



SECOR ASSET MANAGEMENT

Rates Outlook

25 July 2023

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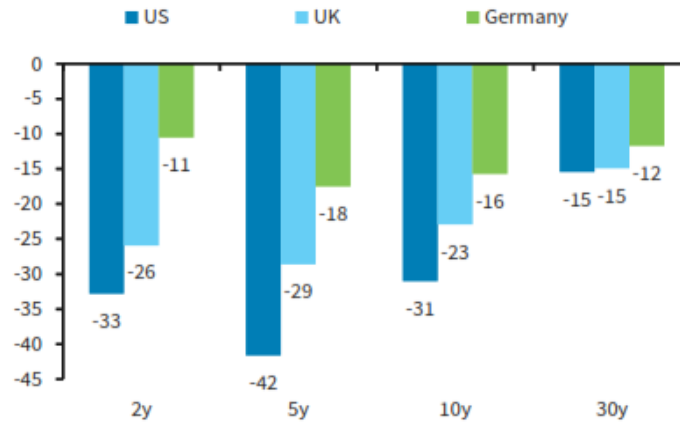
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Overview

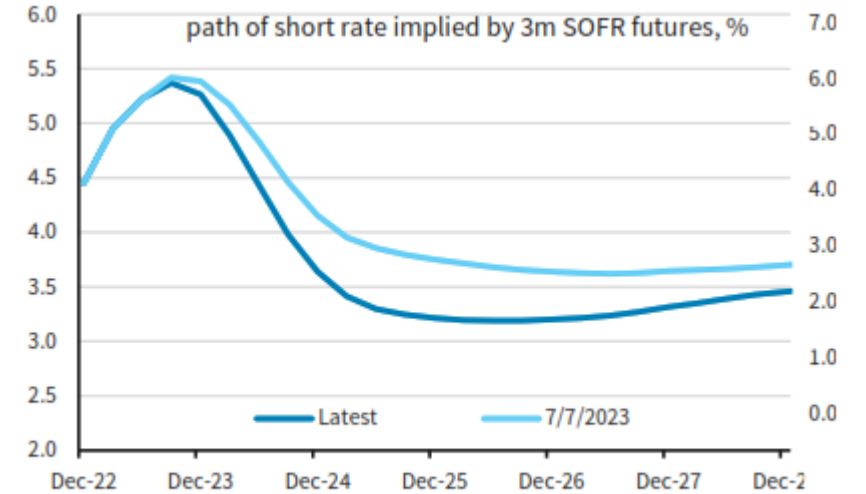
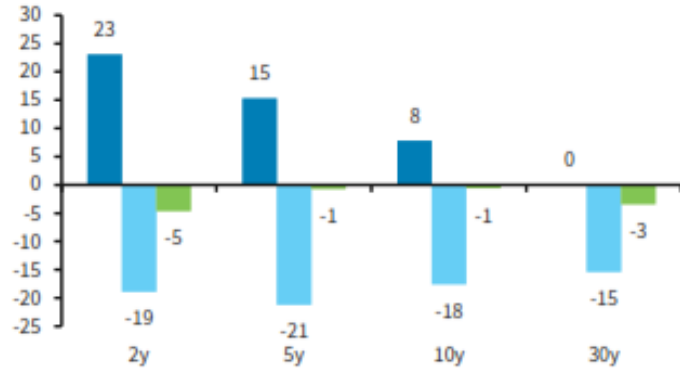
- Incoming data show the economy remains resilient
- Central banks are looking to thread the needle as it focuses on the desired level and length of restrictive policy stance
- Markets are pricing the end of the hiking cycle

