Daily Comment

Confluence Investment Management

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[Posted: March 26, 2025 — 9:30 AM ET] Global equity markets are mixed 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 up 0.3%. Chinese markets were mixed, with the Shanghai Composite essentially unchanged from its previous close and the Shenzhen Composite up 0.4%. US equity index futures are signaling a mildly higher 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 Bessent Gambit" (3/24/25)	"Equities as an Inflation Hedge?" (3/17/25) + podcast	Q1 2025 Report Q1 2025 Rebalance Presentation	The Confluence of Ideas podcast Business Cycle Report

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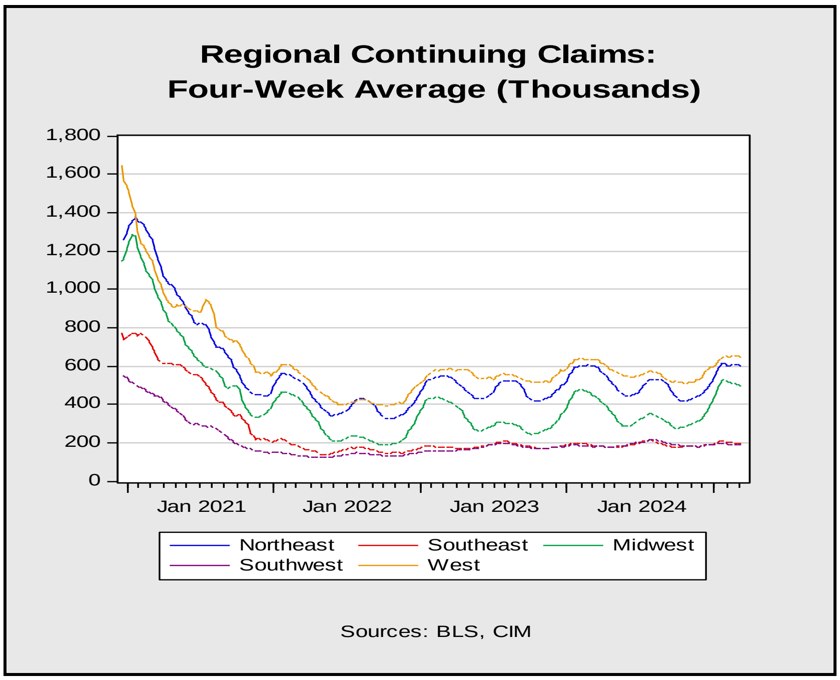
Good morning! Investors are closely tracking the latest tariff developments. Meanwhile, in a historic NHL moment, Alex Ovechkin netted his 889th career goal, placing him just six away from eclipsing Wayne Gretzky's all-time record. Today's *Comment* will analyze the latest consumer confidence data, explore the implications of new semiconductor restrictions, and break down other key financial stories driving the markets. As always, we'll also provide a roundup of domestic and international economic releases.

Soft vs. Hard Data: Recent tariffs and government workforce reductions have significantly dampened consumer confidence, as reported by The Conference Board. However, the economy continues to show signs of growth.

- US consumer confidence plummeted to a three-year low in March, with The Conference Board's index dropping sharply to 92.9 from February's revised 100.1. The decline was driven primarily by collapsing future expectations, as the six-month outlook plunged to 65.2 (down from 74.8), marking its weakest reading in over a decade. Even surveys on present situation conditions have deteriorated, falling from 138.1 to 134.5, suggesting broadening economic concerns among households.

- Tariff-related uncertainty and macroeconomic concerns drove the sentiment shift. Key indicators flashed warning signs, such as inflation expectations breaching 6% (first since 2023) and employment outlooks hitting 12-year lows. The confidence gap between demographics was striking — respondents 55+ showed the most pronounced pessimism, contrasting with modest optimism in the under-35 cohort, which saw a slight uptick.
- While depressed consumer confidence suggests growing economic anxiety, key indicators confirm the underlying economy remains robust. The unemployment rate continues to hold below 5%, with initial jobless claims staying at historically manageable levels. Recent inflation data has also provided encouraging signs of moderation. In essence, despite public pessimism, fundamental economic conditions still point to sustained expansion.

