

Yield Outlook

Central banks becoming increasingly hawkish

- During the past month, we have witnessed a significant repricing of a number of central banks amid mounting inflation, and several central banks have been sending more hawkish signals.
- The Bank of England (BoE) has clearly announced that rate hikes are imminent. Markets are pricing a UK rate hike as early as November. This has prompted us to revise our forecast for UK interest rates, and our call is for three rate hikes during the next 12 months, taking the base rate to 0.75%.
- We now expect two rate hikes, against previously only one, from the US Federal Reserve in 2022 (September and December).
- We still do not expect the ECB to hike rates for the next few years. However, as inflation is proving to be less transitory than previously expected, and given the latest signals from the BoE, markets look likely to continue to price rate hikes into the yield curve. This has led to upward pressure on 2Y-5Y EUR swap rates.
- The Fed will probably have enacted rate lift-off twelve months from now, and we expect to see continuing upward pressure on long-term yields. As such, we expect 10Y US Treasury yields to reach 2% on a 12M horizon. Higher US yields and a steeper EUR money market curve are pushing European yields higher, and we have adjusted our 12M estimate for German 10Y yields from 0.1% to 0.25%.
- Rising commodity prices are causing concern that household purchasing power could be eroded, which would weigh on consumer spending and, ultimately, cause economic growth to slow. Bottlenecks and accompanying inflation pose a growing risk of some kind of stagflation scenario (with high inflation and weak GDP growth) materialising. The latter would tend to anchor long-term yields, as markets would expect weaker growth to resolve the inflation problem, reducing the need for higher short-term rates in the medium term.

Links

[Forecast table](#)

[Forecast Euro area](#)

[Forecast USA](#)

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[Forecast Denmark](#)

[Forecast Sweden](#)

[Forecast Norway](#)

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	1.60	1.70	1.80	2.00
EUR	-0.14	0.00	0.10	0.25
GBP	1.15	1.25	2.30	1.40
DKK	0.14	0.25	0.35	0.50
SEK	0.38	0.40	0.45	0.60
NOK	1.73	1.80	1.85	1.90

Note: EUR = Germany.

10Y swap rates

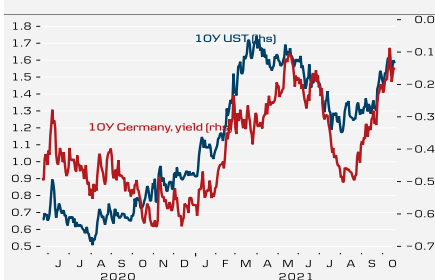
Country	Spot	+3m	+6m	+12m
USD	1.60	1.75	1.85	2.05
EUR	0.25	0.40	0.50	0.65
GBP	1.30	1.45	2.50	1.60
DKK	0.52	0.65	0.75	0.90
SEK	0.95	0.95	0.95	1.05
NOK	1.99	2.10	2.15	2.20

Sources: Danske Bank all three tables

Chief Analyst

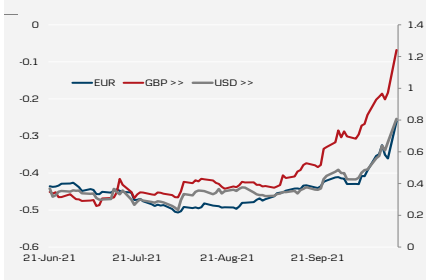
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Long European and US yields have ticked up in the past month, %



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

Money markets pricing more rate hikes (1Y 1Y OIS swap rates), %



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

Highly divergent central banks

For some time, we have paid less attention to the short end of the ECB yield curve.

The reason is that the ECB for long has emphasised that rate hikes would be very slow in coming due to the pandemic. The ECB even adopted a new monetary policy strategy in July. In that connection, ECB President Lagarde emphasised that rates will stay unchanged or be reduced until the ECB sees inflation reaching the 2% mark well before the forecast period expires (typically on an 18-month horizon). At the same time, inflation must be expected to stay at that level during the remainder of the forecast period and, not least, the ECB will accept a ‘transitory’ period in which inflation is – or is expected to be – ‘moderately’ above 2%.

This led markets to conclude that the ECB will not be enacting rate lift-off for the next several years. Our ECB analysts shared this view, given that our macroeconomists assessed that it would be quite difficult for the ECB to present an inflation forecast that would meet the above-mentioned requirements for many years to come. In other words, we were quite confident that the ECB’s policy rates would remain unchanged at today’s level of minus 0.5% for several years.

While our baseline remains that the ECB will not be hiking rates for the next two or three years, uncertainty has definitely increased over the past couple of months. It therefore makes good sense that markets are now pricing a good chance of a small initial rate hike of 10bp by the end of 2022, and that ECB policy rates will be some 35bp higher than now by the end of 2023. We also expect markets to price a ‘steep’ money market curve (0Y-3Y rates) over the next 12 months. We believe this will result in continuing upward pressure on monetary policy-sensitive yields in the 2Y-5Y segment.

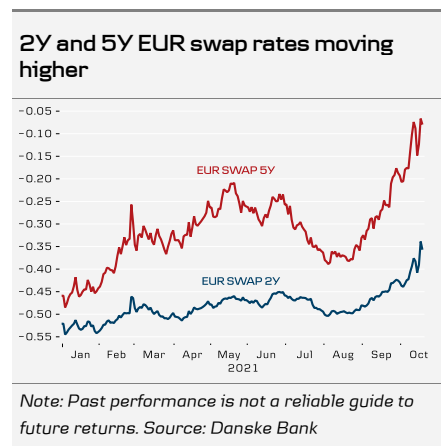
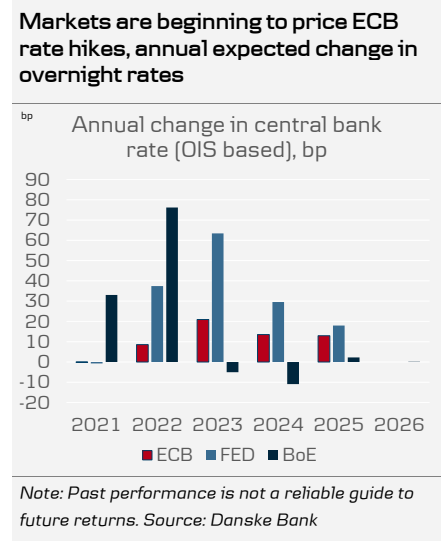
Why do markets not believe in the ECB?

