Seinfeld’s Market

See the collection of the individual charts linked below.

(1) Jerry & George pitch a sitcom about nothing. (2) The Trauma of 2008 may be finally wearing off. (3) Counting anxiety attacks. (4) Fully invested bears are less panic prone. (5) Other than earnings rising, nothing much is happening for stock investors to get excited about one way or the other. (6) In case you missed them: Recent commotions in Greece, China, and Washington were largely ignored. (7) Breadth remains bullish. (8) Are the rich paying their fair share of taxes?

Strategy I: Nothing Bad Happening. “The Pitch” is the 43rd episode of the TV sitcom Seinfeld. It is the third episode of the fourth season. It aired on September 16, 1992. In it, NBC executives ask Jerry Seinfeld to pitch them an idea for a TV series. His friend George Costanza decides he can be a sitcom writer and comes up with the idea of “a show about nothing.”

The bull market in stocks since March 2009 has had a fairly simple script too. As a result of the Trauma of 2008, investors have been prone to recurring panic attacks. They feared that something bad was about to happen again, so they sold stocks. When their fears weren’t realized, the selloffs were followed by relief rallies to new cyclical highs and to new record highs since March 28, 2013. Their jitters are understandable given that the S&P 500 plunged 56.8% from October 9, 2007 through March 9, 2009 (Fig. 1).

From 2009 through 2016, there were four major corrections and several significant scares. Joe and I kept track of them and the main events that seemed to cause them. By our count, there were 57 panic attacks from 2009 through 2016, with 2012 being especially anxiety-prone with 12 attacks. (See our S&P 500 Panic Attacks Since 2009.)

From 2010 through 2012, there were recurring fears that the Eurozone might disintegrate. There were Greek debt crises and concerns about bad loans in the Italian banking sector. Investors were greatly relieved when ECB President Mario Draghi pledged during the summer of 2012 to do whatever it takes to defend the Eurozone. China also popped up from time to time as concerns mounted about real estate bubbles, slowing growth, and capital outflows over there. At the end of 2012, fear of a “fiscal cliff” in the US evaporated when a budget deal was struck at the start of 2013 between Democrats and Republicans. I expected it, though I certainly had no idea that it would be worked out between Vice President Joe Biden and Senate Minority Leader Mitch McConnell. In a November 9, 2013 Barron’s interview titled “Lifting the Odds for a Market Melt-Up,” I observed:

“I have met a lot of institutional investors I call ‘fully invested bears’ who all agree this is going to end badly. Now, they are a bit more relaxed, thinking it won’t end badly anytime soon. Investors have anxiety fatigue. I think it’s because we didn’t go over the fiscal cliff. We haven’t had a significant correction since June of last year. We had the fiscal cliff; they raised taxes; then there was the sequester, and then the latest fiscal impasse. And yet the market is at a record high. Investors have learned that any time you get a sell-off, you want to be a buyer. The trick to this bull market has been to avoid getting thrown off.”
There was another nasty selloff at the start of 2016 as two Fed officials warned that the FOMC was likely to follow 2015’s one rate hike at the end of that year with four hikes in 2016. Debbie and I had predicted “one-and-done” for 2015 and again for 2016. Contributing to the selloff in early 2016 was the plunge in the price of oil, which had started on June 20, 2014 (Fig. 2). That triggered a significant widening in the yield spread between high-yield corporate bonds and the US Treasury 10-year bond yield from 2014’s low of 253 basis points on June 23 to a high of 844 basis points on February 11, 2016 (Fig. 3). The widening was led by soaring yields of junk bonds issued by oil companies. There were widespread fears that all this could lead to a recession. In addition, the Chinese currency was devaluing amid signs of accelerating capital outflows from China (Fig. 4).

I remained bullish. In a February 6, 2016 Barron’s interview titled “Yardeni: No U.S. Recession in Sight,” I reiterated my opinions that the Fed was unlikely to hike the federal funds rate more than once and that the secular bull market remained intact. Joe and I argued on Monday, January 25 that “it may be too late to panic” and that the previous “Wednesday’s action might have made capitulation lows in both the stock and oil markets.” Sure enough, the price of a barrel of Brent crude oil did bottom on Wednesday, January 20. The S&P 500 bottomed on February 11, the same day that the high-yield spread peaked. The S&P 500 Energy sector dropped 47.3% from its high on June 23, 2014 to bottom on January 20, 2016 (Fig. 5). During the summer of 2016, we perceived the end of the energy-led earnings recession and projected that the bull would resume his charge.

