

James Bianco

The Bond Bear Market Continues
South Florida Bond Traders Association
February 2, 2024



Chart 9: Inflection point in long-term rate (i.e. bond yields) expectations

% FMS investors expecting lower long-term rates



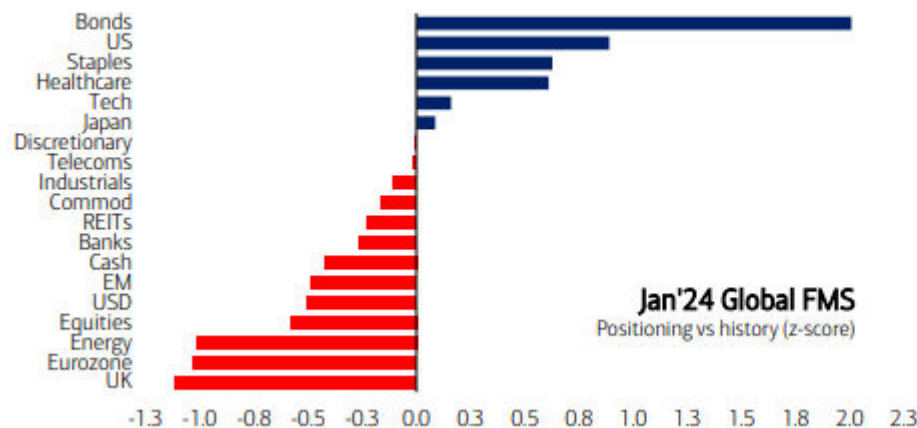
Source: BofA Global Fund Manager Survey, Bloomberg

Investors turned slightly less bullish on bond yields post the 100bps rally in long-term rates over the past 2 months.

55% expect lower bond yields in the next 12 months, down slightly from a record 62% in Dec'23.

Chart 24: Investors OW Bonds, US, staples & healthcare, and UW UK, Eurozone vs history

FMS positioning vs history (z-score)



Source: BofA Global Fund Manager Survey

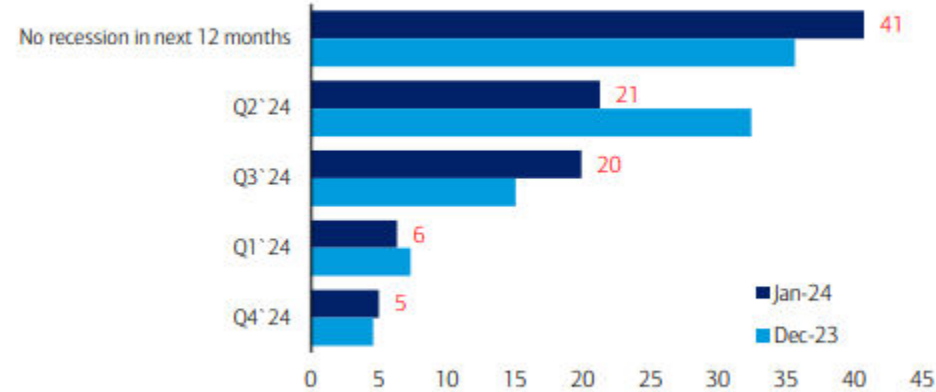
This chart shows FMS investor positioning relative to the average positioning of the past 20 years.

Relative to history, investors are long bonds, US, staples & healthcare...

...and are underweight UK, Eurozone, energy & equities.

Chart 4: Timing of recession?...no recession is #1 FMS answer

When do you expect the US economy to fall into recession?



Source: BofA Global Fund Manager Survey, Bloomberg

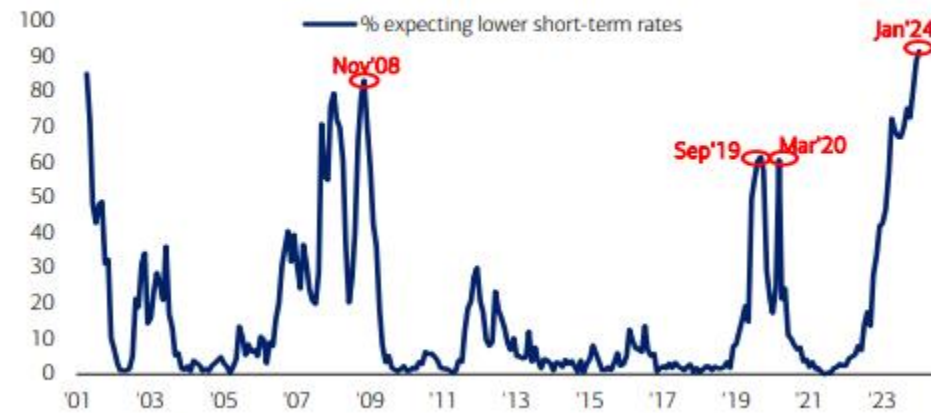
BofA GLOBAL RESEARCH

41% of FMS investors see no recession at all in 2024, a higher percentage than any other answer.

Amongst FMS investors expecting a recession in 2024...21% say Q2, 20% Q3, 6% Q1, and 5% Q4.

Chart 8: Expectations for lower short-term rates at a record high

% FMS investors expecting lower short-term rates in next 12 months

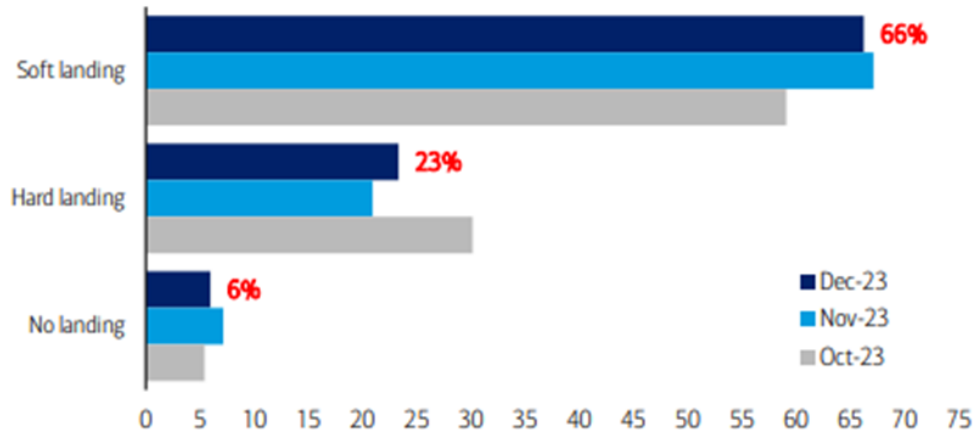


Source: BofA Global Fund Manager Survey

FMS investors have never been as bullish on short-term rates as in Jan'24 (data going back to Apr'01) ...a record of 91% expect short-term rates to be lower in the next 12 months, up from 87% in Dec'23.

Chart 6: "Soft landing" the consensus for 2024

What is the most likely outcome for the global economy in the next 12 months?



Source: BofA Global Fund Manager Survey

BofA GLOBAL RESEARCH

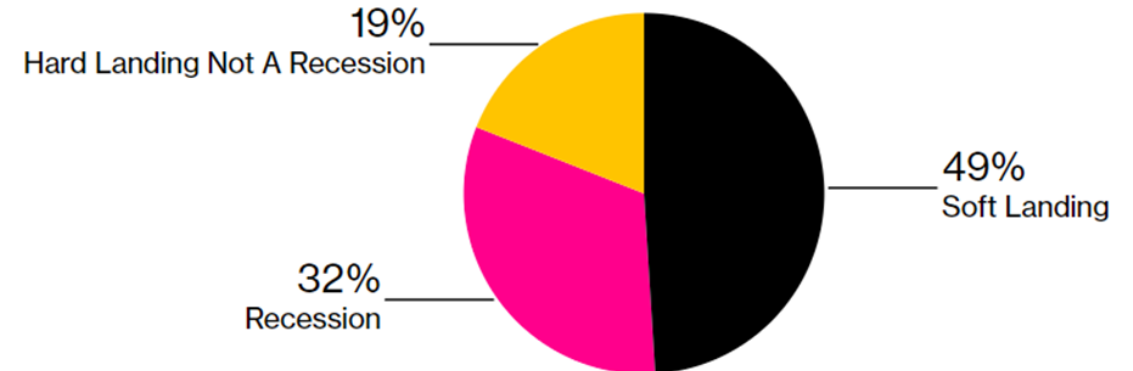
66% of FMS investors expect a "soft landing" for the global economy in the next 12 months.

Expectations for "hard landing" 23%.

When asked about the timing of recession for the US economy, 36% said they expect no recession at all in the next 12 months while 32% expect the US to fall into recession in Q2'24.

Most Economists Don't Expect Recession Within 12 Months

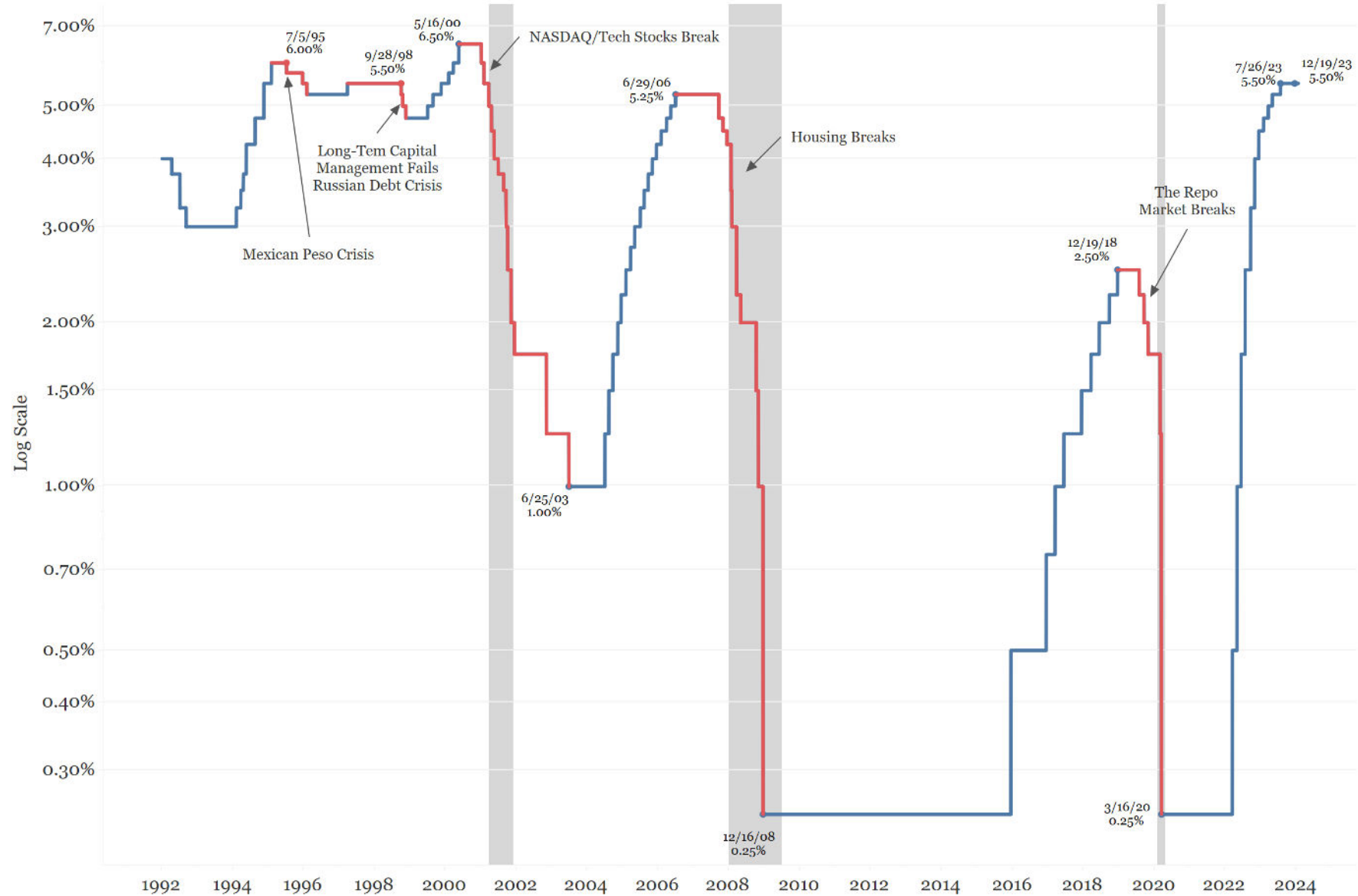
Fewer than one third of economists forecast a recession



Source: Bloomberg News survey of economists Dec. 1-6
Economists were asked if US would have a recession in the next 12 months.

The Fed Hikes Too Much and Something Breaks

The Target Federal Funds Rate Since 1992



Source: Bloomberg

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The Financial Times – (October 19, 2023) [Blackstone warns of looming hit to consumers from surge in bond yields](#)

‘When 30-year mortgages and car loans cost you 8% it will impact consumer behaviour,’ says president

Jonathan Gray, president of Blackstone, said in an interview with the Financial Times that the jump in 10-year Treasury yields would force consumers to tighten their belts. “When 30-year mortgages and car loans cost you 8 percent it will impact consumer behaviour,”

Bankrate.com US Home Mortgage 30 Year Fixed National Avg

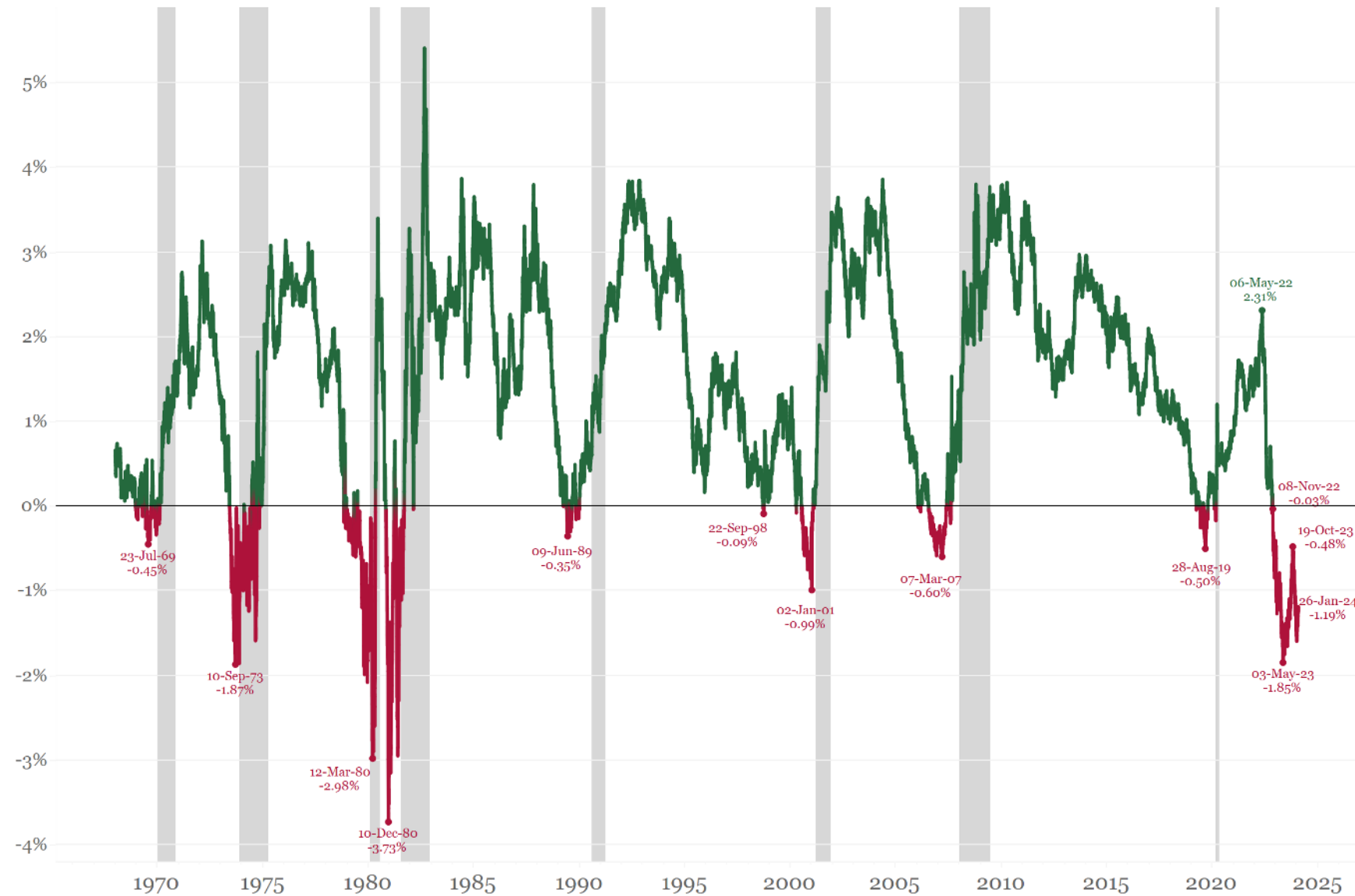


Data Source: Bloomberg, BankRate.com

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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 3-month to 10-year yield curve uninverts for 10 consecutive days

| Date of Inversion | Date of Uninversion | Days Inverted | Date of Next Recession | Calendar Days to Recession From | |
|-------------------|---------------------|---------------|------------------------|---------------------------------|-----------|
| Inversion Date | Unversion Date | | | | |
| 1/10/1969 | 2/21/1969 | 42 | Dec-69 | 325 | 283 |
| 6/14/1973 | 9/30/1974 | 473 | Nov-73 | 140 | -333 |
| 12/8/1978 | 5/13/1980 | 522 | Jan-80 | 389 | -133 |
| 11/7/1980 | 3/31/1981 | 144 | Jul-81 | 236 | 92 |
| 6/6/1989 | 9/7/1989 | 93 | Jul-90 | 390 | 297 |
| 7/31/2000 | 2/8/2001 | 192 | Mar-01 | 213 | 21 |
| 8/1/2006 | 6/11/2007 | 314 | Dec-07 | 487 | 173 |
| 6/6/2019 | 10/23/2019 | 139 | Feb-20 | 268 | 129 |
| 11/22/2022 | ???? | 436 | ???? | 436 | ???? |
| Average | | 262 | | 320 | 66 |

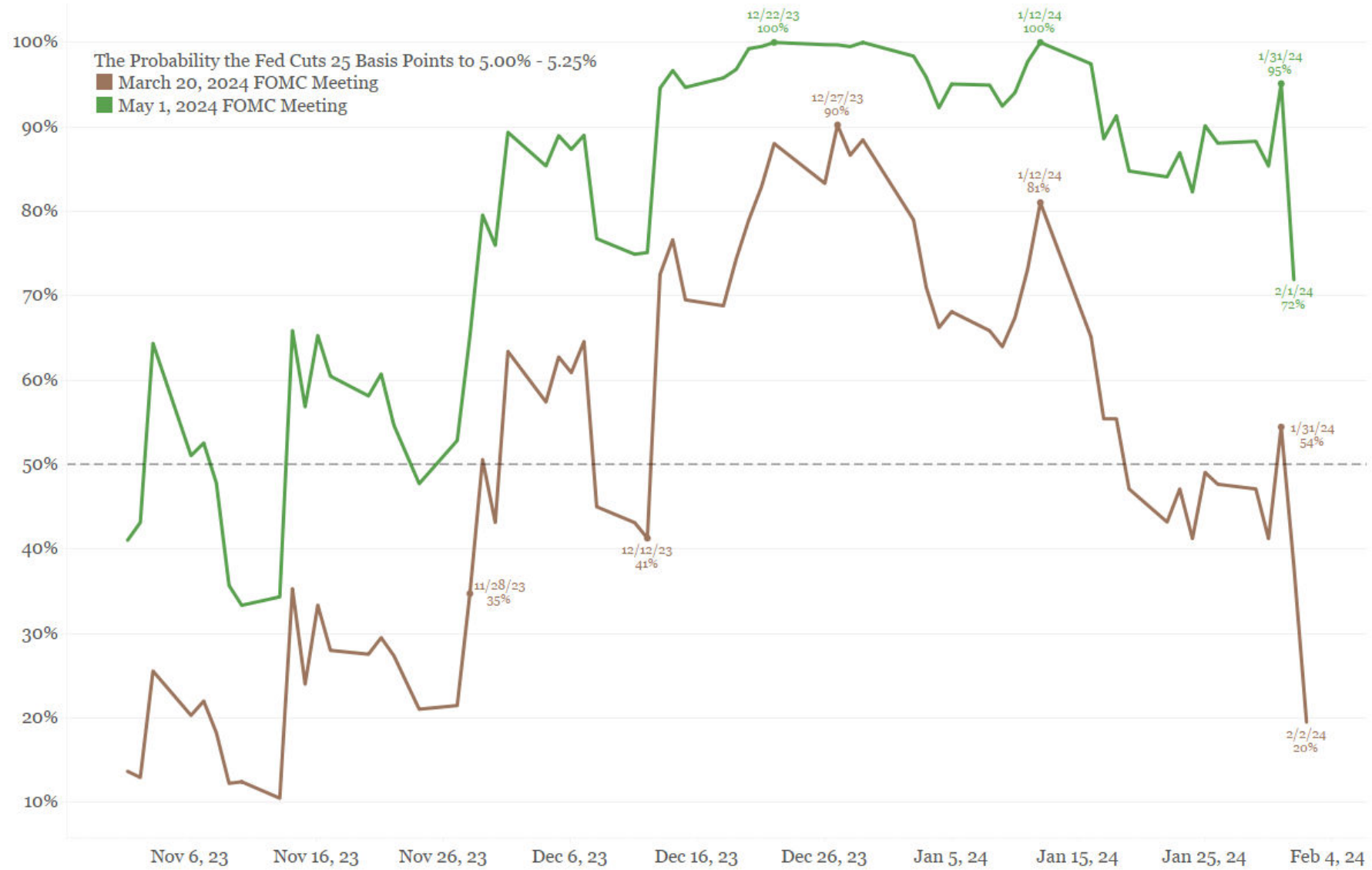
1/10/1969 = Inverted for 24 calendar days, went positive for 33 days, then inverted again for 53 days

6/6/1989 = Inverted for 30 calendar days, went positive for 9 days, inverted again for 26 days

6/6/2019 = Inverted 41 consecutive trading days, went positive for 1 day, then inverted again for 67 days (through

When Will the Fed Cut Rates?