US Rates

Week of 7/10



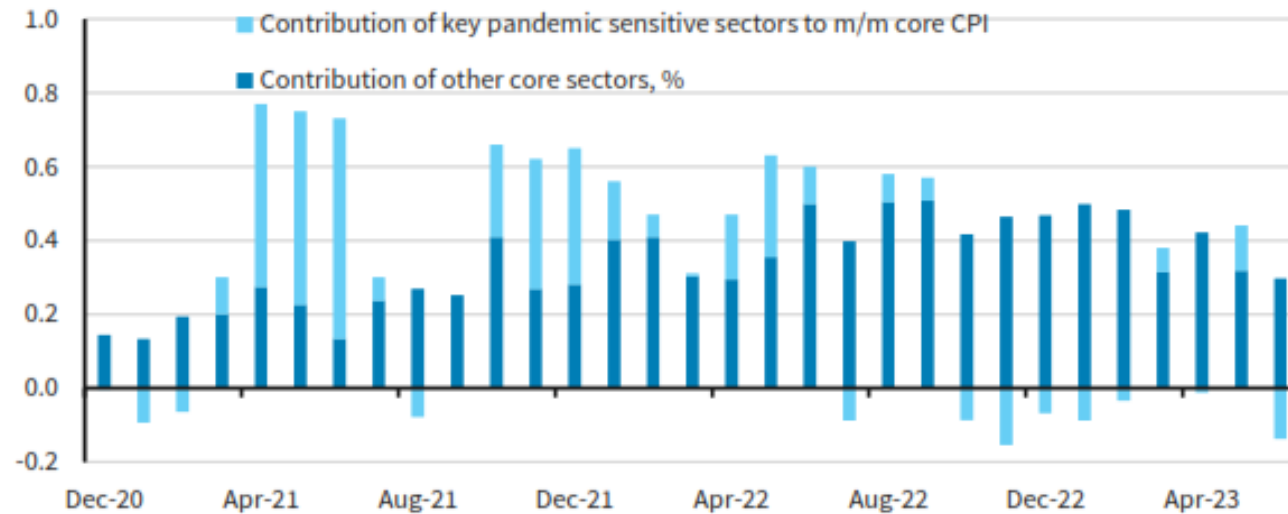
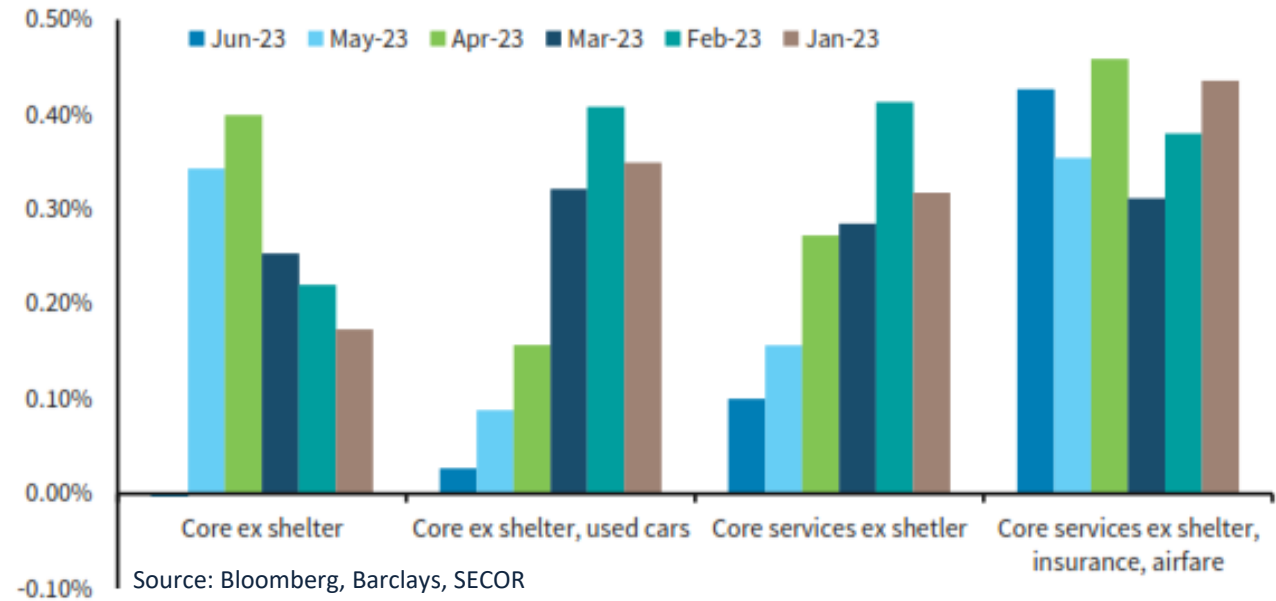
Week of 7/17



