

Yield Spread

Yield spread is the difference in yield between two different bonds (usually with different ratings and therefore of different credit quality). In times of uncertainty, the yield spread widens as investors require extra return for investing in lower grade bonds and for taking on extra risk.

One popular yield spread is the spread between the 10-Year U.S. T-Bond and the Federal Funds rate. The Federal Funds rate is controlled by the U.S. Federal Reserve. When the Federal Funds rate is low (relative to the T-Bond rate), the Fed is seen as being supportive of the economy. The Fed is trying to stimulate the economy. When the Federal Funds rate is high (relative to the T-Bond rate), the Fed is trying to cool the economy off. A high Federal Funds rate is considered bearish.