

Treasury yields climb as markets out-hawk the Fed

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The key question: how far will the hiking cycle go? Markets are pricing in more rate hikes than the median FOMC projection

While the median FOMC projection points to just one additional hike, markets are pricing in between three and four additional rate hikes by September 2027 ([Figures 4](#) and [5](#)).

The reassessment of the policy outlook has pushed Treasury yields sharply higher, with the 10-year yield reaching around 5.3% as markets price in resilient growth ([Figures 8](#) and [9](#)).

The rise in nominal yields has been almost entirely matched by higher real yields ([Figure 10](#)), while breakeven inflation rates remain broadly stable ([Figure 12](#)).

Higher expected short-term real rates, rather than the term premium, now account for most of the rise in the 10-year yield ([Figures 13](#) and [14](#)).

Mortgage rates rose further up ([Figure 16](#)), adding to the drag on the housing sector, while credit spreads remain very low, possibly reflecting increased competition for capital ([Figure 17](#)).

Two weeks ago, the Fed unanimously raised the fed funds rate by 25 bps to 3.75–4.00%, reinforcing its commitment to a more timely return of inflation to target and driving yields higher across the curve

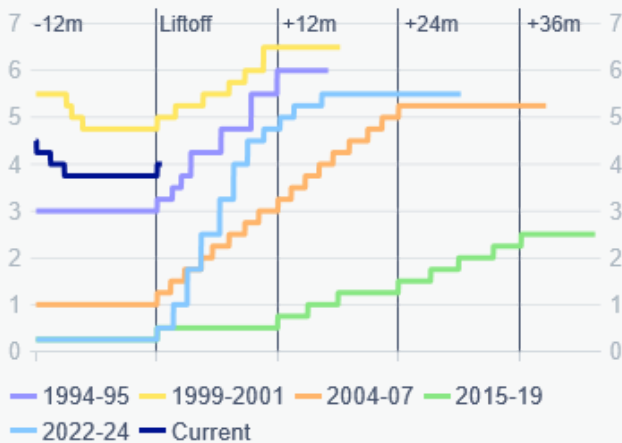
FIGURE 1. FED FUNDS RATE AND TREASURY YIELDS (%)



The gray area indicates the fed funds rate target range
Source: BBVA Research, Fed, Treasury Dept.

The Fed highlighted resilient domestic spending and no longer attributed elevated...

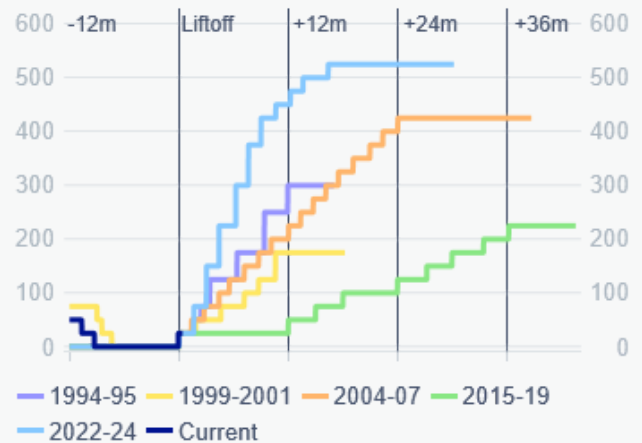
FIGURE 2. FED FUNDS RATE IN TIGHTENING CYCLES (%)



Target rate for the 1994-95, 1999-2001, and 2004-07 cycles; upper limit of the target rate range for the 2015-19 and 2022-24 cycles. Source: BBVA Research, Fed

... inflation and inflationary risks solely to supply-side shocks. While the median FOMC...

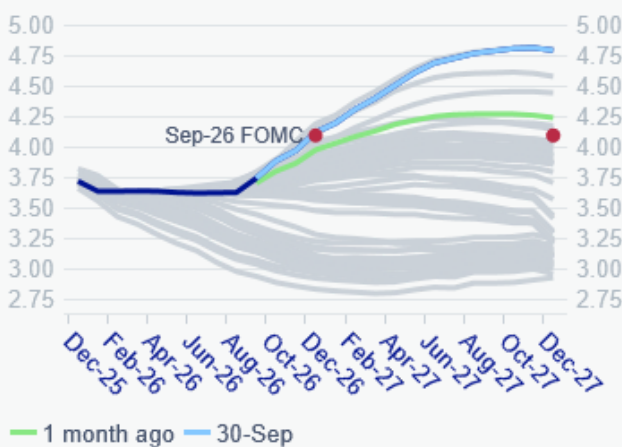
FIGURE 3. FED FUNDS RATE IN TIGHTENING CYCLES (BPS VS LIFTOFF)



Source: BBVA Research, Treasury Dept.

