Daily Comment

By Patrick Fearon-Hernandez, CFA, and Thomas Wash

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 28, 2024 — 9:30 AM ET] Global equity markets are mixed this morning. In Europe, the Euro Stoxx 50 is up 0.7% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed up 0.3%. Chinese markets were mixed, with the Shanghai Composite down 0.4% from its previous close and the Shenzhen Composite essentially unchanged. US equity index futures are signaling a lower open.

With 477 companies having reported so far, S&P 500 earnings for Q2 are running at $61.40 per share compared to estimates of $58.94, which is up 8.0% from Q2 2023. Of the companies that have reported thus far, 80.7% have exceeded expectations, while 14.9% have fallen short of expectations.

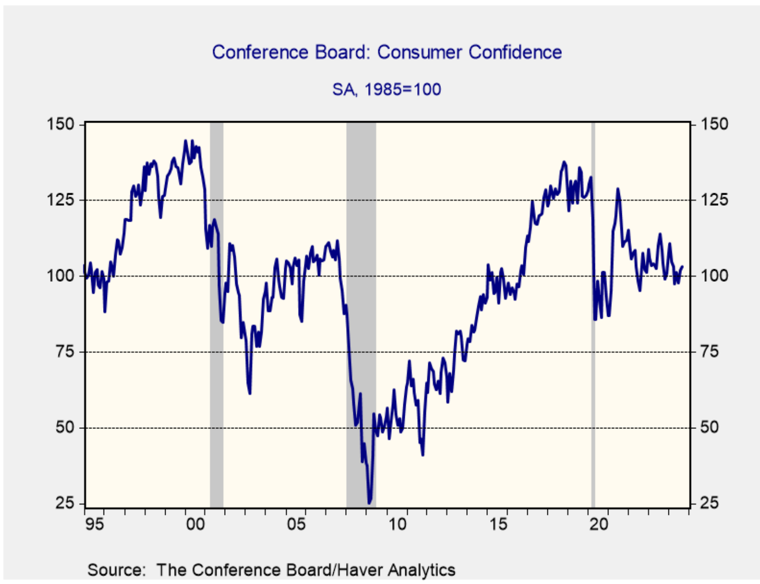
The Confluence macro team publishes a plethora of research reports and multimedia offerings on a weekly and quarterly basis, all available on our website. We highlight recent publications below, with new items of the day emphasized in bold:

- *Bi-Weekly Geopolitical Report* (8/19/2024) (no accompanying podcast for this report): "The Recent Iranian Election: Results & Implications"
- *Asset Allocation Bi-Weekly* (8/26/2024) (with associated podcast): "Activist vs. Accommodative Treasury Issuance"
- *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.

Good morning! Anticipation is high for Nvidia's upcoming earnings report as markets hope for another strong performance. In sports news, NCAA football is considering eliminating the spring transfer window. Today's *Comment* will explore the reasons behind rising confidence but declining job expectations. We will then delve into the ongoing clash between governments and social media companies and analyze Argentina President Javier Milei's policy adjustments. Additionally, this report offers a comprehensive roundup of international and domestic news releases.

Sentiment Improves Despite Job Concerns: Consumer optimism increased in August, even as concerns about employment grew.

- Consumer sentiment reached a six-month high in August as households reported increased confidence in both business conditions and the overall economy. The Conference Board Consumer Confidence Index climbed from a revised 101.9 to 103.3, driven by gains in both the Expectations and Present Situation indexes. The Expectations Index, which remained above 80 for the second consecutive month, rose from 81.1 to 82.5, its highest level since August 2023. Meanwhile, the Present Situation Index improved from 133.1 to 134.4.
- Despite the broader market's positive tone, concerns persisted about the labor market. The report indicated a decline in respondents expressing optimism about job availability and an increase in those finding jobs more challenging to secure. This weaker outlook reflects a broader concern that firms are beginning to slow hiring as the economy shows signs of losing momentum. This sentiment aligns with the Federal Reserve's increased focus on its employment mandate. In July, the employment rate surged to its highest level since October 2021, while job openings showed signs of deceleration.

