MORNING BRIEFING
October 26, 2017

Birth Dearth

See the collection of the individual charts linked below.

(1) P&G not sure why sales are weak. (2) Bringing up fewer babies. (3) Fewer diapers and less shampoo. (4) Pulp nonfiction. (5) Abe wants Japanese to have more babies. (6) Abe also wants to beef up military. (7) Another sales tax hike is on the way. (8) Better Japanese GDP growth led by exports. (9) Inflation remains MIA. (10) In Japan, 75 is the new 65. (11) Will daycare revive Japan?

Staples: Cry Babies. It's not often you hear executives admit not knowing why their products aren't selling well, but that's what P&G's CFO Jon Moeller did in the company's earnings conference call last week. P&G reported 1% y/y increase in organic sales for its fiscal Q1-2018, down from 3% growth a year ago. When asked what was driving US sales deceleration, Moeller said, "We've been unable to put our finger on [it]." No change in consumption levels has been noticed, no move to private labels. Intrigued, I asked Jackie to investigate. Here's what she discovered:

(1) *Blaming babies*. P&G is not the only consumer products company having a tough time. At Kimberly-Clark, a 1% y/y increase in Q3 sales volume was offset by a 1% decline in net price, leaving organic sales flat y/y. At Kimberly-Clark, however, executives blamed the babies—or rather the lack thereof. The US birthrate was down about 3% y/y in Q1, and South Korea's birthrate was down 7%-9% ytd. The decline in the birthrate is expected to be an ongoing problem. "Those babies aren't born this year, and they won't be in the category next year or the year after that. So category weakness is certainly there in a couple of big markets," said Kimberly's CEO Thomas Falk during the conference call.

Indeed, a look at quarterly data from the Centers for Disease Control and Prevention shows that in Q1 the general fertility rate—the total number of births per 1,000 women aged 15-44—was 57.7. That's down 3.8% from Q1-2016, when the fertility rate was 60.0, and it's the only time the quarterly figure has dropped below 60.0 looking back to Q1-2015.

Baby care, which includes diapers and wipes, kicked in 14% of P&G's $65.1 billion of total sales in FY-2017. Kimberly-Clark doesn't break out its product lines as finely; however, it reports that its personal care unit—which includes diapers, wipes, feminine products, and incontinence care products—contributed $9.0 billion, or about half of the company's sales last year.

(2) *Diaper wars*. While there may be fewer babies in the US, the amount of competition doesn't appear to have declined at all. And many of the players are competing on price, according to our admittedly unscientific research on the matter. We searched on Amazon for the best-selling size 5 diapers, and the top brand was P&G's low-cost brand Luvs. Its 140-count box was selling for $22.06, or 16 cents a diaper. P&G's premium (and presumably higher-margin) Pampers size 5 box is the 12th most popular seller, but its 152-count box retails for $52.39, or 35 cents a diaper.

At Target.com, the best-selling size 5 diaper is the Target brand, Up & Up. Its 128-diaper box retails for $21.99, 17 cents a diaper. P&G's Pampers is the third product listed, and its 92-diaper box sells for $31.49, 34 cents a diaper. Kimberly's Huggies brand 96-diaper box sells for $24.29, and it's the 13th product listed. There were also two brands, Honest Company (59 cents per diaper) and Seventh

Generation (42 cents per diaper), pitched to buyers who want a more natural alternative or have kids with allergies.

(3) *Dry cleaning for hair*. The other theory P&G discounted was that consumers were spending more on services, like their mobile phone service, and therefore spending less on staples. "I want a cell phone, so I am not going to wash my hair; it doesn't make a lot of sense to me," said Moeller.

Again, we turned to Amazon for answers. Amazon listed the top three shampoo sellers: Nizoral, an anti-dandruff shampoo owned by Johnson & Johnson; PURA D'OR, an anti-hair loss shampoo that's independently owned; and Art Naturals Organic Moroccan Argan Oil shampoo, which also appears to be independent. Maybe people haven't stopped buying shampoos, just the major brands' offerings—choosing products pitched as more natural that come from boutique manufacturers instead?

