Daily Comment

Confluence INVESTMENT MANAGEMENT

By Patrick Fearon-Hernandez, CFA, and Thomas Wash

[Posted: May 20, 2026 — 9:30 AM ET] Global equity markets are mixed this morning. In Europe, the Euro Stoxx 50 is up 0.8% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed down 0.4%. Chinese markets were lower, with the Shanghai Composite down 0.2% and the Shenzhen Composite down 0.3%. US equity index futures are signaling a higher open.

With 454 companies having reported so far, S&P 500 earnings for Q1 are running at $80.30 per share compared to estimates of $72.32, which is up 12.6% from Q1 2025. Of the companies that have reported thus far, 82.6% exceeded expectations, while 11.9% fell 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 in bold.

Bi-Weekly Geopolitical Report	Asset Allocation Bi-Weekly	Asset Allocation Quarterly	Of Note
"The Trade Trilemma *Revisited*" (5/18/26)	"The Power of Gold" (5/11/26) + **podcast (5/20/26)**	Q2 2026 Report	Confluence of Ideas podcast Confluence Mailbag

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

Our *Comment* opens with our views on how rising bond yields are creating new openings in the market, including in private credit, followed by an update on intensifying tensions in Iran. We also cover increasing Congressional scrutiny of Middle East policy, the US troop drawdown in Poland, and the impact of AI on the labor market. As always, we provide a comprehensive roundup of the latest international and domestic economic indicators.

A New Hope: There is a global sell-off in bonds as markets grapple with rising deficit spending and persistent inflation. On Tuesday, the 10-year US Treasury yield climbed to its highest level in 19 years, while yields in Japan, the UK, and France also rose to multi-year highs. The move reflects investors stepping back from sovereign debt amid mounting concerns over fiscal sustainability and the cost of funding measures intended to cushion the impact of higher rates. However, the rising uncertainty may prompt a rethink of private credit.

- In the US, the rise in yields reflects investors grappling with several mounting risks at once. A combination of war-related energy shocks feeding inflation, large fiscal deficits, and a still-resilient economy has led markets to demand a higher risk premium on government debt. This, in turn, has fueled concerns that the Federal Reserve may need to keep interest rates at current levels for even longer.
- For the rest of the world, concerns center more on expanding fiscal spending alongside a potential slowdown in growth. Governments across Europe and Asia have begun rolling out energy subsidies to help households cope with higher prices. To finance these measures, they are expected to issue additional debt, prompting investors to demand higher compensation to absorb the increased supply.
- However, there have been some clear winners. Rising bond yields have fueled a renewed bid for the AI trade, which investors increasingly view as a relative haven amid higher interest rate expectations. This rotation has supported markets with heavy technology exposure — most notably US large-cap equities, but also South Korea and Taiwan, which remain key exporters of components critical to AI infrastructure.
- Additionally, private credit sentiment may also improve meaningfully as software companies have staged a notable rebound. Software issuers that were effectively written off earlier in the year on "going concern" fears tied to AI disruption are now beginning to stabilize. In particular, large platforms such as ServiceNow, Workday, and Salesforce — initially caught up in the "SaaSpocalypse" narrative — have posted a marked recovery over the past several weeks.
- While higher interest rates create headwinds for the global economy and select sectors, we still see areas that are compelling for investment. AI-linked equities, though crowded, continue to deliver strong performance. At the same time, private credit and business development companies (BDCs) look attractive in this environment, supported by their floating-rate debt exposure, meaningful links to a recovering software sector, and the recent re-rating of many software names.

New Conflict: President Trump has warned that time is running out for Iran to reach an agreement before he authorizes additional strikes. The threat comes as both sides continue to spar over the terms for reopening the Strait of Hormuz. In a show of defiance, Iran has said it is prepared to defend itself against any attack. The growing impasse has prompted regional and global powers to take a more active role in mediating the conflict, while global markets brace for a resolution.

- The president's latest threat came after he said he had received assurances from China that it would not supply weapons to Iran. His remarks referenced last week's meeting with President Xi, in which the two leaders discussed issues ranging from trade and intellectual property to AI and foreign policy. President Trump suggested those talks also included a commitment from Xi not to provide arms to Tehran.

