

**Deloitte.**



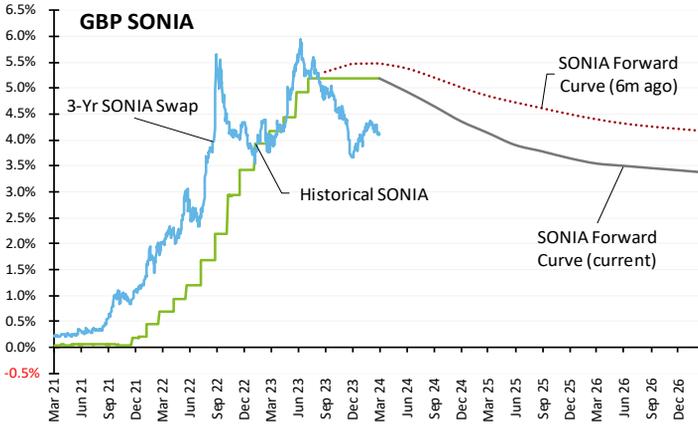
IR and FX Newsletter  
April 2024



## Interest Rate Markets

Interest rates have reduced slightly across the UK, US and EU following the meetings of the respective central banks in March. Whilst base rates were held constant in each jurisdiction, it was the accompanying comments from monetary policymakers that catalysed slight moves lower in swap rates. Furthermore, US PCE inflation data – the Federal Reserve’s (“Fed”) preferred measure of price pressures – was released during the Easter weekend and showed inflationary pressures in-line with market expectations. Per Jerome Powell, the data also matched consensus within the Fed, ensuring markets continued to price in the first 25bps cut for the Fed in July.

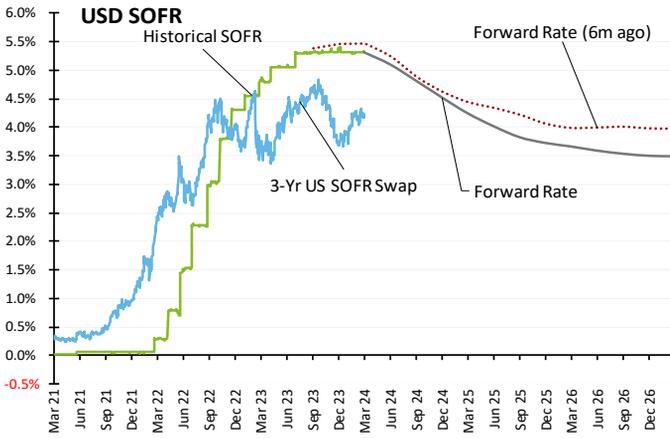
It is also worth noting that the Bank of Japan raised their base rate for the first time since 2007 on 19<sup>th</sup> March, taking Japanese rates out of negative territory.



- The underlying SONIA rate is currently at 5.19%
- BoF E policymakers held rates, as anticipated, at their 21<sup>st</sup> March 2024 meeting, with the first 25bps cut priced in for August 2024, versus June this time last month.
- The 3-year SONIA Swap rate is 4.06%, vs. 4.90% 6 months ago, and down 24bps month-on-month.
- The forward curve is downward sloping from Q3 2024.

	2-year	3-year	5-year
Swap rate (mid level)	4.33%	4.06%	3.76%
Cap @ 5.00% (premium)*	£0.44m	£0.81m	£1.78m
Cap @ 5.50% (premium)*	£0.21m	£0.51m	£1.32m

