

# FED RATE HIKES AND LONG-TERM PORTFOLIOS

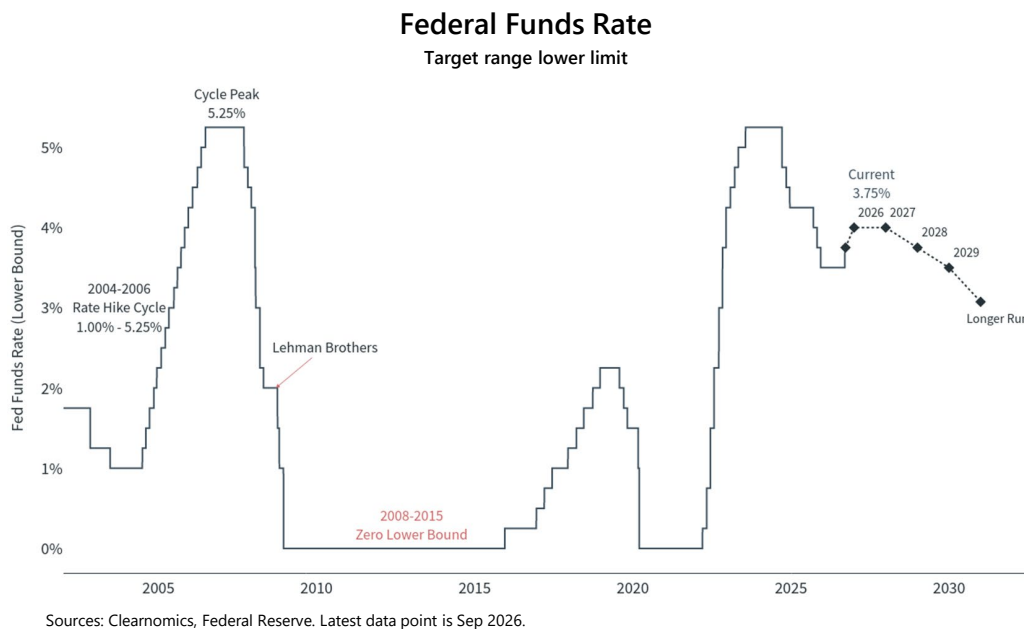
*The Fed's latest rate hike was primarily in response to inflation. What perspectives do investors need to understand how the Fed impacts markets and the economy?*

Much like the common cold, which has to run its course while we treat the symptoms, many economic problems lie beyond the reach of the Fed's tools. Monetary policy is meant to help ease challenges in the job market and inflation, but in practice the Fed does not control the economy directly - it responds to it. Today's primary challenge is stubborn inflation, driven largely by higher oil prices as the war in Iran continues and the closure of the Strait of Hormuz drags on. Interest rate policy cannot resolve these geopolitical issues, but the Fed can try to keep inflation from spreading beyond energy into other categories that affect consumers and businesses. How does seeing the Fed through this lens affect long-term investors and their portfolios?

## The Fed's latest rate hike was anticipated by investors

At its September meeting, the Fed raised policy rates by one-quarter of a percent, to a range of 3.75% to 4.00%. This was the first hike in three years and followed a period of rate cuts from September 2024 to December 2025. Because the decision was widely anticipated, markets took it in stride overall despite some swings immediately after the announcement.

What makes this hike different? The Fed is mostly reacting to higher energy prices, with oil still around \$100 per barrel. Economists call this "cost-push inflation," where supply disruptions lead to higher prices, as opposed to "demand-pull inflation," where an overheating economy drives excessive consumer demand that pushes prices higher.



In 2022, the economy experienced both: low interest rates and government stimulus fueled demand, while the pandemic and Russia's invasion of Ukraine caused supply shocks. Policymakers typically view supply shocks as temporary since they eventually resolve, and oil prices did fall until this year's geopolitical events.

Over the past few cycles, the Fed has preferred steady, well-communicated policy changes, a practice known as "forward guidance." New Fed Chair Kevin Warsh prefers to avoid this approach and has declined to submit his own forecasts to the Fed's quarterly Summary of Economic Projections.

