# The Weekly

## Economic & Market Recap

Peapack-Gladstone Bank, Private Wealth Management

June 1, 2018


| As of 06/01/2018 | | Wk | Wk | | YTD | 12 Mos |
|---|---|---|---|---|---|---|
| | | Net | % | Div | % | % |
| **STOCKS** | Close | Change | Change | Yield | Change | Change |
| DJIA | 24,635.21 | -117.88 | -0.48 | 2.19 | -0.34 | 16.51 |
| S&P 500 | 2,734.62 | 13.29 | 0.49 | 1.91 | 2.27 | 12.52 |
| NASDAQ 100 | 7,083.93 | 123.01 | 1.77 | 0.96 | 10.75 | 21.79 |
| S&P MidCap 400 | 1,958.33 | 11.46 | 0.59 | 1.57 | 3.04 | 12.04 |
| Russell 2000 | 1,647.98 | 21.06 | 1.29 | 1.25 | 7.32 | 18.05 |

| **TREASURIES** | Yield | **FOREX** | Price | Wk %Change |
|---|---|---|---|---|
| 2-Year | 2.47 | Euro/Dollar | 1.17 | 0.02 |
| 5-Year | 2.75 | Dollar/Yen | 109.51 | 0.09 |
| 10-Year | 2.90 | Sterling/Dollar | 1.33 | 0.27 |
| 30-Year | 3.05 | Dollar/Cad | 1.30 | -0.08 |

Source: Thomson Reuters & Bloomberg

### What Caught Our Eye This Week

The U.S. runs a far larger merchandise trade deficit with China than with any other nation but steel is not the reason. The U.S. is the world's largest steel importer. In 2017, the U.S. imported 34.6 million metric tons (MMT) of steel, a 15% increase from 2016 but a 14% decrease from its record high of 40.3 MMT in 2014. The U.S. imports come from 85 countries with 75% coming from just 9 countries. In 2017, the top supplier was Canada (17%) followed by Brazil (14%), South Korea (10%), Mexico (9%), and Russia (8%). Despite producing about half of the world's steel, imports from China were only 2% of the U.S. total steel imports in 2017. The macroeconomic impact of the tariffs on steel and aluminum that went in effect June 1st will likely be small, since they apply to less than 2% of total U.S. merchandise imports. Prior presidents G.W. Bush, Clinton and Reagan also imposed tariffs with little effect. In a market flooded with foreign competition, the tariffs may initially be helpful to American steel and aluminum companies. Ultimately, the retaliatory tariffs on American exports and higher prices for steel and aluminum could negatively impact a range of industries such as construction and manufacturing.

### Economy

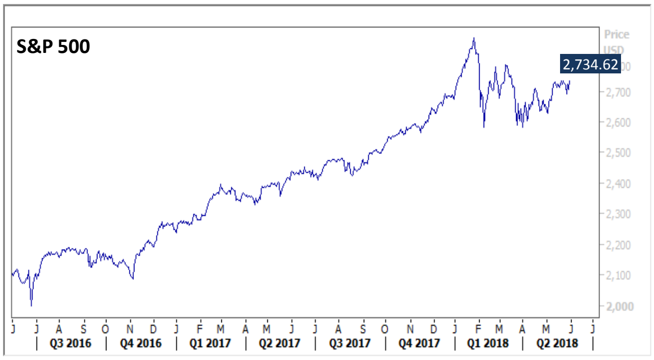
The most anticipated report this week was the nonfarm payroll report, which was released on Friday. This report showed payrolls increasing by 223,000 in May, which was above the consensus forecast of 188,000. The unemployment rate dropped to 3.8% and the U-6 measure of unemployment declined to 7.6%. Average hourly earnings increased by 0.3% and are now up 2.7% year-over-year. The labor force participation rate decreased from 62.8% to 62.7%. Examining the different employment sectors, manufacturing added 18,000 jobs and construction added 25,000. In other news this week, first quarter GDP was reported for the second time and GDP growth dropped from 2.3% to 2.2%. Consumer spending growth was +1.0%, and business spending on equipment was revised up to a 5.5% growth rate. The final read on first quarter GDP will be released on June 28th. On Thursday, personal income and consumption posted impressive gains. Personal income advanced by 0.3% in April, while personal consumption increased by 0.6%. Personal income is now up 3.8% year-over-year and personal consumption is up 4.7%. Disposable personal income has increased by 3.9% over the past 12 months.

