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# March - April Combined Surveys Analysis

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## Sample Intelligence Report: March–April 2025

Welcome to a real Signalgeist report. This is the kind of early insight, deep analysis, and second-order trade strategy our subscribers receive every week.

What you'll find below:

- Breakdown of sentiment surveys across consumers, small businesses, and manufacturers
- First- and second-order economic effects
- Actionable trade ideas and sector outlooks. This is **what it means to be early**.

### **Consumer Confidence Decline: How to Trade the Coming Slowdown**

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#### **Subscribers, brace yourselves.**

Consumer and business confidence is collapsing across the board – and that means opportunity for those who understand what comes next. We've just dissected the latest University of Michigan Sentiment Index, Conference Board Confidence Report, NFIB Small Business Survey, and Regional Fed Manufacturing Outlooks.

Our synthesis reveals cracks forming in the U.S. economic psyche – and we're turning those cracks into **concrete, tradable signals**.

### **Key Survey Signals & Takeaways:**

- **Consumer Sentiment Plunges:** U. Michigan's index falls 11% to 50.8 – the lowest since the Great Recession.
- **Inflation Fears Spike:** 1-year inflation expectations now at 6.7%, highest since 1981.
- **Small Biz Turns Bearish:** NFIB optimism dips below 51-year average; hiring plans fall.
- **Manufacturers Contract:** Philly Fed index at -26.4, Empire State outlook hits historic pessimism.
- **Everyone Sees Job Losses Coming:** 67% of consumers now expect higher unemployment.
- **Tariffs Creating Price Shock:** Businesses and consumers brace for inflation from new trade war.

### **First-Order Effects (Immediate Impacts):**

| Effect                                                                                                          | What It Means                                            |
|-----------------------------------------------------------------------------------------------------------------|----------------------------------------------------------|
|  Discretionary Spending Down | Consumers pull back on big-ticket and non-essentials.    |
|  Business Capex Cut          | Industrials and Tech hit by reduced investment.          |
|  Price Hikes Ahead           | Businesses pass on costs → inflation sticks.             |
|  Rotation to Defensives      | Expect outperformance in Utilities, Staples, Healthcare. |
|  Tighter Lending             | Banks pull back, credit dries up for riskier borrowers.  |

### **Second-Order Effects (Ripple Impacts):**

-  **Margin Compression:** Retailers & manufacturers squeezed between costs and weak demand.
-  **Inventory Glut Risk:** Declining orders + bloated inventories = production cutbacks ahead.

-  **Credit Risk Rising:** More defaults, tighter standards—watch small biz and consumer credit.
-  **Sticky Fed Rates:** High inflation expectations = continued hawkish Fed.
-  **Sector Shockwaves:** Auto suppliers, REITs, regional banks in danger zones.
-  **Market Volatility Incoming:** Consumers turning bearish on stocks → VIX could pop.

| Position                                                                                       | Asset / Sector                             | Rationale                                         |
|------------------------------------------------------------------------------------------------|--------------------------------------------|---------------------------------------------------|
|  Short        | XLY – Consumer Discretionary               | Confidence crash + inflation = spending cuts      |
|  Long         | XLP – Consumer Staples                     | Resilient demand + pricing power                  |
|  Short        | XLI – Industrials                          | Capex slowdown, input cost pressure               |
|  Short        | XLB – Materials                            | Slowing production, margin squeeze                |
|  Long       | XLV / XLU – Healthcare / Utilities         | Defensive sectors outperform in recessions        |
|  Short      | Regional Banks / Credit Exposed Financials | Rising credit risk, tighter lending               |
|  Long       | VIX or VIXY                                | Bearish sentiment + uncertainty = volatility play |
|  Pair Trade | Long High Quality / Short Leveraged Firms  | Margin strength vs. squeeze risk                  |

### **Signalgeist Insight:**

Markets often react to hard data – **but smart money moves on sentiment shifts first**. These surveys give us a rare early window into where the crowd is headed next. Position now to ride the sentiment shockwave as it hits Q2 earnings, consumer behavior, and credit markets.

### **Final Thought:**

Signalgeist subscribers don't wait for CNBC.

You're early. You're ready.

Use these signals before the rest of the market connects the dots.

 **Below is our detailed report:**

## **U.S. Consumer and Business Sentiment (April 2025) – Trends and Trade Implications**

### **University of Michigan Consumer Sentiment – April 2025 (Preliminary)**

**Surging Recession Fears:** A record 67% of consumers expect rising unemployment, the highest since 2009, after five straight monthly increases in this metric. This pessimism on jobs is one factor dragging down the University of Michigan's Consumer Sentiment Index, which plunged 11% in early April 2025 to 50.8 (preliminary) from 57.0 in March. This reading is **near record-low territory**, roughly 30% below its level in December 2024. The decline in sentiment was *"pervasive and unanimous across age, income, education, geographic region, and political affiliation,"* according to the survey director. Qualitatively, households report growing anxiety on multiple fronts: expectations for business conditions, personal finances, and labor markets all deteriorated, flashing *"warning signs that raise the risk of recession"*. Notably, **inflation expectations have spiked** – one-year ahead inflation is seen at **6.7% (the highest since 1981)**, up from 5.0% just a month prior. This surge in expected inflation (driven in part by escalating import tariffs and supply shocks) is eroding real income prospects and further souring consumer outlooks. In summary, the Michigan survey reveals consumers battenning down the hatches: **confidence is at recessionary lows, and a broad-based apprehension about job losses has set in.** These quantitative readings and the grim narrative suggest consumers are likely to **cut back on discretionary spending** and delay big purchases in the coming months.

