Daily Comment

By Patrick Fearon-Hernandez, CFA, and Thomas Wash

Posted: May 22, 2025 — 9:30 AM ET] Global equity markets are lower this morning. In Europe, the Euro Stoxx 50 closed down 1.0% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed down 1.0%. Chinese markets were lower, with the Shanghai Composite down 0.2% from its previous close and the Shenzhen Composite down 1.0%. US equity index futures are signaling a lower open.

With 469 companies having reported so far, S&P 500 earnings for Q1 are running at $63.90 per share compared to estimates of $60.75, which is up 7.3% from Q1 2024. Of the companies that have reported thus far, 77.0% have exceeded expectations, while 19.2% 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 in bold.

Bi-Weekly Geopolitical Report	Asset Allocation Bi-Weekly	Asset Allocation Quarterly	Of Note
"Update on the US-China Military Balance of Power" (5/12/25) + podcast	"The Looming Battle for US Monetary Policy" (5/19/25) + podcast	Q2 2025 Report Q2 2025 Rebalance Presentation	Confluence of Ideas Podcast Value Equity Quarterly Update

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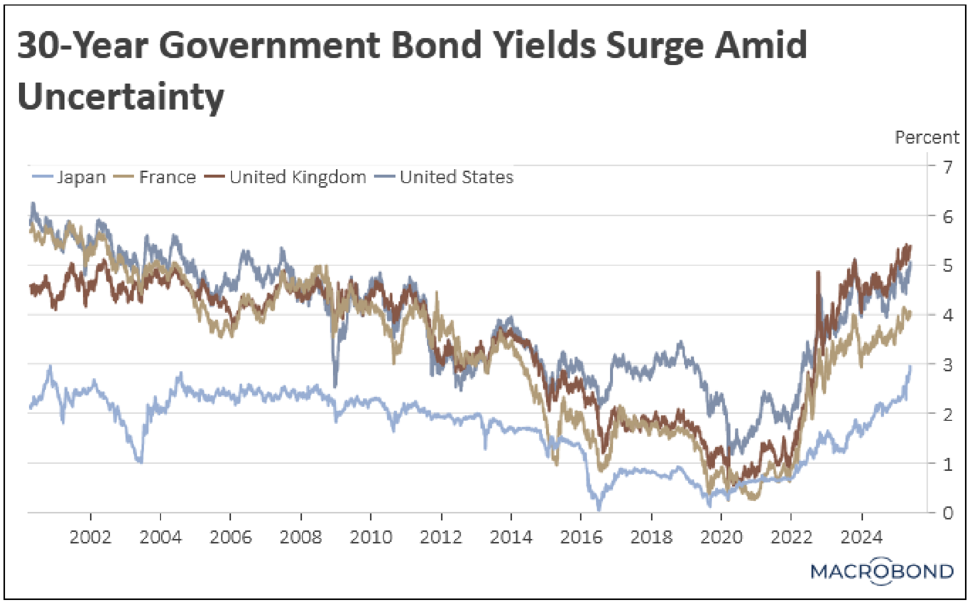
Good morning! Financial markets are monitoring developments in the pending tax legislation. In sports, Tottenham Hotspur ended their 17-year trophy drought with a dramatic Europa League final victory over Manchester United. Today's *Comment* will examine growing concerns about US debt sustainability, analyze progress in EU-US trade negotiations, and highlight other market developments. As usual our report includes a summary of domestic and international economic data releases.

Debt Problem: Tepid demand at auction reflects investor focus pivoting from trade and toward fiscal deficits.

- The Treasury's $16 billion 20-year bond auction on Wednesday saw weak demand as yields rose above 5% for the first time since October 2023. The poor showing resulted in a 1.2 basis point tail (the spread between average and lowest accepted yields), which was significantly wider than the recent -0.4 bp average. This miss reflects dwindling appetite among rate-sensitive buyers, with domestic investors particularly reluctant to absorb the bulk of issuance at current yield levels.

- The weak auction results will likely fuel concerns about sovereign credit quality, especially after Moody's downgrade of the US credit rating last week. Since the decision, long-dated bond yields have climbed across the US and other G-7 economies as investors grow wary of duration risk. Rising debt sustainability worries, persistent inflation, and ongoing trade tensions have all contributed to this reluctance.

