Weekly Market Update

Favorable economic reports help the market celebrate

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ARTICLE HIGHLIGHTS

- Propelled by strong economic data, the S&P 500 Index hits a series of record highs.
- While fixed-income markets are quiet, the 10-year Treasury closes at 3%.
- Chinese stocks retreat amid downbeat economic news.
- Although U.S. stocks may be due for a breather, their long-term outlook remains good.
- In 2014, the U.S. economy should move toward “escape velocity.”

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The S&P 500 Index celebrated during a holiday-shortened week through December 26 as a series of favorable economic releases helped it reel off three consecutive record finishes. The index is on pace for its best yearly performance since 1997.

Foreign developed- and emerging-market stocks also rose through December 26, based on their respective MSCI indexes.

Japanese stocks advanced, underpinned by the dollar climbing to a five-year high vs. the yen. The Nikkei Index is approaching last spring’s market tops, but its currency-fueled gains seem vulnerable.

Although fixed-income markets were quiet this week in very light trading, Treasury rates moved up in the wake of positive economic numbers. On December 26, the 10-year Treasury yield closed at 3% for the first time since July 2011, and the 30-year Treasury hovered just below 4%, a mark it hasn’t touched since August 2011.

Current market updates are available here.

Strong economic data rolls in

Upbeat economic reports highlight an economy that continues to build momentum:

- New jobless claims fell by 42,000 to 338,000, the biggest drop in more than a year.

Financial Services

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- The final December reading of the University of Michigan/Thomson Reuters consumer-sentiment index hit 82.5, up from a final November level of 75.1.
- Orders for durable goods—big-ticket items designed to last more than three years—increased by 3.5% in November, reversing October's decline.
- Americans shook off rising mortgage rates to purchase new homes at a healthy clip. Meanwhile, the average sales price for a single-family home hit a record high of $340,000.

Discouraging news hurts Chinese stocks

Chinese equity markets endured another down week. For the third year in a row, the country's GDP target was marked down to 7.5%, and renewed attempts by the People's Bank of China to control reckless lending by soaking up excess liquidity may weigh on future growth. The cash crunch caused by the spike of short-term rates in the country's interbank lending market also added to investor concerns. However, the central bank pumped money into the system, which calmed markets late in the week.

Outlook

U.S. equities continued their climb, boosted by brightening economic data as well as the tendency of stocks to perform well in December. In fact, the S&P 500 Index has not had a down day since the Federal Reserve announced its decision on December 18 to taper its quantitative easing asset purchases. But as we have stated before, high levels of bullish sentiment, signs of technical exhaustion (meaning the market may have peaked in terms of demand for stocks), and the rally's length all indicate that equities are due for a breather at some point in the near future. That said, we believe U.S. stocks are poised to hit new highs in 2014.

In fixed-income markets, investors have already "priced in" (or reacted to) both the Fed's taper announcement and the economy's improved economic growth. This has helped temper the recent rise in interest rates.

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Next year, the U.S. economy should move toward “escape velocity”—a sustained economic recovery that is less dependent on the support of the Fed’s extraordinary monetary stimulus but is instead propelled by higher consumer demand, robust employment gains, increasing private investment and, in particular, continued strength of the housing market. Attaining this financial independence should signify the start of a return to more normal economic growth and of a more normalized interest-rate environment.