Market Trends 2018/19: Commercial Paper

A Lexis Practice Advisor® Practice Note by Jerry Marlatt, Mayer Brown LLP

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Post-crisis developments in the commercial paper market have led to a significant restructuring of the market and a reduction in the use of commercial paper to securitize assets. This market trends article provides an overview of the commercial paper market and examines the deal structure and process, deal terms and legal and regulatory trends.

For a general overview of commercial paper programs, see Commercial Paper Programs.

Deal Structure and Process

Historical Background

Commercial paper was the name given to notes, drafts, bills of exchange, and bankers' acceptances representing trade acceptances or trade receivables given by buyers to merchants and manufacturers in exchange for merchandise and goods. These documents typically had short-term tenors, usually not more that 30 or 60 days. In turn, the merchants and manufacturers would sell the notes at a discount to investors and dealers in the money market, a market for short-term instruments such as Treasury notes and bills of exchange. The proceeds were used as working capital to finance the production of or an inventory of merchandise and goods.

Commercial paper developed perhaps as early as the late 1700s in New York as the economy of the new country struggled to develop in an environment where bank credit was scarce. The use of commercial paper expanded significantly in the mid-1800s in New York and other U.S. financial centers when the industrial sector was booming and high immigration rates were driving a surging economy. This practice of discounting paper evolved into the issuance of short-term promissory notes by merchants and manufacturers to professional investors and dealers to finance the notes they held from buyers. Financial institutions also began issuing commercial paper notes to fund their short-term requirements, including their purchase at discount of commercial paper in the marketplace. The notes were issued as non-interest bearing, principal-only notes sold at a discount to the face amount. As the issuance of commercial paper continued to develop, the market for commercial paper began to concentrate in financial institutions.

The money market has always been a separate market from the securities market for stocks and bonds. To this day, the commercial paper trading desks at banks are usually separate from the trading desks for securities and staffed by different groups of people. This is true perhaps because commercial paper is viewed as more in the nature of a liquid trade receivable than an investment security.

Commercial paper held by banks has always been viewed as highly liquid. In fact, during the Depression, legislation was drafted to permit Federal Reserve Banks to issue notes up to the amount of the notes, drafts, bills of exchange, and bankers' acceptances they held.

Treatment under the 33 Act

By the time of the adoption of the Securities Act of 1933 (the 33 Act), the commercial paper market was well-developed, but it was an anomaly in the world of corporate securities. Commercial paper was typically short-term, predominantly with 7 to 10-day maturities, although sometimes with longer maturities out to nine months. The proceeds of the sale of commercial paper notes continued to be used as working capital to finance wages and other production costs and inventory. Commercial paper was often repaid by the issuance of new commercial paper and this revolving nature of the obligation, together with the short tenors, contrasted with typical corporate securities.

The short-term, revolving nature of commercial paper was not conducive to the securities registration scheme contemplated by the 33 Act. It was simply not practical to prepare and submit a registration statement for notes that were to be issued every 7 to 10 days. And the registration fees for such constant repeat issuance would have been prohibitive. Registration fees for securities were to be based on the principal amount of securities to be sold without regard to their maturity. Moreover, as noted above, the commercial paper market had historically been viewed as separate and distinct from the securities market.

These characteristics of commercial paper led the Board of Governors of the Federal Reserve System (the Federal Reserve) to request Congress to carve out commercial paper from the registration requirements of the 33 Act. Commercial paper is exempt from registration under the 33 Act by the terms of Section 3(a)(3), which exempts "any note, draft, bill of exchange, or banker's acceptance which arises out of a current transaction or the proceeds of which have been or are to be used for current transactions, and which has a maturity at the time of issuance of not exceeding nine months, exclusive of days of grace, or any renewal thereof the maturity of which is likewise limited." Commercial paper is, however, subject to the anti-fraud provisions of the 33 Act.

Investors in the commercial paper market at the time of enactment of the 33 Act were usually banks, dealers, other financial institutions, and sophisticated individual investors. This was not a market for retail investors. And the high turnover rate of commercial paper required a continuous market presence of investors who were making credit decisions about an issuer as often as weekly, if not daily, as its commercial paper notes rolled at maturity.

Current Market Insights

Nonfinancial Issuers

Issuers of commercial paper notes today continue to be merchants, manufacturers, finance companies, and financial institutions with the addition of some structured finance issuers. The total market is around $1.2 trillion outstanding with seasonal fluctuations; the highest outstanding are typically over year-end.

