

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: September 18, 2024 — 9:30 AM ET] Global equity markets are mixed this morning. In Europe, the Euro Stoxx 50 is down 0.4% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed down 0.5%. Chinese markets were mixed, with the Shanghai Composite up 0.5% from its previous close and the Shenzhen Composite down 0.2%. 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](#) (9/9/2024) (with associated [podcast](#)): “Prospects for the Dollar in a Fracturing World”
- [Asset Allocation Bi-Weekly](#) (9/16/2024) (with associated [podcast](#)): “The Benjamin Button Dividend”
- [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”

Good morning! The market is eagerly anticipating the Federal Reserve's upcoming rate decision. In sports news, Bayern Munich set a new Champions League record for most goals by a single team with a nine-goal victory over Dinamo Zagreb. Today's *Comment* will explore our thoughts on the Fed's anticipated rate cut later today, the potential implications of the ongoing dockworker labor dispute, and the Brazilian central bank's widely expected U-turn. Finally, we'll round out our report with a review of the latest economic data.

Inflation to Unemployment: While the market is focused on the size of today's rate cut, it should also pay close attention to the summary of economic projections, which will outline the future path of interest rates.

- Market expectations for a significant interest rate cut have surged, with the probability of [a 50 bps reduction rising from 34% to over 60% since last Tuesday](#). This shift has been largely driven by former New York Fed President William Dudley's editorial, in which he expressed [optimism that the Fed will take bold action](#) at its next meeting to address labor market challenges. Prior to the July meeting, [he pushed the central bank to cut rates](#), and although the FOMC opted against it, the minutes of the meeting revealed that some [members would have supported such a move](#).

- The decision to implement rate cuts now, rather than at a later time, reflects less of the central bank's stance on inflation and more of its growing concern about the cooling labor market. These two economic indicators have been moving in opposite directions. While core inflation has decreased from 3.9% to 3.2% since the start of the year, the unemployment rate has risen from 3.7% to 4.2%. Consequently, for the first time since 2021, the unemployment rate now exceeds the inflation rate, reinforcing the view that its mandate of price stability and maximum unemployment is balanced.

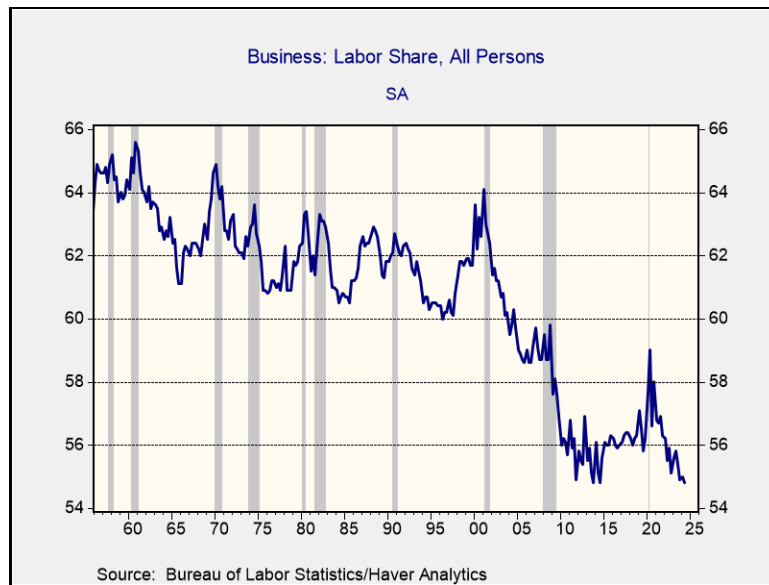


- The Federal Reserve is expected to take a nuanced approach at its upcoming meeting, as plans to implement its first rate cut with the release of its eagerly anticipated economic projections. A 50 bps rate cut today would likely prompt the Fed to express a cautious outlook for future rate reductions. Conversely, a 25 bps cut could encourage officials to signal a willingness to take more aggressive action if needed in the future. However, market sentiment could deteriorate if investors perceive that the Fed is not committed to cutting rates to safeguard the economy.

Labor Strikes Back: Just weeks before the election, the dockworkers' unions are ready to strike in an effort to secure a better labor contract.

