Daily Comment

By Patrick Fearon-Hernandez, CFA, and Thomas Wash

[Posted: January 13, 2025 — 9:30 AM ET] Global equity markets are lower this morning. In Europe, the Euro Stoxx 50 closed down 0.6% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed down 1.8%. Chinese markets were mixed, with the Shanghai Composite down 0.3% from its previous close and the Shenzhen Composite up 0.1%. US equity index futures are signaling a lower open.

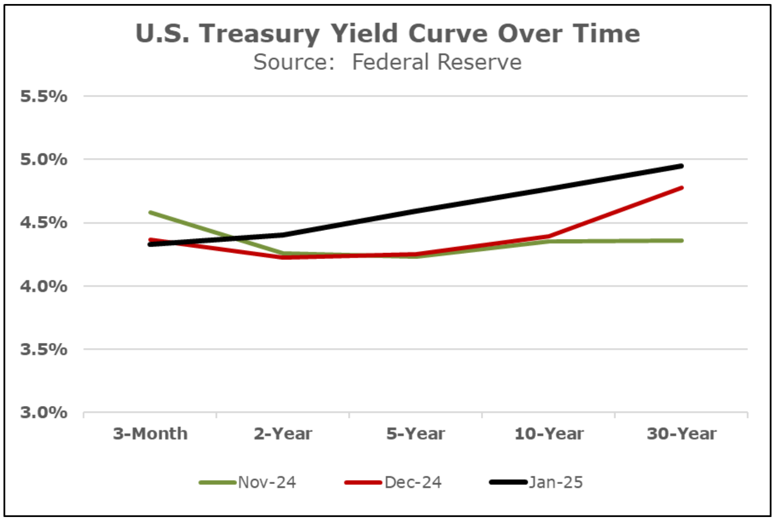
The Confluence macro team publishes a plethora of research reports and multimedia offerings on a weekly and quarterly basis, all available on our website. We highlight recent publications below with new items of the day in bold:

Bi-Weekly Geopolitical Report	Asset Allocation Bi-Weekly	Asset Allocation Quarterly	Of Note
The 2025 Geopolitical Outlook (12/16/24) + podcast	*Household Cash Levels and the S&P 500* (12/9/24) + podcast	Q4 2024 Report Q4 2024 Rebalance Presentation	*The 2025 Outlook: A Year of Political and Policy Change*

Our *Comment* today opens with a few words on the global bond sell-off, which so far this morning is still pushing yields higher. We next review several other international and US developments with the potential to affect the financial markets, including more signs that China is struggling with excess capacity in its industrial sector and new projections pointing to a boom in the construction of natural gas-fired energy plants in the US.

Global Financial Markets: Global bond yields continue to rise this morning, driven largely by outsized US economic growth and concerns about rising fiscal deficits. As we noted in our *Comment* on Friday, the strong December employment report has sparked speculation that the Federal Reserve may stop cutting interest rates. As a result, the US Treasury yield curve is decidedly upward sloping again, reflecting the current "bear steepening."

- The prospect for continued fast economic growth and high interest rates in the US is also boosting the value of the dollar and punishing foreign currencies.
- For example, the euro so far today is trading down approximately 0.5% to $1.0202, while the British pound has plummeted 0.7% to $1.2121.



Global Uranium Market: The price for enriched uranium has hit a record $190 per separative work unit (the standard way to value the effort required to separate uranium into its various isotopes). That marks an enormous jump from $56 three years ago, mostly reflecting global plans to increase the use of nuclear power and looming Western sanctions against Russia, the main refiner of uranium.

- Enriched uranium is typically sold to nuclear generating firms under long-term contracts, so its value can diverge from spot prices for mined uranium. Indeed, while anticipated demand growth and looming sanctions drove up enriched uranium prices in 2024, spot prices were in a correction and fell some 28%.
- Importantly, the continuing rise in enriched uranium prices holds the prospect for a rebound in spot uranium prices. We continue to believe that spot uranium could offer solid investment returns in the coming years.

Eurozone: Philip Lane, chief economist at the European Central Bank, said in an interview that his institution should work to find a "middle path" to cutting interest rates further. According to Lane, the ECB policymakers need to find a rate-cutting path that would still push down price inflation but also support economic growth. Since Lane's statement points to continued eurozone rate cuts, while investors now think US rates may be on hold, the news may be contributing to the euro's weakness so far today.

