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Brevity Series – Jobs and Earnings

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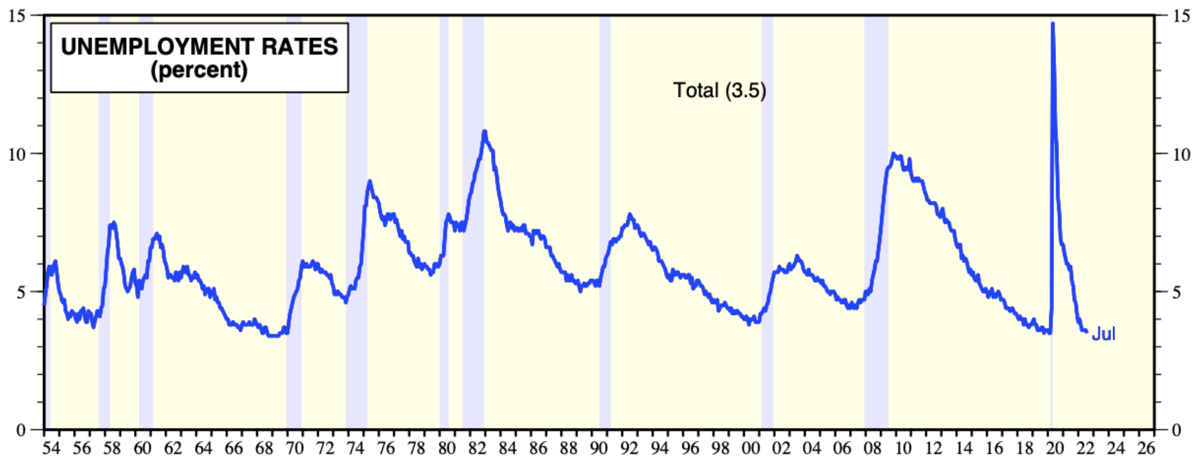
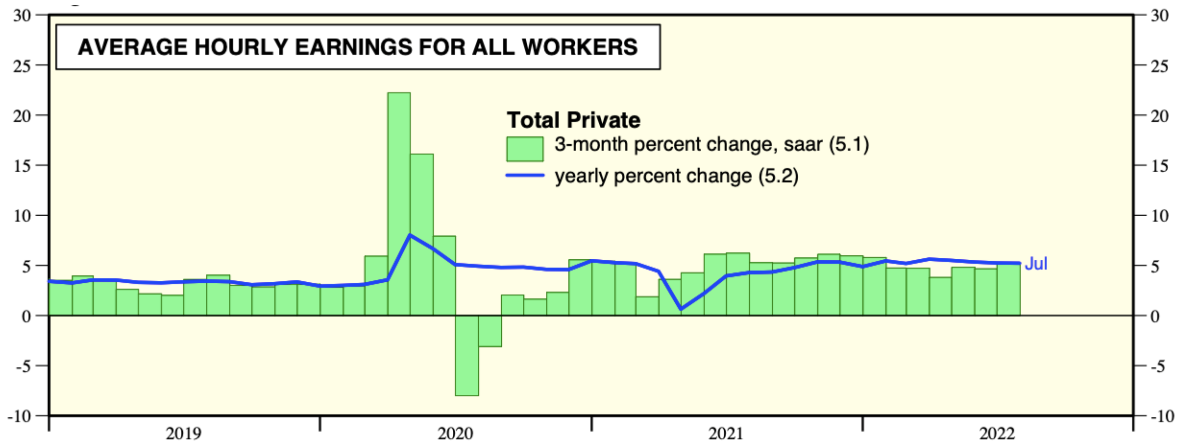
Investors were sharply focused on the July employment report released by the Bureau of Labor Statistics this past Friday morning. It is an important indicator of the health of the U.S. economy. The number of jobs created blew away the consensus expectations of economists. The expectation was for the economy to add 250,000 jobs in July, the actual number was more than double that at 528,000. The July report also revised the May and June employment reports higher. The number of jobs in the U.S. economy is now at a record high, surpassing pre-pandemic levels, and there is effectively no unemployment.



Stock and Bond markets sold off significantly on the news. During periods of Fed tightening good news becomes bad news and bad news becomes good news. Investors fear that the strong employment report will force the Federal Reserve to tighten more aggressively. They may be right, but we greatly prefer good news over bad news. Good news may be interpreted as a short-term negative, but good news is always a long-term positive. It is far easier to reduce employment than to create employment.

