Yardeni Research

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Morning Briefing

More On Sweep Stakes

Check out the accompanying chart collection.

Executive Summary: The polices of both US presidential contenders would widen an already wide fiscal budget deficit, especially in a sweep scenario, where the party that controls the White House controls the two houses of Congress as well. A Trump presidency and GOP sweep look increasingly likely. Today, Eric compares how a win by each of the candidates might affect the US government debt, deficit, and Treasury bond market. … And Jackie examines potential ramifications of a Harris win versus a Trump win on individual S&P 500 sectors and industries. … Also: How Trump won over the crypto crowd.

Politics & Strategy I: Red Vs Blue Wave. Whether Donald Trump or Kamala Harris is the next US president, the outcome is likely to be four years of policies that widen an already wide federal deficit (*Fig. 1*). Harris would favor more spending, partially funded by raising taxes, while Trump would favor tax cuts, partially funded by tariffs. Both hope that stronger economic growth would help fill in the gaps and prevent the debt load from blowing out relative to GDP (*Fig. 2*).

The Committee for a Responsible Federal Budget *estimates* Harris' current proposed plans would increase the federal debt by $4 trillion through 2035—only about half of its estimate for President Trump's proposed plans.

We are still rooting for gridlock, but a GOP sweep (controlling both houses of Congress and the White House) looks more likely than a Democratic sweep. The latest forecast from *FiveThirtyEight* has Trump (52%) beating Harris (48%). Furthermore, according to its model, the Republicans have an 88% chance of flipping the Senate. The odds for the House are currently 52%/48% Republicans versus Democrats, with the majority boiling down to "less than 30 key seats."

As we all know, neither party looks the same as it did 20 years ago. Even if the GOP flips the Senate, our friend Jim Lucier of *Capital Alpha Partners* believes it may take 53 or 54 seats for Trump to have a comfortable majority that sides with him on key issues.

In our view, a Trump win would likely be accompanied by a red wave. These outcomes are not mutually exclusive—if Trump wins by any sizeable margin, it is likely that voters would have chosen Republican congressional candidates as well. A sweep by either party has long been the outcome we believed would widen the deficit the most.

We presented our case for shorting bonds in our August 19 *Morning Briefing*. The thesis was predicated on the Federal Reserve's preparing at the time to cut interest rates despite the economy still running hot. The 10-year Treasury bond yield rode both of those from roughly 3.6% to 4.1% in just a few weeks. The bond market may have sniffed out the rising odds of a GOP sweep, as the 10-year yield climbed to near 4.3% this week (*Fig. 3*). Then again, the backup in yields coincided with better-than-expected economic indicators (as tracked by the Citigroup Economic Surprise Index) and a growing realization that the Fed's 50bps cut in the federal funds rate on September 18 was too much too soon (*Fig. 4*).

Politics & Strategy II: Weighing the Election's Impact. Presidential candidates Trump and Harris propose dramatically different policies, which would have dramatically different impacts on specific S&P 500 sectors and industries. The S&P 500 Technology, Health Care, and Consumer Discretionary sectors in particular would face very different futures under a Harris administration versus a Trump one. The Financials sector, however, may benefit under both candidates due to their spendthrift ways.

Let's compare the ramifications of the two candidates' proposals on specific sectors and industries in the S&P 500:

(1) *Financials: Rates higher for longer.* Polls favoring Trump have improved over the past month, leaving the two candidates in a statistical dead heat. Stock market activity seems to suggest that investors believe that Trump's momentum will lead him into the Oval Office.

Shares of Trump Media & Technology Group have jumped more than 300% since bottoming on September 23. The yield on the 10-year Treasury bond has risen to 4.28% from 3.75% over the same period (*Fig. 5*). And the yield curve has an upward slope this month (*Fig. 6*). Improving prospects for the economy have certainly contributed to higher rates, but the slew of debt that will be sold to finance Trump's or Harris's plans is likely adding to the bond market's jitters.

A steeper yield curve has likely helped the S&P 500 Financials sector index rally this month, outperforming all other S&P 500 sectors except Information Technology. The Financials sector also has responded to stronger-than-expected Q3 earnings reports. On the other hand, loftier interest rates presumably weighed on the Utilities and Real Estate sectors.

