Wentz Weekly

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S&P 500's 48th Record Close of the Year, What Happens from Here?

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Just 511 days and 353 trading days later, the S&P 500 is within points from doubling off the pandemic closing lows of 2,237.40 on March 23, 2020. Nothing has seemed to slow down the very bullish market sentiment. Over this stretch, the deepest pullback was 10.5%, seen during a 15 day stretch in September last year, followed by an 8.9% pullback in October 2020. Other than those two pullbacks, nothing has come close to a correction. We believe the market's constant grind higher may soon slowdown or even pullback from these record high levels. Delta cases are rising and will spread to states that haven't seen hot spots yet as the spread continues which may force certain mandates/restrictions (i.e., mask mandates) which could deter customers and sour sentiment. In fact, the Consumer Sentiment index from the University of Michigan had one of its largest drops ever, falling to its lowest reading of the pandemic as the report called a "stunning loss of confidence in the first half of August." The report did however say the data represents an emotional reaction from consumers and the index should rebound in September. On top of the delta concerns, the Fed should be announcing its taper plans next month and markets are trading at 22.3x 2021 earnings and 19.4x 2022 estimated earnings, both elevated valuations from a historical perspective, and markets are in a historically weak period of the year. If we were to see a pullback we think that would present a buying opportunity, as we are still in the middle of a secular bull market.

Inflation, which we will touch on more in our Outlook Meeting and in next week's newsletter, flattened out in July, but is still rising at a faster pace than normal. According to the Bureau of Labor Statistic's consumer price index, prices rose 0.5% in July, right in line with the increase that was expected. Compared to a year ago, prices were 5.4% higher in July, matching June's pace and in line with expectations after several months of exceeding expectations. The so-called core index, which excludes prices that are not as volatile such as food and energy prices, rose 0.3% in the month and are up 4.3% from a year ago, decelerating from the 4.5% rate in June. One category that drove the headline number much higher in June, new and used car prices, continue to rise at an unprecedented pace, with new car prices 1.7% higher in July and used car prices 0.2% higher, while each are 6.4% and 41.7% higher from a year ago. Shelter, one of the stickier inflation categories, rose 0.4%, in line with previous months but showing signs of picking up in the months ahead. Many services categories, such as restaurants are seeing accelerating prices as well as people feel more comfortable going out, with restaurant and bar prices up 0.8% in the month, accelerating from prior months and up 4.6% from a year ago. Categories such as car prices will see temporary inflationary pressures, but if categories such as shelter continue to creep higher, we believe inflation will be more persistent.

The $1 trillion bipartisan infrastructure bill is now in the hands of the House, which Speaker Pelosi will likely hold up in attempt to get the White House's larger $3.5 trillion reconciliation bill through Congress. Physical infrastructure is part one of the Democrats spending plans and "social/human infrastructure" is the second part, which is where Democrats plan to use budget reconciliation to get it through Congress as it would only need a simple majority. Budget reconciliation is a legislative way to fast-track bills that relate to spending and taxes through a budget resolution, a rule that only needs 50 votes (with the Vice President as the tiebreaker) to pass the Senate. The more important $1 trillion bipartisan bill appears it will he held up in the House as Democrats want commitment from its party that it will pass the budget reconciliation after the bipartisan bill. Latest reports say Pelosi now wants to change a rule that would allow both bills to pass simultaneously after moderates and progressives find more disagreement.

More Fed speak from last week is moving the consensus for a taper announcement to our expectation of the September FOMC meeting with a start date of October/November, moving the consensus up several months. Atlanta Fed President Raphael Bostic said the economy is "well on the road to substantial progress" and would like to target October-December for a range of beginning the taper program but said he would move the timeline up if the next jobs report is just as good as July's. Boston Fed President Eric Rosengren and San Francisco Fed President Mary Daly said the Fed should say in its September meeting it plans to taper. Dallas Fed President Robert Kaplan said the asset purchase program (quantitative easing) is a tool meant to help demand in the economy and currently we do not have a demand issue (we have a supply issue). As a result he would like for the Fed to announce taper in September and begin in October and would want to taper over 8 months to get it over with. Regarding inflation he said the recent reports are consistent with the Fed's outlook, but inflation pressures will broaden into next year and the PCE price index is expected to be 2.5% next year. We believe all the Fed speak is preparing the markets to expect details of tapering from Fed Chairman at the Jackson Hole Symposium or the next FOMC meeting in September and beginning in October/November, something the Fed is communicating slowly to prevent an overreaction in the markets like what was seen during the taper tantrum in 2013.

Company News

- Southwest said it has revised its revenue guidance for the current quarter downward, blaming the delta variant negatively impacting business so far in August, where it is seeing deceleration in books and increase in cancellations.
- Disney had a better quarter than analysts expected with revenue rebounding across the board. Important to its streaming push, Disney+ added 12 million subscribers bringing the total amount to 116 million and bringing the total subscriber count across all platforms to 174 million.
- Adidas announced it has agreed to sell Reebok to Authentic Brands Group for €2.1 billion (approximately $2.5 billion). The company bought Reebok in 2006 for $3.8 billion. In 2007 Reebok generated nearly a quarter of Adidas' sales but dropped to 6.9% in 2020.

The Week Ahead

Second quarter earnings season continues this week with a chunk of results coming from large retailers. Notable reports this week include recent IPOs Oatly and Roblox on Monday; Walmart and Home Depot on Tuesday; Lowe's, Target, TJX, Cisco, and Nvidia on Wednesday; Kohl's, Macy's, L Brands, and Petco on Thursday; and Foot Locker and Deere on Friday. On the economic calendar there is the manufacturing surveys out of the East coast region in the Empire State and Philly Fed manufacturing surveys Monday and Thursday, retail sales on Tuesday where total sales are expected to have fallen 0.2%, starts on new homes Wednesday, and the latest weekly unemployment claims Thursday. Also, on Tuesday, Fed Chairman Jerome Powell will attend a virtual town hall where he is sure to take questions on the Fed's taper plans.