What the proposed Mar-a-Lago Accord could mean for investors

Bond markets

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- The longer-term ambitions outlined in the so-called "Mar-a-Lago Accord" proposals aim to maintain the US dollar's dominance while weakening its value and lowering Treasury yields across the curve by withholding interest from and issuing ultra-long-dated debt to foreign official sector holders.
- Most countries are, in our view, unlikely to sign such an accord, but it may be imposed on those that rely on the US for defense. We think the proposed actions of the accord would likely undermine the credibility of the dollar as a reserve asset, could cause spikes in yields of longer-dated Treasuries, and benefit other high-quality government bonds, safe-haven currencies, and gold.
- While the US administration has not signaled its intention to implement these ideas, in this note, we try to quantify the possible contribution to lowering fiscal deficits and restoring the sustainability of the US government debt path. We would consider changes to our asset allocation in case some of those ideas gain traction.

Source: Getty

The aims of the accord

The global consensus underpinning the liberal world order—a multilateral, rules-based system promoting international trade and capital flows, and aimed at preventing the worst atrocities of the early 20th century—is increasingly at risk. The US, a chief architect of this consensus, was seen as the dominant superpower able to ensure that countries played by the rules. Many within the US now question whether this framework still serves America's economic and national security interests. The current administration seeks strong economic and security alliances with those countries that align themselves with the US. It expects balanced trade and a vibrant manufacturing sector, and a shared commitment to global security where countries address the security threats in their own backyards.

The "Mar-a-Lago Accord" is an extension of the evolution in thinking by certain individuals within the Trump administration about America's role in the world. It's generally understood to be based on a set of proposals that seek to preserve the US dollar's global dominance while also weakening its value. Maintaining the US dollar's dominance as the principal reserve currency and medium of exchange is paramount because it enables the US to project its power through global payments systems.[1] But the US dollar's dominance also has a downside—its persistent overvaluation. As the theory goes, the resulting currency strength hollows out the US manufacturing base and the country's competitiveness, which could potentially undermine America's strategic capability and military preparedness.

Adherents of these proposals claim that foreign countries have artificially weakened their currencies versus the US dollar to achieve export advantages in a wide range of products, which further reinforces US deindustrialization and widens the US trade deficit, creating large capital account surpluses held primarily in the form of US Treasury securities. Countries that participate in the Mar-a-Lago Accord would potentially be given some form of tariff relief[2] and security guarantees in exchange for their willingness to commit to the dollar's dominance in global payments, accept Treasury debt swaps, lower interest payments on their Treasury holdings, and ultimately contribute to a weaker US dollar.

While the US administration has provided few official details on what an eventual Mar-a-Lago Accord would include, officials within the administration are focused on currency adjustments and debt exchanges to address the structural twin federal budget and trade deficits. Therefore, we believe it is important to consider potential outcomes and assess possible investment consequences to support investment decisions in an environment where fiscal dynamics, global trade, and security questions are becoming more intertwined.

In addition to challenges around its implementation, negotiations for such a new accord would be difficult, in our view. While the Plaza Accord of 1985 featured the G5 countries and the Louvre Accord of 1987 the G6, they included central bank representatives who were able to take binding decisions. The current range of "relevant" countries would need to be wider, and ECB representatives, for example, do not hold the power to decide over foreign currency reserves held at the national central banks of euro member countries.

[1] As an example, the Society for Worldwide Interbank Financial Telecommunication (SWIFT) payments platform—together with US and allies' backing—voted to restrict seven Russian banks from accessing the US dollar payments system after Russia's invasion of Ukraine in 2022. In addition, the US together with the rest of the G7 and the European Union froze USD 300 billion of Russian central bank assets to inflict a financial penalty on the Russian government.

[2] It's important to note the ordering: tariffs announced and implemented first to then be able to generate the leverage in negotiations to achieve concessions to alter the international financial system and the government's debt profile. Tariffs are used to generate government revenue, but these can be relaxed or removed altogether in exchange for reduced interest expenses. Either way, the idea is to reduce the deficit.

