Yardeni Research

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# Morning Briefing

## On Emerging Markets, Brazil & S&P 500 Q3 Earnings

*Check out the accompanying chart collection.*

**Executive Summary:** Emerging markets' stock markets are enjoying bull runs. Melissa says there are strong enough earnings support and low enough valuations to suggest opportunities for investors mindful of the risks. … Also: William reports that US tariffs will be tough for Brazil's beleaguered economy to bear. With high interest rates, high inflation, and a President courting voters with fiscal stimulus instead of economic reform, the picture isn't pretty. … And: Joe is impressed by the S&P 500 companies' record-breaking Q3 earnings reports.

**Emerging Markets: Good Run.** Emerging market (EM) equities are enjoying their best run in years. The MSCI Emerging Markets index is up by 26.8% this year in local currencies, its strongest advance since the post-crisis rebound in 2009, helped by a softer dollar, easier global financial conditions, and enthusiasm for AI-linked chipmakers in EM economies (*Fig. 1*).

None of these eliminates the outstanding risks associated with EMs—domestic political instability, trade tensions, geopolitical perils, and pockets of debt stress remain. But, for now, the EM macroeconomic growth path is justifying the equities' runup. The rally has been far from even.

Our take: We see an opportunity to invest broadly across EMs; but be mindful of the risks and regional disparities before leaping into positions.

Here's more:

(1) *Growth path*. The broad upward momentum lines up with the International Monetary Fund's latest *World Economic Outlook*, which now pegs emerging and developing economies on a GDP growth path just above 4.0% y/y in 2025–26—nearly three times the pace expected for advanced economies—while also highlighting how stronger policy

frameworks have made many EMs more resilient to “risk-off” financial market shocks.

(2) *Discount stands*. What’s striking is that this rally hasn’t nearly erased EMs’ valuation discounts (*Fig. 2*). Broadly speaking, the companies in EMs’ MSCI indexes in aggregate trade at about 14 times 12-month forward earnings—a notable discount to the US MSCI’s forward P/E of 23, well below the EMs’ frothy peak valuations of the mid-1990s, and up only slightly from their post-Covid lows.

(3) *Double-digit earnings growth*. The EMs’ collective earnings picture has improved meaningfully in recent years. Their expanding forward earnings growth over the next couple of years reflects the broadening of upbeat earnings beyond the US. Analysts expect EM MSCI companies in aggregate to grow earnings 17.5% in 2026, up from a projected 11.4% in 2025 (*Fig. 3*).

Net earnings estimate revisions for the EM MSCI index—tracking the balance of analysts’ estimate upgrades versus downgrades—has clawed its way back to roughly neutral in November after spending much of the post-2021 period in negative territory (*Fig. 4*).

(4) *Disparities present*. Meaningful valuation differences, however, are evident across regions. For example, the MSCI for Taiwan, home of chipmaker TSMC, sports a pricier forward P/E near 20 after a major price surge this year; that compares with a forward P/E of just 13 for China’s MSCI, which has lagged Taiwan’s index this year (*Fig. 5* and *Fig. 6*).

There’s been a wide dispersion of EM equity market performances so far this year. The top five performing country MSCI indexes—Korea (82.1%), Colombia (62.4%), Greece (52.6%), South Africa (45.2%), and Peru (44.9%)—sharply outpaced the bottom five performers: the Philippines (-5.5%), Saudi Arabia (-5.2%), Thailand (-3.4%), Malaysia (-2.5%), and Indonesia (-1.9%) (*Table 1*).

**Brazilian Economy: Buckling Under the Weight of Tariffs.** Few major economies would have a better excuse for ending 2025 in recession than Brazil. Yet neither the threat of 50% US tariffs nor 15% interest rates have driven the South American powerhouse into the red—yet. Next year could be a different story if President Luiz Inácio Lula da Silva’s administration doesn’t step up efforts to recalibrate trade and address structural impediments to growth.

Economic activity slowed more than expected in September, according to the central bank’s monthly index. The reliable GDP proxy decreased by *0.24% m/m*. On a y/y basis, it rose

1.98%. That's after real GDP had advanced 2.6% y/y in Q2-2025 (*Fig. 7*). Last week, Brazil's Finance Ministry lowered its 2025 *GDP growth forecast* to 2.2% y/y from 2.3% and projected 2026 growth at 2.4%. But these estimates could prove overly optimistic, as the *$2.2 trillion economy* faces a trifecta of headwinds: the trade war, stubbornly high inflation, and elevated interest rates.

As GDP growth slows, each of those headwinds could be aggravated: The tariffs could put upward pressure on Brazil's 4.7% inflation rate (per Finance Ministry projections). That, in turn, could mean the Selic, Brazil's benchmark interest rate, will remain at the current 15% (*Fig. 8*). Moreover, slowing growth could exacerbate an already troubling 78.1% debt-to-GDP ratio as of September, pushing it toward 100% by 2030.

