Daily Comment

By Patrick Fearon-Hernandez, CFA, and Thomas Wash

[Posted: November 25, 2024 — 9:30 AM ET] Global equity markets are generally higher this morning. In Europe, the Euro Stoxx 50 closed up 0.2% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed up 0.1%. Chinese markets were mixed, with the Shanghai Composite down 0.1% from its previous close and the Shenzhen Composite up 0.4%. US equity index futures are signaling a higher open.

With 472 companies having reported so far, S&P 500 earnings for Q3 are running at $63.10 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 18.0% 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
Implications of North Korean Soldiers in the Ukraine War (11/18/24) + podcast	***Bonds and the Post-Election Environment** (11/25/24)* + **podcast**	Q4 2024 Report Q4 2024 Rebalance Presentation	Confluence of Ideas Podcast *The Q4 Asset Allocation Rebalance*

Our *Comment* today opens with news that the US military has been more involved in the recent China-Philippine tensions than was previously known. We next review several other international and US developments with the potential to affect the financial markets today, including another unexpectedly strong showing by a far-right party in a European election and President-elect Trump's latest nominees for his top economic cabinet positions.

United States-Philippines-China: Late last week, the US Navy revealed it has a new task force deployed to the Philippines to help Manila defend its sovereignty in the South China Sea. The US personnel are not directly involved in the Philippine navy or coast guard operations that often come into dangerous contact with Chinese forces, but they do provide reconnaissance and intelligence assets to those operations. They are also training Philippine sailors and helping them integrate US-supplied military equipment into their operations.

- The Navy's forward deployment and close cooperation with Philippine forces had not been disclosed previously. We have often reported on incidents in which Chinese navy, coast guard, and maritime militia forces engage in physical clashes with Philippine forces trying to sail through disputed waters. During those operations, it is now known that US Navy aircraft and drones were somewhere in the vicinity supporting the Philippine forces, although it isn't clear how close.

- The presence of US personnel may be intended to dissuade the Chinese from taking stronger action against the Philippine forces. However, it probably also raises the risk of an accidental clash between US and Chinese personnel.

- The development helps confirm that China's aggressiveness against Manila's territorial waters in the South China Sea is perhaps even more dangerous than the tension between China and Taiwan. At some point, China's territorial pressure on the Philippines could conceivably lead to a scary US-China conflict that would likely have huge negative impacts for the global economy and financial markets.

United States-China-Russia: At the Center for Strategic and International Studies on Friday, outgoing US Deputy Secretary of State Kurt Campbell warned that Beijing and Moscow are increasingly coordinating and cooperating in their foreign policies, in a way that will eventually pose a major threat to US interests. According to Campbell, the Biden administration has tried to keep China and Russia apart, but the effort has been thwarted by their leaders' profound mistrust and conviction that the US is in sharp decline.

- Campbell's statement is consistent with our recent warnings that China and key members of its geopolitical bloc (Russia, Iran, and North Korea) are increasingly cooperating to undermine the US bloc. Acting in a more coordinated, organized way should enhance the China bloc's power, even if its members don't build formal alliances or sign mutual defense treaties. If Beijing and its partners can accept ceding some of their autonomy to act in concert, they can increase their overall power and/or cut their total defense costs.

- At the same time, the US bloc stands at risk of splintering over issues such as tariffs and trade barriers, defense spending, migration, and energy policy. If these issues undermine the US bloc's cohesion, or even if they are merely interpreted as signs of weakness by the China bloc, we think China-bloc leaders will act even more aggressively in places like the South China Sea, the Middle East, Ukraine, Western Europe, and the US.

China: The China Population and Development Research Center has issued a report warning that population declines in the rural provinces bordering Central Asia will lead to security and economic problems if they are not reversed. The report notes that the Central Asian countries along the border still have fast-growing populations. It also suggests that population declines in China's trade hubs along the border could slow its ground-based exports and imports. The report therefore calls for a range of new subsidies to draw workers to the border regions.

- For example, the report notes that the port town of Alashankou in Xinjiang province handles fully half of China's overland trade, and yet its population is only 17,000, of which only 3,423 are permanent residents.

