

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 29, 2024 — 9:30 AM ET] Global equity markets are mixed this morning. In Europe, the Euro Stoxx 50 is up 0.9% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed down 0.3%. Chinese markets were mixed, with the Shanghai Composite down 0.5% from its previous close and the Shenzhen Composite up 1.1%. US equity index futures are signaling a higher open.

With 480 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, 80.8% have exceeded expectations, while 14.8% have fallen short of expectations.

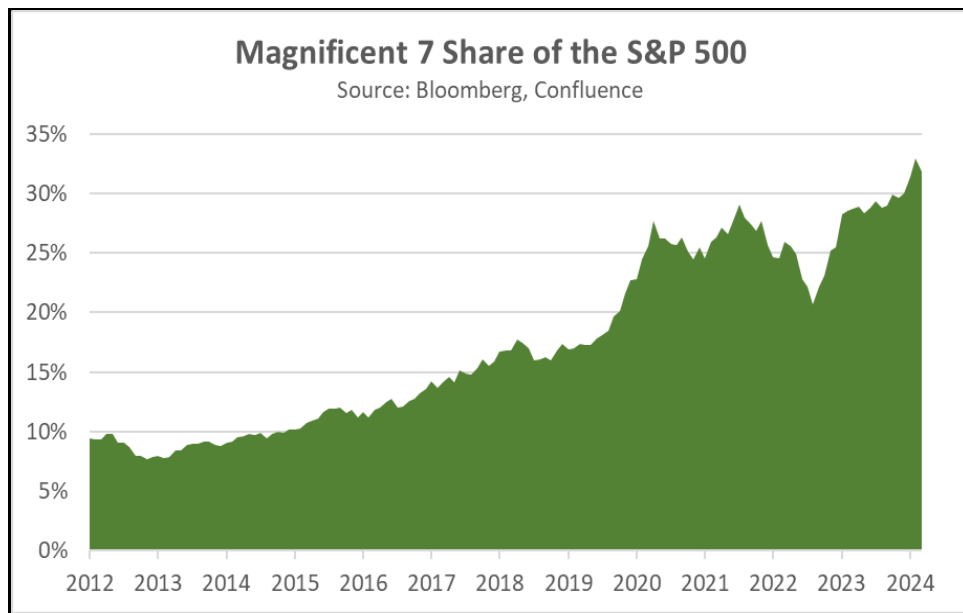
The Confluence macro team publishes a plethora of research reports and multimedia offerings on a weekly and quarterly basis, all available on our [website](#). We highlight recent publications below, with new items of the day emphasized in bold:

- **[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! The market is closely analyzing Nvidia's latest earnings report to assess its implications for the future. In sports news, the New York Giants honored rookie wide receiver Malik Nabers by unretiring the iconic No. 1 jersey. Today's *Comment* will explore the broader significance of Nvidia's earnings for the Magnificent 7, delve into why policymakers are having cold feet heading into the monetary easing cycle, and offer a discussion about the ongoing chip war between China and the West. As always, we'll conclude with a roundup of key international and domestic data releases.

AI Hype Fades: Nvidia's disappointing results will likely intensify pressure on AI-related companies to demonstrate profitability.

