



MORNING BRIEFING

April 11, 2018

Trade War Over Already?

See the [pdf](#) and the [collection](#) of the individual charts linked below.

(1) Trade war and peace. (2) The Chinese President's speech. (3) A perfectly reasonable emperor for life. (4) Xi has turned into one of globalization's biggest defenders. (5) Trump's bilateral approach to making free trade fairer may be working. (6) Is Panic Attack #60 over yet? If so: Here comes another relief rally. (7) The best late-cycle earnings season ever. (8) Shortage of truck drivers hasn't stopped ATA Truck Tonnage Index from making new highs. (9) Record-high tonnage per truck driver: productivity or overtime?

Trade: Just Give Peace a Chance. "Suppose They Gave a War and Nobody Came" is a 1970 feature film. The title is derived from an American antiwar slogan from the hippie subculture during the Vietnam War era, popularized by Charlotte E. Keyes in her 1966 article for *McCall's* magazine titled "Suppose They Gave a War and No One Came."

President Donald Trump recently declared a trade war on China. Stock prices bounced around as the Trump administration threatened to impose tariffs on Chinese goods but gave the Chinese government 60 days to surrender to Trump's demands.

Yesterday, Chinese President Xi Jinping seemed to make peace with the US. In a [speech](#) at the Boao Forum for Asia, an annual summit (dubbed the "Asian Davos"), Xi said China will "work hard" to import more. He said: "China does not seek [a] trade surplus. We have a genuine desire to increase imports and achieve greater balance of international payments under the current account." He sounded like a perfectly reasonable world leader saying:

"We must refrain from seeking dominance and reject the zero-sum game, we must refrain from 'beggar thy neighbor' and reject power politics or hegemony while the strong bully the weak." Furthermore, countries should "stay committed to openness, connectivity and mutual benefits, build an open global economy, and reinforce cooperation within the G-20, APEC and other multilateral frameworks. We should promote trade and investment liberalization and facilitation, support the multilateral trading system. This way, we will make economic globalization, more open, inclusive, balanced and beneficial to all."

Spoken like a true champion of globalization. I have argued that Trump might actually save globalization by promoting fairer trade on a bilateral basis. That approach makes more sense than the multilateral approach, which takes too much time to negotiate and resolve trade frictions.

Xi is clearly confirming that he prefers this approach to a trade war with the US. Xi announced plans to open up China's economy, including lowering tariffs for autos and other products. He pledged to enforce the legal intellectual property of foreign firms: "We encourage normal technological exchanges and cooperation between Chinese and foreign enterprises and protect the lawful [intellectual property] owned by foreign enterprises in China." He seems like a really nice emperor for life.

Strategy: Is Panic Attack #60 Over? If the trade war is over before it even began, then the stock market should be set up for yet another relief rally that will take stock prices to new record highs. The S&P 500 peaked at a record 2872.87 on January 26 ([Fig. 1](#), [Fig. 2](#), and [Fig. 3](#)). It plunged 10.2% to a low of 2581.00 on February 8. It then rebounded only to retest the year's low by falling to 2581.88 on April 2. It was back up to 2656.87 yesterday.

Joe and I are counting the 10.2% plunge from late January through early February as the fifth correction of the current bull market. We are counting the selloff through Friday of last week as the 60th panic attack.

Hopefully, Xi's speech will allow Trump to declare victory in his short trade war with China. He probably needs to spend more time focusing on the humanitarian atrocities in Syria—not to mention his own legal issues at home following the FBI's raid on the home, office, and hotel room of his personal lawyer. We doubt that Trump's legal woes will trigger the 61st panic attack for the market. If not, then investors can go back to focusing on the fundamentals.

The Q1-2018 earnings season has just started. Industry analysts are expecting S&P 500 earnings to be up 17.0% y/y ([Fig. 4](#)). Joe and I wouldn't be surprised if earnings growth is closer to 20.0%. This would be an extraordinary occurrence at this late stage of the economic expansion. Then again, we've never seen the corporate tax rate slashed as radically as it has been as a result of the Tax Cut and Jobs Act passed on December 22, 2017.

