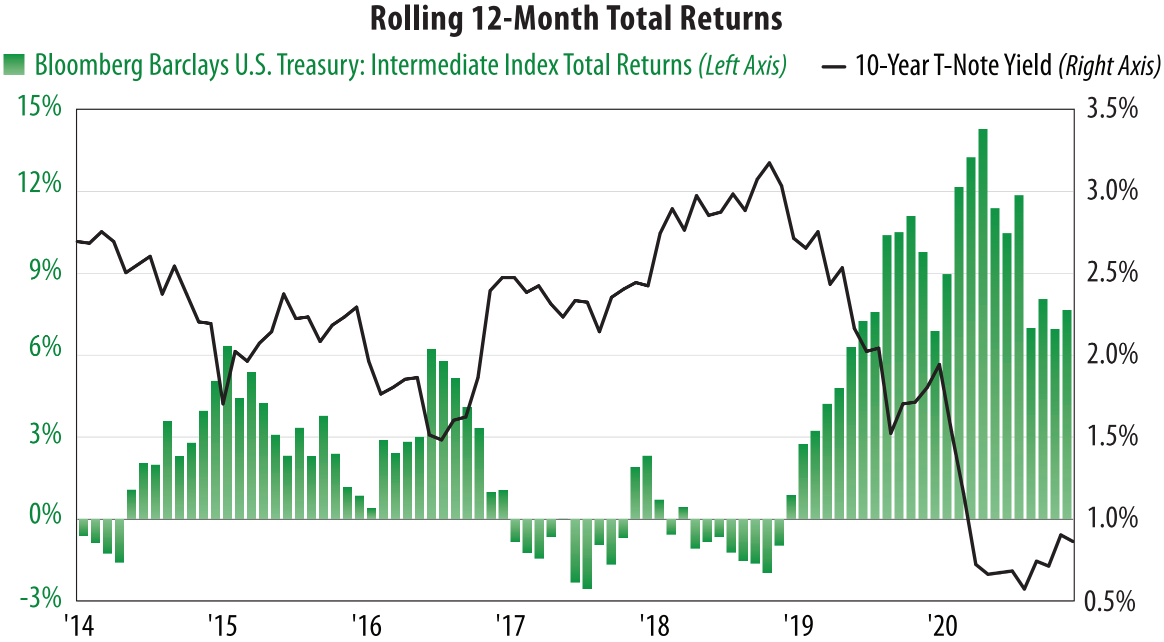
The Pop In Treasury Returns Likely Not Sustainable



Source: Bloomberg Barclays & Federal Reserve. Month end data from 2014 - 11/30/20. **Past performance is no guarantee of future results.**

View from the Observation Deck

1. There is a lot going on in the chart above. Believe it or not, the predominantly negative rolling 12-month total returns posted from the start of 2017 through the end of 2019 were not only anticipated but encouraging, in our opinion.
2. Why would negative returns be encouraging? They were a sign that the process of normalizing interest rates and bond yields was working. Rising interest rates and bond yields reflected a strengthening U.S. economy.
3. Rising rates and yields, however, also tend to push bond prices lower, especially Treasury notes and bonds since they have essentially no credit risk to factor in.
4. If you recall, after having kept its benchmark federal funds target rate (upper bound) artificially low at 0.25% for seven years (12/16/08-12/15/15), the Federal Reserve ("Fed") slowly began raising its target rate starting in December 2015.
5. After only bumping it higher by 50 basis points through the end of 2016, the Fed accelerated its tightening phase in 2017 and 2018, raising it a total of 175 basis points to 2.50%. This was the driver of the normalization process.
6. What happened to the normalization process? In the spirit of brevity, it essentially collapsed due to slower economic growth caused by the Trump administration's trade tariff program (March 2018 to present) and the COVID-19 pandemic (February 2020 to present). And as a result, the federal funds target rate (upper bound) is back at 0.25% and the yield on the 10-year Treasury note (T-note) closed 11/30/20 at 0.84%, well below its three-year high of 3.24% (11/8/20), according to Bloomberg.
7. For those who might have missed it, in February of this year, the White House did acknowledge that President Donald Trump's trade stance "depressed economic growth and business investment," according to Bloomberg.
8. In order to pump up economic activity we need to reopen the economy. In order to that, we need to see one or more of these promising COVID-19 vaccines currently in the developmental pipeline to gain approval from the Food and Drug Administration ASAP. What was the yield on the 10-year T-Note prior to the onset of COVID-19? It closed 1/31/20 at 1.51%, 67 basis points above its close on 11/30 (0.84%), according to Bloomberg.
9. In addition to the near-term potential for one or more vaccines, the Fed has pledged to keep interest rates low for a number of years if need be to stimulate the economy and generate more inflation. Investors who either own or are thinking of purchasing Treasuries should keep a close eye on how the bond market reacts to breaking news on the virus front.

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