Please see below for the RCA|AST Rate Market Update for January 24, 2023. Please let us know if you would like additional market color or have any questions. We are also always happy to provide indications for Caps, Swaps, Terminations or other derivative hedging products. Please feel free to reach out anytime! *-RCA|AST Interest Rate Hedging Desk*

RCA|AST RATE MARKET UPDATE:

- **U.S. Treasury and SOFR swap rates lower for the first time in 4 days**
- **Earnings season reaches its peak this week**
- **Big Tech and Industrials set to report this week; key focus for rates and equity markets**
- **GDP data prints Thursday, Jan 26**
- ***Next FOMC meeting: Feb 1, 2023***

U.S. Treasury and SOFR swap yields were lower this morning for the first time in 4 days as the rate market braces for a host of earning data set for release this week, particularly Big Tech and U.S. Industrials. Market participants are likely seeking the safe haven of U.S. Treasuries while they digest and analyze the myriad of crucial earnings reports the market will see this week.

As the Fed enters the blackout period ahead of its Feb. 1 meeting, markets have priced in a smaller 25-basis-point hike. Even as Fed officials emphatically state rates must stay higher for longer, rate traders and market participants remain skeptical. They still do not believe that monetary policymakers will go above 5%, and many see the Fed cutting rates by the end of the year – as mentioned, this is in stark contrast to what FOMC members were signaling prior to the blackout period. There has been a growing sentiment in the market that inflation has peaked and is rapidly moving toward the Fed's target level and this sentiment was bolstered by the last round of better than expected employment and inflation data. The Fed, on the other hand, has cautioned against jumping to any conclusions and has been adamant that they will stay on the current course of hiking rates. They have also consistently stated that they will need to keep rates higher for longer in order to keep inflation at bay. These conflicting market forces will continue to grapple ahead of next week's meeting. Depending on the outcome of that meeting, the disconnect between the market and the Fed could deepen. There is the *slight* possibility that the Fed unexpectedly shifts gears to a neutral or more accommodative monetary policy, but this is unlikely given the Fed's position to date.

The market will get some important manufacturing, service and housing data this week and we see GDP data print on Thursday. None of these numbers are likely to sway the FOMC from raising rates 25 basis points next week, but the market may nonetheless react to the data based on the hopeful expectation the Fed will need to pivot sooner rather than later. This is likely to create additional rate market volatility and we expect volatility to continue in the run up the FOMC meeting next week. The market will also be keeping a close eye on the U.S. debt ceiling “battle” currently underway in Washington. This issue could impact the U.S. Treasury market and may also impact the Fed’s current quantitative tightening that is currently underway. We will be tracking this and will report any major developments that could impact the broader rate market.

RCA CHART OF THE DAY:

The Bloomberg chart below depicts U.S. CPI for the past 15 months. I thought it made sense to show this chart as we steam towards the FOMC meeting next week. The market is increasingly interpreting recent inflation data as a sign that the Fed can and should pivot to a more accommodative monetary policy, or risk over-tightening and causing a recession. The FOMC, on the other hand, views this information as encouraging, but has remained steadfast that despite the improvement in inflation, we are still a long way from their target inflation level. They have consistently signaled that they will need to keep moving rates higher and hold them there for some time. Furthermore, Fed officials are certainly aware of market sentiment and the possibility of a recession, but they believe that the economy can withstand the rate increases without causing a major recession. This is in essence the dichotomy that currently exists in the market.

CURRENT U.S. TREASURY & SOFR SWAP RATES:

- **Short-term U.S. Treasury rates relatively flat week-on-week, despite intra-day volatility.**
- **Sustained curve inversion underscores market uncertainty**

Term:	U.S. Treasury Rates	1 Week Change
2-Year	4.232%	+2.5 bps
3-Year	3.894%	+1.2 bps
10-Year	3.513%	-3.8 bps

Term	SOFR Swap Rates	1 Week Change
2-Year	4.211%	+1.9 bps
3-Year	3.755%	+1.5 bps
10-Year	3.193%	-4.1 bps

Best Regards,

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