

# MONDAY MORNING KICKOFF

## YOUR MARKET PRIMER FOR THE WEEK AHEAD



### Don't Be Fooled By the Market, Several Uncertainties Loom Ahead

The first week of 2017 is now over. Granted it was a short one for the markets, but it saw the **Dow Jones Industrial Average** come ever so close to breaking through the 20,000 level.

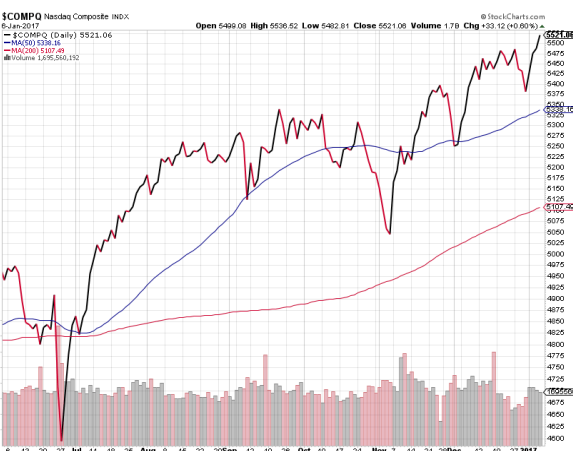
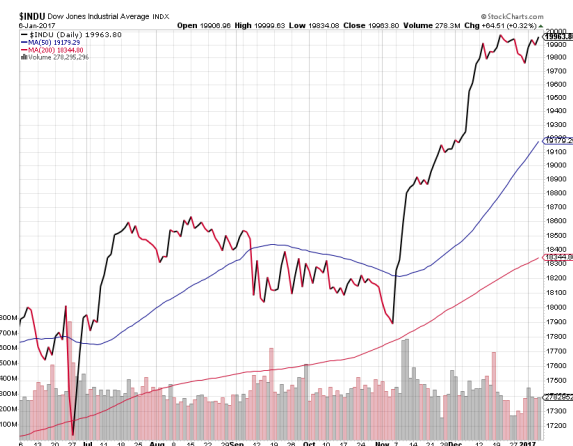
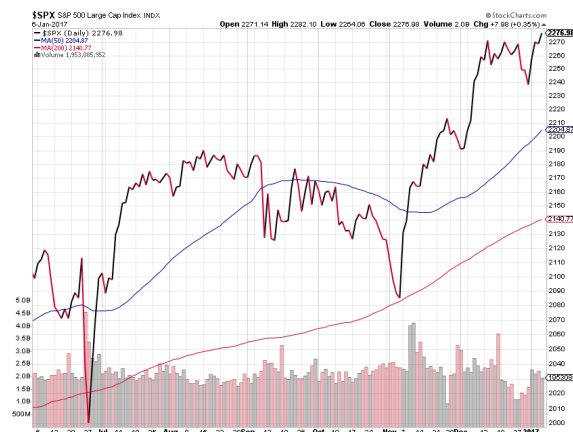
Not to be left out, both the S&P 500 and the Nasdaq Composite Index climbed higher, with the S&P 500 up more than 1.5 percent and the Nasdaq up more than 2.5 percent.

The later benefitted from the **2017 Consumer Electronic Show (CES 2017)** conference last week, which featured the typical announcements that benefit our **Connected Society**, **Asset-Lite** and **Disruptive Technology** investing themes. This year was no different, given the show's focus on new display technologies, digital assistants, and the Connected Car.

Those developments contributed to the technology-heavy Nasdaq breaking out of its mid-December range to close Friday at a new high. Meanwhile, the **S&P 500** closed within points of its 52-week high, or at 17.1x expected 2017 earnings of \$132.92 per share for the S&P 500. Now for a dash of perspective, that earnings forecast equates to 12 percent growth year-over-year — something we've not seen in quite some time.

As we'll discuss further on, there are still a number of uncertainties hanging over our heads — ranging from Trump policies to additional dollar strengthening — all of which could end up weighing on that S&P 500 earnings outlook.

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#### 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 shape the market in the near-term, and in-turn impact our tematics.

## Our First Looks at the Jobs Equation for 2017

CES 2017 wasn't the only center of news last week. Last Friday we received the first Employment Report of 2017 and, in a nutshell, it was weaker than expected. 156K jobs were created in December vs. the expected 176K jobs and much less than the upwardly revised 204K jobs (from prior 178k) created in November. By sector, the job gainers continued to be healthcare, (which bodes well for our **Aging of the Population** investment theme) social assistance, and food services — combined, those three categories accounted for 60 percent of new jobs created in December. Other job gainers included transportation, financial activities, manufacturing and business services.