- The White House has announced that [it will not invoke federal legislation to prevent a potential strike by dockworkers](#) on the East and Gulf Coasts if a labor agreement is not reached by the October 1 deadline. While the US president has the authority to intervene in labor disputes deemed a threat to national security, the administration has chosen not to exercise that power in this instance. Given that over half of US-bound cargo passes through these ports, a strike could significantly disrupt supply chains nationwide and could become a political issue.
- The decision not to intervene in the labor dispute indicates that the administration is keen to avoid actions that could be perceived as anti-union. Since the pandemic, support for labor unions has increased as a tight labor market has compelled employers to offer higher wages to attract and retain workers. This has bolstered the bargaining power of

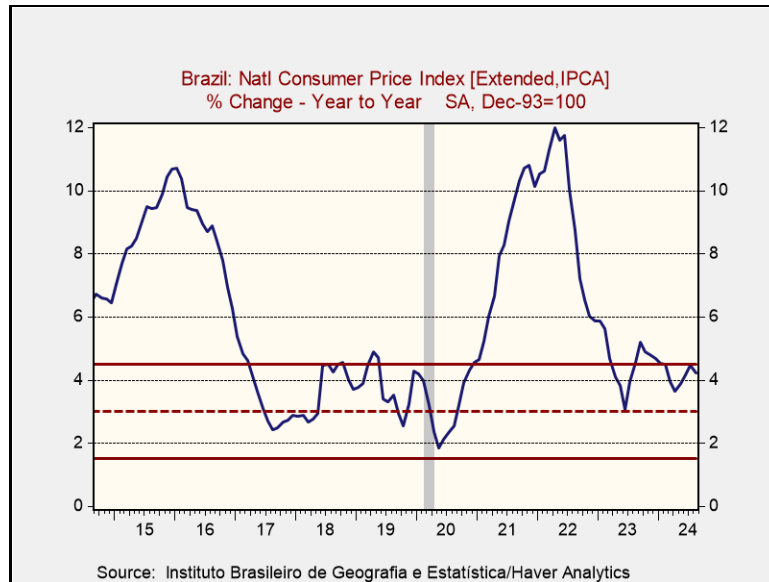
unions as they push for greater concessions. The dockworkers' labor dispute appears to have reached an impasse over wage increases, with union leaders [demanding a 77% pay raise](#), and a [ban on automated cranes, gates, and container movements](#).



- A strike could disrupt supply chains and raise prices, but a more critical long-term concern is the potential slowdown in technological adoption. After the pandemic, workers initially gained a larger share of company earnings, but their shares sharply declined as the economy reopened. While increased immigration played a role, the rise of AI technology also contributed. The recent dispute suggests that technology could become an increasingly political issue in the coming years, especially if firms use it to offset rising labor costs.

Brazil Turns Hawkish: After being one of the first major economies to implement rate cuts, the central bank of Brazil appears to be on track to undo some of those measures later today.

- [Brazil's central bank is expected to raise its benchmark policy rate by 25 basis points](#) to 10.75% on Wednesday. The decision comes as the central bank looks to establish its independence after [previous criticism from President Luiz Lula da Silva](#). Since taking office, Lula has increased public spending, particularly on social programs, raising concerns that the resulting debt could fuel inflation. His chosen successor to take over the central bank, Gabriel Galípolo, has also adopted a hawkish stance, [pledging to take whatever steps are necessary to curb inflation](#).
- The decision to tighten monetary policy reflects the Brazilian economy's signs of overheating. In the second quarter, the economy expanded at an annualized rate of 5.9% — the fastest pace since late 2020. This robust growth coincides with a persistently tight labor market, where the unemployment rate remains near 20-year lows. The combination of strong growth and low unemployment has likely contributed to a rise in overall inflation, which is currently above the central bank's [target rate of 3%, and risks exceeding the tolerance range of 4.5%](#).



- The central bank's anticipated rate hike should serve as a warning about the dangers of excessive interest rate cuts, particularly if the country fails to rein in its spending. While we do not foresee other central banks adopting a more hawkish stance in the near term, a resurgence of inflation could force central bankers to pause and reverse earlier rate cuts to contain price pressures. Should the central bank of Brazil raise interest rates as expected, the country's currency is likely to appreciate relative to its peers.

