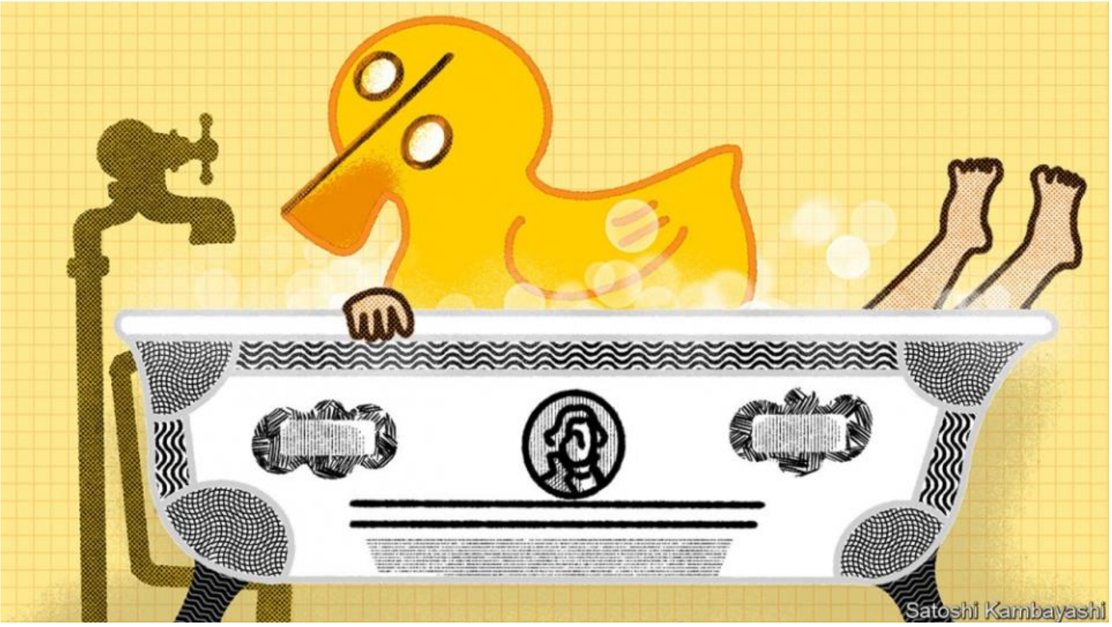
The long-term decline in bond yields enters a new phase

What will happen when interest rates eventually start to rise again?



At the end of 1989, an American in London received a call from a friend back home. The caller had watched the fall of the Berlin Wall and the toppling of Nicolae Ceausescu in Romania with growing dismay. He was at the end of a four-year course in Russian Studies at an elite university with hefty tuition fees. He had learned all the Kremlinology a would-be cold warrior could need—but not that the cold war might suddenly end. “I just took a $60,000 bath,” he said.

This story comes to mind not so much because of fears of a new cold war, this time with China, but because of the bond market's recent response to such fears. Long-term interest rates have tumbled almost as swiftly as communism fell in Europe. The yield on a ten-year Treasury bond has plunged from 2.5% to 2.1% in the past month. Ten-year Bund yields have turned negative again and have reached a new all-time low.