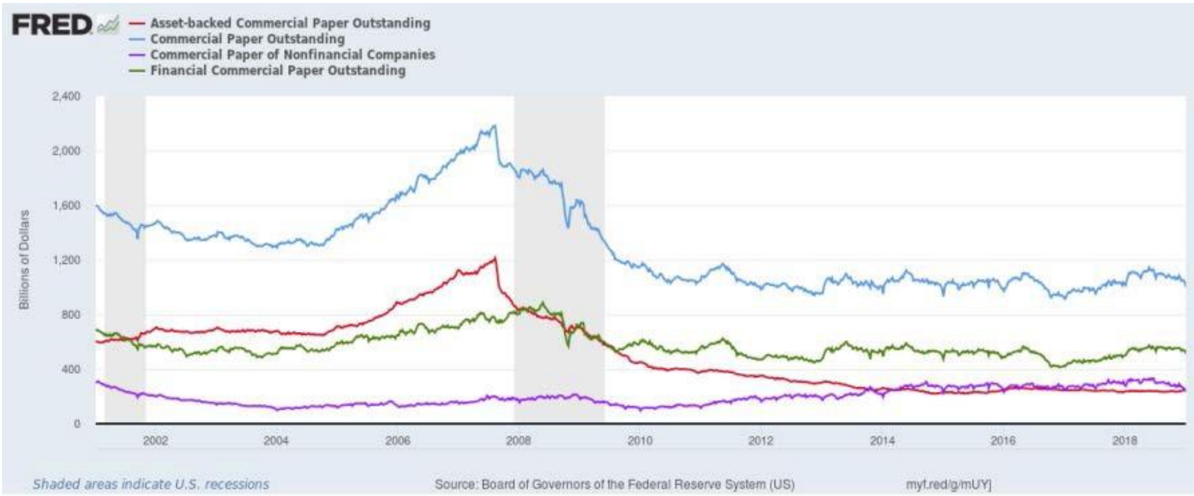
Merchants and manufacturers continue to use commercial paper to fund receivables from buyers of their products, inventory, raw materials, supplies, wages, construction costs, but not permanent financing or capital equipment. Nonfinancial entities issue about 20% of commercial paper outstandings.

Financial Issuers

Financial issuers of commercial paper notes tend to be money center banks, finance companies, and foreign banks. These issuers represent about 50% of market outstandings. Financial institutions use the proceeds as working capital, including to fund loans with maturities of up to five years.

Asset-Backed Commercial Paper

The most common structured finance issuers of commercial paper are asset-backed commercial paper conduits (ABCP Conduits), but over the last 20 years, many other asset-backed issuers have utilized commercial paper, including structured investment vehicles (SIVs) and issuers of collateralized debt obligations (CDOs). Asset-backed commercial paper (ABCP) outstandings came to rival the traditional commercial paper market. By 2007, ABCP outstandings stood at $1.2 trillion and total commercial paper outstandings were around $2.2 trillion. (See the chart below.) However, many of these asset-backed commercial paper issuers failed during the financial crisis due to liquidity concerns. Unlike traditional commercial paper issuers, these structured issuers were funding long-term asset-backed securities with commercial paper and when the market for those securities seized up in the crisis, they were unable to roll their outstanding commercial paper at maturity, leading to a fire sale of assets into rapidly declining markets. Many of these asset-backed issuers were wound down and the losses were absorbed by their sponsors (many of which were financial institutions), but the losses to commercial paper investors nevertheless were staggering. Today, issuance of commercial paper by structured issuers has shrunk back to those issuers funding short-term trade receivables or those issuers with solid liquidity lines of credit to cover any mismatch between the assets funded and the commercial paper issued. They represent about 20% of commercial paper outstandings today and no longer dominate the market. We discuss ABCP in more detail in the following section.



Deal Terms

The Federal Reserve Board maintains extensive data on commercial paper issuance. Current data on commercial outstandings can be found at http://www.federalreserve.gov/releases/cp/ and historical data can be found at https://fred.stlouisfed.org/search?st=commercial+paper and at https://www.federalreserve.gov/datadownload.

Maturities

Commercial paper tends to have very short maturities. In the table below, 64% of commercial paper is issued with a maturity of less than 21 days. The maturities in the following table as of July 30, 2018, are pretty representative of the commercial paper market generally. Note how heavily the maturities are concentrated in the 1 to 4-day period, nearly 60% of outstanding commercial paper. Maturities tend to extend over the year-end as issuers try to bridge a spike in interest rates in this period.

