Yardeni Research

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Morning Briefing

Earings & Valuation Under Trump 2.0 So Far

Check out the accompanying chart collection.

Executive Summary: Even though Q1 earnings were fabulous, most economists, industry analysts, and corporate managements have low hopes that Trump's Tariff Turmoil won't dunk the US economy into a recession this year. Not us: We're counting on the economy's resilience. Today, Dr Ed discusses why the widely expected recession, like others in recent years, will be a no-show. Hard-to-ignore reasons include record-high forward earnings, strong economic indicators, and a forward P/E that hasn't plunged as happens when a recession is imminent. Stock investors seem to be in our camp. Moreover, Trump's tariff overreach is bound to be tempered by the courts and mid-term election realities if nothing else. … Also: Dr Ed reviews "How To Make Millions Before Grandma Dies" (++).

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*.

Strategy I: Recession Forecasts Still in Fashion. Once again, economists are debating the odds of a near-term recession. They've done so over much of the past three years. Most of them reckoned that the tightening of monetary policy, the fall in the Index of Leading Economic Indicators, and the inverting yield curve all meant that a recession was all but inevitable. They were wrong. All along, we counted on the underlying resilience of the US economy to keep GDP growing apace. That worked out well for us.

Here we go again. This year, the naysayers are convinced that Trump's Tariff Turmoil (TTT) will cause a recession during the second half of this year. We are still betting on the resilience of the economy. We've also been betting that Trump will blink and unilaterally deescalate his one-man Tariff Man trade war. So far, so good. Mounting concerns among Republicans that they could lose their majorities in both houses of Congress if TTT causes a recession undoubtedly have softened Trump's stance.

In addition, we anticipated that several court cases would challenge Trump's constitutional authority to impose tariffs. Our good friend Jim Lucier of *Capital Alpha Partners* observes: “The first showdown in court over President Donald Trump’s IEEPA tariffs is coming Tuesday, May 13, at 11 AM ET. The Court of International Trade (CIT) in New York City will hold a hearing on all pending motions in one of four pending challenges to IEEPA in that court. The case brought by the Liberty Justice Center on behalf of small business plaintiffs is *V.O.S. Selections, Inc. et al. v Trump et al.* None other than Trump’s former U.S. Trade Representative Robert Lighthizer said at the Council on Foreign Relations in New York on April 28 that ‘there is a reasonable chance the CIT will enjoin’ Trump’s IEEPA tariffs (See video *here*, minute 49:00).”

Here is what we wrote on April 7: “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.”

The S&P 500’s 18.9% correction since February 19 troughed on April 8; the next day, Trump postponed his April 2 Liberation Day reciprocal tariffs. The S&P 500 closed up 9.5% that day, April 9 (*Fig. 1*). It is now up 13.6% since the trough and only 7.9% below its record high!

The April 17 *WSJ* *reviewed* the latest quarter survey of economists’ forecasts. It was conducted from April 4 to April 8, just before Trump postponed his Liberation Day tariffs. Economists raised the probability of a recession in the next 12 months to 45% from 20%. They expect the unemployment rate to reach 4.7% by December and remain around there into 2026.

The May 3 *WSJ* featured a *story* titled “What Recession? Stock Investors Expect the Good Times to Continue.” It noted: “Wall Street’s best forecasters have been warning that tariffs could spark a recession. Goldman Sachs puts the chances at 45% in the next 12 months. Apollo Global Management’s top economist recently pegged it at 90%.” BCA also remains solidly in the recession camp.

We lowered our odds of a recession from 45% to 35% on May 4. We did so because Trump continued to moderate his stance on tariffs. In addition, the labor market has remained impressively resilient. We are also less concerned about a negative wealth effect on consumer spending now that the stock market has rebounded significantly. Additionally, we expect that capital spending related to datacenters for cloud computing and the onshoring of manufacturing will remain robust.

Consider the following:

(1) Last week's batch of economic indicators lowered the odds of a recession, according to Polymarkets.com, to 51% on Friday from a peak of 66% on May 1 (*Fig. 2*). Meanwhile, the Citigroup Economic Surprise Index for the US has been only slightly negative since April 29 (*Fig. 3*).