There are two main reasons why markets no longer ‘believe in’ the ECB’s narrative of keeping rates on hold for many years.

1. Headline inflation is too high

Firstly, the high level of headline inflation makes it hard to believe it should not affect underlying inflation. In September, headline inflation rose to 3.0% in the eurozone, driven in part by an increase in German inflation to 4.1%. And inflation is not only being pushed up by price increases related to energy and German VAT changes. Underlying inflation in the eurozone was 1.9% in September – the highest level since 2018. In other words, we see increasing signs of high energy prices feeding through to other goods.

Nor is there much to indicate the energy crisis should be short-lived. According to Bloomberg, Gazprom will probably not be sending more natural gas to Western Europe in November and OPEC sees no need to add more oil to the market although high gas prices are boosting oil consumption as, for example, power plants shift from natural gas to oil-related products. And other markets do not seem to be coming to the rescue. Metal prices have rebounded and freight rates are running close to record levels.



2. Other central banks now clearly signalling higher policy rates

Secondly, other central banks are now changing their communications. This is particularly true of the Bank of England (BoE). Only a few months ago, BoE signals were in line with those of the ECB. The rise in inflation would be transient and it would not make sense to hike policy rates in response to a temporary increase in inflation, which indeed has the effect of a tax on consumers. However, recently, BoE governor Andrew Bailey has clearly signalled the BoE's intention to 'react'. The market is now pricing rate hikes from the BoE as early as this year. This coincides with the BoE QE programme expiring. Our new forecast for the Bank of England is slightly more cautious than the market's. We expect three BoE rate hikes in 2022 – one 15bp hike and two 25bp hikes – taking the base rate to 0.75% by the end of 2022.

While the US labour market report for September disappointed the markets slightly, the Federal Reserve still looks set to announce the beginning of bond purchase tapering at its November meeting. We continue to expect the Fed to end its current QE programme of USD120bn by summer 2022.

We now expect the Fed to deliver two policy rate hikes in 2022 (previous forecast: one hike). While we pencil in the hikes for September and December, the market prices the first Fed hike slightly earlier than we do.

Some minor central banks have moved even further. The Reserve Bank of New Zealand and the Norwegian central bank (Norges Bank) have already hiked rates and are signalling further hikes ahead. On the other hand, we wish to emphasise that the Swedish central bank (Riksbank) has not signalled a change in monetary policy strategy.

ECB resists pressure but markets are set to begin pricing rate hikes

As mentioned, we do not expect the ECB to change its rhetoric here and now in spite of rising inflation. The central bank will probably maintain the view that the increase in inflation is transient. However, the risk to policy rates is no longer downside but upside. This means the upward pressure on 2Y-5Y rates could continue.

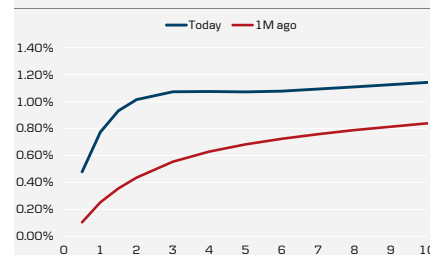
The next test will come when the ECB will have to decide what to do with bond purchases when the Pandemic Emergency Purchase Programme (PEPP) ends at the end of March next year. A pandemic purchasing programme would not make sense in 2022, when the pandemic will probably be over and all EU restrictions have been removed. Hence, we do not expect the programme to be extended. On the other hand, we continue to expect the ECB to simultaneously expand its Public Sector Purchase Programme (PSPP) to avoid an excessive impact on bond markets. However, in a scenario of inflation being less transient than expected, it would probably not come as a major surprise if the ECB skips expanding the PSPP. Overall, we therefore expect less support to low yields from ECB bond purchases in 2022 than we have seen this year.

Not everything indicates yields should go up

On the one hand, many central banks have become more hawkish and inflation has reached a level that entails a risk of rising inflation not being transient. On the other hand, there are increasing worries that the global economy may shift down a gear after the strong growth fuelled by the reopening in the spring and over the summer. Much attention is focused on Chinese GDP growth.

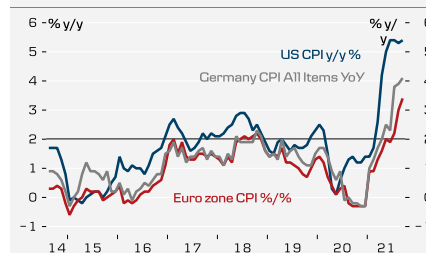
Meanwhile, rising commodity prices are creating concern that household purchasing power may be eroded, which would hit consumer spending and, ultimately, economic growth. Bottlenecks and the ensuing inflation are posing an increasing risk of a stagflation scenario of high inflation and low GDP growth materialising. Any policy rate hikes could add to

Significant change in GBP swap curve over the past month



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

Concern that high commodity-driven inflation could spread to the rest of the economy



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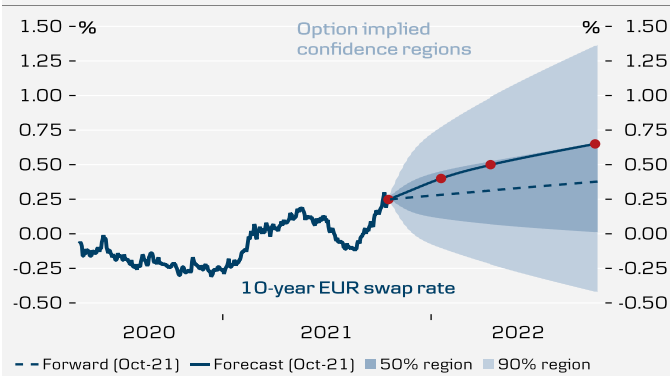
this risk. The latter could, not least, become a reality for Britain. This is probably the reason the market is pricing the Bank of England to gradually lower policy rates again in 2024.

