

THERE'S NO SUCH THING AS A FREE LUNCH

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Without a doubt, the biggest story in bond-land, if not the financial markets in general, thus far in 2021 has been the spike in the [U.S. Treasury 10-year yield](#). This increase has been fueled by a variety of factors, but there is one aspect that has not received the lion's share of attention, and after I did a little research, it really caught my eye; the size of [Treasury auctions](#).

When budget deficits are running in the multi-trillions, guess what? You have to finance this huge gap. That is exactly what is happening for the Treasury debt managers. At this point, the federal government's financing needs reflect the baseline trillion-dollar deficit coming into this fiscal year as well as any holdovers from the prior pandemic-related [fiscal stimulus](#) packages that were enacted. Thus, the \$900 billion package from December is part of the mix, but the \$1.9 trillion dollar proposal currently being debated in the Senate would be another enormous add-on.

U.S. Treasury Auction Amounts (New Issues in billions)			
	Year Ago	2021	Change
2-Year	40.0	60.0	20.0
3-Year	38.0	58.0	20.0
5-Year	41.0	61.0	20.0
7-Year	32.0	62.0	30.0
10-Year	27.0	41.0	14.0
20-Year		27.0	27.0
30-Year	19.0	27.0	8.0
TIPS			
5-Year*	17.0	18.0	1.0
10-Year	14.0	15.0	1.0
30-Year	8.0	9.0	1.0
FRN			
2-Year	20.0	28.0	8.0

Source: U.S. Treasury, as of 3/4/21. Note: Next new issue 5-Year TIPS auction is tentatively scheduled for 4/22/21.

The enclosed table highlights the auction amounts currently in place versus the totals that were being auctioned for each security/maturity a year ago. Certainly, the 20-Year bond stands out as this issue was not being offered at this time in 2020. For the record, this maturity was brought back in May of last year to help with the debt load for the first time since 1986.

The other issue to stand out is the 7-Year note, where the present auction amount is an incredible \$30 billion more than a year ago. The abysmal reception at the most recent auction for this maturity not only made headlines, but also got me thinking that maybe there are limits as to how much paper can be digested without investors commanding higher yields in return. The remaining note structure (2-, 3-, 5-Year) is \$20 billion higher for each maturity, with the aforementioned 10-Year note being \$14 billion above

its 2020 reading.

Interestingly, the [TIPS](#) line-up is 'only' up \$1 billion each, while the [FRN](#) offering got an \$8 billion boost. It seems apparent the debt managers felt the FRN structure would be a preferred vehicle to raise cash rather than TIPS.

Conclusion

So, that raises the question: what is too big? Up until the very disappointing 7-Year note auction last month, it appeared as if auction sizes did not have any near-term limitations. However, maybe, just maybe, budget deficits do matter after all because someone has to finance them, and to quote: "There's no such thing as a free lunch."

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DEFINITIONS

10- Year Treasury: a debt obligation of the U.S. government with an original maturity of ten years.

Auction: a public offering of newly issued debt securities in which pricing is determined via an investor bidding process.

Fiscal Stimulus: Using fiscal policy as a tool to provide economic growth.

Treasury Inflation-Protected Securities (TIPS): Bonds issued by the U.S. government. TIPS provide protection against inflation. The principal of a TIPS increases with inflation and decreases with deflation, as measured by the Consumer Price Index. When a TIPS matures, you are paid the adjusted principal or original principal, whichever is greater.

Floating Rate Treasury Note: a debt instrument issued by the U.S. government whose coupon payments are linked to the 13-week Treasury bill auction rate.