Economic Research Department

BBVA

U.S.

Fed Watch

March18th, 2009

Fed kept its target rate unaltered and intensifies quantitative easing

- **The economic outlook worsened**
- **Fed significantly increased the size of its balance sheet**
- **Similar measures are likely in the near future**

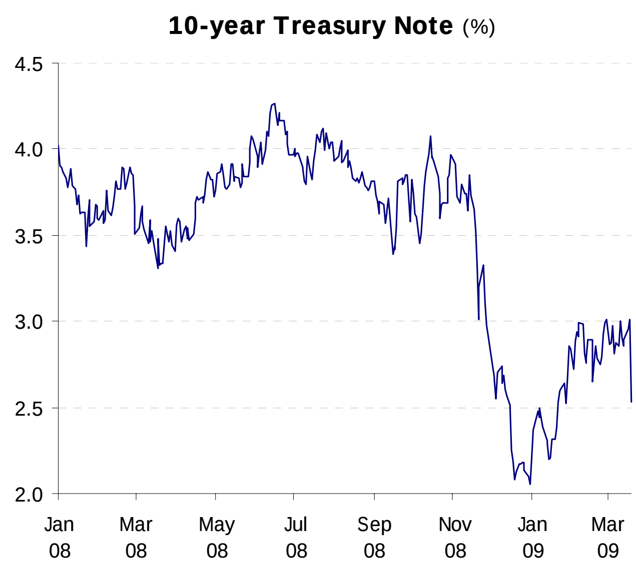
The FOMC decided to maintain its target interest rate at 0 to 0.25%. During the intermeeting period, economic conditions remained weak as "*Job losses, declining equity and housing wealth, and tight credit conditions have weighed on consumer sentiment and spending*." In addition, financial instability has prompted firms to scale back investment, while exports of goods and services have been negatively affected by a global recession.

However, despite these developments, the Fed seems confident that "*policy actions to stabilize financial markets and institutions, together with fiscal and monetary stimulus, will contribute to a gradual resumption of sustainable economic growth."* In light of these developments, the Fed anticipated that *"economic conditions are likely to warrant exceptionally low levels of the federal funds rate for an extended period."* On the inflation front, the Fed expects inflation to remain under control despite downward pressures from increasing economic slack.

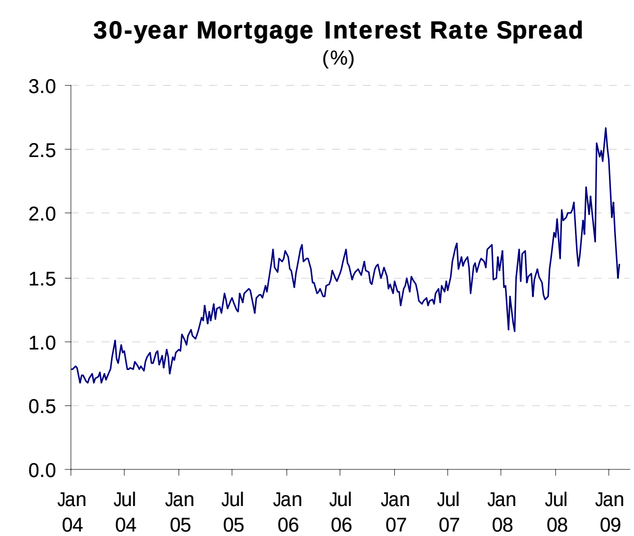
Most importantly, the Fed took additional steps to stabilize financial markets by further increasing the Fed's balance sheet through *"purchasing up to an additional $750 billion of agency mortgage-backed securities, bringing its total purchases of these securities to up to $1.25 trillion this year, and to increase its purchases of agency debt this year by up to $100 billion to a total of up to $200 billion."* Moreover, it also decided to purchase $300bn of longer-term Treasury securities over the next six months and predicted that the range of eligible collateral for the TALF could be expanded.

Bottom-line FOMC finally announced a widely expected purchase of Treasury securities. In addition, the weakness of economic conditions probably tilted the debate on quantitative easing towards the acceptance of more risk taking and a strong balance sheet expansion. This explains reiteration of changes to TALF collateral and today's unanimous vote. These actions, which reflect Fed's strong commitment to financial stability, are expected to boost economic recovery through lower long-term interest rates and higher credit availability. Further actions are likely in the near future if economic conditions continue to deteriorate.

Fed Funds: 0.0-0.25%
Minutes Release: April 8th, 2009
Next Meeting: April 28-29th, 2009



Source: Bloomberg



Source: Bloomberg