



Daily Comment

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and Thomas Wash

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: October 3, 2023—9:30 AM EDT] Global equity markets are lower this morning. In Europe, the Euro Stoxx 50 is down 0.7% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed down 1.5%. Chinese markets are closed for Golden Week. U.S. equity index futures are signaling a lower open.

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**](#) (10/2/2023) (with associated [podcast](#)): “The Oil Weapon Returns”
- [**Weekly Energy Update**](#) (9/28/2023): Crude oil prices continue to rise as inventories decline. In the latest reporting week, crude oil stockpiles fell despite falling refining activity. We also discuss Europe’s rapid moves to prevent Chinese EVs from swamping their automobile markets.
- [**Asset Allocation Quarterly – Q3 2023**](#) (7/20/2023): Discussion of our asset allocation process, Q3 2023 portfolio changes, and our outlook for the markets.
- [**Asset Allocation Q3 2023 Rebalance Presentation**](#) (8/18/2023): 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**](#) (9/25/2023) (with associated [podcast](#)): “Where’s the Recession? A Recap”
- [**Confluence of Ideas podcast**](#) (8/22/2023): “The Economics of Defense in Great Power Competition”
- [**Business Cycle Report**](#) (9/28/2023)

Our *Comment* today opens with a discussion of the battle brewing over Chinese influence at the International Monetary Fund. We next review a wide range of other international and U.S. developments with the potential to affect the financial markets today, including a further worsening of Indian-Canadian relations and dramatic moves in cryptocurrency prices yesterday related to new exchange-traded funds for the assets.

International Monetary Fund-China: IMF President Kristalina Georgieva [has backed institutional reforms that would eventually give China greater voting power](#), according to an interview in the *Financial Times*. In the interview, Georgieva argued that the IMF needs more

funding to help struggling countries around the world, and that China should have more voting power based on the fact that it now accounts for almost one-fifth of the world's economy but only 6% of the fund's capital.

- Nevertheless, U.S. officials have signaled that they want to increase Western control over the IMF, so they would veto an increase in China's capital.
- Capital adjustments at the IMF require the approval of countries that hold at least 85% of the institution's capital. The U.S. holds 17% of the capital, the largest shareholder, so it could unilaterally veto any effort to increase China's position in the fund.

China-Peru-United States: Despite the U.S.'s ability to block increased Chinese diplomatic influence at the IMF, it is still struggling to counter China's growing economic influence in less developed countries. According to new reports, the U.S. [has privately warned Peru that Chinese interests are gaining too much control over that country's key infrastructure](#), including the electric utility serving the capital city of Lima and a new deep-water port on the country's Pacific coast. Control of those assets by Chinese state-owned or state-influenced companies could give Beijing leverage over Peru as it seeks to gain better access to key resources and undermine the U.S.'s geopolitical and economic positions.

India-Canada: New Delhi [has ordered Canada to withdraw about 40 of its diplomats](#) based in India, ostensibly to equalize the number of diplomats each country has in the other. However, the move is widely seen as further retaliation for Ottawa's accusation that Indian agents killed a Sikh separatist and Canadian citizen in British Columbia last June. The Indian government has also imposed a ban on new visas for Canadians wishing to visit India.

