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US inverted yield curve: Economic recession indicator suggests difficult times ahead

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Abstracts

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SUMMARY

The inverted yield curve is feared by many investors in the world as many claim that is a signal that a recession in the economy will soon take place. On the other hand, many argue that is “false advertisement” as it is only indicating the movements of long-term bond yields against short-term bond yields. However, that as its own is a big indicator of something is happening in the economy. The inverted yield curve and the term spread, the different between long-term interest rates and short-term interest rates have been indicators of slowdowns in the US economy over 60 years now, and in all of the cases except one, they signaled that recession was coming.

KEY HIGHLIGHTS

The yield curve is an indicator of bond investors’ behavior. Meaning that demand for short-term bonds will have a different impact on the yield curve than demand for long-term bonds.

The most important factors are herding and loss aversion effect, which both are a physiological phenomenon which takes place in the human mind and affects in a great extent the decision-making process of an investor.

Individual investors are initiators of the inverted yield curve. Meaning that their behavior and their actions dictate which movement the yield curve will take.

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SCOPE

Examines if the inverted yield curve can signal a recession

REASONS TO BUY

Does the inverted yield curve signals a recession? - What is the negative term spread? - Is the US economy currently under threat?

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Contents

1. OVERVIEW

1.1. Catalyst
1.2. Summary

2. THE US YIELD CURVE AS AN EFFECTIVE RECESSION INDICATOR

2.1. The yield curve displays the difference between older and younger bonds
2.2. The yield curve is an expression of bond investors' behavior

3. REAL LIFE IMPLICATIONS OF AN INVERTED YIELD CURVE

3.1. Pessimistic behavior alongside with herding and fear of missing out effect invert the yield curve
3.2. An inverted yield curve has a big impact on fixed-income investors, consumers and financial institutions

4. HISTORICAL ANALYSIS INDICATES THAT AN INVERTED YIELD CURVES SIGNALS RECESSION

4.1. Negative term spread is the real indicator of a recession
4.2. The US economy is currently under threat

5. APPENDIX

5.1. Abbreviations and acronyms
5.2. Sources
5.3. Further reading

6. ASK THE ANALYST

7. ABOUT MARKETLINE

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List Of Figures

LIST OF FIGURES

Figure 1: Yield curve with an upward trend
Figure 2: Yield curve with an downward trend or inverted yield curve
Figure 3: Herding effect in the stock market
Figure 4: The term spread and recessions

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