Would You Rather Lend to the U.S. Government or Microsoft?

Mariya Entina, CFA, CPA | February 2025

As a lender, would you prefer the U.S. government as your debtor or Microsoft? At first glance, the government might seem the safer bet. After all, Washington can print money and collect taxes. But how do their fundamentals compare? Treasury Secretary Scott Bessent recently noted, "We're in the middle of a Bretton Woods realignment, and I'd like to be a part of it."[1] Meanwhile, the Congressional Budget Office projects that the gap between Social Security revenues and outlays will triple in the next six years, reaching an annual run rate of more than a third of a trillion dollars. These growing fiscal challenges raise serious concerns about the creditworthiness of Uncle Sam. In contrast, top-rated corporate credits – like Microsoft – are backed by ample cash-generating assets and significant corporate treasury reserves.

My point here is not to recommend Microsoft debt. As of the date of this publication, DoubleLine holds no Microsoft bonds, as we find more attractive relative value in investment grade corporate credit in other issues. This is a humble thought experiment[2] comparing the fundamentals of a leading company relative to the balance sheet of the U.S. government.

Cash-Flow Generation

Microsoft's cash-flow generation is noteworthy. According to Moody's, Microsoft is expected to generate around $48 billion in free cash flow (FCF) in fiscal year 2025. In contrast, the federal government has negative FCF, as it has been running a budget deficit since 2002, which means federal expenditures exceeded revenues each year. With a reset higher in interest rates across the U.S. Treasury yield curve since 2021, an increasing share of government funds will be used toward interest payments. This deficit spending makes the government dependent on issuing additional debt each year to fund its expenditures, whereas Microsoft earns more money than it spends. Microsoft can reinvest these excess earnings to grow the company – in a sort of virtuous cycle of prosperity – or distribute them for the benefit of shareholders.

Debt and Interest Coverage

Microsoft's debt metrics speak for themselves. As of Dec. 31, 2024, Microsoft had $9 billion of cash in excess of debt outstanding, and its interest coverage ratio was 53.5x – meaning core annual earnings are enough to pay its yearly interest expense 53.5 times over.[3] Microsoft has ample capacity to service its debt, even in challenging economic conditions.

In contrast, the government's debt burden is significantly higher, with over $35 trillion in borrowings. The government's debt affordability is also deteriorating, with receipts-to-interest expense declining from 6.7x in 2018 to just 5.2x in 2023, meaning that 20% of all gross receipts go to pay interest on debt. *(Figure 1)* This high debt burden and rising interest costs pose significant risks to Washington's ability to service its debt without resorting to measures such as debt monetization or restructuring.[4]

Credit Ratings

Microsoft has held the top Aaa and AAA ratings from Moody's and Standard & Poor's, respectively, since 2008. In comparison, the government's credit ratings have been in decline. Although Moody's still assigns the U.S. an Aaa rating, the outlook turned negative in 2023; Fitch cut the government's rating to AA+ in 2023; and S&P cut it to AA+ in 2011.[5] High debt levels, political polarization and a not-so-pretty fiscal outlook weigh on the government's once-golden reputation.

U.S. Government's Ability to Service Its Debt Is Declining While Microsoft's Continues to Grow

June 30, 2018 through June 30, 2023

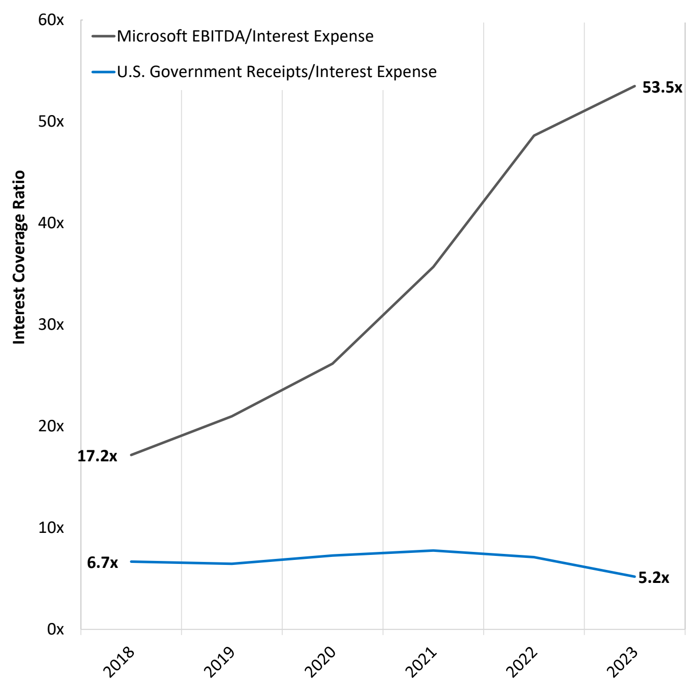

Figure 1
Source: Federal Reserve, Bloomberg

AAA Spread

As of Jan. 31, 2025, 30-year Microsoft bonds yielded 49 basis points above comparable-tenor Treasuries.[6] That's not just a testament to Microsoft's solid credit health but also a potential win-win scenario for those who appreciate an opportunity to both enhance safety and earn a bit of extra juice in income. As the government keeps issuing more bonds to fund its deficits, Microsoft's lack of meaningful debt growth means fewer of its bonds are available, making them scarcer and, in turn, more valuable.

