

## MOST READ ON BLOOMBERG

1. Portugal to Benefit From Broader Aid Fund

2. Bernanke Bets Commodities Won't Fan Inflation

3. Japan Safer Than Top-Rated France

4. Fed Spends 40% on Benchmarks

5. India Predicts Fastest Growth Since '08

6. Indonesia Growth Fastest in 6 Years

7. Besley: BOE May Forecast Slower Inflation

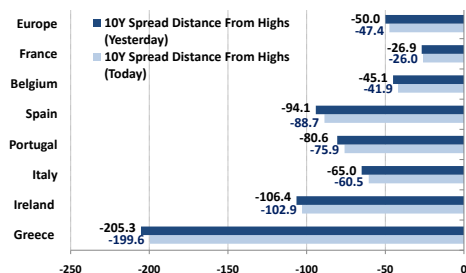
## DATA REPORTS (NEW YORK TIME)

TIME	EVENT	SURVEY	PRIOR
0:00	JN Leading Index CI	101.4	100.6
0:30	AU Foreign Reserves	-	41.6B
0:30	IN FY11 GDP Constant YoY%	8.60%	8.00%
4:30	EC Sentix Investor Confidence	13.3	10.6
6:00	GE Factory Orders MoM (sa)	-1.50%	5.20%
15:00	US Consumer Credit	\$2.000B	\$1.346B
18:50	JN Current Account Balance YOY	24.2%	-15.7%

## ECONOMIC-EVENTS CALENDAR

TIME	EVENT
7:00	EC NATO's Rasmussen Press Conference
9:00	EC ECB's Weber Speaks in Tallinn
9:30	US ECB Announced Bond Purchases
11:00	US Fed To Buy \$7-9bln in Notes/Bonds
12:15	LX ECB's Mersch at Luxembourg Event
TBA	PO Bank of Portugal Data on Banks

## 10Y SPREADS: DISTANCE FROM HIGHS



## TOP CURRENCY PERFORMERS

One day spot return in percent

Japanese Yen	0.64
Australian Dollar	0.35
Norwegian Krone	0.35
New Zealand Dollar	0.27
Swiss Franc	0.26
Brazilian Real	0.10
Taiwanese Dollar	0.08
Danish Krone	0.05
Euro	0.02
Mexican Peso	-0.01

## Consumer Credit, Obama Speech, Stocks Climb

FIRST WORD DAYBOOK:  
Morwenna Coniam

invest in the U.S., 11:30 a.m. **Dutch Central Bank President Nout Wellink** is unlikely to succeed President **Jean-Claude Trichet** at the ECB, Dutch Finance Minister **Jan Kees de Jager** said. **Greek Deputy Prime Minister Theodoros Pangalos** rejected a proposal by German Chancellor **Angela Merkel** to include limits on debt in government constitutions, Ta Nea reported.

■ **WHAT TO WATCH: Consumer borrowing in the U.S.** likely rose by \$2.5 billion in December after increasing \$1.35 billion in November, economists said, 3 p.m. **President Barack Obama**, in a speech to the Chamber of Commerce, will challenge American business leaders to move their cash from the sidelines to

■ **ECONOMICS: European investor confidence** rose to the highest level in more than three years in February, an index showed. **German factory orders** fell in December after jumping five times more than economists expected in November.

■ **GOVERNMENT: Treasury Secretary Timothy F. Geithner** travels to Brazil to discuss bilateral and G20 issues. **Egyptian Vice President Omar Suleiman** and some members of the opposition agreed on limited steps to resolve the crisis.

■ **MARKETS: The MSCI World Index** of stocks climbed to a 2 1/2-year high. The **pound** strengthened against the euro. **Japan's bonds** fell for a third day. **Copper** surged to a record. **Egypt** will try to raise as much as 15 billion Egyptian pounds (\$2.6 billion) in a record sale of Treasury bills.

**BIG PICTURE:** JOSEPH BRUSUELAS, BLOOMBERG ECONOMIST

## Week Ahead in the U.S.: Jobs Data, Consumer Confidence

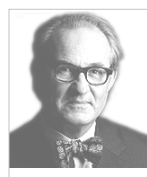
The tepid increase in U.S. total employment observed in January nonfarm payrolls is likely to remain at the top of investors' watch lists as additional employment, consumer confidence and trade data are published this week.

Investors will receive fresh data on the labor market from the JOLT (job openings, layoffs and turnovers) report on Tuesday and weekly initial claims data for the week ending Feb. 5 on Thursday. Recent JOLTS data and the underlying trend in the weekly

claims report both support an improving labor market, as do the recent labor differential in the January estimate of consumer sentiment by the Conference Board and the fresh cycle highs in the employment subcomponents of the ISM surveys of the manufacturing and service sectors.

Seasonal factors due to weather-related effects mean there is some downside risk to the initial claims data on the release. The number of snowstorms across the country throughout the winter is likely to affect the

continued on next page



## KEENE'S CORNER

Michael Pond of Barclays on inflation.

