

U.S. Interest Rates Chartbook

May 2017



Takeaways

- ◆ FOMC minutes and FedSpeak have signaled FOMC readiness to raise the Fed funds rate by another 25bp at its next meeting in June. The Committee's commitment to the gradual reduction of its balance sheet "later this year" remains unchanged and will likely be green lighted once the policy rate extends midway towards the median of the FOMC projected long-run rate of 3.00%

"With the federal funds rate projected to be in the range that is midway to the Committee's projection of the long-run value of the federal funds rate later this year, I would consider it reasonable to assess that this threshold will have been attained before too long"
May 30, 2017, Governor Lael Brainard Speech

"I would view it as appropriate to continue to gradually raise rates. I would also see it as appropriate to begin the process of reducing the size of the balance sheet later this year"
June 1, 2017, Governor Jerome Powell Speech

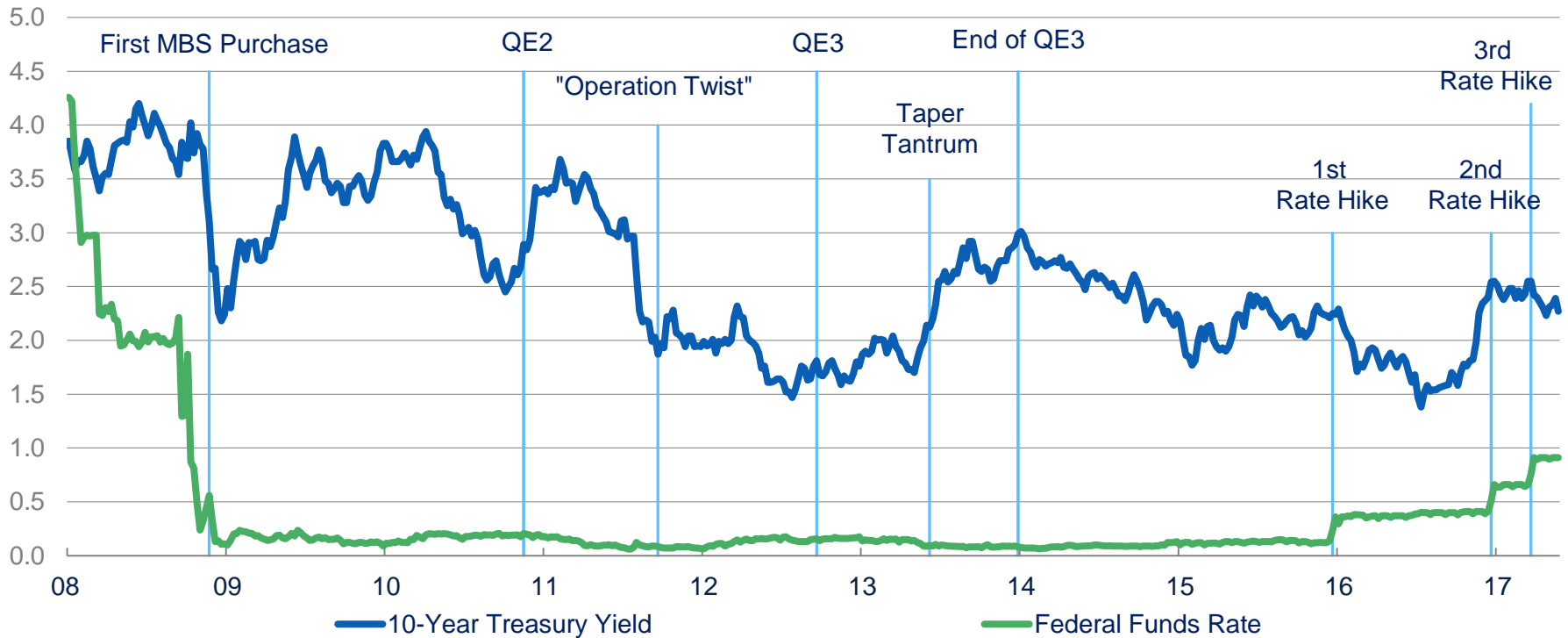
- ◆ The Fed funds futures market is aligned with the FOMC, pricing in two more rate hikes in 2017 with a 98% implied probability for the next rate increase in June, followed by a rate increase in December
- ◆ The yield curve flattens under newly resumed downward pressure on long-term yields as inflation expectations and term premium edge down
- ◆ The baseline is for a gradual increase in long-term yields



Unconventional Monetary Policy

FEDERAL FUNDS RATE AND 10-YEAR TREASURY NOTE

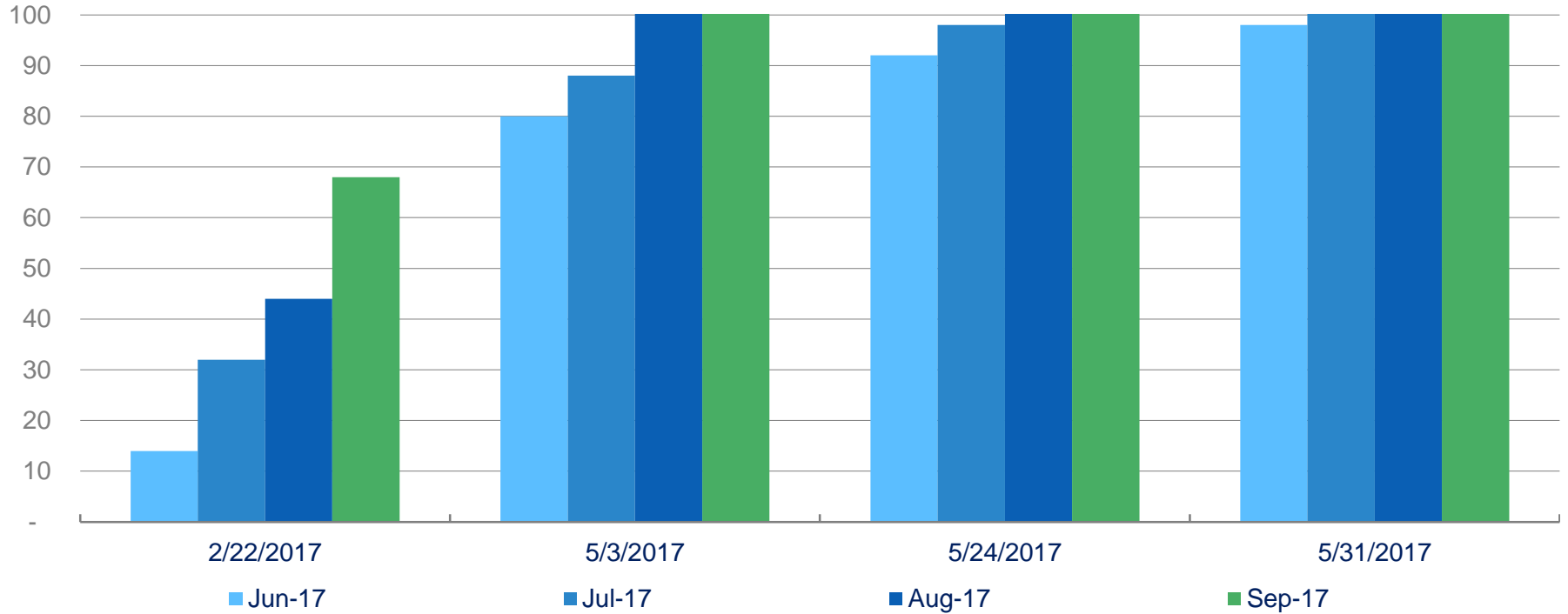
(%)



