Case Study: Identifying Value in Short-Term Floating-Rate Funding

FHLBank Boston

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Overview

- What is SOFR?
- Short-Term Funding Alternatives
- Scenario Analysis: All-In Cost & Different Rate Paths
- Case Studies: Practical Applications

SOFR 101

SOFR is an overnight secured rate tied to Treasury repo markets, and it serves as the reference point for several floating-rate advance structures.

What is SOFR?

- The Secured Overnight Financing Rate measures the cost of financing Treasury securities overnight.

How is it Calculated?

- SOFR is a New York Fed-administered rate based on transaction-level Treasury repo data.

Why is it Important?

- SOFR can move day to day, but the cost of floating-rate funding depends on where it averages over the life of the borrowing.

What Impacts SOFR?

SOFR can move with repo-market pressure, quarter-end balance sheet dynamics, collateral demand, and overall front-end funding conditions.

Policy / Front-end Rates

- Fed target range, IORB, ON RRP

Repo Market Supply/Demand

- Treasury collateral, cash supply, dealer balance sheets

Technical Dates

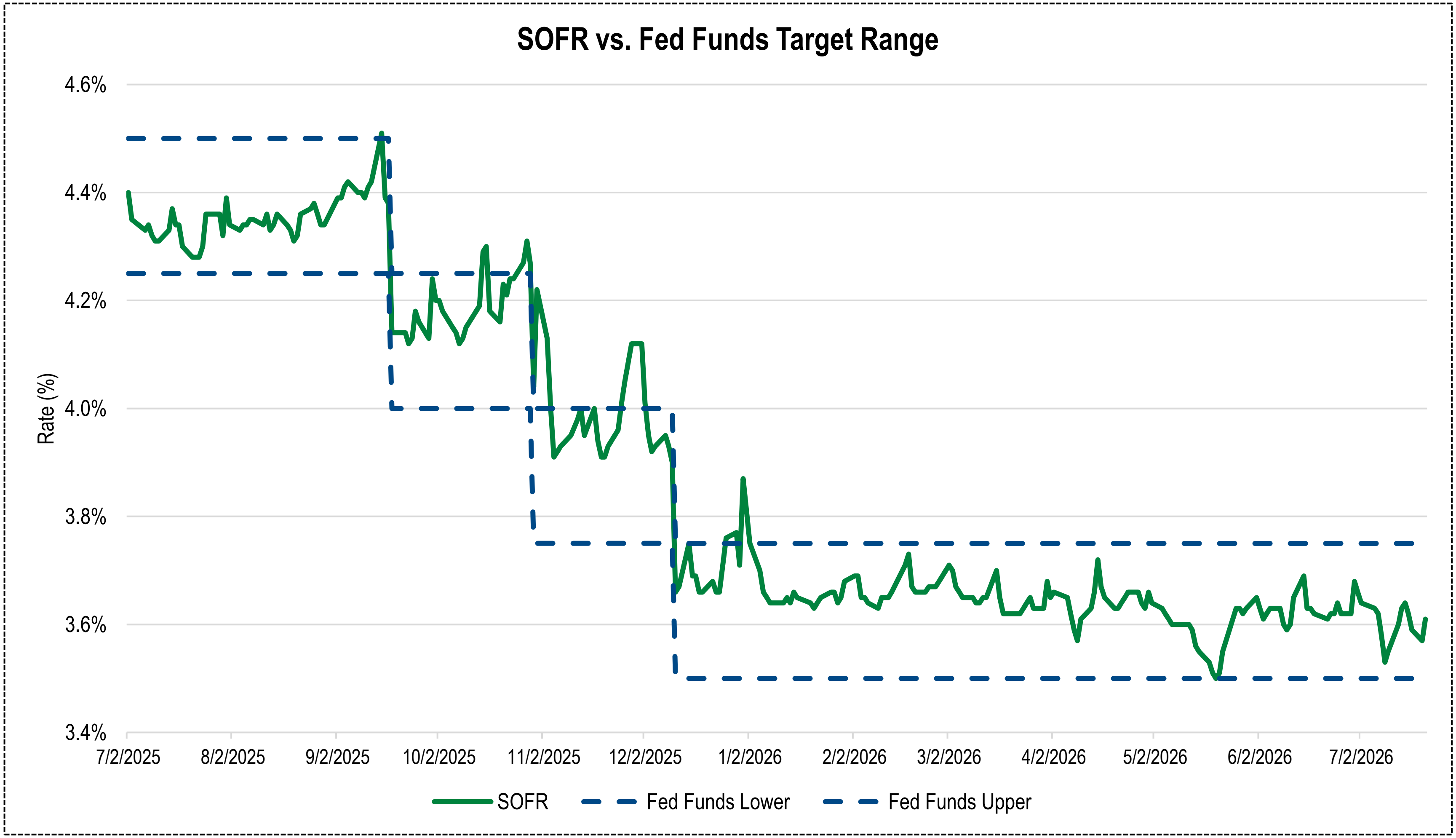
- Month-end, quarter-end, year-end

Market Stress / Balance Sheet Pressure

- Temporary spikes can occur, but averages dilute short-lived moves

SOFR & the Fed Funds Range

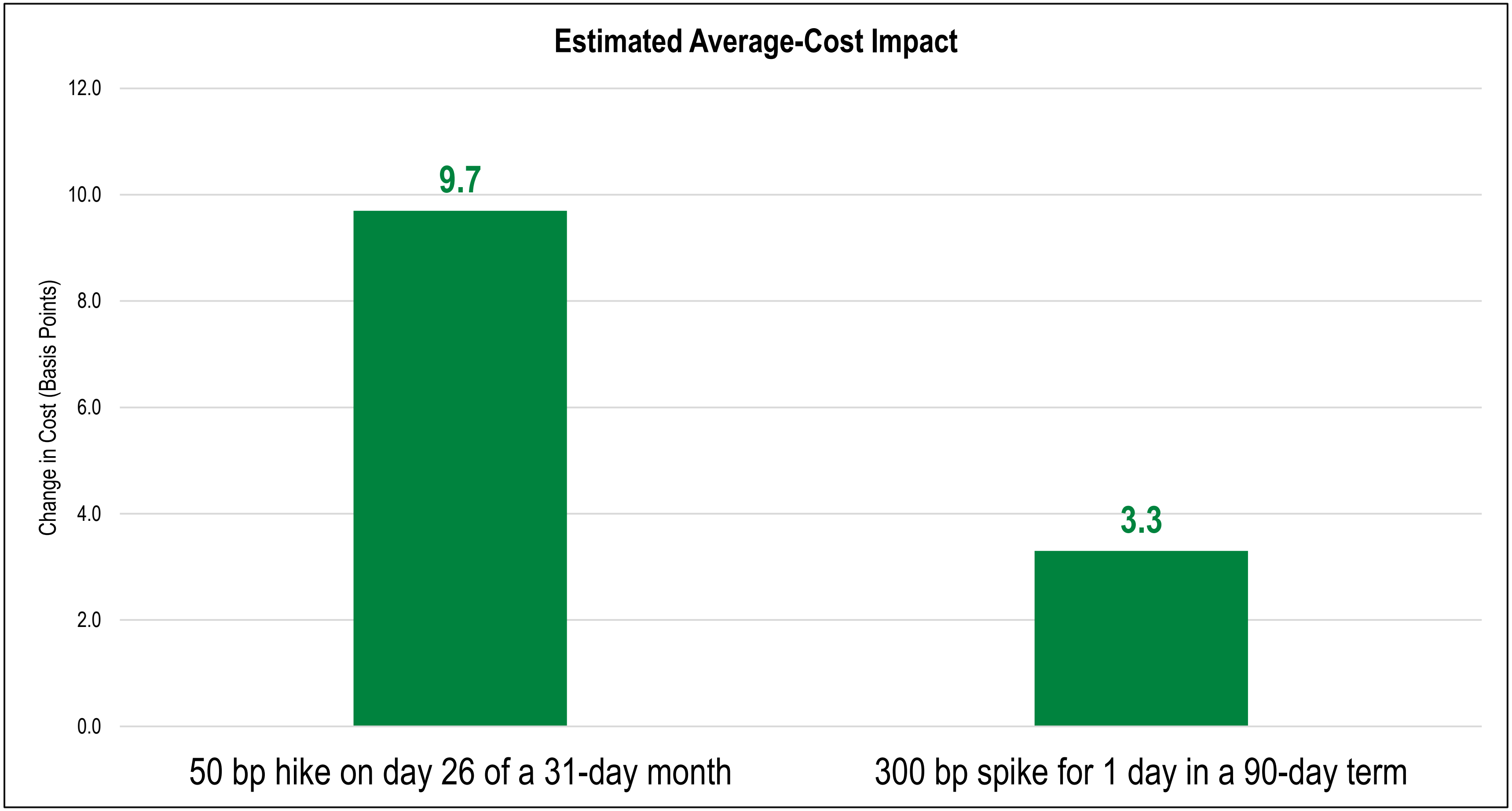
That matters because a SOFR-indexed advance can start below comparable short-term fixed alternatives.



