The Weekly

Economic & Market Recap

Peapack-Gladstone Bank, Private Wealth Management

August 11, 2017

As of 08/11/2017		Wk	Wk		YTD	12 Mos
		Net	%	Div	%	%
STOCKS	Close	Change	Change	Yield	Change	Change
DJIA	21,858.32	-234.49	-1.06	2.30	10.60	17.43
S&P 500	2,441.32	-35.51	-1.43	2.01	9.05	11.70
NASDAQ 100	5,831.53	-68.37	-1.16	1.12	19.90	21.41
S&P MidCap 400	1,711.05	-40.43	-2.31	1.76	3.04	9.68
Russell 2000	1,374.24	-38.08	-2.70	1.47	1.27	11.81

TREASURIES	Yield	**FOREX**	Price	Wk %Change
2-Year	1.29	Euro/Dollar	1.18	0.39
5-Year	1.74	Dollar/Yen	109.09	-1.45
10-Year	2.19	Sterling/Dollar	1.30	-0.20
30-Year	2.79	Dollar/Cad	1.27	0.17

Source: Thomson Reuters & Bloomberg

What Caught Our Eye This Week

London Interbank Offered Rate (LIBOR) is used by banks to set the interest rate of hundreds of trillions of loans, securitizations, and derivatives. It is listed in five major currencies for seven different maturities (overnight to 12-months) with the most common being the 3-month U.S. dollar rate. Reports of rate fixing, which first surfaced during the financial crisis in 2008, led to billions of dollars in fines and the decision to phase out the use of LIBOR by 2021. Last month, the U.S.'s Alternative Reference Rates Committee (ARRC), which is sponsored by the Federal Reserve, selected the Broad Treasuries Financing Rate (BTFR) as its preferred USD LIBOR alternative. The BTFR is a benchmark based on short-term loans known as repurchase agreements which are backed by US Treasuries. The Fed plans on publishing this rate on a daily basis beginning in the first half of 2018. The transition process for moving away from LIBOR remains highly uncertain. The primary concern is how parties will bridge the gap between LIBOR and BTFR for existing instruments. There are over $1.3 trillion in adjustable-rate mortgages in the U.S. that will be affected.

Economy

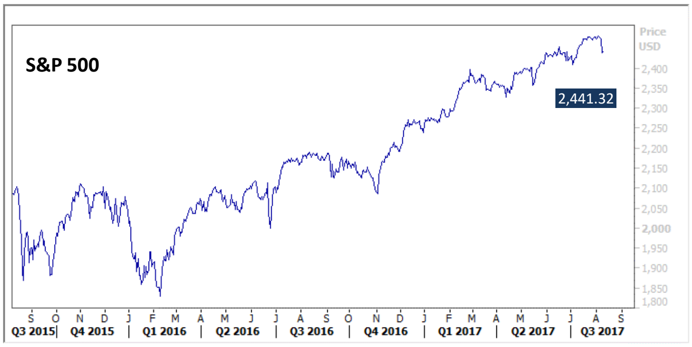
The economic calendar was a bit light this week, and the data points released highlight continued sluggishness in the U.S. economy. On Tuesday, the JOLTS report (Job Openings and Labor Turnover Survey) displayed 6.2 million job openings in June. The "Quits" rate edged down to 2.1%, and over the last twelve months the net employment gain is +2.3 million. Wednesday brought U.S. nonfarm business-sector productivity figures, which once again disappointed with a small gain of +0.9% in the second quarter. Year-over-year productivity numbers have advanced by 1.2%. To put these figures in perspective, the post WWII average is +2.1% of annual growth. The Producer Price Index was released on Thursday, and both headline and core numbers came in below expectations. The headline and core both declined in July by 0.1%. Core services prices were down 0.2%, which is the weakest reading since February of this year. The final report for the week was the Consumer Price Index, which also came in below expectations. Both headline and core figures increased by 0.1% in July, and over the past twelve months both measures are up 1.7%.

Fixed Income/Credit Market

U.S. Treasuries began the week relatively quiet but volatility picked up as the week progressed. On Tuesday, President Trump put the world on edge by announcing that the North Korean regime would be met with 'fire and fury' after North Korea threatened to fire a missile toward an American military base in Guam. On Thursday, President Trump continued his strong rhetoric and further warned the North Korean regime of the consequences of striking the U.S. or one its allies. U.S. stocks sold off while the 10-Year U.S. Treasury Note Volatility Index (TYVIX) surged approximately 7% from 4.26 on Wednesday to 4.56 on Thursday as investors flocked to safe haven assets. The 10-Year U.S. Treasury yield decreased 5 basis points and closed Thursday at 2.198%. Headline risk also precipitated wider credit spreads as both high yield and investment grade option adjusted spreads increased roughly 28 bps to 4.07% and 6.5 bps to 1.09% week over week, respectively.

Equities

Equity benchmarks had their biggest weekly loss in many months as fears about North Korea's ability to launch a missile strike escalated. Headlines highlighting the rising tensions over North Korea dominated the media this week causing volatility to return to the markets. The S&P 500 and NASDAQ were both down over 1% on the week, and the S&P 500 experienced its biggest one day drop of 1.40% since May on Thursday. Small cap stocks were especially hard hit as the Russell 2000 index dropped 2.70% this week extending a three week slide that has seen the Russell 2000 index fall 4.38%. Despite solid second quarter earnings, 73% of companies that have reported exceeded expectations, profit-taking took hold of investor psychology. Companies with the largest gains year-to-date experienced the most substantial losses this week. From a sector perspective, S&P Financials were especially weak dropping 2.70% as rates fell due to traders repositioning to U.S. Treasuries. Conversely, utilities benefited as lower-risk, equity yield plays.



Our View

The flare up in tensions between the United States and North Korea, over North Korea's nuclear ambitions, roiled the financial markets this week. Conflict is an inherent element of the human condition, so geopolitical risks are always a concern for investors. We have highlighted in the past the potential spike in volatility that a geopolitical incident could cause. The increase in volatility can be especially pronounced when valuations are uncomfortably high. Indeed credit-oriented fixed income has been trading at historically tight spreads, and equities are at the top of recent trading ranges. The timing of geopolitical events and their long-term significance is highly unpredictable. Given the inherent uncertainty in geopolitical events, investors tend to over react and return correlations for higher risk assets tend to migrate upward. The speed with which this process happens is often surprisingly rapid, which is why we advocate well-diversified portfolios for risk control.

COMING UP NEXT WEEK		Est.
08/15 NY Fed Manufacturing	(Aug)	11.0
08/15 Retail Sales MM	(Jul)	0.3%
08/15 Retail Control	(Jul)	0.4%
08/16 Housing Starts Number MM	(Jul)	1.220M
08/17 Philly Fed Business Index	(Aug)	18.5
08/17 Industrial Output MM	(Jul)	0.3%
08/18 U Mich Sentiment Prelim	(Aug)	94.0

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