	Amount 1								Number of issues						
		Days to maturity								Days to maturity					
Period	Total	1 - 4 days	5 - 9 days	10 - 20 days	21 - 40 days	41 - 80 days	81+ days		Total	1 - 4 days	5 - 9 days	10 - 20 days	21 - 40 days	41 - 80 days	81+ days
Annual average															
2017	84,232	52,769	11,730	3,848	6,226	3,133	6,526		3,947	2,270	508	254	396	171	350
2018	82,442	47,708	13,574	3,989	6,051	3,487	7,632		4,042	2,154	566	269	413	205	434
2019*	78,050	43,261	11,656	3,680	6,805	3,939	8,710		3,985	2,041	491	265	481	231	476
Monthly average															
2018-Sept.	81,742	47,474	13,879	3,531	6,071	2,784	8,003		4,125	2,254	614	258	406	182	411
Oct.	80,074	46,858	12,581	3,796	5,582	3,214	8,042		3,894	2,128	507	254	382	197	425
Nov.	75,606	42,604	12,737	4,154	4,951	3,191	7,968		3,760	1,980	540	280	337	179	444
Dec.	67,794	38,519	11,105	3,429	5,419	3,084	6,238		3,361	1,808	466	227	348	160	352
2019-Jan.	77,409	42,702	11,762	3,826	6,466	3,992	8,660		3,951	1,994	496	273	471	234	482
Feb.*	80,742	45,606	11,210	3,063	8,228	3,717	8,918		4,127	2,235	470	230	521	220	452

SOURCE: Board of Governors of the Federal Reserve System (U.S.)
1Millions of Dollars
*Data through February 7, 2019

Rates

The equivalent annual rate of interest paid on commercial paper as of February 7, 2019, is set out in the table below. It is noteworthy how little difference there is in the rate for 1-day commercial paper and 90-day commercial paper. Also note that AA asset-backed issuers pay a premium compared to AA financial issuers, but pay nearly the same rate as AA nonfinancial issuers. This represents perhaps the advantage for financial issuers of having access to the discount window at the Federal Reserve.

	AA nonfinancial							A2/P2 nonfinancial					
Period	1-day	7-day	15-day	30-day	60-day	90-day		1-day	7-day	15-day	30-day	60-day	90-day
Feb. 1	2.35	2.36	2.37	2.40	2.46	2.50		2.62	2.68	2.72	2.76	2.83	2.87
Feb. 4	2.37	2.39	2.41	2.43	2.47	2.50		2.61	2.69	2.71	2.76	2.87	2.99
Feb. 5	2.36	2.37	2.39	2.39	2.43	2.46		2.61	2.70	2.72	2.73	2.80	2.87
Feb. 6	2.36	2.38	2.39	2.45	2.46	2.48		2.64	2.66	2.69	2.76	2.83	2.89
Feb. 7	2.36	2.37	2.37	2.41	2.46	2.49		2.60	2.67	2.71	2.74	2.89	3.05

* Data through February 7.
Note: n.a. indicates that trade data was insufficient to support calculation of the particular rate.

	AA financial							AA asset-backed					
Period	1-day	7-day	15-day	30-day	60-day	90-day		1-day	7-day	15-day	30-day	60-day	90-day
Feb. 1	2.36	2.39	2.40	2.43	2.51	2.57		2.46	2.48	2.48	2.49	2.55	2.61
Feb. 4	2.37	2.38	2.39	n.a.	n.a.	2.53		2.46	2.47	2.51	2.54	2.57	2.60
Feb. 5	2.36	2.37	2.39	2.42	n.a.	2.55		2.45	2.48	2.48	2.50	2.55	2.61
Feb. 6	2.36	2.37	n.a.	2.40	2.45	2.51		2.45	2.49	2.50	2.52	2.55	2.60
Feb. 7	2.36	2.40	n.a.	2.36	2.44	2.50		2.45	2.49	2.49	2.50	2.55	2.59

* Data through February 7.
Note: n.a. indicates that trade data was insufficient to support calculation of the particular rate.

SOURCE: Board of Governors of the Federal Reserve System (U.S.)

Outstandings

The chart below shows commercial paper outstanding by issuer sector for 2018 and early 2019. Note that at the end of June, almost 27% of the total outstanding is from foreign financial institutions, 23% from asset-backed issuers, and 30% from nonfinancial entities. Only 24% is from domestic financial institutions.

