

Bianco Research L.L.C.

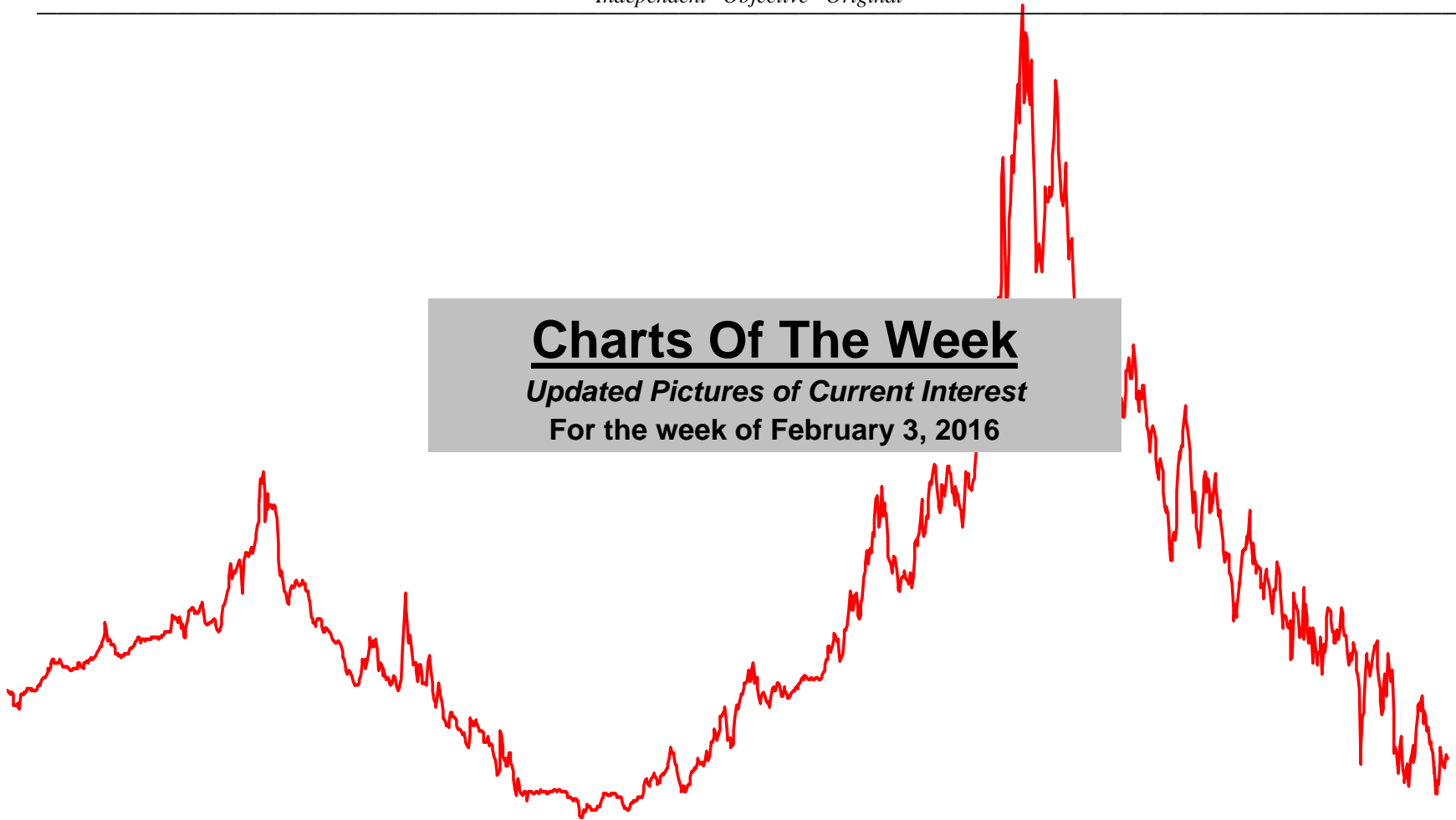
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Charts Of The Week

Updated Pictures of Current Interest

For the week of February 3, 2016



Long-Term Interest Rates - 1900 to 2015

Fed's Fischer Speaks

From Our [Newsclips/Daily Commentary](#)

[Bloomberg.com – Fischer Says Fed's Next Decision Unclear Amid Global Uncertainty](#)

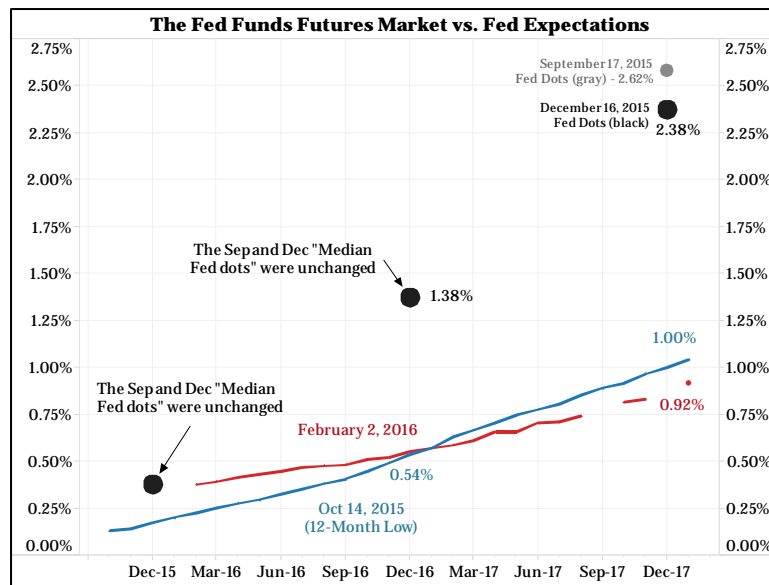
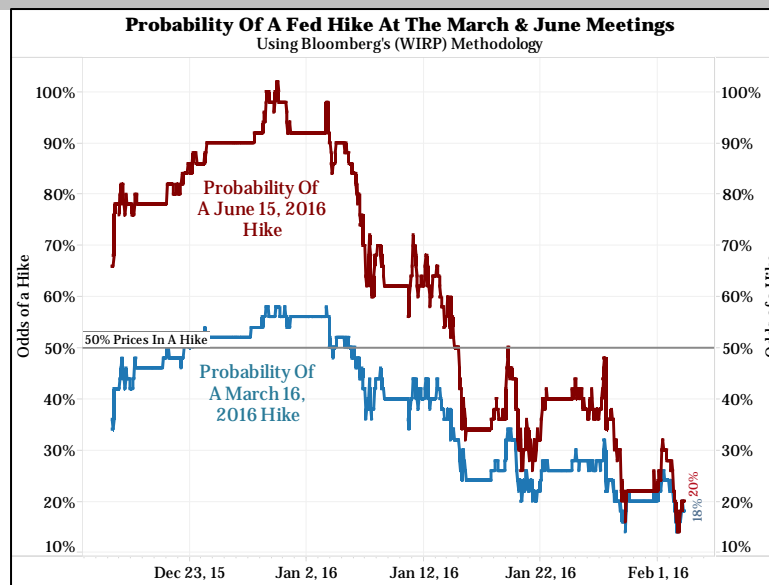
Tells audience not to ask what Fed will do at next meeting

Fed's No. 2 still confident inflation will rise to 2%

Federal Reserve Vice Chairman Stanley Fischer said it was too difficult to gauge the impact on the U.S. economy from recent turmoil in financial markets and uncertainty over China, leaving policy makers undecided about what to do next. "If these developments lead to a persistent tightening of financial conditions, they could signal a slowing in the global economy that could affect growth and inflation in the United States," Fischer told the Council on Foreign Relations in New York on Monday. "But we have seen similar periods of volatility in recent years that have left little permanent imprint on the economy." Fischer's remarks follow a tumultuous January in which expectations for additional interest-rate increases in 2016 plunged. When the Fed raised rates in December for the first time in almost a decade, officials gave projections suggesting they saw four increases this year. Investors currently foresee one, based on futures-market pricing.

Comment

Fischer may be uncertain about the Fed's next move but the market is not. Fed funds futures have priced in one rate hike this year, in December. As the top right chart shows, a hike at the March and/or June meetings is definitely off the table. As the lower right chart shows, the February 2 curve is even flatter than it was in October 2015. This suggests an even more gradual pace of hikes is being priced in.



Are Lower Crude Oil Prices A Credit Event?

