# The Weekly

## Economic & Market Recap

Peapack-Gladstone Bank, Peapack Private Wealth Management

March 8, 2019

| As of 03/08/2019 | | Wk Net | Wk % | Div | YTD % | 12 Mos % |
|---|---|---|---|---|---|---|
| **STOCKS** | Close | Change | Change | Yield | Change | Change |
| DJIA | 25,450.24 | -576.08 | -2.21 | 2.27 | 9.10 | 2.23 |
| S&P 500 | 2,743.07 | -60.62 | -2.16 | 2.01 | 9.45 | 0.17 |
| NASDAQ 100 | 7,015.69 | -135.88 | -1.90 | 1.10 | 10.40 | 0.31 |
| S&P MidCap 400 | 1,860.28 | -65.07 | -3.38 | 1.74 | 11.86 | -2.99 |
| Russell 2000 | 1,521.88 | -67.76 | -4.26 | 1.50 | 12.78 | -3.25 |

| **TREASURIES** | Yield | **FOREX** | Price | Wk %Change |
|---|---|---|---|---|
| 2-Year | 2.46 | Euro/Dollar | 1.12 | -1.21 |
| 5-Year | 2.43 | Dollar/Yen | 111.15 | -0.70 |
| 10-Year | 2.63 | Sterling/Dollar | 1.30 | -1.45 |
| 30-Year | 3.01 | Dollar/Cad | 1.34 | 0.88 |

Source: Thomson Reuters & Bloomberg

**What Caught Our Eye This Week**

Four years ago, the European Central Bank (ECB) embarked on the equivalent of a $2.9 trillion bond buying spree to provide liquidity to the flagging European economy. Last December, this program was halted, and the ECB projected that it may begin to raise interest rates in the latter half of 2019. Since December, a lot has changed. Global growth has slowed considerably, trade tensions have not abated, and the Brexit deadline looms just three weeks from now. On Thursday, the ECB announced that it was changing course. The central bank pushed out to 2020 the time when it expects to increase interest rates (at the earliest). It also instituted the third round of Targeted Long-Term Refinancing Operations (TLTRO III). This program will provide low interest, two-year loans to banks to help them replace about $810 billion in previous TLTRO loans that will come due in the near future. This will also shore up the banks' cash availability at a time when lending is so important to maintaining gross domestic product growth. This all comes at a time when the U.S. Federal Reserve has stopped increasing interest rates for now, and after China's government has announced an aggressive program of tax cuts along with initiative to increase loans to small companies.

**Economy**

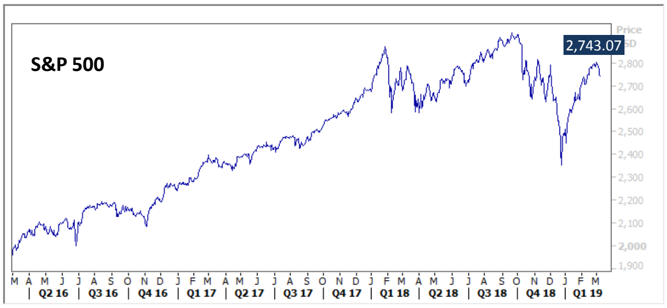
The economic headliner this week was the February employment report which was released on Friday. Nonfarm payrolls rose by 20,000 which was well below estimates of 180,000 and is the smallest increase since September 2017. Although the hiring number was a disappointment, hourly earnings and unemployment figures were strong. Furthermore, the U-6 measure of unemployment (includes part-time workers looking for full-time employment and those less active in seeking work) dropped to 7.3% which is the lowest reading since 2001. Earlier in the week, the ISM non-manufacturing index showed an increase to 59.7 in February from 56.7 in January. This came in well above expectations of 57.4, and all eighteen sectors reported growth in February. The December new home sales report was also released this week, and it showed an increase of 3.7% to a 621,000 annual rate beating the consensus expectation of 600,000. The median price of new homes sold was $318,600 which is down 7.2% from a year ago.

**Fixed Income/Credit Market**

In February, the top performing fixed income sectors were senior loans, 0 to 5-year high yield bonds, and preferred equity with total returns of 2.03%, 1.42%, and 0.58%, respectively. International Treasury bonds (non-currency hedged), long-term bonds, and TIPS (Treasury-Inflation Protected Securities) were February's laggards posting respective total returns of -1.08%, -0.79%, and -0.17%. In aggregate, the sectors that we follow returned 0.22% in February and have a total return profile of 2.39% year-to-date (YTD). Cumulatively within those sectors YTD total return in 2019 far exceeds 2018's total return of 1.07%. With slowing global growth and muted inflation expectations for 2019, we would expect high quality fixed income sectors to perform positively, particularly if interest rates continue to rally. On Thursday, the European Central Bank (ECB) pushed back guidance on rate hikes and announced a new long-term bank lending program which contributed to further downward pressure on U.S. Treasury yields. Week-over-week, the 10-year U.S. Treasury decreased 12.9 basis points to roughly 2.63%.

**Equities**

Major U.S. and global indices closed lower this week, ending the equity market's worst week this year. The decline was amplified by news that the U.S. added only 20,000 jobs (vs. a consensus expectation for 180,000) during the month of February and that China's exports plunged. Weak German industrial production numbers and lowered ECB growth estimates also fed into the growth fear. With the fourth quarter earnings season nearly complete, the market has less fundamental catalysts and is now worried about slowing global growth. In addition, investors harbor concerns that the U.S.-China trade dispute will not come to resolution as quickly as anticipated. The market's strongest sector this week was Utilities at +0.33% and the weakest was Healthcare with a decline of 3.63%.




**Our View**

The European Central Bank sharply lowered its forecast for regional economic growth this year to only 1.1% from 1.7%. Inflation expectations were also reduced to 1.2%, which is well below the ECB's target of 2%. In prior Weekly's, we have detailed the remarkable lengths the ECB has gone to in its attempt to reinvigorate the Eurozone economy since the global financial crisis. Negative interest rate policy in conjunction with a massive quantitative easing program have failed to lift the European economy to an acceptable growth trajectory. In our view, deflationary forces in Europe are clearly the most obvious risk factor to the overall health of the global economy. This week's ECB announcement amplified investors' deepest fear concerning a global economic slowdown. The reaction of the financial markets was predictable. Interest rates fell as bond markets across the global rallied; equity markets fell on earnings worries and the dollar strengthened. We will be monitoring the developments in Europe closely and would expect Europe to be one of the more likely causes of heightened volatility. From a longer-term perspective, Europe's prospects increasingly appear similar to Japan – very low secular growth and deflationary pressures. The U.S. also faces our own economic challenges. Demographics, income inequality, rising government debt, and unsustainably large unfunded obligations will inhibit the secular growth potential of the U.S. as well. The broader implications of muted global growth are significant and have real-world implication regarding financial planning applications. Asset prices and returns across all asset classes are likely to be compressed by low rates and weak growth. For example, with interest rates at 2.64% (U.S. Treasury 10-year), a reasonable return expectation would be roughly 3.25% – the coupon plus some modest positive roll. Assuming the long-term average equity premium, equity returns over the next decade could be less than 7% based on the current rate structure. Historically, large-cap equity returns have approached 11%, but in today's environment we believe that returns greater than 8% could be difficult to achieve.

| COMING UP NEXT WEEK | | Est. |
|---|---|---|
| 03/11 Retail Sales MM | (Jan) | -0.1% |
| 03/13 Durable Goods | (Jan) | -0.5% |
| 03/15 Industrial Production MM | (Feb) | 0.4% |
| 03/15 U Mich Sentiment Prelim | (Mar) | 95.7 |

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