Source: BBVA Research, Federal Reserve Board and Haver Analytics

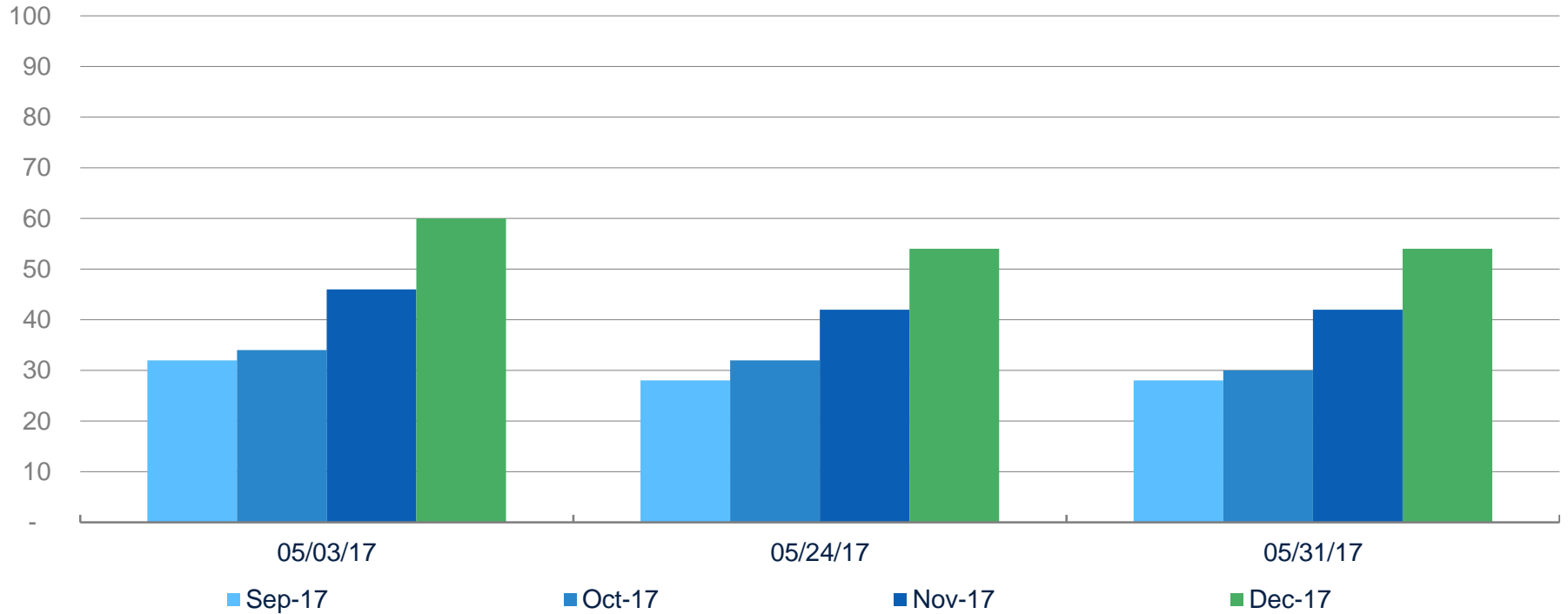
June Rate Hike Probability is at 98%

FED FUNDS FUTURES IMPLIED PROBABILITIES, FOURTH 25BP HIKE
(%)



Fifth Rate Hike is Priced in for 4Q17

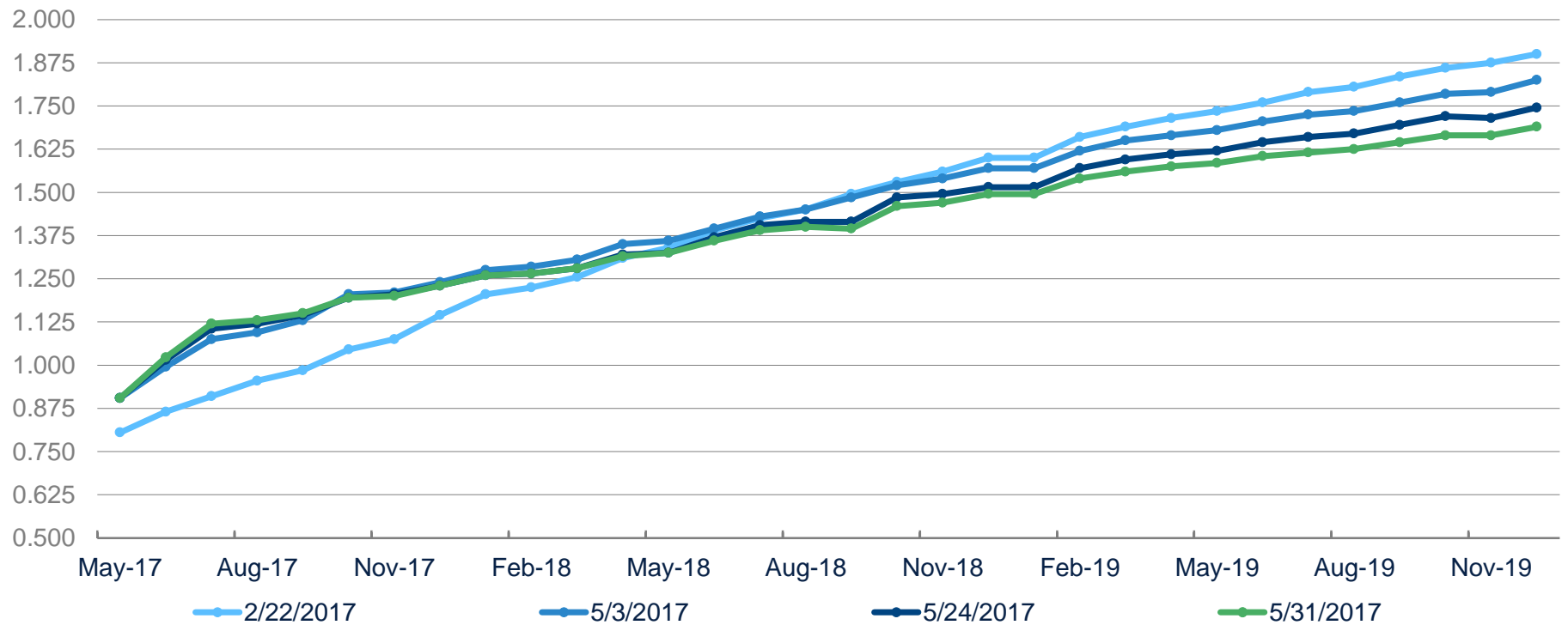
FED FUNDS FUTURES IMPLIED PROBABILITIES, FIFTH 25BP HIKE
(%)



