into repo. Obviously makes sense, you make more money. But now the cash in the account, which is still huge. It’s \$120 billion in the morning, and it goes down to \$60 billion during the course of the day and back to \$120 billion at the end of the day. That cash, we believe, is required under resolution and recovery and liquidity stress testing. And therefore, we could not redeploy it into repo market, which we would’ve been happy to do.

Besides these effective intraday liquidity requirements, the resolution planning rules also impose constraints on the distribution of liquidity across entities and jurisdictions. This is because RLAP calculations not only take into account localized stresses, but also the prospect of local regulators outside the United States requiring incremental liquidity in their jurisdiction (ring-fencing). Stated more broadly, banks are now expected to be able to meet outflows at the material entity or local level, without having to rely on cross-entity or cross-jurisdiction transfers in a time of stress. As we noted in earlier sections, reserves are held in the depository institution within the BHC. The extent of reserve-draining intermediation crucially depends on the amount of these reserves that can be used to finance other parts of the BHC, such as the affiliated broker-dealers. If the RLAP requirement is binding at the material entity level, these intragroup flows may only represent a fraction of the intragroup transfers that would have been conducted without these constraints. In addition, in the case of dollar lending in the FX swap market, reserve-draining intermediation reduces banks’ liquidity buffers in their U.S. material legal entities

and increase their liquidity in foreign central banks outside the United States, which could also make the RLAP requirements more binding.

It is important to note, that RLAP requirements are based on the banks internal liquidity stress testing models (Ihrig et al. (2019)). Thus, it is difficult to identify whether the RLAP requirement indeed affects intragroup liquidity management, or if the binding constraint for the flow of liquidity is explained by banks' business models and their risk tolerance. Beyond RLAP, banks may also decide to maintain liquidity in certain legal entities or have higher preference for reserves than Treasury securities, even in the absence of regulatory constraints, to enhance their resiliency. In addition, it is also quite plausible that not all liquidity management decisions are made at the BHC level. Individual entities can have sufficient autonomy in making their own decisions.

Overall, the factors discussed above determine the minimum overall level of reserves that banks may want to maintain to satisfy both the regulatory requirements and their liquidity needs. Any level of reserves above this minimum level could potentially be used to conduct intermediation transactions. Prior to the repo rate spike in September 2019, the whole banking system still had \$1.4 trillion reserves, but the amount of truly drainable reserves was approaching zero.

7 Conclusion

In this paper, we have documented the crucial role of bank reserves in supporting the well-functioning of dollar funding markets. In particular, we find that U.S. GSIBs reduce their reserves at the Fed in order to lend in the repo and FX swap markets during periods of dollar funding shortage. The internal liquidity sharing within the BHC between broker-dealers and non-broker-dealer entities enables this reserve-based intermediation. These activities are operative as a result of the ample reserve environment set by the Federal Reserve in the post-GFC period. However, as the level of bank reserves declined

since the Fed balance sheet normalization beginning in 2017, reserve-draining intermediation activities of global banks became impaired, leading to the stress observed in money markets in September 2019.

More generally, the interaction between financial regulations and monetary policy have become more complex post-GFC. Regulatory reforms that build the resilience of the financial system increase balance sheet costs for large global banks to intermediate in the short-term funding markets, which could undermine the effectiveness of U.S. monetary policy transmission. Given the critical role of bank reserves in liquidity provision in the new regulatory environment, a large Fed balance sheet is necessary to ensure ample bank reserves, and thus a steady control over the interest rate policy, even when the short-term interest rate is above the zero-lower bound.

Lastly, as the Federal Reserve massively expands its balance sheet in response to the COVID-19 pandemic, banks are again accumulating reserves critical for the supply of liquidity, particularly in times of distress. Going forward, the lessons learned from the earlier (and so far the only post-GFC) episode of Federal Reserve balance sheet normalization before the COVID-19 pandemic can inform future monetary policy and its interaction financial regulations.

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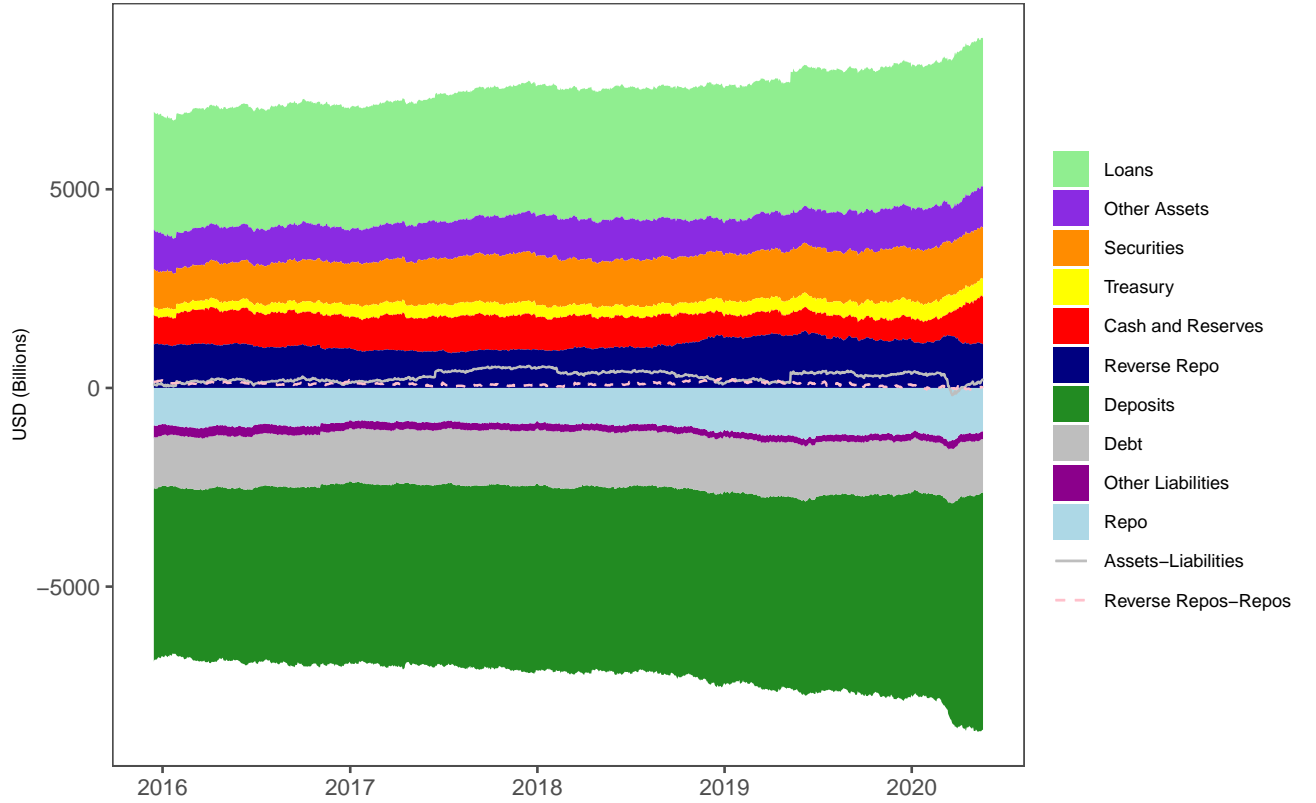
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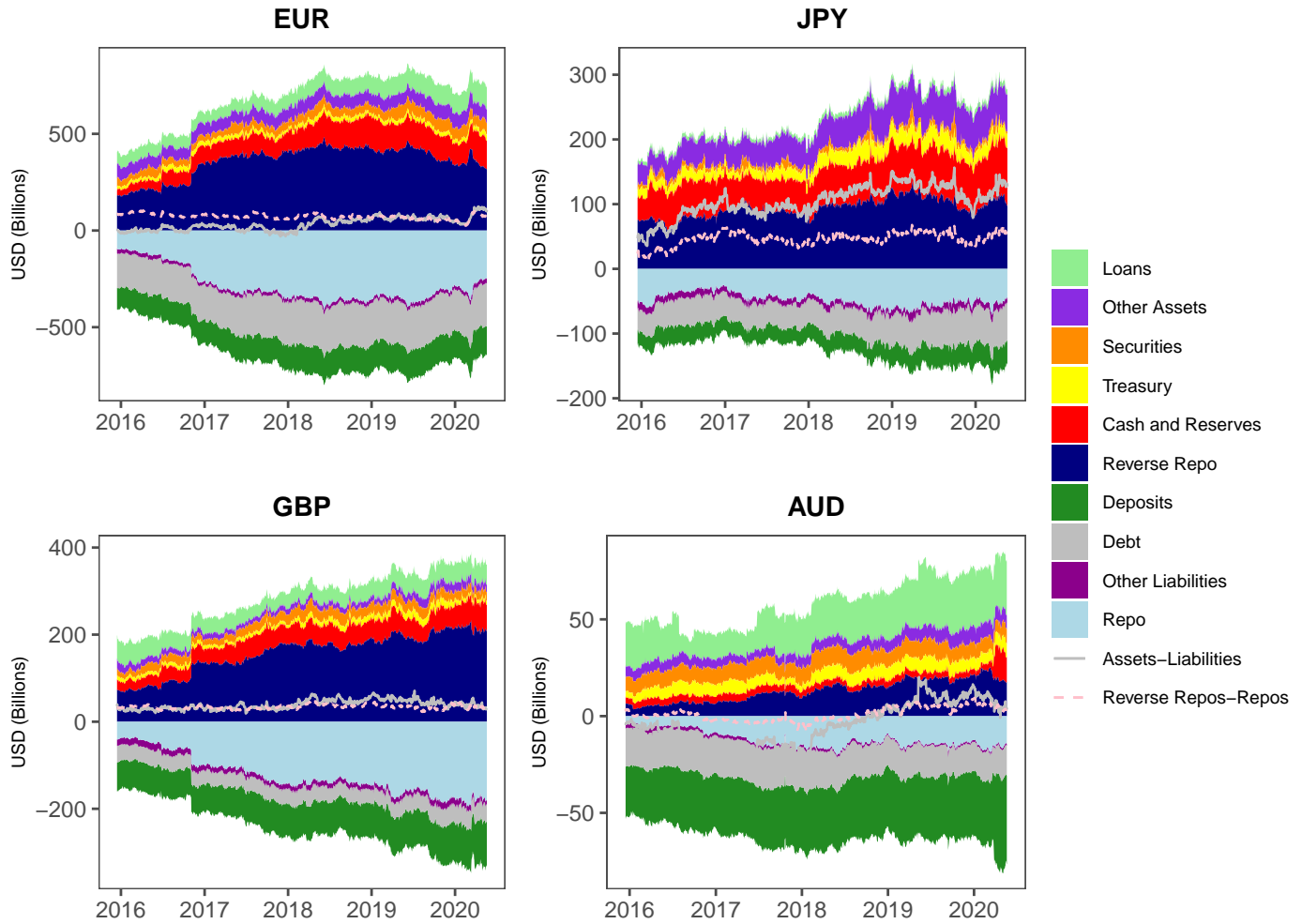
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Figure 1: U.S. GSIBs balance sheet in dollars



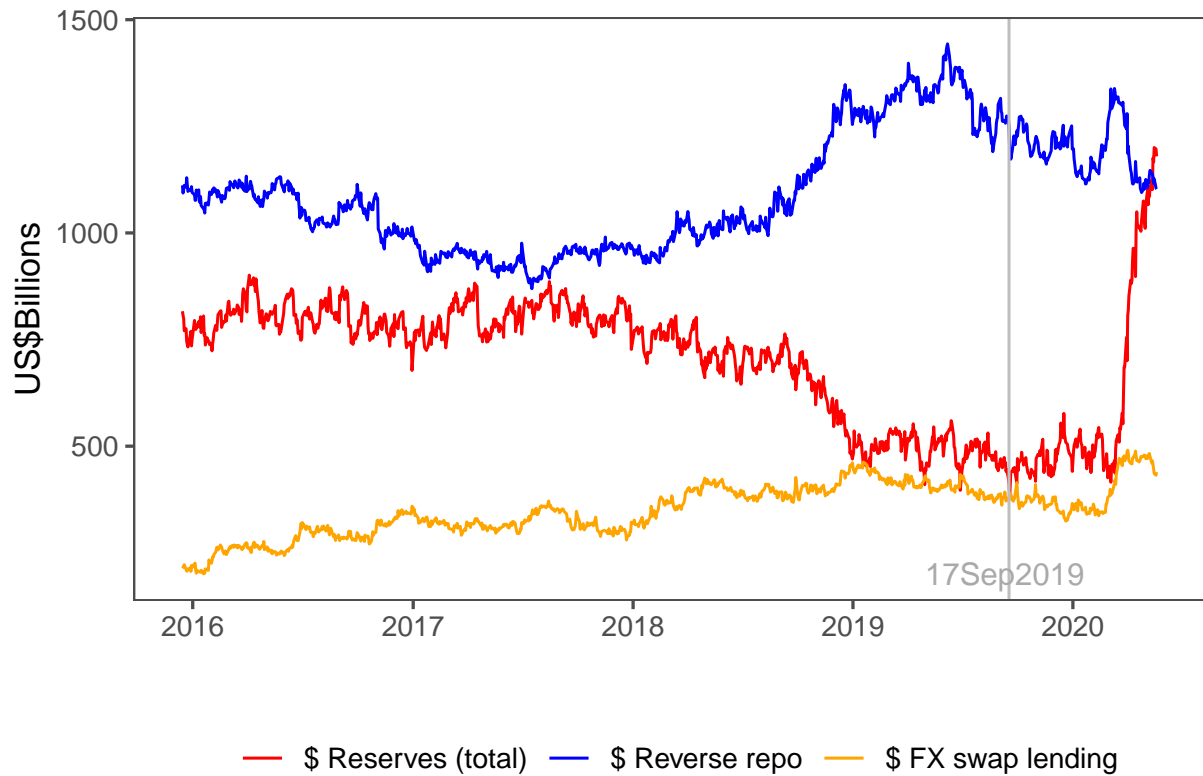
Notes: This figure presents the aggregate balance sheet for six U.S.GSIBs based on the FR 2052a data, including only items denominated in U.S. dollars. Items above zero are classified as assets and those below zero as liabilities. The solid line represents the difference between total assets and total liabilities, while the dashed line measures the net repo position of these banks. The sample period expands from December 2015 until May 2020.

Figure 2: U.S. GSIBs balance sheet in other currencies



Notes: This figure presents the aggregate balance sheet for six U.S. GSIBs for items denominated in euros (EUR), Japanese Yen (JPY), British pounds (GBP), and Australian dollars (AUD) based on the FR 2052a data. Items above zero are classified as assets and those below zero as liabilities. The solid line represents the difference between total assets and total liabilities, while the dashed line measures the net repo position of these banks. The sample period expands from December 2015 until May 2020.

