MONDAY MORNING KICKOFF

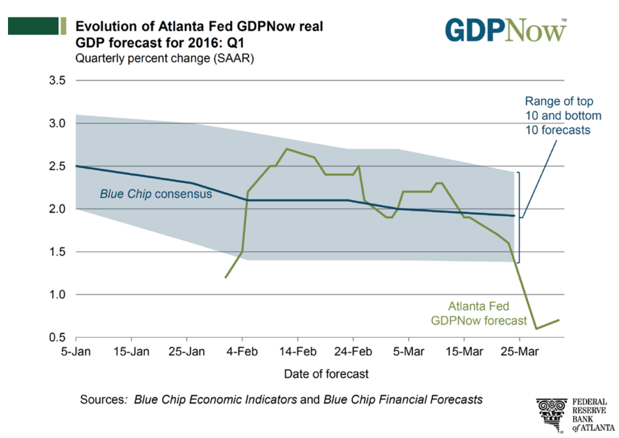
YOUR MARKET PRIMER FOR THE WEEK AHEAD

WEEK OF APRIL 4, 2016

With the close of the stock market last Thursday, we shut the books on not just the month of March, but the March quarter as well. While the quarter started off on a rocky note, it rebounded in the second half, aided by a 4.5% increase in the S&P 500 during March, which led the index to finish the March quarter up slightly less than 1%.

Quite the roller coaster ride to say the least, with the last push higher over the last few days coming as a result of comments from Fed Chairwoman Janet Yellen, who indicated a high probability the Fed would push the eventual boost in interest rates.

As we've discussed, however, the fast and furious rebound of the market since mid-February has come on the heels of economic data pointing to a slowing economy and that has led to a stretched market valuation. The latest forecast, out last week, by the Atlanta Fed's GDPNow forecasting model (see chart lower right) puts its March quarter GDP expectations at 0.7%, which is down dramatically from more than 2% a few weeks prior. Also, Friday's low quality March Employment Report didn't do much to alter the path of the economy during the March quarter – more on that in a few paragraphs.



Thematic Signals

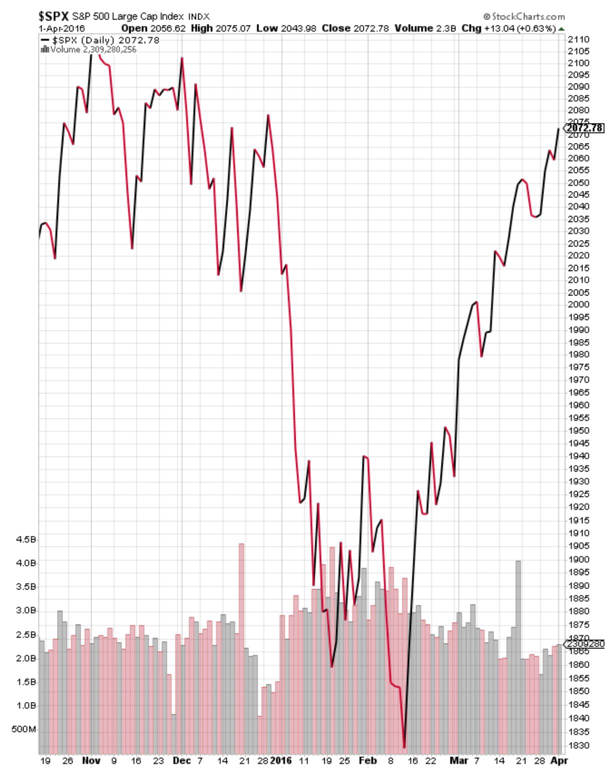
[Russian Oil Output Rises to Record as Production Freeze in Doubt (Scarce Resources)]

[Amazon Plans Big Push to Expand Prime Now Fast Delivery] *(Connecte Society)*

[Tesla's New Model 3 Jump-Starts Demand for Electric Cars] *(Replacement / Demand Technolog)*

[THE GLOBAL SMARTPHONE REPORT: The forces behind the global deceleration in smartphone sales] *(Rise & Fall of the Middle Class)*

[1 in 5 people will be obese by 2025, study says (Fattening of the Population)]



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.

So where does all of these leave the stock market?

As of Friday's market close, the S&P 500 was trading at 17.1x expected 2016 earnings of $120.43 per share, up all of 2.6 percent compared to 2015. On it's own, we realize that "17.1x" is just a number, which means context is needed to truly understand how stretched that valuation is.