**BIG PICTURE** JOSEPH BRUSUELAS  
continued from page 1

claims data through February and possibly into March.

Consumer confidence may remain somewhat dour due to the ongoing inclement weather and rising gasoline prices. The NFIB small business optimism survey will be published on Tuesday and the University of Michigan's estimate of consumer confidence will be released on Friday. The median forecast of a rise to 93.8 in the NFIB survey from 92.6, according to a survey of economists, reflects the recent improvement in overall growth and the rise in personal spending by consumers.

Economists expect the University of Michigan survey, which is more sensitive to movement in equity prices than its cousin produced by the Conference Board, to increase to 75 in the preliminary February estimate from 74.2.

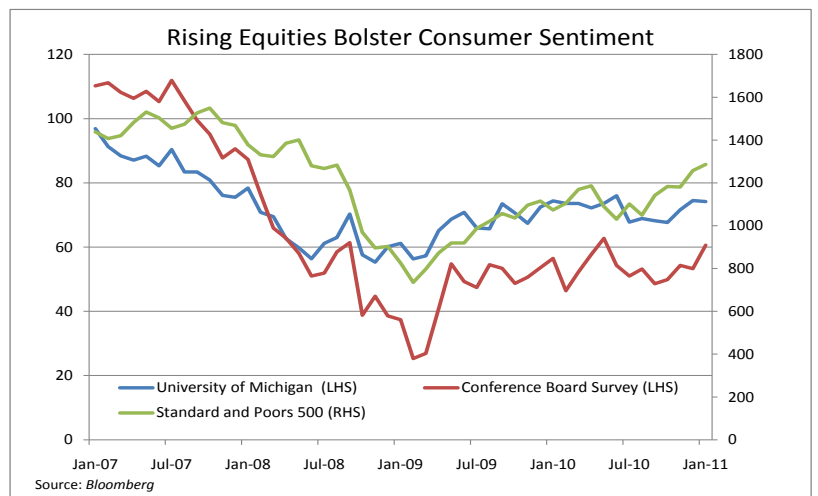
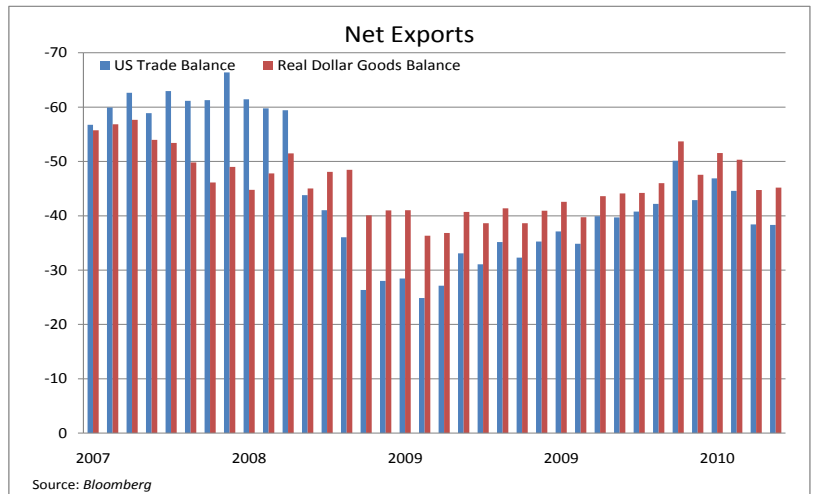
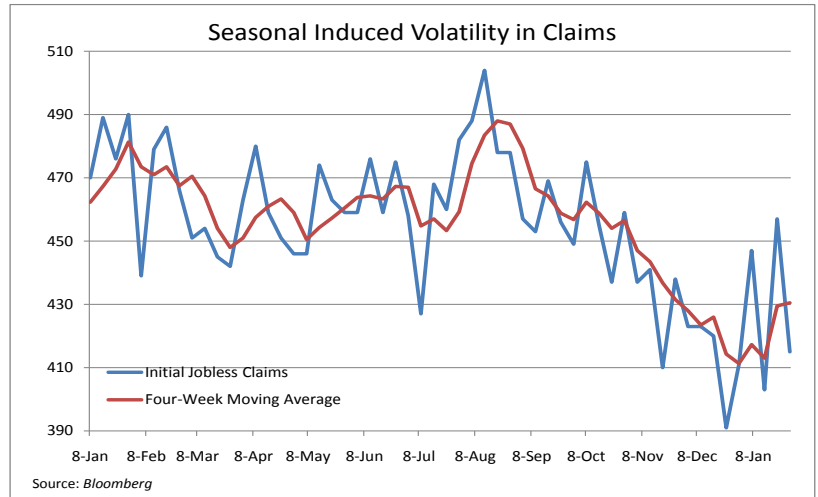
The December trade balance report will provide further information on just how much net exports supported overall growth during the final quarter of 2010. The consensus estimate is that the trade deficit expanded by \$2 billion to \$40.3 billion in December from \$38.3 billion in November.

