



## If history is of any guide...

While the recent Federal Open Market Committee (FOMC) statement demonstrated the willingness of US Federal Reserve (Fed) to increase or reduce the pace of their asset purchases depending on the economic data, it is clear that they expect to taper the asset purchase in the second half of 2013. If the economic recovery plays out in accordance to FOMC's forecast, the tapering of asset purchases will be completed by some point in the middle of 2014. According to the economic projection by FOMC, the first hike in target federal funds rate would probably take place in 2015. Perhaps it is an opportune time to go back in time and assess how Euro Stoxx 50 has performed before and after the previous episodes of major tightening cycles by Fed.

	02 Jul 13	Change	%
<b>Euro Stoxx 50</b>	2603.20	-19.42	-0.74%
<b>DAX</b>	7910.77	-73.15	-0.92%
<b>SMI</b>	7732.62	-8.45	-0.11%

Source: Bloomberg/Phillip Futures

**Chart 1: US federal funds target rate since 1990**



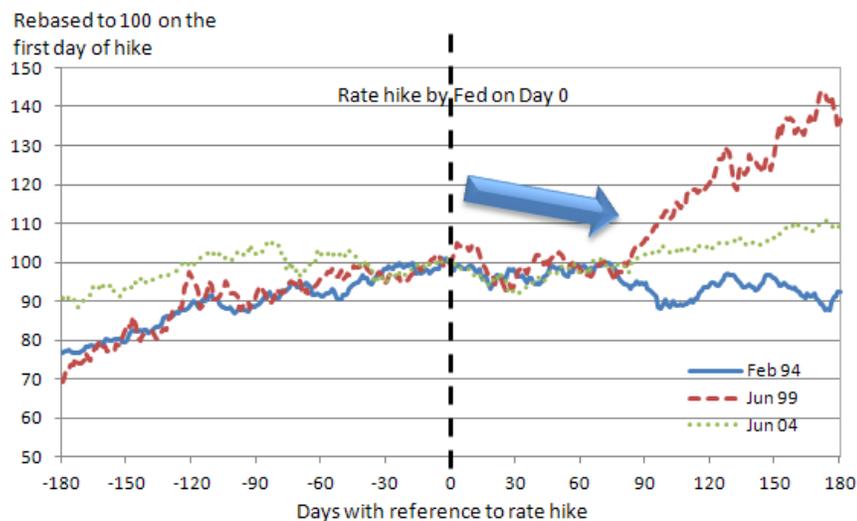
Source: Bloomberg/Phillip Futures

The red arrow in Chart 1 shows the major tightening cycles by US Federal Reserve since 1990. Based on Table 1, we noted that Euro Stoxx 50 has historically performed well prior the start of the tightening cycle by Fed. After the first hike by Fed, Euro Stoxx 50 has historically corrected lower in the first 30 and 60 days. Based on Chart 2 (next page), we do not see any consistent pattern in the performance of Euro Stoxx 50 beyond 60 days.

**Table 1: Euro Stoxx 50 Index performance (prior and post) the previous episodes of Fed tightening cycles**

Month of 1st rate hike	Euro Stoxx 50 performance prior to first Fed rate hike (% Change)			Euro Stoxx 50 performance post first Fed rate hike (% Change)		
	-180d	-60d	-30d	30d	60d	180d
<b>Feb 94</b>	30.5	9.6	1.7	-2.8	-1.2	-7.6
<b>Jun 99</b>	44.1	3.9	5.0	-3.9	-2.6	36.6
<b>Jun 04</b>	10.1	-1.9	5.1	-7.9	-2.5	9.7
<b>Average</b>	28.3	3.9	3.9	-4.9	-2.1	12.9

**Chart 2: Euro Stoxx 50 Index performance (prior and post) the previous episodes of Fed tightening cycles**



Source: Bloomberg/Phillip Futures

## Caveat

The previous episodes of major tightening cycles by Fed appeared to have dampened Euro Stoxx 50 performance. Nonetheless, it is worth noting that there are differences between the past cycles and the current one. First of all, the current easing cycle has brought federal funds target rate down to rock bottom and further boosted by several rounds of quantitative easing. Hence, a better reference point for comparison may not be the first rate hike by Fed (estimated to take place in 2015) but rather the inflection point of the monetary policy bias from ultra loose to less loose (ie tapering of asset purchase estimated to start in the second half of 2013). Secondly, unlike in the past, Fed has enhanced its communication of the outlook on the future path of policy rate via forward guidance. This may change the market reaction to the eventual rate hike as the market would have priced in the changes in forward guidance before the actual rate hike.

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