Daily Comment

Confluence INVESTMENT MANAGEMENT

By Patrick Fearon-Hernandez, CFA, and Thomas Wash

Posted: September 2, 2025 — 9:30 AM ET] Global equity markets are lower this morning. In Europe, the Euro Stoxx 50 is down 0.8% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed down 0.2%. Chinese markets were lower, with the Shanghai Composite down 0.5% from its previous close and the Shenzhen Composite down 2.0%. US 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 in bold.

Bi-Weekly Geopolitical Report	Asset Allocation Bi-Weekly	Asset Allocation Quarterly	Of Note
"Tariff Trilemma: The Three Rs Driving US Trade Policy" (8/25/25) + **podcast**	"Navigating the Waves of BLS Revisions" (8/18/25) + podcast	Q3 2025 Report Q3 2025 Rebalance Presentation	The Confluence Mailbag Podcast Business Cycle Report

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

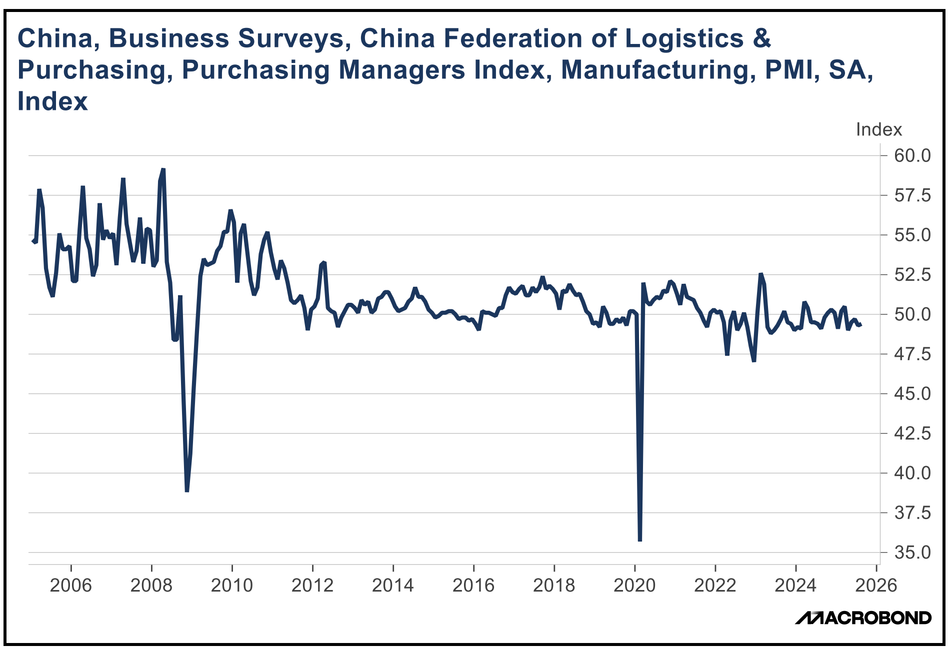
Our *Comment* today opens with some notes on the big Shanghai Cooperation Organization summit in Tianjin, China. We next review several other international and US developments with the potential to affect the financial markets today, including a sharp sell-off in British government bonds and the pound today and a few words on the Friday decision by a US appeals court to invalidate most of the administration's new "reciprocal" tariffs.

China-Shanghai Cooperation Organization: General Secretary Xi welcomed the leaders of about 20 nations for an SCO summit in China on Sunday, including Russian President Putin, Iranian President Pezeshkian, and Indian Prime Minister Modi. To many analysts, Modi's decision to attend the Beijing-led political and security grouping is a worrying sign that India has now at least partially shifted its allegiance to China and away from the US.

- If New Delhi continues to realign with Beijing, it would potentially dash years of hopes in the West that India would be a bulwark against China's growing geopolitical and economic power.
- As a reminder, membership in the SCO is one of the factors we use to assign countries into the world's new geopolitical blocs. It's also one reason why our methodology currently assigns India to the "Leaning China" bloc. Some observers have questioned that assignment, but it's consistent with New Delhi's quick pivot toward Beijing this spring.