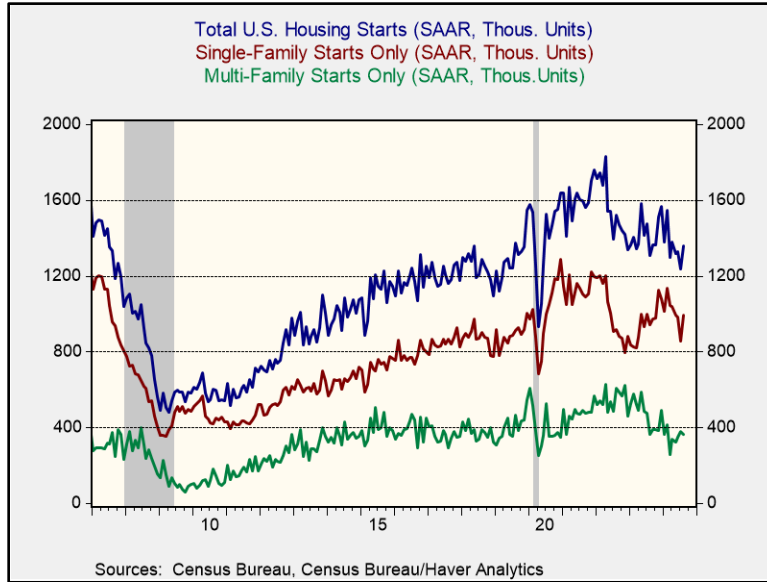
In Other News: Republican presidential candidate Donald Trump has [pledged to restore SALT](#) if elected to a second term, aiming to appeal to high-income suburban voters. Meanwhile, [Nippon Steel's merger plans gained momentum](#) as the Biden administration extended its bid for US Steel, despite delays due to national security concerns and bipartisan opposition. In another development, [Google successfully appealed its 1.5 billion EUR \(\\$1.67 billion\) competition fine](#), signaling that big tech may be able to fend off further regulatory crackdowns.

US Economic Releases

In likely anticipation of a Fed rate cut today, the Mortgage Bankers Association said **mortgage applications** in the week ended September 14 rose 14.2%, compared to last week's gain of 1.4%. Applications for home purchase mortgages rose 5.4%, compared to the prior week's 1.8%, and applications for refinancing mortgages rose an extremely robust 24.2%, after barely budging the week before. According to the report, the average interest rate on a 30-year mortgage dropped another 14 basis points to 6.15%, its lowest level since September 2022. The rate has fallen seven straight weeks, the longest such streak since 2018-19.

August **housing starts** rose to a seasonally adjusted, annualized rate of 1.356 million units, exceeding the expected rate of 1.318 million units and July's 1.237 million. The rate of housing starts in August rose 9.6% from the rate in the previous month, notably ahead of the expected 6.5% and reversing July's 6.9% decline. August **residential building permits** rose to a rate of 1.475 million units, also exceeding the expected rate of 1.41 million units and July's 1.406 million. Permits issued for new housing units in July rose 4.9% from the previous month, also

exceeding the expected 1.0% and reversing July’s decline of 3.3%. Compared with the same month one year earlier, housing starts in August rose 3.91%, while permits fell 6.53%. The chart below shows the growth in new home starts by type of property 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
14:00	FOMC Rate Decision (Upper Bound)	w/w	18-Sep	5.25%	5.50%	***
14:00	FOMC Rate Decision (Lower Bound)	w/w	18-Sep	5.00%	5.25%	***
14:00	Interest on Reserve Balances Rate	w/w	19-Sep	5.15%	5.40%	**
16:00	Total Net TIC Flows	m/m	Jul		\$107.5b	**
16:00	Net Long-Term TIC Flows	m/m	Jul		\$96.1b	**
Federal Reserve						
ET	Speaker or Event	District or Position				
14:30	Jerome Powell Holds Post-Meeting Conference	Chairman of the Board of Governors				

