

2Q16 Earnings Preview

Tailwinds in place add \$21-\$26 EPS next 12 months. 27 stocks.

Earnings are the dog wagging the dog.

S&P 500 earnings have been flat for the last 12 quarters (\$28-\$30 per share), ultimately explaining why equities have been flattish for the past two years. And until earnings begin to grow, the case for owning stocks loses its fundamental support. The headwinds have been in place for some time: (i) steep decline in oil; (ii) 27% surge in USD (hurting exporters); (iii) global manufacturing recession and (iv) generally tight credit conditions. In our view, 2Q16 very likely marks the turning point—1Q16 was the nadir (on EPS) and tailwinds are now in place to drive a reinvigoration of profit growth. 1Q16 earnings season was probably the worst result in a decade, yet stocks managed to gain 9% (2/16-5/15). ***In all likelihood, stocks are going to perform very well during the next month or so, as 2Q16 results show demonstrable improvements in top-line growth. The improvement in 2Q16 results is pretty evident already—positive pre-announcements is highest ratio in 5 years (slide 4).***

- **Four tailwinds are in place, which could add \$21-\$26 in S&P 500 EPS over the next 12 months (slide 3).** As shown, 4 factors are in place that could meaningfully boost EPS: (i) ISM Exports >50 4 months now, averaging 4.2pts higher than 2015; (ii) oil has rebounded sharply from \$26; (iii) corporate bond yields have fallen another 60bp recently; (iv) USD is now posting y/y declines.
- **First, the 4.2 gain in US ISM exports translates to 880bp of EPS growth (slide 6), or \$9.00.** We have talked for sometime about the powerful leading nature of the exports component of ISM manu. and its remarkable correlation to S&P 500 sales and EPS. The recent move to 53.5 (3M avg 52.8) is 4.2 pts above its 2015 avg and implies 800bp acceleration of EPS. In fact, the decisive upturn in EPS pre-announcements have a surprising correlation to the ISM exports (slide 7).
- **Second, Energy EPS still does not reflect recovery in oil forwards and normalization of margins, \$8.00-\$11.00 per S&P 500 share (slide 11 and slide 12).** Oil forwards have risen \$5 since the start of 2015 and historically, this implies a \$25b net income increase for the integrated (\$2.60 per S&P 500 share) (slide 11)—yet Energy EPS estimates are unchanged since Feb 2016, when oil forwards troughed. Additionally, integrated and E&P margins suffer from timing issues and now at lowest levels in 16 years—a normalization of margins in next 12 months to median would add \$70B in EBIT, or \$5-\$8 per S&P 500 share (depending on taxes).
- **Third, interest costs are still falling—investment grade yields are 60bp lower versus a year ago, adding \$3.00 in EPS (slide 13).** The global search carry is pushing US investment grade yields even lower (3.42% HG, 4.7% Baa) and each 10bp of rate is \$0.53 accretion to S&P 500 EPS, or \$3.00 in total (\$879 debt per share, 40% tax rate).
- **Fourth, USD is down y/y beginning in 2Q16 (-1%-2% into YE, slide 14) adds \$1.00-\$3.00 in EPS.** We estimate that each 100bp change in USD is \$0.50-\$1.00 in EPS (using data from FIREapps.com) and therefore, the 1%-2% decline could add \$1.00-3.00 to EPS.
- **What could go wrong? If Brexit proves to be a confidence killer.** The biggest risk to our view is the Brexit negative shock. A UK recession has heightened probabilities as many high-frequency indicators show some negative impact from Brexit. But this does not mean a broader global weakening is underfoot.

BOTTOM LINE: 12 industries have positive sales and EPS revisions for 2Q16. There are 12 industries which saw positive estimate revisions for both sales and EPS into 2Q16. We think some of the best tactical trades over next month will be seen in these groups. These are **Distributors, Electrical Equipment, Life Sciences Tools, Internet Software & Services, Diversified Consumer Services, Oil Gas & Consumable Fuels, Metals & Mining, Hotels Restaurants & Leisure, Pharmaceuticals, Construction Materials, Automobiles, and Building Products.** We identified stocks within these, and highlighted 27 stock ideas: the tickers are **F, FBHS, ALLE, MLM, LKQ, HRB, ETN, EMR, MCD, HOT, WYNN, FB, VRSN, WAT, PKI, TMO, AA, NEM, NUE, FCX, SWN, MUR, MRO, APA, BMY, PFE, and ZTS.**

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Performance	1Q16	2Q16	3Q16	YTD
S&P 500	0.8%	1.9%	-0.0%	2.6%
Cycl (Mat,IT,Disc,Ind)	0.8%	-1.9%	-0.4%	-1.5%
Near Cycl (Ener,Fin)	-2.5%	4.7%	-1.7%	0.3%
Def (Stpl,HC,Tel,Utl)	1.3%	4.1%	1.8%	7.4%
Value	1.5%	3.3%	-0.5%	4.3%
Growth	0.1%	0.6%	0.5%	1.2%

Valuation	2016E	2017E	Target
S&P 500 price	2098	→	2325
Fundstrat EPS Est	\$127	\$142	—
P/E (Y+1)	16.5x	14.8x →	16.4x
Div Yield	2.2%	2.3%	—

Sector Ratings

Cyclicals		Near Cyclicals		Defensives	
Technology	OW	Financials	OW	Telecom	OW
Industrials	OW	Energy	OW	Healthcare	N
Materials	OW			Staples	UW
Discretionary	N			Utilities	UW

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27 Ideas (see [slide 21](#) for rationale)

