Weekly Market Update

After hitting another new high, equities mark time

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Article Highlights

- The S&P 500 Index edges higher but spends much of the week treading water.
- Fixed-income markets are mostly quiet, with Treasury yields trading in a narrow range.
- U.S. data highlights include better-than-expected retail sales and a rise in consumer sentiment.
- Europe shows some signs of economic improvement at the margins.
- Chinese equities rally on stimulus hopes that may be overly optimistic.

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Equities

The U.S. equity market continued to reach new highs during the past week, but its advance was slower and more labored. After closing at a record level of 2,038 on Monday, November 10, the S&P 500 Index hovered near that mark for the remainder of the week, through midday trading on November 14. The market's gains were driven by better corporate earnings estimates, slow-but-steady improvement in forward-looking economic data, and an attractive risk premium (i.e., the expected excess return of U.S. equities versus a risk-free alternative such as Treasury bills).

In non-U.S. markets, European stocks rose modestly for the week through November 13 but struggled on the last trading day as investors digested still-weak economic data and falling oil prices, which hurt shares of European oil stocks. Japan's Nikkei 225 Index continued its recent surge, hitting a seven-year high, although this move has been diluted by yen depreciation. The Japanese currency closed the week above ¥116 to the dollar.

Fixed Income

Treasury yields inched slightly higher for the week. The bellwether 10-year yield stayed in a tight range around 2.35% for much of the week, as data releases showed the U.S. economy still on its growth track, while lingering concerns about Europe's frailty helped keep Treasury rate increases in check. Based on Barclays

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indexes, performance across most fixed-income sectors was flat to slightly negative for the week through November 13.

Investment-grade corporate bonds were among the underperformers, hampered by significant supply headwinds. Investor conviction in high-yield debt was weak, preventing a further rally in high-yield spreads, which remained wider than their tightest levels of the year. Despite the past week's relatively muted returns, nearly all fixed-income categories saw inflows.

For additional insights from TIAA-CREF Global Investment Strategist Dan Morris, view our Weekly Market Perspective Video.

Current headline updates are available here.

U.S. economic data remains largely positive

While not yet accelerating to its fullest potential, U.S. economic growth continues along its positive trajectory. Among the past week's favorable data reports:

- **Retail sales** rebounded from September's decline and climbed 0.3% in October, slightly ahead of expectations. Stripping out the effect of falling gasoline prices, retail sales were up a stronger 0.5%—potentially boding well for the upcoming holiday season.
- **Consumer sentiment** jumped to its highest level since mid-2007, based on the University of Michigan/Thomson Reuters preliminary index reading for November.
- **Small-business optimism** also climbed, touching a two-month high in October, according to the National Federation of Independent Businesses.

On the employment front, **initial weekly jobless claims** rose by 12,000, to 290,000, but remained under 300,000 for the ninth consecutive week. Claims at or below this threshold usually signal real GDP growth of 3% or higher. Meanwhile, the number of **job openings** edged slightly lower in September but were 20% higher than a year ago.

Europe's outlook may be improving slightly at the margins

European economic activity, though still subdued, may be close to turning. So far the region has managed to avert another recession: German and French GDP growth came in at 0.1% and 0.3%, respectively, in the third quarter, while Spain grew at a rate of 0.5%. In addition, corporate earnings have been better than expected, equity valuations and expected returns are compelling, and sentiment is very low (often a precursor to a market rally). For these reasons, Europe remains, in our view, the most attractive region for equity investing. Tempering this outlook is the latest flare-up in the Russia-Ukraine conflict, which represents a significant potential risk.

Chinese equities rally despite weaker signals on the economy

In China, there were more signs of economic cooling, with industrial production, retail sales, and leading indicators falling short of expectations. Chinese equities rallied on the assumption that these weak signals will prompt the central bank to add more stimulus to the economy. Such action is far from certain, however, as the week's data, while softer, was not alarming. Moreover, the government is unlikely to act aggressively unless employment growth materially suffers, which so far has not happened. We think the authorities may provide some measure of easing and have approved a number of new infrastructure projects, but on a relatively small scale compared to previous programs. Outside of China, emerging-market equities saw improved performance during the past week. We are increasingly seeing attractively valued opportunities in these markets.

Outlook

Rising consumer confidence on the heels of falling gasoline prices should translate into a surge in consumer spending in the first half of 2015 and provide a tailwind to further employment growth. Continued strengthening of the dollar is now clearly the consensus view, although the enthusiasm for that trade in the futures market has reached extreme levels. Accordingly, we would not be surprised to see a period of dollar weakness to correct that imbalance.

Similarly, in equity markets, positive near-term sentiment is moving back into a zone that warrants caution. Hedge funds' net exposures to equities have risen nearly to levels seen prior to the market's correction in early October. (Higher exposures are typically associated with subsequent downturns.)

We believe fixed-income markets, broadly, will benefit from both domestic and international flows as we enter 2015, given the likelihood of only modestly higher interest rates. The highest-risk fixed-income categories will remain subject to asset price volatility as we transition slowly toward the Federal Reserve's first rate hike at midyear.

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