

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: January 22, 2021—9:30 AM EST] Global equity markets are generally lower this morning. The EuroStoxx 50 is down 1.0% from its last close. In Asia, the MSCI Asia Apex 50 is also down 1.0%. Chinese markets were mixed, with the Shanghai Composite up 0.4% from the prior close and the Shenzhen Composite down 0.3%. U.S. equity index futures are signaling a lower open. With 62 companies having reported, the S&P 500 Q4 earnings stand at \$38.90, higher than the \$37.94 forecast for the quarter. The forecast reflects a 9.7% decrease from Q4 2019 earnings. Thus far this quarter, 87.1% of the companies have reported earnings above forecast, while 9.7% have reported earnings below forecast.

Good morning. Global equities are lower as fears of a third wave of the coronavirus continue to mount. New developments related to the pandemic lead our coverage today, followed by a discussion of President Biden's first day in office. The report will conclude with a roundup of economic and international news. A new [Asset Allocation Weekly](#) is available, along with the associated [podcast](#) and [chart book](#). The Weekly Energy Update won't be published until Monday as the DOE has decided to publish the weekly data today.

New COVID Variants: As cases begin to rise globally due to various mutations of COVID-19, there are growing concerns that the virus could be with us longer than anticipated. So far, countries that had success in containing the virus last year are seeing a spike in cases. Both China and Japan have re-imposed new travel restrictions in response to the virus as cases have risen in both Beijing and Tokyo. Meanwhile, there have been several studies suggesting that [vaccines may be less effective in protecting](#) against the South African variant of the virus.

COVID-19: The [number of reported cases](#) is 97,425,832 with 2,087,820 fatalities. In the U.S., there are 24,610,051 confirmed cases with 409,641 deaths. For illustration purposes, the *FT* has created an [interactive chart](#) that allows one to compare cases across nations using similar scaling metrics. The *FT* has also issued an [economic tracker](#) that looks across countries with high-frequency data on various factors. The [CDC reports](#) that 37,960,000 doses of the vaccine have been distributed, with 15,053,257 doses injected. The number of second doses, which would grant the highest level of immunity, is 2,394,961. The next challenge will be when the U.K./South African variant becomes more common in the U.S. Both variants spread faster and could lead to another surge in the coming weeks.

Virology

- Even though cases are falling, there is fear among [public health experts that it is still unclear whether the worst is behind us](#).

- New variants in the U.K., Ireland, Brazil, and South Africa have experts suspecting that another spike could soon be on the horizon.
- President Biden has warned that he expects deaths to rise by an additional 100,000 by next month.
- Florida will require people seeking [COVID-19 vaccines to be permanent or seasonal residents of the state](#) amid concerns that foreign visitors were flying in to secure shots.
- On Thursday, Texas [reported its second-biggest daily increase](#) in coronavirus fatalities on record, pushing the state's death toll above 33,000.
- China will give half a million doses of [Sinopharm's vaccine to Pakistan](#) free of charge by the end of January, Pakistan's foreign minister said on Thursday
- [Five people were killed](#) by a fire that erupted at a COVID-19 vaccine-making factory in India.
- During a virtual meeting, [Dr. Anthony S. Fauci reassured the World Health Organization](#) that the United States is committed to working closely with other nations to implement a more effective global response to the pandemic.
- Japan walked back [its goal to secure enough targeted](#) supplies of COVID-19 vaccines by June, one month before the planned start of the Tokyo Olympics.
 - There have been claims that the country will cancel the Olympics altogether and target for 2032, but Japan has since [denied those rumors](#).
- The European Commission proposed identifying “dark red” coronavirus hot spots from which all but essential travel would be discouraged. The proposal was made following fears of a third wave.
- Zimbabwe's government [scaled down operations](#) amid a second wave of coronavirus infections.

