What Steady U.S. Interest Rates Are Telling Investors

Description

The next year may just be the tale of two economies and how different actions lead to different outcomes. North of the border, Bank of Canada has increased rates on several occasions over the past several months, while south of the border, the United States recently chose not to push the “dirty” button by increasing the costs of borrowing — rates remained steady.

Although shares of many Canadian corporations have moved sideways and declined over the past month, the reality is that Bank of Canada has recognized that our economy is strong enough to substantiate a rate hike without any major pullbacks. The United States, on the other hand, has either made the decision to allow the bulls to run wild (under current President Donald Trump), and the Federal Reserve is cognizant that the economy is not strong enough to sustain a rate hike. The stock market could therefore well be on the verge of a major pullback due to the leaps forward it has taken over the past month.

For investors looking for a high-quality name to hold through all phases of an economic cycle (impacting both Canada and the United States), the best alternative may be to focus one’s investment portfolio in Canada. Beginning with the insurance industry, many corners of the market will offer investors a significant amount of potential.

The first name to consider is none other than **Manulife Financial Corp.** (TSX:MFC)(NYSE:MFC), which at its current price of $26 per share offers investors a dividend yield in excess of 3% as the company is starting to enjoy the higher interest rates on its deposits. As the risk-free rate of return increases, so do the rates offered by fixed income alternatives.

As Canadian interest rates increase, the earnings of all insurance companies should experience tailwinds, as more can be done with the deposits that they hold on file.

In addition to the benefits from higher rates, many insurance companies also have a wealth management division, which is benefiting from higher assets under administration, as the overall markets have increased leading to greater fees. Clearly, the stock market’s run has benefits for many companies.

However, Canada’s higher interest rates are not a blessing in disguise for all companies. In the case of **Alimentation Couche-Tard Inc.** (TSX:ATD.B), the higher rates are leading many consumers to have fewer dollars of disposable income available for spending on higher margin items such as chocolate bars and gum. At a current valuation of more than 20 times its earnings, shareholders in this convenience store operator may need to strap themselves in for a long ride should consumers begin to tighten their belts.

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