Weekly Commentary **October 16, 2015**

JEREMY SIEGEL .com

Enough of the Fed! Slow Growth and Low Inflation Keeps Rates Low

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At last Tuesday's Democratic nominee debate, Bernie Sanders exclaimed "Enough of Hillary Clinton's Emails!" I am ready to say the same about the Fed. All market discussion now centers on "Will They or Won't They" raise the funds rate on December. Let me reiterate my opinion. It would be best if they gave us a 25 bp raise in December wrapped in very dovish language, such as: "We will be very patient in assessing the impact of this raise on the economy and financial markets before considering another hike in the funds rate." I think the financial markets – both bond and stock markets – would react favorably to such a declaration. As a veteran market watcher, I have come to appreciate how negative uncertainty, and especially policy uncertainty is for market sentiment. The Fed has not raised rates in over 9 years and few traders want to commit funds in advance of such a move. However, if the Fed does hike and investors see that the world does not end, this would be positive for the financial markets, and particularly for income-generating stocks which have been held back by the reluctance to commit before the first hike.

All said, in the big picture, whether the Fed hikes now or early next year matters little. 25 basis points on the short end of the curve will change the cost of capital by very little. Yellen was perfectly correct when at the press conference that followed the September meeting, she said the path of the future funds rate is far more important than when the Fed starts raising rates. Investors should monitor what is happening to the economy and inflation, and here it looks like more of the same. The sharp fall in unemployment claims to a 39-year low last week signals that the job market is still strong (although it is still too early to get a read on the November 6 labor report). Yet GDP growth last quarter looks like a measly 1.5% and only about 2.5% this quarter. Furthermore, the PPI index shocked on the downside on Wednesday; although yesterday's CPI numbers came in at, or in the case of core inflation, slightly above average. Nevertheless near-zero headline inflation (and outright deflation at the producer level) along with slow GDP growth negate any significant hike in interest rates. This is the positive that the equity market can hang onto despite the decline in 2015 earnings. The next FOMC meeting is two months from today. There will be a lot more data flowing over the dam before a decision is reached. Hopefully the Fed can move to reduce market uncertainty before the holidays.

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