Central banks are obviously aware of the stagflation risk, so what we are witnessing now is in reality central banks recognising that monetary conditions have simply become too expansionary following reopening and that monetary policy needs to be adjusted.

Outlook still muddy but we continue to see upside risk to long yields

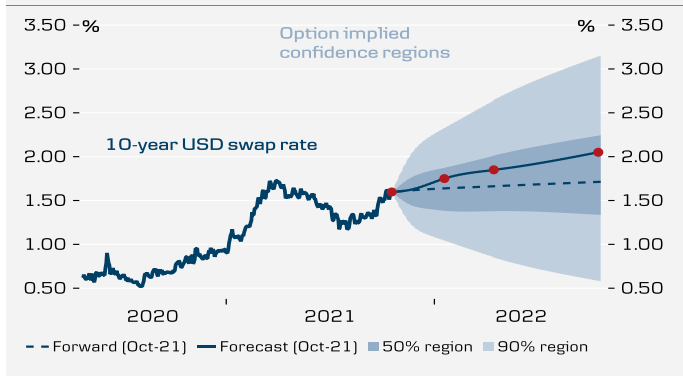
We expect the market focus for the remainder of the year to shift between the factors supporting higher long yields and those pointing to lower yields. In other words, the outlook has remained quite muddy. Looking 6 and 12 months ahead, we still expect the global economy, and particularly the US economy, to continue to grow. And with an initial rate hike having moved closer and a reduced volume of bond buybacks from both the ECB and the Fed, this should tend to push long yields higher in both the US and Europe. We continue to expect US 10Y Treasury yields to rise to 2% on a 12M horizon, while 10Y Bund yields look set to increase to 0.25%.

Forecast for 10Y EUR swap rates



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

Forecast for 10Y USD swap rates



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

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	0.12	0.56	1.22	1.60	0.40	1.15	1.60
	+3m	0.25	0.11	0.65	1.35	1.75	0.55	1.30	1.70
	+6m	0.25	0.11	0.80	1.45	1.85	0.70	1.40	1.80
	+12m	0.50	0.51	1.20	1.65	2.05	1.10	1.60	2.00
EUR *	Spot	-0.50	-0.55	-0.35	-0.07	0.25	-0.65	-0.48	-0.14
	+3m	-0.50	-0.54	-0.35	0.00	0.40	-0.65	-0.40	0.00
	+6m	-0.50	-0.54	-0.30	0.05	0.50	-0.60	-0.35	0.10
	+12m	-0.50	-0.54	-0.20	0.10	0.65	-0.50	-0.30	0.25
GBP	Spot	0.10	0.13	1.14	1.23	1.30	0.71	0.84	1.15
	+3m	0.10	0.37	1.00	1.25	1.45	0.65	0.85	1.25
	+6m	0.25	0.44	1.10	1.25	1.50	0.75	0.85	1.30
	+12m	0.50	0.67	1.15	1.30	1.60	0.80	0.90	1.40
DKK	Spot	-0.60	-0.27	-0.04	0.22	0.52	-0.56	-0.34	0.14
	+3m	-0.60	-0.28	-0.05	0.27	0.65	-0.55	-0.28	0.25
	+6m	-0.60	-0.28	-0.02	0.30	0.75	-0.50	-0.23	0.35
	+12m	-0.60	-0.28	0.08	0.35	0.90	-0.40	-0.18	0.50
SEK	Spot	0.00	-0.09	0.17	0.59	0.96	-0.23	0.08	0.39
	+3m	0.00	-0.03	0.15	0.60	0.95	-0.25	0.10	0.40
	+6m	0.00	-0.03	0.15	0.60	0.95	-0.25	0.15	0.45
	+12m	0.00	-0.03	0.15	0.70	1.05	-0.20	0.25	0.60
NOK	Spot	0.25	0.74	1.54	1.87	1.99	1.05	1.57	1.73
	+3m	0.50	0.96	1.45	1.95	2.10	1.00	1.60	1.80
	+6m	0.75	1.24	1.55	1.95	2.15	1.10	1.60	1.85
	+12m	1.00	1.49	2.20	2.05	2.20	1.75	1.70	1.90

* German government bond yields and euro swap rates

Source: Danske Bank

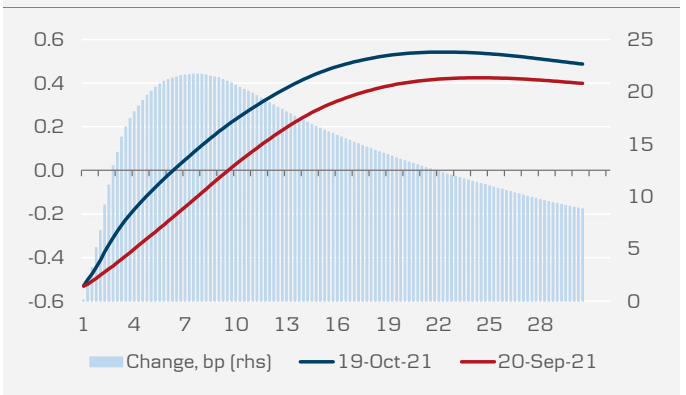
Eurozone forecast

EUR forecast summary

EUR	19/10/2021				--- Forecast ---			--- Fcst vs Fwd in bp ---		
	Spot	+3m	+6m	+12m	+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	-0.55	-0.54	-0.54	-0.54	-2	-5	-16	-2	-5	-16
6M	-0.53	-0.52	-0.52	-0.52	-4	-9	-22	-4	-9	-22
<u>Government Bonds</u>										
2-year	-0.65	-0.65	-0.60	-0.50	-	-	-	-	-	-
5-year	-0.48	-0.40	-0.35	-0.30	-	-	-	-	-	-
10-year	-0.14	0.00	0.10	0.25	-	-	-	-	-	-
<u>Swap rates</u>										
2-year	-0.35	-0.35	-0.30	-0.20	-6	-6	-8	-6	-6	-8
5-year	-0.07	0.00	0.05	0.10	3	-1	1	3	-1	1
10-year	0.25	0.40	0.50	0.65	12	19	27	12	19	27