(2) This week, a bunch of soft and hard economic indicators will be released, mostly for April. The soft indicators include data on small business owners' concerns and expectations from the National Federation of Independent Business' (NFIB) survey of its members. The main hard ones will be retail sales, industrial production, housing starts, and jobless claims.

The NFIB's Small Business Optimism Index (SBOI) dropped sharply in March (*Fig. 4*). It might have ticked up in April in response to the 90-day postponement of Trump's reciprocal tariffs. Then again, the tariffs on China remain prohibitive and undoubtedly depressed sentiment among small business owners who import lots of merchandise from China. We will be watching the SBOI as well as the NFIB data on small business job openings and hiring plans (*Fig. 5*).

(3) May's regional business surveys conducted by the Federal Reserve district banks of New York and Philadelphia will also be released this week. They probably remained depressed in May but less so than in April, which was the height of TTT (*Fig. 6*).

(4) Perhaps the most important report this coming week will be the one for April's retail sales. It's unlikely to show that consumers are retrenching in response to TTT. More likely is that it will be boosted by lots of buying in advance of tariff-related price increases. The Redbook Retail Sales Index rose 6.9% y/y through the May 2 week (*Fig. 7*). The labor market also remains resilient, as confirmed by the latest weekly report for unemployment claims (*Fig. 8*).

Strategy II: Earnings Under Trump 2.0. Industry analysts must finally have received the tariff-recession memo. In recent weeks, they've been slashing their estimates for S&P 500 companies' operating earnings per share (EPS) for the final three quarters of 2025 (*Fig. 9*). That's despite Q1's big earnings beat.

At the start of the latest earnings reporting season, the analysts collectively expected a 6.0% y/y increase in S&P 500 companies' aggregate EPS for Q1. As of the May 8 week, after 90% of the S&P 500 companies had reported Q1 results, the blended estimated/actual growth rate was up to 11.2% y/y. With Q1 growth nearly double the analysts' initial expectations as reporting began, this was far from a weak quarter. Obviously, it was what company managements said on the conference calls that caused analysts to take paring knives to their estimates for the rest of this year; and obviously, it was Trump's Liberation Day shocker that festered rampant uncertainty and pessimism among managements.

As a result, the analysts' 2025 and 2026 EPS estimates were revised down since the start of the year through the May 8 week by about $10 each to $265 and $300 (*Fig. 10*). (We are still estimating $260 and $300.)

S&P 500 forward operating earnings—which is the time-weighted average of analysts' consensus EPS expectations for 2025 and 2026—rose to a record high of $279.13 on April 3. It has been hovering around that level since then, as of the May 8 week. It will converge toward the 2026 analysts' consensus EPS over the rest of the year, as forward EPS by definition do. So despite the downward revisions of analysts' quarterly and annual EPS consensus estimates, there's is no evidence so far of a recession in S&P 500 forward earnings, which tends to fall sharply during economic downturns.

By the way, Joe reports that on a proforma basis, which assumes the S&P 500's current members were also in the index a year earlier, Q1 earnings is up by 14.1% (*Fig. 11*). Excluding the S&P 500 Energy sector, which has been depressed by falling oil prices, S&P 500 proforma Q1 EPS was up 16.1% y/y through the May 9 week (*Fig. 12*).

Bloomberg's Lu Wang reports that 21 of Wall Street's investment strategists predicted in April that S&P 500 EPS will be $261 this year on average, with the median forecast at $257 (*Fig. 13*). At the end of last year, they were projecting $269 on average, with the median at $271 (*Fig. 14*). (We then were at $285.)

According to Bloomberg, Wall Street's strategists predicted in April that the S&P 500 will end the year at 6,047 on average (*Fig. 15*). We remain at 6000.

Strategy III: Valuation Under Trump 2.0. As noted above, forward earnings expectations remain remarkably resilient notwithstanding widespread fears of a recession. The same can be said of valuation multiples.

