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A US REVENUE RECESSION

ANALYTIC INSIGHTS

A REVENUE RECESSION

TWO QUARTERS OF NEGATIVE REVENUE GROWTH

Gordon T Long
9/21/2015

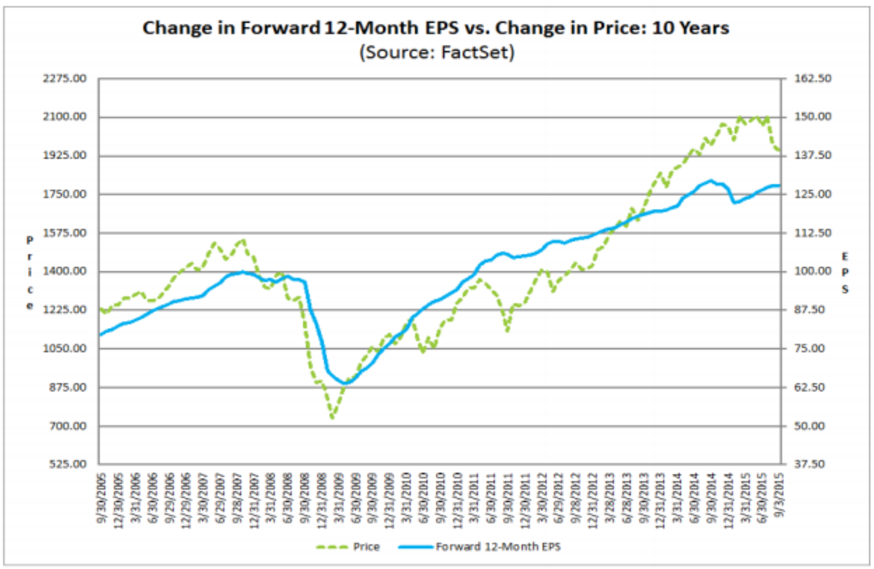
A US REVENUE RECESSION

Two Quarters of Negative Revenue Growth

I have been talking for some time about a potential earnings recession and possibly even something worse on the horizon. Q2 Earning season and conference calls were as we expected.

It marked the first time the S&P 500 index has seen two consecutive quarters of year-over-year revenue declines since Q2 2009 and Q3 2009. The blended revenue decline according to Factset for Q2 2015 was negative -3.4%.

EPS held up by share buybacks has been signaling this problem for some time now.



TWO NEGATIVE QUARTERS – *Revenues then Earnings*

S&P 500 REVENUES – *In a Recession*

An economic recession is characterized as two consecutive quarters of negative growth. Though the media will avoid saying it, two consecutive quarters of negative top line sales growth by the S&P 500 markets indicate a "Revenue Recession". Such an event always precedes worse to come and I was unable to find and example where this was not true!

Q2 2015 marks the first time the S&P 500 index has seen two consecutive quarters of year-over-year revenue declines since Q2 2009 and Q3 2009. As I said earlier, the blended revenue decline for Q2 2015 according to Factset was -3.4%.

FACTSET EARNINGS INSIGHT September 4, 2015

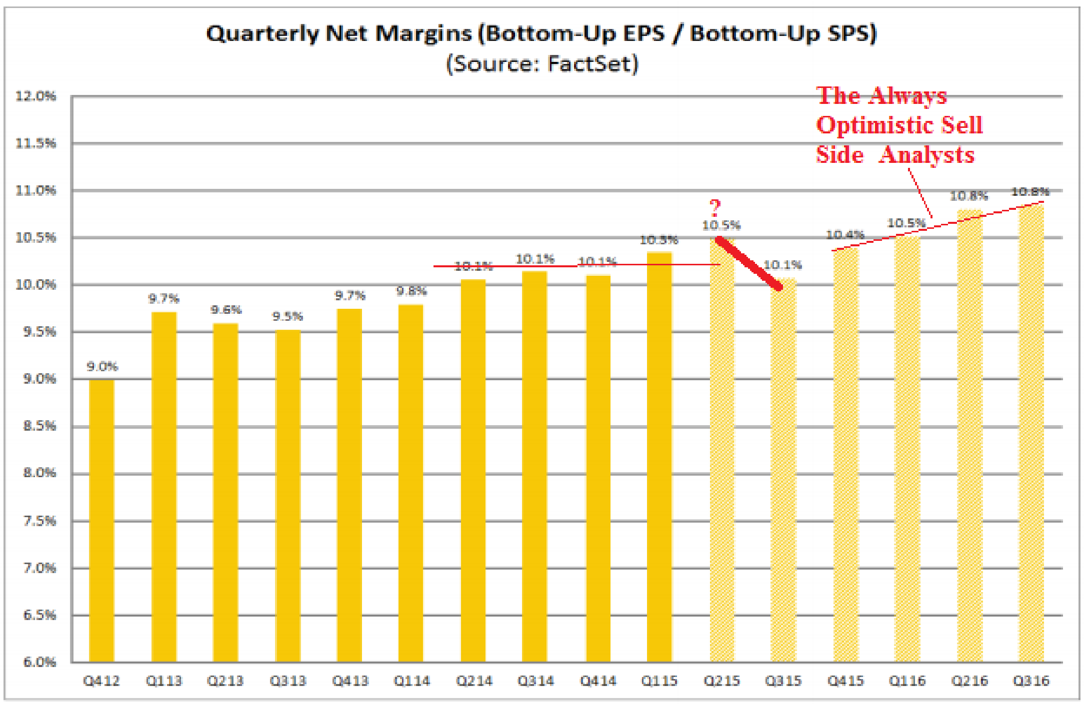
Q2 2015 Earnings Season: By the Numbers

Overview

Due to companies beating revenue estimates in aggregate, the blended revenue decline for Q2 2015 is -3.4%. This marks the first time the index has seen two consecutive quarters of year-over-year revenue declines since Q2 2009 and Q3 2009. At the sector level, the Energy sector reported the largest year-over-year decrease in sales. On the other hand, the Health Care sector reported the largest year-over-year increase in sales.

S&P 500 EARNINGS – *Serious Margin /Currency Issues*

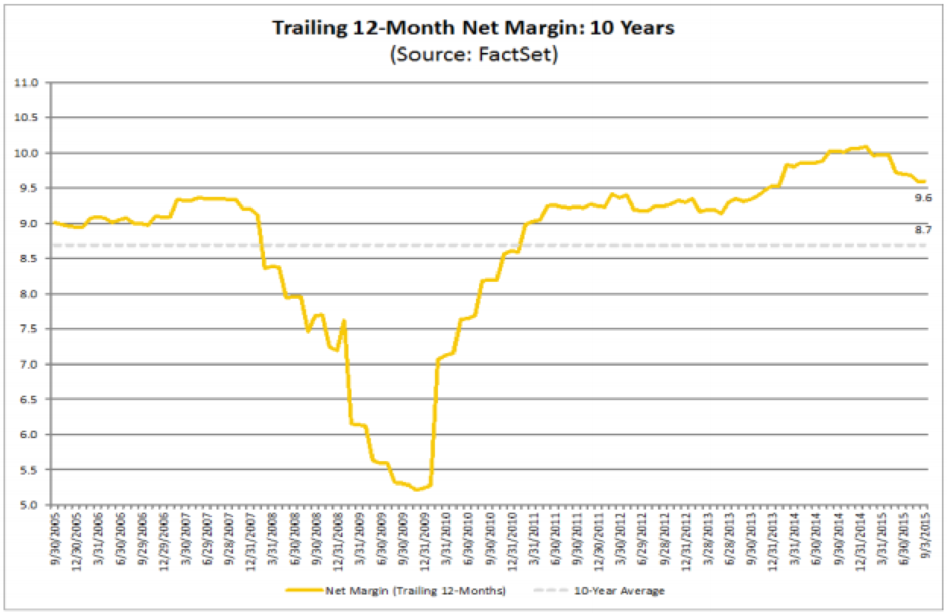
Margins shot up to save the earnings this quarter for reasons no one can explain other than historic levels of new car leases. Also these historic high margins are expected to increase even further? Something is obviously wrong here?



