Yardeni Research

May 5, 2025

Morning Briefing

Is The Recession Over Already?

Check out the accompanying chart collection.

Executive Summary: We believe in the resilience of the US economy. Recent years' monetary tightening didn't bring on a recession; this year's tariff turmoil isn't likely to either. We're lowering the odds we see of a recession back to 35%, where it had been in early March. One reason is that China and the US appear ready to start negotiating a trade deal. Trump needs to get past trade issues for the Republicans to keep their majorities in Congress after the midterms. … Also: The Index of Coincident Economic Indicators has been rising to new record highs. And Friday's jobs report boosted our confidence in the labor market's resilience. …And: Time to raise our S&P 500 target?

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

US Economy I: The Godot Recession Is Back. During 2022, 2023, and 2024, most economists and investment strategists expected that the dramatic tightening of monetary policy would cause a recession. They observed that the inverting yield curve and the falling Index of Leading Economic Indicators were confirming this outlook. We argued that the recession was the most widely anticipated recession of all times that wasn't likely to happen. We called it the "*Godot* recession." We focused on the reasons for the underlying resilience of the economy and dismissed the widely followed leading indicators of recession as misleading.

The Godot recession may be back in 2025. This time, the cause of the widely anticipated downturn is Trump's Tariff Turmoil.

According to Polymarket.com, a trading platform, the chance of a recession was relatively low around 20% from the time President Donald Trump was inaugurated on January 20 through March 11 (*Fig. 1*). The odds then shot up dramatically, especially after April 2 ("Liberation Day"), reaching 64% on April 8. They fluctuated around 55% after Trump postponed for 90 days the reciprocal tariffs that he had announced on April 2 for all countries with one notable exception: China’s tariff remained 145%. The odds of a recession rose to 66% on May 1 following last week’s batch of weak economic indicators (i.e., consumer confidence, ADP payrolls, M-PMI, and jobless claims). The odds fell to 60% on Friday, May 2, following the release of a stronger-than-expected employment report for April.

While economic growth remains our base-case scenario, we did raise our subjective probability of a “tariff-induced” recession from 20% at the start of the year to 35% on March 5. We wrote, “We are still betting on the resilience of consumers and the economy. However, Trump Turmoil 2.0 is significantly testing the resilience of both. That’s why we’ve recalibrated our subjective probabilities.” On March 31, we raised the odds again to 45% and blamed Trump’s Reign of Tariffs. We wrote, “That 45% is also the probability we see that the stock market’s correction will deepen into a bear market in coming months. Yet we still expect an up year, with the S&P 500 rising above 6000 by year-end.”

In other words, we remained, and remain, believers in the resilience of the economy. It withstood the tightening of monetary policy over the past three years. We expect it will withstand this year’s tariff turmoil.

US Economy II: Lowering Our Odds of a Recession. We are now lowering our odds of a recession back down to 35% because we believe that China and the US both may be ready to suspend their tariffs on each other while they negotiate a trade deal. In other words, both sides may be starting to blink. Neither side can bear the pain of a trade war, which might be more painful for China’s economy than America’s economy. On the other hand, Americans have less tolerance for pain than the Chinese (for more on China’s “*chiku*” ethos, see the *Morning Briefing* dated April 29, 2025).

We also expect that Trump will declare victory in his trade war with the rest of the world. By the end of the 90-day postponement period of his Liberation Day reciprocal tariffs, the US is likely to have signed numerous agreements with America’s major trading partners. Stragglers might come around during a second 90-day postponement period. Trump needs to put the trade issue behind him to reduce the odds of a recession, which would harm the Republicans’ chances of holding onto their slim majorities in both houses of Congress.

Trump also needs to get this issue resolved quickly now that numerous court cases have been filed challenging his constitutional authority to impose tariffs under his claim that they are warranted by a national crisis that he declared.

