

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: August 30, 2023—9:30 AM EDT] Global equity markets are mixed this morning. In Europe, the Euro Stoxx 50 is down 0.3% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed up 0.1%. Chinese markets were generally higher, with the Shanghai Composite essentially unchanged from its previous close and the Shenzhen Composite up 0.4%. U.S. 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:

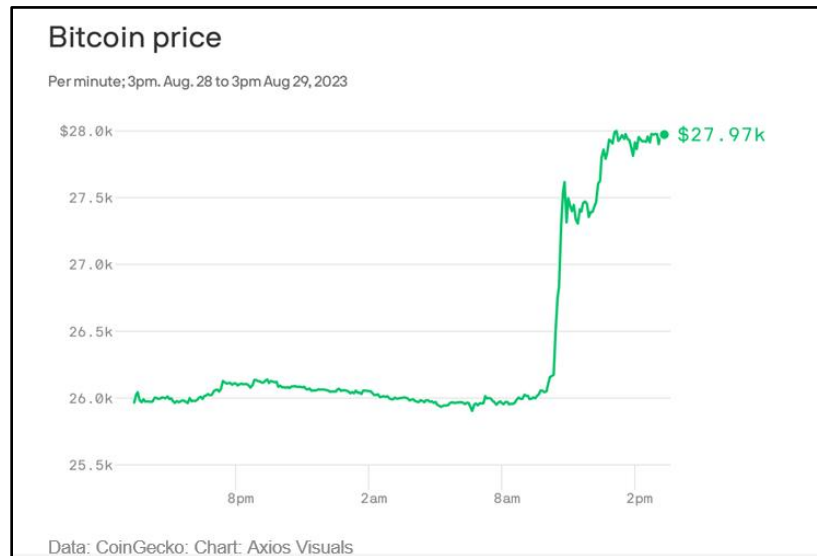
- [Bi-Weekly Geopolitical Report](#) (8/21/2023) (there will be no podcast for this report): “Reflections on the New Cold War”
- [Weekly Energy Update](#) (8/24/2023): European LNG prices are swinging due to the combination of ample storage and worries about shortages this winter. Tensions in the Middle East remain high; although the Gulf State and Iran have been making diplomatic overtures, overall improvements in relations remain scarce.
- [Asset Allocation Quarterly – Q3 2023](#) (7/20/2023): Discussion of our asset allocation process, Q3 2023 portfolio changes, and our outlook for the markets.
- [Asset Allocation Q3 2023 Rebalance Presentation](#) (8/18/2023): Video presentation featuring the Asset Allocation Committee as they review the asset allocation strategies, recent portfolio changes, and the current macro environment.
- [Asset Allocation Bi-Weekly](#) (8/28/2023) (there will be no podcast for this report): “Examining the Rise in T-Note Yields”
- [Confluence of Ideas podcast](#) (8/22/2023): “The Economics of Defense in Great Power Competition”
- [Business Cycle Report](#) (8/24/23)

Our *Comment* today opens with U.S. news, including yesterday’s blockbuster court decision that boosted cryptocurrency prices and a couple of words on the labor market data that boosted stocks. We next review a wide range of other international and U.S. developments with the potential to affect the financial markets today, including signs of sticky inflation in Europe and yet another coup in Africa.

U.S. Cryptocurrency Regulation: A federal court yesterday [ruled that the SEC acted unreasonably when it rejected an application by Greystone Investments to launch an exchange-](#)

[traded fund based on spot Bitcoin](#). The ruling invalidates the SEC’s effort to force cryptocurrency funds to invest only in futures, which would be traded on U.S.-regulated exchanges.