Fed Funds Futures Curve

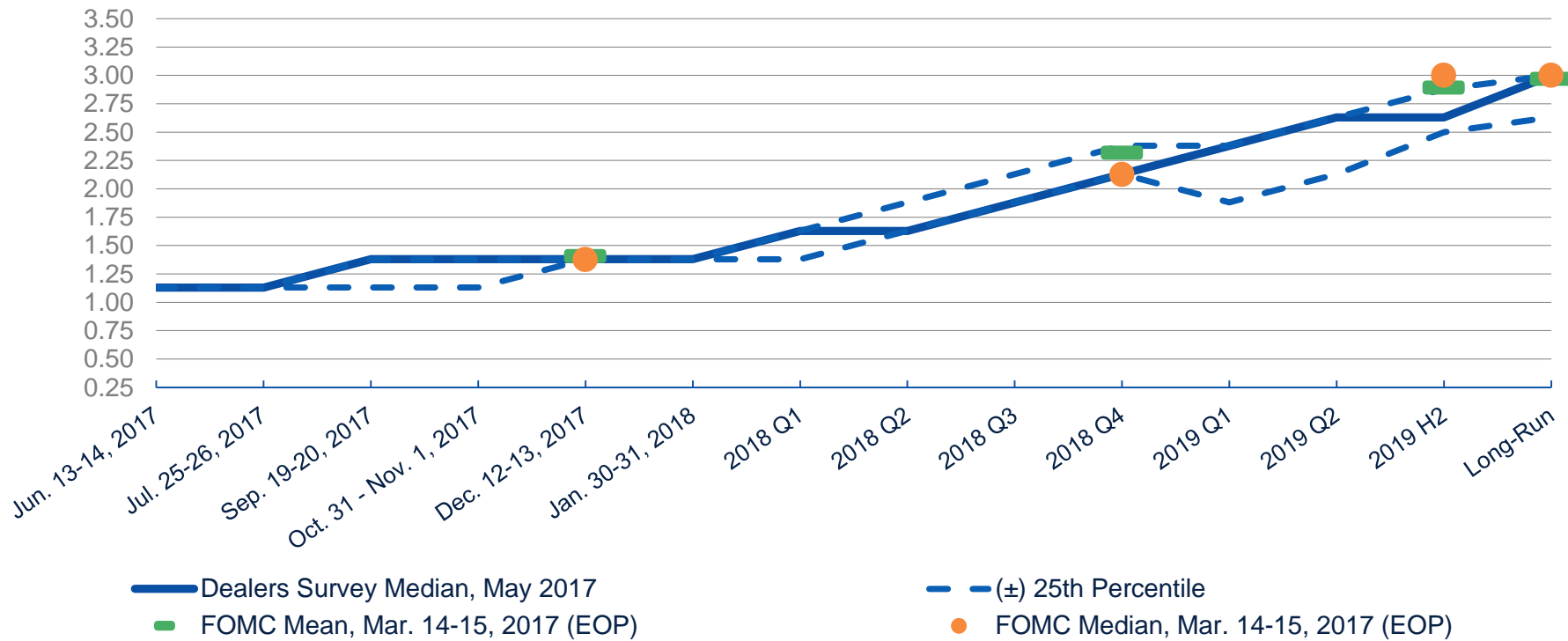
FED FUNDS FUTURES – MOST RECENT, 1 WEEK PRIOR, 1 MONTH PRIOR, 3 MONTHS PRIOR

(%)



Dealers' expectations match the FOMC policy firming path for the end of 2017 to 2018

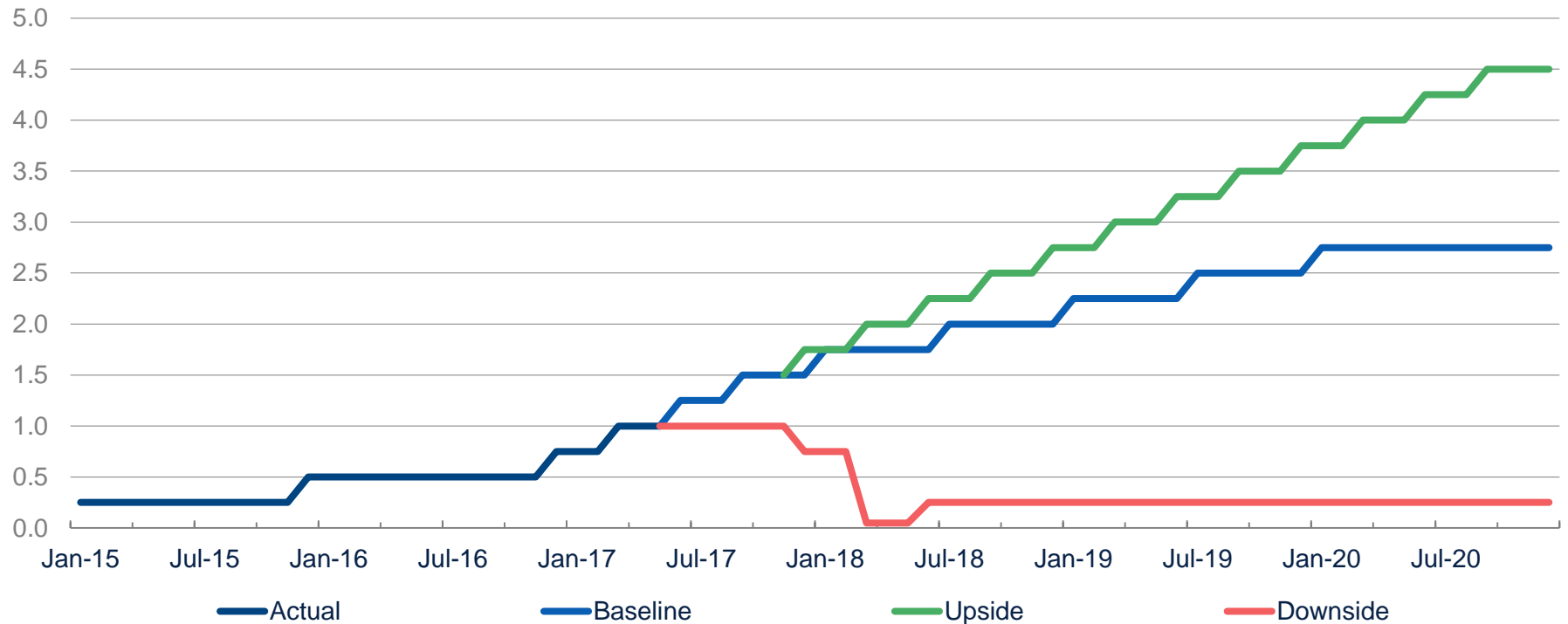
PROJECTED PACE OF POLICY FIRMING
(%)



Source: BBVA Research, Federal Reserve Bank of New York and Federal Reserve Board

BBVA Fed Funds Firming Pace Forecast

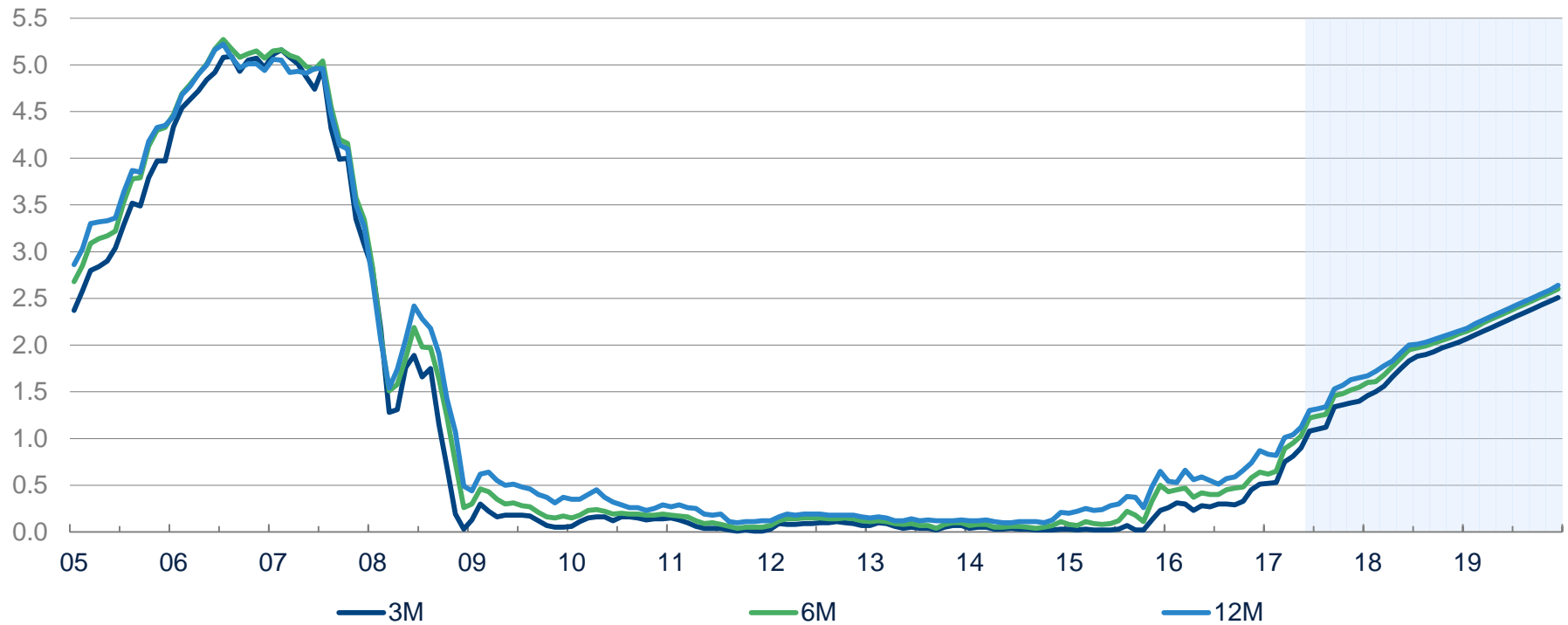
FEDERAL FUNDS RATE
(%, Upper Bound, End of Period)



