FLORIDA PRIME

Weekly Commentary

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Cash rates remained at very low levels last week as the market wrestled with humdrum economic data that suggested an expected second-half pickup isn't here yet. Rates on overnight Treasury and MBS repos slipped a point each to 5 and 6 basis points, respectively, while London interbank offered rates (Libor) held steady, with only one-year Libor bumping up a notch to 0.67%. Four-week and 13-week Treasury bills also rose ever so slightly—1 and 1½ basis points, respectively—to 0.055% each.

The issue continues to be what will Fed policymakers do and when will they do it. Market expectations appear to continue to favor some sort of initial September pullback of the central bank's $85 billion in monthly purchases of longer-term Treasury and agency securities (so-called quantitative easing or QE). But the size of the initial tapering remains in debate, as does the longevity of QE before it ends entirely.

The conundrum for policymakers is whether the economy's ballasts are supportive enough for growth to continue to improve without the tonic of extraordinary monetary accommodation. On that front, the news of the past week was mixed. July industrial production was unchanged versus expectations for an increase, with June also revised down. Moreover, the initial reads on August manufacturing as provided by the New York and Philadelphia Feds' monthly reports also reflected unexpected slowing, while the University of Michigan's initial take on consumer sentiment slipped to its lowest level since April—all indicative of a subpar recovery and still-cautious consumer. On the other hand, July housing starts jumped albeit entirely in the multifamily arena; homebuilder sentiment increased to its highest level since 2005; the latest weekly jobless claims fell to nearly a six-year low; and CPI ticked closer to the Fed's target—all in line with a "data-dependent" Fed's guideposts for beginning to end QE.

On the whole, the week's data was enough to keep pushing up long Treasury yields on the likelihood tapering will start in September. An easing of QE should benefit short rates as well as more supply comes into the market, even as the Fed seems entrenched on holding the target funds rate at historic lows through 2014. But as we said, the questions for just how big an impact any QE moves may have remain: When and by how much?

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Views are as of August 19, 2013, and are subject to change based on market conditions and other factors.