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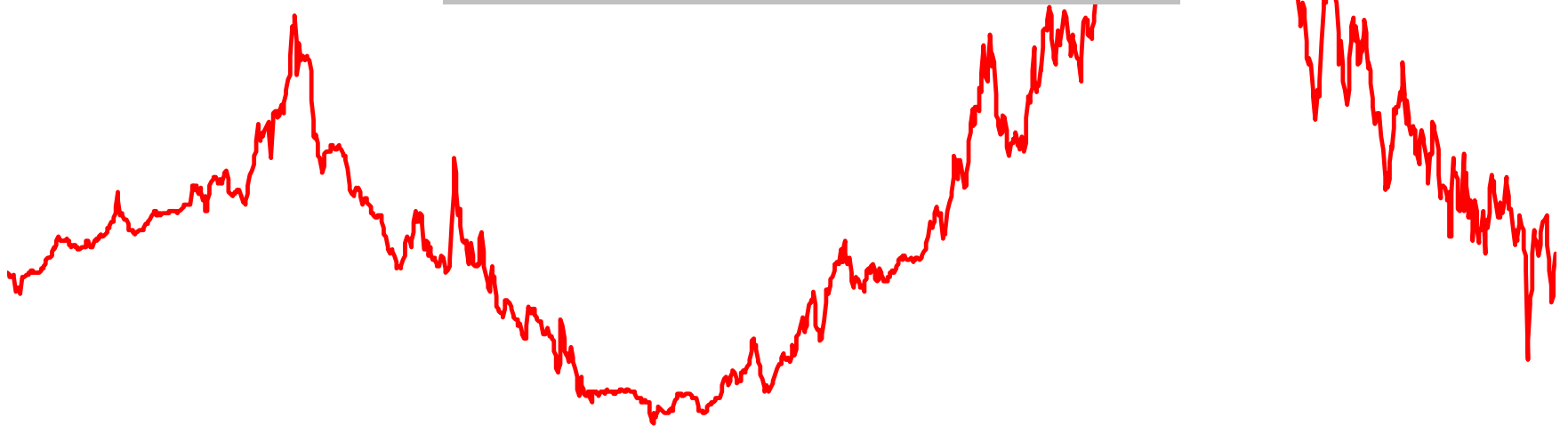
An Arbor Research & Trading Affiliated Company

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Charts Of The Week

Updated Pictures of Current Interest

For the week of October 26, 2011



Long-Term Interest Rates - 1900 to 2010

Dividend Stocks

MarketWatch – [Dividends work for top performing letter](#)

Market timing, phooey! A dividend-yield strategy is working for a top-performing letter. The Utility Forecaster, edited by Roger Conrad, is the No. 2 performer over the year to date through September by Hulbert Financial Digest count, up 8.2% vs. negative 9.86% for the dividend-reinvested Wilshire 5000 Total Stock Market Index...Overall, Utility Forecaster concludes: "The bottom line is, even if current market turmoil turns into something resembling 2008, we can expect essential-service companies to weather it in good shape. ... If you want any sort of income today, you're going to have to own dividend-paying stocks. In fact, with corporate borrowing rates at their lowest levels in generations, the only bonds with decent yields are on the higher-risk end of the spectrum."

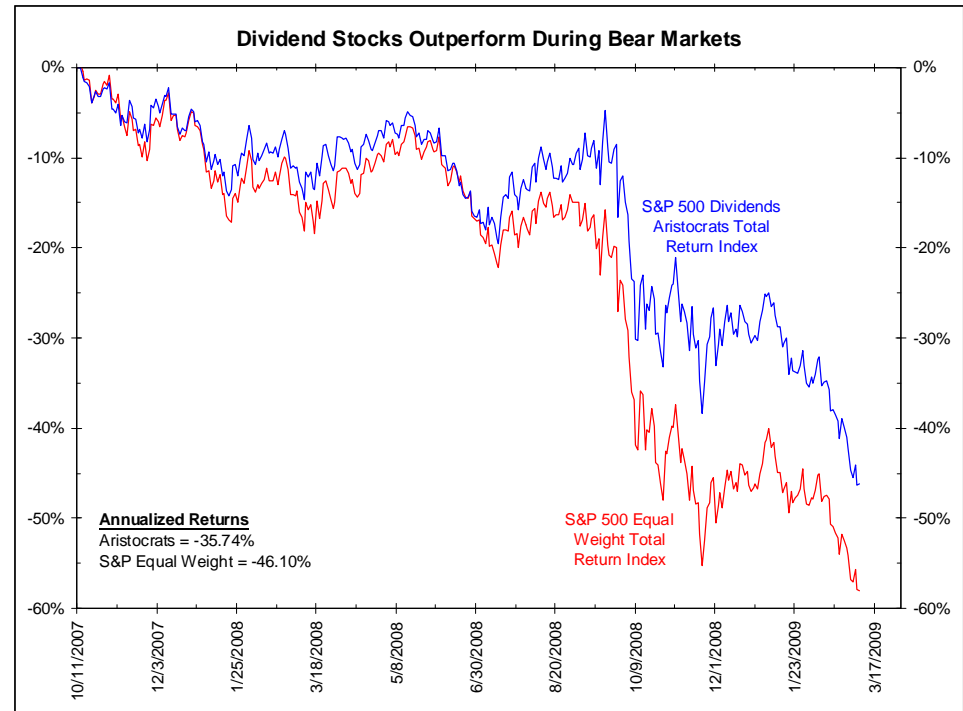
Comment

To be fair, the article above is about a particular dividend fund. While particular funds will either outperform or underperform based on the manager's ability to pick stocks, keep in mind what we said last week regarding dividend funds in general:

Dividend stocks should simply be viewed as a slightly less risky form of stock investing. As such, we should expect dividend-paying stocks to outperform during bear markets and underperform during bull markets.

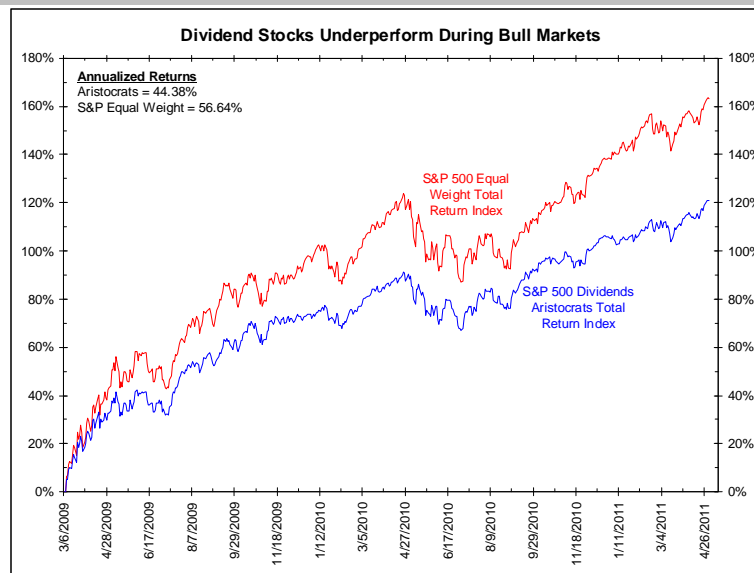
By comparing the S&P Dividends Aristocrats Total Return Index and the S&P Equal Weight Total Return Index, we can see this is indeed the case. The S&P Dividends Aristocrats Index measures the performance of stocks in the S&P 500 that have consistently increased dividends for at least 25 consecutive years. The index is equally weighted, so we compare its total return to that of the S&P 500 Equal Weight Index.

During the bear market from October 11, 2007 to March 6, 2009, dividend-paying stocks outperformed the S&P 500 Equal Weight Index by 11.6%. On an annualized basis, dividend stocks returned -35.74% versus -46.10% for the S&P Equal Weight Index.

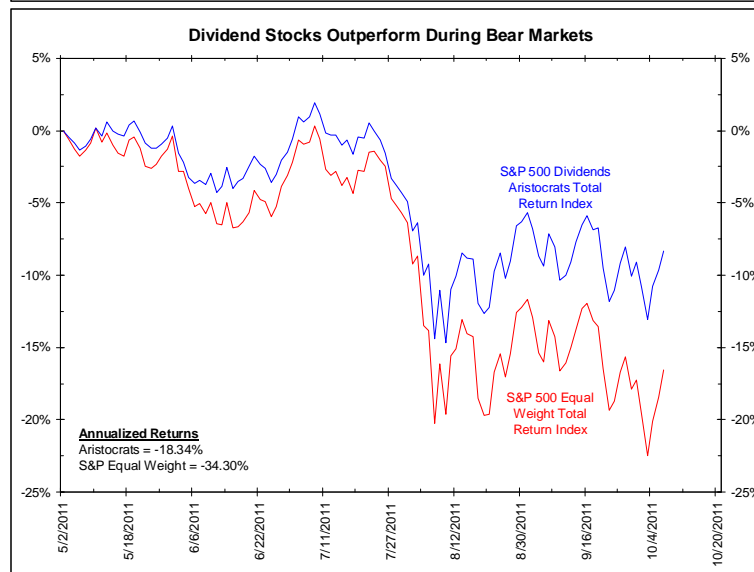


Dividend Stocks - 2

During the bull market from March 6, 2009 to May 2, 2011, dividend-paying stocks underperformed the S&P 500 Equal Weight Index by 42.4%. On an annualized basis, dividend stocks returned 44.38% versus 56.64% for the S&P Equal Weight Index.



