

Looking for something to read? See our [Reading List](#); these books, separated by category, are ones we find interesting and insightful. We will be adding to the list over time.

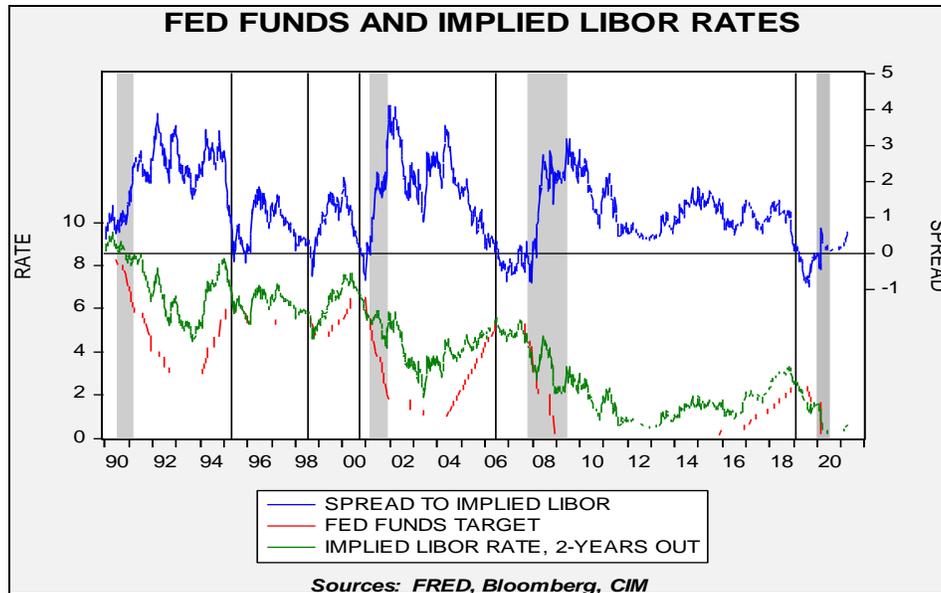
[Posted: April 8, 2021—9:30 AM EDT] Global equity markets are mixed this morning. The EuroStoxx 50 is currently up 0.2% from its prior close. In Asia, the MSCI Asia Apex 50 closed up 0.2%. Chinese markets were mixed, with the Shanghai Composite up 0.1% from its prior close, and the Shenzhen Composite is relatively unchanged. U.S. equity index futures are signaling a higher open.

The Confluence macro team publishes a plethora of research reports and multimedia offerings on a weekly and quarterly basis, all available on our [website](#). We highlight recent publications below, with new items of the day emphasized in bold:

- [Weekly Geopolitical Report](#) (3/29/201): Part III of our series on the Geopolitics of Central Bank Digital Currencies (CBDC)
- **[Weekly Energy Update](#) (4/8/2021)**
- [Asset Allocation Weekly](#) with associated [chart book](#) and [podcast](#) (3/26/2021)
- **[Confluence of Ideas podcast](#) (4/7/2021): “The U.S.-China Balance of Power: Part I”**
- [Asset Allocation Quarterly Rebalance Chart Book](#) (Q1 2021): recaps recent changes to our Asset Allocation portfolios

Good morning all! [U.S. equity futures are mostly elevated this morning](#) in the wake of yet another record S&P 500 close. We open commentary this morning with the Fed minutes. Economics and policy follow with corporate taxes in the spotlight. Pandemic news is next. China news follows, and we close with our international news roundup.

Fed minutes: There were no obvious surprises in the minutes from the March 16/17 meeting. There were [expressions of concern about inflation](#), but it is also obvious that the [FOMC intends to keep rates steady at least into 2023](#). Although there are comments circulating that the market is starting to discount rate hikes sooner than the FOMC is suggesting, our Eurodollar model suggests that rates are merely normalizing, but it doesn't appear to us that the rise in market rates is out of the ordinary.



Eurodollar yields reflect both expectations of policy changes and credit risk. The current spread suggests no rate hikes for two years.

Economics and policy: Better global growth is coming, and a global corporate tax agreement is being floated.

