The Yield Curve

Desjardins
Economic Studies
www.desjardins.com/economics

August 31, 2009

The stock market is climbing, but demand for Treasuries stays strong. Odd? Not really!

Highlights

- The market is wrong to count on looming rate hikes from the Federal Reserve (Fed). The Fed's habit is to wait for more than a year after the jobless rate crests to initiate a monetary firming cycle.
- Our theoretical model for U.S. bonds suggests that rates, at close to 3.50%, are currently in line with the fundamental variables. We therefore expect rates on 10-year T-notes to stay within a range of 3.25% to 4.00% until the end of the year, potentially testing the lower bound along the way.
- It is too early to bank on the yield curve flattening substantially. Usually, the spread between U.S. 10- and 2-year rates only begins to drop substantially once the jobless rate has peaked.
- With less strain associated with deficit financing in Canada, this could be enough to trap Canadian government rates in a tighter range, i.e. between 3.20% and 3.60%, until the end of 2009.

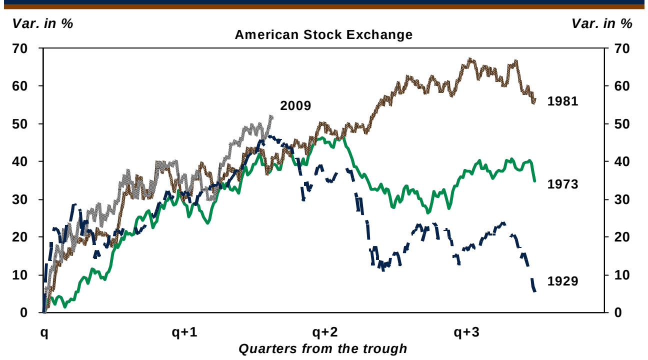
Contents

Summary 1
Monetary Policy
Federal Reserve 6
Bank of Canada 7
European Central Bank 8
Bank of England 9
Bank of Japan 10
Tables 11-12

Summary

Investor sentiment was tested a number of times this summer, with good and bad news coming at such a pace that it was hard to keep up. The economic and financial situation has clearly improved, but, overall, the situation is still compatible with low interest rates. Although the stock markets have been delivering outstanding performance since March's low, the rally seems overlong, historically (graph 1), and the feeling that a correction is due is omnipresent. As a result, investors are showing some caution. The signs of recovery are unequivocal, but many adjustments and challenges still face the major economies, and the consensus is increasingly calling for modest, suboptimal growth.

Graph 1 – What will next months look like for the stock market?



Sources: Datastream and Desjardins, Economic Studies

Under these circumstances, demand for high-quality bonds will continue, helping easily mop up the abundant supply of Treasuries needed to finance the U.S. deficit.[1] In August, the

[1] The Congressional Budget Office (CBO) has just lowered its short-term projection for the budget deficit, from US$1,667B to US$1,587B, and increased its forecast for the long-term deficit (2010-2019), from US$4,441B to US$7,137B.

François Dupuis
Vice-President and Chief Economist

Yves St-Maurice
Director and Deputy Chief Economist

Mathieu D'Anjou
Senior Economist

Francis Généreux
Senior Economist

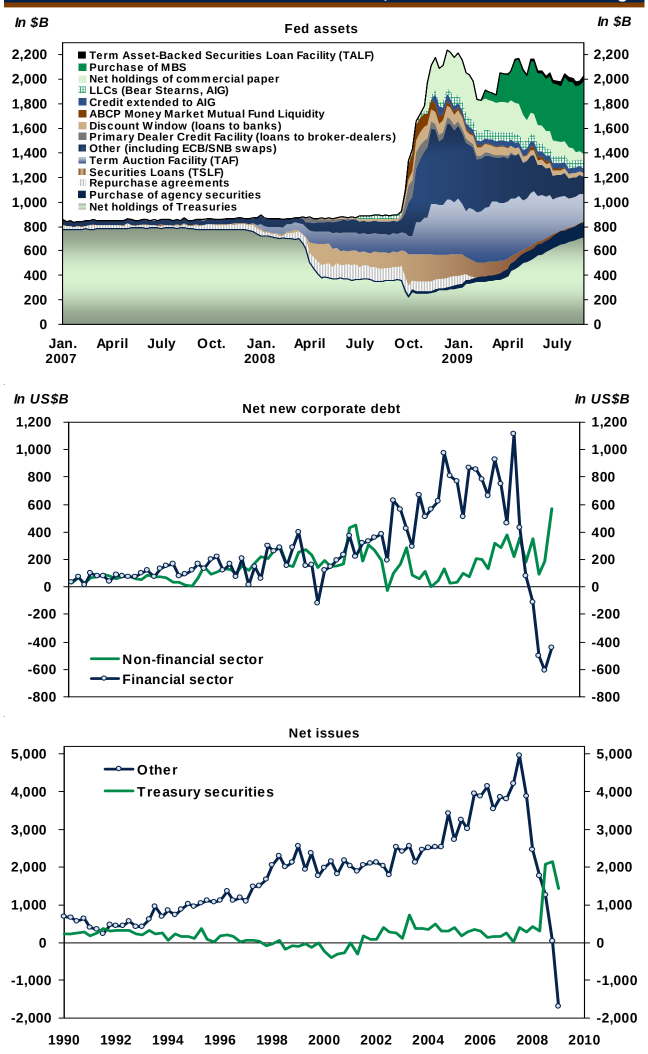
Martin Lefebvre
Senior Economist

Hendrix Vachon
Economist

514-281-2336 *or* 1 866 866-7000, ext. 2336
E-mail: desjardins.economics@desjardins.com

Federal Reserve (Fed) stated that it wanted to gradually wind down its Treasury purchases until the program concludes at the end of October. However, this did not keep the US$75B in securities offered to the market that same week from quickly finding takers. One reason may be that the Fed is still being very active with its MBS and agency security purchase programs, which diminishes the total pool of new issues (graph 2). The sharp drop in credit spreads has allowed non-financial firms to reissue corporate bonds, but the largest segment, banks, is still inactive. Investors looking for quality securities are therefore encouraged to fall back on Treasuries. The proof is in the pudding: a record US$109B issued by the Treasury this week at lower rates was absorbed.