When estimating the impact of changes in the trade data on growth, a useful rule of thumb is that a net swing of \$1 billion in either direction likely adds/subtracts .01 percent to growth. So the current consensus estimate would mean that growth in the final quarter of 2010 might be pulled down to 3 percent from the initial estimate of 3.2 percent.

This week will see six different speakers from the Federal Reserve address the public. Fed Chairman Ben Bernanke will testify before the House Budget Committee on Tuesday, Dallas Fed President Richard Fisher will present his outlook on the economy on Tuesday and the New York Fed's Brian Sack will speak on the Fed's large-scale asset purchase program Wednesday afternoon.

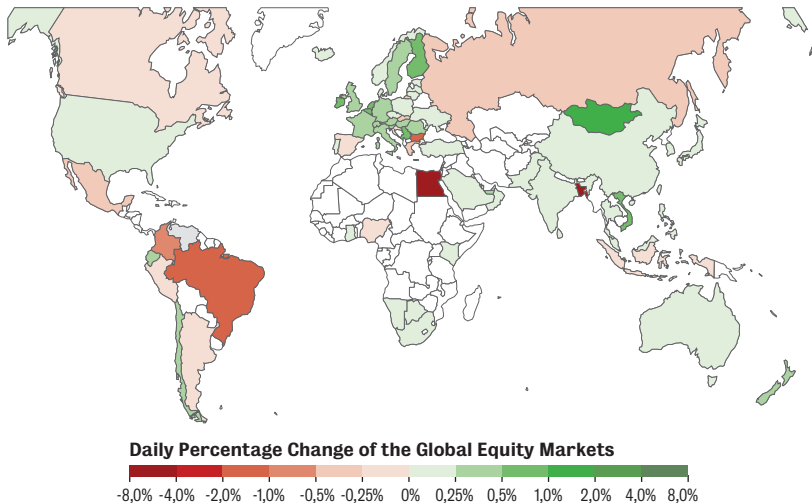
The U.S. Treasury will issue \$32 billion in 3-year notes on Wednesday, \$24 billion in 10-years on Thursday and \$16 billion in 30-year bonds on Friday.

Other important data to be released this week will be the consumer credit report on Monday, as well as wholesale inventories and the monthly budget statement on Thursday.



## OVERNIGHT BY BLOOMBERG NEWS

### Global Equity Performance



### EUROPE

■ An index measuring investor confidence in the euro region jumped to 16.7 in February from 10.6 in January.

■ Germany's factor orders dropped 3.4 percent in December from November, when they climbed 5.2 percent.

■ Norway's industrial production rose 2.2 percent in December from a year earlier after a 3.5 percent gain in November.

■ Sweden posted a budget surplus of 29.9 billion kronor in January.

■ Denmark's industrial output fell 1.1 percent in December after a 1.4 percent decline in November.

■ Portugal aims to increase its exports to 40 percent of gross domestic product, *Jornal de Negocios* reported, citing Economy Minister Jose Vieira da Silva.

■ Ireland's residential rates fell 0.6 percent in 2010 to 830 euros a month, 27 percent below the 2007

peak, according to Daft property website.

■ Estonia's inflation eased to an annual 5.3 percent in January from 5.7 percent in December.

■ Romania's inflation rate will probably end 2011 at 3.6 percent, up from a previous estimate of 3.4 percent, the central bank said.

### ASIA

■ Australia's retail sales climbed 0.2 percent in December from November, when they gained 0.4 percent.

■ Indonesia's economy expanded 6.9 percent in the fourth quarter from a year earlier after growing 5.8 percent in the third.

■ India's economy may expand 8.6 percent in the year ending March 31 from a year earlier, the Central Statistical Organisation said.

### AMERICAS

■ Chile's economic activity grew 5.7 percent in December after a 6.2 percent expansion in November.

## POLITICAL WATCH

BY BLOOMBERG NEWS

### Companies Rap EPA

ConocoPhillips, Boeing and the National Association of Manufacturers are among 201 companies and industry groups that responded to Darrell Issa's request to identify rules his House Oversight and Government Reform Committee should investigate. Of the 111 they cited, 57 came from the Environmental Protection Agency. Issa plans today to release a report. According to copies Bloomberg obtained, among the rules complained about were pesticide permits, air-pollution standards and the financial regulatory overhaul.

### Derivatives Club Access

A proposal to broaden access to clearinghouses may help MF Global Holdings, Jefferies Group and other smaller banks enter a market dominated by Wall Street's biggest banks. The Commodity Futures Trading Commission has proposed a rule that would require clearinghouses in the \$583 trillion global swaps market to open membership to companies with at least \$50 million in capital. The rule "would help break up the club" of derivatives dealer banks on Wall Street, said Robert Litan of the Kauffman Foundation.

### Obama's Challenge

President Barack Obama will challenge American business leaders today to move their cash from the sidelines to invest in the U.S. as part of what he will call a shared burden to boost the nation's economy. Obama will make a case in a speech to the U.S. Chamber of Commerce that he is doing his part to improve the business climate after a free-trade agreement with South Korea, a deal to extend Bush-era tax cuts, and a State of the Union address that proposed more government support for infrastructure and "innovation."

