

The Markets

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MidWestOne™
WEALTH MANAGEMENT



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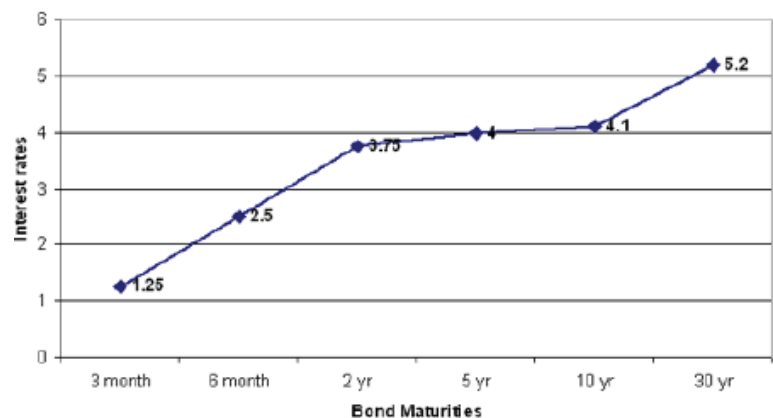
Watching the Yield Curve

Bond maturities and their yields are related. Typically, bonds with longer maturities pay higher yields. Why? Because the longer a bondholder must wait for the bond's principal to be repaid, the greater the risk compared to an identical bond with a shorter maturity, and the more return investors demand.

If you were to draw a line on a chart that compares the yields of, for example, Treasury securities with various maturities, you would typically see a line that slopes upward as maturities lengthen and yields increase. The greater the difference between the yields on T-bills and 30-year bonds, the steeper that slope. A steep yield curve often occurs because investors want greater compensation for tying up their money for longer periods and running the risk that inflation will cut net returns over time. A flat yield curve means that there is little difference between short and long maturities.

However, sometimes the yield curve can actually become inverted; in this case, short-term interest rates are higher than long-term rates. For example, in 2004 the Federal Reserve Board began increasing short-term rates, but long-term rates didn't rise as quickly. A yield curve that stays inverted for a period of time is believed to indicate a recession may be about to occur.

A Sample Treasury Yield Curve



One of the most widely used yield curves is that for Treasury securities. They have virtually no credit risk because they are backed by the full faith and credit of the U.S. government as to the timely payment of principal and interest.

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