### **Conference Board Consumer Confidence – March 2025**

**Multi-Year Low in Expectations:** The Conference Board's Consumer Confidence Index fell to **92.9** in March (1985=100), marking a fourth consecutive monthly

decline and the lowest level in over four years. The decline was led by the Expectations Index, which dropped to **65.2 – a 12-year low**, well below the threshold of 80 that often signals a recession ahead. By contrast, the Present Situation Index (current conditions) remains higher at 134.5, though it slipped modestly. Consumers are thus relatively more uneasy about the *future* than the present. Qualitatively, **inflation and policy worries dominate**: consumers cited high prices for household staples (e.g. eggs) and rising tariffs as key concerns. Indeed, average 12-month inflation expectations in this survey rose to **6.2% in March from 5.8% in February**. Consumers' outlook on the job market and income has darkened considerably – confidence in finding jobs and in income growth **"largely vanished,"** per the Conference Board, with future employment optimism at a 12-year low. Older age groups (35+ especially 55+) turned markedly more pessimistic, while younger consumers (sub-35) saw a slight uptick in confidence (perhaps due to a still-strong current job market). Notably, only **37% of consumers now expect stock prices to rise** in the next year (down 10 points in a month), while **44% expect stocks to decline** – a sharp sentiment reversal towards risk-aversion. On the spending front, consumers report mixed intentions: plans to buy homes and cars have fallen on a trend basis, and many plan to purchase big-ticket items *sooner* rather than later to avoid anticipated price hikes from tariffs. There's also a shift in leisure spending preferences – fewer plan on movies or indoor entertainment, while more plan outdoor activities and travel, and vacation plans have ticked up. In sum, the Conference Board survey quantifies a **deteriorating consumer psyche**: confidence in future business conditions is the weakest since 2013, inflation expectations are high, and recession expectations (the share anticipating a recession) are at a multi-month high. Households appear to be bracing for tougher times ahead by **curtailing non-essentials and adjusting spending plans** in response to expected inflation and uncertainty.

## NFIB Small Business Optimism – March 2025

**Small Business Sentiment Slips Below Historical Average:** The NFIB Small Business Optimism Index fell to **97.4** in March, dropping 3.3 points and **dipping below the 51-year average of 98**. This was the third straight monthly drop and the sharpest decline since mid-2022, effectively erasing the post-election surge in small business confidence that followed late 2024 policy hopes. According to NFIB, *"new policy priorities"* – notably a wave of new tariffs and trade policy shifts

– have **heightened uncertainty** and caused small firms to scale back expectations for sales and expansion. Indeed, the survey's uncertainty index remained elevated (though slightly eased in March from a record February). **Future outlook measures deteriorated significantly:** the net percentage of owners expecting better business conditions in six months plunged 16 points to just 21% (the lowest since late 2024). Similarly, the net share expecting higher sales fell to 3%, a low not seen since before the 2016 election boom. These figures underscore a collapse in small business confidence about the near-term economy. Importantly, this March survey was conducted *before* an April 2 announcement of sweeping new tariffs, meaning sentiment could weaken further as those trade actions bite. NFIB noted that *"the impact of new tariffs is yet to be felt,"* even as businesses were already growing wary.

On the **cost and hiring side**, there are mixed signals. While realized price increases slowed in March — a brief reprieve — 30% of businesses expect to raise prices over the next quarter, the highest rate in a year. This suggests that inflationary pressures, especially those tied to tariffs and supply disruptions, remain persistent beneath the surface. This foreshadows continued inflation in the pipeline. Hiring plans have pulled back: a net 12% of firms plan to increase employment, the lowest in 11 months. While that's still positive, it shows small employers turning cautious on job growth. Many firms are likely in a **"wait-and-see" mode**, holding off on expansion and capital outlays until uncertainty (especially around trade policy and potentially interest rates) diminishes. In summary, America's small businesses are signaling **downside risks ahead** – their optimism has faded to average levels, their outlook for the economy is bleak, and although current operations aren't collapsing, plans for price hikes and reduced hiring point to a more inflationary yet slower-growth environment. This aligns with the deteriorating consumer mood, painting a consistent picture of an economy **losing momentum in early 2025**.

