

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: May 6, 2024—9:30 AM EDT] Global equity markets are higher this morning. In Europe, the Euro Stoxx 50 is up 0.8% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed up 0.9%. Chinese markets were higher, with the Shanghai Composite up 1.2% from its previous close and the Shenzhen Composite up 2.1%. US equity index futures are signaling a higher open.

With 401 companies having reported so far, S&P 500 earnings for Q1 are running at \$56.10 per share compared to estimates of \$54.24, which is up 0.9% from Q1 2023. Of the companies that have reported thus far, 79.1% have exceeded expectations, while 17.0% have fallen short of expectations.

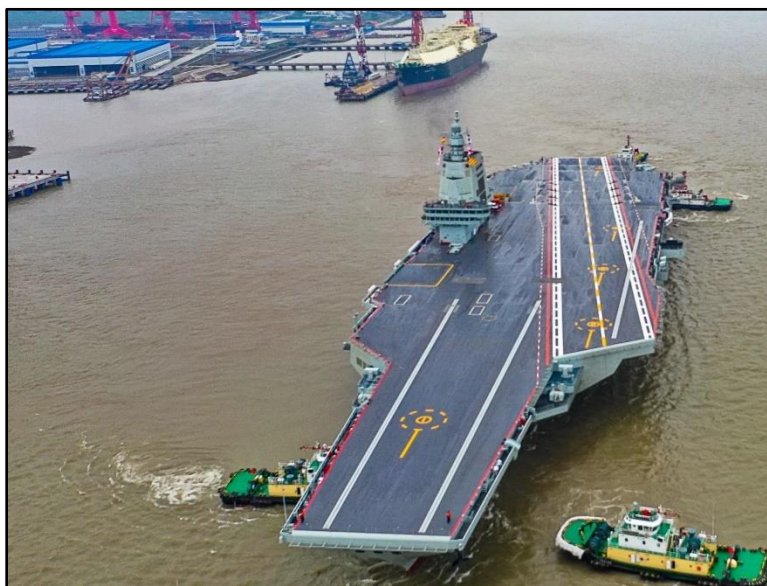
The Confluence macro team publishes a plethora of research reports and multimedia offerings on a weekly and quarterly basis, all available on our [website](#). We highlight recent publications below, with new items of the day emphasized in bold:

- **[Bi-Weekly Geopolitical Report](#)** (4/22/2024) (with associated [podcast](#)): “The Changing Face of War”
- **[Asset Allocation Quarterly – Q2 2024](#)** (4/25/2024): Discussion of our asset allocation process, Q2 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](#)** (4/29/2024) (no accompanying podcast): “The Peace Dividend, Government Debt, and Yield Curve Control”
- **[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”

Our *Comment* today opens with some notes on the China/Russia bloc’s military buildup and increasingly aggressive military operations. We next review several other international and US developments that could affect the financial markets today, including Chinese General Secretary Xi’s visit to Europe this week and a couple of notes on the US labor market.

China: The *Fujian*, China's third aircraft carrier and its first domestically-built one, reportedly [left the port of Shanghai last week for her maiden sea trial](#). According to press reports, the initial trial will focus on testing *Fujian*'s propulsion, navigation, and communications systems. Other systems, such as her state-of-the-art electromagnetic catapults, will be tested in other trials over the next year, before a planned "experimental" cruise in late 2025.

- Reports suggest the People's Liberation Army Navy (PLAN) wants to eventually maintain round-the-clock carrier coverage in both the western Pacific Ocean and the Indian Ocean. To account for vessels out of action for maintenance, training, transit, etc., that implies the PLAN will ultimately need at least three more carriers.
- As we've noted before, the Communist Party continues working to boost China's "comprehensive power" in diplomacy, economics, technology, culture, and military capability. China's surging economic heft was long the main source of its power. However, now that the country has begun to hit big, structural economic headwinds, its rapidly increasing military force is becoming the main threat to the US and its allies.
- As we've also noted before, many US voters and policymakers have become tired of the costs of global hegemony. The resulting populism and isolationism have probably helped encourage China and other authoritarian powers to assert themselves. A key question now is whether Beijing's growing carrier force, rapidly expanding nuclear arsenal, and other aspects of the Chinese military threat might convince Americans to coalesce again and recommit to international leadership in the name of national defense.



