Daily Comment

Confluence INVESTMENT MANAGEMENT

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Posted: June 6, 2025 — 9:30 AM ET] Global equity markets are mixed this morning. In Europe, the Euro Stoxx 50 closed up 0.2% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed down 0.4%. Chinese markets were mixed, with the Shanghai Composite little changed from its previous close and the Shenzhen Composite down 0.1%. US equity index futures are signaling a higher 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 in bold.

Bi-Weekly Geopolitical Report	Asset Allocation Bi-Weekly	Asset Allocation Quarterly	Of Note
"Why Greenland Matters" (5/27/25) + podcast	"The Japan Problem" (6/2/25) + podcast	Q2 2025 Report Q2 2025 Rebalance Presentation	Confluence of Ideas Podcast Value Equity Quarterly Update Business Cycle Report

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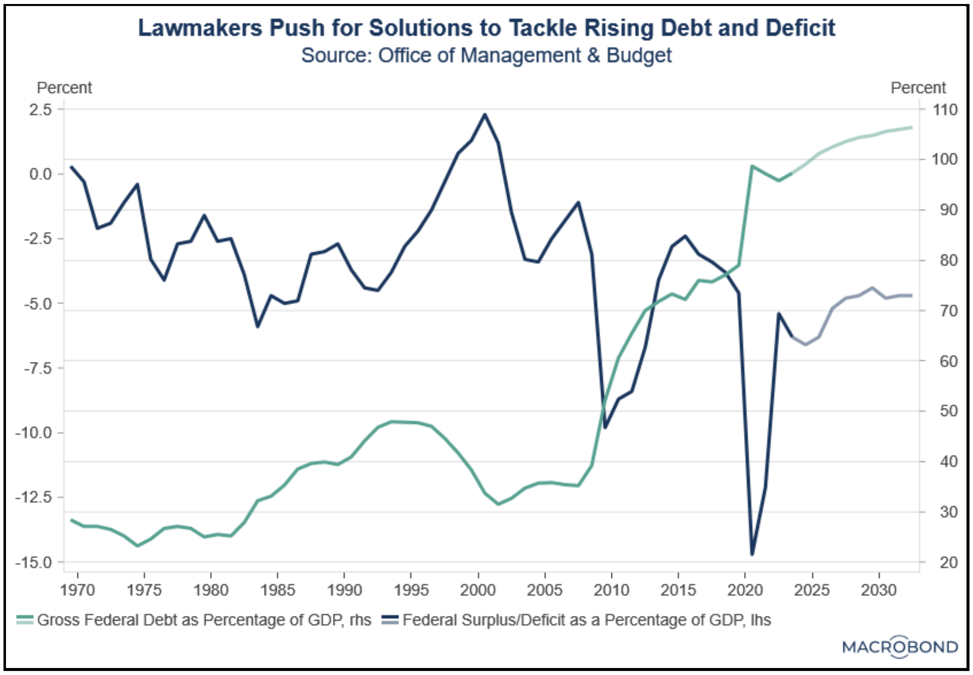
Good morning! The market is closely watching the latest jobs data as a key driver of sentiment. Today's *Comment* begins with an analysis of rising tensions within the Republican Party over the new tax legislation, explores why the ECB may have finished its rate-cutting cycle, and covers other key market developments. As always, the report will also include a summary of recent domestic and international data releases.

Budget Dispute: Divisions over the president's Big, Beautiful Bill have erupted publicly as Republican lawmakers grapple with the legislation's complex policy trade-offs.

- Much of the media coverage has centered on the highly publicized rift between President Trump and Tesla CEO Elon Musk, once dubbed his "Bro-in-Chief," who has emerged as a vocal critic of the bill. Musk has denounced the legislation as fiscally irresponsible and urged Republican lawmakers to block its passage. His remarks coincided with the president's meeting with the Senate Finance Committee where he attempted to rally support for the bill.
- In response to Musk's criticism, the president threatened to terminate federal contracts with Musk's companies, sparking an immediate sell-off in Tesla shares. The billionaire retaliated by floating the possibility of launching a third-party political movement as an

alternative to the Republican Party. However, tensions have since eased following intervention by presidential aides, who arranged a conciliatory call between the two figures to resolve their differences.