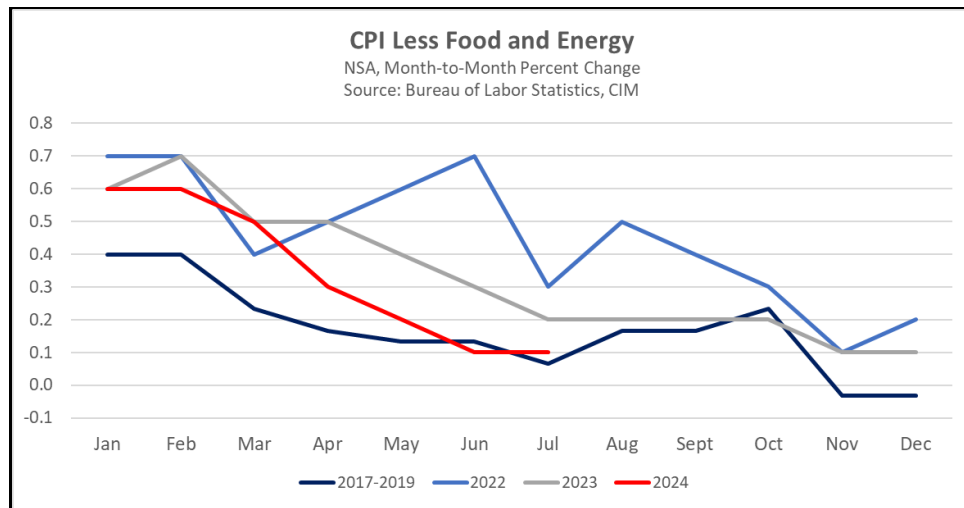
- Despite exceeding analyst expectations with second-quarter revenue of \$30 billion compared to the projected \$28.7 billion, [the US chipmaker's stock price declined](#). Investors sought a more substantial earnings beat and were disappointed by the company's subpar outlook. While the company has expressed confidence in its Blackwell processor, a next-generation AI chip, production delays due to design issues have raised concerns. Despite these challenges, the company expects revenue to increase to \$32.5 billion in the current quarter, surpassing analyst estimates of \$31.9 billion.
- Nvidia's underwhelming earnings could foreshadow broader challenges within the Magnificent 7. This cohort of tech giants has been a major catalyst for the S&P 500's gains this year, but recent signs suggest a potential slowdown. Investors are growing wary of tech companies' abilities to sustain their current valuations, especially given their significantly higher price-to-earnings ratios as compared to the broader large-cap market. These concerns have become more pronounced as companies like [Microsoft, Amazon, and Google have vowed to plow more money into AI](#), despite a lack of concrete results.



- Today's results could further fuel a shift in investor sentiment, driving a rotation toward new market leaders. While other sectors may benefit from this change, large cap stocks are unlikely to be completely overlooked. The emergence of a new market leader will hinge on the economic trajectory over the coming months. As signs of a potential slowdown emerge and the Federal Reserve prepares to ease monetary policy, interest rate-sensitive sectors like Financials and Real Estate may experience a resurgence. However, market volatility is expected to be elevated as investors cope with the uncertainty.

Not So Fast: While many Federal Reserve officials have struck a dovish tone, there are still some holdouts who aren't entirely convinced about the need for a rate cut in September.

- Atlanta Fed President Raphael Bostic on Wednesday [expressed skepticism about the need for an immediate interest rate cut](#) at the upcoming Federal Reserve meeting. During an interview, he noted that while inflation has exceeded his expectations and unemployment has risen more rapidly than anticipated, he still wants more conclusive data before fully supporting lowering rates in September. Over the next two weeks, the Federal Reserve will have two inflation reports for Personal Consumption Expenditure (PCE) and another for the Consumer Price Index (CPI) as well as another jobs report to analyze before its upcoming meeting.
- Bostic is not alone in expressing concerns that inflation may resurface if central banks become complacent. Bank of England Governor Andrew Bailey has tempered [expectations for another rate cut](#) at the central bank's next meeting, due to concerns of a reacceleration in inflation. Despite the recent decline in inflation data, the Bank of England anticipates a higher inflation rate at year's end. In South America, Brazil was one of the first major economies to implement rate cuts but [is now considering an interest rate hike](#) to address an unexpected resurgence in inflation.



