

Yield Outlook

Global central banks have started normalising monetary policy – pulling long yields up

December's Yield Outlook is an abridged version following the series of central bank meetings this week. The full, unabridged publication will return in mid-January.

The overriding conclusion from the series of important central bank meetings this week is clear: Central banks are increasingly concerned that the current surge in inflation is so pronounced that it can no longer be described as merely transitory and that we risk it gaining traction and becoming more persistent.



Initial US rate hike drawing closer as tapering of bond purchases speeds up

The US central bank, the Fed, is leading the charge after deciding at its meeting on Wednesday evening to scale back its bond purchasing programme by a further USD15bn a month to USD30bn a month. This means bond purchases are set to cease by March next year. The accelerated tapering process is in part a sign that the Fed no longer sees a need for the same degree of monetary policy stimulation as previously, but equally important, the decision clearly signals that any future rate hikes could materialise earlier than expected. Fed Chair Powell also added at the meeting that an extended intermission between the phasing out of QE and the first rate hike was unnecessary. We now expect the Fed to initially hike in May 2022 followed by a further hike in September and then December. We anticipate that these quarterly rate hikes will continue throughout 2023, taking the upper limit of the federal funds rate – after no less than 7 rate increases – to 2% by the end of 2023. Our baseline is a final rate hike to 2.25% in 2024.

The market is currently expecting less tightening, pricing a little above 2 rate hikes of 25bp each into the US yield curve in 2022 and two hikes in 2023.

Links

- [Forecast table](#)
- [Forecast Euro area](#)
- [Forecast USA](#)
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Central bank policy rates

Country	Spot	+3m	+6m	+12m
USD	0.25	0.25	0.25	0.50
EUR	-0.50	-0.50	-0.50	-0.50
GBP	0.10	0.10	0.25	0.50
DKK	-0.60	-0.60	-0.60	-0.60
SEK	0.00	0.00	0.00	0.00
NOK	0.25	0.50	0.75	1.00

10Y government bond yields

Country	Spot	+3m	+6m	+12m
USD	1.54	1.70	1.80	2.00
EUR	-0.28	-0.05	0.10	0.25
GBP	0.89	1.10	1.30	1.40
DKK	-0.01	0.20	0.35	0.50
SEK	0.28	0.40	0.45	0.60
NOK	1.66	1.80	1.85	2.00

Note: EUR = Germany

10Y swap rates

Country	Spot	+3m	+6m	+12m
USD	1.59	1.75	1.85	2.05
EUR	0.16	0.35	0.50	0.65
GBP	1.18	1.35	1.55	1.65
DKK	0.41	0.60	0.75	0.90
SEK	0.95	1.00	0.95	1.05
NOK	1.89	2.05	2.10	2.25

Source (all three tables): Danske Bank

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The ‘dots’ from Fed members show they expect rates to be raised three times on average in 2022 and another three times in 2023. This represents a shift from September, when the dots signalled only a 50/50 chance of a single rate hike in 2022.

We therefore expect that monetary policy will tend to not only push short but also medium and long-term US yields up in the course of 2022. We also expect the 2Y-10Y yield curve to flatten – the textbook response in a tightening cycle. Our expectation is that the market in 2022 will be heavily focused on the endpoint for interest rates when the Fed is finished tightening. Our assumption is that a neutral rate would be required, though we certainly cannot rule out the need for a contractionary monetary policy given the high rate of inflation.

What could be the endpoint for the fed funds rate?

The market is pricing the endpoint for the fed funds rate at around 1.5%. We have used a 5Y1Y (1Y interest rate in 5 years) OIS rate plus 15bp as an indicator of the market pricing of the neutral rate or endpoint. The market priced the endpoint or ‘final rate’ at more than 2% back in April. In 2022, we expect to see fresh repricing of the endpoint for the fed funds rate as the labour market continues to tighten. However, it remains unclear whether or not the pandemic has shifted the neutral rate of interest (r^*).

Should the market begin to price a higher end rate or neutral real interest rate (r^*), that would tend to push long nominal US yields higher in 2022.

Overall, we continue to expect 10Y US Treasury yields to increase to 2% by the end of 2022.

ECB scales back bond purchases

At its meeting on 16 December, the ECB announced that net purchases in its Pandemic Emergency Purchasing Programme (PEPP) would stop as expected by the end of Q1 22, and that it would be cut in Q1 next year. To avoid an unduly sharp reduction in bond purchases in Q2 22, the ECB decided to temporarily ramp up the ‘old’ APP purchasing programme from EUR20bn to EUR40bn per month in Q2 22 and EUR30bn in Q3 22, before cutting back to the original level of EUR20bn per month. Note that reinvestments stemming from PEPP will continue in the coming years – which adds up to a considerable amount given the scale of the programme. Overall, however, the announcement means that, in contrast to both 2020 and 2021, the ECB will not buy up the entire net issuance of new bonds in 2022. As the market starts to look ahead to 2023, the volume of bonds the market has to absorb will increase further, which could become a theme, particularly in H2 22.

The ECB and President Lagarde used the press conference to stress that an increase in policy rates was very unlikely in 2022. Indeed, the temporary increase in APP bond purchases was a good opportunity to underline this point, as a rate hike alongside extraordinary buybacks is rather improbable.