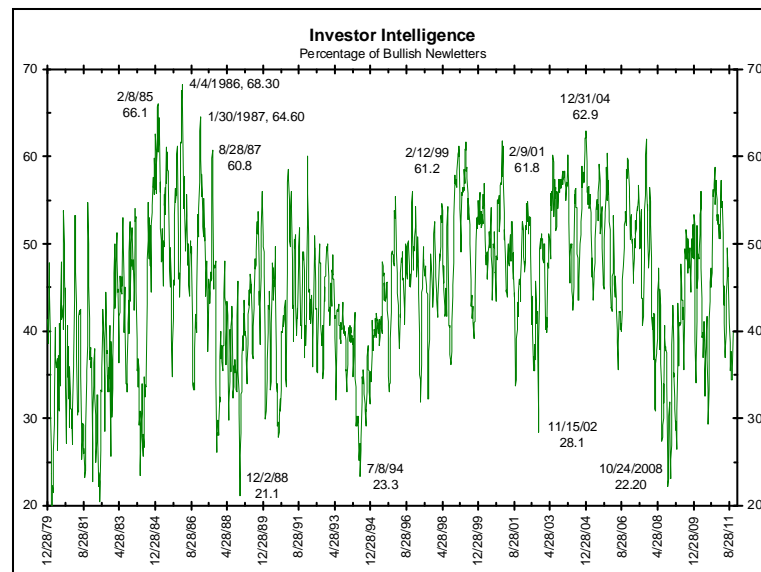
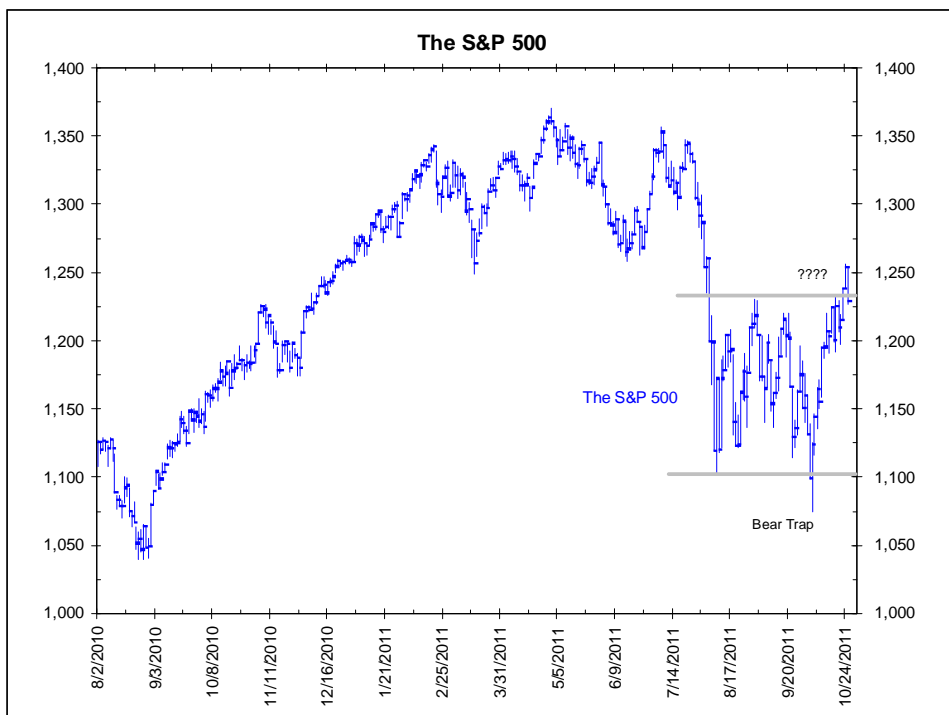
Finally, during the bear market from May 2, 2011 through last Thursday's close, dividend-paying stocks outperformed the S&P 500 Equal Weight Index by 8.19%. On an annualized basis, dividend stocks returned -18.34% versus -34.30% for the S&P Equal Weight Index.



The Stock Market's Range

The New York Times – [Paul J. Lim: The Sunny Side of Doom and Gloom](#)

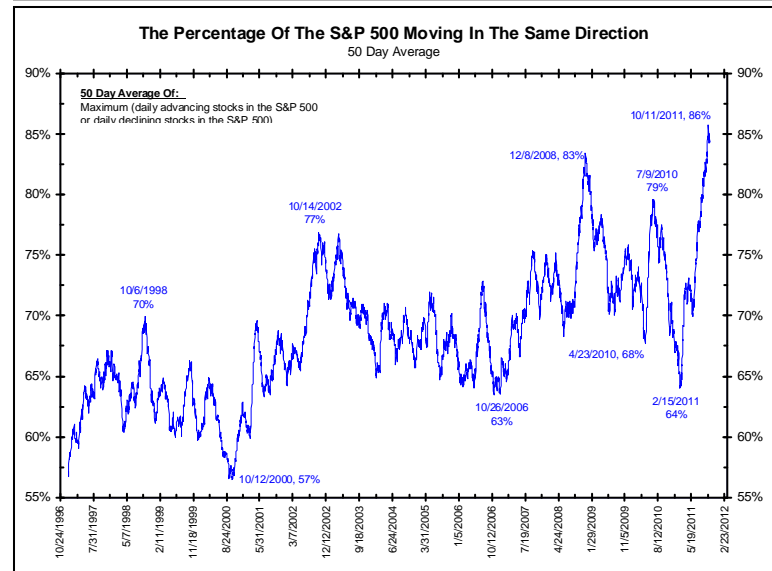
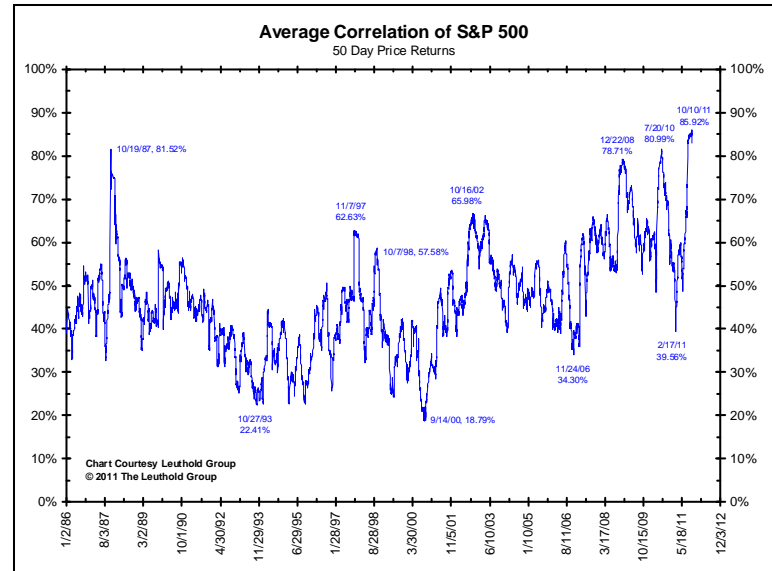
No wonder that investors have shown little confidence in the staying power of the latest rebound, which since Oct. 3 has lifted stock prices by 13 percent, leaving the S. & P. at 1,238. Last week, the Investors Intelligence adviser survey, a widely followed gauge that tracks the opinions of more than 100 independent investment newsletters, showed that bears continued to outnumber bulls even though the index had climbed almost half the way back. But sentiment can be a funny thing. The best thing that Wall Street may have going for it right now is that so many investors are pessimistic. That's because the mood in the market is often regarded as a contrarian indicator of future activity.



