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A new week brings new records for U.S. equities

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Article Highlights

- The S&P 500 posts fresh record highs, while stocks in Europe remain resilient in the face of events in Turkey.
- U.S. Treasuries trade within a narrow range, hovering near pre-Brexit levels.
- Mostly positive housing data dominates the week's U.S. economic reports.
- We have become more cautious on riskier fixed-income categories, looking for attractive entry points should volatility elevate.

Equities

Without much fanfare, U.S. equities notched three record highs during the past week, supported by some strong corporate earnings reports and rising confidence in the U.S. economy, which lifted the dollar to a four-month high. The S&P 500 Index advanced for the fourth consecutive week (about +0.6%), bringing its year-to-date return to over 7.5%.

European equity markets focused on encouraging earnings releases rather than news of Turkey's failed military coup. The broad STOXX 600 Index rose 0.7% in local currency terms and has recouped most of its post-Brexit losses. Investors also harbored hopes for additional monetary easing by major central banks, even as the European Central Bank (ECB), Bank of England, and Bank of Japan stood pat during recent policy meetings. The ECB, as anticipated, maintained its policy rates while indicating that it intends to keep interest rates "at present or lower levels for an extended period of time, and well past the horizon of our net asset purchases," which is scheduled to run through at least March 2017.

Stocks in Asia were mixed for the week. Fresh off its best one-week showing since December 2009, Japan's Nikkei 225 Index gained 0.8%. Chinese equities fell about 1.4%, while more broadly, emerging-market stocks extended their 2016 rally. Year to date through July 21, the MSCI Emerging Markets Index has climbed 11.4%.

Current updates to the week's market results are available here.

Fixed income

U.S. Treasuries traded within a narrow range, staying near their pre-Brexit levels. The yield on the bellwether 10-year note, which began the week at 1.60%, dipped to 1.57% on July 22. (Yield and price move in opposite directions.)

Returns for non-Treasury “spread” sectors ranged from mildly negative to broadly positive for the week through July 21, as these higher-yielding asset classes are still in demand. In particular, fund flows buoyed investment-grade and high-yield corporate bonds, which have realized year-to-date gains of 8.7% and 12.3%, respectively, based on Barclays indexes.

The U.S. economy continues on its solid, if uninspiring, growth path

This week’s batch of U.S. data reports was highlighted by the housing market, which we expect to provide a tailwind for the economy in the second half of the year. Among the week’s releases:

- **Existing-home sales** increased in June (+1.1%) to their fastest pace in nearly a decade. According to the NAHB/Wells Fargo Index, **homebuilder confidence** eased in July but remained positive. Overall, builders believe economic fundamentals are in place for continued slow, steady growth.

- **Housing starts** jumped 4.8% in June, while **building permits**, a forward-looking indicator, rose 1.5%.

- **First-time unemployment claims** edged lower, to 253,000, as did the less-volatile four-week moving average, by 1,250, to 257,750.

- After unexpectedly declining in May, The Conference Board’s index of **leading economic indicators** ticked up 0.3% in June. This points to continued moderate economic growth through the end of 2016 and an expansion that appears resilient enough to weather financial market volatility.

- Supported by solid business conditions overall, **U.S. manufacturing activity** climbed to 52.9 in July, its highest level since last November, according to the “flash” (preliminary) reading of Markit’s Purchasing Managers’ Index (PMI).

- **Regional manufacturing,** however, continues to struggle, with the Philly Fed Index slipping in July. This report comes on the heels of the previous week’s release showing a decline in the Empire State Index.

On July 29, the U. S. government will release its advance estimate of second-quarter GDP, which we expect will improve to an annualized rate of about 3.1%, well ahead of the economy’s current 2.0% trajectory.

Outlook

While the U.S. recovery is on track, global growth remains somewhat fragile but on a modest upswing. Europe is still on target for GDP expansion of about 1.5% this year, as Brexit-induced weakness has yet to materialize outside of the U.K.

Meanwhile, China's second-quarter growth rate was faster than expected. Although we don't foresee China's economy accelerating from current levels, we do believe the government is serious about keeping growth close to the 6.5% range through at least 2020—potentially signaling more stimulus is in store. Commodity prices have risen for much of the year, supporting many developing economies. In our view, the uptick in commodities might signal the end of global deflationary forces, which would certainly be welcomed in Europe, given the region's battle with chronically low prices.

Fixed-income markets have traded in orderly fashion despite the past month's headline-grabbing events, including Brexit, June's much stronger-than-expected payrolls report, and the attempted coup in Turkey. Spread sectors could eke out modest gains in the near term. However, spreads could widen as issuance increases in the coming weeks, or if equity-market volatility picks up from its current low level. Prices for non-Treasury securities could also fall if the 10-year yield were to move closer to 2%. We have become more cautious on riskier fixed-income categories, looking for attractive entry points should volatility elevate.