GLOBAL FINANCIAL
Private Capital
COMPREHENSIVE WEALTH MANAGEMENT

Stop the Madness

SYNOPSIS

- Financial news networks are addicted to the rising interest rate story, but the timing of the first interest rate hike since 2006 is meaningless to a long-term investor.
- The real concern is the velocity of subsequent rate hikes, but the Fed will most likely go very slow over the coming years.
- The reality of the current rate environment is that we will be dealing with lower rates for longer, and a single rate hike is not enough to get us back to the days of easy income.

THE ADDICTION TO RISING INTEREST RATES

It's time for us all to stop focusing on when the Fed will raise interest rates. Turn on any financial news network these days, and it seems as if these shows can't go an hour without talking when the Fed will ultimately move rates up for the first time in almost a decade.

The pundits and forecasters are addicted to this subject because most market watchers are under the assumption that with an interest rate hike comes volatility, and the media loves volatility because more people watch the news during times of heightened market moves (oh and more people watching the news means more advertising dollars for the networks).

In my opinion, there are few subjects out there at the moment that are more irrelevant to a long-term investor than the timing of this first rate hike, yet I get asked daily on the subject.

My answer is the same as it was a year ago, and that is I have absolutely no clue when rates will rise. I still don't think that Janet Yellen even knows for sure, so how could I possibly have some edge here to exploit?

Now, do I think rates belong at zero? Absolutely not and I have argued that Fed policy is one of the reasons why our economy has taken so long to heal. However, the Fed's army of economists probably does not subscribe to my *Thought for the Week* or read my blog, so I position investments under the caveat that I must play by their rules.

In doing so, I ask myself if the timing of an interest rate hike when rates are at zero matters at all, and the answer is unequivocally "no." I am not a day trader, so volatility, which is nothing more than a measure of emotion in markets, does not scare me.

Interest rate hikes are almost always used as a tool to dampen inflation, which is a byproduct of a fast-growing economy. Hence, if the Fed is preparing to raise rates, then it means that inflation is rising, and if inflation is rising, then our economy is growing (most of the time). If the economy is growing, then corporate earnings should be increasing. This logic trail leads to one conclusion – own equities.

For the sake of argument, let's assume for a minute that it is possible to time such events, but I'm just no good at it. Well then how have others' predictions fared? Take a look at the track record because here's the funny thing about interest rate commentary - it's almost all wrong.

Name one market pundit, sell-side analyst, economist, or anyone else on the news who has accurately predicted the path of interest rates over the last two years. All you have to do is go back to 2014 to see that the overwhelming majority of those on TV networks and those paid millions of dollars every year to do uber-intensive research got the call on rates dead wrong.

Now, will the Fed inject some volatility into markets when they finally raise interest rates for the first time since 2006? Probably. Maybe. Actually I have no idea. Predicting emotional responses in financial markets is a useless exercise.

However, if we see and fear-induced selloff in equities, then I will welcome it with open arms because I love to see stocks go on sale for absurd reasons. Stocks selling in the face of a growing economy is almost always a value investor's dream come true.

IMPLICATIONS FOR INVESTORS

Rather than ask yourself *when* rates will rise, long-term investors are better suited trying to determine *how far* and *how fast* the Fed will move over time. Meaning, the velocity of rate hikes is what really matters, and this is where I see the ability to position a portfolio.

The Fed is acutely aware of the situation they have put us all in, and they know that if they were to move rates up too quickly, then they risk driving us back into a recession. Therefore, they will most likely move rates at an incredibly slow pace, especially with inflation below their 2% target, so investors should stay positioned for a low interest rate environment for much longer.

But don't just take my word for it. Stanley Fischer, the Fed's Vice Chairman and second in command behind Janet Yellen, was quoted in a Bloomberg article earlier this week:

> *When it comes to describing how the Federal Reserve will exit the zero-rate era, "liftoff" is all wrong, says Vice Chairman Stanley Fischer. The term, dear to investors and headline writers, "is the most misleading word you can imagine," he said on Monday in Toronto.*
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> *"Liftoff says we're going straight up with the interest rate," Fischer said during a question-and-answer session after a speech on financial crises. "Well, we're going up with the interest rate, then along, and then another little jump. That's not liftoff, that's crawling."*
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> *Source: http://www.bloomberg.com/news/articles/2015-06-01/fischer-rejecting-liftoff-says-rate-rises-will-be-crawling*

The difference here is that my strategy is not predicated upon the *timing* of a singular market event but rather the direction *over time*. Said another way, I am not placing a bet on when the rate hike will occur but rather on the environment that will likely persist for years.

The bottom line is that the madness simply must end, and what makes for good TV programming typically does not align well with investment advice. The timing of the first rate hike since 2006 is irrelevant to a long-term investor, so ignore the stories in the press about rising rates because they provide no value at all.

Instead, position your portfolio to operate in a low interest rate environment because even if the Fed were to raise rates tomorrow, we are still going to be here for a while.

Sincerely,

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