

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: September 14, 2021—9:30 AM EDT] Global equity markets are generally lower this morning. In Europe, the EuroStoxx 50 is currently down 0.1% from its prior close. In Asia, the MSCI Asia Apex 50 closed down 0.4%. Chinese markets were lower, with the Shanghai Composite down 1.4% from its prior close and the Shenzhen Composite down 0.5%. U.S. equity index futures are signaling a higher 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:

- **[Weekly Geopolitical Report \(9/13/2021\): “Afghanistan, Part I: History”](#)**
- [Weekly Energy Update \(9/10/2021\)](#): Ida caused a sharp decline in refinery operations, China is releasing strategic reserve oil to lower prices, and natural gas prices are on a tear.
- [Asset Allocation Q3 2021 Rebalance Presentation \(8/26/2021\)](#): A video discussion of our asset allocation process, portfolio changes in Q3, and the macro environment
- [Asset Allocation Weekly \(9/10/2021\)](#) (with associated [podcast](#)): we discuss the likelihood of Fed Chair Powell’s renomination, the opposition in Congress, and what that opposition could mean for Fed independence
- [Confluence of Ideas podcast \(7/7/2021\)](#): “The Geopolitics of Taiwan and the Issue of Globalization”

Good morning and happy CPI day! We cover the data below, but the quick read is that [prices rose less than expected](#), lifting equity futures, [which were leaning higher before the report](#). [Tropical Storm Nicholas has hit the Texas coast](#), dumping prodigious amounts of rain. The storm track is taking it toward Louisiana. Our coverage begins with the New York Fed’s inflation survey, followed by an update on the uranium market and Facebook (FB, USD, 376.51). Our regular coverage begins with China news. Bond market jitters continue. The international roundup is next; the center-left wins in Norway. We close with pandemic coverage.

NY Fed and Inflation: The New York FRB conducts a survey of consumer behavior and outlooks, and its [recent polling on inflation expectations is sobering](#). The overall inflation expectation for one year out is 5.2%; the three-year rate is 4.0%. Older Americans (over 60) are most concerned, forecasting a 6.0% rate over the next 12 months. But even the under 40 bracket is looking for 4.5%. Check out the above link for the breakdown by education, age, and region.

The bottom line for the Fed is that inflation expectations are rising, and the central bank's only real tool to address it is to weaken aggregate demand, which we doubt it will do.

Uranium on a tear: We have been friendly to uranium on the idea that, eventually, it will become obvious that you can't achieve a carbon-free energy sector without nuclear power. That doesn't mean nuclear power isn't without its externalities, but so does every other power source. The uranium market isn't huge. Much of the production and consumption is tied to long-term contracts, meaning the spot market is even smaller than it looks. In such situations, a small amount of buying can lead to price spikes. Investor interest appears to be high, and that has sent prices up sharply. We don't know how long it will last, but over the long run, we suspect prices will remain higher than seen in recent years.

Facebook (FB, USD, 376.51): In the spirit of *Animal Farm*, it turns out that all animals are equal, but some are more equal than others. A [WSJ report](#) reveals that the social media company does not screen all Facebook users the same.

China: Evergrande (EGRNF, USD, 0.46) remains in the news.

- The steady drip of [bad news from the property developer Evergrande](#) is [now starting to become a broader problem](#). Until around 2015, China essentially prevented defaults. Investors tended to assume they wouldn't occur and, thus, take excessive risk. But the Xi regime has changed the rules of the market, and the [Evergrande situation could prove to be a serious test](#). We are seeing [evidence of protests against the company](#), with [investors demanding their money](#) back, employees demanding their pay, and homeowners demanding their homes get built. The company is [cautiously starting to outline a restructuring plan](#). It is offering investors some mix of cash, payables, and property. The CPC has shown limited tolerance for protests and civil unrest. Beijing will likely press for some sort of resolution, but it looks like there are not enough assets to make all creditors and shareholders whole. In one sense, allowing bankruptcy and restructuring will inject an element of hazard to investors, which isn't a bad thing. However, the fallout could be difficult to manage.
- Blackstone (BX, USD, 129.21) [dropped its plans to purchase Soho China](#) (410, HKD, 2.20) due to concerns over a lengthy regulatory review. It may be a polite way of saying China was never going to approve the transaction. The owners of Soho China are under scrutiny regarding concerns they are dumping their properties in China to flee the country. In the current political environment in China, this is a problem. [Shares in Soho China plunged on the news](#).
- The former head of the PBOC, Zhou Xiaochuan, [criticized the venture capital industry](#) for creating a "winner take all" environment in the digital economy. These comments dovetail with Beijing's recent criticism of the "disorderly expansion of capital." Zhou is an establishment figure in China, and his position is further evidence that the investment practice of funding firms with strong network effects may be under pressure in China. He also suggested that curbing tech monopolies would "[ensure growth](#),"

