Daily Comment

Confluence Investment Management

By Patrick Fearon-Hernandez, CFA, and Thomas Wash

Posted: June 27, 2025 — 9:30 AM ET] Global equity markets are generally higher this morning. In Europe, the Euro Stoxx 50 is up 1.0% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed up 0.2%. Chinese markets were mixed, with the Shanghai Composite down 0.7% from its previous close and the Shenzhen Composite up 0.4%. 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
"Introducing Friedrich Merz" (6/23/25) + podcast	"The Economy That Won't Die" (6/16/25) + podcast	Q2 2025 Report Q2 2025 Rebalance Presentation	NEW: The Confluence Mailbag Podcast **Business Cycle Report**

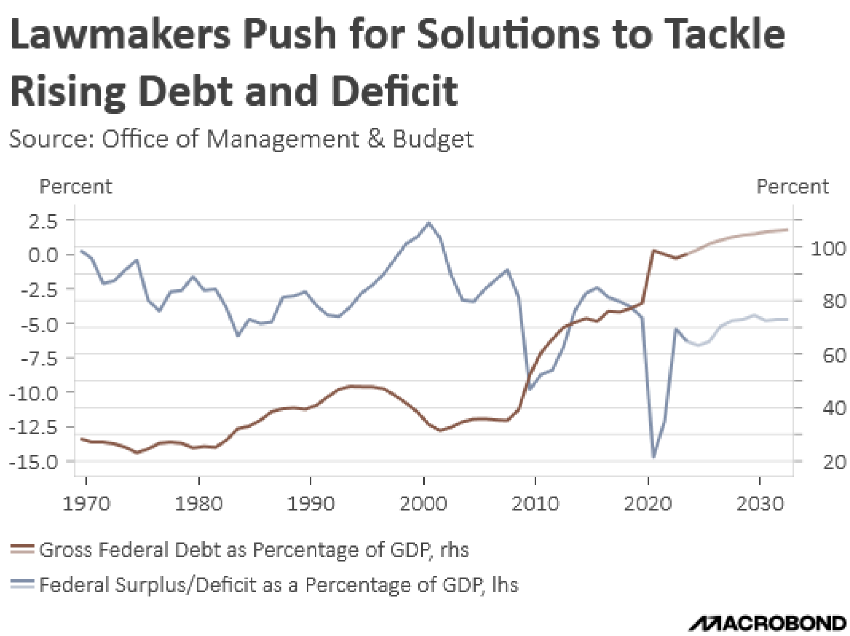
Have a question on the economy, markets, geopolitics, or other important topics? You can submit your queries to our new monthly podcast, *Confluence Mailbag*! Submit your question to mailbag@confluenceim.com.

Good morning! Markets remain squarely focused on US-China trade developments as key deadlines approach. Today's *Comment* will discuss the latest progress on the administration's trade legislation, implications of downward GDP revisions, and other market-moving headlines. We'll conclude with our regular roundup of critical international and domestic data releases.

Big, Beautiful Test: The Senate is set to start voting on the final changes on the Trump tax bill, but there still seem to be major differences within the party.

- Republican senators are preparing to advance their flagship tax bill, though growing dissent in both chambers threatens to derail passage despite looming deadlines. While both Senate and House leadership have endorsed moving forward with votes to meet the president's July 4 target, substantive disagreements over key provisions continue to surface, raising doubts about whether the legislation can clear Congress in its current form.

- Currently, the bill faces revisions ahead of its scheduled vote, with the Senate parliamentarian emerging as a key obstacle. In her advisory role on procedural compliance, she has ruled against several provisions, most notably a measure that would have reduced state tax charges for Medicaid providers from 6% to 3.5%. This change alone would have generated significant federal savings, and its rejection forces lawmakers to reconsider their fiscal approach.