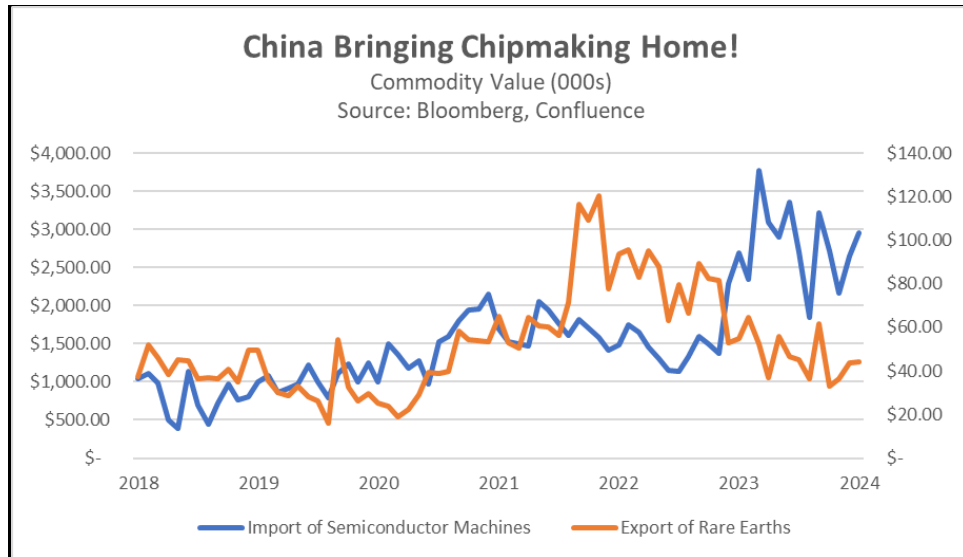
- The PCE is not anticipated to accelerate significantly as some of its components were showing signs of moderation in the Producer Price Index (PPI), but the August CPI report could introduce uncertainty to the Fed's aims for a rate cut. Historically, prices tend to rise during the fall months. This should not be a problem as long as the month-to-month figures remain relatively in line with last year's increase of 0.2%. If inflation rises about that amount, it could call into question the path of future interest rate cuts.

The Fight Over Chips: Western nations have shown no signs of backing down in the face of China's threats over export controls.

- The Netherlands delivered a major setback to China's semiconductor aspirations on Thursday by [denying ASML license renewals for servicing its advanced ultraviolet lithography equipment](#) within the country. This move effectively curtails China's access to the cutting-edge technology essential for developing domestic chip manufacturing capabilities. ASML's lithography machines are indispensable for producing high-

performance chips and China has no way of replacing them. The move comes as China prepares to limit export of key materials needed for chip production.

- The Netherlands' decision aligns with the US-led effort to impose unilateral restrictions on chip exports to China. [Japan and South Korea, while expressing reservations, have also complied with US requests](#) to limit exports that could bolster Beijing's ambitions of developing a domestic chip industry. Behind the scenes, US officials have employed the threat of invoking the Foreign Direct Product Rule against countries that fail to comply. This rule would enable the US to restrict the flow of exports containing even the smallest amount of US technology.



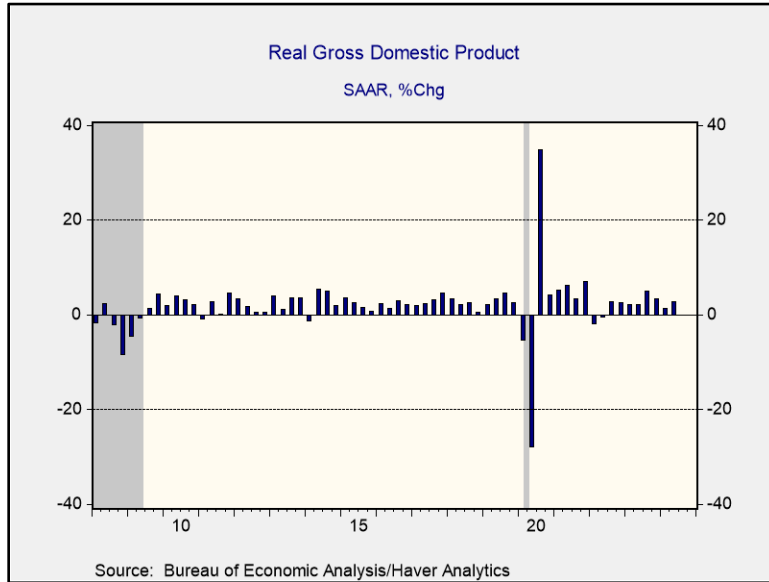
- Denying China access to chipmaking technology is unlikely to prevent the country from eventually developing its own industry. However, it does provide the West with a strategic advantage by incentivizing firms to invest more in the materials needed for chip production. This aligns with the West's broader goal of reducing reliance on Chinese commodities. The escalating competition between the West and China is likely to persist for the foreseeable future as both sides seek to establish dominance in the clean energy and chipmaking sectors as a means of asserting global influence.

