INVESTMENT STRATEGY INSIGHTS

The Tight-and-Loose Labor Market

November 8th, 2021

Labor Market: Simultaneously Tight and Loose

- The labor market's recovery has slowed, capped by residual pandemic effects, but should eventually return to normal

Not the Fed's First [Tapering] Rodeo

- Markets unsurprisingly remained relatively unphased by the Fed's well-communicated gradual tapering of its bond purchases

After Peak Growth

- Earnings growth may be peaking, but growth is likely to continue at a pace high enough to keep investors' attention

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Labor Market: Simultaneously Tight and Loose

- **Labor Market Tightness.** Friday's jobs report showed improvement with a better-than-expected 531,000 person rise in non-farm payrolls and a decline in the unemployment rate to 4.6%. Hidden beneath the surface of this report, however, was a tight labor market with less than one job seeker for each job opening posted and a continued above-average rise in worker's hourly wages. Company surveys and commentary point to a difficulty in finding qualified labor and a need to hike wages to attract employees.
- **Residual Looseness.** Also embedded within the employment report was a labor market participation rate of 61.6%. The overall U.S. labor force of approximately 161 million persons remains over 3 million short of its pre-pandemic high. In parsing the data, it appears that there are two relatively large and partly overlapping cohorts contributing to this labor force deficit: women, likely due to their still-disproportionate societal responsibility of caring for family members during the pandemic, and workers without a college education that may have used the pandemic as an opportunity to better their educational or training position.
- **Off the Sidelines.** Getting workers off the sidelines and back into jobs may take time, but should eventually occur. Those still not in the labor force that are caring for family members should see their situations change as schools reopen and COVID fears recede. Those seeking higher education or additional training should eventually complete their programs. Still others may simply find the burden of a dwindling bank account enough cause to return to work.

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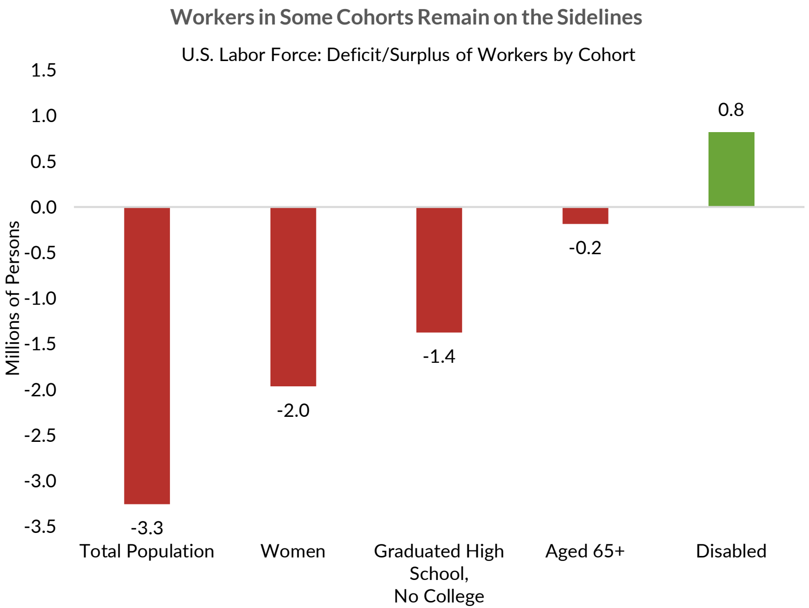
Chart of the Week:



Source: Glenmede, U.S. Bureau of Labor Statistics Data through 9/30/2021
Data shown takes the current size of the U.S. labor force and various subsets, compared to readings as of January 2020. Total Population includes all those in the U.S. civilian noninstitutional labor force, measured in millions of persons. All other categories represent a subset of the Total Population figure.

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Not the Fed's First [Tapering] Rodeo

- **Tapering Plan in Place.** Unsurprising to investors, the FOMC took its first incremental steps in normalizing monetary policy announcing that it will begin tapering. It will reduce its pace of bond purchases by $15 billion per month ($10 billion in Treasuries and $5 billion in mortgage-backed securities) from the current level of $120 billion ($80 billion in Treasuries and $40 billion in mortgage-backed securities) starting in mid-November. The Fed expects to complete this tapering of its purchases in the middle of 2022, allowing the Fed's balance sheet to then plateau at around $9 trillion.
- **Rate Hikes ≠ Tapering?** Fed Chair Jerome Powell has emphasized that the reduction in asset purchases does not share a common decision framework with the timing of interest rate hikes. However, pricing in federal funds futures suggests that investors are expecting at least two rate hikes by the end of 2022. Further, some investors think the FOMC will need to raise rates sooner and more forcefully than the central bank's own projections. Despite the Chairman's attempt to avoid connecting the two, expect the speculation around the timing of rate hikes to persist until the hikes begin.
- **Not the Fed's First Rodeo.** The Fed's prior taper plan provides a guideline for implementation and market reaction. Years after the '08/'09 financial crisis, the Fed began winding down the active expansion of its balance sheet, beginning in mid-December of 2013 and ending in late-October of 2014. Most major asset classes posted positive gains over that period, with global real estate leading the pack with a +14% total return. All else equal, investors should not expect Fed tapering to be a disruptive process for markets.

Markets unsurprisingly remained relatively unphased by the Fed's well-communicated gradual tapering of its bond purchases

After Peak Growth

- **Continued Flow of Earnings Results.** With about 89% of companies in the S&P 500 having reported so far, the blended year-over-year growth rate in earnings, which combines actual results with estimates for companies that have not yet reported, currently sits at +39.1%. So far, 81% of companies have reported a positive earnings surprise, beating consensus estimates by 11.7% on average, despite ongoing supply chain disruptions and labor market tightness.
- **Earnings/Revenues Twin Peaks?** Although EPS growth has been slowing in most sectors, revenue growth has been accelerating in 8 different sectors. This disparity may be explained by the rising costs associated with doing business. The economy continues to recover, with revenues rising, but now costs are rising in many places just as fast, if not faster. Such margin pressure amid strong revenue gains is unique to the current post-pandemic environment, a reflection of pricing pressure on supply-constrained intermediary goods and wage pressure from a surprisingly tight labor market.
- **After-Peak Guidance.** With the peak potentially behind us, some investors have highlighted concern that growth may not be as strong going forward. While it is technically true that peak growth typically occurs after the first year of an economic recovery, such an outcome should not be a primary concern as markets historically have delivered positive returns after earnings growth peaks. The key question will be whether ongoing growth is acceptable. Current estimates, before the impact of the fiscal spending bills, is for near-10% earnings growth in 2022, a level that should keep investors' attentions a little longer.

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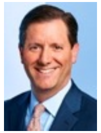
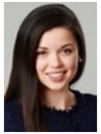


JASON D. PRIDE, CFA
Chief Investment Officer - Private Wealth
Responsible for formulating investment policy and strategy
Serves as a leading member of the Investment Policy Committee
B.S. from Massachusetts Institute of Technology

MICHAEL T. REYNOLDS, CFA
Vice President, Investment Strategy
Responsible for supporting the development of investment strategies, policy and portfolio construction methodologies
Is an active member of the CFA® Society of Philadelphia
B.S. from the Wharton School of the University of Pennsylvania



ILONA V. VOVK, CFP®
Investment Strategy Officer
Responsible for supporting the development of investment strategies, policies and portfolio construction methodologies applied to Private Wealth client portfolios
B.A. and B.S. from Drexel University

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