




Impact of US Interest Rate Hike on Bitcoin

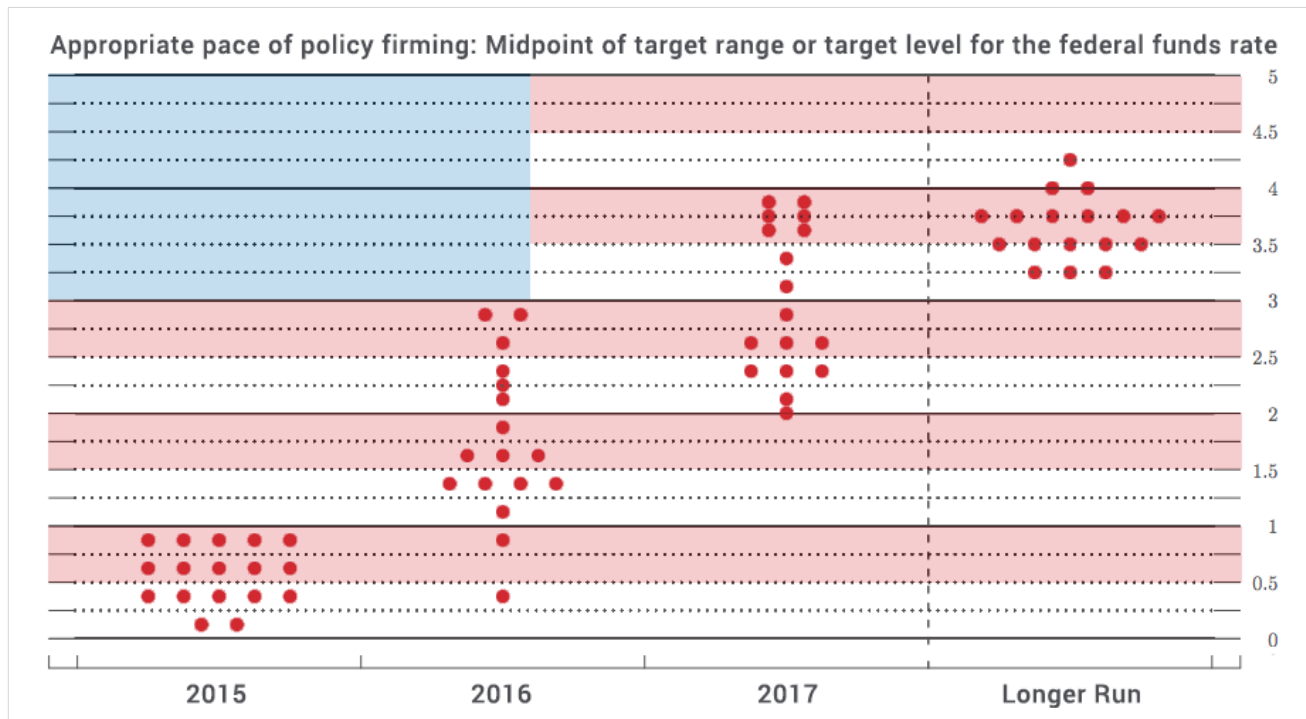
itBit Bitcoin Macro View
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Since its inception, Bitcoin has existed in a zero interest rate environment. This may soon change as the Federal Reserve appears close to raising interest rates for the first time in seven years.

The benchmark interest rate, also known as the federal funds rate, has been set at a record low of 0.25% since December 2008. The soonest the Federal Open Market Committee (FOMC) could raise the rate would be in their next meeting on September 17th.

The latest "dot plot" released in the FOMC's Summary of Economic Projections in June shows that while all 17 members expect the benchmark interest rate to remain below 1%, most are anticipating a rate increase to .50% - .75% by year's end. In 2016 and beyond, the expectations are for interest rates rising and ultimately settling between 3% - 4%.



WHY HIKE THE INTEREST RATE?

The dual mandate of the Federal Reserve is to maintain maximum employment and stable prices. The US unemployment rate is down to 5.3% and lies within targets for a rate hike.

With regards to price stability, the low rates and associated borrowing costs that come with a zero interest rate policy have led to large amounts of capital pouring into speculative assets such as equities, commercial real estate and high-yield bonds. This was in-line with the Federal Reserve's goals following the financial crisis. However, this type of investment can lead to declining productivity growth and potential output hurting long-term growth.

POTENTIAL IMPACT OF US INTEREST RATE HIKE ON BITCOIN

Bitcoin has been perceived in the past as a good hedge against inflation. If the Federal Reserve enacts higher interest rates, the bitcoin price could take a hit as investors and traders move their money out of speculative investments. US Dollar strength has historically hurt bitcoin price and an interest rate hike will only serve to boost USD (more on USD later).

One scenario where Bitcoin could receive a boost is from continued unrest in the global currency markets. If other struggling countries take actions similar to China's recent devaluation of the yuan, the spotlight could once again shine on bitcoin as a valuable alternative currency.

