

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: May 28, 2024—9:30 AM EDT] Global equity markets are mostly lower this morning. In Europe, the Euro Stoxx 50 is down 0.2% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed essentially unchanged. Chinese markets were lower, with the Shanghai Composite down 0.5% from its previous close and the Shenzhen Composite down 1.1%. Conversely, US equity index futures are signaling a 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 emphasized in bold:

- [Bi-Weekly Geopolitical Report](#) (5/20/2024) (there is no associated podcast): “The Great COVID Labor Reform”
- [Asset Allocation Quarterly – Q2 2024](#) (4/25/2024): Discussion of our asset allocation process, Q2 2024 portfolio changes, and our outlook for the markets.
- [Asset Allocation Q2 2024 Rebalance Presentation](#) (5/7/2024): Video presentation featuring the Asset Allocation Committee as they review the asset allocation strategies, recent portfolio changes, and the current macro environment.
- [Asset Allocation Bi-Weekly](#) (5/28/2024) (with associated [podcast](#)): “**The Importance of the Federal Reserve’s Inflation Target**”
- [Confluence of Ideas podcast](#) (5/8/2024) “Reviewing the Asset Allocation Rebalance: Q2 2024”

Our *Comment* today opens with some notes on the rising power of far-right political parties in Europe and the implications for European economic policy. We next review several other international and US developments with the potential to affect the financial markets today, including the UK Labour Party’s vow not to substantially raise taxes after Britain’s July 4 elections and today’s move to T+1 trade settlement in the US financial markets.

European Union: Ahead of the European Parliament elections to be held June 6 to 9, French far-right leader Marine Le Pen [has proposed that her Identity and Democracy \(ID\) group of national conservative parties cooperate with Italian Prime Minister Meloni’s European Conservatives and Reformists \(ECR\)](#) to form the second-largest grouping in the legislature and force EU policy to the right. Meloni has expressed interest in the idea, even though she had been negotiating to support European Commission President von der Leyen’s center-right group.

- Political parties in the various EU member countries typically ally themselves with like-minded parties from other countries to boost their power in the European Parliament.
- President von der Leyen’s European People’s Party (EPP) is currently the legislature’s biggest cross-national group, with 176 of the 703 seats. The leftist Progressive Alliance of Socialists and Democrats is the second-largest group, with 144 seats. The far right is fractured between four different parties, the largest of which are the ECR, with 66 seats, and the ID, with 62 seats.
- Current opinion polls suggest the far-right parties will make significant gains in the elections. If so, a combination of the ECR and ID likely would make it the second-most powerful group in the parliament and force the EPP to adopt more conservative positions in key issues such as immigration and environmental policy.

Eurozone: In an interview with the *Financial Times*, European Central Bank Chief Economist Philip Lane [strongly hinted that the institution will start cutting interest rates at its next policy meeting on June 6](#). Describing the central bank’s read on the eurozone’s current output and price data, Lane said, “Barring major surprises, at this point in time there is enough in what we see to remove the top level of restriction.”

United Kingdom: Shadow Chancellor Rachel Reeves of the opposition Labour Party [has promised that if Labour wins the July 4 elections, it will not raise taxes beyond the handful of modest measures it has already proposed](#) (i.e., extending the windfall tax on energy company profits, applying the value-added tax to private school fees, and ensuring private equity bonuses are “taxed appropriately”). The statements by Reeves appear to be aimed at maintaining Labour’s current lead of 20+ percentage points in public opinion polls.

China: Ma Jiantang, the former Communist Party secretary at the State Council’s Development Research Center, [warned that China is facing severe economic problems because of its low birth rate and falling population](#). Ma argued China must adopt an “urgent” response, but policies are still focused on family planning rather than encouraging births. Ma called for new initiatives such as promoting assisted reproductive technology, registering children born out of wedlock, improving birth insurance, extending maternity leave, and building more childcare centers.

Japan: Bank of Japan Governor Ueda [said at a central banking conference that his institution will continue raising interest rates toward a “neutral” level](#), but because it’s hard to know what that level is for the Japanese economy, the central bank will move cautiously. The statement confirms expectations that the BOJ will likely hike interest rates only slowly in the coming months and quarters. With the Federal Reserve likely to hold US interest rates higher for longer, the BOJ’s approach is likely to continue weighing on the value of the yen (JPY).

New Zealand: The Reserve Bank of New Zealand [said it will impose new restrictions on mortgage lending to preserve financial stability](#) in the face of rising home prices and increasing consumer debt. The new rules will cap the amount of new loans going to borrowers with high debt-to-income and loan-to-value ratios. Since rising home prices and worsening debt burdens are now a problem in many countries, the New Zealand moves could potentially portend similar moves in other countries.