Germany: Laying out the platform of the far-right Alternative for Germany (AfD) in next month's election, party co-leader and chancellor candidate Alice Weidel stressed that an AfD government would push for the mass repatriation of immigrants. Specifically, Weidel used the controversial, expansive term "remigration," which far-right politicians in Germany define as forcibly removing immigrants who either break the law or "refuse to integrate," regardless of their citizenship status.

- Public opinion polls currently show AfD garnering about 20% of the February vote, second only to the center-right Christian Democratic Union, at about 32%. Nevertheless, AfD's prospects for joining a government are in question, as Germany's mainstream parties are all reluctant to strike a coalition deal with it.

- Nevertheless, the large chunk of the electorate that supports AfD illustrates the extent to which anti-immigration sentiment has risen in Europe. That suggests that European migration policy will continue to tighten going forward, despite the region's falling birth rate and demographic challenges.

China: The China Photovoltaic Industry Association has complained that its new cartel aimed at curbing excess production and boosting prices is already being undermined by a Xinjiang solar energy project. In its search for solar panel suppliers, the project reportedly set a bidding limit far below the cartel's price floor of 0.68 yuan ($0.09) per watt and awarded contracts to the firms with the lowest prices. The incident suggests that the Chinese solar panel industry will continue to struggle with excess capacity, falling prices, and vanishing profits.

- Along with electric vehicles, the solar energy industry is one of the best examples of how China's industrial policies have created massive problems with excess capacity, high debt, and budding financial problems.
- Since China's solar energy industry is mostly made up of relatively smaller private firms, it is proving hard to discipline. The government in 2024 issued new regulations to limit the investment in new capacity, but even the existing capacity is far more than enough to supply global demand.
- It now appears that the industry's effort to build a self-regulating cartel also won't stabilize prices or boost profitability. As producers export their excess production at fire sale prices in a desperate effort to survive, one result will likely be continued economic tensions between China and its trade partners.

Malaysia: In a *Financial Times* interview, Economy Minister Rafizi Ramli said Chinese technology companies are quickly ramping up their investments in Malaysia to get around the new US import tariffs that the incoming Trump administration is expected to impose against China. The government expects Chinese firms to invest billions of dollars in new production facilities in Malaysia in the coming years, giving a boost to economic growth.

United States-China: The outgoing Biden administration today unveiled new, expansive export controls on advanced computer chips for artificial intelligence. The rules aim to make it harder for China and other potential adversaries to acquire the chips, which can be used for both civilian and military purposes. Under the rules, 20 close US allies and partners will have uninhibited access to advanced AI-related chips with US technology, but most other countries will require licenses.

- The new rules tighten the Biden administration's previous efforts to crimp Chinese access to advanced AI chips. The previous efforts have in some cases been undermined by loopholes and workarounds.

- At least temporarily, the new rules are likely to rile Beijing and the countries that will now be subject to US licensing requirements. However, it isn't clear that the incoming Trump administration would maintain the rules. Given the strong influence that tech titans have in Trump's circle, it would not be a surprise if they work to water down or reverse the Biden rules in order to preserve US tech firms' access to the Chinese market.

US Energy Industry: Energy consultancy Enverus has issued a report saying the new data centers being built for the AI industry will spur the construction of some 80 new natural gas-fired energy plants in the US by 2030. The report builds on other analysis projecting the new data centers and their enormous energy requirements will also spur more nuclear power generation. However, gas-fired plants are cheaper and quicker to build, so it's reasonable to expect they will satisfy much of the new electricity demand and potentially help drive gas prices higher.

US Insurance Industry: California Governor Gavin Newsom yesterday said the multiple wildfires that have destroyed some 40,000 acres of Los Angeles could be the costliest disaster in US history. AccuWeather estimates the total economic loss from the fires will be $135 billion to $150 billion, and early estimates suggest insured losses will be upward of $20 billion. Because of the high insured losses, property insurers are expected to suffer big losses and pull back from the California market, driving many property owners to the state's backstop plan.

US Economic Releases

There were no economic releases prior to the publication of this report. The table below lists the economic releases and Fed events scheduled for the rest of the day.

