Daily Comment

Confluence INVESTMENT MANAGEMENT

By Patrick Fearon-Hernandez, CFA, and Thomas Wash

[Posted: April 4, 2025 — 9:30 AM ET] Global equity markets are lower this morning. In Europe, the Euro Stoxx 50 closed down 4.9% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed down 0.4%. Chinese markets are closed today for the Qingming Festival. US equity index futures are signaling a lower 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 in bold:

Bi-Weekly Geopolitical Report	Asset Allocation Bi-Weekly	Asset Allocation Quarterly	Of Note
"The Bessent Gambit" (3/24/25) + podcast	"Managing an Economic Slowdown" (3/31/25) + podcast	Q1 2025 Report Q1 2025 Rebalance Presentation	The Confluence of Ideas podcast Business Cycle Report

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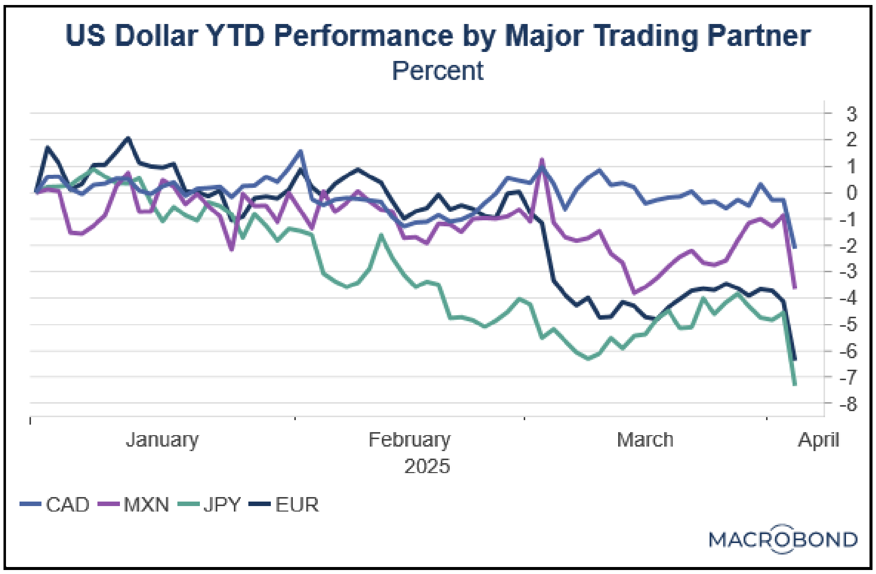
Good morning! Markets are digesting the latest jobs data while reacting to new tariffs from China. In sports, Chattanooga defeated UC Irvine to win the NIT Championship. Today's *Comment* will analyze whether the tariff impact will be temporary or long lasting, examine recession risks, and highlight other market moving news. As always, we'll close with key domestic and international economic data.

The Day After! With flat tariffs set to take effect on April 5 and even more extreme tariffs to follow four days later, the market continues to assess the potential economic impact.

- President Trump has signaled a willingness to consider reducing tariffs — but only in exchange for the right deal. His remarks suggest a potential shift, marking the first indication that he may reconsider the aggressive tariffs imposed on other countries. His response appears to be a reaction to the backlash following his tariff announcement, which triggered the worst market sell-off since the COVID pandemic.
- The sell-off has intensified this morning after China announced a 34% tariff on all US goods, along with export restrictions on rare earths, a critical resource for semiconductor production and other advanced technologies.

