

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 22, 2024—9:30 AM EDT] Global equity markets are mixed this morning. In Europe, the Euro Stoxx 50 is down 0.3% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed up 0.5%. Chinese markets were slightly higher, with the Shanghai Composite essentially unchanged from its previous close and the Shenzhen Composite up 0.2%. Conversely, US equity index futures are signaling a lower open.

With 470 companies having reported so far, S&P 500 earnings for Q1 are running at \$56.40 per share compared to estimates of \$54.24, which is up 0.9% from Q1 2023. Of the companies that have reported thus far, 79.1% have exceeded expectations, while 16.6% 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](#)** (5/20/2024) (there is no associated podcast): “The Great COVID Labor Reform”
- [Asset Allocation Quarterly – Q2 2024](#) (4/25/2024): Discussion of our asset allocation process, Q2 2024 portfolio changes, and our outlook for the markets.
- [Asset Allocation Q2 2024 Rebalance Presentation](#) (5/7/2024): Video presentation featuring the Asset Allocation Committee as they review the asset allocation strategies, recent portfolio changes, and the current macro environment.
- [Asset Allocation Bi-Weekly](#) (5/13/2024) (with associated [podcast](#)): “The Immigration Paradox”
- [Confluence of Ideas podcast](#) (5/8/2024) “Reviewing the Asset Allocation Rebalance: Q2 2024”

Our *Comment* today opens with a potentially incendiary revelation that the US and UK have intelligence showing China is now sending, or preparing to send, lethal aid to Russia for its invasion of Ukraine. We next review several other international and US developments with the potential to affect the financial markets today, including signs of stickier-than-expected consumer price inflation in the UK and a couple of notes on the US financial markets.

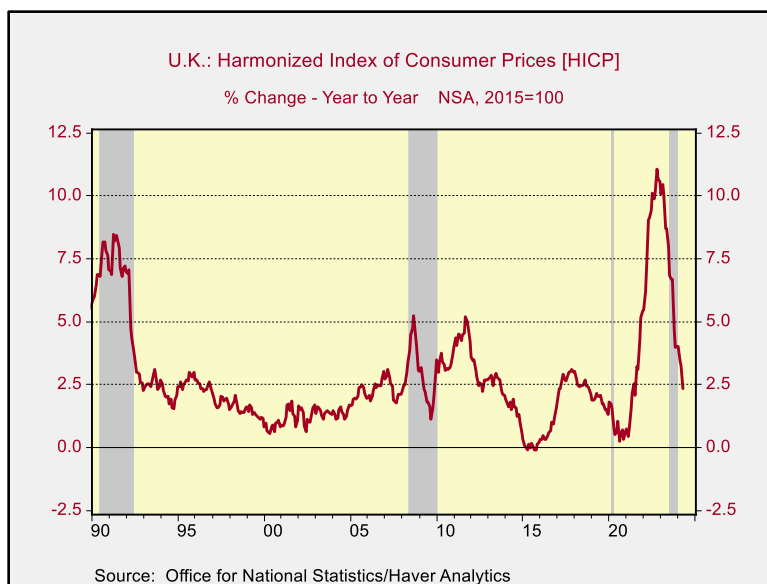
China-Russia: At a defense conference in London today, British Defense Secretary Shapps said new US and UK intelligence [shows that China is currently sending, or will soon be sending,](#)

[lethal aid to Russia for its invasion of Ukraine](#). Shapps said the new intelligence shows that China and Russia have recently developed what he called a “deeper relationship.” This report comes just a week after Russian President Putin visited Chinese General Secretary Xi in Beijing, and as the two are planning another meeting this summer.

- The revelation by Shapps is potentially incendiary. US and other Western leaders have repeatedly warned Beijing not to provide lethal aid to Russia for its illegal invasion of Ukraine. Leaders in Washington have warned that the US would impose sanctions directly on China if it provided such aid to the Kremlin.
- As a reminder, our objective, quantitatively driven methodology for classifying countries by geopolitical bloc places Russia squarely in the China-led camp. More generally, we see Russia as the junior partner in that camp, which explains why we often refer to it as the “China/Russia bloc.” If China has now decided to accept the geopolitical and economic risk of providing lethal aid to Russia despite Western warnings, it suggests the relationship really has deepened, as Shapps suggests.
- Going forward, the new intelligence could potentially force Western leaders to live up to their warnings against Beijing. If that leads to substantial sanctions directly on China, then the current spiral of tensions between the West and China would likely worsen, creating further risks for the global economy and investors.

