Politics

Yellen Grilled by Trump Allies in Odd Feud Over Debt Management

- Some Republicans say she juiced economy to help sway election
- Washington dysfunction seen as risk to Treasury market

By Saleha Mohsin and Liz Capo McCormick
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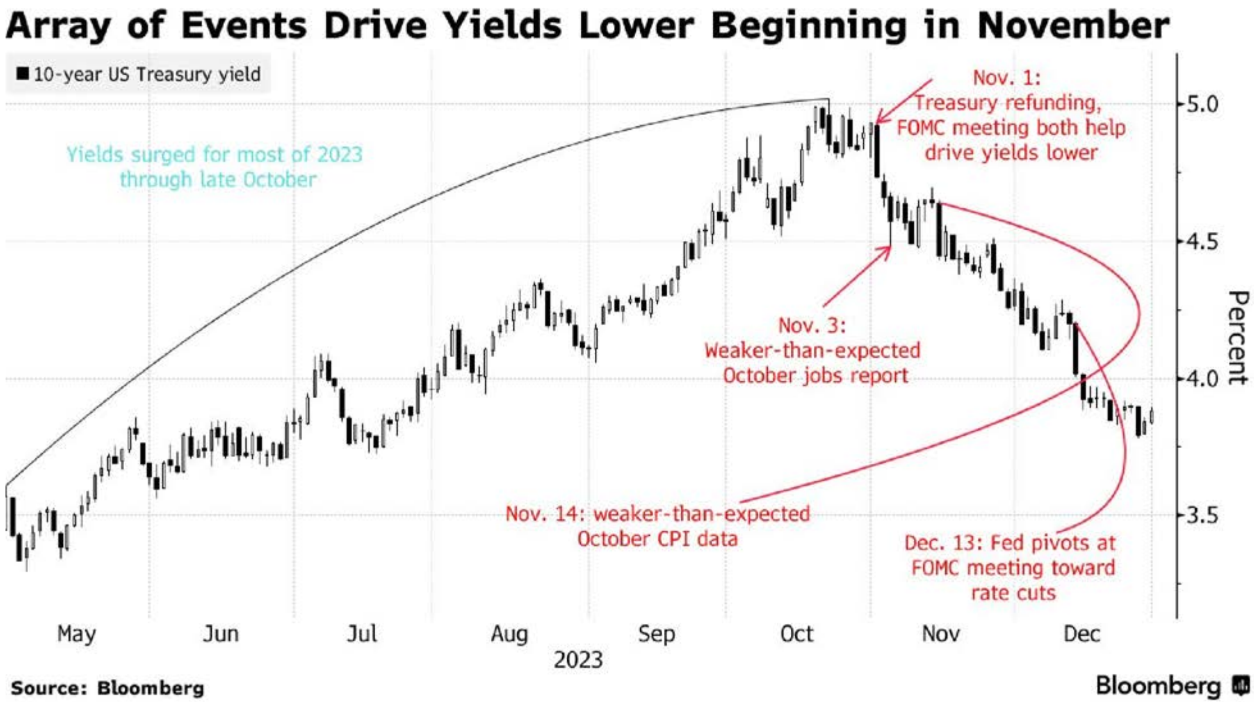
At a time of hyper-polarized politics, even the wonky mechanics of US bond auctions are fair game – and that's making Treasury Secretary Janet Yellen a new favorite target of some Trump-leaning Republicans.

Yellen has found herself on the receiving end of attacks from GOP lawmakers who claim she gamed Treasury debt auctions to juice the economy and make her boss, President Joe Biden, look good. The charge – which Yellen has rejected – was repeated as recently as Tuesday, when Senator Bill Hagerty pushed Federal Reserve Chair Jerome Powell to agree with him that Yellen was playing tricks by structuring debt sales the way she has.

"Some people, including myself, believe this is being done to artificially stimulate markets in the run-up to the election," Hagerty, a Republican from Tennessee and potential Trump cabinet nominee, said in quizzing Powell. The Fed chair downplayed the significance and otherwise declined to comment.

Others sounding the same theme include GOP Senator John Kennedy of Louisiana as well as Scott Bessent, a hedge fund manager and prominent fundraiser for Donald Trump who's seen as a potential pick for a top economic position if the ex-president wins in November.

