

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: August 12, 2024 — 9:30 AM ET]** Global equity markets are mixed this morning. In Europe, the Euro Stoxx 50 is up 0.2% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed up 0.6%. Chinese markets were lower, with the Shanghai Composite down 0.1% from its previous close and the Shenzhen Composite down 0.5%. US equity index futures are signaling a higher open.

With 455 companies having reported so far, S&P 500 earnings for Q2 are running at \$61.30 per share, compared to estimates of \$58.94, which is up 8.0% from Q2 2023. Of the companies that have reported thus far, 79.7% have exceeded expectations while 15.6% 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](#) (8/5/2024) (no accompanying podcast for this report): “The US Geopolitical and Economic Bloc as an Investment Region”
- **[Asset Allocation Bi-Weekly](#) (8/12/2024) (no accompanying podcast for this report): “Is the Sahm Rule Right?”**
- [Asset Allocation Quarterly – Q3 2024](#) (7/16/2024): Discussion of our asset allocation process, Q3 2024 portfolio changes, and our outlook for the markets.
- [Asset Allocation Q3 2024 Rebalance Presentation](#) (8/6/2024): Video presentation featuring the Asset Allocation Committee as they review the asset allocation strategies, recent portfolio changes, and the current macro environment.

Our *Comment* today opens with several items on China’s international relations and domestic economy. We next review several other international and US developments with the potential to affect the financial markets today, including a statement by a British monetary policymaker calling for continued high interest rates and new data showing a recovery in US trucking demand.

**China-Philippines:** Manila [has accused the Chinese air force of harassing a Philippine military transport plane on routine patrol in Philippine airspace](#) near the disputed Scarborough Shoal last Thursday. The Chinese harassment comes despite the recent deal between Beijing and Manila to diffuse tensions over a Philippine military outpost on Second Thomas Shoal, another disputed

outcrop in the South China Sea. The new incident suggests dangerous Chinese-Philippine tensions in the disputed waters are likely to continue, despite one-off deals or lulls.



**China-Estonia-Finland:** On a more positive note, the Chinese government [has admitted that a Chinese-owned ship severed an important natural gas pipeline and damaged communication cables in the Baltic Sea](#) last October. As long suspected, the damage was caused by the Chinese ship dragging its anchor along the seabed. However, Beijing insists the incident was an accident caused by bad weather.

- The incident, which affected a pipeline and communications cables running between Finland and Estonia, had raised fears that it was a sabotage operation to punish Helsinki and Tallin for their opposition to Russia’s invasion of Ukraine. Once investigators tied the incident to the Chinese ship, it also raised concern that Beijing might be cooperating in Russian sabotage.
- Of course, the new admission by Beijing won’t necessarily end the concern about China helping Russia politically and militarily; however, it may help ease that concern in the near term.

**China:** The country’s fourth-largest mutual fund company, Harvest Fund Management, on Friday [said its chairman has resigned due to a corruption investigation](#). The resignation is probably related to Beijing’s new effort to make China a “financial superpower,” in part by cleaning the sector up and purging corrupt officials. Cutting corruption is a laudable goal, but the sector will likely be challenged by other aspects of Beijing’s program, such as capping pay for financial professionals.

- Separately, multiple Western companies [have said in their latest quarterly earnings reports that they are seeing steep declines in their sales in China](#), reflecting both weak consumer demand and a growing preference for Chinese brands.
- The statements are consistent with our view that the US and Chinese geopolitical blocs will continue to decouple. In addition to growing government-imposed trade barriers between the blocs, we think China’s cooling economic growth and reduced appetite for

foreign goods and services will increasingly weigh on foreign investment in the country, especially from the US bloc.

**United Kingdom:** Catherine Mann, an external member of the Bank of England's monetary policy committee, [has warned that consumer price inflation in the UK will likely reaccelerate](#). According to Mann, who dissented from the central bank's decision to cut interest rates earlier this month, business surveys show companies plan to continue hiking wages and prices, which will boost inflation again and require continued tight monetary policy.

