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EHP WHITEPAPER

What the Curve Cannot Tell You

*How far the swaps curve can be trusted,
and where it becomes noise.*

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About this paper

This paper is not a forecast. We do not claim to know where the federal funds rate will end 2026, what oil will do, how Iran will resolve, or how the new Fed chair will lead. What we do claim, and what the empirical record supports, is that nobody else knows either, including the market itself. This is a methodology paper about how to read the swaps curve honestly: which part carries real signal, and which part is mood.



Executive summary

In early June 2026, markets price a 25 basis point Fed hike by year end at roughly coin-flip to two-in-three odds. FedWatch first crossed the 50% line on May 15, after the hottest inflation data of the post-war surge (April CPI at 3.8%, the highest since May 2023), and the June 5 jobs report (172,000 payrolls, roughly double consensus) pushed the priced odds higher still. Estimates of the year-end hike probability now range from the mid-40s to the high-60s percent depending on the venue and the day (CME FedWatch, Kalshi, Polymarket). The venues do not even agree with each other, which is rather the point of this paper. Fifteen weeks ago, that probability effectively did not exist. On February 24, four days before the war began, swaps priced the federal funds rate near 3.1% by end-2026, two-plus cuts from today's 3.50%–3.75% target, with further easing priced into 2027 (Bloomberg). Same instrument, opposite call, in under four months.

Today's curve peaks near 4.0% in mid-2027 and holds the 3.85%–4.00% range through 2028. The pre-war path glided toward 3% and below. That is roughly a 100 basis point swing in the multi-year view. The repricing reflects an inflation surge driven by the Iran war and a new Fed chair, Kevin Warsh, whose confirmation the market reads as deliberately hawkish.

That repricing is the entry point for this paper. The question is not whether the market is right or wrong about the hike. The question is whether the long end of the curve has ever, in its empirical record, been the kind of instrument you would underwrite a real estate hold period to. The answer is no.

What follows is a methodology paper. The curve excels at reading the market's current expectations, but those expectations are only an accurate forecast of actual policy for a few months. Past that, the historical record is striking and consistent across regimes.

"The curve is a faithful read of what the market thinks. What the market thinks is only a reliable forecast of what actually happens for about six months."

What is driving the repricing

The widely cited story in early 2025 was tariffs. The 2026 long-end story is different: the Minneapolis Fed finds the 2026 goods-price surge cannot be explained by tariffs, though tariff pass-through has not disappeared (a Federal Reserve note estimates tariffs had lifted core goods prices 3.1% through February 2026). Three forces are now stacked on top of each other:

- **The Iran war.** Brent crude rose from roughly \$72 per barrel on the eve of the war to peaks above \$120 this spring (Q1 close: \$118, the largest inflation-adjusted quarterly jump in EIA records), before sliding to the low \$90s in late May as ceasefire talks advanced. That still leaves Brent up roughly 30% from pre-war levels (EIA; CNBC). US gasoline crossed \$4 per gallon in late March 2026, the first time since August 2022 (AAA). The OECD's March 2026 Interim Economic Outlook raised its US inflation forecast for 2026 to 4.2%, from 2.8% in December, citing the war as the primary driver.
- **A new Fed chair signaling independence.** Powell's term ended May 15, 2026. The Senate confirmed Kevin Warsh 54–45 on May 13; he was sworn in May 22. A meaningful portion of the long-end repricing reflects a specific market read: Warsh, nominated by the same administration that has publicly pressured the Fed, may want to establish his independence early by holding a more hawkish posture than the inflation data alone would justify. The curve is partly pricing a personality, not just a policy reaction function.
- **Oil and downstream inflation.** Beyond gasoline, the conflict has disrupted helium (Qatar's Ras Laffan facility, roughly a third of world supply and critical to AI data centers, went offline and prices roughly doubled) along with fertilizer and other commodity flows. Core inflation projections have drifted higher: the Fed's March SEP projects 2.7% core PCE for 2026, up from 2.5% in December. Dallas Fed scenario work puts the war's baseline contribution at about 0.6 percentage points on 2026 headline PCE (WP 2609, April 2026).