Nonetheless, the lesson of 2021 is that we need to be a little cautious about basing our own expectations on what the central banks say about the future. Remember that the US Fed was describing inflation as transitory just a few months ago. Likewise, the ECB may well be wrong-footed on inflation – and given a core inflation forecast of 1.9% for 2022, little more would be required to ruffle the feathers of the ECB’s hawks. All in all, however, we expect the ECB to keep policy rates unchanged in 2022, in part because European wage

The 2Y-10Y US yield curve has flattened, bp



Note: Past performance is not a reliable guide to future returns. Source: Macrobond Financial

5Y1Y USD OIS rate indicates a fed funds rate of 1.5% in 5 years

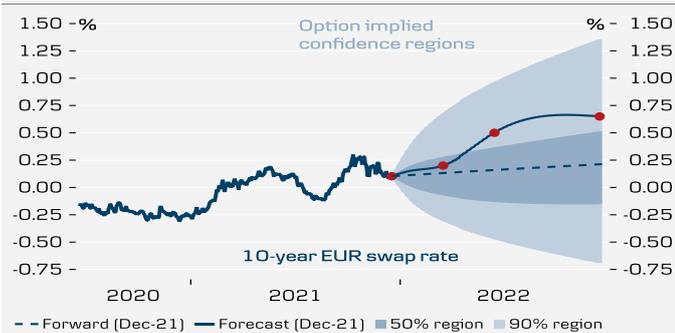


Note: Past performance is not a reliable guide to future returns. Source: Danske Bank

growth is set to remain limited. That being said, the ECB beginning to raise interest rates in 2023 could well be on the cards. As before, our reasoning is that the market is likely to increasingly price rate hikes into the curve in 2023 and 2024, and this would tend to push policy-sensitive yields up in the 2Y-5Y segment.

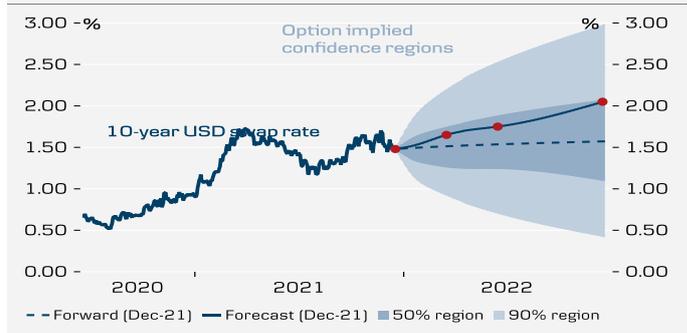
We expect the 10Y Bund yield to increase to 0.2% by the end of 2022.

Forecast: 10Y EUR swap rates



Note: Past performance is not a reliable guide to future returns.
Source: Danske Bank

Forecast: 10Y USD swap rates



Note: Past performance is not a reliable guide to future returns.
Source: Danske Bank

Forecast*

	Horizon	Policy rate	3m x1bor	2-yr swap	5-yr swap	10-yr swap	2-yr gov	5-yr gov	10-yr gov
USD	Spot	0.25	0.22	0.86	1.27	1.48	0.63	1.18	1.42
	+3m	0.25	0.24	1.10	1.45	1.65	0.90	1.35	1.60
	+6m	0.50	0.49	1.20	1.55	1.75	1.00	1.45	1.70
	+12m	1.00	1.03	1.65	1.90	2.05	1.45	1.80	2.00
EUR*	Spot	-0.50	-0.59	-0.36	-0.13	0.10	-0.70	-0.59	-0.37
	+3m	-0.50	-0.54	-0.30	0.05	0.20	-0.65	-0.40	-0.20
	+6m	-0.50	-0.54	-0.25	0.25	0.50	-0.60	-0.20	0.10
	+12m	-0.50	-0.54	-0.15	0.35	0.65	-0.50	-0.10	0.20
GBP	Spot	0.25	0.10	1.07	1.10	1.00	0.51	0.61	0.76
	+3m	0.10	0.22	1.10	1.20	1.15	0.65	0.70	0.90
	+6m	0.25	0.42	1.15	1.40	1.25	0.70	0.90	1.00
	+12m	0.50	0.67	1.45	1.50	1.45	1.00	1.00	1.20
DKK	Spot	-0.60	-0.27	-0.08	0.12	0.33	-0.60	-0.33	-0.10
	+3m	-0.60	-0.28	0.00	0.30	0.45	-0.55	-0.15	0.05
	+6m	-0.60	-0.28	0.03	0.50	0.75	-0.50	0.05	0.35
	+12m	-0.60	-0.28	0.13	0.60	0.90	-0.40	0.15	0.45
SEK	Spot	0.00	-0.11	0.22	0.58	0.81	-0.22	-0.03	0.11
	+3m	0.00	-0.03	0.20	0.65	1.00	-0.20	0.10	0.40
	+6m	0.00	-0.03	0.20	0.60	0.95	-0.20	0.15	0.45
	+12m	0.00	-0.03	0.20	0.70	1.05	-0.15	0.25	0.60
NOK	Spot	0.50	0.83	1.49	1.73	1.75	1.28	1.49	1.54
	+3m	0.50	1.17	1.60	1.80	2.02	1.30	1.50	1.80
	+6m	1.00	1.34	1.70	2.00	2.10	1.40	1.70	1.85
	+12m	1.25	1.70	2.05	2.10	2.25	1.75	1.80	2.00

