Rate hike expectations ease as term SOFR curve flattens

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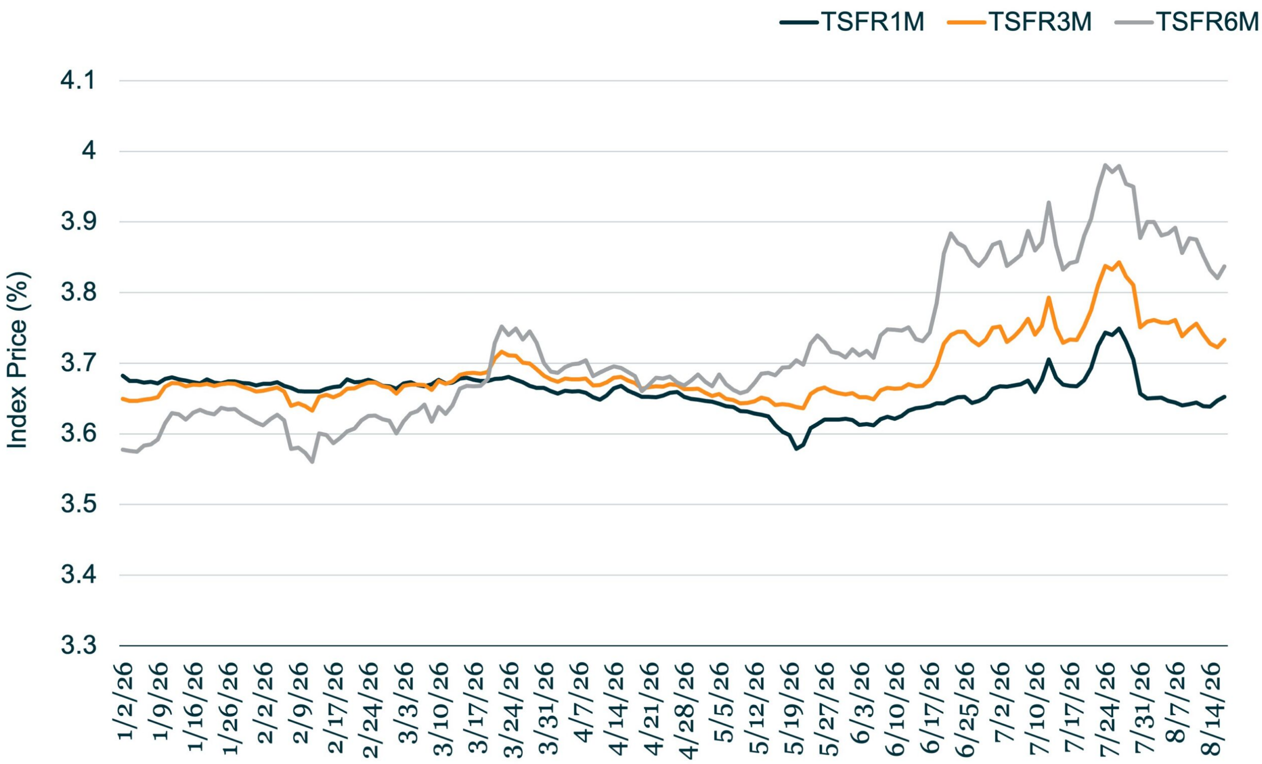

Source: Bloomberg Data

The CME six-month Term SOFR rate reached a recent high of 3.979% on July 28 before retreating to 3.837% as of August 18. Over the same period, the six-month premium over one-month Term SOFR narrowed from a high of 25 basis points to 18bps. The move suggests that while investors have scaled back expectations for a Federal Funds Rate increase over the next six months, the market continues to price in a higher-for-longer rate environment, with limited expectations for near-term cuts.

Following the Federal Open Market Committee meeting on July 29, six-month Term SOFR declined by approximately 10bps over the subsequent three sessions. The rate fell another 5bps following the weaker-than-expected August 7 employment report, further tempering expectations for tighter monetary policy.

The shift in rate expectations has been significant since the beginning of the year. In January, one-month Term SOFR traded at a 10.5 basis point premium to the six-month benchmark, reflecting expectations that the Federal Reserve would continue easing monetary policy. That dynamic reversed on March 19, when the curve inverted and six-month Term SOFR moved to a premium over the one-month rate, signaling a meaningful shift toward a more hawkish outlook. That hawkishness intensified through the summer before peaking in late July.