Daily Comment

By Patrick Fearon-Hernandez, CFA, and Thomas Wash

[Posted: November 15, 2024 — 9:30 AM ET] Global equity markets are generally lower this morning. In Europe, the Euro Stoxx 50 closed down 0.4% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed up 0.4%. Chinese markets were lower, with the Shanghai Composite down 1.5% from its previous close and the Shenzhen Composite down 2.4%. US equity index futures are signaling a lower open.

With 461 companies having reported so far, S&P 500 earnings for Q3 are running at $62.80 per share compared to estimates of $60.44, which is up 4.2% from Q3 2023. Of the companies that have reported thus far, 75.4% have exceeded expectations, while 17.8% 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:

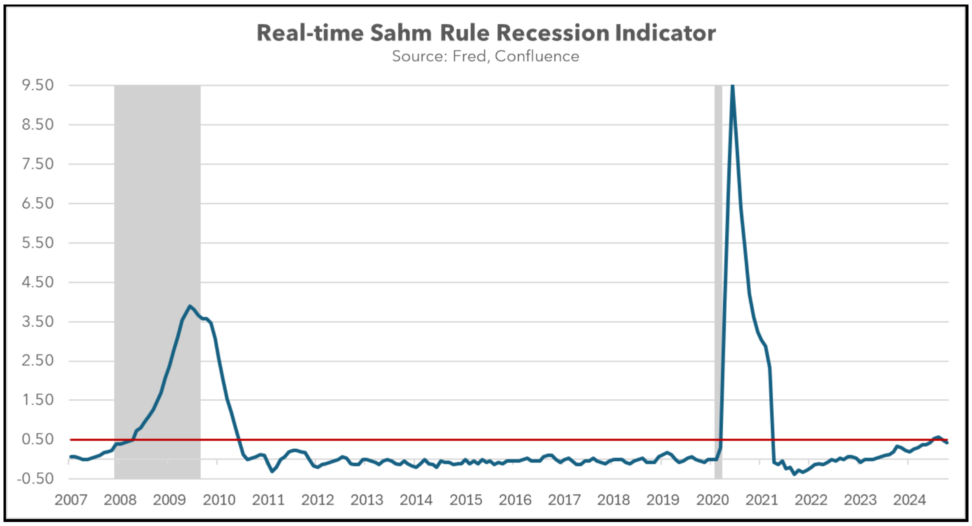
Bi-Weekly Geopolitical Report	Asset Allocation Bi-Weekly	Asset Allocation Quarterly	Of Note
Rising US & Global Debt: A Perspective Check (11/4/24) + podcast	*Let's Talk About Tariffs!* (11/11/24) + podcast	Q4 2024 Report Q4 2024 Rebalance Presentation	Confluence of Ideas Podcast *The Q4 Asset Allocation Rebalance*

Good morning! The market is currently assessing the latest retail sales data. In sports news, the USMNT soccer team defeated Jamaica in the first leg of the quarterfinals of Concacaf Nations League. Today's *Comment* will discuss why the Federal Reserve may scale back interest rate cut expectations in 2025, why investors may be ready to take money off the sidelines, and why Marine Le Pen's presidential bid may potentially be blocked. As usual, the report concludes with a roundup of international and domestic data releases.

Powell Speaks: The Federal Reserve chair gave the first indication that the central bank may be altering the path of interest rates following stronger-than-expected growth.

- On Thursday, Fed Chair Jerome Powell stated that the economy's strength means that the central bank is not in a rush to cut interest rates. His comments followed a CPI report indicating stalled inflation in October and a tight labor market, with jobless claims at their lowest level since May. Although he didn't specifically reference the upcoming December meeting, his remarks led the market to lower its expectations for an imminent rate cut. The latest [CME FedWatch Tool fell from 82.5% to just above 60.0%] on Thursday.

