FLORIDA PRIME

Weekly Commentary

MARCH 18, 2013

Paige Wilhelm
Senior Vice President
Senior Portfolio Manager
Federated Investment Counseling

It was a quiet week in the money market world. London interbank offered rates (Libor) were basically unchanged for the week, with three-month steady at 0.28%, six-month down less than a basis point to 0.44%, and one-year steady at 0.73%. Short-term Treasuries were down slightly, with one-month down two basis points to 0.07%, three-month down one basis point to 0.09%, six-month steady at 0.11%, and one-year down a basis point to 0.14%. Repo rates were volatile for the week, and hovered in the single digits.

Despite public reluctance on the part of a minority of members to continue expanding the Federal Reserve's (the Fed) balance sheet at the current pace of $85 billion a month, this week's Federal Open Market Committee meeting is unlikely to produce any policy shifts. Fed Chairman Ben Bernanke has a firm hold on the doves who represent the majority of the policy-setting committee's voting members, and his recent testimony before Congress made clear he sees no need to put on the brakes anytime soon. Fed funds futures contracts seem to agree, suggesting the benchmark rate will remain effectively at zero until 2015. About the only potential difference coming out of this week's meeting might be a moderate upgrade in the quarterly economic projections accompanying the meeting—not enough to merit any policy changes, but enough to reflect improvements in housing, business investment and employment since its last forecast.

A series of recent reports indicated some strengthening on the economic front, despite higher taxes and gasoline prices that arrived with the New Year. Auto sales are picking up, homebuilding and manufacturing are accelerating, retail sales and consumer sentiment are rising, and the labor market is firming. February's 236,000 increase in payroll jobs was well above consensus, and the latest reports on initial unemployment insurance claims indicate employment's momentum has carried over into March. Inflation rates have started to move, but not so much that the Fed might notice. Import and export prices, as well as headline consumer price index (CPI) and producer price index (PPI), rose above expectations in February on spiking energy costs. CPI's 0.7% month-over-month increase was its fastest since June 2009. Core prices remained relatively moderate, although at 2%, core CPI now stands right at the Fed's target rate, and below the 2.5% trigger the Fed has set for beginning to ease off the throttle. The initial implementation of the sequester out of Washington doesn't seem to have slowed the economy, but it could take several months before the cuts start to bite and generate potential multiplier effects. If sequestration remains unchecked, it's estimated it will represent a monthly drag of 50,000 to 75,000 on full-time equivalent payrolls.

G40461-19 (03/13)