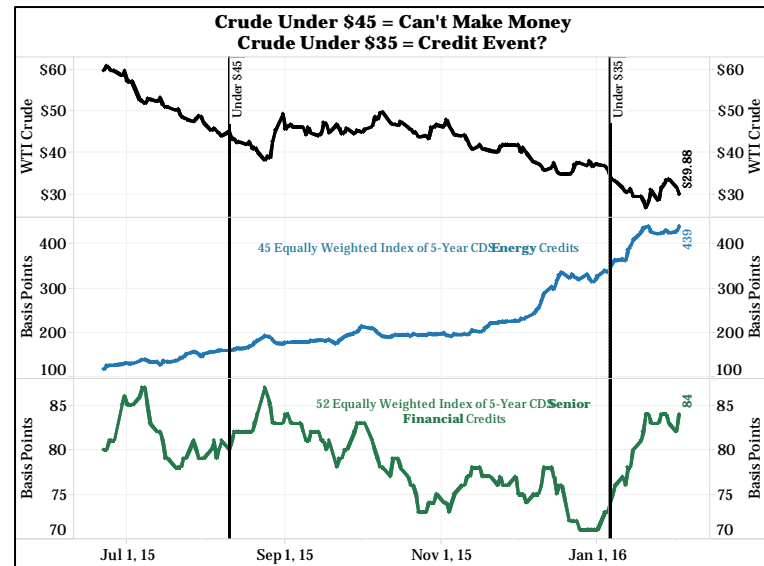
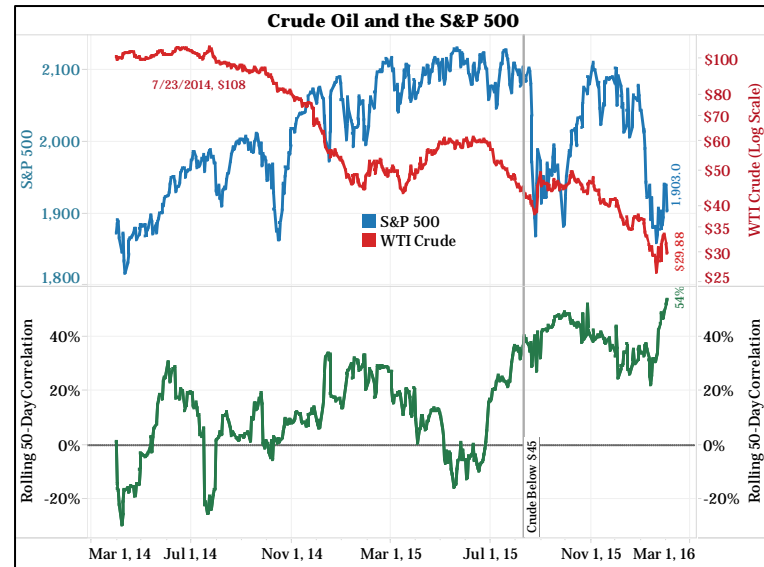
Think Advisors – [Bernice Napach: Why Are Stocks Falling in Sync With Oil Prices?](#)

Jim Bianco, president of Chicago-based Bianco Research, said, “Crude oil has become a credit event as opposed to a consumer event...a big credit event the financial sector has to deal with. ... Banks lent the energy patch billions of dollars and at \$31.50 per barrel of crude many are not getting their money back... At around \$30 or lower a barrel there will not be residual value left” for many oil companies.

Comment

The vertical line in the top right chart highlights August 10, 2015, the date when crude oil (red line) crossed below \$45. As crude continued to sink, its correlation to stocks (green line) rose.

Around the same time, an index of energy credit-default swaps (blue line below) started to soar. Once crude prices fell below \$35, an index of senior financial credit-default swaps (green line) started higher.



Are Lower Crude Oil Prices A Credit Event? - 2

Finally, year-to-date bank stocks (gold and purple) have performed worse than crude oil (black).

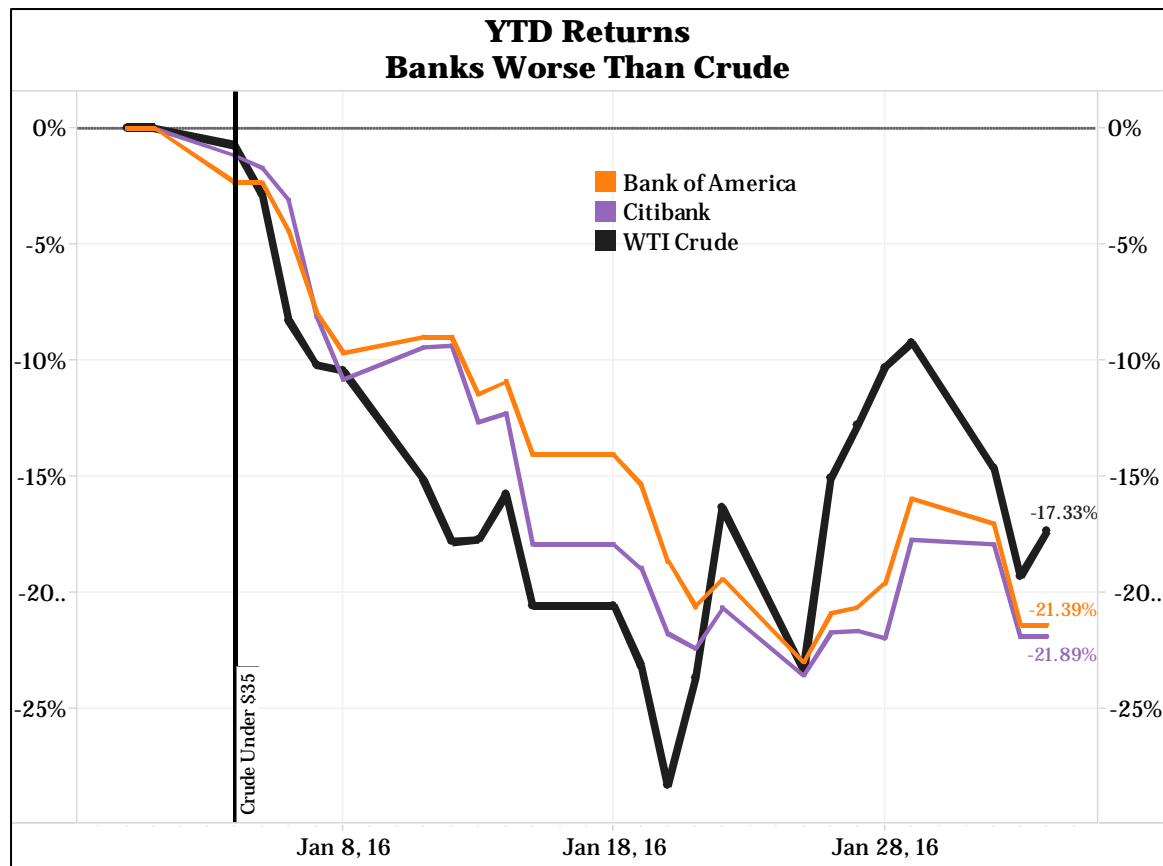
Conclusion

As the charts on this slide and previous slide show, stocks and credit started to move in response to crude oil once prices fell below \$45. They really noticed once crude fell below \$35.

We think the market is saying oil companies cannot make money under \$45. This is why we believe the oil forecasts for year-end are \$45. Producers are forecasting what they need, not necessarily what will happen.

The financial sector started to notice oil once it fell under \$35. Below this level it becomes a credit event for the financial system. Oil companies go from not being able to make money to not being able to pay loans. Further, we would argue that under \$30 energy loans have little-to-no residual value.

Low oil prices are now a credit event for the financial system. That is why so many markets seem to be correlated to oil prices at the moment. When/if crude prices rise above \$45, these correlations will cease to exist.



Still Bullish On Crude, Still Losing Buckets Of Money

From Our [Newsclips/Daily Commentary](#)

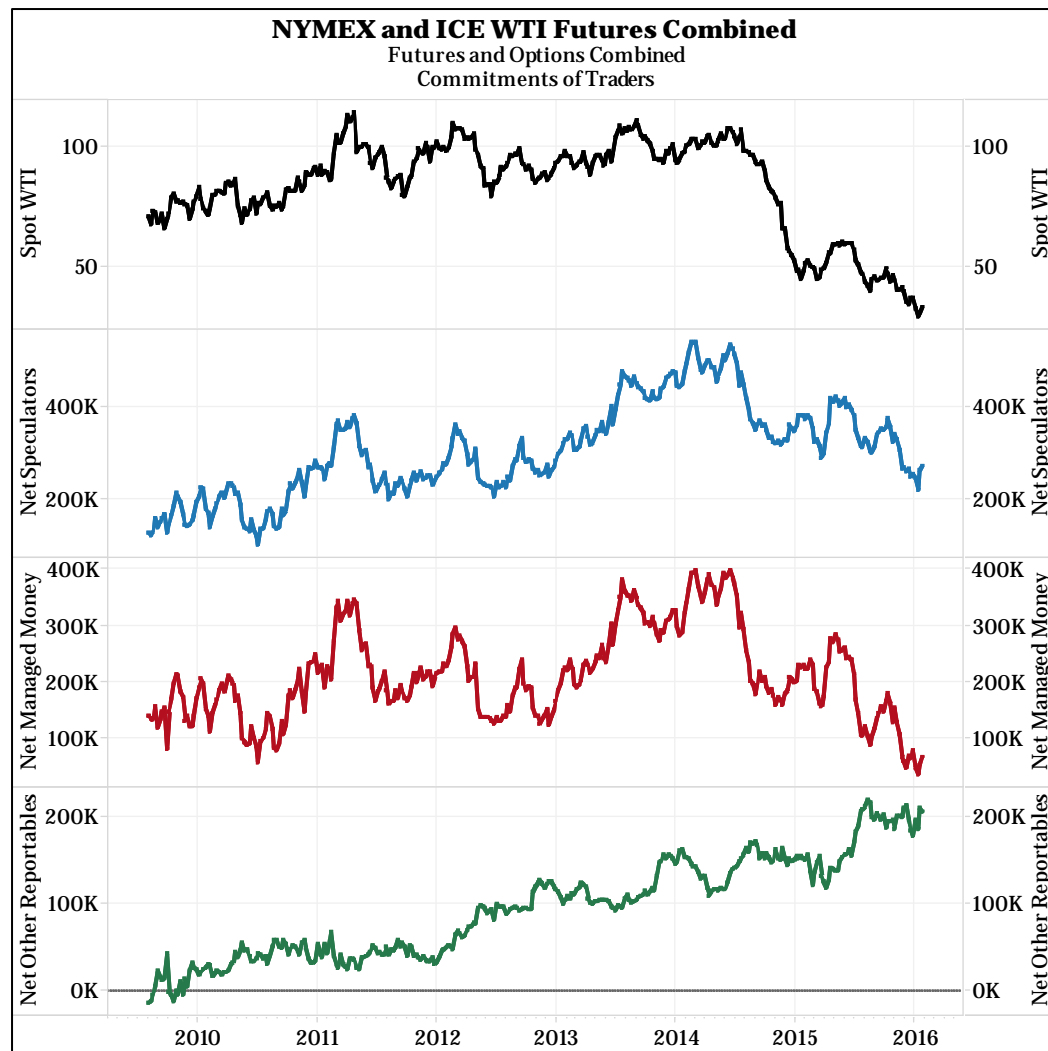
Bloomberg Business – Oil Bulls Jump in at Fastest Pace in Five Years on Rebound Hopes

