

Wentz Weekly

March 15, 2021

Easing Inflation Concerns, For Now...



Investment management for your lifetime

Investors have anxiously been waiting for new inflation data to get a better gauge on the pace of increasing consumer prices. The U.S. Bureau of Labor Statistics reported the consumer price index for all items rose a seasonally adjusted 0.4% in February, meeting estimates and following a 0.3% rise in January, driven mostly higher by a 3.9% increase in energy prices. Core prices – stripping out the volatile food and energy categories – rose a lower than expected 0.1%. Over the last 12 months prices on all items were up 1.7%, while core prices rose 1.3%, compared to 1.4% increase in January. It was a relief for the markets which have been increasingly concerned about inflation in recent months, causing Treasury yields to move higher and pressuring high growth stocks in the equity market. The Covid impact on prices began about a year ago, so we would expect upcoming inflation reports to show much higher moves in prices. The question is how much of the increase in prices will be transitory and how much are businesses willing to absorb rather than pass on to consumers.

The divergence in short-term economic activity between the U.S. and the rest of the world, specifically Europe, is making policy more difficult for central banks. The European Central Bank said last week it plans to accelerate the pace of its bond purchases in effort to contain borrowing costs and boost the eurozone economy. Interest rates across the globe moved higher after recent comments from Fed members downplayed inflation risks, calling any rise transitory and signaled it will not act to contain the recent uptick in longer term rates. ECB President Christine Lagarde said the recent increase in bond yields was more a result of improving growth prospects in the U.S. rather than a recovery in Europe, which led the central bank to act. Many European governments have debt that is over 100% of its GDP, making an increase in rates more troublesome in Europe than in the U.S. The Federal Reserve will meet this week and will be followed by a policy decision and a Jerome Powell press conference Wednesday afternoon where comments will be closely monitored by the markets.

Covid numbers continue to improve as the vaccine rollout accelerates with now over 100 million Americans receiving at least one dose of the vaccine and at least 2.4 million getting vaccinated daily. The government agreed to purchase an additional 100 million doses of the Johnson & Johnson vaccine and we could potentially have another vaccine on the market following recent data by Novavax. The company said final data from its Phase 3 study of over 15k participants showed its Covid vaccine is over 96% effective against mild, moderate and severe disease caused by Covid-19. With the accelerating pace of vaccinations, President Biden directed all states to make all adults eligible for the vaccine by May 1, and said the goal is to allow small group gatherings again by July 4.

More funding will be going to the rollout of vaccines after Biden signed the \$1.9 trillion American Rescue plan into law on Thursday. Roughly \$87 billion of the bill will be spent on Covid response including testing & tracing and funding for distribution of vaccines. There is debate on how much of the bill will go to actual Covid relief, with some estimates saying less than 25% will be used for this purpose. Consumer's balance sheets will almost surely improve, with a family of four expected to receive \$14,000 from the new bill, with over \$11,000 being seen this year from direct rebate payments of \$1,400 per person and an expansion of the child tax credit. The direct payments will support consumer discretionary sectors as many individuals are expected to spend the money right away. As mentioned in previous notes, we also expect the savings rate to surge again in March and April as many individuals and families set some of the money aside in savings. With a record high savings rate and significant pent-up demand, we expect the economy will continue its above trend growth trajectory for some time.

After another multi-trillion dollar Covid-relief bill, the Biden Administration is considering how to pay for the debt raised from the bill and for future spending programs. As we mentioned and expected, now that the stimulus package is signed into law the administration will shift its focus to the first major federal tax increase since 1993, something we think the markets have largely discounted thus far. The challenge will be crafting a bill that will gain the support of every single Democrat in the Senate due to the current 50-50 split. Treasury Secretary Janet Yellen said over the weekend Biden has not decided whether to pursue a wealth tax, something progressive Democrats are pushing hard for. She went on to reiterate Biden's desire for higher taxes on corporations, individuals and on capital gains and dividends. Biden has not endorsed the idea of a wealth tax and Yellen has previously taken a cautious view on it, saying the tax increases mentioned above are alternatives to the wealth tax. Tax reform is an almost certain, especially as House Speaker Pelosi pushes committees to work on an infrastructure package, potentially adding another multi-trillion dollars to the government debt.

Company News

- GE said it has agreed to combine its GE Capital Aviation unit with AerCap. GE said the deal will reduce its debt by \$30 billion. GE shareholders will receive AerCap shares and cash. When the deal is complete, GE shareholders will own 46% of the combined company. The company reduced its EPS guidance as a result of the deal and also recommended a 1-for-8 reverse stock split to lower the number of shares outstanding to a number more typical with comparable companies.
- Netflix is getting more stringent with password sharing. A new message is appearing when logging on saying "If you don't live with the owner of this account, you need your own account to keep watching."
- Local sewing and arts and crafts retailer JoAnn Fabrics is a publicly traded company once again. The stock began trading Friday after its IPO. The company was last publicly traded in 2011, prior to being bought out by private equity firm Leonard Green.

The Week Ahead

The economic calendar is much busier this week. On Monday, the Empire State Manufacturing Survey is released, an indicator of manufacturing conditions in the New York region. On Tuesday we will receive data on retail sales for February, cross border inflation data, industrial production, and the latest update on the change in business inventories. On Wednesday, the Census Bureau reports on the pace of new home construction as well as permits to build new homes. Finally, on Thursday the weekly update on unemployment claims is released along with the Philly Fed Manufacturing survey. The main event of the week will be the Federal Open Market Committee Meeting, followed by the Fed policy decision and Chairman Powell's press conference. Market participants will pay close attention to any commentary on the inflation outlook and any hints at tapering the asset purchase program. The Bank of Japan also meets and will announce its latest policy decision on Friday. The earnings calendar is light, but notable companies reporting include; home builder Lennar on Tuesday; Accenture, Dollar General, FedEx, and Nike on Thursday; and Tiffany on Friday.

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.