

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: December 14, 2021—9:30 AM EST]** Global equity markets are generally lower this morning. In Europe, the EuroStoxx 50 is relatively unchanged from its prior close. In Asia, the MSCI Asia Apex 50 closed down 0.8%. Chinese markets were lower, with the Shanghai Composite down 0.5% from its prior close and the Shenzhen Composite down 0.1%. U.S. equity index futures are signaling a lower open.

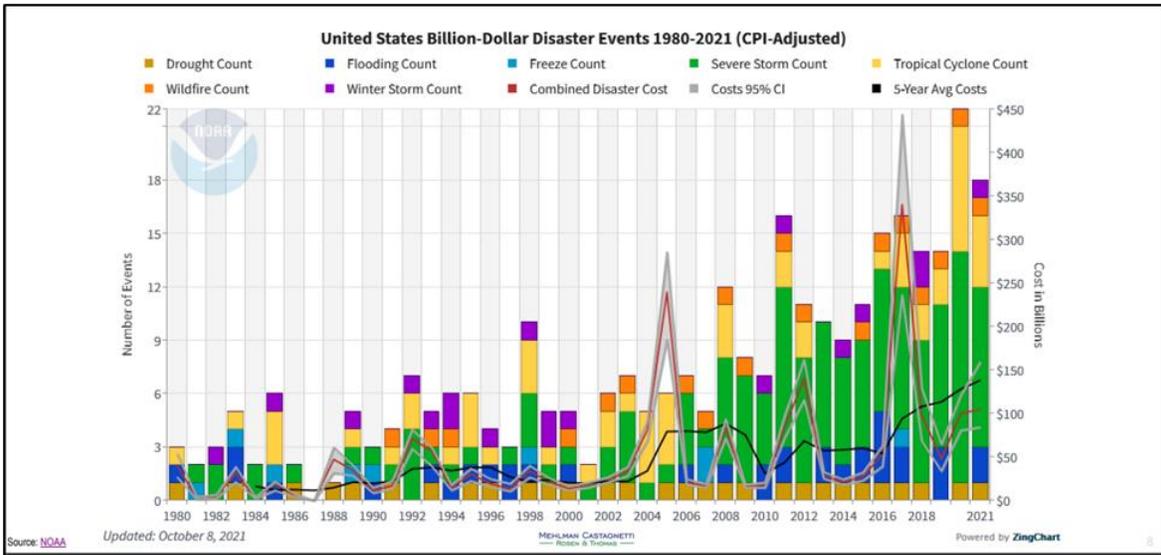
The Confluence macro team publishes a plethora of research reports and multimedia offerings on a weekly and quarterly basis, all available on our [website](#). We highlight recent publications below, with new items of the day emphasized in bold:

- **[Weekly Geopolitical Report \(12/13/2021\): “The 2022 Geopolitical Outlook”](#)**
- [Weekly Energy Update \(12/9/2021\)](#): Oil prices have tumbled on the Omicron variant and on the SPR release. We take a look at gasoline prices relative to wages.
- [Asset Allocation Q4 2021 Rebalance Presentation \(11/4/2021\)](#): A video discussion of our asset allocation process, Q4 2021 portfolio changes, and the macro environment
- [Asset Allocation Weekly \(12/10/2021\)](#) (with associated [podcast](#)): “The Omicron Problem”
- **[Confluence of Ideas podcast \(12/14/2021\): “The Regional Threats from the Taliban in Afghanistan”](#)**

*Note to readers: The Daily Comment will go on holiday after Friday’s comment and return on January 3, 2022. From all of us at Confluence Investment Management, have a Merry Christmas and Happy New Year!*

In today’s *Comment*, we open with a review of key U.S. news, including an update on the weekend’s tornadoes, the status of President Biden’s latest fiscal program, and the opening of the Federal Reserve’s policy meeting today. We next deal with a range of international news, including the recent U.S. pushback against China’s aggressive geopolitical moves. We wrap up with the latest developments regarding the coronavirus pandemic.

**U.S. Tornado Toll:** The number of confirmed fatalities from last weekend’s tornadoes [rose to 88](#), with the vast majority of the deaths in Kentucky. So far, we haven’t seen an estimate of insurable loss damages, but it could be high. Although meteorologists believe the unusually powerful storms for this time of year [had their origin in extraordinarily warm temperatures](#), they couldn’t yet tie them directly to global warming. All the same, we note that as global temperatures trend upward, the increased heat in the atmosphere has coincided with a rise in particularly devastating storms, especially over land, as shown in the graph below.



