

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: October 25, 2024 — 9:30 AM ET] Global equity markets are mostly higher this morning. In Europe, the Euro Stoxx 50 closed down 0.1% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed up 0.3%. Chinese markets were higher, with the Shanghai Composite up 0.6% from its previous close and the Shenzhen Composite up 1.9%. US equity index futures are signaling a higher open.

With 178 companies having reported so far, S&P 500 earnings for Q3 are running at \$60.50 per share, compared to estimates of \$60.44, which is up 4.2% from Q3 2023. Of the companies that have reported thus far, 74.7% have exceeded expectations while 16.9% 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 emphasized in bold:

- [Bi-Weekly Geopolitical Report](#) (10/21/2024) (with associated [podcast](#)): “Israel’s Pager Caper and Supply Chain Security”
- [Asset Allocation Bi-Weekly](#) (10/14/2024) (with associated [podcast](#)): “The Yield Curve Un-Inverts”
- [Asset Allocation Quarterly – Q4 2024](#) (10/22/2024): Discussion of our asset allocation process, Q4 2024 portfolio changes, and our outlook for the markets.

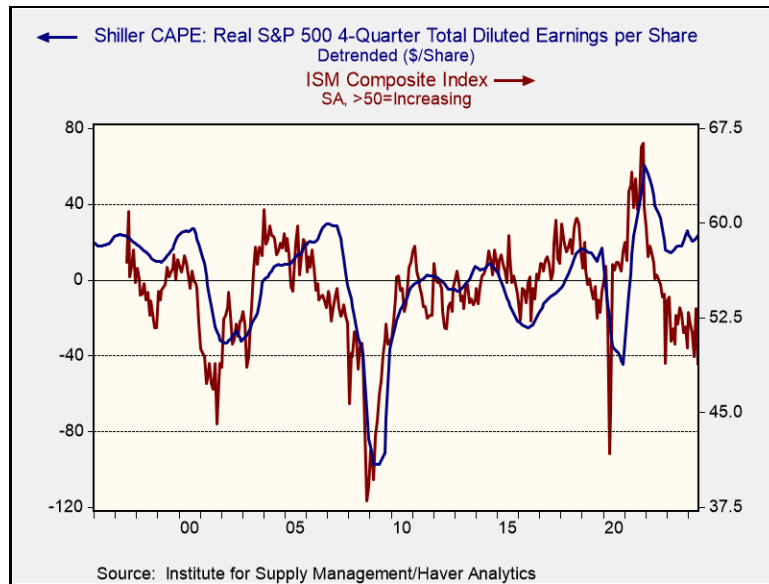
Good morning! The market is eagerly awaiting the latest University of Michigan survey data to assess consumer sentiment ahead of the election. In sports news, the New York Yankees are set to take on the Los Angeles Dodgers in the first game of the World Series. Today’s *Comment* will explore what the strong October Purchasing Managers’ Index (PMI) indicates about corporate earnings. Next, we will provide an update on US chip production, followed by a discussion of Canada’s new immigration policy. As usual, our report will conclude with a roundup of international and domestic data releases.

US Shows Resilience: The latest S&P Global survey suggests that the economy is off to a robust start this quarter, indicating the potential for stable earnings growth.

- [The October flash index showed an increase in business activity](#), with the composite PMI rising from 54.0 to 54.3. The services sector remained a key driver of the economy, while manufacturing continued to lag. Notably, firms raised prices for goods and services at the slowest pace in nearly 4.5 years. However, the employment component pointed to a

slowdown in hiring for the third consecutive month. Despite weakness in exports, firms saw a sharp increase in new business, driven largely by strong domestic demand.

- The strong PMI data is a positive indicator for S&P earnings. As the accompanying chart demonstrates, [a correlation exists between rising PMI values and improving corporate profitability](#). This relationship is likely due to the survey's comprehensive tracking of key business metrics, including new orders, input and output prices, inventory levels, and overall business activity, which provides a valuable snapshot of the operational health of firms. As a result, the PMI has often been a good indicator when tracking the momentum of future corporate earnings.