In fifth place on Amazon's best-selling shampoos list was Batiste Dry Shampoo, owned by Church & Dwight. For the gentlemen in the audience, dry shampoo is a product used to "clean" dry hair instead of washing hair with shampoo. It has grown in popularity as women have gotten busier and as pin-straight hair has gained in popularity. Women don't want to get their hair blown out by a professional every day, so they'll do it on a Monday and use dry shampoo for a few days to make the blowout last. (Once hair is washed, it won't stay perfectly straight anymore.) The trend started a few years ago. Perhaps it suggests that women are indeed washing their hair less often?

P&G has offerings in the dry shampoo category. However, the top sellers on Amazon's list are Church & Dwight's Batiste and independent brands Amika and Not Your Mother's.

(4) *Costlier pulp*. Another interesting takeaway from both conference calls was the mention of higher commodity prices. P&G's Moeller explained: "Following the natural disasters we're now estimating about a $300 million profit hit from higher commodity costs. We knew we'd see higher pulp cost going into year, these costs have continued to increase beyond initial forecast ranges. Ethylene, propylene, kerosene, and the polyethylene and polypropylene resins have increased recently primarily as a result of the hurricanes in the Gulf."

Kimberly-Clark also called out higher prices for pulp, which is used in tissues, paper towels, and diapers. The company's CFO Maria Henry reported: "Commodities were $115 million drag in the quarter, and we now expect full year inflation will be slightly above our previous estimate of $200 million to $300 million. This outlook includes somewhat higher cost estimates for pulp and polymer resin."

(5) *By the numbers*. As the year enters its final stretch, the Consumer Staples sector finds itself far behind in the derby race among S&P 500 sectors. Here's where things stand ytd as of Tuesday's close: Tech (30.8%), Health Care (20.6), Materials (18.3), Financials (15.1), Industrials (14.9), S&P 500 (14.8), Utilities (12.9), Consumer Discretionary (11.8), Real Estate (5.1), Consumer Staples (3.9), Energy (-9.7), and Telecom Services (-13.7) (*Fig. 1*).

The Staples sector is expected to see revenues jump 3.4% and earnings gain 7.4% over the next 12 months (*Fig. 2*). The pace of earnings growth has decelerated over the years, yet the sector's forward P/E has climbed steadily to 19.2 since bottoming at 11.2 in March 2009 (*Fig. 3*). As a result, the sector's P/E-to-growth ratio has jumped to 2.4, up from 1.5-2.0 in years past (*Fig. 4*).

Some industries in the Staples sector have managed to buck the trend and turn in strong stock performances so far this year. The S&P 500 Distillers & Vintners is up 35.4% ytd, and Personal Products, which is solely Estee Lauder, has gained 23.9%. Hypermarkets & Super Centers jumped 18.6% thanks to the gains in Walmart stock, and Soft Drinks (9.2%) and Tobacco (7.1) enjoyed smaller gains.

P&G and Kimberly are both members of the S&P Household Products industry, which has added 4.0% ytd (*Fig. 5*). The industry is expected to grow revenues by 3.1% and earnings by 6.7% over the next 12 months (*Fig. 6*). Even though the industry is growing earnings at a much slower pace than the S&P 500, Household Products has a much higher forward P/E, 21.7, than does the broader index.

The above-market P/E is one of the reasons that we haven't favored the sector. Another has been the Food Retail segment, which is down 20.7% ytd due to the decline in Kroger shares (*Fig. 7*). We thought the industry would face tough times as Amazon grew more aggressive and as German discounters expanded in the US. Indeed, forward earnings estimates have fallen precipitously, and are now expected to decline 3.1% (*Fig. 8*). In just the past year, the industry's forward P/E has compressed to 10.6 from 14.7 (*Fig. 9*).

Times may remain tough. P&G's Moeller noted that the sales you see in stores aren't being funded by his company: "[R]etailers, particularly in the US, are choosing to make investments in price as they compete with each other. And that shows up in the scanner data as a promotion, but it's not one that's been funded by the manufacturer."

Japan: Abe Wants Babies. Riding the tide of the strongest economic growth in two years, Prime Minister Shinzo Abe and his ruling Liberal Democratic Party won a resounding victory in Sunday's election in Japan.

