The United States and its Creditors: How Risky is the US External Position?

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Motivation

- The **international economic order** is undergoing profound shifts amid rising **geoeconomic tensions**.

- The center country at the heart of the uncertainty is the **United States:**
  - **Large net debtor** vis-à-vis the rest of the world. **NIIP position: -90% of GDP** (end 2024)
  - **Rising external liabilities + higher interest rates → Investment income balance turned negative (since 2024)**
  - **~1.4 percentage points of GDP** deterioration from late 2010s peak.

- **A further deterioration is likely**, as net external debt liabilities continue to increase.

- The **epicenter of geoeconomic risk** may now lie **within the U.S. itself.**

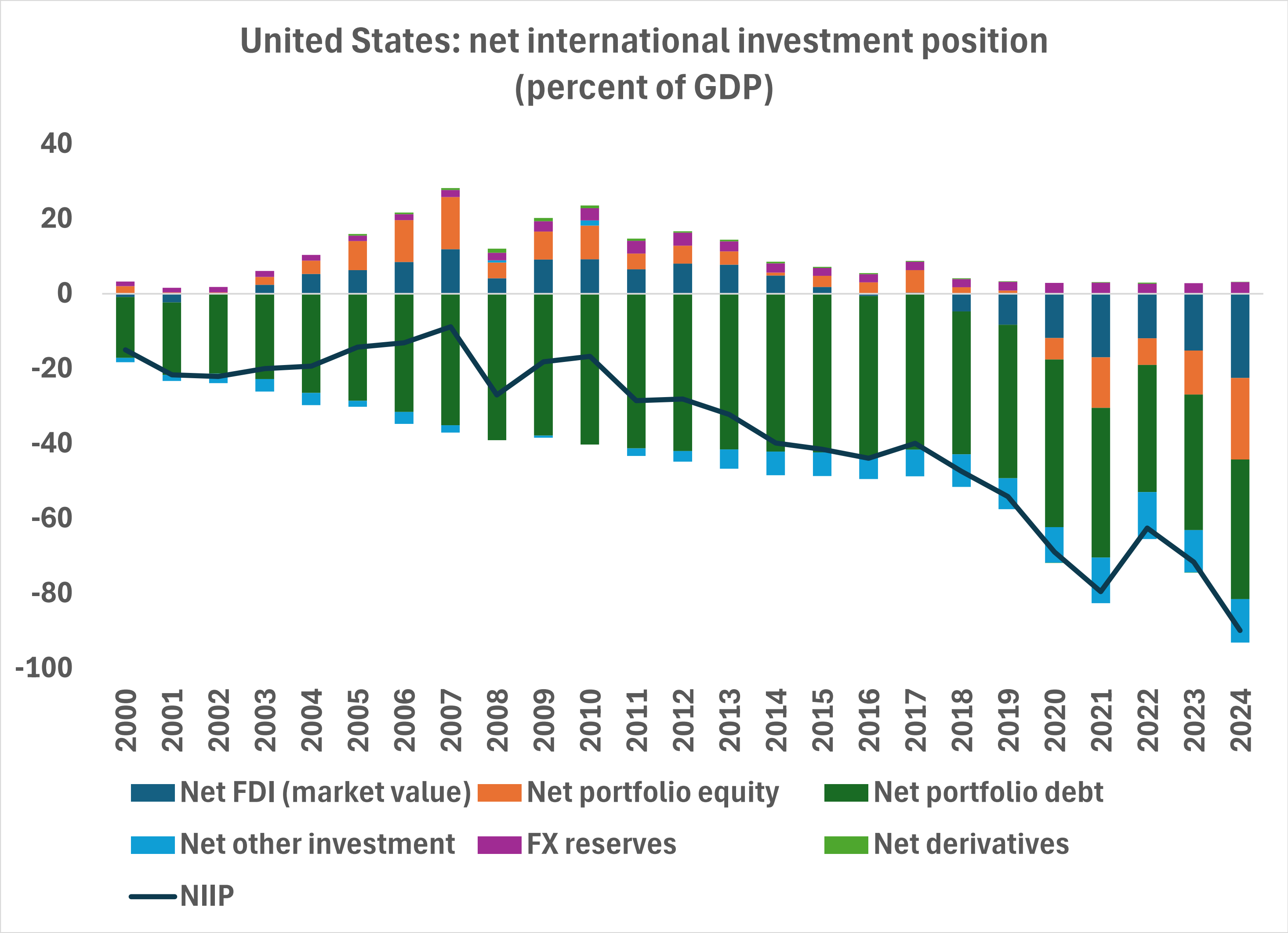
Motivation

- This paper analyzes **the changing structure** of the **U.S. external portfolio.**
  - Examines the factors underpinning **foreign demand for U.S. assets**, particularly **U.S. Treasury securities**.