Israel-Hamas Conflict: An Israeli airstrike in Gaza on Sunday night [killed two senior Hamas military commanders, but it also killed some 45 Palestinian civilians](#). The high level of civilian casualties to take out just two Hamas leaders has further stirred world anger at Israel and deepened Prime Minister Netanyahu's isolation. It also promises to further undermine support for President Biden ahead of the US elections in November.

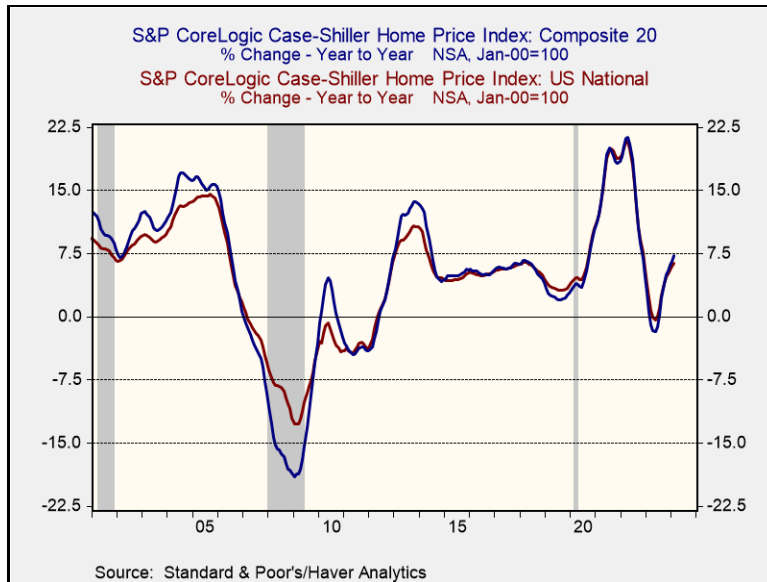
- Separately, Israeli forces got into a shootout with Egyptian troops as they took control of a border crossing between Gaza and Egypt, killing an Egyptian officer.
- The incident once again likely raises the risk of the conflict broadening into a regional war that could disrupt key energy supplies.

US Financial Markets: As of today, trades in equities, corporate bonds, exchange traded funds, mutual funds, and options [will all settle the day after the trade, i.e., T+1](#) versus the previous standard of T+2. The move aims to cut brokers' collateral requirements and reduce price volatility in time of market stress. Several other countries also shifted to T+1 this week, and similar moves are being considered in the UK, Switzerland, and the European Union.

US Commercial Real Estate Market: New data [shows that the vacancy rate for retail properties has fallen to a near-record low of 4.1%, versus 5.0% during the coronavirus pandemic](#) and 7.1% shortly after the Great Financial Crisis of 2007-2008. The low vacancy rate reflects strong economic growth and more disciplined construction in recent years. Although financial difficulties for office properties continue to scare investors out of real estate funds, the retail data serves as a reminder that other areas of commercial real estate are in a strong position.

US Economic Releases

Home prices continued their upward trend in March according to public and private data sources. An index tracked by the Federal Housing Finance Agency showed that home prices rose 0.1% in March. The reading was well below the consensus estimate of 0.5%. Meanwhile, the Case-Shiller Home Price Index, followed by S&P Global, showed that national home prices rose 0.3% in March, compared to the previous month's reading of 0.6%, while home prices in the top 20 cities rose 0.3%, down from the previous month's increase of 0.9%.



The chart above shows the annual change in the S&P CoreLogic National and Top-20 City Home Price Indexes. The country-wide index rose 6.5% from the prior year, while the urban index rose 7.4% in the same period.

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

Economic Releases						
EST	Indicator			Expected	Prior	Rating
10:00	Conference Board Consumer Confidence	m/m	May	96.0	97.0	***
10:00	Conference Board Present Situation	m/m	May	--	142.9	*
10:00	Conference Board Expectations	m/m	May	--	66.4	*
10:30	Dallas Fed Manufacturing Activity	m/m	May	-12.5	-14.5	**
Federal Reserve						
EST	Speaker or Event	District or Position				
9:55	Neel Kashkari Gives Panel Remarks	President of the Federal Reserve Bank of Minneapolis				
13:05	Lisa Cook and Mary Daly Speak on AI	Member of the Board of Governors and San Francisco Fed President				

