

MONDAY MORNING KICKOFF

YOUR MARKET PRIMER FOR THE WEEK AHEAD

WEEK OF JULY 25, 2016


Despite Thursday breaking the 9-day winning streak for the domestic stock market, the S&P 500 closed up more than 0.5 percent last week, setting yet another record in the process and marking the fourth week of gains. As we've entered into June quarter earnings, the upward moves have continued albeit at more measured increments compared to those in June.

Last week, we introduced **The Thematic Index**, and if you missed that news you can [read far more about that here](#). Through the first three weeks of July, The Thematic Index returned 4.6 percent compared to 3.6 percent for the S&P 500 due to a number of our 17 investing themes, delivering better performance month to date. Not to pat ourselves on the back, but this adds to the outperformance achieved over the last several quarters and shows the power of our proprietary thematic investing framework.

Despite the continued ascent of all three major market indices, there is still much concern in the market. Telecom stocks and utilities continued to lead the way last week. Sitting in nicely air conditioned rooms rather than bake in the hottest summer since 1880, according to data from, National Oceanic and Atmospheric Administration (NOAA), we're reminded the move in utility stocks isn't just for dividends and safety.

Putting last week under the microscope

There were a number of non-earnings events last week, including the Republican National Convention (RNC), some upbeat housing data and receipt of the July Flash PMI reports. U.S. housing starts rose more than expected in June, rebounding from a downward-revised 1.7 percent drop in the May and climbing 4.8 percent in June — far better than the 0.2 percent month-on-month increase that was forecasted. Breaking down the data, we find the



Thematic Signals

[Yahoo reveals the secret to Content is King: it better actually be good content](#) *Content is King*

[Thematic driver behind Dollar Shave Club acquisition — not the one you would think](#)

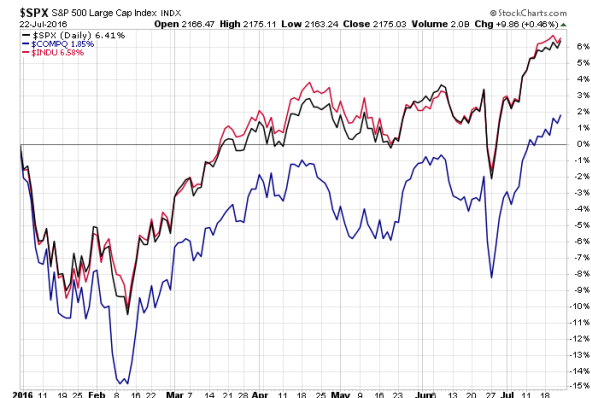
Content is King

[Under Armour brings wearables to the playing field](#) *Connected Society*

[Will a Camera on Every Cop Make Everyone Safer?](#)

Safety & Security

[Rise of Middle Class Key to well-being, not just financial well-being.](#) *Rise & Fall of the Middle Class*



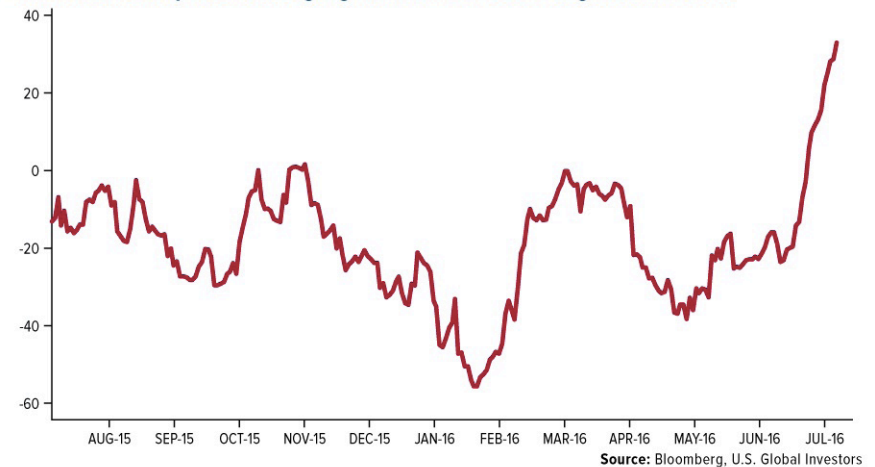
ABOUT THE MONDAY MORNING KICKOFF

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.

month over month increase was led by multi-family housing (up 5.4 percent), but single-family starts were still better than expected (up 4.4 percent). Building-permit activity also topped estimates, rising by 1.5 percent 1.153 million, marking the highest level since February. Warmer than seasonal weather helped has helped new home construction in recent months, while record low borrowing costs helped propel existing and new home sales as well in June.