Source: BBVA Research, Federal Reserve Board and Haver Analytics

BBVA Baseline Forecasts of Treasury Bill Yield

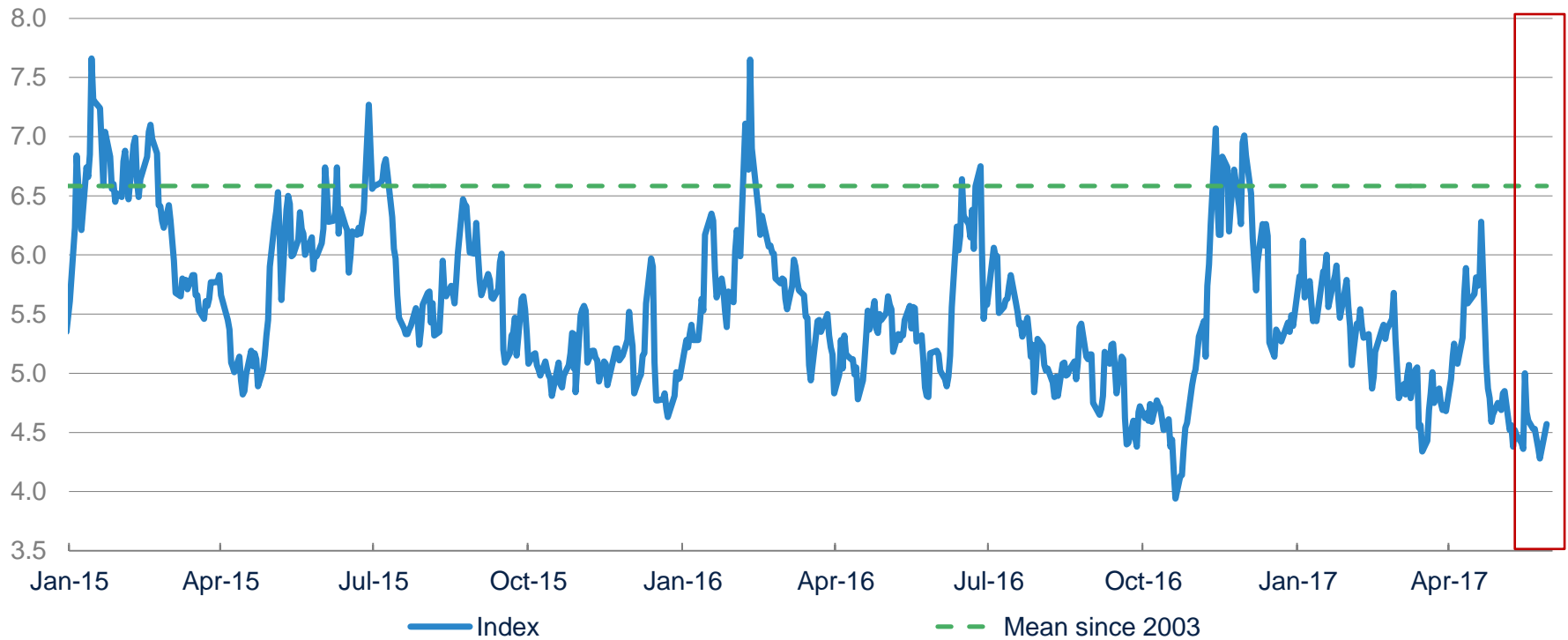
3-MONTH TO 12-MONTH RATES
(%)



Source: BBVA Research, Federal Reserve Board and Haver Analytics

Long-Term Yield Volatility Has Normalized Below Historic Mean

10-YEAR U.S. TREASURY NOTE VOLATILITY
(Daily index)

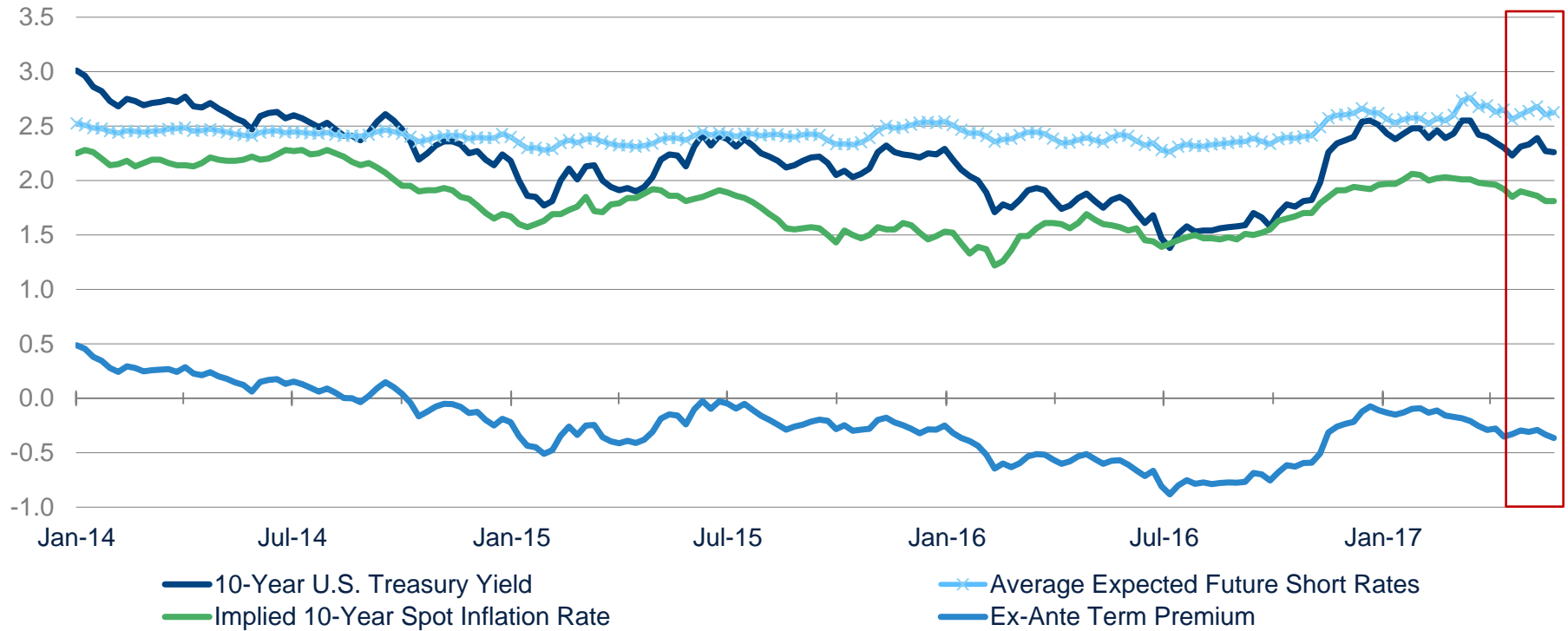


Index measures a constant 30-day expected volatility of 10-Year Treasury Note futures prices, and is calculated based on transparent pricing from the Chicago Board of Trade's actively traded options on the Treasury Note futures

