

RATE ENVIRONMENT

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THE MARKETS

The Federal Reserve showed a willingness to delay rate hikes given volatility in financial markets and concern about global growth, according to minutes of the Dec. 19 meeting. Many participants expressed the view that with muted inflation, the FOMC could be patient about further policy firming, the minutes stated. Fed Boston president Rosengren said in a speech the central bank should pause until there is greater clarity over the economic outlook. He added, "My current expectation is that the more optimistic view will prevail, given factors like robust labor markets and strong consumer confidence." According to Fed funds futures, markets are placing an 85% chance of no change in Fed policy through year-end. Bond yields edged higher as the Treasury's auction of notes last week received lackluster demand from investors and as U.S. stocks gained strength. The S&P 500 gained 2.6% to 2,596 while the Nasdaq closed 3.5% higher to 6,971. In other news, municipal bond funds reported the biggest inflow of cash in two years, according to Lipper.

THE ECONOMY

The ISM's services gauge fell to 57.6 in December, a five-month low, though new orders remained strong. Consumer credit eased slightly to \$22.1 billion and mortgage applications as reported by the Mortgage Bankers Association surged 23%. The CPI eased 0.1% and advanced 0.2% when food and energy were excluded. Consumer prices at the core level were 2.2% higher than one year ago.

New home sales are expected to gain 4% to 566,000 in November while building permits slip 0.2% to 1.28 million. Look for a 0.1% rise in producer prices as retail sales edge up 0.3%. Factory orders likely advanced 0.3% with the trade balance showing a \$54 billion deficit.

KEY RATES

Issue	Value	Last Week	Issue	Value	Last Week
Fed Funds	2.50%	2.50%	2-Year Agency	2.59%	2.57%
Prime	5.50%	5.50%	5-Year Agency	2.62%	2.55%
2-Year Treasury	2.55%	2.50%	15-Year MBS	3.03%	2.97%
5-Year Treasury	2.52%	2.49%	30-Year MBS	3.48%	3.43%
10-Year Treasury	2.71%	2.67%	3-Month LIBOR	2.80%	2.79%

Source: Bloomberg

INTEREST RATE SWAPS / CAPS / FLOORS

Buyer Pays Fixed- Indications only based on quarterly settlements

Term	SWAP			CAP		FLOOR	
	90-Day LIBOR	PRIME		90-Day LIBOR (2.25%)	90-Day LIBOR (3.00%)	90-Day LIBOR (2.25%)	90-Day LIBOR (3.00%)
1-Year	2.77%	5.47%		0.51%	0.21%	0.06%	0.37%
2-Year	2.70%	5.50%		1.29%	0.71%	0.34%	1.03%
3-Year	2.63%	5.55%		2.00%	1.01%	0.77%	1.86%
5-Year	2.61%	5.53%		3.38%	1.63%	1.83%	3.59%

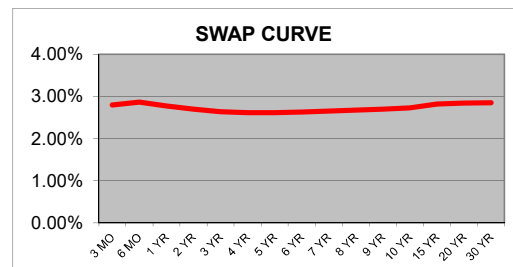
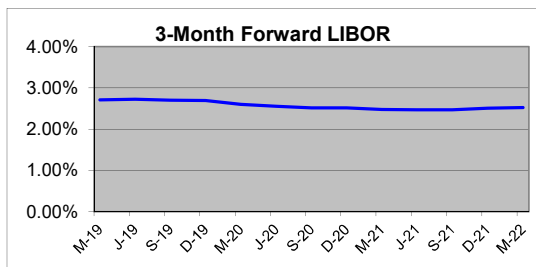
Source: Bloomberg, PNC

OTHER INDICATORS

	Value	% Change YTD		Value	% Change YTD
OIL (30 day futures)	\$ 51.59	13.61%	Dow Jones Ind Avg	23,995.95	2.87%
Commodities (CRB Index)	\$ 178.08	4.88%	NASDAQ	6,971.48	5.07%
EURO (spot)	\$ 1.147	0.03%	S&P 500	2,596.26	3.56%

Source: Bloomberg

YIELD CURVES



Source: Bloomberg

IN THE NEWS

Federal Reserve payments to the Treasury declined in 2018 as the central bank's expenses rose along with short-term interest rates. The Fed sent about \$65.4 billion to the government last year, down 18.45% from the year before and 44.10% from a peak of \$117 billion in 2015, according to preliminary estimates of the central bank's annual financial statements, released Thursday. Meantime, the Fed's expenses are rising as it raises short-term interest rates, including the rate it pays to banks on the money, called reserves, they park at the central bank. The Fed's net income totaled \$63.1 billion in 2018, a 21.81% decline from 2017, the central bank said.