The Weekly

Economic & Market Recap

Peapack-Gladstone Bank, Private Wealth Management

February 23, 2018

As of 02/23/2018		Wk	Wk		YTD	12 Mos
		Net	%	Div	%	%
STOCKS	Close	Change	Change	Yield	Change	Change
DJIA	25,309.99	90.61	0.36	2.09	2.39	21.62
S&P 500	2,747.30	15.08	0.55	1.87	2.74	16.21
NASDAQ 100	6,896.60	125.94	1.86	0.99	7.82	29.33
S&P MidCap 400	1,904.23	3.04	0.16	1.52	0.19	9.79
Russell 2000	1,549.17	5.62	0.36	1.32	0.82	11.01

TREASURIES	Yield	**FOREX**	Price	Wk %Change
2-Year	2.24	Euro/Dollar	1.23	-0.93
5-Year	2.62	Dollar/Yen	106.88	0.52
10-Year	2.87	Sterling/Dollar	1.40	-0.56
30-Year	3.16	Dollar/Cad	1.26	0.68

Source: Thomson Reuters & Bloomberg

What Caught Our Eye This Week

Yesterday, the European Central Bank (ECB) released the minutes of the January meeting of its Governing Council (similar to our Federal Open Market Committee). The committee has agreed to delay announcing any changes to its 2.5 trillion euro bond-purchasing policy that began over three years ago which aimed to keep interest rates low and spur economic growth. The European Union (EU) has a critical impact on global interest rates because the trading block constitutes about 23% of global commerce – almost the same size of the United States' economic influence. The EU is exhibiting strong GDP growth (2.7% in Q4 2017), solid consumer spending, the highest consumer confidence in 17 years, and the lowest unemployment in 9 years. Despite this strength, inflation is forecasted to rise only a modest 1.5% this year; and since the beginning of 2017, the euro has appreciated over 19% relative to the U.S. dollar. A strong euro is a headwind for Europe because it makes goods sold abroad expensive and reduces inflation domestically due to lower import prices. According to analyst estimates, the ECB is expected to continue its bond purchases through the end of this year – probably in volumes that begin to decrease during the fourth quarter. The ECB is then expected to slowly begin to lift interest rates in the latter half of 2018.

Economy

It was an uneventful week for economic data, and the main focus was on existing home sales data which was released on Wednesday. These figures came in below expectations and there also were downward revisions for November and December. January sales numbers declined by 3.2% at an annual rate to 5.38 million units. Over the past 12 months, these sales have declined by 4.8%. Existing home sales declined in all the major regions, and inventories have now been lower on a year-over-year basis for 32 consecutive months. The median price of an existing home decreased to $240,500 in January, and these prices are up 4.7% year-over-year. In other news this week, the Markit manufacturing PMI increased to 55.9 in February, which was the highest level since late 2014. The Markit services PMI also increased by 55.9. Finally on Thursday we were pleased to see weekly jobless claims decline by 7,000 to 222,000 during the week ending February 17th. The four-week moving average is now at 226,000. Weekly jobless claims have now been below 300,000 for 155 consecutive weeks, the longest streak since the 1970s.

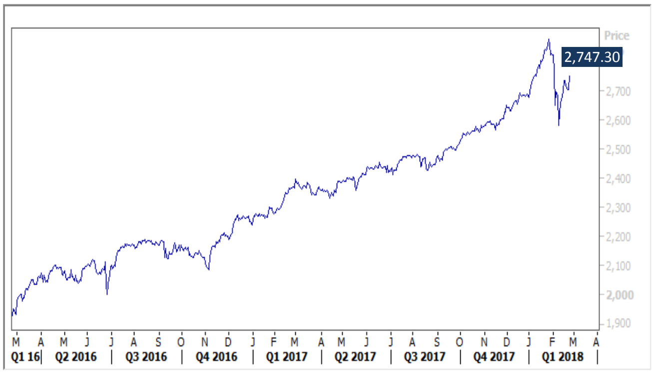
Fixed Income/Credit Market

The march of the 10-year U.S. Treasury towards 3% culminated on Wednesday at 2.95% immediately following the release of the FOMC meeting minutes. Despite stronger than expected growth and inflation, the Fed is committed to a gradual pace of rate increases. As long as economic data does not have any surprises to the downside over the coming weeks, it now seems inevitable that the 10-year Treasury will breach 3%. Market participants are trying to sort out whether the benchmark will retreat from recent highs or if a move past 3% is a signal for a sharp move higher. According to Bloomberg's forward curve matrix, the 10-year Treasury 5-years forward is forecasted to be 3.27% which is not indicative of a sharp move higher. Furthermore, the market is still pricing in approximately three rate hikes over a 1-year horizon – the futures implied Fed funds rate is forecasted to be 2.155% in February 2019.

Equities

Equity markets were slightly positive for the holiday-shortened week. Earnings season is almost complete after approximately 90% of companies in the S&P 500 Index reported their last quarter's results. These were mostly positive with 76% of companies beating earnings expectations showing bottom line growth year-over-year of 15.5%. On the top line, 77% of the group beat analysts' estimates and revenue grew 8.3% year-over-year. Growth style equities gained 1.17% and outperformed value style equities which reported a loss of 0.13% for the week. The top performing sectors for the week were information technology and materials recording gains of 1.61% and 1.34%, respectively. Reflective of value's underperformance this week, consumer staples and telecommunication sectors declined 2.27% and 2.06%, respectively.

S&P 500



Our View

The recent market volatility continued to subside this week as domestic equities traded mostly sideways, U.S. Treasury yields remained relatively range bound (even with $258 billion of new issuance) and the CBOE Volatility Index (VIX) compressed further to roughly 16.5 after spiking to over 50 on February 6th. Even though the domestic economy is on sound fundamental footing (leading economic indicators for January were up 6.2% on a yearly basis), the recent increase in interest rates and wage gains could impact corporate profit margins and weigh on earnings if revenue fails to keep pace. According to Bloomberg, the trailing 12-month profit margin for the S&P 500 is currently 8.84%, which is well above the average of 6.56% dating back to 1990. However, the trailing 12-month S&P 500 profit margin has compressed 46 basis points since the end of August, which corresponds very closely to the recent upward march in U.S. Treasury yields and wage gains. At this point, the market is projecting that further interest rate increases and wage gains will be manageable as earning projections for 2019 are up over 10% compared to the 2018 estimate. We will be keenly focused on monitoring any future modifications to 2019 earnings estimates moving forward.

COMING UP NEXT WEEK		Est.
02/27 Durable Goods	(Jan)	-2.5%
02/27 Consumer Confidence	(Feb)	126.2
02/28 GDP Sales Prelim	(Q4)	3.1%
03/01 Consumption, Adjusted MM	(Jan)	0.2%
03/02 U Mich Sentiment Final	(Feb)	99.0