When crunching the data (see chart right), we found the prior 5-year average forward 12-month P/E ratio to be 14.4x, and the prior 10-year average forward 12-month P/E ratio to be 14.2x, which means the current market multiple is indeed stretched. What hammers that home even more is the 5.5 percent earnings growth rate the S&P 500 has delivered over the last 5 years and 3.9 percent over the last 10 years compared to the 2.6 percent forecasted for 2016 (which includes steep Great Recession led earnings contractions over the 2007-2009 period).

Modest Growth & a Rich Valuation Make Could Make for a Bumpy End to 2015

S&P 500 - Price and Valuation Data, 2001-2017E

	Year End Closing Price		Earnings Per Share	P/E Ratio	EPS Growth
2001	$1,148.08		$46.08	24.9	
2002	$879.82	-23.4%	$48.80	18.0	5.9%
2003	$1,111.92	26.4%	$53.74	20.7	10.1%
2004	$1,211.92	9.0%	$67.08	18.1	24.8%
2005	$1,248.29	3.0%	$73.46	17.0	9.5%
2006	$1,418.30	13.6%	$83.20	17.0	13.3%
2007	$1,468.36	3.5%	$81.79	18.0	-1.7%
2008	$903.25	-38.5%	$71.43	12.6	-12.7%
2009	$1,115.10	23.5%	$59.34	18.8	-16.9%
2010	$1,257.64	12.8%	$83.10	15.1	40.0%
2011	$1,257.60	0.0%	$94.85	13.3	14.1%
2012	$1,426.19	13.4%	$102.47	13.9	8.0%
2013	$1,848.36	29.6%	$108.47	17.0	5.9%
2014	$2,058.90	11.4%	$116.77	17.6	7.7%
2015	$2,043.94	-0.7%	$117.36	17.4	0.5%
2016	$2,072.78 *		$120.43	17.2	2.6%
2017	$2,072.78		$136.68	15.2	13.5%
			2002-2015 Average	**16.7**	**7.8%**
			2002-2015 Max	**20.7**	
			2002-2015 Min	**12.6**	

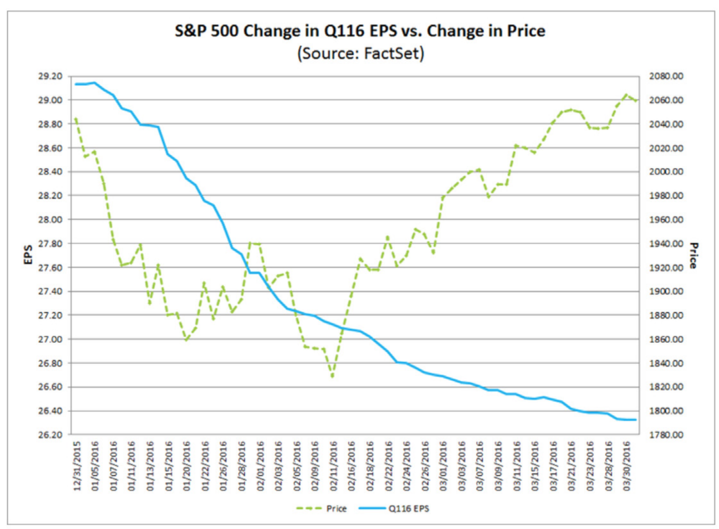
Source: FactSet and Capital IQ. Priced on November 6, 2015

What if...

2016 EPS Growth	S&P 500 EPS	Implied S&P 500 Value	Upside
2.5%	$120.29	$2,010	-2.4%
3.0%	$120.88	$2,020	-1.9%
3.5%	$121.47	$2,029	-1.4%
4.0%	$122.05	$2,039	-1.0%
4.5%	$122.64	$2,049	-0.5%
5.0%	$123.23	$2,059	0.0%
5.5%	$123.81	$2,069	0.5%
6.0%	$124.40	$2,078	0.9%
6.5%	$124.99	$2,088	1.4%
7.0%	$125.58	$2,098	1.9%

Source: FactSet and Capital IQ
* Dated market close April 1, 2016

What's concerning to us is the continued climb in the market when juxtaposed against not only the economic data, but the negative revisions in March quarter revenue and earnings expectations. Per data tabulated by FactSet, March quarter earnings expectations for the S&P 500 have been revised lower by 9.6%, from the initial $29.13 per share even before we entered 2016 to the current $26.32 per share.