- In related news, regulators have [warned against tech giants blocking links](#) to rival companies.
- Alibaba (BABA, USD, 165.41) has [offered details on how it will spend its CNY 100 billion](#) (USD 16 billion) “common prosperity fund.”
- Although it is being dubbed an “anti-fraud” app, a new app also appears to be designed to track Chinese users’ access to foreign financial news sites. If so, it would suggest that China continues to use the “great firewall” to control the news narrative.
- [The SEC’s Gensler indicates Chinese firms listed in the U.S. will need to be audited.](#) We suspect that won’t happen under General Secretary Xi.

International roundup: Labor wins in Norway, the Peronists don’t win in Argentina, and Lebanon gets aid.

- [Norway’s Labor party and its allies look poised to take control of the government.](#) Labor itself won 48 seats out of 169, over half needed to gain control of the legislature. The Center and the Socialist Left won 28 and 13 seats, respectively, giving it a majority of 89 seats. Most important for Norway’s oil and gas industry, the [current coalition does not need the Greens](#) to form a government. The Greens wanted to end exploration which, would have led to eventual declines in production.
- Meanwhile, [the opposition won handily in primary elections in Argentina.](#) Given recent polling, this outcome was not unexpected.
- Lebanon, which is near economic collapse, [has received \\$1.135 billion in SDRs from the IMF.](#) Although this won’t fix the country’s problems, it will likely buy the new government some time.
- Although the Nord Stream 2 pipeline is complete, [it will be several weeks before gas will flow.](#) The line still needs some final work, testing, and regulatory approval.
- Spain, dealing with rapidly rising electricity prices, [has implemented a windfall profits tax.](#)
- The leaders of the Quad—the U.S., Australia, Japan, and India—will meet in Washington on September 24th. This meeting will be the first one in person for this group. China views this arrangement as an alliance to contain China. We agree with Beijing on this one.

COVID-19: The [number of reported cases](#) is 225,359,152, with 4,641,746 fatalities. In the U.S., there are 41,223,105 confirmed cases with 662,252 deaths. For illustration purposes, the *FT* has created an [interactive chart](#) that allows one to compare cases across nations using similar scaling metrics. The *FT* has also issued an [economic tracker](#) that looks across countries with high-frequency data on various factors. The [CDC reports](#) that 456,755,755 doses of the vaccine have been distributed, with 380,831,725 doses injected. The number receiving at least one dose is 209,701,005, while the number receiving second doses, which would grant the highest level of immunity, is 178,982,950. For the population older than 18, 65.0% of the population has been vaccinated. The *FT* has a page on [global vaccine distribution.](#)

