

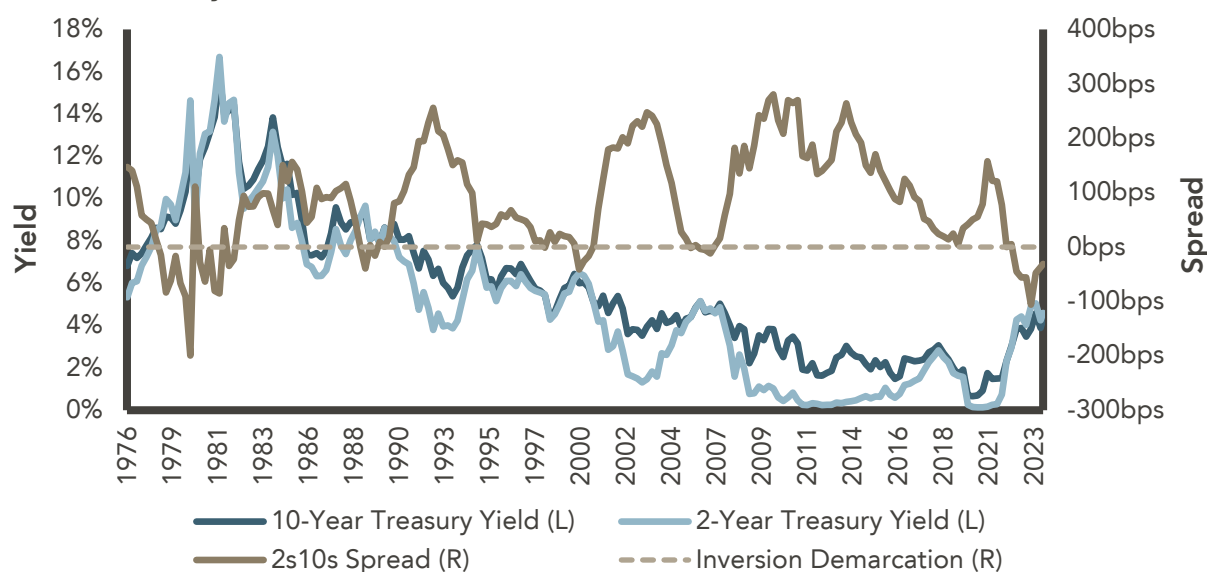
Chart of the Week

February 15, 2024

If the Treasury Curve Could Talk

FRANK VALLE, CFA, CAIA, SENIOR RESEARCH ANALYST

▾ The current inversion of the Treasury curve has been aberrational in length and magnitude relative to history



Source: Bloomberg, Federal Reserve Bank of St. Louis as of February 14, 2024

While most of Marquette's research is written in the third person, this edition of our Chart of the Week series endeavors to anthropomorphize a key feature of the financial system to provide a unique perspective on the current state of capital markets. The following is what readers might expect to hear from a sentient Treasury curve, which is currently suffering from a prolonged inversion.

I just want to feel "normal" again.

For most of my life, longer-dated bonds have provided higher yields than those with shorter maturities. This is often the case since investors expect increased compensation for the increased risks (e.g., higher duration, lower liquidity, etc.) associated with holding long-term bonds, and I am considered upward sloping and normal when these factors are at play. On certain occasions, however, I have been upended as a result of the reversal of those dynamics, though I have usually been able to snap out of those periods of inversion relatively quickly. To that point, the average length of my inversions was less than one year prior to my current funk, which began in July of 2022 and has yet to abate. During this painful time, the 2-Year Treasury yield has been higher than that of the 10-Year by an average of 54 basis points. Put simply, I feel stuck.

CONTINUED >

The last time my inversion was this prolonged or this extreme was during a period of roughly 20 months beginning in the late 1970s amid rampant stagflation. Led by Paul Volcker, the Federal Reserve began aggressively raising the federal funds rate in 1978 to combat elevated price levels, and these efforts led to an acute inversion of more than 200 basis points. I was offered a brief respite in May of 1980, but this period of normalization lasted only a few months before short-term rates started moving higher once again. You may remember this period as the “double-dip recession,” but I think the “double-dip inversion” is just as apt a descriptor given my behavior! I have inverted on a few occasions since that difficult time. Specifically, I became inverted again in the late 1980s after a lengthy peacetime expansion drove inflation higher and the federal funds rate increased as a result. Still, that inversion lasted less than a year, as then-Fed Chair Alan Greenspan was forced to cut rates to mitigate a recession that began in 1990. I next became inverted when the Fed increased rates in the early 2000s after the longest period of domestic economic growth to that point. This inversion lasted around seven months before Greenspan came to the rescue once again by cutting rates following the busting of the Dot-Com Bubble, a fall in business investing, and the September 11th attacks. When I became inverted in the lead-up to the Global Financial Crisis, it was Ben Bernanke who straightened me out after just six months.