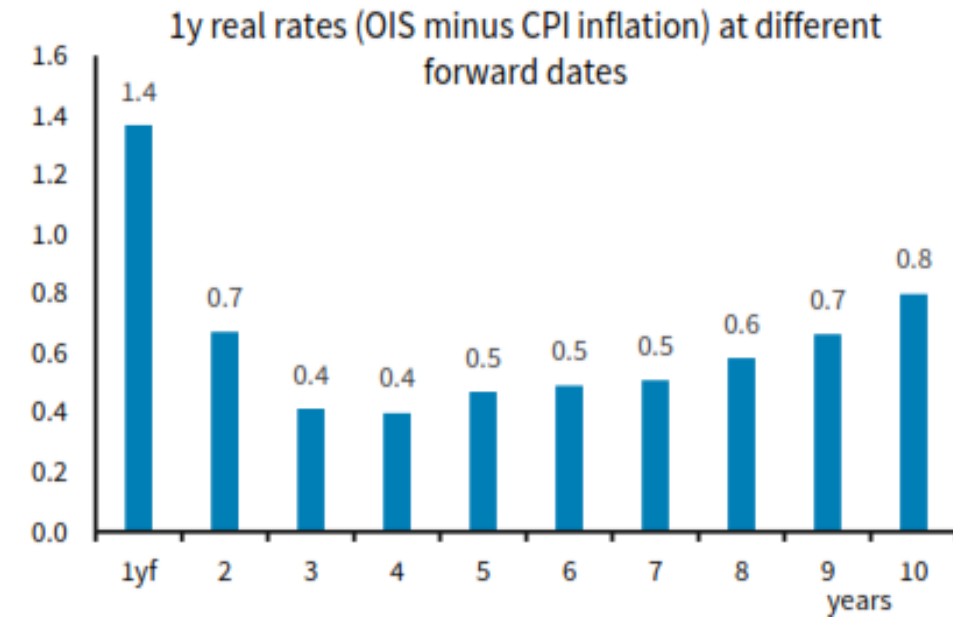
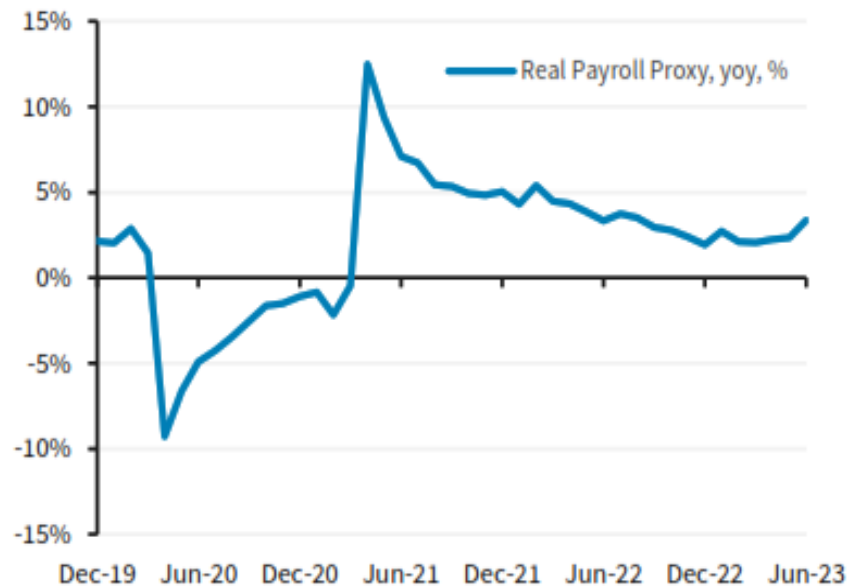
Source: Bloomberg, Barclays Research

- US Treasuries rallied sharply amid softer-than-expected inflation data
- Markets are implying cuts next year though it may be an aggressive target

US Inflation



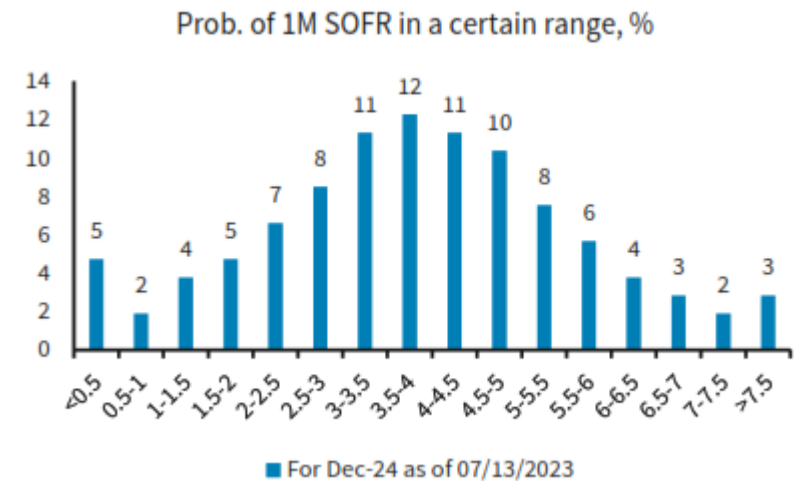
Growth Outlook and Soft Landing?



