In the Long Run, These Equity Losses Barely Register: Macro Man
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By Cameron Crise
(Bloomberg) -- A momentous week has ended with a thud rather than a bang (at least on the data front) as the U.S. employment numbers came out broadly in-line with expectations. To be sure, there were some notable features of the data -- a drop in both household employment and labor participation, though perhaps that was driven by the timing of Good Friday, which fell during the survey week.
You can cherry-pick whatever you like from the figures to support your pre-existing view, so at this point it's hard to say that they change much of anything. For now, the growth picture remains strong enough to support the policy trajectory that's currently priced into rates markets. That, in turn, should continue to apply pressure to equities, regardless of how "cheap" they may seem.
* From a macro perspective, the issue to focus on has clearly rotated from inflation to growth. Pretty much everyone understands that base effects will drive y/y CPI and PCE figures lower, but the run-rate of inflation will remain high enough for central banks to keep worrying ... and keep (or start) tightening. That policy trajectory will change when the growth outlook deteriorates significantly enough that demand looks more correctly aligned with supply. So that's what we'll be watching for.
* While you can point to the 353k drop in household employment as a signal that the economy is weakening, that's a pretty tenuous hook upon which to hang your hat at this point -- particularly given that household employment growth had comfortably outstripped the establishment survey over the prior six months. Moreover, the drop in the participation rate suggests the household figure may well have been a supply, rather than demand, issue -- which is problematic if the relatively elevated level of wages can still not attract fresh workers.

* Recent U.S. PMI data was disappointing, but in a sense it's kind of just reverting to its pre-Covid link with economic growth. The composite ISM (50% manufacturing, 50% services) had a pretty good linkage with quarterly real GDP growth from 1997 through 2019, though of course that relationship fractured

thanks to the crazy GDP figures we saw during 2020. Anyhow, the current composite reading (56.25) is consistent with current-quarter GDP growth of 3.3% based on the pre-Covid regression formula. Guess what the consensus forecast is for Q2 growth on the ECFC page? 3.0%.

* Incidentally, the results don't meaningfully change if we give a higher weight to services in order to more accurately reflect the structure of the economy. Anyhow, it seems fair to say that we'll need to see a notable further deterioration in the tone of the data to warrant a significant alteration in the growth forecast profile ... and thus, the expected policy trajectory. Meanwhile, it's probably worth putting this "terrible" equity market into some perspective.

* The current drawdown in the S&P 500 barely registers on a long-term logarithmic chart. In fairness, you've been hit worse if you've been tilted toward small caps, the NDX, or especially the jargon-rich, earnings-poor "innovation" complex. Last week, however, this column noted that the closest economic analogue to the current state of play was the 1960s, though some may point to the inflationary 1970s as a more-relevant precedent. Either way, look at the price action over a score of years back then and compare it to the current equity "meltdown." The losses sustained this year suddenly look like a drop in the bucket.
* Financial conditions have obviously tightened recently, but in an absolute sense they remain quite easy by historical standards. The recent peak in the GS index (where higher = tighter conditions) was still in the bottom eighth of all observations since 1982, and the bottom 8% of observations between 1982 and 2019. Is that the appropriate setting for an economy with an inflation problem? Probably not.
* The inflows that the likes of ARKK have seen this week suggests that the buy-the-dip mentality might be bloodied, but it's unbowed. Matt Damon will tell you that fortune favors the brave, but in the long run it favors the thoughtful even more. When your discount factor goes from zero to something more than zero, as is the case this year, the net present value of all future earnings goes from something tantamount to infinity to something less than infinity. (If you don't believe me, try dividing by zero in Excel!)
* That shift is real, and it's non-linear, which explains a lot of the price action in the uber-speculative complex. Given current valuations and the retail mentality, it all likely has

further to go. Markets don't move in a straight line, of course, so the occasional (vicious) bounce is to be expected. But until that SPX log chart looks a little more like 1966 or 1969, it's hard to think that the market has "done enough" to price the very manifest economic risks that will confront both Wall Street and Main Street in the months and quarters to come.

* NOTE: Cameron Crise is a macro strategist who writes for Bloomberg. The observations he makes are his own and not intended as investment advice. For more markets commentary, see the Markets Live blog.

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