

James Bianco

Risks For 2019

CFA Los Angeles Annual Forecasting Dinner
January 23, 2019



When Does The S&P 500 Make
The High and Low of the Year?
1927 to 2018

Month	High	Low
January	13	32
February	4	9
March	3	7
April	2	5
May	4	3
June	1	5
July	5	4
August	3	3
September	8	4
October	6	9
November	10	4
December	32	6

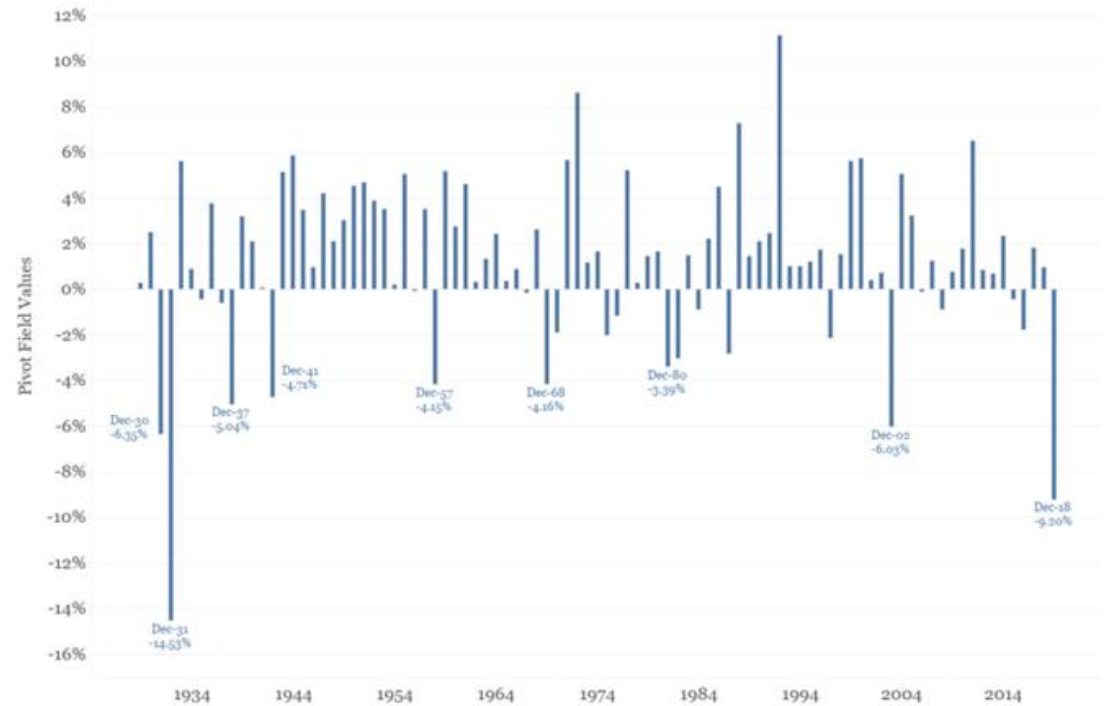
Source: The Chart Store (www.thechartstore.com)

When The Stock Market Makes New Lows In December The Following Year Is Not Pretty!

1927 to 2018						
Year of December Low (date)	Following Year	Recession Year?	The Following Year's S&P 500 Returns			
			Q1	Q2	Full Year	
12/17/1930	1931	Yes	-8.80%	3.32%	-47.07%	
12/17/1931	1932	Yes	-9.98%	-45.44%	-14.78%	
12/29/1941	1942	No	-7.83%	-4.49%	12.43%	
12/14/1973	1974	Yes	-3.66%	-11.84%	-29.72%	
12/20/2000	2001	Yes	-12.11%	-7.26%	-13.04%	
12/17/2018	2019	???	???	???	???	
Average			-8.48%	-13.14%	-18.44%	

Source: The Chart Store (www.thechartstore.com)

S&P 500 Price Return for December Only



Source: Bloomberg

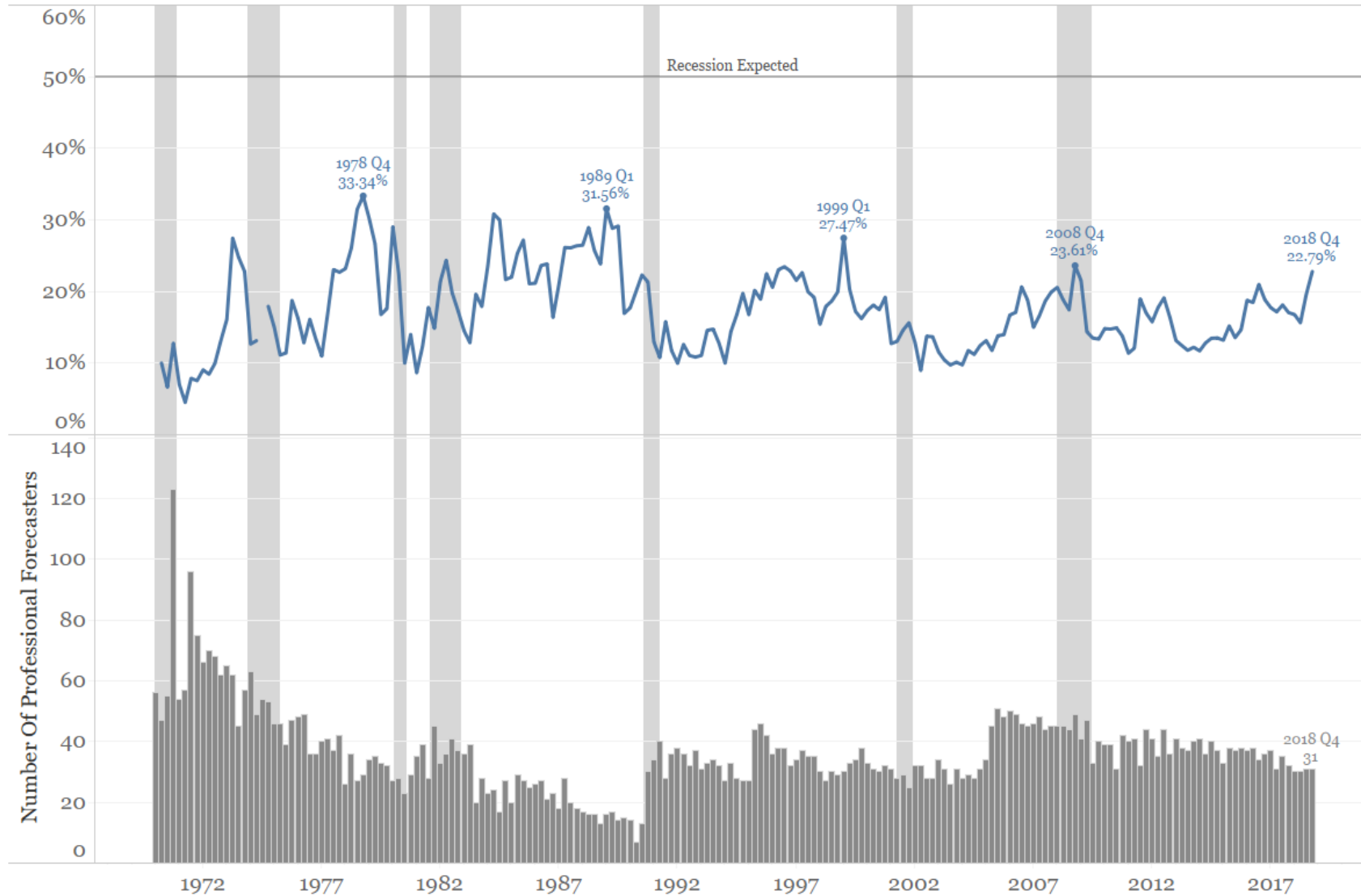
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I don't think that expansions just die of old age. Two things usually end them. One is financial imbalances and the other is the Fed, and usually when the Fed ends a recession — ends an expansion, it's because inflation has gotten out of control and the Fed needs to tighten to bring it down. – Janet Yellen, January 4, 2019

But as Janet says, expansions don't die of old age. I'd like to say they get murdered, instead. – Ben Bernanke, January 4, 2019

They Never See A Recession Coming

Probability of Decline in Real GDP in the Next Four Quarters - Average of A Survey of Professional Forecasters

