Convenience Yield of U.S. Treasuries - Quick Guide (ECON 413)

Atelier quick sheet

1) What is the convenience yield?

It is the extra 'perk' investors get from Treasuries beyond the coupon. Treasuries are a Swiss-army-knife asset: default-free, easy to sell, and easy to borrow against in repo. Those services are valuable, so Treasuries often yield a bit less than comparable assets. That yield gap reflects their convenience (safety + liquidity) value, which we infer from spreads.

2) Why does it matter?

- Explains why safe interest rates can be unusually low: investors 'pay' for safety/liquidity.
- Connects market plumbing to the macroeconomy: when collateral is scarce or balance sheets are tight, spreads move and real activity follows.
- Gives policy levers: QE/LSAPs and the Treasury bills-versus-bonds mix change the supply of money-like safe assets and the term premium.

3) What happens when the convenience yield rises? (positive shock)

- Treasury yields fall relative to private rates; term premia compress; the Aaa-10Y spread widens.
- Financing tightens for firms: corporate-Treasury and loan spreads widen; investment and output fall; unemployment rises; inflation eases.
- External channel: the dollar typically appreciates on impact, so net exports weaken.
- Policy tends to ease: the policy rate drifts down; near the lower bound, balance-sheet tools do more of the work.

4) What moves the convenience yield?

- Demand surges for safe, liquid assets: recessions, uncertainty spikes, flight-to-quality.
- Collateral scarcity and 'specialness': limited on-the-run supply, tight repo markets, bill shortages.
- Intermediation frictions: dealer balance-sheet limits, regulatory changes (e.g., leverage ratios), margin and haircut shifts.
- Public supply and policy: issuance mix (bills vs bonds), QE/LSAPs, buybacks, settlement bottlenecks (e.g., debt-ceiling windows).

5) How we measure it in class (simple proxies)

- Short end (bill convenience): SOFR 30-day compounded average minus 1-month T-bill yield.
- Term (safety/liquidity premium): Aaa corporate yield minus 10-year Treasury yield (our shock proxy).
- Offline fallback: build Aaa-10Y as AAAFFR + FEDFUNDS - GS10 before applying transformations.

6) Reading today's IRFs (in the app)

- Point vs cumulative: point IRFs show the response at each horizon; cumulative IRFs show the total change from impact to that horizon.
- UNRATE: a positive cumulative response means unemployment has risen relative to baseline by horizon h.
- USD index panel: a positive response indicates dollar appreciation (external, risk-off channel).

Takeaway

When Treasuries become more money-like, private borrowing becomes relatively more expensive. That risk-off shift shows up in wider spreads, softer activity and prices, and a stronger dollar. Policy can offset part of this by adjusting the supply and duration of safe assets.