Here's the performance derby for the S&P 500 and its sectors since the start of October through Tuesday's close: Information Technology (4.1%), Financials (3.4), Communication Services (2.5), S&P 500 (1.2), Consumer Discretionary (0.2), Energy (0.0), Industrials (-0.1), Utilities (-1.9), Real Estate (-2.1), Materials (-2.4), Consumer Staples (-2.6), and Health Care (-3.8) (*Fig. 7*).

Within the Financials sector, the Investment Banking & Brokerage industry stock price index has gained 10.7% in October through Tuesday's close, followed by Diversified Banks (6.9%), Asset Management & Custody Banks (6.9), and Regional Banks (3.9) (*Table 1*).

Conversely, the S&P 500 Homebuilding and Automobile Manufactures industries, which are in the Consumer Discretionary sector, could face headwinds as higher interest rates make borrowing to buy a home or a car more expensive (*Fig. 8*). Harris plans to lend a hand by offering first-time homebuyers $25,000 toward their downpayment. After rallying for most of 2024, the Homebuilding industry's stock price index fell 10.0% in October, while the S&P 500 Automobile Manufacturers industry gained 0.1% during the month thanks to GM's strong Q3 earnings report (*Fig. 9* and *Fig. 10*).

(2) *Technology: Betting on Khan's departure.* Lina Khan was named head of the Federal Trade Commission (FTC) by the Biden administration and has been a thorn in the side of technology companies ever since. The agency tried unsuccessfully to block Microsoft's $69 billion acquisition of Activision Blizzard last year. It was reviewing Amazon's offer for iRobot when the two companies agreed to walk away from the deal after the European antitrust agency raised concerns about it.

The FTC is currently examining large technology companies' investments into and partnerships with artificial intelligence companies. Companies under the microscope include Amazon, Alphabet, Microsoft, Anthropic and OpenAI, a January 25 CNBC *article* reported. The FTC also sued Amazon, alleging that it used its position as an e-commerce superstore and fulfillment center to prevent rivals from entering the industry.

A Trump administration would likely appoint its own head of the FTC and head of the Department of Justice's antitrust division. Though Harris hails from California, home to many tech mavens, she is expected to reinstate Khan. Despite Khan's tenure, the S&P 500 Technology sector has soared 34.9% ytd through Tuesday's close, and the Communication

Services sector has added 31.0% (*Fig. 11*).

(3) *Health Care: Sickly under both candidates.* The S&P 500 Health Care sector is the perpetual punching bag for political candidates. Harris has run on the promise to cap the price of insulin for all consumers, not just the seniors who benefit from the $35 price cap today. She'd also expand the $2,000 out-of-pocket cap on drug expenses that seniors enjoy to the masses. And she's expected to expand the number of drugs for which Medicare and Medicaid Services are allowed to negotiate prices faster than a Trump administration might.

Former President Trump wasn't exactly a friend of the pharma industry either. He signed an executive order that would have set Medicare reimbursements for 50 drugs at the lowest price paid for those drugs in other developed countries. A US District Judge blocked the rule because the administration hadn't given the public a chance to comment on it, as is required by law. Trump proposed another executive order that banned drug makers from providing rebates to pharmacy benefit managers and insurers, but it never went forward. Nonetheless, both actions indicate that the former President is willing to try unorthodox ways of reducing drug prices.

Health Care is the worst performing sector in the S&P 500 this month through Tuesday's close and the second worst performing sector ytd. Its returns this month are being dragged down by the Pharmaceuticals (-1.3%) and Biotechnology (-2.6%) industries (*Fig. 12* and *Fig. 13*). More problematic have been the rising prices weighing on the profitability of health insurers in the Managed Health Care industry's stock price index, which has fallen 6.5% in October through Tuesday's close (*Fig. 14*).

By the way, Robert F. Kennedy Jr. said on Monday that former President Donald Trump has promised him "control" of HHS and the Department of Agriculture, according to a video obtained by POLITICO.

