

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 19, 2023—9:30 AM EDT]** Global equity markets are mixed this morning. In Europe, the Euro Stoxx 50 is up 0.2% from its prior close. In Asia, the MSCI Asia Apex 50 Index closed down 0.2%. Chinese markets were generally lower, with the Shanghai Composite essentially unchanged from its previous close and the Shenzhen Composite down 0.9%. 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:

- **[Bi-Weekly Geopolitical Report \(9/18/2023\)](#) (with associated [podcast](#)): “Goodbye Prigozhin”**
- [Weekly Energy Update \(9/14/2023\)](#): Oil prices continue their surge higher. The executive director of the IEA suggests we are approaching peak oil demand; as we note in our report, this announcement will likely push crude oil prices higher.
- [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 \(9/11/2023\)](#) (with associated [podcast](#)): “Fiscal Tightening Looms”
- [Confluence of Ideas podcast \(8/22/2023\)](#): “The Economics of Defense in Great Power Competition”

Our *Comment* today opens with updated forecasts for global economic growth from the Organization for Economic Cooperation and Development. The OECD report also urged central banks to keep hiking interest rates and keep them high to snuff out consumer price inflation. We next review a range of other international and U.S. developments with the potential to affect the financial markets today, including an apparent assassination carried out by Indian agents in Canada and the prospect of tighter U.S. regulations on the naming of investment funds.

**Global Economic Growth:** In its [interim Outlook report](#), the OECD scaled back its forecasts for global economic growth to 3.0% in 2023 and 2.7% in 2024. While the organization

increased its forecasts for U.S. gross domestic product to show growth of 2.2% in 2023 and 1.3% in 2024, it cut its forecasts for other key economies.

- Importantly, the organization now sees much weaker growth in the eurozone, which will be held down by Germany and Italy in particular, and in China, where the economy is being held back by issues such as weak consumer demand, high debt levels, poor demographics, and decoupling policies in the West.
- Despite cutting its growth forecasts for many key economies, the OECD [argued forcefully for central banks to raise interest rates further and keep them high](#) for long enough to be sure consumer price inflation is vanquished.

### GDP growth projections

Real GDP, y-o-y growth, %

▲ upward revision, by 0.3pp or more      ■ no change or smaller than 0.3pp      ▼ downward revision, by 0.3pp or more

	2022	2023	2024		2022	2023	2024
<b>World</b>	3.3	3.0	2.7	<b>G20</b>	3.1	3.1	2.7
<b>Australia</b>	3.7	1.8	1.3	<b>Argentina</b>	5.0	-2.0	-1.2
<b>Canada</b>	3.4	1.2	1.4	<b>Brazil</b>	3.0	3.2	1.7
<b>Euro area</b>	3.4	0.6	1.1	<b>China</b>	3.0	5.1	4.6
<b>Germany</b>	1.9	-0.2	0.9	<b>India</b>	7.2	6.3	6.0
<b>France</b>	2.5	1.0	1.2	<b>Indonesia</b>	5.3	4.9	5.2
<b>Italy</b>	3.8	0.8	0.8	<b>Mexico</b>	3.9	3.3	2.5
<b>Spain</b>	5.5	2.3	1.9	<b>Russia</b>	-2.0	0.8	0.9
<b>Japan</b>	1.0	1.8	1.0	<b>Saudi Arabia</b>	8.8	1.9	3.1
<b>Korea</b>	2.6	1.5	2.1	<b>South Africa</b>	1.9	0.6	1.1
<b>United Kingdom</b>	4.1	0.3	0.8	<b>Türkiye</b>	5.5	4.3	2.6
<b>United States</b>	2.1	2.2	1.3				

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Note: Revisions relative to the latest estimates from the June 2023 Economic Outlook. India projections are based on fiscal years, starting in April. The European Union is a full member of the G20, but the G20 aggregate only includes countries that are also members in their own right. Spain is a permanent invitee to the G20. World and G20 aggregates use moving nominal GDP weights at purchasing power parities.  
 Source: OECD Economic Outlook 113 databases; and OECD Interim Economic Outlook 114 database.

**United Nations General Assembly:** The annual meetings of the UN General Assembly began in New York this week, but the proceedings so far have been [rather sleepy](#). The top news to date is probably the [announcement of a new “Partnership for Atlantic Cooperation” led by the U.S. and encompassing dozens of countries that touch the Atlantic Ocean](#) in Europe, Africa, and the Americas.

