

## THE YIELD CURVE

# Decisive Central Bank Actions Should Keep Bond Yields Very Low

### HIGHLIGHTS

- ▶ The worldwide spread of COVID-19 has heavily impacted the global economy and financial markets. Already quite low, bond yields took a major tumble, hitting historic lows in many cases. As for corporate bonds, the widening of credit spreads has grabbed the most attention.
- ▶ In the face of the demand shock stemming from COVID-19, the Federal Reserve (Fed) jumped into action. In March, it lowered the target range for federal funds to its effective floor of 0.00% to 0.25% and multiplied its securities purchase programs to help keep the financial markets running smoothly. In particular, its program to purchase federal bonds and mortgage agency bonds is now unlimited. In addition, the Fed is now directly supporting the corporate bond market and has multiplied its programs to promote access to credit for borrowers. In many respects, the Fed has been much more aggressive than in 2008, which leads us to believe it will succeed in preventing the current economic crisis from becoming a financial or liquidity crisis.
- ▶ The Bank of Canada (BoC) also took decisive actions to counter the negative financial impacts of the COVID-19 crisis.

Like the Fed, it cut its key interest rate by 150 points in March, bringing the target for the overnight rate down to 0.25%. Although the BoC had previously left the door open to the possibility of negative rates, it now believes that key rates are at their effective floor. Japan and Europe's experiences seem to have convinced it that negative rates could have more undesirable effects than positive ones. The smooth functioning of the Canadian financial system appears to be the BoC's primary concern right now, and it has announced a host of measures, some in coordination with other federal bodies, to ensure access to liquidity and credit. Furthermore, it recently announced that it would purchase at least \$5B per week in federal government securities on the secondary market. This is Canada's first quantitative easing program, and it will continue until the economic recovery is well underway.

- ▶ Overseas central banks are also taking measures to limit the financial repercussions of COVID-19 by lowering their key rates, when still possible, and significantly boosting their asset purchases.

### INTEREST RATE FORECASTS

- ▶ We can expect a long period of stable key rates in North America, as they are currently at their effective floors according to the Fed and the BoC. It will take a certain amount of time and sufficiently strong economic growth to bring the economy back to its full potential after the current crisis. Moreover, central banks will likely opt to cease most of the programs implemented to support the smooth functioning of the financial markets before raising their key rates.
- ▶ Bond yields should also remain very low in the coming quarters, reflecting significant quantitative easing on the part of the central banks and weak inflationary pressures. The various programs implemented by central banks should help minimize financial strains and gradually shrink credit spreads.

