Supplement

What would yield curve shape be if the COVID-19 pandemic hits the economy?

Yield Curve Movements

The Inverting Yield Curve Is About More Than Recession This Time

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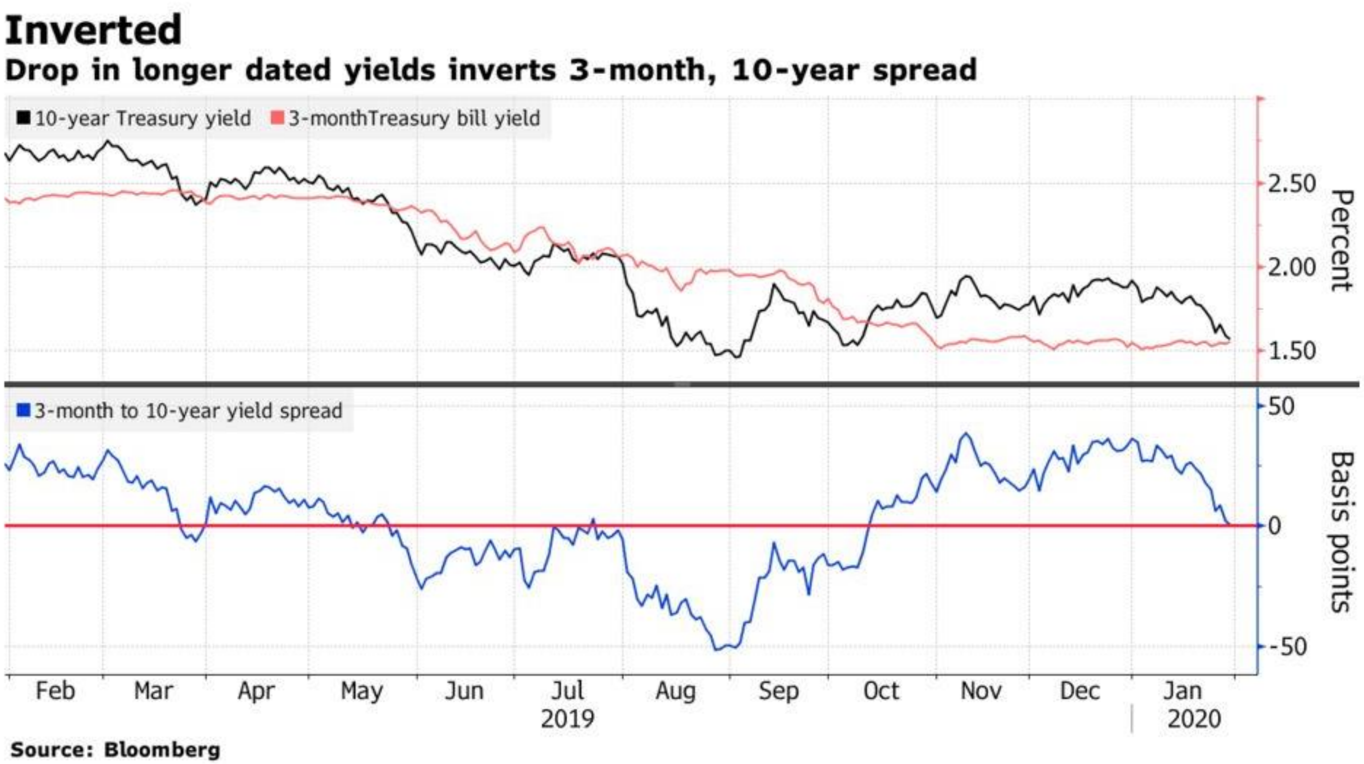

Yield Curve Movements

A key slice of the **U.S. yield curve inverted** for the first time since October 2020, reviving memories of growth fears that plagued investors last year and **signaling doubts that the Federal Reserve will succeed in reviving inflation**.