In Other News: As anticipated, Brazilian President Lula da Silva [has selected his political ally Gabriel Galipolo](#) to lead the country's central bank. This choice is likely to temper expectations of a rate hike at the central bank's upcoming meeting in September. [Russia is finding it difficult to retake land captured by Ukraine](#) in a sign of growing uncertainty about the direction of war. The [California AI bill has garnered significant attention](#) as lawmakers seek to establish safeguards for the development of new AI technologies.

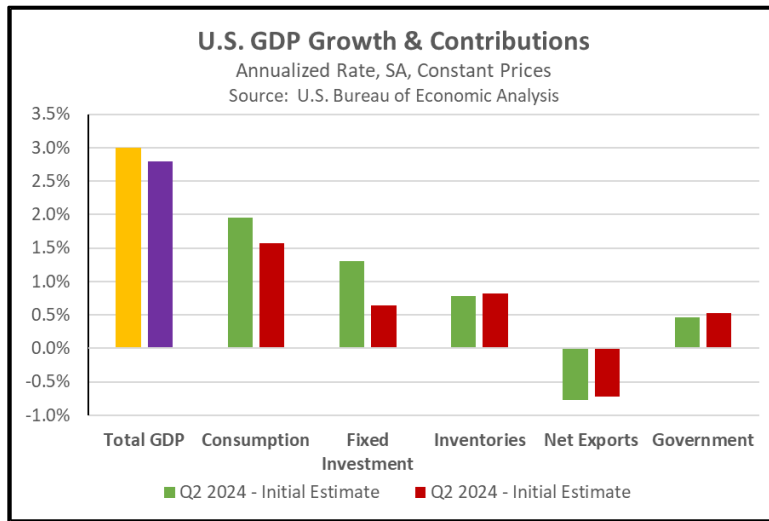
US Economic Releases

The Commerce Department released its second estimate of economic activity for Q2 2024. After stripping out seasonal factors and price changes, second-quarter **gross domestic product (GDP)**

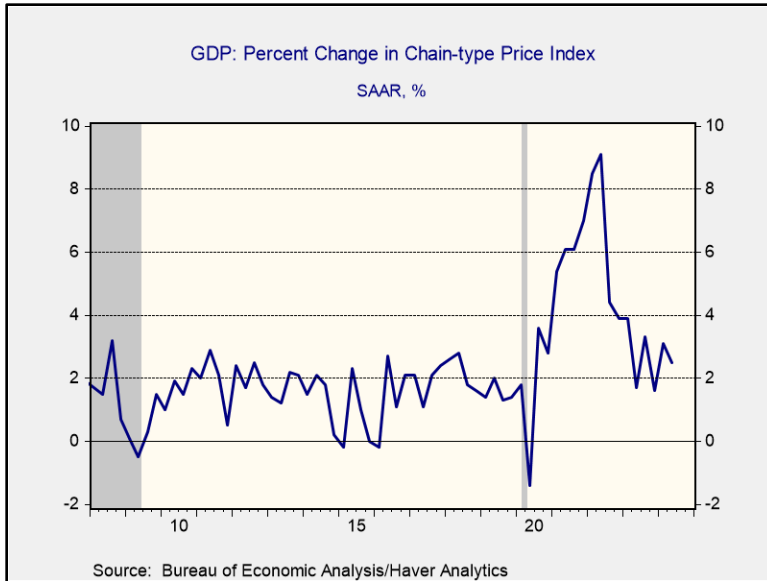
rose at an annualized rate of 3.0%, up from the previous estimate of 2.8%. The chart below shows the annualized growth rate of US GDP since just before the Global Financial Crisis.



