Yardeni Research, Inc.

MORNING BRIEFING
May 1, 2017

Hot Money

See the collection of the individual charts linked below.

(1) Definitive definitions of meltdown and melt-up. (2) The numbers game. (3) Trump's YUGE tax-cut plan cut from 3½ pages to 1 page. (4) Statutory vs effective corporate rates. (5) In my dreams: 15% tax rate on sole proprietorships. (6) Nervous about sky-high valuations, but even more nervous about missing more gains. (7) Equity ETF bubble continues to inflate. (8) Animal spirits a bit less spirited, but still high given softness in hard data. (9) Stocks' pep rally led by spirited actual and expected earnings. (10) Movie review: "The Lost City of Z" (- -).

US Strategy I: 'Yuge' Cut. In the past, the word "meltdown" was defined as "an accident in a nuclear reactor in which the fuel overheats and melts the reactor core or shielding." Since the 1987 stock market crash, the word has also been defined as "a disastrous event, especially a rapid fall in share prices." Of course, stressed humans can sometimes exhibit signs of a meltdown, a phenomenon that can coincide with a meltdown in one's stock portfolio.

The phrase "melt-up" is unambiguously associated with soaring stock prices. It is defined as "the informal term used to describe markets that experience a rapid rise in valuations due to a stampede of investors anxious not to miss out on a rising trend. Gains caused by melt-ups are usually followed quite quickly by meltdowns."

On March 7, Joe and I raised our odds of a melt-up from 30% to 40% and our odds of a subsequent meltdown from 10% to 20%. As a result, our odds of a Nirvana scenario (i.e., a leisurely bull market) dropped from 60% to 40%. We did so because we detected that the "animal spirits" unleashed by Trump's election were driving stock valuations higher. That might turn out to be perfectly okay if the Trump administration succeeds in slashing tax rates, particularly the corporate tax rate. Indeed, Joe and I responded to Trump's victory by raising our S&P 500 earnings forecast for this year from $129 per share to $142. That led us to raise our 2018 number from $136 to $150. (See *YRI S&P 500 Earnings Forecast*.)

We also raised our S&P 500 forecast from 2300-2400 to 2400-2500 for the end of this year. If the market gets to the top end of this range by mid-year, we'll conclude that it is a melt-up, though it might not necessarily be immediately followed by a meltdown if Trump delivers "YUGE" tax cuts. Consider the following:

(1) *Corporate tax rate.* Trump's "massive" tax plan was released last week. It wasn't a plan so much as a one-page outline of goals or discussion points or opening negotiating positions. It was actually just a sketchy update of a previous sketchy three-and-a-half-page outline. They both specifically mention lowering the corporate tax rate to 15% and providing a one-time tax break to stimulate repatriation.

When we raised our earnings and stock price targets, we assumed that the corporate tax rate would be cut significantly. The statutory rate is currently 35%. The effective rate during Q4-2016, according to the National Income and Product Accounts, for all corporations was 23.6% (*Fig. 1*). For the S&P 500, the effective rate was 27.5% during 2015 (*Fig. 2*). Trump is aiming to cut the statutory rate to 15%. That would also be the effective rate with all exemptions and deductions eliminated, as they obviously would have to be. So some companies will actually pay more in corporate taxes, while most would pay less.

If the corporate tax cut occurs later this year but isn't retroactive to 2017, then the impact would remain bullish, since the market shouldn't care much whether it is implemented this year or next year, in our opinion. If it doesn't happen at all, the Trump melt-up in stock prices would leave valuations at or near record highs, making the market vulnerable to a meltdown (*Fig. 3* and *Fig. 4*).

(2) *Repatriated earnings.* Contributing to the melt-up scenario is the possibility that Trump will succeed in lowering the tax rate on repatriated earnings, causing some large fraction of the estimated $2.6 trillion sitting overseas to come back to the US—making America's valuation multiples even greater if the funds are used by companies mostly to buy back their shares.

(3) *Proprietors' income.* Widely discussed but not mentioned in last week's one-pager was the idea that the 15% rate would apply to so-called "mom-and-pop" businesses, i.e., solely owned companies. The three-and-a-half-pager spelled it out as follows: "This lower tax rate cannot be for big business alone; it needs to help the small businesses that are the true engine of our economy. Right now, freelancers, sole proprietors, unincorporated small businesses and pass-through entities are taxed at the high personal income tax rates. This treatment stifles small businesses. It also stifles tax reform because efforts to reduce loopholes and deductions available to the very rich and special interests end up hitting small businesses and job creators as well. The Trump plan addresses this challenge head on with a new business income tax rate within the personal income tax code that matches the 15% corporate tax rate to help these businesses, entrepreneurs and freelancers grow and prosper."

