



MORNING BRIEFING

May 24, 2017

Global Synchronized Moderate Growth

See the [collection](#) of the individual charts linked below.

(1) Wish for better earnings has come true. (2) S&P 1500 rising in record territory. (3) S&P 500 earnings estimates for 2018 high and dry. (4) S&P 500/400/600 all had upside earnings hooks during Q1 reporting season. (5) Altogether now. (6) A world of upbeat PMIs. (7) Real GDP tracking 2% in major economies. (8) Germany's business confidence is soaring. (9) Aging is a drag on growth. (10) Less secular growth until further notice.

Strategy: Stable Earnings Squiggles. Our Blue Angels analysis of the S&P 500/600/400 stock price indexes and their forward earnings and forward P/Es shows that stock prices peaked at record highs in mid-2015, then stalled for about a year before climbing to new record highs during the second half of 2016 ([Fig. 1](#)). A closer look shows that during the stall period, stock prices actually swooned, with the S&P 1500 stock price index falling 14.7% from its record high on May 21, 2015 to last year's low on February 11, 2016 ([Fig. 2](#)).

Back then, investors were worried that the earnings recession in the energy sector might spread to other industries. They also worried that it might cause another financial crisis as yields soared in the high-yield bond market, led by junk bonds issued by energy companies. Everyone was yearning for good earnings. Their wishes came true as the price of oil rebounded during the first half of 2016, and earnings started to grow again on a y/y basis during the second half of last year. Valuation multiples also rebounded.

For the S&P 1500, forward earnings fell 4.1% from the week of October 9, 2014 through the week of March 3, 2016 ([Fig. 3](#)). Since then, it has rebounded 11.4% through mid-May of this year to a new record high. Joe and I continue to be impressed by how well analysts' consensus earnings estimates for 2018 are holding up ([Fig. 4](#)). Here are a few more happy observations on the latest weekly earnings data:

(1) *Earnings growth.* We track the weekly data on analysts' consensus earnings expectations for the current year and coming year for the S&P 1500/500/400/600. We also track their forward earnings, which are the time-weighted averages of the current-year and coming-year forecasts. With all these data points, we can easily calculate analysts' earnings growth expectations. Doing so for the S&P 500 for each year since 2011 shows a downward trend for each year through this year. So far, 2018's expected growth is holding up remarkably well around 12% ([Fig. 5](#)).

(2) *Forward earnings.* The forward earnings of the S&P 500/400/600 all continue rising in record-high territory ([Fig. 6](#)). The same can be said of forward revenues.

(3) *Earnings hooks.* Often during earnings seasons, actual results for the S&P 500/400/600 tend to beat analysts' expectations, resulting in an upward hook for the weekly series we track for each quarter ([Fig. 7](#)). That happened again for the Q1-2017 earnings season, resulting in better-than-expected y/y growth rates of 14.3%, 12.3%, and 8.9% y/y for the S&P 500/400/600.

Global Economy I: Synchronized Moderate Growth. The upbeat outlook for 2018 earnings isn't happening only in the US. Consensus expected earnings estimates are actually rising for both 2017 and 2018 overseas ([Fig. 8](#)). As a result, forward earnings (in local currency) of the All Country World ex-US MSCI rose in mid-May to the highest level since November 2008. Our Blue Angels analysis shows that this stock price index is up 7.6% ytd through Monday and is closely tracking the index's Blue Angels forward earnings (in local currency), with a forward P/E of 14.4 ([Fig. 9](#)). That's below the US MSCI's forward P/E of 17.6.

The EMU MSCI's forward earnings is contributing to the global rebound in the broader overseas earnings measure ([Fig. 10](#)). At the same time, the EMU MSCI forward P/E has rebounded from 13.3 in December to 15.0 currently. As a result, this stock price index is up 10.0% ytd in euros, outperforming (in local currencies) the US MSCI (7.1), the UK MSCI (5.0), and the Japan MSCI (2.3). The latest batch of global economic indicators shows plenty of slow but steady growth, with some better-than-expected numbers out of Europe:

(1) *PMIs*. As Debbie discusses below, the Eurozone C-PMI (56.8), M-PMI (57.0), and NM-PMI (56.2) all were strong in May ([Fig. 11](#)). In the US, the C-PMI (53.9) recovered some ground that was lost at the start of the year, led by the NM-PMI (54.0), while the M-PMI (52.5) fell for the fourth month in a row. Japan's M-PMI (52.0) edged down in May, but has exceeded 50.0 for the past nine months.

