TEMATICA INVESTING

THEMATIC COMMENTARY, EQUITY RESEARCH & INVESTING STRATEGIES

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Tematica Investing, a weekly publication by Chris Versace, is designed for the experienced or professional investor, providing in-depth information on real-time developing thematic strategies, economic outlook, investment trading ideas, and analysis of the most pressing developments for the market, as well as forces that drive both our thematic perspectives and thematic recommendations.

In this Week's Issue

- While the Fed left interest rates unchanged coming out of its March FOMC meeting, it revised its GDP and inflation forecast for the US economy modestly lower vs. December expectations.
- **Regal Entertainment (RGC)** continues to benefit from a robust box office and indications point to more of the same ahead. We are reviewing our price target on RGC shares with an upward bias.
- We are removing **Philip Morris International (PM)** shares from the **Tematica Select List** and issuing a Sell rating at current levels
- We are adding **ComScore (SCOR)** and **Nielsen NV (NLSN)** to the **Tematica Contender List** as part of our ***Connected Society*** investing theme given the continued shift in advertising spend to Digital platforms from TV, Radio and other legacy media.
- More confirmation for our thematic investing lens is found in this week's edition of Thematic Signals

Economics & Commentary

Last week, the market continued to move higher, but the S&P 500 gave back some of that ground thus far this week in anticipation of the Fed's two-day FOMC policy meeting that culminated in today's public statement.

In recent weeks I have been sharing with you my view the Fed would take a pass on raising interest rates at this meeting and — surprise, surprise — the Fed left rates unchanged. This was hardly shock to anyone paying attention, given the economic data that paints a picture of a slowing global economy, additional rounds of monetary policy stimulus outside the U.S. that we discussed in this week's ***Monday Morning Kick Off (MMKO)***, and the utter lack of inflation as evidenced by today's **February Consumer Price Index Report**.

But here's the thing, even by doing nothing, while other central bankers like the European Central Bank, People's Bank of China, Sweden and others have sprinkled more monetary policy fairy dust, the Fed is de facto tightening simply because it is not matching the latest round of stimulus, aka loosening, around the world

What was somewhat surprising in the Fed's FOMC statement was the official ratcheting back of the expected number of rate hikes to 2, down from 4. Peering into the Fed's updated economic forecast, however, that reduction becomes rather clear — the Fed now sees US GDP at 2.2 percent, down from 2.4 percent in December, and inflation running cooler than previously thought for 2016 at 1.2 percent vs. 1.6 percent.

Now for the "say what?" in the report . . .

The Fed sees the US economy slowing in 2017 and 2018 relative to 2016. This fits with the Fed's commentary that was littered with the word "moderate." Moreover, inflation is not expected to hit the Fed's 2.0 percent bogie until 2018, which means if the economy continues to bump along, and the larger global economy remains challenging, we could see the Fed reduce the number of expected rate hikes from 2 to 1 to 0 over the coming months as more data becomes available. To us here at Tematica, it means that much like what's unfolding given the sharp drop in oil prices, and with Anadarko Petroleum cutting another 1,000 employees (17 percent of its work force), there will likely be another shoe to drop on the corporate earnings front in the coming weeks given the slowing economy and persistent currency headwinds.

Last week, we shared our view that earnings expectations for the S&P 500 group of companies in the second half of 2016 are rather robust, and given the weaker than expected February Retail Sales and Industrial Production Reports this week, we continue to have that perspective. That viewpoint was also reinforced by the shortfall in Industrial Output and Retail Sales in China this past January and February, which also served to fan the speculative flames for even more stimulative fairy dust measures in the coming months.

Given the current climate and near-term outlook, we continue to see growth remaining challenged, but to us that means zeroing in on disruptive technologies, pain points and other shifting landscapes that give rise to pronounced thematic tailwinds. We will continue to look for attractively priced dividend payers that are benefitting from these thematic tailwinds as well. Dividend payers such as our **Regal Entertainment Corp. (RGC), Philip Morris International (PM)** and others have been strong performers thus far in 2016, and should continue to be given the softer economic outlook offered by the Fed. Finally, we will continue to be prudent with the **Tematica Select List**, particularly since we see the risk of a repeat of January's earnings season in April, as we continue to build out the **Tematica Contender List**.

