Daily Comment

By Patrick Fearon-Hernandez, CFA, and Thomas Wash

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 2, 2024 — 9:30 AM ET] Global equity markets are mixed 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 up 2.4%. Chinese markets are closed for Golden Week. US equity index futures are signaling a lower 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:

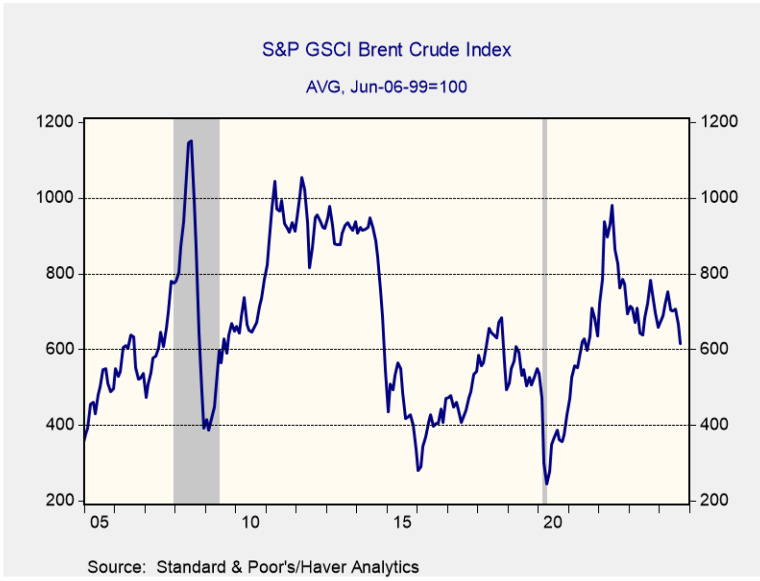
- *Bi-Weekly Geopolitical Report* (9/23/2024) (with associated podcast): "Eight Megatrends Every Investor Should Know"
- *Asset Allocation Bi-Weekly* (9/30/2024) (with associated podcast): "Presidential Cycles and Stock Performance"
- *Asset Allocation Quarterly – Q3 2024* (7/16/2024): Discussion of our asset allocation process, Q3 2024 portfolio changes, and our outlook for the markets.
- *Asset Allocation Q3 2024 Rebalance Presentation* (8/6/2024): Video presentation featuring the Asset Allocation Committee as they review the asset allocation strategies, recent portfolio changes, and the current macro environment.
- *Confluence of Ideas podcast* (9/11/2024) "Reviewing the Asset Allocation Rebalance: Q3 2024"
- *Fixed Income Quarterly* (September 2024)

Good morning! Markets are still grappling with the ongoing Middle Eastern conflict. Today's *Comment* will analyze the escalating Israel-Iran tensions, explore the reasons behind the positive surprise from JOLTS, and provide our perspective on the recent vice presidential debate. Finally, we'll conclude with a roundup of key domestic and international economic data.

Israel-Iran: The two countries have launched attacks against one another in a sign that tensions in the Middle East are rising.

- Iran launched a massive barrage of 180 ballistic missiles against Israel on Tuesday, hours after the White House issued a stern warning about potential Iranian retaliation for a ground incursion into Lebanon. While most of the missiles were intercepted, the recent rocket launches penetrated farther into Israeli territory and came with less warning than the previous attack in April. So far, there is uncertainty as to whether tensions will escalate further, with Israeli Prime Minister Benjamin Netanyahu vowing that Iran "will pay" for the attack and Iran insisting that it is not interested in a broader war.

- The recent attack on Israel has triggered a sharp spike in oil prices, with Brent crude climbing above $75 a barrel — a level not seen since August. While the immediate impact of the attack is clear, the longer-term price trajectory remains less certain. Before the incident, the two warring factions in Libya agreed to a compromise, paving the way for a resumption of oil exports. Meanwhile, the Saudi-led OPEC+ alliance is scheduled to convene today to discuss increasing its production target. As a result, the potential increase in supply is likely to keep oil prices in check.