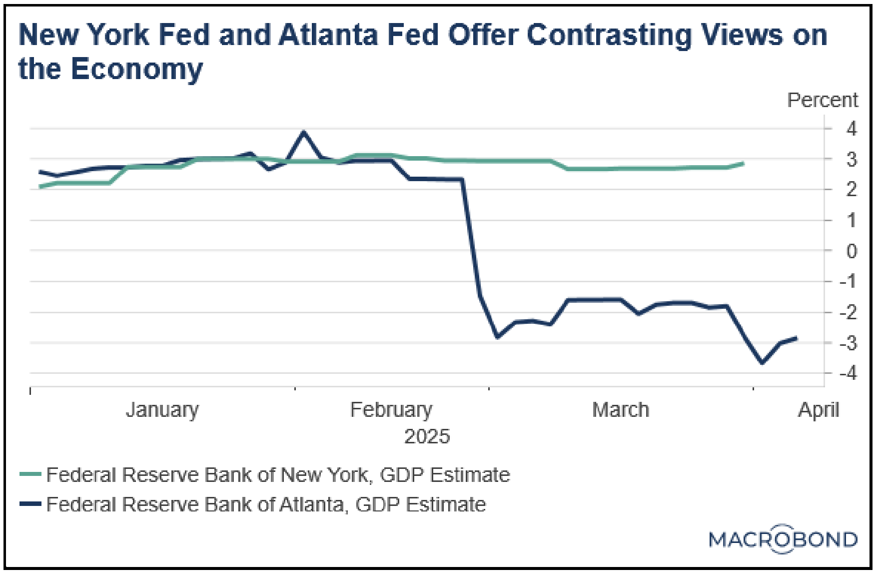
- Despite threats of retaliation from other countries, the responses to US tariffs have been relatively muted so far. Canada imposed tariffs on US auto imports but exempted those covered under the USMCA agreement. Meanwhile, France has encouraged corporations to stop investing in the US but has not put a formal law in place.
- The muted response suggests that negotiations between the US and other nations may still be underway. While existing tariffs could remain in place — and retaliatory measures from trading partners remain possible — the US's reluctance to escalate tensions after Canada's retaliatory auto tariffs signals that the White House may at least be willing to tolerate limited pushback. However, China's tariffs may be a different story.



- The key question facing markets is whether these tariffs will fundamentally reshape global trade dynamics and challenge the dollar's dominance. Yesterday's sharp decline in the US greenback suggests investors are pricing in a scenario where the US retreats from its role as global importer of last resort. This could force trading partners to accelerate currency diversification.

The Recession Question: There are growing signs that the economy is losing momentum; however, there is still no conclusive evidence of a downturn.

- In March, the ISM Services PMI dropped from 53.5 to 50.8, signaling a potential slowdown in economic momentum. The decline was primarily driven by weakening employment conditions, as survey respondents cited growing pessimism about hiring. Notably, the prices-paid component also softened, suggesting businesses may be losing confidence in their ability to sustain pricing power.
- Meanwhile, regional central banks are sending mixed signals. The Atlanta Fed's GDPNow tracker points to a sharp slowdown in recent months, while the New York Fed's Nowcast maintains its projection of steady growth. Markets appear to be more heavily weighting the Atlanta Fed's model, as its real-time tracking, though more volatile, has proven more reliable than the New York Fed's estimates in recent cycles.



- While tariffs remain a concern, markets are primarily focused on economic fundamentals. As long as data continues to show US economic expansion, a market recovery appears likely in the near term. However, should economic indicators deteriorate, the risk of a bear market would increase significantly. At this time, we still think it is a coin toss as to whether we are in midst of a downturn; therefore, we still advise investors to remain calm and patient as things play out.

Tax the Rich? Republicans may drop budget cuts and instead raise taxes on the wealthy, signaling a shift from neoliberal economics to a more populist ideology.

- Conservative lawmakers are proposing to increase the top marginal tax rate to 39.6%, reversing previous Trump-era cuts for high earners. This measure aims to offset costs while maintaining other tax reductions. The proposed revenue would fund the elimination of taxes on tips, overtime pay, and Social Security benefits, as well as the increase in the SALT deduction cap from $10,000 to $25,000.

