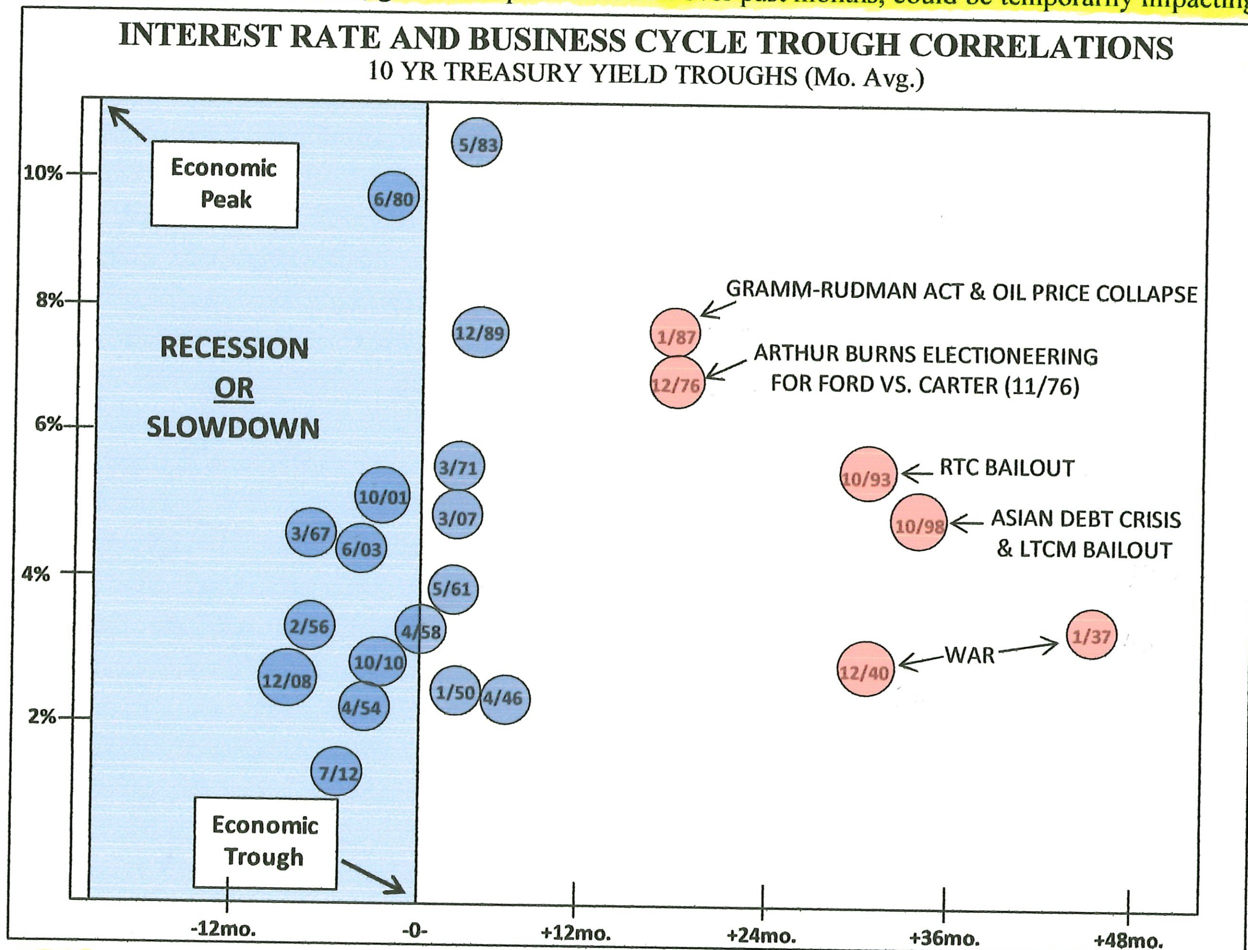
BUSINESS CYCLE DEVELOPMENTS

T-Note yields are still reaching for a cyclical bottom in response to the business cycle bottom. The spike to a *monthly average* low of 1.78% in the T-Note yield in February 2016 appears to have been a response to China's 2nd devaluation and the cut in their reserve requirements in January 2016 and not a low in U.S. yields related to the current U.S. recession. Similar knee-jerk drops in yields – unrelated to the economic cycle – have occurred in response to Black Monday (10/87) or when the ECB started its QE program (1/15). Therefore, we're back to a surveillance of when, and at what levels, will yields turn cyclically higher in response to a U.S. economic recovery.

To date, there's no change in the six of seven **Interest Rate Trough Indicators** which are pointing to March 2016 (January thru May 2016) as an area for the cyclical low in yields responding to economic recovery – see the cluster of observations observed at economic recoveries below. Brexit, which is believed to have been fully discounted, given the open discussion over past months, could be temporarily impacting



yields, but the overwhelming influence has got to be the U.S. economy. It's improving very slowly from the -3.1% decline for 16 months from November 2014 thru March 2016. There's no thrust upward in output, as in past recoveries, from the March 2016 lows, to date. If this weak rebound in the Index of Industrial Production continues then it explains the reluctance of yields to respond as in past periods. This is not one of the six outliers on the attached chart – where yields fail to respond to economic recovery, but continue to decline for many months after recovery. Those outliers were all exogenous shocks triggered by legislation, Fed manipulation or a specific crisis. Assuming no further Fed options for manipulation, the outlook is for U.S. yields to respond to an economic recovery that centers in May 2016 and extends to September 2016.