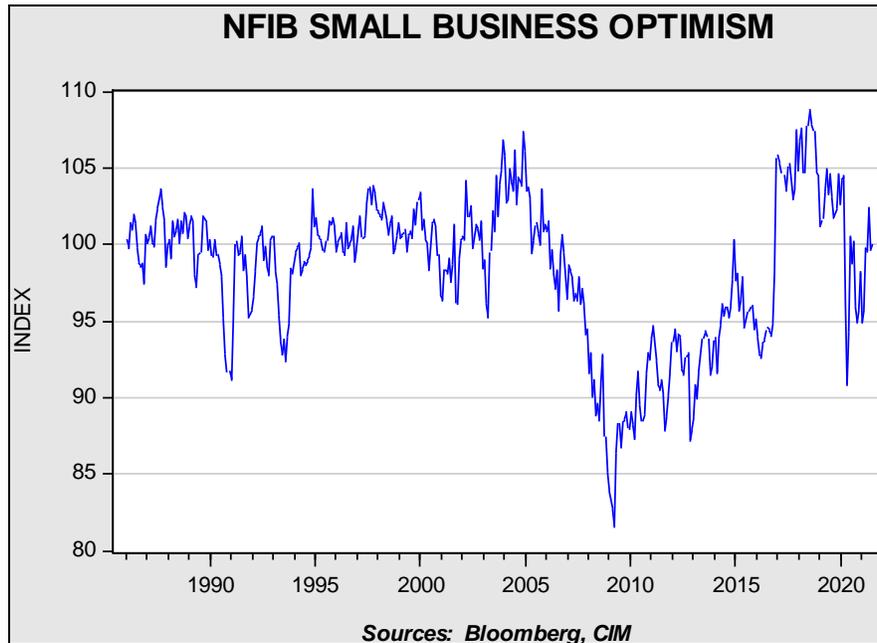
- The [debate of booster shots is heating up.](#) *The Lancet's* most recent research suggests [boosters are not needed at this time.](#) However, the White House is pushing for boosters after promising them and is [accusing the FDA and CDC of withholding data.](#) To us, this

looks like a classic case of a collision between politics and science. Science is a form of inquiry, and “settled science” means that the preponderance of opinion supports a certain point. Since science is inductive, the truths it unearths are always tentative. Politics, on the other hand, is about making decisions with available data. Conflicts are inevitable.

- There are [inquiries about data procedures at the National Institutes of Health](#) after genetic samples of COVID-19 were destroyed at the request of Chinese researchers. Even if this event is innocent, the action does not look good.
- There are [new outbreaks of COVID-19 cases in China](#).

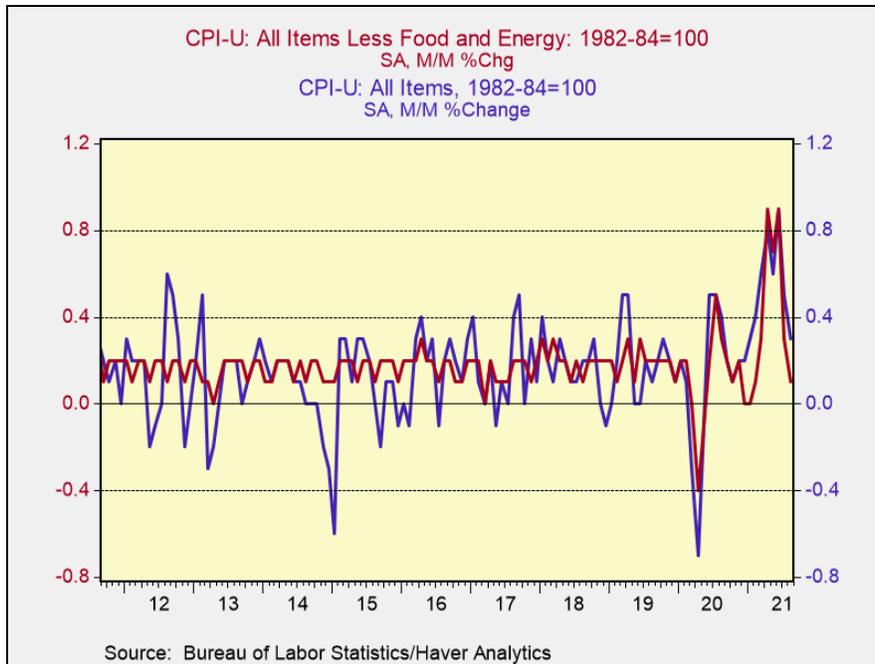
U.S. Economic Releases

In August, small business owners expressed a higher level of optimism, according to the National Federation of Independent Business (NFIB). The NFIB small business optimism index rose to 100.1 from 99.7. Forecasters expected a reading of 99.0.



