

Wentz Weekly

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First Quarter Earnings Kick Off This Week



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The next catalyst for stocks will be the upcoming earnings season which kicks off this week with some of the largest banks the first to report. Investors will be looking for results and forward guidance and commentary on the reopening and recovery to continue to drive momentum in stocks. According to FactSet, analysts are expecting profits on S&P 500 companies to grow 24.5% compared to the same quarter a year ago, the same period the world economy shut down as a result of the pandemic. If this number holds, and if companies report earnings better than expected as they typically do, FactSet says growth could be at least 28% in the quarter, the highest growth in U.S. profits in over a decade. There will be no shortage of things for management teams to discuss on earnings calls. We expect many questions and comments on the reopening and future of working from home, vaccines, supply chain issues, and political issues such as minimum wage, taxes, and infrastructure.

U.S. Treasury Secretary Janet Yellen wrote an op-ed for the Wall Street Journal last week making her case on why the country needs higher corporate tax rates and a minimum tax on profits businesses make overseas, while calling for other governments to end the race to the bottom. The Biden Administration's proposal to raise the corporate tax rate to 28% from 21% to fund part of infrastructure spending would put it near the top in the world. Yellen wrote in the piece that when the U.S. cuts corporate taxes other nations respond and try to undercut the U.S. In effort to fix the 'race to the bottom' Yellen urged nations to agree to a global minimum tax and proposes incentives to achieve this. More importantly for Yellen, the plan calls for a minimum 21% tax on U.S. company's overseas profits. Yellen is pushing hard for the minimum tax, which in theory should stop the flow of business out of a country because the business knows it will be taxed no matter where they go.

The plan for higher corporate taxes and significant spending on infrastructure is still a long way, but the process to pass a bill was made easier last week. The Senate parliamentarian cleared the way for Democrats to use a process known as reconciliation for its infrastructure bill. This means Democrats could use the parliamentary procedure to bypass the 2/3 vote requirement and instead pass a bill with a simple majority – in the current scenario with no Republican support. Democrats have used reconciliation once this year already to pass the Covid related stimulus package last month. Provisions passed through reconciliation must relate to the budget, so any spending or tax changes are generally included in reconciliation. Republicans have criticized the \$2.4 trillion infrastructure proposal so far, calling it too broad based and opposing the increase in corporate taxes. Some Democrats have also been vocal, opposing the proposal unless it included a repeal of the cap on state and local tax deductions, a feature that was part of the Trump tax reform. Significant change from the proposals is all but certain and recent reports suggest Democrats could compromise on the corporate tax rate and may even settle on something lower than the 28% in Biden's proposal.

The global chip shortage is an ongoing issue and is now hitting one of the world's largest companies. Apple, known to manage one of the most complex supply chains, proved it is not immune from the shortage. Production of the MacBook and iPad has been postponed due to a global shortage of key components, Nikkei reported last week. Because of the delay in production, Apple has pushed back orders for the devices from the first half of this year to the second half. Sources told Nikkei the shortage has yet to affect production for the iPhone but says supply for some of its components is very tight. These sources say the delays are a sign the global chip shortage is growing more severe. Apple did not comment but we would expect to hear more on the impact to the company in its earnings call on April 28.

The CEO of JPMorgan, Jamie Dimon, released his annual shareholder letter which said the economy is emerging from the pandemic and thanks to strong savings, significant stimulus including the \$2.3 trillion infrastructure proposal, and the vaccine distribution could lead to a Goldilocks movement that could last into 2023. He went on to say the worse outcomes were prevented thanks to the government's rapid and rather large monetary and fiscal support. Regarding taxes, Dimon said the effort to create equality and higher labor force participation will lead to higher taxes and any change to the corporate tax rate should be reasonable and moderate to keep the U.S. competitive with other countries.

Company News

- Microsoft announced it has entered an agreement to acquire the speech recognition company Nuance Communications. The deal is for \$56 per share in cash, which was a 23% premium to the previous day's closing price.
- Boeing said it told 16 customers they should temporarily ground the 737 MAX airplanes that have been delivered since the grounding order on the MAX planes was removed last November. Boeing said an electrical power system issue needs addressed before resuming operations.
- Carnival said booking volume was up 90% in the first quarter compared to the same quarter a year ago, and "full year 2022 bookings are ahead of what was a very strong 2019, as of March 21," and the company is achieving that with "minimal advertising."

The Week Ahead

It will be a much busier week on the economic calendar as well as earnings calendar as first quarter earnings season kicks off beginning with big banks. Profits in the quarter are expected to have grown 24.2% as we begin to lap the months a year ago when the pandemic began. Expect earnings reports from Fastenal on Tuesday; Goldman Sachs, JPMorgan, and Wells Fargo on Wednesday; Bank of America, Citigroup, Delta, PepsiCo, and United Health on Thursday, and Morgan Stanley, PNC, and Kansas City Southern on Friday. On the economic calendar notable reports include the Consumer Price Index on Tuesday where the report should show an uptick in inflation to 2.5%. On Thursday Retail Sales for March is released where economists are expecting a 5.3% increase in the month thanks to additional government aid. Also on Thursday is jobless claims, the Philly Fed Manufacturing index, and industrial production. Finally, on Friday the Housing Starts and Permits report is released along with a reading on Consumer Sentiment.

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.