That would be a YUGE tax cut for them from the 39.6% rate they pay, which is the top marginal tax rate on personal income. It isn't widely known that pre-tax proprietors' income, which is included in personal income, is almost as big as the pre-tax profits of corporations (*Fig. 5* and *Fig. 6*). The problem is that nearly everyone paying more than a 15% tax rate would scramble to reclassify their tax status as sole proprietors. There are ways to write rules that would limit who could pay the lower rate, but the tax code is clearly one of the deepest areas of the swamp and particularly hard to drain.

US Strategy II: Hot Lava. In recent meetings with several of our accounts, I frequently was asked whether our other accounts are bullish or bearish. I observed that they all are nervous about the extremely elevated level of valuations, but they are fully invested. That's because they are even more nervous about raising cash and missing a continuation of the bull market if Trump succeeds in cutting taxes and repatriating earnings. I pointed out that another reason for the melt-up is the surge in animal spirits visible in equity ETFs data reported last week for March:

(1) *Equity ETFs.* During March, equity ETFs issued $38 billion in net shares, implying a similar net inflow from investors. From November through March, $199 billion has poured into these funds, and $295 billion over the past 12 months (*Fig. 7* and *Fig. 8*).

(2) *Equity mutual funds.* Some of those animal spirits came out of equity mutual funds, which lost $4 billion during March, $12 billion since November, and $166 billion over the past year.

In our 4/3 *Morning Briefing*, we wrote: "So there you have it: The bull may be chasing its own tail. We know that image doesn't quite jibe with the bull charging ahead, but work with us here. The bull has been on steroids from share buybacks by corporate managers, who have been motivated by somewhat different and more bullish valuation parameters than those that motivate institutional investors, as we have discussed many times before. Most individual investors seemingly swore that they would never return to the stock market after it crashed in 2008 and early 2009. But time heals all wounds, and suddenly some of them may have turned belatedly bullish on stocks after Election Day. Add a buying panic of equity ETFs by individual investors to corporations' consistent buying of their own shares, and the result may very well be a melt-up."

US Economy I: Not As Hot. Flipping through our ***Animal Spirits*** chart publication, Debbie and I see that the post-election euphoria is easing off a bit but remains elevated. April's Consumer Optimism Index, which Debbie and I construct by averaging the Consumer Sentiment Index and the Consumer Confidence Index, remains near the previous month's cyclical high (*Fig. 9*). There was a drop in the average of the composite indexes of the six regional business surveys during April to 15.2 from a recent high of 21.8 during February (*Fig. 10*). The average of the new orders indexes fell to 16.0 in April from 24.9 during March. However, both averages remain high, and the average of the six employment indexes rose to 11.6, the highest since July 2014.

On the other hand, the latest batch of hard data is very soft. The Citigroup Economic Surprise Index fell to -4.8% on Friday, down from a recent high of 57.9% on March 15 (*Fig. 11*). As Debbie discusses below, real GDP rose just 0.7% (saar) during Q1, up only 1.9% y/y (*Fig. 12*). It's a bit better-looking excluding government spending with a 2.5% y/y gain. The Employment Cost Index remains subdued, rising 2.3% y/y through Q1, with the wages and salaries component up 2.6% and the benefits component up 1.9% (*Fig. 13*).

So why are all the stock market bulls in such high spirits? Earnings have recovered nicely from the profits recession that lasted from Q3-2015 through Q2-2016. Industry analysts are currently expecting S&P 500 operating profits to show a gain of 10.3% y/y during Q1, 11.0% during 2017, and 12.1% during 2018. As a result, their forward earnings estimate for the S&P 500 has been rising sharply this year into record-high territory with a current reading of $135.90 per share (*Fig. 14*). This measure tends to be a very good leading indicator of actual operating earnings over the coming four quarters as long as there is no recession over that period.

US Economy II: Taxing Matters. When Melissa and I learned on Friday, April 21 that President Trump would be releasing his tax reform plan on Wednesday, April 26, we along with many market participants were expecting more details. We all were disappointed at the lack of substance in the one-page outline. However, the breezy format and its vagueness also seem to suggest that the Trump administration is open for discussion on tax matters. The format also speaks to the administration's goal to streamline the tax code, effectively allowing Americans to be able to do their own taxes on one large index card.