We anticipated all the above in our April 7 *Morning Briefing* titled “Annihilation Days.” We wrote:

“Trump’s Liberation Day last Wednesday triggered Annihilation Days on Thursday and Friday, with the Stock Market Vigilantes giving a costly thumbs-down to Trump’s Reign of Tariffs. Trump officials say they aim to make Main Street wealthy again even if that’s bad for Wall Street. The problem is that Main Street owns lots of equities traded on Wall Street, so the two streets prosper and suffer together. Congress can’t do much to stop Trump given his veto power, but he might get the message that hurting Main Street’s stock portfolios can cause a recession and jeopardize the GOP majority in Congress. If so, he might postpone the reciprocal tariffs, giving trade negotiations time to work. Also, the courts might block Trump’s tariffs. An early end to Trump’s tariff nightmare would result in a V-shaped stock-market bottom. We’re counting on that; the alternative is just plain ugly.”

Sure enough: Trump postponed his reciprocal tariffs two days later, on April 9. The S&P 500 traced out a V-shape, bottoming on April 8 and climbing 14.1% since then through Friday’s close (*Fig. 2* and *Fig. 3*).

We aren’t dismissing the possibility of a recession. There could still be supply disruptions resulting from the still unresolved trade war with China. Regional and national business surveys show weakening economic activity and rising prices during March and April (*Fig. 4*, *Fig. 5*, and *Fig. 6*). Measures of consumer confidence are at recessionary levels, especially those that track consumer expectations (*Fig. 7*). The latter is one of the 10 components of the Index of Leading Economic Indicators (LEI), which has been forecasting a recession since late 2022 (*Fig. 8*). Meanwhile, the Index of Coincident Economic Indicators (CEI) has been rising to new record highs since then through March!

We are betting on the resilience of consumer spending, which has been boosted by the spending of retiring Baby Boomers. We had been concerned recently about the negative wealth effect on consumption because of the drop in stock prices. Now we are less concerned given the subsequent rebound in stock prices. We are also betting on business spending to remain resilient. While tariff-related uncertainties may weigh on capital spending, we expect that spending related to cloud computing and onshoring will remain strong.

US Economy III: The Most Resilient Labor Market. The CEI probably edged up to another record high during April. That’s because nonfarm payroll employment in private industries, which rose to a record high in April, is one of the four components of the CEI

(*Fig. 9*). It tends to boost two of the other components, i.e., real personal income and real manufacturing and trade sales. The fourth CEI component is industrial production, which probably declined in April along with manufacturing aggregate weekly hours, as shown in April's employment report (*Fig. 10*).

By the way, the S&P 500 is also one of the 10 components of the LEI. We lowered our recession/stagflation odds today partly because the stock market is indicating that the outlook for the economy is improving. Friday's jobs report also increased our confidence in the resilience of the labor market. Let's review it:

(1) *Earned Income Proxy*. Aggregate weekly hours in private industries rose 0.1% m/m to a new record high of 4.7 billion during April (*Fig. 11*). Average hourly earnings rose 0.2% m/m last month. So our Earned Income Proxy for wages and salaries in private industries rose 0.3% to a new record high in April (*Fig. 12*). That augurs well for April's consumer spending. Indeed, April's auto sales remained robust at 17.3 million units (saar) (*Fig. 13*).

(2) *Payroll employment.* Payroll employment rose 177,000 during April. We expected 150,000-175,000. So we weren't surprised, though the consensus expectation was lower at 135,000. The previous two months were revised down by 58,000. Nevertheless, the average for the past three months was a solid increase of 155,000 (*Fig. 14*). Much of the strength in payrolls comes from services industries that cater to retiring Baby Boomers, particularly health care and social assistance, leisure and hospitality, and financial activities (*Fig. 15*).

(3) *Federal government employment.* Employment of federal workers fell only 9,000 last month. That followed a decline of 4,000 in March. So far, the DOGE Boys haven't had much impact on federal government employment. Solid gains were registered by health care and social assistance (58,200), transportation and warehousing (29,000), and leisure and hospitality (24,000). We acknowledge that the latter two could weaken if the trade war between China and the US persists.

