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**Crédit Agricole CIB expects bond yields to rise sharply
(Translated by Crédit Agricole CIB)**

PARIS, April 6 (Reuters) - Crédit Agricole Corporate and Investment Bank (CIB) is forecasting a sharp rise in eurozone bond yields, with the borrowing rate on Germany's benchmark 10-year Bund reaching 3.85% in September and 4.40% at the end of 2010, compared with this Tuesday's 3.15%.

With the gradual phase-out of non-conventional financing measures for the banking system and the gradual withdrawal of the supply of liquidity that the European Central Bank has distributed, European Union banks will reduce their government bond purchases, predicts Orlando Green, the bank's strategist.

Banks are obtaining financing at exceptional conditions from the ECB (which has a refinancing rate of 1%) and using this liquidity to purchase government bonds, which yield more than 3% in the 10-year area.

These massive purchases have kept long-term yields at very low levels, explained Orlando Green, who also calls for the ECB's refi rate to climb to 1.25% at the end of 2010 and 1.75% in the first quarter of 2011.

"The ECB is letting it be known that it will start to withdraw liquidity in the second quarter," he said during a meeting with the press.

This outlook is likely to lead banks to make purchases in the two-to-seven-year area of the yield curve and withdraw from the 10-year area.

Another factor putting pressure on rates is the explosion of deficits and government debt linked to the crisis, as well as questions surrounding the credit quality of sovereign issuers.

"Sovereign bond issuance will reach new highs, and this will put pressure on the long end of the curve," the strategist predicted.

In currencies, Daragh Maher, Deputy Head of Global Forex Strategy at CA CIB, does not think that the outlook for the ECB to raise interest rates sooner than the U.S. Federal Reserve will send the euro higher.

"Besides, the ECB's rate hike may meet with a chilly reception in the markets, coming against a backdrop of it anemic growth in the eurozone, weak inflation and more bank write-downs," he explained.

Besides the growth differential between the eurozone and the United States, the strategist predicts that "budgetary credibility will continue to pull the euro down."

"When you buy the euro, 52% of what you are buying is in countries rated AAA and 48% is non-AAA, but when you buy the U.S. dollar, you buy 100% AAA," he added. He expects the euro to slide to \$1.25 at the end of 2010 and to \$1.18 at the end of 2011, compared with \$1.3394 this Tuesday.

(Raoul Sachs, edited by Pascale Denis)

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