Yardeni Research

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Morning Briefing

On Japan, Australia & Earnings

Check out the accompanying chart collection.

Executive Summary: Japan is at an economically precarious time, William reports. GDP is barely growing, yet the BOJ is bent on monetary tightening. A new prime minister is likely to roll out fiscal stimulus measures, but Japan has the heaviest debt of any developed nation; the prospect of fiscal loosening has already roused the Bond Vigilantes. Might Trump renegotiate Japan's trade deal? … Also: Australia's productivity growth problem can't be solved by monetary policy; what's needed are government leaders willing to make bold fiscal reforms. But reformist energy is in short supply in Canberra. … And: Q3 estimate revisions data for S&P 500 companies suggest to Joe yet another quarter of impressive y/y growth.

Japan's Economy I: Tariffs Hitting at Delicate Moment. For Japan, the Trump 2.0 era is beginning to look a lot like Trump 1.0 as its economy finds itself in the center of the collateral damage blast zone.

It's taken a while for President Donald Trump's tariff campaign to catch up with Japan. August may have been the month it did, as industrial production *dropped 1.2% m/m*, the same decline seen in July.

With sizable declines reported in metal products and electronic machinery, many of which typically go to China, there is little doubt that caution is rising among Japan's manufacturers. Retail sales, meanwhile, *fell 1.1% m/m* in August, the flip side of forecasts for a 1.2% increase. Leading the declines were cars, fuel, and online commerce.

Let's consider the possible ripple effects from slowing growth:

(1) *Japan barely growing*. Already, the government expects Japan to *grow just 0.7% y/y* this fiscal year. The timing of this latest downshift is delicate for several reasons. One is the Bank of Japan's (BOJ) determination to continue raising interest rates. Figures like those released on Tuesday make BOJ Governor Kazuo Ueda's window for action even smaller.

(2) *Added election drama.* The Liberal Democratic Party will choose a new prime minister on *October 4* to replace the outgoing Shigeru Ishiba. These figures will add to pressure on frontrunners Shinjiro Koizumi and Sanae Takaichi to outdo each other with plans to roll out new support measures.

That, of course, could run afoul of the Bond Vigilantes, who are already nervous about talk of tax cuts. As it is, Japan has the biggest public debt load among developed nations. Concerns about fiscal loosening recently sent 10-year Japanese government bond yields to their *highest level* since 1999.

Japan's Economy II: Talk of US Trade Deal Redo. Many investors worry about how these various tensions might intersect. Polls show that *in the lead* is Agriculture Minister Koizumi, 44, son of 2001-06 Prime Minister Junichiro Koizumi. He's thought to be a *moderate* on economic issues.

Here's more:

(1) *Trade rethink?* Former Economic Security Minister Takaichi, 64, may have given her campaign a second wind by signaling a willingness to demand a renegotiation of the US-Japan tariff deal. The *15% tariff* is one thing, but the $550 billion "*signing bonus*" that Trump wants in cash is irking hardline conservatives like Takaichi.

On September 28, Takaichi told Fuji TV that: "We must stand our ground if *anything unfair* that is not in Japan's interests comes to light in the process of implementing the deal. That includes a potential renegotiation."

(2) *How Trump might react*. Along with Trump's "signing bonus" talk, Nagatacho, Japan's Capitol Hill, buzzed with shock over trade adviser Peter Navarro bragging that Trump was getting a "*blank check*" from Tokyo. Commerce Secretary Howard Lutnick termed the $550 billion payroll a "national security sovereign fund."

South Korea has decided it can't hand over the $350 billion that Trump World is demanding—equivalent to 80% of Seoul's foreign exchange reserves. The question is: Might all this have Trump tearing up the tariff deals and slapping bigger levies on Japan and Korea?

Japan Inc. is likely to find itself in harm's way regardless of how the US reacts.

Australian Economy I: Productivity 'Crisis.' After cutting rates three times this year, the Reserve Bank of Australia (RBA) held steady on Tuesday, arguing that it needs time to assess the global outlook. Yet the real message seemed to be aimed at government officials in Canberra: Your move, folks.

Last week, RBA Governor Michele Bullock *said* the *$1.7 trillion economy* is "in a good position," enjoying "pretty strong labor markets still and inflation is back in the band" between *2.0% and 3.0%*. Like the Federal Reserve, the RBA has a *dual mandate* of price stability and full employment.

Following Tuesday's decision to leave the benchmark at 3.6%, Bullock said that when it comes to the balance of risks, it "*is all really good, positive news*." With the next RBA move anyone's guess, S&P/ASX 200 stocks ended Tuesday *little changed* at 8,848.

One reason Australia matters is that it often serves as a weathervane for shifts in global trade dynamics. Its sizable, open, and Asia-reliant economy is as good an early warning system as the West has nowadays. At the moment, it's flashing cautious optimism as *US tariffs* hit key trading nations, particularly China, Japan, and South Korea.

Yet the RBA has an even bigger challenge at home: economic complacency that's catching up with the nation's *27 million people*.

Let's look at what's holding Australia back and what it means for the global economy:

(1) *Productivity fail*. The hot debate in Australian economics is whether a productivity crisis is afoot and how to address it.