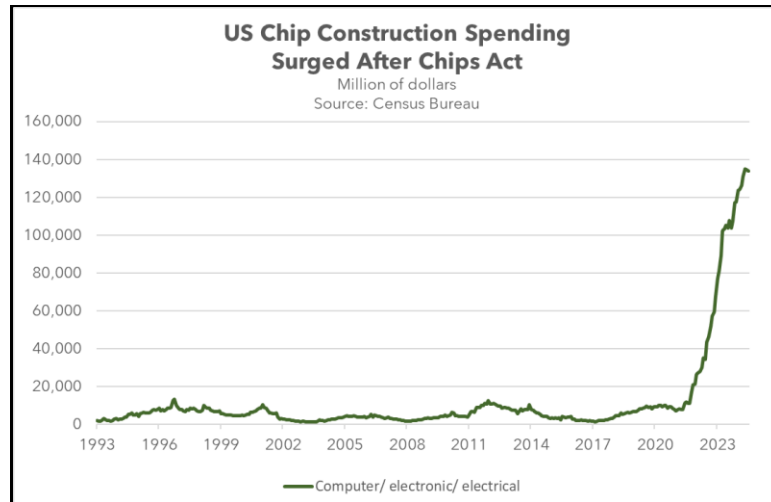


- While the sideways movement in the index suggests that the economy is solidly in expansion, it also signals that significant earnings growth is unlikely in the near term. Nonetheless, this environment favors high-quality stocks with strong profitability and low debt levels, as they are better positioned to deliver sustainable dividends to investors. However, as confidence in a soft landing strengthens and the Fed begins to lower interest rates, we anticipate investors becoming more willing to take on risk.

US Chip Power: Taiwan Semiconductor Manufacturing Co (TSMC) has achieved a significant milestone at its US-based facility, bringing the United States one step closer to domestic chip manufacturing capabilities.

- [TSMC's Arizona plant has surpassed expectations](#), achieving production yields 4% higher than comparable facilities in Taiwan. This achievement, accomplished despite overcoming challenges such as labor disputes and construction delays, is a promising sign for US semiconductor independence. As the primary chip provider for Nvidia and Apple, TSMC's increased domestic production capacity strengthens the company's case for further government support under the CHIPS and Science Act. The company is expected to receive \$6.6 billion in grants under this legislation.

- The expansion of semiconductor manufacturing hubs is at its most robust level in nearly half a century. Investments in facilities dedicated to computer, electronics, and electrical manufacturing now account for nearly 60% of total US construction spending, a significant increase from the approximately 8% share observed a decade ago. The new facilities are expected to [triple the US's chipmaking capacity by 2032](#), elevating its market share from 10% to 14% of global chip production. As a result, the US is better suited to be able to meet its growing demand for chips as it looks to dominate the AI space.

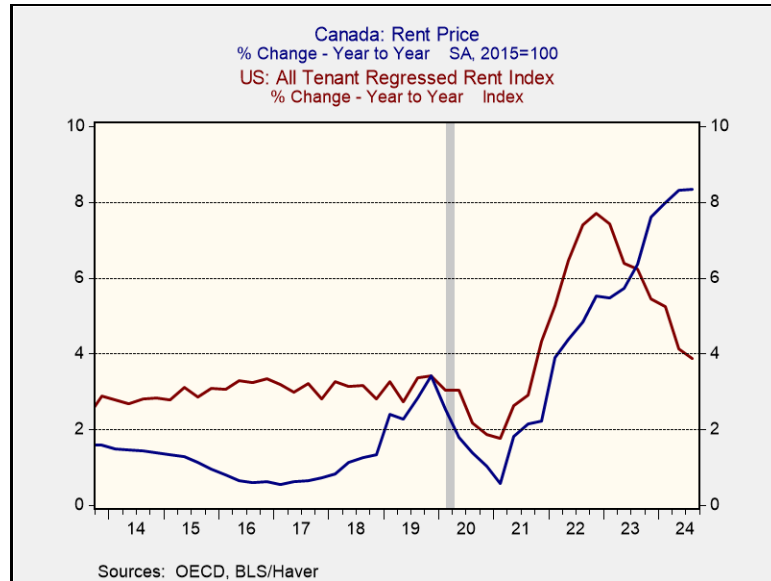


- The development of domestic semiconductor fabrication plants is likely to continue for national security reasons, but their long-term viability may be a concern if firms cannot significantly reduce costs. It has been widely speculated that firms may rely heavily on automation in these new facilities to maintain profitability. However, this could lead to pushback from lawmakers who want firms receiving funding to increase hiring for manufacturing workers. While we do not currently see this as a significant issue, it could become a potential problem in the future.

Canada Immigration Crackdown: Although the increase in foreign workers has bolstered the country’s economy, concerns over the rising costs of living have prompted a reassessment of immigration policy.

