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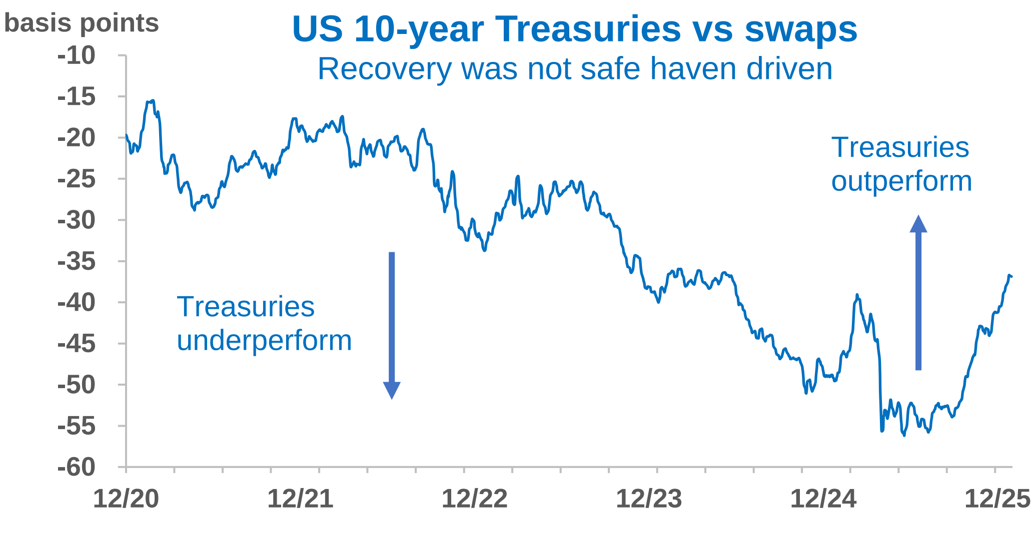
Testing US Treasury safe-haven status

When safe-haven status faltered, Treasuries still rallied. Despite a year dominated by bearish narratives - bond vigilantism, heavy issuance, and a softer dollar - the second half of 2025 delivered one of the strongest stretches of Treasury outperformance versus swaps since the Global Financial Crisis (GFC, 2008). That wasn't obvious from the headlines. Treasuries have struggled to behave like a reliable safe haven during recent geopolitical stress, and with a focus on Venezuela, markets now face a fresh test of whether that dynamic is shifting.

The chart below helps frame the story: a clear reversal in swap spreads, pointing to a recovery in Treasuries that wasn't driven by flight-to-quality flows - but by something deeper.

The spread reflects the difference between the fixed leg of an interest rate swap and the yield on a US Treasury of the same maturity - a clean measure of the Treasury risk premium relative to the risk-free curve, proxied by SOFR. A reversal in the spread occurred through the second half of 2025, reflecting Treasury outperformance, but viewed over the last five years it is in the middle of the range.

Because spreads are quoted as ***swap yield minus Treasury yield***, they have been negative since before the GFC. Negative spreads can be counterintuitive - becoming "less negative" as Treasuries outperform - so the chart uses arrows to make the direction of travel clear.



Source: Bloomberg. US 10Y SOFR (Sovereign Overnight Financing Rate) minus US 10Y Treasury

Swap spreads matter because they offer insight into risk appetite, liquidity conditions, and demand for sovereign debt. Investors use them to assess relative value; issuers use them to understand all-in funding costs. Several forces typically shape spreads, including:

- **Government bond supply**, often driven by shifts in the budget deficit
- **Safe-haven demand** for the US dollar and Treasuries
- **Structural and regulatory factors** affecting the supply-demand balance

To understand the reversal through the second half of 2025 - and what it may mean for 2026 - it's useful to break the story into four themes.

1. Bond supply

Expectations of overwhelming Treasury issuance pushing yields higher simply didn't materialise in 2025. Debt levels remain elevated, but the economy was robust and tariff revenues supported the fiscal picture. By November 2025, the budget deficit had narrowed to 5.9% of GDP, 0.4% lower than the previous year. Markets react most to surprises, and investors entered 2025 positioned for higher yields, not lower. From this we infer that absence of the feared supply shock likely contributed to Treasuries outperforming swaps.

2. Shifts in safe-haven demand

Last April's volatility - triggered by larger-than-expected tariff announcements - led to a period of Treasury underperformance. As highlighted by the Treasury Borrowing Advisory Committee (29 April 2025), the episode saw a rise in term premium, wider bid-offer spreads, and other signs of stress, during which Treasuries did not behave as the traditional safe haven. The geopolitical tensions that have greeted the start of 2026 will reveal whether that dynamic persists or begins to reverse. And events that drive safe-haven demand don't have to be geopolitical, they could also come from adverse market moves, for example in stocks or credit.

3. Anticipation of new structural demand

A more supportive force has been the prospect of increased structural demand for Treasuries. Discussions around recalibrating the Supplementary Leverage Ratio (SLR) and the introduction of the GENIUS Act - both prominent in early 2025 - suggest potentially significant capacity for banks and stablecoin issuers to hold more Treasuries. Estimates vary widely, but the potential scale runs into the USD trillions.

Timeframes remain uncertain. Some positioning may already reflect expectations of SLR reform, and banks still face other constraints such as the Liquidity Coverage Ratio and G-SIB surcharges. Stablecoin-related demand is likely to concentrate in bills, so the impact on longer maturities will depend on how the US Treasury adapts issuance patterns accordingly.

4. The shape of the swap-spread curve

The term structure adds another layer. Longer-dated Treasuries have outperformed swaps more than shorter maturities. Following the tariff-driven shock in April, the turning point for the 10-year spread came on 15 July 2025, when the two-year, 10-year, and 30-year spreads stood at –25bp, –56bp, and –87bp respectively. Since then, the Treasury curve has flattened versus swaps, with the 10-year spread outperforming the two-year by around 10bp and the 30-year broadly tracking the 10-year.

Where next for the 10-year swap spread?

The chart shows a full reversal in Treasury performance versus swaps - more than just a bounce. It is also on the way to a mean reversion of the multi-year trend. If overstated supply fears and underestimated structural demand were the key forces in 2025, the swing factor for 2026 may be whether safe haven status reasserts itself.

Some will point to the early end of QT or curve management speculation. But if the market simply reached peak pessimism and Treasuries became too cheap, then the recent outperformance may be less about policy and more about positioning.

Swap spreads often turn before sentiment does. With Treasuries outperforming across the curve, the market may be quietly signalling that the worst of the bearish narrative is behind us - and that a new chapter is beginning.