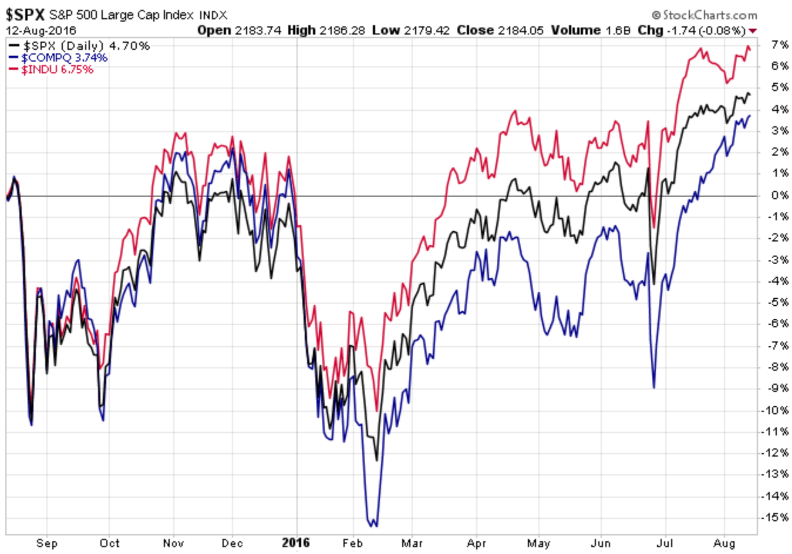
MONDAY MORNING KICKOFF

YOUR MARKET PRIMER FOR THE WEEK AHEAD

WEEK OF AUGUST 15, 2016



ThematicSignals

US Over the Top Video Users Approach Saturation Point *Connected Society / Content is King*

The Burger King 'Whopperito' – More Marketing Fat Than Taste Sizzle *Fattening of the Population*

Apple's Newest Business Isn't at All What You Would Expect *Connected Society / Scarce Resources*

You May Be Broke and Not Know It *Cashstrapped Consumer*

Too Old for Hard Labor, but Still on the Job *Aging of the Population / Tooling & Retooling*

The stock market continued to grind higher last week, with all three major domestic stock indices once again hitting new highs. While the headline was the records achieved and that naturally attracted much attention, the actual coverage was rather cursory and glossed over a number of different points. Given our differentiated perspective relative to the herd mentality, we'd point out those news highs came with only very modest upward moves in the indices this week.

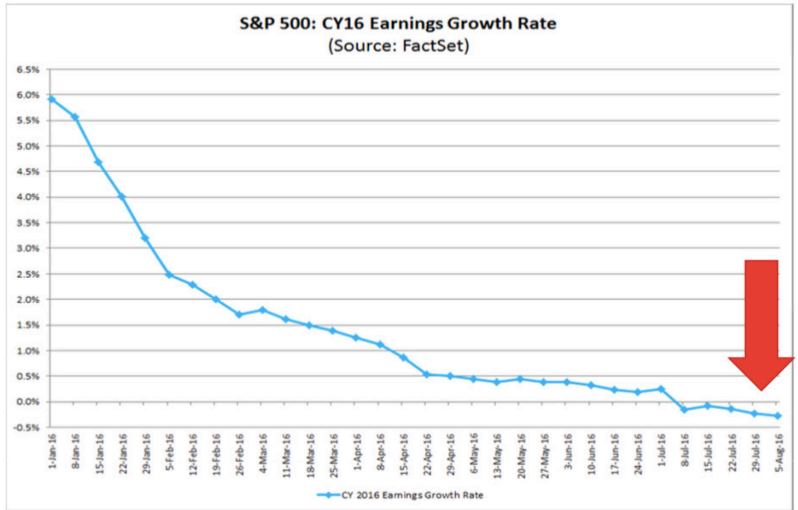
The next logical question, at least to us from our thematic investing perspective, is what are some catalysts that could spark the market higher near-term? With June quarter earnings season winding down, and the number of economic data points slowing down as well over the next few weeks, the answer to that question is likely fewer than most would like to hear.

A Fed rate hike? Even the stock market is beginning to shrug off comments from Federal Reserve central bankers about how a September rate hike is still on the table — more on that in a moment.

As of last week, 91 percent of the **S&P 500** had reported June quarter results, which means there is a high degree of confidence when saying June quarter earnings fell 3.5 percent. Consensus expectations now have revenue growth returning in the current quarter with earnings growth to return in Q4 2016. Perhaps we might have greater confidence in that view if expectations for 2016 S&P 500 earnings didn't continue to fall seemingly every month if not every week this year.