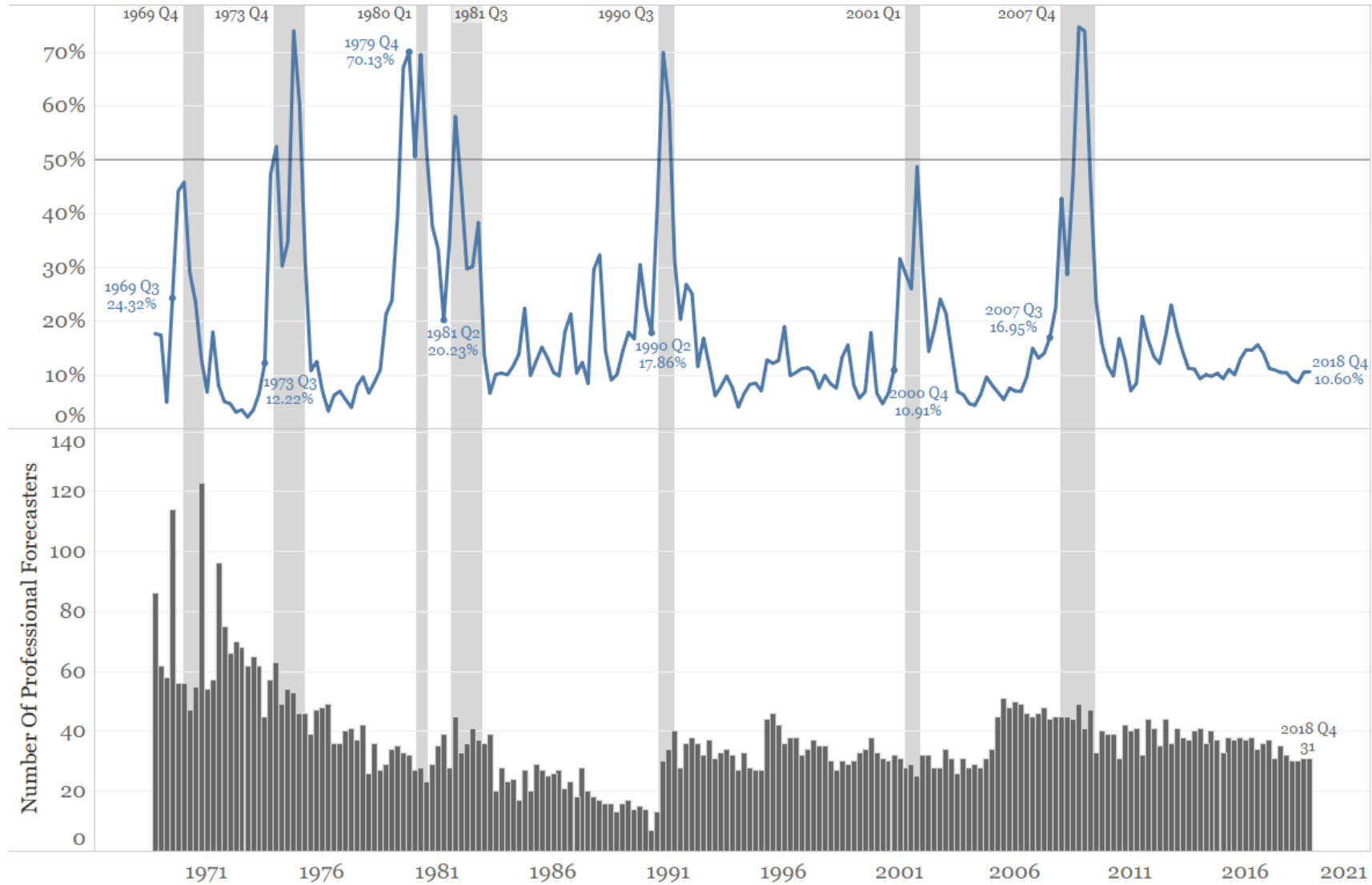


Data Source: Philadelphia Federal Reserve
<https://www.philadelphiafed.org/research-and-data/real-time-center/survey-of-professional-forecasters>

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The Anxious Index

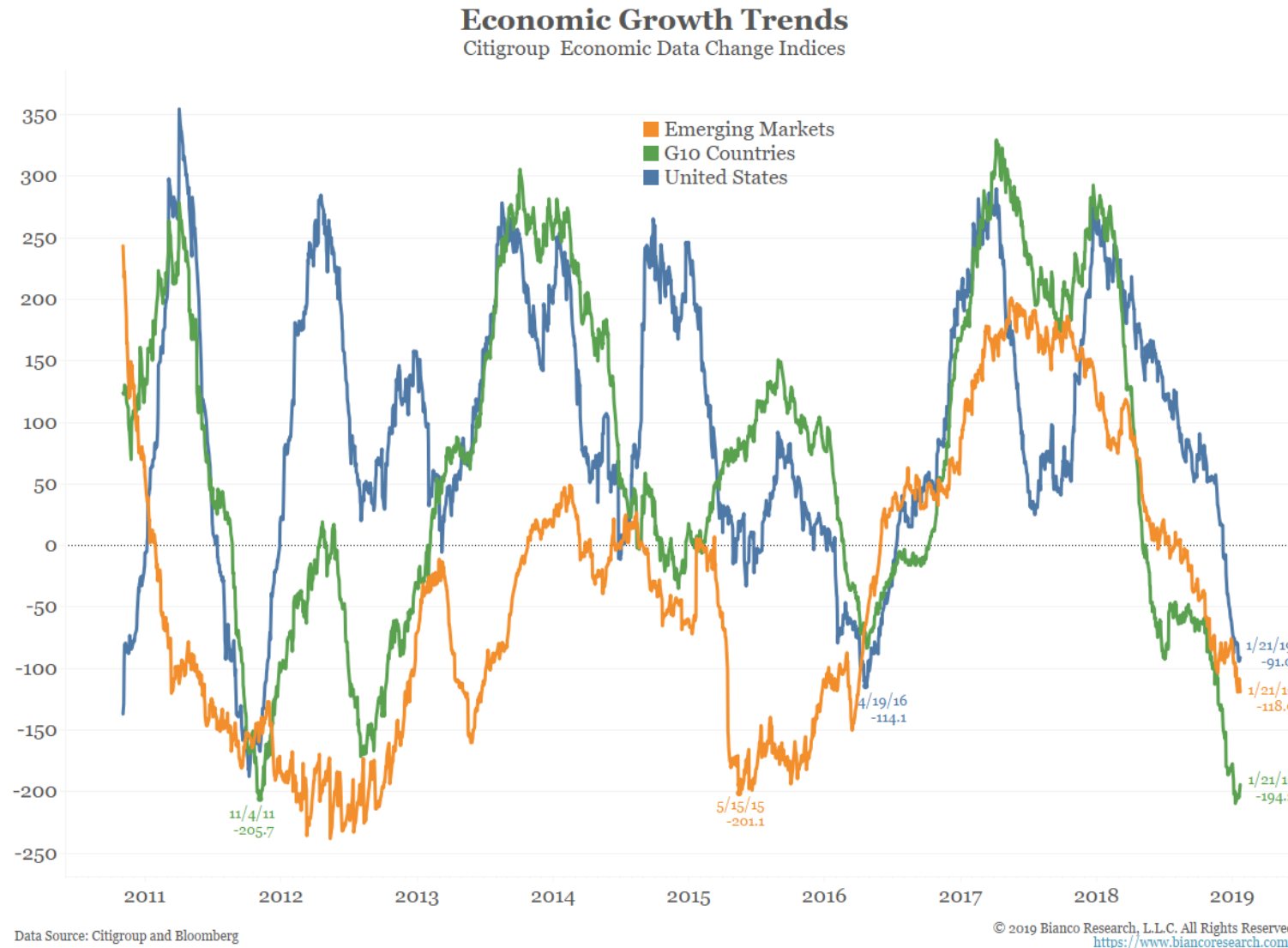
Probability of Decline in Real GDP in the Following Quarter



