

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 29, 2021—9:30 AM EDT] Global equity markets are generally higher this morning. The EuroStoxx 50 is currently up 0.4% from its prior close. In Asia, the MSCI Asia Apex 50 closed down 0.1%. Chinese markets were higher, with the Shanghai Composite up 0.5% from its prior close and the Shenzhen Composite up 0.2%. U.S. equity index futures are signaling a lower open.

We have published our latest [Weekly Geopolitical Report](#), which constitutes Part II of our series on the geopolitics of Central Bank Digital Currencies (CBDC). We also have several other recent multimedia offerings. There is a new [chart book](#) recapping the recent changes we made to our Asset Allocation portfolios. Here is our latest [Confluence of Ideas podcast](#). Our most recent [Asset Allocation Weekly](#), [chart book](#), and [podcast](#) are also available. Note: Due to the upcoming Good Friday and Easter holidays, we will not publish an AAW this week; it will resume on April 9. Finally, here is our latest [Weekly Energy Update](#). You can find all this research and more on our [website](#).

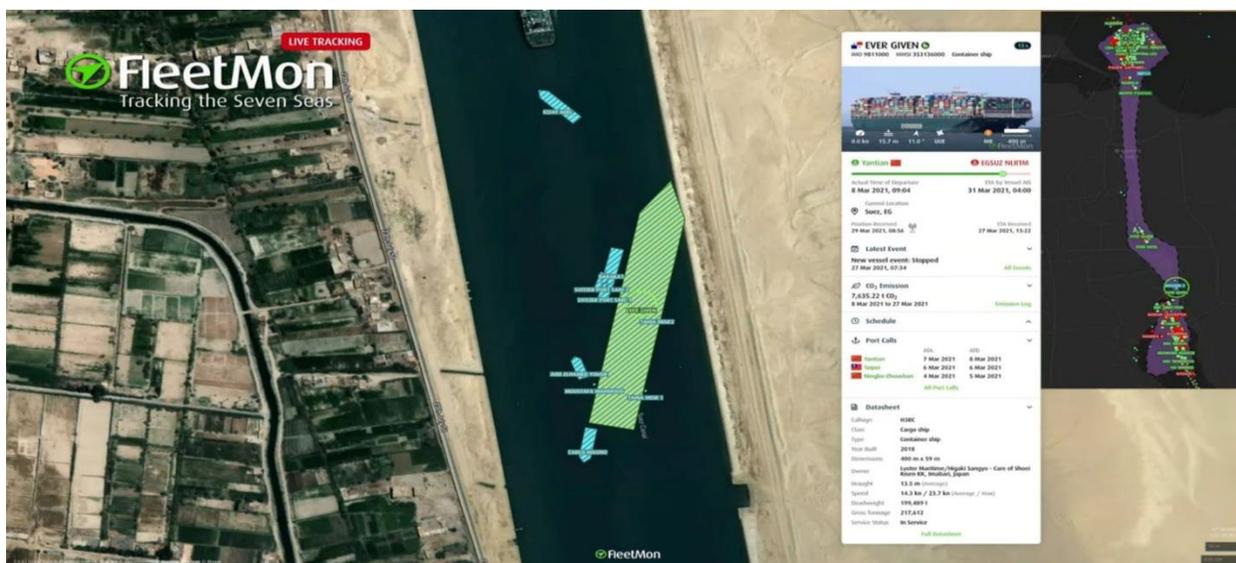
Good morning and happy Monday! We are down to the elite eight in NCAA men's basketball, and opening day is just around the corner! [U.S. equity futures are a bit lower this morning](#) but off their worst levels of the overnight session. Coverage starts today with reports that a large family office is facing massive margin calls, which have led to aggressive selling of select equities. We look at who is behind the situation and its potential impact. Up next is the latest on the Suez situation. International news follows, with Myanmar and Germany's supreme court featured. China news is next; economics and policy follow, and we close with the latest on COVID-19.

