



17 January 2025

Charts of the Week: Yielding Conclusions

A HAVER ANALYTICS[®] podcast and publication

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Written by [Andy Cates](#), Senior Economist

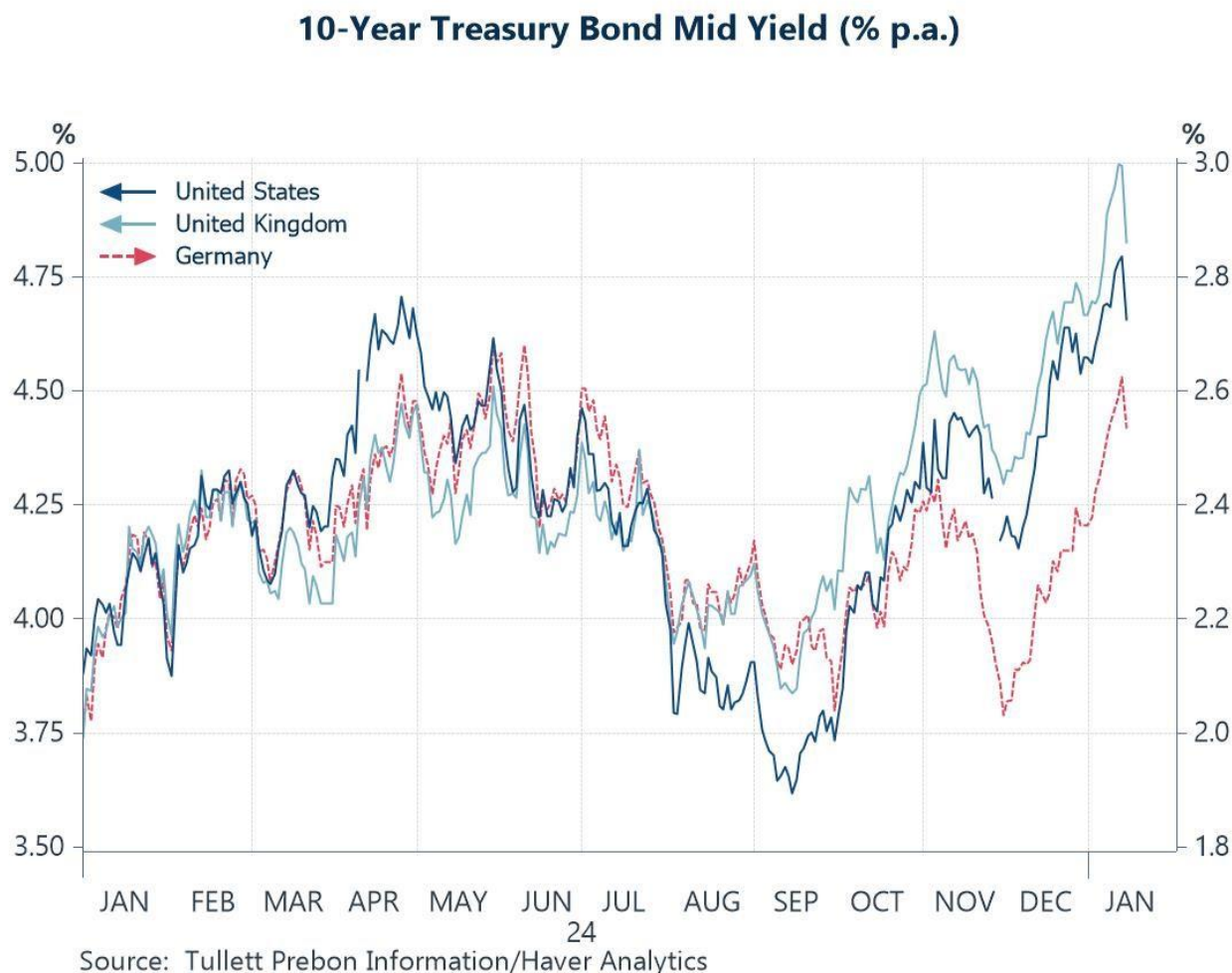
A steep sell-off in global bond markets has dominated financial headlines over the past week or so, drawing intense scrutiny from investors and policymakers alike (chart 1). The implications of this for the global economy, however, will depend on the underlying drivers that have been fuelling the rout. With our charts this week, we examine the data to identify some of the likely culprits. Inflation concerns are front and centre, with rising consumer prices in recent months (chart 2) reigniting fears of tighter monetary policy. Waning overseas demand, particularly from Japan and China (charts 3 and 4), may also be playing a significant role. Meanwhile, quantitative tightening (chart 5) has possibly siphoned liquidity from financial markets, while fiscal policy uncertainties are further rattling investor confidence. The easy conclusion is that all these factors—ranging from inflationary pressures to fiscal risks—are complicit to varying degrees. However, whether this marks the beginning of a broader reckoning or merely a passing squall hinges on how incoming data now evolve and how policymakers respond to these challenges. On that first point, weaker-than-expected inflation data from the US and UK this week appear to have stopped the rot for now (chart 6). On the latter, a new US administration could add another layer of unpredictability and the coming weeks could prove pivotal in shaping market expectations and the trajectory of the global economy.

