

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: May 15, 2023—9:30 AM EDT]** Global equity markets are up this morning. In Europe, the Euro Stoxx 50 is currently up 0.2% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed up 1.0%. Chinese markets were higher, with both the Shanghai Composite and the Shenzhen Composite closing up 1.2%. U.S. equity index futures are signaling a higher open.

With 459 companies having reported so far, S&P 500 earnings for Q1 are running at \$53.10 per share compared to the estimate of \$50.89, which is down 7.3% from Q1 2022. Of the companies that have reported thus far, 77.8% have exceeded expectations while 18.70% have fallen short of expectations.

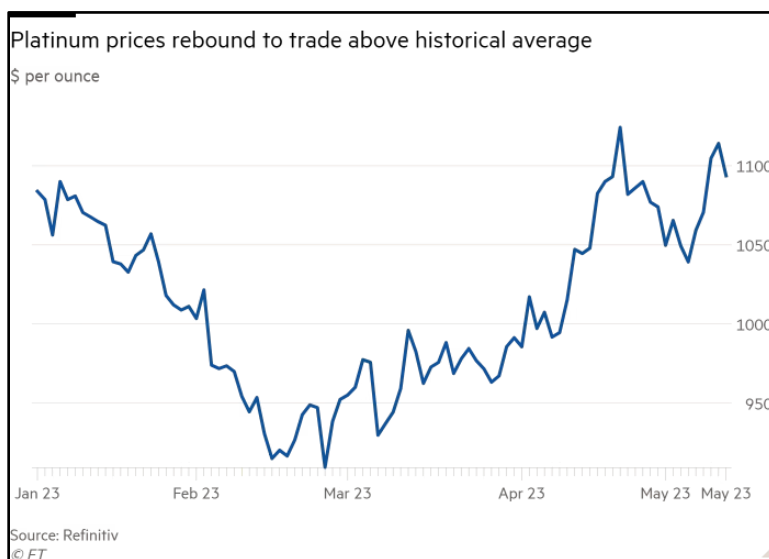
The Confluence macro team publishes a plethora of research reports and multimedia offerings on a weekly and quarterly basis, all available on our [website](#). We highlight recent publications below, with new items of the day emphasized in bold:

- [Bi-Weekly Geopolitical Report](#) (5/1/2023) (with associated [podcast](#)) “Implications of the Iran-Saudi Arabia Détente”
- [Weekly Energy Update](#) (5/11/2023): We update the weekly data and note that streamlining the permitting process has allies from both the fossil fuel and alternative energy industries.
- [Asset Allocation Quarterly – Q2 2023](#) (4/25/2023): Discussion of our asset allocation process, Q2 2023 portfolio changes, and our outlook for the markets.
- [Asset Allocation Q2 2023 Rebalance Presentation](#) (5/11/2023): Video presentation featuring the Asset Allocation Committee as they review our asset allocation strategies, recent portfolio changes, and the current macro environment.
- [Asset Allocation Bi-Weekly](#) (5/8/2023) (with associated [podcast](#)): “Why We Are Keeping Duration Short”
- [Confluence of Ideas podcast](#) (3/8/2023): “Reflections on Inflation”

Our *Comment* today opens with a major mining merger that underscores our oft-stated view that global commodity markets are set to enter a prolonged boom period once we get past the expected recession. We next review a wide range of other international and U.S. developments with the potential to affect the financial markets today, including an unexpectedly strong performance by President Erdoğan in Turkey’s elections over the weekend and upbeat comments by Treasury Secretary Yellen regarding the negotiations over the U.S. federal debt limit.

**Global Commodity Markets:** Canadian gold miner Newmont (NEM, \$45.94) [has agreed to buy Australian miner Newcrest \(NCMGY, \\$18.81\) in a move that will expand Newmont's access to minerals such as copper](#), which are expected to be in high demand as the world transitions to electric vehicles and other forms of electrification.

- More generally, Newmont's move is consistent with our view that global fracturing and insufficient investment will boost prices for a range of mineral commodities in the coming years. Even automakers [are looking to get into mining](#) in order to control prices for key mineral inputs.
- Separately, the World Platinum Investment Council [issued a report forecasting that global platinum demand will jump 28% this year to 8.2 million ounces](#). However, the report also warned that sporadic electricity production in South Africa, the main producer, will leave a deficit of almost one million ounces. The deficit is expected to further buoy platinum prices in the near term.