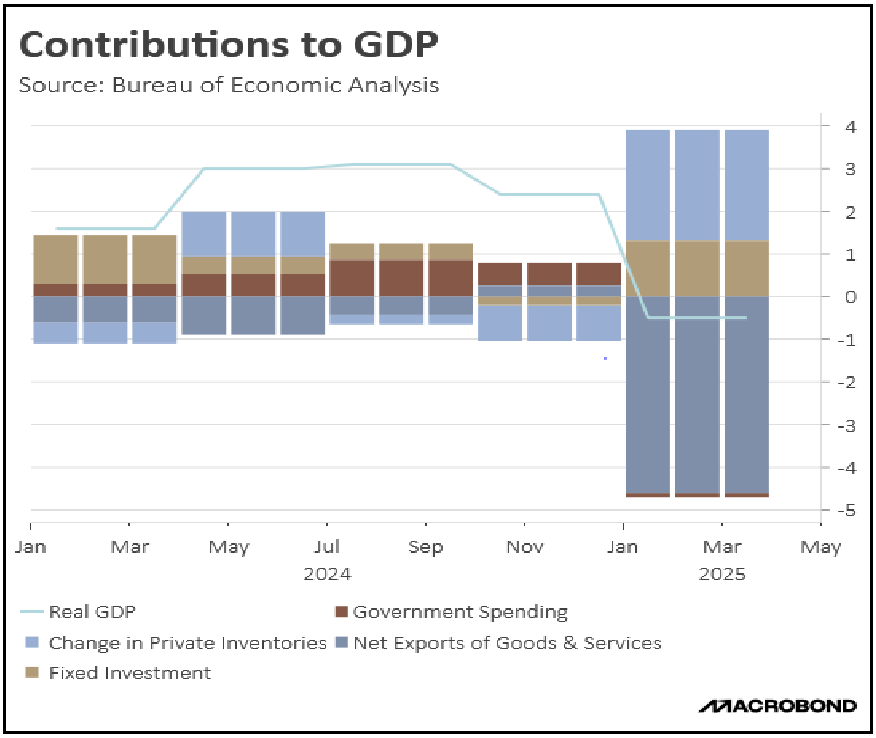


- Significant disagreement persists among House and Senate Republicans regarding the SALT deduction cap. Lawmakers from high-tax states continue to push for a substantial increase above current levels, with some threatening to withhold support for the bill without modifications. Meanwhile, conservatives from low-tax states oppose raising the cap, arguing it would disproportionately benefit wealthier households.
- While the bill remains in legislative limbo, passage this week appears likely, though a short extension remains an option. Approval would likely provide sufficient momentum to propel the S&P 500 to record highs. Looking ahead, we anticipate market attention will quickly shift to the outlook for rate cuts and economic growth, both of which face unusual uncertainty due to ongoing trade policy developments.

GDP Overstated: The third reading of the GDP showed that the economy did worse than originally expected.

- Economic output took a hit with the latest revision, which now reflects an annualized contraction of 0.5%, notably worse than the initial estimate of a 0.2% decline. This more significant downturn was largely fueled by moderation in personal consumption, specifically a slowdown in spending on services. While minor downward revisions to investment spending also contributed, a slight offset came from a less severe decline in net exports and government spending within the GDP figures.

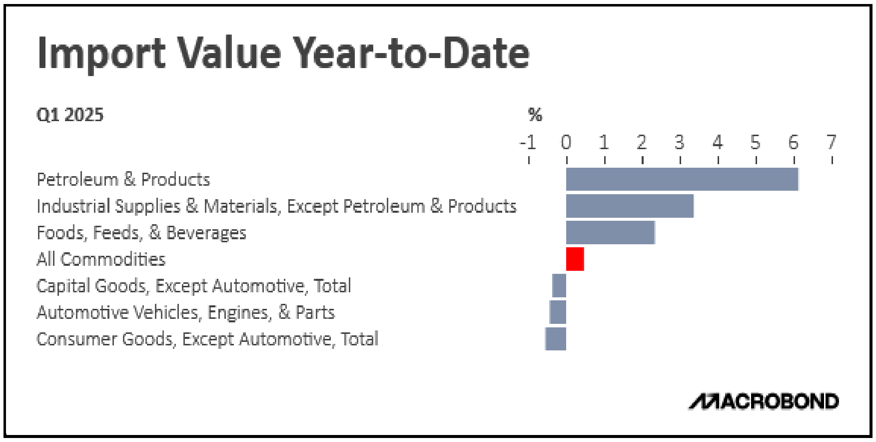
- The sharper downturn in Q1 will likely prompt investors to closely monitor the Q2 economic performance. Current estimates from the Atlanta Fed's GDPNow project a significant rebound, with an annualized growth rate of 3.4%. This anticipated increase is primarily attributed to a strong positive contribution from net exports and a pickup in consumer spending.



