Corporate earnings under pressure

In the past four weeks, many listed companies reported their half-year figures. The overall impression is that conditions have become more difficult for companies. There is not a single company that does not explicitly mention inflation as a major problem for its own business.

And that is not all: many companies in the manufacturing sector continue referring to supply bottlenecks and component shortages. In service industries in particular, a shortage of labor is leading to lost sales. The many canceled flights at European airports are mainly due to the lack of personnel there. In addition, companies in the consumer goods sector report a dampening of consumer demand due to higher prices. In addition, there are sometimes complaints that employees are unable to travel to carry out necessary maintenance work or even sales abroad (especially China in view of the lockdowns there). The Corona epidemic, which is still not ending, is adding to the problem, and finally, the spectre of an incomplete energy supply is hovering over the European economy.

In view of these developments, it is not surprising that the stock market has had to deal with a number of profit warnings in the last four weeks. Major American banks, which regularly open the reporting season, consistently reported that business was becoming more difficult. Investment banking in particular suffered from a drop in the number of IPOs and corporate takeovers or mergers. At least there were reports of brisk business in bond, currency and equity trading.

The software sector also reported more subdued business, albeit at a high level. At Microsoft, profit expectations were lowered due to a strong U.S. dollar, and at SAP, this was done based on the scaling back of Russian activities.

The environment for companies in the Internet sector, which mainly earn their money from advertising, has also deteriorated. The two big ones in the sector, Alphabet and Meta announced restraint in hiring. The situation was similar for Apple.

In the capital goods sector, there was talk of well-filled order books, but these converted into fewer sales than usual due to the difficulties mentioned above. Nevertheless, there were also some bright spots, for example at SAF Holland and Hermle Maschinenbau.

Companies in energy-intensive sectors such as chemicals and steel feel threatened. Much will depend on the extent to which price increases for upstream products can be passed on to end users. Despite all difficulties, BASF reported quite robust business at the end of the first half. The statements from Covestro were less encouraging.

Companies in the healthcare sector fared little better. The declining earnings situation there is often justified by wage inflation and a shortage of labor. A severe profit warning at Fresenius Medical Care may serve as a pars pro toto here.

Unsurprisingly, the energy sector is currently enjoying a tailwind. Major companies in the sector such as Shell, Exxon, BP, Chevron, OMV, TotalEnergies, Shell and Germany's RWE as well reported significantly higher earnings figures for the first half of the year. On the negative side, the partial nationalization of Uniper stands out.

In contrast, after many years of rapid growth, e-commerce is now experiencing a downturn. Fashion retailer Zalando and even Amazon have had to report that customers are holding back.

All in all, it may be a good sign after months of bearish stock markets that many stock prices have recently been trending upwards despite the gloomy economic situation. This suggests that to a large extent the bad news had already been priced in.

Sincerely yours,

Fund managers and co-investors

Dr. Christoph Bruns Ufuk Boydak

This text was originally published in German.

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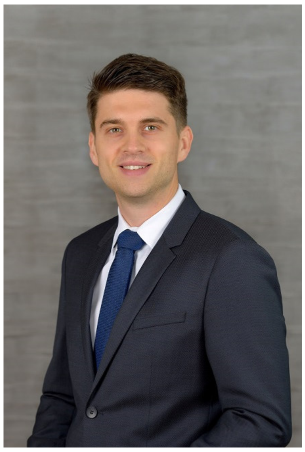

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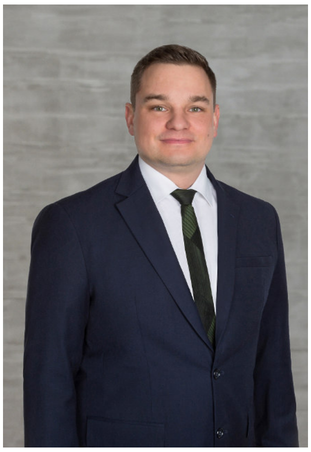

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