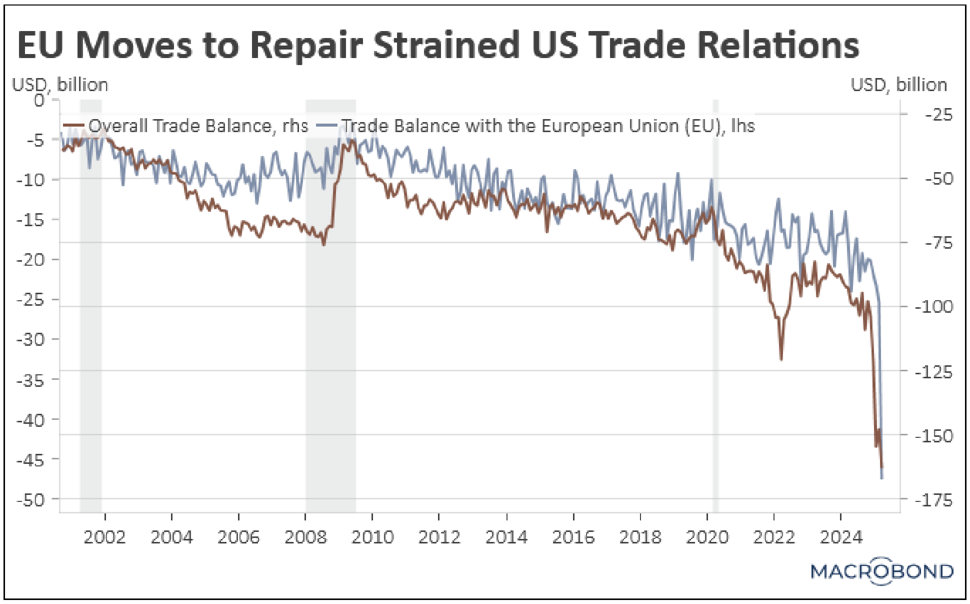


- Investors are closely tracking the new tax bill's progress through Congress as lawmakers debate critical provisions. Key sticking points include proposed cuts to green energy credits and Medicaid, along with potential tax increases aimed at covering the bill's costs. According to Congressional Budget Office estimates, the legislation could increase the national debt by approximately $3.8 billion over the next 10 years.
- The interplay between rising interest rates and the proposed tax bill creates competing forces for equity markets. While the stimulus measures could bolster business and household incomes, potentially driving higher consumption and investment, tightening financial conditions may pressure corporate margins and dampen household borrowing. Although we currently assess the tax package as a net positive, the trajectory of interest rates warrants close monitoring, as further increases could pose headwinds for equities.

EU Wants a Deal: Brussels has updated its trade proposal to the Trump administration in an effort to prevent further tariff escalation.

- The new proposal aims to address White House priorities on regulatory reform and trade policy more effectively. Although specific details have not yet been released, the framework seeks to identify areas of alignment, particularly regarding international labor standards, environmental protections, and economic security measures. The plan also includes provisions for targeted investments and strategic procurement initiatives in key sectors such as energy and artificial intelligence.

- The EU's latest proposal comes as it seeks to revive negotiations with the US and build diplomatic momentum. Initially, the bloc offered a "zero-for-zero" tariff arrangement on automobiles and industrial goods, but the White House rejected the proposal. The EU remains hopeful that it can persuade the current administration to reduce tariffs and has warned of retaliatory measures if it fails to secure a more favorable deal than the one recently obtained by the UK.



- The upcoming US-EU negotiations are expected to focus primarily on trade reciprocity and equitable market access. Washington has consistently argued that Brussels maintains regulatory frameworks that effectively serve as non-tariff barriers, particularly targeting American agricultural exports and digital services. These measures have significantly hindered the ability of US companies to compete fairly in the European market.
- Nevertheless, a US-EU agreement appears increasingly likely, as the White House has emphasized its goal of finalizing a trade deal by mid-summer. We anticipate the new framework will center on coordinated efforts to counterbalance China's economic influence, resulting in a mutual reduction — though not complete elimination — of tariffs. As negotiations progress, we expect trade tensions to gradually ease in the coming weeks.

AI Importance: A senior CIA official has declared that outpacing China in artificial intelligence development now represents America's foremost intelligence priority.

