

Wentz Weekly

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Fourth Quarter Earnings Continue to Impress



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Corporate earnings are increasing for the first time in several quarters, reflecting an improving economic picture in the U.S. as the vaccine rollout accelerates and the economy continues to reopen. Over 74% of companies in the S&P 500 have reported Q4 2020 results and of those that have reported, more are beating profit estimates than average and are beating profits estimates by a much wider margin than average. Four out of every five companies reporting are beating estimates, better than the average beat rate of 74%, according to FactSet. Companies are reporting profits 15% above the average estimate, a margin that doubles the average. Fourth quarter earnings are exceeding expectations so much that estimates now call for an increase in earnings compared to the same period a year prior. Earnings growth is now expected to be 2.8% versus the estimate on December 31 that called for a 9.3% decline. The improving earnings picture is one of a handful of reasons equities continue to move higher.

In a speech before the Economic Club of New York, Federal Reserve Chairman Jerome Powell reiterated his stance he is not worried about inflation and is committed to accommodative monetary policy to achieve maximum employment, even with higher inflation. Powell emphasized the Fed will not tighten monetary policy in response to a strong labor market, and when inflation has been running persistently below 2% the Fed will let inflation surpass 2% "for some time." The Fed is still not thinking about shrinking the size of its balance sheet and said it is not the time to think about addressing the national debt issue, while calling on more fiscal support from Congress. On Tuesday inflation data was released showing a smaller increase than expected in the most recent month. Compared to a year ago, a basket of core consumer prices are 1.4% higher, a smaller rise than expected, easing concerns in the equity market that inflation would lead to higher rates and pressure equity multiples.

The next steps of the reconciliation process are underway as House committees draft legislation that will be included in the next Covid relief package. The goal is to have an initial vote the week of February 22 while targeting the final passage by mid-March, the same time elements in the most recent December Covid bill expire. More details will emerge this week as the draft is worked on, while a debate is heating up on including a minimum wage increase. We continue to believe a bill will be passed within the next month in the \$1.5 trillion range, which is approximately 7% of U.S. GDP.

In addition to a Covid relief bill, President Biden remains focused on an infrastructure package, holding a meeting with a bipartisan group of Senators, the Vice President, and Transportation Secretary. The move signals a package targeting infrastructure spending may be seen much earlier than expected. A price tag has not been discussed, nor has discussions around pushing the potential bill through with reconciliation, hinting that it may receive bipartisan approval. We believe an infrastructure spending plan is very likely, which would provide an additional boost to the economy and much needed improvement to U.S. infrastructure, while benefiting sectors such as industrials.

Demand for semiconductors that power technology that we use on a daily basis has significantly increased over the years but supply has been disrupted over the pandemic, leading to a shortage of semiconductors needed for key consumer goods. The recent shortage has become so severe it has caught the attention of the White House, with the Biden administration planning on signing an executive order to evaluate supply chain issues. GM was the latest to report the extent of the shortage. The company has shut down three manufacturing facilities across North America and said it expects a \$1.5 billion to \$2.0 billion impact on adjusted profits. Research firm IHS Markit said the chip shortage could impact production of 672,000 vehicles in the first quarter and may last into the third quarter of 2021. The shortage started during the pandemic when vehicle manufacturers thought the slump in auto sales would be longer lasting and used up existing inventory rather than buying new chips, in addition to the surge in demand for electronics as remote work became the new normal. Since the auto market quickly recovered, manufacturers ramped up chip orders and chip makers have struggled keeping up due to the rush in orders and time-consuming aspect behind chip production. Vehicles are requiring many more chips due to the increasing number of features such as assisted driving technology. The chip constraints are broad based and have occurred in everything from vehicles to consumer electronics and it remains uncertain when supply issues will improve.

Company News

- A report from Counterpoint Research says the iPhone 12 mini represented just 5% of overall iPhone sales in the first half of January, well below expectations. Some analysts are expecting, due to weak demand for smaller screens, Apple could potentially halt production for the mini this year.
- The move to electric vehicles continues with Toyota being the latest to announce a big investment. The company said it plans to launch three new EV models in the U.S. this year. By 2025 its goal is to have EV models make up 25% of new vehicles, and 70% by 2030.
- It is becoming clear Microsoft is targeting another social media acquisition. The Financial Times reported the company approached Pinterest on a possible acquisition, however talks are no longer active after Pinterest said it wants to remain independent.

The Week Ahead

The earnings calendar remains busy this week with at least 48 S&P 500 companies scheduled to report. Highlights include CVS, AIG, and Palantir on Tuesday, Shopify, Twilio, Fastly, Marathon Oil, and Hilton on Wednesday, Applied Materials, Roku, BigCommerce, and Walmart on Thursday, and Deere on Friday. Elsewhere on the corporate front several investor conferences take place, the most notable the Consumer Analyst Group of New York Conference (CAGNY), which will feature presentations by a number of consumer companies. The economic calendar will be busier with the highlight of the week being several housing data reports and the January retail sales report where the consensus is for a 1.0% increase for the month. Housing starts along with existing home sales will be released Thursday and Friday. We will also see results of key manufacturing surveys. Outside of the economic and corporate calendars, Congress will continue working on drafting a Covid-19 relief bill which we still expect to pass by mid-March. Also, the Robinhood CEO and several executives from trading firms will appear before the House to testify on the extreme market moves from the short squeezed stocks.

The S&P 500 is an unmanaged index of 500 widely held stocks that is generally considered representative of the U.S. stock market. The Dow Jones Industrial Average (DJIA), commonly known as "The Dow" is an index representing 30 stock of companies maintained and reviewed by the editors of the Wall Street Journal. The Russell 2000 Index measures the performance of the 2,000 smallest companies in the Russell 3000 Index, which represent approximately 8% of the total market capitalization of the Russell 3000 Index. The NASDAQ composite is an unmanaged index of securities traded on the NASDAQ system. Every investor's situation is unique and you should consider your investment goals, risk tolerance and time horizon before making any investment. Sector investments are companies engaged in business related to a specific sector. They are subject to fierce competition and their products and services may be subject to rapid obsolescence. There are additional risks associated with investing in an individual sector, including limited diversification. Information contained herein was received from sources believed to be reliable, but accuracy is not guaranteed. Information provided is general in nature and is not a complete statement of all information necessary for making an investment decision and is not a recommendation or a solicitation to buy or sell any security. Investing always involves risk and you may incur a profit or loss. Keep in mind that individuals cannot invest directly in any index. Past performance does not guarantee future results. There is no assurance these trends will continue, or forecasts will occur.