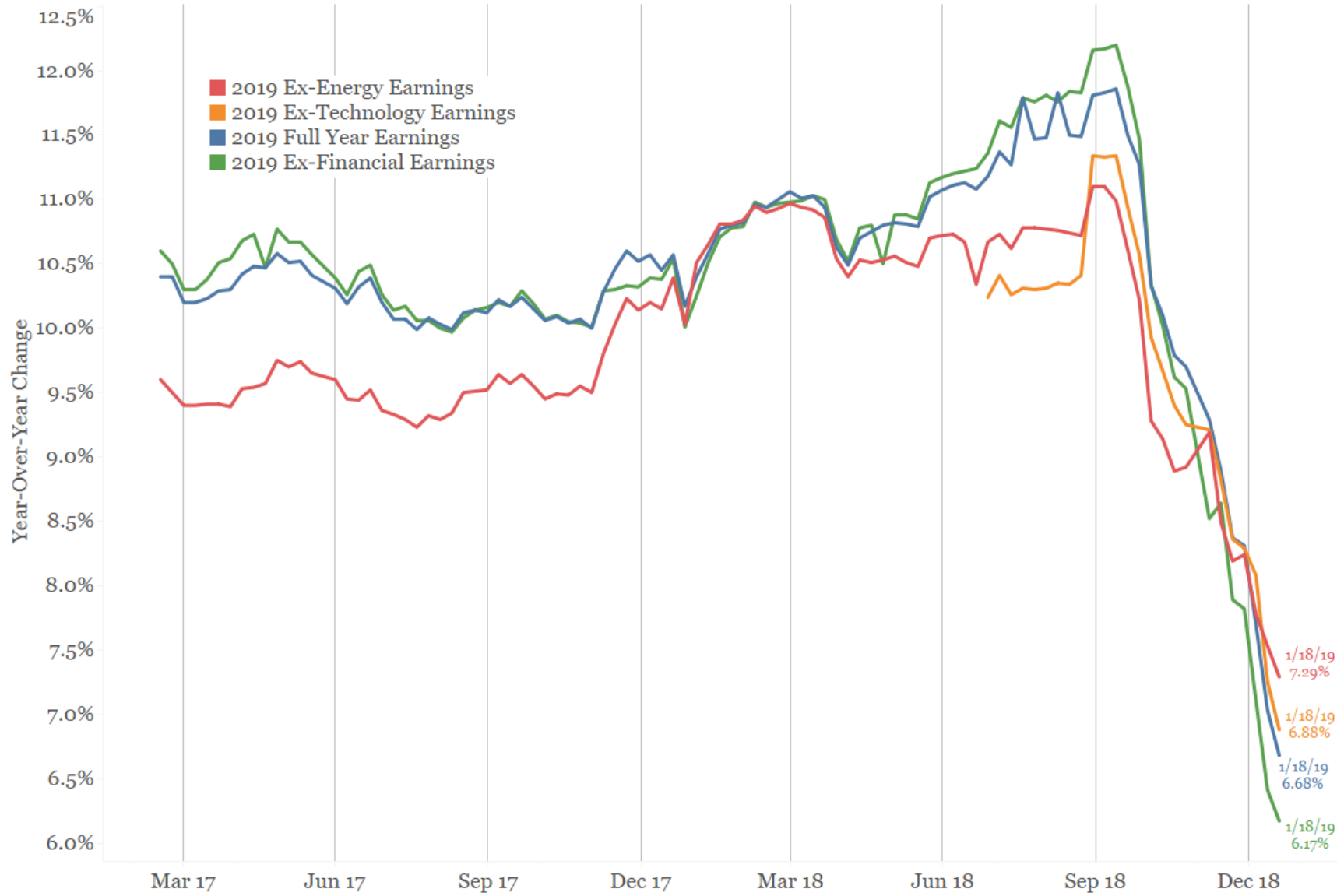
Data Source: Philadelphia Federal Reserve
<https://www.philadelphiafed.org/research-and-data/real-time-center/survey-of-professional-forecasters>

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*“There’s really **no reason to think that this cycle can’t continue for quite some time, effectively indefinitely,**” Powell said Wednesday at an event in Washington hosted by The Atlantic magazine and the Aspen Institute.*
– [Bloomberg](#), October 4, 2018



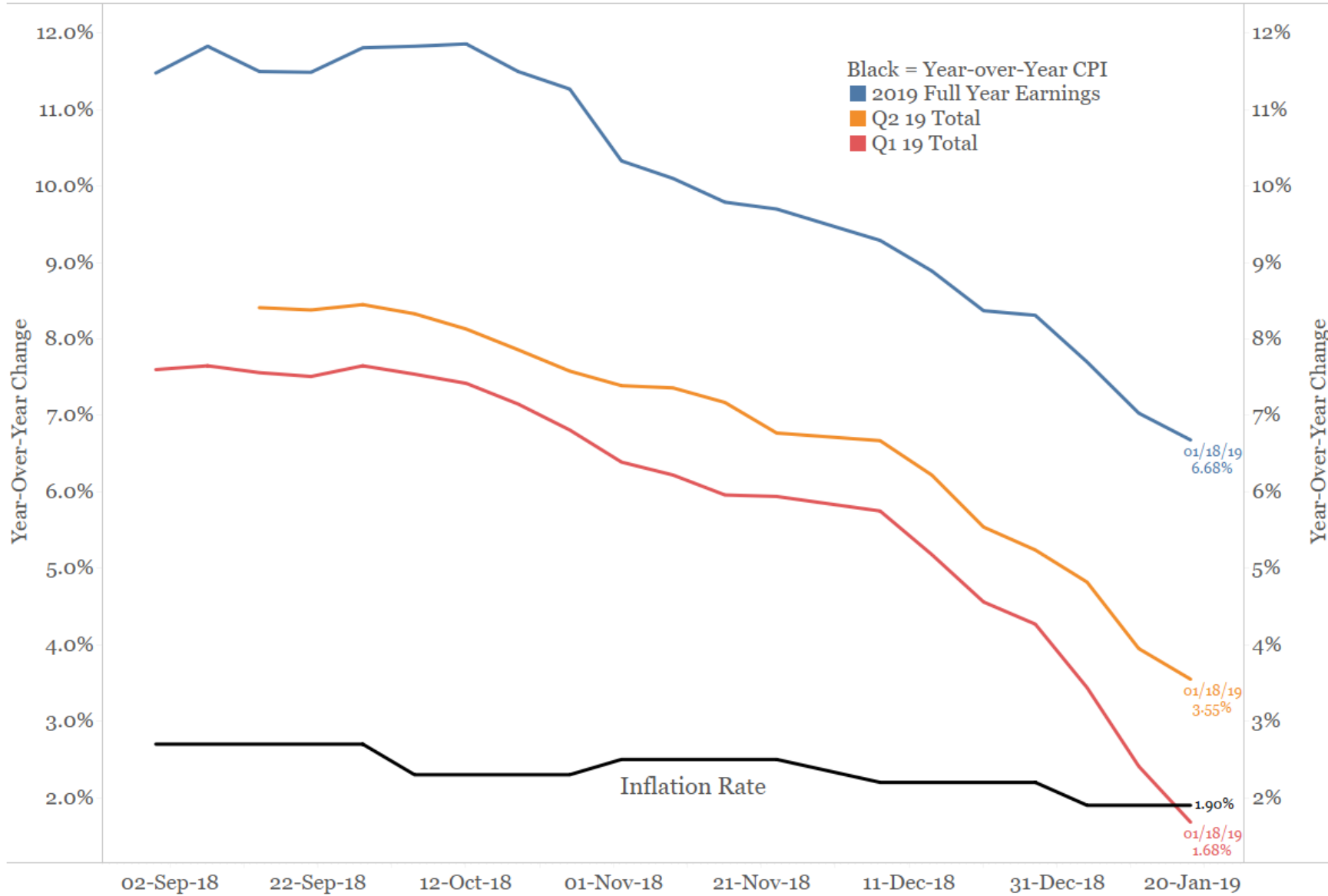
2019 S&P 500 Earnings Expectations



Source: Bloomberg

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2019 S&P 500 Operating Earnings Expectations



