MORNING BRIEFING
November 29, 2017

Barreling Along

See the pdf and the collection of the individual charts linked below.

(1) Full throttle, pedal to the metal, and escape velocity. (2) Truck tonnage index at record high. (3) Intramodal railcar loadings at record high. (4) Home shopping may be boosting truck traffic. (5) Animal spirits remain highly spirited. (6) Consumer optimism survey suggests jobless rate could soon fall below 4.0%! (7) Regional business surveys are upbeat. (8) Outlook for new orders looking good. (9) German business index hits a new high, which is bullish for German stocks. (10) Movie review: "Three Billboards" (+).

US Economy I: Full Throttle. The US economy is exceeding the speed limit. That limit was around 2% y/y growth in real GDP from the second half of 2010 through Q3 of this year (*Fig. 1*). However, on a q/q-saar basis, real GDP growth rose from 1.2% during Q1 to 3.1% during Q2, and 3.0% during Q3. The Atlanta Fed's GDPNow is currently tracking real GDP growth at an annualized rate of 3.4% during Q4.

Meanwhile, the US transportation indicators that Debbie and I monitor show that the trucking industry has the pedal to the metal and railcars are barreling down the tracks. It's heady stuff:

(1) *Trucking.* The ATA truck tonnage index jumped to a record high during October (*Fig. 2*). It is up a whopping 9.9% y/y, the best growth rate since December 2013 (*Fig. 3*). This index is volatile on a m/m basis. Smoothing it with a three-month moving average shows that it has tended to be a good leading indicator for real business inventories (*Fig. 4*). So the recent strength in trucking may reflect lots of optimism on the part of retailers about the holiday selling season. That's a reasonable expectation given that the unemployment rate fell to a cyclical low of 4.1% during October.

Of course, the bricks-and-mortar retailers are fighting back against the online retailers by slashing prices and providing lots of incentives for consumers to come to shop at the malls. Meanwhile, the rising share of online retail sales might be increasing the demand for trucking services to cart merchandise to fulfillment centers and from those centers to the home shopping crowd.

(2) *Railroads.* The three-month moving average of the trucking index is highly correlated with the 26-week moving average of railcar loadings of intermodal containers (*Fig. 5*). The latter is confirming the strength in the former. Intermodal railcar loadings has been chugging along into record-high territory in recent weeks.

US Economy II: Happy Days. The optimism reflected in the transportation indexes is confirmed by November's consumer optimism surveys, which Debbie discusses below. She also discusses November's regional business surveys, which are also extremely upbeat. Love him or hate him, there's no denying that one year after President Donald Trump was elected, the economy's animal spirits remain in high spirits. Here are a few of the highlights:

(1) *Consumer surveys.* The Consumer Sentiment Index (CSI) dipped this month, following a strong gain during October (*Fig. 6*). Debbie and I are bigger fans of the Consumer Confidence Index (CCI), which continued to soar this month to the highest reading since November 2000 (*Fig. 7*).

The CCI has been more sensitive to labor market conditions than the CSI. We particularly like the CCI series showing whether respondents agree that "jobs are hard to get," or "available," or "plentiful" (*Fig. 8*). During November, only 16.9% of them said that jobs are hard to get, the lowest since August 2001. This series is highly correlated with the unemployment rate (*Fig. 9*). The jobless rate fell to a cyclical low of 4.1% during October. It might have fallen below 4.0% this month! The CCI was up for all age groups during November, though it soared among those who are 55 years old and older (*Fig. 10*).

(2) *Business surveys.* Debbie and I monitor the five monthly business surveys conducted by the Federal Reserve Banks of Dallas, Kansas City, New York, Philadelphia, and Richmond. We focus on the averages of their overall business conditions indexes, their new orders indexes, and their employment indexes (*Fig. 11*). The overall index dipped this month but remained near previous cyclical highs. The composite orders index jumped back near the cyclical high at the beginning of the year. The employment index edged down, but remained very high.

Helping to boost real GDP growth this year has been the recovery in core nondefense capital goods orders (*Fig. 12*). This series had been depressed by the global recession in the energy sector. It fell 14.9% from a September 2014 peak to a May 2016 trough. Since then, it is up 10.5% through October. The regional composite index for new orders suggests that business spending on durable goods probably stayed strong in November.

German Economy: No Speed Limit on Autobahn. At the same time that the US economy's cruise speed is showing signs of improving, so is Germany's. The country's IFO business confidence index soared to yet another record high during November (*Fig. 13*). Needless to say, this is a bullish development for the Germany MSCI stock price index, which is up 9.1% ytd and 19.3% y/y (in euros). It certainly looks like a global synchronized boom and a global bull market in stocks based on the performances of the US and German economies and stock markets.