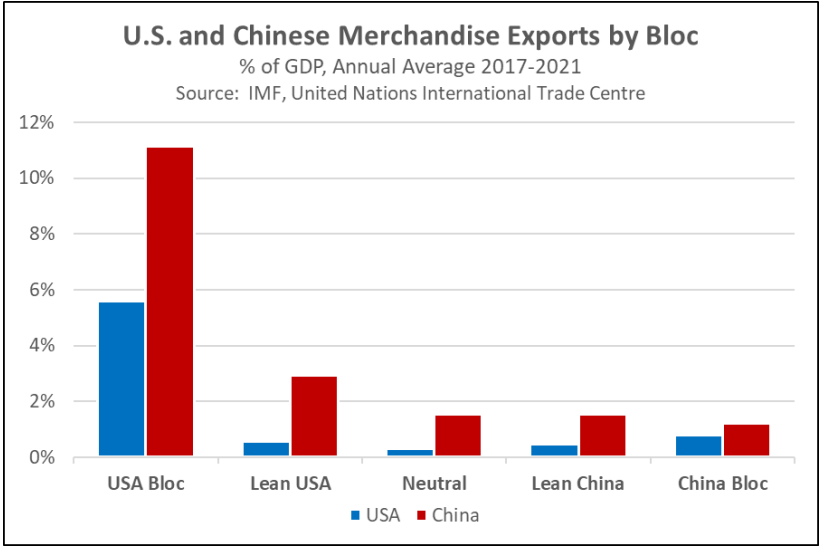
- Even though the SEC could still decide to appeal to the Supreme Court, the ruling allowing the formation of spot-Bitcoin ETFs is expected to spur a major increase in the demand for cryptocurrencies.
- As a result, Bitcoin and other cryptocurrencies jumped in value yesterday, with Bitcoin alone up approximately 7.7% to \$27,970.



U.S. Trade Policy: Following up on former President Trump’s recent call for a 10% tariff against all imports, [there are signs the other declared Republican presidential candidates are swinging to the same view](#). The sentiment is especially negative towards China, where several top politicians have called for rescinding permanent normal trade relations with the country and boosting domestic manufacturing through protectionist policies ranging from tariffs and import barriers to subsidies.

- While it’s widely recognized that there is already broad, bipartisan support among centrist Republicans and Democrats for a bigger defense budget and a stronger response to China’s geopolitical aggressiveness, it now appears that industrial protectionism is becoming another area of bipartisan agreement, at least as it relates to China.
- One key question is whether U.S. protectionist policies will be applied broadly, even against the U.S.’s key allies and other members of its geopolitical bloc.
 - Tariffs and other policies applied against Washington’s allies would threaten to weaken the U.S. bloc and potentially spark a global, chaotic trade war marked by an “every man for himself” attitude. It could also drive some U.S. allies or potential allies into a closer economic relationship with China.
 - In contrast, sparing U.S. allies would help preserve Washington’s key economic leverage over China. As shown in the chart below, over 10% of Chinese gross

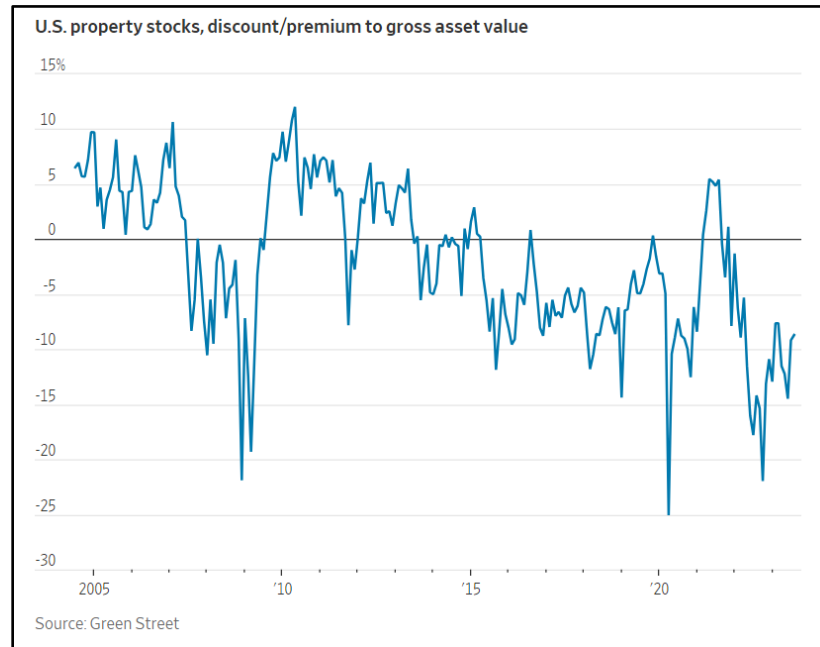
domestic product comes from exporting to the overall U.S.-led bloc, making it imperative to maintain the bloc's unity and coordination versus Beijing.



