Daily Comment

By Patrick Fearon-Hernandez, CFA, and Thomas Wash

Posted: August 13, 2025 — 9:30 AM ET] Global equity markets are higher this morning. In Europe, the Euro Stoxx 50 is up 0.8% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed up 2.4%. Chinese markets were higher, with the Shanghai Composite up 0.5% from its previous close and the Shenzhen Composite up 1.3%. US equity index futures are signaling a higher open.

With 453 companies having reported so far, S&P 500 earnings for Q2 are running at $66.70 per share, compared to estimates of $64.65, which is up 5.0% from Q2 2024. Of the companies that have reported thus far, 81.6% have exceeded expectations while 14.2% 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
"Update on US and China Defense Spending" (8/11/25) + podcast	"No Country for Recessions" (8/4/25) + podcast	Q3 2025 Report Q3 2025 Rebalance Presentation	The Confluence of Ideas Podcast Value Equities Quarterly Update

Have a question on the economy, markets, geopolitics, or other important topics? You can submit your queries to our new monthly podcast, *Confluence Mailbag*! Submit your question to mailbag@confluenceim.com.

Our *Comment* will begin by exploring the market's optimism for a rate cut at the upcoming Fed meeting. We will then analyze other key stories shaping the market, including the intensifying AI competition between the US and China, diplomatic efforts to bring Iran to the negotiating table on its nuclear program, and the factors keeping crude prices low. We will conclude with an assessment of other major international and domestic developments influencing financial markets.

September Rate Cut: The latest CPI report aligned with expectations, prompting investors to price in another rate cut at the Fed's upcoming meeting. The data showed that overall inflation rose 2.7% year-over-year, while core inflation, which excludes volatile food and energy prices, climbed from 2.9% to 3.1%. The increase has largely eased concerns about tariff-driven inflation, giving the Fed more flexibility to shift focus from its price stability mandate and toward maximizing employment.

- The most notable takeaway from the CPI report was that services inflation was the primary driver of price increases in July. Airline fares increased by the most in three years, while medical care and recreational services also contributed to the uptick. Meanwhile, commodity prices, which are more sensitive to tariffs, moderated, largely due to declining gasoline prices.
- Even though the increase in core CPI isn't ideal, the market seems to believe that Federal Reserve officials will view the impact of tariffs as transitory and instead focus on the labor market. The Fed appears to be split into three groups: some officials want to cut rates, others favor holding them steady, and a final group is still undecided.
- The upcoming payroll report will likely be a decisive factor in the Federal Reserve's decision on whether to cut rates and by how much. A strong report will probably result in a minimal rate cut, or possibly none at all. Conversely, another weak report would likely prompt the Fed to implement a 50-basis-point cut, compensating for its earlier inaction.
- The market's attention appears to be divided between monetary policy and trade policy. Investors are seeking clarity on trade deals while also hoping for lower interest rates to improve lending conditions. A rate cut would likely support equity and bond prices but would also put downward pressure on the US dollar.

China's AI Push: The country is rapidly expanding its AI capabilities in a bid to rival the US in the field. Recently, China's open-source AI advancements have drawn significant attention from American tech firms, which have predominantly kept their models proprietary. US observers worry that broader access to these open-source models could accelerate their adoption, potentially establishing them as the global standard.

- These concerns follow the release of several AI models from Chinese companies this year, including DeepSeek's R1 Model. Other notable releases making an impact in the field are Alibaba's Qwen, as well as models from Moonshot, Z.ai, and MiniMax.
- Competition from China is a significant risk to the AI sector's growth, and US companies, particularly those in the Magnificent 7, are facing scrutiny over their capital expenditures. There is some worry that long-term demand may not be sufficient to justify these large investments.
- The US's reliance on foreign revenue remains a significant concern, particularly since China's continued ascent could threaten American companies' earnings. While US tech firms currently maintain some momentum, the stretched valuations of major players and mega cap tech stock's overwhelming dominance in the S&P 500 suggest that exploring other sectors may also add some portfolio value.

