Hot Charts

Economics and Strategy

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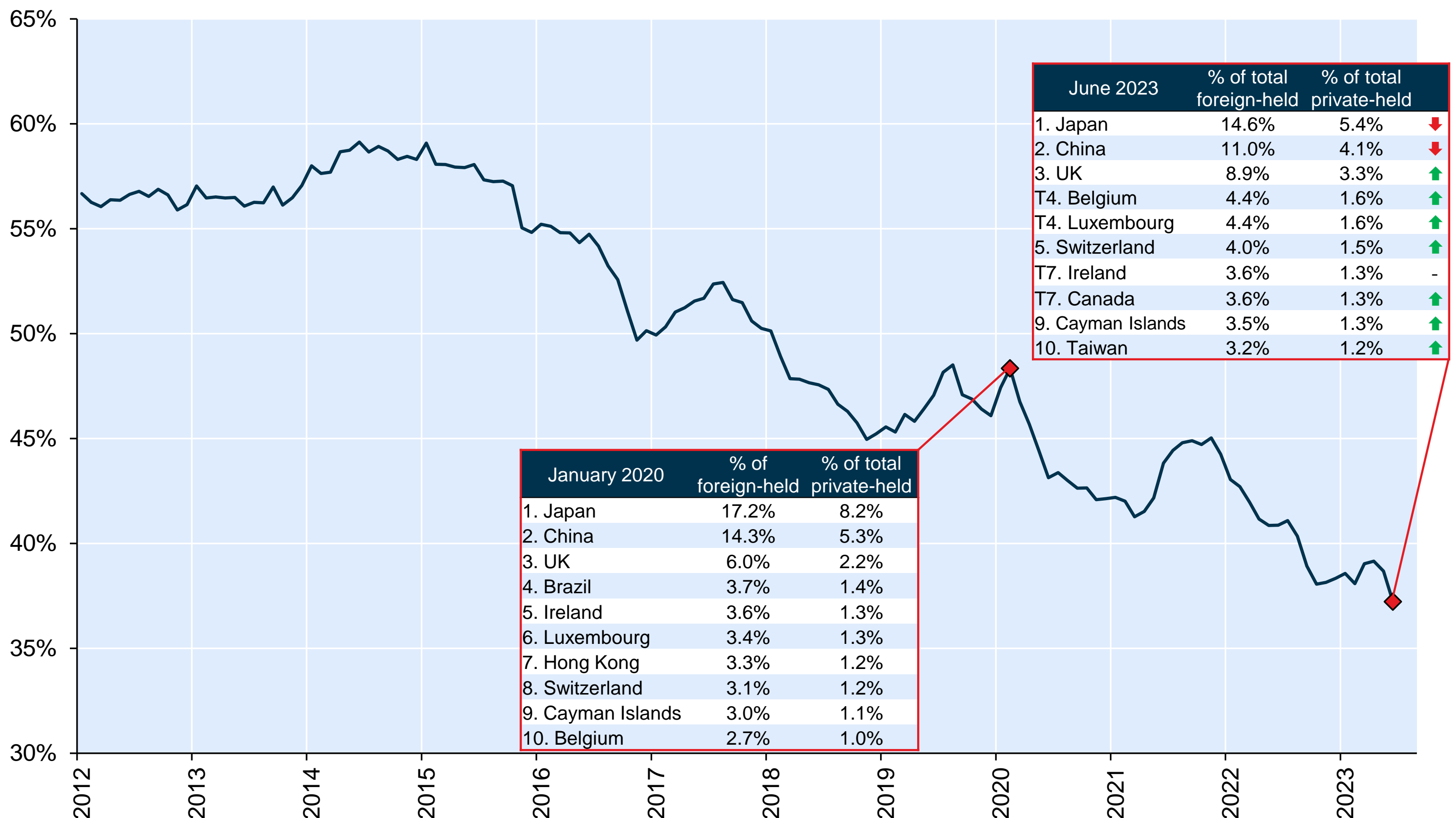
U.S.: Foreign investor pullback adds pressure on bond yields

By Jocelyn Paquet & Taylor Schleich

Over the last year U.S. inflation has fallen from ~9% to just above 3%, an impressive and rapid pace of disinflation. While one might naturally assume this should translate to lower interest rates, this has hardly been the case. Instead, the bellwether 10-year Treasury yield has jumped from 3.0% to 4.3% over the past year, including a steady and unrelenting sell-off over recent weeks/months. To be sure, today's higher interest rates predominantly reflect an ongoing reassessment of the long-run neutral rate of interest as the U.S. economy continues to prove resilient to higher rates (long-dated SOFR futures imply a rate of ~4% today versus ~3% a year ago). But there are other factors working at the margins and their influence could be magnified going forward. For one, there's the seemingly unsustainable fiscal path that the U.S. is on. Bond issuance will remain under pressure amidst growing deficits and elevated borrowing costs, this contributing to Fitch's well-publicized credit rating downgrade earlier this month. CBO analysis suggests that publicly held debt could jump from ~$26 trillion in 2023 to ~$45 trillion by 2033, and for now, supply is being supplemented by the Fed ongoing QT efforts. At the same time—as today's *Hot Chart* indicates—the all-important foreign investor base has been retreating from the Treasury market on a relative basis, their ownership share of privately-held Treasury securities (i.e., excluding the Fed) slipping from just under 50% pre-COVID to less than 40% in June. Moreover, the largest non-resident holders of USTs—China and Japan—have continued to pull back from the Treasury market on a relative *and* absolute basis. In the here and now, the Chinese monetary authority is having to defend its currency and Japan is slowly inching closer to policy normalization, neither of which argue for marginal re-engagement. Now, we don't want to suggest that the USD is at risk of losing its status as the global reserve currency but it's becoming increasingly difficult for demand to keep pace with ever-growing supply. Barring fiscal retrenchment (unlikely from either side of the political aisle) or a revival of major foreign investors, upward pressure on the term premium may be a feature of the U.S. bond market for some time… particularly relative to peers, like Canada, where fiscal sustainability is less of a concern and non-residents are more engaged than ever.

U.S.: Foreign buyers gradually retreating from U.S. Treasury market

Share of privately-held U.S. Treasury securities owned by foreigners (w/ detailed breakdown for select periods)



June 2023	% of total foreign-held	% of total private-held	
1. Japan	14.6%	5.4%	↓
2. China	11.0%	4.1%	↓
3. UK	8.9%	3.3%	↑
T4. Belgium	4.4%	1.6%	↑
T4. Luxembourg	4.4%	1.6%	↑
5. Switzerland	4.0%	1.5%	↑
T7. Ireland	3.6%	1.3%	-
T7. Canada	3.6%	1.3%	↑
9. Cayman Islands	3.5%	1.3%	↑
10. Taiwan	3.2%	1.2%	↑

January 2020	% of foreign-held	% of total private-held
1. Japan	17.2%	8.2%
2. China	14.3%	5.3%
3. UK	6.0%	2.2%
4. Brazil	3.7%	1.4%
5. Ireland	3.6%	1.3%
6. Luxembourg	3.4%	1.3%
7. Hong Kong	3.3%	1.2%
8. Switzerland	3.1%	1.2%
9. Cayman Islands	3.0%	1.1%
10. Belgium	2.7%	1.0%

NBF Economy and Strategy (data via Bloomberg) | Note: Privately-held U.S. Treasury securities calculated as total public debt less intragovernmental holdings and Treasury securities held outright at the Federal Reserve

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