Daily Comment

By Patrick Fearon-Hernandez, CFA, and Thomas Wash

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 24, 2024—9:30 AM EDT] Global equity markets are higher this morning. In Europe, the Euro Stoxx 50 is up 0.4% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed up 2.8%. Chinese markets were higher, with the Shanghai Composite up 0.8% from its previous close and the Shenzhen Composite up 1.2%. US equity index futures are signaling a higher open.

With 115 companies having reported so far, S&P 500 earnings for Q1 are running at $54.00 per share, compared to estimates of $54.24, which is up 0.9% from Q1 2023. Of the companies that have reported thus far, 82.6% have exceeded expectations while 14.8% have fallen short of expectations.

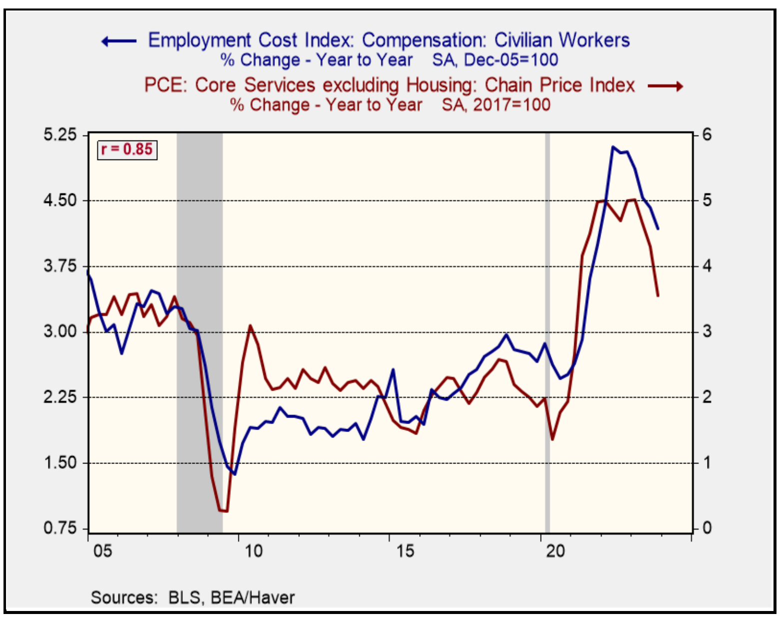
The Confluence macro team publishes a plethora of research reports and multimedia offerings on a weekly and quarterly basis, all available on our website. We highlight recent publications below, with new items of the day emphasized in bold:

- *Bi-Weekly Geopolitical Report* (4/22/2024) (with associated podcast): "The Changing Face of War"
- *Asset Allocation Quarterly – Q1 2024* (1/26/2024): Discussion of our asset allocation process, Q1 2024 portfolio changes, and our outlook for the markets.
- *Asset Allocation Q1 2024 Rebalance Presentation* (2/5/2024): Video presentation featuring the Asset Allocation Committee as they review the asset allocation strategies, recent portfolio changes, and the current macro environment.
- *Asset Allocation Bi-Weekly* (4/15/2024) (with associated podcast): "The Incremental Uranium Demand for Weapons"
- *The 2024 Outlook: Slow-Bicycle Economy* (12/18/2023) (with associated *Confluence of Ideas* podcast)
- *Confluence of Ideas podcast* (2/13/2024) "Reviewing the Asset Allocation Rebalance: Q1 2024"
- *Keller Quarterly* (4/18/24)

Good morning! Stocks are surging on good news from Tesla. In the NHL, the Florida Panthers stole another victory, extending their series lead to 2-0 against the Tampa Bay Lightning. Today's *Comment* examines how rising labor power could complicate the Federal Reserve's fight against inflation. We also explain why markets are reacting positively to the latest PMI data and discuss how global investors are keeping a close eye on upcoming elections in India. As usual, the report concludes with a round-up of international and domestic news releases.

US Labor Power: Workers have scored a string of victories since the pandemic's end, but these gains are now coming with drawbacks.

