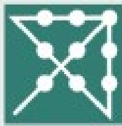
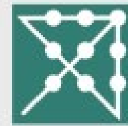
 Yardeni Research 

MORNING BRIEFING
October 31, 2022

Bear Bottoms

Check out the accompanying chart collection.

Executive Summary: The bear market has clawed 30% out of stock valuations, returning the S&P 500's forward P/E to its historical average of 15. But October 12 may have marked the bear's bottom. If GDP and inflation perform as we expect and the Fed does what everyone expects, that bottom should hold. … We think the stock market has discounted a soft-landing scenario (to which we give a 60% subjective probability) but is nervous about a hard landing (40%). … Also: The MegaCap-8 stocks' outsized influence over their resident indexes has been diminished. … Movie review: "All Quiet on the Western Front" (+ + +).

YRI Monday Webcast. Join Dr. Ed's live Q&A webinar on Mondays at 11 a.m. EST. You will receive an email with the link to the webinar one hour before showtime. Replays of the Monday webinars are available *here*.

Strategy I: So Far, So Good. The S&P 500 rose 4.0% last week and 2.5% just on Friday to close at 3901. It is up 9.1% since it bottomed at 3577 on a closing basis on October 12. If that was the bear market's bottom, then it lasted 282 days (since the January 3 record high) and trimmed the index by 25.4% (*Fig. 1* and *Fig. 2*).

The index is now 18.7% below its January 3 record high of 4796. It jumped easily above its 50-day moving average on Friday. It is likely to retest its 200-day moving average, which was 4098 on Friday. Joe and I are still expecting it to revisit its August 16 high of 4305 by the end of this year. The Santa Claus rally might have started already, and Santa's sled is likely to be supercharged by the congressional midterm elections, as we first discussed in our *October 19* *Morning Briefing* and explored further on *October 24*.

The bear market in the S&P 500 has been entirely attributable to a 30% plunge in the S&P 500's forward P/E from 21.5 on January 3 to 15.1 on October 12 (*Fig. 3*). We continue to believe, as we've been writing, that the 15.0 level should hold as long as the economic outlook is for a soft landing rather than a hard one. The forward earnings of the S&P 500 increased 4.6% since the first week of January through the third week of October (*Fig. 4*). This weekly proxy for earnings peaked during the June 23 week, falling 1.8% through the October 20 week. (FYI: "Forward P/E" is the multiple using "forward earnings," which is the

time-weighted average of analysts' consensus operating earnings-per-share estimates for this year and next.)

Admittedly, during the summer, we had thought that the June 16 low of 3666 was the bottom of the current bear market in the S&P 500. In our opinion, that level has provided some good support during the most recent selloff, which was triggered by more hawkish talk by Fed officials.

Fortunately, Fed officials haven't been talking this week because their blackout period started on October 22 prior to their FOMC meeting on Tuesday and Wednesday of this coming week.

However, we will hear from Fed Chair Jerome Powell at his press conference on Wednesday. He should be a bit less hawkish than he was following the 75bps rate hike on September 21. At that point, he said this (emphasis ours): "[T]oday … we've just moved, I think, probably, into the very lowest level of what might be restrictive, and, certainly, in my view and the view of the Committee, there's a way to go." That certainly freaked out the bond and stock markets until recently.

On Wednesday, the FOMC is expected to announce another 75bps hike to a range of 3.75%-4.00%. That would make the fourth consecutive hike of that magnitude. Powell will have to acknowledge that the federal funds rate is now further into restrictive territory and will be even more so come the FOMC's December meeting, when the rate is widely expected to be raised by 50bps to 75bps.

Keep in mind that September's *FOMC Summary of Economic Projections* showed that the committee's median forecast for the federal funds rate was 4.4% by the end of this year and 4.6% by the end of next year. The committee believed that would be restrictive enough to lower the PCED inflation rate from 5.4% this year to 2.8% next year.