Source: New York Fed, Federal Reserve via FRED, FHLBank Boston

Overnight Repricing Averaged Across the Term

A one-day SOFR move does not equal the cost impact over a 1-month or 3-month advance.



Source: FHLBank Boston

Approx. impact = rate shock × days affected ÷ days in term

Short-Term Advance Solutions

The right comparison depends on how long the funding need lasts and how much certainty the member wants.

Daily Cash Manager Advance

- **Fit:** Overnight or uncertain funding
- **Value:** Maximum flexibility
- **Tradeoff:** No term certainty

SOFR-Indexed Advance

- **Fit:** Short-term funding where fixed certainty may be costly
- **Value:** Term funding with floating exposure
- **Tradeoff:** Rate can reset during the term

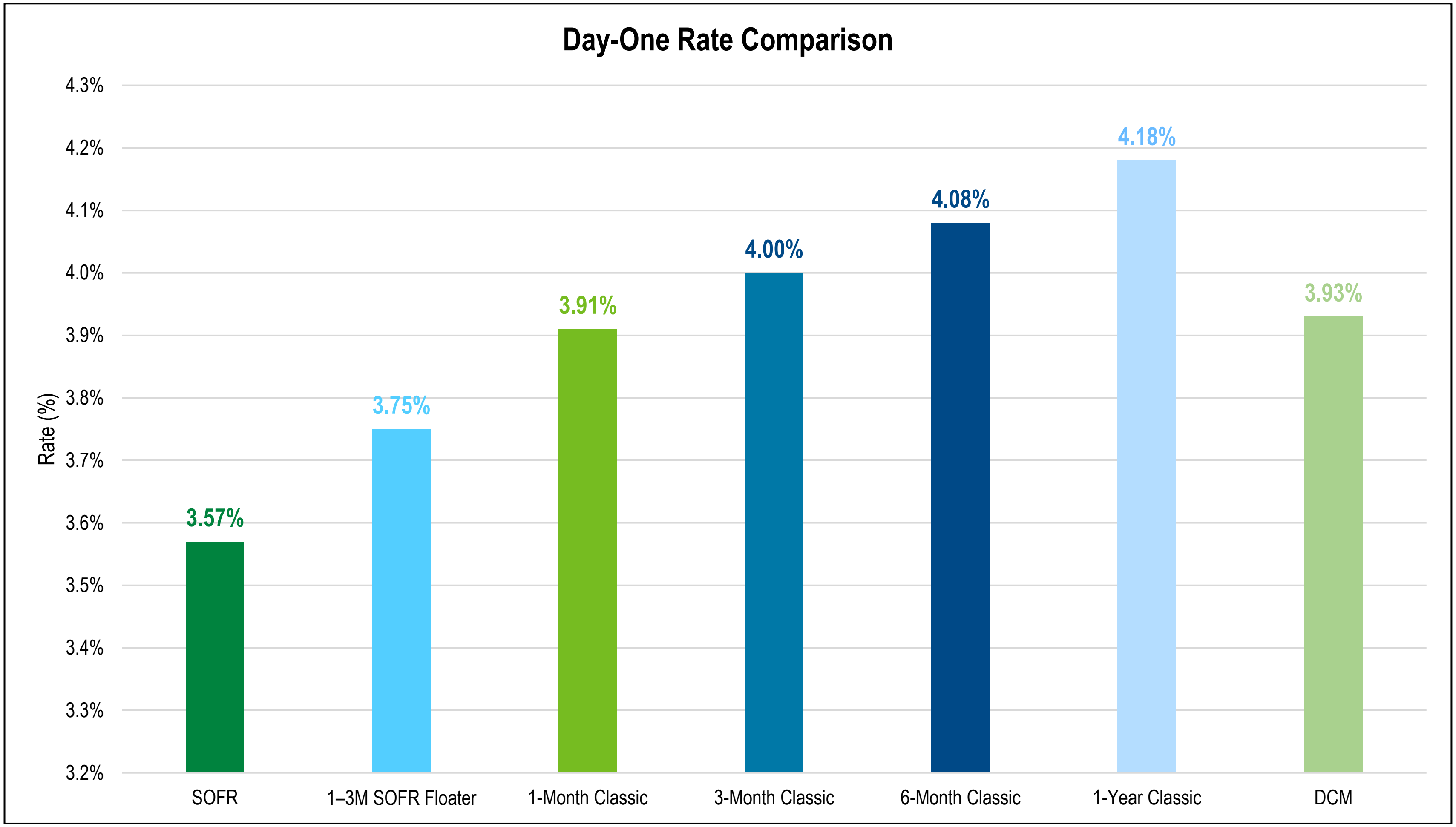
