Many economists line up behind Fed on outlook

By Paul Davidson and Barbara Hansen June 24, 2013

Most economists surveyed by USA TODAY say economic growth will not be slowed by the Federal Reserve's market-rattling announcement last week that it will likely rein in its extraordinary stimulus this year.

Well over half of the economists surveyed said growth will not be reduced if the Fed begins to pare back its $85 billion in monthly government bond purchases later this year, then ends them by mid-2014.

That's the road map outlined by Fed Chairman Ben Bernanke at a news conference after a Fed meeting Wednesday, assuming the economy and labor market continue to improve and the 7.6% unemployment rate falls to 7% by the middle of next year. The survey of 41 economists was conducted June 21.

Bernanke's unexpected remarks set off a 550-point drop in the Dow Jones industrial average Wednesday and Thursday — its biggest two-day decline in 19 months. Yields on 10-year Treasury bonds, which influence interest rates broadly for consumers and businesses, have risen from 2.18% to 2.54%.

Financial markets worried that the economy isn't strong enough to withstand the withdrawal of the Fed's stimulus, which has held down interest rates, buoying the stock market and home sales since last fall.

But three out four economists surveyed said their economic outlook supports the Fed's tentative blueprint for phasing out the bond purchases. The economists expect unemployment to fall to 7.3% by December.

"The U.S. economy will learn how to function without (the Fed's) crutches," says **Bernard Baumohl, chief economist of the Economic Outlook Group.** He noted that the share of income Americans are using to pay off debt has fallen to a 30-year low, corporations are sitting on near-record cash reserves, and credit conditions have eased.

The stock market's plunge last week, he says, "does not reflect economic fundamentals. We will likely see some sanity come back (to the markets) in coming days."

Baumohl says a further rise in interest rates should be anticipated as the Fed pulls back its stimulus. He expects 10-year Treasuries to approach 3% by the end of the year. And 30-year mortgage rates could climb from 3.93% to 4.25% by December, the economists' median estimate shows.

But **Baumohl** says that's still cheap money by historical standards, and other forces will continue to propel the housing market, particularly job growth and rising home prices.

He believes, however, that Bernanke unnecessarily shook markets by disclosing too much about its tentative plans too soon, noting that economic reports are not yet indicating strong growth. According to the economists' median estimate, they expect the Standard & Poor's 500 stock index to rise 3.2% the rest of the year to 1,643, but that's below Tuesday's close of 1,651 — before Bernanke's remarks.

UBS economist Maury Harris disagrees, saying Bernanke needed to acclimate investors to an economy that doesn't live off the Fed's steroids. "There was no way to candy-coat it," he says.

Joel Naroff of Naroff Economic Advisors is among the 15 economists who believe Bernanke went too far, and the economy isn't yet strong enough to handle a scaling back of the Fed's easy money policy. "I think he's blowing it," Naroff says.

He was forecasting economic growth of 3.5% next year but now thinks a phaseout of the Fed's bond-buying could cut that by a quarter to a half a percentage point as home sales slow in 2014.

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