

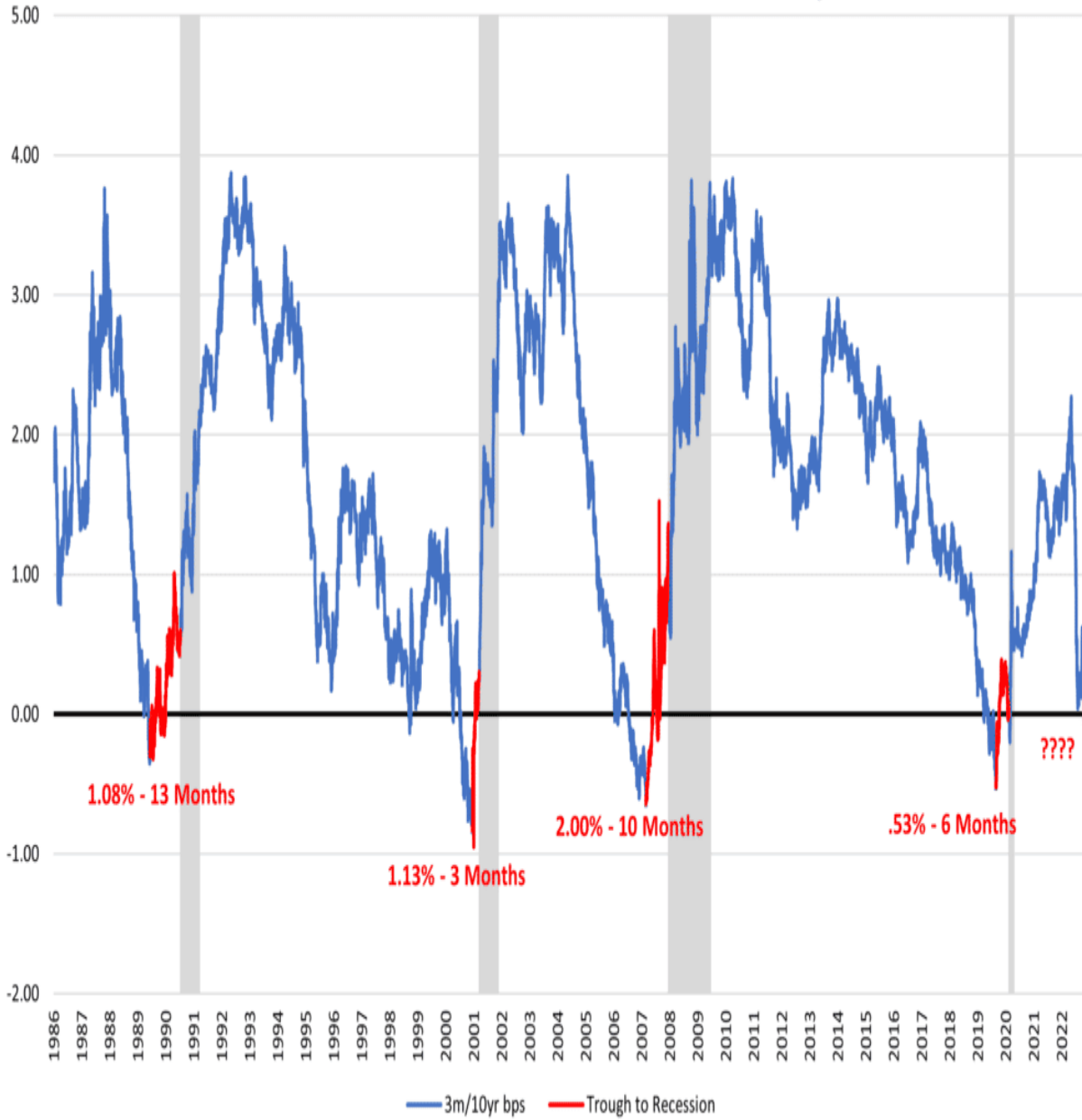


## Fed's Yield Curve Forecasts Recession

Q3 GDP rose nicely, but the Fed's preferred yield curve has spoken. It says a recession is imminent. The graph below charts the yield difference between the 3-month Treasury bill and the 10-year Treasury note. The Fed often reminds us that an inversion in the 3m/10yr UST curve is a precursor for recessions. Every time, as we annotate in red, the ten yield is lower than the three-month yield for more than a few days, a recession follows.