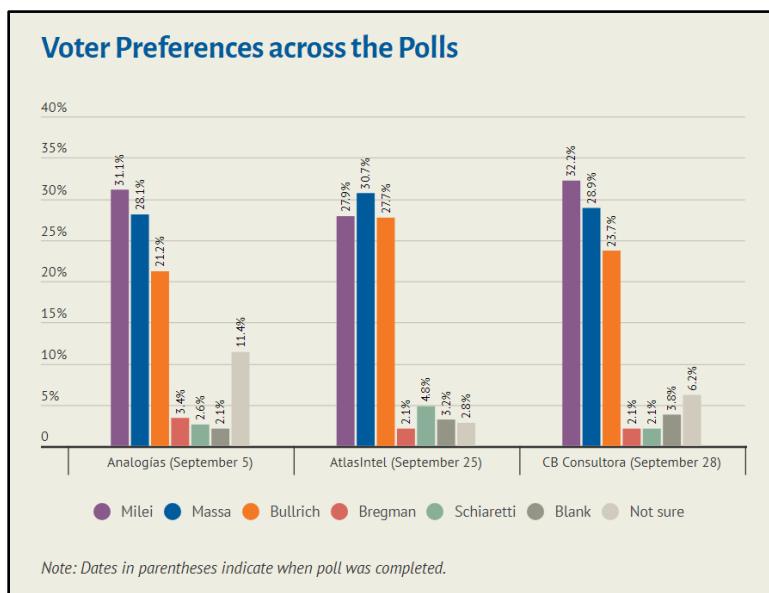
- The worsening bilateral tensions have weakened Canadian Prime Minister Trudeau's domestic political position, especially as some have accused him of pandering to Canada's sizable Sikh community.
- The tensions could also complicate the West's efforts to enlist Indian support to counter China's growing geopolitical power and aggressiveness.
 - Despite that concern, authorities in New Delhi [this morning raided the homes of journalists, contributors, and staff of the website NewsClick](#), alleging that the news outlet is a Chinese propaganda organ.
 - The move follows several other measures that New Delhi has taken against Chinese influence in India as relations worsened in recent years.

European Union: Average home prices rose by a seasonally adjusted 0.3% in the second quarter, partially reversing the declines in each of the previous two periods. Nevertheless, second-quarter home prices in the broader EU [were down 1.1% from the same period one year earlier, and prices in the eurozone were down 1.7%](#). That marks the first annual home-price declines in Europe since 2014.

- The fall in home values largely reflects the European Central Bank's long campaign of interest-rate hikes to combat high consumer price inflation, but it also shows economic headwinds for particular regions and sectors, such as German manufacturing.

- German home prices had the worst annual declines, down 9.9%, while prices in Denmark were down 7.6%, and prices in Sweden were down 6.8%.
- In contrast, prices were up 13.7% in Croatia and 10.7% in Bulgaria.

Argentina: In an effort to derail the presidential ambitions of radical libertarian Javier Milei, who is currently first in the opinion polls ahead of the October 22 election, Economy Minister Sergio Massa [has pledged to form a unity government if he wins the balloting](#). However, vowing to form a government that would include Milei's libertarians and Patricia Bullrich's traditional center-right parties may alienate Massa's own left-wing populist Peronists. As of now, Milei remains in the electoral driver's seat, raising the chance that he will come to power and try to implement his agenda of steep government spending cuts, deregulation, and dollarization of the economy.



U.S. Politics: Last night, Florida Republican Rep. Matt Goetz [announced a motion to oust House Speaker McCarthy over his weekend deal with the Democrats for a short-term funding bill for the government](#). The motion launches a process that will require a vote by Wednesday evening. With the Republicans having only 221 seats, while the Democrats have 212, it would appear at first glance that only a few Republican rebels could leave McCarthy at peril, especially if all the Democrats voted against him, as they traditionally would. In this case, however, the prospect of a hard-right Speaker [could encourage the cooperation of at least some Democrats to save McCarthy's skin](#), especially if they could wring concessions out of McCarthy to do so.

U.S. Cryptocurrency Markets: Bitcoin, Ethereum, Litecoin, and other cryptocurrency prices [jumped yesterday as Grayscale Investments filed paperwork to convert its \\$5-billion Bitcoin futures ETF](#) to a fund that could invest in the spot cryptocurrency. Also yesterday, the first seven exchange-traded funds for Ethereum futures were launched. However, prices for the various cryptocurrencies gave up most or all of their gains by the end of the day as the new

Ethereum futures ETF garnered little investor interest. Market data suggest turnover for the new ETFs totaled only about \$7 million.

- Tepid demand for the Ethereum futures ETFs may show that individual investors are less interested in cryptocurrencies than previously thought. However, some observers suggest that investors simply prefer funds that invest in spot cryptocurrencies. Of course, today's high interest rates on money market funds have probably also sapped demand for cryptocurrencies.
- The Securities and Exchange Commission has signaled it may approve spot Bitcoin and Ethereum ETFs in the coming months.