Classic Advance

- **Fit:** Known need or budget certainty
- **Value:** Fixed cost for the full term
- **Tradeoff:** Market rate expectations are already priced in

Payment timing varies by product and selected structure. The case-study model later compares nominal and present-value cost where payment timing differs.

Short-Term Solutions: Day 1 Rates

SOFR-Indexed Advance rates are currently starting below comparable short-term fixed funding, creating day-one savings.

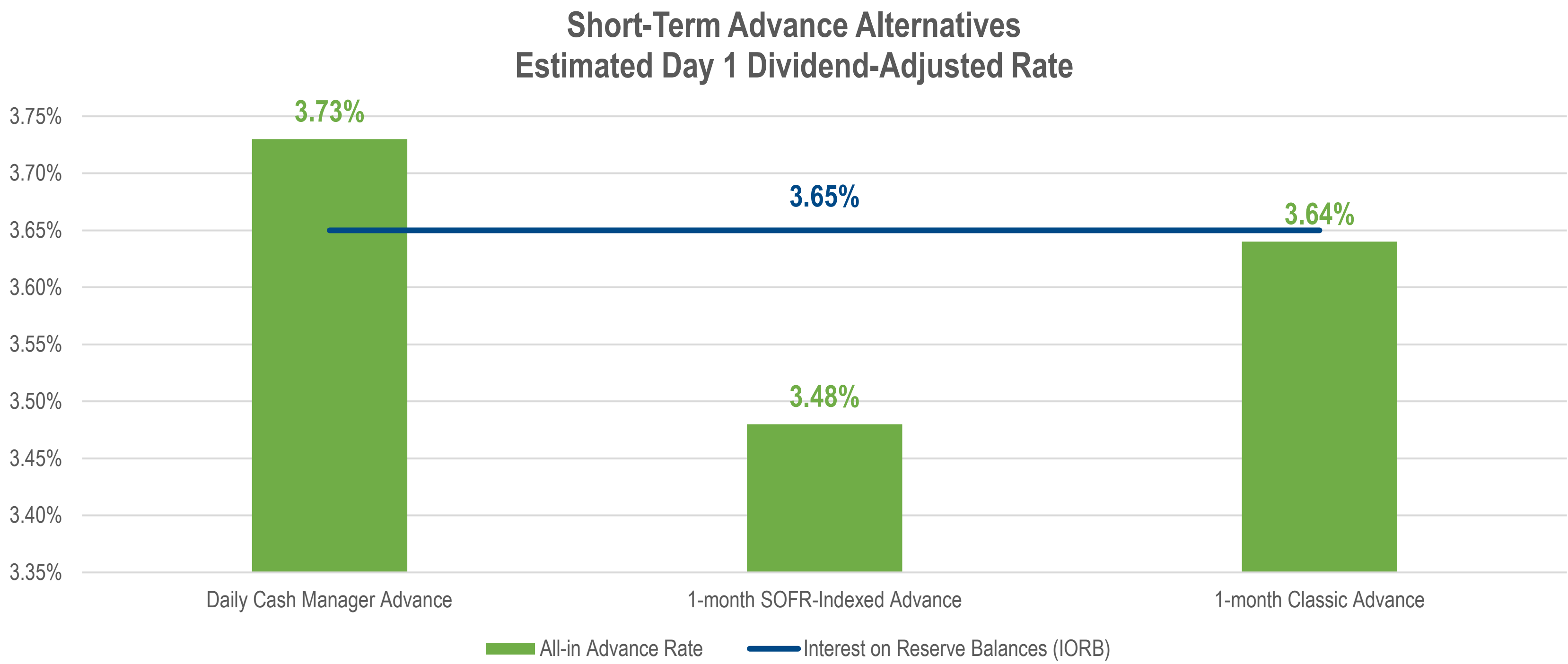


Source: New York Fed, FHLBank Boston

Classification: Public

Scenario Analysis: Unchanged Rates

The benefit of a lower starting point plus additional capital stock gives the SOFR-Indexed Advance an initial cushion vs. other short-term alternatives.

