Basis Points – January 17, 2019

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Above the Fold

- The strength in the dollar that we saw for most of 2018 may be fading, which is positive for foreign economies and currencies, specifically emerging markets. Strength in the dollar last year came from rising interest rates due to Fed rate hikes, surging oil prices, repatriation of cash to American companies from foreign holdings and a much stronger U.S. economy relative to the rest of the world. What a difference a few months makes as energy prices have corrected sharply, the Fed seems to be data dependent and on hold for now, and interest rates have declined.
- Bank of America reported that fourth-quarter earnings rose sharply, helped by rising interest rates and lower taxes. The second largest bank in the U.S. by assets reported profits for the fourth quarter of 70 cents a share vs. street expectations of 63 cents per share. Full-year 2018 profit of $28.2 billion was the largest in Bank of America's history. The results show that big lenders are benefiting from the Fed's rate increases, as higher rates mean banks can charge more for loans, and the Fed's slow pace of rate increases has allowed big banks to charge borrowers more for loans without having to significantly increase payouts to depositors.
- The U.S. housing market slowed sharply last fall as home mortgage rates surpassed the 5 percent level, which moved many would-be homebuyers to the sidelines. However, the downturn in mortgage rates that began in November finally has homebuilders feeling better about their business. Builder sentiment rose two points to 58 in January, after dropping steadily throughout 2018. NAHB Chairman Randy Noel noted: "The gradual decline in mortgage rates in recent weeks helped to sustain builder sentiment. Low unemployment, solid job growth and favorable demographics should support housing demand in the coming months."

Three Things

- Jason Zweig notes in the WSJ that Amazon recently became the world's largest company by market capitalization. Over the past 100 years, there have only been 10

companies that have ever ranked No. 1 among all U.S. stocks by market capitalization, and Amazon just became the 11th. Past No. 1's by market cap include Microsoft, Apple, Exxon Mobil, GE, Walmart, Altria, IBM, DowDuPont, GM and AT&T. Although many financial writers and politicians may caution that today's market is "narrow" or "concentrated" or "top-heavy," with the largest stocks accounting for an unusually large share of total value, that is not backed up by historical data. Today's biggest technology companies are not turning into unstoppable juggernauts of growth, and the top of the list turnover is not accelerating. Amazon, at less than 3 percent of the total value of all U.S. stocks, can be called a small company compared to the giants of the past. AT&T was 13 percent of total U.S. stock-market value back in 1932; General Motors, 8 percent in 1928; and IBM was 7 percent in 1970. And the market cap of the top 10 highly valued companies relative to the total equity market these days is about average when compared to the giants of the last 100 years.
- The birth rate in America has been declining, but some places are more fertile than others. Only South Dakota's and Utah's fertility rates reached the level needed to sustain the current population, which is 2.1 babies born for every two people. There are vast differences in birth rates among the United States. States in the Midwest and the Southeast had higher rates of fertility compared with the Northeast or West Coast. South Dakota has the highest fertility rate, at 2.23 births per two people, while the District of Columbia has the lowest, at 1.42 births. Hispanic women had the highest fertility rate of the ethnicities studied, while Caucasians had the lowest fertility rates in all states.
- When California voted in 2016 to allow the sale of recreational marijuana, advocates of the move envisioned thousands of pot shops obtaining state licenses, making the drug easily available to all adults within a short drive. But the L.A. Times reports that after one year of full legalization, California's legal market hasn't performed as state officials and the cannabis industry had hoped. Retailers and growers say they've been stunted by complex regulations, high taxes and decisions by most cities to ban cannabis shops. At the same time, many residents are going to city halls and courts to fight pot businesses they see as nuisances, and police chiefs are raising concerns about crime triggered by the marijuana trade. Many citizens voted for legalization, but few towns want the stores in their neighborhoods. State officials estimated there would be as many as 6,000 cannabis shops licensed in the first few years. But the state has issued just 547 licenses to marijuana retail stores so far. State officials also predicted that legal cannabis would eventually bring in up to $1 billion in revenue a year, but tax revenue is falling far short of estimates, at only $471 million in revenue this year. Less than 20 percent of cities in California allow retail shops to sell cannabis for recreational use.

Did You Know

The Department of Energy (DOE) reports that U.S. oil production, already at an all-time high this year, will increase by another 2 million barrels per day (bpd) by 2020, and that year the U.S. will start exporting more crude oil and fuel than it imports, the Energy Information Administration (EIA) said in its latest forecast. American drillers pumped an average 10.9 million bpd in 2018, breaking the record going back to 1970. EIA sees U.S. output averaging 12.1 million bpd this year and 12.9 million bpd in 2020. The DOE said that according to its outlook, the Permian region of Texas and New Mexico will continue to push U.S. production into record territory over the next 24 months, approaching 13 million bpd some time in 2020.

The U.S. is now much less dependent on foreign oil. In 2018, net imports of oil and petroleum products fell from 3.8 million bpd to 2.4 million bpd. EIA forecasts net imports will dwindle to 1.1 million bpd next year and just 100,000 bpd in 2020. The U.S. already ships out more natural gas than it imports. Next year, gas production will jump another 8 percent to a new all-time high at 90.2 billion cubic feet per day.

By 2020, EIA thinks natural gas will generate 37 percent of the country's electric power, up from 35 percent last year. Meanwhile, coal's share of electric power generation will slip from 28 percent to 24 percent during the same period. That will help contribute to a further drop in U.S. coal production.

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