# Daily Comment

By Patrick Fearon-Hernandez, CFA, and Thomas Wash

**[Posted: March 21, 2025 — 9:30 AM ET]** Global equity markets are lower this morning. In Europe, the Euro Stoxx 50 closed down 0.7% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed down 1.1%. Chinese markets were lower, with the Shanghai Composite down 1.3% from its previous close and the Shenzhen Composite down 1.8%. US equity index futures are signaling a lower open.

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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 |
|---|---|---|---|
| "United Arab Emirates: An Overview" (3/10/25) + podcast | "Equities as an Inflation Hedge?" (3/17/25) + podcast | Q1 2025 Report<br>Q1 2025 Rebalance Presentation | The Confluence of Ideas podcast<br>Business Cycle Report |

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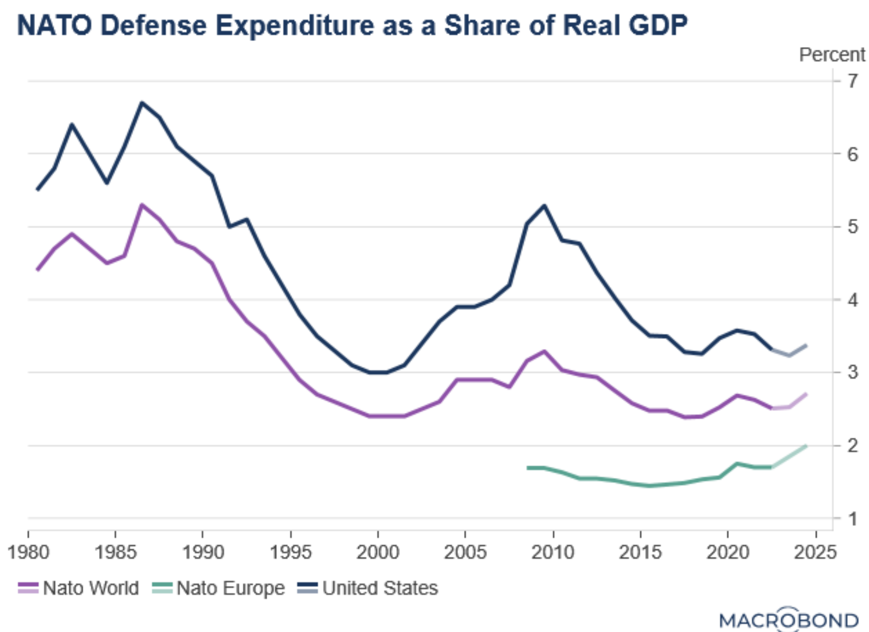
Good morning! Markets are looking for clues on consumer sentiment, as tariff uncertainty impacts demand projections. In sports, the NCAA tournament's low rate of perfect brackets (1.65%) highlights its unpredictable nature. Today's *Comment* will cover Europe's NATO contingency plans, US critical minerals production efforts, and other market-relevant developments. As always, the report will include a summary of key domestic and international data releases.

**Amerexit?** European leaders are formulating transition plans for a potential US withdrawal from NATO, aiming to bolster their own security capabilities while enabling the US to redirect more of its strategic focus toward China.

- The UK, France, Germany, and Nordic countries are spearheading a plan to substantially boost defense spending across the alliance, positioning Europe to assume the bulk of the financial and operational responsibilities for continental defense in the event of a unilateral US withdrawal from NATO. The agreement outlines a 5- to 10-year timeline for Europe to strengthen its military capabilities, ensuring a smooth transition and the ability to independently safeguard its security interests.