Buried inside those latest round of 2016 forecasts we find second half earnings are expected to advance 9.5 percent compared to the first half.

Two observations: that expected rate is down from 13 percent or so expectation being batted around several weeks ago and nearly all the expected growth comes in the December quarter. Quite a tall order when we consider that corporations have been more focused on buyback spending and dividend hikes than investing in their business — we don't see this changing dramatically until at least early 2017. It is an election year.



Q2 2016: EARNINGS SCORECARD

EXHIBIT 3A. S&P 500: Q2 2016 EARNINGS VS. EXPECTATIONS

Sector	Above %	Match %	Below %	Surprise Factor %	Reported Total #	Index Total #
Consumer Discretionary	77%	6%	17%	6%	64	83
Consumer Staples	71%	14%	14%	3%	28	36
Energy	62%	8%	30%	-26%	37	37
Financials	66%	13%	21%	3%	92	92
Health Care	83%	9%	8%	3%	53	57
Industrials	69%	13%	18%	6%	67	68
Materials	56%	11%	33%	3%	27	27
Technology	82%	14%	4%	8%	57	67
Telecom Services	60%	20%	20%	1%	5	5
Utilities	54%	7%	39%	4%	28	28
S&P 500	71%	11%	18%	4%	458	500
Real Estate	50%	18%	32%	-1%	28	28
Financials Ex-Real Estate	73%	11%	16%	4%	64	64

Source: Thomson Reuters I/B/E/S

Call us skeptical, but all of this feels very much like Wall Street is attempting to play some Jedi mind tricks, asking investors like us to ignore reality (*"These are not the droids you are looking for"*).

Then there is this: last week the **NY Federal Reserve** reported US household debt hit $12.29 trillion in 2Q 2016, up $434 billion from a year earlier. The culprits were:

- **Greater auto debt,** up $97 billion year-over-year to $1.10 trillion, coinciding with the 17.5 million cars and light trucks sold in the U.S. in 2015, breaking a 15-year record and a 5.7 percent increase over 2014.

- **Higher credit card debt,** which marked its 14th consecutive quarterly increase as well as higher levels of both mortgage debt and student loan debt. Even though interest rates remain low, higher debt levels generate greater interest payments and pressure already stretched consumers incomes.

Why does this matter? As we saw in the initial **2Q 2016 GDP** print, it was the consumer that, "led" the way, but with higher debt levels, the odds are pretty good that the consumer may not have all that much more to give as we enter the seasonally strong second half shopping season. While this is likely to crimp Back to School spending some, the real impact is likely to be felt afterward as shoppers turn to the year-end holidays.

Put those together and once again net income expectations are looking a tad aggressive for 2016 and the December quarter in particular. Notice we said net income, which removes the accretive and wonder-bra like effect of share repurchase programs.

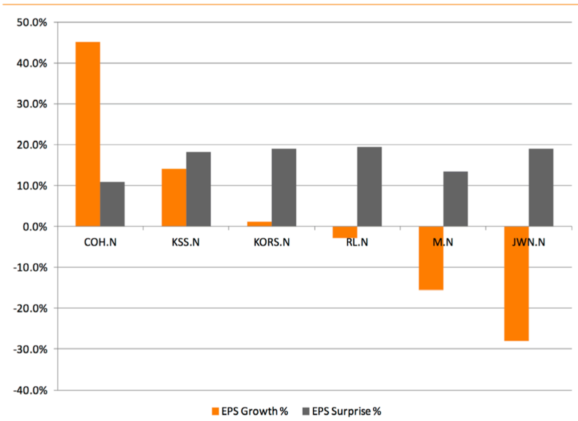
But what if corporate buyback programs begin to slow?

Both **CVS Health (CVS)** and **Alphabet (GOOGL)** have already completed their 2016 share repurchase programs and odds are they are not the only ones. Potentially more risk to the downside for earnings expectations over the next few quarters even before we start focusing on how aggressive current 2017 earnings expectations (up 13.3 percent year over year!) are for the S&P 500.

As we said above, 91 percent of the S&P 500 companies have reported earnings already. Given the non-calendar fiscal year ends for most retailers, those earnings will take center stage as 19 of the 35 companies in the index scheduled to report earnings over the next two weeks are retailers.