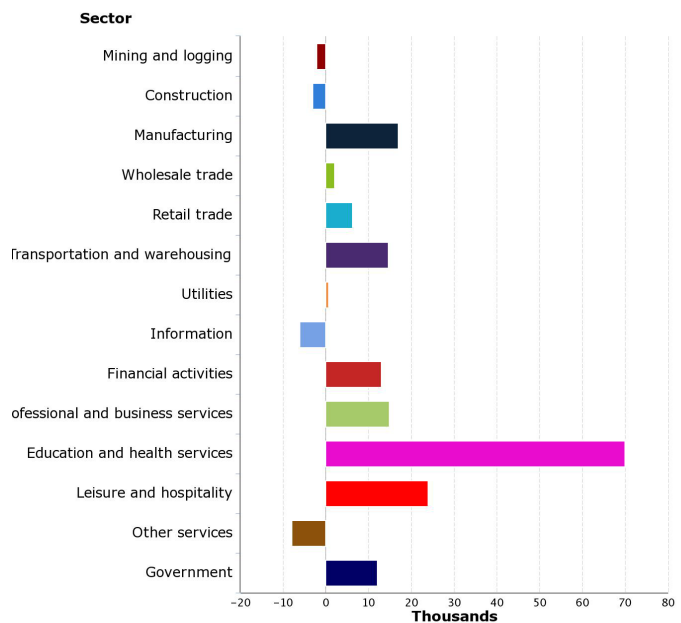
The big miss relative to expectations in the December report was with private sector jobs, which came in at 144K in December vs. 198K in November. The even bigger realization was the labor force participation ratio was little changed in December at 62.7 — and level that was essentially unchanged during all of 2016. The same goes for the employment-population ratio, which once again hovered near 59.7 percent. Those figures put a sobering view on the media touting the final month of President Obama's term marked the 75th straight month that US employers added jobs, the longest such stretch on record since 1939.

In our view, those payroll-to-population and employment-to-population figures help explain the angst that led to the election of Donald Trump, as well as the post-election optimism and hope for the economy. While we are all for hope and enthusiasm, it's never been a good move to invest based on those two things. As sobering reminder, we have yet to hear the policies to be proposed by President-elect Trump, yet to know which policies will be passed and what the potential economic impact will be.

We'd also note this report tends to be volatile month-to-month, so we like to look

Employment change by industry, December 2016, seasonally adjusted, 1-month net cha

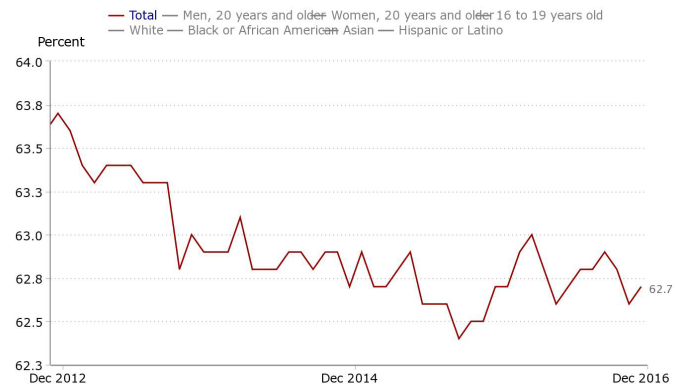
Click on bars to drill down



Source: U.S. Bureau of Labor Statistics.

Civilian labor force participation rate, seasonally adjusted

Click and drag within the chart to zoom in on time periods



Hover over chart to view data.  
 Note: Shaded area represents recession, as determined by the National Bureau of Economic Research.  
 Persons whose ethnicity is identified as Hispanic or Latino may be of any race.  
 Source: U.S. Bureau of Labor Statistics.

the data from a longer-term perspective, like the twelve month moving average, to get a better idea of the longer-term trends. From that lens we can see that new job creation peaked back in February of 2015 and has been trending downward ever since. Not exactly something the media is reporting, and again, it helps explain the voter mindset this past November.

That Trump uncertainty, along with the fact that we are caught between the recent end to 2016 and the start of December quarter earnings season that begins shortly, means we are more or less in investing limbo.