Speaking at a virtual event, the former presidential candidate said "[T]he key that President Trump has promised me is control of the public health agencies, which are HHS and its sub-agencies, CDC, FDA, NIH, and a few others … and then also the USDA." Kennedy did not specify whether he was referring to the HHS secretary post. An appointment of Kennedy to a cabinet position like HHS secretary would require Senate confirmation, which could be a significant hurdle given his vaccine skepticism and other controversial positions.

(4) *Consumer Discretionary: Tax cuts for everyone.* The Trump and Harris campaigns are handing out tax cuts and tax credits like Tic Tacs. Both camps want to eliminate taxes on

tips.

Harris has said she'd boost the child tax credit to $3,000 and give new parents a $6,000 tax credit. But Harris is expected to raise taxes on the wealthy by increasing the capital gains taxes from 20% to 28% for anyone making $1 million or more. She may also ensure that households with $100 million or more in assets face a tax rate of at least 25%.

Trump would end taxes on Social Security and overtime, while also extending all of the tax breaks under the Tax Cuts and Jobs Act. He also promises to reinstate the State and Local Tax deduction.

If their promises come to fruition, high-end end retailers could suffer under a Harris administration, while retailers catering to lower- and middle-class consumers could benefit. Under Trump, all retailers stand to benefit from increased consumer spending, but they also could be hurt if the many imported goods they sell get slapped with tariffs. Trump has proposed tariffs of 10%-20% on imported goods. Il manufacturers pass the tariffs' cost on to retailers and retailers pass on the higher costs to consumers in the form of price increases, consumers may buy less; if retailers don't do so, their costs will rise and margins will shrink. Neither are good options.

(5) *Energy: Watch supply.* The Trump camp has said it will be far friendlier to the Energy sector, lifting regulations imposed by the Biden administration and presumably continued under Harris. But in an odd twist, Harris may be better for the sector. If the Harris administration limits drilling and that reins in supply, the price of oil could perform better than it would if Trump increases drilling, putting additional pressure on an already oversupplied market.

Disruptive Technologies: Bitcoin for Trump. Former President Trump, the self-described "crypto-candidate," has endeared himself to the crypto community. He believes the US should be the crypto capital of the world, and his campaign accepts donations in bitcoin and other crypto currencies. Trump has promised to create a national bitcoin reserve and introduced a new crypto company, World Liberty Financial, which some believe will be a crypto borrowing and lending platform. While Trump and the Trump organization don't own the company, they may receive compensation from it.

Trump has gained crypto fans by promising to fire Securities & Exchange Commission (SEC) Chair Gary Gensler, whose term expires in January 2026. Gensler is unpopular among the crypto crowd because he considers most crypto coins unregistered securities, he has highlighted the fraud and scams in the crypto market, and he has enforced investor protection laws. The crypto bros accuse him of regulatory overreach.

Ironically, it was also under Gensler that a bitcoin ETF was approved. Since the ETF launched on January 11, bitcoin has soared more than 50% (*Fig. 15*). During October, the cryptocurrency has gained roughly 13.9%, pushed higher by the awareness of growing US deficits and rising Treasury bond interest rates in addition to Trump's gains in the polls.

Harris has said much less about the crypto market, but she has promised to support digital currencies and has used Mark Cuban to court the crypto community. She has called for stronger regulatory oversight of the crypto markets, and she's considered more likely to retain Gensler as SEC chair.

While bitcoin would likely fall if Harris wins the election, its response to a Trump presidency is harder to gauge. Bitcoin could continue to rally, or given its ytd gains, the currency could fall in a classic case of buy-the-rumor-sell-the-news.