Figure: 27 companies seeing positive EPS estimate revisions for 2Q16

Priced as of 7/7/2016

	Ticker	Name	Current price	Market cap (\$M)	Daily liquidity (3-MAVG)	YTD relative return	Short interest		2Q16 estimate revisions		Upcoming earnings report date	P/E ('16E)	EV / EBITDA
							Short interest % of float	Short interest Z-Score	Sales	EPS			
Automobiles	1 F	Ford Motor Co	\$12.75	\$50,654	\$421	-10.2%	3.9%	-0.40	-1.5%	7.4%	7/28/2016	6.4x	2.6x
Building Products	2 FBHS	Fortune Brands Home & Secu	\$58.78	\$9,015	\$94	3.3%	5.6%	0.34	0.4%	1.9%	7/27/2016	22.0x	13.0x
	3 ALLE	Allegion Plc	\$68.64	\$6,571	\$42	1.5%	2.0%	0.16	1.3%	1.8%	7/28/2016	19.8x	14.8x
Construction Materials	4 MLM	Martin Marietta Materials	\$195.35	\$12,410	\$142	40.4%	5.7%	-1.00	1.7%	4.3%	8/2/2016	25.4x	13.3x
Distributors	5 LKQ	Lkq Corp	\$31.97	\$9,805	\$98	5.3%	2.7%	-0.66	13.3%	3.1%	7/28/2016	16.8x	10.9x
Diversified Consumer Services	6 HRB	H&R Block Inc	\$23.50	\$5,182	\$99	-32.1%	10.9%	0.62	1.8%	3.9%	9/1/2016	12.8x	6.7x
Electrical Equipment	7 ETN	Eaton Corp Plc	\$60.11	\$27,530	\$143	12.9%	1.4%	-0.33	0.8%	0.0%	7/27/2016	13.8x	n/m
	8 EMR	Emerson Electric Co	\$52.37	\$33,692	\$190	6.9%	2.7%	0.51	1.3%	0.6%	8/2/2016	16.7x	9.6x
Hotels Restaurants & Leisure	9 MCD	Mcdonald'S Corp	\$120.92	\$106,151	\$677	-0.3%	2.3%	0.50	1.7%	1.7%	7/26/2016	21.2x	13.4x
	10 HOT	Starwood Hotels & Resorts	\$75.54	\$12,807	\$224	15.2%	3.5%	-0.27	4.3%	1.9%	7/27/2016	25.5x	12.6x
	11 WYNN	Wynn Resorts Ltd	\$88.96	\$9,055	\$282	25.9%	13.7%	0.18	0.2%	13.0%	7/27/2016	26.3x	13.4x
Internet Software & Services	12 FB	Facebook Inc-A	\$115.85	\$331,366	\$2,880	8.1%	1.1%	-1.84	1.6%	12.1%	7/27/2016	30.6x	18.3x
	13 VRSN	Verisign Inc	\$83.40	\$9,047	\$64	-7.2%	19.6%	0.53	0.8%	0.5%	7/28/2016	23.6x	n/m
Life Sciences Tools & Services	14 WAT	Waters Corp	\$142.47	\$11,532	\$65	3.2%	3.7%	0.22	2.1%	1.2%	7/26/2016	22.0x	14.8x
	15 PKI	Perkinelmer Inc	\$52.59	\$5,734	\$35	-4.5%	2.7%	0.23	0.1%	1.8%	7/28/2016	18.3x	14.2x
	16 TMO	Thermo Fisher Scientific Inc	\$149.06	\$58,657	\$210	2.4%	1.2%	-0.83	2.4%	1.8%	7/28/2016	17.9x	16.1x
Metals & Mining	17 AA	Alcoa Inc	\$9.34	\$12,283	\$235	-8.0%	9.5%	0.46	-0.5%	13.8%	7/11/2016	22.6x	8.4x
	18 NEM	Newmont Mining Corp	\$40.96	\$21,731	\$306	125.0%	1.9%	-0.58	1.2%	36.2%	7/20/2016	27.6x	9.2x
	19 NUE	Nucor Corp	\$51.51	\$16,377	\$132	25.2%	2.7%	-0.38	11.2%	45.1%	7/21/2016	17.6x	7.2x
	20 FCX	Freeport-Mcmoran Inc	\$10.67	\$13,360	\$493	55.0%	11.5%	0.52	-4.5%	86.8%	7/26/2016	11.1x	5.9x
Oil, Gas & Consumable Fuels	21 SWN	Southwestern Energy Co	\$12.33	\$6,062	\$217	70.8%	19.6%	0.73	-4.0%	33.0%	7/21/2016	n/m	17.2x
	22 MUR	Murphy Oil Corp	\$30.00	\$5,166	\$123	31.0%	12.1%	0.71	4.9%	36.7%	7/27/2016	n/m	7.1x
	23 MRO	Marathon Oil Corp	\$14.74	\$12,494	\$291	14.4%	4.3%	0.62	-1.5%	26.7%	8/3/2016	n/m	10.6x
	24 APA	Apache Corp	\$54.90	\$20,781	\$209	20.8%	4.2%	0.52	6.2%	43.5%	8/4/2016	n/m	10.4x
Pharmaceuticals	25 BMJ	Bristol-Myers Squibb Co	\$74.08	\$123,662	\$420	5.1%	1.0%	-0.45	4.1%	5.7%	7/28/2016	28.2x	n/m
	26 PFE	Pfizer Inc	\$35.77	\$216,940	\$1,013	8.2%	0.9%	-0.10	0.9%	3.9%	8/2/2016	14.8x	n/m
	27 ZTS	Zoetis Inc	\$47.69	\$23,664	\$166	-3.1%	1.1%	-0.18	0.8%	2.1%	8/3/2016	24.5x	n/m
Median				\$12,807	\$209	6.9%	3.5%	0.18	1.3%	3.9%		21.2x	11.8x
% of stocks positive									88%	100%			

Source: Fundstrat, FactSet, Bloomberg.

