The Weekly

Economic & Market Recap

Peapack-Gladstone Bank, Private Wealth Management

August 10, 2018

As of 08/10/2018		Wk	Wk		YTD	12 Mos
		Net	%	Div	%	%
STOCKS	Close	Change	Change	Yield	Change	Change
DJIA	25,313.14	-149.44	-0.59	2.15	2.40	15.88
S&P 500	2,833.28	-7.07	-0.25	1.83	5.97	16.20
NASDAQ 100	7,408.30	12.82	0.17	0.97	15.82	27.99
S&P MidCap 400	1,996.02	-4.02	-0.20	1.52	5.02	16.87
Russell 2000	1,686.80	13.43	0.80	1.33	9.85	22.90

TREASURIES	Yield	**FOREX**	Price	Wk %Change
2-Year	2.60	Euro/Dollar	1.14	-1.37
5-Year	2.75	Dollar/Yen	110.92	-0.32
10-Year	2.88	Sterling/Dollar	1.28	-1.87
30-Year	3.03	Dollar/Cad	1.31	1.16

Source: Thomson Reuters & Bloomberg

What Caught Our Eye This Week

Due to rising incomes, plentiful jobs, and high levels of consumer confidence in the United States, consumer spending has become robust. This along with other demand drivers has generated a flood of business for companies involved with retailing, energy, mining, construction and manufacturing. Companies have worked many years to streamline their supply chains to reduce any slack and to lower costs. This tight capacity is now producing significant backlogs of supplies, components and services all along the supply chain. In order to remediate these backlogs, companies are frantically trying to increase capacity and hire all types of skilled workers to include machinists, welders, robotics engineers and truck drivers. Given that the unemployment rate is now at 3.9%, skilled workers are difficult to find. In the transportation industry, due to the lack of trucks and drivers, rates on the spot truck market in July increased 29% from the prior year. Additionally, in July, trucking companies ordered three times the number of new class 8 trucks (big rigs) that they ordered during the same month last year. All of this economic activity is driving up prices and ultimately creating delays for product delivery. We are clearly in the latter half of this economic cycle.

Economy

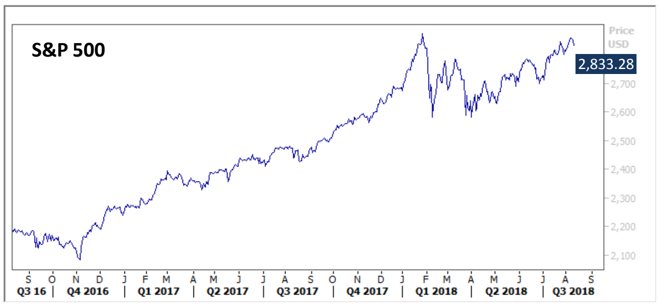
This week the economic data was centered around inflation statistics with the release of the producer price index and the consumer price index. On Thursday, the PPI figures came in below expectations with no change during the month of July. Over the past 12 months, this metric has increased by 3.3%. The core PPI which excludes food and energy increased by 0.1% and is now up 2.7% year-over-year. The biggest influence on the headline figure was energy prices which declined by 0.5%. The consumer price index was reported on Friday and showed an increase of 0.2% in July, which was in line with expectations. Over the past year, this index has increased by 2.9%. The core CPI also increased by 0.2% and is now up 2.4% year-over-year. Owner's equivalent rent (the shelter index) had the largest influence on the headline figure, rising by 0.3%. On Tuesday, the JOLTS report (job openings and labor turnover survey) showed 6.7 million job openings in June. The jobs opening rate came in at 4.3%, and the quits rate edged down to 2.3%. This report also showed a net employment gain over the past 12 months of 2.5 million.

Fixed Income/Credit Market

This time last year investors were inundated by headlines speculating over the timing of the Fed's balance sheet reduction and its potential impact on the U.S. Treasury yield curve. After several months of forewarning investors about unwinding in the near-term, we received confirmation in September that the Fed would commence the roll-off in October 2017. According to the U.S. Condition of All Federal Reserve Banks Total Assets (FARBAST) Index, the Fed's balance sheet currently stands at $4.26T, a net yearly change of -$211B. To date, the unwinding has been benign and discussions surrounding the roll-off have all but disappeared from the headlines. However, this is subject to change in October 2018 when the Fed is expected to increase its roll-off to $50B/m or $600B/yr. Even at that rate, it will take the Fed a minimum of five years to unwind the balance sheet to pre-crisis levels which was less than $1T at the end of 2Q 2008 when it stood at $893B.

Equities

Equity markets began the week on a positive note supported by strong second quarter earnings results and robust economic fundamentals. On Tuesday, the S&P 500 posted its second highest close in history, just 14 points below its January 26th record. Another noteworthy item came that afternoon in the form of a tweet from Tesla CEO and founder, Elon Musk. He announced that he was considering taking the company private and claimed that the funding for this has already been secured. While shares surged 11% on the news, almost all the gains have since been erased due to skepticism over Musk's remarks. The January S&P 500 record remains intact after escalating geopolitical tensions, trade war fears and a decline in oil prices dragged down equity markets for the remainder of the week. The largest selloff occurred on Friday after a severe decline in the Turkish lira triggered fears that a deepening crisis in Turkey could spread to other global economies. The three major equity indexes finished the day down more than 0.7% which pushed the S&P 500 into negative territory for the week. The worst performing sector of the week was consumer staples (-1.9%) and the best performing was telecommunications (+2.14%).



Our View

Financial markets have been remarkably resilient throughout the bull market run. In only a handful of notable periods have an investor's confidence and resolve been tested. The "taper tantrum" which resulted from the Fed's decision to gradually reduce the size of quantitative easing in 2013 was one such example. As we approach the mid-term elections, it would not be unusual for market volatility to increase. There is typically an identifiable catalyst that creates some uncertainty in the markets that precipitates a market drawdown. As we examine the horizon for potential investment risks, the most obvious concerns are a policy mistake by a major central bank or a full-blown trade war. The spark that causes a correction, however, is often less obvious (e.g. a currency crisis in a small emerging market economy). This week the equity markets sold off on Friday due to the dramatic plunge of the Turkish Lira. Turkey depends heavily on borrowing from foreign sources to fund growth, so its economy can be damaged by capital flight creditors lose confidence. Additionally, Turkey does not have the necessary reserves to pay foreigners back. Turkey's economy has overheated, with inflation running at an astonishingly high 16%. The market's risk appetite can be damaged for a time by the deepening problem of an emerging economy like Turkey. In our view, Turkey is unlikely to lead to a systemic economic issue, but it is worth paying attention to.

COMING UP NEXT WEEK		**Est.**
08/15 Retail Sales	(Jul)	0.1%
08/15 Industrial Production MM	(Jul)	0.3%
08/15 Capacity Utilization MM	(Jul)	78.2%
08/16 Philly Fed Business Index	(Aug)	22.0
08/17 U Mich Sentiment Prelim	(Aug)	97.9

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