What Will Rate Cuts Mean For You?

For the first time in four years, the Federal Reserve has cut short-term interest rates. The Fed has indicated that this cut may be followed by several others in the months ahead. What will these lower rates mean to you as a consumer and an investor?

Let's first look at the potential impact on your purchasing abilities. Generally speaking, rate cuts should be good news for consumers who need to borrow — which basically includes all of us. Keep in mind, though, that a lowering of interest rates will affect some types of loans and debt faster than others. For example, you might start seeing lower rates on car loans more quickly than you will on credit cards. And since credit card rates are already quite high, they'll likely remain so even after the Fed's actions. Still, any decline will be welcome, and your best bet will be to shop around for a card that offers the most favorable rates, along with other features, such as a good rewards program.

If you're looking to buy a home or refinance an existing one, you should also benefit from lower interest rates. One big problem, of course, is that housing prices are likely to remain high for the foreseeable future because of the shortage of homes on the market. Nonetheless, if you took out a mortgage for a higher rate in the past few years, you may be able to save some money by refinancing, though you'll have to weigh all the factors involved, such as closing costs. Other types of housing-related loans, such as home equity loans and adjustable-rate mortgages, are closely tied to market interest rates, so you may see some movement in these areas before long.

Now, let's turn to what lower rates might mean to you as an investor. Lower interest rates typically are good for the stock market. One reason for this is because it's cheaper for businesses to borrow money to expand their operations, which ideally will lead to greater profitability, and corporate profits are still a key driver of stock prices. But the picture isn't quite that simple because not all market sectors benefit equally from lower interest rates.

Lower rates may also help you if you own bonds. You may see their value increase as interest rates fall because other investors will be willing to pay more for your bonds and earn the higher rate they offer. Long-term bonds in particular often benefit the most from falling rates because they lock in higher yields over time. On the other hand, some savings vehicles, such as certificates of deposit (CDs), may become less attractive as they follow the Federal Reserve's lead and begin paying lower interest rates. But if you have longer-term CDs, your higher rates will continue until your CDs mature.

In any case, as we enter a lower-interest-rate environment, you might consider reviewing your investment portfolio to determine what, if any, changes you may want to make. But you'll always want your investment mix to reflect your goals, risk tolerance and time horizon — and that's true no matter what's happening with interest rates.

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