Daily Comment

By Patrick Fearon-Hernandez, CFA, and Thomas Wash

Posted: August 20, 2025 — 9:30 AM ET] Global equity markets are mixed this morning. In Europe, the Euro Stoxx 50 is up 0.1% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed down 1.5%. Chinese markets were higher, with the Shanghai Composite up 1.0% from its previous close and the Shenzhen Composite up 0.8%. US equity index futures are signaling a lower open.

With 461 companies having reported so far, S&P 500 earnings for Q2 are running at $66.80 per share compared to estimates of $64.65, which is up 5.0% from Q2 2024. Of the companies that have reported thus far, 81.5% have exceeded expectations, while 14.4% 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	"Navigating the Waves of BLS Revisions" (8/18/25) + 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 first address recent doubts about the AI boom, then examine other critical market developments, including the trade calm between the US and China, the eurozone's pivot toward new trade partners, and a call for the resignation of an FOMC member. We will conclude with an overview of other global and domestic factors shaping the financial landscape.

AI Spook: US equities sold off sharply on Tuesday after an MIT study cast doubt on the commercial viability of generative AI. The research, which drew from a significant dataset of interviews, surveys, and deployment analyses, revealed a staggering 95% of AI pilots did not

produce a meaningful boost to revenue or productivity. This finding directly challenges the high valuations of AI-focused companies, prompting the market downturn.
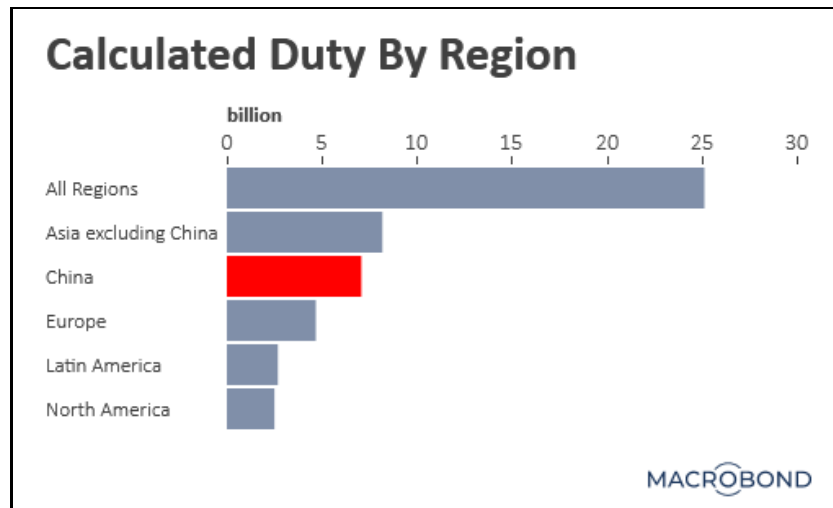
- However, the study suggests that the models' poor performances stem less from their technical quality and more from flawed corporate integration. The report found that companies partnering with external AI specialists achieved a 67% success rate — double the 33% rate of those that relied solely on in-house development.

- While slow adoption cycles are typical for new technologies, the current pace raises serious questions about the tech sector's massive capital expenditures and potential overcapacity. For context, Alphabet's projected 2025 capex of $85 billion exceeds France's entire military budget for 2027. This aggressive build-out of AI data centers, intended to meet anticipated demand, risks creating a significant capacity glut and fuels concerns about a brewing bubble.

