

AI-00986 Bond Yield vs Fed Interest Rate

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Explain the relationship of fed interest rates to bond yield. How does the bond yield affect the risk on or risk off sentiment?

Federal interest rates and bond yields have an inverse relationship. When the Fed raises interest rates, bond yields typically rise as well. This happens because investors can now earn a higher return on new bonds issued with the prevailing interest rate. As a result, the price of existing bonds with lower fixed interest rates becomes less attractive, causing their prices to fall and their yields to rise to become more competitive.

This relationship between bond yields and risk sentiment is complex. Higher bond yields can be seen as a sign of a stronger economy, which can be positive for risk-on sentiment. However, rising yields can also indicate inflation concerns, which can lead to risk-off sentiment. Investors may become more cautious and seek out safer assets like bonds when inflation is a worry.

Ultimately, the impact of bond yields on risk sentiment depends on the specific economic conditions and investor expectations.

Sure! Here is the summary in a table format:

Factor	Effect
Federal Interest Rates	Increase
Bond Yield	Increase
Reason	New bonds offer higher returns, making existing bonds less attractive
Impact on Risk Sentiment	Complex

Positive for Risk-On	Sign of stronger economy
Positive for Risk-Off	N/A
Negative for Risk-On	N/A
Negative for Risk-Off	Inflation concerns lead to seeking safer assets like bonds