Stocks rallied to the highest level in 21 years and posted 16 straight sessions of gains, on renewed hopes that the economic reforms first introduced in 2013 to halt three decades of deflation and known as "Abenomics" will continue. Hallmarks of Abenomics include an easy monetary policy to achieve 2.0% inflation, fiscal stimulus, and growth initiatives to promote private investment.

This fresh victory emboldens Abe to move forward with his plan to amend Japan's 70-year-old post-war Constitution to include language legitimizing the Japanese military known as the "Self-Defense Forces," an action that requires a two-thirds majority of both houses of the Diet, Japan's parliament, a 10/22 article in the *NYT* explained. Majority approval from the public also is required. With North Korea launching missiles and trading threats of war with the US, Abe hopes his plan will resonate with voters, though pacifism runs deep in the culture and opinion polls show the public is divided on the issue, according to a 10/23 report on the Wire. As currently written, the Constitution renounces war and prohibits an army. He is likely to use the occasion of a visit by President Trump on November 5 to bolster his case. Indeed, Trump and Abe agreed to work together to ratchet up the pressure on North Korea, as we noted yesterday.

Topping Abe's agenda, too, is the need to tackle Japan's biggest problem: an aging population and low birth rate (*Fig. 10* and *Fig. 11*). Abe plans to increase the sales tax in 2019 to 10% from 8.0%, taking advantage of improving consumer confidence, and use a portion of the proceeds to fund child care and free college tuition (*Fig. 12*). The rest will be used to reduce national debt, more than twice Japan's \$4.94 trillion GDP, ranking it highest among advanced nations in terms of debt-to-GDP (*Fig. 13*). The tax hike has been postponed numerous times in the past on concerns that the economy was too weak; yet this time Abe has vowed to push ahead, barring a financial crisis on a par with 2008. A tax hike in 2014 to 8.0% from 5.0% threw the country into recession.

The victory was all the sweeter for Abe coming on the heels of two domestic scandals that drove his approval ratings below 30%, a level that has proven fatal to past prime ministers, according to a 7/25 report in *The Guardian.* Abe's decision to call for snap elections a year early caught the opposition off guard and poorly prepared.

The MSCI Japan Index is up 16.8% in dollars and 14.2% in yen ytd through Tuesday, with much of those gains coming since September (*Fig. 14*). With the market valued at a forward P/E of 14.3 and earnings growth estimated at 16.8% this year and 5.7% next year and estimates rising, there's room for more gains. I asked Sandra to have a look at the data that has driven the stock market enthusiasm and underpins Abe's win. Here is what she reports:

(1) *Quickening GDP growth.* The economy grew at the fastest pace in two years in Q2, the sixth straight quarter of economic growth, on strengthening domestic demand. On an annualized basis, real GDP expanded by 2.5% in the April-June period, the biggest jump since Q1 2015 (*Fig. 15*). The growth rate was revised significantly downward from a preliminary estimate of 4.0%, following a slowdown in private non-residential investment, but continues to represent a healthy clip.

Domestic demand rose a powerful 3.8% (saar) from the previous quarter. Household consumption, representing 60% of GDP, increased by 3.4% (saar) q/q, and capital spending accelerated by 7.1% (saar) q/q.

There has also been a pickup in industrial production, up 2.0% in August, as machinery orders rebounded in July and August (*Fig. 16*).

(2) *Exports surging.* Exports expanded at the fastest pace in nearly four years in August, rising 18.0% y/y, well ahead of forecasts of 14.3% growth and the biggest increase since November 2013, according to a 9/19 Bloomberg piece. It was the ninth monthly increase. Autos and semiconductors led the growth, which were helped by a weaker yen. Exports to China, Japan's biggest trading partner, rose 25.8% y/y. US shipments increased 21.8% y/y, and those to the European Union rose 13.7% y/y.

(3) *Imports rising.* Strengthening domestic demand—mainly for coal, liquefied natural gas, and crude oil—lifted imports 15.2% y/y in August versus a projected 11.6%. It was the eighth month in a row of increases.