Downward Pressure on Term Premium Resumed

10-YEAR U.S. TREASURY TERM PREMIUM & MARKET INFLATION EXPECTATIONS

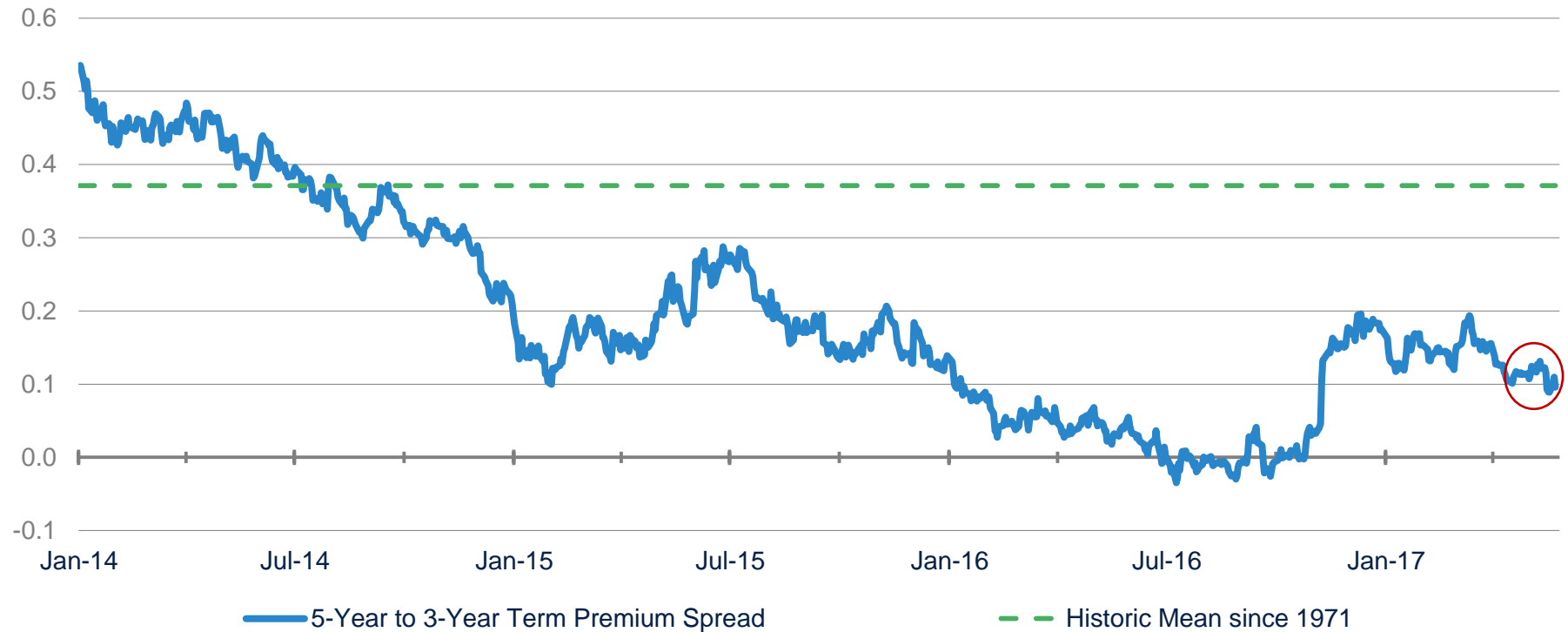
(Weekly, %)



Mid-Term Duration-Risk Compression Has Stabilized at 11 Basis Points

DURATION-RISK COMPRESSION

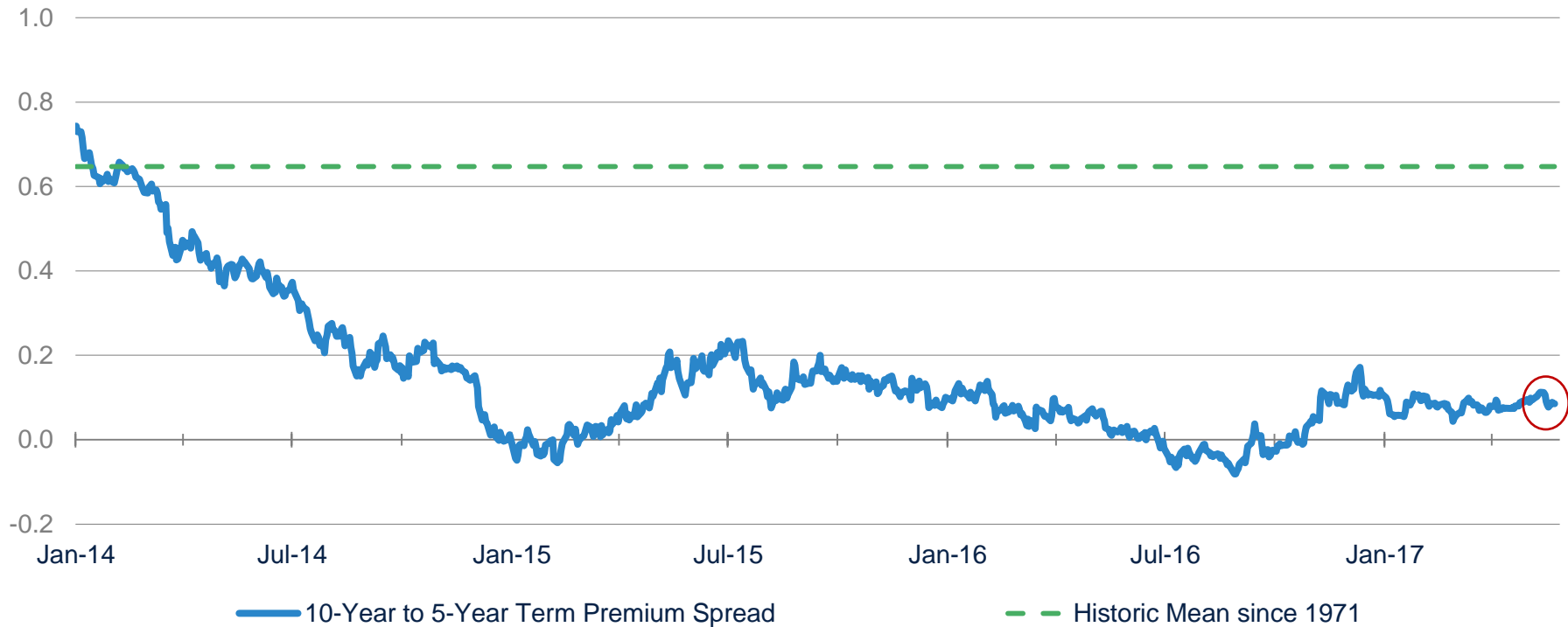
(Daily, %)



Calculated as the difference between 5-Year and 3-Year term premium reported by the New York Fed ACM (Adrian, Crump, and Moench) five-factor, no-arbitrage term structure model incorporating pricing factors.