If those are the drivers, can anyone really call year end?

Reading the long end of the curve as a hike call today is implicitly a forecast on five or six independent and unrelated variables. To get the year-end policy stance right, you would need confidence in all of the following at once:

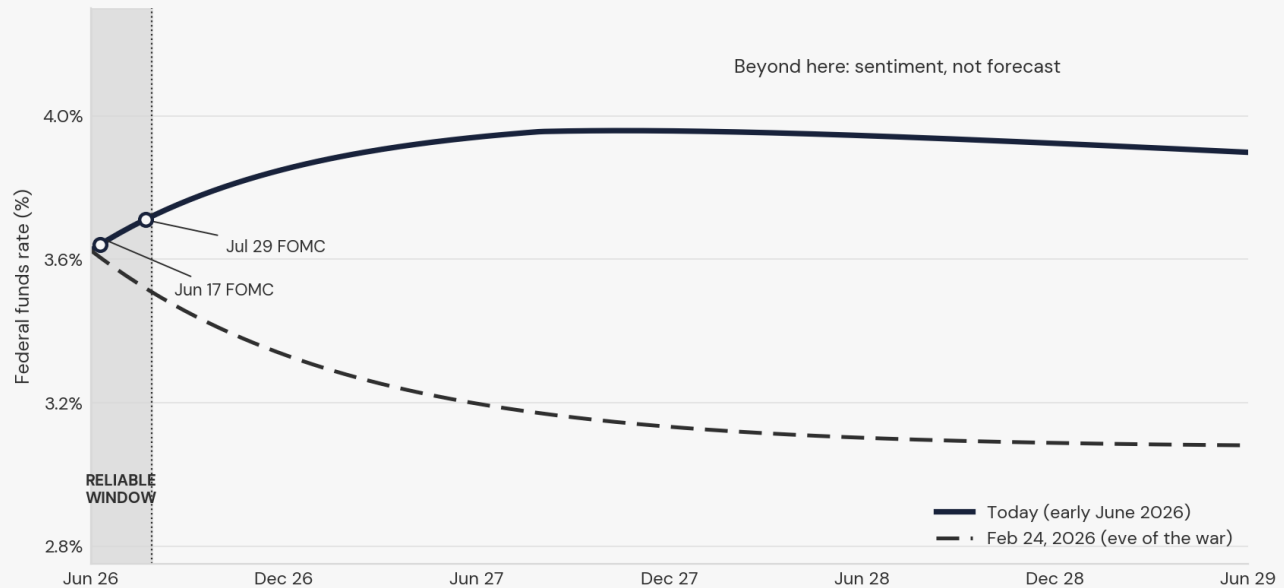
- How does the Iran war resolve, and on what timeline?
- What does Brent do over the next six months?
- Does Warsh's early independence-signaling harden into a sustained hawkish stance, or fade after his first few meetings?
- How politically insulated is the Fed actually going to be, and how does that read change between now and December?
- Does the inflation pass-through from oil prove sticky, or does it fade as supply adjusts?
- What does the labor market do alongside all of the above?

The probability of being right on year-end policy is not the simple market-implied number. It is the joint probability of being right on all of the inputs above, each independently uncertain. Stack them and the confidence interval is wide enough to drive a portfolio through.

"We do not claim to be experts on Iran, the energy market, the inflation pass-through, and the personal positioning of a new Fed chair, all at once. Neither does the market. That is the point."

THE CURVE, ILLUSTRATED

Where the curve actually matters, and how much it swings



Source: EHP illustration of overnight indexed swap pricing: the current implied path (early June 2026) versus the pre-war path (Bloomberg, Feb 24, 2026: $\approx 3.1\%$ by end-2026 with further cuts priced into 2027). Paths are stylized. The shaded reliable window covers the next two FOMC meetings.