## Regional Federal Reserve Business Surveys (Manufacturing Outlook)

**Manufacturing Slowdown Deepens:** Regional manufacturing sentiment has taken a sharp turn for the worse, as illustrated by the Philadelphia Fed's April 2025 survey. The chart shows the Philly Fed's current activity index (brown line)

plunging into negative territory and the six-month outlook index (black line) remaining subdued. In April, the **Philadelphia Fed's general activity index collapsed to -26.4** (from +12.5 in March), the lowest reading since 2023. Nearly 40% of manufacturers reported decreases in activity, vs only 13% reporting increases. New orders dried up – the new orders index plummeted to -34.2, a level not seen since the 2020 recession onset – and shipments turned negative as well. **Manufacturing firms are essentially in contraction**, with order books shrinking. The employment index in Philly's survey fell to near zero, implying employment was flat on net (84% of firms kept headcounts steady). Firms have cut back working hours (average workweek index fell sharply to -12.7) even though outright layoffs haven't started yet.

Inflationary pressures remain intense in the manufacturing supply chain. The Philadelphia Fed's prices paid index jumped to **51.0**, the highest since mid-2022, with 54% of firms facing higher input costs. Prices received by firms for their own goods also rose (index at 30.7), but not as dramatically – indicating **margin squeeze** as input costs are rising faster than many firms can increase their selling prices. Looking ahead, manufacturers in the Philly survey expressed very tepid expectations: the future general activity index was barely positive (6.9) – essentially **stall-speed optimism** – and the future employment index dipped below zero for the first time since 2016, signaling that as many firms expect to cut jobs as add them in the next six months. Capital expenditure plans are nearly flat (future capex index ~2, with ~75% of firms expecting to spend the same, and few increasing investment). In short, **producers are hunkering down**: they foresee little growth ahead and are hesitant to invest or hire given soft demand and costly inputs.

The New York Fed's **Empire State Manufacturing Survey** for April echoes this weakness. Business conditions in NY remained in contraction (headline index **-8.1**), and while that was an improvement from March's nadir, **new orders and shipments were still negative** (orders index -8.8). Like in Philadelphia, employment was roughly flat-to-down and the workweek shortened. Price pressures accelerated for a fourth month – **prices paid index hit 50.8 and prices received 28.7, the fastest increases in over two years** – confirming that manufacturers are dealing with rising costs and attempting to push through higher prices. Critically, **outlook sentiment in New York turned outright pessimistic**. The Empire State future conditions index plunged ~20 points to **-7.4**, which is **the**

**second-lowest expected outlook in the survey's 20+ year history.** In other words, NY factories have almost never been this downbeat about the next six months. The fact that inventories are building up in the region (inventory index +7.4) even as orders fall suggests a looming inventory glut, which could force production cuts ahead.

Across multiple Fed district surveys (Philadelphia, New York, and others), the **qualitative commentary is of "worsening conditions"**: demand is softening, and uncertainty from trade policy (tariffs) is cited as a factor dampening new orders. Many firms report continued ability to raise prices (reflecting input cost pass-through and perhaps panic buying before tariffs), but they are also indicating that **growth is stalling**. This dichotomy – **falling output vs. rising prices** – is essentially a stagflationary signal coming from the manufacturing sector.

## Synthesis of Survey Trends (Qualitative and Quantitative)

Bringing these surveys together, several **common themes** emerge:

- **Declining Sentiment Across the Board:** Virtually every confidence measure – consumers, small businesses, manufacturers – has been **trending down for multiple months**. Quantitatively, indices are at or near multi-year lows (e.g., 12-year low for consumer expectations, multi-year low outlook for NY manufacturers, etc.). The breadth of the decline (across demographics for consumers, and across regions for businesses) underscores that the pessimism is widespread. These surveys collectively point to a **marked slowdown in economic momentum** as of spring 2025.
- **Trade Policy and Tariff Concerns:** A driving narrative in these reports is the escalation of the trade war and tariffs. Both consumers and businesses frequently mentioned tariffs and trade policy uncertainty as reasons for gloom. In early April, tariffs on many Chinese goods jumped to 125%, with China retaliating in kind, alongside broad U.S. import tariffs (10% on most goods, 25% on autos, steel, aluminum). The **impact of these tariffs is twofold**: they are **raising prices (inflation)** and **creating uncertainty/disruption** for businesses. The Fed's Beige Book-style anecdotes (and NFIB commentary) highlight that firms are unsure how new trade rules will play out and are postponing decisions. Consumers, for their part, fear higher prices on

imported goods and overall economic fallout from a trade war. This policy backdrop is a unifying catalyst behind the slump in sentiment.

