



## What Does a U.S. Rate Hike Mean for Canadian Stocks?

### Description

Since the global financial crisis, any talk by the Fed of a rate hike has triggered considerable fear in financial markets. Higher interest rates increase the cost of money, making debt more expensive, thereby increasing the hurdle that companies have to meet to generate a return on their investments. It also applies short-term pressure to the price of shares because their yields become less attractive.

For these reasons, the Fed has taken a rather dovish stance since the last rate hike in December 2015, which was the first in nearly a decade.

Nonetheless, the Fed recently tabled the prospects for yet another rate hike in either June or July of this year. This can be attributed to a range of indicators, including a steadily improving job market, resilient consumer spending, and stronger housing market, all of which highlight that the U.S. economy is performing strongly.

Any increase in U.S. interest rates will have both harmful and beneficial effects on a number of Canadian companies.

### Now what?

Higher interest rates don't bode well for the outlook of gold and will have an impact on the performance of already beaten-down gold miners.

You see, as rates rise, they cause the U.S. dollar to strengthen, and with the dollar and gold sharing a negatively correlated relationship, the price of gold will fall.

Higher rates also increase the opportunity cost associated with holding non-yielding gold, while increasing the attractiveness of those assets such as money market and debt securities that have yields linked to U.S. rates. This means that investors will shift from gold to those investments with yields that benefit from higher interest rates, causing prices to fall further.

Weak gold prices will place pressure on the margins of gold miners and their profitability, plus they could even make some gold deposits uneconomic to mine, forcing them revise their gold reserves

downwards and even shutter non-economic production.

Another effect of an increase in interest rates is that it will make debt more expensive, causing financing costs to rise and placing further pressure on the margins of heavily indebted miners such as **Barrick Gold Corp.** ([TSX:ABX](#))([NYSE:ABX](#)).

This isn't solely restricted to gold miners. Higher interest rates will be felt by a range of commodities miners as a stronger U.S. dollar negatively affects commodity prices and causes the cost of U.S. dollar-denominated debt to rise. This will place greater pressure on **Teck Resources Ltd.** ([TSX:TCK.B](#))([NYSE:TCK](#)), which has almost US\$7 billion in U.S. dollar-denominated debt and is struggling with the impact of weak steel-making coal and copper prices on its cash flows.

Nonetheless, a U.S. rate hike is not all bad news for Canadian companies.

After all, it will cause the value of the Canadian dollar to fall, making exports more attractive and helping to boost economic growth and the manufacturing sector.

Another beneficiary will be **Toronto-Dominion Bank** ([TSX:TD](#))([NYSE:TD](#)).

Banks benefit from higher interest rates because they increase the yield the banks can generate from investing customer deposits as well as boosting the margins on loans.

All of this should trigger a healthy bump in Toronto-Dominion's bottom line; it's the 10th-largest U.S. bank and derives over a quarter of its income from the U.S.

### So what?

A U.S. rate hike may not be inevitable, but if it occurs it will have an impact on the price of gold, placing further pressure on an already beleaguered industry. Nevertheless, it is not all bad news. Not only will Canadian banks with U.S. operations benefit, but it will cause the loonie to weaken against the U.S. dollar, making exports more attractive and helping to boost economic growth.

### CATEGORY

1. Bank Stocks
2. Investing
3. Metals and Mining Stocks

### POST TAG

1. Editor's Choice

### TICKERS GLOBAL

1. NYSE:B (Barrick Mining)
2. NYSE:TD (The Toronto-Dominion Bank)
3. NYSE:TECK (Teck Resources Limited)
4. TSX:ABX (Barrick Mining)
5. TSX:TD (The Toronto-Dominion Bank)
6. TSX:TECK.B (Teck Resources Limited)

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