



The plan ... meets the signal!

The plan meets the signal

Every month, we put our plan on paper.

We study the rate of change in growth and inflation, compare the incoming data with forward monthly projections and nowcasts, and describe the economic environment we believe has the highest probability of developing. We do it publicly because a plan is more useful when readers can see the reasoning behind it ... and what happens when new information arrives.

But the plan is only one part of our process.

We also follow the signals ... of a multi-factor model based off the rate of change in price, volume, and volatility ... to determine whether markets are behaving as the plan would suggest.

When the signals change, we have to be willing to adjust with them ... signals > quads!

In August's *The Audible*, our working path called for growth to begin accelerating in September while inflation decelerated. That combination pointed toward Quad 1.

Growth appears to be accelerating.

Inflation, however, is no longer following the path we expected.

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Based on the most recent data and nowcasts, both rates of change now point toward acceleration ... making Quad 2 (reflation) the more probable September environment.

That is an adjustment to the plan. It is also the reason we put the plan on paper in the first place.

Growth ... look beneath the headline

If you looked only at August's headline durable goods report, you might wonder what all the excitement is about.

New orders were essentially unchanged MoM, while their YoY growth rate decelerated -330 basis points to +8.5%.

That sounds like a slowdown.

Dig a little deeper, though, and the rate of change looks considerably more interesting.

Core capital goods orders increased +1.6% MoM and accelerated +80 basis points to +14.1% YoY ... a five-year high in their YoY growth rate, according to the latest data set.

Orders for durable goods excluding defense and aircraft increased +0.3% MoM and remained +10.3% YoY. That annual rate did decelerate -20 basis points from the prior month, so we should not describe every underlying series as accelerating. But it remains near the high end of this cycle.

How can the headline be flat while core capital goods are accelerating?

Private aircraft and parts orders fell -4.3% MoM and were -19.5% YoY. Aircraft orders are volatile. The headline's YoY comparison also became more difficult as the year-earlier growth rate rose from +3.3% to +7.7%. Both factors weighed on the headline's reported rate of change.

Meanwhile, some of the strongest annual gains were concentrated in areas that matter to the current investment cycle:

- Defense capital goods orders: +34.6% YoY
- Defense search and navigation equipment: +19.2% YoY
- Computer and electronic manufacturing: +16.5% YoY
- Primary metals: +20.1% YoY

That combination is consistent with the strength we have been watching in AI investment, industrial capacity, and defense related spending.

It also calls for some care in our interpretation. Strong orders in these categories do not mean every corner of the economy is accelerating at the same speed ... as housing remains weak given the current uncomfortable level of mortgage rates.

Some manufacturing surveys have stronger headline readings than their underlying new orders or shipments would suggest ... and a surge in capital investment should not automatically be mistaken for an equally strong consumer market.

The bottom line is that we do not need every data series to move in perfect unison to recognize an economic shift.

Our primary question as it relates to growth remains ... **is its rate of change improving?!**

A flat durable goods headline, a modest deceleration in one underlying annual series, and a sharp acceleration in core capital goods can all be true at once. Taken together with the other incoming growth signals, the newer capital investment data add meaningful support to the acceleration case.

So far, that is the part of our September plan, outlined in August, that appears to be playing out.

Inflation ... the Other Side of the quad

The larger change is inflation.

To understand why, it helps to follow the sequence rather than focus on a single CPI print. Headline CPI reached +4.25% YoY in May. It then slowed to +3.53% YoY in June and +3.36% YoY in July. That was a cumulative -89 basis point deceleration from May to July.

By August, that downward progression had stopped. Headline CPI edged up to +3.40% YoY ... a +4-basis point acceleration from July.

On its own, four basis points would hardly settle an argument about the next economic environment. The September trajectory has since moved considerably.

WTI spot crude fell roughly 10% from September 15 to September 23. Despite that retreat, Hedgeye's latest headline CPI nowcast still calls for +3.74% YoY in September. If realized, that would be a further +34 basis point acceleration from August and would put the annual rate +38 basis points above July's low.

The base case has risen +7 basis points since Hedgeye's September 21 update. That change in the estimate is itself information: as more of the month's inputs became available, the expected inflation rate moved higher.

Hedgeye's current range also points in the same direction:

September headline CPI scenario	Estimated YoY rate	Change from August's +3.40%
Downside	+3.63%	+23 basis points
Base case	+3.74%	+34 basis points
Upside	+3.85%	+45 basis points

Even the downside estimate would represent a meaningful acceleration from August.

Let's be precise: September CPI has not been reported. The official release is scheduled for October 14.

These are estimates, and estimates can change. We are describing the current trajectory, not presenting the September figure as an accomplished fact ... though, Hedgeye's monthly inflation nowcast is updated weekly ... and has reported approximately 90% directional accuracy from the onset of initially publishing their monthly nowcast.

That being said, markets do not wait for every backward-looking number to become final before it begins repricing the probable path ahead.

