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Treasury Financing Alternatives: Judy Shelton's Treasury Trust Bonds

With US Treasury yields elevated, the government continues to issue debt at interest rates unseen since before the 2008 financial crisis, raising fundamental questions on how to finance spending without locking in prohibitively high costs. Our previous discussion of yen-financing as an alternative government funding mechanism focused on exploiting the vast pools of excess liquidity in Japan, where yields remain at sub-1.5% levels, but there may be another route—one that draws on the stability and intrinsic value of gold.

Judy Shelton has proposed an alternative to traditional Treasury debt issuance: gold-linked bonds, or "Treasury Trust Bonds" (TTBs see Shelton, *Cato Journal*, 2012). Unlike conventional fiat-backed securities, these bonds would offer investors the choice at maturity to redeem in either US dollars or a fixed weight of gold. The fundamental appeal of this structure lies not in forcing the US to part with its gold reserves but in leveraging their presence as a backstop, which in turn would allow the government to issue debt at lower rates than those dictated by a purely fiat system. Gold's historical role as a stabilizing asset offers built-in assurances against devaluation, making these bonds attractive to investors concerned with the potential weakening of the dollar by either Fed error or fiscal profligacy.

Because gold is both a non-defaultable and non-yielding asset yet maintains its purchasing power across time, Treasury Trust Bonds would likely command a far lower interest rate than current Treasury issuances, simply because their linkage to gold instills confidence. The US government currently pays over 4.5% on long-term Treasury debt, a figure that reflects market uncertainty about inflation, fiscal sustainability, and the trajectory of Federal Reserve policy. By contrast, gold-linked bonds, backed by tangible reserves, could attract sovereign wealth funds, foreign central banks, and institutional investors at much lower yields. The structure of these bonds—likely zero-coupon, meaning they sell at a discount but mature at full face value—would further reduce immediate financing costs for the government while reassuring investors that their purchasing power remains protected.

The appeal extends beyond lower borrowing costs. Treasury Trust Bonds would effectively reprice US gold reserves for financing purposes without requiring a full return to the gold standard. Currently, the US Treasury holds 261,498,926 ounces of gold—but it still prices those reserves at just $42.22 per ounce, a relic of the Bretton Woods era. This outdated accounting metric pegs the total value of US gold reserves at just $11 billion, whereas at today's market price of over $2,900 per ounce, the real value exceeds $758 billion. This means the Treasury is sitting on an underutilized asset worth nearly three-quarters of a trillion dollars—one that could serve as a confidence anchor for a new class of low-interest Treasury securities. Rather than physically selling any gold, the mere presence of this reserve backing could allow for more favorable debt issuance terms, reducing reliance on Federal Reserve-driven monetary conditions.

This mechanism also leaves Federal Reserve machinations outside of the debt equation for both the Treasury and investors. Rather than relying on interest rate policy dictated by the Fed, Treasury Trust Bonds offer an independent, market-driven alternative that directly aligns investor incentives with long-term value preservation. At a time when Powell's Fed remains steadfast in holding rates higher for longer, dismissing concerns about mortgage affordability and broader financial conditions, Shelton's proposal provides a funding mechanism that bypasses monetary policy uncertainty entirely.

The Zero-Coupon Advantage with a Gold Tie-In

At first glance, the zero-coupon nature of Treasury Trust Bonds might seem to undermine their potential interest rate advantage, given that zero-coupon bonds traditionally carry higher yields than coupon-bearing equivalents. However, the gold linkage fundamentally changes that equation. Here's why:

