# WE HAVE LIFT-OFF

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The result of today's FOMC meeting may have been the worst kept secret from the policy makers I've seen in my career. In a widely telegraphed move, the Fed raised the target range for Fed Funds by a quarter point, to 0.25%-0.50%. This rate hike represented the first increase since December 2018, which was probably one of the more 'stop and go' rate hike cycles in recent memory. Now that we finally have the much awaited lift-off, the question becomes, what will this rate hike cycle look like?

Up until Russia's invasion of Ukraine, it appeared as if this rate hike episode would be kind of straightforward. Inflation continued to run white-hot, and the Fed was way behind the curve. In other words, the voting members had a lot of catching up to do, and the money and bond markets were moving toward the possibility the Fed could raise rates at just about every FOMC meeting that remained this year and then follow up with additional hikes in 2023.

Without a doubt, the Fed is facing a number of conundrums as they embark on this rate increase cycle and that has resulted in concerns about overly aggressive increases that could adversely impact the economy. As I noted in last week's blog post, it is important to put U.S. monetary policy into some proper perspective. With today's rate hike, the Fed moved Fed Funds off of *zero*, but by only 25 basis points (bps). In addition, the Fed just wrapped up their latest quantitative ease (QE) program, where the policy makers bought an incredible $4.6 trillion in Treasury and MBS securities. Think about that number for a minute. QE1, QE2 and QE3 purchases all added up to bring their total securities holdings to about $4.25 trillion over a six-year period (2008-2014). The just-completed QE4 surpassed that total in just two years.

Why is this important? Because the Fed has only just begun to remove the emergency measures designed to offset and guide the financial markets and economy through a once-in-a-generation pandemic. There is a loooong way to go before monetary policy will enter restrictive territory.

It is this precise backdrop the Fed appears to be embracing, while also acknowledging geopolitical risks, as well. As of this writing, barring a stock or funding market meltdown sparked by the Ukraine crisis, the policy makers appear poised to raise rates at their next three FOMC meetings (May 4, June 15 & July 27), at a minimum. Don't forget, balance sheet run off could also commence later this spring.

**Conclusion**

Whether the voting members decide on a 50 bps rate hike at some point or raise rates at every meeting this year, the Fed tightening cycle has only just begun. It could easily run its course over the next two years, and perhaps even into 2024. Thus, preparing your portfolio for this type of rate outlook is not really a short-term tactical move, but rather a strategic asset allocation decision.

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## DEFINITIONS

**Federal Open Market Committee (FOMC)** : The branch of the Federal Reserve Board that determines the direction of monetary policy.

**Federal Reserve** : The Federal Reserve System is the central banking system of the United States.

**Federal Funds (Fed Funds)** : Excess reserves that commercial banks and other financial institutions deposit at regional Federal Reserve banks

**Rate Hike** : refers to an increase in the policy rate set by a central bank. In the U.S., this generally refers to the Federal Funds Target Rate.

**Inflation** : Characterized by rising price levels.

**Basis point** : 1/100th of 1 percent.

**Quantitative Easing (QE)** : A government monetary policy occasionally used to increase the money supply by buying government securities or other securities from the market. Quantitative easing increases the money supply by flooding financial institutions with capital, in an effort to promote increased lending and liquidity.

**Balance sheet** : refers to the cash and cash equivalents part of the Current Assets on a firms balance sheet and cash available for purchasing new position.