As I mentioned earlier, my current inversion is particularly pronounced relative to my history, and I have spent the last several months asking myself the following question: How can I get out of this predicament? In theory, longer-dated yields could increase and restore my normalcy, however market participants have such strong demand for long-dated bonds at present that those yields may be range-bound. With that in mind, an appeal to Jerome Powell to lower the federal funds rate may be my only hope. This being the case, you can imagine my dismay at this week’s CPI reading, which came in hotter than expected at 3.1% on a year-over-year basis. Until we see inflation inch closer to the 2.0% target established by the Fed, I believe that Powell will likely hold short-term rates at their current levels and my inversion will continue. ■

PREPARED BY MARQUETTE ASSOCIATES

180 North LaSalle St, Ste 3500, Chicago, Illinois 60601 PHONE 312-527-5500
CHICAGO BALTIMORE MILWAUKEE PHILADELPHIA ST. LOUIS WEB marquetteassociates.com

CONFIDENTIALITY NOTICE: This communication, including attachments, is for the exclusive use of the addressee and contains proprietary, confidential and/or privileged information; any use, copying, disclosure, dissemination, or distribution is strictly prohibited. Marquette Associates, Inc. retains all proprietary rights they may have in the information.

Marquette Associates, Inc. ("Marquette") has prepared this document for the exclusive use by the client or third party for which it was prepared. The information herein was obtained from various sources, including but not limited to third party investment managers, the client's custodian(s) accounting statements, commercially available databases, and other economic and financial market data sources.

The sources of information used in this document are believed to be reliable. Marquette has not independently verified all of the information in this document and its accuracy cannot be guaranteed. Marquette accepts no liability for any direct or consequential losses arising from its use. The information provided herein is as of the date appearing in this material only and is subject to change without prior notice. Thus, all such information is subject to independent verification and we urge clients to compare the information set forth in this statement with the statements you receive directly from the custodian in order to ensure accuracy of all account information. Past performance does not guarantee future results and investing involves risk of loss. No graph, chart, or formula can, in and of itself, be used to determine which securities or investments to buy or sell.

Forward-looking statements, including without limitation any statement or prediction about a future event contained in this presentation, are based on a variety of estimates and assumptions by Marquette, including, but not limited to, estimates of future operating results, the value of assets, and market conditions. These estimates and assumptions, including the risk assessments and projections referenced, are inherently uncertain and are subject to numerous business, industry, market, regulatory, geopolitical, competitive, and financial risks that are outside of Marquette's control. There can be no assurance that the assumptions made in connection with any forward looking statement will prove accurate, and actual results may differ materially.

The inclusion of any forward-looking statement herein should not be regarded as an indication that Marquette considers forward-looking statements to be a reliable prediction of future events. The views contained herein are those of Marquette and should not be taken as financial advice or a recommendation to buy or sell any security. Any forecasts, figures, opinions or investment techniques and strategies described are intended for informational purposes only. They are based on certain assumptions and current market conditions, and although accurate at the time of writing, are subject to change without prior notice. Opinions, estimates, projections, and comments on financial market trends constitute our judgment and are subject to change without notice. Marquette expressly disclaims all liability in respect to actions taken based on any or all of the information included or referenced in this document. The information is being provided based on the understanding that each recipient has sufficient knowledge and experience to evaluate the merits and risks of investing.

This presentation does not constitute an offer to sell, or a solicitation of an offer to buy, any interest in any investment vehicle, and should not be relied on as such. Targets, ranges, and expectations set forth in this presentation are approximations; actual results may differ. The information and opinions expressed herein are as of the date appearing in this material only, are subject to change without prior notice, and do not contain material information regarding the Marquette Model Portfolio, including specific information relating to portfolio investments and related important risk disclosures. The descriptions herein of Marquette's investment objectives or criteria, the characteristics of its investments, investment process, or investment strategies and styles may not be fully indicative of any present or future investments, are not intended to reflect performance and may be changed in the discretion of Marquette. While the data contained herein has been prepared from information that Marquette believes to be reliable, Marquette does not warrant the accuracy or completeness of such information. Client account holdings may differ significantly from the securities in the indices and the volatility of the index may be materially different from client account performance. You cannot invest directly in an index.

About Marquette Associates

Marquette was founded in 1986 with the sole objective of providing investment consulting at the highest caliber of service. Our expertise is grounded in our commitment to client service — our team aims to be a trusted partner and as fiduciaries, our clients' interests and objectives are at the center of everything we do. Our approach brings together the real-world experience of our people and our dedication to creativity and critical thinking in order to empower our clients to meet their goals. Marquette is an independent investment adviser registered under the Investment Advisers Act of 1940, as amended. Registration does not imply a certain level of skill or training. More information about Marquette including our investment strategies, fees and objectives can be found in our ADV Part 2, which is available upon request and on our website. For more information, please visit www.MarquetteAssociates.com.