Strategy II: Has the S&P 500 Discounted a Hard Landing? One of our accounts recently asked us to assess the extent to which the stock market has discounted a garden-variety recession. That's an interesting question. Joe and I have been thinking and writing about this question all year.

Our current assessment is that the market has discounted a rolling recession, a.k.a. a "soft landing," "growth recession," or "mid-cycle slowdown." We give this soft-landing scenario a 60% subjective probability; the remaining 40% we assign to the hard-landing one. We think

investors have discounted the former but remain nervous about the latter.

The stock market has been working on forming a bottom since September, finding support around the June 16 low of 3666, as we noted above. That bottom should hold if real GDP growth, on a y/y basis, hovers between 0.5% and 1.5% through the first half of next year and then recovers to more normal growth during the second half of next year, as discussed below. In addition, it should hold if the Fed delivers two more hikes in the federal funds rate by the end of this year (as is widely expected) and then pauses rate-hiking during the first few months of next year. Furthermore, the bottom should hold if inflation shows clear signs of moderating in coming months, as we continue to expect.

Let's examine the extent to which the stock market is discounting a soft landing or a hard landing. Since we think that it has mostly discounted the former, we reckon that the latter could send the S&P 500 down by another 10%-15% from its most recent bottom on October 14. Consider the following:

(1) *LEI.* The Index of Leading Economic Indicators (LEI) peaked at a record high during February and is down 2.9% through September (*Fig. 5*). As we've previously observed, the LEI has a good record of calling recessions. It peaked on average by 13.7 months before the previous seven business cycle peaks (prior to the pandemic). So the next business cycle peak is likely to occur next year around March or April and will be followed by the next recession, according to the LEI model. That could happen if the Fed is forced to resume tightening after a brief pause because inflation remains persistently high. That's not our most likely scenario.

(2) *S&P 500.* The S&P 500 is one of the 10 components of the LEI (*Fig. 6*). According to the S&P 500, the latest recession should have started already around May of this year. While the LEI is only available since January 1959, the S&P 500 is available starting in 1928. Since the end of WWII, the S&P 500 has peaked on average by five months before the past 11 business cycle peaks (prior to the pandemic).

By the way, with only one exception, the S&P 500 has bottomed near the ends of previous recessions, not before they'd even started! The one exception was the Tech Wreck bear market during the early 2000s, when the S&P 500 didn't bottom until 11 months after the recession back then had ended.

The current recession is the most widely anticipated downturn that hasn't happened—so far. If it does happen, there is likely to be more downside for earnings and the valuation

multiple, sending the S&P 500 still lower. Again, that's not our most likely scenario.

(3) *History.* The current bear market started on January 3 of this year. Let's say that it lasted 282 days, ending on October 12, when the S&P 500 was down 25.4%. That compares favorably with the average bear market: Since 1929, the prior 22 bear markets (including the brief 2020 pandemic selloff) lasted 341 days on average, with the S&P 500 falling 36.6% on average (*Table 1*). Those were mostly hard landings, of course.

(4) *Forward earnings.* As noted above, S&P 500 forward earnings rose to a record high during the June 23 week and has been relatively flat below that peak since then. The S&P 500 is determined by its forward earnings multiplied by its forward P/E. The former is determined by industry analysts, while the latter is determined by investors. So far, forward earnings has been moving sideways, rather than diving as it invariably does during recessions as analysts—who rarely see recessions coming—scramble to slash their earnings estimates.

During the October 20 week, industry analysts did continue to shave their earnings-per-share estimates for the next five quarters from Q4-2022 through Q4-2023 (*Fig. 7* and *Fig. 8*). Nevertheless, their annual estimate for 2023 at $238.78 remained above their forward earnings of $235.58. Very soon, at the start of the new year, forward earnings will be giving increasingly more weight to the analysts' estimate for 2024, which is currently $258.03 (*Fig. 9*).