When should we expect a recession? As the graph highlights, it has taken between three and thirteen months from the trough of the yield curve inversion until the official NBER recession declaration. Making timing a little tricky is the clock doesn't start ticking until the yield curve troughs. Based on Fed Funds futures, we expect the three-month yield will rise from 4.05% to 4.80%. Unless the 10-year yield falls by .75% over the coming months, the Fed's yield curve will invert further. Such a trough in the Fed's yield curve may take another couple of months to form. Then we can start the recession clock.

# 3 month/10 year UST Curve & Recessions



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## What To Watch Today

### Economy

- 8:30 a.m. ET: **Employment Cost Index**, 3Q (1.2% expected, 1.3% prior)
- 8:30 a.m. ET: **Personal Income**, month-over-month, September (0.4% expected, 0.3% prior)
- 8:30 a.m. ET: **Personal Spending**, month-over-month, September (0.4% expected, 0.4% prior)
- 8:30 a.m. ET: **Real Personal Spending**, month-over-month, September (0.2% expected, 0.1% prior)
- 8:30 a.m. ET: **PCE Deflator**, month-over-month, September (0.3% expected, 0.3% prior)
- 8:30 a.m. ET: **PCE Deflator**, year-over-year, September (6.3% expected, 6.2% prior)
- 8:30 a.m. ET: **PCE Core Deflator**, month-over-month, September (0.5% expected, 0.6% prior)
- 10:00 a.m. ET: **Pending Home Sales**, month-over-month, September (-5.2% expected, -2.0% prior)
- 10:00 a.m. ET: **Pending Home Sales NSA**, year-over-year, September (-22.5% prior)
- 10:00 a.m. ET: **University of Michigan Consumer Sentiment**, October final (59.6 expected, 59.8 prior)

