

DAILY GLOBAL
COMMENTARY

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Fed Adopts More Aggressive Measures to Fix the Credit Machine and Facilitate Working of Economy

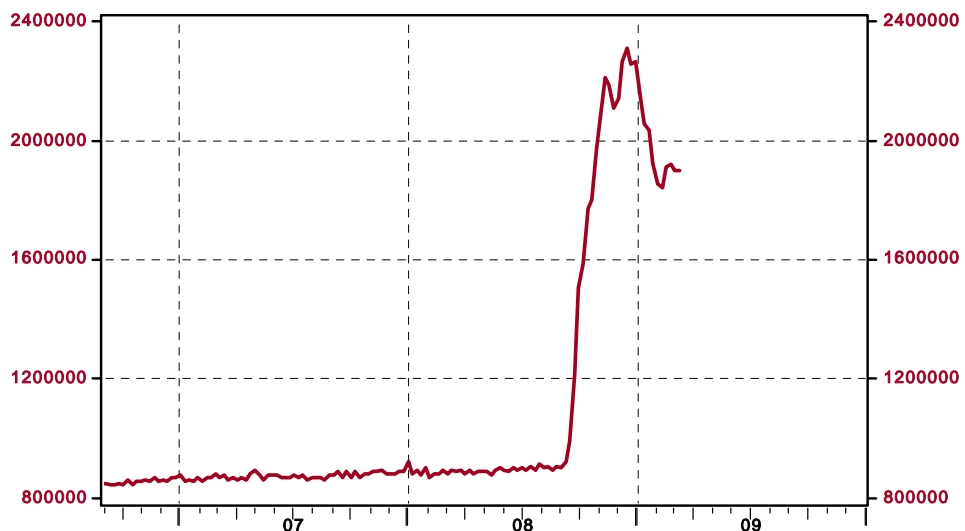
March 18, 2009

The Federal Reserve held the overnight federal funds rate unchanged at 0%-0.25%, as expected. The expansion of existing programs and the decision to purchase long-dated Treasury securities were surprise elements of the announcement. The Fed's balance sheet was \$1.9 trillion for the week ended March 11. Today's announcement noted that the Fed would purchase an additional \$750 billion of agency mortgage-backed securities, increase the purchase of agency debt by \$100 billion, and buy \$300 billion of longer-term Treasury securities, which amounts to an expansion of the balance sheet by \$1.15 trillion. The net impact could be smaller as other programs could possibly shrink.

Chart 1

All Fed Res Banks: Total Assets

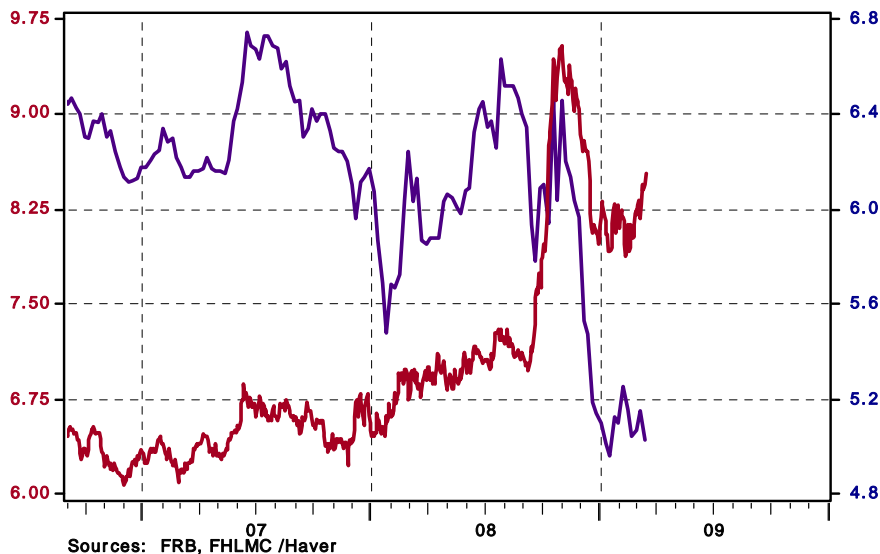
EOP, Mil.\$



Source: Federal Reserve Board /Haver Analytics

Equity and bond markets responded favorably after the policy announcement. The objective of purchasing Treasury securities is to bring about a reduction in long rates with the expectation that these lower rates would trickle down to private sector securities such that mortgage rates and other private sector borrowing costs would be less burdensome. We will be tracking these borrowing rates closely to assess the impact of the Fed's actions. The 30-year mortgage rate was 5.03% as of the week ended March 11 and Moody's Baa corporate bond yield was 8.54% on March 16.