(4) *Payroll employment diffusion index.* It was encouraging to see that the payroll employment diffusion index remained above 50.0% during April (*Fig. 16*).

Strategy: To Raise or Not To Raise Our S&P 500 Target? At the start of the year, our S&P 500 target for the end of this year was 7000. When we raised our odds of a recession on March 5 to 35%, we lowered our target to 6400. We lowered it again on March 31 to 6000, when we raised the odds of a recession to 45%.

Now that we are lowering the odds of a recession back to 35%, should we be raising our S&P 500 target back to 6400? We are inclined to do so given the power of the V-shaped rally in the S&P 500. However, we aren't ready to do so given the following two issues:

(1) *Earnings*. The outlook for S&P 500 earnings is deteriorating. Tariffs are first and foremost taxes on domestic importers. The 10% baseline tariff on all imports from most countries was announced by Trump on Liberation Day and imposed on April 5. There is also a 25% tariff on autos, aluminum, and steel. The 145% tariff on China remains in force as well.

Over the past 12 months through March, corporate tax receipts totaled $502.19 billion (*Fig. 17*). The currently active tariff rates could raise over $300 billion in import duties over the coming 12 months. That would be a significant increased tax burden on corporate profits unless they are passed through to consumer prices. Some companies, such as those in the auto industry, might find that hard to do.

(2) *Valuation*. The valuation multiple of the S&P 500 bottomed at 18.1 on April 8. It was back up to 20.5 on Friday (*Fig. 18*). It is very unlikely to bounce back to the 22.1 at which it began the year.

Calendars

US: Mon: ISM Services NM-PMI 50.6; S&P Global Composite & Services PMIs 51.2/51.4; Loan Officer Survey. **Tues:** Goods & Services Trade Balance -$129b. (FXStreet estimates)

Global: Mon: Eurozone Sentix Investor Confidence. **Tues:** Eurozone PPI -1.1%; Eurozone, Germany & France C-PMIs 50.1, 49.7 & 47.3; Eurozone, Germany & France NM-PMIs 49.7, 48.8 & 46.8; France Industrial Production 0.2%; UK C-PMI & NM-PMI 48.2 & 48.9; China Caixin NM-PMI. (FXStreet estimates)

Strategy Indicators

Global Stock Markets (US$ Performance) (*link*): The US MSCI index jumped 2.9% last week and improved to 7.7% below its January 23 record high. That compares to a bigger 4.8% gain for the AC World ex-US index to a seven-month high and only 0.7% below its

June 15, 2021 record high. The AC World ex-US MSCI index now has outperformed the US MSCI in 12 of the past 15 weeks. EM Asia was the best performing region last week, with a gain of 4.0%, ahead of EM (3.3%), EAFE (3.1), and the AC World ex-US. EM Latin America was the worst regional performer, with a slight decline of 0.1%, followed by EMEA (1.0), EMU (2.9), and Europe (3.1). The Taiwan MSCI index performed the best among country indexes last week, with a gain of 9.6% out of a correction to 9.9% below its July 11, 2024 record high, followed by Australia (4.7), Hong Kong (3.9), South Africa (3.8), and Switzerland (3.5). The Mexico MSCI index, with a w/w drop of 2.1%, was the only country to decline, followed by small gains for Spain (0.3) and Brazil (0.8). In terms of ytd performance rankings, the US MSCI index remains the second-worst country, with a decline of 3.4%, and trails the 9.6% gain for the AC World ex-US. Among the regional indexes outperforming the AC World ex-US ytd, EMU now leads with a gain of 19.8%, followed by EM Latin America (18.4), Europe (16.0), EAFE (12.1), and the AC World ex-US. EM Asia is the worst ytd performer, albeit with a gain of 3.8%, followed by EM (5.4) and EMEA (8.7). Looking at the major selected country markets that we follow, Spain is the best ytd performer, with a gain of 30.9%, followed by Germany (26.4%), Mexico (20.0), South Africa (18.1), and Brazil (17.7). The worst performing countries ytd: Taiwan (-5.5), the US (-3.4), India (1.4), Japan (4.7), and Hong Kong (5.1).

