Interest Rate Market Insight

October 14, 2014

• The Columbus Day holiday and closed bond market failed to slow the selling in global equities and oil, as the S&P 500 has now slipped nearly 5% in three trading days, its worst streak in over three years, gapping below its 200-day moving average to 1874. The yield curve fell over 13 bps from 2s to 10s, with the biggest price rally at the 5-year maturity. The 2.28% Friday print on the 10-year yield was a 15-month low, but the curve is down another 5-11 bps in early trade this morning. The long end of the yield curve has flattened 85 bps in the last year. In light of recent inflation metrics domestically and the latest IMF report highlighting disinflation and slower growth, Federal Reserve members have been taking a notably dovish tone in the past week, most notably Vice Chair Fischer, who stated that "if foreign growth is weaker than anticipated, the consequences for the U.S. economy could lead the Fed to remove accommodation more slowly than otherwise." The futures market implication for 3-month LIBOR is now below 0.80% for December 2015. Import and export prices failed to imply any inflation across borders for September, with the former slipping 0.5% MoM and the latter down 0.2% thanks to petroleum and agricultural price declines.

• The IMF's 2015 global growth rate was downgraded from 4% to 3.8% in their latest report, however the US growth expectation rose to 2.2% from 1.7% for this year and moved up slightly to 3.1% growth for 2015. Their expectation for the Fed funds target rate increase was mid-year, however this consensus seems to be shifting by the minute to later in the year. While the data last week was quite limited, initial jobless claims fell again to 287k, where the 4-week average now sits as well. While the 3-year note auction was well received, the 10- and 30-year maturities were absorbed with much less fanfare, even as rates plummeted by week-end. Consumer credit expanded only $13.5 billion in August, 30% less than expected as revolving credit slowed. The wholesale trade report showed inventories advancing a faster-than-expected 0.7% MoM for August thanks to slowing auto sales. With German investor confidence falling to a two year low, the country's Economic Ministry has reduced GDP growth rates to 1.2% and 1.3% for 2014-15, respectively, and nobody is ruling out a technical recession for Q2-Q3 2014, where we may possibly see back-to-back quarters of economic contraction--and this from the strongest Eurozone country.

• Plenty of data will be crammed into the remaining four trading days this week, most notably retail sales, which should slip 0.1% on the headline and rise 0.5% ex autos and gas thanks to well-documented sluggishness in those complexes. Producer prices for final demand should rise only 0.1% for both headline and core metrics, and the Empire State and Philly Fed surveys are both expected to stay strong above 20 readings. Industrial production should rise 0.4% for September after an unexpected fall in August, and housing starts are expected to rebound above a 1MM annualized rate for last month after dropping more than 14% in August. The Fed's Beige book economic report is out tomorrow.

Index Rates	Last	Week Ago	Month Ago	Year Ago
1-month LIBOR	0.15%	0.15%	0.15%	0.17%
3-month LIBOR	0.23%	0.23%	0.23%	0.24%
6-month LIBOR	0.32%	0.32%	0.33%	0.37%
12-month LIBOR	0.55%	0.57%	0.58%	0.63%
Fed Funds Target	0.25%	0.25%	0.25%	0.25%
Prime Rate	3.25%	3.25%	3.25%	3.25%
SIFMA Muni Swap Index	Call	0.03%	0.04%	0.07%

Treasury Rates	Last	Week Ago	Month Ago	Year Ago
2-yr Treasury	0.43%	0.56%	0.57%	0.34%
3-yr Treasury	0.88%	1.03%	1.08%	0.68%
5-yr Treasury	1.53%	1.72%	1.79%	1.43%
7-yr Treasury	1.97%	2.15%	2.23%	2.07%
10-yr Treasury	2.28%	2.44%	2.54%	2.68%
30-yr Treasury	3.01%	3.12%	3.27%	3.74%
2s-10s Spread	1.86%	1.88%	1.97%	2.34%

Taxable Swap Rates	Last	Week Ago	Month Ago	Year Ago
2-yr LIBOR Swap	Call	0.80%	0.77%	0.47%
3-yr LIBOR Swap	Call	1.27%	1.23%	0.76%
5-yr LIBOR Swap	Call	1.86%	1.88%	1.53%
7-yr LIBOR Swap	Call	2.20%	2.25%	2.15%
10-yr LIBOR Swap	Call	2.52%	2.60%	2.73%

Tax-Exempt Swap Rates	Last	Week Ago	Month Ago	Year Ago
2-yr SIFMA Swap	Call	0.46%	0.44%	0.30%
3-yr SIFMA Swap	Call	0.81%	0.78%	0.53%
5-yr SIFMA Swap	Call	1.35%	1.38%	1.19%
7-yr SIFMA Swap	Call	1.72%	1.77%	1.78%
10-yr SIFMA Swap	Call	2.08%	2.15%	2.37%

All else equal, amortizing swaps and caps will have lower rates and costs, respectively. Please call for specific structure pricing requests.

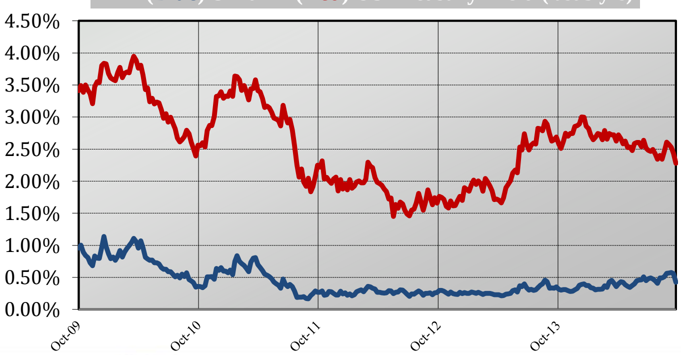
Agency Rate Caps (in bps)	LIBOR = 3%	LIBOR = 4%	LIBOR = 5%	LIBOR = 6%
3-yr LIBOR Cap	33	18	18	8
4-yr LIBOR Cap	88	47	27	33
5-yr LIBOR Cap	163	87	50	31
7-yr LIBOR Cap	340	199	120	75

Fwd Implied 3mL Rate	Last
Dec. 14	0.23%
Dec. 15	0.90%
Dec. 16	1.91%
Dec. 17	2.56%

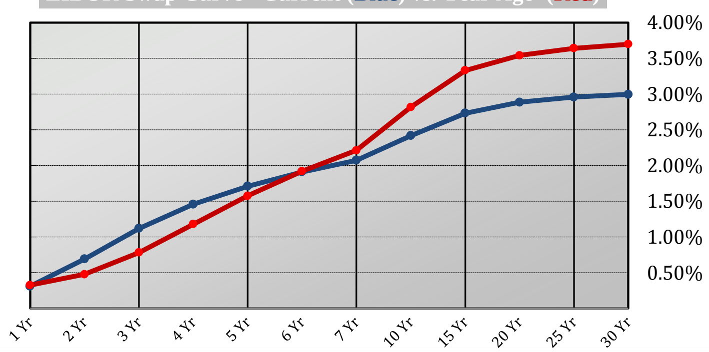
Conventions

Source: Bloomberg. LIBOR swaps use 1-month LIBOR, monthly payments, act/360 for both legs. SIFMA swaps reset weekly and pay monthly, act/act. For %of LIBOR swaps, multiply the %used by the taxable swap rate. No amortization.

2 Yr (Blue) & 10 Yr (Red) US Treasury Yield (last 5 yrs)



LIBOR Swap Curve - Current (Blue) vs. Year Ago (Red)



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