WHAT THE FRONT END IS PRICING TODAY

FOMC meeting	Hold	Move (hike or cut)
June 17, 2026	~96%	~4%
July 29, 2026	~95%	~5%

Source: CME FedWatch, fed funds futures implied probabilities as of June 9, 2026. Both meetings are priced as near-certain holds at the current target of 3.50% to 3.75%; residual probabilities skew toward a hike following the June 5 employment report. The year-end hike probability (roughly mid-40s to high-60s percent across CME FedWatch, Kalshi, and Polymarket) sits almost entirely in the September–December meetings.

How much of the curve can you trust

Two distinct things happen as you move out the curve, and they get conflated in most commentary.

Measurement. The OIS curve cleanly reflects the market's current expectations of the federal funds rate path. Lloyd (2018) shows that one-to-twenty-four month OIS rates reliably measure expectations of future short-term rates in the US, euro area, and Japan (one to eighteen months in the UK). Past two years the rates contain persistent term premia and require model adjustment, but inside two years they are a faithful read of consensus.

Forecasting. Whether those expectations turn out to be accurate predictions of what the Fed actually does is an entirely separate question. The empirical record on this is much weaker. Gürkaynak, Sack and Swanson (2007) find fed funds futures dominate other market instruments out to roughly six months. Beyond that, errors compound and risk premia take over. We use the next two FOMC meetings as the decision-relevant threshold in our own underwriting.

"The market is consistent and measurable. It is just frequently wrong about what actually happens."

The Fed's own admission of uncertainty

Every quarter the Federal Reserve publishes its Summary of Economic Projections. Each SEP contains a fan chart of the federal funds rate, with a 70% confidence interval built from the root mean squared error of 20 years of professional and government forecasts (the methodology comes from Reifschneider and Tulip, 2017).

The Fed's own published uncertainty band is sobering. At the 2027 horizon, the 70% confidence interval for the federal funds rate is 200 basis points wide on each side of the median.

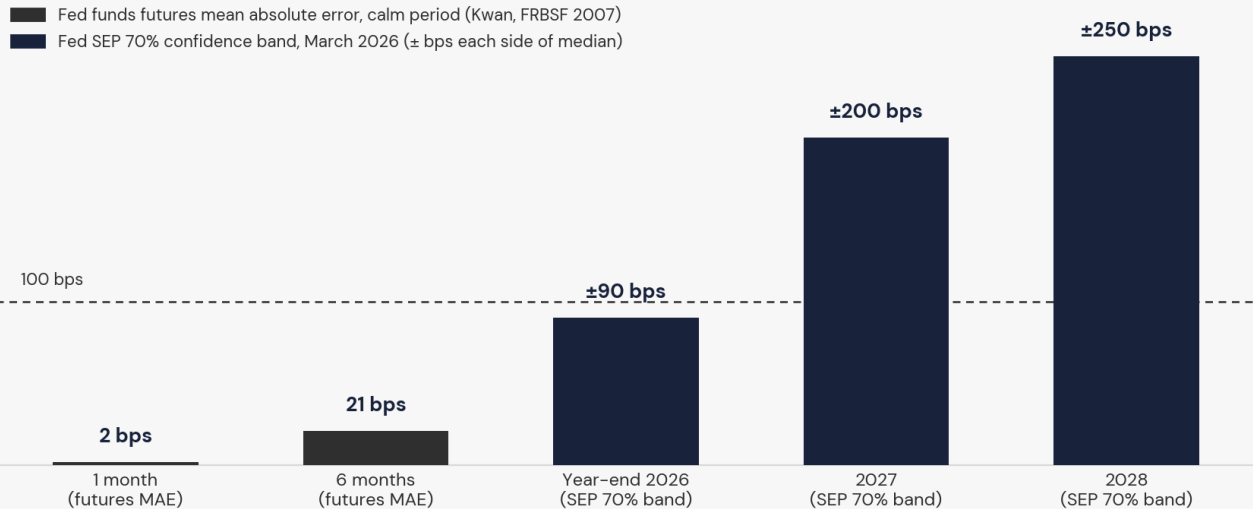
Forecast horizon	Fed's $\pm$ error range (70% confidence)
Current year (2026)	± 90 bps
~1 year out (2027)	± 200 bps
~2 years out (2028)	± 250 bps

Source: Federal Reserve Summary of Economic Projections, March 18, 2026 (Table 2, Figure 5). Bands are plus or minus the RMSE of professional and government rate forecasts over 2006 to 2025.

