The Treasury yield curve has inverted, but that’s not the only economic indicator worth following

The inversions continue to happen in the yield curve. This Wall Street-speak means that short-term fixed-income investments like bonds are paying more interest than comparable longer-term
investments, something that hasn’t happened since 2007.

The latest example is the 3-month Treasury bill (yielding 2.45 percent) slightly inverting with the 10-year Treasury (approximately 2.44 percent). Though, according to Bloomberg data they were also even for part of the morning as well.

“The Fed’s downgrade of economic assessment and expectations has spooked investors sufficiently that the 3-month Treasury yield and 10-year Treasury yield are nearing inversion,” says Greg McBride, CFA, Bankrate’s chief financial analyst. “An inversion is an ominous recessionary indicator, but can precede a recession by as much as two years – so don’t start packing up canned goods and heading for the hills quite yet.”
Still a positive sign

The 10-year yield still tops the 2-year Treasury rate, a more widely watched recession indicator. The spread, however, is fewer than 10 basis points.

![Graph showing the yield curve from January 2019 to March 2019](image)

Source: Department of the Treasury

When the yield curve inverts – meaning a shorter-term Treasury bill has a higher yield than a long-term Treasury – it’s predicted every recession back to the late 1960s, McBride says.

Keep in mind that investors usually demand a higher rate of interest for locking up their money longer.

The first Treasury that people buy when risk increases is the 10-year Treasury, says Campbell Harvey, a professor of finance at Duke University.

Harvey says the recent inversion is a lead indicator of a potential recession.

It’s important to note that the media – and others – follow the spread between the 2-year Treasury and the 10-year Treasury, which have flattened to a spread of around 10 basis points, but haven’t inverted.
Why the 90-day Treasury may be a key Treasury to monitor

Harvey says he wrote his 1986 doctoral dissertation at the University of Chicago about the yield curve, focusing on the comparison between the spread between the five-year note and the 90-day Treasury bill. The latter length is key, because it equals the time in a quarter.

“So, there’s always a lead time. The lead time is empirically anywhere from three quarters to six quarters,” Harvey says.

When the 90-day Treasury bill and the 5-year Treasury inverted, the clock started. If it continues for a full quarter, Harvey says that would forecast a recession beginning in 2020.

But Harvey says that the yield curve inversion isn’t the only item on his watch list. According to U.S. Department of the Treasury data, there was a five basis point spread between the 3-month Treasury bill and the 10-year Treasury yesterday.

If the two-year Treasury is higher than the 10-year Treasury, this is an inverted yield curve. Under normal circumstances, a longer-term Treasury should have a higher yield than one with a shorter time horizon.

Even though comparing the 10-year Treasury and the two-year Treasury is a common comparison, there are other comparisons to use.

There are more economic indicators than just the yield curve

- Duke CRO survey: 62 percent of U.S. CRO’s surveyed believe a recession will have begun by the end of 2020.
- Anti-growth trade policy: Harvey says most people are looking at the world trade situation – focusing on China and the U.S. Harvey’s more focused on Brexit. “That would cause very significant disruption of trade in Europe,” Harvey says. “Indeed, there’s some countries in Europe that could be in recession already.”
• **Increased market volatility**: “That’s essentially associated with people in corporations being more hesitant to make capital investment,” Harvey says.

• **Inverted yield curve**: Gradually, the 3-month Treasury bill has been surpassing longer-term treasuries. With the 3-month Treasury bill and the 5-year inverting a couple of weeks ago. And the 3-month Treasury bill and the 10-year Treasury one basis point apart, according to Bloomberg, on Friday morning.

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