- The official's remarks follow concerted US efforts to strengthen international partnerships regarding semiconductor supply chains. CIA leadership has announced plans to reorganize the agency and refocus priorities to better counter China's technological advancements. This strategic shift reflects the expanding nature of US-China competition, which has evolved beyond trade disputes to encompass critical technology sectors.

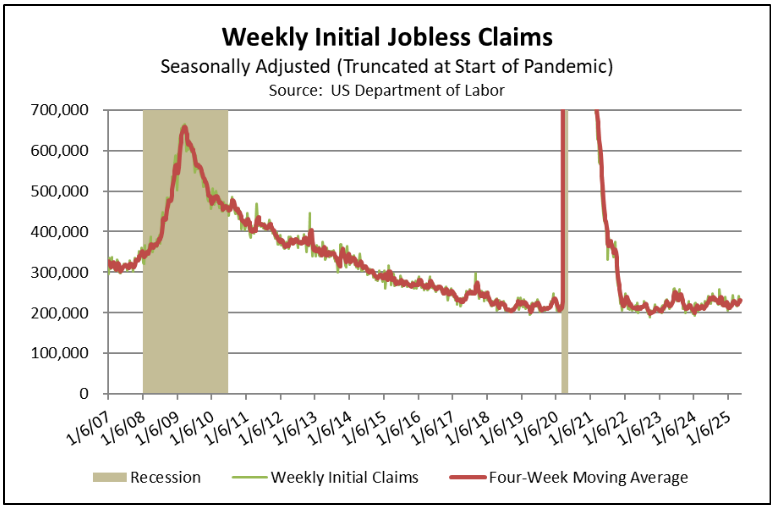
- President Trump's recent trip to the Middle East signaled this shift in US policy priorities. During his visit, the president sought to strengthen alliances with Gulf nations by offering access to advanced American AI technology and commitments to support their technological infrastructure development. Additionally, his administration has rolled back previous restrictions that limited these countries' ability to acquire critical components for building domestic tech ecosystems.
- The escalating competition has prompted new restrictions for companies and nations engaging in technology trade with China. The White House has warned that countries utilizing Chinese-developed semiconductor technology risk losing access to critical US technological exports. Meanwhile, American firms continue lobbying the administration to maintain access to China's lucrative and expanding technology market.
- As outlined in our escalation ladder framework mentioned in our export controls report, the focus on AI trade restrictions represents an escalation in tensions. We anticipate that these trade measures, currently targeting goods, will expand to the diplomatic sphere as both nations seek to rally third-party countries to their respective positions. While we do not view this technological competition as likely to trigger immediate military conflict, the emerging AI arms race is clearly exacerbating strategic tensions between the two powers.

The Golden Dome: The president's push to develop an advanced missile defense system aims to bolster national security, but risks accelerating a new arms race in space.

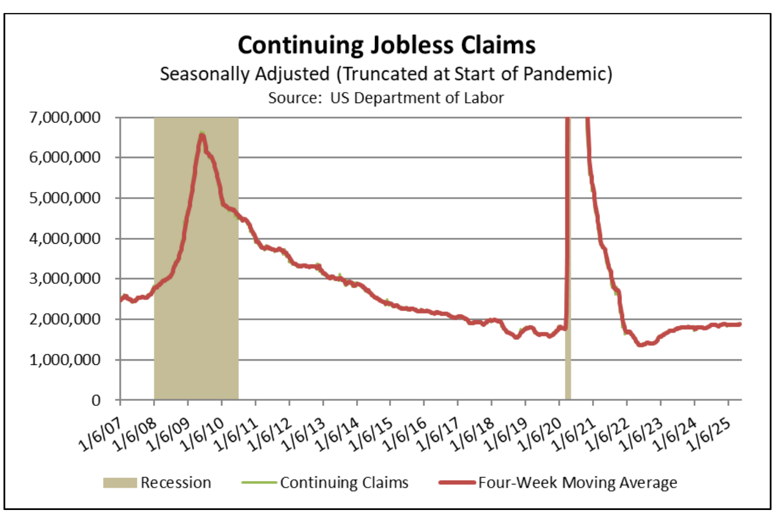
- Earlier this week, the president approved a $175 billion missile defense shield initiative, appointing a Space Force general to oversee its development. The program aims to deploy a constellation of advanced satellites capable of detecting, tracking, and potentially intercepting inbound missiles targeting the United States — a direct response to escalating threats from Russia and China.
- China has condemned the move, warning it could trigger a destabilizing space arms race and further escalate tensions between the two powers. Beijing has called on the US to reconsider the program's development, although it recognizes that Washington is unlikely to alter course. Analysts suggest China's objections may signal its intent to pursue a comparable system, potentially accelerating military competition in orbit.
- The missile shield initiative highlights the return of Cold War-era tensions between global powers. This strategy evokes strong parallels with the Mutually Assured Destruction (MAD) doctrine that dominated geopolitics in the 1980s, when rival nations amassed nuclear arsenals solely to prevent first strikes. Notably, similar defensive systems were considered but ultimately abandoned during that period. We think the situation is a reminder of the rise in global geopolitical tensions.