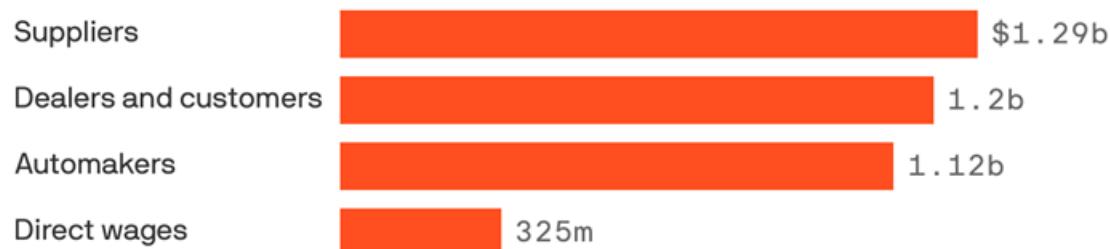
U.S. Commercial Real Estate Market: New data suggests companies have had some success forcing their employees back into the office after the pandemic era's work-from-home policies, but that [has only been enough to push office occupancy up to about 50.4% of 2019 levels](#).

Moreover, occupancy is now highly skewed to Tuesday through Thursday, with offices only about 30% occupied on Mondays and Fridays. Separate data shows the overall office vacancy rate in the third quarter rose to 19.2%, just short of the record rate of 19.2% in 1991.

U.S. Auto Strike: As the United Auto Workers' strike against the top U.S. automakers continues, new research [shows how the economic cost is broadening out to suppliers, dealers, and to the workers themselves](#). According to the Anderson Economic Group, suppliers to the manufacturers under strike lost \$1.3 billion in the first two weeks of the strike, while the manufacturers themselves lost \$1.1 billion and auto workers have lost \$325 million. In related news, Ford (F, \$12.31) and General Motors (GM, \$32.47) [said they have laid off an additional 500 workers at plants not under strike but that were affected by the work stoppages](#), bringing the total of workers laid off as a consequence of the strike to about 6,000.

Estimated losses during the first two weeks of the UAW strike

From Sept. 15-29, 2023



Data: Anderson Economic Group; Chart: Axios Visuals

U.S. Economic Releases

There were no economic releases prior to the publication of this report. 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	JOLTS Job Openings	m/m	Aug	8815k	8827k	**
	Wards Total Vehicle Sales	m/m	Sep	15.40m	15.04m	*
Federal Reserve						
No Fed speakers or events for the rest of today						

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	Monetary Base	y/y	Sep	5.6%	1.2%	1.6%	**	Equity bullish, bond bearish
	Monetary Base, End of Period	m/m	Sep	¥672.6t	¥674.4t		*	Equity and bond neutral
Australia	Building Approvals	m/m	Aug	7.0%	-8.1%	-7.4%	***	Equity bullish, bond bearish
New Zealand	CoreLogic House Prices	y/y	Sep	-7.3%	-8.7%		*	Equity bullish, bond bearish
India	S&P Global India Manufacturing PMI	m/m	Sep	57.5	58.6		***	Equity bearish, bond bullish
EUROPE								
Switzerland	CPI	y/y	Sep	1.7%	1.6%	1.8%	***	Equity and bond neutral
	Core CPI	y/y	Sep	1.3%	1.5%	1.5%	*	Equity and bond neutral
AMERICAS								
Canada	S&P Global Canada Manufacturing PMI	m/m	Sep	47.5	48.0		***	Equity and bond neutral
Mexico	Gross Fixed Investment	y/y	Jul	29.1%	28.8%	29.4%	**	Equity and bond neutral
Brazil	S&P Global Brazil Manufacturing PMI	m/m	Sep	49.0	50.1		***	Equity and bond neutral
	Trade Balance	m/m	Sep	\$8904m	\$9767m	\$9545m	**	Equity and bond neutral
	Exports	m/m	Sep	\$28431m	\$31211m	\$30994m	*	Equity and bond neutral
	Imports	m/m	Sep	\$19527m	\$21444m	\$21449m	*	Equity and bond neutral
	Formal Job Creation	m/m	Aug	220844	142702	143004	**	Equity and bond neutral
	Industrial Production	y/y	Aug	0.5%	-1.1%	1.0%	***	Equity bearish, bond bullish