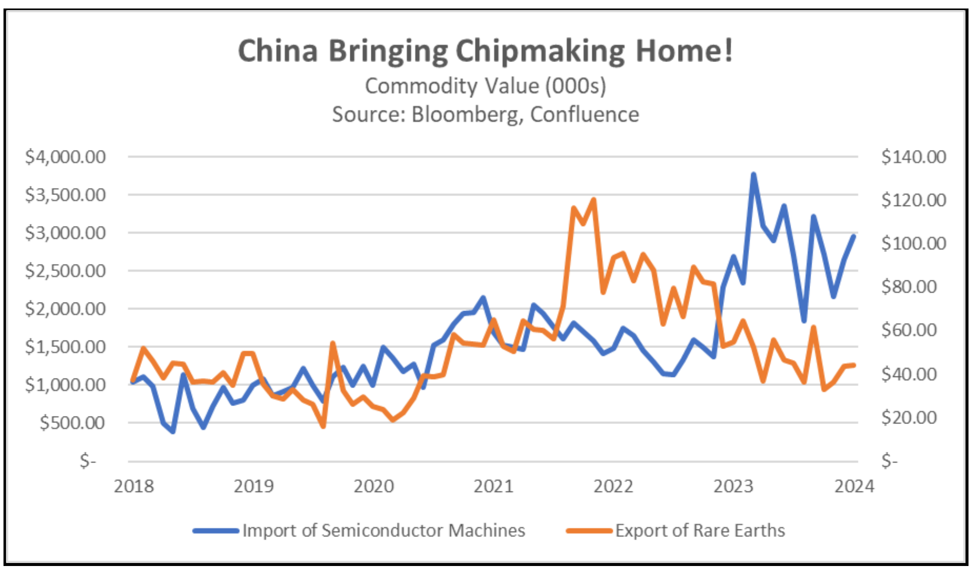
- This initiative emerges as the Trump administration intensifies its pressure on Western allies to significantly increase their defense spending. On Thursday, reports revealed that NATO will call for Europe and Canada to boost their expenditure on military equipment and weapons by 30%. Simultaneously, the US is urging member countries to raise their defense spending to 5% of GDP — a figure that surpasses the current 2% benchmark and even exceeds the percentage of GDP that the US allocates to its own defense.




- The move coincides with widespread expectations that the US is poised to scale back its military presence in Europe. Last month, a Pentagon official confirmed that the US is considering relocating up to 100,000 troops from the region, signaling a potential shift in its strategic priorities.
- Growing doubts about the US commitment to Europe have intensified pressure on European nations to develop contingency plans to support Ukraine. The UK has signaled its willingness to assist Ukraine in enforcing a ceasefire by potentially deploying ground troops, as well as air and naval forces. Simultaneously, the EU is advancing efforts to allocate 5 billion EUR ($5.4 billion) to secure ammunition for Ukraine, though France and Italy are pushing for adjustments to the proposal before finalizing the agreement.
- The increase in military spending across EU countries is expected to elevate their debt levels, as governments may need to borrow additional funds to fulfill their defense obligations. This could lead to a rise in bond issuance by individual nations. We are closely monitoring the potential for implicit backing of defense-related bonds by EU institutions, which could enhance the attractiveness of these securities and help lower borrowing costs across the EU bloc.

**More Mining Please!** President Trump has invoked war powers to facilitate the mining of critical minerals, a strategic move aimed at bolstering the United States' competitive edge in military technology amid an intensifying rivalry with China.

- On Thursday, the [president signed an executive order invoking the Defense Production Act] to expedite and streamline the production of critical minerals, underscoring the importance of national security. The order empowers the government to fast-track project permitting and provide financial support, including loans, to bolster the domestic mining industry. This action aligns with the president's broader mission to secure the resources necessary for developing advanced technologies.
- The Trump administration's efforts to secure critical resources extend beyond its borders. The [US is currently exploring a deal to gain access to Ukraine's mineral reserves] as part of the proposed peace negotiations with Russia. Additionally, the administration's interest in acquiring Greenland may, in part, [be driven by its rich deposits of rare earth elements]. Meanwhile, the [Democratic Republic of the Congo has sought to leverage its mineral wealth] to gain US support in its fight against rebel groups.
- The US is accelerating efforts to diversify its critical mineral supply chains due to growing vulnerabilities, particularly concerning its reliance on China. [China's dominance, notably its 70% control of global rare earth production] (as shown in the chart below), has become a strategic concern. Recent export restrictions on chip-related minerals, imposed in response to US semiconductor technology limitations, underscore the escalating strategic rivalry.




