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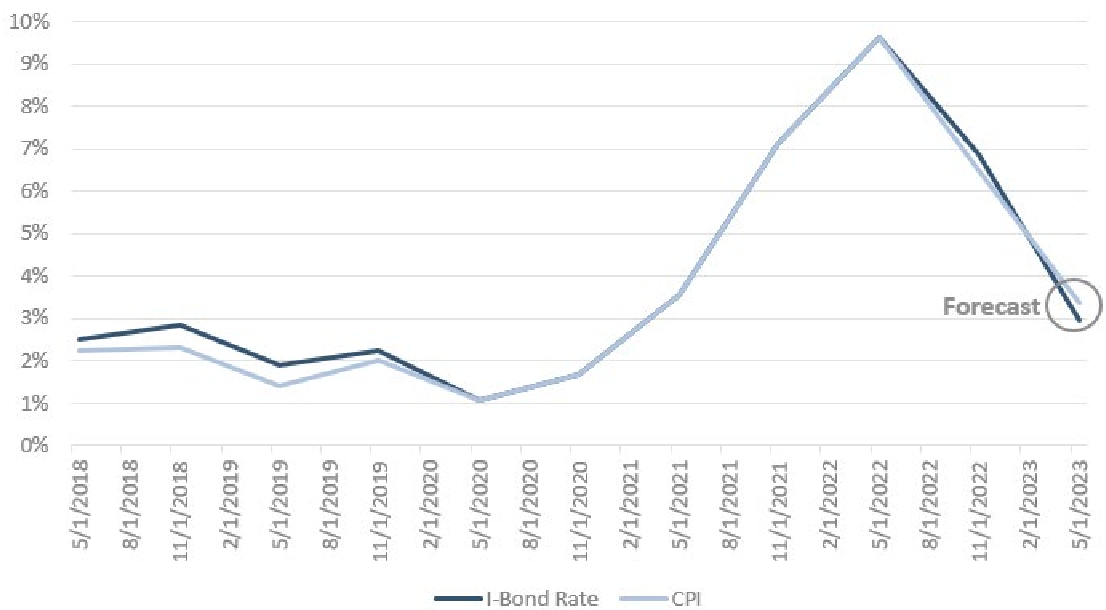
MARKET COMMENTARY

Fig. 1: I-Bond Rate Expected to Fall Below 4% in May



Source: TreasuryDirect.gov, Mill Creek.

I-bonds (a type of US savings bond designed to protect against inflation) became a hot commodity in 2022. **As we've noted**, TreasuryDirect's website crashed in October due to a surge of investors eager to lock in an eye-popping risk-free rate of 9.6%. However, with yields expected to reset from the current 6.9% to below 4% next month (Fig. 1), we have likely already seen the peak in demand.
I-bonds have a few quirky features - individuals are restricted to purchasing a maximum amount of $10,000, there is a penalty for selling bonds in less than five years, and, perhaps most importantly, the interest rate resets twice a year. Specifically, an I-bond's coupon is the sum of two components: a fixed rate and an inflation rate. The Treasury arbitrarily sets the fixed rate which is currently 0.4%. The inflation rate is based on CPI (includes food and energy) and resets every May 1 and November 1.

Therefore, the decision to invest in I-bonds depends primarily on your view of inflation moving forward. For example, assuming a five-year hold, inflation must trend above 3% for today's I-bond to earn more than a 5-year Treasury Note (3.6%). The breakeven inflation rate on a 5-year TIPS is 2.4%, which implies that purchasing an I-bond today is making an active bet against market expectations. In summary, I-bonds are a useful tool for managing inflation risk within fixed income portfolios, but we believe (and hope) the highs of 2022 are behind us.

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