

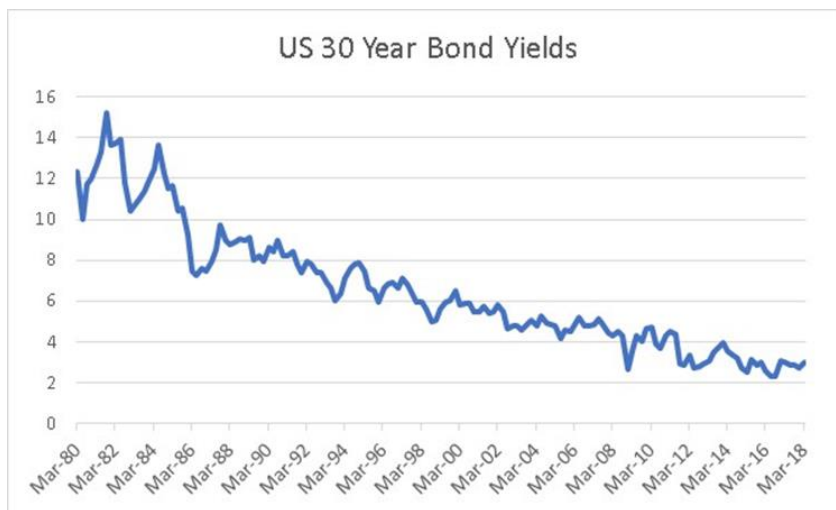
**US 10 TO 30 YEAR TREASURY SPREADS ARE TOO NARROW**



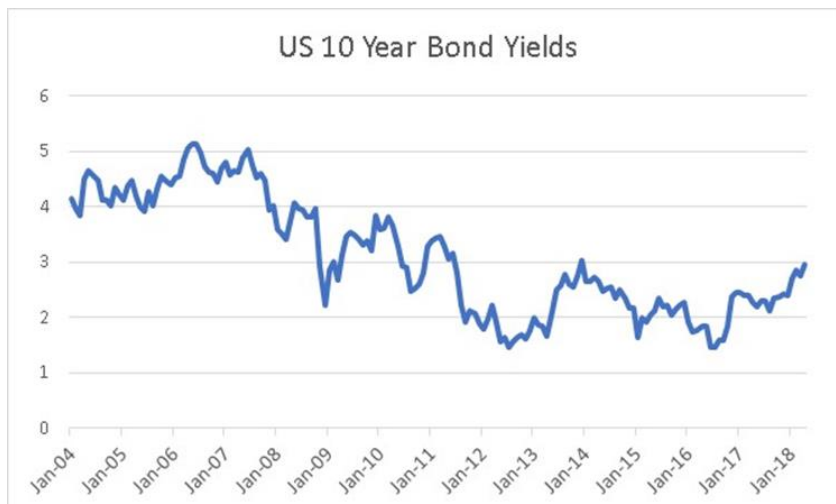
Russell Clark's  
Market Views

"The spread between 30 year and 10 year US bond yields is nearing record lows. This means that the 30 year yield is too low, or the 10 year yield is too high – but which is it?"

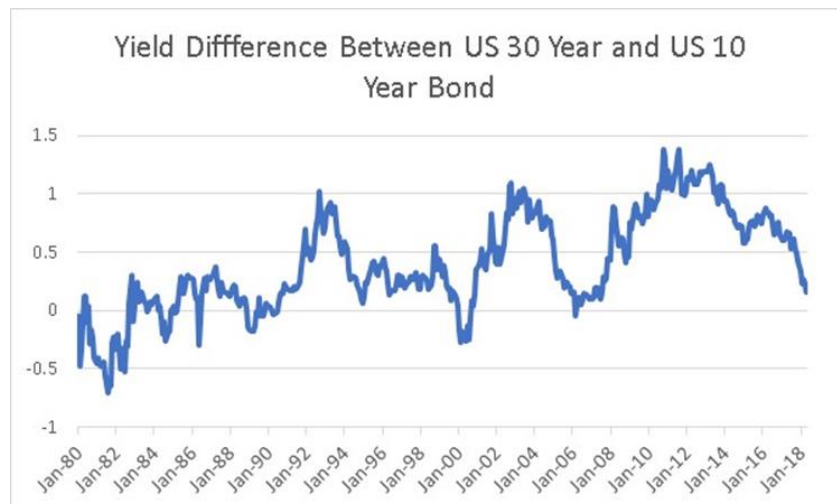
US 10-year bond (treasuries) yields have risen from 1.4% post Brexit to over 3% recently. This is close to the highest yield in 7 years and has prompted talk of the end of the bond bull market. My view, underlined by the importance of housing to the US consumer, is that this makes the 30 year treasury far more important than the 10 year. 30 year bond yields have risen recently to 3%, but are far lower than the highs of 4% seen in 2013.