- The IMF meetings are being held virtually this week; they usually are held in Washington this time of year. Mainly due to aggressive U.S. fiscal action, but also aided by expectations of [waning pandemic influence](#), the group [raised its forecast](#) for this year’s global GDP growth to 6%, up from the 5.5% forecast made in January. [Despite this rising growth, the dispersion of growth is also widening](#); vaccine distribution has mostly been focused on the developed world, meaning that the emerging world economies are mostly lagging.
- Morning Consult, a survey firm, notes in a [recent study](#) that states dependent on tourism are lagging in the recovery.
- We usually don’t engage in a deep analysis of proposed tax changes until we are confident that they will be passed. That doesn’t mean we are not paying attention. For now, we will rely on the work of others in this area. Here you will find [some background on the details of U.S. corporate taxes](#). Although the headline focus tends to be on the marginal rate, the bigger battle is in the details. The U.S. corporate tax code has provisions that tax multinational corporations on their global income. The idea is that America is the home of a large number of global firms, and merely taxing their U.S. operations allows them to [avoid taxes on what may be the bulk of their earnings](#). At the same time, most foreign nations also tax these firms on their “domestic” operations. Thus, there is a complicated set of rules that govern tax credits on foreign taxes paid. [This area is where the controversy lies](#). Of course, a major problem is that some nations have low or no corporate taxes. Firms are, therefore, encouraged to locate some level of operations there, where profits are funneled to further avoid taxes. [One way to address](#)

[this issue](#) is to create a [minimum global standard of taxation](#); [there is some EU support for this idea](#). However, for some of these small nations that benefit from the current arrangement, it would be very difficult to get them to sign off on a minimum tax regime. The bottom line is that we are still a long way from actually seeing tax changes.

- The tax increases are part of the infrastructure package, which, to be fair, stretches the word “infrastructure” [so broadly](#) it really is no longer meaningful. There are two new threats to getting this package passed:
 - [The Democrats’ margin in the House continues to narrow](#). There are currently five vacant seats in the House; three are vacant due to representatives joining the administration. On April 6, Alcee Hastings (D-FL) died at 84 from pancreatic cancer. The other vacancy was Ron Wright (R-TX), who passed away from complications tied to COVID-19. After the November elections, the Democrats held a 222-213 margin; that is now 218-212. Under House rules, vacancies must be filled by special elections. Two will be held in May, one in June, one in November, and the Florida one has not been set. Two of the elections may lead to a switch in parties; the other two are not expected to change. Currently, there are seven Democrats who hold districts that Trump won in 2020. For the Speaker, the margin has narrowed to the point where it will make it difficult to pass more radical measures.
 - The narrow margin in the Senate means that White House legislation either needs 10 GOP senators to pass (assuming unanimity among the Democrats) or the passage via budget reconciliation rules. The reconciliation rules do restrict what can be put into a bill (it has to have some relationship to budget matters decided by Senate Parliamentarian). Several of the proposed measures in the president’s proposal are in danger of not meeting these requirements, [which may reduce the scope of the measure](#).
- We also note the infrastructure bill includes [plans to increase the housing supply](#). We view this as an important idea if the goal is to narrow wealth inequality. For the bottom 90% of households, residential real estate is the largest part of wealth. There is a need for greater supply. It remains to be seen whether this part of the bill (a) is part of the final version and (b) addresses the issue.
 - An interesting sidelight to the pandemic’s effect on rents is the well-documented drop in the rents in previously fashionable urban areas, but the [consequent jump in rents in outlying areas](#) was not initially noticed. The rise is pricing out residents who were living in these areas.
- Although the concept of shareholder primacy was not directly part of the Reagan/Thatcher revolution, it was sort of a fellow traveler. Shareholder primacy is the idea that companies should be run for the sole benefit of the owners. Milton Friedman, Michael Jensen, and William Meckling are names most closely tied to the notion. [In the 1930s, Adolf Berle and Gardiner Means argued for a broader responsibility for managers](#).