US Stock Indexes (*link*): All of the 48 major US stock indexes that we follow rose for a second straight week during the week ending May 25. The S&P MidCap 400 Pure Growth index was the best performer with a gain of 5.4%, ahead of S&P 500 LargeCap Pure Growth (4.6%), S&P MidCap 400 Growth (4.4), S&P 500 Transportation (4.4), and Dow Jones 20 Transports (4.3). The S&P 500 LargeCap Pure Value index, with a gain of 1.7%, was the worst performer, followed by Dow Jones 15 Utilities (1.8), Nasdaq Industrials (2.1), S&P 500 LargeCap Value (2.2), and S&P MidCap Pure Value (2.4). Just three of the 48 indexes are higher so far in 2025, down from 47 of 48 rising ytd in mid-February and 46 rising for all of 2024. With a gain of 5.8%, the Dow Jones 15 Utilities is in the top spot as the best performer so far in 2025, ahead of S&P 100 Equal Weighted Total Return (0.9), S&P 100 Equal Weighted (0.2), Russell 1000 Value (0.0), and Russell 3000 Value (-0.5). The worst performing major US stock indexes ytd: S&P 600 SmallCap Pure Value (-15.2), S&P 600 SmallCap Value (-13.5), S&P 600 SmallCap Equal Weighted (-11.5), Dow Jones 20 Transports (-11.4), and S&P 600 SmallCap (-10.7).

S&P 500 Sectors Performance (*link*): Ten of the 11 S&P 500 sectors rose during the week ending May 2, and five were ahead of the S&P 500's 2.9% gain. That compares to 10 of the 11 S&P 500 sectors rising a week earlier when only three sectors were ahead of the S&P 500's 4.6% gain. The outperformers last week: Industrials (4.3%), Communication Services

(4.2), Information Technology (4.0), Financials (3.6), and Real Estate (3.4). The underperformers last week: Energy (-0.7%), Health Care (0.3), Consumer Staples (1.1), Consumer Discretionary (1.6), Utilities (1.9), and Materials (2.8). The S&P 500 is down 3.3% ytd; but eight of the 11 sectors are ahead of the index, and only four of the 11 are in the red. Consumer Staples still wears the crown as the best ytd performer, with a gain of 5.5%, ahead of Utilities (5.2), Financials (2.9), Real Estate (2.8), Industrials (2.1), Materials (1.2), Health Care (0.6), and Communication Services (-2.2). These three sectors continued to lag the S&P 500 so far in 2025: Consumer Discretionary (-12.4), Information Technology (-8.4), and Energy (-4.1).

US Economic Indicators

Employment (*link*): Employment blew past expectations again in April, though there were downward revisions to the prior two months. *Payroll employment* jumped 177,000 in April, above the 138,000 expected gain, while revisions show both March (to 185,000 from 228,000) and February (102,000 from 117,000) payrolls were revised lower, for a net loss of 58,000. *Private payroll* employment climbed 167,000 in April, slowing slightly from March's gain of 170,000, with the *service-providing* sector adding 156,000 to payrolls last month, following 161,000 in March, and the *goods-producing* sector adding 11,000 jobs, a slight uptick from March's 9,000 gain. *Within service-producing industries*, once again *health care* led the pack, adding 51,000 in April—in line with the average monthly gain of 52,000 over the prior 12 months—with hospitals (22,000) and ambulatory health care services (21,000) once again leading the gains in this sector. *Transportation & warehousing* employment increased 29,000 in April, an acceleration from March's 3,000 increase and considerably stronger than the average monthly gain of 12,000 over the prior 12 months. *Financial activities* employment continued to trend higher, increasing 14,000, adding 103,000 jobs since its trough last April. *Social assistance* jobs is also trending higher, but at a slower pace, adding 8,000 jobs last month, slowing from the average monthly gain of 20,000 the prior 12 months. *Federal government* jobs continued to fall, dropping 9,000 in April—and is down 26,000 since January. *Within goods-producing industries*, jobs climbed 11,000, with *construction* (11,000) leading the gain, while *durable goods manufacturing* and *mining & logging* added 2,000 and 1,000 to payrolls, respectively; *nondurable goods manufacturing* jobs fell 3,000. Meanwhile, *government* jobs rose 10,000, led by a 13,000 gain in local government employment; federal government employment fell again in April, dropping 9,000.