(2) *GDP*. The latest y/y growth rates for Q1 real GDP for the UK (2.1%), Eurozone (2.0), US (1.9), and Japan (1.6) suggest that the global economy is enjoying global synchronized growth that is between a boom and a bust ([Fig. 12](#)). There is more divergence within the Eurozone as follows: Spain (3.0%), Germany (1.7), France (0.8), and Italy (0.8) ([Fig. 13](#)).

(3) *German Ifo*. Below, Debbie also reviews May's German Ifo Business Confidence survey. The overall index soared to the highest reading in the history of the survey going back to 1991, led by the current situation index, which also rose to the highest on record ([Fig. 14](#))!

Global Economy II: New Normal Is the Norm. Debbie and I aren't seeing as much discussion about the New Normal recently as in the years following the Great Recession. We and other economists also have been spilling less ink on the concept of "secular stagnation." Could it be that we all have resigned ourselves to accept that economic growth is likely to remain relatively subdued compared to past growth? It seems so, with one important exception: President Donald Trump still believes that his policies will revive economic growth in the US from 2% per year back up to 3%-4%.

We wish him well. However, while his election seems to have revived lots of dormant animal spirits, Trump may be fighting the forces of demography. Mother Nature usually wins in this case. Fertility rates have plunged below the replacement rate almost everywhere around the world. People are living longer. Consequently, populations are aging. Melissa and I updated our analysis of these global demographic trends in the 11/3/16 [Morning Briefing](#).

The Census Bureau released a thorough [report](#) on this subject in March titled "An Aging World: 2015." The conclusion is as follows:

"When the global population reached 7 billion in 2012, 562 million (or 8.0 percent) were aged 65 and over. In 2015, 3 years later, the older population rose by 55 million and the proportion of the older population reached 8.5 percent of the total population. With the post World War II baby boom generation in the United States and Europe joining the older ranks in recent years and with the accelerated growth of older populations in Asia and Latin America, the next 10 years will witness an increase of about 236 million people aged 65 and older throughout the world. Thereafter, from 2025 to

2050, the older population is projected to almost double to 1.6 billion globally, whereas the total population will grow by just 34 percent over the same period.”

Our conclusion is that these demographic trends are weighing on global growth and will continue to do so. They may also be weighing on productivity, as older experienced workers retire and are replaced by younger inexperienced ones. This may also explain why wage inflation remains low, especially in the United States, because the latter are bound to get paid less than the former. This is the gist of a 3/7 [FRBSF Economic Letter](#) titled “What’s Up with Growth?”

To monitor these trends, we are tracking real GDP trend growth rates over 40-quarter periods (10 years) at annual rates for the US, Germany, Japan, and the UK ([Fig. 15](#)). The trend across all four has been for a noticeable slowing in secular growth.

CALENDARS

US. Wed: Existing Home Sales, 5.650mu, FHFA Price Index 0.5%, MBA Mortgage Applications, EIA Petroleum Status, FOMC Minutes, Kashkari, Kaplan. **Thurs:** Jobless Claims 237k, Advanced Merchandise Trade Balance -\$64.7b, Kansas City Fed Manufacturing Index 7, Weekly Consumer Comfort Index, EIA Natural Gas Report, Brainard, Kaplan. (Bloomberg estimates)

Global. Wed: Germany Gfk Consumer Confidence 10.2, Japan M-PMI Flash Estimate, BOC Rate Decision 0.50%, Draghi, Kuroda. **Thurs:** UK GDP 0.3%q/q/2.1%/y/y, Japan Headline, Core, and Core-Core CPI 0.4%/0.4%/0.0% Y/Y, OPEC Meeting. (DailyFX estimates)

US ECONOMIC INDICATORS

Regional M-PMIs ([link](#)): Three Fed districts so far have reported on manufacturing activity for May—New York, Philadelphia, and Richmond. We average the composite, orders, and employment measures as data become available. The composite index fell for the third month to 12.9 this month from 26.3 in February, which was the highest reading since July 2004. A pickup in the Philadelphia (to 38.8 from 22.0) region was more than offset by a sharp slowing in Richmond’s (1 from 20) to a near standstill, and the first contraction in New York’s (-1.0 from 5.2) since October. The new orders gauge slipped for the second month to 7.0 from 28.6 in March, which was the best reading since May 2004. Over the two-month period, Philadelphia’s gauge (25.4 from 38.6) slowed but remained at a high level, while Richmond’s (0 from 26) fell to zero and New York’s (-4.4 from 21.3) swung from expansion to contraction. Meanwhile, the employment measure slowed for the second month to 11.7, though held near April’s cyclical high of 15.4, which was the best hiring pace since May 2011. Manufacturers in both the Philadelphia (17.3 from 19.9) and New York (11.9 from 13.9) regions added to payrolls at a robust pace, while employment in the Richmond area slowed significantly, with its measure falling from a cyclical high of 20 in March to 6 this month.