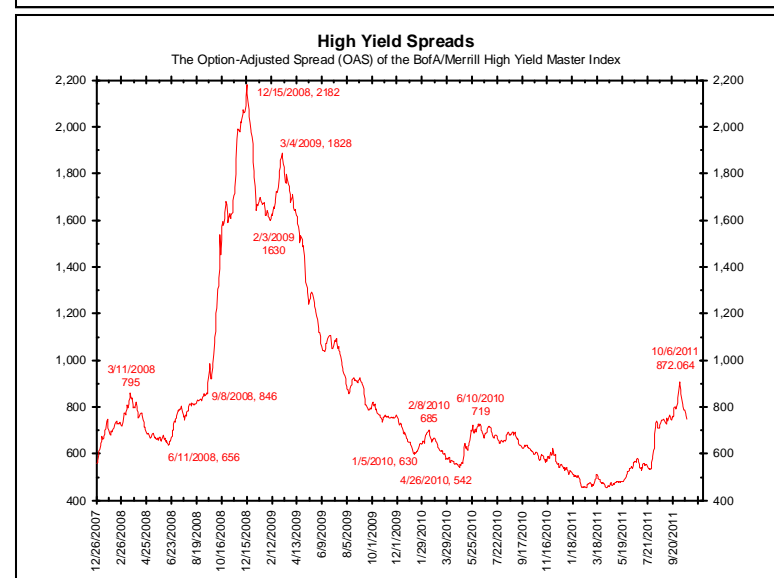
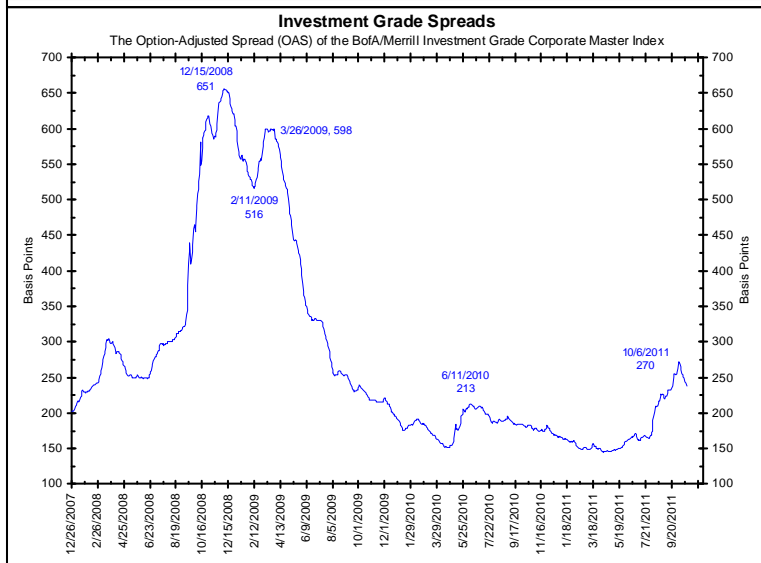
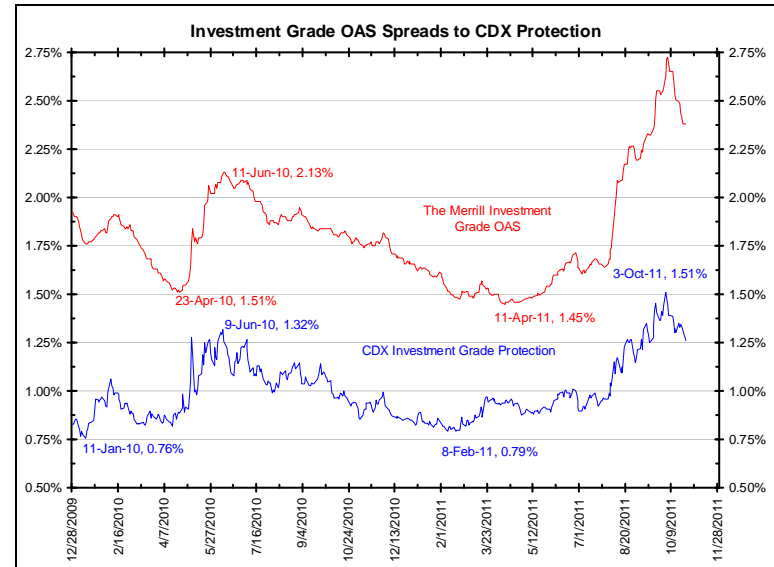
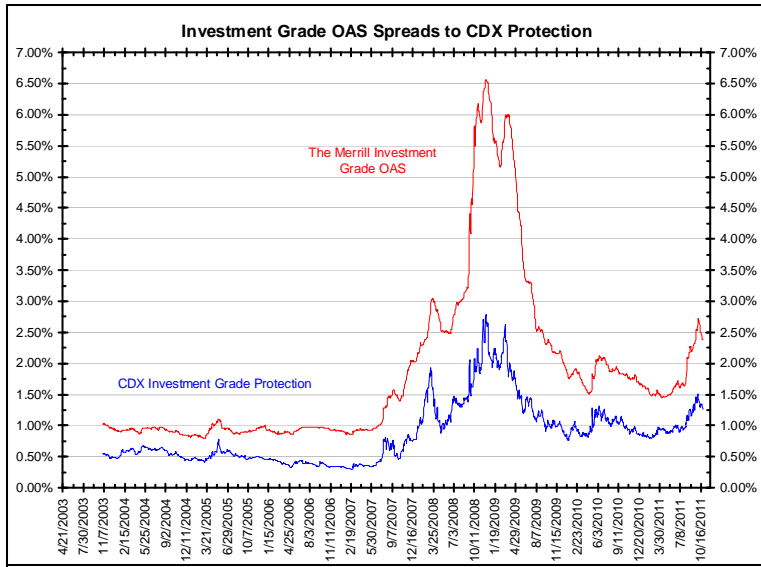
Market Correlation

From Our [Newsclips/Daily Commentary](#)

We also discussed market correlation in depth in our September 29, 2011 conference call ([handout](#), [audio](#), [webcast](#), [transcript](#)). To the right are the updated charts that were used in the discussion.



An Updated Look At Credit



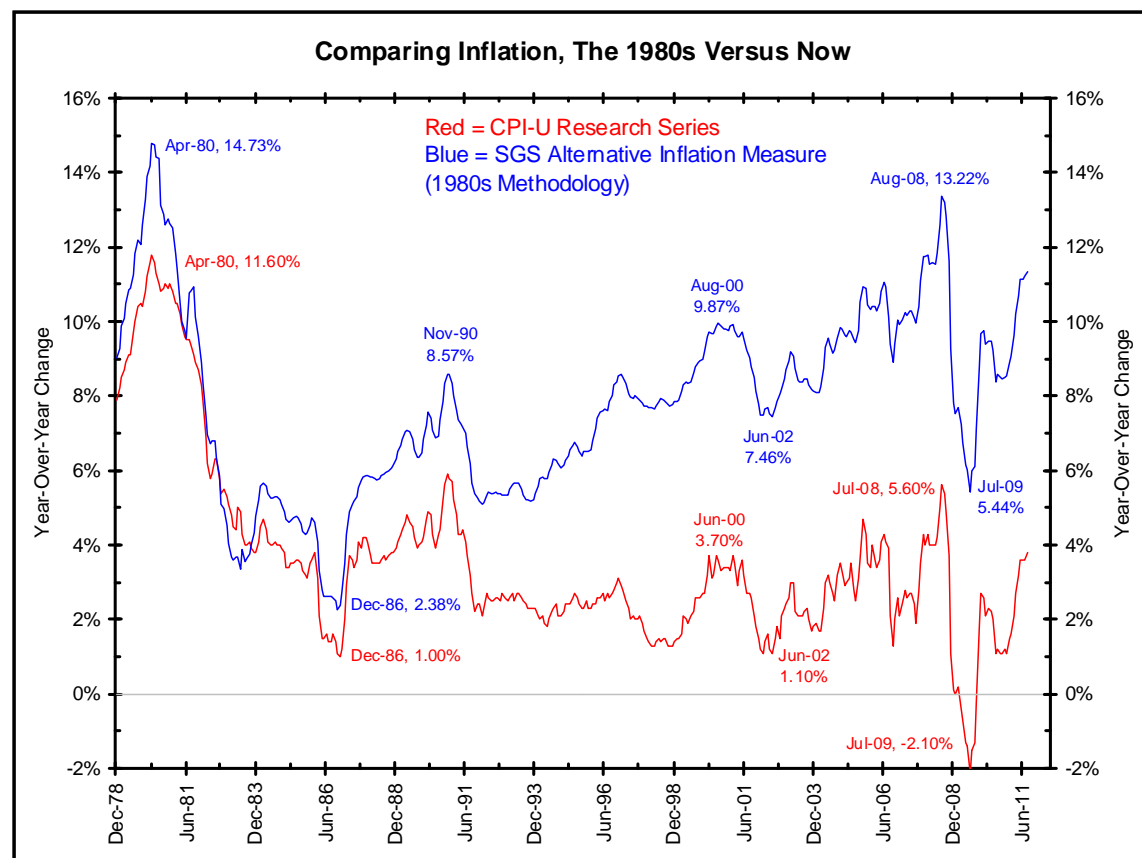
Are We About To Have Too Much Inflation?