Who is Bill Hwang? He comes out of Tiger Management, a hedge fund of yesteryear run by Julian Robertson. He was one of Robertson's "tiger cubs," fund managers who spun out of Tiger Management to start their own hedge funds. Hwang took an initial stake of \$23 million at the turn of the century and turned it into \$8.0 billion by the end of 2007. His firm is called Archegros Capital Management, and it is a "long/short" hedge fund. Since 2007, his fortunes have been mixed. He was caught in the massive short squeeze of Volkswagen (VWAGY, USD 32.53), which rose 82% in one day after Porsche (POAHY, USD, 10.29) announced it had purchased shares. He also [paid the SEC \\$44 million in fines over insider trading](#) of Chinese bank stocks. Hong Kong exchanges banned him from trading for four years in 2014. In response to these legal challenges, as well as market issues, Hwang converted his hedge fund into a family office.

On Friday, Goldman Sachs (GS, USD, 327.39), Credit Suisse (CS, USD 12.87), and Morgan Stanley (MS, USD, 79.98),¹ who acted as prime brokers for Archegos, issued margin calls on the family office. Nomura (NMR, USD, 6.61) and Credit Suisse have warned they may “[incur substantial losses](#).” Reports indicate that [banks liquidated at least \\$30 billion](#) (yes, with a “B”) of positions. Hwang tends to run a concentrated portfolio with leverage, which accentuates both gains and losses. His holdings appear to be weighted toward U.S. media companies and Chinese tech stocks. It appears the brokers initiated the stock sales, meaning this was a forced margin liquidation.

Here is the “known/known”—the sales are massive and were done in blocks, suggesting the bankers were worried about losses and wanted to move quickly to get as much out of the collateral as they could. This sort of action with a trader of this size isn’t common. Here are the “known/unknowns”—first, hedge fund managers often participate in the same ideas, and thus the sharp declines in selected stocks may also have ramifications for other managers. Second, the leverage may have been larger than one would expect. Margin loans are fixed at 50%, but traders can increase their leverage through derivatives, e.g., options, swaps, single stock futures, etc. We suspect Hwang’s positions were highly leveraged, which triggered the unified response. Third, and perhaps most important, we don’t know yet if the selling is nearly complete or if there is more to come. The [initial weakness in stock index futures](#) suggests worries were elevated; so far, it looks like we may be close to completion, and this event is just another tale of hubris and leverage. It is also possible that we aren’t finished yet, and wider selling may still be possible.

Suez: There is some good news on this front. The combined efforts of tugboats and excavators, along with the moon (from high tide), have [partially refloated](#) the stuck container vessel.



(Source: FleetMon)

¹ UBS (UBS, USD, 16.04) and Deutsche Bank (DB, USD, 12.35) also are listed as prime brokers, but we haven’t seen a direct mention that they were involved in margin sales.

The ship's bow has been [freed from the eastern bank](#), and the [stern has been shifted](#) into the channel. However, even if the boat is freed, it will take weeks for traffic to normalize completely. This is leading [shippers to consider alternative routes](#). Security of supply concerns are leading consumers to [reconsider just-in-time inventory methods](#). [Insurance firms are also facing a raft of claims](#).

International news: Myanmar increasingly looks like a civil conflict, and the German Supreme Court throws a potential spanner into the Eurobond.