Since the late 1970s, shareholder primacy has come to dominate thinking about how corporations should be run. However, in recent years, there has been a steady shift to the Berle and Means position where managers balance competing interests, including labor, shareholders, stakeholders, and society at large.¹

- The latest [JP Morgan](#) (JPM, USD, 153.41) [shareholder letter](#) makes it abundantly clear that [shareholder primacy is on its way out](#). Instead of maximizing value for shareholders, the stated purpose of a corporation is to be a responsible community citizen. The recent spate of corporate decisions and comments on political behaviors is part of this trend.
- The [dollar's share of global reserves has fallen below 60% to 59% in December](#), the lowest level since 1995. Although the greenback remains the world's primary reserve currency, there is clear concern about the continued focus on dollars for reserve purposes. These include rising Treasury debt² and the U.S. weaponization of the dollar for foreign policy purposes.
 - There has been an emerging idea [that Chinese sovereign debt may be an alternative to Treasuries](#). The yields are higher and Beijing's fiscal policy, at least on the surface, looks less risky (although central government debt is not excessive, the real risk is the local government borrowing, and defaults in that sector likely end up on the central government balance sheet). If this notion catches hold, the reserve currency threat from the CNY will become much more credible.
- The NY FRB reports that the [majority of stimulus checks are being saved or used to pay down debt](#).
- The western U.S. appears to be in a deep drought. As summer approaches, this condition raises the [possibility of a rough fire season](#) for this region.

COVID-19: The [number of reported cases](#) is 133,250,442 with 2,890,706 fatalities. In the U.S., there are 30,923,521 confirmed cases with 559,117 deaths. Both [cases and fatalities in the U.S.](#) are declining. For illustration purposes, the *FT* has created an [interactive chart](#) that allows one to compare cases across nations using similar scaling metrics. The *FT* has also issued an [economic tracker](#) that looks across countries with high-frequency data on various factors. The [CDC reports](#) that 225,294,435 doses of the vaccine have been distributed with 171,476,655 doses injected. The number receiving at least one dose is 109,995,734, while the number of second doses, which would grant the highest level of immunity, is 64,422,618. The *FT* has a page on [global vaccine distribution](#). The [Axios state map](#) shows a mixed picture, with the net result of mostly steady infection rates.

Virology

- The AstraZeneca (AZN, USD, 48.42) vaccine situation is becoming a mess. European regulators now admit that there is a [blood clotting problem with the vaccine](#). It rarely occurs, and given the relative risk of clotting compared to the dangers of the virus, [there](#)

¹ The ESG movement would be part of this idea.

² This is nothing new, BTW. The [Triffin dilemma](#), which discussed this problem, emerged in the 1960s.

[is a case for continued use](#). However, with alternative vaccines available, it's hard to suggest that it should be widely used.

- EU nations have responded as expected; the AstraZeneca vaccine is mostly restricted to older recipients. [Belgium](#), [Italy](#), [Spain](#), and the [U.K.](#) are restricting distribution.
- [Romanians are generally refusing](#) to accept the vaccine.
- The [EU has essentially banned vaccine exports](#). [India will restart exports in June](#) if the current surge in cases declines.
- The Czech Republic's inability to control the pandemic has led to the [firing of the nation's health minister](#). He is the third to be fired since the pandemic began.
- Due to COVID-19, Chile, which was planning on voting on a new constitution, [has delayed the election](#).
- One of the difficulties in examining the impact of the virus is the total fatality count. The data above rely on reports from medical facilities, and, in some cases, the determination of death is difficult. An alternative method is to look at the normal death rate and see how many "excess" deaths occurred. Although also imperfect, it can offer a broader estimate of the impact of the pandemic. For example, if a person committed suicide due to a drug overdose that was partly driven by social isolation, it might be considered a pandemic-related fatality. A [recent study suggests](#) that last year, there were 523,322 excess fatalities and 378,039 directly attributed to COVID-19.
- The Brazil variant (P.1) is starting to spread and is [currently hitting British Colombia](#). It appears to be quite virulent; the most recent outbreak closed a popular ski resort and shut down the Vancouver Canucks of the NHL. Meanwhile, in the U.S., [the U.K. variant \(B.1.1.7\) is becoming dominant](#).
- To some extent, the U.S. is [facing a race between vaccination and variant spread](#).
- With vaccine cards becoming the informal vaccine passport, a [thriving market](#) for fake or stolen vaccine cards is developing.

China: Regional tensions remain elevated, and it appears the U.S. is backing down from a boycott of the Olympics.