**Turkey:** In yesterday's presidential election, President Recep Tayyip Erdoğan and opposition leader Kemal Kılıçdaroğlu [came in first and second, respectively, but it appears neither won the required 50% to avoid a run-off ballot](#). That ballot will take place on May 28. Separately, Erdoğan's alliance appeared to be on track to maintain its majority in parliament after clinching 323 of the 600 seats in the National Assembly, compared with the opposition alliance's 211 seats.

- Erdoğan's tally in the presidential election was better than recent polling suggested, which could prompt destabilizing allegations of fraud.
- In any case, the president's better-than-expected results could lead to disappointment among investors looking for a return to more orthodox economic policies in Ankara and renewed cooperation with the West. Indeed, Turkish stocks are falling on the news so far this morning.

**Greece:** In happier news from the same neighborhood, S&P [recently assigned a “positive” outlook on Greece’s sovereign credit rating](#). That sets the stage for the country to possibly regain an investment-grade rating if the winner of the May 21 elections commits to continuing favorable economic policies. S&P currently rates Greece’s foreign debt at BB+/B, one step below investment grade.

- Greece was the poster child for Europe’s fiscal troubles during the Great Financial Crisis more than a decade ago.
- Now, however, economic growth in Greece is skyrocketing and government economic policies have improved markedly.
- Regaining an investment-grade credit rating would lower the government’s interest payments just when rapidly rising rates are becoming a greater headwind.

**Russia-Ukraine War:** After months of slowly pulling back as Russian forces advanced through the eastern city of Bakhmut, Ukrainian forces [have not only caught the Russians unawares with a small counterattack, but some reports suggest they may now be trying to surround the city](#). If that’s the case, the Ukrainians could trap the Russian troops, ammunition, and equipment deployed there. Such an event, which would probably be distinct from the expected large-scale Ukrainian counterattack, would further weaken the Russian military and be a major embarrassment for President Putin.

**China-United States:** The Chinese government [said it has sentenced a U.S. citizen to life in prison for espionage](#). The U.S. citizen, 78-year-old John Shing-wan Leung, also has permanent-residency status in Hong Kong. He was arrested in April 2021. The case could further strain ties between China and the U.S. despite recent government-to-government meetings aimed at reducing tensions.

- Separately, some Chinese students in the U.S. [are pushing back against the Chinese Communist Party’s effort to control their activity even when they’re thousands of miles from home](#).
- The small group of Chinese students studying at George Washington University in Washington, DC, has announced the establishment of an Independent Chinese Student Union to give young local Chinese a platform to organize and express political ideas free from the party’s prying eyes.
- The students say their aim is to protect students from the CCP and the Chinese Students and Scholars Association that the party directs. They also aim to convince the university to fully divest from “companies complicit in the Uyghur genocide and which enable the CCP.”

**China-Vietnam-Philippines:** In a new stand-off over control of the South China Sea, the Chinese government [has dispatched coast guard ships and ostensibly private fishing vessels to an area where Vietnam said it would expand oil drilling](#). Reports indicate the Chinese coast guard ships have provocatively cut off Vietnam’s coast guard vessels sailing near an existing oil well. Separately, the Philippine government [has attempted to assert its sovereignty over areas of the](#)

[South China Sea by placing navigation buoys in its exclusive economic zone](#) near the disputed Spratly Islands. China so far has not responded to the placement of those buoys.

**Thailand:** In elections over the weekend, two opposition parties [took the lion's share of the 500 seats in parliament](#). The progressive Move Forward Party was the top vote-getter, earning a projected 151 seats, while the populist Pheu Thai Party earned 141 seats. However, the ruling military junta will have the ultimate say in who forms the next government, a process that could take weeks.

**Argentina:** The government today [will unveil a series of tough economic measures designed to avoid a big currency devaluation ahead of October's elections](#). The measures reportedly will include a 600 bps rise in interest rates, increased central bank intervention in the currency markets, and the elimination of tariffs on food imports to help bring down inflation. The measures apparently don't address the key causes of Argentina's economic problems, such as its big budget deficit.

