

The Credit Market Lens: AI Capex and the Limits of Crowding Out

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Key takeaways:

- The AI bond boom has created a simple but potentially misleading market narrative that corporate issuance is crowding out Treasuries. With hyperscalers borrowing heavily and Treasury supply still elevated, it is tempting to blame higher yields on too much duration chasing too little debt-buying capacity.
- That story gets the mechanism wrong. AI capex can lift real rates, but through the saving-investment channel: A large investment boom absorbs labor, power, equipment, and construction capacity unless saving rises enough to offset it.
- The data do not support direct Treasury crowding out. Unanticipated AI debt deals leave little statistically significant footprint in 10-year yields, term premia, or swap spreads, pointing instead to policy expectations and broader macro forces as the cleaner explanation for the rate move.

A popular narrative for the rise in bond yields over the past few months is that the debt-funded AI capital expenditure cycle is crowding out the Treasury market. The crowding-out argument can appear compelling: AI companies are expected to continue to issue unprecedented amounts of debt at a time when Treasury supply remains elevated. Because both ultimately draw from the same pool of investor capital, yields must rise to clear the market.

The problem with this argument is that this is not how crowding out conventionally works. The textbook mechanism runs in the opposite direction: Government borrowing absorbs a finite pool of savings, pushes up interest rates, and crowds out interest-rate sensitive private investment.

So, is this time different? Can private-sector financing, however large, crowd out a \$32 trillion Treasury market? As we argue below, AI capex just like any other large capex cycle, can and likely will exert upward pressure on real (inflation-adjusted) yields. But that is not evidence of crowding out via portfolio rebalancing, which is a frequently encountered view among market participants.

One important nuance, and one that is often overlooked in the AI capex debate, is that this upward pressure on real rates is largely independent of how the AI capex cycle is financed. The roughly \$1 trillion in hyperscaler capex expected this year consumes the same real resources whether it is funded with debt, retained earnings, or equity issuance. What matters for equilibrium real rates is the underlying gap between desired investment and desired saving, not the liability used to finance it.

This nuance is particularly important in the case of retained earnings. The fact that a firm uses cash already on its balance sheet does not mean the investment is somehow "pre-funded" from a macroeconomic perspective. Deploying retained earnings into AI infrastructure simply converts saving into investment and consumes the same labor, power, and construction resources as any other form of financing. The financing source changes the ownership of claims and the allocation of risk, but not the economy's consumption of real resources.

To be clear, financing choices still matter for asset prices, risk allocation, and market technicals, which is the second channel we discuss next. But for the macroeconomic arithmetic linking desired saving, desired investment, and equilibrium real rates, a dollar of debt-financed capex is no different from a dollar financed through retained earnings or equity issuance.

Bottom line: Across nominal yields, term premia, and swap spreads, the evidence that surprise AI debt issuance is pushing Treasury yields higher is weak. The AI capex boom may well lift equilibrium real rates through the saving-investment channel, but the narrower claim that AI bond supply is directly crowding out Treasuries is hard to find in the data.

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