... projection points to just one additional hike, markets are pricing in a much more...

FIGURE 4. FUTURES-IMPLIED FED FUNDS RATE (%)



The gray lines indicate weekly implied rate paths over the past year. Source: BBVA Research, CME, Fed

... aggressive path, with three additional hikes fully priced in by September 2027

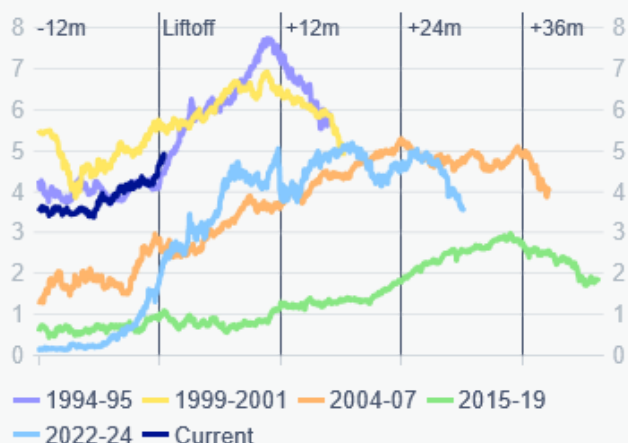
FIGURE 5. FUTURES-IMPLIED FED FUNDS RATE (%)



The gray area indicates the fed funds rate target range Source: BBVA Research, CME, Fed

A cooler-than-expected core PCE print and downward revisions were not enough...

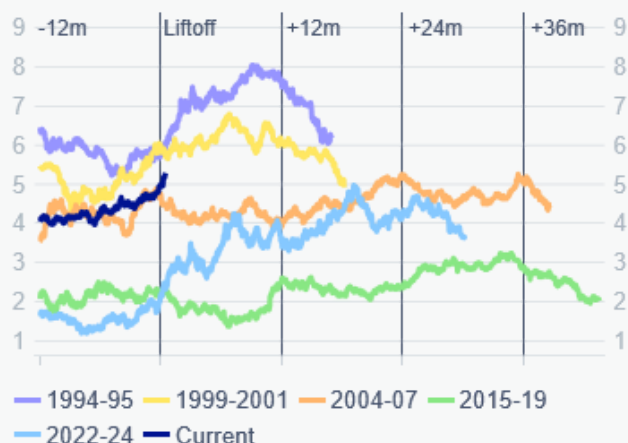
FIGURE 6. 2-YEAR TREASURY YIELD IN TIGHTENING CYCLES (%)



Source: BBVA Research, Treasury Dept.

... to stop long-term rates from climbing further. Reflecting this shifting rate outlook, ...

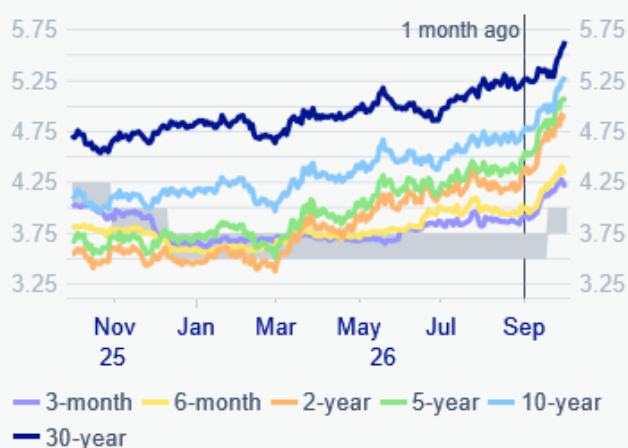
FIGURE 7. 10-YEAR TREASURY YIELD IN TIGHTENING CYCLES (%)



Source: BBVA Research, Treasury Dept.

... Treasury yields have surged, with the 10-year yield hitting a 24-year high of...

