Economic Brief

The BakerGroup

Market Comment: Points to Ponder

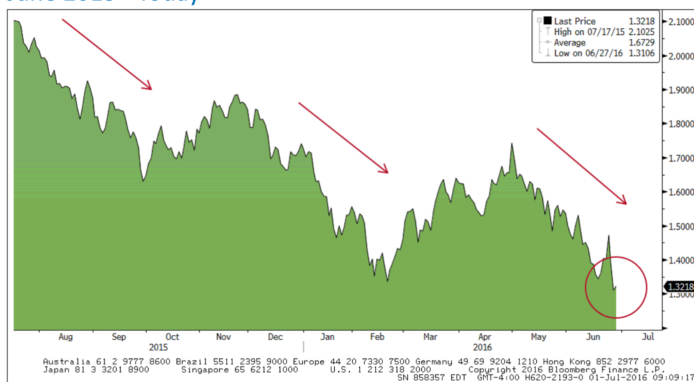
Treasury yields are hitting historic lows as pre-holiday position squaring is all about risk aversion. After a couple of days of respite, currencies are gravitating back to the immediate post-“Brexit” levels, and bonds are rallying again. The 2yr T-note yield fell to .56%, as low as has been seen since last October. But the real action is in longer maturities. The 10yr yield punctured it’s cycle low from 2012 (barely) by hitting 1.38% overnight. Meanwhile, the long-bond traded at 2.19%. Never thought we’d see that. But stay tuned. Inflation expectations are also hitting all-time lows. The Fed’s preferred measure of forward inflation, their Five Year Forward Breakeven rate is now at 1.32%... the lowest since the Fed began tracking this measure in 1999.

As expectations of lower global growth in the wake of “Brexit” feed into expectations of lower inflation, it puts more downward pressure on bond yields. Central banks’ efforts to “reflate” economies have been hampered by all of the usual suspects: debt overhang, ageing populations, etc. And now with the shock of Brexit, the global economy will likely be stuck in low gear for yet an even longer time. For the US, safe-haven flows will also keep a bid in the bonds.

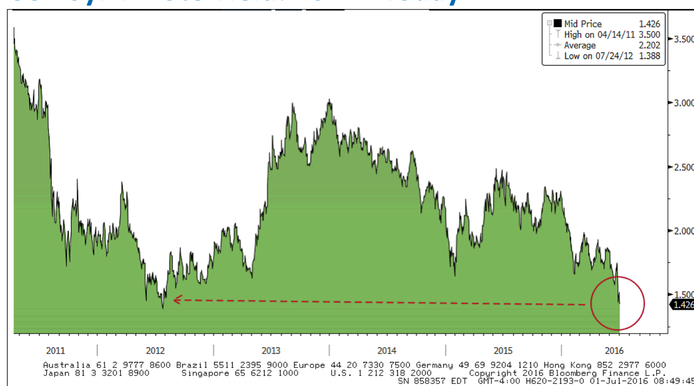
Not to beat a dead horse, sound like a broken record, or any other pertinent metaphor, but sitting on excess cash in anticipation of higher rates is sub-optimal in this environment. Rein in duration if needed, but stay in the game. Prudent deployment, not market timing, is in order. The (not so) new normal lives on.

Fed’s 5yr Forward Breakeven Inflation Rate:

June 2015 - Today



US 10yr T-Note Yield: 2011 - Today



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