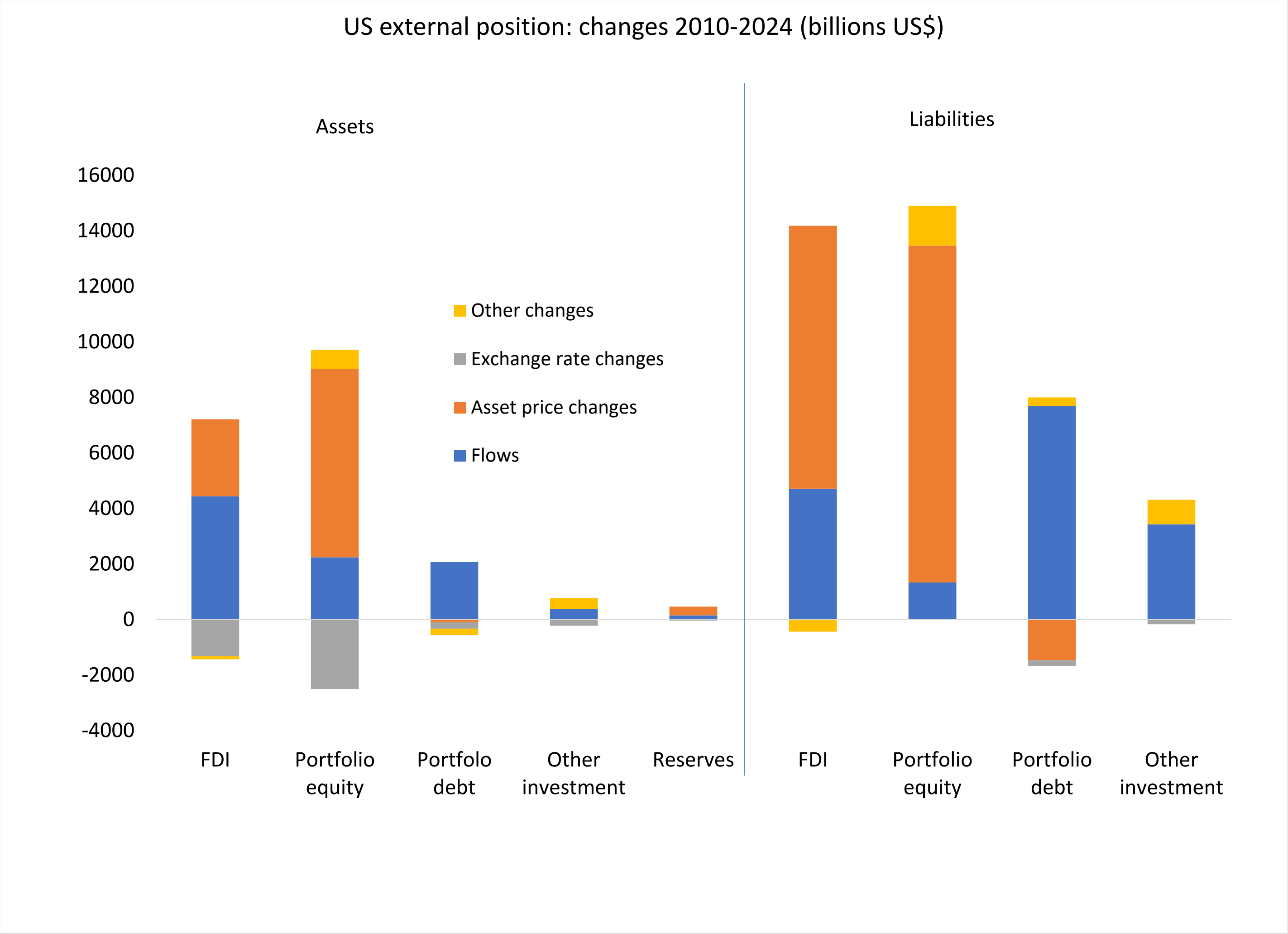
- Examines compositional shifts in **U.S. bilateral external positions:**
  - **Geographically**
  - **By asset class**
  - Address the **"financial center bias"** by providing estimates of creditor positions closer to a **nationality-based concept.**
  - **By investor class** (official vs. private investors).

- Assess how these dynamics may affect the **riskiness** of the U.S. external position and portfolio preferences for U.S. assets.