- Tensions in the first island chain remain elevated.
 - Beijing is warning Japan [not to adopt U.S. sanctions](#) over the Uighurs and Hong Kong. It also continues to [pressure the Philippines](#) by massing Chinese vessels in its territorial waters.
 - One of China's diplomatic tactics is to attempt to make all regional relationships bilateral. If it can force each individual nation to negotiate one-on-one, it stands a better chance of dominating the relationship. The U.S. is a threat to this tactic because it is powerful enough to create a unified response.
 - We note the U.S. [has sent the USS Theodore Roosevelt](#) and the associated strike group to the area to bolster defenses.
 - Japan is considering [deploying F-35s](#) to its south to defend the [disputed Senkaku islands](#) (known by China as the Diaoyu islands).

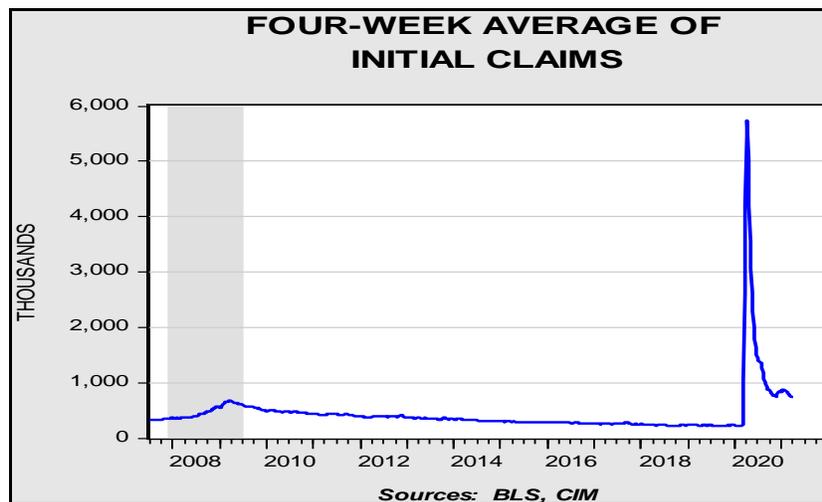
- Taiwan is starting its annual war games with one part [based on a Chinese invasion](#). [Beijing is repeatedly violating](#) Taiwan's defense identification zone.
- A boycott of the summer Olympics next year has [apparently been considered by Washington](#). However, the State Department has [signaled that a boycott isn't likely](#).
- [Multinational firms struggle](#) to reduce their China exposure and are increasingly caught between the U.S. and China. [China's size makes avoiding China costly](#). We also note that some of China's most advanced military technology is [being built with Taiwan and American technology](#). These goods are acquired by purchases through Chinese private tech companies.
 - A recent Chinese hack of Microsoft (MSFT, USD, 249.90) shows [signs that it was facilitated by earlier data gathering](#). If so, China may have built a database of personal information that it is weaponizing for cyberattacks.
- One of the more interesting developments for Chinese society is that the one-child policy will soon lead to a situation where most Chinese children won't have much of an extended family. Only children for generations are those who eventually lack aunts and uncles. It is unclear what sort of impact this will have, but a [recent report](#) by Eberstadt and Verdery explores the issue. On a related issue, [China is expected to release data](#) from its 2020 census soon.

International news: Our roundup.

- Myanmar's junta is considering [extending military rule](#) for up to two years as the government tries to cope with continued unrest.
- The U.S. is [considering retaliation](#) against Russia for its recent cyberattacks and other nefarious activities. The EU should take notice; the Biden administration is considering [appointing a special envoy to thwart the NordStream 2 pipeline](#).

