Could Another Interest Rate Hike Come This Week?

Description

Towards the end of last week, the loonie briefly surpassed the US$0.81 level for the first time in two years. While the loonie finished Friday slightly lower at US$0.805, many pundits now believe that another interest rate hike could be coming sooner than expected.

The monthly U.S. jobs report from last week highlighted that the U.S. economy was growing weaker than expected with fewer jobs being created in August. This effectively puts pressure on the U.S. Fed to keep rates as they are and not commit to another hike.

A separate report, also released last week, indicated that Canada was growing on an annual basis twice as fast as our southern neighbors. That could have the inverse effect and suggests another rate hike is approaching; experts suggest it could come sooner than initially expected.

What does a rate hike mean?

If the Bank of Canada does move to raise interest rates again, it'll make borrowing money more expensive, but companies such as **Manulife Financial Corp.** (TSX:MFC)(NYSE:MFC) stand to benefit significantly thanks to the nature of their business model.

Insurers such as Manulife receive premiums from their clients, which are paid out as claims. Thankfully, not everyone files a claim, and the difference between the premium and claim amounts is known in the industry as a float. That float is invested and earns interest for the company.

While you may not think that a quarter percentage point interest bump will yield significant interest earnings, keep in mind that the amount of the float is measured in billions, and Manulife is a massive insurer with one in three Canadians as clients and an international presence in both the U.S. and Asia.

A similar environment can be said of **Toronto-Dominion Bank** (TSX:TD)(NYSE:TD). Toronto-Dominion has a large presence in the U.S., where the number of deposits and branches exceeds what the bank has in Canada. This translates into a greater portion of earnings coming from the U.S., where interest rates are already notably higher, and keeps Toronto-Dominion far more diversified than any of its peers.

As rates rise, expect Toronto-Dominion to pass that increase on to lenders, resulting in stronger margins.

As interest rates continue to rise, so too will the loonie, which has already gained significantly over the past month. This effectively increases the buying power of retailers that import most of their goods. That increased buying power can lead to purchasing more of the same goods for less or buying higher-quality products at a decreased price. **Canadian Tire Corporation Limited** (TSX:CTC.A) will benefit from this uptick.

Final thoughts

There will be winners and losers from an interest rate hike, but one point that most investors fail to realize is that the last time we had an environment of higher interest rates was well over 30 years ago, when the federal lending rate was a whopping 19%.

Fortunately, a return to those interest rates at this point is more of an impossibility.

An important point to keep in mind, particularly when considering those investments that would suffer under an environment of higher rates, is that interest rate increases are slow, and it will take several years of increases before interest rates come close to the level of many of the dividend-paying stocks on the market today.

CATEGORY

1. Bank Stocks
2. Dividend Stocks
3. Investing

TICKERS GLOBAL

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2. NYSE:TD (The Toronto-Dominion Bank)
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Author
dafxentiou