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Interest Rates Rise _ in the Markets

NEW YORK (AP) - A recent rise in interest rates has touched off a debate about how investors should react, and with the Federal Reserve about to weigh in, the hand-wringing will likely continue.

Some investors contend the run-up in interest rates -- the benchmark 10-year Treasury has risen about 35 basis points, or 0.35 percentage point, in about three weeks -- signals the bond market's concern that the economy is holding up better than expected. Bond investors have in part reacted to perhaps surprisingly strong data for the housing sector in recent weeks and this week greeted a mixed report on housing by focusing on the negative implications for fixed-income markets. Figures on existing home sales showed a drop in inventories for December, a development some said indicated a stabilizing of the housing market.

But rising interest rates could imperil the very recovery in housing that has some bond investors concerned. Rising rates, of course, would make buying a home more expensive.

Interest rates will consume Wall Street's attention next week when the Fed's Open Market Committee gathers for the first time this year at a two-day meeting that starts Tuesday. The central bank, in its bid to curb inflation by slowing the economy gradually, has left short-term interest rates unchanged at its last four meetings, a development that follows a string of 17 straight increases that began in 2004.

While investors expect the bank will stand pat on rates next week, the market will looking for clues on the Fed's subsequent moves.

"The Fed will not lower rates now because inflationary pressures are there and the economy is not falling out of bed," said Axel Merk, whose Merk Investments runs a fund that largely focuses on major currencies outside the United States.

"If you look at the 10-year rate, it has a huge implication for the housing market. It has become more expensive to buy a home now. We were spared that last year because we had extremely low long-term interest rates."

Peter Schiff, president of Europacific Capital Inc., who is bearish on prospects for the dollar and the U.S. economy overall, contends investors have misinterpreted recent economic data.

"Interest rates are rising and I don't think it is the result of signs of a strengthening economy. I think it's a greater perception that the housing market has a long way to drop."

He said a decrease in inventories of homes for sale reflects a slow market at this time of year and contends home owners have taken their properties off the market with plans to list them again in the spring and summer.

"The fact that inventories are down isn't a reflection of how many homes sold, it's a reflection of how many homes weren't sold."

Michael Gregory, senior economist at BMO Nesbitt Burns, believes higher-than-normal temperatures in parts of the country have tainted economic data.

"There is a legitimate debate going on in the markets because you've had unseasonably warm weather boosting up the data," he said, naming housing as one area that might be affected.

Ordinarily, fewer sellers list homes in the colder months and some construction work, including the building of homes, can slow.

Gregory said figures on employment and consumer spending could have been given a lift by temperatures that made people more likely to venture out. "The big question is, 'Are we going to get a bit of payback when the weather is more normal?'" He expects a soft patch in the economy that could follow an unusually strong winter and might lead the Fed to cut rates sooner than the markets now appear to expect.

He said an economic slowdown could spark a rally in the bond market and bring down yields, as prices and yields move in opposite directions.

"I think the market will price back in some possibility that the Fed could cut rates in the first half of the year."

"I think the key thing will be the wording of the statement on Tuesday," he said, referring to the Fed's widely anticipated comments following its meeting.