		Nonfinancial			Financial				
Period	Total	Total	Domestic	Foreign	Total	Domestic	Foreign	Asset-backed	Other
Monthly-end levels									
2018-July	1,064.2	296.3	232.7	63.6	524.7	256.7	268.0	242.8	.3
Aug.	1,059.8	291.5	231.3	60.2	530.4	255.7	274.7	237.5	.4
Sept.	1,069.6	290.7	232.4	58.3	543.0	264.9	278.1	235.4	.5
Oct.	1,063.8	265.7	211.2	54.5	564.1	265.5	298.5	233.5	.6
Nov.	1,071.3	261.3	211.3	50.0	569.3	263.3	306.0	240.2	.5
Dec.	1,076.1	267.9	206.1	61.8	551.0	252.7	298.3	256.8	.5
2019-Jan.	1,042.0	263.6	193.6	70.0	528.2	233.2	295.0	249.3	.9
Weekly (Wednesday) levels									
Jan. 9	1,073.1	265.3	204.1	61.2	546.8	233.4	313.5	260.4	.5
Jan. 16	1,065.6	263.8	201.2	62.6	542.5	237.7	304.9	258.7	.5
Jan. 23	1,068.6	269.8	206.7	63.2	543.3	237.7	305.6	254.9	.6
Jan. 30	1,078.5	279.1	212.6	66.5	547.2	240.5	306.8	251.4	.8
Feb. 6	1,057.0	273.7	217.4	56.3	532.6	231.2	301.5	250.0	.6

SOURCE: Board of Governors of the Federal Reserve System (U.S.)

Legal and Regulatory Trends

Today commercial paper is sold in book-entry form through the Depository Trust Company. There is virtually no paper-based commercial paper anymore. In 2006, about 20% of commercial paper was sold directly by issuers to investors, often by finance companies, but predominately commercial paper is sold through dealers who purchase as principal and resell to investors. Direct issuers today represent about 20% of the market as indicated by the table below under Directly-placed. There is little secondary market in commercial paper. Given the short-term nature of commercial paper, investors tend to hold commercial paper until maturity. Those investors who find a need for cash generally resell the commercial paper they hold to the dealer who sold it to them.

Period	Total	Nonfinancial			Financial			Asset-backed	Other
		Total	Domestic	Foreign	Total	Domestic	Foreign		
Year-end levels									
2017	1,045.8	294.7	232.6	62.1	511.2	239.9	271.3	239.9	.0
2018	1,076.1	267.9	206.1	61.8	551.0	252.7	298.3	256.8	.5

Period	Financial							Special categories					
	Domestic				Foreign			SEC rule 2a-71		Directly-placed			
	U.S. owned	Foreign bank parent	Foreign nonbank parent	Other	Bank	Other		Tier-1	Tier-2	Nonfinancial	Financial	Asset-backed	Other
Year-end levels													
2017	71.6	79.7	67.4	.0	127.8	128.2		411.1	68.2	35.1	112.7	49.9	.0
2018	76.1	90.5	65.6	.0	166.0	114.5		390.8	73.7	8.3	78.6	31.9	.0

SOURCE: Board of Governors of the Federal Reserve System (U.S.)

Section 3(a)(3)

Commercial paper has been traditionally sold in reliance on the exemption from registration under the 33 Act provided in Section 3(a)(3), but there is a growing movement to issue commercial paper under Section 4(a)(2) of the 33 Act in a private placement even if Section 3(a)(3) would be available. Section 3(a)(3) provides no restriction in the manner of sale or the offerees or purchasers of the notes. Notably, however, the proceeds of commercial paper sold under Section 3(a)(3) must be used for current transactions, a term for which the Securities and Exchange Commission (SEC) has issued many no-action letters, but which basically means operating costs, including wages, raw materials, inventory, and a variety of other current expenses and excludes capital expenses, such as equipment or buildings.

For more information on Section 3(a)(3) exemption, see Section 3(a)(3) Exemption for Commercial Paper.

Current Transactions

The SEC noted in Securities Act Rel. No. 33-4412 (Sep. 20, 1961) that "[t]he legislative history of the Act makes clear that Section 3(a)(3) applies only to prime quality negotiable commercial paper of a type not ordinarily purchased by the general public, that is, paper issued to facilitate well recognized types of current operational business requirements and of a type eligible for discounting by Federal Reserve banks." The SEC went on to reference Regulation A as promulgated by the Board of Governors of the Federal Reserve System prior to enactment of the Securities Act of 1933, which governed advances and discounts by Federal Reserve banks, and stated that "a Federal Reserve bank may discount for a member bank a negotiable note, draft, or bill of exchange, bearing the endorsement of a member bank, which has been issued, or the proceeds of which are to be used in producing, purchasing, carrying or marketing goods or in meeting current operating expenses of a commercial, agricultural or industrial business, and which is not to be used for permanent or fixed investment, such as land, buildings, or machinery, nor for speculative transactions in securities…" The SEC stated further that "[w]hat is a current transaction is, of course, a question which must be considered in light of the particular facts and business practice surrounding individual cases."