- **Inflation Expectations at Highs, Real Income Pressures:** A striking quantitative signal is the surge in inflation expectations – consumers see the highest near-term inflation in decades, and businesses are experiencing the fastest cost increases in years. This is squeezing real incomes and profit margins. Consumers specifically call out expensive essentials (food, fuel), which eats into disposable income. The **qualitative commentary** in surveys notes persistent concern about “*high prices*” for necessities. At the same time, wage growth expectations are limited (e.g., fewer consumers expect income increases now, and manufacturers plan only moderate wage hikes of ~3–4%). The net result is a **cost-of-living crunch** that is undermining confidence and likely consumer spending. In businesses, rising input costs without commensurate pricing power translates to **margin compression** (as evident in manufacturing surveys where input cost indexes far exceed output price indexes). High inflation also raises the specter of more aggressive Fed tightening, which adds to uncertainty.
- **Labor Market: Turning from Strength to Weakness:** Until recently, strong employment and wage gains were a pillar supporting consumer confidence. Now we see cracks forming. Quantitatively, the share of consumers expecting job availability to worsen has climbed sharply (Michigan’s measure of expected unemployment up is highest since the Great Recession; Conference Board also shows a rise in those expecting “fewer jobs” ahead). Small businesses are pulling back hiring plans, and manufacturers’ future employment intentions have slipped into neutral/negative territory. While headline employment numbers have yet to show major weakness, forward-looking sentiment data is flashing red. With 67% of consumers expecting rising unemployment and businesses pulling back on hiring, the labor market appears poised for a turn. The discrepancy between stable current metrics and worsening expectations suggests an inflection point is approaching. Qualitatively, this is a major psychological shift – people are no longer confident in job security, which typically leads to precautionary belt-tightening by households. The fact that these expectations indices are at recession-era levels (while actual unemployment hasn’t yet spiked) could indicate we are at

a **turning point** in the labor cycle. Companies might move from “steady” employment to hiring freezes or even layoffs if demand continues to wane.

- **Divergence Between Present Conditions and Expectations:** A notable aspect is that **current conditions, while softer, are not as dire as future expectations**. For example, consumers still say current business conditions are more positive than negative on balance, and jobs are “plentiful” vs “hard to get” by roughly a 2:1 margin in the present. Small businesses report current sales trends that, while down, aren’t collapsing. Many manufacturers kept employment and production stable through March. However, the expectations (6-month ahead) components have sunk well below normal. This gap suggests that **economic actors are essentially anticipating a downturn before it fully hits**. Such a dynamic can be self-fulfilling: if businesses and consumers *act* on their negative expectations (cut spending, halt hiring), it will bring about the slowdown they fear. The surveys thus may be foreshadowing an imminent pullback in actual economic activity in Q2/Q3 2025.
- **Pocket of Resilience – Travel and Experiences:** One quirky qualitative finding: despite the overall caution, some consumers indicated plans to **increase spending on travel and outdoor activities** (perhaps to seize the moment before things possibly worsen, or as a shift away from goods consumption). Vacation plans rose, even as other entertainment spending plans fell. This could hint that the services side of the economy (especially travel/leisure) might see a short-term boost, as consumers pivot their limited discretionary budgets toward experiences rather than goods. However, this may be a temporary effect (possibly driven by tariff-induced price timing and post-pandemic pent-up travel demand) that could fade if the economy truly enters recession. It’s a reminder that even in a downturn, not all sub-sectors move in lockstep – there can be **rotation in consumer priorities**.

In summary, both quantitative data (the index levels, diffusion measures, etc.) and qualitative commentary (surveyed reasons, anecdotes) align to tell a story of an economy at a **delicate juncture**. Confidence has been dented by trade turmoil and inflation, and while conditions are not catastrophic yet, many leading indicators from sentiment point to a possible recession on the horizon. With this backdrop, we now assess how these sentiment trends translate into first- and second-order

effects on various sectors of the S&P 500, and ultimately into potential trading strategies.

## First-Order Effects on the Economy and S&P 500 Sectors

“First-order effects” are the direct, immediate impacts one would expect given the sentiment shifts and data trends. Based on the surveys:

- **Pullback in Consumer Discretionary Spending:** The plunge in consumer sentiment is likely to **hit non-essential consumer demand first**. When confidence falls and inflation bites, households typically cut back on big-ticket and discretionary purchases – for example, postponing buying new appliances, cars, or luxury items, and reducing spending on dining out or entertainment. We already see evidence of this in survey data: plans to buy homes and cars have declined, and more consumers say now is a bad time to buy costly items. This bodes ill for the **Consumer Discretionary sector** (retailers, automakers, apparel, leisure products, etc.). We can expect **weak sales in segments like automotive, furniture, consumer electronics, and specialty retail** as first-order casualties of low consumer confidence. Conversely, **Consumer Staples (essentials)** should see steadier demand – people still need to buy food, household supplies, and healthcare items even in hard times. In fact, staples may even experience *forward buying*: the Conference Board noted some consumers intend to purchase appliances **before** tariffs drive prices higher. Thus, a first-order effect is a **rotation of consumer spending from discretionary toward essentials and value-focused options**. Quantitatively, this could mean softer Q2 sales numbers for discretionary firms and potentially a build-up in inventories of unsold goods.
- **Business Investment and Hiring Slowdown:** With small business optimism dropping and manufacturers turning pessimistic, a clear first-order effect is that **businesses will curb capital expenditures and hiring**. The surveys show new orders and capital spending plans nearly flat or falling. Firms large and small are likely to **delay expansion projects, equipment purchases, and new hires** until they have more clarity or until demand picks up. This directly impacts sectors like **Industrials and Technology** (for example, lower capex means less demand for industrial equipment, factory automation, enterprise

