



# A Note from the AB Fixed Income Trading Desk

Thoughts from Our Senior Portfolio Managers

## Did Someone Repo My Cash?

*"Life is not a matter of holding good cards, but sometimes, playing a poor hand well."* —Jack London

The government finally reopened last week. Despite ending a historic long shutdown, economic data remains sparse, and other corridors of Washington gained the ear of market participants. The deluge of Fed speak following the Federal Open Market Committee revealed independent views on monetary policy as well as some less traditional topics. Mainly, it was Dallas Fed President Lorie Logan that made headlines stating the federal funds rate (FFR) hasn't been accurately representing the pressure building in funding markets. Her suggestion is other funding rates like the secured overnight financing rate (SOFR)—not the FFR—should serve as the Fed's primary benchmark in gauging monetary policy.

At the same time, the Fed's decision to end quantitative tightening (QT) has sparked new questions about the health of the funding markets (often referred to as repo markets), where cash and collateral flow through the system's plumbing. In this iteration of the note, we will unpack how funding markets work, why Logan may be justified in her comments and what risks could be lying under the hood.

## Key Takeaways

- The government reopened, ending the longest shutdown in history.
- Early signs of repo imbalances—alongside the end of QT—pulled investor focus to funding markets.
- The Fed has tools to maintain stability; still, pockets of pressure are likely in the weeks ahead.

## Recent Market Events and Data Releases (November 3, 2025–November 14, 2025)

Corporate earnings have peaked with most of the largest companies having reported. Despite that, reports from issuers in the high-yield market remain in full swing. Outside corporates, the market moving events were as follows:

**"Open for Business":** The record-breaking 43-day government shutdown finally ended. Funding is in place through January 30, and the economic data pipeline is restarting. Some missed October reports may not be backfilled while others are likely to be smoothed or consolidated.

**Institute for Supply Management Check-In: Manufacturing** for October came in at **48.7**, continuing to signal contraction. Meanwhile, **Services** showed some green shoots and printed **52.4** as demand held up. However, the employment component slipped to **48.2**.

**University of Michigan Consumer Sentiment Index:** Headline confidence **fell to 50.3**, reaching the second-lowest print on record. One-year inflation expectations ticked up to 4.7%; long-run held around 3.6%.

**Yields:** Treasury yields were relatively unchanged over the period, staying within a window of roughly 5 basis points, while credit spreads in both investment-grade and high yield also hovered in a tight band.

## Portfolio Manager Perspectives

**What is Logan's qualm?** The Fed currently uses the FFR to guide funding conditions and monetary policy, but the Fed funds market has largely devolved into a low volume, idiosyncratic trade that is no longer representative of broader funding conditions. SOFR, with an average volume of \$4.5 trillion per day, would serve as a cleaner benchmark.

**What's a repo, anyway?** A repurchase agreement (repo) is essentially a short-term, collateralized loan. One party sells a Treasury bill (or similar collateral) to another with an agreement to repurchase it—often the next day—at a slightly higher price. It's the foundation of modern financial funding: how banks finance their balance sheets and how leveraged investors borrow cash efficiently.

**What's going on now?** Recently, SOFR—the most visible repo rate—spiked above the Fed's upper policy bound, raising eyebrows about potential liquidity strains or even a repeat of the 2019 “repo-colyse.” This can happen during heavy settlement periods like quarter-end and the rate has since fallen back into bands, but this has caught the attention of the FOMC and select market participants.

The Fed sets a target range for short-term rates, defining a lower bound and an upper bound to guide where it wants overnight funding costs to trade. As of the last FOMC meeting, that range was 3.75% to 4.00%. Here's how the Fed enforces those boundaries (*Display 1*):

**Lower Bound (3.75%):** Reverse Repo Facility (RRF)—This is where the Fed effectively borrows excess cash from the market, paying an interest rate that acts as the floor. If there's too much cash sloshing around, investors can park it at the Fed for 3.75%, preventing market rates from falling below that level.