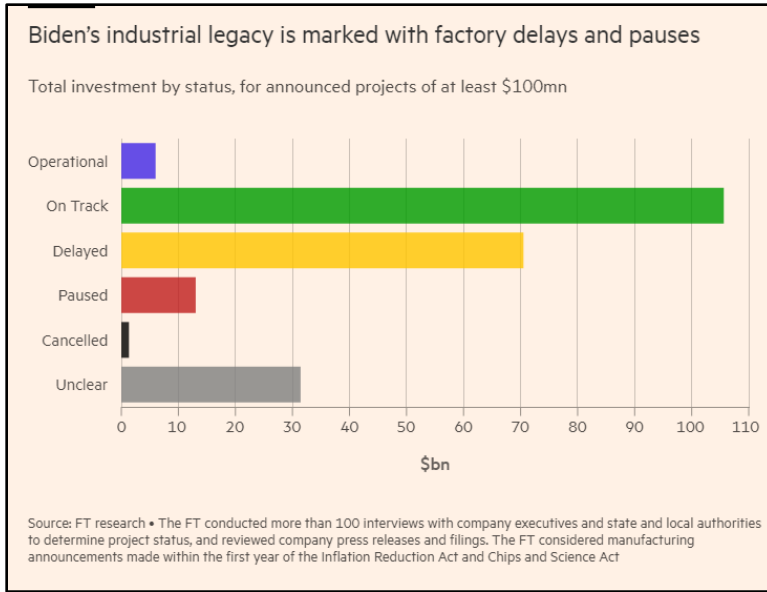
**Russia-Ukraine:** The Ukrainian military's surprise incursion into Russia's Kursk region last week [is apparently continuing](#). The Ukrainians have now advanced as much as 20 miles into Russia, and reports today say they [have tried to open up a new incursion into the Belgorod region, farther south](#). The Russian military has had to respond by stitching together several inexperienced, poorly prepared, under-strength units, and those units still have not been able to push the Ukrainians back over the border.

- The aim of the incursions may be to force the Kremlin to redeploy troops and other military assets away from the frontlines in Ukraine, easing pressure on Kyiv's troops.
- Even though Kyiv's goal may be rather limited, the incursion is embarrassing for Russian President Putin and his military officials. If it continues, it could become a more serious political problem.
- Because of that, it's important to remember that if the fighting on Russian soil continues, Putin could unleash a bigger-than-expected assault to crush the Ukrainian forces, even if it means temporarily pulling resources off the frontlines in Ukraine.

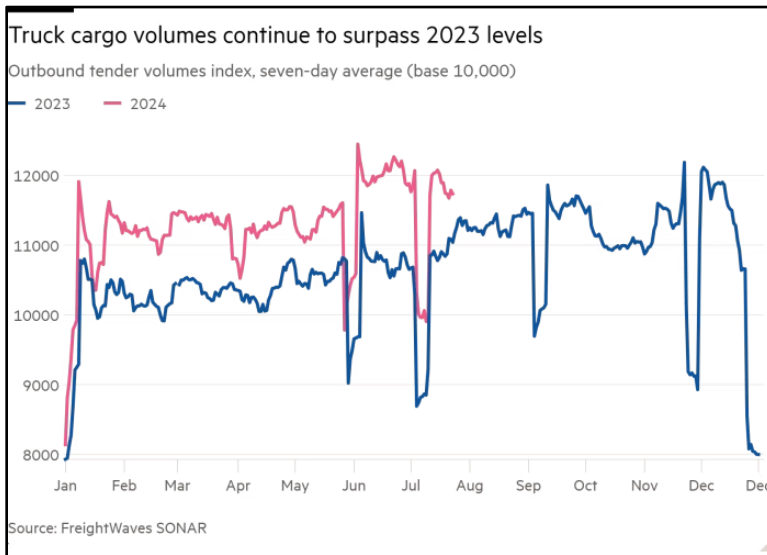
**US Politics:** At a campaign rally in Las Vegas over the weekend, Vice President Harris said that along with hiking the federal minimum wage, she [would seek to eliminate income taxes on tips](#) for service and hospitality workers. The proposal on tips echoes a recent promise by former President Trump and signals that Harris may try to meet or exceed any populist economic ideas espoused by her rival between now and the November election.

- Exempting tips from taxes would probably have only a small impact on federal revenues. After all, many service and hospitality workers have such low income that they aren't liable for taxes. Those that are liable for taxes are often in the lowest tax bracket.
- Nevertheless, if the two candidates get into a bidding war for the populist vote, they could begin to promise more costly proposals, such as big spending increases or broader tax cuts for favored groups.

**US Industrial Policy:** New research by the *Financial Times* [shows that about 40% of the factory investments announced in the first year of the CHIPS Act and Inflation Reduction Act have been delayed or paused](#). While it isn't clear whether that rate is unusually small or large for similar unsubsidized project, the data is likely to be a black eye for the Biden administration. On a more positive note, the slow progress on some projects may also reduce or slow their draw on the federal budget, lowering their negative impact on the budget deficit in the near term.



**US Trucking Industry:** New data from logistics data firm FreightWaves shows that trucking shipment orders in the second quarter were up 9% year-over-year, while tender rejections (a measure of capacity tightness) rose 1.3%. The figures suggest trucking demand is now rebounding again, even if pricing remains in the doldrums due to issues such as excess fleet size. In turn, stronger trucking demand could point to a rebound in the US industrial sector and help calm fears about a recession in the US economy.



## US Economic Releases

No major economic reports have come out so far today. The table below lists the economic releases and/or Fed events scheduled for the rest of the day.

