



As markets are likely to price in further rate cuts into 2025 once the Fed moves, CIO sees lower bond yields by year-end, forecasting the 10-year Treasury yield at 3.85%. (UBS)

# Evidence continues to support a start to Fed easing later this year

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**The yield on 10-year US Treasuries rose 5 basis points to 4.34% on the last trading day of June, bringing the rise to almost 10 basis points basis last week, with a pickup in inflation in Australia and Canada highlighting investor concerns over sticky price pressures in parts of the world.**

Month-end index rebalancing—in which bonds sold during the month are added and some older ones drop out—also contributed to Friday's sell-off in US Treasuries, cutting short what was set to be the biggest monthly bond rally of the year. US 10-year yields fell 15 basis points in June, following a drop of 17 basis points in May.

However, despite the volatility in yields, the latest US data remain consistent with an economy headed for a soft landing, with the Federal Reserve's favored inflation gauge—the core personal consumption expenditure (PCE) price index—decelerating further in May. We see evidence that continues to support a start to the Fed's policy easing cycle later this year.

**Inflation has resumed falling.** May's core PCE rose 0.1% month-over-month, down from April's 0.2% and marking the smallest advance this year. The annual pace, at 2.6%, was also the slowest in more than three years and down from the peak of 5.6%. This came after encouraging data for the consumer price index (CPI) for May—released earlier in June—adding to evidence that the trend toward lower inflation, which went into reverse in the first quarter, has resumed. In addition, real consumption growth for the first quarter of 2024 was revised down to an annualized pace of 1.5%, from 2%, and the June quarter appears to be shaping up for a similar growth rate. This more moderate growth in spending is helping to ease inflationary pressure.

**Other data also point to a cooling of economic activity.** While real GDP growth for the first three months of this year was revised up to 1.4% quarter-over-quarter, slightly ahead of the previous estimate of 1.3%, it remains well below the

3.4% growth pace recorded for the fourth quarter. Separately, preliminary durable goods orders posted sluggish 0.1% month-over-month growth in May, pending home sales for the same month contracted amid elevated mortgage rates, while continuing jobless claims rose to the highest level since 2021. Looking ahead, key data releases this week include the labor report for June and the Job Openings and Labor Turnover Survey for May. Softer numbers could add some urgency for the Fed as it considers the timing of rate cuts.

**The Fed will follow the lead of economic data.** Fed officials have maintained their data-dependent stance in their recent remarks, with Richmond Fed President Thomas Barkin saying the inflation battle hasn't been won, and San Francisco Fed President Mary Daly saying it's too early to tell when it will be appropriate to lower borrowing costs. But both policymakers acknowledged the lagged effects of elevated rates, with Daly saying the latest inflation data indicate monetary policy is working. With Fed officials deeming the current rate as restrictive, we maintain the view that incoming data should allow the US central bank to start cutting rates later this year.

So, as markets are likely to price in further rate cuts into 2025 once the Fed moves, we see lower bond yields by year-end, forecasting the 10-year Treasury yield at 3.85%. The combination of lower rates and moderate growth is supportive for diversified fixed income strategies—we favor complementing a core holding in quality bonds with a satellite in higher-yielding parts of the market.

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Original report - [Volatile treasury yields mask evidence of soft landing, 1 July 2024.](#)

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