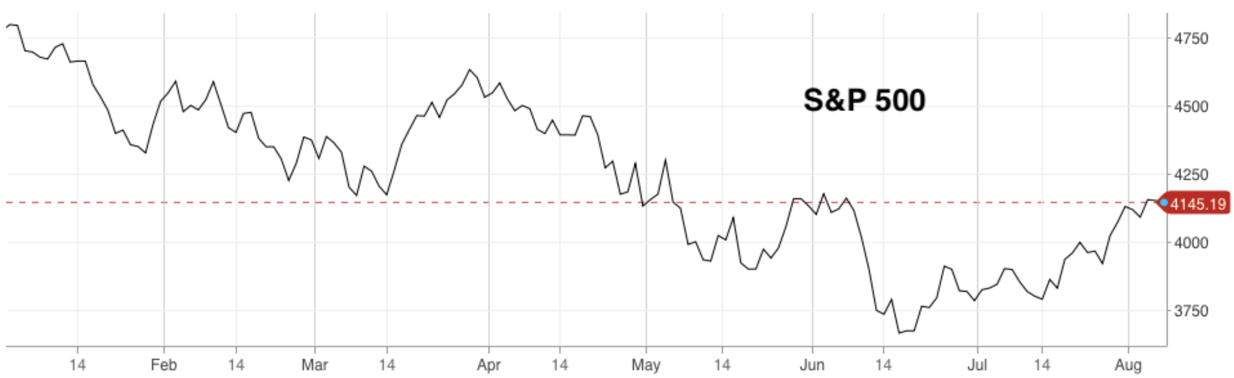
Although the jobs added number dominated the headlines, the number we were most focused on in

Friday's employment report was wage inflation. Wage inflation came in at 5.2%. That's still a bit too high, but it is well below the current 9.1% CPI. It supports our thesis that inflation is inflating corporate revenues faster than it is inflating corporate costs.

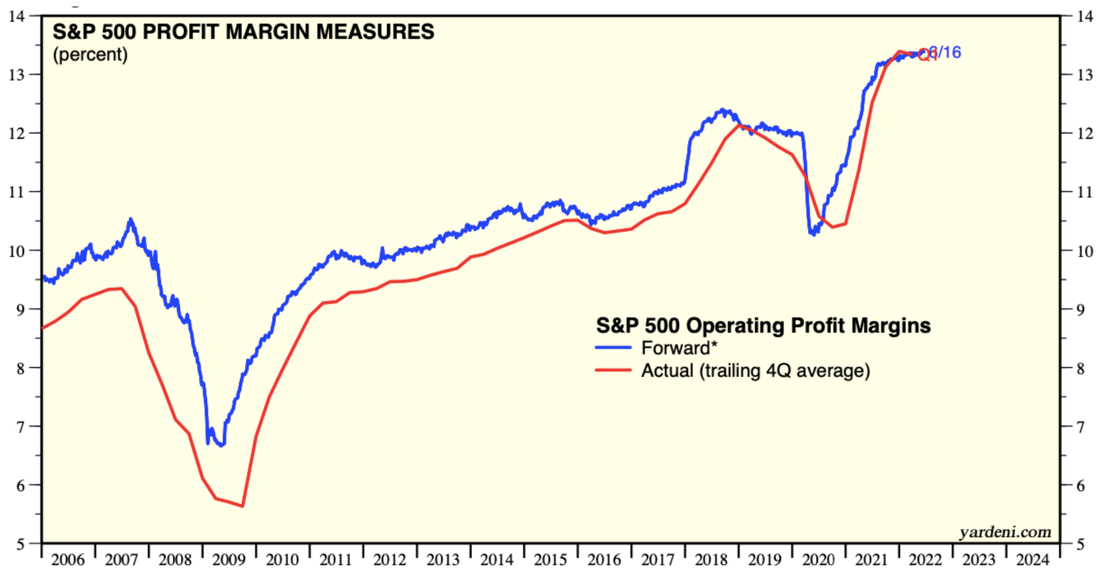


Labor is the largest component of corporate costs. Higher labor costs hurt corporate profits. For all the complexities of stock market pricing it really comes down to this; investors will pay the price for a stock that they perceive to be the present value of that company's future earnings. The price of a stock represents that equilibrium opinion. The reason why stocks fluctuate much more (higher volatility) during periods of economic uncertainty is partly due to a wider divergence of opinions on future corporate earnings. Bears believe the Fed will need to crush the economy and future earnings in order to get inflation under control. Bulls believe the Fed can moderate inflation with only minimal harm to corporate earnings. Those are two very different views of what the future holds.