software, and commercial vehicles). It also impacts **Materials**, as lower capex and construction mean less demand for commodities (steel, copper, chemicals) used in projects. Additionally, a hiring slowdown – already signaled by NFIB’s reduced hiring intentions – means the robust job gains that powered consumer spending could abate. Companies might implement hiring freezes or trim openings as a first response to uncertainty. The **Unemployment rate may begin to tick up modestly** in coming months if this sentiment translates to action, though the surveys suggest this is just starting. For now, the first-order effect is **fewer help-wanted signs** – a cooling in the red-hot labor market, which in turn would moderate wage growth and consumer spending power.

- **Price Increases and Inflation Persistence:** Another immediate effect of the current environment is that many businesses are **raising prices to cope with higher costs**. Both the NFIB and regional Fed surveys indicate a large share of firms plan price hikes in the near term (30% of small businesses plan increases; manufacturers’ prices indexes are high). So one first-order outcome is **sticky inflation in certain categories**: consumers will continue to see elevated prices for goods and services in the next 1-3 months, Inflation continues to pressure consumers through eroded real wages and purchasing power. However, firms with strong pricing power, such as those in oligopolistic or branded sectors may maintain margins or grow revenues. This divergence is critical: while inflation punishes volume-driven or price-sensitive businesses, it can reinforce strength in defensives with cost-pass-through capabilities. From a macro standpoint, these price increases complicate the Fed’s job – but within our horizon, the direct effect is **headline CPI remaining elevated**, which could bolster sectors like **Energy and Commodities** (often inflation beneficiaries) or firms that supply consumer staples (food producers, etc., who see revenue uptick from price). However, persistent inflation also **dampens real consumer spending**, reinforcing the pullback in volume of goods sold (consumers pay more, but get less, which hurts discretionary volume sales).
- **Shift to Defensive Posture:** In financial markets, a first-order reaction to rapidly deteriorating sentiment is typically a **shift toward “defensive” sectors and assets**. Investors and companies alike batten down the hatches. Corporations may increase liquidity reserves and tighten credit standards (anticipating tougher times), and investors rotate into sectors like Utilities,

Healthcare, and Consumer Staples, which are viewed as more resilient in downturns. We have already seen consumers themselves favoring necessity spending; on the corporate side, essential service providers (electricity, healthcare) usually see stable demand even if the economy slows. Thus, an immediate effect is likely a **relative strengthening of defensive sectors' outlook** versus cyclical sectors. This isn't a direct result from the surveys per se, but it's a rational first-order market implication of the surveys' message of a looming slowdown.

- **Financial Conditions Tightening (Sentiment-Driven):** Although not a direct survey output, one can infer that banks and lenders will react to widespread gloom by becoming more cautious. A first-order effect could be **tighter credit availability** for marginal borrowers (e.g., small businesses might find loans slightly harder to get or more expensive, and consumers might face stricter credit card or auto loan standards). The sentiment of rising recession risk and higher inflation may lead banks to price in more risk. Additionally, interest rates on the short end could remain high or rise if the Fed responds to inflation expectations – 54.6% of consumers now expect higher interest rates ahead, showing that the public anticipates tighter policy. In the 1-3 month horizon, this means **financing costs for businesses and consumers remain elevated**, which is directly negative for interest-rate-sensitive sectors like Housing/Real Estate (mortgages will stay pricey) and could dampen any interest-sensitive spending (auto loans, etc.).

In essence, the first wave of impact from these souring sentiment trends is a **broad economic deceleration**: consumers buy less (especially discretionary items), businesses spend and hire less, and many firms raise prices to try to protect margins (keeping inflation high). Some sectors (staples, healthcare, utilities) feel less of a blow on the demand side, while others (retail, travel-related discretionary, autos, capital goods) feel it quickly. These direct effects set the stage for the more **second-order effects** we discuss next.