## We also can't talk job creation without considering the Fed.

Yes, the Fed just raised interest rates in December for the second time in two years, but it also telegraphed it could raise those same interest rates three more times in 2017 — yes, not 1, not 2, but 3 times in a twelve month period. That's a far more rapid pace than we've seen and it sent bank stocks like **JPMorgan (JPM)**, **Wells Fargo (WFC)**, **Citigroup (C)** and others soaring.

The big question is will the Fed actually raise interest rates that many times in 2017?

Remember the Fed talked quite a bit about boosting interest rates over the last two years, yet has only raised them twice during that time period, and that means while the Fed may like to hit its target of boosting rates three times in 2017, odds are it will remain not only data-dependent but also dependent on us waiting to understand the policies to be proposed by Trump and their impact. The recent notes from the Federal Reserve Open Market Committee meeting indicated that they are concerned that Trump may push through legislation and policies that are inflationary, which would shift the Fed into a more hawkish stance.

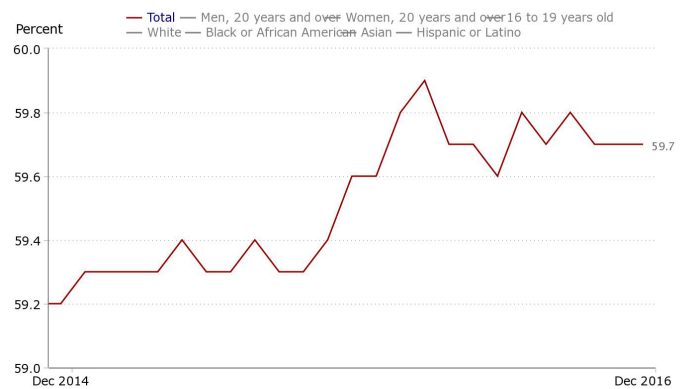
In other words, we're back in the "will they, won't they" Groundhog Day like nature of watching the Fed as we enter and move deeper into 2017. Pretty much, more of the same to what we saw in 2015 and 2016.

## Let's layer in even more data to add some perspective to Friday's Employment Report.

Early last week, we learned the Manufacturing economy was on stronger footing in December compared to November, per data from ISM and Markit Economics, but also per ISM the services economy slipped and ADP's take on December job creation was less than expected. It's looking like the National Retail Federation may once again have overestimated consumer spending this past holiday shopping season. Following a 2.7 percent decrease

### Employment & population ratio, seasonally adjusted

Click and drag within the chart to zoom in on time periods



Hover over chart to view data.  
 Note: Shaded area represents recession, as determined by the National Bureau of Economic Research.  
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 Source: U.S. Bureau of Labor Statistics.

in November and December comparable sales, **Macy's (M)** announced additional layoffs as it begins to close 100 of its 730 locations. The same day, **Kohl's Corp. (KSS)** announced that its stores also had disappointing holiday sales figures and did **JCP Penny (JCP)**. Adding to the brick & mortar retail pain, **Barnes & Noble (BKS)**, **L Brands (LB)** and **Sears Holdings (SHLD)** added their own disappointing holiday results.

How bad was it?

It was so bad that Sears, which is closing 150 Sears and Kmart locations, agreed to sell its Craftsman tool business to **Stanley Black & Decker (SWK)** for \$900 million.

By comparison, **Amazon (AMZN)** shared that it shipped billions of packages this past holiday shopping season, and added even more Amazon Prime customers to its roster. Even as it offered a dour view on brick & mortar retail, Macy's outgoing CEO Terry Lundgren did mention double-digit increases at its digital business. Even when Nike reported its quarterly earnings in mid-December it boasted a 46 percent year-over-year increase at nike.com.