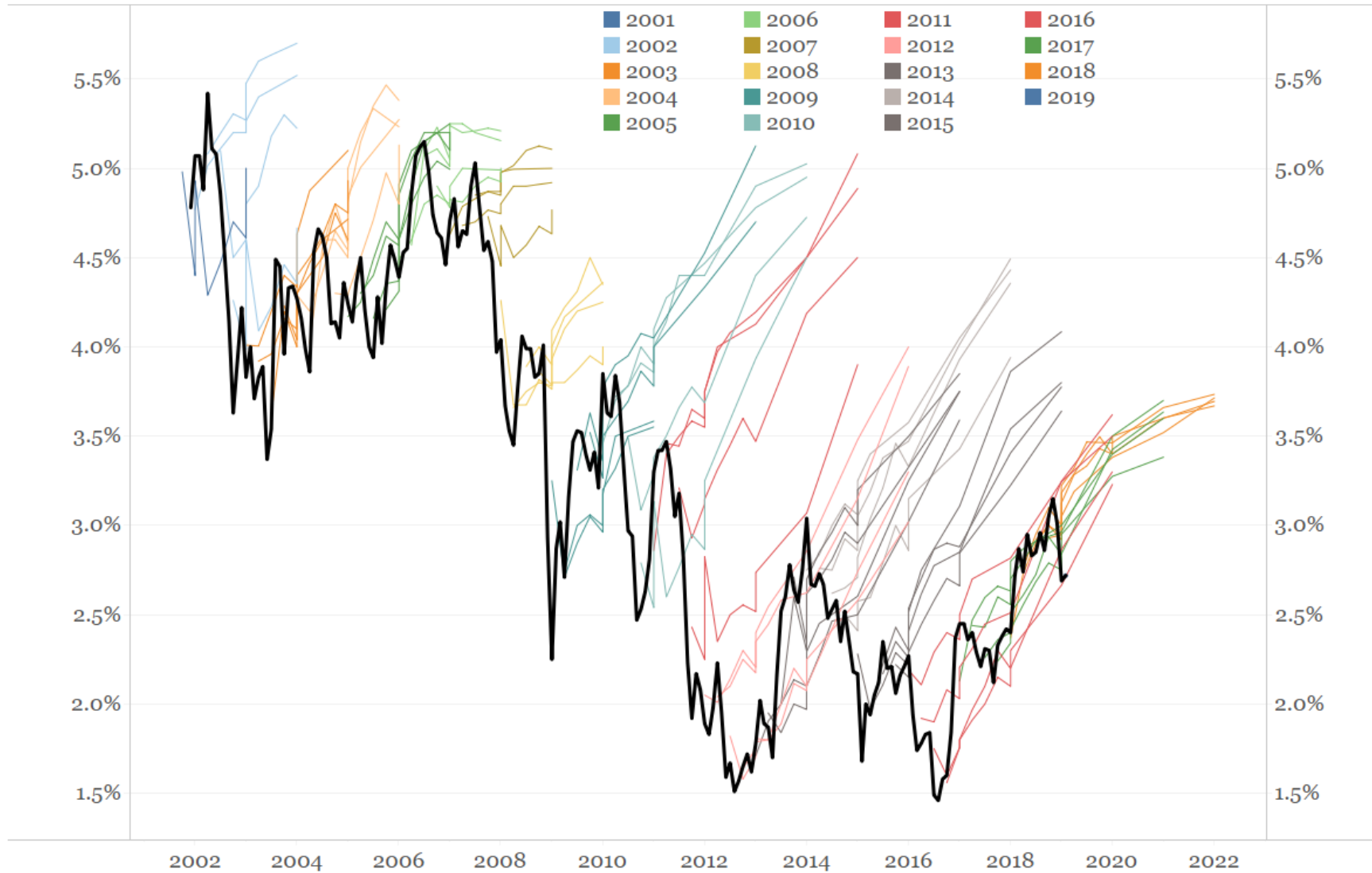
Source: Bloomberg

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Survey of Professional Forecasters

10-Year Treasury Yield

Philadelphia Federal Reserve



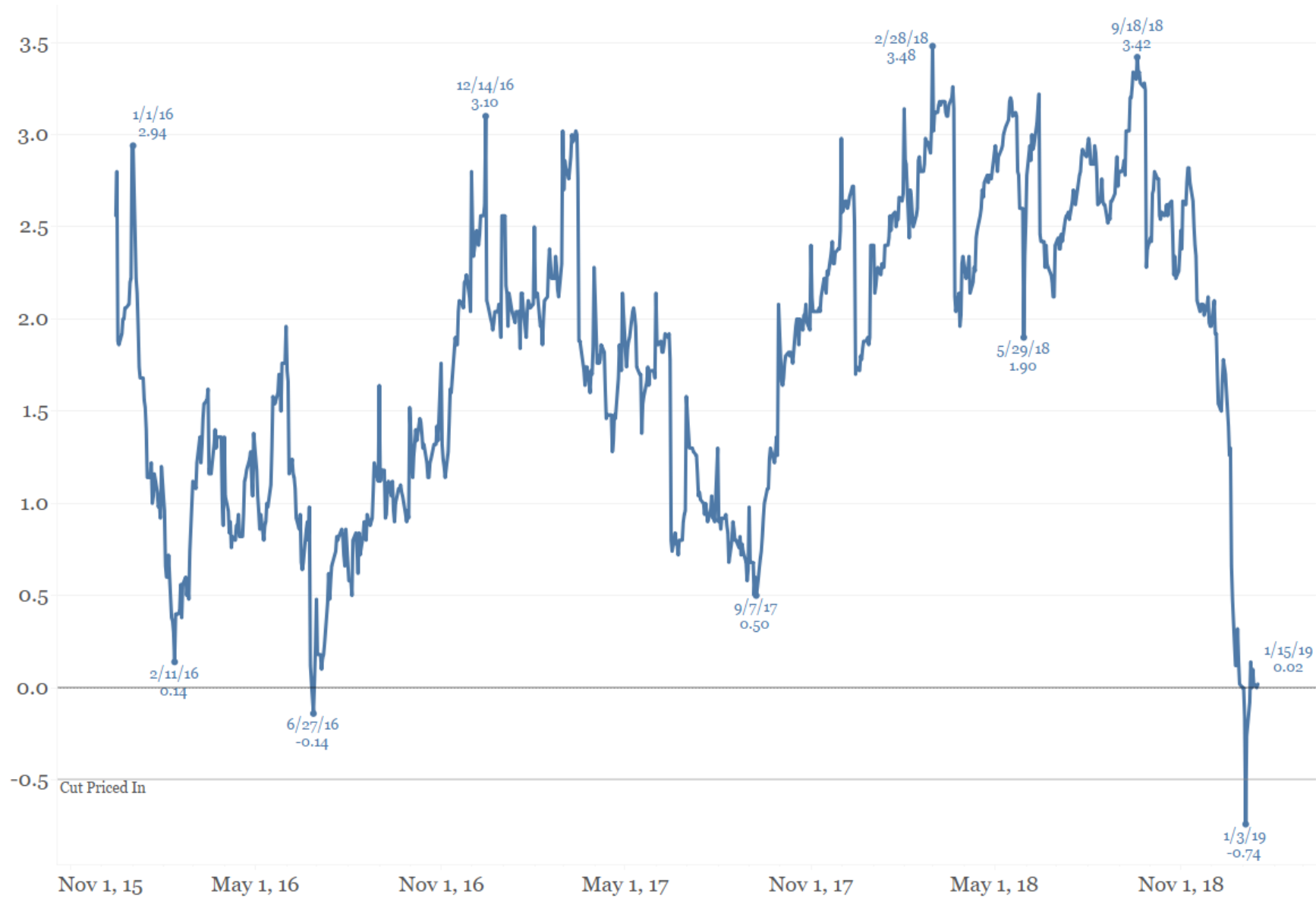
Data Source: Federal Reserve Bank of Philadelphia
<https://www.philadelphiafed.org/research-and-data/real-time-center/survey-of-professional-forecasters/data-files>

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So we thought carefully about this, on how to normalize policy and came to the view that we would effectively have the balance sheet runoff on automatic pilot and use monetary policy, rate policy to adjust to incoming data.

– Jay Powell, December 19, 2019

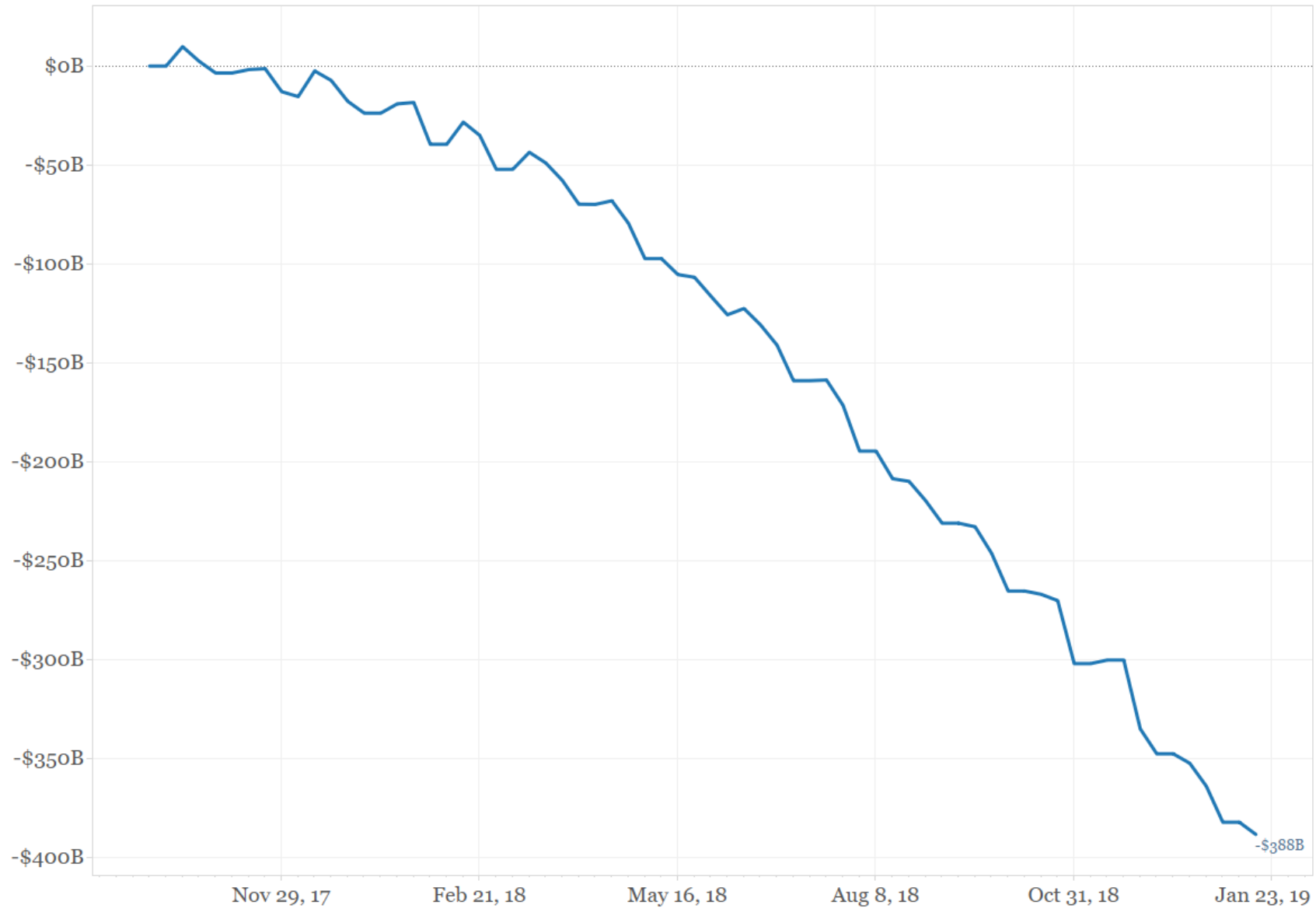
Number of Hikes Over The Next 12 Months



Source: Bloomberg WIRP Function

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How Much Has The Fed Reduced It Balance Sheet?