Sky News on August 13 asked Australian Treasurer Jim Chalmers directly whether productivity was in crisis. Chalmers denied that the productivity problem is a crisis but called it "a *big challenge* that we're confronting together," before changing the subject: "Let's not skip lightly over the very welcome news yesterday that interest rates have been cut for the third time in six months and that means very meaningful relief for millions of Australians" and "more money in the pockets of people who are under pressure."

In short, Canberra officials aren't confronting the problem, even as China's rise accelerates the economic clock for Group of 20 nations. They include Chalmers' boss, Prime Minister Anthony Albanese, who since May 2022 has done little to raise Australia's competitive game.

If not a crisis, the failure by a succession of governments to increase the efficiency of the workforce is a self-inflicted wound that's festering.

(2) *Passing the buck*. Since at least Tony Abbott's time as prime minister (2013-15), every government has discussed the productivity challenge and passed it on to the next one. Over 2013-23, says Australia Institute's Jim Stanford, the nation's average productivity growth was 0.39%, *ranking 29th* out of 37 Organisation for Economic Co-operation and Development countries reporting data.

(3) *Weak investment*. Oxford Economics in an *August report* discussed Australia's "stalled" productivity growth: "[O]utput per hour worked is barely higher than in 2017, with productivity growth far below the pace of the late 1990s and early 2010s."

Australia's productivity problem, Oxford explained, "is multifaceted. Sustained weakness in business investment has prevented workers from getting the tools they need. At the same time, technological gains have slowed. Workforce changes are also at play, with the *non-market sector* becoming a larger part of the economy in recent years."

Australian Economy II: Reformist Energy in Short Supply. What's needed is not just a return to the drawing board but a look back at not-so-distant Australian history when leaders did big things. It's now time to increase competitiveness, incentivize innovation, and recalibrate tax policies.

Consider the following:

(1) *Reformist heyday*. Every government since the early 1990s has let the RBA take the lead on economic issues, instead tending to its various pet issues. Prior to the early 1990s was a period of economic retooling under *former prime ministers Bob Hawke and Paul Keating*. From 1983-96, they scrapped import tariffs, allowed the dollar to trade freely, opened the financial industry to global competition, and built a compulsory national pension program.

Australia needs to rekindle the reformist energy that transformed a geographically remote nation into a global financial center. Albanese and Chalmers can start by raising the nation's productivity ranking.

(2) *Time of rapid change*. Complacency during a time of rapid change makes the challenge more daunting each year, says Shane Oliver at financial giant AMP. As *Oliver sees* it: "A

surging population over the last 20 years with inadequate infrastructure and housing supply has led to urban congestion and poor housing affordability, which contribute to poor productivity growth—notably via increased transport costs and speculative activity around housing diverting resources from more productive uses."

The RBA can only do so much to keep Australia in a "good place." It's now the government's turn.

Strategy: A Ninth Straight Quarter of Earnings Growth! Here we are in the final week of a quarter, when steep declines in industry analysts' estimates are typical. Yet the Q3 "earnings warning season" has been atypically quiet, just as it was during Q2. Then, analysts stood pat during what's also called "confession season," having over-cut estimates when management guidance was absent during Trump's Tariff Turmoil. Might the lack of cutting now presage a Q3 earnings surprise better than Q2's?

The consensus proforma Q3 earnings growth forecast for S&P 500 companies in aggregate began the quarter at 8.0% y/y and actually improved to 8.8% as of the September 26 week (*Fig. 1*). That's highly unusual. Since we began tracking the consensus quarterly data in 1994, earnings forecasts have ended the quarter higher during just 22 of those 126 quarters, or less than 20% of the time.

We expect the typical earnings surprise "hook"—i.e., the sudden uptick in the charted estimates data once actual results are tacked on—to peg Q3-2025's final y/y growth at a double-digit percentage rate for a fourth straight quarter. That would also mark the S&P 500's ninth straight quarter of positive y/y earnings gains, the longest such stretch since the 12 quarters ended Q2-2019.

While weaker-than-double-digit y/y earnings growth—and even y/y declines—are forecast for some of the S&P 500 sectors, y/y revenues growth prospects remain broad across the sectors, Joe reports.

Here are more of Joe's takeaways from the latest estimates data:

(1) *Broad sector revenue growth expected again in Q3.* Ten of the 11 S&P 500 sectors' revenues should grow y/y in Q3, unchanged from Q2's count and a slight improvement from nine sectors in Q1 (*Fig. 2*). That's also the highest count since Q3-2022 and is hardly indicative of a revenues recession.

Information Technology has been leading all sectors in revenues growth since Q1-2024; its Q3-2025 revenues should rise 14.8% y/y, a double-digit rate for a sixth straight quarter. Also notable: Materials' expected 4.5% y/y revenue gain would be only its second in 12 quarters. Only Energy's revenues are forecast to drop in Q3, albeit just 1.9% y/y.