Trailing 12-Month Net Margins

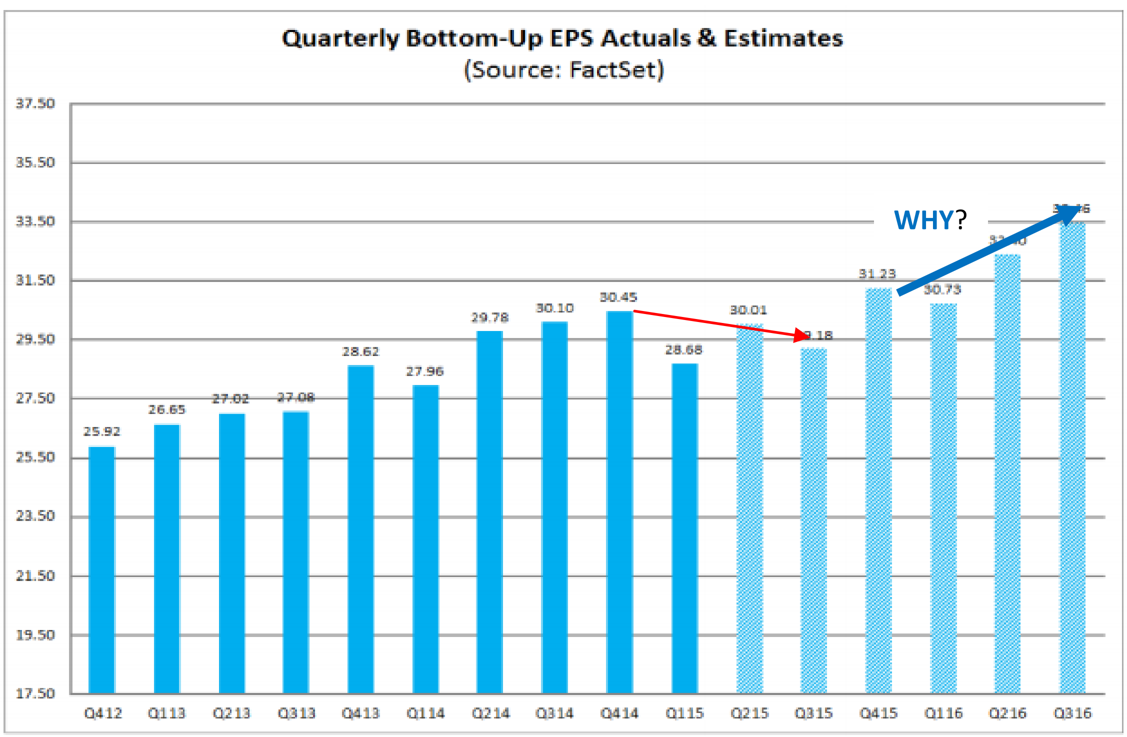
Maybe this is the correct way to look at what is happening with margins and what we can expect going forward?

Net Margins: Current & Historical



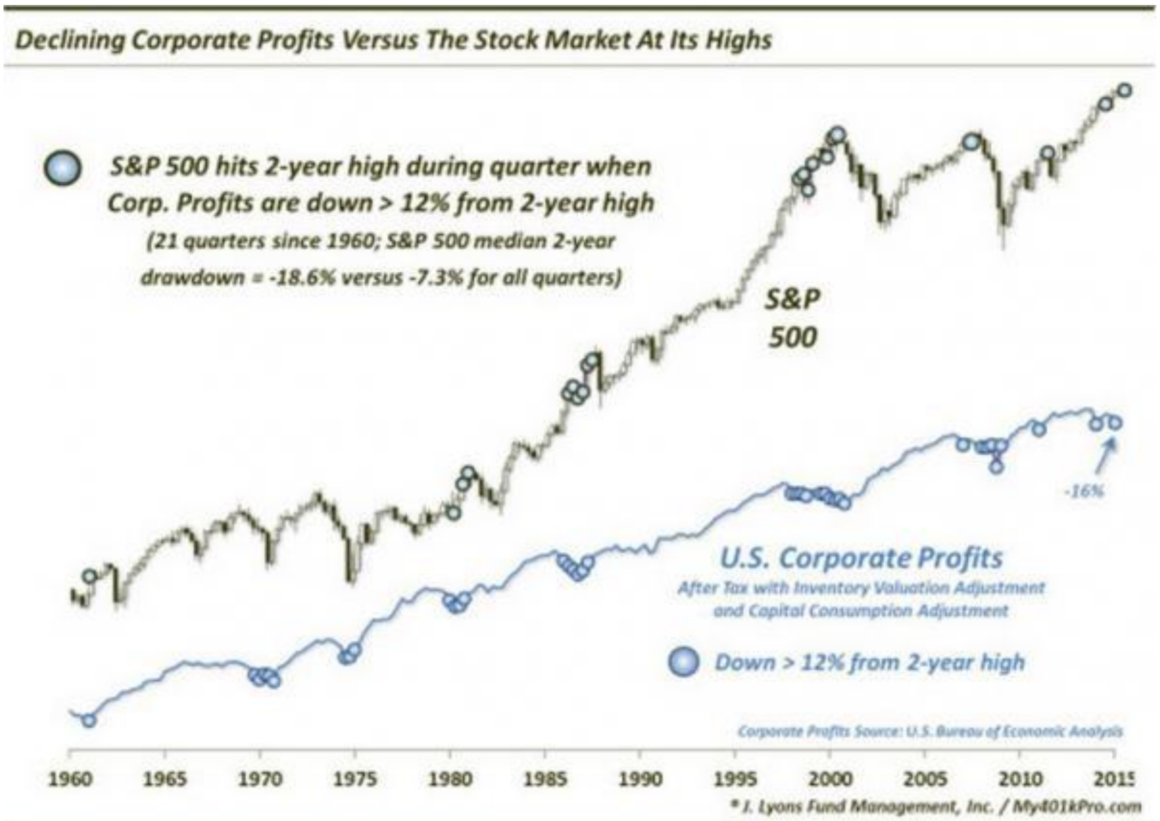
S&P 500 EARNINGS – *Does Anyone Actually Believe these #'s?*

It doesn't take much analysis to see the Sell Side Analysts are hoping for a miracle! In a moment we will take a tour of the world looking for where that miracle may be found?



VALUATIONS

Valuations by any measure are at historical levels as are corporate profit levels. It is difficult to see how both can be sustained much longer. We have talked extensively about this with many charts in previous sessions and I will leave you to review previous LONGWave slide sets.

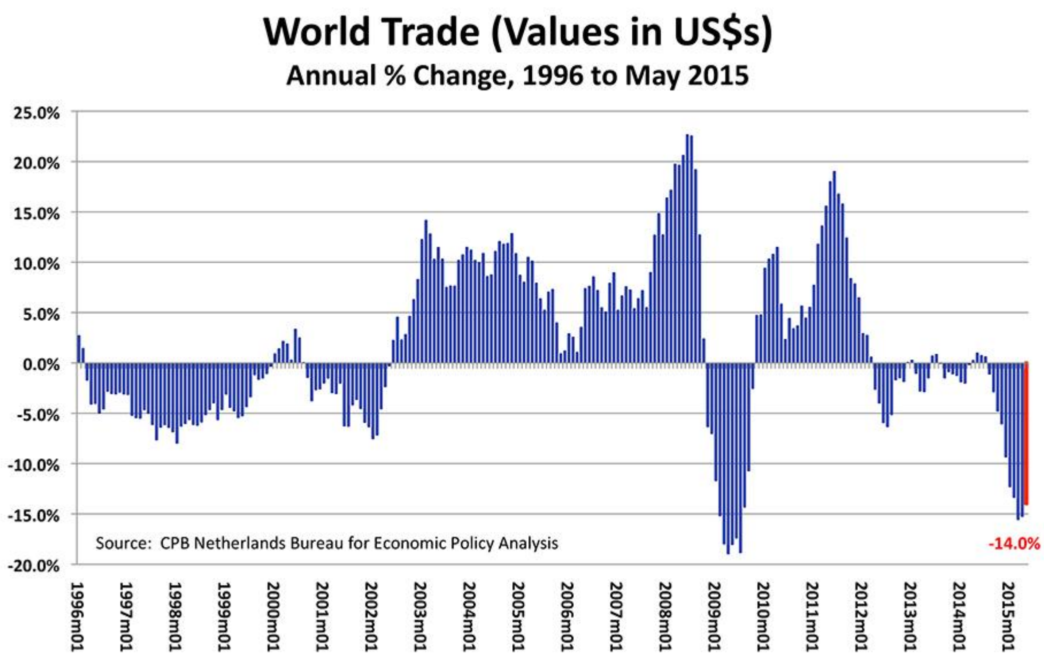


GLOBAL SLOWING – Suddenly Everyone "Gets the Memo"

Let's walk around the world and see what we see.