Graph 2 – Federal Reserve's balance sheet: some measures aren't utilized as much, while others are climbing

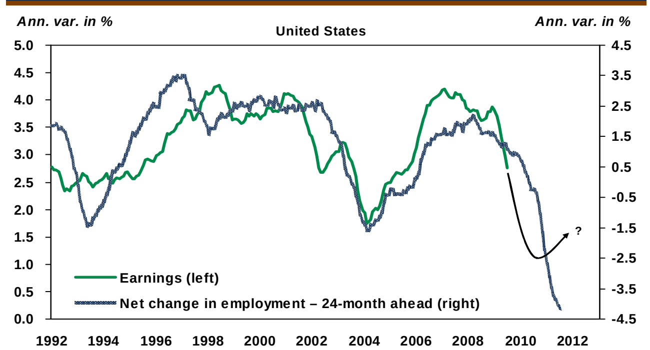


Sources: Federal Reserve Board, Federal Reserve and Desjardins, Economic Studies

NO INFLATION IN VIEW… FOR A LONG TIME

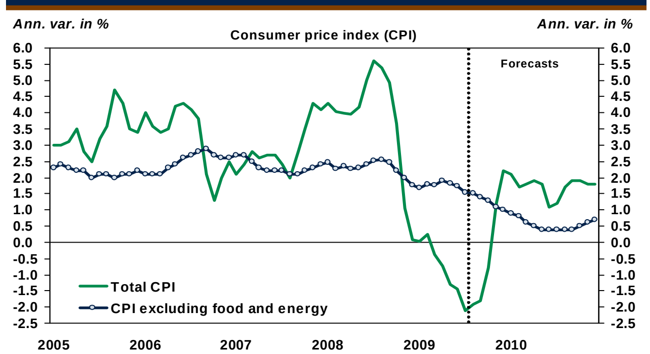
The crux of the story remains "deflation vs. inflation." On this point, we are maintaining our stance: in the near term, the risks of ex-energy disinflation are greater than the risks of inflation. Whether in terms of demand (consumption) or supply (inputs and wages), there is almost no inflation pressure underlying the American economy. For one thing, the severe recession has driven the output gap to a low not seen since 1982, a situation that will take several years to resolve. For another, the employment market's deterioration means that wage growth is increasingly soft and will probably remain so for the next two years (graph 3). Therefore, although deflation by the total consumer price index (CPI) will clearly turn around quickly due to the recent increases in oil prices, ex-energy disinflation will remain a substantial concern for Fed leaders (graph 4).

Graph 3 – Income growth should slow further



Sources: Datastream and Desjardins, Economic Studies

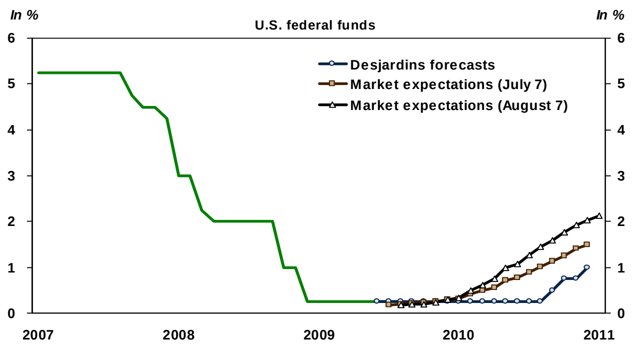
Graph 4 – Ex-energy disinflation will continue in the United States



Sources: Bureau of Labor Statistics and Desjardins, Economic Studies

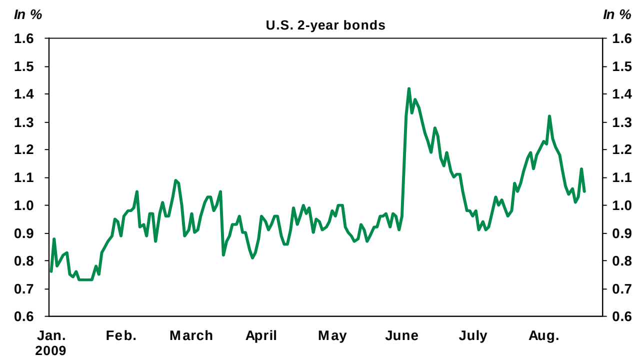
As a result, the market is wrong to count on looming rate hikes from the Fed. Since July's employment report, the market has started pricing in increases for the end of the year (graph 5 on page 3), but the Fed's habit is to wait for more than a year after the jobless rate crests to initiate a monetary firming cycle (graph 6 on page 3).

Graph 5 – Markets are expecting early monetary tightening



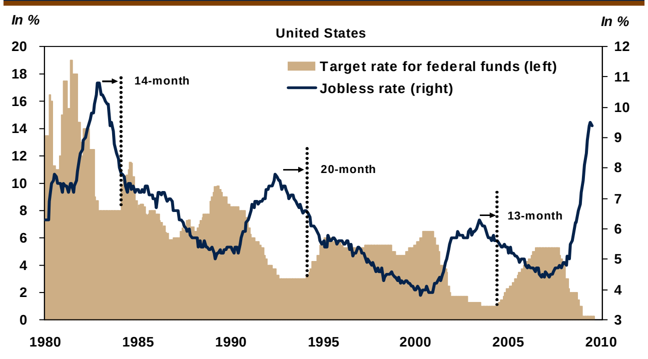
Sources: Bloomberg and Desjardins, Economic Studies

Graph 7 – The short-end of the curve is very volatile



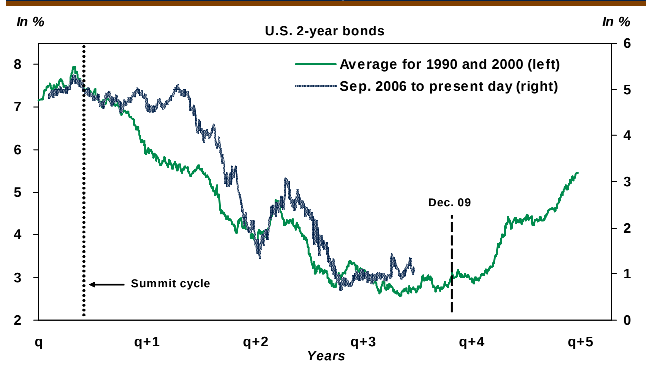
Sources: Datastream and Desjardins, Economic Studies

Graph 6 – The Federal Reserve hikes interest rates only where the unemployment rate recovers significantly



Sources: Bureau of Labor Statistics, Datastream and Desjardins, Economic Studies

Graph 8 – ...but rates should remain low until the beginning of next year



Sources: Datastream and Desjardins, Economic Studies

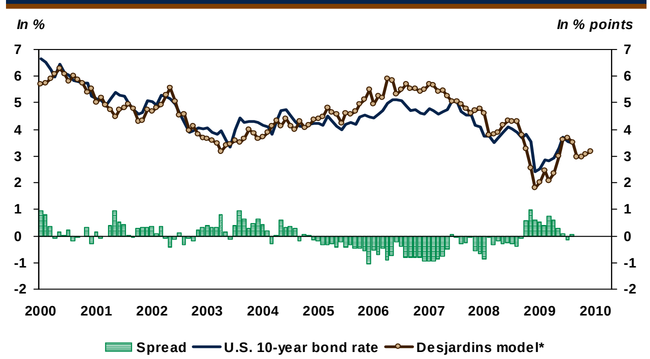
For many, it is the abnormally low federal funds rate that could prod the Fed to start normalizing interest rates more quickly than forecast. We should remember just two things. The first is that excess production capacity in combination with the current disinflation means that an extraordinary level of easing is still needed. The second is that premature firming could plunge the global economy back into enormous difficulties.

