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Macro Market Insights

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Stuck in Purgatory

Financial markets have been going through another wave of directionless movements as they obsess over the "will they or wont they" question as to when the US Federal Reserve will begin to raise interest rates. This uncertainty has in many instances led to range- bound volatility in a number of asset classes where we are not short of large price gyrations; however, markets like gold are caught in a defined trading range. In the instance of gold, on more than a few occasions we have seen a floor around $1,140 US per ounce to a ceiling around $1,300. It seems the days are gone where the story of record low interest rates or increasing inflation expectations will fuel gold's next rally. As well, the lack of uncertainty stemming from likely economic outcomes and no real surprises to financial markets has seen the gold market remaining at bay.

Exceptions to this are of course the recent actions taking by the Swiss National Bank to end their peg to the Euro, but that one off event has now arguably been overlooked by financial markets and one still might wonder how well it taught a lesson to investors of the potential for a violent rebalancing in asset prices. The story has reverted back to record low interest rates from policy makers and a global economy that continues to lethargically move forward as it's pulled along by a recovering US consumer.

The question regarding interest rates though is one that has almost become meaningless for two particular reasons. The first is that American central bankers are moving away from their forward guidance approach to financial markets. No longer do markets require reassuring of record low rates for years into the future in order to keep credit markets at ease, and provide fuel for the equity markets. Investors are beginning to take comfort in what they believe to be a domestically strengthening US economy without the life support of a liquidity backstop by the Fed. Central bankers in the US are attempting to withdraw themselves from the picture.

The second reason the interest rate discussion is becoming less relevant in the US is because the pace at which they raise rates will be of little to no impact on markets. A rate move at this point in the cycle is more of significance to providing a signal to markets that we are lifting off emergency level lows. It's not to say, curtail reckless borrowing habits of US homebuyers or over-levered corporations.

All else being equal, considering a US Fed that begins to move interest rates in accordance with a gradually improving economy will have limited impact on financial markets. Interest rate policy will not be a determining story for asset prices like precious metals as it has in years past because the story has already been anticipated. Whether it creates more volatility when we finally see liftoff is another question as thinner trading volumes have made the gold market more vulnerable to dramatic moves; however, this steadfast trading range seems more and more likely to be tested in a to be determined scenario.