(5) *Forward P/E.* The bears correctly observe that it would be very unusual to see the next bull market start at a forward P/E of around 15.0, which is the historical average of the P/E ratio (using reported earnings from 1935-1978 and forward earnings since 1979) (*Fig. 10*). Since the bears expect a hard landing, they conclude that the latest bear market hasn't bottomed yet. It will do so only after analysts are forced by the coming recession to slash their estimates for S&P 500 revenues, profit margins, and earnings. Along the way, investors are likely to respond by further lowering the P/E multiple they are willing to pay for falling earnings. In this scenario, the P/E could fall much lower, especially if inflation remains stubbornly high during the recession, as happened during the Great Inflation of the 1970s. Again, that's the bears' scenario, not ours.

(6) *Sentiment.* Also supporting our view that the bear bottom has occurred is the extreme bearish readings in various surveys of investors' sentiment. For example, this year, Investors Intelligence Bull-Bear Ratio has been below 1.00 for 17 of the 26 weeks since early May (*Fig. 11*). It can stay this low for quite some time during bear markets. But it tends

to be a very good contrarian “buy” indicator for long-term investors.

Strategy III: Less Mega in MegaCap-8. So far this year through Friday, the performance derby shows that the eight very high-capitalization stocks known as the “MegaCap-8” (-33.4%) collectively has underperformed the S&P 500 (-18.2%) and the DJIA-30 (-9.6%). The MegaCap-8 still accounts for 21.5% of the market capitalization of the S&P 500, but that’s down from a record 26.4% during the week of November 19, 2021 (*Fig. 12*). It still accounts for 48.0% of the market cap of S&P 500 Growth, down from the peak of 50.9% during the February 25 week. Here are a few more pertinent updates on the MegaCap-8:

(1) *Market cap.* Since the S&P 500 peaked at a record high on January 3, the market cap of the MegaCap-8 is down 33.4%, or $4.0 trillion, through Friday’s close (*Fig. 13*). Their float-adjusted market-cap decline of $3.3 trillion accounted for 44% of the $7.5 trillion drop in the S&P 500’s market cap over the same period.

Here are the percentage and dollar declines (in billions) of the individual MegaCap-8 stocks ytd: Meta (-71.5%, -$669 billion), Nvidia (-53.2, -391), Netflix (-50.7, -135), Amazon (-37.7, -638), Alphabet (-35.1, -674), Tesla (-32.0, -340), Microsoft (-30.4, -767), and Apple (-14.1, -410) (*Fig. 14*).

(2) *Valuation.* At 24.7, the forward P/E of the MegaCap-8 was still relatively high at the end of last week (*Fig. 15*).

(3) *DJIA.* The DJIA-30 includes just one MegaCap-8, namely Microsoft. This concentrated portfolio is down just 9.6% ytd. It jumped 14.4% this month through Friday, representing its best October performance ever, going back to 1921, and its best month overall since a 14.4% gain in January 1976.

Strategy IV: Trading Corner. Here is Joe Feshbach’s latest call on the market: “Previously, I said this rally should take the S&P 500 up to the 3850-3900 range, and we’re right at the upper range. However, the short-term charts still look a little higher to me. The S&P 500 took out its previous high of 3886, while the Nasdaq has not. The Nasdaq should exceed 11682 before any short-term peak is reached, in my opinion. The put/call ratio has been just okay, but did have a huge day on the Meta shellacking, while breadth has improved but is still nothing to celebrate. So while the market should climb higher over the short term, I don’t think there is significant upside at this point, and most likely a trading range will ensue.”

Movie. “All Quiet on the Western Front” (+ + +) (*link*) is a German production on Netflix of

the Erich Maria Remarque's book of the same name about the horrors experienced by a young German soldier fighting in the trenches during World War I. There is no glory in this anti-war movie. Wars have horrible consequences. The *WSJ* *review* observed that "the military high command on both sides … had 20th-century armaments and 19th-century thinking." Unfortunately, we are seeing a similar disaster today in real time playing out in Ukraine. The weapons are much more destructive today and the thinking is just as primitive. The acting and the cinematography are superb.