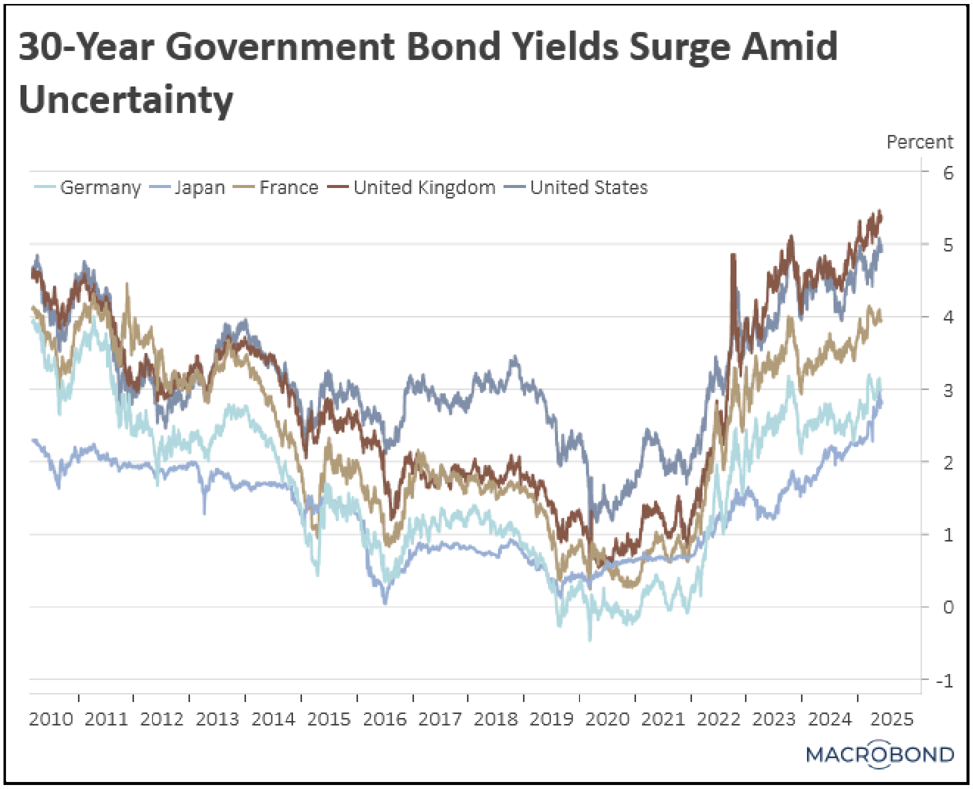


- Behind the scenes, congressional Republicans may be moving toward significant concessions to advance their tax legislation after negotiations with President Trump. In closed-door meetings with GOP lawmakers, the president reportedly supported measures to achieve Medicare savings while indicating an openness to reducing the planned SALT deduction cap increase.
- Nevertheless, the bill remains far from finalized, with several controversial provisions still under debate. Two lesser-discussed but significant items include a proposed 10-year moratorium on state-level AI regulation and making the 2017 corporate tax cuts permanent. These divisions threaten to complicate the bill's path through the House following Senate revisions. Despite these headwinds, we maintain our projection that the legislation will ultimately pass within the next month.

A Hawkish Cut: The European Central Bank has cut rates but signaled that it is nearing the end of its easing cycle.

- The ECB cut its benchmark policy rate by 25 basis points to 2.00%, matching market expectations, as it steps up efforts to shield the eurozone economy from escalating US trade tensions. The move cements the ECB's status as the most aggressive easing force among major central banks this year. The decision was not unanimous, however, with Governing Council member Robert Holzmann dissenting in favor of holding rates steady, citing lingering data uncertainties.

- The ECB's decision to cut rates comes amid signs of economic recovery in the eurozone, with inflation finally easing from elevated levels. First-quarter GDP growth accelerated to 0.6%, doubling the previous quarter's pace, and was driven primarily by stronger investment activity. While headline inflation in the region fell below 2% in May for the first time since 2021, underlying price pressures remain persistent, with services inflation still running significantly above pre-pandemic levels.