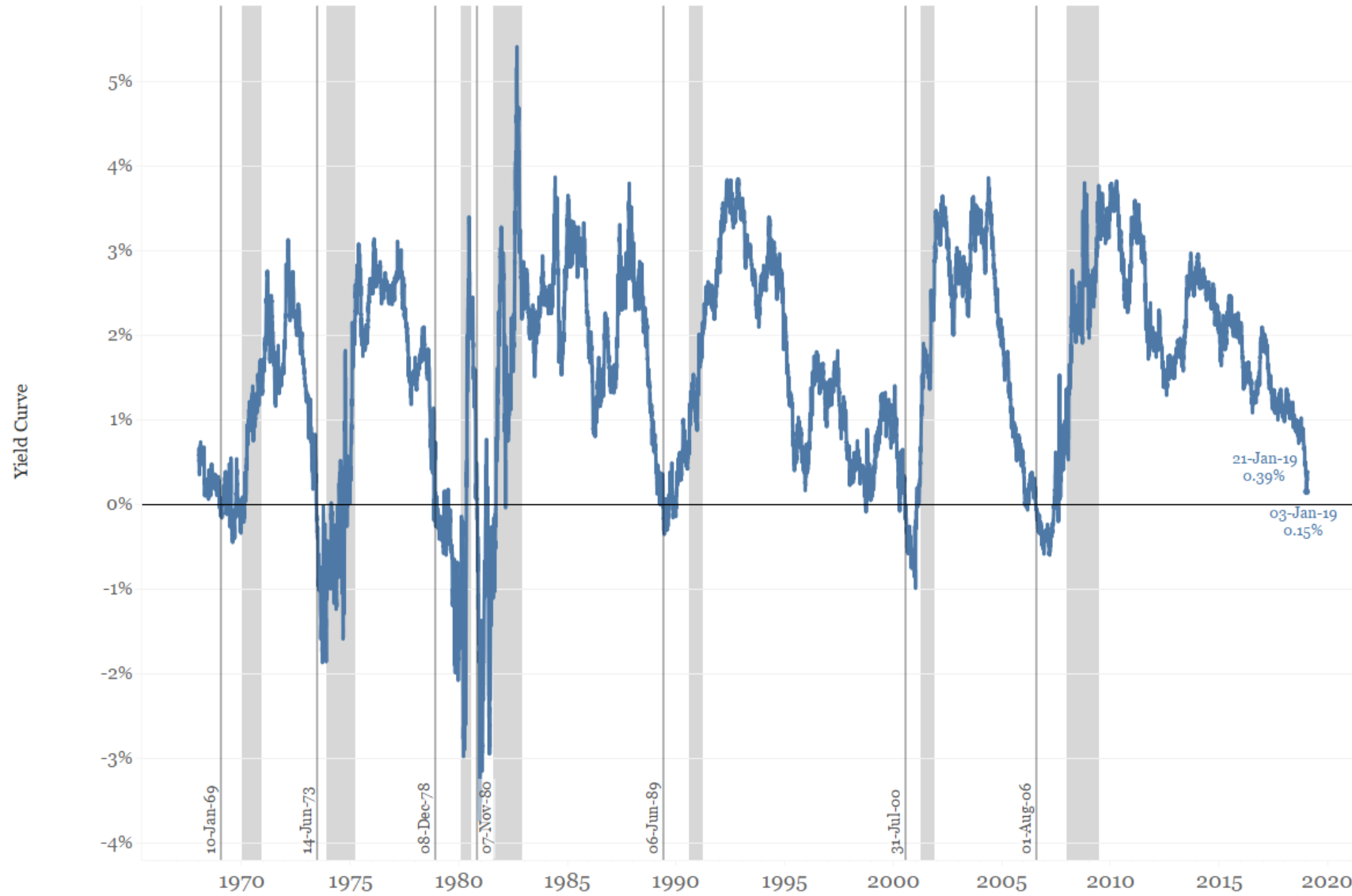


Data Source: Bloomberg

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Yield Curve Inversions Lead Recessions

10-Year less 3-Month Yield Curve



Data Source: Federal Reserve and Bloomberg

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How Long Until The Recession?

When the 3M/10Yr Curve Inverts For 10 Straight Days

Date of Inversion	Date of Next Recession	Days to Next Recession
1/10/1969	Dec-69	325
6/14/1973	Nov-73	140
12/8/1978	Jan-80	389
11/7/1980	Jul-81	236
6/6/1989	Jul-90	390
7/31/2000	Mar-01	213
8/1/2006	Dec-07	487
Average		311

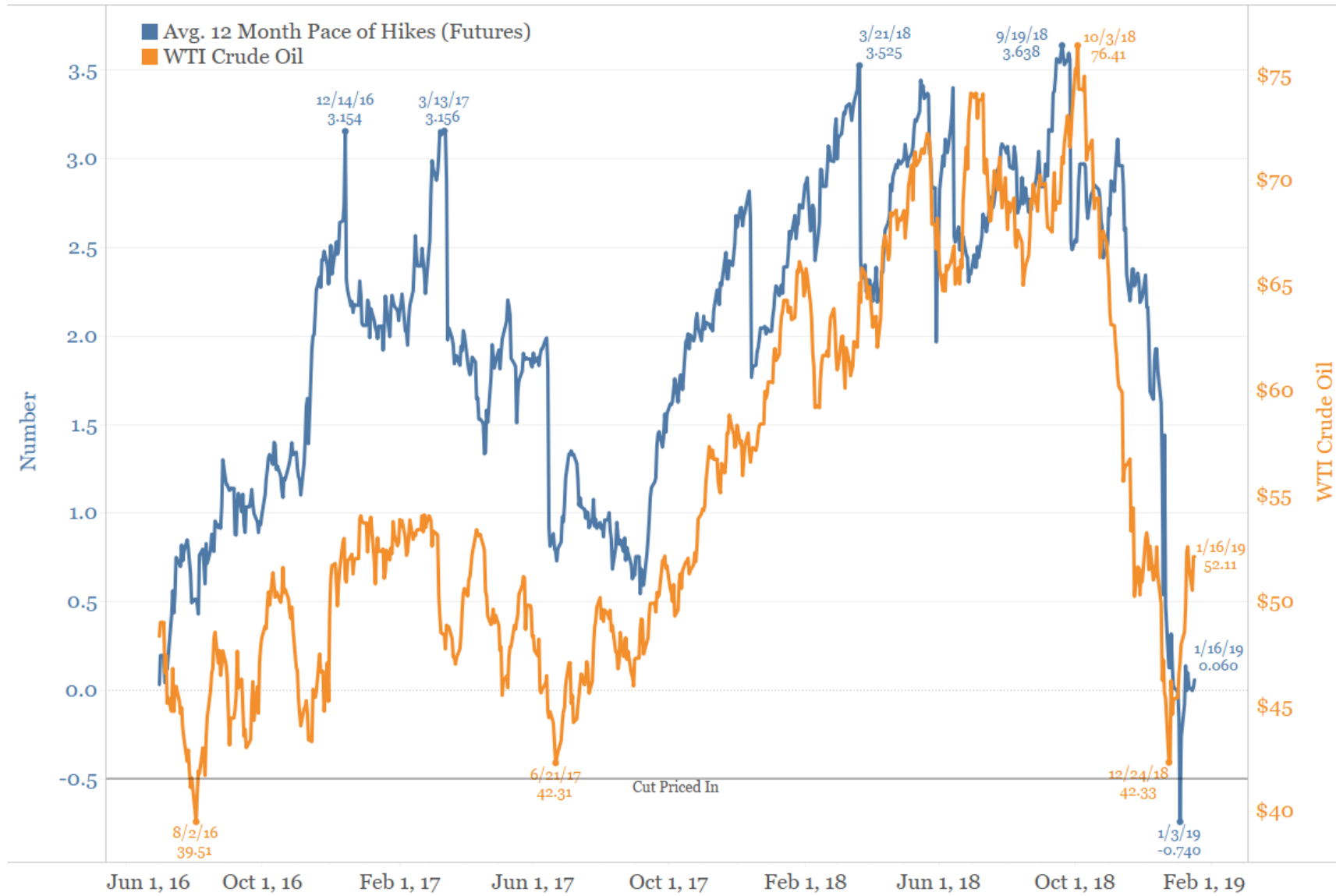
And particularly *with the muted inflation* readings that we've seen coming in, we will be *patient* as we watch to see how the economy evolves. But we're always prepared to shift the stance of policy and to shift it significantly if necessary in order to promote our statutory goals of the maximum implement and stable prices. – **Jay Powell, January 4, 2019**

