John Dessauer Investments, Inc.

John Dessauer's market review and update as of Wednesday April 13, 2022

JP Morgan CEO Jamie Dimon is right. In his annual letter to shareholders, he said that the U.S. economy is facing unprecedented risks. He offered a largely upbeat view of the economy's health but pointed out that the combination of inflation and war in the Ukraine present completely different circumstances than what we have experienced in the past.

Russia and the Ukraine are key producers of metal, energy, and agricultural commodities. Russia, for example, accounts for 10% of the world's oil production. With the U.S. attacking domestic oil producers, no wonder the oil price is above $100 a barrel.

In addition to these economic pressures Shanghai, a city of millions, is in total lockdown because of a rise in Covid cases. Death from Covid is rising in the U.K. Just when we hoped the worst of the pandemic was behind us comes the news from Shanghai and the U.K. Before this latest Covid development the cruise industry was suffering from Covid fears. Fear of getting Covid on a cruise has been making it difficult for cruise lines to get the desired number of passengers. They all are running at reduced capacity to allow more space for passengers. Still, even though many if not most cruise lines require all crew and passengers to be fully vaccinated, there are fears of breakthrough Covid cases.

The cruising industry's data support concerns that Covid fear was affecting consumer behavior before the latest news from Shanghai. Now it seems likely that consumers will be worrying about getting Covid for many more months to come.

Jamie Dimon in his annual letter also said: “In hindsight, the medicine was probably too much and lasted too long.” He was referring to the Biden stimulus spending and the inflation that followed. Democrats are in denial about the causes of rising inflation. And the Russian invasion of the Ukraine has made the inflation situation worse. Still, it would be very positive if the Biden Administration would admit their role in causing the inflation and reverse course to help bring it back down. That hasn’t happened, leaving it to the Federal Reserve to attack inflation.

While Fed Chair Powell was using the word “transitory” when he spoke about inflation, the bond market remained calm. That has changed. “March of 2022 will be remembered as the beginning of the acceleration of the worst bear market in bonds in 50 years.” (Morgan Stanley, April 2022.) That acceleration began after Fed governor Lael Brainard said the central bank was strongly committed to curbing inflation. Last year she advocated sticking with easy-money policies. Her reversal bolstered expectations that the Fed will now reduce its trillion $ in assets more aggressively as interest rates are raised.

Bond market investors now worry that the Fed will raise interest rates higher than expected this year. When interest rates go up bond prices go down. Now they are going down in anticipation of rising interest rates.

It is a shame that Democrats are not willing to back down on their anti-American energy rhetoric and policies. In the April 4 issue the *Wall Street Journal* had this to say: “Democrats have gasoline price amnesia, or hope Americans do. On Wednesday they’re holding another political struggle session to lash oil and gas CEOs for surging gasoline prices. But only last autumn they were demanding that these same companies produce less oil to reduce the global supply of crude.

If progressives truly cared about the climate, they'd support more U.S. oil and gas production, which could replace supply from countries with lower environmental standards and higher emissions."

The number one greenhouse gas is methane. American energy companies are the world's best in preventing methane pollution when drilling for oil and gas. And the oil we produce is cleaner than oil coming from Venezuela and Russia. That oil requires more treatment than U.S. oil.

The bottom line is that we are stuck with rising inflation and can only hope the Fed will not have to go too far in tightening monetary policy to get inflation under control.

We are now entering first quarter earnings reporting season. In the fourth quarter of last year earnings per share for the companies in the S&P 500 index were up 32.1% from a year earlier. Clearly rising costs did not hurt profit margins last year. But this year is looking different. There was a surge in fuel costs at the end of February when Russia invaded the Ukraine. Over time companies can pass on these costs to consumers, but the suddenness of some of these increases probably meant that companies could not act fast enough to prevent inflation from taking a bite out of first quarter earnings.

Analysts are now estimating that first quarter profits for the S&P 500 companies will be up 6.4% from a year ago. Actual earnings tend to come in better than the estimates. But even a 6.4% gain after the surge in profits last year would be something to celebrate. I find it interesting that these same analysts expect revenue for the S&P 500 companies to be 10.9% better than a year ago. Are analysts putting too much weight on rising labor and other costs? Or do companies have more pricing power than analysts believe?

JPMorgan Chase economists estimate first quarter GDP growth to be 10.4%. If they are right, then I expect S&P per share profits to be better than the current 6.4% estimate.

In any case corporate profits are rising nicely. That provides fundamental support for stock prices. The Covid fear and all the other uncertainties are causing stock market volatility. That is understandable, but don't be tempted to try trading this market. The long-term outlook is still bright.

I will have the next market review and update for you one week from today on Wednesday April 20, 2022

All the best,

John Dessauer