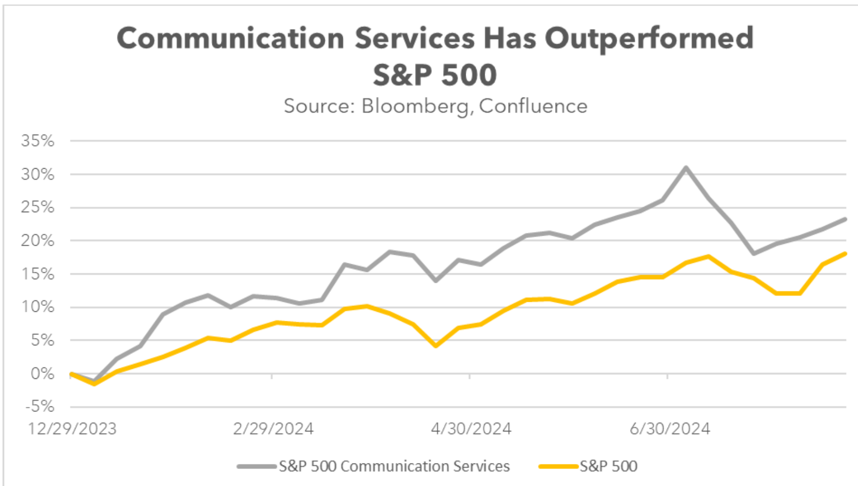


- The rise in consumer confidence is another indication that earlier-month recession fears may have been exaggerated. This bodes well for the equity market, bolstering the chances of a soft landing, especially given recent signals from numerous Fed officials favoring a September rate cut. However, it also suggests that a substantial rate cut may be less likely, given the economy's relative stability. Nevertheless, the upcoming jobs report will likely be pivotal in determining the size of the rate cut, as another surge could reinforce the notion that the Fed is behind the curve.

Social Media Takes the Stage: Social media companies and governments are increasingly at odds over the definition of free speech.

- In a letter to the House Judiciary Committee, Meta CEO Mark Zuckerberg accused the Biden administration of pressuring the company to limit content related to the COVID-19 pandemic. Zuckerberg argued that such restrictions were inconsistent with Meta's content standards and vowed to resist any future attempts to influence the platform’s policies. In response, the White House defended its actions, asserting that its requests for tech companies to curtail misinformation were aimed at protecting public health during the outbreak.

- His comments come amid a growing public outcry over the role of social media in disseminating divisive content. Earlier this month, Elon Musk, CEO of X (formerly Twitter), faced criticism from the UK government for suggesting that the country was on the brink of civil war. This shift coincides with the aging of the US social media audience, hindering the platforms' abilities to increase advertising revenue. Despite being perceived as a platform for younger users, Meta's median user age is between 30 and 39, with less than a quarter of its user base under 24.



- The ongoing debate about social media content has significant implications for the Communications sector. Many of these companies rely heavily on online advertising as a solid revenue source. Over the past few years, Meta and Alphabet have been major drivers of growth within the Communications sector. While these firms are likely to benefit from the upcoming election season, subsequent regulatory efforts could weigh on the overall sector as lawmakers seek to curtail the power of these tech giants.

Argentina: While he has had some victories, Argentine President Javier Milei is increasingly making more concessions as he looks to revive the economy.

- Since taking office, Milei and his administration have implemented a series of policy adjustments. On Tuesday, the Argentine government announced a reduction in tariffs aimed at combating inflation. Milei's decision to lower the import tax from 17.5% to 7.5% represents a reversal from his initial post-election increase. Additionally, he has softened his stance on China, shifting from campaign rhetoric that labeled Chinese party leaders as "assassins" to a recognition of the importance of Chinese investment and trade for Argentina's future.
- Milei's policy pivot comes amidst Argentina's struggle to achieve economic growth, despite implementing painful austerity measures. Since taking office, Milei has enacted significant cuts to real pensions and public sector wages, while freezing public

infrastructure projects. These measures have strengthened the government's financial position, resulting in five consecutive budget surpluses and a faster-than-expected deceleration in inflation. However, the economy entered a recession in the first quarter, with economic activity in all but one sector posting annual declines in June.

- Despite being early in his first term, the president has demonstrated the challenges faced by those perceived as extremists in attempting to deviate significantly from their predecessors' policies. While presidents play a crucial role in setting agendas, they often inherit situations that necessitate compromise. Therefore, it's essential to consider the broader political landscape when assessing the potential impact of a new leader on the market. That said, Argentina's long-term outlook is looking better since Milei has implemented some of his reforms.

In Other News: The US has affirmed its commitment to defend Israel if attacked by Iran, underscoring the ongoing threat of conflict in the region. In domestic politics, Democratic presidential candidate Kamala Harris and her running mate, Tim Walz, are scheduled for their first CNN interview, which aims to provide voters with deeper insights into their candidacies. Meanwhile, Mexican President Andrés Manuel López Obrador has suspended relations with the US and Canadian embassies in response to disagreements over his judicial reform plans.

