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FIXED INCOME PERSPECTIVE f*rom the Investment Advisory Group*

Global Flight-to-Quality Sends US Treasury Yields to Historic Lows

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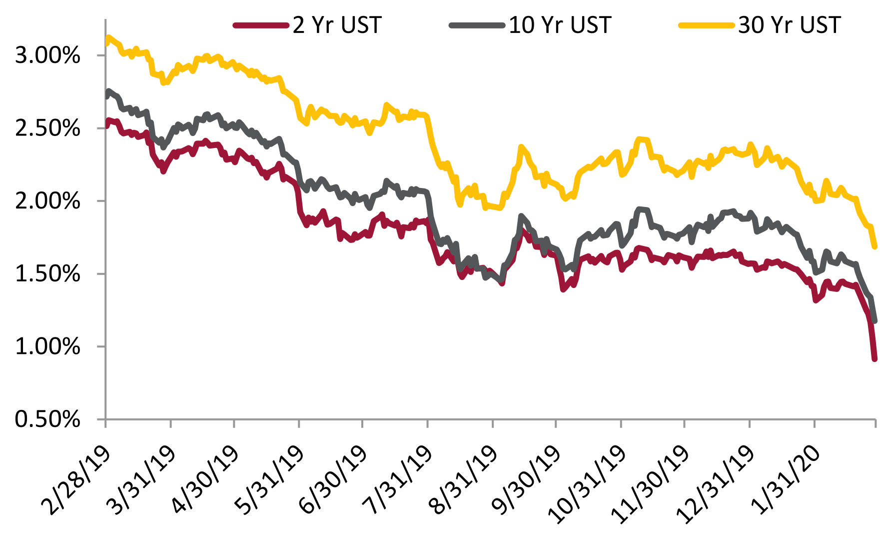
What Happened

Fears and uncertainty around the coronavirus (COVID-19) spreading and becoming a global pandemic have gripped markets and sent US yields tumbling. Questions over the coronavirus's near-term impact on economic growth and the international supply chain are fueling a worldwide flight-to-quality. The yields of 10- and 30-year US Treasury bonds continue to discover historic lows as global investors look to the US for safe haven relief. Early Friday morning, the 10- and 30-year yields fell below 1.20% and 1.70%, respectively. Shorter-term securities are trading in close proximity to the 1.0% level. This suggests market participants expect the US Federal Reserve (Fed) and other global central banks to announce a new round of stimulative action (e.g., interest rate cuts).

2-, 10-, and 30-Year US Treasury Yields Fall on Global Flight-to-Quality



Source: SunTrust IAG, Bloomberg

Our Take

The modest global economic growth uptick we envisioned for 2020 is at risk due to the coronavirus outbreak. The 10- and 30-year US Treasury yields fell roughly 0.45% over the past three weeks. This, coupled with heightened investor anxiety, leads us to lower our 2020 yield outlook.

While an inverted 3Mo/10Yr yield curve has stoked recession fears, we see the 2Yr/10Yr curve's positive slope by 0.24% as a possible salve for immediate recession concerns. Fed funds futures trading implies the market now expects three full rate cuts in 2020. Such strong expectations apply a great deal of pressure for the Fed to act.

High yield spreads spiked 120 basis points in just ten days to their widest since January 2019. The current rate environment offers a more attractive level to begin adding to high yield for those investors awaiting an entry point.

Bottom Line

The US Treasury rally has been significant. After breaching its historic low (1.36%), the 10-year yield continues to fall closer to the 1.0% level. The move in yields to the downside was swift, and they may fall further. On balance, we believe much of the downside move has occurred, with a fair amount of pessimism and slower growth now priced in.

Our base case remains that the US will avoid recession in 2020. We expect rates to trade in a lower range and for global central banks to take action. The Fed will meet March 17-18, where we expect a rate cut with the potential for an interim cut sooner. We would be reluctant to extend duration at today's levels, but maintain our high-quality bias to provide ballast in diversified portfolios.

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