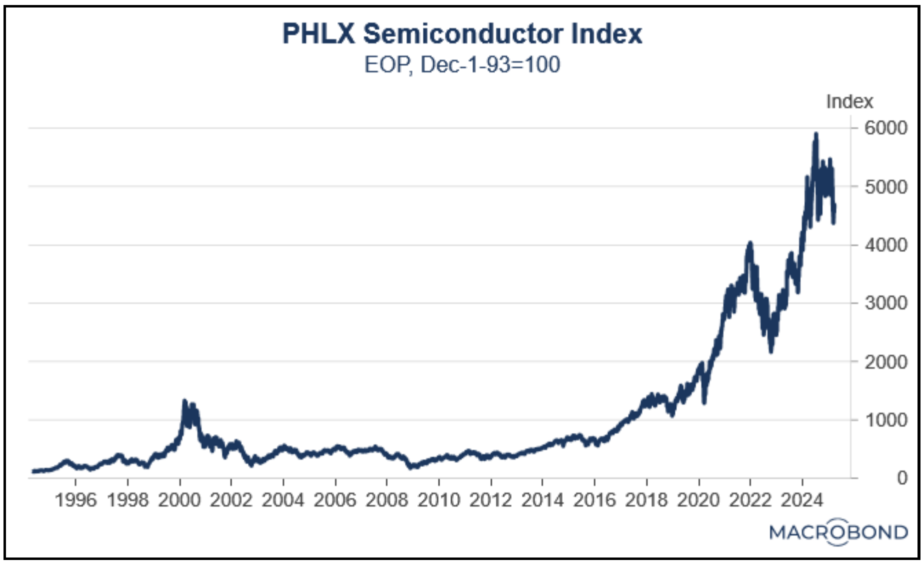


- The recent dip in consumer confidence warrants close monitoring, as it signals growing household concerns about economic conditions. However, the labor market's resilience and robust consumer spending during the significant Conference Board confidence drop in 2022 suggest that confidence surveys may not provide a complete picture of economic performance. In summary, while current trade tensions could create modest headwinds for growth, we find no definitive evidence that the economy has entered a recession.

Chipmaker Ultimatum: Foreign governments and tech firms are pushing for relaxed US semiconductor export controls ahead of the May 15 sanctions deadline, reflecting the mounting challenges of operating in today's geopolitically divided marketplace.

- The "AI Diffusion Rule," a late-term Biden administration regulation restricting the sale of high-performance computing technology to specific nations, has sent shockwaves through the semiconductor industry. This framework aims to safeguard advanced US technology and maintain America's competitive edge by compelling other countries to adhere to US standards. This move appears to be a strategic effort by the US to ensure its continued leadership in the AI space.

- The restrictions have drawn frustration from both corporations and foreign governments, as they cap potential sales for tech firms while pushing nations to align more closely with US interests. Semiconductor companies fear losing access to lucrative markets like China, which is pouring billions into AI infrastructure. Meanwhile, US allies — including Saudi Arabia, Israel, and Mexico — face new hurdles in developing their own domestic tech industries under the tightened export regime.
- The Trump administration has shown no willingness to relax these restrictions. In fact, it escalated the measures on Tuesday by adding 80 companies and organizations — predominantly Chinese, but also including firms from Iran, South Africa, and Taiwan — to a blacklist barring them access to US semiconductor technology on national security grounds.



- Geopolitical tensions are anticipated to strain chipmakers' profitability due to the growing bifurcation of supply chains between US-aligned and China-aligned entities. Coupled with the semiconductor industry's cyclical nature, these factors could generate significant headwinds. Considering these challenges, we believe diversifying investments beyond traditional big tech firms may offer value in optimizing portfolio returns in the current environment.

Growing Trade Volatility: President Trump has signaled an unwavering stance on tariffs, seeking to condition markets to expect — or at least react less sharply to — new trade restrictions.

- On Tuesday, President Trump announced limited tariff exemptions effective April 2, while tempering expectations for widespread relief. He maintained his commitment to the tariffs but hinted at a more nuanced strategy, favoring calibrated adjustments over rigid reciprocal actions. These remarks coincided with reports that his administration is exploring a more targeted implementation of the tariffs due next Wednesday, possibly encouraging last minute deal making with countries before the deadline.

- At the same time, the president has accelerated efforts to impose tariffs on copper, moving ahead of schedule. This follows President Trump's earlier directive to the US Commerce Department to complete a 270-day investigation into the metal's trade patterns. However, the review appears to be concluding significantly earlier than planned, with expectations that Trump will soon announce 25% tariffs on copper imports. The announcement has already led to a surge in copper prices.

- A key focus is the market's reaction to evolving trade dynamics. In recent months, equities have shown significant swings and increased volatility. As these fluctuations become more commonplace, we anticipate investor attention shifting towards economic fundamentals — specifically, tangible evidence of tariff impacts — rather than solely policy announcements. Assuming continued economic resilience, the period of heightened volatility may be receding.