The US NIIP by Financial Instrument (% of GDP)

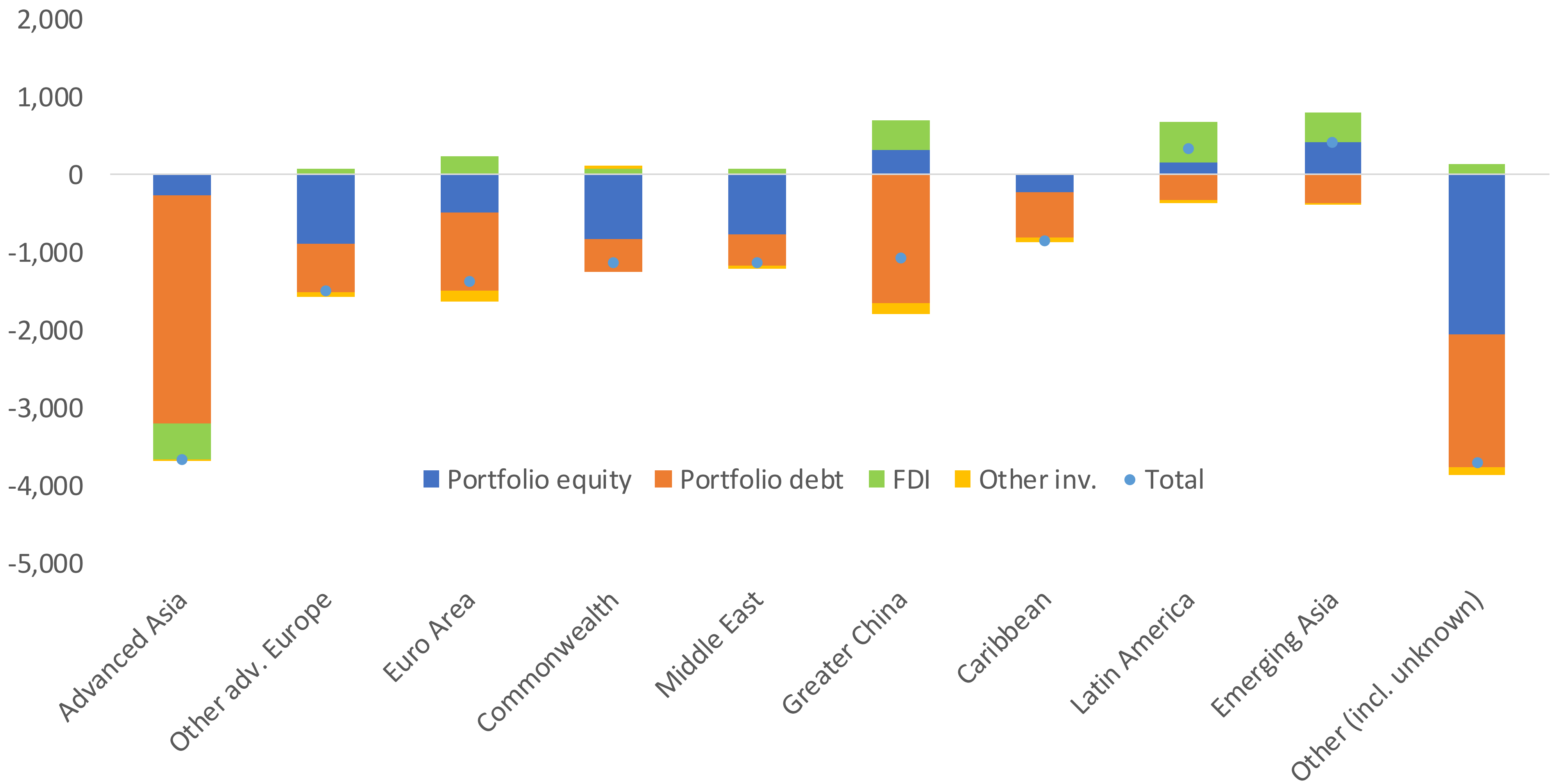


Flows and Valuation changes have shaped the Evolution of the US NIIP by Asset Class



The Geography of US Net External Liabilities in 2023 by Asset Class

(partial nationality-based correction, billions US$)



How have the creditors changed? US net external position by region (2017 vs 2023, billions US$)

Advanced economies dominate U.S. gross and net financial exposures

- Several factors explain these changes.
  - Recent large current account surpluses in advanced European and Asian economies.
  - A favorable valuation effect.
  - China has been diversifying its allocation of external assets since the end of the GFC (allocating surplus dollars elsewhere).

