Interest rates for the Eurozone and US diverge

Important interest rate announcements were made in June, both in the UK and the US.

The US Federal Reserve announced its seventh 0.25% increase in interest rates since December 2015, taking the level to 1.75%-2.00%. The rise had already been incorporated in market prices by the time it arrived, so of more interest were the press release and other papers which accompanied the announcement. These pointed to two more rate rises in 2018, and possibly three more in 2019. They also dropped a long-standing reference to interest rates remaining, “below levels that are expected to prevail in the longer run”.

The following day the European Central Bank (ECB) decided to leave rates unchanged, again a widely anticipated move – the ECB has kept its main interest rate at zero since March 2016.

The market again focused on the background papers, which revealed the ECB’s tapering of its quantitative easing (QE – so-called money printing) programme, will come to an end in December and that interest rates were expected to be unchanged, “at least through the summer of 2019”. The first part was no surprise, but the statement on interest rates was not expected. The markets reacted accordingly, pushing the Euro down against the US dollar.

Controlling market shocks

The relationship between central banks and investment markets is a curious one these days as the banks go out of their way to make sure markets are kept informed. As a result, the markets are now more interested in the next-but one action. The market responses to these recent rate announcements are two good examples.

The need for the banks to flag their intentions was underlined by the ‘taper tantrum’ of 2013, which happened when the Chairman of the US Federal Reserve first suggested that QE could be scaled back. Nobody thought QE would continue forever, but the mere hint that it might end gave global markets a shock, causing sharp movements in share prices, bond yields and currency rates.

Ultimately, the message from both the US and the Eurozone is the same: interest rates are set to rise, albeit at different paces, and QE will no longer be a prop to markets.

For insight into what this might mean for your investments and whether any changes are necessary, please talk to us.

The value of your investment can go down as well as up and you may not get back the full amount you invested.

Past performance is not a reliable indicator of future performance.

Investing in shares should be regarded as a long-term investment and should fit in with your overall attitude to risk and financial circumstances.