Calendars

US: **Thurs:** Personal Income & Spending 0.3%/0.4%; Core PCED 0.3%; Employment Cost Index 0.9%q/q; Initial Claims 231k; Chicago PMI 47.1; Fed's Balance Sheet. **Fri:** Nonfarm & Private Payroll Employment 111k/115k; Average Hourly Earnings 0.3%; Average Workweek 34.2 hours. Unemployment Rate 4.1%; ISM M-PMI & Price Index 47.5/48.9; Construction Spending -0.1%; Baker Hughes Rig Count. (FXStreet estimates)

Global: **Thurs:** Eurozone Headline & Core CPI 1.9%/2.6%y/y; Eurozone Unemployment Rate 6.4%; Germany Retail Sales -0.8%; France CPI 0.2%m/m/1.5%y/y; Italy CPI 0.0%Italy Unemployment Rate 6.2%; ECB Economic Bulletin; Japan Housing Starts -4.2%; China Caixin M-PMI 49.7; Breeden. **Fri:** Eurozone GDP 0.2%q/q/0.8%y/y; Eurozone Business & Consumer Survey 96.4; Eurozone Consumer Confidence -12.5; Eurozone Industrial Sentiment -10.5; Germany GDP -0.1%q/q/-0..3%y/y; Germany CPI 0.2%m/m/1.8%y/y; Germany Unemployment Rate 6.1%; France GDP 0.3%q/q; Italy GDP 0.2%q/q/0.7%y/y; Spain GDP 0.6%q/q/3.0%y/y; Spain CPI 1.7%y/y; BOJ Interest Rate Decision 0.25%; Japan Industrial Production 0.9%; Japan Retail Sales 2.1%yy; Japan Household Confidence 36.7; China M-PMI & NM-PMI 50.0/50.5; Schlegel; Schnabel; Nagel; Rogers; Macklem. (FXStreet estimates)

Strategy Indicators

Stock Market Sentiment Indicators (*link*): The *Bull-Bear Ratio* rose for the second week to 2.69 this week after falling from 2.62 to 2.35 the prior week. *Bullish sentiment* slipped to 57.6% this week after climbing the prior two weeks by 5.1ppts (to 58.3% from 53.2%)—which was the most bulls since late July (when the report noted seven consecutive weeks with bulls over 60%, ending at 64.2%). Bullish sentiment was at 43.5% seven weeks ago—which was the lowest percentage since last August. Meanwhile, *bearish sentiment* edged up to 22.0% this week after edging down from 22.2% to 21.7% last week, remaining in a tight range. Both are still far above the mid-July percentage of just 14.9%. The *correction count* edged up to 20.4% this week, after edging down from 20.4% to 20.0% last week. Recent readings are down from 33.9% in early September and now nearing the low levels during early summer. In the *AAII Sentiment Survey* (as of October 24), bullish sentiment among individual investors about the short-term outlook for stocks fell during the latest week, while bearish and neutral rose. *Bullish sentiment* sank 7.7ppts to 37.7%, remaining above its historical average of 37.5% for the 50th time in 51 weeks. *Neutral sentiment* increased 3.2ppts to 32.4%, moving above its historical average of 31.5% for the first time in 16 weeks. *Bearish sentiment* increased 4.5ppts to 29.9%—below its historical average of 31.0% for the 10th time in 11 weeks.

S&P 500 Earnings, Revenues, Valuation & Margins (*link*): The S&P 500's forward profit margin was unchanged w/w at a record high of 13.4% during the October 24 week. It is now 3.1ppts above its seven-year low of 10.3% during April 2020. Forward revenues and earnings were both at record highs during the October 3 week, but each edged down less than 0.1% w/w to 0.2% and 0.4% below their respective highs. Prior to that, revenues and earnings had been steadily making new record highs for just over 12 months. That compares to its prior 16-month string of record highs from March 2021 to June 2022; prior to that, they peaked just before Covid-19 in February 2020. The consensus expectations for forward revenues growth was steady w/w at 5.6%, and remains close to its 23-month high of 5.8% during the August 1 week. It has gained 3.3ppts from its 33-month low of 2.3% during the February 23, 2023 week. That's down from a record high of 9.6% growth at the end of May 2021 and compares to 0.2% forward revenues growth during April 2020, which was the lowest reading since June 2009. The forward earnings growth forecast fell 0.1pt w/w to 14.1% from a 36-month high of 14.2%. It's now 10.8ppts above its 31-month low of 3.3% during the February 16, 2023 week. That's down from its 23.9% reading at the end of April 2021, which was at its highest since June 2010 and up substantially from its record low of -5.6% at the end of April 2020. Analysts expect revenues to rise 4.5% in 2024 (down