US Economic Releases

The Mortgage Bankers Association today said ***mortgage applications*** in the week ended August 23 rose 0.5%, compared to last week's decline of 10.1%. Applications for home purchase mortgages rose 0.9%, while applications for refinancing mortgages fell 0.1%. According to the report, the average interest rate on a 30-year mortgage declined to 6.44%, compared to 6.5% the previous week. This is the lowest rate since April of 2023 and extends a lengthening trend of declines. Despite this, we have seen erratic movements in the pace of mortgage applications, due to persistent affordability challenges posed by high home prices. If the Fed begins to cut rates in the autumn, as increasingly expected, this could lead to further declines in mortgage interest rates and a more sustained uptrend in mortgage applications.

The table below lists the economic releases and Fed events scheduled for the rest of the day.

Economic Releases		
No economic releases for the rest of today		
Federal Reserve		
ET	**Speaker or Event**	**District or Position**
13:15	Christopher Waller Speaks on Payments in India	Member of the Board of Governors
18:00	Raphael Bostic Speaks on Economic Outlook	President of the Federal Reserve Bank of Atlanta

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								
Australia	CPI	y/y	Jul	3.5%	3.8%	3.4%	**	Equity and bond neutral
EUROPE								
Eurozone	M3 Money Supply	y/y	Jul	2.3%	2.3%	2.7%	***	Equity and bond neutral
Germany	GfK Consumer Confidence	m/m	Sep	-22.0	-18.6	-18.2	**	Equity bearish, bond bullish
France	Consumer Confidence	m/m	Aug	92	91	92	***	Equity and bond neutral
Italy	Industrial Sales WDA	y/y	Jun	-3.7%	-4.8%		*	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)	534	533	1	Down
3-mo T-bill yield (bps)	496	496	0	Down
U.S. Sibor/OIS spread (bps)	505	506	-1	Down
U.S. Libor/OIS spread (bps)	502	503	-1	Down
10-yr T-note (%)	3.81	3.82	-0.01	Flat
Euribor/OIS spread (bps)	352	352	0	Down
Currencies	**Direction**			
Dollar	Up			Down
Euro	Down			Up
Yen	Down			Up
Pound	Down			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.

	Price	Prior	Change	Explanation
Energy Markets				
Brent	$78.32	$79.55	-1.55%	
WTI	$74.22	$75.53	-1.73%	
Natural Gas	$1.89	$1.90	-1.00%	
12-mo strip crack	$19.44	$19.62	-0.92%	
Ethanol rack	$1.99	$1.99	0.36%	
Metals				
Gold	$2,502.91	$2,524.64	-0.86%	
Silver	$29.43	$29.98	-1.81%	
Copper contract	$422.80	$430.35	-1.75%	
Grains				
Corn contract	$390.75	$392.75	-0.51%	
Wheat contract	$535.50	$535.50	0.00%	
Soybeans contract	$979.00	$986.50	-0.76%	
Shipping				
Baltic Dry Freight	1,721	1,762	-41	
DOE Inventory Report				
	Actual	**Expected**	**Difference**	
Crude (mb)		-2.78		
Gasoline (mb)		-2.15		
Distillates (mb)		-0.82		
Refinery run rates (%)		0.1%		
Natural gas (bcf)		34		

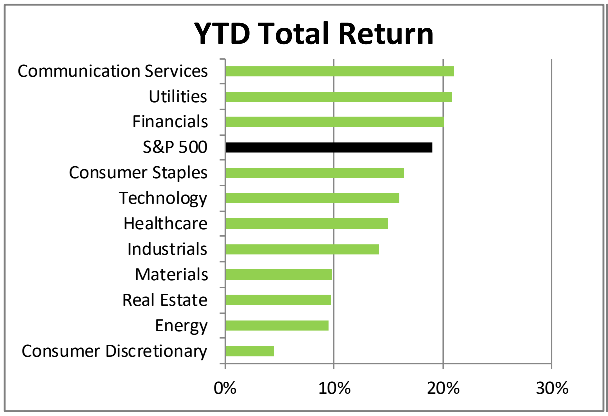
Weather

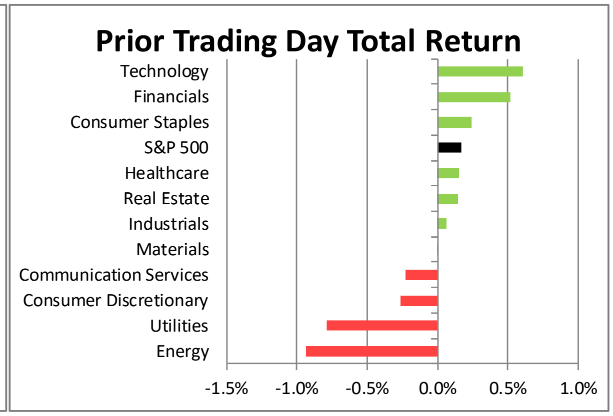
The 6-to-10-day and 8-to-14-day forecasts currently call for warmer-than-normal temperatures in the western third of the country, along the Gulf Coast, and in Florida, with cooler temperatures along the Atlantic Coast. The precipitation outlooks call for wetter-than-normal conditions in the Pacific Northwest and the Southeast, with drier than normal conditions in the Desert Southwest, northern Great Plains, the Great Lakes region, and New England.

