MONDAY MORNING KICKOFF

YOUR MARKET PRIMER FOR THE WEEK AHEAD

WEEK OF SEPTEMBER 12, 2016

Before we took our Labor Day siesta last week, we mentioned September tends to be one of the worst months for the stock market. After trending sideways for pretty much most of August and the first few days of September, we were proven prescient, with several items hitting last week that raised "caution ahead" flags. Those events also renewed Fed talk about the next interest rate move, and that on the back of those flags, much like a dog on the 4th of July, the market was spooked, sending all the major indices into retreat mode — the DOW down 394.46 points, the NASDAQ down 2.5%, and our preferred market benchmark, the Standard & Poor's 500, down 2.45%.

The "caution ahead" flags included the back-to-back weak **August ISM Manufacturing** and **Employment Reports**, which were followed this week by the **August ISM non-manufacturing Index** (better known as the service sector) falling to 51.4 in August from 55.5 in July — the lowest level since early February 2010 and the biggest monthly drop since November 2008. Looking at the combined ISM reports, August fell to 51.2 from 55.1 in July marking the lowest reading since January 2010 and the largest monthly drop since November 2008.

What this tells us is the forecasted rebound in the economy is not shaping up quite as expected.

While you might think the market was spooked following the North Korea's latest nuclear bomb test, which is indeed pretty unnerving, it was **Federal Reserve Bank of Boston President Eric Rosengren** who rocked the market last Friday. During a speech, Rosengren said that "a reasonable

Thematic Signals

[This land is MY land, this land is MY land...](#)
Scarce Resources

[Why Uber chose this city to test its self-driving car fleet](#) *Disruptive Technologies*

[Coca-Cola's (KO) Management trying not to let its can get kicked down the road](#)
Fattening of Population / Foods with Integrity

[JCPenney launches new plus-size only line designed by Project Runway winner](#)
Fattening of Population

[LEGO, spreading pain throughout the world](#)
Rise & Fall of the Middle Class

READ MORE

TEMATICA RESEARCH

ABOUT THE MONDAY MORNING KICKOFF

In order to get ready for the week ahead, the team at Tematica traces the key happenings of the past week and looks at the economic and earnings calendars slated to come out for the coming week in order to identify key catalysts that are bound to the shape the market in the near-term, and in-turn impact our tematics.

case can be made" for tightening interest rates to avoid overheating the economy. Given the August data received thus far, we're inclined to think Rosengren is either still jet-lagged from his recent trip to China last month where he made similar comments, or he hasn't had time to digest the latest data. In our view, Rosengren's comments likely mean additional weight will be put on this week's **August PPI and CPI readings**.

Keep in mind, Rosengren's comments came after the Fed's latest **Beige Book** was published during the middle of last week. The Beige Book is based on data compiled on or before August 29th and its findings revealed that most of the 12 districts reported "fairly modest" wage pressures that are expected to remain as such over the coming months. Overall, price increases were subdued and consumer spending was little changed.

Federal Reserve Bank of Boston President Eric Rosengren

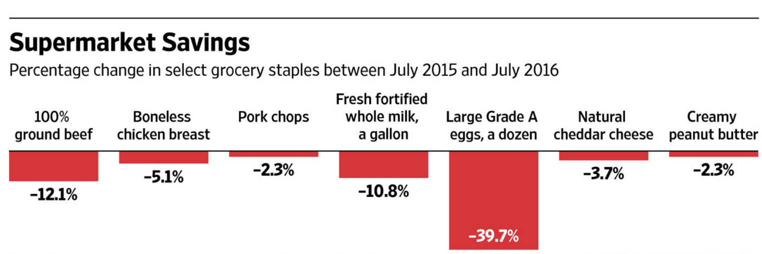
"If we want to ensure that we remain at full employment, gradual tightening is likely to be appropriate," he said. "A failure to continue on the path of gradual removal of accommodation could shorten, rather than lengthen, the duration of this recovery."

Uncertainty surrounding the outcome of the presidential election appears to be increasing caution around expansion plans, with only modest expectations for sales and construction activity in the coming months. While not exactly a measure of the market, to say the least, we found it telling that the word "flat" was used 56 times in the August report, versus 36 times in the last Beige Book this past July. **Where can you get that kind of analysis?**

Our key takeaway was the Beige Book gave little indication that we are likely to see what others have been predicting as a dramatic surge in growth during the second half of 2016, something we've been quite openly skeptical of, given the lack of identifiable catalysts for such a move. The follow through on that thought is prospects for a pronounced pickup earnings from the S&P 500 companies in the December quarter is likely to underwhelm, relative to current expectations.

One piece of news that caught the market by surprise and provoked a critical look at grocery stocks.