Biden Administration: In his first full day in office, President Biden signed executive orders invoking the Defense Production Act that will allow for the promotion of vaccine production and improved testing, especially for travelers. In addition, this administration appears to be posturing to take a tougher stance against Russia, while also maintaining some of the China policies of the previous administration. Lastly, there appear to be more details about the impending impeachment trial of former President Trump. Below are our thoughts about these stories:

- The new executive orders have been aimed at providing some relief while the administration works to push through its ambitious stimulus plan. As we mentioned in yesterday's [report](#), executive orders have been used as a de facto way to get things done in Washington as partisanship has made cooperation politically toxic. However, Biden has emphasized that he would look to achieve some bipartisan support to get his bill passed. On Thursday, a bipartisan group of 16 senators that included Mitt Romney (R-Utah), Susan Collins (R-Maine), and Joe Manchin (D-West Virginia) met with Biden aide [Brian Deese to discuss details of the plan](#). So far, none have come out for or against the proposal, although Romney suggested he isn't sure if he is interested in another round of stimulus.
- Outside of executive orders, the president has made some changes to foreign policy. The president has pushed for a [five-year extension of the Nuclear Arms Treaty](#) with Russia, while also stating that he will seek to hold the country accountable for its perceived

aggressions against the U.S. and its dissidents. At issue is the SolarWinds cyber-attack that took place last year as well as the attempted murder of Putin rival Alexei Navalny. The president has stated that he has sought [a report of Russian misdeeds](#) and will come to a decision on a response after receiving the findings of this report.

- The president's proposed \$1.9 trillion stimulus package is looking to make its way through Congress, which will likely be the first test of his political capital. House Speaker Nancy Pelosi has agreed to take up the measure in February, vowing a speedy passage, while Senate Republicans have raised concerns over the swelling of the federal deficit at [Janet Yellen's confirmation](#) hearing on Tuesday. Although we are doubtful of a quick passage of the bill through Congress, as it would need 60 votes to avoid a filibuster, we are optimistic that the more palatable parts of the bill have a great chance of making its way through Congress. The \$15/hour minimum wage will likely not be part of the final bill. That being said, the president is expected to sign an [executive order](#) that would boost the minimum wage for federal workers.
- One of the biggest obstacles of a speedy passage of the bill is the upcoming impeachment trial for former President Donald Trump. On Thursday, Senator Mitch McConnell stated that he would like a [hearing to begin in February](#) in order to give Mr. Trump's defense team time to mount a defense. He just recently [found an attorney to represent him](#) during the hearings on Thursday. So far, Nancy Pelosi has not formally sent the articles of impeachment to the Senate, but she is expected to do so any day now. An impeachment hearing could potentially distract senators from being able to push Biden's stimulus through Congress, although the Democrats have argued that a trial should be straightforward and quick. A conviction could prevent President Trump from running again in 2024, but in order for that to happen he would need 17 Republicans to find him guilty. The possibility of a conviction seems slim as Trump is still popular within his party. So far, prediction markets have the count between 53-56 votes against the president, although there isn't much confidence of this outcome.

International news:

- Google threatened to make [its search engine unavailable in Australia](#) if the government moves ahead with plans to make tech giants pay for news content.
- [Israeli airstrikes](#) targeted a site near the city of Hama in northwestern Syria. The airstrikes are believed to be aimed at areas connected to Iran's missile production.
- [Twin suicide bombings](#) ripped through a crowded marketplace in Baghdad, killing at least 32 people and wounding at least 75 others. Islamic State has taken responsibility for the attack, making this attack its first in two years.
- Critics of Thailand's royal family are now [facing criminal charges](#) as more people begin testing the political taboo of questioning the family's importance in Thai society.

Economic News:

- On Thursday, Janet Yellen provided a [written response to members of the Senate Finance Committee](#). In it, she expressed an openness to work with Congress to protect households earning "less than \$400,000" from losing their tax cuts, suggested the wealthy will be audited at higher rates, and mentioned that she will not seek to reopen the Fed lending phased out by her predecessor but will continue to act within the mandate. In

addition, she stated that Biden will not actively seek a weaker currency and is expected to return to the Rubin compromise, where the U.S. says it supports a “strong dollar” but merely means it won’t use the exchange rate as a policy tool.

- Each of the [12 Federal Reserve bank presidents](#) were renewed to a five-year term on Thursday.