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)	566	566	0	Up
3-mo T-bill yield (bps)	531	531	0	Up
TED spread (bps)	LIBOR and the TED Spread have been discontinued.			
U.S. Sibor/OIS spread (bps)	541	541	0	Up
U.S. Libor/OIS spread (bps)	543	543	0	Up
10-yr T-note (%)	4.74	4.68	0.06	Flat
Euribor/OIS spread (bps)	395	395	0	Up
Currencies	Direction			
Dollar	Up			Up
Euro	Flat			Down
Yen	Flat			Down
Pound	Down			Down
Franc	Down			Down
Central Bank Action	Current	Prior	Expected	
RBA Cash Rate Target	4.100%	4.100%	4.100%	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	\$90.14	\$90.71	-0.63%	
WTI	\$88.39	\$88.82	-0.48%	
Natural Gas	\$2.85	\$2.84	0.25%	
Crack Spread	\$22.64	\$24.02	-5.74%	
12-mo strip crack	\$24.31	\$25.12	-3.22%	
Ethanol rack	\$2.49	\$2.49	0.07%	
Metals				
Gold	\$1,825.74	\$1,828.03	-0.13%	
Silver	\$21.02	\$21.05	-0.11%	
Copper contract	\$362.30	\$364.15	-0.51%	
Grains				
Corn contract	\$486.75	\$488.75	-0.41%	
Wheat contract	\$566.25	\$564.75	0.27%	
Soybeans contract	\$1,264.25	\$1,277.00	-1.00%	
Shipping				
Baltic Dry Freight	1,737	1,701	36	
DOE Inventory Report				
	Actual	Expected	Difference	
Crude (mb)		-0.5		
Gasoline (mb)		-1.0		
Distillates (mb)		-1.3		
Refinery run rates (%)		-0.5%		
Natural gas (bcf)		98		

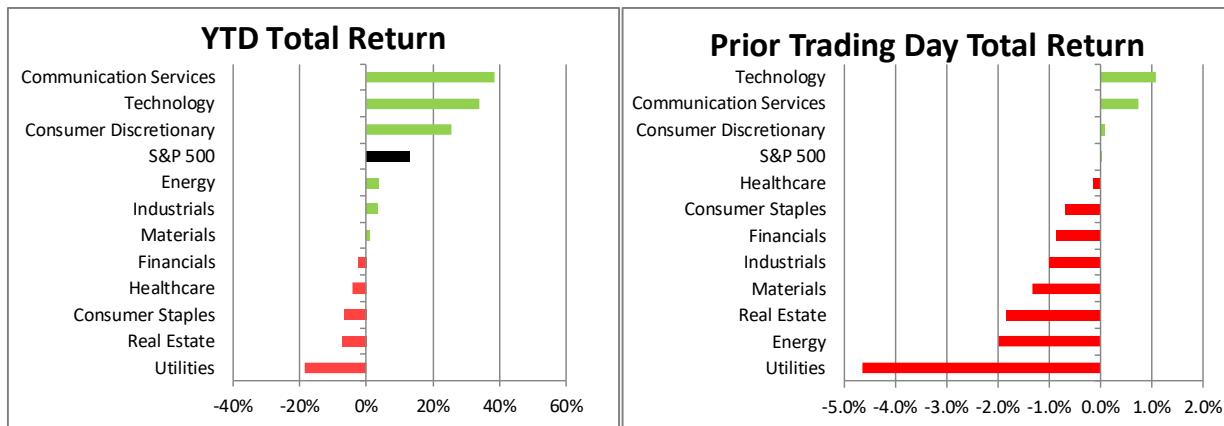
Weather

The 6-10 and 8-14 day forecasts currently call for warmer-than-normal temperatures to spread from the Rocky Mountains and Great Plains toward the Midwest, with cooler-than-normal temperatures expected for the rest of the country. The precipitation outlook calls for wetter-than-normal conditions in the Pacific Northwest and Southeast, with dry conditions in the Midwest, Northeast, and Great Plains.