## Second-Order Effects (Downstream and Indirect Impacts)

Second-order effects are the ripple effects that occur as the initial impacts work through supply chains, balance sheets, and broader economic linkages. Given the

first-order developments, we anticipate several consequential second-order effects in the coming 1-3 months:

- **Corporate Margin Compression and Earnings Risk:** As noted, many firms are getting squeezed between rising input costs and a consumer base unwilling or unable to absorb unlimited price increases. **Profit margins are likely to contract** for companies that were unable to fully hedge or pass along cost inflation. This especially applies to sectors like **Consumer Discretionary and Industrials** – for example, retailers and consumer goods makers might face higher import costs due to tariffs plus higher wage bills, even as their sales volumes drop. Similarly, manufacturers of intermediate goods may see order cancellations (lower volumes) just as costs for raw materials (like steel, aluminum with new tariffs) spike – a profit double-whammy. The surveys already hint at this: input price indices are outpacing output price indices, and small businesses report deteriorating sales expectations alongside plans for price hikes. This dynamic means **Q2 corporate earnings could disappoint** in many cyclical industries. Companies might issue profit warnings or cut guidance due to cost pressures and demand shortfalls. In stock terms, this margin compression risk will likely lead to underperformance of high-cost, low-margin businesses and benefit those with **strong pricing power or lower cost exposure**.
- **Inventory Gluts and Production Cutbacks:** A subtler second-order effect is the potential for **inventory build-up** leading to a sharper production response. The Empire State survey noted inventories were still expanding even as orders fell. Similarly, if consumer spending falls suddenly, retailers could find themselves with excess inventory (a scenario reminiscent of early 2023's retail glut). **Excess inventories** force businesses to cut future orders and production until the backlog is worked off. We may see discounting (to clear unsold goods) which pressures margins further, and manufacturers idling factories temporarily to align supply with lower demand. This will particularly impact upstream suppliers: for instance, if auto dealerships see cars sitting on lots due to weak demand and high prices, auto manufacturers will slow assembly lines, which in turn hits parts suppliers (electronics, tires, metals, etc.). Thus the second-order effect of the initial consumer pullback can be an **amplified decline in industrial output** a month or two later as the supply chain adjusts. The **Materials sector** could feel this via reduced orders for raw materials (less

steel needed if fewer cars/buildings are made). **Semiconductor and tech hardware firms** might also see order push-outs if their client industries are trimming inventories. This inventory cycle effect can make a slump self-reinforcing for a few quarters.

- **Rising Credit Risk and Financial Strain:** With cash flows under pressure and confidence low, more firms (and some consumers) could face **difficulty meeting their debt obligations**, introducing credit risk as a second-order issue. Small businesses often operate on thin margins – the NFIB survey suggests many expect worse sales and still-high costs, which could lead to missed loan payments or need for credit line drawdowns. In the consumer sphere, if unemployment starts to rise even slightly, some highly indebted households might default on loans. Banks and lenders will likely respond by tightening credit standards further and increasing loan loss provisions. **Financial sector impacts** may include widening credit spreads, especially for lower-rated corporate bonds, as investors demand more yield to compensate for higher default risk. We might also see stress in areas like **commercial real estate** if businesses close or reduce operations (affecting landlords' rental incomes). While a full credit crunch might be beyond a 3-month horizon unless things deteriorate rapidly, the early signs could be present: e.g., upticks in delinquency rates, or difficulty for risky borrowers to roll over debt. Second-order, this credit tightening then feeds back into even less spending and investment – a classic negative feedback loop heading toward recession.
- **Policy Response and Monetary Tightening:** Another consequential effect is how policymakers respond. The **Federal Reserve**, eyeing 40-year-high inflation expectations in consumers, may lean hawkish despite the growth slowdown. In the short term, this could mean continued high policy rates or even additional rate hikes – an outcome that would further raise borrowing costs across the economy. The **yield curve** could flatten or invert more deeply as short rates rise and long-term growth expectations fall. For sectors, this specifically hurts interest-sensitive areas: **Real Estate Investment Trusts (REITs)** and homebuilders could suffer from higher financing costs and weaker property demand. High-growth **Technology stocks** might also feel second-order pain, as higher rates reduce the present value of future earnings (and if credit is tighter, funding for unprofitable tech firms dries up). On the flip side, if the Fed prioritizes growth and signals caution, that could weaken the dollar or

ease rates – but given the inflation backdrop, the more likely near-term stance is hawkish (as Fed officials have warned that tariffs pose both inflation and growth risks). Thus, we might see an unusual mix of **tight monetary conditions into a slowing economy**, which is challenging for risk assets.

- **Sectoral Cascades (Specific Examples):** Some industries will have unique knock-on effects. For instance, consider the **auto sector**: a first-order hit from tariffs (25% tariff on imported vehicles and parts) and low consumer confidence is fewer car sales. A second-order effect is that **auto suppliers** (parts manufacturers, tire companies, electronics suppliers) see reduced orders, and dealer inventories swell (prompting heavy discounting). Auto lenders (captive finance arms or banks with large auto loan books) could then see rising delinquencies if consumers who did buy overpaid and fall behind, or if used car values drop leading to higher loan-to-value ratios. Another example: **Retail and Commercial Real Estate** – if retail sales falter, stores (especially smaller ones) might close or not renew leases, impacting commercial REIT incomes; similarly, weakness in industrial production could soften demand for warehouse and manufacturing space. These cross-sector ripple effects mean investors should watch not just the directly exposed companies but also their **ecosystem** (suppliers, creditors, landlords, etc.), which can transmit stress further.
- **Market Volatility and Sentiment Feedback:** Finally, the pervasive uncertainty and negative sentiment can itself be a second-order driver of market behavior. The Conference Board noted an uptick in uncertainty references by consumers, and small business uncertainty, while slightly down from a peak, is still above historical norms. We have effectively a market sentiment loop where consumer/business gloom can translate to **investor gloom**, increasing volatility. If equity markets respond with declines (some of which we've likely seen given the drop in stock expectations), that in turn can further dent consumer confidence (wealth effects). So, a second-order effect is **higher financial market volatility** and potentially sharper swings in asset prices as the tug-of-war between inflation fears and recession fears plays out. Already, consumers turning bearish on stocks might presage outflows from equity funds or reduced retail investor activity.