Calendars

US: **Mon:** Dallas Fed Manufacturing Index; Chicago PMI. **Tues:** ISM Manufacturing & Price Indexes 49.9/53.0; Construction Spending -0.5%; Job Openings 10.00m; API Weekly Crude Oil Stocks; OPEC Meeting. (DailyFX estimates)

Global: **Mon:** Eurozone CPI Headline & Core Flash Estimate 10.2%/4.8% y/y; Eurozone GDP 1.0%; Germany Retail Sales -0.3%m/m/-4.9%y/y; Spain Retail Sales; Italy GDP 0.3%q/q/2.0%y/y; UK Nationwide Housing Prices; Japan Household Confidence 31.0; Japan M-PMI 50.7; China Caixin M-PMI 49.0; RBA Interest Rate Decision 2.85%; Lane. **Tues:** Germany Import Prices 0.6%m/m/31.7%y/y; UK M-PMI 45.8; Lowe. (DailyFX estimates)

Strategy Indicators

Global Stock Markets Performance (*link*): The US MSCI index rose 3.9% last week and posted its third gain in four weeks. The index finished the week out of a bear market at 19.8% below its record high on December 27. The US MSCI ranked 24th of the 48 global stock markets that we follow in a week when 39 of the 48 countries rose in US dollar terms. The AC World ex-US index rose 2.3% and ended the week at 29.4% below its June 15, 2021 record high, but most EM regions moved lower. EM Eastern Europe was the best performer with a gain of 7.2%, followed by EMU (5.3%) and EAFE (4.1). BIC was the worst performing region last week, with a decline of 5.7%, followed by EM Latin America (-3.4), EM Asia (-2.5), and EMEA (-0.8). Poland was the best-performing country last week, with a gain of 9.8%, followed by Austria (7.9), Sweden (7.5), and Ireland (7.3). Among the 12 countries that underperformed the AC World ex-US MSCI last week, China's 9.0% decline was the biggest, followed by those of Hong Kong (-7.7), Brazil (-7.6), Turkey (-3.5), and

Pakistan (-3.0). The US MSCI's ytd ranking remained steady w/w at 20/49. After lagging for much of year through July, the US MSCI's ytd decline of 19.3% is now less than the AC World ex-US's 26.2% drop. EM Latin America is up 3.6% ytd and along with EAFE (-25.1) are the only regions outperforming the AC World ex-US. The laggards: EM Eastern Europe (-86.1), BIC (-35.2), EMEA (-35.1), EM Asia (-34.4), and EMU (-28.4). The best country performers so far in 2022: Turkey (35.8), Jordan (15.5), Chile (13.8), Argentina (9.3), and Brazil (7.9). Apart from Russia, in which investors have lost 100.0% of their investment this year, here are the worst-performing countries ytd: Sri Lanka (-67.2), Poland (-45.1), Hungary (-44.1), China (-43.1), and Taiwan (-41.8).

