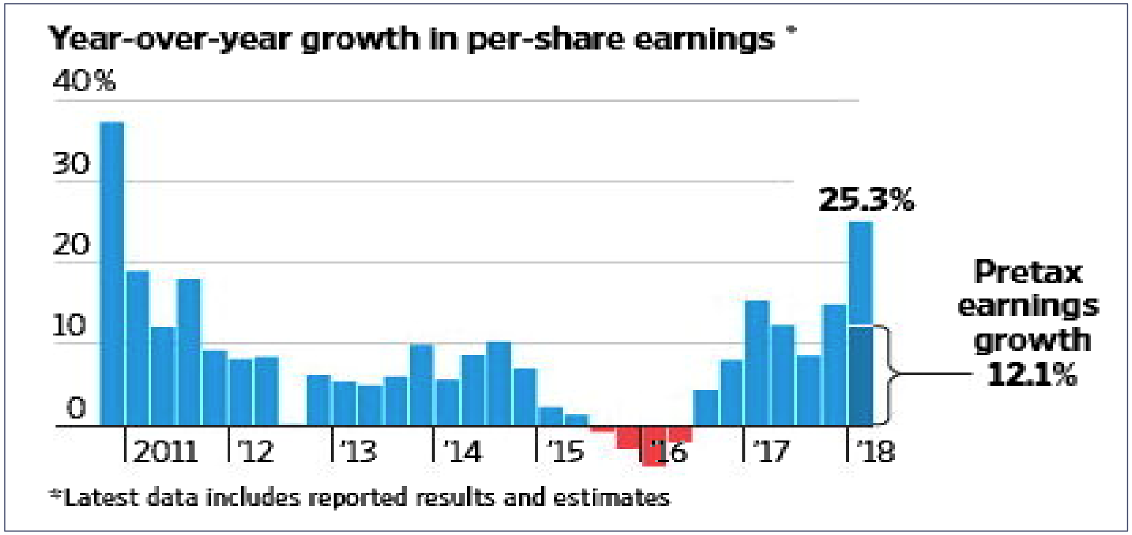
Market Recap

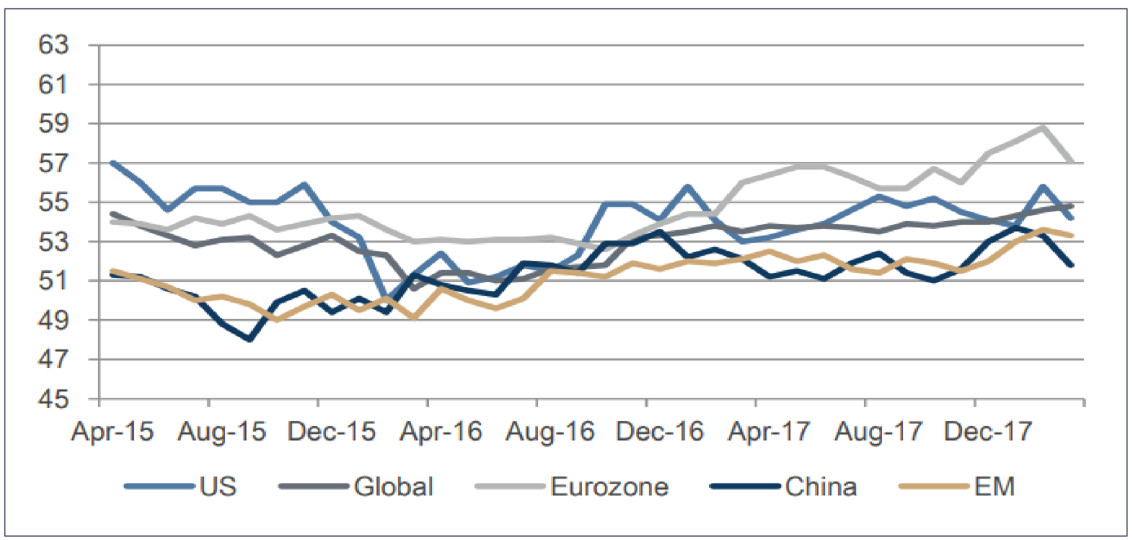
Accelerating Earnings Growth



Source: WSJ

First quarter earnings growth rates have risen steadily, helped by stronger than expected revenue growth, higher pre-tax earnings growth, and lower corporate taxes. As of May 3rd, first quarter earnings for the S&P 500 were estimated to grow 25.3% year over year, the seventh consecutive quarter in which earnings growth has been positive. While many have attributed the strong growth in earnings to a lower corporate tax rate, pre-tax earnings growth is a healthy 12.1%, driven primarily by 8.5% growth in revenues year over year, the highest level of revenue growth since the 3rd quarter of 2011. Nevertheless, these impressive earnings growth rates may prove difficult to sustain in 2019 given that the benefits of tax reform will no longer be reflected in year over year figures.

Global Growth Entering More Mature Phase



Source: Neuberger Berman

Global manufacturing purchasing manager indices ("PMIs") have peaked in recent months, and it appears they are unlikely to achieve new highs in the current economic cycle. As a leading indicator for the economy, the pullback in PMI readings suggests that current GDP growth levels may be in the midst of plateauing. With demand heating up, bottlenecks are now beginning to form in certain parts of the supply chain, most notably in raw materials and transportation costs. Although this new development is causing headaches for some manufacturers, running into capacity constraints is a natural feature of late cycle dynamics. The resolution (or lack thereof) of ongoing international trade tensions will help determine whether the slowdown is a gradual or more aggressive process.