Meanwhile, as Joe noted yesterday, forward revenues for the S&P 500/400/600 continue rising into record-high territory ([Fig. 5](#)). Forward earnings for the three indexes all rose to fresh record highs during the first week of April ([Fig. 6](#)). Our Blue Angels analysis shows that with forward earnings moving to record highs, a rebound in forward P/Es to January's highs would certainly mean new highs for the stock indexes ([Fig. 7](#)).

US Economy: Still Trucking Along. There's a shortage of truck drivers in the US. Yet somehow, the truck freight index compiled by the American Trucking Associations (ATA) continues to make new highs. A 2/9 Bloomberg [article](#) titled "The U.S. Is Running Out of Truckers" warns that "for a variety of reasons, it's truck drivers that represent the most worrisome constraint on U.S. economic growth at the moment." Consider the following:

(1) *Lifeblood.* The Bloomberg article adds, "The trucking industry is unique because it's the lifeblood of moving goods around the country, representing 70 percent of the nation's freight volume by weight. Without enough trucks and drivers on the road, some combination of things is going to happen: Shipments will be delayed, and producers will have to pay higher prices to get goods to market."

The [ATA](#) corroborates the importance of their industry to the economy: "The trucking industry is the lifeblood of the U.S. economy. Nearly 71% of all the freight tonnage moved in the U.S. goes on trucks. Without the industry and our truck drivers, the economy would come to a standstill."

(2) *Employment.* The Bloomberg article also reports the following about the number of truck drivers: "The level of employment in the truck transportation industry, the category broken out in the Bureau of Labor Statistics' employment report, is essentially unchanged since the middle of 2015. This level happens to coincide with the peak attained in the last economic cycle in 2006" ([Fig. 8](#)).

(3) *Tons of freight.* Meanwhile, the ATA Truck Tonnage Index edged down in February from its record high the previous month ([Fig. 9](#)). It is up 7.9% y/y through February using the less volatile three-month moving average ([Fig. 10](#)). That matches its highest readings since the end of 2013. This growth rate

tends to be a coincident indicator of real GDP growth on a y/y basis.

(4) *“Productivity.”* We can divide the ATA index by payroll employment in the trucking industry ([Fig. 11](#)). It has gone vertical over the past year. That’s not really a measure of productivity. Instead, it probably reflects longer hours worked by truck drivers to meet demand. So it might be a measure of fatigue rather than productivity.

Effective April 1, truckers must switch from logging their hours on paper to doing it electronically or face fines. That may reduce driver capacity by no longer allowing drivers to fudge their hours on paper to stay on the road longer.

(5) *Driverless trucks.* What about self-driving trucks? They probably are still a ways off from replacing truck drivers. One major accident could set back their implementation for some time. Meantime, the Bloomberg article laments that the prospect of technological disruption in the trucking industry is “hardly giving prospective workers the incentive to commit to multi-week classes to attain a commercial driver’s license for an industry that might be going away.”

CALENDARS

US. Wed: Headline & Core CPI 2.4%/2.1% y/y, Atlanta Fed Business Inflation, Treasury Budget - \$186.0b, MBA Mortgages Applications, EIA Petroleum Status Report, FOMC Minutes. **Thurs:** Jobless Claims 230k, Import & Export Prices 0.2%/0.3%, Weekly Consumer Comfort Index, EIA Natural Gas Report. (*Wall Street Journal* estimates)

Global. Wed: UK Headline & Manufacturing Industrial Production 2.9%/3.3% y/y, UK NIESR GDP Estimate 0.3%, China CPI & PPI 2.6%/3.3% y/y, Draghi, Lowe, Yi Gang. **Thurs:** Eurozone Industrial Production 0.1% m/m/3.6% y/y, BOE Credit Conditions & Bank Liabilities Surveys, ECB Publishes Account of March Meeting, Carney, Kuroda, Yi Gang. (DailyFX estimates)

STRATEGY INDICATORS

YRI Weekly Leading Index ([link](#)): Our Weekly Leading Index (WLI)—a good coincident indicator that can confirm or raise doubts about stock market swings—fell for the third week since reaching a new record high during the week of March 10. Since then, the WLI is down 1.2% during the final three weeks of March, after climbing eight of the prior nine weeks by a total of 8.2%. Our WLI is the average of our Boom-Bust Barometer (BBB) and Bloomberg’s Weekly Consumer Comfort Index (WCCI). Our BBB contracted 2.2% over the three-week period, following a nine-week jump of 13.0%. Jobless claims, one of the components of our BBB, rose for the third week to 228,250 (4-wa), not far from the 222,750 reading three weeks ago—which was the lowest level since 1973. Meanwhile, the CRB raw industrial spot price index, another BBB component, remains in a volatile flat trend, moving up to the middle of the range. The WCCI is at its highest reading since 2001.

