

Wentz Weekly

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Job Growth Continued in January Despite Omicron



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Economists were worried about the effect Omicron had on the economy and labor markets in the second half of December and January so much that they were expecting very few job gains in January. They might have been surprised when the Department of Labor report released Friday morning showed 467,000 job gains in the month. Adding onto that was an upward revision of 510,000 job gains in December, above the initial estimate of 199,000. Even better was numbers on the labor force – the report said another 1.4 million people entered the labor force, something that could help ease the near record high 11 million job openings. However, this data reflects new population estimates that were introduced in January, if these were not applied in the month participation in the labor force would have been unchanged. Nonetheless, it was a solid headline number and gets the labor market closer to its pre-covid levels where just 5.7 million were unemployed (compared to the 6.5 million now). A bigger number is 5.7%. This reflects the increase in wages over the past 12 months, which was above expectations and accelerated from the 4.7% rate we saw in December. For comparison purposes, wages averaged 2.3% year-over-year growth when Americans were recovering from the Financial Crisis and through the 2010's. If Americans are making more money, they are in better condition to spend and keep the economy growing. However, that could mean higher inflation as employers may look to raise prices to offset higher wages.

In what could have turned out to be a “good news is bad news” type report, investors instead chose to brush aside the worries over higher interest rates and tighter monetary policy and instead on Friday chose to celebrate the strong labor report with the equity market moving higher. That wasn't the case in the fixed income market where yields moved higher (when rates rise, the price of bonds decline). The 10-year Treasury yield finished the week at 1.93% after a 8 basis point move higher on Friday. In addition, markets are increasingly seeing a higher chance of a more aggressive move at the Fed's next meeting. The probability of a 50 basis point (0.50%) increase in rates in the March meeting moved to 40%, up from 30% prior to Friday's labor report. The markets continue to price in a more aggressive Fed and remain uncertain on the stance of its balance sheet, which will continue to cause volatility as we move forward. We would continue to look at income producing securities with strong cash flows in this environment, which is why we continue to favor value over growth.

Over the past two years, mega cap tech companies have easily exceeded expectations every earnings report as they have benefited from the pandemic and post-pandemic environment. Fourth quarter 2021 earnings results were a little more mixed but still mostly positive. Apple was the first to report and blew away expectations with a solid forecast due to strong sales in iPhones and growth in service revenue. Alphabet's (Google parent) quarter might have been even better, with advertising revenue well above estimates thanks to its YouTube and Google search ads and cloud segment. The company also announced a 20-for-1 stock split which will result in a share price of approximately 150. Amazon was a little light on expectations as e-commerce sales slowed, but showed but higher profits than expected as it was able to better control rising costs. Microsoft also easily beat expectations thanks to its cloud and Windows segments and gave a solid forecast above expectations. Facebook was the clear underperformer, evident in the \$230 billion drop in its market value – the largest single day dollar decline of any U.S. company ever. The company reported a drop in user metrics, slowing ad sales, and slowing earnings growth. We have passed the peak in earnings season but there is still a little less than 50% of the S&P 500 companies yet to report.

A year ago, AT&T announced its plans to merge its WarnerMedia unit with Discovery to form a new publicly traded company. It was unsure how the deal would happen but last week provided more details in what will be a spinoff of WarnerMedia, which is expected to close in the second quarter. The biggest impact of the change is a smaller dividend to AT&T shareholders. The company said it will pay out approximately 40% of its free cash flow to shareholders after the deal. We know AT&T says free cash flows will be around \$20 billion which means \$8 billion in dividends annually, and if you do the math that is somewhere around \$1.11 per share, down from its current rate of \$2.08 per share. This would still rank it as one of the highest dividend payers, at current price with a 4.6% yield post-spinoff. AT&T is transforming to focus more on its core operations; wireless and broadband. It has taken moves, including this one, to sell off non-core assets and pay off its massive debt load (at one point it was the most indebted U.S. company). The new AT&T will look different than the current one – one focused more on its core operations where it does well.

Company News

- In conjunction with its earnings report that beat expectations, Google parent Alphabet said it will implement a 20-for-1 stock split in the form of a one-time stock dividend. If approved, the split will occur on July 15 for shareholders on record as of July 1.
- Bloomberg reported last week that Cedar Fair, parent company of Cedar Point, received a takeover offer from SeaWorld Entertainment for \$3.4 billion, or \$60 per share. Cedar Fair said it would review the offer. Cedar Fair previously turned down a \$70 per share takeover offer from Six Flags in 2019.
- On Monday morning, ultra-low cost carrier Frontier Airlines said it has agreed to buy competitor Spirit Airlines for \$25.83 per share, in a stock and cash deal valued at \$2.9 billion, or a 19% premium to Friday's closing price. Frontier shareholders will own about 51.5% and existing Spirit shareholders will own about 48.5% of the combined company.

The Week Ahead

We are past the bulk of fourth quarter earnings reports, but still have a wave of companies reporting this week. At least 75 S&P 500 companies will report this week with notable reports coming from: Hasbro, Amgen, and Tyson Foods on Monday; BP, Chipotle, Pfizer, and DuPont on Tuesday; DraftKings, CVS, Disney, and Toyota on Wednesday; Zillow, Twitter, Coca-Cola, PepsiCo, Expedia, and Philip Morris on Thursday; and Under Armour and Newell Brands on Friday. The economic calendar is lighter this week but still includes key inflation reports. Data will come from the consumer price index on Thursday where economists are expecting a 0.5% monthly increase in prices with a 7.3% y/y gain which would be a new 41 year high in inflation, accelerating from 7.0% last month. Elsewhere, we will see trade data Tuesday, jobless claims Thursday, and the report on consumer sentiment 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.