

Yield Outlook

Uncertainty about US banking sector clouds rate outlook

Rates markets have been heavily impacted by the collapse of the SVB and other US banks, causing severe liquidity distress in recent days. US institutions have responded relatively quickly, not least, the Federal Reserve, which has provided a USD25bn 1y liquidity facility to contain the problem at an attractive 1y USD OIS+10bp. The knee-jerk reaction was a solid flight-to-quality in core yields (Germany and the US) on the back of a significant repricing of central bank expectations and steeper curves. While we are still to see the full scale of the US banking sector problems, the sector is probably much more robust than in 2008, as US Treasury Secretary Yellen has also pointed out.

Just days ahead of the financial market stress, Fed chair Powell in response to the still very tight labour market and resilient economic activity, said that the Fed might need to re-accelerate the pace of rate hikes and that rates were ‘likely to be higher’ than previously anticipated. Powell’s upbeat assessment confirmed what was already priced by markets. During the period from the publication of the February edition of *Yield Outlook* 1m ago until the financial turbulence erupted, we saw central bank pricing rise 40bp and 50bp to 5.64% and 4.06%, respectively, for the Federal Reserve and the ECB. During the same period, markets gradually pushed out the point when peak policy rates would likely be reached. At a certain point, markets priced the ECB peak policy rate to be reached only in February next year. That said, during the past week, we have seen a significant downward repricing of the policy rates peak to 4.75% and 3.2%, respectively, for the Fed and the ECB.

On the back of the economic resilience and still accelerating underlying inflation in Europe, we also revised our call for ECB policy rates earlier this month. We outlined our expectation of a 50bp rate hike in both March and May followed by 25bp in June and July, bringing the peak policy rate to 4%. Looking slightly beyond our projected horizon, we still anticipate the ECB to cut rates starting in summer 2024 – not with the aim of easing policy but to keep it broadly constant as inflation and inflation expectations decline (see also *ECB Preview - Higher for longer - now seen at 4%*, 2 March. Yesterday, the ECB hiked rates 50bp as expected but gave no guidance for May, while repeating the data dependency (see also *Flash ECB Review - 50bp hike, but no guidance for May*, 16 March).

Unusually wide ranges prevail at this point in time as the banking turmoil continues, which is also reflected in realised volatility in rates markets, and the outcome space is very wide. While markets have changed narrative from a recession to a no landing scenario during the past month, markets are now also faced with the uncertainty about the US banking sector, and risks of no further tightening as long as the turmoil prevails have been noted. As a result, the projections in this piece represent the baseline scenario of how we see rates evolve. However, with the unusually large outcome space, we see 10y German benchmark yields in a 1.75-3.25% range in the coming 3m. Markets are pricing 10y EUR swap rates between 1.8% and 4.06% in 3 months’ time with a 90% probability.

While the risks are visible on the horizon, we note that the economy has proven resilient since the start of the year, with particularly labour markets remaining strong. Following the 517k new jobs in the US in February, the US added more than 300k in February. This is

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Central bank policy rates

Country	Spot	+3m	+6m	+12m
USD	4.75	5.25	5.25	5.25
EUR	3.00	3.75	4.00	4.00
GBP	4.00	4.25	4.25	4.00
DKK	2.60	3.35	3.60	3.60
SEK	3.00	3.75	4.25	4.00
NOK	2.75	3.25	3.25	3.00

10Y government bond yields

Country	Spot	+3m	+6m	+12m
USD	3.50	3.80	3.60	3.40
EUR	2.25	2.75	2.60	2.50
GBP	3.42	3.30	3.30	3.20
DKK	2.52	2.85	2.70	2.60
SEK	2.28	2.55	2.65	2.70
NOK	2.96	3.10	2.80	2.80

Note: EUR = Germany

10Y swap rates

Country	Spot	+3m	+6m	+12m
USD	3.56	3.85	3.65	3.45
EUR	2.94	3.25	3.10	2.90
GBP (OIS)	3.40	3.40	3.40	3.30
DKK	3.10	3.40	3.25	3.05
SEK	2.88	3.00	2.80	2.75
NOK	3.00	3.15	2.85	2.80

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

Source: Danske Bank for tables above

Director

Piet Haines Christiansen
+45 4514 1518
phai@danskebank.dk

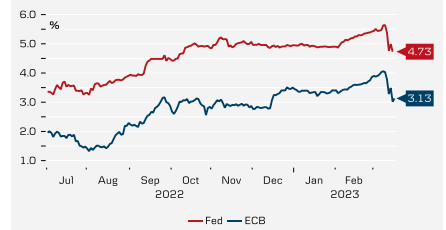
likely to maintain the tightening bias of major central banks in the absence of further escalation of the banking turmoil.

We expect rates to be close to peak levels, not least, in the US, but we see minor upside risks to European rates, as we expect the ECB to pause later than the Fed. The timing of the pause has historically served as a predictor of the decline in longer dated yields. On a 12M horizon, we see clear downside risks to global rates.