Reading in between the bullet points, it seems that Trump already has moderated some of the aggressive tax agenda he floated on the campaign trail. (Here is the old plan from candidate Trump's website, and here is the new one.) To get a better understanding of last week's proposal, let's refer back to two relevant analyses that we previously reviewed. One is from the Tax Policy Center (TPC) titled: "An Analysis of Donald Trump's Revised Tax Plan" dated 10/18/16. The other is also from TPC and titled "An Analysis of the House GOP Tax Plan" dated 9/16/16, based on the House GOP's "A Better Way" tax plan, which was released on 6/24/16. Melissa prepared a one-page *table* comparing the TPC's estimates for the two plans.

The plans had lots of overlap. They also had a few significant differences. Trump's bottom line, according to the TPC's estimates, would add nearly $6 trillion to the federal debt over the next 10 years, while the House GOP's proposals would add less than half of that, or $2.5 trillion. Let's review how Trump's latest one-pager might change the math:

(1) *Corporate tax-rate cut!* Trump remains committed to his campaign promise to lower the federal statutory corporate income tax rate to 15%. The GOP had proposed a rate of 20%, which would cost

about $500 billion less over 10 years than Trump's rate according to the TPC's estimates. Worth noting also is that most Republicans continue to agree that the alternative minimum tax (AMT) should be repealed for businesses and individuals.

(2) *Territorial system*. The one-pager stated that business reform would include a "[t]erritorial tax system to level the playing field for American companies." That would mean that US companies would owe US tax only on what they earn domestically. As for profits that were earned overseas by US multinational corporations and were technically never brought back to the US, Trump will call for a low, one-time tax on the $2.6 trillion.

(3) *BAT off the table?* On January 16, Trump said that he didn't like the idea of a border adjustment tax (BAT) because it sounded complicated. The latest one-pager ignored the subject. Last Wednesday morning, Treasury Secretary Steve Mnuchin said, "We don't think it works in its current form, and we will have discussions with [House tax writers] about revisions." Using the GOP's approach, BAT would generate $1.2 trillion in tax receipts according to the TPC.

(4) *Individual rates tweaked*. TPC estimated around the same cost of $1.5 trillion for both initial plans to lower tax rates and reduce the tax brackets for individuals. But Trump tweaked the individual income tax rates from his original one-pager to the latest one. It reduced the rate for the lowest income tax bracket to 10% from 12% and increased it for the highest income tax bracket from 33% to 35%. The middle bracket stayed the same at 25%.

Importantly, Trump's latest one-pager didn't specify to what income brackets those rates would apply. So it's impossible to quantify the impact on Trump's bottom line. In any event, the tweaks could be an attempt to show that Trump is willing to do more for lower-income earners.

(5) *Deducting deductions*. Also excluded from the one-pager were details on exactly how itemized deductions would be reduced. We expected Trump would be more aggressive on them in order to offset some of the revenues lost from the individual tax rate reductions. Comparing the TPC estimates for Trump's original approach versus the GOP's yields a sizable $1.3 trillion difference.

The GOP plan sought to repeal virtually all itemized deductions except for the mortgage interest and charitable contribution. Trump initially proposed capping deductions rather than repealing most of them. According to the latest one-pager, Trump will seek to "protect the home ownership and charitable gift tax deductions." Does that mean that all other itemized deductions would go? The wording vaguely suggests so. In any event, the one-pager proposes to double the standard deduction, which would greatly reduce the need to itemize for many taxpayers.

By the way, Trump also happened to exclude any reference to repealing personal exemptions, a provision that was included in his campaign proposal and also in the GOP's plan. That's significant because the provision would offset the tax receipts lost from increasing the standard deduction. We will have to wait and see whether that's revisited. We will also have to wait and see whether interest deductions (for individuals with pass-through business income or corporations that opt to expense investments) are disallowed in the final version of the plan, since no indication was given in the one-pager.

(6) *Passing over pass-throughs*. Trump's latest one-pager is silent on the treatment of pass-through business income included on individual returns. On April 25, before it was released, the *WSJ* reported that White House officials said that Trump was planning to seek a top tax rate of 15% on owner-operated businesses. But again, that wasn't specifically confirmed in the latest official talking points.