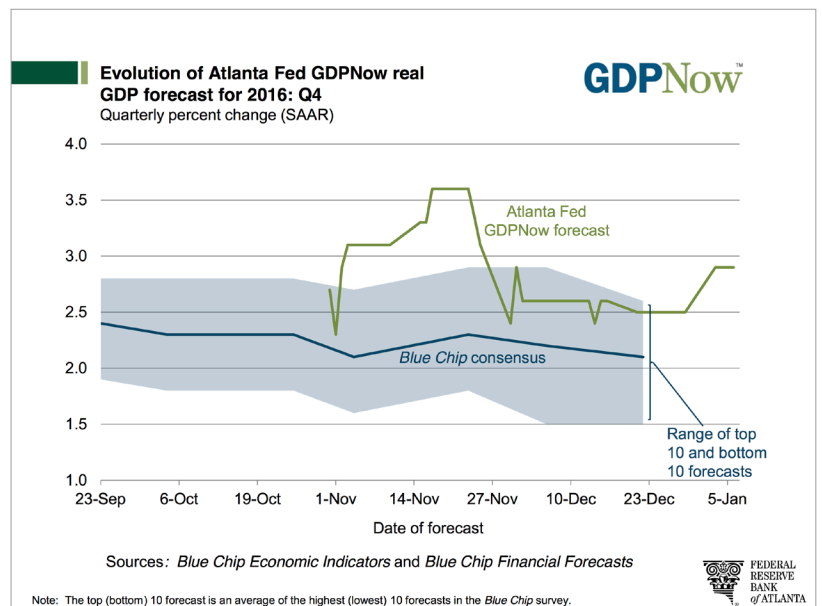
We take all of those comments as positive indicators for the accelerating shift towards online and mobile commerce that is a key aspect of our **Connected Society** investing theme. Those comments also help explain why 5.8 million packages were expected to be returned during the first full week of January by US holiday shoppers, adding to the increased demand enjoyed by shippers such as **FedEx (FDX)** and **United Parcel Service (UPS)** from the shift to online and mobile shopping.

Factoring in the December Employment Report, the Atlanta Fed's GDP Now reading still sat at 2.9 percent for 4Q

MANUFACTURING AT A GLANCE						
December 2016						
Index	Series Index Dec	Series Index Nov	Percentage Point Change	Direction	Rate of Change	Trend* (Months)
PMI®	54.7	53.2	+1.5	Growing	Faster	4
New Orders	60.2	53.0	+7.2	Growing	Faster	4
Production	60.3	56.0	+4.3	Growing	Faster	4
Employment	53.1	52.3	+0.8	Growing	Faster	3
Supplier Deliveries	52.9	55.7	-2.8	Slowing	Slower	8
Inventories	47.0	49.0	-2.0	Contracting	Faster	18
Customers' Inventories	49.0	49.0	0.0	Too Low	Same	3
Prices	65.5	54.5	+11.0	Increasing	Faster	10
Backlog of Orders	49.0	49.0	0.0	Contracting	Same	6
New Export Orders	56.0	52.0	+4.0	Growing	Faster	10
Imports	50.5	50.5	0.0	Growing	Same	3
<b>OVERALL ECONOMY</b>				Growing	Faster	91
<b>Manufacturing Sector</b>				Growing	Faster	4

Manufacturing ISM® Report On Business® data is seasonally adjusted for the New Orders, Production, Employment and Supplier Deliveries Indexes.

\*Number of months moving in current direction.



2016 as of last Friday vs. the third GDP print of 3.5 percent for 3Q 2016. As we've discussed in these pages during December, other firms are well below that 2.9 percent forecast for 4Q 2016, including the NY Federal Reserve and its NowCast publication. The Wall Street Journal's latest Economic Forecasting Survey puts GDP at 2.3 percent for 4Q 2016 as well as 1Q 2017 with a modest uptick to 2.4 percent in 2Q 2016. If Q4 comes in around 2 percent, we will have seen 1.6% GDP growth for the full year of 2016, a far cry from the 2.6% in 2015 and well below the pre-financial crisis long-term average going back to the 1930s of over 3 percent.

**No matter how we slice it, the economy is shifting down a gear or two and faces some headwinds in the dollar, which could get worse should the Fed actually raise interest three times this year.**

Putting it all together reminds us that despite the enthusiasm and hope that has overtaken the stock market about President-elect Trump jumpstarting the economy, we still have to navigate through the December quarter and most likely at least the first half of 2017 before his policies, whatever they wind up being, start to have an impact on the economy. Given warnings from retailers, as well as cautionary comments from **Honeywell (HON)** and **Adobe Systems (ADBE)** over the potential impact of continued dollar strength in 2017, there are reasons to look at the recent market moves and think it has gotten a bit ahead of itself, with the forward price-to-earnings ratio on the S&P 500 at levels not seen since 2002, which was quickly followed by a 30 percent decline in the market.

As Tematica's Chief Macro Strategist Lenore Hawkins pointed out during a visit with Varney & Company on Fox Business last Friday, the market is not pricing in the level of political risk we face this year, with elections coming up in Germany, France, the Netherlands and potentially Italy. Those elections, that include the threat of euro-skeptics Marine Le Pen in France and the Five Star Movement in Italy gaining political momentum, could lead to serious weakening with the euro.