Long-Term Duration-Risk Compression Has Stabilized at 10 Basis Points

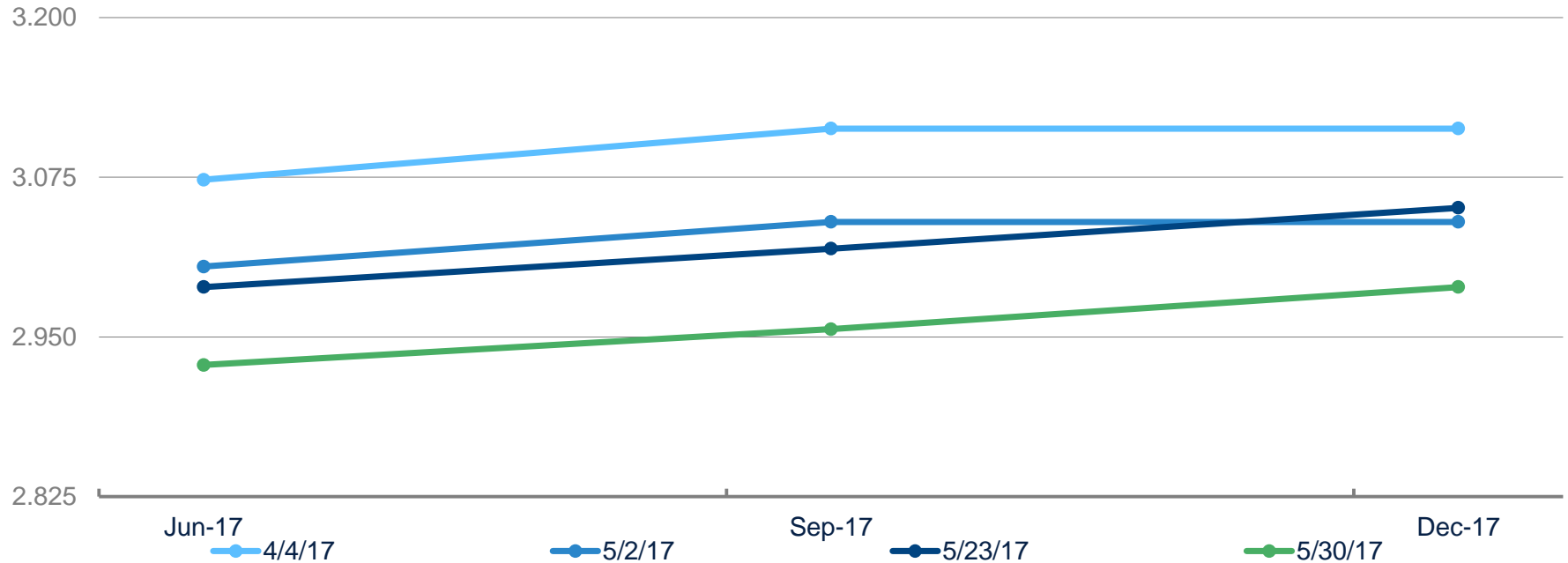
DURATION-RISK COMPRESSION
(Daily, %)



Calculated as the difference between 10-Year and 5-Year term premium reported by the New York Fed ACM (Adrian, Crump, and Moench) five-factor, no-arbitrage term structure model incorporating pricing factors.

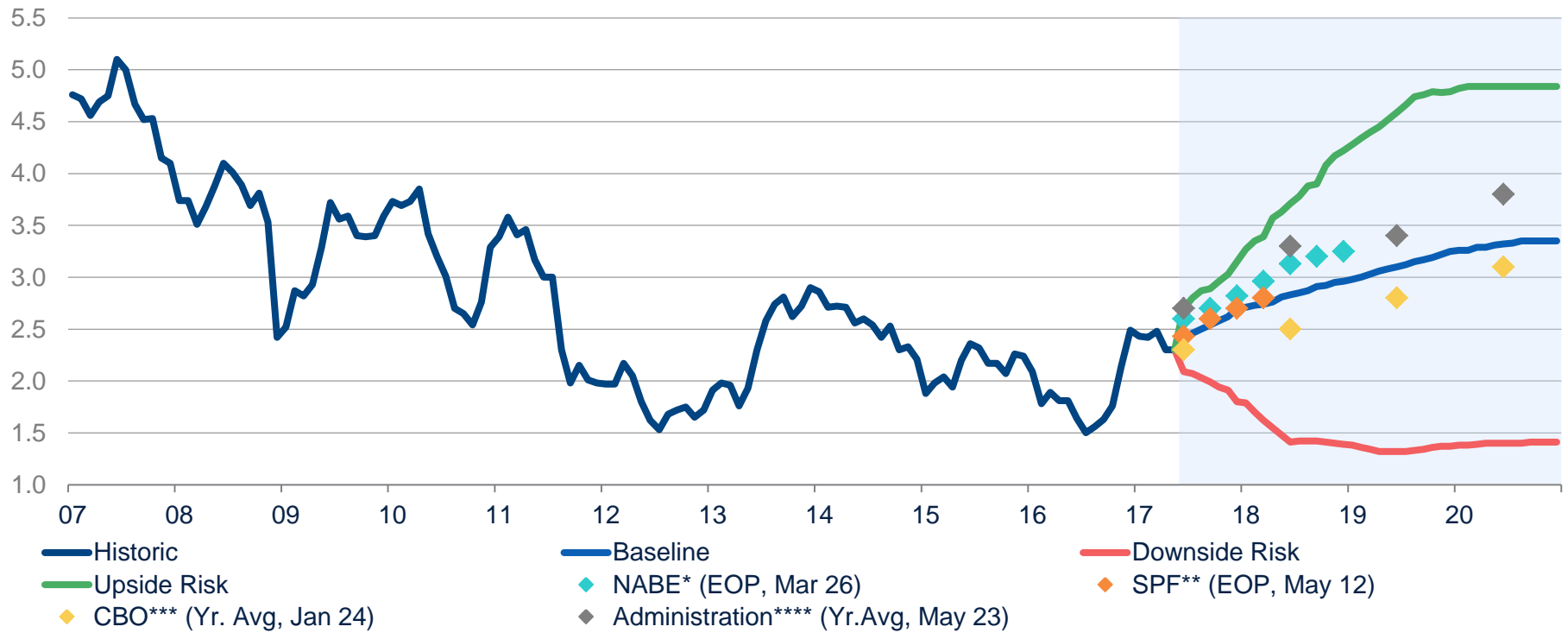
Futures Declined, Discounting a 6bp Raise in 10YTN Yields Over the Next 2 Quarters

10-YEAR U.S. TREASURY YIELD FUTURES – MOST RECENT, 1 WEEK PRIOR, 1 MONTH PRIOR, 3 MONTHS PRIOR (%)



10-Year Treasury Yield Forecasts

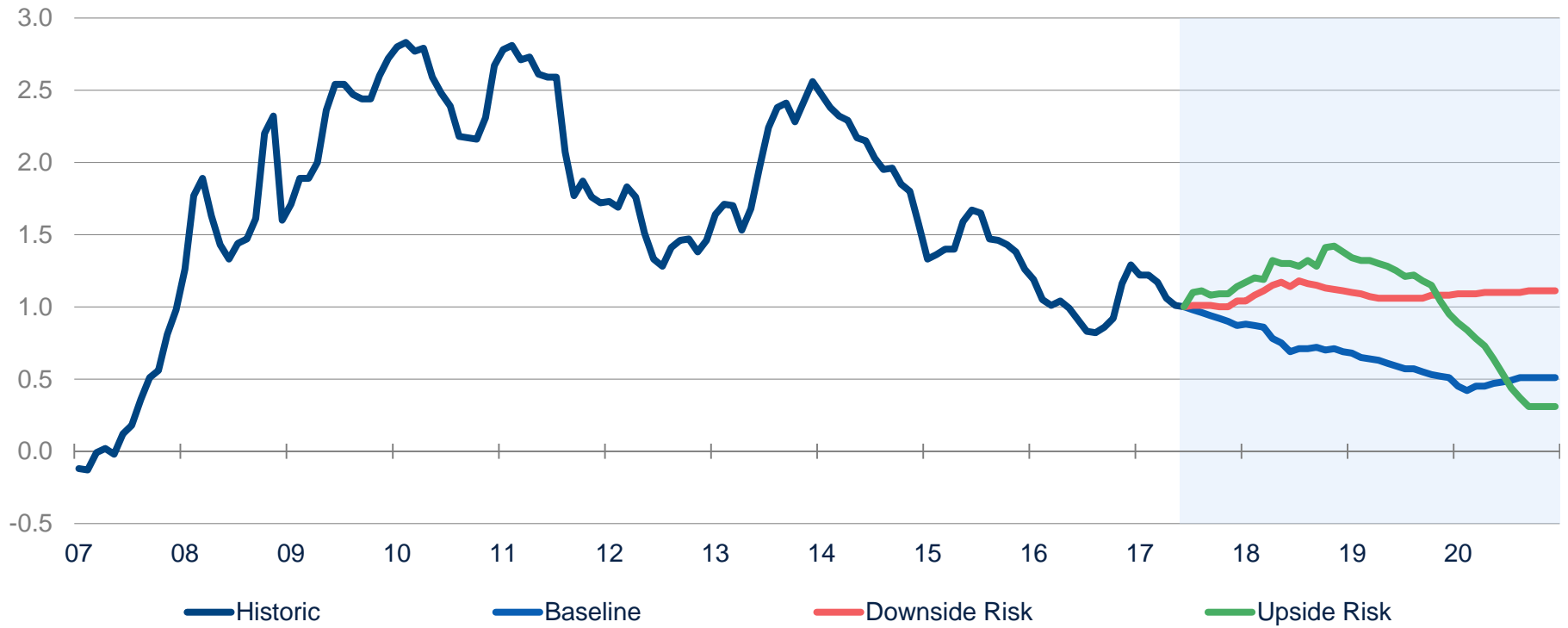
10-YEAR U.S. TREASURY YIELD (%)