Applied to the Fed's March 2026 projections, with a 3.1% median for 2027, the 70% interval at 2027 spans 1.1% to 5.1%. Near-recession cuts and cycle highs sit inside the same range. Roughly 30% of the time, reality lands outside even that. The Fed itself notes (SEP Figure 5 footnote) that the interval is not a strict forecast of the dot plot, because the dots reflect appropriate policy rather than the most likely outcome, but it bounds the realistic range.

UNCERTAINTY, VISUALIZED

Forecast uncertainty grows with horizon



Two different yardsticks, one direction: mean absolute errors of fed funds futures in calm periods (Kwan, FRBSF Economic Letter 2007–15) alongside the Fed's SEP 70% confidence bands (March 2026). The units differ (realized error versus a confidence band) but both grow steeply with horizon.

How forecast error grows with horizon

The empirical record on fed funds futures and OIS forecast accuracy points in one direction: the curve is excellent at short horizons, then degrades sharply.

Inside six months, the curve is excellent. In calm periods, fed funds futures produce a mean absolute error of roughly 2 basis points at one month and 21 basis points at six months (Kwan, FRBSF Economic Letter 2007–15, June 2007).

By one to two years, the realistic range is measured in hundreds of basis points. The Fed's own 70% band reaches ± 200 basis points at the 2027 horizon. At horizons this long, rate forecasts barely improve on a naive constant-rate benchmark, a finding established for Treasury yields by Duffee (2002) and Ang and Piazzesi (2003) and extended to short-rate forecasting in subsequent work.

Errors are systematically largest at inflection points. Professional forecasters over-predict the funds rate in easing cycles and under-predict it in tightening cycles, and absolute errors scale with rate variability (NY Fed Liberty Street, August 2011). Forecasts are most accurate when rates are flat, which is when you do not need the forecast, and least accurate when rates are moving, which is when you do.

"What looks like forecast error past six months is partly something cleaner: a risk premium of roughly 3 to 5 basis points per month of horizon (Piazzesi and Swanson, JME 2008)."

That premium compounds to roughly 31 basis points at the six-month horizon on average, and it is largest exactly when uncertainty is highest, swelling well beyond its average in recessions and at turning points. By one year, the contract behaves more like a risk-adjusted asset price than an unbiased forecast. When the long end “moves 100 bps,” part of that move can be premium re-rating rather than a genuine shift in the expected policy path. Treating it as a forecast confuses the two.

The historical track record

The case against using the long end of the curve as a forecast is not theoretical. It is the consistent empirical record of the past two decades. In nearly every meaningful Fed regime change since 2007, market pricing or consensus forecasts (or both) have missed by 75 to 500-plus basis points at the six-to-twenty-four month horizon, and the misses cluster exactly at the turns.

EPISODES OF LARGE MISSES

2007 to 2008 Lehman cycle

The Fed cut from 5.25% to 0 to 0.25% over roughly fifteen months. Neither market pricing nor official forecasts anticipated the depth or speed of the easing (NY Fed Liberty Street, November 2011).

May 2013 Taper tantrum (OIS specific)

Forward OIS rates for end-2019, which embed term premium and are not a pure expectation, swung from roughly 2.5% before Bernanke's May 2013 testimony to above 4% in the months after, then back toward 2% by 2017 (Snider/Alhambra analysis of OIS forwards). Three different long-end calls for the same date. Realized end-2019 fed funds: roughly 1.55%.

2015 to 2016 Forecasted hikes that did not happen

The December 2015 dot plot implied four 25bp hikes for 2016 (median 1.375%). The Fed delivered one, a 75 basis point miss versus the dots, with market pricing missing by less. Released FOMC transcripts (Bloomberg, January 2022) show Powell and Brainard pivoted away from hikes early in 2016.