- The Federal Trade Commission has enacted a rule banning non-compete clauses used by employers. This change empowers 30 million workers to pursue opportunities at competing firms without fear of recourse, potentially boosting their wages and career mobility. Additionally, the Department of Labor also expanded overtime pay eligibility to salaried workers earning under $58,600 annually, significantly increasing the threshold from $35,500. These combined changes to labor rules will likely face resistance from businesses and advocacy groups through the court system, but also signal a potential shift in power dynamics, with workers gaining more leverage.
- Regulations enhancing workers' bargaining power, coupled with an exceptionally tight labor market, pose a formidable challenge to the Federal Reserve's efforts to curb inflation. The close correlation between the PCE core services index and the employment cost index is a critical indicator, suggesting a potential wage-price spiral. In this scenario, rising wages could be offset by price increases as businesses pass on higher labor costs to consumers. This dynamic explains why policymakers like Atlanta Fed President Raphael Bostic prefer restrictive-for-longer monetary policy as the economy continues to add jobs at a healthy clip.

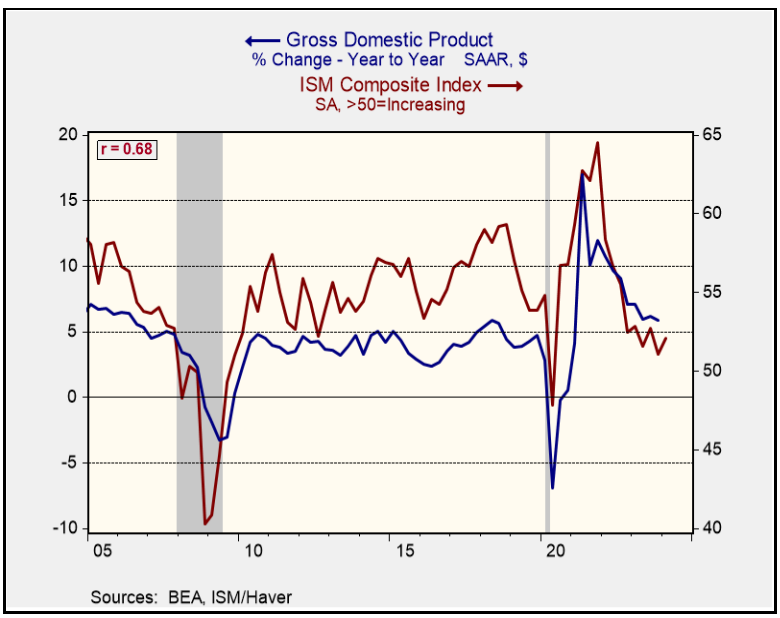


- Stronger worker bargaining power could signal a shift in economic priorities, potentially favoring greater equity over pure efficiency. Historically, periods with stronger worker rights and income equality have often coincided with higher employment and inflation. While artificial intelligence may eventually ease some price pressures, its uneven adoption across sectors makes the timeline uncertain. This could lead the Federal Reserve to raise its neutral rate — the interest rate considered neither stimulative nor restrictive —

to manage inflation. It may be close to around 3% to 4%, which is above the Fed's long-term projection of 2.5% as outlined in its summary of economic projections.

US Loss is Europe's Gain: The purchasing manager survey has boosted investor confidence, suggesting an improvement in market conditions for both the US and Europe, albeit for different reasons.

- Disappointing Purchasing Managers' Index (PMI) data released on Tuesday revealed a sudden contraction in both the US services and manufacturing sectors. This is a significant shift from expectations of continued growth. The services PMI dropped from 51.7 to 50.9, and manufacturing fell to 49.9 from 51.9. Notably, the employment indicator also dipped for the first time since June 2020, raising concerns about a potential slowdown in job growth. Remember, readings below 50 in the PMI indicate a decline in private sector activity. The dollar fell following the report as it weakened the case for prolonged policy restrictions.
- However, a brighter picture emerges in Europe. Both the eurozone and UK PMI data indicated an acceleration in growth. The composite euro area index climbed from 50.3 to 51.4, while the UK composite index surged from 52.8 to 54.0. This robust upswing fuels hope that the worst of the economic downturn might be receding, especially as these countries prepare to cut policy rates sometime this summer. Despite the overall improvement in the index, manufacturing PMIs in both the eurozone and the UK remain in contraction territory.



