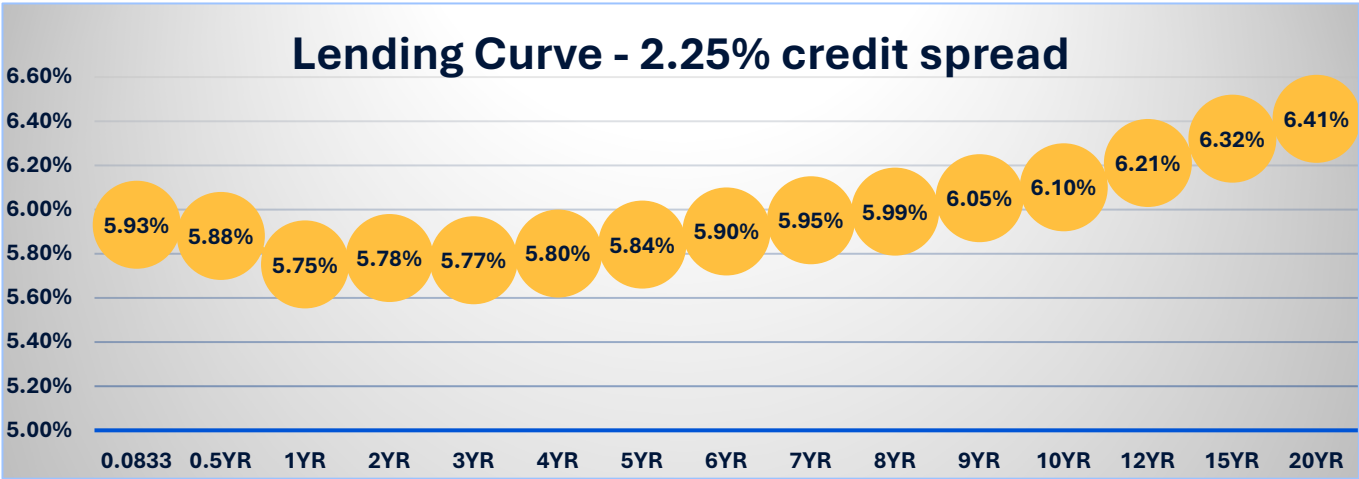


Three Pertinent Observations for Lenders and Borrowers

1. Borrowers Are Facing a Flat Lending Curve Out to 7 Years

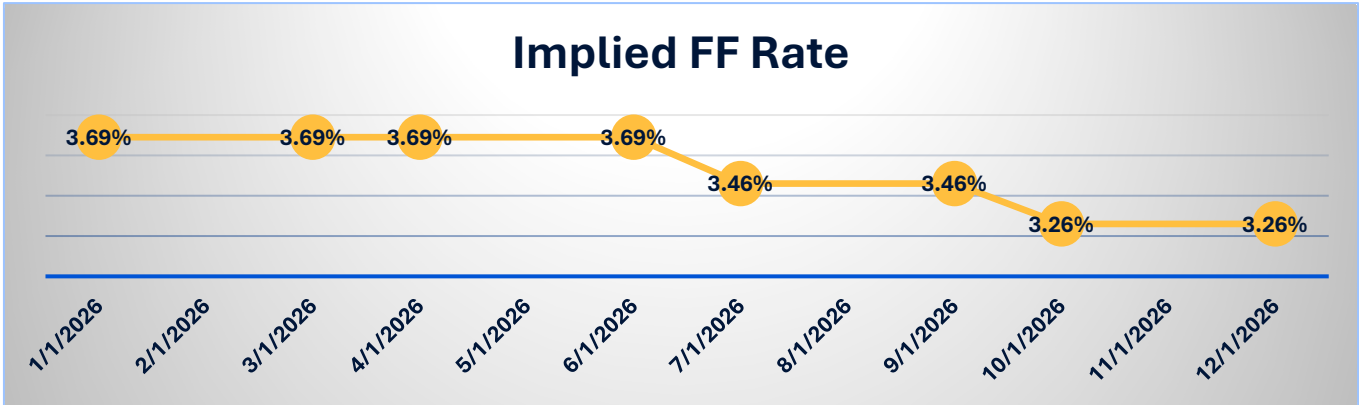
As of this publication, the borrowing rate for A- and B-rated credits (approximately S+2.25%) is shown in the chart below. The difference in all-in coupon between floating-rate loans and 7-year fixed-rate loans is currently negligible.

This environment creates a compelling opportunity for borrowers seeking to eliminate interest-rate volatility. For effectively the same cost, borrowers can lock in a 7-year (or even 10-year) fixed-rate loan and secure long-term financing certainty—an uncommon advantage in most rate cycles.



2. What Happens If POTUS Pressures the Fed to Cut Rates?

Market pricing currently reflects expectations for modest rate cuts—roughly two cuts anticipated in 2026. These expectations are already embedded in the flat lending curve.





However, borrowers should consider a second, less intuitive narrative:

- Since September 2024, the Fed has lowered short-term rates, yet long-term rates have risen.
- The Federal Reserve remains divided, consistent with a likely policy pause in 2026, given persistent inflation and late cycle uncertainty.
- Leadership changes and political scrutiny have raised the bar for future cuts, as threats to Fed independence historically result in higher, not lower, long-term rates.
- The Fed's own dot plot signals only one additional cut in 2026.
- Cutting rates when inflation is above target risks accelerating inflation, which could force policymakers into a hard reversal—potentially pushing long term rates higher.

3. The Borrower's Dilemma

Attempting to time interest rates is inherently speculative—yet human nature tempts us to try. Borrowers are better served by grounding decisions in business fundamentals rather than rate predictions (including ours).

Key questions borrowers should prioritize:

1. **Hold Period:** What is the expected ownership or investment horizon? Financing maturity should broadly match the hold objective.
2. **Rate Sensitivity:** How exposed is NOI or EBITDA to interest-rate movements? If cash flows are not rate-sensitive, fixed-rate financing typically offers superior risk-adjusted value.
3. **Financing Friction Costs:** Consider all-in entry and exit costs—appraisals, legal fees, prepayment penalties, make whole provisions, refinancing flexibility with the same lender, and collateral substitution options.
4. **Portfolio Strategy:** Borrowers with multiple credit facilities should approach their financing decisions like asset managers, structuring their debt strategically to improve flexibility and reduce long-term costs. This includes laddering maturities across different points on the yield curve, diversifying collateral structures, leveraging individual institutions' lending preferences, and maximizing optionality for future refinancing or loan assumptions

Borrowers can meaningfully reduce long-term financing costs by focusing on factors they can predict—business cash flows, hold periods, operational needs—rather than playing the rate-forecasting game.

The ARC Team can help you evaluate the optimal financing structure for your client's specific profile. Reach out to discuss tailored strategies that balance rate risk, business needs, and long-term financial flexibility.