First Trust
Weekly OUTLOOK

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National Debt A Growing Threat

There is more than one reason the 10-year Treasury yield is 5.23% today. Most importantly, the Fed has stopped anchoring interest rates at artificially low levels. Fear of inflation is likely another. However, both of those are related to the massive government debt the US has created.

Fiscal Year 2026 ends September 30 and it looks like net interest on the national debt will top $1.0 trillion, which is more than the US spends on its military. At $ 1.0 trillion, the US will spend 3.3% of GDP on interest, the highest on record going back to at least World War II. In the 1980s and 1990s, the US had debt payments relative to GDP nearly this high. Yet, interest rates were falling!

Why? Because the US had a path to better fiscal health, including President Reagan's supply-side tax cuts (which boosted GDP growth). Reagan also boosted defense spending but restrained other spending. Then Reagan's policies led to a collapse in the Berlin Wall and the peace dividend that followed. President Clinton and House Speaker Newt Gingrich brokered deals to reduce spending more (Ending Welfare as We Know It). These fiscal actions resulted in budget surpluses and net interest expenses falling to a range of 1 – 2% of GDP for 25 years.

This time around, we think the problem is much worse than back in the 1980s-90s and the prospect for bringing interest costs back down to the 1-2% range are much slimmer.

Social Security and Medicare costs have gone from about 6% of GDP in the 1980s-90s to about 9% now. And military spending can't really go much lower.

In other words, although we'd love to see a set of policies put in place to bring the interest burden back down, with our current Congress focused on College Football and not spending restraint it's hard to imagine it not going even higher.

We think this is part of the reason why long-term Treasury yields are up so much recently. The saving rate is lower as a share of income than net interest as a share of GDP for the first time since these data were fully measured. And that makes it tough to fund both $2 trillion budget deficits and $1 trillion in datacenter buildouts at the same time.

The best path for the federal government to take would be to continue the recent downward pressure the Trump Administration has exerted on domestic discretionary spending. But that's unlikely to be enough. Going forward, the US budget position cries out for entitlement reform, but Congress seems unable, unwilling, or unconcerned about acting.

Our biggest fear is that if we wait too long to address entitlements we may eventually get to the point where tax hikes become necessary, or at least very likely, like a national consumption-style tax or value-added tax layered on top of our already overly burdensome set of taxes. Even Reagan signed some tax hikes into law, but to be fair at the end of his term actual tax rates were significantly lower than when he took office.

We aren't predicting Armageddon any time soon, but one way or another our debt burden is pushing inexorably toward a breaking point.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
9-30 / 7:30 am	Q2 GDP Final Report	+1.5%	**+1.5%**		+1.5%
7:30 am	Q2 GDP Chain Price Index	+6.4%	**+6.4%**		+6.4%
7:30 am	Personal Income – Aug	+0.4%	**+0.5%**		+0.4%
7:30 am	Personal Consumption – Aug	+0.9%	**+0.9%**		+0.2%
8:45 am	Chicago PMI – Sep	51.0	**49.8**		47.1
10-1 / 7:30 am	Initial Claims – Sep 26	200K	**200K**		197K
9:00 am	ISM Index – Sep	55.0	**54.8**		54.6
9:00 am	Construction Spending – Aug	0.0%	**0.0%**		-0.5%
afternoon	Total Car/Truck Sales – Sep	16.3 Mil	**16.2 Mil**		16.8 Mil
10-2 / 7:30 am	Non-Farm Payrolls – Sep	90K	**136K**		162K
7:30 am	Private Payrolls – Sep	87K	**127K**		127K
7:30 am	Manufacturing Payrolls – Sep	12K	**9K**		16K
7:30 am	Average Hourly Earnings – Sep	+0.3%	**+0.3%**		+0.3%
7:30 am	Average Weekly Hours – Sep	34.3	**34.3**		34.4
7:30 am	Unemployment Rate – Sep	4.1%	**4.1%**		4.1%
9:00 am	Factory Orders – Aug	+0.1%	**+0.3%**		+0.9%