A new tropical disturbance has formed a few hundred miles southeast of Bermuda. It has a 10% chance of developing into a cyclone and is tracking northeastward, away from the continental United States.

Data Section

US Equity Markets – (as of 8/27/2024 close)

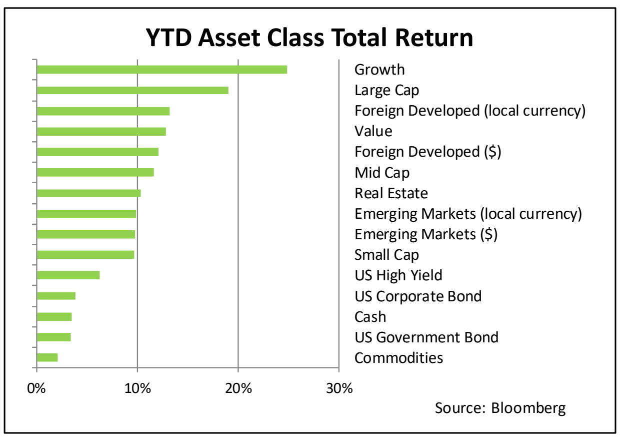




(Source: Bloomberg)

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 8/27/2024 close)

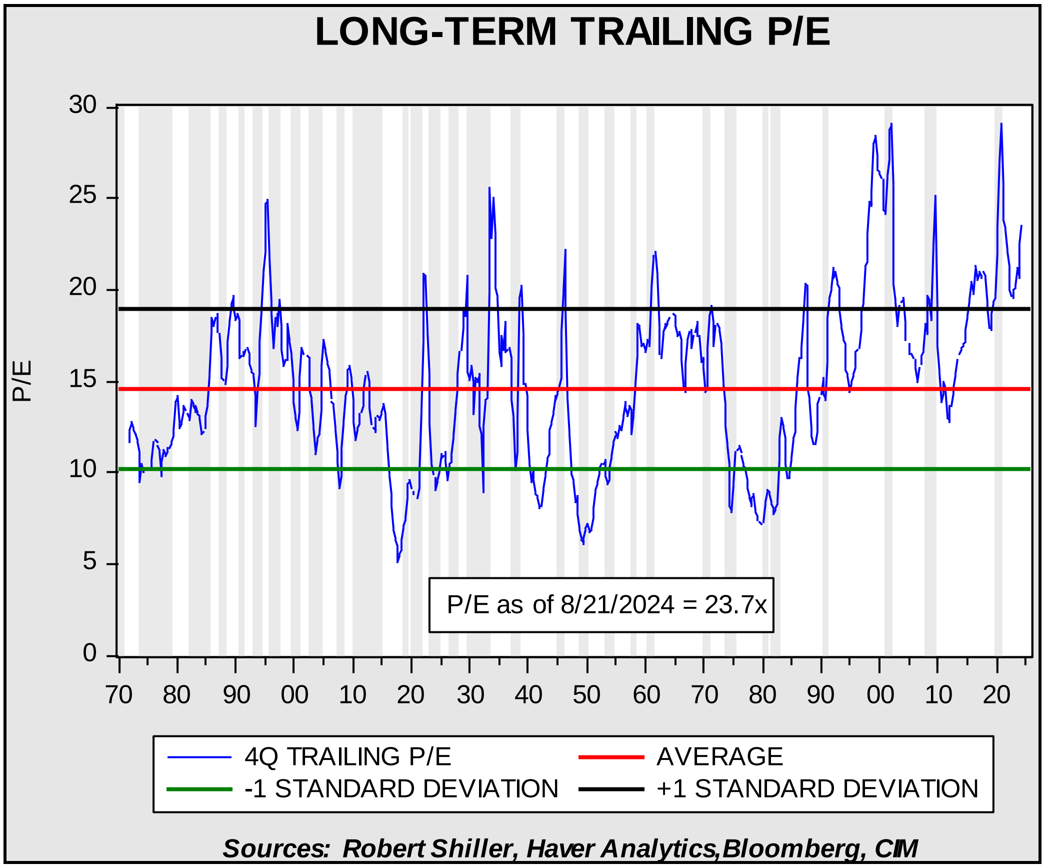


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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 22, 2024



Based on our methodology,[1] the current P/E is 23.7x, up 0.1 from our last report. The increase in the multiple was due to a slight pickup in the stock price index.

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 (Q2). 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.