China-Russia: Also at the SCO summit, the Kremlin said China and Russia have now finally agreed to jointly build the Power of Siberia 2 natural gas pipeline, an enormous new conduit between the countries. Once completed in the 2030s, the new pipeline would allow Russia to shift its gas exports away from Europe in favor of markets in China, which, in turn, would allow China to cut its imports of expensive LNG. However, it appears that commercial terms are still being negotiated, including pricing issues that have long been a stumbling block for Beijing.

China: The official purchasing managers' index for manufacturing rose to a seasonally adjusted 49.4 in August, while the private-sector Caixin PMI for manufacturing jumped to 50.5. For a true gauge of what's happening in the Chinese factory sector, analysts sometimes average the two, and using that method, the reading rose from 49.4 to 49.9. That still leaves the reading below the 50 level that indicates growth, but it does suggest that Chinese manufacturing is now basically just stagnant rather than falling, at least in part because of the government's stimulus measures.

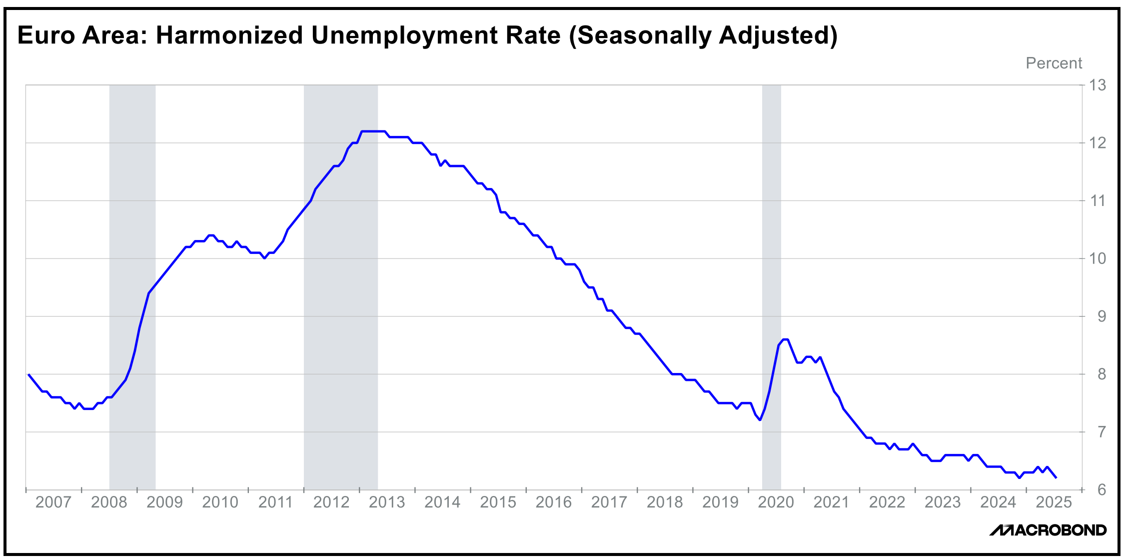


Japan: Despite Tokyo's recent decision to double its defense spending and rearm to meet the growing geopolitical threat from China, new reports say it only managed to recruit half the 20,000 fresh troops it planned to hire in 2023. As with many nations in the US geopolitical bloc, military recruiting in Japan is facing challenges such as the country's poor population growth, tight labor market, low military pay, and the perception of military service as dangerous.

- Those factors will likely make it hard for Japan to respond to US pressure for a more robust military effort.
- In turn, that could mean Japan will be more vulnerable to US moves to punish it for not rearming more aggressively.

Indonesia: The country's wave of protests against corruption and lawmaker perks intensified over the weekend with looting, arson and deadly violence in multiple cities. The unrest became so bad that President Subianto was forced into an embarrassing cancelation of his trip to the SCO summit in China. He also was forced to strike a deal with several political parties to cut housing allowances and suspend overseas work trips for members of parliament. Those moves have helped calm the situation, but economically disruptive protests could still reignite.