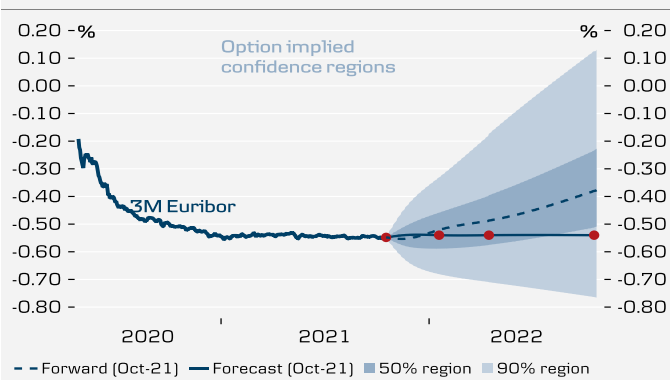
Source: Danske Bank

1M change in EUR swap rates



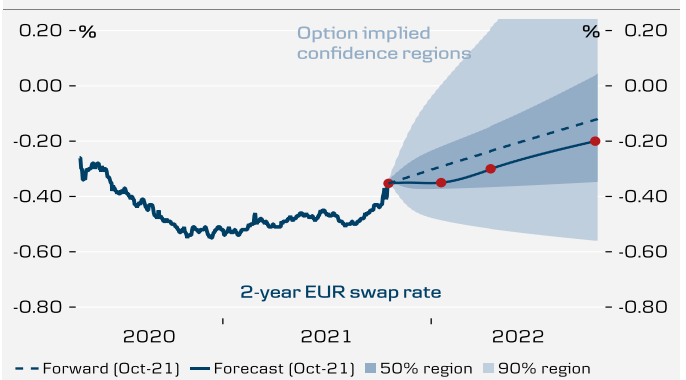
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

3M Euribor rates



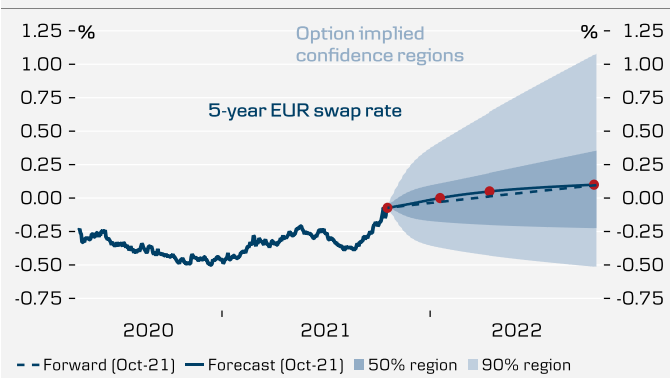
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

2Y EUR swap rates



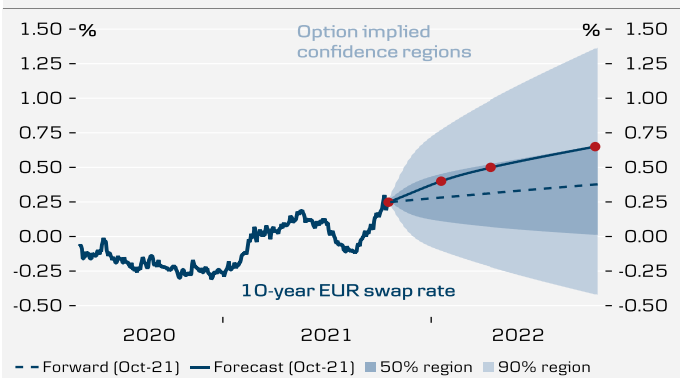
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

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

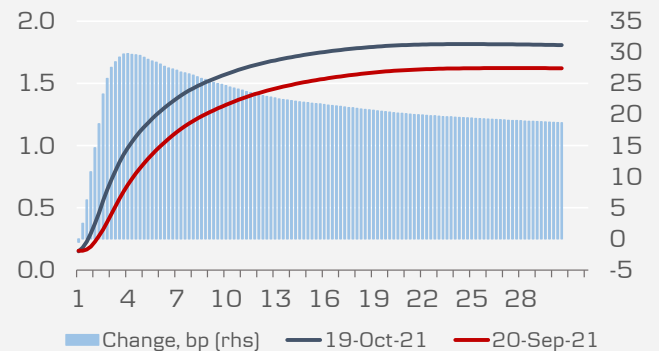
US forecast

USD forecast summary

19/10/2021	--- Forecast ---				--- Fcst vs Fwd in bp---		
USD	Spot	+3m	+6m	+12m	+3m	+6m	+12m
<u>Money Market</u>							
Fed Funds	0.25	0.25	0.25	0.50	-	-	-
3M	0.12	0.11	0.11	0.51	-6	-13	-5
<u>Government Bonds</u>							
2-year	0.40	0.55	0.70	1.10	-	-	-
5-year	1.15	1.30	1.40	1.60	-	-	-
10-year	1.60	1.70	1.80	2.00	-	-	-
<u>Swap rates</u>							
2-year	0.56	0.65	0.80	1.20	-6	-7	1
5-year	1.22	1.35	1.45	1.65	4	6	9
10-year	1.60	1.75	1.85	2.05	10	15	26

