

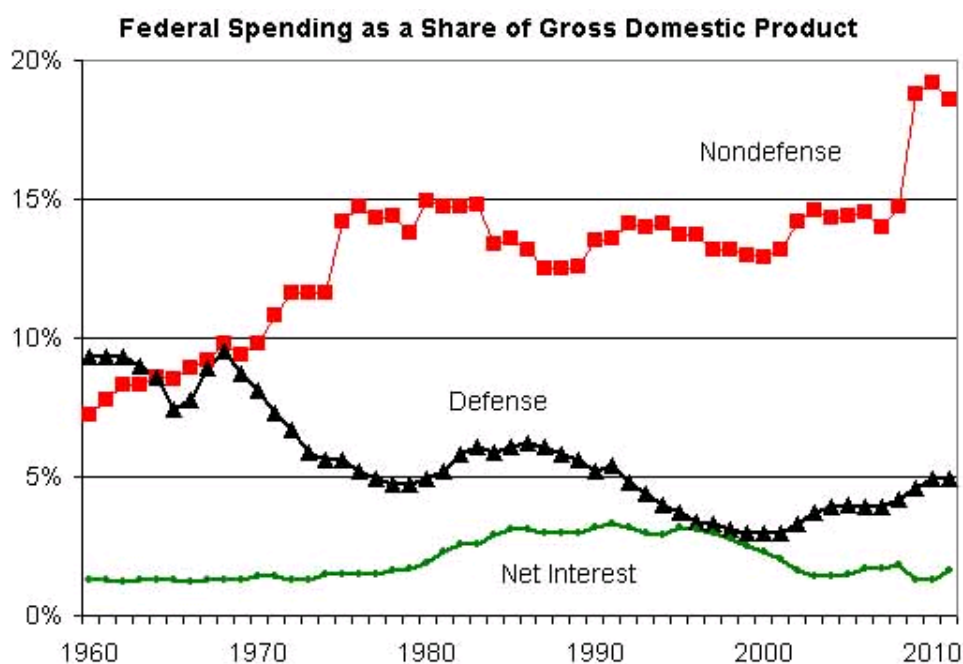


## MarketWatch

FEBRUARY 2, 2010, 4:06 PM ET

### Treasury rates have to go up

Take a look at this chart and tell me what your first reaction is (I'll give you mine below). This shows five decades of government spending by category. Only one category has been going up and that is the red line.



Source: [Cato Institute](#)

My first reaction was to think, 'Treasury rates have to go up.' As we can see from this chart, Non-Defense Spending was under 10% of GDP for years and then it went up into a range of 15% of GDP. Now, we have seen another ramp up to 19%. Defense spending was on a long-term downtrend until 2001 when spending on defense turned up again.

We have been in a benign environment for decades with interests heading lower along with a protracted decline in defense spending. Now, at least, interest rates are very likely to enter an up trend. This chart is from the following report on the Cato Institute's blog.

[5 Decades of Federal Spending](#) (Cato Institute, Feb. 1, 2010, Chris Edwards)

**Defense:** *In the post-9/11 years, defense spending bumped up to a higher plateau of around 4 percent of GDP. But now we have jumped to an even higher level of around 4.9 percent of GDP.*

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***Interest:*** *The Federal Reserve's easy money policies reduced federal interest payments in recent years. That is coming to an end. Obama's budget shows that interest payments will start rising rapidly next year and hit 3 percent of GDP by 2015. And that's an optimistic projection.*

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***Nondefense:*** *This category includes all other federal spending. After a steady decline during the Clinton years to 12.9 percent of GDP, President Bush pushed up nondefense spending to a higher plateau of around 14.5 percent. Then came the recession and financial crisis, and the Bush-Obama tag team hiked spending to an even higher level of around 19 percent of GDP. That level of nondefense spending is almost double the level in 1970 measured as a share of the economy.*

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This increase in spending is the cause (along with declining tax revenues due to the recession) of our burgeoning Federal budget deficits. The only way to finance the deficit is by issuing more debt and that is what the U.S. Treasury is doing. Our national debt is growing so rapidly that I just don't see how Treasury interest rates can stay at these levels.

Due to the downward pressure of the real estate slump and the deleveraging of businesses, there has not been much upward pressure on interest rates. As the economy perks up, that will change.

Hat tip: [Instapundit](#)

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