US Economic Releases

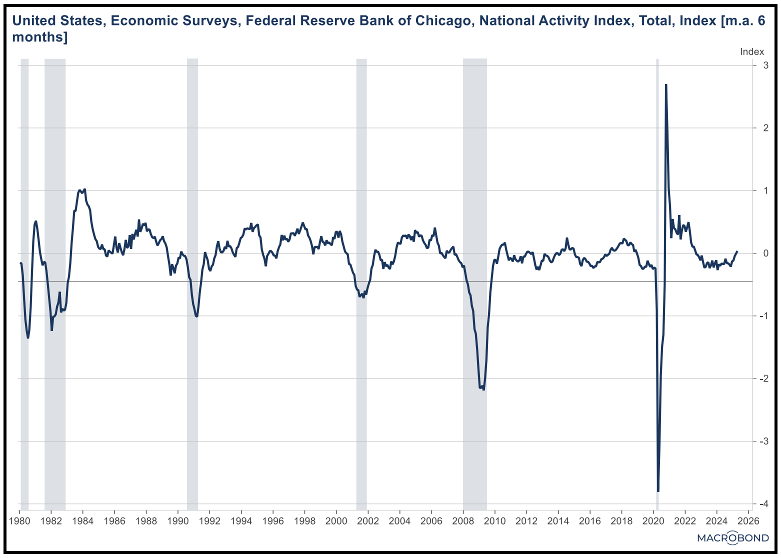
In the week ended May 17, ***initial claims for unemployment benefits*** fell to a seasonally adjusted 227,000, below both the expected level of 230,000 and the previous week's level of 229,000. The four-week moving average of initial claims, which helps smooth out some of the volatility in the series, rose to a still-modest 231,500. The chart below shows how initial jobless claims have fluctuated since just before the Great Financial Crisis. The chart is truncated through much of the pandemic period because of the extremely high level of claims at that time.



In the week ended May 10, the number of ***continuing claims for unemployment benefits*** (people continuing to draw benefits) rose to a seasonally adjusted 1.903 million, above the anticipated reading of 1.882 million and the prior week's revised reading of 1.867 million. The four-week moving average of continuing claims rose to 1,887,500. Excluding the unusual pandemic era, the four-week moving average is now at its highest level since April 2018, suggesting that those employees who do lose their jobs are finding it quite hard to find a new one. The chart below shows how continuing claims have fluctuated since the GFC. It is also truncated during the pandemic period because of the high level of claims at the time.



Separately, the Chicago Fed said its April ***National Activity Index (CFNAI)*** declined to -0.25, matching expectations but falling from 0.03 in March. The CFNAI, which encompasses dozens of separate indicators to capture all aspects of current economic activity, is designed so that readings above 0.00 reflect the economy growing at trend. Our analysis shows that when the six-month moving average of the CFNAI falls below -0.45, it suggests the economy is in recession. With the latest reading, the index suggests the economy is still growing at about its average rate. The chart below shows how the CFNAI has fluctuated over the last several decades.