- Similarly, the city of Manzhouli in Inner Mongolia accounts for over 60% of China's overland trade with Russia, and its registered population dropped from 128,900 in 2020 to just 88,800 in 2023.

European Union: As EU leaders continue working on their proposal for a centralized fund to help member countries rebuild their defense forces, France has dropped its demand that any funds provided for weapons purchases be spent in the EU. Instead, France will reportedly support a rule that up to 35% of any such funds can be channeled to non-EU suppliers. The French climbdown increases the chance that the proposal will be approved. It also likely means that major US defense contractors will get a significant slice of any new EU military funding.

France: As usual, the first wines of the new grape harvest, the *Beaujolais nouveau*, were released last week on the third Thursday of November. *Le Beaujolai nouveau c'est arrivé*! This author tried in vain to enjoy them, as he usually does, but he found them way too young and under-developed. Life is too short to drink bad wine, so for your Thanksgiving turkey, we recommend a nice, big, well-cellared Zinfandel, or perhaps a Riesling from Germany or the US.

Lithuania: A DHL cargo plane crashed into a house today during an attempted emergency landing near the capital city of Vilnius. The crash killed one crew member and injured several people on the ground. Authorities are investigating the incident and haven't ruled out terrorism. Given the recent string of suspected Russian sabotage attacks across Europe, including an effort to start a fire on DHL planes, it would be no surprise if the attack is ultimately tagged to the Kremlin. If it is, the incident would further worsen European-Russian tensions.

Romania: Călin Georgescu, a pro-Russia candidate formerly associated with the right-wing populist AUR party, won yesterday's first-round presidential elections with 23.0% of the vote. Liberal leader Elena Lasconi came in second with 19.2%, slightly ahead of leftist Prime Minister Marcel Ciolacu, who had led the polls ahead of the election. If the results are confirmed, voters will choose between Georgescu and Lasconi in a run-off election in two weeks.

- The results are the latest in a long string of surprisingly strong performances by pro-Russia, right-wing nationalist parties across Europe. At some level, it is likely that the Russian intelligence services have tipped the scales with clandestine influence campaigns and political interference. Nevertheless, the results point to a strong backlash against the European Union and its traditional economic, political, and social policies.

- Whoever wins the run-off election will become the most powerful politician in Romania, with the right to name the prime minister and make key decisions on national security and foreign affairs. If Georgescu wins the presidency, Romania could become a less reliable member of not only the EU, but also of the North Atlantic Treaty Organization.

US Economic Policy: President-elect Trump on Friday and Saturday announced his nominees for most of the remaining top posts in his administration. Among his most key economic-policy nominees, he said he wants Scott Bessent, a hedge-fund manager and protégé of billionaire

philanthropist George Soros, to be Treasury secretary. Trump also named [Russell Vought](#) to head the White House Office of Management and Budget, just as he did in his first term.

- Bessent's nomination is likely to be well received by investors, considering his strong understanding of the bond and currency markets, focus on bringing down the federal budget deficit and regulation, and intent to help balance US foreign trade. The investor-friendly pick helps explain why US stock prices [are up approximately 0.5%](#) so far this morning.

- Vought, who became a key leader in the Heritage Foundation's "Project 2025" program, has championed not only tight fiscal spending, but also quick, aggressive action to bring independent agencies such as the Federal Reserve and the Securities and Exchange Commission under tighter control by the White House.

- More broadly, commentators to date have focused mostly on the idea that Trump's cabinet nominees have been marked mostly by their loyalty to him and their willingness to disrupt the status quo in Washington. We actually think the key aspect of the nominees is that they represent a broad range of ideologies, from leftist to right-wing. That reflects the wide nature of Trump's coalition. Going forward, the big issue may be how Trump will hold such a wide coalition together, given their divergent interests.

US Defense Industry: The *Wall Street Journal* today says President-elect Trump [is also mulling two financiers who have invested in start-up defense technology firms to be his deputy defense secretary](#). The two are Trae Stephens, a partner at the Founders Fund venture capital firm, and Stephen Feinberg, a billionaire investor.

