

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: March 1, 2023—9:30 AM EST] Global equity markets are higher this morning. In Europe, the Euro Stoxx 50 is currently up 0.7% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed up 3.3%. Chinese markets were higher, with the Shanghai Composite and the Shenzhen Composite both closing up 1.0%. U.S. equity index futures are signaling a higher open.

With 487 companies having reported so far, S&P 500 earnings for Q4 are running at \$54.20 per share compared to estimates of \$52.85. Of the companies that have reported thus far, 68.8% have exceeded expectations, while 25.3% have fallen short of expectations.

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](#) (2/21/2023) (with associated [podcast](#)) “*Chip War: Book Review*”
- [Weekly Energy Update](#) (2/23/2023): We continue to chronicle the rise in commercial crude oil inventory and comment on the IAEA news that Iran is dangerously close to weapons-grade uranium enrichment. We also note how oil and gas markets are adjusting to the war in Ukraine, now one year since it began.
- [Asset Allocation Quarterly – Q1 2023](#) (1/19/2023): Discussion of our asset allocation process, Q1 2023 portfolio changes, and our outlook for the markets.
- [Asset Allocation Bi-Weekly](#) (2/27/2023) (with associated [podcast](#)): “Federal Reserve Policymakers in 2023: Hawks or Doves?”
- [Asset Allocation Q1 2023 Rebalance Presentation](#) (2/2/2023): Video presentation featuring the Asset Allocation Committee as they review our asset allocation strategies, recent portfolio changes, and the current macro environment.
- [Confluence of Ideas podcast](#) (2/1/2023): “The 2023 Outlook”

Our *Comment* today opens with some positive economic news out of China, where manufacturing and services both appear to be recovering from the recent COVID-19 infection wave. We next review a wide range of other international and U.S. developments with the potential to affect the financial markets today, including a warning from the Bank of England’s Governor Bailey that investors shouldn’t necessarily think his central bank will hike interest rates much further.

China: The official purchasing managers' index for manufacturing [jumped to 52.6 in February, bursting past expectations and coming in well above the reading of 50.1 in January](#). In fact, the February reading [was the highest since April 2012](#). Meanwhile, the February PMI for nonmanufacturing rose to 56.3, also exceeding expectations and marking an improvement from its January reading of 54.4. As with most major PMIs, readings over 50 indicate expanding activity. Taken together, the figures for January and February suggest China's recovery from its pandemic shutdowns is now gathering pace, although it's important to remember that Chinese data in those months could be distorted by the shifting Lunar New Year holiday.

China-Belgium: The Belgian government's Center for Cybersecurity said a Chinese state entity [was most likely responsible for the January 2021 spearfishing attack on Belgian parliament member Samuel Cogolati](#). The attack was launched shortly after Cogolati wrote a parliamentary resolution warning of "crimes against humanity" against the Uyghur Muslims in China.

- Coupled with European officials' recent willingness to warn China against supplying weapons to Russia for its war in Ukraine, the Belgian government's willingness to call out China's aggression against Cogolati suggests officials on the Continent are now coming around to a U.S.-style, hardline stance against Beijing.
- If that trend continues, it would help solidify the evolving U.S.-led geopolitical and economic bloc, while also likely intensifying the West's tensions with China and creating new risks for investors.

United States-China: Yesterday, the new House Select Committee on the Chinese Communist Party [held its initial meeting](#), with Republican Chair Mike Gallagher vowing that the panel will "investigate and expose the ideological, technological, and military threats posed by the Chinese Communist party." The initial meeting included testimony from four witnesses who called out a range of threats from China, along with statements castigating China from both Republicans and Democrats. We suspect the committee will further fuel U.S. voters' concerns about China and energize support for military, industrial, and political initiatives against Beijing.

Iran: The International Atomic Energy Agency [confirmed that it discovered a small amount of uranium purified to a near-weapons grade level of 84%](#) at a spot inspection in Iran last month. Iran has reportedly told the agency that it inadvertently enriched the uranium to that level, but the IAEA's confirmation of the finding is likely to further heighten tensions between the West and Iran. The news could also bring forward a potential Israeli attack on the country.

Israel: Besides the unsettling news from Iran, the Israeli government [is also struggling with growing violence between Jewish settlers and Palestinians in the West Bank](#). In recent days, fighting erupted after a Palestinian gunman shot two Jewish settlers dead in Huwara, a Palestinian town south of Nablus, where the Israeli army killed 11 Palestinians and injured 100 more last week in its deadliest raid on the West Bank since 2005.