S&P 500/400/600 Performance (*link*): All three of these indexes moved higher w/w for just the fourth time in 10 weeks and left bear market territory. LargeCap rose 4.0%, behind the gains for SmallCap (6.1%) and MidCap (5.3), which were these two indexes' best performances in 22 weeks. LargeCap finished the week at 18.7% below its record high on January 3; MidCap is 16.3% below its record high on November 16; and SmallCap is 18.4% below its November 8 record high. Thirty-two of the 33 sectors moved higher for the week, the same as a week earlier. SmallCap Utilities was the best performer with a gain of 7.4%, followed by SmallCap Consumer Discretionary (7.2), SmallCap Industrials (7.1), MidCap Financials (6.9), SmallCap Real Estate (6.7), and LargeCap Industrials (6.7). LargeCap Communication Services (-2.9) was the biggest underperformer last week, followed by LargeCap Consumer Discretionary (0.7), MidCap Materials (2.3), LargeCap Energy (2.8), and MidCap Energy (3.2). In terms of 2022's ytd performance, LargeCap's 18.2% decline continues to trail those of MidCap (-14.3) and SmallCap (-14.6). Four of the 33 sectors are positive so far in 2022, up from three a week earlier. Energy continues to dominate the top performers: LargeCap Energy (62.2), SmallCap Energy (53.5), MidCap Energy (45.0), MidCap Consumer Staples (0.3), and MidCap Financials (-2.1). The biggest ytd laggards: LargeCap Communication Services (-38.5), SmallCap Real Estate (-29.8), LargeCap Consumer Discretionary (-29.7), LargeCap Real Estate (-28.9), and SmallCap Consumer Discretionary (-27.3).

S&P 500 Sectors and Industries Performance (*link*): Ten of the 11 S&P 500 sectors rose last week, and seven outperformed the composite index's 4.0% rise. That compares to a 4.7% gain for the S&P 500 a week earlier, when all 11 sectors rose and five outperformed the index. Industrials was the top performer, with a gain of 6.7%, followed by Utilities (6.5%), Financials (6.2), Real Estate (6.2), Consumer Staples (6.1), Health Care (5.0), and Tech (4.3). Communication Services (-2.9) was the worst performer, followed by Consumer Discretionary (0.7), Energy (2.8), and Materials (3.3). The S&P 500 is down 18.2% so far in 2022 with seven sectors ahead of the index and just one in positive territory. The best

performers in 2022 to date: Energy (62.2), Consumer Staples (-5.3), Health Care (-5.8), Utilities (-5.9), Industrials (-10.6), Financials (-12.6), and Materials (-17.4). The ytd laggards: Communication Services (-38.5), Consumer Discretionary (-29.7), Real Estate (-28.9), and Tech (-25.7).

S&P 500 Technical Indicators (*link*): The S&P 500 rose 4.0% last week and improved relative to its 50-day moving average (50-dma) and its 200-day moving average (200-dma). The index moved back above its 50-dma for the first time in seven weeks, but closed below its 200-dma for the 36th time in 39 weeks. It had been above its 200-dma for 81 straight weeks through early February. The S&P 500's 50-dma moved lower for the 20th time in 26 weeks as the index improved to 1.7% above its falling 50-dma from 3.2% below a week earlier and a 15-week low of 10.6% below at the end of September. That compares to a 23-month high of 8.7% above its rising 50-dma the week in early August and a 27-month low of 11.1% below its falling 50-dma in mid-June. The index had been mostly trading above its 50-dma from late April 2020 to early April 2022; in June 2020, it was 11.7% above, which was the highest since its record high of 14.0% in May 2009. That compares to 27.7% below on March 23, 2020—its lowest reading since it was 29.7% below on Black Monday, October 19, 1987. The price index closed Friday at 4.8% below its falling 200-dma, up from 8.8% below a week earlier and an 18-week high of 0.8% below in early August. It remains above its 26-month low of 17.1% below its falling 200-dma in mid-June. The latest reading is down sharply from 10.8% above its rising 200-dma in November 2021. That compares to 17.0% above in December 2020, which was the highest since November 2009 and up from the 26.6% below registered during the Great Virus Crisis on March 23, 2020—the lowest reading since March 2009. At its worst levels of the Great Financial Crisis, the S&P 500 index was 25.5% below its 50-dma on October 10, 2008 and 39.6% below its 200-dma on November 11, 2008. The 200-dma fell for a 26th straight week, but its pace of decline is slowing now from its fastest rate since July 2009.