2018 to 2019 Powell pivot, wrong direction

The December 2018 SEP projected two more hikes for 2019. The Fed actually cut 75 basis points over July, September, and October 2019: wrong direction by approximately 125 basis points versus the dots (roughly 75 versus market pricing, which had already faded the hikes).

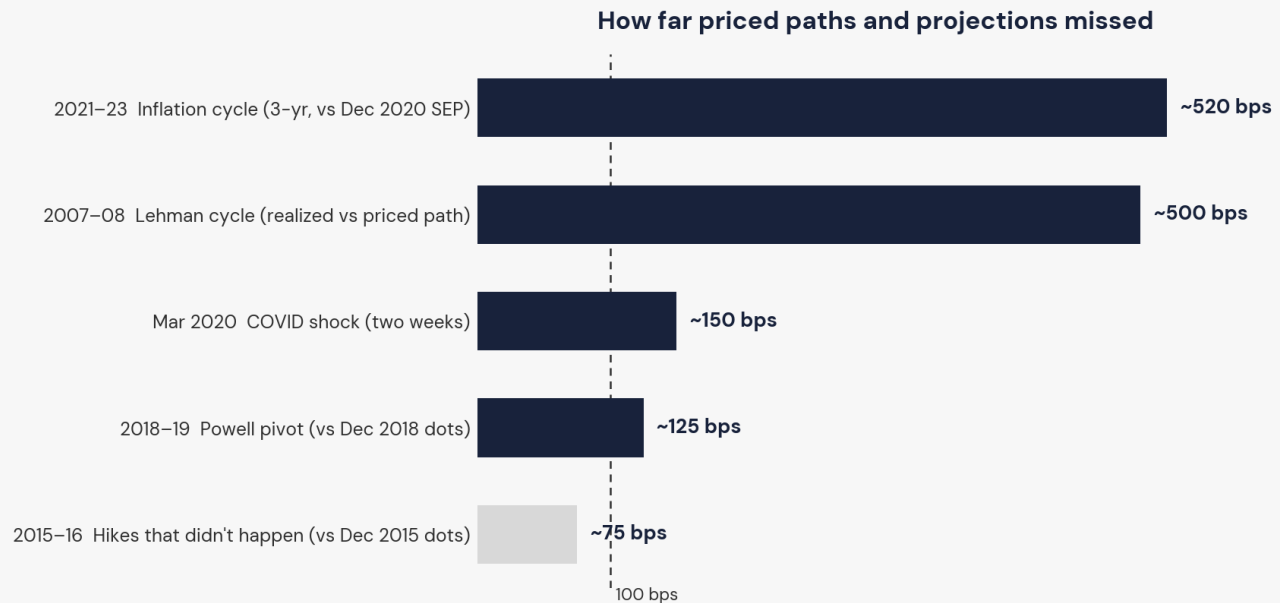
March 2020 COVID shock

The late-2019 curve and the December 2019 SEP priced approximately stable rates through 2020. In twelve days of March 2020 the Fed cut 150 basis points. Markets entirely missed the regime change.

2021 to 2023 Inflation cycle, the closest analog

Both market pricing and the December 2020 SEP saw rates near zero through 2023. Actual year-end fed funds: 0.1% (2021), 4.3% (2022), 5.3% (2023). The realized miss was roughly 420 basis points at two years and 520 at three, wider than the entire vertical range of most rate charts.

THE MISSES, VISUALIZED



Approximate magnitude of each episode's miss, versus the benchmark noted. The 2015-16 episode (75 bps, shown in gray) is the smallest of the set, and still equals three full policy moves. Sources: Federal Reserve SEP tables and statements; FRED; NY Fed; Bloomberg; Alhambra. Magnitudes are approximations for illustration.

"The dots are not a great forecaster of future rate moves. And that's not because... it's just because it's so highly uncertain. There is no great forecaster of the future. So dots to be taken with a big, big grain of salt."

