Peapack Private
Wealth Management

The Weekly
Economic & Market Recap

June 24, 2022

6/24/2022		Wk Net	Wk %	Div	YTD %	12 Mos %
STOCKS	Close	Change	Change	Yield	Change	Change
DJIA	31,500.68	1611.90	5.39	2.10	-13.31	-7.88
S&P 500	3,911.74	236.90	6.45	1.64	-17.93	-8.31
NASDAQ	11,607.62	809.27	7.49	0.87	-25.81	-19.22
S&P MidCap 400	2,334.40	113.91	5.13	1.76	-17.86	-13.60

TREASURIES	Yield	**FOREX**	Price	Wk %Change
2-Year	3.06	Euro/Dollar	1.05	0.83
5-Year	3.18	Dollar/Yen	135.22	-0.06
10-Year	3.13	GBP/Dollar	1.23	0.90
30-Year	3.26	Dollar/Cad	1.29	-1.21

Source: Bloomberg/FactSet

What Caught Our Eye This Week

The four-month-old war in Ukraine continues to impact inflation in the food and energy markets as well as the United States' foreign aid commitments. Military success in this consequential conflict could ameliorate many of the challenges that are impacting the global economy. Since early April, the fighting has shifted to the Eastern part of Ukraine and can be characterized as a war of attrition, with the Russian Army capitalizing on its 10-to-1 artillery advantage and its ability to effectively resupply its operations. According to the International Monetary Fund, Ukraine's economy is estimated to decline by 35% this year. This in turn is solidifying its reliance on international aid. Since the start of the war, the U.S. has committed $5.6 billion in direct military assistance to Ukraine. Some of this aid was included in the $40.1 billion Ukrainian aid bill which Congress approved and President Biden signed in May. Beyond the military assistance which primarily includes combat equipment and munitions, the package authorized significant sums for other purposes such as intelligence support, the deployment of U.S. troops to Eastern European countries, humanitarian aid, economic assistance, and money to help pay for scarce food. Since the war began, the European Union has provided $2.1 billion in direct military assistance to Ukraine, and individual European countries have independently provided several billion dollars' worth of military equipment. Much more is needed to sustain Ukraine's efforts, but the level of global cooperation is encouraging.

Economy

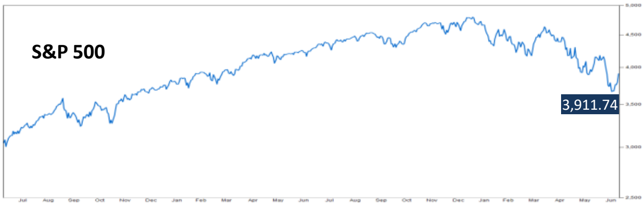
On Tuesday, the May existing home sales report showed a decline of 3.4% during the month to a 5.410 million annual rate, marginally beating expectations of 5.400 million. Existing home sales have now declined for four consecutive months, and sales are down 8.6% compared to a year ago. Despite the decline in sales, the median price of an existing home rose to $407,600 in May and is up 14.8% year-over-year (YoY). On Thursday, the S&P Global U.S. PMI report signaled further easing in the rate of expansion in business activity during the month of June. The U.S. Services PMI declined to 51.6 from 53.4 in May, the lowest in five months and well below forecasts of 53.5. In addition, the U.S. Manufacturing PMI declined to 52.4 from 57.0 in May, well below consensus expectations of 56.3. In other news, new single-family home sales increased 10.7% in May to a 0.696 million run rate, easily beating consensus expectations of 0.590 million. The increase in new home sales during May broke a four-month losing streak.

Fixed Income/Credit Market

U.S. Treasury Note yields rallied this week following Fed Chair Powell's testimony to Congress regarding the state of the economy. The benchmark 10-year Treasury yield dropped approximately 9.5 basis points (bps) to 3.13% after reaching a decade high of roughly 3.48% ten days ago. The likelihood of a recession, due to the Fed's commitment to curb inflation, is expected to put pressure on corporate balance sheets which caused credit spreads to widen significantly the last several weeks. Thus far in June, investment grade (IG) option adjusted spreads (OAS) have increased 19 bps to 149 bps. Meanwhile the move higher in HY OAS has been much more dramatic at +119 bps to 525 bps. More specifically, during the same period, 5-year AA, A, and BBB-rated composites increased 14, 15.6, and 18.4 bps, respectively. Furthermore, 5-year BB and B-rated composites widened 90.6 and 106.1 bps, respectively in June.

Equities

Following last week's selloff, U.S. equities began the holiday-shortened week with a rally, closing sharply higher. There was no clear catalyst behind the bounce, but oversold conditions and depressed sentiments may have played a role. Wednesday was uneventful with little to no change, closing slightly lower. There was some strength on Thursday, although narratives remained fixated on negative earnings revisions, monetary policy tightening, inflation, and recession uncertainties. The week finished strong, ending the three-week losing streak as the S&P 500, Dow, and Nasdaq gained +6.45%, +5.39%, and +7.49%, respectively. Energy was the only sector to record a loss, down -1.55%. Growth stocks outperformed value.



Our View

The financial market conversation has centered around inflation and the Federal Reserve for six months. At the heart of the discussion is the central question of how much damage the Fed will do to the economy to bring inflation back to an acceptable level. We have argued that the Fed is relatively early in its tightening cycle. The Fed funds rate remains well below the neutral rate, that is neither expansionary nor constrictive, and the process of quantitative tightening has only just begun. The Fed will not reach its monthly balance sheet runoff target until September. Despite the early stage of the tightening, the economy has already been impacted and has begun to slow. In anticipation of a more aggressive policy stance by the central bank, interest rates for mortgages, automobiles, corporate debt, and many other things have meaningfully risen, which is starting to bite into demand. We received more evidence of broad base slowing last week. The U.S. Composite Purchasing Managers Index (PMI), which encompasses both the manufacturing and service sectors, fell to 51.2 in June from 53.6. Although any reading above 50 suggests expansion, the indicator has fallen in the last five months and is trending in the wrong direction. The disappointing Composite PMI number follows the prior week's decline in retail sales, with consumer spending being pinched by higher energy costs. Retail sales in May fell 0.3%, the first decline in month-over-month spending this year. The equity market is also confirming an economic slowdown. Over the last three months, economically sensitive sectors such as consumer discretionary (-23.0%) and industrials (-16.1%) have lagged the general market. Defensive sectors, such as utilities (-4.5%), healthcare (-5.2%) and staples (-3.5%), have significantly outperformed. Earnings expectations have not reflected any meaningful slowdown. On the contrary, according to FactSet, earnings estimate for the S&P 500 is higher today than before the first-rate hike in March. We think investors should be cautious and skeptical of market rallies until the slowing of the economy is reflected in earnings estimates. Equities are pricing in a period of economic softness, but it would be unusual for the equity market to make substantial forward progress until there is validation that earnings estimates properly reflect the current economic conditions.

COMING UP NEXT WEEK		Consensus	Prior
06/27 Durable Orders SA M/M (Preliminary)	(May)	0.20%	0.48%
06/27 Pending Home Sales M/M	(May)	-2.5%	-3.9%
06/28 Consumer Confidence	(Jun)	102.0	106.4
06/29 GDP SAAR Q/Q (Final)	(Q1)	-1.5%	-1.5%
06/30 Personal Consumption Expenditure SA M/M	(May)	-	0.90%
06/30 Personal Income SA M/M	(May)	0.50%	0.40%
06/30 Chicago PMI SA	(Jun)	59.0	60.3
07/01 ISM Manufacturing SA	(Jun)	55.0	56.1

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