S&P/Russell LargeCaps & SMidCaps ([link](#)): LargeCaps are performing about the same as MidCaps so far in 2018, but the SmallCaps are closest to their January record highs now. Here’s how they rank ytd through Monday’s close, along with their 2017 performance and their percentage changes since their record highs in January: S&P SmallCap 600 (-0.5% ytd, 11.7% in 2017, -4.9% from record high), Russell SmallCap 2000 (-1.4, 13.1, -6.0), Russell LargeCap 1000 (-2.2, 19.3, -8.8), S&P LargeCap 500 (-2.3, 19.4, -9.0), and S&P MidCap 400 (-2.4, 14.5, -7.1). Forward revenues and earnings are at record highs now for all the S&P and Russell indexes. Earnings momentum remains healthy, as the yearly change in forward earnings is up from six-year lows in early 2016 and should remain strong in 2018 due to the boost from the TCJA. In the latest week, the rate of change in LargeCap’s forward earnings

was steady at 20.1% y/y, down slightly from a seven-year high of 20.3% in mid-March, and compares to a six-year low of -1.8% in October 2015; MidCap's rose to 23.8% from 23.3%, which compares to a seven-year high of 24.0% in mid-March and a six-year low of -1.3% in December 2015; and SmallCap's rose to a seven-year high of 27.7% from 26.9%, which compares to a six-year low of 0.3% in December 2015. Here are the latest consensus earnings growth rates for 2018 and 2019: LargeCap 19.7% and 10.1%, MidCap 19.8% and 12.2%, and SmallCap 23.3% and 17.1%.

S&P 500 Growth vs Value ([link](#)): The S&P 500 Growth index is up 0.3% ytd, well ahead of the 4.9% decline for its Value counterpart. Value is still in a 10.4% correction from its January 26 record high, while Growth is down 7.8% since then. During 2017, Growth's 25.4% gain was double the 12.6% rise for Value. Growth had trailed Value in the four months following the election. Now Growth's 28.1% gain since the election is leading the 15.1% increase logged by Value. During 2016, the S&P 500 Growth index underperformed its Value counterpart by a wide margin, rising just 5.1% vs Value's 14.3% gain. Growth is expected to deliver more than double the rate of revenue growth (STRG) that Value does over the next 12 months, but forward earnings growth (STEG) is only slightly higher for Growth; specifically, 9.3% STRG and 16.9% STEG are projected for Growth, respectively, vs 4.5% and 15.9% for Value. Prior to February's selloff, Growth's P/E of 21.8 on January 26 was its highest since May 2002, while Value's 16.6 on January 3 was its highest since April 2002. Through Monday, Growth's P/E had edged up to 19.0 from its 15-month low of 18.8 on April 2 and Value's 14.1 was up from a 25-month low of 13.9 on March 23. Regarding NERI, Growth's was positive in March for an 11th straight month, and rose to a record high of 22.3% from 21.2% in February; that compares to a five-year low of -16.2% in April 2015. Value's NERI was also positive in March for an 11th month (following 33 months of negative readings), and rose to record high of 21.2% from 20.4%; that compares to a five-year low of -20.3% in April 2015. The TCJA has boosted the consensus 2018 earnings estimate and the forward profit margin for both Growth and Value. Growth's 2018 estimate has risen 6.9% vs Value's 6.2% gain. Growth's forward profit margin has jumped to a record high of 16.2% from 14.4% prior to the TCJA's passage, and Value's has risen to a 10-year high of 9.8% from 9.1%.