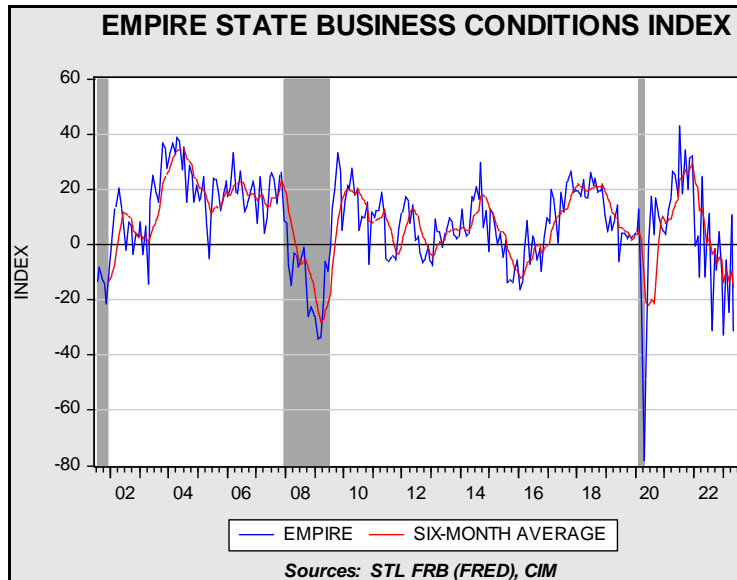
**U.S. Fiscal Policy:** Over the weekend, Treasury Secretary Yellen [said administration officials and congressional Republicans were making progress in their negotiations over an increase in the federal debt limit](#). According to Yellen, the negotiators "have found some areas of agreement" that could lead to a deal that would avoid having the government default on its debt. Reports suggest one potential area of agreement is to temporarily cap federal spending, rather than institute outright cuts, while another is to claw back unused pandemic relief funds. Any deal that removes the risk of a government debt default could prompt a relief rally in financial markets. However, any such rally could be short-lived as investors start to focus again on the likelihood of a recession.

**U.S. Municipal Economies:** Conference and hotel demand in North America [finally surpassed 2019 levels](#) in the fourth quarter of 2022, according to the Events Industry Council, an organization consisting of convention trade groups. Rebounding convention business will likely give a welcome boost to downtown areas in many cities and help bolster municipal tax bases.

**U.S. Weather:** The Pacific Northwest [has been hit with a record-breaking heat wave](#), with temperatures reaching the high 80s in Seattle and the mid-90s in Portland. If they last longer than anticipated, the high temperatures could raise the risk of flooding, worsened drought, and a more dangerous forest fire season.

## **U.S. Economic Releases**

Manufacturing activity in the New York area plummeted in May, according to Federal Reserve Bank of New York's Empire Manufacturing Survey. The regional central bank's general business conditions index came in at -31.8, the sharpest drop in the index since April 2020. The reading was below consensus estimates of -3.9 and previous report's reading of +10.8. Although the index is very volatile, figures below zero indicate contraction.



The chart above shows the FRBNY Empire Manufacturing general business index and its six-month moving average, which currently sits at -19.52. The index's decline was driven by a sharp drop in orders and shipments, thus signaling a slowdown in factory activity. As a result, the weak report will likely reinforce concerns about a potential recession.