- The contrasting economic picture could favor European equities, especially if it leads to a weaker dollar. A potential slowdown in the US might prompt the Fed to keep the door open for rate cuts this year as it aims to avoid a policy misstep. A disappointing GDP report tomorrow, although unlikely, could further encourage the Federal Open Market Committee to maintain a neutral-to-dovish stance at its meeting next week. Meanwhile, stronger GDP data in Europe and the UK could offer support for the euro (EUR) and pound (GBP) as these countries contemplate loosening monetary policy in the coming months.

Indian Elections: Prime Minister Narendra Modi looks to tighten the grip on his government as voters head to polls for the first of six phases of voting.

- Modi and his Hindu nationalist Bharatiya Janata Party (BJP) are widely anticipated to clinch victory in the election, with official results slated for release on June 4. Meanwhile, the opposition, spearheaded by the once-dominant Indian National Congress, seems to be grappling with internal discord, which has cast a shadow of doubt on whether the coalition can stay together to form a government if it wins. The weakness has given Modi an opportunity to attack his rivals over their welfare plan, suggesting it could lead to a redistribution of wealth to benefit minority groups, particularly Muslims.
- While the BJP is heavily favored, its goal of securing over 400 out of the 543 parliamentary seats — a milestone not achieved since 1984 — might be harder to achieve. A cornerstone of the group's reelection bid lies in the robustness of the economy, consistently ranked among the world's fastest growing. Nonetheless, criticism looms over the party's approach, with concerns raised about economic growth being accompanied by widening income disparities, especially in rural areas. Additionally, the country's unemployment rate remains a significant concern, standing at over 7% — a sharp increase from the sub-4% rate we saw nearly a decade ago.

- The reelection of Modi is poised to be welcomed by markets, with investors viewing him as instrumental in steering the country towards robust and sustainable growth. However, the election has proven to be more hostile than in previous years. Attacks on voting booths and allegations of vote rigging, especially in regions favoring the incumbent, have surfaced. As a result, there have been calls for a redo of voting in several areas. An extension of an already long electoral contest risks diminishing investor optimism.

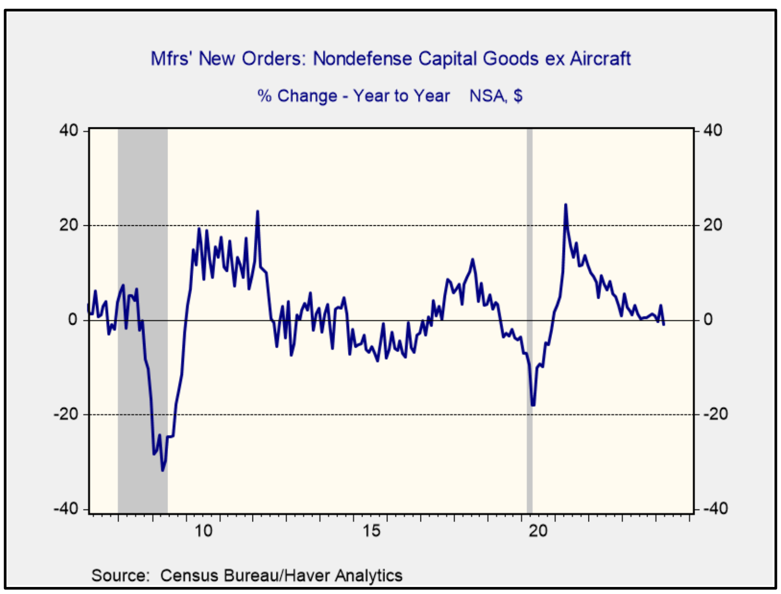
Although we expect the election to end in line with expectations, there is an elevated chance of unrest following the results.