### Fixed Income/Credit Market

Using the 10-year U.S. Treasury Note Volatility Index (TYVIX) as a gauge, it was a volatile month for U.S. Treasuries. Month-over-month the TYVIX surged 15.5% from 3.93 to 4.54 peaking at 5.08 on May 29th. On the heels of a rapid sell-off in Italian bonds, most of the volatility came during the last week of the month which caused a flight-to-quality trade in the U.S. Treasury market. Before the holiday weekend, the TYVIX closed at 3.81 then spiked 33.3% during this week's first trading session. The demand for safe-haven assets put downward pressure on U.S. Treasury yields which decreased as much as 18.1 basis points (bps) at the 5-year tenor on Tuesday. The 10-year U.S. Treasury also hit a monthly low on Tuesday and closed at 2.78%, a one-day decrease of 15 bps. By Thursday May 31st, geopolitical fears abated and the 10-year tenor worked its way back up to close May at approximately 2.86%. Despite the recent overall drop in yields, investors in fixed rate assets need to continue taking caution in a rising rate environment.

### Equities

The holiday shortened trading week was eventful as investors had to digest major political, trade and economic headlines resulting in increased volatility in the equity markets. On Tuesday, the S&P 500 index posted its biggest one-day percentage decline in a month over concerns of a political crisis in Italy. The risk-off trade was further driven by downbeat guidance from some large US banks, namely Morgan Stanley which stated that "transactional revenues remain slow after March". Stocks rebounded nicely the following day as concerns abated over political turmoil abroad and a surge in oil prices helped push the energy sector higher. Investor anxiety returned on Thursday after the United States imposed a 25% tariff on steel and a 10% tariff on aluminum on imports from Canada, Mexico and the European Union. The renewed fears of a global trade war triggered the second sell-off in equities for the week led by substantial declines in the consumer staples and industrials sectors. The week ended on a very positive note on the back of strong job and employment data. Equities rallied on Friday and the S&P 500 index finished the week marginally positive. Although political concerns, trade conflicts and interest rate movements have recently rocked equity markets, the underlying fundamentals still appear to be strong. The first quarter is the highest quarterly earnings growth rate in seven years.




### Our View

Despite relatively positive economic releases this week, the financial markets were extremely volatile, buffeted by both geopolitical events in Italy and renewed trade concerns. As the week began, the DJIA dropped over 391 points as anti-establishment political leaders in Italy struggled to form a new coalition government. Some pundits even express concern that rising nationalism in Italy represented an existential threat to the European Union. These fears are significantly overblown. There is legitimate concern regarding the continued weakness of the banking system in the EU, but a fracturing of the EU will not happen over any reasonable investment horizon. Later in the week stocks sold off again as concerns of a trade war emerged with the U.S. announcing tariffs on aluminum and steel imports from Canada, Mexico and the EU. We believe that the prospect of a major trade war developing is remote. It is clearly not in the interests of any of the major developed economies to allow a meaningful trade breakdown, including the U.S. Additionally, there are facilities such as the G7 Summit to ameliorate trade tensions. Canada will host a G7 meeting on June 8-9 with the focus on investing, job creation, advancing gender equality, etc. Easing trade tensions will obviously be an important subtheme. Investors are getting distracted by very low probability events that pose a significant tail risk. In our view, we think investors should be focused on economic fundamentals which remain solid. The real threat to the market is potential rising inflation expectations and central bank normalization.

| COMING UP NEXT WEEK | | Est. |
|---|---|---|
| 06/04 Factory Orders MM | (Apr) | -0.5% |
| 06/05 ISM N-Mfg PMI | (May) | 57.5 |
| 06/07 Consumer Credit | (Apr) | 14.0B |

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