Global bond markets

The sell-off in bond markets has been a global phenomenon. This is illustrated in chart 1 showing the movement in 10-year government bond yields in the US, UK and Germany over the past 12 months. Still, as

the chart's scaling indicates, divergences in yield levels between the US and UK versus Germany suggest different dynamics have been at play. The US and UK, for example, have been leading the sell-off compared with Germany (and other eurozone members).

Chart 1: 10-year bond yields in the US, UK and Germany



Global inflation expectations

That suggests that inflation expectations coupled with inflation uncertainty have been a driver of higher yields. Chart 2 below shows the evolution of consensus forecasts for CPI inflation in 2025 across the US, UK, the euro area (and Japan) throughout 2024. Notably, expectations for inflation in the US and UK inflation rose steadily over the year. In contrast, euro area inflation forecasts remained relatively stable, hovering close to the ECB's target of around 2%. We will focus more on this again below but for the record Japan's inflation forecasts saw a gradual uptick, at the same time, but remained modest, increasing from 1.5% to just above 2%.

Chart 2: The evolution of consensus CPI forecasts for 2025 in the US, Japan, euro area and UK

Blue Chip Survey: Evolution of Consensus Forecast for CPI Inflation in 2025

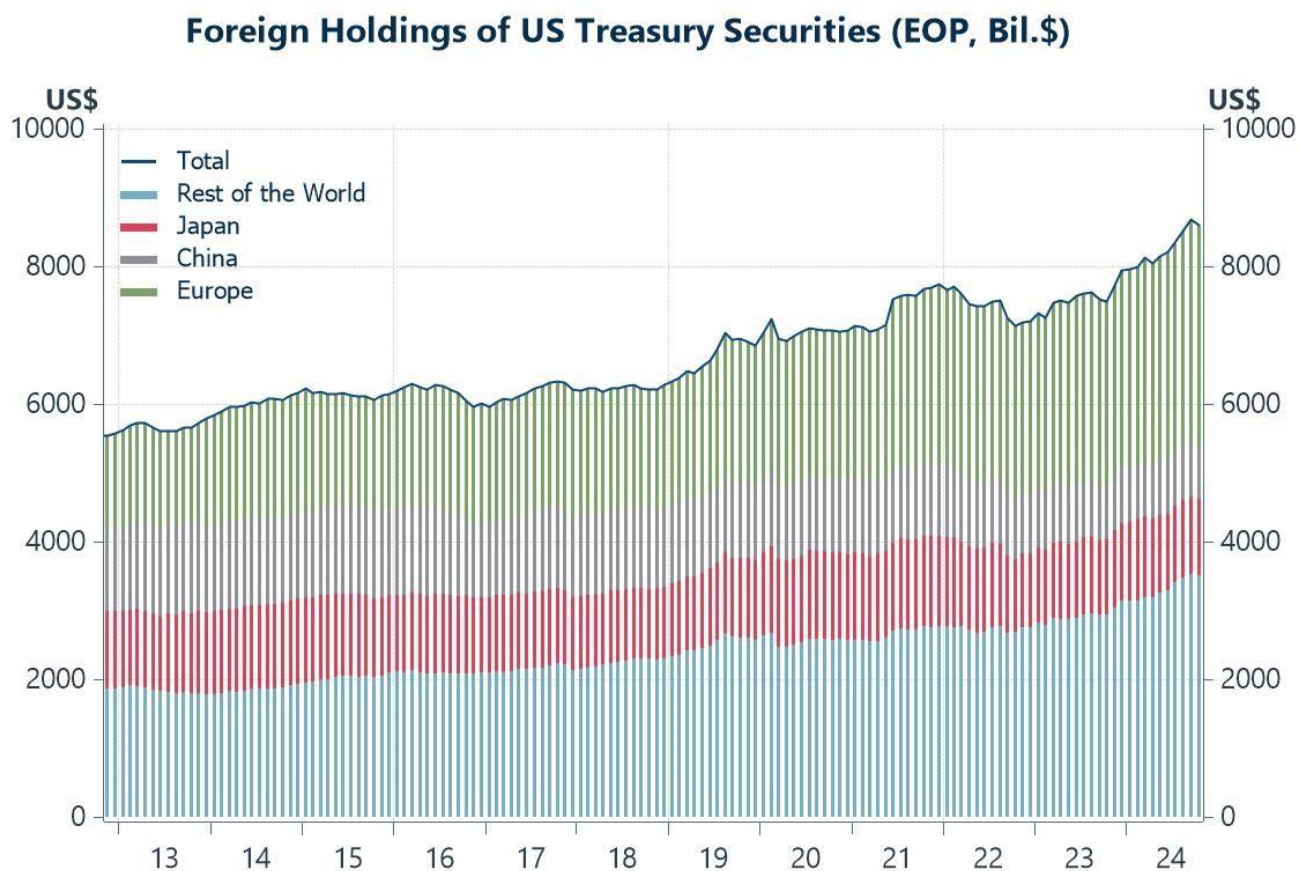


Source: Wolters Kluwer/Haver Analytics

Overseas demand

The role of overseas demand for US government debt in driving US yields higher could also have been significant. Chart 3 below shows the evolution of foreign holdings of US Treasury securities from 2013 to 2024, segmented by key regions: Japan, China, Europe, and the rest of the world. Over the period, total foreign holdings steadily increased, surpassing \$9 trillion by 2024. Notably, Japan has now emerged as the largest single holder of US Treasuries, with its share growing significantly, while China's holdings, though substantial, have showed some decline in recent years. But a new US administration led by President-elect Trump could now be further disrupting this picture. A potential pivot toward more protectionist policies alongside some question marks about the independence of the Fed and the dollar's role as the world's reserve currency could be combining to undermine overseas demand for safe-haven assets in the United States.