Eurozone: In a report yesterday, the region's July unemployment rate fell to a seasonally adjusted 6.2%, down from 6.3% in June and marking a new record low. The decline was especially impressive given the eurozone's recent spate of weak economic growth. The drop in joblessness is expected to discourage the European Central Bank from a further interest-rate cut at its next policy meeting next week.



United Kingdom: In a potential sign of capital flight sparked by slow economic growth and rising public debt, 30-year gilt yields today spiked to 5.72%, reaching their highest level since 1998. Meanwhile, the pound depreciated 1.4% against the dollar, ending at $1.3352. The jump in government borrowing costs will likely put even more pressure on Prime Minister Starmer's Labour Party government to come up with difficult tax hikes and/or spending cuts, which could further weigh on the economy and UK assets.

Russia-Ukraine War: In a previously unreported development that heralds a new era in warfare, Ukraine has been using drone swarm technology in its defense against Russia's invasion over the last year. The technology involves loading multiple drones with artificial intelligence so they can operate, communicate, coordinate among themselves, and attack Russian positions or carry out other tasks autonomously, reducing the number of Ukrainian soldiers needed for the task. The technology is now expected to become a big part of the global defense industry.

United States-China: In the latest example of a high-profile scientist leaving the US to return to China, epidemiologist and human microbiome scientist Wang Leyao has left her positions at the University of Massachusetts at Amherst and the National Institutes of Health to join the Shenzhen Medical Academy of Research and Translation (Smart) as a senior research fellow in its Institute of Human Immunology. As we've noted before, the string of top scientists returning home could help China overtake or expand its lead over the US in key industries.

US Tariff Policy: A federal appeals court late Friday ruled that the White House's "reciprocal" and fentanyl tariffs against China, Mexico, and Canada are illegal, upholding a lower court's decision to block them. However, the court let the tariffs remain in place until October 14 to facilitate a likely administration appeal to the Supreme Court. So far, the decision doesn't seem to be having much impact on the global financial markets, perhaps reflecting uncertainty that the Supreme Court will invalidate the tariffs.

US "Recession": As economists and market strategists, we're always on the lookout for a shift in the business cycle, so we were struck by new research from data analysis group IFS claiming the US is already in recession. However, on closer inspection, it turned out that the report, titled "The Sex Recession," focuses on survey results showing a big drop in the number of Americans having, er, intimate relations. It's not clear if this type of recession will affect the stock market, but the researchers note that it points to a further fall in the US birth rate and population growth.

