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After much speculation it finally happened and on December 19, 2018, the Federal Reserve raised the federal funds rate—the interest rate that banks and similar institutions charge to loan money to each other. That's good and bad depending on where rates touch you and your finances. If you have a savings account and/or other investments, it's great. If you have credit cards or loans with variable interest rates, it's not so great. And, if you're in the market for a new loan or credit card, it's not going to be good. Chances are high too, more rate increases will follow.

How and Why Interest Rates Increased

On December 19, the Federal Reserve raised its rate for benchmark funds from 2.25% to 2.5%. That's a quarter-point increase. This is the fourth time the reserve has increased rates in 2018.

The Federal Reserve raises—or lowers—interest rates to control inflation. Higher rates make it harder for banks to borrow money from each other, which is how loans work. When it's harder for banks to borrow from each other, they pass on their lost money opportunities on to borrowers.

The Downside of the Interest Rates Increase for You

The rate hike means higher interest rates on both loan and credit accounts—think credit cards and home equity lines of credit (HELOCs)—as well as investment accounts. So, you'll pay more interest on your credit card debt. And with four other increases preceding this one, the new increase only adds to the impact on your finances.

Variable interest rates on credit cards are based on the prime rate. And as federal funds rates rise, the prime rate does, too. The Wall Street Journal defines the prime rate as, "… an important index used by banks to set rates on many consumer loan products, such as credit cards or auto loans." The prime rate is typically few percentage points above the federal funds rate. The rate affects not only loans and credit cards, but home equity lines of credit and credit-card rates.

Rates will rise equally to the federal funds rate increase and go up .25%:

- If you have credit card with a variable rate of 13.99%, you'll be paying a rate of 14.24% soon.
- If you have a HELOC with a rate of prime plus 1%, which most are, you can expect to pay a 6.50% interest rather than your previous 6.25%.
- Any other loan or credit account you have with a variable rate will rise too.

Rate increases take time to filter down to consumers—usually a few months. So, if you have credit card or home equity line of credit debt, do what you can to pay it down or wipe it out now. That way, in two months, when the increase hits your accounts, you won't feel as much of the sting.

If you have a lot of credit card debt, consider consolidating that debt on to the card with the lowest interest rate today. Or, apply for a new credit card with a lower rate than your current card. Either pay off the card with the highest interest quickly or transfer card debt to your new card. Better, yet, get a card that offers 0% interest for a time on balance transfers and move all your credit card debt to that card if you can.

The Upside of the Interest Rates Hike for You

Interest rates work both ways for consumers—against loans and credit—and for savings and investments. Banks that make more money on interest from loans can pass that extra money on to customers who have savings products with them. So if you have a savings account, an interest-bearing checking account, CDs and other investments, there's a chance you may see bump in your interest rate. Sadly, there is no guarantee.

Over the past three years, there have been eight increases in the federal rate fund, and savings account interest rates have been mostly flat. But, if your bank doesn't bump your rate in a few months, shop around, chances are you can find a higher rate. And with a national average savings account interest rate is just 0.09%, higher is better.[1]Online savings accounts pay some of the highest rates available with an average of over 2%.

And if you have mortgage or car loan or other long-term loan with a rate that's locked in, you won't pay more in interest. However, if you are seeking a new loan, you'll may have to pay a higher interest rate now than you would have last week. The good news is that loan rates don't always rise as sharply as the federal fund rate. For example, the federal funds rate has gone up 2% in the last year years, but a typical 30-year mortgage has only gone up .065%.

1 Federal Deposit Insurance Corp, https://www.fdic.gov/regulations/resources/rates/

Note: It's important to remember that interest rates, fees and terms for credit cards, loans and other financial products frequently change. As a result, rates, fees and terms for credit cards, loans and other financial products cited in these articles may have changed since the date of publication. Please be sure to verify current rates, fees and terms with credit card issuers, banks or other financial institutions directly.

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