- The move to raise taxes on top earners signals a deliberate shift by conservatives to shed their "party of the wealthy" image. Conservatives are also targeting two controversial loopholes: eliminating the carried interest tax break — long criticized for favoring private equity — and ending preferential tax treatment for sports team purchases.

- The proposed tax hike on high earners will likely face internal GOP resistance, as many members have historically pledged opposition to all tax increases. Just this year, nearly every Republican voted against measures that would limit tax cuts for the wealthy if paired with Medicaid reductions, highlighting the party's traditional stance.

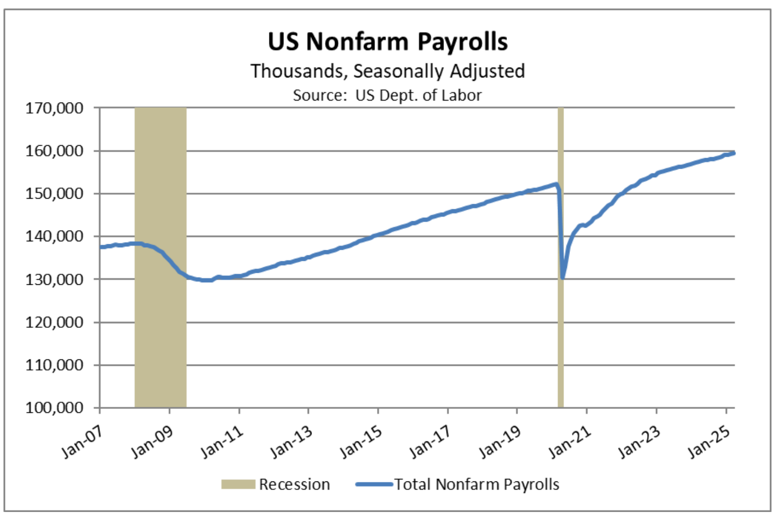
- Republican support for taxing the wealthy may be a last-ditch effort to pass their stalled tax bill. With the party divided and deficit-conscious members hesitant, this move could both satisfy fiscal conservatives and potentially draw Democratic backing. As a result, we are highly optimistic that a tax bill will be finalized over the next few weeks.

Shake Up in Defense: The president has fired several members of his National Security Council team as part of the fallout over the Signal leak.

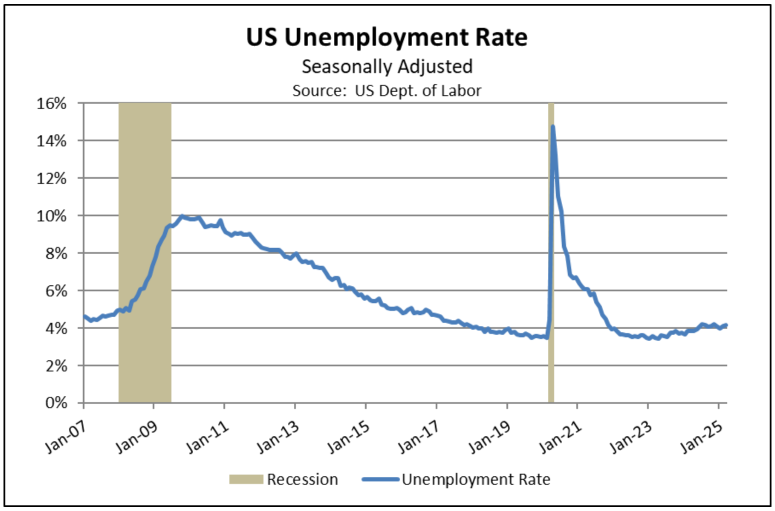
- The decision appears to stem from Laura Loomer, a social media personality and trusted Trump confidant. She reportedly urged the president to target those responsible for leaking information to a journalist during sensitive discussions about the administration's approach to Houthi conflicts in the Red Sea.
- Loomer's growing influence in the administration signals the populist wing's resurgence within a presidency that has traditionally favored tech and financial sector allies. Earlier this year, she had an X account suspended and lost access to certain pay features after she challenged Elon Musk’s stance on visas for skilled workers claiming that they go against the “America First” agenda.
- Loomer's rise amid Musk's waning clout underscores the president's transactional leadership, rotating favor between party factions as political winds shift. Should populists consolidate influence, expect a doubling down on contentious policies, potentially rattling markets with abrupt ideological pivots.