U.S. Economic Releases

There were no U.S. data releases or Federal Reserve events so far today.

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

Economic Releases						
EDT	Indicator			Expected	Prior	Rating
9:45	Markit US Manufacturing PMI	m/m	Jan P	56.5	57.1	**
9:45	Markit US Services PMI	m/m	Jan P	53.4	54.8	**
9:45	Markit US Composite PMI	m/m	Jan P	--	55.3	**
10:00	Existing Home Sales	m/m	Dec	6.56m	6.69m	**
10:00	Existing Home Sales	m/m	Dec	-1.9%	-2.5%	**
Fed Speakers or Events						
No speakers or events scheduled						

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
ASIA-PACIFIC								
Japan	Nati CPI	y/y	Dec	1.2%	-0.9%	-1.3%	**	Equity bullish, bond bearish
	Nati CPI Ex Fresh Food	y/y	Dec	1.0%	-0.9%	-1.1%	**	Equity bullish, bond bearish
	Jibun Bank Japan PMI Mfg	m/m	Jan P	49.7	50.0		***	Equity bearish, bond bullish
	Jibun Bank Japan PMI Services	m/m	Jan P	45.7	47.7		**	Equity bearish, bond bullish
	Jibun Bank Japan PMI Composite	m/m	Jan P	46.7	48.5		**	Equity bearish, bond bullish
Australia	Markit Australia PMI Mfg	m/m	Jan P	57.2	55.7		***	Equity bullish, bond bearish
	Markit Australia PMI Services	m/m	Jan P	55.8	57.0		**	Equity and bond neutral
	Markit Australia PMI Composite	m/m	Jan P	56.0	56.6		**	Equity and bond neutral
	Retail Sales MoM	m/m	Dec P	-4.2%	7.1%	-1.5%	**	Equity bearish, bond bullish
New Zealand	BusinessNZ Manufacturing PMI	m/m	Dec	48.7	54.7		***	Equity bearish, bond bullish
	CPI	m/m	4Q	1.4%	1.4%	1.1%	**	Equity and bond neutral
Europe								
Eurozone	Markit Eurozone Manufacturing PMI	m/m	Jan P	54.7	55.2	54.4	***	Equity and bond neutral
	Markit Eurozone Services PMI	m/m	Jan P	45.0	46.4	44.5	**	Equity and bond neutral
	Markit Eurozone Composite PMI	m/m	Jan P	47.5	49.1	47.6	**	Equity and bond neutral
Germany	Markit/BME Germany Manuf. PMI	m/m	Jan P	57.0	58.3	57.2	***	Equity and bond neutral
	Markit Germany Services PMI	m/m	Jan P	46.8	47.0	45.0	**	Equity bullish, bond bearish
	Markit/BME Germany Composite PMI	m/m	Jan P	50.8	52.0	50.0	**	Equity and bond neutral
France	Manufacturing Confidence	m/m	Jan	98.0	94.0	94.0	*	Equity and bond neutral
	Markit France Manufacturing PMI	m/m	Jan P	51.5	51.1	50.5	***	Equity bullish, bond bearish
	Markit France Services PMI	m/m	Jan P	46.5	49.1	48.4	**	Equity bearish, bond bullish
	Markit France Composite PMI	m/m	Jan P	47.0	49.5	49.0	**	Equity bearish, bond bullish
United Kingdom	GfK Consumer Confidence	m/m	Jan	-28	-26	-30	*	Equity and bond neutral
	Public Finances (PSNCR)	m/m	Dec	40.6b	23.6b		*	Equity and bond neutral
	PSNB ex Banking Groups	m/m	Dec	34.1b	26.1b	32.0b	**	Equity and bond neutral
	Public Sector Net Borrowing	m/m	Dec	33.4b	25.4b	31.4b	*	Equity and bond neutral
	Retail Sales Ex Auto Fuel YoY	y/y	Dec	6.4%	5.3%	7.4%	**	Equity and bond neutral
	Retail Sales Inc Auto Fuel YoY	y/y	Dec	2.9%	2.1%	4.0%	*	Equity and bond neutral
	Markit UK PMI Manufacturing SA	m/m	Jan P	52.9	57.5	53.6	***	Equity bearish, bond bullish
	Markit/CIPS UK Services PMI	m/m	Jan P	38.8	49.4	45.0	**	Equity bearish, bond bullish
	Markit/CIPS UK Composite PMI	m/m	Jan P	40.6	50.4	45.5	**	Equity bearish, bond bullish
AMERICAS								
Canada	Retail Sales	m/m	Nov	1.3%	0.4%	0.0%	**	Equity bullish, bond bearish
	Retail Sales Ex Auto	m/m	Nov	2.1%	0.0%	0.3%	**	Equity bullish, bond bearish