**Upper Bound (4.00%):** Standing Repo Facility (SRF)—This is the mirror image. The Fed lends cash at a set rate: 4.00%—to keep borrowing costs from shooting too high. If SOFR rises above the ceiling, banks should, in theory, tap this facility, which pressures market rates lower through competition.

**So, what's the problem?** Despite **some** usage of the SRF, SOFR has breached the upper bound. Why? It's about optics and transparency. The SRF is public—tapping it comes with stigma. In funding markets, perception matters. A bank that borrows from the Fed risks signaling it might be facing liquidity trouble. So instead, institutions often choose to pay above-market rates in private repo transactions just to stay under the radar.

**Is there a cash crunch?** Not quite—but there's a growing imbalance between cash and collateral, mainly between Treasuries and mortgage-backed securities (MBS). When you see the RRF (*Display 2*) swell, it means lenders are content to earn the lowest rate in the system, suggesting cash is abundant. That's been true as money-market fund (MMF) assets hit record highs—the primary source of overnight cash (*Display 3*). But when SOFR creeps above the upper bound or banks start using the SRF, it signals the opposite: too much collateral, not enough cash.

**Why the pressure on collateral?** It's a balance-sheet triangle between the banks, the government and the Fed. The US Treasury continues to issue massive amounts of new debt—over \$35 trillion outstanding and \$3–4 trillion in new issuance annually (*Display 4*). The Fed, through QT, has stepped back as a major buyer, shrinking its balance sheet (*Display 5*). That leaves the rest of the market holding more Treasuries and financing them in repo markets, which increases their funding needs. The result is more collateral flooding the system just as cash availability becomes constrained.

**But aren't MMFs flush with cash?** They are—but that cash isn't always available for overnight lending. As the Fed cuts rates (good for bonds, not for cash), MMFs are shifting from overnight lending into buying T-bills outright, locking in yields for longer. That move is effectively neutral for the system but removes some of the “recyclable” overnight cash banks rely on.

**Don't banks still have plenty of reserves?** They do—but those reserves are starting to decline. Banks hold cash at the Fed as part of post-global financial crisis capital rules—what the Fed calls “ample reserves.” But as banks soak up excess Treasury supply, they're starting to tap those reserves. However, as a share of GDP, reserve levels remain abundant or nearly twice that of 2019 levels. (*Display 6*).

**Does this tie back to QT?** Only indirectly. The end of QT was telegraphed well in advance, part of a gradual unwind once liquidity looked sufficient. The Fed has been careful not to overtighten. It's also reinvesting principal from its MBS holdings into T-bills—about \$15 billion per month—to absorb some of the excess collateral.

**What to look for?** (1) Large and sustained usage of the SRF. (2) Prolonged periods of SOFR setting above the Fed's upper bound (leaky ceiling). (3) Heavy US Treasury issuance. (4) Quarter-end and year-end reporting periods when banks reduce repo for balance sheet purposes.

**What if things break?** If conditions deteriorate, the Fed has tools at the ready. (1) It can use MBS principal repayments to buy back T-bills, pulling collateral out of the system. (2) It can lower the SRF rate (the ceiling) without waiting for a policy meeting, invoking interest in cheaper financing. (3) And, if needed, it could implement targeted reserve management operations—like mini-QE—focused on the front end of the curve rather than across maturities, which would buy excess collateral out of the system.

**What keeps us up at night?** A sharp drop in MMF assets. If investors move out of MMFs quickly, the cash base in the system could shrink just as collateral remains high, creating the classic conditions for stress in funding markets. Inadequate access to funding for the levered community could snowball into a broader market phenomenon (forced selling to raise cash).

**Bottom line:** We expect liquidity to remain constrained in the weeks ahead, but the Fed knows the playbook. Officials are closely monitoring market plumbing and the tools to stabilize conditions are well understood. For now, the system isn't breaking—but it's a reminder that even in calm markets, the pipes underneath are never fully out of sight.