TOO EARLY TO EXPECT THE SLOPE TO FLATTEN EXTENSIVELY

With the Fed disinclined to take its foot off the monetary accelerator too soon, we recommend buying two-year bonds on weakness. Rates have been very volatile, particularly following employment figures; fluctuating between 1.00% and 1.40% over the summer, they have provided good yield opportunities (graph 7). As in the 1990 and 2001 cycles, markets tend to prematurely price in rate increases. This situation does not seem to be very different, historically, suggesting that the two-year rates should be confined in a stable range for several more months (graph 8).

The economic recovery could drive real rates on longer-term bonds a little higher, but this should be offset by the nominal portion of the rates, as inflation will be subdued and inflation expectations will remain well anchored. Here, our theoretical model for U.S. bonds suggests that rates, at close to 3.50%, are currently in line with the fundamental variables (graph 9).

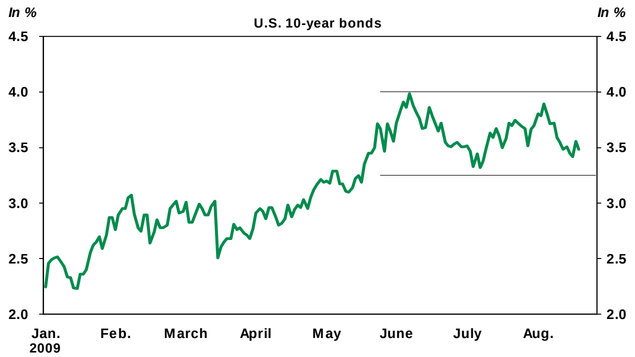
Graph 9 – The situation is compatible with low interest rates in the United States



* Based on expected growth and inflation and the debt burden of the United States.
Source: Desjardins, Economic Studies

We therefore expect rates on 10-year T-notes to stay within a range of 3.25% to 4.00% until the end of the year, potentially testing the lower bound along the way (graph 10).

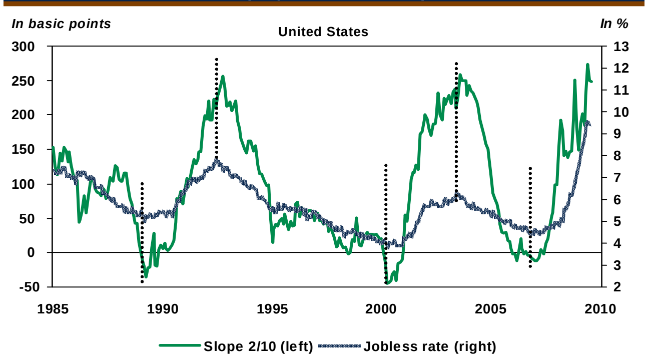
Graph 10 – U.S. rates should continue to evolve in a tight range



Sources: Datastream and Desjardins, Economic Studies

Under these circumstances, it is too early to bank on the yield curve flattening substantially. Usually, the spread between U.S. 10- and 2-year rates only begins to drop substantially once the jobless rate has peaked (graph 11). Employment results have started to reflect slower deterioration in the job market in July. However, the situation remains fragile and the jobless rate is expected to continue to head for 10% until the beginning of 2010.

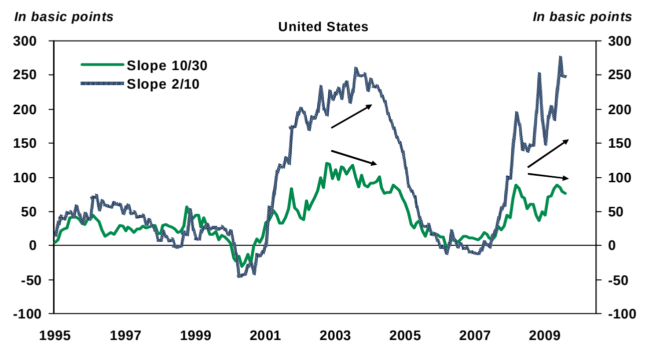
Graph 11 – The curve usually flattens shortly after the unemployment rate has peaked



Sources: Bureau of Labor Statistics, Datastream and Desjardins, Economic Studies

It would be better to initially anticipate flattening by the long end of the yield curve (graph 12). Whether the bond market is going up or down, at current levels, the spread between 30- and 10-year rates in the United States is consistent with flattening. In the event of economic recovery, the 10-year rates will likely slowly ascend toward the 30-year rates. If the market is not anticipating any inflation, demand for long-term securities from pension fund and insurance company managers will put downside pressure on the rates for 30-year maturities.

Graph 12 – The long end of the curve will flatten before the short end

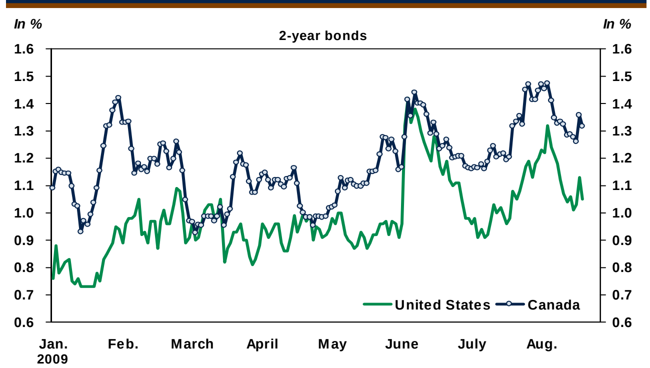


Sources: Bureau of Labor Statistics, Datastream and Desjardins, Economic Studies

THE CANADIAN MARKET IN A GOOD POSITION

In Canada, although the bond market's movement is essentially influenced by movements in the U.S. market, the short end of the Canadian curve has been more volatile since this year began. However, they have shown a smaller range in the last few months, with two-year rates fluctuating between 1.15% and 1.50% this summer (graph 13). However, we still think this is excessive volatility due to the Bank of Canada (BoC) commitment to keep the key rate at 0.25% until mid-2010.