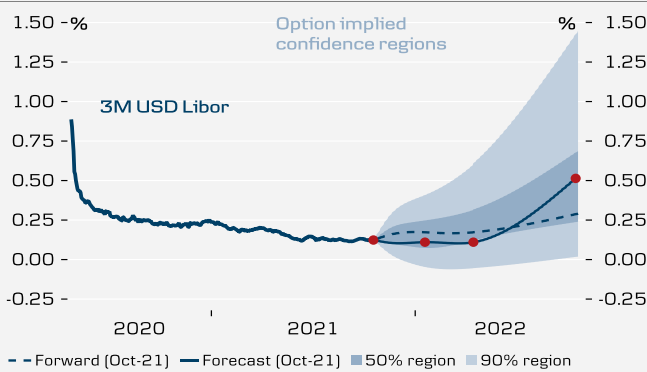
Source: Danske Bank

1M change in USD swap (3M) rates



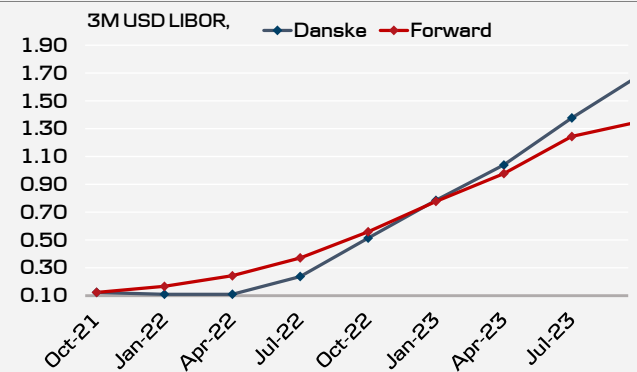
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

3M USD Libor rates



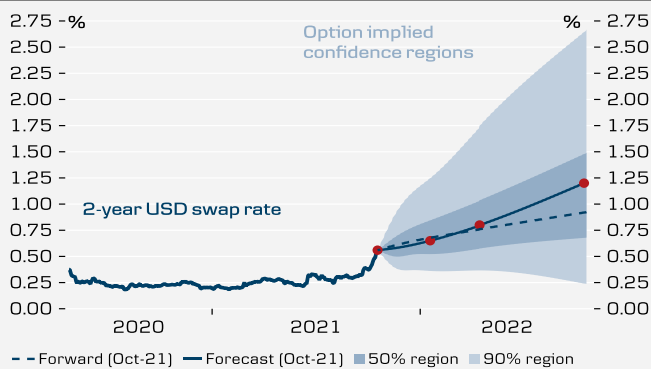
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

Danske Bank forecast and forwards



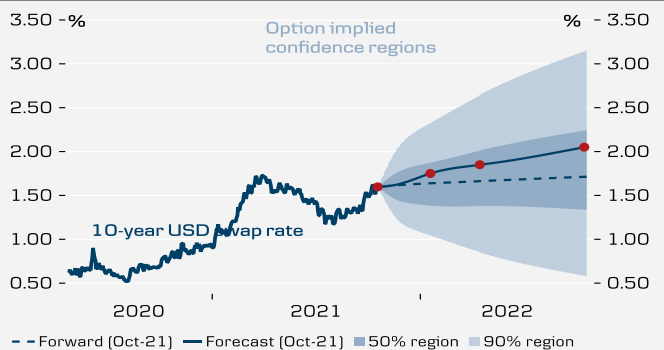
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

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

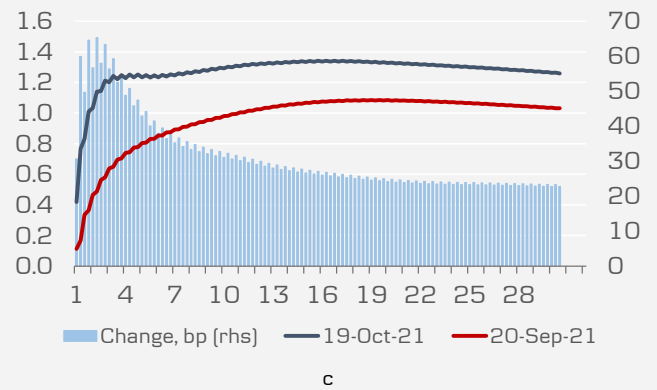
UK forecast

GBP forecast summary

19/10/2021 GBP	--- Forecast ---				--- Fcst vs Fwd in bp ---		
	Spot	+3m	+6m	+12m	+3m	+6m	+12m
<u>Money Market</u>							
Repo	0.10	0.1	0.25	0.5	-	-	-
3M	0.13	0.37	0.44	0.67	-41	-59	-60
<u>Government Bonds</u>							
2-year	0.71	0.65	0.75	0.80	-13	-12	-4
5-year	0.835	0.85	0.85	0.9	-1	-5	-1
10-year	1.15	1.25	1.30	1.40	7	7	14
<u>Swap rates</u>							
2-year	1.14	1.00	1.10	1.15	-34	-30	-27
5-year	1.23	1.25	1.25	1.30	-5	-7	-6
10-year	1.30	1.45	1.50	1.60	11	15	24

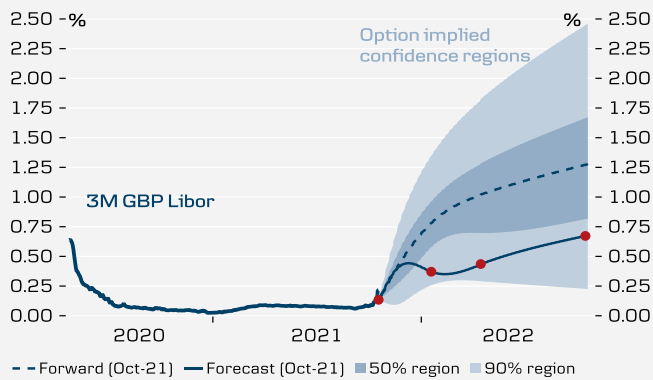
Source: Danske Bank

1M change in GBP swap (6M) rates



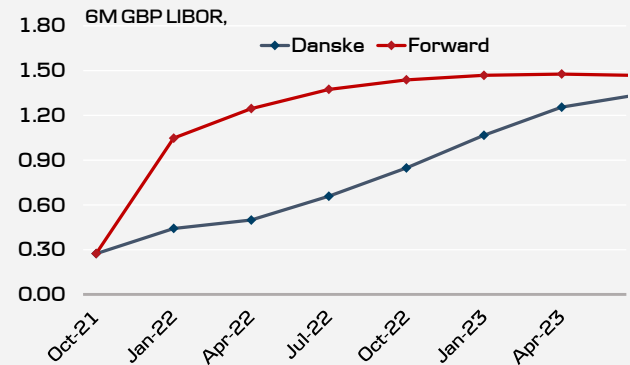
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