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	Leading Index CI	m/m	Mar F	112.2	111.4		**	Equity and bond neutral
	PPI Services	y/y	Apr	2.8%	2.4%	2.5%	*	Equity and bond neutral
Australia	Retail Sales	m/m	Apr	0.1%	-0.4%	0.2%	***	Equity and bond neutral
South Korea	Retail Sales	y/y	Apr	10.8%	10.9%		**	Equity and bond neutral
	Depart. Store Sales	y/y	Apr	-2.0%	8.9%		*	Equity and bond neutral
	Discount Store Sales	y/y	Apr	-6.7%	6.2%		*	Equity and bond neutral
China	Industrial Profits	y/y	Apr	4.0%	-3.5%		*	Equity and bond neutral
EUROPE								
Germany	IFO Business Climate	m/m	May	89.3	89.3	90.4	***	Equity and bond neutral
	IFO Current Assessment	m/m	May	88.3	88.9	89.8	**	Equity bearish, bond bullish
	IFO Expectations	m/m	May	90.4	89.7	90.8	**	Equity and bond neutral
Switzerland	Domestic Sight Deposits CHF	w/w	24-May	452.5b	459.0b		*	Equity and bond neutral
	Total Sight Deposits CHF	w/w	24-May	461.2b	467.4b		*	Equity and bond neutral
AMERICAS								
Canada	Retail Sales	m/m	Mar	-0.2%	-0.1%	-0.1%	**	Equity and bond neutral
	Retail Sales Ex-Autos	m/m	Mar	-0.6%	-0.2%	0.3%	**	Equity bearish, bond bullish
Mexico	Current Account Balance	q/q	1Q	-\$12582m	\$11817m	-\$7500m	*	Equity and bond neutral
Brazil	Total Outstanding Loans	m/m	Apr	5894b	5882b		**	Equity and bond neutral
	IBGE Inflation IPCA-15	m/m	May	3.70%	3.77%	3.74%	***	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)	560	560	0	Up
3-mo T-bill yield (bps)	525	525	0	Up
U.S. Sibor/OIS spread (bps)	534	534	0	Up
U.S. Libor/OIS spread (bps)	535	536	-1	Up
10-yr T-note (%)	4.47	4.47	0.00	Up
Euribor/OIS spread (bps)	380	381	-1	Down
Currencies	Direction			
Dollar	Down			Up
Euro	Up			Up
Yen	Flat			Down
Pound	Up			Up
Franc	Up			Down

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.

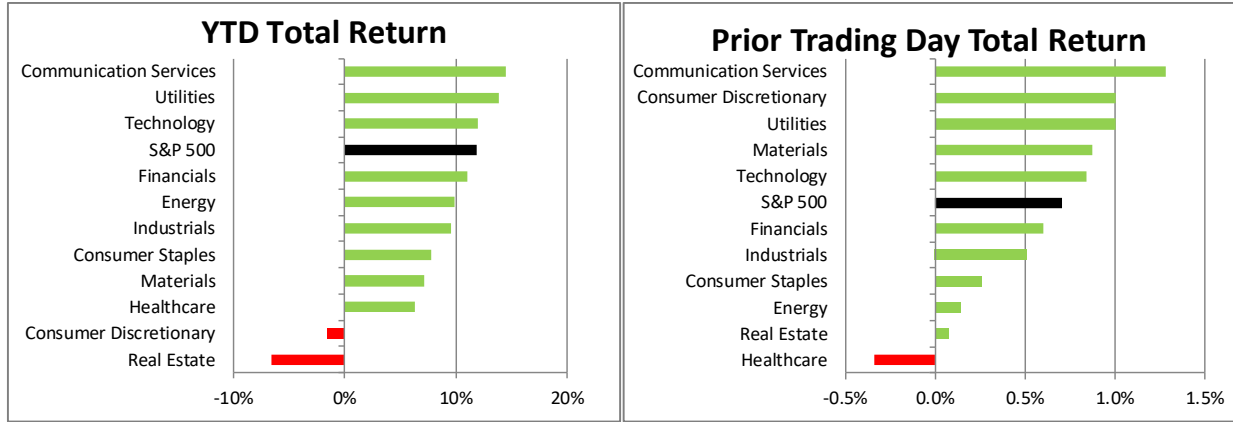
DOE Inventory Report	Price	Prior	Change	Explanation
Energy Markets				
Brent	\$83.21	\$83.10	0.13%	
WTI	\$78.85	\$77.72	1.45%	
Natural Gas	\$2.50	\$2.52	-0.67%	
12-mo strip crack	\$22.38	\$22.68	-1.35%	
Ethanol rack	\$1.94	\$1.94	0.00%	
Metals				
Gold	\$2,346.69	\$2,350.97	-0.18%	
Silver	\$31.61	\$31.63	-0.06%	
Copper contract	\$482.10	\$475.35	1.42%	
Grains				
Corn contract	\$467.25	\$464.75	0.54%	
Wheat contract	\$705.50	\$697.25	1.18%	
Soybeans contract	\$1,243.00	\$1,248.00	-0.40%	
Shipping				
Baltic Dry Freight	1,797	1,796	1	

Weather

The 6-10 and 8-14 day forecasts call for warmer-than-normal temperatures in most of the country, with cooler temperatures expected in the lower Ohio Valley. The precipitation outlook calls for wetter-than-average conditions throughout most of the country with drier-than-normal conditions expected in the Rocky Mountain and Midwest regions.