Both economies have clearly achieved the "escape velocities" long awaited by the Fed and the ECB. This means that the Fed will continue Fed Chair Janet Yellen's policy of gradually normalizing monetary policy under incoming Fed Chairman Jerome Powell. It also means that the ECB may need to reconsider the continuation of its ultra-easy monetary policy sooner rather than later.

So far, the amazing miracle is that inflation has remained amazingly subdued. Debbie and I aren't that amazed, since we've been predicting this would be the case. Nevertheless, we are impressed. Strong growth with low inflation justify currently high valuation multiples, but risk triggering a stock market meltup.

Movie. "Three Billboards" (+) (*link)* is a quirky movie with quirky characters. It's a bit like a Coen Brothers movie, and even stars Frances McDormand, who is married to one of the brothers and has appeared in lots of their movies. Like a Coen-made movie, this one takes place in a rural town with lots of goofy characters caught in tenuous positions of committing, hiding, or dealing with a murder in their midst. Also playing an interesting part is Woody Harrelson.

CALENDARS

US. Wed: Real GDP & PCE 3.3%/2.5%, GDP Price Deflator 2.2%, Corporate Profits, Pending Home Sales 1.0%, MBA Mortgage Applications, EIA Petroleum Status Report, Beige Book, Yellen, Dudley. **Thurs:** Personal Income & Consumption 0.3%/0.3%, Headline & Core PCED 1.5%/1.4% y/y, Jobless Claims 240k, Chicago PMI 63.5, Weekly Consumer Comfort Index, EIA Natural Gas Report, Kaplan. (*Wall Street Journal* estimates)

Global. Wed: Eurozone Economic Confidence 114.6, Germany CPI 0.3%m/m/1.7%y/y, France GDP 0.5%q/q/2.2%y/y, Japan Industrial Production 1.8%m/m/7.2%y/y, Bundesbank Presents 2017 Financial Stability Report. **Thurs:** Eurozone CPI Headline & Core Flash Estimate 1.6%/1.0% y/y, Eurozone Unemployment Rate 8.9%, Germany Unemployment Change & Unemployment Claims Rate -10k/5.6%, Germany Retail Sales 0.3%m/m/2.8%y/y, Japan CPI Headline, Core, and Core-Core 0.2%/0.8%/0.2% y/y, Japan Jobless Rate 2.8%, Japan Household Spending -0.3% y/y, Japan Housing Starts 950k, China M-PMI 51.5. (DailyFX estimates)

STRATEGY INDICATORS

S&P 500/400/600 Forward Earnings (*link*): Forward earnings rose to yet another record high last week for all three indexes. SmallCap ticked up w/w after falling for the first time in 13 weeks. LargeCap's forward earnings was higher for an 18th straight week, and MidCap's for a 14th week. Momentum remains strong as the yearly change in forward earnings is up from six-year lows in early 2016, and should remain strong if tax reform occurs. In the latest week, LargeCap's forward earnings rose to a 70-month high of 10.3% y/y from 10.2%, which compares to a six-year low of -1.8% in October 2015; MidCap's rose to a 71-month high of 15.4% from 15.3%, which compares to a six-year low of -1.3% in December 2015; and SmallCap's improved to a 16-week high of 11.4% from 10.9%, which compares to a 39-month high of 13.0% in mid-July and a six-year low of 0.3% in December 2015. LargeCap's consensus growth rates expected for 2017 have remained strong throughout this year instead of falling. Furthermore, the growth rates for 2018 should remain strong for all three indexes if the corporate tax rate changes sooner rather than later. Here are the latest consensus earnings growth rates for 2017 and 2018: LargeCap 11.3% and 11.3%, MidCap 10.4% and 14.2%, and SmallCap 5.5% and 20.2%.

