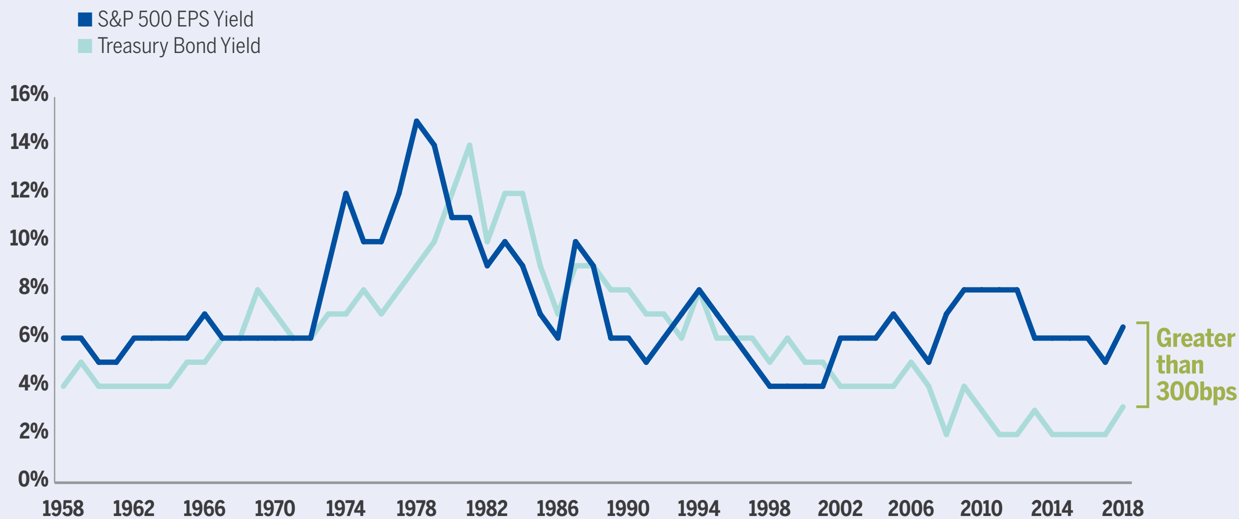
ALGER

Alger On the Money

Will Rising Rates Hurt Stocks?

Will higher interest rates bring down stock prices? Many investors are concerned about rising rates but an examination of current stock valuations relative to bonds reveals that stocks haven't priced in how low interest rates have become and therefore may not suffer as rates climb.



Source: FactSet, Federal Reserve and S&P, as of October 31, 2018.

- EPS "yield" is calculated by dividing EPS for the next 12 months by a stock's current market price. It indicates the percentage of each dollar invested in the stock that is estimated to be earned by the company over the next year, similar to the current yield of a bond.
- Historically, the EPS yield on stocks has been approximately equivalent to those of Treasury bonds but since the Global Financial Crisis when central banks slashed interest rates, equity yields have been much higher than bonds, which indicates that equities have been trading at an attractive valuation relative to bonds.
- Similar to the Taper Tantrum of 2013 when rising interest rates only briefly hurt stocks before equities went on to post strong gains, the current cushion between equity and bond yields may indicate that investors need not worry that falling Treasury bond prices will drag down stocks with them.

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