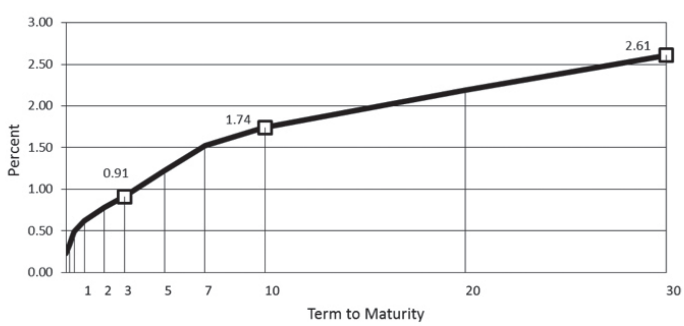
# 2016 Investment Symposium: Sentimentally Speaking

**By Frank Grossman**

Every year at our symposium, there is much discussion during the sessions and in the corridors regarding the outlook for bond markets. So this time around, when the 2016 Investment Symposium convened in New York City on March 14–15, the organizing committee decided to conduct a brief sentiment survey gauging how attendees thought rates might stand in a year's time.

Treasury yields at the end of February were 0.91 percent for the three-year note, 1.74 percent for the 10-year note, and 2.61 percent for the 30-year bond (refer to graph below). These key rates moved up during the two weeks prior to the symposium, but since the meeting they have declined by more than 30 basis points due to concerns about weak U.S. job and gross domestic product (GDP) growth, and more latterly the U.K. Brexit referendum on June 23.

US Treasury Yields (Feb. 29, 2016)




Part A of the survey asked attendees the following question specifically targeting yields for the three- and 10-year notes (QA1 and QA2, respectively), and the 30-year bond (QA3):

> "From your personal perspective, what's the outlook for the U.S. Treasury rates on Feb. 28, 2017 (i.e., in one year's time) as compared to their levels at Feb. 29, 2016?"

Table A: 2016 Investment Symposium Sentiment Survey—Part A Results

| | | QA1 | QA2 | QA3 | # | % | # | % |
|---|---|---|---|---|---|---|---|---|
| Shift Up | | a | a | a | 7 | 11.7 | 7 | 11.7 |
| Tilt Steeper | Long-Term Up I | b | b | a | 2 | 3.3 | 5 | 8.3 |
| | Long-Term Up II | b | a | a | 2 | 3.3 | | |
| | Short-Term Down II | c | c | b | 1 | 1.7 | | |
| No Change | | b | b | b | 17 | 28.3 | 17 | 28.3 |
| Twist Flatter | | a | b | c | 3 | 5.0 | 3 | 5.0 |
| Tilt Flatter | Long-Term Down I | b | b | c | 1 | 1.7 | 19 | 31.7 |
| | Long-Term Down II | b | c | c | 4 | 6.7 | | |
| | Short-Term Up II | a | a | b | 5 | 8.3 | | |
| | Short-Term Up I | a | b | b | 9 | 15.0 | | |
| Shift Down | | c | c | c | 7 | 11.7 | 7 | 11.7 |
| Other | | b | a | b | 1 | 1.7 | 1 | 1.7 |
| No Opinion | | d | d | d | 1 | 1.7 | 1 | 1.7 |
| Total | | | | | 60 | 100.0 | 60 | 100.0 |

Four response options were provided for each key rate:

a. Higher (25 or more basis points higher);
b. Roughly unchanged (within +/- 25 basis points);
c. Lower (25 or more basis points lower); and
d. No opinion.

Sixty surveys were completed, and their yield curve outlook is summarized in Table A. Focusing solely on the 30-year yield responses (QA3), there was a modest downward sentiment overall: 19 percent, or 11 of 59 respondents with an opinion, anticipated a higher rate; 25 percent, or 15 respondents, foresaw a lower rate; while a 56 percent majority, or 33 respondents, felt the long rate would remain roughly unchanged. Possibly an interesting result, however, examining responses for all three key rates together has the potential to reveal more about where respondents think rates are going.

Twenty-eight percent of respondents anticipated roughly no change in three key rates year over year. Those 12 percent who saw an upward shift were balanced by an equal number expecting generally lower rates across the entire yield curve—demonstrating that some actuaries certainly felt that rates could indeed decline further with even more valuation pain possible. A flattening of the term structure was indicated by nearly 37 percent of respondents, with either a tilt down in long-term rates, or a tilt up in short-term rates, or a combination of both via a twist.

Given the importance of long-term rates for many actuaries, including duration-matching risk managers, we also thought it worth asking about the attractiveness of ultra-long bonds. Part B of the survey posed a follow-on question about the potential appeal of 50-year sovereign debt:

> "From the perspective of your (current or recent) organization and/or clients, and bearing in mind their strategic investment and/or risk management objectives, would they be interested in purchasing ultra-long (i.e., 50-year credit risk free) sovereign bonds:
>
> 1. If the ultra-long sovereign bonds had **liquidity** similar to 30-year sovereign bonds?
> 2. If the ultra-long sovereign bonds had **liquidity and yield** similar to 30-year sovereign bonds?"

The second question referred to a 50-year bond that traded flat to a 30-year issuance, providing an opportunity to lock in current yields (thereby avoiding reinvestment risk should future rates continue southward) or better offset long-term liability cash flows. This time three response options were provided for each question—a) Yes; b) No; and c) No opinion—and the responses are set out in Table B.

Table B: 2016 Investment Symposium Sentiment Survey—Part B Results

| | QB1 | QB2 | # | % |
|---|---|---|---|---|
| Liquidity & Yield | a | a | 27 | 45.0 |
| Liquidity But Not Yield | a | b | 6 | 10.0 |
| Neither Liquidity or Yield | b | b | 6 | 10.0 |
| Other 1 | a | c | 1 | 1.7 |
| Other 2 | b | c | 1 | 1.7 |
| Other 3 | b | a | 3 | 5.0 |
| Other 4 | c | a | 3 | 5.0 |
| No Opinion | c | c | 13 | 21.7 |
| Total | | | 60 | 100.0 |

Forty-five percent of respondents, and a majority of those with an opinion, indicated an interest in a 50-year sovereign bond with similar liquidity and yield to a 30-year bond. Maybe someone should write a letter to the U.S. Treasury Secretary Jack Lew to let him know? Ten percent said they would take the longer term and liquidity but not the 30-year yield, possibly hoping for better days ahead. One respondent actually wrote, "Yes, please!" beside his/her response to the first Part B question.

Our presumption was that a "Yes" response to the second liquidity and yield question (QB2) would imply a similar "Yes" to the first liquidity question (QB1), and that the converse would hold as well (i.e., not being interested in liquid ultra-long bonds also meant not being interested in a liquid ultra-long bond at any yield including 30-year risk-free rates). But some of our respondents didn't see it that way, prompting us to wonder whether the questions as posed were crystalline for all. Perhaps some symposium attendees had something else in mind?

At this juncture, one might well ask whether the sentiment survey constitutes an auspicious augury of future rates, particularly as the survey was conducted on March 15? But there's never a reliable soothsayer around when you really need one, so we'll simply have to wait and see.

Frank Grossman, FSA, FCIA, MAAA, is an independent actuary based in Toronto, and may be reached at Craigmore54@hotmail.ca.