0.1ppt w/w) and 5.6% in 2025 (unchanged w/w) compared to a revenues gain of 2.1% in 2023. They expect an earnings gain of 9.2% in 2024 (down 0.1ppt w/w) and a 15.0% rise in 2025 (unchanged w/w) compared to an earnings gain of 2.4% in 2023. Analysts expect the profit margin to rise 0.5ppt y/y to 12.4% in 2024 (unchanged w/w), compared to 11.9% in 2023, and to rise 1.1ppts y/y to 13.5% in 2025 (unchanged w/w). The S&P 500's weekly reading of its forward P/E edged down 0.1pt w/w to 21.8 from a 42-month high of 21.9, and is up 2.1pts from a 14-week low of 19.7 during the August 8 week and 6.5pts from a 30-month low of 15.3 in October of 2022. It also compares to 23.1 in early September 2020, which was the highest level since July 2000, and to a 77-month low of 14.0 in March 2020. The S&P 500 weekly price-to-sales ratio fell 0.02pt w/w to a 2.91 from a record high of 2.93 a week earlier. That's up from a six-month low of 2.22 during the October 26, 2023 week and compares to 49-month low of 1.65 in March 2020.

S&P 500 Sectors Earnings, Revenues, Valuation & Margins (*link*): During the October 24 week, forward revenues rose for four of the 11 S&P 500 sectors, and forward earnings rose for four sectors. This led to rising forward profit margins w/w for three sectors. Two sectors posted record-high forward revenues this week: Financials and Health Care. These six sectors are not far from their record-high forward revenues recently during the past few weeks: Communication Services, Consumer Discretionary, Consumer Staples, Information Technology, Real Estate, and Utilities. Industrials' forward revenues is 3.3% below its early September record due to Boeing's strike. Energy and Materials are the biggest laggards at 5.4% and 13.2% below, respectively. These two sectors had record-high forward earnings this week: Communication Services and Financials. These eight sectors are less than 3.3% below their recent records: Consumer Discretionary, Consumer Staples, Health Care, Industrials, Information Technology, Real Estate, and Utilities. Forward earnings remains depressed for Energy and Materials, which are 30.4% and 21.6% below their respective post-pandemic highs. Looking at the forward profit margin, most of the sectors have recovered from their early 2023 forward profit margin lows to near-record high readings again. In recent weeks, the Consumer Discretionary, Financials, Industrials, and Information Technology sectors were in that club. Among the laggards, Energy's forward margin has cratered 1.3pts to a 31-month low of 9.6% from its six-month high of 10.9% in mid-June; Consumer Staples' 6.9% is 0.2ppt above its seven-year low in March 2023; and Health Care's 8.7% is up 0.2ppt since its record low in April. The annual profit margin is expected to fall y/y in 2024 for Energy, Materials, and Real Estate and to improve for the other eight sectors. Here's how the S&P 500 and its 11 sectors rank based on their current forward profit margin forecasts along with their record highs: Information Technology (26.5%, down from its 27.6% record high in September), Financials (19.4, down from its 19.8 record high in August 2021), Communication Services (18.0, down from its 18.1 record high during the

August 8 week), Real Estate (17.4, up 0.2ppt w/w and down from its 19.2 record high in 2016), Utilities (14.2, down from its 14.8 record high in April 2021), S&P 500 (13.4, a record high in seven of the past eight weeks), Materials (11.2, down from a 20-month high of 11.6 in July and from its 13.6 record high in June 2022), Energy (9.6, down 0.1ppt w/w to a 31-month low and from its 12.8 record high in November 2022), Industrials (11.1, down from its 11.2 record high in early October), Consumer Discretionary (9.2, a record high this week), Health Care (8.7, up 0.2ppt from its 8.5 record low at the end of April and down 0.1ppt w/w and from its 11.5 record high in February 2022), and Consumer Staples (6.9, down from its 7.7 record high in June 2020).