- Business investment will be a critical indicator for assessing whether recession risks have truly receded. Notably, first-quarter spending, particularly on information technology projects, served as a key buffer that possibly prevented an even deeper economic contraction. Going forward, we'll be closely monitoring whether this resilience in capital expenditures persists amid tighter financial conditions and lingering uncertainty.

Updates on Trade Deals: With less than two weeks until the trade deadline expires, the president continues to make progress on key trade negotiations.

- Commerce Secretary Howard Lutnick announced that the administration has reached a trade deal with China. The agreement, pending signatures from Presidents Trump and Xi, would grant the US access to rare earth minerals. In return, the US is expected to resume ethane shipments to China upon finalization of the deal.
- The agreement should prove particularly beneficial for US tech stocks, as it secures access to critical production inputs. Rare earth minerals, essential components in everything from smartphones to advanced jet engines, represent just one example of the vital resources now more reliably available to these companies under the deal's framework.



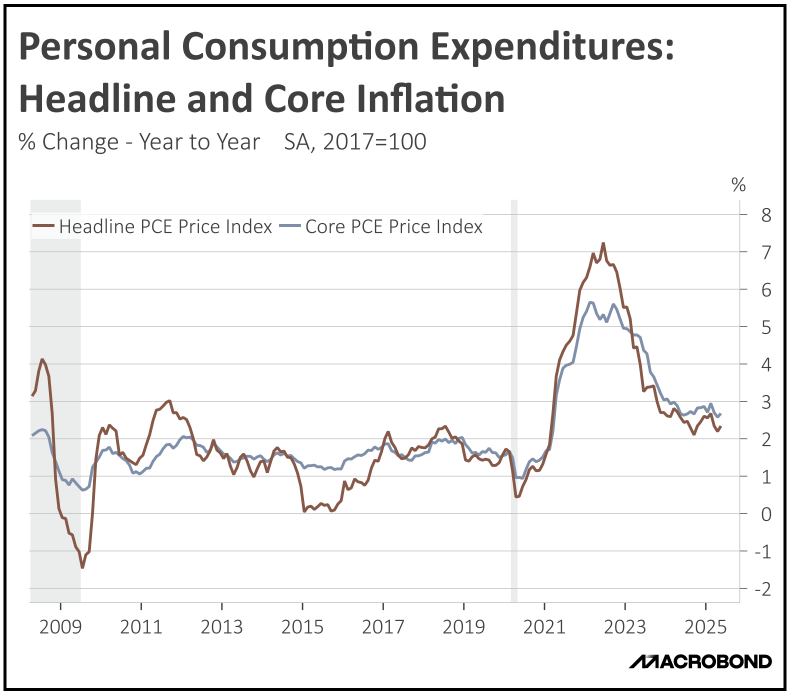
- While import tariffs dominate trade policy discussions, export controls represent a more systemic economic vulnerability. The fundamental asymmetry lies in substitution dynamics — markets can typically be replaced more readily than critical supply chains. Consequently, the economy's resilience (and by extension, market performance) will depend heavily on its ability to prevent material shortages before they emerge.

Germany's Past: The Social Democrats are set to clash over differences on how to deal with Russia.