## Investment Implications

While funding issues may bubble up, we do not expect them to spiral. Our core guidance is unchanged.

- **Ultra Short-Term Bond.** Hiccups in repo can create brief alpha opportunities, but the more durable opportunity may be to move excess cash from money markets into vehicles that can earn a yield above cash and capture capital appreciation as the Fed continues to cut front-end rates.
- **Core-Plus Bond.** Short- to intermediate-term yields still can offer the best risk-adjusted balance across outcomes. A softer labor market could pull the belly of the curve lower, while our base case is for attractive, range-bound yields. Core-plus also provides additional income over governments and can add a meaningful ballast to equity risk.
- **High Yield.** We remain constructive on credit, acknowledging softness at the margins for the lowest-rated, most challenged issuers. With yield-to-worst that rivals long-run equity returns but with much less volatility, we continue to implore investors to trim equity over weights and re-allocate to high yield. It helps keep expected returns intact and can soften drawdowns.

As government agencies reopen and release more data, there will be plenty to discuss in the weeks ahead.

On behalf of the team,

Scott DiMaggio, Gershon Distenfeld, Matt Sheridan, Fahd Malik, Will Smith, John Taylor, Serena Zhou, Tim Kurpis, Christian DiClementi, Sonam Dorji and AJ Rivers

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## European Tariff Scenarios

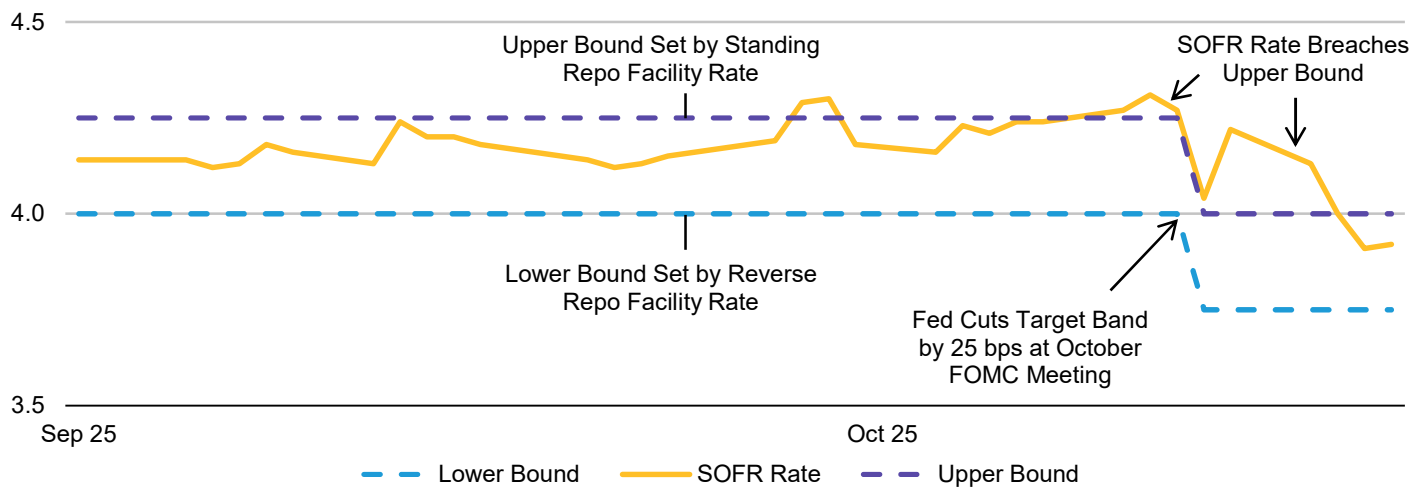
2025 Forecasts	Counterfactual No Tariffs at All (Percent)	Upside No Universal Tariffs (Percent)	Current Situation 10% Universal Tariffs (Percent)	April 2–9 20% Universal Tariffs (Percent)	Downside 30% Universal Tariffs (Percent)
Growth (YoY)	1.10	0.80	0.06	0.30	–0.60
Inflation (Annual)	2.00	1.80	1.60	1.70	1.40
ECB Deposit Rate (Year-End 2025)	2.00	1.75	1.75	1.75	1.00
Recession Probability	30.00	40.00	60.00	70.00	90.00