Market based inflation expectations set new highs during the past month but are now steady

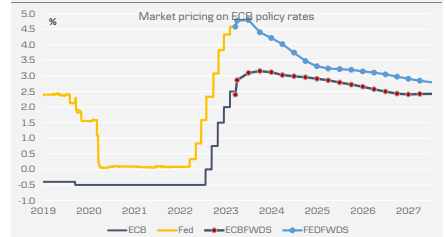
While the peak in headline inflation is firmly behind us, inflation forwards saw a brisk spike during the past month, with 5y5y EUR inflation shooting above its USD equivalent and peaking at 2.62%, but it is now back at 2.47%, which was the peak in summer 2022.

Market pricing of ECB and Fed peak policy rates



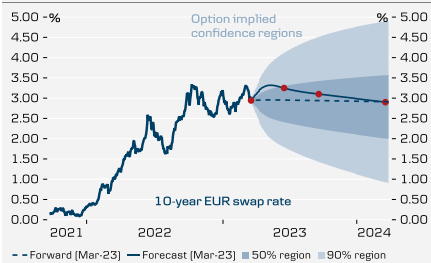
Source: Macrobond Financial and Danske Bank

Rate path trajectory



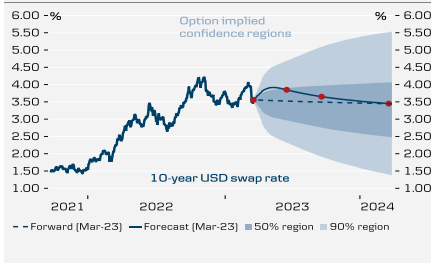
Source: Danske Bank

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

Forecasts

	Horizon	Policy rate	3m xlbbr	2-yr swap	5-yr swap	10-yr swap	2-yr gov	5-yr gov	10-yr gov
USD	Spot	4.75	4.94	4.42	3.79	3.56	3.99	3.59	3.50
	+3m	5.25	5.40	5.10	4.25	3.85	4.70	4.10	3.80
	+6m	5.25	5.40	4.90	4.15	3.65	4.50	4.00	3.60
	+12m	5.25	5.00	4.70	4.05	3.45	4.30	3.90	3.40
EUR*	Spot	3.00	2.82	3.29	3.04	2.94	2.58	2.29	2.25
	+3m	3.75	4.08	3.45	3.25	3.25	2.90	2.70	2.75
	+6m	4.00	4.16	3.20	3.05	3.10	2.70	2.55	2.60
	+12m	4.00	4.13	3.00	3.00	2.90	2.60	2.50	2.50
GBP**	Spot	4.00		4.12	3.74	3.40	3.39	3.32	3.42
	+3m	4.25		4.10	3.80	3.40	3.40	3.40	3.30
	+6m	4.25		4.10	3.80	3.40	3.40	3.40	3.30
	+12m	4.00		3.90	3.60	3.30	3.20	3.20	3.20
DKK	Spot	2.60	3.08	3.47	3.22	3.10	2.74	2.51	2.52
	+3m	3.35	3.77	3.60	3.40	3.40	3.05	2.85	2.85
	+6m	3.60	3.85	3.35	3.20	3.25	2.85	2.70	2.70
	+12m	3.60	3.84	3.15	3.15	3.05	2.75	2.65	2.60
SEK	Spot	3.00	3.25	3.56	3.04	2.88	2.91	2.42	2.28
	+3m	3.75	4.15	3.65	3.20	3.00	3.20	2.60	2.55
	+6m	4.25	4.40	3.30	2.90	2.80	2.90	2.60	2.65
	+12m	4.00	4.00	3.00	2.80	2.75	2.60	2.60	2.70
NOK	Spot	2.75	3.36	3.25	3.00	3.00	2.96	2.90	2.96
	+3m	3.25	3.45	3.45	3.35	3.15	3.10	3.10	3.10
	+6m	3.25	3.36	3.20	3.10	2.85	2.90	2.90	2.80
	+12m	3.00	3.20	3.05	2.95	2.80	2.75	2.80	2.80

* German government bond yields and euro swap rates ** Based on OIS swap rates. Note 3M GBP Libor is no longer published