Nevertheless, we suspect that pass-through business income is yet another area where the Trump administration might moderate its latest stance. The GOP plan had put a cap on the pass-through business income tax rate at 25% versus Trump's original 15% proposal. That had contributed to a $1.1 trillion difference in the cost to the government from the two plans.

Movie. "The Lost City of Z" (- -) (*link*) is a somewhat interesting story about a rather uninteresting British explorer obsessed with finding a lost city in the jungles of Amazonia during the early 1900s. He is a controversial member of the Royal Geographical Society, who is derided for believing in El Dorado, the mythical hidden city of immense wealth. The film is loosely based on the true-life drama of Col. Percival Fawcett, who disappeared during his last foray into the steamy forest on his ill-fated quest. It's a good movie to catch up on some Zs.

CALENDARS

US. Mon: Personal Income & Consumption 0.3%/0.1%, Headline & Core PCED 1.8%/1.7% y/y, ISM & Markit M-PMIs 56.5/52.8, Construction Spending 0.5%, Total & Domestic Motor Vehicle Sales 17.2mu/13.5mu. **Tues:** FOMC Begins. (Bloomberg estimates)

Global. Mon: Japan M-PMI, BOJ Minutes of March Meeting. **Tues:** Eurozone Unemployment Rate, Eurozone M-PMIs, UK M-PMI, China Markit-Caixin M-PMI 51.4, Japan Composite & NM-PMIs, RBA Rate Decision 1.50%, Kuroda. (DailyFX estimates)

STRATEGY INDICATORS

Global Stock Markets Performance (*link*): The US MSCI index rose 1.5% last week, ranking 28th of the 49 markets as 40 rose in US dollar terms—compared to 13th a week earlier, when it rose 0.9% as 22 markets moved higher. The AC World ex-US index outperformed the US MSCI, rising 2.4% compared to a 0.1% gain a week earlier. EMU was the best-performing region last week, with a gain of 5.3%, followed by EM Eastern Europe (4.3%), EMEA (3.6), and EAFE (3.0). EM Latin America was the week's worst-performing region, with a decline of 0.1%, followed by gains for BRIC (1.6) and EM Asia (1.9). Greece (11.3) was the best-performing country last week, followed by Austria (9.1), Poland (8.2), Denmark (6.2), and France (6.2). Chile (-3.5) was the worst performer, followed by Colombia (-2.7), Egypt (-2.2), Canada (-1.3), and Jordan (-1.2). In April, the US MSCI rose 1.0%, ranking 33/44 and behind the 1.9% gain for the AC World ex-US index as most regions rose. That compares to a flat performance in March, when it ranked 38/44 and was behind the 2.1% rise for the AC World ex-US in a month when all regions rose. The best regions in April: EMU (3.8), EMEA (3.0), EM Eastern Europe (2.6), EAFE (2.3), and EM Asia (2.1). April's worst-performing regions: EM Latin America (-0.4) and BRIC (1.8). The US MSCI is up 6.7% ytd, with its ranking down two slots w/w to 33/49, and continues to trail the AC World ex-US (9.3) on a ytd basis. Forty-two of the 49 markets are positive ytd, led by Argentina (38.3), Poland (31.3), Turkey (20.9), Austria (19.1), Spain (19.1), and India (18.9). The worst country performers ytd: Russia (-4.9), Jordan (-2.2), Pakistan (-1.6), Morocco (-0.9), Egypt (-0.3), and Canada (-0.3). The best-performing regions ytd: EM Asia (15.6), BRIC (13.4), EMU (12.4), EM Latin America (11.1). The worst-performing regions, albeit with gains: EM Eastern Europe (2.7), EMEA (4.0), and EAFE (8.9).