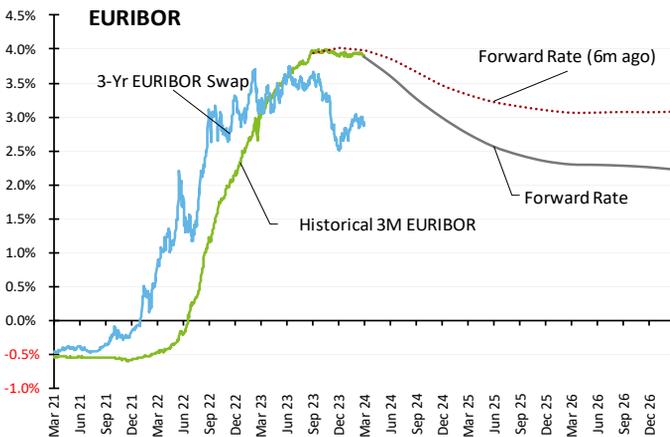
\*£100m hedge notional



- SOFR is currently 5.34%, inside the Fed Funds target rate range of 5.25%-5.50%.
- The Federal Reserve held rates at their meeting on 20<sup>th</sup> March, with markets now forecasting the first 25bps rate cut in July 2024.
- The 3-year SOFR Swap rate is 4.17%, vs. 4.61% 6m ago, and flat MoM.
- The forward curve is inverted from Q3 2024.

	2-year	3-year	5-year
Swap rate (mid level)	4.46%	4.17%	3.92%
Cap @ 5.00% (premium)*	\$0.48m	\$0.80m	\$1.66m
Cap @ 5.50% (premium)*	\$0.19m	\$0.44m	\$1.13m

\*\$100m hedge notional



- 3-month EURIBOR is 3.89%.
- The ECB held rates at 4.00% at their meeting on 7<sup>th</sup> March. Markets still anticipate the ECB’s first 25bps rate cut in June 2024.
- The 3-year EURIBOR Swap rate is currently 2.77%, vs. 3.57% 6 months ago.
- The forward curve is inverted from Q2 2024.

	2-year	3-year	5-year
Swap rate (mid level)	3.00%	2.77%	2.56%
Cap @ 3.50% (premium)*	€0.39m	€0.66m	€1.43m
Cap @ 4.00% (premium)*	€0.11m	€0.31m	€0.89m

\*€100m hedge notional

## What can be done in the current Interest Rate markets?



### Borrowers can fix rates below the current floating rate:

Not only is there no additional cost to fix floating rate exposure, but the current downward forward curve allows borrowers to fix rates at levels below the current floating rate:

- SONIA 3m is 5.18% and a vanilla 5y Swap is 3.76%. On a GBP 100m financing, swapping to fix reduces interest costs in year 1 by **GBP 1.42m**.
- SOFR 3m at 5.30% and a vanilla 5y Swap is 3.92%. On a USD 100m financing, swapping to fix reduces interest costs in year 1 by **USD 1.38m**.
- EURIBOR 3m at 3.89% and a vanilla 5y Swap is 2.56%. On a EUR 100m financing, swapping to fix reduces interest costs in year 1 by **EUR 1.33m**.



### Longer- term hedges are cheaper than shorter-term hedges:

Because of the downward forward curve, long term hedges are cheaper than short term hedges:

- GBP swap:      1-year: 4.87%,                      3-year: 4.06%,                      5-year: 3.76%
- USD swap:      1-year: 5.01%,                      3-year: 4.17%,                      5-year: 3.92%
- EUR swap:      1-year: 3.61%,                      3-year: 2.77%,                      5-year: 2.56%



### Pre-hedging achieves even lower rates:

Pre-hedging future debt (assumed closing is in 6 months) is cheaper than at current hedge rates:

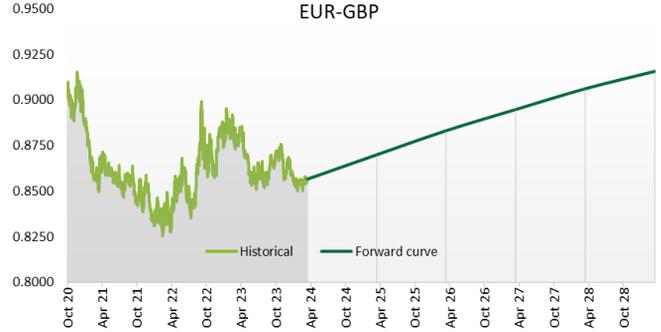
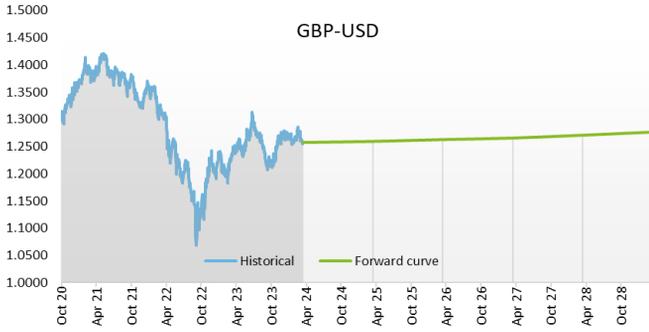
- GBP 5-year Swap starting in 6 months: 3.57%
- USD 5-year Swap starting in 6 months: 3.73%
- EUR 5-year Swap starting in 6 months: 2.40%



