WHEN THE MARKET SPEAKS

In August, for the first time, the US public debt exceeded $40 trillion. For fiscal year 2026, the federal deficit is estimated at around 5.8% of gross domestic product (GDP): about 2.6% is attributable to the negative primary balance, while 3.3% is represented by net interest, now over one trillion dollars per year, and federal defense spending itself. The problem is not just about Washington. Japan and Europe also have to finance expansionary fiscal policies just as investors demand higher yields to hold long-term debt.

August's attention has thus returned to global debt sustainability, finding one of the most vulnerable points in Sanae Takaichi's Japan. The yen had reached 164 against the dollar at the end of July, before the joint intervention of the United States and Japan, while the yield on the 30-year Japanese government bond went above 4%. In the United States, the *30-year Treasury* exceeded 5.2%, returning to levels not seen in almost twenty years.

Complicating the picture has come private debt. The issuance of bonds related to artificial intelligence infrastructure is approaching $500 billion this year, with the main *Cloud Service Providers* responsible for about $220 billion. The weighted average maturity of these issues is close to fifteen years[1]. States and companies are therefore simultaneously looking for capital, creating increasing competition on the long end of the curve. In such an environment, it is not surprising that the dollar has weakened and gold has resumed its upward path.

More intriguing, however, was the behavior of the stocks. After the sharp decline in July, the S&P 500 appreciated by almost 3%, the Nasdaq by about 4%, the Euro Stoxx 50 by 1.5% and the Nikkei by 3%. August thus confirmed the surprising solidity of the stock markets,

[1] Dati in "Stock Rebound, Yields Hit New Hight, but the Dollar Weakens: Making Sense of the Divergence, 27 agosto 2026, *MacroMicro Blog*, *https://en.macromicro.me/blog/ceo-house-view-stocks-rebound-treasury-yields-hit-new-highs-but-the-dollar-weakens-making-sense-of-the-divergence-across-markets.*

supported above all by an exceptionally strong earnings season. Artificial intelligence remained one of the main drivers, but the rise gradually widened. Nvidia's excellent results and *guidance* on August 26 provided further confirmation of the strength of the AI investment cycle.

Debt versus growth

Debt sustainability can be traced back to a simple relationship between the cost of debt and the nominal growth of the economy. As long as the economy grows enough to absorb the cost of financing, high debt remains manageable. When this relationship reverses stably, interest rates begin to fuel the debt itself. This is where the delicate American balance lies today. On the one hand, fiscal deterioration can no longer be ignored, on the other, the economy continues to surprise with its solidity. Consumption and investment resist, and the gigantic cycle of artificial intelligence continues to fuel economic activity and profits.

This explains the apparent paradox of August: Treasuries under pressure, a weak dollar, strong gold and, at the same time, stocks close to their highs. The bond market signals concern about debt, inflation and new issuance; the equity market, on the other hand, continues to bet on earnings growth.

Bessent, Druckenmiller e Warsh

It is in this context that what has happened in recent weeks becomes interesting. Faced with the rise in long-term yields, Treasury Secretary Scott Bessent doubled his long-term Treasury buybacks. The response of Stanley Druckenmiller, his old mentor, was very harsh: the bond market was not dysfunctional, it was simply incorporating deficits, inflation and a huge supply of debt into prices. Intervening, according to him, meant moving from liquidity management to price management.

Then came Kevin Warsh in Jackson Hole. The new Fed chair was categorical: 2% inflation is a "firm and fixed" target, and price stability remains the responsibility of the central bank. But Warsh also said something perhaps more important: the Fed must stop constantly suggesting to markets how to interpret the economy. Forward *guidance* risks creating a "hall of mirrors," in which investors look to the Fed and the Fed looks to investors. In a world of AI, geopolitics, manufacturing transformations, and rising debt, Warsh wants to leave more of the task of processing information and turning it into prices to the market. Those prices then become a signal that the Fed can use in conjunction with economic data.

It's hard not to notice a curious convergence between three men who have been professionally linked for decades. Bessent, who is responsible for financing more than $40 trillion in debt, is forced to send a signal to the bond market. Druckenmiller reminds him that that very market needs to exercise discipline over fiscal policy. Warsh argues that the Fed should talk less and let the markets speak more. Is there any indirect direction between the three? Who knows. But the convergence is too intriguing to ignore.

And now?

Warsh's very firm speech raised expectations of a rate hike in September, but that doesn't mean this is inevitable. There is an important element: although current inflation remains above target, market-based ten-year inflation expectations remain around 2.3%. Anchoring long-term expectations is critical to the Fed's credibility and leaves Warsh a chance to wait for the next data before deciding.

In November, the United States will face the *midterm* elections, and Donald Trump has a clear interest in going to the polls with lower energy prices and a favorable economic backdrop. The war with Iran and tensions in the Strait of Hormuz have contributed to the rise in American gasoline, turning geopolitics into an electoral problem as well. It is therefore reasonable to expect the White House to try, where possible, to reduce the geopolitical tensions that fuel the price of energy. Not necessarily to help the Federal Reserve, but the effect could be just that: lower oil and gasoline would improve upcoming inflation data and give Warsh more freedom.

This opens a possible division of labor: policy seeks to mitigate external shocks, the Fed firmly defends the 2% target, while the market is left more free to determine prices and yields.

For investors, the message therefore remains relatively simple. Fundamentals suggest staying invested in equities, maintaining technology and artificial intelligence but increasing diversification.

On the fixed income side, it is more prudent to favour short and intermediate durations, avoiding taking on too much risk on the long end of the curves.

As uncertainty in the markets increases, gold and liquidity maintain an important protective role: the former as a structural defence against debt and fiscal uncertainty, the latter to take advantage of any corrections. August therefore leaves us with two seemingly contradictory messages: debt calls for prudence, while growth and earnings suggest staying invested.

For now, fundamentals continue to win. But in the coming months, as Bessent, Druckenmiller and Warsh seem to suggest in different ways, it will probably be even more important to let the market speak - and above all to know how to listen -.