S&P 1500/500/400/600 Performance (*link*): All three indexes rose last week, LargeCap the most in 10 weeks, but no indexes have recorded a new record high in at least eight weeks. LargeCap's gain, of 1.5%, outpaced both SmallCap's (1.4%) and MidCap's (0.9) last week as 24 of the 33 sectors rose, down from 26 rising a week earlier. LargeCap and MidCap ended the week 0.5% and 1.5% below their March 1 record highs, respectively, and SmallCap ended 1.4% below its record high on February 21. Last week's top gainers: MidCap Health Care (3.6), SmallCap Health Care (3.2), LargeCap Tech (2.6), SmallCap Industrials (2.5), and LargeCap Health Care (2.4). Real Estate dominated last week's worst performers: SmallCap Real Estate (-2.5), MidCap Real Estate (-2.5), SmallCap Energy (-2.5), LargeCap Real Estate (-2.0), and LargeCap Telecom (-1.5). All three market indexes rose in April and after falling in March. LargeCap's gain, of 0.9%, was slightly ahead of SmallCap's (also 0.9) and MidCap's (0.8). Twenty-two of the 33 sectors advanced in April, up from 15 rising in March. April's best performers: SmallCap Telecom (9.4), MidCap Health Care (3.7), SmallCap Consumer Staples (3.5), and SmallCap Consumer Discretionary (2.9). April's laggards: SmallCap Energy (-12.6), MidCap Energy (-8.2), LargeCap Telecom (-4.4), MidCap Telecom (-4.3), and LargeCap Energy (-2.9). Twenty-six of the 33 sectors are positive ytd, with LargeCap (6.5) beating MidCap (4.3) and both easily ahead of SmallCap (1.6). The biggest sector gainers ytd: LargeCap Tech (14.9), MidCap Health Care (13.6), SmallCap Health Care (11.6), LargeCap Consumer Discretionary (10.6), LargeCap Health Care (9.5), and MidCap Tech (8.9). The worst performers ytd: SmallCap Energy (-24.4), MidCap Energy (-21.2), MidCap Telecom (-18.7), LargeCap Energy (-10.0), and LargeCap Telecom (-9.2).

S&P 500 Sectors and Industries Performance (*link*): Eight of the 11 sectors rose last week, and five outperformed the S&P 500's 1.5% gain. This compares to eight sectors rising a week earlier, when five outperformed the S&P 500's 0.8% gain. Tech was the best-performing sector for the week, with a gain of 2.6%, followed by Health Care (2.4%), Consumer Discretionary (2.0), Materials (1.8), and Financials (1.6). Real Estate was last week's worst performer, with a decline of 2.0%, followed by Telecom (-1.5), Utilities (-0.1), Energy (0.1), Consumer Staples (0.3), and Industrials (1.3). The S&P 500 rose 0.9% in April as seven sectors moved higher and five beat the index; that compares to three sectors rising and three beating the S&P 500's 0.1% decline in March. The leading sectors in April: Tech (2.4), Consumer Discretionary (2.4), Industrials (1.7), Health Care (1.5), and Materials (1.4). Telecom was the biggest laggard in March, with a drop of 4.4%, followed by Energy (-2.9), Financials (-1.0), Real Estate (0.0), Utilities (0.7), and Consumer Staples (0.8). So far in 2017, nine of the 11 sectors are higher, and five have outperformed the S&P 500's 6.5% gain. The best performers in 2017 to date: Tech (14.9), Consumer Discretionary (10.6), Health Care (9.5), Materials (6.7), and Consumer Staples (6.5). The six sectors underperforming the S&P 500: Energy (-10.0), Telecom (-9.2), Financials (1.1), Real Estate (2.7), Industrials (5.8), and Utilities (6.2).

Commodities Performance (*link*): Twelve of the 24 commodities we follow rose last week, up from four rising a week earlier. The week's best performers: Feeder Cattle (8.8%), Lean Hogs (8.3), Live Cattle (6.3), and Lead (5.1). Last week's laggards: Unleaded Gasoline (-5.9), Silver (-3.8), Heating Oil (-3.3), GasOil (-2.8), and Sugar (-2.3). April saw just nine of the 24 commodities climb, up from seven rising in March and led by Feeder Cattle (16.6), Live Cattle (11.9), Kansas Wheat (4.0), Natural Gas (2.7), and Cotton (2.0). April's laggards: Cocoa (-12.1), Unleaded Gasoline (-9.1), Nickel (-5.7), Silver (-5.4), and Zinc (-5.2). The best performers in 2017 so far: Feeder Cattle (23.7), Aluminum (12.8), Lead (12.1), Lean Hogs (11.9), and Cotton (11.6). The energy-related commodities are beginning to dominate this year's laggards to date again: Sugar (-17.3), Cocoa (-13.4), Heating Oil (-12.8), Natural Gas (-12.0), GasOil (-9.8), Brent Crude (-8.4), Crude Oil (-8.2), and Unleaded Gasoline (-7.3).