- His comment comes as the labor market shows signs of improvement since the Sahm Rule was triggered over the summer. In July, the three-month moving average of the unemployment rate rose 0.5 percentage points above its 12-month low for the first time since the pandemic. While such a sharp increase is typically associated with recessions, this time may have been a false alarm. As of October, the moving average is only 0.43 percentage points above the minimum, an elevated but not recession-indicative level.

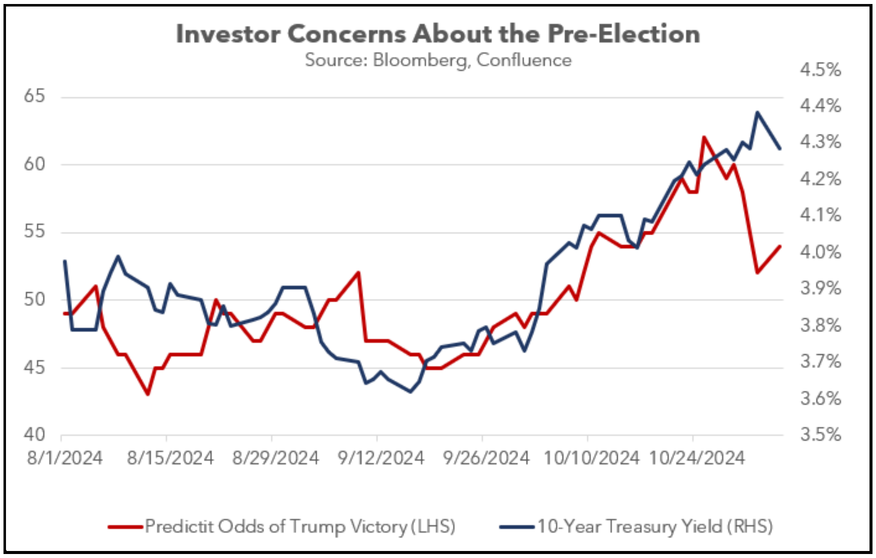


- The Fed chair's remarks indicate that policymakers may lower their expectations for rate cuts next year. The latest Summary of Economic Projections had forecast a 100-basis-point rate reduction in 2025, driven by concerns over potential labor market softening. However, given recent economic data indicating a less immediate recession risk, policymakers may opt to slow the pace of rate cuts for the next year. While a December rate cut remains possible, the chance of an indefinite pause is starting to increase.

Money on the Sidelines: Elevated interest rates and pre-election jitters have driven investors toward short-term funds, a shift that could carry significant implications for financial markets in the coming year.

- In September, [US money market funds topped $7 trillion for the first time], according to the Office of Financial Research. This surge highlights investors' sustained interest in higher deposit interest rates, even as the Federal Reserve has implemented a 50-basis-point rate cut and signaled further reductions. The milestone underscores a growing trend of investors favoring short-term cash holdings while awaiting clearer market direction. Notably, [Warren Buffett, the highly respected investor, has begun reducing his stake in Apple and increasing his cash reserves], reflecting this cautious sentiment at the time.

- The significant rise in risk aversion was driven by uncertainty surrounding what appeared to be a closely contested election. With polls remaining tight in the days leading up to the vote, investors adopted a cautious stance, bracing for outcomes on either side. This nervousness was reflected in the increasing yields on 10-year Treasurys despite the Federal Reserve's 50 bps rate cut in September. The yield rise was seen as a "Trump trade," fueled by concerns over a potentially widening deficit driven by the prospect of additional fiscal stimulus and tariffs.

