

Daiwa's View

10-year US yield topped 3.8%

- If projection for policy interest rate is unchanged, point of reference will be 3.95%

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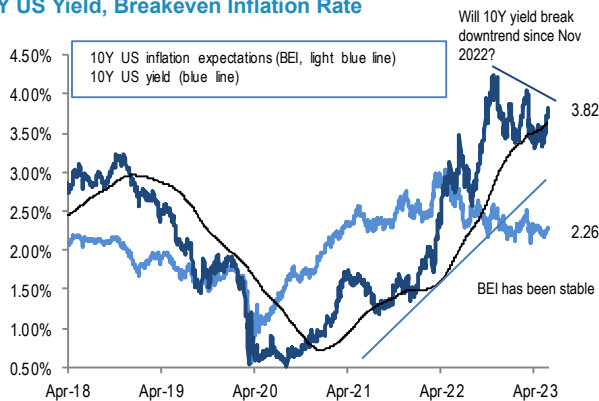
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10-year US yield topped 3.8%

Yesterday, the 2-year US yield and 10-year yield rose to 4.53% (+15bp) and 3.82% (+8bp), respectively. At the end of last week, the market was pricing in the probability of additional rate hikes by the time of the July FOMC meeting at only 20%, but that had risen to around 100% as of last night, suggesting a change in which additional rate hikes are now the main scenario. As previously reported, the 10-year US yield is now virtually approaching the limit for negative yields. Therefore, if the projected level of the terminal rate were to rise, the 10-year yield would also tend to slide to a similar degree.

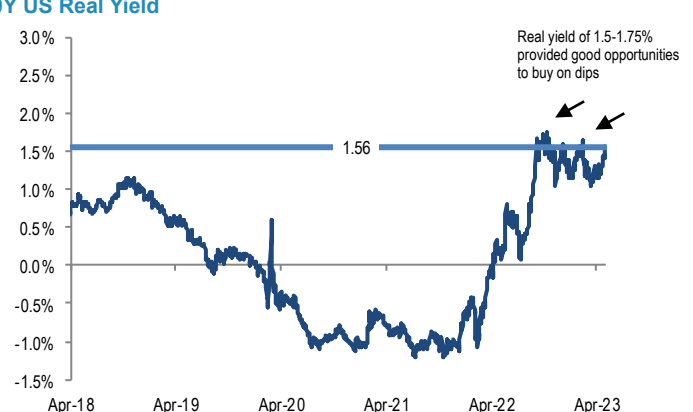
Meanwhile, when we observe the 10-year US yield as “breakeven inflation rate (BEI) + real yield,” we find that the 10-year BEI has been stable at around 2.3% (2.26% as of yesterday). In contrast, the real yield rose to 1.56% last night, just 18bp below the peak since the outbreak of the COVID-19 pandemic (1.74%) logged in November 2022, and 10bp below the peak immediately before the collapse of Silicon Valley Bank (1.66%).

10Y US Yield, Breakeven Inflation Rate



Source: Bloomberg; compiled by Daiwa Securities.

10Y US Real Yield



Source: Bloomberg; compiled by Daiwa Securities.

What is important from the standpoint of the real yield is whether projections for the real policy rate (i.e., federal funds rate – core PCE inflation) will change in the Summary of Economic Projections (SEP) to be released at the June FOMC meeting. This is because, when core PCE projections are raised in the SEP, changes in the real policy rate (i.e., the Fed's intended constraints) become limited, even if there is a rise in the median of dot plots. Since the pandemic, the 10-year real yield has formed a dip at 1.5-1.75%, which is largely in line with the peak of the real policy rate shown by the SEP. If the projection for the real policy rate does not change substantially in the SEP and the 10-year real yield peaks at around 1.7% this time, too, we forecast that the peak will be around 3.95% (given the BEI).

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