There is only one atmospheric disturbance active in the Atlantic Ocean. Tropical Storm Philippe is in the central Atlantic and is expected to move across Antigua and Barbuda later today. On average, Atlantic hurricane activity peaks on September 15.

Data Section

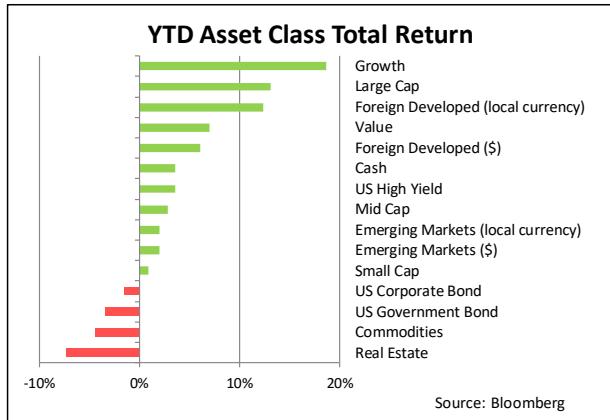
U.S. Equity Markets – (as of 10/2/2023 close)



(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 10/2/2023 close)

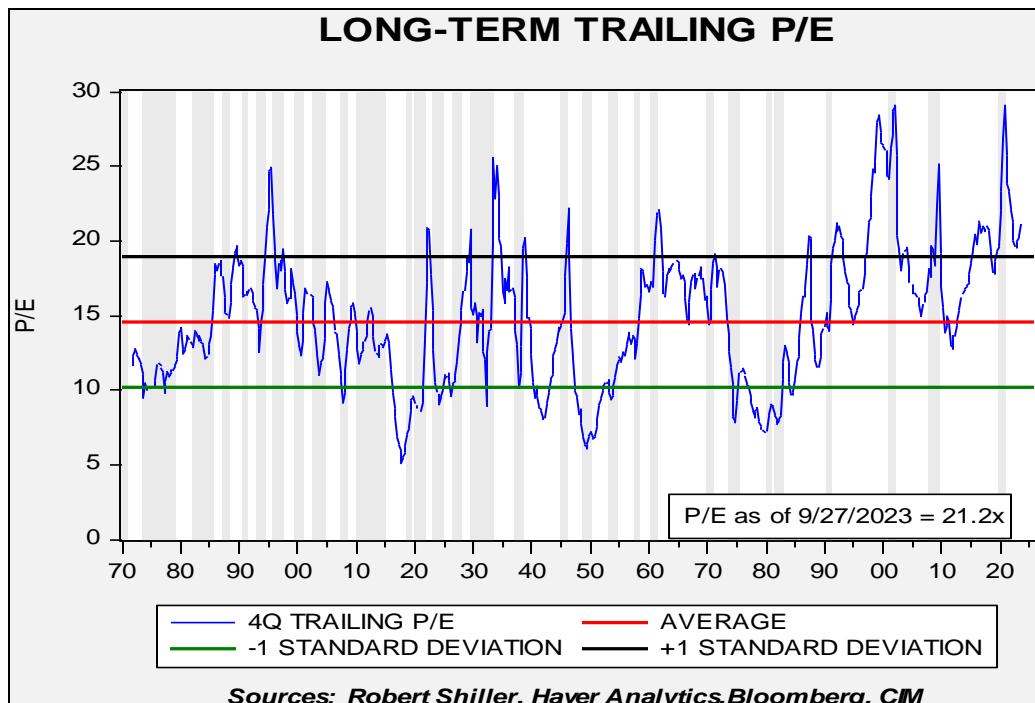


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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

September 28, 2023



Based on our methodology,¹ the current P/E is 21.2x, up 0.1x from last week. Weaker earnings estimates led to the rise in the 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.

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 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.