22 September, 2022

# U.S. Fed again hikes interest rates by 75 bps in aggressive bid to fight inflation

**Key Highlights:**

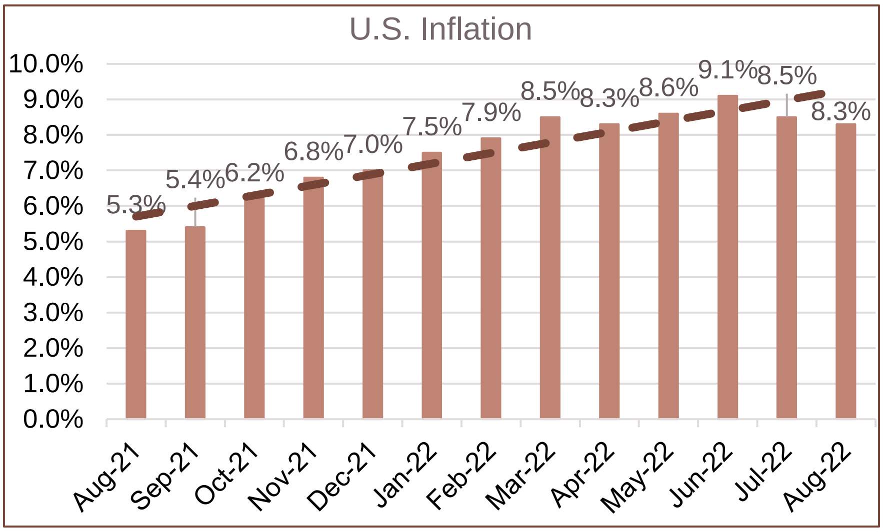
- The U.S. Federal Reserve **raised its target interest rate by 75 bps to a range of 3.00%-3.25%.**
- **This is the third straight 75 bps hike** in this rate hike cycle.
- FOMC members see further rate hikes this year and next, with **no cuts until 2024.**
- The Dot Plot **Projections for interest rates - 4.40% at the end of 2022 & 4.60% at the end of 2023.**

## Current Update:

- In line with market expectation, the Federal Reserve on Sep 21, 2022 once again **raised interest rates by 75 bps** and indicated it will keep hiking well above the current level.
- The U.S. policy makers voted unanimously to lift their key rate to a **target range of 3.00% to 3.25%**.
- In its effort to lower inflation which is near its highest levels since the early 1980s, the central bank took its interest rate up, **the highest it has been since early 2008.**
- Powell said the indicated path of rates showed the Fed was "strongly resolved" to bring down inflation from the highest levels in four decades and that officials would "**keep at it until the job is done**" even at the risk of unemployment rising and growth slowing to a stall.
- The Fed said that "recent indicators point to modest growth in spending and production," but **the new projections put year-end economic growth for 2022 at 0.2%, rising to 1.2% in 2023, well below the economy's potential.**
- The **unemployment rate in August 2022 at 3.7% and is projected to rise to 3.8% this year and to 4.4% in 2023**.

