



Fed Keeps 'Extended Period' Pledge, Sees Rebound (Update1)

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By Craig Torres



Dec. 16 (Bloomberg) -- The Federal Reserve repeated its pledge to keep interest rates "exceptionally low" for "an extended period" and said the economy is strengthening.

"Household spending appears to be expanding at a moderate rate, though it remains constrained by a weak labor market, modest income growth, lower housing wealth, and tight credit," the Federal Open Market Committee said in a statement today after meeting in Washington. "Businesses are still cutting back on fixed investment" and "remain reluctant to add to payrolls." Deterioration in the labor market is "abating."

Chairman Ben S. Bernanke, who faces a confirmation vote for a second term by the Senate Banking Committee tomorrow, is battling what he calls "significant **headwinds**" of declining **credit** and continuing job losses. While the economy has returned to growth after the deepest **recession** since the 1930s, most economists surveyed by Bloomberg News predict the **unemployment rate** will exceed 10 percent through June. Consumer spending is still below its level of two years ago.

Officials kept their benchmark overnight **lending rate** between banks in a range of zero to 0.25 percent, where it has been for a year. Policy makers restated that low interest rates are contingent on "low rates of resource utilization, subdued inflation trends, and stable **inflation expectations**."

"Inflation will remain subdued for some time," the statement said. The consumer price index, minus food and energy, rose 1.7 percent for the 12 months ending November, unchanged from October, the Labor Department reported today.

The dollar was little changed against the euro after the decision, while stocks pared gains. Treasury notes advanced.

Agency Purchases, Liquidity

The Fed said it will continue **purchases** of agency mortgage- backed securities totaling \$1.25 trillion and about \$175 billion of agency debt through the first quarter of next year. The FOMC and the Fed's Board of Governors reiterated that "most of the Federal Reserve's special liquidity facilities will expire on Feb. 1 2010." The Fed also said it's working with other central banks to close temporary liquidity swap arrangements by Feb. 1.

"The Federal Reserve expects that amounts provided under the Term Auction Facility will continue to be scaled back in early 2010," the statement said.

The decision was unanimous.

The FOMC met after a week of reports suggesting economic growth picked up in the fourth quarter. **Retail sales** climbed 1.3 percent in November, twice as much as anticipated in a Bloomberg News survey of economists. **Inventories** rose in October for the first time since August 2008, and exports in the same month increased to the highest levels in 11 months.

Forecasts Raised

The numbers led economists at Goldman Sachs Group Inc. and JPMorgan Chase & Co. to raise their forecasts for fourth quarter growth by a full percentage point. JPMorgan lifted its estimate to a 4.5 percent annual growth rate in the final three months of 2009, compared with a previous prediction of 3.5 percent. Goldman economists increased their estimate to 4 percent from 3 percent. Gross domestic product grew 2.8 percent in the third quarter after shrinking for each of the previous four quarters.

"There is more of a self-sustaining dynamic developing," Julia Coronado, senior U.S. economist at BNP Paribas SA in New York, said before the announcement. "We are still in a very deep hole."

Previous Recessions

Consumer spending, which fell the most since 1980 during the recession, rose to \$9.25 trillion on an annual basis in the third quarter. Purchases were still below the pre-recession peak of \$9.36 trillion in the fourth quarter of 2007.

By contrast, consumption grew every quarter of the March to November 2001 recession. In the 1990 slump, which began in the third quarter of that year, consumption surpassed the pre-recession peak in the third quarter of 1991. The downturn ended in the first quarter of that year.

Each of the last three recessions has seen a slow recovery in employment, though the jobless rate is higher now than at the end of the previous two slumps. While the economy grew in July to September, unemployment jumped to 10.2 percent in October and was 10 percent in November. The rate continued to rise past the November 2001 trough in economic activity, peaking at 6.3 percent in June of 2003. The prior recession ended in March of 1991, and unemployment continued to rise until peaking in June 1992 at 7.8 percent.

GE, Caterpillar

General Electric Co. is ready to go "back on offense" next year after slimming its portfolio and maneuvering through the worst of the finance arm's challenges, Chief Executive Officer Jeffrey Immelt said during his annual investor meeting in New York yesterday. Caterpillar Inc., the world's largest maker of bulldozers and excavators, aims to bring back some laid-off workers next year as sales improve, Chief Executive Officer Jim Owens said in a Bloomberg TV interview on Dec. 11. The company cut about 18,700 full-time jobs since Dec. 2008 as the global recession eroded demand.

The economic reports are "unlikely to materially affect the committee's outlook for next year," Laurence Meyer, a former Fed governor and vice chairman of Macroeconomic Advisers LLC said before the decision. They "may give the committee more confidence in its expectation that a sustainable recovery is underway."

Fed officials said last month the economy will grow 2.5 to 3.5 percent next year, fast enough to bring the unemployment rate down only to 9.3 to 9.7 percent in the fourth quarter, according to their central tendency estimates.

Production Gain

Factories in the U.S. made more goods in November than anticipated, extending a rebound in manufacturing that will give the world's largest economy a lift into 2010. Production in November was still below the average level of the past two years.

The 56-year-old Fed chairman has focused on restoring liquidity and credit in the U.S. financial system, expanding the central bank's **balance sheet** to \$2.18 trillion in the process.

Stocks have rallied as low interest rates have caused investors to seek higher returns. The **Standard and Poor's** 500 Index is up about 23 percent this year. The Fed's mortgage purchases helped push rates on a 30-year fixed-rate loan to 4.71 in the week ending Dec. 3, the lowest since mortgage buyer **Freddie Mac** of McLean, Virginia began keeping records in 1971.

Stiglitz, Phelps

Nobel prize-winning economists Edmund Phelps and Joseph Stiglitz of Columbia University in New York both warned last week that growth is at risk if businesses don't start adding more jobs. Pitney Bowes Inc., the Stamford, Connecticut maker of office automation equipment and software, said Dec. 15 it expects to cut 10 percent of jobs in a reduction program that will continue into 2010.

"The fact that the stock market is up or that credit markets are less frozen should not distract us from the problems ahead," Stiglitz told the Joint Economic Committee of Congress on Dec. 10. "These problems are

especially grave in the labor market.”

While the unemployment rate dropped two tenths of 1 percent in November, the duration of unemployment reached another high, and weekly wages “are essentially stagnating,” Stiglitz said.

The Fed is unlikely to change interest rates until the third quarter of 2010, according to the median projection of 62 economists surveyed by Bloomberg News in the first week of December.

“The Fed is looking at a variety of indicators beyond some normalization in the pace of economic growth,” Dan Greenhaus, chief economic strategist at Miller Tabak & Co. in New York, said before the statement. “You need strong growth to drive employment, and you need strong employment to drive spending.”

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