#1: Factors supporting 2H16 EPS to beat “consensus”

As discussed in the following pages, we see four factors that support higher EPS over the next 12 months. These are in addition to traditional GDP growth as a driver.

- In aggregate, we see these tailwinds representing \$21-\$26 in EPS gains compared to current EPS run-rate.

Figure: 4 factors supporting higher EPS over next 12 months

Fundstrat estimates

Driver		EPS Impact		Description
1	ISM Exports > 50	US ISM exports now avg 52.8 vs 48.6 in 2015.	+\$9.00 +1 point = 2.2% EPS growth	The 4.2 point improvement implies S&P 500 EPS accelerates 800bp. The ISM improving due to weaker USD, abatement of oil shock and general easing of financial conditions. This is pre-BREXIT.
2	2016 oil forwards \$5 higher	Energy EPS not yet reflecting higher Oil	+\$8-\$11 \$5 delta oil = \$2.60 EPS EBIT margin = \$5 -\$8	The Energy sector is going to be a major contributor to S&P 500 EPS growth over next 12 months. Between improved oil prices (\$2.60 per S&P 500 share) and margin normalization (\$5-\$8), the aggregate impact could be \$8-\$11 per S&P 500 share.
3	Corp bond yields falling	Investment grade yields down 60bp	+\$3.00 Each 10bp is \$0.53 in EPS — S&P 500 debt/share is \$879.	Each 10bp drop in debt costs is \$0.53 in incremental EPS (40% tax rate). With falling interest rates and room for US yields to decline, this is a tailwind for US corporates.
4	USD is down y/y	USD faces easier y/y comparisons	+\$1-\$3 Each 100bp change in USD is \$0.50-\$1.00	USD is facing easier comparisons y/y and beginning in 2Q16 is down y/y.
Aggregate Tailwinds		\$21-\$26 tailwinds		

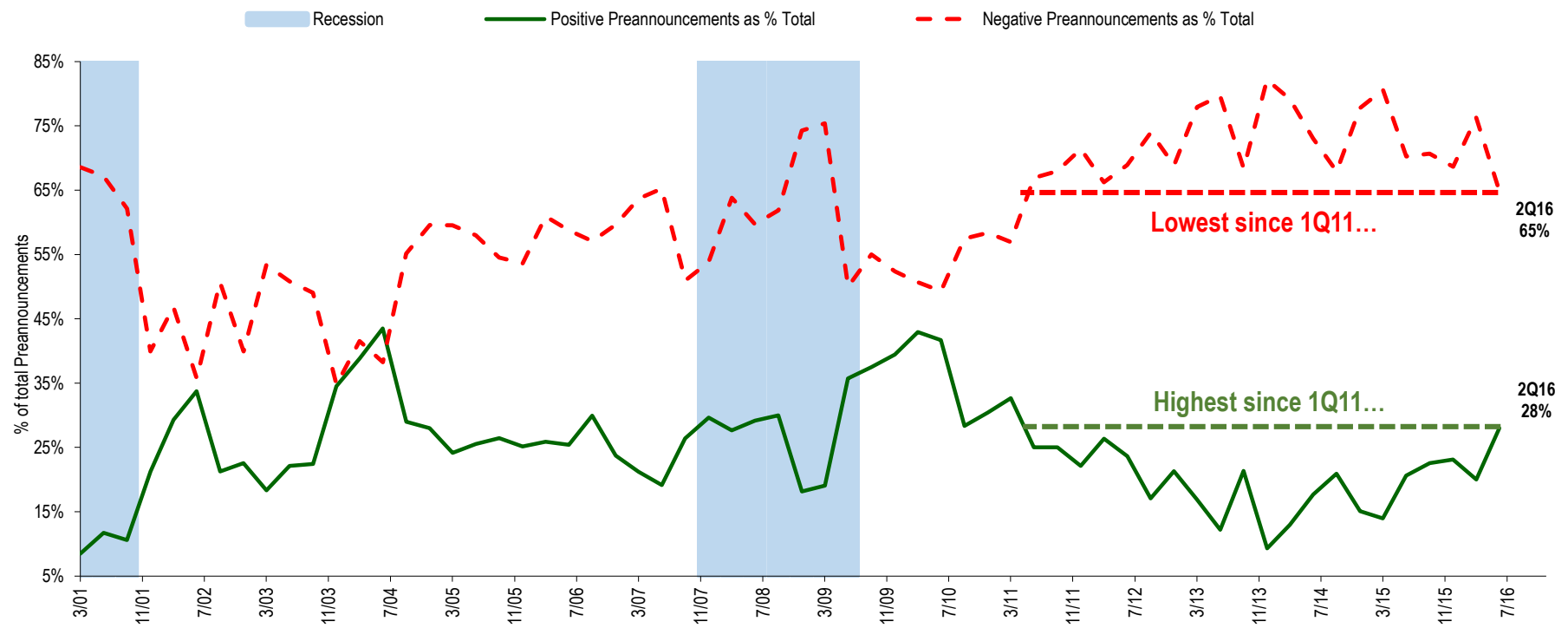
Source: Fundstrat, FactSet, Bloomberg.

#2: Positive EPS pre-announcements are highest since 1Q11

As the chart below makes pretty clear, earnings pre-announcements have been trending higher and as shown below, 28% of pre-announcements have been positive – this is the highest level since 1Q11.

