Interest Rate Market Insight

July 7, 2014

• Are we back? Whether from a super vacation, the weather quarter of decline, or the Great Recession, the answer may be yes, based on the data that continue to pour in for markets to monitor. Equity markets hit another record high last week, with Dow 17,000 now in the rearview and S&P 2000 a handful of points away, while the bond market began to discount the mid-2015 rhetoric for rate rises a bit more seriously, pushing the Treasury curve roughly 10 bps higher from the 3-year point and beyond. The European Central Bank met and stood pat with its new lower rates (negative ones for bank deposits sitting at the ECB) and did not turn on a new asset purchase program as yet, as some fear that peripheral European sovereign debt could find its way out of bank portfolios in a hurry if they did so. The rare Thursday nonfarm payrolls report produced some fireworks of its own, with 288,000 net new jobs trumping estimates by 70,000 on the back of broad sector gains, which left the unemployment rate at a mere 6.1%. Revisions added nearly 30,000 payrolls to the prior two months and pushed April's reading above 300,000, while the government sector actually added 26,000 payrolls after many quarters of flat or negative job production. The ADP private payrolls report did a nice job of presaging the slack in expectations on Wednesday with a 281,000 print. The dollar moved higher on the report. The rest of the data were more in-line than beat, particularly so with ISM manufacturing and service indices hovering above 55 still in solid growth mode, jobless claims rising 315k WoW, right around the 4-wk moving average, and a -$44 billion trade deficit. Factory orders and construction spending did fall slightly MoM. One negative, yet highly influential report that was released last week came from the Bank of International Settlements (the BIS is the central bank for central banks). Their annual report highlighted the euphoria in risk assets that has been caused by super-accommodative monetary policy, the startlingly low levels of interest rates and volatility, and a concern that deflation has become overly feared by markets as a result of the Great Depression, despite the fact that the modern era has none of the same output declines associated with that period. The Federal Reserve has now shifted its gaze to inflation with the assumption that Q1 GDP was an aberration. $71 billion of 3-, 10-, and 30-year paper will be auctioned by Treasury this week, with slackening demand in the front end auctions becoming a trend.

• We still might not have everyone back in the office or on the trading floors yet this week, but those that show will be closely watching a fair number of FOMC officials speaking and not too much on the data front. After a monthly record rise in consumer credit two months prior, $17.5 billion in additional gains are expected to be reported as vehicle sales and student loans remain hot. The wholesale trade report should show inventories rising slower at +0.6% MoM relative to 1.1% the month prior, and the Federal Reserve will release the closely monitored minutes from the last FOMC meeting, with soothsayers hoping to see a shift from dove to hawk in the rhetoric likely to be disappointed.

Index Rates	Last	Week Ago	Month Ago	Year Ago
1-month LIBOR	0.16%	0.15%	0.15%	0.19%
3-month LIBOR	0.23%	0.23%	0.23%	0.27%
6-month LIBOR	0.33%	0.33%	0.32%	0.41%
12-month LIBOR	0.55%	0.55%	0.54%	0.69%
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	0.06%	0.05%	0.05%

Treasury Rates	Last	Week Ago	Month Ago	Year Ago
2-yr Treasury	0.51%	0.47%	0.40%	0.37%
3-yr Treasury	0.96%	0.88%	0.83%	0.65%
5-yr Treasury	1.74%	1.65%	1.64%	1.42%
7-yr Treasury	2.24%	2.13%	2.19%	1.97%
10-yr Treasury	2.64%	2.53%	2.60%	2.50%
30-yr Treasury	3.47%	3.36%	3.44%	3.49%
2s-10s Spread	2.13%	2.06%	2.20%	2.14%

Taxable Swap Rates	Last	Week Ago	Month Ago	Year Ago
2-yr LIBOR Swap	Call	0.57%	0.52%	0.54%
3-yr LIBOR Swap	Call	0.98%	0.94%	0.85%
5-yr LIBOR Swap	Call	1.67%	1.68%	1.57%
7-yr LIBOR Swap	Call	2.13%	2.18%	2.14%
10-yr LIBOR Swap	Call	2.56%	2.63%	2.66%

Tax-Exempt Swap Rates	Last	Week Ago	Month Ago	Year Ago
2-yr SIFMA Swap	Call	0.34%	0.31%	0.34%
3-yr SIFMA Swap	Call	0.63%	0.60%	0.57%
5-yr SIFMA Swap	Call	1.25%	1.25%	1.18%
7-yr SIFMA Swap	Call	1.70%	1.73%	1.71%
10-yr SIFMA Swap	Call	2.14%	2.20%	2.21%

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

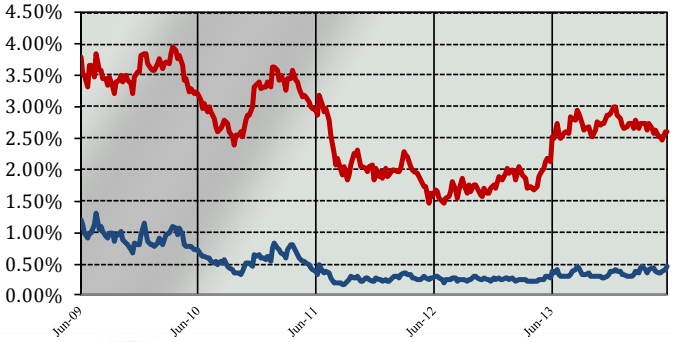
Agency Rate Caps (in bps)	LIBOR = 3%	LIBOR = 4%	LIBOR = 5%	LIBOR = 6%
3-yr LIBOR Cap	36	20	14	10
4-yr LIBOR Cap	102	58	35	23
5-yr LIBOR Cap	191	112	67	42
7-yr LIBOR Cap	419	258	159	101

Fwd Implied 3mL Rate	Last
Dec. 14	0.28%
Dec. 15	1.05%
Dec. 16	2.13%
Dec. 17	2.88%

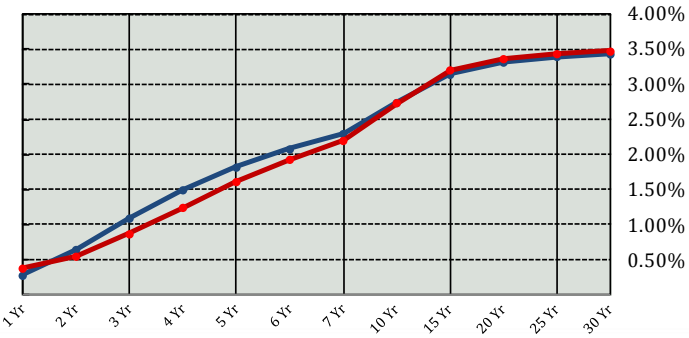
Conventions

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)



Cardea Partners is a firm of seasoned professionals dedicated to bringing transparency of execution and structuring to end-users in the interest rate swap marketplace. We help our clients get great pricing and clarity when dealing with interest rate swaps, caps and other options, mandatory hedge requirements, accounting and effectiveness testing demands, ISDA negotiation, and dealing with old transactions. ***Don't hedge without us!***

CARDEA PARTNERS

Independent Derivative Advisory Services

Cleveland, OH (440-892-8000)

San Francisco, CA (925-988-0703)

Miami, FL (954-642-1270)

cardeapartners.com