Chart 2
Moody's Seasoned Baa Corporate Bond Yield
 % p.a. (l)
FHLMC: 30-Year Fixed-Rate Mortgages: U.S.
 %



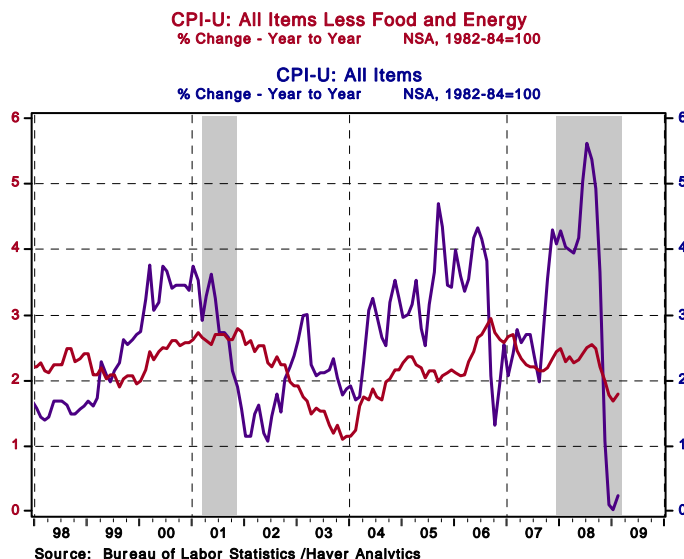
The Fed noted the economy continues to contract and concluded that “*although the near-term economic outlook is weak, the Committee anticipates that policy actions to stabilize financial markets and institutions, together with fiscal and monetary stimulus, will contribute to a gradual resumption of sustainable economic growth.*” With regard to inflation, the FOMC indicated that there is “*some risk that inflation could persist for a time below rates that best foster economic growth and price stability in the longer term.*” Essentially, the Fed’s view about inflation is unchanged from the January policy statement.

Higher Gas Prices Mostly Responsible for Sharp Increase in Consumer Price Index in February

The Consumer Price Index (CPI) moved up 0.4% in February, following a 0.3% increase in January. Gains of the energy price index in January (+1.7%) and February (+3.3%) helped to raise the headline readings during these months. The Labor Department has indicated that about two-thirds of the all items increase was from higher prices for gasoline. The gasoline price index increased 8.3% in February after a 6.0% jump in January. The food price measure rose 0.1% in January and was followed by a 0.1% drop in February. Excluding food and energy, the core CPI has recorded gains of 0.2% in January and February. On a year-to-year basis, the CPI rose 0.2% in February after registering readings close to zero in each of the two prior months. The core CPI increased 1.79% in February vs. a 1.68% increase in January.

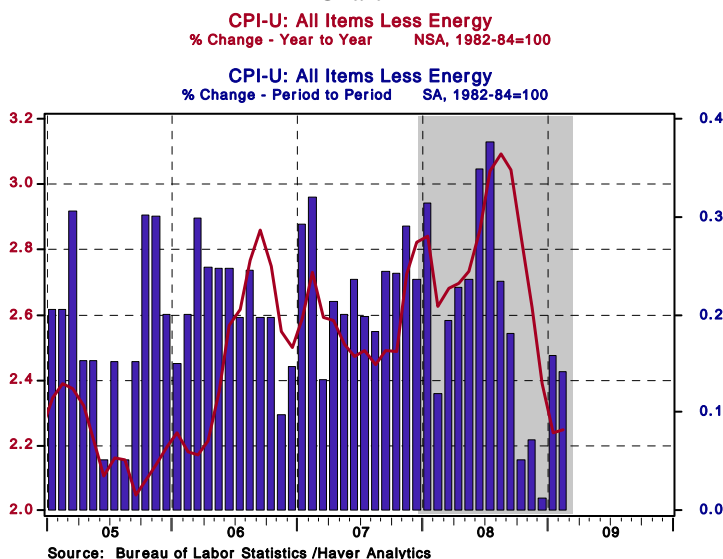
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Chart 3



The CPI excluding energy has recorded gains between +0.01% and +0.18% in the last six months. The year-to-year change of this price index has been nearly steady at 2.25% in the last two months. The price trends of the core CPI and CPI less energy have reduced anxiety about deflation in the near term, for now. The headline CPI index is most likely to post year-to-year declines for several months, reflecting the sharp increase in energy prices during the latter-half of 2008.