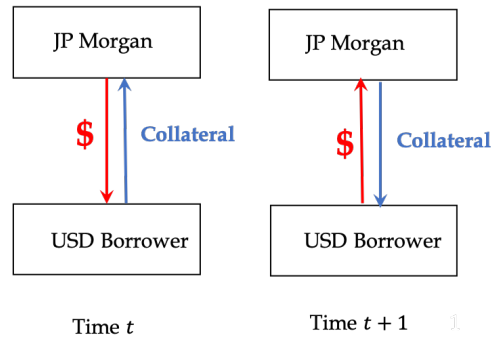
Figure 3: U.S. GSIBs' dollar liquidity provision



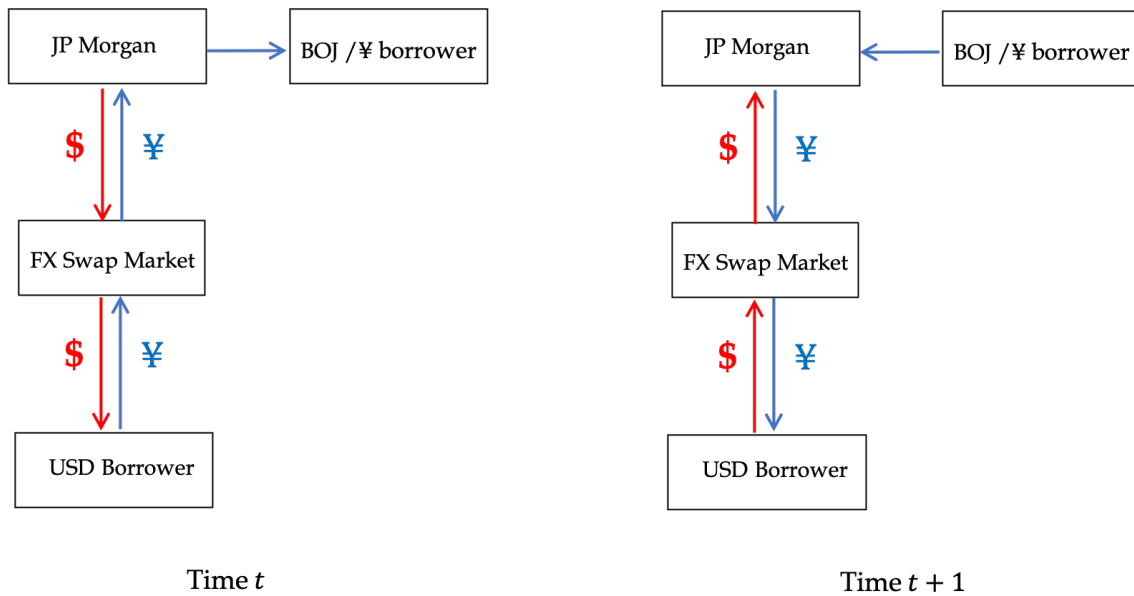
Notes: This figure shows the time series of U.S. GSIBs' total dollar reserves in red, dollar reverse repo lending in blue, and dollar FX swap lending in orange. The discussions of these short-term scalable components of bank assets are provided in Section 3. The vertical gray line shows the beginning of the Fed repo facility on September 17, 2019. The sample is measured daily from December 2015 to May 2020.

Figure 4: Cash flows for dollar lending in repo and FX swap markets

(A) Dollar lending in the repo market

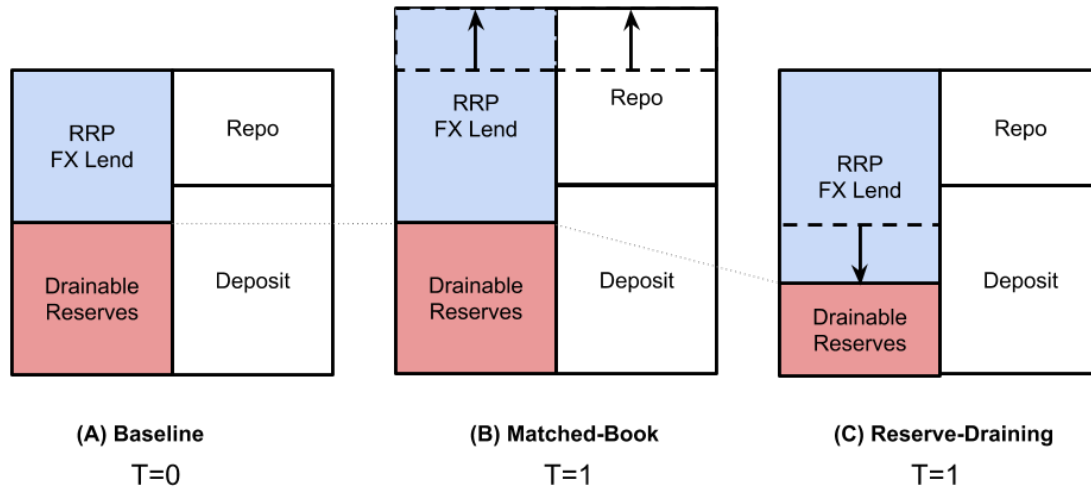


(B) Dollar lending in the FX swap market



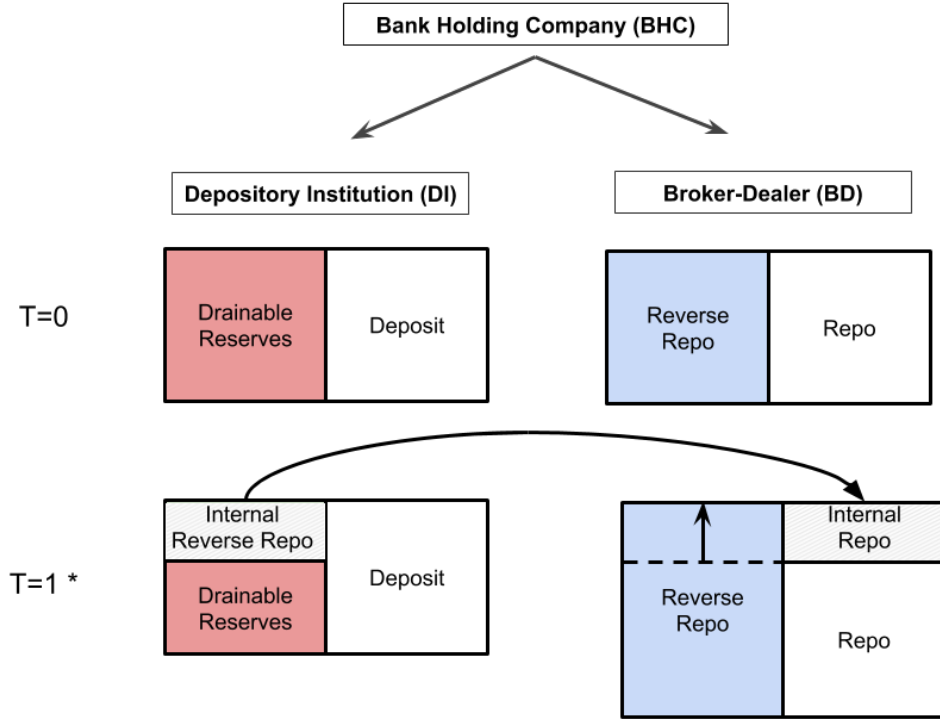
Notes: This figure shows a schematic representation of the dollar lending activities conducted by U.S. GSIBs. Panel (A) shows dollar lending in the repo market. Panel (B) shows dollar lending in the FX swap market.

Figure 5: An illustration of different types of dollar intermediation



Notes: This figure shows the aggregate short-term scalable balance sheet for dollar liquidity provision and two types of dollar funding intermediation. Panel (A) shows the baseline balance sheet. The asset items include the sum of the reverse repos and FX swap lending in dollars (shown in blue), and drainable reserve balances at the Federal Reserve beyond the reserve requirement and other regulatory demand (shown in red). The liability items include repos and deposits denominated in dollars. Panel (B) shows matched-book intermediation through which a bank increases repo borrowing by the same amount as the increase in short-term dollar lending in repo and FX swap markets. Panel (C) shows reserve-draining intermediation through which a bank reduces its drainable reserve balances to increase its short-term dollar lending, while leaving the overall size of the bank balance sheet unchanged.

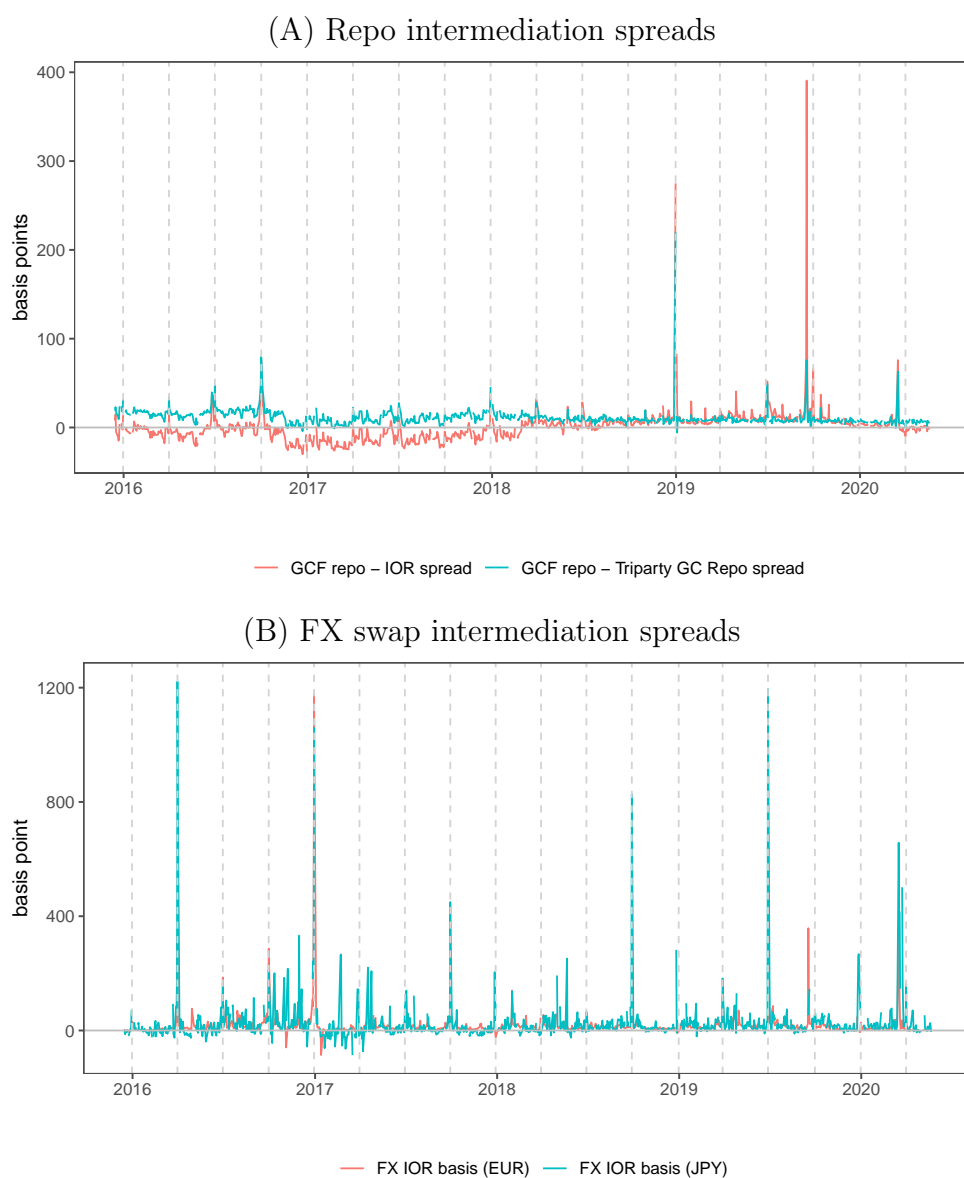
Figure 6: Intra-bank Transfer for Reserve-Draining Intermediation



* BHC and DI balance sheet size unchanged
BD balance sheet expands at $T=1$

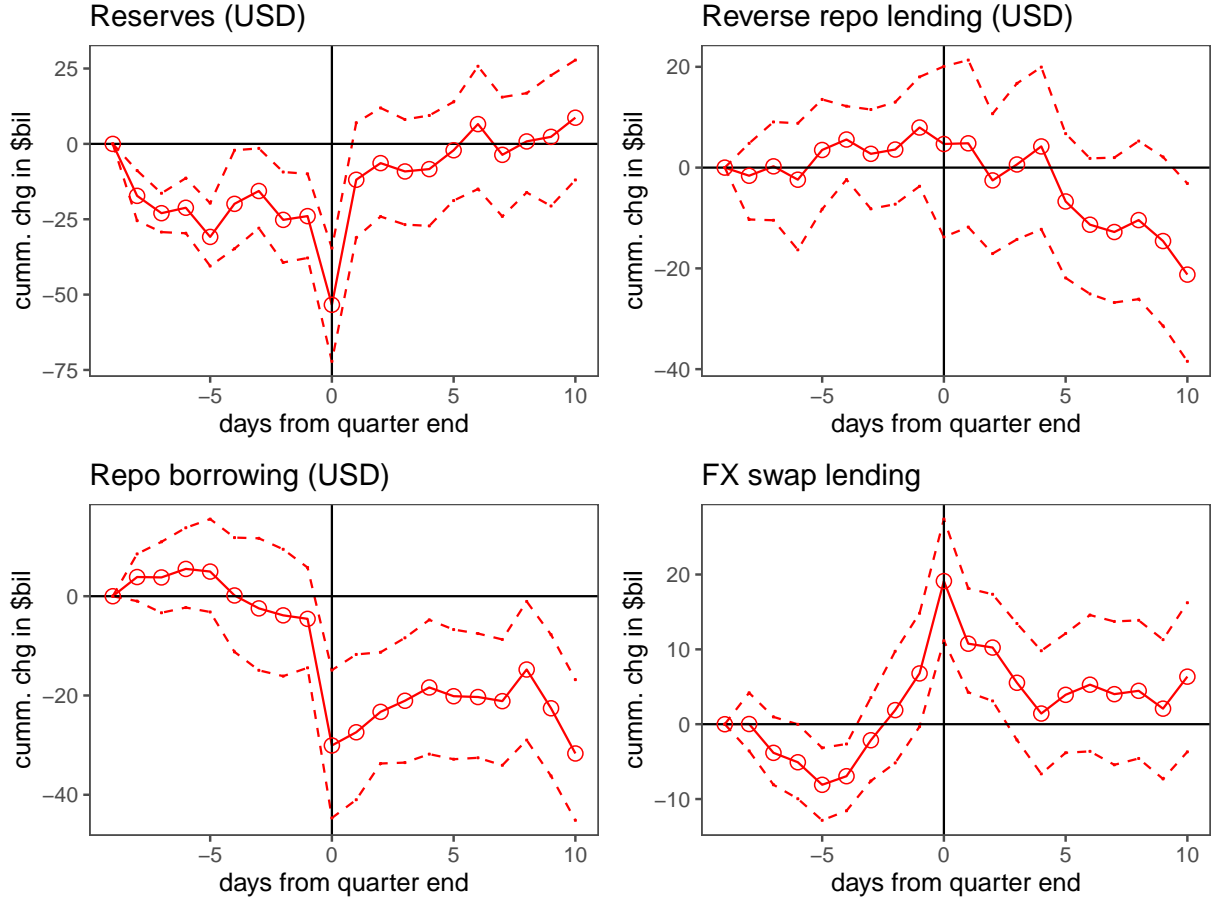
Notes: This figure illustrates the intra-office transfer between the depository institution (DI) and the broker-dealer (BD) subsidiary of the same bank-holding company (BHC) that enables reserve-draining intermediation. The top two diagrams show the baseline balance sheet for the DI and the BD at $T = 0$. The bottom two diagrams show the new balance sheets after additional reserve-draining intermediation at $T = 1$. The DI reduces its reserve balance, and transfers the proceeds to the BD through an internal reverse repo lending. The BD uses the additional funding from the internal repo position to expand its reverse repo position. Deposit and external repo positions remain unchanged. After netting out internal positions, the overall size of the BHC's balance sheet stays unchanged at $T = 1$.