**U.S. Fiscal Policy:** President Biden [lobbied Senator Joe Manchin of West Virginia](#) by phone yesterday in another effort to garner the senator’s support for the Democrats’ \$1.75 trillion “Build Back Better” social policy and climate change legislation. However, neither side reported any breakthrough, other than agreeing to talk again in the coming days.

**U.S. Monetary Policy:** Today, the Fed [begins its latest two-day policy meeting](#). When the new policy statement is released tomorrow, the officials [are expected to say they will accelerate the tapering of their bond-buying to end the program by March](#), which would position them to start hiking the benchmark fed funds interest rate in the first half of the year if they so choose. However, Chair Powell’s [abrupt mutation into an inflation hawk](#) has some investors nervous about what the policymakers will actually do at the meeting. Until the decision is out, it could lead to further volatility in the markets as it did yesterday.

- As we noted in our *Comment* yesterday, most major central banks are holding a policy meeting this week, but [their expected policy actions range widely](#). Importantly, the IMF warned in its latest review of the British economy that the Bank of England [is already behind on tamping down inflation pressures and must not delay rate hikes](#), even as the fast-spreading Omicron mutation of the coronavirus has some observers thinking the central bank might punt on rate hikes this week.
- Separately, the Canadian government and the Bank of Canada yesterday [agreed to renew the central bank’s mandate to target 2% annual inflation](#), with a new emphasis on giving the central bank flexibility to address economic challenges and help obtain full employment when conditions warrant.
  - Under the renewed mandate, which runs until the end of 2026, the central bank will set rate policy to achieve 2% annual inflation or the midpoint of a 1% to 3% target range.
  - The bank will have flexibility in rate setting to achieve “maximum sustainable employment . . . The central bank will utilize the flexibility of the 1% to 3%

range only to an extent that is consistent with keeping medium-term inflation expectations well anchored at 2%.”

**United States-China:** In a major policy speech delivered in Jakarta, Secretary of State Blinken [criticized “Beijing’s aggressive actions” against its neighbors and reaffirmed Washington’s commitment](#) to an Indo-Pacific region “free from coercion and accessible to all.”

- Blinken said the U.S. plans to strengthen its treaty alliances with Japan, South Korea, Australia, the Philippines, and Thailand in order to counter China’s aggressive geopolitical moves. In addition, he said the Biden administration is developing a “comprehensive Indo-Pacific economic framework” that would include co-operation on trade, the digital economy, technology, supply chain resilience, and investments in decarbonization.
- Although the speech broke little new ground, it drew a sharp rebuke from the Chinese government, which understands that its effort to build up Chinese power and geopolitical influence could be hemmed in to the extent that foreign nations understand the threat they face from China.

**United States-China-Japan:** Elaborating on comments he made earlier this month, former Japanese Prime Minister Abe said that any Chinese attack on a U.S. military vessel in a contingency concerning Taiwan [could become a situation allowing Japan to exercise the right of collective self-defense, i.e., military action](#). Pointing out that Yonaguni Island — Japan’s westernmost territory — is only 110 kilometers away from Taiwan, Abe said, “If something happens here, it will definitely become a crucial situation” affecting Japan’s peace and security as stipulated in the country’s security legislation. The statement points to a growing realization in Japan that the country faces a severe security risk from China and needs to strengthen its alliance with the U.S. to counter it.

**Norway:** NATO General Secretary Jens Stoltenberg [said he has applied to become the governor of Norway’s central bank starting next October](#). Stoltenberg, who formerly served as Norway’s prime minister, and finance minister before that, is a political heavyweight who would likely be a front-runner for the position, along with current deputy governor Ida Wolden Bache.

- Stoltenberg’s supporters have said that having a political heavyweight in the role would be desirable and that few understand Norway’s economy as well as Stoltenberg, who, as finance minister, came up with the spending rule that decides how much government can take out of the oil fund each year. Stoltenberg’s leadership of the central bank would likely be well received by investors.
- In contrast, however, Stoltenberg’s critics argue that the credibility of both Norges Bank and the country’s sovereign wealth fund would be placed at risk by putting a former politician — and one who is close friends with current Labor leader and prime minister Jonas Gahr Støre— in charge.

