Flash Update: US Rate Markets – Friday 8/16/2024

- **Rates drift lower on weaker-than-expected housing data and dovish Fed-speak**
- **New Home Construction falls to lowest level since May 2020**
- **Chicago Fed President Goolsbee said the economy is flashing "warning signs"**
- **However, Consumer Sentiment increased for the first time in five months**
- **Currently, SOFR swap rates are ~1-3 bps lower this morning**
- **Elevated intra-day rate volatility is likely to continue for the near term**
- **Next Up: Chairman Powell's keynote address at the Jackson Hole Economic Policy Symposium**
- **Chairman Powell is scheduled to speak next Friday, August 23rd at 10:00 am eastern**

US Treasury Yields and SOFR swap rates slid lower this morning on dovish Fed-speak and weaker-than-forecasted housing data. The drop in rates stalled after better-than-expected Consumer Sentiment data printed at 10:00 am. SOFR swap rates are currently down ~1-3 bps across the curve (See Chart 1). The rate movement this morning further underscores the intra-day rate volatility the market can expect in the near term.

This morning Federal Reserve Bank of Chicago President Austan Goolsbee said the labor market and some leading indicators on the economy are flashing "warning signs", adding there are concerns unemployment will continue to rise. His comments tempered yesterday's hot Retail Sales data and pushed rates lower as traders continue to assess the path forward for the Fed. Weaker-than-expected housing data also contributed to lower rates this morning – new-home construction in the US fell in July to the lowest level since May 2020. Consumer Sentiment data released at 10:00 am showed consumers remain optimistic, which bodes well for consumer spending. Consumer Sentiment rose for the first time in five months and helped to offset the weaker housing data seen earlier this morning.

The next big event on the horizon for rate markets is the Fed's annual Jackson Hole Economic Policy Symposium, to be held from August 22-24. The Jackson Hole event is widely anticipated – market participants are hoping Fed officials will provide additional clarity on rate cuts, particularly with the latest batch of data in hand. Federal Reserve Chair Powell will be the keynote speaker at the conference. Chairman Powell will speak at 10:00 am eastern on Friday, August 23. The topic of his keynote address will be the "US Economic Outlook". Powell's comments are *highly* anticipated by market participants. His comments could set the tone for rates for the remainder of the year. We will have more details on the Jackson Hole event next week.

CHART 1: ***US RATES SNAPSHOT: 10:00 AM Eastern***

UST YIELDS **SWAP SPREADS** **SOFR SWAP RATES**

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2Y	4.069	-0.025	-20.1101	-0.2501	3.8710	-0.0250
3Y	3.876	-0.023	-22.8638	-0.0538	3.6500	-0.0214
4Y	3.815	-0.017	-28.7300	+0.1450	3.5378	-0.0187
5Y	3.771	-0.018	-28.8489	+0.2861	3.4826	-0.0170
7Y	3.807	-0.015	-36.0925	+0.1175	3.4475	-0.0156
10Y	3.894	-0.018	-43.8650	+0.2600	3.4576	-0.0153
20Y	4.255	-0.017	-75.4850	+0.2200	3.5026	-0.0144
30Y	4.153	-0.017	-80.3644	+0.4182	3.3505	-0.0135