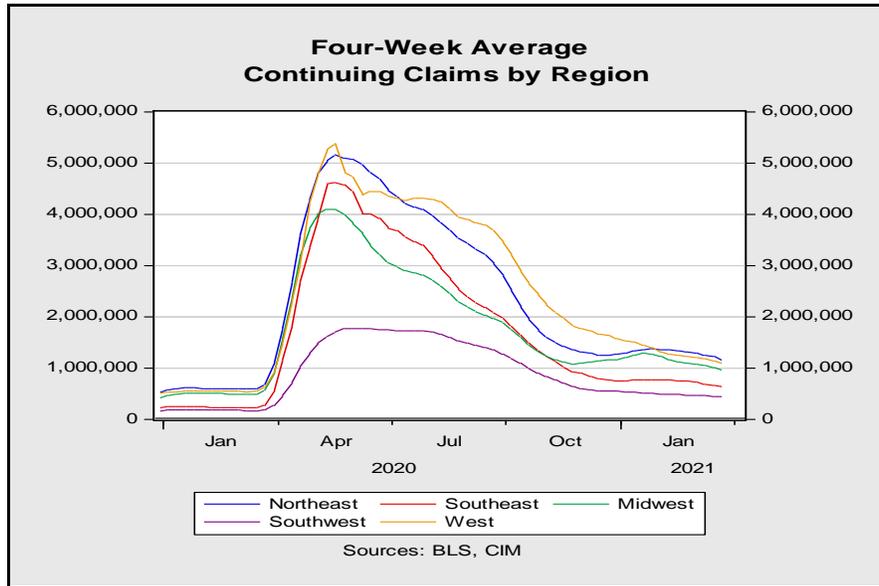
U.S. Economic Releases

Initial claims rose for the second consecutive month, potentially casting doubt on the strength of the recovery. For the week ending April 3, initial claims came in at 744K up from the previous week's reading of 728K. Initial claims were expected to come in at 680K.



The chart above shows four-week moving average of initial claims. The moving average rose from 721.25K to 723.75K.

In the preceding week, continuing claims came in at 3.734MM, down from the previous reading of 3.750MM. Forecasters expected a reading of 3.683MM.



The chart above shows the four-week average of continuing claims by region.

The table below lists the domestic data releases and Fed events scheduled for the rest of today.

Economic Releases						
EDT	Indicator			Expected	Prior	Rating
9:45	Langer Consumer Comfort	w/w	4-Apr		50	***
Fed Speakers or Events						
EST	Speaker or event	District or position				
11:00	James Bullard Discusses Economic and Monetary Policy	President of the Federal Reserve Bank of St. Louis				
12:00	Jerome Powell Takes Part in IMF Panel on Global Economy	Chairman of Board of Governors of Federal Reserve				
14:00	Neel Kashkari Discusses Economic Outlook	President of the Federal Reserve Bank of Minneapolis				

Foreign Economic News

We monitor numerous global economic indicators on a continuous basis. The most significant international news that was released overnight is outlined below. Not all releases are equally significant, thus we have created a star rating to convey to our readers the importance of the various indicators. The rating column below is a three-star scale of importance, with one star being the least important and three stars being the most important. We note that these ratings do change over time as economic circumstances change. Additionally, for ease of reading, we have also color-coded the market impact section, which indicates the effect on the foreign market. Red indicates a concerning development, yellow indicates an emerging trend that we are

following closely for possible complications, and green indicates neutral conditions. We will add a paragraph below if any development merits further explanation.