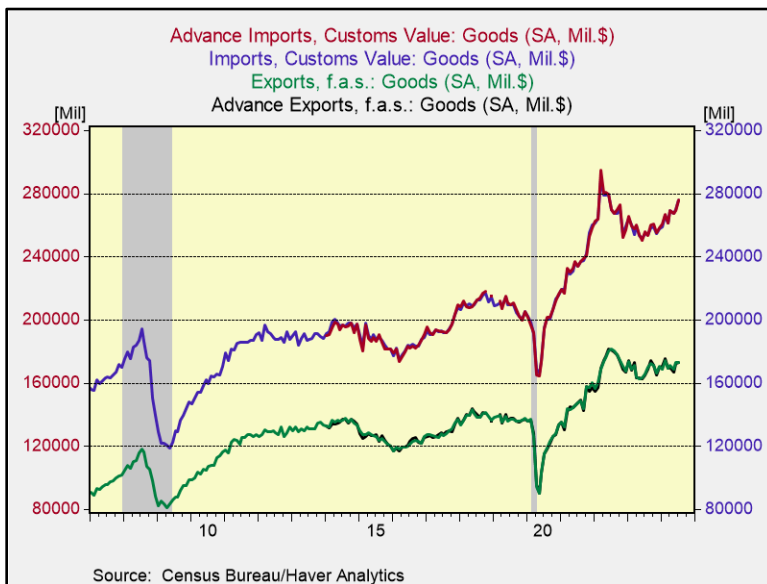
A closer look at the details in the report shows that consumer and investment spending was stronger than originally thought. The chart below shows the contributions to the annualized growth rate in the second quarter.



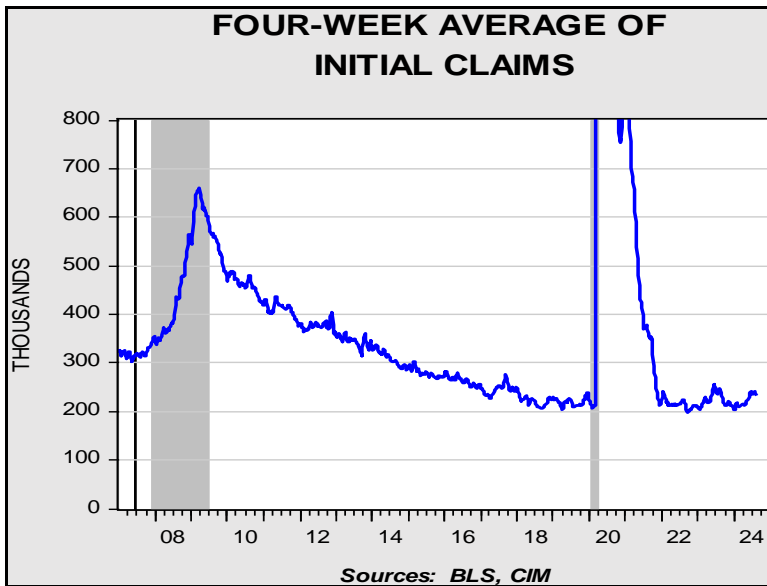
The GDP report also includes the broadest measure of US inflation, which was milder than originally thought. The GDP deflator was revised downward from 3.1% to 2.5%. The chart below shows the year-over-year change in the GDP Price Index over the last several decades.