Net-long position jumped 35% through Jan. 26, CFTC data show

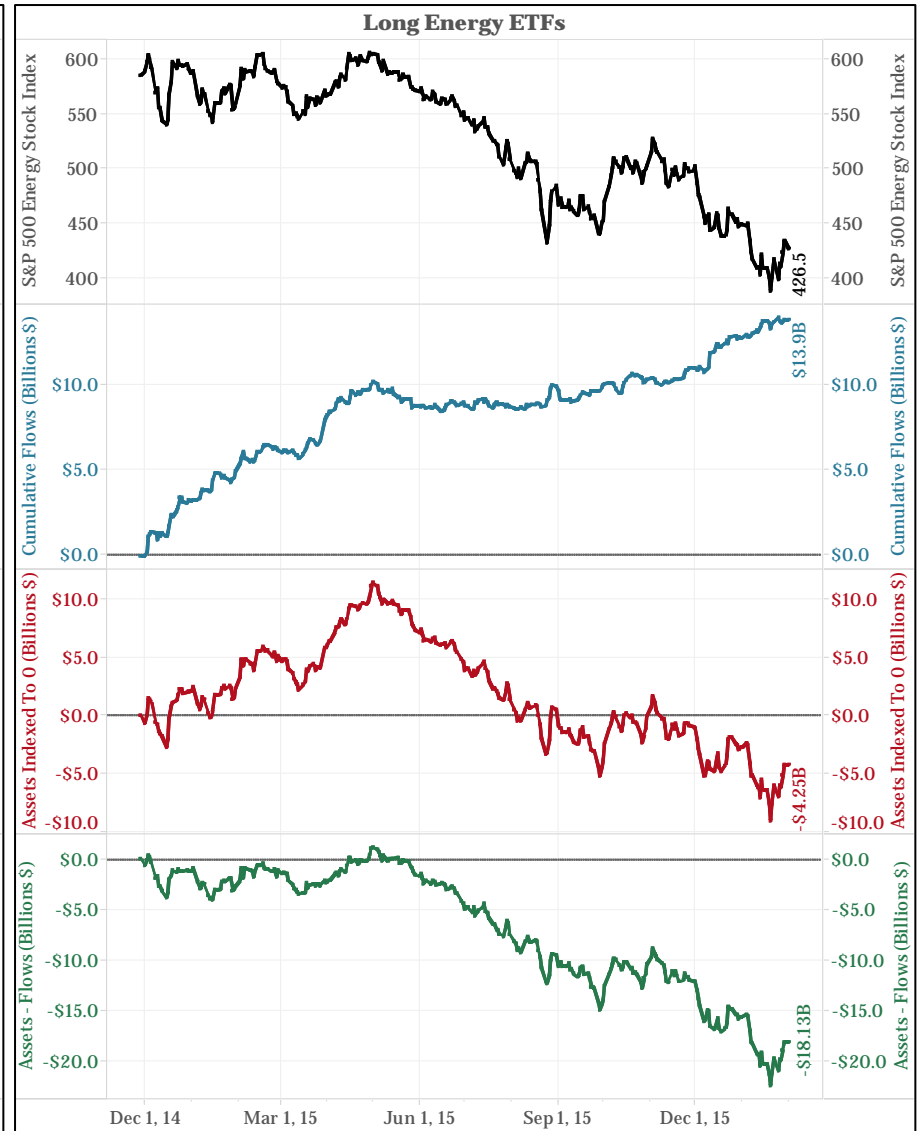
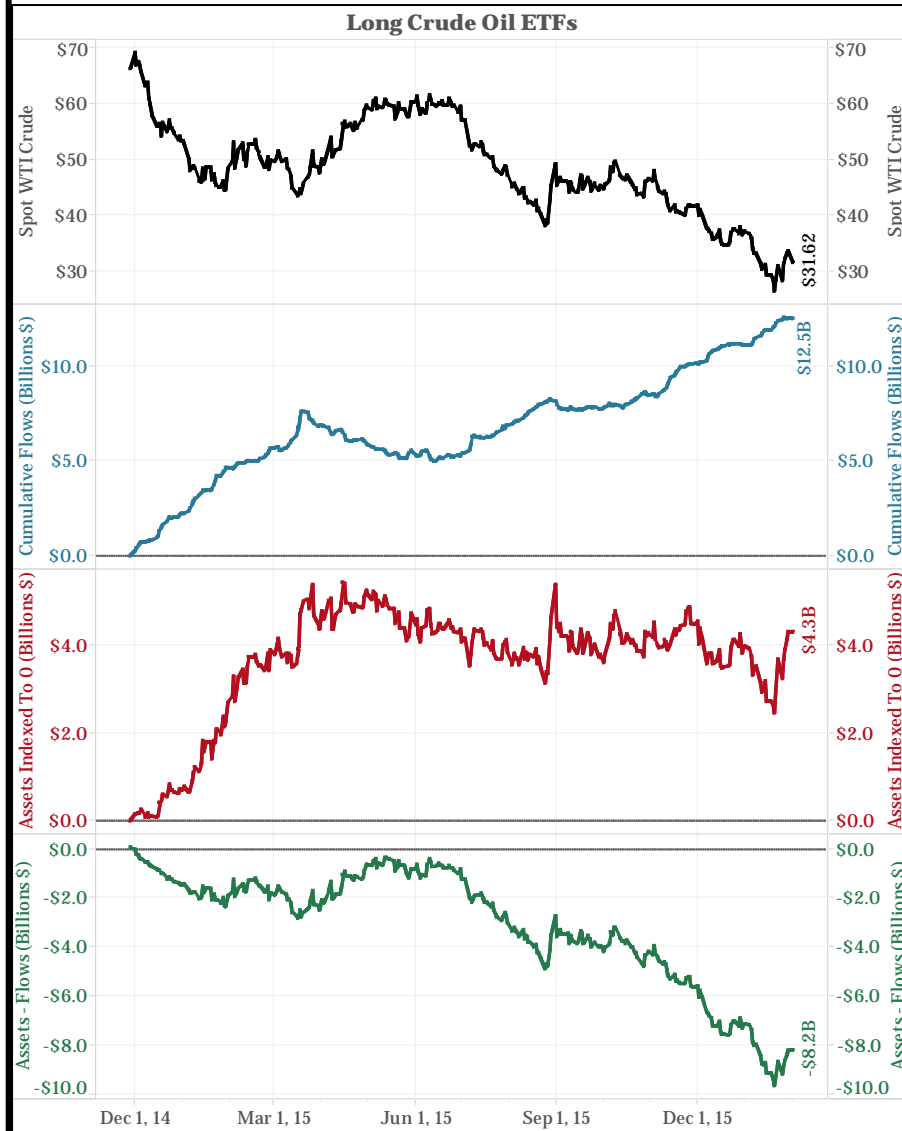
Hedge funds increased bullish oil bets by the most since 2010 as prices climbed to a three-week high. West Texas Intermediate crude futures capped a second weekly gain and have surged 27 percent from a 12-year low, spurred by speculation that Russia and OPEC may discuss oil production. OPEC delegates and Russia's Energy Minister Alexander Novak said no talks have been scheduled. Novak also said that cutting output is possible only if all crude-exporting nations are in agreement. "There's still a good amount of short-covering taking place after we fell to our lows," said John Kilduff, a partner at Again Capital LLC, a New York-based hedge fund that focuses on energy. "You've seen a lot of movement recently on rumors of a possible production cut." Speculators' net-long position in WTI increased 35 percent in the week ended Jan. 26 to 110,432 contracts of futures and options, the biggest percentage gain since October 2010, data from the U.S. Commodity Futures Trading Commission show. Longs, or wagers on rising prices, increased by 23,031 to 289,181 and short positions dropped by 5,444 contracts to 178,749.

Comment

As the story above points out and the chart below shows, hedge funds increased their net long position in crude oil last week to the largest since 2010.



Still Bullish On Crude, Still Losing Buckets Of Money - 2



Alphabet (Google) Tops Apple In Market Cap

From Our [Newsclips/Daily Commentary](#)

Yahoo Finance – [Google-owner Alphabet vaults past Apple as most valuable firm](#)

Google-parent Alphabet snatched Apple's crown as the world's most valuable firm based on the value of shares that leapt with better-than-expected earnings. At the official close of trade, Alphabet was worth \$530.1 billion based on its share value, compared to \$534.7 billion for Apple, but shares in the Internet search colossus soared in after-hours trading to reach \$791 shortly before 0400 GMT. If those gains hold in official trading when the Nasdaq opens in New York City on Tuesday, Alphabet would officially overtake Apple as the world's biggest company by market value.

Comment

So is this good news for Alphabet? According to a study by Robert D. Arnott and Lilian J. Wu of Research Affiliates, the answer is no. As they wrote:

When you are #1, you have a bright bull's-eye painted on your back. Governments and pundits are gunning for you. Competitors and resentful customers are gunning for you. Indeed, in a world of fierce competition and serial witch hunts in the halls of government, that target is probably painted on your front and sides too. In a world that generally roots for the underdog, hardly anyone outside of your own enterprise is cheering for you to rise from world-beating success to still-loftier success. For investors, Top Dog status — the #1 company, by market capitalization, in each sector or market — is disarmingly unattractive. We find a statistically significant tendency for top companies in each sector to underperform both the overall sector and the stock market as a whole.