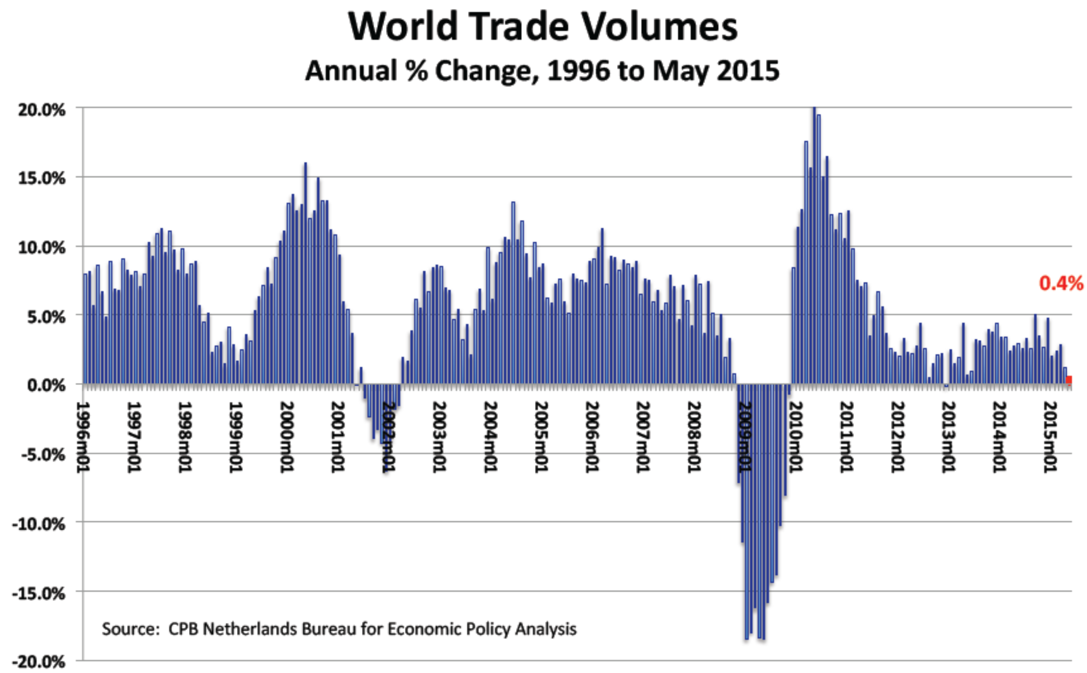
WORLD TRADE – Values in US$s

Ouch! I certainly haven't seen this chart on CNBC? Why not? Because the Sell Side are their advertisers! People might get nervous if they saw a chart like this!



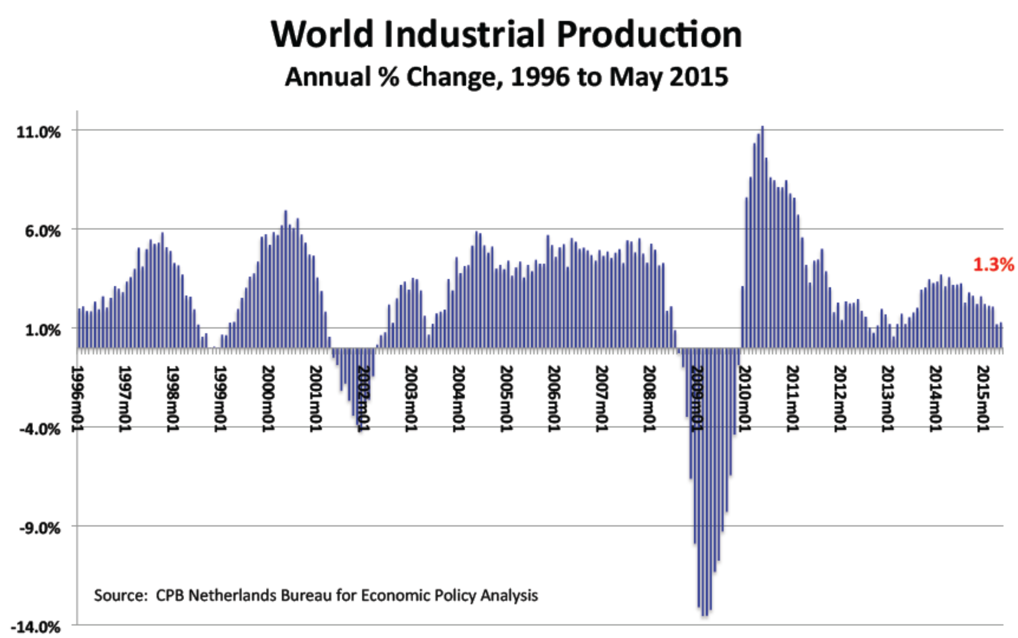
WORLD TRADE – Volumes

Let's take out price for a moment and consider just global trade volumes. The analyst's report on CNBC it may be down but that is because of currency issues. They are right to a degree then leave currencies off the table when they avoid earnings headwinds due the exchange issues associated with a strong dollar. We will get to that in a moment.



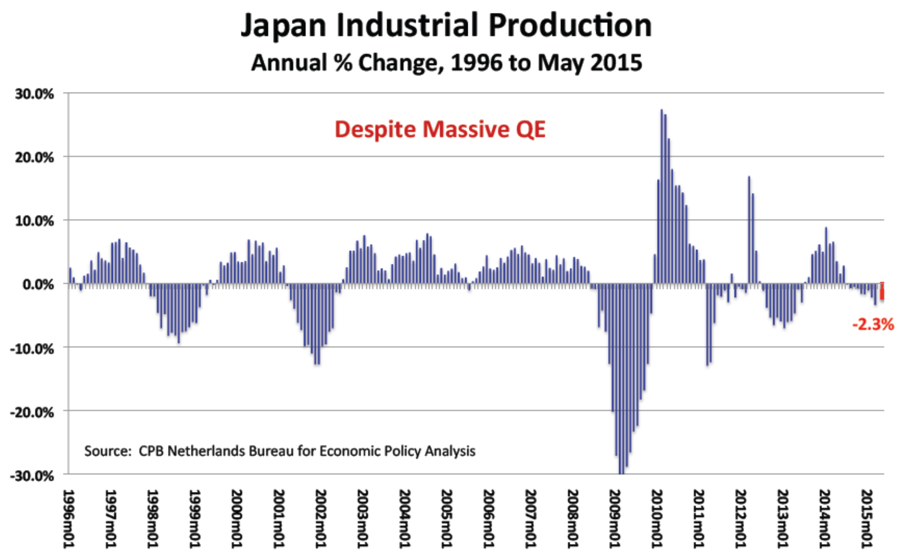
WORLD INDUSTRIAL PRODUCTION – 1.3%

Consider global industrial production versus trading products. Cheap money after the 2008 financial crisis clearly lifted production and supply. The trend has been down as it approaches contraction as demand is not there to match the ramped up supply.



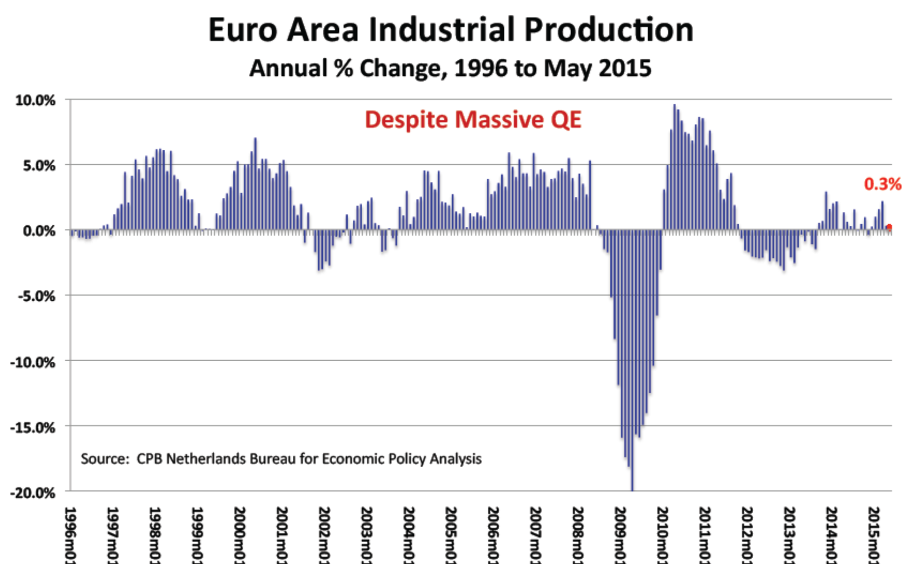
JAPAN INDUSTRIAL PRODUCTION – -2.3%

Japan's industrial production is already negative. With used car inventories a problem and 3 year lease returns about to hit the market with prices falling 7%, it doesn't bode well for the Japanese auto makers.



