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Band-aid on a fiscal hole

By Taylor Schleich, Ethan Currie & Vy Le

Last week, U.S. Treasury Secretary Scott Bessent delivered a jolt to an otherwise sleepy bond market. The stated goal of increasing longer-end bond buybacks was to improve liquidity, but the move was likely intended at least partly to quell the steady rise in borrowing costs. Bessent followed the announcement with an interview in which he explained that long-term yields are not reflecting “fundamentals,” argued that corporates should be issuing in the belly of the curve (i.e., not competing with the sovereign) and suggested that the U.S. can grow out of its debt burden. On the last point, we’d respectfully disagree. While the Secretary pledged to unveil a greater focus on “fiscal consolidation” this week, it would take a herculean effort to fix the U.S. fiscal trajectory—an outcome we view as unlikely. It follows that fundamentals *do* support high and rising long-term yields.

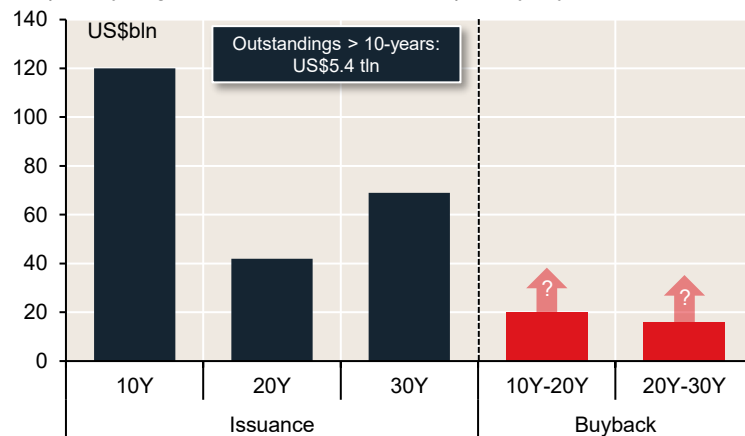
At the same time, as Bessent mentioned, the Treasury does have both the tools and firepower to lean against rising borrowing costs. The \$4 billion amount tied to each buyback operation, for example, is not a hard

cap. The Treasury could also draw down the TGA to fund additional purchases rather than offsetting them with more bill issuance, provided it were willing to operate with a structurally smaller cash buffer. It could also skew issuance toward shorter maturities to take pressure off the long end, even though Bessent criticized his predecessor for doing precisely that. But while these could be impactful, they are temporary stopgaps. Without addressing the underlying fiscal problems, market forces are likely to continue pushing yields higher over time.

In this *Market View*, we put some of Bessent’s recent claims in context and lay out the fiscal predicament facing the world’s largest economy. Ultimately, we expect a modest further upward drift in long-term Treasury yields, though there may be a soft ceiling not far above pre-intervention levels. Risks to our forecast are skewed higher, however, and if those upside risks materialize, we’d expect bond markets with better fundamentals—Canada, for example—to outperform.

Chart 1: Buybacks are small relative to issuance

US quarterly long-term note/bond issuance and quarterly buyback run-rate*

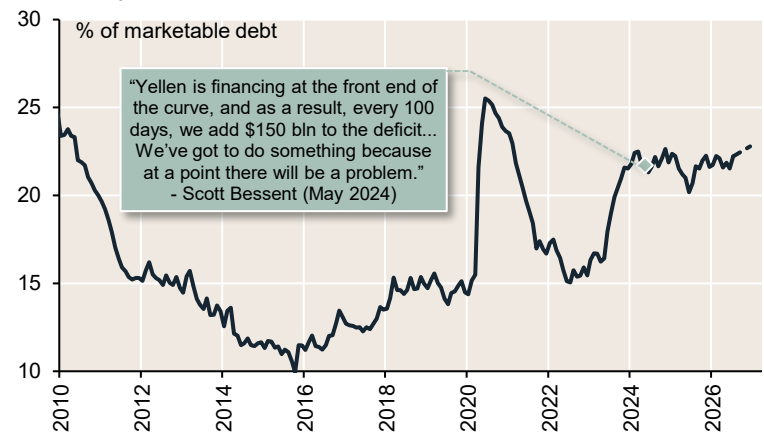


Source: NBC, US Treasury | Note: *Assumes >\$4 bln size applied to all operations in quarter