Figure 7: Short-term intermediation spreads for dollar funding



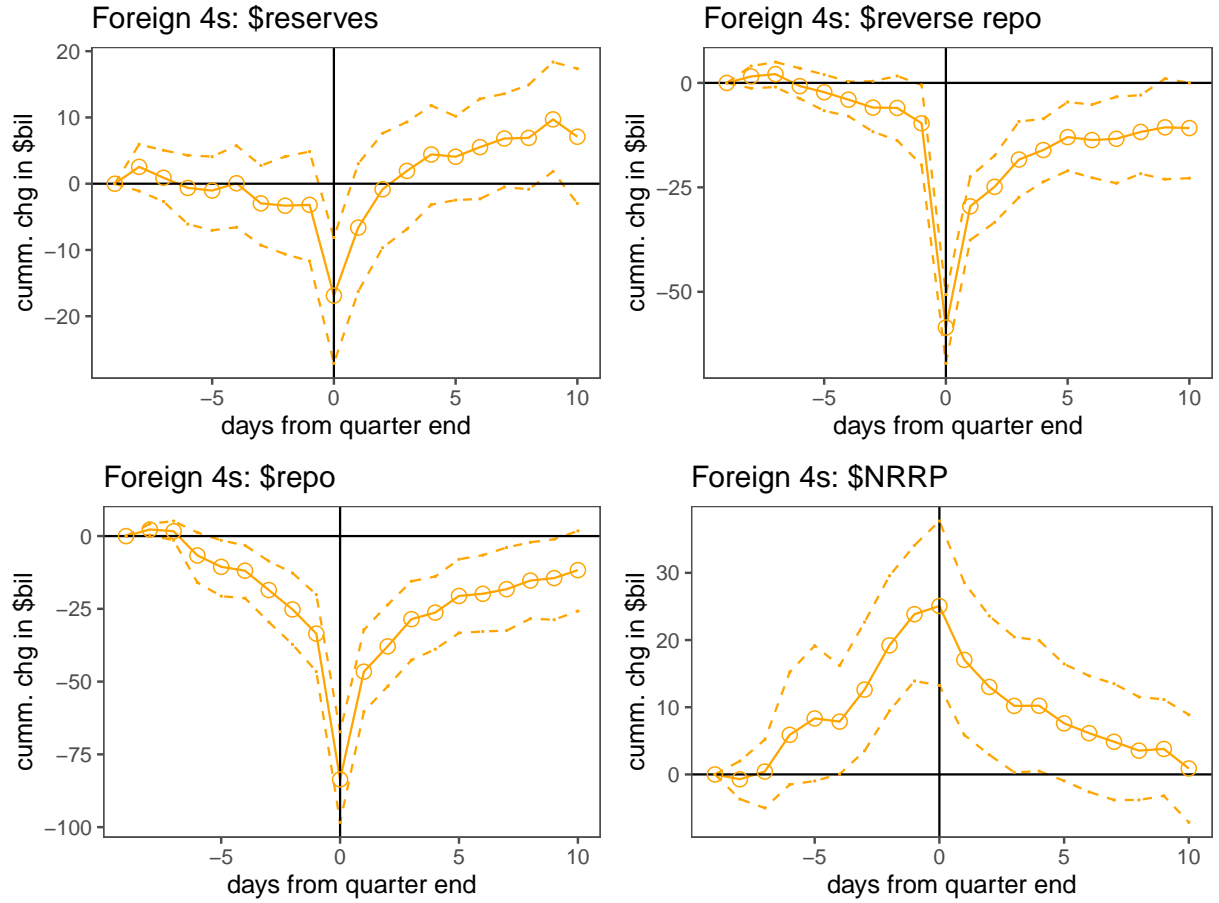
Notes: This figure shows various intermediation spreads for dollar funding intermediation. In Panel (A), we plot the difference between the GCF general collateral Treasury repo rate and interest on excess reserve (IOR) at the Federal Reserve ("GCF repo - IOR spread"), and the difference between the GCF and Triparty Treasury general collateral repo spread ("GCF Repo - Triparty GC Repo Spread"). In Panel (B), we plot the spread of the implied dollar funding rate by swapping the ECB deposit rate over the Fed IOR (FX IOR Basis (EUR)), and the spread of the implied dollar funding rate by swapping the BOJ deposit rate over the Fed IOR (FX IOR Basis (JPY)). The dashed vertical lines denote quarter-ends.

Figure 8: U.S. GSIBs' liquidity provision around quarter-ends



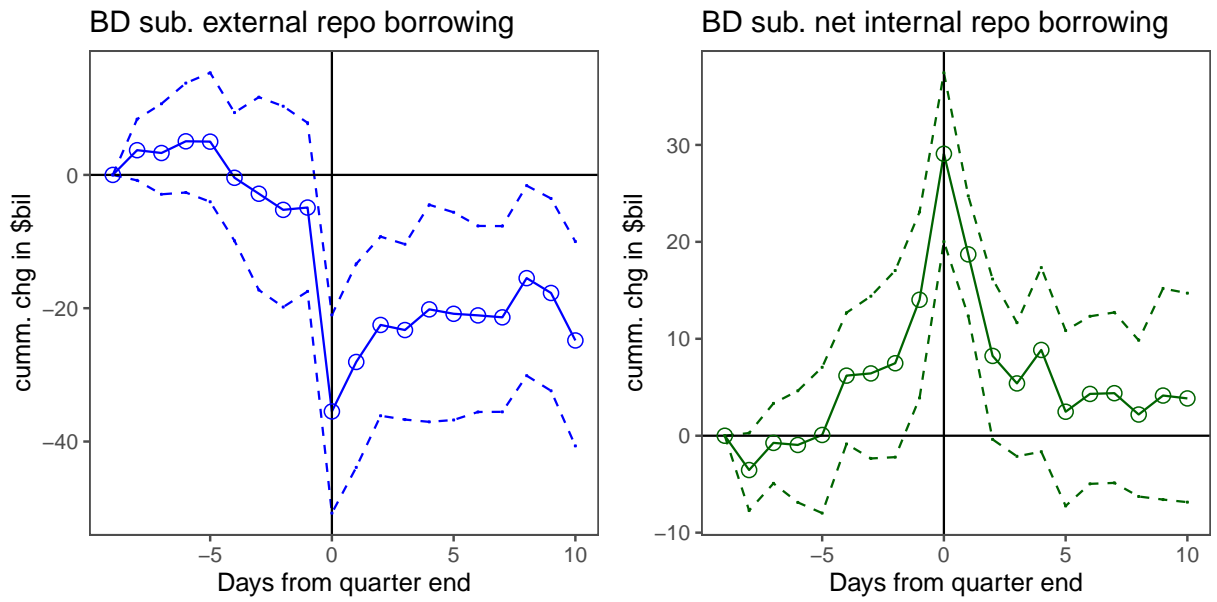
Notes: This figure shows quarter-end changes in U.S. GSIBs' dollar reserves, reverse repo lending, repo borrowing, and FX swap lending. The discussions of these liquidity measures are provided in Section 3. The dotted lines denote the 95% confidence interval with bootstrapped standard errors.

Figure 9: Foreign banks' liquidity provision around quarter-ends



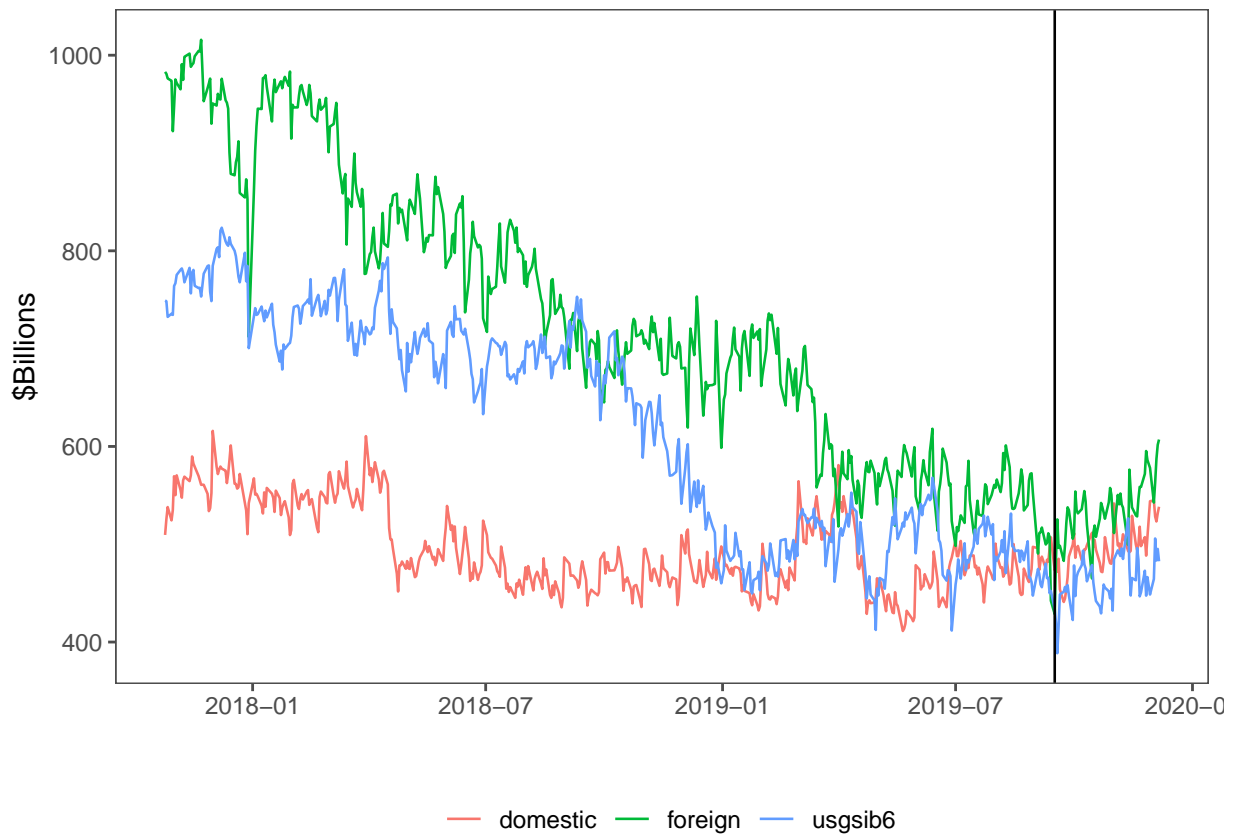
Notes: This figure shows quarter-end changes in foreign banks' dollar reserves, reverse repo lending, repo borrowing, and net reverse repo lending. The positions are aggregated across four foreign banking offices in the U.S. with daily reporting requirements for FR2052a. The discussions of these liquidity measures are provided in Section 3. The dotted lines denote the 95% confidence interval with bootstrapped standard errors.

Figure 10: Broker-dealer dollar repo borrowing and intra-bank transfers near quarter-ends



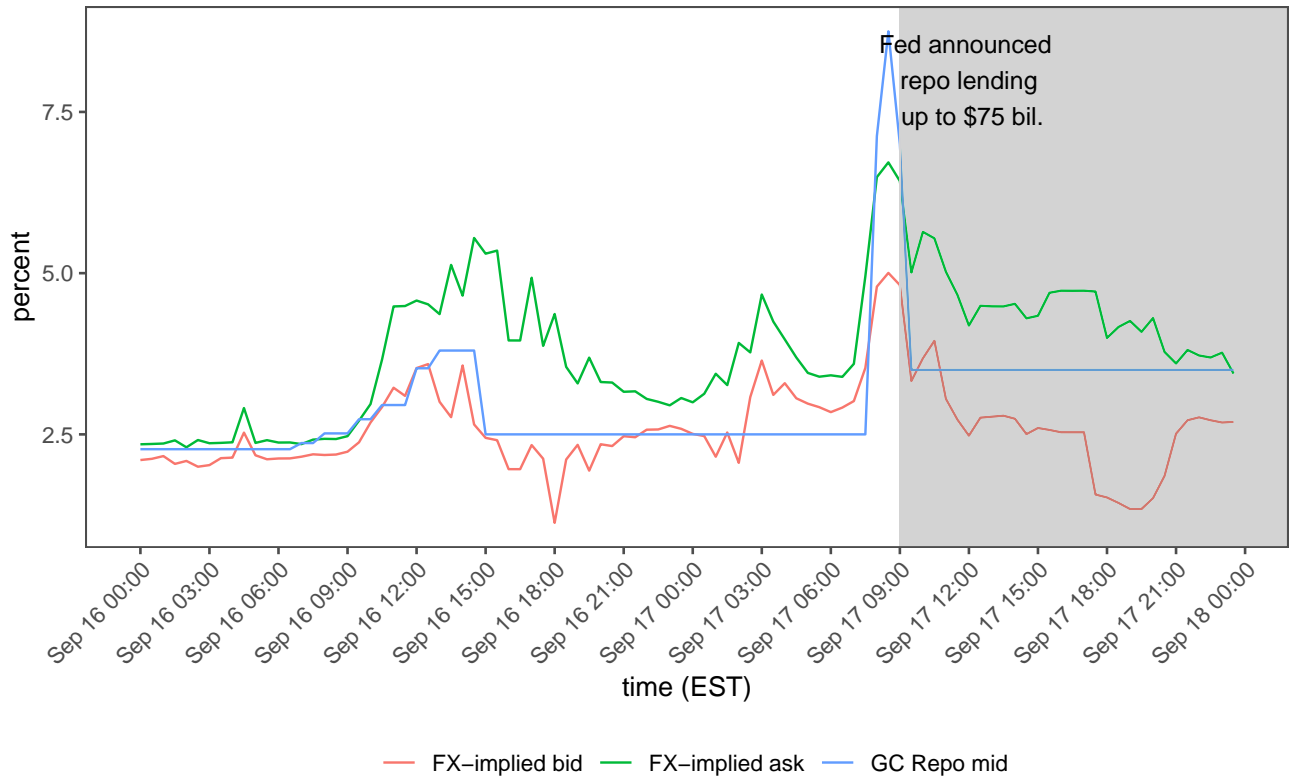
Notes: This figure shows quarter-end changes in external repo borrowing and net internal repo borrowing of the broker-dealer entities. The left panel shows broker-dealers external repo borrowing from unaffiliated third-party lenders. The right panel shows broker-dealers' net internal repo borrowing (gross internal repo borrowing minus gross internal repo lending) from affiliated non-broker-dealer entities. The dotted lines denote the 95% confidence interval with bootstrapped standard errors.

