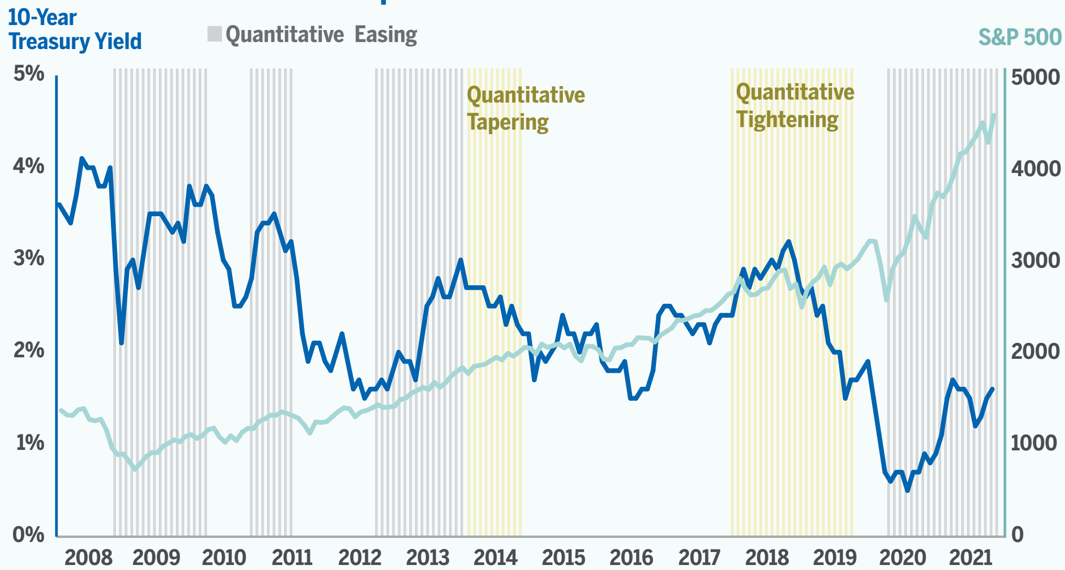
Alger On the Money

A View on the U.S. Market

Should You Fear the Taper?

With the Federal Reserve currently tapering its quantitative easing, a look at history may shed light on the impact of the change on financial markets, including interest rates and stocks.

Federal Reserve Balance Sheet Trends and the Impact on Financial Markets



Source: FactSet and Alger.

- Interest rates have generally risen during quantitative easing, as the chart above suggests. That may be counterintuitive to some given a very large purchaser of bonds may be expected to drive yields lower. However, we believe that historically, the market priced in the stimulative impact of quantitative easing on the economy, which actually boosted interest rates during periods of quantitative easing.
- During both the tapering of 2014 (when the Fed's balance sheet grew at a slower pace) and when quantitative tightening occurred in 2018 and 2019 (when the Fed's balance sheet declined), interest rates trended lower as the market priced in slower economic growth.
- Given that history suggests that interest rates may decline during the current tapering, we believe investors' fear of rising rates may be alleviated i.e. concern about higher interest rates lowering the present values of future earnings may be misplaced. Therefore, lower interest rates may potentially support that equities and stocks could fare well as they did during the previous tapering and quantitate tightening periods.

Inspired by Change, Driven by Growth.

The S&P 500 is a stock market index tracking the performance of 500 large companies listed on stock exchanges in the U.S.

Quantitative easing is the expansion of the Federal Reserve's balance sheet.

Quantitative tapering is the reduction of the Federal Reserve's balance sheet expansion.

Quantitative tightening is the reduction of the Federal Reserve's balance sheet.

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