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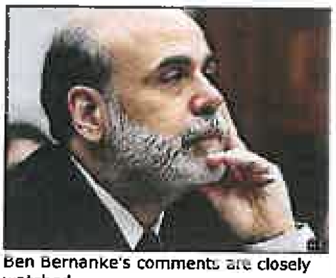
Fed warns of $100bn credit losses

Federal Reserve chairman Ben Bernanke has warned that the crisis in the US sub-prime lending market could cost up to $100bn.



Ben Bernanke's comments are closely watched

In a second day of testimony to Congress, Mr Bernanke said credit losses associated with sub-prime mortgage failures were "significant".

Wall Street is nervous about the exposure of banks and other lenders to the riskier sub-prime market.

Earlier this month, Bear Stearns bailed out two sub-prime focused hedge funds.

It has since said one of them has "very little value" and the other is now worthless.

Fears have grown in recent weeks that the downturn in the housing market, prompted by more people's inability to pay their mortgages, will cause instability and retrenchment in the wider economy.

But the June minutes from the Federal Reserve's rate-setting committee showed that despite the continued housing slump, inflation remained the central bank's overriding concern.

The decision to leave interest rates on hold at 5.25% was underpinned by fears that core inflation, stripping out volatile energy and food prices, would fail to recede.

Economists now expect rates to stay at that level for the rest of the year.

Downbeat note

In two days of testimony before US legislators, Mr Bernanke has sounded a persistently downbeat note on the state of the housing market and the woes of the sub-prime sector, which have led to the collapse of about 30 lenders.

"The credit losses associated with sub-prime have come to light and they are fairly significant," Mr Bernanke told a Senate Committee.

> **More than a million Americans lost their homes last year**
>
> Senator Robert Menendez

"Some estimates are in the order of between $50bn and $100bn of losses."

The Fed's handling of the sub-prime market, which it regulates, came under fire from senators, who argued it should have done more to protect vulnerable consumers from inappropriate and improper mortgage practices.

"More than a million Americans lost their homes last year," said Senator Robert Menendez.

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"In my mind, this is not just simply a time for suggestions, it is a time for solutions."

Mr Bernanke said the Fed was reviewing current regulations on lending practices in a "responsible" manner.

Wider problems?

The Fed remained "alert" for any signs that housing weakness may destabilise the economy as a whole, Mr Bernanke added.

It has already acknowledged the impact of reduced activity in the housing market on consumer spending, cutting its forecast for economic growth this year.

It has also said it expects the unemployment rate to rise from 4.5% to 4.75% by year-end.

The housing market has a cold and it is feared the germs may spread

Despite the impact of the crisis in the sub-prime mortgage market, the US economy has performed better in the second quarter of the year than the first.

The economy has continued to create new jobs at a healthy clip while the number of unemployment benefit claimants is now at its lowest since early May.

But the Conference Board, publishing its latest economic analysis on Thursday, said that it expected economic growth to slow in the next few months.

Worries over the economic outlook have not daunted investors, with the leading US share index, the Dow Jones Industrial Average, closing above 14,000 for the first time.

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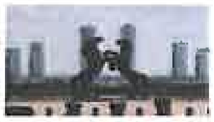
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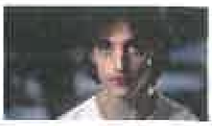
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