### Funding of Hedging costs can be done at favourable rates

Hedging costs for Option products (such as Caps) are typically paid upfront, however these costs can be deferred over time. This cost deferral can be done via the derivative desks at favourable rates (at SONIA, SOFR or EURIBOR, without additional margin), rather than via additional borrowing under the facility agreements (at SONIA, SOFR or EURIBOR plus margin).

# Currency Markets



- GBP-USD has trended moderately lower through March, amid the prospect of higher-for-longer rates in the US, lending momentum to the dollar.
- Option premia increased by up to 14% indicatively month-on-month, depending on the protection sought, due to higher volatility.
- Forward FX rates remain slightly a benefit for GBP sellers through 5 years, indicating a moderately higher interest rate environment in the US over that period.

- EUR-GBP is flat MoM as markets continue to predict when the ECB and BOE will begin lowering their respective rates.
- The cost of hedging via options for EUR-GBP decreased marginally, by up to 7%, depending on the level of protection sought, amid a lower FX volatility backdrop.
- FX forward rates are still a benefit for EUR sellers, out through 5 years, as markets price in the first rate cut from the ECB for June, versus August from the Bank of England.

GBP-USD Spot Rate: 1.262	<u>6mo</u>	<u>12mo</u>	<u>18mo</u>
Forward rate	1.263	1.265	1.266
GBP Put Option* (ATMS**)	\$2.39m	\$3.52m	\$4.23m
GBP Put Option* (5% OTMS***)	\$0.66m	\$1.57m	\$2.21m
* GBP 100m Put option premium			
** At-the-money Spot rate:	1.262		
*** 5% Out-of-the-money vs Spot rate:	1.199		

EUR-GBP Spot Rate: 0.855	<u>6mo</u>	<u>12mo</u>	<u>18mo</u>
Forward rate	0.860	0.866	0.873
GBP Put Option* (ATMS**)	€1.96m	€3.27m	€4.27m
GBP Put Option* (5% OTMS***)	€0.29m	€1.03m	€1.75m
* GBP 100m Put option premium			
** At-the-money Spot rate:	0.855		
*** 5% Out-of-the-money vs Spot rate:	0.897		

Data source: Refinitiv and ICE Data Services, as of 28<sup>th</sup> March 2024

## Hedging Advisory and Derivatives Execution team



Hedging Strategy Advice



Outsourced Derivative Execution



Financial Market Knowledge



Derivative Pricing Expertise



**Paolo Esposito**  
Lead Director

+44 20 7007 8964  
[pesposito@deloitte.co.uk](mailto:pesposito@deloitte.co.uk)



**Mark Beckett**  
Director

+44 20 7303 7849  
[mbeckett@deloitte.co.uk](mailto:mbeckett@deloitte.co.uk)



**Svenja Schumacher**  
Director

+44 20 7007 9363  
[scschumacher@deloitte.co.uk](mailto:scschumacher@deloitte.co.uk)



This publication has been written in general terms and we recommend that you obtain professional advice before acting or refraining from action on any of the contents of this publication. Deloitte LLP accepts no liability for any loss occasioned to any person acting or refraining from action as a result of any material in this publication.

Deloitte LLP is a limited liability partnership registered in England and Wales with registered number OC303675 and its registered office at 1 New Street Square, London EC4A 3HQ, United Kingdom.

Deloitte LLP is the United Kingdom affiliate of Deloitte NSE LLP, a member firm of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee ("DTTL"). DTTL and each of its member firms are legally separate and independent entities. DTTL and Deloitte NSE LLP do not provide services to clients. Please [click here](#) to learn more about our global network of member firms.

© 2024 Deloitte LLP. All rights reserved.  
Designed by CoRe Creative Services. RITM1299442