

Wentz Weekly

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Covid's Comeback, Will it Threaten the U.S. Recovery?



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Renewed concerns about the spread of Covid, specifically the new Delta variant which is said to be highly transmissible and now accounts for 83% of new cases, had investors in a risk-off mood to begin the week last week. New cases have almost quadrupled in less than a month, with the 7-day average rising to 40,246 up from 11,480 just a month ago, bringing back worries of new lockdown measures. As of July 22, the CDC says 35% of U.S. counties are seeing high levels of transmission with cases on the rise in nearly 90% of jurisdictions. An increase of cases also increases the chances of the virus mutating which could lead to a new variant, however data the CDC is observing suggest the vaccines are effective against new variants so far.

While new cases remain an important number to track, new hospitalizations could be a better indicator on the severity of the disease and the likelihood of another economic shutdown or specific restrictions (new travel restrictions, etc). The high vaccine levels in those most vulnerable and the high effective rate at preventing severe illness should keep hospitalization rates low going forward. In the U.S., nearly 50% of the 18+ population is fully vaccinated, with over 70% receiving at least one dose, and over 80% of the 65+ age population is fully vaccinated. While the new Delta variant will continue to create headlines and spread mostly among the unvaccinated, at this point we do not think it threatens the progress the U.S. economy has made since the worst of the pandemic a year ago. With a significant amount of cash still on the sideline, pent-up demand, monetary and fiscal support, and a strong earnings season, we continue to favor equities moving forward.

New unemployment claims rose to 419,000 for the week ended July 17, the highest level in two months. The four-week average, which tends to be a better indicator of a trend was steady at 385,250, one of the lowest levels of the pandemic. Despite the lower number of new claims, there are still 3.236 million Americans collecting state unemployment benefits. As we mentioned in past newsletters, over half of the states have ended the federal enhanced pandemic unemployment payments and we finally saw a large drop in pandemic benefits being paid in the data (this data lags two weeks). As of July 3, according to the DOL there are still 9.268 million Americans collecting federal pandemic benefits, a decline of 1.129 million from the prior week, after plateauing around 11 million for several weeks.

One of the pioneers in the subscription business, Netflix reported its second quarter results that exceeded analysts' expectations. The company reported 1.54 million new global subscribers across its platform and revenues that grew 19% to \$7.34 billion for the quarter. However, investors punished shares after its forecast for new subscribers for the current quarter was 3.5 million, well below the 5.9 million that analysts were expecting. In addition, looking deeper at its second quarter and its most profitable divisions, the U.S. and Canada, saw a net loss of 430,000 subscribers. More importantly for the company going forward, the management team gave an optimistic tone on its content for the remainder of the year as its investments into content ramp up. In addition, it commented on its move into video games saying it is in the early stages into its move into gaming and it would be focused near-term on mobile games but is still in the experimental stages.

The housing sector continues its hot streak after the housing starts and permits, and existing home sales reports for June all came in above expectations and near the highest levels since the 2000's housing boom. The National Association of Realtors said existing home sales rose 1.4% in June, and up 23% from a year ago, to an annualized pace of 5.860 million homes. The 23.4% increase in the median home price has encouraged more homeowners to put their home up for sale, improving supply very slightly in the month, however historically low inventory remains in place with just 3.9 months supply on the market in June. The Census Bureau said construction on new homes rose 6% in June, and up 29% from a year ago, to an annualized pace of 1.546 million homes, one of the highest rates in 15 years. Permits to build a new home also increase, in attempt to keep up with the unprecedented demand.

A consequence of such a strong housing market coupled with shortages is an imbalance between supply and demand. Builders are struggling to keep up with demand, and not being helped by the shortages of building materials, land, and labor. This was evident in the largest U.S. homebuilders most recent earnings report. D.R. Horton said its future orders are down, but not because of a shortfall in demand, but because the company is holding back sales. The company said it is restricting the pace of its sales orders essentially because it cannot keep up with the demand. As Barron's notes, this is a textbook definition of inflation – when too much money chases too few goods.

Company News

- Intel reported 2nd quarter results above expectations and said it expects the shortage in semiconductors to bottom in the second half of this year but not completely recover for another year or two after it bottoms.
- Chipotle beat expectations in its latest quarter with comparable store sales growth of over 30%. The CEO said the company would not have been able to beat expectations if it did not pass on higher costs to customers, something it was able to do without experiencing a decline in sales.
- Uber Freight, who offers data tools to carriers and shippers, said it is acquiring Transplace, a transportation management software and logistics company. The deal is worth \$2.25 billion including up to \$750 million in Uber stock and the remainder in cash.

The Week Ahead

The calendar will be busy this week with many corporate events, economic data, and a Federal Reserve meeting. On the earnings calendar, it will be one of the busiest weeks of the quarter with at least 165 S&P 500 companies set to report quarterly results. Notable reports this week include: Lockheed Martin, Hasbro, and Tesla on Monday; Apple, Alphabet, Microsoft, Visa, AMD, UPS, GE, 3M, and Starbucks on Tuesday; Facebook, Shopify, Boeing, PayPal, Ford, Qualcomm, Pfizer, and Spotify on Wednesday; Amazon, Comcast, Altria, Anheuser-Busch, and T-Mobile on Thursday; and AbbVie, Procter & Gamble, Caterpillar, Exxon, and Chevron wrapping the week up on Friday. It will be an important week of economic data as well. New home sales are released Monday and consumer sentiment surveys are released Tuesday and Friday. On Thursday we receive the first estimate on second quarter GDP where economists are estimating the economy grew at an 8.0% annualized pace in the quarter. Finally on Friday we will see the latest on consumer spending and personal income, and an important measure of labor costs in the quarterly employment cost index. The Federal Reserve conducts its FOMC meeting on Tuesday and Wednesday with a post meeting press conference Wednesday at 2:30 pm. Markets will be looking for any hints of the Fed tapering its asset 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.