Magnificent 7 Stage a Powerful Rebound After Rocky Start
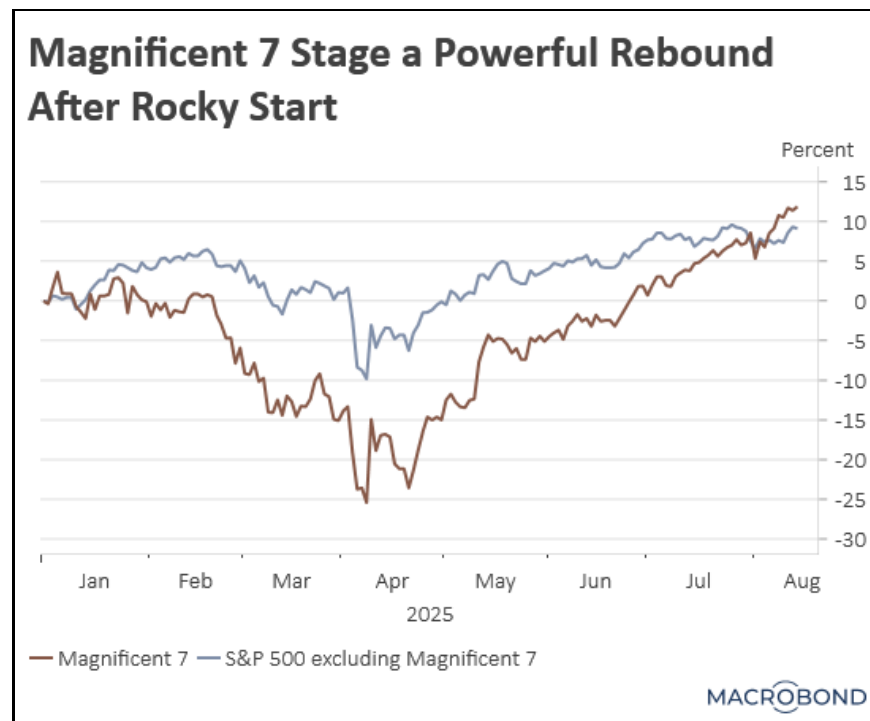
- The market's gains remain narrowly concentrated in the Magnificent 7, even as concerns over tariffs have subsided. This persistent lack of breadth heightens the market's vulnerability to a sentiment-driven pullback. Given these concentrated risks and elevated uncertainty, we advise investors to maintain a disciplined and prudent approach to portfolio construction.

US Satisfied: The White House is leaning toward maintaining the status quo with China, its largest rival. Signaling this intent, Treasury Secretary Scott Bessent stated the US is "very happy" with the existing tariff structure. This position was reinforced last week by the administration's decision to extend the trade deal deadline by 90 days into November, suggesting a deliberate pause to de-escalate tensions.

- The significant tariff revenue collected on Chinese imports is a major factor in the White House's support for the status quo. These duties are the primary contributor to US import tax receipts, and available evidence suggests the financial burden is largely falling on Chinese exporters rather than American consumers.

Calculated Duty By Region

billion

Region	
All Regions	~26
Asia excluding China	~8
China	~7
Europe	~5
Latin America	~3
North America	~3

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- The current period of trade calm is a positive for the market, as it mitigates the risk of further supply chain disruption. Given the recent weakness in the Chinese economy, US trade negotiators now possess significant leverage to secure concessions. Consequently, we remain optimistic that the administration can reach an agreement, which would substantially reduce market uncertainty.

State Stablecoin: Wyoming has launched the first state-sponsored stablecoin, the Frontier Stable Token (FRNT), to cement its status as a blockchain hub and attract investment. Backed by a 102% reserve of US dollars and short-term Treasurys, FRNT will leverage blockchain technology to offer faster, cheaper transactions for businesses and consumers. The timing of its unveiling at the state's Blockchain Symposium, coinciding with the Jackson Hole Economic Symposium, signals the industry's aspiration to compete against the traditional financial system.

Eurozone Looking Elsewhere: ECB President Christine Lagarde has urged the EU to strengthen its relationships with non-US countries. While she affirmed the importance of the eurozone's relationship with the US, she also stressed that the region should strive to keep its economy more export oriented. These were her first comments since the EU struck a deal with the US. Referring to the new arrangement, she also stated that she expects growth to slow due to trade uncertainty.