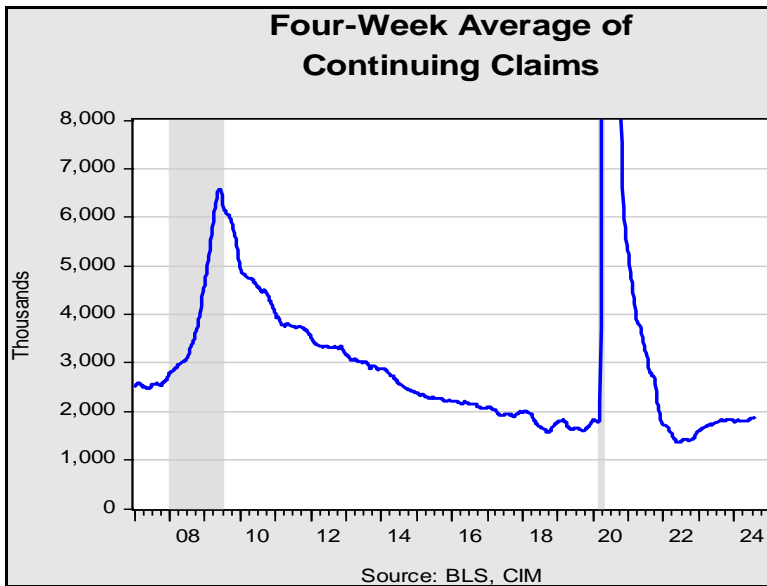
A preliminary estimate released this morning showed the US *merchandise trade balance* in July came in at a seasonally adjusted deficit of \$102.7 billion, versus an expected value of \$97.8 billion and a June value of \$96.6 billion. According to the data, total merchandise exports were essentially unchanged, while imports rose 2.3%. Compared with the same month, one year earlier, exports in July rose 4.9%, while imports rose 7.7%. The chart below shows the monthly value of US exports and imports since just before the Global Financial Crisis.



In the week ended August 24, *initial claims for unemployment benefits* fell to a seasonally adjusted 231,000, versus an expectation of 232,000 and the prior week's 233,000. The four-week moving average of initial claims, which helps smooth out some of the volatility in the series, fell to 231,500. The chart below shows how initial jobless claims have fluctuated since just before the Global Financial Crisis.



In the week ended August 17, the number of *continuing claims for unemployment benefits* (people continuing to draw benefits) rose to a seasonally adjusted 1.868 million, versus an expectation of 1.87 million and the prior week’s 1,855 million. The four-week moving average of continuing claims rose to 1.865 million. The chart below shows how continuing claims have fluctuated since the GFC.



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						
ET	Indicator			Expected	Prior	Rating
10:00	Pending Home Sales	m/m	Jul	0.2%	4.8%	**
10:00	Pending Home Sales NSA	y/y	Jul	-2.0%	-7.8%	*
Federal Reserve						
ET	Speaker or Event	District or Position				
15:30	Raphael Bostic Gives Intro to Fed, 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								
Japan	Japan Buying Foreign Stocks	w/w	23-Aug	¥898.8b	¥353.2b		*	Equity and bond neutral
	Japan Buying Foreign Bonds	w/w	23-Aug	¥1542.9b	¥1850.9b		*	Equity and bond neutral
	Foreign Buying Japan Stocks	w/w	23-Aug	-¥438.3b	-¥47.5b		*	Equity and bond neutral
	Foreign Buying Japan Bonds	w/w	23-Aug	¥859.4b	¥1536.4b		*	Equity and bond neutral
	Consumer Confidence Index	m/m	Aug	3670.0%	3670.0%	3700.0%	*	Equity and bond neutral
Australia	Private Capital Expenditure	q/q	2Q	-2.2%	1.9%	1.0%	**	Equity bearish, bond bullish
New Zealand	ANZ Activity Outlook	m/m	Aug	37.1	16.3		*	Equity and bond neutral
	ANZ Business Confidence	m/m	Aug	50.6	27.1		**	Equity and bond neutral
EUROPE								
Eurozone	EU27 New Car Registrations	y/y	Jul	0.2%	4.3%		***	Equity and bond neutral
	Consumer Confidence	m/m	Aug F	-13.5	-13.4		**	Equity and bond neutral
	Services Confidence	m/m	Aug	6.3	5.0	5.2	**	Equity bullish, bond bearish
	Industrial Confidence	m/m	Aug	-9.7	-10.4	-10.8	***	Equity bullish, bond bearish
	Economic Confidence	m/m	Aug	96.6	96.0	96.0	***	Equity and bond neutral
Germany	CPI	y/y	Aug P	1.9%	2.3%	2.1%	***	Equity and bond neutral
	CPI, EU Harmonized	y/y	Aug P	2.0%	2.6%	2.2%	**	Equity and bond neutral
Russia	Retail Sales	m/m	Jul	6.10%	6.30%	5.40%	***	Equity bullish, bond bearish
	Unemployment Rate	m/m	Jul	2.40%	2.40%	2.40%	***	Equity and bond neutral
	Industrial Production	y/y	Jul	3.3%	2.7%	2.8%	***	Equity and bond neutral
AMERICAS								
Brazil	FGV Inflation IGPM	y/y	Aug	4.26%	3.82%	4.43%	***	Equity and bond neutral
	Total Outstanding Loans	m/m	Jul	6046b	6035b		**	Equity and bond neutral
	Formal Job Creation	m/m	Jul	188021	205905	190000	**	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)	532	534	-2	Down
3-mo T-bill yield (bps)	495	496	-1	Down
U.S. Sibor/OIS spread (bps)	502	504	-2	Down
U.S. Libor/OIS spread (bps)	499	502	-3	Down
10-yr T-note (%)	3.83	3.84	-0.01	Down
Euribor/OIS spread (bps)	351	352	-1	Down
Currencies	Direction			
Dollar	Up			Down
Euro	Down			Up
Yen	Flat			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.