Instead, his goal is for markets to react to the underlying data rather than to what the Fed will do next, which is one reason investors expected this hike with over a 90% probability before the meeting. Right or wrong, this makes data on the labor market, inflation, and growth even more important. While inflation remains higher than many would prefer, unemployment is still historically low and GDP growth has been steady.

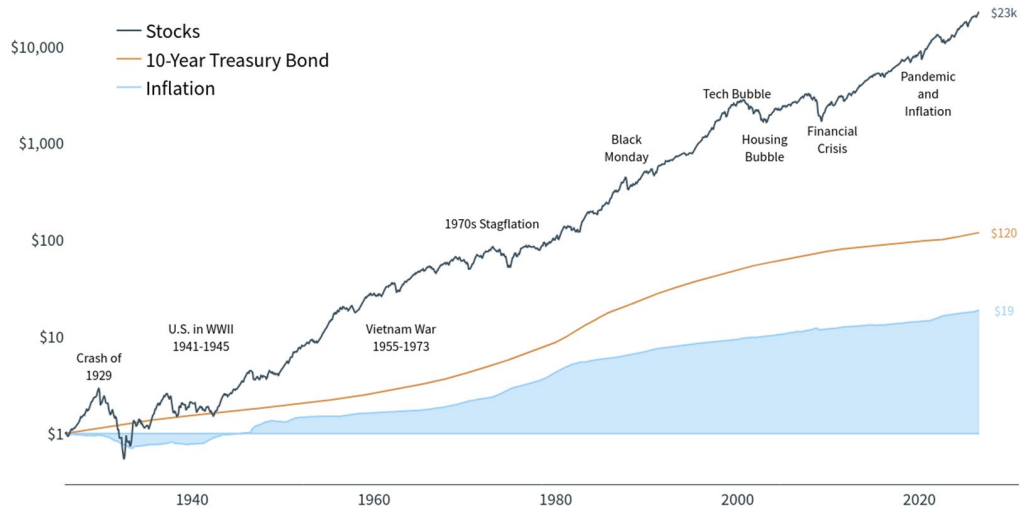
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## Rate hikes are a normal part of the economic cycle

This is one reason the Fed only raised rates by 0.25%. Projections from other Fed officials suggest one more hike later this year before a pause through 2027, with rates declining only slowly after that — a change from their June forecasts, which called for lower rates. These figures should be taken with a grain of salt, since they can change quickly from meeting to meeting depending on economic trends.

### Growth of \$1 Since 1926

S&P Composite total returns, 10-Year Treasury bond, and inflation (log scale)



Sources: Clearnomics, Robert Shiller, Standard & Poor's, BLS. Latest data point is Jul 2026.

It's understandable that some investors view higher rates as negative for markets, but that depends on why the Fed is raising them. It's not at all unusual for markets and interest rates to move higher together, especially later in the business cycle.

A growing economy and strong corporate earnings can support both rising stock prices and a Fed that is trying to keep inflation in check. Over the past six months, the S&P 500, the Dow Jones Industrial Average, and the Nasdaq have all moved toward new all-time highs, supported by strong earnings and the buildout of AI data centers, even as interest rates have risen to multi-decade highs.

There is also a misconception that the Fed's role is to fine-tune the economy, a view partly created during Alan Greenspan's tenure from the late-1980s to the mid-2000s, when the Fed's decisions were opaque. In practice, the Fed is more often reacting to events than sitting comfortably in the driver's seat. The chart above shows how rate hikes have played out across many different environments, often over long cycles.

## Staying invested is the best way to address inflation in the long run

Ultimately, investors care about Fed policy and interest rates because of the impact on their portfolios and financial plans. While the Fed attracts a great deal of attention, its decisions are only one part of the picture.

The accompanying chart shows how financial markets have supported investors over the past century despite countless Fed decisions, economic shocks, recessions, and geopolitical challenges. Inflation pushed costs higher by 19 times over this period, so what cost \$1 in 1926 now costs \$19. Even so, stocks and bonds both significantly outpaced inflation, helping those who stayed invested generate income and build wealth over time.

Of course, markets never move in straight lines, and investors should always be prepared for uncertainty. This is why maintaining an appropriate portfolio that reflects long-term financial plans remains more important than trying to predict or time the Fed's next decision.



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