UNITED STATES: WILL EASING LEVERAGE REQUIREMENTS STIMULATE DEMAND FOR TREASURIES?

WAYS TO RELAX THE SLR STANDARD

Balance sheet freed up in Q1 2025 by a reduction in the eSLR requirement from 5% to 3%+50%*method 1 G-SIB surchage

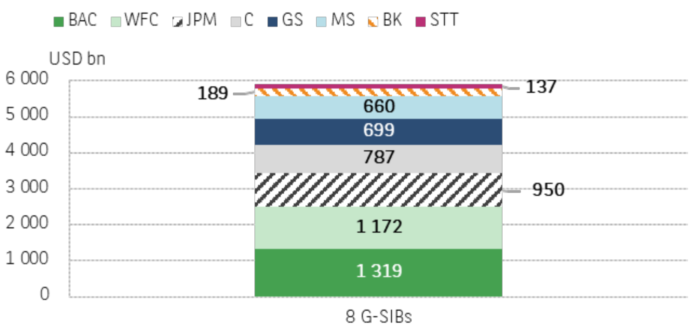

CHART 1 SOURCES : SNL FINANCIAL, FED, FSB, BNP PARIBAS CALCULATIONS

Improvement in SLR ratios enabled by a reduction in the ratio denominator

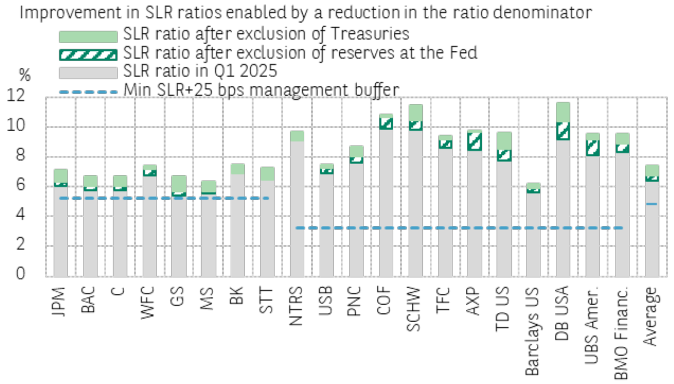

CHART 2 SOURCES : SNL FINANCIAL, BNP PARIBAS CALCULATIONS

In the coming months, a relaxation of the Basel leverage ratio[1] (Supplementary Leverage Ratio, SLR) could be proposed in the United States. The aim is to ease the balance sheet constraints on primary dealers, most of which are subsidiaries of large banks[2], and thereby improve intermediation conditions in the US Treasury market.

Various options for easing the rules could be considered

A first option would be to reduce the enhanced SLR requirements (eSLR) specific to global systemically important banks (G-SIBs) and their deposit-taking subsidiaries (5% and 6% respectively) to the level of the Basel recommendation (i.e., 3% plus a buffer set at 50% of the method 1 G-SIB surcharge[3]). Under this assumption, the weighted average requirement for the eight US G-SIBs would be 3.86%. Given their Tier 1 capital stock in Q1 2025, this first option would allow them collectively to increase their exposure to risk-free assets by a maximum of around USD 6 trillion (Chart 1, representing an increase of nearly 30% of their overall exposure).

A second option would be to deduct reserves held with the Federal Reserve and US Treasuries from the SLR ratio denominator. On average, this exclusion would reduce the leverage exposure (ratio denominator) of the 20 banking groups subject to the SLR requirement by 13% and improve their SLR ratio by 100 basis points (Chart 2). As the outstanding amount of these risk-free assets would no longer have any effect on the SLR ratio, this option would in theory allow unlimited holdings.

A measure to support Treasury market stability

However, this relief alone should not encourage banks to buy Treasuries on a large scale. This could increase G-SIB capital surcharges (which are linked to balance sheet size), increase transformation and interest rate risks, conflict with their internal market risk exposure limits and profitability targets, or even weaken their liquidity position.

In our view, the challenge of this easing will not be so much to place the additional paper issued by the US Treasury on banks' balance sheets in order to compensate for investors' lack of appetite, but rather to strengthen this appetite by reassuring investors about banks' ability to play their role as intermediaries, particularly in the event of a shock.

1 The SLR requirement, set at 3%, expresses the bank's Tier 1 capital amount as a ratio of its total exposure, which includes all balance sheet assets (some of which are recorded at their gross values) and a simplified measure of off-balance sheet commitments. The leverage exposure of banks predominantly engaged in custody, safekeeping and asset servicing activities (e.g., Bank of New York Mellon, State Street and Northern Trust) excludes a large portion of their reserves held at central banks.
2 Only the largest bank holding companies (those with consolidated balance sheets exceeding USD 250 billion or with at least USD 75 billion in non-bank assets, weighted short-term wholesale funding or off-balance sheet exposure) and their main deposit-taking subsidiaries are subject to the SLR.
3 In the United States, the capital surcharge imposed on G-SIBs is determined using two methods: the Financial Stability Board method (method 1) and the more stringent Federal Reserve method (method 2).

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