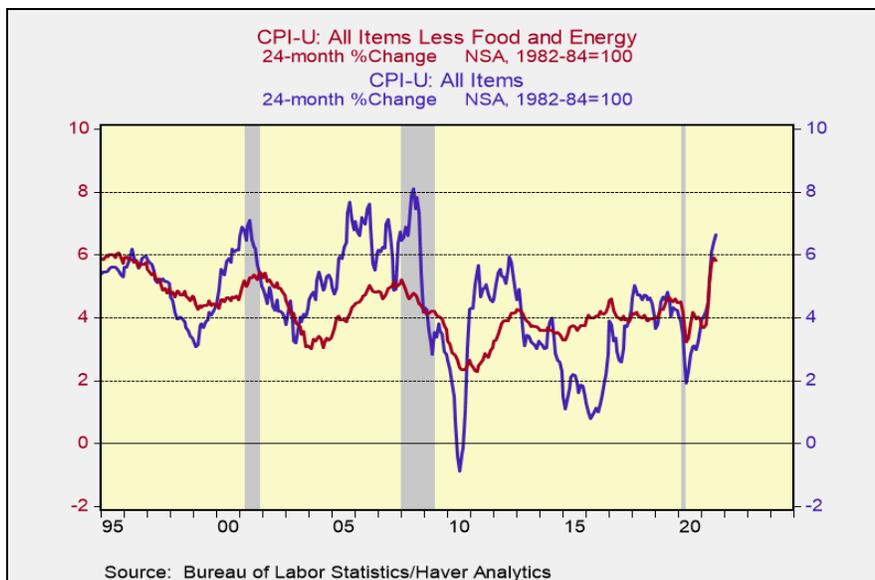
The chart above shows the level of the NFIB Small Business Optimism Index.

Consumers’ prices remained elevated in July but showed signs of moderating. The Consumer Price Index (CPI) came in at 273.567, below expectations of 273.835. The change represents a rise of 0.3% from the prior month, a reading below the 0.4% expected, and a rise of 5.3% from the prior year. Excluding energy and food, consumer prices came in at 279.338, below expectations of 279.74. The change represents a rise of 0.1% from the prior month, better than the 0.3% forecast, and a rise of 4.0% from the prior year.



Even though annual inflation remains above 5%, the monthly inflation suggests that price pressures are starting to ease. Headline CPI rose 0.3% from the prior month, while core CPI rose 0.1%. As the chart above shows, the most recent prices have slowed down considerably over the last two months. As a result, we believe this report reinforces the argument that inflation is most likely transitory.

Looking at the two-year rate of change, which avoids the base effects, inflation is elevated but not well above previous highs.



There are no economic releases or Fed events scheduled for the rest of the day.

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
Japan	Industrial Production	m/m	Jul	-1.5%	-1.5%		***	Equity and bond neutral
	Capacity Utilization	m/m	Jul	-3.4%	6.2%		***	Equity bearish, bond bullish
India	CPI	y/y	Aug	5.3%	5.6%	5.6%	***	Equity bullish, bond bearish
Australia	ANZ Roy Morgan Consumer Confidence	w/w	12-Sep	103.1	100.0		***	Equity bullish, bond bearish
	House Price Index	y/y	2Q	16.8%	7.5%	14.0%	**	Equity bullish, bond bearish
	NAB Business Conditions	M	Aug	14	11		**	Equity bullish, bond bearish
	NAB Business Confidence	M	Aug	-5	-8		**	Equity and bond neutral
New Zealand	REINZ House Sales	y/y	Aug	-26.5%	-11.7%		**	Equity bearish, bond bullish
EUROPE								
France	Bank of France Industry Sentiment	m/m	Aug	104	105	105	***	Equity and bond neutral
UK	Claimant Count Rate	m/m	Aug	5.4%	5.7%		**	Equity bullish, bond bearish
	Jobless Claims Change	m/m	Aug	-58.k	-7.8k		**	Equity bearish, bond bullish
	Average Weekly Earnings 3M/YoY	y/y	Jul	8.3%	8.8%	8.2%	**	Equity and bond neutral
	ILO Unemployment Rate 3Mths	m/m	Jul	4.6%	4.7%	4.6%	***	Equity and bond neutral
	Employment Change 3M/3M	m/m	Jul	183k	95k	199k	**	Equity and bond neutral
AMERICAS								
Mexico	ANTAD Same-Store Sales	y/y	Aug	4.5%	15.3%		***	Equity bearish, bond bullish
Brazil	Trade Balance Weekly	w/w	12-Sep	\$1399m	\$673m		**	Equity bullish, bond bearish
Canada	Bloomberg Nanos Confidence	w/w	10-Sep	61.2	61.6		***	Equity and bond neutral

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.

