The FED Indicates It May Get Aggressive with Interest Rate Hikes, Cutting Balances

April 7, 2022 - The FED has come under some significant pressure to start raising interest rates in order to combat inflation. That process actually started at the last FED meeting which resulted in 25 basis point increase in rates (NOTE: 25 basis points = 1/4 of 1%). But many of the members of the FED board of governors weren't really happy with a response that timid, and indications are that they will be a lot more aggressive in future meetings. Beyond that, the minutes of their last meeting also show that they were in agreement on cutting their monthly balance sheets significantly; both on bond purchases and mortgage-backed securities. These moves will both help and potentially hurt consumers. How you will be impacted really depends upon how you plan to spend your money. Here is what you need to know.

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It is clear from the meeting minutes that with regard to interest rates, many of the members of the FED Board of Governors want to raise interest rates again by 50 basis points at their next meeting. And they are taking the point of view that this could just be the beginning. With regard to their balance sheet cuts, they have agreed already to scale back their bond purchases by $60 Billion per month, and their mortgage-backed securities purchases by $35 Billion a month. This will be implemented over the next three months.

All of this will have a very real impact for consumers. It means that there will be less money in the system overall. That's good if your goal is to drive down inflation. In a normal economy, these changes could have a fairly immediate impact on consumer prices. Unfortunately, while the FED may have some control over inflation being caused by too much money in the system, nothing they do will have an impact on energy prices, and those prices are responsible for a large portion of the inflation we're currently experiencing. The bottom line here is that the interest rate hikes may prevent inflation from getting worse, their impact will be limited by policy decisions made by the Biden administration.

Interest rate hikes will also negatively impact many consumers. Those with large credit card balances and other forms of variable rate loans will start to see their payments rise on a monthly basis. And anyone shopping for a loan will find that the amount they qualify for will go down while the amount they will have to pay for that loan will go up.

This is likely to be doubly true for anyone shopping for a home. That's because not only are interest rates increasing but, as previously noted, the FED is decreasing its purchases of mortgage-backed securities. In plain English, that means that getting a home loan is about to become more difficult and more expensive at the same time.

In addition to consumer concerns, these changes will also impact businesses and any plans they may have that involve

the use of credit. Plans for expansion may have to be placed on hold. And any expansions that do take place will certainly be more expensive.
Hang on folks. It's going to be a bumpy ride.

by Jim Malmberg
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