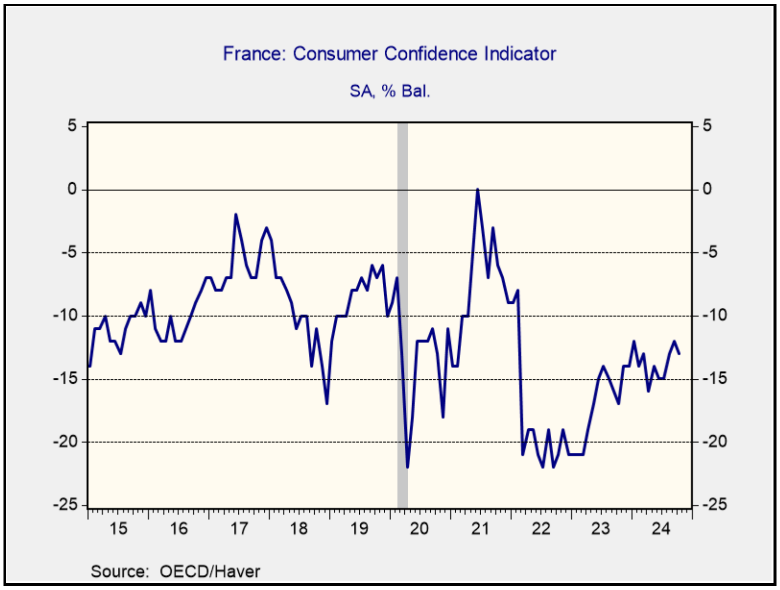


- With the election concluded and Republican President-elect Donald Trump securing a decisive victory, investor risk aversion is likely to diminish significantly. The market's sharp reaction to the outcome hints at the potential for a broader rally if promises of tax cuts and deregulation are realized. Consequently, we anticipate that a substantial portion of sidelined capital could flow back into the equity market in 2025, assuming the Federal Reserve maintains a steady course and avoids having to make an embarrassing U-turn in its monetary policy. This should be bullish for risk assets.

Le Pen in Trouble: The leader of France's right-wing National Rally party could miss out on the next presidential election following accusations of funds misappropriation.

- French prosecutors have accused Marine Le Pen and members of her party of misappropriating European Union funds by diverting them to domestic activities rather than their intended EU-related purposes. They have recommended a 300,000 EUR ($316,890) fine for Le Pen, a 2 million EUR ($2.1 million) fine for the party, two years in prison or house arrest, and a five-year ban on holding public office. While a ruling is not expected for months, the prosecutor has called for a "provisional execution" of the sentence, which could prevent her from running for office even if the decision is sent to the appeals court.

- Le Pen's potential exclusion from the presidential race comes at a time when her popularity has surged, while her opponent's has sharply declined. Her party not only secured the most votes in the European Parliament elections, but also led in the first round of the legislative elections, though it finished third in the second round. Meanwhile, French President Emmanuel Macron's approval rating has fallen below 25% as he grapples with a loss of public trust following his controversial pension reform, which raised the retirement age from 62 to 64.

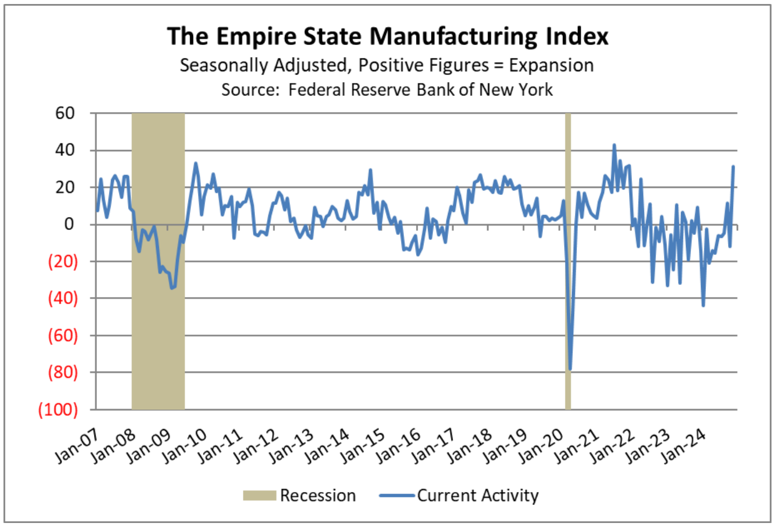


- While the immediate impact on French financial markets may be limited due to the presidential election taking place in 2027, the long-term implications of a popular leader's legal troubles cannot be ignored. The perception of a politically motivated prosecution could erode public trust in the justice system, fueling a populist backlash that benefits the National Rally. This could, in turn, lead to increased market volatility, affecting French equities and bond yields. As the trial progresses, vigilant monitoring is crucial to assess its potential impact on the political landscape and financial markets.