* German government bond yields and euro swap rates
Source: Danske Bank

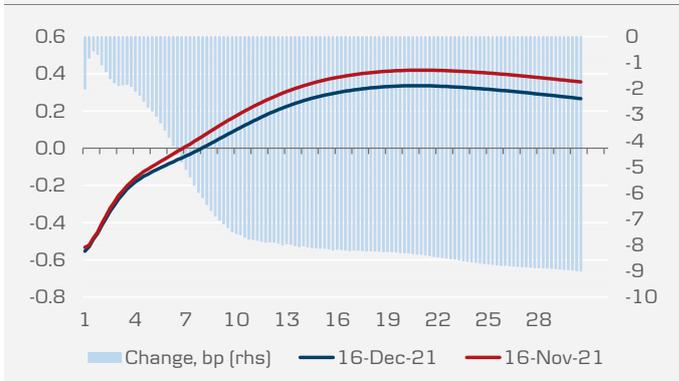
Eurozone forecast

EUR forecast summary

16/12/2021	--- Forecast ---				--- Fcst vs Fwd in bp ---		
EUR	Spot	+3m	+6m	+12m	+3m	+6m	+12m
<u>Money Market</u>							
Refi	0.00	0.00	0.00	0.00	-	-	-
Deposit	-0.50	-0.50	-0.50	-0.50	-	-	-
3M	-0.60	-0.54	-0.54	-0.54	0	-5	-19
6M	-0.55	-0.52	-0.52	-0.52	-3	-9	-25
<u>Government Bonds</u>							
2-year	-0.68	-0.65	-0.60	-0.50	-	-	-
5-year	-0.58	-0.40	-0.20	-0.10	-	-	-
10-year	-0.36	-0.20	0.10	0.20	-	-	-
<u>Swap rates</u>							
2-year	-0.34	-0.30	-0.25	-0.15	-3	-5	-6
5-year	-0.10	0.05	0.25	0.35	12	9	33
10-year	0.12	0.20	0.50	0.65	5	32	42

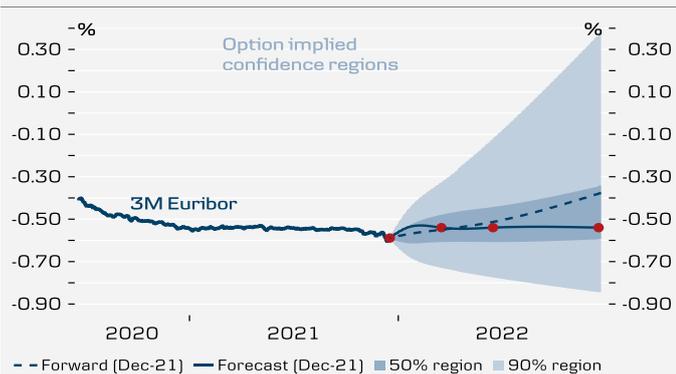
Source: Danske Bank

1M change in EUR swap rates



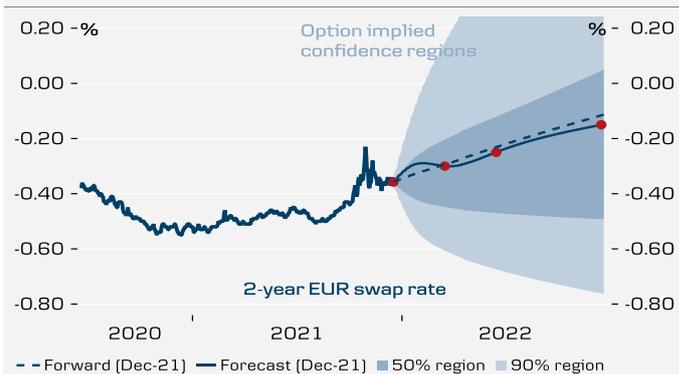
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

3M Euribor rates



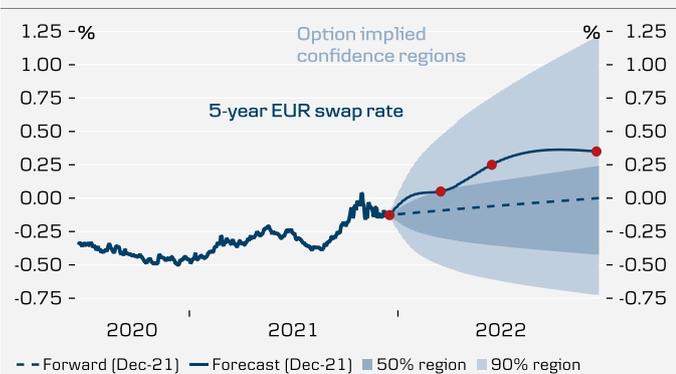
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Source: Danske Bank

2Y EUR swap rates



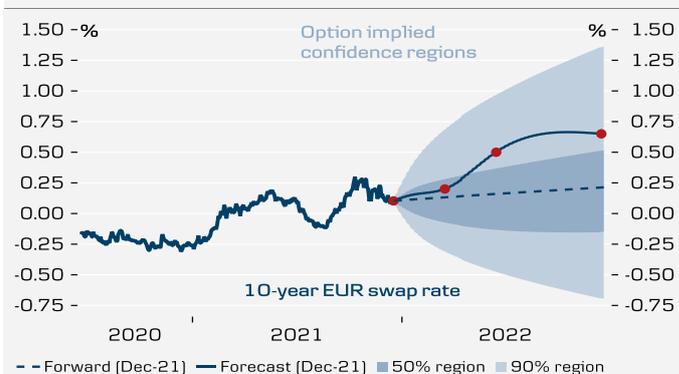
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Source: Danske Bank