U.S. Labor Market: In the Job Openings and Labor Turnover Survey released yesterday, July vacancies [came in at a seasonally adjusted 8.8 million, well below expectations and down from 9.2 million in June](#). That means the ratio of job openings to unemployed workers has now fallen to 1.5, far below the roughly 2.0 seen early last year. In turn, that suggests the demand for labor continues to cool, raising the prospect for slower wage growth, reduced inflation pressures, and a potential end to the Federal Reserve's interest-rate hikes. The data release goes far toward explaining the big jump in stock prices yesterday.



U.S. Commercial Real Estate Market: The *Wall Street Journal* today [has a useful story looking at various indicators of where the commercial real estate industry is headed](#). For example, the story notes that publicly traded property stocks are currently trading at about a 10% discount to their gross asset values—a decent proxy for the size of the price falls that investors still expect in private real-estate values.



U.S. Weather: Hurricane Idalia, now a Category 3 storm, [has made landfall this morning](#) in northwestern Florida. Some 30 counties in the state are under evacuation orders, and damage is anticipated to be extensive. Travel is also likely to be disrupted throughout the region. We expect to provide more details on any economic impact from the storm in our *Comment* the rest of the week.

Eurozone: New data [shows price pressures remain high](#). In Spain, the August consumer price index was up 2.4% from the same month one year earlier, accelerating from the gains of 2.1% in the year to July and just 1.6% in the year to June. Excluding the volatile food and energy components, the August “core” CPI re-accelerated to show a rise of 5.9% on the year. Meanwhile, in the key German state of North Rhine-Westphalia, the August CPI was up 5.9% year-over-year, accelerating from 5.8% in July. The figures suggest that overall eurozone inflation data will be worrisome enough to prompt the European Central Bank to hike interest rates further in September.

China-India: The Indian government [lodged a formal protest against China for releasing a new “standard map” that shows Indian territory as part of China](#). The two countries have long had territorial disputes along their poorly demarcated border in the Himalaya Mountains, but the frictions have worsened since a bloody clash between Chinese and Indian troops in the area in 2020. The frictions are a key reason why India has been reluctant to join the China/Russia geopolitical bloc and is instead becoming close to the U.S. and its bloc.

Russia-Ukraine War: Overnight, Ukrainian forces evidently [used swarms of drones to attack military targets across Russia and were able to damage or destroy several aircraft](#) at an air force base near the city of Pskov. That is just the latest Ukrainian attack to successfully damage some of Russia’s powerful, expensive aircraft, illustrating how the Ukrainians continue to develop their own brand of “asymmetric” warfare. The Ukrainian successes may not necessarily bring about its key goals in the war, but they will help to further degrade the Russian military.

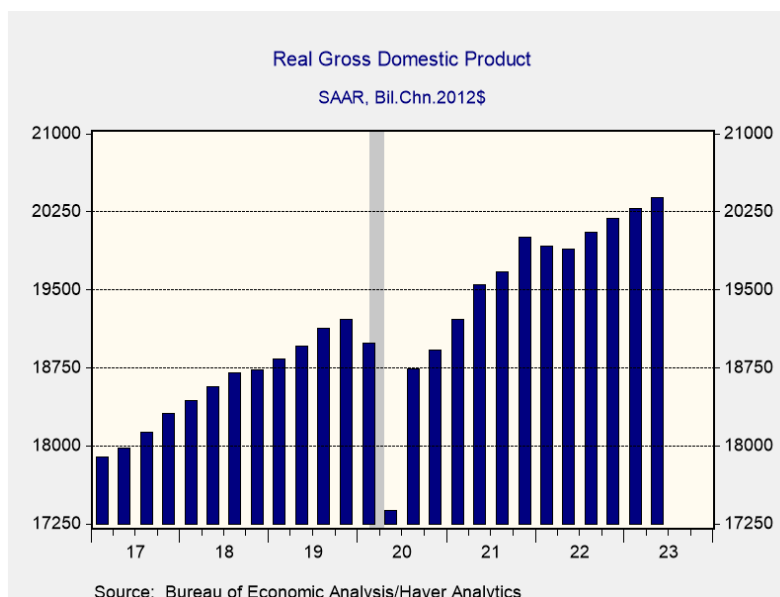
Gabon: Following closely on the recent coup in Niger, military officers in the central African nation of Gabon [have staged a coup and toppled the country’s recently re-elected president](#). The former French colony is a member of the Organization of the Petroleum Exporting Countries, but it is not one of OPEC’s major oil producers.