Conclusion

While the U.S. government might seem like a safe bet due to its ability to print money and collect taxes, the financial metrics and credit ratings tell a different story. In a world where many people's "ultimately safe bet," Treasuries, aren't as rock solid as they once seemed, it might well be time to give high-grade corporate issuers a second look. So, whom will you lend to? ■

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About the Author

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Ms. Entina joined DoubleLine in 2019. She is a Portfolio Manager on the Global Developed Credit team, focusing on investment grade corporate bonds. In addition, she is a contributing member of the Fixed Income Asset Allocation Committee and a corporate sector specialist on DoubleLine's Responsible Investment team, overseeing and monitoring the Responsible Investment integration for the Global Developed Credit team. Prior to DoubleLine, Ms. Entina was an Investment Research Analyst at Pacific Life, where she covered transportation, aerospace & defense, automotive OEMs, captive finance, auto parts suppliers, diversified manufacturing and infrastructure credit. Prior to Pacific Life, she held roles at Capital Group and KPMG LLP. She holds a B.A. in Economics and Accounting from the University of California, Los Angeles. Ms. Entina is a licensed CPA, CFA® charterholder, SASB FSA Credential Holder and has earned the CFA Institute Certificate in ESG Investing.

About the DoubleLine Global Developed Credit Team

The Global Developed Credit (GDC) team manages $9 billion in assets in investment grade (IG) and below-IG corporate credit from issuers domiciled in the U.S. and other developed economies, including fixed income securities and bank debt. The GDC team underwrites the individual credits and actively risk-manages the economic-sector concentration, duration and other aggregate characteristics of DoubleLine's corporate credit portfolios and sleeves of multi-sector portfolios. The team comprises 22 investment professionals, including portfolio managers, analysts and traders.

Endnotes

[1] Mr. Bessent's evocation of a "Bretton Woods realignment" refers to a potential shift in global financial systems. The statement refers to the United Nations Monetary and Financial Conference held in Bretton Woods, N.H., in July 1944 near the end of World War II. The Bretton Woods agreement tied currencies of nations outside the communist powers of the Soviet Union, China and their satellites to the U.S. dollar, which was backed by gold until 1971.

[2] As all experiments should be undertaken with humility.

[3] Microsoft had $75.5 billion in cash and $66.5 billion in debt outstanding as of Dec. 31, 2024.

[4] For an analysis of the possible trajectories of the U.S. budget deficit and debt spirals toward theoretical crisis levels under different interest-rate scenarios, please read July 2024 research paper "U.S. Debt Spiral Briefing: A Scenario Survey as Washington Drifts Toward a Reckoning" by DoubleLine fixed income asset allocation strategist Ryan Kimmel. https://doubleline.com/wp-content/uploads/Debt-Spiral-Briefing_Kimmel_July-2024.pdf For an update of Mr. Kimmel's work, see "US fiscal path unsustainable despite improved budget forecasts, says DoubleLine," Reuters, Jan. 21, 2025. https://www.reuters.com/markets/us/us-fiscal-path-unsustainable-despite-improved-budget-forecasts-says-doubleline-2025-01-21/

[5] Fitch downgraded the U.S. Treasury on Aug. 1, 2023. Moody's placed its negative outlook on Nov. 10, 2023. S&P downgraded on Aug. 5, 2011.

[6] The reference security for Microsoft Corp. is MSFT 4 ¾% maturing Nov. 3, 2055.

Basis Points (bps) – Basis points (or basis point (bp)) refer to a common unit of measure for interest rates and other percentages in finance. One basis point is equal to 1/100th of 1%, or 0.01% or 0.0001, and is used to denote the percentage change in a financial instrument. The relationship between percentage changes and basis points can be summarized as: 1% change = 100 basis points; 0.01% = 1 basis point.

Free Cash Flow (FCF) – Cash a company produces through its operations after subtracting any outlays of cash for investment in fixed assets like property, plant and equipment. In other words, FCF is the cash left over after a company has paid its operating expenses and capital expenditures.

Interest Coverage Ratio (ICR) – Debt and profitability ratio that shows how easily a company can pay interest on its outstanding debt. It is calculated by dividing a company's earnings before interest, taxes, depreciation and amortization (EBITDA) by its interest expense during a given period.

Investment Grade (IG) – Rating that signifies a municipal or corporate bond presents a relatively low risk of default. Bonds below this designation are considered to have a high risk of default and are commonly referred to as high yield (HY) or "junk bonds." The higher the bond rating the more likely the bond will return 100 cents on the U.S. dollar.

Tenor – Length of time remaining before a financial contract expires. It is sometimes used interchangeably with the term maturity, although the terms have distinct meanings. Tenor is used in relation to bank loans, insurance contracts and derivative products.

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