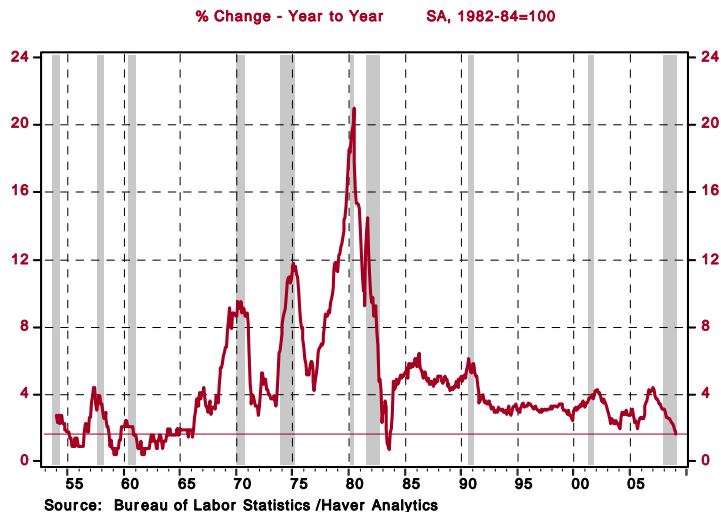
Chart 4



In February, higher prices for clothing (+1.3%), medical care (+0.3%), new cars (+0.8%), education (+0.4%), cigarettes (+0.7%) and recreation (+0.4%) accounted for the gain in the core CPI. Shelter costs, the largest component of the core CPI, held nearly steady in February, with the year-to-year change at 1.67%, the smallest increase since September 1983.

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Chart 5
CPI-U: Shelter



Conclusion – The Fed will watch core CPI prices closely such that a deflationary trend is not entrenched.

CONSUMER PRICE INDEX – FEBRUARY 2009

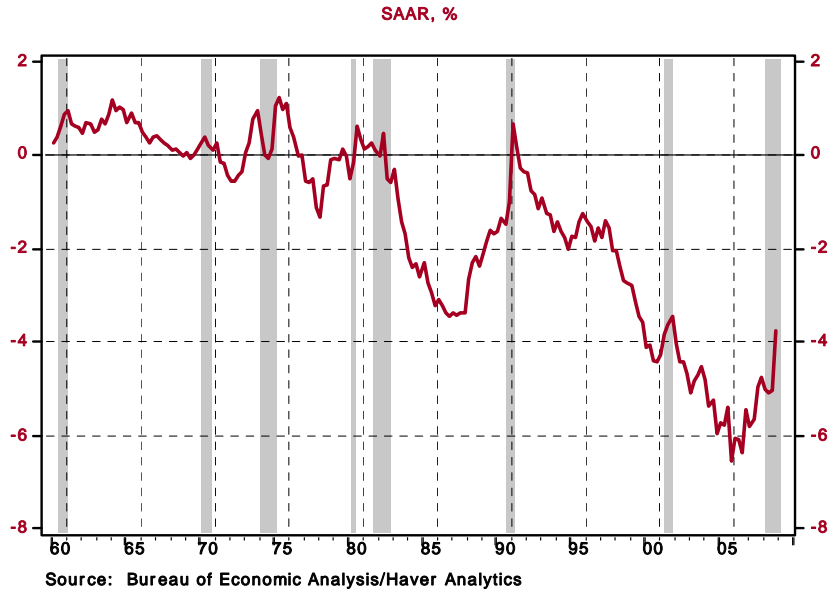
	% change prior month	annualized % change			% change	
		year-to-date	3 mo. ago	6 mo. ago	Feb-09 yoy	Feb-08 yoy
CPI - ALL ITEMS	0.4	4.1	-0.5	-5.0	0.2	0.1
CORE - ALL ITEMS LESS FOOD & ENERGY (77.75)*	0.2	2.2	1.5	1.1	1.8	1.8
CPI ALL ITEMS LESS ENERGY (92.4)	0.1	1.8	1.2	1.2	2.2	2.4
FOOD (14.63)	-0.1	-0.3	0.0	2.2	4.8	5.9
ENERGY (7.62)	3.3	34.5	-17.4	-47.8	-18.5	-21.3
SHELTER (33.2)	0.0	0.9	0.7	1.3	1.7	1.9
COMMODITIES (39.6)	0.9	8.7	-2.9	-12.9	-3.3	-4.1
COMMODITIES LESS FOOD & ENERGY (21.5)	0.4	3.1	1.2	-0.5	0.0	-0.6
SERVICES (60.4)	0.1	1.4	1.3	0.8	2.7	3.0
SERVICES LESS ENERGY SERVICES (56.3)	0.1	1.8	1.6	1.6	2.5	2.7
FRB CLEVELAND MEDIAN CPI	0.2	2.5	2.1	2.3	2.8	2.9