So congratulations to Alphabet for making it to number 1. History suggests investors should consider selling it.



Peak Capitalizations And S&P 500 Weighting								
In \$Billions								
Rank	Stock	Date	At The Peak			2/1/2016		From Cap Peak
			Capitalization	Date	% of S&P 500	% of S&P 500	Capitalization	
1	Google	1-Feb-16	\$570.00	1-Feb-16	3.23%	1.99%	\$570.00	0.0%
2	Apple	23-Feb-15	\$774.69	18-Sep-12	4.88%	3.73%	\$534.66	-31.0%
3	Microsoft	27-Dec-99	\$613.26	14-Nov-02	3.70%	1.81%	\$432.72	-29.4%
4	Facebook	1-Feb-16	\$327.58	1-Feb-16	1.86%	1.16%	\$327.58	0.0%
5	Berkshire Hathaway	18-Dec-14	\$376.46	22-Oct-08	2.25%	1.94%	\$318.59	-15.4%
6	Exxon Mobil	18-Oct-07	\$527.17	21-Nov-08	5.34%	2.02%	\$317.59	-39.8%
7	Johnson & Johnson	24-Sep-14	\$306.40	8-Oct-02	2.39%	1.53%	\$288.79	-5.7%
8	Amazon	29-Dec-15	\$325.31	28-Jan-16	1.73%	0.90%	\$270.64	-16.8%
9	GE	28-Aug-00	\$593.93	6-Oct-00	4.79%	1.31%	\$270.30	-54.5%
10	Wells Fargo	22-Jul-15	\$301.33	12-May-10	1.61%	1.47%	\$255.08	-15.3%
11	AT&T	26-Sep-07	\$261.22	3-Dec-08	2.18%	0.93%	\$222.58	-14.8%
12	Procter & Gamble	26-Dec-14	\$252.54	21-Nov-08	2.61%	1.24%	\$219.39	-13.1%
13	JP Morgan	22-Jul-15	\$260.07	10-Oct-08	2.01%	1.10%	\$216.67	-16.7%
14	Wal-Mart	27-Dec-99	\$309.26	16-Oct-02	3.20%	1.50%	\$216.13	-30.1%
15	Verizon	29-Jul-14	\$215.43	20-Sep-01	1.63%	1.04%	\$206.54	-4.1%
16	Coca-Cola	14-Jul-98	\$217.27	9-Oct-02	1.81%	0.99%	\$187.01	-13.9%
17	Pfizer	11-Jul-00	\$308.43	26-Jun-03	3.17%	1.08%	\$186.24	-39.6%
18	Chevron	24-Jul-14	\$256.71	11-Dec-08	2.05%	1.06%	\$160.52	-37.5%
19	Oracle	1-Sep-00	\$260.73	7-Sep-00	1.96%	1.01%	\$152.59	-41.5%
20	Intel	31-Aug-00	\$502.71	23-Aug-00	3.81%	0.87%	\$145.44	-71.1%
21	Bank of America	4-Oct-06	\$248.11	8-Aug-06	2.01%	0.87%	\$145.36	-41.4%
22	Merck	29-Nov-00	\$218.79	20-Dec-00	1.93%	0.94%	\$141.77	-35.2%
23	Citigroup	5-Feb-01	\$283.35	14-Jul-03	2.66%	0.78%	\$126.55	-55.3%
24	IBM	13-Jul-99	\$249.43	12-Dec-01	2.06%	0.83%	\$121.10	-51.4%
25	Cisco	27-Mar-00	\$551.63	26-Jul-00	3.85%	0.74%	\$119.19	-78.4%
					25 Stock Total		\$5,583.02	
S&P 500			20-Jul-15	\$19,473.51	NA	NA	\$15,820.17	-19.8%
					Top 25 Percentage Of The S&P 500		35.74%	

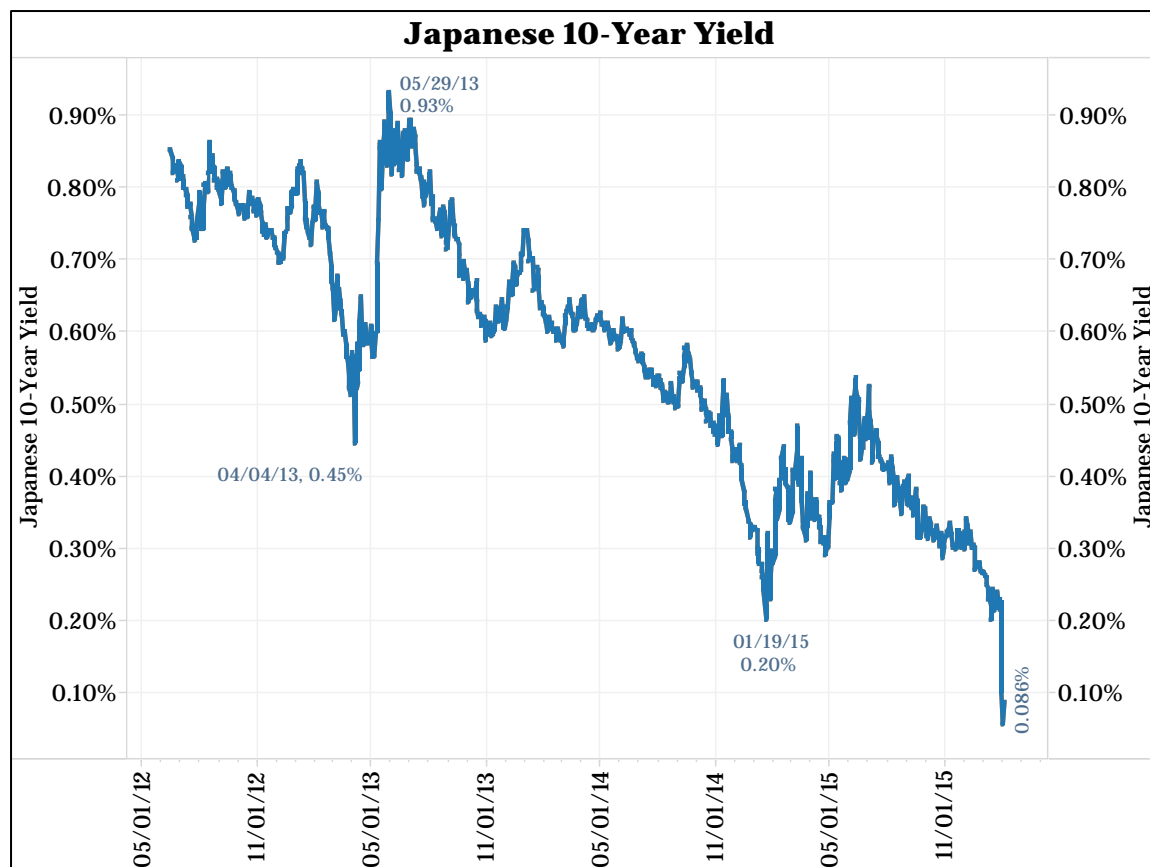
Japan Has More Tools To Drive Rates Even Lower

[Bloomberg.com](#) – [Japan's Central Bank Isn't Out of Options Yet, Abe Aide Says](#)