- Consideration of the two private-equity leaders reflects the fact that much of the new defense spending that we expect around the world will probably flow into small, newly established firms specializing in advanced technologies such as autonomous weapons, quantum computing, hypersonics, and specialized materials.

- Indeed, Defense Department leaders have already recognized the importance of such new technologies in rebuilding and renewing the US military. The department has already launched various initiatives designed to help nurture and support small firms providing those innovations.

- We still see new business for big, well-established traditional defense firms, especially in Europe and Asia. Nevertheless, the new flow of funds into smaller defense start-ups could spur an exciting rush of innovation that will lead to many interesting initial public offerings in the coming years.

US Movie Industry: On its opening weekend, movie musical "Wicked" [racked up strong theater ticket sales of $114 million, setting the stage for a potentially long and lucrative run worldwide](#). Meanwhile, on its opening weekend, "Gladiator II" pulled in almost $56 million. The good results suggest the nation's movie studios and theaters could be turning the corner after a long period of weak sales.

US Economic Releases

There were no economic releases prior to publication time. The following table lists the economic releases and Fed events scheduled for the rest of today.

Economic Releases						
ET	Indicator			Expected	Prior	Rating
10:00	Chigago Fed National Activlty Index	m/m	Oct	0.20	-0.28	**
10:30	Dallas Fed Manufacturing Activity	m/m	Nov	-2.4	-3.0	**
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								
Japan	Leading Economic Index	m/m	Sep F	109.1	109.4		**	Equity and bond neutral
	Coincident Index	y/y	Sep F	115.3	115.7		**	Equity and bond neutral
	Nationwide Dept Sales	y/y	Oct	-0.7%	2.3%		***	Equity and bond neutral
New Zealand	Retail Sales Ex Inflation	q/q	3Q	-0.1%	-1.2%	-0.5%	***	Equity and bond neutral
	Trade Balance NZD	m/m	Oct	-1544m	-2154m		**	Equity and bond neutral
	Exports NZD	m/m	Oct	5.77b	4.91b		**	Equity and bond neutral
	Imports NZD	m/m	Oct	7.31b	7.06b		**	Equity and bond neutral
EUROPE								
Germany	IFO Business Climate	m/m	Nov	85.7	86.5	86.0	***	Equity and bond neutral
	IFO Current Assessment	m/m	Nov	84.3	85.7	85.5	**	Equity bearish, bond bullish
	IFO Expectations	m/m	Nov	87.2	87.3	87.0	**	Equity and bond neutral
Switzerland	Domestic Sight Deposits CHF	w/w	22-Nov	451.0b	455.0b		*	Equity and bond neutral
	Total Sight Deposits CHF	w/w	22-Nov	459.4b	463.4b		*	Equity and bond neutral
AMERICAS								
Canada	Retail Sales	m/m	Sep	0.4%	0.4%	0.4%	**	Equity and bond neutral
	Retail Sales Ex-Autos	m/m	Sep	0.9%	-0.8%	0.4%	**	Equity and bond neutral
Brazil	Current Account Balance	m/m	Oct	-$5880m	-$6863m	-$6200m	**	Equity and bond neutral
	Foreign Direct Investment	m/m	Oct	$5717m	$5229m	$5000m	**	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)	442	442	0	Down
U.S. Sibor/OIS spread (bps)	452	452	0	Down
U.S. Libor/OIS spread (bps)	448	449	-1	Down
10-yr T-note (%)	4.35	4.40	-0.05	Down
Euribor/OIS spread (bps)	302	301	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	
PBOC 1-Year Med-Term Lending (Bil.)	900.0b	700.0b	900.0b	On Forecast
PBOC 1-Year Med-Term Lending Facility	2.00%	2.00%	2.00%	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.