Nigeria: Ruling party candidate Bola Tinubu [has now been declared the winner of Saturday's presidential election after final results showed him with 8.8 million votes](#). Atiku Abubakar of the opposition People's Democratic Party came in second with 7.0 million votes, and Peter Obi,

the Labor party contender whose youth-focused campaign turned the usual two-party race into a competitive three-man battle, came in third with 6.1 million votes. Because of the fractured vote and Tinubu's advanced age coupled with his reputation for corruption, it would not be surprising if political tensions and instability remain in Nigeria for some time.

United Kingdom: Bank of England Governor Bailey [warned that investors shouldn't necessarily believe that the central bank will need to impose many additional interest-rate hikes](#) to cool the economy and bring down inflation. According to Bailey, his policymakers still have no presumption that they would need to raise interest rates further from the current 4.00% level.

- While financial markets now expect rates to rise to 4.75% by the end of 2023, up from an expectation of a peak of 4.25% at the start of February, Bailey said he had not seen anything in the data to justify the change in outlook.
- Despite Bailey's comments signaling a potential for lower-than-anticipated interest rates, the GBP is trading only slightly weaker today at about \$1.2014.

U.S. Labor Market: Two large on-line recruiting companies [said they are seeing the number of job openings fall faster than indicated by the government's monthly JOLTS report](#). The data suggests that the U.S. labor market may be cooling faster than indicated by the top-line official reports. If so, it could mean that the anticipated recession is taking hold and inflation pressures could soon start to moderate despite the exceedingly strong economic activity in January.

U.S. Student Loans: The Supreme Court [held oral arguments yesterday on the validity of President Biden's pandemic-driven program providing student loan relief](#). By all accounts, the conservative majority expressed skepticism that the administration could order such a broad-ranging policy change without the consent of Congress, even though it relied on a law giving it some power to modify such a program. Since the court's final decision may not come until summer, millions of people with student loans [will now spend months in a state of uncertainty](#) regarding their debt obligations.

U.S. Cryptocurrency Regulation: After New York officials halted new issues of the BUSD stablecoin last month because of regulatory questions, new reports [say investors have pulled about \\$6 billion from the product, reducing the amount in circulation by one-third](#). The figures illustrate the cryptocurrency regulatory risks that we have long warned about.

U.S. Economic Releases

Higher borrowing costs continue to weigh on home loan demand. According to an index tracked by the Mortgage Bankers Association, mortgage applications fell 5.7% in the week ending February 17. Last week, interest rates hit their highest level since mid-November. The average 30-year fixed-rate mortgage rose 9 bps from 6.62% to 6.71%. As a result, the tracker for purchases fell 5.6% from the prior week, while the refinance tracker fell 5.5% in the same period.

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

Economic Releases						
EST	Indicator			Expected	Prior	Rating
9:45	S&P Global Manufacturing PMI	m/m	Feb F	47.8	47.8	***
10:00	Construction Spending MoM	m/m	Jan	0.2%	-0.4%	**
10:00	ISM Manufacturing PMI - Prices Paid	m/m	Feb	48.0	47.4	**
10:00	ISM Manufacturing PMI	m/m	Feb	45	44.5	**
10:00	ISM Manufacturing PMI - Employment	m/m	Feb		50.6	*
10:00	ISM Manufacturing PMI - New Orders	m/m	Feb		42.5	**
	Wards Total Vehicle Sales	m/m	Feb	14.68m	15.74m	***
Federal Reserve						
EST	Speaker or Event	District or Position				
9:00	Neel Kashkari Takes Part in a Moderated Discussion	President of the Federal Reserve Bank of Minneapolis				