- In general, pre-announcements skew negatively and only in the earliest stages of an EPS recovery (2001, 2004 and 2010) were they even approaching 50%.
- But the obvious trend highlighted below is that earnings pre-announcement trends have been improving.

Figure: Positive pre-announcements highest level in 5 years... never really high, but definitely improving



Source: Fundstrat, Thomson Reuters.

#2a: Seeing a pick-up in positive revenue guidance...

We have highlighted some of the recent guidance updates (which are mostly similar but not exactly the same as a pre-announcement).

- As shown below, of the 7 revenue updates, 6 were for higher sales.
- These include companies like **CRM**, **LULU**, **NWL** and even **UTX**. In other words, we think 2Q16 results will highlight an improvement in global growth prospects.

Figure: 86% of Sales guidance revisions and 64% of EPS guidance revisions were positive

Ticker	Sector	Guidance update date	Guidance changes for the current unreported fiscal year				
			Revenue	EPS	Operating cash flow	Free cash flow	Capex
STZ	Staples	6/30/2016			+10.3%		
TSCO	Discretionary	6/29/2016	-1.4%	-1.9%			-4.0%
MCK	Healthcare	6/29/2016		+1.0%			
CRM	Technology	6/28/2016	+1.3%	-6.9%			
RHT	Technology	6/22/2016		-1.3%			
LULU	Discretionary	6/8/2016	+0.6%	+1.4%			
EAT	Discretionary	6/8/2016				+13.7%	
MIK	Discretionary	6/7/2016		+0.5%			
NWL	Discretionary	4/29/2016	+0.5%	+25.3%			
NUS	Staples	4/28/2016	+2.3%	-4.4%			
ZBH	Healthcare	4/28/2016	+0.5%	+0.6%			
RTN	Industrials	4/28/2016		+1.9%			
UTX	Industrials	4/27/2016	+1.2%				
FDX	Industrials	3/16/2016		+1.4%			+4.3%
# cos revising guidance			7	11	1	1	2
Average guidance chg			+0.7%	+1.6%	+10.3%	+13.7%	+0.2%
% positive			86%	64%	100%	100%	50%

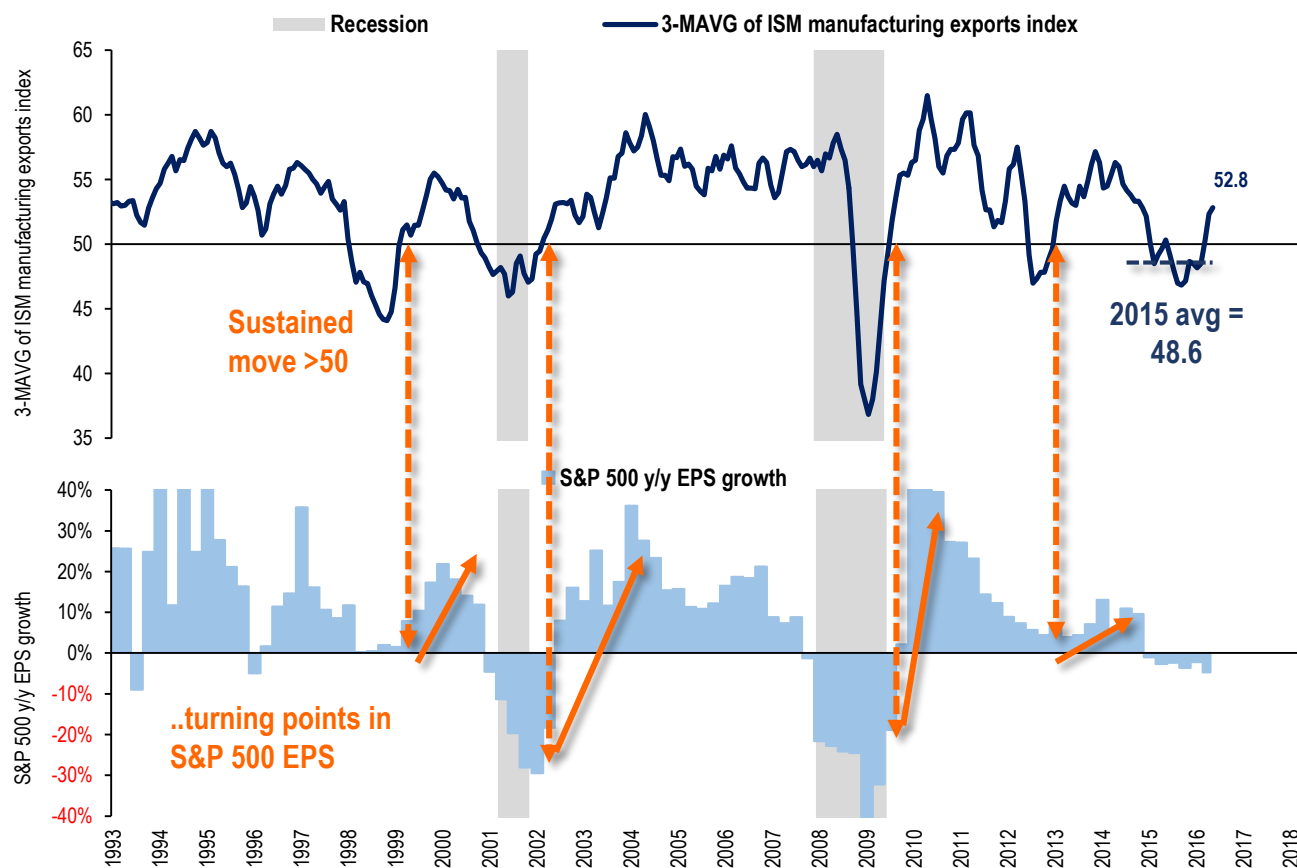
Source: Fundstrat, Bloomberg.