- To wean countries from China’s embrace, the pact offers improved economic, environmental, and scientific ties among the signatories.
- The agreement also contains pledges to support territorial integrity and political independence, although it doesn’t include any security or military ties.

**China-United States:** The American Chamber of Commerce in Shanghai said an annual survey of its members [showed that only 58% were optimistic about their business prospects in China over the coming five years](#). That marked the lowest level of optimism in the survey since it was

launched in 1999. As we have warned previously, companies that export to China or participate in its markets are likely to face headwinds because of issues like worsening U.S.-China tensions; clampdowns on trade, technology, and investment flows; and China's own domestic economic challenges.

**China-Germany:** The Chinese government on Sunday [called in the German ambassador to complain about Foreign Minister Baerbock's recent description of President Xi as a dictator](#). The incident highlights the increasingly frosty relationship between China and Germany as some German officials take a harder line on China while others keep trying to maintain good relations in the interest of trade and investment. Ultimately, we suspect the hardliners in Germany will win the day, with negative consequences for the trade-dependent economy.

**India-Canada:** In an emergency meeting with lawmakers, Canadian Prime Minister Trudeau [said his government is investigating "credible allegations" that Indian agents may have helped kill an exiled Sikh leader near Vancouver](#) in June. The Sikh leader, Hardeep Singh Nijjar, was a Canadian citizen, prompting Trudeau to call the violation of Canadian sovereignty especially heinous. In response, Ottawa yesterday expelled a senior Indian diplomat.

- The incident will further strain Indian-Canadian relations, with potential economic consequences. The Canadian government recently cancelled a trade mission to Mumbai set for October.
- If true, the incident also points to an ominous shift toward brazen, extraterritorial measures by Indian Prime Minister Modi, who many accuse of becoming increasingly authoritarian. If Modi really is adopting the extraterritorial "justice" practiced by authoritarian leaders such as Chinese President Xi, Russian President Putin, and Saudi Crown Prince Mohammed Bin Salman, it may become more politically difficult for the U.S. to embrace New Delhi as a partner in its geopolitical competition with China.

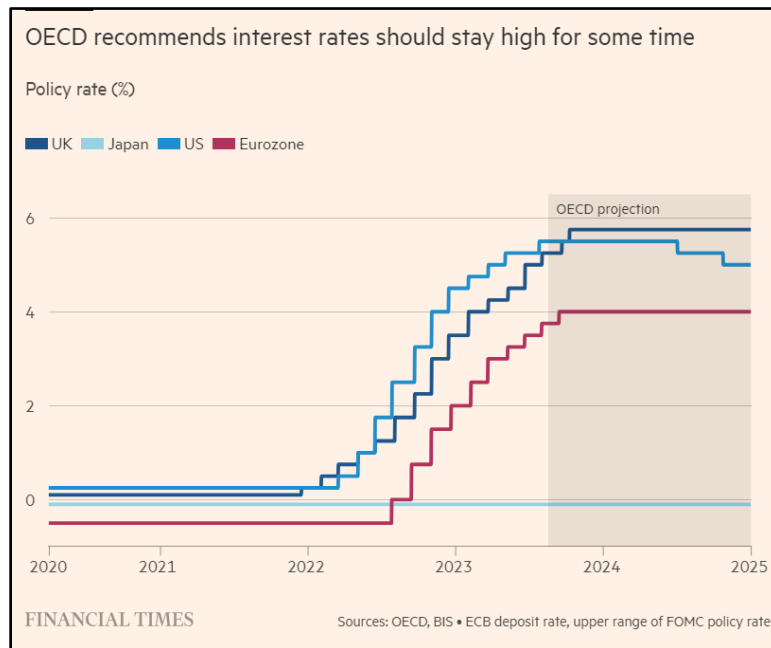
**Poland:** Ahead of national elections next month, the ruling right-wing Law and Justice Party [is reeling from a scandal in which officials are accused of selling Polish visas at foreign consulates](#) despite the government's assurances it is being tough on illegal immigration. The political threat from the scandal is probably a reason why the government this week clamped down on Ukrainian food imports to bolster its largely rural voter base. The Law and Justice Party is still leading the opinion polls, but if its support declines further and it falls out of power, Polish rule-of-law issues would probably no longer be a thorn in the side of the European Union.