What qualifies as a current transaction varies by industry. For example, the purchase of nuclear fuel may constitute a current transaction for an electric power company and granting a loan for a term not exceeding five years may constitute a current transaction for a bank. For a broker-dealer, a current transaction would be "(i) financing margin loans for its customers; (ii) carrying inventories of direct federal obligations and obligations of federal government agencies; (iii) carrying inventories of money market instruments with maturities of not more than one year from their date of purchase; (iv) financing amounts due to the

Company from other broker-dealers and financial institutions arising in the ordinary course of Company's business from fails to deliver and securities borrowed; and (v) payment of the Company's current operating expenses, such as payroll, employee travel, rent and similar items. None of the proceeds are used to finance any permanent or fixed investment, such as land, buildings, equipment or other capital expenditures, nor are proceeds used to finance any securities inventory not described in (ii) or (iii) above." See SEC no action letter issued to Robert W. Baird & Co. Incorporated (Feb. 26, 1986).

Rule 144A

However, as noted above, proceeds from 3(a)(3) commercial paper must be used for current transactions and may not be used, for example, to fund the acquisition of a company. Where short-term funding is desirable for an acquisition or other capital expense, this prohibition led companies to turn to the issuance of short-term notes under Section 4(a)(2) of the Securities Act, which enables private placements. Such notes came to be called 4(a)(2) commercial paper and for such commercial paper, there is no limitation on use of proceeds. Initially, 4(a)(2) commercial paper was not as attractive to investors as 3(a)(3) commercial paper because as a private placement, the notes were restricted securities and therefore had to be issued at a steeper discount. By the early 2000s, however, the 4(a)(2) commercial paper market had grown to such an extent that very little, if any, pricing distinction remained with 3(a)(3) commercial paper.

4(a)(2) commercial paper is generally sold to institutional accredited investors under Regulation D or to qualified institution buyers under Rule 144A. Over time, many programs have moved to sales solely to qualified institutional buyers. This is due primarily to the JOBS Act related amendments to Regulation D with respect to "bad actors."

Section 3(a)(2)

Banks and U.S. branches of foreign banks can also issue short-term notes without registration under the exemption provided by Section 3(a)(2) of the 33 Act for securities issued or guaranteed by banks. Similar to Section 3(a)(3), Section 3(a)(2) provides no restriction on the manner of sale of the notes or on the purchasers of the notes, unlike Section 4(a)(2) [Note that there may be restrictions under the rules of the Office of the Comptroller of the Currency (OCC) for those banks or foreign bank branches that are subject to regulation by the OCC]. Nonbank issuers may also rely on Section 3(a)(2) to issue short-term notes if they obtain a guarantee or letter of credit from a bank or U.S. branch of a foreign bank. This practice was more prevalent in the 1990s than today. Under current capital requirements, the capital charge for the letters of credit discourages their use for short-term note programs.

ABCP

Conduits, SIVs, Foreign Banks

Asset-backed commercial paper began to emerge in the 1970s as investment banks challenged commercial banks by providing commercial paper financing for trade receivables as an alternative to revolving credit facilities at commercial banks. ABCP conduits are a form of securitization. Investment banks established special purpose entities (SPE) that purchased trade receivables from merchants and manufacturers using the proceeds of commercial paper issued by the SPE. The commercial paper was typically rolled over at maturity, but ultimately the commercial paper was repaid by the receipts on the trade receivables. Losses on the trade receivables were covered by purchasing the receivables at a discount and any excess recoveries over losses and financing and operating costs were returned to the originating merchant or manufacturer. The sponsoring investment bank typically acted as a dealer for the commercial paper and as the administrative agent for the SPE. The administrative agent was responsible for assessing the credit risk of the receivables and negotiating pricing for the purchase of the receivables. To fend off disintermediation by investment banks, U.S. commercial banks and foreign banks began to establish ABCP conduits to protect their customer relationships by providing commercial paper financing to their institutional banking customers. At the time of the financial crisis e.g., Citibank had 16 ABCP conduits.