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

Source: Danske Bank

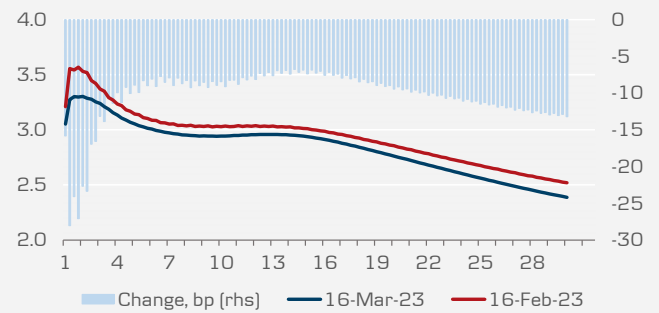
Eurozone forecast

EUR forecast summary

16/03/2023	--- Forecast ---			--- Fcst vs Fwd in bp ---			
EUR	Spot	+3m	+6m	+12m	+3m	+6m	+12m
Money Market							
Deposit	3.00	3.75	4.00	4.00	-	-	-
3M	2.82	4.08	4.16	4.13	75	77	84
6M	3.13	4.27	4.30	3.95	81	85	60
Government Bonds							
2-year	2.58	2.90	2.70	2.60	-	-	-
5-year	2.29	2.70	2.55	2.50	-	-	-
10-year	2.25	2.75	2.60	2.50	-	-	-
Swap rates							
2-year	3.29	3.45	3.20	3.00	10	-11	-18
5-year	3.04	3.25	3.05	3.00	21	4	7
10-year	2.94	3.25	3.10	2.90	30	16	-1

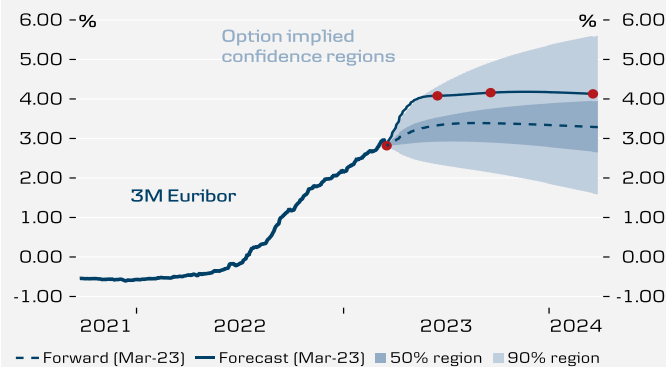
Source: Danske Bank

1M change in EUR swap rates



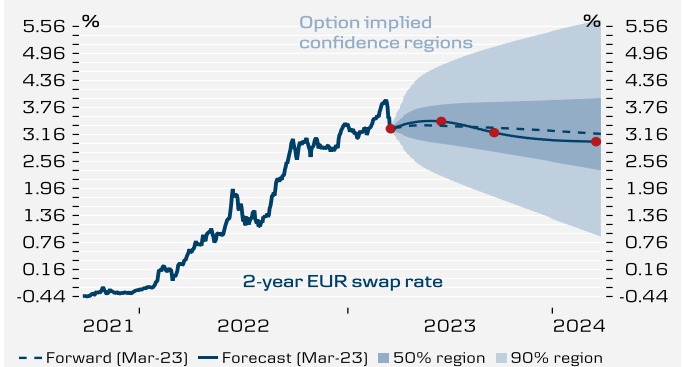
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

3M Euribor rates



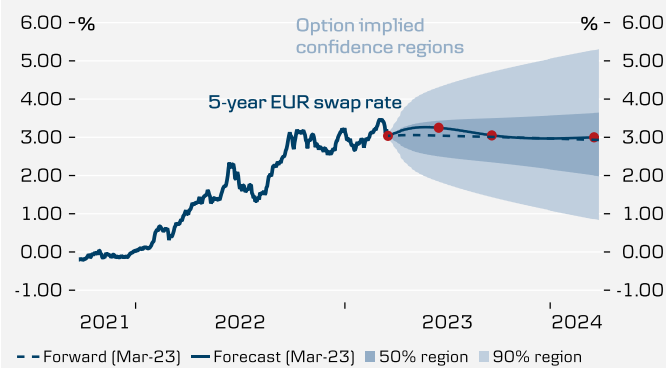
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

2Y EUR swap rates



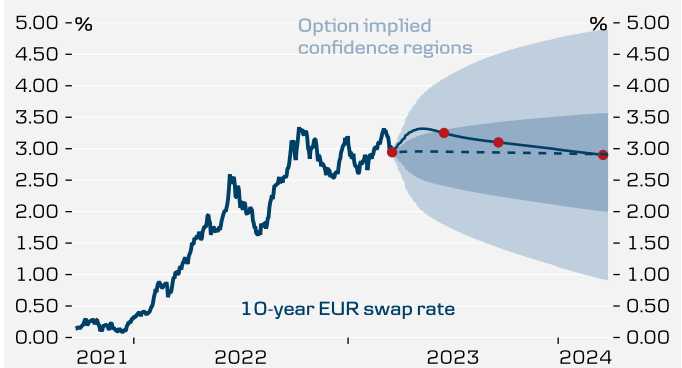
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