Figure 11: Dollar reserves by bank holding company entity type



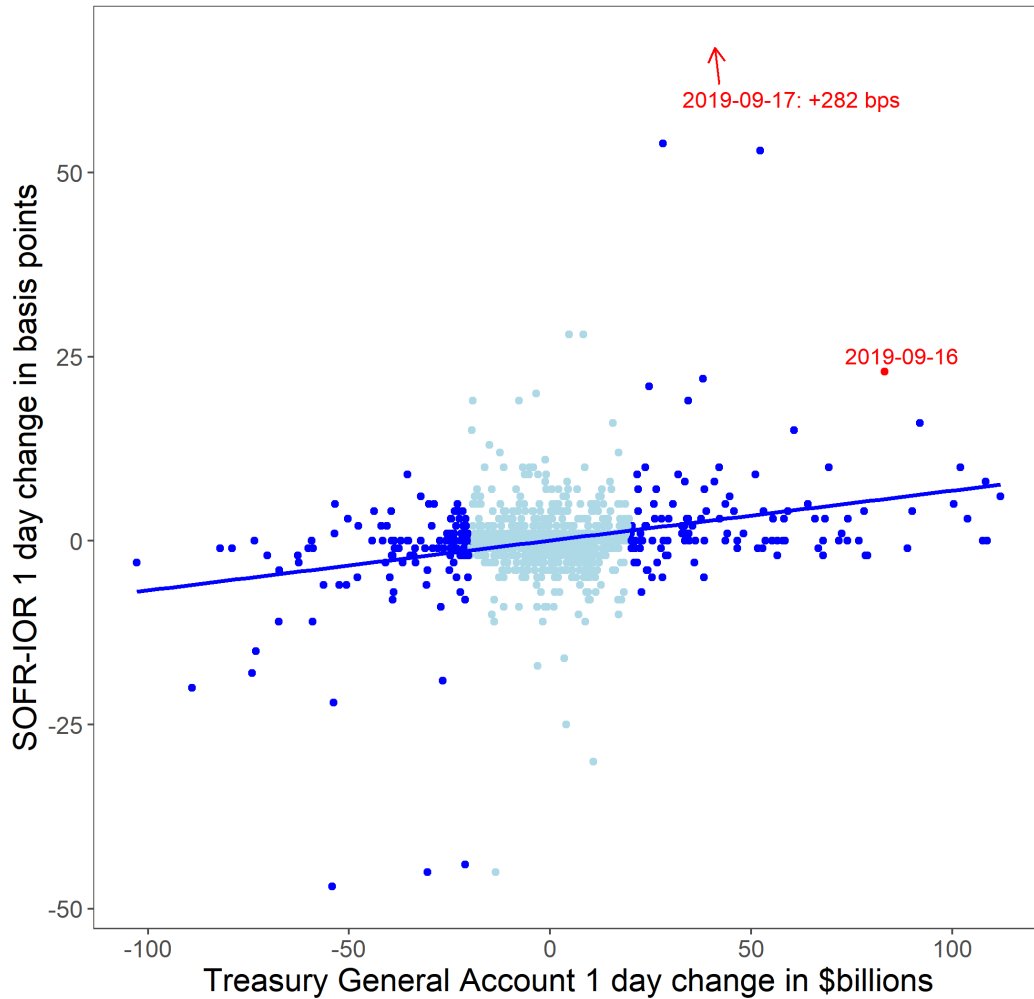
Notes: This figure shows the distribution of total reserve balances across different types of banks. The blue line shows the reserve balances of the U.S. GSIBs in our sample. The red line shows the reserve balances of other U.S. banks. The green line shows the reserve balances of foreign banks. The vertical line denotes September 16, 2019.

Figure 12: September 19 intraday overnight repo and FX-implied funding rates



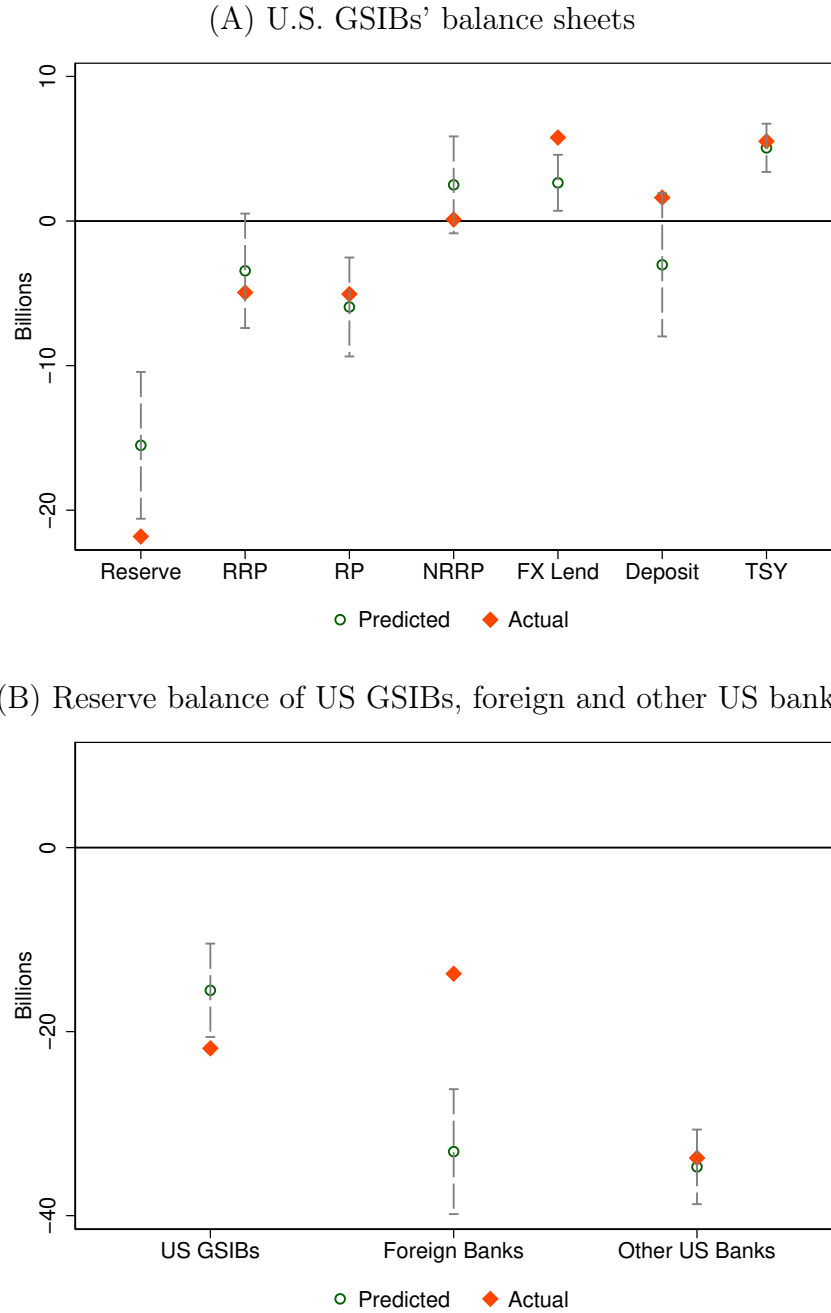
Notes: This figure shows the intraday repo rate and implied dollar funding rates from the FX swap market. The blue line shows the general collateral repo rate from the Thomson Reuters Tick History. The green and red lines show the bid and ask rate, respectively, for the implied dollar funding rate by swapping the deposit rate at the ECB into dollars on the overnight basis. The overnight implied FX swap rate is calculated based on the Bloomberg data with calculation details shown in Footnote [22](#).

Figure 13: Treasury General Account and SOFR-IOR Spread



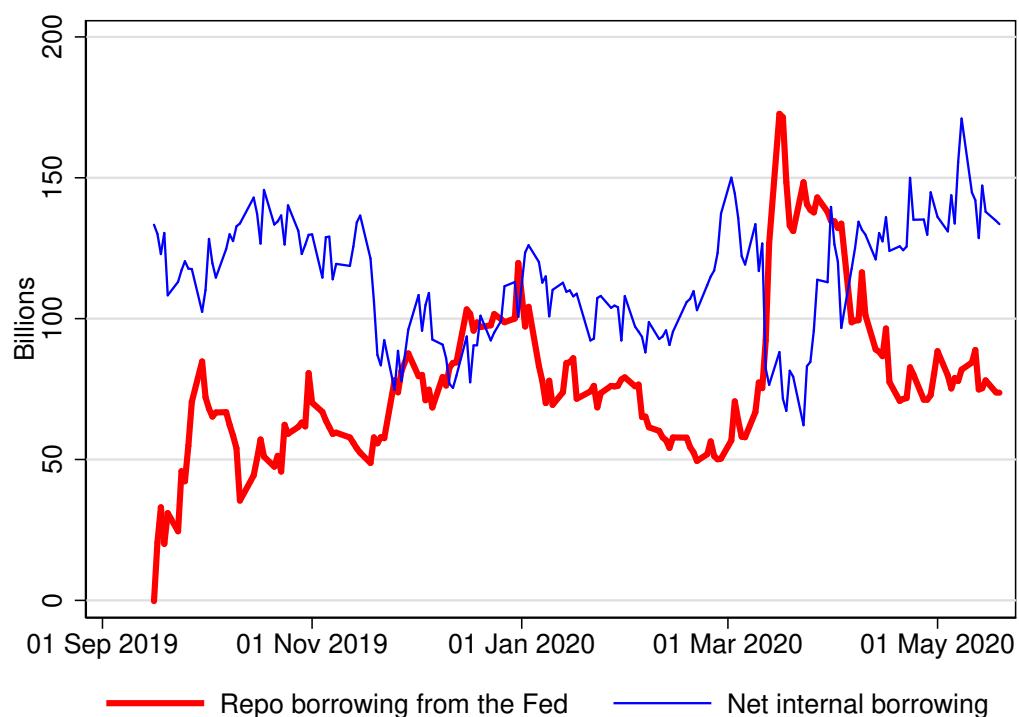
Notes: This figure shows a scatter plot between the daily changes in the spread between the secured overnight financing rate (SOFR) and the interest on excess reserves (IOR) at the Federal Reserve in basis points on the vertical axis, and the daily change in the Treasury General Account (TGA) balance in billions of dollar on the horizontal axis. Dark blue dots denote days with daily changes in the TGA balance greater than \$20 billion in absolute value. The light blue dots denote days with daily changes in the TGA balance less than or equal to \$20 billion. The straight line is the fitted regression line for large TGA change days, with the exception of September 17, 2019 and September 18, 2019 that are beyond the graph. The sample period is December 15, 2015 to May 18, 2020.

Figure 14: Predicted and actual one-day change on September 16, 2019



Notes: Panel A shows the predicted and actual one-day change in the intermediation activities of the U.S. GSIBs on September 16, 2019. The green dot shows the point estimate for the predicted one-day change based on the regression results in Table 2 and the \$83 billion TGA increase on September 16, 2019. The vertical dashed line denotes the 95 percent confidence interval for the point estimate of the predicted change. Panel B shows the predicted and actual one-day change in the reserve balance of U.S. GSIBs, foreign banks, and other U.S. banks. The green dot shows the point estimate for the predicted one-day change based on the regression results in Table 4.

Figure 15: Broker-dealers Fed Repo Facility Usage and Internal-cash Substitution



Notes: This figure shows the Fed repo facility draw and internal repo borrowing (from affiliated depository institutions) by broker-dealer arms of U.S. GSIBs since the establishment of the repo facility on September 16, 2019.

Table 1: Impacts of Quarter-Ends, TGA, and SOMA Fluctuations on Intermediation Spreads

	<i>Dependent variable:</i>					
	$\Delta SOFR - IOR$	$\Delta GCF - IOR$	$\Delta TGCR - IOR$	$\Delta GCF - TGCR$	$\Delta EURIOR$	$\Delta JPYIOR$
	(1)	(2)	(3)	(4)	(5)	(6)
$Qend_t$	12.400*** (2.600)	30.400** (13.600)	8.010*** (2.580)	22.300* (11.500)	137.000** (59.900)	416.000*** (118.000)
$Qstart_t$	-11.000*** (3.690)	-31.800** (13.200)	-6.350** (2.600)	-25.500* (14.400)	-153.000* (80.400)	-257.000*** (92.500)
ΔTGA_t	0.047*** (0.008)	0.072*** (0.016)	0.039*** (0.008)	0.033*** (0.012)	0.272*** (0.062)	0.455*** (0.158)
$\Delta SOMA_t$	-0.579*** (0.146)	-1.510** (0.660)	-0.479*** (0.153)	-1.030* (0.589)	-2.680** (1.330)	1.470 (2.310)
Constant	-0.238** (0.121)	-0.586** (0.241)	-0.197* (0.104)	-0.378* (0.197)	-0.452 (0.653)	-1.660 (1.930)
N	933	930	933	930	902	837
R ²	0.294	0.285	0.227	0.198	0.237	0.362

Notes: This table shows the regression results of the quarter-end dummies, TGA and SOMA fluctuations on daily changes in various intermediation spreads. The dependent variables are as follows: daily changes in the SOFR–IOR spread (Column 1), daily changes in the GCF repo–IOR spread (Column 2), daily changes in the Triparty (TGCR) repo–IOR spread (Column 3), daily changes in the GCF–TGCR repo spread (Column 4), daily changes spread between the overnight implied dollar rate by swapping the ECB deposit rate and the Fed IOR (Column 5), and daily changes in the spread between the overnight implied dollar rate by swapping the BOJ deposit rate and the Fed IOR (Column 6). The independent variables are as follows: $Qend_t$, a dummy variable indicating the last business day of the quarter; $Qstart_t$, a dummy variable indicating the first business day of the quarter; ΔTGA , daily changes in the TGA balance; $\Delta SOMA$, daily changes in the Fed portfolio holdings of Treasury securities. Robust standard errors are reported in the parentheses with significance levels denoted by *p<0.1; **p<0.05; ***p<0.01.

