Peapack Private Wealth Management

September 6, 2019

09/06/2019		Wk	Wk		YTD	12 Mos
		Net	%	Div	%	%
STOCKS	Close	Change	Change	Yield	Change	Change
DJIA	26,797.46	394.18	1.49	2.28	14.88	3.17
S&P 500	2,978.71	52.25	1.79	1.92	18.82	3.12
NASDAQ	8,103.07	140.19	1.76	1.02	22.12	1.35
S&P MidCap 400	1,911.51	30.31	1.61	1.78	14.94	-6.23

TREASURIES	Yield	**FOREX**	Price	Wk %Change
2-Year	1.54	Euro/Dollar	1.10	0.32
5-Year	1.43	Dollar/Yen	106.78	0.59
10-Year	1.57	GBP/Dollar	1.23	1.11
30-Year	2.06	Dollar/Cad	1.32	-0.36

Source: FactSet

What Caught Our Eye This Week

Outside of a clear resolution on trade talks with China, which global equity markets viewed more optimistically this week, the largest concern on investors' minds is whether the U.S. economy will fall into recession within the next year. While the inversion of the U.S. Treasury yield curve (as measured by the spread between 3-month bills and 10-year bonds) suggests an elevated risk of recession, other economic data are less supportive and do not portend that there will be trouble ahead. Many elements of this morning's employment report remain positive. These include the unemployment rate holding steady at 3.7% and a small increase in average weekly hours worked (+0.1 from July to 34.4). In addition, the U.S. ISM Non-Manufacturing Index released Thursday rebounded to 56.4, above the consensus forecast of 55.3 and up from 53.7 in July. The weighted average of non-manufacturing and manufacturing indices is consistent with GDP growth of just under 2% annualized. This suggests that the domestic economy is holding up and that a recession is not imminent. However, poor fixed investment and weak business confidence are clear risks that could threaten the economy moving forward, especially if trade tensions do not subside.

Economy

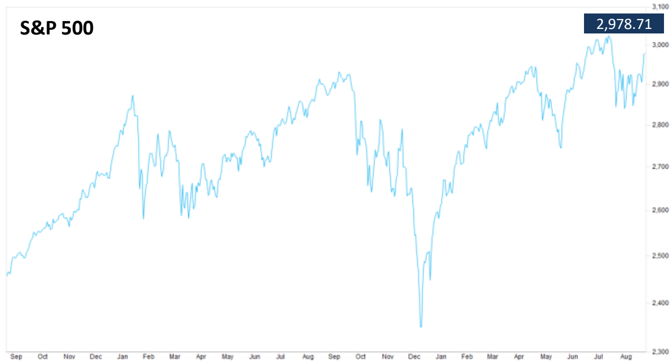
The most anticipated report this week was the nonfarm payroll report, which was released on Friday. This report showed payrolls increasing by 130,000 in August, which was less than the consensus forecast of 160,000. The unemployment rate was unchanged at 3.7% and the U-6 measure of unemployment increased from 7.0% to 7.2%. The labor force participation rate inched up to 63.2%, as the household survey measure of employment increased by a massive 590,000. Average hourly earnings gained 0.4% month-over-month, making the advance over the past 12 months now at 3.2%. Examining the different employment sectors, manufacturing added 4,000 jobs, healthcare gained 24,000 and professional and business services added 37,000. Also this week, the ISM manufacturing survey declined to 49.1 in August, which was the first time this metric slipped below 50 since August of 2016. Later in the week, the ISM nonmanufacturing survey surprised to the upside posting a 56.4 in August, comfortably above consensus expectations.

Fixed Income/Credit Market

The U.S. Investment-grade (IG) primary market was in focus this week with issuers selling $74B worth of bonds through Thursday. With financing costs near record lows and $16T of negative yielding securities across Europe and Asia, lower yields have done little to spur demand from investors in U.S. IG debt. Furthermore, yields on U.S. IG bonds have an average yield to worst (YTW) of 2.77% whereas ten years ago IG bonds yielded an average of 5.09%. Despite the abundance of supply, IG credit spreads remain roughly 23 basis points (bps) lower than the ten-year average at 120 bps which has supported outsized price gains. The Bloomberg Barclays US Investment Grade Corporate Bond Index has provided investors with a year-to-date total return of 13.4% which is a far cry from the 2.5% of losses in 2018. After U.S. Treasury yields spiked as much as 10.8 bps at the 5-year tenor on Thursday on Brexit delays, positive trade talks, and stronger than expected economic data it will be interesting to see if the deluge of IG corporate supply continues.

Equities

Domestic equities continued their upward trajectory during the holiday-shortened trading week with the S&P 500 gaining over 1.75%. Following four consecutive weeks of declines, stocks have now posted back-to-back weekly gains. On Tuesday, equities sold off after the U.S. implemented tariffs on roughly $110 billion of Chinese goods over the weekend. A weak ISM manufacturing number also contributed to the risk-off sentiment. That quickly changed the following day mainly due to Hong Kong's withdrawal of its controversial extradition bill that triggered nearly three months of social unrest. Stocks continued to rally on Thursday and all three major indices finished the day up over 1.25%. Confirmation of the U.S. and China agreeing to hold face-to-face talks in early October as well as upside surprises in U.S. economic data fueled the risk-on atmosphere. All sectors were in the green for the week with energy leading the pack gaining 2.64%.



Our View

Over the past decade, global central banks have reduced interest rates in aggregate more than 700 times and pumped trillions of dollars into the economy through bond purchases. Even with the extraordinarily accommodative monetary policy previously described, price pressures in major developed economies remain muted and fall short of policymakers' inflation targets. The Fed's preferred measure of inflation is core personal consumption expenditures (PCE) and ultimately looks to achieve a symmetric target of 2.0%. Over the past ten years, core PCE has averaged approximately 1.60% and has only breached 2.0% briefly in 2011-2012 and 2018. Given the economic deterioration abroad (particularly in the manufacturing sector) and subdued inflation pressures, the Fed has embarked on a new rate cutting path. However, the market has doubts that the Fed will be able to resuscitate inflation through conventional rate cuts as the 10-year break-even inflation rate currently resides at roughly 1.55% – 46 basis points below its mean over the past decade. With current monetary policy tools appearing incapable of reigniting inflation, there has been renewed talk of a concept called helicopter money that could potentially help drive inflation higher. Helicopter money was coined back in 1969 by Milton Friedman. The idea centers on the one-time creation of money by the central bank that is either directly deposited into individual's bank accounts or obtained through tax rebates. The theory is that consumers now flush with new funds will go out and spend, which will drive up demand and cause prices to rise. One of the main shortfalls of helicopter money is that it devalues the currency due to the increase in money supply and could lift inflation beyond its intended target. Nevertheless, the potential implementation of helicopter money is a long way off and accommodative monetary policy coupled with fiscal stimulus remains the safest way to solve the inflation predicament.

COMING UP NEXT WEEK		**Est.**
09/11 PPI SA M/M	(Aug)	0.10%
09/12 CPI SA M/M	(Aug)	0.10%
09/13 Retail Sales SA M/M	(Aug)	0.10%
09/13 Michigan Sentiment NSA (Preliminary)	(Sep)	91.0

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