Economic Bellwether: Despite apparent corporate optimism from home improvement retailers about consumer health, earnings results have been mixed. Home Depot missed estimates and warned that tariffs may force price changes. In contrast, competitor Lowe's beat estimates and raised its outlook, benefiting from its acquisition of Foundation Building Materials. This divergence may partly reflect a slowdown in housing activity, a potential sign of economic uncertainty.
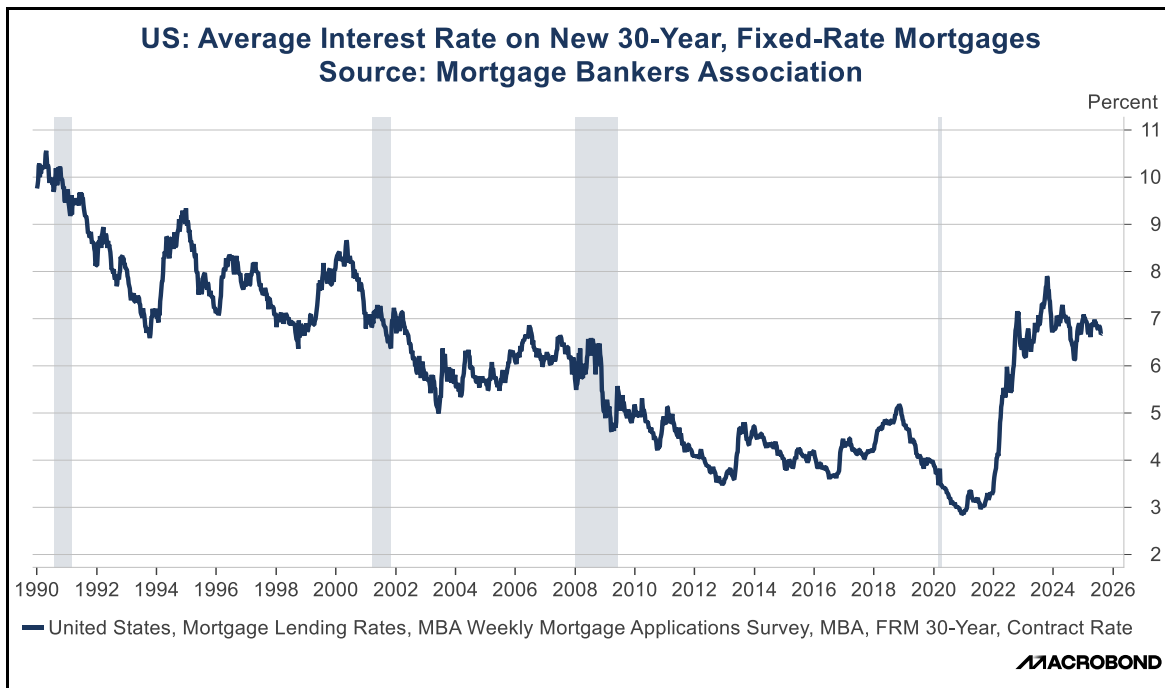
Israel Call Up: The Israeli government has announced that it will call up 60,000 reservists as part of its ongoing military operations in the Gaza Strip. The decision was made two days after Hamas reportedly accepted a ceasefire agreement that closely mirrored a proposal from the previous US administration. Despite the potential for de-escalation, Israel has stated its intent to continue its offensive, citing the goal of eliminating the threat posed by Hamas. While the conflict is expected to persist, analysts believe it is unlikely to expand regionally.

Trump Broadens Attack: President Trump has called for the resignation of Federal Reserve Governor Lisa Cook following allegations that she falsified bank documents to receive favorable mortgages. This move is consistent with the president's stated objective to reshape the Federal Open Market Committee (FOMC) with members aligned with his economic views. The demand for her resignation comes as the president intensifies his pressure on the central bank to lower interest rates at its next meeting.

Japan Government Bonds: Japan's super-long-term government bonds have recently attracted strong foreign investment, with aggregate buying reaching a record $63 billion in recent months. This surge in demand is primarily driven by foreign investors looking to capitalize on rising interest rates, which have increased amid concerns over higher government spending. Additionally, a weaker US dollar is playing a role, as investors seek to benefit from a stronger yen, particularly if the Bank of Japan follows through with plans to tighten its monetary policy.