- On Saturday, the Myanmar military celebrated [Armed Forces Day](#), and on [Sunday](#), [funerals were held for those who recently died in the violence](#). Both events triggered protests and [attacks by security forces](#), leading to a [bloody weekend](#) where [over 100 people perished](#) in the [violence](#). [U.S. and EU officials have condemned the violence](#), but given China's support for the regime, there is little that can be done from the U.N. The [army appears to be following a path that it can rein in the protests by escalating](#) the attacks. So far, [the rising death toll doesn't seem to be reducing the scale of the protests](#). There are reports that [Thailand is seeing an influx of refugees](#) from the fighting. China has made large investments in Myanmar to create a land bridge to the Indian Ocean, allowing it to avoid various chokepoints closer to the South China Sea that are ostensibly controlled by the U.S. Navy. A breakdown in civil order will put these investments and plans at risk. We continue to watch to see if China attempts to intervene directly.
- The [German Supreme Court has raised questions about German participation](#) in the €750 billion Eurobond scheme. Although this doesn't scotch the deal, it does raise a potential risk that we will need to monitor closely. Politically, the potential ouster of the conservative coalition from power would tend to bring a more Eurocentric political group to power. But the courts could still pose a problem.
- Slovakia's PM, Igor Matovic, has [stepped down](#) after his government faced defections over his unilateral decision to import the Sputnik V vaccine.
- [Protests emerged in Turkey](#) over the weekend in response to Erdogan's decision to pull out of a treaty that specifically protected women from violence.
- Alex Salmond, a major figure in Scotland's SNP, who was [recently acquitted of sexual harassment charges](#), has announced the [creation of a new political party](#). Although it will support independence for Scotland, the division will make it more difficult to actually build momentum for separation.

China: The EU and China are engaging in dueling sanctions, and China and Iran formalize ties.

- In light of EU sanctions on Chinese officials for human rights violations, [Beijing has replied](#) in kind. [The CAI investment deal between China and the EU remains in the balance](#). There are also worries that the [application of sanctions may have misfired](#) to some degree.
 - China has also [sanctioned U.S. and Canadian officials](#).
- China, in a direct threat to U.S. policy in the Middle East, [has inked an investment and security deal with Iran](#). The move will complicate the U.S. attempts to create a policy response with Iran.

- [Industrial profits in China surged](#) in January and February.
- As part of its “belt and road” project, China has made inroads into the Balkans. [Its behavior in Serbia has recently been profiled](#); local leaders like the investment, and local people seem to be bearing the cost of adjustment.
- [USTR Tai held her first interviews](#) over the weekend; the bottom line, the Biden administration appears to be using Trump-era tariffs as leverage in negotiations.
- On the security front, [China is challenging the Philippines](#), and U.S. officials are sounding the alarm over the [vulnerability of Taiwan](#).

Economics and policy: Infrastructure, taxes, and inflation lead the headlines.

- The Biden administration continues to [float a massive infrastructure package](#). [Tax hikes](#) are also being considered. Although there is much talk, we still think the path to getting both done is fraught with risk. One factor is that [tax hikes are not universally popular](#) with centrist Democrats.
- China has been a deflationary force on the global economy for decades. [That may be starting to reverse](#) as costs rise in China to the point where Chinese firms are no longer willing to absorb them. At the same time, China’s recent pullback from stimulus is [adversely affecting commodity prices](#). We don’t expect this situation to persist, but it is leading to price consolidation.
- Amazon (AMZN, USD, 3052.03) should know within the next [week](#) or so if its Alabama facility [will approve a union](#).
- We are seeing a [developed world surge in home prices](#), partly due to the pandemic. Although U.S. housing markets are clearly “hot,” [lending behavior is much more responsible](#) compared to the “naughts.”
- [Farmland prices are also soaring](#) due to elevated grain prices.

COVID-19: The [number of reported cases](#) is 127,285,692 with 2,785,365 fatalities. In the U.S., there are 30,262,717 confirmed cases with 549,335 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 180,646,465 doses of the vaccine have been distributed with 143,462,691 doses injected. The number receiving at least one dose is 93,631,163, while the number of second doses, which would grant the highest level of immunity, is 51,593,564. The *FT* has a page on [global vaccine distribution](#).

Virology

- First, the bad news: [Brazil is facing a public health crisis](#). Cases are surging, and the hospitals are overwhelmed. The government refuses to engage in lockdowns, so we expect continued elevated infection rates. India is also facing a new surge in cases with [new variants](#) reported.
- Now, the good news: So far, vaccines appear to be very effective. [Older people are showing signs of being protected from the disease](#), and [few health care workers are reporting infections after inoculations](#).