US Economic Releases

There were no economic releases prior to the publication of this report. The table below lists the economic releases and 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	Aug F	53.3	53.3	***
10:00	ISM Manufacturing	m/m	Aug	49.0	48.0	**
10:00	ISM Prices Paid	m/m	Aug	65.0	64.8	**
10:00	ISM New Orders	m/m	Aug	48.0	47.1	**
10:00	ISM Employment	m/m	Aug	45.0	43.4	*
10:00	Construction Spending	m/m	Jul	-1.0%	-0.4%	**
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	Capital Spending	y/y	2Q	7.6%	6.4%	6.1%	**	Equity bullish, bond bearish
	S&P Global Japan Manufacturing PMI	m/m	Aug F	49.7	49.9		***	Equity and bond neutral
	Monetary Base	y/y	Aug	-4.1%	-3.9%		**	Equity and bond neutral
Australia	S&P Global Australia Manufacturing PMI	m/m	Aug F	53.0	52.9		***	Equity and bond neutral
	Melbourne Institute Inflation	y/y	Aug	2.8%	2.9%		***	Equity and bond neutral
	ANZ-Indeed Job Advertisements	m/m	Aug	0.1	-0.6		*	Equity and bond neutral
	Building Approvals	m/m	Jul	-8.2%	12.2%	-5.0%	***	Equity bearish, bond bullish
	BoP Current Account Balance	q/q	2Q	-A$13.7b	-A$14.1b	-A$16.0b	***	Equity and bond neutral
New Zealand	Building Permits	m/m	Jul	5.4%	-6.0%		**	Equity and bond neutral
	Terms of Trade Index	q/q	2Q	4.1%	1.9%	1.9%	*	Equity bullish, bond bearish
South Korea	Exports	y/y	Aug	1.3%	5.8%	2.3%	***	Equity and bond neutral
	Trade Balance	m/m	Aug	$6514m	$6610m	$5999m	*	Equity and bond neutral
	Imports	y/y	Aug	-4.0%	0.7%	-2.5%	**	Equity bearish, bond bullish
	S&P Global South Korea PMI Manufacturing	m/m	Aug	48.3	48.0		***	Equity and bond neutral
	CPI	m/m	Aug	1.7%	2.1%	1.9%	***	Equity and bond neutral
China	Official Manufacturing PMI	m/m	Aug	49.4	49.3	49.5	***	Equity and bond neutral
	Official Services PMI	m/m	Aug	50.3	50.1	50.2	**	Equity and bond neutral
	Official Composite PMI	m/m	Aug	50.5	50.2		*	Equity and bond neutral
	RatingDog China PMI Mfg	m/m	Aug	50.5	49.5	49.8	***	Equity bullish, bond bearish
India	GDP	y/y	2Q	7.8%	7.4%	6.7%	*	Equity bullish, bond bearish
EUROPE								
Eurozone	HCOB Eurozone Manufacturing PMI	m/m	Aug F	50.7	50.5	50.5	***	Equity and bond neutral
	Unemployment Rate	m/m	Jul	6.2%	6.2%	6.2%	**	Equity and bond neutral
	CPI	y/y	Aug P	2.1%	2.0%	2.1%	***	Equity and bond neutral
	Core CPI	y/y	Aug P	2.3%	2.3%	2.2%	**	Equity and bond neutral
Germany	HCOB Germany Manufacturing PMI	m/m	Aug F	49.8	49.9	49.9	***	Equity and bond neutral
France	HCOB France Manufacturing PMI	m/m	Aug F	50.4	49.9	49.9	***	Equity and bond neutral
	Budget Balance YTD	y/y	Jul	-142.0b	-100.4b		*	Equity and bond neutral
Italy	HCOB Italy Manufacturing PMI	m/m	Aug	50.4	49.8	49.8	***	Equity and bond neutral
	Unemployment Rate	m/m	Jul	6.0%	6.2%		**	Equity and bond neutral
	New Car Registrations	y/y	Aug	-2.7%	-5.1%		*	Equity and bond neutral
	Budget Balance	m/m	Aug	-0.1	14.2b		*	Equity and bond neutral
	PPI	y/y	Jul	2.4%	3.9%		**	Equity and bond neutral
UK	Nationwide House Price Index	y/y	Aug	2.1%	2.4%	2.7%	***	Equity bearish, bond bullish
	Net Lending Sec. on Dwellings	m/m	Jul	4.5b	5.4b	3.5b	*	Equity and bond neutral
	Mortgage Approvals	m/m	Jul	65.4k	64.6k	64.2k	***	Equity and bond neutral
	M4 Money Supply	y/y	Jul	2.9%	3.3%		*	Equity and bond neutral
	S&P Global UK Manufacturing PMI	m/m	Aug F	47.0	47.3	47.3	***	Equity and bond neutral
Switzerland	Real Retail Sales	y/y	Jul	0.7%	3.9%		**	Equity and bond neutral
	PMI Manufacturing	m/m	Aug	49.0	48.8	47.0	***	Equity and bond neutral
	PMI Services	m/m	Aug	43.9	41.8		***	Equity and bond neutral
	Domestic Sight Deposits CHF	w/w	29-Aug	447.7b	442.5b	--	*	Equity and bond neutral
	Total Sight Deposits CHF	w/w	29-Aug	472.3b	469.5b	--	*	Equity and bond neutral
Russia	S&P Global Russia Manufacturing PMI	m/m	Aug	48.7	47.0	47.3	***	Equity and bond neutral
AMERICAS								
Canada	GDP	y/y	Jun	9.0%	1.2%	1.3%	**	Equity and bond neutral
Mexico	S&P Global Mexico Manufacturing PMI	m/m	Aug	50.2	49.1		***	Equity and bond neutral
	IMEF Manufacturing Index SA	m/m	Aug	45.6	45.3		*	Equity and bond neutral
	IMEF Non-Manufacturing Index SA	m/m	Aug	49.9	49.3		*	Equity and bond neutral
Brazil	S&P Global Brazil Manufacturing PMI	m/m	Aug	47.7	48.2		***	Equity and bond neutral
	GDP	y/y	2Q	2.2%	2.9%	2.2%	***	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)	405	405	0	Down
U.S. Sibor/OIS spread (bps)	416	416	0	Down
U.S. Libor/OIS spread (bps)	411	412	-1	Down
10-yr T-note (%)	4.28	4.23	0.05	Up
Euribor/OIS spread (bps)	207	206	1	Up
Currencies	**Direction**			
Dollar	Up			Down
Euro	Down			Up
Yen	Up			Down
Pound	Down			Down
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	$69.22	$68.15	1.57%	
WTI	$65.73	$64.01	2.69%	
Natural Gas	$2.94	$3.00	-1.90%	
Crack Spread	$24.00	$23.58	1.76%	
12-mo strip crack	$23.87	$23.51	1.53%	
Ethanol rack	$2.15	$2.15	0.00%	
Metals				
Gold	$3,489.29	$3,476.07	0.38%	
Silver	$40.61	$40.70	-0.21%	
Copper contract	$457.35	$459.05	-0.37%	
Grains				
Corn contract	$418.75	$420.25	-0.36%	
Wheat contract	$526.50	$534.25	-1.45%	
Soybeans contract	$1,044.25	$1,054.50	-0.97%	
Shipping				
Baltic Dry Freight	2,024	2,025	-1	