Chart 3: Overseas holdings of US Treasuries



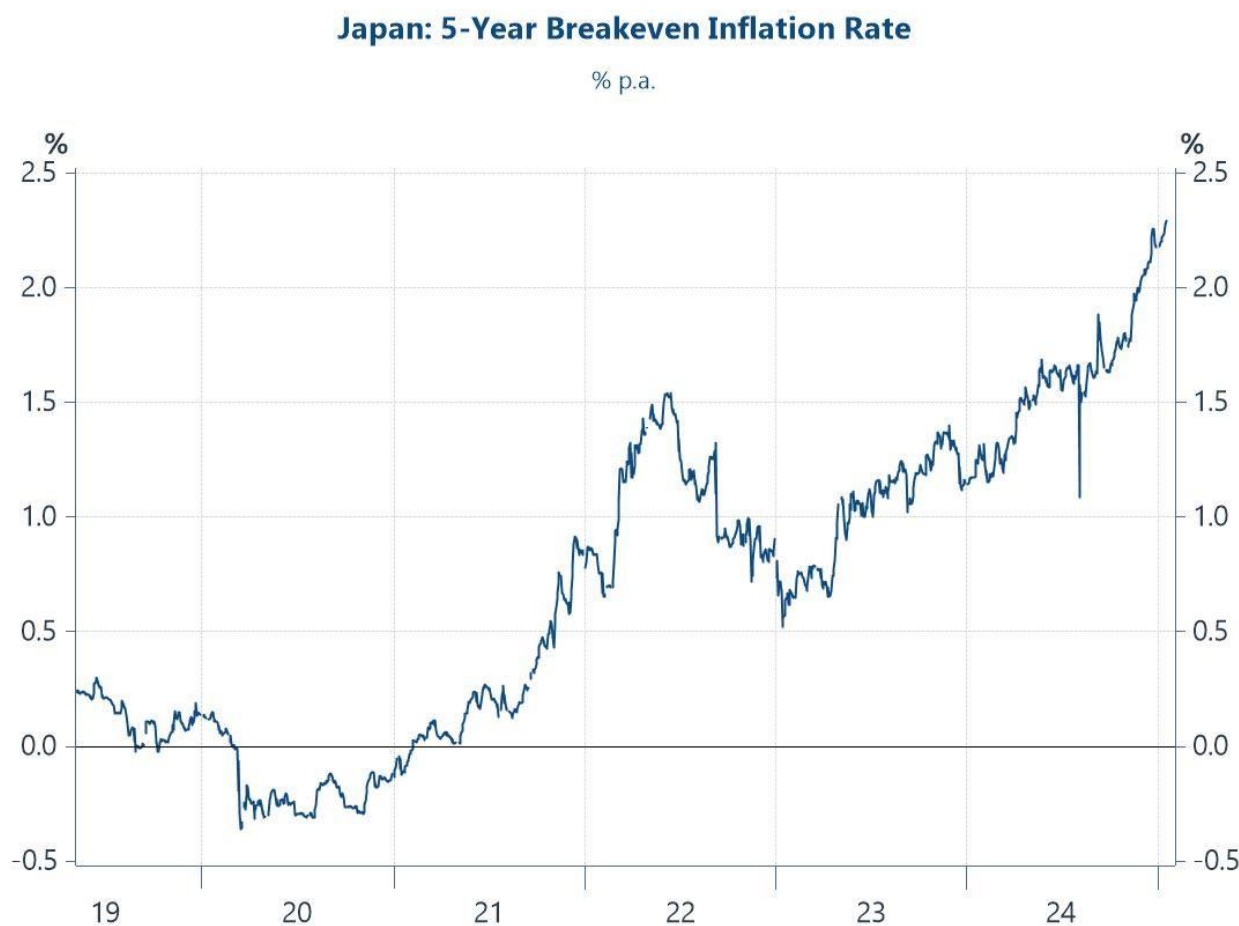
Source: U.S. Treasury/Haver Analytics

Japan

Japan is worthy of some further separate comment in this regard. That's because its capital flows are highly significant for global financial markets due to Japan's status as one of the world's largest net creditor nations. Changes in Japanese capital flows—such as a shift back to domestic assets driven by rising yields or inflation expectations—usually create ripple effects, influencing global bond yields, currency markets (particularly the yen), and risk sentiment. This is why, notwithstanding relatively stable consensus inflation forecasts for 2025 that we noted above, the sharp rise in longer-term market-based inflation forecasts is noteworthy. Chart 5 below illustrates Haver's calculations for the 5-year breakeven inflation rate in Japan from 2019 to 2024, and shows a sustained increase in those expectations in recent years. That follows several years of subdued expectations driven by entrenched deflationary pressures and weak demand. That the 5-year breakeven inflation rate crossed 2% toward the end of last year is also noteworthy given the Bank of Japan's inflation

objectives. For it potentially signals that monetary policy is still loose and that a further campaign to normalise policy beckons in the months ahead.

