Peapack Private Wealth Management

The Weekly
Economic & Market Recap

Peapack Private Wealth Management April 26, 2019

As of 04/26/2019		Wk	Wk		YTD	12 Mos
		Net	%	Div	%	%
STOCKS	Close	Change	Change	Yield	Change	Change
DJIA	26,543.33	-16.21	-0.06	2.16	13.79	9.13
S&P 500	2,939.88	34.85	1.20	1.89	17.26	10.22
NASDAQ 100	7,826.68	136.96	1.78	1.00	23.64	17.70
S&P MidCap 400	1,973.92	20.49	1.05	1.63	18.69	4.15
Russell 2000	1,591.82	26.07	1.66	1.44	18.04	2.18

TREASURIES	Yield	**FOREX**	Price	Wk %Change
2-Year	2.28	Euro/Dollar	1.12	-0.90
5-Year	2.29	Dollar/Yen	111.58	-0.31
10-Year	2.50	Sterling/Dollar	1.29	-0.62
30-Year	2.92	Dollar/Cad	1.35	0.44

Source: Thomson Reuters & Bloomberg

What Caught Our Eye This Week

Generation Z is a cohort of approximately 70 million people born between 1997 and 2012 and will represent 20% of the U.S. population by 2034. Generation Z is not only larger, but more racially and ethnically diverse than either millennials or baby boomers. According to Forbes, Gen Z is already positioned to become the largest generation of consumers by the year 2020. and they will account for between 29 to 143 billion in direct spending. McKinsey notes that Gen Z's preferences for individual expression of identity, social consciousness, and ethics drive its consumption patterns and will likely have long-term implications for portfolios. Gen Z demands value and authenticity from its brands. Who will likely gain share in this new world? Companies that market directly to the consumer and have high exposure to a growing Hispanic population. Expect to see larger companies acquire some of these brands (e.g. WalMart's purchase of Bonobos) to adapt to a more fragmented marketplace. Shifting brand preferences will place even more pressure on retailers that are already stressed due current over-retailed environment.

Economy

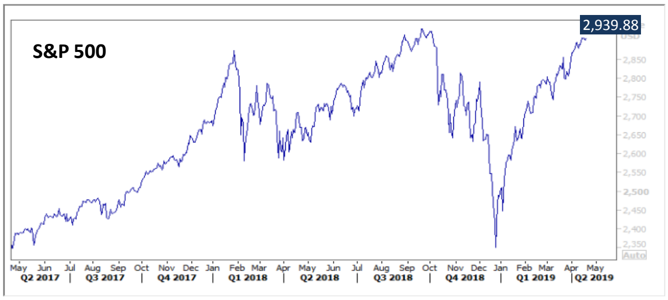
The economic headliner this week was Friday's report on first quarter real GDP. This was the first look at Q1 GDP and growth was better than expected, advancing by 3.2%. There were some temporary factors that are likely to reverse in coming quarters. Exports surged and imports declined and there was a large accumulation of unsold merchandise. Residential construction decreased by 2.8%, which was the fifth straight quarterly decline. Inventories increased at a $128.4 billion rate, which contributed 0.65% to overall growth. Business fixed investment spending was a bright spot, advancing by 2.8%. The next look at Q1 GDP will be on May 30th. In other news this week, existing home sales figures disappointed with a 4.9% decline to 5.21 million units at an annual rate. These sales have now decreased by 5.4% over the past 12 months. March durable goods orders were reported on Thursday and showed a 2.7% gain solidly beating expectations. Core capital goods orders increased by 1.3% reaching a new expansion high.

Fixed Income/Credit Market

According to the Bloomberg Barclays Municipal Bond Index, tax-exempt New Jersey bonds have provided investors with a total return of 3.56% year-to-date (YTD), outperforming the U.S. Aggregate Index by 78 basis points (bps). 10-year municipal debt backed by the state of New Jersey is currently trading at approximately 57 bps above the Bloomberg 10-year AAA municipal index, which is roughly 6.7 bps below the one-year average. However, the 10-year NJ debt trades at approximately 2.50% which is 100% of the 10-year U.S. Treasury (UST) compared to a 75.7% municipal to UST ratio nationally. The slope of the NJ muni bond curve also provide investors with a significant carry advantage. The spread between the 2-year and 30-year NJ tax-exempt general obligation bonds is 144 bps, whereas the 2-year and 30-year spreads for U.S. Treasuries and the AAA muni index are 63.5 and 102.6 bps, respectively. New Jersey's visible 30-day supply is $187.6MM while the amount of debt expected to retire is $444MM, equating to net supply of negative $256.4MM which should drive positive price performance.

Equities

Earnings season is in full swing with almost two-thirds of the S&P 500's constituents releasing results this week and next. Equity markets started off strong with the S&P 500 and Nasdaq both hitting new all-time closing highs on Tuesday. Those records were broken again on Friday on the back of a strong first quarter GDP report that showed the U.S. economy growing at a rate well above expectations. The combination of better-than-feared earnings results and ongoing solid U.S. economic data have boosted investor optimism. According to Zacks Investment Research, as of Wednesday, total earnings for the 131 S&P 500 members that have reported are up 2.3% on +4.8% higher revenues. Expectations coming into the quarter were for a decline in earnings of 4.2%. The S&P 500 gained 1.20% on the week with healthcare being the best performing sector returning +3.66% and energy being the worst performer returning -1.21%.



Our View

The risk-on market environment thus far in 2019 has allowed high yield bonds to return approximately 8.6% year-to-date according to the Bloomberg Barclays US Corporate High Yield Total Return Index. One of the major drivers of high yield bond performance has been the incredibly low corporate default rate, which resides slightly above 1% and compares very favorably to the 30-year average of 3.7%. The high yield option adjusted spread, which typically widens in anticipation of an uptick in defaults, is currently only 355 basis points and is 155 basis points below the mean dating back to 1994. As the above-mentioned figures indicate, investors have not been bashful when it comes to investing in high yield bonds, but although the sun is shining on the asset class now numerous storm clouds are positioned on the horizon. First, historically low interest rates since the financial crisis have encouraged companies to issue debt for share repurchases, acquisitions and other corporate purposes. Moreover, BBB-rated bonds which are one step above high yield have ballooned to roughly $3.4 trillion and are 2.8 times the total high yield market. If there are a multitude of downgrades in the BBB space during the next recession, it will cause forced selling as many institutional investors will have to exit their high yield holdings to maintain investment grade credit quality. To make matters worse, due to regulations that were enacted after the financial crisis, broker-dealers are limited in the inventories they can hold which means major buyers during times of stress are no longer available and further diminishes liquidity in an already-illiquid asset class. It is our expectation that high yield bonds will experience excessive spread widening through the next economic downturn due to elevated supply and limited demand dynamics and it is our preference to favor high quality fixed-income securities at the current stage of the business cycle.

COMING UP NEXT WEEK		Est.
04/29 Personal Income MM	(Mar)	0.4%
04/29 Consumption, Adjusted MM	(Mar)	0.7%
05/01 ISM Manufacturing PMI	(Apr)	54.8
05/02 Factory Orders MM	(Mar)	1.3%
05/03 Non-Farm Payrolls	(Apr)	180k
05/03 ISM N-Mfg PMI	(Apr)	56.8

For more information about our solutions: http://peapackprivate.com