FLORIDA PRIME

Weekly Commentary

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The down-to-the-wire debt-ceiling showdown sent one-month Treasury bill yields soaring last week as investors sought to avoid the securities for fear of being caught holding them in case of a government default. Yields on one-month T-bills ended the week at 0.35%, nearly triple the prior week's level and up from under 0.02% just two weeks ago. Yields on overnight Treasury and agency mortgage repo rates also jumped during the past week from the mid-single digits to the high teens. The action was more subdued on the longer end of the government cash curve, with yields on 13-week and 26-week bills up 2½ and 2 basis points, respectively, to 0.035% and 0.06%. And in the credit markets, short-term rates held at low levels.

The past week's activity in the Treasury market reflected nervousness over whether Congress and the White House could strike a compromise on a budget deal in time to avoid a default. Treasury Secretary Jack Lew has said the U.S. will have exhausted its borrowing authority as of October 17, and the market fears that even if the default is short-lived, it could significantly disrupt the short-term government credit markets, cause longer-term damage to the country's reputation and prompt the Fed to put off any tapering of its $85 billion in monthly bond purchases until 2014.

Because of the ongoing government shutdown, there wasn't a lot of economic data released last week. Perhaps most notable were the minutes from the September 17-18 Federal Open Market Committee (FOMC) meeting, at which policymakers unexpectedly delayed the start of slowing the aforementioned quantitative easing. The minutes characterized the no-tapering decision as a close call, consistent with the idea that policymakers exited with the idea that the FOMC would likely taper later this year and end purchases around mid-2014. But as noted, the subsequent government shutdown/debt-ceiling showdown throws a wrinkle into this scenario.

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