

THE YIELD CURVE

Although Economic Activity Is Gradually Resuming, Bond Yields Should Remain Very Low

HIGHLIGHTS

- ▶ The drop in COVID-19 cases in the parts of Europe and North America that had been hardest hit means that economies can keep opening up slowly. Signs that activity was rebounding as of May, particularly the job gains in the United States and Canada, allowed stock indexes to keep shooting up and even start putting upside pressure on long-term bond yields. The U.S. 10-year yield thus temporarily went over 0.90% in early June, posting a spread of almost 70 basis points with the 2-year yield. The uptrend did not last, with the Federal Reserve's (Fed) worried tone and another rise in pandemic cases in several countries and U.S. states quickly putting downside pressures back on bond yields.
- ▶ Although the worst COVID-19 scenarios, including a widespread population lockdown for several quarters, seem to be fading, central banks remain very concerned about the situation. Fed leaders' new forecasts suggest negative consequences on inflation and the unemployment rate for several years, and signal that key rates should remain where they are until the end of 2022. At the press conference, Jerome Powell even said that "we're not even thinking about, thinking about raising rates," promising to use all of the Fed's tools proactively and aggressively to foster the recovery.
- ▶ The decision to purchase individual corporate bonds then reinforced this message. Many now think the Fed could resort to forward guidance or even target longer-term bond yields to make sure financial conditions stay highly accommodative.
- ▶ The Canadian economic situation was also characterized by a spectacular tumble by activity and employment in March and April. The onset of opening up suggests a rebound as of May, which should persist for the coming months. Like us, the Bank of Canada (BoC) is, however, predicting it will take years to get back to a situation as favourable as it was prior to the pandemic. The measures that were rapidly introduced by the BoC at the start of the crisis improved the functioning of financial markets, which allowed it to reduce the frequency of certain operations to ensure short-term liquidity. However, the BoC is promising to continue with massive Canadian government bond purchases until the recovery is well underway.
- ▶ Central banks overseas are also determined to pursue their efforts to foster a rapid rebound by economic activity. Recently, the Bank of England announced a £100B increase in its bond purchases.

INTEREST RATE FORECASTS

- ▶ The hoped-for economic rebound in many countries seems to be materializing, but activity and hiring levels will remain much lower than they were prior to the crisis. We think it will be 2022 before we return to pre-crisis real GDP levels. This will prompt the central banks to keep their key rates at their floor at least until late in 2022. In this context, we only expect bond yields to edge up as central banks, with the Fed in the lead, will not hesitate to use all the tools at their disposal to keep the slope from steepening sharply, which would risk curbing the economic recovery.

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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
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	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10

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	0.15	0.15	0.15	0.15	0.15	0.15	0.15
Federal bonds												
2-year	2.29	1.76	1.66	1.58	0.25	0.20	0.25	0.30	0.35	0.40	0.45	0.50
5-year	2.23	1.76	1.54	1.68	0.36	0.35	0.40	0.45	0.50	0.55	0.60	0.65
10-year	2.41	2.00	1.67	1.92	0.67	0.70	0.75	0.80	0.85	0.90	0.95	1.05
30-year	2.82	2.53	2.11	2.39	1.32	1.45	1.50	1.55	1.60	1.65	1.70	1.75
Yield curve slopes												
5-year - 3-month	-0.17	-0.36	-0.34	0.13	0.25	0.20	0.25	0.30	0.35	0.40	0.45	0.50
10-year - 2-year	0.13	0.24	0.01	0.34	0.41	0.50	0.50	0.50	0.50	0.50	0.50	0.55
30-year - 3-month	0.42	0.41	0.23	0.84	1.21	1.30	1.35	1.40	1.45	1.50	1.55	1.60
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	0.30	0.35	0.40	0.45	0.50	0.55	0.60
5-year	1.52	1.39	1.40	1.68	0.60	0.40	0.45	0.50	0.55	0.60	0.65	0.70
10-year	1.62	1.46	1.37	1.70	0.71	0.55	0.60	0.70	0.75	0.80	0.85	0.95
30-year	1.90	1.68	1.53	1.76	1.32	1.10	1.15	1.25	1.30	1.40	1.45	1.50
Yield curve slopes												
5-year - 3-month	-0.15	-0.27	-0.25	0.02	0.39	0.20	0.25	0.30	0.30	0.35	0.40	0.45
10-year - 2-year	0.07	-0.01	-0.21	0.01	0.29	0.25	0.25	0.30	0.30	0.30	0.30	0.35
30-year - 3-month	0.23	0.02	-0.12	0.10	1.11	0.90	0.95	1.05	1.05	1.15	1.20	1.25
Yield spreads (Canada—United States)												
3-month	-0.73	-0.46	-0.23	0.11	0.10	0.05	0.05	0.05	0.10	0.10	0.10	0.10
2-year	-0.74	-0.29	-0.08	0.11	0.17	0.10	0.10	0.10	0.10	0.10	0.10	0.10
5-year	-0.71	-0.37	-0.14	0.00	0.24	0.05	0.05	0.05	0.05	0.05	0.05	0.05
10-year	-0.79	-0.54	-0.30	-0.22	0.04	-0.15	-0.15	-0.10	-0.10	-0.10	-0.10	-0.10
30-year	-0.92	-0.85	-0.58	-0.63	0.00	-0.35	-0.35	-0.30	-0.30	-0.25	-0.25	-0.25

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
26	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
8	Bank of Korea	s.q.	0.75
15	Bank of Canada*	s.q.	0.25
21	Bank of Mexico	-50 b.p.	6.00
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	-50 b.p.	5.50
27	Bank of Korea	-25 b.p.	0.50
June			
2	Reserve Bank of Australia	s.q.	0.25
3	Bank of Canada	s.q.	0.25
4	European Central Bank	s.q.	0.00
10	Federal Reserve	s.q.	0.25
15	Bank of Japan	s.q.	-0.10
17	Bank of Brazil	-75 b.p.	2.25
18	Bank of England	s.q.	0.10
18	Bank of Norway	s.q.	0.00
18	Swiss National Bank	s.q.	-0.75
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*		
15	Bank of Japan		
16	European Central Bank		
16	Bank of Korea		
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.