Movie Box Office and RGC Shares Remain Strong

One of the stronger performers on the **Tematica Select List** has been **Regal Entertainment Corp. (RGC)**, a ***Content is King*** thematic investment benefitting from a resurgence at the movie box office. Building on the momentum that began with "Star Wars: The Force Awakens", "Deadpool" and more recently "Zootopia", advance ticket sales for the soon to be released "Batman v Superman: Dawn of Justice's" suggest another strong move in the box office.

According to Deadline, "BvS" is outpacing both "Deadpool" and "Avengers" in advance ticket sales. "Deadpool" opened with $132.4 million last month and "The Avengers" broke records in 2012 with it's $207.4 million opening weekend. Deadline states that "Batman v Superman" has reportedly earned between $20 million-$25 million in advance ticket sales, which puts it on course similar to "Dark Knight Rises" in 2012, which opened to $160.9 million.

Looking past "BvS" the slate of upcoming movies to be had from Marvel, Pixar and other studios look strong, which should continue to the momentum at the box office. While our published price target on RGC shares is $24, we are currently reviewing it with an upward bias. As the shares trend higher we will look to inch up the recommended stop loss from $19 as well.

Removing Philip Morris International (PM) from the Tematica Select List

Since we added **Philip Morris International (PM)** shares to the Tematica Select List last October as a ***Guilty Pleasure*** investment, the shares have climbed more than 20 percent significantly outperforming the S&P 500, which rose just 1.6 percent over the same time period. The position benefitted from the rotation back to dividend yielding stocks over the last few months as signs of global growth slowed. Fitting with our ***Guilty Pleasure*** view, the inelastic nature of the company's products meant the business and the shares would be a safe haven in that environment. While global growth is still on a slowing glide path, PM shares have now entered over bought territory and historically when this has happened the shares have soon corrected.

As such, we will use yesterday's market strength to issue a Sell on PM shares and remove them from the Tematic Select List.

Adding to the Tematica Contender List

Coming out of the December quarter earnings season it's no surprise that our ***Connected Society*** investing theme is encroaching on more and more of our lives. From shopping and banking to how we communicate and stay in touch, the ***Connected Society*** is touching us in more and more ways. More retailers from **Foot Locker (FL) to Aeropostale (AERO) to Macy's (M)** and even **Costco Wholesale (COST)** are all focusing their efforts on online and mobile offerings to match the shift in consumer preferences.

Stepping back a bit, people already spend more than 490 minutes of their day with some sort of media, according to a new report by ZenithOptimedia. If we think about the amount of time that we spend online – non-voice time spent on tablets and mobile phones grew 11.3 percent in 2015 to 2 hours and 54 minutes up from 46 minutes in 2011, time on desktops and laptops dipped over the same period, with bigger drops in time spent with TV and print publications.

Meshing together the outlook for streaming services such as **Netflix (NFLX)**, Hulu and others, as well as broadcast and cable networks embracing streaming, with social media and more robust online and mobile shopping, means people will be spending even more time online in the coming years, especially as mobile network speeds improve further. Moreover, a growing global install base of connected devices (smartphones, tablets and the like) means even more people will be spending more time online.

We've already started to see a shift in where companies, especially mega-cap consumer product companies like **Nike (NKE), McDonald's (MCD), Proctor & Gamble (PG), Kellogg (K)** and the like, are spending their advertising budgets. Over the last few years, online and mobile have been taking a bite out of TV and Radio advertising, and we've all seen the creative destruction the Internet has had on print publishing, especially newspapers.

We see no slowdown in the shift in where advertising dollars are spent. In fact, a new report from eMarketer (see right) confirms the likelihood that digital advertising will continue to take advertising spending share from all other forms (TV, print radio and other) in the coming years. To us, this raises the following question – how will advertisers know where online, in what apps and elsewhere in the mobile and connected device landscape to reach their target market?

The answer to that question has us starting to dig into two companies – **Comscore (SCOR)** and **Nielsen NV**