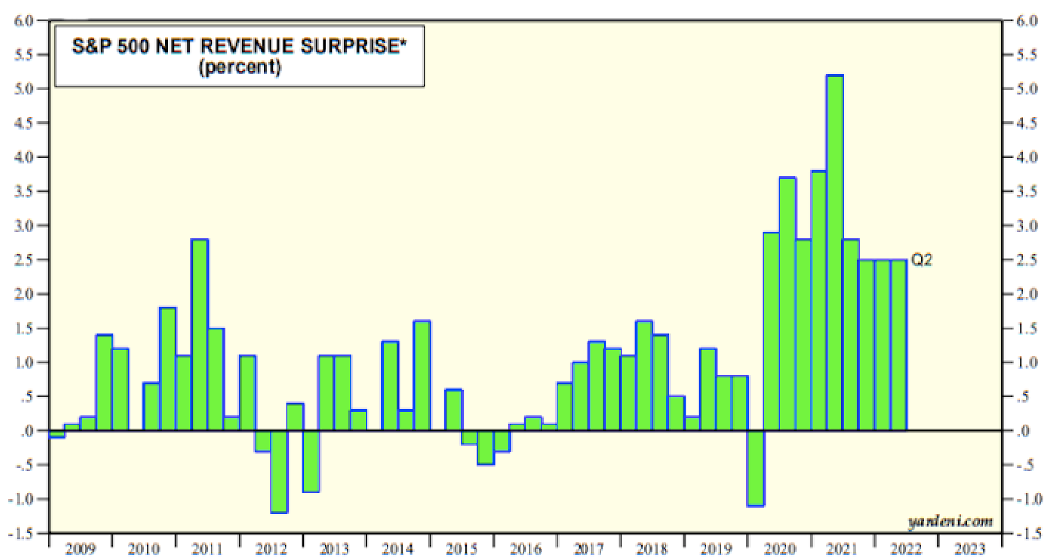
After falling 23%, since June 16th the S&P 500 has recovered 10% of its losses and is now down -13% YTD. The Bears pushed markets lower over inflation fears. The Bulls have fought back with the help of Q2 earnings.

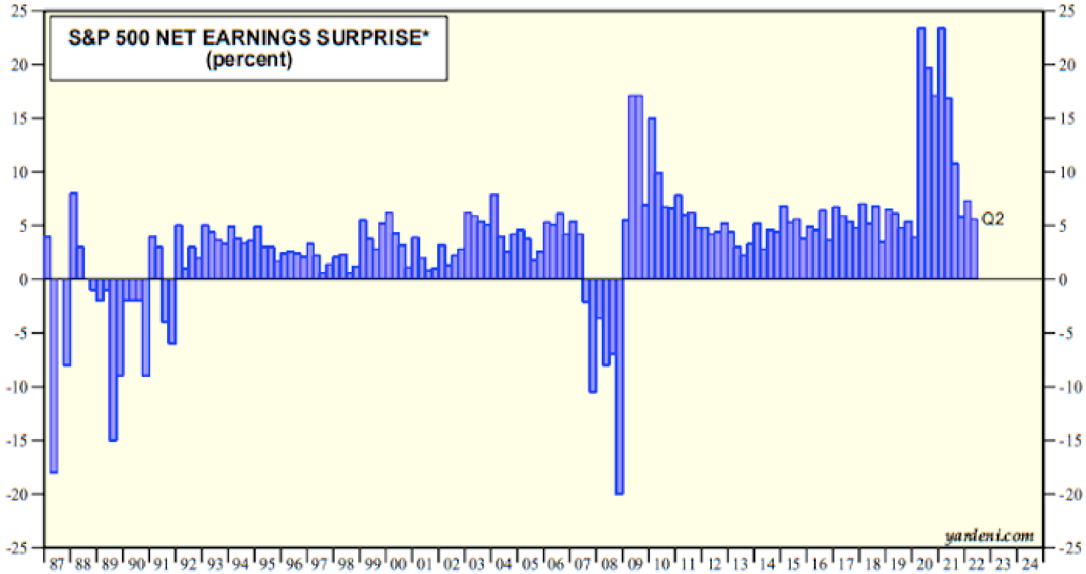


Reported earnings are once again coming in stronger than forecasted earnings. Fears of inflation eroding profits through higher costs are not being realized. It once again appears that technology and globalization are enabling corporations to increase worker productivity and avoid a wage-price spiral. This is protecting record-high profit margins.