A \$4 bln/operation long-term UST buyback is small relative to supply or the long-term debt stock. That said, this isn’t a hard cap and support is theoretically unlimited, which sent a powerful signal. But buying these bonds requires cash and we don’t see the Treasury issuing more bonds to fund that. Rather, short-term issuance may be leaned on—a strategy Bessent criticized Yellen for using.

Chart 2: T-bill share of issuance high and drifting up

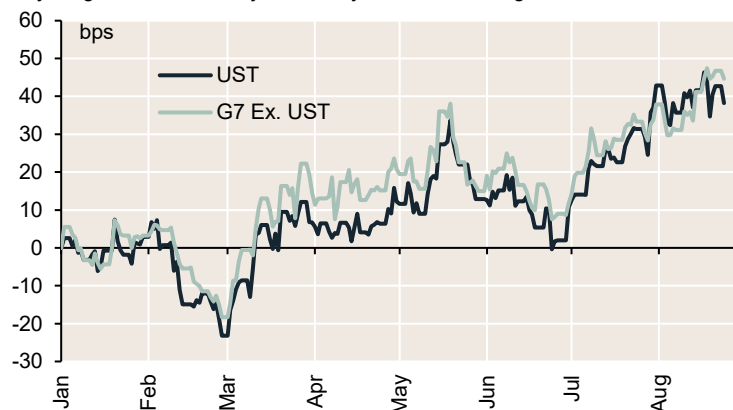
US Treasury bill share of marketable debt stock



Source: NBC, BBG, U.S. Treasury, TBAC | Note: TBAC projection through U.S. FY-end.

Chart 3: The long-end yield surge isn’t just a UST story...

30-year government bond yield 2026 year-to-date change

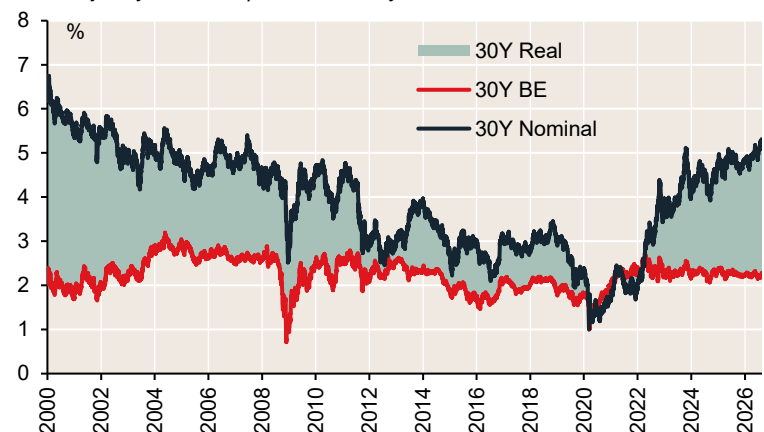


Source: NBC, Bloomberg | Note: G7 ex. UST is simple average

Rising long-end yields isn’t exclusive to the U.S. In fact, U.S. 30Y yields have risen less than over half the G7 this year (only Canada and Germany, who both enjoy more favorable fiscal positioning, sold off less). This sell-off isn’t about elevated inflation expectations either. Breakevens have been low and stable, with *real* yields driving the nominal rise. This dynamic has durability in our view.