Following the surprising Brexit vote that summer, the stock market declined for just two days despite lots of gloomy predictions. Just prior to the presidential election, I argued that the rebound in earnings, following the recession in the energy industry, would likely push stock prices higher no matter who won. After Donald Trump did so, I raised my outlook for the S&P 500, expecting that a combination of deregulation and tax cuts would boost earnings. The latest bull market was still going strong in early 2017.

I was interviewed again in the February 4, 2017 issue of Barron’s saying, “It would be a mistake to bet against what President Trump might accomplish on the policy side. I’m giving him the benefit of the doubt, hoping good policies get implemented and bad ones forgotten. We could get substantial tax cuts. All his proposals don’t need to be implemented for the Trump rally to be validated. If you get $1 trillion to $2 trillion coming back from overseas because of a lower tax on repatriated corporate earnings, that would be very powerful in terms of keeping the market up.”

So far, investors are relieved that the bad outcomes predicted by the naysayers about Trump in the White House haven’t happened. The anticipated bullish outcomes are also still mostly on-the-come. Nothing really terrible or wonderful is happening other than that earnings are rising in record-high territory again, as we discussed just yesterday (Fig. 6).

By the way, in case you missed it, you might be relieved to know that Greece and its international creditors yesterday reached a preliminary deal allowing the country to receive yet another round of bailout payments in exchange for promises to raise taxes and to further cut pensions and social spending. Chinese stocks seem to be stabilizing this week, having dropped sharply during the second half of April after officials slammed what they called short-term speculators. This past Sunday evening, congressional leaders reached an agreement on a spending deal that would fund the government through the end of September and avoid a looming shutdown. This weekend, the French are likely to elect a President who is all for the EU and euro. These developments should all be a relief, though no one really worried much about any of them this time. Nothing bad is happening, which is good news for stocks.

**Strategy II: Good Breadth.** A glance at some of the more widely followed technical indicators of the
stock market shows that the bull remains on solid ground because nothing bad is happening. The S&P 500 VIX was down to 10.11 on Monday, the lowest since February 19, 2007 (Fig. 7). It is well correlated with Investors Intelligence weekly reading of bearish sentiment, which remained relatively low at 17.9% at the end of April.

In some ways, it almost seems like a new bull market started in early 2016 once the price of oil bottomed. The percentage of S&P 500 stocks that had positive y/y comparisons plunged to 28% on February 12, 2016 (Fig. 8). This measure of breadth rebounded to 90% on February 10. That was the highest reading since September 5, 2014, just before oil prices plunged. In late April, 77% of the S&P 500 stock prices were still up on a y/y basis.

US Taxes: Fair Shares. Most Americans believe that the wealthy among us don’t pay their fair share of income taxes. Melissa and I have been looking at the data and conclude that the rich are not guilty as charged. In fact, the evidence suggests that top earners pay more than their fair share, actually paying above half of US personal income taxes. Last week, President Donald Trump released guidelines for a tax plan that would lower tax rates for all income levels. Some have characterized the plan as slanted in favor of the top income brackets. For example, look no further than the 4/27 New York Times cover story titled “Tax Overhaul Would Aid Wealthiest.” But of course, an across-the-board tax cut would benefit disproportionately those who pay the bulk of the taxes! Let’s have a look at the data:

(1) Wealthy shares. We track the Internal Revenue Service (IRS) annual data in our Income Taxes Paid By Income Level. US taxpayers with adjusted gross income (AGI) over $200,000 paid 58.3% of total income taxes in 2014 (Fig. 9). That compares to their 34.2% share of total AGI that year (Fig. 10). So top earners paid a higher share of total income taxes than the share of AGI they earned.

Meanwhile, the opposite was true for lower income groups. Taxpayers earning between $100,000 and $200,000 annually paid 21.6% of all income taxes, while their share of total AGI was 24.2%. Those earning under $100,000 paid 20.2% of all income taxes, while their share of AGI was 41.6%.