5Y EUR swap rates



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

10Y EUR swap rates



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

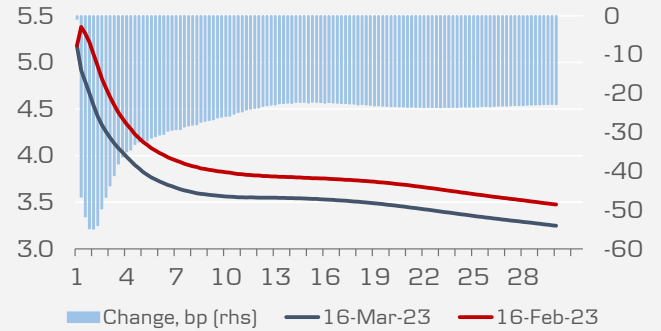
US forecast

USD forecast summary

16/03/2023	--- Forecast ---				--- Fcst vs Fwd in bp ---		
USD	Spot	+3m	+6m	+12m	+3m	+6m	+12m
Money Market							
Fed Funds	4.75	5.25	5.25	5.25	-	-	-
3M	4.94	5.40	5.40	5.00	19	68	71
Government Bonds							
2-year	3.99	4.70	4.50	4.30	-	-	-
5-year	3.59	4.10	4.00	3.90	-	-	-
10-year	3.50	3.80	3.60	3.40	-	-	-
Swap rates							
2-year	4.42	5.10	4.90	4.70	87	88	98
5-year	3.79	4.25	4.15	4.05	56	56	61
10-year	3.56	3.85	3.65	3.45	34	19	6

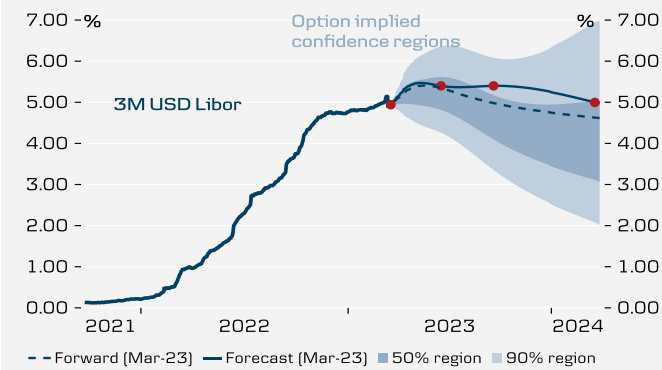
Source: Danske Bank

1M change in USD swap (3M) rates



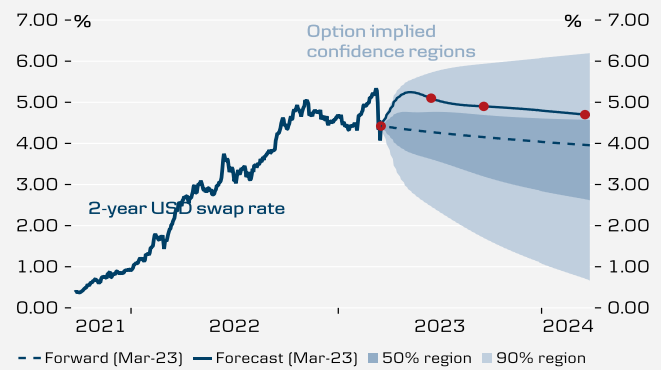
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

3M USD Libor rates



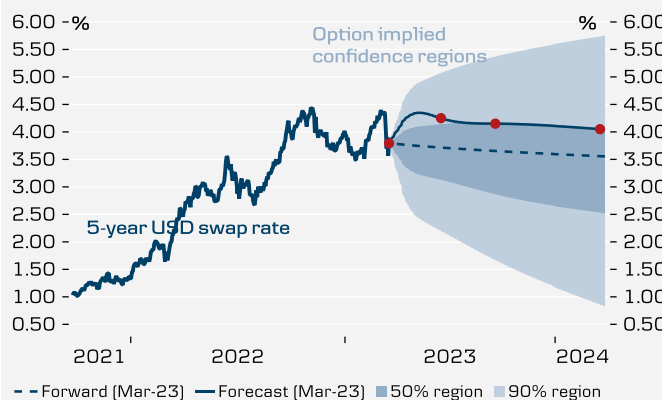
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

2Y USD swap rates



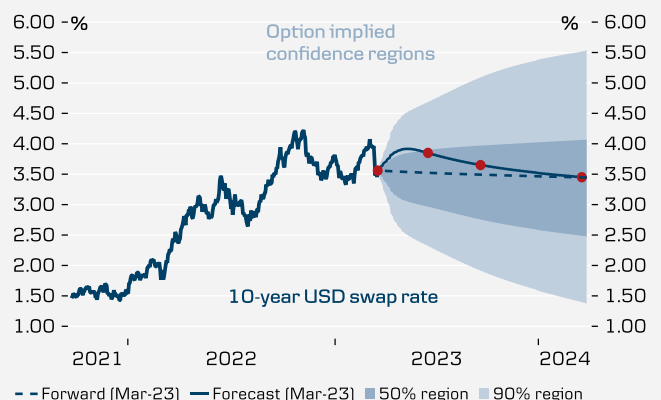
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