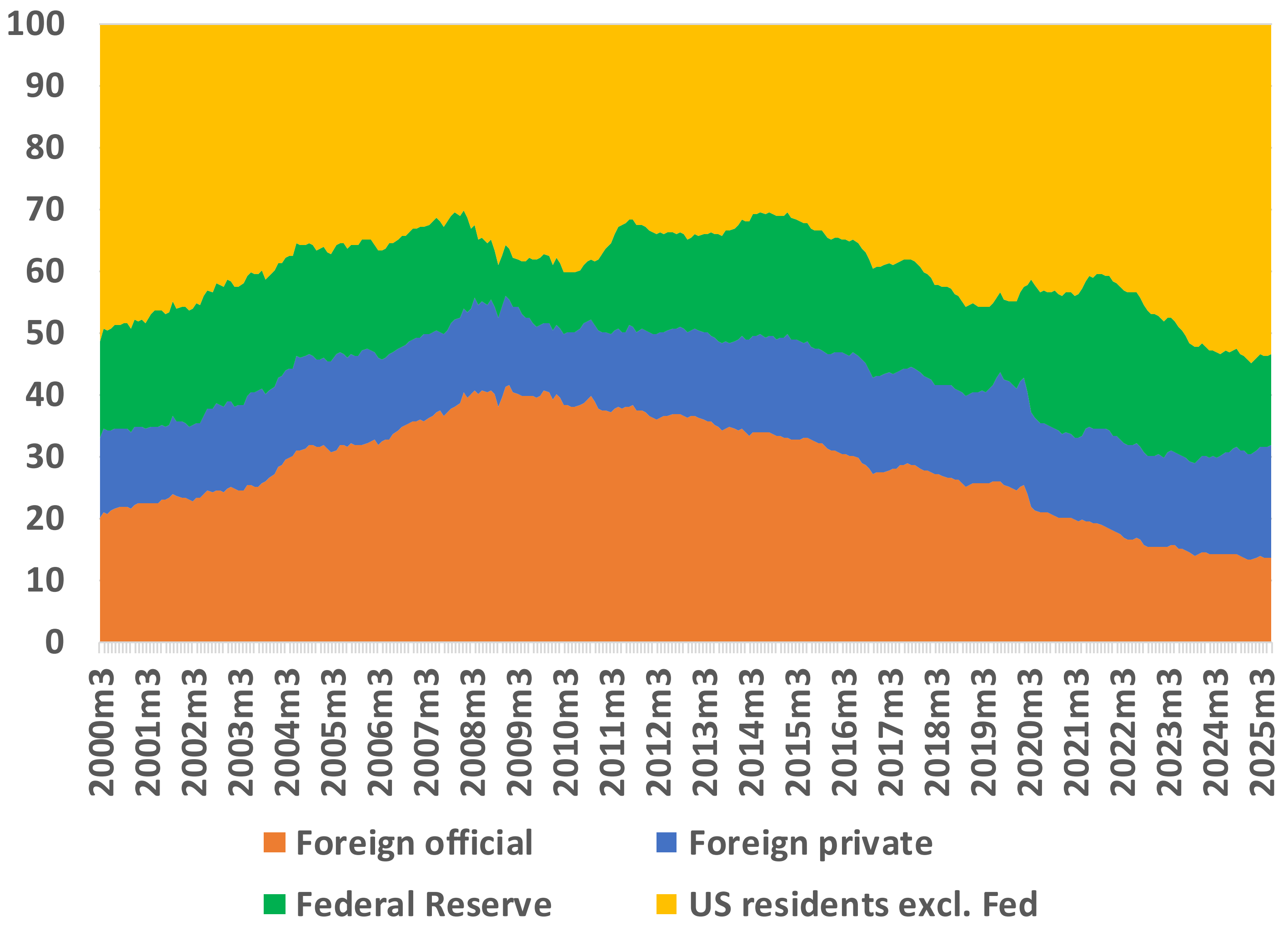
- The nationality correction **reduces certain creditor positions**. E .g., **the euro area**. Flows intermediated via Ireland, Luxembourg, and the Netherlands.
  - Increases uncertainty about creditors' identities and sectoral composition.

What are the risk implications of these findings?