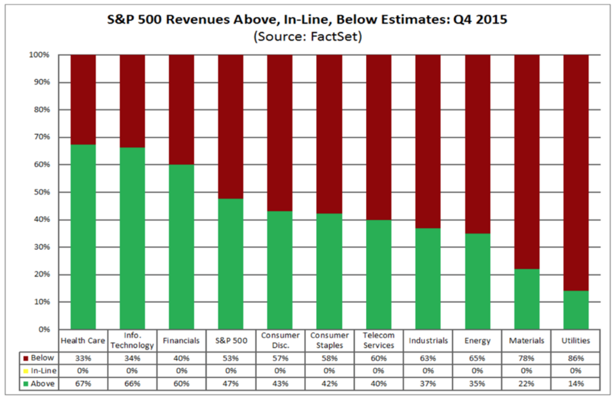
As FactSet points out, "the estimated year-over-year earnings decline for Q1 2016 is -8.5%, which is below the expected earnings growth rate of 0.8% at the start of the quarter (December 31). This percentage decline was larger than the trailing 5-year average (-4.0%) and trailing 10-year average (-5.3%) for a quarter. In fact, this was the largest percentage decline in the bottom-up EPS estimate during a quarter since Q1 2009 (-26.9%)."

It's not just earnings, but revenue associated with the S&P 500 group of companies is expected to fall for the fifth consecutive quarter with no rebound expected until the September quarter for both revenue and earnings.

As we've said before, this has us thinking second-half earnings expectations calling for a 14.7% increase versus the first half are rather aggressive, to put it mildly. For us this means listening to commentary about the back half of 2016 during the upcoming earnings season, which should begin before we know it.

Putting all of this together — the continued melt up in the stock market on the back of eroding fundamentals that has led to stretched valuations and overly aggressive earnings expectations for the back half of 2016 — in our view, the potential risk-to-reward to be had in the near term is far more to the risk side.

As such, in our thematically long-only products, **Tematica Investing**, we've shied away from adding growth-ier companies of late, in favor of higher dividend yielding companies, which should benefit from the Fed's rate hike push out and garner investor favor as expected market volatility returns. Of course, each of the companies on the Tematica Select List benefits from one of our 14 thematic tailwinds. Over in our trading service, **Tematica Pro**, we've added some hedging plays and put on some positions that will benefit from eroding fundamentals and prospects for even greater negative earnings revisions.

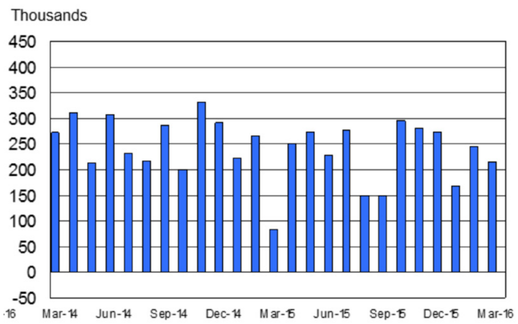


	Health Care	Info. Technology	Financials	S&P 500	Consumer Disc.	Consumer Staples	Telecom Services	Industrials	Energy	Materials	Utilities
Below	33%	34%	40%	53%	57%	58%	60%	63%	65%	78%	86%
In-Line	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
Above	67%	66%	60%	47%	43%	42%	40%	37%	35%	22%	14%

Turning to The Week Ahead

Turning our gaze to this week, it will be a light one in terms of economic data and corporate earnings. On the economic docket, we'll get Gallup's US Consumer Spending Measure as well as the Labor Market Conditions Index reports on Monday as well as February Factory Orders. We also get the March ISM Services Report and the minutes from the Fed's March meeting as well as the JOLTs report, which should help put more perspective around what we considered to be a rather low quality March Employment Report.

Chart 2. Nonfarm payroll employment over-the-month change, seasonally adjusted, March 2014 – March 2016



Not only were the number of jobs created in March below the 12-month average, but with demonstrative job growth in lower wage jobs, such as retail (+47,000), health care (+44,000), and leisure and hospitality (+40,000), making up 61% of the month's new jobs, it's easy to see why we haven't seen more robust wage inflation. For those not convinced, digging even further into the report, we find that one of the overall largest job creation categories was part-time work, which jumped 135,000 jobs in March, or more than half the number of overall jobs reported by the Labor Department. The bottom line is even though the Unemployment Rate ticked up to 5.0% in March, it is far from indicating the true nature of what's going on when it comes to jobs, hence our taking a look at it from several directions, which includes this week's JOLTS report.