- During the press conference, ECB President Christine Lagarde described current monetary policy as being in a "good place," while suggesting the central bank may be approaching the end of its easing cycle. These remarks triggered an immediate sell-off in global bond markets, as investors recalibrated expectations for long-term interest rates amid growing recognition that the ultra-low-rate environment of recent decades may not return.
- The ECB's decision to halt further monetary easing appears partially driven by escalating US-EU trade tensions. Washington has repeatedly criticized accommodative policies by foreign central banks, accusing them of deliberately maintaining lower interest rates than the US to weaken their currencies and gain unfair trade advantages. This criticism intensified recently when the US Treasury explicitly urged the Bank of Japan to hike its policy rates to strengthen the yen in its semi-annual currency report.
- Global bond yields appear to be undergoing a structural shift, with markets increasingly pricing out any return to the historic lows seen following the 2008 financial crisis and the pandemic. This suggests the global economy may be entering a period of tighter financial conditions and more restrictive trade policies, potentially creating headwinds for

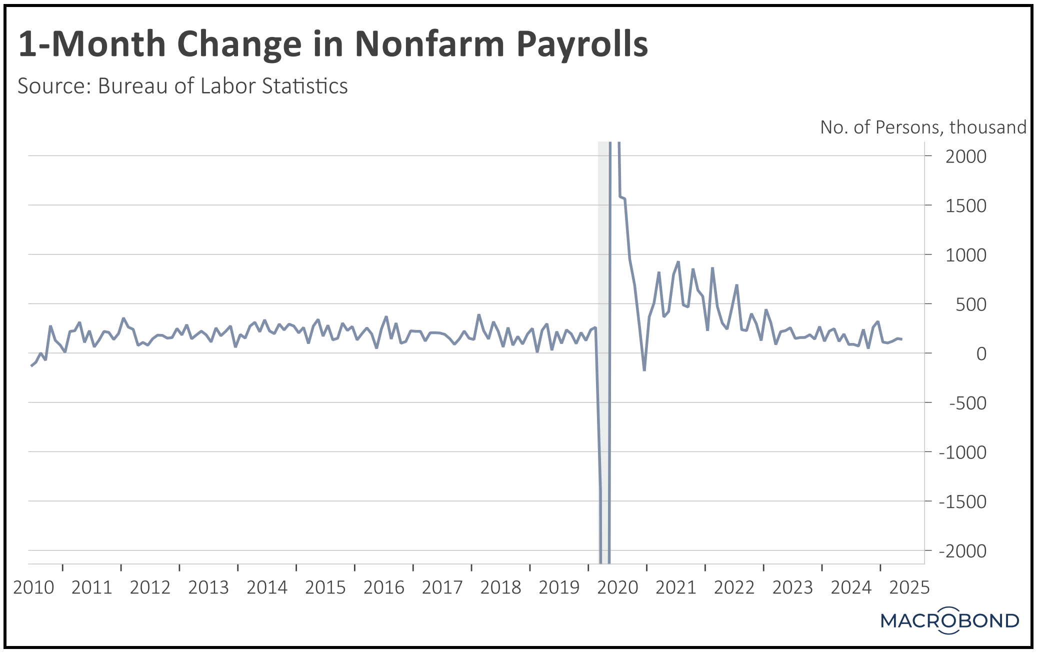
economic growth. In this environment, we favor a quality bias, as financially stable firms are better positioned to weather these challenges than their more leveraged counterparts.

Trump and Xi Speak: Tensions between the two largest economies appear to be easing following a phone call between their leaders.

