FLORIDA PRIME

Weekly Commentary

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Short rates continued to hover at low levels as spiking energy and commodities prices—West Texas Intermediate crude briefly topped $100 a barrel last week and retail gasoline prices neared a 2½-year high–have so far failed to percolate through to most key core inflation measures in any significant way. In fact, six-month and one-year London interbank offered rates (Libor) actually dipped a basis point each last week to 0.46% and 0.79%, respectively. The question, of course, is whether these highly visible non-core price increases will carry over to consumers' inflation expectations, which – while not as much as prices themselves—can actually impact inflation.

If inflationary expectations were a concern, they weren't yet showing up in the latest readings of consumer confidence. Both the Conference Board and University of Michigan gauges for February jumped to 3-year highs last week, led by notable improvements in labor-market conditions and expectations about the future—the Conference board's expectations component was its highest since December 2006. On the jobs front, initial jobless claims fell to 391,000 for the week ending February 19, dropping the 4-week moving average to a 3-½ year low of 402,000. Claims have come in below 400,000 in three of the four latest reporting weeks, indicating jobs are starting to pick up. We'll get a better handle on the situation this Friday, when the government releases its employment situation for February. Also last week, durable goods orders rose a robust 2.7% in January after declining in December, but the headline betrayed weakness in this volatile metric—ex-transportation, orders actually fell 3.6% in January after rising a respective 3% and 4.6% the prior two months.

On the downside, 2010's fourth-quarter GDP was revised downward to 2.8% from an initially estimated 3.2% increase. The revision was driven by sharp downward revisions in spending, some on the consumer side (consumer spending still rose a healthy 4.1% clip) but primarily on the state and local government side as states and localities dealt with gaping budget holes and the prospect of future deficits. Housing had a mixed week as existing home sales unexpectedly rose in January while new home sales fell more than expected. Home prices remain under pressure because of relatively high levels of inventory and the number of distressed sales—nearly 4 in every 10 existing-home sales in January were distressed properties, a 12-month high. About the best that can be said for housing at this point is that it may be stabilizing at extremely low levels.

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Views are as of February 28, 2011, and are subject to change based on market conditions and other factors.