From Our Recent [Inflation Watch](#) Update

1980 Inflation

Because the CPI measure has morphed so many times throughout the years ([detailed here](#)), one complaint often lodged against the BLS is that inflation rates today cannot be compared to inflation rates from, say, 1980. In an attempt to offer a more apples-to-apples comparison of historical inflation, the BLS maintains a series known as the CPI-U Research Series. It reverse engineers the CPI based on today's index weights and methodology all the way back to 1978.

The chart below shows the CPI-U Research Series in red. But what if we wanted to know what the inflation rate would be today based on the index rules used in the past? To get this answer, we must turn to [Shadow Government Statistics](#). This website, run by economist John Williams, calculates CPI using the same methodology used in 1980. That is shown in blue. According



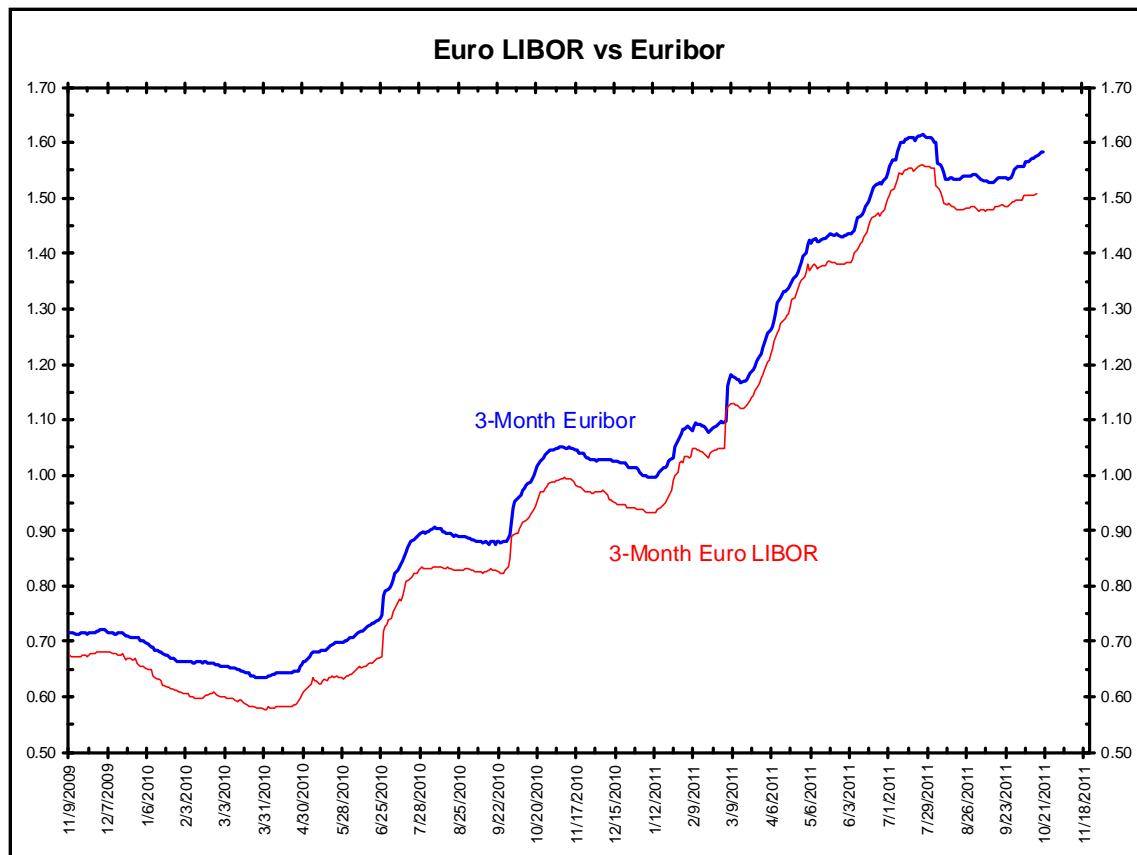
Euro-LIE-bor

[The Financial Times – Brussels escalates Euribor investigation](#)

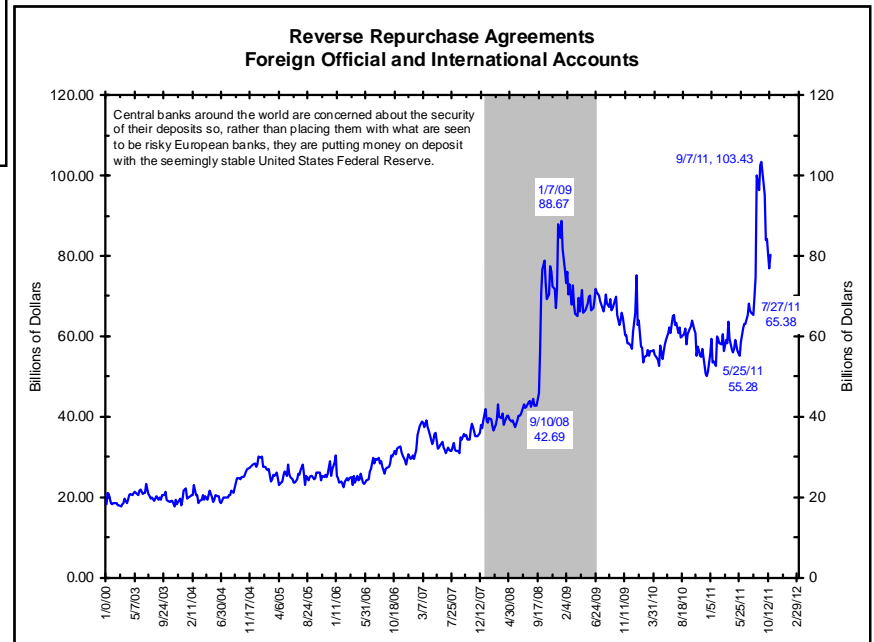
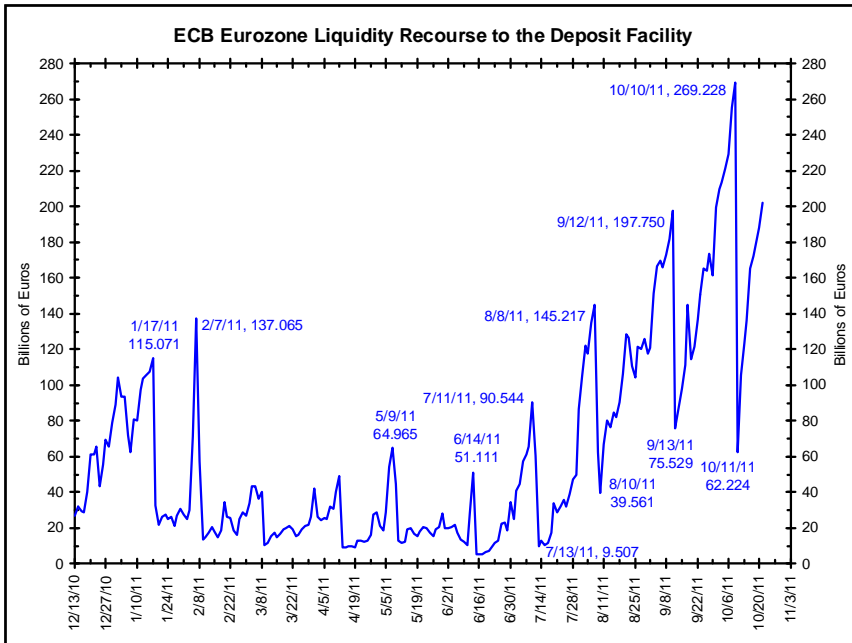
European regulators seized documents from several big banks in London and France this week after being tipped off by one of the banks caught up in the worldwide probe of interbank lending that it had uncovered potential problems connected to the EU-based Euribor rate, people familiar with the probe said. The European Commission's competition arm confirmed on Wednesday that it had launched unannounced inspections of several members of the panel that sets Euribor, or the Euro Interbank Offered Rate, the benchmark at which European banks lend to each other. Fewer than 10 of the 44 members were involved, the people said. Investigators from Washington, Brussels and Tokyo have been working together for more than a year to probe whether Libor, the London-based reference point for \$350,000bn in contracts was rigged at the height of the financial crisis. The work expanded to include Tibor, the smaller Tokyo-based version, after UBS turned over information to the US Department of Justice about the setting of yen and dollar rates in Japan in exchange for partial immunity.

Comment

Back in August we discussed the possibility that the European interbank interest rates were fictional numbers. We also noted that the American LIBOR numbers are so widely believed to be fictions that Charles Schwab is suing 11 reporting banks.