5Y 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

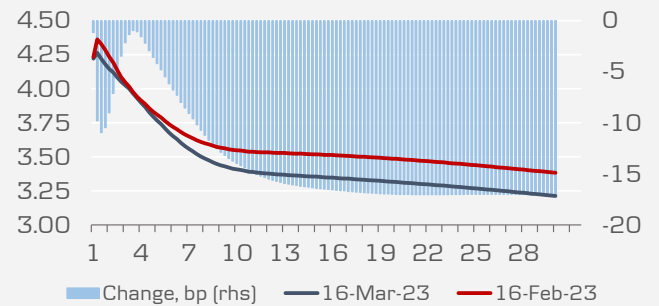
UK forecast

GBP forecast summary

16/03/2023	--- Forecast ---				--- Fcst vs Fwd in bp ---		
GBP	Spot	+3m	+6m	+12m	+3m	+6m	+12m
<u>Money Market</u>							
Bank rate	4.00	4.25	4.25	4	-	-	-
<u>Government Bonds</u>							
2-year	3.39	3.40	3.40	3.20	18	-29	-2
5-year	3.316	3.4	3.4	3.2	20	1	-9
10-year	3.42	3.30	3.30	3.20	-2	-14	-16
<u>Swap rates (SONIA OIS)</u>							
2-year	4.12	4.10	4.10	3.90	2	9	4
5-year	3.74	3.80	3.80	3.60	12	18	32
10-year	3.40	3.40	3.40	3.30	2	6	2

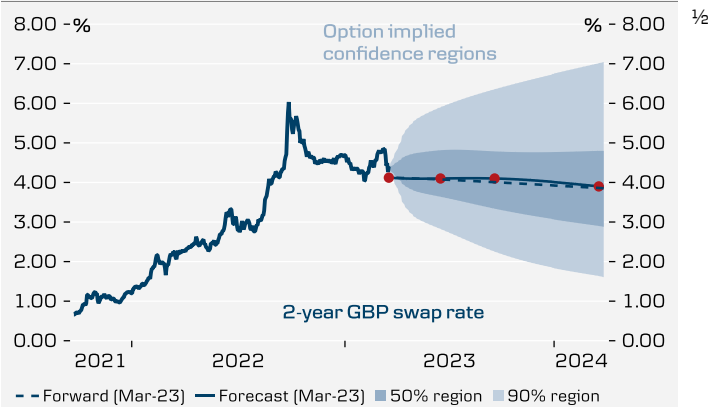
Based on OIS swaps
Source: Danske Bank

1M change in GBP swap (6M) rates



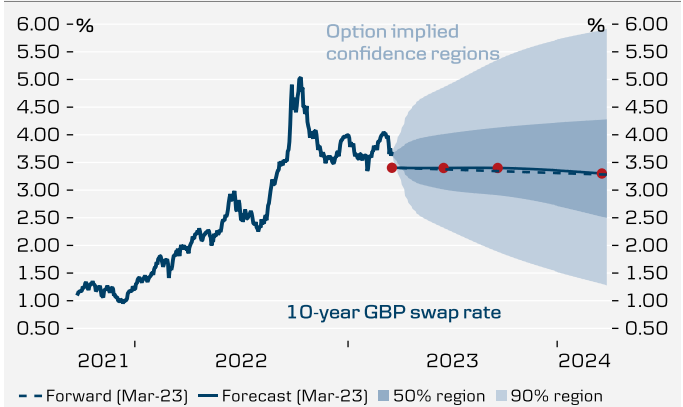
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

2Y UK swap rates



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

10Y UK swap rates



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

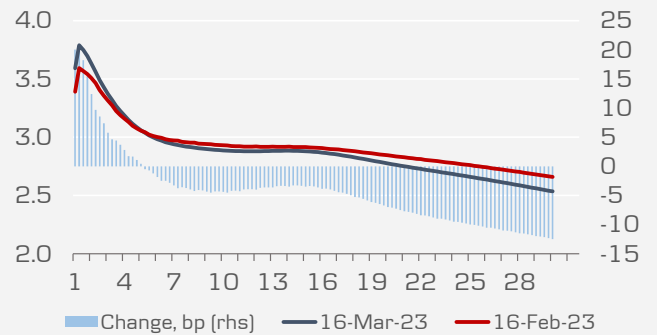
Sweden forecast

SEK forecast summary

16/03/2023	--- Forecast ---				--- Fcst vs Fwd in bp ---		
SEK	Spot	+3m	+6m	+12m	+3m	+6m	+12m
<u>Money market</u>							
Repo	3.00	3.75	4.25	4.00	-	-	-
3M	3.25	4.15	4.40	4.00	26	53	49
<u>Government bonds</u>							
2-year	2.91	3.20	2.90	2.60	-	-	-
5-year	2.42	2.60	2.60	2.60	-	-	-
10-year	2.28	2.55	2.65	2.70	-	-	-
<u>Swap rates</u>							
2-year	3.56	3.65	3.30	3.00	14	-7	-7
5-year	3.04	3.20	2.90	2.80	20	-3	1
10-year	2.88	3.00	2.80	2.75	13	-4	-3