## NEWSMAKERS

BY BLOOMBERG NEWS

**Jan Hatzius**, chief economist at Goldman Sachs, cut the forecast for the U.S. jobless rate to 8 percent by the end of 2012 from a previous estimate of 8.25 percent.

White House budget director **Jacob Lew** said President **Barack Obama** will send Congress a “tough choices” budget next week that would cut some of his own programs in the environment, community development and services for the poor to rein in the deficit.

Former Bank of England policy maker **Tim Besley** said the central bank's quarterly forecasts will probably show inflation reaching the 2 percent target.

Czech Republic President **Vaclav Klaus** said the social-market economy has become the dominant system in Europe and

**Commerzbank AG** forecasts the price of wheat will decline to \$820 per bushel on average for the second quarter of 2011, from the current price of \$885.25.

**Standard Chartered Bank** expects a decline to \$650 per bushel. The median forecast is \$770 per bushel, according to a Bloomberg survey.

is keeping the continent from becoming more successful in growth terms.

Tunisia's interim Prime Minister **Mohamed Ghannouchi** called for international funding to help with the rebuilding and recoup the \$5 billion to \$8 billion losses caused by the political upheaval last month, the Financial Times reported.

Bank of Japan Governor **Masaaki Shirakawa** said Japan's economy is recovering and performing relatively well compared with other economies.

**Akash Reddy**, an economist at Citibank, expects New Zealand to raise its official cash rate in September.

South Korean President **Lee Myung Bak** said the government needs to create a task force with civilian experts to tackle food security, Yonhap News reported.

Nobel laureate **Joseph Stiglitz** said U.S. and European subsidies have undermined incentives to invest in agriculture in the developing world, one of the causes of food inflation, l'Express reported.

Send us news about hires or new appointments at [econbrief@bloomberg.net](mailto:econbrief@bloomberg.net).

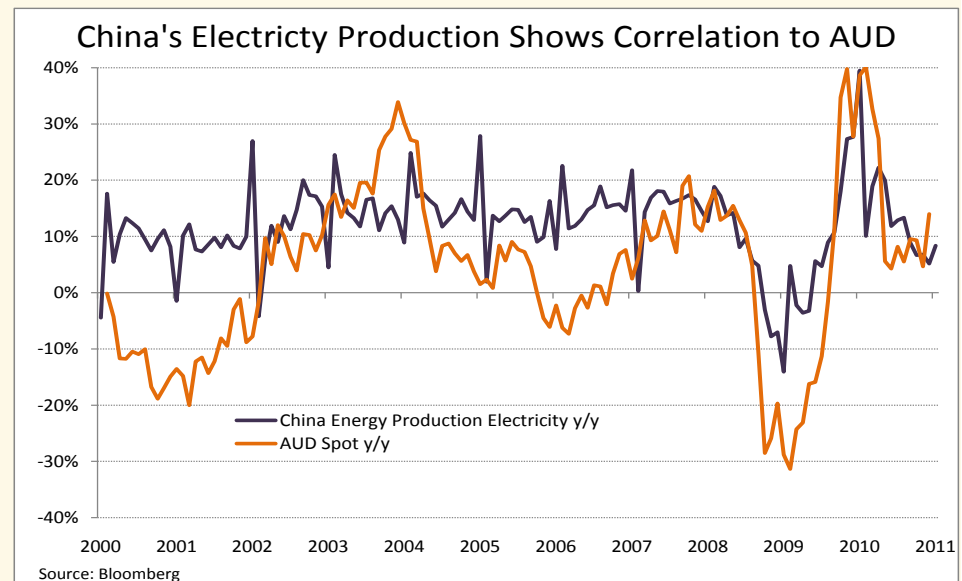
## China Edge for Aussie *MICHAEL MCDONOUGH, Bloomberg Economist*

Investors making bets on the Aussie dollar may need look no further than China to gain an advantage.

Since 2007, the Australian currency has demonstrated a strong correlation with Chinese electricity production (along with some other key Chinese economic indicators, including money supply). Electricity production serves as a good proxy for Chinese growth and is released on a monthly basis. Since 2007, the year-over-year change in the Aussie dollar spot price and Chinese electricity production has exhibited an R squared of 0.66 percent. Since 2008, it has been even higher — 0.71 percent.

Driving this relationship is likely the fact that in 2009, China was the destination for 70 percent of Australia's exported iron ore. On the back of its stimulus package, China imported 43 percent more Australian ore in 2009 than 2008, sparking a mining hiring boom that drove up employment across Australia. This trend continued in 2010 with China's iron ore imports from Australia averaging 22.1 million tons a month, higher than 2009's average of 21.8 million tons.

What goes up may well come down. According to the AUD forward curve, traders are anticipating the Aussie currency will



depreciate 4.6 percent over the next 12 months. This is likely due to the belief that tightening in China may snuff out the country's seemingly insatiable demand for Australia's raw commodities.

