October 15th 2021

ONE SWALLOW DOESN'T MAKE A SUMMER

Following just a few earnings reports (ie only 8 members of the S&P 500), Wall Street's (positive) reaction could raise the issue of whether the bar has been set too low for 3Q. We would however be very careful not to draw such a conclusion or consider that earnings will easily/largely offset the negative headwinds resulting from higher input costs/wages/bottlenecks etc. It is still very early days (regarding the earnings season) while, as shown below, expectations were probably too low on US banks (contrary to other sectors).

What's more, as explained yesterday, whereas banks' valuations are no longer cheap, reserve releases are just a one-off (which has been priced-in for a long time) + the boom in M&A fees will not last if we are right about any forthcoming setback on markets & economic growth + the traditional activities were far from exciting in all the reports. Interestingly, the CEOs of Goldman + JP Morgan + Morgan Stanley all asked the Fed to act (and "prick this bubble", dixit James Gorman!).

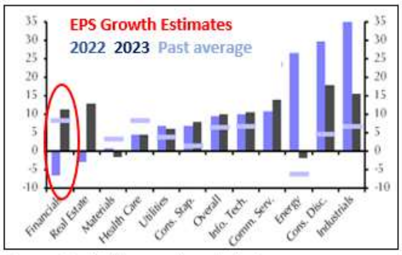
The difficulty of the current situation is the Pavlovian/denial mentality which is now dominant; especially after the covid recovery. Any headwinds are ignored, in the belief that they will all be temporary, thanks to the bull market that has so far successfully passed through any crisis since 2009.

Witness, among others, the top economic research institutes in Germany which have cut their GDP growth forecasts by 1.3% for 2021 (from 3.7% to 2.4%), to immediately raise 2022 estimates by 0.90% (from 3.9% to 4.8%), while also expecting 2023 GDP growth to slow to 1.9%! Ditto with inflation, which they all expect to return to 2% in 2023, following a 0.5% to 1% overshoot (above the ECB target) in 2022 & 2021 respectively.

A few months ago, all were expecting to enjoy a massive economic boom + the roaring 20's were supposed to be back + etc (a scenario we never subscribed to). Instead of that, we are now dealing with an energy & supply crisis + inflation & global GDP growth slowdown + cenbanks tightening, while valuations remain elevated, but who cares (as the future is expected to be so bright indeed)?

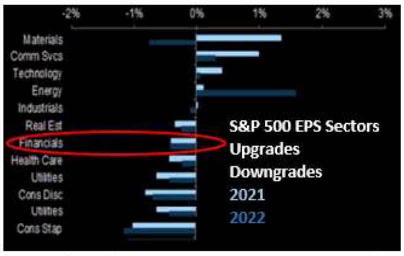
Sadly, such kind of blind behaviour/psychology is reminiscent of so many excessive/extreme periods/turning points we have already seen in the past (2000, 2007, etc).

US EPS ESTIMATES + GLOBAL EPS ESTIMATES REVISION + US CPI vs US PPI



Source Capital Economics - **chart 1**

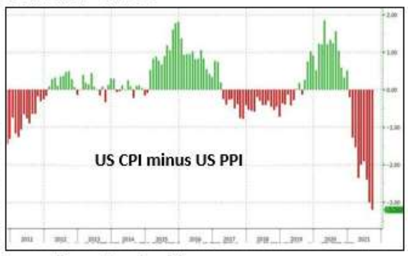
Source FactSet - **chart 2**



Source Ibes - **chart 3**

Source WSJ - **chart 4**

Source Refinitiv - **chart 5**



Source Barron's - **chart 6**

As shown on the first three charts above, the US banking sector was rather badly ranked in terms of upgrades/downgrades/expectations ahead of the season, contrary to the tech sector for instance. A surprise on the upside could thus happen on financials, but this cannot be viewed as a leading indicator for the whole earnings season. Many sectors still have to prove that they can pass on higher expenses/costs to customers (as witnessed by the CPI-PPI differential – chart 6), and the coming days will see numerous noisy hit/miss reports.

Following an upward EPS revision on the S&P 500 by 12% (ex financials) during the 3rd quarter, don't expect a remake of 1Q & 2Q, where the beats reached 23% & 17% on average respectively. Worse, in the current context (as explained many times), we doubt that in the US the 3-4% typical earnings estimates' beat reached in the past will be met.

Meanwhile, a peak is in place in all regions, be it in terms of revisions (chart 4) and EPS, and history shows that a period of consolidation/pullback usually follows on the markets (chart 5). Answer in the coming weeks…

EUROSTOXX FUT – DAILY

Short-term structures have been lacking clarity since the top of wave III, hence the reason why we have been struggling since then. However, 1) we will keep a negative bias, actually as long as the highs of September are intact, while 2) we can mention the possibility of the formation of head & shoulder pattern on many indices like the Eurostoxx above + the Dow Jones + etc.

DAX FUT – DAILY

Same comment as above.

S&P 500 FUT – DAILY

The "good news" with the current rebound (that we were not expecting) is that 1) we may regain some short-term visibility (structures developed since the top of September are anything but clear) and 2) we will soon get an answer as to whether a top of larger degree is well in place.

NASDAQ FUT – DAILY

Same comment than on the S&P 500.

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