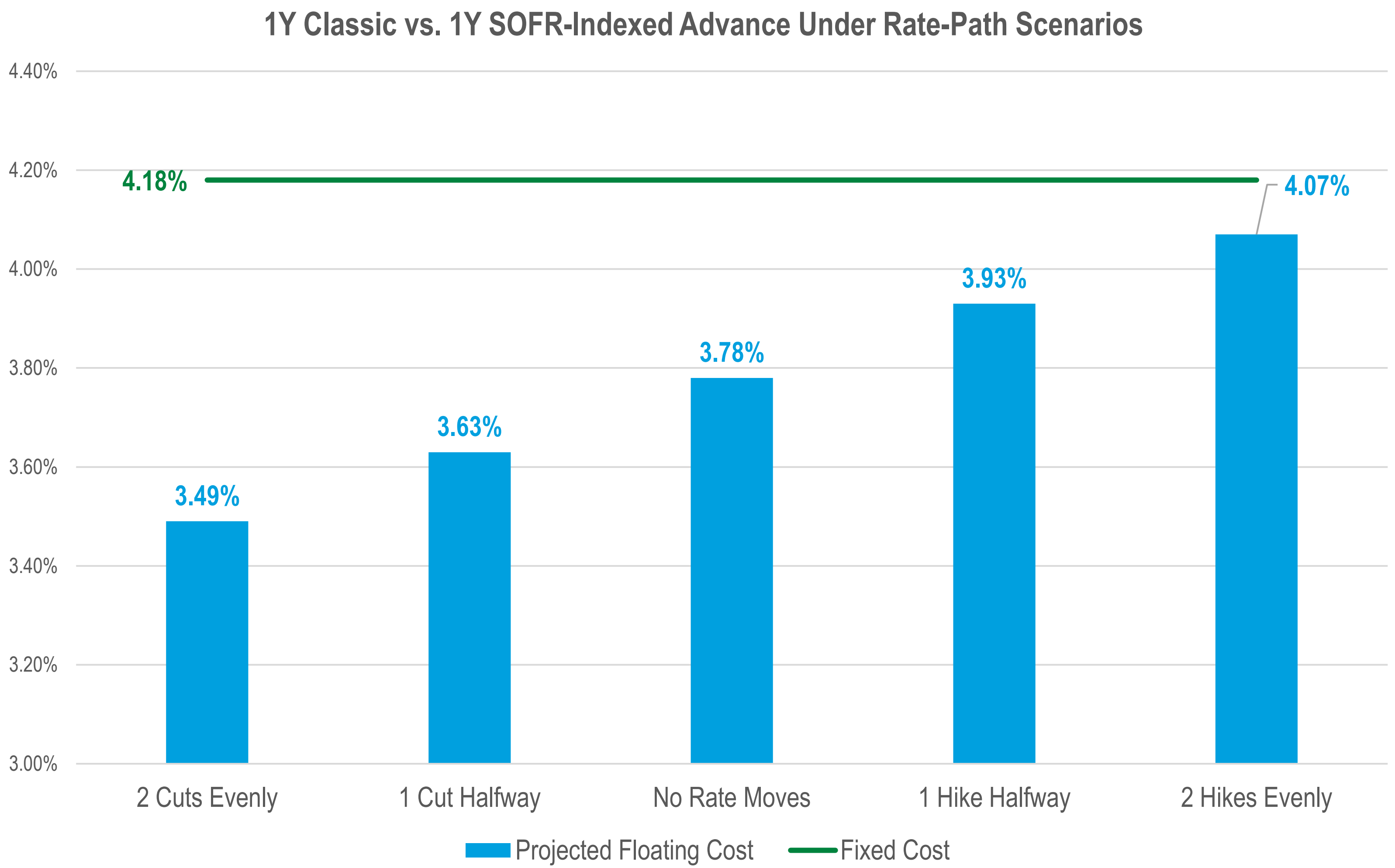


Advance Type	Posted Rate	Activity Stock	Dividend Benefit	Estimated All-in Rate	Savings vs. 1-month Classic
Daily Cash Manager	3.93%	3.00%	20.1 bp	3.73%	-8.7 bp
1-month SOFR-Indexed	3.75%	4.00%	26.8 bp	3.48%	+16.0 bp
1-month Classic	3.91%	4.00%	26.8 bp	3.64%	0.0 bp