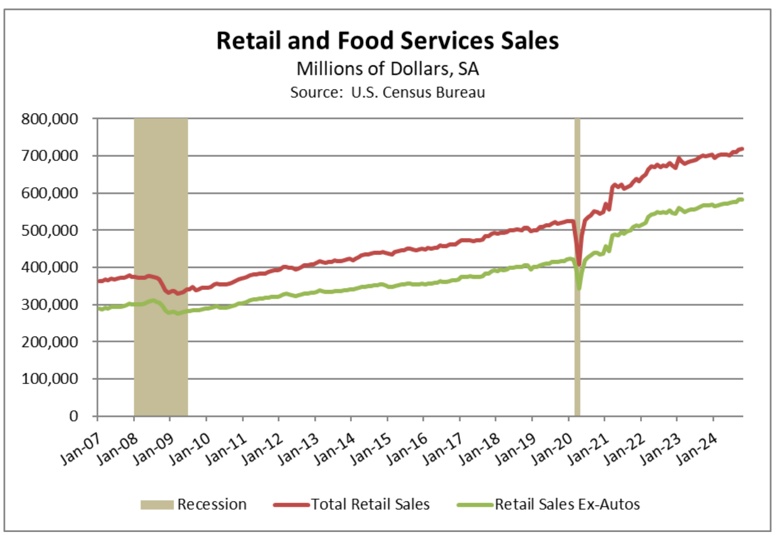
In Other News: Argentina is considering withdrawing from the Paris climate accord, signaling that countries are increasingly resistant to burdensome environmental regulations. Meanwhile, China is finding it relatively inexpensive to borrow in the market as it seeks capital to help finance the fiscal stimulus necessary to revive its economy. Additionally, the ratings agency Moody's has downgraded Mexico's credit outlook due to the recent judicial reforms, indicating that these changes are sparking a backlash from investors.

US Economic Releases

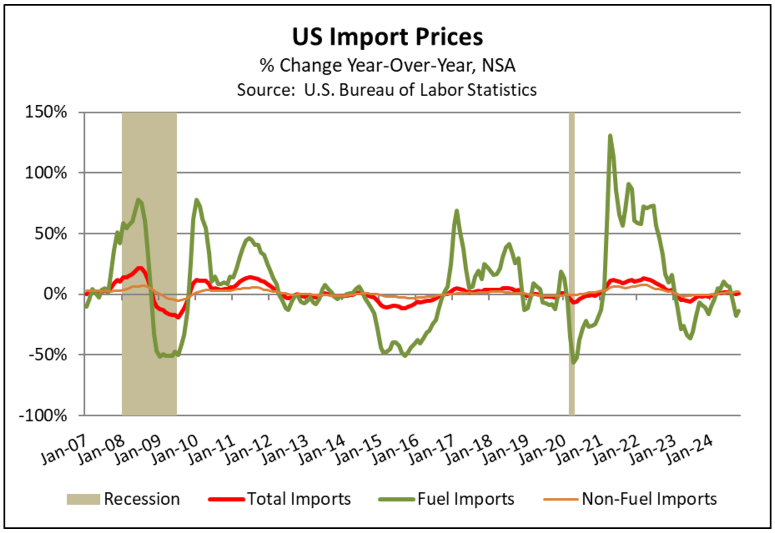
The New York FRB said its November ***Empire State Manufacturing Index*** rose to a seasonally adjusted 31.2, far surpassing both the expected reading of 0.0 and the October reading of -11.9. This index is designed so that positive readings point to expanding factory activity in New York state. At its current level, the index suggests factory activity in New York has recently surged. The chart below shows how the index has fluctuated since just before the Global Financial Crisis.



