WRAPUP 3-Fed's Lockhart says bar high to further easing

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* Lockhart won't rule out more easing but says bar is high
* Officials see growth picking up in second half
* Bullard worried about large balance sheet
* Fed policy currently highly accommodative (Adds comments, byline)

By Mark Felsenthal and Pedro da Costa

WASHINGTON, July 29 (Reuters) - The U.S. economy should pick up steam in the second half of the year despite a dismal performance in recent months, allowing the Federal Reserve to keep policy on hold for now, two top Fed officials said.

Against the backdrop of a congressional crisis over U.S. debt, both officials expressed a strong reluctance to take additional monetary easing steps, though they both agreed no options should be taken off the table.

Data on Friday showed the economy expanded a paltry 1.3 percent in the second quarter. Even worse, the first quarter's reading was revised down sharply to an annualized 0.4 percent -- dangerously close to contraction.

Growth may have been damaged in July by continued uncertainty over the debt limit, which is risking the prospect of a once-unthinkable U.S. ratings downgrade.

Saying he had not given up hope for a stronger second half following dismal growth data for the first and second quarters published on Friday, Atlanta Fed President Dennis Lockhart said he was in a wait-and-see mode with regards to policy.

"While at present I do not see much risk of another outright recession, I don't think we can dismiss the possibility that we're in a persistent slow-growth recovery," Lockhart told the Third Annual Rocky Mountain Economic Summit.

If growth picks up as he expects, Lockhart said, then the Fed would begin unwinding its extraordinary monetary support to the financial system late next year.

"If, however, I come to conclude that we're in a world that portends a long period of very weak growth, high unemployment, and painful structural adjustment, the much-anticipated policy normalization may have to be rethought."

Lockhart's counterpart at the St. Louis Fed, James Bullard, said he was worried about the inflation risks posed by the Fed's large balance sheet, which was expanded sharply to a record $2.8 trillion in response to the financial crisis.

The Fed cannot buy Treasury debt directly and would not be able to intervene to prevent a default, Bullard said.

"If it led to a generalized crisis we can come in and provide liquidity to markets as we did in 2008 and 2009," he said. "But the Fed doesn't have any ability to fix this situation."

Bullard is viewed as a centrist and Lockhart is seen as somewhat more of a growth-focused dove along the spectrum of Fed officials' views.
The next meeting of the Fed's policy-setting Federal Open Market

Committee is scheduled for Aug. 9, but neither official is a voting member of the panel.

The U.S. central bank in June ended a second round of quantitative easing and indicated it will watch developments in the economy for a while before taking any further steps.

Since the Fed has already cut interest rates to near zero and bought a cumulative $2.3 trillion in assets over two installments to boost growth, the central bank's choices are limited if it decides more stimulus is necessary.

Some analysts believe the Fed would be most likely to bolster its promise to maintain a large balance sheet or a long period of very low rates.

Bullard and Lockhart said that headwinds facing the economy in the first half of the year are already beginning to moderate and should allow the economy to grow more quickly.

"I think we're in better shape for better growth in the second half of the year," Bullard said. (Editing by Chizu Nomiyama and Kenneth Barry)