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What the Heck Is the Yield Curve? And What Is It Telling Us?

Experts say something called the **yield curve** is pointing to another U.S. recession. But what does that mean?

Terms straight out of economics class don't often find their way into everyday conversation, so we'll try to break it down into plain English -- and let you know if there's anything you can do to protect yourself.

**So, like, what is the yield curve?**
bonds. Think 10-year Treasury notes versus two-year notes.

When things are going well for the economy, rates on long-term bonds are higher than rates on short-term bonds. In exchange for the risk of locking away your money for a longer period, you get higher interest.

It’s protection against the inflation that can flare up during a stronger economy and hurt the value of your money.

**What’s the problem now?**

But recently, long-term bond yields have been tumbling.

Nervousness over the U.S. trade war with China prompted investors to buy up government bonds as a safe haven for their money. The demand for bonds has pushed their prices higher, and when that happens their yields — or interest rates — go lower.

What’s causing experts to worry is that shorter-term investments are starting to pay higher interest than longer-term ones. That’s called an inverted yield curve — and historically, it has spelled recession.

"When the yield curve inverts, it’s not the time to borrow money to take a vacation to Orlando," says Duke University finance professor Cam Harvey, in an interview with Research Affiliates. "This is the time to save."

If you don’t have an emergency fund, you’d better go on that quickly.

**Why should we trust it?**

An inverted yield curve indicates an economic storm is coming.
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The yield curve is a line that plots the yields from Treasury bonds that mature at different times. Normally, it slopes upward, indicating that investors expect higher returns for longer-term investments. An inverted yield curve is when short-term bonds have higher yields than long-term bonds. One exception was in the mid-1960s. But even then, the economy slowed down drastically, stopping just short of a recession.

Note that while an inverted yield curve can indicate a recession is coming, it’s no help with telling us when that will happen.

Sometimes, a recession has come six months later. Other times, it has taken as long as two years.

What should you do?