- After a period of escalating tensions, Chinese President Xi and President Trump have finally connected via phone to address their ongoing trade disputes. President Trump indicated that the productive conversation sets the stage for a new series of high-level trade negotiations between the two nations. This breakthrough follows mutual accusations of failing to honor the recent trade agreement made in Geneva.
- Trump's decision to hold talks stemmed from his efforts to persuade Beijing to resume exports of rare earth minerals, following China's move to tighten restrictions in retaliation for US limits on software sales. While there was no public discussion of either side easing their trade barriers, signs of potential concessions did emerge. China, for its part, suggested that the talks should facilitate the return of Chinese students to US universities.
- The talks come as both economies face mounting pressure from trade tensions. Recent factory data in China reveals that manufacturing activity contracted at its fastest pace since September 2022, driven largely by a sharp drop in export prices. Meanwhile, purchasing manager surveys indicate that manufacturers are grappling with rising input costs, which may force businesses to raise prices. Additionally, there are signs that the labor market may be showing signs of cooling.
- While talks between the two sides are a positive development for the market, lingering uncertainty over future trade policy will likely fuel further volatility. Both countries stand to lose significantly from a potential decoupling, yet they acknowledge that their relationship is unsustainable in its current form. We expect negotiations to drag on for months as both sides seek to mitigate the economic fallout of an eventual separation. That said, any meaningful breakthrough in talks could trigger a sharp equity rally.

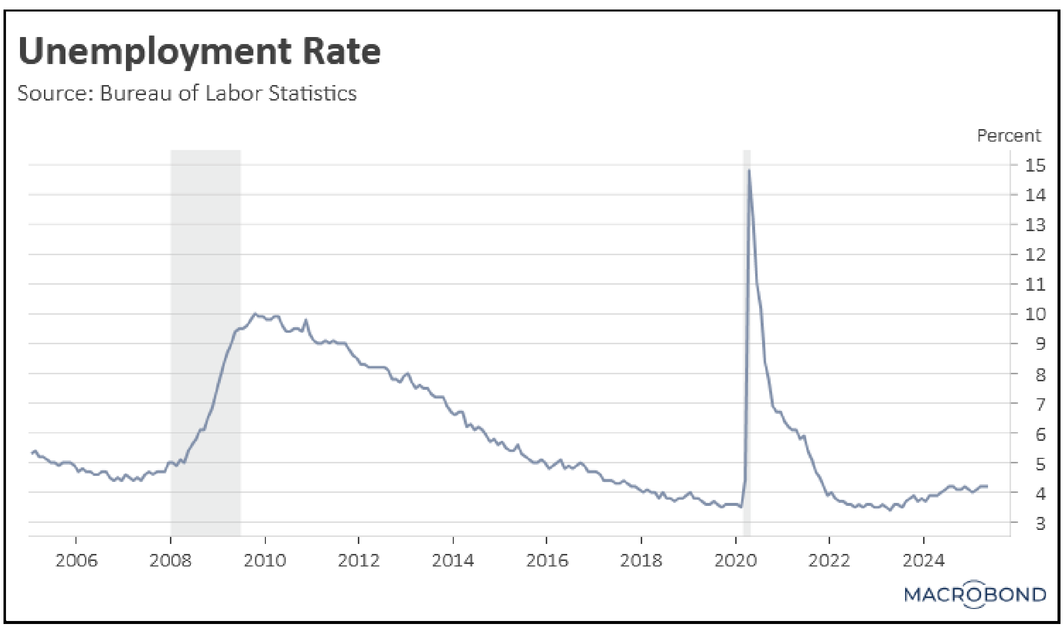
US Economic Releases

Job growth exceeded expectations in May, with the Bureau of Labor Statistics ***nonfarm payrolls*** reporting 139,000 new jobs, slightly above the forecast of 137,000. ***Private sector payrolls*** also outperformed, adding 140,000 jobs compared to expectations of 120,000. Meanwhile, ***manufacturing payrolls*** declined sharply, falling by 8,000 jobs instead of the projected drop of 1,000, marking a harsher contraction than anticipated.



The chart above shows the monthly change in nonfarm payrolls. While jobs were able to beat expectations, the number suggests that job creation has slowed over recent months.

Meanwhile, the latest household survey indicates that labor market conditions remained broadly stable compared to the previous month. The ***unemployment rate*** held steady at 4.2%, matching expectations. This unchanged figure coincides with a slight decline in the ***participation rate***, which fell from 62.6% to 62.4%, suggesting more people left the workforce than joined it. Meanwhile, ***hourly earnings*** picked up, increasing by 0.4% month-over-month, just above the anticipated 0.3% rise.



