The End of Cheap Duration

The structural repricing of rates, duration and fixed income.

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Introduction

The bond market has moved well beyond the conditions that characterized the pre-Covid era. After years of historically low Treasury yields and exceptionally cheap duration, the market experienced a pronounced repricing of fixed income. The scale and persistence of this adjustment raise a broader question about the regime in which bonds are now being priced.

This report examines that transition through the U.S. 10-Year Treasury, the benchmark at the centre of global fixed income markets, and its transmission across major bond ETFs. The analysis moves from the evolution of the Treasury market to the behaviour of different fixed-income exposures, before bringing the evidence together to assess the broader implications of the new environment.

Key takeaways

- **A structural rate regime shift has taken place.** The post-Covid inflation shock and subsequent monetary tightening ended the era of historically compressed Treasury yields and triggered a broad repricing of duration.
- **Duration was the main transmission mechanism.** The repricing of yields translated into substantial losses across major bond ETFs, with longer-duration exposure experiencing deeper price declines.
- **Credit risk amplified the adjustment.** The larger decline in corporate bonds relative to sovereign exposure highlights the additional impact of widening credit premia alongside duration risk.
- **The new regime extends beyond monetary policy.** Persistent fiscal deficits and rising debt introduce an additional source of term-premium pressure, making the debasement trade a relevant lens for understanding long-duration Treasury pricing.

1. The U.S. 10-Year Treasury Yield: A Structural Regime Shift

Figure 1: U.S. 10-Year Treasury Yield, monthly candlesticks from 2002 to present. The chart shows the post-Covid repricing from historic lows to a structurally higher-rate regime.



Source: TradingView.

The U.S. 10-Year Treasury Yield chart points to a clear regime shift in interest rates relative to the pre-Covid era. Having spent years anchored near historic lows, Treasury yields underwent a sharp repricing that pushed the 10-year rate to substantially higher levels. Rather than reverting, the market appears to have entered a new higher-rate regime.

(i) Inflation

Persistent inflationary pressures were a key driver of the post-pandemic repricing of U.S. rates. Although inflation subsequently moderated and the Fed began cutting rates, the 10Y remained elevated. This happened because 10Y rates reflect both expectations of future short-term rates and the term premium required by investors to hold long-duration Treasuries.

(ii) Growth and labor market

The U.S. economy has remained resilient despite this restrictive stance, with GDP growth and a labor market avoiding the sharp deterioration many had expected. This resilience has reduced expectations of a rapid return to the low-growth, low-rate environment that characterized the pre-Covid period.

(iii) Fiscal policy

The other structural driver is the fiscal drift of the U.S. government. The federal deficit has remained near 6% of GDP even outside recession, while gross federal debt has climbed above 120% of GDP. As a consequence, persistent deficits and rising debt can increase the compensation required to hold long-term Treasuries, contributing to higher long-term yields and a higher term premium.

(iv) Term premium

The 10Y reflects both expectations of future interest rates and the term premium required to hold long-duration Treasuries. Growth resilience has supported expectations of higher long-run rates, while persistent fiscal deficits and greater uncertainty have increased the compensation investors demand for duration, helping explain why the 10Y remains elevated.

As the deepest and most liquid bond market in the world, the 10-Year Treasury serves as the benchmark for the cost of capital across the entire financial system. Its yield anchors the pricing of mortgages, corporate bonds and equity valuation models, meaning this structural repricing has propagated well beyond government debt. Any shift in its level therefore carries direct implications for the cost of financing throughout the real economy.

2. The Transmission to Bond ETFs: Duration and Credit Risk

Figure 2: Performance of major bond ETFs (BND, BNDX, LQD) over the last five years, weekly data. The systematic decline in bond prices reflects the repricing of duration and credit risk.



Source: TradingView.

ETF	Exposure	Avg Duration	5Y Loss
Vanguard Total Bond Market (BND)	Broad U.S. investment-grade bonds	5.7 years	-17.81%
Vanguard Total International Bond (BNDX)	Broad international investment-grade bonds ex-US	6.5 years	-17.85%
iShares iBoxx $ Investment Grade Corporate (LQD)	USD-denominated corporate bonds	7.71 years	-23.50%

Sources: Vanguard, iShares.