5Y EUR swap rates



Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

10Y EUR swap rates



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Source: Danske Bank

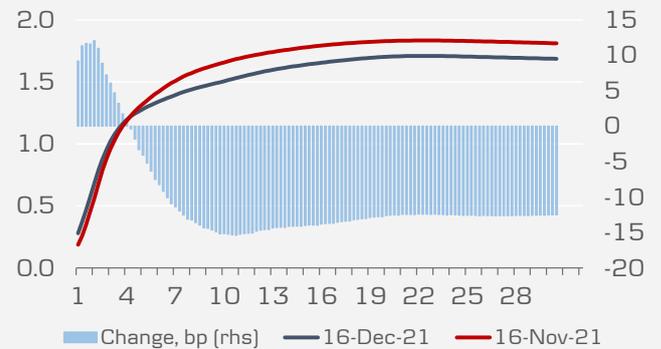
US forecast

USD forecast summary

16/12/2021	--- Forecast ---				--- Fcst vs Fwd in bp ---		
USD	Spot	+3m	+6m	+12m	+3m	+6m	+12m
<u>Money Market</u>							
Fed Funds	0.25	0.25	0.50	1.00	-	-	-
3M	0.21	0.23	0.49	1.02	-11	-8	2
<u>Government Bonds</u>							
2-year	0.64	0.90	1.00	1.45	-	-	-
5-year	1.22	1.35	1.45	1.80	-	-	-
10-year	1.45	1.60	1.70	2.00	-	-	-
<u>Swap rates</u>							
2-year	0.87	1.10	1.20	1.65	5	-1	20
5-year	1.31	1.45	1.55	1.90	7	10	35
10-year	1.52	1.65	1.75	2.05	9	14	38

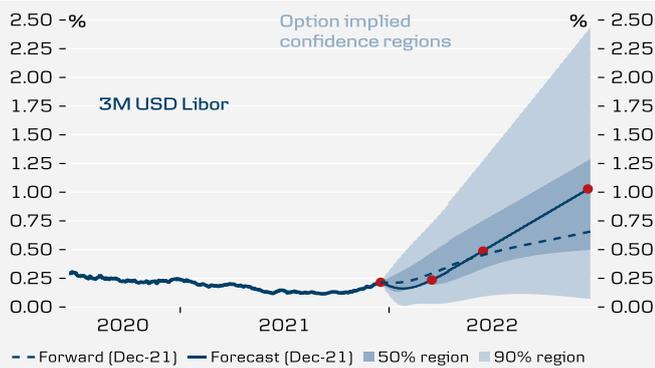
Source: Danske Bank

1M change in USD swap (3M) rates



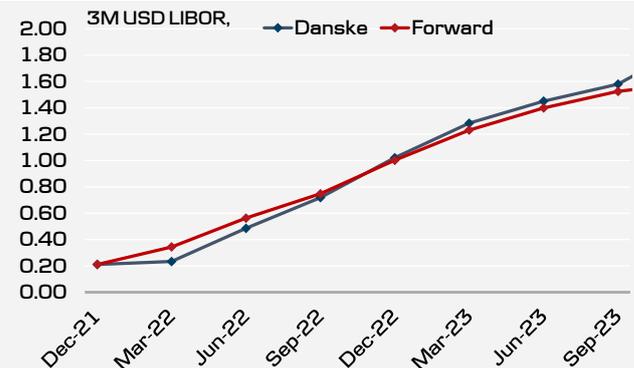
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3M USD Libor rates



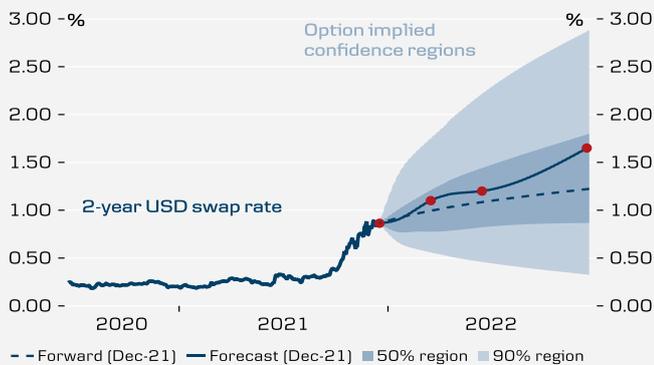
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Source: Danske Bank

Danske Bank forecast and forwards



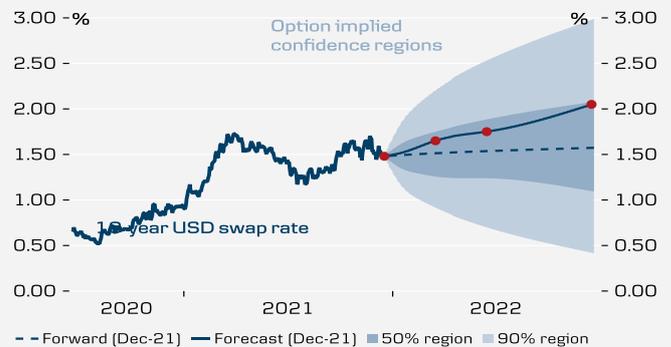
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