Guatemala: Electoral authorities on Monday evening [suspended the center-left Seed Movement of President-elect Bernardo Arévalo, potentially preventing the party’s legislators from taking their seats in Congress](#) and hamstringing Arévalo’s administration. The party has appealed to a higher court, but it is not clear whether they will be successful, given that their focus on fighting corruption threatens many of Guatemala’s vested interests.

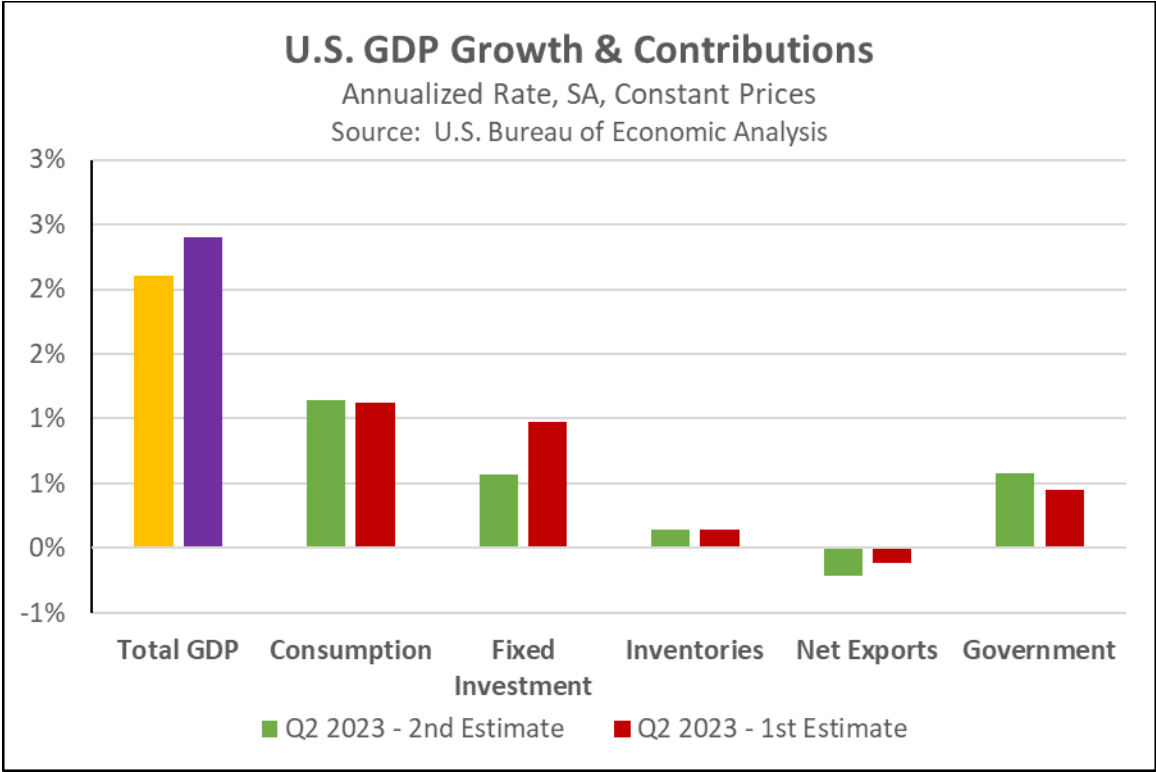
U.S. Economic Releases

Residential loan demand rose for the first time in five weeks. According to an index tracked by the Mortgage Bankers Association, mortgage applications rose 2.3% in the week ending August 25. The increases come as interest rates stalled in the prior week. The average 30-year fixed-rate mortgage was unchanged from the prior week at 7.31%. As a result, the tracker for purchases and refinancing rose 2.0% and 2.5% from the prior week, respectively.