Average Time Spent per Day with Major Media by US Adults, 2011-2017
hrs:mins

	2011	2012	2013	2014	2015	2016	2017
Digital	**3:34**	**4:10**	**4:48**	**5:09**	**5:29**	**5:45**	**5:56**
—Mobile (nonvoice)	**0:46**	**1:28**	**2:15**	**2:37**	**2:54**	**3:08**	**3:18**
——Radio	0:16	0:26	0:32	0:39	0:44	0:49	0:52
——Social networks	0:04	0:09	0:18	0:23	0:27	0:30	0:32
——Video	0:03	0:09	0:17	0:22	0:26	0:29	0:32
——Other	0:23	0:44	1:08	1:14	1:17	1:20	1:22
—Desktop/laptop*	**2:30**	**2:24**	**2:16**	**2:14**	**2:12**	**2:11**	**2:10**
——Video	0:12	0:20	0:22	0:23	0:24	0:25	0:25
——Social networks	0:21	0:22	0:17	0:16	0:15	0:14	0:13
——Radio	0:12	0:07	0:06	0:06	0:06	0:06	0:06
——Other	1:45	1:35	1:31	1:28	1:27	1:26	1:25
—Other connected devices	**0:18**	**0:18**	**0:17**	**0:19**	**0:23**	**0:26**	**0:28**
TV**	**4:34**	**4:38**	**4:31**	**4:22**	**4:11**	**4:03**	**3:58**
Radio**	**1:34**	**1:32**	**1:30**	**1:28**	**1:27**	**1:25**	**1:24**
Print**	**0:46**	**0:40**	**0:35**	**0:32**	**0:30**	**0:28**	**0:27**
—Newspapers	0:28	0:24	0:20	0:18	0:17	0:16	0:15
—Magazines	0:19	0:17	0:15	0:13	0:13	0:12	0:11
Other**	**0:39**	**0:38**	**0:31**	**0:26**	**0:24**	**0:22**	**0:21**
Total	**11:08**	**11:39**	**11:55**	**11:57**	**12:00**	**12:04**	**12:05**

*Note: ages 18+; time spent with each medium includes all time spent with that medium, regardless of multitasking; for example, 1 hour of multitasking on desktop/laptop while watching TV is counted as 1 hour for TV and 1 hour for desktop/laptop; *includes all internet activities on desktop and laptop computers; **excludes digital*
Source: eMarketer, Oct 2015

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US Total Media Ad Spending Share, by Media, 2014-2020
% of total

	2014	2015	2016	2017	2018	2019	2020
TV	**39.1%**	**37.7%**	**36.8%**	**35.8%**	**34.8%**	**33.7%**	**32.9%**
Digital	**28.3%**	**32.6%**	**35.8%**	**38.4%**	**40.8%**	**43.1%**	**44.9%**
—Mobile	10.9%	17.3%	22.7%	26.2%	28.8%	31.0%	32.9%
Print	**17.4%**	**15.4%**	**13.9%**	**12.9%**	**12.2%**	**11.6%**	**11.1%**
—Newspapers*	9.1%	8.0%	7.2%	6.6%	6.1%	5.7%	5.5%
—Magazines*	8.3%	7.4%	6.8%	6.4%	6.1%	5.8%	5.6%
Radio**	**8.4%**	**7.8%**	**7.4%**	**7.0%**	**6.7%**	**6.4%**	**6.1%**
Out-of-home	**4.0%**	**4.0%**	**3.9%**	**3.8%**	**3.7%**	**3.5%**	**3.4%**
Directories*	**2.8%**	**2.5%**	**2.2%**	**2.0%**	**1.9%**	**1.7%**	**1.6%**

*Note: *print only; **excludes off-air radio & digital*
Source: eMarketer, March 2016

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(NLSN). While the two businesses have their similarities, they also have significant differences and we are working our way toward understanding those as well as determining potential entry points from a stock perspective. As we do our homework, we'll place both on the **Tematica Contender List** under the ***Connected Society*** investing theme. We may act on one, none or both in the coming weeks, but only after share our findings.

Tematica Contenders

As we roll up our sleeves each week we add companies and discard others to our list of Tematica Select Contenders. These are companies that we're doing more work on and in some cases we're waiting for the risk to reward tradeoff to reach more appetizing levels.

AMZN	Amazon.com	*Connected Society*
CHGG	Chegg Inc.	*Tooling & Retooling*
CMG	Chipotle Mexican Grill	*Foods that Are Good for You*
SCOR	Comscore	*Connected Society*
GLW	Corning Inc.	*Disruptive Technologies*
IMMR	Immersion Corp.	*Disruptive Technologies*
KIM	Kimco Realty	*Rise & Fall of the Middle Class*
LOCK	Lifelock	*Safety & Security*
MKC	McCormick & Co.	*Cashstrapped Consumer / Middle Class*
MRK	Merk & Co.	*Aging of the Population*
NLSN	Nielson NV	*Connected Society*
PANW	Palo Alto Networks	*Safety & Security*
SYNA	Synaptics Inc.	*Disruptive Technologies*
SBUX	Starbucks Inc.	*Rise & Fall the Middle Class*
UNFI	United Natural Foods	*Foods with Integrity*
VZ	Verizon Communications	*Content is King / Connected Society*
XYL	Xylem, Inc	*Scare Resources*

Thematic Signals: Ripped from the Headlines

If you missed last week's ***Tematica Investing*** we introduced Thematic Signals, which highlights confirming data points and items to watch for our list of investing themes. Pretty much what you would call, Ripped from the Headlines. Here we go...