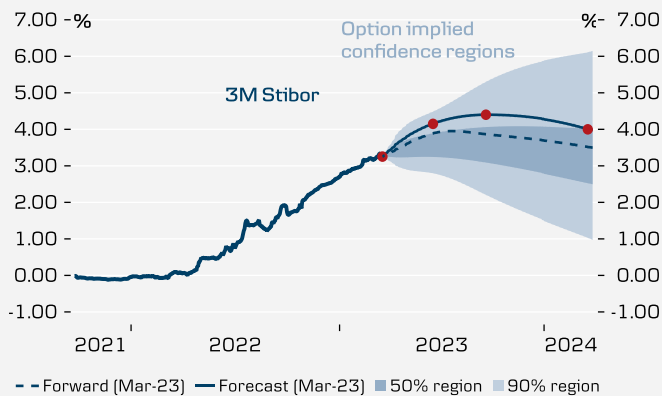
Source: Danske Bank

1M change in SEK swap (3M) rates



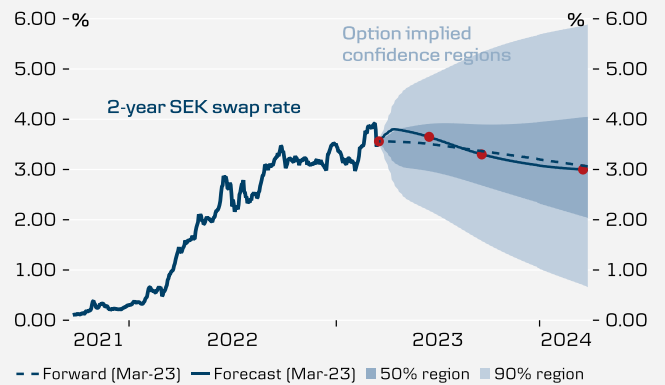
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

3M Stibor rates



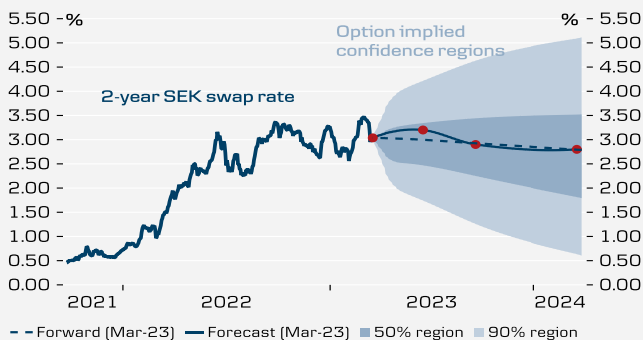
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

2Y SEK swap rates



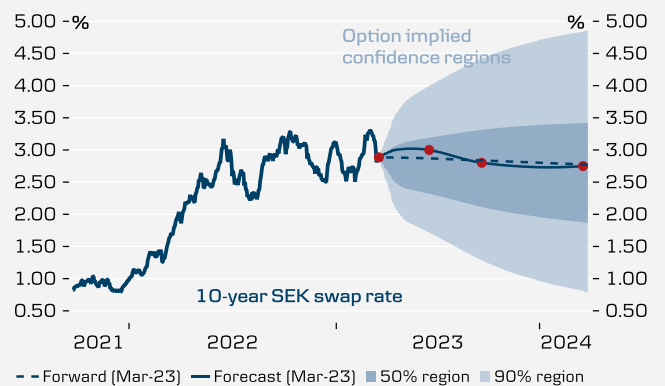
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

