Interest Rate Market Insight

August 18, 2014

• That single digit equity swoon was enough to temper bearishness, as broader indices are now back within a percent of all-time highs after last week, but the lingering effect of now-subsiding volatility has been continued strength for US and European government debt. The resultant yields are down to six month lows for domestic issues (2.34% and 3.13% for 10- and 30-year paper, respectively, after well-received auctions), while the standard bearer of the EU, the German 10-year bund, fell to a multi-*century* low yield below 1%. The US dollar has been very strong amidst the turmoil in Ukraine, Gaza, and Iraq, and oil prices have been surprisingly soft ($95/bbl for WTI crude). While the state of global yields will no doubt be intently discussed this week at the annual central bank symposium in Jackson Hole starting Thursday, Fed Chair Yellen and ECB President Draghi may be laying out the logic for differing strategies. The former is weighing a 4% Q2 GDP print and improved jobs data and the latter is dealing with potential deflation and recession in France and Germany, two economies that are much more impacted by sanctions and blowback from the Russia-Ukraine spat than the US. In premarket trade, equity futures and the yield curve are pointing higher.

• Data points that came through last week had a muted effect, particularly in retail sales data, which rose a less than expected 0.1% MoM at their core and were flat on the headline. With slowing consumer sales, a 0.4% rise in business inventories MoM for June may be more than desirable, but the growth was down from the month prior. Jobless claims rose 21k to 311k WoW after a string of lower lows, but the 4-week average is still only 297k. While the Friday cycle was dominated by news of Ukrainians destroying part of a Russian convoy, the data for the day was relatively strong, in particular producer prices for final demand that showed ebbing inflationary pressure in the space (+0.2% MoM core, 1.6% YoY). Industrial production rose 0.4% MoM and capacity utilization hit 79.2% for July, while the Empire State Manufacturing survey slipped to a 15 reading, which while down from the month prior, is still solid growth for the sector. Accounting for the large number of Fed officials speaking last week ahead of the Jackson Hole gathering, the most impactful was the first of the week, when Vice Chair Stanley Fischer spoke in a much more dovish manner than a hawk might have. The latest complaint with the jobs recovery is the millions of part time workers.

• Before members of the FOMC meet at Jackson Hole, the minutes from their last meeting will be released Wednesday, which most likely will dive into the how significantly the hawkish faction is gaining traction, if at all. Much of the data for the week focuses on the disappointing but powerful housing sector as we get housing starts (over 900k annualized hopefully), existing home sales (5MM), and the homebuilder sentiment index, which should remain strong at 53. The Philly Fed index should stay solidly above 20 when released on Thursday, and leading indicators should double to +0.6% MoM. Consumer prices (CPI) are expected to decline on the headline and rise ex food and energy.

Index Rates	Last	Week Ago	Month Ago	Year Ago
1-month LIBOR	0.16%	0.16%	0.15%	0.18%
3-month LIBOR	0.23%	0.24%	0.23%	0.26%
6-month LIBOR	0.33%	0.33%	0.33%	0.39%
12-month LIBOR	0.55%	0.55%	0.55%	0.67%
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	0.05%	0.05%	0.06%

Treasury Rates	Last	Week Ago	Month Ago	Year Ago
2-yr Treasury	0.41%	0.45%	0.48%	0.35%
3-yr Treasury	0.86%	0.90%	0.97%	0.70%
5-yr Treasury	1.54%	1.62%	1.69%	1.52%
7-yr Treasury	1.99%	2.09%	2.17%	2.17%
10-yr Treasury	2.34%	2.42%	2.55%	2.77%
30-yr Treasury	3.13%	3.23%	3.37%	3.81%
2s-10s Spread	1.93%	1.98%	2.07%	2.42%

Taxable Swap Rates	Last	Week Ago	Month Ago	Year Ago
2-yr LIBOR Swap	Call	0.66%	0.64%	0.51%
3-yr LIBOR Swap	Call	1.09%	1.07%	0.86%
5-yr LIBOR Swap	Call	1.74%	1.74%	1.66%
7-yr LIBOR Swap	Call	2.13%	2.17%	2.28%
10-yr LIBOR Swap	Call	2.50%	2.58%	2.84%

Tax-Exempt Swap Rates	Last	Week Ago	Month Ago	Year Ago
2-yr SIFMA Swap	Call	0.38%	0.37%	0.33%
3-yr SIFMA Swap	Call	0.70%	0.68%	0.58%
5-yr SIFMA Swap	Call	1.28%	1.30%	1.24%
7-yr SIFMA Swap	Call	1.67%	1.73%	1.81%
10-yr SIFMA Swap	Call	2.07%	2.17%	2.36%

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

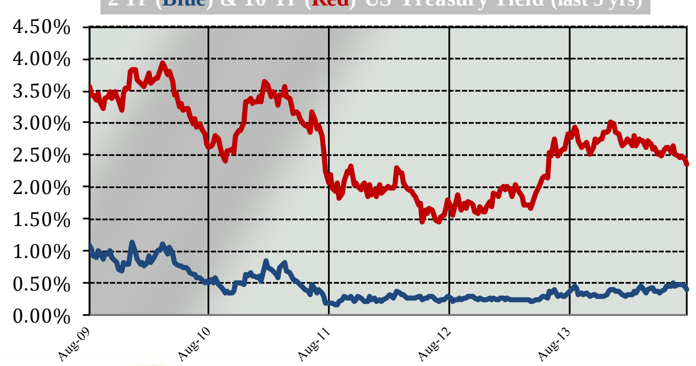
Agency Rate Caps (in bps)	LIBOR = 3%	LIBOR = 4%	LIBOR = 5%	LIBOR = 6%
3-yr LIBOR Cap	32	18	17	13
4-yr LIBOR Cap	91	51	30	20
5-yr LIBOR Cap	177	96	57	36
7-yr LIBOR Cap	360	218	133	84

Fwd Implied 3mL Rate	Last
Dec. 14	0.25%
Dec. 15	0.91%
Dec. 16	1.93%
Dec. 17	2.64%

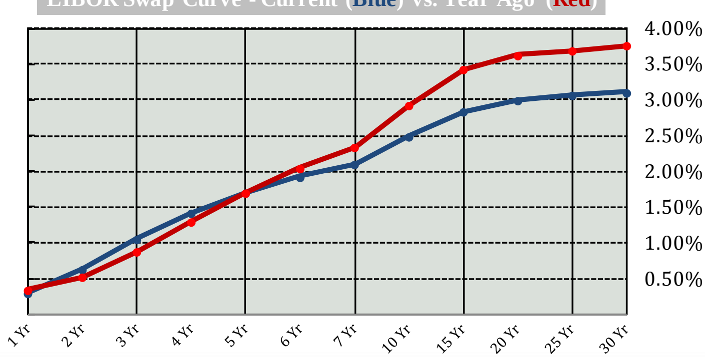
Conventions

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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