Daily Comment

By Patrick Fearon-Hernandez, CFA, and Thomas Wash

[Posted: February 20, 2025 — 9:30 AM ET] Global equity markets are mixed this morning. In Europe, the Euro Stoxx 50 closed up 0.6% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed down 1.0%. Chinese markets were mixed, with the Shanghai Composite essentially unchanged from its previous close and the Shenzhen Composite up 0.6%. US equity index futures are signaling a lower open.

With 403 companies having reported so far, S&P 500 earnings for Q4 are running at $64.70 per share compared to estimates of $64.79, which is up 11.7% from Q4 2023. Of the companies that have reported thus far, 76.1% have exceeded expectations, while 17.4% 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 in bold:

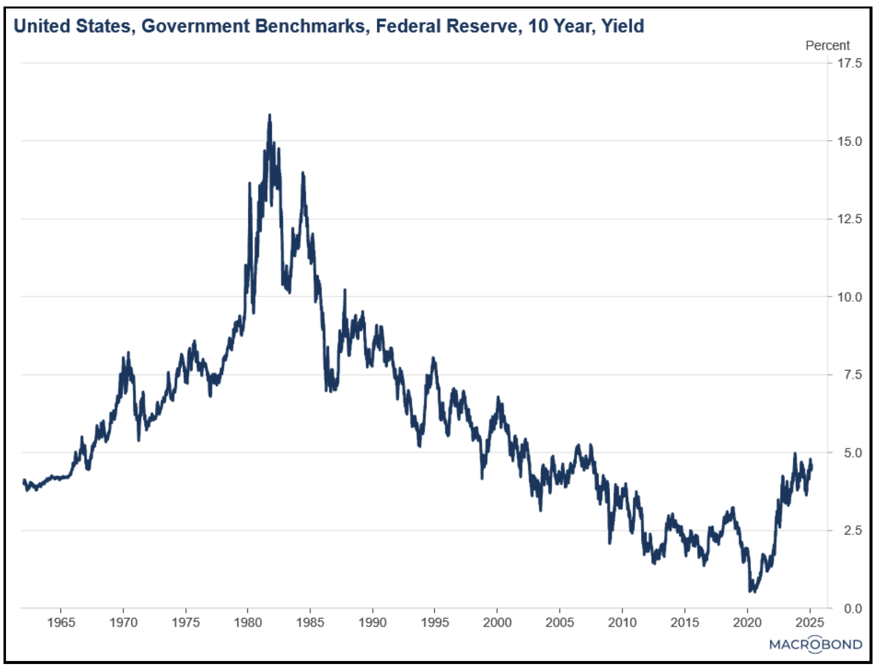
Bi-Weekly Geopolitical Report	Asset Allocation Bi-Weekly	Asset Allocation Quarterly	Of Note
"Middle Eastern Stock Markets: An Overview" (2/10/25) + podcast	"Our Take on the Initial Trump Tariffs" (2/18/25) + podcast	Q1 2025 Report Q1 2025 Rebalance Presentation	The Confluence of Ideas podcast Business Cycle Report

---

Good morning! The market is currently digesting the latest comments from President Trump regarding China. In sports news, reigning champions Real Madrid secured a dominant victory over Manchester City in the UEFA Champions League playoffs. Today's *Comment* will cover our insights on the recent FOMC meeting minutes, provide an update on the Republican effort to advance President Trump's agenda, and discuss other market-related developments. As usual, we will also summarize key international and domestic data releases.

Fed Cuts On Hold: The minutes from the January FOMC meeting revealed that Fed officials remain cautious about adjusting monetary policy. Their hesitation stems from concerns over the recent uptick in economic activity and uncertainties surrounding recent policy proposals. Additionally, officials started discussions about their plans for further quantitative tightening.

