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Rising Bond Yields Are A Good Thing

***e*Research Corporation** is pleased to provide an article by Scott Grannis for his Blog, "Calafia Beach Pundit".

In this article, Mr. Grannis provides a couple of charts to support his belief that "the epic bond bond bull market is a thing of the past."

The article is reproduced below, beginning on the next page, or you can go to this specific Blog at the following link: **Rising bond yields are a good thing**

You can also visit Scott Grannis' Home Page for his Blog at the link below:
http://scottgrannis.blogspot.ca/

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Tuesday, January 30, 2018

Rising Bond Yields Are A Good Thing

Stocks are nervous because bond yields are rising. As I noted six weeks ago, the bond market is beginning to figure things out: corporate tax cuts are going to lead to a stronger-than-expected economy, and that in turn means the Fed is going to have to raise rates by more than expected.

The key 5-year real yield on TIPS is now 0.45%, and that is 65 bps higher than it was a year ago. 10-year Treasury yields are 2.73% today, and it looks more and more like the epic bond bull market is a thing of the past. We are still in the early innings, however.

Chart #1

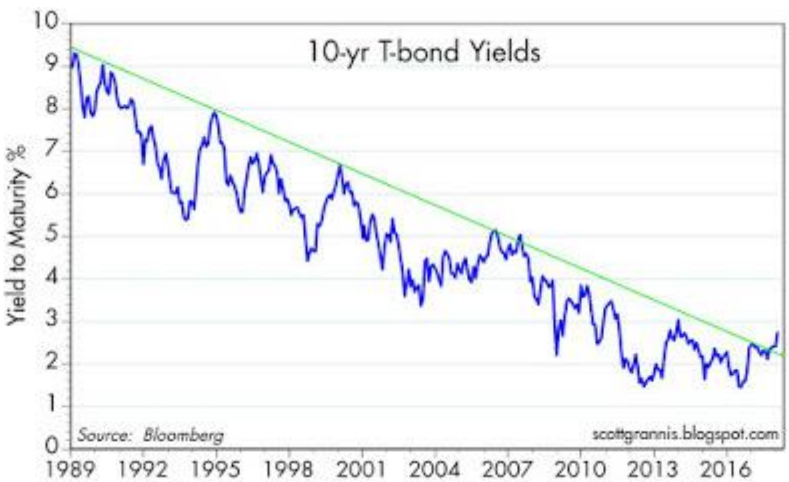


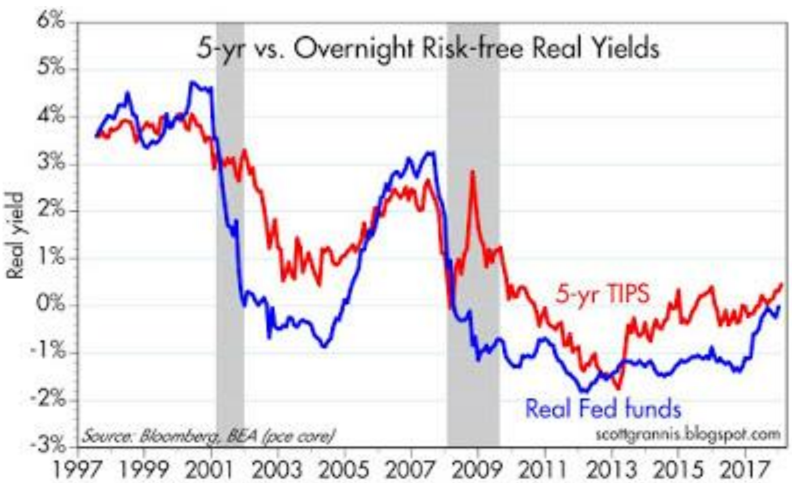
Chart #1 updates Chart #4 from this post earlier this month. The down-trend in bond yields looks to have been broken, and there is plenty of room for yields to move higher still.

<continued>

Chart #2

Chart #2 compares the all-important 5-year real yield on TIPS with the current real Fed funds rate.

The spread between the two is widening, which means the market is pricing in more Fed tightening than it had previously expected. This is good.



But there are still some troubling signs which suggest the market is not yet convinced that the Fed is going to be tightening by as much as it should, given the decline in the demand for money, as I noted in Chart #5 in this post.

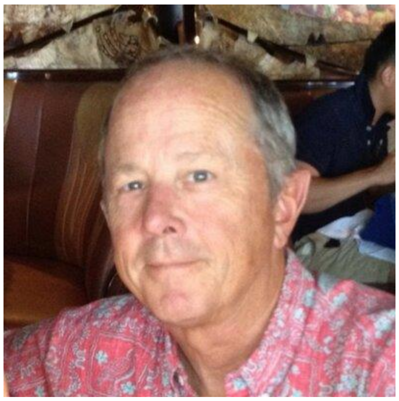
Gold prices are down a bit from their recent highs, but I would like to see them lower still. The dollar has been steady for the past few days, but it is still down by over 10% in the past year.

If the markets were convinced that the economy was strengthening and the Fed would be raising real rates in tandem, then I have to believe the dollar would be a lot stronger and gold weaker. These are things to watch carefully as the year progresses. As I say, we are still in the early innings in all of this.

I am doing my best to keep up, despite having a great time traveling through New Zealand, a trip that has long been on our bucket list.

BW: See ABOUT THE AUTHOR on the following page.

ABOUT THE AUTHOR



Scott Grannis was Chief Economist from 1979-2007 at Western Asset Management, a Pasadena-based, global manager of fixed-income portfolios for institutional clients.

He now enjoys keeping up on economics, markets, and politics from his condo overlooking Calafia Beach on the southern California coast, where he likes to think that he is immune to Wall Street group-think.

Married for 45 years to his Argentine wife, Norma, he has four children and five grandchildren (four boys and one girl).

He is a believer in supply-side economic theory, as practiced by his mentors, the late Jude Wanniski, Art Laffer, and Larry Kudlow. John Rutledge is another of his mentors, from the days that they worked together at Claremont Economics Institute.

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