2Y USD swap rates



Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

10Y USD swap rates



Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

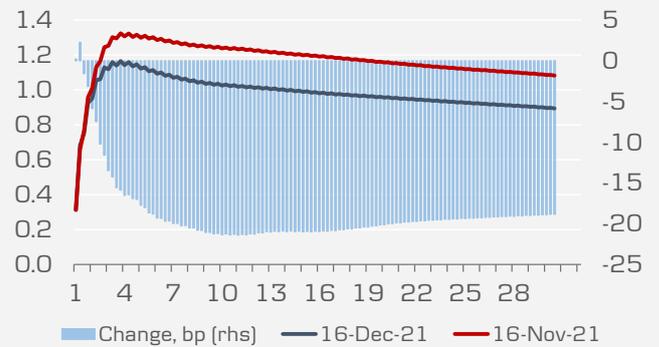
UK forecast

GBP forecast summary

16/12/2021	--- Forecast ---				--- Fcst vs Fwd in bp ---		
GBP	Spot	+3m	+6m	+12m	+3m	+6m	+12m
<u>Money Market</u>							
Repo	0.10	0.1	0.25	0.5	-	-	-
3M	0.09	0.22	0.42	0.67	-43	-53	-51
<u>Government Bonds</u>							
2-year	0.50	0.65	0.70	1.00	11	8	33
5-year	0.602	0.7	0.9	1	13	33	40
10-year	0.75	0.90	1.00	1.20	11	18	33
<u>Swap rates</u>							
2-year	1.06	1.10	1.15	1.45	-15	-17	12
5-year	1.10	1.20	1.40	1.50	4	23	46
10-year	1.02	1.15	1.25	1.45	10	20	41

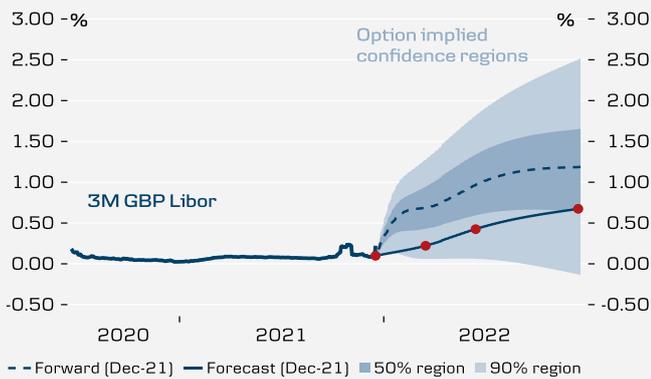
Source: Danske Bank

1M change in GBP swap (6M) rates



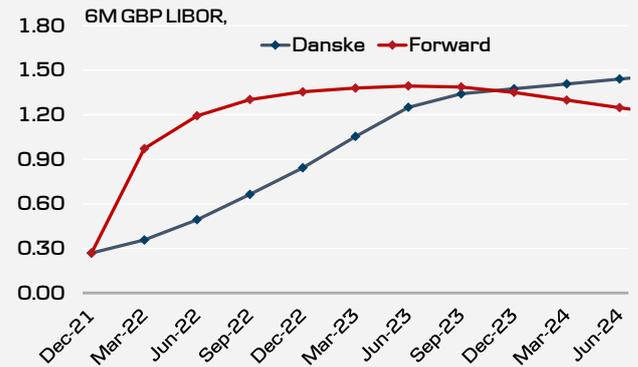
Note: Past performance is not a reliable guide to future returns
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3M GBP Libor rates



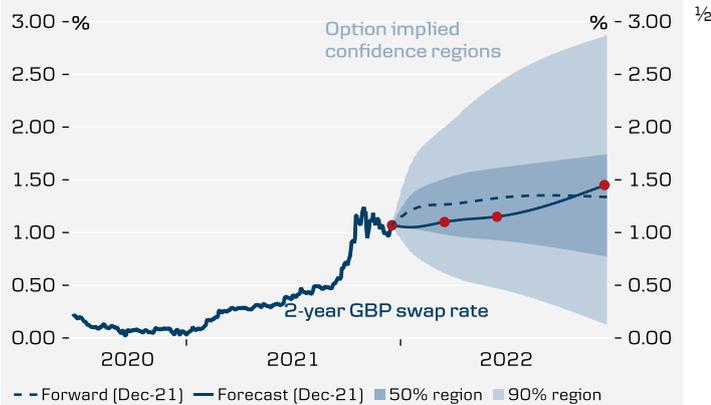
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Source: Danske Bank

Danske Bank forecast and forwards



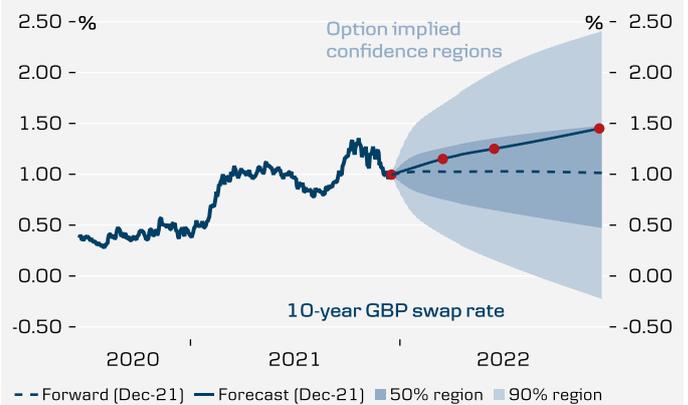
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Source: Danske Bank