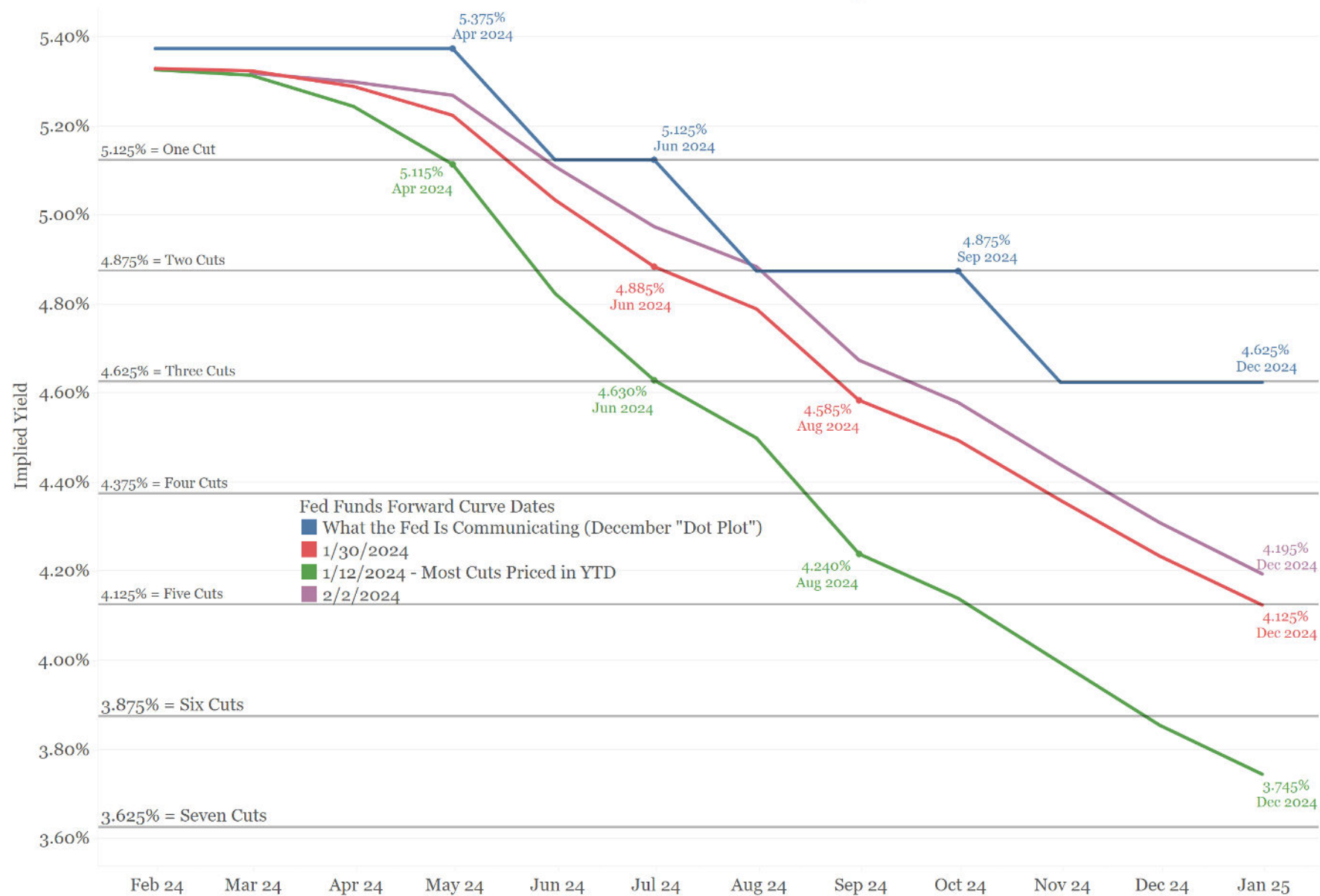
Odds the Fed Cuts the Target Rate to 5.00% to 5.25%
As Calculated by the Chicago Mercantile Exchange's Fed Watch Tool



Source: Chicago Mercantile Exchange
<https://www.cmegroup.com/trading/interest-rates/countdown-to-fomc.html>

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What Is the Fed Funds Market Pricing In?



Source: Chicago Mercantile Exchange, Bloomberg

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10-Year Treasury Yield



Source: U.S. Treasury & The Federal Reserve

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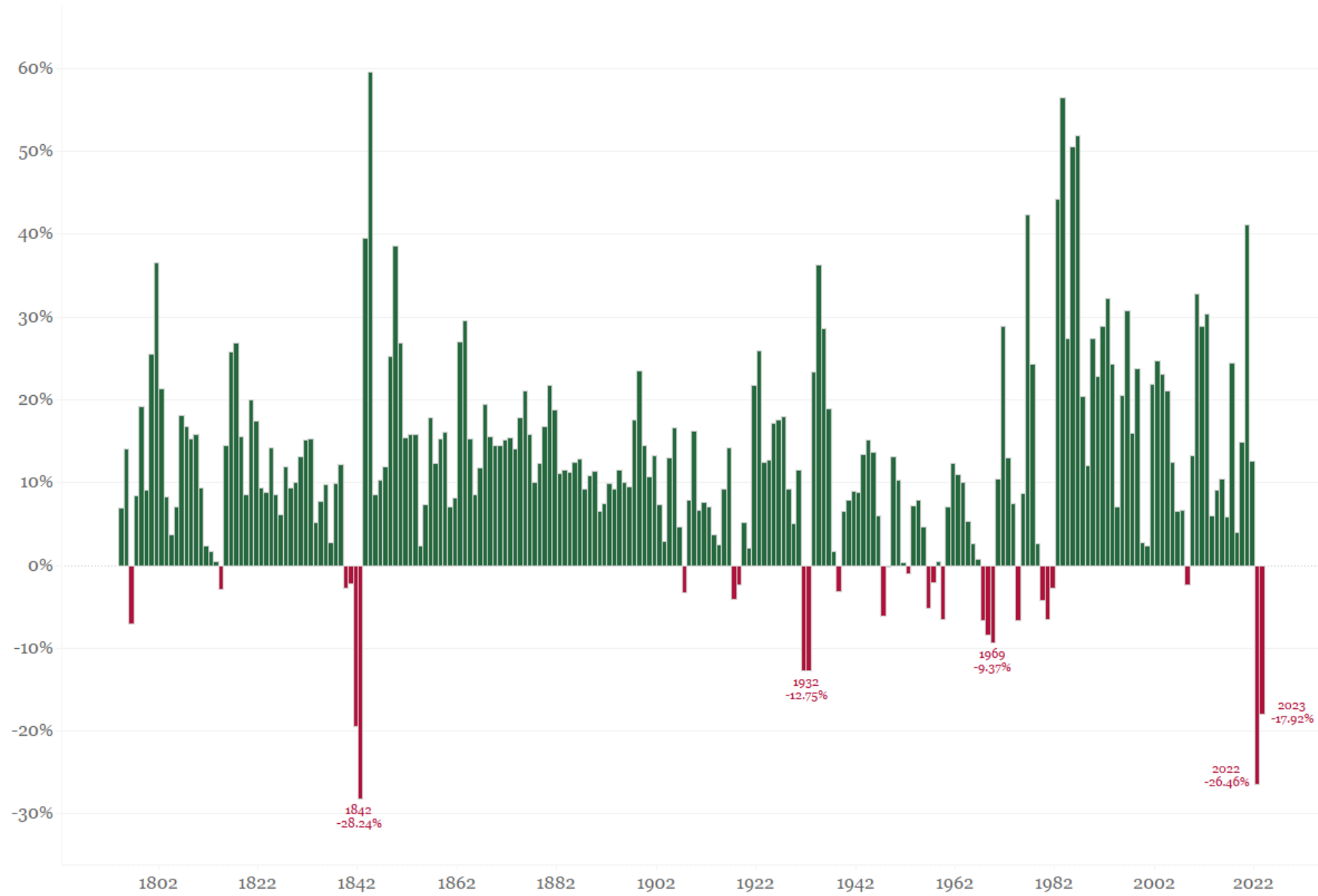
US 10-Year Yield



Source: Bloomberg

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Rolling Three-Year US Long-Term Nominal (Before Inflation) Bond Total Returns



Source: Edward F. McQuarrie
<http://www.edwardfmcquarrie.com/wp-content/uploads/2021/07/Real-returns-on-stocks-and-bonds-1793-to-2019-version-2-0.xlsx>

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Bloomberg – (November 29, 2023) Bill Ackman Bets Fed Will Cut Interest Rates as Soon as First Quarter

What’s happening is the real rate of interest, which is what impacts the economy, keeps increasing as inflation declines,” Ackman said in an upcoming episode of The David Rubenstein Show: Peer-to-Peer Conversations. Ackman said that if the Fed keeps rates in the roughly 5.5% range when inflation trends below 3%, “that’s a very high real rate of interest.”

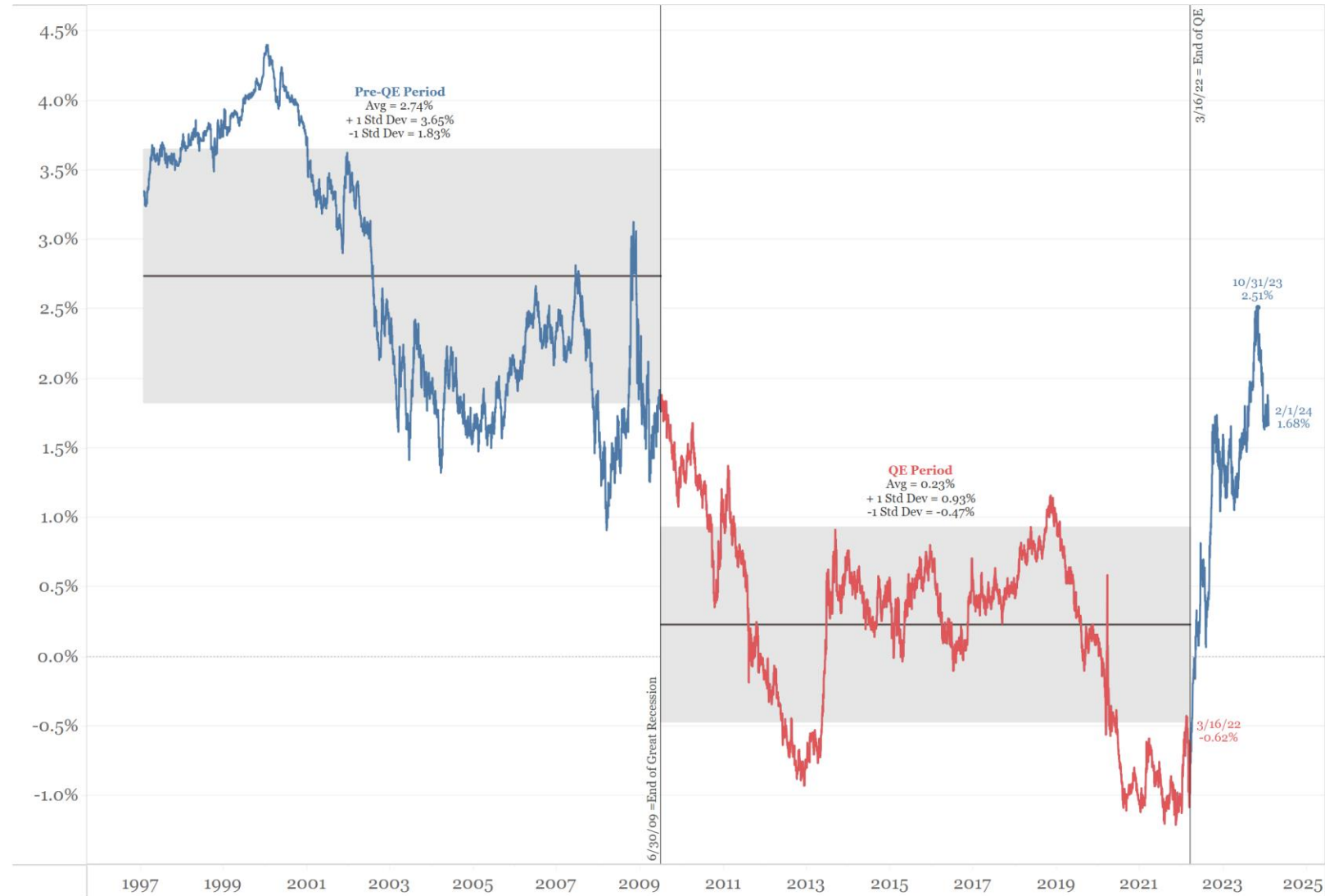
The Wall Street Journal – (December 19, 2023) Nick Timiraos: Fed Official Says Rate Cuts Could Be Needed Next Year to Prevent Overtightening

San Francisco Fed President Mary Daly said her outlook for interest rates and inflation was “very close” to the median of projections from 19 Fed officials last week. Most of them penciled in at least three rate cuts next year amid a faster decline in inflation than they anticipated...Daly said that if inflation continues its steady decline of recent months, the Fed’s benchmark interest rate “will still be quite restrictive even if we [cut rates] three times next year.”

Bloomberg – (January 22, 2024) Fed Should Stop Quantitative Tightening, Reduce Interest Rates Soon, Bill Gross Says

“Real interest rates are simply too high,” Gross added. Yields on 10-year inflation-linked bonds, which are viewed as a measure of the true cost of borrowing, surged to a 15-year high of 2.6% in October, before sliding down to about 1.8%, currently. Gross said he’d like to see the yields fall to about 1% to 1.5%, so that “the economy will not go into a significant recession.”

US 10-Year TIPS Yield

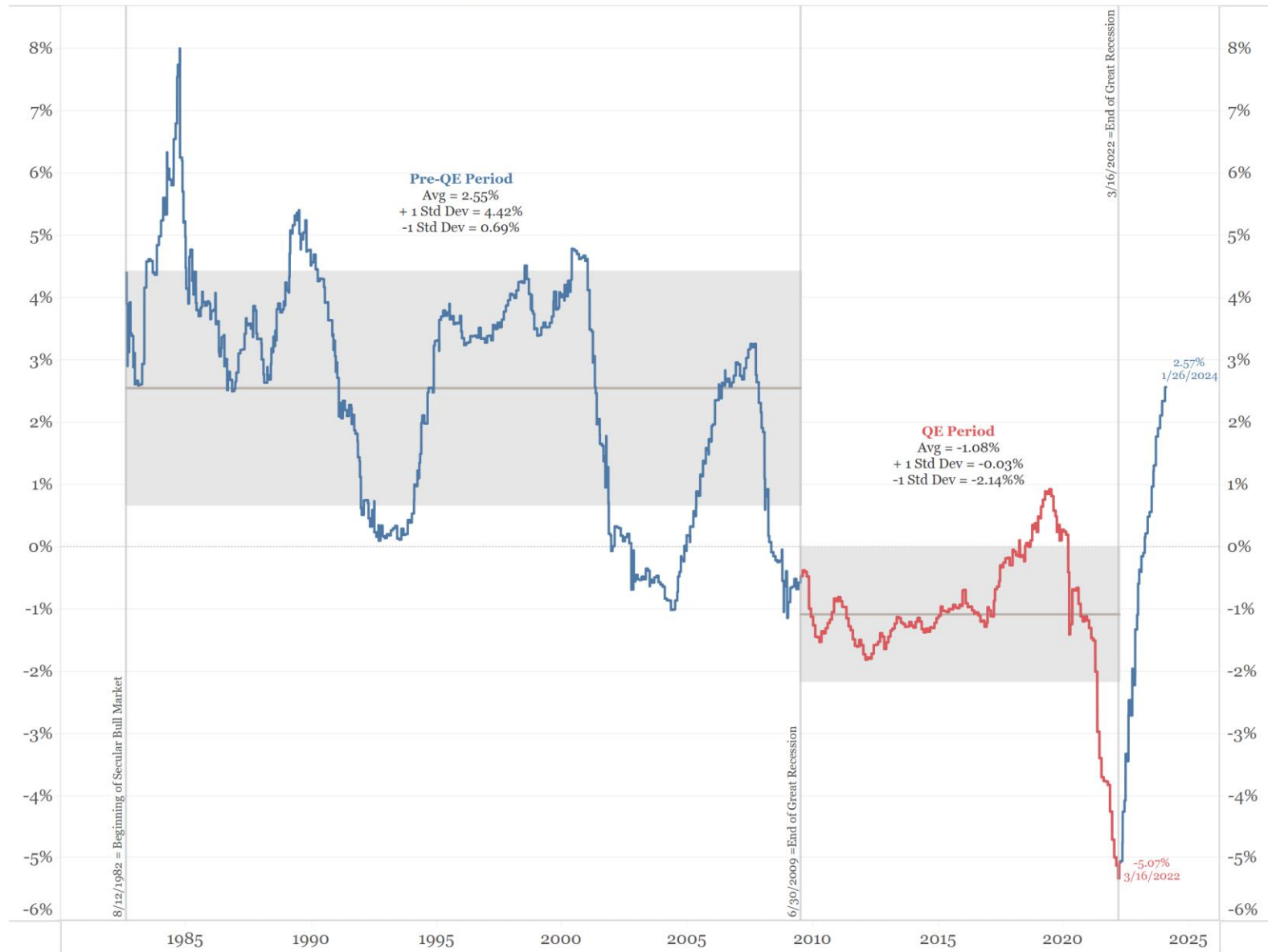


Source: Bloomberg

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The Real Fed Funds Rate

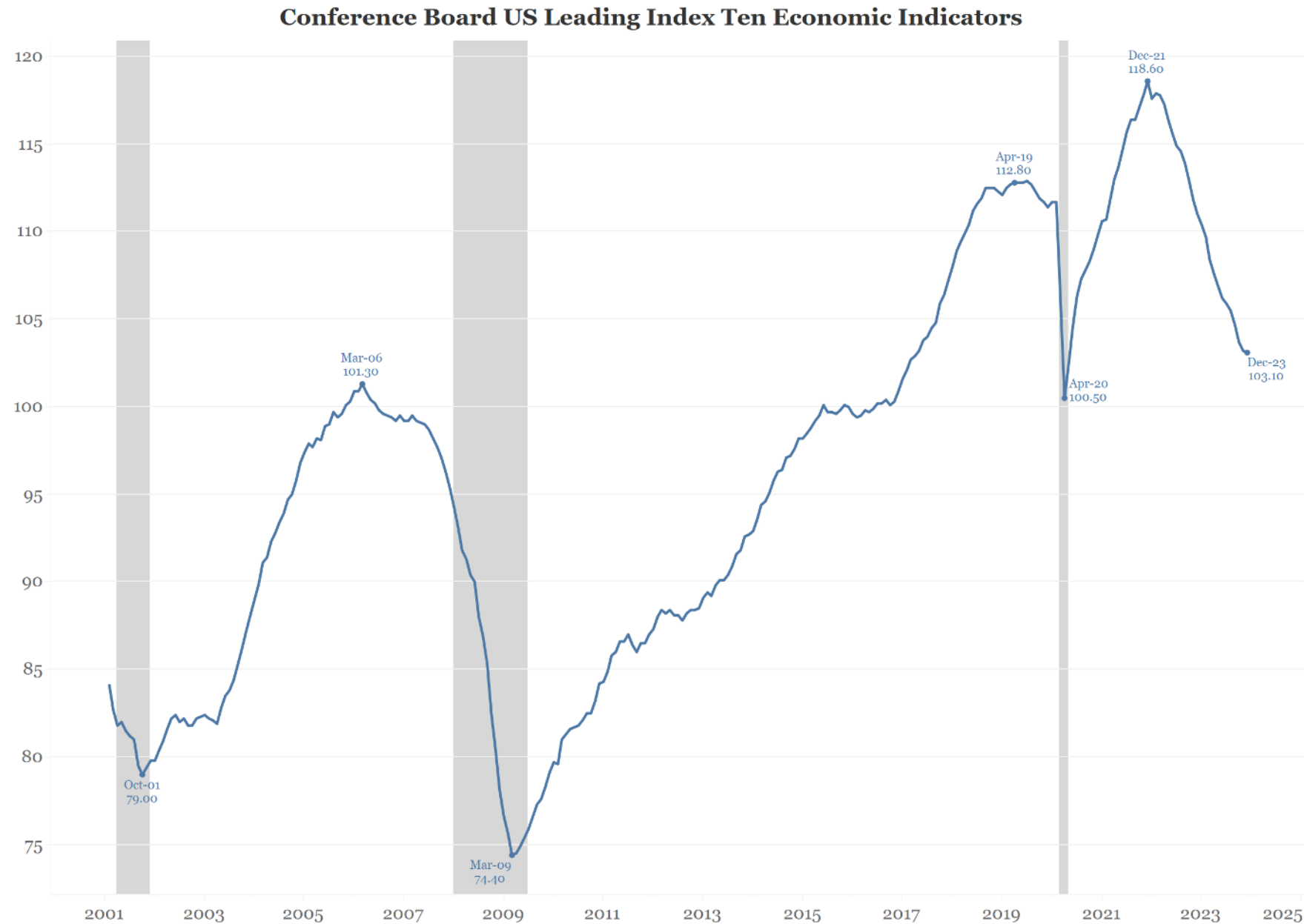
Upper End of Fed's Target Range Minus Core PCE



Source: Bloomberg

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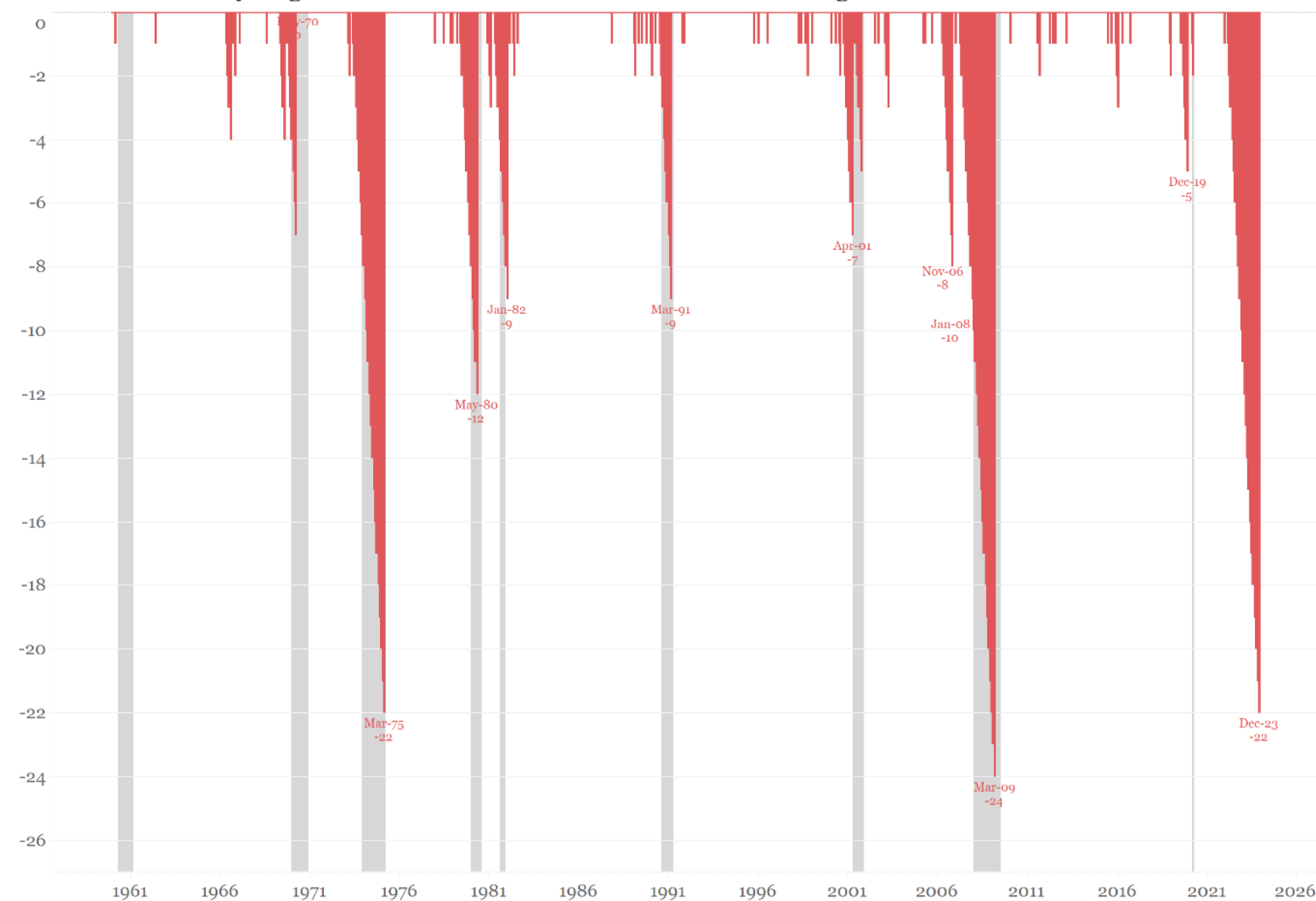
*All models are wrong.
Some models are useful
– George Box*