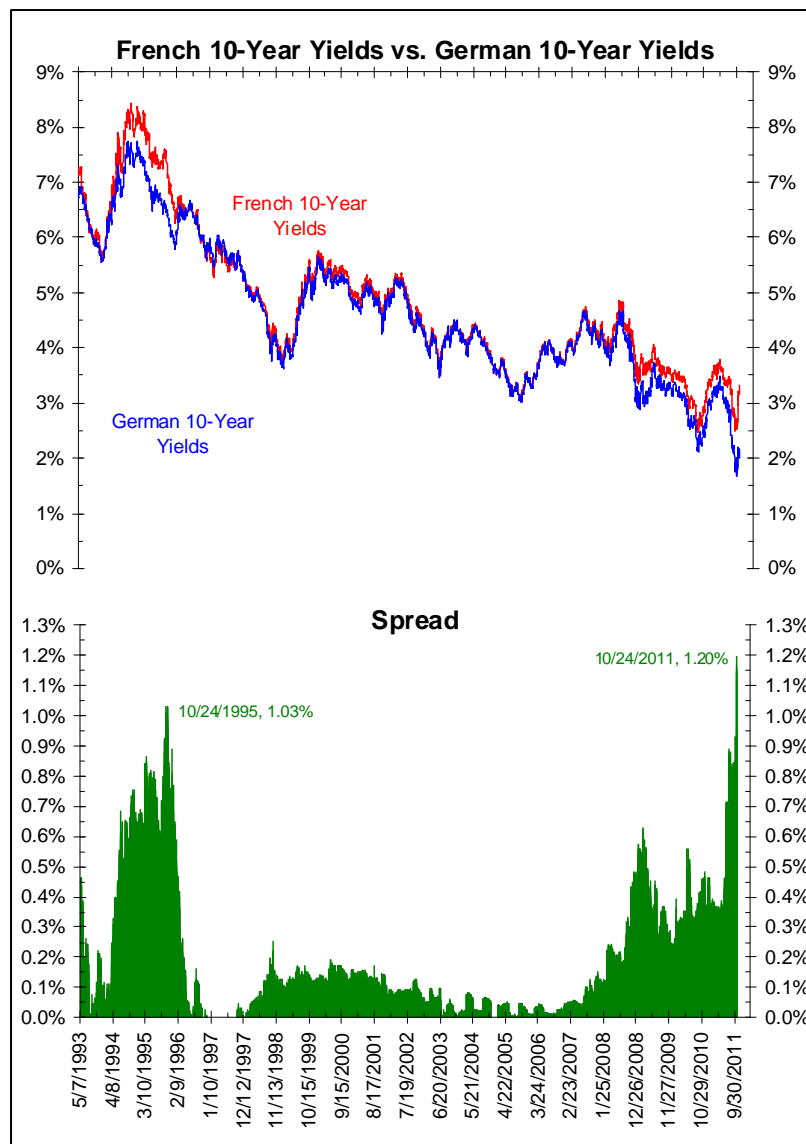
European Banks



French 10 Year Yields vs. German 10-Year Yields

[Bloomberg.com – France Likely to Lose Top Rating in Stressed Economic Scenario, S&P Says](#)

France is among euro-region sovereigns likely to be downgraded in a stressed economic scenario, according to Standard & Poor's. The sovereign ratings of Spain, Italy, Ireland and Portugal would also be reduced by another one or two levels in either of New York-based S&P's two stress scenarios, the ratings firm said in a report dated today. These assume low economic growth and a double-dip recession in the first set of circumstances, and add an interest-rate shock to the recession in the second. "Ballooning budget deficits and bank recapitalization costs would likely send government borrowings significantly higher under both scenarios," S&P analysts led by Chief Credit Officer Blaise Ganguin in Paris wrote in the report. "Credit metrics would deteriorate sharply as a result." S&P is seeking to take account of the economic slowdown that hit Europe in the second quarter and which has led the ratings company to trim 2012 growth forecasts to an average of between 1 percent and 1.5 percent. France would follow the so-called peripheral euro-region nations that have already been downgraded, with Moody's Investors Service saying earlier this week that its top rating was under threat.



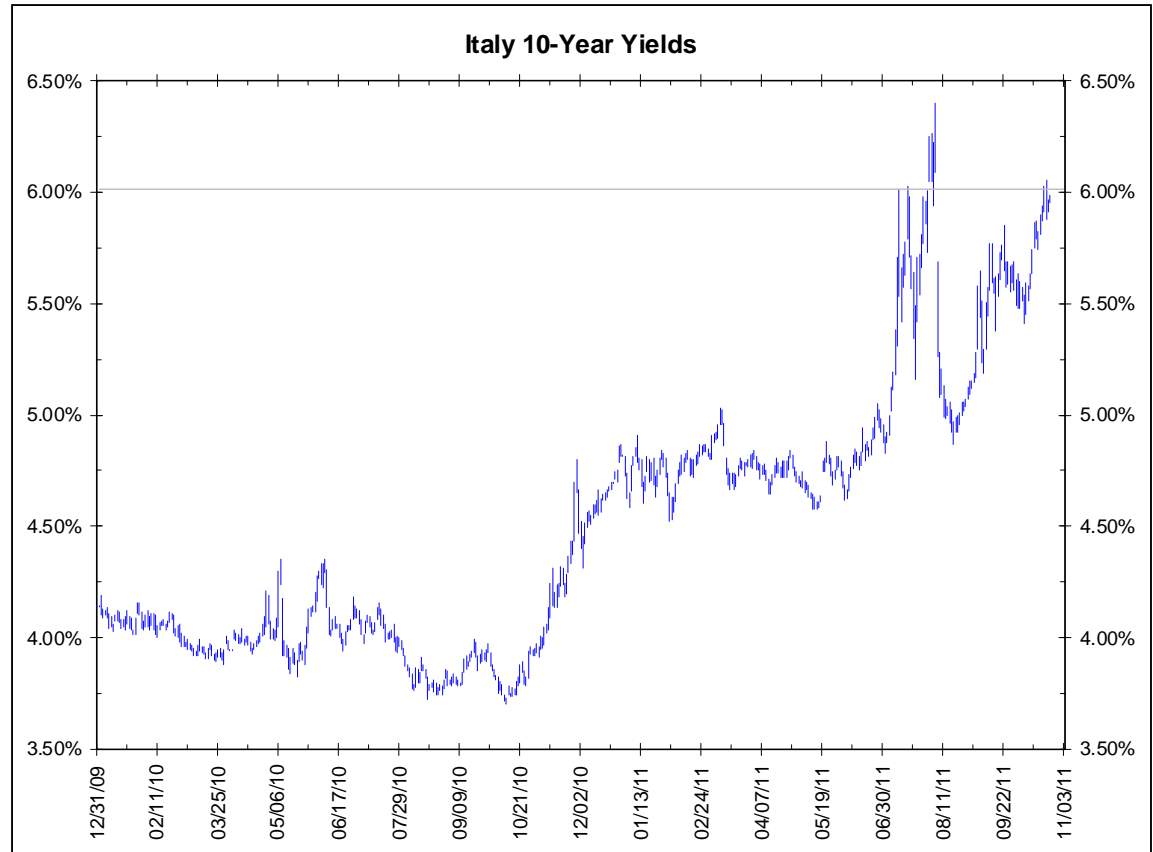
Italy

Comment

Will Italy deliver? See the chart to the right. The continued rise towards 6% indicates the market does not believe so.

[The Financial Times- Pressure on Italy in eurozone struggle](#)

Germany and France have turned on Italy to demand further action to boost growth and reduce its huge debt, as leaders of the eurozone struggled to agree on how to boost their rescue fund to stop contagion in the sovereign debt markets before a Wednesday deadline. Angela Merkel, the German chancellor, and Nicolas Sarkozy, French president, held tough talks with Silvio Berlusconi, at the start of the day-long summit in Brussels, insisting that he take more radical measures to restore the trust of investors. Confidence in Italy's public finances is critical to preventing the spread of the Greek debt crisis across the eurozone, but France and Germany are worried that Mr Berlusconi is not taking tough enough measures.