Data Section

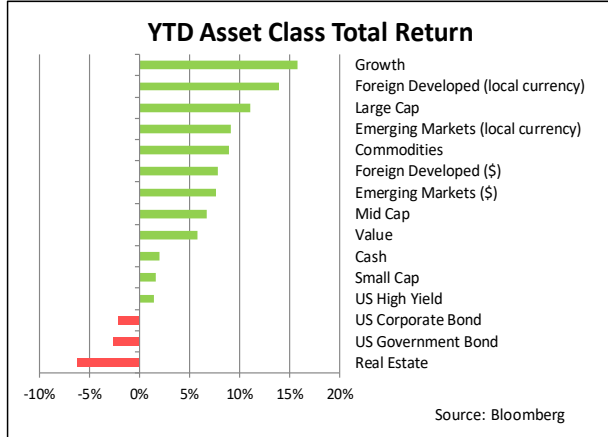
US Equity Markets – (as of 5/24/2024 close)



(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 5/24/2024 close)

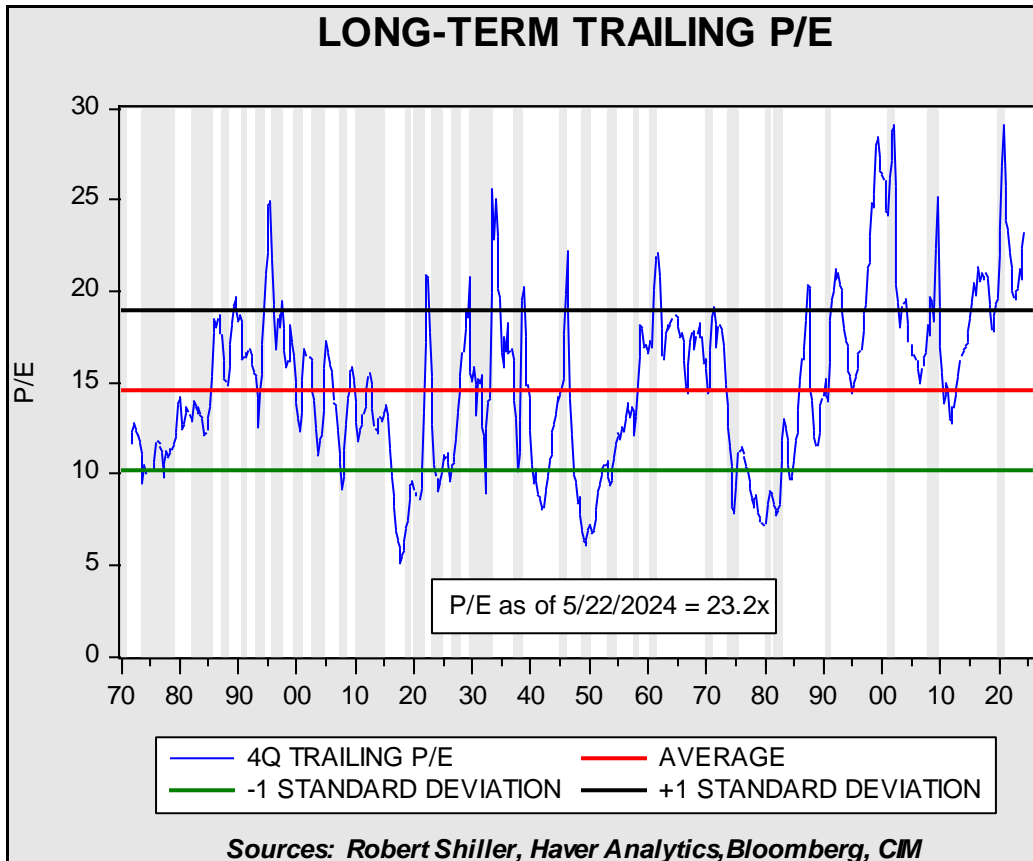


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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

May 23, 2024



Based on our methodology,¹ the current P/E is 23.2x, unchanged from our last report. Despite a rise in the stock price index, the valuation multiple remained unchanged due to a corresponding increase in company 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 (Q2, Q3 and Q4) and one estimate (Q1). 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.