**Libya:** In the aftermath of last week's floods, which killed thousands in the coastal city of Derna, hundreds of citizens yesterday [participated in a violent demonstration demanding an investigation into who was responsible and why the government's response has been so poor](#). A key issue is why two nearby dams burst amid torrential rainfall. Some reports say the dams hadn't been maintained for 20 years, despite the provision of government appropriations.

- Derna lies in the territory controlled by Khalifa Haftar, a warlord who is supported by Russia and some Persian Gulf monarchies.

- At least for now, the demonstrators are focusing their ire on civilian authorities in the provincial government. However, if they start to target Haftar and his forces, they could spark a bloody crackdown and perhaps even international intervention.

**U.S. Monetary Policy:** The Federal Reserve will begin its latest policy meeting today, with its decision on interest rates due tomorrow at 2:00 PM EDT. The officials [are widely expected to hold the benchmark fed funds rate steady at its current range of 5.25% to 5.50%](#). The question is whether they’ll provide any guidance on future policy changes. Many investors continue to look for rate cuts in the coming months, but we think they’ll be disappointed. We believe the Fed will try to keep policy tight for an extended period to make sure consumer price inflation is really dead, as recommended by the OECD.



**U.S. Regulatory Policy:** The Securities and Exchange Commission tomorrow [will take up a proposal to tighten its “names rule” to crack down on deceptive fund descriptions](#). The new truth-in-advertising rule would require that at least 80% of the assets held by mutual funds and other investment vehicles match the fund’s description as presented to investors. Financial industry officials warn that the rule could discourage stock picking, violate free speech protections, and force funds to sell assets at a loss when markets are volatile.

**U.S. Defense Industry:** At a conference last week, Defense Department Undersecretary for Acquisitions and Sustainment Bill LaPlante unexpectedly announced that the U.S. [is now far ahead of schedule on the Pentagon’s goal of boosting production of 155-mm artillery shells](#). According to LaPlante, output of the shells has already doubled versus just six months ago, to 28,000 shells per month. Production is now expected to reach 57,000 per month next spring and 100,000 per month by fiscal year 2025, which begins next October. The military’s original goal was 85,000 per month by fiscal 2028.

- The surge in production for 155-mm shells will help replenish U.S. stockpiles and allow for the continued support of Ukraine as it tries to defend itself against Russia’s invasion.
- Although the 155-mm shell is just one of many different types of ammunition and weapons systems that are important to the U.S. military, the surge in its output is welcome evidence that the U.S. defense industry may be able to generally boost production faster than previously thought. That would be a critical capability as the U.S. works to quickly rebuild its armed forces in response to China’s rapid military buildup and increased geopolitical aggressiveness.
- The surge in 155-mm shell output also helps confirm our view that we will see a bigger, re-invigorated industrial sector as companies bring production back home from China or elsewhere, and as U.S. and allied defense budgets are ratcheted upward. We continue to believe that industrial firms and defense contractors, in particular, will offer attractive investment opportunities in the coming years.

## U.S. Economic Releases

Construction of new dwellings slowed more than expected in August. Housing starts expanded at an annual rate of 1283k last month, according to the U.S. Census Bureau. The reading showed that homebuilding fell 11.3% from the prior month, much worse than the expected decline of 2.5%. However, homebuilder plans for future projects unexpectedly jumped. Building permit applications increased 6.9% from July to August, reaching an annual rate of 1543k.



The chart above shows new home constructions for multi- and single-family homes. In August, homebuilders were able to expand single-family homes at an annual pace of 941k, and multi-family homes at annual rate of 342k.