Truce Coming Soon? Ukraine and Russia have agreed to a temporary ceasefire on sea and energy targets. However, significant challenges remain in reaching a comprehensive peace agreement to resolve the broader conflict.

- While the full terms of the agreement remain unclear, the deal represents the first formal accord between the warring parties. US mediators secured Russian participation by offering targeted sanctions relief in exchange for reduced military operations. For its part, Ukraine has demonstrated willingness to follow America's diplomatic lead in these negotiations.

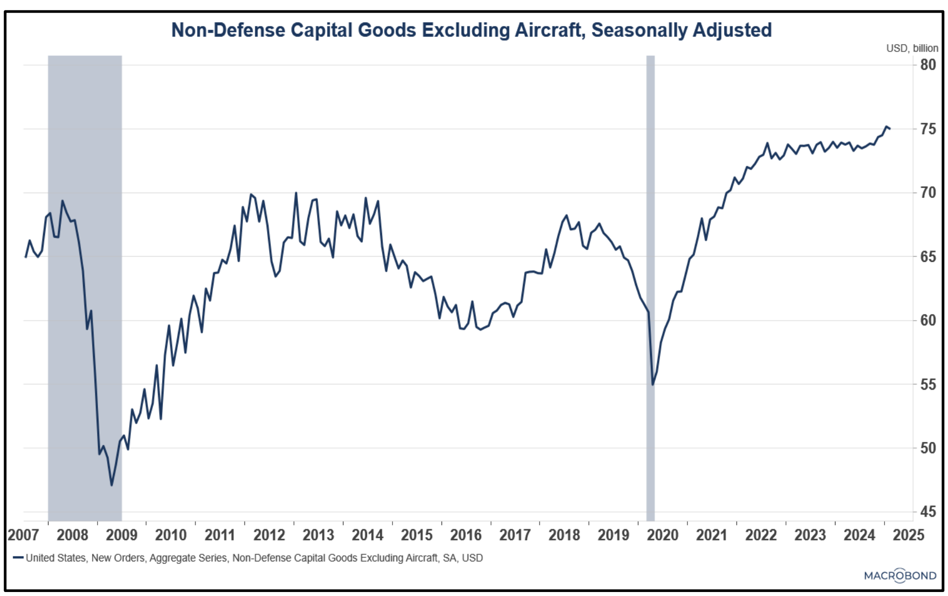
- However, no clear timeline for resolving the conflict has emerged, particularly from the Russian side. President Trump recently criticized Putin for deliberately stalling peace negotiations, but remains optimistic that a deal can be done. Analysts speculate that Putin, facing mounting war costs, continues to seek tangible justification for the invasion's "success," most likely through complete control of the Donbas region.

- A resolution to the Ukraine-Russia conflict would significantly impact global markets, with particularly pronounced effects on European economies and commodity markets, especially oil. While we maintain our base-case expectation for a negotiated settlement before year-end, the bargaining process will likely prove more protracted than Western powers, including the US administration, would prefer.

US Economic Releases

The Mortgage Bankers Association today said ***mortgage applications*** for the week ended March 21 fell 2.0%, extending the previous week's decline of 6.2%. Purchase applications rose 0.7%, extending the previous week's slight rise of 0.1%; however, refinancing applications continued to decline, 5.3% this week after the previous week's fall of 12.8%. The average interest rate on a 30-year mortgage essentially held steady, falling 1 basis point to 6.71%.

February ***durable goods*** orders surprisingly rose by a seasonally adjusted 0.9%, versus an expected decline of 1.0%; however, this represents a deceleration from the previous month's rise of 3.3%. Durable goods orders are often driven by transportation equipment, where just a few airliner orders can have a big impact. Still, February ***durable goods orders excluding transportation*** also rose 0.7%, exceeding the expected 0.2% rise and the previous month's gain of 0.1%. Finally, the durable goods report also includes a key proxy for corporate capital investment. In February, ***nondefense capital goods orders ex-aircraft*** fell 0.3%, falling short of both the expected gain of 0.2% and the previous month's gain of 0.9%. Compared with the same month one year earlier, overall durable goods orders in February rose 0.5%, while durable orders ex-transport fell 1.4%. Nondefense capital goods orders ex-aircraft rose 2.3%. The chart below shows the progression of nondefense capital goods orders ex-aircraft since just before the Global Financial Crisis.