### Earnings

	Company	Time	Estimate		Growth	Surprise	
					Show only confirmed?		
✓	<b>XOM</b>	Exxon Mobil Corp.	6:30 AM ET	\$3.88	\$119.12 B	61.4%	+ = -
✓	<b>CVX</b>	Chevron Corporation	6:15 AM ET	\$5.02	\$57.94 B	29.6%	+ = -
✓	<b>EQNR</b>	Equinor ASA	BMO	\$1.78	\$57.68 B	147.9%	+ = -
✓	<b>ABBV</b>	AbbVie Inc.	7:40 AM ET	\$3.56	\$14.92 B	4.0%	+ = -
✓	<b>CHTR</b>	Charter Communicati...	7:00 AM ET	\$7.94	\$13.89 B	5.7%	+ = -
✓	<b>LYB</b>	LyondellBasell Indust...	6:30 AM ET	\$2.96	\$13.27 B	4.5%	+ = -
✓	<b>SNY</b>	Sanofi	5:00 AM ET	\$1.31	\$11.70 B	-4.9%	+ = -
✓	<b>IMO</b>	Imperial Oil Ltd	BMO	\$2.00	\$14.08 B	73.2%	+ = -
✓	<b>FMX</b>	Fomento Economico ...	8:30 AM ET	-	\$7.11 B	-0.1%	+ = -
✓	<b>BBVA</b>	Banco Bilbao Vizcaya...	BMO	\$0.23	\$6.06 B	-3.6%	+ = -
✓	<b>CL</b>	Colgate-Palmolive Co.	6:55 AM ET	\$0.74	\$4.52 B	2.4%	+ = -
✓	<b>NEE</b>	NextEra Energy Inc	7:30 AM ET	\$0.79	\$5.63 B	28.8%	+ = -
✓	<b>GWV</b>	W.W. Grainger, Inc.	8:00 AM ET	\$7.19	\$3.89 B	15.4%	+ = -
✓	<b>DVA</b>	DaVita Inc.	BMO	\$1.67	\$2.98 B	1.4%	+ = -
✓	<b>NWL</b>	Newell Brands Inc.	7:00 AM ET	\$0.47	\$2.29 B	-17.8%	+ = -
✓	<b>AON</b>	AON Plc	6:00 AM ET	\$2.01	\$2.80 B	3.6%	+ = -
✓	<b>BAH</b>	Booz Allen Hamilton ...	6:45 AM ET	\$1.12	\$2.24 B	6.4%	+ = -
✓	<b>AVTR</b>	Avantor, Inc.	6:00 AM ET	\$0.33	\$1.97 B	7.4%	+ = -
✓	<b>FTS</b>	Fortis Inc.	6:20 AM ET	\$0.50	\$1.87 B	7.2%	+ = -
✓	<b>ACDVF</b>	Air Canada	6:00 AM ET	\$0.41	-	-	+ = -
✓	<b>JKS</b>	JinkoSolar Holding C...	7:35 AM ET	\$0.79	\$2.57 B	93.2%	+ = -
✓	<b>CHD</b>	Church & Dwight Co.,...	6:55 AM ET	\$0.65	\$1.30 B	-0.9%	+ = -
✓	<b>AB</b>	AllianceBernstein Hol...	6:20 AM ET	\$0.60	\$800.00 M	-26.8%	+ = -
✓	<b>BLMN</b>	Bloomin' Brands Inc	7:00 AM ET	\$0.33	\$1.05 B	3.9%	+ = -
✓	<b>BSAC</b>	Banco Santander-Chi...	BMO	\$0.48	\$638.14 M	-30.4%	+ = -
✓	<b>CRI</b>	Carter's, Inc.	6:10 AM ET	\$1.65	\$855.14 M	-4.0%	+ = -
✓	<b>NMRK</b>	Newmark Group, Inc.	8:15 AM ET	\$0.47	\$746.05 M	-5.3%	+ = -
✓	<b>ITCB</b>	Itaú Corpanca	BMO	\$0.29	\$426.27 M	-34.8%	+ = -
✓	<b>NVT</b>	nVent Electric plc	6:30 AM ET	\$0.59	\$705.13 M	9.7%	+ = -
✓	<b>CRTO</b>	Criteo S.A.	7:00 AM ET	\$0.46	\$226.34 M	-55.5%	+ = -
✓	<b>PIPR</b>	Piper Sandler Compa...	8:00 AM ET	\$2.08	\$328.31 M	-26.3%	+ = -
✓	<b>GNTX</b>	Gentex Corp.	8:00 AM ET	\$0.39	\$502.67 M	25.8%	+ = -
✓	<b>SMP</b>	Standard Motor Prod...	8:30 AM ET	\$0.95	\$380.88 M	2.9%	+ = -
✓	<b>COWN</b>	Cowen Group Inc	4:15 PM ET	\$0.56	\$285.74 M	-22.6%	+ = -
✓	<b>GTLS</b>	Chart Industries Inc.	6:30 AM ET	\$1.21	\$449.40 M	36.9%	+ = -
✓	<b>B</b>	Barnes Group Inc.	6:30 AM ET	\$0.48	\$323.87 M	-0.4%	+ = -
✓	<b>SLCA</b>	U.S. Silica Holdings, I...	6:00 AM ET	\$0.38	\$402.15 M	50.5%	+ = -
✓	<b>NEP</b>	Nextera Energy Partn...	7:30 AM ET	\$0.63	\$378.78 M	50.3%	+ = -

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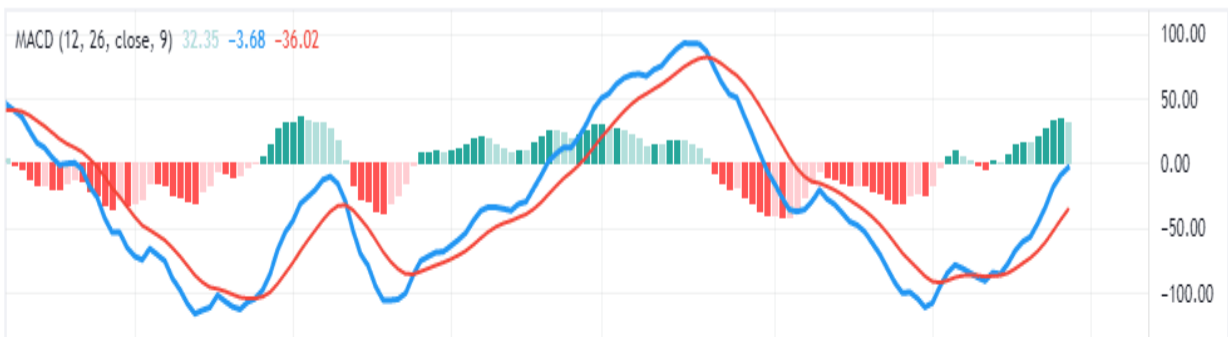
## Market Trading Update

Another tough day of trading yesterday as Facebook's massive disappointment sent the stock plunging to the lowest levels in several years, closing below \$100/share. After the close, Amazon disappointed as well, another Megacap name that will weigh on the S&P 500 today. While reporting some weaknesses in product sales, Apple did better and may provide some support.

