# Is the Market Right That the Fed Is Wrong?

## As markets tumble, some on Wall Street argue the Fed raised rates too soon

By

**GREGORY ZUCKERMAN** and **BEN EISEN**

Updated Jan. 16, 2016 12:24 p.m. ET

Wall Street is learning what life is like with less central-bank support.

For years, the Federal Reserve has been a crucial underpinning for stock and bond markets. Just when it looked like the economy was faltering or investors needed a boost of confidence, the Fed was there to cut interest rates, take steps to try to boost growth or assure investors it would keep rates superlow. Much of the reason stocks, risky bonds and other assets soared after the financial crisis was the helping hand lent by the Fed.

In a matter of weeks, that has changed in dramatic fashion after the Fed last month pushed interest rates higher and displayed an appetite for as many as four additional interest-rate increases this year.

Now, [with stocks sinking](http://www.wsj.com/articles/global-stocks-fall-on-oil-and-china-woes-1452850130)as the dollar rises, the Chinese economy faltering, [oil prices collapsing](http://www.wsj.com/articles/oil-prices-fall-below-30-a-barrel-1452853918)and U.S. growth showing signs of a slowdown, some are questioning whether the central bank misjudged the ability of the economy and markets to withstand rising rates and whether the Fed will stay the course.

In recent communications with clients, Ray Dalio of hedge fund Bridgewater Associates LP, which manages $154 billion, argued that the Fed should stand pat for now and be “agnostic” about raising rates later this year, according to a person familiar with the matter.  [Jeffrey Gundlach](http://topics.wsj.com/person/G/Jeffrey-Gundlach/285), who runs asset manager DoubleLine Capital LP, has said the Fed shouldn’t be considering boosting rates any time soon and was premature raising rates last month.

 “The market is saying the economy is slowing quite considerably. If the market is right, [Fed officials] almost certainly won’t raise rates as much as they said during the December meeting,” said Ben Inker, co-head of asset allocation at GMO, a money-management firm co-founded by Jeremy Grantham.

The central bank hasn’t exactly pulled the rug out from under investors. The Fed’s interest-rate move was widely forecast. And its rates are still well below the long-term average, meaning the bank’s stance is still relatively supportive of economic growth and markets.

Other stimulative efforts for the economy by the Fed, such as holding trillions of dollars in bonds, remain in place. And Fed officials have indicated the bank won’t automatically raise rates further but will consider any changing circumstances.

And despite the market anxieties, some investors and analysts say Wall Street needs to start to wean itself from the Fed’s easy-money policies and that the Fed likewise needs to show Wall Street it won’t always come to its rescue.

Still, the disconnect between investors and the Fed was shown in stark relief Friday. As the Dow Jones Industrial Average plunged 391 points and Barclays PLC reduced its estimate of U.S. growth in the fourth quarter of last year to 0.3%, Federal Reserve Bank of San Francisco President John Williams called the U.S. economy “dynamic, “resilient” and “in good shape.”

Mr. Williams, who said he doesn’t keep a data terminal on his desk and tries not to get caught up in day-to-day market moves, said the Fed might raise rates at least three times this year, though he emphasized any moves would be gradual.

Investors have begun to wager that the Fed will prove hesitant to move rates in 2016, despite repeated comments from various Fed officials that they are sticking to their course. The December federal-funds futures contract is priced at a level that implies an 82% chance the Fed will raise interest rates one time this year, down from close to 100% just a few weeks ago, said  Peter Boockvar, chief market analyst at Lindsey Group.

“The market does appear to now be pushing the Fed” away from raising rates, said Joseph LaVorgna, chief U.S. economist at [Deutsche Bank](http://quotes.wsj.com/DB) AG. “History says the market will win out because it has the ability to cause the damage that the Fed and others desperately want to avoid, which is a recession.”

[**How Fed Rates Move Markets**](http://graphics.wsj.com/reacting-to-fed-rates/)

Some on Wall Street say investors’ hand-wringing is overdone and the Fed should stick to its guns and keep raising rates. Barclays Chief Economist Michael Gapen noted that U.S. labor markets, which have been a reliable indicator of future economic growth, show no sign of weakness.

“Much of the pervasive gloom hanging over the U.S. outlook is unwarranted,” he argued in a research note.

And Mr. Boockvar of Lindsey Group argued that the Fed should raise rates this year, even if it risks pushing the economy into a recession, because it will put the U.S. on a healthier long-term trajectory.

“There will never be a good time to raise rates after being so easy for so long,” he said, “but we can either turn into Japan,” which has had low rates and low growth for many years, “or break out of the trap” by boosting interest rates.

Regardless of the Fed’s ultimate moves, it is possible the experience of recent weeks will leave investors less likely to seek consolation from the central bank.

“We’ve got this situation where the stock market has become fascinated with what the Federal Reserve does and really thinks the Federal Reserve is there to help the stock market,” said Mr. Inker of GMO. “It could be that the Federal Reserve would like that relationship to change.”

**Corrections & Amplifications:**
Barclays PLC reduced its estimate of U.S. growth in the fourth quarter of last year to 0.3%. An earlier version of this article incorrectly stated that the reduction was to 0.4%. (Jan. 16, 2016) Also, Peter Boockvar, chief market analyst at Lindsey Group, said the Federal Reserve should raise rates this year. An earlier version of this article incorrectly said he said the Fed should raise rates several times this year. (Jan. 17, 2016)