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	Jibun Bank Manufacturing PMI	m/m	Feb F	47.7	47.4		***	Equity and bond neutral
Australia	GDP	y/y	4Q	2.7%	5.9%	2.7%	***	Equity and bond neutral
	CPI	y/y	Jan	7.4%	8.4%	8.1%	**	Equity bullish, bond bearish
New Zealand	CoreLogic House Prices	y/y	Feb	-8.9%	-7.2%		*	Equity and bond neutral
	Building Permits	m/m	Jan	-1.5%	-7.2%	-7.10	**	Equity bullish, bond bearish
South Korea	Trade Balance	m/m	Feb	-\$5.300b	-\$12.690b	-\$6.011m	*	Equity and bond neutral
	Exports	y/y	Feb	-7.5%	-16.6%	-8.8%	***	Equity bullish, bond bearish
	Imports	y/y	Feb	3.6%	-2.6%	-2.8%	**	Equity bullish, bond bearish
China	Official Manufacturing PMI	m/m	Feb	52.6	50.1	50.6	***	Equity bullish, bond bearish
	Official Services PMI	m/m	Feb	56.3	54.4	54.9	**	Equity bullish, bond bearish
	Caixin Manufacturing PMI	m/m	Feb	51.6	49.2	50.7	***	Equity bullish, bond bearish
India	S&P Global Manufacturing PMI	m/m	Feb	55.3	55.4		***	Equity and bond neutral
EUROPE								
Eurozone	S&P Global Manufacturing PMI	m/m	Feb F	48.5	48.5	48.5	***	Equity and bond neutral
Germany	Unemployment Change	m/m	Feb	2.0k	-22.0k	-11.0k	***	Equity and bond neutral
	Unemployment Claims Rate	m/m	Feb	5.5%	5.5%	5.5%	**	Equity and bond neutral
	S&P Global/BME Manufacturing PMI	m/m	Feb F	46.3	46.5	46.5	***	Equity and bond neutral
	CPI	y/y	Feb P	8.7%	8.7%	8.5%	***	Equity and bond neutral
	CPI, EU Harmonized	y/y	Feb P	9.3%	9.2%	9.0%	**	Equity and bond neutral
France	S&P Global Manufacturing PMI	m/m	Feb F	47.4	47.9	47.9	***	Equity and bond neutral
Italy	S&P Global Manufacturing PMI	m/m	Feb	52.0	50.4	51.0	***	Equity and bond neutral
UK	Nationwide House Price Index	y/y	Feb	-1.1%	1.1%	-0.9%	***	Equity and bond neutral
	Mortgage Approvals	m/m	Jan	39.6k	35.6k	40.5k	***	Equity and bond neutral
	S&P Global/CIPS Manufacturing PMI	m/m	Feb F	49.3	49.2	49.2	***	Equity and bond neutral
Switzerland	Real Retail Sales	y/y	Jan	-2.2%	-2.8%	-3.0%	**	Equity bullish, bond bearish
	Manufacturing PMI	m/m	Feb	48.9	49.3	50.5	***	Equity and bond neutral
Russia	S&P Global Manufacturing PMI	m/m	Feb	53.6	52.6	51.1	***	Equity bullish, bond bearish
AMERICAS								
Canada	GDP	y/y	Dec	2.3%	2.8%	2.7%	**	Equity and bond neutral
Mexico	International Reserves Weekly	w/w	24-Feb	\$200.083b	\$200.374b		*	Equity and bond neutral
Brazil	S&P Global Manufacturing PMI	m/m	Feb	49.2	47.5		***	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.

Fixed Income	Today	Prior	Change	Trend
3-mo Libor yield (bps)	495	496	-1	Up
3-mo T-bill yield (bps)	464	470	-6	Up
TED spread (bps)	31	25	6	Widening
U.S. Sibor/OIS spread (bps)	489	489	0	Up
U.S. Libor/OIS spread (bps)	492	492	0	Up
10-yr T-note (%)	3.93	3.92	0.01	Flat
Euribor/OIS spread (bps)	272	270	2	Up
Currencies	Direction			
Dollar	Down			Down
Euro	Up			Up
Yen	Up			Down
Pound	Up			Down
Franc	Up			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.

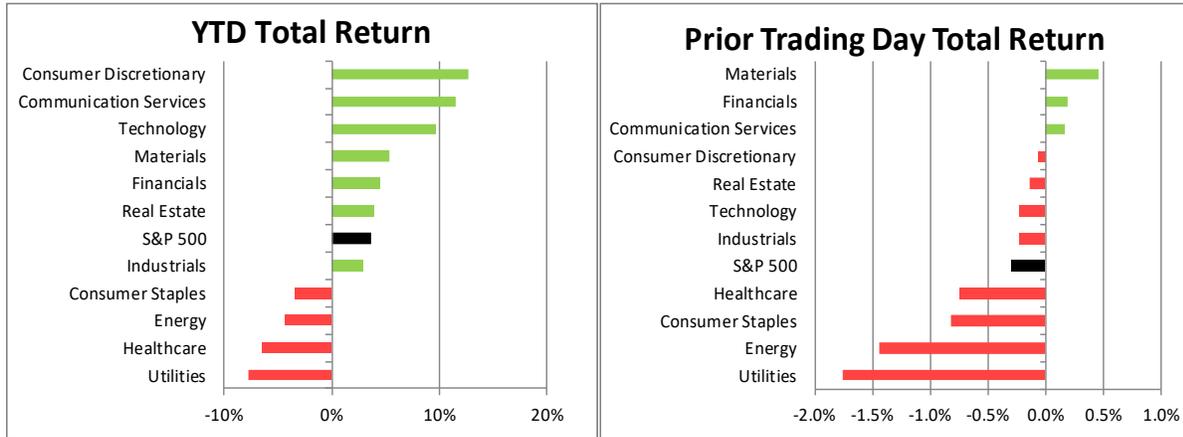
DOE Inventory Report	Price	Prior	Change	Explanation
Energy Markets				
Brent	\$83.18	\$83.45	-0.32%	
WTI	\$76.58	\$77.05	-0.61%	
Natural Gas	\$2.77	\$2.75	0.73%	
Crack Spread	\$36.99	\$36.22	2.13%	
12-mo strip crack	\$29.66	\$29.25	1.39%	
Ethanol rack	\$2.28	\$2.28	-0.01%	
Metals				
Gold	\$1,837.52	\$1,826.92	0.58%	
Silver	\$21.06	\$20.91	0.71%	
Copper contract	\$415.10	\$408.95	1.50%	
Grains				
Corn contract	\$630.50	\$630.25	0.04%	
Wheat contract	\$706.25	\$705.50	0.11%	
Soybeans contract	\$1,489.75	\$1,479.00	0.73%	
Shipping				
Baltic Dry Freight	990	935	55	
DOE Inventory Report				
	Actual	Expected	Difference	
Crude (mb)		1.9		
Gasoline (mb)		-1.0		
Distillates (mb)		-0.5		
Refinery run rates (%)		-0.3%		
Natural gas (bcf)		-72		