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**
10:00	Neel Kashkari Hosts Fed Listens Event and Conversation	President of the Federal Reserve Bank of Minneapolis
13:10	Alberto Musalem Speaks on Economy and Monetary Policy	President of the Federal Reserve Bank of St. Louis

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	PPI Services	y/y	Feb	3.0%	3.2%	3.1%	*	Equity and bond neutral
	Leading Economic Index	m/m	Jan F	108.3	108.0		**	Equity and bond neutral
	Coincident Index	y/y	Jan F	116.1	116.2		**	Equity and bond neutral
Australia	CPI	y/y	Dec	2.4%	2.5%	2.5%	**	Equity and bond neutral
EUROPE								
France	Consumer Confidence	m/m	Mar	92	93	94	***	Equity bearish, bond bullish
UK	CPI	y/y	Feb	2.8%	3.0%	3.0%	***	Equity and bond neutral
	CPI Core	y/y	Feb	3.5%	3.7%	3.6%	***	Equity and bond neutral
	CPI Services	m/m	Feb	5.0%	5.0%	4.9%	*	Equity and bond neutral
	Retail Price Indes	m/m	Feb	394.5	394.0	391.7	**	Equity and bond neutral
	RPI	y/y	Feb	3.4%	3.6%	3.5%	**	Equity and bond neutral
	House Price Index	y/y	Jan	4.9%	4.6%		*	Equity and bond neutral
AMERICAS								
Mexico	International Reserves Weekly	w/w	21-Mar	$236731m	$236288m		*	Equity and bond neutral
Brazil	Current Account Balance	m/m	Feb	-$8.758b	-$8.655b	-$9.000b	**	Equity and bond neutral
	Foreign Direct Investment	m/m	Feb	$9.300b	$6.501b	$5.500b	**	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 T-bill yield (bps)	418	418	0	Up
U.S. Sibor/OIS spread (bps)	431	431	0	Down
U.S. Libor/OIS spread (bps)	432	432	0	Down
10-yr T-note (%)	4.34	4.31	0.03	Up
Euribor/OIS spread (bps)	237	237	0	Down
Currencies	**Direction**			
Dollar	Up	US		Down
Euro	Down	Euro		Up
Yen	Up	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.

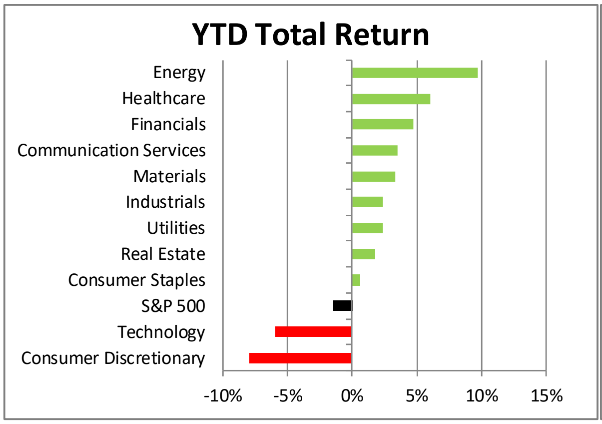
	Price	Prior	Change	Explanation
Energy Markets				
Brent	$73.67	$73.02	0.89%	
WTI	$69.66	$69.00	0.96%	
Natural Gas	$3.86	$3.84	0.52%	
Crack Spread	$24.33	$24.29	0.14%	
12-mo strip crack	$21.13	$21.09	0.19%	
Ethanol rack	$1.88	$1.89	-0.20%	
Metals				
Gold	$3,028.87	$3,020.09	0.29%	
Silver	$33.77	$33.73	0.13%	
Copper contract	$527.65	$521.05	1.27%	
Grains				
Corn contract	$458.75	$457.75	0.22%	
Wheat contract	$542.75	$543.25	-0.09%	
Soybeans contract	$1,003.50	$1,001.75	0.17%	
Shipping				
Baltic Dry Freight	1,642	1,652	-10	
DOE Inventory Report				
	Actual	**Expected**	**Difference**	
Crude (mb)		1.98		
Gasoline (mb)		-1.50		
Distillates (mb)		-1.00		
Refinery run rates (%)		-0.5%		
Natural gas (bcf)		38		

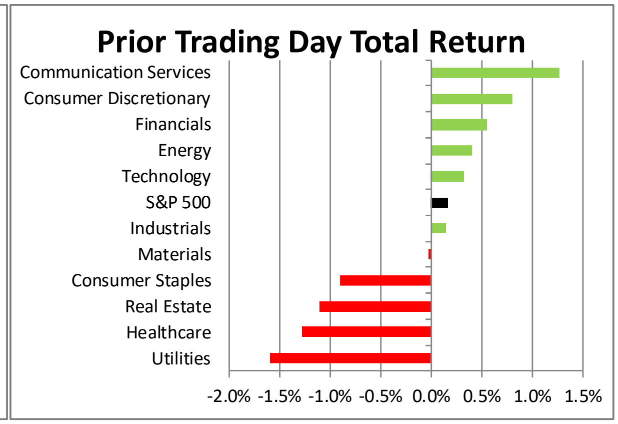
Weather

The 6-to-10 and 8-to-14-day forecasts indicate warmer-than-normal temperatures across most of the country, with cooler conditions expected in northern California, Oregon, and Washington. For precipitation, wetter-than-normal conditions are likely for most of the country.