GLOBAL ECONOMIC INDICATORS

US PMI Flash Estimate ([link](#)): Private-sector growth this month accelerated at its fastest pace in three months, after slowing steadily from January to March. Markit’s C-PMI rose for the second month to 53.9 after falling from a 14-month high of 55.8 in January to 53.0 in March, driven by the service sector. The NM-PMI climbed for the second month to a four-month high of 54.0 after falling the previous two months from 55.6 to 52.8. Meanwhile, the M-PMI declined for the fourth straight month from 55.0 in January to an eight-month low of 52.5. According to the report, service providers cited improving economic conditions and a greater willingness to spend among clients for the acceleration in business activity. Job growth improved after recording a near seven-year low in April, as renewed pressures on

operating capacity helped boost hirings this month. In contrast, the deceleration in manufacturing activity was widespread, with softer rates of growth in output, new orders, and employment.

Eurozone PMI Flash Estimates ([link](#)): Growth in the Eurozone this month continued to run at its fastest pace in six years, according to the flash estimate. The C-PMI remained at 56.8, which is the best pace since spring 2011; it was as low as 52.6 last September. Growth continued to pick up in the manufacturing sector, with the flash M-PMI (to 57.0 from 56.7) reaching a 73-month high; the NM-PMI (56.2 from 56.4) was little changed around April's six-year high. Overall new order growth slowed slightly from April's fast pace, led by a mild deceleration of new business into the service sector; manufacturing business grew at its best pace since April 2011, boosted by exports. Order backlogs across the two sectors posted the second-largest rise in six years. Jobs were added at the second-best pace since August 2007, with manufacturers hiring at the steepest rate in the survey's 20-year history. Job gains in the service sector matched April's pace, which was the best since early 2008. Price pressures continued to mount. By country, France (57.6 from 56.6) and Germany (57.3 from 56.7) C-PMIs showed the best growth since May 2011 and April 2001, respectively. Growth eased across the rest of the Eurozone, though remained close to a ten-year high.

Japan M-PMI Flash Estimate ([link](#)): Japan's manufacturing activity this month expanded at the slowest pace in six months, according to its flash estimate. The M-PMI fell for the second time in three months, dropping to 52.0, after having reached a three-year high of 53.3 in February. May's report shows a widespread slowdown in production, new orders, and employment, all expanding at the slowest pace since last November. The report noted a "wait-and-see" attitude among clients, as excess inventories and sharp rises in raw materials costs are cause for concern.

Germany Ifo Business Climate Index ([link](#)): German businesses confidence soared to a new record high this month. The Ifo business climate index advanced for the fourth month from 109.9 in January to 114.6—the highest in the history of the survey going back to 1991. Business assessment of the current situation continued to improve, with the measure climbing for the ninth straight month from 113.1 in August to 123.2 this month, also the highest in survey history. The expectations component is still trending higher, rising from 103.1 at the start of the year to 106.5 this month—the highest since February 2014. Ifo's expectations component correlates closely with German factory orders and production; the overall index tracks exports more closely. Recent Ifo data predict a continued acceleration in German activity.

Contact us by [email](#) or call 480-664-1333.

Ed Yardeni, President & Chief Investment Strategist, 516-972-7683
Debbie Johnson, Chief Economist, 480-664-1333
Joe Abbott, Chief Quantitative Strategist, 732-497-5306
Melissa Tagg, Director of Research Projects & Operations, 516-782-9967
Mali Quintana, Senior Economist, 480-664-1333
Jackie Doherty, Contributing Editor, 917-328-6848
Valerie de la Rue, Director of Institutional Sales, 516-277-2432
Mary Fanslau, Manager of Client Services, 480-664-1333
Sandy Cohan, Senior Editor & Webmaster, 570-775-6823

Copyright (c) Yardeni Research, Inc. Please read complete [copyright and hedge clause](#).