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INTEREST RATES

Fed expected to hold steady

Figures pointing to a cooling U.S. economy are expected to deter the Federal Reserve from raising interest rates today.

By Kevin G. Hall

McClatchy News Service

WASHINGTON - The Federal Reserve is expected to leave interest rates unchanged today for a second-straight month, and many analysts now think there won't be any more rate increases this year.

If true, that's good news for consumers, since the Fed's increases in the benchmark federal funds rate, an overnight rate that banks charge each other, influence a broad array of bank loans to consumers and businesses.

Falling oil and gasoline prices, along with a steeper-than-expected drop in new housing starts, are combining to reduce inflationary pressures that push up prices throughout the economy. The Fed's main job is to keep inflation in check. It now appears that the Fed's pause last month, which left the fed-funds rate at 5.25 percent after 17 consecutive quarter-point rate raises, may have ended the credit-tightening cycle that began in June 2004.

"I think we've probably seen the peak in terms of the Fed tightening. I think the economy will be soft enough for the second half of the year that over time it will help curb inflationary pressures," said Martin Regalia, chief economist of the U.S. Chamber of Commerce and former Fed staffer.

When the Fed paused on Aug. 8, it issued a statement indicating that monetary policymakers believed the slowing U.S. economy would remove enough inflationary pressures to make another rate increase essentially overkill. The Fed said it wanted time to gauge the effects of its previous rate hikes, which take time to affect the economy.

Two months ago, crude oil cost more than $70 a barrel, and other raw materials were in hot demand globally and therefore were pricey. These trends drove up inflation, or the general rise of prices across the economy.

But in recent weeks, prices for oil, gas and many commodities have fallen sharply. And on Tuesday, the Commerce Department reported that housing starts dropped 6 percent in August to an annualized rate of 1.665 million.

That's the lowest rate in more than three years and a steeper plunge than most economists expected. Since housing drives much of U.S. economic activity, the slump points to a slowing economy. While a hot economy fans inflation, a slowing one douses it, reducing pressure on the Fed to raise rates.

"My view is we're done, and we'll have enough slowness brought on by the housing market and related consumer spending that they are probably cutting rates by the first quarter of next year," said Keith Hembre, the chief economist for First American Funds in Minneapolis.

It all depends, however, on whether energy prices spike up again and whether consumer and producer prices continue their downward trend. Both have been at the high end of the Fed's perceived tolerance zone.