- As the president prepares additional measures against Iran, he appears to have helped nudge NATO toward considering a larger role. The alliance has reportedly discussed deploying naval forces to the strait if it remains closed into early July. While there are still no clear signs of the unanimous backing required for such an operation, the debate itself suggests momentum is starting to move in that direction.
- The growing involvement of additional countries has increased the risk that the conflict could widen beyond Iran. China's role raises the prospect of the war evolving into a proxy confrontation with the United States, potentially driving a further deterioration in bilateral relations if tensions escalate. At the same time, possible NATO involvement could draw European states more directly into the crisis, adding another layer of complexity and heightening the risk of broader regional instability.
- In a world where conflict risks are rising, we expect these conditions to favor hard assets and broad-based increases in defense spending. Precious metals look particularly appealing as non-US-aligned countries, including China, seek to hedge their exposure to the dollar. Defense companies, especially in Europe, may also benefit as governments are forced to shoulder a greater share of their own security burden.

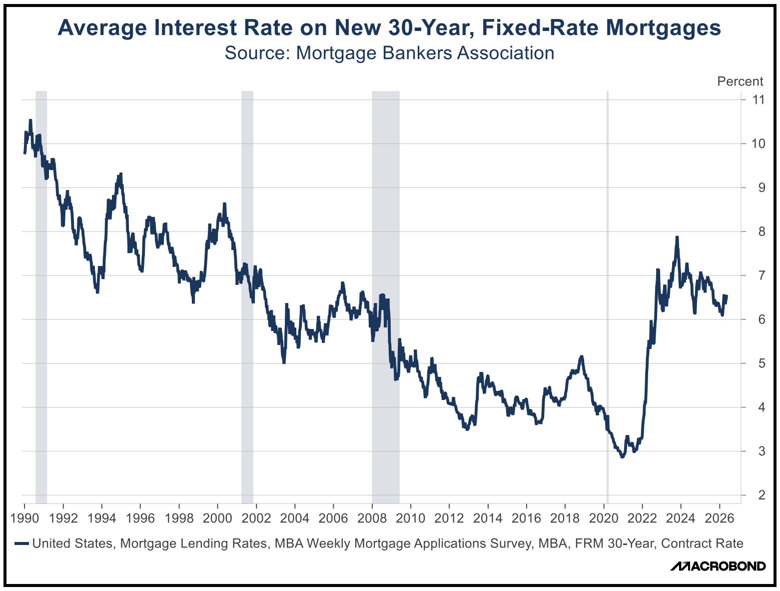
Congressional Pushback: There is growing pressure in Washington to bring the US standoff with Iran to an end. On Tuesday, Republicans joined Democrats in clearing a key procedural hurdle that paved the way for a final vote on a resolution to halt the war in Iran. The bipartisan push reflects the conflict's increasing political unpopularity and could complicate the president's efforts to secure further concessions from Tehran. That said, we think any such bill is unlikely to become law and will remain largely symbolic.

US Withdrawal: The US military has begun reducing its troop presence in Europe as it seeks to recalibrate its foreign policy posture. This week, Washington canceled the planned deployment of 4,000 troops to Poland, bringing the regional force level back toward its pre-Ukraine-invasion baseline and signaling a White House push for Europe to lessen its dependence on US security guarantees. In our view, this shift is likely to spur higher EU defense spending as European governments move toward greater self-reliance in defense.

AI Job Displacement: A growing number of technology and financial firms are turning to AI to streamline operations and reduce headcount. Standard Chartered's CEO, for example, has signaled plans to cut nearly 8,000 roles as the bank seeks to eliminate redundancies, while Meta has pursued similar reductions in the name of efficiency. So far, AI-related layoffs have been relatively contained, but the acceleration of investment in automation raises the risk that job cuts could broaden into other sectors over time.

US Economic Releases

The Mortgage Bankers Association said ***mortgage applications*** in the week ended May 15 fell 2.3%, erasing all of their 1.7% gain in the previous week. Applications for home purchase mortgages fell 4.1%, just erasing their 3.9% rise in the prior week. Applications for refinancing mortgages only edged down 0.1%, but that still marked the fourth straight week of declines. The average interest rate on a 30-year, fixed-rate mortgage rose 10 basis points to 6.56%. The chart below shows how mortgage rates have changed over time.