United Kingdom-Hong Kong-China: A former Royal Marine and UK immigration official who had been arrested for spying for Hong Kong [was found dead in a park west of London](#). The incident is likely to spark concern that China, through its Hong Kong operatives, is working to silence Westerners who have been coopted to work for its intelligence services. Such concern would heighten the existing tensions between the US and China/Russian geopolitical blocs.

United Kingdom: The April consumer price index [was up just 2.3% from the same month one year earlier, after increases of 3.2% in the year to March](#) and 3.4% in the year to February. Consumer price inflation in the UK is now well below its cycle peak of 11.1% in October 2022. Nevertheless, the slowdown in April wasn’t quite as dramatic as investors were expecting. The data has therefore reduced expectations that the Bank of England could cut interest rates at its June policy meeting.



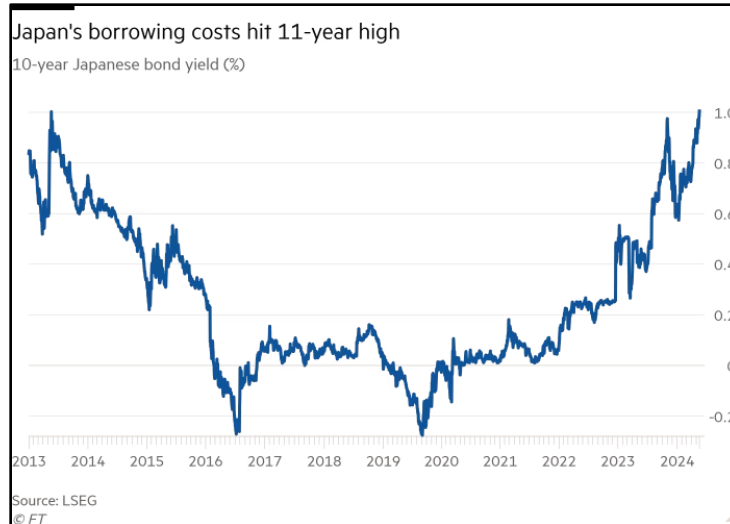
France: President Macron [has embarked on an emergency trip to France’s overseas territory of New Caledonia, an island some 900 miles northeast of Australia](#), to help quell the rioting touched off by a new French law, which gives nonindigenous citizens in the territory more voting rights. Importantly, the unrest is threatening Macron’s vision of leveraging New Caledonia’s vast nickel supplies to make Europe a leader in green technologies.

Israel: The Israeli government today [recalled its ambassadors to Ireland, Spain, and Norway over the trio’s plan to formally recognize a Palestinian state](#) effective May 28. Several other European countries have recognized a Palestinian state for years, but the move by Ireland, Spain, and Norway appears to have touched a nerve in Tel Aviv amid growing international criticism of Israel over its war against Hamas in the Gaza Strip.

- Of course, Israeli leaders are also angry about an International Criminal Court (ICC) prosecutor’s recent request for arrest warrants for Israeli and Hamas leaders over their conduct in the conflict.
- Reflecting the US’s largely bipartisan support for Israel, Secretary of State Blinken yesterday [said the Biden administration will work with Congress to craft sanctions](#) on the ICC to punish it for the prosecutor’s call to arrest the Israeli leaders.

Japan: As investors increasingly expect the Bank of Japan (BOJ) to further tighten monetary policy, the yield on 10-year Japanese government bonds (JGB) [rose above 1% today for the first time in 11 years](#). The most recent leg up in yields began on May 13, when the BOJ surprised investors by buying a smaller-than-expected amount of 5-year and 10-year JGBs.

