



Treasuries and How the U.S. Government is Funded

The U.S. government is a large federal bureaucracy that needs money to run its operations. To this end, the government funds itself in two ways. First is the tax revenue it collects. However, the government often does not collect enough in taxes to fund itself. Additionally, federal inflows and outflows do not coincide throughout the year, leading to budgetary shortfalls. As a result, the Department of the Treasury (the Treasury) issues bonds of varying maturities referred to as Treasuries. In 2024 alone, Treasury security issuance stood at \$4.7 trillion. The incredible safety of U.S. Treasuries, combined with the stability of the U.S. economy and financial system, means there is strong, lasting demand for these financial products. Additionally, the Treasury market underpins much of the U.S. financial system itself. However, the importance of the Treasury market also makes it a point of friction for the financial system, and any disruption to the market could lead to large-scale disruptions across the financial system. As the U.S. economy and financial system continue to expand and the U.S. continues to issue large amounts of Treasuries, special attention needs to be paid to both the Treasury market and the mechanisms the Treasury uses to fund the U.S. government.

How Does the U.S. Government Fund Itself?

After Congress appropriates funds, the executive branch begins to execute that funding. However, the Federal Government often runs a budget deficit, meaning it spends more than it receives in a fiscal year. A budget surplus is the opposite: when the government receives more in funding than it spends in a fiscal year. The accumulation over years of budget deficits is the national debt, and the accumulation of budget surpluses is the national surplus.

The amount of Treasuries that the federal government sells in a year is driven primarily by the budget deficit. The larger the deficit, the more money will need to be raised by selling Treasuries to investors. However, even without a budget deficit, Treasuries would still need to be sold occasionally throughout the year. The dates of federal expenditures do not match the dates on which the federal government receives its income. In fact, the federal government receives the majority of its revenue during four months: January, April, June, and September. Those four months correspond to the times when most individuals and businesses pay federal taxes. As a result, Treasuries are used to smooth out timing differences between large federal program outlays and tax revenue.

The Treasury is responsible for all Treasury sales. Specifically, the Office of Debt Management (ODM) within the Treasury is tasked with debt issuance decisions and the management of public debt. The main objective for the Treasury when financing the government is to keep borrowing costs as low as possible over time. Their objective is achieved by issuing debt regularly and predictably, ensuring transparency in Treasury decision-making, and continuing efforts to improve the sale process.

Currently, two types of debt are used to finance the government: marketable and non-marketable debt. Marketable debt is debt

Center Forward Basics

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Yield: The return to an investment over a set period of time. This takes into account any appreciation of price as well as interest rates.

Interest Rate: The amount of money received on a fixed-income product, expressed as a percentage.

Futures: A type of financial contract where buyers and sellers agree to sell a product at a set date in the future for an agreed-upon price in the present.

that can be bought and sold on public exchanges by individuals. Non-marketable debt is debt that cannot be resold on public markets. Currently, the vast majority of debt is marketable, with five types: Treasury bills (T-Bills), Treasury notes (T-Notes), Treasury bonds (T-Bonds), Treasury Inflation-Protected Securities (TIPS), and Treasury Floating Rate Notes (FRNs). T-Bills are the shortest-term securities, maturing in one year or less. T-Notes are the intermediary term Treasuries, maturing between 2 and 10 years. Finally, T-Bonds have the longest dated maturities, maturing in either 20 years or 30 years. TIPS are Treasuries that protect investors from inflation by increasing or decreasing the interest payment based on the rate of inflation. Lastly, FRNs have a two-year maturity, and their interest rates move with changes in the specific T-Bill interest rate.

All of the marketable securities, which account for approximately 98% of publicly held debt, are sold through an auction process. All Treasury auctions and the amount of securities being offered are scheduled and announced before the auction date. Participants in the auction can then submit a “competitive bid” for the securities they want. The bid includes the number of Treasuries a participant wishes to purchase and the interest rate at which they will buy them. Additionally, participants can enter a “non-competitive bid,” which simply states the number of Treasuries they would like to purchase, not the interest rate at which they will be purchased. Non-competitive bids, by not specifying an interest rate to purchase the securities, will accept whatever interest rate is ultimately determined by the auction process.

The Federal Reserve (the Fed) serves as the Treasury’s agent for selling its marketable securities and handles the mechanical aspects of the auction. In this role, the Fed works with primary dealers to help sell Treasuries to investors who bid on Treasuries. Primary dealers are securities brokers and dealers with a trading relationship with the New York Federal Reserve and are the largest purchasers of Treasuries sold at auction. Primary dealers are important intermediaries in the Treasury market and are responsible for most of the Treasuries sold to the secondary market.

After Treasury securities are put to auction, all bids are compiled, the competitive bids are tallied, and, through this open market process, Treasury determines the yield for the batch of Treasuries being offered. One component of this process is the “when-issued market.” This market consists of investors who request Treasuries from primary dealers and helps determine the open market yield. As the name suggests, these investors make requests for Treasuries before the auction is completed and will buy Treasuries once the auction is complete and primary dealers have finished purchasing them.

