Hi «Name»,

Good Morning! Please see below for the RCA | AST Defeasance Rate Market Update for February 17, 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 | February 17, 2023:

- **Treasury and Swap yields increased this week**
- **Rate market capitulates to the FOMC**
- **Strong economic data, stubborn inflation and Hawkish Fed-Speak all contribute to higher rates**
- **Fed officials have been clear they will continue to raise rates until inflation is controlled**

We continued to see rates march higher this week as market participants recalibrated FOMC expectations yet again. Traders who had hoped to see a disinflationary trend continue, forcing the Fed to rethink their forward path, were disappointed this week. CPI and PPI both printed higher than the market anticipated and dashed hopes of a Fed pivot in 2023. Additionally, robust retail sales, strong manufacturing data and a resilient consumer bolstered the FOMC's assertion that the economy can absorb the aggressive tightening cycle underway and not fall into a recession. Hawkish Fed-speak was the final blow this week – all of the factors mentioned above were too much for the market to ignore. Rates began moving higher after the Feb 2 meeting and have steadily increased since. Right now the market is nervously hoping that the Fed will only tighten 3 more times before pausing. If the market is wrong and inflation does not abate to the Fed's satisfaction, they have been clear they will continue to increase rates until the job is done. We expect volatility to continue as a jittery market assesses forward rate expectations – for now the market has reluctantly capitulated to the Fed.

TABLE 1: ***1-Week Movement in Term SOFR Interest Rate Swaps***

Swap Tenor	February 10, 2023 Rate	February 17, 2023 Rate	Change:
2 Year SOFR Swap	4.567%	4.755%	+18.8 bps
3 Year SOFR Swap	4.118%	4.339%	+22.1 bps
5 Year SOFR Swap	3.699%	3.899%	+20.0 bps
10 Year SOFR Swap	3.442%	3.608%	+16.6 bps
1M CME Term SOFR	4.56153%	4.56350%	+< 1 bp

Table 1 (above) shows SOFR swap yield movement for the past week. Strong economic data, resilient inflation and a chorus of Hawkish Fed-speak all contributed to the increase in SOFR swap rates. Basically, the rate market was forced once again to reprice FOMC expectations. There is still a high degree of uncertainty in the rate market, so we could continue to see knee-jerk market reactions to economic data or Fed-speak causing intra-day rate volatility. That said, there is an asymmetric bias toward higher rates as a nervous and disappointed rate market has grudgingly gotten back into the FOMC's boat – for now.

CHART 1: ***1-Month Change – SOFR Swap Rates***

The Bloomberg graph below illustrates the month-on-month change in SOFR swap rates. I wanted to highlight this chart as it clearly shows the rate increase we have seen across the curve since the Feb 2 FOMC meeting. The rate move started with Powell's comments and a strong employment report and was further supported by higher than expected inflation data, strong Retail Sales and healthy manufacturing data. Hawkish Fed-speak helped sustain the rate increase as rate market participants finally threw up their hands and capitulated to the FOMC and current monetary policy. The FOMC-sensitive 2-Year SOFR swap was up 59 basis points MoM (+14.2%) – that clearly illustrates the market "accepting" that the FOMC will continue to raise rates and do not currently plan to lower rates anytime soon.