The chart above shows the unemployment rate. Recent data confirms that while the labor market remains historically tight, there are emerging signs of moderation. With the jobless rate holding steady and wages rising, the Federal Reserve may prioritize its inflation-fighting mandate in the upcoming policy meeting.

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

Economic Releases						
EST	**Indicator**			**Expected**	**Prior**	**Rating**
15:00	Consumer Credit	m/m	Apr	$10.000b	$10.172b	*
Federal Reserve						
EST	**Speaker or Event**	**District or Position**				
10:00	Michelle Bowman Gives Speech on Supervision, Regulation	Member of the Board of Governors				

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	Household Spending	y/y	Apr	-0.1%	2.1%	1.5%	**	Equity and bond neutral
	Leading Economic Index	m/m	Apr P	103.4	107.6	103.9	**	Equity and bond neutral
	Coincident Index	y/y	Apr P	115.5	115.8	115.4	**	Equity and bond neutral
Australia	Foreign Reserves	m/m	May	A$105.6b	A$102.4b		**	Equity and bond neutral
EUROPE								
Eurozone	Retail Sales	y/y	Apr	2.3%	0.4%	1.5%	*	Equity bullish, bond bearish
	GDP SA	y/y	1Q T	1.5%	1.2%	1.2%	***	Equity and bond neutral
	Employment	y/y	1Q F	0.7%	0.8%		**	Equity and bond neutral
Germany	Industrial Production WDA	y/y	Apr	-1.8%	-0.7%	-1.0%	**	Equity and bond neutral
	Trade Balance	m/m	Apr	14.6b	21.3b	19.1b	*	Equity and bond neutral
	Exports	m/m	Apr	-1.7%	1.2%	-1.4%	*	Equity and bond neutral
	Imports	m/m	Apr	3.9%	-1.4%	0.5%	*	Equity and bond neutral
France	Trade Balance	m/m	Apr	-7968m	-6248m	1.05%	*	Equity and bond neutral
	Current Account Balance	m/m	Apr	-4.1	1.0b		*	Equity and bond neutral
	Industrial Production	y/y	Apr	-2.1%	0.1%	-0.3%	***	Equity and bond neutral
	Manufacturing Production	y/y	Apr	-1.6%	-0.1%		**	Equity and bond neutral
Switzerland	Foreign Currency Reserves	m/m	May	703.6b	703.0b		*	Equity and bond neutral
Russia	Gold and Forex Reserves	m/m	30-May	$678.7b	$678.5b		***	Equity and bond neutral
	Money Supply, Narrow Definition	w/w	30-May	18.03t	18.09t		*	Equity and bond neutral
AMERICAS								
Canada	International Merchandise Trade	m/m	Apr	-7.14b	-2.26b	-1.50b	*	Equity and bond neutral
	Net Change in Employment	m/m	May		7.4k	17.5k	***	Equity and bond neutral
	Unemployment Rate	m/m	May		6.9%	7.0%	***	Equity and bond neutral
	Participation Rate	m/m	May		65.3%	65.3%	*	Equity and bond neutral
Brazil	FGV Inflation IGP-DI	y/y	Apr		15.57%	13.83%	**	Equity and bond neutral
Brazil	Trade Balance	m/m	May	$7239m	$7637m	$8300m	**	Equity and bond neutral
	Exports	m/m	May	$30156m	$329900m	$31222m	*	Equity and bond neutral
	Imports	m/m	May	$22918m	$22263m	$22900m	*	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)	423	423	0	Up
U.S. Sibor/OIS spread (bps)	431	431	0	Up
U.S. Libor/OIS spread (bps)	431	432	-1	Up
10-yr T-note (%)	4.39	4.39	0.00	Down
Euribor/OIS spread (bps)	195	196	-1	Down
Currencies	**Direction**			
Dollar	Up			Down
Euro	Down			Up
Yen	Up			Up
Pound	Down			Up
Franc	Down			Up
Central Bank Action	**Current**	**Prior**	**Expected**	
ECB Deposit Facility Rate	2.00%	2.25%	2.00%	On Forecast
ECB Main Refinancing Rate	2.15%	2.40%	2.15%	On Forecast
ECB Marginal Lending Facility	2.40%	2.65%	2.40%	On Forecast
Bank of Russia Key Rate	20.00%	21.00%	20.00%	On Forecast
RBI Repurchase Rate	5.50%	6.00%	5.75%	Below Forecast
RBI Cash Reserve Ratio	3.00%	4.00%	4.00%	Below 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.