But what I do know is that we will be prepared to *adjust policy quickly and flexibly*, and to use all of our tools to support the economy, should that be appropriate, to keep the expansion on track, to keep the labor markets strong and to keep — to keep inflation near 2 percent. – **Jay Powell, January 4, 2019**

And so we also said at the very beginning, I think in our original — certainly, the first policy normalization plans that I was involved in 2014, we said that we would be prepared to adjust our normalization plans as appropriate to achieve our goal. So if we ever came to the conclusion that any aspect of our normalization plans was — was somehow interfering with our achievement of our statutory goals, we wouldn't hesitate to change it, and that would include the balance sheet, certainly. – **Jay Powell, January 4, 2019**



Comparing Crude Oil and Fed Policy



Source: Bloomberg

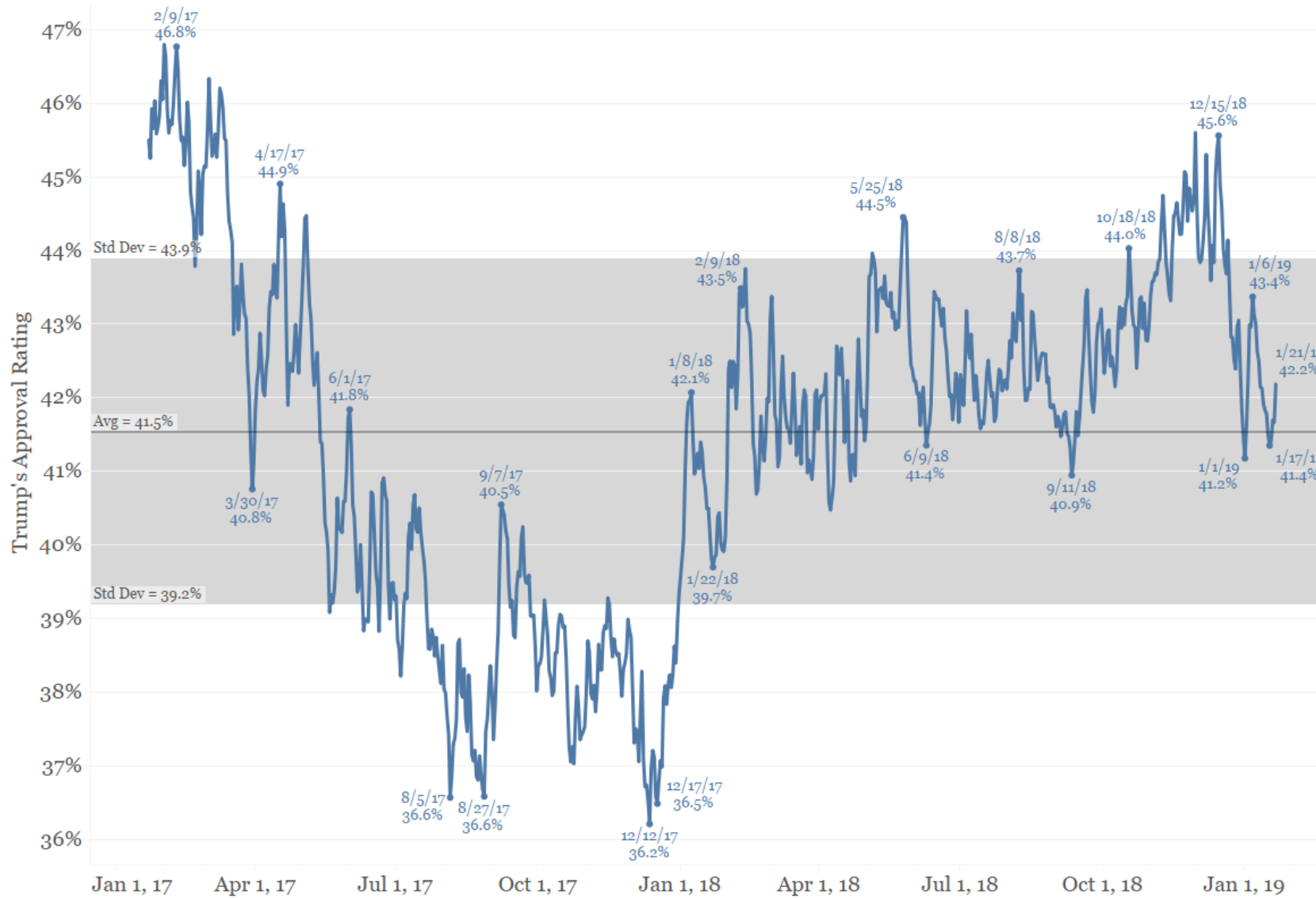
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The markets are fearful that Powell may be in the process of killing yet another recession. Consider what he has said recently:

- **October** – The funds rate is a long way from neutral (hawkish)
- **November** – The funds rate is just below the range of estimates (dovish)
- **December** – Balance sheet reductions are on “automatic pilot” (hawkish)
- **January 4** – The Fed can be patient and flexible (dovish)
- **January 10** – The balance sheet will be ‘substantially smaller’ (hawkish)

Would Powell please make up his mind and choose one? These changes of heart have played a large role in the market’s volatility over the past few months.

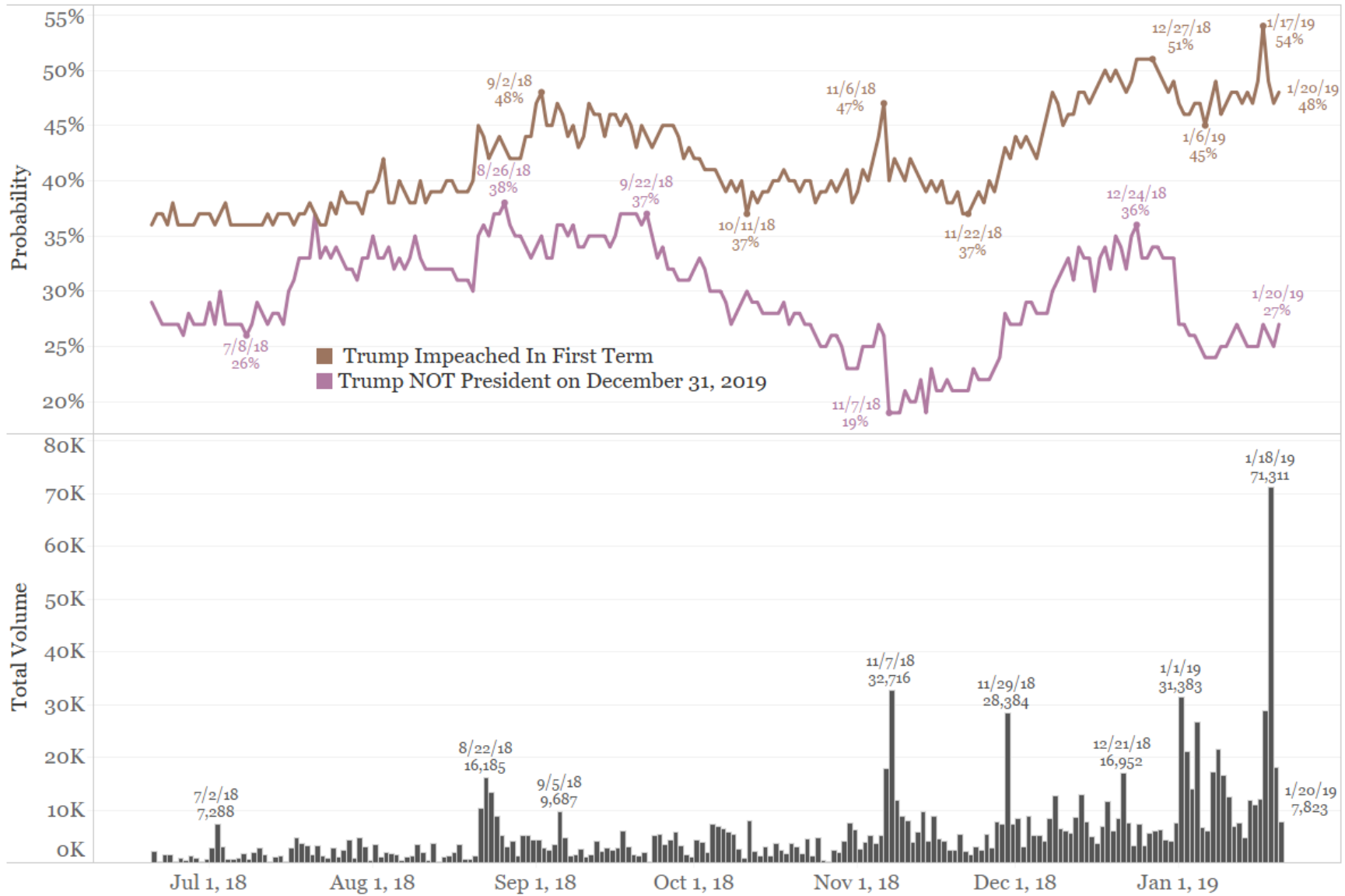
Rolling 5-Day Average Of All Trump's Approval Rating



