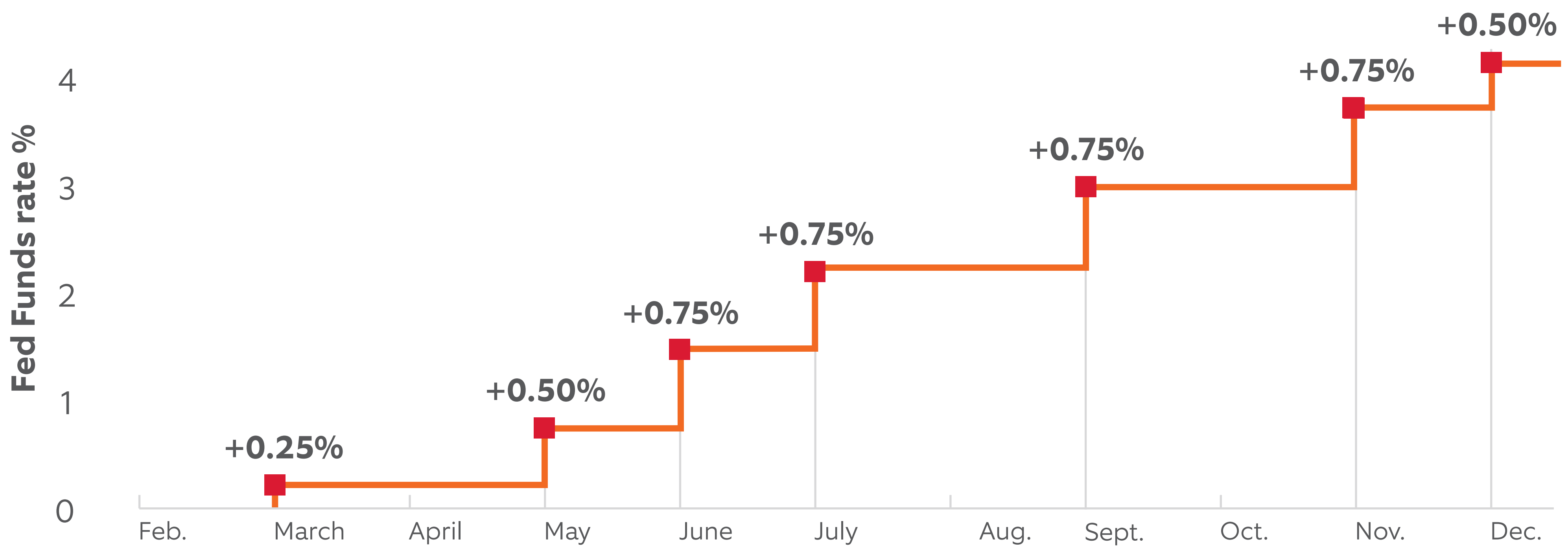
Where to Invest When Rates are Rising

Look to asset classes that have responded strongly after previous rate hikes, including high-yield bonds, value stocks, natural resources and more.

The Federal Reserve's seven interest rate hikes in 2022 sparked a period of intense market volatility and fears of a potential recession. As a result, it's not surprising that investors may be increasingly concerned about mitigating the risks in their portfolios against the impact of high inflation.

2022 Interest Rate Hikes



Source: U.S. Federal Reserve

It can be instructive to examine how asset classes have performed during earlier rising rate environments. We examined four previous Fed rate hike cycles (1994, 1999, 2004, and 2015) and identified areas of opportunity for investors when interest rates are rising.

Fixed Income: Consider High-yield Bonds

High-yield bond returns were double the returns of investment grade bonds during the past four Fed rate hike cycles. During the rate hike cycles of 2004 and 2015, high-yield bonds even outperformed equities.[1]

Average return during past four Fed rate hikes[2]

Equities: Look at Factors and Natural Resources Stocks

Higher growth stocks may be more volatile in rising-rate environments. In contrast, value stocks, higher-quality stocks, stocks featuring strong dividend yield, and stocks of companies in natural resources industries have delivered strong returns during rising rate cycles.

Average one-year returns during the past four Fed rate hikes[3]

Value	Quality	Natural Resources	Dividend yield	U.S. equities
10%	9.7%	25%	8.8%	6.8%

Not all rising-rate environments occur against the same macroeconomic backdrop, so the past success of any of these asset classes does not necessarily mean they will outperform today.

For more insights, read our article on preparing portfolios for rising interest rates.

1 Bloomberg. Comparison of the MSCI USA Index performance and the Bloomberg High Yield 2% Capped Index returns for two full year time frames of 2004 and 2015. Indexes are unmanaged and cannot be invested in directly. Index performance does not reflect any fees or expenses. Performance of an index is not illustrative of any particular investment. Past performance does not guarantee future results.

2 Bloomberg. Comparison of the Bloomberg Aggregate Bond Index (Agg) performance and the Bloomberg Barclays High Yield 2% Capped Index returns for four full year time frames of 1994, 1999, 2004, and 2015. Indexes are unmanaged and cannot be invested in directly. Index performance does not reflect any fees or expenses. Performance of an index is not illustrative of any particular investment. Past performance does not guarantee future results.

3 Bloomberg. Comparison of the MSCI Barra "Value" factor index versus the MSCI USA Index performance returns for four full year time frames of 1994, 1999, 2004, and 2015. Northern Trust & Bloomberg. Comparison of the Northern Trust "Quality" factor index versus the MSCI USA Index performance returns for four full year time frames of 1994, 1999, 2004, and 2015. Northern Trust & Bloomberg. Comparison of the MSCI Barra "Dividend Yield" factor index versus the MSCI USA Index performance returns for four full year time frames of 1994, 1999, 2004, and 2015. Indexes are unmanaged and cannot be invested in directly. Index performance does not reflect any fees or expenses. Performance of an index is not illustrative of any particular investment. Past performance does not guarantee future results.