

# Interest Rates and Market Returns

## Don't Fear the Fed



The Federal Reserve (Fed) raised interest rates a total of 425 basis points (bps) in 2022 over a span of seven meetings — 25 bps in March; 50 bps in May; 75 bps in June, July, September and November; 50 bps in December — and has continued into 2023. Fed tightening is viewed by many investors as a negative for the capital markets and while the lead up is often accompanied by an increase in volatility — as has been the case this time — many investments have, on average, moved higher after the uncertainty is removed and the first rate hike is in the books.

### SELECT ASSET CLASSES: AVERAGE TOTAL RETURN FOR PERIODS FOLLOWING FIRST FEDERAL RESERVE RATE HIKE\*

Asset Class	Index	6 Months Following	12 Months Following	18 Months Following	24 Months Following
<b>US EQUITIES</b>					
US Large-Cap Equities	S&P 500	2.46%	9.83%	10.12%	8.55%
US Mid-Cap Equities	S&P Midcap 400	1.68	11.24	14.77	11.29
US Small-Cap Equities	S&P Smallcap 600	2.36	14.19	15.16	11.04
Dividend-Paying Equities	Dow Jones US Select Dividend	0.84	3.35	10.77	12.82
US Growth	Russell 3000 Growth	4.59	15.26	11.88	7.93
US Value	Russell 3000 Value	0.03	4.10	8.86	9.02
<b>FIXED AND ALTERNATIVE INCOME</b>					
High Yield Bonds	ICE BofA US High Yield Index	0.87	4.06	4.49	5.08
Investment Grade Bonds	Bloomberg US Aggregate Bond Index	-0.17	3.90	4.87	5.15
Municipal Bonds	ICE US Broad Municipal Index	-0.62	3.73	5.03	5.25
Preferreds	S&P Preferred Stock	4.84	9.87	7.59	4.34
Real Estate Investment Trusts (REITs)	S&P United States REIT	1.82	10.16	11.37	14.39
<b>INTERNATIONAL EQUITIES</b>					
Emerging Market Equities	MSCI Emerging Markets	8.83	17.71	14.45	10.67
International Equities	MSCI ACWI ex-US	6.73	14.45	12.77	8.12
<b>OTHER</b>					
Commodities	Bloomberg Commodity	3.59	13.15	15.75	11.56

Over the shorter-term, international equities led the way, as not all Central Banks move in tandem.

Longer-term, small/mid cap US equities, dividend-paying equities, commodities and REITs closed the gap.

With most periods showing average positive total returns, our key take-away is one that we believe investors should always remember: *It's time in the market, not timing the market, that builds long-term wealth.*

 Highest average returns for each period

\*As of 2/28/2023. For this table, a tightening cycle is defined as two or more hikes to the Fed Funds Rate in a 12-month period. Since 1990, there have been five occurrences with initial rate hikes on 2/4/1994, 6/30/1999, 6/30/2004, 12/15/2016 and 3/17/2022. The returns shown are averages for the tightening cycles (as applicable), with a significant range in returns for some asset classes. Return for US Small-Cap Equities does not include the 2/4/1994 cycle; the Preferreds returns do not include the 2/4/1994 or 6/30/1999 cycles — index data was not available during these periods. The direction and absolute level of interest rates are only one of many factors that drive investment returns.

Data source: MorningstarDirect and <https://www.federalreserve.gov/monetarypolicy/openmarket.htm>. Returns are cumulative for all periods shown. **Past performance does not guarantee future results.** It is not possible to invest directly in an index. Above returns are not indicative of any AAM product.

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Visit [www.aamlive.com](http://www.aamlive.com) or contact a financial professional to discuss potential opportunities in a rising rate environment.