US Economic Indicators

GDP (*link*): *Real GDP* was weaker than expected during Q3, while inflationary pressures continued to slow. Real GDP expanded 2.8% (saar)—slightly below the 3.0% increase expected—and slower than Q2's 3.0%. Meanwhile, the quarterly gain in the GDP deflator eased to 1.8% (saar) from 2.4% during Q2, with the PCED slowing from 2.5% during Q2 to 1.5% during Q3. Excluding food and energy, the increase slowed to 2.2% (saar) from 2.8% during Q2. The gains in Q3 real GDP were led by consumer spending, exports, and federal government spending. *Real consumer spending* expanded 3.7% (saar) during Q3, with *goods* (6.0%, saar) consumption accelerating from Q2's 3.0% increase, and *services* (2.6) consumption little changed from Q2's 2.7%. Within goods consumption, both *durable goods* (to 8.1% from 5.5% during Q2) and *nondurable goods* (4.9 from 1.7) consumption accelerated during Q3. The gain in *goods* consumption was led by other nondurable goods (led by prescription drugs) and motor vehicles & parts, while the gain in services consumption was driven by health care (led by outpatient services)—along with food service & accommodations. *Real nonresidential fixed investment* advanced 3.3% (saar), slowing from 3.9% and 4.5% the prior two quarters. Equipment spending, however, expanded at a double-digit pace of 11.1%, following a 9.8% jump during Q2. Meanwhile, intellectual property products has shown little gain the past two quarters, rising 0.6% during Q3, virtually matching Q2's 0.7%; it had increased 7.5% and 5.2% the previous two quarters. Spending on structures contracted 4.0%, the first decline since Q4-2021. Real *government spending* accelerated 5.0% (saar), led by federal (9.7%) government spending, which was boosted by a 14.9% increase in national defense spending. State & local government spending increased 2.3% for the second successive quarter. *Residential investment* was a drag on real GDP growth, falling 5.1% (saar) during Q3 after a 2.8% shortfall during Q2; it began the year with a double-digit surge of 13.7% during Q1. Overall, *trade* was also drag on GDP growth last quarter. The 8.9% (saar) increase in exports reflects an increase in goods, led by capital goods ex auto, while 11.2% increase in imports also was led by capital goods ex autos. (Note: imports, are a subtraction in the calculation of GDP.)

ADP Employment (*link*): "Even amid hurricane recovery, job growth was strong in October," noted Nela Richardson, chief economist of ADP. "As we round out the year, hiring in the US is proving to be roust and broadly resilient." *Private payrolls* blew past the forecast, increasing a larger-than-expected 233,000 in October and exceeding the consensus estimate of a 114,000 increase as well as September's 143,000. Job creation hit its highest level since July 2023. Service-providing jobs climbed 211,000 in October, while goods-producing industries increased 22,000. Within *services-providing* industries, education & health services (53,000) posted the biggest monthly gain, followed by trade/transportation & utilities (51,000), leisure & hospitality (37,000), professional & business services (31,000), other services (21,000), financial activities (11,000), and information services (7,000). Within *goods-producing* industries, construction (37,000) jobs continued to lead the pack, while employment in the natural resources/mining (4,000) also added jobs. Meanwhile, the manufacturing (-19,000) sector cut jobs during the month. According to the report, the yearly pay increase for *job-stayers* eased slightly to 4.6%, continuing a two-year slowdown, while the rate for *job-changers* slowed to 6.2% in October.

Global Economic Indicators

Eurozone Economic Sentiment Indicators (*link*): The Economic Sentiment Indexes (ESIs) for both the EU and the Eurozone dipped 0.7 points in October to 96.0 and 95.6, respectively. ESIs among the *six largest EU economies* all declined this month, except for Germany (+0.8 points to 89.4). Spain (-4.8 to 102.4) and France (-4.7 to 93.6) posted the largest setbacks, followed by Poland (-3.6 to 8.4) and the Netherlands (-2.3 to 98.7), with Italy (-0.5 to 99.5) posting a smaller decline. By *sector*, for the overall EU, retail trade (+0.9 to -5.4), construction (+0.7 to -7.0), and consumer (+0.5 to -11.2) sentiment rose, while services (+0.1 points to 6.9) sentiment barely budged; industry (-1.8 to -12.6) sentiment took a further hit in October.

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