Source: Bloomberg, Conference Board
<https://www.conference-board.org/topics/us-leading-indicators>

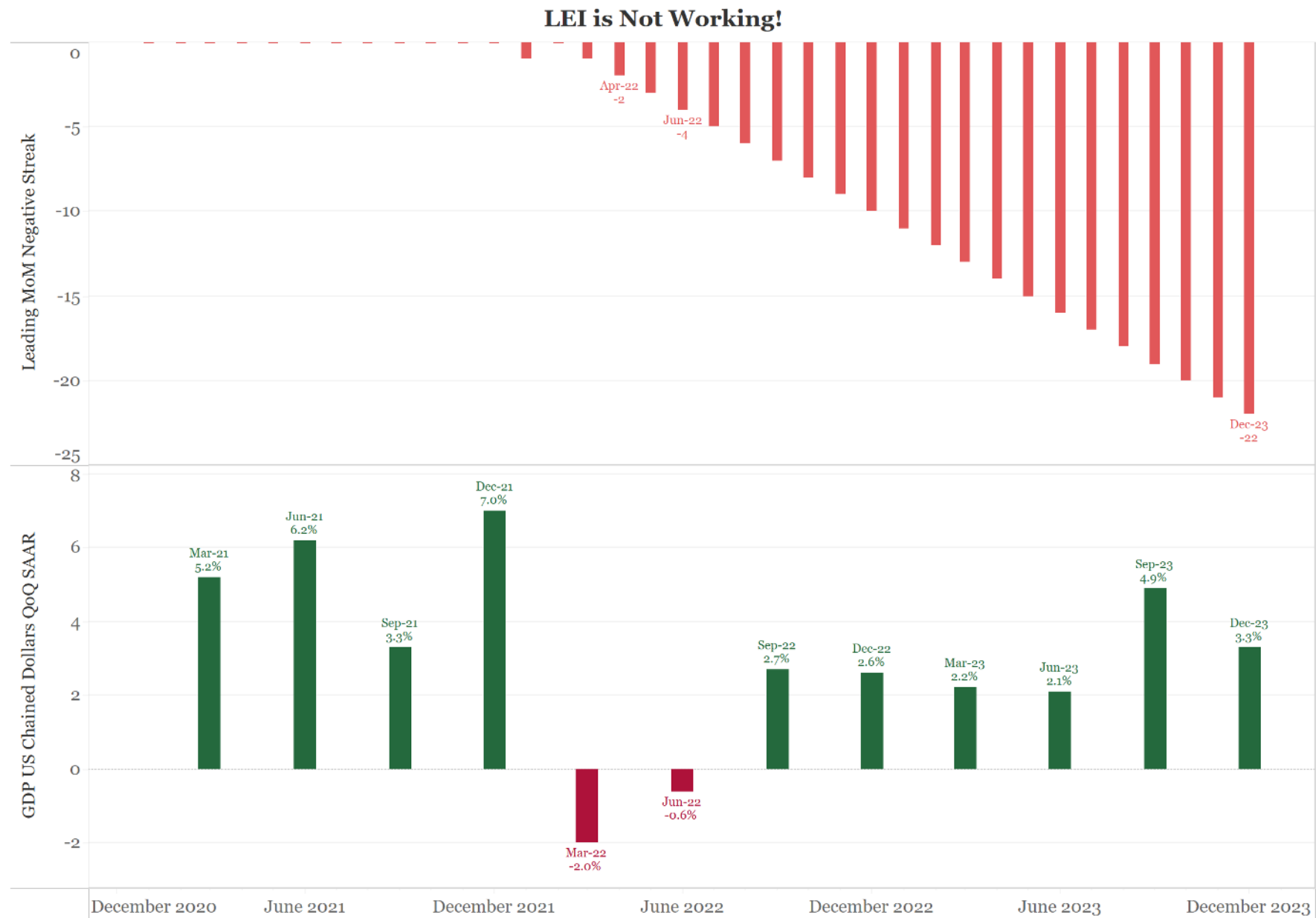
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Monthly Negative Streak in the Conference Board Leading Economic Indicator Index



Source: Bloomberg, Conference Board
<https://www.conference-board.org/topics/us-leading-indicators>

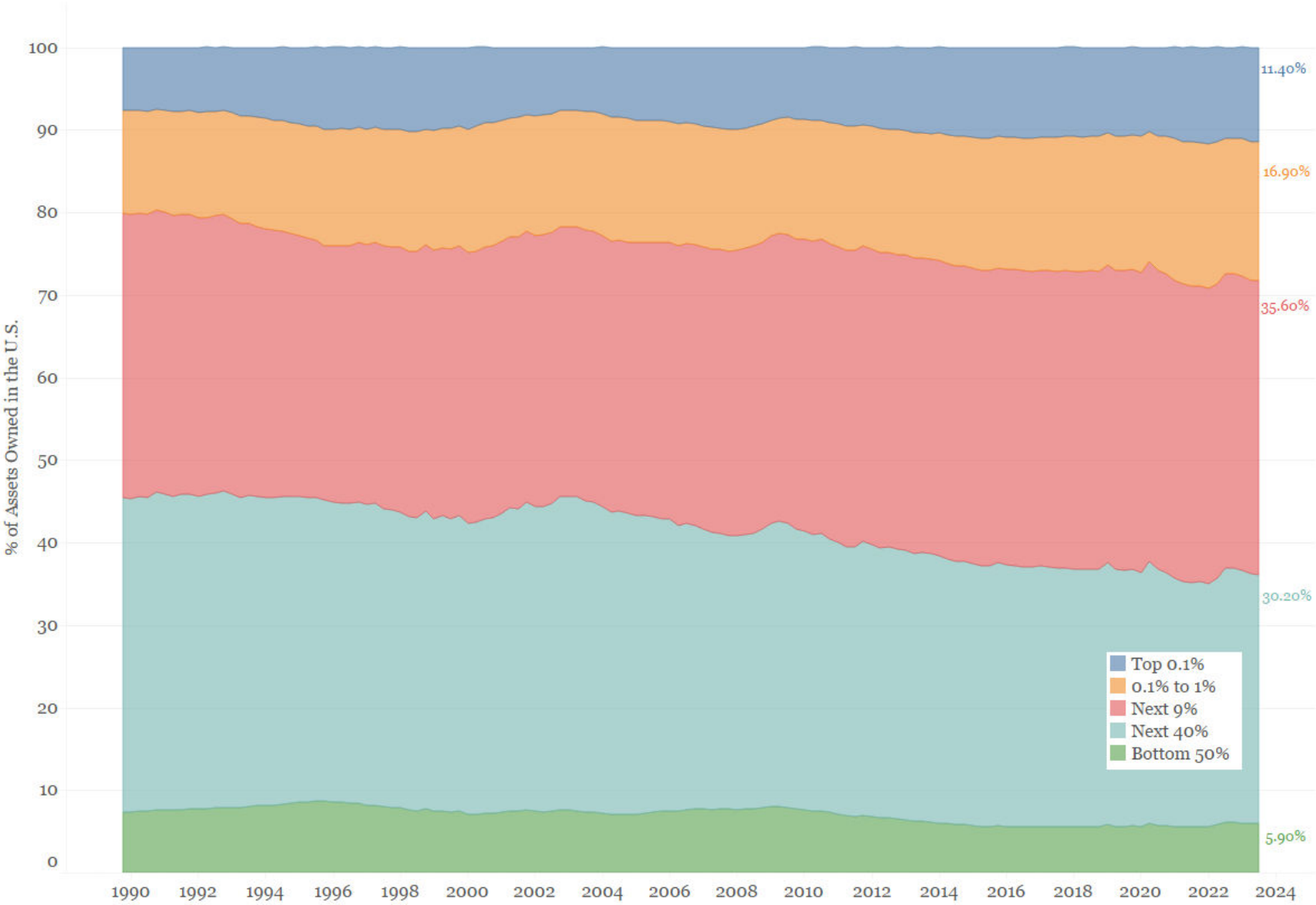
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Source: Bloomberg, Conference Board
<https://www.conference-board.org/topics/us-leading-indicators>

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Distribution of Assets in the U.S.

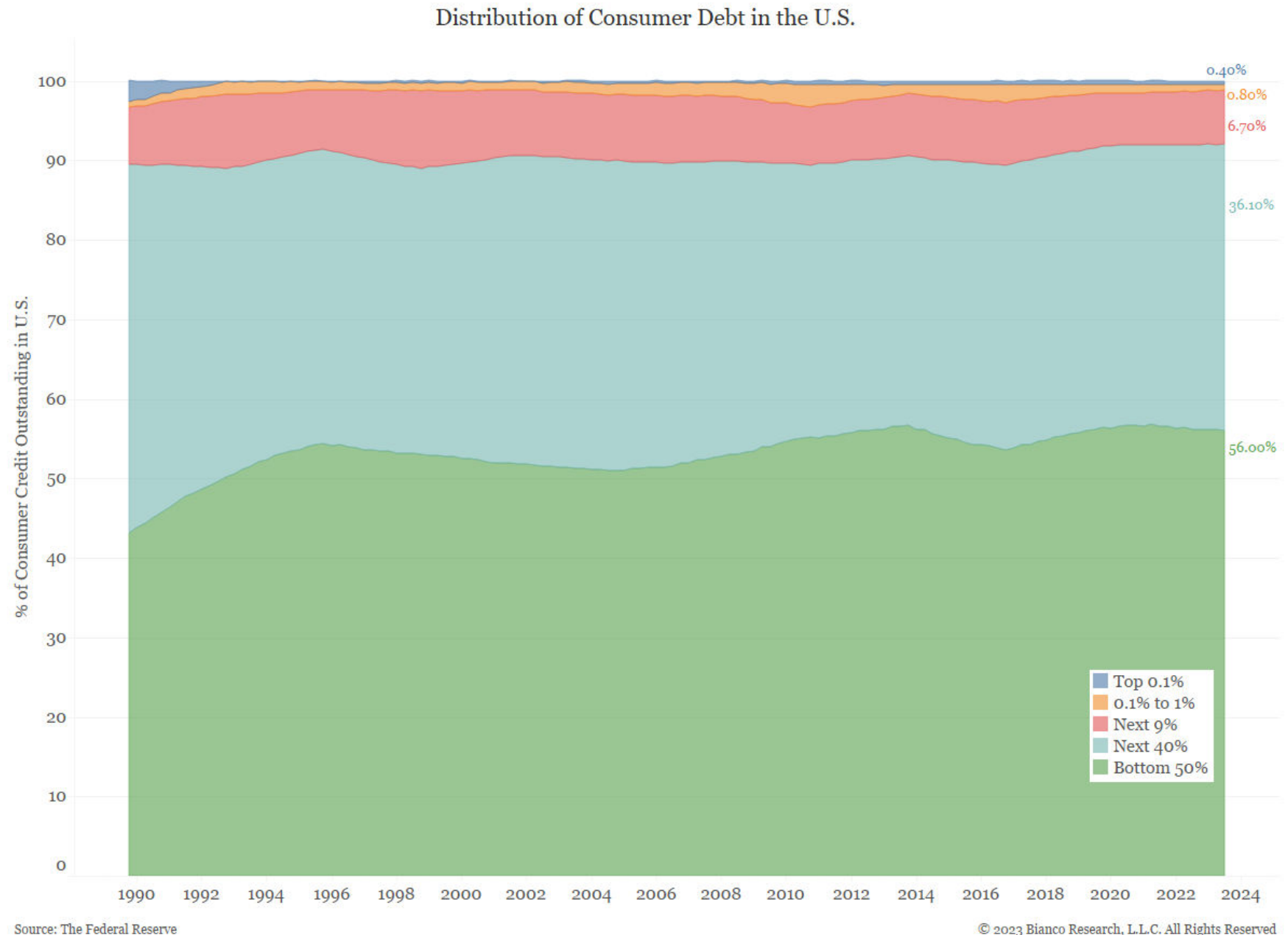


Source: The Federal Reserve

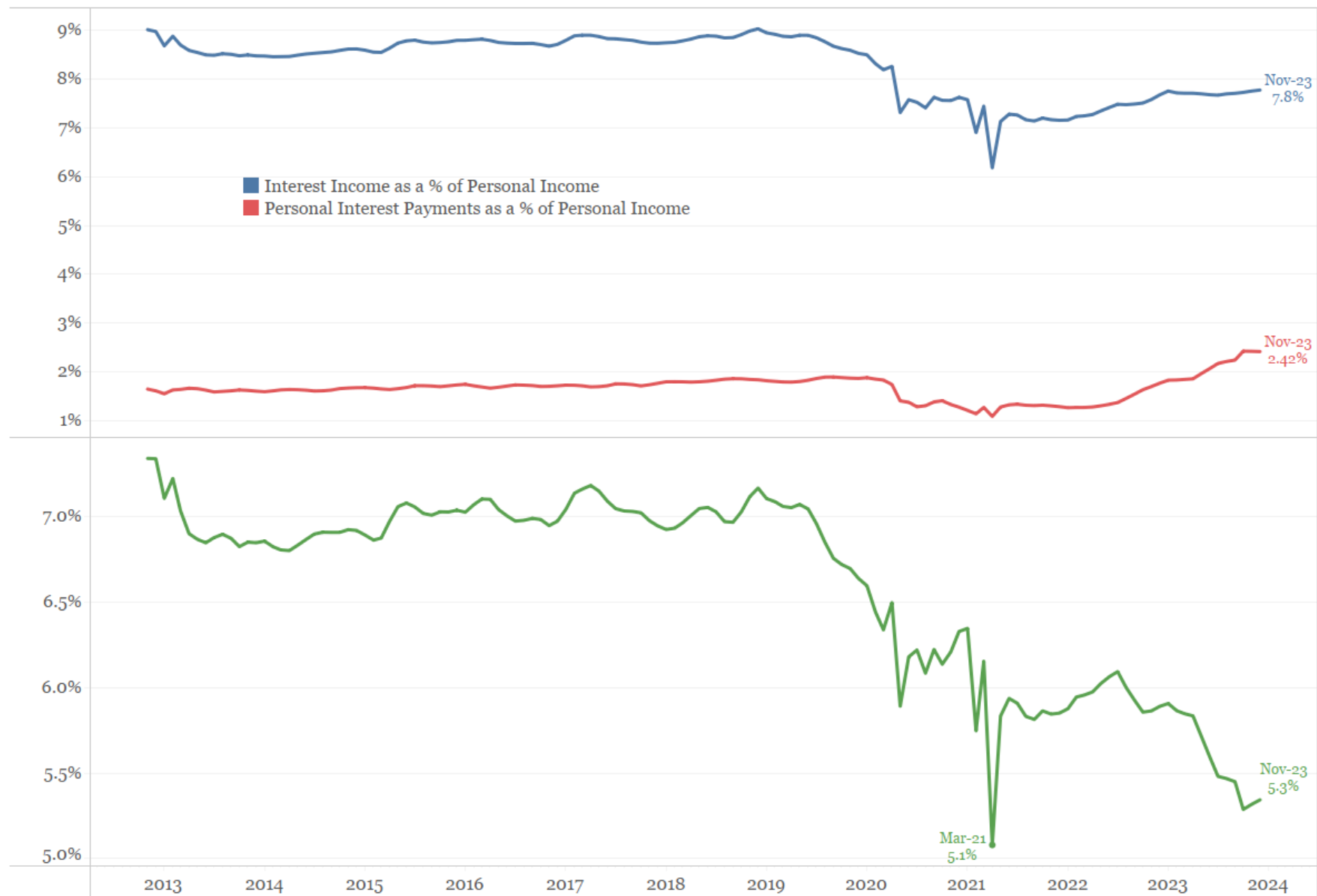
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•CNBC - (December 20, 2023) [62% of Americans are living paycheck to paycheck, as holiday spending, credit card debt rise](#)

Half of consumers plan to take on more debt to cover those holiday expenses, according to another report by Ally Bank. Only 23% have a plan to pay it off within one to two months. "Not only is sticking to a budget harder today," said Sarah Foster, a Bankrate analyst, "but it's all the more imperative, too." "Credit card financing rates have hovered at the highest levels ever recorded since last fall, meaning carrying a balance could cost a heavy price," she said.



Personal Interest Expense and Income



Data: BEA

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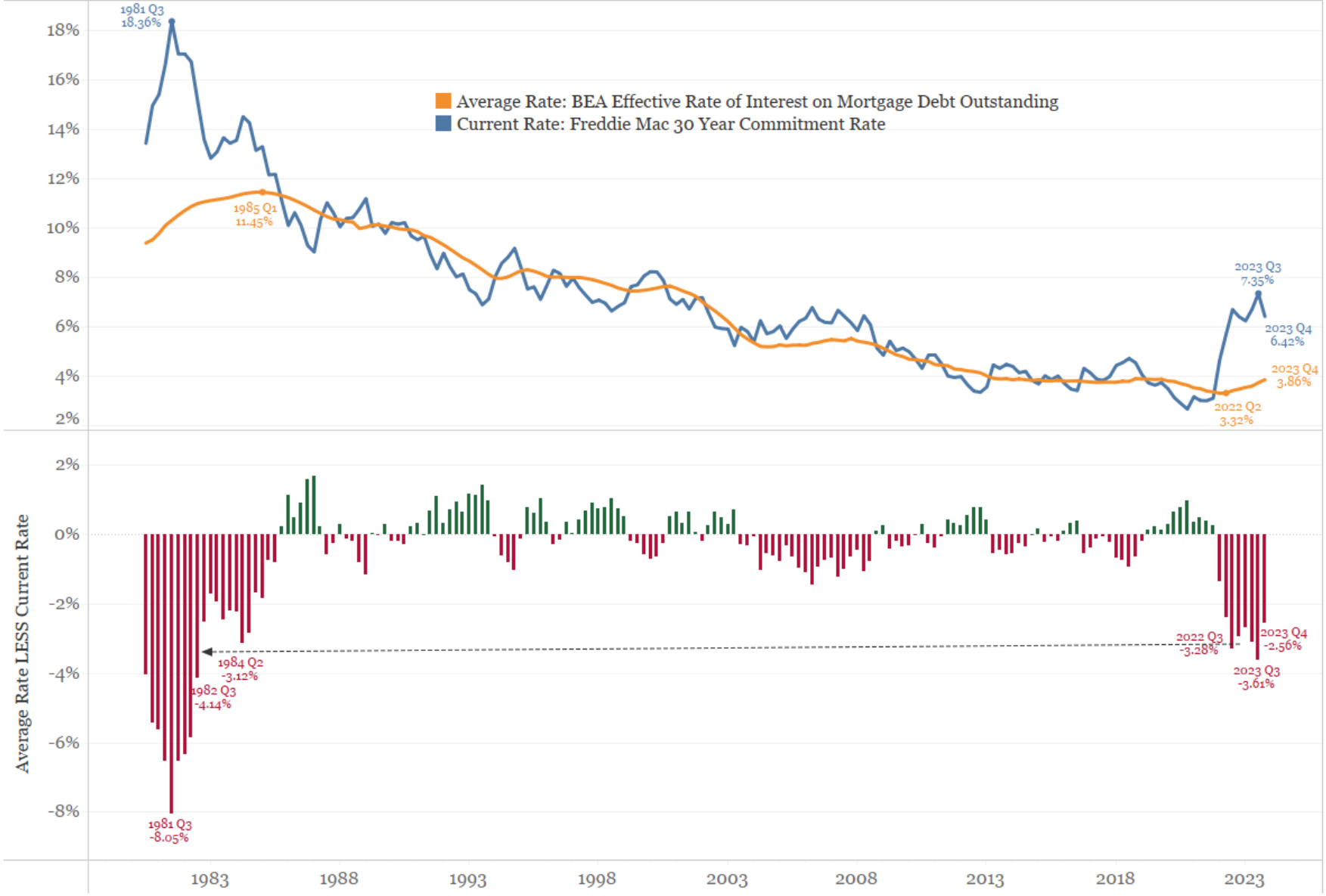
Non-Financial Corporation Net Interest Payments



Data: BEA
<https://www.bea.gov/itable>

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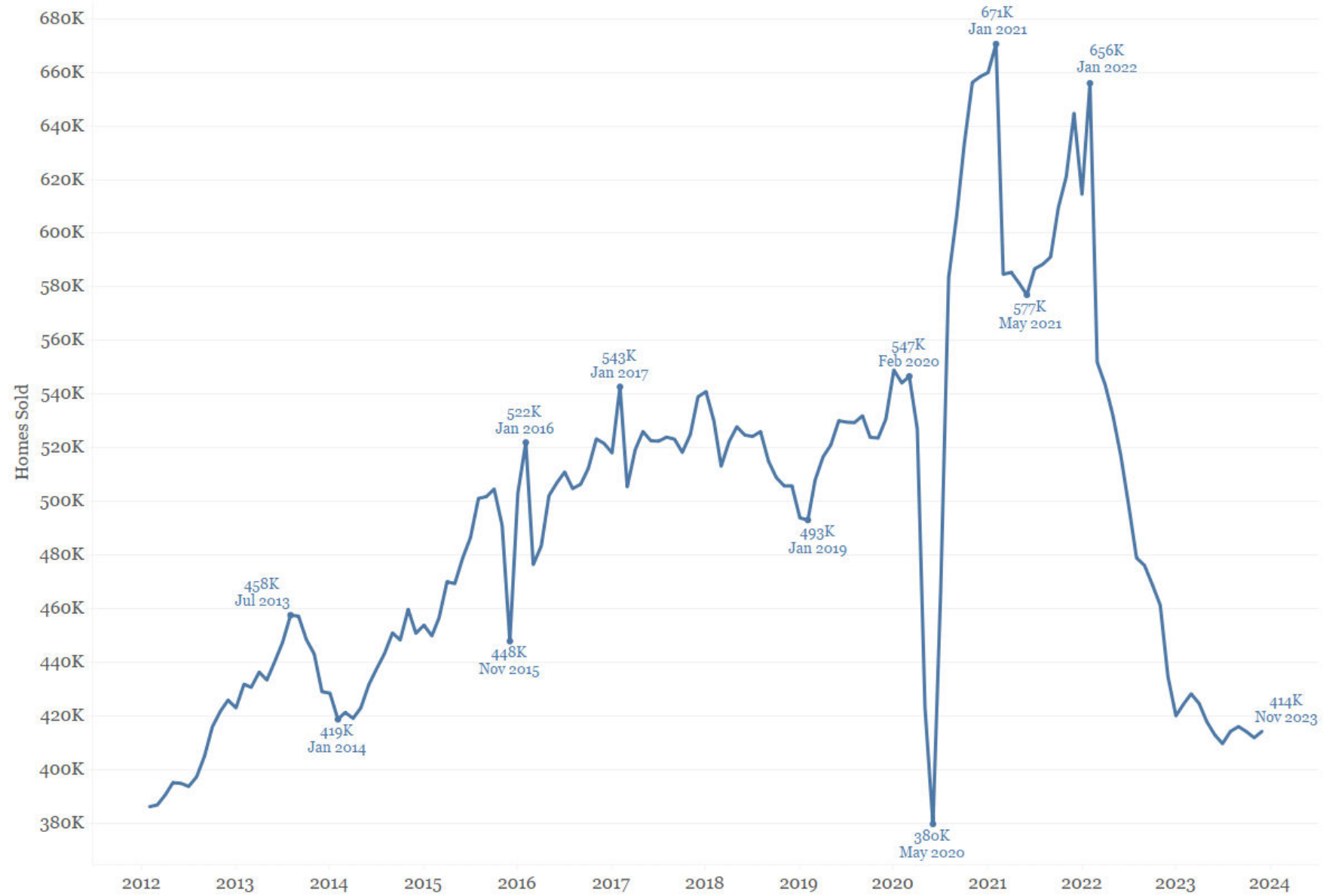
The Average and Current Mortgage Rate