Wages (*link*): Average hourly earnings (AHE) for *all workers on private payrolls* increased

0.2% in April, while the three-month rate increased 2.6% (saar), more than a percentage point below the yearly rate of 3.8%, which matched March's gain. The yearly rate was below 4.0% for the fourth straight month. April's yearly rate is down from November's 4.2%; it was at 3.6% last July, which was the lowest since May 2021. *Service-providing industries showing three-month rates above their yearly rates*: retail trade (7.0% & 4.5% y/y), wholesale trade (5.6 & 2.5), financial services (5.3 & 4.3), and transportation & warehousing (4.1 & 3.0). *Service-providing industries showing three-month rates below their yearly rates:* utilities (-2.2% & 2.0% y/y), other services (-1.8 & 2.9), education & health services (0.6 & 3.3), professional & business services (2.0 & 4.4), and information services (3.8 & 5.2). Within *goods-producing* industries, the annualized three-month rate was just below the yearly rate for *durable goods* manufacturing (4.6 & 4.9), while the three-month rate for *nondurable goods* manufacturing (2.4 & 3.3) was roughly a percentage point below the yearly rate.

Earned Income Proxy (*link*): Our Earned Income Proxy (EIP), which tracks consumer incomes and spending closely, climbed to yet another a new record high in April, increasing 0.3%. *Average hourly earnings* in April advanced 0.2%, while *aggregate weekly hours* edged up 0.1%—with private payroll employment up 0.1% and the average workweek flat. Over the past 12 months, our EIP advanced 5.3%—with aggregate weekly hours up 1.5% and average hourly earnings up 3.8%.

Unemployment (*link*): The *number of unemployed* rose 82,000 in April to 7.16 million, with the *unemployment rate* holding at 4.2%—remaining in a narrow range from 4.0% to 4.2% since last May. *Household employment* rose 436,000 last month, while the *labor force* was 518,000 higher. The *participation rate* edged for the second month to 62.6% in April from 62.4% in February—which was the lowest since January 2023. *By race:* The unemployment rates in April fell for Asians (to 3.0% from 3.5%), while they ticked up by 0.1ppt for Whites (to 3.8%), Hispanics (5.2), and African Americans (6.3). *By education:* Unemployment rates rose in April for those with less than a high-school diploma (to 6.2% from 5.8%) and some college or an associate's degree (3.7 from 3.5), while ticked down for those with high-school degrees (4.0 from 4.1) and those with a bachelor's degree or higher (2.5 from 2.6).