Source: FiveThirtyEight Blog
<https://projects.fivethirtyeight.com/trump-approval-ratings/>

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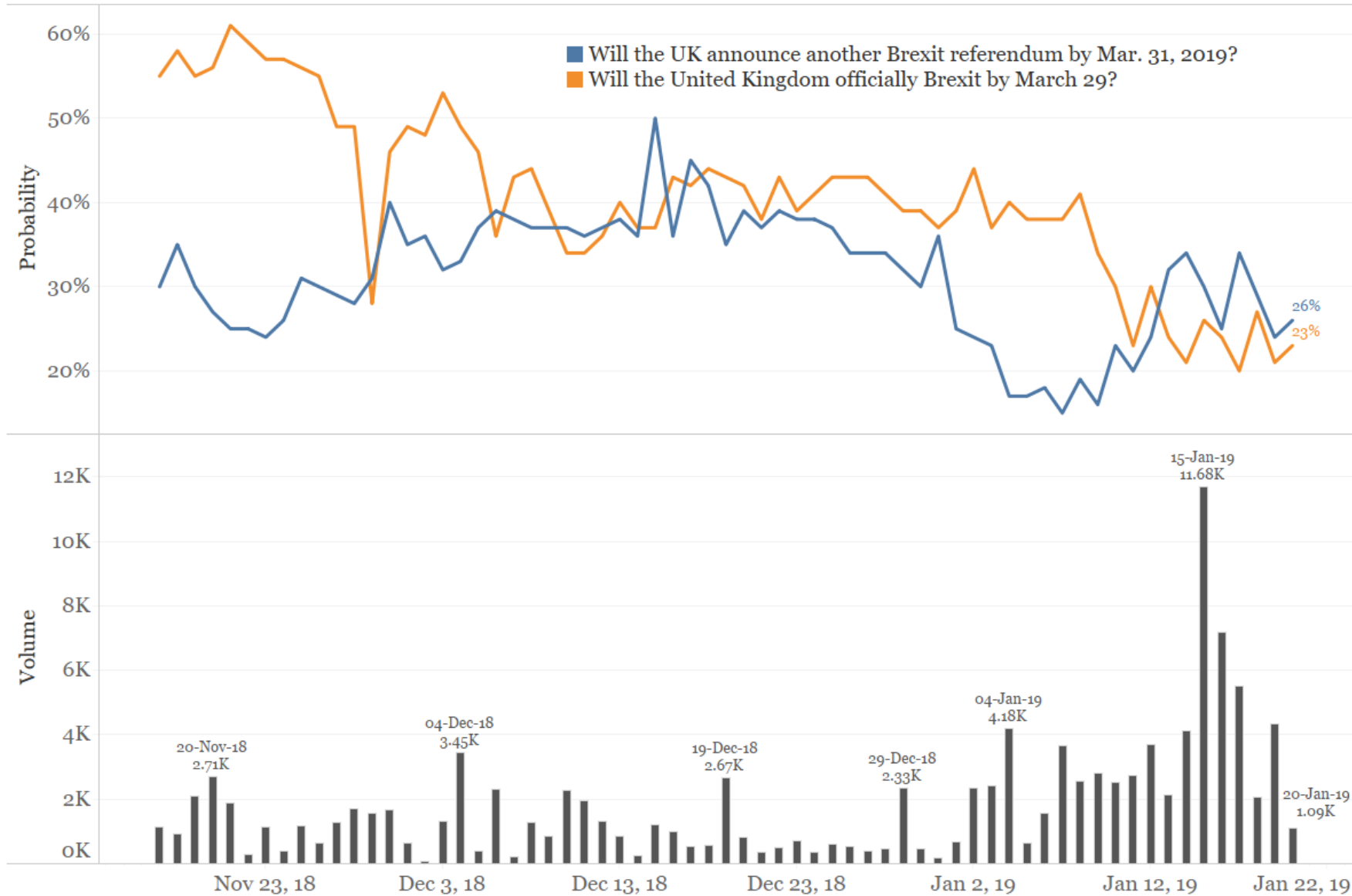
Predictit.com Betting Against Trump



Source: Predictit.com
<https://www.predictit.org/markets/detail/3537/Will-Donald-Trump-be-impeached-in-his-first-term>

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Brexit, What Will Happen?

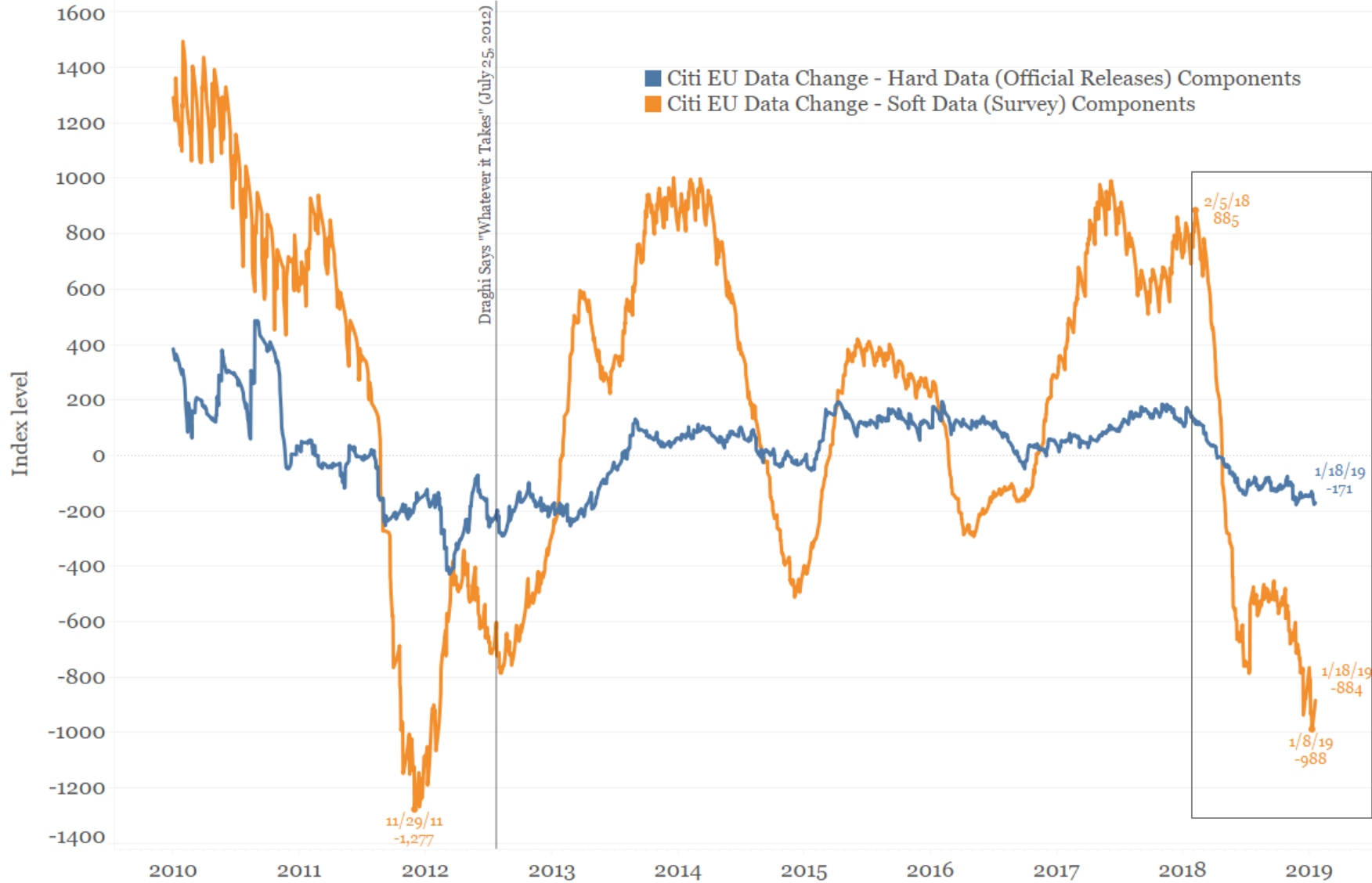


Source: predictit.com
<https://www.predictit.org/markets/detail/4672/Will-the-United-Kingdom-officially-exit-the-European-Union-by-March-29>
<https://www.predictit.org/markets/detail/5049/Will-the-UK-announce-another-Brexit-referendum-by-Mar-31,-2019>