- It appears that [vaccine passports are going to be part of our lives](#). The development of proof of vaccination or immunity is fraught with risk but is probably necessary for the reopening of the economy.
- Full herd immunity probably won't be possible [until children are vaccinated](#).
- Russia is [quietly importing vaccines](#) to deal with shortages.

U.S. Economic Releases

There were no economic releases prior to the publication of this report. The table below lists the domestic releases and Fed events scheduled for the rest of the day.

Economic Releases						
EDT	Indicator			Expected	Prior	Rating
10:30	Dallas Fed Manufacturing Activity	m/m	Mar	14.5	17.2	***
Fed Speakers or Events						
EST	Speaker or event	District or position				
11:00	Christopher Waller to Speak at Peterson Institute	Federal Reserve Board				

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								
China	BoP Current Account Balance	m/m	4Q	\$123.8b	\$130.2b		**	Equity and bond neutral
	Industrial Profits YTD	y/y	Feb	178.9%			**	Equity bullish, bond bearish
EUROPE								
Switzerland	Domestic Sight Deposits CHF	w/w	26-Mar	630.0b	628.7b		*	Equity and bond neutral
	Total Sight Deposits CHF	w/w	26-Mar	702.7b	702.9b		*	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)	20	19	1	Up
3-mo T-bill yield (bps)	1	2	-1	Neutral
TED spread (bps)	19	18	1	Up
U.S. Libor/OIS spread (bps)	7	7	0	Up
10-yr T-note (%)	1.66	1.68	-0.02	Neutral
Euribor/OIS spread (bps)	-54	-54	0	Neutral
EUR/USD 3-mo swap (bps)	3	3	0	Down
Currencies				
dollar	Up			Down
euro	Flat			Up
yen	Flat			Up
pound	Up			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.

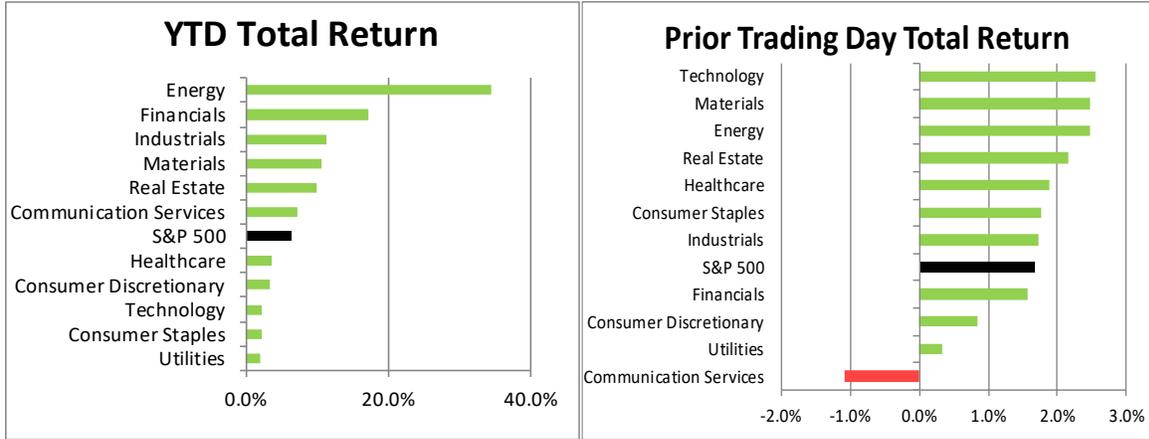
	Price	Prior	Change	Explanation
Energy Markets				
Brent	\$64.43	\$64.57	-0.22%	
WTI	\$60.65	\$60.97	-0.52%	
Natural Gas	\$2.55	\$2.56	-0.20%	
Crack Spread	\$19.97	\$19.83	0.67%	
12-mo strip crack	\$17.75	\$17.70	0.29%	
Ethanol rack	\$1.98	\$1.97	0.20%	
Metals				
Gold	\$1,724.20	\$1,732.52	-0.48%	
Silver	\$24.73	\$25.06	-1.32%	
Copper contract	\$404.55	\$406.80	-0.55%	
Grains				
Corn contract	\$549.00	\$552.50	-0.63%	
Wheat contract	\$615.00	\$613.25	0.29%	
Soybeans contract	\$1,401.00	\$1,400.50	0.04%	
Shipping				
Baltic Dry Freight	2178	2172	6	

Weather

The 6-10 and 8-14 day forecasts currently call for warmer than normal temperatures for most of the country, with cooler temps on the East and West coasts. The forecast calls for wetter than normal conditions in Texas and the Rocky Mountains, dry conditions are expected everywhere else.

