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Week 6 News Analysis

https://www.ft.com/content/5d1830ff-6194-4db1-ad52-eaa7b189cacf

"Tighter US Bond market could dull pressure on Treasury prices from QE tapering", Financial Times, August 13, 2021

The bond market is experiencing very high demand and a relatively low supply, keeping yields down. The Treasury is considering reducing the amount of bonds it will sell, owing to the lessened need for funding stimulus programs. The Fed is also considering tapering it's purchases of bonds. Normally a Fed taper would lead to an increase of debt available for investors, but with a simultaneous taper of Treasury sales there may be little effect in the market. At a Treasury note auction this past Wednesday, foreign buyers bought 77% of available bonds, worth $32bn. This left big financial companies who are obliged to absorb excess supply taking the smallest percentage of offerings on record.

The high demand of low yield bonds it's telling of how much investors value (practically) guaranteed positive returns, no matter how small. Negative rates in many other top rated bonds (e.g. ECB), and a week of difficult news (IPCC report, Taliban advances, China's 5-year plan for continued tightened markets) likely contributed to the international flight to security. Treasury yields slipped further after the release of the UMich consumer confidence index showing that consumers are less confident now than they have been since April 2008[1].

At the same time, banks on Wall Street anticipate that the current bull market will continue for at least the short term[2], and investment banks are quickly returning to business as usual[3]. Multiple inflation pressures (wage driven, tight supply chains[4], increased government spending[5], and increases in M1) make the longer term outlook very unclear, but positive earnings reports and new infrastructure commitments are keeping short term projections rosy.

Overall, the market right now is highly conflicted, and it's interesting that the highly liquid bond market may render another of the Fed's tools (a reduction in QE) less effective than in the past. Differing sentiments between Wall Street and consumers is not unusual, but the present disconnect is particularly vertigo inducing.

1https://www.ft.com/content/cdad3914-f0e2-4b1d-b85f-baa044c09a72
2https://www.ft.com/content/4b53fe3a-b0de-4827-bcd9-613593547f2c
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