Rise and Fall

As this ABCP sector matured, the ABCP conduits began to fund longer term assets in addition to trade receivables and to issue a mixture of commercial paper and medium-term notes to finance the purchase of the assets. This practice evolved into the creation of SIVs, the failure of which in 2007 was a triggering event for the financial crisis. The SIVs were created to arbitrage the spread between the return on various asset-backed securities (ABS) held as assets and the cost of funding such assets with medium-term notes and commercial paper. SIVs were designed to liquidate their assets to repay maturing obligations in the event the medium-term notes or commercial paper could not be rolled. In the summer of 2007, the market for ABS seized up and liquidity was unavailable. Many SIVs failed along with a number of ABCP conduits.

European Commercial Paper

While a commercial paper market developed in the United States in the nineteenth century, a market for commercial paper in Europe did not develop until the 1980s. Today the European commercial paper (ECP) market is approximately €820B in outstanding amount. The market is dominated by financial institutions, which constitute about 80% of outstandings. Some statistics can be found at: http://www.ecb.europa.eu/stats/financial_markets_and_interest_rates/step for programs that qualify for STEP (Short-Term European Paper).

The Role of Money Market Funds

In the early 1970s, financial regulators imposed limits on interest that could be paid on deposit accounts. This action led depositors to turn to money market funds, which were not subject to such limitations, for higher interest rates. In turn, banks turned to the commercial paper market to obtain funds to replace lost deposits. And money market funds purchased more commercial paper with the increased funds received from depositors. This symbiotic relationship led to even more dramatic growth of money market funds in the late 1970s and early 1980s as the limitation on interest paid on bank deposits became more important with surging interest rates due to a high inflation rate. This growth in money market funds led to significant growth in commercial paper amounts outstanding. This growth was accompanied by a significant decline in the direct issuance of commercial paper to investors and increased reliance on dealer-placed commercial paper.

By 1991, money market funds held $535 billion in total assets. By 1999, money market funds had tripled in size to $1,579 billion and by 2007, money market fund assets stood at $3,757 billion. This equaled almost 50% of U.S. commercial bank assets, whereas in 1991, money market funds were only 15% of U.S. commercial bank assets. Money market funds had become a significant factor in the financial markets of the United States. The impact of the crisis on money market funds was stark: by the end of 2010 more than $1 trillion was withdrawn from the funds.

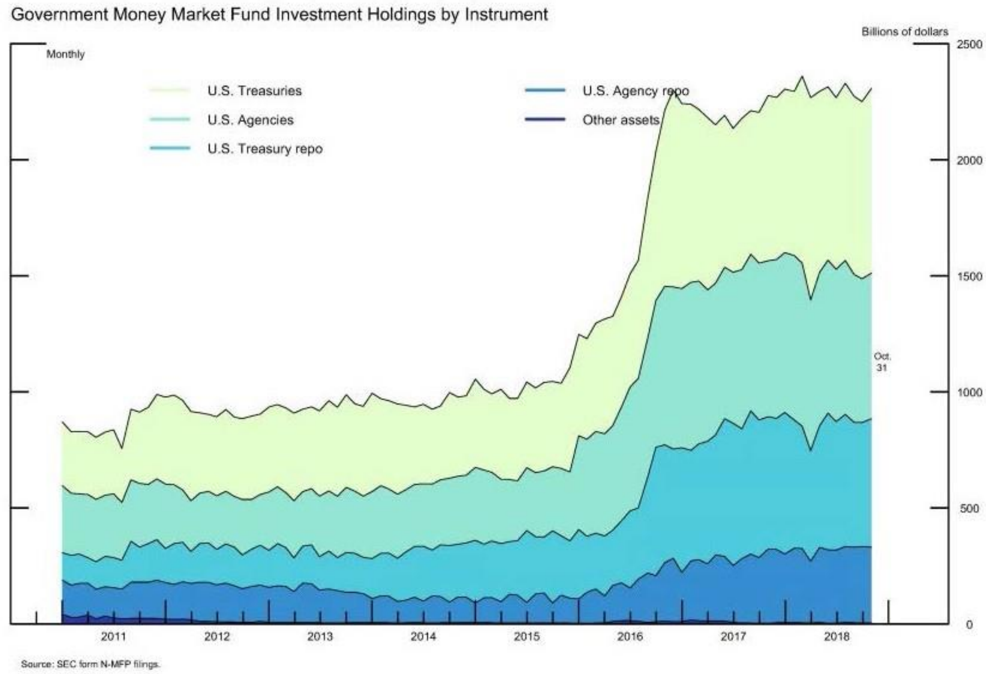
Money market funds came to be the biggest investor group for commercial paper and commercial paper became the largest asset class for money market funds prior to the financial crisis. In 2007, commercial paper accounted for 32% of asset holdings for money market funds. In early 2007, money market funds and mutual funds held nearly $775 billion of commercial paper. Even after the crisis and before the SEC changed the asset requirements for money market funds in 2016, such funds would typically hold a third of commercial paper outstanding. The short-term nature of commercial paper particularly suited money market funds. Moreover, before the financial crisis, money market funds were a heavy investor in ABCP.