Fujian embarking on her maiden sea trial. (Source: South China Morning Post)

China/Russia Geopolitical Bloc: In addition to building up their armed forces, China and other members of its bloc keep launching aggressive military and intelligence operations against US treaty allies. For example, Chinese forces [continue to harass Philippine ships trying to resupply the country's marines at an outpost in the South China Sea](#). Russian intelligence services [are also reportedly ramping up their sabotage against infrastructure and defense industry facilities in NATO countries](#), including an apparent arson attack against a German defense firm last week.

- As we've noted in the past, Chinese and Russian attacks on US treaty allies are especially dangerous. If such attacks are deemed serious enough, the US could come under pressure to help defend the targeted country per their mutual defense agreement.
- Given their aggressiveness, China's military operations against the Philippines and Russia's sabotage attacks on NATO soil are probably more dangerous than most observers realize. Beijing and Moscow clearly feel emboldened, and they appear to be probing the West's willingness to defend itself. That presents a risk that they could cross a red line and potentially touch off a conflict.

China-European Union: General Secretary Xi today [began an important visit to Europe](#), where he is expected to try to break US-European unity against China on international issues such as Beijing's backing of Russia in its invasion of Ukraine and its dumping of low-cost exports onto the world market. Xi today met with European Commission President von der Leyen and French President Macron, who have taken a hard line against China's actions. However, the more conciliatory German Chancellor Scholz declined to join the meeting.

- The recent Chinese and Russian military buildups, provocative military actions, and spying have already prompted the US and its allies to start boosting their defense budgets and rebuilding their armed forces, but the progress to date has been slow and spotty.
- Notably, Prof. Steve Tsang, director of the SOAS China Institute in London and author of a new book on Xi's political thought, has argued that the general secretary is too bent on global domination to be deterred militarily. [Tsang argues that Xi is more afraid of being cut off from Western markets, capital, and technology](#), which could destabilize China's domestic economy and political environment. If true, a united European threat to freeze out China economically could help bring Beijing to heel.

United Kingdom: In local elections late last week, the ruling Conservative Party of Prime Minister Sunak [lost about half the municipal council seats it was defending](#), likely portending a significant loss in the national parliamentary elections this fall. Election observers are warning that the projected results could result in a hung parliament, in which neither the Conservatives, Labor, nor any other party can cobble together a majority. The political uncertainty is likely to be a headwind for UK equities in the coming months.

Israel-Hamas Conflict: The Israeli military today [warned Palestinians around the southern Gaza city of Rafah to evacuate ahead of its planned offensive against Hamas fighters in the area](#). The warning comes as the latest Israeli-Hamas negotiations for a peace deal appear to have faltered. Any Israeli attack on Rafah is likely to again raise concerns about the conflict broadening and potentially further isolate Israel on the world stage.

Panama: In national elections yesterday, pro-business conservative José Raúl Mulino [won the presidency, putting him in a position to carry out his agenda of reinvigorating the economy](#). Mulino has vowed to focus on infrastructure investment, such as building a train line across the country to complement the Panama Canal. [However, it isn't clear how he will approach the sudden closure of the Cobre Panama copper mine](#), which accounted for about 1% of global supply before it was suddenly shuttered last year amid protests over environmental damage.

US Labor Market: Although our *Comment* on Friday included our initial reaction to the April labor report, we want to add one more observation. Specifically, when calculated using our preferred method, [the year-over-year rise in average hourly earnings slowed much more sharply than indicated by the financial press’s measure](#). Press reports say average hourly earnings in April were up 3.9% from the same month one year earlier, slowing from a rise of 4.1% in the year to March. Our measure shows the growth rate slowed all the way to 3.2%.