2Y UK swap rates



Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

10Y UK swap rates



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Source: Danske Bank

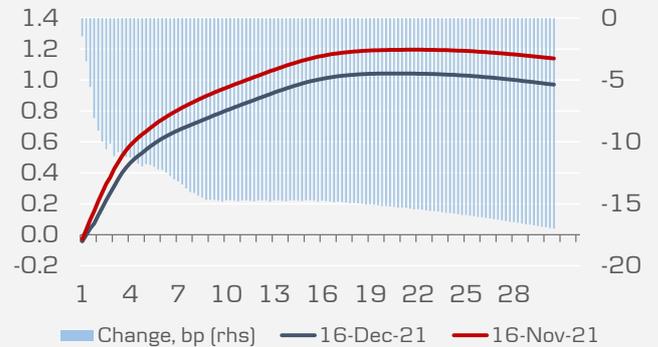
Sweden forecast

SEK forecast summary

16/12/2021	Spot	--- Forecast ---			--- Fcst vs Fwd in bp ---		
SEK		+3m	+6m	+12m	+3m	+6m	+12m
Money market							
Repo	0.00	0.00	0.00	0.00	-	-	-
3M	-0.11	-0.03	-0.03	-0.03	-6	-11	-24
Government bonds							
2-year	-0.23	-0.20	-0.20	-0.15	-	-	-
5-year	-0.03	0.10	0.15	0.25	-	-	-
10-year	0.11	0.40	0.45	0.60	-	-	-
Swap rates							
2-year	0.22	0.20	0.20	0.20	-12	-21	-38
5-year	0.59	0.65	0.60	0.70	1	-9	-7
10-year	0.82	1.00	0.95	1.05	14	6	10

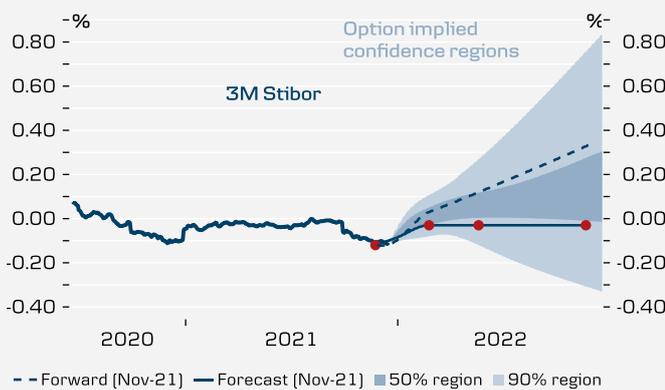
Source: Danske Bank

1M change in SEK swap (3M) rates



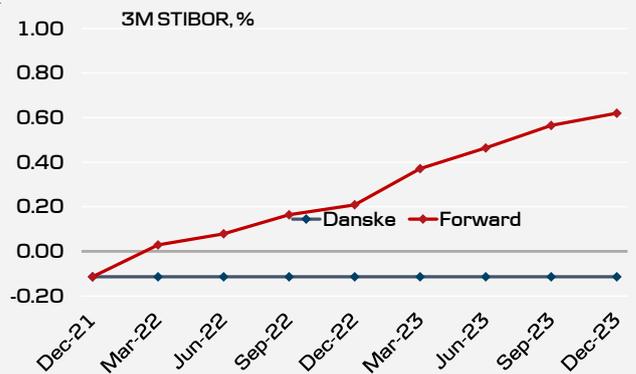
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

3M Stibor rates



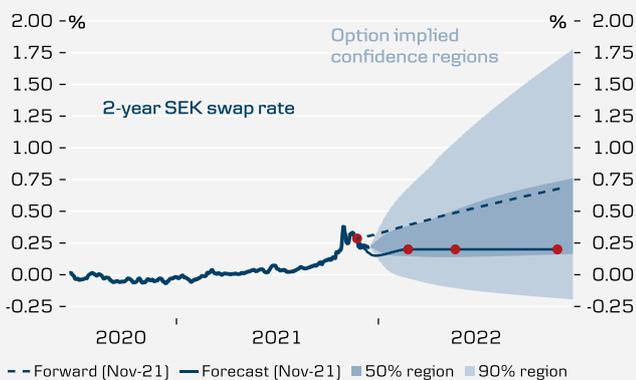
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Source: Danske Bank

Danske Bank forecast and forwards



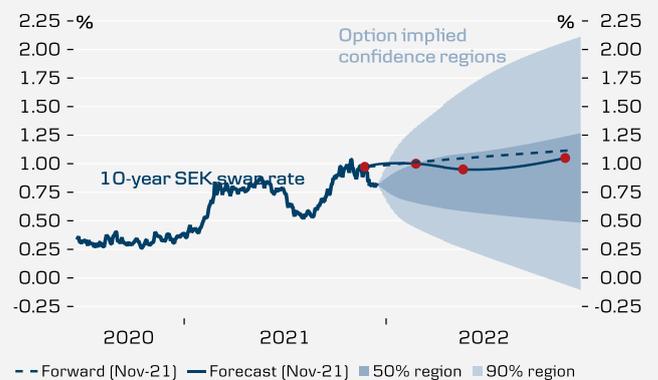
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