The **July US Flash PMI** data from Markit Economics rose to 52.9, its highest level since November, with output growth hitting the best level in eight months, and manufacturing payrolls had the biggest gain in a year. Corroborating this improvement, the **Citi Economic Surprise Index** (see right), which measures how data released compares to expectations has been on the rise lately (when data is coming in weaker than expected the index declines, when it comes in stronger than expected, it rises). Taming those bullish signs, were comments made during last week's earnings conference calls, including:

Citi Economic Surprise Index Highlights Recent Bout of Strong Economic Data



“Relative to the macro environment, the steel-consuming sectors that were weak in 2015 such as energy, heavy equipment, and agriculture will likely remain so in 2016.”

— **Steel Dynamics (STLD) CEO Mark Millett**

“The largest corporate clients...continues to be a tough segment. I don’t think there’s many of the Fortune 500 who are going on calls like we’re having right now and talking about growing their T&E budgets.”

— **American Express (AXP) CEO Jeff Campbell**

While we are receiving improving signs on the domestic economy, not all sectors and indicators are recovering at the same vector and velocity. This suggests the speed of the economy in the back half of the year is not likely to reach breakout velocity and will likely continue at its contained pace, as it has over the last several years. As you have no doubt seen, this is an election year and a contentious one at that, which will more than likely weigh on business investment in the coming months.

On the post Brexit front

The **July Flash PMI data for the Eurozone** reflected as expected a plummet in the UK economy post Brexit (the UK’s PMI Composite Index dropped to 47.7 in July vs. 52.4 in June), with output and new orders both falling for the first time since the end of 2012. This could be the data the **Bank of England (BOE)** was waiting for before

joining the latest round in the monetary easing bandwagon. The move lower in the pound relative to the dollar last week seems to point to rising expectations for such a move from the BOE. That UK PMI reading came after the International Monetary Fund (IMF), citing slower growth in the US, UK and Japan, downgraded its forecast for global economic growth this year to 3.1 percent, which is down 0.1 percent and the same growth rate we saw in 2015. Parsing the revised IMF forecast, we find the IMF now expects the US economy to grow 2.2 percent this year, down from its 2.4 percent forecast in April and slower than last year's 2.4 percent. Although the fund kept its forecast for a pickup in 2017 at 2.5 percent.

We continue to get mixed signals with companies such as **Goldman Sachs (GS)**, **IBM (IBM)** and American Express signaling little Brexit related disruption. Offsetting those comments, the ZEW Indicator of Economic Sentiment for Germany plunged 26 points in July to -6.8. Professor Achim Wambach, the ZEW president, said "Uncertainty about the [Brexit] vote's consequences for the German economy is largely responsible for the substantial decline in economic sentiment... In particular, concerns about the export prospects and the stability of the European banking and financial system are likely to be a burden on the economic outlook."

Our view has been the market has quickly digested the Brexit news, but ask any lactose intolerant person that eats some full fat ice cream and they'll tell you it's only a matter of time before some indigestion kicks in. We see the same developing with the UK's expected separation from the EU in the coming months.

Turning to the Week Ahead

Last week we shared with subscribers that quarterly corporate reporting is very much like assembling a 500-piece jigsaw puzzle — it comes more into focus as more pieces are assembled. With 25 percent of the companies in the S&P 500 reporting earnings to date for 2Q 2016, 68 percent have reported earnings above the mean estimate and 57 percent have reported sales above the mean estimate. Factoring in those reports, the expected blended earnings decline for the S&P 500 companies is now -3.7 percent compared to -5.5 percent on June 30 — better but still another quarter of declining earnings. On the revenue side, the blended year-over-year sales decline for 2Q2016 now looks more like -0.3 percent, compared to the estimated sales decline of -0.8 percent at the end of the June quarter.