## US Economic Scenarios

Economic Outcome	Description	Probability (Percent)
<b>Hard Landing/Deep Contraction</b>	Either an external shock occurs, or business-cycle dynamics deteriorate sharply. Growth slows rapidly and central banks have to act aggressively to support growth.	20
<b>Soft Landing/Mild Contraction</b>	Growth slows, labor markets weaken and central banks hurry to get back to neutral. The magnitude of the slowdown defines the terminal rate and inflation expectations determine the speed with which it is reached.	35
<b>Rebalancing</b>	Both inflation and growth approach trend levels slowly, leaving the Fed comfortable easing policy slowly and remaining restrictive well into 2025, with cuts of 25 basis points at some, but not all, meetings until the policy hits neutral in late 2025 or 2026.	35
<b>Stagflation</b>	The economy slows, but inflation expectations rise, trapping the Fed between a rock and a hard place.	5
<b>No Landing</b>	The economy performs despite headwinds, and inflation stays elevated enough to keep the Fed on hold for some time to come.	5

### Display 1: Repo Rates Breached the Fed's Upper Bound

Secured Overnight Financing Rate



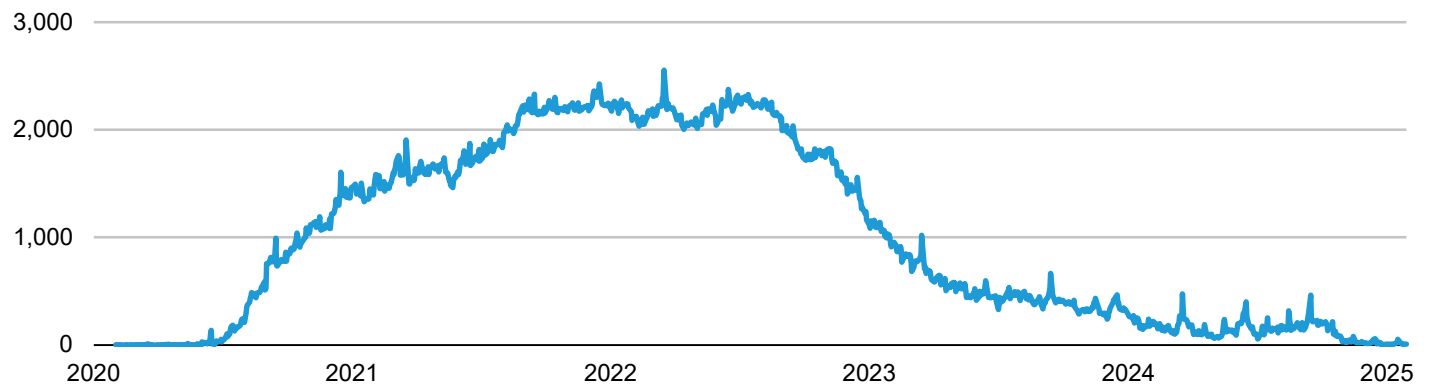
bps: basis points

As of November 14, 2025

Source: Bloomberg and US Bureau of Labor Statistics

### Display 2: The Reverse Repo Facility Balance Is Approaching Zero

NY Fed Reverse Repo Data by Counterparties Amount of Accepted Bids

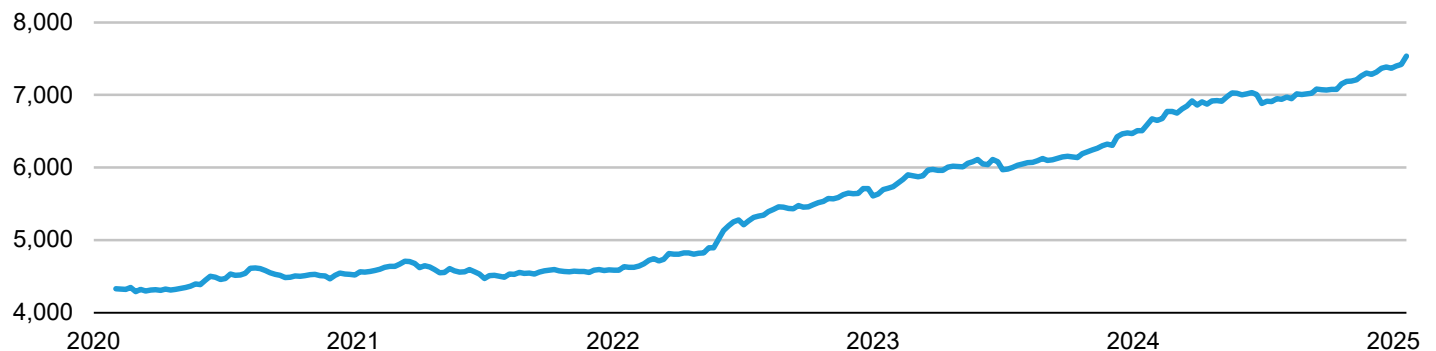


As of November 14, 2025

Source: Bloomberg

### Display 3: Money-Market Assets Have Hit All-Time Highs

Money-Market Fund Assets

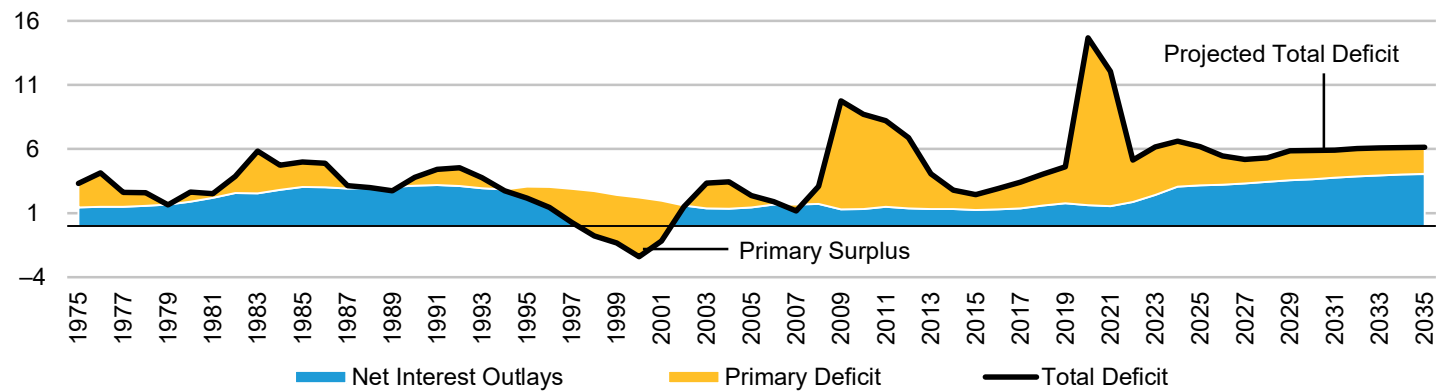


Through November 14, 2025

Source: Bloomberg High Yield Index

