

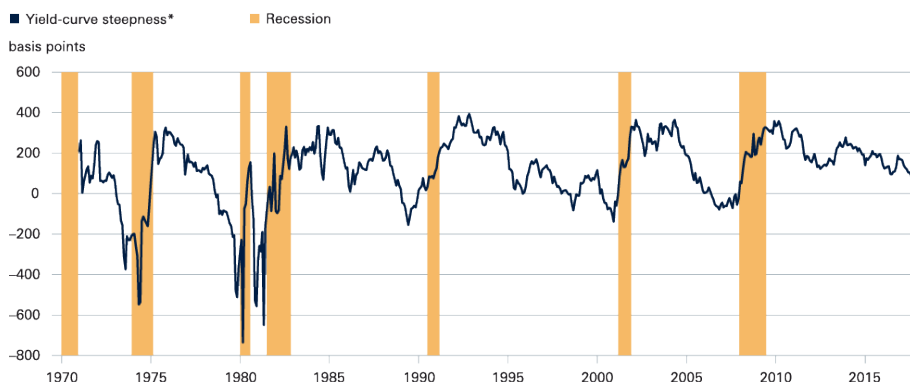


Chart of the week

Since 2010, the U.S. yield curve has flattened, but this does not necessarily suggest that recession risks have grown.

Since at least 1970, every recession in the United States has been preceded by an inverted yield curve. However, there have also been inverted yield curves that were not immediately followed by a recession, as our chart of the week shows. An inverted yield curve is unusual. It arises when short-term yields rise above long-term yields, or when long-term yields fall below short-term yields. Normally, you would demand a higher yield when buying, say, 10-year U.S. Treasuries than those with a 2-year maturity. How much higher partly depends on how high you expect economic growth, inflation, and the future path of the US Federal Reserve Board's (the Fed's) policy rates to be. This makes the yield curve quite a useful, and widely watched, economic indicator.

We expect the U.S. yield curve to flatten further. Growth skeptics may take this as a sign of economic gloom. However, it has on average taken 14 months until an inverted yield curve (10-year Treasury bond yield minus federal funds rate) was followed by recession. Extrapolating from the recent flattening that would suggest a recession at some point in the early 2020s. Of course, all this might be less applicable than history suggests. Through quantitative easing, central banks seemingly have significantly distorted yield curves. In any case, we don't currently expect the U.S. economy to drop into a recession for the next two years.



Sources: Bloomberg Finance L.P., Deutsche Asset Management Investment GmbH as of 12/7/17
* 10-year U.S. Treasury bond yield minus federal funds rate

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Glossary

Federal funds rate

The **federal funds rate** is the interest rate, set by the Fed, at which banks lend money to each other, usually on an overnight basis.

Quantitative easing (QE)

Quantitative easing (QE) is an unconventional monetary-policy tool, in which a central bank conducts broad-based asset purchases.

U.S. Federal Reserve Board (the Fed)

The **U.S. Federal Reserve Board**, often referred to as "**the Fed**", is the central bank of the United States.

Yield curve

A **yield curve** shows the annualized yields of fixed income securities across different contract periods as a curve.

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