- The Trump administration's push to increase production of critical resources is likely to benefit chipmakers in the long term, as it could lead to lower input costs. However, this move also signals a deepening rivalry between the US and China. While we remain cautiously optimistic that this competition will not escalate into direct conflict, the ongoing AI arms race offers little reassurance and underscores the growing tensions between the two global powers.

**US Earnings Concern:** Just weeks before the president is set to implement new tariffs, there are growing concerns that businesses are already experiencing significant margin pressures.

- FedEx Corporation has lowered its profit outlook for the third consecutive quarter, citing ongoing weakness and "uncertainty in the US industrial economy" as primary concerns. The company's freight business has been particularly impacted, with fewer shipments and lower weights continuing to drag down earnings. FedEx's CEO highlighted that the unpredictable demand in the current economic environment has further exacerbated these challenges, intensifying concerns about the company's near-term performance.
- Retail giant Nike has also expressed unease by warning that its sales are likely to suffer in the current quarter. The company attributed the anticipated downturn to the impact of new tariffs and a significant decline in consumer confidence. This gloomy outlook appears to align with the findings of the University of Michigan's consumer survey, which revealed that 66% of consumers expect unemployment to rise over the next 12 months.
- Amid widespread concerns about the economy, it's worth noting that hard data still does not provide strong evidence of a recession. In the upcoming quarter, earnings reports will be a critical focus. If companies manage to deliver positive surprises, equities could potentially overcome the current negative sentiment and weather the concerns about tariffs. However, if earnings disappoint, the markets may face significant turbulence.

**UK Trouble Builds:** The Starmer government faced a double blow of bad news within the last 24 hours. Borrowing in February significantly overshot expectations, while the country's largest airport was forced to shut down due to a fire.

- The government ran a budget deficit of 10.7 billion GBP ($13.8 billion) last month, significantly surpassing the Office for Budget Responsibility's forecast of 6.5 billion GBP ($8.4 billion). This shortfall was driven by lower-than-expected tax revenues and higher public expenditures, casting doubt on its ability to meet self-imposed fiscal targets. The overshoot is likely to heighten pressure on the government to curb spending as it strives to balance the current budget — excluding investment — by the 2029-30 fiscal year.
- At the same time, Heathrow Airport was forced to shut down for the remainder of the day after a nearby fire disrupted power to the hub. While the cause remains unclear, authorities have launched an investigation, including the possibility of terrorism. The airport closure is likely to heighten concerns about the resilience of the country's critical infrastructure, particularly at a time when security has become an increasingly pressing issue throughout Europe.
- While UK Prime Minister Keir Starmer has seen a recent surge in popularity due to his handling of the Trump administration, his net approval rating remains deeply negative at -23. This could worsen if he is compelled to implement unpopular decisions, such as budget cuts, or if he faces additional security threats. The uncertainty surrounding his administration is likely to weigh on government bonds, as it raises doubts about his ability to restore the country's fiscal stability.

## US Economic Releases

No major US reports have been released so far today. The following table lists the releases and/or Fed events scheduled for the rest of the day.

| Economic Releases | | |
|---|---|---|
| No economic releases for the rest of today | | |
| **Federal Reserve** | | |
| **EST** | **Speaker or Event** | **District or Position** |
| **8:30** | Austan Goolsbee | President of the Federal Reserve Bank of Chicago |
| **9:05** | John Williams Speaks in Bahamas | President of the Federal Reserve Bank of New York |