EU Borrowing: European leaders are debating the structure of joint debt issuance and how to mitigate fiscal spillover risks among member states. One proposed solution would link debt obligations to each country's spending plans and would necessitate a repayment of borrowed funds if nations exceed their budget allocations. The framework also includes provisions for emergency crisis loans, which would require unanimous approval from all member states.

- A move toward fiscal union within the EU could increase borrowing capacity and lower the cost of borrowing for member states. This, in turn, may help boost asset prices across the region.
- While reforms are expected to face opposition from countries like the Netherlands and Germany, we anticipate that potential progress on EU reforms will be a key driver of sustained optimism for the region.

Panama Canal: The Panama Canal Authority is preparing to launch a tender for the operation of ports on both the Atlantic and Pacific coasts. This move would allow the Authority to retain ownership of the ports while outsourcing their management to a third party. The decision to maintain control over both ports comes amid rising US-China tensions over the strategic waterway and follows US concerns about growing Chinese influence in the canal's operations.

- A surge in regional trade, driven by recent US tariffs, has heightened the importance of the ports, particularly for the US, which aims to closely monitor trade flows.
- A potential takeover of the ports illustrates how nations may attempt to remain neutral while navigating the growing rivalry between the US and China.

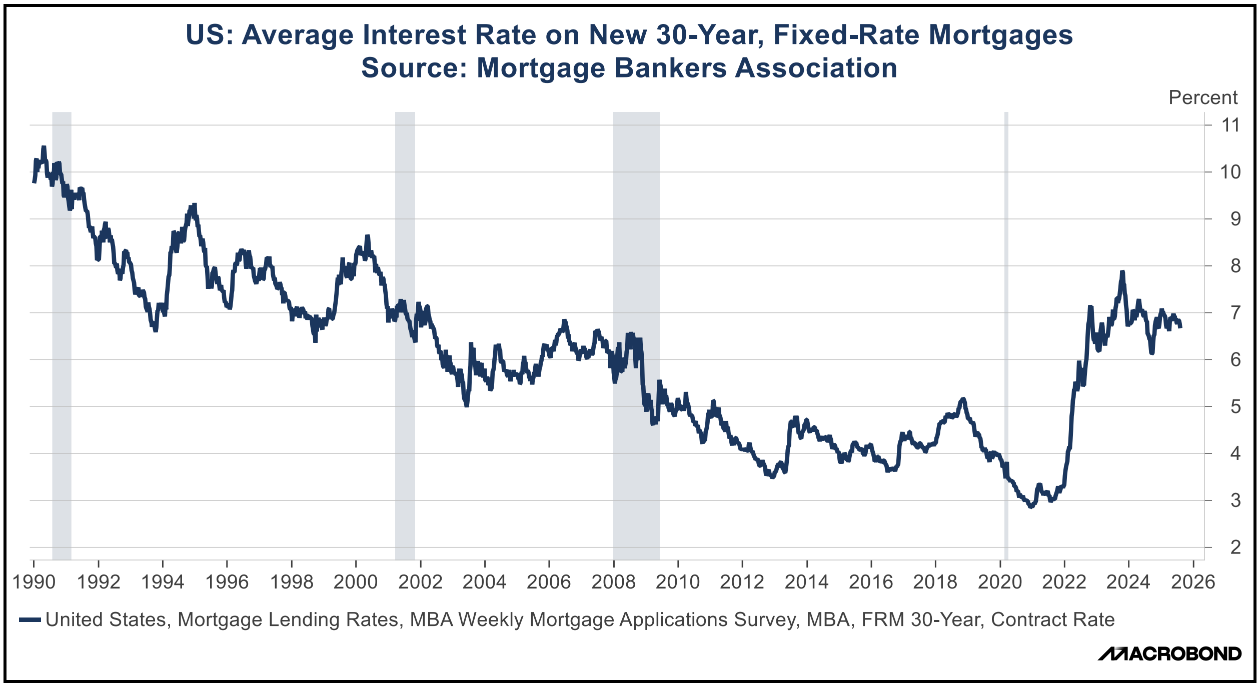
Iran Talks: Germany, the UK, and France have issued a joint statement warning they are prepared to reimpose sanctions on Iran unless it resumes nuclear negotiations with the US. The European powers have set an August deadline for Tehran to return to talks or face renewed sanctions. Iran has countered by threatening to withdraw from the nuclear agreement entirely if punitive measures are reinstated.