#3: US ISM Exports 4 points > 2015, implies 800bp EPS acceleration

The June ISM Exports posted a 53.5, an improvement over the last few months and boosting the 3-month moving average to 52.8. This is now 4 months above 50 after spending most of 2015 below 50.

- As shown on bottom right table, each 1 point increase in ISM Exports adds 2.2% to S&P 500 EPS growth. The recent ISM reading of 52.8 is 4.2 points above the 2015 average (see below). As shown below, history suggests S&P 500 EPS growth should rise by 800bp relative to 2015 growth rates.
- We believe this recovery reflects abating of oil shock, weakening USD and generally improving conditions.

Figure: 3-MAVG of ISM manufacturing exports index and S&P 500 y/y EPS growth
Since 1993



Date	ISM exports index	3-MAVG of ISM exports	S&P 500 1Y fwd Sales	S&P 500 1Y fwd EPS growth (y/y)
3/31/1999	50.1	51.1	12.8%	18.1%
3/31/2002	50.6	50.5	1.2%	25.2%
8/31/2009	55.5	51.8	3.9%	39.6%
2/28/2013	53.5	51.8	2.3%	13.1%
Average	52.4	51.3	5.0%	24.0%
Median	52.1	51.5	3.1%	21.6%
% of times positive			100%	100%
Current				
6/30/2016	53.5	52.8	n/a	n/a

Regression: $Y = -1\% + 0.021 * X$
 X = ISM exports 3M avg
 Y = S&P 500 EPS growth

Since 1990, each 1-point increase in ISM exports adds 2.20% to EPS growth.

In other words, the rise in ISM exports implies EPS growth rates accelerated 800bp or so in next 12 months

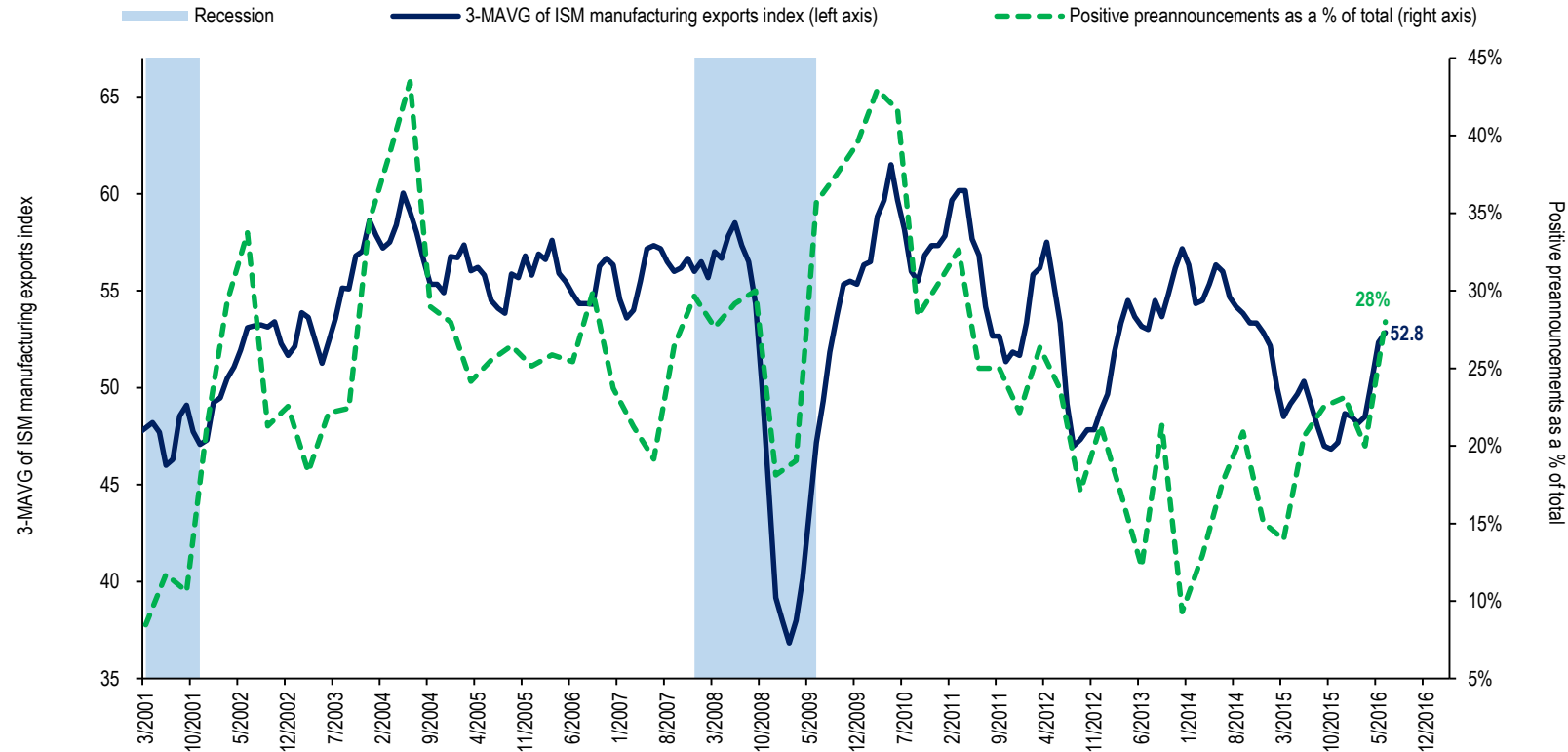
Source: Fundstrat, Bloomberg, ISM.

#3a: ISM Exports explain positive EPS pre-announcements...