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	Trade Balance	y/y	Aug	-¥695.3b	-¥628.7b	-¥1432.4b	**	Equity and bond neutral
	Exports	y/y	Aug	5.6%	10.2%	10.6%	*	Equity bearish, bond bullish
	Imports	y/y	Aug	2.3%	16.6%	15.0%	*	Equity bearish, bond bullish
	Core Machine Orders	y/y	Jul	8.7%	-1.7%	2.5%	**	Equity bullish, bond bearish
Australia	Westpac Leading Index	m/m	Aug	-0.05%	-0.03%		**	Equity and bond neutral
New Zealand	Wespac Consumer Confidence	m/m	3Q	90.8	82.2		*	Equity and bond neutral
India	Imports	y/y	Aug	3.3%	7.5%		**	Equity and bond neutral
	Trade Balance	m/m	Aug	-\$29643m	-\$23497m	-\$22800m	**	Equity and bond neutral
	Exports	y/y	Aug	-9.3%	-1.5%		**	Equity and bond neutral
EUROPE								
Eurozone	Construction output	y/y	Jul	-2.2%	-1.3%		*	Equity and bond neutral
	CPI	y/y	Aug F	2.2%	2.6%	2.2%	***	Equity and bond neutral
	Core CPI	y/y	Aug F	2.8%	2.8%	2.8%	**	Equity and bond neutral
UK	CPI	y/y	Aug	2.2%	2.2%	2.2%	***	Equity and bond neutral
	CPI Core	y/y	Aug	3.6%	3.3%	3.6%	***	Equity and bond neutral
	Retail Price Index	m/m	Aug	389.9	387.5	389.5	**	Equity and bond neutral
	RPI	y/y	Aug	3.5%	3.6%	3.4%	**	Equity and bond neutral
AMERICAS								
Canada	Housing Starts	m/m	Aug	217.4k	279.8k	250.0k	**	Equity and bond neutral
	CPI	y/y	Aug	2.0%	2.5%	2.1%	***	Equity and bond neutral
Mexico	Aggregate Supply and Demand	y/y	2Q	2.1%	2.7%	2.7%	*	Equity bearish, bond bullish

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)	512	520	-8	Down
3-mo T-bill yield (bps)	474	473	1	Down
U.S. Sibor/OIS spread (bps)	482	482	0	Down
U.S. Libor/OIS spread (bps)	478	479	-1	Down
10-yr T-note (%)	3.67	3.65	0.02	Up
Euribor/OIS spread (bps)	348	349	-1	Down
Currencies	Direction			
Dollar	Flat			Down
Euro	Flat			Up
Yen	Up			Up
Pound	Up			Up
Franc	Up			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	\$72.85	\$73.70	-1.15%	
WTI	\$70.28	\$71.19	-1.28%	
Natural Gas	\$2.34	\$2.32	0.56%	
12-mo strip crack	\$18.76	\$18.74	0.08%	
Ethanol rack	\$1.87	\$1.87	0.24%	
Metals				
Gold	\$2,577.73	\$2,569.50	0.32%	
Silver	\$30.62	\$30.70	-0.28%	
Copper contract	\$430.35	\$427.30	0.71%	
Grains				
Corn contract	\$414.25	\$412.50	0.42%	
Wheat contract	\$578.00	\$575.75	0.39%	
Soybeans contract	\$1,018.75	\$1,006.00	1.27%	
Shipping				
Baltic Dry Freight	1,901	1,896	5	
DOE Inventory Report				
	Actual	Expected	Difference	
Crude (mb)		-0.10		
Gasoline (mb)		1.00		
Distillates (mb)		1.00		
Refinery run rates (%)		-1.1%		
Natural gas (bcf)		54		

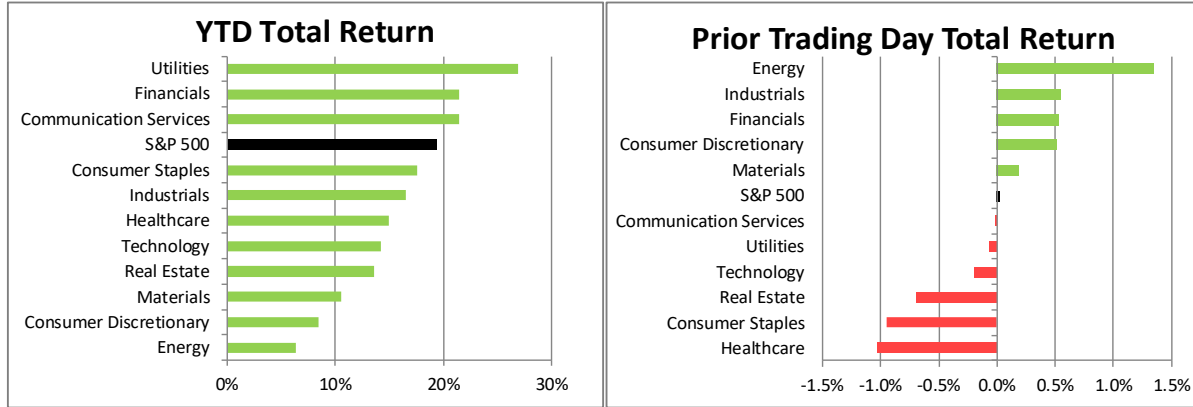
Weather

The 6-to-10-day and 8-to-14-day forecasts currently call for warmer-than-normal temperatures across the majority of the country, with the exception of near-normal temperatures along most of the East Coast. The precipitation outlook calls for wetter-than-normal conditions in the Southeast and Atlantic Coast, with dry conditions in most of the West and New England.