## 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 | National CPI | y/y | Feb | 3.7% | 4.0% | 3.5% | *** | Equity and bond neutral |
| | National CPI Ex-Fresh Food | y/y | Feb | 3.0% | 3.2% | 2.9% | ** | Equity and bond neutral |
| | National CPI Ex-Fresh Food & | y/y | Feb | 2.6% | 2.5% | 2.6% | * | Equity and bond neutral |
| | Japan Buying Foreign Bonds | w/w | 14-Mar | -¥87.6b | -¥353.7b | | * | Equity and bond neutral |
| | Japan Buying Foreign Stocks | w/w | 14-Mar | -¥752.5b | ¥1177.6b | | * | Equity and bond neutral |
| | Foreign Buying Japan Bonds | w/w | 14-Mar | ¥3396.7b | ¥686.4b | | * | Equity and bond neutral |
| | Foreign Buying Japan Stocks | w/w | 14-Mar | -¥1806.2b | -¥219.6b | | * | Equity and bond neutral |
| New Zealand | Exports NZD | m/m | Feb | 6.74b | 6.06b | | ** | Equity and bond neutral |
| | Trade Balance NZD | m/m | Feb | 510b | -544m | | ** | Equity and bond neutral |
| | Imports NZD | m/m | Feb | 6.23b | 6.60b | | ** | Equity and bond neutral |
| South Korea | PPI | y/y | Feb | 1.5% | 1.8% | | ** | Equity and bond neutral |
| EUROPE | | | | | | | | |
| Eurozone | ECB Current Account SA | m/m | Jan | 35.4b% | 38.4b | | * | Equity and bond neutral |
| France | Business Confidence | m/m | Mar | 97 | 96 | 96 | ** | Equity and bond neutral |
| | Manufacturing Confidence | m/m | Mar | 96 | 97 | 97 | * | Equity and bond neutral |
| | Retail Sales SA | m/m | Feb | 0 | -0.50% | | * | Equity and bond neutral |
| Italy | Current Account Balance | m/m | Jan | -3811m | 4340m | | * | Equity and bond neutral |
| UK | Public Finances (PSNCR) | m/m | Feb | 6.4b | -22.4b | | * | Equity and bond neutral |
| | Public Sector Net Borrowing | m/m | Feb | 10.7b | -13.3b | 7.0b | * | Equity and bond neutral |
| | PSNB ex Banking Groups | m/m | Feb | 10.7b | -13.3b | | ** | Equity and bond neutral |
| | GfK Consumer Confidence | m/m | Mar | -19 | -20 | -20 | *** | Equity and bond neutral |
| Switzerland | M3 Money Supply | y/y | Feb | 2.3% | 1.7% | | ** | Equity and bond neutral |
| Russia | Gold and Forex Reserves | m/m | 14-Mar | $641.9b | $639.1b | | *** | Equity and bond neutral |
| | Money Supply, Narrow Definition | w/w | 14-Mar | 18.11t | 18.09t | | * | Equity and bond neutral |
| AMERICAS | | | | | | | | |
| Canada | Industrial Product Price | m/m | Feb | 0.4% | 1.4% | 0.3% | ** | Equity and bond neutral |
| | Raw Material Prices | m/m | Feb | 0.3% | 3.5% | -0.4% | * | 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) | 419 | 419 | 0 | Up |
| U.S. Sibor/OIS spread (bps) | 430 | 430 | 0 | Down |
| U.S. Libor/OIS spread (bps) | 432 | 432 | 0 | Down |
| 10-yr T-note (%) | 4.21 | 4.24 | -0.03 | Down |
| Euribor/OIS spread (bps) | 239 | 241 | -2 | Down |
| **Currencies** | **Direction** | | | |
| Dollar | Up | US | | Down |
| Euro | Down | Euro | | Up |
| Yen | Up | Japan | | Up |
| Pound | Down | UK | | Up |
| Franc | Down | Switzerland | | Up |
| **Central Bank Action** | **Current** | **Prior** | **Expected** | |
| Bank of Russia Key Rate | 21.00% | 21.00% | 21.00% | 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.

