

Fixed Income: All Things Must Pass

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Certainly, the lion's share of the post-election focus within the fixed income arena has been on the U.S. Treasury (UST) market, and rightfully so, considering the recent rate developments across the maturity spectrum. Somewhat lost in the headlines have been some of the changes that have occurred within the rest of the G7 sovereign debt universe.

Post-Brexit, G7 sovereign debt yields were the "horse leading the cart" in terms of the direction for the Treasury market, but post-U.S. election, it's been the opposite. In other words, the rise in the UST 10-Year yield has helped push its G7 counterparts to higher readings as well. However, it should be noted that the overarching rising trend has not been a one-for-one relationship. To be sure, the 10-year rate increases abroad have not kept pace with what has been witnessed thus far in the U.S. To provide some perspective, as of this writing, the UST 10-Year yield has risen 45 basis points (bps) since election day; the remaining G7 increases have been as follows: Japan +7 bps, Germany +9 bps, UK +17 bps, France +24 bps, Canada +29 bps, Italy +37 bps.

U.S. 10-Year vs. 10-Year German Bund

[\[Image unavailable\]](#)

As a result, spread relationships, or relative value, have definitely shifted. With the German bund market essentially being viewed as "the Treasuries of the eurozone," this is where we will turn our attention. Since the "taper tantrum" in 2013, the 10-Year UST/bund spread has been on a rather visible upward trend. From the beginning of 2013 through the recent U.S. election, the spread moved from a low of +25 bps to as high as +190 bps. Post-election, this differential has risen by roughly 40 bps to break through the +200 bps threshold and now resides at its widest reading since 1989!

It is interesting to note that going into the final month or so of the campaign season, foreign purchases of Treasuries had revealed a discernible downward pattern. According to the most recent Treasury International Capital (TIC) data, foreign holdings of Treasuries through September had fallen by \$125.3 billion. Mainland China represented two-thirds of this total, or \$83.8 billion, dropping its UST holdings to their lowest level since 2012. Unfortunately, the TIC data operate with a one-month lag, so we won't be able to see the official foreign figures during this post-election surge in UST rates until the January 2017 report.

Conclusion

Will this historically wide spread serve as an incentive for foreign buying of Treasuries? One could make the case that G7 sovereign rate differentials have moved in the UST market's favor. Another supporting factor comes from the technical side of the equation, as the Relative Strength Index (RSI), which measures

whether the UST 10-Year is overbought or oversold, last week hit its highest oversold reading since 1990. That being said, the Treasury arena still seems to be in a phase of determining where the bottom lies, a process that seems to be causing global investors trepidation about jumping in too soon.

Unless otherwise noted, data source is Bloomberg, as of 11/18/2016.

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