- In January, the committee unanimously voted to hold rates steady as it awaits clearer signs of progress on inflation. Fed officials highlighted concerns about upside risks to inflation, citing potential trade restrictions, a slowdown in immigration, and geopolitical tensions that could disrupt supply chains. Additionally, they noted that seasonal factors might further complicate the assessment of inflation trends.
- Their comments came ahead of the latest CPI report, which showed a stronger-than-expected acceleration in inflation for January. While factors such as auto and tenant insurance, along with egg prices, drove much of the increase — likely on a temporary basis — goods inflation moderated notably. This has raised concerns that progress on inflation may be stalling.
- Regarding the Fed's balance sheet, the central bank believes that reserves remain abundant but cautioned that the debt ceiling may be obscuring underlying issues. Consequently, there is concern that once the debt limit is lifted, reserves could decline more rapidly to levels deemed "appropriate." As a result, officials also discussed temporarily suspending the balance sheet runoff until the debt limit issue is resolved.



- The potential end of the balance sheet runoff is likely to provide a much-needed boost for US government bonds, as it is expected to increase demand. That said, a moderation in inflation and additional Fed rate cuts could also push long-term yields lower.

Trump Picks a Side: President Trump [has thrown his support behind the House Republican tax cut bill](), aiming to consolidate all his priorities into a single comprehensive piece of legislation, which he has famously described as "one big beautiful bill."

- The president's decision comes amid escalating tensions between Senate and House Republicans, who are struggling to align on a cohesive strategy to advance the Trump administration's agenda. The primary divergence lies in their approaches. The Senate bill seeks an early victory by prioritizing immigration reform and raising the debt ceiling, thereby creating breathing room to deliver on tax reform. In contrast, the House bill adopts a more comprehensive approach, aiming to tackle all pressing issues simultaneously.

- The differing approaches stem from concerns that the House bill may lack the necessary support to pass through Congress. While it includes tax cuts, it also proposes reductions to certain social spending programs, which are likely to face significant pushback from moderate lawmakers. Moreover, such opposition could delay lawmakers' ability to meet the March 14 government funding deadline, potentially exacerbating market uncertainty.
- So, while the president has indicated a preference for the House bill, he has also expressed willingness to support the Senate bill to ensure the legislation moves forward. Furthermore, the White House has shown openness to reducing defense spending as another avenue for achieving savings. We remain optimistic that a new tax bill will be passed this year, which would be highly bullish for US equities.

China Deal Possible? President Trump believes he can still secure a trade deal with China, despite rising tensions. His comments come just a few weeks before tariffs on Mexico and Canada, which the administration plans to impose, are set to take effect on March 4.

- Trump imposed a 10% additional tariff on imports from China shortly after taking office in January, citing concerns that China was not doing enough to curb the flow of fentanyl into the US and to address its unfair trade practices. While his decision was widely expected, the tariff rate was significantly lower than the 100% tariffs he had promised during his campaign, suggesting a potential moderation in his stance.
- That said, his true intentions remain unclear. The president may be using China as a signal to other countries that he is open to negotiating deals. Notably, his comments come just a day after he pledged to impose 25% tariffs on autos, pharmaceuticals, and semiconductors.
- So far this year, the dollar has weakened significantly amid signs that the president is less willing to pursue aggressive tariff measures than many had feared before he took office. This trend could continue if he steps back from other trade-related threats.

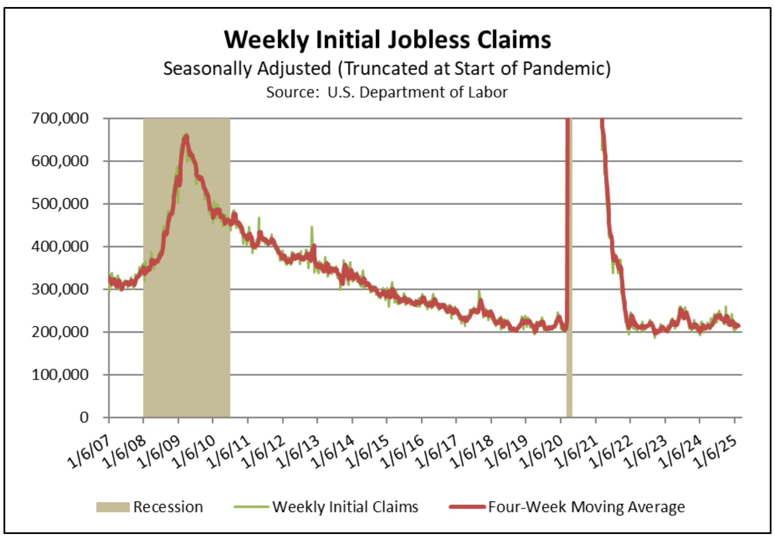
Canadian Elections: The Conservative Party's once-insurmountable lead has narrowed significantly in recent weeks, raising doubts about its ability to form a strong coalition in the upcoming election.