## U.S. Inflation peeking:

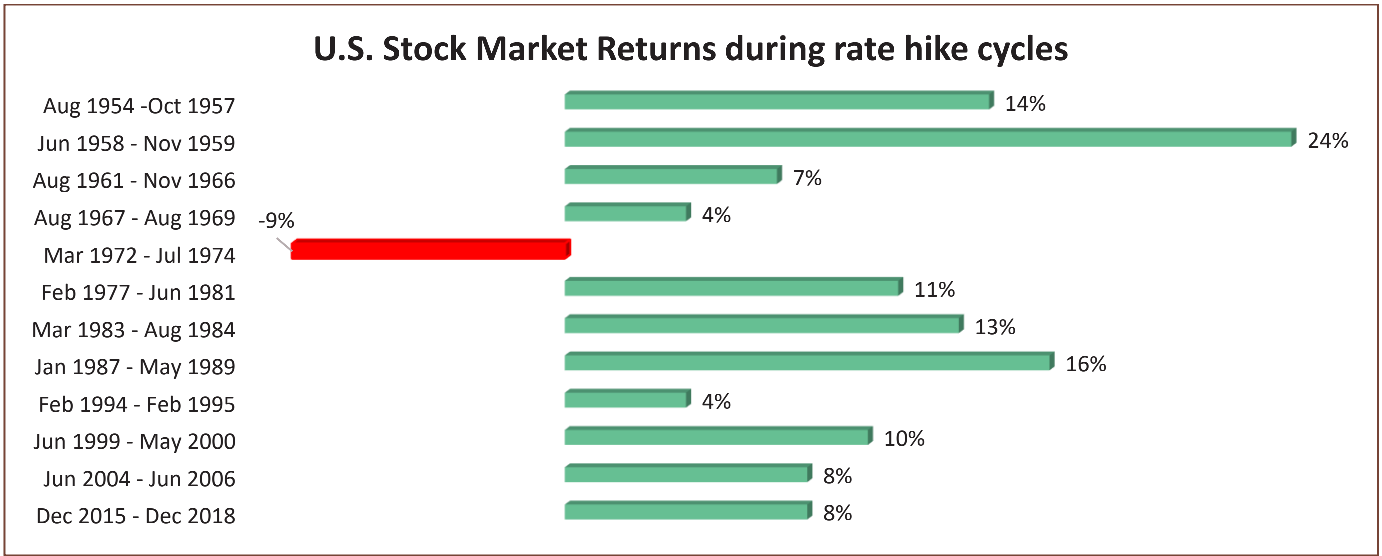
- Recent inflation data has shown little to no improvement despite the Fed's aggressive tightening.
- The **new projections put it on a slow path back to 2% in 2025.**
- US consumer price index peaked at 9.1% Y-o-Y in June but it failed to come down as quickly in recent months as Fed officials had hoped. In August, it was still 8.3%.



**Impact on Markets:**

- In reaction to the hawkish stance of the Fed, the U.S. equities, **S&P 500 shed 1.71% to 3,789.93,** and the **Nasdaq Composite slumped 1.79% to 11,220.19 on Sep 21, 2022**.
- **Indian shares fell on Sep 22, 2022, in line with Asian peers, while the rupee hit a record low 80.38 against U.S. dollar in early trade on Sep 22, 2022.**
- The benchmark **Indian 10-year government bond yield rose to 7.27% levels in the early session on Sep 22, 2022**. On the previous day, it had ended at 7.23% levels.

**History of 12 U.S. rate hike cycles have proven that the S&P 500 has risen by an average annualised rate of 9.4%**




*Source: Moneycontrol Returns less than one year are absolute and greater than one year are CAGR*

**To Conclude:**

In India, the rising U.S. interest rates present challenges for the RBI Governor as inflation in the domestic market is showing signs of receding. When the Fed raises its policy rates, the difference between the interest rates of India and the U.S. narrows. This makes emerging countries such as India less attractive for the currency carry trade. **Market expects the RBI to hike rates further in the upcoming policy meet scheduled on Sep 30, 2022.** The interest rate differential between India and the U.S. is to attract dollar at a time when India is expected to witness a record current account deficit. Further, a weakening rupee will put pressure on inflation via higher cost of imported goods and services.

We believe **Global equity markets, including the Indian markets will stay volatile for the time being, till the rate hike cycle continues globally amid Ukraine & Russia conflict, and its effect on global inflation**. With further rate hike are on the cards for most of major developed economies across the world fear of **"stagflation"** are at their highest since the onset of the Great Recession in 2008.

**Investment Approach:**

Investors should not try to time the market and **investors should follow the desired asset allocation** to avoid unfavourable portfolio outcomes in case of any volatility that flows in the Indian markets due to tapering.

22 September, 2022

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