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Investment Institute

Market Commentary

Weekly perspective on current market sentiment | **September 9, 2021**

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Last week's S&P 500 Index: +0.6%

Fixed-income tweaks

Key takeaways

- We have lowered our year-end target ranges for both the Treasury's 10-year note and 30-year bond for this year and next.
- We continue to believe rates will drift higher over the coming 15 months but to a lesser magnitude than earlier anticipated.

Even though we are looking at domestic economic growth north of 6% this year and better than 5% in 2022, interest rates have remained low. And longer-term Treasury securities historically respond to inflationary pressures as well, but expectations for the highest year-over-year Consumer Price Index (CPI) readings since mid-2008 have not deterred bond buyers from bidding prices higher and keeping yields lower than what we thought would be the case as we looked ahead and tried to project where rates might settle at the end of this year and next.

Of course, the current rise in the delta variant and the ongoing supply-chain disruptions have caused headwinds for the economy and sparked a number of economic-growth downgrades in recent weeks, including from our economists. Interest rates typically have a tough time rising when growth prospects start to diminish relative to previous expectations. In addition, the Federal Reserve (Fed) continues to buy $120 billion of bonds in the open market each and every month, at least for the time being. Foreign buying continues to be a meaningful factor. Note that as of the time of this writing the yield on the 10-year German Bund (government bond) is -33 basis points (100 basis points=1%). That's right, investors are paying the German government to hold their money. As a result, on a relative basis, the current 1.35% yield on the U.S. 10-year Treasury note looks pretty good.

While we expect economic growth to remain well above average this year and next, our expectations for the yield on the Treasury's 10-year note and 30-year bond were too high. As a result, we have lowered our target ranges for both securities for year-end (YE) 2021 and YE 2022 to levels we feel are more realistic given the above-mentioned issues.

For this year, we have lowered the YE target ranges for the 10-year Treasury note to 1.5%-2.0% from the previous 2.0%-2.5% and the 30-year Treasury bond to 2.25%-2.75% from the previous 2.75%-3.25%. While the magnitude of our anticipated rise in yields has decreased, our thesis that rates will slowly increase over the coming 15 months remains intact.

Overall, we continue to believe that the Fed will begin the process of buying fewer bonds each month late this year or early next. The announcement that tapering purchases will start could very well come at this month's Federal Open Market Committee (FOMC) two-day meeting that begins on September 21. We also continue to believe the Fed will not lift the fed funds interest rate target this year or next.

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