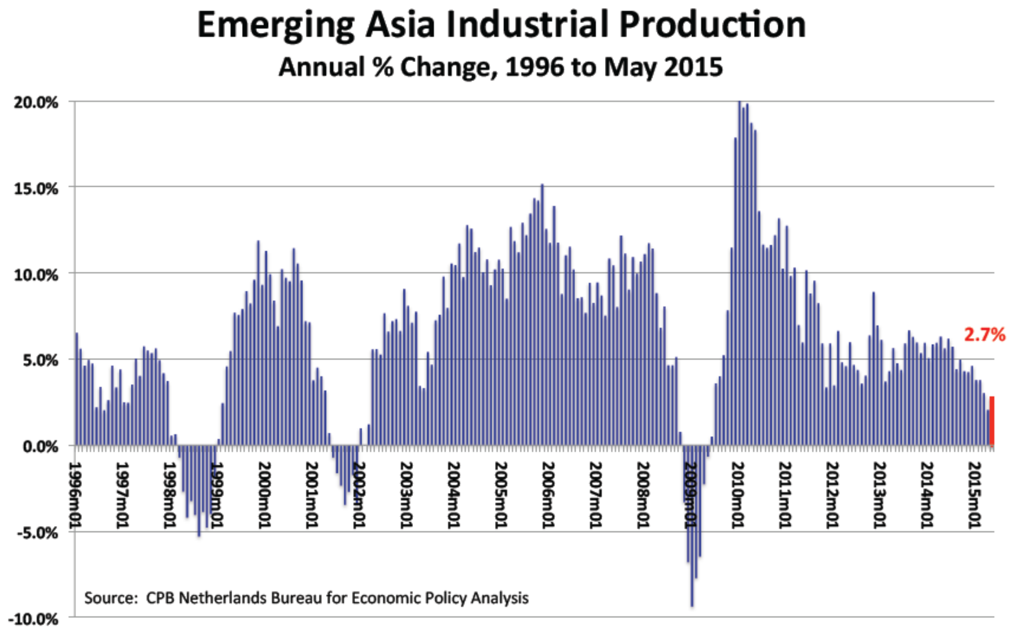
EURO AREA INDUSTRIAL PRODUCTION

The Euro area industrial production is barely positive and the same thinking can be said about all the European auto sales it is reliant on.



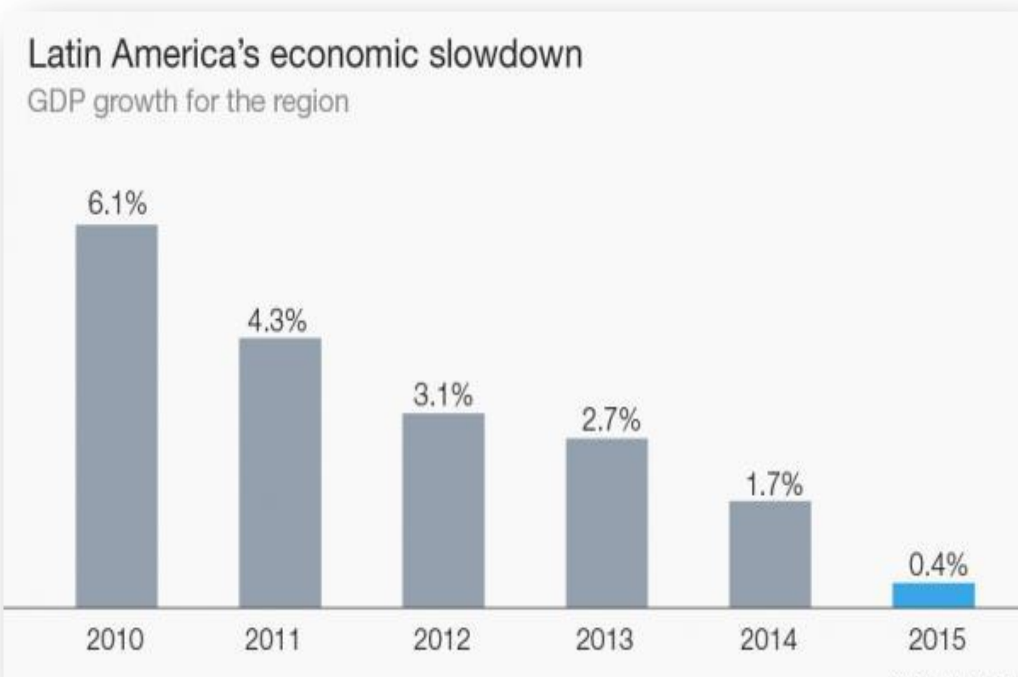
EMERGING MARKETS INDUSTRIAL PRODUCTION

Emerging markets are falling fast but look somewhat better – at least currently. We will talk about Emerging Markets more in a moment.



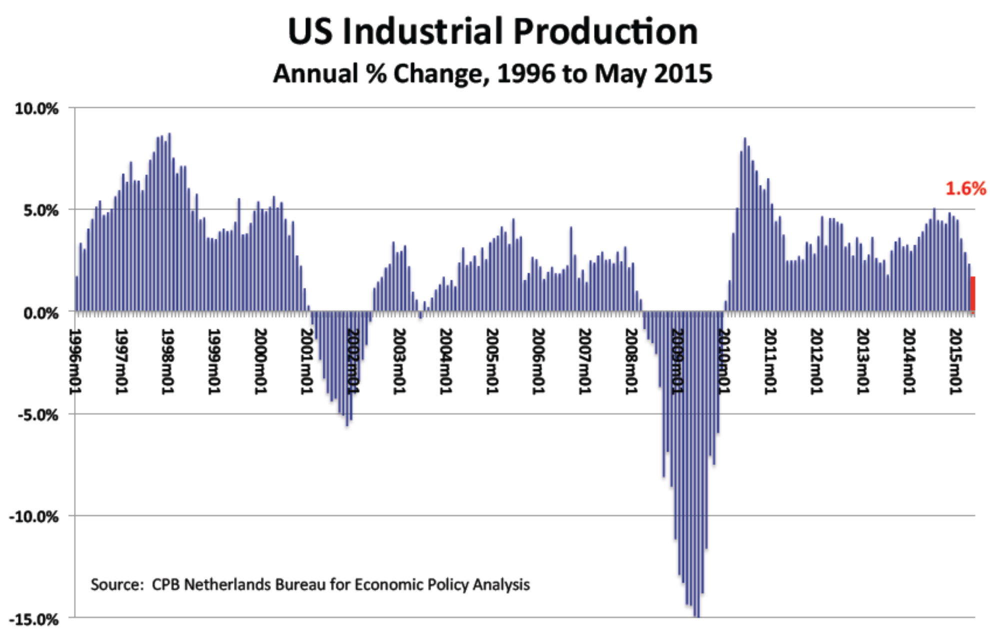
LATIN AMERICA ECONOMIC SLOWDOWN

I think this graphic of Latin America really shows the degree of problem. Brazil is already in a recession levels. Falling commodity prices are having a profound impact across all these Latin American economies so dependent on their export of commodities to the more industrialized developed economies.



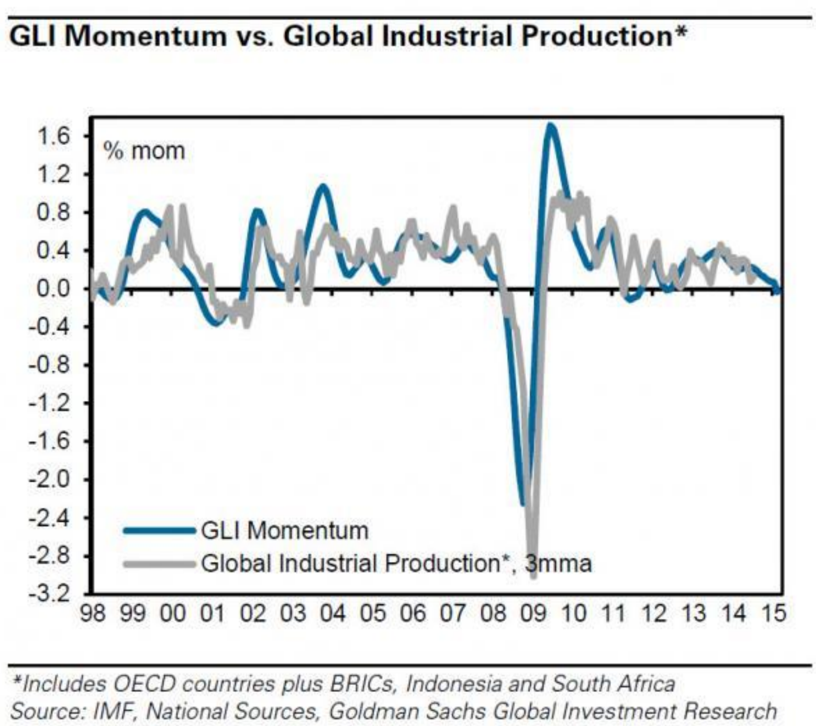
US INDUSTRAL PRODUCTION

Everyone says the global engine will be the recovering US economy. This chart and many others I have shown in these presentations suggest this is likely a flawed premise!



GLI MOMENTUM V GLOBAL INDUSTRIAL PRODUCTION

Even perennial bulls like Goldman Sachs are sending strong signals of concern, as is Deutsch Bank, Morgan Stanley and most of the other international banks. In the July GMTP report I laid out the warnings from the IMF, World Banks, OECD and BIS. Concerns are everywhere and with the US potentially raising rates and further strengthening the US dollar it has the potential to be like throwing a match on a tinder box.