US Economic Releases

The Mortgage Bankers Association said ***mortgage applications*** in the week ended August 15 fell 1.4%, erasing part of their 10.9% jump in the previous week. Applications for home purchase mortgages edged up 0.1%, building on their 1.4% gain in the prior week. However, applications for refinancing mortgages slumped 3.2%, giving back part of their 23.0% jump in the prior seven-day period. According to the report, the average interest rate on a 30-year mortgage rose 1 basis point to 6.68%. The chart below shows how mortgage rates have changed over time.

US: Average Interest Rate on New 30-Year, Fixed-Rate Mortgages
Source: Mortgage Bankers Association

United States, Mortgage Lending Rates, MBA Weekly Mortgage Applications Survey, MBA, FRM 30-Year, Contract Rate

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**
11:00	Christopher Waller Speaks at Wyoming Blockchain Symposium	Member of the Board of Governors
14:00	U.S. Federal Reserve Releases Meeting Minutes	Federal Reserve Board
15:00	Raphael Bostic in Moderated Conversation on 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	Trade Balance	y/y	Jul	-¥117.5	¥153.1b	¥198.5	**	Equity and bond neutral
	Exports	y/y	Jul	-2.6%	-0.5%	-2.1%	*	Equity and bond neutral
	Imports	y/y	Jul	-7.5%	0.2%	-10.0%	*	Equity bullish, bond bearish
	Core Machine Orders	y/y	Jun	7.6%	4.4%	4.7%	**	Equity and bond neutral
	Tokyo Condominiums for Sale	y/y	Jul	34.1%	-1.3%		*	Equity and bond neutral
EUROPE								
Eurozone	CPI	y/y	Jul F	2.0%	2.0%	2.0%	***	Equity and bond neutral
	Core CPI	y/y	Jul F	2.3%	2.3%	2.3%	**	Equity and bond neutral
Germany	PPI	y/y	Jul	1.5%	-1.3%	1.4%	**	Equity and bond neutral
UK	CPI	y/y	Jul	3.8%	3.6%	3.7%	***	Equity and bond neutral
	CPI Core	y/y	Jul	3.8%	3.7%	3.7%	***	Equity and bond neutral
	Retail Price Index	m/m	Jul	406.2	404.5	405.1	**	Equity and bond neutral
	RPI	y/y	Jul	4.8%	4.4%	4.5%	**	Equity and bond neutral
	RPI Ex Mort Int.Payments	y/y	Jul	4.70%	4.30%		*	Equity and bond neutral
	House Price Index	y/y	Jun	3.70%	2.70%		*	Equity and bond neutral
AMERICAS								
Canada	CPI	y/y	Jul	1.7%	1.9%	1.8%	***	Equity and bond neutral
Mexico	International Reserves Weekly	w/w	15-Aug	$243109m	$243222m		*	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)	411	410	1	Down
U.S. Sibor/OIS spread (bps)	420	421	-1	Down
U.S. Libor/OIS spread (bps)	416	417	-1	Down
10-yr T-note (%)	4.30	4.31	-0.01	Up
Euribor/OIS spread (bps)	203	203	0	Down
Currencies	**Direction**			
Dollar	Up			Down
Euro	Down			Up
Yen	Up			Down
Pound	Down			Up
Franc	Down			Up
Central Bank Action	**Current**	**Prior**	**Expected**	
PBOC 1-Year Loan Prime Rate	3.00%	3.00%	3.00%	On Forecast
PBOC 5-Year Loan Prime Rate	3.50%	3.50%	3.50%	On Forecast
RBNZ Official Cash Rate	3.00%	3.25%	3.00%	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.