5Y 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

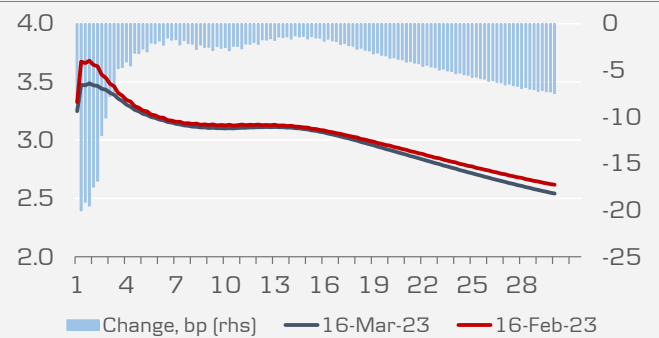
Denmark forecast

DKK forecast summary

16/03/2023	--- Forecast ---				--- Fcst vs Fwd in bp ---		
DKK	Spot	+3m	+6m	+12m	+3m	+6m	+12m
Money Market							
CD	2.60	3.35	3.60	3.60	-	-	-
Repo	2.75	3.50	3.75	3.75	-	-	-
3M	3.08	3.77	3.85	3.84	37	38	48
6M	3.45	3.66	3.70	3.70	13	16	26
Government bonds							
2-year	2.74	3.05	2.85	2.75	-	-	-
5-year	2.51	2.85	2.70	2.65	-	-	-
10-year	2.52	2.85	2.70	2.60	-	-	-
Swap rates							
2-year	3.47	3.60	3.35	3.15	10	-11	-20
5-year	3.22	3.40	3.20	3.15	19	2	5
10-year	3.10	3.40	3.25	3.05	30	16	-1
30-year	2.54	3.00	2.90	3.05	47	39	58

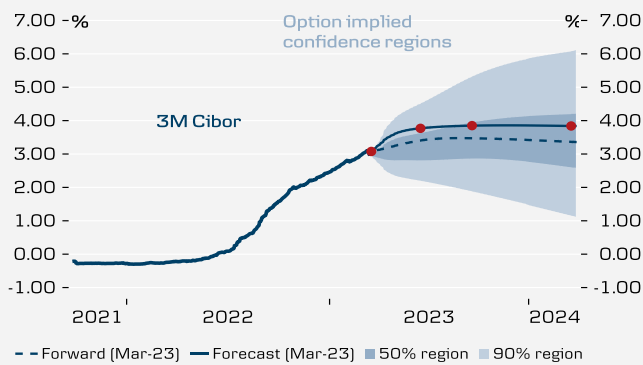
Source: Danske Bank

1M change in DKK swap (6M) rates



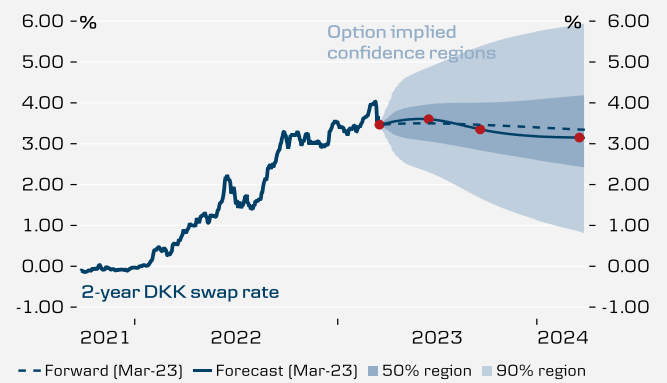
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

3M Cibar rates



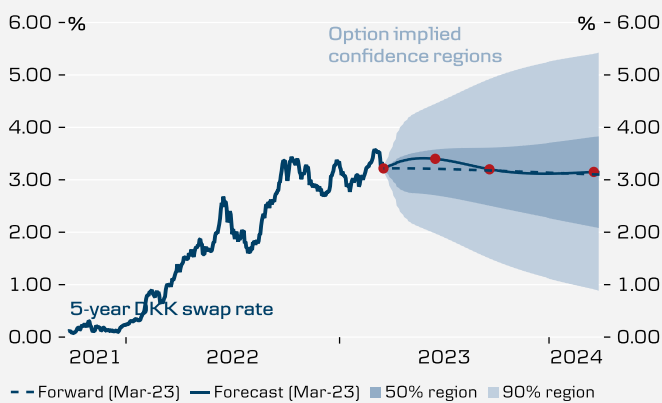
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

2Y DKK swap rates



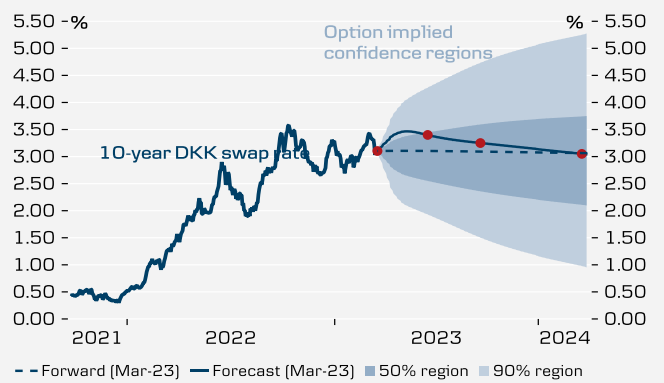
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