Country	Indicator			Current	Prior	Expected	Rating	Market Impact
ASIA-PACIFIC								
Japan	BoP Current Account Balance	m/m	Feb	¥2916.9b	¥646.8b	¥2000.0b	**	Equity and bond neutral
	Japan Buying Foreign Stocks	w/w	2-Apr	-¥199.0b	-¥368.0b		*	Equity and bond neutral
	Japan Buying Foreign Bonds	w/w	2-Apr	¥377.0b	¥200.7b		*	Equity and bond neutral
	Foreign Buying Japan Stocks	w/w	2-Apr	¥978.4b	-¥852.4b		*	Equity and bond neutral
	Foreign Buying Japan Bonds	w/w	2-Apr	¥568.6b	-¥2393.1b		*	Equity and bond neutral
	Tokyo Avg Office Vacancies	m/m	Mar	5.42	5.24		***	Equity and bond neutral
	Bankruptcies	m/m	Mar	-14.3%	-31.5%		**	Equity and bond neutral
Japan	Consumer Confidence Index	m/m	Mar	36.1	33.8	35.5	**	Equity and bond neutral
	Eco Watchers Survey Current SA	m/m	Mar	49	41.3	45	**	Equity and bond neutral
	Eco Watchers Survey Outlook SA	m/m	Mar	49.8	51.3	51.8	**	Equity bearish, bond bearish
New Zealand	ANZ Activity Outlook	m/m	Apr	16.4	16.6		**	Equity and bond neutral
	ANZ Business Confidence	m/m	Apr	-8.4	-4.1		**	Equity and bond neutral
EUROPE								
Eurozone	PPI	m/m	Feb	1.5%	0.0%	1.3%	**	Equity bearish, bond bullish
Germany	Factory Orders	m/m	Feb	1.2%	1.4%	1.2%	**	Equity and bond neutral
	Markit Germany Construction PMI	m/m	Mar	47.5	41.0		**	Equity and bond neutral
France	Trade Balance	m/m	Feb	-5249m	-3946m		**	Equity and bond neutral
	Current Account Balance	m/m	Feb	-2.6b	-1.6b		**	Equity bullish, bond bearish
Russia	Markit/CIPS UK Construction PMI	m/m	Mar	61.7	53.3	55.0	**	Equity bullish, bond bearish
Switzerland	Foreign Currency Reserves	m/m	Mar	930.5b	914.2b		*	Equity and bond neutral
Russia	Wellbeing Fund	m/m	Mar	\$182.3b	\$182.1b		*	Equity and bond neutral
	Official Reserve Assets	m/m	Mar	573.3b	586.3b	580.0b	*	Equity bearish, bond bullish
	CPI	w/w	5-Apr	0.2%	0.2%		***	Equity and bond neutral
AMERICAS								
Brazil	FGV Inflation IGP-DI	m/m	Mar	2.2%	2.7%	2.6%	***	Equity and bond neutral
	Vehicle Sales Anfavea	m/m	Mar	189389	167391		**	Equity and bond neutral
	Vehicle Production Anfavea	m/m	Mar	200340	197035		**	Equity and bond neutral
	Vehicle Exports Anfavea	m/m	Mar	36782	33064		**	Equity and bond neutral
Mexico	Gross Fixed Investment	m/m	Jan	-10.6%	-11.5%	-12.5%	**	Equity and bond neutral
Canada	Int'l Merchandise Trade	m/m	Feb	1.04b	1.41b	1.30b	**	Equity and bond neutral
	Ivey Purchasing Managers Index SA	m/m	Mar	72.9	60		**	Equity and bond neutral

Financial Markets

The table below highlights some of the indicators that we follow on a daily basis. Again, the color coding is similar to the foreign news description above. We will add a paragraph below if a certain move merits further explanation. (Due to technical issues data could not be updated for this report)

	Today	Prior	Change	Trend
3-mo Libor yield (bps)	20	19	1	Up
3-mo T-bill yield (bps)	1	2	-1	Neutral
TED spread (bps)	19	18	1	Up
U.S. Libor/OIS spread (bps)	7	7	0	Up
10-yr T-note (%)	1.64	1.66	-0.02	Neutral
Euribor/OIS spread (bps)	-54	-54	0	Neutral
EUR/USD 3-mo swap (bps)	1	1	0	Down
Currencies				
dollar	Flat			Down
euro	Flat			Up
yen	Up			Up
pound	Flat			Up
franc	Flat			Up

Commodity Markets

The commodity section below shows some of the commodity prices and their change from the prior trading day, with commentary on the cause of the change highlighted in the last column.

(Due to technical issues data could not be updated for this report)

	Price	Prior	Change	Explanation
Energy Markets				
Brent	\$63.28	\$62.74	0.86%	
WTI	\$59.82	\$59.33	0.83%	
Natural Gas	\$2.48	\$2.46	0.94%	
Crack Spread	\$20.83	\$20.76	0.33%	
12-mo strip crack	\$18.10	\$18.04	0.30%	
Ethanol rack	\$2.06	\$2.06	0.18%	
Metals				
Gold	\$1,738.50	\$1,743.27	-0.27%	
Silver	\$25.04	\$25.16	-0.50%	
Copper contract	\$408.40	\$411.65	-0.79%	
Grains				
Corn contract	\$557.25	\$554.25	0.54%	
Wheat contract	\$615.75	\$615.50	0.04%	
Soybeans contract	\$1,422.00	\$1,418.75	0.23%	
Shipping				
Baltic Dry Freight	2092	2072	20	
DOE inventory report				
	Actual	Expected	Difference	
Crude (mb)	-3.5	-2.0	-1.5	
Gasoline (mb)	4.0	0.2	3.8	
Distillates (mb)	1.5	1.0	0.5	
Refinery run rates (%)	0.10%	0.75%	-0.65%	
Natural gas (bcf)		22.0		