Here are the sectors' proforma y/y revenues growth forecasts for Q3-2025: Information Technology (14.8%), Health Care (7.9), Communication Services (7.1), S&P 500 ex-Energy (6.4), Real Estate (6.3), Utilities (5.9), S&P 500 (5.7), Materials (4.5), Industrials (4.4), Consumer Discretionary (3.8), Financials (3.4), Consumer Staples (2.8), and Energy (-1.9).

(2) *Earnings growth less broad for the 11 sectors.* Only seven of the 11 S&P 500 sectors are expected to grow earnings y/y in Q3-2025. That's down from eight sectors during H1-2025 and a whopping ten in Q4-2024, which was the most since Q1-2021. However, we think all 11 sectors could post positive y/y earnings growth following their earnings surprise hooks. That hasn't happened since Q2- and Q3-2021, when the US economy was reopening after Covid lockdowns.

Among the four lagging sectors, Consumer Discretionary's earnings is expected to fall y/y in Q3 for the first time in 11 quarters; Consumer Staples' is expected to fall for a second time this year; Energy's is expected to fall for a fifth straight quarter; and Utilities is expected to drop for a second quarter following eight straight gains.

Among the seven sectors expected to post earnings growth in Q2, five are expected to grow faster than the S&P 500 and at a double-digit percentage rate to boot.

Here's how the S&P 500 sectors' consensus earnings growth rates stack up for Q3-2025: Information Technology (22.2%), Real Estate (18.4), Industrials (15.1), Materials (14.1), Financials (12.3), S&P 500 ex-Energy (9.6), S&P 500 (8.8), Communication Services (5.3), Health Care (0.1), Consumer Discretionary (-1.1), Consumer Staples (-2.5), Utilities (-3.2), and Energy (-5.1).

Here are their y/y revenues and earnings growth forecasts: Communication Services (6.0% revenues growth, 5.3% earnings growth), Consumer Discretionary (3.8, -1.1), Consumer Staples (2.8, -2.5), Energy (-1.9, -5.1), Financials (3.4, 12.3), Health Care (7.9, 0.1), Industrials (4.4, 15.1), Information Technology (14.8, 22.2), Materials (4.5, 14.1), Real Estate (6.3, 18.4), S&P 500 (5.7, 8.8), S&P 500 ex-Energy (6.4, 9.6), and Utilities (5.9, -3.2).

Calendars

US: Wed: ADP Employment Change 50k; MBA Mortgage Applications; Atlanta Fed GDPNow 3.9%. **Thurs:** Initial Claims 22,000; Factory Orders 1.4%; Motor Vehicle Sales 16.2mu; Logan. (Source: FX Street)

Global: Wed: Eurozone, Germany, France, Italy & Spain M-PMI 49.5, 48.5, 48.1, 50.0 & 54.0; UK M-PMI 46.2; Eurozone & Core Harmonized CPI 2.2% & 2.3%y/y; UK House Prices 0.2%; De Guindos; Elderson. **Thurs:** Eurozone Unemployment Rate 6.2%; Italy Unemployment Rate 6.0%; Spain Unemployment Change 8.4k; Japan Consumer Confidence 35.2; De Guindos. (Source: FX Street)

US Economic Indicators

Consumer Confidence (*link*): Consumer confidence sank to a five-month low in September, as consumers felt the strain from both new tariffs and rising prices. *Headline consumer confidence* fell for the second month, from 98.7 in July to 94.2 in September; it was at 112.8 last November. The *present situation* component dropped for the fourth consecutive month, from 135.5 in May to 125.4 in September, while *expectations* slipped for the second month to 73.4 in September, after climbing from 55.4 in April to 76.0 in July. Expectations have been below the threshold of 80 that typically signals a recession ahead since February of this year. Consumers' assessments of *current business conditions* deteriorated in September, with 19.5% of consumers saying business conditions were good, down from 21.8% in August, while 15.4% said they were bad, up from 14.6% in August. Consumers remained concerned about the labor market, with 26.9% of consumers saying jobs were plentiful, down from 30.2% in August, while 19.1% said jobs were hard to get, the same as in August. Consumers were a bit more pessimistic about *future business conditions* in September, with 18.7% expecting conditions to improve, down from 20.2% in August, while 22.3% expected business conditions to deteriorate, down from 23.5% in August. Consumers' outlook for the *labor market in six months* cooled further in September, with 16.1% of consumers expecting more jobs to be available, down from 17.9% in August, while 25.6% anticipated fewer jobs, a couple of ticks below July's 25.9%.

JOLTS (*link*): The number of job openings was unchanged at 7.2 million in August, while both hires and total separations were little changed at 5.1 million. *Private industry* job openings rose 56,000, while government job openings fell 37,000, with federal down 61,000 and state & local government up 25,000. *By industry*, accommodation & food services (+106,000) posted the most job openings in September, followed by health care & social assistance (+81,000), and retail trade (+55,000), while construction (-115,000) recorded the largest decline, followed by professional & business services (-39,000), nondurable goods manufacturing (-26,000), and finance & insurance (-23,000). There was 1.0 *available job for each unemployed* person; this ratio was at a recent high of 2.0 during July 2022. *Separations* include quits, which are generally voluntary separations initiated by employees—serving as a measure of workers' willingness or ability to leave jobs. *Total quits* were little changed in August at 3.1 million.

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