**Global Supply Chains:** Data from the OECD [indicate corporate capital investment fell](#) in the U.S., Canada, Japan, Germany, South Korea, the Netherlands, and Switzerland during the third quarter, despite the excess of demand over supply that’s driving up prices worldwide. The

causes of the slowdown appear mixed. Many businesses cite price rises, supply-chain problems, and uncertainty regarding how long the surge in consumer spending will last.

**COVID-19:** Official data show confirmed cases [have risen to 270,933,004 worldwide, with 5,316,286 deaths](#). In the U.S., confirmed cases rose to 50,120,820, with 798,722 deaths. (For an interactive chart that allows you to compare cases and deaths among countries, scaled by population, click [here](#).) Meanwhile, in data on the U.S. vaccination program, [the number of people who have received at least their first shot totals 239,274,656](#). The data show that 72.1% of the U.S. population has now received at least one dose of a vaccine, and 60.9% of the population is fully vaccinated.

### *Virology*

- U.K. officials [reported the first death of someone infected with the Omicron mutation](#) and the hospitalization of at least ten others. The government continues to raise the alarm about a massive wave of Omicron infections and the potential need to impose strict new lockdowns to combat them. In Denmark, Omicron [is already driving record-high infections and is expected to become the dominant strain this week](#).
- Chinese officials also [reported their country's first Omicron infection](#). The infection was discovered in a traveler who arrived in the northern port city of Tianjin from overseas last Thursday. Later, state television [reported that a second Omicron case was discovered in the southern city of Guangzhou](#), raising fears that the government might clamp down on factory activity and further snarl global supply chains under its “zero-tolerance” COVID-19 policy.
- In the U.S., an administration official warned that an “explosion” of new COVID-19 cases driven by Omicron [is now imminent](#). Even though most cases won't be severe, the sheer number will ensure that hospitalizations will surge and put further stress on the nation's healthcare system.
- In California, the state government [will again require masking in all public indoor settings, regardless of vaccination status](#), as it confronts rising case rates ahead of the winter holidays and uncertainty about the Omicron variant.
- To encourage vaccinations, grocery chain Kroger (KR, \$45.63) [said it would no longer provide two weeks of paid emergency leave for unvaccinated employees](#) who contract COVID-19 unless local jurisdictions require otherwise. The company will also add a \$50 monthly surcharge to company health plans for unvaccinated managers and other non-union employees.
- Based on final trial results, Pfizer (PFE, \$55.20) [said its antiviral treatment for COVID-19 cuts the risk of hospitalization or death by up to 89% in high-risk patients](#).
  - The trial was held while Delta was the dominant variant, but Pfizer said early lab work suggested the antiviral will continue to work against Omicron, and other studies are underway.
  - Pfizer's apparent success with its antiviral, known as Paxlovid, underlines how the scientific community is broadening its toolkit against the coronavirus. Not only have the vaccines proven to be safe and effective in preventing the most

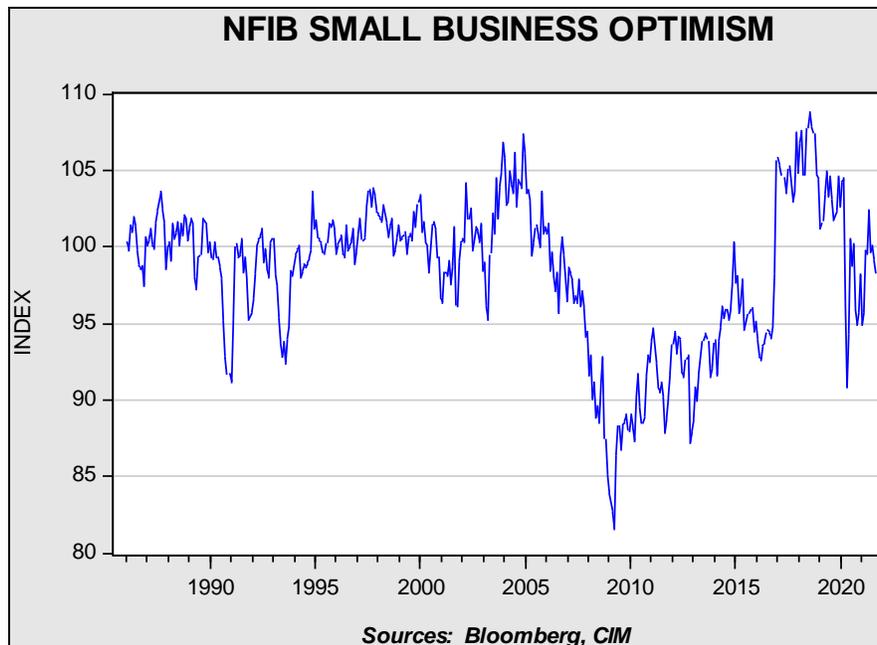
serious illnesses from COVID-19, but now antiviral treatments are starting to prove their worth in managing the disease among those who get infected. Since that provides hope that society can eventually live relatively comfortably with the virus, it's a positive for the global economy and risk markets, at least as long as a dangerous new mutatiois doesn't arise.