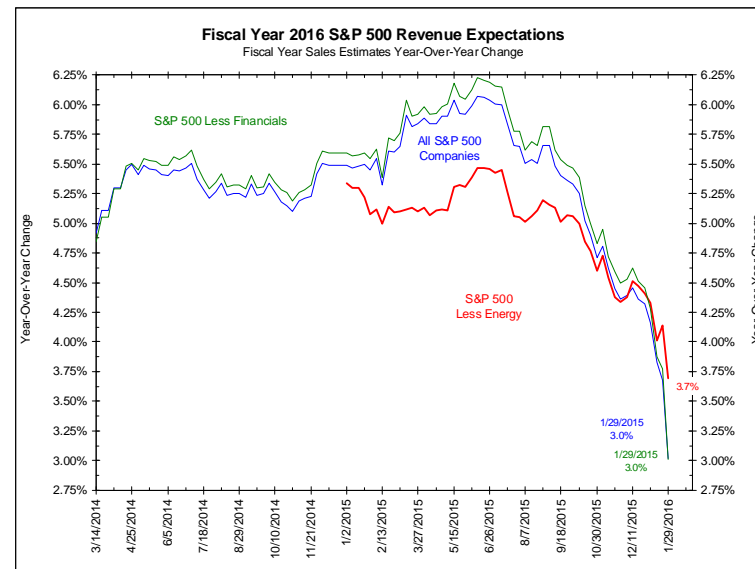
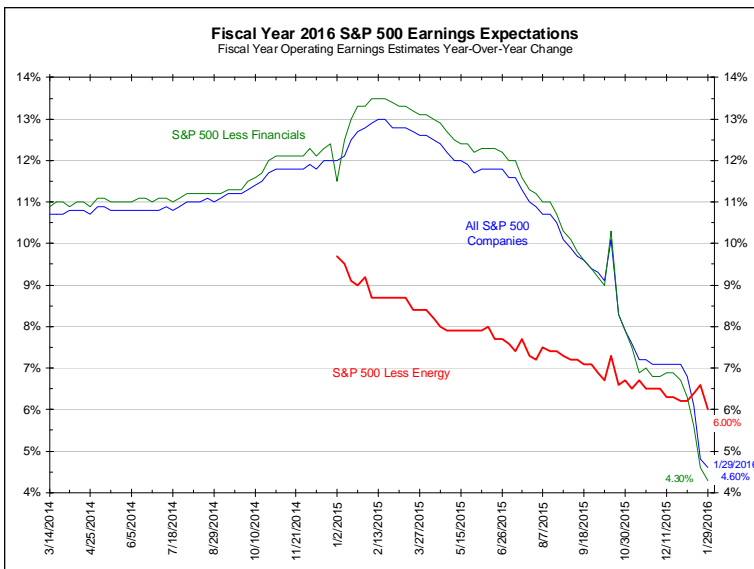
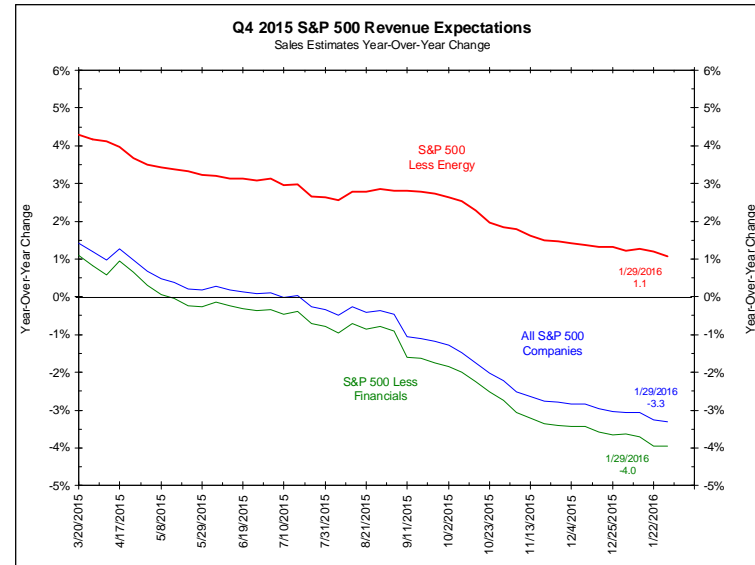
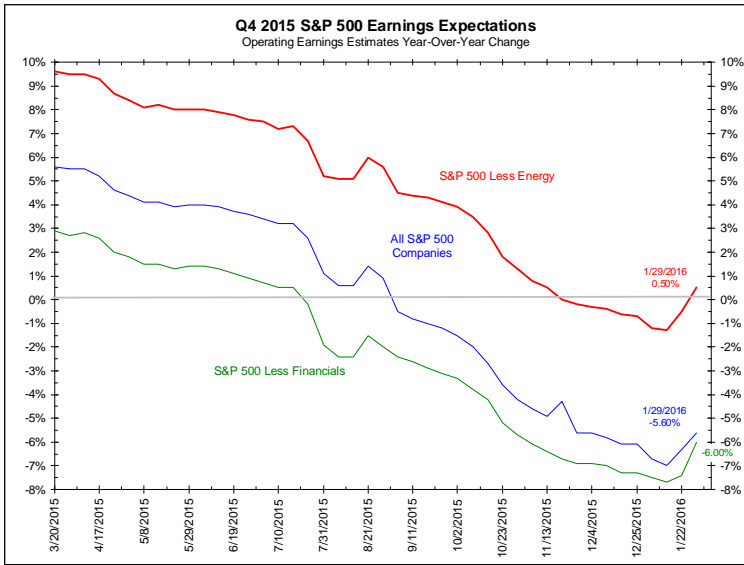
Negative interest rates 'not the last resort' for BOJ: Seko

Move won't affect depositors if banks act properly: Seko

The Bank of Japan isn't running out of policy options in its attempt to reinvigorate the economy, a senior government official said Tuesday, days after the central bank surprised investors by adopting a negative interest-rate strategy to spur banks to lend more. "I don't think that's the case," Deputy Chief Cabinet Secretary Hiroshige Seko said when asked in an interview whether BOJ policy making was nearing its limits. "There are other central banks that have introduced lower negative interest rates," he said. "This is not the last resort." BOJ Governor Haruhiko Kuroda's decision to penalize a portion of banks' reserves held at the central bank is a strategy once shunned by central bankers, yet which recently has been adopted by Sweden, Denmark, Switzerland and the European Central Bank. The strategy will complement the record asset-purchase program that has expanded the central bank's balance sheet to three quarters the size of the economy.



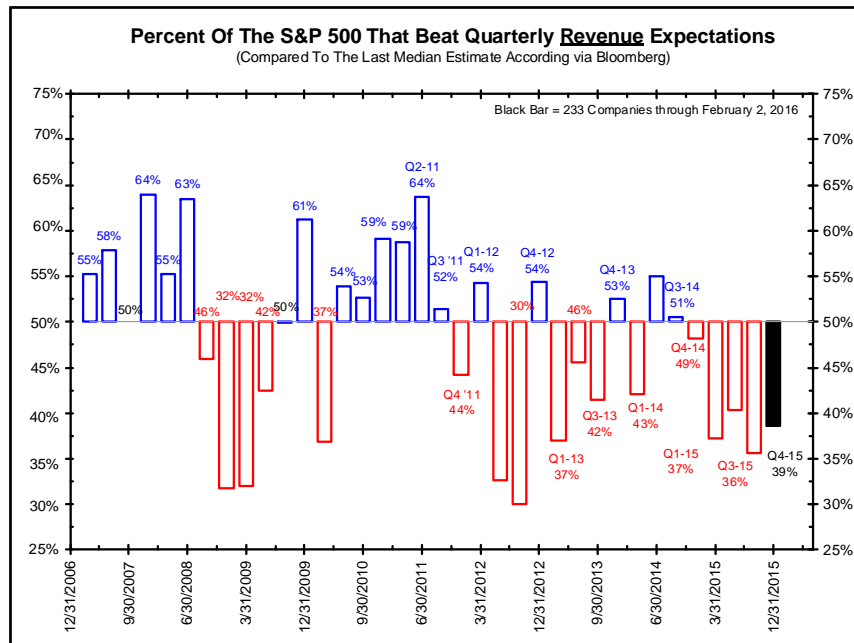
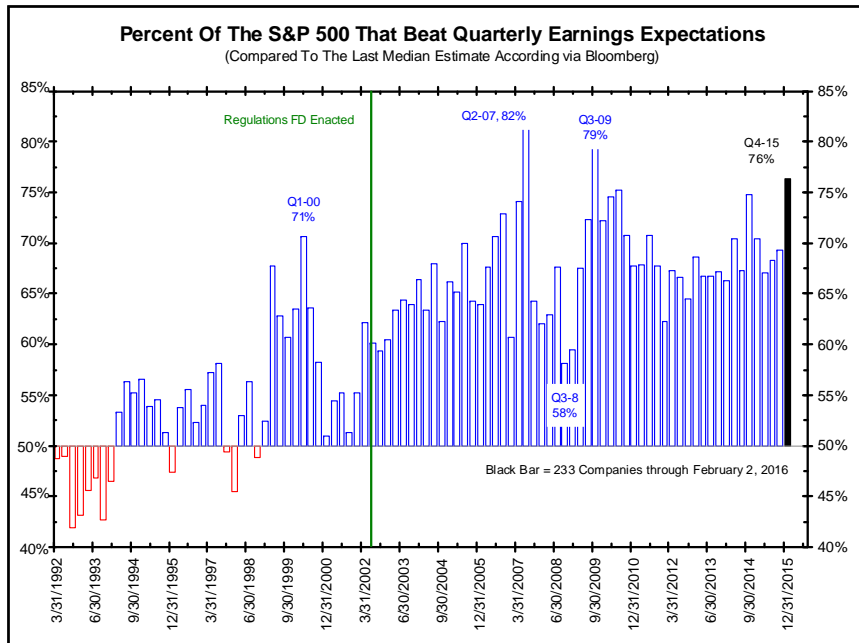
Earnings Expectations



Beat Rates

Fact Set – Above Average Drop in S&P 500 EPS Estimate for Q1'16 to Date, as Energy EPS Falls 54%

During the month of January, analysts lowered earnings estimates for companies in the S&P 500 for the quarter. The Q1 bottom-up EPS estimate (which is an aggregation of the estimates for all the companies in the index) dropped by 4.7% (to \$27.76 from \$29.14) during this period. How significant is a 4.7% decline in the bottom-up EPS estimate during the first month of a quarter? How does this decrease compare to recent quarters? During the past year, (four quarters) the average decline in the bottom-up EPS estimate during the first month of a quarter has been 3.3%. During the past five years (20 quarters), the average decline in the bottom-up EPS estimate during the first month of a quarter has been 1.9%. During the past 10 years, (40 quarters) the average decline in the bottom-up EPS estimate during the first month of a quarter has been 2.2%



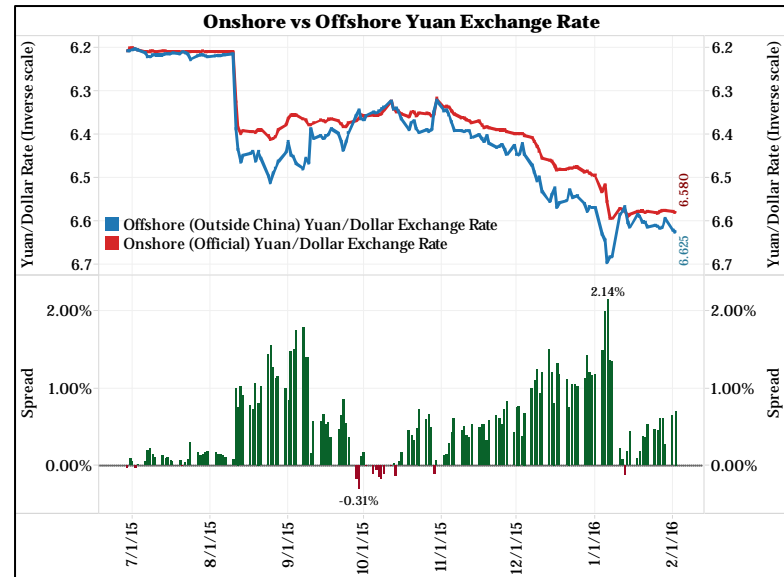
Still Trying To Stabilize The Yuan

[The Financial Times – China targets offshore renminbi short selling with new reserve ratio](#)

