Peapack Private Wealth Management

June 26, 2020

6/26/2020		Wk	Wk		YTD	12 Mos
		Net	%	Div	%	%
STOCKS	Close	Change	Change	Yield	Change	Change
DJIA	25,015.55	-855.91	-3.31	2.62	-12.34	-5.77
S&P 500	3,009.05	-88.69	-2.86	2.01	-6.86	3.14
NASDAQ	9,757.22	-188.91	-1.90	0.88	8.74	23.75
S&P MidCap 400	1,719.32	-65.40	-3.66	2.08	-16.66	-9.57

TREASURIES	Yield	**FOREX**	Price	Wk %Change
2-Year	0.17	Euro/Dollar	1.12	0.17
5-Year	0.30	Dollar/Yen	107.33	0.34
10-Year	0.65	GBP/Dollar	1.23	-0.38
30-Year	1.37	Dollar/Cad	1.37	1.09

Source: Bloomberg/FactSet

What Caught Our Eye This Week

Supply disruptions in the sugar market have prices for the sweetener poised for their best quarter since June 2016. Raw sugar futures traded recently at $0.12 per pound on the New York Mercantile Exchange (NYMEX), up 13% since March 31st. The price of sugar often mirrors the price of energy (sugar crops can be processed into ethanol, a biofuel sometimes used to power engines), so the rally in energy markets has also lifted sugar prices. Traders caution, however, that the burst in prices has not been driven by fundamental factors and may be short-lived. Brazil (the world's largest producer) is increasing output and any further coronavirus lockdowns portend a potential drop in demand as people cut back on dining out, going to the movies, and attending sporting events. While consumption levels can be tricky to forecast, demand is thought to be closely tied to economic growth. Both lockdowns and changes in consumer behavior have led to a drop in global sugar consumption of approximately 2.1 million metric tons since the beginning of Covid-19 restrictions. While analysts expect the rise in prices to subside as Brazil increases its forward-year production by 9.6 million metric tons, any elongated Covid-19-related restrictions could easily overwhelm the increased supply.

Economy

This week we observed a full economic calendar starting with existing home sales data on Monday. Existing home sales dropped 9.7% in May to 3.91 million units at an annual rate. This level is the lowest going back to October of 2010, and overall these sales are down 26.6% year-over-year. On the positive side the median price of an existing home increased to $284,600, which is a gain of 2.3% over the past twelve months. Orders for durable goods were posted on Thursday and surged 15.8% easily beating expectations. The headline figure was inflated by defense orders, which were up 20.4%, but "core" orders and shipments registered strong advances rising 2.3% and 1.3%, respectively. On Friday, personal income and personal consumption data were released displaying wide divergences. Personal income decreased by 4.2% in May while personal consumption increased by 8.1%. Wages and salaries rebounded by 2.7% and the personal savings rate declined from an all-time high (32.2%) in April to 23.2% in May. Government transfer payments dropped by 17% and when excluding these numbers from the personal income data, personal income was up 1.6%.

Fixed Income/Credit Market

Interest rates across the U.S. Treasury (UST) curve rallied back this week decreasing as much as 8.7 basis points (bps) at the 30-year tenor. The flight-to-quality trade was precipitated by a resurgence of Covid-19 cases in several states in the U.S. as well as some other hot spots abroad. Exacerbating the rally are potential trade conflicts between the U.S. and Canada as well as the U.S. and the European Union. Week-over-week the benchmark 10-year Treasury Note dropped 5.5 bps to approximately 0.64% which decreased the slope of the 2-year and 10-year curve 3.4 bps to a spread of 47.3 bps. The historically low level of U.S. Treasury yields and the global uncertainties facing us today make striking the right balance between risk and reward challenging. Investors seeking the safety and security of U.S. Treasuries should consider the 7-year UST for curve positioning with the 2-7-10 butterfly spread currently trading at 16.6 bps. A common strategy for active fixed income traders is to buy the middle tenor of the butterfly and sell the wings when butterfly spreads are positive.

Equities

Heightened volatility continued to put downward pressure on stocks this week and all three major domestic equity indexes finished sharply in the red. It was relatively quiet earlier in the week as stocks crept higher with the Nasdaq Composite posting a new all-time high on Tuesday. The upward trend quickly reversed the following day over concerns of a coronavirus resurgence and the possibility for a rollback on the reopening of the economy. Regional spikes in new coronavirus cases in areas such as the Southern and Western states pushed U.S. daily new coronavirus cases to a fresh national record. Equities regained some of their losses on Thursday due to a late-afternoon rally which was led by bank stocks due to a rollback of some Volcker Rule restrictions. The rally was short-lived and stocks sold off sharply on Friday after the Federal Reserve released its annual stress test of major banks. The test showed that some banks could get close to their minimum capital level requirements in scenarios tied to the coronavirus pandemic. Furthermore, the Fed is requiring the big banks to suspend share buybacks and cap dividend payments at current levels for the third quarter. All sectors finished the week lower with technology being the relative outperformer and energy being the relative under-performer.

Our View

The performance divergence between the major equity market indexes during the stock market's recovery has continued. The discrepancy between many indexes is at levels we have not seen in many decades. For example, the Dow Jones Industrial Average is down roughly 10% from the beginning of the year, yet the tech-laden Nasdaq Composite has rallied almost 12%. Large-cap stocks have decisively outperformed small-cap stocks with a performance differential of 10.7% on a year-to-date basis and 12.8% over the last 12 months. The divergence between growth and value has been even more staggering as large-cap growth stocks (Russell 1000 Growth) have outpaced large-cap value (Russell 1000 Value) by more than 24% in 2020. We have highlighted market divergences in the past as they are often reconciled in a market downdraft causing a change in market leadership. Many strategists consider significant market divergences as a warning sign for volatility ahead.

Another type of divergence that we are also becoming concerned with is the disparate impact the recession is having on personal income and savings. Across the major industrialized countries, according to Capital Economics, employment has fallen by over 55 million, and another 35 million have been furloughed. In the U.S. alone more than 20 million workers have already lost their jobs. The pandemic has devasted workers in some industries such as restaurants, travel, leisure, and retail. Workers in other industries have been largely unaffected from an employment and income perspective. Shuttered retail shops and businesses have not allowed those who have retained their jobs to spend their earnings as they ordinarily would. These workers have experienced an involuntary rise in their savings. Because a disproportionate number of people in lower-wage service jobs have been negatively affected by the recession, the underlying problem of income inequality and the growing economic chasm between the wealthy and the middle class will only get worse due to the economic downturn. The structural causes of income and wealth inequality have been in place for decades, but the issue seems to be coming to ahead and is likely to be a major subject in the November election.

COMING UP NEXT WEEK		Consensus	Prior
06/30 Consumer Confidence	(Jun)	90.0	86.6
07/01 ISM Manufacturing SA	(Jun)	48.5	43.1
07/02 Nonfarm Payrolls SA	(Jun)	2,500K	2,509K
07/02 Durable Goods SA M/M (Final)	(May)	13.1%	15.8%

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