Crude Price Weakness: A supply surge and weak demand are expected to pressure oil prices in the coming months. According to the IEA, global inventories are projected to increase by 2.96 million barrels per day, driven by rising production (led by Saudi Arabia) and an economic slowdown concentrated in Asia. However, the agency cautioned that the outlook remains uncertain, particularly if sanctions on Iran and Russia intensify.

Trump-EU: President Trump is set to speak with European leaders ahead of his planned talks with Russian President Putin later this week. The discussions will focus on a potential land swap deal, which may require Ukraine to cede some territory to Russia in exchange for a peace agreement. Both sides aim to negotiate terms that ensure a fair and lasting resolution.

US Economic Releases

The Mortgage Bankers Association said ***mortgage applications*** in the week ended August 9 jumped 10.9%, accelerating from their 3.1% gain in the previous week. Applications for home purchase mortgages rose a modest 0.5%, after increasing 1.3% in the prior week. In contrast, applications for refinancing mortgages surged 23.0%, following their 5.2% increase the week before. What drove the surge in refinancings? According to the report, the average interest rate on a 30-year mortgage fell 10 basis points to 6.67%, reaching its lowest level in more than four months. The chart below shows how mortgage rates have changed over time.



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

Economic Releases		
No economic releases for the rest of today		
Federal Reserve		
EST	**Speaker or Event**	**District or Position**
8:00	Thomas Barkin Repeats Remarks on Economy	President of the Federal Reserve Bank of Richmond
13:00	Austan Goolsbee Speaks at Monetary Policy Luncheon	President of the Federal Reserve Bank of Chicago
13:30	Raphael Bostic Speaks on the Economic Outlook	President of the Federal Reserve Bank of Atlanta

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	PPI	y/y	Jul	2.6%	2.9%	2.5%	***	Equity and bond neutral
	Machine tool orders	y/y	Jul P	3.6%	-0.5%		**	Equity and bond neutral
Australia	Wage Price Index	m/m	2Q	3.40%	3.40%	3.30%	***	Equity and bond neutral
South Korea	Unemployment Rate	m/m	Jul	2.5%	2.6%	2.6%	***	Equity and bond neutral
China	New Yuan Loans	m/m	Jul	12870	12920.0b	13220.0b	**	Equity and bond neutral
	Money Supply M2	y/y	Jul	8.8%	8.3%	8.3%	***	Equity bullish, bond bearish
	Money Supply M1	y/y	Jul	5.6%	4.6%	5.2%	*	Equity and bond neutral
	Money Supply M0	y/y	Jul	11.8%	12.0%		*	Equity and bond neutral
EUROPE								
Germany	Wholesale Price Index	y/y	Jul	0.5%	0.9%		*	Equity and bond neutral
	CPI	y/y	Jul F	2.0%	2.0%	2.0%	***	Equity and bond neutral
	CPI, EU Harmonized	y/y	Jul F	11.8%	1.8%	1.8%	**	Equity and bond neutral
AMERICAS								
Canada	Building Permits	m/m	Jun	-9.0%	12.8%	-4.00	**	Equity and bond neutral
Mexico	International Reserves Weekly	w/w	8-Aug	$243,222	$242516m		*	Equity and bond neutral
Brazil	Retail Sales	y/y	Jun	2.7%	1.7%	2.8%	***	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 T-bill yield (bps)	412	413	-1	Up
U.S. Sibor/OIS spread (bps)	420	422	-2	Down
U.S. Libor/OIS spread (bps)	416	418	-2	Down
10-yr T-note (%)	4.26	4.29	-0.03	Up
Euribor/OIS spread (bps)	203	203	0	Down
Currencies	**Direction**			
Dollar	Up			Down
Euro	Down			Up
Yen	Up			Flat
Pound	Down			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	$65.75	$66.12	-0.56%	
WTI	$62.70	$63.17	-0.74%	
Natural Gas	$2.77	$2.81	-1.42%	
Crack Spread	$26.26	$26.43	-0.62%	
12-mo strip crack	$23.10	$23.23	-0.57%	
Ethanol rack	$1.89	$1.89	-0.13%	
Metals				
Gold	$3,359.92	$3,348.26	0.35%	
Silver	$38.55	$37.91	1.68%	
Copper contract	$458.00	$458.50	-0.11%	
Grains				
Corn contract	$396.25	$394.50	0.44%	
Wheat contract	$506.00	$505.00	0.20%	
Soybeans contract	$1,042.00	$1,032.75	0.90%	
Shipping				
Baltic Dry Freight	2,017	2,038	-21	
DOE Inventory Report				
	Actual	**Expected**	**Difference**	
Crude (mb)		-0.91		
Gasoline (mb)		-0.72		
Distillates (mb)		1.25		
Refinery run rates (%)		-0.7%		
Natural gas (bcf)		54		

