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The Day Ahead: 2 Ways to Look at Bonds "Best Rally" of 2018

You may have noticed that, as of February 22nd, bonds haven't been experiencing the same sort of pain that characterized the first month and a half of 2018. We've been discussing the ensuing weeks as a sort of sideways consolidation, but could it grow into **something more**?

There are **two ways to answer** that question. Actually, there are more than 2 ways, but only 2 that we'll examine today. The first is to look at more exotic technical indicators (relative to simple trend-lines and pivot points, anyway. There are certainly far more exotic studies than these). The chart below has what you might call the more mainstream exotic technical indicators: Bollinger Bands (a 21-day exponential moving average with 2 standard deviations on either side) and the fast/slow stochastics, a momentum indicator.



MBS & Treasury Market Data

| | Price / Yield | Change |
|----------------|---------------|---------|
| MBS UMBS 5.0 | 99.37 | +0.02 |
| MBS GNMA 5.0 | 99.93 | +0.02 |
| 10 YR Treasury | 3.9068 | +0.0029 |
| 30 YR Treasury | 4.1960 | +0.0028 |

Pricing as of: 9/1 7:34PM EST



Average Mortgage Rates

| | Rate | Change | Points |
|--------------------------------|-------|--------|--------|
| Mortgage News Daily | | | |
| 30 Yr. Fixed | 6.43% | +0.02 | 0.00 |
| 15 Yr. Fixed | 5.95% | 0.00 | 0.00 |
| 30 Yr. FHA | 5.82% | +0.02 | 0.00 |
| 30 Yr. Jumbo | 6.62% | 0.00 | 0.00 |
| 5/1 ARM | 6.28% | -0.01 | 0.00 |
| Freddie Mac | | | |
| 30 Yr. Fixed | 6.35% | -0.51 | 0.00 |
| 15 Yr. Fixed | 5.51% | -0.65 | 0.00 |
| Mortgage Bankers Assoc. | | | |
| 30 Yr. Fixed | 6.44% | -0.06 | 0.54 |
| 15 Yr. Fixed | 5.88% | -0.16 | 0.68 |
| 30 Yr. FHA | 6.36% | -0.06 | 0.85 |

As the chart suggests, if we manage to simply stay somewhat flat today, it'll be the **first time in 2018** that yields have closed for 2 straight days below the middle bollinger band. It would also potentially confirm a move below the mid-point of the longer-term stochastic. While both of those are technically positive developments, they both have "yeah buts."

| | Rate | Change | Points |
|--------------|-------|--------|--------|
| 30 Yr. Jumbo | 6.75% | +0.07 | 0.39 |
| 5/1 ARM | 5.98% | -0.27 | 0.65 |

Rates as of: 8/30

The biggest objection anyone could raise to relying on these more exotic techs in the current environment is that such behavior is to be expected any time bonds move sideways after having moved sharply higher in the previous month or two. In other words, these patterns are the typical **byproducts** of consolidation following a sell-off. They tell us more about what's happened in the past and less about what might happen in the future. If we were to look at past examples of similar behavior to try to get a read on the future, we'd see a wide variety of suggestions. Sometimes rates continue to fall and sometimes they move back up.

We can **simplify** our assessment by looking strictly at trend lines and pivot points. These are just straight lines that mark levels where bonds have been more likely to bounce in the past. As we've discussed on several recent occasions, 2.795% is an important floor, and one that 10yr yields haven't been eager to break below (apart from the single attempt on the day of the massive stock market sell-off).

If yields manage to make it below 2.795, there's an **even bigger challenge** waiting in the mid 2.6% range. That's essentially the gateway back into the post-election trading range (before the 2018 sell-off).



The bottom section of the chart introduces a few ascending trend lines. These essentially mark the push back from the lows seen in mid-2012. **There's only been one** confirmed break higher out of these lines and one confirmed break lower. And while yields are technically slightly higher at the moment, it's not what I'd consider a "confirmed" break at the moment. It's more in line with what we saw in the middle of 2015. With this in mind, if yields are able to move back inside the ascending yellow lines, it could foreshadow more improvement--short-term gains inside a broader trend of losses.

The first order of business, in any event, would be to break below 2.795. With overnight lows of 2.797% and some weakness since then, that's **far from a done deal**.

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