Given the thin calendar, we expect ISM Services Index and the FOMC minutes will receive more attention than usual. In the ISM Services Report, we'll be looking to see if the service economy rebounded in March or if growth continued to slow as it did in February. As for the Federal Open Market Committee minutes, we've had several post-Fed meeting speeches and talks by various Fed heads, but even so the minutes may offer additional insight into what the Fed is group-thinking.

Rounding out the week, Fed Chairwoman Janet Yellen will be participating in a conversation with former Fed chairs Ben Bernanke, Alan Greenspan and Paul Volcker. While we don't expect fireworks, the passage of time as well as more data should make for an interesting conversation among the Fed heads. As with presidents of the past, perhaps Bernanke, Greenspan and Volcker will offer some guidance to Yellen, but we certainly don't expect her to abandon the "clear as mud" speak embraced by Fed Chairs.

Thematic Earnings on Our Radar

We consider this week to be the calm before the earnings storm that begins with **Alcoa's (AA)** March quarter earnings report on April 11, and we'll be using that time to get prepared for the coming onslaught of reports and company commentary. Even so there will be several earnings reports on tap that offer us a number of insights and confirming data points. For example, last week **Dave & Buster's Entertainment (PLAY)** CEO Steve King said something rather confirming about what we are calling the next round of

ECONOMIC CALENDAR, APRIL 4 - 8, 2016

DATE	REPORT / SPEECH	DATA
4-Apr	**Factory Orders**	Feb
5-Apr	**Trade Balance**	Feb
5-Apr	**ISM Services**	Mar
6-Apr	**MBA Mortgage Index**	2-Apr
6-Apr	**Crude Inventories**	2-Apr
6-Apr	**FOMC Minutes**	16-Mar
7-Apr	**Continuing Claims**	26-
7-Apr	**Initial Claims**	2-Apr
7-Apr	**Natural Gas Inventories**	2-Apr
7-Apr	**Consumer Credit**	Feb
8-Apr	**Wholesale Inventories**	Feb

EARNINGS CALENDAR, MAR. 28 - APR. 1, 2016

DATE	COMPANIES REPORTING
MONDAY	
TUESDAY	• Darden Restaurants Inc (DRI) • Greenbrier Companies (GBX)
WEDNESDAY	• Bed Bath & Beyond Inc. (BBBY) • Constellation Brands Inc (STZ) • Global Payments Inc (GPN) • Monsanto Co (MON)
THURSDAY	• Carmax Inc (KMX) • ConAgra Foods Inc (CAG) • Rite Aid Corp (RAD) • Ruby Tuesday Inc (RT) • WD-40 Co (WDFC)
FRIDAY	

creative destruction associated with our **Connected Society** investing theme that centers around mall stores.

We're working on a special report on the subject, and we think the implications to be had approach the creative destruction that's been had in the newspaper industry – more on this soon. Much like a puzzle, it's assembling these earnings, industry and other data nuggets that enables us to see things through our thematic perspective rather than be trapped with the rest of the investing herd.

Here are the reports in the coming days that have caught our thematic eye:

- ***Aging of the Population:*** Rite Aid Corp. (RAD), Walgreens Boots Alliance (WBA)
- ***Cashless Consumption***: Global Payments (GPN)
- ***Cash Strapped Consumer:*** Bed Bath & Beyond (BBBY), CarMax (KMX), PriceSmart (PSMT)
- ***Economic Acceleration/Deceleration:*** Apogee Enterprises (APOG), Greenbrier Companies (GBX), RPM International (RPM), WD-40 Company (WDFC)
- ***Fattening of the Consumer:*** ConAgra Foods (CAG), Darden Restaurants (DRI)
- ***Foods with Integrity:*** The Fresh Market (TFM)
- ***Guilty Pleasure:*** Constellation Brands (STZ)
- ***Rise & Fall of the Middle Class:*** Monsanto (MON), CarMax (KMX), PriceSmart (PSMT)

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Important Disclosures and Certifications