In summary, the second-order impacts suggest an environment that could **broaden a modest slowdown into a more pronounced downturn**. Margin squeezes lead to cost-cutting (jobs, capex), inventory corrections lead to production cuts, credit worries lead to less lending – all reinforcing the initial demand shock. For investors and analysts, these are critical to anticipate because they can **create opportunities or risks that aren't obvious from the first-order news alone**. For instance, a savvy observer might short a seemingly insulated supplier stock because they foresee their key customers cutting orders; or avoid a bank stock not because of current earnings, but due to expected loan losses down the line. Recognizing these chain reactions is key to formulating effective trades, which we turn to next.

## Trade Ideas and Sector Strategies (1–3 Month Horizon)

Based on the above insights from sentiment surveys, here are **concrete trade ideas** for S&P 500 sectors and related macro instruments, structured around first- and second-order effects. Each idea includes a brief rationale linking back to the survey findings:

| Trade Idea                                               | Type               | Rationale & Insight Linkage                                                                                                                                                                                                                                                                                                                                                                                                                                                                | Time Horizon |
|----------------------------------------------------------|--------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------|
| <b>Underweight or Short Consumer Discretionary (XLY)</b> | Sector ETF / Short | <b>Weak consumer sentiment</b> and high inflation signal a pullback in non-essential spending. The plunge in confidence to recessionary levels will likely hit retailers, automakers, apparel companies, and travel-related firms directly (first-order effect). Tariffs on consumer goods (e.g. electronics, autos) raise input costs and prices, further dampening demand. Expect earnings disappointments or cautious guidance from discretionary companies as consumer demand softens. | 1–3 months   |

|                                                  |                    |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                           |            |
|--------------------------------------------------|--------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------|
| <b>Overweight or Long Consumer Staples (XLP)</b> | Sector ETF / Long  | In a downturn, consumers <b>prioritize essentials</b> over luxuries. Staples like food, beverages, household products should see relatively stable demand. Notably, consumers are concerned about staples' prices but will still purchase them, allowing strong brands to pass on costs. Many staple companies have pricing power to maintain margins despite inflation. This defensive sector typically outperforms when confidence is low and recession risk is rising.                                                 | 1–3 months |
| <b>Underweight Industrials (XLI)</b>             | Sector ETF / Short | <b>Manufacturing activity is contracting sharply</b> , per regional Fed surveys (Philly Fed index at -26.4). New orders and shipments are down, implying lower revenues for industrial firms (machinery, aerospace, equipment) in coming months. Additionally, tariff-driven cost increases (steel/aluminum) could squeeze margins for capital goods manufacturers (second-order effect). With business investment likely on hold and future expectations weak, the Industrials sector faces a challenging quarter ahead. | 1–3 months |
| <b>Underweight Materials (XLB)</b>               | Sector ETF / Short | A broad economic slowdown and wary businesses mean less demand for <b>raw materials</b> . If manufacturing and construction projects are delayed or canceled (first-order effect of low confidence), producers of metals, chemicals, and other materials will see reduced orders. At the same time, trade disruptions (tariffs) can raise input                                                                                                                                                                           | 1–3 months |

|                                                        |                   |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                   |            |
|--------------------------------------------------------|-------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------|
|                                                        |                   | costs or create gluts in certain commodities – e.g. if global demand falters, oil and metal prices may soften, hurting producers. Materials firms are also margin-squeezed when energy and feedstock costs spike. Thus, the outlook for Materials is bearish in a stagflationary slowdown scenario.                                                                                                                                                                                                                                               |            |
| <b>Overweight Healthcare (XLV) and Utilities (XLU)</b> | Sector ETF / Long | These <b>defensive sectors</b> tend to hold up in downturns. Healthcare demand is relatively inelastic – people need medications and services regardless of sentiment. Utilities (electricity, water, etc.) have stable cash flows and often act as safe havens. With recession signals flashing (Conference Board expectations well below 80, investors are likely to rotate into these sectors. They also offer dividends that become attractive as growth stocks falter. Going long defenses can help balance the risk of shorts in cyclicals. | 1–3 months |
| <b>Short Select Financials (Banks)</b>                 | Equity Short      | Banks face a <b>two-pronged second-order risk</b> : slower loan growth (as consumers and small businesses pull back) and rising credit risk. Consumers are growing pessimistic about paying bills and jobs, which could lead to higher delinquencies on credit cards, auto loans, etc., a few months out. Small business loan demand may soften, and existing borrowers appear less optimistic about their ability to expand (or even survive if conditions worsen). Regional banks with heavy commercial and                                     | 2–3 months |