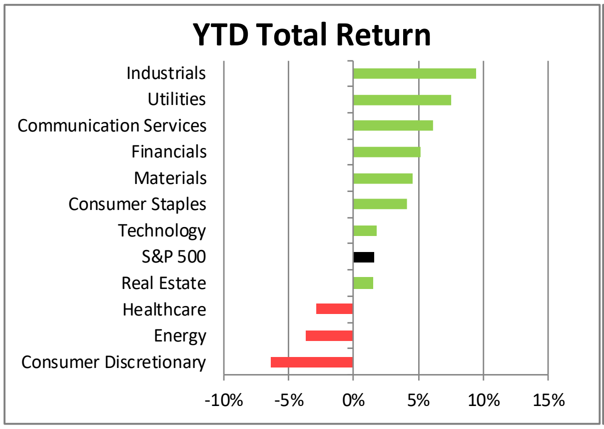
	Price	Prior	Change	Explanation
Energy Markets				
Brent	$65.31	$65.34	-0.05%	
WTI	$63.31	$63.37	-0.09%	
Natural Gas	$3.72	$3.68	1.12%	
Crack Spread	$23.59	$23.79	-0.86%	
12-mo strip crack	$21.19	$21.40	-0.98%	
Ethanol rack	$1.83	$1.84	-0.36%	
Metals				
Gold	$3,362.50	$3,352.65	0.29%	
Silver	$36.14	$35.65	1.37%	
Copper contract	$488.80	$493.30	-0.91%	
Grains				
Corn contract	$436.00	$439.50	-0.80%	
Wheat contract	$542.25	$545.50	-0.60%	
Soybeans contract	$1,047.50	$1,051.75	-0.40%	
Shipping				
Baltic Dry Freight	1,626	1,489	137	
DOE Inventory Report				
	Actual	**Expected**	**Difference**	
Crude (mb)	-4.30	-3.13	-1.18	
Gasoline (mb)	5.22	-0.50	5.72	
Distillates (mb)	4.23	0.17	4.06	
Refinery run rates (%)	3.2%	1.0%	2.2%	
Natural gas (bcf)	122	113	9	

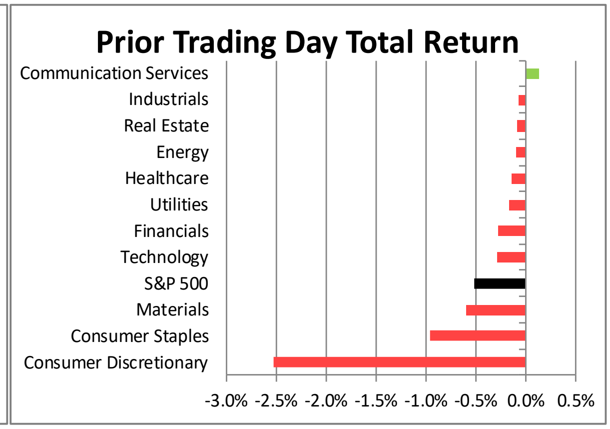
Weather

The 6-to-10-day and 8-to-14-day forecasts currently call for warmer-than-normal temperatures for most of the country, with cooler temperatures in the Pacific region. The outlook calls for wetter-than-normal conditions for most of the country that is expected to recede north and south of the country, with dry conditions expected in New England.