- Recent polling reveals a decline in voter trust in the US, likely influenced by trade disputes and jokes about the country's potential statehood. Voters express greater confidence in the Liberal party's ability to advocate for them in dealings with the US.
- Additionally, Prime Minister Justin Trudeau's decision to step down has contributed to the party's surge in support, as he had become deeply unpopular with the public. His departure has been a central theme in the Conservative Party's messaging, particularly due to his support for a carbon tax.

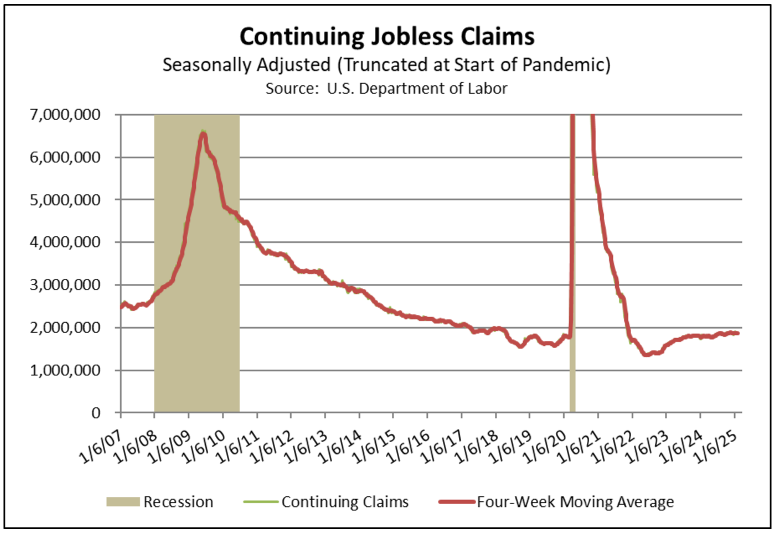
- The latest polls show that the Conservative Party's advantage has narrowed significantly, dropping from an 18% lead over its Liberal rivals to just 7%. The survey indicates that the Conservatives now hold 39% of public support, compared to 32% for the Liberals.
- The rise of the Liberal party could compel the Conservatives to adopt a more confrontational trade policy toward the US to win sufficient parliamentary support. Such a strategy increases the risk of escalating trade tensions between the two nations.

US Economic Releases

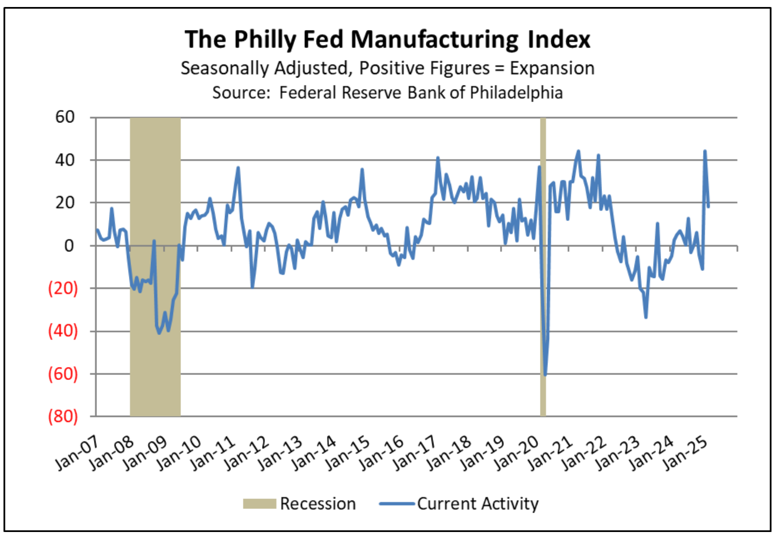
In the week ended February 15, ***initial claims for unemployment benefits*** rose to a seasonally adjusted 219,000, above both the expected level of 215,000 and the previous week's revised level of 214,000. However, despite the rise last week, the four-week moving average of initial claims, which helps smooth out some of the volatility in the series, fell to a low of 215,250, suggesting the demand for labor remains strong and firms are still reluctant to lay off workers. The chart below shows how initial jobless claims have fluctuated since just before the Great Financial Crisis. The chart is truncated through much of the pandemic period because of the extremely high level of claims at that time.