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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    | Q1    | Q2f   | Q3f   | Q4f   | Q1f   | Q2f   | Q3f   | Q4f   |
| <b>United States</b>  |       |       |       |       |       |       |       |       |       |       |       |       |
| Federal funds         | 2.50  | 2.50  | 2.00  | 1.75  | 0.25  | 0.25  | 0.25  | 0.25  | 0.25  | 0.25  | 0.25  | 0.25  |
| <b>Canada</b>         |       |       |       |       |       |       |       |       |       |       |       |       |
| Overnight funds       | 1.75  | 1.75  | 1.75  | 1.75  | 0.25  | 0.25  | 0.25  | 0.25  | 0.25  | 0.25  | 0.25  | 0.25  |
| <b>Zone euro</b>      |       |       |       |       |       |       |       |       |       |       |       |       |
| 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  |
| <b>United Kingdom</b> |       |       |       |       |       |       |       |       |       |       |       |       |
| Base rate             | 0.75  | 0.75  | 0.75  | 0.75  | 0.10  | 0.10  | 0.10  | 0.10  | 0.10  | 0.10  | 0.10  | 0.10  |
| <b>Japan</b>          |       |       |       |       |       |       |       |       |       |       |       |       |
| Main key rate         | -0.10 | -0.10 | -0.10 | -0.10 | -0.10 | -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    | Q1   | Q2f   | Q3f   | Q4f   | Q1f   | Q2f   | Q3f   | Q4f   |
| <b>UNITED STATES</b>                        |       |       |       |       |      |       |       |       |       |       |       |       |
| <b>Treasury bills</b>                       |       |       |       |       |      |       |       |       |       |       |       |       |
| 3-month                                     | 2.40  | 2.12  | 1.88  | 1.55  | 0.11 | 0.05  | 0.10  | 0.10  | 0.15  | 0.15  | 0.15  | 0.20  |
| <b>Federal bonds</b>                        |       |       |       |       |      |       |       |       |       |       |       |       |
| 2-year                                      | 2.29  | 1.76  | 1.66  | 1.58  | 0.25 | 0.25  | 0.35  | 0.40  | 0.45  | 0.50  | 0.55  | 0.65  |
| 5-year                                      | 2.23  | 1.76  | 1.54  | 1.68  | 0.36 | 0.40  | 0.45  | 0.50  | 0.60  | 0.65  | 0.75  | 0.90  |
| 10-year                                     | 2.41  | 2.00  | 1.67  | 1.92  | 0.67 | 0.70  | 0.75  | 0.85  | 0.95  | 1.00  | 1.05  | 1.25  |
| 30-year                                     | 2.82  | 2.53  | 2.11  | 2.39  | 1.32 | 1.30  | 1.35  | 1.40  | 1.45  | 1.50  | 1.55  | 1.70  |
| <b>Yield curve slopes</b>                   |       |       |       |       |      |       |       |       |       |       |       |       |
| 5-year - 3-month                            | -0.17 | -0.36 | -0.34 | 0.13  | 0.25 | 0.35  | 0.35  | 0.40  | 0.45  | 0.50  | 0.60  | 0.70  |
| 10-year - 2-year                            | 0.13  | 0.24  | 0.01  | 0.34  | 0.41 | 0.45  | 0.40  | 0.45  | 0.50  | 0.50  | 0.50  | 0.60  |
| 30-year - 3-month                           | 0.42  | 0.41  | 0.23  | 0.84  | 1.21 | 1.25  | 1.25  | 1.30  | 1.30  | 1.35  | 1.40  | 1.50  |
| <b>CANADA</b>                               |       |       |       |       |      |       |       |       |       |       |       |       |
| <b>Treasury bills</b>                       |       |       |       |       |      |       |       |       |       |       |       |       |
| 3-month                                     | 1.67  | 1.66  | 1.65  | 1.66  | 0.21 | 0.20  | 0.20  | 0.20  | 0.25  | 0.25  | 0.25  | 0.25  |
| <b>Federal bonds</b>                        |       |       |       |       |      |       |       |       |       |       |       |       |
| 2-year                                      | 1.55  | 1.47  | 1.58  | 1.69  | 0.42 | 0.35  | 0.40  | 0.45  | 0.50  | 0.55  | 0.60  | 0.65  |
| 5-year                                      | 1.52  | 1.39  | 1.40  | 1.68  | 0.60 | 0.50  | 0.55  | 0.60  | 0.65  | 0.70  | 0.75  | 0.80  |
| 10-year                                     | 1.62  | 1.46  | 1.37  | 1.70  | 0.71 | 0.65  | 0.70  | 0.80  | 0.85  | 0.90  | 0.95  | 1.05  |
| 30-year                                     | 1.90  | 1.68  | 1.53  | 1.76  | 1.32 | 1.25  | 1.30  | 1.35  | 1.35  | 1.40  | 1.45  | 1.50  |
| <b>Yield curve slopes</b>                   |       |       |       |       |      |       |       |       |       |       |       |       |
| 5-year - 3-month                            | -0.15 | -0.27 | -0.25 | 0.02  | 0.39 | 0.30  | 0.35  | 0.40  | 0.40  | 0.45  | 0.50  | 0.55  |
| 10-year - 2-year                            | 0.07  | -0.01 | -0.21 | 0.01  | 0.29 | 0.30  | 0.30  | 0.35  | 0.35  | 0.35  | 0.35  | 0.40  |
| 30-year - 3-month                           | 0.23  | 0.02  | -0.12 | 0.10  | 1.11 | 1.05  | 1.10  | 1.15  | 1.10  | 1.15  | 1.20  | 1.25  |
| <b>Yield spreads (Canada—United States)</b> |       |       |       |       |      |       |       |       |       |       |       |       |
| 3-month                                     | -0.73 | -0.46 | -0.23 | 0.11  | 0.10 | 0.15  | 0.10  | 0.10  | 0.10  | 0.10  | 0.10  | 0.05  |
| 2-year                                      | -0.74 | -0.29 | -0.08 | 0.11  | 0.17 | 0.10  | 0.05  | 0.05  | 0.05  | 0.05  | 0.05  | 0.00  |
| 5-year                                      | -0.71 | -0.37 | -0.14 | 0.00  | 0.24 | 0.10  | 0.10  | 0.10  | 0.05  | 0.05  | 0.00  | -0.10 |
| 10-year                                     | -0.79 | -0.54 | -0.30 | -0.22 | 0.04 | -0.05 | -0.05 | -0.05 | -0.10 | -0.10 | -0.10 | -0.20 |
| 30-year                                     | -0.92 | -0.85 | -0.58 | -0.63 | 0.00 | -0.05 | -0.05 | -0.05 | -0.10 | -0.10 | -0.10 | -0.20 |

