

# MARKET SIGHT LINES



## **Animal Spirits Are in Focus: A Look at Some Soft and Hard Data**

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We've spent the last number of weeks discussing various potential economic and market scenarios for this year, including the concept of Animal Spirits, or the emotions and instincts that drive economic growth and market behavior. Lately there is an increasing risk that the Animal Spirits of consumers and business leaders may be weakening, as they may be increasingly worried about the uncertainty of things like tariffs and government layoffs. In this week's Sight|Lines, we review some "soft" and "hard" economic and market data to better understand how things are unfolding.

### **THE TAKEAWAY: THE "HARD" DATA REFLECTS CONTINUED STRENGTH, BUT "SOFT" DATA SIGNALS A POSSIBLE SLOWDOWN**

As we monitor the impact of policy changes in Washington, it is helpful to look at both "soft" economic data, which reflects sentiment and expectations, as well as "hard" data, which measures actual economic outcomes. In summary:

- The consumer continues to benefit from a solid labor market, including increasing wages, and this is contributing to solid retail sales over the last year.
- Consumer survey data is weakening, but some data remains positive and other data negative as it relates to an assessment of the overall environment.
- Business activity remains positive, with profits and earnings growth remaining solid and industrial production growing, year over year.
- Business survey data is showing business sentiment is softening, but still positive.
- Consensus forecasts for the economy remain positive, although we expect some softening.
- Consensus forecasts for earnings growth and future stock market levels also remain positive, but we are anticipating a softening in this data as well.
- Stock market performance is often one of the more important leading economic indicators, and recent market weakness may well be reflecting investors' worry about a potential recession and more precipitous decline in company profits and earnings.

While there has been increased uncertainty around tariffs and government layoffs, so far the data is showing worries about a pending recession may be overdone.

## **IN-DEPTH: “HARD” ECONOMIC DATA IS REFLECTING STRONG FUNDAMENTALS, BUT SOME “SOFT” ECONOMIC DATA IS SIGNALING WORRIES OF A SLOWDOWN**

As we look to gauge the impact of Washington policy changes, some "soft" economic data, which reflects sentiment and expectations, is signaling a possible slowdown, even as "hard" data, which measures actual economic outcomes, is still showing strong fundamentals. Going deeper:

- The labor market and consumer activity remain strong:
  - Unemployment sits at 4.1%, with initial jobless claims and nonfarm payrolls holding steady.
  - Retail sales were up 4.2% over the year ended January.
- Consumer survey data is weakening, but mixed:
  - The Conference Board Consumer Confidence Index declined in February (98.3) but remains positive.
  - The University of Michigan Consumer Sentiment Index also declined (64.7), but in this case to more negative levels on worries about tariffs and inflation.
- Business activity remains positive:
  - In 2024, S&P 500 revenue rose 5.1%, and earnings growth is estimated to have been 10.6%.
  - Industrial production rose 2% during the year ended January.
- Business survey data is showing business sentiment is softening, but still positive:
  - The Institute for Supply Management (ISM) Manufacturing Purchasing Managers' Index (PMI) fell to 50.3 in February.
  - The ISM Services PMI rose to 53.5, showing both readings signaling expansion.
  - The Conference Board CEO Confidence Survey rose to 60, the highest level in three years.
  - The National Federation of Independent Business Small Business Optimism Index fell to 100.7, also softening, but modestly positive.
- Consensus forecasts for the economy and stock market remain positive:
  - The consensus GDP 2025 growth forecast sits at 2.3%.
  - Consensus earnings growth remains healthy at 11.3%.
  - The average year-end S&P 500 forecast is 6,501, reflecting a 17% return from current levels.
- Stock market performance is often seen as an important leading economic indicator:
  - The S&P 500 has declined 9.0% from its highs in February and is down 5.0% year to date.
  - Recent market weakness seems to reflect investors' worries about a potential recession and a related decline in company profits and earnings, but for the moment, this may be overdone.

### **CONCLUSION**

Over recent weeks we've discussed various potential economic and market scenarios for this year: positive, neutral, and negative. We've often referred to how Animal Spirits, or the emotions and instincts that drive economic growth and market behavior, play a role. Some "soft" economic data is signaling an increasing risk that the Animal Spirits of consumers and business leaders may be weakening, but "hard" economic data still reflects strength. Since "soft" data results are sometimes a precursor to "hard" data results, a careful monitoring of the environment is warranted, and we will share updates regularly.

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**Figure 1. Hard vs. Soft Economic & Market Indicators**

Category	Indicator/Measure
<p><b>SOFT DATA</b> <i>reflects sentiment and expectations</i></p>	<p>ISM Manufacturing PMI ISM Services PMI NFIB Business Optimism Index Conference Board Consumer Confidence Index University of Michigan Consumer Sentiment Index Conference Board CEO Confidence Index Consensus Forecasts for GDP &amp; Company Earnings</p>
<p><b>HARD DATA</b> <i>measures actual economic outcomes</i></p>	<p>Unemployment Rate Retail Sales Industrial Production S&amp;P 500 Revenue &amp; Earnings Results</p>

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Asset allocation and diversification do not ensure a profit and may not protect against loss. There are special considerations associated with international investing, including the risk of currency fluctuations and political and economic events. Investing in emerging markets may involve greater risk and volatility than investing in more developed countries. Due to their narrow focus, sector-based investments typically exhibit greater volatility. Small company stocks are typically more volatile and carry additional risks, since smaller companies generally are not as well established as larger companies. Property values can fall due to environmental, economic, or other reasons, and changes in interest rates can negatively impact the performance of real estate companies. When investing in bonds, it is important to note that as interest rates rise, bond prices will fall. The Standard & Poor's 500 index is a capitalization-weighted index that is generally considered representative of the U.S. large capitalization market. The Dow Jones Industrial Average (DJIA) is a price-weighted average of 30 significant stocks traded on the New York Stock Exchange (NYSE) and the NASDAQ. The DJIA was invented by Charles Dow back in 1896. The MSCI EAFE index (Europe, Australasia, and the Far East) is a free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the U.S. and Canada. The National Federation of Independent Business Small Business Optimism Index measures the overall optimism and outlook of small business owners regarding the economic conditions, sales expectations, hiring plans, and capital expenditures. It provides valuable insights into the sentiment of small businesses, which are a vital component of the U.S. economy. VIX is a trademarked ticker symbol for the Chicago Board Options Exchange Market Volatility Index, a popular measure of the implied volatility of S&P 500 index options. The Conference Board Measure of CEO Confidence™ is a barometer of the health of the U.S. economy from the perspective of U.S. chief executives. The measure of CEO confidence is based on CEOs' perceptions of current and expected business and industry conditions. The survey also gauges CEOs' expectations about future actions their companies plan on taking in four key areas: capital spending, employment, recruiting, and wages.

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