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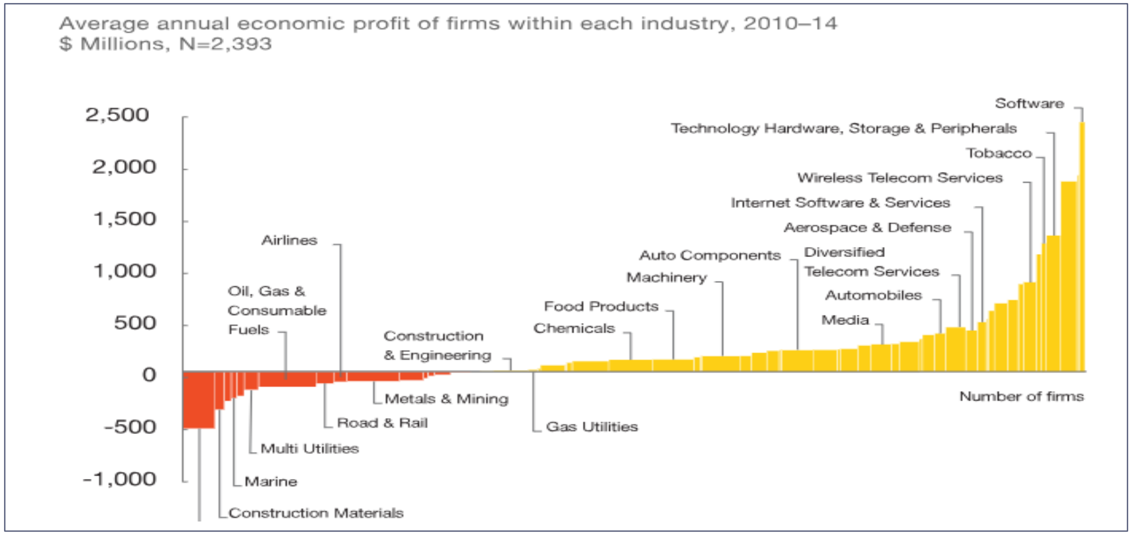
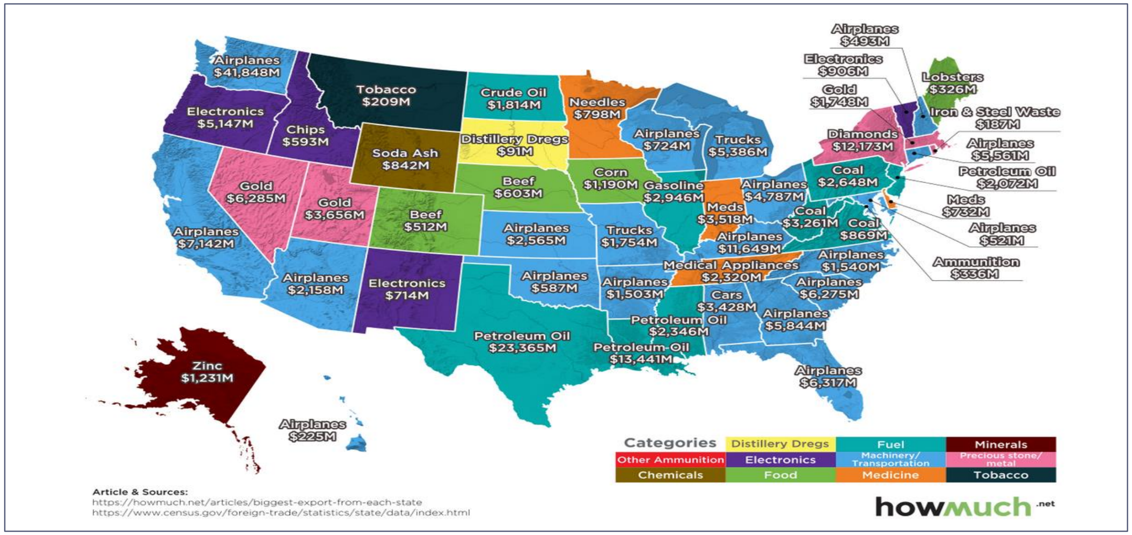
Economic Profitability Among Industries



Source: McKinsey

A recent McKinsey study on economic profits (defined as a company's profit net of its cost of capital) provides an interesting framework for thinking about the tensions governing competition and profit across various industries. The core underlying assumption is that excess profits attract competition, which in turn erode industry profits to their natural point of equilibrium. The study's findings generally validate this principle, but also shed light on some wrinkles at either extreme of the spectrum – while the average industry makes almost no economic profit, those in the top quintile earn a profit that is 30x greater than the average. This suggests that it may be better to be an average competitor in a highly profitable industry rather than an above average competitor in less profitable industry.

Production Differences Among States



Source: HowMuch.net and Census Bureau

Different regions of the country excel at producing different things. States like Colorado, Nebraska, and Iowa excel at grains and livestock, while states like Texas, Louisiana and Mississippi excel at petroleum oil. Mountain-West states like Nevada and Utah tilt heavily towards the metals and mining industry, while rust-belt states like Virginia, West Virginia and Pennsylvania tilt heavily towards coal. A significant number of states are heavily exposed to the transportation industry, with either airplanes, trucks or cars representing the largest production category in nineteen states. Surprisingly, Oregon is the only state which sees electronics as its top product, with California (home to Silicon Valley) producing a higher dollar volume of airplanes than technology related products.

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