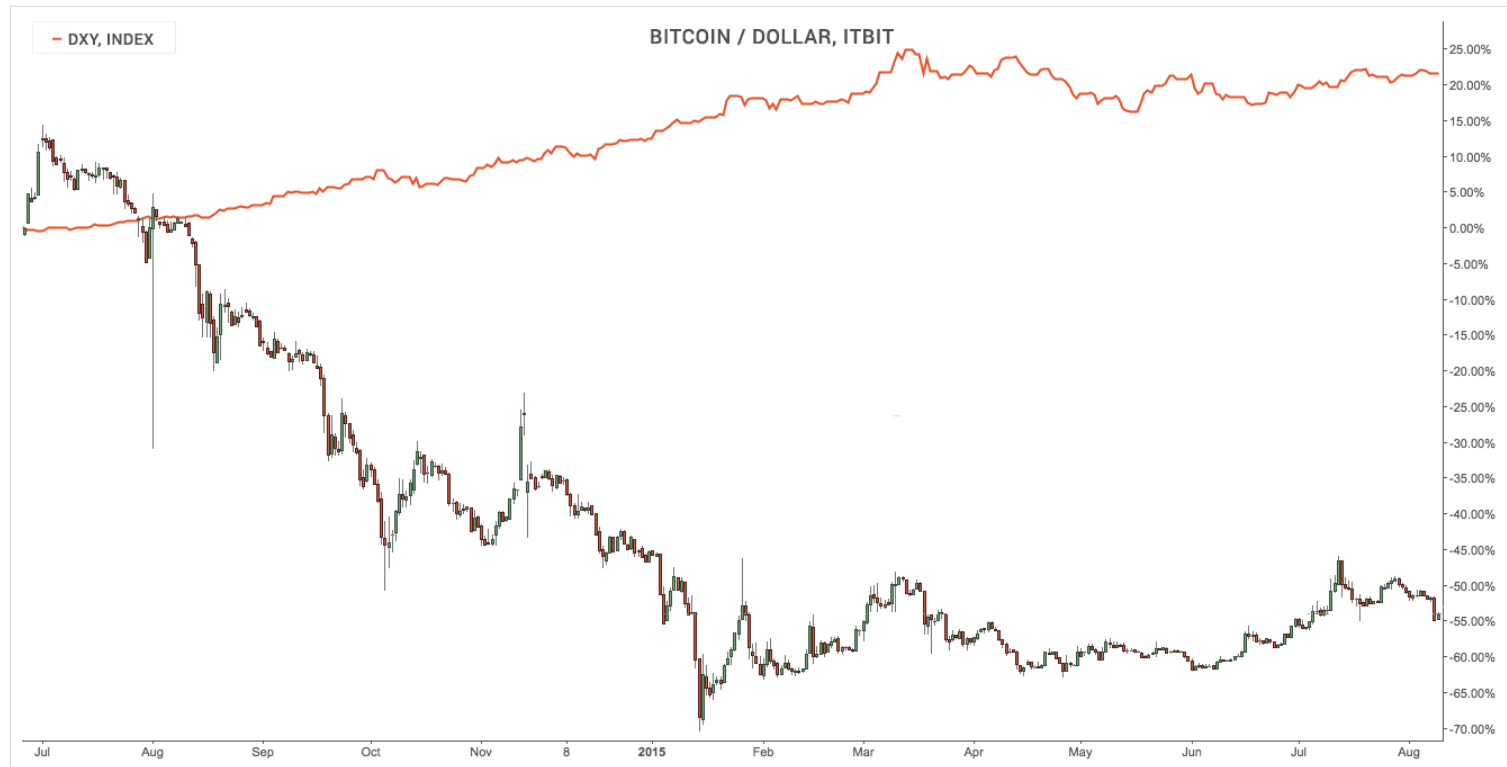
What If The Rate Remains Unchanged?

A continuation of the easy money policy of the last six years likely means that bitcoin will continue to primarily trade on technicals and sentiment. The currency market (USD in particular) has been controlling the global macroeconomic picture of late and bitcoin should continue to follow its lead in the short-term. should continue to follow its lead in the short-term.

TWO GLOBAL FINANCIAL TRENDS BITCOIN TRADERS SHOULD WATCH

Strong US Dollar

As we mentioned above, the US Dollar should benefit from a rise in the federal funds rate as this is indicative of a strengthening economy and often leads to increased investment in-flows. This should be helpful for US stocks but could negatively impact the price of bitcoin which historically has shown an inverse relationship to the Dollar.



Decrease in Speculative Investment

Rising interest rates may reduce investment in speculative assets. The shift away from higher-risk asset classes such as high-yield debt has slowly begun. The chart below of JNK, a proxy for high yield bonds, has broken down very quickly as talk of a US interest rate hike have intensified.



At this stage, bitcoin remains a speculative asset. Mass outflows to more stable investments with lower risk profiles will negatively impact the bitcoin price.

FOUR KEY TAKEAWAYS FOR BITCOIN TRADERS

- 1** Bitcoin has been perceived in the past as a good hedge against inflation. If the Federal Reserve enacts higher interest rates, the bitcoin price could take a hit as investors and traders move their money out of speculative investments.
- 2** There isn't great certainty around what will happen if rates remain unchanged. A continuation of the easy money policy of the last six years likely means that bitcoin will continue to trade primarily on technicals and sentiment.
- 3** The US Dollar should benefit from a rise in the federal funds rate. This should be helpful for US stocks but could negatively impact the price of bitcoin which historically has shown an inverse relationship to the Dollar.
- 4** The shift away from higher-risk asset classes such as high-yield debt has slowly begun. Bitcoin remains a speculative asset and mass outflows to more stable investments with lower risk profiles will negatively impact the price.



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