Weekly Market Update

Greece and the Fed vie for investor attention

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Article Highlights

- The Fed expresses little urgency to raise interest rates and outlines a slow pace of increases.
- U.S. equities withstand Greek woes and rise for the week on the Fed's dovish message.
- European stocks trim the week's losses, also benefiting from the Fed's supportive tone.
- We believe the risk of "contagion" from the Greek debt crisis is low.

June 19, 2015

Equities

Although fears of a Greek default continued to weigh on markets, U.S. equities received a boost from the Federal Reserve. By expressing confidence in the economy while also indicating that the pace of interest-rate increases will be slow (with the possibility of only one rate hike this year), the Fed delivered a dose of positive news. Against this backdrop, the S&P 500 Index rose 1.3% for the week through June 18, before giving back some gains the next day.

In Europe, the Fed's dovish signals provided a respite from concerns over Greece, but stocks still fell 0.6% for the week. Greek shares fared much worse than the region as a whole, plummeting 11%.

Shares in China also plunged amid rising fears of a bubble in the country's volatile equity markets, while Japanese equities declined about 1%.

Fixed income

The Fed's tone was mildly supportive for fixed-income markets. The yield on the bellwether 10-year U.S. Treasury, which moves in the opposite direction of its price, fell from 2.39% at the beginning of the week to close at 2.27% on June 19, amid increased demand for safe-haven assets.

Yields on European sovereign debt weathered the week's uncertainty surprisingly well. Investors seem to be betting that a Greek default, should one occur, will have a much smaller impact now than it would have had several years ago, as

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Eurozone financial markets—including those on the periphery, such as Italy and Spain—are better prepared for such an event.

Returns for U.S. spread products (higher-yielding, non-U.S. Treasury securities) were mostly positive for the week through June 18. However, outflows continued to hurt high-yield bonds, while their investment-grade counterparts also lost ground.

Current updates are available here.

For additional investment insights from TIAA-CREF Global Investment Strategist Dan Morris on the situation in Greece, view our Weekly Market Perspective Video.

The Fed looks to engineer a gradual change in policy

The week was highlighted by the Fed's June policy meeting and Chair Janet Yellen's post-meeting press conference. In addition to holding short-term interest rates near zero, the Fed indicated that the upward move in rates, whenever it begins, will be deliberate—even slower than officials had previously predicted. We were not surprised by the Fed's decision to raise rates gradually, having long believed that any rate increases will be measured and less aggressive compared to previous tightening cycles.

Meanwhile, economic releases during the week were generally mixed to positive. Among the highlights:

- **First-time unemployment claims** dropped 12,000, to 267,000, and the less-volatile four-week moving average also fell, to 276,750. Both remained near 15-year lows.
- The index of **leading economic indicators** published by The Conference Board rose for the third consecutive month in May, a sign the economy is poised to rebound in the second half of the year.
- **U.S. regional manufacturing indexes** were mixed, as the Philly Fed hit its highest level of the year while the Empire State index dipped slightly.
- Although **housing starts** fell by a more-than-expected 11.0% in May after surging in April, **building permits**, a forward-looking indicator, reached their highest level since January 2007. Meanwhile, **homebuilder confidence** hit a nine-month high in June.
- Rising gasoline costs boosted **U.S. consumer prices** in May by the most in over two years (+0.4%). Stripping out volatile food and energy costs, so-called "core" consumer prices rose by only 0.1%.

Outlook

The end game in Greece is approaching. Depositor flight from the country's banks has accelerated, increasing the odds of capital controls. We continue to believe that an agreement between the Greek government and its international creditors will ultimately result, although negotiations could last for months. Even if Greece were to leave the Eurozone (a prospect we still deem unlikely), in our view the country is "ring fenced," meaning the potential for upheaval in Athens to spread to other economies and markets is low.

Along those lines, we were encouraged by the rebound in Eurozone stock and bond prices during the past week, and consider corrections triggered by the Greek fallout as potential buying opportunities. Meanwhile, our outlook for the S&P 500 Index remains the same: a year-end target of 2,300, with a correction of 5% to 10% once the index hits the 2,150 to 2,200 range. For fixed-income investors, bonds are reasonably priced at current levels, although stocks, broadly speaking, appear to offer better upside.

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