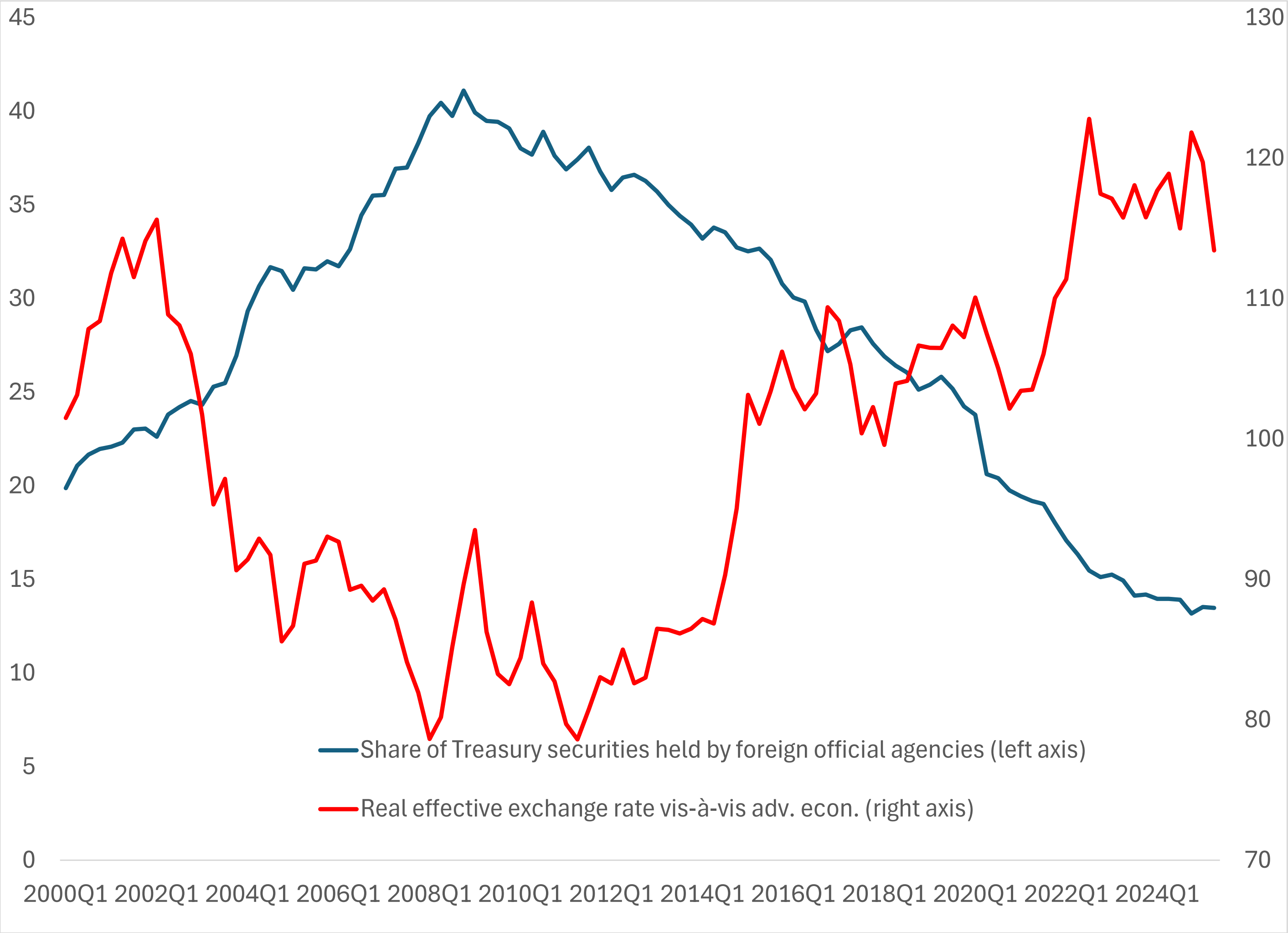
- IIP statistics point to **rising equity liabilities** (portfolio investment & FDI) …
- …but steadily rising **external net debt** poses more serious challenges
  - **Unfavorable fiscal dynamics** and
  - Higher **real interest rates** over the past few years **increased debt service costs.**
- 2nd half of paper focuses on **foreign holdings of U.S. Treasury securities** →
  - **60 percent** of **foreign holdings of U.S. bonds** and
  - **over one-third of U.S. Treasury securities outstanding**.

Holders of U.S. Marketable Treasury Securities

- There is a **large shift** in the pattern of **foreign holdings of USTs.**
- **A diminishing role for foreign official investors** who accounted for the lion's share in 2008.
- Offset by a **rising role for private investors.**



The foreign official share of U.S. treasury securities and the real effective exchange rate are strongly correlated.