Revisiting the US structural budget deficit

As we wrote in our December 2024 paper on "Taxes, spending, debt, and deficits under Trump 2.0," achieving a substantial reduction in the fiscal deficit, which stood at USD 2.2 trillion—or 7.6% of GDP—in 2024, is a critical yet difficult goal for many within the administration and Congress. The income generated from higher tariffs would likely prove insufficient to make a serious dent in the budget, to say nothing of the numerous counter-forces involved. For example, restoring US domestic production would lower imports and the tariff revenue. And tariffs that are too high would weigh on trade flows while risking a broad economic downturn, which would only worsen the budget deficit through higher social spending and lower economic activity. The administration objects to raising revenue through higher taxes, and efforts to materially curb current spending are unlikely to generate sufficient savings to balance the budget and would weigh on economic growth if taken to an extreme.

As interest on US government debt is now the single largest line item—at over 13% of general government revenues in 2024—in the budget and is growing as existing bonds mature, attention has shifted to potential ways to reduce the cost of debt. Because of the US dollar's reserve currency status, Treasury yields are arguably already lower than they would otherwise be. The proposed Mar-a-Lago Accord would put an additional burden of reducing interest expenses on foreign official holders. Several recent statements from members of the US administration stressed the importance of low long-term bond yields for achieving its economic and policy goals.

In our past reports on debt sustainability, we outlined four ways to reduce government debt:

1. economic growth through high productivity,
2. fiscal austerity,
3. financial repression, and
4. default / debt restructuring.

Regarding the first option, we believe that the US could slowly grow out of its debt if it manages to constrain its fiscal deficit to about 3.0-3.5% of GDP, which means it has to resort to the other three options if the government wants to stop the rise in the debt ratio.

With regard to the second option, cutting back the size of government institutions under initiatives of the Department of Government Efficiency (DOGE) is the only example of *fiscal austerity,* and we have yet to see its effects in hard numbers. Breakdowns of current government spending

—total nondefense discretionary spending was USD 1tr in 2024—suggest that even sharp cuts there can only shave off a small portion of the overall deficit. According to the Congressional Budget Office (CBO), the federal government's 2.3mn workers were employed at a cost of USD 271bn in 2022 (about 1% of GDP), so even massive layoffs can only generate moderate cost savings relative to a USD 2.2tr fiscal deficit.

The ongoing budget process may deliver further spending cuts, but also revenue cuts, and it is yet unclear to what extent it will reduce the fiscal deficit. In its 25 March update, Moody's projected the federal government deficit to widen "to about 8.5% of GDP by 2035 from around 6.3% in 2025, driven by increased interest payments and health-related entitlement costs." This would result in a rise of the federal government debt ratio to 130% of GDP from close to 100% this year. The general government debt ratio, including state and municipal debt, which is what most other countries typically report, stood at 121% of GDP by the end of 2024.

Moody's forecasts include an extension of the 2017 Tax Cuts and Jobs Act and no material additional tax cuts (like proposed corporate tax reductions and exclusion from taxes of overtime and tipped income as well as social security benefits). Also, it includes only small spending cuts, reflecting an expectation for no bipartisan support for entitlement reform.

Another avenue for financial repression

A long-term ambition in the proposed Mar-a-Lago Accord is to devalue the USD, ideally by having foreign reserve holders sell US dollar assets in exchange for their national currencies. Selling pressure on US Treasuries and rising yields are a notable risk, endangering the administration's ambition to also achieve lower Treasury yields. Therefore, several proposals clearly fall into the wider definition of *financial repression*—i.e., measures where the government uses its regulatory and political powers to constrain or lower the cost of its debt.