Table 2: Impact of TGA, SOMA, and quarter-end constraints on Intermediation Activities

	<i>Dependent variable:</i>						
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
	ΔRSV_t	ΔRRP_t	ΔRP_t	$\Delta NRRP_t$	ΔFX_t	$\Delta Deposit_t$	$\Delta TSY_t^{outright}$
$Qend_t$	-26.200*** (7.420)	-6.570 (7.270)	-29.500*** (4.810)	23.000*** (5.190)	10.600*** (3.150)	1.780 (4.470)	3.230 (2.830)
$Qstart_t$	42.000*** (5.480)	-6.780 (5.320)	0.916 (4.200)	-7.700* (4.250)	-8.420** (3.270)	29.900*** (4.670)	-0.745 (1.520)
ΔTGA_t	-0.181*** (0.036)	-0.041* (0.025)	-0.078*** (0.021)	0.037* (0.022)	0.031*** (0.012)	-0.034 (0.038)	0.060*** (0.010)
$\Delta SOMA_t$	0.492 (0.305)	-1.150*** (0.302)	-0.359 (0.257)	-0.794*** (0.249)	-0.178 (0.116)	-0.895*** (0.241)	-0.090 (0.056)
Constant	-0.482 (0.610)	-0.052 (0.472)	0.553 (0.412)	-0.605 (0.399)	0.082 (0.229)	-0.196 (0.607)	0.102 (0.201)
N	932	932	932	932	932	932	932
R^2	0.142	0.044	0.104	0.086	0.067	0.073	0.046

Notes: This table shows regression results of one-day changes in the TGA account (ΔTGA_t), net SOMA purchase ($\Delta SOMA_t$), and quarter-end ($Qend_t$) and quarter-starts ($Qstart_t$) on daily changes in the U.S. GSIBs intermediation activities. The dependent variables are as follows: changes in reserves (Column 1), changes in dollar reverse repos (Column 2), changes in dollar repos (Column 3), changes in net dollar reverse repos, or the difference between reverse repos and repos in dollars (Column 4), changes in dollar lending in the FX swap market (Column 5), changes in dollar deposits (Column 6), and changes in outright Treasury holdings (Column 7). $Qend_t$ is a dummy variable indicating the last business day of the quarter, and $Qstart_t$ is a dummy variable indicating the first business day of the quarter. Robust standard errors are reported in parentheses with significance levels denoted by *p<0.1; **p<0.05; ***p<0.01.

Table 3: TGA fluctuations and intra-bank transfers

	Broker-Dealers		Non-Broker Dealers	
	(1) External ΔRP_t	(2) Net Internal ΔRP_t	(3) External ΔRP_t	(4) $\Delta Reserves_t$
$Qend_t$	-30.800*** (4.930)	14.600*** (3.190)	1.240 (1.500)	-26.200*** (7.420)
$Qstart_t$	3.640 (3.850)	-11.800*** (2.420)	-2.720** (1.300)	42.000*** (5.480)
ΔTGA_t	-0.069*** (0.020)	0.020 (0.016)	-0.010 (0.008)	-0.181*** (0.036)
$\Delta SOMA_t$	-0.345 (0.232)	-0.307*** (0.114)	-0.014 (0.099)	0.492 (0.305)
Constant	0.495 (0.384)	-0.157 (0.309)	0.058 (0.147)	-0.482 (0.610)
N	932	932	932	932
R^2	0.123	0.066	0.008	0.142

Notes: This table shows regression results of daily changes in the TGA balances and Fed SOMA holdings on daily changes in the repo borrowing and intra-office transfers between the broker-dealer entities and non-broker-dealer entities. Columns 1-2 show regression results for changes in broker-dealer entities' external repo borrowing from a third party outside the same bank and net internal repo borrowing from non-broker-dealer entities of the same bank, respectively. Column 3 shows results for changes in external repo borrowing of the non-broker-dealer entities, and Column 4 shows results for changes in the Fed reserve position of the non-broker-dealers. Robust standard errors are reported in parentheses with significance levels denoted by *p<0.1; **p<0.05; ***p<0.01.

Table 4: Impact of TGA, SOMA, and quarter-end constraints on reserve distribution

	<i>Dependent variable:</i>			
	$\Delta RSV_t^{USGISBs}$	$\Delta RSV_t^{Foreign}$	$\Delta RSV_t^{Domestic}$	$\Delta ONRRP_t$
	(1)	(2)	(3)	(4)
$Qend_t$	-28.000*** (7.240)	-101.000*** (20.200)	25.500*** (4.510)	95.000*** (16.800)
$Qstart_t$	42.900*** (5.460)	82.800*** (18.700)	1.050 (6.380)	-119.000*** (19.000)
ΔTGA_t	-0.186*** (0.035)	-0.406*** (0.044)	-0.406*** (0.033)	0.055 (0.043)
$\Delta SOMA_t$	0.573** (0.286)	2.570*** (0.613)	-0.692*** (0.203)	-1.230** (0.537)
Constant	-0.363 (0.590)	0.688 (0.717)	-0.893* (0.488)	-0.198 (0.644)
N	931	931	931	931
R^2	0.159	0.384	0.268	0.425

Notes: This table shows regression results of one-day changes in the TGA account (ΔTGA_t), net SOMA purchases ($\Delta SOMA_t$), and quarter-end ($Qend_t$) and quarter-starts ($Qstart_t$) on daily changes in reserve balances for financial institutions and in the balance of the Federal Reserve's ON RRP facility. Column 1 shows regression results for changes in reserve balances for the six U.S. GSIBs in our sample, while column 2 shows results for foreign banks with U.S. branches and subsidiaries. Column 3 shows results for other U.S. banks not classified in the other two groups. Column 4 shows results for changes in the ON RRP facility. $Qend_t$ is a dummy variable indicating the last business day of the quarter, and $Qstart_t$ is a dummy variable indicating the first business day of the quarter. The sample period is December 15, 2015 until August 31, 2019. Robust standard errors are reported in parentheses with significance levels denoted by *p<0.1; **p<0.05; ***p<0.01.

Table 5: U.S. GSIBs' Fed Repo Line Usage and Intermediation Activities

	<i>Dependent variable:</i>				
	ΔRSV_t	ΔRRP_t	$\Delta R P_t^{exFed}$	$\Delta NRRP_t^{exFed}$	$\Delta F X_t$
	(1)	(2)	(3)	(4)	(5)
$\Delta FedRepo$	-0.014 (0.229)	0.291* (0.153)	-0.446** (0.185)	0.784*** (0.171)	0.254*** (0.096)
Constant	4.960** (2.340)	-0.832 (1.510)	-0.769 (1.140)	-0.055 (1.400)	0.127 (0.715)
N	158	158	158	158	158
R ²	0.00002	0.021	0.079	0.151	0.066

Notes: This table shows the relationship between U.S. GSIBs' draw on the Fed repo facility ($\Delta FedRepo$) and their various intermediation activities. The dependent variables are as follows: changes in reserves (Column 1), changes in dollar reverse repos (Column 2), changes in dollar repos excluding borrowings from the Fed repo facility (Column 3), changes in net dollar reverse repos excluding borrowings from the Fed repo facility (Column 4), changes in dollar lending in the FX swap market (Column 5). The sample period is from October 1, 2019 to May 18, 2020. Robust standard errors are reported in the parentheses with significance levels denoted by *p<0.1; **p<0.05; ***p<0.01.

Internet Appendix

"U.S. Banks and Global Liquidity"

Ricardo Correa Wenxin Du Gordon Liao

A FR 2052a and FR Y9-C Comparison

This comparison between the LCR assessment data and the FR Y-9C data serves two important functions. First, it verifies that the daily balance sheet snapshots assembled from the liquidity monitoring reports are of high quality and broadly match the public filings reported on quarter-ends. Second, the comparison highlights an advantage of the LCR monitoring data for assessing the gross amount of intermediation in dollar liquidity. As the FR Y-9C data defers to Generally Accepted Accounting Principles (GAAP) standards in the netting treatment of certain balance sheet items, matched-book exposures in repurchase agreements (repos) are significantly lower as reported in this form. For instance, the gross exposure in repo borrowing aggregated across the six GSIBs is around \$1.8 trillion at the end of 2018 according to the LCR data, but only around \$800 billion according to the FR Y-9C. The former more accurately reflect the volume of repo intermediation from other sources.¹

Figure [A1](#) shows that repo and reverse repo positions are significantly larger in FR2052a than in Y9-C. The net reverse repo positions from the two sources have similar trends. The other main asset and liability items from the two sources are broadly in line with each other.

¹Daily triparty repo volume was around \$2.2 trillion and GCF repo was around \$700 billion at the end of 2018, according to the Federal Reserve Bank of New York. Additionally, sizable bilateral repo borrowings also make up a large part of the banks' repo exposure.

B Intraday rate movements during the September 2019 event

This section describes the intraday movements in several rates during the September 16 and 17 event shown in Figure 12.

Even though the GC repo rate spiked to its high on Tuesday September 17, the repo market was already experiencing significant strains on Monday after the TGA balance increase. The morning of Monday, September 16th started with elevated but orderly secured funding rates. Both GC repo and FX implied dollar rate were trading around 2.5%, which is around 20 basis points higher than the previous trading day's close and 40 basis points higher than the interest on reserve. The bid-ask spread in FX swapped dollar funding was also relatively tight. The GC repo rate increased steadily throughout the day peaking around 4.5% (mid) by late afternoon, when the market closed for the day. The timing of the repo rate increase in late morning and early afternoon suggests that auction settlement-related financing is likely a driver of the repo rate increase.²

The elevated secured funding rates carried over to Tuesday from the day before. Despite the lack of additional Treasury settlement or tax payment on Tuesday (the TGA balance only increased by \$8 billion on Tuesday), the GC repo borrowing rate quickly increased to a high of 10% by early-morning, when the bulk of the repo volume occurs, and the FX-implied funding rate reacted in lock step. Shortly after 9 a.m, the Federal Reserve Bank of New York announced that it would conduct repo operations and ultimately lent \$53 billion to primary dealers in overnight repo. The secured funding rates declined sharply thereafter.

²Since the repo market starts trading early in the morning, a large fraction of trades were done before 9 a.m., around this time, \$78 of new treasury issuance was settled through the Bank of New York Mellon (BNYM) (Since 2017, BNYM has been the sole provider of U.S. government securities settlement and triparty repo services for broker-dealers.). Primary dealers typically draw down or overdraft their clearing accounts at BNYM to fund the treasury settlement, and, over the course of the day, these dealers sell the new bonds in exchange for cash to “refill” their clearing account by 3:30 pm (Pozsar, 2019). A fraction of the newly issued treasury bonds were sold off to real-money investors, and the remaining portion of the new issuance were bought by levered investors or remained in dealer's inventory, both of which required repo financing.

C Dealer security financing needs

In this section, we present suggestive evidence that dealers' own security financing needs also contributed to the September 2019 liquidity crunch in addition to the breakdown of reserve-based intermediation.

Decomposing the balance sheet shifts by subsidiary, we find that the decline in reserves in depository institutions coincided with an increase in repo borrowing by the broker-dealer affiliates to finance the holdings of Treasury securities. Dealer accumulation of Treasury securities is likely related to reduced demand from real money institutions at Treasury auctions as the Treasury yield curve flattened and inverted throughout this period. Figure A8 shows that these broker-dealer reached their highest level of external repo financing (net reverse repo reached their lowest level) immediately prior to the repo rate spike. This financing need coincided with an increase in primary dealers' accumulation of coupon securities throughout 2018 and early 2019, as shown in Figure A9.³

Two additional trends that are typically associated with funding strains also emerged around the same time. First, broker-dealer were increasingly reliant on worse collaterals to finance their borrowings. Panel A in Figure A10 shows that broker-dealers have historically net lend out cash against Treasuries collateral, but net borrowed cash against non-Treasury collaterals. In 2019, broker-dealers reduced the net lending collateralized by Treasuries and increased the reliance on funding using non-Treasuries as collateral. An increasing fraction of the borrowing were backed by equities and Government Sponsored Enterprise (GSE) bonds. Second, dealers became more engaged in maturity transformation in 2019. Panel B in Figure A10 shows that while dealers continue to net lend the same amount of termed repo with maturity greater than one-week, they have started to borrow with short maturity repo contracts. Dealers became net borrowers of short-maturity repo, as opposed to net lender in earlier period.

³Primary dealers shown in Figure A9 include dealers beside those affiliated with the six GSIBs.

The maturity and collateral mismatch observed in 2019 bear resemblance to the hallmarks of broker-dealer’s repo financing just prior to the financial crisis. The key difference is that this time, the funding pressure arises from the need to finance Treasury securities, rather than illiquid securities.

D FX swap exposure in the bank trading book

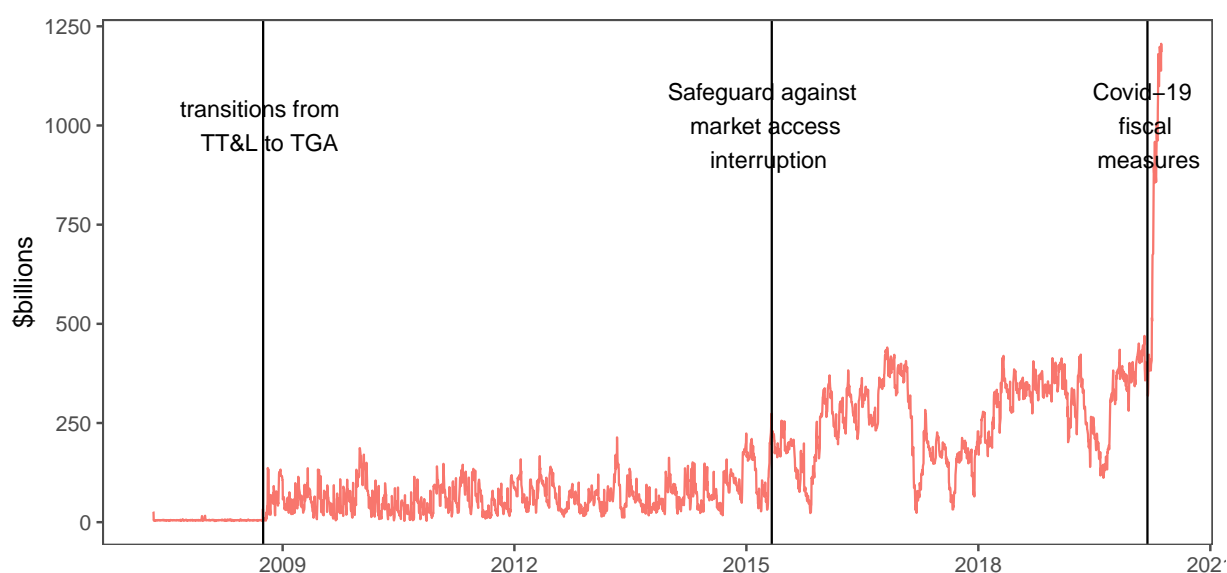
Figure [A11](#) plots the foreign currency funding gap for the four major currencies, and our estimated FX swap exposure in the bank’s trading book based on information included in the FR Y-14 data. We can observe that a positive foreign currency funding gap in euros, yen and sterling is indeed matched by a short position in the foreign currency and a long position in dollars in the FX swap market. Since the FR Y-14 data only capture FX swap exposure in the trading book, it is not surprising that these exposures are lower than the overall foreign currency funding gap. In the case of the euro, the correlation between the overall euro funding gap and the estimated short-euro-long-dollar FX swap position in the trading book is about 70%.

