FINANCIAL MARKETS

THE FED HIKING CYCLE & ITS EFFECT ON GOLD

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BLACKWELL GLOBAL

Blackwell Global is a global brokerage, aiming to be the most trusted financial service provider. We are committed to transparency, integrity and service excellence.

Founded in 2010, we now have global presence in over 90 countries.

We believe that sound investment and trading decisions begin with a strong grounding in financial education. Our goal is to make this available to everyone - and this free eBook is part of that commitment.

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WHAT'S IN STORE FOR THE FED?

FOREWORD

We've seen many central banks adopt a dovish tone in early 2019.

One of those central banks is the Federal Reserve, which has given itself room for manoeuvre. Global growth anxieties and trade tensions have made policymakers question the pace at which they hike interest rates.

This eBook explores what we can expect from the Federal Reserve's hiking cycle in 2019. Plus, we'll analyse how it could affect one particular Blackwell Global product: Gold (XAUUSD).

Patrick Latchford
CEO, Blackwell Global Investments (UK) Limited

CAUTIOUS TONES FROM THE FED?

WHY DOES FED MONETARY POLICY MATTER?

Before we explore the current monetary policy of the Federal Reserve, it's important to clarify why it matters to traders.

In short, the US central bank has the ability to move the markets. Specifically, its monetary policy can affect the price of financial assets.

This happens because monetary policy controls the flow of capital within an economy.

For example, as the flow of capital in an economy tightens, through something such as higher interest rates, the native currency can appreciate in value.

The reverse is also true. So if the flow of capital in an economy increases due to lower interest rates, the native currency can depreciate in value.

Monetary policy moves can also be indicative of an economy's overall health. Higher interest rates are usually a sign that an economy is growing and that inflation needs to be kept in check. Lower interest rates, or quantitative easing programmes, often point to an economy that needs stimulus for economic growth.

For this reason, adjustments in monetary policy can affect investor and business confidence. That's why it's not uncommon for central bank announcements to influence the stock market.

If a central bank's economic outlook for an economy is uncertain, it can lead to investors moving their capital to so-called safe haven assets such as Gold.

FED MONETARY POLICY

Let's take a closer look at the Federal Reserve's current monetary policy.

The central bank is in the middle of what's called a "hiking cycle".

This simply means it has been gradually increasing interest rates for a period of time.

Specifically, the Federal Reserve has increased interest rates on nine separate occasions since December 2015. The current Federal Funds Rate (which is what traders often refer to as "interest rates") stands between 2.25% - 2.5%.

In December 2018 - which was the last occasion rates increased - the Federal Reserve forecast that it would increase interest rates two times (down from three) in 2019.

However, since the turn of the year, policymakers have retreated from this stance, citing concerns about the global economy, trade tensions and the fading effect of US tax cuts.

MARCH MEETING

The most recent Federal Reserve meeting took place on Wednesday 20th March 2019.

In that meeting, the central bank said that the US economy, while being healthy, was showing signs of slowing. With this in mind, policymakers forecast no further rate hikes for the remainder of 2019.

Specifically, the central bank cut its GDP growth forecast for 2019 from 2.3% to 2.1%. The GDP forecast for 2020 is weaker still at 1.9%. US inflation remains below the central bank's target of 2%, removing the need to increase rates to keep consumer price increases in check.

Federal Reserve Chair, Jerome Powell, stated at the March meeting that current data means the bank can hold steady with rates for the time being.

US DOLLAR & GOLD

The Federal Reserve has essentially paused its hiking cycle. This could have an effect on both the US dollar and Gold.

Now, as a trader, what you need to know is that USD and Gold have an inverse relationship. This means that the price levels of each asset tend to move in opposite directions. For example, if the price of USD in increases (in comparison with other currencies), the price of Gold decreases.

The reason for this inverse relationship is actually quite simple. All you need to know is that Gold is priced in US dollars.

This can have two consequences.

Firstly, if the value of the US dollar increases, Gold becomes more expensive to buy in other currencies. This weakens demand for Gold and puts downward pressure on its price.

Secondly, if the value of the US dollar decreases, Gold becomes cheaper to buy in other currencies. This drives demand for Gold and acts to increase its price.

Plus - it's important to remember that Gold is viewed as a safe haven asset. So when investors and financial institutions don't have an appetite for risk, some move their capital into a stable asset such as Gold, which then increases in price.

FED IMPACT ON XAUUSD

With Blackwell Global, you can trade Gold (XAUUSD). As the Federal Reserve has paused its hiking cycle and forecast slower growth, there is potential that the price of Gold (XAUUSD) could increase.

Traders should pay particular attention to two issues.

First, traders should monitor US/China trade tensions. In particular, if there are signs that trade deal negotiations are stalling, the US dollar will likely face downward pressure. Investors could also move their capital to safe-haven assets in this scenario.

Second, traders should track economic data from the US. At March's Federal Reserve meeting, Jerome Powell did not rule out a rate cut as the next monetary policy move. If US economic data misses forecasts, the US dollar could again face downward pressure. Investors could also shift their capital away from US equities into safe-haven assets, such as Gold.


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WHY BLACKWELL GLOBAL?

We can't pretend that is easy to become a successful trader. But we are here to help and support you as you make your trading journey, providing dedicated resources such as our demo trading accounts and regularly published research materials.

Founded in 2010, Blackwell Global was established to offer brokerage solutions for private and institutional clients. Blackwell Global is a Straight Through Processing or STP broker who provide their clients with superior liquidity and price feeds from top international banks. These are offered alongside 24-hour technical support, market research tools, educational materials, professional partnership programmes and fully integrated trading platforms.

We offer access to multiple asset classes including more than 60 currency pairs, precious metals and other contracts for differences. As a global broker, we are always striving to achieve excellence in our customer service, as well as developing innovative technology to support our customers needs.

Today, the Blackwell Global group of companies has a presence in over 90 countries. To find out more about Blackwell Global please go to: www.blackwellglobal.com

Or contact Customer Support:

Tel: +44 (0)20 7397 3781
Email: cs@blackwellglobal.com

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