Peapack Private

Wealth Management

The Weekly

Economic & Market Recap

Peapack Private Wealth Management

January 24, 2020

1/24/2020		Wk	Wk		YTD	12 Mos
		Net	%	Div	%	%
STOCKS	Close	Change	Change	Yield	Change	Change
DJIA	28,989.73	-358.37	-1.22	2.20	1.58	17.96
S&P 500	3,295.47	-34.15	-1.03	1.79	2.00	24.89
NASDAQ	9,314.91	-74.03	-0.79	0.93	3.82	32.58
S&P MidCap 400	2,065.15	-30.40	-1.45	1.74	0.10	15.59

TREASURIES	Yield	**FOREX**	Price	Wk %Change
2-Year	1.48	Euro/Dollar	1.10	-0.63
5-Year	1.50	Dollar/Yen	109.44	-0.67
10-Year	1.68	GBP/Dollar	1.31	0.28
30-Year	2.13	Dollar/Cad	1.31	0.62

Source: Bloomberg/FactSet

What Caught Our Eye This Week

Palladium is one of six platinum-group metals. About 85% of palladium is utilized in exhaust systems in cars in order to help turn toxic pollutants into less harmful carbon dioxide and water vapor. It is also used in electronics and jewelry. The price of palladium has doubled over the last year and is up more than 25% this year. With the recent price for palladium at about $2,500 an ounce, the metal is now more expensive than gold. Palladium's price rally will likely continue as demand is expected to outpace supply for the ninth straight year. The metal is mined primarily in South Africa and Russia, and mostly extracted as a secondary product from operations that are focused on other metals. Over the last 15 years, supply has contracted by 1 million ounces or 12%, while demand has risen by 4 million ounces or by 57%. Usage is increasing as governments, especially China and India, tighten regulations on pollution from vehicles. Most analysts expect a modest pickup in global automotive sales in 2020 (following two years of contraction) and the stricter emission standards requiring higher palladium amounts should support the higher prices. Car manufacturers are having to pay more for the metal and may eventually pass on the price increase to consumers.

Economy

It was an uneventful week for economic data, so the main focus was on the existing home sales report, which was released on Wednesday. These figures increased by 3.6% to 5.54 million units at an annual rate and were comfortably ahead of consensus estimates. This level of home sales was the highest monthly figure going back to February of 2018. Over the past 12 months, existing home sales have increased by 10.8%, and the median sales price ($274,500) has advanced by 7.8%. Focusing on the December transactions, 43% of homes sold were on the market for less than a month. Based on a plethora of inputs, it appears that real residential investment was up close to 5% in the 4th quarter. In other news this week, the Conference Board Leading Economic index declined in December to 111.2, driven by negative contributions from rising unemployment insurance claims and a drop in housing permits. This widely followed index has now declined in 4 out of the last 5 months. Finally, on Thursday, weekly jobless claims increased by 6,000 during the week ending January 18th to 211,000. The four-week moving average is now at 211,000.

Fixed Income/Credit Market

Longer-dated interest rates along the U.S. Treasury curve have decreased year-to-date (YTD) as much as 25.7 basis points (bps) at the 30-year tenor. The benchmark 10-year Treasury has dropped 23.4 bps which has narrowed the spread between the 2-year and 10-year tenors 15.7 bps to 19.1 bps. Looking at U.S. ETF fund flows by asset class indicates investors are making a push to capture more yield. YTD, bank loans and preferred equity funds have had the biggest net fund flows increasing their market caps 6.3% and 3.4%, respectively. From a credit quality perspective, high yield funds have increased their market cap by 4.3% whereas the investment-grade market cap increased 1.4%. Curve positioning has taken on a barbell approach as investors increased the long-term market cap 2.5% and the ultra-short market cap 1.8%. Meanwhile, short-term and intermediate duration bonds have increased market caps of just 0.5% and 0.9%, respectively. The 10-year U.S. Treasury closed the week down 13.8 bps at approximately 1.69%.

Equities

Investors focused on concerns about the spread of the coronavirus, a slower global economic growth forecast from the International Monetary Fund, and a new round of fourth quarter earnings reports. Domestic equities were relatively flat for the first two trading days of the holiday shortened week. Stocks opened lower on Thursday due to mixed earnings reports and news that China imposed a strict quarantine on the city of Wuhan to control the spread of the virus. Markets rallied later in the day but gains were quickly lost on Friday with market's declining 0.9%, as the second report of a coronavirus victim was announced in Chicago. Eighty-six companies have reported fourth quarter results so far and, in aggregate, revenue is up 3.26% year-over-year and earnings up 0.83% year-over-year. Earnings have beat analysts' expectations by 3.94% so far. Oil fell over 7.7% this week, a drop of $4.50 a barrel. Utilities gained 2.4% outperforming all other sectors. Energy was the worst performing sector posting a weekly decline of 4.2%.

Our View

The European Central Bank left policy unchanged this week which was widely expected. The deposit rate remained at -0.50% and QE at E20B per month. What struck us was the ECB's announcement that the central bank would conduct its first strategic review of policy since 2003. The review will address a range of relevant topics but will center on inflation. Despite aggressive stimulus for many years, the ECB has failed to lift inflation to its inflation target just below 2%. Some analysts have cynically suggested that it was not a failure of monetary policy, but rather measurement error and that inflation is running hotter than indicated. Lower than expected inflation, as predicted by classic econometric models such as the Phillips Curve, is not unique to Europe. Inflation is running stubbornly below the Federal Reserve's desired level as measured by the core PCE index. Additionally, wage growth disappointed in December growing at a tepid pace of only 2.9% year-over-year. Employment growth has been strong with the U.S. economy on average producing 160,000 new jobs per month over the last year, which should be sufficient in a late-cycle environment to provide support for additional wage and consumption growth. Financial markets are not pricing in any inflation risk. The real existential threat to the bull market is inflation and rising inflation expectations. Equity indexes will experience drawdowns and corrections related to geopolitical tensions, the outbreak of viruses and political uncertainty. Generally, these types of issues will not cause economic dislocations sufficient to drive the economy into a recession. Rising inflation can force a significant enough change in interest rates and Federal Reserve policy to imperil the economy, and in turn the bull market. We are a long way from inflation sparking the next recession. There are other reasons for equities to correct, such as earnings disappointments. The market will be focused on forward guidance from the earnings' reports.

COMING UP NEXT WEEK		Est.
01/27 New Home Sales SAAR	(Dec)	730.0K
01/28 Durable Orders SA M/M (Prelim)	(Dec)	1.0%
01/28 Consumer Confidence	(Jan)	128.1
01/29 Pending Home Sales M/M	(Dec)	0.50%
01/30 GDP Chain Price SAAR Q/Q (First Prelim)	(Q4)	1.7%
01/31 Michigan Sentiment NSA (Final)	(Jan)	99.3

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