(4) *Inflation dormant.* Still, for all Japan's progress, inflation remains near zero, far from Abe's 2.0% target. Despite a tight labor market, wages remain stagnant, as firms are reluctant to boost salaries on concerns that they won't be able to pass price hikes onto customers (*Fig. 17*). To break the logjam, the government now is considering expanding tax incentives to encourage companies to raise wages, according to a 10/24 *NYT* story.

(5) *Demographic implosion.* It's been called "the ticking time bomb" threatening Japan and its economy: Japan's population is now expected to shrink by close to a third by 2065, to 88 million from 127 million in 2015, according to figures updated in April by the health ministry and detailed in a 4/11 story in *The Telegraph.* By 2065, people aged 65 and older will make up 38% of the population compared with 10% for those aged 14 and under. That suggests there will be only 1.2 working people to support every person over 65 by 2065, compared with 2.1 in 2015. This has serious negative implications for the country's healthcare system, pension system, tax revenue, and labor productivity.

Japan just broke its own record for the number of people living beyond 100 years: There are 67,824 centenarians, according to data released in September by the health ministry, compared with 339 in 1971, notes a 9/15 report in Business Insider.

The government is focusing on providing more child care in an effort to attract more women into the workforce as a way of stemming the declining population growth. And it's redefining "elderly" to age 75 and up from 65 as a way of keeping more people in the workforce. Robotics and artificial intelligence are also a priority.

One sure way to address the problem is to allow large-scale immigration. Health ministry forecasters reckon that if the number of foreigners were to increase by 250,000 every year, it would add significantly to the population and raise the total to 100.7 million by 2065. Yet Japan is a homogeneous society that has historically been reluctant to embrace immigration, which remains an unpopular subject. Quietly, though, Japan's resident foreign worker population has risen 40% since 2013, according to a 3/28 report by the Migration Policy Institute.

The sun will come out tomorrow in the Land of the Rising Sun. But for Japanese stocks to keep rising over the long term, Abe and his ruling party will have to find the answer to the population problem.

CALENDARS

US. Thurs: Advance Merchandise Trade Balance -$69.3b, Jobless Claims 235k, Kansas City Fed Manufacturing Index, Pending Home Sales 0.4%, Weekly Consumer Comfort Index, EIA Natural Gas Report, Kashkari. **Fri:** Real GDP, PCE, and Price Deflator 2.5%/2.3%/1.6%, Consumer Sentiment Index 101.0, Baker-Hughes Rig Count. (Bloomberg estimates)

Global. Thurs: Germany Gfk Consumer Confidence 10.8, Japan CPI Headline, Core, and Core-Core 0.7%/0.7%/0.2% y/y, ECB Rate Decision 0.00%, ECB Marginal Lending Facility & Deposit Facility Rates 0.25%/-0.40%. **Fri:** Germany Retail Sales 3.2%y/y. (DailyFX estimates)

STRATEGY INDICATORS

Stock Market Sentiment Indicators (*link*): Our Bull/Bear Ratio (BBR) climbed to 4.13 this week—the highest reading since April 2015. Bullish sentiment posted its third straight reading of 60.0% or above, increasing to 62.3% this week—near its high for the year of 63.1% recorded in late February. It's up 15.2ppts the past six weeks. Most of the move to greater bullishness came from the correction camp, with the correction count down 10.1ppts over the six-week period to 22.6%—the lowest reading since reaching its low for the year of 20.4% during the final week of February. Bearish sentiment barely budged for the second week, edging down to 15.1% and reversing last week's uptick from 15.1% to 15.2%. Accordingly, bearish sentiment remains below the narrow 16.5%-18.3% range shown most of this year; it was at 20.2% six weeks ago. The AAII Ratio slipped to 57.6% last week after rebounding from 52.0% to 59.7% the week before. Bullish sentiment fell from 39.8% to 37.9% during the week, while bearish sentiment rose a percentage point to 27.9%.

