

Investor Update: Two Key Points About the Fed's Rate Hike



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Much of the chatter about yesterday's interest rate hike by the Federal Reserve overlooks two key points. First, over the past 61 years, stocks have tended to rise during the 12-month period following the first rate hike. Secondly, it's different this time.

Put asterisks by both of those statements.

I'll start with the reassuring news. As we discussed in the **December AAI Dividend Investing report**, first rate hikes have been followed by higher stock prices over the following 12 months. Stocks have particularly risen when a rate-tightening cycle was started in response to economic growth. In the six 12-month periods starting in 1954 with core inflation at levels that TIAA-CREF characterized as low, stocks rose four times. Stocks rose every time when core inflation was low, bond valuations were high and interest rates were first raised.

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AAII Model Portfolio Update

There are no rule changes to the Shadow Stock Portfolio, but an adjustment was made to the section on stock order guidance. Previously, when the need for liquidity was discussed, it was suggested that the average daily dollar volume of a stock should be at least four times the size of the position you wish to create. AAI founder and chairman James Cloonan now feels that this should be increased to 10 times the desired position size.

For example, if you wish to establish a position of \$10,000 in a stock, then you should restrict choices to stocks with average daily volume equal to at least \$100,000. This will make getting in and getting out of the stock much more efficient. Along those lines, James Cloonan requires an average

daily volume of \$300,000 for the stocks selected for the Model Shadow Stock Portfolio. This is why the number of stocks passing Cloonan's screen is less than the number of stocks that qualify under the basic rules.

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- **Follow the Fed, but Be Smart About It** - Returns for large-cap and small-cap stocks are lower, but still positive, during the full period of restrictive monetary policy.
- **Don't Fight the Fed: Interest Rates and Their Impact on the Stock Market** - S&P Capital IQ market strategist Sam Stovall said in this 2009 article that the S&P 500's average 12-month gain following a first rate hike was 6.2%.
- **Will the Rate Hike Change How You Invest?** - Tell us on the AAll.com Discussion Boards.

AAll Sentiment Survey

Pessimism jumped to its highest level since September, while optimism fell to its lowest level since July. [More about this week's results.](#)

This week's results:

- Bullish: 23.9%, down 4.6 points
- Neutral: 36.8%, down 4.9 points
- Bearish: 39.4%, up 9.5 points

Historical averages:

- Bullish: 39%
- Neutral: 31%
- Bearish: 30%

Take the [Sentiment Survey](#).

What's Trending on AAll

1. [The Individual Investor's Guide to Personal Tax Planning 2015](#)

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3. **How Interest Rate Changes Affect the Price of Bonds**

The Week Ahead

The U.S. stock exchanges will close early, at 1:00 p.m. (Eastern), on Thursday. The U.S. financial markets will be closed on Friday in observance of Christmas. Our offices will be closed on Thursday and Friday (December 24 and 25), and there will not be an Investor Update sent next week. On behalf of everyone at AAIL, I wish you a merry Christmas.

Dow component Nike (**NKE**) will report its quarterly results on Tuesday. Joining Nike will be fellow S&P 500 members Cintas Corp. (**CTAS**) on Monday and ConAgra (**CAG**), Micron Technology (**MU**) and Paychex (**PAYX**) on Tuesday. These will likely be the last earnings reports from S&P 500 companies released in 2015.

On the economic calendar, November existing home sales and the second revision to third-quarter GDP will be released on Tuesday. Wednesday will feature November durable goods orders, November personal income and spending, November new home sales and the University of Michigan's final December consumer sentiment survey. Weekly initial jobless claims will be released on Thursday, as usual.

The Treasury Department will auction \$13 billion of two-year floating-rate notes on Wednesday.

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