Q2 2016: EARNINGS SCORECARD

EXHIBIT 2A. S&P 500: Q2 2016 EARNINGS VS. EXPECTATIONS

Sector	Above %	Match %	Below %	Surprise Factor %	Reported Total #	Index Total #
Consumer Discretionary	57%	17%	26%	9%	23	83
Consumer Staples	75%	13%	13%	1%	8	36
Energy	60%	20%	20%	15%	5	37
Financials	69%	16%	16%	7%	32	92
Health Care	88%	13%	0%	4%	8	57
Industrials	74%	4%	22%	6%	23	68
Materials	50%	17%	33%	2%	6	27
Technology	74%	21%	5%	9%	19	67
Telecom Services	0%	100%	0%	0%	1	5
Utilities	-	-	-	-	0	28
S&P 500	68%	15%	17%	6%	125	500

Source: Thomson Reuters I/B/E/S

Upside earnings surprises reported by companies in the Information Technology, Industrials, and Financials sectors were mainly responsible for the decrease in the overall earnings decline for the index during the past week.

Before we get all giddy about the aggregate impact of last week's quarterly reports, let's remember that there are more than 1,100 companies reporting earnings this week, including 2013 S&P 500 companies and 12 components of the Dow Jones Industrial Average. Among those companies are a number of heavy weights and well held companies like **Alphabet (GOOGL)**, **MasterCard (MA)**, **United Parcel Service (UPS)** and alongside **Amazon (AMZN)**, **Apple (AAPL)**, and **Facebook (FB)**. As these 1,100 companies report quarterly results, the picture of June-quarter earnings and the level of quality vs. financial shenanigans (such as buybacks, tax rates and one-time gains) should come into far greater focus.

Aside from the barrage of earning reports, we have the Democratic National Convention and of course the economic calendar as well. On that calendar we have June reports for Consumer Confidence and Durable Orders as well as a number of July regional Fed manufacturing reports Dallas, Richmond, Kansas City and Chicago. Following the continued month over month rebound in the Flash July US Manufacturing PMI report, we'll look for corroborating signals in those regional Fed reports. This week also brings the first cut at 2Q 2016 GDP and the July Fed rate decision. We continue to see the Fed standing pat until later in 2016 at the soonest when it comes to an interest rate hike.

As the market has continued to creep higher, we've noticed the Chicago Board Options Exchange (CBOE) Volatility Index (VIX), which shows the market's expectation of 30-day volatility, has continued to move lower. Late July-early August, however, tends to be a time of year when we see seasonal weakness in the S&P 500. As all those earnings reports come in, Wall Street recomputes earnings expectations and then promptly heads to the beach as the velocity of those reports dies down.

One seasonal study from Moore Research Center shows the market historically turns "decisively bearish" in these last couple of weeks of July, with little reprieve until the first few weeks of August have passed. We'd note the seasonally low trading volume during this time tends to exacerbate stock price swings, much like it does in late December. Per Moore Research, this pattern has repeated itself in 12 of the previous 15 years. Given the continued new highs and stretched valuation — 18.3x expected 2016 earnings for the S&P 500 — mixed with lingering uncertainties, we suspect we are likely to see that pattern hold yet again. We'll continue to be focused on identifying both thematic contenders as well as active positions for the Tematica Select List.

ECONOMIC CALENDAR, JULY 25 - 29, 2016		
DATE	REPORT / SPEECH	DATA
26-Jul	Case-Shiller 20-city Index	May
26-Jul	Consumer Confidence	Jul
26-Jul	New Home Sales	Jun
27-Jul	MBA Mortgage Index	23-Jul
27-Jul	Durable Orders	Jun
27-Jul	Durable Orders, ex-	Jun
27-Jul	Pending Home Sales	Jun
27-Jul	Crude Inventories	23-Jul
27-Jul	FOMC Rate Decision	Jul
28-Jul	Initial Claims	23-Jul
28-Jul	Continuing Claims	16-Jul
28-Jul	International Trade in Goods	June
28-Jul	Natural Gas Inventories	23-Jul
29-Jul	GDP-Adv.	Q2
29-Jul	Chain Deflator-Adv.	Q2
29-Jul	Employment Cost Index	Q2
29-Jul	Chicago PMI	Jul
29-Jul	Michigan Sentiment - Final	Jul

EARNINGS ANNOUNCEMENTS THIS WEEK

AGING POPULATION

- Anthem Inc (ANTM)
- Baxter International Inc (BAX)
- CryoLife Inc (CRY)
- Gilead Sciences Inc (GILD)
- HealthStream Inc (HSTM)

AFFORDABLE LUXURIES

- Callaway Golf Co (ELY)
- Harley-Davidson Inc (HOG)
- Luxottica Group SpA (LUX)
- LVMH Moët Hennessy Louis Vuitton (MC)
- L'Oreal SA (OR.PA)
- Ruth's Hospitality Group Inc (RUTH)