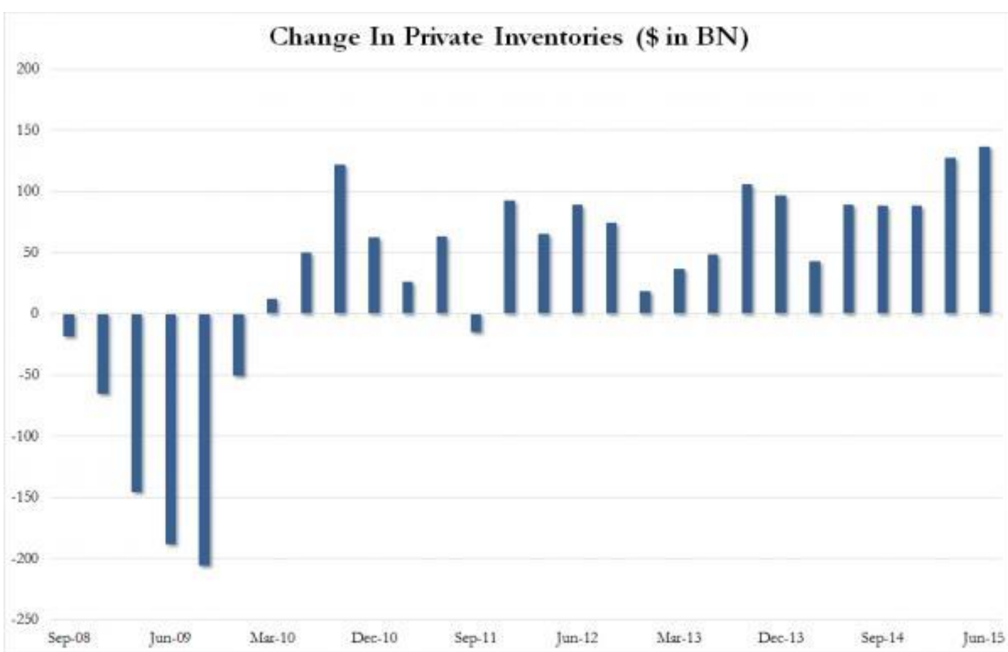


RISK OF US MANUFACTURING RECESSION

This chart from Bank of America Merrill Lynch also lays out what may be ahead regarding a possible US manufacturing recession.

CHANGE IN PRIVATE INVENTORIES

Evidence point to the fact that it has been a build out in increased inventories and stocking associated with cheap financing that has artificially held up overall industrial production.



POTENTIAL EARNINGS RECESSION

Clearly we already have a revenue recession and we are very close to an earnings recession.

Earnings in Q1 were initially reported at -0.4%

Overview

With 72% of the companies in the S&P 500 reporting actual results for Q1 to date, fewer companies are reporting actual EPS above estimates (71%) and actual sales above estimates (46%) than average.

However, the companies that are reporting upside earnings surprises are surpassing estimates by much wider margins (+6.2%) than average.

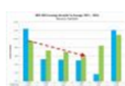
As a result of the upside earnings surprises, the blended (combines actual results for companies that have reported and estimated results for companies yet to report) earnings decline for Q1 2015 is -0.4%, which is smaller than the estimate of- 4.7% at the end of the first quarter (March 31). At the sector level, the Energy sector is reporting the largest year over-year decrease in earnings of all ten sectors, while the Health Care and Financial sectors are reporting the highest earnings growth rates for the quarter.

The blended revenue decline for Q1 2015 is -2.6%, which is unchanged from the estimate of -2.6% at the end of the first quarter (March 31). At the sector level, the Energy sector is reporting the largest year-over-year decrease in sales of all ten sectors. On the other hand, the Health Care sector is reporting the highest growth in sales for the quarter.

During the Q1 earnings season, the market will continue to watching for comments from companies regarding the impact on earnings and revenues of slower global economic growth, lower oil and gas prices, and the stronger U.S. dollar.

Looking at future quarters, analysts are expecting year-over-year declines in earnings to continue through Q3 2015. However, analysts are projecting record-level EPS for Q4 2015. Analysts also expect net profit margins to continue to rise to record levels (based on per-share estimates) starting in Q2.

The forward 12-month P/E ratio is 16.8, which is above the 5-year and 10-year averages.



Earnings Growth To Collapse Most Since 2009 In Q2
Submitted by Tyler Durden on 06/22/2015 - 13:17

"The estimated earnings decline for Q2 2015 is -4.7%. If this is the final earnings decline for the quarter, it will mark ***the first year-over-year decrease in earnings since Q3 2012 (-1.0%), and the largest year-overyear decline in earnings since Q3 2009 (-15.5%)."***

Goldman Just Crushed The "Strong Fundamentals" Lie; Cuts EPS, GDP, Revenue And Profit Forecasts
Submitted by Tyler Durden on 06/30/2015 - 22:15

To summarize: the first revenue drop for the S&P in 5 years, a major downward revision in EPS now expecting just 1% increase in 2015 EPS, a 25% cut to GDP forecasts, a machete taken to corporate profits and 10 Yields, and not to mention double digit sales declines for some of the most prominent tech companies in the world. And that, in a nutshell, is the "strong fundamentals" that everyone's been talking about.

POTENTIAL EARNINGS RECESSION

Earnings in Q2 were reported at -0.7%. It says we are very close to or already in an earnings recession. The early Q3 earnings show the trend continuing.

During the first two months of the third quarter, analysts lowered earnings estimates for companies in the S&P 500 for the quarter. The Q3 bottom-up EPS estimate (which is an aggregation of the estimates for all the companies in the index) dropped by 2.7% (to $29.25 from $30.06) during this period.

FACTSET
EARNINGS INSIGHT

John Butters, VP, Sr. Earnings Analyst
jbutters@factset.com

Media Questions/Requests
media_request@factset.com

S&P 500 September 4, 2015

Key Metrics

- **Earnings Scorecard:** Of the 495 companies tha~~t have reported e~~arnings to date for Q2 2015, 74% have reported earnings above the mean estimate and 51% have reported sales above the mean estimate.
- **Earnings Growth:** For Q2 2015, the blended earnings decline is 0.7%. The last time the index reported a year-over-year decrease in earnings was Q3 2012 (-1.0%).
- **Earnings Revisions:** On June 30, the estimated earnings decline for Q2 2015 was -4.6%. Nine sectors have higher growth rates today (compared to June 30) due to upward revisions to earnings estimates and upside earnings surprises, led by the Health Care sector.
- **Earnings Guidance:** For Q3 2015, 77 companies have issued negative EPS guidance and 30 companies have issued positive EPS guidance.
- **Valuation:** The 12-month forward P/E ratio is 15.3. This P/E ratio is based on Thursday's closing price (1951.13) and forward 12-month EPS estimate ($127.76).

POTENTIAL EARNINGS RECESSION

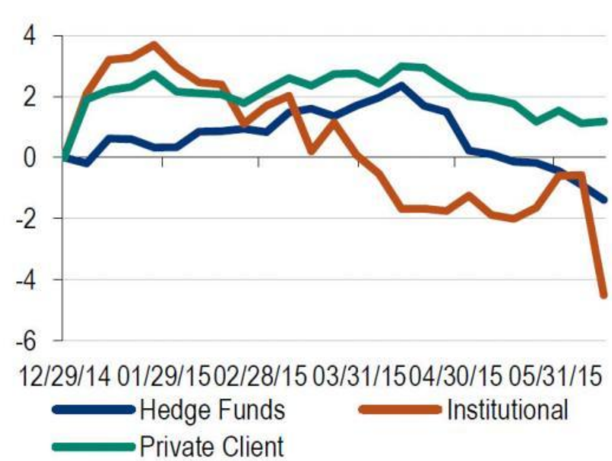
HEADLINE

Wall Street braced for profit declines

HEADLINE

The -Smartest Money- Is Liquidating Stocks At A Record Pace- -Selling Everything That's Not Bolted Down-

Chart 2: YTD cum. flows by client type ($bn)