Graph 13 – Volatility has fallen a bit, but it remains elevated

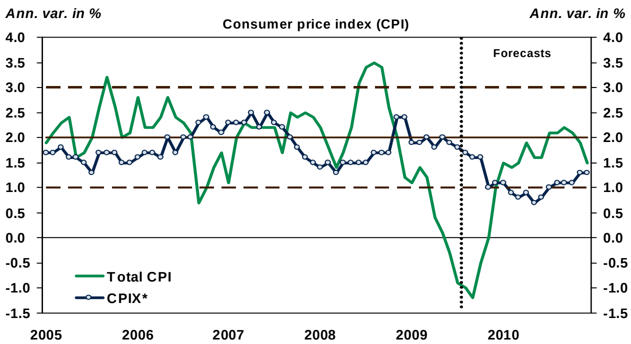


Sources: Datastream and Desjardins, Economic Studies

We acknowledge that Canada is in a better position than most of its G7 counterparts and that the global economic and financial context is improving. However, the situation is still not ripe for a monetary firming cycle; we expect the BoC to maintain an accommodative bias until at least June 2010.

Our main concern is disinflation. Although total deflation hit -0.9% in July, a low that dates back to 1953, prices are expected to swing back into positive territory by year's end due to the rise in oil prices (graph 14 on page 5). The problem is more closely tied to the BoC's reference index, which excludes

Graph 14 – Total deflation will prove temporary in Canada, but core inflation is preoccupying



* Which excludes eight of the most volatile elements.
Sources: Statistics Canada and Desjardins, Economic Studies

eight of the most volatile components, such as energy, as the widening output gap and a strong Canadian dollar will put pressures on prices in the second half of the year and early next year. With less strain associated with deficit financing in Canada, this could be enough to trap Canadian government rates in a tighter range, i.e. between 3.20% and 3.60%, until the end of 2009. Subsequently, the Canadian economy's relative performance and, in particular, less concern about long-term inflation (as the BoC refrained from using quantitative easing policies) should allow the Canadian bond market to outperform the U.S. market when rates eventually come up.

François Dupuis
Vice-President and Chief Economist

Martin Lefebvre
Senior Economist

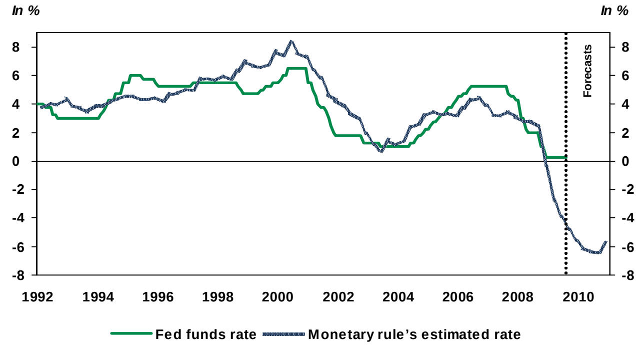
FEDERAL RESERVE

The Fed must be patient and cautious

- Federal Reserve (Fed) leaders must be encouraged by the turn of events. There are more and more signs that the U.S. economy is recovering and the worst—an abyss like the Great Depression—has clearly been avoided. The real estate market, the main source of the economy's woes, even seems to be stabilizing with some upticks in sales and the value of homes. The financial markets are also in a better position.
- However, the game is not yet over, and there is still some evident weakness in economic activity. Job losses remain substantial, although the monthly losses are not as large as they were last winter. Retail sales fell in July, and consumer confidence is still shaky, although some indexes came up in August.
- It is not clear whether the nascent recovery can stand on its own, apart from the government and Fed efforts to kick-start it. Although GDP growth is being stimulated by public spending and auto sales due to the Cash for Clunkers program, households are still skittish because of the deterioration in their balance sheets and rise in unemployment. Financial institutions also have to tackle the accumulated bad debt and risky investments in commercial real estate. The number of bank bankruptcies also picked up in the summer, a sign that the situation is fragile.
- The Fed must therefore be both cautious and patient, as the recovery is vulnerable to further shocks. Moreover, activity volumes in some financial markets, such as commercial paper, remain very low. Under the circumstances, a policy that would prematurely limit the economy's recovery must be avoided at all costs.
- Fortunately, inflation's evolution is giving the Fed a lot of leeway. Inflation reached a low of -2.1% in July on a decline by energy prices from their July 2008 peak. Total inflation could shoot up in the next few months due to the increase in oil prices, but core inflation, which excludes food and energy, should continue to moderate. At 1.5% in July, it will slowly close in on a low of 0.5% in mid-2010.
- Under the circumstances, in the near term, the Fed should gradually start to unwind its unconventional measures, which the improved situation and markets will in any case render less necessary. Only once the recovery is well under way and the risks of a renewed slump are over should the Fed start to move to raise interest rates.

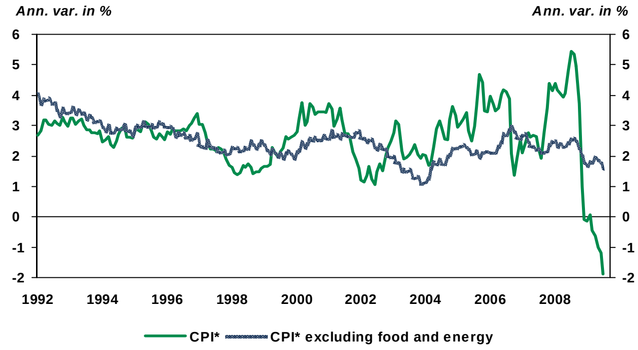
Forecasts: The economic situation is showing signs of improving, and the recovery is beginning. However, it remains fragile and subject to shocks. The Fed will thus be cautious, keeping the target rate for federal funds in its current range until the second half of 2010.

