

THE YIELD CURVE

Second Wave of COVID-19 Will Prompt Central Banks to Maintain Highly Accommodative Monetary Policies

HIGHLIGHTS

- ▶ Movements in North American bond yields have been limited in the last few months. Throughout the third quarter, 10-year U.S. federal bond yields hovered between 0.50% and 0.75%. Meanwhile, Canadian 10-year yields stayed approximately 10 basis points below U.S. yields. Shorter-term yields were even more stable. However, long-term U.S. yields have recently felt a bit more upward pressure, particularly when the door appears to be opening for a new fiscal stimulus plan.
- ▶ Both the Federal Reserve (Fed) and the Bank of Canada (BoC) have promised to keep key rates at their effective lower bound until the economy has fully recovered, which could take several years. In fact, the latest forecasts by Fed leaders suggest that key rates will remain stable until the end of 2023, despite fairly positive developments to the economic situation. The Fed also announced that it was adopting average inflation targeting, signalling that it would tolerate inflation above 2% following the current period of low inflation. It also confirmed an expansionary bias by explaining that its monetary policy would only react to shortfalls to full employment.
- ▶ The initial rebound in economic activity following the spring lockdown clearly exceeded the expectations of North American monetary authorities. However, the recent surge in COVID-19 cases in several countries, including Canada, which is forcing many governments to reinstate some lockdown measures, should curb the recovery's momentum in the fourth quarter. The political situation in the United States, which is hindering government assistance for households and businesses, and the possibility that the election results on November 3 will be contested, also pose major risks to the economic outlook. As inflationary pressure remains very low, the Fed and the BoC will thus remain highly vigilant and continue their large-scale bond purchases in the coming months.
- ▶ The rise in COVID-19 cases in Europe is particularly worrisome. This will spur the European Central Bank and the Bank of England to maintain ultra-accommodative monetary policies, particularly as European currencies are still fairly strong compared to the U.S. dollar and Brexit is far from being resolved. The Bank of England even appears to be more seriously considering resorting to negative key rates, if it becomes necessary.

INTEREST RATE FORECASTS

- ▶ Our interest rate scenarios still hold overall. No changes to North American key rates are anticipated for the next few years as central banks are aiming to return to favourable pre-pandemic conditions as quickly as possible, particularly for the labour market.
- ▶ Fears over public finances and the supply of bonds may persist, but the effects on bond yields should be limited as long as the Fed and the BoC continue their large-scale bond purchases. We're unlikely to see a halt to these purchases or a true upward trend in bond yields before a few quarters, and then only if pandemic-related risks subside significantly.