Data Section

US Equity Markets – (as of 3/25/2025 close)

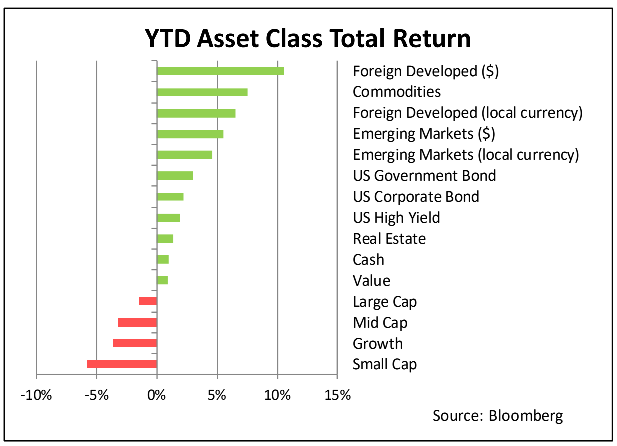




(Source: Bloomberg)

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 3/25/2025 close)

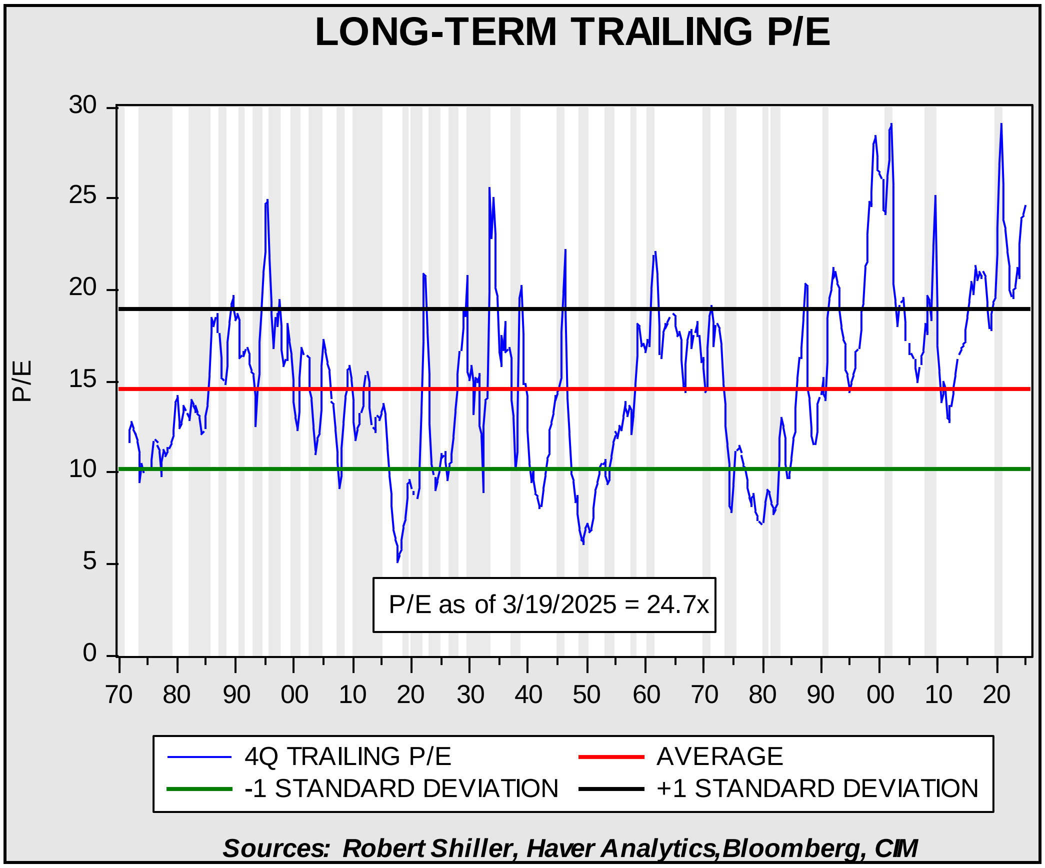


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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.

[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.