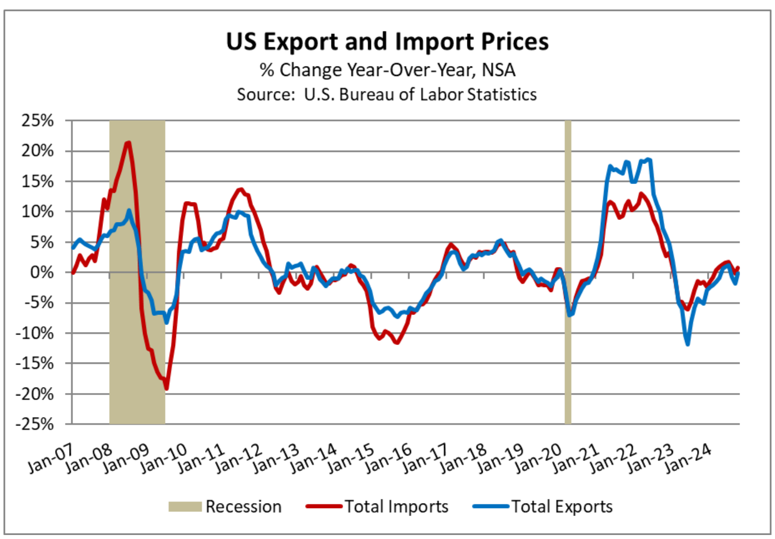
Separately, October ***retail sales*** rose by a seasonally adjusted 0.4%, beating the anticipated rise of 0.3% but marking only half the revised 0.8% increase in September. Overall retail sales are often driven by the volatile auto and auto parts sector, which makes up almost one-fifth of the total. That was true last month, as October ***retail sales excluding autos and auto parts*** were up only 0.1%, short of both their expected increase of 0.3% and the previous month's revised 1.0% jump. Overall retail sales in October were up 4.6% from the same month one year earlier, while sales excluding autos and auto parts were up 4.2%. The chart below shows how retail sales have changed since just before the GFC.



Finally, October ***import prices*** were up 0.3% from the previous month, compared with their expected decline of 0.1% and their decreases of 0.4% in September and 0.3% in August. Of course, import prices are often driven by volatility in the petroleum fuels category, and that happened last month. October ***import prices excluding fuels*** were up 0.2%, above their anticipated gain of 0.1% and matching their gain in September. Overall import prices in October were up 0.8% year-over-year, while import prices excluding fuels were up 2.3%. The chart below shows the year-over-year change in import prices since just before the GFC.



According to the report, ***export prices*** in October were down 0.1% from one year earlier, entirely because of weak pricing in the key agriculture category. Comparing the annual change in export prices versus import prices provides a sense of the US "terms of trade," or the relative advantage or disadvantage the country is facing because of trends in international trade prices. The chart below compares the year-over-year change in US export and import prices since just before the GFC.



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

Economic Releases						
ET	**Indicator**			**Expected**	**Prior**	**Rating**
10:00	Business Inventories	m/m	Sep	0.2	0.3	*
Federal Reserve						
ET	**Speaker or Event**	**District or Position**				
8:30	Austan Goolsbee on CNBC	President of the Federal Reserve Bank of Chicago				
9:00	Susan Collins Gives Opening Remarks	President of the Federal Reserve Bank of Boston				
10:30	Susan Collins Apprears on Bloomberg TV	President of the Federal Reserve Bank of Boston				
13:15	John Williams Gives Opening Remarks	President of the Federal Reserve Bank of New York				
14:05	Austan Goolsbee on Bloomberg Television	President of the Federal Reserve Bank of Chicago				
15:00	Thomas Barkin Speaks on Yahoo Finance	President of the Federal Reserve Bank of Richmond				