The Aggregate Foreign Official Holdings Share

Baseline specification using monthly data (2000 to mid-2025):

$$s_{FO,t} = \alpha + \beta_1 REER_{US_{AE},t} + \beta_2 s_{FRB,t} + \beta_3 \frac{FX\ Reserves}{World\ GDP}_t + \beta_4\, RORO_t + \beta_5\, GFI_t + \epsilon_t,$$

Where:

- $s_{FO,t}$ is the aggregate foreign official holdings share of US Treasuries/US marketable debt
- $REER_{US_{AE},t}$ is the real effective exchange rate of the United States vis-à-vis advanced economies
- $s_{FRB,t}$ captures the Federal Reserve's holdings of outstanding Treasuries,
- $\frac{FX\ Reserves}{World\ GDP}_t$ is a scaling variable,
- $RORO_t$ is the risk-on risk-off index from Chari et. al. (2025)
- GFI_t is a geopolitical fragmentation index from Fernandez-Villaverde (2025).

The Aggregate Foreign Official Holdings Share

Table 1 Determinants of Foreign Official Holdings of US Treasury Securities

	Dependent Variable: Foreign Official Holdings Share (%)				
VARIABLES	(1)	(2)	(3)	(4)	(5)
Real Exchange Rate (US vs. AEs)	-0.586***	-0.531***	-0.548***	-0.271***	-0.290***
	(0.0135)	(0.0162)	(0.0151)	(0.0143)	(0.0143)
FX Reserves Ratio (% World GDP)	0.0212***	0.0204***	0.0445***	0.0581***	0.0635***
	(0.00647)	(0.00628)	(0.00681)	(0.00461)	(0.00368)
Federal Reserve UST share (%)		-0.437***	-0.460***	-0.448***	-0.457***
		(0.0499)	(0.0472)	(0.0343)	(0.0332)
RORO index (Z-score)			0.0291		-0.00997
			(0.0238)		(0.0165)
Geopolitical Fragmentation Index				-8.206***	-8.046***
				(0.329)	(0.323)
Constant	83.98***	86.11***	85.16***	54.20***	55.50***
	(1.611)	(1.593)	(1.516)	(1.664)	(1.609)
Observations	304	304	263	289	251
R-squared	0.839	0.871	0.896	0.950	0.965

Standard errors in parentheses
*** p<0.01, ** p<0.05, * p<0.1

The Aggregate Foreign Official Holdings Share

- The **decline** in the **foreign official holdings share** is well explained by:
  - **much-reduced reserve accumulation** during the past decade,
  - **increased Federal Reserve Treasury holdings**, and
  - **a hefty dollar appreciation** against other reserve currencies from advanced economies (negative correlation with the REER). **Central banks rebalance their portfolios** to **avoid large swings** in **currency shares.** Economic significance (elasticity of -1)
  - **geopolitical fragmentation reduces foreign official holdings of USTs.**

- Absent a **renewed push to accumulate foreign reserves** or **sizable dollar depreciation**, official demand would be unlikely to rise substantially.

Trend increase in foreign private participation in the U.S. sovereign debt market

… even given evolving global financial and geopolitical conditions.

Several factors explain this rise in demand:

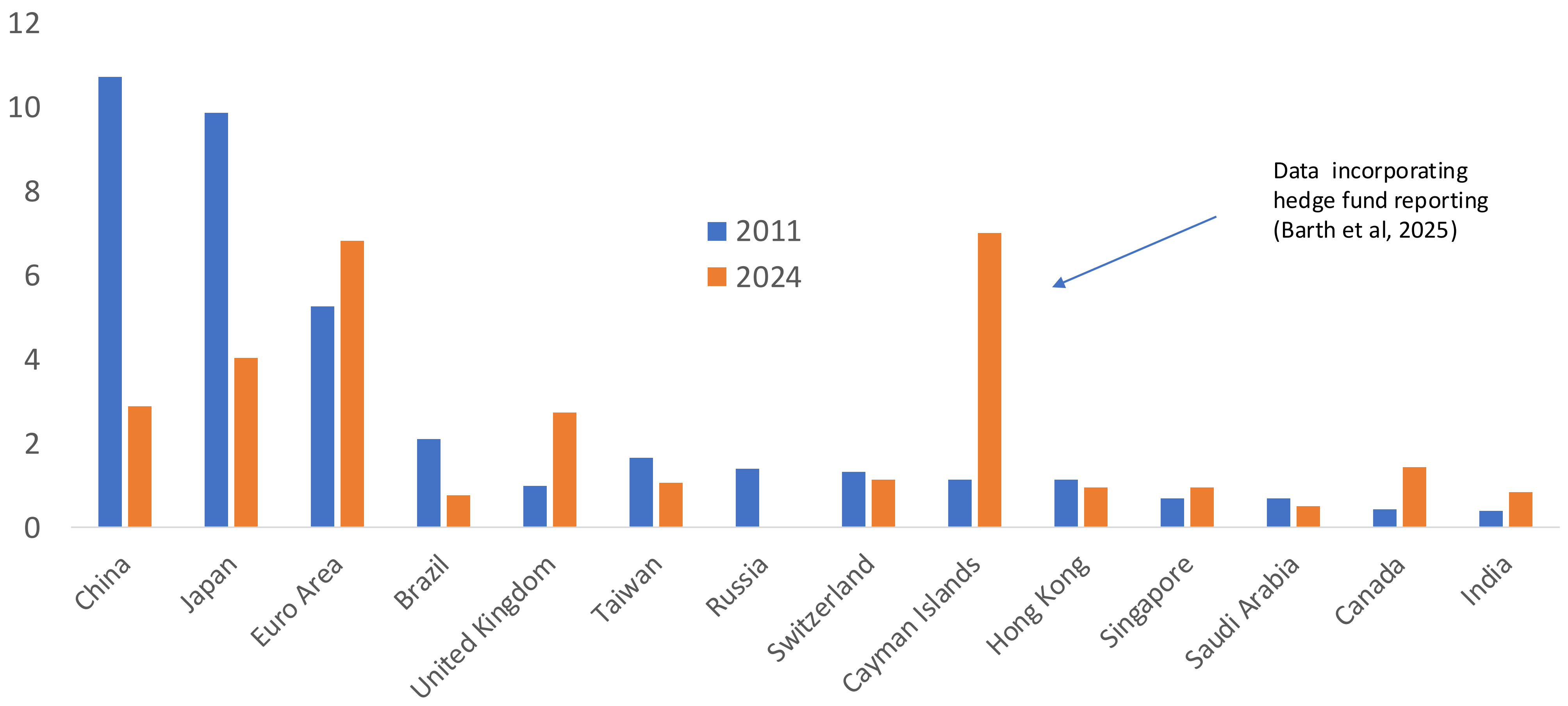
Increases in parallel with the size of the global bond market.

- U.S. dollar real appreciation.
- An expansion in marketable U.S. debt.
- global portfolio debt assets ratio.
- Increase during global “risk-off” episodes.
- Geopolitical fragmentation significantly dampens foreign private demand.

Risks?

Change in country shares of U.S. Treasury holdings, 2011-2024

(percentage points)



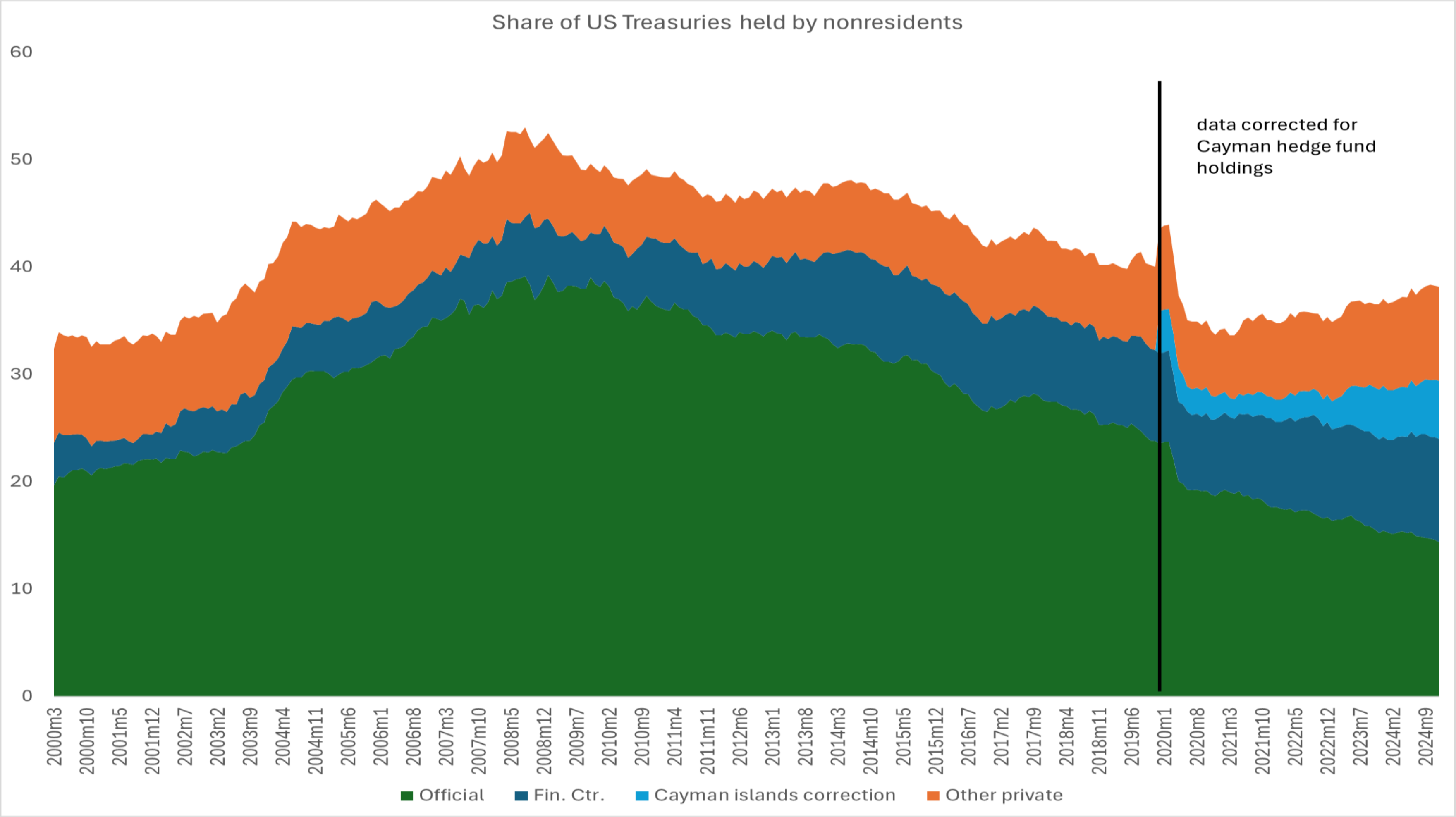
Between 2011 and 2024, the aggregate foreign UST share declined by about 8.5 percentage points (46.6% to 38.1%)