The S&P 500's forward P/E (i.e., the multiple using forward earnings as the "E") fell from about 22 at the start of this year to 18 on April 8 (*Fig. 16*). Now it is back a bit above 20. Leading the way down in the S&P 500's correction was a sharp drop in the forward P/E of the Magnificent-7 stocks from 31 to 22. It is now back at 25.

Usually in recessions, the forward P/E of the S&P 500 falls into the single digits. It hasn't done so this time because the stock market isn't pricing in a recession. Neither are industry analysts, according to their latest EPS estimates.

During the previous bear market, the forward P/E bottomed at 15.1 on October 22, 2022. That too was a relatively high P/E and occurred because the most widely anticipated recession of all times was a no-show. History may already be repeating itself in the performance of the stock market and the economy so far this year.

Movie. "How To Make Millions Before Grandma Dies" (+ +) is a 2024 Thai comedy drama about life and death and families. Mengju is the mother of three adult children. She is diagnosed with late-stage colorectal cancer. Her three children suddenly come to visit her more often now that they are thinking about their inheritance. Her grandson, a university dropout, moves in with her to curry favor. The cast does a great job of portraying a contentious family that is probably similar to many other families with mixed emotions regarding their immediate relatives. (See our movie reviews *archive*.)

Calendars

US: Mon: US Federal Budget $256b; Loan Officer Survey; Kugler. **Tues:** Headline & Core CPI 0.3%m/m, 2.3%y/y & 0.3%m/m, 2.8%y/y; NFIB Small Business Optimism Index 95.0. (FXStreet estimates)

Global: Mon: Eurogroup Meeting; Lombardelli; Green; Mann; Taylor; Buch. **Tues:** Germany ZEW Economic Sentiment 9.8; UK Average Hourly Earnings Index Plus Bonus 5.2%; UK Claimant Count 22.3k; UK Unemployment Rate 4.5%; Japan PPI 0.2%m/m, 4.0%y/y; Pill; ECOFIN Meetings; Balz; Bailey. (FXStreet estimates)

Strategy Indicators

Global Stock Markets (US$ Performance) (*link*): The US MSCI index fell 0.4% last week, and weakened to 8.1% below its January 23 record high. That compares to a slight decline of less than 0.1% for the AC World ex-US index, which remains just 0.7% below its June 15, 2021 record high. The US MSCI has outperformed the AC World ex-US in just three of the past 16 weeks. EM Latin America was the best performing region last week, with a gain of 1.5%, ahead of EM (0.5%), EM Asia (0.4), EMEA (0.2), and the AC World ex-US. Europe was the worst regional performer, with a decline of 0.7%, followed by EAFE (-0.2) and EMU (-0.2). The Hong Kong MSCI index performed the best among country indexes last week, with a gain of 3.8%, followed by Taiwan (3.1), Mexico (1.7), and Brazil (1.4). The India MSCI index was the worst performer w/w with a drop of 2.5%, followed by Switzerland (-1.7), Australia (-1.6), France (-1.3), and Sweden (-1.0). In terms of ytd performance rankings, the US MSCI index is now the worst country, with a decline of 3.8%, and trails the 9.6% gain for the AC World ex-US. Among the regional indexes outperforming the AC World ex-US ytd, EM Latin America now leads with a gain of 20.2%, followed by EMU (19.6), Europe (15.2), EAFE (11.9), and the AC World ex-US. EM Asia is the worst ytd performer, albeit with a gain of 4.2%, followed by EM (5.9) and EMEA (8.9). Looking at the major selected country markets that we follow, Spain is the best ytd performer, with a gain of 31.0%, followed by Germany (26.3%), Mexico (22.0), Brazil (17.7), and South Africa (19.0). The worst performing countries ytd: the US (-3.8), Taiwan (-2.5), India (-1.2), Australis (3.7), and Japan (5.6).