In Other News: The US [Senate passed a bill that could force a ban on TikTok,](#) owned by Chinese company ByteDance. This move, while likely to face legal challenges, underscores the deepening tensions between the US and China. In [Pennsylvania's primary elections,](#) both President Biden and former President Trump secured comfortable victories, but also saw a notable number of protest votes.

US Economic Releases

The Mortgage Bankers Association today said ***mortgage applications*** in the week ended April 19 fell 2.7%, compared to last week's gain of 3.3%. Applications for home purchase mortgages fell 1%. Applications for refinancing mortgages fell 5.6%. According to the report, the average interest rate on a 30-year mortgage rose to 7.24%, compared to 7.13% the previous week.

March ***durable goods*** orders rose by a seasonally adjusted 2.6%, compared to an expected 2.5%. Every other reporting category met expectations. Durable goods orders are often driven by transportation equipment, where just a few airliner orders can have a big impact. March ***durable goods orders excluding transportation*** rose 0.2%. Finally, the durable goods report also includes a key proxy for corporate capital investment. In March, ***nondefense capital goods orders ex-aircraft*** also rose 0.2%. Compared with the same month one year earlier, overall durable goods orders in March rose 3.62%, while durable orders ex-transport fell 1.89%. Nondefense capital goods orders ex-aircraft fell 0.83%. The chart below shows the progression of nondefense capital goods orders ex-aircraft since just before the previous recession.



There are no economic releases or Fed events scheduled for the rest of the day.

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	Services PPI	y/y	Mar	2.3%	2.2%	2.1%	*	Equity and bond neutral
Australia	CPI	y/y	Mar	3.5%	3.4%	3.4%	***	Equity and bond neutral
New Zealand	Trade Balance NZD	m/m	Mar	588m	-218m	-315m	**	Equity and bond neutral
	Exports NZD	m/m	Mar	6.50b	5.89b	5.79b	**	Equity and bond neutral
	Imports NZD	m/m	Mar	5.91b	6.11b	6.10b	**	Equity and bond neutral
South Korea	Consumer Confidence	m/m	Apr	100.7	100.7		*	Equity and bond neutral
EUROPE								
Germany	IFO Business Climate	m/m	Apr	89.4	87.9	88.8	***	Equity bullish, bond bearish
	IFO Current Assessment	m/m	Apr	88.9	88.1	88.7	**	Equity and bond neutral
	IFO Expectations	m/m	Apr	89.9	87.7	88.9	***	Equity and bond neutral
Italy	Consumer Confidence	m/m	Apr	95.2	96.5	96.8	***	Equity bearish, bond bullish
	Manufacturing Confidence	m/m	Apr	87.6	88.4	89.2	***	Equity bearish, bond bullish
	Economic Sentiment	m/m	Apr	95.8	97.0		**	Equity and bond neutral
AMERICAS								
Mexico	International Reserves Weekly	w/w	19-Apr	$217261m	$217186m		*	Equity and bond neutral
Brazil	FGV Consumer Confidence	y/y	Apr	93.2	91.3		*	Equity and bond neutral

Financial Markets

The table below highlights some of the indicators that we follow daily. 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.

Fixed Income	Today	Prior	Change	Trend
3-mo Libor yield (bps)	558	559	-1	Flat
3-mo T-bill yield (bps)	524	522	2	Up
U.S. Sibor/OIS spread (bps)	533	532	1	Flat
U.S. Libor/OIS spread (bps)	534	534	0	Up
10-yr T-note (%)	4.64	4.60	0.04	Up
Euribor/OIS spread (bps)	388	389	-1	Down
Currencies	**Direction**			
Dollar	Up			Up
Euro	Down			Down
Yen	Flat			Down
Pound	Down			Down
Franc	Down			Down

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.