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
<b>ASIA-PACIFIC</b>								
<b>EUROPE</b>								
Eurozone	CPI	y/y	Aug F	5.2%	5.3%	5.3%	***	Equity and bond neutral
	Core CPI	y/y	Aug F	5.3%	5.3%	5.3%	**	Equity and bond neutral
Italy	Current Account Balance	m/m	Jul	5156m	5995m		*	Equity and bond neutral
Switzerland	Real Exports	m/m	Aug	5.9%	-4.0%	-4.9%	*	Equity bullish, bond bearish
	Real Imports	m/m	Aug	1.5%	-1.8%		*	Equity bullish, bond bearish
<b>AMERICAS</b>								
Canada	Housing Starts	m/m	Aug	252.8k	255.0k	250.0k	**	Equity and bond neutral
	Industrial Product Price	m/m	Aug	1.3%	0.4%	0.2%	**	Equity bullish, bond bearish
	Raw Materials Price Index	m/m	Aug	3.0%	3.5%	1.0%	*	Equity bullish, bond bearish
Brazil	Economic Activity Index	y/y	Jul	0.66%	2.10%	1.00%	**	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.

Fixed Income	Today	Prior	Change	Trend
3-mo Libor yield (bps)	566	567	-1	Up
3-mo T-bill yield (bps)	529	530	-1	na
TED spread (bps)	LIBOR and the TED Spread have been discontinued.			
U.S. Sibor/OIS spread (bps)	539	539	0	Up
U.S. Libor/OIS spread (bps)	541	541	0	Up
10-yr T-note (%)	4.34	4.33	0.01	Flat
Euribor/OIS spread (bps)	388	387	1	Up
<b>Currencies</b>	<b>Direction</b>			
Dollar	Down			Up
Euro	Up			Down
Yen	Flat			Down
Pound	Up			Down
Franc	Up			Flat

## 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
<b>Energy Markets</b>				
Brent	\$94.72	\$94.43	0.31%	
WTI	\$92.23	\$91.48	0.82%	
Natural Gas	\$2.74	\$2.73	0.40%	
Crack Spread	\$29.30	\$29.60	-1.03%	
12-mo strip crack	\$28.20	\$28.56	-1.25%	
Ethanol rack	\$2.51	\$2.53	-0.89%	
<b>Metals</b>				
Gold	\$1,935.18	\$1,933.84	0.07%	
Silver	\$23.35	\$23.24	0.46%	
Copper contract	\$374.10	\$377.90	-1.01%	
<b>Grains</b>				
Corn contract	\$468.50	\$471.50	-0.64%	
Wheat contract	\$585.25	\$591.25	-1.01%	
Soybeans contract	\$1,311.75	\$1,316.75	-0.38%	
<b>Shipping</b>				
Baltic Dry Freight	1,439	1,381	58	
<b>DOE Inventory Report</b>				
	<b>Actual</b>	<b>Expected</b>	<b>Difference</b>	
Crude (mb)		0.3		
Gasoline (mb)		1.1		
Distillates (mb)		1.1		
Refinery run rates (%)		-1.0%		
Natural gas (bcf)		52		

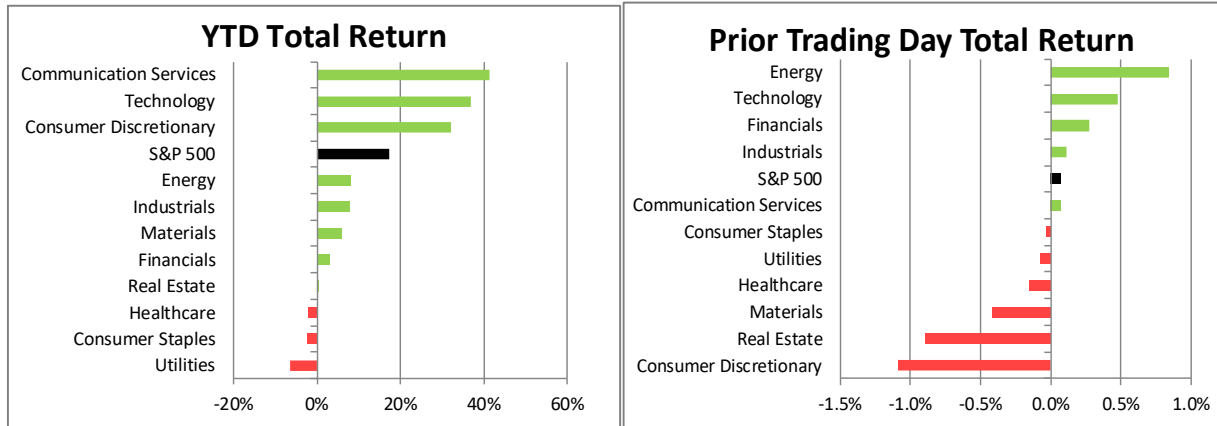
## Weather

The 6-10 and 8-14 day forecasts currently call for warmer-than-normal temperatures throughout most of the country, with below-normal temperatures throughout the southern Pacific region. The precipitation outlook is calling for wetter-than-normal conditions for most of the central states, with dry conditions expected in the Rocky Mountains and Great Lakes regions.

