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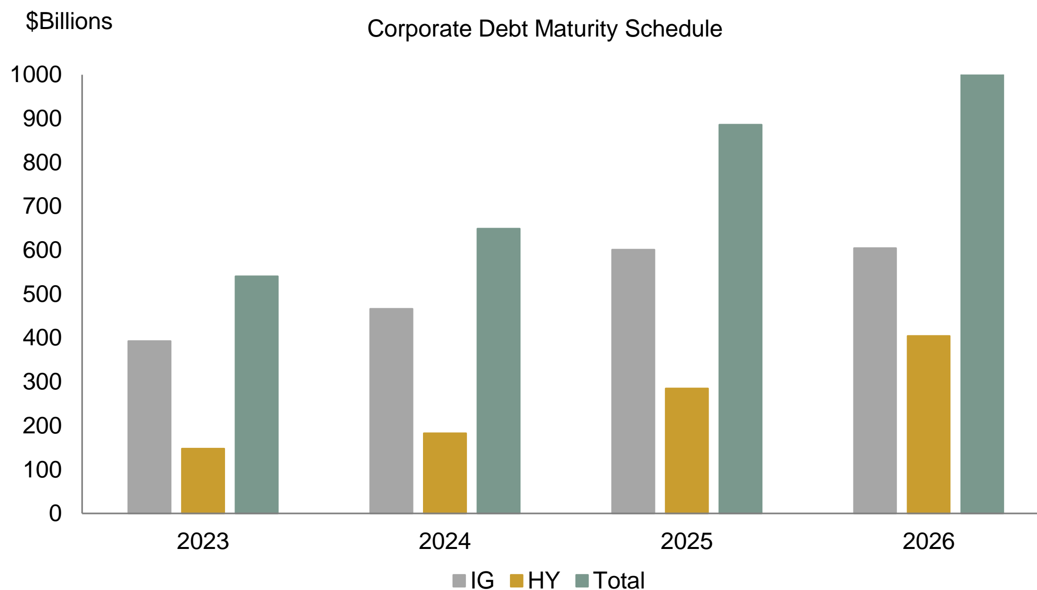
The Great Debt Repricing

Interest rates broadly decreased in the forty years prior to 2022. This allowed — we would argue *conditioned* — consumers, businesses, and governments into accepting more debt and leverage. Meanwhile, the current inflationary episode necessitates higher interest rates from the Fed and other central banks. This makes existing leverage untenable. **Ultimately the forces of fiscal and financial dominance will steer the Fed into cutting rates both *nominally* and in *real* terms.** We discuss below.

Consumers' non-mortgage interest payments are up over 60% from their pre-pandemic highs (+50% YoY in October). Mortgage payments will also rise further from their Q2 level of 4% of disposable personal income. As a result, delinquencies are rising quickly (see our November 13 note). This also applies to the US government which allocated 16% of FY-2023 receipts toward interest! This is likely to increase as the Treasury anticipates borrowing another $1.6T in Q4 2023 and Q1 2024. Assuming a 4.37% interest rate (average Treasury Note and Bond yield), leads to another $70B of interest expense (1.6% of FY-23 tax receipts). However, **nonfinancial corporate debt[1] is particularly noteworthy, which has looming maturity walls**, shown below. Between high yield and investment grade, there is **$649B in debt maturing in 2024, $886B in 2025, and $1.0T in 2026 which will have to be refinanced at much higher rates.** The natural result of this is that businesses will be faced with a Hobson's choice of paying debt or paying employees. The Fed will need to cut rates by more than many investors think. We say this starts in March.



Sources: Bloomberg, SMBC Nikko

1. a. Excludes banks, funds, insurance and financial institutions, also excludes leveraged loans.
   b. Excludes issuers that were not rated.
   c. No sovereigns, government agencies, regional, supranationals, development banks or the like.
   d. High yield = bonds rated below investment grade by either Moody's or S&P.

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