- The party will convene on Friday to deliberate its future stance toward Russia, as members seek to reconcile their historical advocacy for détente — a policy many credit with helping to topple the Berlin Wall — with current demands for heightened defense expenditures. This strategic reassessment comes amid escalating geopolitical tensions.
- The ongoing dispute risks undermining the government's ability to approve critical defense legislation. With the ruling coalition holding a fragile 13-seat majority, even limited defections from SPD members could stall key votes, potentially paralyzing security funding efforts.
- While German equities have been among this year's top performers, much of the rally has been fueled by expectations of higher defense spending. As a result, we are closely monitoring intra-coalition tensions, particularly their potential to disrupt fiscal commitments, to assess whether this market strength reflects a sustainable trend or merely short-term optimism.

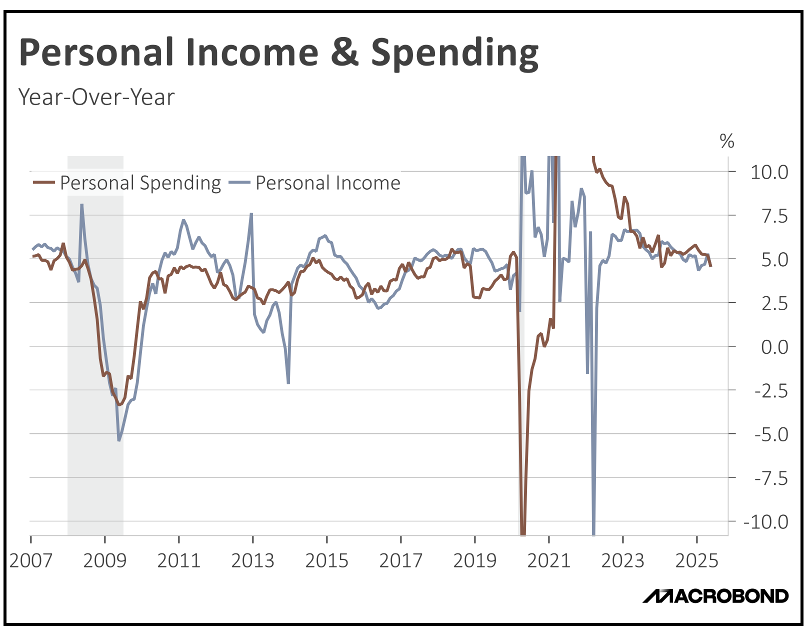
US Economic Releases

Inflation moderated in May, with the ***headline PCE price index*** rising just 0.1% for the second consecutive month, according to the Bureau of Economic Analysis. However, underlying price pressures showed signs of persistence. The ***Core PCE index***, which excludes volatile food and energy costs, ticked up slightly, with monthly inflation accelerating from 0.1% to 0.2%.



The chart above shows the year-over-year trends in both headline and core PCE inflation. In May, headline inflation edged up to 2.3% from 2.2%, while core inflation similarly rose to 2.7% from 2.6%.

In May, ***Personal Income*** declined by a seasonally adjusted 0.4%, sharply missing expectations of a 0.3% increase and reversing April's downwardly revised gain of 0.7%. Meanwhile, ***Personal Spending*** also dipped, falling 0.1%, well below the anticipated level and April's 0.2% rise.



The chart above tracks annual changes in personal income and personal spending since just before the Great Financial Crisis. As of May, personal income rose 4.5% year-over-year, matching the 4.5% increase in spending over the same period.

