

Flash Update: US Rate Markets – Monday 3/25/2024

- Rates creep higher this morning on Hawkish Fed-speak by Atlanta Fed President Raphael Bostic
- Bostic says he favors one rate cut this year, thinks Fed can be patient
- Next batch of key economic data starts later this week
- We see GDP released on 3/28 and PCE, Personal Income and Personal Spending released on 3/29
- There are a number of Fed officials scheduled to speak this week (See Chart 3)

Good Morning!

US Treasury and SOFR swap rates edged 2-5 bps higher this morning on hawkish comments from Atlanta Fed President Bostic (See Chart 1). Bostic said that he still favors one rate cut this year – the Fed’s new consensus dot-plot shows three rate cuts penciled in for 2024, and that is what the market has priced into the forward curve. He also stated that cutting rates “too soon could be more disruptive” than waiting a bit too long to cut. Bostic was also optimistic on the economy – he said that “if the economy performs as expected, the Fed can afford to be patient”. He added that he does expect the economy and inflation to slow gradually as we move through 2024. Bostic is a known hawk – or more accurately, a known proponent of the Fed’s “wait-and-see” mode, so his comments are being taken with a grain of salt by the market. That said, his comments were enough to slow down the market’s rate cut euphoria and push rates a bit higher this morning. There are a host of Fed officials scheduled to speak this week (See Chart 3), and we see the next batch of important economic data later this week. The data highlights are final 4Q GDP on 3/28 and PCE, Personal Consumption and Personal Expenditures on 3/29. With economic growth and inflation squarely in focus for a data-driven Fed, the data later this week is highly anticipated.

Chart 1: US RATES SNAPSHOT: 10:30 AM Eastern

UST YIELDS | SOFR SWAP SPREADS | SOFR SWAP RATES

GV	Ask/Chg	SOFR/GV	SOFR OIS
2Y	4.621 +0.031	-11.0800 -0.0600	4.5104 +0.0308
3Y	4.386 +0.034	-15.0400 +0.1200	4.2382 +0.0375
4Y	4.309 +0.040	-22.0000 +0.5000	4.0859 +0.0419
5Y	4.223 +0.041	-22.7700 +0.4200	3.9960 +0.0445
7Y	4.242 +0.042	-32.7000 +0.3000	3.9156 +0.0447
10Y	4.239 +0.042	-36.1300 +0.1500	3.8806 +0.0441
20Y	4.503 +0.038	-64.1300 +0.1800	3.8639 +0.0409
30Y	4.416 +0.039	-73.1000 +0.0300	3.6859 +0.0380

Source: Bloomberg, LLP | 10:30 AM NY Rates Snapshot

Chart 2: Economists See Upper Bound Fed Funds Rate at 5.25% By June Meeting

The Bloomberg table below shows the results of latest Bloomberg survey. Economists were asked to forecast the upper-bound of the fed funds rate through the 2Q of 2026. You can see the median shows three 25 bp rate cuts during 2024 – that is in sync with the Fed’s most recent dot-plot and forward market pricing. That is a rare

alignment of economists, traders and the Fed! However, given Bostic's comments this morning, the current alignment could decouple quickly.

Fed Funds Upper Bound Forecasts: Bloomberg Economists Survey

	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q
	2024	2024	2024	2025	2025	2025	2025	2026	2026
# of replies	72	72	75	66	61	57	59	33	32
Median	5.25%	5.00%	4.75%	4.25%	4.00%	3.75%	3.50%	3.25%	3.13%
Average	5.29%	4.97%	4.62%	4.28%	3.95%	3.70%	3.50%	3.33%	3.23%
High Forecast	5.50%	5.50%	5.25%	5.00%	5.00%	5.00%	5.25%	5.25%	5.25%
Low Forecast	5.00%	4.50%	4.00%	3.25%	2.75%	2.25%	2.00%	2.00%	2.00%

Source: Bloomberg, LLP | Upper Bound Fed Funds Forecasts – Economists

Chart 3: Federal Reserve Speech Schedule: Week of 3/25

There are a number of Fed officials scheduled to speak this week. Atlanta Fed President Bostic's comments this morning pushed rates higher when he directly stated he favors one 25 bp rate cut this year. The market mostly ignored the comments, but rates still edged higher. The market wants three rate cuts this year. Should they start to doubt the Fed will deliver three rate cuts this year, forward pricing will need to adjust – higher. Fed officials are back on the tape this week - the market will be listening.