Chart 4: Haver's calculations for Japan's 5-year breakeven inflation rate

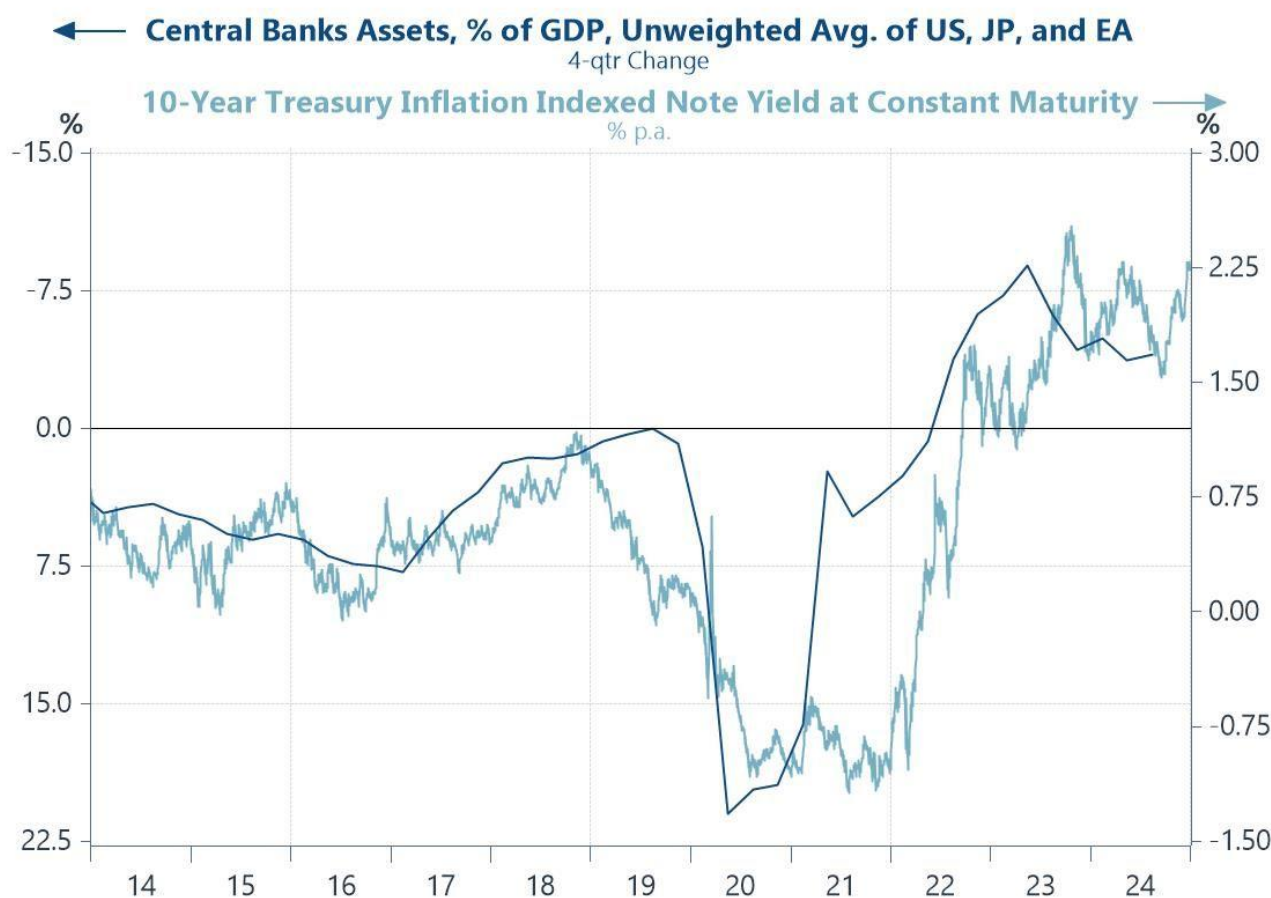


Source: Japan Securities Dealers Association/Haver Analytics

Quantitative tightening

Central bank monetary policies more generally are also worthy of some discussion and particularly their balance sheet policies. Chart 5 below depicts the relationship between central banks' asset holdings as a percentage of GDP (a four-quarter change of an unweighted average for the US, Japan, and the euro area) and the real 10-Year bond yield in the US. The chart underscores the close connection between central bank asset purchases and real yields. In combination with looser US fiscal policy – and a higher degree of government bond issuance – the underlying supply and demand dynamics in the US Treasury market (and other government debt markets) have been shifting. Reduced demand from central banks, in other words, has coincided with additional supply from governments, and thereby amplifying upward pressure on real yields.