The market did manage to hold onto the 3800 level, but unless the markets can muster a rally, that support is now at risk of getting broken today. If it does, the 20-dma remains the last support level before a retest of lows. If that does become the case, the risk to the downside increases markedly. We are starting to reduce risk in portfolios further today and raising additional cash for the time being. Once markets stabilize we will look to rebuild allocations accordingly.



TradingView



## **GDP Oddities**

GDP was stronger than expected, growing at 2.6%. Growth is now positive for the year, after -.6% and -1.6% GDP in the second and first quarters, respectively. The table below from Charles Schwab breaks down GDP into its components.

GDP components					
	% of real GDP	3Q22 real GDP	2Q22 real GDP	1Q22 real GDP	4Q21 real GDP
▪ Consumer spending	70.7%	1.4%	2.0%	1.3%	3.1%
▪ Government spending	17.0%	2.4%	-1.6%	-2.3%	-1.0%
-Federal: 6.8%		3.7%	-3.4%	-5.3%	0.0%
-State/local: 10.2%		1.7%	-0.6%	-0.4%	-1.6%
▪ Net exports of goods and services	(-6.4%)	2.8*	1.2*	-3.1*	-0.2*
-Exports: 13.0%		14.4%	13.8%	-4.6%	23.5%
-Imports: (19.4%)		-6.9%	2.2%	18.4%	18.6%
▪ Fixed investment	17.7%	-4.9%	-5.0%	4.8%	0.6%
-Nonresidential: 14.7%		3.7%	0.1%	7.9%	1.1%
-Residential: 3.1%		-26.4%	-17.8%	-3.1%	-1.1%
▪ Change in private inventories	--	-0.7*	-1.9*	0.2*	5.0*
	<b>Real GDP</b>	<b>2.6%</b>	<b>-0.6%</b>	<b>-1.6%</b>	<b>7.0%</b>

Source: Charles Schwab, Bureau of Economic Analysis, as of 9/30/2022. \*Represents contribution to percent change in real GDP. Numbers may not add up to 100% due to rounding. Real GDP based on annualized Q/Q % change.

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There are two extreme readings within the report worth noting. First, fixed investment, accounting for about 18% of GDP, detracted from growth. The decline was due to a sharp fall in investment in residential housing. In fact, residential investment single handily reduced GDP by 1.4%, the largest negative contribution since 2007. Given high mortgage rates and plummeting homebuilder sentiment, this was expected. The concern, however, is that residential fixed investment (RFI) tends to lead the economy by about a year. The graph below shows the strong leading relationship between RFI and ISM.



— ISM    — Residential Fixed Investment as a % of Total FI YoY% - 12-Month Lead (RHS)



Source: Refinitiv Datastream - Global Macro Investor



— ISM    — Residential Fixed Investment as a % of Total FI YoY% - 12-Month Lead (RHS)



The second outlier is foreign trade. Net exports (exports minus imports) are often a negative component of GDP as America runs a perpetual trade deficit. However, in the third quarter, exports handily outstripped imports adding 2.8% to GDP growth, accounting for its **largest contribution to GDP in over 40 years**. This is somewhat surprising, given a strong dollar favors imports. Looking into the data, we find exports were led higher by *petroleum and products*. We think increased natural gas needs from Europe, along with higher energy prices, are the likely culprit.

The GDP price index was +4.1%. While high, it is a welcome sign inflationary pressures are easing. The Q2 price index was +9.1%.

## **Seasonality in a Bear vs. Bull Market**

The graph below, from Top Down Charts, sheds new and concerning light on seasonality patterns for the S&P 500. As it shows, markets tend to go higher in the fourth quarter. However, in bear markets, October's tend to have decent gains but said gains are often erased in November or December.