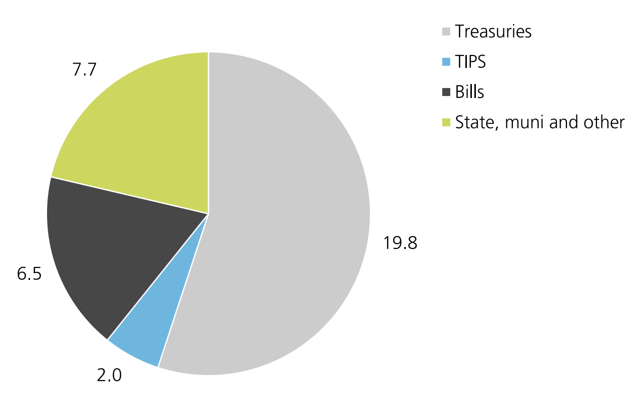
Key proposals include withholding part of the interest on Treasuries and issuing so-called century bonds or even perpetual bonds to certain foreign official sector holders. The authors justify paying less or no interest to those bondholders as compensation for the US providing a safe reserve asset and access to its security umbrella. From a credit perspective, it is *foreign financial repression*. It can be viewed as an extension of traditional domestic financial repression, which the US has used in the past, whereby certain regulated entities are required to hold large amounts of Treasuries on their balance sheet or where reference interest rates are being capped in a way that results in negative real interest rates. Typically, financial repression works best if supported by the central bank. A likely change in leadership at the Fed in 2026 could raise support for possible efforts by the Treasury to engage in financial repression.

Withholding interest / charging a fee

The paper suggests the US may use the International Emergency Economic Powers Act (IEEPA) from 1977 to make foreign reserve accumulation less attractive by "imposing a user fee on foreign official holders of Treasury securities," by withholding part of the coupon payments. Even if only applied to certain official sector creditors, such a measure would likely scare many private holders of Treasuries. And if it's applied to existing bonds, it could even cross the line to be considered an event of *default*. Disguising it as a fee instead of a non-payment of the full interest when due would still likely be captured by rating agencies' definition of a default. For example, Moody's states as one of four events constituting a default: "a change in the payment terms of a credit agreement or indenture imposed by a third party such as the sovereign that results in a diminished financial obligation, such as a forced currency re-denomination or a forced change in some other aspect of the original promise, such as indexation or maturity."

A possible alternative would be to include such "fee" provisions only into newly issued Treasuries, so that investors know the terms ahead of purchase. However, this could lead to a perceived seniority of older bonds over those with the interest withholding / fee provision, most likely leading to different yields as investors who are (currently) not targeted by the fee would still prefer the old bonds.

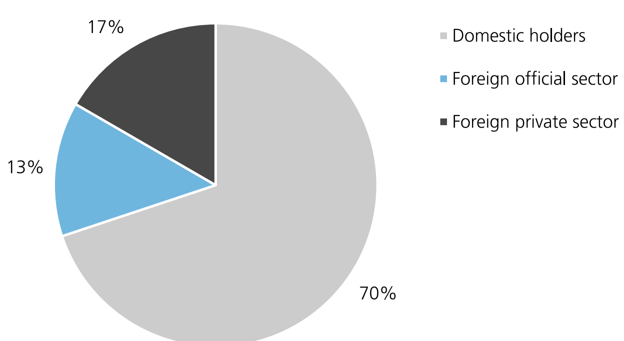
Figure 1 - Breakdown of USD 36tr in US government debt



Source: Bloomberg, IMF, as of 14 April 2025.

From a fiscal perspective, the share of Treasuries from which interest would be partially withheld would need to be sufficiently large to have any meaningful impact on the budget. There are USD 19.8tr of nominal bonds, USD 2.0tr of inflation-linked Treasuries outstanding, and USD 6.5tr of Treasury bills (see Fig. 1). US Treasury data from January suggests that a total of USD 8.5tr are held by foreigners, of which USD 3.4tr are Treasury bonds and notes held by the foreign official sector (see Fig. 2). Withholding one percent of interest from all of them would reduce spending by USD 34bn, or 0.3% of this year's expected general government revenues, amounting to 0.11% of GDP. Of course, the government could apply higher or different fees to different countries, but the overall coupon due on the bonds would act as a cap for this approach.