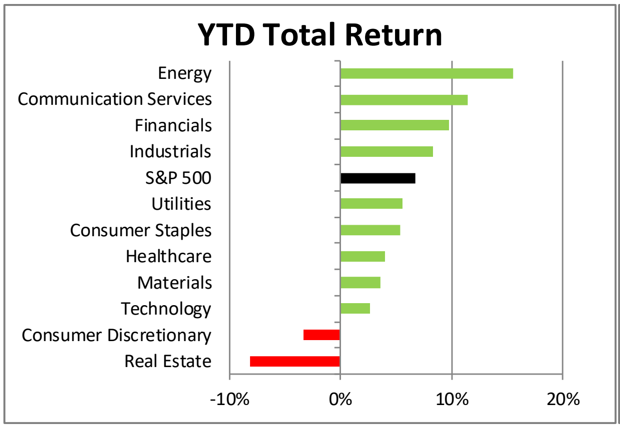
DOE Inventory Report	Price	Prior	Change	Explanation
Energy Markets				
Brent	$88.18	$88.42	-0.27%	
WTI	$83.00	$83.36	-0.43%	
Natural Gas	$1.80	$1.81	-0.44%	
Crack Spread	$28.58	$28.40	0.64%	
12-mo strip crack	$24.12	$24.12	-0.02%	
Ethanol rack	$1.84	$1.83	0.21%	
Metals				
Gold	$2,315.67	$2,322.02	-0.27%	
Silver	$27.09	$27.31	-0.78%	
Copper contract	$448.80	$446.00	0.63%	
Grains				
Corn contract	$451.75	$452.50	-0.17%	
Wheat contract	$599.25	$602.75	-0.58%	
Soybeans contract	$1,180.75	$1,182.00	-0.11%	
Shipping				
Baltic Dry Freight	1,804	1,882	-78	
DOE Inventory Report				
	Actual	**Expected**	**Difference**	
Crude (mb)		2.0		
Gasoline (mb)		-1.4		
Distillates (mb)		-1.8		
Refinery run rates (%)		0.5%		
Natural gas (bcf)		86		

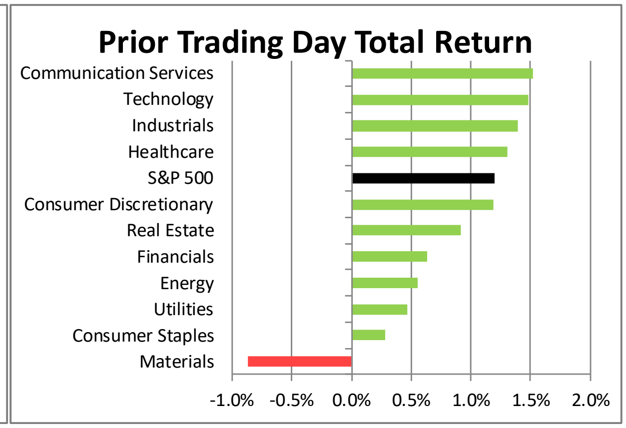
Weather

The 6-10 and 8-14 day forecasts call for warmer-than-normal temperatures across the majority of the country, with the exception of cooler-than-normal temperatures expected in the Pacific Northwest. The current precipitation forecast predicts wetter-than-average conditions across the Great Plains, Northern Tier, and Pacific Northwest, while the lower Atlantic coast is expected to experience drier conditions.

Data Section

US Equity Markets – (as of 4/23/2024 close)

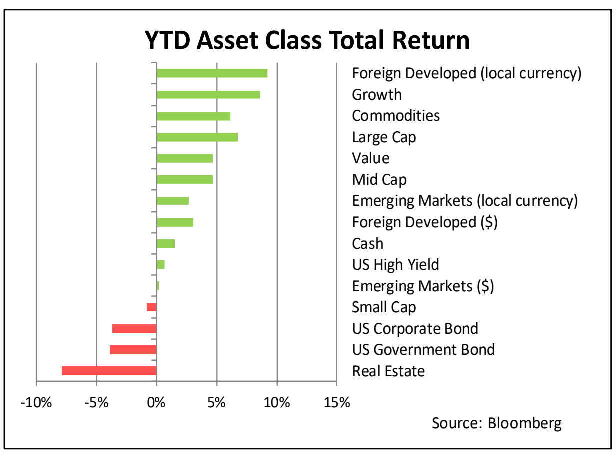




(Source: Bloomberg)

