FLORIDA PRIME

Weekly Commentary

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New week, same story: Short credit rates held at low levels and Treasury bills continue their move down last week as Federal Reserve policymakers stuck to their easy-money guns and events overseas reinforced the risk-averse trade. Four-week T-bills dipped another basis point to 0.06%, 13-week bills fell 2 basis points to 0.09% and 26-week bills dropped 2 basis points to 0.135%.

The move down on the T-bill front wasn't solely driven by the Treasury securities' haven status; the continued run-off of supply as the Treasury's Supplemental Financing Program winds down also has played a role. There is about $25 billion left in the $200 billion program, though it is though it will be renewed if, as expected, a debt-ceiling deal is worked out in the next few weeks. The drop in T-bill rates—four-week bills were trading above 0.15% in early February before this latest downdraft—also has carried over to repo rates, which have dipped back down into the single digits.

The irony is that economic fundamentals would suggest that we should be headed toward a rising-rate environment, with reports continuing to point to an improving economy and sniffs of higher headline inflation. Philadelphia's manufacturing index for March jumped to its highest level since 1984; the OECD composite leading indicator for the U.S. climbed a 60th straight month in January to its highest since September 2007; the Conference Board's leading indicators snapped back from January's lull, rising 0.8% in February; and the 4-week moving average of jobless claims came in below 400,000 for the third time in four weeks. Even the Fed acknowledged an improving economy last week while still holding to policy language in support of a target funds rate at unprecedented lows for an extended period and to completion of QE2. It's about halfway through its commitment to buy $600 billion of intermediate- to longer-term Treasury security purchases by the end of June.

But the Japanese quake and tsunami, the turmoil in the Middle East and the ongoing sovereign-debt saga in Europe continue to weigh on the markets and the risk-averse trade. So for now, international events appear to be muscling out economic fundamentals in the money markets. We still expect that will change this year, but until we see clear signs of such, we're moved out average maturities a bit to capture slightly more yield.

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Views are as of March 21, 2011, and are subject to change based on market conditions and other factors.