Similar insights can be gleaned from a June 2016 Congressional Budget Office (CBO) report titled The Distribution of Household Income and Federal Taxes, 2013. During 2013, according to the CBO, households in the highest income quintile paid 69.0% of federal taxes while they received an estimated 52.6% of before-tax income. “In all other quintiles, the share of federal taxes was smaller than the share of before-tax income,” according to the report. In the bottom quintile, households received 5.1% of income and paid 0.8% of taxes. Households in the middle quintile received 13.9% of income and paid 8.9% of taxes.

(2) Net recipients. A public policy blog from the American Enterprise Institute (AEI) did some number-crunching based on the CBO data. According to AEI’s arithmetic, only the two highest income quintiles were actually net tax payers. The average net federal tax rates after government transfers for the highest to lowest quintiles were as follow: 21.8%, 2.5%, -11.2%, -25.7%, and -34.6%. The effective rates for the lowest, second, and middle income quintiles are negative because those groups received more in government benefits (i.e., Social Security, Medicare, Medicaid, unemployment insurance, etc.) than they paid in taxes.

AEI cleverly outlined another way to think about the burden of the “net payer households” in the top income quintile. The average US household in the top income quintile in 2013 paid $57,700 in taxes. But think of it as if they wrote four checks—three in the amounts of $8,800, $12,200, and $7,800, representing the average net transfer payments to a household in the lowest, second, and middle-income quintiles (i.e., the “net recipients”), and a fourth check for the balance of $28,900 that would go directly to the federal government. Considered this way, the highest income quintile is financing the
“system of transfer payments” and “funding the operation of the federal government.”

(3) **Unfounded perception.** Notwithstanding what the data show, 63% of Americans who responded to Gallup’s 2017 Economy and Finance Survey said that upper-income people pay too little in taxes and 48% said that lower-income people pay too much in taxes. To the same question, 51% of respondents said that middle-income people also pay too much in taxes.

Brookings Institution fellow Vanessa Williamson published a book of interviews about how Americans feel about taxation. According to the 3/29 *Washington Post*, Williamson said: “If you ask people what bothers them most about taxes, the most common answer is that they think … the wealthy aren’t paying their fair share. But people tend to understand this as a problem of loopholes. They think that the reason rich people aren’t paying enough is that they have access to all these special deductions.”

Again, the data tell a different tale. In 2014, taxpayers earning $0 to $50,000 had deductions equivalent to 11.9% of their AGI (Fig. 11). That was almost exactly the same percentage as those earning over $500,000, at 11.6%! The group that benefited most from deductions was the second to lowest income group, earning $50,000 to $100,000 with 32.8% in deductions relative to their AGI.

**CALENDARS**

**US. Wed:** ADP Employment 170k, ISM & Markit NM-PMIs 55.8/52.3, MBA Mortgage Applications, EIA Petroleum Status, Treasury Refunding Announcement, FOMC Announcement. **Thurs:** Merchandise Trade Balance -$44.5b, Factory Orders 0.4%, Nonfarm Productivity 0.0%, Jobless Claims 246k, Challenger Job-Cut Report, Weekly Consumer Comfort Index, EIA Natural Gas Report. (Bloomberg estimates)

**Global. Wed:** Eurozone GDP 0.5%q/q/1.7%y/y, Germany Unemployment Change & Unemployment Rate -11k/5.8%. **Thurs:** Eurozone Retail Sales 0.0%m/m/2.1%y/y, Eurozone, Germany, France, and Italy Composite PMIs 56.7/56.3/57.4/54.6, Eurozone, Germany, France, and Italy NM-PMIs 56.2/54.7/57.7/53.6, UK Composite & NM-PMIs 54.5/54.5, Draghi, Poloz, Lowe. (DailyFX estimates)