Sprouts Farmers Market (SFM) revised its guidance for the third quarter and for the full fiscal 2016 downward, pushing its stock down nearly 14%, citing food deflation as the culprit. Of course falling food prices impact all grocery chains, and thus this news rippled throughout the category, sending shares of **Whole Foods Market (WFM), Kroger (KR) , Supervalu (SVU)** and **Costco Wholesale (COST)** lower, as well as America's largest grocer, **Wal-Mart**



(WMT) whose shares fell over 3% just last week. Adding to the mix, Friday morning Kroger reported its quarterly results. Those results came in ahead of expectations — good news of course — but the company also commented that sales comparisons are trending toward the low end of expectations, deflation is expected to continue and consumers are cautious about the economy. Other than that, things are looking great! (Note our sarcasm in that statement).

Consumer Credit Balances

Outstanding consumer credit balances increased in July by a seasonally adjusted $17.7 billion versus expectations for a $16 billion increase for a 5.83% adjusted annual growth rate in July compared to 4.8% in June. Rising credit balances can reflect one of two things: increased confidence or rising financial stress.

Consumer Credit Outstanding [1]
Seasonally adjusted. Billions of dollars except as noted.

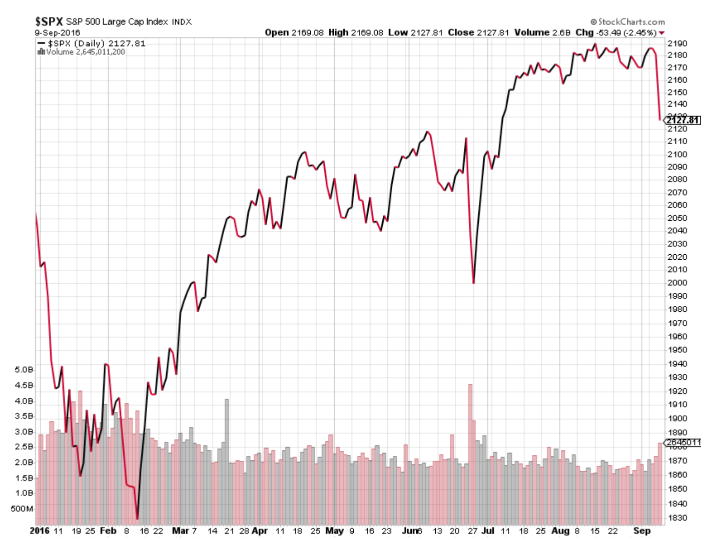
	Year					Quarter					Month		
						2015			2016				
	2011	2012	2013	2014	2015	Q2	Q3	Q4	Q1[r]	Q2[r]	May[r]	Jun[r]	Jul[p]
Total percent change (annual rate)[2]	4.2	5.9	6.0	7.2	7.0	7.9	7.1	6.2	5.6	6.4	7.5	4.8	5.8
Revolving	0.2	0.5	1.4	3.9	5.2	6.9	5.6	5.9	4.8	7.2	5.9	11.5	3.4
Nonrevolving [3]	6.0	8.3	7.9	8.4	7.7	8.3	7.7	6.3	5.9	6.1	8.1	2.4	6.7
Total flow (annual rate)[2,4]	111.1	164.1	175.8	221.8	232.7	266.6	244.1	216.3	199.1	230.3	270.8	174.3	212.6
Revolving	2.1	4.2	12.0	33.8	46.4	62.3	51.0	54.6	44.7	68.7	55.8	110.0	33.3
Nonrevolving [3]	109.0	159.9	163.9	188.0	186.4	204.4	193.1	161.8	154.3	161.7	215.1	64.3	179.2
Total outstanding	2,758.3	2,920.4	3,096.2	3,318.0	3,535.7	3,435.6	3,496.6	3,535.7	3,585.5	3,643.1	3,628.6	3,643.1	3,660.8
Revolving	841.5	845.7	857.7	891.5	937.9	911.5	924.2	937.9	949.1	966.2	957.1	966.2	969.0

Given that we've seen total hours worked by the American employee falling, we aren't inclined to assume increased confidence levels just yet. Paired with the continued increase in auto loan delinquencies, we suspect it means at least a portion of consumers are once again on the verge of being overextended.

Given the consumer is one of the key engines of the US economy, this pours some cold water on any robust second half expectations for both GDP and earnings, particularly retail earnings.

Markets Breakout of Range, Unfortunately in the Wrong Direction

All of this culminated with the major indices finally breaking with the summer trend of sideways trading that we've never seen before. Looking back to when the S&P 500 index began in 1928, never before has it experienced a 42-day trading period with a smaller hi/lo spread. That confluence of factors led the S&P 500 to fall 2.45% on Friday.