Source: New York Fed, FHLBank Boston

Scenario Analysis: 1-Year Horizon

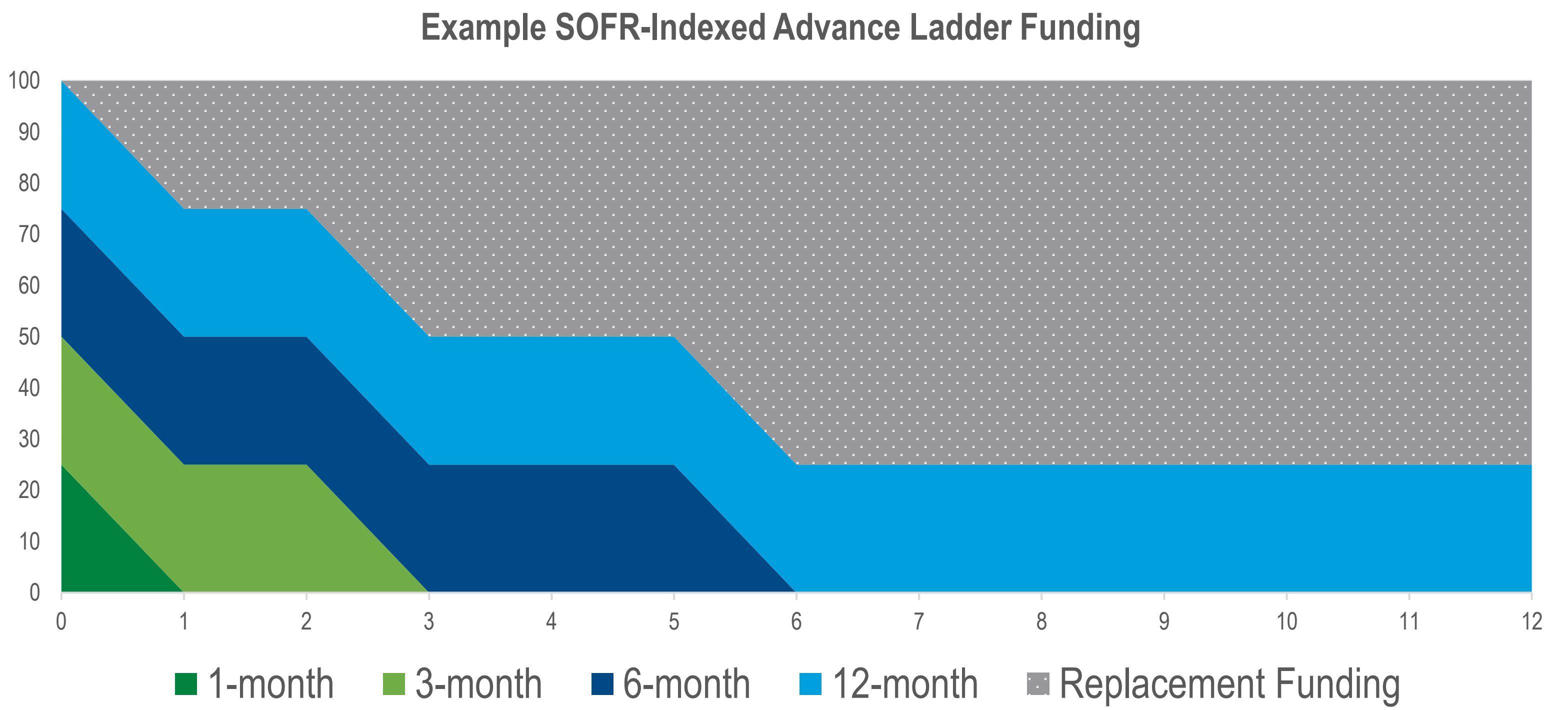
Across the displayed scenarios, floating remains below fixed; the starting cushion is not fully exhausted even after two evenly spaced 25-basis-point hikes.