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	GDP SA	q/q	3Q P	0.20%	0.5%	0.2%	***	Equity and bond neutral
	GDP Deflator	q/q	3Q P	2.50%	3.1%	2.7%	***	Equity and bond neutral
	Industrial Production	y/y	Sep F	-2.6%	-2.8%		***	Equity and bond neutral
	Capacity Utilization	y/y	Sep	4.4%	-5.3%		**	Equity and bond neutral
	Tertiary Industry Index	m/m	Sep	-0.2%	-1.1%	0.2%	***	Equity and bond neutral
New Zealand	BusinessNZ Manufacturing PMI	m/m	Oct	45.8	47.0		***	Equity and bond neutral
China	Industrial Production	y/y	Oct	5.3%	5.4%	5.6%	***	Equity and bond neutral
	Retail Sales	y/y	Oct	4.8%	3.2%	3.8%	**	Equity and bond neutral
	Fixed Assets Ex Rural YTD	y/y	Oct	3.4%	3.4%	3.5%	**	Equity and bond neutral
India	Wholesale Prices	m/m	Oct	2.36%	1.84%	2.30%	**	Equity and bond neutral
	Trade Balance	m/m	Oct	-$27142m	-$20781m	-$22000m	*	Equity and bond neutral
	Exports	y/y	Oct	17.2%	0.5%		**	Equity and bond neutral
	Imports	y/y	Oct	3.9%	1.6%		**	Equity and bond neutral
EUROPE								
France	CPI	y/y	Oct F	1.2%	1.2%	1.2%	***	Equity and bond neutral
	CPI, EU Harmonized	y/y	Oct F	1.6%	1.6%	1.5%	**	Equity and bond neutral
	CPI Ex-Tobacco Index	q/q	Oct	118.83	118.50	118.76	*	Equity and bond neutral
Italy	CPI, EU Harmonized	y/y	Oct F	1.0%	1.0%	1.0%	***	Equity and bond neutral
UK	Industrial Production	y/y	Sep	-1.8%	-1.7%	-1.1%	***	Equity bearish, bond bullish
	Manufacturing Production	y/y	Mar	-0.7%	-0.3%	0.0%	**	Equity bearish, bond bullish
	Index of Services 3M/3M	m/m	Sep	0.1%	0.1%	0.2%	**	Equity and bond neutral
	Visible Trade Balance	m/m	Sep	-£16321m	-£15212m	-£15800m	**	Equity and bond neutral
	Trade Balance	m/m	Sep	-£3462	-£2015m	-£1200m	**	Equity and bond neutral
	GDP	y/y	3Q P	1.0%	0.7%	1.0%	***	Equity and bond neutral
	Total Business Investment	y/y	3Q P	4.50%	0.20%		*	Equity and bond neutral
Switzerland	Producer & Import Prices	y/y	Oct	-1.8%	-1.3%		**	Equity and bond neutral
Russia	Gold and Forex Reserves	m/m	8-Nov	$620.8b	$632.7b		***	Equity and bond neutral
	Money Supply, Narrow Definition	w/w	8-Nov	18.30t	18.29t		*	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)	440	442	-2	Down
U.S. Sibor/OIS spread (bps)	452	452	0	Down
U.S. Libor/OIS spread (bps)	449	449	0	Down
10-yr T-note (%)	4.44	4.44	0.00	Up
Euribor/OIS spread (bps)	301	302	-1	Down
Currencies	**3 Mo**			
Dollar	Down	US		Down
Euro	Down	Euro		Up
Yen	Up	Japan		Up
Pound	Up	UK		Up
Franc	Up	Switzerland		Up
Central Bank Action	**Actual**	**Prior**	**Expected**	
Bank of Mexico Overnight Rate	10.250%	10.500%	10.250%	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	$72.27	$72.56	-0.40%	
WTI	$68.47	$68.70	-0.33%	
Natural Gas	$2.69	$2.79	-3.27%	
Crack Spread	$17.97	$17.67	1.68%	
12-mo strip crack	$20.39	$20.29	0.53%	
Ethanol rack	$1.76	$1.76	0.02%	
Metals				
Gold	$2,566.90	$2,564.85	0.08%	
Silver	$30.60	$30.45	0.49%	
Copper contract	$421.45	$414.05	1.79%	
Grains				
Corn contract	$431.75	$430.75	0.23%	
Wheat contract	$551.50	$548.25	0.59%	
Soybeans contract	$997.00	$987.50	0.96%	
Shipping				
Baltic Dry Freight	1,692	1,630	62	
DOE Inventory Report				
	Actual	**Expected**	**Difference**	
Crude (mb)	2.09	1.60	0.49	
Gasoline (mb)	-4.41	1.00	-5.41	
Distillates (mb)	-1.39	1.27	-2.66	
Refinery run rates (%)	0.9%	0.7%	0.2%	
Natural gas (bcf)	42	39	3	