Assets Sorted by Spread w/ 200-dmas (*link*): Assets Sorted by Spread w/ 200-dmas (link): Spreads between prices and 200-day moving averages (200-dmas) rose last week for 13/24 commodities, 6/9 global stock indexes, and 24/33 US stock indexes compared to 4/24, 2/9, and 27/33 rising a week earlier, respectively. Fifteen commodities trade above their 200-dmas, down from 16 a week earlier as Crude Oil and Gasoil turned negative w/w and Kansas Wheat turned positive. Commodities' average spread improved to 1.2% from 0.3%. Among assets, Commodities walked away with three of the top five spots last week: Lean Hogs leads all commodities and all assets at 20.3% above its 200-dma, followed by Feeder Cattle (20.1) and Live Cattle (11.9). Feeder Cattle performed the best of all commodities and all assets last week, improving 9.5ppts..Cocoa (-23.5) and Sugar (-19.1) trade at the lowest of all commodities and all assets relative to their 200-dmas. Unleaded Gasoline was the worst performer of all commodities and all assets last week, tumbling 6.8ppts to 1.6%. The global indexes trade at an average of 6.1% above their 200-dmas, up from 5.1% above in the prior week. All nine of the global indexes trade above their 200-dmas, unchanged from a week earlier. Chile (12.2) leads the global indexes, followed by Germany (11.1)--which was the group's best performer last week, with a 2.9ppt advance. China (2.0) is trading at the lowest relative to its 200-dma of the global assets and also had the weakest performance of its country peers last week, falling 1.0ppts. The US indexes trade at an average of 4.0% above their 200-dmas, with 28 of the 33 sectors above, up from a 3.4% average a week earlier, when 28 sectors were above. The US stock indexes no longer dominate the top ten assets trading above their 200-dmas as they did in early March. LargeCap Tech now leads all US stock indexes at 12.0% above its 200-dma, followed by SmallCap Telecom (11.4), MidCap Health Care (10.7), and MidCap Tech (10.2). MidCap Health Care rose 3.5ppts w/w for the biggest gain among US stock indexes. MidCap Telecom trades 15.2% below its 200-dma, the lowest among the US stock indexes. SmallCap Real Estate fell 2.7ppts w/w to 2.7% for the worst performance of the US stock indexes.

S&P 500 Technical Indicators (*link*): The S&P 500 index remained in a Golden Cross last week for a 53rd week (after 17 weeks in a Death Cross). The index's 50-day moving average (50-dma) relative to its 200-dma fell for a fifth week after rising since early December. Its 50-dma was 5.3% above its 200-dma, down from 5.4% a week earlier and from a 34-month high of nearly 5.5% in early April. That's up from a six-month low of 2.0% in early December and a 52-month low of -4.5% in March 2016. The S&P 500's 50-dma moved higher for a 24th week as the index closed above its 50-dma for the first time in three weeks. The index had been below its 50-dma for two straight weeks for the first time since the November election. The S&P 500 improved to 0.9% above its rising 50-dma from 0.1% below a week earlier and a 23-week low of -1.0% in mid-April. That's down from a 38-week high of 4.8% above its rising 50-dma on December 13 and compares to a 52-month high of 6.2% in March 2016 and a five-month low of -7.8% in January 2016. The S&P 500 continued its early November bounce off its 200-dma last week and rose to 6.3% above its rising 200-dma from 4.9% a week earlier and mid-April's 19-week low of 4.2%. That's down from a 38-month high of 9.4% on March 1. The 50-dma and 200-dma both rose together for a 22nd week, but at a slower pace than in recent weeks.

S&P 500 Sectors Technical Indicators (*link*): Seven of the 11 sectors improved relative to their 50-dmas last week, and eight improved relative to their 200-dmas. Seven of the 11 sectors trade above their 50-day moving averages (50-dmas), up from six a week earlier and from three in mid-April, which was the lowest since the election. Health Care and Materials rose back above their 50-dmas in the latest week, and Real Estate moved below. Energy remained below for a 15th straight week, and Financials and Telecom were below for a sixth week. All 11 sectors were above their 50-dmas during mid-January, and all 11 were below the week before the election, for the first time since December 11, 2015. Nine of the 11 sectors were above their 200-dmas last week, unchanged from a week earlier. Energy remained below its 200-dma for a tenth week and Telecom for a sixth. Nine sectors are in a Golden Cross, with 50-dmas higher than their 200-dmas, unchanged from a week earlier and leaving Energy and Telecom still out of the club. All 11 had been in a Golden Cross during a 21-week streak that ended October 24, the longest such stretch since October 2014. Eight of the 11 sectors have rising 50-dmas, unchanged from a week earlier, as Financials' 50-dma fell for a fourth week; Energy's dropped for a 12th week and Telecom's for an 11th. However, just seven sectors have rising 200-dmas, unchanged from a week earlier, as Utilities started rising and Health Care began falling. Real Estate's 200-dma fell for a seventh week and Telecom's for a fifth.