	Price	Prior	Change	Explanation
Energy Markets				
Brent	\$79.07	\$78.65	0.53%	
WTI	\$75.00	\$74.52	0.64%	
Natural Gas	\$2.07	\$2.10	-1.19%	
12-mo strip crack	\$19.20	\$19.23	-0.13%	
Ethanol rack	\$2.01	\$2.01	0.27%	
Metals				
Gold	\$2,519.96	\$2,504.61	0.61%	
Silver	\$29.48	\$29.13	1.23%	
Copper contract	\$420.75	\$421.80	-0.25%	
Grains				
Corn contract	\$391.75	\$390.75	0.26%	
Wheat contract	\$536.75	\$541.50	-0.88%	
Soybeans contract	\$988.50	\$977.00	1.18%	
Shipping				
Baltic Dry Freight	1,755	1,721	34	
DOE Inventory Report				
	Actual	Expected	Difference	
Crude (mb)	-0.85	-2.78	1.93	
Gasoline (mb)	-2.20	-2.15	-0.05	
Distillates (mb)	0.28	-0.82	1.09	
Refinery run rates (%)	1.0%	0.1%	0.9%	
Natural gas (bcf)		35		

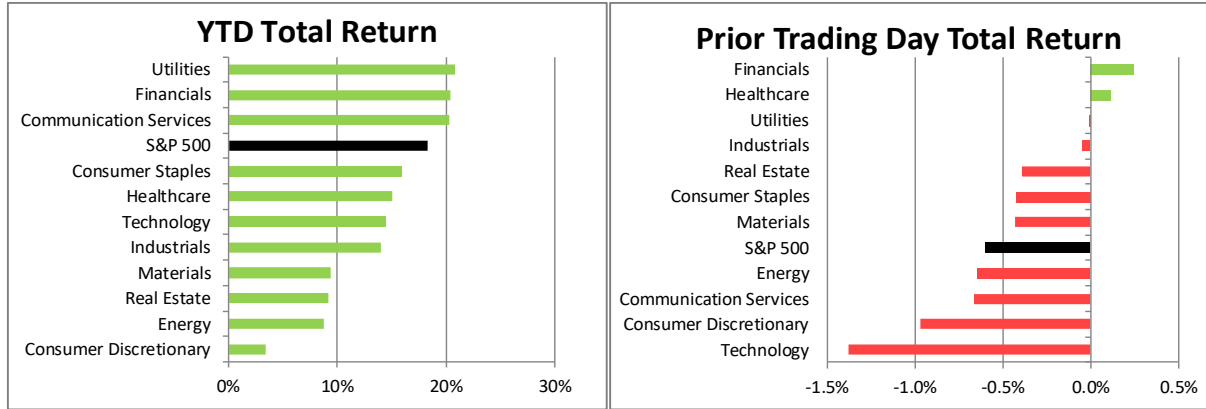
Weather

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

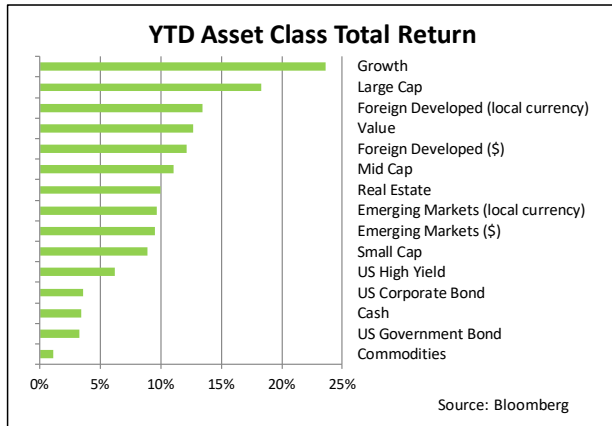
US Equity Markets – (as of 8/28/2024 close)



(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 8/28/2024 close)

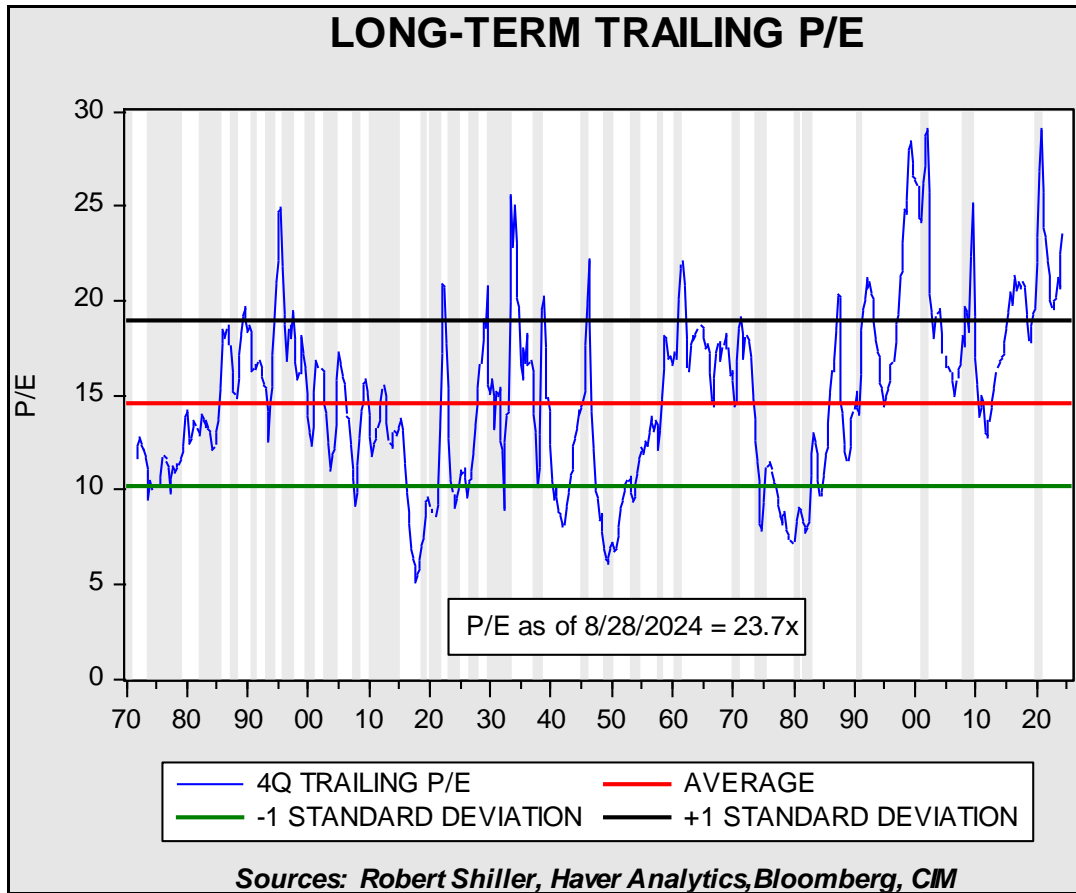


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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 29, 2024



Based on our methodology,¹ the current P/E is 23.7x, unchanged from our last report. The increase in stock price index was offset mostly by an increase 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.

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 (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.