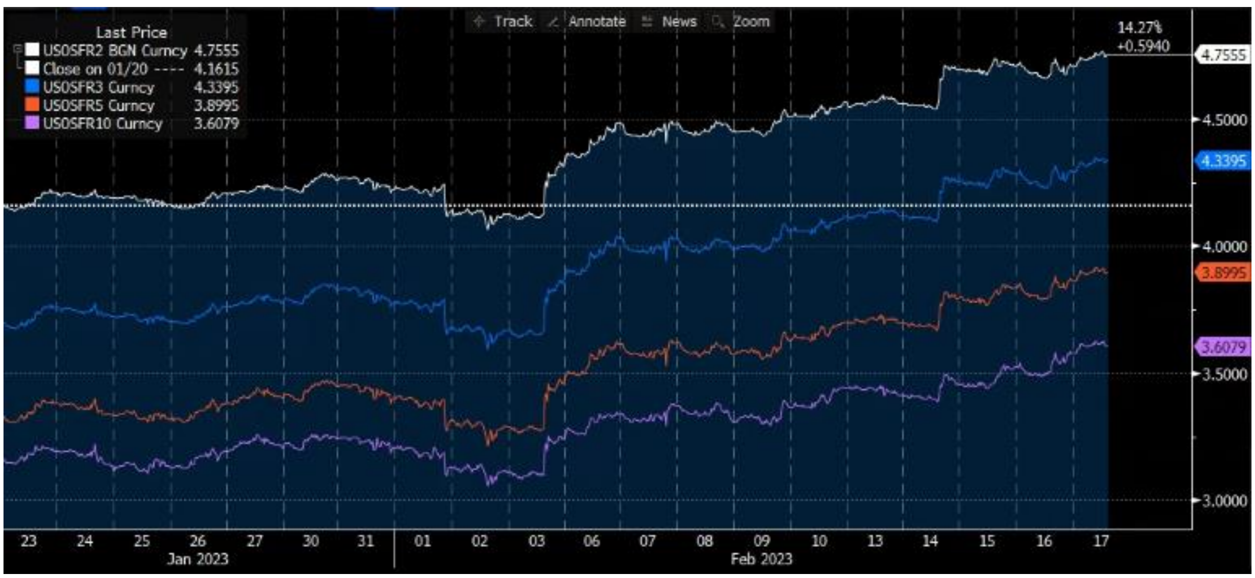
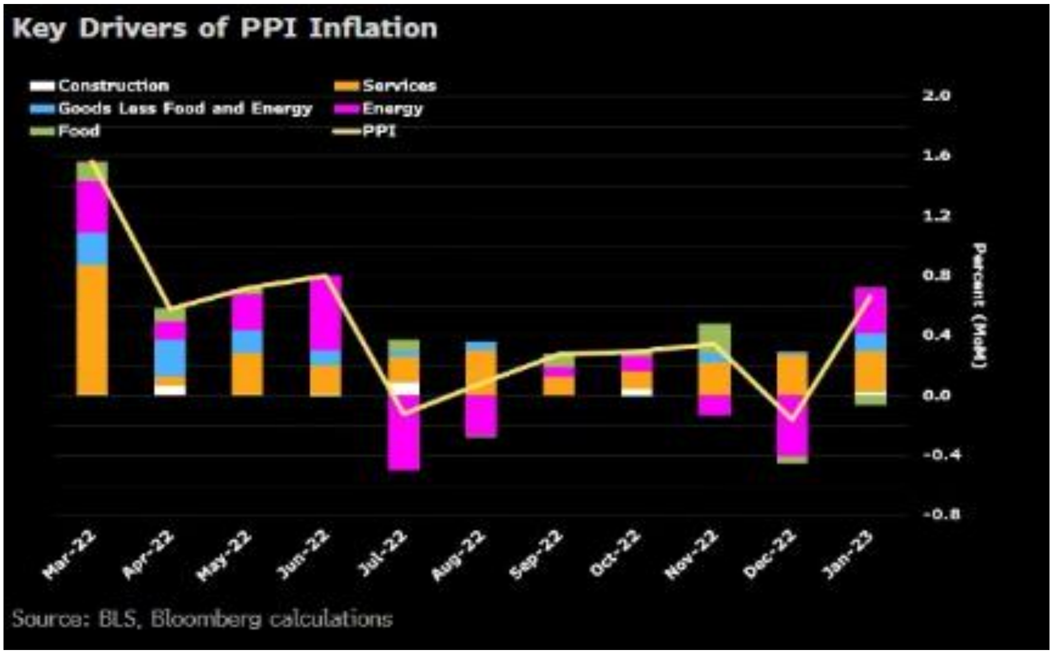


CHART 2: PPI Prior 12-Months | Key Drivers of PPI Inflation

The following Bloomberg chart breaks down the key drivers of yesterday's higher than expected PPI inflation data. PPI declined in December, so the market was hopeful that trend would continue in January. The significant increase in PPI caught the market off guard and as we discussed above, led to rates moving higher. The PPI data also provided further hard evidence that the FOMC will likely stay on the current path and continue to increase rates. Market participants are now calling for *at least* 3 more 25 basis point hikes – in March, May and June. Fed terminal rate expectations are also adjusting higher – some forecasters now expect the terminal rate may need to approach 5.50% in order for the FOMC to be satisfied inflation is under control. The forecasted terminal rate could always be revised higher, should we continue to see inflationary pressure and the U.S. economy remains healthy.



Rates Market: *The Week Ahead*

- **FOMC Meeting Minutes released Wednesday 2/22**
- **Economic data highlights for next week: Existing Home Sales 2/21; *GDP, 2/23*; New Home Sales 2/24**

Next week the market is likely to be focused on Thursday's GDP release and the housing data also scheduled to print. The FOMC will release the Feb 2 Meeting Minutes on 2/22, which may provide further clarity on the Fed's current mindset. Keep in mind the minutes are already somewhat "stale" given the economic data and Fed-speak the market has seen and heard over the past few weeks. The minutes may, however, provide some tidbits on the FOMC's plans for the next couple of meetings and what they will be focusing on. I do not think the market expects any surprises, so I do not anticipate the release of the minutes to be a market moving event. Keep an eye on Thursday's GDP data – a strong GDP number will likely tick rates higher as the market continues to capitulate to monetary policy. A weaker than expected GDP number may cause the market to pause, even drop slightly, as traders evaluate the impact it could have on rate hikes beyond the May meeting.

Best Regards,

Mark Perlow
AST Defeasance Consultants
Rate Cap Advisors
Direct: (212) 500-0922
Email: mperlow@astdefeasance.com

If you wish to no longer receive this market updates, please just reply back and let us know!