Chart 4: ...nor is it one of problematic inflation expectations

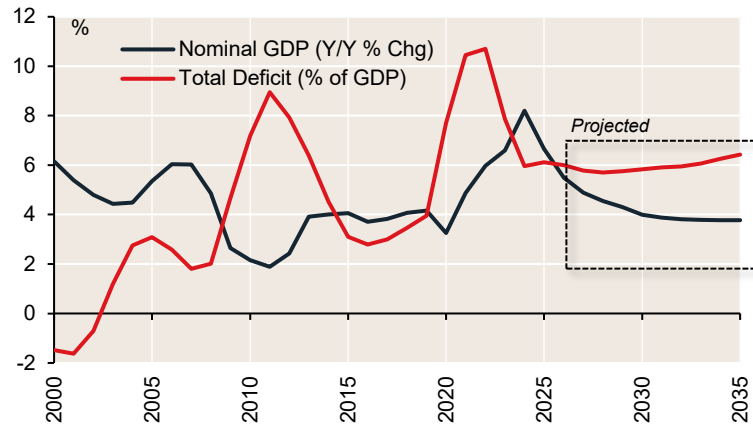
UST 30-year yield decomposed into real yield and breakeven inflation rate



Source: NBC, Bloomberg

**Chart 5: Grow your way out of the deficit? Unlikely.**

U.S. nominal GDP growth and deficit (3Y moving average): Actual vs. projected

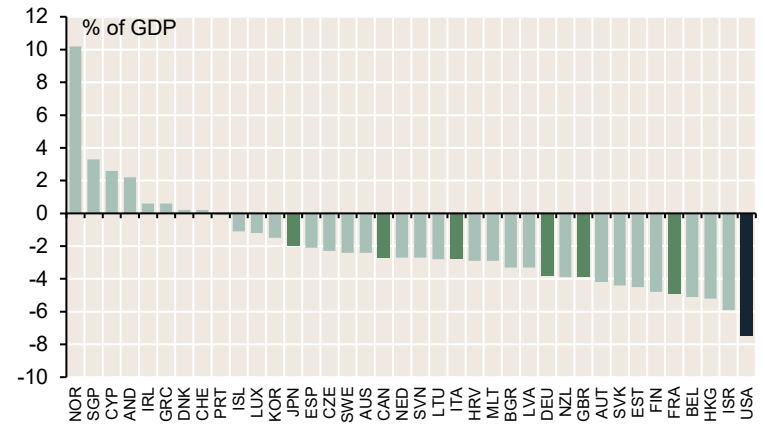


Source: NBC, CBO | Note: CBO projections from Feb-2026 baseline beginning 2026

While growing your way out of a deficit sounds nice, it's simply not possible if you believe in most mainstream estimates of future GDP growth. The U.S. deficit (outright, and as a % of GDP) is set to grow over the next decade. And though larger deficits are also a global phenomenon, the U.S. fiscal shortfall is on another level, by far the largest among advanced economies (shown above).

Chart 6: The U.S. has the largest advanced economy deficit

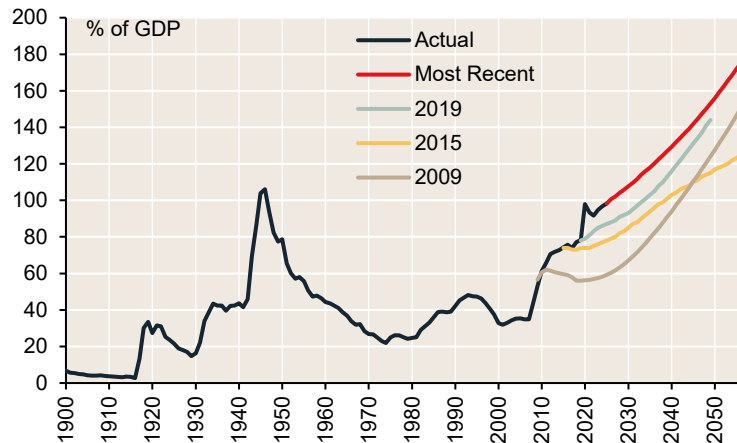
IMF projection for general government balance as a share of GDP (2026)