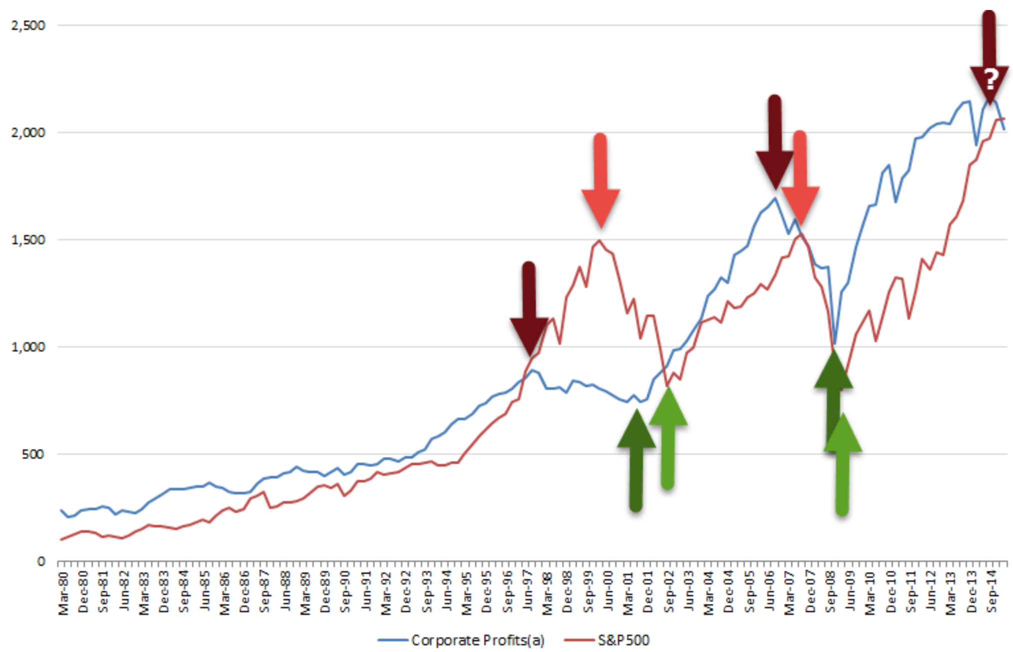


Source: Bank of America Merrill Lynch

POTENTIAL EARNINGS RECESSION

HEADLINE

The Corporate Earnings Cycle Has Just Turned Negative in the US



The Coming US Recession Charted

Submitted by Tyler Durden on 06/20/2015 - 20:15

The idea of an imminent US recession may seem moot as all the self-proclaimed experts and talking heads still acts as we are well into a recovery and patiently waiting for the forthcoming escape velocity which will take care of all ills plaguing today's over-indebted society. Never do they stop to think about why things looks as dismal as they do. The **sheer scale of the backwardness** shown in such gross economic illiteracy suggest to us there is ulterior motives behind so-called Keynesian economic theories. *Comparing GDP with cumulative goods sold and inventory accumulation since 2000 should tell you everything you need to know.* **The US economy is now on the verge of a new recession.**

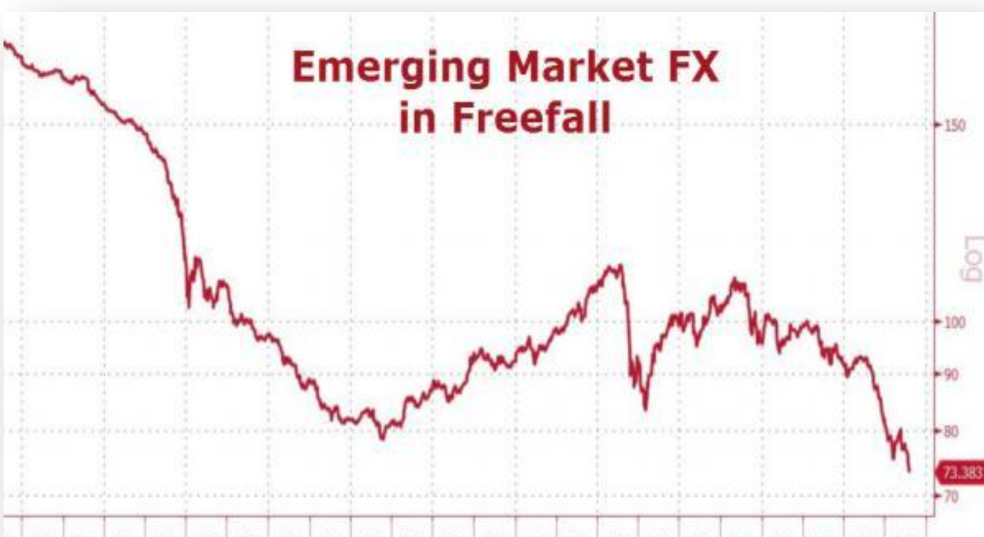
US DOLLAR SQUEEZE – *A $9T Problem*

ASIAN DOLLAR INDEX

The crisis across Emerging Markets and Asia is emblematic of previous crisis. Maybe even worse!

EMERGING MARKET FX FREEFALL

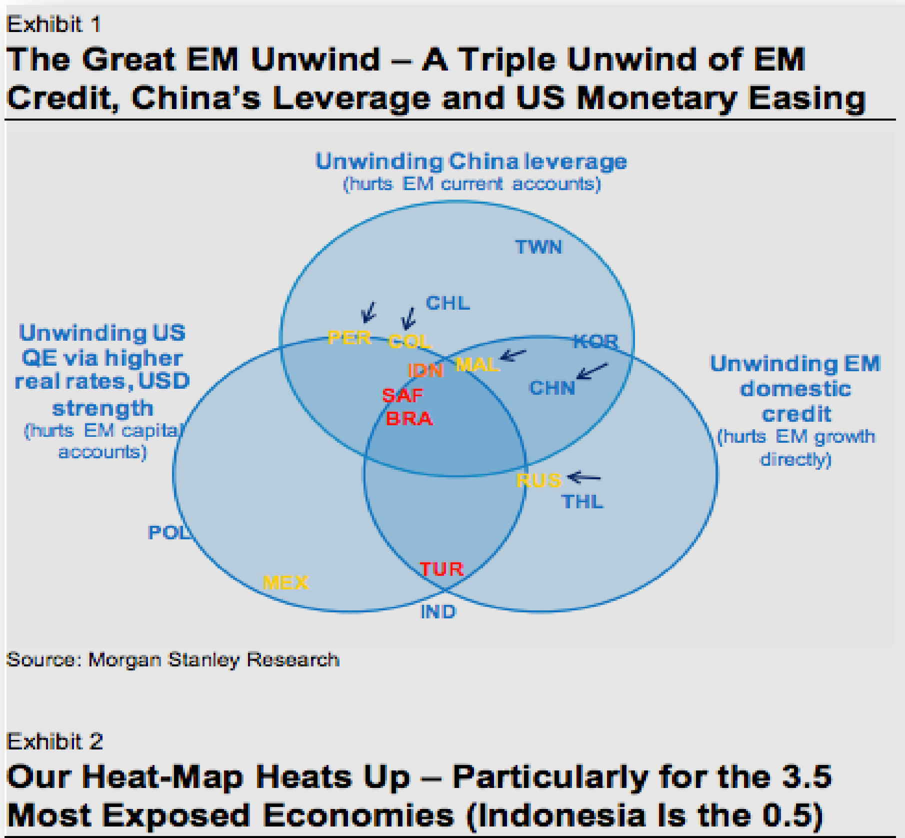
It more than just about debasement of currencies that are being used to gain economic advantage. It is actually capital and hot money leaving which is pushing down the currencies and by default pushing up the US dollar.



We also have Emerging Markets on the wrong side of a $9T USD Carry Trade. We have effectively a global short squeeze on against those who were betting on its demise.

THE GREAT EM UNWIND

What is called the “Great EM Unwind” is underway. A triple unwind of Emerging Market Credit, China’s massive unregulated and uncontrolled financial leverage and the threat of US Monetary Easing by the Federal Reserve.



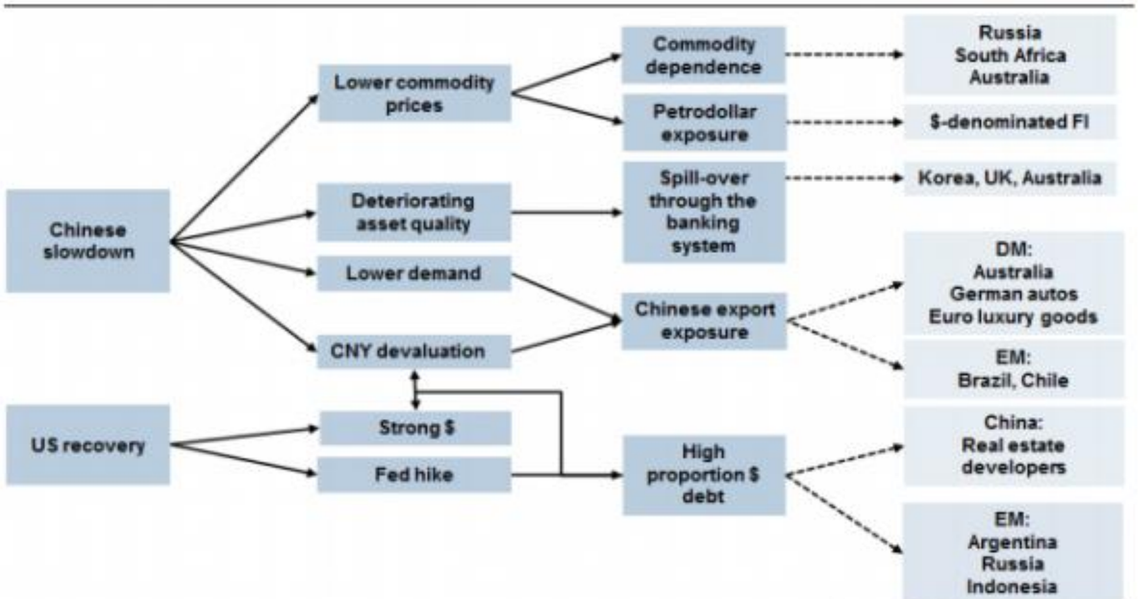
US DOLLAR STRENGTH

The strength of the US dollar has been almost parabolic since the Federal Reserve’s “TAPER” program was enacted

CHINESE CONTAGION

If all this is bad enough we have the global manufacturer with a 1929 level market crash and dramatically slowing economy with numerous points of contagion threatening.