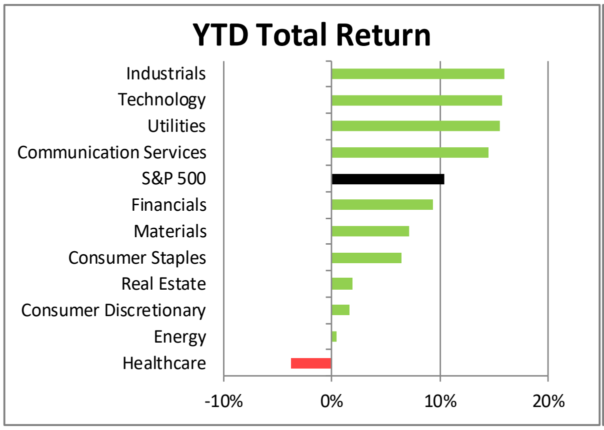
Weather

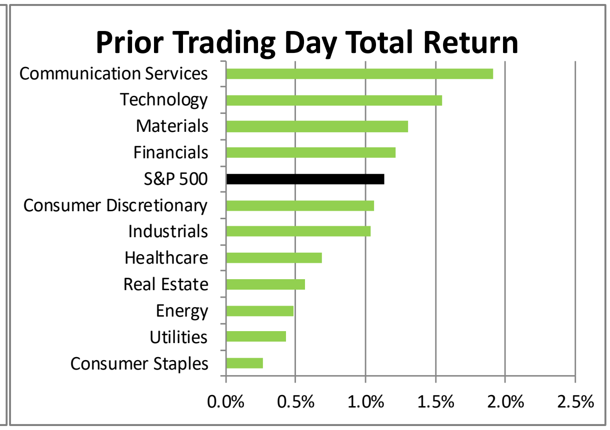
The 6-to-10-day and 8-to-14-day forecasts currently call for warmer-than-normal temperatures throughout the entire western half of the country and the Gulf coast, with cooler-than-normal temperatures in New England. The forecasts call for wetter-than-normal conditions in the Rocky Mountains, the southern Great Plains, and the Southeast, with dry conditions expected in Oregon, Idaho, and New England.

The Atlantic is currently active with three tropical disturbances. One disturbance is crossing the Yucatan Peninsula and traveling northwesterly today, but it is assessed to have only a 20% chance of developing into a cyclone within the next seven days. There is also a disturbance in the northern Atlantic south of Nova Scotia, but it is assessed to have only a 20% chance of cyclone formation in the coming week. Finally, Tropical Storm Erin is in the central Atlantic and moving westward slowly. The storm poses no immediate threat to the US.