Financial Markets for Treasuries

Once the auction completes, Treasuries begin trading on the secondary market. The secondary market for Treasuries is one of the largest public markets in the world, much larger than the U.S. public equity markets. In 2024, the average daily trading volume (ADV) for U.S. Treasuries was \$907.9 billion for primary dealers alone, compared with \$607.7 billion for U.S. equities. U.S. Treasuries are considered some of the safest assets in the world and are considered nearly risk-free. As a result, Treasuries are often purchased for their safety, allowing investors to profit from the interest rate with the assurance that their investments will retain their value. However, the safety of U.S. Treasuries means the interest income is lower than that of other investment vehicles. Though the reduced interest rate does allow the U.S. government to borrow on more favorable terms than other nations. The safety also makes Treasuries the preferred vehicle for money market funds. Money market funds are the safest and most stable type of mutual funds. This is achieved by purchasing short-term debt, and the vast majority of that short-term debt, 99.5%, is in government securities, often mostly U.S. Treasuries. Money market funds are also unique: when cash is placed in a brokerage account, the broker-dealer generally keeps it in its money market fund as a proxy for actual cash.

One of the largest uses of U.S. Treasuries is in the repo and reverse repo market. Repo stands for repurchase agreement, and, per the moniker, it is a short-term cash loan, almost always overnight or up to 48 hours, and is collateralized primarily by U.S. Treasuries. A repo occurs between banks or other large financial institutions. A repo occurs when one institution lends cash to another, backed by the borrower’s securities, generally Treasuries. The lender then receives slightly more money than they loaned at the end of the loan period. The difference between the money loaned and the money received is the interest on the repo, and the rate is called the repo rate. A reverse repo is simply the opposite of a repo agreement, lending money to receive interest on a short-term basis, with the loan collateralized, again, mostly by Treasuries. Repos (and reverse repos) allow banks to meet their capital requirements and manage cash. Repos are thus a significant part of the financial system “plumbing,” and U.S. Treasuries, as collateral, underpin this market. In fact, in the third quarter of 2025, the average daily exposure of the repo

market was \$12.6 trillion.

Basis Trade

A unique part of the repo market is the basis trade. The basis trade profits through the small difference between the cash, or current, and futures prices of Treasuries. This difference is known as the basis. It is important to note that basis trades are not unique to the Treasury market, and this price discrepancy is traded on in multiple securities. However, due to the size and importance of the Treasury market, the basis trade in Treasuries has gained outsized attention and been the subject of policy debates. A basis trade utilizes the interplay among the Treasury, futures, and repo markets to generate a relatively small profit. As a result of the small profit, it is only economical for larger investors like hedge funds, although many other investors participate in the basis trade. The trade hinges on the repo market, and so investors are either providers or purchasers of repos, depending on the current repo rate. If investors are “buying the basis,” they will be participants in the repo market and, very basically, are looking to profit from the repo rate being lower than the price it would take to borrow a Treasury today and sell it on the futures market. The opposite trade, “selling the basis,” features investors as sellers of repos.

Policy concerns have been raised about the potential impacts of the basis trade on the Treasury market. Due to the small profits the basis trade makes, many investors need to leverage their trades, or take on debt, to make them economical. As a result, concerns have been raised that leveraged trades could lead to a rapid unwinding of basis trades, disrupting the broader Treasury market. Risks over the exposure of those providing leverage to basis traders have also been highlighted as potentially disruptive to the financial system. Lastly, the increase in basis trading has also been highlighted as a possibly disruptive market force, distorting the overall futures market. However, others have pointed to the benefits of the basis trade. Experts have highlighted how the basis trade has led to increased liquidity and decreased volatility. In fact, during the 2020 COVID pandemic, there were significant disruptions to the Treasury market. Subsequent studies by the Federal Reserve and others have shown that the basis trade was not a primary driver of Treasury market volatility, nor did stresses from this crisis on basis trade lead to greater illiquidity.

Additionally, as many have highlighted, it is difficult to attribute a rise in the basis trade simply to more investors proactively entering the market. The U.S. Treasury market, as explained previously, is an enormous fixed-income market that has grown steadily over the years. As a result, the growing size of the Treasury market needs to be considered when examining the increase in the basis trade, especially since increased consumer demand for any security must be matched by a seller. Basis traders have been foundational to providing the necessary liquidity for the Treasury futures market. Lastly, while many of the funds are levered to take advantage of the basis trade, experts contend that the funds are still properly capitalized and subject to legal requirements that ensure their safety. Additionally, lenders to investors participating in the basis trade argue that they employ sophisticated risk management tools to ensure their loans are not subject to undue risk. Calls for reform of the basis trade are unlikely to subside anytime soon. While more can always be done to improve market stability and efficiency, these reforms should balance the costs they could impose on the Treasury market, such as higher borrowing costs for the U.S. government, reduced liquidity, and potentially greater volatility.

The U.S. Treasury market is the largest government securities market in the world, vital to the U.S. financial system, and provides nearly risk-free securities to both Americans and investors globally. Any efforts to reform this incredibly important market and strengthen it must take into account the wide array of impacts and potential disruptions those reforms may cause.

Links to Other Resources

- BlackRock – [What are money market funds?](#)
- Congressional Research Service – [How Treasury Issues Debt](#)
- Federal Reserve – [The Treasury Securities Market: Overview and Recent Developments](#)
- Investopedia – [Basis Trading: Definition, How It Works, Example](#)

- Investopedia – [Repurchase Agreements Explained: Benefits, Examples, and Potential Risks](#)
- Managed Funds Association – [MFA on Treasury Market Structure](#)
- New York Federal Reserve – [The Treasury Auction Process: Objectives, Structure, and Recent Adaptations](#)
- Office of Financial Research – [Basis Trades and Treasury Market Illiquidity](#)
- Office of Financial Research – [Sizing the U.S. Repo Market](#)
- SIFMA – [Capital Markets Fact Book](#)
- Vanguard – [What are money market funds and how do they work?](#)