#### Display 4: The US Government Is Expected to Run Continued Budget Deficits

Percentage of GDP

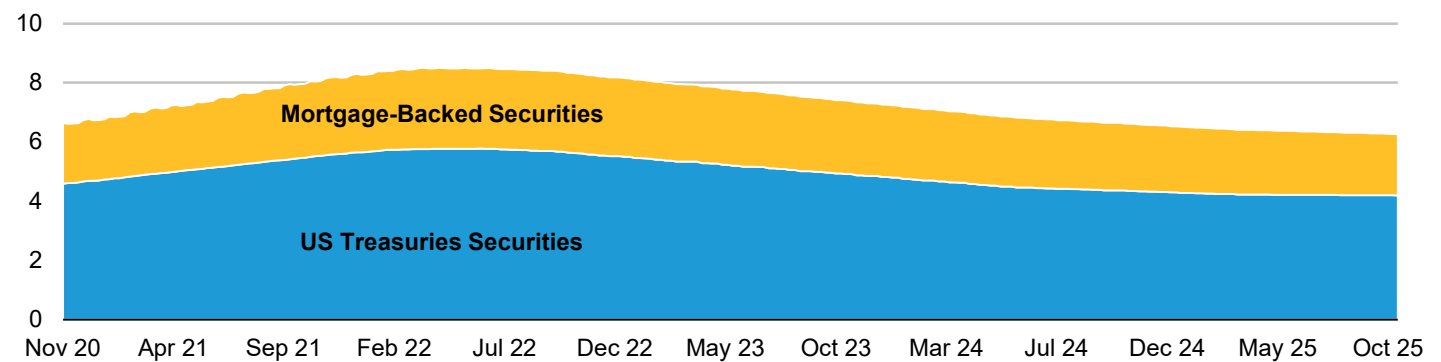


Through November 14, 2025

Source: Bloomberg and S&P 500

#### Display 5: The Federal Reserve Is Shrinking Its Balance Sheet

Federal Reserve Balance Sheet (Percent)

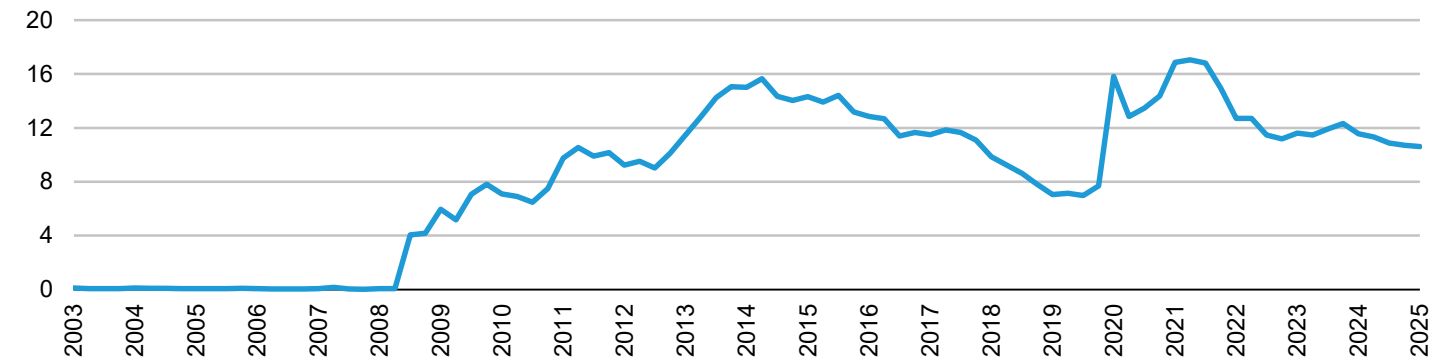


As of November 14, 2025

Source: Bloomberg

#### Display 6: RRF Levels Remain Abundant or Nearly Twice That of 2019 Levels

Reserve Levels as Share of GDP



As of June 30, 2025

Source: Bloomberg

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## Investment Risks to Consider

The value of an investment can go down as well as up, and investors may not get back the full amount they invested. Capital is at risk. Past performance does not guarantee future results.

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IMA-841285-2025-11-17