Looking across countries:

- China and Japan: **14** pp decline in joint share.
- China: \$1.15 trillion (2011) → \$759 billion (2024). UST outstanding ↑ \$15.5 trillion at MV
- Underestimate? Large increase in custodial holdings via Euroclear (Setser 2023a).
- Japan: holdings constant in nominal terms→ large drop in share.
- Russia sold most of its Treasuries in 2018, following the imposition of U.S. sanctions.
- Massive increase in holdings by Cayman Islands (\$1.7 trillion) – see Barth et al. 2025
- India's holdings of USTs increased five-fold to \$219 billion.

5. **Cross-sectional regressions** show that changes in **UST shares** are **positively correlated** with **FX Reserve shares** and countries with **mostly-private holdings**. Countries with **mostly official holdings** show **a very large decline**, on average.

Growth in foreign private share reflects holdings by financial centers



Summary

- Assessment of US position from a (partial) nationality perspective
  - US creditors are mostly advanced economies, reduced role for China
- Analysis of foreign holdings of US Treasuries: official holdings
  - Decline in foreign share after GFC reflects waning FX reserve accumulation and large USD appreciation vis-à-vis other reserve currencies
- Analysis of foreign holdings of US Treasuries: private holdings
  - Increase in private share reflects rising holdings by advanced economies, especially financial centers (Cayman Islands; UK, IRE-LUX). Difficult to identify ultimate investors.
- Sensitivity to market conditions likely much higher
  - Large holdings by hedge funds
  - Likely increase in holdings associated with collateral role of Treasuries in financial markets as opposed to ultimate holdings

What do these results suggest moving forward?

- Structural moderation in official-sector demand for U.S. government debt:
  - A strong recovery in official Treasury purchases is unlikely absent a renewed period of rapid reserve accumulation or a sizeable downward adjustment in the dollar.
  - Compositional trends in global reserves indicate a gradual decline in the U.S. dollar’s share and a shift away from U.S. Treasuries in official portfolios.

- The geographic composition of private investors displays greater concentration from countries more closely geopolitically aligned with the United States.
  - Rising geopolitical frictions even within the “Western” bloc highlight vulnerabilities with potentially material implications for private Treasury demand (Chari et al, 2025).

What do these results suggest moving forward?

- Our analysis highlights the opacity of foreign private holdings.
  - The growing role of financial center intermediaries increasingly obscures the identification of ultimate holders.
  - The rising importance of highly mobile investors whose positions may be sensitive to shifts in global risk sentiment and funding conditions (e.g., hedge funds).

- Broader macro-financial implications:
  - A sustained rise in U.S. external liabilities implies larger future income transfers abroad.
  - If foreign official demand for Treasuries remains subdued and private demand becomes more sensitive to risk or geopolitical factors, U.S. interest rates could become less countercyclical.

Thank you!!

Change in country holdings of U.S. Treasury securities, 2011-2024

(billions US$)