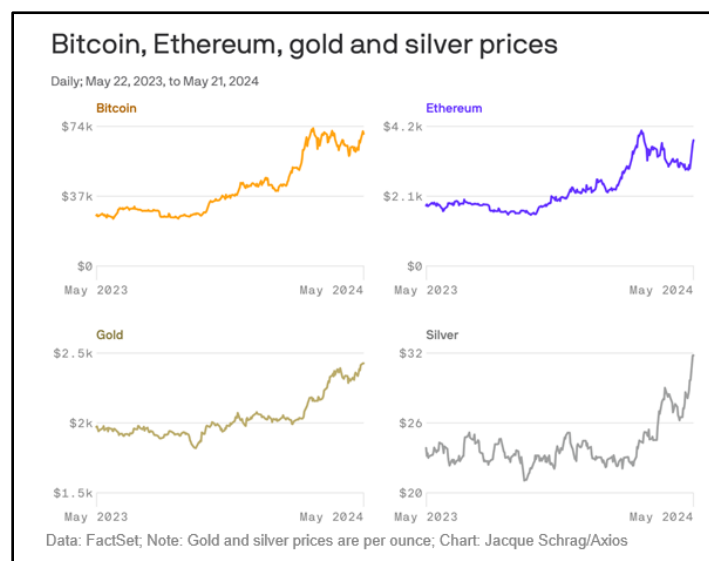
- Despite the rise in 10-year yields, however, the yen (JPY) has continued to weaken.
- The currency is trading down 0.25% to 156.57 per dollar (\$0.0064) so far this morning.



US Stock Market: One key event for the stock market today [will be Nvidia's earnings release](#), due shortly after market close. Given that Nvidia and other artificial-intelligence darlings have been key drivers of the overall stock indexes recently, anticipation of the release could have a significant impact on trading today.

US Commodity Markets: In another note on the financial markets, we've noticed that there's a [new acronym being used to describe a fast-rising appreciating set of assets](#). The new acronym, BEGS, refers to Bitcoin, Ethereum, Gold, and Silver. The common threat in these assets is that they have no associated cash flow, so they should in theory be struggling against today's high interest rates.

- For bitcoin and Ethereum, it appears that their recent upward trajectory mostly reflects expectations of more cryptocurrency deregulation.
- For gold and silver, the upward momentum reflects rising geopolitical tensions and strong buying by Chinese central bankers and consumers.



US Economic Releases

Homebuyer interest in mortgages ticked up last week as rates dipped slightly. According to the Mortgage Bankers Association (MBA), applications to purchase homes increased 1.9% for the week ending May 17. This uptick coincides with a decrease in borrowing costs, as the average 30-year fixed-rate mortgage fell 7 basis points to 7.01%. As a result, the MBA's purchase tracker rose 1.9%, while the refinance tracker saw a larger jump of 7.4%.

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
10:00	Existing Home Sales	m/m	Mar	5.77m	6.02m	**
Federal Reserve						
EST	Speaker or Event	District or Position				
9:40	Austan Goolsbee Gives Opening Remarks	President of the Federal Reserve Bank of Chicago				
14:00	FOMC 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 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	Trade Balance	y/y	Apr	-¥462.5	¥387.0b	-¥296.0b	**	Equity and bond neutral
	Exports	y/y	Apr	8.3%	7.3%	11.0%	*	Equity bearish, bond bullish
	Imports	y/y	Apr	8.3%	-5.1%	8.9%	*	Equity bearish, bond bullish
	Core Machine Orders	y/y	Mar	2.7%	-1.8%	1.4%	**	Equity and bond neutral
South Korea	PPI	y/y	Apr	1.8%	1.5%		**	Equity and bond neutral
	Business Survey - Manufacturing	m/m	Jun	76	74		**	Equity and bond neutral
	Business Survey - Non-Manufacturing	m/m	Jun	72	71		*	Equity and bond neutral
EUROPE								
UK	Public Finances (PSNCR)	m/m	Apr	-5.2b	21.7b		*	Equity and bond neutral
	Public Sector Net Borrowing	m/m	Apr	19.6b	12.1b	18.5b	*	Equity and bond neutral
	PSNB ex Banking Groups	m/m	Apr	20.5b	13.1b	19.3b	**	Equity and bond neutral
	CPI	y/y	Apr	2.3%	3.2%	2.1%	***	Equity and bond neutral
	CPI Core	y/y	Apr	3.9%	4.2%	3.6%	***	Equity and bond neutral
	RPI	y/y	Apr	3.3%	4.3%	3.3%	**	Equity and bond neutral
AMERICAS								
Canada	CPI	y/y	Apr	2.7%	2.9%	2.7%	***	Equity and bond neutral
Mexico	International Reserves Weekly	w/w	17-May	\$218953m	\$218229m		*	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 Libor yield (bps)	559	559	0	Flat
3-mo T-bill yield (bps)	524	523	1	Up
U.S. Sibor/OIS spread (bps)	534	533	1	Flat
U.S. Libor/OIS spread (bps)	535	534	1	Up
10-yr T-note (%)	4.46	4.41	0.05	Up
Euribor/OIS spread (bps)	382	382	0	Down
Currencies	Direction			
Dollar	Up			Up
Euro	Down			Flat
Yen	Down			Down
Pound	Flat			Up
Franc	Down			Down
Central Bank Action	Current	Prior	Expected	
RBNZ Official Cash Rate	5.500%	5.500%	5.500%	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.