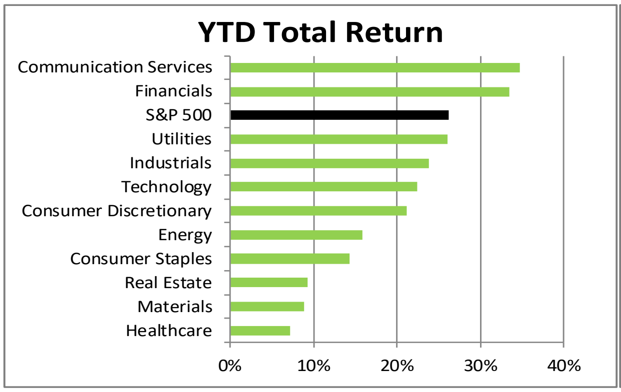
Weather

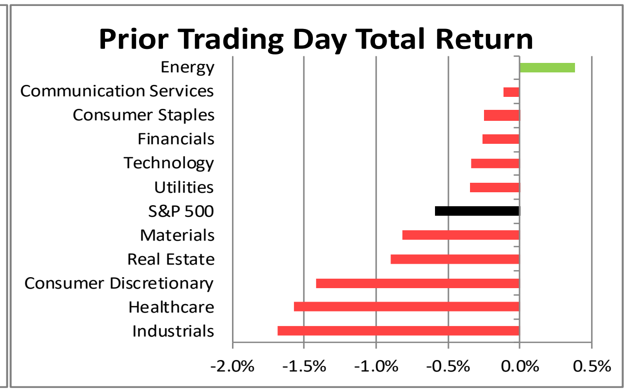
The 6-to-10-day and 8-to-14-day forecasts currently call for warmer-than-normal temperatures along the West Coast, in the northern stretches of the Great Lakes region, and in the Northeast, with cooler-than-normal temperatures in the Great Plains, the Mississippi Valley, and the Southeast. The forecasts call for wetter-than-normal conditions in the Upper Midwest and southern Florida, with dry conditions in the southern Rocky Mountains and Great Plains.

Tropical Storm Sara has now formed in the Caribbean Sea off the coast of Honduras and is moving northwesterly. It is expected to bring heavy rains, winds, and flooding to Central America and Mexico in the coming days.