3M GBP Libor rates



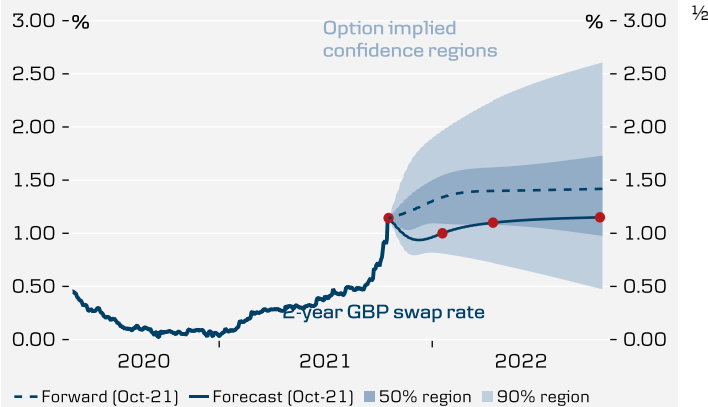
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

Danske Bank forecast and forwards



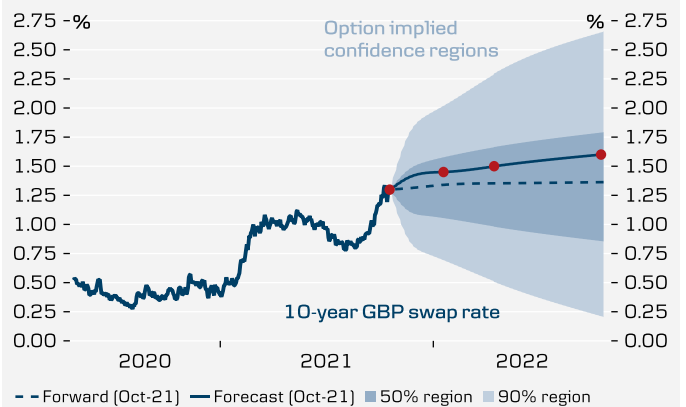
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

2Y 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

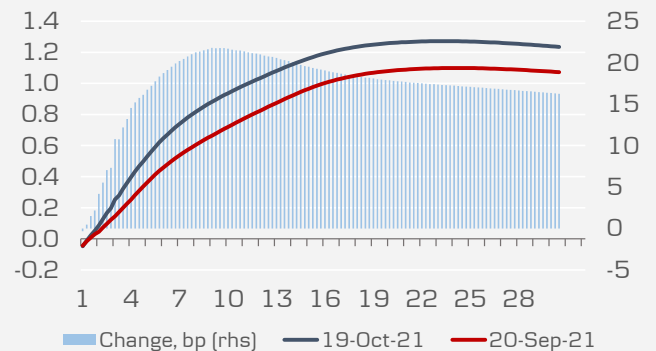
Sweden forecast

SEK forecast summary

19/10/2021	--- Forecast ---				--- Fcst vs Fwd in bp ---		
SEK	Spot	+3m	+6m	+12m	+3m	+6m	+12m
Money market							
Repo	0.00	0.00	0.00	0.00	-	-	-
3M	-0.09	-0.03	-0.03	-0.03	-2	-9	-19
Government bonds							
2-year	-0.23	-0.25	-0.25	-0.20	-	-	-
5-year	0.08	0.10	0.15	0.25	-	-	-
10-year	0.39	0.40	0.45	0.60	-	-	-
Swap rates							
2-year	0.17	0.15	0.15	0.15	-8	-18	-32
5-year	0.59	0.60	0.60	0.70	-6	-12	-13
10-year	0.96	0.95	0.95	1.05	-5	-9	-7

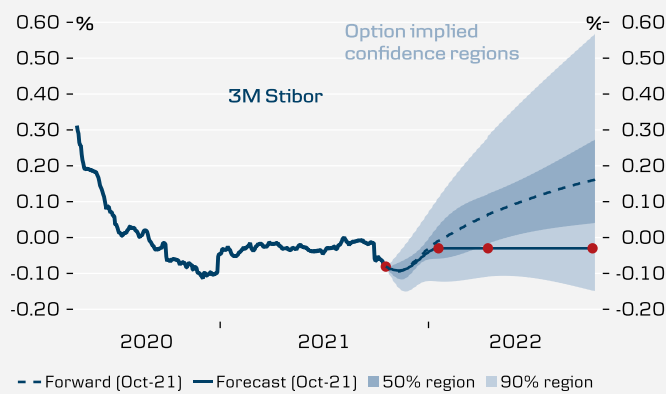
Source: Danske Bank

1M change in SEK swap (3M) rates



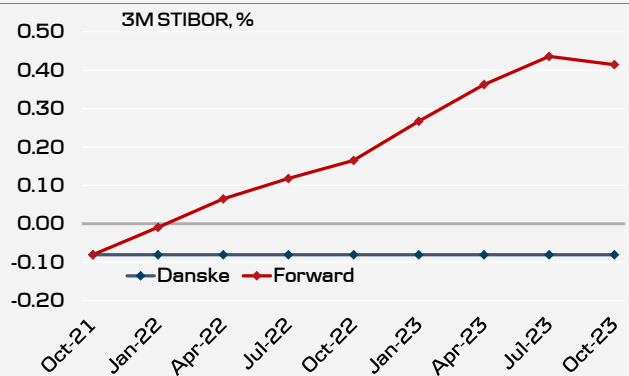
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