Data Source: Bloomberg, Freddie Mac, Bureau of Economic Analysis (BEA)

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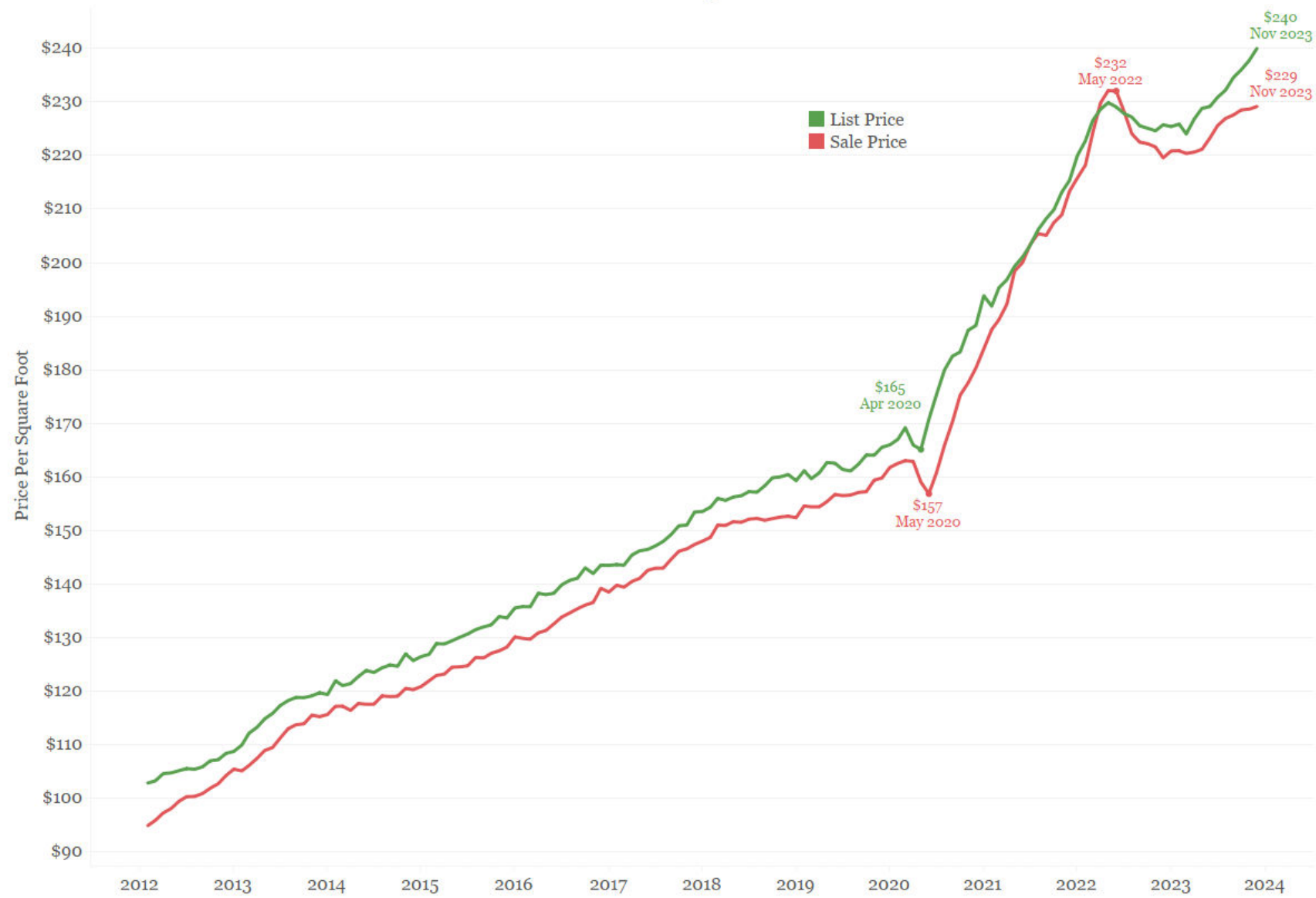
Homes Sold Each Month



Source: Redfin

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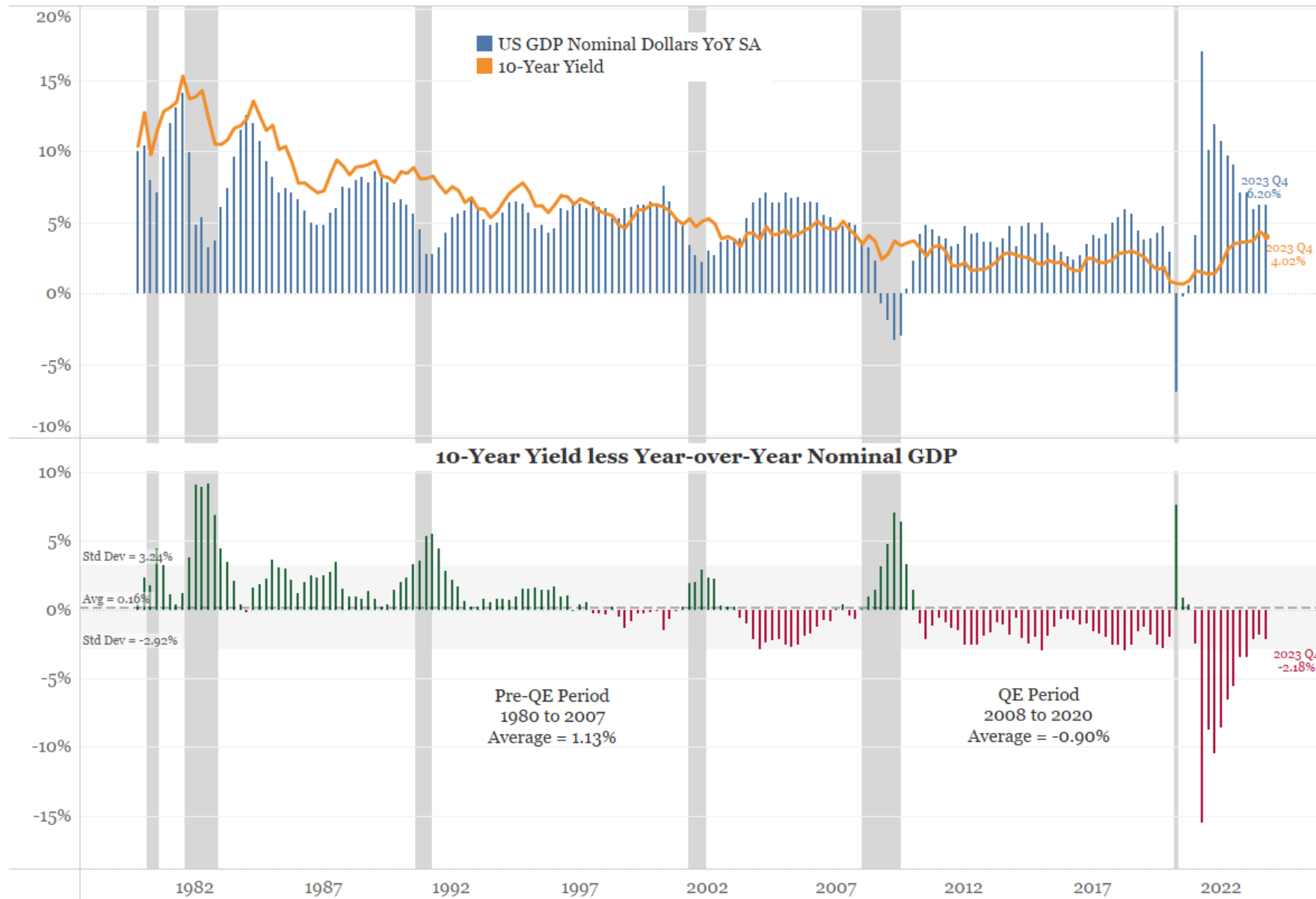
Median Price Per Square Foot



Source: Redfin

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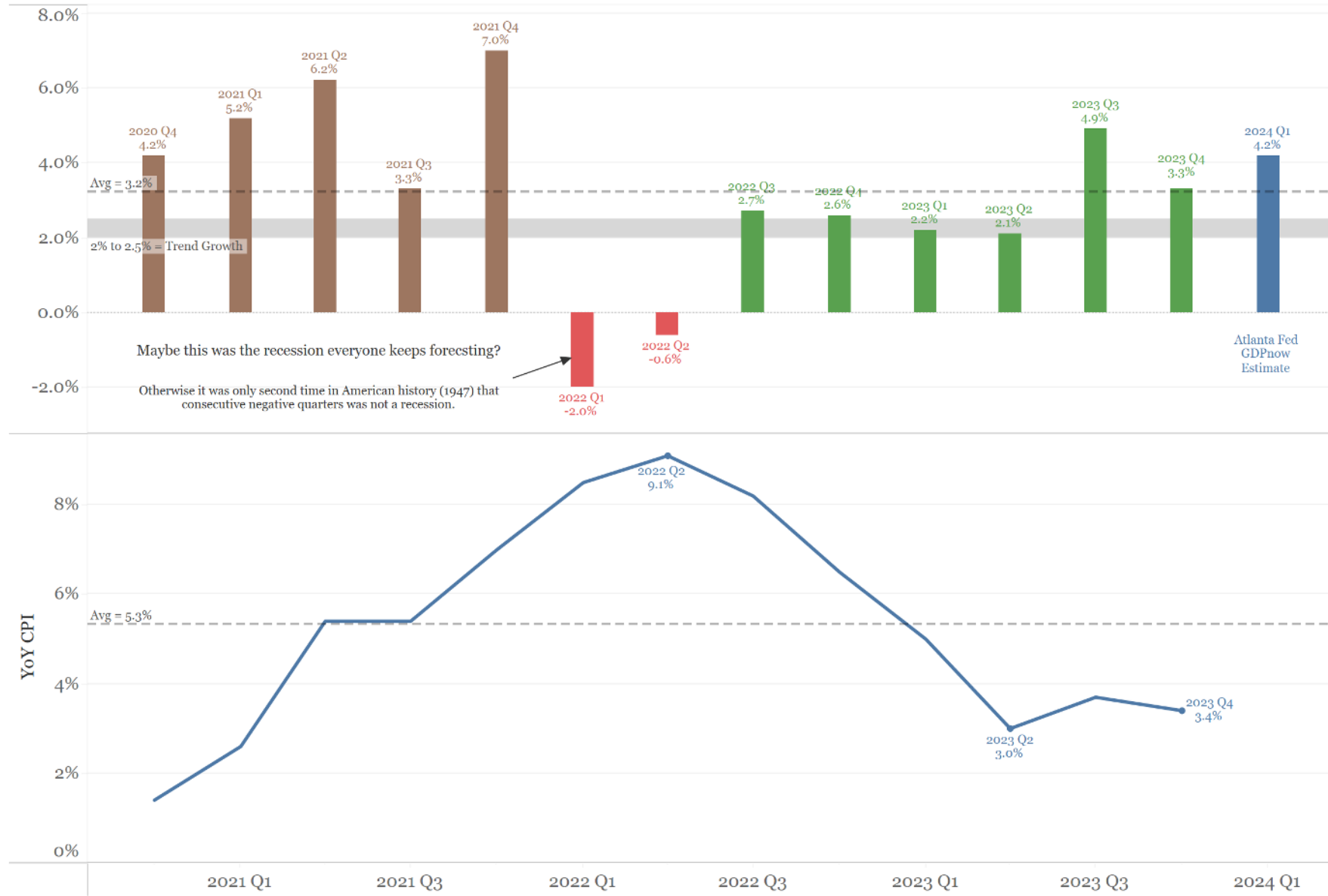
Year-Over-Year Nominal GDP and 10-Year Yield



Data Source: Bloomberg

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GDP and Inflation Since The Lockdowns Ended

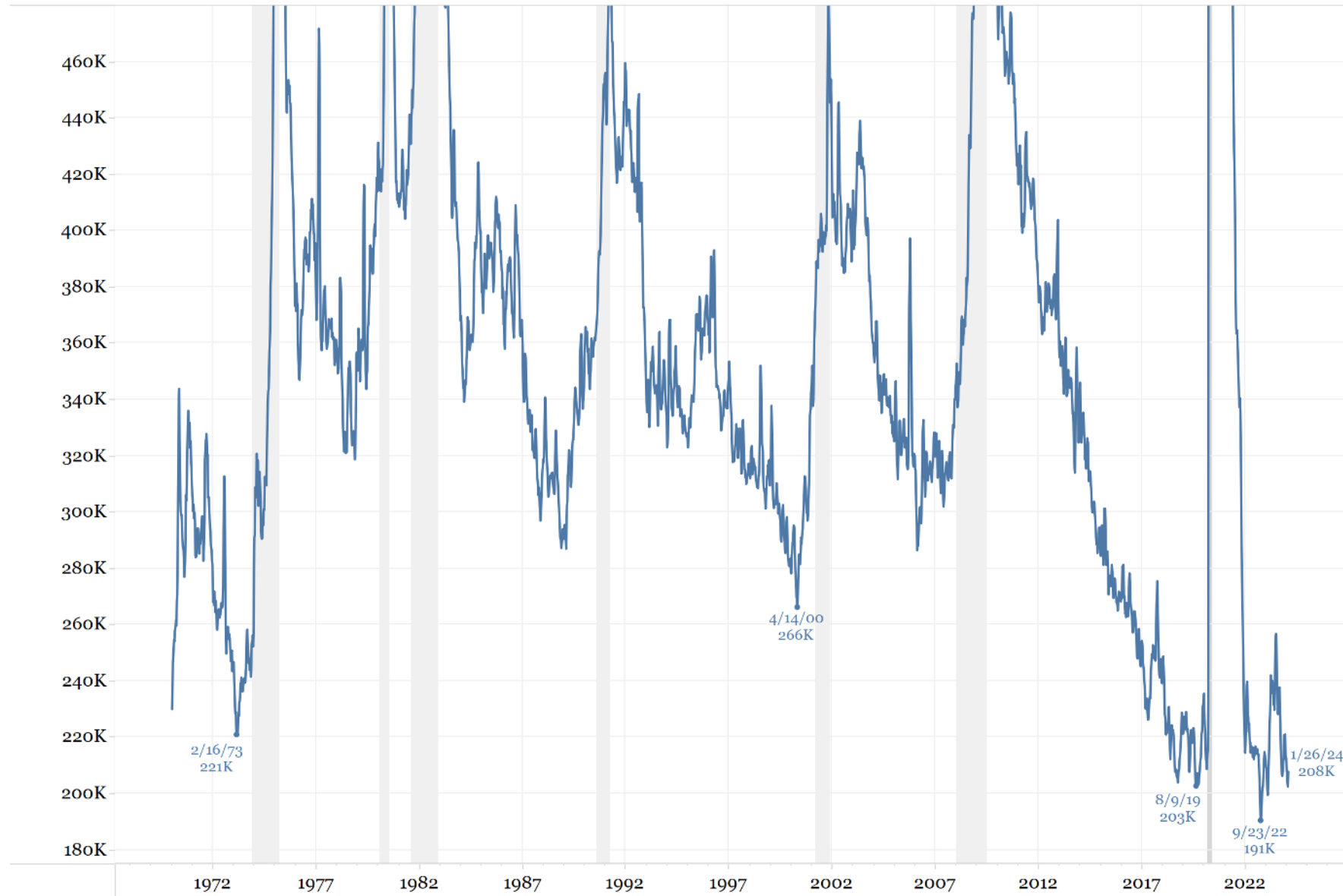


Data Source: Bloomberg

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Weekly Initial Claims - Focus on Cycle Lows

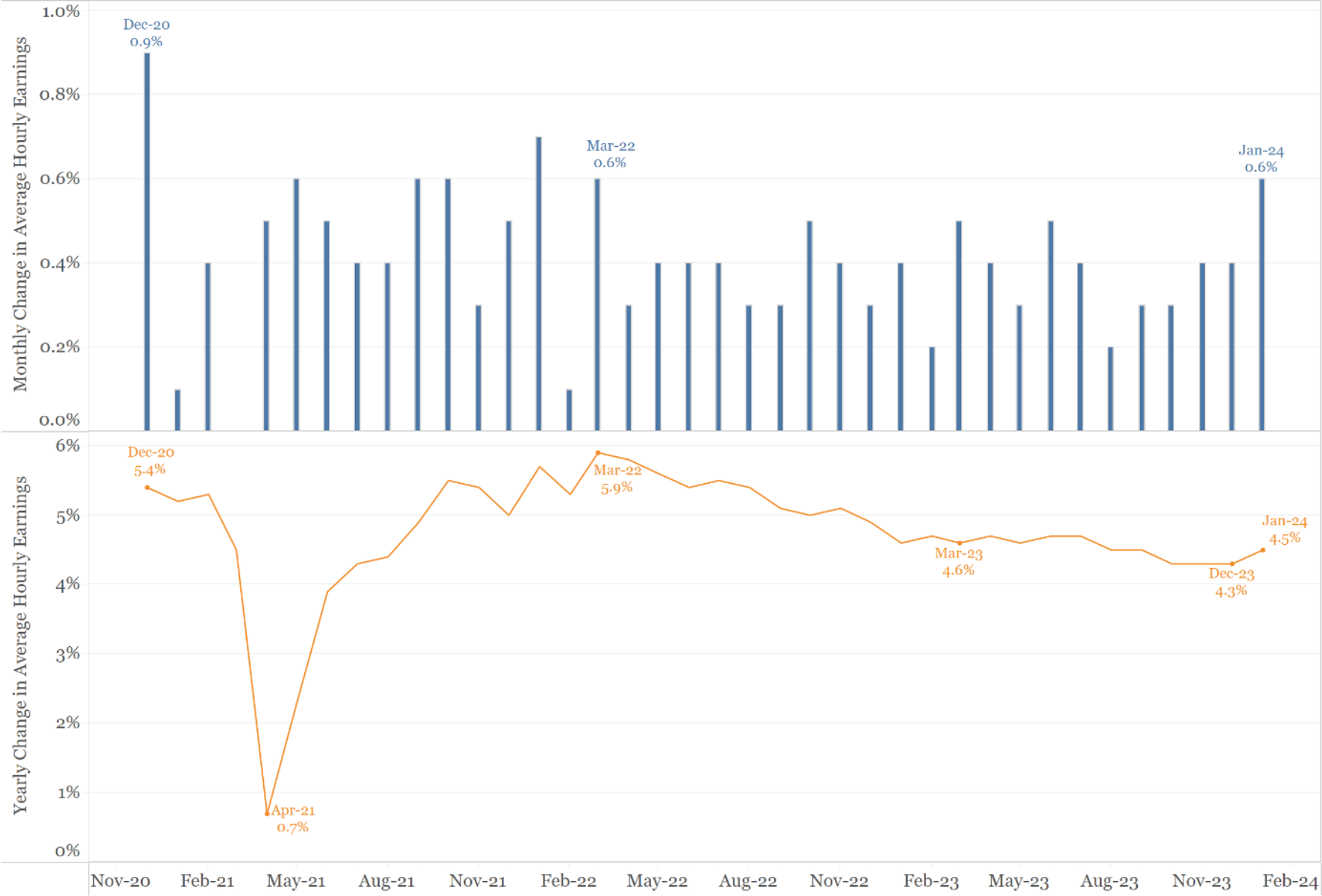
Rolling 4-Week Average



Data Source: Bureau of Labor Statistics

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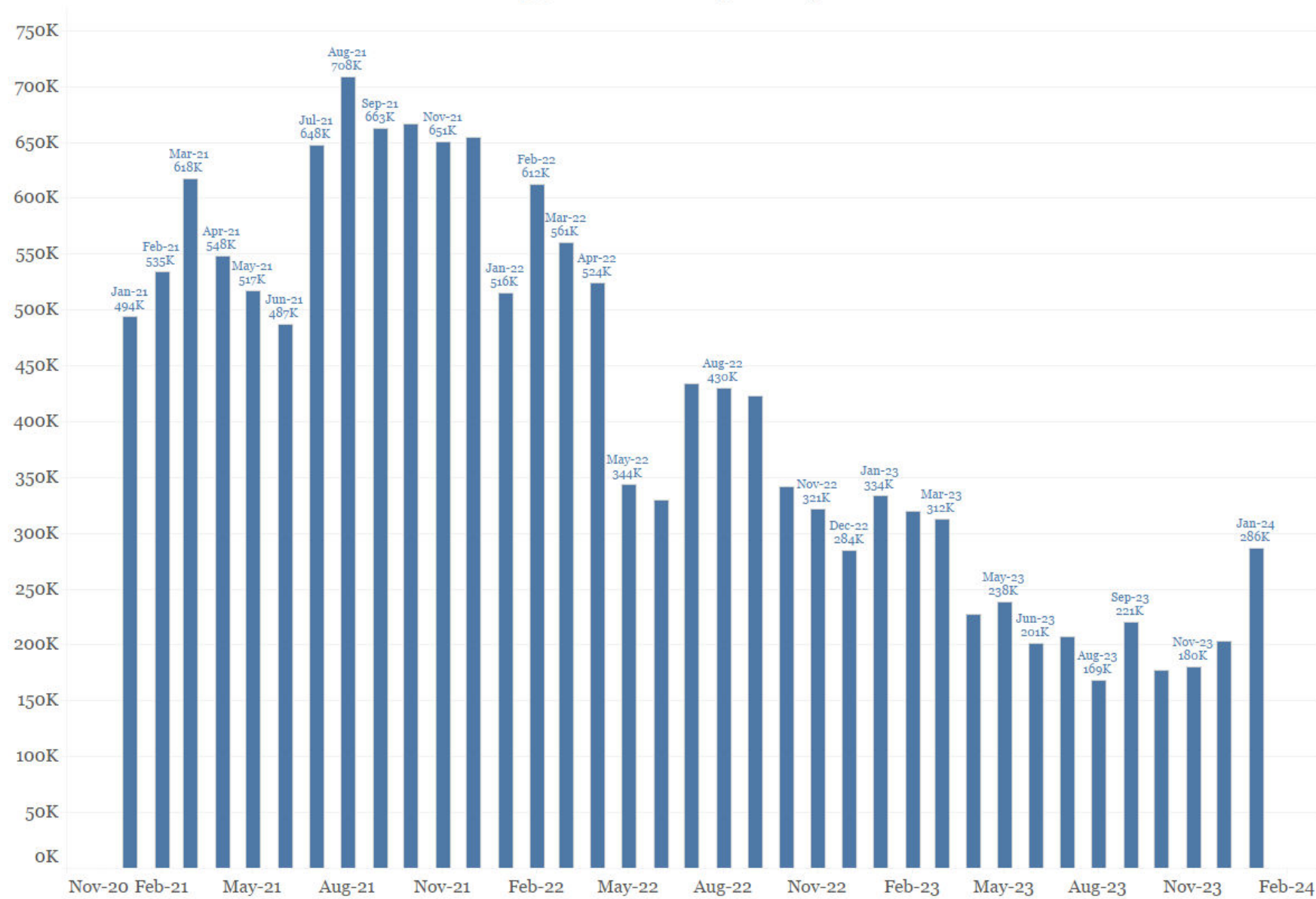
Average Hourly Earnings Growth