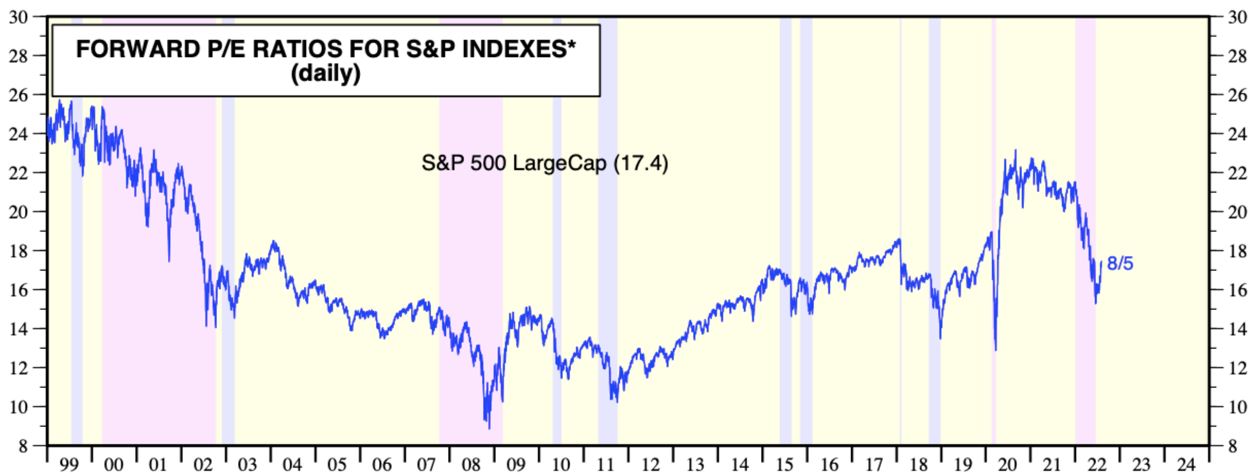


So far 71% of S&P 500 companies have reported. 68% have beaten their revenue estimates and 77% have beaten their earnings estimates.





What's remarkable about this recent sell-off and subsequent partial recovery in stock markets is that it is almost entirely attributable to changing valuation multiples, corporate earnings have been extremely consistent. It's investors' fears and uncertainty about future corporate earnings that are driving prices up and down, not earnings. Earnings and earnings growth continue to be strong.



We continue to expect inflation to moderate and for the S&P 500 (currently 17.4X) to eventually return to trading within an 18X to 20X range. There is nothing in the recent jobs or inflation data that we find overly troubling. On the contrary, we find it encouraging.

We hope everyone is enjoying the summer. Perhaps many of you have taken advantage of the stronger Dollar (and fewer Covid restrictions) to travel overseas. We hope so. MMFS will also be traveling internationally.

The MMFS Team

Jon C Mommaerts, CFP®: Jon is a Principal of Mommaerts Mahaney Financial Services, Inc. He has over 30 years of experience working with professionals and those about to retire. He is a member of the Financial Planning Association, as well as a member of the Preferred Financial Advisors.

J. Matthew Tuccini, CFP®: Matt has over 17 years of experience working in the financial services industry with vast experience in retirement planning, tax strategies, and financial planning.

Robert Kea, CFA: Bob has over 30 years of experience in portfolio management. He was a founding member and Co-Head on Putnam's Asset Allocation Group, which managed $12Bn in both retail and institutional assets.

Jason Rolling, Financial Advisor: Jason has been in the financial services industry for the past 15 years. His financial experience includes retail banking, consumer & commercial lending, bank management at the local, regional and SVP level, wealth management, and financial planning.

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Mommaerts Mahaney Financial Services, Inc. provides advisory services through ERTS Wealth Advisors, LLC, a registered investment advisor.
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