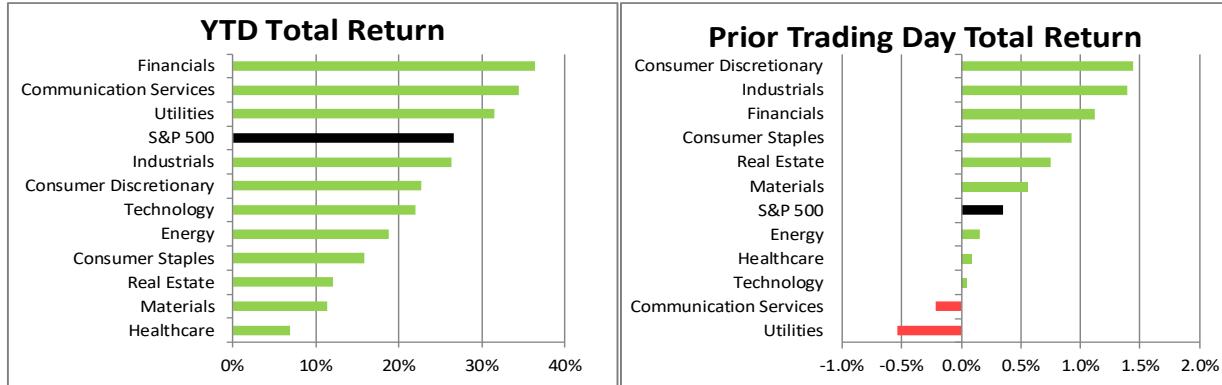|	Price	Prior	Change	Explanation
Energy Markets				
Brent	$75.16	$75.17	-0.01%	
WTI	$71.17	$71.24	-0.10%	
Natural Gas	$3.32	$3.13	6.04%	Supply Pessimism
Crack Spread	$17.10	$17.08	0.07%	
12-mo strip crack	$20.34	$20.30	0.19%	
Ethanol rack	$1.75	$1.74	0.13%	
Metals				
Gold	$2,681.04	$2,716.19	-1.29%	
Silver	$30.77	$31.35	-1.85%	
Copper contract	$416.00	$413.30	0.65%	
Grains				
Corn contract	$433.25	$435.25	-0.46%	
Wheat contract	$557.50	$564.75	-1.28%	
Soybeans contract	$987.75	$983.50	0.43%	
Shipping				
Baltic Dry Freight	1,537	1,576	-39	

Weather

The 6-to-10-day and 8-to-14-day forecasts currently call for warmer-than-normal temperatures along the West Coast and in the Desert Southwest, with cooler-than-normal temperatures in the eastern half of the country. The forecasts call for wetter-than-normal conditions along the Gulf Coast in Texas and Louisiana and in northern Montana, with dry conditions prevailing in most of the rest of the country.

There are currently no major atmospheric disturbances in the Atlantic Ocean area. We will discontinue our regular tropical storm updates once we reach the end of the Atlantic hurricane season on November 30.
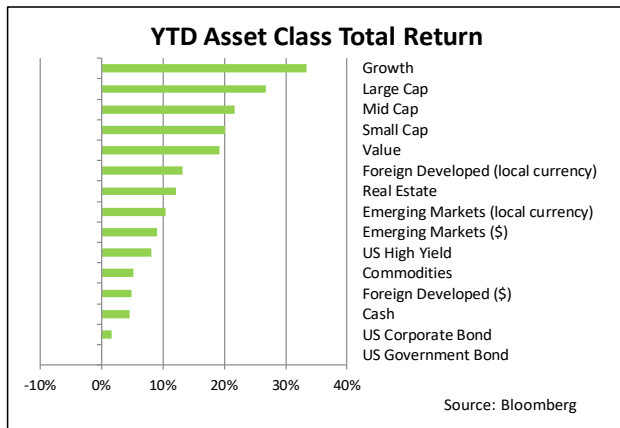
Data Section

US Equity Markets – (as of 11/22/2024 close)

YTD Total Return

Sector	Return
Financials	~36%
Communication Services	~34%
Utilities	~31%
S&P 500	~26%
Industrials	~26%
Consumer Discretionary	~22%
Technology	~21%
Energy	~18%
Consumer Staples	~15%
Real Estate	~11%
Materials	~10%
Healthcare	~7%

