



With the Fed likely to begin easing later this year amid falling inflation, CIO maintains their positive outlook for quality bonds and quality stocks. (UBS)

Labor report supports return of market optimism

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The US added fewer jobs than expected in April, according to the latest labor report, which sent equities higher and bond yields lower on Friday. The S&P 500 rose 1.3%, the largest daily gain since February, while the yield on the 10-year US Treasury fell 7 basis points to 4.5%.

In addition to a smaller-than-expected increase in employment growth, other aspects of the labor report were also on the softer side. Average hourly earnings growth was the lowest since June 2021, and the unemployment rate ticked up to 3.9%. The data came after Fed Chair Jerome Powell earlier last week downplayed concerns about possible rate hikes, prompting a return of market optimism. The S&P 500 is now 3.2% higher than its recent low in April, and the 10-year US Treasury yield is 20 basis points below its 2024 high.

Investors are likely to stay on the lookout for clear evidence that disinflation has resumed. But the latest sets of economic indicators and market development continue to support our view of a soft landing for the US economy, which should allow the Fed to cut rates later this year, providing a supportive backdrop for quality bonds and quality stocks.

The labor market looks simultaneously solid, disinflationary, and sufficiently balanced. Details of the labor report showed that in addition to the smaller rise in hourly earnings, average weekly hours worked also declined. This implies that labor income growth was weak. Also released last week was the Jobs Opening and Labor Turnover Survey (JOLTS), which pointed to fewer job openings and a lower quit rate than before the pandemic began. Both indicators have negative implications for wage growth, and should lead to a slowdown in consumer spending amid historically low household savings rate. We continue to expect a renewed fall in inflation prints in the months ahead.

The Fed remains biased toward easing. In addition to backing away from possible rate hikes, one of Powell's main messages last week was that the central bank believes the current policy is sufficiently restrictive to bring down inflation.

We remain confident that shelter inflation will fall based on data on new rental leases, while the drop in April's ISM services survey into contraction territory showed a slowdown in broader economic activity. Chicago Fed President Austan Goolsbee said that latest labor data gave him added confidence the US economy is not overheating.

Corporate earnings have been healthy. With reports in from companies that represent 80% of the S&P 500's market capitalization, the first quarter earnings seasons has been solid. Some 60% of those companies beat sales estimates, with 76% beating earnings forecasts. Guidance has also been positive, with rising bottom-up consensus earnings estimate for the second quarter. The results overall give us greater conviction in our view for 9% earnings growth for full-year 2024, with earnings growth broadening out beyond the large-cap growth companies.

So, with the Fed likely to begin easing later this year amid falling inflation, we maintain our positive outlook for quality bonds and quality stocks. We think the current bond yields are attractive, and see the potential for capital gains as investors start to price in more meaningful rate-cutting cycle in 2025 and 2026. Growing investment in generative artificial intelligence should also underpin further equity upside.

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Original report - [Labor report supports return of market optimism, 6 May 2024.](#)

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