Peapack Private Wealth Management

September 13, 2019

09/13/2019		Wk	Wk		YTD	12 Mos
		Net	%	Div	%	%
STOCKS	Close	Change	Change	Yield	Change	Change
DJIA	27,219.52	422.06	1.58	2.25	16.68	4.69
S&P 500	3,007.39	28.68	0.96	1.90	19.97	4.10
NASDAQ	8,176.71	73.64	0.91	1.02	23.23	2.80
S&P MidCap 400	1,963.16	51.65	2.70	1.74	18.05	-3.59

TREASURIES	Yield	**FOREX**	Price	Wk % Change
2-Year	1.79	Euro/Dollar	1.11	0.33
5-Year	1.75	Dollar/Yen	108.07	1.21
10-Year	1.90	GBP/Dollar	1.25	1.18
30-Year	2.37	Dollar/Cad	1.32	0.14

Source: FactSet

What Caught Our Eye This Week

The so-called gig economy was born out of the rise of the internet in the 1990's. It provided a place to connect people looking for flexible part-time employment and those looking to hire flexible workers. It is estimated that 45% of American workers have a "side" job. This week, the California state lawmakers approved a landmark bill, AB5, that will force companies to classify independent contractors as employees. Contract workers have no access to protections such as unemployment insurance, workers compensation, minimum wage, social security or healthcare. Despite this, most gig workers say they would not choose full-time employment. BCG Henderson Group reported that only 20% of freelancers would prefer full-time employment. The workers' reasons include the flexibility that gig work provides: enabling them to work from home, spending more time with family, and volunteering. While bill AB5 affects companies such as Uber, Lyft, Doordash, and Instacart, it is anticipated that it could extend to other sectors such as construction and trucking. The obvious impact will be an increase in company costs which undoubtedly will be passed on to the consumer. Ultimately, the companies affected will not only have to adjust their business plans, but they will have to lay off workers. This may cause unintended consequences that will require continued legislation to address additional issues in the future.

Economy

The economic headliner this week was the retail sales report, which was released on Friday. Retail sales increased by 0.4% in August which was better than expected. Retail sales have now increased for six consecutive months and are up 4.1% over the past 12 months. The all-important control category, which excludes food service, autos, gas and building materials advanced by 0.3%. Nonstore sales now make up 12.8% of overall retail sales and are up 16.0% year-over-year. On Tuesday, the JOLTS report (job openings and labor turnover survey) showed 7.217 million job openings as of July 31st. The "quits" rate increased to 2.4% which is a new high for the expansion, and the net employment gain over the past 12 months is a respectable 2.6 million. The producer price index data was released on Wednesday and displayed a modest increase of 0.1% in August. The "core" PPI advanced by 0.3% and is now up 2.3% year-over-year. Finally, on Thursday, the consumer price index showed a 0.054% increase in August matching consensus expectations. The "core" CPI increased by 0.256% and is now up 2.4% over the past 12 months (the largest 12-month increase since late 2008).

Fixed Income/Credit Market

Week-over-week, U.S. Treasury yields increased as much as 35.1 basis points (bps) at the 30-year tenor. Benchmark 2-year and 10-year Treasury yields increased 34.1 bps and 25.8 bps, respectively, which increased the spread between the two tenors 8.3 bps. The 2-year and 10-year Treasury spread closed Friday at 10.1 bps. The Fed's preferred measure of yield curve inversion, the 3-month Bill and 10-year Note (3m10y) spread increased 33.3 bps to a spread of -5.9 bps. While far from normal, the change in the 3m10y spread is encouraging given that it closed at a ten year low of roughly -50 bps on August 28th. The rise in yields can be attributed to positive economic data coming out of the U.S., the easing of trade tensions between the U.S. and China, and the European Central Bank (ECB) cutting its deposit rate further below zero from -0.4% to -0.5% on Thursday. Additionally, beginning on November 1st the ECB will revive its bond purchasing program at €20 billion a month until they hit their inflation target of just below 2.0%.

Equities

The S&P 500 rose above the 3,000 level for the first time since late July. Reports surfaced that global central banks will provide stimulus, China will suspend tariffs on some American imports, and progress toward an interim trade deal with China is being considered. On Monday, economic data out of China reported the fourth month of falling imports and exports, suggesting the trade war is having a heavier effect on the world's second largest economy. Mid-week trade tensions eased after China announced U.S. products such as cancer drugs, lubricants, pesticides and shrimp meal will be exempt from tariffs for about a year instead of being imposed next week. In addition, the administration is evaluating whether they will delay plans to impose a 15% tariff on $160B of Chinese goods on December 15th. The leading sector was financials gaining 3.9% driven by an increase in rates. The worst performing sector was real estate down 3.1%.

Our View

Equity markets have rallied over the last several weeks as both the United States and China have made several conciliatory gestures in the trade war. China has decided to exempt purchases of U.S. soybeans and pork from punitive tariffs. Relief on soybeans and pork certainly removes some political pressure on President Trump. Chinese agriculture imports of U.S. products are down dramatically since the trade war began hurting farmers, which are an important Trump constituency. The move by the Chinese follows the Trump administration's two-week postponement of tariff increases on $250 billion of Chinese goods that were scheduled for October 1st. There has been some speculation in the press that an interim trade deal may be in the works that is limited in scope and focuses strictly on trade issues. An agreement, even an interim one, would partially remove some of our concern regarding corporate profits and margins in 2020 and would allow market valuations to continue to lift. However, we do not believe a trade deal that effectively addresses the thornier issues regarding national security and intellectual property is on the horizon. It is hard to know if the Trump administration would be willing to accept a limited trade deal. The S&P 500 currently trades at a roughly 17 times earnings (forward 12 months). Although the current multiple is above the average multiple over the last 20 years, valuations are not extreme and arguably reasonable considering the current level of interest rates. Interest rates have been compressed largely due to central banks driving short-rates down and distorting the term structure due to quantitative easing. This week the European Central Bank kicked off another round of stimulus by lowering rates 25 basis points and restarting QE. The ECB will be buying €20 billion worth of bonds per month starting in November. The Fed is widely expected to lower the policy rate 25 basis points at next week's meeting. The predominant reason equities have risen back to old highs has been the dramatic shift from policy normalization back toward boundless accommodation.

COMING UP NEXT WEEK		Est.
09/17 Industrial Production SA M/M	(Aug)	0.20%
09/18 Housing Starts SAAR	(Aug)	1,260K
09/19 Leading Indicators SA M/M	(Aug)	0.10% R

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