The Weekly

Economic & Market Recap

Peapack-Gladstone Bank, Peapack Private Wealth Management

March 29, 2019

As of 03/29/2019		Wk	Wk		YTD	12 Mos
		Net	%	Div	%	%
STOCKS	Close	Change	Change	Yield	Change	Change
DJIA	25,928.68	426.36	1.67	2.24	11.15	7.57
S&P 500	2,834.40	33.69	1.20	1.95	13.07	7.33
NASDAQ 100	7,378.77	52.71	0.72	1.05	16.57	12.12
S&P MidCap 400	1,896.27	41.28	2.23	1.70	14.02	0.93
Russell 2000	1,539.74	33.82	2.25	1.49	14.18	0.67

TREASURIES	Yield	**FOREX**	Price	Wk %Change
2-Year	2.26	Euro/Dollar	1.12	-0.80
5-Year	2.23	Dollar/Yen	110.84	0.82
10-Year	2.41	Sterling/Dollar	1.30	-1.29
30-Year	2.81	Dollar/Cad	1.34	-0.57

Source: Thomson Reuters & Bloomberg

What Caught Our Eye This Week

Since the end of last year, U.S. authorities have conducted an all-out global blitz to convince governments and global telecommunications network providers against purchasing Huawei's fifth-generation (5G) wireless equipment. The U.S. government insists that the 32-year-old Chinese company has the potential to use its equipment to spy on or sabotage networks globally on behalf of the Chinese government. Huawei dominates the global telecom market in the current 4G wireless technology, and it is the leader in the 5G technology that will control the next generation of networks that are now being built. By some accounts, Huawei's technology is up to two years ahead of its rivals' capabilities which include Nokia, Ericsson and ZTE. The company employs 80,000 scientists, and it spends over 20% more on research and development each year than Nokia and Ericsson combined. Huawei's equipment is often sold at a 50% discount (or more) to its competitors, and the company's service is considered by some to be the best in the industry. The U.S. government has practically banned the use of Huawei equipment in this country since 2012, but it has not been widely successful at convincing other nations to follow suit. The U.S.'s staunchest ally in this effort has been the U.K.; however, British authorities have determined that it cannot do without Huawei equipment at least in the periphery of its national networks.

Economy

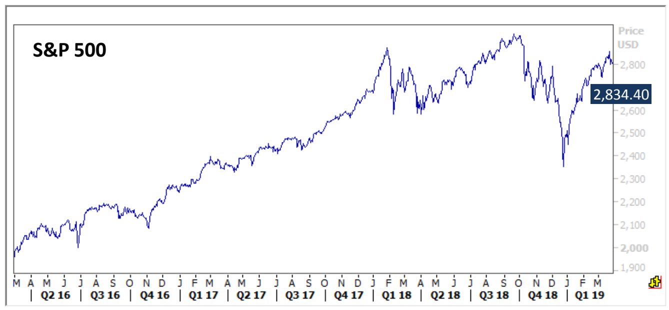
The economic headliner this week was Thursday's report on fourth quarter real GDP. This was the final look at Q4 GDP and the growth of 2.2% was revised down from the previous estimate of 2.6%. Consumer spending was weaker than initially estimated and residential investment declined at a 4.7% annual pace. Corporate profits also disappointed showing only 0.4% growth in the fourth quarter. On the positive side, growth on exports was revised slightly higher to a 1.8% annual pace. Finally business investment was a positive contributor to overall GDP, adding 0.73 percentage points to the fourth quarter's 2.2% growth rate. In other news this week, both housing starts and permits disappointed in February. Housing starts declined by 8.7% to 1.162 million units and permits decreased by 1.6% to 1.296 million. Over the past 12 months, housing starts are down 9.9%. On Friday, we were pleased to see personal income increase by 0.2% in February, matching expectations. Personal income is now up 4.2% year-over-year.

Fixed Income/Credit Market

The FOMC statement in March was extremely dovish and the Fed confirmed its patient stance by adjusting its dot plot down to show no further rate hikes in 2019. The Fed expects GDP to grow at only 2.1% in 2019, while the most recent annualized Core PCE reading came in at 1.8% which is below the Fed's 2% inflation target. Furthermore, market-based inflation expectations over the next 5 years according to the TIPS market suggest that inflation will reside close to 1.79%. Over a one-year horizon, the U.S. Treasury yield curve is expected to steepen roughly 21 basis points (bps) between the 2-yr and 10-yr tenors; according to Bloomberg's forward curve projections. However, much of the steepening is projected to occur because of a 13 bp decrease in the 2-yr Note yield. If the forward curve is an accurate representation of where interest rates will be one year from now, duration risk should be added cautiously at the 7-yr tenor where the total return is forecasted to be 2.63% versus 2.09% and 1.37% for the 10-yr and 30-yr tenors, respectively.

Equities

It was a quiet week in the U.S. equity market as investors continued to digest last week's inversion of the U.S. Treasury yield curve. This was evidenced by the NYSE having both of its lowest trading volume days in 2019 this week. The release of the Mueller report appeared to be a nonevent for equities with the major indexes closing mostly flat on Monday, but stocks posted considerable gains the following day after the Treasury rally took a pause. On Thursday, stocks were lifted by positive trade news from Reuters who reported that China has made proposals regarding technology transfers that go beyond previous gestures. In other news, ride-hailing company Lyft started trading in the public market Friday with an IPO price of $72 and there was strong demand for the stock. Concerns over the inverted yield curve and a global economic slowdown were not enough to suppress investors' appetite for equities as the S&P 500 gained 1.20% on the week. Industrials led the market, and the only two sectors to decline were communication services and utilities.



Our View

The spread between the 3-month U.S. Treasury bill and the 10-year U.S. Treasury note inverted last Friday for the first time since August of 2007. Market participants and economists often view yield curve inversions as a warning signal that a recession may be looming. Moreover, an inverted yield curve has preceded each of the past seven recessions dating back to the late 1960's; however, there have been some false signals along the way. The predictive power of an inverted yield curve consists primarily of the size of the negative spread and the amount of time the curve remains inverted. The recent yield curve inversion only averaged less than 4 basis points and had a lifespan of just 5 days. Furthermore, there is additional data which leads us to believe that the current yield curve inversion is giving a false indication of a future recession. First, the front end of the U.S. Treasury yield curve is artificially high due to heavy Treasury bill issuance to fund the expanding U.S. budget deficit and pay tax refunds and the backend of the yield curve is being partially compressed by technical dynamics from negative interest rates overseas. Second, corporate credit spreads, which typically expand in anticipation of a rise in defaults and economic stress, are still extremely tight by historic standards. For example, the Bloomberg Barclays U.S. High Yield OAS is currently 402 basis points (bps), which is 110 bps below the mean dating back to 1994. Lastly, the change in leading economic indicators on a year-over-year basis stood at 3.0% as of its most recent release. Historically, when year-over-year leading economic indicators fall below 0%, a recession is highly probable in the near future. It is our belief that predicting a recession is not an inconsequential task and it is often fraught with error; but based on the evidence above, a near-term recession appears improbable at the current juncture.

COMING UP NEXT WEEK		Est.
04/01 Retain Sales MM	(Feb)	0.3%
04/01 ISM Manufacturing PMI	(Mar)	54.1
04/02 Durable Goods	(Feb)	-1.3%
04/03 Non-Farm Payrolls	(Mar)	170k

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