US Economic Releases

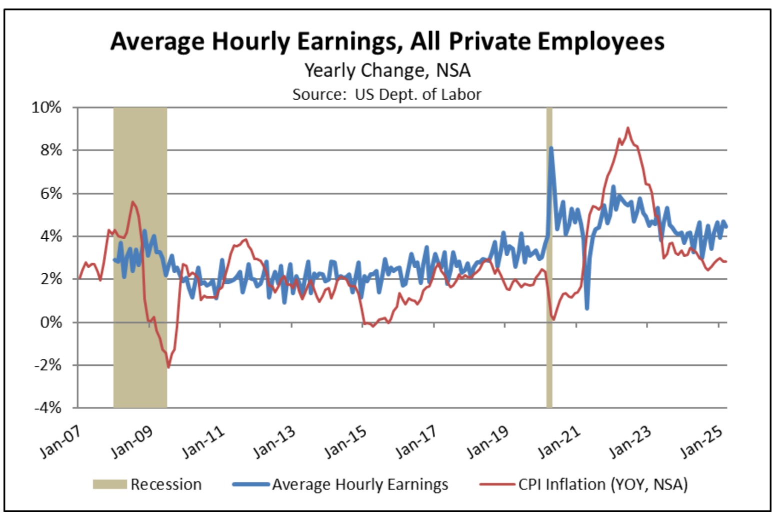
March ***nonfarm payrolls*** rose by a seasonally adjusted 228,000, smashing the expected gain of 141,000 and almost doubling the downwardly revised February rise of 117,000. As might be expected because of the Trump administration’s government personnel reductions, virtually all the job gains in March were in the private sector. The chart below shows the change in nonfarm payrolls since shortly before the Great Financial Crisis.



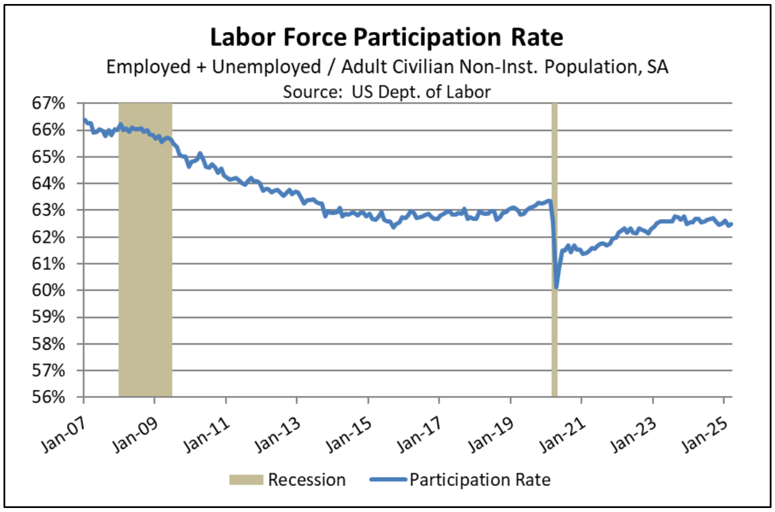
Nevertheless, despite the good job creation, the March ***unemployment rate*** rose to a seasonally adjusted 4.2%, rather than being unchanged at 4.1% as anticipated. The data shows that the rise in the rate of joblessness happened because more people started looking for work than found jobs. The chart below shows how the unemployment rate has evolved since just before the GFC.



