

## AST DEFEASANCE RATE MARKET UPDATE

Good Morning! Please see below for the RCA | AST Defeasance *Rate Market Update* for June 27, 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 your defeasance needs, or for interest rate caps, swaps or other derivative hedging products. Please feel free to reach out anytime! -RCA | AST Interest Rate Hedging Desk

### RATE MARKET UPDATE: June 27, 2023 | Range Bound Rate Market Awaits Data

- Rates steady as market participants await key economic data
- Odds growing for a 25 bp rate hike at the July 26 FOMC meeting. (Approx 80% chance for +25 bps)
- Markets calm after Russia political drama quiets, though concerns remain
- US market focused on growth and inflation for clues on forward monetary policy

Rates have remained range bound over the past week as market participants wait for economic data and listen for monetary policy direction from Fed officials. You can see from Table A below (Source: Bloomberg) that the Fed-sensitive 2-year SOFR Swap rate initially moved higher during the second day of Powell’s testimony to Congress – the market finally heard the hawkish slant. However, mixed Fed-speak this week and the Russian political turmoil put the brakes on higher rates and led to a flight to quality to safer US Treasuries. This suppressed market rates and since then, the market has been cautiously trading in a relatively tight range. This morning rates opened 1-2 basis points lower, but reversed on stronger than expected New Home Sales, which *surged* to +12.2%! (+12.2% actual vs. -1.2% expected!) This number should keep the bias toward rates drifting higher as we await the other important economic data we see later this week. Rates are currently higher by 2-4 basis points after the strong housing data.

**TABLE A: 2Y SOFR SWAP RATE**

Date	Last Price
Fr 06/30/23	
Th 06/29/23	
We 06/28/23	
Tu 06/27/23	4.6585
Mo 06/26/23	4.6255
Fr 06/23/23	4.6313
Th 06/22/23	4.6892
We 06/21/23	4.6122
Tu 06/20/23	4.6000
Mo 06/19/23	



Source: Bloomberg, LLP

As mentioned, the market will see some important economic data the rest of the week, so we do expect volatility to pick-up as we move through the week. We see 1Q GDP, Personal Consumption and Pending Home Sales data on 6/29 and Personal Spending, PCE Inflation Data and the Univ. of Michigan economic data series on 6/30. This is a big week for data and it could set the rate tone for the summer.

June 30 is also the LIBOR “sunset” date, month-end, quarter-end and the half-year mark for 2023, so it is possible that will create some additional rate volatility as we approach month-end. Large institutional market participants are often active at month end/quarter end, which can add to market volatility. The cessation of LIBOR may also contribute to market volatility as traders scramble to transition LIBOR trades prior to the 6/30 deadline.

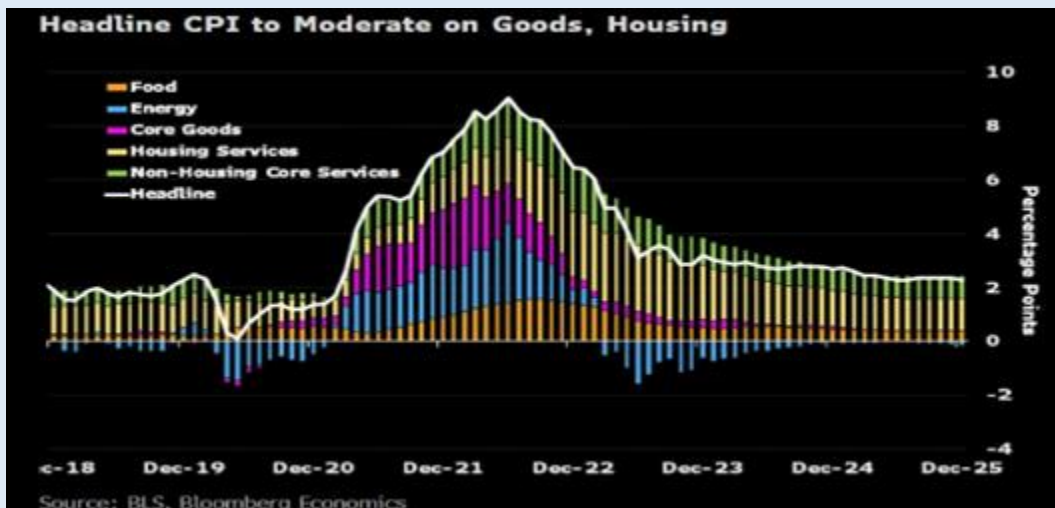
### CHART 1: 2Y, 3Y & 5Y SOFR SWAP RATES – PRIOR 30 DAYS

The Bloomberg chart below shows 2y (white), 3y (blue) and 5y (orange) SOFR Interest Rate Swap rates (a key driver for cap premiums) for the prior 30 days. You can see term SOFR rates have bounced around the past 30 days but have been largely range bound as the market lacks a clear direction forward for rates. Powell’s recent testimony to Congress and hawkish Fed-speak have underscored the Fed’s determination to stifle inflation. That said, they have strongly hinted that although further rate hikes may be warranted, they are nearing the end of this historic tightening cycle. They have stated that they will be monitoring the data closely to determine when to stop raising rates and shift monetary policy to a neutral stance. Market participants seem to be coming to terms with the view that the Federal Reserve will not cut interest rates this year and that other central banks will continue raising rates to quell inflation. At the moment market participants see the Fed hiking by 25 basis points next month. There is also growing sentiment that given the FOMC is nearing the end of this cycle, they may in fact be able to engineer a “soft landing” and avoid a severe or prolonged recession.



**CHART 2: Headline CPI Projected Lower**

The below Bloomberg chart details economist’s projections for Headline CPI through 2025. I found this chart compelling as it clearly shows the recent disinflation trend is projected to continue and to be within shouting distance of the Fed’s communicated 2.00% target by early 2024. Market participants and the FOMC will be watching the next batch of PCE and CPI data for evidence inflation continues to drop. We see the next PCE data on 6/30 and the next CPI data prints on 7/14.



**CHART 3: Bloomberg Economists Poll: Latest Fed Funds Rate Projections**

We end this update with an “FYI” chart for your reference. The below Bloomberg chart details economist’s quarterly projections for the Fed Funds Rate until 4Q 2025. Economists expect 1 to 2 more 25 basis point rate hikes in the third quarter of this year. They then anticipate a rate cut in early 2024, followed by additional rate cuts the remainder of 2024 and finishing up in early 2025. Again, this chart is meant to provide insight into what economists from major banks and dealers are thinking about forward rates – they are likely communicating this information to their clients and trading desks, which can influence market sentiment and market pricing.

	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q
	2023	2023	2024	2024	2024	2024	2025	2025	2025	2025
# of replies	63	65	61	59	54	53	29	28	27	26
Median	5.50%	5.50%	5.25%	4.75%	4.25%	3.75%	3.50%	3.00%	3.00%	2.88%
Average	5.41%	5.36%	5.06%	4.66%	4.22%	3.89%	3.61%	3.29%	3.17%	3.08%
High Forecast	5.75%	5.75%	5.75%	5.75%	5.75%	5.75%	5.50%	5.50%	5.50%	5.50%
Low Forecast	4.75%	4.25%	3.25%	2.75%	1.25%	1.25%	1.25%	1.25%	1.25%	1.75%
Previous median	5.25%	5.25%	4.75%	4.25%	4.00%	3.50%	3.00%	3.00%	2.75%	n/a
Change in median	0.25%	0.25%	0.50%	0.50%	0.25%	0.25%	0.50%	0.00%	0.25%	n/a

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