John Dessauer Investments, Inc.

John Dessauer's market review and update as of Wednesday June 15, 2022

I was feeling pretty down after the 880 point Dow drop last Friday and the continuing drop on Monday. I thought the stock market looked undervalued before that plunge. So I was very happy to see the following from Mitch at Zacks investment management:

"Sentiment about the U.S. economy is overwhelmingly negative, even as growth fundamentals continue to point to expansion. In my view, that's bullish.

In a recent *Wall Street Journal*-NORC poll, conducted with the University of Chicago, a staggering 83% of respondents said the economy was in a poor or 'not so good' state. 35% of respondents reported being unhappy with their financial situation, which marks the highest level of dissatisfaction since 1972 – the first year of the survey.

Consider this: According to the poll's findings, people are more unhappy today *than they were in the aftermath of the 2008 Global Financial Crisis*, when the jobless rate was double-digits and millions of people lost their homes. Today's inflationary pressures, and in particular higher food and gas prices, are a major thorn in folks' sides. I get that. But thinking the economy today is worse off than it was in 2008 and 2009 feels like sentiment has become overly pessimistic. If economic growth exceeds these hyper-low expectations, even by just a little, I think that's great for stocks.

Early data in Q2 point to this better-than-expected growth outcome.

The most important growth factor in the U.S. economy – consumer spending – continues to exceed expectations. Data shows consumer spending increased 0.9% in April, with March's figure revised higher from 1.1% to 1.4%. Consumers are also increasingly shifting from goods spending to services spending, which should bode well for inflationary pressures in the second half of 2022. Goods spending was up 0.8% in April, while services spending in areas like hotels and restaurants moved up 0.9%.

The U.S. Labor Department also reported that employers added 390,000 new jobs in May, with wages increasing 5.2% year-over-year. For the year leading up to May, the economy added a robust 400,000 jobs per month, *the strongest period of job gains dating back to 1939*. Initial jobless claims also fell to 200,000 in the final week of May, indicating that employers are holding on to workers in hopes of avoiding further shortages. The unemployment rate remained steady at 3.6%, a far cry from the 10+% unemployment rate reached during the 2008 Financial Crisis and the Covid-19 pandemic.

Manufacturing and services in the U.S. continue to demonstrate resilience. The May Manufacturing PMI was 56.1%, which marked an increase of 0.7% from April and firmly suggests the economy remains in expansion mode. Manufacturing activity has been expanding for 24 straight months now in the U.S., and businesses surveyed continue to point to strong demand looking ahead. For every cautious comment made in the survey, there were five positive growth comments.

The U.S. services sector also posted strong activity in May, with the Services PMI registering at 55.9%. Services have also expanded for 24 months straight. A close read of the May jobs report offers a hint that the services sector could feel additional tailwinds heading into summer—retailers cut nearly 61,000 jobs in May, but leisure and hospitality employers added 84,000.

Finally, the inflation issue – while still a negative force in the economy – improved slightly in April. The personal consumption expenditures (PCE) price index ticked up by 0.2%, which marked the smallest rate of increase since November 2020. The 12-month rate of increase in April (+6.3%) was also a step down from March's +6.6%. Excluding food and energy prices, the PCE rose +4.9% year-over-year in April, which marked the smallest increase since last December. It's still too early to call 'peak inflation,' but April showed the issue getting better – not worse.

Bottom Line for Investors

My goal with this week's column was not to demonstrate that the U.S. economy is in perfect shape and that no one should worry. Plenty of headwinds persist.

But I do firmly believe the positives outweigh the negatives, with key growth fundamentals nearly confirming expansion in the months ahead. Perhaps the obvious revelation here is that inflation is a very powerful negative force for sentiment, but it also may be so powerful that it causes many people to miss or ignore the parts of the economy that are working well and growing. In my view, that creates a bullish setup: any time a strong or modestly strong economy is under-appreciated to this degree, even the tiniest upside surprise can send stocks rallying."

In my view the greatest threat to the economy is the Biden talk about raising taxes. The recent data from the Congressional Budget Office shows that there is no need for higher taxes. The Federal Government is enjoying record inflows of tax revenue.

"Individual income tax collections are poised to reach $2.6 trillion, or 10.6% of the economy in the fiscal year that ends Sept. 30, according to the Congressional Budget Office. That is up from 9.1% in 2021 and would mark a record in the 109-year history of the tax, topping the war-tax receipts of 1944 and the dot-com boom of 2000." (The Wall Street Journal 6/6)

Given the President's poor approval ratings and the ongoing inflation uncertainty I doubt the President will be able to push through such a massive tax hike between now and November. After that, if the polls are right, he will not be able to raise taxes because he will have lost control of the House and perhaps the Senate.

When stocks fall under heavy selling pressure you never know exactly when or at what level the selling will stop and the rebound begin. What history tells us is that a rebound is coming. And given the underlying economic strengths the coming rebound is very likely going to be strong and setting the stage for future stock market gains.

There is a sign that inflation really is peaking. A national real estate organization published a report showing that home price are falling in ten major cities, including Los

Angeles. If the inflation peak is confirmed by other data then the stock market will rebound soon, catching all the current sellers by surprise.

I will have the next market review and update for you one week from today on Wednesday June 22, 2022

All the best,

John Dessauer