In the week ended February 8, the number of ***continuing claims for unemployment benefits*** (people continuing to draw benefits) rose to a seasonally adjusted 1.869 million, above both the anticipated reading of 1.868 million and the prior week's revised reading of 1.845 million. The four-week moving average of continuing claims fell to 1,862,500, but it remains higher than it was before the coronavirus pandemic. That suggests that the unlucky few workers who are laid off these days are finding it harder to land new positions and are stuck on unemployment for some time. The chart below shows how continuing claims have fluctuated since the GFC. It is also truncated during the pandemic period because of the high level of claims at the time.



Separately, the Philadelphia FRB said its February ***Philly Fed Index*** fell to a seasonally adjusted 18.1, beating the expected reading of 14.3 but still down sharply from the January reading of 44.3. The index, officially called the Philadelphia FRB Manufacturing Activity Index, is designed so that positive readings point to expanding factory activity in the mid-Atlantic region. At its current level, the index suggests mid-Atlantic manufacturing is growing again, but with lots of volatility. The chart below shows how the index has fluctuated since just before the GFC.



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

Economic Releases						
EST	Indicator			Expected	Prior	Rating
10:00	Leading Index	m/m	Jan	-0.1%	-0.1%	***

Federal Reserve		
EST	Speaker or Event	District or Position
9:35	Austan Goolsbee Speaks in Moderated Q&A	President of the Federal Reserve Bank of Chicago
12:05	Alberto Musalem Speaks to Economic Club of NY	President of the Federal Reserve Bank of St. Louis
14:30	Michael Barr Speaks on Supervision and Regulation	U.S. Federal Reserve Vice Chairman for Supervision
17:00	Adriana Kugler Speaks on Inflation, Phillips Curve	Member of the Board of Governors

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 Bonds	w/w	14-Feb	¥241.0b	¥1755.6bb		*	Equity and bond neutral
	Japan Buying Foreign Stocks	w/w	14-Feb	¥345.4b	-¥1267.4b		*	Equity and bond neutral
	Foreign Buying Japan Bonds	w/w	14-Feb	¥78838b	-¥187.8b		*	Equity and bond neutral
	Foreign Buying Japan Stocks	w/w	14-Feb	-¥352.8b	-¥384.4b		*	Equity and bond neutral
Australia	Employment Change	m/m	Jan	44.0k	60.0k	20.0k	***	Equity and bond neutral
	Unemployment Rate	m/m	Jan	4.1%	4.0%	4.1%	***	Equity and bond neutral
	Participation Rate	m/m	Jan	67.3%	67.2%	67.1%	**	Equity and bond neutral
South Korea	PPI	y/y	Jan	1.7%	1.7%		**	Equity and bond neutral
	Consumer Confidence	m/m	Feb	95.2	91.2		*	Equity and bond neutral
EUROPE								
Eurozone	Construction output	y/y	Dec	-0.1%	0.3%		*	Equity and bond neutral
Germany	PPI	y/y	Jan	0.5%	0.8%	1.2%	**	Equity bullish, bond bearish
France	Retail Sales SA	y/y	Jan	-0.7%	-0.8%		*	Equity and bond neutral
Italy	Current Account Balance	m/m	Dec	4228m	-493m		*	Equity and bond neutral
Switzerland	Real Exports	m/m	Jan	-3.9%	5.4%		*	Equity and bond neutral
	Real Imports	m/m	Jan	-1.9%	4.7%		*	Equity and bond neutral
Russia	PPI	y/y	Jan	9.7%	7.9%		***	Equity and bond neutral
Russia	Gold and Forex Reserves	m/m	14-Feb	$628.5b	$626.9b		***	Equity and bond neutral
AMERICAS								
Mexico	Retail Sales	y/y	Dec	-0.2%	-1.9%	-1.5%	***	Equity bullish, bond bearish

