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Banks pump billions to calm the markets

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Summary:
The US Federal Reserves pumped more than 100 bilion dollars to save the financial markets

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Article Body:
Fed joins global bid to ease credit crisis
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The Federal Reserve and central banks around the world yesterday took the extraordinary step of pumping more than $100 billion into financial markets riven by a credit crisis, the largest such intervention since the September 11 terrorism attacks.
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In a rare public statement, the Fed said it wanted to ensure financial markets had enough money to continue operating in an orderly fashion.

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"In current circumstances," the Fed said, banks "may experience unusual funding needs because of dislocations in money and credit markets."

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Financial markets are reacting seemingly overnight to the jarring end of an era of easy money, when higher-risk borrowers enjoyed nearly unfettered access to huge sums at low interest rates. The market for subprime mortgages, to people with less than perfect credit histories, cracked first and remains the most seriously impaired, but other types of credit such as corporate junk bonds and mortgages backing commercial property are also under duress.

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So far, the central bankers' strategy of rapid, severe intervention shows signs of working. Earlier yesterday, European stock markets posted losses of as much as 3 percent, and it appeared US markets would follow suit when the Dow Jones industrial average began the day with a 212-point decline. But as the Fed pumped money into the US system through the day, stocks began to rally, and the Dow finished the day down just 31.14 points, at 13,239.54. Despite the tremendous, sudden investor anxiety and wild market gyrations and losses, the Dow actually ended the week up -- just barely -- with a 0.4-percent gain.

"Within the stock market there has been massive dislocation, and the Fed provided everyone a little room to unwind," said Kevin Cronin, chief investment officer at Putnam Investments in Boston. If lenders had been unable to continue providing credit, he said, then interest rates would have exploded, potentially leading to a widespread reduction in economic activity.

The Fed "wanted to let the air out of the balloon," Cronin said.

The Fed yesterday loaned $38 billion to US banks to help them finance credit and lending operations, on top of a similar $24 billion the US regulator provided Thursday. Earlier yesterday, central bankers in Europe, Japan, Asia, and Canada made similar moves.

The central banks' actions enabled lenders to have enough money available to loan to investors to buy, sell, or hold securities as they would normally. Without such additional funds, a shortage of credit could cause markets to seize and prices to go haywire.

"Central bankers did two things," said Art Hogan, chief market analyst at Jeffries & Co. in Boston. "They added much needed liquidity to the market and signaled that they stand at the ready for a system that may or may not need more help."

More problems seem to arrive daily. Yesterday, shares of Countrywide Financial Corp. fell nearly 3 percent one day after the biggest US mortgage lender said credit problems among its own borrowers are worsening, and it anticipated more difficulty funding loans. Separately shares in Washington Mutual Inc., the big savings and loan, were down 2 percent a day after it said it faces risks from lower market liquidity.

Yesterday's stock swings capped three weeks in which the Dow Jones industrial average often moved at triple-digit levels in each trading session. The turmoil reflects uncertainty about financial markets even though the economy itself appears to remain stable, according to economists and traders.

"The fundamentals, underlying inflation, economic growth rates, US employment growth, are still robust," said Nariman Behravesh, chief economist at Global Insight of Waltham. "The markets are panicking a little, but it's still a financial story. As long as the central banks succeed in calming markets down, I don't see this spreading to the broader economy."

The volatility still poses longer-term strategy questions for the Fed. One is whether to lower interest rates, even though this week Fed policy makers elected to keep their benchmark lending rate at 5.25 percent, arguing that inflation is a greater risk to the economy than the credit shortage. But by lowering its interest rate, the Fed would make it cheaper to borrow money. That would ease pressures on the real estate sector and other investments by, for example, lowering the overall cost of transactions such as buying a home or refinancing a mortgage.

Richard Yamarone, chief economist at Argus Research in New York, said he suspects the Fed will simply try to hold the line on interest rates. He noted that in its statement to the markets yesterday the Fed made a point of mentioning the current interest rate of 5.25 percent.

"They're saying to the markets, 'Listen, we're giving you some breathing room, but we're still sticking to our guns' " on the interest rates, Yamarone said.