Data Section

US Equity Markets – (as of 11/14/2024 close)

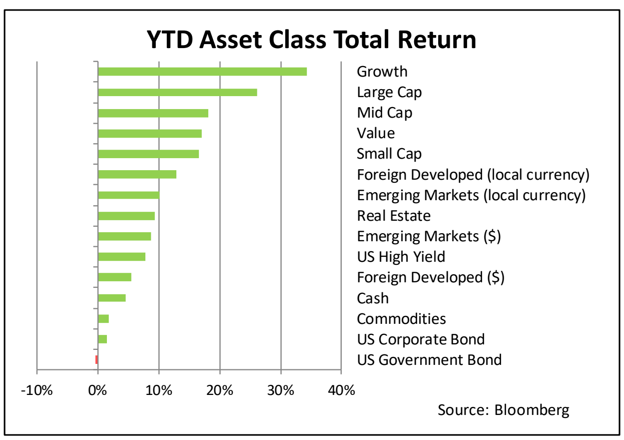




(Source: Bloomberg)

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 11/14/2024 close)

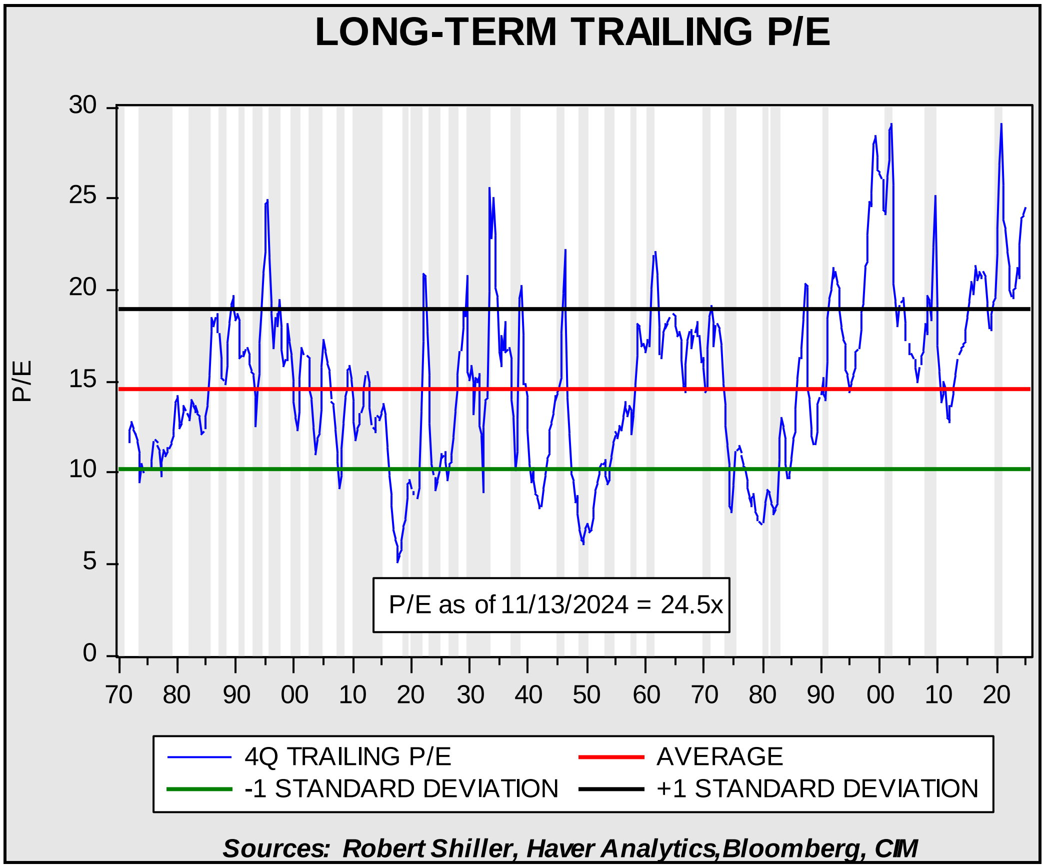


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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

November 14, 2024



Based on our methodology,[1] the current P/E is 24.5x, up 0.1 from our last report. The increase is the multiple was driven by an increase 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 (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.