# The StockCharts.com Market Message

*Featuring our commentators, John Murphy and Arthur Hill*

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## TREASURY YIELDS FALL BELOW 200-DAY AVERAGE ON WEAK INFLATION NUMBERS -- CRUDE OIL FALLS TO LOWEST LEVEL IN A YEAR -- LOWER FOREIGN BOND YIELDS ARE ALSO WEIGHING ON TREASURY YIELDS

*By John Murphy*

**TEN-YEAR TREASURY YIELD FALLS BELOW 200-DAY AVERAGE...** Expectations are for another Fed rate hike this afternoon. Bond yields, however, are falling sharply. Chart 1 shows the **10-Year Treasury Yield ($TNX)** falling 9 basis points to the lowest level since last November. The yield has also slipped below its 200-day average for the first time in seven months. While the Fed controls short-term rates, long term rates are determined by other factors, including inflation. Today's yield drop is based primarily on weak inflation numbers (and weaker retail sales data). The CPI for May fell 0.1%, which pushed its annual rate to 1.9% (below the Fed target of 2%). Core CPI (excluding food and energy) gained 0.1% in May, but fell to 1.7% over the last year. That figure is down from 2.3% in January, and marks the second decline in the last three months. Weak inflation numbers can be associated with a weaker economy, and makes it more difficult for the Fed to justify higher rates. And weakens the case for higher bond yields. Energy has been the biggest contributor to the CPI drop.


(click to view a live version of this chart)

**Chart 1**

**FALLING ENERGY PRICES PULL YIELDS LOWER...** Although food and energy prices are excluded from core inflation figures (apparently economists don't shop or drive), they are an important part of overall price inflation. But they are included in the headline CPI figures, and energy prices s have been a big drag on those figures. And bond yields. Chart 2 compares the **10-Year T-Note** (green bars) to the price of the **United States Oil Fund (USO)** over the last year (black line). Rising oil prices during 2016 helped set the stage for an upturn bond yields during the second half of that year. After rising together during the fourth quarter, both markets peaked at the end of year. And both have been trending lower since then. The black line shows the USO price of oil falling to the lowest level in a year today. Most other commodities have also been falling. The **Bloomberg Commodity Index** recently fell to the lowest level in a year as well. Falling commodity prices are one of the main reasons that bond yields are dropping. Another reason has to do with even lower foreign bond yields.

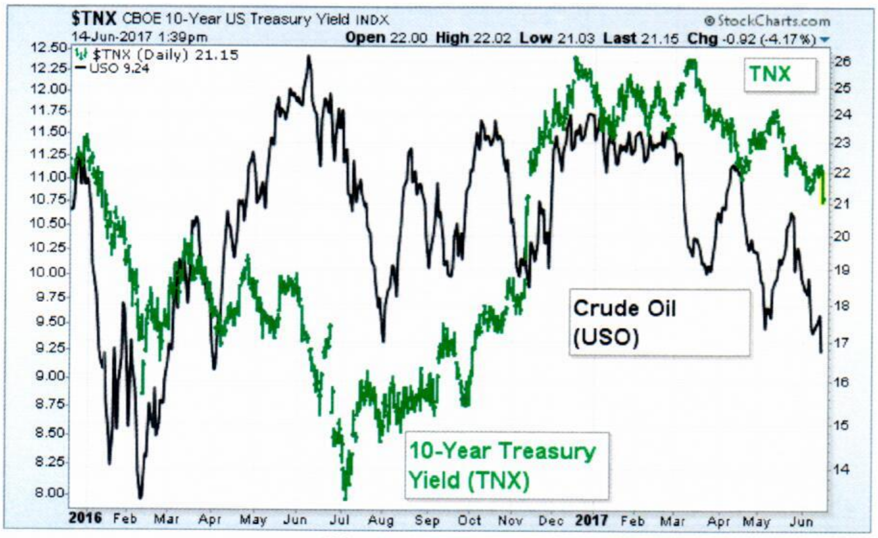


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**Chart 2**

**FOREIGN BOND YIELDS WEIGH ON TREASURY YIELD...** Historically low foreign bond yields (including bonds with negative yields) are another factor pulling Treasury yields lower. Chart 3 plots the **10-Year Treasury yield** (through Tuesday) relative to 10-Year yields in **Britain (red**

**line), Germany (blue line), and Japan (orange line).** The Japanese yield is anchored near zero. British and German 10-Year yields have fallen to 0.92% and 0.22% today respectively. By contrast, the 10-Year Treasury yields 2.11%. That may seem low to American investors. But that higher Treasury yield looks very attractive to foreign buyers. Even though the Fed is starting to hike short-term rates here, quantitative easing in Europe and Japan is keeping their bond yields from rising. That may explain why Treasury yields are higher than foreign developed yields. But it also explains why it's hard for bond yields to climb in that low global yield environment. I recently suggested that stronger foreign stock markets were helping support U.S. large cap multinationals that benefit from foreign sales. Treasuries are also benefiting from foreign influences. Rising foreign bond prices (supported by central bank buying) are helping keep a strong bid under Treasury bonds. The fact that Treasury yields are higher than foreign bond yields also makes Treasuries a relative bargain. So don't be too surprised if bond yields don't jump on today's expected rate hike. Treasury yields are reacting to falling foreign yields, and all of them may be reacting to falling energy prices.

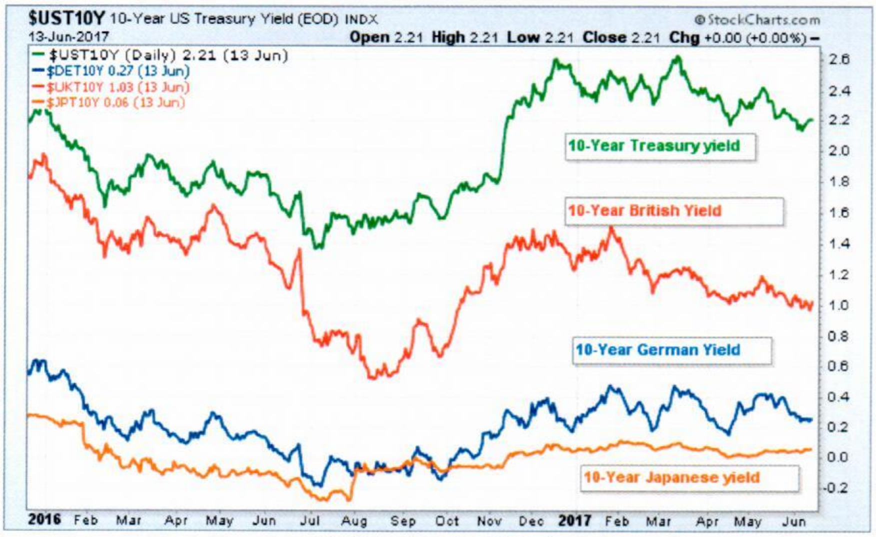


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**Chart 3**

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