The second revision of the gross domestic product (GDP) showed that the economy grew at an annual rate of 2.1% in the second quarter of 2023, slower than the initial estimate of 2.4%. The current real GDP currently sits at 20.385 trillion.

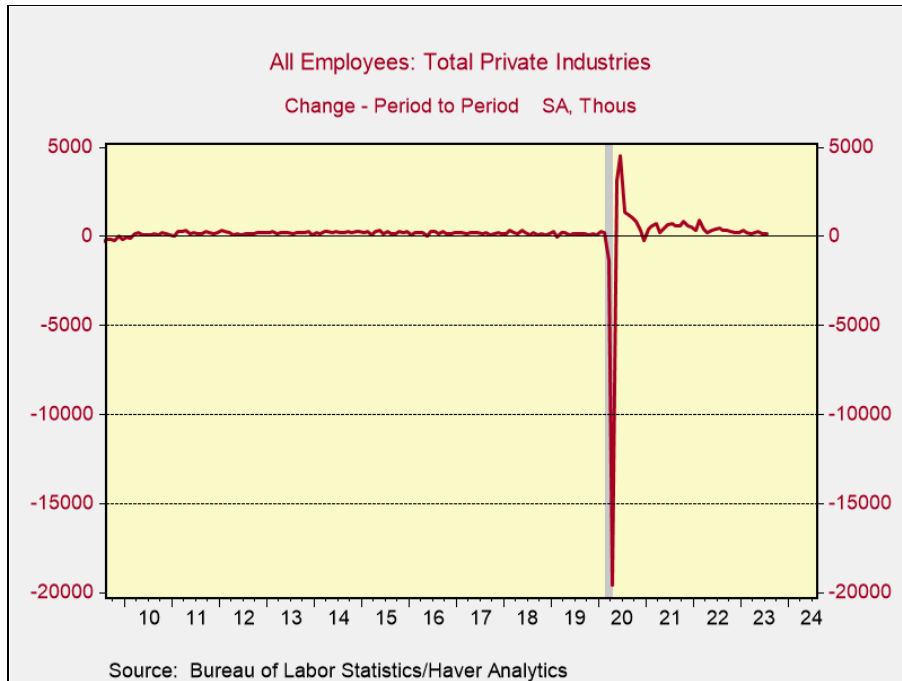


The downward revision was driven primarily by lower-than-expected investment spending. Investment decreased from 5.7% to 3.3%, offsetting the modest increase in personal consumption which increased from 1.6 to 1.7%.



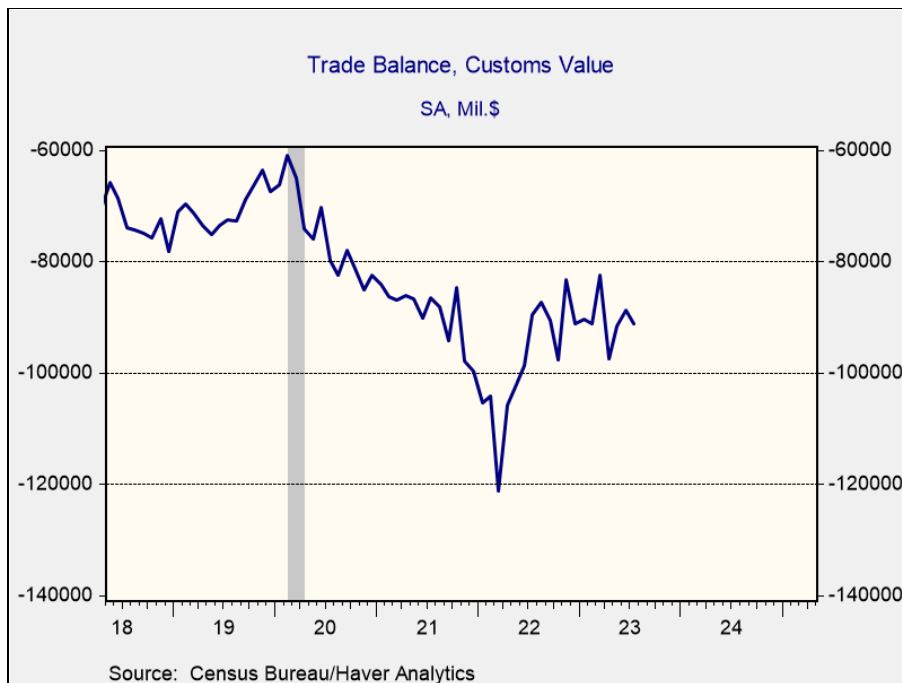
The chart above shows the changes in the contribution to GDP. Consumption and government spending were revised upwards, while fixed investment and net exports were revised downward.