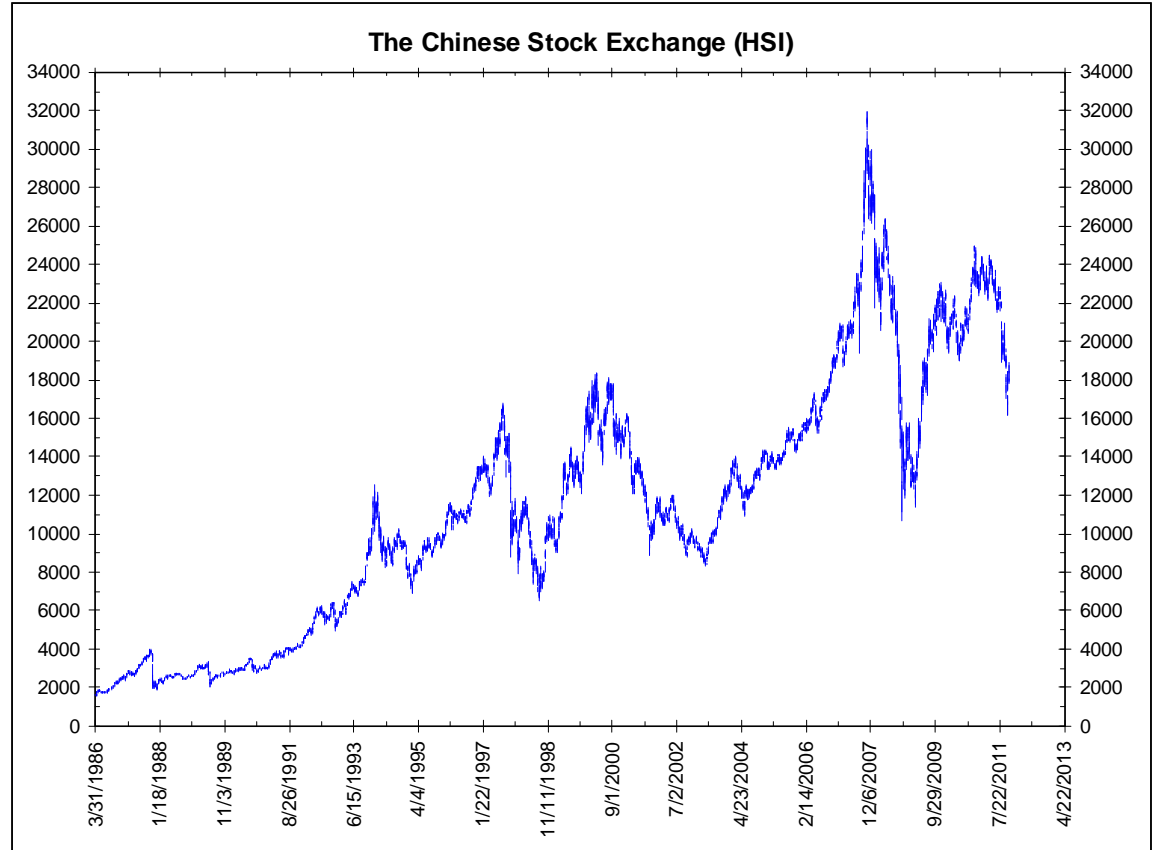
China

TIME Magazine – [Be Very Afraid of The China Bubble](#)

What's the most important economic question in the world today? One contender is whether the euro will collapse. Another is whether the U.S. will plunge into a double-dip recession. But a third, and possibly the most important over the long term, is whether China can save the world—or whether the entire country is a \$6 trillion bubble that's ready to pop. That's the size of the Chinese economy, now the second largest in the world, after the U.S.'s. China contributed 19% of global economic growth in 2010, and that's expected to increase to 24% this year. China's strength is essential to...

Comment

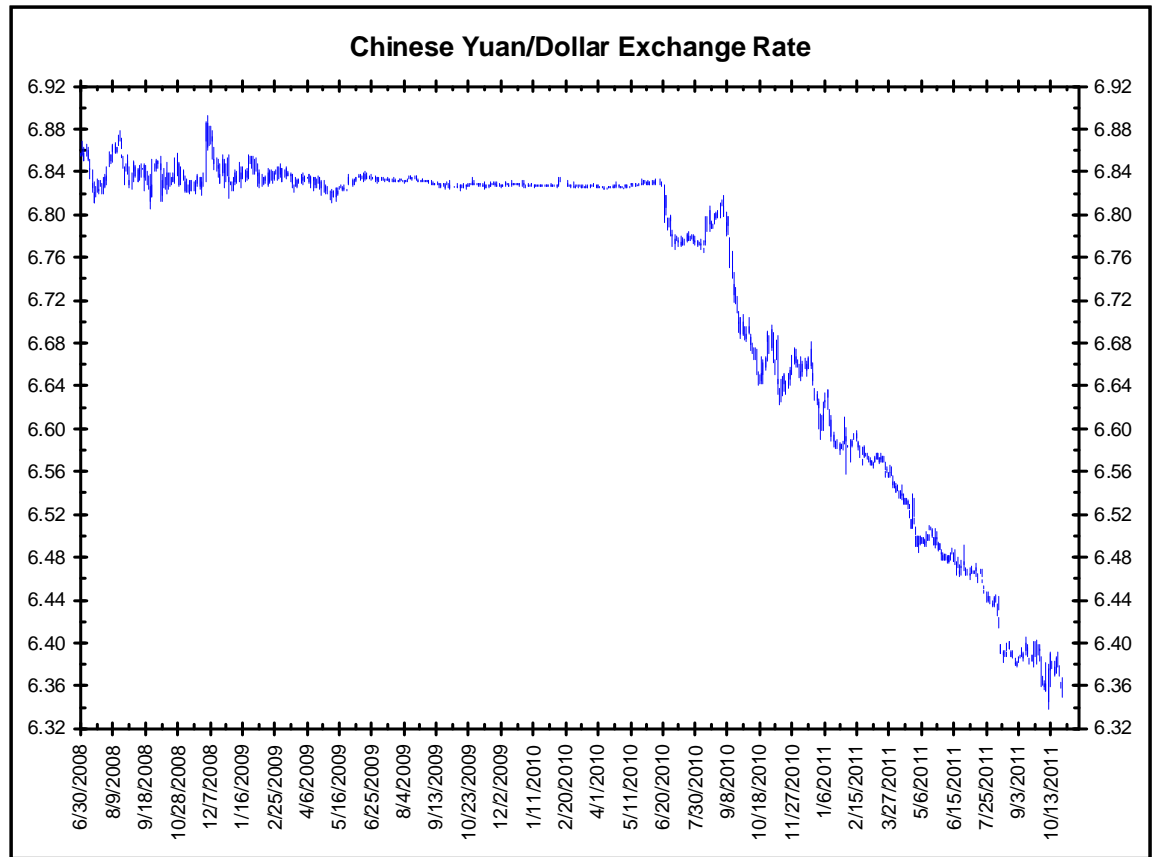
Considering both the [TIME cover](#) above and the slumping Chinese stock market chart shown below, is the idea that Chinese stocks are in a bubble about to pop now fully known and discounted in prices?



The Yuan

[The Wall Street Journal – China Offers Case Against Rapid Yuan Rise](#)

China's currency, the yuan, is now close to the equilibrium level, and pushing for rapid appreciation in the near term will only be counterproductive, Chinese Foreign Ministry spokeswoman Jiang Yu said Wednesday. Ms. Jiang, speaking at a regular news briefing, said the yuan has appreciated around 30% since the country's exchange rate reform in 2005. "In the short term, pushing for rapid yuan appreciation is not possible. If Chinese economic growth slows, it will reduce global aggregate demand," she said. "We will continue to push forward with yuan exchange rate reform, but that process will be gradual." The U.S. Congress has been pressuring China to allow the yuan to appreciate at a faster pace, with the Senate in recent weeks passing a measure that would require more aggressive action against Beijing's currency policy, including trade penalties. "This is not the right way to solve U.S. domestic problems," Ms. Jiang said. Speaking about reports that China may participate in an investment vehicle proposed by euro-zone leaders to raise funds for bank recapitalization, Ms. Jiang didn't specifically comment, but said China is open to different ideas on working with Europe.