- The press typically calculates annual wage growth using seasonally adjusted figures. Since both the current figure and the year-earlier one could be distorted by bad adjustments, that raises the risk of an inaccurate growth calculation. We prefer to use non-adjusted figures for year-over-year changes. We think our approach reduces the risk of inaccuracies from bad adjustment factors.
- In any case, as we noted on Friday, the report included several indicators pointing to softer labor demand, i.e., much more moderate growth in payrolls, a rise in the unemployment rate, and a contraction in the average work week. The apparent cooling in labor demand doesn’t necessarily point to a big economic contraction. Still, it could well keep the Federal Reserve on track to start cutting interest rates by late summer.

US Stock Market: In another development that touches on both the labor market and stocks, Chipotle Mexican Grill [has proposed a massive 50-to-1 stock split](#) to make it easier for small investors, including the firm’s own workers, to buy the stock. At Chipotle’s recent price of about \$3,155 per share, the split should bring the price down to about \$63. Shareholders are due to vote on the proposed split on June 6. Chipotle officials say easier access to the stock aims to improve employee retention amid labor shortages for lower-skilled workers.

US Economic Releases

There were no economic releases prior to the publication of this report. The table below lists the economic releases and/or Fed events scheduled for the rest of the day.

Economic Releases	
No economic releases for the rest of today	
Federal Reserve	
EST	Speaker or Event
12:50	Thomas Barkin Speaks on Economic Outlook
13:00	John Williams Participates in Fireside Chat
14:00	Senior Loan Officer Opinion Survey on Bank Lending Practices
District or Position	
	President of the Federal Reserve Bank of Richmond
	President of the Federal Reserve Bank of New York
	U.S. Federal Reserve

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								
Australia	Melbourne Institute Inflation	m/m	Apr	3.70%	3.8		***	Equity and bond neutral
New Zealand	ANZ Commodity Price	m/m	Apr	0.5	-1.3		**	Equity and bond neutral
	Caixin Composite PMI	m/m	Apr		52.8	52.7	**	Equity and bond neutral
China	Caixin Services PMI	m/m	Apr	52.5	52.5	52.7	**	Equity and bond neutral
India	HSBC India PMI Composite	m/m	Apr F	51.5	62.2		**	Equity and bond neutral
	HSBC India PMI Services	m/m	Apr F	60.8	61.7		**	Equity and bond neutral
EUROPE								
Eurozone	HCOB Eurozone Services PMI	m/m	Apr F	53.3	52.9	52.9	**	Equity bullish, bond bearish
	HCOB Eurozone Composite PMI	m/m	AprF	51.7	51.4	51.4	**	Equity and bond neutral
	PPI	y/y	Mar	-7.8%	-8.5%	-7.7%	**	Equity and bond neutral
Germany	HCOB Germany Services PMI	m/m	Apr F	53.2	53.3	53.3	**	Equity and bond neutral
	HCOB Germany Composite PMI	m/m	Apr F	50.6	50.5	50.5	**	Equity and bond neutral
France	HCOB France Services PMI	m/m	Apr F	51.3	50.5	50.5	**	Equity bullish, bond bearish
	HCOB France Composite PMI	m/m	Apr F	50.5	49.9	49.9	**	Equity bullish, bond bearish
Italy	HCOB Italy Composite PMI	m/m	Apr	52.6	53.5	53.3	**	Equity bearish, bond bullish
	HCOB Italy Services PMI	m/m	Apr	54.3	54.6	54.6	**	Equity and bond neutral
Switzerland	Domestic Sight Deposits CHF	w/w	3-May	461.5b	467.3b		*	Equity and bond neutral
	Total Sight Deposits CHF	w/w	3-May	473.2b	475.7b		*	Equity and bond neutral
Russia	S&P Global Services PMI	m/m	Apr	50.5	51.4		**	Equity and bond neutral
	S&P Global Composite PMI	m/m	Apr	51.9	52.7		**	Equity and bond neutral
AMERICAS								
Canada	S&P Global Composite PMI	m/m	Apr	49.3	47		*	Equity and bond neutral
	S&P Global Services PMI	m/m	Apr	49.3	46.4		*	Equity and bond neutral
Brazil	Net Debt % GDP	m/m	Mar	61.10%	60.90%	61.30%	**	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)	559	560	-1	Up
3-mo T-bill yield (bps)	523	524	-1	Up
U.S. Sibor/OIS spread (bps)	532	532	0	Up
U.S. Libor/OIS spread (bps)	534	534	0	Up
10-yr T-note (%)	4.48	4.51	-0.03	Down
Euribor/OIS spread (bps)	383	385	-2	Down
Currencies	Direction			
Dollar	Flat			Up
Euro	Up			Up
Yen	Down			Down
Pound	Up			Down
Franc	Flat			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.