Source: New York Fed, FHLBank Boston

Balancing Current & Future Liquidity Needs

As a recurring funding need proves more durable, members can layer SOFR-indexed advances by expected life while keeping flexibility to reduce, replace, or maintain the advance layer over time.

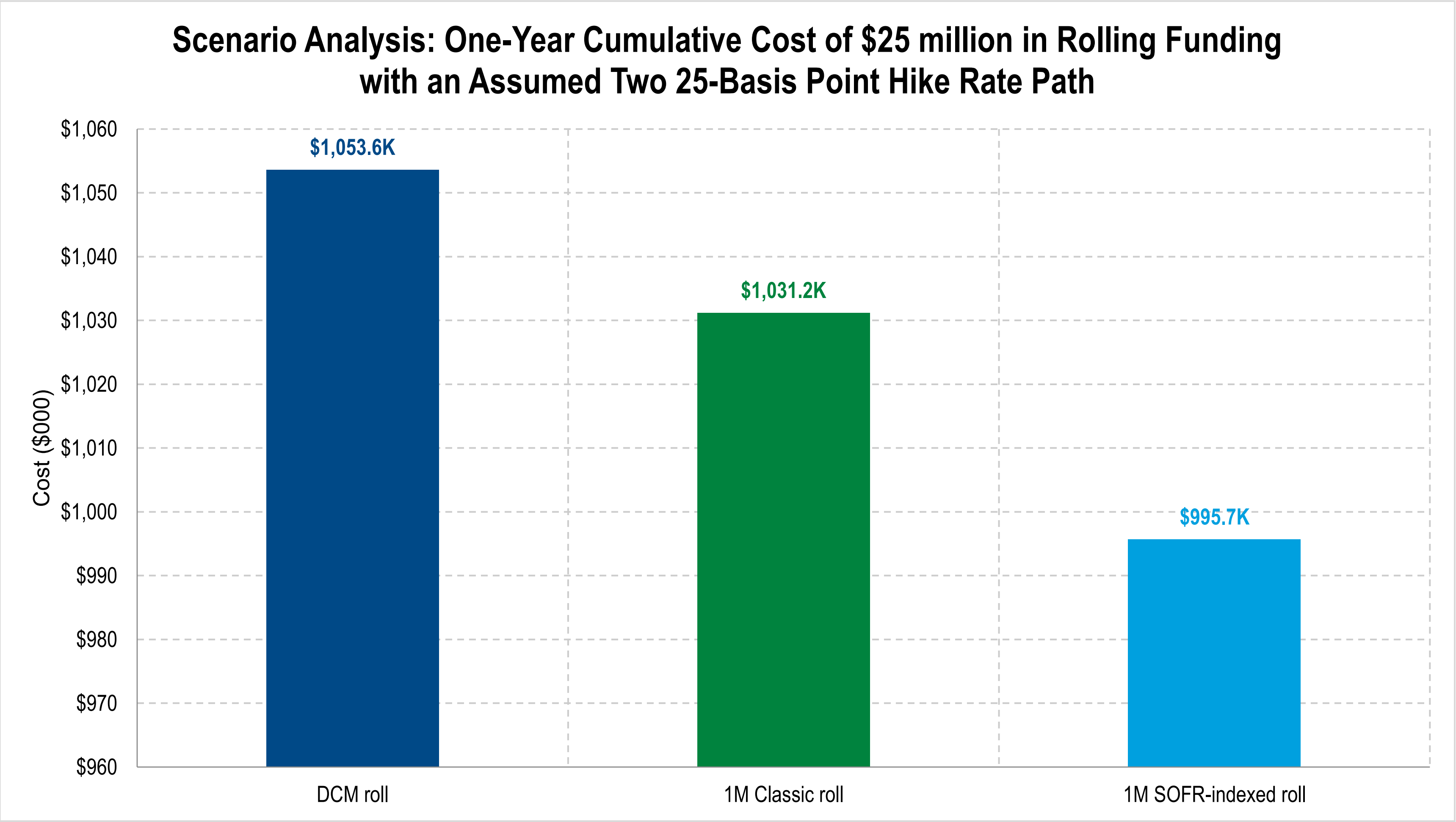


Funding Considerations		
Pay down advances efficiently if liquidity needs are reduced	Replace at shorter terms if liquidity is building up	Term out if rate conditions and balance sheet needs call for it