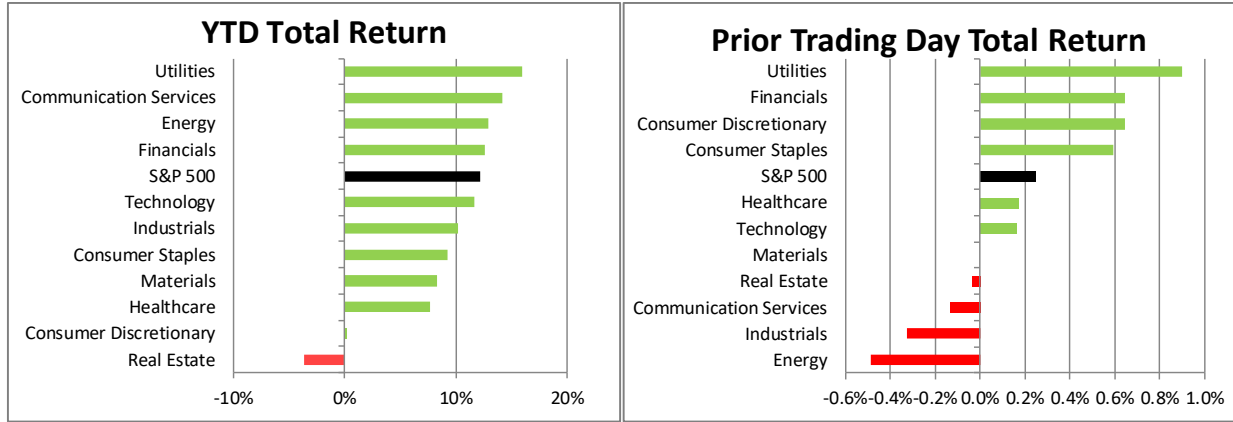
DOE Inventory Report	Price	Prior	Change	Explanation
Energy Markets				
Brent	\$82.25	\$82.88	-0.76%	
WTI	\$78.05	\$78.66	-0.78%	
Natural Gas	\$2.66	\$2.67	-0.34%	
12-mo strip crack	\$22.40	\$22.71	-1.33%	
Ethanol rack	\$1.93	\$1.93	-0.15%	
Metals				
Gold	\$2,406.91	\$2,421.05	-0.58%	
Silver	\$31.55	\$31.98	-1.33%	
Copper contract	\$498.25	\$510.60	-2.42%	
Grains				
Corn contract	\$461.25	\$458.00	0.71%	
Wheat contract	\$707.50	\$697.50	1.43%	
Soybeans contract	\$1,239.25	\$1,236.25	0.24%	
Shipping				
Baltic Dry Freight	1,829	1,847	-18	
DOE Inventory Report				
	Actual	Expected	Difference	
Crude (mb)		-2.00		
Gasoline (mb)		-1.38		
Distillates (mb)		0.30		
Refinery run rates (%)		0.5%		
Natural gas (bcf)		83		

Weather

The 6-10 and 8-14 day forecasts call for warmer-than-normal temperatures throughout most of the country, with cooler temperatures expected in the Midwest and Mid-Atlantic states. The forecasts call for wetter-than-average conditions throughout most East Coast and southern states, with drier-than-normal conditions expected in the Rocky Mountain and Pacific regions.