Ouch!

It's been our view that once both Wall Street and Main Street got back to work, rolled up their sleeves to review the latest economic reports and juxtaposed them against earnings expectations, odds are market volatility would kick back up.

We were not disappointed, but with most of Wall Street focusing on what the Fed may do at the conclusion of the Fed's FOMC meeting on Sept 21, we still have concerns over what we see as aggressive earnings expectations as we move from 3Q 2016 to 4Q 2016. After all, if recent economic data in the form of the **August Employment Report, August ISM Index** and **August ISM Services Index** are showing the wrong vector and velocity for the US economy, odds are earnings expectations for 2016 will once again need to be reset lower. Balance that against the S&P 500 — our preferred barometer for the stock market — trading at 18.X consensus earnings expectations, and any downward revision means we are paying even more for slower earnings growth.

Last Thursday we learned the European Central Bank was going to leave all its key rates unchanged, despite inflation in the 19-nation block remaining at historical lows. It will continue its asset-purchase program of $90 billion through the end of March 2017. No new monetary stimulus there, but what they've got going has been pretty substantial as it is, without clear success from such efforts. Pretty much validating what we've seen here at home.

Hmmm… at some point, economic reality is going to catch up with earnings expectations. We will continue to navigate potentially choppy waters through the rest of September and into October carefully as it pertains to the ***Tematica Investing Select List*** as well as our larger thematic facing Thematic Index.

With that in mind, let's turn our attention to the week ahead…

We have a full week of trading ahead of us, and that means a full plate of economic data. On the heels of the disappointing ISM indices, this week we have **August Retail Sales** and both inflation measures (CPI and PPI) for the month. Once again we expect the Retail Sales report to put some perspective and clarity on recently reports on August same-store-sales results from a variety of retailers. In our view, companies like the **Gap (GPS)** and **Buckle (BKE)** are very different animals compared to **Wal-Mart (WMT)** and **Costco (COST)**.

Also on deck is the **August Industrial Production Report**, which is likely to show continued strength in utility production given the hot, hot, hot month of August, but we'll be looking for confirmation for the **ISM Manufacturing Index** when we examine the **Industrial Production report** in detail. We'll also be looking for confirmation in our latest Tematica Pro call option trade.

As we look to get a bead on how September is shaking out and what the overall third quarter is looking like, we'll get our first clues this week from the **Empire**

ECONOMIC CALENDAR SEPT 12 - 16, 2016

DATE	REPORT / SPEECH	DATA
13-Sep	**Treasury Budget**	Aug
14-Sep	**MBA Mortgage Index**	10-Sep
14-Sep	**Export Prices ex-ag.**	Aug
14-Sep	**Import Prices ex-oil**	Aug
14-Sep	**Crude Inventories**	10-Sep
15-Sep	**Initial Claims**	10-Sep
15-Sep	**Continuing Claims**	3-Sep
15-Sep	**Retail Sales**	Aug
15-Sep	**Retail Sales ex-auto**	Aug
15-Sep	**PPI**	Aug
15-Sep	**Core PPI**	Aug
15-Sep	**Philadelphia Fed**	Sep
15-Sep	**Current Account Balance**	Q2
15-Sep	**Empire Manufacturing**	Sep
15-Sep	**Industrial Production**	Aug
15-Sep	**Capacity Utilization**	Aug
15-Sep	**Business Inventories**	Jul
15-Sep	**Natural Gas Inventories**	10-Sep
16-Sep	**CPI**	Aug
16-Sep	**Core CPI**	Aug
16-Sep	**Mich Sentiment**	Sep
16-Sep	**Net Long-Term TIC Flows**	Jul

Manufacturing and **Philly Fed Index.** We're already starting to see cracks in the Atlanta **Fed's GDPNow** forecast for the September quarter. If the data to come resembles that which we've gotten over the last several weeks, odds are the downward revisions will continue.

EARNINGS ON TAP THIS WEEK

AGING OF THE POPULATION

- Imprivata (IMPR)

CASHLESS CONSUMPTION

- USA Technologies (USAT)

CONNECTED SOCIETY

- Adobe Systems (ADBE)
- Oracle Corp. (ORCL)

CONTENT IS KING

- Marcus Corp. (MCS)

DISRUPTIVE TECHNOLOGIES

- Apigee Corp. (APIC)

ECONOMIC ACCELERATION/DECELERATION

- GMS Inc. (GMS)

FATTENING OF THE POPULATION

- Farmer Brothers (FARM)
- Cracker Barrel (CBRL)

FOODS WITH INTEGRITY

- United Natural Foods (UNFI)
- Hain Celestial (HAIN)

FOLLOW US: