Fed keeps interest rates steady, sees inflation rising this year

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WASHINGTON (Reuters) - The U.S. Federal Reserve kept interest rates unchanged on Wednesday but said it anticipated inflation would rise this year, in a sign it is still on track to raise borrowing costs in March under incoming central bank chief Jerome Powell.

Citing solid gains in employment, household spending and capital investment, the Fed said it expected the economy to expand at a moderate pace and the labor market to remain strong in 2018.

"Inflation on a 12-month basis is expected to move up this year and to stabilize" around the Fed's 2 percent target over the medium term, the central bank said in a statement following a two-day policy meeting, the last under Fed Chair Janet Yellen.

The Fed also said its rate-setting committee had unanimously selected Powell to succeed Yellen, effective Feb. 3. Powell, a Fed governor who has worked closely with Yellen in recent years, was nominated by President Donald Trump and confirmed by the U.S. Senate.

Powell is not expected to dramatically change the policies embraced by Yellen, who spearheaded the move away from the near-zero interest rates adopted to nurse the economy back to health and spur job growth after the 2007-2009 recession.

Fed policymakers have been encouraged in recent months as the U.S. economy picked up speed and the unemployment rate fell to a 17-year low of 4.1 percent. The Fed repeated on Wednesday it expected "further gradual" rate increases will be warranted.

"The Fed left open the door for a March increase, but that's built in already," said Bruce Bittles, chief investment strategist at Robert W. Baird & Co in Sarasota, Florida.

U.S. stocks slightly extended gains immediately after the release of the Fed statement. Short-term interest rate futures showed traders were continuing to bet the Fed would raise rates three times in 2018, starting at its next meeting in March.

UPGRADED INFLATION VIEW

The Fed raised rates three times last year and currently projects three more increases this year even as it continues to trim its balance sheet on a largely pre-set schedule.

That gradual path of rate increases will hinge on a continued pickup in inflation, which has lingered below the Fed's target despite a strong job market.

In its statement, the Fed noted that market-based measures of inflation have increased in recent months despite remaining low.

The statement did not address the likely impact of the Trump administration's tax overhaul on economic growth.

Several Fed policymakers recently have said they expect the changes, which include an estimated $1.5 trillion in corporate and individual tax cuts, to provide an economic lift by boosting business and household spending.

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The U.S. economy grew 2.3 percent in 2017.

U.S. stocks have soared to record highs in recent weeks as investors calculated that corporate profits would rise after the passage of Trump's tax legislation.

There were no dissents in the Fed's decision on Wednesday.