Current Account Deficit Shrinks as Imports Fall

The current account deficit of the U.S. economy was \$132.8 billion in the fourth quarter, down from \$181.3 billion in the third quarter. During 2008, the current account deficit narrowed to \$673.3 billion from \$731.2 billion in 2007. This is the smallest current account deficit since 2004. The current account deficit as a percent of GDP was 3.7% in the fourth quarter of 2008, the lowest since the fourth quarter of 2001. On an annual basis, the current account deficit was 4.7% of GDP, the lowest since 2002. In sum, the current account deficit has narrowed to a significant extent.

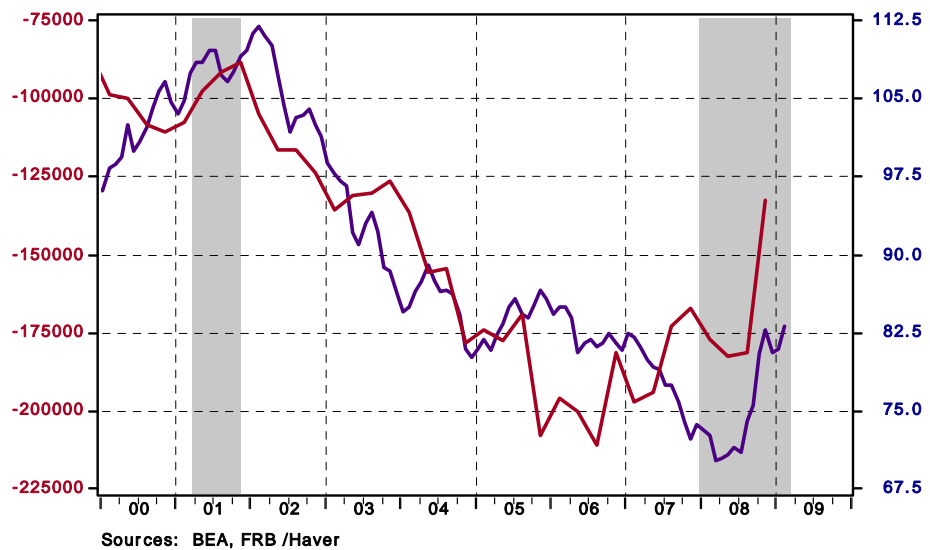
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Chart 6
Balance on Current Account as a % of GDP



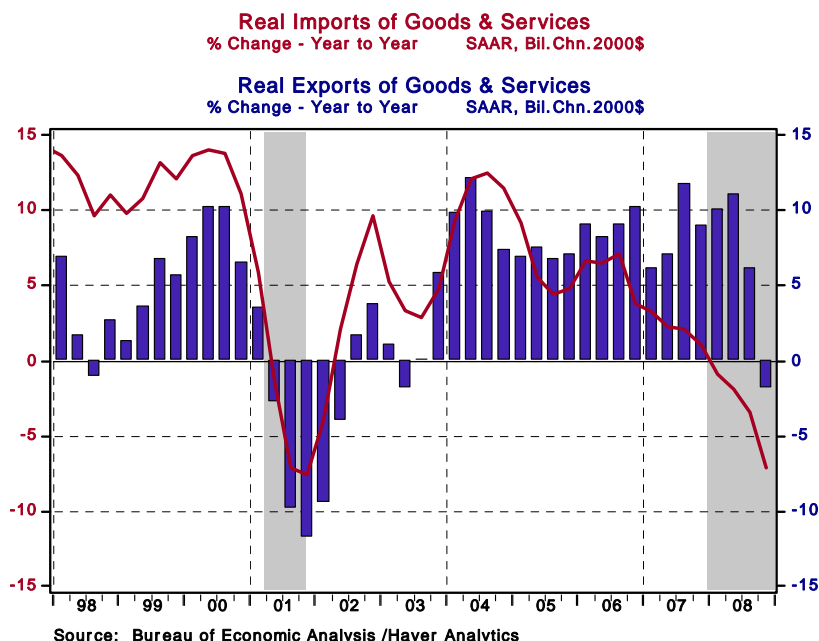
The remarkable improvement in the current account deficit was due to the growth in exports, a decline in the trade-weighted dollar prior to second-half of 2008, and a sharp drop in imports as economic growth slowed in the U.S. (see charts 7 and 8).

