SCHLINDWEIN ASSOCIATES
INVESTMENT COUNSEL

# Revisit

In its attempt to lower inflation, the Federal Reserve has raised its policy interest rate target to the highest level in 17 years. Much has occurred in economies and markets over this long stretch of time, including the Great Recession and the pandemic-induced, worldwide downturn. Four U.S. presidents have occupied the White House, and three chairpersons have led the Fed. Overall, it has been a period characterized by historically low interest rates. How has this low-rate regime impacted the fortunes of workers and investors? A review of trends in key indicators can provide perspective for economic activity and investing ahead.

## PERSPECTIVE

On May 3, the Federal Reserve raised the target for its policy interest rate for the tenth time in fourteen months. The new range, 5% - 5¼%, brought the rate back to a level last reached in May 2006. The trajectory of this increase was much steeper than that of the earlier period. Chart I shows the divergent paths of the policy rate from higher to lower levels and back again. Also visible is the extended period of "zero interest rate policy" which dragged the average rate over the whole period down to 1.2%. In contrast, the rate averaged 4.6% over the full 69 years of its data history. In addition, historical high and low quartile levels for the rate were 6.3% and 1.8% respectively. This has been a truly unusual policy rate experience.

The Federal Reserve's mandate has been to achieve maximum employment and inflation at the rate of 2% over the longer run. The inflation objective was achieved until recently. Chart II tracks the unemployment rate. Notable increases in the rate correspond with periods of economic contraction. Over the 74-year history of data, the unemployment rate has averaged 5.7% with high and low quartile levels of 6.8% and 4.4% respectively. Before and now after the pandemic-induced economic contraction, the unemployment rate reached notably low levels. While different measures such as average hours worked and average hourly wages can bring more context to the assessment, the period of low policy rates has been favorable for workers.

Albeit with notable corrections along the way, stock prices moved higher over the past two decades as shown in Chart III. Lower interest rates supported this uptrend both by facilitating corporate growth and by raising the price multiple assigned to corporate earnings. Total return (dividends plus price appreciation) for the Dow Jones Industrial Average was a respectable +9.3% per year. While economic contraction was a proximate cause of the most recent bear markets, interest rate levels played more a secondary role. The impact on business activity and stock markets from the most recent rise in rates remains a work in progress with modest adversity to date.

## INVESTMENT IMPLICATIONS

While the Federal Reserve policy rate now has revisited a 17-year high, general conditions for economic activity, employment and stock markets remain favorable at this time. Inflation rates have trended lower but are yet to reach policy objectives. One clear difference is the level of bond yields, 3.4% for a 10-year U.S. Treasury today versus 5.0% twenty years ago. Uncontrollable market uncertainties highlight the wisdom of revisiting investment goals, time horizons and risk tolerances at any time to remove uncertainties for that which can be controlled.

CHART I

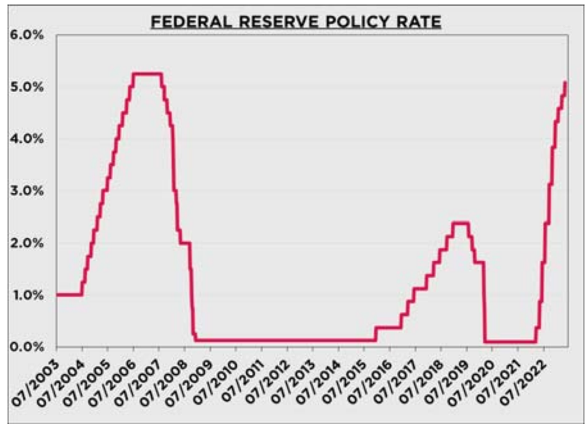


CHART II

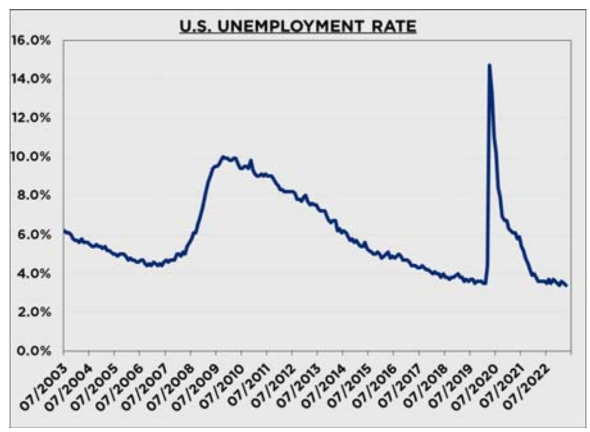


CHART III