	Today	Prior	Change	Trend
3-mo Libor yield (bps)	12	11	1	Down
3-mo T-bill yield (bps)	3	4	-1	Neutral
TED spread (bps)	9	7	2	Neutral
U.S. Libor/OIS spread (bps)	8	8	0	Down
10-yr T-note (%)	1.33	1.33	0.00	Down
Euribor/OIS spread (bps)	-54	-54	0	Neutral
EUR/USD 3-mo swap (bps)	4	4	0	Down
Currencies	Direction			
dollar	Down			Down
euro	Flat			Up
yen	Down			Neutral
pound	Up			Neutral
franc	Flat			Neutral
Central Bank Action	Current	Prior	Expected	
Chinese Medium-Term Lending Rate		2.950%		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	\$74.13	\$73.51	0.84%	
WTI	\$70.97	\$70.45	0.74%	
Natural Gas	\$5.27	\$5.23	0.82%	
Crack Spread	\$20.38	\$20.20	0.93%	
12-mo strip crack	\$20.24	\$20.13	0.56%	
Ethanol rack	\$2.59	\$2.60	-0.25%	
Metals				
Gold	\$1,787.79	\$1,793.75	-0.33%	
Silver	\$23.64	\$23.74	-0.43%	
Copper contract	\$433.95	\$436.70	-0.63%	
Grains				
Corn contract	\$ 515.50	\$ 513.25	0.44%	
Wheat contract	\$ 696.00	\$ 687.00	1.31%	
Soybeans contract	\$ 1,290.00	\$ 1,284.75	0.41%	
Shipping				
Baltic Dry Freight	4163	3864	299	
DOE inventory report				
	Actual	Expected	Difference	
Crude (mb)		-3.6		
Gasoline (mb)		-3.0		
Distillates (mb)		-2.0		
Refinery run rates (%)		2.50%		

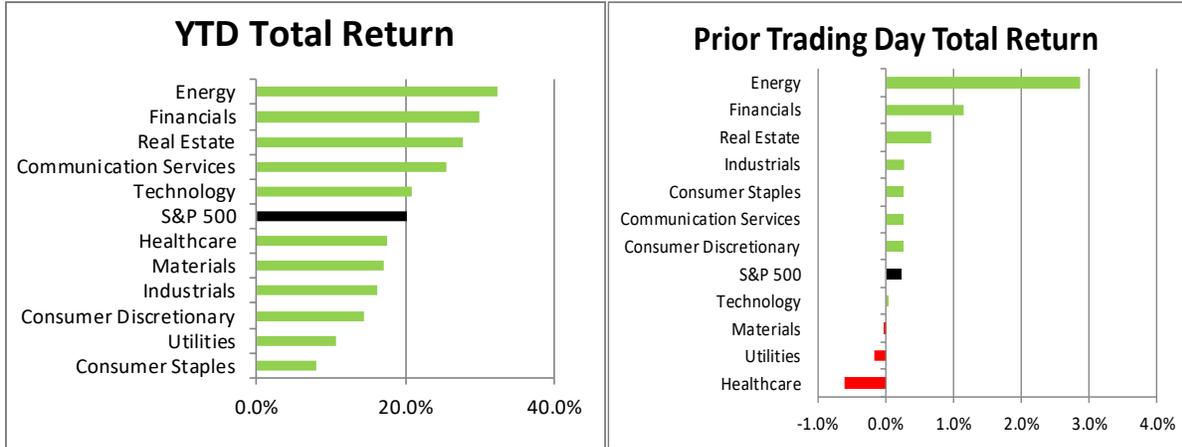
Weather

The 6-10 day and 8-14 day forecasts currently call for warmer-than-normal temperatures throughout the entire eastern two-thirds of the country, with cooler temperatures only in the Pacific Northwest. The forecast calls for wetter-than-normal conditions in the South, the Northeast, and the Pacific Northwest, with dry conditions in the Great Plains.

There are currently three cyclonic disturbances in the Atlantic region and one off the coast of West Africa. One, Tropical storm Nicholas, hit the Texas coast yesterday and is expected to move towards Louisiana. The other two disturbances are in the Atlantic Ocean but are not expected to develop into tropical storms within the next 48 hours. On average, hurricane activity peaks on September 10.