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**
9:45	S&P Global US Manufacturing PMI	m/m	May P	49.9	50.2	***
9:45	S&P Global US Services PMI	m/m	May P	51	50.8	***
9:45	S&P Global US Composite PMI	m/m	May P	50.3	50.6	***
10:00	Existing Home Sales	m/m	Apr	4.10m	4.02m	***
10:00	Existing Home Sales MoM	m/m	Apr	2.0%	-5.9%	*
11:00	Kansas City Fed Manfacturing Index	m/m	May	-5	-4	*
Federal Reserve						
EST	**Speaker or Event**	**District or Position**				
8:00	Thomas Barkin Participates in Fireside Chat	President of the Federal Reserve Bank of Richmond				
14:00	John Williams Gives Keynote Remarks	President of the Federal Reserve Bank of New York				

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	Core Machine Orders	y/y	Mar	8.4%	1.5%	-1.8%	**	Equity and bond neutral
	Japan Buying Foreign Bonds	q/q	16-May	¥2824.6b	¥1928.7b		***	Equity and bond neutral
	Japan Buying Foreign Stocks	q/q	16-May	-¥226.3b	¥250.8b		***	Equity and bond neutral
	Foreign Buying Japan Bonds	q/q	16-May	-¥241.4b	-¥141.1b		***	Equity and bond neutral
	Foreign Buying Japan Stocks	q/q	16-May	¥714.9b	¥439.0b		***	Equity and bond neutral
	Jibun bank Composite PMI	m/m	May P	49.8	51.2		*	Equity and bond neutral
	Jibun Bank Manufacturing PMI	m/m	May P	49.0	48.7		***	Equity and bond neutral
	Jibun Bank Services PMI	m/m	May P	50.8	52.4		**	Equity and bond neutral
	Machine tool orders	y/y	Apr F	7.7%	7.7%	--	**	Equity and bond neutral
Australia	S&P Global Australia Composite PMI	m/m	May P	50.6	51.0		*	Equity and bond neutral
	S&P Global Australia Manufacturing PMI	m/m	May P	51.7	51.7		***	Equity and bond neutral
	S&P Global Australia Services PMI	m/m	May P	50.5	51.0		*	Equity and bond neutral
India	HSBC India PMI Mfg	m/m	May P	61.2	59.7		***	Equity and bond neutral
	HSBC India PMI Composite	m/m	May P	58.3	58.2		**	Equity and bond neutral
	HSBC India PMI Services	m/m	May P	61.2	58.7		**	Equity and bond neutral
EUROPE								
Eurozone	HCOB Eurozone Manufacturing PMI	m/m	May P	49.4	49.0	49.2	***	Equity and bond neutral
	HCOB Eurozone Services PMI	m/m	May P	48.9	50.1	50.5	**	Equity bearish, bond bullish
	HCOB Eurozone Composite PMI	m/m	May P	49.5	50.4	50.6	*	Equity bearish, bond bullish
Germany	HCOB Germany Manufacturing PMI	m/m	May P	48.8	48.4	48.4	***	Equity and bond neutral
	HCOB Germany Services PMI	m/m	May P	47.2	49.0	49.0	**	Equity bearish, bond bullish
	HCOB Germany Composite PMI	m/m	May P	48.6	50.1	50.1	**	Equity bearish, bond bullish
	IFO Business Climate	m/m	May	87.5	86.9	86.9	***	Equity bearish, bond bullish
	IFO Current Assessment	m/m	May	86.1	86.4	86.4	**	Equity and bond neutral
	IFO Expectations	m/m	May	88.9	87.4	87.4	**	Equity and bond neutral
France	Business Confidence	m/m	May	96	97	97	**	Equity bearish, bond bullish
	Manufacturing Confidence	m/m	May	97	100	99	*	Equity bearish, bond bullish
	HCOB France Manufacturing PMI	m/m	May P	49.5	48.7	48.9	***	Equity bullish, bond bearish
	HCOB France Services PMI	m/m	May P	47.4	47.3	47.7	**	Equity and bond neutral
	HCOB France Composite PMI	m/m	May P	48.0	47.8	48.1	**	Equity and bond neutral
UK	Public Finances (PSNCR)	m/m	Apr	9.1b	2.8b		*	Equity and bond neutral
	Public Sector Net Borrowing	m/m	Apr	20.2b	14.1b	17.9b	*	Equity and bond neutral
	PSNB ex Banking Groups	m/m	Apr	20.2b	14.1b		**	Equity and bond neutral
	S&P Global UK Manufacturing PMI	m/m	May P	45.1	45.4	46.1	***	Equity and bond neutral
	S&P Global UK Services PMI	m/m	May P	50.2	49.0	50.0	**	Equity and bond neutral
	S&P Global UK Composite PMI	m/m	May P	49.4	48.5	49.3	**	Equity and bond neutral
AMERICAS								
Mexico	GDP NSA	y/y	Q1 F	0.8%	0.8%	0.8%	***	Equity and bond neutral
	Economic Activity IGAE	y/y	Mar	2.54%	-0.64%	2.90%	**	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)	423	424	-1	Up
U.S. Sibor/OIS spread (bps)	433	433	0	Up
U.S. Libor/OIS spread (bps)	432	433	-1	Down
10-yr T-note (%)	4.61	4.60	0.01	Up
Euribor/OIS spread (bps)	205	206	-1	Down
Currencies	**Direction**			
Dollar	Up			Down
Euro	Down			Up
Yen	Up			Up
Pound	Down			Up
Franc	Down			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.