United States – Monetary rule



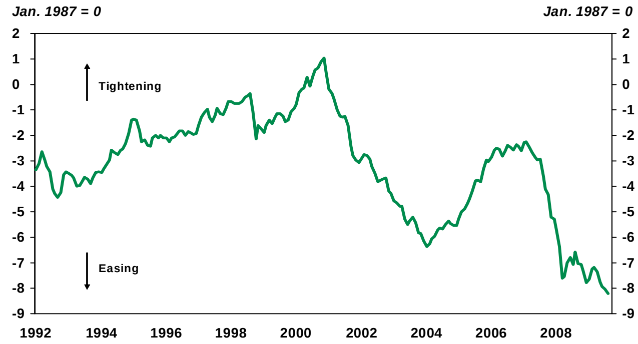
Sources: Datastream and Desjardins, Economic Studies

United States – Inflation rate



* Consumer price index.
Sources: Datastream and Desjardins, Economic Studies

United States – Monetary conditions index



Sources: Datastream and Desjardins, Economic Studies

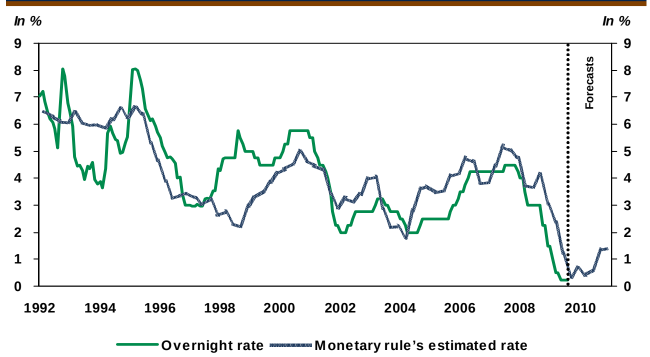
BANK OF CANADA

The BoC worried about the strong loonie

- The Bank of Canada (BoC) did not change its monetary policy in July. The key rate is at a floor of 0.25%, and the BoC has reiterated that it is committed to keeping it there until mid-2010 if its inflation scenario materializes. At this point in the economic cycle, the strategy seems to be completely in line with our monetary rule, which indicates that the "zero" rate policy should be maintained until the second half of 2010.
- On the economic front, real GDP declined by 3.4% (annualized) in the second quarter, after a 6.1% drop in the first quarter. In its latest *Monetary Policy Report*, the BoC was nonetheless upbeat, calling for real GDP growth of 1.3% in the third quarter of 2009. From our perspective, we continue to believe that Canada's real GDP will remain slightly in negative territory in the third quarter. The fact is that business inventories remain exceptionally high.
- Under these circumstances, we can expect the job market to continue to struggle until early 2010. However, a number of signals are corroborating an economic recovery before the end of the year. The leading indicator has shot up, and consumer confidence has improved. New manufacturing orders recently jumped 18.4%, the biggest increase since this time series began in 1992, suggesting that sales will rise substantially in the next few months.
- In the meantime, the BoC will monitor price evolution. The total annual inflation rate fell to -0.9% in July, something last seen in July 1953. Because it is both temporary and highly specific, deflation will no doubt not be a source of concern for monetary authorities. Their whole focus will thus be on what the core index (CPIX) is doing. The core index's annual change should gradually decline (especially towards the end of 2009), as the widening negative output gap increasingly makes itself felt.
- The impact of the loonie, whose recent surge has put rumours of BoC intervention in the foreign currency market back on the table, is another source of concern. Deputy Governor Timothy Lane's first public speech dealt with the flexibility the BoC had for trying to remedy it. However, we think it would be ill advised for the Bank to try to offset the impacts of rising oil prices on the Canadian dollar.

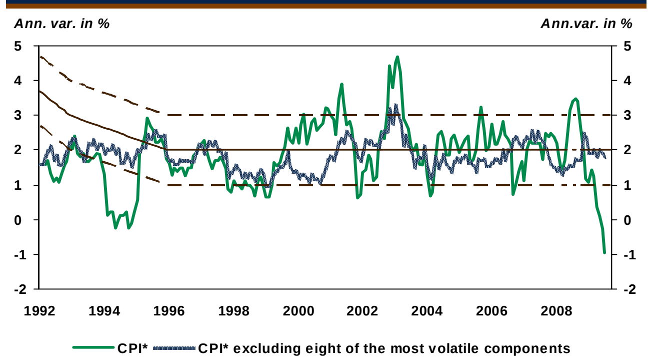
Forecasts: Everything suggests that the BoC will keep its commitment to maintaining the key rate at a low of 0.25% until June 2010. A scenario of slightly lower inflation than forecast could even force the BoC to put off the first rate increases until later.

Canada – Monetary rule



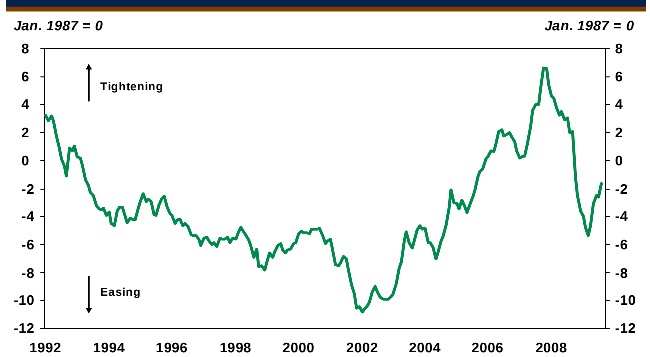
Sources: Datastream and Desjardins, Economic Studies