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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	Q2	Q3	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	Q2	Q3	Q4f	Q1f	Q2f	Q3f	Q4f
UNITED STATES												
Treasury bills												
3-month	2.40	2.12	1.88	1.55	0.11	0.16	0.10	0.10	0.10	0.10	0.15	0.15
Federal bonds												
2-year	2.29	1.76	1.66	1.58	0.25	0.17	0.13	0.15	0.15	0.20	0.25	0.35
5-year	2.23	1.76	1.54	1.68	0.36	0.28	0.27	0.30	0.30	0.35	0.40	0.50
10-year	2.41	2.00	1.67	1.92	0.67	0.65	0.68	0.70	0.70	0.75	0.80	0.90
30-year	2.82	2.53	2.11	2.39	1.32	1.41	1.45	1.50	1.50	1.50	1.55	1.60
Yield curve slopes												
5-year - 3-month	-0.17	-0.36	-0.34	0.13	0.25	0.12	0.17	0.20	0.20	0.25	0.25	0.35
10-year - 2-year	0.13	0.24	0.01	0.34	0.41	0.49	0.55	0.55	0.55	0.55	0.55	0.55
30-year - 3-month	0.42	0.41	0.23	0.84	1.21	1.25	1.35	1.40	1.40	1.40	1.40	1.45
CANADA												
Treasury bills												
3-month	1.67	1.66	1.65	1.66	0.21	0.20	0.12	0.20	0.20	0.20	0.25	0.25
Federal bonds												
2-year	1.55	1.47	1.58	1.69	0.42	0.28	0.25	0.30	0.30	0.30	0.35	0.40
5-year	1.52	1.39	1.40	1.68	0.60	0.36	0.36	0.40	0.40	0.40	0.45	0.50
10-year	1.62	1.46	1.37	1.70	0.71	0.52	0.57	0.60	0.65	0.70	0.75	0.80
30-year	1.90	1.68	1.53	1.76	1.32	0.99	1.11	1.15	1.15	1.15	1.20	1.25
Yield curve slopes												
5-year - 3-month	-0.15	-0.27	-0.25	0.02	0.39	0.16	0.24	0.20	0.20	0.20	0.20	0.25
10-year - 2-year	0.07	-0.01	-0.21	0.01	0.29	0.24	0.32	0.30	0.35	0.40	0.40	0.40
30-year - 3-month	0.23	0.02	-0.12	0.10	1.11	0.79	0.99	0.95	0.95	0.95	0.95	1.00
Yield spreads (Canada—United States)												
3-month	-0.73	-0.46	-0.23	0.11	0.10	0.04	0.02	0.10	0.10	0.10	0.10	0.10
2-year	-0.74	-0.29	-0.08	0.11	0.17	0.11	0.12	0.15	0.15	0.10	0.10	0.05
5-year	-0.71	-0.37	-0.14	0.00	0.24	0.08	0.09	0.10	0.10	0.05	0.05	0.00
10-year	-0.79	-0.54	-0.30	-0.22	0.04	-0.13	-0.11	-0.10	-0.05	-0.05	-0.05	-0.10
30-year	-0.92	-0.85	-0.58	-0.63	0.00	-0.42	-0.34	-0.35	-0.35	-0.35	-0.35	-0.35

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	s.q.	0,25
25	Bank of Mexico	-50 b.p.	5,00

Date	Central banks	Decision	Rate
July			
1	Bank of Sweden	s.q.	0,00
7	Reserve Bank of Australia	s.q.	0,25
14	Bank of Japan	s.q.	-0,10
15	Bank of Korea	s.q.	0,50
15	Bank of Canada*	s.q.	0,25
16	European Central Bank	s.q.	0,00
29	Federal Reserve	s.q.	0,25
August			
4	Reserve Bank of Australia	s.q.	0,25
5	Bank of Brazil	-25 b.p.	2,00
6	Bank of England	s.q.	0,10
11	Reserve Bank of New Zealand	s.q.	0,25
13	Bank of Mexico	-50 b.p.	4,50
20	Bank of Norway	s.q.	0,00
26	Bank of Korea	s.q.	0,50
September			
1	Reserve Bank of Australia	s.q.	0,25
9	Bank of Canada	s.q.	0,25
10	European Central Bank	s.q.	0,00
16	Bank of Brazil	s.q.	2,00
16	Bank of Japan	s.q.	-0,10
16	Federal Reserve	s.q.	0,25
17	Bank of England	s.q.	0,10
22	Reserve Bank of New Zealand	s.q.	0,25
22	Bank of Sweden	s.q.	0,00
24	Bank of Norway	s.q.	0,00
24	Bank of Mexico	-25 b.p.	4,25
24	Swiss National Bank	s.q.	-0,75
October			
6	Reserve Bank of Australia	s.q.	0,25
13	Bank of Korea	s.q.	0,50
28	Bank of Brazil		
28	Bank of Canada*		
28	Bank of Japan		
29	European Central Bank		
November			
3	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		
25	Bank of Korea		
26	Bank of Sweden		
December			
1	Reserve Bank of Australia		
9	Bank of Brazil		
9	Bank of Canada		
10	European Central Bank		
16	Federal Reserve		
17	Bank of England		
17	Bank of Norway		
17	Bank of Japan		
17	Bank of Mexico		
17	Swiss National Bank		

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; ** To be determined.