S&P 500 Sectors Technical Indicators (*link*): Seven of the 11 S&P 500 sectors are trading above their 50-dmas, up from two sectors a week earlier. These four sectors still trade below their 50-dma: Communication Services, Consumer Discretionary, Real Estate, and Utilities. At the end of September, all 11 sectors were below. Energy and Health Care are the only sectors with a rising 50-dma. Looking at the more stable longer-term 200-dmas, Health Care and Industrials joined Energy in the latest week as the only sectors above that measure. For perspective, at the depths of the Great Virus Crisis in April 2020, Health Care was the only sector trading above its 200-dma. Health Care also joined Energy as the only sectors with a rising 200-dma now.

US Economic Indicators

GDP (*link*): Real GDP expanded during Q3 for the first time in three quarters, though there were more signs of weakness than strength. The economy advanced 2.6% (saar) last quarter after contracting 0.6% and 1.6% the prior two quarters, with yearly growth at a paltry 1.8%. *Real consumer spending* increased only 1.4% (saar), following gains of 2.0% and 1.3% the prior two quarters, with the yearly percent change slowing from a peak of 16.6% during Q2-2021 to only 2.0% last quarter. Real consumer goods consumption contracted for the third straight quarter, slumping 1.2% (saar) during Q3, with both nondurable (-1.4) and durable (-0.8) goods consumption in the red; services consumption slowed to 2.8% (saar) from 4.6% during Q4. Meanwhile, *real gross private domestic investment* contracted 8.5% (saar), following a 14.1% drop during Q2, as investment in *real residential* (-26.4%, saar) and *nonresidential structures* (-15.3) continued to post double-digit declines, while inventory investment continued to slow. Meanwhile, *real nonresidential investment* expanded 3.7% (saar) after virtually no growth during Q2 as spending on equipment (10.8) and intellectual property products (6.9) continued to show healthy growth, more than offsetting the decline in nonresidential structures. *Real inventory investment* was a drag on growth again last quarter, slowing to $61.9 billion from $110.2 billion and $214.5 billion the prior two quarters. Meanwhile, real GDP got a big boost from trade, with *real net exports of goods & services* narrowing $156.5 billion, to -$1.27 trillion, as exports (14.4%, saar) posted another double-digit gain last quarter, while imports (-6.9) contracted. *Real government spending* expanded 2.4% during Q3 after declining the prior two quarters by 1.6% and 2.3%.

Contributions to GDP Growth (*link*): Trade was by far the biggest positive contributor to real GDP during Q3, followed by consumer spending, nonresidential fixed investment, and government spending. Trade contributed 2.77ppts to Q3 real GDP, with both exports (1.63ppt) and imports (1.14) adding to the top line. Real consumer spending contributed 0.97ppt to Q3 real GDP as growth in services consumption (1.24) more than offset the contraction in goods consumption (-0.28)—with nondurable goods consumption (-0.20) accounting for most of the decline in the latter. Nonresidential fixed investment added 0.49 to real GDP as positive contributions from equipment (0.54) and intellectual property products (0.36) more than offset the drag from structures (-0.41). Equipment spending was a mixed bag, with positive contribution from spending on transportation equipment (0.63) and information processing equipment (0.18) more than offsetting the negative contributions from industrial equipment (-0.17) and other equipment (-0.11). Government spending added to real GDP growth for the first time since Q1-2021, with both federal (0.23) and state & local (0.19) spending contributing. In the meantime, residential investment was a drag on

real GDP for the sixth successive quarter, subtracting 1.37ppt last quarter, while inventory investment (-0.70) subtracted from real GDP growth for the second consecutive quarter.