- The extent to which the conflict escalates will significantly influence oil prices. A broader war, involving Israeli strikes on Iranian oil infrastructure or an Iranian blockade of the Strait of Hormuz, could drive crude prices substantially higher. Currently, there is no indication that either side is seeking a major escalation. The US and its allies are actively working to de-escalate the situation. However, Israel's recent denial of entry to UN Secretary-General António Guterres has raised concerns about its willingness to reduce tensions.

Job's Surprise: Job openings surged in August; however, there are still signs that the labor market is cooling.

- The Job Openings and Labor Turnover Survey (JOLTS) revealed a surge in job openings in August, reaching a three-month high of 8.04 million. This uptick was primarily fueled by increased openings in construction and state and local government sectors. Despite the rise in available positions, concerns persist regarding labor demand. Hiring rates dipped to 3.3%, equaling their lowest point since the pandemic began. The number of job openings to the number of unemployed ratio was held to a three-year low of 1.1, down from the post-pandemic peak of 2.0 and slightly below the pre-pandemic ratio of 1.2.
- The mixed JOLTS report has muddied the waters on the labor market's true health. The rise in construction jobs was likely fueled by lower interest rates, reflecting expectations

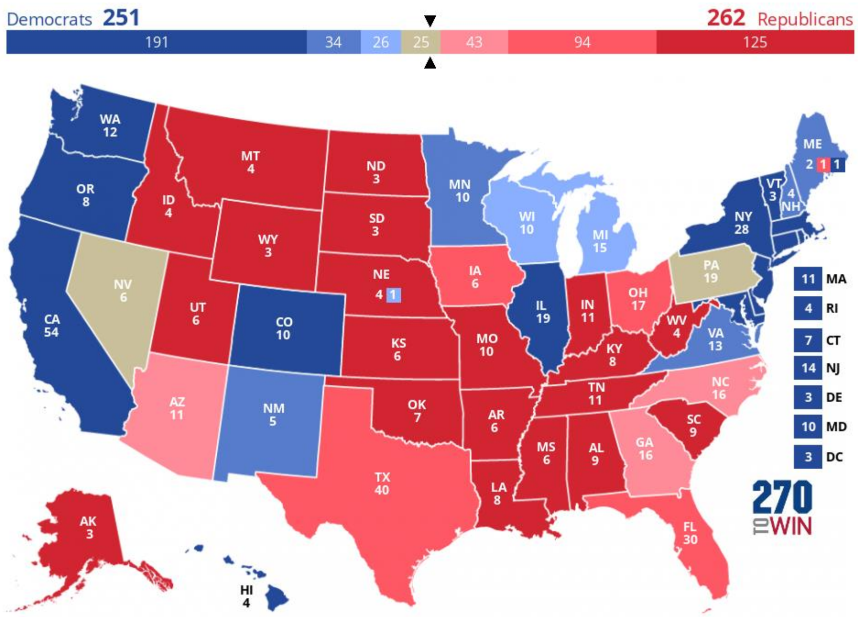
of Fed cuts. The 10-year Treasury yield declined by nearly 50 basis points from early July to late August. Although this did not lead to an increase in construction spending, there was a noticeable rise in activity, particularly in housing starts. However, sectors less sensitive to interest rate changes, such as retail trade and transportation, experienced noticeable declines, which is likely to reinforce concerns that hiring is cooling.

- The size and timing of the Fed's next rate cut will be heavily influenced by the jobs report, which will be released on Friday. While the JOLTS report was broadly positive, other surveys released last month have predominantly flashed warning signs that the labor market is cooling. If the BLS jobs report shows a slowdown in job creation or another uptick in the unemployment rate, Fed officials may seek to adjust policy to ensure that they do not lose control over the maximum employment mandate.

Vice Presidential Debate: The contest between the two vice-presidential candidates may not have produced sound bites, but it offered both sides a strong platform to share their visions for the country.