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 T-bill yield (bps)	421	422	-1	Down
U.S. Sibor/OIS spread (bps)	432	433	-1	Down
U.S. Libor/OIS spread (bps)	434	434	0	Down
10-yr T-note (%)	4.51	4.53	-0.02	Down
Euribor/OIS spread (bps)	253	252	1	Down
Currencies	**3 Mo**			
Dollar	Up	US		Up
Euro	Down	Euro		Down
Yen	Up	Japan		Up
Pound	Down	UK		Down
Franc	Down	Switzerland		Down
Central Bank Action	**Bank section (otherwise, I have**		**Expected**	
PBOC 1-Year Loan Prime Rate	3.10%	3.10%	3.10%	On Forecast
PBOC 5-Year Loan Prime Rate	3.60%	3.60%	3.60%	On Forecast

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.

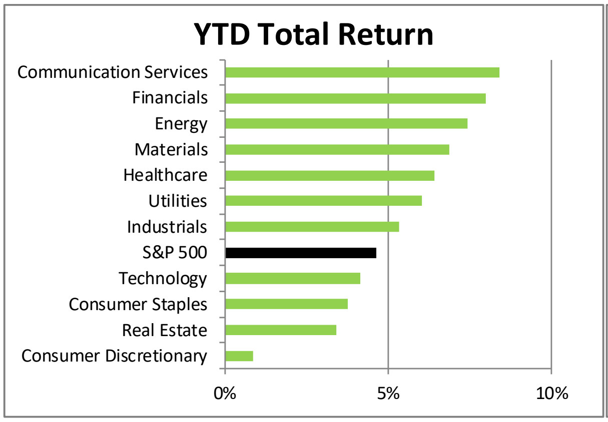
	Price	**Prior**	**Change**	**Explanation**
Energy Markets				
Brent	$76.34	$76.04	0.39%	
WTI	$72.29	$72.25	0.06%	
Natural Gas	$4.19	$4.28	-2.15%	
Crack Spread	$21.02	$20.71	1.51%	
12-mo strip crack	$22.27	$22.17	0.43%	
Ethanol rack	$1.92	$1.92	-0.13%	
Metals				
Gold	$2,942.87	$2,933.39	0.32%	
Silver	$33.08	$32.70	1.18%	
Copper contract	$466.10	$461.40	1.02%	
Grains				
Corn contract	$517.50	$512.25	1.02%	
Wheat contract	$608.75	$606.50	0.37%	
Soybeans contract	$1,055.50	$1,048.25	0.69%	
Shipping				
Baltic Dry Freight	904	841	63	
DOE Inventory Report				
	Actual	**Expected**	**Difference**	
Crude (mb)		3.00		
Gasoline (mb)		-1.00		
Distillates (mb)		-1.50		
Refinery run rates (%)		-0.6%		
Natural gas (bcf)		-193		

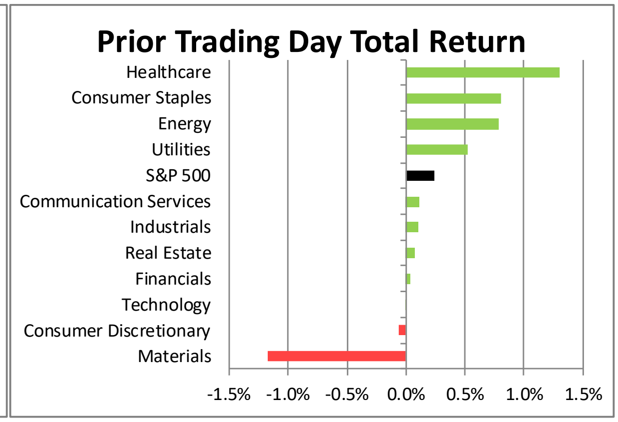
Weather

The 6-to-10-day and 8-to-14-day forecasts currently call for cooler-than-normal temperatures only in Florida, with warmer-than-normal temperatures from the West Coast to the Great Plains. The forecasts call for wetter-than-normal conditions in the Dakotas and the Northeast, with dry conditions in the Far West.