Figure 2 - Holders of US Treasury securities (USD 28tr)



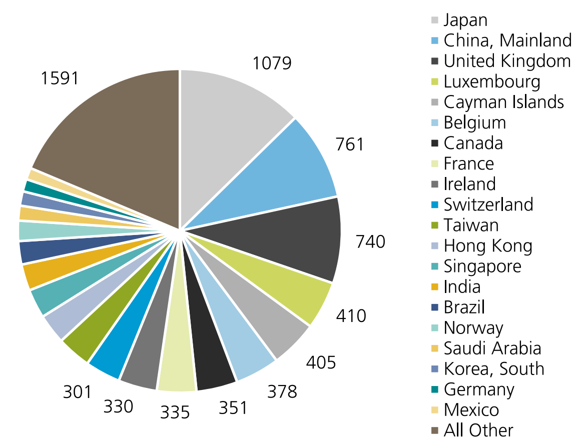
Source: US Treasury, as of 31 January 2025.

Also, the administration could consider extending the fee beyond the official sector—targeting the USD 8.5tr instead of only the USD 3.4tr held by the official sector. Doing so would also address the issue that some countries hold Treasuries through funds domiciled in other countries, which is not captured by the Treasury data used in Figures 2 and 3. This would likely result in severe turmoil in global bond markets and while it could reduce foreign holdings of Treasuries, it could also challenge the US dollar's reserve asset status, as investors would diversify into alternative assets (like other government bonds and gold) much like they did after Russia's central bank assets were frozen.

Century bonds

A second proposal is to issue a special type of long-term bond only to official sector holders that the US administration intends to effectively charge for providing a safe reserve asset and protection under its security umbrella (see Fig. 3). These replacement bonds could have long tenors, like 100 years or even perpetual structures, and carry very low or nonexistent coupons. Currently, a large share of foreign official sector holdings are in short-dated bonds.

Figure 3 - Foreign holders of Treasury securities by economy (USD bn)



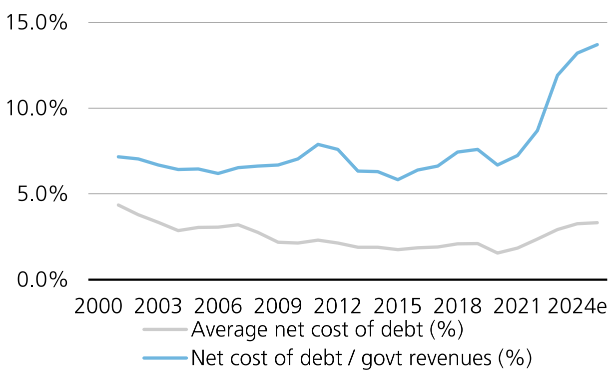
Source: US Treasury, as of 31 January 2025. Treasury International Capital System data does not identify the ultimate owner, for example of bonds held by investment funds.

To illustrate the economic costs that affected governments would need to accept, and the likely political pressure required for them to buy such bonds at par value (100), note that a 30-year zero coupon Treasury would have a fair cash price of 24 at a current market yield of 4.8%. For a 100-year zero coupon note, a fair price (using the same yield, as there is no Treasury bond beyond 30 years) would be 9. Given tariffs are paid by US consumers of imports, accepting the economic impact of tariffs can be preferable to a foreign country, depending on the amount of century bonds it would be asked to hold and the relevance of protection through the US security umbrella.

By issuing a separate type of bonds bilaterally to specific countries, there would be no direct credit implications for the other Treasury securities outstanding. If such investors gradually swap from existing Treasuries to century bonds, the pool of Treasuries would shrink accordingly (ignoring new issuance to finance persistent deficits). Therefore, this form of financial repression contains somewhat less risk of scaring private holders of existing Treasuries, but can of course still lead to concerns about further unorthodox bond market measures.

From a credit perspective, lengthening the funding profile and reducing the fiscal sensitivity to swings in interest rates would be a positive. The extent of the impact would depend on the amount of debt being swapped into such century bonds relative to the overall debt burden. In the unlikely "best case," where all of the USD 3.4tr of Treasuries held by foreign official holders (equivalent to 15% of the Treasury market volume) would be swapped, the US may save about USD 100bn in annual interest expenses—about 1% of this year's expected general government revenues, or 0.33% of GDP. As a reminder, the US spent 13.7% of revenues on debt service in 2024 (see Fig. 4).