Data Section

US Equity Markets – (as of 6/5/2025 close)

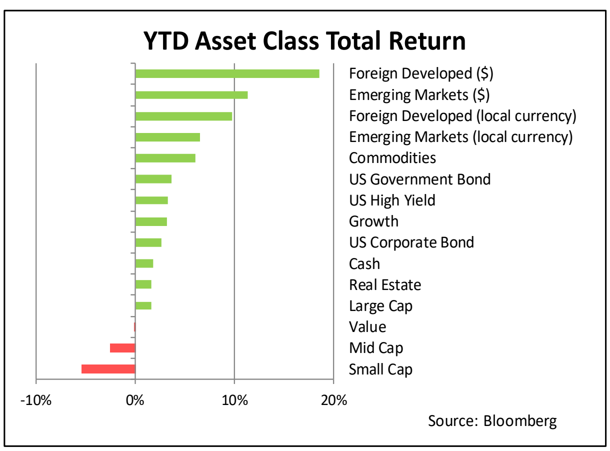




(Source: Bloomberg)

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 6/5/2025 close)

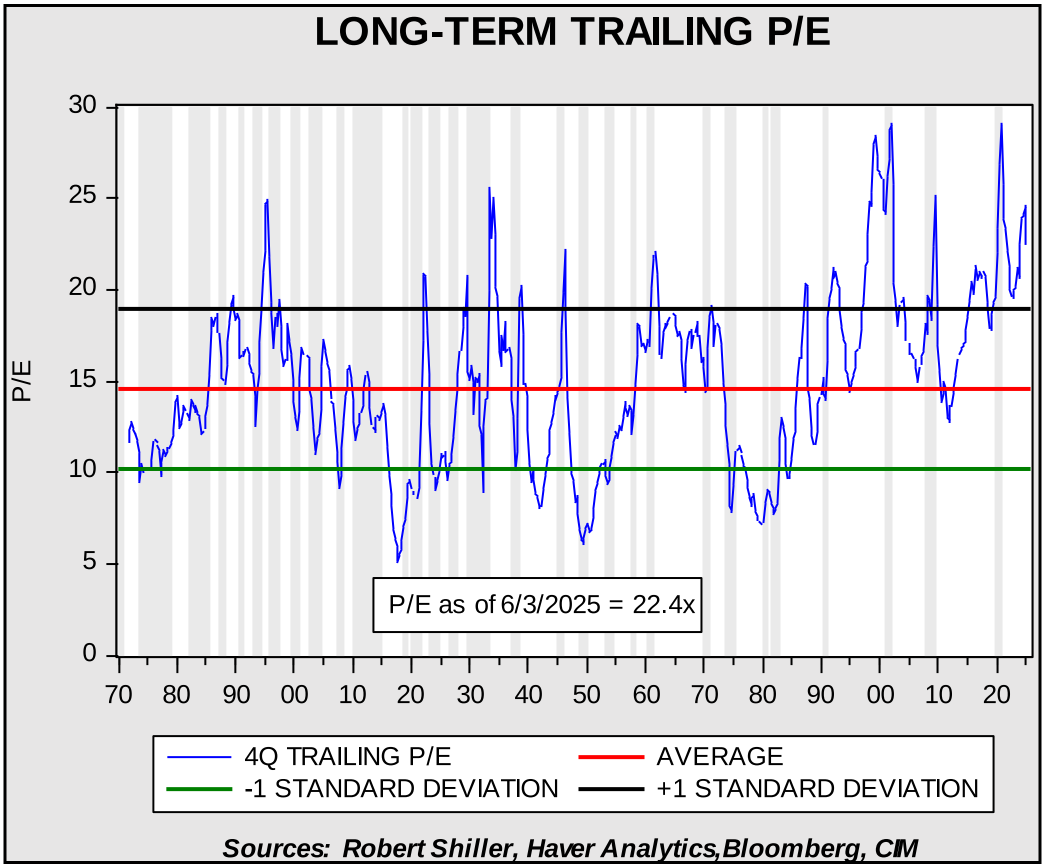


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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

June 4, 2025



Based on our methodology,[1] the current P/E is 22.4x, up 0.1 from our last report. The increase in the multiple was due to a rise 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.

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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 (Q2, Q3, and Q4) and one estimate (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.