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	U. of Michigan Consumer Sentiment	m/m	Jun F	60.5	60.5	***
10:00	U. of Michigan Current Conditions	m/m	Jun F	63.2	63.7	**
10:00	U. of Michigan Future Expectations	m/m	Jun F		58.4	**
10:00	U. of Michigan 1-Year Inflation Expectation	m/m	Jun F	5.2%	5.1%	*
10:00	U. of Michigan 5-10 Year Inflation Expectation	m/m	Jun F	4.1%	4.1%	*
11:00	Kansas City Fed Services Activity	m/m	Jun		11	*
Federal Reserve						
EST	**Speaker or Event**	**District or Position**				
7:30	John Williams Serves as Session Chair	President of the Federal Reserve Bank of New York				
9:00	Beth Hammack and Lisa Cook Participate in Fed Listens	Cleveland Fed President and Fed Governor				

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	Jobless Rate	m/m	May	2.5%	2.5%	2.5%	***	Equity and bond neutral
	Job-To-Applicant Ratio	m/m	May	1.24%	1.26%	1.26%	***	Equity and bond neutral
	Tokyo CPI	y/y	Jun	3.1%	3.4%	3.3%	**	Equity and bond neutral
	Tokyo CPI Ex-Fresh Food	y/y	Jun	3.1%	3.6%	3.3%	***	Equity and bond neutral
	Tokyo CPI Ex-Fresh Food & Energy	y/y	Jun	3.1%	3.3%	3.3%	*	Equity and bond neutral
	Retail Sales	y/y	May	2.2%	3.3%	2.5%	**	Equity and bond neutral
	Depart. Store & Supermarket Sales	y/y	May	0.6%	1.5%		*	Equity and bond neutral
New Zealand	ANZ Consumer Confidence Index	m/m	Jun	98.8	92.9		*	Equity and bond neutral
China	Industrial Profits	y/y	May	-1.1%	3.0%	1.0%	*	Equity bearish, bond bullish
	BoP Current Account	q/q	1Q F	$165.4b	$165.6b		**	Equity and bond neutral
EUROPE								
Eurozone	Consumer Confidence	m/m	June F	-15.3	-15.3	-15.3	**	Equity and bond neutral
	Economic Confidence	m/m	Jun	94.0	94.8	94.8	***	Equity and bond neutral
	Industrial Confidence	m/m	Jun	-12.0	-10.4	-10.0	***	Equity bearish, bond bullish
	Services Confidence	m/m	Jun	2.9	1.8	1.6	**	Equity bullish, bond bearish
France	CPI	y/y	Jun P	0.9%	0.7%	0.8%	***	Equity and bond neutral
	CPI, EU Harmonized	y/y	Jun P	0.8%	0.6%	0.7%	**	Equity and bond neutral
	PPI	y/y	May	0.2%	-0.7%		*	Equity and bond neutral
Italy	Consumer Confidence Index	m/m	Jun	96.1	96.5	97.0	***	Equity bearish, bond bullish
	Economic Sentiment	m/m	Jun	93.9	93.1		**	Equity and bond neutral
	Manufacturing Confidence	m/m	Jun	87.3	86.6	87.0	***	Equity and bond neutral
	Industrial Sales WDA	y/y	Apr	1.1%	-1.2%		*	Equity and bond neutral
	PPI	y/y	May	2.8%	3.8%		**	Equity and bond neutral
Russia	Gold and Forex Reserves	m/m	20-Jun	$687.2b	$682.8b		***	Equity and bond neutral
	Money Supply, Narrow Definition	w/w	20-Jun	18.33t	18.29t		*	Equity and bond neutral
AMERICAS								
Mexico	Unemployment Rate NSA	m/m	May	2.75%	2.54%	2.59%	***	Equity and bond neutral
Brazil	FGV Inflation IGPM	y/y	Jun	4.39%	7.02%	5.15%	***	Equity bullish, bond bearish
	Total Outstanding Loans	m/m	May	6653b	6615b		**	Equity and bond neutral
	National Unemployment Rate	m/m	May	6.2%	6.6%	6.3%	*	Equity and bond neutral
	Central Govt Budget Balance	m/m	May	-40.6b	18..0b	-40.00b	*	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)	421	421	0	Up
U.S. Sibor/OIS spread (bps)	429	429	0	Down
U.S. Libor/OIS spread (bps)	429	429	0	Down
10-yr T-note (%)	4.27	4.24	0.03	Down
Euribor/OIS spread (bps)	198	199	-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**	
Bank of Mexico Overnight Rate	8.00%	8.50%	8.00%	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	$68.00	$67.73	0.40%	
WTI	$65.57	$65.24	0.51%	
Natural Gas	$3.64	$3.53	3.15%	
Crack Spread	$24.19	$25.03	-3.32%	
12-mo strip crack	$22.24	$22.64	-1.75%	
Ethanol rack	$1.79	$1.79	0.19%	
Metals				
Gold	$3,282.23	$3,327.92	-1.37%	
Silver	$35.99	$36.66	-1.80%	
Copper contract	$507.45	$512.05	-0.90%	
Grains				
Corn contract	$410.25	$404.00	1.55%	
Wheat contract	$542.00	$536.75	0.98%	
Soybeans contract	$1,021.50	$1,016.50	0.49%	
Shipping				
Baltic Dry Freight	1,553	1,665	-112	
DOE Inventory Report				
	Actual	**Expected**	**Difference**	
Crude (mb)	-5.84	-1.10	-4.74	
Gasoline (mb)	-2.08	0.50	-2.58	
Distillates (mb)	-4.07	1.00	-5.07	
Refinery run rates (%)	1.5%	0.7%	0.8%	
Natural gas (bcf)	96	87	9	