- On Thursday, [the country released its Immigration Levels Plan](#), which aims to reduce the number of permanent residents by 20% by 2025. The new restrictions will cap the number of immigrants, leading to a contraction in the overall population over the next two years. Moderate growth is expected to resume in the third year. This policy change comes amid a growing backlash against the country's immigration policies, which have [allowed over 2.35 million people to immigrate since mid-2022](#), roughly the population of Houston.
- The surge in immigration has contributed to economic overheating, with rental inflation being a particular concern. Despite moderation in other areas and a decline in overall

inflation, rental inflation has continued to accelerate, rising over 8% in Q3 2024 from the previous year. However, immigration has also helped boost Canada's economic growth to [match that of the US, at just over 2% per year over the past decade](#). As a result, there is an expectation that the restrictions could also slow the overall economy.



- The economic impact of immigration restrictions will depend largely on their effect on labor productivity. A significant increase in the labor supply can sometimes lead firms to become less inclined to adopt new technologies and improve their processes, which could potentially offset some of the production gaps caused by labor shortages. However, we believe that Canadian financial assets may benefit from the potential boost to consumer sentiment and spending resulting from these restrictions. Therefore, we maintain a cautiously optimistic outlook for the country.

In Other News: Cleveland Fed President [Beth Hammack has reiterated that the central bank has more work to do before declaring victory](#) over inflation, further indicating that many Fed officials favor a gradual approach to interest rate cuts. Meanwhile, [new home sales increased in September as prospective buyers](#) took advantage of the drop in mortgage rates. Russian President Vladimir Putin's [ambiguous explanation for the presence of North Korean troops in Russia](#) suggests that he may be using the additional manpower to demonstrate his willingness to escalate the conflict in Ukraine.

US Economic Releases

September *durable goods* orders fell by a seasonally adjusted 0.8%, slightly stronger than the expected drop of 1.0% but matching the value for the previous month. Durable goods orders are often driven by transportation equipment, where just a few airliner orders can have a big impact. September *durable goods orders excluding transportation* rose 0.4%, slightly exceeding the expected drop of 0.1% but slightly cooler than the previous month's gain of 0.6%. Finally, the

durable goods report also includes a key proxy for corporate capital investment. In September, *nondefense capital goods orders ex-aircraft* rose 0.5%, again slightly exceeding the expected gain of 0.1%. Compared with the same month one year earlier, overall durable goods orders in September fell 3.0%, while durable orders ex-transport rose 0.6%. 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 economic releases or Fed events scheduled for the rest of the day.

Economic Releases						
ET	Indicator			Expected	Prior	Rating
10:00	U. of Michigan Consumer Sentiment	m/m	Oct F	69.1	68.9	***
10:00	U. of Michigan Current Conditions	m/m	Oct F		62.7	**
10:00	U. of Michigan Future Expectations	m/m	Oct F		72.9	**
10:00	U. of Michigan 1-Year Inflation Expectation	m/m	Oct F	2.9%	2.9%	*
10:00	U. of Michigan 5-10 Year Inflation Expectation	m/m	Oct F	3.0%	3.0%	*
11:00	Kansas City Fed Services Activity	m/m	Oct		-2	*
Federal Reserve						
11:00	Susan Collins Speaks in Fireside Chat				President of the Federal Reserve Bank of Boston	