Fed Officials On The Tape This Week:

	Date	Time	A	M	R	Event
21)	03/25	08:25				Fed's Bostic Participates in Moderated Conversation
22)	03/25	09:05				Fed's Goolsbee Appears on Yahoo Finance
23)	03/25	10:30				Fed's Cook Speaks on Dual Mandate
24)	03/27	18:00				Fed's Waller Speaks on Economic Outlook
25)	03/29	11:15				Fed's Daly Delivers Opening Remarks
26)	03/29	11:30				Fed's Powell Speaks in Moderated Discussion

Product Update:

Week of 3/25/24 - What We Are Seeing In The Rates Market

New cap volume continues to increase as do borrowers seeking to extend existing caps. Despite a shift in market pricing regarding Fed rate cuts, the forward curve is *still* pricing in ~3 rate cuts for 2024 – just starting a bit later in the year. Should inflation continue to trend higher, rate cut expectations may be reduced further.



Given the uncertainty that still remains about forward rates, many clients are grappling with when or if to extend. This is a difficult question – our advice has been to monitor the market closely and be on-boarded and ready to trade, should the market move in your favor. We also advise borrowers to check the market pricing for extensions, similar to how you purchased the original cap. Market pricing discovery is a key component to any cap transaction – new caps, extensions or terminations.

We also encourage our clients to speak to their lenders. In some cases recently we have seen lenders approve shorter term extensions (i.e. 3 months) – some borrowers may need to extend, but not for the *full* year. Other borrowers are simply looking to dynamically manage hedging rate risk by entering shorter term caps and hoping cap premium costs will drop ahead of the next cap purchase. This is not without risk, but could be a viable strategy if you believe rate are going down next year.

There is an increasing interest in exploring interest rate swaps as a possible hedge alternative. IR Swaps lock in a synthetic fixed rate and do not require an upfront premium. Unlike an interest rate cap, swaps are secured derivatives, so the counterparty selection process is more challenging with a swap. There are also additional variables that factor into the decision to pursue an interest rate swap, or to unwind an existing swap. *Please let us know if you would like to learn more about interest rate swaps.*

On another front, borrowers who have “floors” embedded in their loan have been considering purchasing a separate, stand-alone interest rate floor to *offset* the loan floor. Borrowers with a loan floor will *not* be able to benefit from floating rates that drop below the loan floor rate. They will miss out on the benefit of lower floating rates, which depending on the rate environment can be significant. To offset the loan floor, borrowers can purchase an interest rate floor which will payout should floating rates drop below the floor’s strike rate. Details vary depending on the individual situation – some borrowers prefer to choose a strike on the floor that matches the floor rate on the loan, whereas others look to use a strike rate below the loan floor. (For example: Your loan floor is 3.50% - the floor you purchase can be priced at the loan floor of 3.50%, or you could look at a strike of 3.00%). The lower the floor strike, the cheaper the premium cost of the floor. Pricing ultimately depends on the individual situation and objective.

We also continue to see clients grappling with ways to manage burdensome replacement cap escrow costs. In certain cases there *may* be a way to restructure the existing cap to extract value which can offset escrow created cash-flow pressure. Short of biting the bullet and purchasing the replacement cap and ceasing escrow deposits, restructuring the cap can add risk. Many of the solutions are designed to alleviate short term cash flow pressure but as mentioned, often create additional rate risk.

Please contact us if you would like to discuss an upcoming rate cap extension, explore ways to reduce or eliminate escrow deposits for replacement caps or learn more about interest rate Swaps or Floors.

Disclaimer: *The information provided in this communication is intended for discussion purposes only. Nothing presented in this communication should be taken as a recommendation or forecast. All market data shown is indicative only and subject to change depending on current market conditions.*

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Rate Cap Advisors was established in 2015 that focus on providing commercial real estate interest rate cap solutions. Our innovation and desire to explore new possibilities that benefit our clients have allowed us to save our clients millions of dollars. No matter the service or product, we take great pride in our pursuit of perfection with a unparalleled closing track record.