Data Section

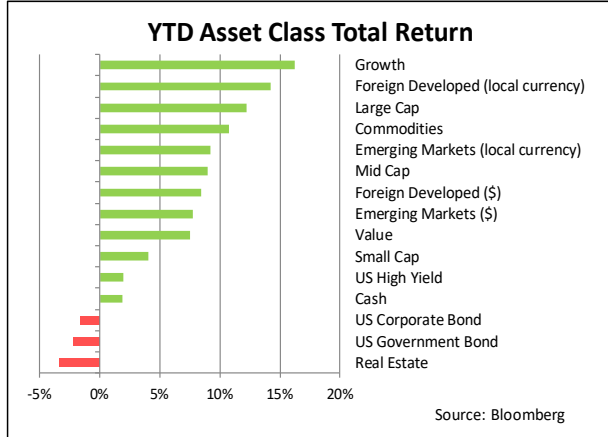
US Equity Markets – (as of 5/21/2024 close)



(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 5/21/2024 close)

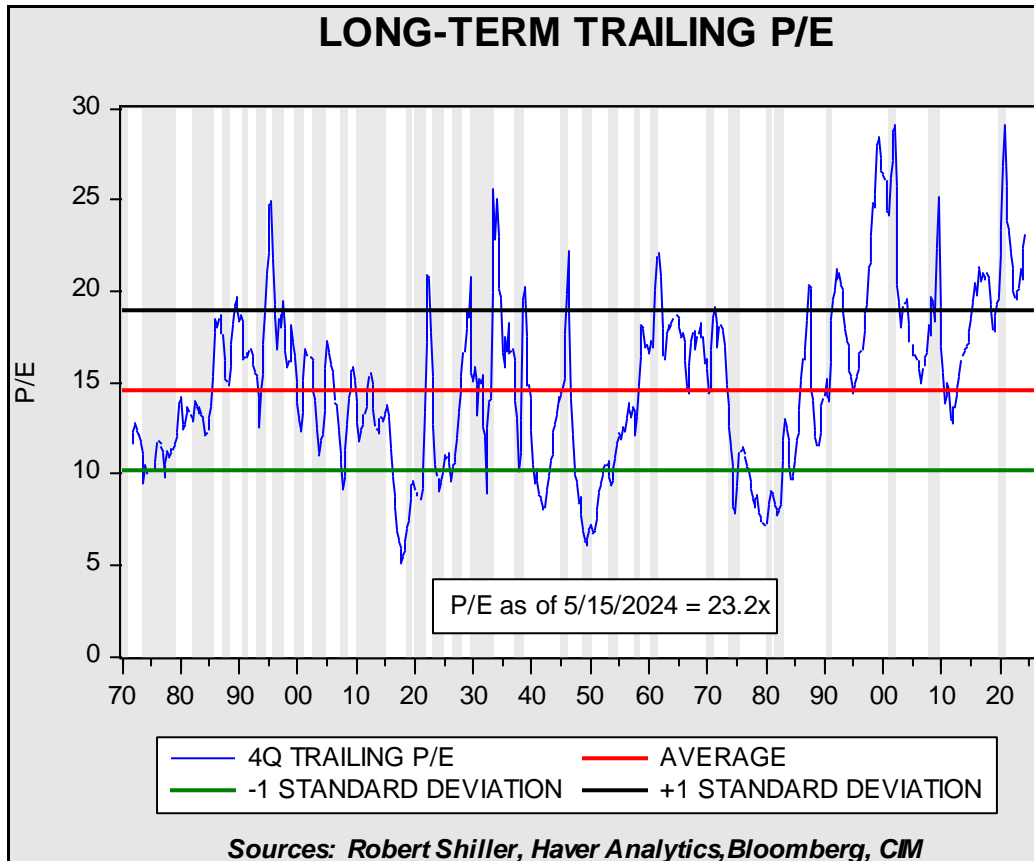


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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 16, 2024



Based on our methodology,¹ the current P/E is 23.2x, up 0.1x from our last report. The increase in the multiple reflects an increase in the S&P 500 Index, outweighing the increase 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 (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.