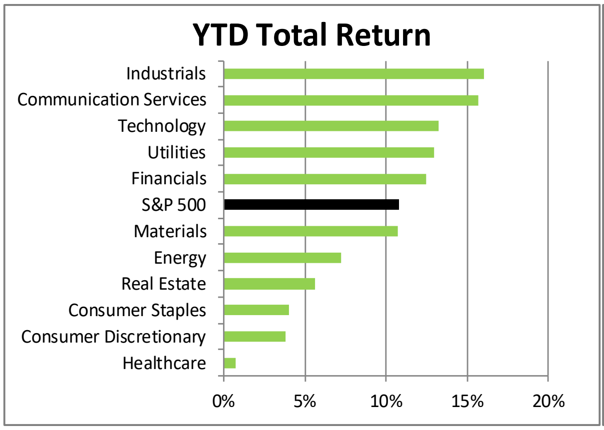
Weather

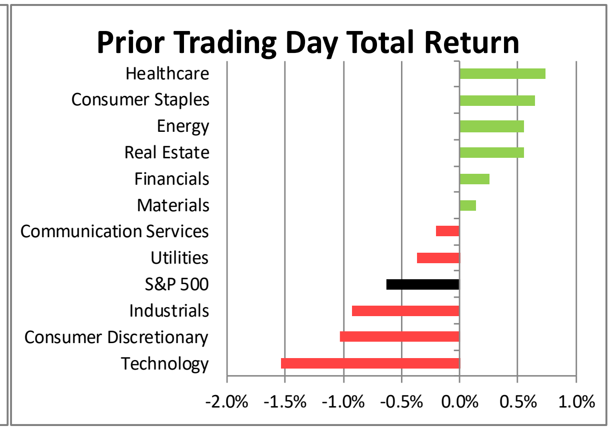
The 6-to-10-day and 8-to-14-day forecasts currently call for warmer-than-normal temperatures in most of the country, with cooler temperatures in the New England, Mid-Atlantic and Pacific regions. The forecasts call for wetter-than-normal conditions in the Far West, Great Plains and on the Eastern Seaboard, with dry conditions in the New England and Great Lakes regions.

There is now only one tropical disturbance in the Atlantic Ocean area. It is currently sitting off the western coast of Africa and is assessed to have a 70% chance of cycle formation in the next seven days.

