

U.S. Treasuries: Home on the Range

Published August 10, 2016

Kevin Flanagan

Head of Investment and Fixed Income Strategy

Over the last month, the U.S. Treasury (UST) market have reached new all-time lows, placing yield levels into what our July 13, 2016, blog post referred to as “[Into Uncharted Waters](#)”. Since then, the UST 10-Year note has been navigating this newfound territory, trying to establish a new trading range in the process. With two monthly jobs reports now under its belt, the 10-Year yield has recently been exhibiting some signs that perhaps a near-term band has been established. In the post-Brexit investment world, fixed income investors have been wrestling with global growth concerns, both in the present and in terms of what the future may entail. As for the U.S., the sparring match has been between soft real sector data, such as GDP, and what is arguably the most important set of statistics to bond investors, the monthly employment report. Let’s take a quick look at this dichotomy. Thus far in 2016, according to the latest real GDP data, the economy is growing at a paltry rate of only 1.0%, a visible slowing from 2014/2015, when growth was averaging a 2.5% clip. Meanwhile, the last two jobs reports have apparently laid to rest any concerns that may have arisen following the surprisingly soft May figures. To provide some perspective, in May, nonfarm payrolls rose by only 24,000; but at 274,000, the average gain for the June/July period has far exceeded expectations. The unemployment rate has remained at 4.9% despite a surge of 821,000 in the civilian labor force, while average hourly earnings have stayed at the upper end of the recent range, at 2.6%. **U.S. Treasury 10-Year Yield Technical Levels**



Source: Bloomberg, as of 8/5/2016.

In a surprising twist, the UST 10-Year yield hit its all-time closing low of 1.36% following the release of the June employment data in early July. Typically, jobs data that beat consensus forecasts (as was the case last month too) do not elicit a bond market rally. Interestingly, since then, the 10-Year yield has been consistently moving higher. In fact, the most recent UST 10-Year note auction may have offered a glimpse of investors' lack of appetite, at least for now, as demand was measured at its lowest level since March 2009. From a technical perspective, the 10-Year yield has breached the Fibonacci line of 1.5674% a few times (a 23.6% retracement from the all-time low of 1.3180% that was reached on July 6, 2016) but remains measurably below the next level of 1.7217%, which would represent a 38.2% retracement from the aforementioned low. For the record, a 50% retracement would occur at the 1.8464% level. **Conclusion** So, where does that leave the UST 10-Year? Certainly, the 1.65% 2.45% trading range that had been in effect from roughly fall 2014 through early June of this year has now been replaced and pushed to the downside. From a near-term perspective, technical analysis would seem to point toward a new operating band of 1.30% to 1.75%/1.85%. Given the uncharted waters thesis, a negative geopolitical event or economic surprise (such as a U.S. recession) could create a new all-time low in yield, while on the other side of the ledger, a breach of the 50% retracement level would put 1.9711% in play.

Important Risks Related to this Article

Fixed income investments are subject to interest rate risk; their value will normally decline as interest rates rise. In addition, when interest rates fall, income may decline. Fixed income investments are also subject to credit risk, the risk that the issuer of a bond will fail to pay interest and principal in a timely manner or that negative perceptions of the issuer's ability to make such payments will cause the price of that bond to decline.