Economic Releases						
ET	Indicator			Expected	Prior	Rating
11:00	NY Fed 1-Yr Inflation Expectations	m/m	Jul	--	3.02%	
14:00	Monthly Budget Statement	m/m	Jul	-\$242.0b	-\$66.0b	**
Federal Reserve						
No Fed speakers or events for the rest of today						

## 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
<b>ASIA-PACIFIC</b>								
<b>India</b>	CPI	y/y	Jul	5.5%	5.1%	3.6%	***	Equity bearish, bond bearish
	Industrial Production	y/y	Jun	4.2%	5.9%	5.5%	***	Equity bearish, bond bullish
<b>EUROPE</b>								
<b>Germany</b>	Wholesale Price Index	y/y	Jul	-0.1	-0.6		*	Equity and bond neutral
<b>Switzerland</b>	Domestic Sight Deposits CHF	w/w	9-Aug	455.5b	445.5b		*	Equity and bond neutral
	Total Sight Deposits CHF	w/w	9-Aug	463.1b	453.9b		*	Equity and bond neutral
<b>Russia</b>	GDP	y/y	2Q A	4.0%	5.4%	4.2%	**	Equity and bond neutral
	CPI	y/y	Jul	9.1%	8.6%	9.1%	***	Equity and bond neutral
	Core CPI	y/y	Jul	8.6%	8.7%		**	Equity and bond neutral
<b>AMERICAS</b>								
<b>Canada</b>	Net Change in Employment	m/m	Jul	-2.8k	-1.4k	25.0k	***	Equity bearish, bond bullish
	Unemployment Rate	m/m	Jul	6.4%	6.4%	6.5%	***	Equity and bond neutral
	Participation Rate	m/m	Jul	65.0%	65.3%	65.3%	*	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)	537	536	1	Down
3-mo T-bill yield (bps)	507	508	-1	Down
U.S. Sibor/OIS spread (bps)	513	513	0	Down
U.S. Libor/OIS spread (bps)	510	511	-1	Down
10-yr T-note (%)	3.95	3.94	0.01	Down
Euribor/OIS spread (bps)	356	358	-2	Down
Currencies	Direction			
Dollar	Flat			Down
Euro	Flat			Up
Yen	Down			Up
Pound	Flat			Up
Franc	Down			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.

DOE Inventory Report	Price	Prior	Change	Explanation
<b>Energy Markets</b>				
Brent	\$80.38	\$79.66	0.90%	
WTI	\$77.69	\$76.84	1.11%	
Natural Gas	\$2.24	\$2.14	4.39%	Supply Pessimism and Rising Demand
12-mo strip crack	\$21.34	\$21.20	0.65%	
Ethanol rack	\$1.95	\$1.95	0.12%	
<b>Metals</b>				
Gold	\$2,440.81	\$2,431.32	0.39%	
Silver	\$27.89	\$27.46	1.57%	
Copper contract	\$404.70	\$399.30	1.35%	
<b>Grains</b>				
Corn contract	\$393.00	\$395.00	-0.51%	
Wheat contract	\$533.75	\$542.50	-1.61%	
Soybeans contract	\$997.25	\$1,002.50	-0.52%	
<b>Shipping</b>				
Baltic Dry Freight	1,670	1,683	-13	

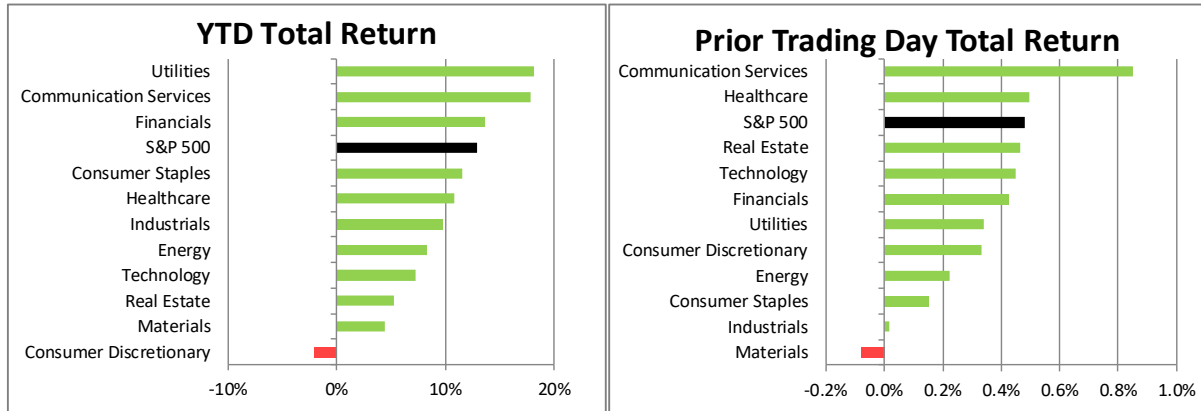
## Weather

The 6-10 and 8-14 day forecasts currently call for warmer-than-normal temperatures for most of the country, with cooler temperatures on the West Coast. The precipitation outlook calls for wetter-than-normal conditions in the Pacific Northwest and East Coast, with dry conditions in the Southwest and Great Lakes regions.