5Y DKK swap rates



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

10Y DKK swap rates



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

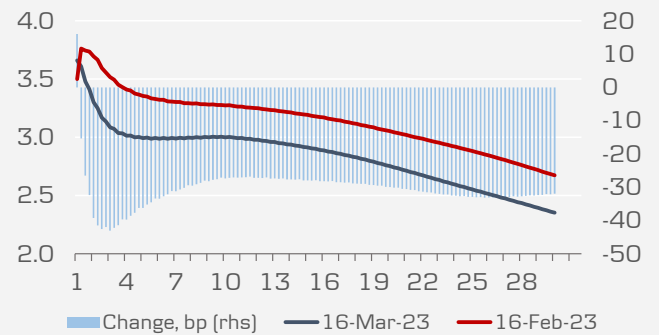
Norway forecast

NOK forecast summary

16/03/2023	--- Forecast ---				--- Fcst vs Fwd in bp ---		
NOK	Spot	+3m	+6m	+12m	+3m	+6m	+12m
<u>Money market</u>							
Deposit	2.75	3.25	3.25	3.00	-	-	-
3M	3.36	3.45	3.36	3.20	-14	-12	15
6M	3.57	3.70	3.57	3.45	5	7	43
<u>Government bonds</u>							
2-year	2.96	3.10	2.90	2.75	-	-	-
5-year	2.90	3.10	2.90	2.80	-	-	-
10-year	2.96	3.10	2.80	2.80	-	-	-
<u>Swap rates</u>							
2-year	3.25	3.45	3.20	3.05	32	20	26
5-year	3.00	3.35	3.10	2.95	39	18	9
10-year	3.00	3.15	2.85	2.80	17	-11	-12

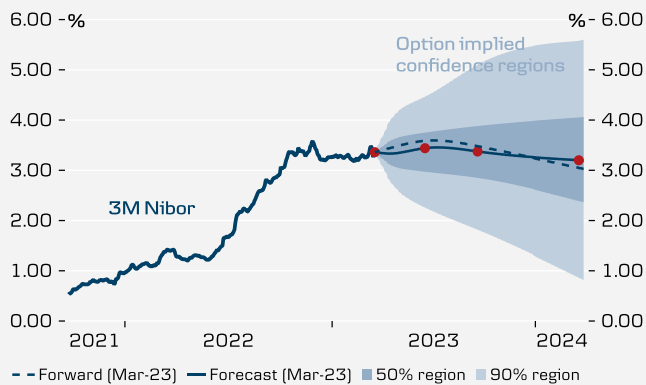
Source: Danske Bank

1M change in NOK swap (6M) rates



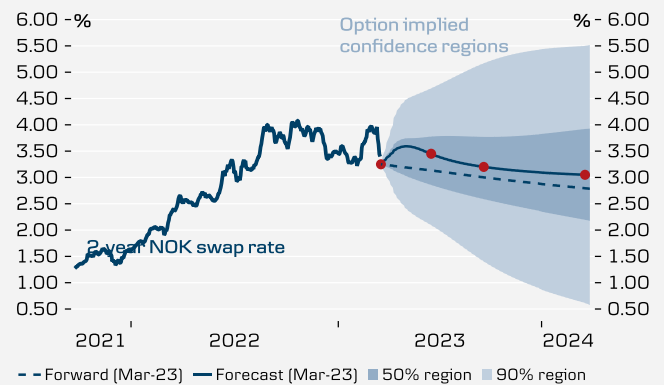
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

3M Nibor rates



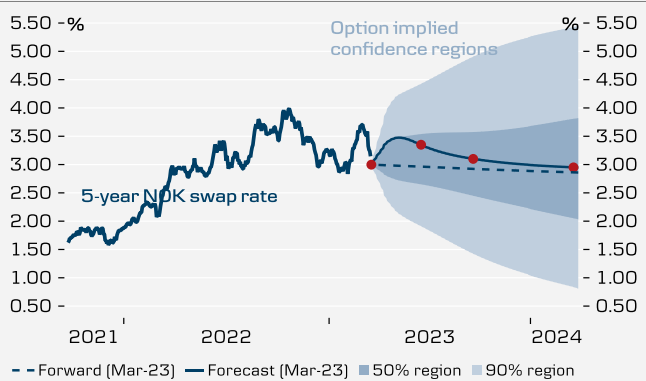
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

2Y NOK swap rates



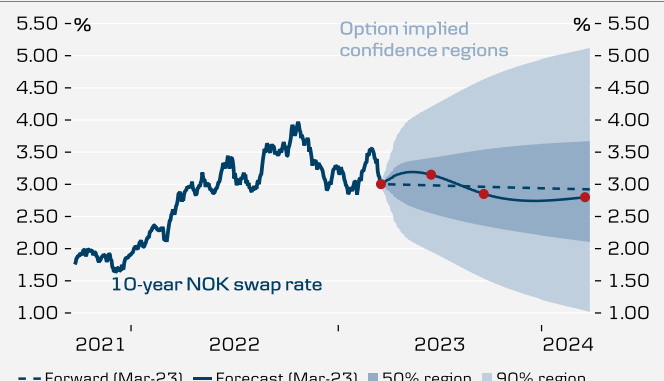
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

5Y 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
Source: Danske Bank

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