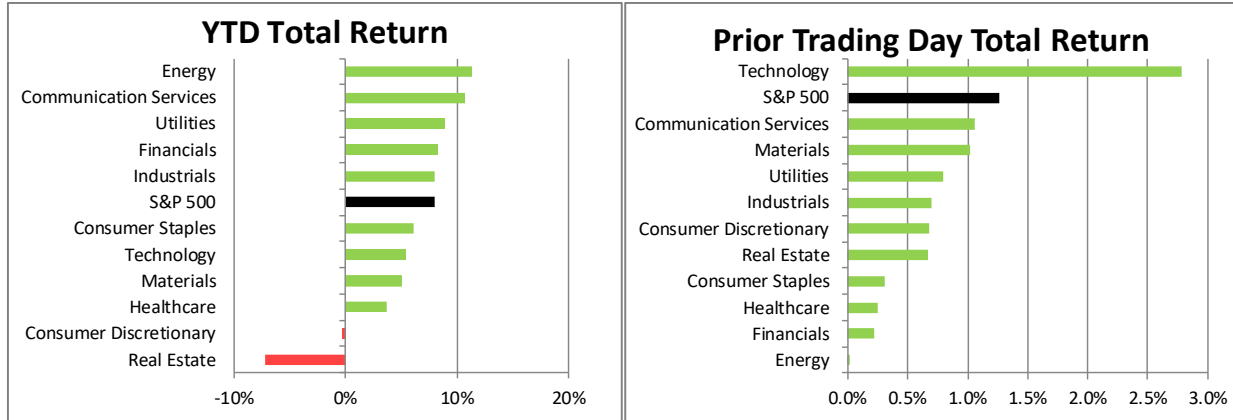
DOE Inventory Report	Price	Prior	Change	Explanation
Energy Markets				
Brent	\$83.66	\$82.96	0.84%	
WTI	\$78.85	\$78.11	0.95%	
Natural Gas	\$2.17	\$2.14	1.21%	
12-mo strip crack	\$22.79	\$23.02	-0.99%	
Ethanol rack	\$1.86	\$1.86	0.11%	
Metals				
Gold	\$2,320.44	\$2,301.74	0.81%	
Silver	\$27.15	\$26.56	2.21%	
Copper contract	\$462.95	\$455.70	1.59%	
Grains				
Corn contract	\$458.00	\$460.25	-0.49%	
Wheat contract	\$612.00	\$622.50	-1.69%	
Soybeans contract	\$1,212.25	\$1,215.00	-0.23%	
Shipping				
Baltic Dry Freight	1,876	1,774	102	

Weather

The 6-10 and 8-14 day forecasts call for warmer-than-normal temperatures in the Pacific and Rocky Mountain regions, with cooler-than-normal temperatures in the Midwest, South, and the Mid-Atlantic. The forecasts call for wetter-than-average conditions in the Southwest and New England regions, with dry conditions expected in the Pacific Northwest.