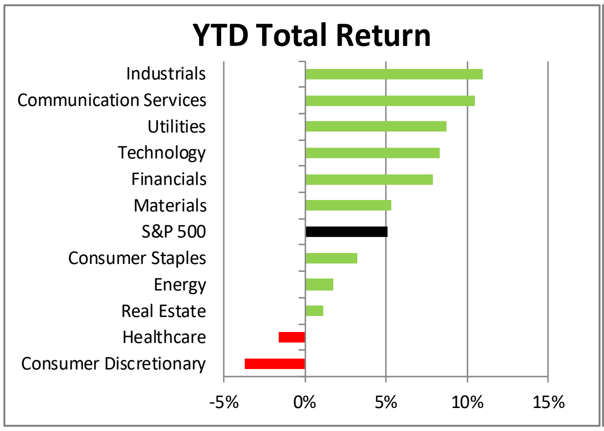
Weather

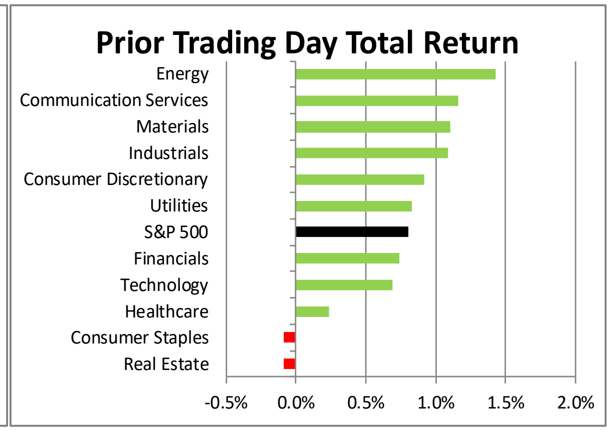
The latest 6-to-10-day and 8-to-14-day forecasts indicate warmer-than-normal conditions in the Pacific Northwest and the Southeast, with cooler-than-normal conditions in Southwest and Great Plains regions. The precipitation outlook shows wetter-than-normal conditions for most of the country west of California.

The 7-day tropical weather outlook indicates potential development of a tropical disturbance south of the Yucatan Peninsula. However, forecast models suggest this system is unlikely to organize into a tropical cyclone within the next seven days.