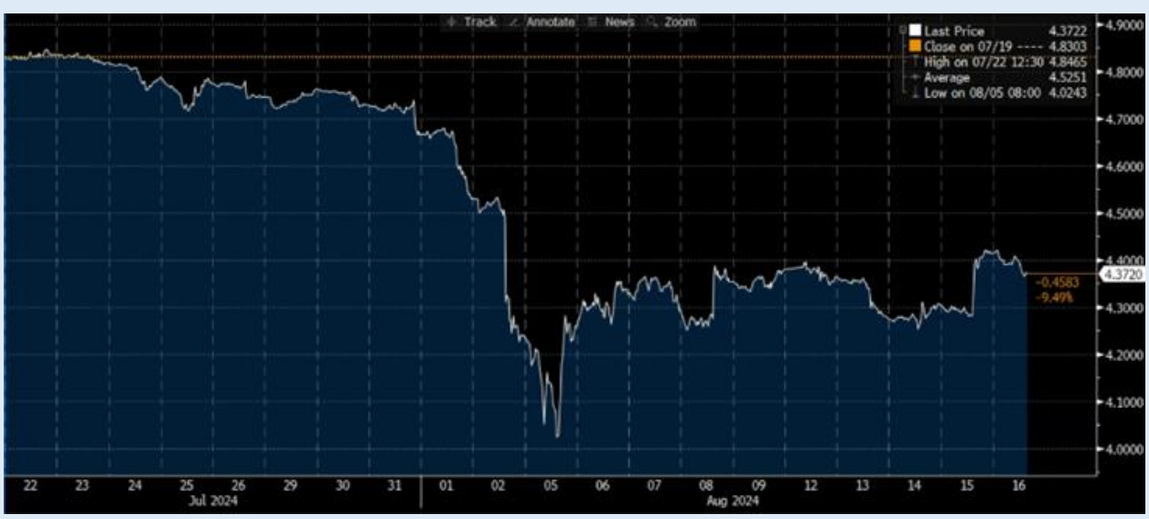
Source: Bloomberg, LLP | 10:00 AM NY Rates Snapshot

Note: ***First column is the current market level, second column is the change on the day; 'Red' = Lower; 'Green' = Higher; 'White' denotes active trading***

CHART 2: ***SOFR SWAP RATES DRIFT LOWER ON WEAK HOUSING DATA, DOVISH FED-SPEAK***

SOFR swap rates dipped lower this morning on disappointing housing data and dovish Fed-speak. Volatility remains elevated, and I expect that to be the case for the near term. Swap rates will be the most volatile at the Fed-sensitive short-end of the curve, particularly 1-year and 2-year SOFR swaps. Traders are likely to continue to adjust forward pricing as new economic data is released. That said, SOFR swap rates remain near the lows for the prior 12-months and cap premiums are also the lowest we have seen in months.

CHART 2: 1Y SOFR SWAP RATE, PRIOR 30 DAYS



Source: Bloomberg, LLP | 1Y SOFR SWAP RATE, PRIOR 30 DAYS

CHART 3: ***MARKET EXPECTS FED TO CUT RATES IN SEPTEMBER; 50 BP CUT STILL UP FOR DEBATE***

The Fed is widely expected to reduce borrowing costs at their next gathering Sept. 17-18, but there is still widespread speculation around just how big that cut will be. While most economists expect a 25 bp reduction, a few prominent forecasters (including Citigroup Inc. and JPMorgan Chase & Co.) anticipate a larger, 50 basis point adjustment. The lack of firm conviction in the market surrounding the magnitude of 2024 rate cuts will keep rates volatile. Current market pricing supports a 25 bp rate cut in September, but after today's drop in swap rates, forward pricing shows ~30 bps of rate cuts in September. That implies the market thinks there is still a chance the Fed could cut rates 50 bps in September.

The next big event for the market is Chairman Powell's testimony next week. He is expected to say that the balance of risk between the Fed's mandates – full employment and low inflation - is about even. I expect him to signal a rate cut is coming, but not to indicate whether it will be a 25 basis point cut or a 50 bp cut. From my perspective, I think the question of "25 or 50" in September will ultimately depend on the August jobs report. The GDP data on 8/29 and the PCE inflation data on 8/30 are also important, but I believe it will come down to the August Employment Report. Weaker-than-expected jobs data would likely reignite talk for a 50 bp rate cut at the September FOMC meeting.

CHART 3: Current Fed Rate Cut Expectations Through Jan-2025

Source: Bloomberg, LLP | FED RATE CUT EXPECTATIONS

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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