Traders may be jumping the gun. The implementation in January of China's 12th five-year plan may help support

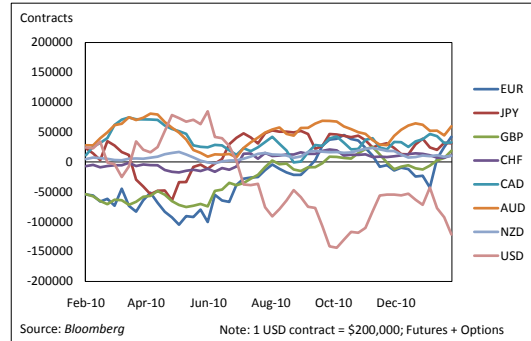
China's commodity demand by bolstering investment in public/low income housing as well as infrastructure projects, all of which require extensive commodity inputs. Unless China reverses course on its objectives, commodity demand through the five-year plan may help buoy the Aussie over at least the next year.

# COMMITMENTS OF TRADERS

DAVID POWELL, BLOOMBERG ECONOMIST

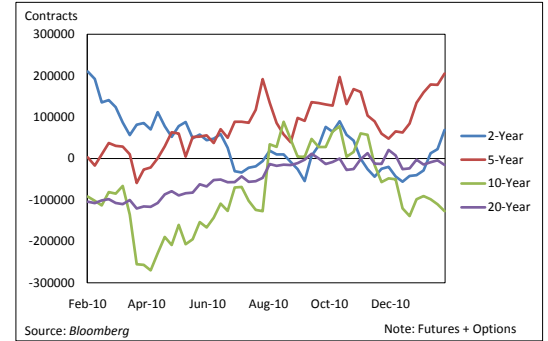
Speculators appear to expect loose monetary policy in the U.S. to weigh on the dollar and 5-year rates. Subdued levels of inflation leave oil as a more attractive commodity investment than gold.

## Currencies



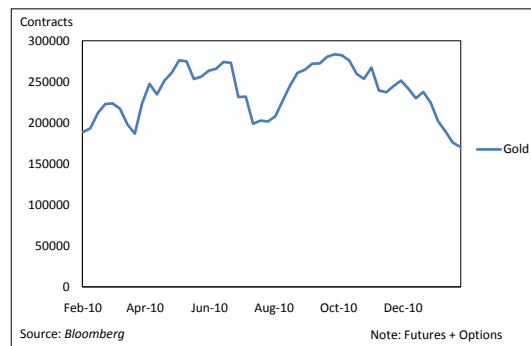
Speculators increased their net long euro position by 17,192 contracts to 42,042. That is 1.7 standard deviations above the one-year average and the highest level since mid-October. It has probably been reduced since the end of the reporting period, with European Central Bank President Trichet having dispelled the notion that the Governing Council was on the verge of raising interest rates. EUR/USD will probably continue to decline along with the spread between two-year euro-area and U.S. swap rates.

## U.S. Treasury Securities



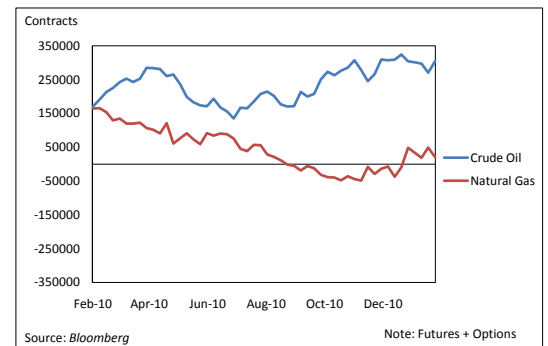
Non-commercial accounts increased their net holdings of 5-year U.S. Treasury notes by 26,980 contracts to 204,890. That is 2 standard deviations above the one-year average and the largest position in more than a year. At the same time, speculators increased their net short position in 10-year notes by 16,669 contracts to bring the total to 127,110. Those positions are consistent with a view that the Federal Reserve will leave interest rates unchanged for the foreseeable future.

## Gold



The net long gold position of speculators fell by 5,122 contracts to 170,706 during the latest reporting period. That is 2.2 standard deviations below the one-year average. The reduction in the holdings of gold, a commodity used to hedge against inflation, suggests that market participants do not expect the loose monetary policy of the Federal Reserve and other central banks around the globe to result in high levels of inflation.

## Energy Products



Non-commercial accounts increased their net long crude oil position by 33,124 contracts to 303,801. That is just below the recent high of 324,335 registered in December. The large long oil position that has been maintained, while the long gold position has been reduced, shows that crude has been the "commodity of choice" of speculators. This week's report, as a whole, suggests that speculators look for the Federal Reserve to remain on hold as inflation remains subdued, preventing the dollar from appreciating, weighing on five-year government yields, leaving gold unattractive, and fueling a bubble in the oil market.