**All investments involve risk; principal loss is possible. Risks:** An investment in common stocks should be made with an understanding of the various risks of owning common stock, such as an economic recession and the possible deterioration of either the financial condition of the issuers of the equity securities or the general condition of the stock market. The value of a company's preferred stock will react more strongly than bonds and other debt to actual or perceived changes in the company's financial condition. Preferred stock is subject to the risks that a company may defer or not pay dividends, and, in certain situations, may call or redeem its preferred stock or convert it to common stock. Fixed income securities are subject to certain risks including, but not limited to: interest rate risk (changes in interest rates may cause a decline in the market value of an investment); credit risk (changes in the financial condition of the issuer, borrower, counterparty, or underlying collateral), prepayment risk (debt issuers may repay or refinance their loans or obligations earlier than anticipated). Market risk, or systematic risk, is the risk that results from the characteristic behavior of an entire market or asset class. The prices of international securities may be more volatile than the securities of US issuers because of economic conditions abroad, political developments, and changes in the regulatory environment of foreign countries; these risks are more pronounced for investments in issuers in developing or emerging market countries. Investments in small- and mid-cap companies involve greater risks including increased price volatility compared to the market or larger companies. Declines in real estate values, changes in interest rates, economic downturns, overbuilding and changes in zoning laws and government regulations can have a significant negative effect on companies in the real estate industry, including REITs.

**Index Definitions:** **S&P 500 Index** is an unmanaged market capitalization weighted index used to measure 500 companies chosen for market size, liquidity and industry grouping, among other factors. The **S&P MidCap 400 Index** is designed to measure the performance of 400 mid-sized companies. **S&P SmallCap 600®** seeks to measure the small-cap segment of the U.S. equity market. The index is designed to track companies that meet specific inclusion criteria to ensure that they are liquid and financially viable. Both the S&P 400 and S&P 600 are separate and distinct from the S&P 500 Index. The **Dow Jones US Select Dividend Index** is an unmanaged index of 100 stocks used to measure performance of dividend-paying US equities. The **Russell 300® Index** measures the performance of approximately 3,000 stocks and includes all large-cap, midcap and small-cap US equities, along with some microcap stocks. The combined market capitalization represents approximately 98% of the value of all US equities. The **Russell 3000® Growth Index** measures the performance of the broad growth segment of the US equity universe. It includes those Russell 3000 companies with relatively higher price-to-book ratios, higher I/B/E/S forecast medium term (2 year) growth and higher sales per share historical growth (5 years). The **Russell 3000® Value Index** measures the performance of the broad value segment of the US equity universe. It includes those Russell 3000 companies with relatively lower price-to-book ratios, lower I/B/E/S forecast medium term (2 year) growth and lower sales per share historical growth (5 years). **ICE BofA US High Yield Index** tracks the performance of US dollar denominated below investment grade corporate debt publicly issued in the US domestic market. The **Bloomberg US Aggregate Bond Index** is an unmanaged, broad based index composed of US dollar denominated, investment grade, fixed rate taxable bonds with at least \$250 million par amount outstanding and at least one year to final maturity. The **ICE US Broad Municipal Index** tracks the performance of over 58,000 investment grade tax-exempt municipal bonds representing over \$1.6 trillion in total market capitalization. **S&P US Preferred Stock Index** is designed to measure the performance of the US preferred stock market. Preferred stocks pay dividends at a specified rate and receive preference over common stocks in terms of dividend payments and liquidation of assets. The Index is comprised of U.S. traded preferred stocks that meet criteria relating to minimum size, liquidity, exchange listing, and time to maturity. The index is weighted by total market capitalization, subject to a single issuer weight cap of 10%. The **S&P US REIT Index** is a free-float adjusted, market capitalization-weighted index that defines and measures the investable universe of publicly-traded real estate investment trusts domiciled in the United States. The **MSCI Emerging Markets Index** is designed to represent the performance of large- and mid-cap securities in 27 emerging market countries and covers approximately 85% of the free float-adjusted market capitalization in each country. The **MSCI ACWI (all country world index) ex-US** is designed to capture large and mid cap representation across 22 of 23 developed market countries (excluding the US) and 27 emerging market countries and covers approximately 85% of the global equity opportunity set outside the US. **Bloomberg Commodity Index (BCOM)** reflects commodity futures price movements and is calculated on an excess return basis. The index rebalances annually weighted 2/3 by trading volume and 1/3 by world production and weight-caps are applied at the commodity, sector and group level for diversification. Roll period typically occurs from 6th-10th business day based on the roll schedule.

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