- Real incomes are accelerating
- Real rates are already priced to fall below long-run levels over the coming years

US Volatility

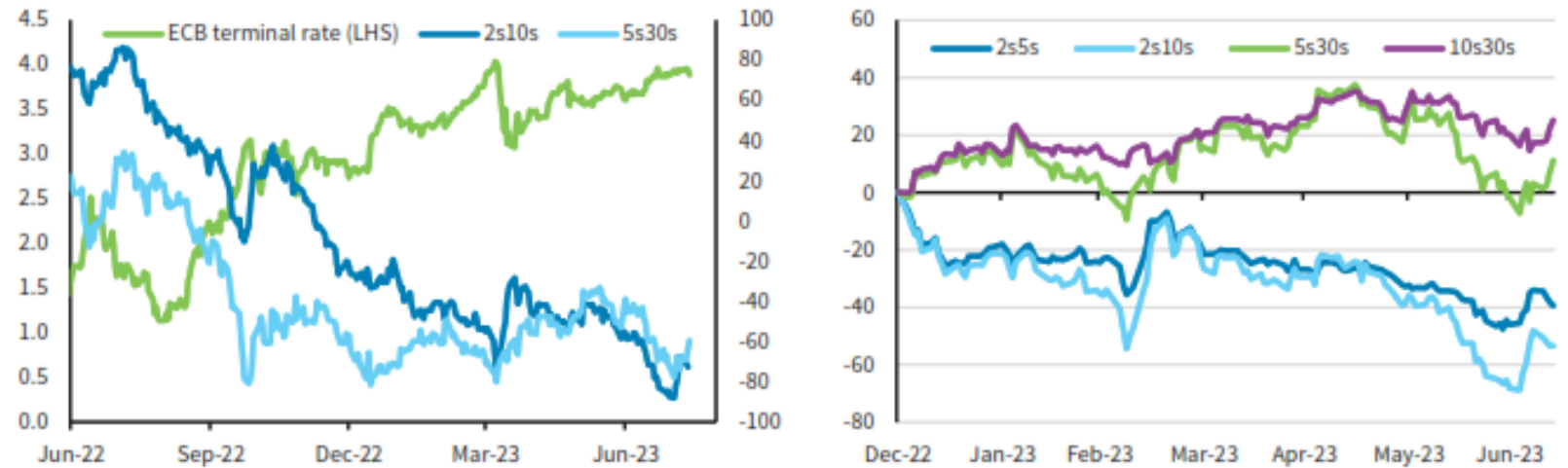
Hiking cycle pause	Realized 10y rate volatility relative to 12m prev	Recession date	Months to start of recession
Oct-59	Increased	Apr-60	7
Nov-66	Increased		
Jun-69	Increased	Dec-69	7
Jul-74	Increased	Nov-73	0
Mar-80	Increased	Jan-80	0
Jun-81	Decreased	Jul-81	2
Aug-84	Increased		
Feb-89	Decreased	Jul-90	18
Feb-95	Decreased		
May-00	Decreased	Mar-01	11
Jun-06	Decreased	Dec-07	19
Dec-18	Increased	Feb-20	15



- Hiking cycle near the end stages. Could it mean higher or lower volatility?
- End of hiking and change in vol has correlation to length before next recession
- Tail risks for the Fed path are getting compressed