<u>Data Section</u>

US Equity Markets – (as of 6/26/2025 close)

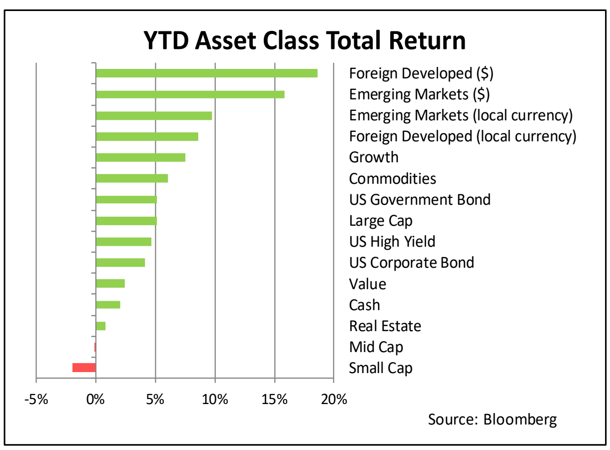




(Source: Bloomberg)

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 6/26/2025 close)

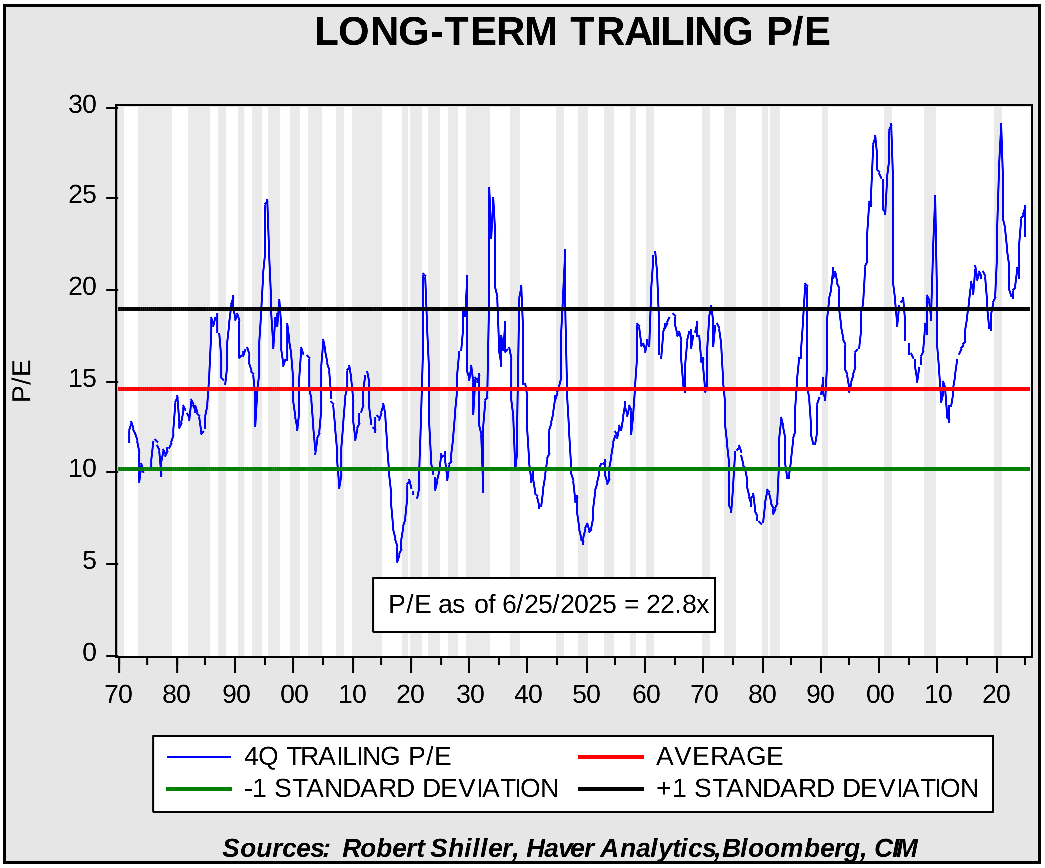


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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 26, 2025



Based on our methodology,[1] the current P/E is 22.8x, 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.