What Impact Would Tighter Monetary Policy Have on Your Investments?

A new president is about to take office. Successful investors will be the ones who anticipate how the next administration and congress will affect the economy and how the various factors at play will affect investments. In the case of Trump and a Republican controlled congress we expect tax cuts, an attempt to bring corporate cash back from overseas and increased spending on U.S. infrastructure. If these plans come to fruition there will be at least short and medium term stimulus to the economy. A predictable result will also be increased interest rates, namely a tighter monetary policy. The value of the dollar will rise versus other currencies. Our concern today is what impact would tighter monetary policy have on your investments? Bloomberg writes about the outlook on the **Fed, Trump and the dollar**.

> *PKO Bank Polski, which topped Bloomberg's overall accuracy rankings for the final quarter of 2016, sees the dollar's rise pushing the euro to 95 U.S. cents or even lower by the end of June, a level not seen in 15 years. That's the lowest call for the pair among 53 forecasters, according to data compiled by Bloomberg.*
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> *The forecast is based on the prospects of a tighter monetary policy from the Federal Reserve, coupled with markets expecting President-elect Donald Trump's fiscal measures to "translate into higher growth and inflation," said Jaroslaw Kosaty, the chief FX strategist at the bank, Poland's biggest.*

Will the impact of tighter monetary policy be solely because of a stronger dollar? How will inflation be affected if the Fed does not raise rates rapidly enough?

How Fast Will the Fed Hike Rates?

The Federal Reserve has been criticized by some, including the incoming president, for moving too slowly to raise interest rates. Now one of the Fed's members calls for **faster interest rate hikes** according to *Reuters*.

> *Boston Fed President Eric Rosengren on Monday called for the U.S. central bank to step up its pace of interest rate increases from the once-a-year pattern it has pursued since 2015, warning of inflation risks if it does not.*
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> *"I expect that appropriate monetary policy will need to normalize more quickly than over the past year," Rosengren told the Connecticut Business and Industry Association.*

At 4.7 percent, unemployment is at a level that is sustainable over the long run, he said, and inflation is on track to reach the Fed's 2 percent target by the end of this year. If the unemployment rate falls further, he said, inflation could overshoot that target, "which would place the economic recovery at risk."

Tighter monetary policy in the form of higher interest rates may come sooner rather than later. This will drive up the interest that your CDs earn at the bank and the rates on US Treasuries. It will hopefully forestall inflation but if the Fed does not act fast enough the value of your savings will be eroded. Companies that export will be hurt as international sales fall off. And, if Trump starts a trade war, all bets are off and you may just want to convert everything to cash and put it under your mattress!