|                                                                   |                              |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       |                              |
|-------------------------------------------------------------------|------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------|
|                                                                   |                              | <p>industrial loan exposure, or banks reliant on consumer lending, could underperform. Additionally, if the Fed stays hawkish due to inflation, yield curves may invert further, crimping bank profitability. <i>Trade:</i> consider shorting a regional bank ETF or specific bank stocks with large retail/SME portfolios.</p>                                                                                                                                                                                                                                                                                                                                                                                                       |                              |
| <p><b>Long Volatility (VIX futures or call options, VIXY)</b></p> | <p>Macro / Hedge</p>         | <p>Despite some equity market declines, implied volatility remains muted, suggesting a tactical opportunity. If upcoming data confirms sentiment weakness, a delayed volatility spike may materialize. A long VIX position here hedges downside and exploits lagged market reaction to worsening fundamentals</p>                                                                                                                                                                                                                                                                                                                                                                                                                     | <p>1–2 months (tactical)</p> |
| <p><b>Pair Trade – Long Quality, Short Leverage:</b></p>          | <p>Equities (Pair Trade)</p> | <p>A nuanced equity strategy is to go <b>Long high-quality companies</b> (strong balance sheets, high margin, pricing power) and <b>Short weaker peers</b> in affected industries. For example, within Consumer Discretionary, long a discount retailer or a staple-oriented retailer (that can steal share in downturns) vs. short a luxury retailer or department store chain that is very sensitive to spending cuts. Or within Industrials, long a company with diversified revenue and defense contracts (stable government demand) vs. short a pure-play cyclical machinery stock. The rationale is that second-order effects (credit stress, margin compression) will hit weaker players hardest, whereas well-capitalized</p> | <p>3 months</p>              |

|  |  |                                                                                                                                                     |  |
|--|--|-----------------------------------------------------------------------------------------------------------------------------------------------------|--|
|  |  | leaders can weather the storm and even capture market share. This pair approach banks on dispersion within sectors as the recession fears play out. |  |
|--|--|-----------------------------------------------------------------------------------------------------------------------------------------------------|--|

**Note:** All the above trades should be monitored frequently, as incoming data (e.g., actual retail sales, industrial production, CPI, and company earnings releases) will either confirm or challenge the survey-based thesis. If, for instance, a sudden resolution of trade disputes occurs (e.g., tariff rollbacks beyond the partial April 9 reversal noted by U. Michigan, sentiment could rebound quickly, and the short positions in cyclicals would need re-evaluation. Conversely, if inflation runs even hotter than expected or unemployment suddenly jumps, deeper defensive positioning could be warranted.

These trade ideas aim to capitalize on the **first-order impacts** (like reduced consumer spending hurting retailers) and **second-order impacts** (like reduced spending leading to supplier margin pain and credit issues) identified in the sentiment analysis. By deploying a mix of shorts, longs in defensives, and hedges, an investor can create a portfolio that benefits from the scenario these surveys are collectively foreshadowing: an economic slowdown with persistent inflation, essentially a **stagflation-lite environment** leading into mid-2025.

## Conclusion

The latest sentiment surveys paint a cautionary picture for the U.S. economy. Consumers are gloomy about the future and bracing for tough times, small businesses are on edge and scaling back ambitions, and manufacturers are feeling the pain of a demand slowdown coupled with rising costs. Such a combination of factors (falling confidence, trade disruptions, and high inflation) has historically been a warning sign of an impending economic downturn. While nothing is certain and sentiment can shift, the **alignment of qualitative narratives and quantitative data trends** across these independent surveys provides a compelling signal. Investors would be wise to heed these warning signs by adjusting sector exposures and hedging against downside risks, while positioning for resilience in areas that can weather an inflationary downturn. The next 1–3 months will be critical to watch: if hard data starts to confirm the soft survey data (e.g., weaker retail sales, lower capital goods orders, rising jobless claims), the

trade ideas outlined above should gain traction. Ultimately, the goal is to transform these rich survey insights into **actionable strategies** – protecting portfolios and finding opportunities amid the challenges that a crisis of confidence can generate.

**Sources:** The analysis and data above are based on the latest releases and commentary from the University of Michigan Surveys of Consumers, The Conference Board Consumer Confidence survey, the NFIB Small Business Optimism Index, and regional Federal Reserve bank manufacturing surveys (Philadelphia Fed and New York Fed), among other related reports. These sources provide a comprehensive view of sentiment across different economic agents, which we have synthesized to inform the conclusions and investment ideas.

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