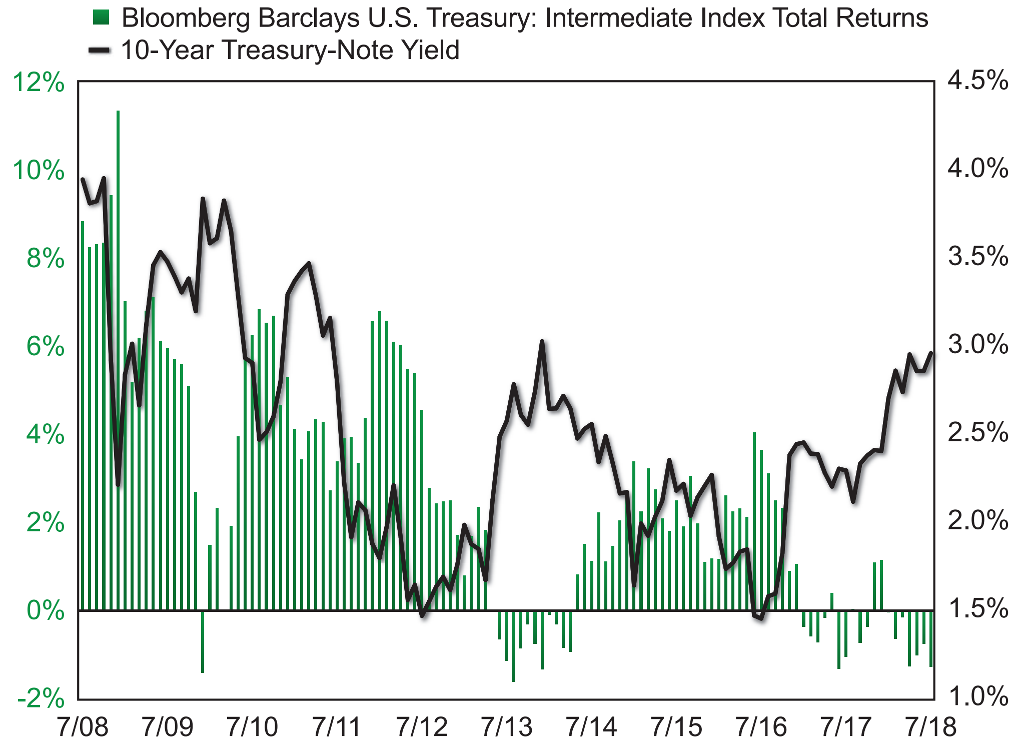
Treasury Yields Are Up Since July 2016 And Returns Have Suffered

Rolling 12-Month Total Returns *(7/31/08-7/31/18)*



Source: Bloomberg Barclays and Federal Reserve. Past performance is not guarantee of future results.

View from the Observation Deck

1. The yield on the benchmark 10-year Treasury-note (T-note) rose from its all-time closing low of 1.36% on 7/8/16 to 2.96% on 7/31/18, or an increase of 160 basis points (bps), according to Bloomberg.
2. Over the same period, the Federal Reserve (the "Fed") raised the federal funds target rate (upper bound) from 0.50% to 2.00%, or an increase of 150 bps, roughly in line with the rise in the 10-year T-note, according to Bloomberg.
3. The rise in interest rates and Treasury yields was accompanied by a notable decline in the rolling 12-month total returns posted by the Bloomberg Barclays U.S. Treasury: Intermediate Index (see chart).
4. From January 2017 through July 2018, 15 of the 19 rolling 12-month total returns were negative. The returns ranged from -1.33% to 1.14%.
5. Over the same period, the trailing 12-month Consumer Price Index (CPI) averaged 2.3%, according to Bloomberg. The lowest level reached by the CPI was 1.6%. That means that none of the rolling 12-month total returns kept pace with inflation.
6. Bond yields have been low on a historical basis for several years. The last time the yield on the 10-year T-note approached the 4.00% mark was on 4/5/10, when it closed at 3.99%, according to Bloomberg.
7. Brian Wesbury, Chief Economist at First Trust Advisors, is forecasting two more Fed rate hikes by the end of 2018 and as many as four more by the end of 2019, which could take the federal funds target rate to 3.5% using the current quarter-point per hike pace.
8. If economic growth continues to strengthen and/or inflation heats up, bond investors need to be cognizant of the potential for higher interest rates and bond yields moving forward, in our opinion.

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