FLORIDA PRIME

Weekly Commentary

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Cash rates ticked up but remained at low levels last week, with overnight Treasury and mortgage-backed repos closing at 4 and 6 basis points, respectively, up from 2 and 4 the previous week, on month-end pressures and bill settlements. Repo rates are expected to remain in the low-to-mid single digits for much of September on lower bill supply. Credit rates also held at low levels last week, with one-month, three-month and six-month London interbank offered rates (Libor) unchanged and one-year Libor up a point to 0.68%.

A disappointing report on August jobs marred what otherwise had been a relatively solid week on the economic news front, as both the ISM Manufacturing and Nonmanufacturing gauges surprised in August, hitting two- and eight-year highs, respectively; domestic auto sales jumped 12.8% to a pre-recession seasonally adjusted annual run rate of 16 million; and weekly jobless claims fell to a better-than-expected 320,000. All of this set up hopes for the jobs report, which unfortunately laid an egg. Nonfarm payrolls rose only 169,000 versus expectations for an increase of 180,000, but the bigger downers were downward revisions trimming 74,000 jobs off the previous months' gains and a decline in the labor force participation rate to 62.3%, its lowest level since 1978.

What does this all mean for tapering QE3 when the Fed policymakers meet next week? We still expect the policy-setting Federal Open Market Committee (FOMC) to unveil plans to initiate reductions in the $85 billion of monthly Treasury and agency purchases, with the cutbacks getting underway later this month or in October. Policymakers may taper the magnitude of monthly tapering to around $10 billion to start, but with a press conference with Chairman Ben Bernanke scheduled afterward, it's likely they would prefer to get the ball rolling and allow Bernanke to more fully explain their thinking. Otherwise, if the FOMC were to wait but still hew to its goal of ending quantitative easing by next June, much larger monthly reductions may be necessary later this year, potentially rattling the markets and marking an inauspicious end to Bernanke's chairmanship, which is set to expire in January. Given Bernanke's stewardship through the global financial crisis, it's difficult to envision the FOMC taking such a course.

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Views are as of September 9, 2013, and are subject to change based on market conditions and other factors.