## NEWS OF NOTE

## Fed Spends 40% on Benchmarks as Newest Prove Cheapest

The Federal Reserve's Treasury purchases already have succeeded in driving investors to junk bonds and stocks. Now, policy makers are focusing on benchmark government securities, helping contain rising yields that set rates on everything from corporate debt to mortgages.

More than 40 percent of the government bonds the Fed bought in January for its so-called quantitative easing were auctioned in the previous 90 days, up from 20 percent in December and 15 percent in November, according to Bank of America Merrill Lynch. The central bank is concentrating on newer securities as its \$600 billion program depletes primary dealers' holdings of Treasuries to the lowest since November 2009.

The Fed purchases are helping keep a lid on borrowing costs for companies and homebuyers as the economy recovers. Yields on corporate bonds have averaged about 4.84 percent since the buying began in November, below the 5.48 percent for all of 2010, according to Bank of America Merrill Lynch indexes. Quantitative easing has boosted demand for Treasuries as President Barack Obama's budget deficits exceed \$1 trillion, adding to the nation's \$8.96 trillion in marketable debt. Since Nov. 3, when Fed Chairman Ben S. Bernanke announced the plan to buy government debt to keep the economy from falling into deflation, 10-year yields have increased about one percentage point as expectations for inflation rose.

The Fed became the biggest owner of U.S. government debt in November, when holdings reached \$896.7 billion, overtaking China's \$895.6 billion, according to Treasury and central bank data. It purchased \$288 billion since Nov. 12, mostly from dealers.

— By Cordell Eddings and Daniel Kruger

### Russia Follows China

Russia, the only one of the so-called BRIC countries without capital controls, is following China and Turkey in relying on reserve requirements to drain cash from the economy.

"We stand ready to continue increasing mandatory requirements, if needed," Bank Rossii Chairman Sergey Ignatiev said on Feb. 4.

The central bank on Jan. 31 increased the mandatory reserve ratio while unexpectedly leaving its deposit rates unchanged after inflation in January accelerated to the fastest in 15 months.

Emerging economies are weighing the need to curb inflation against the risk of attracting speculative capital from near-zero interest rates in the

U.S. and Europe.

Russia has kept the benchmark refinancing rate at a record-low 7.75 percent since June and last week raised the mandatory reserve level for liabilities to 3.5 percent for non-resident companies and 3 percent for individuals and others, both from 2.5 percent.

The policy response in countries including Turkey and Russia is "highly unorthodox" and may lead to more aggressive rate increases, said Maria Gordon, an emerging-market equity portfolio manager at Pacific Investment Management Co.

China has set record-high reserve requirements and Latin American nations from Brazil to Peru are lifting ratios and returning to capital controls to stem currency rallies.

— By Paul Abelsky

### AROUND THE WEB New research and commentary on the Web

#### Economists missed the financial crisis for three big reasons:

"specialization, the difficulty of forecasting, and the disengagement of much of the profession from the real world," writes Raghu Rajan, a professor at University of Chicago Booth.

<http://forums.chicagobooth.edu/faultlines?entry=30>

#### "Macroeconomics in the years leading up to the recent crisis

had become a technically demanding subject and was naturally dominated by people who were good at that sort of thing," writes Axel Leijonhufvud of UCLA and the University of Trento, in a CEPR Policy Insight looking at the state of macroeconomic theory. "But unless you took much pride and joy in its technical aspects, it had also become deadly dull."

<http://www.cepr.org/pubs/PolicyInsights/PolicyInsight53.pdf>

"Managerial vocal cues contain useful information about firms' fundamentals," according to a study from William J. Mayew and Mohan Venkatachalam of Duke University. Paul Kedrosky thinks it all sounds a bit Blade Runner-esque.

<http://www.afajof.org/afa/forthcoming/8893p.pdf>

[http://paul.kedrosky.com/archives/2011/02/bladerunner\\_com.html](http://paul.kedrosky.com/archives/2011/02/bladerunner_com.html)

## TRENDS

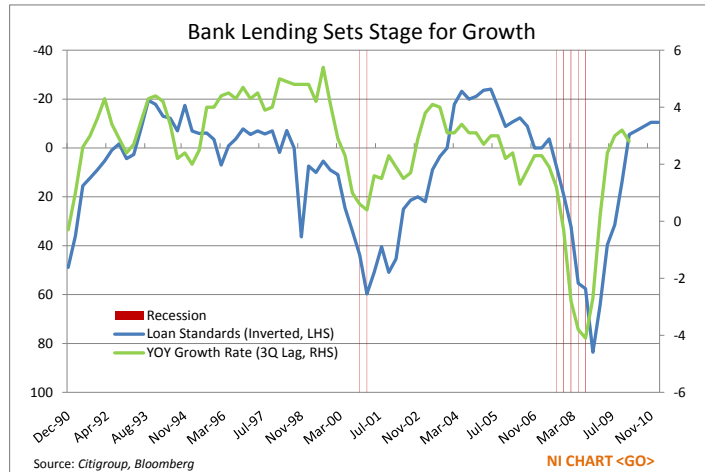
### Easier U.S. Bank Loans Signal 'Robust' GDP Growth

U.S. banks are setting the bar for corporate borrowers low enough to fuel economic expansion this year, according to Tobias Levkovich, Citigroup's chief U.S. equity strategist.