Mapping Chinese contagion



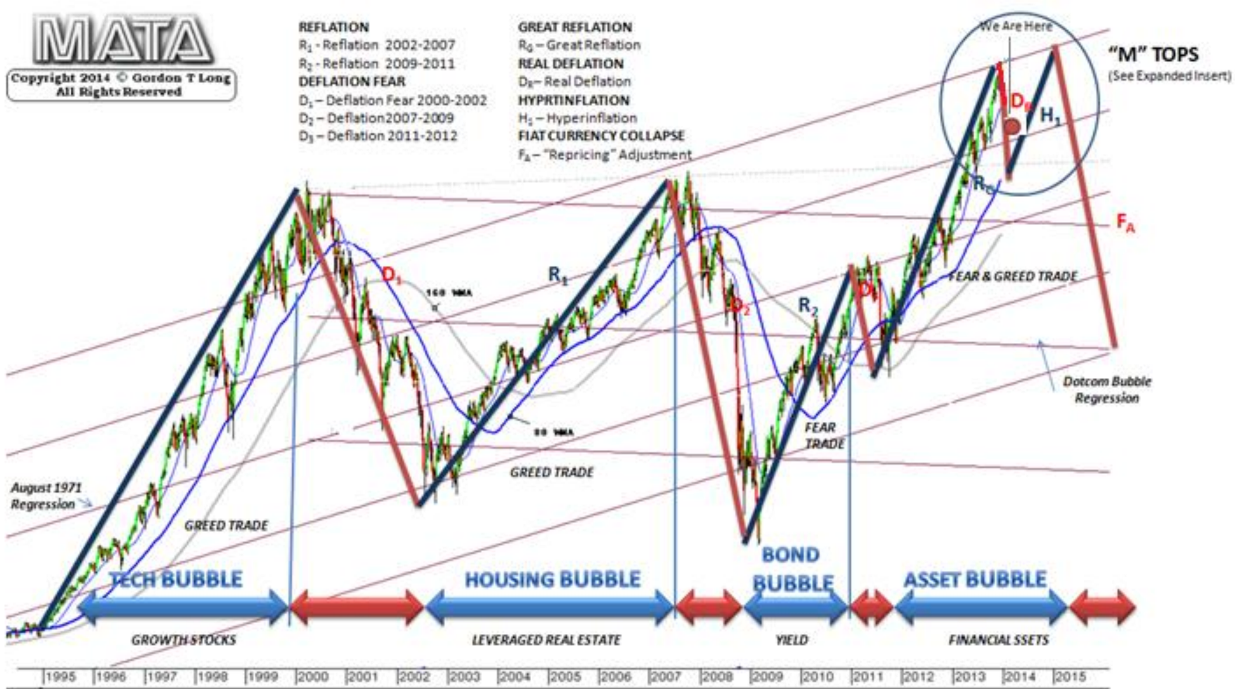
Source: RBS Macro Credit Research

REAL DEFLATION – *Our "M" Top Revisited*

"M" TOP – Revisited

I have shown this chart "M" chart many times over the last year and a half. The current leg down is the Real Deflationary leg which I warned of in the Globalization Trap. It is fundamentally about excess supply from cheap money which results in a commodity collapse, lose of pricing power and the export of deflation to the US in terms of asset value and to some degree products. The US inflation will be primarily in what people need (versus want), don't finance and are domestically centered. All types of home and professional services, healthcare etc fall in this range, which are increasing by 6-8% per year.

Note before we leave this chart that the regression lines with standard deviations start in August 1971. This is labeled on the far left side of the chart.



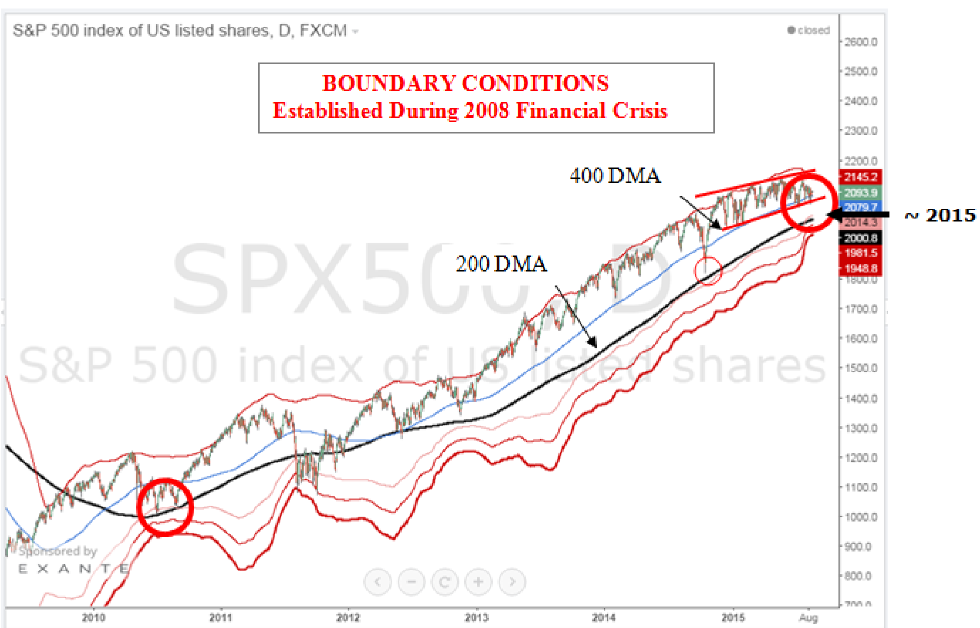
PRICING PRESSURES

This chart is the previous schematic chart in actual real time available on Triggers. Again, it shows the regression lines going back to 1972 when the US dollar became a Fiat Currency.

We the central bankers will step in, in a massive coordinated way with "helicopter" money and collateral guarantees before or as we approach the long term red regression.

DECAY VORTEX

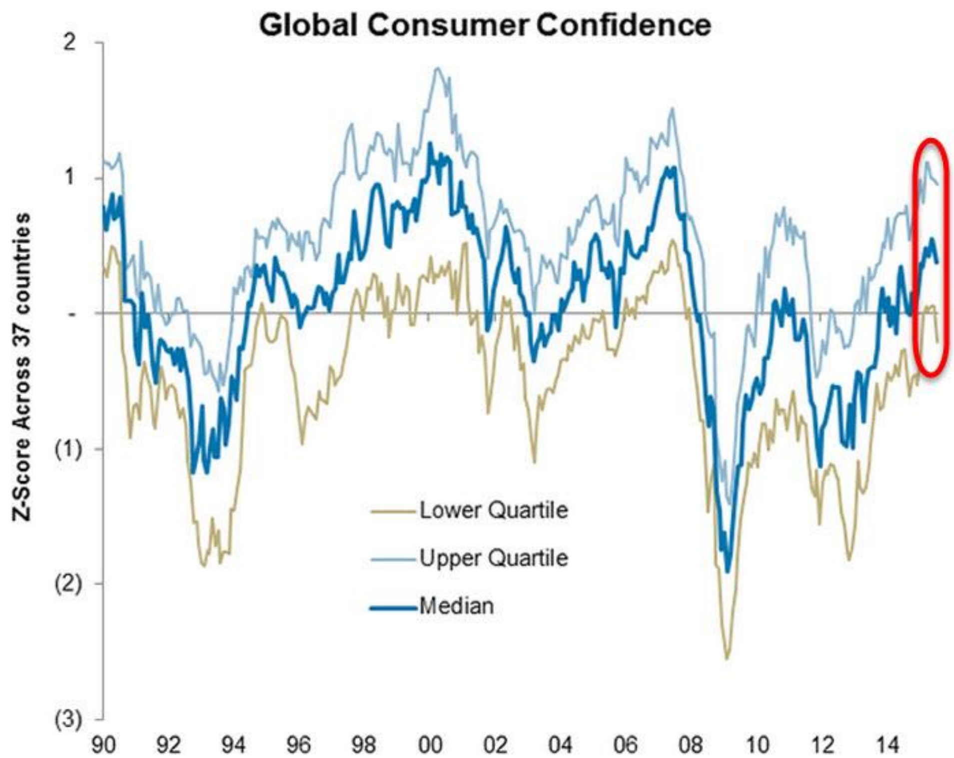
What this chart shows the boundary conditions established by trading volatility during the 2008 financial crisis. We believe they show a similar lower limit around 2015 in the S&P 500 index.



