

Impact of Impending Rise of Interest Rates

James Bullard, President of the Federal Reserve Bank of St. Louis, recently predicted an increase in interest rates during the first quarter of 2015. Although some opinions regarding interest rates may vary, the general consensus seems to point to 2015. An increase in rates serves the ultimate purpose of maintaining stable and low inflation in the long-run. While rates are expected to rise gradually, bankers and consumers will certainly feel an eventual impact.

An increase in interest rates could cause some issues for the average consumer. Individuals that currently have variable-rate debt will likely feel the biggest impact. Those with significant debt in credit cards, adjustable-rate mortgages, or other forms of debt with a floating interest rate will have to pay even more to eliminate their debt. Rising rates will also likely tighten up the bank accounts of many, which will decrease the average consumer's willingness to take on debt in the form of loans. While banks would certainly like to see a greater return on each individual loan they issue, the increasingly rising reluctance of consumers to take on loans is of concern for bankers. Ultimately, rates aren't expected to rise to a rate that would be of major concern to bankers, so the banking industry's concern is greatly limited.

An increase in the Fed Funds Rate could also have an indirect impact on the stock market. Consumers aren't the only ones taking on loans from banks; most businesses also use bank loans as a means of financing. Rising rates will make consumers and businesses more reluctant to spend. If companies choose not to spend as much money, their opportunity to expand is greatly damaged. This reluctance to expand will often cause a decrease in profits,

which will often cause stock prices to fall. Struggles in the stock market would cause issues across the board. The Federal Reserve would greatly lessen the risk of these issues occurring by making the rise in rates gradual, which is expected.

Some consumers may also actually benefit from a rise in rates. Those individuals that continuously practice safe money-saving strategies by putting their money in savings accounts will start to see higher returns. Money that is invested in savings accounts today will hardly see any return, if any, but if interest rates eventually rise to two or three percent, those returns will be much more significant. With interest rates being expected to rise in the near future, the practice of “safe investing” will become much more profitable.

Even though rising interest rates can and likely will cause headaches for a wide range of consumers, this looming trend should not be solely viewed as a bad thing. An increase in rates indicates the Federal Reserve is confident in the current conditions of the country’s economy. Although highly unlikely, if rates were to increase rapidly to a rate above the norm, then concern would be more warranted. The historically low rates of the last six years are unheard of in this country’s history; therefore, shifting back to the norm is a good sign. Ultimately, rising interest rates should serve as a strong indication that the Great Recession of the new millennium is behind us.

-Joe Thouvenot

Bio: Thouvenot is a junior and finance major in the Romain College of Business at the University of Southern Indiana. He is a member of Omicron Delta Epsilon, an international honors society for economics. Thouvenot is expected to graduate with an honors diploma in May of 2016.