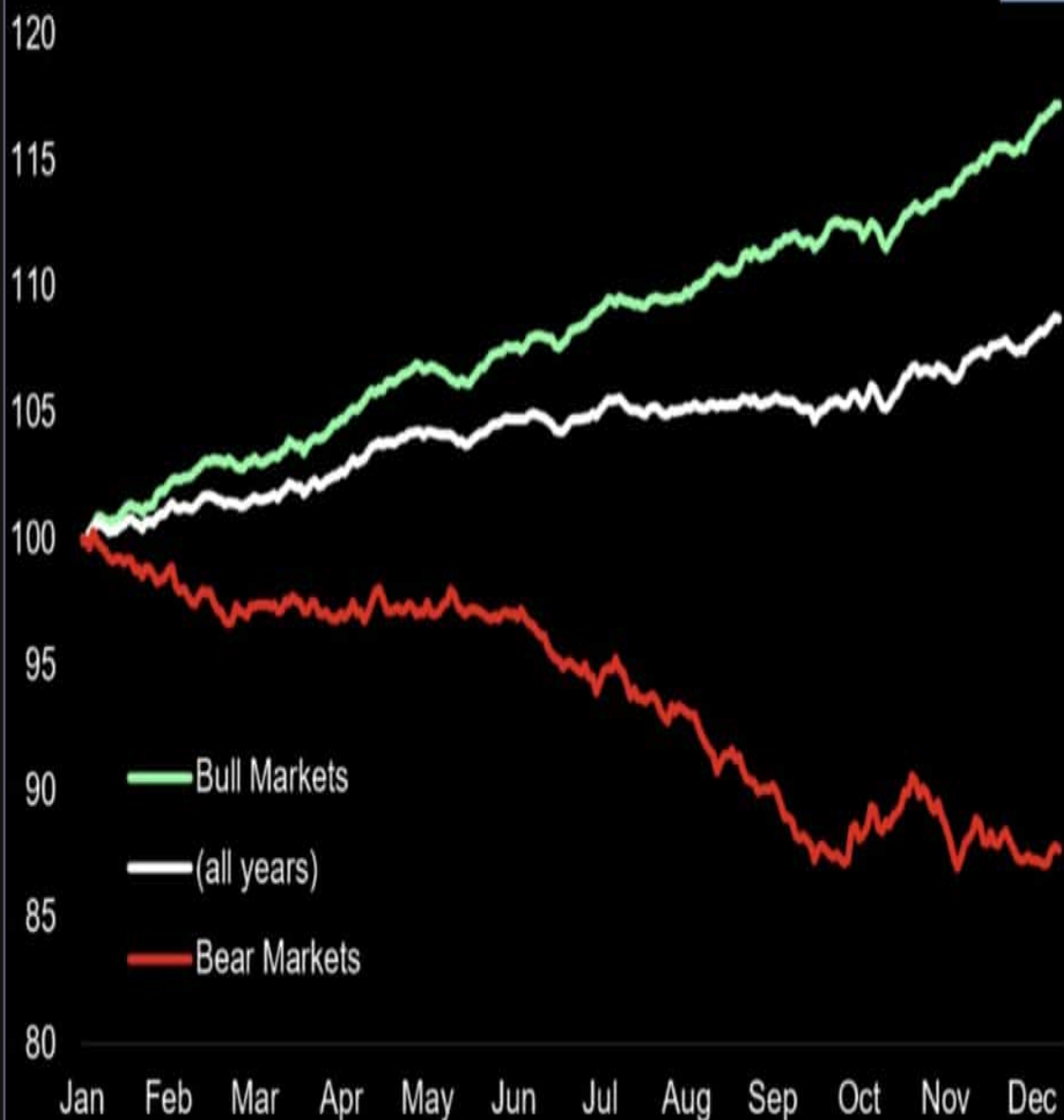
# Bear market seasonality

Very different from normal seasonality. Seasonality does not look the same in different market regimes. We should be very close to the "seasonal top" for bear markets right now and heading lower into year-end.