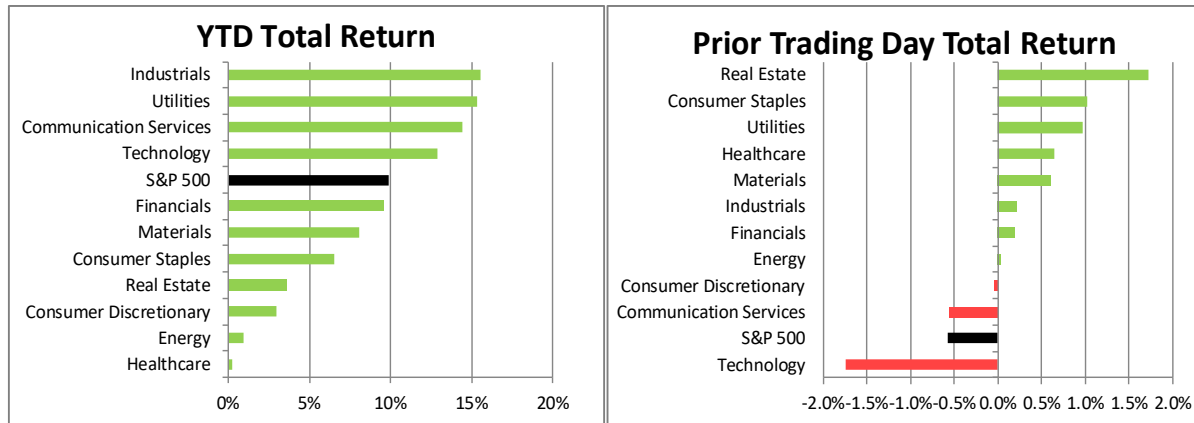|	Price	Prior	Change	Explanation
Energy Markets				
Brent	$66.52	$65.79	1.11%	
WTI	$63.06	$62.35	1.14%	
Natural Gas	$2.75	$2.77	-0.61%	
Crack Spread	$27.78	$27.66	0.45%	
12-mo strip crack	$23.81	$23.61	0.83%	
Ethanol rack	$1.90	$1.91	-0.18%	
Metals				
Gold	$3,329.93	$3,315.78	0.43%	
Silver	$37.13	$37.39	-0.69%	
Copper contract	$448.90	$448.85	0.01%	
Grains				
Corn contract	$401.75	$403.25	-0.37%	
Wheat contract	$522.75	$521.25	0.29%	
Soybeans contract	$1,034.00	$1,033.75	0.02%	
Shipping				
Baltic Dry Freight	1,964	2,022	-58	
DOE Inventory Report				
	Actual	**Expected**	**Difference**	
Crude (mb)		-0.85		
Gasoline (mb)		-0.32		
Distillates (mb)		1.48		
Refinery run rates (%)		-1.0%		
Natural gas (bcf)		18		

Weather

The 6-to-10-day and 8-to-14-day forecasts currently call for warmer-than-normal temperatures in the Pacific Northwest, southern Texas, and Florida, with cooler-than-normal temperatures in the Great Plains, Midwest, and East Coast regions. The forecasts call for wetter-than-normal conditions in the Rocky Mountains and along the East Coast, with dry conditions in the Midwest.

There are now three tropical disturbances in the Atlantic Ocean area. Hurricane Erin is off the Carolinas and is expected to move northeasterly along the East Coast, bringing heavy rains and high tides to the region over the next several days. There is also a tropical disturbance in the central Atlantic that is moving northwesterly toward the US and is assessed to have a 60% chance of developing into a cyclone within the next week. Finally, there is a tropical disturbance off the western coast of Africa that is moving westerly and is assessed to have a 40% chance of cyclone formation in the same period.
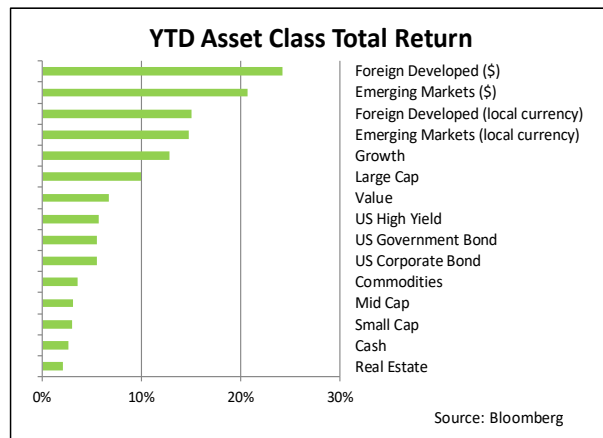
Data Section

US Equity Markets – (as of 8/19/2025 close)