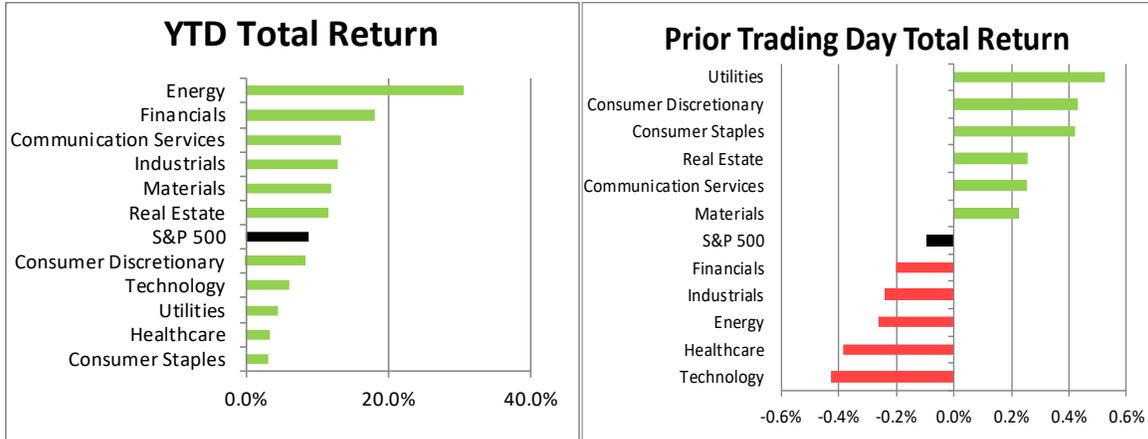
Weather

The 6-10 and 8-14 day forecasts currently call for cooler than normal temperatures for most of the country, with warmer temps in the Pacific region. The forecast calls for wetter than normal conditions along eastern and southwestern states, dry conditions are expected for most of the country.

Data Section

U.S. Equity Markets – (as of 4/6/2021 close)

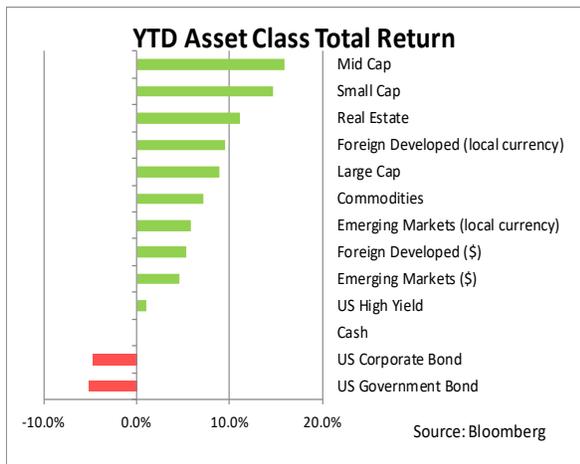
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(Source: Bloomberg)

These S&P 500 and sector return charts are designed to provide the reader with an easy overview of the year-to-date and prior trading day total return. Sectors are ranked by total return; green indicating positive and red indicating negative return, along with the overall S&P 500 in black. These charts represent the new sectors following the 2018 sector reconfiguration.

Asset Class Performance – (as of 4/6/2021 close)