Data Section

US Equity Markets – (as of 2/19/2025 close)

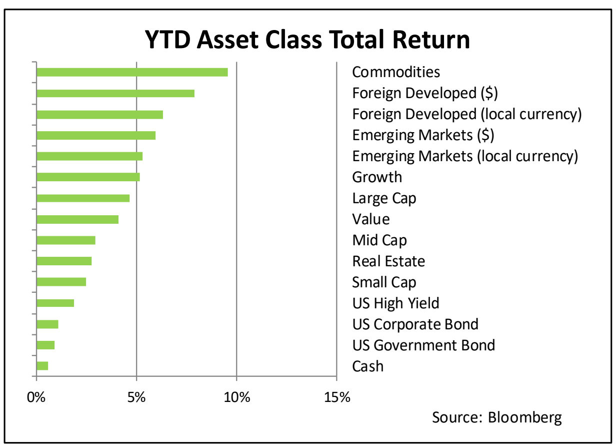




(Source: Bloomberg)

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 2/19/2025 close)

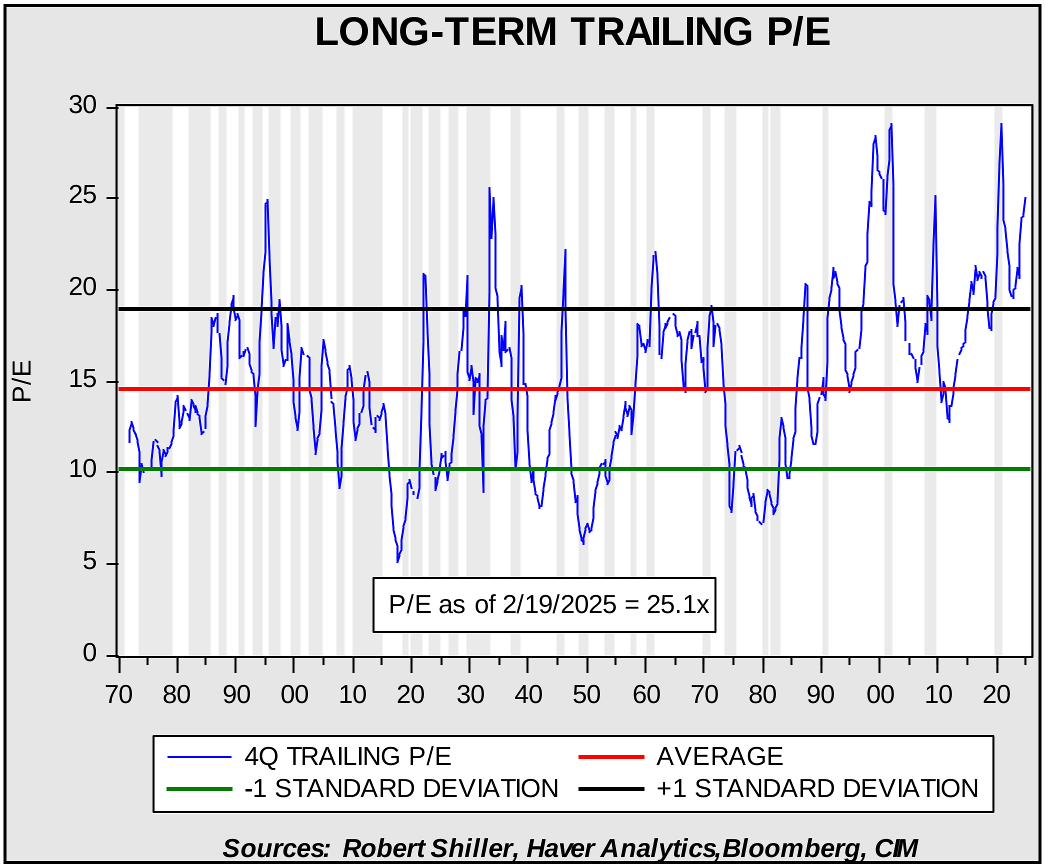


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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

February 20, 2025



Based on our methodology,[1] the current P/E is 25.1x, unchanged from our last report. The increase in the stock price index was offset by a rise 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 (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.