* National Association for Business Economics (NABE) Outlook median forecast compiled from a panel of NABE members. Last release date March 26, 2017
 ** Survey of Professional Forecasters (SPF) conducted by Federal Reserve Bank of Philadelphia. Last release date May 12, 2017
 *** Congressional Budget Office (CBO). Last release date January 24, 2017
 **** Administration: 2018 Budget. Last release date May 23, 2017

Yield Curve Slope Forecasts

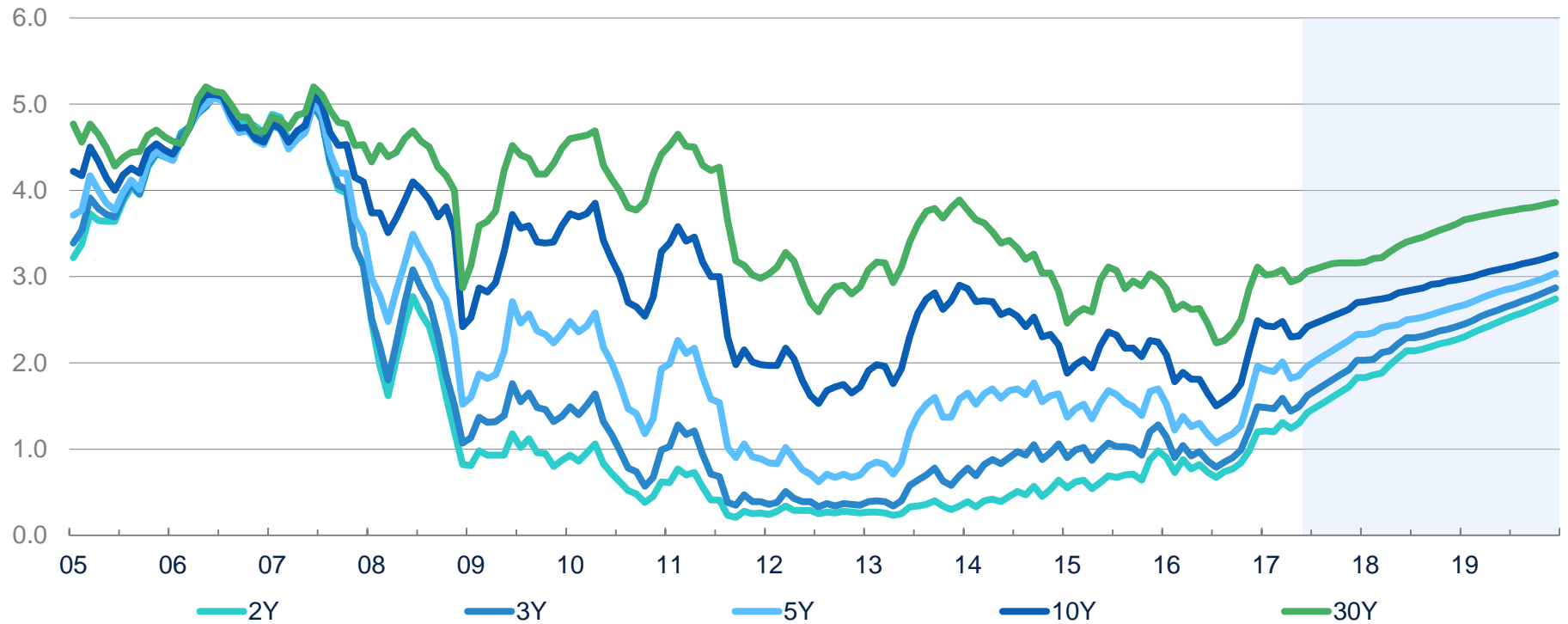
TREASURY YIELD CURVE SLOPE
(%, 10Y-2Y)



Source: BBVA Research, Federal Reserve Board and Haver Analytics

Treasury Yield Curve Baseline Forecasts

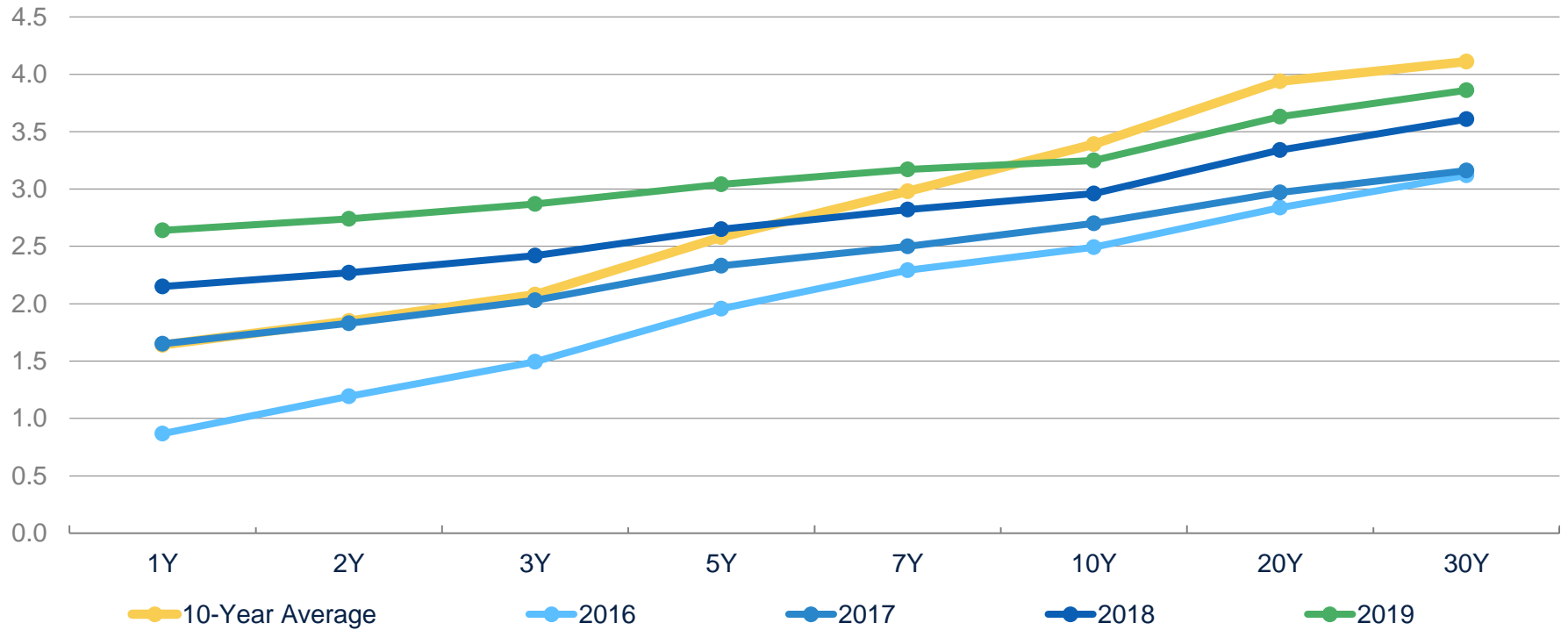
U.S. TREASURY YIELD CURVE
(%)



Treasury yield curve is estimated with a three-factor no-arbitrage model linked to macroeconomic factors measuring growth, inflation and monetary policy. Estimates are based on BBVA research baseline forecast for GDP growth, inflation and Fed funds rate.