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

Economic Releases		
No economic releases for the rest of today		
Federal Reserve		
EST	**Speaker or Event**	**District or Position**
9:15	Michael Barr Speaks on Consumer Financial Health	Members of the Board of Governors
14:00	U.S. Federal Reserve Releases Meeting Minutes	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 shift 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								
India	Eight Infrastructure Industries	m/m	Apr	1.70%	1.20%		*	Equity and bond neutral
EUROPE								
Eurozone	CPI	y/y	Apr F	3.0%	3.0%	3.0%	***	Equity and bond neutral
	Core CPI	y/y	Apr F	2.2%	2.2%	2.2%	**	Equity and bond neutral
Germany	PPI	y/y	Apr	1.7%	-0.2%	1.5%	**	Equity and bond neutral
UK	CPI	y/y	Apr	2.8%	3.3%	3.0%	***	Equity and bond neutral
	CPI Core	y/y	Apr	2.5%	3.1%	2.6%	***	Equity and bond neutral
	Retail Price Index	m/m	Apr	414.4	411.4	416.1	**	Equity and bond neutral
	RPI	y/y	Apr	3.0%	4.1%	3.6%	**	Equity bullish, bond bearish
	House Price Index	y/y	Mar	0.0%	1.7%		*	Equity and bond neutral
AMERICAS								
Canada	CPI	y/y	Apr	2.8%	2.4%	3.1%	***	Equity and bond neutral
	Building Permits	m/m	Mar	10.3%	-7.8%	2.40	**	Equity bullish, bond bearish
	Consumer Price Index	m/m	Apr	168.0	167.4	168.3	*	Equity and bond neutral
Mexico	International Reserves Weekly	w/w	15-May	$255758m	257030m		*	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)	356	357	-1	Up
U.S. Sibor/OIS spread (bps)	363	363	0	Down
U.S. Libor/OIS spread (bps)	364	364	0	Up
10-yr T-note (%)	4.64	4.67	-0.03	Up
Euribor/OIS spread (bps)	220	222	-2	Up
Currencies	**3 Mo**			
Dollar	Down	US		Up
Euro	Up	Euro		Down
Yen	Up	Japan		Down
Pound	Up	UK		Down
Franc	Up	Switzerland		Down
Central Bank Action	**Actual**	**Prior**	**Expected**	
PBOC 5-Year Loan Prime Rate	3.50%	3.50%	3.50%	On Forecast
PBOC 1-Year Loan Prime Rate	3.00%	3.00%	3.00%	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.

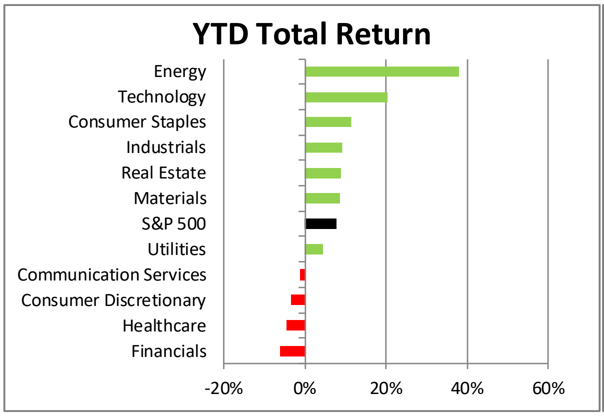
	Price	Prior	Change	Explanation
Energy Markets				
Brent	$108.55	$111.28	-2.45%	
WTI	$101.72	$104.15	-2.33%	
Natural Gas	$3.09	$3.11	-0.74%	
Crack Spread	$51.74	$54.00	-4.18%	
12-mo strip crack	$41.65	$43.85	-5.04%	
Ethanol rack	$2.21	$2.21	0.03%	
Metals				
Gold	$4,493.59	$4,482.61	0.24%	
Silver	$75.63	$73.73	2.57%	
Copper Contract	$623.70	$620.65	0.49%	
Grains				
Corn contract	$472.75	$475.25	-0.53%	
Wheat contract	$669.25	$667.25	0.30%	
Soybeans contract	$1,207.00	$1,209.50	-0.21%	
Shipping				
Baltic Dry Freight	3,054	3,092	-38	
DOE Inventory Report				
	Actual	**Expected**	**Difference**	
Crude (mb)		-2.50		
Gasoline (mb)		-2.16		
Distillates (mb)		-1.65		
Refinery run rates (%)		0.90%		
Natural gas (bcf)		98		

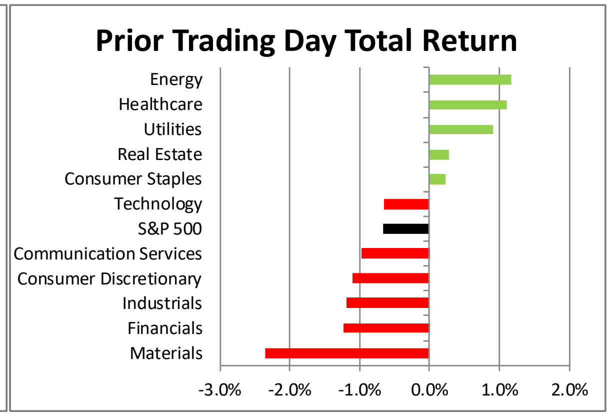
Weather

The 6-to-10-day and 8-to-14-day forecasts currently call for warmer-than-normal temperatures in the northern and central Rocky Mountains, the Great Plains, and all points east of the Mississippi River, with near-normal temperatures elsewhere. The outlook calls for wetter-than-normal conditions in the central and southern Rocky Mountains, the southern Great Plains, and the Deep South, with dry conditions in the Great Lakes region.