Interestingly, ISM exports 3M moving average has done a pretty good job over the last 15 years of explaining earnings pre-announcements.

- As shown below, as ISM moves above 50, EPS trends tend to turn positive.
- In other words, this is simply corroborating that the upturn in ISM exports is a harbinger to better EPS results in coming quarters.

Figure: Positive EPS pre-announcements are correlated with ISM Exports...



Source: Fundstrat, Bloomberg, Thomson Reuters.

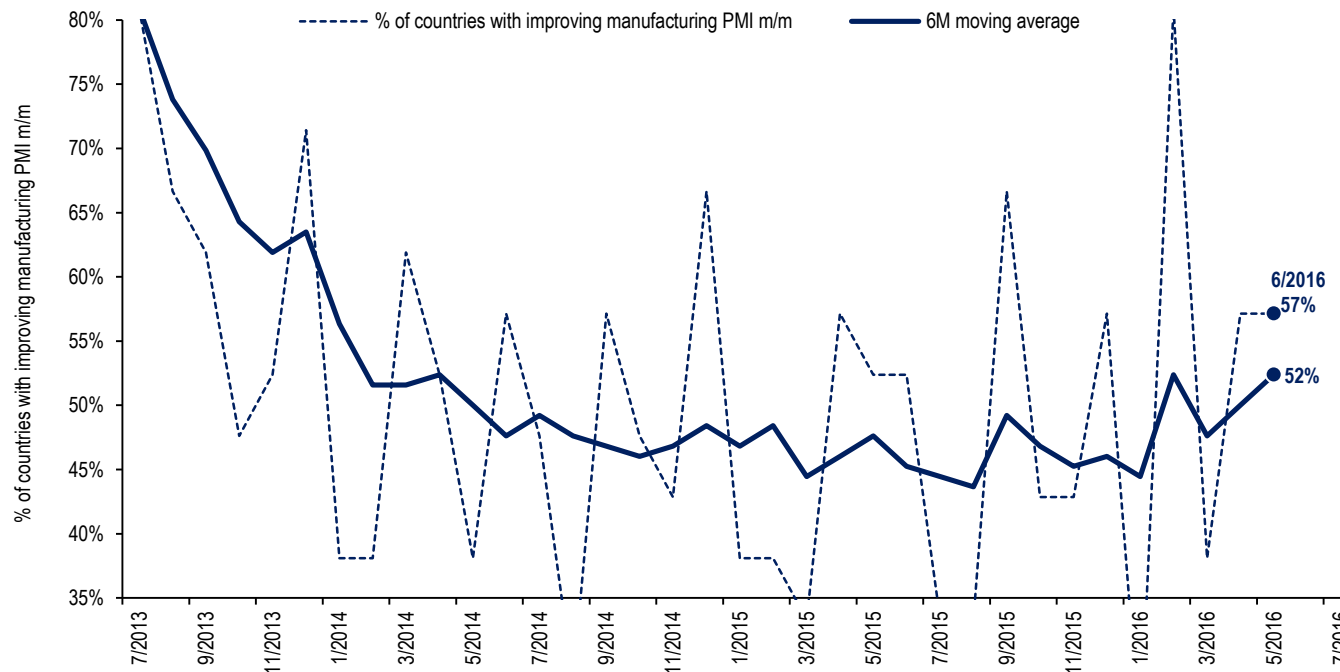
#3b: Global PMIs, more broadly, are improving... pre-Brexit...

Global PMIs, in general, have shown improvement. Based on the 24 countries, which report some type of manufacturing PMI (many of these are Markit series), the majority are now seeing improvement month-over-month.

- We realize this is pre-Brexit and therefore, the readings could deteriorate in the next few months, but the broader improvement in global PMIs corroborates the recovery in the ISM exports reading.
- There are several reasons we believe the global PMIs have started to recover – those are the same factors aiding the recovery in US ISM exports component.

Figure: The major of countries are seeing manufacturing PMIs improving...

24 countries. 6M moving average of % of countries with improving manufacturing PMI



The number of countries with improving PMIs is now over 50%. The 6-month moving average is the best level in 2-years (52%).

Granted, this is prior to Brexit but there is a good chance that Brexit's impact on global economic growth is significantly more muted than markets suggest...

Source: Fundstrat, Bloomberg.