Source: Bureau of Labor Statistics

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Rolling 3-Month Average of Payrolls

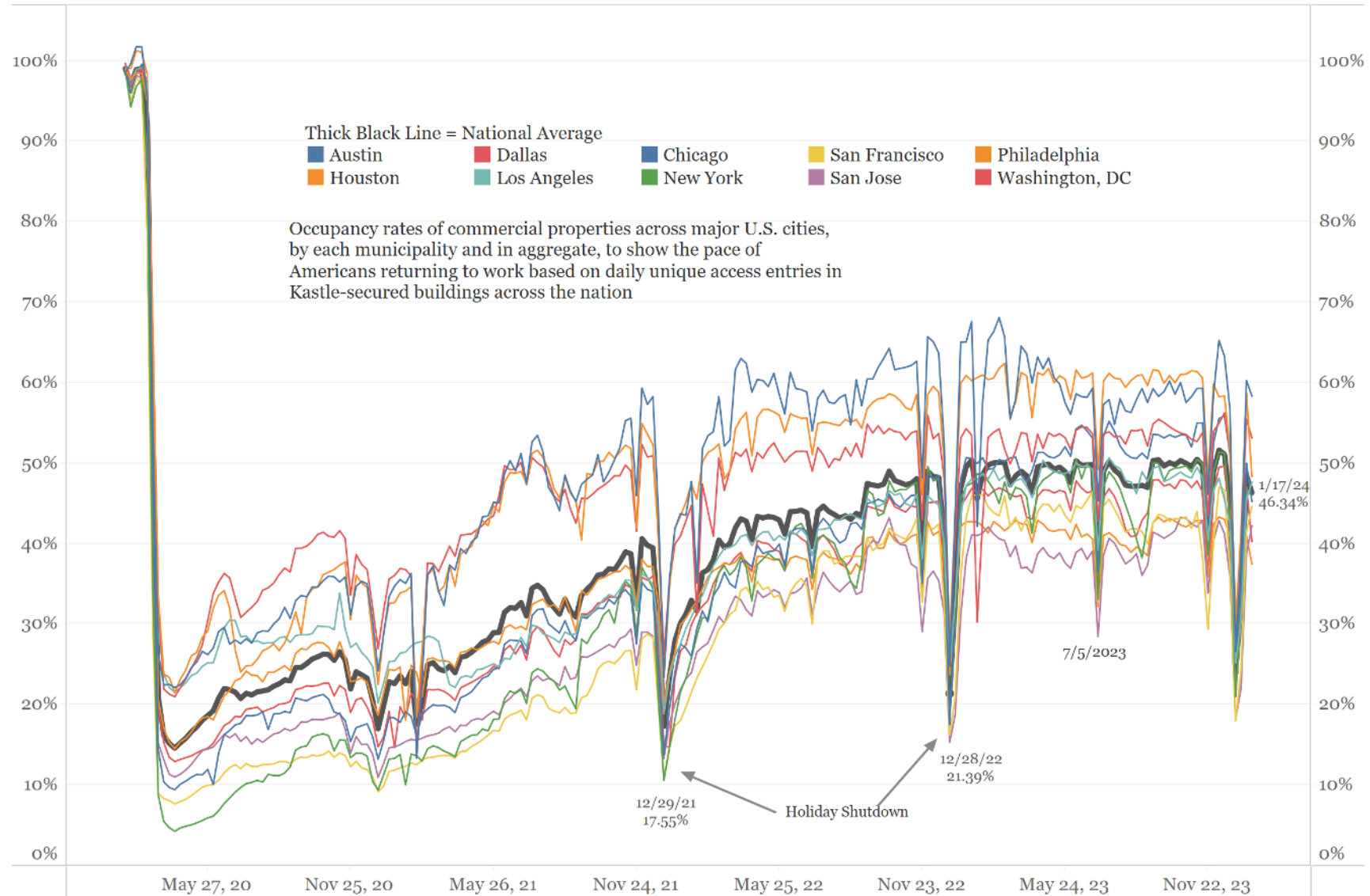


Source: Bloomberg

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Kastle Back to Work Indices

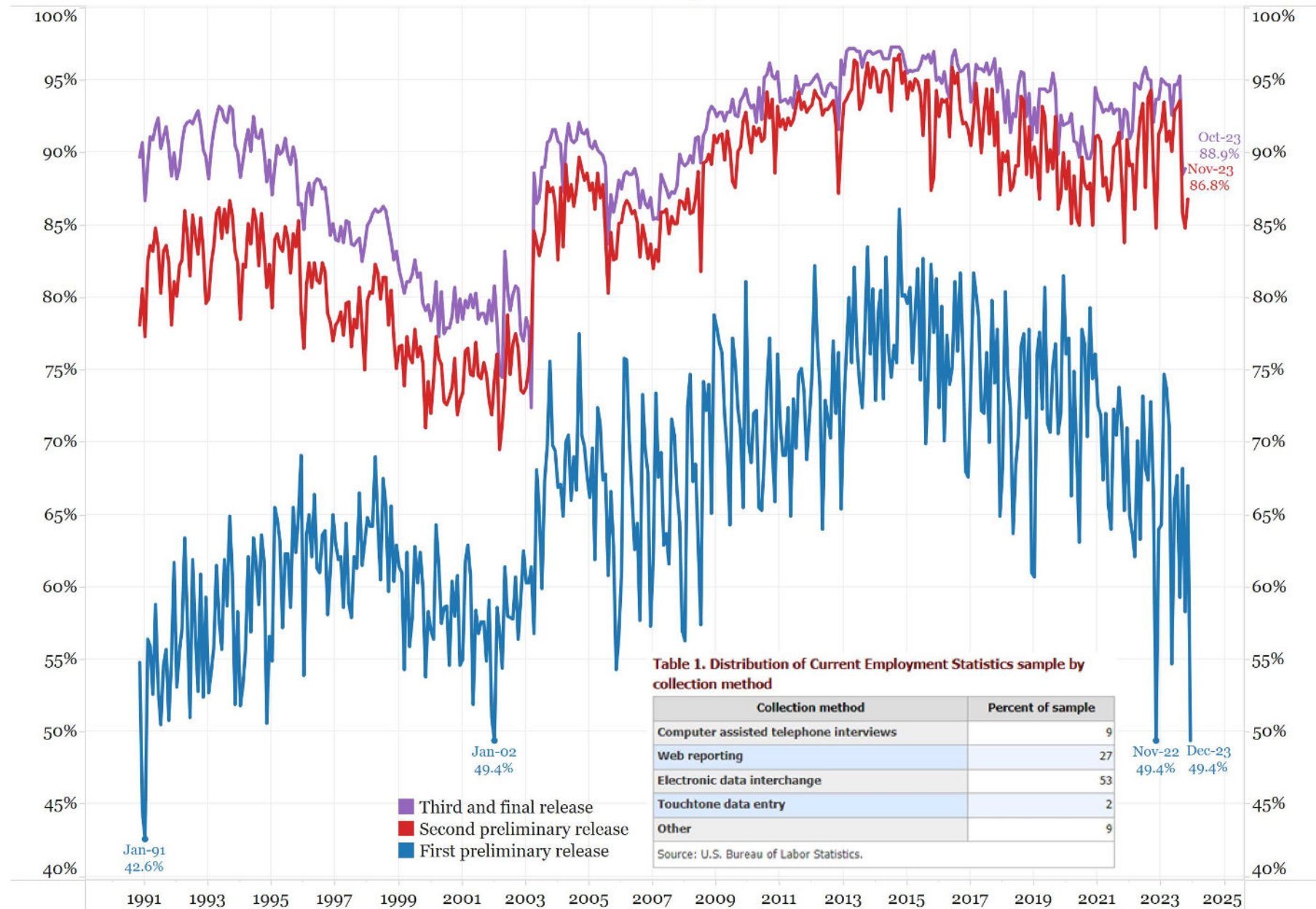
Percentage of City Office Space Currently in Use



Source: Kastle
<https://www.kastle.com/getting-america-back-to-work/>

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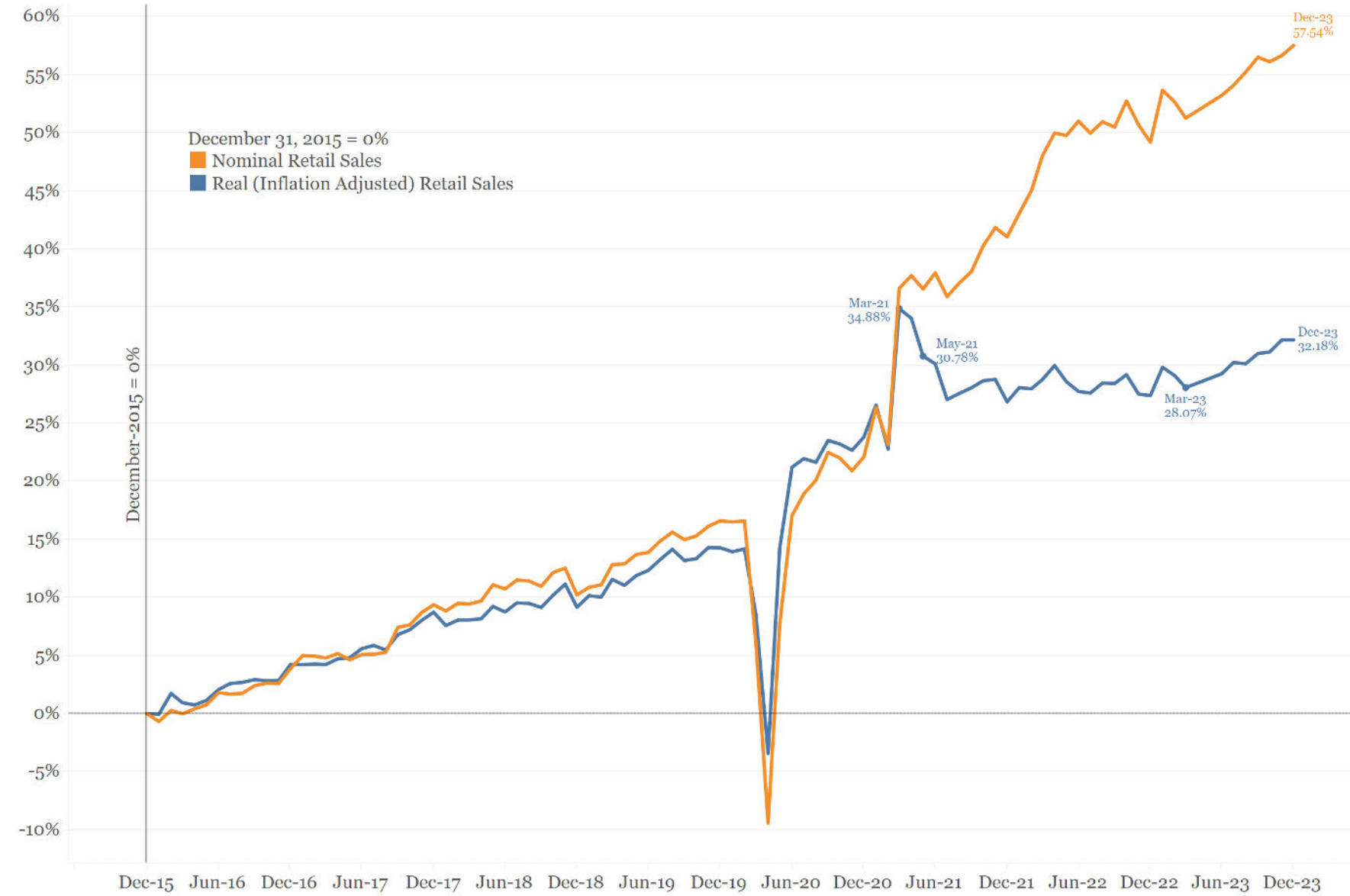
BLS Payroll Response Rates



Data Source: Bureau of Labor Statistics

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**The Growth in Nominal and Retail Sales
Do Not Confuse Sales with Inflation!**



Source: Census Bureau

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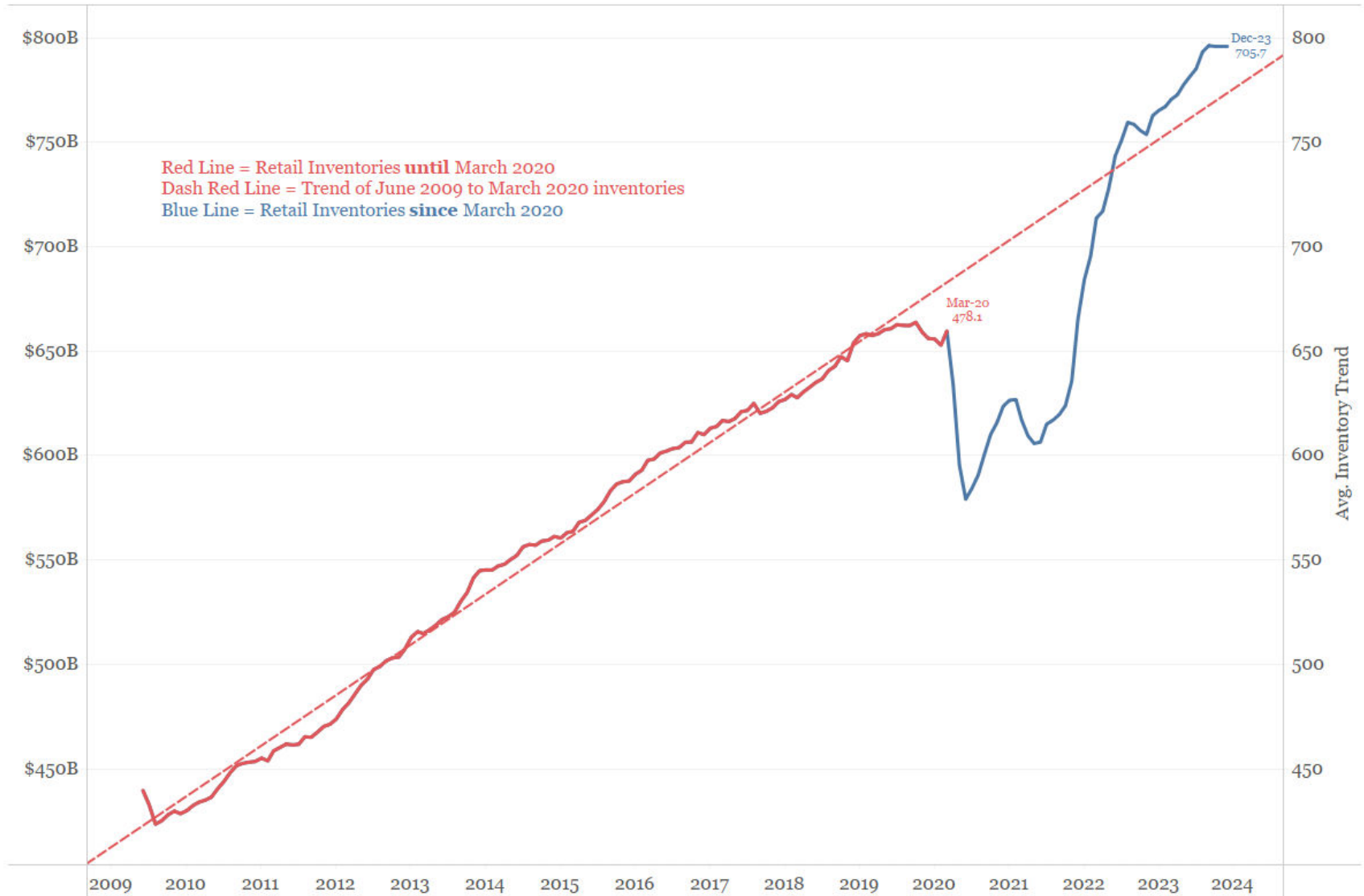
McKinsey & Company – (May 8, 2023)
Thinking beyond markdowns to tackle retail's inventory glut

In the United States alone, retailers are sitting on \$740 billion in unsold goods. Clearing inventory and building more resilient and agile supply chains require action across five dimensions.

Over the past 18 months, retail supply chains have experienced unprecedented demand and supply shifts. Pandemic-related disruptions from the end of 2021 to the start of 2022 led to goods arriving late—or, in some cases, after the season. As retailers sought to overbuy inventory to mitigate potential shortages, softening demand and a sudden shift in consumer spending in the middle of last year left them with an inventory glut needing to be marked down or warehoused.

What Does The Consumer Want?

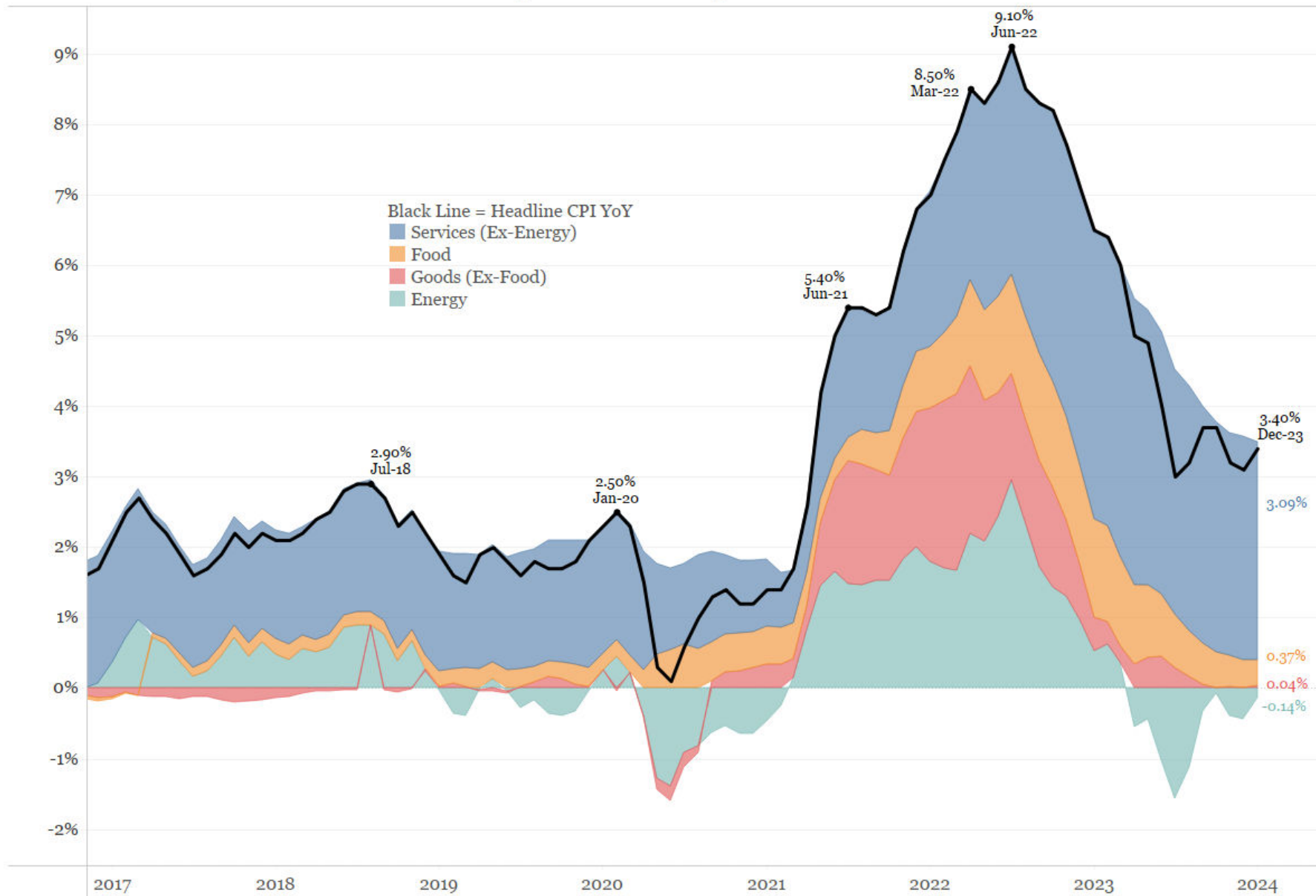
The Retail Industry Struggles With Inventory Management



Source: Census Bureau

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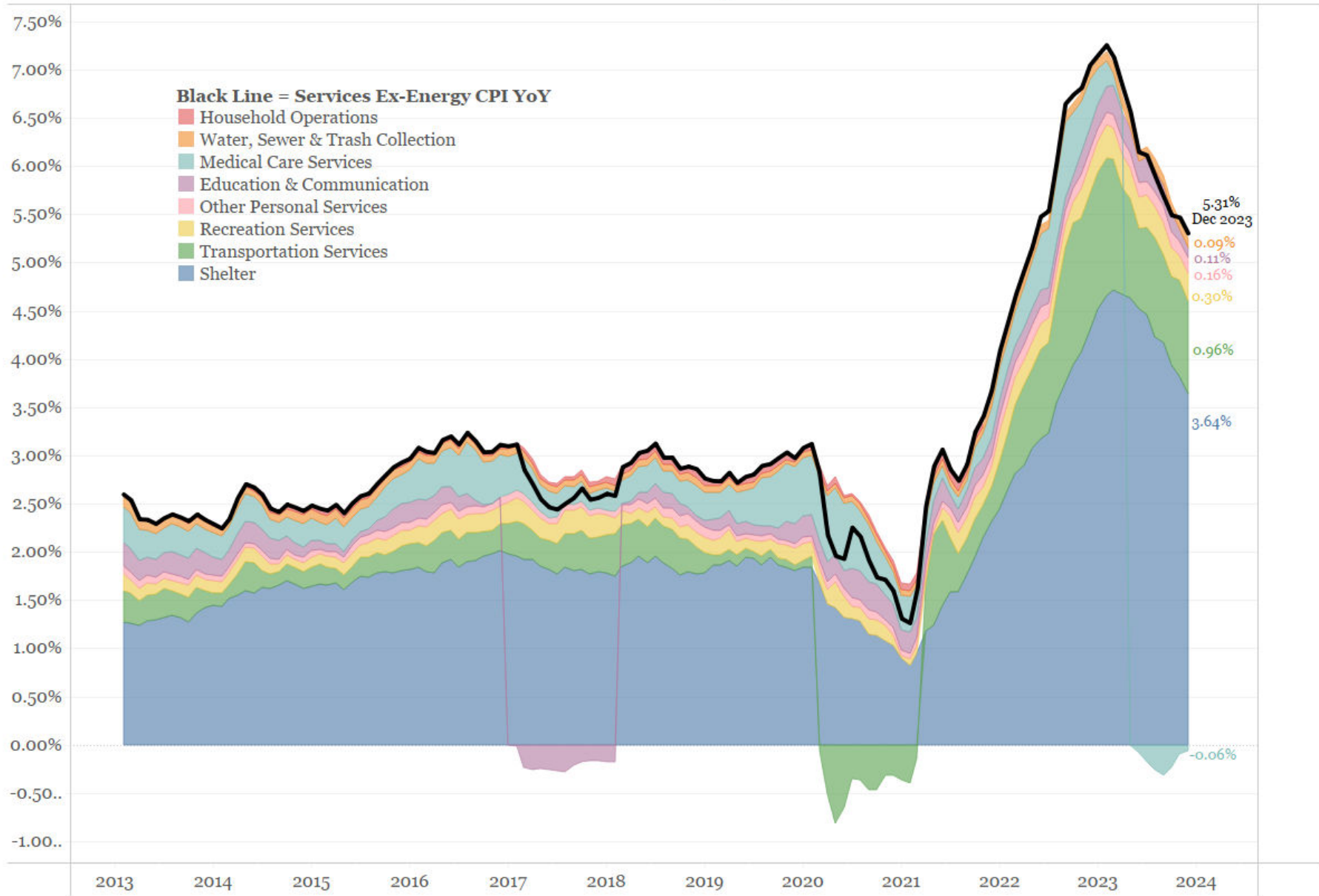
Breaking Down CPI's Major Contributors



