

August 12, 2009



FEDERAL RESERVE

The Fed will wind down Treasuries purchases

ACCORDING TO THE FEDERAL RESERVE (Fed)

- The information received since June suggests that economic activity is levelling out.
- The prices of energy and other commodities have risen recently. However, substantial resource slack is likely to dampen cost pressures and the committee expects that inflation will remain subdued for some time.
- To promote economic recovery and to preserve price stability, the target for the federal funds rate will be maintained at 0 to 0.25% for an extended period.
- The program to purchase US\$300B in Treasuries should be completed by the end of October.

COMMENTS

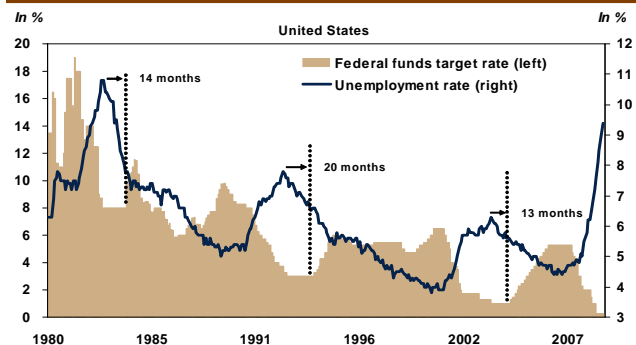
To no one's surprise, the Fed opted this afternoon to keep the target for the federal funds rate between 0 and 0.25%. The real question was whether, as the Bank of England did last week, the Fed would expand its Treasuries purchase program, which is expiring rapidly. With its answer, the Fed has decided to take a stand with the optimists. The US\$300B plan will continue as planned until the end of October but, in order to promote a smooth transition, the Fed is undertaking to gradually slow the pace of its purchases (there is about US\$50B left to finish the program).

With the ongoing improvement by economic and financial variables, there was no need to do more to secure economic recovery, especially as the markets, still concerned about its potential impact on inflation, were not unanimous about the quantitative easing program. Again, the Fed has not said much in regard to inflation, standing pat: it will not be a problem for some time.

Although the U.S. economy seems to be poised to return to growth, today's statement should not be construed as auguring an upcoming key rate increase. First, the Fed will have to be sure that, over the coming months, the economy can function without the support of its many programs. A watchful eye must also be kept on the Fed's mandates: employment growth and price stability. On one hand, the

Fed tends to start an interest rate firming cycle more than a year after the unemployment rate has crested. On the other, with the huge output gap created by at least seven quarters of production below potential, non-energy price pressures are almost non-existent. Parallel to that, with the job market's ongoing deterioration, wage pressures are subdued and the lags that are generally noted with the economic cycle show that workers will have weak bargaining power for the next two years.

Generally, the Fed won't raise interest rates before the labour market improves significantly



Sources: Bureau of Labor Statistics, Datastream and Desjardins, Economic Studies

Implications: The Fed should gradually reveal its quantitative policy exit strategies to the markets, but it is still too early for rate hikes. The gradual withdrawal from Treasuries purchases in the context of a large supply could mean higher long bond rates more quickly than expected.

Martin Lefebvre
Senior Economist

François Dupuis
Vice-President and Chief Economist

Yves St-Maurice
Director and Deputy Chief Economist

Mathieu D'Anjou
Senior Economist

Francis Généreux
Senior Economist

Martin Lefebvre
Senior Economist

Hendrix Vachon
Economist

514-281-2336 or 1 866 866-7000, ext. 2336
E-mail: desjardins.economics@desjardins.com

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EXCERPT FROM THE FEDERAL RESERVE PRESS RELEASE

Information received since the Federal Open Market Committee met in June suggests that economic activity is leveling out. Conditions in financial markets have improved further in recent weeks. Household spending has continued to show signs of stabilizing but remains constrained by ongoing job losses, sluggish income growth, lower housing wealth, and tight credit. Businesses are still cutting back on fixed investment and staffing but are making progress in bringing inventory stocks into better alignment with sales. [...] The prices of energy and other commodities have risen of late. However, substantial resource slack is likely to dampen cost pressures, and the Committee expects that inflation will remain subdued for some time.

[...] The Committee will maintain the target range for the federal funds rate at 0 to 1/4 percent and continues to anticipate that economic conditions are likely to warrant exceptionally low levels of the federal funds rate for an extended period. As previously announced, to provide support to mortgage lending and housing markets and to improve overall conditions in private credit markets, the Federal Reserve will purchase a total of up to \$1.25 trillion of agency mortgage-backed securities and up to \$200 billion of agency debt by the end of the year. In addition, the Federal Reserve is in the process of buying \$300 billion of Treasury securities. To promote a smooth transition in markets as these purchases of Treasury securities are completed, the Committee has decided to gradually slow the pace of these transactions and anticipates that the full amount will be purchased by the end of October. 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 Federal Reserve is monitoring the size and composition of its balance sheet and will make adjustments to its credit and liquidity programs as warranted.

**Table 1
Schedule and key rates**

Date	Central Bank	Decision	Rate
June 2008			
2	Reserve Bank of Australia	s.q.	3.00
4	European Central Bank	s.q.	1.00
4	Bank of England	s.q.	0.50
4	Bank of Canada	s.q.	0.25
10	Reserve Bank of New Zealand	s.q.	2.50
10	Bank of Brazil	-100 b.p.	9.25
15	Bank of Japan	s.q.	0.10
17	Bank of Norway	-25 b.p.	1.25
18	Swiss National Bank	s.q.	0.25
19	Bank of Mexico	-50 b.p.	4.75
24	Federal Reserve	s.q.	0.00 / 0.25
July 2008			
2	European Central Bank	s.q.	1.00
2	Bank of Sweden	-25 b.p.	0.25
7	Reserve Bank of Australia	s.q.	3.00
9	Bank of England	s.q.	0.50
14	Bank of Japan	s.q.	0.10
17	Bank of Mexico	-25 b.p.	4.50
21	Bank of Canada	s.q.	0.25
22	Bank of Brazil	-50 b.p.	8.75
29	Reserve Bank of New Zealand	s.q.	2.50
August 2008			
4	Reserve Bank of Australia	s.q.	3.00
6	European Central Bank	s.q.	1.00
6	Bank of England	s.q.	0.50
10	Bank of Japan	s.q.	0.10
12	Bank of Norway	s.q.	1.25
12	Federal Reserve	s.q.	0,00 / 0,25

s.q.: status quo; b.p. : basis points
Source: Desjardins, Economic Studies

**Table 2
Coming soon**

Date	Central Bank
August 2009	
21	Bank of Mexico
September 2009	
1	Reserve Bank of Australia
2	Bank of Brazil
3	European Central Bank
3	Bank of Sweden
9	Reserve Bank of New Zealand
10	Bank of England
10	Bank of Canada
16	Bank of Japan
17	Swiss National Bank
18	Bank of Mexico
23	Bank of Norway
23	Federal Reserve
October 2009	
6	Reserve Bank of Australia
8	European Central Bank
8	Bank of England
13	Bank of Japan
16	Bank of Mexico
20	Bank of Canada
21	Bank of Brazil
22	Bank of Norway
28	Reserve Bank of New Zealand
28	Bank of Japan
29	Bank of Sweden
November 2009	
2	Reserve Bank of Australia
4	Federal Reserve

Source: Desjardins, Economic Studies