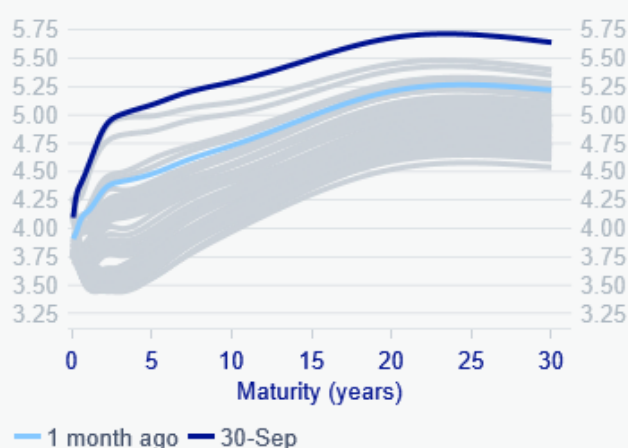
FIGURE 8. TREASURY YIELDS (%)



The gray area indicates the fed funds rate target range
Source: BBVA Research, Fed, Treasury Dept.

... around 5.3%. The sharp rise in Treasury yields this month reflects expectations of...

FIGURE 9. TREASURY YIELD CURVE (%)



The gray lines indicate weekly curves over the past year; intermediate rates calculated with natural cubic spline interpolation
Source: BBVA Research, Treasury Dept.

... resilient economic growth ahead: the rise in nominal yields has been almost entirely...

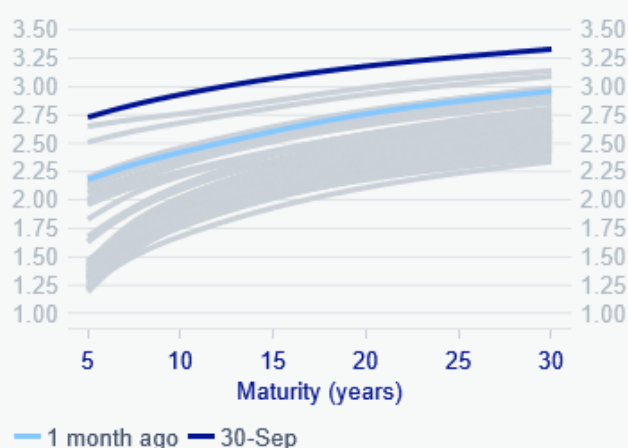
FIGURE 10. TREASURY REAL YIELDS (TIPS) (%)



Source: BBVA Research, Fed, Treasury Dept.

... matched by higher real yields across the curve, while breakeven inflation rates have...

FIGURE 11. TREASURY REAL YIELD CURVE (TIPS) (%)



The gray lines indicate weekly curves over the past year; intermediate rates calculated with natural cubic spline interpolation
Source: BBVA Research, Treasury Dept.

... remained broadly stable. Higher expected short-term real rates, rather than the term...

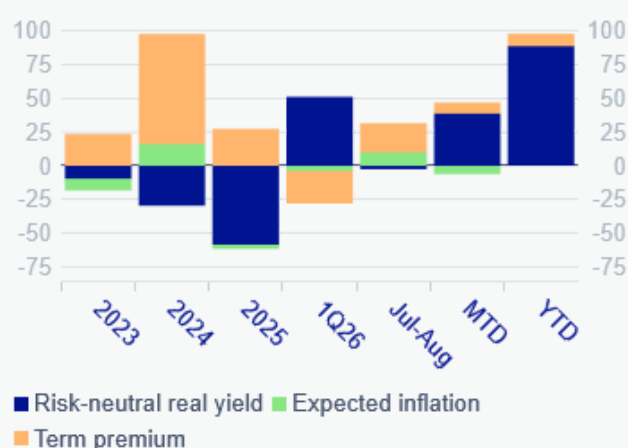
FIGURE 12. BREAKEVEN INFLATION RATES (%)



Source: BBVA Research, Treasury Dept.

... premium, now account for most of the rise in the 10-year yield. While no longer the main...

FIGURE 13. 10-YEAR TREASURY YIELD CHANGE BREAKDOWN (BPS)



* Based on the NY Fed ACM model
Source: BBVA Research, Fed, Treasury Dept.

... driver, term premia continue to keep a high floor under yields. The...

