

Wentz Weekly

June 14, 2021

Federal Open Market Committee Meeting Preview



Fed members have consistently reiterated their message that the short-term increase in inflation will be transitory and ease once covid related impacts – base effects, pent up demand, supply chain shortages, and labor shortages – fade. Last week's inflation report showed consumer prices rose 5.0% from a year ago, the fastest rate in over a decade, while core prices (stripping out the volatile food and energy categories) rose at the fastest rate since 1992. While much of the index gains were from "temporary" factors, we are seeing signs of "sticky" inflation. Some prices are sticky meanings they may not respond to changing market conditions as quickly as other "flexible" priced goods. The Atlanta Fed attempts to capture the change in sticky prices in its sticky-price consumer price index. The index rose 4.5% on an annualized basis while its flexible index rose 18.7% on an annualized basis.

At the end of the day what matters is how the Fed and the markets interpret inflation expectations. The Fed has maintained its view that the recent rise in inflation will pass and the markets have traded on that expectation. Last week the S&P 500 rose 0.41% to a new record high while the 10-year Treasury yield fell to a low of 1.45%, the lowest since March. The main event this week will be the Fed's post-meeting announcement and Chairman Powell's press conference on Wednesday. The meeting will also conclude with an update on the Fed's projections as well as the "dot plot" – where the Fed sees interest rates in the short and medium term. What we are focusing on is what the new expectation is on inflation and if the Fed will begin discussions on tapering its bond purchase program. We know it will be some time before the Fed starts peeling back the amount of bonds it is purchasing, but for now the bigger question is have they began the discussion on the timing. As of its last meeting, they have not. If the FOMC does, we expect the markets, especially growth, to have an immediate reaction to the downside. Expect volatility toward the latter half of the week.

Last week the Bureau of Labor Statistics released the latest on the consumer price index, a measure of the change in prices paid by consumer for a basket of consumer goods and services. The index showed another large increase in May, rising 0.6% and more than the 0.4% increase expected. Compared to a year ago the index for prices was up 5.0% vs 4.6% expected and up from 4.2% in April. Core prices rose 0.7% after a 0.9% increase in April with the yearly rate at 3.8% up from 3.0% and also above the expectation of 3.4% and the highest y/y rate since 1992. Similar to the April inflation report, used cars made up 1/3 of the monthly gain with used car prices up 7.3% in the month and 30% higher from a year ago. Also significant, every major category in the index was up over 2% from a year ago with the exception of medical costs. Some services are seeing higher prices as well including food away from home (restaurants), rising 4.0% from a year ago versus food at home (groceries) up just 0.7% y/y.

Job openings are at a record high. According to the DOL's Job Opening and Labor Turnover Survey, as of the last day in May there were 9.28 million job openings, shattering the previous record the month prior by one million and over 30% higher than pre-pandemic levels. Food service firms hold the most job openings currently, followed by "other services," illustrating the strong snapback in demand for service related jobs thanks to the economic reopening and removal of restrictions. We also take note that the amount of hirings in the month was unchanged at 6.1 million while separations saw a jump higher. Within the separations category, 4.0 million quit their jobs, a record high amount of quits in one month. We believe this suggests employees feel confident they are able to quit their jobs and find a higher paying job. We believe the dynamics of the current jobs market is going to continue to drive the average wage higher, especially at the lower end, which has the ability to affect longer-term inflation. An interesting side note, the number of job openings (9.28 million) is about the same as the number of Americans considered unemployed at 9.31 million.

While Congress remains in deadlock in the U.S. on an infrastructure bill, more specifically over the issue of raising the corporate tax rate, a group of countries have agreed to support a new minimum global tax for corporations. The agreement was made after a meeting between the G7 countries that includes the U.S., Canada, France, Germany, Italy, Japan, and the United Kingdom. A statement following the meeting said the countries support a global minimum tax of 15% on multinational companies and they hope to make further progress on the agreement at the Group of 20 meeting in July. The agreement also has the support of President Biden, who proposed the idea to Republicans as a way to raise additional funds for his infrastructure proposal. A note by Goldman Sachs several weeks ago notes a tax increase on foreign and domestic profits would reduce earnings of S&P 500 companies by about 3% in 2022.

Company News

- For almost two decades, people have waited for a new treatment that could help slow, cure, or prevent the progressive brain disease of Alzheimer's. Last week in a highly anticipated decision, the U.S. FDA said it approved Biogen's Alzheimer's treatment called aducanumab, which helps slow down the disease. Shares of Biogen jumped as much as 63% on the news and finished up 38% on the day.
- Lordstown Motors wrote in an SEC filing that there was substantial doubt about its ability to continue as a going concern if it cannot raise additional capital to fund the production of its vehicles. Shares fell 29% from the highs of the day.
- Macquarie Infrastructure agreed to sell its Atlantic Aviation unit to private equity group KKR for \$4.48 billion in cash. The board of directors expects to authorize a cash distribution to shareholders following the closing of the transaction.

The Week Ahead

It will be another quiet week on the earnings calendar this week. Notable companies reporting quarterly results include Oracle on Tuesday, Lennar on Wednesday, and Kroger, Adobe, and Smith & Wesson on Thursday. On the corporate calendar, outside of earnings, several companies will hold annual meetings including Activision Blizzard, General Motors, and Humana. The number of economic data reports picks up this week. Tuesday morning we will see the producer price index, measuring the change in inflation at the producer level. We will also see retail sales for May where economists are expecting a 0.5% decline, a small pullback from the strong stimulus induced spring spending months. On Wednesday, the Census Bureau reports data new residential construction where the consensus forecast has an annualized 1.63 million new housing starts. Jobless claims, expected to show another pandemic low, and the Philly Fed manufacturing survey index, expected to show continued strength in manufacturing conditions in the Northeast, are released Thursday. The main event for the week will be the FOMC meeting Tuesday and Wednesday followed by its policy announcement Wednesday at 2:00 pm, and then Chairman Powell's post-meeting press conference. The meeting and conference will be closely followed for any clues of a shift in the committee's stance on inflation and its bond purchase program.

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.