AC World ex-US MSCI (*link*): This index is up 20.3% ytd in dollar terms after rising 1.7% in 2016. In local-currency terms, the index has risen a lower 13.8% ytd compared to its 4.1% gain for all of 2016. Local-currency forward revenues improved 0.3% m/m, and has risen 6.5% from a five-year low in March 2016 to near its highest level since November 2015. Forward revenues has been more stable longer term and is down just 4.5% from its October 2014 record high. Local-currency forward earnings has performed better, with a 0.7% rise m/m and a 19.7% rise from its six-year low in March 2016 to its highest level since October 2008, but remains 6.9% below its September 2008 record. Revenues are expected to rise 7.3% in 2017 and 4.8% in 2018 following a 1.0% decline in 2016, and earnings are expected to rise 16.6% (2017) and 8.9% (2018) after rising 3.8% (2016). Analysts are forecasting STRG of 5.3%, down from a seven-year high of 6.8% in March and up from a cyclical low of 2.3% in March 2016. Their STEG forecast of 10.2% is down from a four-year high of 14.1% in March, but up from their 6.3% forecast in January 2016, which was the lowest in seven years. The implied profit margin is expected to rise to 7.7% in 2017 from 7.1% in 2016 before improving to 8.0% in 2018. The forward profit margin forecast of 7.9% is at a six-year high now. NERI was positive in October for the first time in three months as it improved to 0.5% from -0.4%, but is down from a 76-month high of 2.7% in May. That compares to a 51-month low of -11.3% in March 2016. The P/E rose to a 15-month high of 14.5 in October from 14.2 in September, which compares to a 16-month low of 12.4 in February 2016 and a six-year high of 15.3 in April 2015. The index's 11% discount to the World P/E has improved from a record-low 13% discount in early March.

EMU MSCI (*link*): The EMU's MSCI price index has gained 24.7% ytd in dollar terms after falling 1.2% in 2016. In euro terms, the price index is up a lower 11.9% ytd following a 1.8% gain for all of 2016. Euro-based forward revenues improved 0.4% m/m and has improved 3.1% from its six-year low in May 2016 to 1.2% below its cyclical high (August 2015) and 7.8% from its record high (September 2008). Euro-based forward earnings had stalled from 2011 to 2016—but is now 7.3% above its prior cyclical high in September 2015 to near its highest level since September 2011. It remains 22.6% below its record high (January 2008) after rising 0.6% m/m, but has improved 14.7% from its 23-month low in June 2016. Analysts expect revenues to rise 5.1% and 3.2% in 2017 and 2018, respectively, after falling 1.8% in 2016, but think earnings will rise 10.6% in 2017 and 8.9% in 2018 following a 4.9% increase in 2016. Forecasted STRG of 3.5% is down from a six-year high of 5.0% in April, but up from 2.0% in May 2016. Forecasted STEG of 9.2% is down from a 78-month high of 21.0% in February, which compares to a seven-year low of 5.7% in April 2016. STEG had been higher than LTEG (currently 12.8%) from July 2016 to May 2017, but is trailing now. The forward profit margin has improved 1.8ppts to a six-year high of 7.5% from a cyclical bottom of 6.2% in May 2013. The implied profit margin is expected to improve to 7.1% in 2017 from 6.8% in 2016 before rising another 0.4ppt to 7.5% in 2018. NERI was negative in October for a third month following eight straight positive readings, but improved to -3.9% from a 14-month low of -4.2% in September. Those readings are down from a 131-month high of 8.1% in May, which compares to a 24-month low of -13.2% in April 2016. The P/E of 14.6 is up from 14.3 in September, which compares to a 13-year high of 16.4 in April 2015 and a 30-month low of 12.2 in February 2016. That represents a 10% discount to the World MSCI's P/E now, up from a record-low 25% discount during 2011. But the current reading is still well below the 1% premium during April 2015—the post-euro-inception record high.