FIGURE 14. 10-YEAR TREASURY YIELD BREAKDOWN (%)



Based on the NY Fed ACM model
Source: BBVA Research / Fed

... upward shift in the policy path has given the US dollar renewed momentum

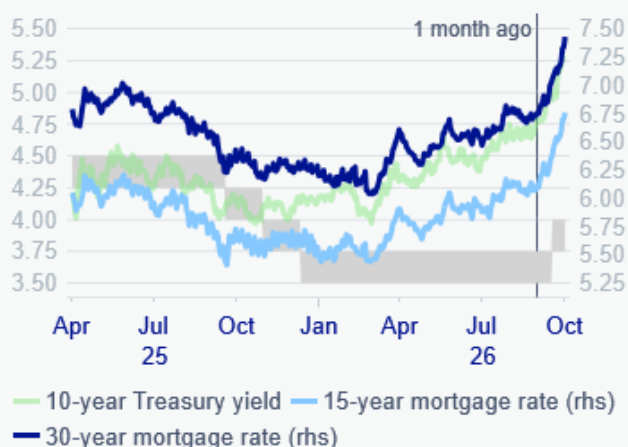
FIGURE 15. 10-YEAR TREASURY YIELD & DXY INDEX (% & INDEX POINTS)



Source: BBVA Research, ICE, Treasury Dept.

Yields pushed mortgage rates even higher, deepening the drag on the housing sector

FIGURE 16. MORTGAGE RATES (%)



The gray area indicates the fed funds rate target range (rhs)
Source: BBVA Research, Bankrate, Fed, Treasury Dept.

Credit spreads remain very low, possibly reflecting increased competition for capital

FIGURE 17. CORPORATE BOND YIELD SPREADS (%)



Spreads over the 10-year Treasury yield; the shaded area indicates the deviation from the historical average since 2008
Source: BBVA Research, Fed, Treasury Dept.

The sharp repricing in Treasury yields has pushed bond market volatility higher, though only to somewhat above its historical average

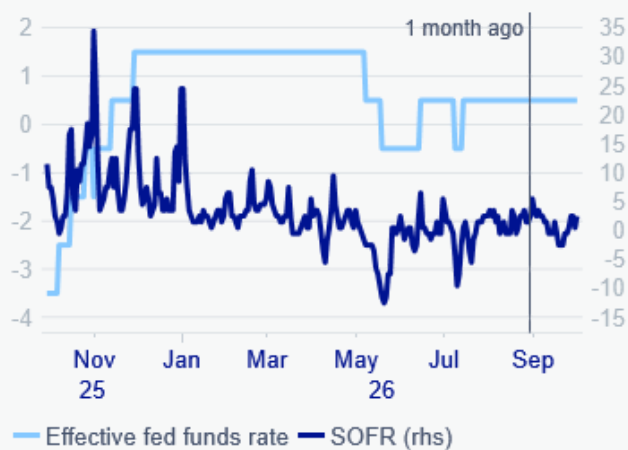
FIGURE 18. ICE BOFAML MOVE INDEX (INDEX POINTS)



The shaded areas indicate the ranges within one and two standard deviations from the mean
Source: BBVA Research, ICE BofAML

The recent increase in volatility has not translated into funding pressures while ...

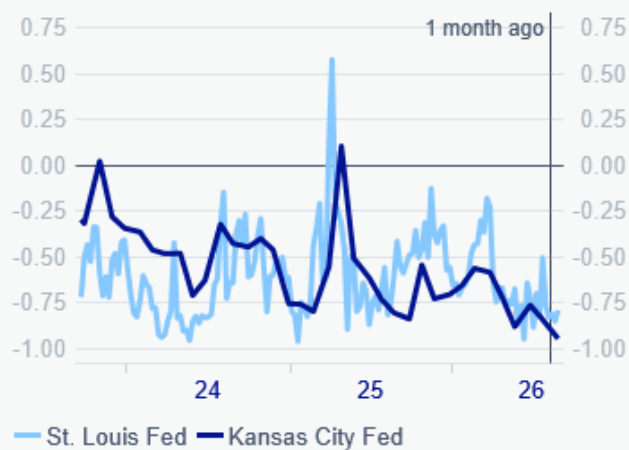
FIGURE 19. MONEY MARKET RATE SPREADS (BPS)



Spreads over the midpoint target fed funds rate
Source: BBVA Research, Fed

... broader financial stress remains contained despite persistently high interest rates

FIGURE 20. FED FINANCIAL STRESS INDEXES (>0: ABOVE AVG. FIN. STRESS)



Source: BBVA Research, Fed

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