The collapse of the asset-backed commercial paper market put significant pressure on money market funds and the Lehman Brothers bankruptcy triggered a crisis for many market funds. As a heavy investor in Lehman commercial paper, the Reserve Primary Fund was an immediate casualty of the Lehman Brothers bankruptcy filing as the filing triggered a run on the fund. Concern about commercial paper holdings of other money market funds quickly led to runs on other funds.

The importance of the commercial paper market to the general economy was immediately apparent as corporations scrambled to draw on bank lines of credit to replace commercial paper financing. This led to the extension of deposit insurance to money market funds, the purchase of commercial paper by the Federal Reserve and capital injections for many financial institutions.

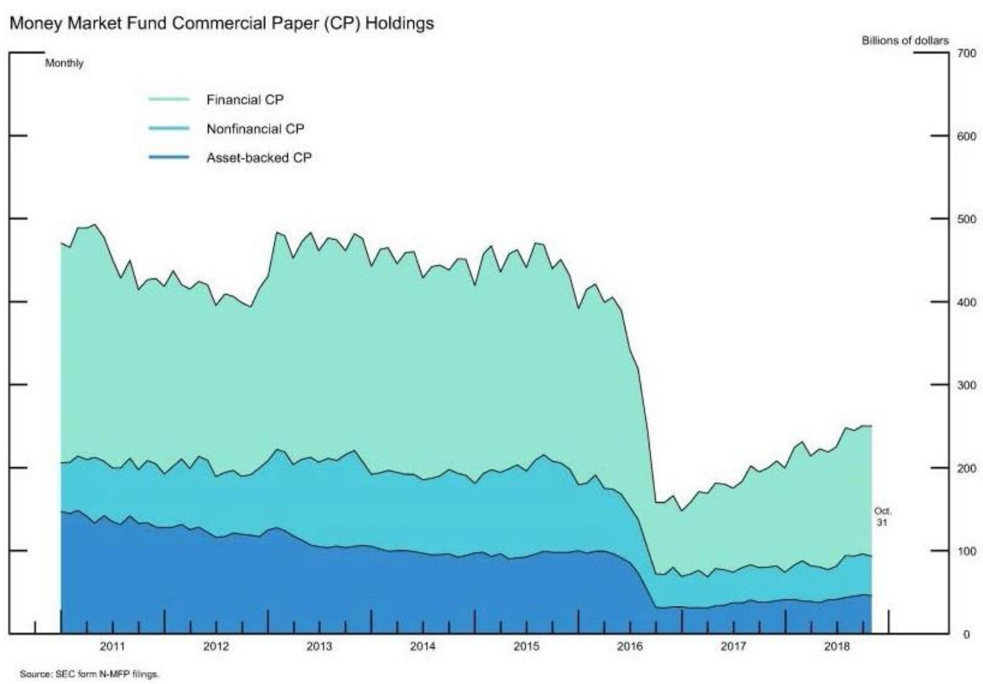
The run on money market funds convinced the SEC that crucial changes were required in the regulations that governed money market funds. In 2014, the SEC amended Rule 2a-7 under the Investment Company Act of 1940 that regulated money fund assets in order to reduce the risk of a run on a fund. The key elements of the amendment required funds to compute the value of their assets using market factors and to instill a system of gates and fees to limit the amount of withdrawals from funds. These changes notably did not apply to retail funds (Funds that limit all beneficial owners to natural persons) or to government money market funds. (Funds that invest at least 99.5% of their assets in securities of the United States government or an instrumentality of the government or repurchase agreements that are full collateralized). The result was a restructuring of many funds to become government funds in order to avoid the imposition of limitations on withdrawals.

In October 2016, the SEC changes to the rule for money market funds became effective. In anticipation of this change, there was a dramatic shift in money market fund assets of more than $1 trillion into the U.S. government securities as shown in the chart below for government money market funds.