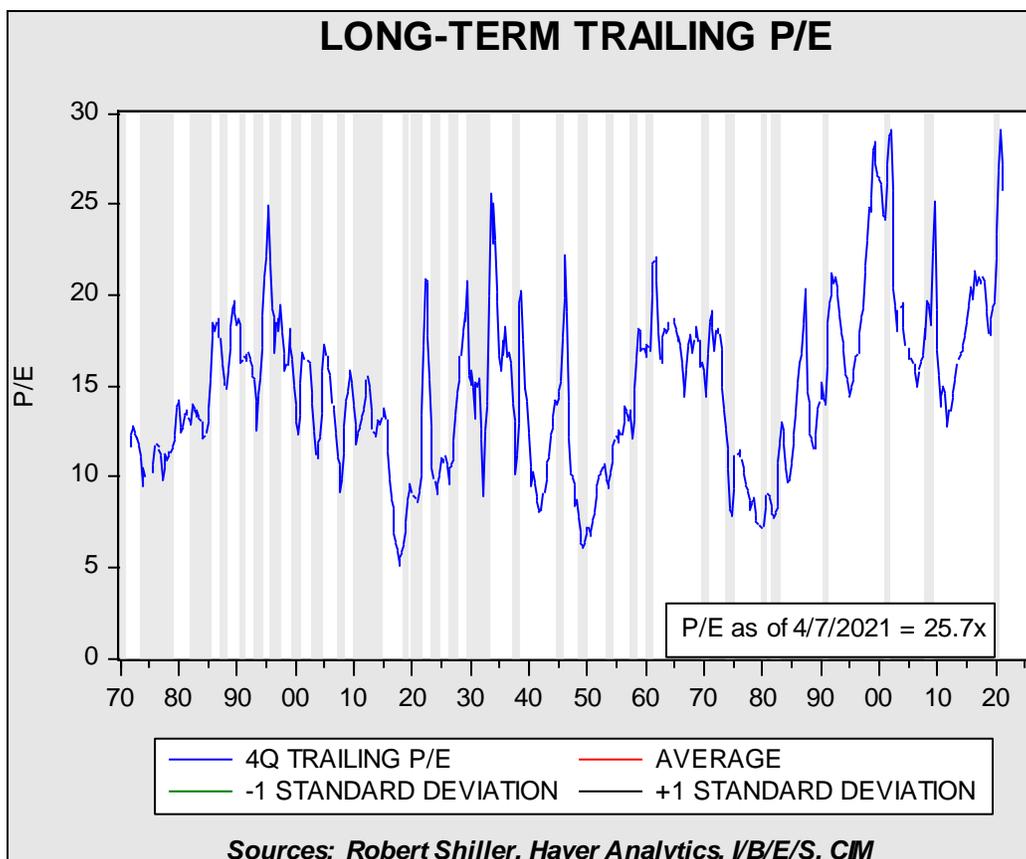


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

Asset classes are defined as follows: Large Cap (S&P 500 Index), Mid Cap (S&P 400 Index), Small Cap (Russell 2000 Index), Foreign Developed (MSCI EAFE (USD and local currency) Index), Real Estate (FTSE NAREIT Index), Emerging Markets (MSCI Emerging Markets (USD and local currency) Index), Cash (iShares Short Treasury Bond ETF), U.S. Corporate Bond (iShares iBoxx \$ Investment Grade Corporate Bond ETF), U.S. Government Bond (iShares 7-10 Year Treasury Bond ETF), U.S. High Yield (iShares iBoxx \$ High Yield Corporate Bond ETF), Commodities (Bloomberg total return Commodity Index).

P/E Update

April 1, 2021



Based on our methodology,³ the current P/E is 25.7x, down 1.4x from last week. We have moved into Q2, which affected the ratio.

This report was prepared by Confluence Investment Management LLC and reflects the current opinion of the authors. It is based upon sources and data believed to be accurate and reliable. Opinions and forward-looking statements expressed are subject to change. This is not a solicitation or an offer to buy or sell any security.

³ This chart offers a running snapshot of the S&P 500 P/E in a long-term historical context. We are using a specific measurement process, similar to *Value Line*, which combines earnings estimates and actual data. We use an adjusted operating earnings number going back to 1870 (we adjust as-reported earnings to operating earnings through a regression process until 1988), and actual operating earnings after 1988. For the current quarter, we use the I/B/E/S estimates which are updated regularly throughout the quarter; currently, the four-quarter earnings sum includes two actual quarters (Q3 and Q4) and two estimates (Q1 and Q2). We take the S&P average for the quarter and divide by the rolling four-quarter sum of earnings to calculate the P/E. This methodology isn't perfect (it will tend to inflate the P/E on a trailing basis and deflate it on a forward basis), but it will also smooth the data and avoid P/E volatility caused by unusual market activity (through the average price process). Why this process? Given the constraints of the long-term data series, this is the best way to create a long-term dataset for P/E ratios.