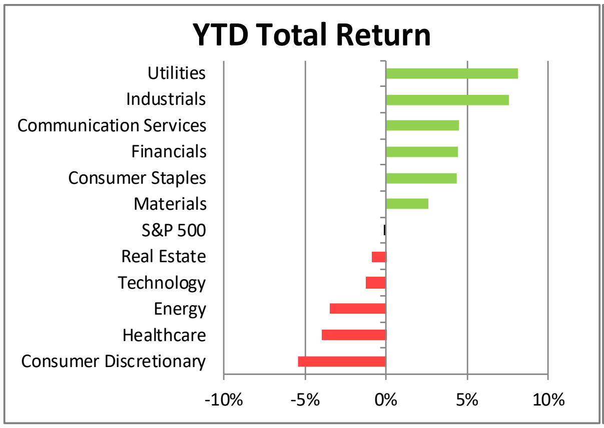
	Price	Prior	Change	Explanation
Energy Markets				
Brent	$63.65	$64.91	-1.94%	
WTI	$60.37	$61.57	-1.95%	
Natural Gas	$3.33	$3.37	-1.04%	
Crack Spread	$26.32	$27.05	-2.71%	
12-mo strip crack	$22.10	$22.84	-3.23%	
Ethanol rack	$1.90	$1.89	0.34%	
Metals				
Gold	$3,297.04	$3,314.96	-0.54%	
Silver	$32.75	$33.39	-1.93%	
Copper contract	$459.55	$467.20	-1.64%	
Grains				
Corn contract	$458.00	$461.00	-0.65%	
Wheat contract	$543.00	$549.25	-1.14%	
Soybeans contract	$1,057.25	$1,062.75	-0.52%	
Shipping				
Baltic Dry Freight	1,337	1,340	-3	
DOE Inventory Report				
	Actual	**Expected**	**Difference**	
Crude (mb)	1.33	-1.10	2.43	
Gasoline (mb)	-1.02	-2.00	0.98	
Distillates (mb)	0.58	-1.40	1.98	
Refinery run rates (%)	0.5%	0.7%	-0.2%	
Natural gas (bcf)		119		

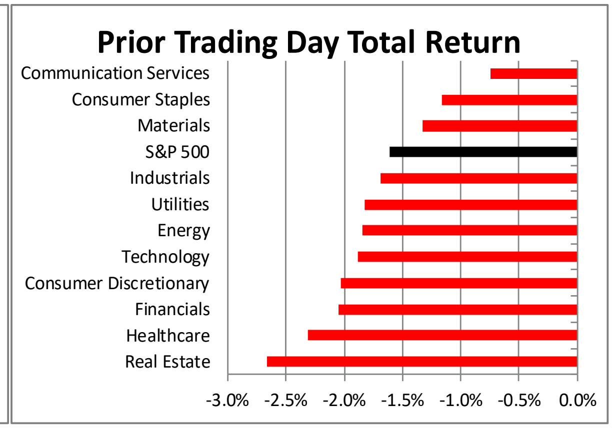
Weather

The 6-to-10 and 8-to-14-day forecasts currently call for warmer-than-normal temperatures in the Far West, the northern Great Plains, and southern Florida, with cooler-than-normal temperatures in the southern Great Plains and the Deep South. The forecasts call for wetter-than-normal conditions in the southern Great Plains and along the Gulf Coast, with dry conditions in the northern Rocky Mountains, the northern Great Plains, and the Midwest.