Private payrolls showed that the country added less jobs than expected. According to the payroll company ADP, employers added 177k in August, below expectations of 195k but above the previous month’s revised reading of 128k.



The chart above shows the level of ADP private payrolls.

The U.S. goods trade deficit widened to \$91.18 billion in June, from \$88.8 billion in May. Imports rose 4.7 billion to \$256.0 billion, while exports increased 2.4 billion to \$164.8 billion.



The chart above shows the level of the U.S. trade balance in goods.

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

Economic Releases						
No economic releases for the rest of today						
EST	Indicator			Expected	Prior	Rating
10:00	Pending Home Sales	m/m	Jul	-1.0%	0.3%	**
10:00	Pending Home Sales NSA	y/y	Jul	-15.7%	-14.8%	**
Federal Reserve						
No Fed speakers or events for the rest of today						

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	Consumer Confidence Index	y/y	Aug	36.2	37.1	37.4	**	Equity bearish, bond bullish
Australia	Building Approvals	m/m	Jul	-8.1%	-7.7%	-7.9%	***	Equity and bond neutral
	CPI	y/y	Jul	0.1%	-1.3%	-1.0%	***	Equity bearish, bond bearish
New Zealand	Building Permits	m/m	Jul	-5.2%	3.5%	3.4%	**	Equity bearish, bond bullish
EUROPE								
Eurozone	Consumer Confidence	m/m	Aug F	-16.0	-16.0		**	Equity and bond neutral
	Economic Confidence	m/m	Aug	93.3	94.5	93.5	***	Equity and bond neutral
	Industrial Confidence	m/m	Aug	-10.3	-9.4	-9.3	***	Equity bearish, bond bullish
	Services Confidence	m/m	Aug	3.9	5.7	5.4	**	Equity bearish, bond bullish
Germany	Import Price Index	y/y	Jul	-13.2%	-11.4%	-13.1%	**	Equity and bond neutral
	CPI	y/y	Aug P	6.1%	6.2%	6.0%	***	Equity and bond neutral
	CPI, EU Harmonized	y/y	Aug P	6.4%	6.5%	6.4%	**	Equity and bond neutral
Italy	Consumer Confidence	m/m	Aug	106.5	106.7	106.6	***	Equity and bond neutral
	Manufacturing Confidence	m/m	Aug	97.8	99.3	99.1	***	Equity bullish, bond bearish
	Economic Sentiment	m/m	Aug	106.8	109.1	108.9	**	Equity bullish, bond bearish
	Industrial Sales WDA	y/y	Jun	1.3%	-0.5%	1.6%	*	Equity bullish, bond bearish
UK	Mortgage Approvals	m/m	Jul	49.4k	54.7k	54.6k	**	Equity and bond neutral
Switzerland	KOF Leading Indicator	m/m	Aug	91.1	92.2	92.1	**	Equity bearish, bond bullish
	Credit Suisse Survey Expectations	m/m	Aug	-38.6	-32.6		**	Equity and bond neutral
AMERICAS								
Mexico	International Reserves Weekly	w/w	25-Aug	\$203719m	\$203482m		*	Equity and bond neutral
Brazil	FGV Inflation IGPM	y/y	Aug	-7.20%	-7.72%	-7.47%	***	Equity and bond neutral
Brazil	Formal Job Creation	m/m	Jul	142702	157198	156615	**	Equity and bond neutral