## Conditional Seasonality: S&P 500

Seasonality During Bull vs Bear Markets 1965-2021

TOP  
DOWN  
CHARTS



Top Down Charts

# Bear market seasonality

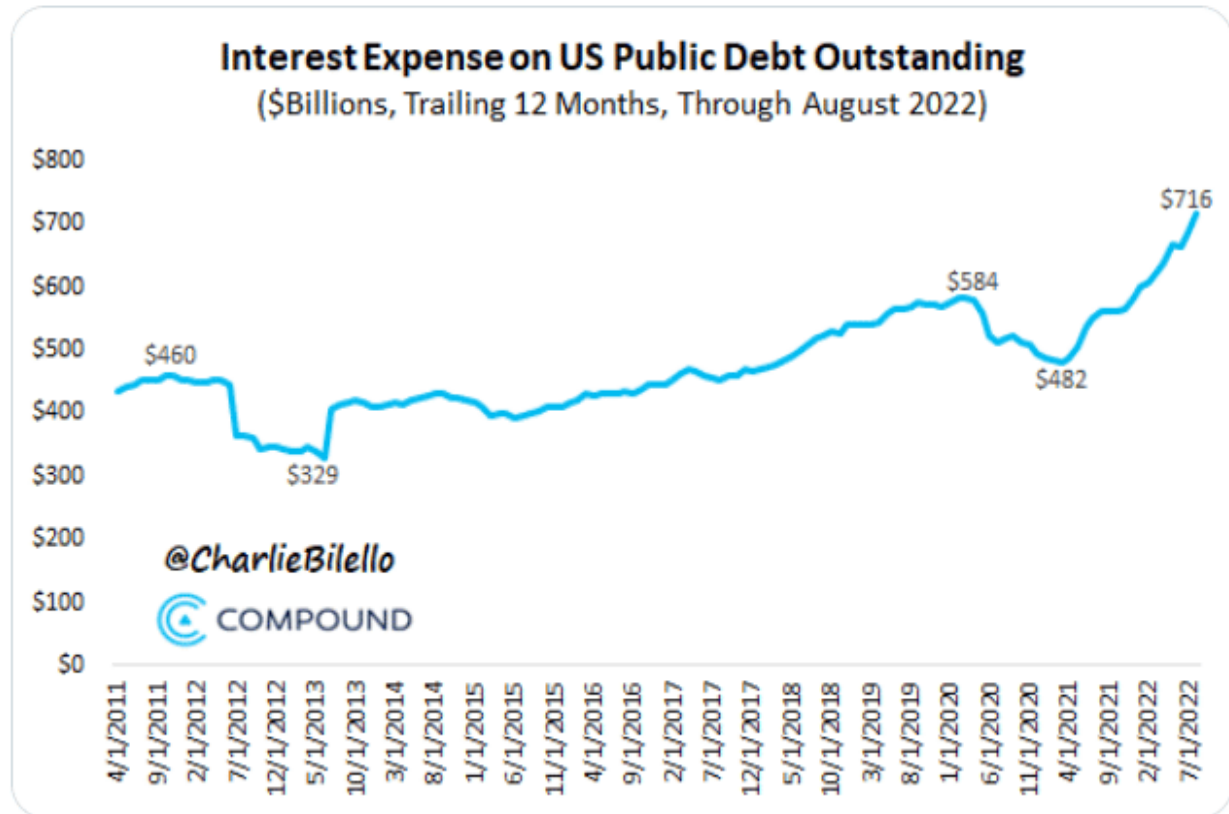
## **Larger Federal Deficits**

The Tweet below from Samantha LaDuc shows how the surge in interest rates is pushing the interest expense for the U.S. Treasury higher. To put \$716 billion, and rising, into perspective, the entire deficit for 2019 was just under \$1 trillion. From 2013 to 2017, the entire deficit was less than \$716 billion. This is yet another reason that higher interest rates are not sustainable.

Samantha LaDuc  
@SamanthaLaDuc

...