Economic Releases						
ET	Indicator			Expected	Prior	Rating
14:00	Federal Budget Balance	m/m	Dec	-$73.8b	-$366.8b	**
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
ASIA-PACIFIC								
Australia	Melbourne Institute Inflation	y/y	Dec	2.6%	2.9%		***	Equity and bond neutral
New Zealand	Building Permits	m/m	Nov	5.3%	-5.2%		**	Equity and bond neutral
China	Exports	y/y	Dec	10.7%	6.7%	7.5%	**	Equity bullish, bond bearish
	Imports	y/y	Dec	1.0%	-3.9%	-1.0%	**	Equity bullish, bond bearish
	Trade Balance	m/m	Dec	104.84	$97.44b	$100.00b	***	Equity bullish, bond bearish
India	CPI	y/y	Dec	5.2%	5.48%	5.30%	***	Equity and bond neutral
EUROPE								
Germany	Current Account Balance	m/m	Nov	12.1b	13.7b		**	Equity and bond neutral
France	Industrial Production	y/y	Nov	-1.1%	-0.9%	-1.3%	***	Equity and bond neutral
	Manufacturing Production	y/y	Nov	-1.5%	-1.7%		**	Equity and bond neutral
Switzerland	Domestic Sight Deposits CHF	w/w	10-Jan	437.1b	426.6b		*	Equity and bond neutral
	Total Sight Deposits CHF	w/w	10-Jan	445.1b	439.6b		*	Equity and bond neutral
Russia	Money Supply, Narrow Definition	w/w	27-Dec	18.95t	18.71t		*	Equity and bond neutral
AMERICAS								
Canada	Building Permits	m/m	Nov	-5.9%	-4.1%	1.40	**	Equity bearish, bond bullish
	Net Change in Employment	m/m	Dec	90.9k	50.5k	25.0k	***	Equity and bond neutral
	Unemployment Rate	m/m	Dec	6.7%	6.8%	6.9%	***	Equity and bond neutral
	Participation Rate	m/m	Dec	65.1%	65.1%		*	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)	485	485	0	Down
3-mo T-bill yield (bps)	422	422	0	Down
U.S. Sibor/OIS spread (bps)	431	430	1	Down
U.S. Libor/OIS spread (bps)	433	433	0	Down
10-yr T-note (%)	4.76	4.76	0.00	Up
Euribor/OIS spread (bps)	277	279	-2	Down
Currencies	**Direction**			
Dollar	Up	US		Down
Euro	Down	Euro		Up
Yen	Down	Japan		Up
Pound	Down	UK		Up
Franc	Down	Switzerland		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.

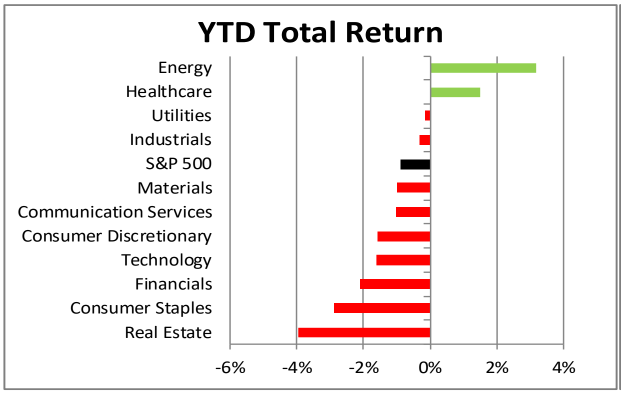
	Price	Prior	Change	Explanation
Energy Markets				
Brent	$81.26	$79.76	1.88%	
WTI	$78.28	$76.57	2.23%	
Natural Gas	$4.11	$3.99	2.98%	
Crack Spread	$16.29	$16.47	-1.10%	
12-mo strip crack	$20.87	$20.64	1.11%	
Ethanol rack	$1.76	$1.75	0.48%	
Metals				
Gold	$2,671.98	$2,689.76	-0.66%	
Silver	$29.77	$30.41	-2.09%	
Copper contract	$430.60	$430.40	0.05%	
Grains				
Corn contract	$474.75	$470.50	0.90%	
Wheat contract	$539.00	$530.75	1.55%	
Soybeans contract	$1,035.50	$1,025.25	1.00%	
Shipping				
Baltic Dry Freight	1,048	969	79	

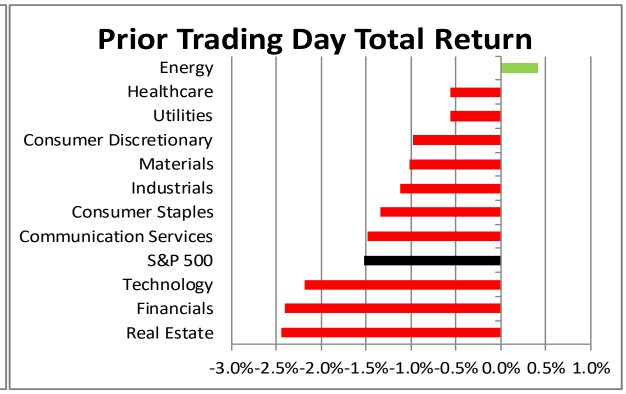
Weather

The 6-to-10-day and 8-to-14-day forecasts currently call for cooler-than-normal temperatures for most of the country. The precipitation outlook calls for wetter-than-normal conditions in the Rocky Mountain region and the East Coast, with dry conditions expected on the West Coast and the northern Midwest region.

