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AWAITED RATE HIKE AND A ROILING MARKET

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Ahead of the Federal Reserve meeting on Wednesday, June 15, investors sent the S&P 500 into bear market territory, meaning the index fell over 20% from recent records.[1] Volatility gripped markets as concerns arose that the Fed would need to fight stubborn inflation with more aggressive rate hikes.[2]

Indeed, on June 15th Fed officials decided to hike rates by 75 basis points (0.75%), the largest such increase since 1994.[3] The hike helps to reinforce the Fed's inflation-fighting credibility, according to Barclays economists,[4] and some believe the Fed will raise rates by another 75 basis points in July.[5]

This short article will cover some of the context around this rate hike, and what you need to know about what lies ahead.

The Inflation Surprise—And Fed Response

Despite some signs of slowing inflation last month,[6] on June 10th the Labor Department reported that the Consumer Price Index (CPI) increased 8.6% for the year ending in May, its largest 12-month growth rate since December 1981.[7] The CPI measures household spending on goods and services.

We think it's safe to say that this number took a lot of people by surprise. As Fed Chair Jerome Powell told The Wall Street Journal in an interview last month, "What we need to see is clear and convincing evidence that inflation pressures are abating and inflation is coming down. And if we don't see that, then we'll have to consider moving more aggressively."[8]

At this point, the Fed has made that pivot. After the last rate hike of 50 basis points (0.5%) in May, Chair Powell said the Fed wasn't "actively considering" a hike of 75 basis points.[9, 10]

Even just last week, expectations for a three-quarters of a percentage point hike were just 3%.[11] However, in the days since this new CPI data became public, the market quickly repriced expectations to predict exactly such a hike, with 95% odds.[12]

As of this writing on Wednesday afternoon, markets have welcomed the Fed's decision, with stocks maintaining gains for the day.[13] However, this month's sharp selloff is a stark reminder of how quickly expectations can turn on a dime. We would not be surprised to see volatility continue as we navigate a challenging time in both economic and geopolitical history.

Should this change your long-term outlook? We consider periods of volatility and uncertainty when developing financial and investment plans. Inflation pressures mean that you use lose money not just when markets are volatile, but also when maintaining your funds in cash. Your buying power is diminished as goods become more expensive and thus it is also imperative to find investments that can provide a hedge against inflation. We know it can be difficult to absorb all this news—to that end, please do not hesitate to give us a call or schedule an appointment to talk through your questions, your portfolio, and any concerns you might have.

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The S&P 500 Index is an unmanaged, market value-weighted index of 500 stocks generally representative of the broad stock market.

CPI - The Consumer Price Index is a measure of the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services. Indexes are available for the U.S. and various geographic areas. Average price data for select utility, automotive fuel, and food items are also available.

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