Source: Bloomberg

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Breaking Down Services Ex-Energy's Major Contributors



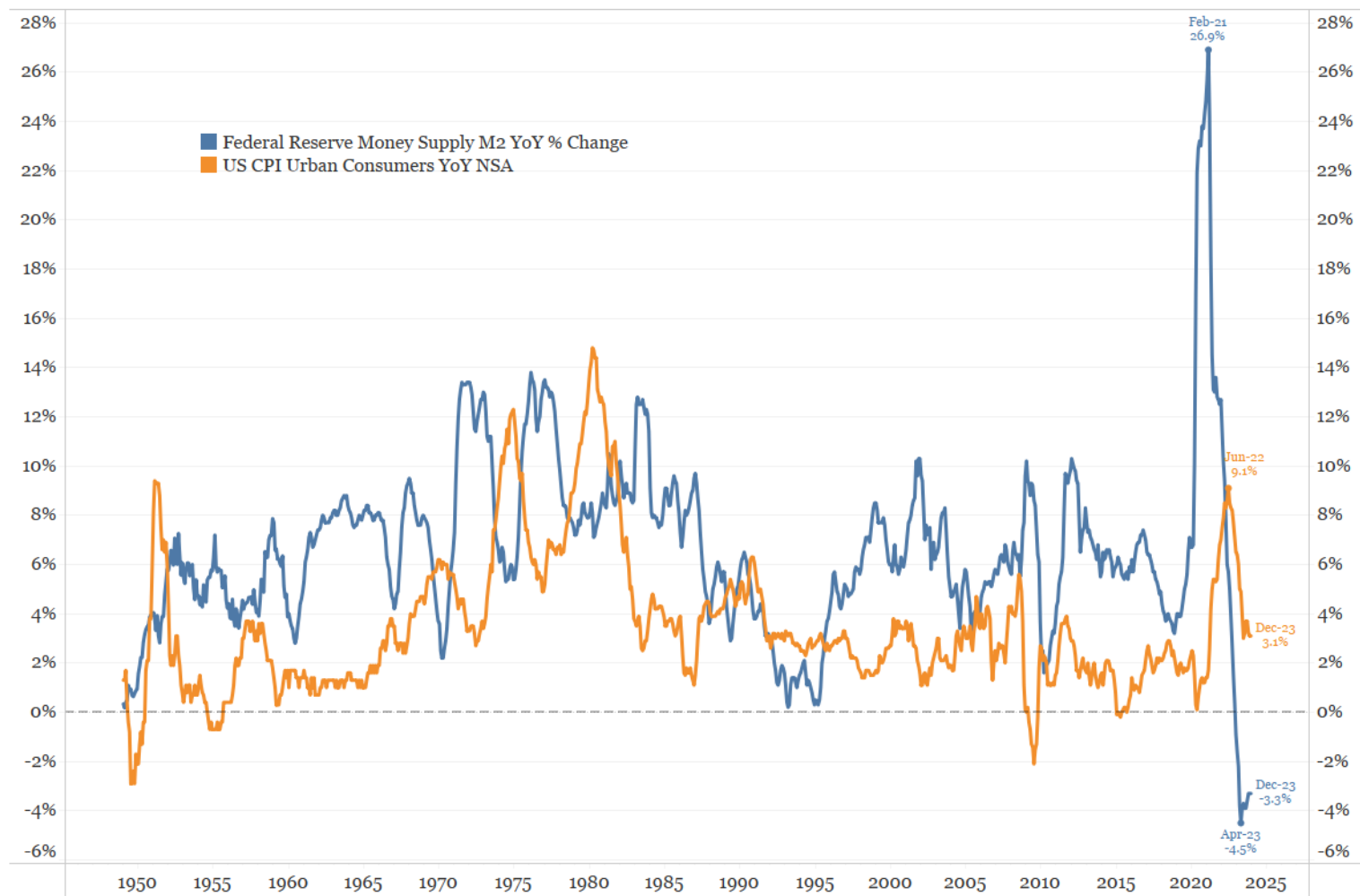
Source: Bloomberg

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• **Financial Times – (October 2017) Fed has no reliable theory of inflation, says Tarullo**

He was particularly doubtful about the weight inflation expectations play in rate-setting policy, given the “range and depth of unanswered questions” about how they are formed and measured. “The substantive point is that we do not, at present, have a theory of inflation dynamics that works sufficiently well to be of use for the business of real-time monetary policymaking,” said Mr Tarullo in a speech at the Brookings think-tank in Washington.

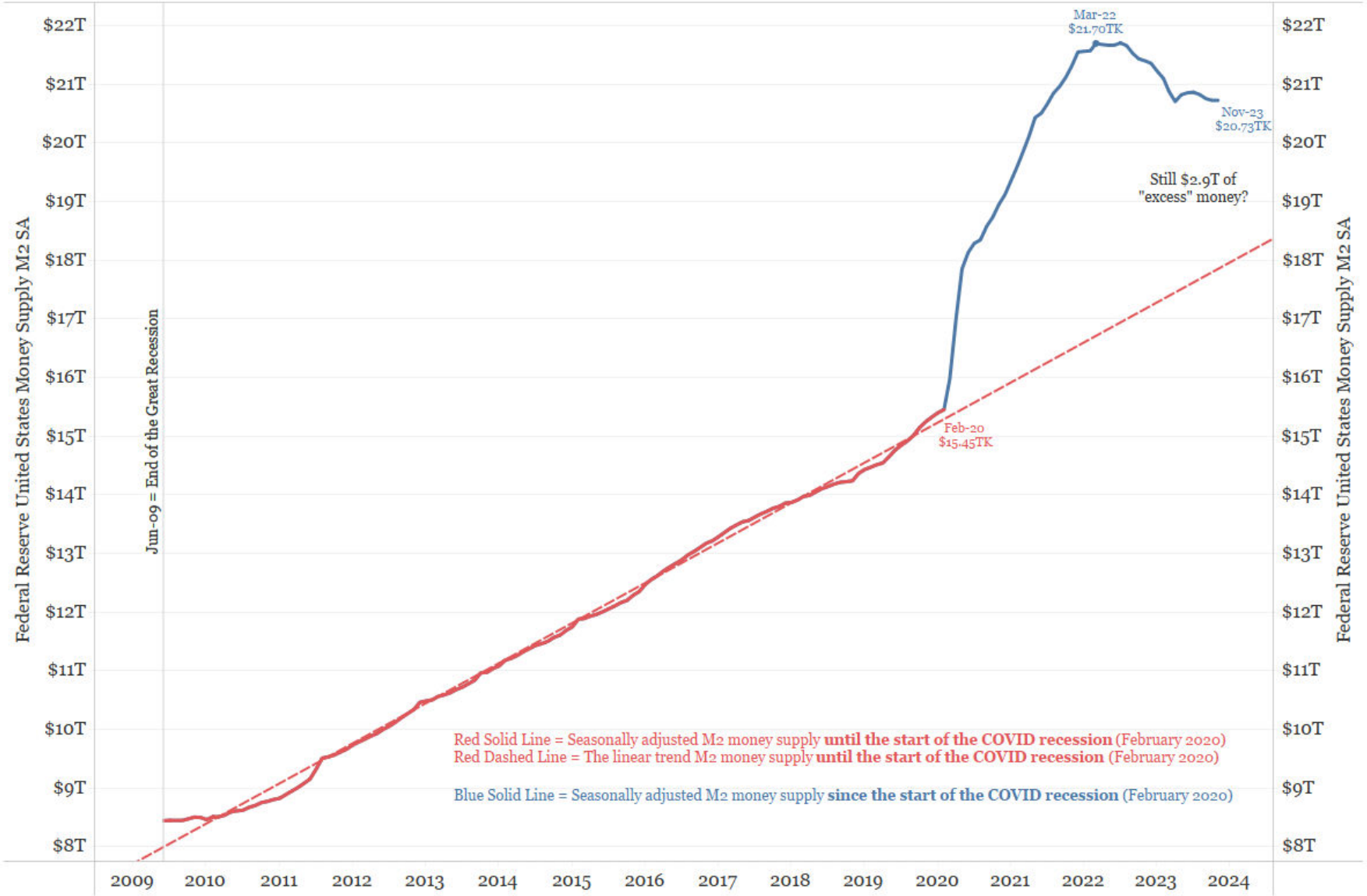
Money Supply and Inflation
A Historically Weak Relationship That Has Grown Weaker Over The Years



Data Source: New York Federal Reserve, Bloomberg

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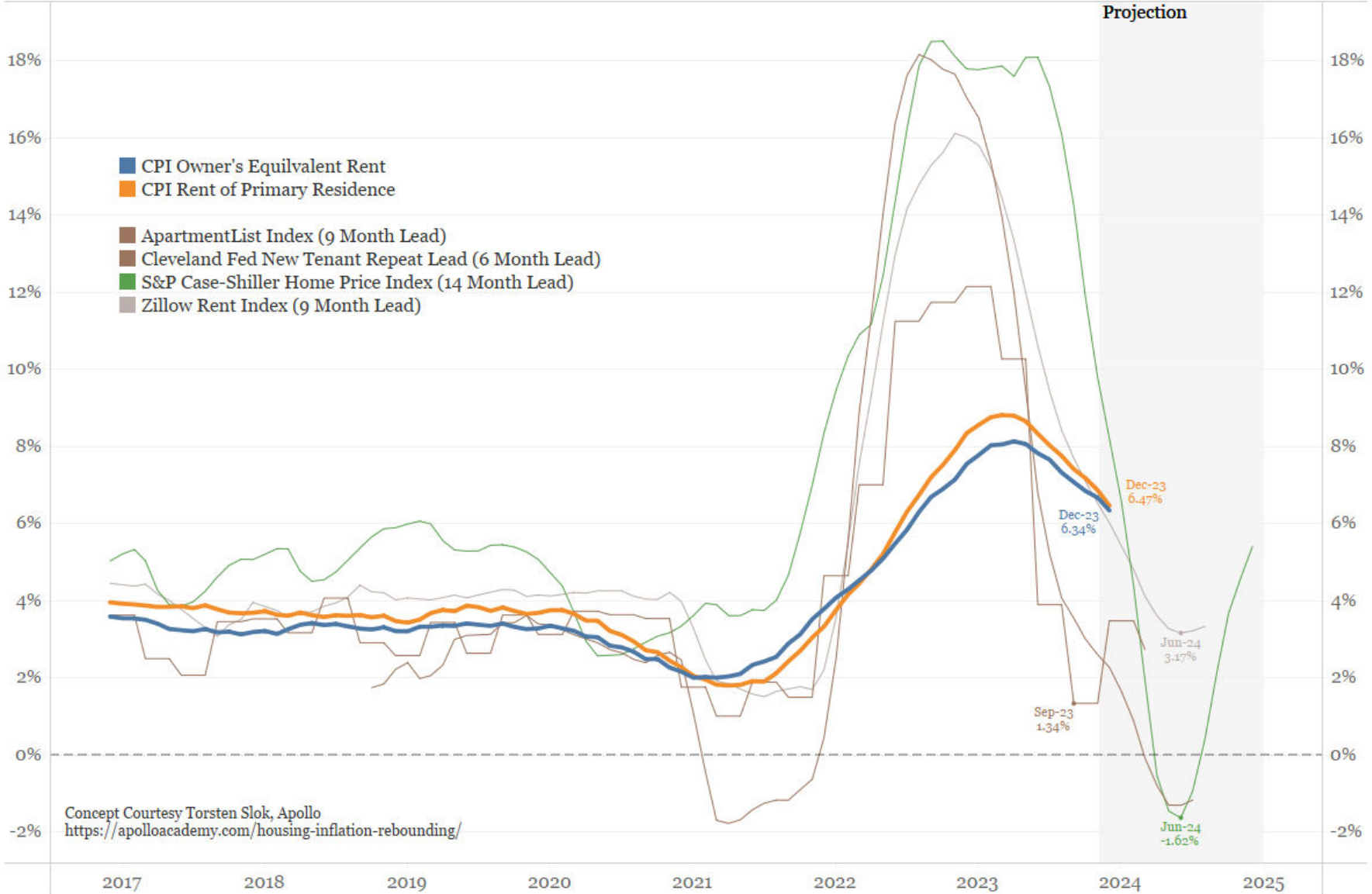
Still Too Much Money Chasing Too Few Goods?
M2 Money Supply and its Pre-COVID Trend



Data Source: New York Federal Reserve, Bloomberg

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Leading Shelter Inflation Year-over-Year Percentage Change



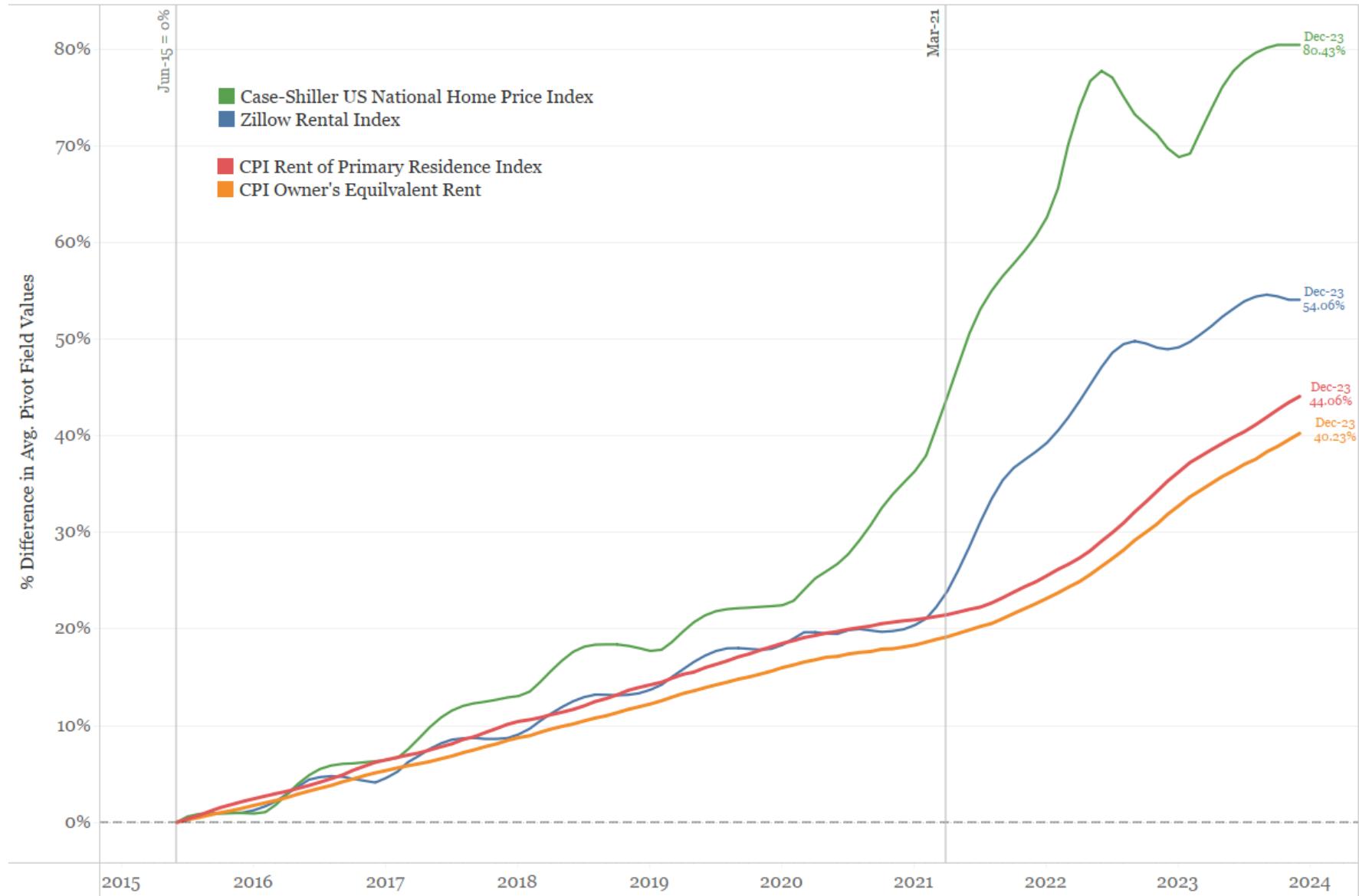
Concept Courtesy Torsten Slok, Apollo
<https://apolloacademy.com/housing-inflation-rebounding/>

Source: The Bureau of Labor Statistics, Bloomberg

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CPI Measures of Inflation Are Behind

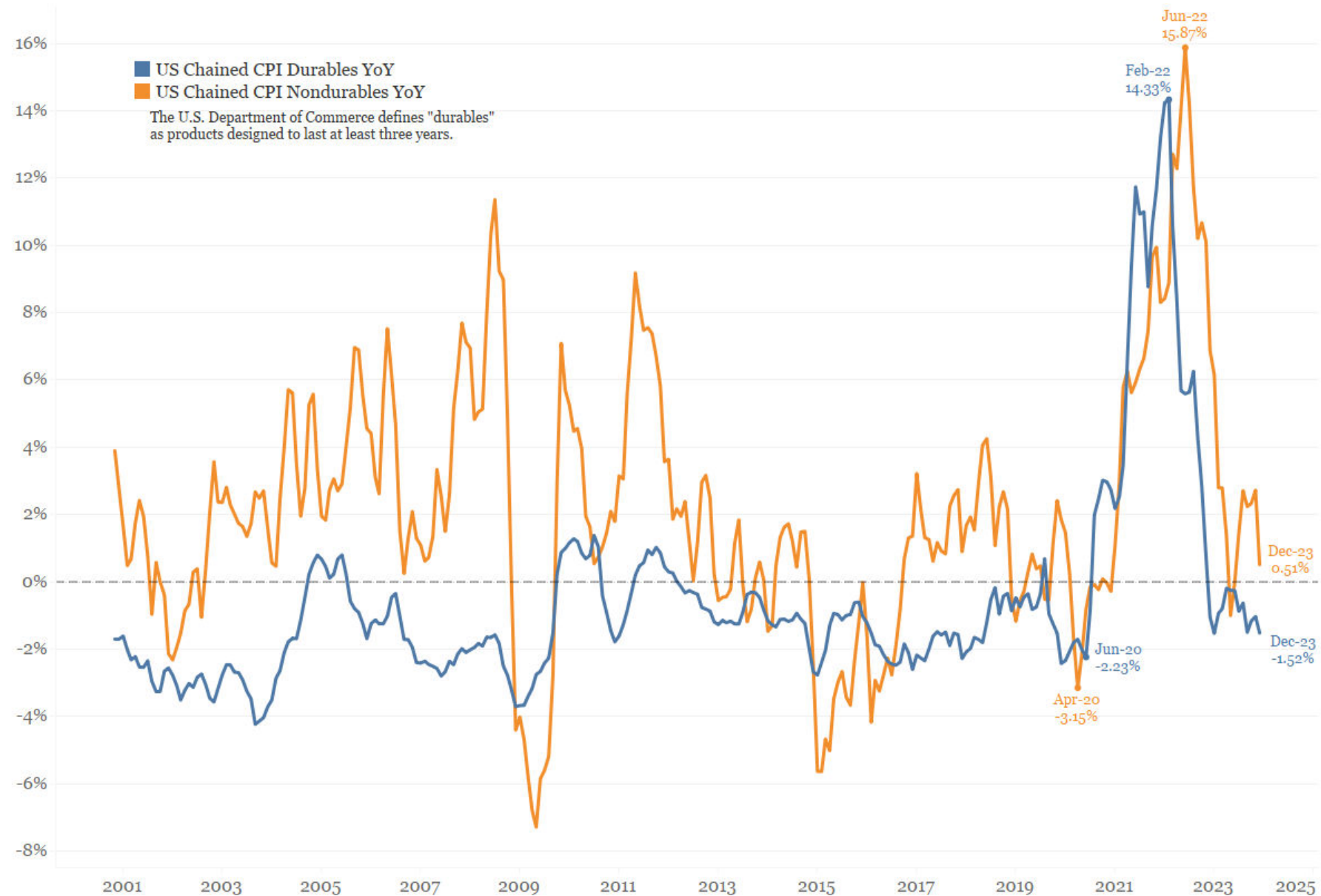
Cumulative Change



Source: The Bureau of Labor Statistics, Bloomberg

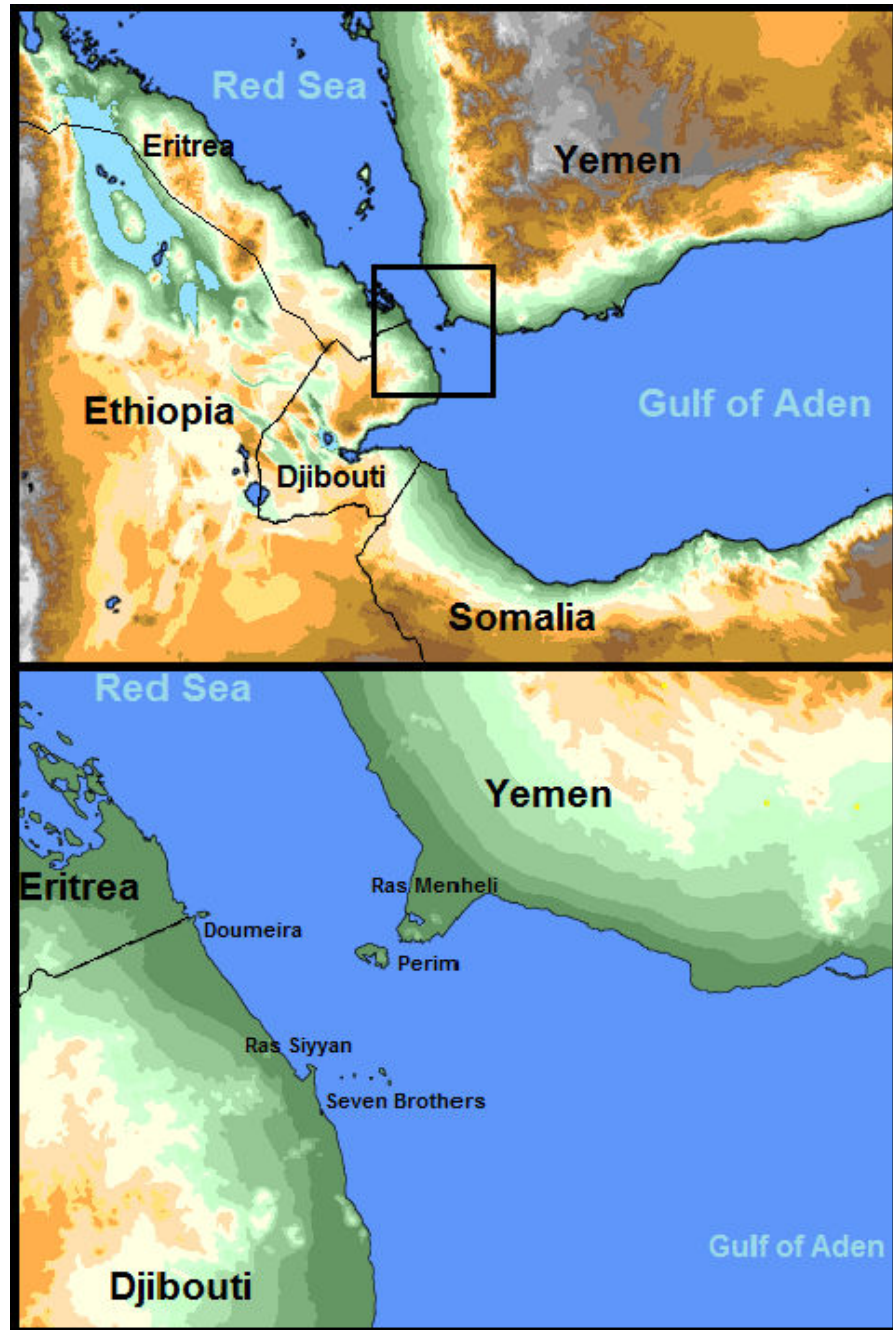
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US Chained CPI Durables YoY & US Chained CPI Nondurables YoY



