Encouraging signs

by the St. Louis Post-Dispatch

It's too early to say for certain, but there are signs that the panicky U.S. credit market is beginning to get a grip. If so, most Americans should escape relatively unscathed from this month's financial anxiety attack.

One sign that things are calming down: Smart players are starting to look for bargains on Wall Street. The Bank of America, for example, agreed to invest $2 billion in the ailing Countrywide Financial, the nation's biggest mortgage company.

Slightly more than a week ago, an analyst at Merrill Lynch speculated that Countrywide could go bankrupt, dragged under by its investments in subprime mortgages. The firm's stock dropped through the floor, and the company confirmed it was laying off about 500 employees.

The Bank of America move gives it the equivalent of about a 16 percent ownership stake in the company, suggesting that the bottom hasn't fallen out of the mortgage business, that good borrowers still will be able to get loans, that lenders still can make money and that smart people are aware of all these things.

Gary Thayer, chief economist at A.G. Edwards, sees other signs that the crisis is easing a bit. Investors are starting to venture beyond ultra-safe Treasury bills and move back toward corporate bonds and other forms of debt. If things keep going as they are, Mr. Thayer said he thinks the credit crisis will produce only a slight hiccup in the economy's overall growth rate.

Even that scenario, however, would offer little comfort to the thousands of mortgage industry employees who have lost their jobs - 20,000 in this month alone. And borrowers who got subprime mortgages for too much money and who face ballooning interest rates already are struggling to hold onto their homes.

Last week the Congressional Budget Office was in synch with Thayer's perspective, projecting a 1.9 percent economic growth rate this year.

The real worry, of course, is a broad panic that would freeze lending of all sorts reaching well beyond the mortgage industry and create the possibility of a recession. The investments that have lost much of their value and marketability are bonds backed by packages of subprime mortgages, but they're held by financial institutions of all sorts, making it difficult to be sure which companies might end up in trouble.

That has made the bond market nervous, and if such concerns spread far enough, the debt market can get

bogged down and even good borrowers would have trouble getting loans. Those consequences would ripple through the economy far beyond the housing industry, slowing business investment, causing layoffs and possibly bringing on a recession.

The economy seemed to be on the cusp of such a panic some three weeks ago. Since then, the Federal Reserve has shoveled money into the banking system to make sure there are funds available for lending, and it also has taken some subtler measures to keep credit flowing.

These efforts may have been enough to drag the credit markets out of their funk. If not, the Fed still has its biggest gun in reserve: a general cut in short-term interest rates.

Wall Street has been crying for just such a move to rescue its investments, but the Fed's boss, Ben Bernanke, has been moving cautiously, and rightly so. The Fed's job is to protect the overall economy, not reckless big-time investors.

Reprinted from the St. Louis Post-Dispatch - CNS

Encouraging signs by the St. Louis Post-Dispatch