January 13, 2017

Global equity rally takes a breather

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Article Highlights

- European and U.S. equity benchmarks finish roughly flat for the week.
- U.S. Treasuries trade within a narrow range, while continued strong demand benefits non-Treasury fixed-income sectors.
- In a light week for U.S. data releases, business owners express further optimism, although consumer sentiment moves lower.
- For U.S. equities, fourth-quarter corporate earnings will be key to Q1 performance.
- Fixed-income markets will seek specifics on President-elect Trump's policy agenda, along with a range of economic data points, in gauging the direction of interest rates.

Equities

With few economic data reports to digest, U.S. equities drifted lower for most of the week. Some solid earnings releases from major banks on January 13 provided a modest boost, enabling the S&P 500 Index to finish essentially flat, one week after setting an all-time high.

In Europe, equity markets were largely unimpressed by more positive news about the Eurozone's recovery, with the broad STOXX 600 Index up a slight 0.1% (in local terms), hard on the heels of entering bull-market territory. In 2016, Germany's economy, the region's largest, grew at its fastest rate in five years. For the currency bloc as a whole, industrial output surged in November, and unemployment held firm at its lowest level since July 2009. This data follows a multi-year high in the Eurozone's manufacturing and service sectors and a healthy uptick in inflation.

Asian markets also failed to extend their previous week's gains. A stronger Japanese yen weighed on the exporter-heavy Nikkei 225 Index, while a slide in exports hurt Chinese shares.

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

Fixed income

Like U.S. equities, U.S. Treasuries moved within a narrow range during the week. The yield on the bellwether 10-year note dipped modestly on January 11 following President-elect Donald Trump’s highly anticipated first press conference, which provided fewer policy details than the markets had hoped for. Late in the week, though, some stronger-than anticipated inflation data temporarily pushed the 10-year yield higher. It closed at 2.40% on January 13.

Meanwhile, demand for non-Treasury fixed-income “spread sectors” continued apace. Returns for high-yield and investment-grade corporate bonds, along with structured products such as asset-backed and mortgage-backed securities, were all positive for the week through January 12.

Business owners’ mood improves further

In a light week for U.S. data releases, optimism among businesses continued its post-election surge, while consumer sentiment edged lower. Among the week’s reports:

- **Small-business sentiment** soared in December to its best level in 12 years, as measured by the NFIB index. This is the second consecutive month in which small business owners have reported a much brighter outlook.

- **Consumer sentiment** dipped slightly in January, according to January’s preliminary reading of the University of Michigan index.

- **Retail sales** rose by a below-forecast 0.6% in December. Disappointingly, most of the increase was concentrated in sales of automobiles and gas, with little improvement in other areas.

- **First-time unemployment claims** rose by 10,000, to 247,000, but remain near the lowest level in decades. Claims are often volatile early in the year as workers move in and out of the workforce following the holiday shopping season. The less volatile four-week average declined by 1,750, to 256,500.

- **The producer price index,** a measure of wholesale costs, rose for a second straight month in December amid higher prices for energy products, leading to the biggest year-on-year gain in just over two years.

Outlook

We will be scrutinizing fourth-quarter U.S. corporate earnings reports as they are released over the next few weeks. Forward guidance from CEOs will be most important in light of the unexpected U.S. election result and broad-based strengthening in the global and U.S. economies. A sunnier outlook for profits, hiring, and future investment could boost stock prices.

In the near term, fixed-income markets will seek clarity on Trump’s economic agenda in order to gauge the direction of interest rates. Looking further ahead, markets will focus on key economic releases— including wage growth, employment gains, and consumer spending and confidence—as well as the Fed's reaction to this data as officials weigh the timing of their next rate hike.