Data Section

US Equity Markets – (as of 1/10/2025 close)

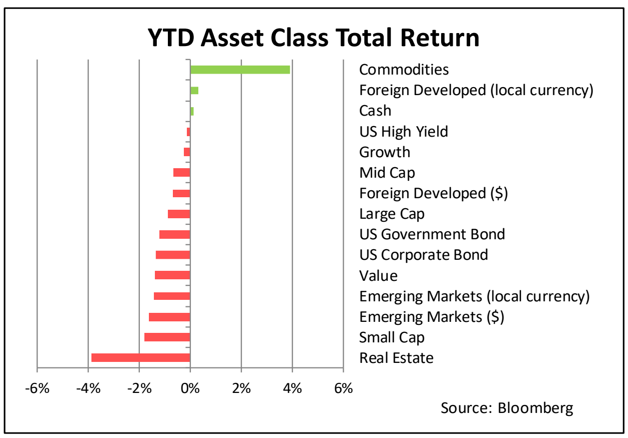




(Source: Bloomberg)

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 1/10/2025 close)

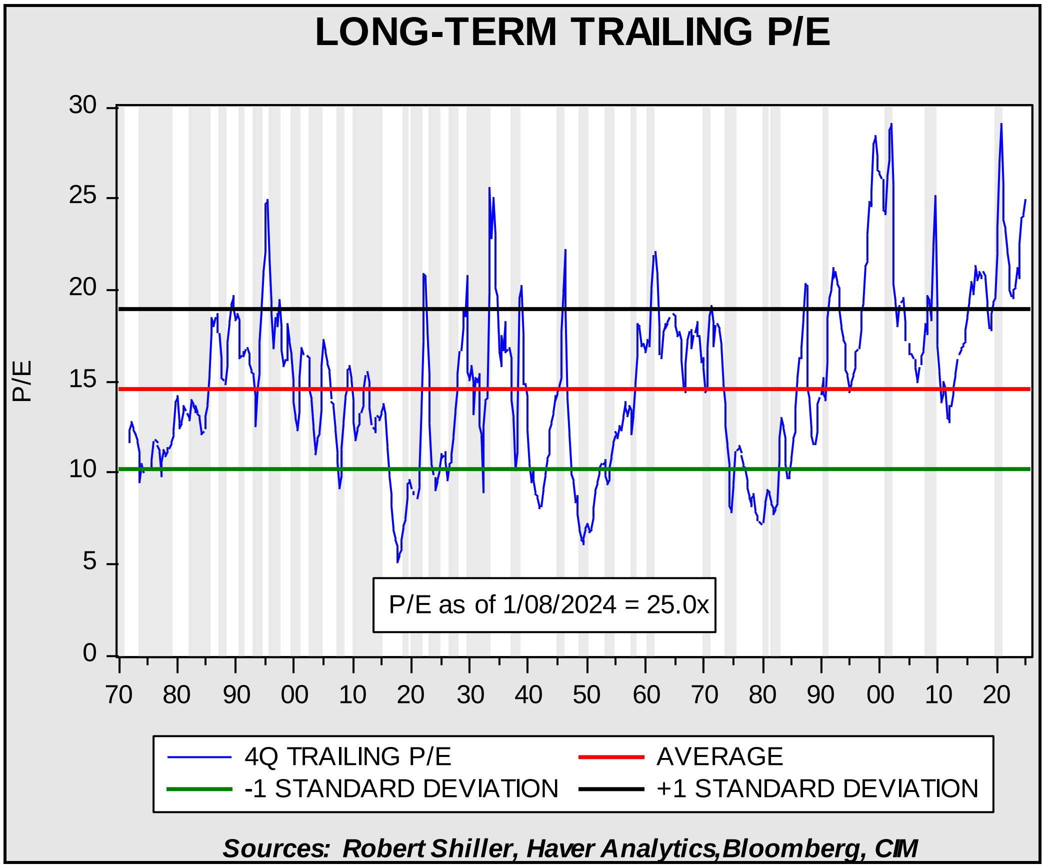


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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

January 10, 2024



Based on our methodology,[1] the current P/E is 25.0x, down 0.1 from our last report. The decrease was due to a decline 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.

---

[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.