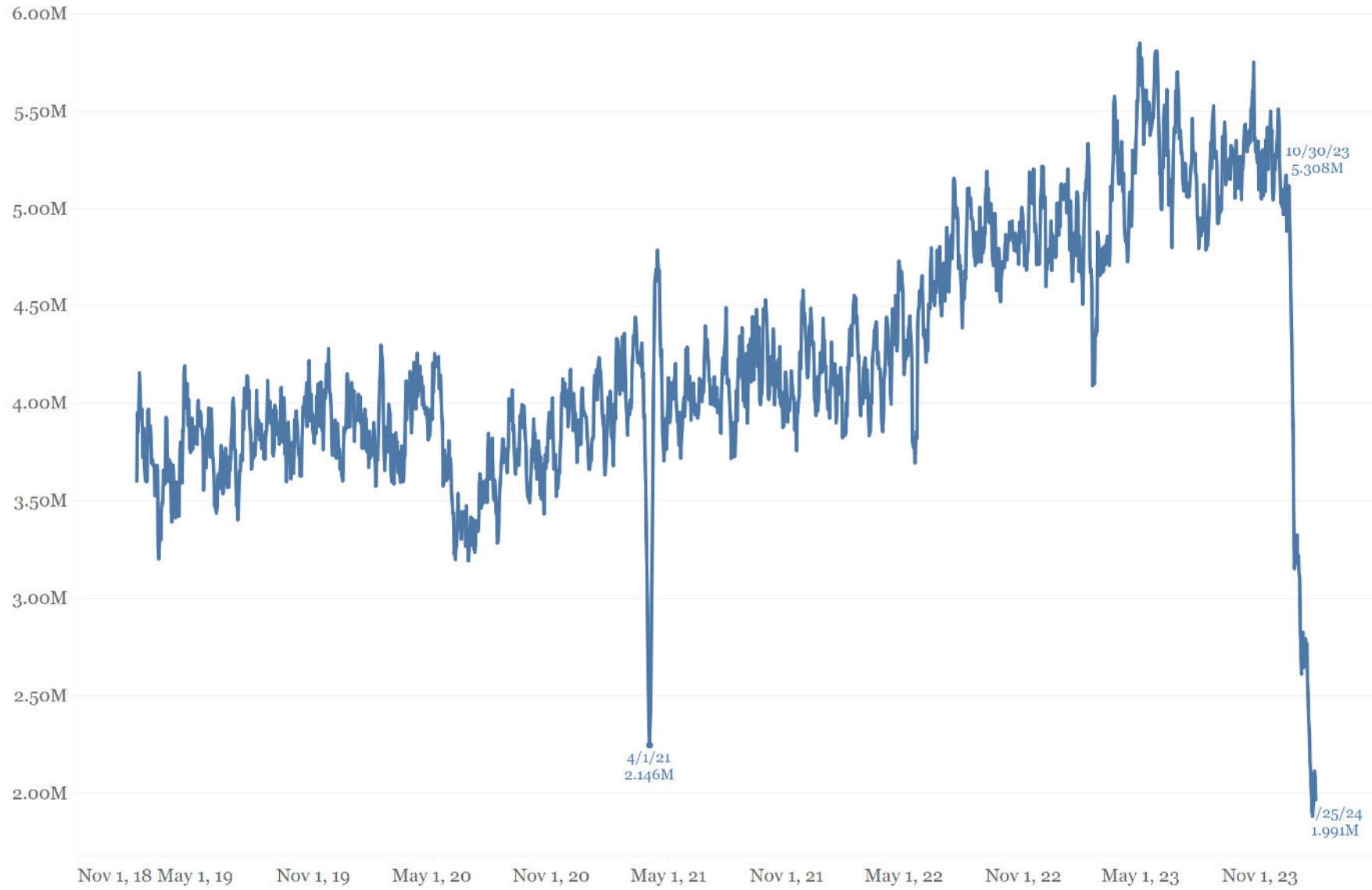
Source: The Bureau of Labor Statistics, Bloomberg

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Metric Tons of Trade Volume Transiting the Bab el-Mandeb Strait Choke Point

7-Day Average

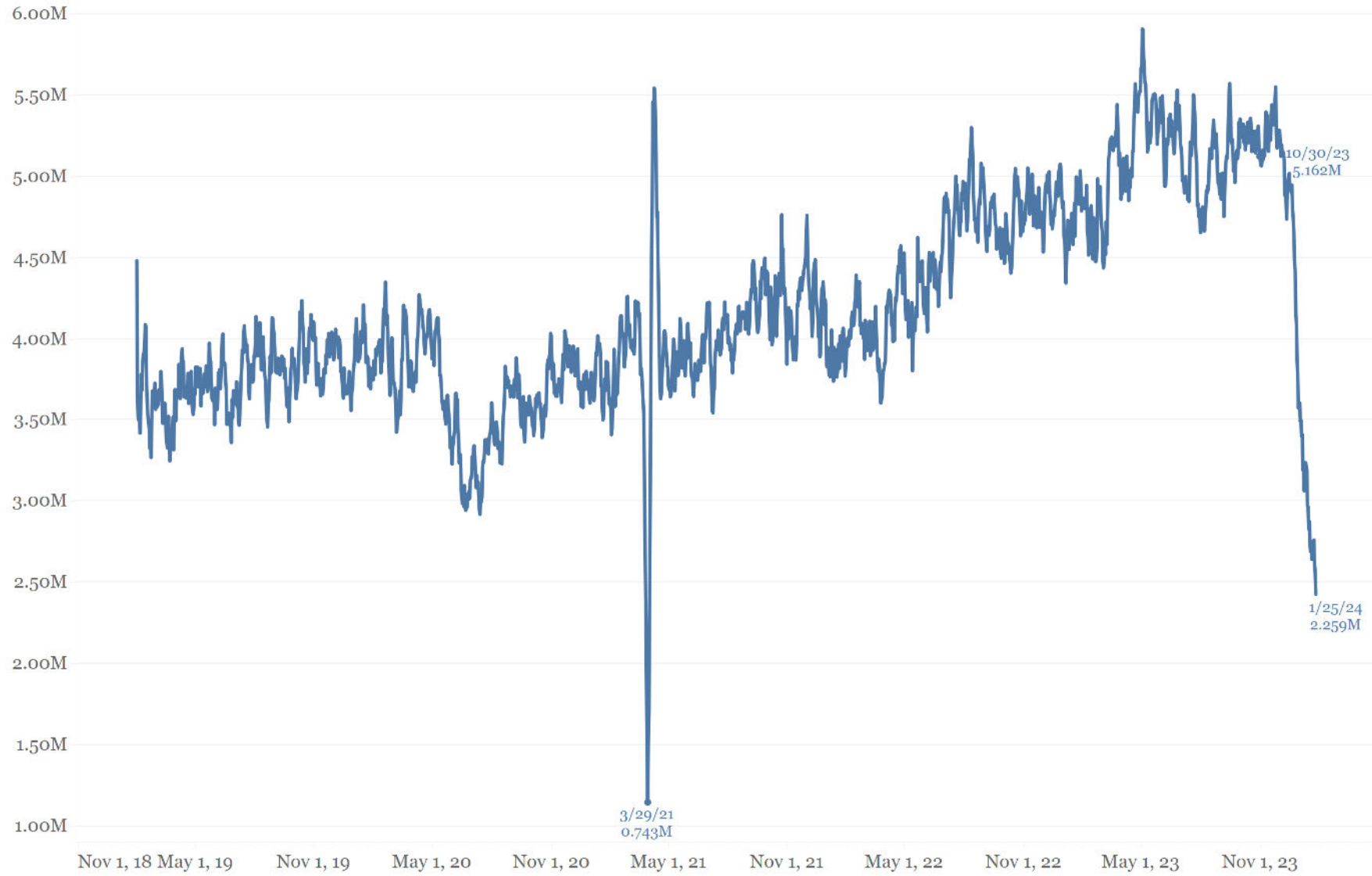


Data Source: IMF Port Watch
<https://portwatch.imf.org/pages/port-monitor>

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Metric Tons of Trade Volume Transiting the Suez Canal Choke Point

7-Day Average

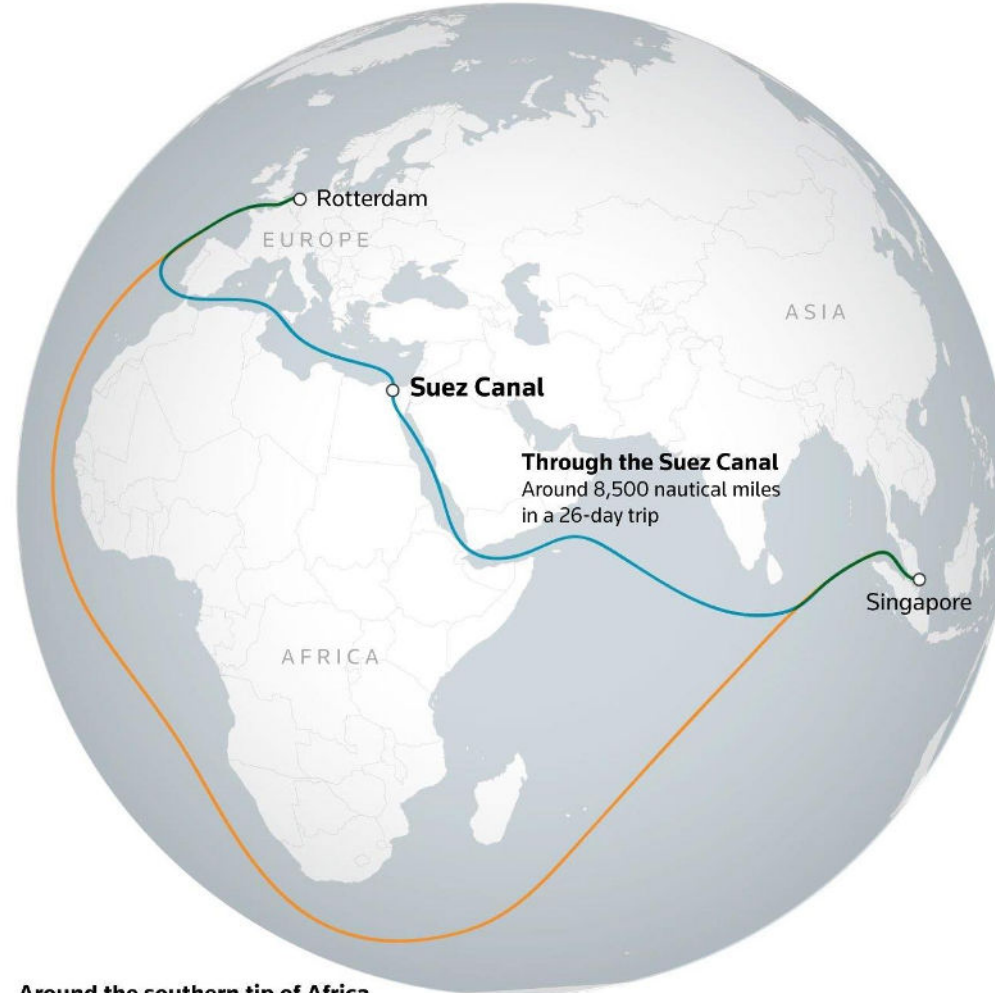


Data Source: IMF Port Watch
<https://portwatch.imf.org/pages/port-monitor>

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Vessels re-routing

Attacks by Yemen's Houthi militants on ships in the Red Sea are disrupting maritime trade through the Suez Canal, with some vessels re-routing to a much longer East-West route via the southern tip of Africa.



Through the Suez Canal
Around 8,500 nautical miles
in a 26-day trip

Around the southern tip of Africa
Around 11,800 Nautical miles
in a 36-day trip

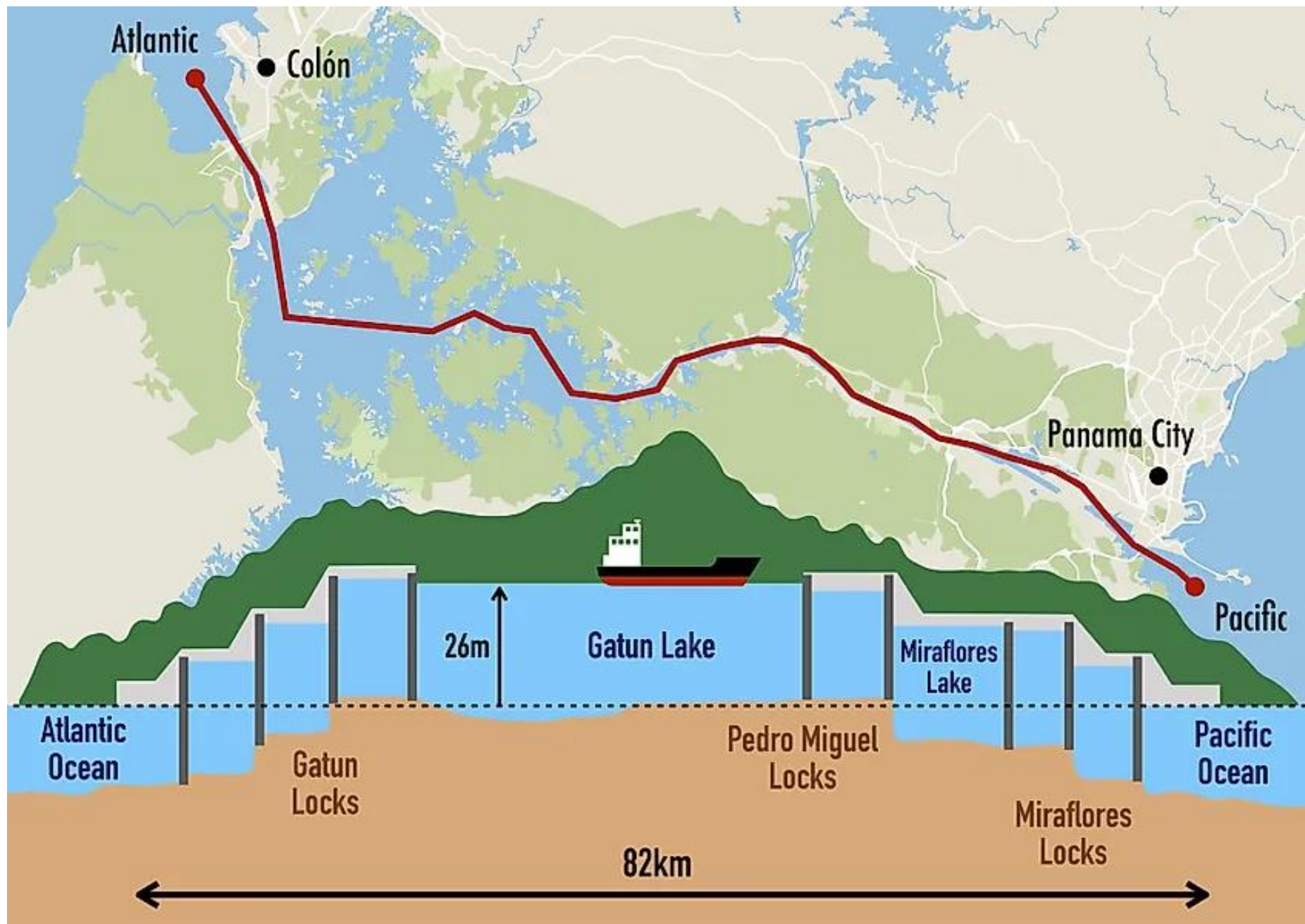
Sources: LSEG; Planet Labs; Maps4News; Shoeni Kisen Kaisha
Reuters Staff • Dec. 19, 2023 | REUTERS

WCI Composite Container Freight Benchmark Rate per 40 Foot Box Drewry

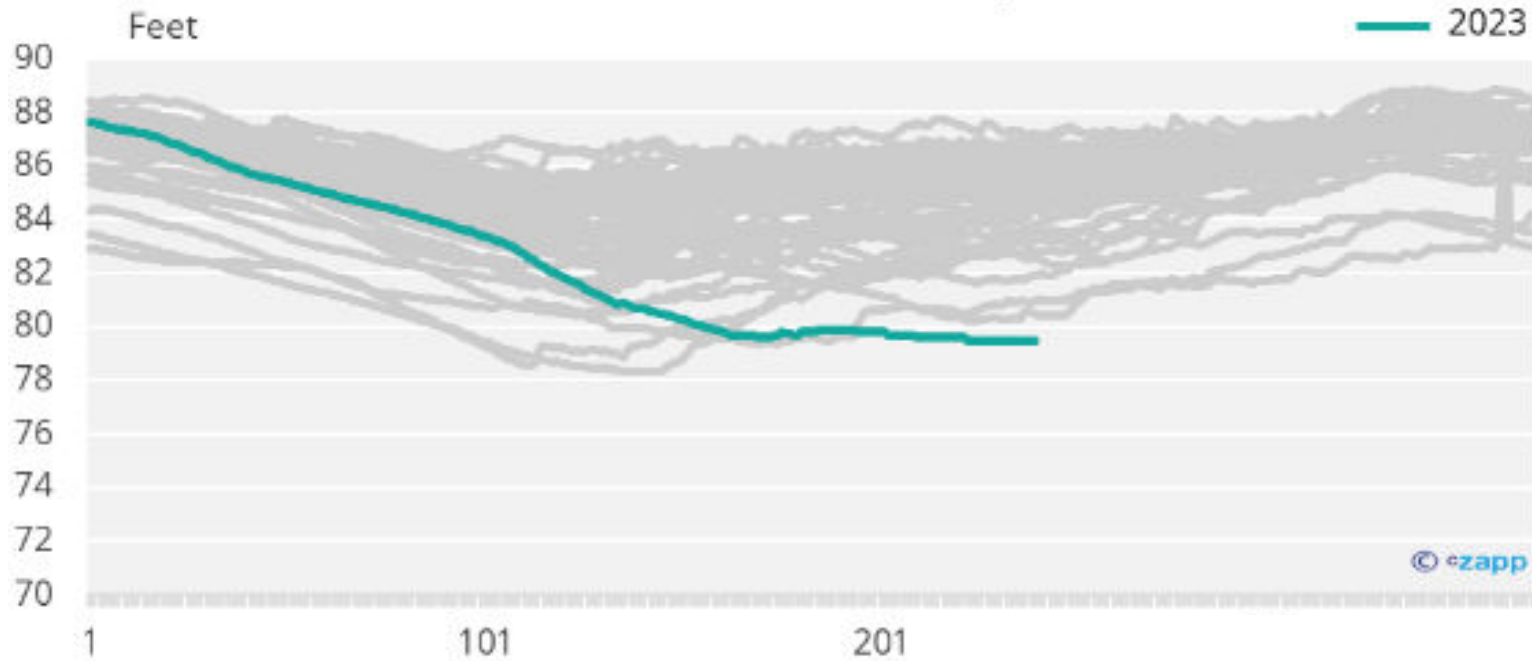


Source: Bloomberg

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Water Levels in 2023 Predicted to Be Lowest Yet in Q3

