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The Effect of FED Interest Decisions on Stock Markets: An Application of Developing Countries

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Extensive Summary

The aim of the Central Bank in an economy is to achieve economic stability and reach full employment production level. Central Banks try to restore price stability and full employment production level by affecting interest rate and total demand by making some changes in money supply. The Federal Reserve System (FED) was established in 1913 by the American Congress. The most important reason why the FED has a different role and place than other Central Banks is that the policy decisions taken and implemented while managing the American economy have the potential to have an impact on other economies of the world, especially on the economies of developing countries.

The aim of the research is to reveal the effect of the interest rate decisions taken in the FED meetings on the stock markets of developing countries. Event study method was used to analyze the effect of FED interest rate decisions on developing country stock markets. According to the results of the analysis with the 2016 data, it was concluded that the decisions taken by the American Central Bank regarding the policy rate have no significant effect on the stock markets of developing countries. This result means that FED interest rate decisions have no effect on the stock markets of developing countries. [Şerefoğlu, 2014; Dündar, 2015; Uysal, 2016; While it is not compatible with the results of Aktaş et al., 2018], it is compatible with the findings of [Artichoke, 2018].

The actors of the stock markets of developing countries follow the FED meetings with interest and rationalize their expectations regarding the possible decision to come out of the meeting based on the inflation and employment data announced regarding the American economy before the meeting. Therefore, the markets give the reaction before the decision and reflect it on the prices. In the days following the interest rate decision, the market remains unresponsive as expectations are met. When the first six meetings of the year in which the interest rate decision was not taken are evaluated, it is seen that the FED provided information to the public prior to the meeting in accordance with the principle of transparency and signals to the public whether it will make an interest rate increase decision in the language it uses. Understanding FED's monetary policies correctly and reading the signals about macroeconomic projections before the meeting are important in terms of reducing the negative impact of any interest rate decision taken by FED on the markets.