f: forecasts

Sources: Datastream and Desjardins, Economic Studies

# Schedule 2020 of Central Bank Meetings

| Date            | Central banks               | Decision  | Rate  |
|-----------------|-----------------------------|-----------|-------|
| <b>January</b>  |                             |           |       |
| 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  |
| <b>February</b> |                             |           |       |
| 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              | -25 b.p.  | 7.00  |
| 27              | Bank of Korea               | s.q.      | 1.25  |
| <b>March</b>    |                             |           |       |
| 2               | Reserve Bank of Australia   | -25 b.p.  | 0.50  |
| 3               | Federal Reserve             | -50 b.p.  | 1.25  |
| 4               | Bank of Canada              | -50 b.p.  | 1.25  |
| 11              | Bank of England             | -50 b.p.  | 0.25  |
| 12              | European Central Bank       | s.q.      | 0.00  |
| 13              | Bank of Norway              | -50 b.p.  | 1.00  |
| 13              | Bank of Canada              | -50 b.p.  | 0.75  |
| 15              | Reserve Bank of New Zealand | -75 b.p.  | 0.25  |
| 15              | Federal Reserve             | -100 b.p. | 0.25  |
| 16              | Bank of Korea               | -50 b.p.  | 0.75  |
| 16              | Bank of Japan               | s.q.      | -0.10 |
| 18              | Reserve Bank of Australia   | -25 b.p.  | 0.25  |
| 18              | Bank of Brazil              | -50 b.p.  | 3.75  |
| 19              | Bank of England             | -15 b.p.  | 0.10  |
| 19              | Swiss National Bank         | s.q.      | -0.75 |
| 20              | Bank of Norway              | -75 b.p.  | 0.25  |
| 20              | Bank of Mexico              | -50 b.p.  | 6.50  |
| 26              | Bank of England             | s.q.      | 0.10  |
| 27              | Bank of Canada              | -50 b.p.  | 0.25  |
| <b>April</b>    |                             |           |       |
| 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       |           |       |
| <b>May</b>      |                             |           |       |
| 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               |           |       |
| <b>June</b>     |                             |           |       |
| 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 |
|------------------|-----------------------------|----------|------|
| <b>July</b>      |                             |          |      |
| 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             |          |      |
| <b>August</b>    |                             |          |      |
| 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               |          |      |
| <b>September</b> |                             |          |      |
| 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         |          |      |
| <b>October</b>   |                             |          |      |
| 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               |          |      |
| <b>November</b>  |                             |          |      |
| 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   |          |      |
| <b>December</b>  |                             |          |      |
| 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.