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
16:00	Net Long-Term TIC Flows	m/m	Mar		\$71.0b	**
16:00	Total Net TIC Flows	m/m	Mar		\$28.0b	**
Federal Reserve						
EST	Speaker or Event	District or Position				
9:15	Neel Kashkari Makes Intro. Remarks at Labor Market Conference	President of the Federal Reserve Bank of Minneapolis				
14:00	Raphael Bostic Speaks on Bloomberg TV	President of Federal Reserve Bank of Atlanta				
15:00	Raphael Bostic Holds Media Availability Q&A	President of Federal Reserve Bank of Atlanta				
17:00	Lisa Cook Gives Commencement Address at UC Berkeley	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
<b>ASIA-PACIFIC</b>								
Japan	Machine tool orders	y/y	Apr P	-14.4%	-15.2%		**	Equity and bond neutral
	PPI	m/m	Apr	5.8%	7.2%	7.4%	**	Equity and bond neutral
India	Trade Balance	m/m	Apr	-\$15.240b	-\$19.730b	-\$19.550b	*	Equity and bond neutral
	Exports	y/y	Apr	-12.7%	-13.9%		**	Equity and bond neutral
	Imports	y/y	Apr	-14.1%	-7.9%		**	Equity bearish, bond bullish
	Wholesale Prices	y/y	Apr	-0.9%	1.3%	-0.4%	**	Equity and bond neutral
<b>EUROPE</b>								
Eurozone	Industrial Production WDA	y/y	Mar	-1.4%	2.0%	0.1%	**	Equity bearish, bond bullish
Switzerland	Producer & Import Prices	y/y	Apr	1.0%	2.1%		**	Equity bullish, bond bearish
	Domestic Sight Deposits CHF	w/w	12-May	507.1b	505.7b		*	Equity and bond neutral
	Total Sight Deposits CHF	w/w	12-May	520.1b	525.6b		*	Equity and bond neutral
Russia	CPI	y/y	Apr	2.31%	3.51%	2.40%	***	Equity and bond neutral
	Core CPI	y/y	Apr	1.99%	3.72%		**	Equity and bond neutral
<b>AMERICAS</b>								
Canada	Housing Starts	m/m	Apr	261.6k%	213.9k%	213.8k%	**	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)	532	532	0	Up
3-mo T-bill yield (bps)	502	504	-2	Up
TED spread (bps)	30	28	2	Widening
U.S. Sibor/OIS spread (bps)	510	509	1	Up
U.S. Libor/OIS spread (bps)	511	510	1	Up
10-yr T-note (%)	3.49	3.47	0.02	Flat
Euribor/OIS spread (bps)	335	332	3	Up
Currencies	Direction			
Dollar	Down			Down
Euro	Up			Up
Yen	Down			Down
Pound	Up			Up
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.

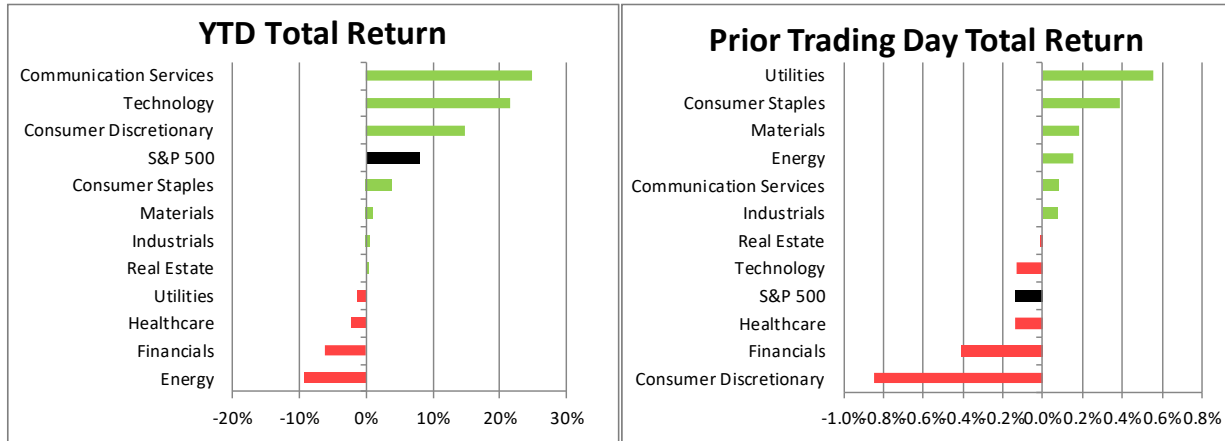
DOE Inventory Report	Price	Prior	Change	Explanation
<b>Energy Markets</b>				
Brent	\$74.57	\$74.17	0.54%	
WTI	\$70.46	\$70.04	0.60%	
Natural Gas	\$2.32	\$2.27	2.29%	
Crack Spread	\$30.24	\$30.17	0.21%	
12-mo strip crack	\$24.58	\$24.47	0.42%	
Ethanol rack	\$2.55	\$2.54	0.20%	
<b>Metals</b>				
Gold	\$2,013.04	\$2,010.77	0.11%	
Silver	\$23.96	\$23.97	-0.04%	
Copper contract	\$377.45	\$372.85	1.23%	
<b>Grains</b>				
Corn contract	\$589.75	\$586.25	0.60%	
Wheat contract	\$649.25	\$635.00	2.24%	
Soybeans contract	\$1,399.75	\$1,390.00	0.70%	
<b>Shipping</b>				
Baltic Dry Freight	1,558	1,608	-50	

