Interest Rate Risk Management Weekly Update

October 17, 2016

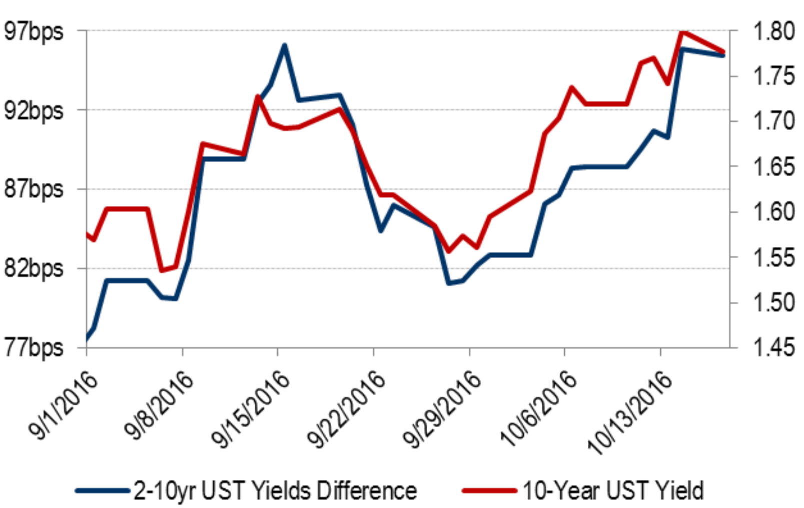
Current Rate Environment

Short Term Rates	Friday	Prior Week	Change
1-Month LIBOR	0.54%	0.53%	0.01% ↑
3-Month LIBOR	0.88%	0.88%	0.00%
Fed Funds	0.50%	0.50%	0.00%
Fed Discount	0.75%	0.75%	0.00%
Prime	3.50%	3.50%	0.00%
US Treasury Yields			
2-year Treasury	0.84%	0.83%	0.01% ↑
5-year Treasury	1.29%	1.26%	0.03% ↑
10-year Treasury	1.80%	1.72%	0.08% ↑
Swaps vs. 3M LIBOR			
2-year	1.11%	1.12%	(0.01%) ↓
5-year	1.35%	1.32%	0.03% ↑
10-year	1.68%	1.61%	0.07% ↑

Fedspeak & Economic News:

- The global economic picture is starting to look a bit rosier. While there is certainly reason to be concerned over possible slip-ups in the future, progress is being made in important economic centers. To start in the United States, retail sales numbers came in at a robust 0.6 percent for the month of September. PPI inflation numbers beat expectations (0.3 percent vs. 0.0 percent the month before) and initial jobless claims continue to point to gains in the overall labor market. In Europe, industrial production recovered sharply for August, up 1.6 percent following a -0.7 percent print in July and hinted at an overall rebound for the Euro area for the third quarter. Italy made the most progress with a 1.7 percent increase in industrial production vs. consensus of -0.1 percent. This week, China takes the spotlight as important economic data releases are expected to show significant improvement after the real estate market is proving healthier and government spending on infrastructure was boosted this summer.
- What does this all mean for the path of monetary policy? Back in the US, minutes from the September FOMC meeting were released and showed significant disagreement on the timing of the next interest rate hike. The labor force continues to be a top concern and many Fed officials still believe there is slack in the labor market. New York Fed President Dudley recently noted that "you certainly want to go as far as you can. You don't want to keep people unemployed just because you think you're already at full employment rate." Nonetheless, market participants anticipate enough FOMC members will be ready in December, pricing in a nearly 70 percent chance of a rate hike.
- European central bankers were prodded at a meeting in Washington last week and hinted at concern over the efficacy of negative interest rates in the European Union and the impact on bank profitability. The rethink of rates sparks the question of tapering in the EU and the path towards monetary policy normalization. No immediate action is expected to be announced at this week's ECB meeting but some guidance is expected towards the end of the year. Asset purchases are likely to continue well into 2017 but the conversation is beginning to turn towards a tighter monetary policy. ECB President Mario Draghi commented this past weekend that inflation in the Eurozone is likely to pick up in 2017 and 2018 and should hit the target by 2019.

The US Treasury Curve Steepens as Term Premia Unwind



Source: Bloomberg

The UST curve has steepened as the difference between 2- and 10-year US Treasury yields has widened, which has been attributed to the divergence between the two securities' yields. It is believed the material increase in longer term rates recently has been driven by market participants' reassessment of unconventional monetary policy: Investors believe we will see less of it going forward due to its limited efficacy. Global government bond yields have risen as term premia have unwound in response.

The Week Ahead

- **China** will release its **third-quarter GDP estimate** at 22:00 EDT Tuesday; consensus suggests GDP held at 6.7 percent for a third straight quarter. Production and retail sales estimates for September will also be released at the same time.
- **San Francisco Fed President John Williams** will speak on Wednesday and Friday
- The **European Central Bank** will conclude its policy meeting on Thursday at 7:45 EDT followed by a press conference hosted by ECB President Mario Draghi at 8:30 EDT.

Date	Indicator	For	Forecast	Last
17-Jan	Industrial Production MoM	Sep	0.2%	(0.4%)
18-Oct	CPI MoM	Sep	0.30%	0.20%
19-Oct	Housing Starts	Sep	1175k	1142k
20-Oct	Leading Index	Sep	0.2%	(0.2%)

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