Chart 7
SA, Mil. \$
Nominal Trade-Weighted Exch Value of US\$ vs Major Currencies
Mar-73=100



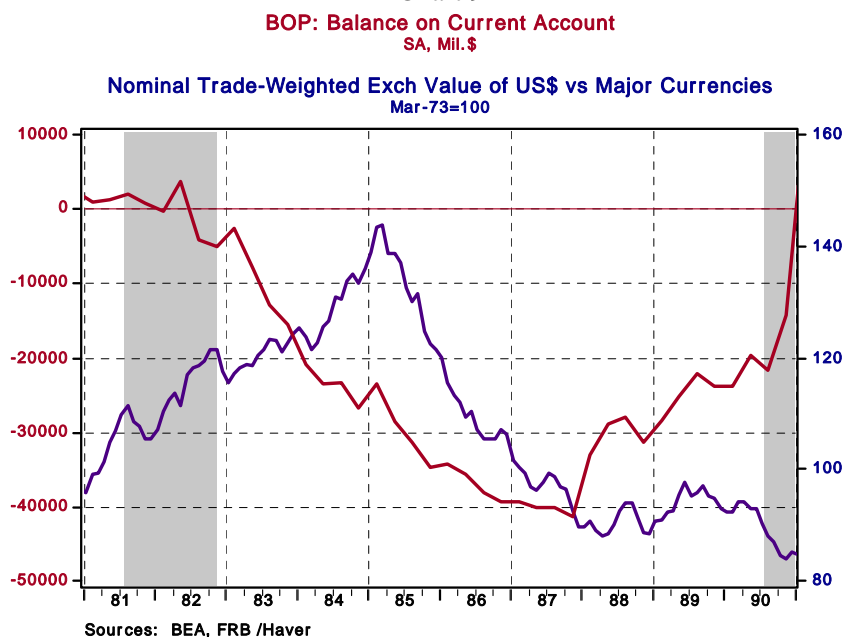
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Chart 8



In the late 1980s, when the current account deficit as a percent of GDP reached a record high of 3.4% of GDP (1987) and improved thereafter, the weakness of the dollar and exports were largely responsible for a narrowing of the current account deficit. Imports continued to advance until the 1990-91 recession commenced (see charts 9 and 10)