A fall in the euro currency would strengthen the dollar significantly, which would weigh on not only dollar-denominated commodities, but also export business for US companies. In other words, the current currency headwind could get even stronger.

If we get more of the same commentary from Honeywell, Adobe, Macy's, Sears, JC Penney, Kohls's and even **Fattening of the Population** thematic contender **Sonic Corp. (SONC)** that shared it saw a "sluggish consumer landscape" in the December quarter, we could very well see the market pullback from current levels as the flow of December quarter earnings reports heat up. Should that come to pass, on the back of reset expectations, odds are stocks will be at much fall to more favorable prices than they stand now and that is likely to offer a buying opportunity.



## Gearing Up for a Full 5 Days of Trading & Data

We'll get several clues this week as to whether our pullback expectations are likely as we dip into December quarter earnings with industrial companies **Alcoa (AA)** and **WD40 (WDFC)** as well as **Cashless Consumption** contender **Global Payments (GPN)**. Given the year-end strength in our **Economic Acceleration/Deceleration** investing theme and the number of industries that it touches, we'll be breaking down Alcoa's market commentary and outlook.

Mid-week we get a look at **Cash-strapped Consumer** company **SuperValu (SVU)** and **Connected Society** building block company **Taiwan Semiconductor (TSM)** and potential **Tooling & Re-Tooling** company **Staffing 360 (STAF)**. Closing out the week is a financial smorgasbord on Friday with **JPMorgan Chase (JPM)**, **Wells Fargo (WFC)**, **Bank of America (BAC)**, **Blackrock (BLK)** and **PNC Financial Services (PNC)**, all reporting December quarter results. Inside those reports, we'll be looking to hear about the pace of new loan activity as well as their view on the overall economy in 2017.

Reading between those lines, you likely realized that, yes, this week we're back to a full 5 days of market activity — the first in two weeks! That dribble of earnings reports aside, we've got a full plate of economic data. Among the various reports, the two standouts are likely to be the December PPI, which will be watched closely by the Fed, and December Retail Sales reports. Given recent comments from **Macy's (M)** and other retailers, we're not expecting any upside surprises in the December Retail Sales Report. We will be digging into it to for data relative to our **Cash-strapped Consumer, Connected Society** and other investment themes.

This week we also have the 35th Annual JPMorgan Healthcare Conference 2017, the Needham and Company's 19th Annual Growth Conference as well as the North American International Auto Show of Detroit 2017. We expect there to be much fodder for our Aging of the Population investment theme at the JPMorgan conference, while the auto show is likely to result in several announcements pertaining to driver assisted and driverless technologies. Odds are the recent announcement that **AT&T (T)** is partnering with **Honda Motor (HMC)** to bring 4G LTE connectivity into its vehicles as well as the deals announced by both **Amazon (AMZN)** and **Alphabet (GOOGL)** to bring their digital assistants — Echo and Google Home — to cars from **Hyundai, Ford (F)** and **Chrysler (FCAU)**, is just the start of the Connected Car news flow this week.

Yep, it's going to be a busy one, but be sure to enjoy the week and we'll be back with you next Monday with the next MMKO.

ECONOMIC CALENDAR		JAN 9-13, 2017
DATE	REPORT / SPEECH	DATA
9-Jan	<b>Consumer Credit</b>	Nov
10-Jan	<b>JOLTS - Job Openings</b>	Nov
10-Jan	<b>Wholesale Inventories</b>	Nov
11-Jan	<b>MBA Mortgage</b>	6-Jan
11-Jan	<b>Crude Inventories</b>	6-Jan
12-Jan	<b>Export Prices ex-ag.</b>	Dec
12-Jan	<b>Import Prices ex-oil</b>	Dec
12-Jan	<b>Initial Claims</b>	7-Jan
12-Jan	<b>Continuing Claims</b>	31-
12-Jan	<b>Natural Gas Inventories</b>	7-Jan
12-Jan	<b>Treasury Budget</b>	Dec
13-Jan	<b>PPI</b>	Dec
13-Jan	<b>Core PPI</b>	Dec
13-Jan	<b>Retail Sales</b>	Dec
13-Jan	<b>Retail Sales ex-auto</b>	Dec
13-Jan	<b>Business Inventories</b>	Nov
13-Jan	<b>Mich Sentiment</b>	Jan

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