Jerome Powell, FOMC press conference, June 16, 2021. The same is true of the swaps curve. The market and the Fed are reading the same uncertain future. Neither reads it well past a few months.

From thesis to underwriting

This paper is a methodology paper, not a market call. We are not arguing that the Fed will or will not hike by year end. We are arguing that the part of the curve making that claim is the part that has historically been least worth listening to. The next question is what we actually do about it.

How this shows up in our process. The first line of defense against rate uncertainty at EHP is the financing structure itself. Every loan in the portfolio is fixed-rate, sized at close so the equity return path through the hold period does not depend on where the curve sits at any point along the way. Rate risk re-enters at one well-defined point: the refinance assumption at exit. That is where we apply an explicit plus 50 to plus 75 basis point stress on the prevailing rate curve. We do not run that stress because we believe rates will rise by that amount. We run it because the historical record presented in the previous section tells us that a 50 to 75 basis point miss at the relevant horizon is not an edge case. It is closer to the median outcome of the past two decades.

What we look for: breakeven cushion. Practically, the test we apply to a deal is the gap between our underwritten refinance assumption and the rate at which the deal IRR would drop below our hurdle. We call that the breakeven cushion. A deal with thin cushion does not get approved on the strength of a benign curve. It gets approved on the strength of a margin of safety that does not depend on the curve being right.

AN ILLUSTRATION (HYPOTHETICAL)

Take a stylized value-add multifamily acquisition closing in mid-2026, financed with a five-year fixed-rate agency loan. The in-place rate is locked at close. What we stress is the rate at which the asset refinances out at the end of the hold. The prevailing OIS curve at acquisition implies a refinance assumption at exit of approximately 6.50%. Under the curve, the deal IRR clears 16%. Run the same deal under our standard +75 basis point stress (refinance assumption of 7.25%) and the IRR falls to roughly 14%, still above our 13% hurdle. The breakeven, where IRR meets hurdle, sits at approximately 7.85%, about 135 basis points above the curve. That gap is the breakeven cushion. A deal with less than roughly 100 basis points of cushion does not get approved on the strength of the curve. All figures are hypothetical and for illustration only; targets are forward-looking estimates and not guarantees.

"We do not stress test because we expect a hike. We stress test because the record says a 50 to 75 basis point miss is closer to the median outcome than the tail."

This is not a moment to be pencils down

There is a final point in this discipline that matters more than the stress test itself. A curve repricing of roughly 100 basis points in under four months is not, on its own, a reason to step back from acquisitions. If anything, it is closer to the opposite signal.

Long-end volatility of this magnitude is historically the environment in which other capital pauses. Underwriters who depend on the curve being right cannot pencil deals. Transaction volume thins. Sellers who need liquidity transact at prices that reflect that thinness. None of this is a prediction about where rates go. It is an observation about how capital behaves when rate uncertainty spikes, and the observation is durable across cycles.

Our position is therefore not to wait. The same methodology that tells us the long end of the curve is noise also tells us that paralysis based on the long end is paralysis based on noise. We continue to underwrite, with the discipline described above. Environments like this one are typically where that discipline earns its return.

Summary

- Read the front end of the curve (next one to two FOMC meetings) as a real signal. Today, that signal is hold.
- Treat anything past a year as a directional mood reading, not a number to underwrite to. Today's year-end hike, priced anywhere from a coin flip to two-in-three odds depending on the venue, is a year-end call, outside the empirically reliable window.
- The in-place financing structure (fixed-rate, sized at close) is the first protection. The plus 50 to plus 75 basis point stress is applied to the refinance assumption at exit. Look for breakeven cushion at that point, not curve confirmation.
- Do not confuse curve uncertainty with reasons to pause. Long-end volatility of this magnitude is historically the environment in which opportunistic acquisitions get made, not the environment in which they are deferred.

If this resonates

If you would like to discuss how this framework has applied to a recent EHP acquisition, or how we currently scenario-test our refinance windows in the pipeline, reach out at info@ehpcapital.com or +1 (786) 540-0660. We are always happy to walk LPs through the underwriting work behind a deal.

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