EUR Rates

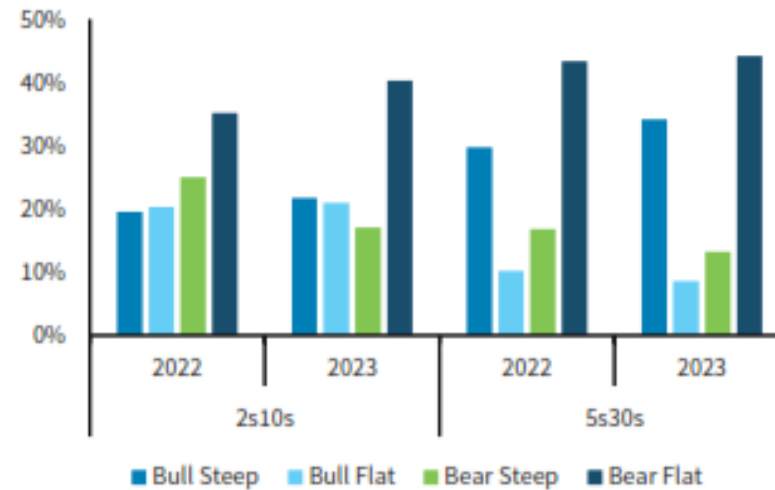
EUR Spread Moves



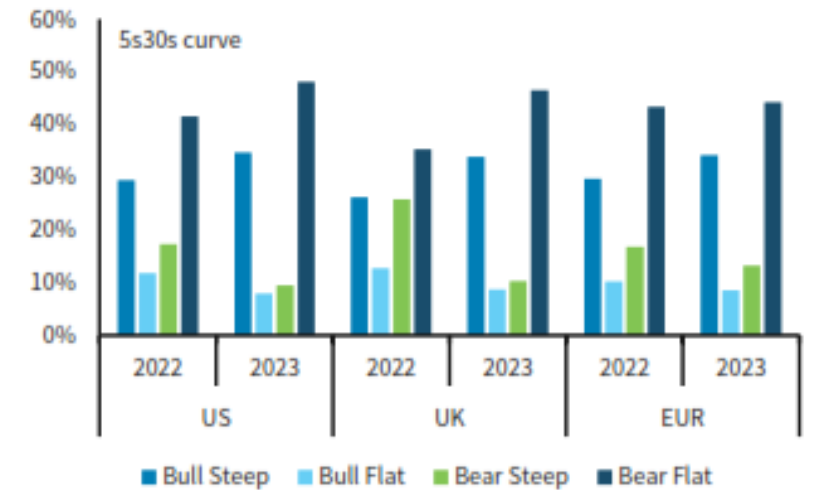
- EUR5s30s and 10s30s have steepened YTD even as the flattening pressure on 2s5s and 2s10s has persisted

EUR Rates

EUR Curve Movements

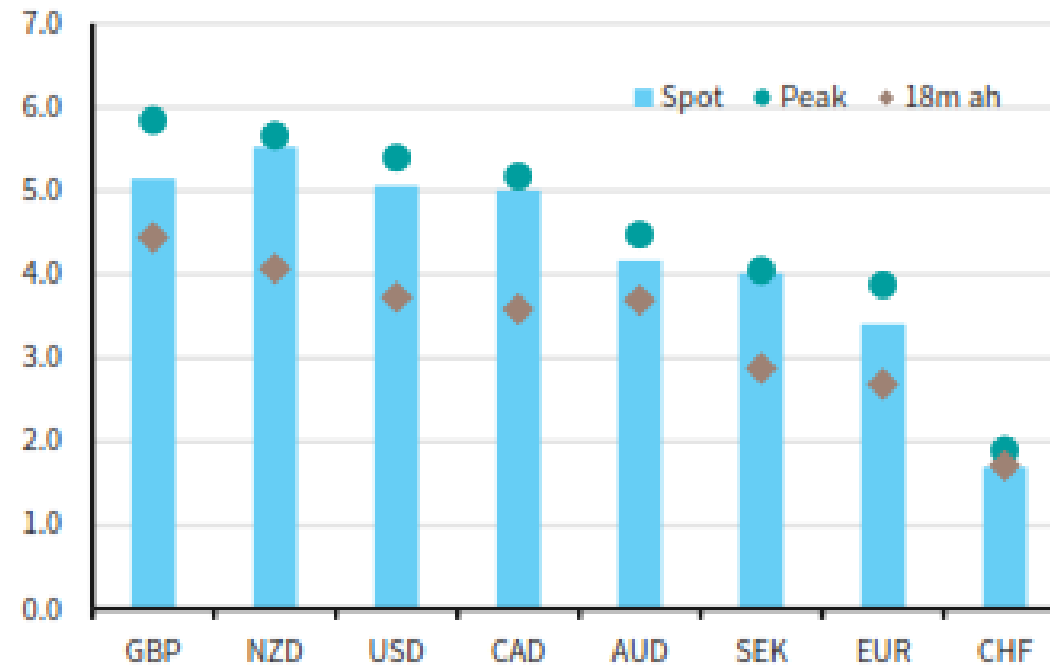


US, UK and EUR Curve Movements



- Bear-flattening has been the dominant EUR curve dynamic in 2022 and 2023 as the rate cycle gained more traction
- Across EUR, US and UK, on a vast majority of trading days the curve has bull-steepened or bear-flattened