Figure A1: Comparison of FR 2052a and FR Y-9C



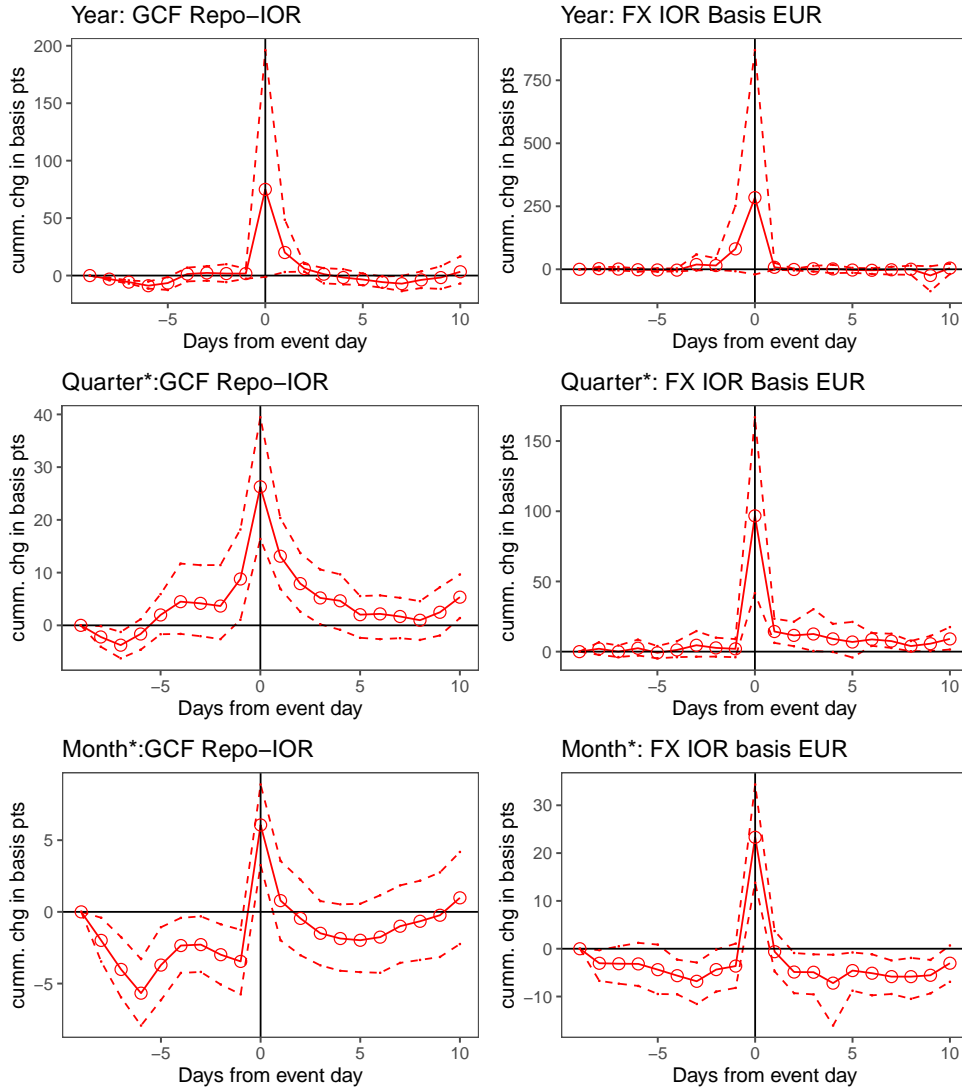
Notes: This figure provides a comparison between the balance sheet items constructed from various inflow and outflow product categories in FR 2052a and the reported balance sheet items in FR Y9-C.

Figure A2: Fluctuations in the Treasury General Account Balance



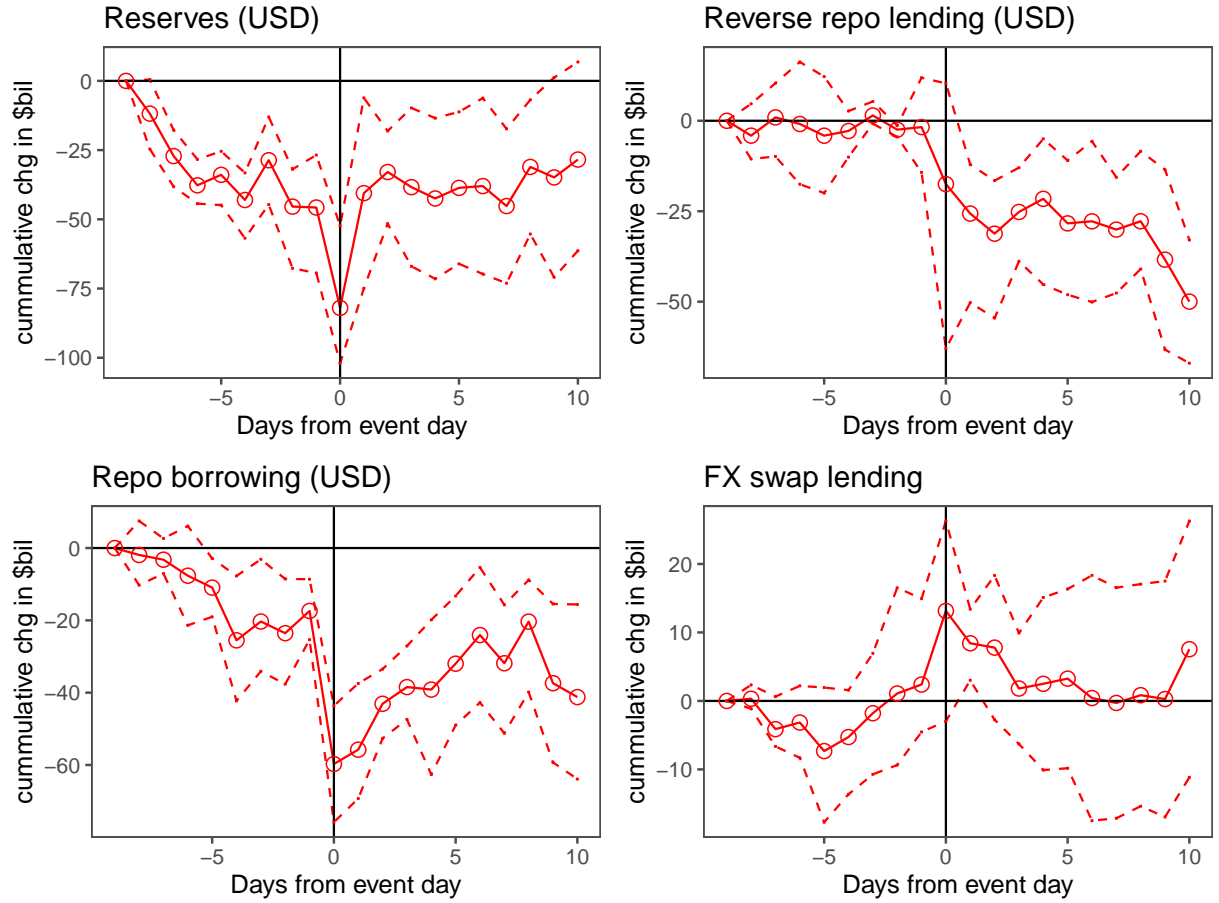
Notes: This figure shows time series of the Treasury General Account (TGA) balance. Prior to 2009, the U.S. Treasury held most of its balances in commercial banks through the Treasury Tax and Loan Program. In May 2015, the Treasury expanded its TGA balance to protect against a potential interruption in market access. In March 2020, Increased fiscal spending relating to the COVID-19 pandemic further prompted large increase in the TGA account.

Figure A3: Period-end short-term intermediation spreads



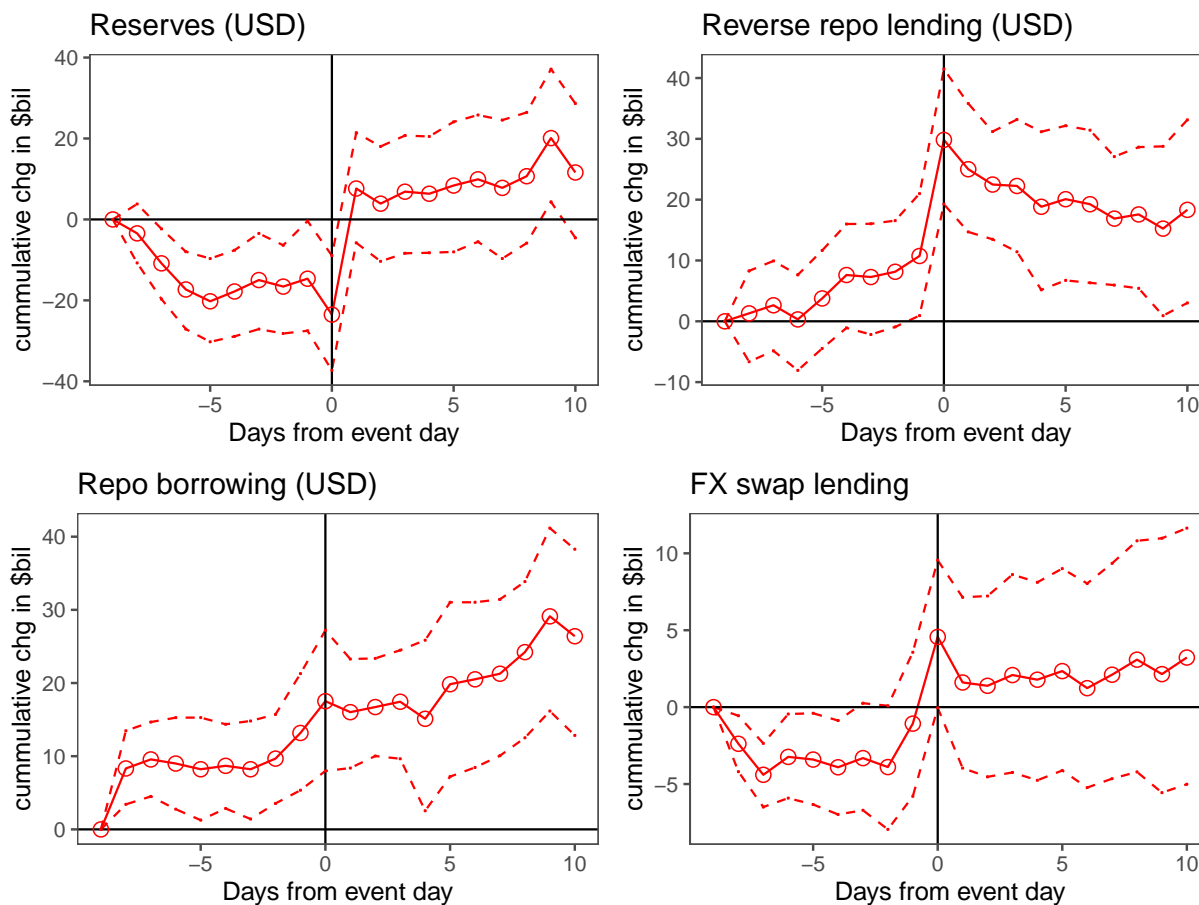
Notes: This figure shows the period-end effects on short-term funding spreads. The left column shows the spread between the GCF repo rate and the interest on reserve (IOR) at the Federal Reserve. The right column shows the EUR overnight FX IOR basis, measured as the spread of the implied dollar funding rate by swapping the ECB deposit rate minus the Fed IOR. The sample period is from December 2015 to September 2019. Quarter-ends refer to quarter-ends that are not year-ends. Month-ends refer to month-ends that are not quarter-ends. The dotted lines denote the 95% confidence interval with bootstrapped standard errors.

Figure A4: U.S. GSIBs' liquidity provision around year-ends



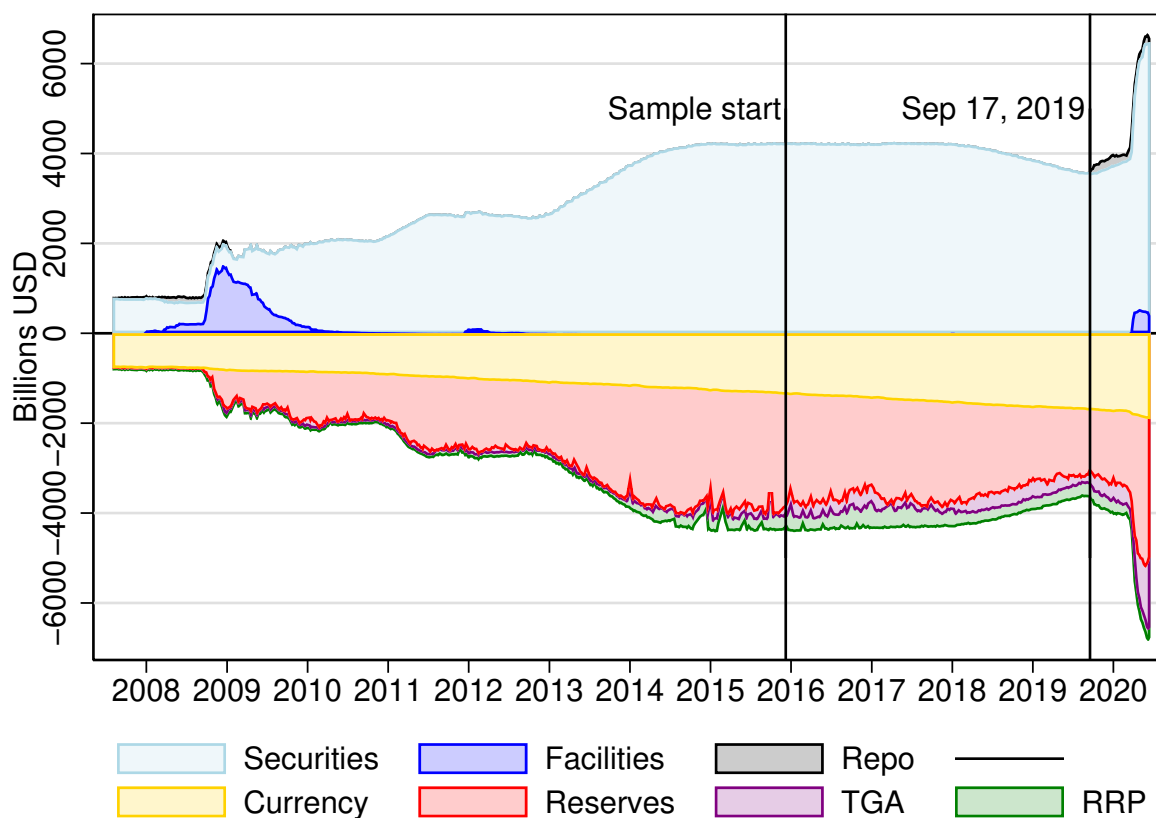
Notes: This figure shows year-end changes in U.S. GSIBs' dollar reserves, reverse repo lending, repo borrowing, and FX swap lending. The discussions of these liquidity measures are provided in Section 3. The dotted lines denote the 95% confidence interval with bootstrapped standard errors.