It's a quirky line of argument that stretches back to last year. Here's the gist: After a slump in Treasuries sent key US interest rates to their highest levels in more than a decade, Yellen's team announced on Nov. 1 a tempering in the trajectory of long-term borrowings in a way that helped stem, and then reverse, the selloff. At the same time, the Treasury moved to beef up sales of bills, which are shorter-dated.



The misdeed, as the Republicans tell it, is that by engineering a decline in long-term yields, she pushed down consumer borrowing rates to boost home sales and more. On top of that, they say, by increasing auctions of Treasury bills at 5% yields – currently higher than those on long-term bonds – she intentionally paid out more money than needed to investors to give them extra purchasing power.

Confused? Yellen herself appeared perplexed at times when she attempted to respond to an aggressive line of questioning from Kennedy on Capitol Hill back in June about whether her maneuvers amounted to market timing that created a "sugar high" for the economy. "In federal borrowing," she explained, "our objective is to issue at least cost over time and not to try to time the market."

Many bond market experts agree - which isn't to say Yellen's decisions had no impact. The Treasury's tweaks did help to steady markets. But other macroeconomic forces were also at play. And the adjustments – while involving billions of dollars – were relatively minuscule in a market approaching $30 trillion and "well within normal adjustments they would make," said Michael Pugliese, senior economist at Wells Fargo & Co.

Yellen fielded pointed questions in June from Senator John Kennedy about her debt-management decisions. *Photographer: Tierney L. Cross/Bloomberg*

Of course, a sound bite centered on the mechanics of debt management isn't the kind of zinger that resonates far and wide. But the fact that some politicians are embracing it places fresh emphasis on the interplay between the country's ballooning deficits and the day-to-day economy. The US debt pile is set to keep growing amid a dearth of political will to tighten finances. And it could be argued that profligate deficit spending is what's priming the economic pump. Regardless, the injection of politics threatens to complicate the already difficult task of managing federal borrowing.

Several dealers already see the Treasury needing to increase long-term debt sales next year, whoever is in the White House. Strategists at Barclays Plc say that boosts to note and bond auction sizes could begin as soon as February.

"The Treasury securities market is being beset by a combination of economic, political and technical challenges, which are feeding off and compounding each other," said Eswar Prasad, a Cornell University professor and senior fellow at the Brookings Institution. "Political dysfunction in Washington creates another significant risk."

Within the Treasury, the chorus of criticism has struck a nerve – so much so, that the top US Treasury official overseeing debt sales saw fit to launch a forceful rebuttal of what he called "common misperceptions" in a speech to an industry group on Thursday evening.

Regular, Predictable

"We issue securities in a regular and predictable fashion as part of our strategy to borrow at the lowest cost over time," Josh Frost, assistant secretary for financial markets, said in prepared remarks. But "regular and predictable issuance doesn't mean that Treasury steadfastly 'stays the course' even when presented with new information and situations," he added.

Read more: US Treasury Counters 'Misconceptions' Over Debt-Sales Strategy

Frost is a political appointee, tapped by Biden, but the majority of the debt management team are career staffers – meaning they've served under both political parties.

The US Treasury has a mandate to borrow through debt issuance the money needed to fund the US deficit *Source: Bloomberg*

Bessent, the Trump ally, rejected Frost's argument. "He hasn't given a good justification for why they have dramatically increased bills issuance. Are we fighting a war? Is the economy in deep downturn? Is there a national emergency? No, we've been suffering from too-high inflation," Bessent said in an interview.