Emerging Markets MSCI (*link*): The EM MSCI price index is up 29.1% ytd in US dollar terms after rising 8.6% in 2016. In local-currency terms, EM has gained a lower 25.2% ytd compared to a 7.1% gain in 2016. Local-currency forward revenues rose 1.7% m/m and is up 7.5% from a four-year low in June 2016 to 9.5% below its November 2014 record. Local-currency forward earnings has fared substantially better, rising 0.9% m/m to a second straight monthly record high for the first time since January 2014; it has improved 25.5% from April 2016's six-year low. Revenues are expected to rise 10.0% in 2017 and 8.2% in 2018 following a 2.3% gain in 2016, leading to earnings gains of 21.5% (2017) and 12.2% (2018) following a 7.7% rise in 2016. Forecasted STRG of 8.5% is back on an uptrend since early 2016, but is down from a four-year high of 9.6% in late January. STEG of 13.4% is down from 13.9% a month ago, and is below LTEG (21.7%) again. The implied profit margin is expected to improve to 6.9% in 2017 from 6.3% last year before edging up to 7.2% in 2018. The forward profit margin of 7.1% is the highest since January 2013 and up from a record low of 6.0% in February 2016, but remains more than 3ppts below its 10.3% record high in December 2007. NERI has been negative for 80 months, but barely so as it improved m/m to -0.03% from -0.7%. That compares to an 83-month low of -10.2% in March 2016. Emerging Markets' valuation has been more stable recently than that of the rest of the world. The P/E was up to 12.8 from 12.5 in September. That's the highest P/E since January 2010 and compares to a 17-month low of 10.2 in August 2015. The index is trading at a 21% discount to the World MSCI P/E, up from a 10-year-low 30% discount in August 2016.

MSCI World & Region Net Earnings Revisions (*link*): Analysts' recent earnings revisions through October point toward improving optimism about profits across the world. All regions improved m/m during October, but most remain below their multi-year highs in May. The AC World MSCI's NERI was positive for a ninth month and for the first time since June 2011, improving 0.8ppt to 1.5% from 0.7% in September, but is down from a 74-month high of 3.3% in May. The AC World Ex-US was positive for the first time in three months as it improved 0.9ppt to 0.5%, which compares to a 76-month high of 2.6% in May. Emerging Markets' NERI was negative for an 80th straight month, but barely so as EM Asia turned slightly positive for the first time in 76 months and EM Latin America was negative for a 15th month. EM Eastern Europe was the strongest, rising 2.4ppts to 3.1% from 0.7%, and has been positive in 12 of the past 14 months; Europe was negative for a third month following 10 positive readings; EAFE was positive for an 11th month; EMU was negative for a third straight month following eight positive readings. October's scores among the regional MSCIs: United States (3.7% in October, up from 3.4% in September), EM Eastern Europe (3.1, 0.7), AC World (1.5, 0.7), EAFE (0.8, 0.1), AC World ex-US (0.5, -0.4), EM Asia (0.03, -0.4), Emerging Markets (-0.02, -0.8), Europe (-1.8, 13-month low of -2.4), EM Latin America (-3.3, -5.0), Europe ex-UK (-3.4, 12-month low of -4.2), and EMU (-3.9, 14-month low of -4.2).

MSCI Countries Net Earnings Revisions (*link*): NERI was positive for 16/44 MSCI countries in October. That's up from 12/44 in September, which was the lowest since July 2016, and compares to 29/44 in June, which was the highest since June 2010. NERI improved m/m in October for 30/44 countries compared to 21/44 rising in September, but that's still down from 32/44 in May, which had been the most since June 2016. China's NERI was at a 94-month high in October, followed by Poland's, at a 92-month high, and Switzerland's (88-month high). On the flip side, Greece's was at a 21-month low, followed by those of Netherlands (15), Sweden (15), Ireland (13), and Spain (13). The 19-month positive NERI streak for Hungary is the best, followed by those of Austria (17), China (14), Hong Kong (12), Poland (12), Turkey (12), Italy (11), and Japan (11). Brazil's NERI has been negative for 88 straight months, followed by the negative streaks for South Africa (41), India (36), New Zealand (17), Thailand (13), Mexico (12), and Pakistan (11). NERI turned positive in October for four countries: Argentina, Canada, Norway, and Russia. Hungary's NERI has been the strongest recently, with positive readings in 28 of the past 29 months.