Financial Markets

The table below highlights some of the indicators that we follow on a daily basis. 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.

doe	Today	Prior	Change	Trend
3-mo Libor yield (bps)	567	565	2	Up
3-mo T-bill yield (bps)	531	531	0	Up
TED spread (bps)	LIBOR and the TED Spread have been discontinued.			
U.S. Sibor/OIS spread (bps)	540	540	0	Up
U.S. Libor/OIS spread (bps)	542	542	0	Up
10-yr T-note (%)	4.14	4.12	0.02	Flat
Euribor/OIS spread (bps)	378	377	1	Up
Currencies	Direction			
Dollar	Flat			Down
Euro	Flat			Up
Yen	Down			Down
Pound	Up			Up
Franc	Flat			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.

DOE Inventory Report	Price	Prior	Change	Explanation
Energy Markets				
Brent	\$86.00	\$85.49	0.60%	
WTI	\$81.68	\$81.16	0.64%	
Natural Gas	\$2.71	\$2.66	1.73%	
Crack Spread	\$34.77	\$34.39	1.12%	
12-mo strip crack	\$29.14	\$28.96	0.63%	
Ethanol rack	\$2.40	\$2.40	0.21%	
Metals				
Gold	\$1,940.01	\$1,937.54	0.13%	
Silver	\$24.64	\$24.72	-0.33%	
Copper contract	\$382.80	\$383.90	-0.29%	
Grains				
Corn contract	\$490.50	\$486.75	0.77%	
Wheat contract	\$606.75	\$600.50	1.04%	
Soybeans contract	\$1,398.25	\$1,392.50	0.41%	
Shipping				
Baltic Dry Freight	1,107	1,080	27	
DOE Inventory Report				
	Actual	Expected	Difference	
Crude (mb)		-2.2		
Gasoline (mb)		-1.3		
Distillates (mb)		-1.0		
Refinery run rates (%)		0.5%		
Natural gas (bcf)		31		

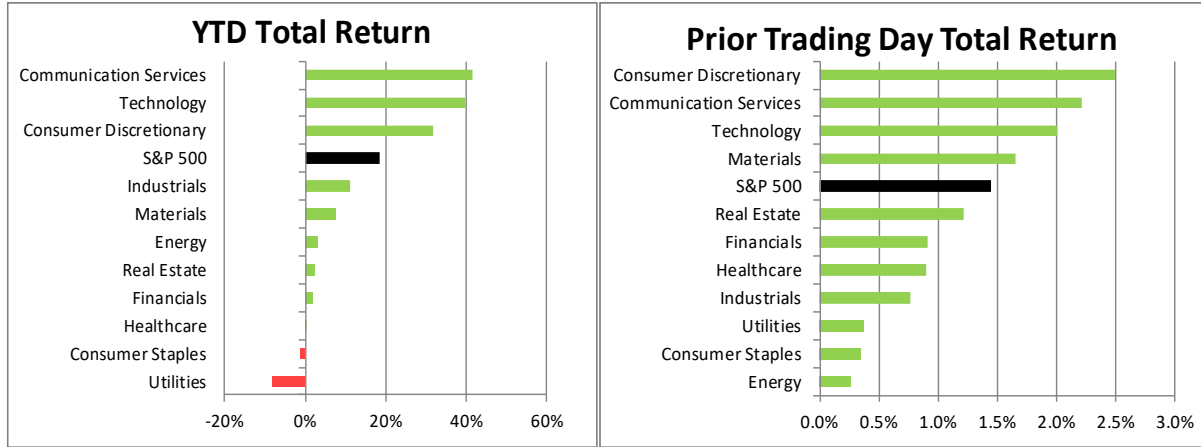
Weather

The 6-10 and 8-14 day forecasts currently call for warmer-than-normal temperatures for most of the country, with below-normal temps in the Pacific region. The precipitation outlook shows dry conditions are expected in most states, with wet conditions in the northern Pacific region.

There are four atmospheric disturbances in the Atlantic Ocean. Hurricane Franklin is moving northward in the Atlantic Ocean. Hurricane Idalia has made landfall in Florida. The other two disturbances are deep in the Atlantic and have at most a 40% chance of cyclone formation within the next 48 hours.