Read more: Trump Ally Bessent Says Yellen Using Post to Aid Biden 2024 Bid

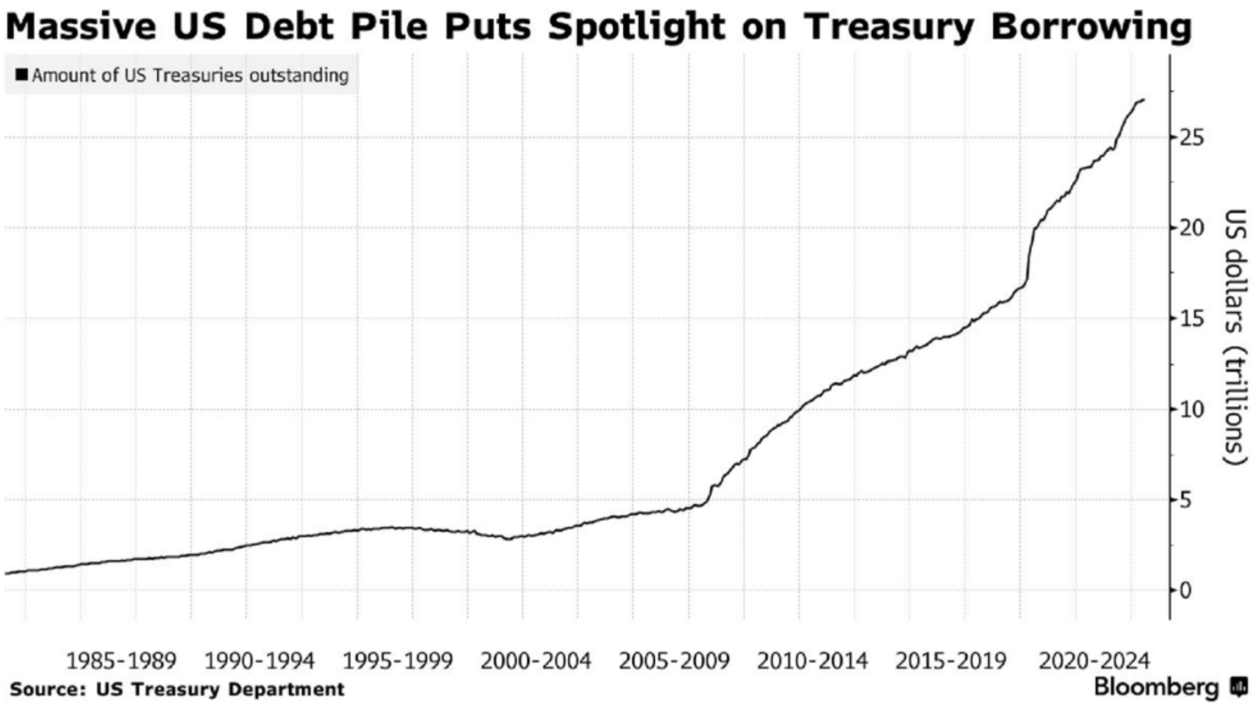
One thing remains clear: With its power to decide how best to borrow, the Treasury has significant sway over the world's benchmark debt. But there are limits. Ultimately, it's Congress that determines spending and sets the US budget, which in turn dictates how much the Treasury needs to borrow. It's the Fed that controls money supply and sets baseline interest rates. And it's investors in the marketplace who determine what the US government must pay.

Read more: What If the Fed's Hikes Are Actually Sparking US Economic Boom?

What the Treasury is doing with debt issuance "is probably not one of the primary variables affecting financial markets or the economy," Goldman Sachs Group Inc. analyst Alec Phillips said in an interview.

Against this backdrop – and with the Republican convention kicking off next week in Milwaukee, and Biden's fate in the balance amid calls from Democrats to bow out of the presidential race – Yellen is now beginning the process of formulating the government's debt issuance strategy for the three months ahead of the election.

The preparation includes a closed-door meeting with an elite committee of debt market participants – known as TBAC – to garner advice on the ideal mix of securities to sell, shortly before the department's July 31 announcement on issuance plans.



It was in just such a quarterly policy release last November – in the wake of a tumble in Treasuries driven by concerns over mounting US deficits – that Yellen's Treasury decided to temper long-term debt increases. The move surprised some dealers, as officials had signaled in August they would likely boost sales of the debt in November at the same cadence as the prior quarter.

This is where Republicans see a motive, pointing to the announcement being out of line with the consensus of dealer forecasts. Even so, a sizable minority had predicted the result. And it matched the recommendation of some TBAC members.

Either way, Treasury officials take pains to stress that they don't just rubber-stamp TBAC's or dealers' recommendations. And in the end, the November pullback in long-term debt issuance amounted to roughly a 1% change, Frost said in his Thursday speech. "This was not outside of any norms," he said.

Whether Frost’s pushback will silence the critics remains to be seen. As for politics?

“It’s highly unlikely that the discussion will resonate with virtually any voters,” Goldman’s Phillips said.
– With assistance from Stephanie Lai