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 4/23/2024 close)

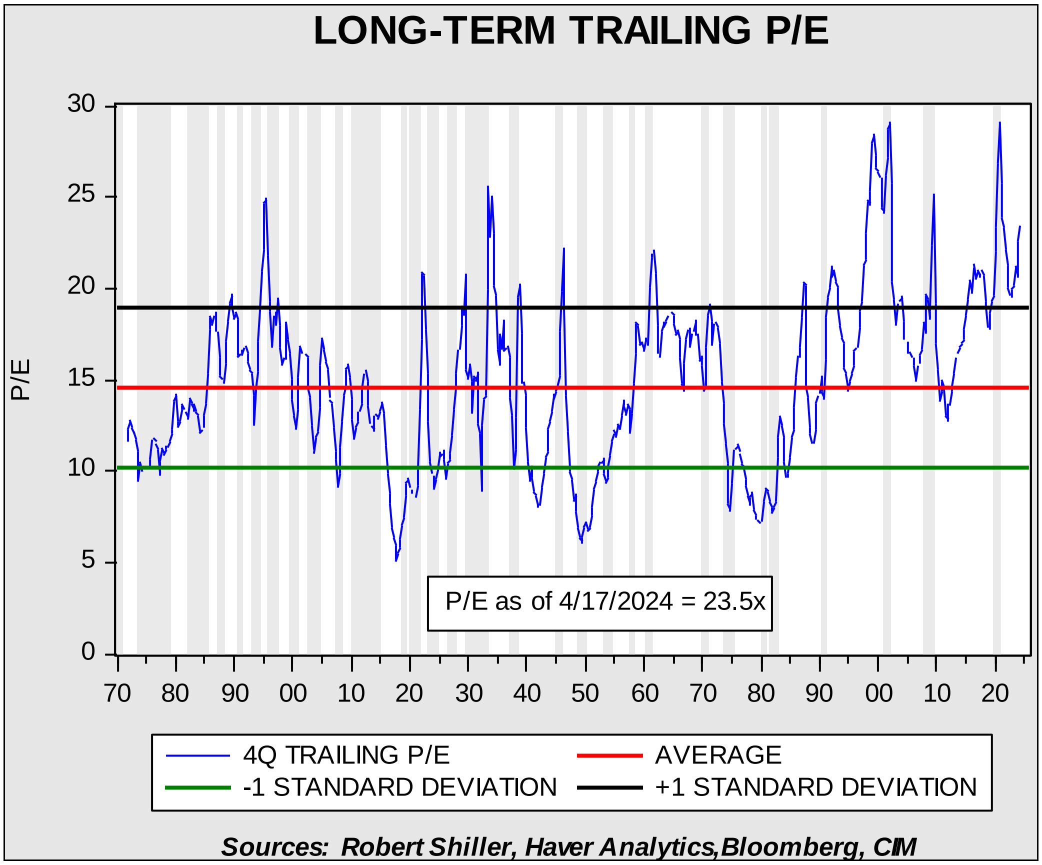


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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), US Corporate Bond (iShares iBoxx $ Investment Grade Corporate Bond ETF), US Government Bond (iShares 7-10 Year Treasury Bond ETF), US High Yield (iShares iBoxx $ High Yield Corporate Bond ETF), Commodities (Bloomberg total return Commodity Index), Value (S&P 500 Value), Growth (S&P 500 Growth).

P/E Update

April 18, 2024



Based on our methodology,[1] the current P/E is 23.5x, up 0.1x from our last report. The increase in the multiple reflects a slight decrease in earnings, outweighing the decline in the stock price index.

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[1] 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 Bloomberg estimates which are updated regularly throughout the quarter; currently, the four-quarter earnings sum includes three actual quarters (Q2, Q3 and Q4) and one estimate (Q1). 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.