- During the debate, both sides tried to highlight the qualifications of their respective presidential candidates. Senator JD Vance argued that former President Donald Trump helped to lower inflation to 1.5% and increase take-home pay for American families while he was in office. Meanwhile, Minnesota Governor Tim Walz argued that Vice President Kamala Harris had helped lower insulin prices and had passed much-needed infrastructure legislation. Neither candidate made a significant impact, but they did not make any major mistakes either.
- With 33 days remaining until the election, there doesn't appear to be a clear front-runner, which is different from previous election cycles. In the last election, President Joe Biden was considered the comfortable favorite to win the presidency and enjoyed very

favorable polling. However, this year, the polls have tightened considerably, [with Harris trailing broadly across swing states](), according to data collected by Real Clear Politics.



(Source: www.270towin.com and Polymarket)

- While Ohio Senator JD Vance appeared the most poised and composed during the debate, the lack of viral moments may render the contest inconsequential to the election. According to our current electoral forecast, based on betting odds, the election is likely to be a toss-up, potentially coming down to Pennsylvania. Betting odds slightly favor Harris, although polling shows an advantage in the other direction. It's important to note that the president's impact on financial markets is not as significant as that of the legislative branch, with betting odds currently favoring a split Congress.

In Other News: French Prime Minister Michel Barnier has proposed raising taxes to address the country's debt, indicating a move towards unpopular measures. At the same time, dockworkers in the US have gone on strike, which could potentially disrupt US supply chains. Additionally, UK Prime Minister Keir Starmer is heading to Brussels to help improve relations with the EU as the two sides seek to secure deals on defense and food.

US Economic Releases

The Mortgage Bankers Association today said ***mortgage applications*** in the week ended September 27 fell 1.3%, compared to last week's gain of 11.0%, interrupting what had been a robust positive trend. Applications for home purchase mortgages rose 0.7%, while applications for refinancing mortgages fell 2.9%, after rising 20.3% the prior week. According to the report, the average interest rate on a 30-year mortgage rose one basis point to 6.14%. While the pace of home purchase mortgages has held relatively steady, the refinancing pace has shown signs of being sensitive to changes in rates.

The following table lists the economic releases or Fed events scheduled for the rest of the day.

Economic Releases		
No economic releases for the rest of today		
Federal Reserve		
ET	**Speaker or Event**	**District or Position**
9:00	Beth Hammack Gives Welcome Remarks	President of the Federal Reserve Bank of Cleveland
10:05	Alberto Musalem Gives Welcoming Remarks	President of the Federal Reserve Bank of St. Louis
11:00	Michelle Bowman Speaks on Community Banking	Member of the Board of Governors
12:15	Thomas Barkin Speaks on Economy	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	Monetary Base	y/y	Sep	-0.1%	0.6%	--	**	Equity bearish, bond bullish
	Monetary Base, End of Period	m/m	Sep	¥673.5t	¥674.9t	--	*	Equity and bond neutral
	Consumer Confidence Index	m/m	Sep	36.9	36.7	37	*	Equity and bond neutral
South Korea	CPI	y/y	Sep	1.6%	2.0%	1.9%	***	Equity and bond neutral
	S&P Global South Korea PMI Manufacturing	m/m	Sep	48.3	51.9	--	***	Equity bearish, bond bullish
EUROPE								
Eurozone	Unemployment Rate	m/m	Aug	6.4%	6.4%	6.4%	**	Equity and bond neutral
Italy	Unemployment Rate	m/m	Aug	6.2%	6.4%	6.5%	**	Equity and bond neutral
AMERICAS								
Canada	S&P Global Canada Manufacturing PMI	m/m	Sep	50.4	49.5	--	***	Equity bullish, bond bearish
Mexico	Gross Fixed Investment	y/y	Jul	6.4%	-1.1%	4.8%	**	Equity bullish, bond bearish
	Vehicle Domestic Sales	y/y	Sep	116543	127684	--	***	Equity and bond neutral
Brazil	S&P Global Brazil Manufacturing PMI	m/m	Sep	53.2	50.4	--	***	Equity bullish, bond bearish
	Industrial Production	y/y	Aug	2.2%	6.1%	2.2%	***	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)	449	446	3	Down
U.S. Sibor/OIS spread (bps)	460	462	-2	Down
U.S. Libor/OIS spread (bps)	457	458	-1	Down
10-yr T-note (%)	3.78	3.73	0.05	Down
Euribor/OIS spread (bps)	325	328	-3	Down
Currencies	**Direction**			
Dollar	Flat			Down
Euro	Flat			Up
Yen	Down			Up
Pound	Flat			Up
Franc	Down			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	$75.59	$73.56	2.76%	
WTI	$71.98	$69.83	3.08%	
Natural Gas	$2.97	$2.90	2.59%	
12-mo strip crack	$19.41	$19.42	-0.08%	
Ethanol rack	$1.82	$1.81	0.45%	
Metals				
Gold	$2,649.43	$2,663.23	-0.52%	
Silver	$31.46	$31.46	0.01%	
Copper contract	$461.40	$458.90	0.54%	
Grains				
Corn contract	$431.00	$429.00	0.47%	
Wheat contract	$604.50	$599.00	0.92%	
Soybeans contract	$1,047.75	$1,057.25	-0.90%	
Shipping				
Baltic Dry Freight	2,030	2,084	-54	
DOE Inventory Report				
	Actual	**Expected**	**Difference**	
Crude (mb)		-1.43		
Gasoline (mb)		0.20		
Distillates (mb)		-2.00		
Refinery run rates (%)		-0.7%		
Natural gas (bcf)				

