The Last Time Interest Rates Increased, This ETF Rose 50% in a Year

Description

Trying to predict the full impact of an interest rate hike can be difficult, if not impossible, to forecast. There are many variables to take into account, and from my days of studying economics, I know there is never just one path or anything definitive about what how one change in policy will impact the economy as a whole, because there are too many moving parts along the way.

Although the past does not predict the future, history often repeats and could offer some insight as to what may happen. Rising interest rates will certainly have a negative impact on the performance of many businesses due to rising costs and a more expensive currency. The popular belief is that banks will benefit the most, since higher interest rates will create an opportunity for financial institutions like **Royal Bank of Canada** (TSX:RY)(NYSE:RY) or **Toronto-Dominion Bank** (TSX:TD)(NYSE:TD) to raise lending rates higher and cash in on a higher spread.

Stock performance by the banks the last time rates went up

The last time interest rates increased was in September 2010, and it was the third hike that year, with the first coming in June. In the case of TD Bank, its stock price increased by 16% in the year after the first interest rate hike. By comparison, Royal Bank only saw its stock appreciate by 3% during the same period.

If the window is pushed to after the third hike, then TD Bank's return shrinks to less than 4%, and Royal Bank's share price declines over 7%. Clearly, this is not as simple as forecasting that a rate hike will definitively lead to improved performance among bank stocks.

A couple of ETFs did well after the hike

Gold is one commodity that has done well in good times and in bad, and it is difficult to predict how it may react to a rise in interest rates. Gold does not have any significant correlation to interest rates, so it would be incorrect to suggest there is a significant relationship between the two.

However, in the year after the first interest rate hike, **iShares Gold Bullion ETF HDG** (TSX:CGL) saw its stock price appreciate in value over 26% and 50% in the year following the third hike.

Similarly, **Horizons Gold ETF** (TSX:HUG) also increased 24% in price the year after the first hike and went up almost 49% in the 12 months following the September interest rate hike.

Since the interest rate increase last month…

Horizons Gold is up almost 5%, while the iShares Gold Bullion has increased over 3%. There is certainly no guarantee the ETFs will follow the same path the stocks were on in 2010, but it might offer an indication that the ETFs are, once again, responding positively to the rate increase.

Bottom line

There are many factors that have likely impacted the ETFs, and gold prices have likely played a significant role in that. But it is important to note that stocks are not linear, and it is not as simple as assuming that bank stocks will improve since rates have gone up. There are many factors that can impact a stock's price, making it difficult to isolate any one factor.

CATEGORY

1. Bank Stocks
2. Dividend Stocks
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2. NYSE:TD (The Toronto-Dominion Bank)
3. TSX:CGL (iShares Gold Bullion ETF)
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Author
djagielski