Personal Consumption Deflator (*link*): September's PCED rose 0.3%, matching August's pace which followed a 0.1% downtick in July—which was the first monthly decline since April 2020; the measure had increased 1.0% in June. Meanwhile, core prices rose 0.5% for the second straight month in September after showing no change in July The yearly headline rate held at 6.2%, down from June's 7.0% peak—which was the highest reading since the end of 1981; it was at 4.6% a year ago. The yearly core rate accelerated for the second month to 5.1% in September after slowing from 5.0% in June to 4.7% in July; it peaked at 5.4% during February and March. On a *three-month annualized basis*, the core rate slowed to 4.2% in September after climbing from 4.2% in July to 4.9% in August; it was at 5.3% in June. The three-month rate for durable goods slowed to 2.8% (saar) in September, easing for the second month since June's 5.1%, while the three-month rate for core nondurable goods prices slowed to 2.3% from August's 4.8%. Meanwhile, services prices ex energy is hovering just below its recent June peak of 5.4% (saar) for the third month, ticking down to 4.5% in September. The three-month annual rates for consumer durable goods (2.8%, saar & 5.7% y/y), consumer core nondurable goods (2.3 & 3.8), and consumer core services (4.5 & 4.9) prices were all below their yearly rates. *PCED components for which three-month rates lag yearly rates*: gasoline & other energy products (-83.2% & 20.2%), lodging away from home (-17.6 & 3.1), household appliances (-17.0 & 0.4), airfares (-10.8 & 32.9), used motor vehicles (-6.0 & 7.1), sports & recreational vehicles (-3.7 & -0.2), clothing & footwear (-1.0 & 5.7), hospitals (1.1 & 2.9), recreation services (1.5 & 4.5), prescription drugs (2.4 & 2.7), alcoholic beverages purchased for off-premise consumptions (2.9 & 3.0), professional & other services (3.8 & 7.0), transportation services (6.0 & 16.4), tobacco (6.4 & 8.2), furniture & home furnishings (7.8 & 10.2)), new motor vehicles (8.8 & 9.3), motor vehicles & parts (10.2 & 12.7), food & nonalcoholic beverages purchased for off-premise consumption (12.1 from 13.4). *PCED components for which three-month rates exceed yearly rates*: personal care products (11.4 & 6.8), tenant rent (9.2 & 7.2), owner-occupied rent (8.7 & 6.7), education services (2.7 & 2.3), physician services (1.7 & 0.2), and video audio & information processing (0.4 & -0.7).

Consumer Sentiment Index (*link*): Consumer sentiment confirmed its preliminary estimate, edging up just 1.3 points this month to 59.9 in October, but was just 9.9 points above its all-time record low of 50.0 in June. The report notes that while lower-income consumers reported sizable gains in overall sentiment, consumers with considerable stock market and housing wealth showed notable declines. The October *present situation component* climbed for the fourth month from 53.8 to 65.6, while the *expectations component* fell 1.8 points to

56.2 after no change in September; it had jumped a surprising 10.7 points in August. The *one-year expected inflation rate* rose to 5.0% this month after easing steadily from 5.3% in June to 4.7% by September, with increases reported across age, income, and education. The *five-year expected inflation rate* climbed back up to 2.9%, after falling to 2.7% in September—which was the first time it fell below the 2.9%-3.1% range since last July. According to the report, "Uncertainty over inflation expectations remains elevated, indicating that inflation expectations are likely to remain unstable in the months ahead."

Employment Cost Index (*link*): Compensation for private workers are rising, but not if you adjust for inflation. Compensation in private industry increased 1.1% during Q3, with wages and salaries up 1.2% and benefits up 0.8%—and all three measures slowing from Q2 gains of 1.5%, 1.6% and 1.3%. The yearly inflation rates slowed for all three measures from their recent peaks during Q2: compensation (to 5.2% from 5.5%), wages & salaries (5.2% from 5.7%), and benefits (5.0% from 5.3%). Adjusting for inflation, total compensation is down 2.8% y/y, with wages & salaries and benefits falling 2.7% and 3.0%, respectively. Yearly rates for *goods-producing industries* show a slowing in total compensation (to 4.6% from 4.7%) from the Q2 peak, reflecting a slowing in benefits (5.0 & 5.3); the wages & salaries (5.0 & 4.7) rate continues to accelerate. Looking at *service-providing industries*, the compensation (5.4 & 5.8) rate eased along with wages & salaries (5.3 & 5.9), while benefits (5.4 & 5.3) showed a slight uptick. The real compensation measure for goods-producing industries fell 3.4%, with wages & salaries and benefits down 2.9% and 4.2%, respectively, while these rates for service-providing industries fell 2.6%, 2.7%, and 2.6%.