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.

	Today	Prior	Change	Trend
3-mo Libor yield (bps)	22	22	0	Down
3-mo T-bill yield (bps)	7	7	0	Neutral
TED spread (bps)	15	15	0	Up
U.S. Libor/OIS spread (bps)	8	8	0	Up
10-yr T-note (%)	1.09	1.11	-0.02	Neutral
Euribor/OIS spread (bps)	-54	-54	0	Neutral
EUR/USD 3-mo swap (bps)	5	4	1	Down
Currencies	Direction			
dollar	Up			Down
euro	Flat			Up
yen	Down			Up
pound	Down			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.

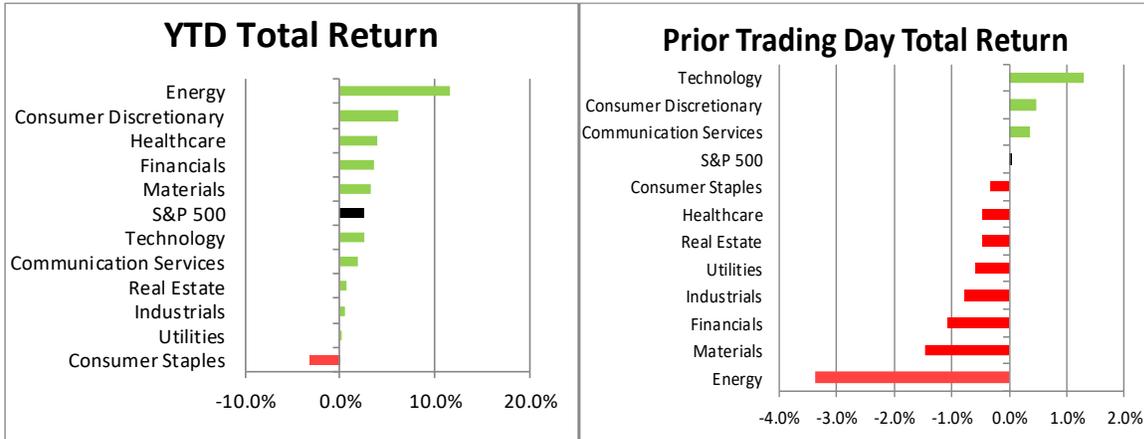
	Price	Prior	Change	Explanation
Energy Markets				
Brent	\$54.69	\$56.10	-2.51%	
WTI	\$51.70	\$53.13	-2.69%	
Natural Gas	\$2.44	\$2.49	-2.17%	
Crack Spread	\$12.48	\$12.72	-1.93%	
12-mo strip crack	\$14.20	\$14.43	-1.57%	
Ethanol rack	\$1.66	\$1.66	0.10%	
Metals				
Gold	\$1,842.19	\$1,870.02	-1.49%	
Silver	\$25.19	\$25.94	-2.87%	
Copper contract	\$364.75	\$364.15	0.16%	
Grains				
Corn contract	\$515.25	\$524.25	-1.72%	
Wheat contract	\$645.50	\$660.75	-2.31%	
Soybeans contract	\$1,340.00	\$1,370.25	-2.21%	
Shipping				
Baltic Dry Freight	1837	1828	9	
DOE inventory report				
	Actual	Expected	Difference	
Crude (mb)		-1.3		
Gasoline (mb)		2.6		
Distillates (mb)		1.6		
Refinery run rates (%)		-0.50%		
Natural gas (bcf)		-169.0		

Weather

The 6-10 and 8-14 day forecasts currently call for cooler than normal temperatures throughout the Southwest and Northeast, with warmer temperatures from the upper Midwest to the Gulf Coast. Wetter than normal conditions are expected on the West Coast and throughout the Mississippi Valley, with dry conditions expected in Texas and Florida.