DM Terminal Rate Projection

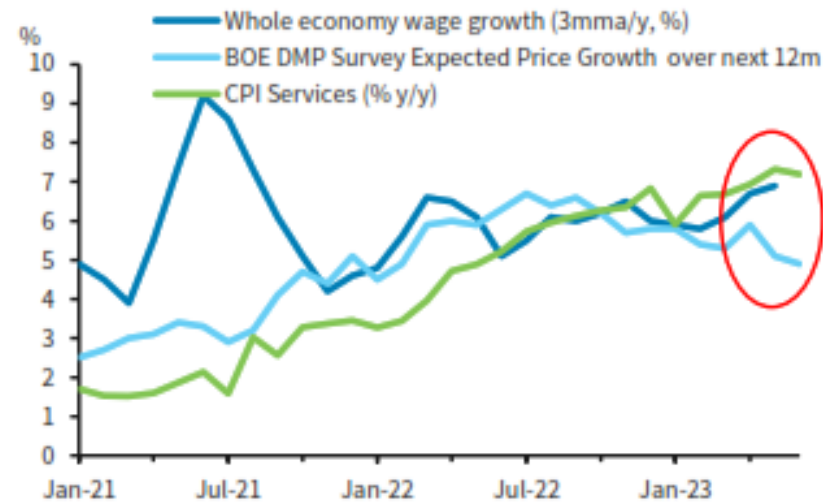


UK Rates

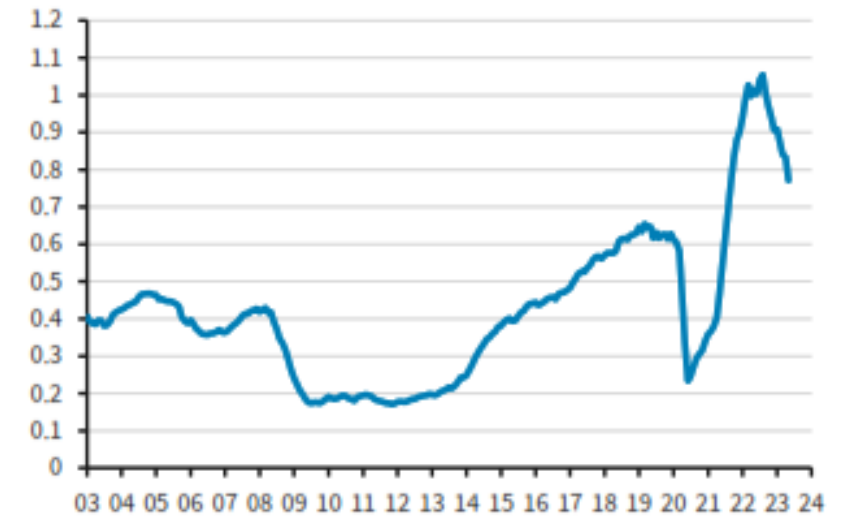
- UK's terminal rate is still the highest in the DM economies even though it has declined