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	Tokyo CPI	y/y	Oct	1.8%	2.2%	1.8%	**	Equity and bond neutral
	Tokyo CPI Ex-Fresh Food	y/y	Oct	1.8%	2.0%	1.7%	***	Equity and bond neutral
	Tokyo CPI Ex-Fresh Food & Energy	y/y	Oct	1.8%	1.6%	1.6%	*	Equity and bond neutral
	PPI Services	y/y	Sep	2.6%	2.7%	2.7%	*	Equity and bond neutral
	Coincident Index	y/y	Aug F	114.0	113.5		*	Equity and bond neutral
	Leading Economic Index	m/m	Aug F	106.9	106.7		**	Equity and bond neutral
	Nationwide Dept Sales	y/y	Sep	2.3%	3.9%		***	Equity and bond neutral
New Zealand	ANZ Consumer Confidence Index	m/m	Oct	91.2	95.1		*	Equity and bond neutral
EUROPE								
Eurozone	M3 Money Supply	y/y	Sep	3.2%	2.9%	2.9%	***	Equity and bond neutral
Germany	IFO Business Climate	m/m	Oct	86.5	85.4	85.6	***	Equity and bond neutral
	IFO Current Assessment	m/m	Oct	85.7	84.4	84.4	**	Equity and bond neutral
	IFO Expectations	m/m	Oct	87.3	86.4	87.0	**	Equity and bond neutral
France	Consumer Confidence	m/m	Oct	94.0	95.0	95.0	***	Equity bearish, bond bullish
Italy	Consumer Confidence	m/m	Oct	97.4	98.3	98.5	***	Equity bearish, bond bullish
	Manufacturing Confidence	m/m	Oct	85.8	83.6	87.0	***	Equity bearish, bond bullish
	Economic Sentiment	m/m	Oct	93.4	95.6		**	Equity and bond neutral
UK	GfK Consumer Confidence	m/m	Oct	-21	-20	-20	***	Equity bearish, bond bullish
Russia	Gold and Forex Reserves	m/m	18-Oct	\$624.9b	\$622.3b		***	Equity and bond neutral
	Money Supply, Narrow Definition	w/w	18-Oct	18.47t	18.43t		*	Equity and bond neutral
AMERICAS								
Brazil	FGV Consumer Confidence	m/m	Oct	93	93.7		*	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)	448	449	-1	Down
U.S. Sibor/OIS spread (bps)	460	461	-1	Down
U.S. Libor/OIS spread (bps)	456	456	0	Down
10-yr T-note (%)	4.19	4.21	-0.02	Up
Euribor/OIS spread (bps)	307	309	-2	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 Russia Key Rate	21.000%	19.000%	20.000%	Above Forecast
PBOC 1-Year Med-Term Lending (Bil.)	700.0b	300.0b	600.0b	Above 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	\$75.01	\$74.38	0.85%	
WTI	\$70.85	\$70.19	0.94%	
Natural Gas	\$2.53	\$2.52	0.40%	
12-mo strip crack	\$19.82	\$19.92	-0.52%	
Ethanol rack	\$1.73	\$1.73	-0.02%	
Metals				
Gold	\$2,727.08	\$2,736.17	-0.33%	
Silver	\$33.34	\$33.68	-1.03%	
Copper contract	\$433.40	\$435.15	-0.40%	
Grains				
Corn contract	\$417.75	\$421.50	-0.89%	
Wheat contract	\$573.50	\$581.50	-1.38%	
Soybeans contract	\$996.75	\$1,005.00	-0.82%	
Shipping				
Baltic Dry Freight	1,417	1,445	-28	
DOE Inventory Report				
	Actual	Expected	Difference	
Crude (mb)	5.47	1.00	4.47	
Gasoline (mb)	0.88	-1.90	2.78	
Distillates (mb)	-1.14	-1.01	-0.14	
Refinery run rates (%)	1.8%	-0.2%	2.0%	
Natural gas (bcf)	80	65	15	

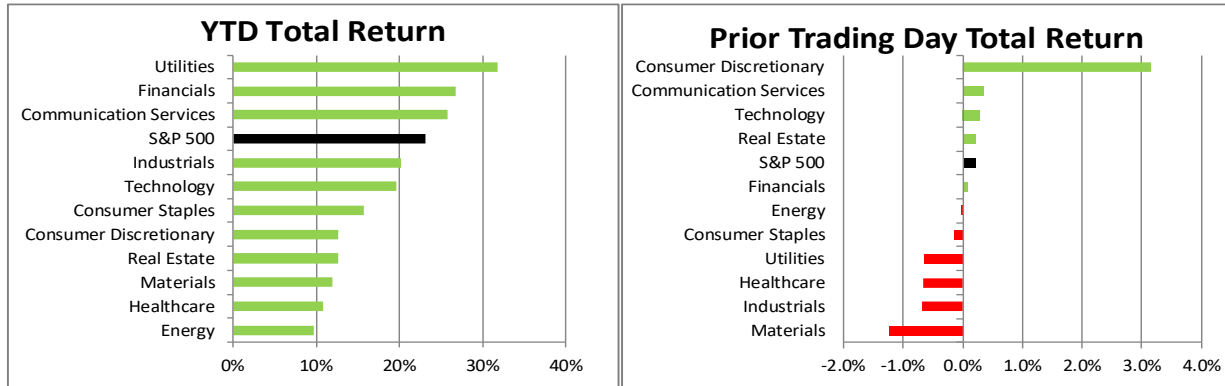
Weather

The 6-to-10-day and 8-to-14-day forecasts currently call for warmer-than-normal temperatures from the Great Plains eastward, with near-normal temperatures from the Rocky Mountains westward. The forecasts call for wetter-than-normal conditions in the Rocky Mountains, the Great Plains, the Mississippi Valley, and Florida, with near normal conditions for the rest of the country.