Prior Trading Day Total Return

Sector	Return
Consumer Discretionary	~1.4%
Industrials	~1.4%
Financials	~1.2%
Consumer Staples	~0.9%
Real Estate	~0.8%
Materials	~0.6%
S&P 500	~0.4%
Energy	~0.2%
Healthcare	~0.1%
Technology	~0.05%
Communication Services	~-0.2%
Utilities	~-0.5%

(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 11/22/2024 close)

YTD Asset Class Total Return

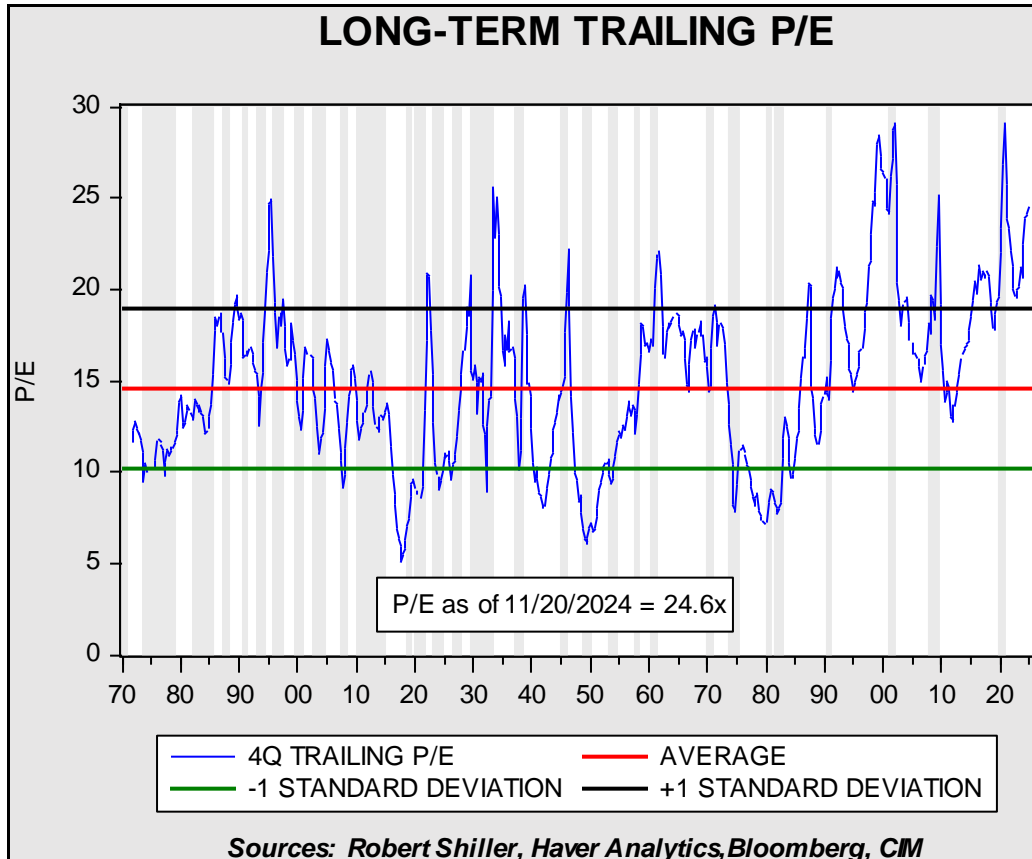| Asset Class	
Growth	
Large Cap	
Mid Cap	
Small Cap	
Value	
Foreign Developed (local currency)	
Real Estate	
Emerging Markets (local currency)	
Emerging Markets ($)	
US High Yield	
Commodities	
Foreign Developed ($)	
Cash	
US Corporate Bond	
US Government Bond	

Source: Bloomberg

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 21, 2024

LONG-TERM TRAILING P/E

P/E as of 11/20/2024 = 24.6x

Legend: 4Q TRAILING P/E — AVERAGE — -1 STANDARD DEVIATION — +1 STANDARD DEVIATION

Sources: Robert Shiller, Haver Analytics, Bloomberg, CIM

Based on our methodology,[1] the current P/E is 24.6x, up 0.1 from our last report. The increase in 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.