Data Section

US Equity Markets – (as of 5/21/2025 close)

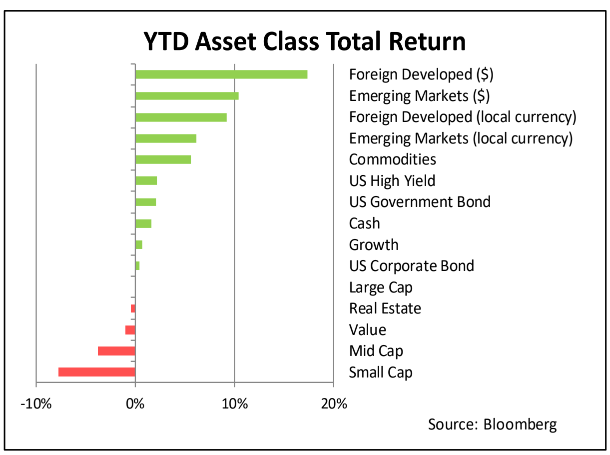




(Source: Bloomberg)

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 5/21/2025 close)

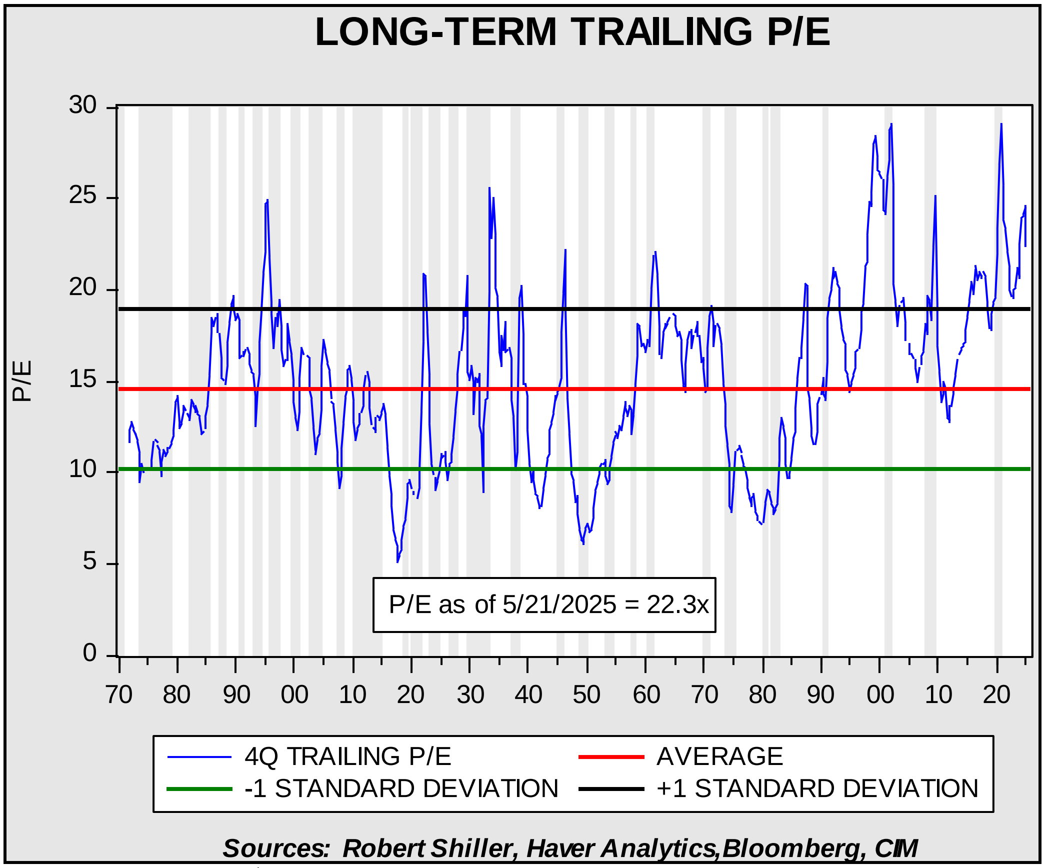


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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 22, 2025



Based on our methodology,[1] the current P/E is 22.3x, up 0.3 from our last report. The rise in the stock price index outweighed the increase in earnings.

[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.