Data Section

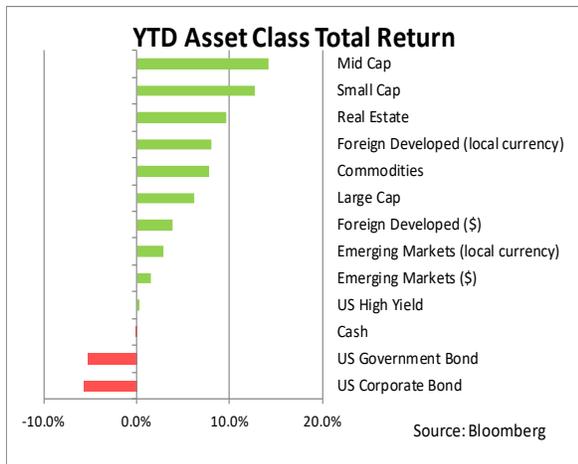
U.S. Equity Markets – (as of 3/26/2021 close)



(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 3/26/2021 close)

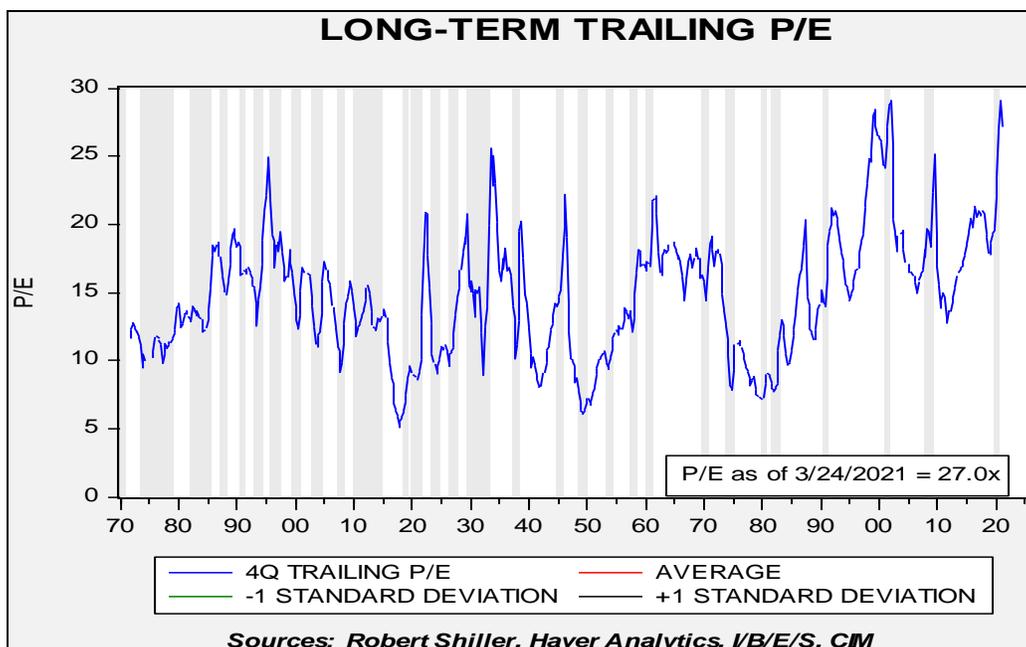


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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

March 25, 2021



Based on our methodology,² the current P/E is 27.0x, down 0.8x from last week. Rapidly rising earnings expectations led to the decline in the ratio.

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.

² 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 (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.