2Y SEK swap rates



Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

10Y SEK swap rates



Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

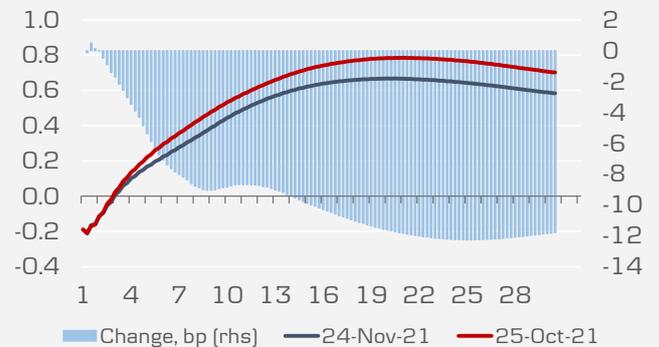
Denmark forecast

DKK forecast summary

24/11/2021	--- Forecast ---				--- Fcst vs Fwd in bp ---		
DKK	Spot	+3m	+6m	+12m	+3m	+6m	+12m
<u>Money Market</u>							
CD	-0.60	-0.60	-0.60	-0.60	-	-	-
Repo	-0.45	-0.45	-0.45	-0.45	-	-	-
3M	-0.28	-0.28	-0.28	-0.28	-1	-3	-15
6M	-0.19	-0.18	-0.18	-0.18	0	-5	-17
<u>Government bonds</u>							
2-year	-0.64	-0.55	-0.50	-0.40	-	-	-
5-year	-0.26	-0.28	-0.23	0.02	-	-	-
10-year	0.05	0.20	0.35	0.50	-	-	-
<u>Swap rates</u>							
2-year	-0.05	0.05	0.08	0.18	5	2	1
5-year	0.19	0.37	0.40	0.65	14	14	32
10-year	0.46	0.60	0.75	0.90	11	23	32

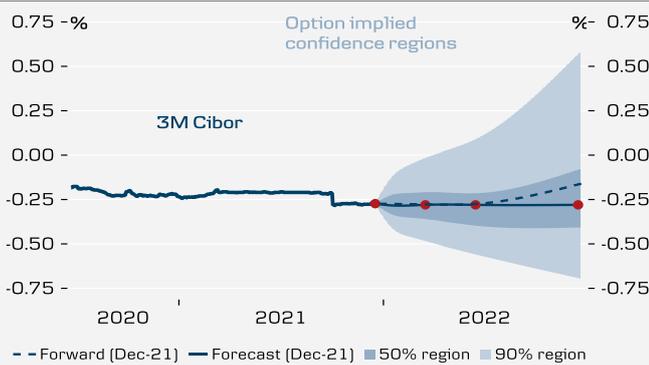
Source: Danske Bank

1M change in DKK swap (6M) rates



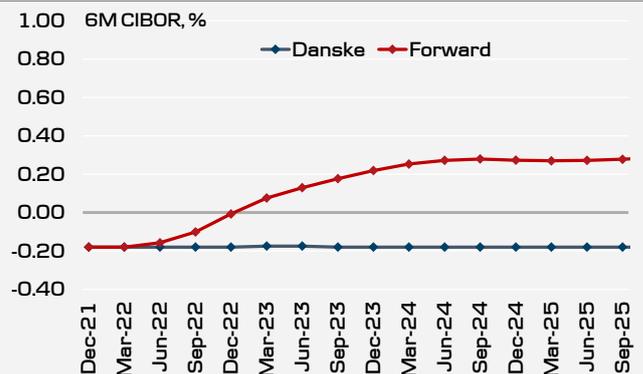
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3M Cibur rates



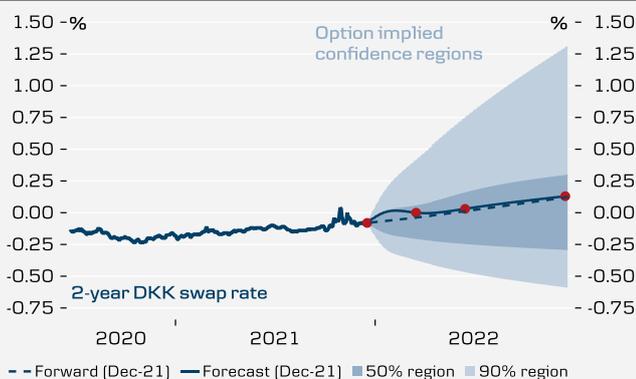
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Danske Bank forecast and forwards



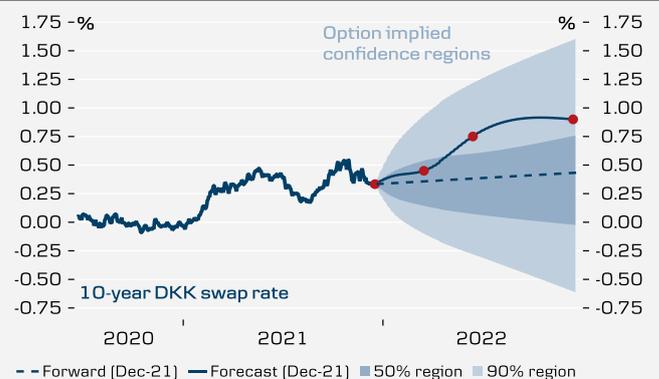
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Source: Danske Bank

