CAPITAL VIEW INVESTMENT GROUP

Advisors with D.A. Davidson & Co. member SIPC

Quarterly Newsletter

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What does our current interest rate environment mean for your money?

It's hard to believe that the first quarter of this year has already come and gone – but we hope 2023 is off to a great start for you!

The Federal Reserve, or central bank of the United States often referred to as "The Fed", has been busy over the past 12 months aggressively raising interest rates as a mechanism to try and bring down the soaring inflation that the United States hasn't experienced in over 40 years.

When the Fed raises interest rates, it is important to understand how that can impact your money. With this in mind we have highlighted 4 issues to consider during this rising rate environment:

1. Rising rates means lower bond prices.
2. Rising rates often means volatility for stocks.
3. Rising rates means debt is even more expensive.
4. Rising rates have made cash and cash equivalent investments more attractive.

1. Lower Bond Prices – But Higher Yields

Bonds are typically thought of as a ballast to offset much of the market risk associated with stocks, but 2022 proved to be a unique year where investors saw negative returns in both stocks and bonds. Why is that? This is because interest rates and bond prices are inversely correlated, so as The Fed has been raising interest rates to try and bring down inflation, bond prices have been falling as a result. However, while bond prices have been falling, yields have been rising. A recent article from Capital Group highlighted, "The yield on the Bloomberg U.S. Aggregate Index, a widely used benchmark for investment-grade bond markets, was 4.25% as of January 25, 2023. That compares to 1.75% on December 31, 2021." (Source: Capital Group, "3 reasons why 60/40 portfolios may make a comeback, February 2, 2023.) While we expect the Fed to incur a few more interest rate hikes in 2023 and know that bond prices may subsequently fall a bit further – we believe the brunt of the interest rate increases are now in the rearview. With the dramatic rise in yields, fixed income has become much more attractive over the past several months.

2. Volatility for Stocks

In many cases, higher interest rates spells volatility for the stock market. This is because businesses (represented by stocks) tend to borrow less money when it becomes more expensive to do so. When this happens, often a company's earnings will grow slower than anticipated. The impact of this is felt most among Growth stocks, such as technology companies – where growth projections are often reduced in a rising rate environment, which negatively impacts the stock price. Value stocks on the other hand, particularly dividend paying stocks, typically weather the storm better during this kind of market environment – though that is not to say that they are immune to volatility.

3. Debt Is Even More Expensive

Rising interest rates also means that the cost of borrowing money in any form is more expensive – whether that is through auto loans, mortgages, home equity lines of credit or credit cards. The interest rates on all of these forms of debt have increased over the last year. We recommend taking an inventory of any debt you have, particularly if the rate of interest is variable, as it has likely increased steadily over the past several months. We advocate paying down these debts, especially if they have been acquired during this rising rate environment.

4. Cash and Cash Equivalent Investments are More Attractive

The silver lining to all of this is that increasing interest rates means just that – any interest bearing account is now paying you more for your money. As of the writing of this newsletter, 6-month Treasury Bills are yielding 5.11% as shown on Bloomberg's website (Source:https://www.bloomberg.com/markets/rates-bonds/government-bonds/us.) and 1-year CD's are yielding up to 5.35%. For conservative securities, these are very attractive rates that have not been seen in many years. We encourage you to contact us to discuss taking advantage of these investment vehicles.

Bottom Line

The rising interest rate environment we find ourselves in presents both challenges and opportunities. We expect that over time inflation will come down, the Fed will adjust rates accordingly and the stock market will rally once again. Our view is that a well-diversified portfolio is the best way to position assets for long term investing. Please do not hesitate to reach out if you have any questions or would like us to review your financial plan and goals.

Best Regards, Mark, Brad T., Drew, Brad H., Renee & Erin

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