US Stock Indexes (*link*): Twenty-three of the 48 major US stock indexes that we follow rose during the week ending May 9, down from all 48 indexes rising in the prior two weeks. The S&P MidCap 400 Pure Value and Nasdaq Industrials indexes were the best performers, with gains of 1.3%, ahead of S&P SmallCap 600 Pure Value (1.0%), Russell MidCap Growth (0.9%), and Russell MidCap (3.0). The Dow Jones 15 Utilities index, with a decline of 0.8%, was the worst performer, followed by S&P 100 (-0.7), Russell 1000 Growth (-0.6), Nasdaq Industrial (-0.6), Russell 3000 Growth (-0.6), and S&P 500 LargeCap Growth (-0.6). Just two 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 5.0%, 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 (0.7), Russell 1000 Value (0.0), S&P 100 Equal Weighted (-0.1), and S&P 500 LargeCap Pure Value (-0.2). The worst performing major US stock indexes ytd: S&P 600 SmallCap Pure Value (-14.4), S&P 600 SmallCap Value (-12.9), Dow Jones 20 Transports (-11.7), S&P 600 SmallCap Equal Weighted (-11.1), and S&P 600 SmallCap (-10.2).

S&P 500 Sectors Performance (*link*): Six of the 11 S&P 500 sectors rose during the week ending May 9, and seven were ahead of the S&P 500's 0.5% decline. That compares to 10 of the 11 S&P 500 sectors rising a week earlier, when five sectors were ahead of the S&P 500's 2.9% gain. The outperformers last week: Industrials (1.1%), Consumer Discretionary (0.8), Utilities (0.5), Energy (0.4), Information Technology (0.3), Financials (0.1), and Materials (-0.4). The underperformers last week: Health Care (-4.3%), Communication Services (-2.4), Consumer Staples (-1.0), and Real Estate (-0.8). The S&P 500 is down 3.8% ytd, but six of the 11 sectors are positive ytd and eight are ahead of the index. Utilities now wears the crown as the best ytd performer, with a gain of 5.8%, ahead of Consumer Staples (4.4), Industrials (3.2), Financials (3.0), Real Estate (2.0), Materials (0.8), Energy (-3.7), and Health Care (3.7). These three sectors continued to lag the S&P 500 so far in 2025: Consumer Discretionary (-11.7), Information Technology (-8.2), and Communication Services (-4.5).

US Economic Indicators

Productivity & Labor Costs (*link*): Productivity during the first quarter posted its first decline since Q2-2022, not surprising following GDP's Q1 loss of 0.3%—the first decline in three years—while manufacturing productivity posted its strongest quarter since Q1-2021. *Nonfarm productivity* fell 0.8% (saar), reflecting a 0.3% decline in output and a 0.6% increase in hours worked. Meanwhile, *manufacturing* productivity jumped an impressive 4.5% (saar), with output leaping 5.1% and hours worked rising 0.5%. Within manufacturing, durable goods productivity soared 7.1%, with output up 7.9% and hours worked up 0.8%, while nondurable goods productivity rose 2.2%—with output advancing 2.3% and hours worked barely budging, ticking up 0.1%. *Turning to unit labor costs*, the *nonfarm sector* saw a 5.7% (saar) jump during Q1, reflecting a 4.8% rise in hourly compensation and a 0.9% decline in productivity. Versus a year ago, it was up 1.3%, slowing from 3.4% during Q1-2024. *Manufacturing* unit labor costs climbed 1.6% (saar) during Q1, with hourly comp rising 6.2% and productivity rising 4.5%. Unit labor costs were only 0.7% above a year ago.

Global Economic Indicators

Germany Industrial Production (*link*): German industrial production in March was a surprise on the upside, ahead of Trump tariffs. Industrial production, which includes construction, rebounded 3.0%, considerably above consensus expectations of a 0.8% gain, and the largest monthly gain increase October 2021. It followed February's 1.3% shortfall. *By industry*, leading March gains were advances in output in the pharmaceutical (19.6%), auto (8.1), and machinery & equipment (4.4) industries, with construction (2.1) also contributing. *By sector*, there were widespread gains, with both consumer and capital good output jumping 4.9% during the month, while intermediate goods production also rose, but by a smaller 1.1%. Industrial production during Q1 expanded 1.4%, the largest quarterly gain since Q1-2022, while output versus a year ago was basically flat, ticking up 0.2%.

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