Chart 9

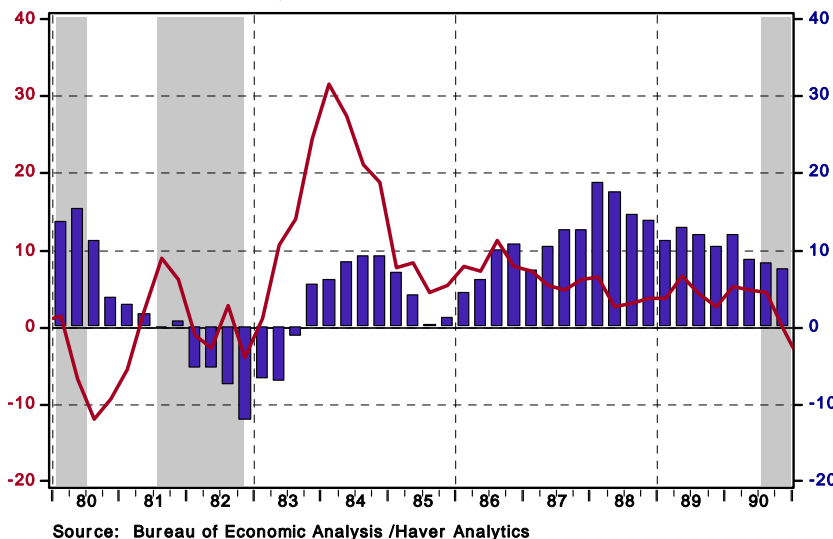


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Chart 10

Real Imports of Goods & Services
 % Change - Year to Year SAAR, Bil.Chn.2000\$

Real Exports of Goods & Services
 % Change - Year to Year SAAR, Bil.Chn.2000\$

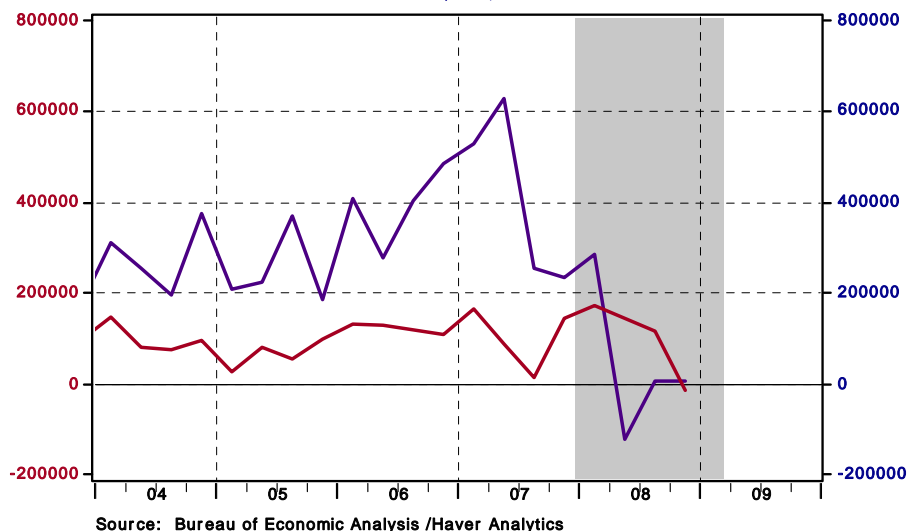


Net capital inflows to the U.S. increased slightly in the third (+7.3 billion) and fourth (+6.0 billion) quarters of 2009, after a drop of \$122 billion in the second quarter. Official net capital inflows declined in the fourth quarter of 2008.

Chart 11

BOP: Foreign Official Assets in the U.S., Net
 SA, Mil.\$

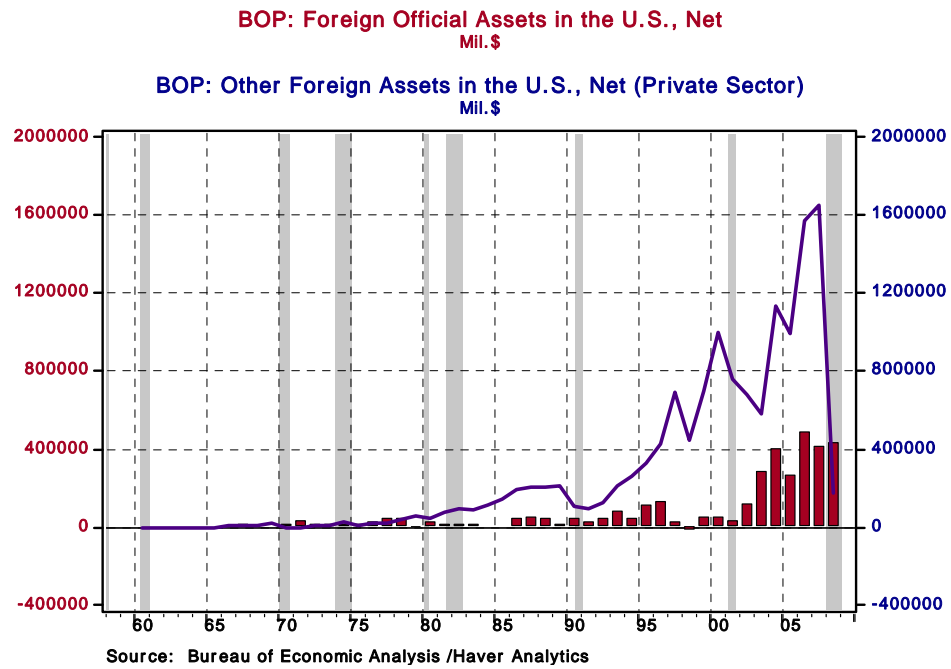
BOP: Other Foreign Assets in the U.S., Net (Private Sector)
 SA, Mil.\$



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Private sector net capital inflows to the U.S. were significantly smaller in 2008 (\$177.7 billion) compared with the net inflows in 2007 (\$1.6 trillion).

Chart 12



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