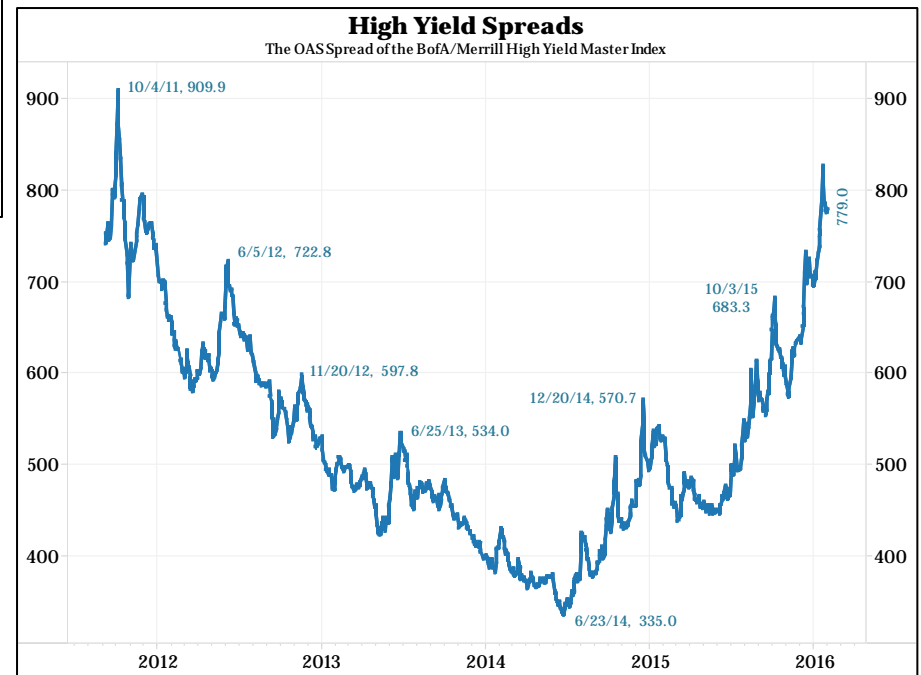
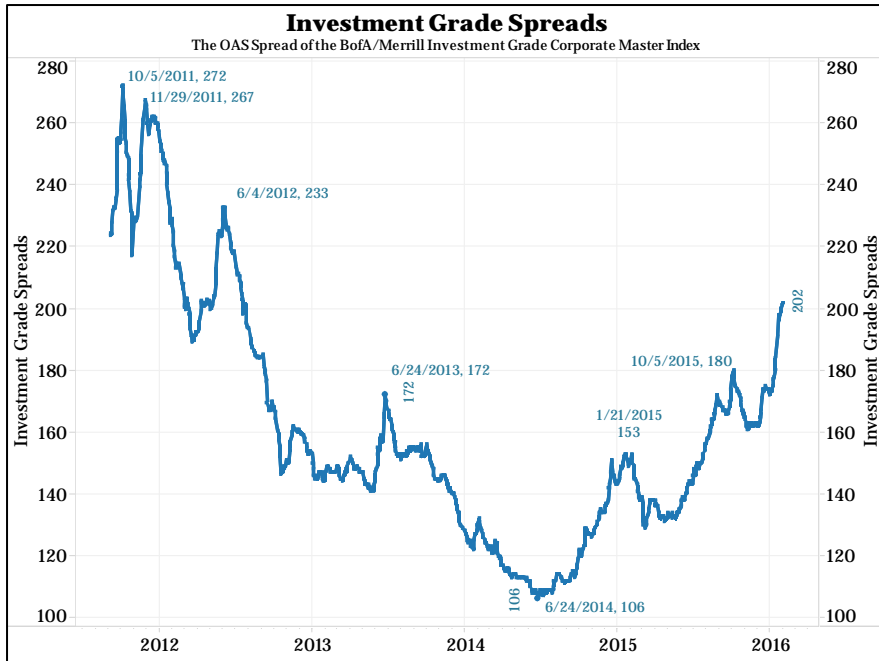
China is to force some banks to set aside a portion of their offshore renminbi deposits as reserves in its latest bid to squeeze liquidity and stymie speculation on depreciation of the currency. It is the first time China has imposed a reserve requirement for offshore renminbi. Domestic large banks are obliged to hold 17.5 per cent of onshore renminbi deposits as reserves. The move, announced on Monday, marks an escalation of efforts by the People's Bank of China to discourage capital outflow and curb renminbi weakness in both the onshore and offshore markets. The spread between onshore and offshore renminbi widened to a record early this month before the PBoC intervened in the offshore — or CNH — market in Hong Kong to narrow the gap. The onshore renminbi has fallen 2.7 per cent against the dollar since December.

Comment

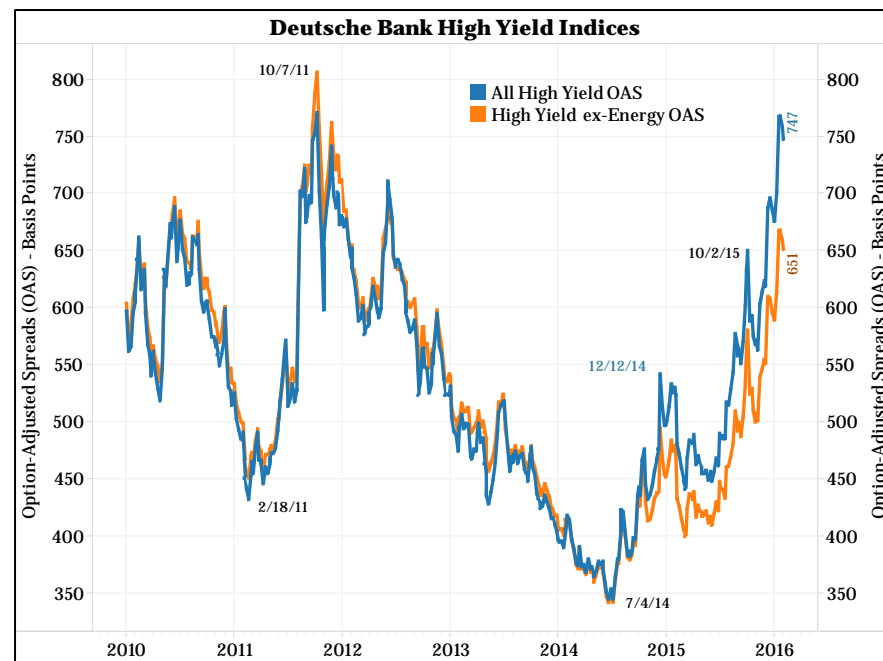
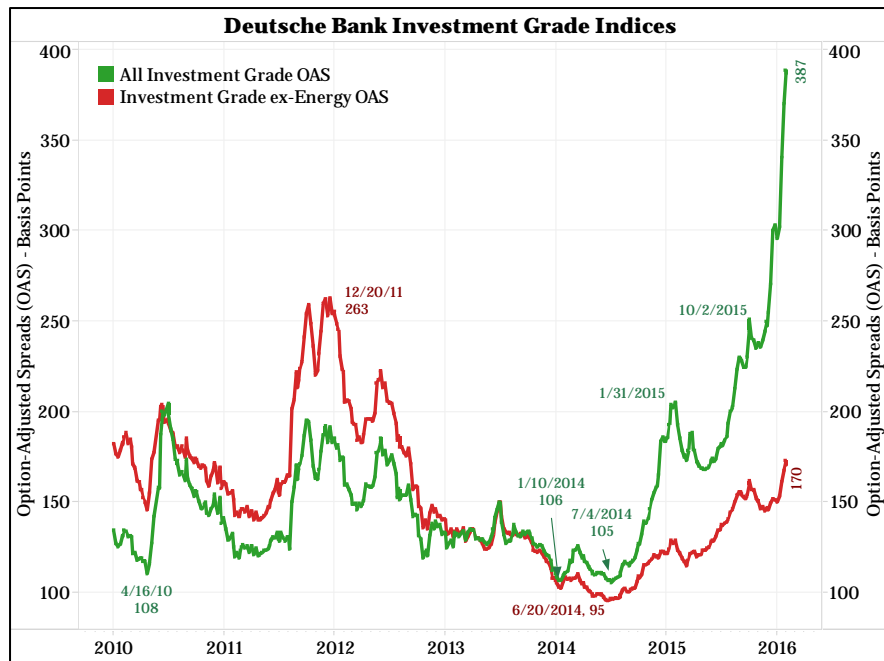
As we [detailed last week](#), the Chinese government/PBoC are stabilizing the yuan (both official and unofficial) as shown in the chart to the right. That does not mean all is well. The level of stress still exists as shown in the Hong Kong dollar chart below. Chinese officials cannot control the Hong Kong dollar and its decline is a signal of investor concern about mainland China.