3M Stibor rates



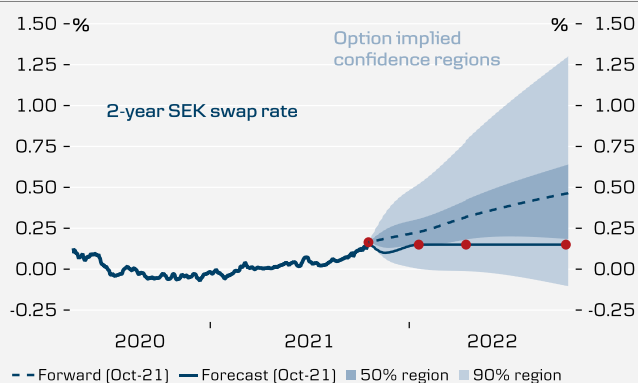
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

Danske Bank forecast and forwards



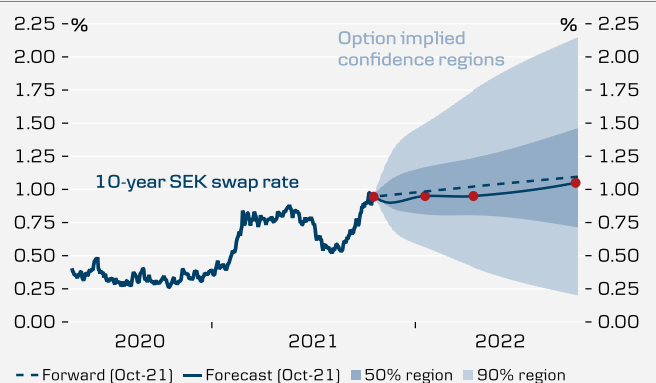
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

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

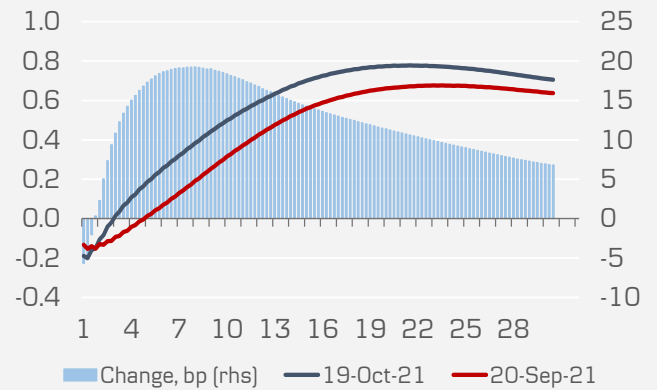
Denmark forecast

DKK forecast summary

DKK	19/10/2021				--- Forecast ---			--- Fcst vs Fwd in bp ---		
	Spot	+3m	+6m	+12m	+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	-0.27	-0.28	-0.28	-0.28	-2	-3	-15	-	-	-
6M	-0.19	-0.17	-0.17	-0.17	-1	-4	-17	-	-	-
<u>Government bonds</u>										
2-year	-0.56	-0.55	-0.50	-0.40	-	-	-	-	-	-
5-year	-0.34	-0.28	-0.23	-0.18	-	-	-	-	-	-
10-year	0.14	0.25	0.35	0.50	-	-	-	-	-	-
<u>Swap rates</u>										
2-year	-0.04	-0.05	-0.02	0.08	-6	-9	-10	-	-	-
5-year	0.22	0.27	0.30	0.35	1	0	-3	-	-	-
10-year	0.52	0.65	0.75	0.90	10	17	26	-	-	-
30-year	0.70	0.77	0.77	0.82	6	5	9	-	-	-

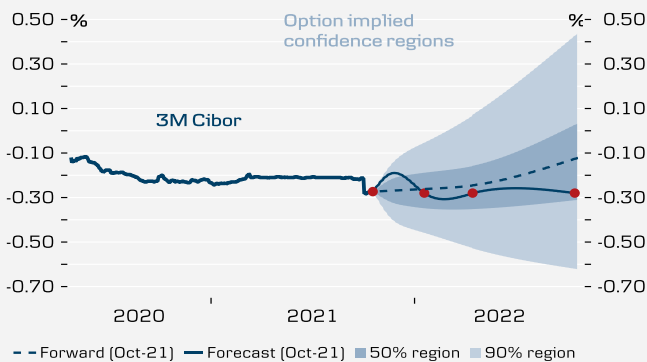
Source: Danske Bank

1M change in DKK swap (6M) rates



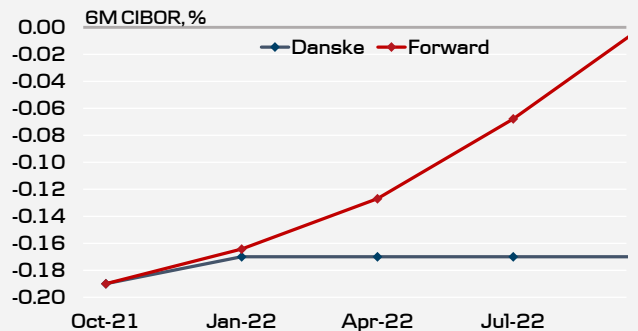
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

3M Cibar rates



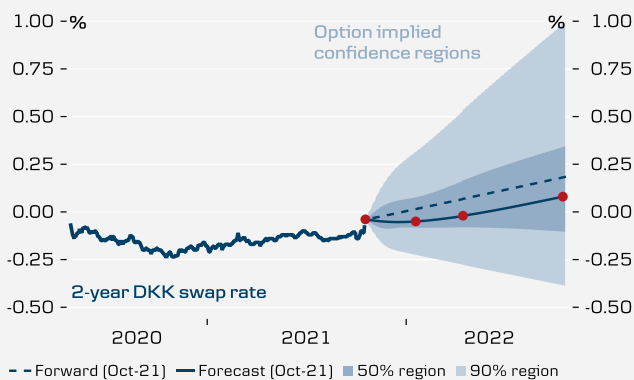
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