Source: New York Fed, FHLBank Boston

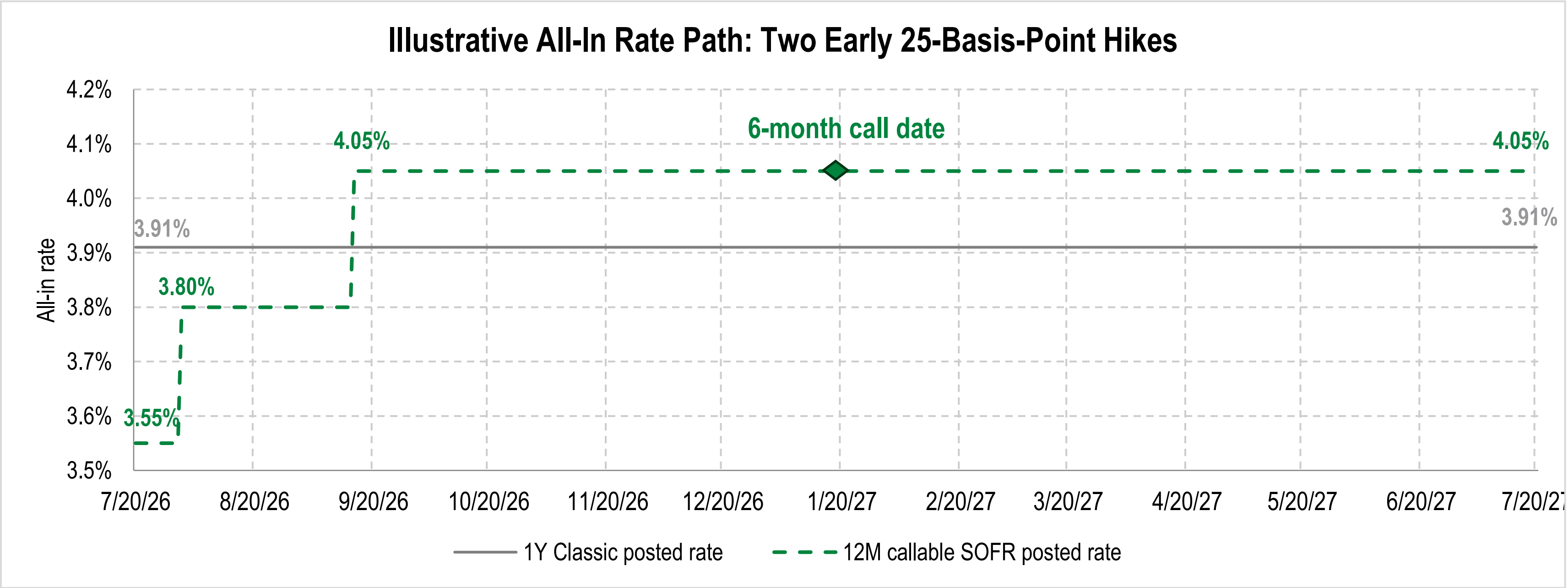
Case Study 1: If It Keeps Rolling, It Is Already Floating

A recurring short-term layer funded through DCM or repeated 1-month advances is already exposed to the future rate path.



Case Study 2: Certainty vs. a Six-Month Decision Point

A callable floating-rate advance can be compared with a fixed-rate advance by measuring starting cushion, hike risk, payment timing, and the value of a reassessment point before maturity.



Nominal cost on a $25MM 1-Year borrowing

Scenario	1-Year Classic	12M/6M (1X) Callable SOFR	Difference
No hike	$1,059.5K	$968.3K	($91.3K)
One hike at 6-Months	$1,059.5K	$999.7K	($59.8K)
Two early hikes	$1,059.5K	$1,076.4K	+$16.9K

From Rate View to Funding Structure

SOFR-indexed funding is not an all-or-nothing call; the decision should match the expected life, stability, all-in cost, and option value of the funding need.

Define the Need

- Is the funding need overnight, weekly, monthly, seasonal, or durable?

Separate Base From Volatility

- Recurring balances may support term funding
- True daily swings may belong in DCM

Compare Gross and All-In Cost

- Quoted rates matter
- Activity stock, dividend assumptions, and payment timing can change the answer

Run the Path

- SOFR cost depends on the average rate over the term
- Reset timing determines how much of the path each product lives through

Match the Structure

- DCM for volatility
- Short SOFR for near-term base
- Longer SOFR or fixed for durable needs

Thank You

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