UK Inflation

Measures of Inflation Persistence



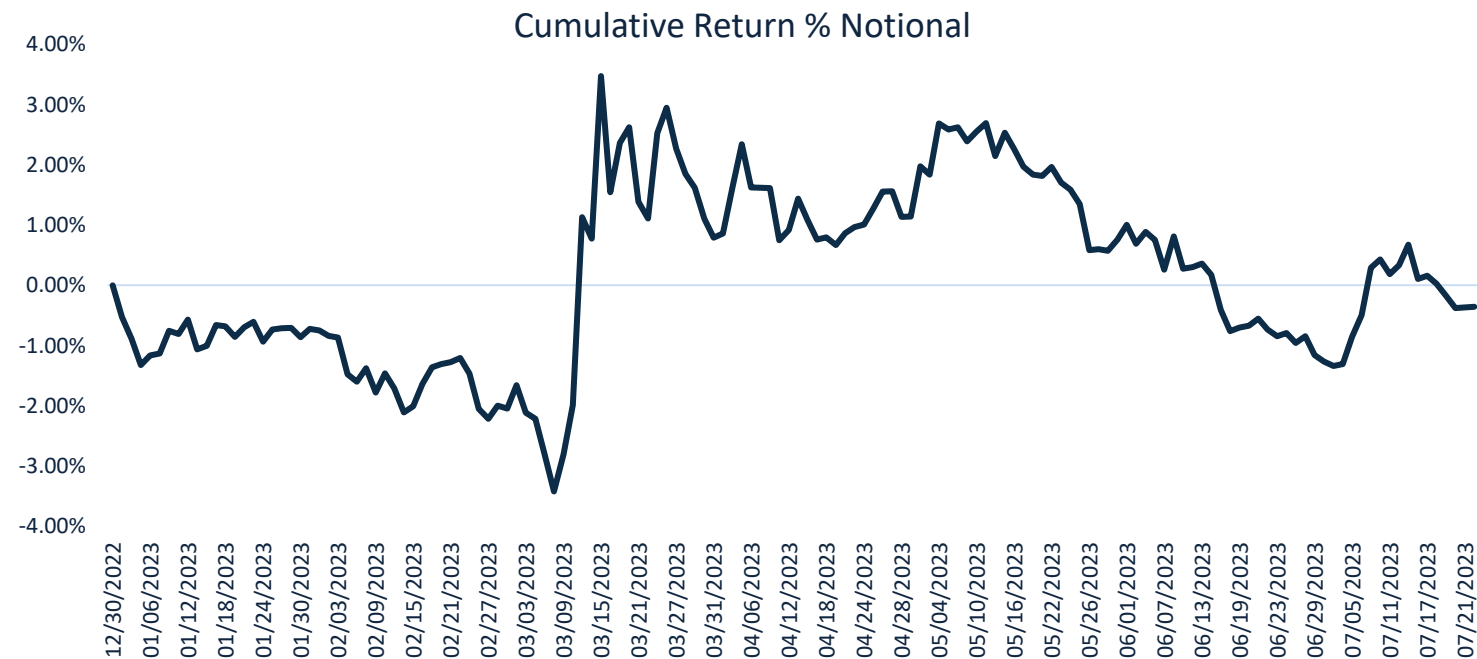
UK Vacancy to Unemployed Ratio



- Economic releases since the last MPC meeting present a mixed picture

Trade Bet Performance: USD 2s10s Curve Steepener

- Currently -0.36% return since beginning of 2023 when trade was recommended
- Trade benefitted in March 2023 during “banking crisis”
- Curve has continued to flatten since with hike expectations being pushed out from EOY 2022
- Spread currently at -118 bps seems attractive from valuations standpoint
- Although signs pointing towards soft landing, we remain cautious as central banks are still heavily data dependent



Factors	Comments	Historical Range
Valuations and Fundamentals	<ul style="list-style-type: none"> Longer term we expect rates to become more range bound with eventual lower volatility We are nearing the end of the hiking cycle There is a question around the aggressiveness of the rate cuts being priced 	
Technicals	<ul style="list-style-type: none"> We expect 2s10s and 5s30s steepening opportunity (though fundamentals may disagree) 	
Macro Impact	<ul style="list-style-type: none"> Inflation may have peaked but still a big risk. Markets still watching economic data prints to determine policy path which should be supportive of volatility in the near term US may be leading the disinflation and UK's print has been following 	
Overall	<ul style="list-style-type: none"> 9-to-12 month view vs Fwds 	

● Current Quarter
 X Last Quarter

Scenario-Based Outlook: Neutral Duration

- Key take aways

- Rates should eventually stabilize over the next 1 to 2 years as inflation normalizes and monetary policy pivots
- There are risks around data prints as the central banks are more data driven
- Overall, we are neutral vs the forward rates

As of 21 July 2023	30yr EUR Swap	30yr GBP Swap	30yr USD Swap
Spot Rates	2.63%	3.83%	3.26%
Probabilities			
Tail risks: Recession shock, geo-political environment deteriorates	5%	5%	5%
Policy mistake, Inflationary surprises, Earnings below expectations	35%	35%	35%
Base Case: Soft Landing	45%	45%	45%
Positive earnings + falling inflation and improved productivity	15%	15%	15%
Probability Weighted Rate	2.64%	3.83%	3.25%
Implied 1yr Forward Rate	2.53%	3.70%	3.12%
Difference vs Forward	0.10%	0.12%	0.12%

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