Unless interest rates fall sharply in the coming months, the interest expense on Public Debt will soon surpass \$1 trillion on an annual basis and become the largest line item in the budget. 🙄



Samantha LaDuc  
@SamanthaLaDuc

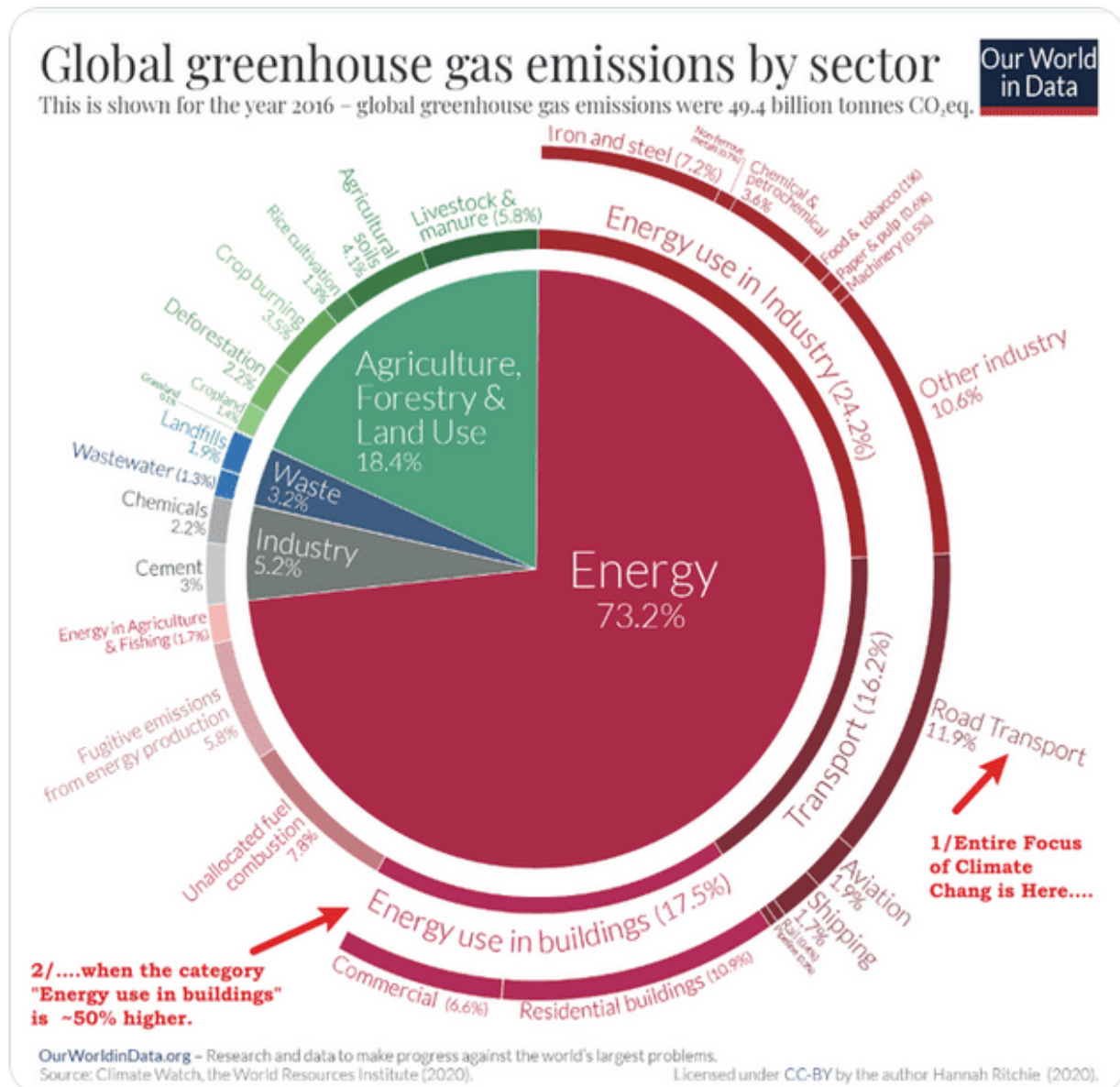
...

Unless interest rates fall sharply in the coming months, the interest expense on Public Debt will soon surpass \$1 trillion on an annual basis and become the largest line item in the budget. 🙄



## Tweet of the Day

What's amazing is they acknowledge that autos are only 12% of CO2 emissions, we blame the car companies for our driving and nobody is protesting "buildings" or the makers of buildings. What are we missing?



What's amazing is they acknowledge that autos are only 12% of CO2 emissions, we blame the car companies for our driving and nobody is protesting "buildings" or the makers of buildings. What are we missing?



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