ASSET-LITE

- Alphabet Inc (GOOGL)
- Booz Allen Hamilton Holding Corp (BAH)
- Dolby Laboratories Inc (DLB)
- Marriott International Inc (MAR)
- MicroStrategy Inc (MSTR)
- Navigant Consulting Inc (NCI)
- Neustar Inc (NSR)
- Safeguard Scientifics Inc (SFE)

ECONOMIC ACCELERATION / DECELERATION

- 3M Co (MMM)
- Caterpillar Inc (CAT)
- Dow Chemical Co (DOW)
- DuPont Fabros Technology Inc (DFT)
- E I du Pont de Nemours and Co (DD)
- General Dynamics Corp (GD)
- Heartland Express Inc (HTLD)
- Knight Transportation Inc (KNX)
- Norfolk Southern Corp (NSC)
- PACCAR Inc (PCAR)
- Roadrunner Transportation Systems Inc (RRTS)
- United Technologies Corp (UTX)

CASHLESS CONSUMER

- Check Point Software Technologies Ltd (CHKP)
- MasterCard Inc (MA)

CASH STRAPPED CONSUMER

- AvalonBay Communities Inc (AVB)
- Lumber Liquidators Holdings Inc (LL)
- Tanger Factory Outlet Centers Inc (SKT)

CONNECTED SOCIETY

- Akamai Technologies Inc (AKAM)
- Amazon.com Inc (AMZN)
- Apple Inc (AAPL)
- Citrix Systems Inc (CTXS)
- Facebook Inc (FB)
- NETGEAR Inc (NTGR)
- Overstock.com Inc (OSTK)
- Shutterfly Inc (SFLY)
- Texas Instruments Inc (TXN)
- Twitter Inc (TWTR)
- United Parcel Service Inc (UPS)
- Sprint Corp (S)

CONTENT IS KING

- Carmike Cinemas Inc (CKEC)
- Comcast Corp (CMCSA)
- GoPro Inc (GPRO)
- IAC/InterActivecorp (IAC)
- Live Nation Entertainment Inc (LYV)
- Meredith Corp (MDP)
- Nielsen Holdings PLC (NLSN)
- Outerwall Inc (OUTR)
- Regal Entertainment Group (RGC)
- Verizon Communications Inc (VZ)
- World Wrestling Entertainment Inc (WWE)

DISRUPTIVE TECHNOLOGIES

- iRobot Corp (IRBT)
- SolarCity Corp (SCTY)

FATTENING OF POPULATION

- BJ's Restaurants Inc (BJRI)
- Bloomin' Brands Inc (BLMN)
- Buffalo Wild Wings Inc (BWLD)
- Cheesecake Factory Inc (CAKE)
- Coca-Cola Co (KO)
- Domino's Pizza Group PLC (DOM)
- J & J Snack Foods Corp (JJSF)
- McDonald's Corp (MCD)
- Mindbody Inc (MB)
- Mondelez International Inc (MDLZ)
- Nutrisystem Inc (NTRI)
- Panera Bread Co (PNRA)

FOODS WITH INTEGRITY

- Danone SA (BN)
- Where Food Comes From Inc (WFCF)
- Whole Foods Market Inc (WFM)

FOUNTAIN OF YOUTH

- GNC Holdings Inc (GNC)
- Revlon Inc (REV)

GUILTY PLEASURES

- Altria Group Inc (MO)
- Golden Entertainment Inc (GDEN)
- Hershey Co (HSY)
- Las Vegas Sands Corp (LVS)
- Match Group Inc (MTCH)
- Wynn Resorts Ltd (WYNN)

RISE & FALL OF MIDDLE CLASS

- Airbus Group SE (AIR)
- Boeing Co (BA)
- JetBlue Airways Corp (JBLU)
- Under Armour Inc (UA)
- Petmed Express Inc (PETS)
- Colgate-Palmolive Co (CL)
- Expedia Inc (EXPE)

SCARCE RESOURCES

- Exxon Mobil Corp (XOM)

SAFETY & SECURITY

- Equifax Inc (EFX)
- TASER International Inc (TASR)
- Verisign Inc (VRSN)

TOOLING & RETOOLING

- American Campus Communities Inc (ACC)
- Capella Education Co (CPLA)
- ExamWorks Group Inc (EXAM)
- Monster Worldwide Inc (MWW)
- Robert Half International Inc (RHI)
- Strayer Education Inc (STRA)

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