US ECONOMIC INDICATORS

NFIB Small Business Optimism Index ([link](#)): "It has been a remarkable 16 months for small business optimism," said NFIB president and CEO Juanita Duggan. "This is the first time in 35 years where the fewest number of small business owners have told us that taxes are their number one business problem. They've been so optimistic that they feel confident enough to raise wages and invest in their business, which grows the economy." March's Small Business Optimism Index (SBOI) slipped to 104.7 after climbing to 107.6 in February—which was the second-highest reading in the 45-year history of the survey, 1983's 108.0 being the highest. Of the 10 components of the SBOI, the two employment components—hiring plans (to 20% from 18%) and current job openings (35 from 34)—were the only ones to post an increase last month. Better business conditions (32 from 43) and sales expectations (20 from 28) were the biggest drags on March's SBOI, but NFIB's chief economist noted that these large declines were from historically high levels and still left the overall index among the 20 best in survey history. Meanwhile, earnings trends (-4 from -3) held nearly all of January's 11-point surge, posting one of the best readings in survey history.

GLOBAL ECONOMIC INDICATORS

Global Leading Indicators ([link](#)): In February, the OECD's composite leading indicators (CLIs)—designed to anticipate turning points in economic activity relative to trend six to nine months ahead—once again pointed to stable growth momentum in the OECD (100.1) as a whole. Stable growth momentum remained the assessment of CLIs for the United States (100.1), Japan (100.0), and Canada (100.5). Meanwhile, there are signs of growth losing momentum emerging in Germany (100.7), France

(100.2), Italy (100.7), and the Eurozone (100.4) as a whole; the UK's (99.2) CLI continues to point to easing growth. There are signs of strength in the emerging economies, with CLI's in Brazil (103.9), Russia (101.1), and India (100.5) pointing to growth gaining momentum, while stable growth momentum remains the outlook for China's (98.9) industrial sector.

Germany Manufacturing Orders ([link](#)): German factory orders barely budged in February after plunging at the start of this year; still, activity remained at a high level. The Economy Ministry noted, "The trend in manufacturing orders has weakened markedly. Despite the muted start to the year, orders should continue to grow. The global economy continues to be in an upswing, so that demand for German industrial goods should remain high." February billings ticked up a smaller-than-expected 0.3% (vs 1.5% consensus estimate), after a 3.5% drop from December's record high. February's advance was driven by a 1.4% rebound in foreign orders; domestic order fell for the second month, by 1.4% m/m and 3.7% over the period. A 4.6% jump in billings from within the Eurozone accounted for all of the advance in foreign orders in February, as gains in capital (7.9%) and intermediate (1.7) goods orders more than offset a 4.6% drop in consumer goods ones. Meanwhile, demand from outside the Eurozone ticked down 0.6%, with declines in intermediate and consumer goods billings more than offsetting a slight gain in capital goods orders, which have been stalled around record highs. The decline in domestic orders during February was widespread, with capital (-2.7), consumer (-0.7), and intermediate (-0.3) goods orders all in the red.

Germany Industrial Production ([link](#)): German industrial production in February fell for the second time since reaching a new record high in November. Following the release of the data, the ministry said that production has lost momentum, but added "the good order situation and the positive mood among companies suggest that the industry will remain on an upward trend," though that growth momentum is likely to be weaker than last year. That's confirmed by March's M-PMI, which fell from 63.3 in December to 58.2 by March—still a robust level. Germany's headline production—which includes construction—fell 1.6% in February and 2.0% the past three months; excluding construction, it fell 1.5% and 2.3% over the comparable periods. Manufacturing output followed a similar script, sinking 1.9% in February and 2.5% since reaching a record high in November. Over the three months through February, capital (-4.2%), intermediate (-1.3), and consumer (-0.7) goods production all contracted, though all levels remained near recent highs.

Contact us by [email](#) or call 480-664-1333.

Ed Yardeni, President & Chief Investment Strategist, 516-972-7683
Debbie Johnson, Chief Economist, 480-664-1333
Joe Abbott, Chief Quantitative Strategist, 732-497-5306
Melissa Tagg, Director of Research Projects & Operations, 516-782-9967
Mali Quintana, Senior Economist, 480-664-1333
Jackie Doherty, Contributing Editor, 917-328-6848
Valerie de la Rue, Director of Institutional Sales, 516-277-2432
Mary Fanslau, Manager of Client Services, 480-664-1333
Sandy Cohan, Senior Editor, 570-775-6823

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