We had a glimpse of what is likely to come from **Macy's (M), Nordstrom (JWN)** and a few other retailers last week that reported bottom line results that were in-line or better than expected even though revenue continued to fall. Despite those "good" retail reports, revenues continued to drop on a year over year basis and bottom line results benefitted by share buybacks, particularly at Macy's.

EXHIBIT 2A. RETAILERS REPORTING THIS WEEK: EPS GROWTH AND SURPRISE



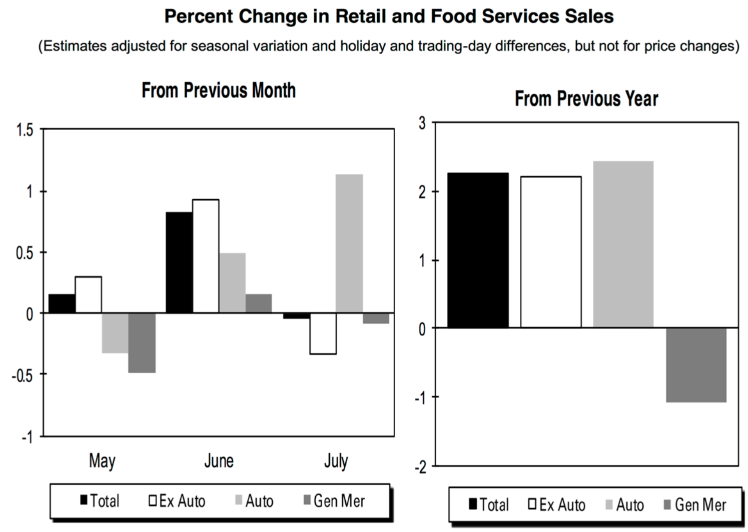
Source: Thomson Reuters I/B/E/S

Think of it this way, if brick & mortar retail was truly doing well, odds are Macy's would not be closing another 100 stores, roughly 15 percent of its retail footprint. But as Macy's CEO Terry Lindgren pointed out, there is excess retail capacity in the US, roughly 5.5 times the number of retail physical locations in America per capita than any country in the world, which means we are likely to see more "rationalization" ahead as traditional retailers continue to struggle with what is to them a ***Connected Society*** headwind.

Friday's July Retail Sales Report offered Connected Society Confirming Data.

The headline figure for the **July Advance Monthly Retail Trade and Food Services Survey (MARTS),** or more commonly known as the **July Retail Sales Report** came in unchanged versus June, and while the number was up 2.3 percent vs. July 2015, it fell short of expectations. It seems those higher debt levels we mentioned above are already starting to weigh on consumer purse strings.

Excluding the impact of auto sales, July retail sales fell 0.3 percent month over month. We'd also note that comparisons were affected by the sharp drop in retail gas station sales, down 2.7 percent month over month and a whopping 11 percent year over year, which reflects the 6.3 percent drop in gas prices in July vs. June (a 19.4 percent drop year over year in July) per Energy Information Administration data. Digging into the line items, much like we've seen in the last several reports, the July data bolstered the case for the accelerating shift toward digital (online and mobile) shopping - year over year, non-store retail sales rose 14.1 percent.



Returning to our earlier mention of the Fed Rate hike, the softer than expected July Retail Sales report knocked some wind out of the Fed tightening expectations, which reverberated through to the US dollar. The weaker dollar helped oil prices move modestly higher, adding to some of the biggest gains in over a month at the end of last week. Per the weekly Baker Hughes rig count report, the number of US crude oil rigs continued to rise last week with another 15 back in production. While that continues the upward trend, the total number of rigs in production was 396, well below the 672 that were pumping away this time last year. From our perspective, we'll continue to watch the demand side of the equation as much as the supply side both here at home and abroad.

Speaking of which, on Friday the **International Monetary Fund** shared it view that China's economy will grow 6.6 percent this year. While that is better than expected, the report went on to forecast a continued slowing in China's economy over the next several years as the country struggles with "slower private investment and weak external demand." More reasons to think global growth will have a tough time breaking out of the malaise of the last few years, and something to ponder as we begin to shift our focus from 2016 earnings to those already robust 2017 earnings expectations. When Wall Street gets off the beach in a few weeks, odds are this will soon become a topic of conversation.

Looking Forward to the Week Ahead

We've already touched on what's coming from an earnings perspective — retail, retail and more retail, but what about the economic calendar for this week?

We'll be paying close attention to the July housing data as well as the **July industrial production report**. We'll also be assembling the various regional Fed manufacturing reports for August as we look to piece together the degree to which the economy is picking up as some expect from that initial and horrific 2Q 2016 GDP print.

