

Brief Update on CMAST Interest Rate Projections (Q2 2022)

In response to the current low interest rate environment, FHFA has updated the methodology used to produce the interest rate projections that accompany the state-level CMAST house price paths. All interest rate projections are now driven by the evolution of the target federal funds (TFF) rate, which, *when applicable*, drops from its current level down to 0-25 basis points (bps) over the course of the first 18-months of the stress scenario. This sharp decline in the TFF rate is designed to replicate the Federal Open Market Committee's actions at the onset of the last housing crisis. All long-term relationships are estimated using data from 1996-2015. This represents a 20-year look back period from the end-date used to estimate state-level, long-run house price trends.

Prior to this methodological update, the 2- and 10-year Swap rate projections were modeled separately based upon their average rate of change between August 2007 and December 2008. During this period, the 2-year Swap rate decreased from approximately 5.0 percent to 1.8 percent and the 10-year Swap rate decreased from approximately 5.4 percent to 2.7 percent. This large and rapid decrease was predicated on August 2007 rate levels, which were a product of a higher interest rate environment. Under the updated methodology, all interest rate changes are dictated by the difference between the current TFF rate and a 0-25 bps target rate. This allows each set of rate projections to evolve at a different speed based upon the current rate environment.

In response to the rising interest rate environment, FHFA has updated the anchor point used to construct its CMAST interest rate projections. Prior to this change, interest rate projections were constructed based upon the previous quarter's market environment (e.g., the CMAST interest rate projections released in June were constructed based upon March 31st rates). To better accord with the rapid increase in rates, CMAST interest rate projections will now be constructed based upon only a one-month lag (e.g., June's CMAST interest rate projections will be constructed based upon May 31st rates).