Canada – Inflation rate



* Consumer price index.
Sources: Datastream and Desjardins, Economic Studies

Canada – Monetary conditions index



Sources: Bank of Canada and Desjardins, Economic Studies

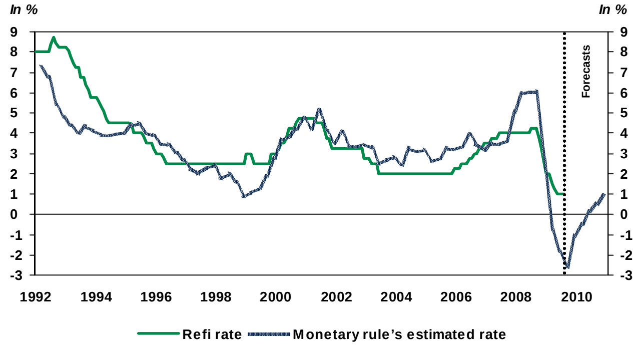
EUROPEAN CENTRAL BANK

The ECB will stay on the sidelines for several months

- The European Central Bank (ECB) has not adjusted its monetary policy in the last few months, with its key rate at 1.00% since May. The covered bond purchase program is following its course and should still reach €60B. The ECB is taking care to keep its options open, but it appears that monetary easing is over in the euro zone. The ECB will have avoided instituting true quantitative policy, although our monetary rule suggests that it should have gone much further with its action. Statements from ECB leaders have even undergone a major shift lately, with questions about whether or not further extraordinary measures needed to be adopted giving way to pessimistic remarks intended to quash the idea that key rates would come up soon.
- The noteworthy improvement in the euro zone's economic statistics is behind the ECB's change in stance. The recession continued last spring, but at a much slower pace. The zone's real GDP pulled back by an annualized 0.4% in the spring after posting a brutal plunge in the previous two quarters. Five of the zone's sixteen countries, including Germany and France, have even started to grow again. Moreover, the sharp upswing by the purchasing manager indexes and consumer and business confidence suggests that the situation is going to keep improving. Some data are still soft, however, especially retailing, which pulled back in May and June.
- The improvement in the economic statistics is not impressing ECB leaders. Over the last few weeks, they have repeatedly stated that the economic situation would continue to be tough. According to Council member Yves Mersch, the economic recovery is not sustainable and is still based on monetary and fiscal stimuli. The ECB also remains concerned about the deceleration of money supply growth and lending. It is still calling for economic activity to remain soft until the end of the year, with a slow recovery only seen in 2010. Inflation pressures should therefore remain quite subdued, with the annual change in prices at -0.2% in August, according to the flash estimate.

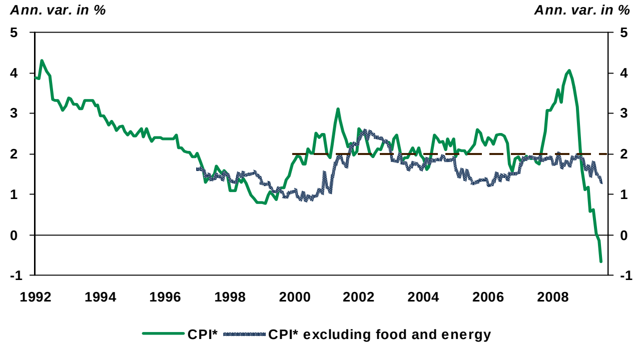
Forecasts: Improving economic statistics confirm that monetary easing is over in the euro zone. Like the ECB, we expect to see a modest, seesaw recovery, with more bad news potentially on the way. It will thus be necessary to keep key rates at their floor for a long time yet, to ensure price stability in the medium term.

Euro zone – Monetary rule



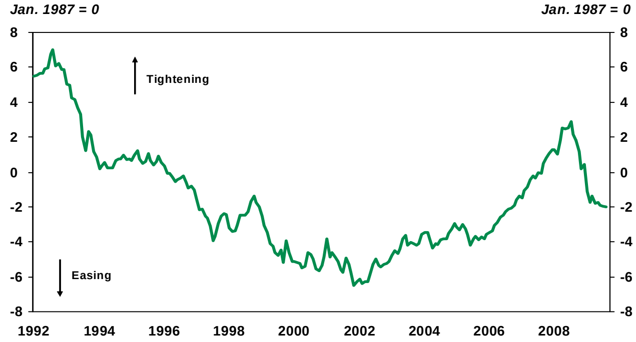
Sources: Datastream and Desjardins, Economic Studies

Euro zone – Inflation rate



* Consumer price index.
Sources: Datastream and Desjardins, Economic Studies

Euro zone – Monetary conditions index



Sources: Datastream and Desjardins, Economic Studies

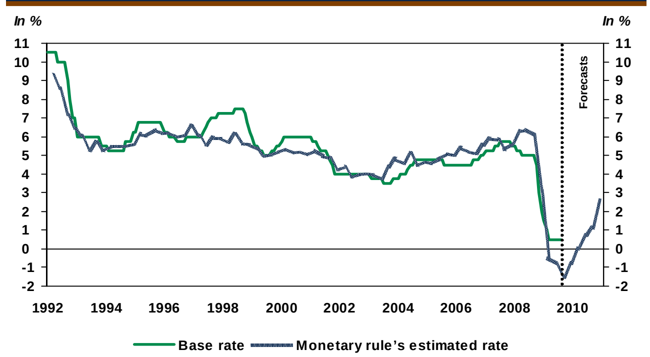
BANK OF ENGLAND

The signs of recovery do not calm the BoE's concerns

- The Bank of England's (BoE) August meeting was especially important. It was a given that the key rate would stay at its lower bound, 0.50%. However, the £125B asset purchase program had been completed and the BoE had to decide whether to pursue its quantitative policy any further. Once again, the BoE has taken the risk of doing too much rather than not enough, expanding its program by £50B. Most observers had been expecting an increase of no more than £25B. This took the program above the previous ceiling, requiring the approval of the British government.
- The end of the purchase program would have removed a support from the economy and Britain's financial system, representing monetary policy firming. Some encouraging economic statistics that have been released recently in the United Kingdom, however could have been seen as a signal that the crutch was no longer essential. After dropping by an annualized 9.3% in the first quarter of 2009, Britain's real GDP fell by 2.6% in the spring. However, everything is now signalling that the recession is coming to an end. Indicators of activity in manufacturing and services have climbed just above the level that indicates growth, while retail sales rose in June and July. Most statistics are also showing a nascent recovery in the housing sector.
- The BoE's leaders have noted the improvement in the economic indicators but judge that they do not allow them to gauge whether the recovery will be sustainable in the medium term. A number of factors, including credit conditions, high private sector and public sector debt loads and worker insecurity could put the brakes on the recovery. Moreover, BoE leaders are concerned about soft money supply growth, despite the quantitative measures, and by the pullback in loans to business. The BoE's new forecast therefore calls for the British economy to post a slow recovery. It anticipates that the existence of substantial excess capacity will put downside pressure on inflation for several quarters. At 1.8% in July, the inflation rate could stay under the 2% target in the medium term. This convinced the BoE to expand its quantitative policy again.

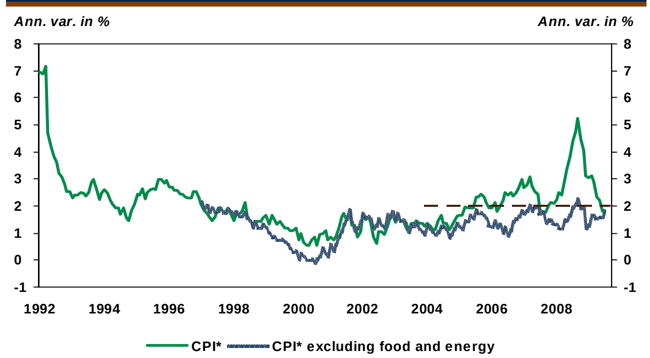
Forecasts: In a context in which the British government has very little fiscal leeway and in which the pound sterling tends to rise, we can understand why the BoE would want to avoid any monetary policy firming. Three of the nine monetary policy council members, including the Governor, were even in favour of a still larger increase in the asset purchase program. In this context, the key rate should stay at its floor until at least mid-2010.

