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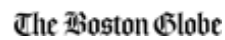
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Fear trumps hope on recession

Fed, administration look for quick \$150b stimulus as downbeat indicators send stocks plunging 300 points

By Robert Gavin

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Globe Staff / January 18, 2008

The Bush administration and Federal Reserve chairman Ben Bernanke agreed yesterday that the federal government should pump as much as \$150 billion into the faltering US economy, but it wasn't enough to stem recession fears that swamped investors and added to Wall Street's losing streak.

The Dow Jones industrial average plunged more than 300 points, falling to its lowest level in 10 months. The Dow, which closed at 12,159.21, has lost 2,000 points, or 14 percent, since peaking in October.

Sparking the sell-off was another round of poor economic data. Housing starts fell more than 14 percent in December and are now at their lowest level since 1991. A report from the Philadelphia Federal Reserve Bank showed manufacturing activity in its region contracting sharply, read by some analysts as another signal that the economy is heading for recession - if it's not already there.

"Investors are increasingly of the view that we're going to suffer a full-blown recession," said Mark Zandi, chief economist at [Moody's Economy.com](#), a West Chester, Pa., forecasting firm. "The economy contracted in December, and it feels like it's contracting in January, and once you start getting negative numbers, it's hard to get out of."

President Bush and Congress, however, are hoping that one way out is a stimulus package that would quickly put money into the pockets of low- and middle-income households as a way to jump-start consumer spending, which

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accounts for about 70 percent of economic activity in the United States. Consumers, battered by rising energy prices, plunging home values, and a weakening job market, are beginning to curtail spending, which could push the economy into a recession.

Bush is said to be considering a plan that would include rebates of \$800 for individuals and \$1,600 for families, as well as tax breaks for businesses buying equipment. Congressional leaders say the package could cost \$150 billion.

Bernanke, testifying before the House Budget Committee, said such stimulus, as long as it is temporary and doesn't widen the long-term federal deficit, could give the economy a needed boost. He reiterated that the Fed is ready to aggressively cut interest rates to stave off a recession.

Many analysts expect the Fed, which has already sliced its benchmark interest rate by a point since September, to cut another half-point when policy makers meet at the end of this month.

That would bring the rate to 3.75 percent, the lowest since September 2005.

Cutting interest rates lowers borrowing costs, encouraging consumers and businesses to spend. This time, however, cutting interest rates may not be enough by itself, analysts said. The still-sinking housing market is blunting the impact of lower rates, discouraging buyers and reducing equity that owners might tap to support spending.

That's why a stimulus package "is probably needed to avoid a full-blown recession," said Nariman Behravesh, chief economist at Global Insight, a Waltham forecasting firm. "It's unclear interest rates are going to do it alone, and it could provide an extra kick."

But not enough for investors. Bernanke's support of a stimulus package was read by some as more evidence the economy is deteriorating.



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Adding to the pressure on stocks have been weak corporate earnings and multibillion dollar losses by financial firms that held securities backed by defaulting subprime mortgages.

For example, [Merrill Lynch](#) & Co. yesterday wrote off nearly \$10 billion in losses in the fourth quarter alone, much of it related to the subprime mortgage meltdown.

Diane Swonk, chief economist of Mesirov Financial, a Chicago investment firm, said fear that more big losses are coming is sparking panic on Wall Street. Overseas, markets continued to plummet today, with Japan's benchmark Nikkei 225 stock index losing 387.67 points, or 2.8 percent, in morning trading.

The US economy, while weakened, still has some strengths.

The Labor Department reported yesterday first-time claims for jobless benefits, a key indicator of the labor market, fell for the third consecutive week and to their lowest level since September. At 301,000 last week, they are far below the 400,000 level that economists say signals a recession. In addition, falling interest rates and now a likely stimulus package will give the economy more support.

Among the reasons Wall Street is reacting so negatively: Many of the companies with the biggest problems are Wall Street investment firms.

"Perceptions become greater than reality," she said. "It's hard to see the forest for the trees when you're in the part of the forest that's burning."

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