US ECONOMIC INDICATORS

GDP (*link*): Real GDP expanded at the slowest pace in three years last quarter, impeded by the slowest growth in consumer spending (0.3%, saar) since 2009. The economy grew only 0.7% (saar) during Q1, slowing from 2.1% and 3.5% the prior two quarters. The slowdown in real consumer spending was led by only the second decline in durable goods consumption (-2.5) in six years; growth rates in nondurable goods (to 1.5 from 3.3) and services (0.4 from 2.4) consumption both eased, with the latter's the weakest since Q1-2013. Real capital spending was a big bright spot in the report, accelerating 9.4%—the best growth since Q4-2013—boosted by a record increase in mining exploration shafts & wells (a category that includes oil structures). Spending on overall structures soared 22.1% (saar), a rate not seen in three years, while investment in equipment (9.1) posted its best pace since Q3-2015. Real investment in intellectual property products advanced 2.0% (saar), faster than Q4's 1.2% but considerably below Q3's 9.0% pace. Real residential investment swelled 13.7%, following a 9.6% advance during Q4, which followed two quarters of decline. The trade gap narrowed slightly as exports (5.8) grew faster than imports (4.1) last quarter. These positive contributions were partly offset by decreases in private inventory investment (to $10.3 billion from $49.6 billion) and declines of 1.9% and 1.6%, respectively, in federal and state & local government spending.

Contributions to GDP Growth (*link*): Real capital spending replaced consumer spending as the number-one contributor to real GDP last quarter; business inventories and government spending were both drags on growth. (1) Nonresidential fixed investment (1.12ppt) contributed positively to GDP growth last quarter as spending on structures (0.55), equipment (0.49), and intellectual property products (0.08) all added to growth. (2) Residential investment (0.50) was a positive contributor for the second consecutive quarter after subtracting from growth the prior two quarters. (3) Trade (0.07) was a small contributor to Q1 growth after being the only detractor from Q4 growth; exports added 0.68ppt, while imports subtracted -0.61ppt. (4) Real consumer spending accounted for only 0.23ppt of real GDP growth during Q1 versus 2.40ppts during Q4. Goods consumption (0.02) was basically neutral—as a negative contribution from durable goods (-0.19) spending nearly wiped away a positive contribution from nondurable's (0.22); services consumption contributed 0.21ppt. (5) Inventory investment (-0.93) was the biggest drag on growth during Q1, all nonfarm (-0.97). (6) Real government expenditures (-0.30) subtracted from GDP growth for the first time in three quarters, with both state & local (-0.17) and federal (0.13) government spending in the red.

Durable Goods Orders & Shipments (*link*): March's report showed capital spending continued to climb. Nondefense capital goods shipments ex aircraft (used in calculating GDP) rose for the fourth time in five months, jumping 1.5% in the two months through March. The comparable orders measure (a proxy for future business investment) rose for the sixth straight month, though was little changed around recent highs the past couple of months. These core shipments accelerated 7.3% (saar) during Q1, the best quarterly performance since Q3-2014. Real core orders expanded 5.9% (saar) during Q1, also the strongest quarter since Q3-2014, though not far from the 5.3% pace recorded during the final quarter of 2016. Headline durable goods orders began 2017 on an up note, advancing 0.7% in March after gains of 2.3% in February and 2.4% in January. Excluding transportation, orders slipped for the first time since last June, by 0.2%, after an eight-month gain of 5.4%.