Data Section

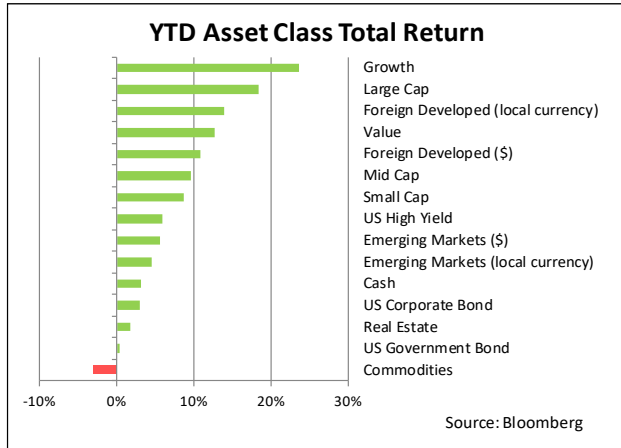
U.S. Equity Markets – (as of 8/29/2023 close)



(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 8/29/2023 close)

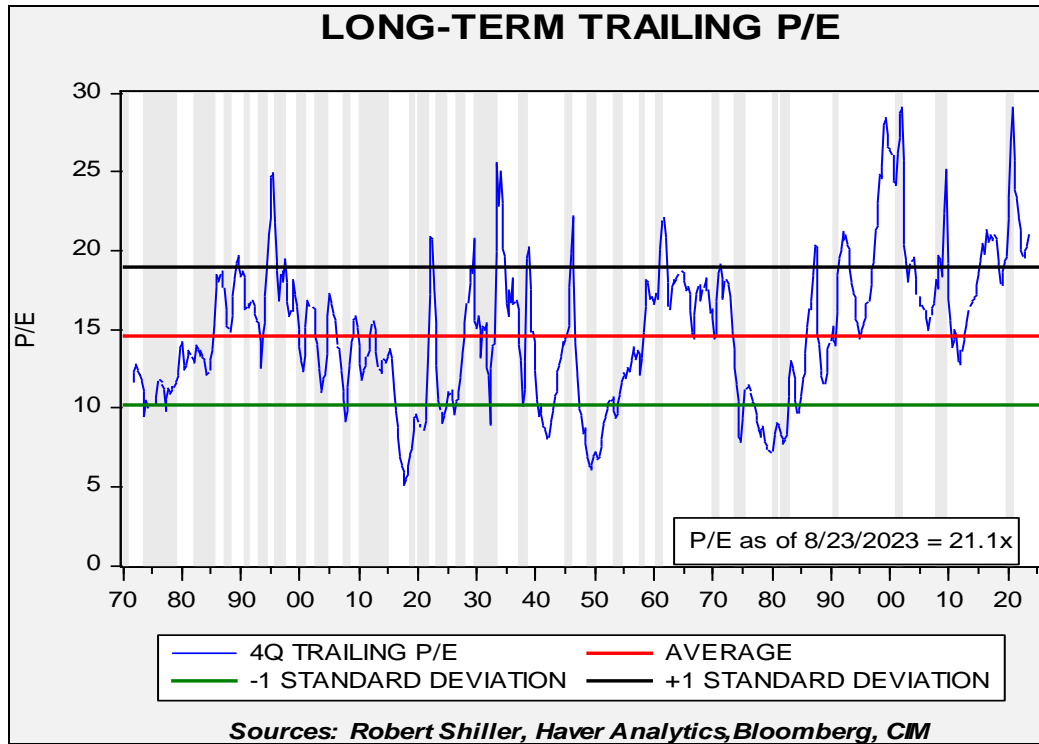


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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), U.S. Corporate Bond (iShares iBoxx \$ Investment Grade Corporate Bond ETF), U.S. Government Bond (iShares 7-10 Year Treasury Bond ETF), U.S. 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 24, 2023



Based on our methodology,¹ the current P/E is 21.1x, down 0.1x from last week. Improved earnings coupled with falling index values led to the modest decline in the multiple.

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 two actual quarters (Q3 and Q4) and two estimates (Q1 and 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.