Data Section

US Equity Markets – (as of 5/19/2026 close)

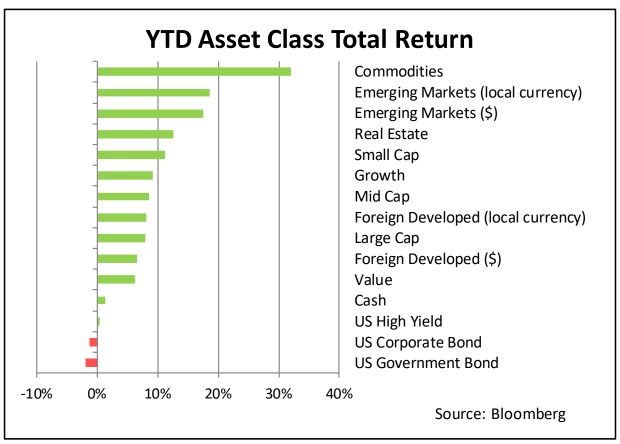




(Source: Bloomberg)

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 5/19/2026 close)

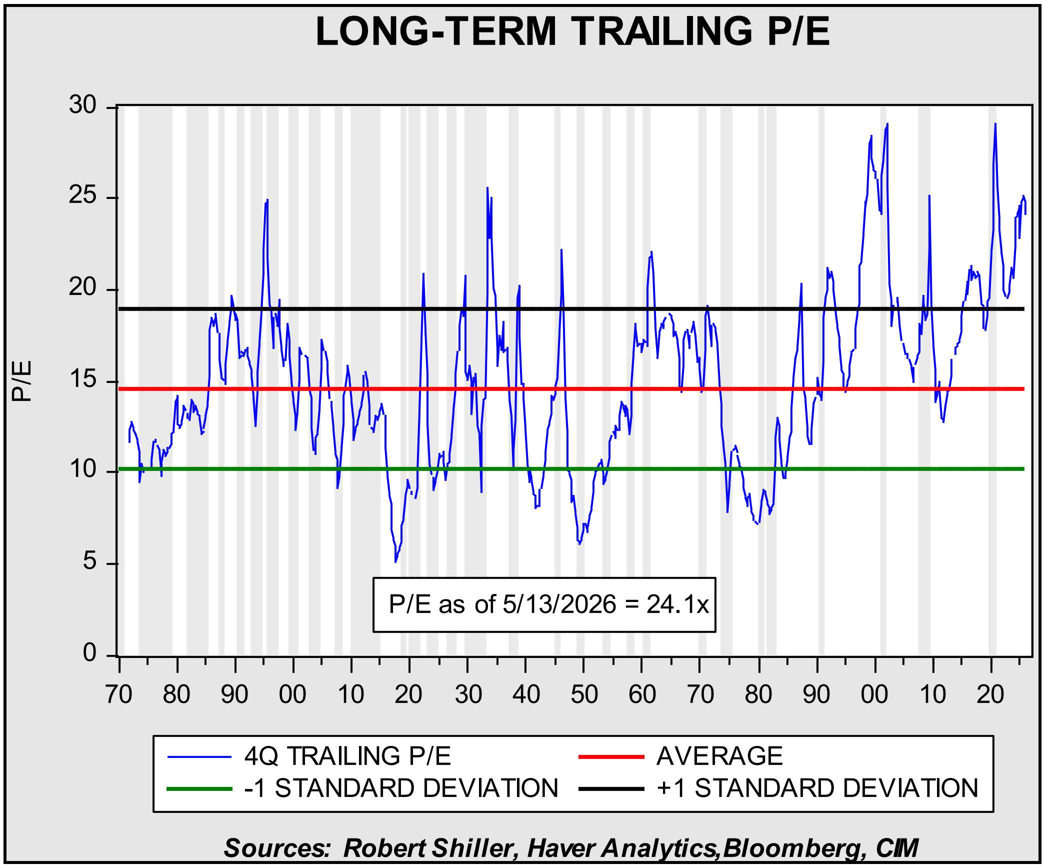


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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

May 14, 2026



Based on our methodology,[1] the current P/E is 24.1x, up 0.3 from the previous report. Last week, the increase in the stock price index outpaced the rise in earnings.

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 Bloomberg estimates which are updated regularly throughout the quarter; currently, the four-quarter earnings sum includes three actual quarters (Q1, Q2, Q4) and one estimate (Q3). 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.