The remnants of Tropical Depression Gordon are slowly circling in the mid-Atlantic, where it is projected to drift northward in the open ocean. It retains a 30% chance of cyclonic formation.

Data Section

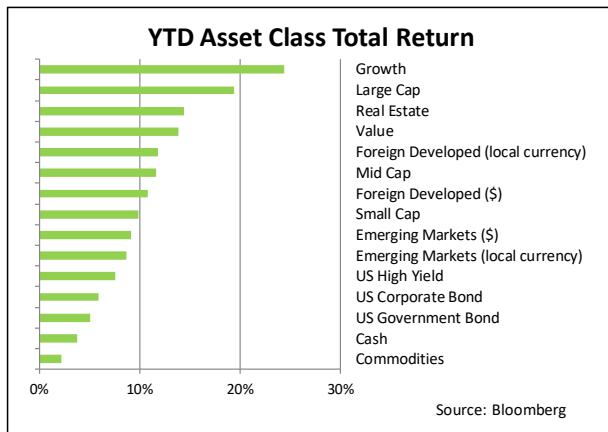
US Equity Markets – (as of 9/17/2024 close)



(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 9/17/2024 close)

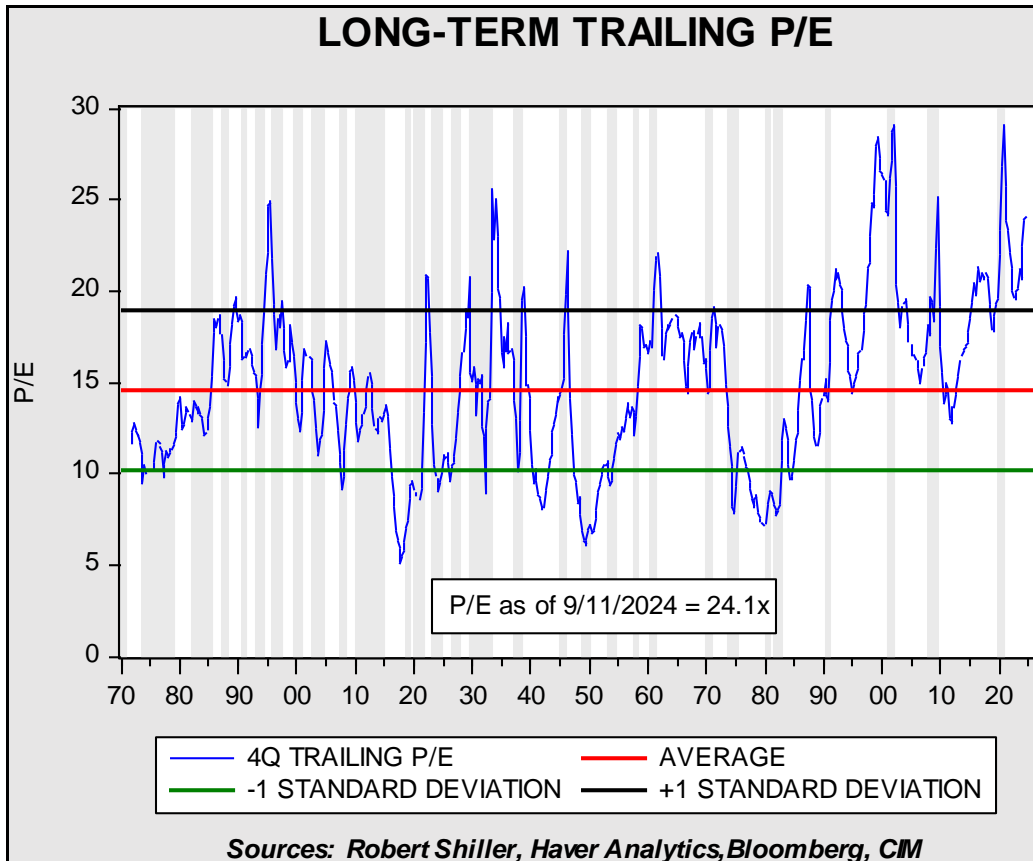


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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 12, 2024



Based on our methodology,¹ the current P/E is 24.1x, unchanged from our last report. Both the stock price index and 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 (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.