

## AST DEFEASANCE RATE MARKET UPDATE

Good Morning! Please see below for the RCA | AST Defeasance *Rate Market Update* for May 2, 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: May 2, 2023 | FOMC Meeting Preview](#)

- Rates down ~7-10 bps this morning; rates largely range bound
- JOLTS jobs report weaker than expected
- Market awaits tomorrow's FOMC rate decision
- Consensus calling for a 25 bp rate hike
- FOMC is also anticipated to adopt a "hawkish pause"
- Rate decision due tomorrow at 2:00 PM, followed by Chairman Powell's press conference

US Treasury and SOFR swap rates were down 7-10 bps this morning as the JOLTS jobs report posted weaker than expected results. That said, the market awaits tomorrow's FOMC rate decision – the main event for this week. Market participants expect the Fed to raise the overnight rate 25 basis points at tomorrow's meeting. This will result in an overnight rate of 5.00% (5.00% lower bound/5.25% upper bound). In addition, the FOMC is widely anticipated to communicate a monetary policy shift to a "hawkish pause" in response to recent banking sector turmoil and concerns further rate increases may cause a US recession. That said, inflation remains sticky, the labor market remains tight (despite this morning's JOLTS jobs number) and so far, the US consumer has remained resilient. In addition, many prominent global economies are also struggling to contain inflation which will also have an impact on the FOMC's go-forward monetary policy. While there are many reasons for the FOMC to pause, there is still enough uncertainty surrounding the inflation outlook that the Fed will likely remain vigilant and ready to raise rates again should conditions warrant.

As has been the case for recent meetings, Chairman Powell's press conference immediately following the meeting will be closely watched. He is expected to communicate a "hawkish pause". That likely translates to a Fed that is willing to wait and see what the impact of the rate hikes to date will be, but prepared to continue on a higher rate path should inflation start to trend higher. The FOMC is not expected to communicate any intention to cut rates during 2023 at tomorrow's meeting. Powell is also likely to emphasize that the FOMC continues to view lowering inflation as their primary monetary policy objective. There will likely be media questions concerning the health of the banking sector and the First Republic failure – Powell is expected to echo his prior comments and reiterate that US banks are sound, safe and well capitalized.

We do not see any major economic data released prior to the meeting, but it is worth noting that the situation with the US Debt Ceiling is starting to get the attention of the markets. If this is not resolved quickly we could see higher short term rates for T Bills and short term Treasuries. We will have more on the debt ceiling situation in future updates. I do expect the market to remain jittery for the short term and we could see traders overreact to any data released or debt ceiling chatter prior to the meeting.

### [CHART 1: 1 Year, 2 Year & 3 Year SOFR Swap Rates – Prior 30 Days](#)

The Bloomberg graph below details the 1Y, 2Y & 3Y SOFR swap rate for the past 30 days. Despite elevated intra-day volatility over the prior 30 days, rates have drifted higher as we approach the FOMC rate decision. 1Y swap rates, the most sensitive to FOMC rate moves, are up ~7% over the prior 30 days, 2Y and 3Y swaps slightly less. The market is anxious for the Fed to pause and ideally, pivot to a neutral or dovish monetary policy stance. However, sticky inflation, a strong labor market and resilient manufacturing and consumer spending have forced the Fed to continue to raise rates and to communicate that they are willing to raise rates further, if necessary. I do expect

some elevated rate volatility – potentially tomorrow post-meeting but more likely in the days following the meeting as the market digests the results and Powell’s comments.



**CHART 2: 2 Year SOFR Swap Rate – Prior 3 Trading Sessions**

The Bloomberg chart below shows the 2Y SOFR swap rate for the prior three trading sessions. Despite the market’s desire for the Fed to pause and pivot, rates for the FOMC sensitive 2Y tenor have crept higher as we approach the meeting. There is definitely a wide range of opinions on the June meeting and what the Fed will do. Powell’s comments and media Q&A tomorrow will no doubt set the tone for the June meeting. As we have been discussing, recent economic data has been mixed overall and has not provided a clear direction for the economy. Yes, many fear a recession, but many market participants also acknowledge that the data does not *clearly* show that a recession is a foregone conclusion. Reconciling the dichotomy between market expectations and the FOMC dot plot is likely to lead to continued elevated levels of rate volatility and heightened market uncertainty.



**CHART 3: Bloomberg Economists Forecast**

The Bloomberg table below summarizes the Bloomberg Economists’ economic data and Fed Funds forecast for this year and next. This is for your information only and meant to provide a flavor of short term expectations. Per below, Bloomberg economists do not anticipate a rate cut in 2023 but they *do* anticipate deteriorating economic conditions as we move through 2023. Please keep in mind forecasts are *ever-changing* and we get a full series of economic data prior to the June 14<sup>th</sup> FOMC meeting. *Stay tuned!*

INDICATOR	3Q21	4Q21	1Q22	2Q22	3Q22	4Q22	1Q23	2Q23	3Q23	4Q23	2022	2023	2024
GDP (Percent QoQ AR)	2.7	7.0	-1.6	-0.6	3.2	2.7	1.1	0.6	-1.3	-0.9	0.9	-0.2	1.3
Unemployment Rate	5.1	4.2	3.8	3.6	3.6	3.6	3.5	3.9	4.3	4.5	3.6	4.5	5.0
CPI (Percent YoY)	5.3	6.7	8.0	8.6	8.3	7.1	5.8	4.5	4.0	3.7	7.1	3.7	2.9
Core CPI (Percent YoY)	4.1	5.0	6.3	6.0	6.3	6.0	5.6	5.2	4.5	4.2	6.0	4.2	3.1
Fed Funds Rate	0.25	0.25	0.50	1.75	3.25	4.50	5.00	5.25	5.25	5.25	4.50	5.25	4.25

As of April 28, 2023

Actual

Full-year GDP growth rates are 4Q/4Q.

Forecast

Unemployment and inflation rates annual forecasts are 4Q averages.

Fed Funds values are upper bound of target range.

**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.