## Weather

The 6-10 and 8-14 day forecasts currently call for warmer-than-normal temperatures along the West Coast, in the Rocky Mountain region, and in Florida, with cooler-than-normal temperatures in the Southwest. The forecasts are calling for wetter-than-normal conditions in the Southwest, Texas, and the Southeast, with dry conditions expected in most of the Pacific Northwest, the northern Rocky Mountain region, and the northern Great Plains.

**Data Section**

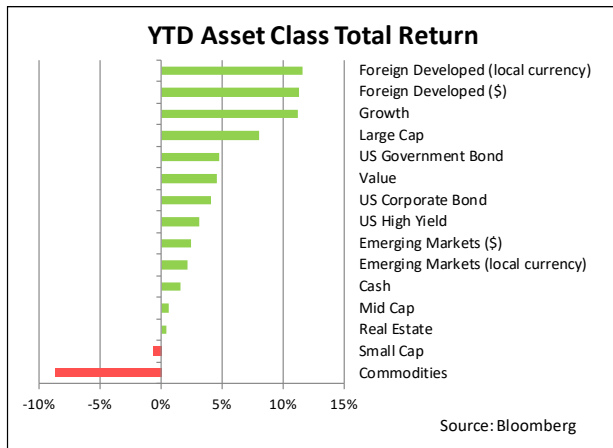
**U.S. Equity Markets – (as of 5/12/2023 close)**



(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 5/12/2023 close)**



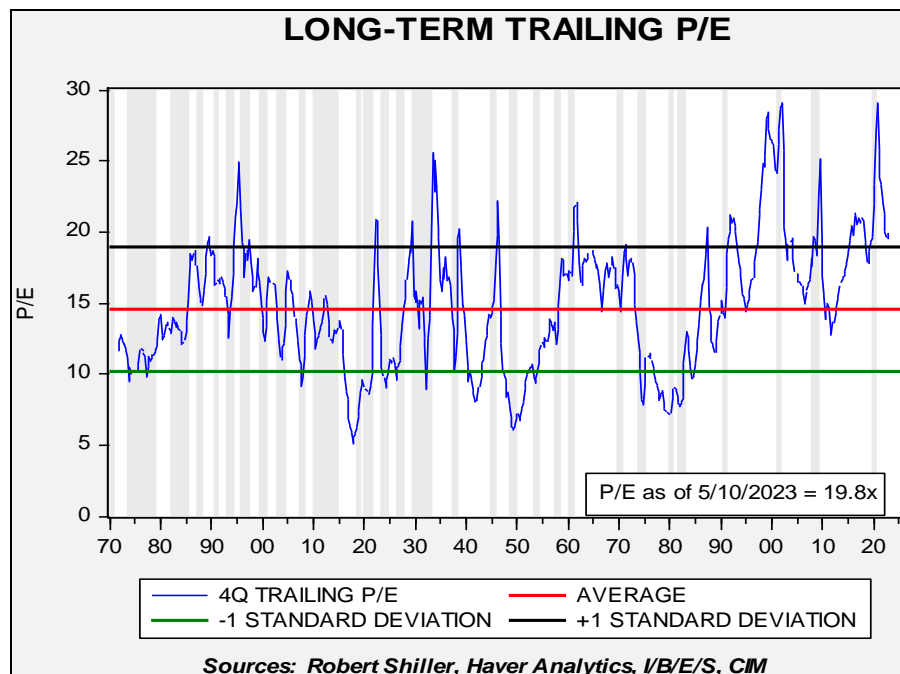
This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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

May 11, 2023



Based on our methodology,<sup>1</sup> the current P/E is 19.8x, down 0.2x from last week. Improved earnings led to the lower 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.*

<sup>1</sup> 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 (Q3 and Q4) and two estimates (Q1 and Q2). 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.