YTD Total Return

Sector	
Industrials	
Utilities	
Communication Services	
Technology	
S&P 500	
Financials	
Materials	
Consumer Staples	
Real Estate	
Consumer Discretionary	
Energy	
Healthcare	

(Axis: 0% to 20%)

Prior Trading Day Total Return

Sector	
Real Estate	
Consumer Staples	
Utilities	
Healthcare	
Materials	
Industrials	
Financials	
Energy	
Consumer Discretionary	
Communication Services	
S&P 500	
Technology	

(Axis: -2.0% to 2.0%)

(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 8/19/2025 close)

YTD Asset Class Total Return

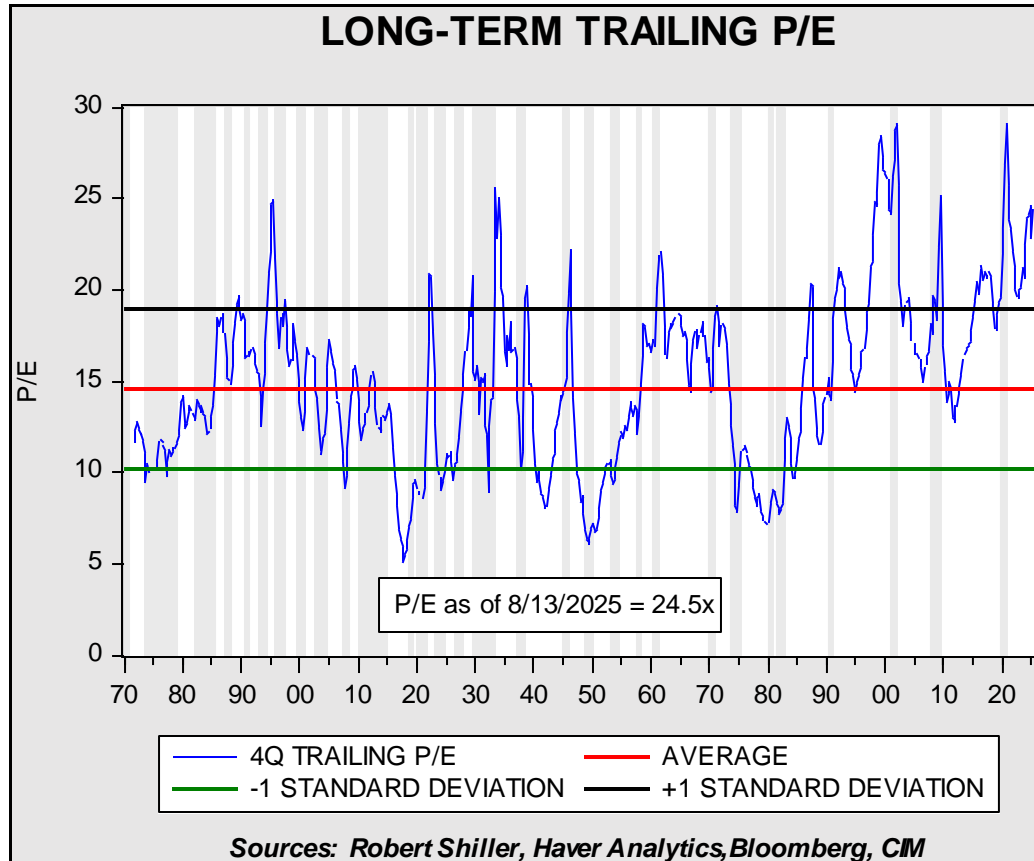| Asset Class	
Foreign Developed ($)	
Emerging Markets ($)	
Foreign Developed (local currency)	
Emerging Markets (local currency)	
Growth	
Large Cap	
Value	
US High Yield	
US Government Bond	
US Corporate Bond	
Commodities	
Mid Cap	
Small Cap	
Cash	
Real Estate	

(Axis: 0% to 30%)

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

August 14, 2025

LONG-TERM TRAILING P/E

P/E as of 8/13/2025 = 24.5x

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 24.5x, up 0.1 from our last report. The increase was due to the rise in the stock price index outweighing the 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.

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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, 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.