Source: NBC, IMF Fiscal Monitor | Note: Dark green bars denote other G7 economies

Chart 7: Sustained shortfalls have led to rising debt stock

U.S. government debt held by the public (% of GDP): Actual vs CBO projections

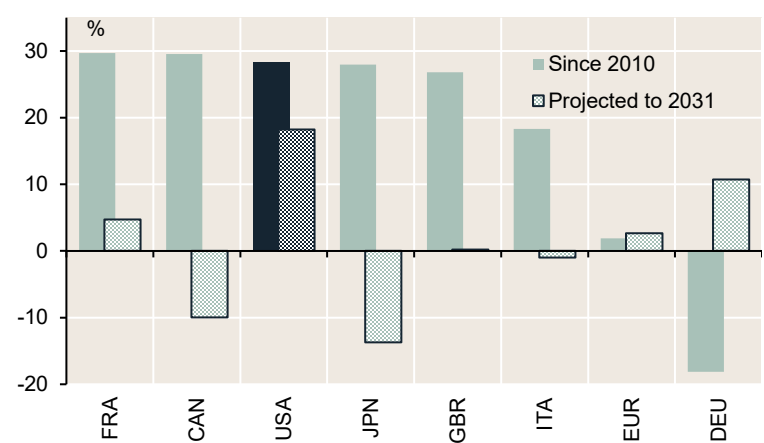


Source: NBC, CBO | Note: From CBO extended baseline projections (latest = Feb-2026)

Over time, ongoing deficits have pushed the U.S. debt burden steadily higher. In dollars, the debt stock continues to set new records (now over \$32 trillion) and as a share of GDP, is set to reach an all-time record by the turn of the decade (and if history is any guide, the CBO may be understating the pace of the increase). Again, the U.S. is not alone in accumulating debt—most advanced economies have since the GFC, and the U.S. isn't even the worst offender. However, the pace of debt growth is set to slow or contract in most economies...not really the case in the U.S.

Chart 8: Unlike some others, no fiscal consolidation in view

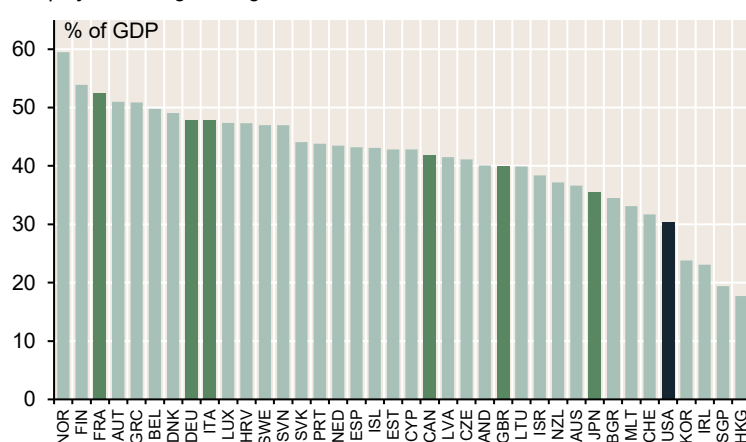
Change in gross debt-to-GDP ratio of G7 countries: 2010-2025 and 2025-2031



Source: NBC, IMF | Note: 2026-2031 projected via IMF; EUR is Eurozone aggregate

Chart 9: More scope for revenue increases (i.e., tax hikes)...