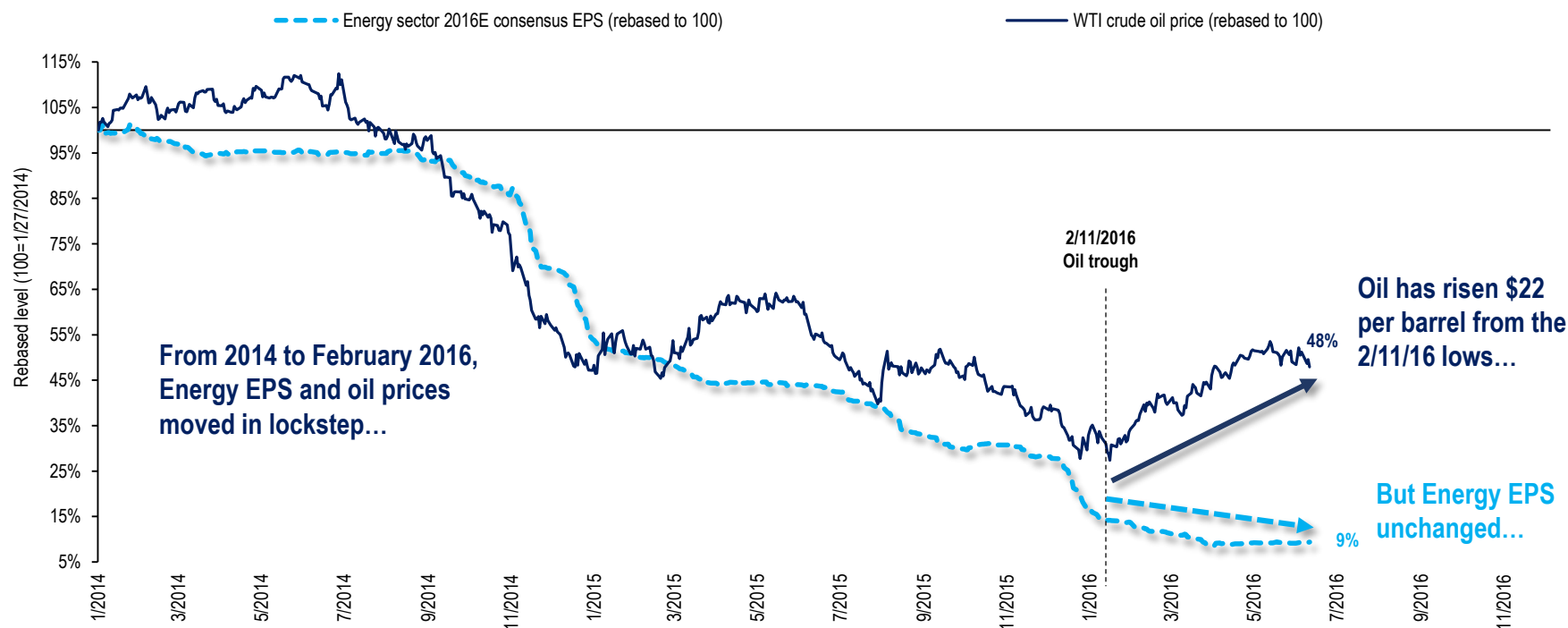
#4: Since February 2016, Energy EPS and Oil prices diverged...

As many of our clients are aware, oil prices and Energy sector EPS generally track closely but since February 11, 2016, Energy EPS forecasts and oil prices have diverged.

- What is interesting from the chart below, is that for the last two years, as oil prices moved, so did Energy sector EPS. In LOCKSTEP.
- But since February 2016, we have seen a recovery in oil prices but no upward revision in Energy EPS. Granted, there are multiple potential reasons—are cost timing differentials or hedging accounting for this? It is not entirely clear.

Figure: Energy EPS estimates are negative since oil trough

WTI crude oil and Energy EPS estimates (rebased to 100=1/27/2014)



Source: Fundstrat, Bloomberg, FactSet.

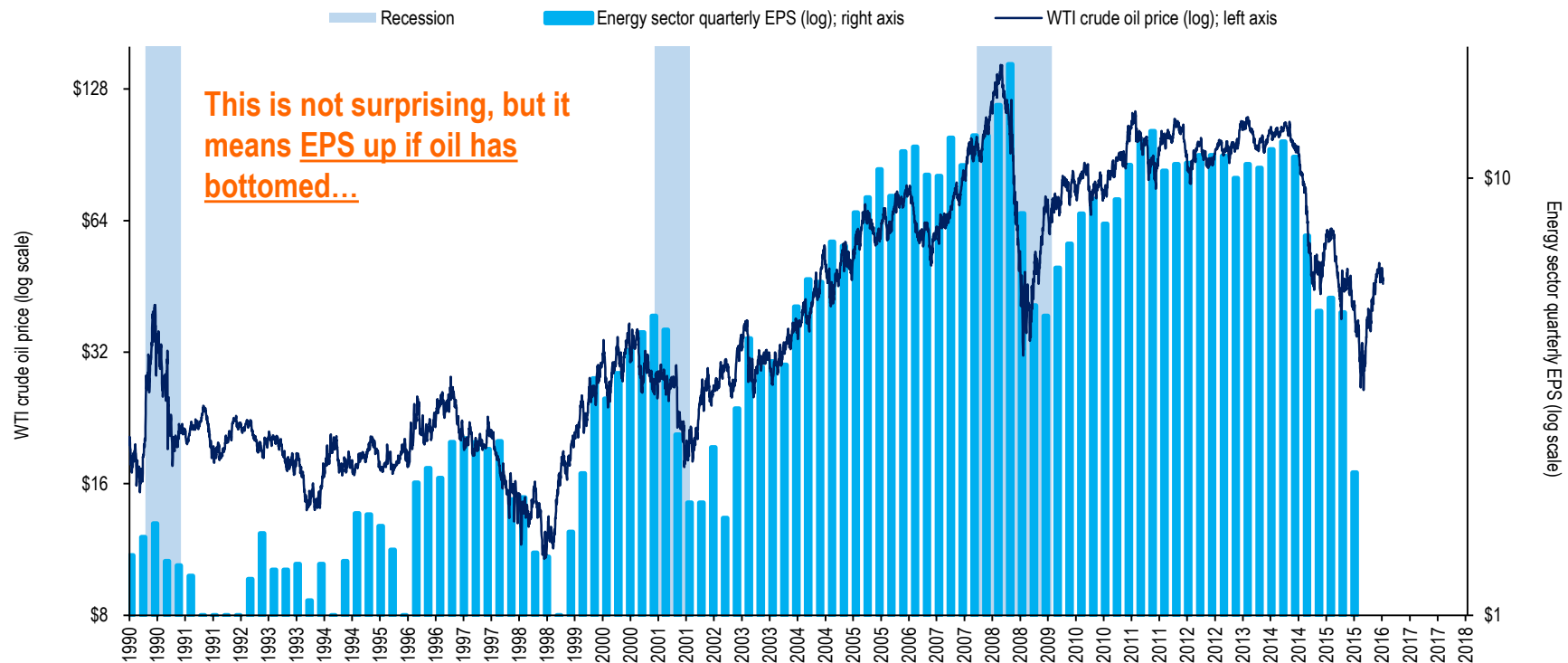
#4a: For past 25 years, oil and Energy EPS move in sync...