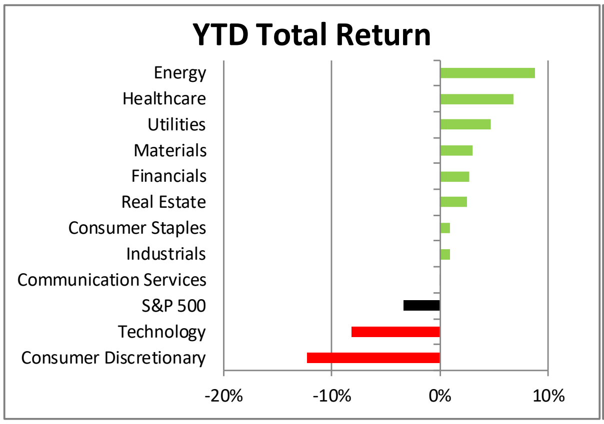
| | Price | Prior | Change | Explanation |
|---|---|---|---|---|
| **Energy Markets** | | | | |
| Brent | $71.67 | $72.00 | -0.46% | |
| WTI | $67.80 | $68.07 | -0.40% | |
| Natural Gas | $3.91 | $3.98 | -1.58% | |
| Crack Spread | $24.03 | $24.35 | -1.32% | |
| 12-mo strip crack | $20.89 | $21.01 | -0.57% | |
| Ethanol rack | $1.91 | $1.90 | 0.35% | |
| **Metals** | | | | |
| Gold | $3,031.06 | $3,044.90 | -0.45% | |
| Silver | $33.13 | $33.59 | -1.37% | |
| Copper contract | $505.00 | $511.20 | -1.21% | |
| **Grains** | | | | |
| Corn contract | $468.50 | $469.00 | -0.11% | |
| Wheat contract | $558.75 | $557.25 | 0.27% | |
| Soybeans contract | $1,013.50 | $1,013.00 | 0.05% | |
| **Shipping** | | | | |
| Baltic Dry Freight | 1,635 | 1,637 | -2 | |
| **DOE Inventory Report** | | | | |
| | **Actual** | **Expected** | **Difference** | |
| Crude (mb) | 1.75 | 1.00 | 0.75 | |
| Gasoline (mb) | -0.53 | -3.00 | 2.47 | |
| Distillates (mb) | -2.81 | -0.50 | -2.31 | |
| Refinery run rates (%) | 0.4% | 0.0% | 0.4% | |
| Natural gas (bcf) | 9 | 5 | 4 | |

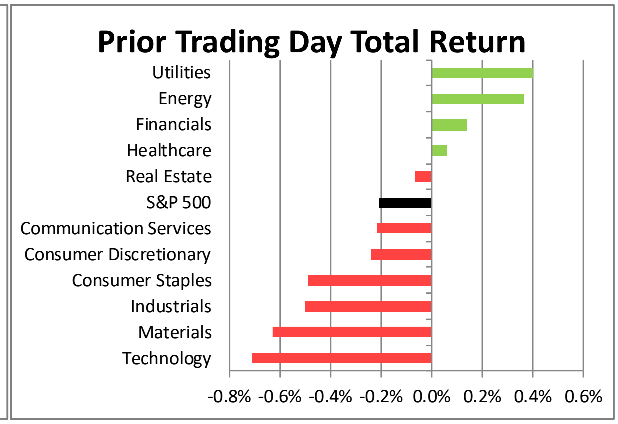
## Weather

The 6-to-10 and 8-to-14-day forecasts currently call for cooler-than-normal temperatures in the Midwest, the mid-Atlantic states, and the Northeast, with warmer-than-normal temperatures from the Great Plains westward and in Florida. The forecasts call for wetter-than-normal conditions in the northern half of the country and Texas, with dry conditions in New Mexico and Arizona.