**STRATEGY INDICATORS**

**S&P 500 Earnings Season Monitor** (link): With two-thirds of the S&P 500 companies finished reporting Q1-2017 results, their revenue and earnings surprise metrics and y/y growth are stronger than at the comparable point of the Q4 season. Of the 329 companies in the S&P 500 that have reported, 77% exceeded industry analysts’ earnings estimates by an average of 6.7%; they have averaged a y/y earnings gain of 10.8%. At the same point in Q4-2016, a lower percentage of companies (70%) in the S&P 500 had beaten consensus earnings estimates by a smaller 4.1% and earnings were up a lower 7.9% y/y. On the revenue side, 63% beat sales estimates so far, coming in 0.7% above forecast and 8.0% higher than a year earlier. During Q4, a lower 49% were above forecast, which exceeded estimates by a smaller 0.3% and rose a lower 4.3% y/y. Q1 earnings results are higher for 65% of companies versus a higher 71% at the same point in Q4, but revenues are higher for 78% versus 72%. The S&P 500’s earnings beat is the highest in eight quarters and the revenue surprise is the best in nine quarters. These figures will change as more companies report, but the results to date are encouraging and bode well for future estimate revision activity. However, y/y growth is likely to slow in the coming quarters as comparisons become less easy.

**US ECONOMIC INDICATORS**

**Auto Sales** (link): Motor vehicle sales remained around recent lows in April, edging up to 16.9mu
(saar), after falling from a cyclical high of 18.4mu at the end of last year to 16.6mu in March, which was slowest pace since February 2015. Light truck sales continued to slide, falling to an eight-month low of 8.6mu (saar); it reached a cyclical high of 9.3mu four months ago. Domestic car sales, at 4.7mu (saar), was little changed from March’s five-year low of 4.6mu (saar). Meanwhile, sales of imports climbed to 3.6mu (saar) last month after sinking to a nine-month low of 3.4mu in March; it was at a cyclical high of 3.9mu in December.

GLOBAL ECONOMIC INDICATORS

Global Manufacturing PMIs (link): Global manufacturing activity in April slowed to a three-month low, though held around the Q1 average of 52.9. The JP Morgan M-PMI slipped to 52.8 from 53.0 the previous two months. Both output (to 53.7 from 54.2) and new orders (53.7 from 54.2) rose at a slower rate, while new export orders (52.6 from 52.4) and employment (51.5 from 51.4) grew at a slightly faster pace. The developed nations (to 54.1 from 53.9) recorded stronger growth than emerging markets (50.8 from 51.6), as the former was back up at January’s cyclical high, while the latter fell from March’s near three-year high. While US manufacturing (52.8 from 53.3) showed a mild deceleration in growth last month, the Eurozone (56.7 from 56.2) saw its best growth in six years, the UK (57.3 from 54.2) its best in three years, and Japan (52.7 from 52.4) one of its fastest rates over the past three years. Within the Eurozone, seven out of the eight nations covered posted robust growth: Germany (58.2, near March’s 71-month high), Austria (58.1, 73-month high), the Netherlands (57.8, steady near its cyclical high), Italy (56.2, 73-month high), France (55.1, 72-month high), Ireland (55.0, 3-month high), and Spain (54.5, 2-month high); Greece’s (48.2) manufacturing sector continued to contract. The slowdown in the emerging markets was mainly centered in China (50.3, 7-month low), which expanded only marginally.

US M-PMI (link): Manufacturing activity in April grew at the weakest pace since last fall according to Markit’s survey and at the slowest so far this year according to ISM’s. The ISM M-PMI fell for the second month, to 54.8, after rising steadily from 49.4 in August to 57.7 in February—which was the highest since August 2014. Only the production (to 58.6 from 57.6) and inventories (51.0 from 49.0) measures improved last month, with the former holding near February’s cyclical high of 62.9, while the latter expanded for the second time in 22 months, the first occurring in February. The new orders measure (57.5 from 64.5) dipped, though remained at a robust level as new export orders (59.5 from 59.0) expanded at the fastest pace since November 2013. The employment index (52.0 from 59.9) showed manufacturers hired at a considerably slower pace than in March, when it jumped to its best reading in six years. Still, it’s in expansionary territory for the seventh month, after contracting seven of the first eight months of 2016. The supplier deliveries’ gauge (55.1 from 55.9) remained near March’s 27-month high. Markit’s M-PMI eased for the third month since reaching a 22-month high of 55.0 at the start of this year, falling to a seven-month low of 52.8 last month. According to the report, “The signs of slowing growth are most evident in the domestic consumer sector, but investment goods manufacturers continue to fare well, enjoying stronger capital equipment spending from the energy sector in particular. Exports have also perked up, with April seeing the steepest increase in foreign orders for eight months.” Despite the slowdown, hiring picked up in April, along with business optimism.