Fed Keeps Purchase Targets Unchanged, Sees Stability (Update2)

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By Scott Lanman and Craig Torres

April 29 (Bloomberg) -- The Federal Reserve refrained from increasing purchases of Treasuries and mortgage securities, signaling the worst of the recession may be over.

"The economy has continued to contract, though the pace of contraction appears to be somewhat slower," the Fed's Open Market Committee said in a statement after a two-day meeting in Washington. "Household spending has shown signs of stabilizing, but remains constrained by ongoing job losses, lower housing wealth and tight credit."

Chairman **Ben S. Bernanke** is watching for signs of a slowing contraction as the Fed's loans and bond purchases reduce the cost of credit for households and businesses. Consumer spending rebounded in the first quarter, while the slump in housing and inventories pushed the economy to its worst performance in five decades, the Commerce Department reported earlier today.

"The committee will continue to evaluate the timing and overall amounts of its purchases of securities in light of the evolving economic outlook and conditions in financial markets," the Fed statement said.

Bonds fell after the Fed failed to commit to increase its buying of long-term Treasuries. The yield on the benchmark 10- year note jumped to 3.11 percent at 2:22 p.m. in New York, from 3.02 percent late yesterday. The Standard & Poor's 500 Index remained higher at 875.11, a gain of 2.4 percent from yesterday.

Funds Rate Steady

The FOMC kept the **federal funds rate** target at a range of zero to 0.25 percent for the third straight meeting and repeated its intentions to keep the target rate low.

Today's decision was unanimous. At the **previous** FOMC meeting in March, policy makers agreed to buy $300 billion of long-term Treasury debt within six months while increasing purchases of mortgage-backed securities to $1.25 trillion this year from $500 billion and doubling purchases of housing-agency debt to $200 billion.

The Fed panel said the economy "is likely to remain weak for a time," and officials expect "a gradual resumption of sustainable growth in a context of price stability."

Former Fed Chairman **Paul Volcker** said the U.S. economy is "leveling off at a low level" and doesn't need a second fiscal stimulus package.

Still, the economy is functioning only by "the grace of government intervention" and "we're in for a long slog" before a recovery takes hold, Volcker said on Bloomberg Television's "Conversations with **Judy Woodruff**" airing this weekend. He is head of President **Barack Obama**'s Economic Recovery Advisory Board.

Fed Strategy

The Fed's strategy appears to be easing credit for banks, corporations and households. The three-month London interbank offered rate, or **Libor**, for dollars fell to 1.03 percent today, the lowest level since June 2003, the British Bankers' Association said. The **TED spread**, the difference between what the Treasury and banks pay to borrow dollars for three months, has narrowed to 0.91 percentage point, from as high as 4.64 percentage points on Oct. 10.

Companies have raised a record $468 billion in U.S. bond sales this year. The average cost of a 30-year fixed-rate **mortgage** fell to 4.80 percent last week, down from 6.03 percent a year ago, according to data from

Freddie Mac.

The Fed released its decision hours after the government reported the U.S. economy contracted at a 6.1 percent annual pace in the first quarter, reflecting declines in housing and a record slump in inventories. The economy contracted at a 6.3 percent annual rate in the last three months of 2008.

'Green Shoots'

Bernanke said in an interview with CBS's "60 Minutes" program that aired March 15 that the Fed's efforts so far had brought down mortgage rates, among evidence of "green shoots" in some markets.

A month later, the Fed chief gave a speech saying there were signs that the "sharp decline" in the economy was slowing, indicating a potential "first step" toward a recovery. His outlook is partly supported today by a 2.2 percent gain in consumer spending in the first quarter, the most in two years. Consumer spending accounts for 70 percent of the economy.

Officials cut the benchmark lending rate to as low as zero in December and switched to using direct bond purchases and loans to support credit markets.

"The Fed is following an extraordinarily expansionary policy," **William Poole**, a senior fellow at the Cato Institute in Washington and former president of the St. Louis Fed, said before policy makers issued their statement. "There is I think accumulating evidence that we may not be all that far from a bottom" of the contraction. Poole spoke in an interview with Bloomberg Radio.

Full Details

The public won't get full details on whether Fed officials adjusted their outlooks until May 20, when the central bank releases minutes of this week's meeting. That report will include a new round of quarterly economic projections of growth, inflation and unemployment from the Fed's five governors and 12 district-bank presidents on the FOMC.

Policy makers have lowered their projections for 2009 gross domestic product several times, forecasting in January an average range of contraction of 1.3 percent to 0.5 percent. A year ago, officials foresaw growth this year ranging from 2.1 percent to 2.7 percent.

The **recession** that began in December 2007, triggered by the housing collapse and credit crisis, has wiped out 5.1 million jobs from the U.S. economy, pushing the **unemployment** rate to a quarter-century high of 8.5 percent.

'Dead Leaves'

"There's been lots of talk about 'green shoots,'" **Robert Eisenbeis**, a former Atlanta Fed research director who is now chief monetary economist for Vineland, New Jersey-based Cumberland Advisors, said before today's meeting concluded. "You can find a lot of dead leaves too."

Even so, economists expect the annual pace of the contraction to slow in the second quarter to about 2 percent, the median estimate in a Bloomberg News survey. That should pick up to a 0.4 percent annual growth rate in the third quarter, according to the same survey, conducted March 30 to April 8.

Reports last week showed that orders for U.S. **durable goods** in March fell less than forecast and sales of **new houses** were higher than projected.

Separately, about 140 Fed staff members are coordinating capital tests on the 19 largest banks to assure they can continue to lend if the economy worsens. Results of the exams are scheduled for release the week of May 4. Bernanke said in an April 14 speech in Atlanta that the U.S. "will not have a sustainable recovery" without a stabilization of the financial system and credit markets.

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Last Updated: April 29, 2009 15:07 EDT