S&P 500/400/600 Forward Valuation (*link*): Forward P/E ratios rose for all three indexes last week. LargeCap's weekly forward P/E rose to a four-week high of 18.0 from 17.9, matching late October's reading, which was the highest level since March 2004. It's up from a 15-month low of 14.9 in January 2016 and the post-Lehman-meltdown P/E of 9.3 in October 2008, but remains well below the tech bubble's record high of 25.7 in July 1999. SMidCap's P/Es had stalled for most of 2017 following the post-election meltup, but has been rising again recently. MidCap's forward P/E rose to a 30-week high of 18.3 from 18.2, and is slightly higher than LargeCap's P/E again after being below during August and September for only the second time since 2009. MidCap's P/E remains below its 15-year high of 19.2 in late February and the record high of 20.6 in January 2002, but is up from a three-year low of 15.0 in January 2016. SmallCap's rose to 20.0 from 19.7, which compares to a 15-year high of 20.5 in December 2016 when Energy's earnings were depressed. That's up from a three-year low of 15.5 in February 2016, and just 0.9ppt below SmallCap's record-high P/E of 20.9 in April 2002. Prices remain near record highs for all three indexes, but their "E"s still remain low as analysts await the passage of legislative changes to the tax rate and its positive impact on corporate earnings. Looking at their daily forward price/sales (P/S) ratios, valuations last week were mostly steady for the three indexes: LargeCap's P/S of 1.99 is down from a record high of 2.02 in early November, MidCap's 1.28 is down from a record high of 1.39 in early March, and SmallCap's 1.01 is down from 1.08 in early March and its record high of 1.17 in November 2013.

S&P 500 Sectors Quarterly Earnings Outlook (*link*): With the Q3 earnings season nearly 98% complete, Q4 earnings revisions activity has slowed considerably. The S&P 500's Q4-2017 EPS forecast dropped a penny w/w to $34.72, and is down only 0.7% from $34.98 at the end of Q3. The $34.72 estimate represents a forecasted pro forma earnings gain for Q4-2017 of 11.5%, unchanged from a week earlier and compared to Q3-2017's blended estimate/actual of 8.3%, Q2's 12.3%, and Q1's 15.3%, which was the strongest growth since Q3-2011 owing mostly to easier comps for Energy. Since the end of Q3, Q4 estimates are higher for three sectors, lower for seven, and steady for one.

Energy's Q4 forecast has risen 15.6% followed by these sectors: Utilities (up 3.1%), Tech (2.1), and Telecom (0.0). Industrials' Q4-2017 forecast has fallen 9.3% for the worst decline, and is followed by: Materials (-8.3), Real Estate (-5.9), Consumer Discretionary (-5.1), Health Care (-2.2), Financials (-1.9), and Consumer Staples (-1.1). The S&P 500's Q4-2017 forecasted earnings gain of 11.5% y/y would be its sixth straight gain after four declines. Nine of the 11 sectors are expected to record positive y/y earnings growth in Q4-2017, and four are expected to beat the S&P 500's forecasted y/y earnings gain of 11.5%. That's because analysts expect Energy to report another large profit jump in Q4 relative to very low earnings a year ago. That's better than Q3-2017, with eight sectors expected to rise y/y, but down from Q2-2017, when all 11 sectors rose y/y for the first time since Q3-2011. The latest forecasted Q4-2017 earnings growth rates vs. their blended Q3-2017 growth rates: Energy (120.9% in Q4 vs. 161.0% in Q3), Materials (25.6, 7.0), Tech (14.3, 23.9), Financials (14.1, -7.3), S&P 500 (11.5, 8.3), Utilities (9.3, -4.6), Consumer Staples (8.5, 4.5), Consumer Discretionary (5.8, 3.8), Health Care (4.6, 8.3), Industrials (4.0, 3.1), Real Estate (-1.1, 3.8), and Telecom (-2.1, -2.8). On an ex-Energy basis, S&P 500 earnings are expected to rise 9.3% y/y in Q4, up from 6.0% in Q3, which is the slowest growth since ex-Energy earnings rose just 2.2% in Q2-2016. That compares to gains of 9.6% in Q2 and 11.0% in Q1.

US ECONOMIC INDICATORS

Consumer Confidence (*link*): "Consumers are entering the holiday season in very high spirits and foresee the economy expanding at a healthy pace into the early months of 2018," according to the Conference Board's latest survey. Consumer confidence in November increased for the fifth month from 117.3 in June to 129.5 this month—the highest reading since November 2000! The expectations component drove this month's gain, jumping 4.3 points to 113.3—its highest reading since September 2000, boosted primarily by optimism of further improvements in the labor market. The six-month jobs' outlook showed the percentage expecting more jobs (22.6%) continued to surpass those expecting fewer jobs (11.0), with the spread improving for the third month to 11.6ppts—the widest since the January 1984! Consumers' assessment of the present situation improved moderately, from 152.0 to 153.9 this month, the highest reading since June 2001. Consumers' view of the current job market remains at a 16-year high—with those saying jobs are plentiful (37.1%) at the highest percentage since June 2001, and those saying jobs are hard to get (16.9) at the lowest since August 2001.