In August, our September framework anticipated growth accelerating while inflation decelerated:

Growth ↑ / Inflation ↓ = Quad 1

The newer growth data and inflation trajectory suggest a different combination:

Growth ↑ / Inflation ↑ = Quad 2

The important change is not simply that inflation remains above a particular level. It is that, after decelerating from May through July, its YoY rate of change turned modestly higher in August and is now estimated to accelerate more sharply in September.

That is the audible.

What the market is saying ... and who is speaking?

Several market signals have moved in a direction which supports the changing Quad assessment.

In the latest research, the U.S. Dollar Index was up **+0.8% WoW** and **+2.1% over the prior month**. Treasury yields rose across the curve over that same month, with the **2-year yield up +67 basis points**, the **10-year up +53 basis points**, and the **30-year up +33 basis points**. Gold weakened as the dollar and yields advanced.

The Federal Reserve also raised its target rate by **25 basis points** at its September meeting.

Those developments deserve attention. Yet we should be careful about turning any one market price into a complete explanation of the economy.

Mike Green's recent work raises a useful question: **Who, or what, is producing the price we are treating as a signal?**

A Treasury yield reflects the interaction of growth and inflation expectations with Treasury issuance, benchmark rules, institutional mandates, futures positions, leverage, and the capacity of intermediaries to absorb risk. Federal Reserve researchers have documented how some mutual funds use Treasury futures to obtain benchmark-related duration and how hedge funds often take the other side of those positions.

That does **not** prove passive or benchmark-related flows caused the recent increase in yields. Nor does it tell us how much of a particular move came from economic news versus market structure.

For us, the distinction is practical. The growth and inflation data help identify the probable Quad.

Price, volume, and volatility help us evaluate how markets are responding and whether our positioning still fits what is happening in real time. As noted above, we place a greater emphasis on the market signal ... and while remaining curious about the forces behind them ... the "why" leaves more room for interpretation as well as error.

Narrow breadth ... don't guess?!

The same principle applies to individual equities.

As of September 28, Barchart's measure showed 43.93% of S&P 500 stocks above their simple 200-day moving average. Put differently, roughly 56% were below that long-term trend measure.

While this is a single measure of breadth, it does suggest market participation has narrowed. It does not tell us that 56% of stocks suffered a "Wall Street" defined correction, and it does not tell us what the index must do next.

While some investors see poor breadth and conclude the market is about to break. Others notice that breadth has become such a popular worry that they begin looking for a rebound. Either outcome is possible.

Rather than guess ... we follow our signals ... allowing them to guide our next move.

Does participation improve as the Quad 2 growth data continue to arrive? Do more stocks begin confirming the move? Or does the index remain dependent on a smaller group of companies while the broader market weakens?

Those are questions the signals can help answer. A compelling narrative about breadth cannot answer them in advance.

The next read

Hedgeye's current forward Quad count suggests a greater persistence of Quad 2 conditions than its earlier 3-1-2 path implied. The updated monthly sequence is **2-2-1-2-2 from September through January** ... four of the next five months tracking toward Quad 2.

That is useful as a working map ... and, like every forward map, it is subject to change.

Our immediate checkpoints are more concrete:

- Does the October 14 CPI release confirm the September inflation acceleration now being estimated?
- Do incoming growth data continue to show acceleration beyond the strongest capital investment categories?
- Do the dollar, yields, sector leadership, and market breadth continue to confirm the environment ... or begin to diverge from it?
- What do price, volume, and volatility tell us as those data arrive?

We will not defend an old Quad simply because we published it last month. We also will not assume that a new Quad lasts indefinitely because the latest readings support it.

Every month, we put the plan on paper.

Every day, we watch the signals.

Final thoughts

In August, we wrote: "Be stubborn about the process ... flexible about the conclusion."

Following our signals through September was a test of whether we meant it.

The growth acceleration we anticipated has gained support. The expected inflation deceleration has not.

Hedgeye's latest September nowcast points instead to a meaningful acceleration, shifting our working assessment toward Quad 2.

At the same time, our signals led us to reduce exposure in both individual small cap equities as well as the Russell 2000 at the index level itself ... while increasing exposure to large cap growth.

Here's the rub ... small caps typically outperform in Quad 2 ... how flexible can you be?!

Just because something is "typical" doesn't mean it's set in stone!

The Fed has acted. Bond yields and the dollar have risen. Market breadth has narrowed. Each adds information ... and each requires interpretation within the larger process.

We do not get paid for insisting that August's September forecast was right. We don't remain in a position simply because it "should" be working in the respective Quad. We are responsible for recognizing when the probabilities change and adjusting our conclusions accordingly.

That same discipline belongs in a financial plan. We can map retirement income, spending, investments, taxes, insurance, and the needs of a family using the best information available today. Then life ... and markets ... supply new information.

A retirement date moves. Healthcare costs change. One spouse retires sooner than expected. The income plan that made sense a few years ago may need an adjustment today.

A plan gives us direction. A process tells us when to make an adjustment.

When was the last time your plan was tested against the life you're living now ... and the retirement you're preparing for?

If something has changed ... or you simply want to understand where you stand ... [Schedule your free consultation today.](#)

As always ... Good investing!



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