Data Section

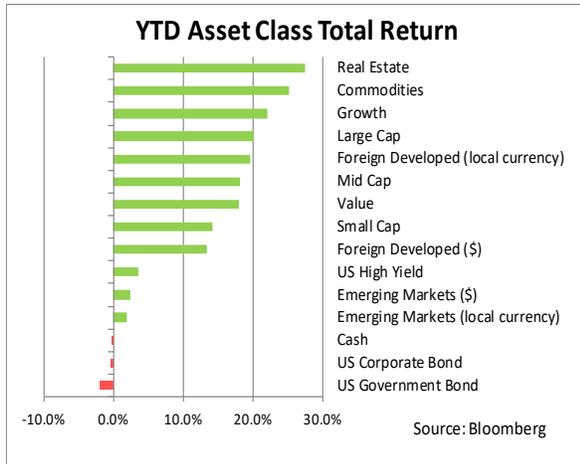
U.S. Equity Markets – (as of 9/13/2021 close)



(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 9/13/2021 close)

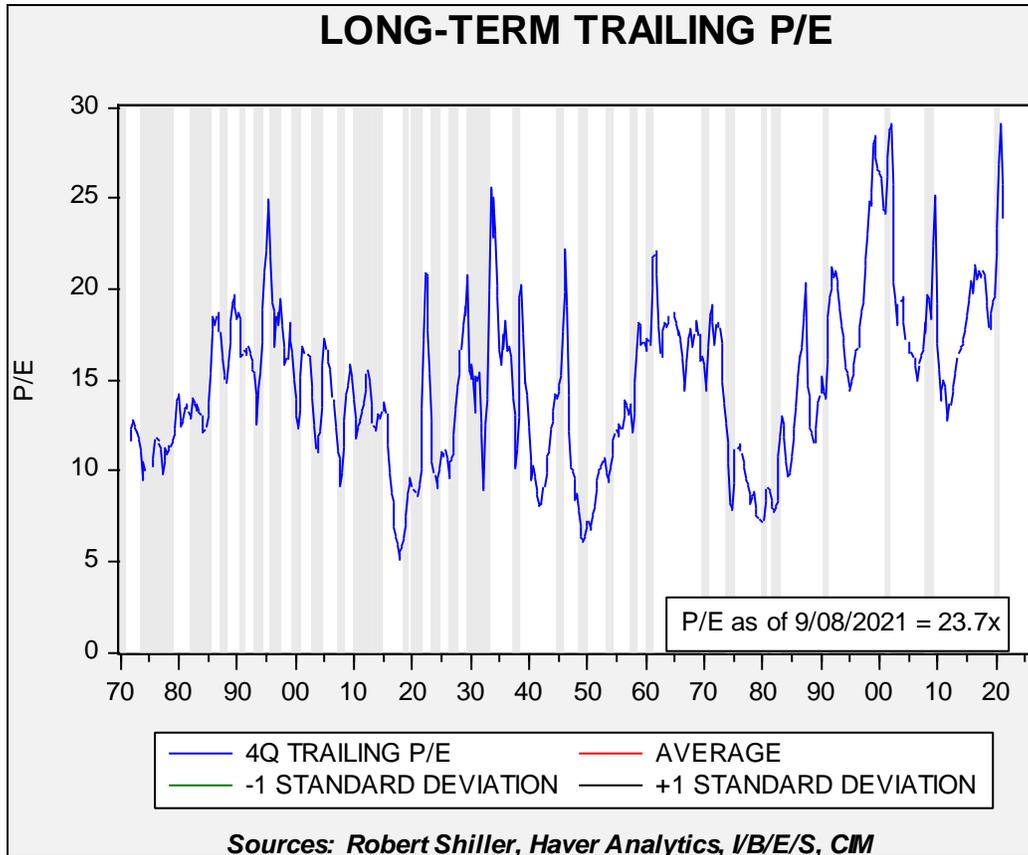


This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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 9, 2021



Based on our methodology,¹ the current P/E is 23.7x, up 0.1x from last week. Higher index values 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 I/B/E/S estimates which are updated regularly throughout the quarter; currently, the four-quarter earnings sum includes three actual quarters (Q4, Q1 and Q2) 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.