# Interest Rate Risk Management Weekly Update

October 27, 2014

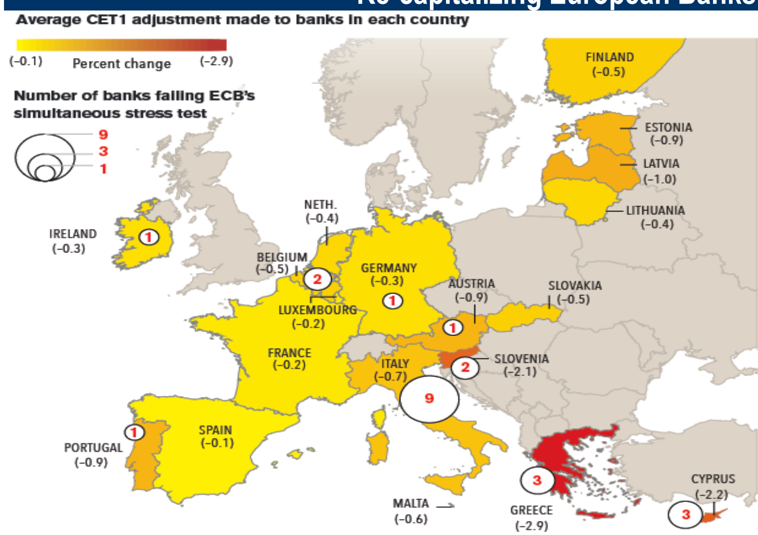
## Current Rate Environment

| Short Term Rates | Friday | Prior Week | Change |
|---|---|---|---|
| 1-Month LIBOR | 0.15% | 0.16% | (0.01% ) |
| 3-Month LIBOR | 0.23% | 0.23% | 0.00% |
| Fed Funds | 0.25% | 0.25% | 0.00% |
| Fed Discount | 0.75% | 0.75% | 0.00% |
| Prime | 3.25% | 3.25% | 0.00% |
| **US Treasury Yields** | | | |
| 2-year Treasury | 0.39% | 0.37% | 0.02% |
| 5-year Treasury | 1.50% | 1.41% | 0.09% |
| 10-year Treasury | 2.27% | 2.19% | 0.08% |
| **Swaps vs. 3M LIBOR** | | | |
| 2-year | 0.69% | 0.69% | 0.00% |
| 5-year | 1.72% | 1.66% | 0.06% |
| 10-year | 2.46% | 2.40% | 0.06% |

## *Fed Speak & Economic News:*

- Despite volatility subsiding last week, it remains elevated, which is reflective of heightened uncertainty around the Fed's timeline for rate normalization. When the Fed concludes its two-day meeting on Thursday, it is likely that we will see the end of asset purchases. Some, including St. Louis Fed President James Bullard, have called for extending asset purchases beyond the end of the month as long-term inflation prospects remain subdued. The over 20-percent fall in the price of crude oil from its YTD peak, coupled with a stronger US dollar and feeble global growth prospects support the argument. However, a delay in tapering will be viewed by the market as extremely dovish and would indicate that the Fed has lost confidence in growth prospects.
- Instead, the central bank will likely reiterate that the decision to hike rates will be data dependent. In addition, market participants believe that the phrase "considerable time" will remain in the Fed's forward-guidance language because Fed members remain cautious given recent mixed economic data. We have seen continued progress in the labor market and the manufacturing sector, while the housing market has been slow to recover, despite rays of optimism beginning to shine through; the recent drop in mortgage rates should help bolster the housing market. Consumer inflation (CPI) in September inched higher, bringing the year-over-year rate to 1.7 percent; a healthy level, but below the Fed's two percent goal. The meeting will not follow with a press conference nor will SEP projections be provided.
- Results from the ECB's capital assessment of 130 banks were released on Sunday, providing some upbeat news for an economy that so desperately needs it. Despite the fact that 25 banks will need to raise additional capital, the rest, according to the ECB and the European Banking Authority, have met the more stringent stress thresholds to outlast the next economic crisis, and those that have not are well on their way to plugging the gaps. See the chart below for additional information.
- Reuters reported that the ECB is considering corporate bond purchases and may announce its decision as soon as December. It is worth mentioning that some ECB officials have denied the report. The market, however, continues to price in balance sheet expansion from the central bank. ECB officials will meet on November 6, expectantly bringing some clarification on the matter.

## Re-capitalizing European Banks




Compared to the stress tests of 2011 and 2010, the more recent assessment by the ECB has been based on tougher measures and is meant to provide more transparency over a bank's assets. Of the 25 banks that failed the test, producing a capital shortfall of approximately €25B, 12 have been given credit raising capital after the December 2013 deadline. Of the 13 others, Italy had four banks (the highest of any country) and Greece had two that have still not met the requirement of 8% Tier 1 capital and will need to raise another €3.3B and €2.7B, respectively. These shortfalls come on the low end of expectations.

*Source: Bloomberg*

## U.S. Economic Data

- Existing home sales printed better than expected at 5.17M vs consensus of 5.10M
- CPI for September increased 0.1% compared to 0.0% expected
- Market US Manufacturing PMI was reported lower to 56.2 compared to survey of 57.0; the number still remains well in expansion territory
- New home sales were just below expectation at 467k vs 470k consensus; the prior reading was revised lower by 38k to 466k

| Date | Indicator | For | Forecast | Last |
|---|---|---|---|---|
| 27-Oct | Markit US Services PMI | Oct P | 57.8 | 58.9 |
| 27-Oct | Pending Home Sales MoM | Sep | 1.0% | (1.0% ) |
| 28-Oct | Durable Goods Orders | Sep | 0.4% | (18.2% ) |
| 28-Oct | Consumer Confidence Index | Oct | 87.0 | 86.0 |
| 29-Oct | Fed QE3 Pace | Oct | $0B | $15B |
| 30-Oct | GDP Annualized QoQ | 3Q A | 3.1% | 4.6% |
| 30-Oct | Personal Consumption | 3Q A | 1.9% | 2.5% |
| 31-Oct | Personal Income | Sep | 0.3% | 0.3% |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