Let's take a closer look at why 2026 could be a rough year for Brazil:

(1) *Trade: Doing the export shuffle.* The Trump 2.0 era is a big wildcard for Brazil's economy. President Donald Trump initially imposed a 15% tariff on all Brazilian imports into the US back in April. On Friday, he made a U-turn—removing tariffs on beef, coffee, tropical fruits, and other commodities altogether. That caused a flurry of excitement in Brasilia until, on Saturday, Brazilian Vice President Geraldo Alckmin clarified that Brazilian goods generally would be *tariffed in the US at a still-high 40%*.

Theories for why Trump imposed outsized tariffs on the country in the first place include anger over the BRICS's (Brazil, Russia, India, China, and South Africa) angling to replace the dollar and the government's convicting former President Jair Bolsonaro, a Trump ally, on charges of attempting a coup.

Brazil must accelerate efforts to tap other export markets. This process is well afoot, of course. Eurasia Group's Ian Bremmer notes that Lula's government is busily "deepening economic ties with Europe, China and Canada." It's worth noting, too, that the European Union is finalizing a *trade deal* with the South American trading bloc Mercosur.

Thanks to these pivots, the Brazilians have "increased their *total exports* despite big falls in sales to the US," observes Adam Slater at Oxford Economics. Between August and October, exports increased *6.4% y/y* despite the share of US shipments dropping to just 8%. Yet the work of reorienting trade flows to avoid US tariffs is far from done.

Any hopes that Lula might meet with Trump at this weekend's Group of 20 summit have been dashed; the US is *boycotting* the event in South Africa.

(2) *Fiscal stimulus despite high inflation.* With US-Brazil relations at a standoff, Lula's best course of action may be to retool his economy. He has begun to do so, but via fiscal stimulus instead of the supply-side reforms that are needed.

In August, Lula's government rolled out a $5.5 billion "*Sovereign Brazil*" package to support the nation's beleaguered exporters. It postponed taxes on companies in harm's way and incentivized consumers to buy made-in-Brazil products over imports. Short-term stimulus measures helped fuel a 24.8% ytd gain (in local currency) in the Brazil MSCI equities index (*Fig. 9*).

Lula will be running for a *fourth term* in the presidential election scheduled for October 2026, which is likely to mean stepped up government spending to curry favor with voters.

Budget dramas are all too common in Brazil. In May, for example, Lula proposed measures to shore up the government's *fiscal position*. Instead, he provoked the Bond Vigilantes, who in turn sent yields higher (*Fig. 10*). Debt traders were unhappy about plans to hike taxes on offshore investments held by Brazilian funds.

The gambit seemed to run afoul of Lula's pledges to reduce social spending. Last month, Congress handed Lula a setback when it *failed to pass* legislation to raise taxes on banks and billionaires. Now as an election approaches, investors are increasingly dismissive of Brasilia's pledge to generate a budget surplus in 2026.

(3) *High interest rates, soaring currency.* The country's benchmark interest rate, set at 15%, poses a significant headwind limiting economic growth. Persistently high rates of interest are likely damaging investment and consumer spending. This cries out for Lula's team to focus more on supply-side upgrades than fiscal loosening.

The Brazilian real, meanwhile, has *soared 13.6%* versus the dollar this year (*Fig. 11*). That poses a clear and present danger for manufacturing (*Fig. 12* and *Fig. 13*). It could limit overseas demand for soybeans, sugar, coffee, beef, iron ore, and crude oil. And it adds to the long list of reasons why the year ahead could be a rocky one for Brazil.

**Strategy: S&P 500 Q3 EPS at a Record High!** With 92% of the S&P 500 companies having reported June-quarter results through Tuesday's open, their aggregate "blended" quarterly EPS—a mix of actual EPS for companies that have reported and consensus estimates for those that haven't—is $72.60 (*Fig. 14*). That's a new record high for the S&P 500, exceeding the prior one ($66.68 in Q2-2025) by an astounding 8.9% (see our *web pub*

"S&P 500 Quarterly Metrics").

The degree to which Q3-2025 earnings beat analysts' expectations was stunning for a third straight quarter. The S&P 500's 10.4% earnings surprise is the 10th best recorded (since Q1-1987) and easily exceeded Q2's 8.2% beat (*Fig. 15*).

Also up: Q3's blended EPS relative to analysts' expectations at the end of June before reporting season began; at that point, their consensus estimates implied EPS of $67.24 (*Fig. 16*).

As for Q3's year-over-year growth, that's in the double digits for a fourth consecutive quarter. With 8% of the companies left to report, the S&P 500's blended y/y earnings growth rate for Q3 is 14.9%, a 15-quarter high and marking the ninth straight quarter of positive y/y earnings growth (*Fig. 17*).

Viewing growth through a different lens, S&P 500 earnings rose 16.9% y/y in Q3 on a proforma same-company basis. That marks its ninth straight quarter of positive y/y earnings growth and its fourth of double-digit percentage gains (*Fig. 18*).