2Y DKK swap rates



Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

10Y DKK swap rates



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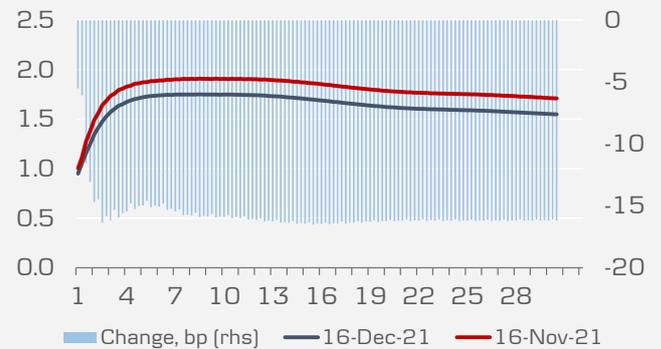
Norway forecast

NOK forecast summary

16/12/2021 NOK	--- Forecast ---				--- Fcst vs Fwd in bp ---		
	Spot	+3m	+6m	+12m	+3m	+6m	+12m
<u>Money market</u>							
Deposit	0.50	0.75	1.00	1.25	-	-	-
3M	0.75	1.16	1.34	1.69	13	11	11
6M	0.90	1.30	1.43	1.82	11	6	11
<u>Government bonds</u>							
2-year	1.32	1.30	1.40	1.75	-	-	-
5-year	1.51	1.50	1.70	1.80	-	-	-
10-year	1.56	1.80	1.85	2.00	-	-	-
<u>Swap rates</u>							
2-year	1.48	1.60	1.70	2.05	-2	-3	17
5-year	1.73	1.80	2.00	2.10	1	18	23
10-year	1.75	2.02	2.10	2.25	25	31	44

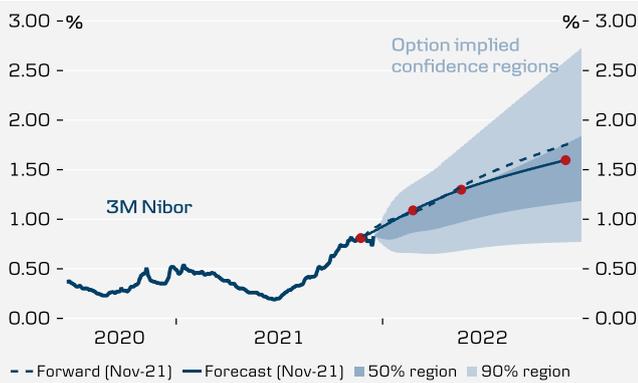
Source: Danske Bank

1M change in NOK swap (6M) rates



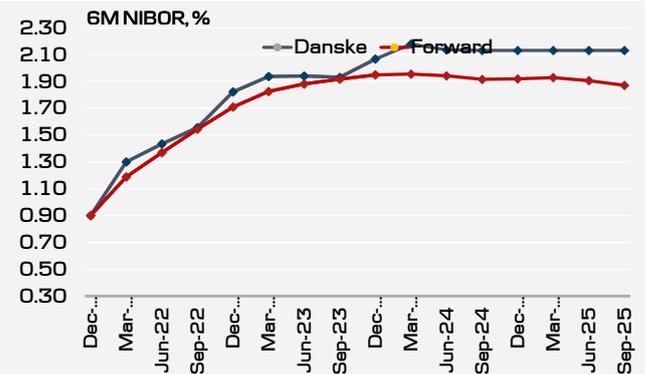
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

3M Nibor rates



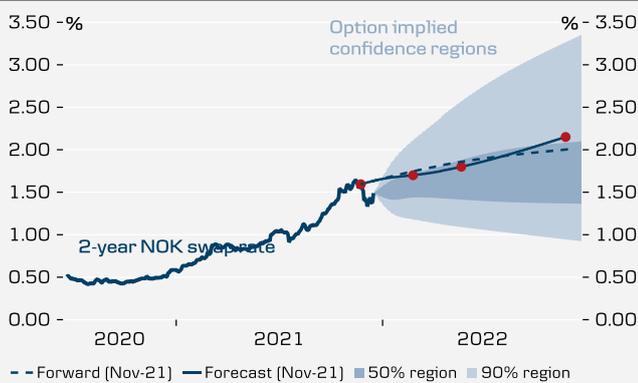
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

Danske Bank forecast and forwards



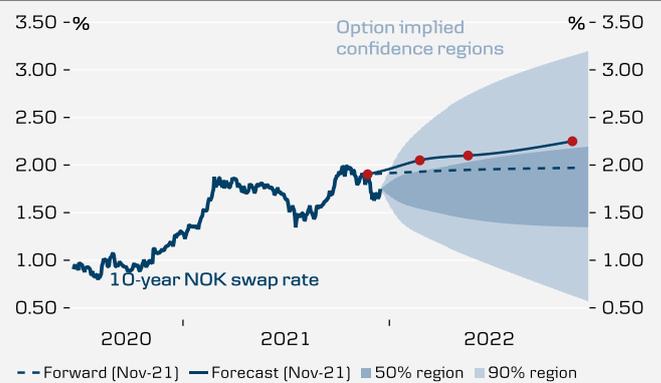
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

2Y NOK swap rates



Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

10Y NOK swap rates



Note: Past performance is not a reliable guide to future returns
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