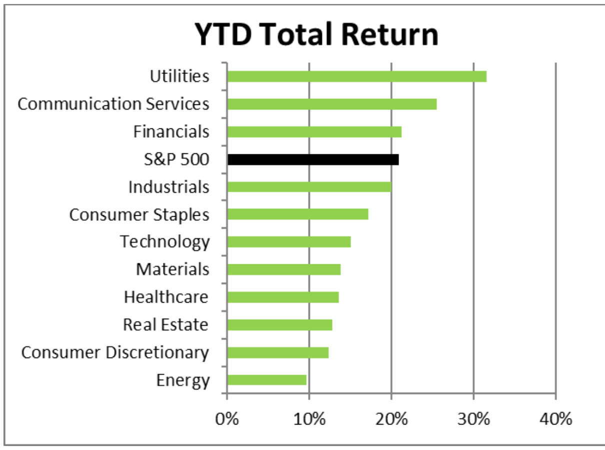
Weather

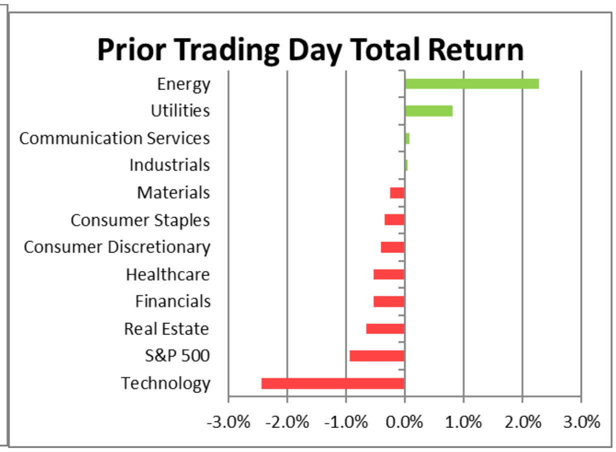
The 6-to-10-day and 8-to-14-day forecasts currently call for warmer-than-normal temperatures in Florida and from the Great Lakes and Mississippi River westward, with a pocket of colder-than-normal temperature in the Mid-Atlantic coastal region. The forecasts call for wetter-than-normal conditions in Florida, with dry conditions prevailing in most of the rest of the country.

Several hundred miles west of the Cape Verde islands, Tropical Storm Kirk is charting a northwesterly course well-distant from land. Meanwhile, just south of the Cape Verdes, a tropical depression is showing a 90% chance of cyclonic formation.

