Strategy

JefMacro Weekly—What Will End The Cycle? Small Businesses Hold The Key

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Key Takeaway

GREED & fear's "best guess" would be Chinese equities bounce 25% if Covid restrictions were relaxed, however, cases, lockdowns rising. Global Strategy expects SPX to reach 4200 by '23 based on flattish earnings growth; made 3 changes to sector allocation. CPI was better than anticipated, Aneta changed the expected Dec hike to 50bps, but kept 5.1% terminal rate by March. The labor market is still strong, thanks to small businesses, but likely to crack in Q1.

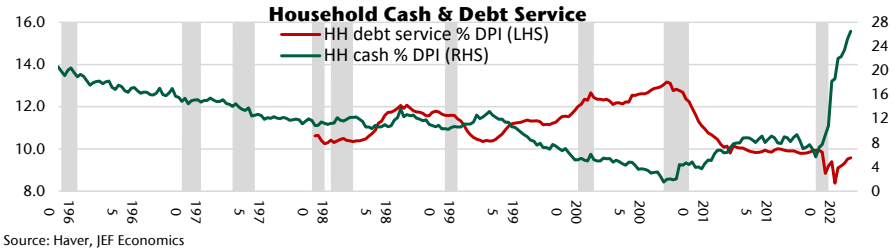
GREED & fear—Our "best guess" on how much Chinese equities would rally on relaxation of Covid suppression was 25%. GREED & fear is concerned that Covid cases and localised lock downs are rising. There are some signs of relaxation. President Xi Jinping has stopped always wearing a mask in public. Several regions no longer require a pre-travel negative test for a domestic train or flight ex Beijing. Talk of easing entry requirements for arriving foreign executives.

Aneta Markowska—CPI news came in better than expected. We expect another soft CPI print in November and a 50bps increase in December rather than 75bps, but we are keeping our assumption of a 5.1% terminal rate by March. Small businesses are currently driving the labor market due to unprecedented pricing power. However, we should see small business profits crack in Q1 due to increased wages and higher rates.

Global Strategy—One of the points of confusion is that earnings are nominal, but a recession is measured in real variables. High prices boost corporate profits but depress output. One key tenet moving into '23 is that SPX is experiencing a typical profit recession, not a credit or deflationary shock. We expect flattish EPS growth in '23, below consensus, and expect the SPX to move to 4,200. We made three sector changes with most notable being Tech down to Mod. Bearish.

Brad Bechtel—USD bulls see a lot of bargains, but that's not how the market views it. They are chasing, which means the pain is not over for USD bulls. If the US is going to a higher terminal rate faster than the rest of G10, how can the USD underperform G10 currencies? Be careful chasing, as we're unsure how far we can run without the real rate side and the Fed capitulating. If both stay firm, then the USD will struggle to stay weak.

The consumer is still strong, no need to cut back on spending



Source: Haver, JEF Economics

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