WHAT TO EXPECT

GLOBAL CONSUMER CONFIDENCE

Alan Greenspan often testified before congress that sentiment and confidence shifts were the one thing he wished he could predict and control. They determined economic directional shifts. We are seeing this shift occur globally ….



US ECONOMIC CONFIDENCE

….. and we have seen this beginning to change in the US since Q1 2015. It is very cyclical in nature and needs to be carefully watched.

U.S. Economic Confidence Index -- Weekly Averages Since August 2014

Latest results for week ending Aug. 30, 2015

Gallup U.S. Daily tracking

GALLUP

ENERGY & COMMODITIES

It cannot be understated what the impact of falling oil prices has on the economies of many export economies. They are being forced to issue bonds or sell assets because of falling current accounts. This reduces the massive petrodollar profits flows into the global financial system.

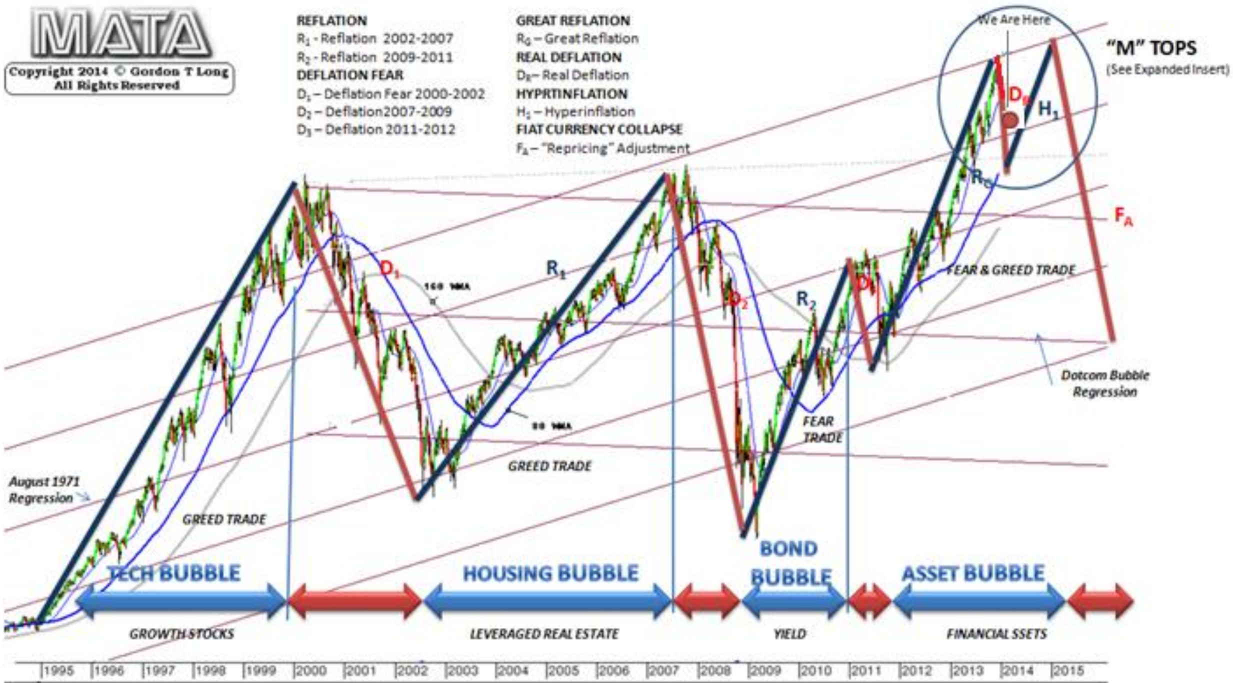
KEY SUPPORT LEVELS

As we have pointed out in previous MATA reports we believe the anticipated fear will be contained within the rising trend channels shown here – at least through early fall.

FINAL LIFT

As I said, we believe the Real Deflation leg is well underway. It has been clear in the commodities market since the beginning of TAPER. It has only recently become evident to the US equity markets. When the Fed is forced into QE4, helicopter money or collateral guarantees we can expect real elevated Inflation and the strong possibility of eventually seeing Hyperinflation.

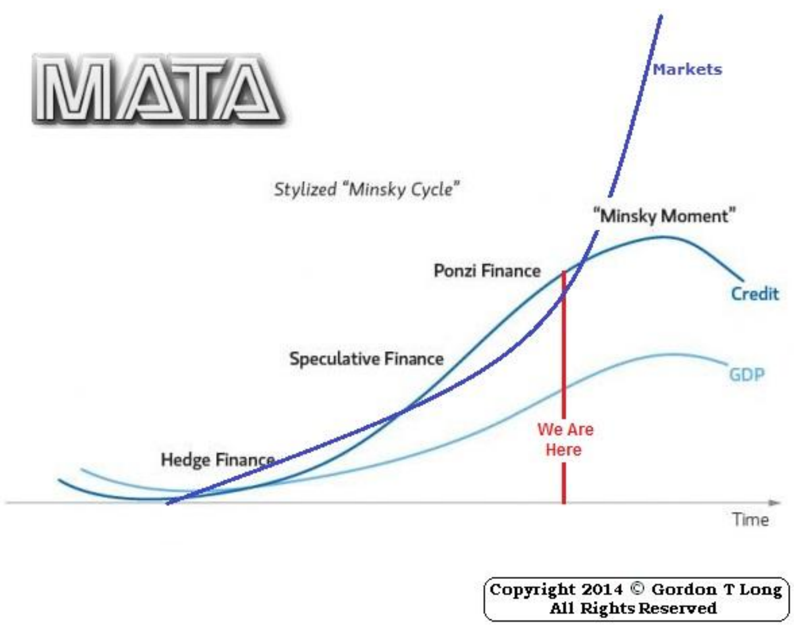
As I am aft to keep saying, never forget, Hyperinflation is a Currency Event which explodes prices higher as confidence in the currency is lost. It will be about lost confidence in the US dollar, or possibly the replacement of the US$ as the dominant global currency during a de-dollarization event.



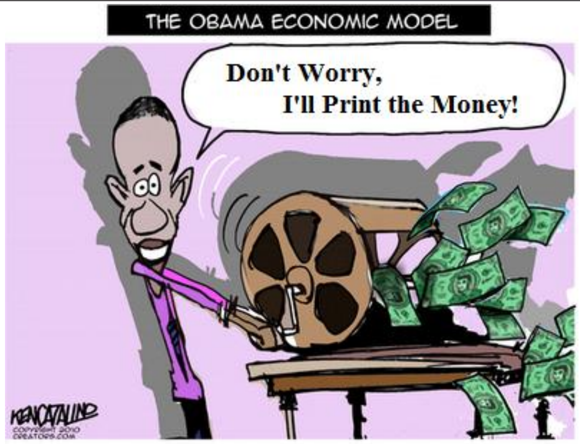
WHAT LIES AHEAD – Our Sense

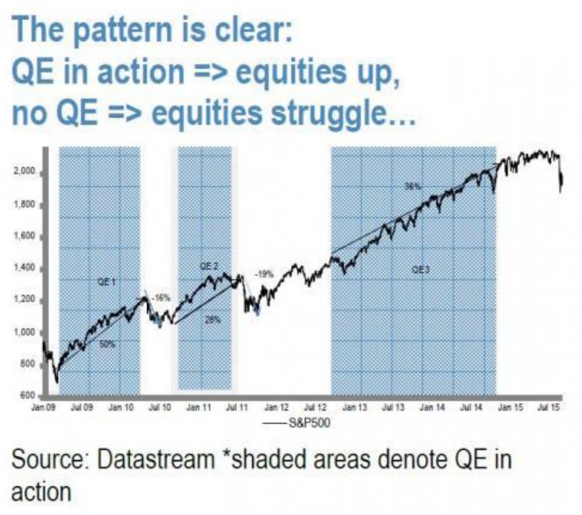
Let me reiterate, I continue to fully expect a Minsky Melt-up before all this ends very badly in mid 2016.

Eventually, it will be clear to all that central bank policies have been a failure. The government's policy of Financial Repression are becoming too heavy handed as productivity falls, high paying jobs disappear and tapped out consumer demand steadily slows.



In closing I would like take a moment as a reminder





Gordon T Long
Publisher & Editor
general@GordonTLong.com