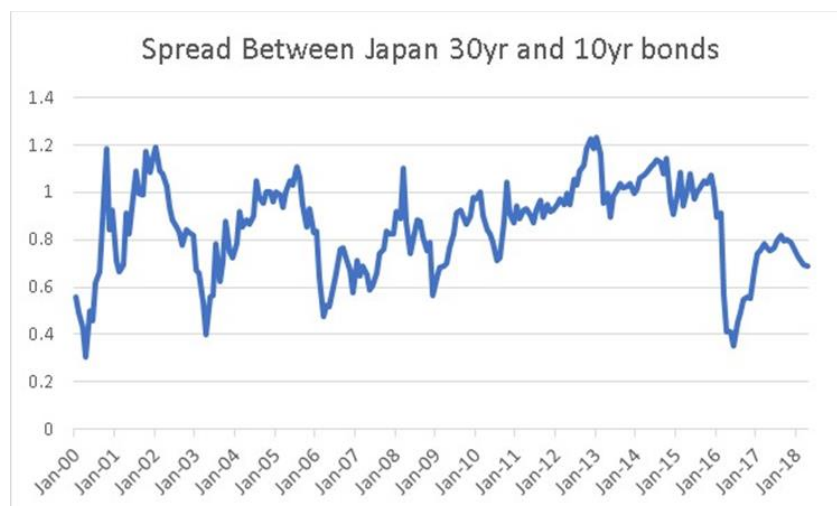
The 10-year bond yield has moved back to levels not seen since 2011, or very briefly in 2013.



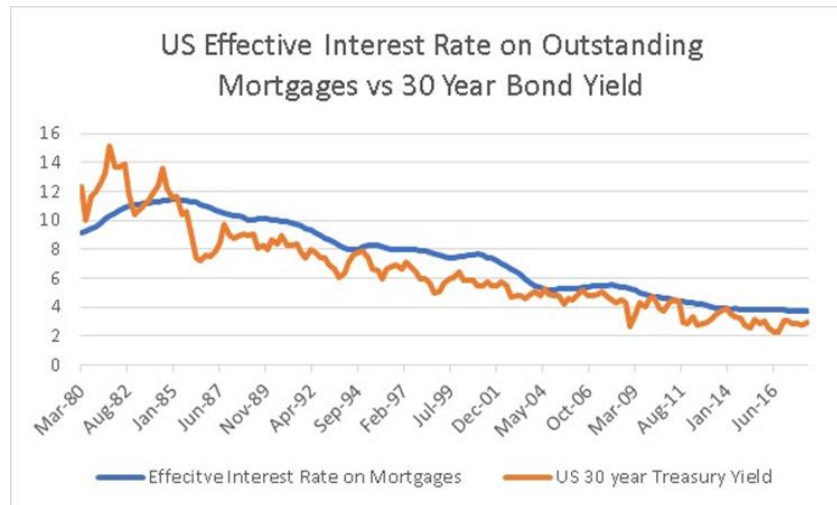
The much smaller sell off in 30-year bonds relative to 10-year bonds has seen the spread between US 10-year treasuries and 30-year treasuries fall to very low levels.



Not only is the spread low versus its own history, it is very low in comparison to either Japan or Germany. Both Japan and Germany currently have spreads of 70bps between their 30-year and 10-year treasuries. Note the start data for Japan and Germany coincides with the earliest data point available on the generic 30-year bond series on Bloomberg.



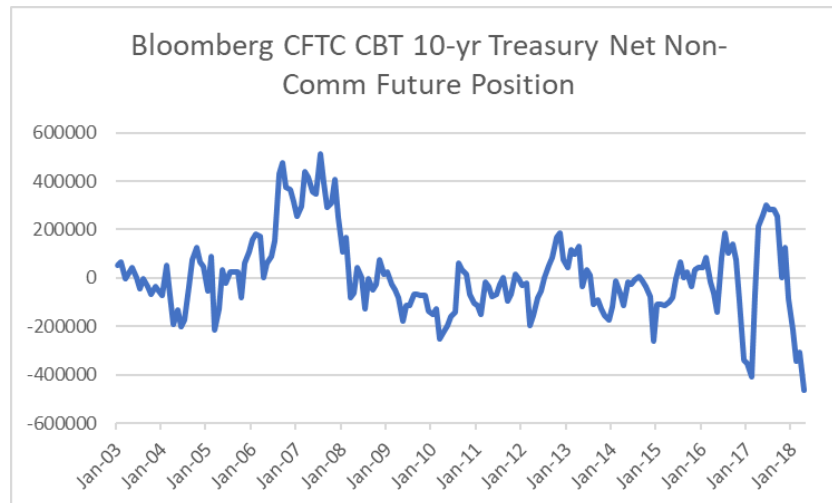
The very low spread in the US offers up two different possibilities; either the 30-year yield is too low, or the 10-year yield is too high. The 30-year mortgage rate is the key driver of both mortgage demand and refinancing. The effective interest rate on outstanding mortgage debt in the US has followed 30-year bond rates lower over time.



Looking at the chart below, we can see that whenever the rate on outstanding mortgage debt begins to rise, US domestic economic weakness has tended to follow. This happened in 2000, and in 2007. Currently offered rates are above outstanding rates, suggesting that if 30 year bond yields continue to rise, then US housing demand will begin to be impacted.



If higher mortgage rates slow growth, then the spread will more likely normalise through the 10-year bond yields falling. Currently, the market has a record spot position in US 10-year bonds.



To my mind, 30-year bond yields are unlikely to rise further, as they will begin to impact the housing market. If higher yields did impact growth then given the very low spread between the ten year bond and the 30 year bond, the move in the 10 year would likely be quite large.

## INFORMATION

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