Data Section

US Equity Markets – (as of 10/1/2024 close)

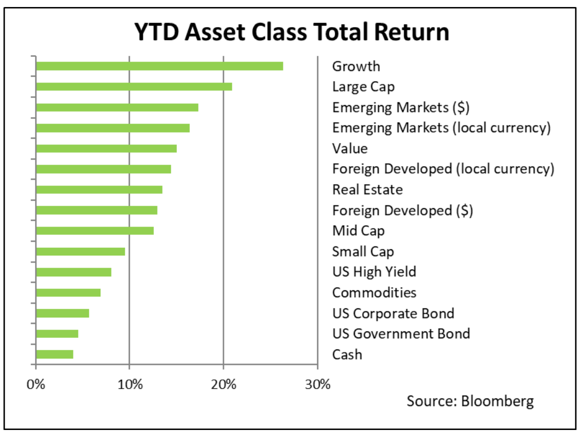




(Source: Bloomberg)

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 10/1/2024 close)

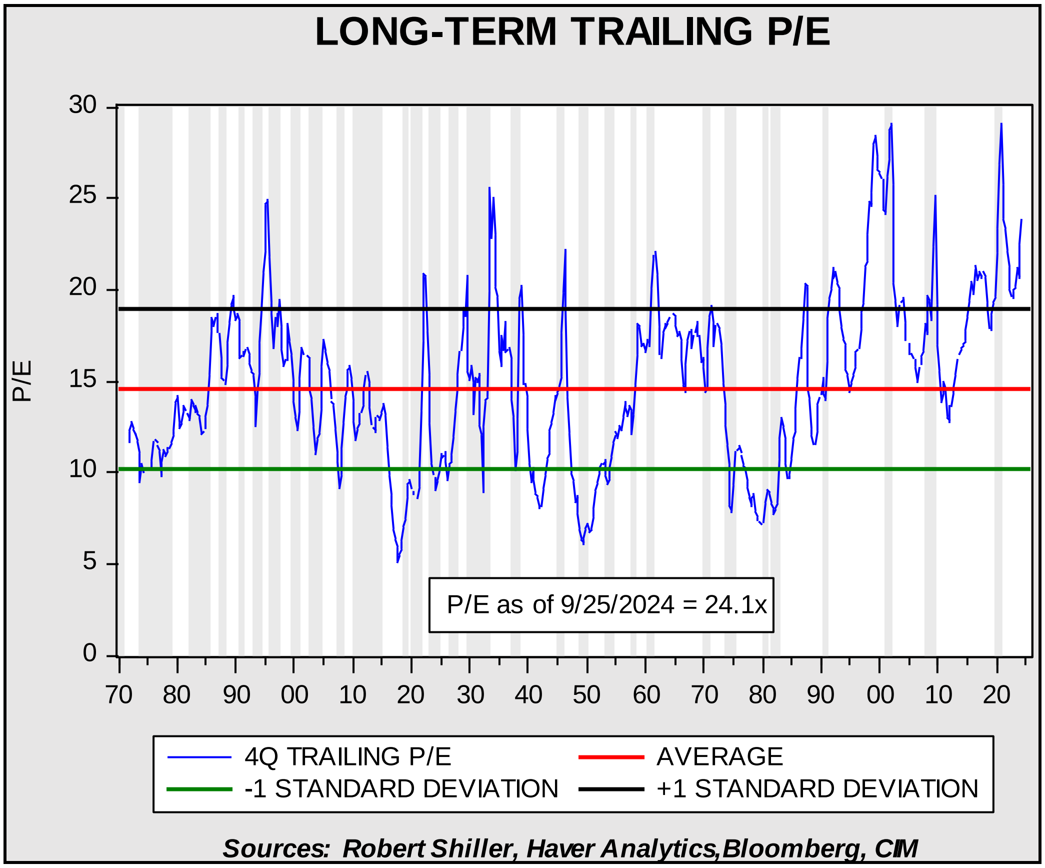


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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

September 26, 2024



Based on our methodology,[1] the current P/E is 24.1x, unchanged from our last report. The stock price index improved slightly, while earnings were little changed from the previous week.

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 (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.