Interest Rate Market Insight

April 7, 2014

• In what was an interesting data point cluster last week, trading provided for a vicious and potentially lasting reversal on Friday, leaving the Dow and S&P 500 1% below all-time highs achieved midweek and crushing the tech-laden Nasdaq Composite. Treasuries and other debt instruments were sold off as well, sending yields higher at the back end of the curve in particular. The nonfarm payrolls report was generally in line with consensus at +192k, all private payrolls, with positive revisions of 37k for February and March readings counterbalancing the shoddy weather, and the unemployment rate was flat MoM at 6.7%. Wages failed to rise MoM, underemployment ticked up to 12.7%, and the workweek rose to 34.5 hours. The Friday jobs data was preceded by so-so figures from ADP private payrolls (191k net new) and jobless claims (+326k WoW, up 15k). The NFP whisper number was for a weather-aided whipsaw beat above 225,000, but perhaps the implied disappointment with the figures was more rally fatigue. ISM manufacturing and service indices both missed consensus with 53 handles, so modest growth persists in both sectors for the time being. The trade balance was wider than expected at -$42.3 billion, which will weigh on Q1 GDP projections that already appear to be staggering lower. The European Central Bank met and decided against further stimulus at the moment, while most of the bankers observed the deflation risk that could force them to ease policy in the near future. The policy situation seems similar to the US in 2011, although structural unemployment in the EU remains much worse than then or now domestically. While risk assets may be over-ready for a pullback, what Treasuries will do from here is more of a split decision, with yields in the belly extended beyond likely achieved forward short-rates and the long end may be gaining buyers that are hold-to-maturity types. The next catalysts will be spring house purchasing season and the myriad earnings reports for Q1 that will be upon us soon. Chicago PMI remained in growth mode but missed strong consensus of 59.0 by coming in at 55.9, a similar reading to the flash PMI Manufacturing index of 55.5, and factory orders rose 1.6% MoM in February after a fall in January.

• Price action and quarterly repositioning could be the driving factors this week, so look for the rotation to continue in lieu of many new data points. We do get the minutes from the FOMC meeting this week, and seeing how Chair Yellen handled preparation for the first press conference may be interesting to absorb. Friday, the producer price index for final demand (PPI-FD) in March is expected to rise 0.1% MoM and 0.2% excluding food and energy compared to declines of equal magnitude for each in February. Treasury will auction 3-, 10, and 30-year paper with face of $64 billion as well, and Bullard, Kocherlakota, Evans, Tarullo, and Plosser will be giving Fed speeches this week.

Index Rates	Last	Week Ago	Month Ago	Year Ago
1-month LIBOR	0.15%	0.15%	0.16%	0.20%
3-month LIBOR	0.23%	0.23%	0.24%	0.28%
6-month LIBOR	0.33%	0.33%	0.33%	0.44%
12-month LIBOR	0.56%	0.56%	0.55%	0.72%
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%	0.04%	0.11%

Treasury Rates	Last	Week Ago	Month Ago	Year Ago
2-yr Treasury	0.41%	0.45%	0.34%	0.23%
3-yr Treasury	0.87%	0.91%	0.69%	0.32%
5-yr Treasury	1.70%	1.75%	1.54%	0.70%
7-yr Treasury	2.28%	2.32%	2.17%	1.15%
10-yr Treasury	2.72%	2.72%	2.70%	1.76%
30-yr Treasury	3.58%	3.55%	3.65%	2.99%
2s-10s Spread	2.31%	2.27%	2.36%	1.54%

Taxable Swap Rates	Last	Week Ago	Month Ago	Year Ago
2-yr LIBOR Swap	Call	0.56%	0.46%	0.37%
3-yr LIBOR Swap	Call	1.01%	0.81%	0.48%
5-yr LIBOR Swap	Call	1.78%	1.59%	0.87%
7-yr LIBOR Swap	Call	2.30%	2.18%	1.33%
10-yr LIBOR Swap	Call	2.76%	2.73%	1.88%

Tax-Exempt Swap Rates	Last	Week Ago	Month Ago	Year Ago
2-yr SIFMA Swap	Call	0.33%	0.27%	0.28%
3-yr SIFMA Swap	Call	0.64%	0.53%	0.36%
5-yr SIFMA Swap	Call	1.32%	1.21%	0.69%
7-yr SIFMA Swap	Call	1.83%	1.81%	1.10%
10-yr SIFMA Swap	Call	2.32%	2.38%	1.59%

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

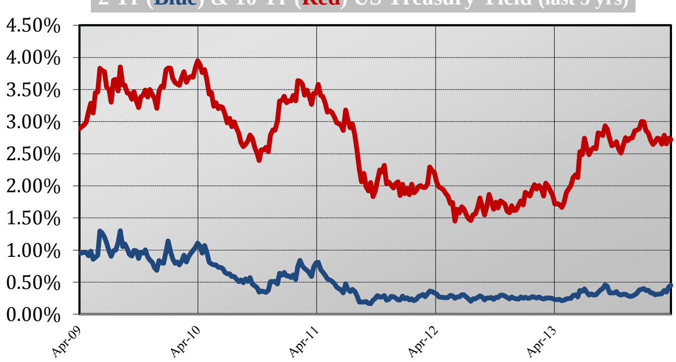
Rate Caps (cost in bps)	Strike = 4.00%	Strike = 5.00%
3-yr LIBOR Cap	25	18
5-yr LIBOR Cap	125	78
7-yr LIBOR Cap	295	190
10-yr LIBOR Cap	593	396

Fwd Implied 3mL Rate	Last
Dec. 14	0.31%
Dec. 15	1.13%
Dec. 16	2.29%
Dec. 17	3.11%

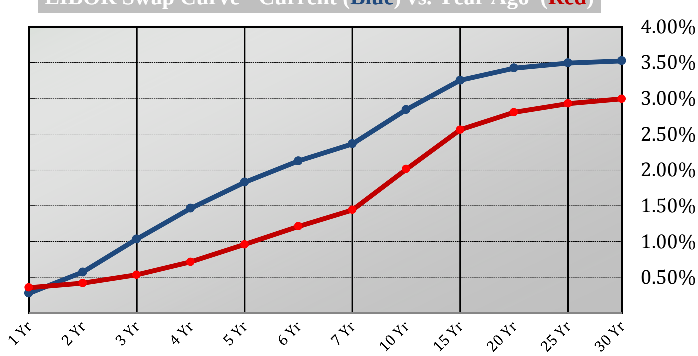
Conventions

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

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!***

Independent Derivative Advisory Services

Cleveland, OH (440-892-8000)

San Francisco, CA (925-988-0703)

Miami, FL (954-642-1270)

cardeapartners.com