# FUNDAMENTALLY SPEAKING

A simple explanation of the finance terms we all hear about but don't really understand

# US bond yields still rising thanks to higher cash rate

**ROWAN JONES**

In the last week the yield on 10-year US government bonds surged to their highest level in 15 years, with yields exceeding 4.6 per cent. To give some context, in April this year these bonds were yielding 3.5 per cent and it was only two years ago the yield was a miserly 1.5 per cent.

But what does the bond yield represent and why are they still rising?

The yield of a bond is the income return an investor expects to receive each year. For the issuer of the bond, the yield reflects their annual cost of borrowing. This means today's buyers of US government bonds are in line to receive an income of 4.6 per cent.

As a result it's also become a lot more expensive for governments around the world to fund their debt.

The reason yields have continued their upward march is largely due to the market expecting that official interest rates will remain higher for longer.

This expectation has been guided by the consistent US Federal Reserve commentary that containing inflation was its number one priority.

One of the consequences of higher bond yields is that it increases the return hurdle for all other types of investment. The reason being is that US government bonds are viewed as a "risk-free" rate as they are backed by the US Government and the likelihood of default is pretty much zero.

This means that for an investment to be attractive enough to entice potential investors to risk their capital, it must be offering a return that is well in excess of the risk-free rate of 4.6 per cent.

This rate is one of the reasons we have witnessed weakness in other asset classes, such as ASX-listed property stocks.

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Illustration: Don Lindsay