Regional M-PMIs (*link*): Five Fed districts now have reported on manufacturing activity for April—New York, Philadelphia, Dallas, Richmond, and Kansas City—and show growth in the sector slowed for the second month from February's fast pace. We average the composite, orders, and employment measures as data become available. The composite index slipped to 14.2 this month from 21.6 last month and 23.5 in February—which was the highest reading since summer 2004. The Philadelphia (to 22.0 from 43.3), New York (5.2 from 18.7), and Dallas (16.8 from 24.5) measures all slowed the past two months after improving dramatically in February, though the latter's was little changed in April. The Richmond (20 from 22) and Kansas City (7 from 20) indexes fell from their cyclical highs in March; it was the first decline in eight months for the former and in five months for the latter. The new orders gauge slipped to 16.0 this month from 25.5 last month, which was the best reading in the history of this measure going back to 2004. New orders in the Philadelphia (27.4), Kansas City (8), and New York

(7.0) regions all grew at the slowest pace in four months, though Philly's held near March's cyclical high. Meanwhile, Dallas' orders (11.5 from 9.5) expanded at a slightly faster pace than March; Richmond's was unchanged at March's seven-year high of 26. The employment measure eased a bit, slipping to 11.3 after improving the prior thee months from -1.0 to 13.5, which was the best hiring pace since May 2011. Manufacturers in the Philadelphia (19.9) and New York (13.9) regions are showing a pickup in hiring, adding to payrolls at the fastest pace since May 2011 and March 2015, respectively. The Dallas (8.5) and Kansas City (9) gauges show a steady pace of hiring, holding around recent highs. Meanwhile, hiring in Richmond slowed dramatically, with its index falling from 20 to 5 this month.

Employment Cost Index (*link*): Gains in yearly compensation costs remained subdued last quarter, though have been accelerating recently. Private industry compensation increased 2.3% y/y during Q1, in the middle of the 2.2%-2.4% range the past four quarters. The rate for wages & salaries was 2.6% y/y, at the top of the 2.3%-2.6% range over the past year; the yearly rate for benefits' costs (1.9% y/y) was below 2.0% for the eighth straight quarter, but was the highest rate in two years. For Q1, compensation costs rose 0.8%, up from 0.5% the previous two quarters and the highest in 11 quarters. Wages & salaries accelerated 0.9%, the largest quarterly gain in a decade, while benefits costs rose at a two year high of 0.6%.

Consumer Sentiment (*link*): Consumer sentiment in April held around January's cyclical high. Richard Curtin (the director of the survey) noted, "Consumers are more optimistic about the economy in general, especially independents and Republicans. I would expect spending to come back after a first-quarter slowdown." The Consumer Sentiment Index climbed for the second month to 97.0 (below the mid-month reading of 98.0), after falling from a cyclical high of 98.5 in January to 96.3 in February—which was the first decline in sentiment since the election. The present situation index dipped to 112.7 (below its preliminary estimate of 115.2) after reaching a cyclical high of 113.2 in March; it's up 8.5 points from its recent low of 104.2 in September. The expectations component climbed to a three-month high of 87.0 from 86.5 the prior two months; it's holding just below January's two-year high of 90.3.

GLOBAL ECONOMIC INDICATORS

Eurozone Economic Sentiment Indicators (*link*): The Economic Sentiment Index (ESI) for both the Eurozone (+1.6 points to 109.6) and the EU (+1.4 points to 110.6) rose markedly in April to their highest levels since August and September of 2007, respectively. This month, four of the five largest Eurozone economies posted gains of 1.0 point or more: Germany (+1.8 points to 111.0), Italy (+1.4 to 107.0), France (+1.2 to 106.3), and Spain (+1.0 to 107.9); the Netherlands' ESI climbed 0.8 point to 109.0. At the sector level, construction confidence (+3.7 to -6.2), services confidence (+1.4 to 14.1), and industry confidence (+1.3 to 2.5) all climbed to new cyclical highs. Meanwhile, consumer confidence (+1.4 to -3.6) and retail trade confidence (+1.4 to 3.2) remained in volatile flat trends—the former at the top of its range, near its cyclical high.

Eurozone CPI Flash Estimate (*link*): April's CPI rate is expected to be 1.9% y/y, according to the flash estimate, bouncing back to a level in line with the ECB goal. In March, the rate slowed to 1.5% after accelerating 2.0% in February—surpassing the ECB inflation target of just under 2.0% for the first time in four years. Meanwhile, the core inflation rate—which excludes food, alcohol & tobacco—was the highest in almost four years, climbing 1.2% y/y from 0.7% in March, which was near its record low of 0.6% in spring 2015. Of the main components, prices for energy (to 7.5% from 7.4% y/y) and services (1.8 from 1.0) accelerated from March, the former only slightly, while gains in prices for food, alcohol & tobacco (1.5 from 1.8) slowed; the non-energy industrial goods inflation rate was unchanged at 0.3% y/y.

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