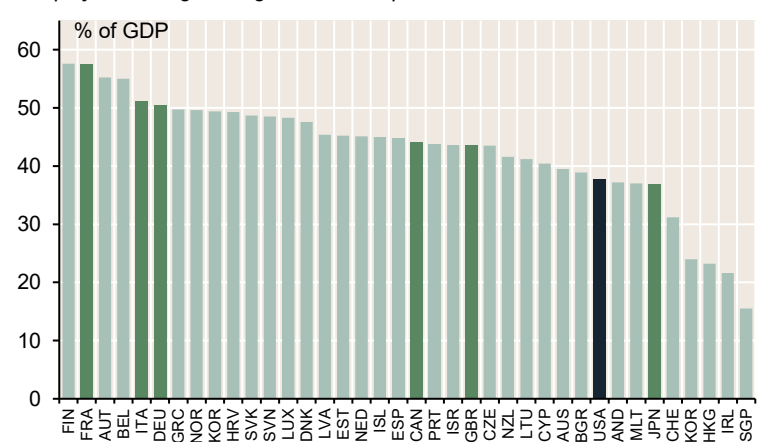
IMF projection for general government revenue as a share of GDP: 2026



Source: NBC, IMF Fiscal Monitor | Note: Dark green bars denote other G7 economies

Chart 10: ...as spending is at the low-end of global spectrum

IMF projection for general government expenditure share of GDP: 2026

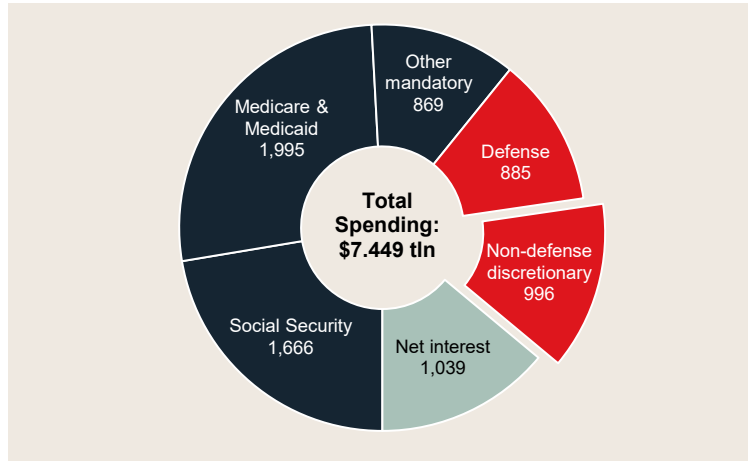


Source: NBC, IMF Fiscal Monitor | Note: Dark green bars denote other G7 economies

Relative to other advanced economies, U.S. revenue collection as a share of GDP is at the low end of the spectrum, which suggest tax increases are the easier way to address persistent fiscal shortfalls. Meanwhile, spending as a share of GDP isn't exceedingly high—at least relative to other advanced economies. As DOGE found out last year, there's not all that much fat to trim.

Chart 11: Not a ton of easy 'fat to trim' on U.S. budget

U.S. federal spending by category: 2026 projection

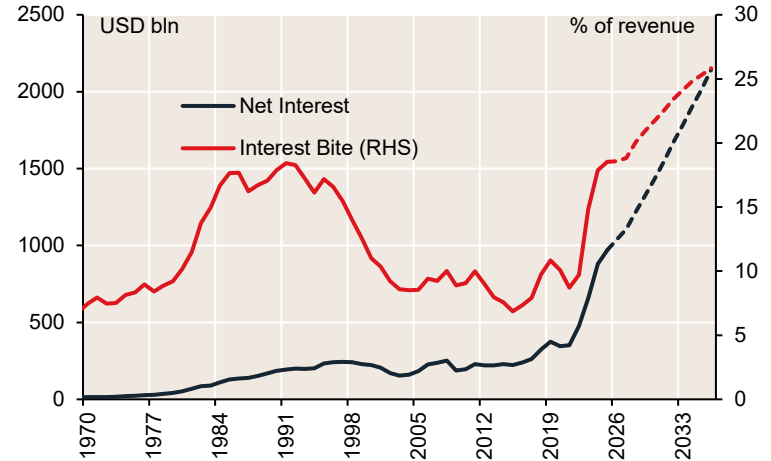


Source: NBC, CBO | Note: *Based on CBO's Feb-2026 Budget and Economic Outlook

Without making difficult/politically unpopular decisions, it's hard to see material spending cuts being made. If Medicare/aid and Social Security are untouchable and the U.S. continues to fund its military and pay interest on debt, there's less than a trillion of discretionary spending to 'play with' (or 13% of spending). Speaking of interest on debt, this has exploded in recent years. 10 years ago, Washington spent \$240 billion on interest or ~7% of revenue. Interest payments have since quadrupled, consuming >18% of each revenue dollar. Unchecked, interest will double in the next decade.

