Treasury bond yield inversion signals economic pain

Rising yields on shorter-term Treasurys may signal correction in equity markets or recession

Hawkish comments by Federal Reserve Chairman Jerome Powell about efforts to tame inflation have deepened the inversion of the bond yield curve for U.S. Treasury securities, which many on Wall Street have come to view as a leading indicator of an upcoming recession.

Powell delivered the Fed's semi-annual update to Congress on monetary policy this week and told lawmakers that the central bank will need to raise interest rates higher than previously expected because inflation has remained persistently high despite a series of rate hikes amid strong economic growth.

One of the most closely watched spreads on the yield curve is that between the two-year and 10-year Treasury notes, which is referred to as the "2/10 spread" as shorthand. The 2/10 spread has been inverted in July 2022 – just four months after the Fed began to raise rates last March.

The 2/10 spread reached negative 103.1 basis points on Tuesday – the largest inversion between those securities since September 1981 when the economy was in a recession as the Fed was raising interest rates to tamp down rampant inflation – and widened to about 107 basis points Wednesday.

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