In another potential reflection of reduced government employment in the expensive job market of Washington, DC, ***average hourly earnings*** in March rose only slightly to a seasonally adjusted $36.00, up just 3.8% from the same month one year earlier. That was a disappointment, given that average earnings were expected to rise by an annual 4.0%, as they did in February. The chart below shows the year-over-year growth in average hourly earnings since just before the GFC.



A final key indicator in the monthly employment report focuses on the share of the adult, civilian, noninstitutionalized population that is either working or looking for work. The March ***labor force participation rate (LFPR)*** rose to a seasonally adjusted 62.5%, beating expectations that it would be unchanged at 62.4%. The chart below shows how the LFPR has changed over the last several decades.



The following table lists the 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**	**District or Position**
11:25	Jerome Powell Speaks on Economic Outlook	Chairman of the Board of Governors
12:00	Michael Barr Speaks on AI and Banking	Member of the Board of Governors
12:45	Christopher Waller Speaks on Payments	Member of the Board of Governors

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	Household Spending	y/y	Feb	-0.5%	0.8%	-0.8%	**	Equity and bond neutral
Australia	Household Spending	y/y	Feb	3.30%	3.20%	3.20%	*	Equity and bond neutral
India	HSBC India PMI Composite	m/m	Mar F	595.0	58.6		**	Equity and bond neutral
	HSBC India PMI Services	m/m	Mar F	58.5	57.7		**	Equity and bond neutral
EUROPE								
Germany	Factory Orders WDA	y/y	Feb	-0.2%	0.1%	1.5%	***	Equity bearish, bond bullish
	HCOB Germany Construction PMI	m/m	Mar	40.3	41.2		*	Equity and bond neutral
France	Industrial Production	y/y	Feb	-0.4%	-1.2%	-1.3%	***	Equity bullish, bond bearish
	Manufacturing Production	y/y	Feb	-1.2%	-2.0%		**	Equity and bond neutral
Italy	Retail Sales	y/y	Feb	-1.5%	0.9%		**	Equity and bond neutral
UK	New Car Registrations	m/m	Mar	12.40%	-1.00%		*	Equity and bond neutral
	S&P Global UK Construction PMI	m/m	Mar	46.4	44.6	46.6	**	Equity and bond neutral
Switzerland	Unemployment Rate	m/m	Mar	2.9%	2.9%	2.9%	**	Equity and bond neutral
Russia	Gold and Forex Reserves	m/m	28-Mar	$645.6b	$650.4b		***	Equity and bond neutral
	Money Supply, Narrow Definition	w/w	28-Mar	17.94t	18.11t		*	Equity and bond neutral
AMERICAS								
Canada	International Merchandise Trade	m/m	Feb	-1.52b	3.13b	3.50b		Equity bearish, bond bullish
	S&P Global Canada Services PMI	m/m	Mar F	41.2	46.6		*	Equity and bond neutral
	S&P Global Canada Composite PMI	m/m	Mar	42.0	46.8		*	Equity and bond neutral
Mexico	Consumer Confidence	Mar	m/m	46.0	46.3	46.0	*	Equity and bond neutral
Brazil	S&P Global Brazil Composite PMI	m/m	Mar F	52.6	51.2		***	Equity and bond neutral
	S&P Global Brazil Services PMI	m/m	Mar	52.5	50.6		***	Equity and bond neutral
	FGV Inflation IGP-DI	y/y	Mar	8.57%	8.78%	8.53%	**	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 T-bill yield (bps)	416	419	-3	Up
U.S. Sibor/OIS spread (bps)	420	425	-5	Down
U.S. Libor/OIS spread (bps)	420	426	-6	Down
10-yr T-note (%)	3.90	4.03	-0.13	Down
Euribor/OIS spread (bps)	235	236	-1	Down
Currencies	**Direction**			
Dollar	Up	US		Down
Euro	Down	Euro		Up
Yen	Up	Japan		Up
Pound	Down	UK		Up
Franc	Down	Switzerland		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.