#### *Economic and Financial Market Impacts*

- In its monthly report, the International Energy Agency [predicted that the Omicron mutation will only modestly reduce global oil demand](#) in the coming months. Coupled with rising output in both OPEC and non-OPEC countries, that should help bring the market back into balance and eliminate the recent tightness that drove up prices earlier this year, according to the IEA.

### **U.S. Economic Releases**

Sentiment among U.S. small business owners rose slightly in November, according to the National Federation of Independent Business (NFIB). Last month, the NFIB Small Business Optimism Index was in line with expectations at 98.4.



The chart above shows the level of NFIB Small Business Optimism.

The prices paid by produced surged in November. The PPI Final Demand Index rose 0.8% from the prior month compared to expectations of 0.5%. Excluding food and energy, PPI rose 0.7% from the prior month compared to expectations of 0.4%. Lastly, Core PPI, which excludes food, energy, and trade services, rose 0.7% from the prior month compared to expectations of 0.4%.



The chart above shows the annual change in the headline and Core PPI. Headline PPI rose 9.7% from the prior year, while Core PPI rose 6.9%.

There are no economic releases or Fed events scheduled for the rest of the day.

### 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.

	Indicator			Current	Prior	Expected	Rating	Market Impact
<b>ASIA-PACIFIC</b>								
<b>Japan</b>	Industrial Production	m/m	Oct	1.8%	1.1%		***	Equity bullish, bond bearish
	Capacity Utilization	m/m	Oct	6.2%	-7.3%		***	Equity bullish, bond bearish
<b>India</b>	CPI	y/y	Nov	4.91%	4.48%	5.10%	***	Equity bullish, bond bearish
	Wholesale Prices	y/y	Nov	14.23%	12.54%	11.98%	**	Equity bearish, bond bullish
<b>Australia</b>	ANZ Roy Morgan Consumer Confidence	w/w	12-Dec	108.0	107.5		***	Equity bullish, bond bearish
	NAB Business Conditions	m/m	Nov	12	11		**	Equity bearish, bond bullish
	NAB Business Confidence	m/m	Nov	12	21		**	Equity bearish, bond bullish
<b>EUROPE</b>								
<b>Eurozone</b>	Industrial Production WDA	y/y	Oct	3.3%	5.2%	3.0%	***	Equity bullish, bond bearish
<b>UK</b>	Claimant Count Rate	m/m	Nov	4.9%	5.1%		***	Equity bullish, bond bearish
	Jobless Claims Change	m/m	Nov	-49.8k	-14.9k		***	Equity and bond neutral
	Average Weekly Earnings 3M/YoY	y/y	Oct	4.9%	5.8%	4.6%	**	Equity bullish, bond bearish
	Weekly Earnings ex Bonus 3M/YoY	y/y	Oct	4.3%	4.9%	4.0%	**	Equity bullish, bond bearish
	ILO Unemployment Rate 3Mths	m/m	Oct	4.2%	4.3%	4.2%	**	Equity and bond neutral
	Employment Change 3M/3M	m/m	Oct	149k	247k	225k	**	Equity bearish, bond bullish
<b>Switzerland</b>	Producer & Import Prices	m/m	Nov	0.5%	0.6%		**	Equity and bond neutral
<b>AMERICAS</b>								
<b>Brazil</b>	Trade Balance Weekly	w/w	12-Dec	\$652m	\$1075m		**	Equity bearish, bond bullish
<b>Canada</b>	Bloomberg Nanos Confidence	w/w	10-Dec	60.0	59.8		***	Equity and bond neutral
<b>Mexico</b>	ANTAD Same-Store Sales	y/y	Nov	9.3%	11.6%		**	Equity bearish, bond bullish