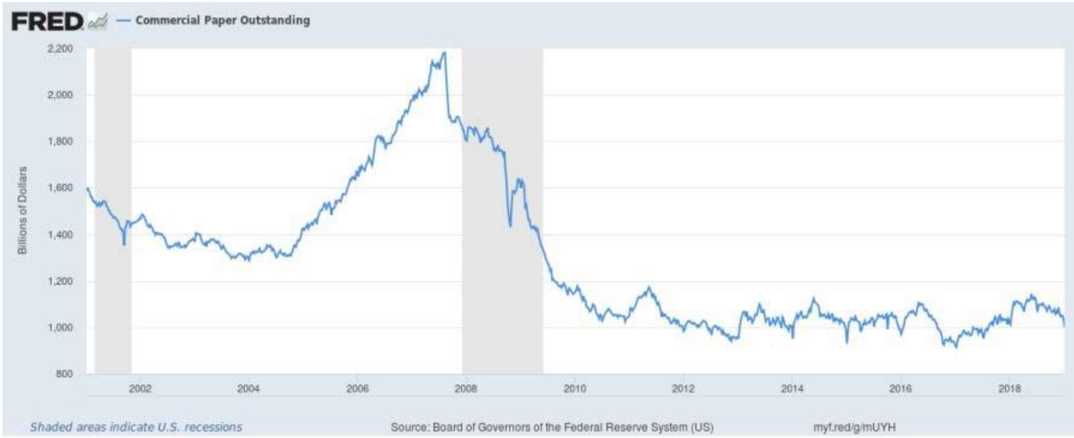
SOURCE: Board of Governors of the Federal Reserve System (U.S.)

With the huge increase in government money market funds, there was a corresponding decrease of investment in all types of commercial paper by money market funds as shown in the chart below.



SOURCE: Board of Governors of the Federal Reserve System (U.S.)

However, as shown in the chart below for outstanding commercial paper, there has been no dramatic drop in the level of commercial paper outstanding despite the very significant drop in commercial paper holdings by money market funds. Starting in June or July 2016, the spread to the federal funds rate for commercial paper started to peak and commercial paper outstandings fell by 20% in the July–October period. By early 2017, the peak in the spread to federal funds rate had disappeared. In terms of the amount of commercial paper, the market fully recovered. Issuers are apparently finding sufficient demand from other institutional investors and money fund holdings have increased from the lows of late 2016. Mutual funds, other than money market funds, corporate, and other investors continue to be active buyers of commercial paper.



SOURCE: Board of Governors of the Federal Reserve System (U.S.)

Market Outlook

The prospects for the commercial paper market remain strong, although it is unlikely that the asset-backed sector of the market will ever regain its dominance. Commercial paper remains a cost-effective alternative to financing with bank loans for many large companies with good credit and for finance companies and financial institutions. On the demand side, the commercial paper market continues to be a market where institutional investors can find short-term investments in the size and maturity of their choice and even the significant decline in purchases by money market funds has not adversely impacted market outstandings.

The commercial paper market has experienced two major disruptions in the last 10 years. The market appears to have survived those disruptions, with some assistance from the Federal Reserve in 2008. Today the commercial paper market continues to provide significant levels of working capital funding to the economy. Asset-backed funding levels have been drastically reduced, removing substantial maturity mismatches and the related risk from the market. It may be expected that as interest rates rise in the next few years, there will be more reliance on commercial paper funding and market outstandings will grow.

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Jerry Marlatt is a partner in Mayer Brown's New York office and a member of the Corporate & Securities practice. He represents issuers, underwriters and placement agents in public and private offerings of debt, covered bonds, surplus notes, securities of structured investment and specialized operating vehicles, and securities repackagings.

Representative transactions include the first covered bond by a US financial institution, the first covered bond program for a Canadian bank, surplus notes and common stock for a US monoline insurance company, eurobond offerings by US issuers, and securities offerings for a variety of structured vehicles, including CBOs, SIVs, CDOs, derivative product companies, ABCP conduits and credit-linked investments.

Jerry is co-author of Considerations for Foreign Banks Financing in the US, published by International Financial Law Review (2012; updated 2014, 2016); a contributor to Covered Bonds Handbook, published by Practising Law Institute (2010; updated 2012-2014); and a charter member of the United States Covered Bonds Council. Jerry was named "Dealmaker of the Year" in 2013 by The American Lawyer for his work as issuer's counsel on the first covered bond deal ever registered with the Securities and Exchange Commission