Yield Curve Forecasts

TREASURY YIELD CURVE BASELINE FORECAST
(%, End of Period)

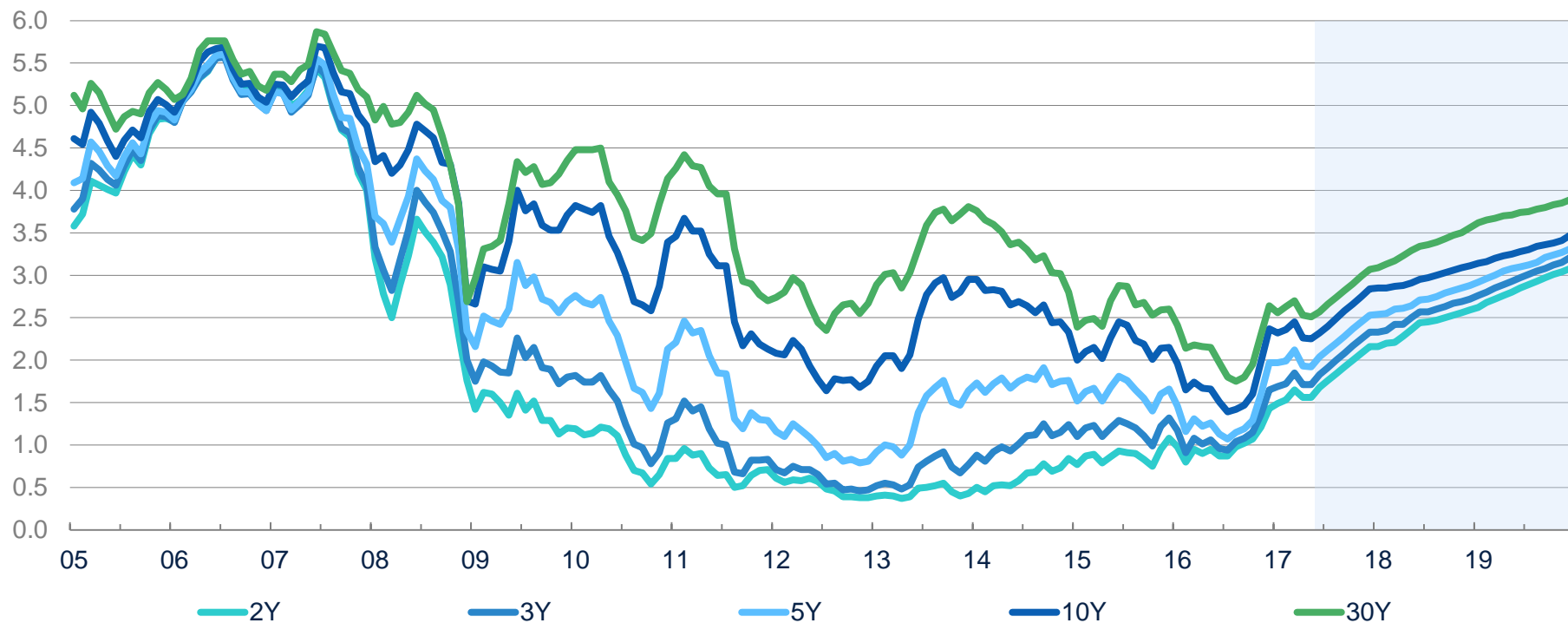


Treasury yield curve is estimated with a three-factor no-arbitrage model linked to macroeconomic factors measuring growth, inflation and monetary policy. Estimates are based on BBVA research baseline forecast for GDP growth, inflation and Fed funds rate.

Swap Curve Baseline Forecasts

U.S. SWAP RATES

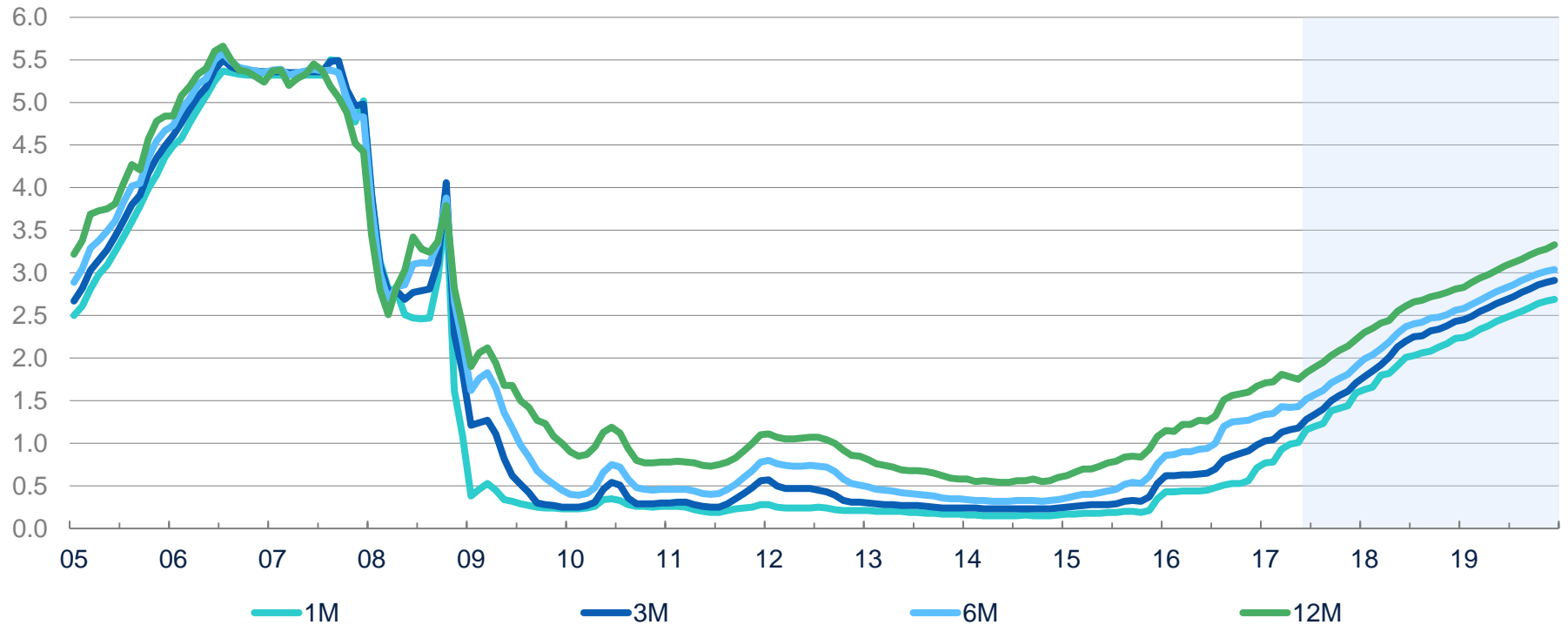
(%)



Source: BBVA Research, Federal Reserve Board and Haver Analytics

LIBOR Curve Baseline Forecasts

U.S. DOLLAR LIBOR RATES
(%)



Source: BBVA Research, Federal Reserve Board and Haver Analytics

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