TIME

# Why a Rate Hike Is an Indicator of a Healthy Economy

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Forget about your brackets in the March Madness pool. The surest bet this month has been that the Federal Reserve would raise interest rates at next meeting. And it did, boosting the federal funds target rate to 1% from 0.75% on March 15.

It's now a lock, as the bookies say, that rates will continue to climb this year. The bookies in this case are the futures traders who have pegged the chances of another rate increase at 88%. Federal Reserve Chair Janet Yellen nearly screamed it out in a recent speech: "We currently judge that it will be appropriate to gradually increase the federal funds rate if the economic data continue to come in about as we expect."

After eight years of limbo-low interest rates, why the rush to raise, which triggers higher rates in just about everything else financial? And why would a guy who is heavily invested in the rate-sensitive real estate business when he's not President want to preside over such a move?

Because at this point a rate rise is an indicator of a healthy economy. For the Fed's purposes, that means we're close to full employment and prices are under control. "This is the patient at the hospital front desk being released," says Tom Siomades, head of Hartford Funds Investment Consulting Group.

The hospital bill has to be paid, though: as interest rates float upward, you will be seeing rising costs for mortgages, car loans and credit-card debt which is currently north of 16%. Home mortgages, which are tied to the 10-year Treasury note, have been rising steadily to a recent 4.38% average nationally. That will make owning a home more expensive, one of the reasons home sales are heating up as buyers try to lock in rates. For downsizers looking to cash in, it's become a good time to make the move. For first-time home buyers, on the other hand, the math is getting a little tougher.

Among the clear winners will be savers, who have been suffering for years. Whether they are retirees, people nearing retirement or those who are just parking cash for later on, the rate increase will boost the paltry yields on CDs and money-market accounts. According to Crane Data, the average rate paid by the top 100 money funds is 0.5%, but it's expected to jump to 0.75%. That certainly may not seem significant, but when you consider that these accounts hold some $2.6 trillion, the move means an additional $675 million in interest flowing from banks into savers' pockets on an annualized basis.

And according to Morningstar, investors seeking less risk shifted $412 billion into fixed-income instruments, even as bond prices fell, which happens as interest rates rise. It's a bit counterintuitive that people are going into bonds, but by pushing more into short-duration bonds, asset managers can reinvest in higher-yielding notes fairly quickly as rates rise.

That's happening even as the post-election Trump bump sent the S&P up about 10%. It raises the question of whether the stock market, goosed by the President's proposed fiscal and regulatory policies, may soon suffer some jitters. "Investors are really high on the fumes that everything Trump promises is going to come through," says **Bernard Baumohl, chief global economist at the Economic Outlook Group.** "If it doesn't, you could see a capitulation." By promising lower taxes, relaxed regulations and a muscular $1 trillion infrastructure program, the Trump Administration has stoked expectations to what Goldman Sachs CEO Lloyd Blankfein calls a "growthier" environment. But uncertainty over whether the President can actually execute those plans consider the hurdles the White House is facing as it tries to replace Obama care could cause the market to pause.

In raising rates, the Fed is declaring that the recovery from the Great Recession and what a wimpy one it turned out to be is finally history. At the same time, once it has raised rates, the Fed can then resort to its traditional toolbox a rate cut if the economy gets wonky again.

More broadly, the news is good for retirement savers. We have economic growth, income growth and job growth, and inflation is behaving as the Fed desires, reaching its 2% target. It means that America is getting back to normal. The one caveat to consider is that in Washington, D.C., normal left town a long time ago and doesn't figure to be back anytime soon.

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