Chart 12: Interest payments to grow (outright and relative)

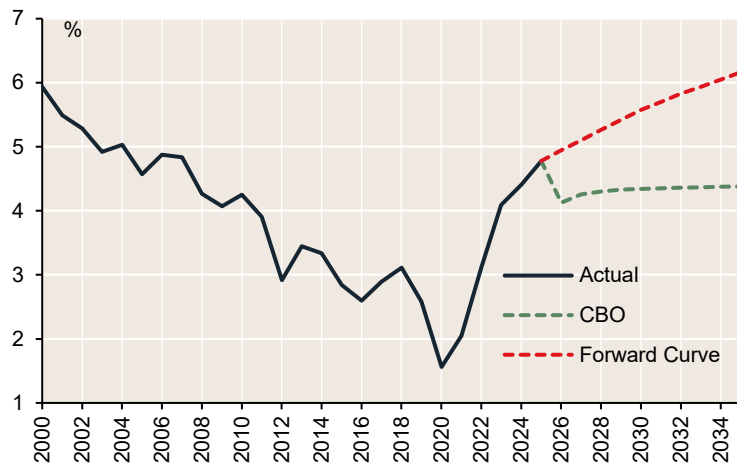
Net interest expenditure and interest bite (% of revenue): Actual vs projected



Source: NBC, CBO | Note: 'Interest bite' = net interest expense / total revenue

Chart 13: Debt servicing may prove even costlier

UST 10Y nominal yield: Actual (annual average) vs projected by CBO & forwards

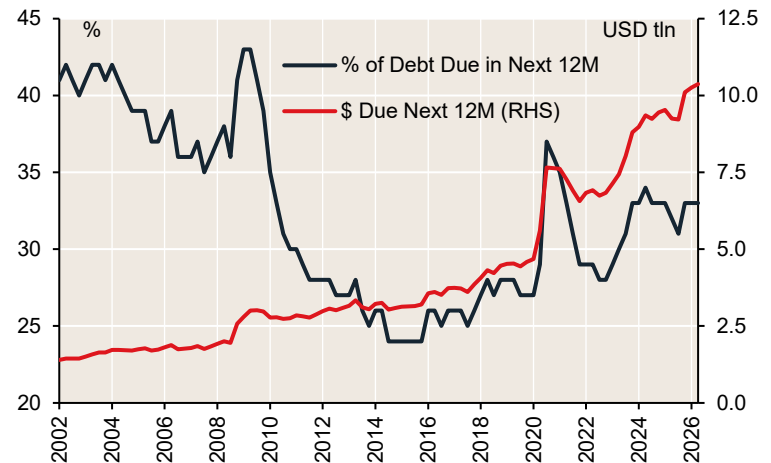


Source: NBC, CBO, Bloomberg

The CBO's Budget & Economic Outlook assumes a 10-year treasury yield of roughly 4.3% over the next decade and that already produces some alarming interest payment schedules. If the forward curve materializes, even more interest would be racked up. Also note the U.S. is more exposed to refinancing risk than a decade ago, with about a third of its debt due to mature in the next year. Here's hoping Fed rate hikes can continue to be avoided.

Chart 14: Record refinancing needs approaching (again)

UST principal repayments due in next 12 months: Outright vs as % of total stock



Source: NBC, Bloomberg | Note: Quarterly average data



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