

Rates Spark: Funds rate now below 10yr SOFR

We have published our 2026 Rates Outlook, which you can find [here](#). On the Fed, it was a cut with some hawkish undertones, but Chair Powell showed more concern about the labour market than about inflation risks. And the outcome came with something bordering on renewed quantitative easing, given the leeway to go out to 3yr Treasuries if needed



Finally, we have the funds rate below 10yr SOFR – now that's more normal

The recent FOMC meetings share a theme: rates are converging toward what appears to be a landing zone on several fronts, even if only temporarily. The balance sheet is now on freeze (there is a floor set for bank reserves), and the funds rate is now close to where it is looking more normal, or at least close to it. Let's delve into both.

First, the level of the funds rate and floating rates in general. The 3mth SOFR rate is finally below the 10yr SOFR rate (just this week). Which means, at long last, it's cheaper to fund floating than to fund fixed. This is with the 10yr SOFR having been under rising pressure in the past weeks, but also

as the 3mth SOFR has been tamed by the rate-cutting narrative. It's the first time since the second half of 2022 (and briefly in January 2025) that the 10yr SOFR rate has been above most floating rates, and that will be copper-fastened as soon as the Fed cuts by 25bp in a bit. For players who have baulked at the idea of swapping to floating on account of negative impact carry, that has now gone away (at least for as long as 10yr SOFR remains elevated).

Second, liquidity conditions. Repo has been trending tight in the past few months, and things reached a point of no return when the effective funds rate began to de-anchor and trek towards the rate on excess reserves (now just 1bp below). The Fed reacted at the previous FOMC meeting by reverse engineering this into a rationale for freezing the balance sheet, where further MBS roll-offs would be matched by T-bills buying. But as we've noted, the Fed will ultimately have to re-expand the balance sheet at the same pace as the nominal economy is growing. So, if nominal GDP is growing at 3-5%, bank reserves too should expand at that rate. The Fed has reacted to this reality by implementing flexibility to buy T-bills in excess of the MBS roll-off, to ensure ample reserves.

Reserve management purchases is the term the Fed is using to describe its T-bill buying agenda, as in fact they can go out as far as three years in Treasuries if needed. That's quite deviant from a pure T-bills buying programme, and bordering in fact on QE. They'll start with \$40bn of buying, and suggest it will wane in later months due to seasonal liquidity circumstances. Good for the front end!

Thursday's events and market views

From Europe, we have little notable data, but the US should publish trade balance data for September and also the weekly jobless claims. Consensus sees the jobless claims rising to 220k from the previous 191k reading. Furthermore, the Bank of England's Andrew Bailey will speak about financial stability.

In terms of issuance, we have Italy with 3Y, 4Y and 5Y BTPs for a total of €5bn. The US will auction a 30Y Bond totalling \$22bn.

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