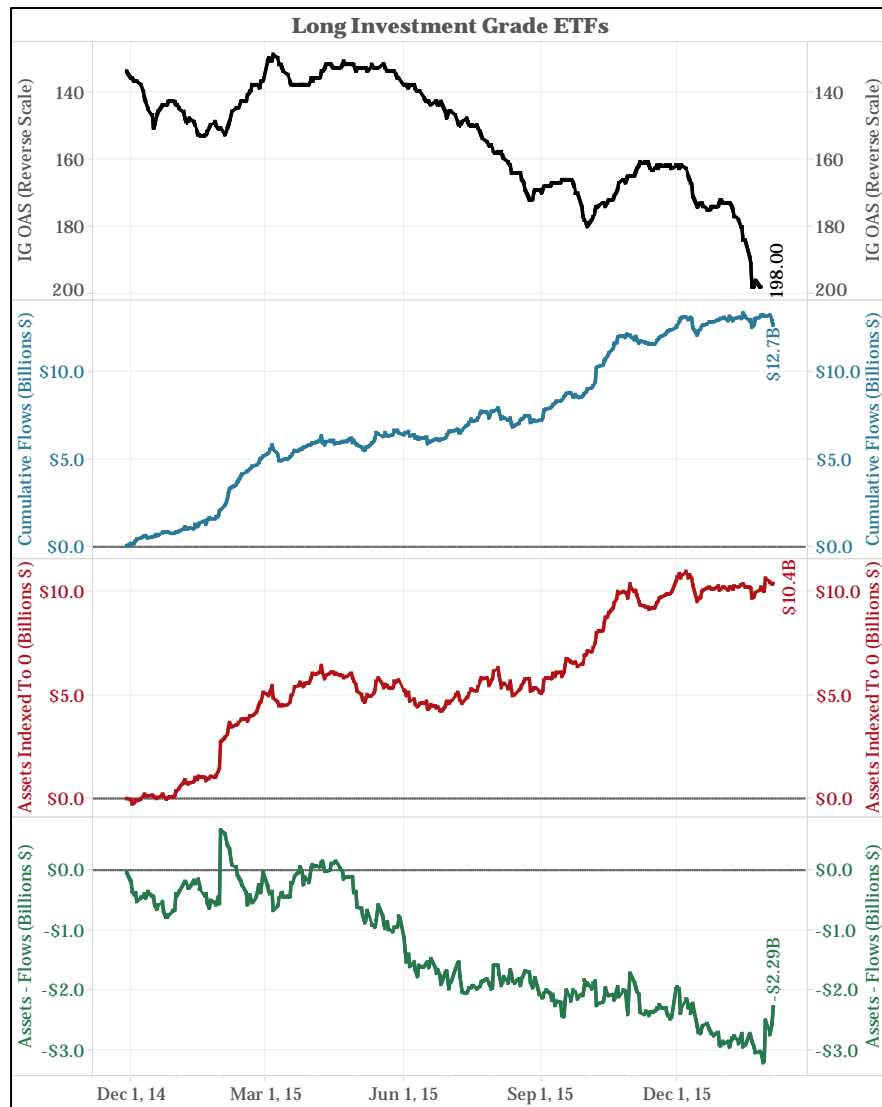
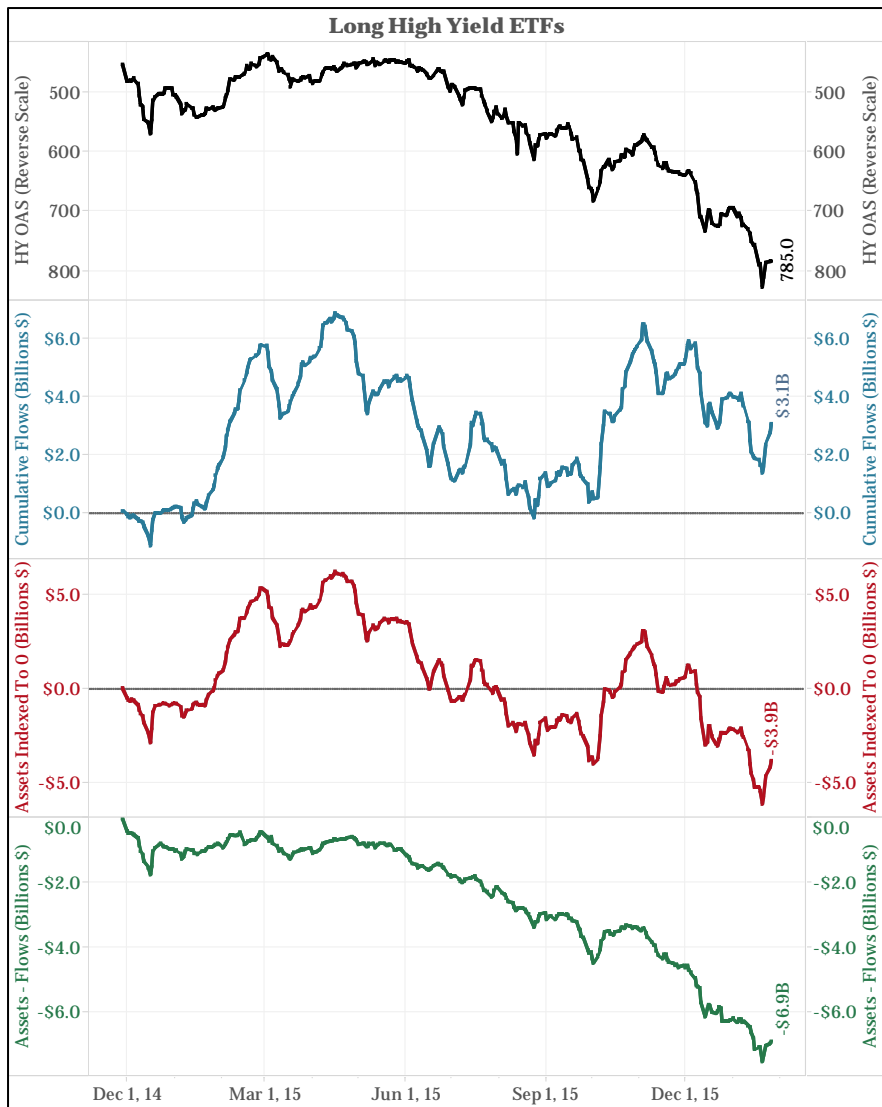
Credit Spreads