The chart compares changes in standards for commercial and industrial loans to the largest companies, based on a survey of senior loan officers by the Federal Reserve, with the economy's year-over-year growth rate. Levkovich published a similar chart last week.

Bankers easing loan criteria outnumbered those that are tightening by 10.5 percentage points in the Fed's most recent quarterly survey, released last week. This percentage was the same in last year's fourth quarter, the most favorable period for borrowers since 2006.

Shifts in lending standards tend to precede changes in the pace of economic growth by about nine months, Levkovich wrote in a report. For this reason, the chart displays GDP figures with a nine-month lag.



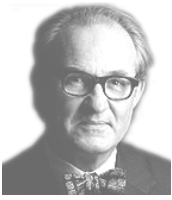
"GDP should be relatively robust through late this year," the report said, as easier access to credit clears the way for many companies to invest. The expansion outlook represents "an encouraging backdrop" for gains in stocks, he wrote.

Levkovich sees the Standard & Poor's 500 Index ending the year at 1,400, amounting to an 11 percent gain for 2011. His projection matches the median estimate of 13 strategists in a Bloomberg survey.

— David Wilson

## MARKET INDICATORS

BOND MARKET				CURRENCY MARKET			
	10-YEAR YIELD	1-DAY CHANGE IN BP	YTD CHANGE IN BP		LAST VS. USD	1-DAY% CHANGE	YTD% CHANGE
U.S.	3.41%	2.0	11.4	Swedish Krona	6.4515	0.28%	-3.87%
Euro-Area	3.19%	-1.7	22.6	Czech Koruna	17.6675	0.34%	-5.49%
Germany	3.19%	-1.6	22.7	Hungarian Forint	197.9500	-0.11%	-4.90%
France	3.56%	-0.8	19.9	Polish Zloty	2.8523	0.28%	-3.71%
U.K.	3.68%	-1.3	28.4	Russia Ruble	29.6797	0.09%	-2.81%
Switzerland	1.87%	-1.0	15.0	S. Africa Rand	7.0909	0.41%	6.97%
Norway	3.85%	-0.2	12.8	Turkish Lira (000)	1584380.0000	0.16%	2.60%
Sweden	3.41%	-0.7	13.2	Brazil Real	1.6743	-0.13%	0.78%
Turkey	9.24%	12.0	123.0	Mexican Peso	12.0378	0.01%	-2.45%
S. Africa	8.62%	10.1	46.2	Chinese Renminbi	6.5860	0.03%	-0.32%
Canada	3.28%	-3.6	15.6	Hong Kong Dollar	7.7890	-0.04%	0.20%
Brazil	12.79%	2.5	62.6	Indian Rupee	45.7562	0.42%	2.35%
Mexico	7.23%	3.8	27.2	Indonesian Rupiah	9031.0000	0.02%	0.39%
Australia	5.50%	-3.2	-4.6	Singapore Dollar	1.2794	0.06%	-0.31%
New Zealand	5.50%	-1.1	-37.4	S. Korea Won	1113.8300	-0.04%	-1.08%
Japan	1.22%	-1.1	9.6	Taiwan Dollar	19.5400	0.31%	1.56%
Hong Kong	2.72%	-1.2	-13.8	<b>COMMODITY MARKET</b>			
Singapore	2.62%	-1.0	-9.0		<b>LAST VALUE</b>	<b>1-DAY CHANGE</b>	<b>1-DAY% CHANGE</b>
<b>CURRENCY MARKET</b>							
	<b>LAST VS. USD</b>	<b>1-DAY% CHANGE</b>	<b>YTD% CHANGE</b>	Crude Oil (Brent)	97.97	0.58	0.60%
Euro	1.3738	0.03%	2.64%	Gasoline (NYM)	238.16	-4.90	-2.02%
Japanese Yen	82.3900	-0.64%	1.57%	Natural Gas (NYM)	4.32	-0.18	-4.04%
British Pound	1.5911	-0.11%	1.92%	Gold (CMX)	1318.40	-14.60	-1.10%
Swiss Franc	0.9429	-0.26%	0.82%	Silver (CMX)	27.03	-0.10	-0.36%
Canadian Dollar	0.9945	0.11%	-0.35%	Copper (LME)	9587.75	146.75	1.55%
Australian Dollar	0.9957	0.37%	-2.70%	Aluminum (LME)	2459.00	32.00	1.32%
New Zealand Dollar	0.7743	0.27%	-0.76%	UBS-Bloomberg Cmtdy	1376.81	2.55	0.19%
Danish Krone	5.4256	-0.04%	-2.56%	Goldman Sachs Cmtdy	629.99	-4.84	-0.76%
Norwegian Krone	5.7790	-0.36%	-0.74%	CRB Index	331.39	-1.44	-0.43%
				Baltic Dry Index	1186.00	-48.00	-3.89%



## KEENE'S CORNER

Tom Keene and Ken Prewitt talk to **Michael Pond**, interest rate strategist at Barclays Capital, about inflation.