How did the S&P 500's 11 sectors, the Magnificient-7 stocks, and the remaining S&P 493 do last quarter? Below, Joe puts their aggregate Q3 earnings results under his analytical lens:

(1) *More sectors driving S&P 500's earnings growth.* During Q3, 10 of the 11 S&P 500 sectors delivered rising earnings y/y, up from eight during Q2 and the highest count since 10 sectors did so in Q4-2024. Five sectors recorded stronger y/y growth than the S&P 500 in Q3, and six posted double-digit y/y percentage gains (*Fig. 19*).

Those counts for Q3 represents a notable upshift from eight sectors rising y/y in Q2, when only three sectors grew faster than the S&P 500 and the same three recorded double-digit gains. Furthermore, six of the 11 sectors posted record-high quarterly EPS in Q3. That compares to just one sector, Communication Services, with record-high EPS during H1-2025.

Energy's earnings fell y/y for a fifth straight quarter and the ninth time in 10 quarters. Materials' earnings growth turned positive again in Q3 and touched a 14-quarter high but has declined y/y in 10 of the last 13 quarters.

On the bright side, Information Technology's Q3 earnings rose y/y for a tenth straight quarter and grew at a double-digit percentage rate for a ninth quarter. Consumer Discretionary and Financials both marked their 11th straight quarter of positive y/y earnings growth. Communication Services' posted a fifth straight quarter of double-digit y/y percentage growth and its tenth quarter of rising earnings.

Here's how the sectors' y/y earnings growth rates for Q3 have stacked up so far on a proforma basis: Information Technology (28.7%), Financials (25.0), Industrials (23.2), Real Estate (22.8), Materials (20.2), S&P 500 (16.9), Communication Services (16.7), Consumer Discretionary (9.3), Health Care (5.2), Utilities (4.2), Consumer Staples (1.0), and Energy (-1.5).

(2) *Magnificent-7.* Through Tuesday's market open, six of the Magnificent-7, all but Nvidia, have reported results so far. The "Magnificent-6's" aggregate Q2 earnings surprise was 16.2%, and its y/y earnings growth of 26.8% was nearly triple the consensus' 9.2% forecast—all well above the S&P 500's measures (*Fig. 20*).

Three of the six had double-digit percentage earnings surprises, and five had double-digit y/y earnings growth. Here are the Q3 earnings surprises and y/y earnings growth rates for the Magnificent-6: Alphabet (33.3% earnings surprise, 46.2% y/y earnings growth), Amazon (23.9, 36.4), Microsoft (12.7, 25.2), Meta (8.4, 20.2), Apple (4.4, 12.8), and Tesla (-8.7, -30.6).

(3) *Another strong quarter for S&P 493*. The S&P 493 delivered positive y/y earnings growth in Q3 for a seventh straight quarter. Earnings growth of 12.8% y/y was in the double digits for the third time in four quarters and well above analysts' consensus forecast of just 3.1% growth. The S&P 493's aggregate Q3 earnings results beat consensus forecasts by 8.5%, behind the Magnificent-7's stellar earnings beat of 16.2%.

## Calendars

**US: Wed:** Philadelphia Fed Manufacturing Index 3.0; MBA Mortgage Applications; Atlanta Fed GDPNow; Minutes of Fed's October FOMC Meeting. **Thurs:** Existing Home Sales 4.08mu; Goolsbee; Paulson; Cook. (Source: FX Street)

**Global: Tues:** Japan Core Machinery Orders 2.4%m/m, 5.4%y/y; Canada Housing Starts

275k; Dhingra; Tuominen; Elderson; Pill. **Wed:** Germany PPI 0.0%m/m, -1.9%y/y; UK CBI Industrial Trend Orders -30. (Source: FX Street)

## US Economic Indicators

**NAHB Housing Market Index** (*link*): "While lower mortgage rates are a positive development for affordability conditions, many buyers remain hesitant because of the recent record-long government shutdown and concerns over job security and inflation," notes NAHB Chairman Buddy Hughes. "More builders are using incentives to get deals closed, including lower prices, but many potential buyers still remain on the fence." The *housing market index* (HMI) in November was relatively flat, ticking up to 38 this month from 37 last month. *Current sales* conditions increased 2 points to 41, while *sale expectations* dipped 3 points to 51. The gauge tracking *traffic of prospective home buyers* ticked up a point to 26. *By region*, looking at three-month averages for the HMIs, the South (+3 points to 34), Northeast (+2 to 48), and West (+2 to 30) moved higher during the month, while the Midwest fell a point to 41. According to the report, "41% of builders reported cutting prices in November, a record high in the post-Covid period and the first time this measure has passed 40%." Meanwhile, the *average price cut* held at 6% in November, after staying at 5% from last November through this September. The *use of sales incentives* was 65% again in November, matching September and October. Robert Dietz, NAHB's chief economist forecasts, "After a decline in single-family housing starts in 2025, NAHB is forecasting a slight gain in 2026 as builders continue to report future sales conditions in marginally positive territory."

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