US Manufacturing PMI (*link*): The ISM M-PMI contracted for the second straight month in April after expanding the first two months of the year. April's *M-PMI* dipped from 50.3 in February to 49.0 in March and a five-month low of 48.7 in April; the M-PMI was at 50.9 at the start of this year. It was at a recent low of 46.9 in October—which was the lowest level since December 2023. According to ISM, the *overall economy* continued its expansion for the 60th month after a one-month contraction in April 2020. (A manufacturing PMI above 42.5 over a period of time generally indicates an expansion of the overall economy.) *New orders* (to 47.2 from 45.2) contracted for the third successive month, following three straight months of expansion, though April's measure showed it fell at a slower pace than during March, which was the weakest reading since May 2023. Meanwhile, the *production* (44.0 from 48.3) measure showed a sharp contraction during April, down from a recent peak of 52.5 during January. April's reading was the weakest since May 2020. Prior to January's 52.5 reading, this measure was in contraction territory, below 50.0, for eight straight months. *Inventories* (50.8 from 53.4) accumulated at a slower pace last month, while *suppliers' deliveries* (55.2 from 53.5) continued to show a slowing in deliveries (a reading above 50 indicates slower deliveries). The employment (46.5 from 44.7) measure showed jobs fell at a slower pace last month. Meanwhile, *prices* (69.8 to 69.5) continued to accelerate at a fast pace due to tariffs.

Construction Spending (*link*): Construction spending unexpectedly fell in March, on widespread declines. *Total construction* spending dropped 0.5% in March versus the consensus estimate of a 0.2% gain, while February's increase was revised down to 0.6%, initially reported as a 0.7% advance. *Private construction* investment declined 0.6%, with both nonresidential (-0.8%) and residential (-0.4) investment reporting declines during the month. Investment in *nonresidential* construction was led by declines in religious (-2.9%), health care (-2.2), office (-1.8), educational (-1.7), lodging (-1.6), and commercial (-1.0) building. Meanwhile, residential construction spending on new single-family projects ticked up 0.1%. *Versus a year ago*, total construction spending was 2.8% above a year ago, with private construction investment up 2.3% and with both residential (2.8) and nonresidential (1.6) above year-ago levels. Meanwhile, public construction building slipped 0.2% last month, led by declines in power (-4.8), commercial (-1.6), and amusement & recreation (-1.0) facilities. Public construction investment, however, was 4.7% above a year ago.

Auto Sales (*link*): *Motor vehicle* sales slipped in April to 17.3 million units (saar), after climbing from 15.5 million in January to 17.8 million in March—which was the highest reading since April 2021. April sales were well above the consensus estimate of 15.7 million. Over the two months through April, sales averaged 17.6 million units, largely driven by tariff-related buying. *Light-truck* sales ticked down to 14.4 million units, from March's 14.7 million units, though were up 13.5% since the start of this year. Meanwhile, car sales ticked down to 2.9 million units in April from 3.2 million in March, remaining in a flat trend around 3.0 million.

Global Economic Indicators

Global Manufacturing PMIs (*link*): "Global PMI falls into contraction territory as new orders decline and global trade worsens" was the headline of the April report. The *JP Morgan Global M-PMI* (to 49.8 from 50.3) fell back below the breakeven point of 50.0 for the first time in four months, though the rate of decline was marginal. Three of the five PMI components—new orders, employment, and stocks of purchases—were in contraction territory, while output and supplier delivery times both improved during the month. Of the 28 countries for which PMI *new export* data were available for April, all except Germany, India, and Greece saw new export business decline—with the US, Canada, and Mexico particularly hard hit. *Production* expanded for the fourth straight month, though remained weak. *By country*, India, Ireland, and the Philippines saw the greatest increases in production, while China and the Eurozone also recorded gains. Meanwhile, the US and Japan were two of the larger countries in contraction territory. *By sector*, both consumer and intermediate goods production climbed last month, while investment goods were unchanged. *New business* declined for the first time in four months in April, with new exports orders posting its steepest decline since 2023 on widespread declines in consumer, intermediate, and investment goods. Meanwhile, *business optimism* sank to its lowest level since October 2022, reflecting concerns about tariff and protectionism—with manufacturing sentiment not far off lows seen in 2019—when these concerns were also on the rise. *Turning to prices*, average purchase prices continued to accelerate, while output change inflation hit a 25-month high.

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, 732-241-6502
Melissa Tagg, Senior Global Investment Strategist, 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