Aging of the Population

According to a new report from the Economic Policy Institute titled "The State of American Retirement: How 401Ks Have failed Most American Workers" that analyzed the Survey of Consumer Finances between 2000 and 2013, slightly less than one-half of prime working-age families (that's families headed up by someone between the ages of 32 and 61) have a grand total of bubkes in their retirement accounts.

Cashless Consumption

Amazon.com (AMZN) has filed a patent application for a payment system that lets you purchase goods with your smiling face. Amazon's rationale for moving in this direction seems to be based on all the flaws and hassles associated with more typical passwords.

Cash Strapped Consumer

The average price of branded prescription drugs in the U.S. has doubled in the past five years, a finding that threatens to fuel the political backlash against high prices... The rate of seriously delinquent subprime car loans soared above 5 percent in February, according to Fitch Ratings. That's worse than during the Great Recession and the highest level since 1996.

Connected Society

We are on the cusp of a totally connected world. The Internet of Things is no longer an emerging trend, it has arrived. If you want evidence — real evidence rather than the speculation of industry analysts — then take a look at:

- The $1.4 billion **Cisco (CSCO)** reputedly put on the table at the start of February to acquire IoT platform provider Jasper Technologies.
- Online sales grew nearly 50 percent year-over-year for beauty supply retailer **Ulta Salon & Cosmetics (ULTA)** in fiscal 2015.
- **Goldmand Sachs (GS)** is buying an online retirement-savings startup that is barely a year old, as the Wall Street bank adjusts to the growing influence of technology in finance
- Shopgate announced Friday (March 11) that it has added Apple TV apps to its catalog of shoppable portals, allowing any retailer to create its own path to purchase through Apple TV. The service, which debuted at SXSW Interactive on Saturday (March 12), highlights the omnicommerce functionality of selling on a large-screen format through partnerships with two NBA teams — Kevin Durant's Oklahoma City Thunder and Stephen Curry's league-leading Golden State Warriors.

Economic Acceleration/Deceleration

Chief executive officers of large American companies are not becoming more upbeat on the U.S. economy in 2016 than they were in the fourth quarter of 2015. The Business Roundtable CEO Economic Outlook Index rose slightly from 67.5 in the fourth quarter of 2015 to 69.4 this year. The long-term average for the index is 79.9... Mixed expectations for near-term sales, investment, hiring and growth point to an economy that continues to lack momentum. These results only reinforce the need for Congress and the Administration to act this year to enact policies that boost job creation and economic growth

New Demand, New Solutions

U.S. mayors rank energy efficient LED lighting as the most promising technology for city managers to reduce their energy use and carbon emissions over the coming two years, according to a survey held at the United States Conference of Mayors (USCM).

Safety & Security

A further complication to the story is that IoT devices and software needs to integrate with existing legacy infrastructure. Security runs the risk of becoming an afterthought in the great IoT land-grab.

Tooling and Re-Tooling

When the OECD tested half-a-million 15-year-old students around the world in a test known as PISA in 2012, US teens came in 27th place in math, below their counterparts in Estonia, Latvia, Vietnam, and Spain.

Companies Mentioned

Aeropostale (ARO)
Amazon.com (AMZN)
Anadarko Petroleum (APC)
Cisco Systems (CSCO)
Comscore (SCOR)
Costco Wholsale (COST)
Foot Locker (FL)
Goldman Sachs (GS)
Kellogg (K)
Macy's (M)
McDonald's (MCD)
Netflix (NFLX)
Nielsen NV (NLSN)
Nike (NKE)
Philip Morris International (PM)
Proctor & Gamble (PG)
Regal Cinema Group (RGC)
Ulta Salon & Cosmetics (ULTA)

Analyst Positions

At the time of publication, Mr. Versace, Chief Investment Officer of Tematica Research had no positions in the shares of companies mentioned in this issue.

Important Disclosures and Certifications

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