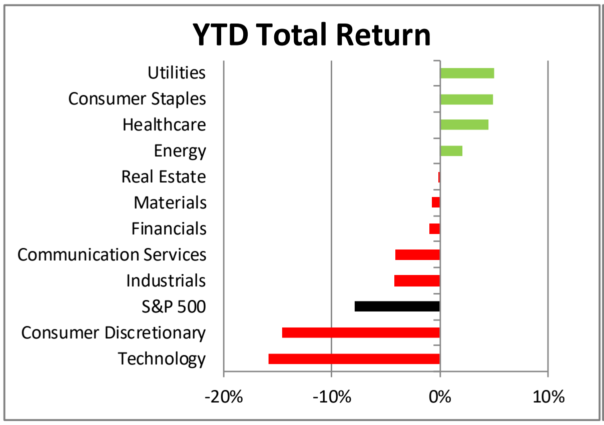
	Price	Prior	Change	Explanation
Energy Markets				
Brent	$65.48	$70.14	-6.64%	Tariffs, demand pessimism
WTI	$62.17	$66.95	-7.14%	Tariffs, demand pessimism
Natural Gas	$4.13	$4.14	-0.10%	
Crack Spread	$24.36	$24.43	-0.28%	
12-mo strip crack	$21.08	$21.60	-2.41%	
Ethanol rack	$1.90	$1.90	0.10%	
Metals				
Gold	$3,130.91	$3,115.34	0.50%	
Silver	$31.39	$31.86	-1.46%	
Copper contract	$462.90	$482.85	-4.13%	
Grains				
Corn contract	$453.00	$457.50	-0.98%	
Wheat contract	$527.00	$536.00	-1.68%	
Soybeans contract	$991.75	$1,011.50	-1.95%	
Shipping				
Baltic Dry Freight	1,540	1,583	-43	
DOE Inventory Report				
	Actual	**Expected**	**Difference**	
Crude (mb)	6.17	-0.50	6.67	
Gasoline (mb)	-1.55	-1.55	0.00	
Distillates (mb)	0.26	-0.80	1.06	
Refinery run rates (%)	-1.0%	0.5%	-1.5%	
Natural gas (bcf)	29	28	1	

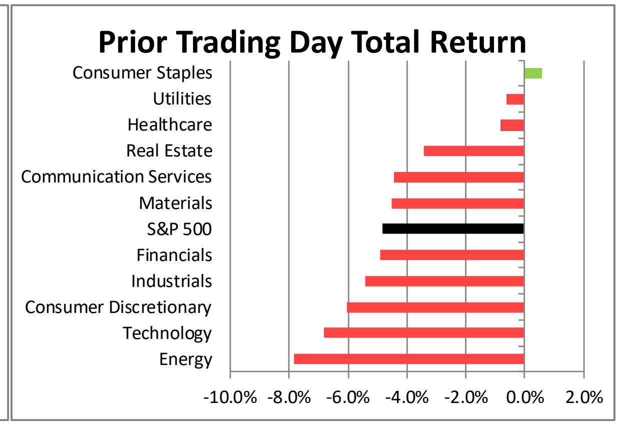
Weather

The 6-to-10 and 8-to-14-day forecasts show warmer-than-normal temperatures extending from the West Coast through the Great Plains, with cooler-than-normal temperatures from the Mississippi River eastward. The forecasts show wetter-than-normal conditions in the Pacific Northwest and the Northeast, with drier-than-normal conditions in California, the Rocky Mountains, the Great Plains, and the Mississippi Valley regions.