Data Section

US Equity Markets – (as of 8/12/2025 close)

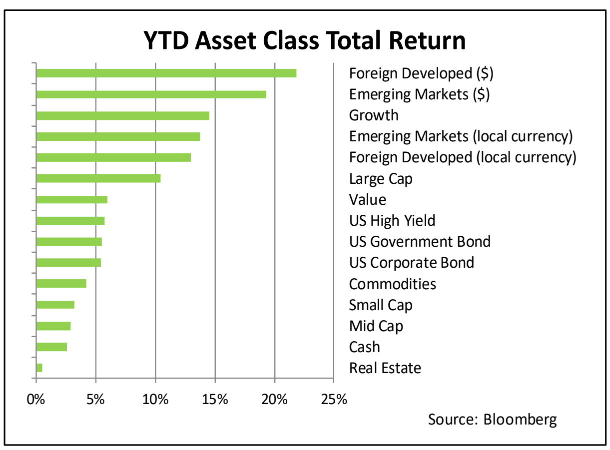




(Source: Bloomberg)

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 8/12/2025 close)

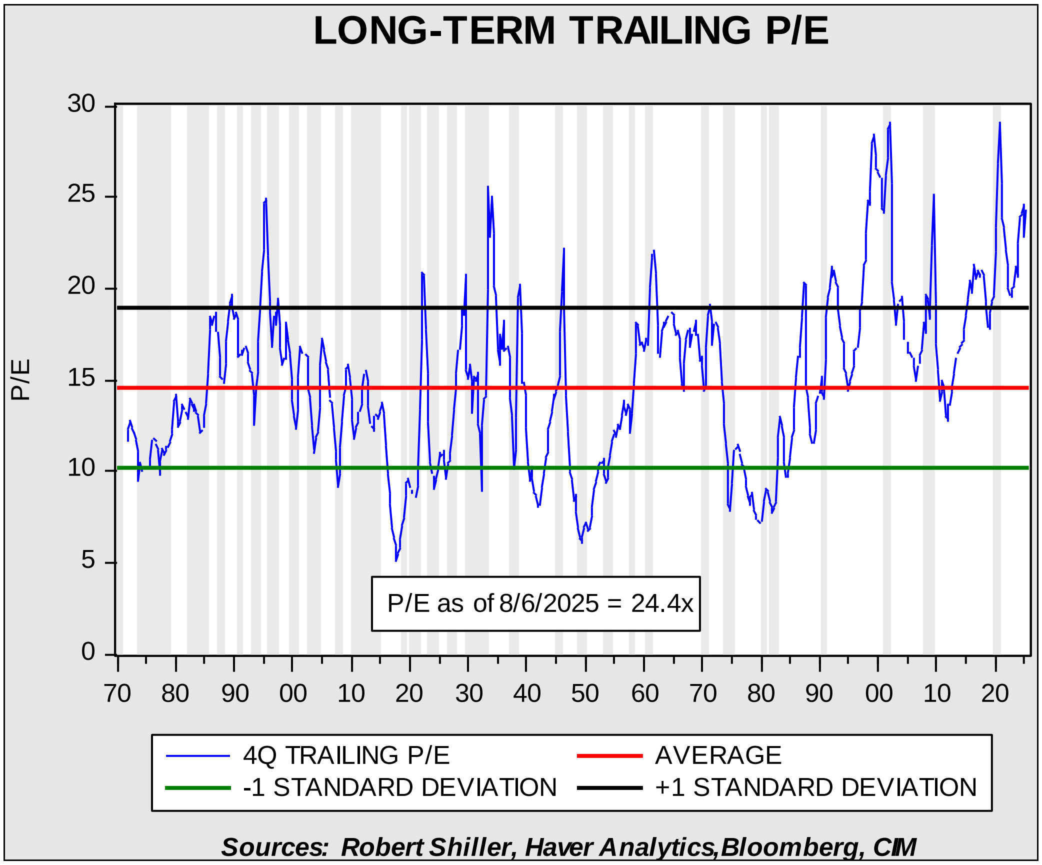


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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

August 7, 2025



Based on our methodology,[1] the current P/E is 24.4x, down 0.1 from our last report. The drop was due to the increase in earnings outweighing the 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.

[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, Q3, Q4) 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.