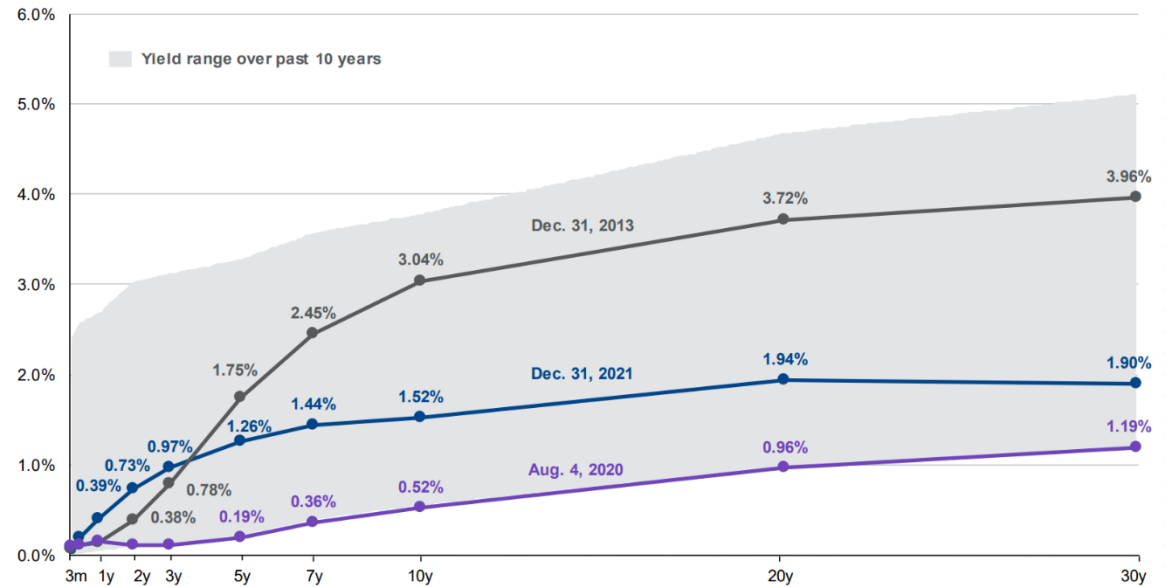


## BCA Market Perspective © Shape of the Yield Curve January 2022

During the fourth quarter of 2021 the two-year treasury yield rose from 0.28% to 0.73%, while the 10-year treasury yield remained the same at 1.52%. This phenomenon where short-term rates rise while longer term rates stay the same is known as a flattening of the yield curve and tends to signal a future of slowing economic growth.

The chart to the right shows three distinct yield curves: the current yield curve on December 31, 2021 (blue), the yield curve on December 31, 2013 (gray) which represents the curve's steepest levels in reaction to the Fed announcing it would begin pairing back its bond-buying program, and the yield curve on August 4, 2020 (purple) which reflects the record low on the 10-year treasury, driven by safe haven demand and pessimism around U.S. pandemic recovery.<sup>1</sup>

U.S. Treasury yield curve



The \$14.8 trillion Treasury market includes Treasury bills, notes and bonds with maturities ranging from one-month to 30-years. “The yield curve plots the yields of all Treasury securities, and investors watch its shape to extrapolate market expectations.”<sup>2</sup> The yield curve is typically upward sloped, which signals economic growth and justifies investor expectations for a higher return given the incremental maturity risk. But from time to time, the yield curve may invert, a sign that has predicted past recessions. The recent rise of short-term rates suggests the Fed is expected to push for higher rates in the near future in order to curb inflationary concerns. Rising rates could slow the economy, by increasing borrowing costs.

In December, Fed Chairman Jerome Powell mentioned that “we’re (the Fed) in a position where we’re ending our taper by March, in two meetings, and we’ll be in a position to raise interest rates as and when we think it’s appropriate”. Based on Fed’s Summary of Economic Projections, investors should expect three hikes in 2022, beginning in March, and three additional hikes in 2023. Bond markets, however, are worried about hiking into a flat yield curve, and may question the Fed’s ability to raise rates without triggering an abrupt end to the recovery. It can not be understated how important 2022 will be, as investors keep a close eye on broad financial conditions, maximum employment, price stability, and of course the shape of the yield curve.

<sup>1</sup> Source: FactSet, Federal Reserve, J.P. Morgan Asset Management

<sup>2</sup> Source: Reuters