The Weekly

Economic & Market Recap

Peapack-Gladstone Bank, Private Wealth Management

June 15, 2018

As of 06/15/2018		Wk	Wk		YTD	12 Mos
		Net	%	Div	%	%
STOCKS	Close	Change	Change	Yield	Change	Change
DJIA	25,090.48	-226.05	-0.89	2.19	1.50	17.47
S&P 500	2,779.66	0.63	0.00	1.91	3.95	14.26
NASDAQ 100	7,255.76	103.14	1.44	0.96	13.43	27.27
S&P MidCap 400	1,992.37	-8.30	-0.41	1.57	4.83	13.64
Russell 2000	1,683.91	11.42	0.68	1.25	9.66	19.42

TREASURIES	Yield	**FOREX**	Price	Wk %Change
2-Year	2.55	Euro/Dollar	1.16	-1.38
5-Year	2.80	Dollar/Yen	110.66	0.99
10-Year	2.92	Sterling/Dollar	1.33	-0.97
30-Year	3.05	Dollar/Cad	1.32	2.10

Source: Thomson Reuters & Bloomberg

What Caught Our Eye This Week

The U.S. pay-tv landscape has been under pressure for years thanks to tech companies like Netflix and Amazon. Struggling to compete, AT&T, a distributor of content, and Time Warner, an owner of content, announced their intent to merge almost 2 years ago. In the first fully-litigated vertical merger case in 40 years, the judge ruled in favor of the companies. The government failed to prove that vertical integration in the industry leads to higher content prices which would harm consumers. In theory, by combining the two, the companies can achieve efficiency benefits that should lower prices for consumers. One way for a company to grow is by vertical integration, such as with AT&T and Time Warner. These two companies are engaged in different stages of a supply chain and therefore do not compete. It was widely expected that the ruling would be in their favor. This ruling could be a bellwether for the other mega mergers that are in the pipeline. Two deals in healthcare, CVS-Aetna and Cigna-Express Scripts, are also vertical mergers. Deals that are more horizontal (company acquires a similar business and thus eliminates competition) may face more challenges. The Sprint - T-Mobile deal is an example of a horizontal merger because it would bring the number of carriers from four to three.

Economy

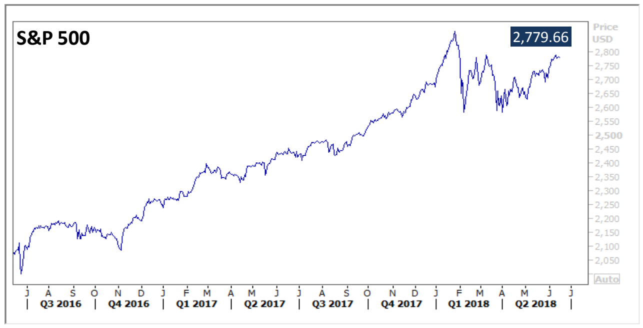
This week the economic data was centered around inflation statistics with the release of the producer price index and the consumer price index. On Tuesday the CPI figures matched consensus expectations with an increase of 0.2% in May. Over the past twelve months, this metric has increased by 2.8%. The "core" CPI which excludes food and energy prices advanced by 0.2% and is now up 2.2% year-over-year. The biggest influence on the headline figure was energy prices, which increased by 0.9%. The producer price index was reported on Wednesday and displayed an increase of 0.5% in May, which was well above the consensus forecast. Over the past year this index has increased by 3.1%. The "core" PPI increased by 0.3% and is now up 2.4% year-over-year. Energy prices had the heaviest influence on the headline figure rising by 4.6%. Finally on Thursday the retail sales report showed an advance of 0.8% in May, which was well above expectations. Retail sales are now up 5.9% year-over-year and the pace of consumer spending appears to be accelerating. The all-important control category, which excludes food service autos, gas, and building materials, advanced by 0.5%.

Fixed Income/Credit Market

On Wednesday, the Fed raised its target range 25 basis points (bps) to 1.75% - 2.00%, making the effective Fed funds rate 1.89%. The tone of the FOMC meeting remained hawkish which suggests the Fed will continue with a gradual path towards normalization as long as labor markets and inflation targets remain favorable. With the Fed roughly split between an additional one or two rate hikes in 2018 and robust Treasury supply, there continues to be significant pressure on the front-end of the U.S. Treasury yield curve. Prior to the Fed's decision on Wednesday, the 2-year and 10-year Treasury spread was trading around its lowest level since 2007 at approximately 41 bps. However, over the last two days we've seen the spread compress even further by about 4.1 bps to close the week at 36.9 bps. The 2Y and 10Y Treasuries end this week at 2.55% and 2.92%, respectively.

Equities

Major equity indexes ended the week mixed as stocks were buffeted on an abundance of news. Major central banks (The Federal Reserve, the European Central Bank and the Bank of Japan) all held meetings and made rate announcements that equity investors reacted to and produced intraday volatility. The NASDAQ shrugged off interest rate concerns following the Fed's meeting to set a record on Thursday as investors continue to favor growth stocks. The banking sector sold off sharply as the spread between short-term and long-term rates compressed potential narrowing net interest margins. Trade concerns once again impacted the equity markets on Friday as the U.S. imposed about $50 billion worth of tariffs on imports from China. The fear of China's retaliation was reflected by the broad market selling off with the DJIA down more than 1% intraday. Equities partially recovered after China announced its retaliation of only $34 billion in tariffs. From a sector perspective, the worst performing sectors this week were telecommunications and energy down 3.1% and 2.1%, respectively. AT&T dragged down the telecommunications group and energy stocks were hurt by lower oil prices. The best performing sector was consumer discretionary on strength in retail stocks and hope for consolidation in the entertainment space.



Our View

Investors had several interesting and pertinent news items to digest this week. The Federal Reserve raised their benchmark rate another quarter of a percentage point, as expected, but the forward rate projections suggest a slightly more hawkish tilt. Fed officials expect an additional two hikes this year and three more next year. If these anticipated rate increases come to fruition, the fed funds target would increase to 3.0% to 3.25% by the end of 2019 and will probably exceed the neutral interest rate. The neutral interest rate is the rate that is neither stimulative or restrictive regarding policy. The more hawkish tone caused the treasury yield curve to flatten as the 2-year to 10-year treasury spread hit a cycle low of 35 basis points. The European Central Bank also met this week and announced their intention to phase out its QE program by the end of the year. The ECB also indicated that they would not consider raising rates until the summer of 2019 which financial markets interpreted as dovish. But from a broader perspective, markets are beginning to take notice of the growing divergence in central bank policy. The one-year Treasury bill has climbed from 1.97% to 2.31% over the last three months, and the U.S. dollar has appreciated 6.3%. Emerging market sovereign debt has been especially hard hit this year as much of their debt payments are dollar denominated. As economic growth paths and the pace of central bank policy normalization diverge, asset class correlations will as well.

COMING UP NEXT WEEK		**Est.**
06/19 Housing Starts	(May)	1.317M
06/20 Existing Home Sales	(May)	5.52M
06/22 Markit Mfg PMI Flash	(Jun)	56.5

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