There are currently no tropical disturbances in the Atlantic basin.

Data Section

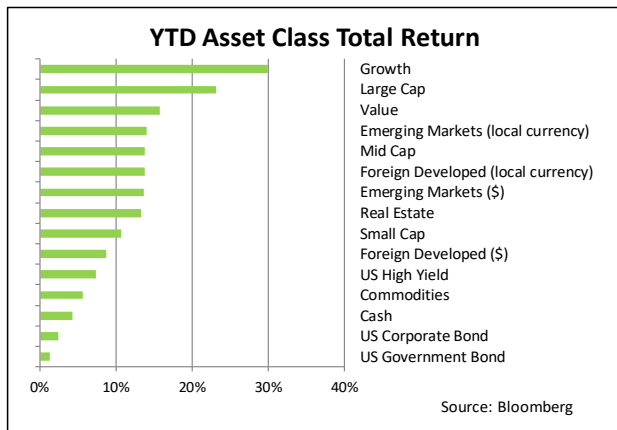
US Equity Markets – (as of 10/24/2024 close)



(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 10/24/2024 close)

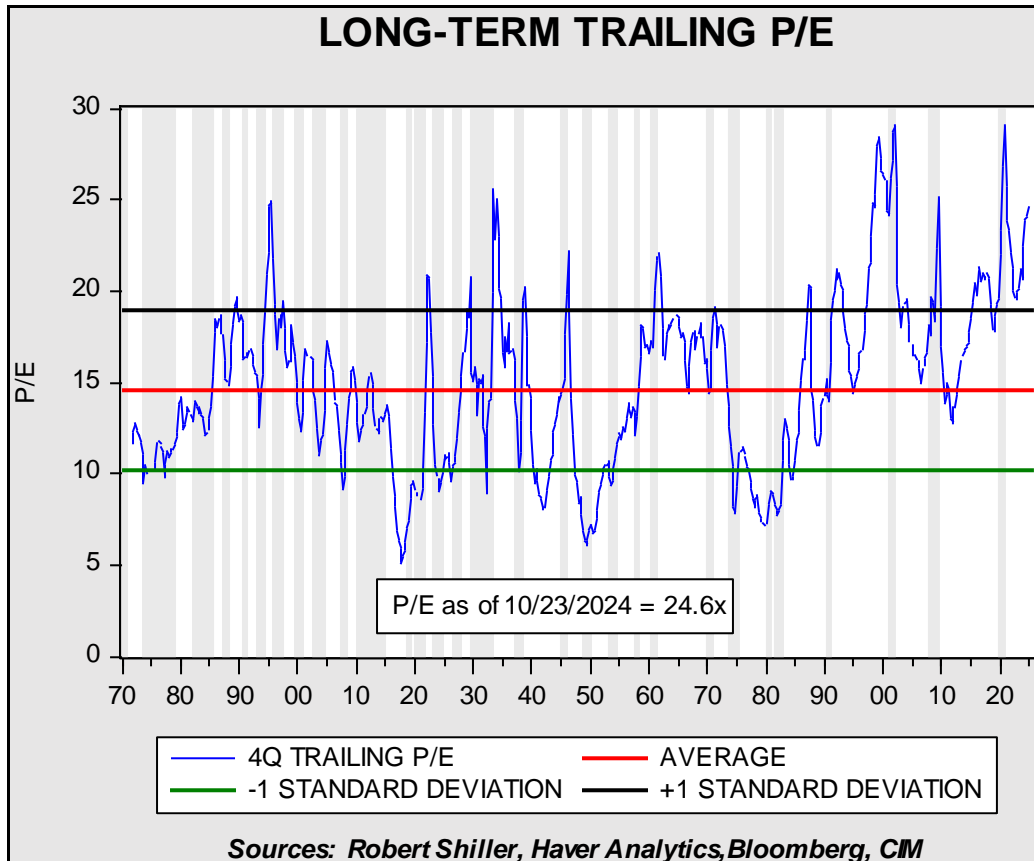


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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

October 24, 2024



Based on our methodology,¹ the current P/E is 24.6x, unchanged from our last report. The stock price index increase was offset by an increase in 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 (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.