United Kingdom – Monetary rule



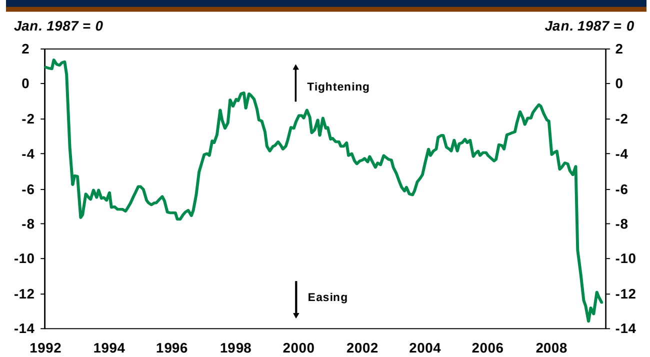
Sources: Datastream and Desjardins, Economic Studies

United Kingdom – Inflation rate



* Consumer price index.
Sources: Datastream and Desjardins, Economic Studies

United Kingdom – Monetary conditions index



Sources: Datastream and Desjardins, Economic Studies

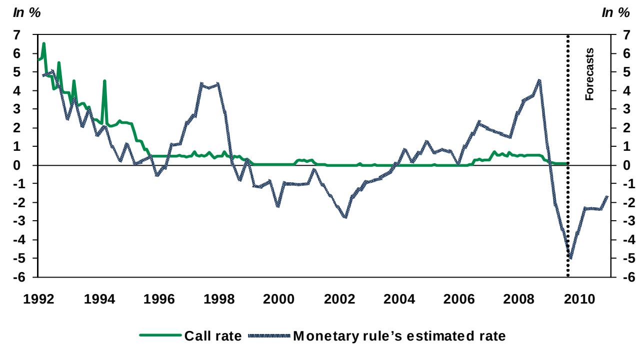
BANK OF JAPAN

The economy promises a long convalescence

- Japan's recession ended in the second quarter of 2009, when the country's real GDP posted an annualized increase of 3.7%. The Japanese downturn, which ran from Q1 of 2008 to Q1 of 2009, caused the economy to contract by 8.3% in all. A substantial output gap was created which will take more than a few quarters to resolve.
- The main components that contributed to the recent real GDP increase were consumption and foreign trade. The economic stimulus plan instituted by the Japanese government provided substantial support to the effort by consumers, while strong demand from China was primarily behind the improvement in foreign trade. Japan's GDP is still 7.5% below its winter 2008 peak, while industrial output is down 22.9% over the last year. Japan's economy is promising a long convalescence, and upcoming real GDP increases could be smaller. Japan's domestic demand is still sapped by the employment market's deterioration, as well as by a low business investment rate.
- Japan's annual inflation rate was -2.2% in July, already below the level seen during the previous deflation period. Inflation according to the index that excludes energy and fresh food prices is not down as much, but it is still a considerable -0.9%. The forecast slow recovery and deflation will not allow the Bank of Japan to quickly undertake monetary policy firming. Financial strains have nonetheless eased. Businesses are having much less difficulties in finding short-term financing. Activity in the corporate bond market is also up, but, for businesses with low credit ratings, access remains tight.
- Japanese voters went to the polls this weekend to elect a new government. Japan's fundamental problems, such as demography and dependence on foreign trade, fuelled a number of debates during the campaign. The proposals made by Japan's democratic party, which finally won, included creating an allowance for children and increasing public financing for education. However, these policies could add to the pressure on the country's already precarious public finances.

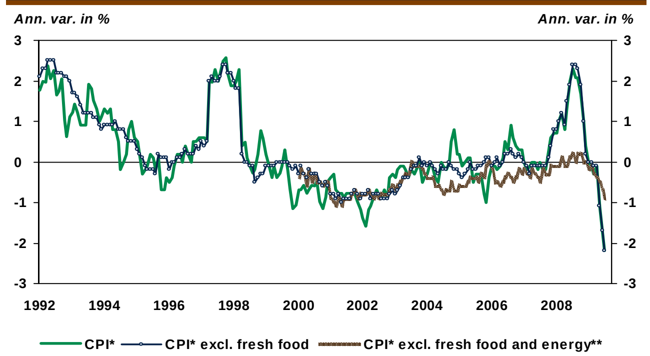
Forecasts: Despite the recovery that has begun, deflation and Japan's substantial excess production capacity will prompt monetary authorities to stay on the sidelines for several more quarters.

Japan – Monetary rule



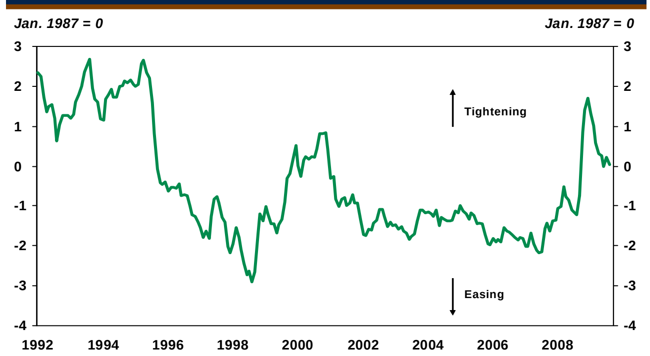
Sources: Datastream and Desjardins, Economic Studies

Japan – Inflation rate



* Consumer Price Index; ** The series begins in 2000.
Sources: Datastream and Desjardins, Economic Studies