Data Section

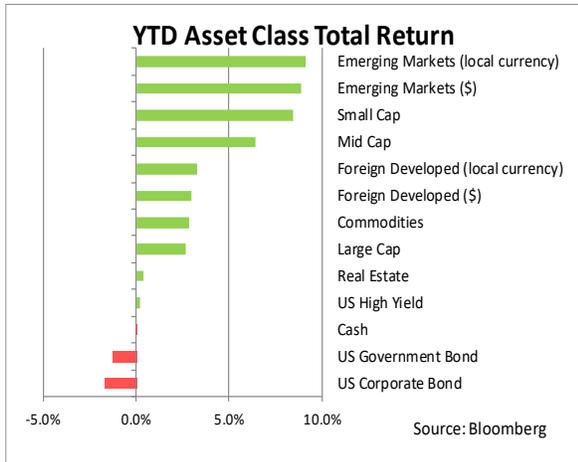
U.S. Equity Markets – (as of 1/21/2021 close)



(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 1/21/2021 close)

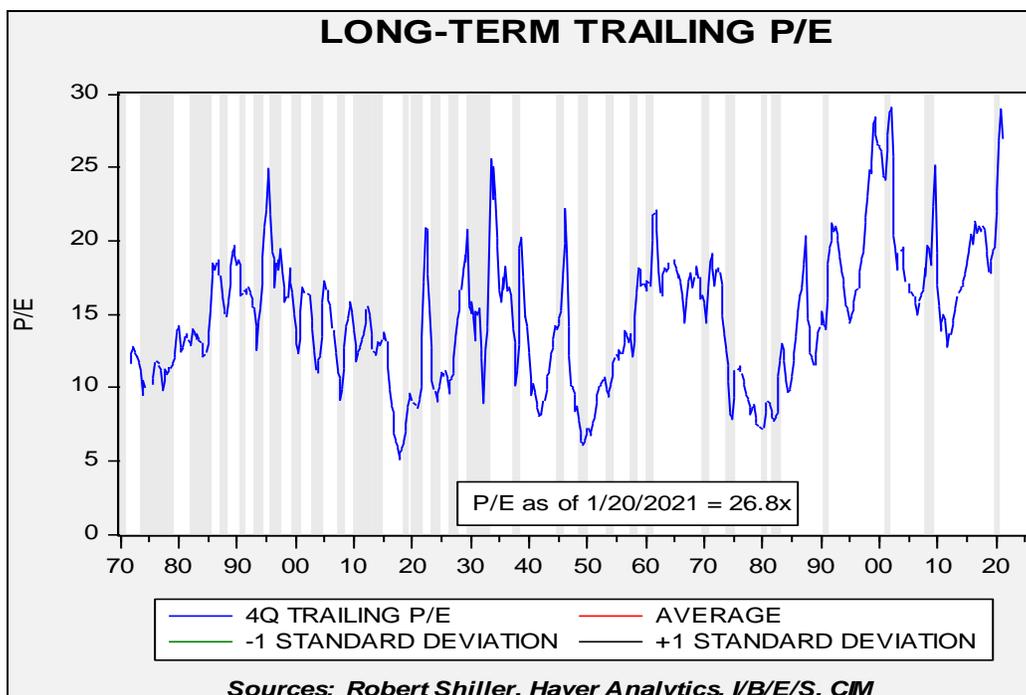


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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).

P/E Update

January 21, 2021



Based on our methodology,¹ the current P/E is 26.8x, down 0.3x from last week. Improving earnings offset higher equity values to bring a contraction of 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 I/B/E/S estimates which are updated regularly throughout the quarter; currently, the four-quarter earnings sum includes two actual quarters (Q2 and Q3) and two estimates (Q4 and Q1). 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.