The three ETFs provide a cross-section of fixed-income exposures, allowing us to assess how the repricing of interest rates translated into different segments of the bond market. BND and BNDX offer broad investment-grade bond exposure with relatively similar duration, while LQD combines longer duration with additional exposure to corporate credit risk.

The impact of duration is clear: longer-duration bonds are more sensitive to changes in interest rates and therefore experience larger price declines when yields rise. This relationship is visible in the different performance of the ETFs, with LQD recording the deepest decline alongside the highest duration.

The underperformance of LQD also reflects the additional role of credit risk. Unlike broad bond exposures, corporate bonds are affected not only by movements in government yields but also by changes in credit spreads. During the 2022 tightening cycle, the widening of corporate spreads increased the pressure on investment-grade corporate bonds, amplifying the losses generated by the rise in Treasury yields.

The combination of higher duration and credit-spread exposure therefore provides a useful explanation for the larger decline recorded by LQD. The episode illustrates how a single macroeconomic shock can propagate through different channels of fixed income, with duration acting as the primary transmission mechanism and credit risk further amplifying the adjustment.

3. Final Overview and Portfolio Implications

In order to fully understand the current bond market, we must go through the transition from the old to the new regime. This shift began in 2020 with the Covid shock. The pandemic triggered an immediate and severe liquidity crisis across the financial markets. With the intention of stabilizing the system, the Fed intervened with aggressive Quantitative Easing, a massive bond-buying program designed to inject liquidity into the market and drive down interest rates.

This intervention caused an extreme compression of Treasury yields. Rates remained anchored near historic lows for years, creating an environment of unusually cheap capital. As a result, bond prices reached unprecedented highs. However, these distorted market conditions paved the way for a severe structural shift in the interest rate regime.

The transformation of the fixed income market created an inevitable sequence of events, a disastrous domino effect. The primary result was a sudden inflation shock. Persistent price pressures forced central banks to abandon their accommodative policies. They quickly shifted direction to a rapid and aggressive monetary tightening policy. This sudden shift pushed Treasury yields to substantially higher levels.

Higher duration means deeper decline when interest rates rise. For this reason, the market experienced a violent duration repricing. Consequently, major bond ETFs recorded a systematic price decline. This chain of events ultimately weakened the traditional role of bonds. They failed to act as a reliable portfolio protection tool when investors needed it most.

Beyond inflation, a new structural factor emerged to redefine the bond landscape: the debasement trade. The U.S. government is currently facing a severe fiscal drift. The federal deficit remains anchored near 6% of GDP, even without an active economic recession. Meanwhile, gross federal debt has climbed above 120% of GDP.

Persistent deficits and constantly rising debt fuel strong investor concerns about long-term fiscal sustainability. They also raise questions about the real, long-term value of the currency. In response to these growing fears, investors naturally seek protection from debasement. They now demand greater compensation, often reflected in a higher term premium, to hold long-term Treasuries.

This fiscal phenomenon is not the only explanation for current 10Y levels. Instead, it serves as a new interpretive key that enriches our reading of the current bond regime. The U.S. 10-Year Treasury acts as the ultimate benchmark for the global financial system. Therefore, this structural repricing has propagated well beyond government debt. It has fundamentally transformed the overall cost of capital for the entire real economy.

Portfolio implications

The transition to a structurally higher-rate environment changes the role of duration within multi-asset portfolios. Fixed income can no longer be viewed purely through its income potential or as an automatic source of portfolio protection: the sensitivity of long-duration assets to rate repricing makes duration management increasingly relevant, particularly when inflation, fiscal risk and term premia can move independently of the short-term policy path.

From a portfolio perspective, the key implication is therefore not simply to reduce or increase bond exposure, but to distinguish duration, credit and macro-regime risk within fixed income allocation. The 10-Year Treasury remains the central reference point because changes in its yield propagate across bonds and other asset classes, making the management of rate sensitivity increasingly important for overall portfolio construction.

Bottom line. The end of cheap duration marks a broader change in portfolio construction: rate exposure, rather than simply bond exposure, has become a central source of risk across multi-asset portfolios.

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