## 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.

Fixed Income	Today	Prior	Change	Trend
3-mo Libor yield (bps)	20	20	0	Down
3-mo T-bill yield (bps)	3	5	-2	Neutral
TED spread (bps)	17	15	2	Neutral
U.S. Libor/OIS spread (bps)	9	9	0	Down
10-yr T-note (%)	1.43	1.42	0.01	Down
Euribor/OIS spread (bps)	-60	-59	-1	Neutral
EUR/USD 3-mo swap (bps)	14	15	-1	Down
<b>Currencies</b>	<b>Direction</b>			
Dollar	Down			Neutral
Euro	Up			Up
Yen	Down			Neutral
Pound	Up			Neutral
Franc	Up			Neutral
<b>Central Bank Action</b>	<b>Current</b>	<b>Prior</b>	<b>Expected</b>	
China Lending Facility Rate		2.950%		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.

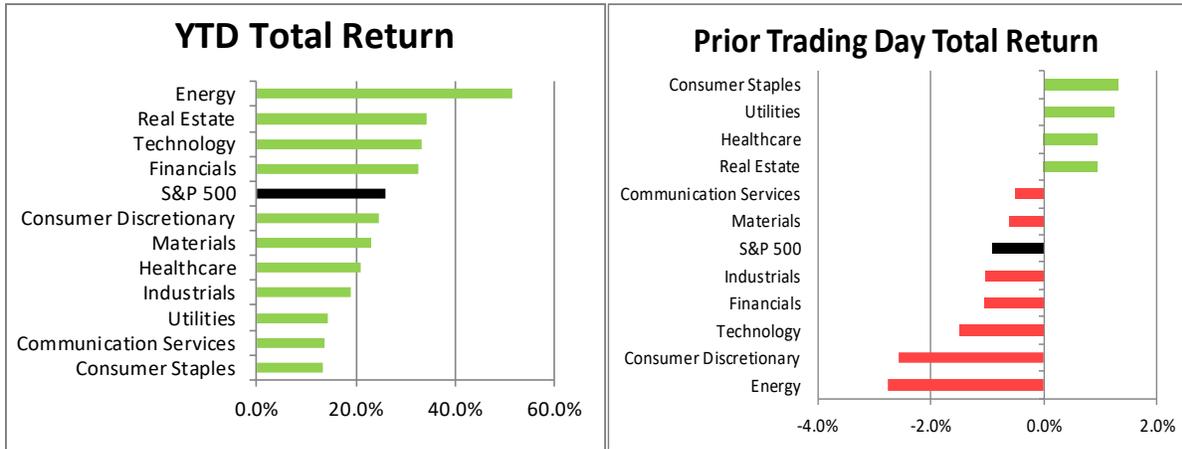
	Price	Prior	Change	Explanation
<b>Energy Markets</b>				
Brent	\$74.46	\$74.39	0.09%	
WTI	\$71.34	\$71.29	0.07%	
Natural Gas	\$3.73	\$3.79	-1.79%	
Crack Spread	\$19.36	\$19.48	-0.61%	
12-mo strip crack	\$20.08	\$20.21	-0.64%	
Ethanol rack	\$3.29	\$3.30	-0.40%	
<b>Metals</b>				
Gold	\$1,785.29	\$1,786.67	-0.08%	
Silver	\$22.20	\$22.33	-0.61%	
Copper contract	\$428.30	\$428.40	-0.02%	
<b>Grains</b>				
Corn contract	\$582.75	\$585.00	-0.38%	
Wheat contract	\$782.75	\$788.75	-0.76%	
Soybeans contract	\$1,247.50	\$1,250.75	-0.26%	
<b>Shipping</b>				
Baltic Dry Freight	3,216	3,272	-56	
<b>DOE inventory report</b>				
	<b>Actual</b>	<b>Expected</b>	<b>Difference</b>	
Crude (mb)		-2.3		
Gasoline (mb)		2.0		
Distillates (mb)		0.2		
Refinery run rates (%)		0.50%		

## Weather

The 6-10 day and 8-14-day forecasts currently call for warmer-than-normal temperatures throughout the South, Midwest, and Great Plains, with cooler-than-normal temperatures only along the Pacific and Rocky Mountain regions. The forecasts call for wet conditions throughout most of the country, with dry conditions in the Great Plains.