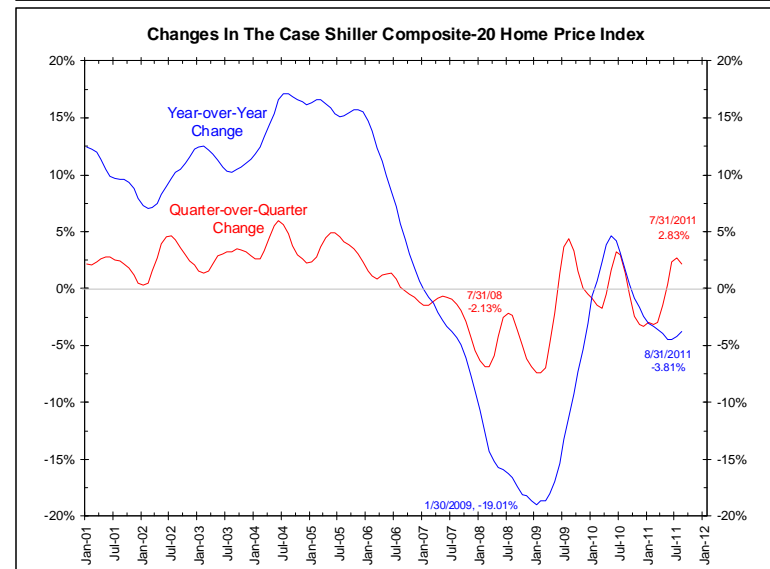
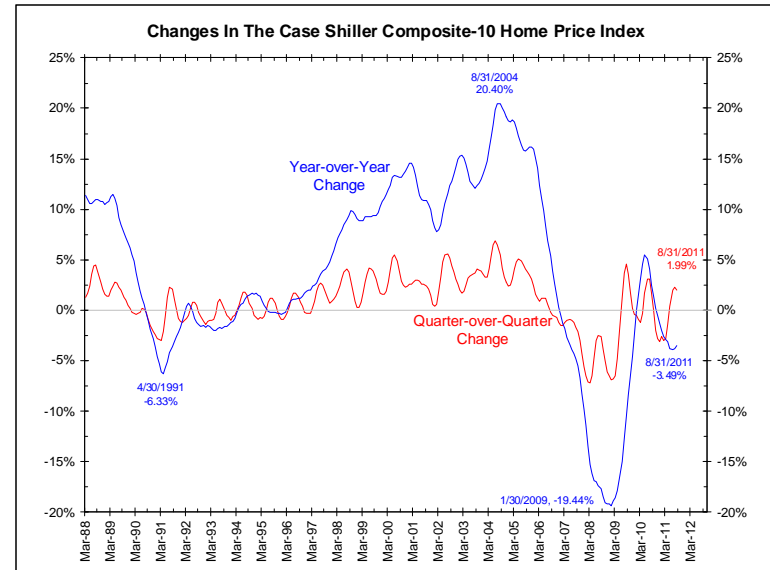


Case Shiller Home Prices Update

From Our [Newsclips/Daily Commentary](#)

[Bloomberg.com - Home Prices in U.S. Cities Fall More-Than-Forecast 3.8%, Case-Shiller Says](#)

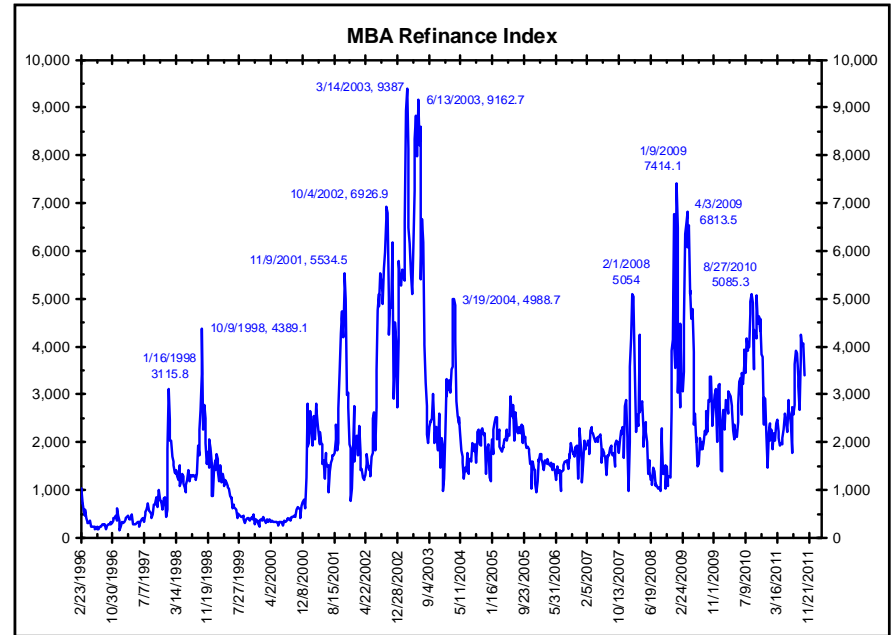
Home prices in 20 U.S. cities dropped more than forecast in August, highlighting one of the obstacles facing the economic recovery in its third year. The S&P/Case-Shiller index of property values in 20 cities fell 3.8 percent from August 2010, the group said today in New York. The median forecast of 30 economists surveyed by Bloomberg News was for a 3.5 percent decline. Recovering the 31 percent plunge in home prices from their 2006 peak will probably be years in the making as foreclosures throw more properties on the market and sales flag. Federal Reserve policy makers like William Dudley are among those that believe bolstering housing is among the “most pressing issues” facing the central bank. “There is still a big imbalance between demand and supply,” said Guy LeBas, chief fixed-income strategist at Janney Montgomery Scott LLC in Philadelphia, who projected a 3.9 percent decline. “Prices will keep declining into 2012.” Consumer confidence unexpectedly slumped in October to the lowest level since March 2009 as Americans’ outlooks for employment and incomes soured, another report today showed. The Conference Board’s sentiment index decreased to 39.8 from a revised 46.4 reading in September. Economists projected the October gauge would climb to 46, according to the median forecast in a Bloomberg survey.



Refis

Reuters.com – [U.S. throws lifeline to underwater homeowners](#)

Homeowners who owe more than their properties are worth got new help on Monday with the government's expansion of a refinancing program in a step that could help up to 1 million borrowers. The regulator of mortgage finance giants Fannie Mae and Freddie Mac eased the terms of a program that helps so-called underwater borrowers who have made payments on time but have been unable to refinance. "These are important steps that will help more homeowners refinance at lower rates, save consumers money and help get folks spending again," President Barack Obama said in remarks to the press and a handful of neighbors standing outside of a house in Las Vegas, where he had met with a family that benefited from his housing programs. The Nevada city was hard hit by the foreclosure crisis. The overhaul, which would only help a fraction of the country's 11 million underwater borrowers, is the latest government effort to breathe life into the crippled U.S. housing market. Officials have been frustrated that numerous attempts to bolster the sector and help borrowers have had little success. The Federal Housing Finance Agency said it was scrapping a cap that prohibited borrowers whose mortgages exceeded 125 percent of their property's value from refinancing loans backed by Fannie Mae and Freddie Mac under the government's Home Affordable Refinance Program (HARP).

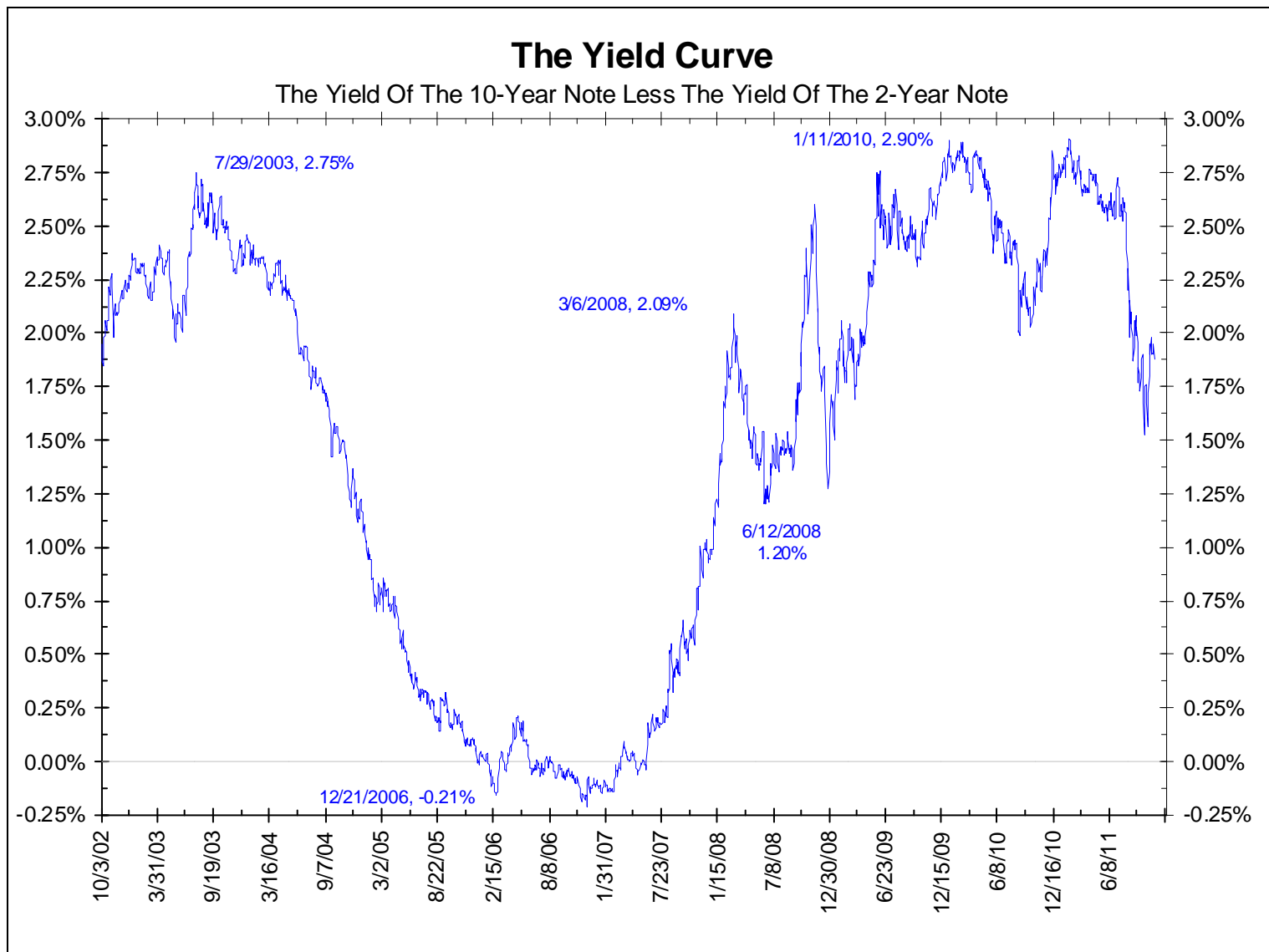


Comment

According to Census data, a total of 76.428 million owner occupied units existed in the U.S. as of 2009. Of those, 50.3 million currently had a mortgage on their property. If the latest tweak to the HARP guidelines is only estimated to help 1 million people, that means less than 2% of all mortgages in the U.S. will be able to take advantage of these changes.