Currently, the ever-optimistic Atlanta Fed GDP Now reading sits at 3.5 percent for the current quarter. Before we get all "rah-rah" over that forecast, we'd note this model is already inching down current quarter expectations.

Also too, this model originally predicted

- Growth of +2.9 percent in 4Q 2015, with the actual coming in at 0.9 percent;
- Predicted +2.7 percent for 1Q 2016, with the actual at +0.8 percent;;
- And +2.9 percent for 2Q 2016, with the actual currently at +1.2 percent.

Yeah… we'll continue to focus on the data rather than rely on the predictive powers of the Atlanta Fed.

A few weeks ago, we cautioned that as the frequency of June quarter corporate earnings slowed, we would be entering a seasonally weak time for the market. It seems that once again, the financial media is catching up to our way of thinking — this headline "Traders bet on another late-August volatility spike" appeared on CNBC.com last week, with the gist of the story being that if the Volatility Index (better known as the "VIX") was below 12 in August, "there was almost a sure bet that the VIX will be higher three months out by more than 6 percent with a fair possibility of an outsized move."

Heading into the weekend, the VIX was once again well below 12. As we enter the dog days of summer, better known as the last few weeks of August we'll continue to keep an eye on the VIX. With the market at increasingly stretched valuation levels, we will continue to be prudent with the Tematica Select List as well as our own proprietary Thematic Index. As of Friday's market close that index is up more than 14 percent year to date compared to 6.84 percent for the S&P 500.

As the next few weeks progress, there is a strong likelihood the pace of things will continue to slow until summer vacations are over and we move past

ECONOMIC CALENDAR		AUG. 15 - 19, 2016
DATE	REPORT / SPEECH	DATA
15-Aug	**Empire Manufacturing**	Aug
15-Aug	**NAHB Housing Market Index**	Aug
15-Aug	**Net Long-Term TIC Flows**	Jun
16-Aug	**Building Permits**	Jul
16-Aug	**Core CPI**	Jul
16-Aug	**CPI**	Jul
16-Aug	**Housing Starts**	Jul
16-Aug	**Core CPI**	Jul
16-Aug	**Housing Starts**	Jul
16-Aug	**Building Permits**	Jul
16-Aug	**Capacity Utilization**	Jul
16-Aug	**Industrial Production**	Jul
16-Aug	**Capacity Utilization**	Jul
17-Aug	**MBA Mortgage Index**	13-Aug
17-Aug	**Crude Inventories**	13-Aug
17-Aug	**FOMC Minutes**	27-Jul
18-Aug	**Initial Claims**	13-Aug
18-Aug	**Continuing Claims**	6-Aug
18-Aug	**Philadelphia Fed**	Aug
18-Aug	**Leading Indicators**	July
18-Aug	**Natural Gas Inventorie**	

the Labor Day weekend (September 5). From our perspective, that relatively quieter time will allow us to roll up our sleeves on potential contenders for both the Tematica Select List as well as the Thematic Index.

EARNINGS ANNOUNCEMENTS THIS WEEK

The following are just some of the earnings announcements we'll have our eye on for thematic confirmation data points:

AFFORDABLE LUXURY

- Coty Inc (COTY)

CASHSTRAPPED CONSUMER

- Home Depot Inc (HD)
- TJX Companies Inc (TJX)
- Childrens Place Inc (PLCE)
- Target Corp (TGT)
- Stein Mart Inc (SMRT)
- Tuesday Morning Corp (TUES)

CONNECTED SOCIETY

- NetApp Inc (NTAP)

CONTENT IS KING

- MSG Networks Inc (MSGN)

DISRUPTIVE TECHNOLOGIES

- Cree Inc (CREE)

FATTENING OF POPULATION

- Famous Dave's of America Inc (DAVE)
- Domino's Pizza Enterprises Ltd (DPZ)

FOODS WITH INTEGRITY

- Hain Celestial Group Inc (HAIN)

GUILTY PLEASURES

- Nestle SA (NESN.VX)

RISE & FALL OF MIDDLE CLASS

- Dick's Sporting Goods Inc (DKS)
- American Eagle Outfitters Inc (AEO)
- Gap Inc (GPS)
- Foot Locker Inc (FL)

SAFETY & SECURITY

- Alarm.Com Holdings Inc (ALRM)

TOOLING & RETOOLING

- Learning Tree International Inc (LTRE)

TOOLING & RETOOLING

- DeVry Education Group Inc (DV)