Durable Goods Orders & Shipments (*link*): Durable goods orders in September posted a smaller-than-expected gain, though climbed to its highest level since July 2014. Meanwhile, core capital goods orders and shipments both dipped in September after a string of gains to new record highs. *Nondefense capital goods shipments excluding aircraft* (used in calculating GDP) slipped 0.5% last month, but that was after climbing in every month but one since its April 2020 bottom, by a total of 34.8%, to a new record high. Meanwhile, *core capital goods orders* (a proxy for future business investment) slumped 0.7% in September after advancing all but four months since April 2020, climbing 35.6% over that 28-month period to a new record high. *Total durable goods orders* rose 0.4% in September, smaller than the 0.6% expected gain, while revisions showed August's 0.2% decrease was revised up to a 0.2% increase. September's gain was led by a 2.1% jump in transportation equipment orders to its highest level since summer 2014, while durable goods orders excluding transportation recorded its first decline in seven months, sinking 0.5%, led by notable declines in orders for communications equipment (-3.2%), primary metals (-1.7), and electrical equipment, appliances & components (-1.3).

Pending Home Sales (*link*): "Persistent inflation has proven quite harmful to the housing market," said Lawrence Yun, NAR's chief economist. "The Federal Reserve has had to drastically raise interest rates to quell inflation, which has resulted in far fewer buyers and even fewer sellers." The *Pending Home Sales Index* (which tracks sales when a contract is signed but the transaction has not yet closed) fell for the fourth successive month by 10.2% in September and 20.2% over the period to 79.5—the lowest since April 2020. *Regionally*, pending home sales fell in all regions on both a monthly and yearly basis; here's the tally: South (-8.1% m/m & -30.0% y/y), Midwest (-8.8 & -26.7), West (-11.7 & -38.7), and Northeast (-16.2 & -30.1). Yun noted, "The new normal for mortgage rates could be around 7% for a while. . . . Only when inflation is tamed will mortgage rates retreat and boost home purchasing power for buyers."

Global Economic Indicators

Eurozone Economic Sentiment Indicators (*link*): The Economic Sentiment Indexes (ESI) for both the EU and Eurozone continued to slide in October, falling to their lowest levels since August and November 2020, respectively. The EU's ESI (-1.5 points to 90.9) is down 25.7 points since its recent peak of 116.6 last October, while the Eurozone's (-1.1 to 92.5) is 25.4 points lower than its 117.9 peak last October. *ESIs among the six largest EU economies* were mixed, with ESIs in Germany (-1.0 to 90.9) and Italy (-0.9 to 95.0) falling, while being essentially unchanged in the Netherlands (-0.3 to 90.3) and France (unchanged at 96.2); ESIs improved slightly in Poland (+0.4 to 88.6) and Spain (+1.4 to 98.0). *By sector*, Industrial confidence fell further into contractionary territory, dropping nine of the 10 months since reaching a record high of 12.9 in December, plunging to -2.6 in October—slipping below zero last month for the first time since January 2021. Services confidence has been sliding since its recent peak of 17.9 last October, declining to a 18-month low of 1.9 this October on widespread weakness. Meanwhile, consumer confidence (to -28.9 from -29.6) was little changed from September's record low, while construction (-0.2 from -0.4) barely budged from its recent low; retail trade (-7.0 from -7.8) confidence picked up slightly due to a marked improvement in retailers' assessment of the past business situation.

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, 570-228-9102

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