## Data Section

### **US Equity Markets** – (as of 3/20/2025 close)

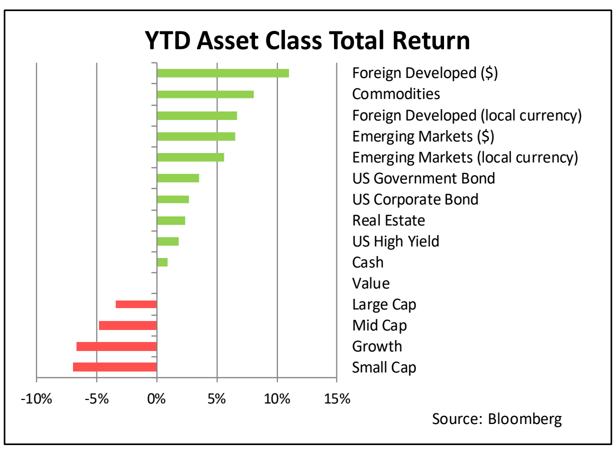



*(Source: Bloomberg)*

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 3/20/2025 close)

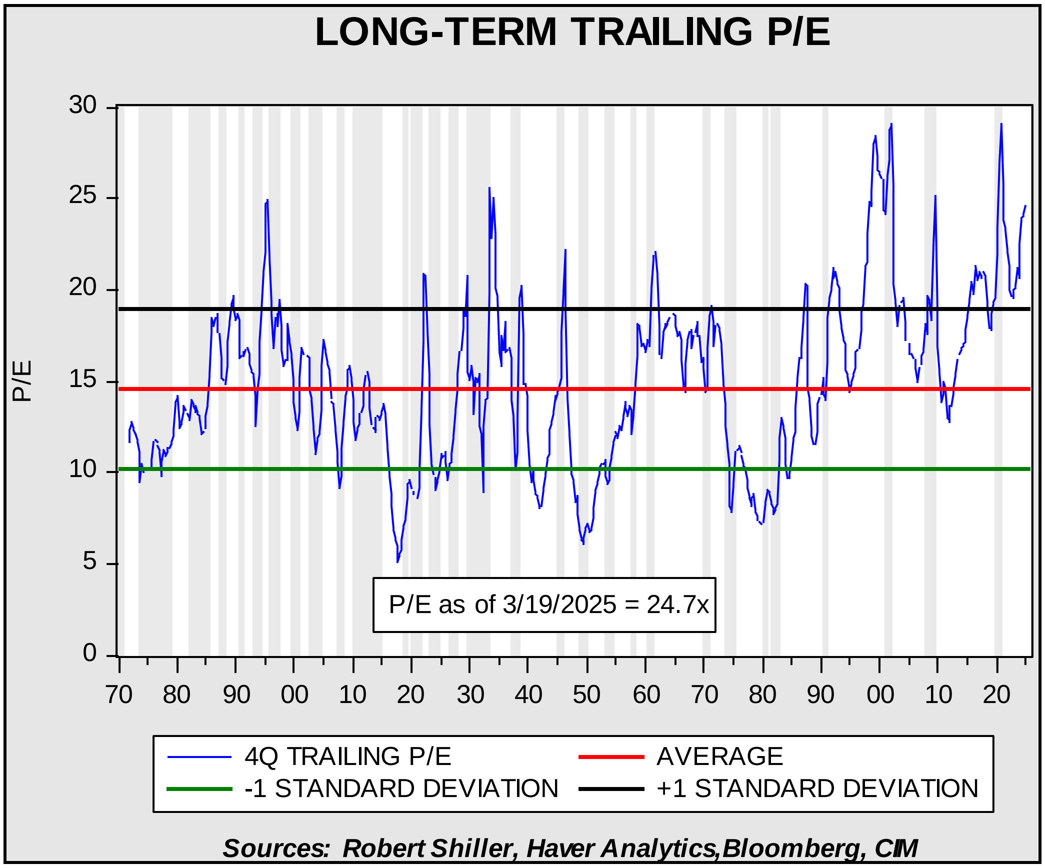



This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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

March 20, 2025




Based on our methodology,[1] the current P/E is 24.7x, down 0.1 from our last report. The drop in multiple was driven primarily by 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.*

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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 (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.