Figure 4 - US general government debt costs have increased



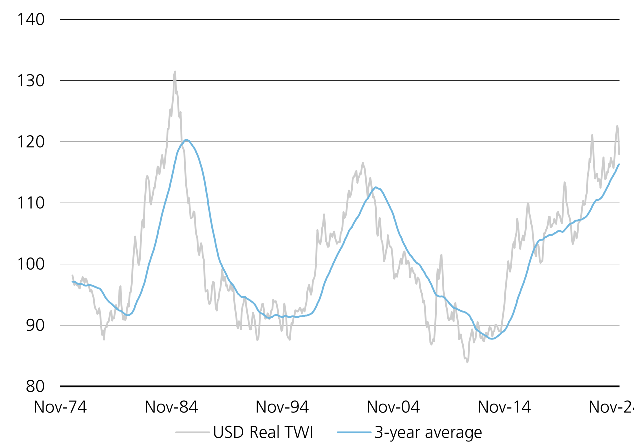
Source: UBS, IMF, as of 14 April 2025

Market implications

We think the measures suggested would likely result in heightened uncertainty about the safe-haven status of Treasuries, but they would likely help the US government mitigate part of its fiscal pressures. Returning to a sustainable debt path still requires Congress to legislate measures to meaningfully reduce the budget deficit. As a result, we would expect yields of longer-dated Treasuries to remain vulnerable to spikes as foreign investors diversify their safe assets or reserve holdings into other high-quality government bonds, and as US investors reduce their allocations over fears of financial repression leading to negative real yields. Such episodes can be countered by further financial repression, lowering yields again. Aside from a generally higher term premium, we would also expect heightened volatility, reducing the risk-adjusted appeal of longer-dated bonds compared to shorter tenors.

The USD's rich valuation when looking back over the last 50 years, with sizeable twin deficits and elevated investment positions by foreign investors in the US, suggests that an adjustment to a lower USD equilibrium would unlikely be very gradual, especially against highly liquid G10 and safe haven currencies. Mean reverting to a longer-term average —trade weighted—would initially mean mid-teen downside for the USD from current levels. A resetting of the USD would likely come with a shift higher in currency market volatility over a longer period as well. Potentially larger currency trends and higher volatility would speak in favor of more active currency management (hedging activity).

Figure 5 - In real trade-weighted terms, the USD stands at lofty levels
Monthly data

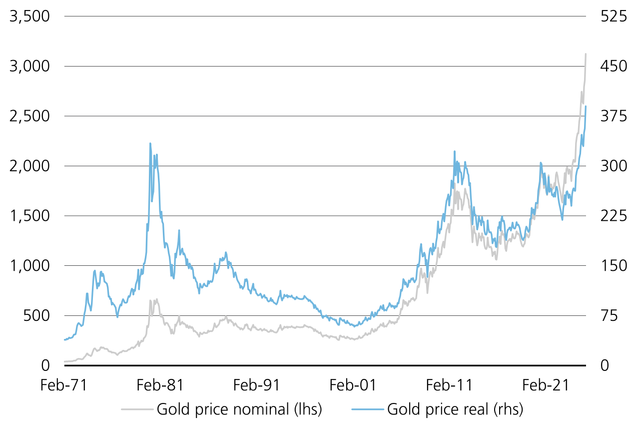


Source: UBS, Bloomberg, as of 14 April 2025

The knock-on effect of the USD getting reset wouldn't just impact currency markets. Commodity markets are generally quoted in USD but mainly produced and consumed outside the US. Over time, a larger USD decline would speak for higher commodity prices. Moreover, concerns over the safe-haven status of US Treasuries would likely continue to play in favor of commodities such as precious metals, mainly gold. We have already seen investors allocating more to gold in an effort to reduce USD exposure and reap the potential gains of gold's diversification benefits. This has pushed gold to elevated levels from a production cost perspective while providing price support for the broader sector.

Figure 6 - Gold prices have skyrocketed in nominal and real terms already

Monthly data, values in USD/oz



Source: UBS, Bloomberg, as of 14 April 2025

Appendix

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