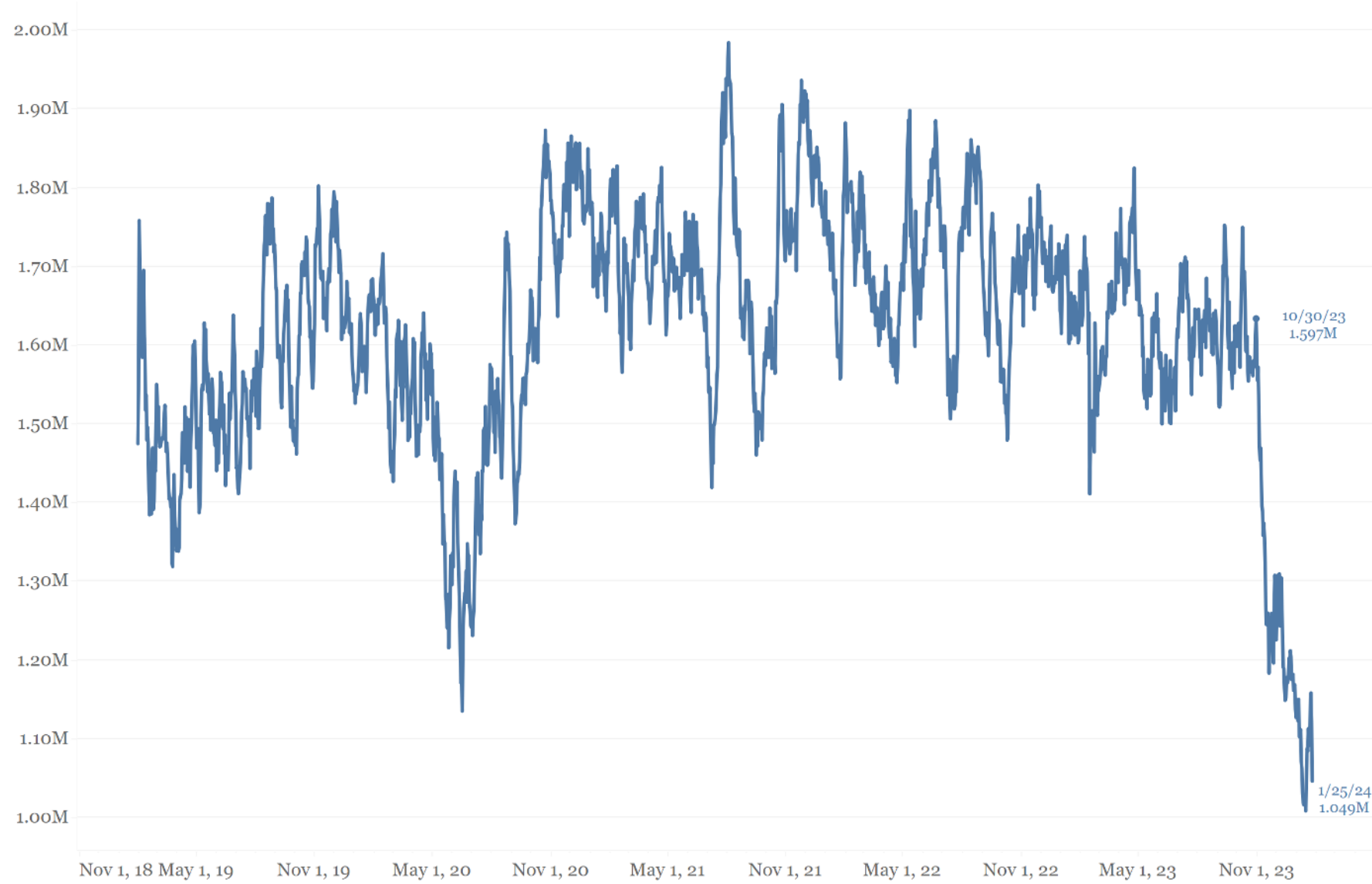


Gatun Lake Level

December 2023



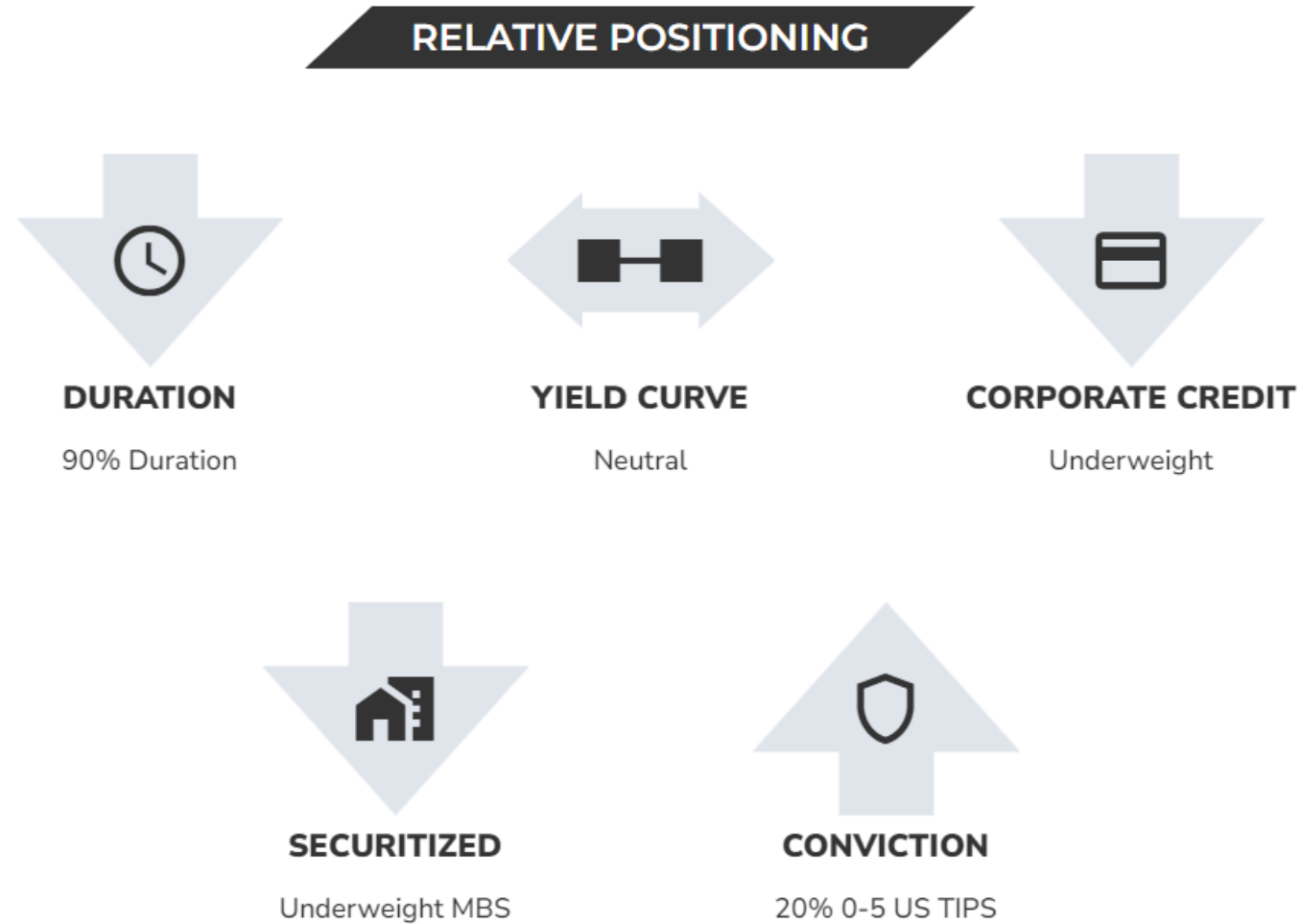
Metric Tons of Trade Volume Transiting the Panama Canal Choke Point
7-Day Average



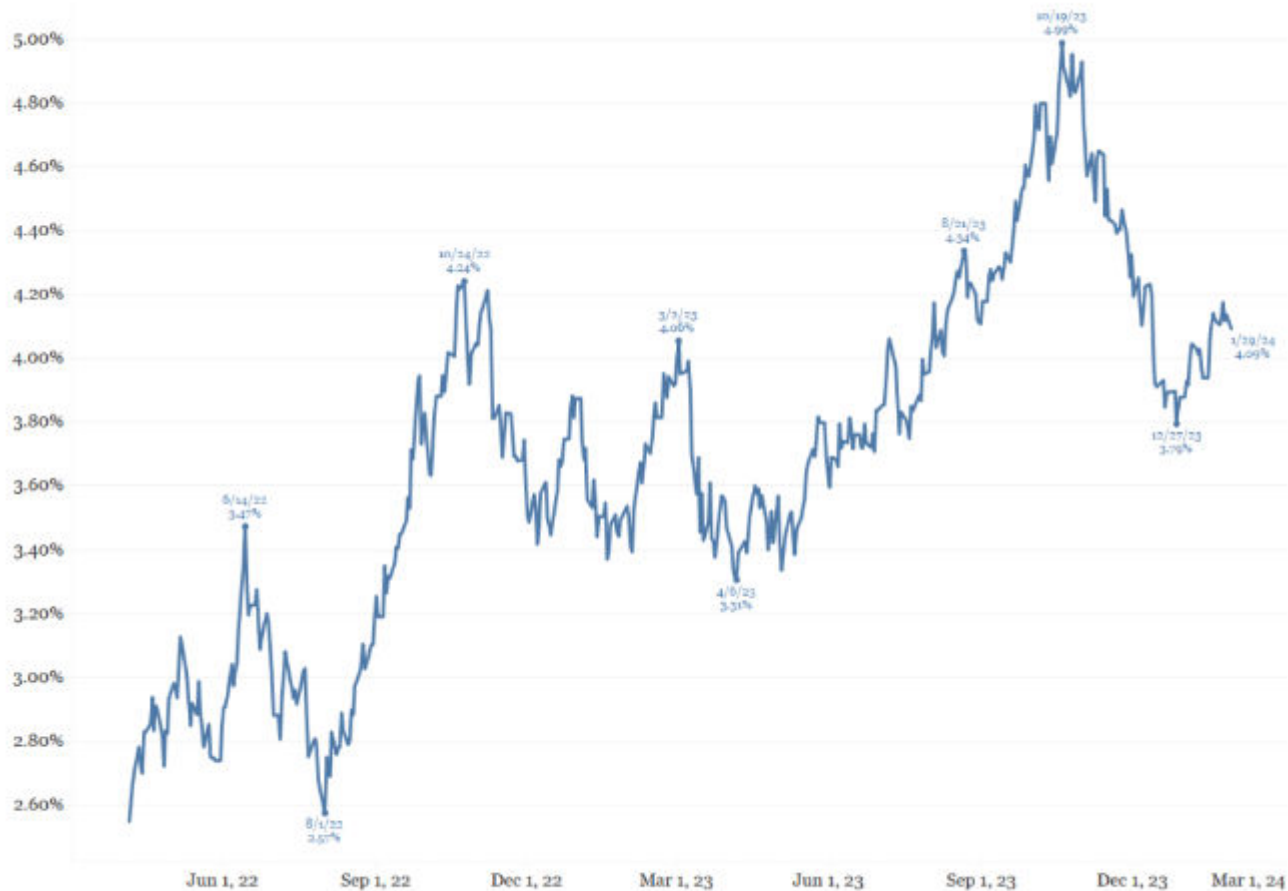
Data Source: IMF Port Watch
<https://portwatch.imf.org/pages/port-monitor>

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<https://www.biancoresearch.com/>

The Bianco Research Total Return Index (BTRINDEX). The ETF “WTBN” Tracks It
www.biancoadvisors.com



US 10-Year Yield



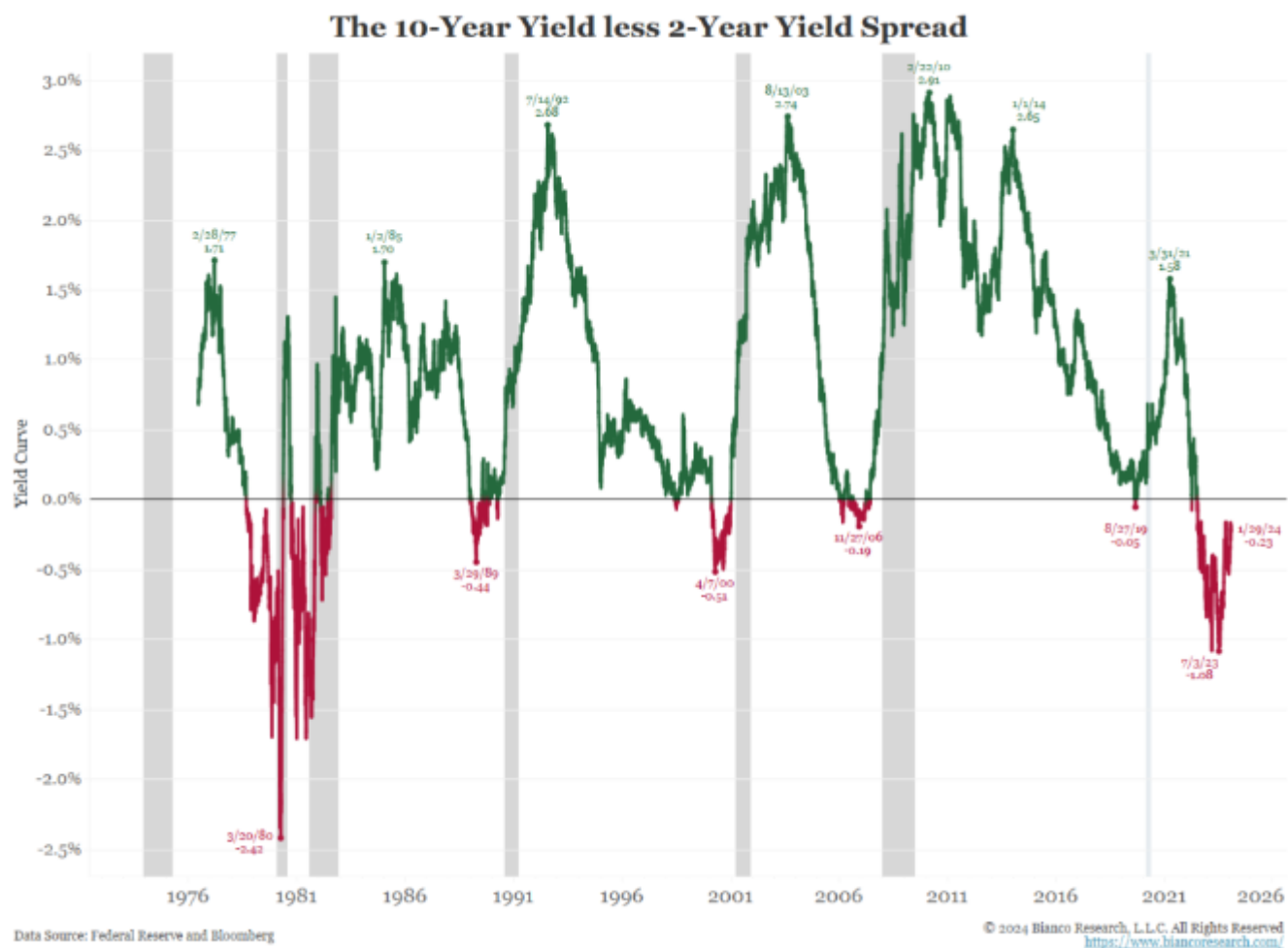
Source: Bloomberg

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90% Duration

The index is underweight duration, based on the belief rates could head higher.

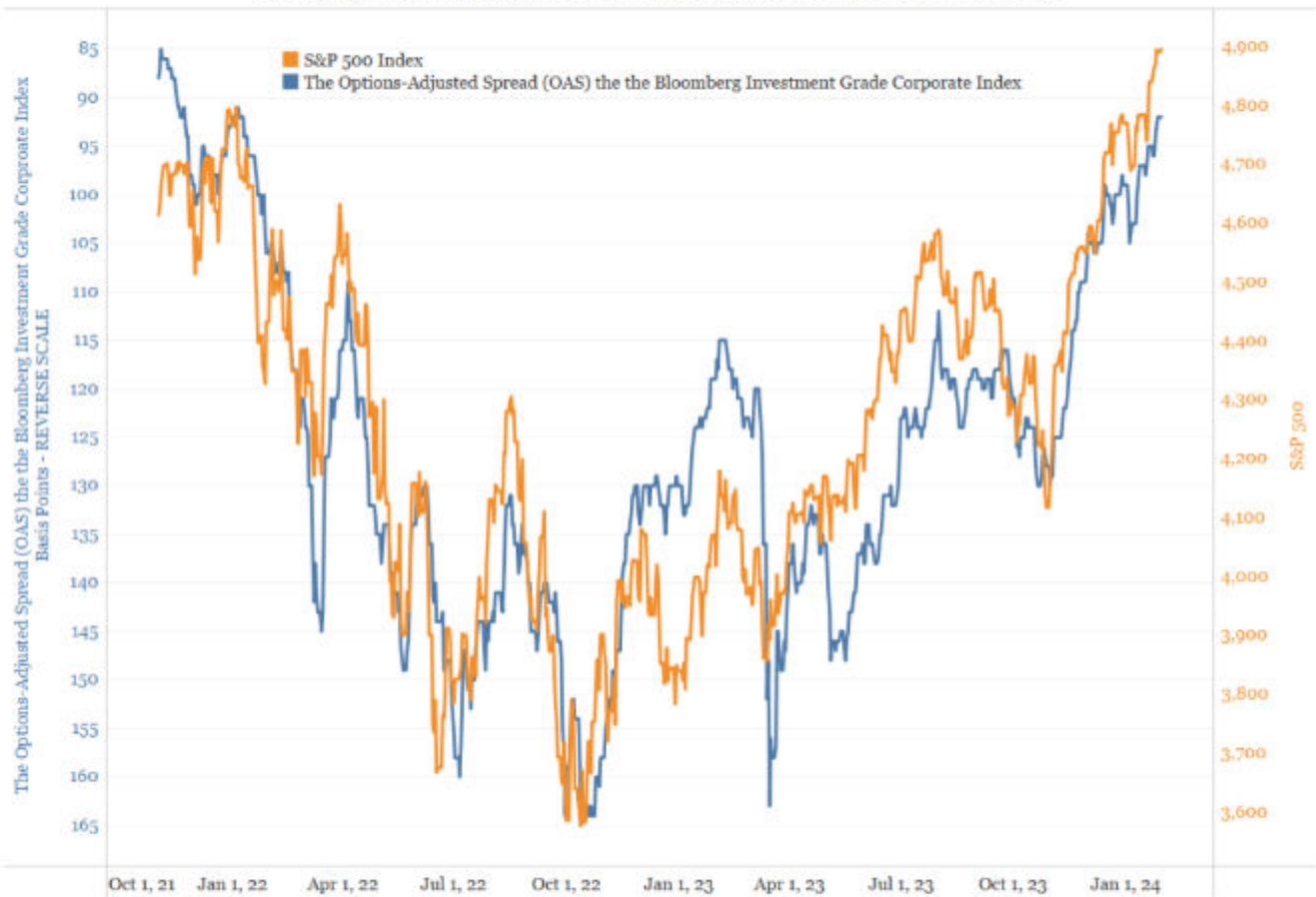
The 10-year yield was recently at a 16-year high. While yields have fallen since October, we do not believe this trend is over.



Neutral Curve Position

The Index holds no curve position relative to the benchmark.

Looking at US Aggregate Credit Index OAS and the S&P 500 Index



Sources: Bloomberg

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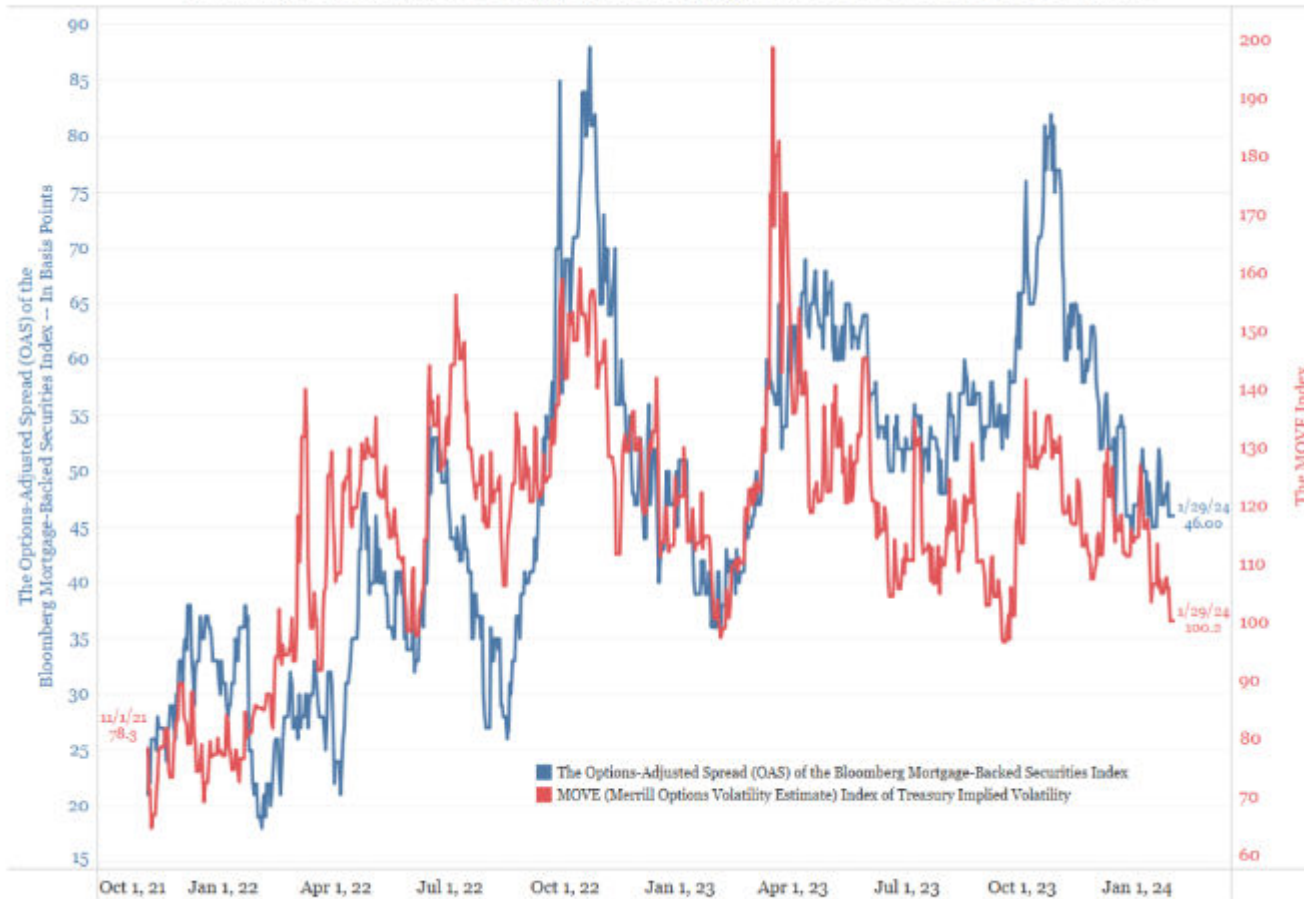
90% Underweight Credit

The index has a 90% allocation to corporates relative to the benchmark. In other words, the index holds an underweight allocation to corporate credit.

The chart shows investment-grade corporate spreads (blue) and the S&P 500 (orange) move in tandem. Relative credit performance moves with equity prices.

With stocks at all-time highs, and record corporate bond issuance in January, we are reducing our credit exposure from 100% to 90% as we see increased risks.

Tracking Volatility With US Aggregate Mortgage Index OAS and the MOVE Index



Source: Bloomberg

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80% Underweight Securitized

All mortgages have an embedded option because holders can pre-pay their mortgage anytime. Because of this structure, the option-adjusted spread (OAS) of mortgages (blue line) and the MOVE Index (red line), which measures the implied volatility of 30-day interest rate options, have a tight relationship.

Given the uncertainty surrounding inflation, Fed policy, and the belief that rates will move higher, look for the yield curve to bear steepen. This can “un-invert” the yield curve in the coming months, and provide a tailwind to mortgage relative performance.

We remain underweight at 80% relative, up from 72% last month.

Short TIPS (0 to 5 years) Index



source: Bloomberg

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20% TIPS Conviction Allocation

The index holds a 20% allocation to 0-5 year TIPS as inflation protection.

The index owns short-maturity inflation securities (TIPS). The 2-year inflation break-even rate has held between 200 and 230bps. The committee anticipates inflation to exceed this level over the next two years. Short-maturity inflation protection is attractive, especially if inflation remains sticky and persistent.

| Name | February 2024 | January 2024 |
|-----------------------------------------------|---------------|--------------|
| iShares MBS ETF | 23.30 | 21.00 |
| iShares 0-5 Year TIPS Bond ETF | 20.00 | 20.00 |
| Vanguard Long-Term Corporate Bond ETF | 8.14 | 9.00 |
| WisdomTree Floating Rate Treasury ETF | 8.00 | 8.00 |
| Vanguard Short-Term Corporate Bond ETF | 7.24 | 8.00 |
| Schwab Long-Term U.S. Treasury ETF | 7.00 | 7.00 |
| Vanguard Intermediate-Term Corporate Bond ETF | 6.41 | 7.09 |
| Schwab Short-Term U.S. Treasury ETF | 5.91 | 5.91 |
| iShares 7-10 Year Treasury Bond ETF | 5.50 | 5.50 |
| iShares BBB Rated Corporate Bond ETF | 5.00 | 5.00 |
| iShares 3-7 Year Treasury Bond ETF | 3.50 | 3.50 |

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