Danske Bank forecast and forwards



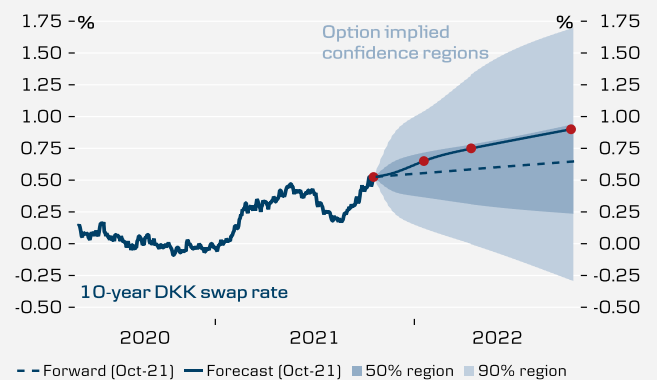
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

2Y DKK swap rates



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

10Y DKK swap rates



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

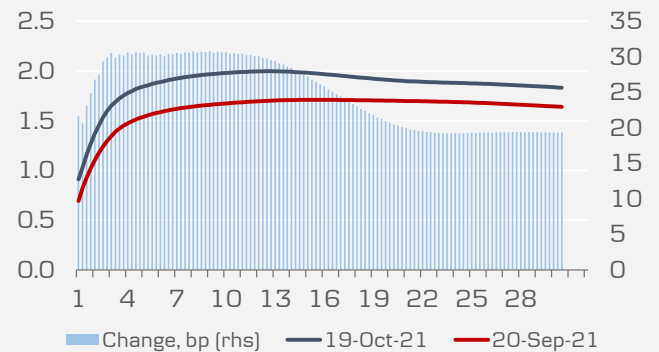
Norway forecast

NOK forecast summary

19/10/2021	--- Forecast ---				--- Fcst vs Fwd in bp ---		
NOK	Spot	+3m	+6m	+12m	+3m	+6m	+12m
<u>Money market</u>							
Deposit	0.25	0.50	0.75	1.00	-	-	-
3M	0.74	0.96	1.24	1.49	-4	0	-19
6M	0.90	1.16	1.37	1.65	-1	-4	-15
<u>Government bonds</u>							
2-year	1.05	1.00	1.10	1.75	-	-	-
5-year	1.57	1.60	1.60	1.70	-	-	-
10-year	1.73	1.80	1.85	1.90	-	-	-
<u>Swap rates</u>							
2-year	1.54	1.45	1.55	2.20	-25	-29	19
5-year	1.87	1.95	1.95	2.05	1	-4	-2
10-year	1.99	2.10	2.15	2.20	8	10	12

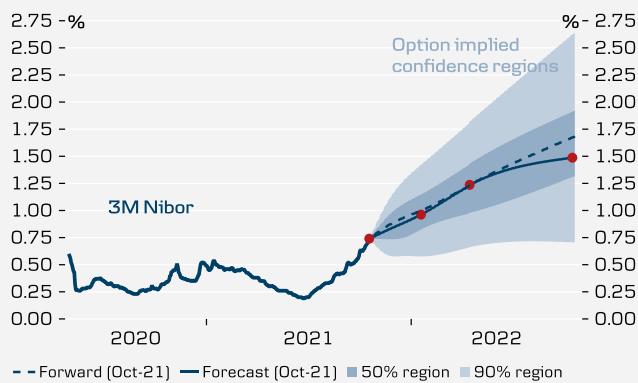
Source: Danske Bank

1M change in NOK swap (6M) rates



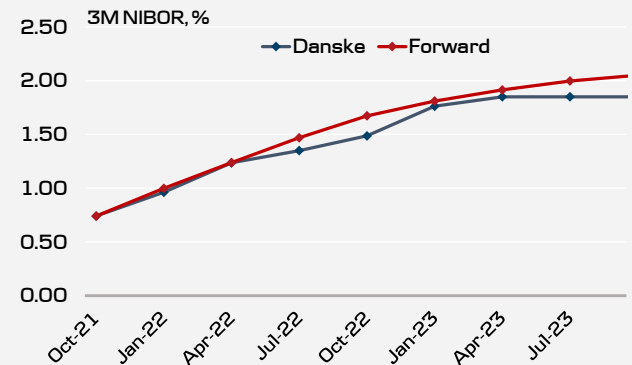
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

3M Nibor rates



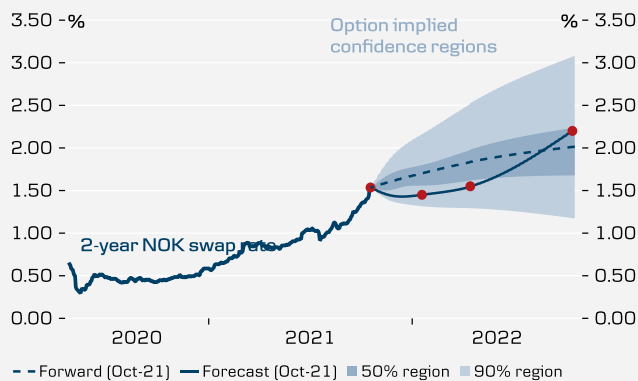
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

Danske Bank forecast and forwards



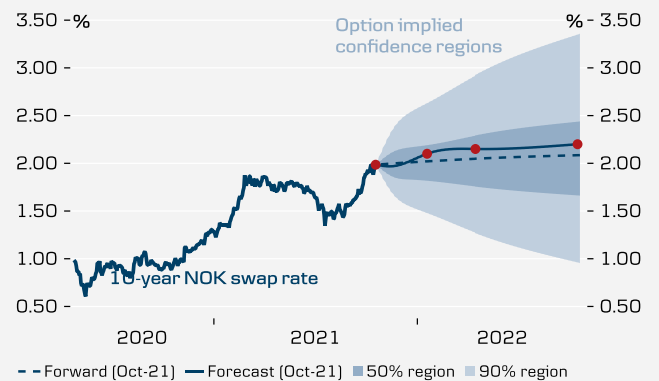
Note: Past performance is not a reliable guide to future returns
Source: Danske Bank

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
Source: Danske Bank

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