Data Section

US Equity Markets – (as of 4/3/2025 close)

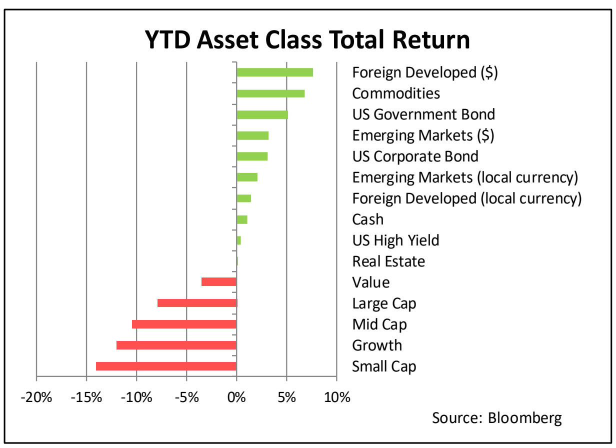




(Source: Bloomberg)

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 4/3/2025 close)

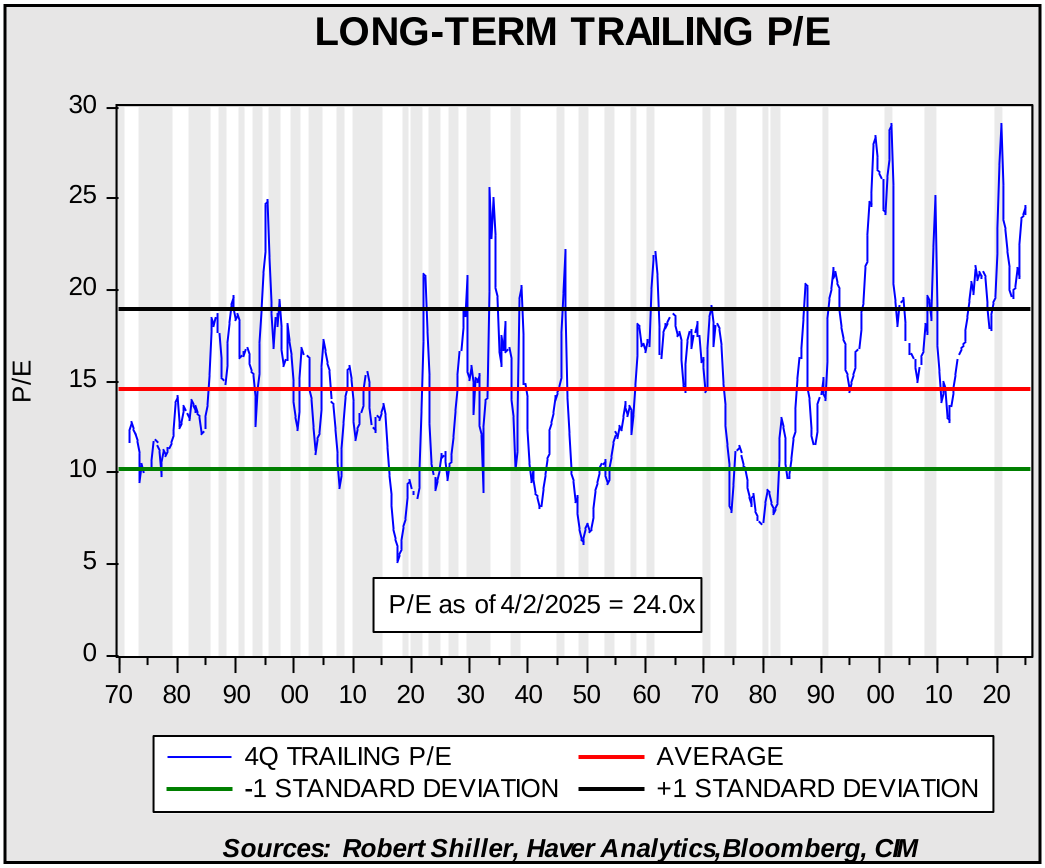


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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 3, 2025



Based on our methodology,[1] the current P/E is 24.0x, down 0.7 from our last report. The drop in the multiple resulted primarily from a decrease in the stock price index and an increase in earnings.

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.

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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 (Q1, Q2, and Q3) and one estimate (Q4). 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.