

THE YIELD CURVE

Concern over the Coronavirus Boosts the Bond Market

HIGHLIGHTS

- ▶ Following last fall's rise, North American bond yields edged down at the start of 2020 on mixed economic statistics. The coronavirus then triggered a sharp drop in yields, with investors fleeing to safe-haven securities and once again starting to bank on monetary easing in North America. The U.S. 10-year yield, which ended 2019 above 1.90%, thus closed in on 1.50% at the end of January. Canadian yields pulled back even more sharply. Although an upswing in optimism recently drove stock markets to new heights, bond yields have only ticked up since the start of February.
- ▶ Speaking before Congress, Jerome Powell stated that the Federal Reserve (Fed) was closely monitoring the emergence of the coronavirus. This could get investors to continue to look for further monetary easing around mid-2020. For now, however, there is nothing to indicate that the Fed will rush into action. It still says that the current monetary policy will likely remain appropriate if the economy evolves as expected. The latest news in this area is fairly encouraging, with the ISM manufacturing index crossing back above 50, indicating that activity is expanding, and the job market getting the new year off to a strong start.
- ▶ The Bank of Canada (BoC) took a fairly positive tone in December, then surprised many observers once again by showing much more concern at its January 22 meeting. Although it recognizes the role of temporary factors in Canada's weak growth at the end of 2019, it is not ruling out the possibility of it being linked to a more lasting trend, especially on the consumer side. This prompted it to clearly open the door to monetary easing, which favoured Canada's bond market. However, the reassuring economic numbers published since the January meeting, particularly on Canadian households, do not point to rapid action from the BoC.
- ▶ Although the uncertainty surrounding Brexit has declined, the Bank of England is concerned about the weak British economy and inflation. Several of its leaders had even opened the door to monetary easing. In the end, the business activity indexes posted a major rebound, convincing them to stick with the status quo at the January 30 meeting. As the negotiations to establish trade terms with Europe promise to be tough, a key rate cut later this year remains likely. For its part, the European Central Bank should maintain a very accommodating monetary policy.

INTEREST RATE FORECASTS

- ▶ Bond yields could keep moving in tandem with news on the coronavirus in the near term. If the situation degenerates and starts to have major, persistent impacts outside China, several central banks, including the BoC, could add monetary policy stimulus to support economic growth.
- ▶ For now, it is more likely that the epidemic will not have a major lasting impact on growth in Canada and the United States. In this case, North American key rates should be steady throughout 2020 and bond yields could gradually climb back toward the levels seen at the end of last year.

François Dupuis, Vice-President and Chief Economist • Mathieu D'Anjou, Deputy Chief Economist

Benoit P. Durocher, Senior Economist • Francis Généreux, Senior Economist • Jimmy Jean, Macro Strategist • Hendrix Vachon, Senior Economist

Desjardins, Economic Studies: 514-281-2336 or 1 866-866-7000, ext. 5552336 • desjardins.economics@desjardins.com • desjardins.com/economics

NOTE TO READERS: The letters k, M and B are used in texts and tables to refer to thousands, millions and billions respectively.

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TABLE 1
Key interest rates

END OF PERIOD IN %	2019				2020				2021			
	Q1	Q2	Q3	Q4	Q1f	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
United States												
Federal funds	2.50	2.50	2.00	1.75	1.75	1.75	1.75	1.75	1.50	1.25	1.25	1.25
Canada												
Overnight funds	1.75	1.75	1.75	1.75	1.75	1.75	1.75	1.75	1.75	1.50	1.25	1.25
Zone euro												
Refinancing rate	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
United Kingdom												
Base rate	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.50	0.25	0.25	0.25	0.25
Japan												
Main key rate	-0.10	-0.10	-0.10	-0.10	-0.20	-0.20	-0.20	-0.20	-0.20	-0.20	-0.20	-0.20