Durable Goods Orders & Shipments (*link*): Both core capital goods shipments and orders in October remained at high levels, though the latter took a minor step back. Nondefense capital goods orders ex aircraft (a proxy for future business investment) edged down 0.5% after rising the prior three months by a total of 4.8% to its highest reading since September 2014; October's decline was only the second this year. The comparable shipments measure (used in calculating GDP) climbed for the 11th time in 12 months—up 0.4% m/m and 8.3% y/y—to its highest reading since December 2014. Both core capital goods orders and shipments expanded at double-digit rates—of 13.8% and 12.5% (saar), respectively—during three months ending October, based on the three-month average. Headline durable goods orders slipped 1.2% after rebounding 4.2% during the two months ending September. Excluding transportation, orders advanced for the eighth time in 10 months, by 0.4% in October and 6.0% ytd, to its highest level since July 2008.

Regional M-PMIs (*link*): All five Fed districts so far have reported on manufacturing activity for this month—New York, Philadelphia, Kansas City, Richmond, and Dallas—and they show growth in the sector remains steadfast. We average the composite, orders, and employment measures as data become available. The composite index fell this month, though remains at a very high level, slipping from 24.1 (which was the highest since July 2004) to 21.5 this month—averaging 22.2 the past three months. The Richmond (to 30 from 12) region posted its fastest growth in the history of its survey going back to November 1993, while the remaining four regions—Philadelphia (to 22.7 from 27.9), New York

(19.4 from 30.2), Dallas (19.4 from 27.6), and Kansas City (16 from 23)—showed growth eased, though remained robust. The new orders gauge accelerated for the fourth month from 11.9 in July to 23.8 this month, near March's cyclical high of 24.5, led by a record pace in Richmond (35 from 17) billings. The Philly (21.4 from 19.6) and New York (20.7 from 18.0) regions showed a slight pickup in orders' growth this month, while Kansas City (22 from 27) and Dallas (20.0 from 24.8) billings slowed from high levels. The employment measure fell from 18.8 to 14.9 this month as manufacturers in the Philadelphia (22.6 from 30.6), New York (11.5 from 15.6), Kansas City (16 from 21), and Dallas (6.3 from 16.7) regions continued to add to payrolls at a healthy pace, just not as fast as last month. Meanwhile, Richmond (18 from 10) manufacturers matched their fastest pace this year.

Existing Home Sales (*link*): Existing home sales in October rebounded to their best pace since July, but remained below a year ago for the second straight month due to supply shortages. Existing home sales—tabulated when a purchase contract closes—posted its first back-to-back gain this year, jumping 2.0% in October, after a 0.4% uptick in September, to a four-month high of 5.48mu (saar). Single-family sales climbed 2.7% over the two-month period to 4.87mu (saar), while multi-family sales continued its up-and-down pattern, rising 1.7% last month to 610,000 units (saar), after a 1.6% fall in September. According to NAR's chief economist, "While the housing market gained a little more momentum last month, sales are still below year ago levels because low inventory is limiting choices for prospective buyers and keeping price growth elevated." Total and single-family sales were 0.9% and 1.0% below a year ago, while multi-family sales were flat. The number of existing single-family homes on the market at the end of October fell to 1.60mu—10.1% below a year ago—recording y/y declines for the 29th consecutive month; unsold inventory was at 3.9 months' supply. (Note: According to the NAR, the residual effects from Hurricanes Harvey and Irma are still seen in parts of Texas and Florida. However, sales should completely bounce back to their pre-storm levels by the end of the year, as demand for buying in these areas was strong before the storms.)

New Home Sales (*link*): October new home sales soared to the highest level in 10 years after activity was temporarily restrained by hurricanes Harvey and Irma. Sales climbed 6.2% to 685,000 units (saar)—the highest since October 2007—following a 14.2% surge in September. (New home sales are tabulated when contracts are signed, making new home sales a timelier barometer of the residential market than existing home sales.) In October, there were 282,000 new homes on the market, with the supply of homes at the current sales rate dropping to 4.9 months. Meanwhile, the NAHB's homebuilders' optimism index for November reached an eight-month high of 70—the second-highest reading (next to March's 71) since the housing bubble of 2005. The current sales component rose 2 points to 77, while the gauge for future sales dipped slightly to 77—both lofty levels; buyer traffic climbed 2 points to 50.

GLOBAL ECONOMIC INDICATORS

Germany Ifo Business Climate Index (*link*): "The German economy is on track for a boom," according to Ifo's Clemens Fuest. The Ifo business climate index remains on a steep uptrend, climbing to 117.5 this month—the highest in the history of the survey, going back to 1991. The expectations component unexpectedly rose from 109.2 to 111.0 this month—the most optimistic since November 2010. Meanwhile, the present situation component ticked down from 124.8 to 124.4, not far from July's cyclical 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 a further acceleration in German activity.

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