Data Section

US Equity Markets – (as of 8/29/2025 close)

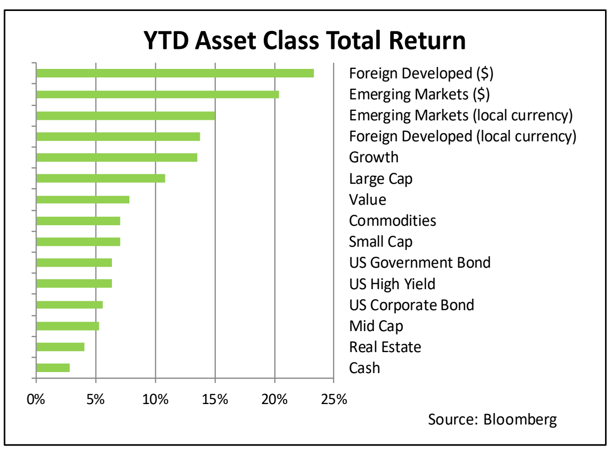




(Source: Bloomberg)

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 8/29/2025 close)

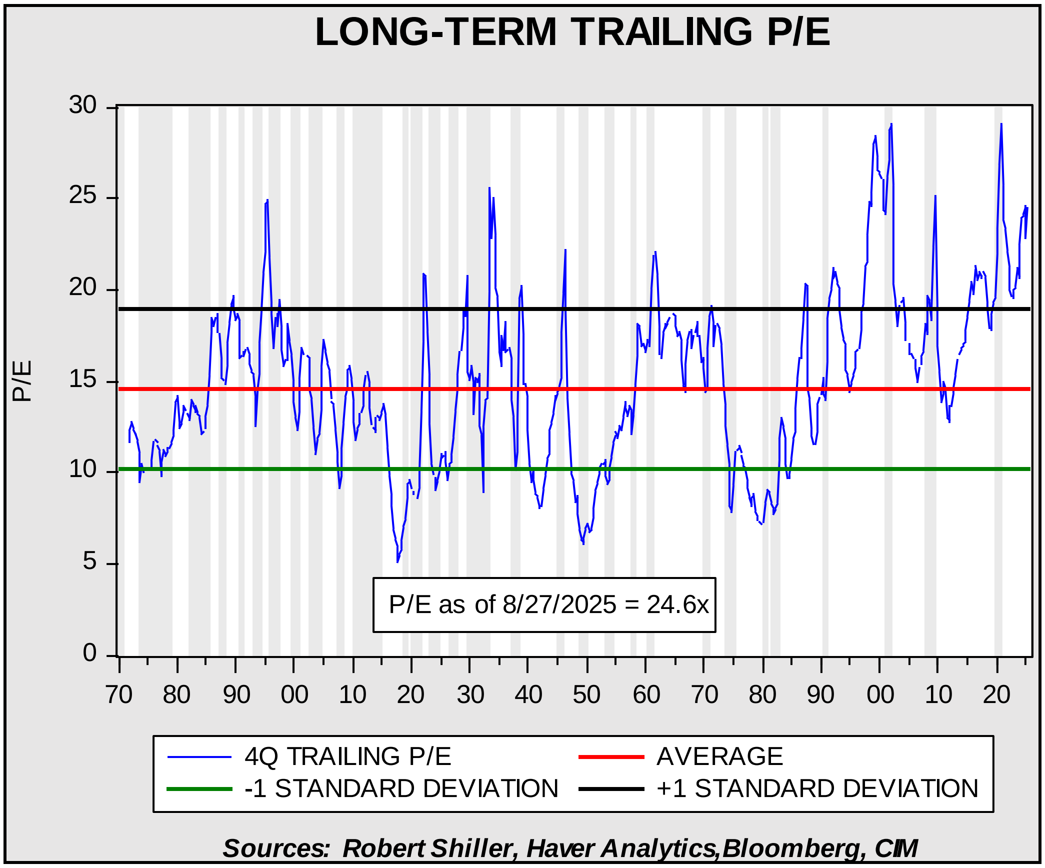


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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

August 28, 2025



Based on our methodology,[1] the current P/E is 24.6x, which is up from 0.1 from the previous report. The increase was driven by a rise in the stock price index outpacing 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 (Q1, Q3, Q4) and one estimate (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.