ABOVE THE FRAY

Are Higher Rates Cause to Add More Fixed Income?

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Bond yields have been higher in the last few years than at any time since the Global Financial Crisis.[1] This makes for a good opportunity set in fixed income. But some investors are asking if we've reached the point where expected bond returns are so high that it makes sense to trade off some equity exposure for more weight in fixed income.

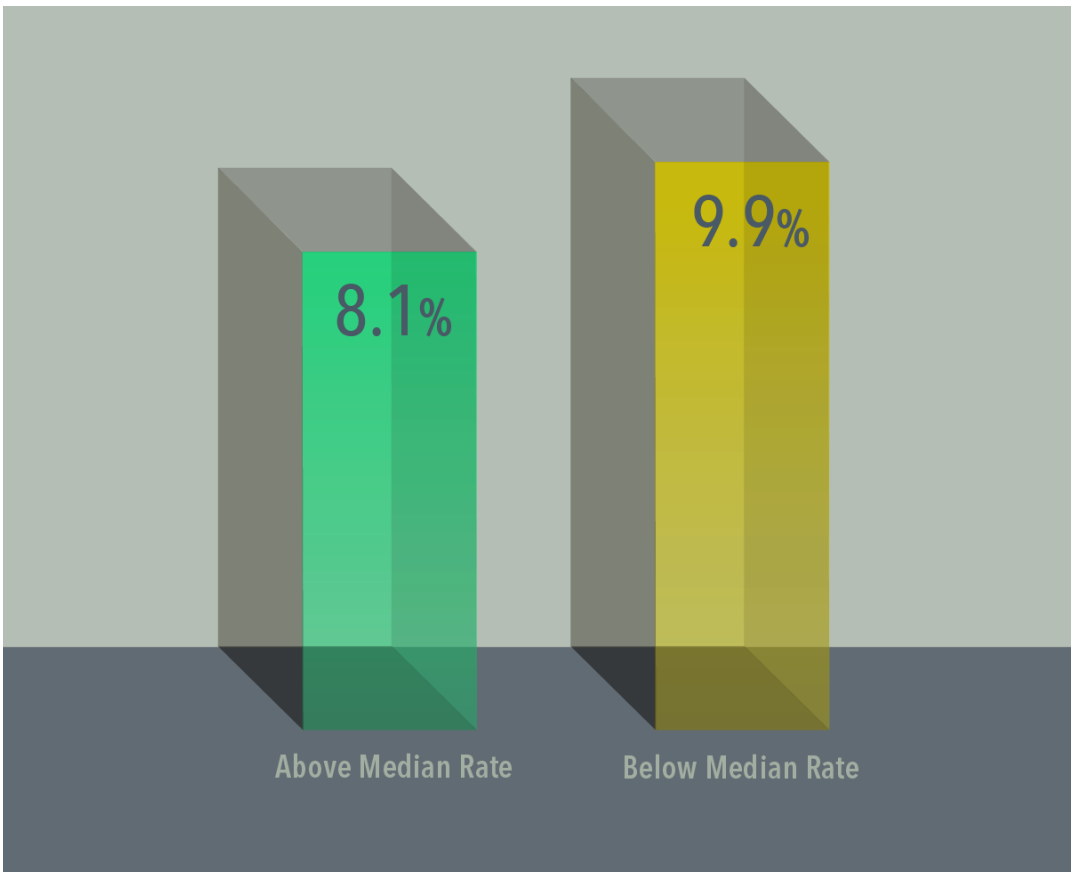
One thing to keep in mind is that discount rates for stocks factor in current interest rates. All else equal, higher bond yields should lead to higher expected stock returns. In other words, the premium for stocks over bonds may not shrink just because of higher rates.

It makes sense then, that the US equity premium has historically been unrelated to the level of interest rates. In years when the One-Month US Treasury Bill rate was below its historical median, the average equity premium was about 9.9%. In above-median rate years, it was 8.1%. However, the difference between these averages is not statistically reliable,[2] meaning there's not enough evidence to support the premise that the premium is higher in one environment than the other.

Given that the evidence suggests the excess returns for stocks over bills are similar regardless of interest rate level, investors should be cautious changing up their stock/bond mix based on current yields.

Please see the end of this document for important disclosures.

Exhibit 1
Average Annual Equity Premium Conditional on One-Month Treasury Bill Rates at Start of Year 1927–2025



Past performance is not a guarantee of future results.

Equity premium is the return of the S&P 500 Index in excess of US Treasury bills. S&P data © 2026 S&P Dow Jones Indices LLC, a division of S&P Global. One-month Treasury Bill returns from ***Ken French data library****.*

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The Future Is Unknown, So Plan Accordingly

1. Based on market yield on US Treasury securities at 10-year constant maturity. Courtesy of Federal Reserve Bank of St. Louis.
2. The precision around the difference in these averages, measured using a t-test, is below the threshold required to distinguish from noise.

Discount rate: A financial metric used to determine the present value of future cash flows.

Equity premium: The return difference between stocks and a risk-free asset, such as short-term Treasury bills.

Premium: A return difference between two assets or portfolios.

Yield: The return on a bond investment. Price and yield are inversely related, and as the price of a bond goes up, its yield goes down.

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