The ***gap between the yield on three-month and 10-year Treasuries at one point slipped to as low as minus 2 basis points*** on Thursday. The ***spread -- seen by some as a <u>warning signal</u> because it has inverted before each of the past <u>seven U.S. recessions</u>*** *-- last reached those levels as economic conditions deteriorated at the height of the **trade war**.*

With the **coronavirus outbreak (in January 30,2020)** ***threatening to disrupt the Chinese economy***, concerns about the business cycle are undoubtedly a factor. But more important still are **emerging doubts over the <u>ability and commitment of policy makers</u> to <u>shore up growth and spur inflation</u>**.

Yield Curve Movements

Following his press conference Wednesday, fed funds futures showed **increased conviction by traders that a cut is coming this year**, although they continue to price in just one quarter-point reduction.

The **inversion** *"highlights broader market fears that the* ***virus and its human and economic threat could spread***. The more that it does, the *more likely it starts to alter consumer and corporate behavior*, thereby ***promoting policy action to mitigate the dangers***.*"*

"We are closely monitoring the emergence of the coronavirus, which could lead to disruptions in China that spill over to the rest of the global economy"

Jerome Powell, Federal Reserve Chair


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ECONOMY | ECONOMIC DATA

Fed Report: Possible Spillovers From Coronavirus Pose New Risk to Economic Outlook

Semiannual report to Congress says global slowdown in manufacturing and trade appears to be nearing an end

Federal Reserve Chairman Jerome Powell will present the central bank's semiannual report to Congress next week.

PHOTO: MANUEL BALCE CENETA/ASSOCIATED PRESS

What would

steepen yield curves imply?

Yield Curve Movements

Treasury yield curve steepens as bond market signals economic rebound underway

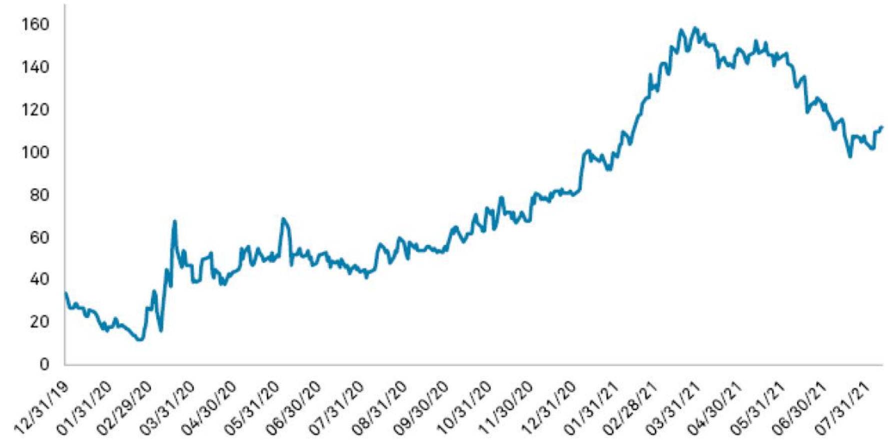
Analysts say the **steepening curve** — *a linear comparison of interest rates for bonds with different maturities* — is the ***government bond market <u>reflecting growing expectations for a robust rebound and a healthy, post-pandemic economy</u>*** as *longer-maturity yields rise faster than shorter-term yields*.

Yield Curve Movements

By **early April**, the ***yield curve began to flatten*** on ***slowing vaccination rates, stagnant unemployment, a global supply bottleneck***, *and* ***fears of the impact of COVID-19 variants.***

The mid-July low *may have been a bottom* and the yield curve may be **facing months of steepening**. The curve will ***likely continue to steepen*** as the market ***prices in ongoing, rising inflation*** and a ***Fed gradually moving towards a rate hike***.

Difference between the US Treasury 10-year bond yield and the 2-year bond yield (bps)



Data compiled Aug. 12, 2021.
Source: S&P Global Market Intelligence

The **risk of inflation rising** also tends to ***push yields up*** as investors seek ***compensation for the potential loss of purchasing power***.