Figure A5: U.S. GSIBs' liquidity provision around month-ends



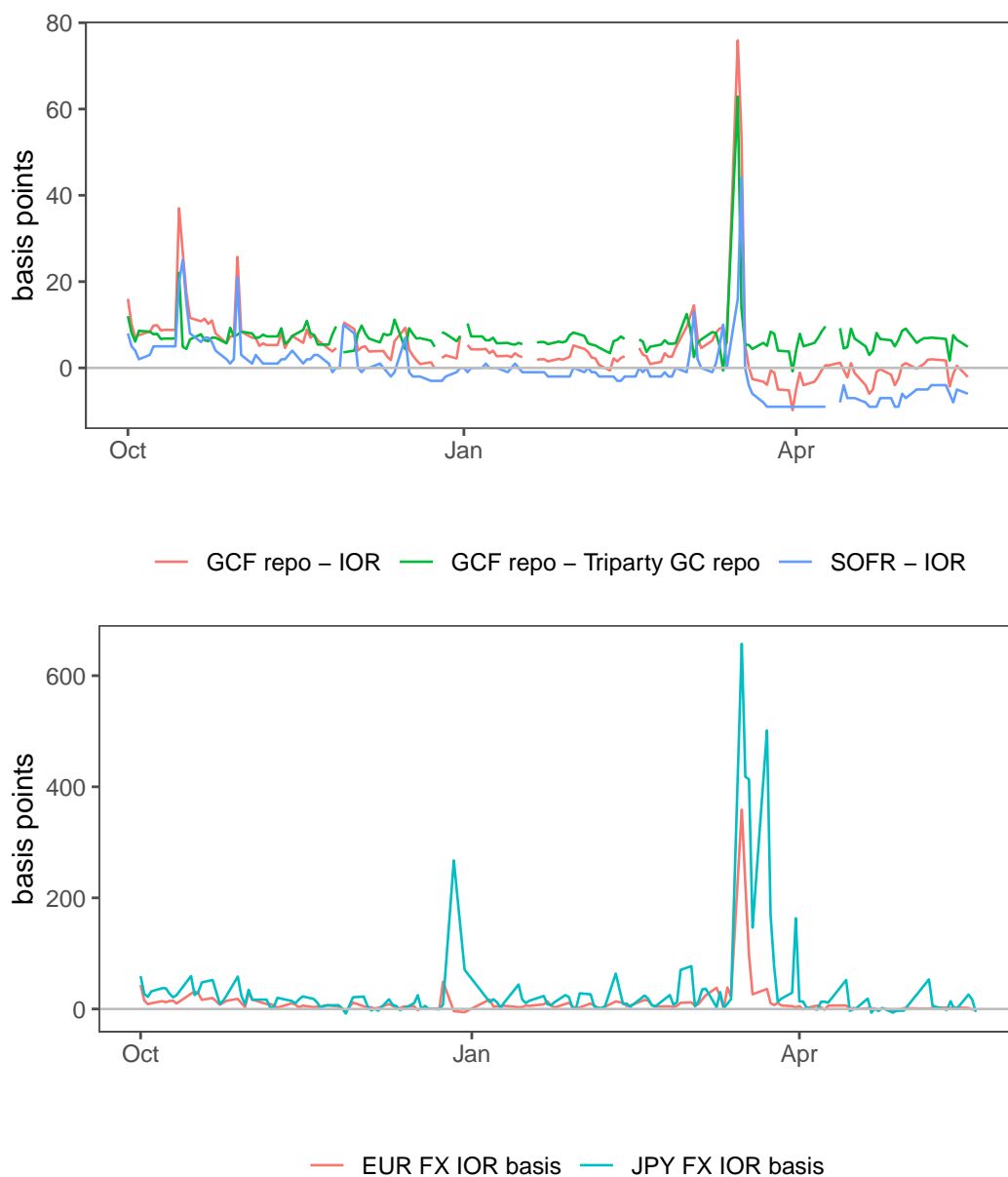
Notes: This figure shows month-end changes in U.S. GSIBs' dollar reserves, reverse repo lending, repo borrowing, and FX swap lending. The discussions of these liquidity measures are provided in Section 3. Month-ends are defined as month-ends that do not coincide quarter-ends. The dotted lines denote the 95% confidence interval with bootstrapped standard errors.

Figure A6: Evolution of the Federal Reserve Balance Sheet Post-GFC



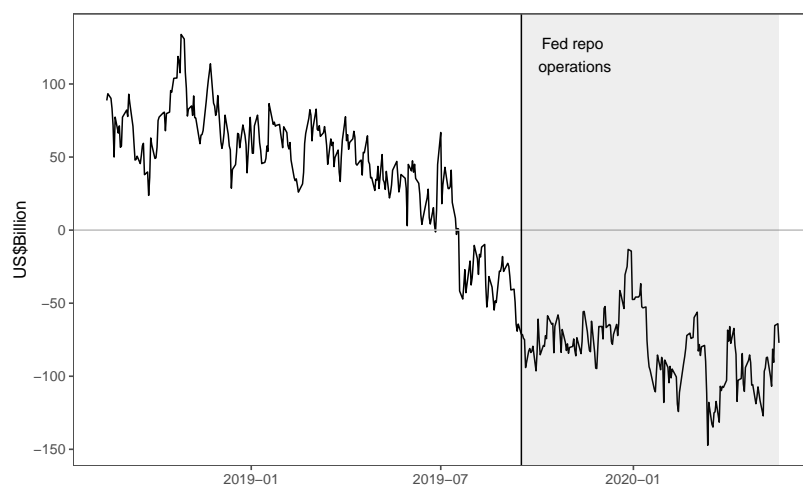
Notes: This figure plots major assets and liability items of the Federal Reserve post-GFC. "Securities" refers to outright securities holdings, "Facilities" denotes liquidity facility, including central bank swap lines; "Repo" denotes the repo facility; "Currency" denotes currency in circulation; "Reserves" denotes total bank reserves; "TGA" denotes the Treasury general account; and "RRP" denotes the reverse repo facility.

Figure A7: Dollar Funding Spreads Since September 2019



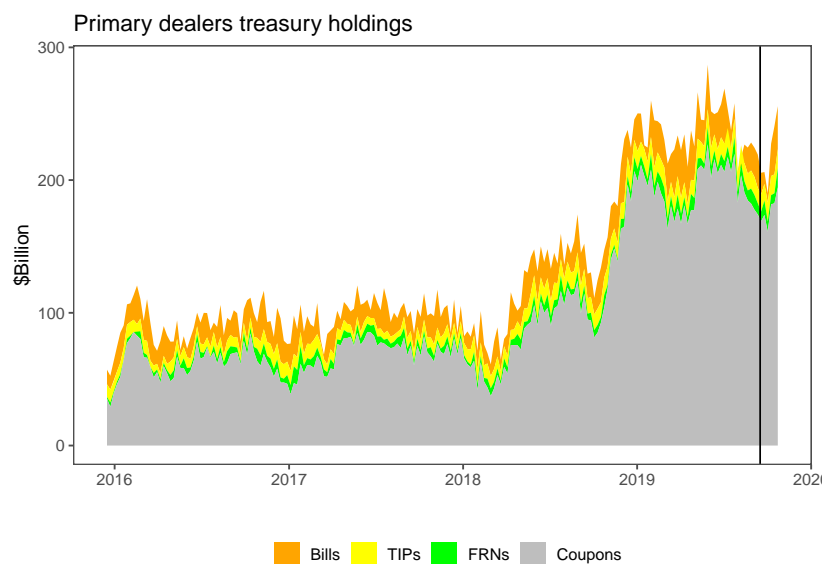
Notes: This figure shows the funding spreads since post the repo rate spike in September 2019. In the top panel, we plot the spread between the GCF general collateral Treasury repo rate and interest on excess reserve (IOR) at the Federal Reserve ("GCF repo-IOR"), the spread between the GCF and Triparty Treasury general collateral repo spread ("GCF Repo - Triparty GC Repo Spread"), and the spread between the Secured Overnight Financing Rate (SOFR) and the IOR ("SOFR-IOR"). In the bottom panel, we plot the spread of the implied dollar funding rate by swapping the ECB deposit rate over the Fed IOR ("EUR FX IOR basis"), and the spread of the implied dollar funding rate by swapping the BOJ deposit rate over the Fed IOR ("JPY FX IOR basis").

Figure A8: Broker-dealer dollar net reverse repo



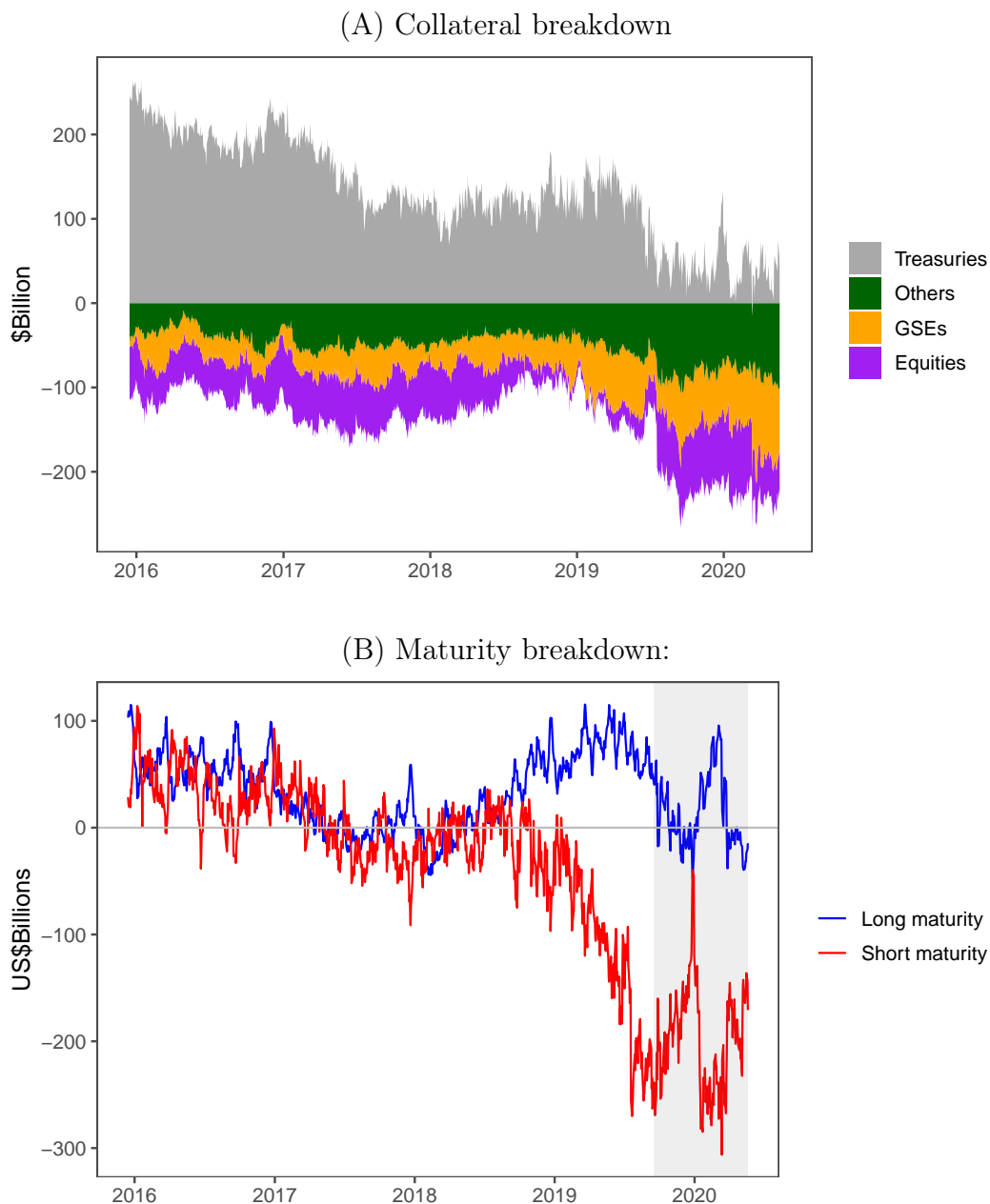
Notes: This figure shows the net reverse repo position (reverse repos minus repos) denominated in dollars for the broker-dealer entities of U.S. GSIBs in our sample. The shaded area denotes the period since the Fed introduced the repo facility on September 17, 2019.

Figure A9: Prime dealers treasury holdings



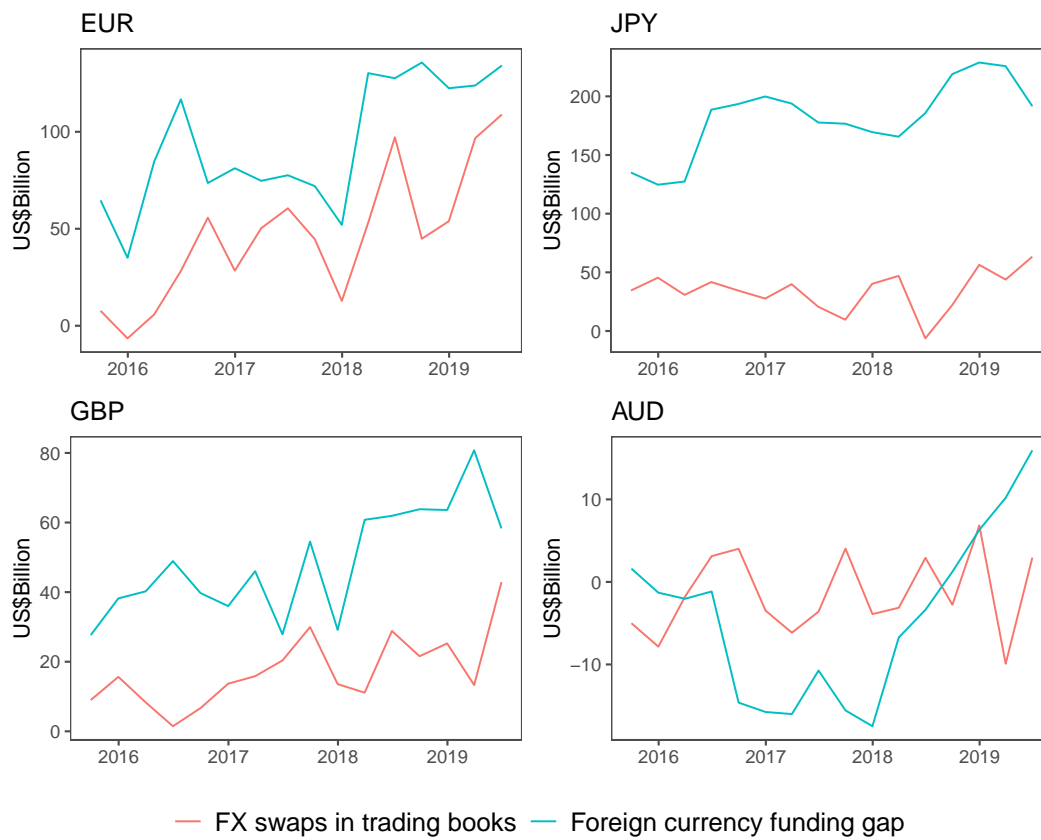
Notes: This figure shows the net Treasury holdings for all prime dealers (including primary dealers within our sample U.S. GSIBs and all other primary dealers). The data is from weekly public release of FR 2004 filings.