**Q: Whispers of inflation out there. Prices paid and some of the manufacturing indexes. You have written up on real estate. Okay, we all know there is inflation. Why do the economists say there is none?**

**A:** Well, it is not that there is none. So you look at core measures and we think that core CPI has now bottomed, but the Fed focuses on the core PCE - the personal consumption expenditure index within the GDP release. And that continues to move lower, so the Fed is looking at inflation trending down. The rest of the markets are looking at inflation starting to pick up a bit.

**Q: Well, that is food and fuel when you talk about core and CPI. But in a story earlier this morning, the London Metals Exchange, copper \$10,000 a metric ton. It's never been seen.**

**A:** Absolutely. So that is hitting a record and it is not just copper. Food prices and energy prices, cotton prices have now moved up 4.5 times what they were in the middle of 2009. So you are see broad-based commodity increases, not just food and energy prices. Those increases are likely to feed in through core in the coming year or so despite the fact that there is still plenty of slack in the economy looking at the unemployment rate.

**Q: In the coming year or so?**

**A:** That's right. Again, we don't look for rapid inflation, anywhere near hyperinflation. But we think we have come off the lows that the Fed is still concerned about. That leaves the Fed likely to leave stimulative policy in place a bit too long causing growth — and inflation to pick up a bit too much down the road.

**Q: Well, let's talk about your reading of history, and for that, your colleague, Dean Maki and Lawrence Kantor. The great certitude of early 2011 is that the Fed won't raise rates. Even if there is a set of data that suggests that, they won't raise rates. Push against that. History tells me at some point central banks have to react.**

**A:** Eventually we think they will. But right now this is a very dovish Fed, very concerned about the downside risk relative to the upside risk. So they think that inflation goes a bit too high, they know what to do. Bernanke on his 60 Minutes interview said he has 100 percent confidence - 100 percent, in being able to bring inflation back down if it gets too high. They are not that confident of being able to bring inflation up if we slip into deflation. So that is why they are much more likely to leave this over-stimulative policy in place too long rather than risk a double dip. The Fed has reminded the investment community that back in the Great Depression and in Japan stimulative policies were removed too early and those caused a double dip. This Fed is not likely to repeat those mistakes.

**Q: Do we know what Bernanke means when he says too high? How high is too high?**

**A:** I mean he has talked about super normal inflation. So hyperinflation is not something that they are considering, but super normal inflation - five to six percent. Again, they target two percent, but that is on core PCE. So headline can run, food and energy prices can rise pretty significantly before the Fed gets concerned about a general rise in prices. So we think that the market might be starting to price in concerns over inflation because the Fed is focused on this one measure that remains quite low. We see the unemployment rate drop, but it is still a very high rate. We think there is quite a bit less slack in the economy than the Fed does. And that is why we haven't seen deflation over the past couple of years.

**Q: What is your view?**

**A:** If oil prices continue to go up and food prices continue to go up, that is not volatility, that is just inflation. But the Fed often looks at those more as a tax on the consumer that could actually slow growth down the road. We think that we could see

headline inflation running above core inflation for a long period, rather than headline just simply being volatile around core. That means consumer inflation over a long period is going to be higher than the measure that the Fed focuses on.

*(This interview was condensed and edited.)*

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### Bloomberg Brief Economics

Bloomberg LP

731 Lexington Avenue, New York, NY 10022

212-318-2000

**Newsletter** Ted Merz

**Executive Editor** [tmerz@bloomberg.net](mailto:tmerz@bloomberg.net)

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**Executive Editor** [dross@bloomberg.net](mailto:dross@bloomberg.net)

202-624-1881

**Economics** Jennifer Rossa

**Newsletter Editors** [jrossa@bloomberg.net](mailto:jrossa@bloomberg.net)

212-617-8074

*Nipa Piboontanasawat* [npiboontanasawat@bloomberg.net](mailto:npiboontanasawat@bloomberg.net) *Chris Kirkham* [ckirkham@bloomberg.net](mailto:ckirkham@bloomberg.net)  
+852-2977-6628 +44-20-7673-2464

**Staff Economists**

*Joseph Brusuelas* [jbrusuelas3@bloomberg.net](mailto:jbrusuelas3@bloomberg.net) *David Powell* [dpowell24@bloomberg.net](mailto:dpowell24@bloomberg.net)  
212-617-7664 +44-20-7073-3769

*Michael McDonough* [mmcdonough10@bloomberg.net](mailto:mmcdonough10@bloomberg.net) *Richard Yamarone* [ryamarone@bloomberg.net](mailto:ryamarone@bloomberg.net)  
212-617-7392 212-617-8737

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on the web at [www.Bloomberg.com/brief/economics](http://www.Bloomberg.com/brief/economics)

To contact the editors: [econbrief@bloomberg.net](mailto:econbrief@bloomberg.net)

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