

THE YIELD CURVE

Central Banks Expected to Remain in Control of Bond Markets for a Good While

HIGHLIGHTS

- ▶ COVID-19 continues to dominate current events. The economic indicator meltdown in March and April, including the loss of over 20 million jobs in the United States, illustrates that the current crisis represents an economic shock of unprecedented proportions in contemporary history. At the same time, signs that the pandemic is slowing in several countries and the gradual easing of lockdown measures are cause for hope that economic activity will resume in the coming months. Benefiting also from the unheard of support on the part of central banks and governments, the stock markets have thus performed very well in recent weeks, and the main North American indices are posting gains of about 30% since bottoming out in March. This stock market rebound has not been reflected in bond yields, which remained very low in April.
- ▶ Once again, the impression that stock markets and bond yields in North America are moving in diverging directions is mostly a reflection of the actions taken by central banks. By very quickly lowering their key rates to almost zero and, in particular, by launching massive, diversified securities purchases, the Federal Reserve (Fed) and the Bank of Canada (BoC) succeeded in allaying fears of a major financial crisis. This helped the stock markets and riskier bonds. The central banks' actions are also directly supporting the demand for government bonds, keeping yield extremely low. Government measures to support households and companies have also played a crucial role in reassuring investors. The costs of these measures combined with the economic struggles will however cause government deficits and borrowing needs to balloon. This recently caused some upside pressure on the yields of longer maturity U.S. bonds.
- ▶ The BoC announced that Tiff Macklem will take the reins of this institution on June 3. This new governor should opt for continuity and has already indicated that he was comfortable with a 0.25% effective key rate floor under the current circumstances. By announcing in mid-April that it would buy longer-term provincial bonds and even corporate bonds, the BoC also helped to reduce credit spreads.
- ▶ Overseas central banks are also continuing to implement measures to ensure that financial conditions remain favourable. Despite a recent unfavourable judgment on the part of the German constitutional court, the European Central Bank seems determined to continue with its bond purchases and is even considering the option of buying riskier assets.

INTEREST RATE FORECASTS

- ▶ We still expect key rates in North America to remain stable for a long while. For now, nothing seems to suggest that the Fed and the BoC will be tempted by negative rates. Their primary concern in the coming quarters will be to ensure that financial conditions remain favourable and that access to credit and liquidity remain easy.
- ▶ The governments' major borrowing needs could continue to cause some concerns and maintain a bit of a slope on North American yield curves. A persistent, significant increase in long-term bond yields would nevertheless be very surprising in the short term as low inflation and a weak economy will push central banks to continue purchasing bonds at current levels, and even increase them if needed.

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.

IMPORTANT: This document is based on public information and may under no circumstances be used or construed as a commitment by Desjardins Group. While the information provided has been determined on the basis of data obtained from sources that are deemed to be reliable, Desjardins Group in no way warrants that the information is accurate or complete. The document is provided solely for information purposes and does not constitute an offer or solicitation for purchase or sale. Desjardins Group takes no responsibility for the consequences of any decision whatsoever made on the basis of the data contained herein and does not hereby undertake to provide any advice, notably in the area of investment services. The data on prices or margins are provided for information purposes and may be modified at any time, based on such factors as market conditions. The past performances and projections expressed herein are no guarantee of future performance. The opinions and forecasts contained herein are, unless otherwise indicated, those of the document's authors and do not represent the opinions of any other person or the official position of Desjardins Group. Copyright © 2020, Desjardins Group. All rights reserved.

TABLE 1
Key interest rates

END OF PERIOD IN %	2019				2020				2021			
	Q1	Q2	Q3	Q4	Q1	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
United States												
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
Canada												
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
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	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
Japan												
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
UNITED STATES												
Treasury bills												
3-month	2.40	2.12	1.88	1.55	0.11	0.10	0.10	0.10	0.15	0.15	0.15	0.15
Federal bonds												
2-year	2.29	1.76	1.66	1.58	0.25	0.25	0.30	0.40	0.45	0.50	0.50	0.55
5-year	2.23	1.76	1.54	1.68	0.36	0.40	0.45	0.55	0.60	0.65	0.65	0.70
10-year	2.41	2.00	1.67	1.92	0.67	0.70	0.75	0.85	0.90	0.95	1.00	1.05
30-year	2.82	2.53	2.11	2.39	1.32	1.40	1.45	1.50	1.50	1.55	1.55	1.60
Yield curve slopes												
5-year - 3-month	-0.17	-0.36	-0.34	0.13	0.25	0.30	0.35	0.45	0.45	0.50	0.50	0.55
10-year - 2-year	0.13	0.24	0.01	0.34	0.41	0.45	0.45	0.45	0.45	0.45	0.50	0.50
30-year - 3-month	0.42	0.41	0.23	0.84	1.21	1.30	1.35	1.40	1.35	1.40	1.40	1.45
CANADA												
Treasury bills												
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
Federal bonds												
2-year	1.55	1.47	1.58	1.69	0.42	0.35	0.40	0.45	0.50	0.55	0.55	0.60
5-year	1.52	1.39	1.40	1.68	0.60	0.45	0.55	0.60	0.65	0.70	0.70	0.75
10-year	1.62	1.46	1.37	1.70	0.71	0.65	0.70	0.80	0.85	0.90	0.90	0.95
30-year	1.90	1.68	1.53	1.76	1.32	1.25	1.30	1.35	1.40	1.45	1.45	1.50
Yield curve slopes												
5-year - 3-month	-0.15	-0.27	-0.25	0.02	0.39	0.25	0.35	0.40	0.40	0.45	0.45	0.50
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	0.35
30-year - 3-month	0.23	0.02	-0.12	0.10	1.11	1.05	1.10	1.15	1.15	1.20	1.20	1.25
Yield spreads (Canada—United States)												
3-month	-0.73	-0.46	-0.23	0.11	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
2-year	-0.74	-0.29	-0.08	0.11	0.17	0.10	0.10	0.05	0.05	0.05	0.05	0.05
5-year	-0.71	-0.37	-0.14	0.00	0.24	0.05	0.10	0.05	0.05	0.05	0.05	0.05
10-year	-0.79	-0.54	-0.30	-0.22	0.04	-0.05	-0.05	-0.05	-0.05	-0.05	-0.10	-0.10
30-year	-0.92	-0.85	-0.58	-0.63	0.00	-0.15	-0.15	-0.15	-0.10	-0.10	-0.10	-0.10

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	-25 b.p.	7.00
27	Bank of Korea	s.q.	1.25
March			
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
April			
7	Reserve Bank of Australia	s.q.	0.25
9	Bank of Korea	s.q.	0.75
15	Bank of Canada*	s.q.	0.25
28	Bank of Sweden	s.q.	0.00
28	Bank of Japan	s.q.	-0.10
29	Federal Reserve	s.q.	0.25
30	European Central Bank	s.q.	0.00
May			
5	Reserve Bank of Australia	s.q.	0.25
6	Bank of Brazil	-75 b.p.	3.00
7	Bank of England	s.q.	0.10
7	Bank of Norway	-25 b.p.	0.00
12	Reserve Bank of New Zealand	s.q.	0.25
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.