Figure A10: Broker-dealer dollar net reverse repo by collateral and maturity



Notes: Panel (A) shows collateral breakdown of the net reverse repo position for the broker-dealer entities of the U.S. GSIBs. For a given collateral type, a positive number indicates that the broker-dealers are lending more than borrowing against the collateral. Panel (B) shows the maturity breakdown of the net reverse repo position for the broker-dealer entities of the U.S. GSIBs. Long-maturity refers to contracts with maturity greater than one week, and short-maturity refers to contracts with maturities of one week or less.

Figure A11: U.S. GSIBs funding gaps by currency and FX swaps



Notes: This figures shows the quarterly foreign currency funding gap as the difference between foreign currency assets and liabilities for U.S. GSIBs in blue based on the FR 2052a data for the EUR, JPY, GBP and AUD. The red line shows and the estimated FX swap exposure that goes long in dollars and short in the respective foreign currency from the Y14 data.

Table A1: Impacts of Quarter-Ends, TGA, and SOMA Fluctuations on Intermediation Spreads: Post September 2019

	<i>Dependent variable:</i>					
	$\Delta SOFR - IOR$	$\Delta GCF - IOR$	$\Delta TGCR - IOR$	$\Delta GCF - TGCR$	$\Delta EURIOR$	$\Delta JPYIOR$
	(1)	(2)	(3)	(4)	(5)	(6)
$Qend_t$	-1.650 (1.970)	-3.680 (6.380)	-0.001 (0.029)	-3.600 (3.790)	6.690 (21.700)	138.000** (58.500)
$Qstart_t$	-14.300 (12.500)	-12.400 (13.700)	-0.172 (0.131)	4.870*** (1.360)	-1.440 (9.460)	-29.400 (42.500)
ΔTGA_t	0.045*** (0.017)	0.086** (0.036)	0.0004** (0.0002)	0.046 (0.028)	0.223 (0.177)	0.533 (0.367)
$\Delta SOMA_t$	-0.010 (0.036)	-0.027 (0.042)	-0.0001 (0.0004)	-0.023 (0.032)	-0.141 (0.148)	-0.955* (0.526)
Constant	-0.213 (0.435)	-0.241 (0.482)	-0.002 (0.005)	-0.035 (0.311)	0.512 (1.250)	6.600 (5.090)
N	155	157	155	155	150	134
R ²	0.153	0.154	0.180	0.055	0.051	0.110

Notes: This table shows the post-September 2019 regression results of the quarter-end dummies, TGA and SOMA fluctuations on daily changes in various intermediation spreads. The dependent variables are as follows: daily changes in the SOFR–IOR spread (Column 1), daily changes in the GCF repo–IOR spread (Column 2), daily changes in the Triparty (TGCR) repo–IOR spread (Column 3), daily changes in the GCF–TGCR repo spread (Column 4), daily changes spread between the overnight implied dollar rate by swapping the ECB deposit rate and the Fed IOR (Column 5), and daily changes in the spread between the overnight implied dollar rate by swapping the BOJ deposit rate and the Fed IOR (Column 6). The independent variables are as follows: $Qend_t$, a dummy variable indicating the last business day of the quarter; $Qstart_t$, a dummy variable indicating the first business day of the quarter; ΔTGA , daily changes in the TGA balance; $\Delta SOMA$, daily changes in the Fed portfolio holdings of Treasury securities. The sample period is from October 1, 2019 to May 18, 2020. Robust standard errors are reported in the parentheses with significance levels denoted by *p<0.1; **p<0.05; ***p<0.01.

Table A2: Impact of Quarter-Ends, TGA, and SOMA Fluctuations on Intermediation Activities: Post September 2019

	<i>Dependent variable:</i>						
	ΔRSV_t	ΔRRP_t	ΔRP_t	$\Delta NRRP_t$	ΔFX_t	$\Delta Deposit_t$	$\Delta TSY_t^{outright}$
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
$Qend_t$	-43.700*** (12.100)	-10.900 (33.800)	-29.200*** (6.430)	18.300 (27.800)	8.600*** (2.430)	-40.000*** (4.800)	-5.210 (6.270)
$Qstart_t$	49.000*** (8.500)	-28.700 (21.300)	-24.500*** (7.370)	-4.270 (18.100)	-6.510 (6.060)	16.500 (14.400)	10.500* (5.820)
ΔTGA_t	-0.293*** (0.075)	0.109** (0.045)	0.010 (0.032)	0.100** (0.048)	0.070*** (0.022)	-0.053 (0.078)	0.035 (0.026)
$\Delta SOMA_t$	0.511*** (0.131)	-0.190** (0.078)	-0.105** (0.051)	-0.085 (0.069)	-0.019 (0.044)	0.305*** (0.111)	-0.068 (0.043)
Constant	-0.191 (2.230)	1.770 (1.700)	1.350 (1.400)	0.421 (1.690)	0.029 (0.851)	2.990 (2.040)	0.788 (0.710)
N	157	157	157	157	157	157	157
R ²	0.301	0.123	0.123	0.060	0.101	0.101	0.061

Notes: This table shows the post-September 2019 regression results of one-day changes in the TGA account (ΔTGA_t), net SOMA purchase ($\Delta SOMA_t$), and quarter-end ($Qend_t$) and quarter-starts ($Qstart_t$) on daily changes in the U.S. GSIBs intermediation activities. The dependent variables are as follows: changes in reserves (Column 1), changes in dollar reverse repos (Column 2), changes in dollar repos (Column 3), changes in net dollar reverse repos, or the difference between reverse repos and repos in dollars (Column 4), changes in dollar lending in the FX swap market (Column 5), changes in dollar deposits (Column 6), and changes in outright Treasury holdings (Column 7). $Qend_t$ is a dummy variable indicating the last business day of the quarter, and $Qstart_t$ is a dummy variable indicating the first business day of the quarter. The sample period is from October 1, 2019 to May 18, 2020. Robust standard errors are reported in parentheses with significance levels denoted by *p<0.1; **p<0.05; ***p<0.01.

Table A3: Comparisons of FX Lending Measures

	<i>Dependent variable:</i>					
	ΔFX_t	ΔFX_t^{all}	ΔFX_t	ΔFX_t^{all}	ΔFX_t	ΔFX_t^{all}
	(1)	(2)	(3)	(4)	(5)	(6)
$Qend_t$			10.600*** (3.150)	8.480*** (2.360)	11.400*** (3.170)	8.900*** (2.420)
$Qstart_t$			-8.420** (3.270)	-8.640*** (2.700)	-8.270** (3.290)	-8.560*** (2.710)
ΔTGA_t	0.040*** (0.013)	0.030** (0.012)	0.031*** (0.012)	0.021* (0.012)		
$\Delta TSY_t^{Issuance}$					0.004 (0.018)	0.007 (0.019)
ΔTGA_t^{Other}					0.045*** (0.015)	0.029** (0.014)
$\Delta SOMA_t$			-0.178 (0.116)	-0.197* (0.113)	-0.217* (0.118)	-0.217* (0.115)
Constant	0.191 (0.238)	0.181 (0.242)	0.082 (0.229)	0.103 (0.239)	0.188 (0.233)	0.157 (0.239)
N	932	932	932	932	932	932
R ²	0.012	0.007	0.067	0.049	0.070	0.050

Notes: This table shows regression results of one-day changes in the TGA account (ΔTGA_t), net SOMA purchase ($\Delta SOMA_t$), and quarter-end ($Qend_t$) and quarter-starts ($Qstart_t$) on daily changes in two measures of dollar lending in the FX swap market. The benchmark measure ΔFX_t is defined by Equation 1. The alternative measure ΔFX_t^{all} is defined by Equation 2. Column 5 and 6 shows additional breakdown of TGA into changes in net Treasury issuance (ΔTSY_t^{Issue}) and other components of TGA (ΔTGA_t^{Other}). Robust standard errors are reported in parentheses with significance levels denoted by *p<0.1; **p<0.05; ***p<0.01.

Table A4: Impacts of Quarter-Ends, Different Components of TGA, and SOMA Fluctuations on Intermediation Spreads

	$\Delta SOFR - IOR$	$\Delta GCF - IOR$	$\Delta TGCR - IOR$	$\Delta GCF - TGCR$	$\Delta EURIOR$	$\Delta JPYIOR$
	(1)	(2)	(3)	(4)	(5)	(6)
$Qend_t$	11.200*** (2.720)	29.200** (14.200)	7.110*** (2.710)	22.100* (12.000)	146.000** (60.300)	425.000*** (118.000)
$Qstart_t$	-11.200*** (3.670)	-32.000** (13.200)	-6.520** (2.580)	-25.500* (14.400)	-152.000* (79.900)	-257.000*** (91.700)
$\Delta TSY_t^{Issuance}$	0.086*** (0.011)	0.111*** (0.020)	0.069*** (0.009)	0.042** (0.017)	-0.013 (0.069)	0.178 (0.155)
ΔTGA_t^{Other}	0.026** (0.010)	0.051* (0.026)	0.023** (0.010)	0.028 (0.021)	0.407*** (0.094)	0.638*** (0.216)
$\Delta SOMA_t$	-0.523*** (0.152)	-1.460** (0.688)	-0.436*** (0.160)	-1.020* (0.612)	-3.130** (1.430)	0.929 (2.330)
Constant	-0.391*** (0.119)	-0.738*** (0.195)	-0.313*** (0.099)	-0.415*** (0.159)	0.658 (0.646)	-0.519 (2.140)
N	933	930	933	930	902	837
R ²	0.311	0.288	0.242	0.198	0.243	0.365

Notes: This table shows the regression results of the quarter-end dummies, different components of TGA fluctuations, SOMA fluctuations on daily changes in various intermediation spreads. The dependent variables are as follows: daily changes in the SOFR–IOR spread (Column 1), daily changes in the GCF repo–IOR spread (Column 2), daily changes in the Triparty (TGCR) repo–IOR spread (Column 3), daily changes in the GCF–TGCR repo spread (Column 4), daily changes spread between the overnight implied dollar rate by swapping the ECB deposit rate and the Fed IOR (Column 5), and daily changes in the spread between the overnight implied dollar rate by swapping the BOJ deposit rate and the Fed IOR (Column 6). The independent variables are as follows: $Qend_t$, a dummy variable indicating the last business day of the quarter; $Qstart_t$, a dummy variable indicating the first business day of the quarter; ΔTGA_t^{Other} , daily changes in TGA balance unrelated to net Treasury issuance; $(\Delta TSY_t^{Issuance})$, net treasury issuance; and $\Delta SOMA$, daily changes in the Fed portfolio holdings of Treasury securities. Robust standard errors are reported in parentheses with significance levels denoted by *p<0.1; **p<0.05; ***p<0.01.

Table A5: Impacts of Quarter-Ends, Different Components of TGA, and SOMA Fluctuations on Intermediation Activities

	<i>Dependent variable:</i>						
	ΔRSV_t	ΔRRP_t	ΔRP_t	$\Delta NRRP_t$	ΔFX_t	$\Delta Deposit_t$	$\Delta TSY_t^{outright}$
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
$Qend_t$	−29.100*** (7.470)	−11.400 (7.180)	−31.700*** (4.960)	20.300*** (5.130)	11.400*** (3.170)	−3.440 (4.260)	3.850 (2.870)
$Qstart_t$	41.500*** (5.450)	−7.690 (5.110)	0.515 (4.170)	−8.200** (4.150)	−8.270** (3.290)	28.900*** (4.410)	−0.626 (1.500)
ΔTSY_t^{Issue}	−0.087* (0.053)	0.118*** (0.040)	−0.008 (0.033)	0.126*** (0.037)	0.004 (0.018)	0.139*** (0.046)	0.039*** (0.014)
ΔTGA_t^{Other}	−0.232*** (0.045)	−0.127*** (0.029)	−0.116*** (0.027)	−0.011 (0.027)	0.045*** (0.015)	−0.128*** (0.045)	0.071*** (0.012)
$\Delta SOMA_t$	0.627** (0.308)	−0.926*** (0.284)	−0.258 (0.256)	−0.667*** (0.240)	−0.217* (0.118)	−0.647*** (0.220)	−0.120** (0.060)
Constant	−0.848 (0.628)	−0.673 (0.480)	0.279 (0.421)	−0.952** (0.408)	0.188 (0.233)	−0.874 (0.647)	0.182 (0.207)
N	932	932	932	932	932	932	932
R ²	0.148	0.074	0.111	0.098	0.070	0.096	0.048

Notes: This table shows regression results of one-day changes in the TGA account unrelated to net Treasury issuance (ΔTGA_t^{Other}), net treasury issuance (ΔTSY_t^{Issue}), net SOMA purchase ($\Delta SOMA_t$) on daily changes in the U.S. GSIBs intermediation activities. The dependent variables are as follows: changes in reserves (Column 1), changes in dollar reverse repos (Column 2), changes in dollar repos (Column 3), changes in net dollar reverse repos, or the difference between reverse repos and repos in dollars (Column 4), changes in dollar lending in the FX swap market (Column 5), changes in dollar deposits (Column 6), and changes in outright Treasury holdings (Column 7). $Qend_t$ is a dummy variable indicating the last business day of the quarter, and $Qstart_t$ is a dummy variable indicating the first business day of the quarter. Robust standard errors are reported in parentheses with significance levels denoted by *p<0.1; **p<0.05; ***p<0.01.

Table A6: Comparisons of Outright versus Repo-financed Treasury Holdings

	<i>Dependent variable:</i>		
	ΔTSY_t^{all}	$\Delta TSY_t^{outright}$	$\Delta TSY_t^{fin.}$
	(1)	(2)	(3)
$Qend_t$	-0.612 (2.940)	3.850 (2.870)	-4.470** (1.900)
$Qstart_t$	-1.480 (1.800)	-0.626 (1.500)	-0.852 (1.420)
ΔTSY_t^{Issue}	0.071*** (0.016)	0.039*** (0.014)	0.032** (0.012)
ΔTGA_t^{Other}	0.063*** (0.013)	0.071*** (0.012)	-0.007 (0.009)
$\Delta SOMA_t$	-0.306*** (0.095)	-0.120** (0.060)	-0.186** (0.085)
Constant	0.159 (0.223)	0.182 (0.207)	-0.023 (0.149)
N	932	932	932
R ²	0.052	0.048	0.034

Notes: This table shows regression results of one-day changes in the TGA account unrelated to net Treasury issuance (ΔTGA_t^{Other}), net treasury issuance (ΔTSY_t^{Issue}), net SOMA purchase ($\Delta SOMA_t$), and quarter-end dummies on daily changes in Treasury holding-related positions. The dependent variables are as follows: ΔTSY_t^{All} , daily changes in total Treasury holdings of U.S. GSIBs, including outright holdings and repo-financed Treasury holdings (Column 1); $\Delta TSY_t^{outright}$, daily changes in outright Treasury holdings (Column 2); and $\Delta TSY_t^{fin.}$, daily changes in repo-financed Treasury holdings (Column 3). $Qend_t$, is a dummy variable indicating the last business day of the quarter, and $Qstart_t$ is a dummy variable indicating the first business day of the quarter. Robust standard errors are reported in parentheses with significance levels denoted by *p<0.1; **p<0.05; ***p<0.01.