Data Section

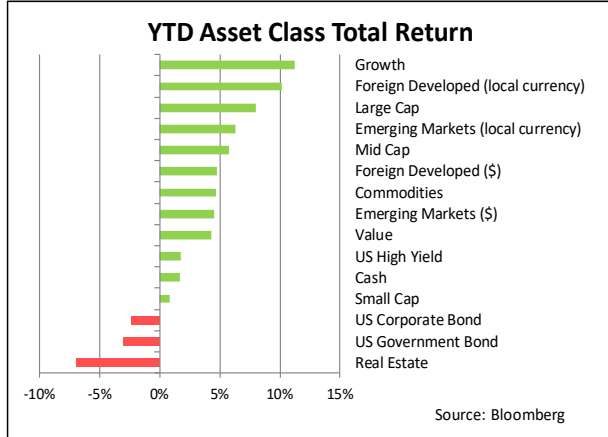
US Equity Markets – (as of 5/3/2024 close)



(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 5/3/2024 close)

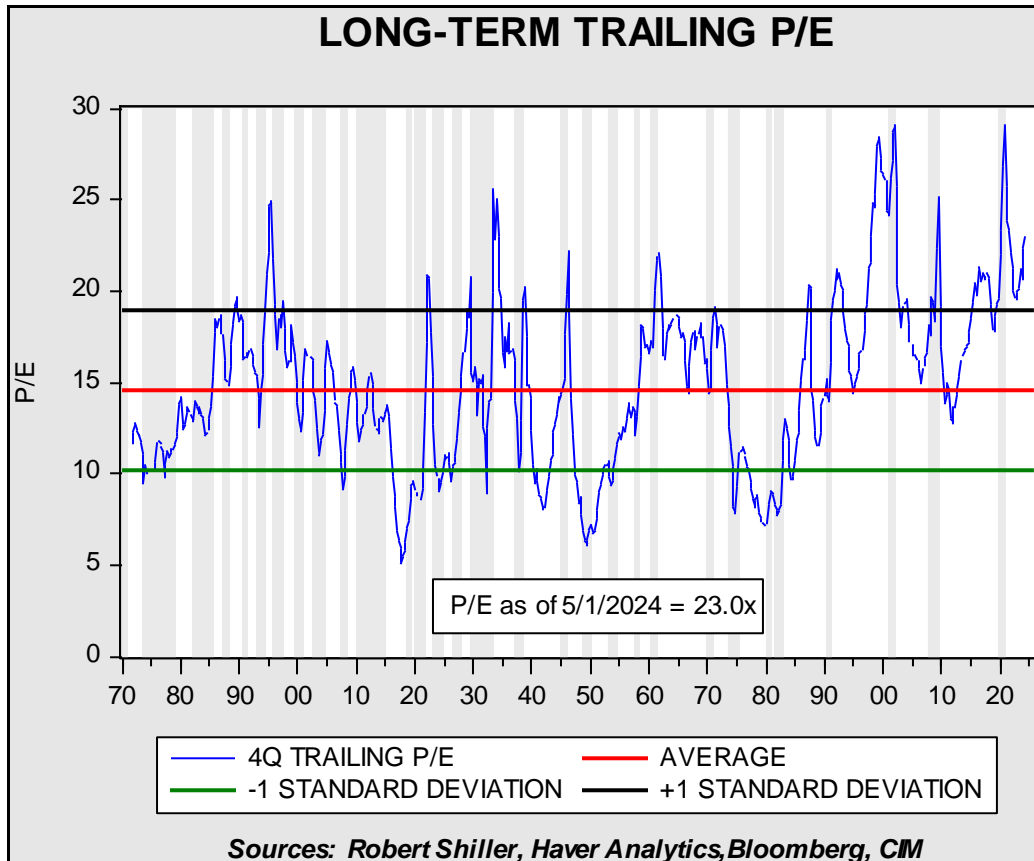


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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

May 2, 2024



Based on our methodology,¹ the current P/E is 23.0x, down 0.2x from our last report. The decrease in the multiple reflects a decline in the S&P 500 Index.

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.

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.