A tropical disturbance is currently located near the Leeward Islands in the Atlantic Ocean. It has a greater than 60% chance of developing into a cyclone and is expected to move towards Puerto Rico later this week.

**Data Section**

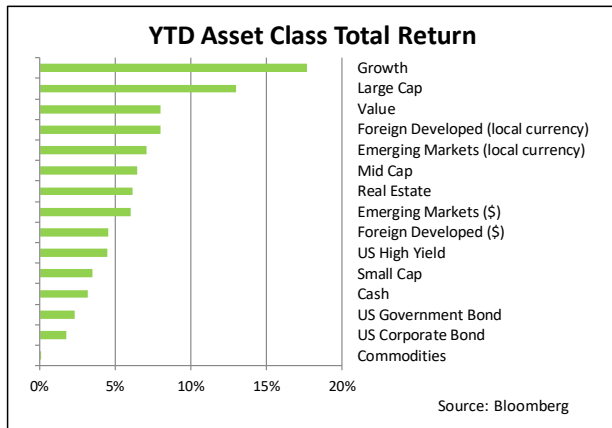
**US Equity Markets – (as of 8/9/2024 close)**



(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 8/9/2024 close)**

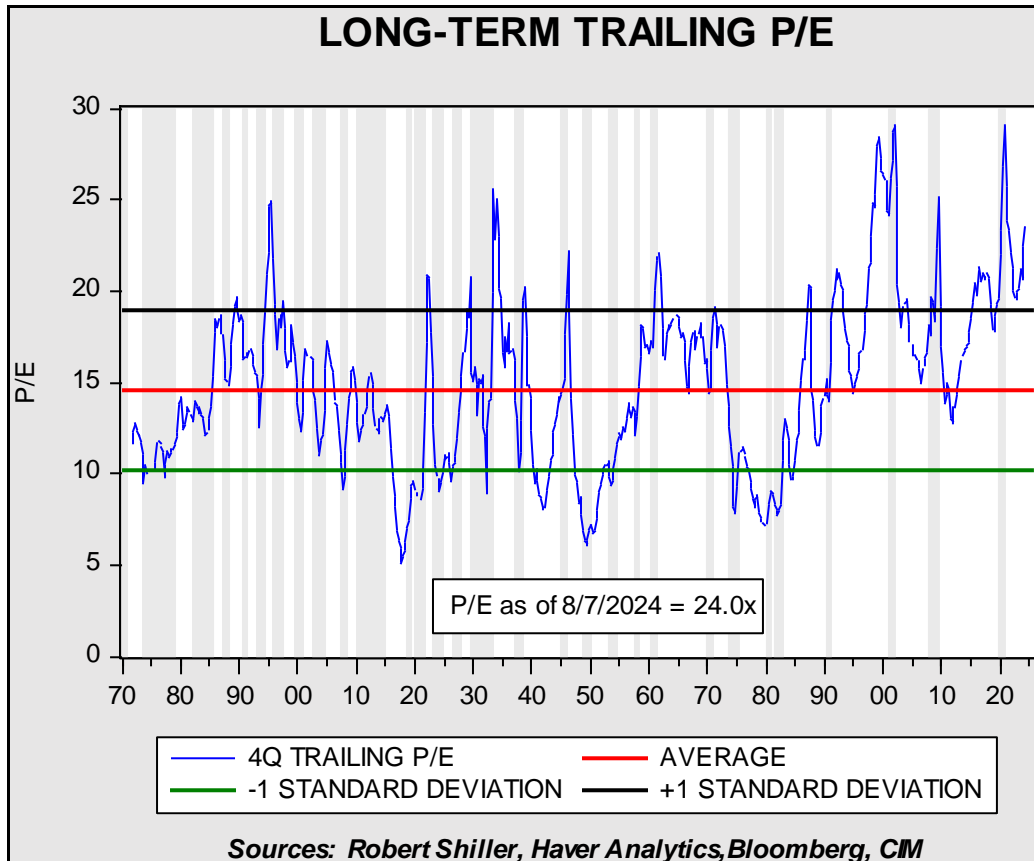


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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

August 8, 2024



Based on our methodology,<sup>1</sup> the current P/E is 24.0x, unchanged from our last report. The lack of movement in the multiple was due to the decline in the stock price index, which was offset by a decline 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.*

<sup>1</sup> 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.