Weather

The 6-10 and 8-14 day forecasts show colder-than-normal temperatures spreading from the Pacific, Rocky Mountain, and New England regions to the entire country. Meanwhile, warmer-than-normal temperatures are expected throughout the Deep South. The forecasts show wetter-than-normal conditions throughout the majority of the nation, with dry conditions in New England.

Data Section

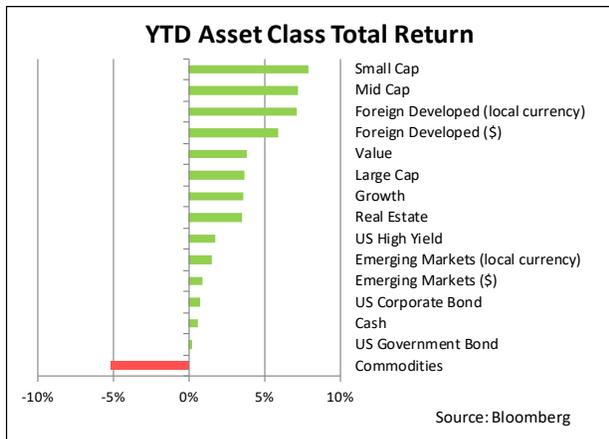
U.S. Equity Markets – (as of 2/28/2023 close)



(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 2/28/2023 close)

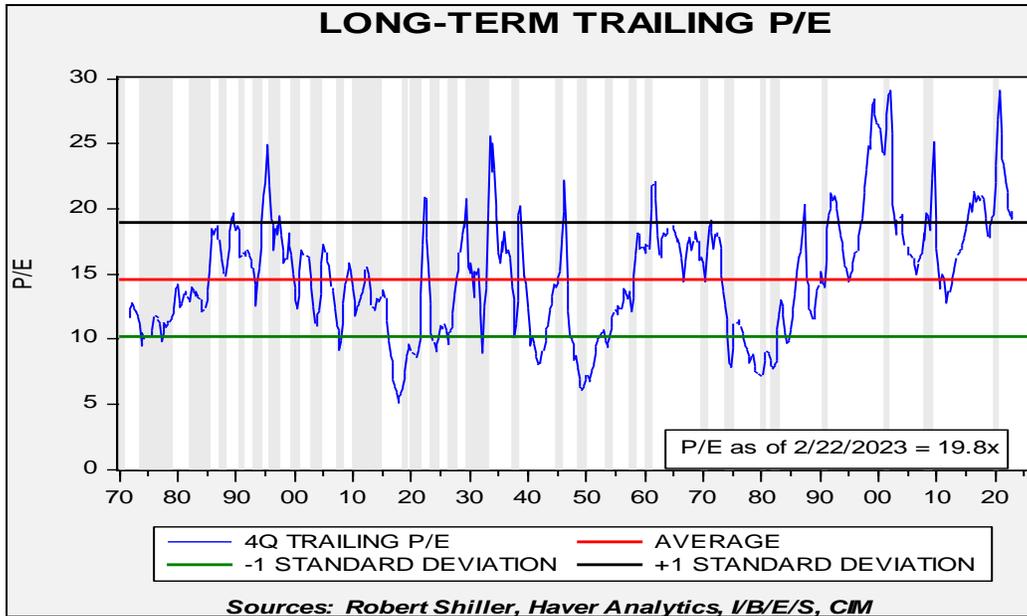


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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

February 23, 2023



Based on our methodology,¹ the current P/E is 19.8x, unchanged from last week.

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.