CIF Sector Recommendation Report (Spring 2013)

Sector: Financials

Review Period: Feb 5th 2013 - Feb 18th 2013

Section (A)  Sector Performance Review

<table>
<thead>
<tr>
<th>Ticker</th>
<th>Current Price</th>
<th>Beg. Price</th>
<th>Stop-loss Price</th>
<th>Target Price</th>
<th>% Cap Gain</th>
<th># Shares</th>
<th>Current Value</th>
<th>vs. Sector vs. S&amp;P 500</th>
</tr>
</thead>
<tbody>
<tr>
<td>S&amp;P 500</td>
<td>$INX</td>
<td>1530.94</td>
<td>1495.71</td>
<td></td>
<td>2.36%</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sector ETF</td>
<td>XLF</td>
<td>$17.93</td>
<td>$17.41</td>
<td></td>
<td>2.99%</td>
<td>15200</td>
<td>$272,536.00</td>
<td>0.63%</td>
</tr>
</tbody>
</table>

Since Monday was President’s Day and the market was closed, I use the next day closed prices for my report. Looking at the price graph from finance.yahoo.com, the financials sector is in line with the S&P 500. The sector performs slightly better with a gain of 0.63% gain compared to the market.
According to finance.yahoo.com, 7 West 57th Street Realty Co. has filed a lawsuit against Citigroup, JPMorgan Chase, The Royal Bank of Scotland Group, Barclay PLC, USB AG, and Bank of America for their roles in LIBOR rate manipulations. The company claimed that these banks falsely stated the interest rates at which lenders can borrow money among themselves on a daily basis to the British Bankers Association. AIG announced that they wanted to buy back bonds worth up to $1.25 billion to cut down its debt.

Top traders have moved from bank prop trader to hedge fund manager in response to new Volcker rules that forbid banks from trading with their own funds. Banks including Bank of America, Goldman Sachs, and Morgan Stanley began closing down their prop trading operations before the rule was finalized. According to Bloomberg.com, equity trading was hardest-hit by job cuts in 2012. The top 10 investment banks eliminated 2,700 front-office workers.

Goldman Sachs has an intention to raise $600 million for a publicly traded credit fund, which will be structured as a business development company and funded nearly 25% by the bank itself. The reason of this move is business development companies are categorized outside the purview of the Volcker rules.

Wells Fargo’s total loans increased by approximated $16.9 billion in the fourth quarter 2012 including about $9.7 billion growth in mortgages. Mortgage banking represents about 30% of the company’s operating fee revenue. Its strong refinance volumes come from the lower rates and the Home Affordable Refinance Program commission.

The biggest positive mover from the sector holdings during the review period is CBRE Group Inc. (CBG): the stock price increased 12.96%. Fourth quarter earnings shows revenue growth of 14% and profit growth of 22% from the last year. Their forecast EPS is also higher than Wall Street estimate. The company operates as a global commercial real estate services company. The biggest negative mover from the sector holdings during the review period is The McGraw-Hill Companies Inc. (MHP): the stock price decreased 8.51%. The stock drop is due to a US government $5 billion lawsuit against S&P. The government accused the rating agency of fraud scheme in mortgage-related securities in the 2008 financial crisis.

The largest two holdings from the sector are JP Morgan Chase (JPM) weighted 8.61% and Berkshire Hathaway (BRK.B) weighted 8.44%. Deepak Gulati – JPM’s global head of proprietary trading is quitting the company to start a hedge fund in Switzerland. Berkshire Hathaway teamed up with 3G Capital – a Brazilian private equity firm – to acquire the ketchup company H.J. Heinz Co. worth $28 billion.
Many individual firms are expected to come up with lawsuits similar to the 7 West case about LIBOR manipulation by banks. Therefore, the reputation of these big banks will be damaged and it can affect the performance of these banks in the near future. The business model to be seen as a solution of the Volcker problem will be used by other banks and similar business development companies will be created. Banks have posted strong performance and their stocks are at 52 week high range. I believe part of the reason is the revenue from HARP refinance fee. Even though the Volcker rule is tightening the banks, they already found a solution and I think more will come up.

**Section (B)  Sector Holding Updates**

We don’t have any stock in the financial sector right now.

**Section (C)  Sector Recommendations**

Based on my research, I recommend CIF to stay put with its current industrial sector holdings. The institutions in the sector are doing pretty well in general. The budget deficit problem has been pushed back to the beginning of March and the uncertainty of how the government will solve this is still there. The market doesn’t seem to be afraid of the debt ceiling problem this time with the stocks are near their 52-week high. Beside that risk, I don’t see any big threat that would damage the financials sector.

**Section (D)  Sector Holding Recommendations**

We don’t have any stock in the financial sector right now.

**References**

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