Considering Core Logic's estimate that 22.5% of all homes in the U.S. are underwater and another 5% have near negative equity, most underwater homeowners will not be helped by the changes in this program.

An Updated Look At The Yield Curve

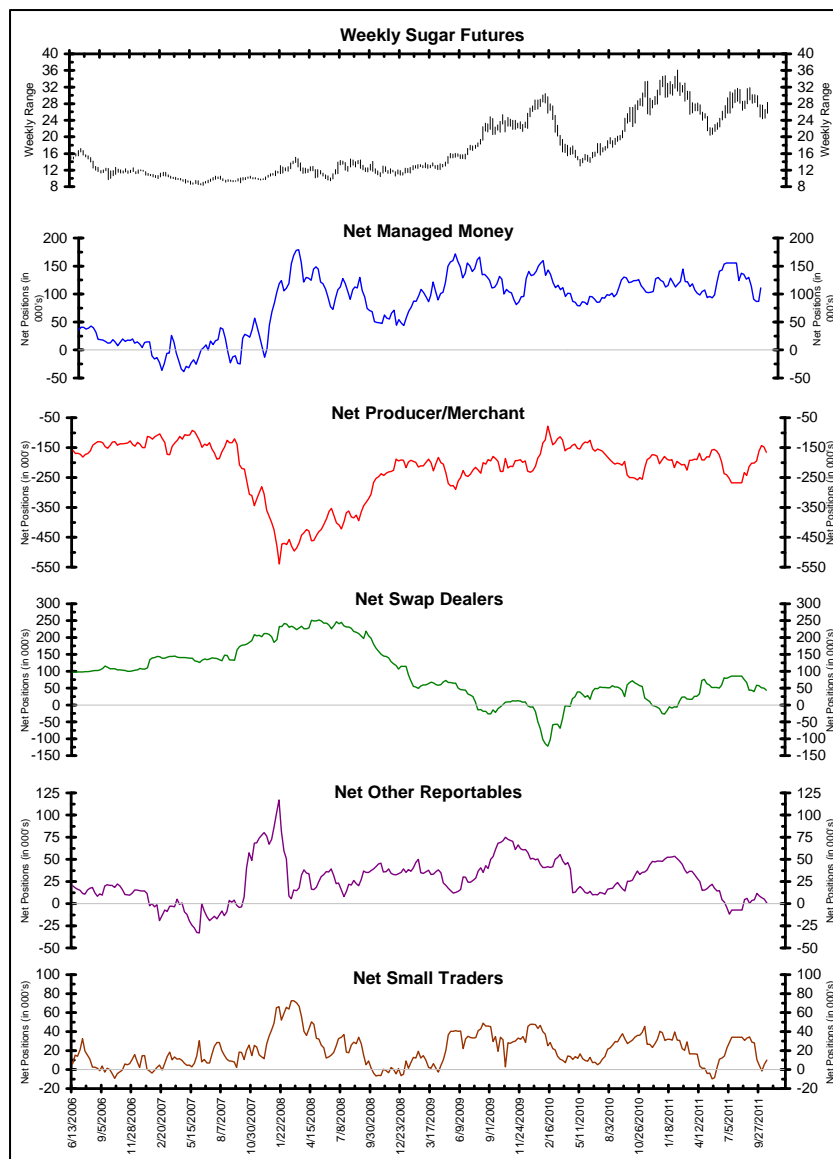


Sugar Futures: Funds Add To Long Positions

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

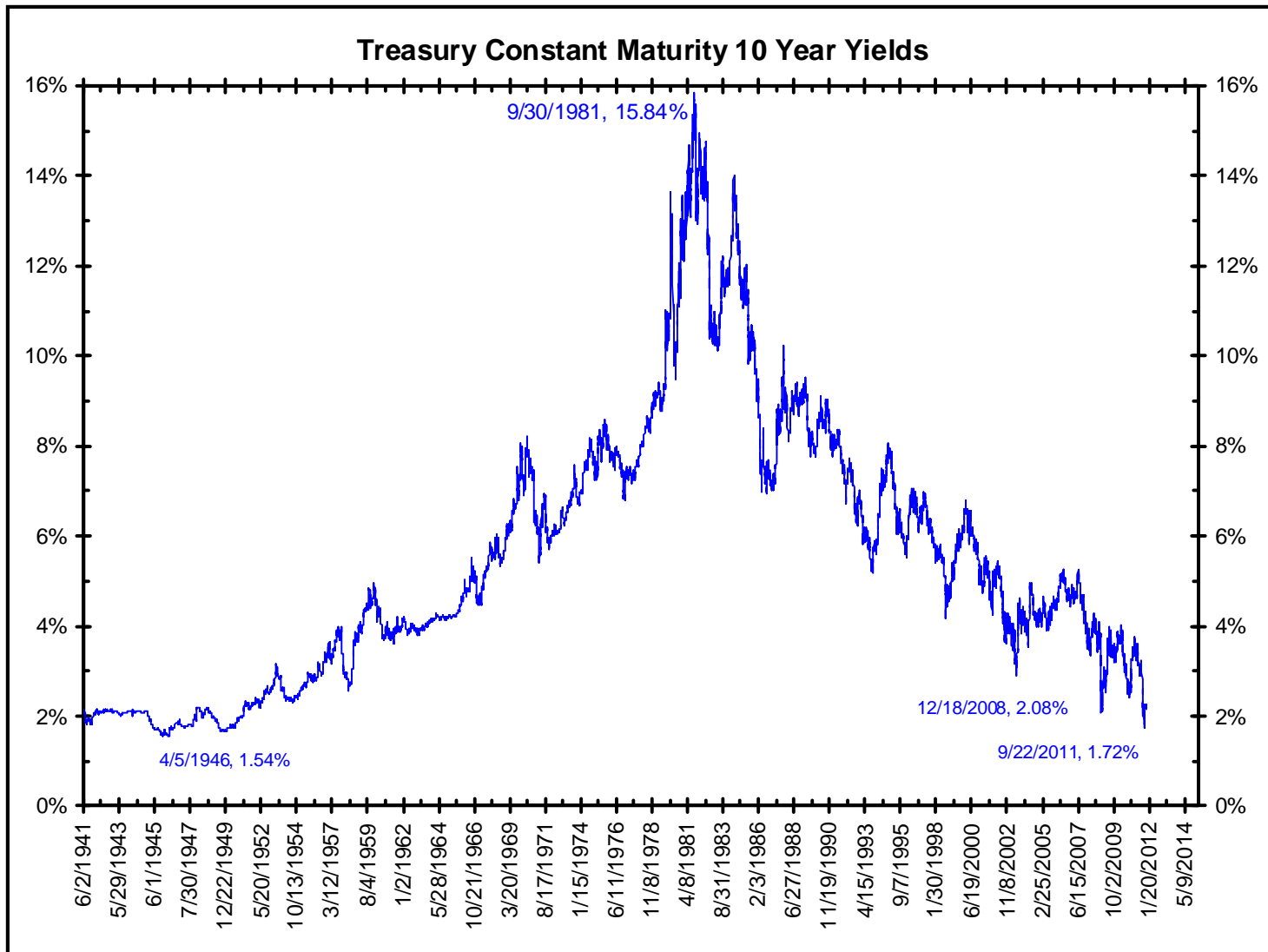
Friday's Commitments of Traders data for sugar futures showed Managed Money was net long 111,041 contracts on October 18.

The funds added to their net long position in front of a post-reporting selloff in sugar. The Other Reportables sold in front of the downturn.



Treasury Constant Maturity 10 Year Yields

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



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