November 2016
Ask a Trust Officer

The yield curve

Dear Trust Officer:

What is the “yield curve”? What does it tell us? Does the Federal Reserve Board control the yield curve? How do I take the yield curve into account in shaping my portfolio??—*Novice Investor*

Dear Novice:

The yield curve is a graph of current interest rates for various bond maturities. Normally, the curve slopes upward; that is, interest rates are higher as the time to a bond’s maturity increases. Sometimes the curve flattens, as short-term interest rates and longer-term rates edge closer together. When the yield curve slopes downward, when long-term rates are lower than short-term rates, the curve is said to be “inverted.” This situation may occur when investors think that the prospects for future inflation are much lower than today’s. An inverted yield curve is thought by some observers to be a signal of a coming recession.

The Fed controls only the shortest-term interest rates, the discount rate and the federal funds rate, which are overnight interest rates. However, the Fed’s program of quantitative easing has had effects all along the yield curve.

There are many strategies that we can tell you about in managing a bond portfolio, including:

- Matching maturities to your time horizon;
- Building a bond ladder;
- Balancing risks with intermediate maturities.

We’d be pleased to tell you more at your earliest convenience.

Do you have a question concerning wealth management or trusts? Send your inquiry to aspears@firstbankrichmond.com.

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