There is currently one atmospheric disturbance in the Atlantic Ocean area. Hurricane Nigel is moving through the central Atlantic; however, it is not expected to make landfall. We note that Atlantic hurricane activity peaks, on average, September 15.

**Data Section**

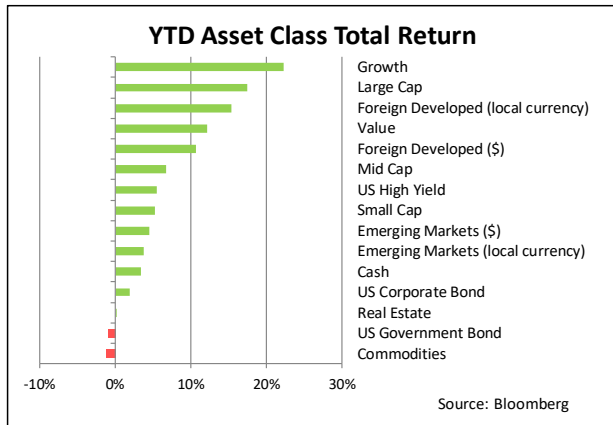
**U.S. Equity Markets – (as of 9/18/2023 close)**



(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 9/18/2023 close)**



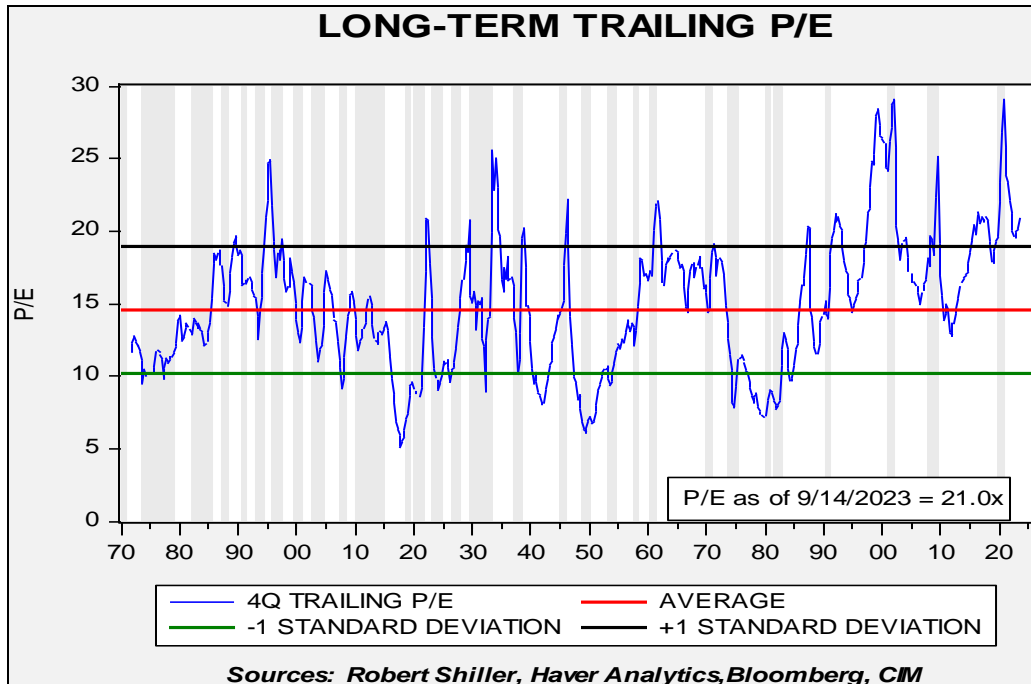
This chart shows the year-to-date returns for various asset classes, updated daily. The asset classes are ranked by total return (including dividends), with green indicating positive and red indicating negative returns from the beginning of the year, as of prior close.

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 14, 2023



Based on our methodology,<sup>1</sup> the current P/E is 21.0x, unchanged from last week.

*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.*

<sup>1</sup> 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.