Chart 5: Central bank balance sheets versus US 10-year real yields

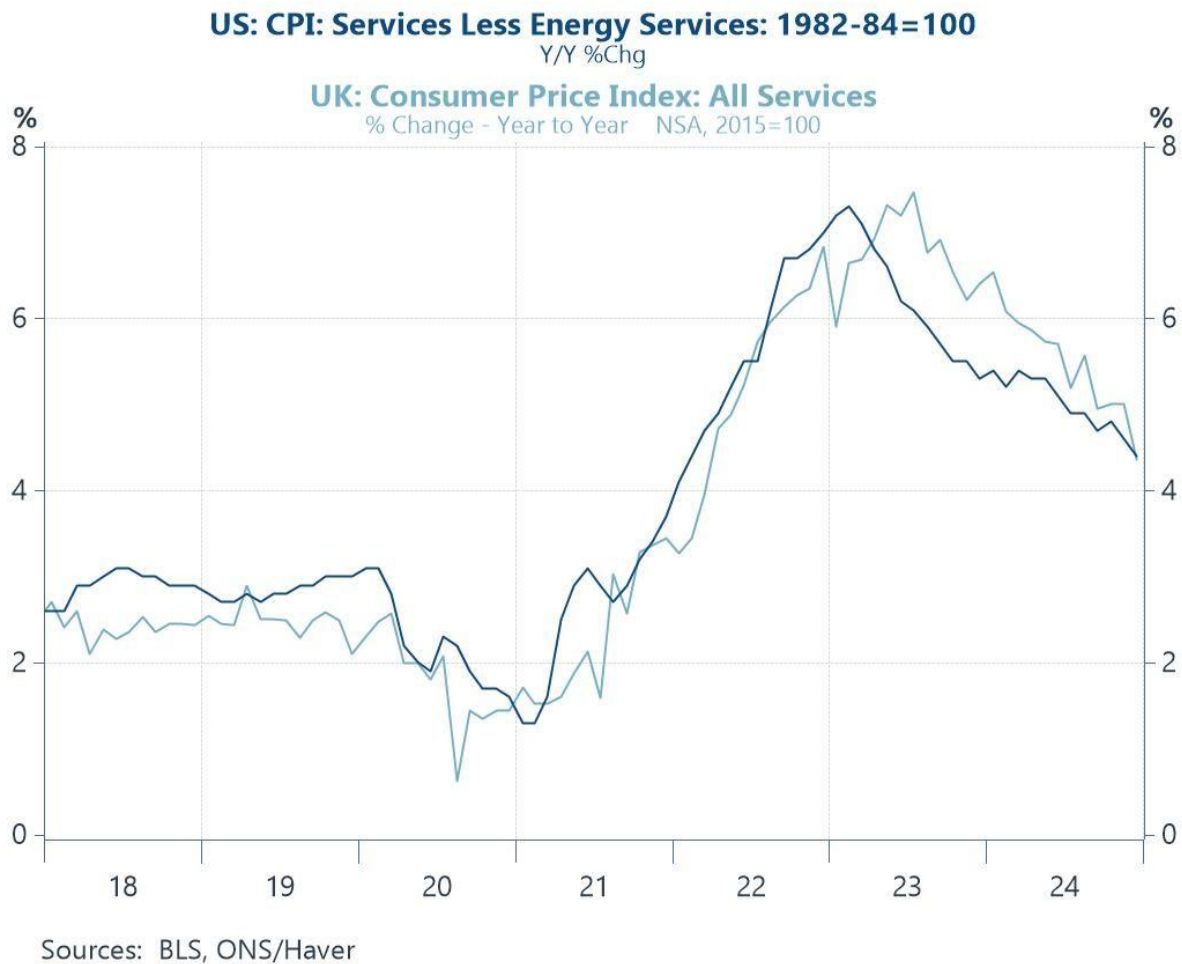


Source: Federal Reserve Board/Haver Analytics

US and UK inflation

The key takeaway from this discussion is that a confluence of factors has driven global yields higher in recent weeks. Inflation and monetary policy concerns, fiscal policy uncertainty, and shifts in capital flows have all likely contributed. As highlighted earlier, the trajectory of yields from here will hinge on incoming economic data and how policymakers respond. On that first point, however, it was notable that this week brought some encouraging news: the latest CPI inflation reports from both the US and UK came in weaker than expected. Notably, the details were also reassuring, with service-sector inflation showing further signs of moderation in both economies (see chart 6 below). This could ease some of the pressure on central banks to keep monetary policy restrictive in the period immediately ahead.