**Data Section**

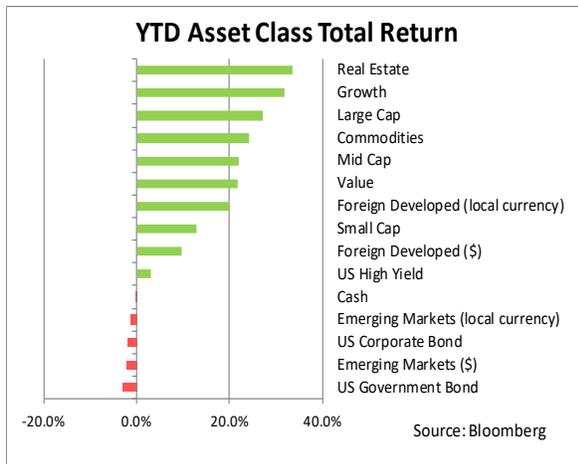
**U.S. Equity Markets – (as of 12/13/2021 close)**



(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 12/13/2021 close)**

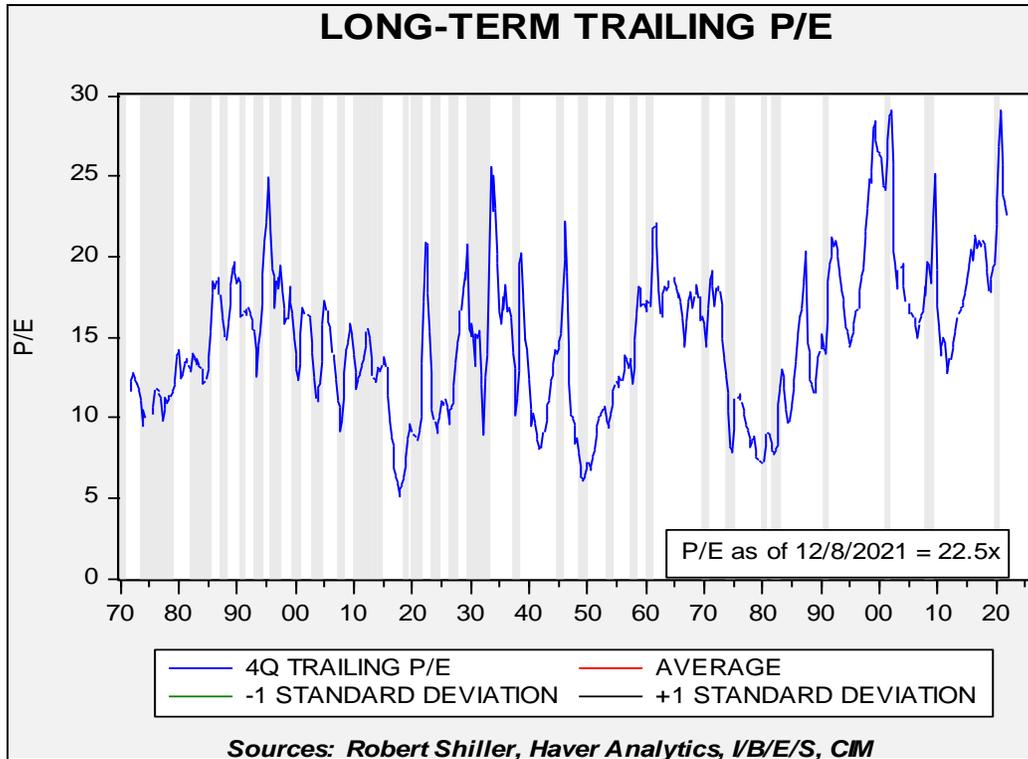


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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

December 9, 2021



Based on our methodology,<sup>1</sup> the current P/E is 22.5x, up 0.2x from last week. The rise in the multiple is due to higher index prices.

*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.*

<sup>1</sup> 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 I/B/E/S 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.