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Week in Review: Stocks gain as investors watch central banks craft stimulus exit strategies

For the week ended March 19, 2010

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Investors watched this week as central banks and governments around the world struggled to craft exit strategies from massive stimulus measures now that the global economy has begun to expand. The U.S. Federal Reserve Board's commitment to keep rates low for the foreseeable future and Japan's move to expand its liquidity provisioning helped bolster risk appetite this week. Concerns that a European bailout of Greece may fall apart pressured markets. News that India unexpectedly raised its interest rates also sparked concern among investors who worried that withdrawal of stimulus measures would curb global growth.

In the United States, data signaled that the recovery was on track and drove the Dow Jones Industrial Average to a new 17-month intraday high on Friday and pushed the Standard & Poor's 500 Stock Index to its highest levels since September 2008.

U.S. economic news

Fed signals rates will remain unchanged; inflation stable

The Fed signaled this week that the recovery is not yet strong enough to stoke inflation or justify higher borrowing costs. While the central bank said it will end purchases of \$1.25 trillion worth of mortgage-backed securities, which has been one of its main supports for the U.S. economy, the Fed did indicate it will be at least several more months before it raises short-term rates from near-zero levels. News of tame inflation this week backed up the Fed's assessment. The cost of living was unchanged in February, restrained by rents and cheaper gasoline. The core Consumer Price Index rose 0.1% in February, capping the smallest gain since 2004.

Gradual improvement in the labor market

Last week, for the third week in a row, fewer Americans filed first-time claims for jobless benefits. Initial jobless claims were decreased by 5,000 in the week ended March 13. A sustained

increase in payrolls is still needed for consumer spending, which accounts for about 70% of the economy, to jumpstart growth. Other data this week included reports that the index of U.S. leading indicators, rose 0.1% in February, the smallest gain in almost a year and that manufacturing in the Philadelphia area expanded at a faster pace in March than February.

U.S. and global corporate news

Boeing said it would boost aircraft production amid an expected increase in demand. The news caused industrial stocks to rally on Friday. The company announced plans to increase production of its 777 and 747 aircraft earlier than expected amid increasing demand in the airplane industry.

Four **Rio Tinto Group** employees will stand trial in Shanghai on March 22, about nine months after being arrested on suspicion of bribery and stealing state secrets. The detention of the four strained relations between China and Australia and came a month after Rio Tinto rejected a \$19.5 billion investment from state-owned **Aluminum Corporation of China**. The company, also known as CHINALCO, is Rio's biggest shareholder.

Porsche forecast a second, consecutive-year loss because of the costs of its purchase of a majority stake in **Volkswagen** last year. The company reported that net income for the six months through January 31 fell 83%.

Global economic news

Greece pushes European Union for aid

Greek Prime Minister George Papandreou warned this week that Greece cannot hold out much longer if it has to keep paying current market interest rates. He set a one-week deadline for the European Union to craft a financial aid mechanism. If the E.U. cannot come up with such a solution, he said, he would have to seek aid from the International Monetary Fund. E.U. leaders have dismissed an IMF option, which they said would make it appear that the E.U. cannot resolve its own crisis. Greece needs to raise about \$14 billion to refinance bonds that come due April 20 and May 19. Investors this week were demanding that Greece pay three percentage points more than Germany on its three-year debt.

India unexpectedly raises rates

The Reserve Bank of India unexpectedly raised interest rates on Friday after inflation accelerated to a 16-month high. It was the first time since July 2008 that the bank has raised rates. In a surprise decision coming a month before the scheduled monetary policy meeting, the bank raised its benchmark reverse repurchase rate to 3.5%, from a record low of 3.25%, and the repurchase rate to 5% from 4.75%.

BOJ doubles lending program

In response to government calls to curb a deflationary trend that is thwarting economic recovery, the Bank of Japan doubled a lending program that is aimed at encouraging credit growth. The BOJ's move comes as other central banks around the world are withdrawing stimulus measures.

Signs of economic strengthening in United Kingdom

U.K. jobless claims unexpectedly fell in February at the fastest pace since 1987. The news, suggesting recovery is strengthening, provides a boost for Prime Minister Gordon Brown, who is seeking to convince voters that his Labour Party has the best plan for economic recovery.

Iceland's central bank, the Sedlabank, cut its benchmark interest rate, the seven-day collateral lending rate a half a point to 9% and its deposit rate to 7.5% from 8%.

Latvia's ruling coalition collapsed this week amid difficulties in carrying out the aggressive fiscal cuts that are needed to keep the country's program with the International Monetary Fund on track. The People's Party quit the ruling coalition after Latvian Prime Minister Valdis Dombrovskis refused to sign its proposal to shelve planned tax hikes.

Stay focused and diversified

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s: MA; cn: PB; nn: N1; sn: S1; pn: article/data/news/week_in_review; buid: ; time: 1269440038648