Chart 6: Service sector inflation in the US and UK



About the author



Haver Analytics is pleased to bring [Andy Cates's](#) commentaries on the state of the global economy to its clients. Andy has more than 25 years of experience forecasting the global economic outlook and in assessing the implications for policy settings and financial markets. He has held various senior positions in London in a number of Investment Banks including as Head of Developed Markets Economics at Nomura and as Chief Eurozone Economist at RBS. These followed a spell of 21 years as Senior International Economist at UBS, 5 of which were spent in Singapore. Prior to his time in financial services Andy was a UK economist at HM Treasury in London holding positions in the domestic forecasting and macroeconomic modelling units. He has a BA in Economics from the University of York and an MSc in Economics and Econometrics from the University of Southampton.

Series info:

Chart 1: 10-year bond yields in the US, UK and Germany

Series 1: R111MA@INTDAILY

R111MA@INTDAILY [United States: 10 Year Treasury Bond Mid Yield (% p.a.)]

Series 2: R112MA@INTDAILY

R112MA@INTDAILY [United Kingdom: 10 Year Treasury Bond Mid Yield (% p.a.)]

Series 3: R134MA@INTDAILY

R134MA@INTDAILY [Germany: 10 Year Treasury Bond Mid Yield (% p.a.)]

Chart 2: The evolution of consensus CPI forecasts for 2025 in the US, Japan, euro area and UK

Series 1: DAAD25@BLUECHIP

DAAD25@BLUECHIP [BCEI: US Consumer Price Index: 2025 Forecasts: Consensus (Y/Y %Chg)]

Series 2: DGBD25@BLUECHIP

DGBD25@BLUECHIP [BCEI: Change in Consumer Price Index: UK: Consensus: 2025 Forecast (%)]

Series 3: DJPD25@BLUECHIP

DJPD25@BLUECHIP [BCEI: Change in Consumer Price Index: Japan: Consensus: 2025 Forecast (%)]

Series 4: DEZD25@BLUECHIP

DEZD25@BLUECHIP [BCEI: Change in Consumer Price Index: Euro area: Consensus: 2025 Forecast (%)]

Chart 3: Overseas holdings of US Treasuries

Series 1: FH001TB@USINT

FH001TB@USINT [Foreign Holdings of US Treasury Securities (EOP, Bil.\$)]

Series 2: (((FH001TB@USINT - FH158TB@USINT) - FH170TB@USINT) - FH924TB@USINT)

FH001TB@USINT [Foreign Holdings of US Treasury Securities (EOP, Bil.\$)]

FH158TB@USINT [Japan: Holdings of US Treasury Securities (EOP, Bil.\$)]

FH170TB@USINT [Europe: Holdings of US Treasury Securities (EOP, Bil.\$)]

FH924TB@USINT [China: Holdings of US Treasury Securities (EOP, Bil.\$)]

Series 3: FH158TB@USINT

FH158TB@USINT [Japan: Holdings of US Treasury Securities (EOP, Bil.\$)]

Series 4: FH924TB@USINT

FH924TB@USINT [China: Holdings of US Treasury Securities (EOP, Bil.\$)]

Series 5: FH170TB@USINT

FH170TB@USINT [Europe: Holdings of US Treasury Securities (EOP, Bil.\$)]

Chart 4: Haver's calculations for Japan's 5-year breakeven inflation rate

Series 1: R158F5V@INTDAILY

R158F5V@INTDAILY [Japan: 5 Year Breakeven Inflation Rate (% p.a.)]

Chart 5: Central bank balance sheets versus US 10-year real yields

Series 1: diff(((N023FAPG@G10 + N158FAPG@G10) + N111FAPG@G10) / 3),4)

N023FAPG@G10 [Euro Area: Central Bank Assets as a % of GDP (NSA, %)]

N158FAPG@G10 [Japan: Central Bank Assets as a % of GDP (NSA, %)]

N111FAPG@G10 [U.S.: Central Bank Assets as a % of GDP (NSA, %)]

3

Series 2: FII10@DAILY

FII10@DAILY [10-Year Treasury Inflation Indexed Note Yield at Constant Maturity (% p.a.)]

Chart 6: Exports less imports of oil and petroleum products in selected major economies

Series 1: YPCUSSLE@USECON

YPCUSSLE@USECON [CPI-U: Services Less Energy Services: 1982-84=100 (Y/Y %Chg)]

Series 2: yyr%(D7F5@UK)

D7F5@UK [UK: Consumer Price Index: All Services (NSA, 2015=100)]

Get in touch

Drop us a line on sales@haver.com and someone from our team will connect with you to discuss your data needs.