S&P 500 Q3 Earnings Season Monitor (*link*): With 33% of S&P 500 companies finished reporting Q3-2017 earnings and revenue results through midday Wednesday, their percentage surprise and y/y growth results are mostly weaker compared to the same point during the Q2 earnings season, but more companies have reported positive y/y revenue and earnings growth. Of the 165 companies in the S&P 500 that have reported, 73% exceeded industry analysts' earnings estimates, by an average of 3.0%; they have averaged a y/y earnings gain of 8.7%. At the same point during the Q2-2017 reporting period, a higher percentage of S&P 500 companies (78%) had beaten consensus earnings estimates by a higher 6.7%, and earnings were up a higher 12.5% y/y. On the revenue side, 71% beat sales estimates so far, with results coming in 1.1% above forecast and 4.8% higher than a year earlier. At this point in the Q2 season, a higher 73% had exceeded revenue forecasts by a higher 1.4%, but sales rose a lower 3.4% y/y. Q3 earnings results are higher for 76% of companies, vs 68% at the same point in Q2, and revenues are higher for 84%, vs 81% a quarter ago. Although these figures will change markedly as more Q3-2017 results are reported in the coming weeks, particularly for the insurers, the early results are encouraging. Q3-2017 should mark the fifth straight quarter of positive y/y earnings growth despite the negative impact of the three hurricanes. However, growth is likely to fall back into the low single digits following double-digit percentage growth in Q1 and Q2, which was the first double-digit growth seen since Q3-2011.

US ECONOMIC INDICATORS

Durable Goods Orders & Shipments (*link*): Both core capital goods orders and shipments in September climbed to their highest readings since 2015. Nondefense capital goods orders ex aircraft (a proxy for future business investment) has only posted one decline this year, up 1.3% m/m and 6.5% ytd, to its highest reading since January 2015. The comparable shipments measure (used in calculating GDP) climbed for the tenth time in 11 months—up 0.7% m/m and 7.2% over the period—to its highest reading since September 2015. Both core capital goods orders and shipments expanded at double-digit rates of 11.1% and 10.2% (saar), respectively, during Q3—the strongest quarterly performance for both since Q3-2014. Headline durable goods orders rebounded 4.2% during the two months ending September—after tumbling 6.8% in July and soaring 6.5% in June—which were driven by wide swings in aircraft orders. Excluding transportation, orders advanced for the seventh time in nine months, by 0.7% in September and 5.0% ytd, to its highest level since summer 2014.

New Home Sales (*link*): September new home sales soared to the highest level since October 2007, with the number of properties in which construction hasn't yet started (236,000) the highest in over a decade. Sales skyrocketed 18.9% to 667,000 units (saar), after falling the previous two months from 619,000 units to 561,000 units, with sales in the South jumping 25.8%. (New home sales are tabulated when contracts are signed, making new home sales a timelier barometer of the residential market than existing home sales.) The government was not able to estimate what impact, if any, the hurricanes had on the data, though sales outside the hurricane-affected areas in the Northeast (33.3%) and Midwest (10.6) also posted double-digit gains during the month; sales in the West edged slightly higher. In September, there were 279,000 new homes on the market, with the supply of homes at the current sales rate dropping to five months. Meanwhile, homebuilders' confidence for October returned to the high 60s, rebounding 4 points to 68, following September's hurricane-related fall. NAHB's Chairman Granger MacDonald noted the rebound in confidence from the "initial shock of the hurricanes", but warned "that builders need to be mindful of long-term repercussions from the storms, such as intensified material price increases and labor shortages."

GLOBAL ECONOMIC INDICATORS

Germany Ifo Business Climate Index (*link*): German business confidence blew past forecasts this month, rebounding to a new record high. The Ifo business climate index jumped to 116.7—the highest in the history of the survey, going back to 1991—after sinking from 116.0 to 115.3 in September. (The consensus forecast was for a further decline in business confidence.) The expectations and current situation components both moved higher, though the former led October's gain. The expectations component soared from 107.5 to 109.1—its best reading since December 2010. Business assessment of the current situation recovered from 123.7 to 124.8, just shy of July's record high of 125.7. Ifo's expectations component correlates closely with German factory orders and production; the overall index tracks exports more closely. Recent Ifo data continue to support an 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