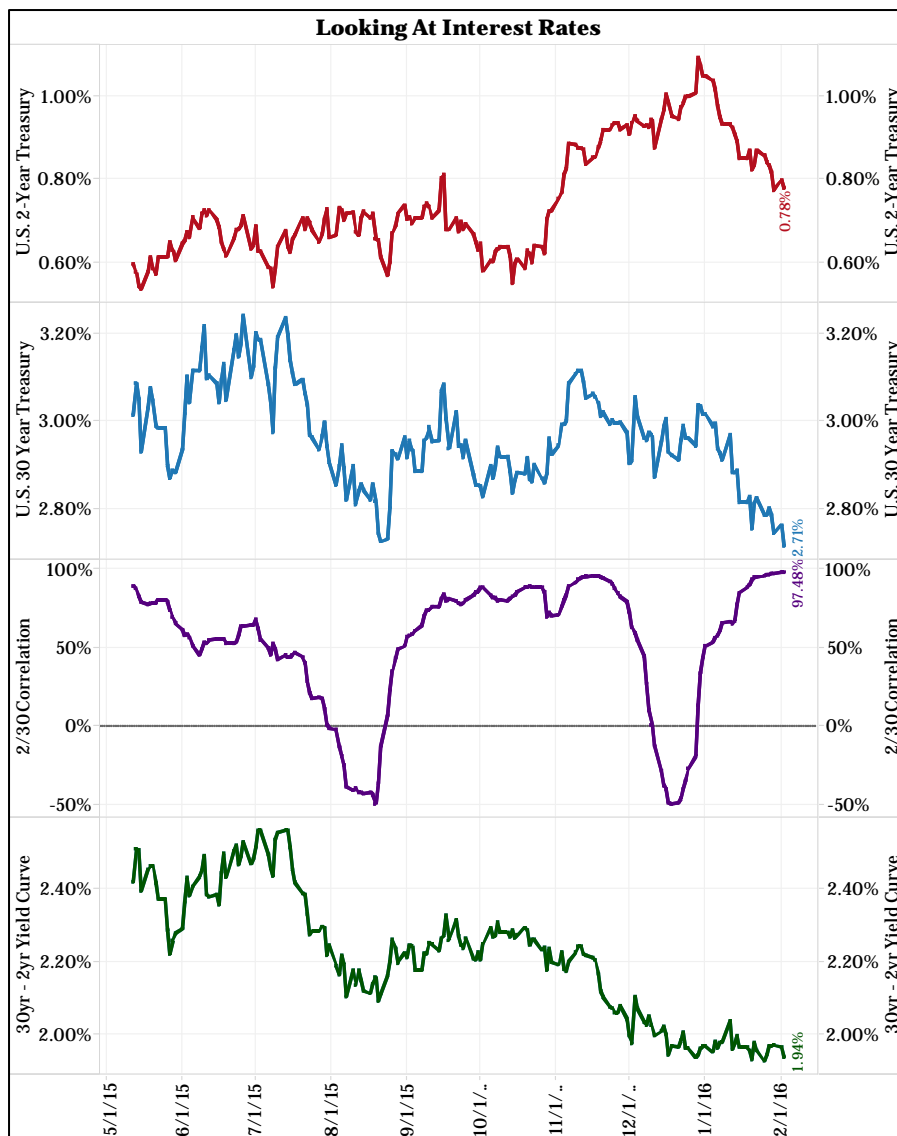
Credit Spreads ex Energy



High Yield and Investment Grade ETFs

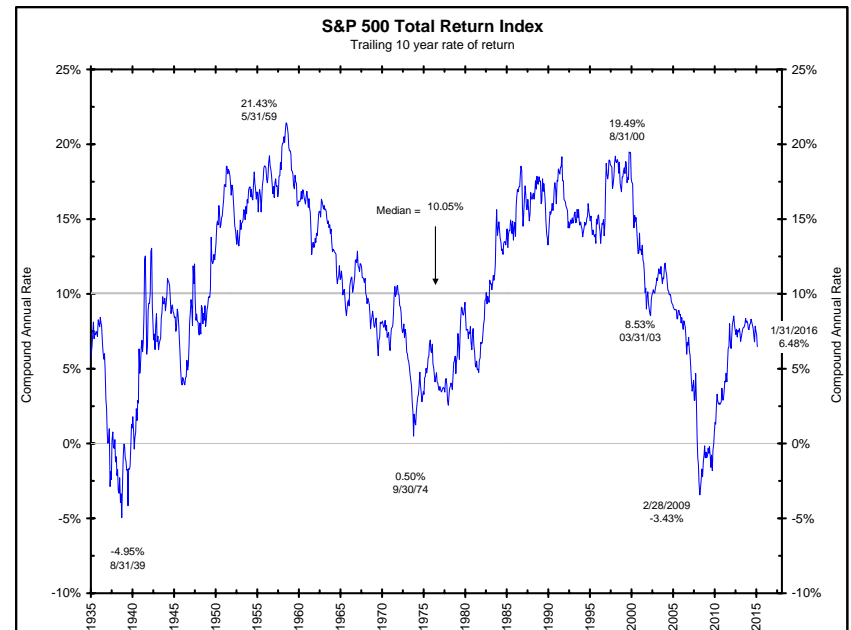
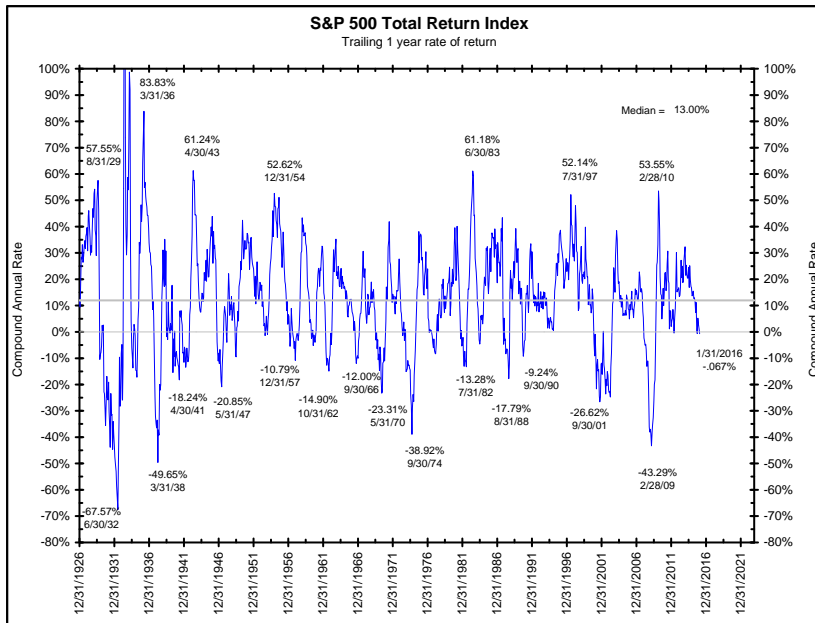


Looking At Interest Rates



A Long-Term Look At Stock Returns

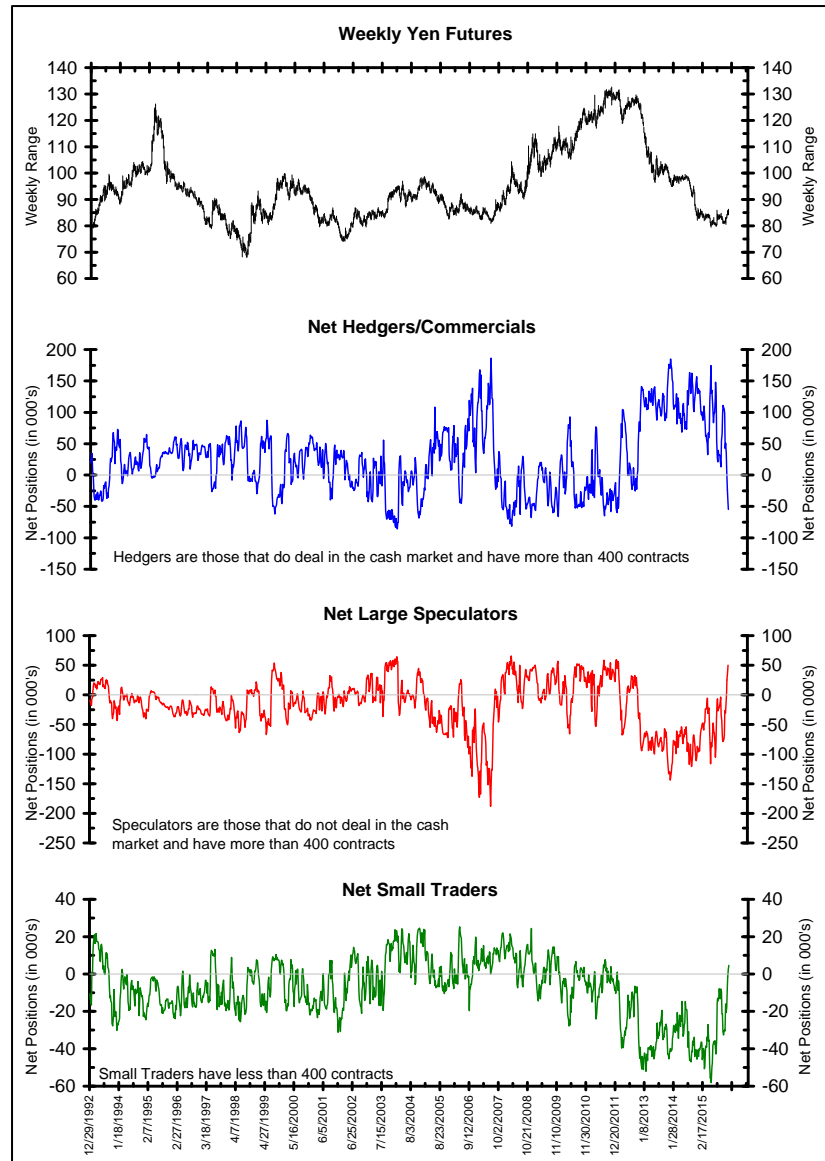
From Our Recent [Total Return Review](#)



Japanese Yen Futures: Large Speculators Continue To Buy Aggressively

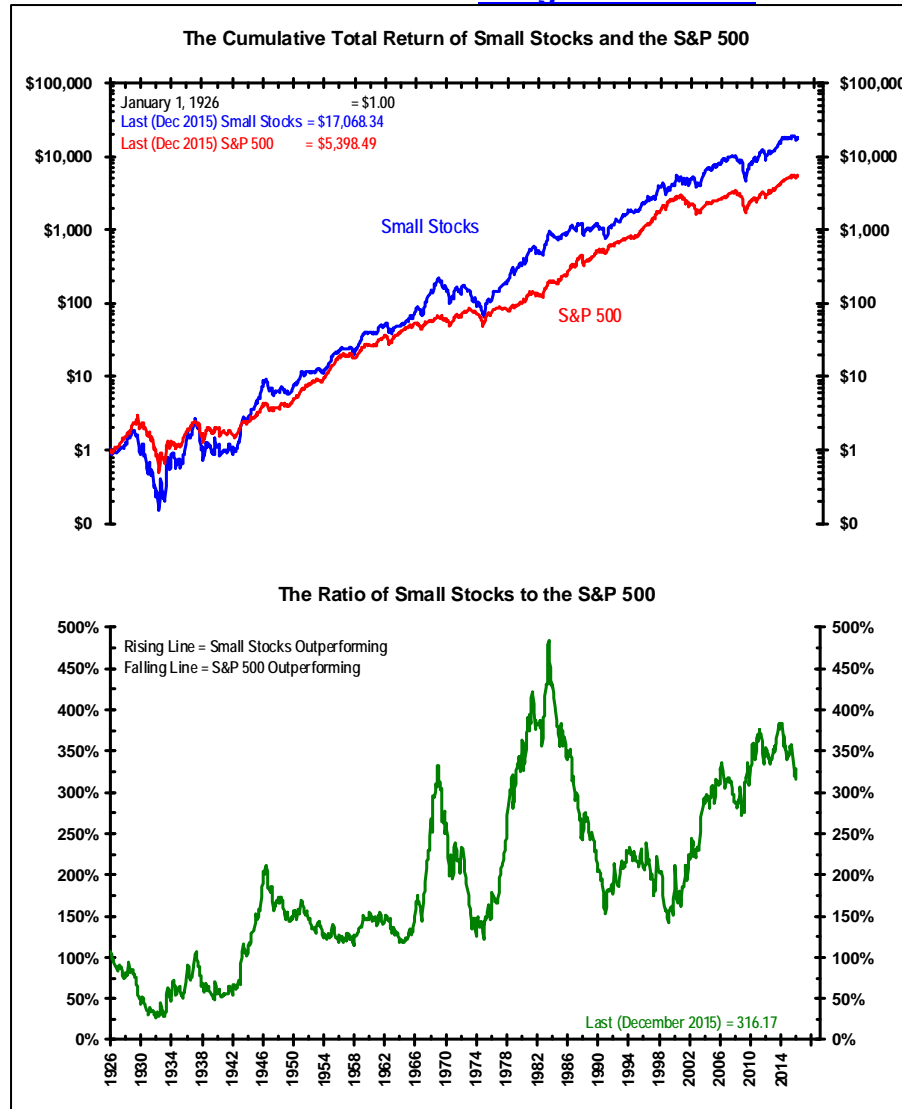
From Our Latest [Commitment Of Traders Update](#)

Friday's Commitments of Traders data Japanese yen futures showed Hedgers were net short 54,641 contracts on January 26. At the same time, Friday's report showed the Large Speculators were net long 50,026 contracts on January 26.



LT Outlook: The Cumulative Total Return of Small Stocks and the S&P 500

From Our Collection of [Long-Term Charts](#)



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