f: forecasts

Sources: Datastream and Desjardins, Economic Studies

TABLE 2
Fixed income market

END OF PERIOD IN %	2019				2020				2021			
	Q1	Q2	Q3	Q4	Q1f	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
UNITED STATES												
Treasury bills												
3-month	2.40	2.12	1.88	1.55	1.55	1.60	1.65	1.60	1.35	1.10	1.10	1.10
Federal bonds												
2-year	2.29	1.76	1.66	1.58	1.50	1.65	1.75	1.65	1.35	1.20	1.20	1.20
5-year	2.23	1.76	1.54	1.68	1.50	1.70	1.80	1.65	1.35	1.25	1.30	1.35
10-year	2.41	2.00	1.67	1.92	1.65	1.85	2.00	1.85	1.50	1.40	1.45	1.50
30-year	2.82	2.53	2.11	2.39	2.15	2.30	2.40	2.25	1.95	1.90	1.95	2.00
Yield curve slopes												
5-year - 3-month	-0.17	-0.36	-0.34	0.13	-0.05	0.10	0.15	0.05	0.00	0.15	0.20	0.25
10-year - 2-year	0.13	0.24	0.01	0.34	0.15	0.20	0.25	0.20	0.15	0.20	0.25	0.30
30-year - 3-month	0.42	0.41	0.23	0.84	0.60	0.70	0.75	0.65	0.60	0.80	0.85	0.90
CANADA												
Treasury bills												
3-month	1.67	1.66	1.65	1.66	1.65	1.65	1.70	1.65	1.55	1.30	1.20	1.20
Federal bonds												
2-year	1.55	1.47	1.58	1.69	1.55	1.65	1.75	1.65	1.45	1.30	1.25	1.25
5-year	1.52	1.39	1.40	1.68	1.40	1.60	1.75	1.65	1.35	1.25	1.25	1.30
10-year	1.62	1.46	1.37	1.70	1.40	1.60	1.80	1.65	1.35	1.30	1.35	1.40
30-year	1.90	1.68	1.53	1.76	1.55	1.75	1.90	1.80	1.55	1.50	1.55	1.60
Yield curve slopes												
5-year - 3-month	-0.15	-0.27	-0.25	0.02	-0.25	-0.05	0.05	0.00	-0.20	-0.05	0.05	0.10
10-year - 2-year	0.07	-0.01	-0.21	0.01	-0.15	-0.05	0.05	0.00	-0.10	0.00	0.10	0.15
30-year - 3-month	0.23	0.02	-0.12	0.10	-0.10	0.10	0.20	0.15	0.00	0.20	0.35	0.40
Yield spreads (Canada—United States)												
3-month	-0.73	-0.46	-0.23	0.11	0.10	0.05	0.05	0.05	0.20	0.20	0.10	0.10
2-year	-0.74	-0.29	-0.08	0.11	0.05	0.00	0.00	0.00	0.10	0.10	0.05	0.05
5-year	-0.71	-0.37	-0.14	0.00	-0.10	-0.10	-0.05	0.00	0.00	0.00	-0.05	-0.05
10-year	-0.79	-0.54	-0.30	-0.22	-0.25	-0.25	-0.20	-0.20	-0.15	-0.10	-0.10	-0.10
30-year	-0.92	-0.85	-0.58	-0.63	-0.60	-0.55	-0.50	-0.45	-0.40	-0.40	-0.40	-0.40

f: forecasts

Sources: Datastream and Desjardins, Economic Studies

Schedule 2020 of Central Bank Meetings

Date	Central banks	Decision	Rate
January			
16	Bank of Korea	s.q.	1.25
20	Bank of Japan	s.q.	-0.10
22	Bank of Canada*	s.q.	1.75
23	European Central Bank	s.q.	0.00
23	Bank of Norway	s.q.	1.50
29	Federal Reserve	s.q.	1.75
30	Bank of England	s.q.	0.75
February			
3	Reserve Bank of Australia	s.q.	0.75
5	Bank of Brazil	-25 b.p.	4.25
11	Reserve Bank of New Zealand	s.q.	1.00
12	Bank of Sweden	s.q.	0.00
13	Bank of Mexico		
27	Bank of Korea		
March			
2	Reserve Bank of Australia		
4	Bank of Canada		
12	European Central Bank		
18	Bank of Brazil		
18	Federal Reserve		
19	Bank of Norway		
19	Bank of Japan		
19	Swiss National Bank		
24	Reserve Bank of New Zealand		
26	Bank of England		
26	Bank of Mexico		
April			
7	Reserve Bank of Australia		
9	Bank of Korea		
15	Bank of Canada*		
28	Bank of Sweden		
28	Bank of Japan		
29	Federal Reserve		
30	European Central Bank		
May			
5	Reserve Bank of Australia		
6	Bank of Brazil		
7	Bank of England		
7	Bank of Norway		
12	Reserve Bank of New Zealand		
14	Bank of Mexico		
28	Bank of Korea		
June			
2	Reserve Bank of Australia		
3	Bank of Canada		
4	European Central Bank		
10	Federal Reserve		
16	Bank of Japan		
17	Bank of Brazil		
18	Bank of England		
18	Bank of Norway		
18	Swiss National Bank		
23	Reserve Bank of New Zealand		
25	Bank of Mexico		

Date	Central banks	Decision	Rate
July			
1	Bank of Sweden		
7	Reserve Bank of Australia		
15	Bank of Canada*		
16	European Central Bank		
16	Bank of Korea		
22	Bank of Japan		
29	Federal Reserve		
August			
4	Reserve Bank of Australia		
5	Bank of Brazil		
6	Bank of England		
11	Reserve Bank of New Zealand		
13	Bank of Mexico		
20	Bank of Norway		
27	Bank of Korea		
September			
1	Reserve Bank of Australia		
9	Bank of Canada		
10	European Central Bank		
16	Bank of Brazil		
16	Federal Reserve		
17	Bank of Japan		
17	Bank of England		
22	Reserve Bank of New Zealand		
22	Bank of Sweden		
24	Bank of Norway		
24	Bank of Mexico		
24	Swiss National Bank		
October			
5	Reserve Bank of Australia		
14	Bank of Korea		
28	Bank of Brazil		
28	Bank of Canada*		
29	European Central Bank		
29	Bank of Japan		
November			
2	Reserve Bank of Australia		
5	Bank of England		
5	Bank of Norway		
5	Federal Reserve		
10	Reserve Bank of New Zealand		
12	Bank of Mexico		
26	Bank of Korea		
26	Bank of Sweden		
30	Reserve Bank of Australia		
December			
7	Bank of Mexico		
9	Bank of Brazil		
9	Bank of Canada		
10	European Central Bank		
16	Federal Reserve		
17	Bank of England		
17	Bank of Norway		
17	Swiss National Bank		
18	Bank of Japan		

NOTE: Certain banks may decide to change rates in-between the scheduled meetings. The abbreviations s.q. and b.p. correspond to status quo and basis points respectively. * Monetary Policy Report published.