1. **Gold as a Trust Anchor**: The yield premium on zero-coupon bonds generally arises from inflation risk and the lack of coupon payments. But by offering gold as a redemption option, the Treasury neutralizes the primary driver of that premium. Gold is a non-defaultable, inflation-resistant asset that inherently boosts investor confidence, reducing the yield required to attract buyers.
2. **Market Discipline and Investor Behavior**: Gold-linked zero-coupon bonds provide built-in market discipline. If inflation fears mount, investors may choose gold redemption, signaling concerns about monetary stability. But as long as inflation expectations remain contained, investors will likely accept lower yields due to the safety net gold offers.
3. **Immediate Fiscal Relief**: With zero-coupon TTBs, the Treasury avoids near-term interest expenses entirely. In a fiscal environment where deficits are swelling and interest payments consume an increasing share of the budget, this structure grants policymakers breathing room. By deferring interest costs and potentially lowering overall yields through the gold premium, these bonds offer a double-edged fiscal advantage.
4. **Historical Precedent for Gold-Linked Bonds**: Historical evidence suggests that gold-anchored sovereign bonds have consistently commanded lower yields than their fiat-backed counterparts. Markets tend to reward the monetary discipline implied by gold convertibility with lower required returns.

Of course, the success of Treasury Trust Bonds hinges on more than just the structural appeal of gold-backed stability. If the Federal Reserve were to allow persistent dollar weakness—such as the 55+% devaluation of the dollar against gold witnessed during the Biden administration—investors would logically opt for gold redemption over weaker dollars. This dynamic could strain reserves, undermining the bonds` cost-saving intent. As such, the Treasury and the Fed would need to coordinate policy to maintain a relatively stable gold-dollar exchange rate, ensuring the bonds` long-term viability. Without that coordination, TTBs risk becoming a conduit for draining US gold reserves.

The result is a bond instrument that subverts the traditional relationship between coupon structure and yield. While zero-coupon bonds typically yield more than coupon-bearing bonds, TTBs` gold tie-in could invert that relationship, delivering long-term financing at rates well below current Treasury yields.

This mechanism, in effect, reintroduces the idea of gold fixity into longer-term debt instruments. To approximate where rates might stand, we should look at comparable eras when the dollar was linked to gold and US citizens were allowed to own gold (unlike during the 1933–1974 period). The most relevant period is 1870–1914, when long-term Treasury yields typically ranged from 3.0% to 3.5%, a full 100 to 150 basis points below current levels.

Skeptics may argue that the introduction of gold-backed debt could disrupt fiat-based monetary frameworks or create unwanted volatility in gold markets. Yet, the broader financial system has already begun to shift in ways that reflect growing skepticism of unbacked fiat regimes. Emerging market central banks, including those in China, India, and Turkey, have aggressively increased gold reserves over the past two years, signaling a move away from US dollar dependency. Introducing a gold-linked bond would not only align with this evolving macroeconomic reality but also provide the US with a strategic advantage: securing lower borrowing costs while reinforcing the stability of its debt markets.

Additionally, the act of financing a significant portion of long-term bond issuance through Treasury Trust Bonds could, by itself, exert downward pressure on Treasury yields through the basic dynamics of supply and demand. In 2022, the US Treasury sold $8.3 trillion in long-term bonds. If Treasury Trust Bonds were introduced to cover even 10% of that volume, the resulting reduction in the supply of standard Treasury securities could, by making those securities suddenly scarcer, increase their market price and lower yields significantly. This supply-driven yield compression, if strategically executed, could ease borrowing costs across the broader Treasury curve.

Of course, this is only one possible avenue for reducing the government`s borrowing costs. As previously discussed, issuing yen-denominated bonds to access Japan’s abundant liquidity pools is another potential option. There may well be others. The task for the new administration is not to adopt any single strategy but rather to explore a range of creative, cost-effective financing approaches—whether through Treasury Trust Bonds, yen-based issuance, or other innovations that leverage the strengths of the US`s financial position.

The stakes are clear: relying solely on traditional Treasury issuance leaves the US beholden to the Fed’s restrictive stance, driving higher interest payments that balloon the deficit and crowd out more productive uses of government funds. Treasury Trust Bonds, by offering investors the certainty of a gold-backed redemption option without depleting reserves, provide a promising alternative—one grounded in historical monetary principles yet uniquely suited to the present financial environment. It could lay the groundwork for a more resilient dollar, leveraging gold`s historical stability in an era of fiscal uncertainty.

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