The Weekly

Economic & Market Recap

Peapack-Gladstone Bank, Private Wealth Management

June 16, 2017

As of 06/16/2017		Wk	Wk		YTD	12 Mos
		Net	%	Div	%	%
STOCKS	Close	Change	Change	Yield	Change	Change
DJIA	21,384.28	112.31	0.53	2.32	8.21	20.59
S&P 500	2,433.15	1.38	0.06	1.96	8.67	17.08
NASDAQ 100	5,681.48	-60.47	-1.05	1.13	16.82	28.42
S&P MidCap 400	1,753.46	-4.08	-0.23	1.69	5.59	18.57
Russell 2000	1,406.73	-14.98	-1.05	1.45	3.64	22.50

TREASURIES	Yield	**FOREX**	Price	Wk %Change
2-Year	1.32	Euro/Dollar	1.12	-0.07
5-Year	1.74	Dollar/Yen	110.83	0.43
10-Year	2.15	Sterling/Dollar	1.28	0.20
30-Year	2.77	Dollar/Cad	1.32	-1.92

Source: Thomson Reuters & Bloomberg

What Caught Our Eye This Week

The stock market is made up of many investing participants who are constantly trying to anticipate the profitability of companies (earnings) in the future. At any given point in time, there is a published consensus of analyst earnings estimates for each company. Over the long term, the prices of stocks reflect the present value of these discounted earnings that are expected in the future. Generally speaking, as companies' prospects change over time, it is the revisions to these earnings estimates that have the greatest impact on the change in stock prices. Since the beginning of this year, information technology companies on average increased in price by 15.4%, the highest of any sector. It is no coincidence that technology sector earnings estimates were also revised upward by 4.4%, the most of any other sector this year. The energy sector this year declined in price by 12.3%, the worst of any sector. It is also interesting to observe that the energy sector had one of the worst estimate revisions of all the sectors, a decline of 7.0%. In the short term, the relationship between price movements and estimate revisions may not always be in sync, but over the long term, the correlation is quite strong.

Economy

This week offered an abundance of economic news with most of the data arriving in on the soft side of the ledger. Starting on Wednesday, retail sales declined 0.3% in May, which was the largest drop in 16 months. Retail sales have increased 3.8% year-over-year. The all important control category which excludes food service, autos, gas and building materials was unchanged. Overall, only four of 12 retail subsectors posted gains. Department stores had their biggest drop since July of 2016 and restaurant spending has receded now for four consecutive months. Once again, non-store retailers dominated the landscape making up 10.9% of total retail sales. Also on Wednesday the consumer price index declined for the second time in three months dropping 0.1% in May. The "core" CPI increased by .06%, but over the last three months this heavily scrutinized metric is flat, a development that has happened just three other times in the past 50 years. Over the past 12 months, "core" CPI is up 1.7%. Thursday brought us industrial production figures and these numbers were unchanged in May while manufacturing output decreased by 0.4%. The lone bright spot was mining output which increased by 1.6%. Finally, weekly jobless claims showed a drop of 8,000 to 237,000 during the week ending June 10th. The four-week moving average is now at 243,000.

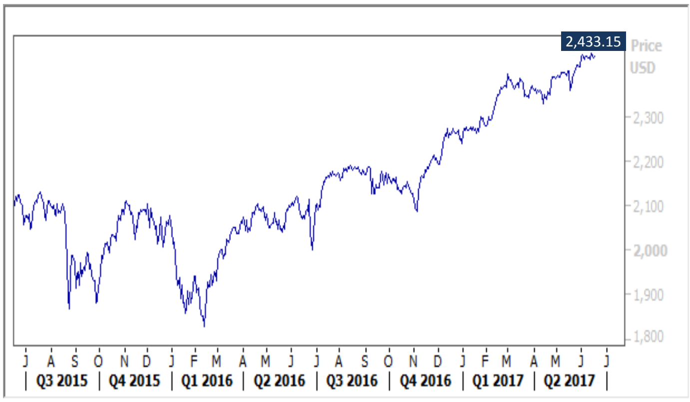
Fixed Income/Credit Market

On Wednesday the FOMC increased the Fed Funds rate for the second time this year. Similar to the last three rate hikes, interest rates actually compressed approximately 6 bps at the 10Y tenor to 2.15% from Tuesday's close of 2.21%. According to Bloomberg, the implied probability of a September rate hike is now only 16%, calling into question whether or not the Fed can achieve the three 25 bp rate hikes they were targeting in 2017. The FOMC also released some details on how they expect to normalize their $4.3 trillion balance sheet. Moreover, caps will be in place in order to gradually runoff the balance sheet starting with $10B a month initially, and slowly increasing over 12 months until it reaches $50B per month. Decreasing the size of the Fed balance sheet at a gradual pace will allow the market to absorb the added supply and mitigate a significant disruption to the interest rate landscape.

Equities

The U.S. equity market started the week on a down note, as the selling in technology companies continued. The energy sector also contributed to early week losses as oil inventory levels remained elevated. With the summer driving season upon us, gasoline prices should be rising; but due to stubbornly high inventory levels, prices have stayed low. The mid-week Federal Reserve meeting resulted in the expected increase in the Fed Funds rate, acted as a catalyst for strength in the financial sector. The Fed rate increase was quickly followed by banks raising their prime lending rate to 4.25%. On the whole, the major stock indexes did not show much movement for the week, although the underlying sectors were extremely volatile. Industrial companies rose despite weak manufacturing output, and utilities and real estate companies also did well. On Friday, Amazon announced its plans to buy Whole Foods for almost $14 billion which caused shares of other grocery retailers to sell off dramatically due to the fear of Amazon's encroachment.

S&P 500



Our View

Dominating the financial news this week was the Federal Reserve's decision to raise its target on the Fed Funds rate by one quarter of a point to between 1 and 1.25 percent. The Fed also gave specifics regarding its plan to reduce the $4.3 trillion balance sheet. Notably, the yield curve continued to flatten. Over the last three months, the Treasury 2-to-10 year spread has contracted 40 basis points (bps) to 83 bps. The Fed's three rate increases over the last six months and anticipated future rate hikes have lifted the short end of the yield curve. Declining inflation expectations and a weaker first half domestic economic environment have caused yields for longer maturities to decline. The 2-to-10 year spread that we monitor closely is a predictor of economic health. It would be disconcerting to see this indicator continue to decline, especially with implied 5-year inflation expectations at 1.50%. Indicators that have been reliable in the past may have less predictive value in the future due to the market distortion caused by global central banks.

COMING UP NEXT WEEK		**Est.**
06/21 Existing Home Sales	(May)	5.54M
06/21 Existing Home Sales % Chg	(May)	-0.5%
06/22 Initial Jobless Claims	(Jun)	240k
06/23 Markit Mfg PMI	(Jun)	53.0
06/23 New Home Sales – Units	(May)	0.600M

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