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Economic Actors In The EU Are Very Worried

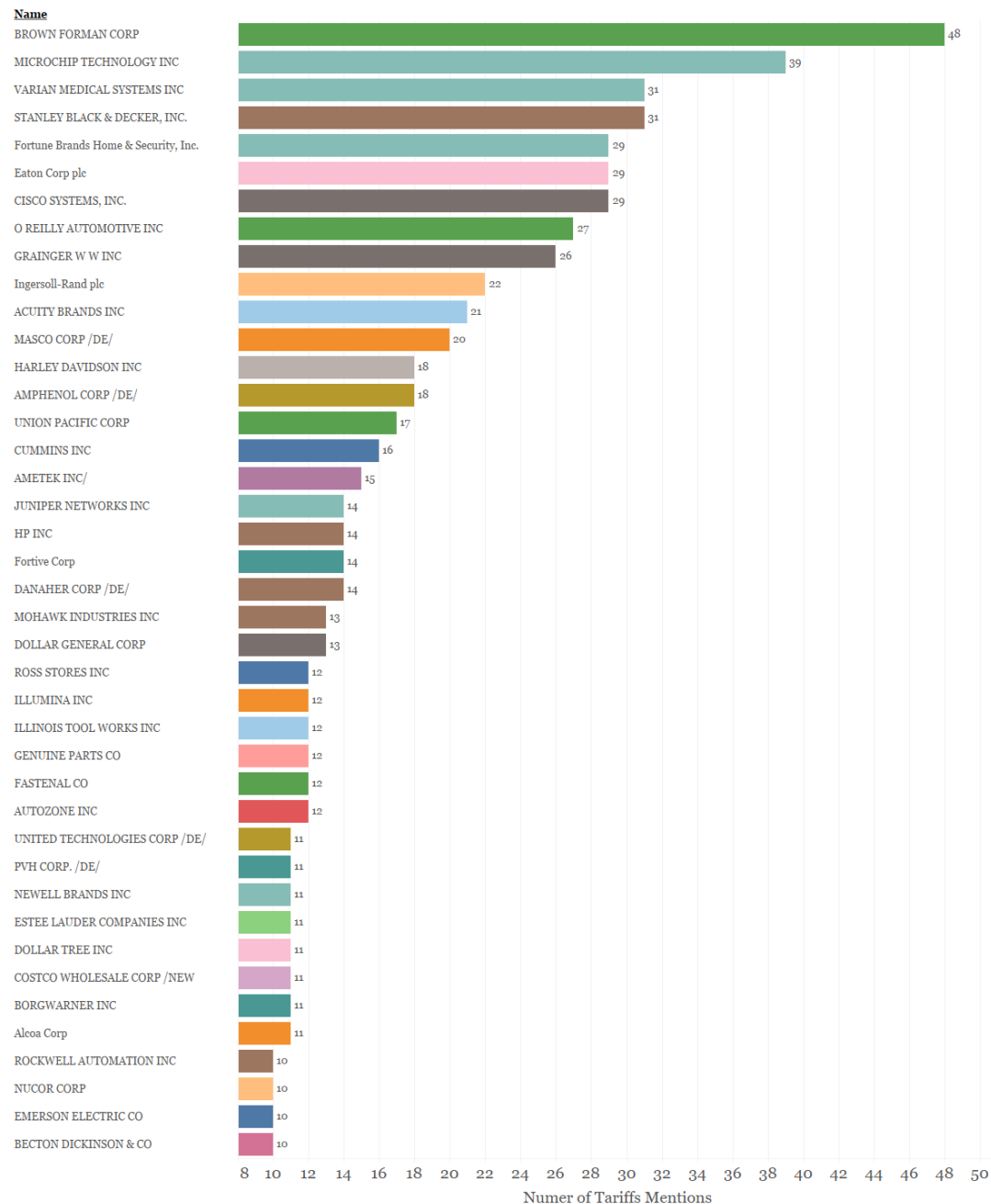
Citi EU Soft vs. Hard Data Change Indices



Data Source: Citigroup, Bloomberg

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What Companies Are Most Concerned About Tariffs?



Between October 1 and December 13, 481 S&P 500 companies held earnings calls, held an investor day or presented at investment conferences.

We found 189 (39%) companies mentioned tariffs at least once this quarter. Put another way, 292 (61%) of corporate presentations did not mention tariffs. Of the 189 that did mention tariffs:

91 of 189 (48%) presentations mentioned tariffs fewer than four times, signifying a passing reference to an issue that is not a problem.

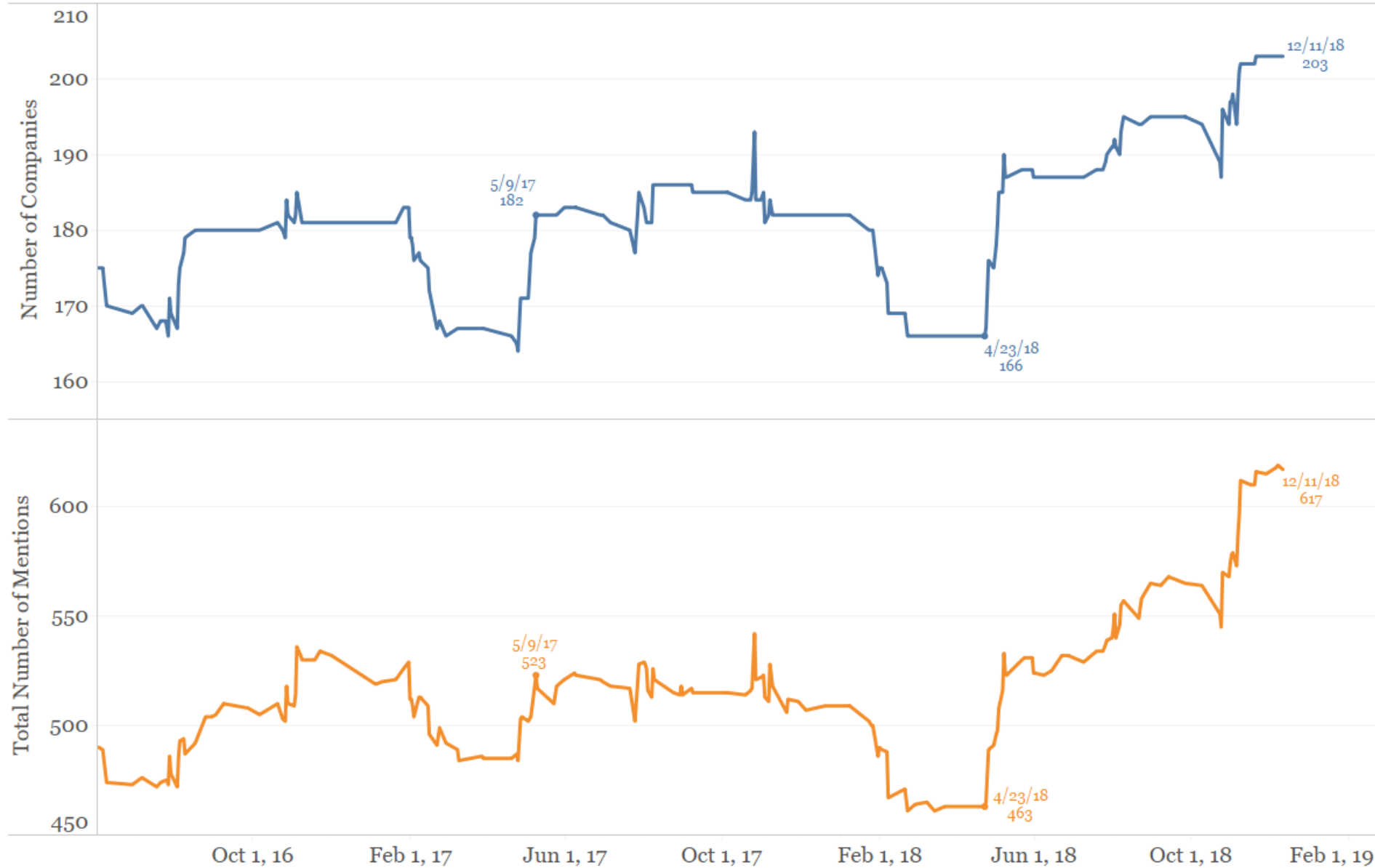
57 of 189 (30%) presentations mentioned tariffs between four and 10 times. This might not necessarily be a sign of serious concern, but this group is talking about tariffs.

41 of 189 (22%) presentations mentioned tariffs 10 times or more. This signifies an issue of serious concern that needs to be discussed. These companies are detailed in the next chart.

So only 41 of 481 companies (9%) this quarter seem to show serious concern over tariffs. 61% never mentioned them once!

60% Of S&P 500 Companies Do Not See China or Tariffs as a Risk

"China" and "Tariffs" Mentions in the Risk Factors Section of the 10-q
Rolling 90-Day Sum



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