Japan – Monetary conditions index



Sources: Datastream and Desjardins, Economic Studies

Table 1
Key interest rates

End of period in %	2008 Q1	2008 Q2	2008 Q3	2008 Q4	2009 Q1	2009 Q2	2009 Q3f	2009 Q4f	2010 Q1f	2010 Q2f	2010 Q3f	2010 Q4f
United States												
Federal funds	2.25	2.00	2.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.50	1.00
Canada												
Overnight funds	3.50	3.00	3.00	1.50	0.50	0.25	0.25	0.25	0.25	0.25	0.50	1.00
Euro zone												
Refinancing rate	4.00	4.00	4.25	2.50	1.50	1.00	1.00	1.00	1.00	1.00	1.00	1.50
United Kingdom												
Base rate	5.25	5.00	5.00	2.00	0.50	0.50	0.50	0.50	0.50	0.50	1.00	1.50
Japan												
Overnight funds	0.50	0.50	0.50	0.30	0.10	1.10	0.10	0.10	0.10	0.10	0.10	0.50

f: forecasts
Sources: Datastream and Desjardins, Economic Studies

Table 2
Schedule and key rates

Date	Central Bank	Decision	Rate
June 2008			
4	European Central Bank	s.q.	1.00
4	Bank of England	s.q.	0.50
4	Bank of Canada	s.q.	0.25
10	Reserve Bank of New Zealand	s.q.	2.50
10	Bank of Brazil	-100 b.p.	9.25
15	Bank of Japan	s.q.	0.10
17	Bank of Norway	-25 b.p.	1.25
18	Swiss National Bank	s.q.	0.25
19	Bank of Mexico	-50 b.p.	4.75
24	Federal Reserve	s.q.	0.00 / 0.25
July 2008			
2	European Central Bank	s.q.	1.00
2	Bank of Sweden	-25 b.p.	0.25
7	Reserve Bank of Australia	s.q.	3.00
9	Bank of England	s.q.	0.50
14	Bank of Japan	s.q.	0.10
17	Bank of Mexico	-25 b.p.	4.50
21	Bank of Canada	s.q.	0.25
22	Bank of Brazil	-50 b.p.	8.75
29	Reserve Bank of New Zealand	s.q.	2.50
August 2008			
4	Reserve Bank of Australia	s.q.	3.00
6	European Central Bank	s.q.	1.00
6	Bank of England	s.q.	0.50
10	Bank of Japan	s.q.	0.10
12	Bank of Norway	s.q.	1.25
12	Federal Reserve	s.q.	0.00 / 0.25
21	Bank of Mexico	s.q.	4.50

s.q.: status quo; b.p. : basis points
Source: Desjardins, Economic Studies

Table 3
Coming soon

Date	Central Bank
September 2009	
1	Reserve Bank of Australia
2	Bank of Brazil
3	European Central Bank
3	Bank of Sweden
9	Reserve Bank of New Zealand
10	Bank of England
10	Bank of Canada
16	Bank of Japan
17	Swiss National Bank
18	Bank of Mexico
23	Bank of Norway
23	Federal Reserve
October 2009	
6	Reserve Bank of Australia
8	European Central Bank
8	Bank of England
13	Bank of Japan
16	Bank of Mexico
20	Bank of Canada
21	Bank of Brazil
22	Bank of Norway
28	Reserve Bank of New Zealand
28	Bank of Japan
29	Bank of Sweden
November 2009	
2	Reserve Bank of Australia
4	Federal Reserve
5	European Central Bank
5	Bank of England

Source: Desjardins, Economic Studies

Table 4
United States: fixed income market

End of period in %	2008 Q1	2008 Q2	2008 Q3	2008 Q4	2009 Q1	2009 Q2	2009 Q3f	2009 Q4f	2010 Q1f	2010 Q2f	2010 Q3f	2010 Q4f
Key rate												
Federal funds	2.25	2.00	2.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.50	1.00
Treasury bills												
3-month	1.38	1.90	0.92	0.11	0.21	0.19	0.20	0.25	0.25	0.40	0.80	1.30
Federal bonds												
2-year	1.62	2.61	1.99	0.76	0.81	1.12	1.10	1.10	1.25	1.90	2.50	3.00
5-year	2.47	3.33	2.98	1.55	1.68	2.56	2.40	2.40	2.65	3.10	3.40	3.60
10-year	3.43	3.98	3.82	2.25	2.69	3.52	3.20	3.40	3.60	3.80	4.00	4.20
30-year	4.30	4.53	4.30	2.69	3.57	4.31	4.40	4.50	4.60	4.70	4.80	4.90
Yield curve												
5-year - 3-month	1.09	1.43	2.06	1.44	1.47	2.37	2.20	2.15	2.40	2.70	2.60	2.30
10-year - 2-year	1.81	1.36	1.84	1.49	1.88	2.40	2.10	2.30	2.35	1.90	1.50	1.20
30-year - 3-month	2.92	2.63	3.38	2.58	3.36	4.12	4.20	4.25	4.35	4.30	4.00	3.60

f: forecasts
Sources: Datastream and Desjardins, Economic Studies

Table 5
Canada: fixed income market

End of period in %	2008 Q1	2008 Q2	2008 Q3	2008 Q4	2009 Q1	2009 Q2	2009 Q3f	2009 Q4f	2010 Q1f	2010 Q2f	2010 Q3f	2010 Q4f
Key rate												
Overnight funds	3.50	3.00	3.00	1.50	0.50	0.25	0.25	0.25	0.25	0.25	0.50	1.00
Treasury bills												
3-month	1.88	2.50	1.90	0.89	0.40	0.25	0.30	0.30	0.35	0.45	0.80	1.30
Federal bonds												
2-year	2.63	3.25	2.79	1.09	1.07	1.21	1.30	1.30	1.40	2.00	2.60	3.10
5-year	2.91	3.46	3.17	1.70	1.75	2.46	2.55	2.60	2.90	3.40	3.65	3.75
10-year	3.43	3.74	3.76	2.69	2.78	3.36	3.30	3.50	3.70	4.00	4.20	4.30
30-year	3.94	4.08	4.23	3.46	3.56	3.86	4.00	4.30	4.50	4.70	4.90	5.00
Yield curve												
5-year - 3-month	1.03	0.96	1.27	0.81	1.35	2.21	2.25	2.30	2.55	2.95	2.85	2.45
10-year - 2-year	0.80	0.49	0.97	1.60	1.71	2.15	2.00	2.20	2.30	2.00	1.60	1.20
30-year - 3-month	2.06	1.58	2.33	2.57	3.16	3.61	3.70	4.00	4.15	4.25	4.10	3.70
Spreads (Canada - U.S.)												
3-month	0.50	0.60	0.98	0.78	0.19	0.06	0.10	0.05	0.10	0.05	0.00	0.00
2-year	1.01	0.63	0.80	0.32	0.27	0.09	0.20	0.20	0.15	0.10	0.10	0.10
5-year	0.44	0.13	0.19	0.15	0.07	-0.10	0.15	0.20	0.25	0.30	0.25	0.15
10-year	0.00	-0.24	-0.07	0.44	0.09	-0.16	0.10	0.10	0.10	0.20	0.20	0.10
30-year	-0.36	-0.45	-0.07	0.76	0.00	-0.45	-0.40	-0.20	-0.10	0.00	0.10	0.10

f: forecasts
Sources: Datastream and Desjardins, Economic Studies