December, 2016

Dear Valued Investor:

The Federal Reserve's (Fed) policy-making arm, the Federal Open Market Committee (FOMC), raised its target for the federal funds rate by 0.25% (25 basis points) yesterday as expected at the conclusion of its two-day meeting. By raising this key overnight borrowing rate, the Fed raised interest rates for the first time in 2016, and for just the second time since the Great Recession (the last time the Fed raised rates was December 2015). The Fed raised rates because it believes economic growth has picked up and should continue without the added support of very low interest rates. Although market participants largely expected this outcome, the big story in yesterday's meeting is that the FOMC now expects to raise rates three times in 2017. At the September 2016 FOMC meeting, the Fed expected just two hikes in 2017, and the market and the Fed were aligned on that assessment before yesterday.

Fed Chair Janet Yellen emphasized, "Our decision to raise rates…[can] certainly be understood as a reflection of the confidence we have in the progress the economy has made and our judgment that progress will continue and the economy has proven to be remarkably resilient. So it is a vote of confidence in the economy."

Yesterday's rate hike was well telegraphed, and the fed funds futures market had been pricing in a nearly 100% chance of a hike for some time. Though the potential for some bond market volatility in the short term exists, I don't expect another broad-based bond sell-off (or a corresponding quick rise in rates) given that markets have had plenty of time to digest the possibility of a rate hike.

For the stock market, this decision is potentially positive as well. Stocks have historically done well during periods of rising but low interest rates, as higher rates tend to be accompanied by improving expectations for economic growth. I am encouraged by LPL Research's recent review of 23 periods of rising rates, during which the S&P 500 rose 83% of the time.* Yet, rate hikes also reaffirm that we are in the mid-to-late stage of the economic cycle. In this part of the cycle, we can expect additional equity market volatility.

Now that a rate hike has occurred, many of us have questions about the pace of future rate hikes. The FOMC noted that it expects the pace of rate hikes to be gradual and that any future hikes will be data dependent and not on a preset course. Fed Chair Janet Yellen confirmed this strategy during her post-meeting press conference. And our view remains that the economy, labor market, and inflation will track to—or perhaps just above—the Fed's forecasts for 2017, suggesting at least two 25 basis point hikes in 2017 are likely and quite possibly three.

Yesterday's rate hike reaffirms that we are returning to a more typical economic environment, which is a welcome change from the environment we have lived in since the Great Recession. And although we have seen another change in Fed policy, what shouldn't change is our commitment to the long-term investment goals that may ultimately be our blueprint for success.

As always, if you have any questions, I encourage you to contact me.

Sincerely,

Rick Fisher, CFP®

IMPORTANT DISCLOSURES

**See Weekly Market Commentary: Can't Stocks and Bond Yields Just Get Along? (December 12, 2016)*

The economic forecasts set forth in the presentation may not develop as predicted.

The opinions voiced in this material are for general information only and are not intended to provide or be construed as providing specific investment advice or recommendations for any individual security.

The Federal Open Market Committee (FOMC) is the branch of the Federal Reserve Board that determines the direction of monetary policy. The eleven-person FOMC is composed of the seven-member board of governors, and the five Federal Reserve Bank presidents. The president of the Federal Reserve Bank of New York serves continuously, while the presidents of the other regional Federal Reserve Banks rotate their service in one-year terms.

This research material has been prepared by LPL Financial LLC.

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