Apologies for stating the obvious, but oil is the primary driver of Energy earnings as shown below:

- There is simply no way for Energy companies to generate a higher level of EPS at low oil prices and it is pretty hard for them to lose money when oil prices are high.
- This relationship is evident looking at the chart below—for the past 25 years, one could basically predict the Energy Sector EPS just by plotting the price of oil.

Figure: Energy EPS is all about Oil...

WTI crude oil price (left axis) and S&P 500 Energy sector quarterly EPS (right axis) since 1990



Source: Fundstrat, Bloomberg, FactSet.

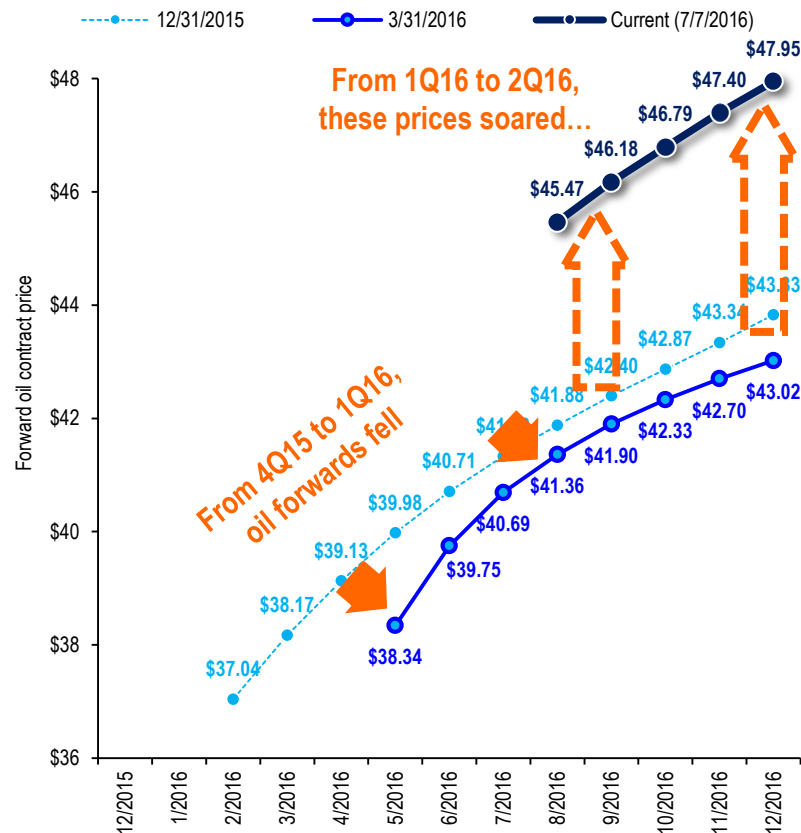
#4b: Change “oil forwards” suggests \$2-\$3 EPS upside next few quarters

When analysts modeled 2016 EPS for the **Integrated Oil** stocks, these were based on a 2016 oil forecast of \$41.50, which was the price of the oil curve in December 2015.

- Since then, oil has risen \$7-\$9 (depending at what point we look at on the strip) and this will have a dramatic impact on Integrated Oil’s net income. If oil remains flat into year-end, this would add \$25 billion in net income for the “majors”, and add \$2.61 in S&P 500 EPS.

Figure: Oil curve has improved vs. end of 2015 and 1Q16

Priced as of 7/7/2016



Source: Fundstrat, Bloomberg CCRV.

Figure: S&P 500 EPS impact from changes in Integrated Oils

Analysts forecasts for 2016 were based on \$41.50 oil in 2016

Oil Price Assumption (WTI)	RANGE 2016 Incremental Net Income					
	\$31.50	\$36.50	\$41.50	\$49.40	\$55.00	\$65.00
XOM	(\$17,383)	(\$8,691)	–	\$13,732	\$23,466	\$40,849
CVX	(\$9,632)	(\$4,816)	–	\$7,609	\$13,003	\$22,635
COP	(\$2,034)	(\$1,017)	–	\$1,607	\$2,746	\$4,780
OXY	(\$892)	(\$446)	–	\$704	\$1,204	\$2,095
CNQ	(\$902)	(\$451)	–	\$713	\$1,218	\$2,120
CVE	(\$879)	(\$439)	–	\$694	\$1,187	\$2,065
Total Net Income	(\$31,721)	(\$15,861)	–	\$25,060	\$42,824	\$74,545

Oil Price Assumption (WTI)	RANGE Incremental Impact to 2016 S&P500 EPS					
	\$31.50	\$36.50	\$41.50	\$49.40	\$55.00	\$65.00
XOM	(\$1.92)	(\$0.96)	–	\$1.52	\$2.59	\$4.51
CVX	(\$1.06)	(\$0.53)	–	\$0.84	\$1.44	\$2.50
COP	(\$0.22)	(\$0.11)	–	\$0.18	\$0.30	\$0.53
OXY	(\$0.10)	(\$0.05)	–	\$0.08	\$0.13	\$0.23
CNQ	–	–	–	–	–	–
CVE	–	–	–	–	–	–
Incremental S&P 500 EPS	(\$3.31)	(\$1.65)	–	\$2.61	\$4.47	\$7.77

Source: Fundstrat, Bloomberg CCRV.

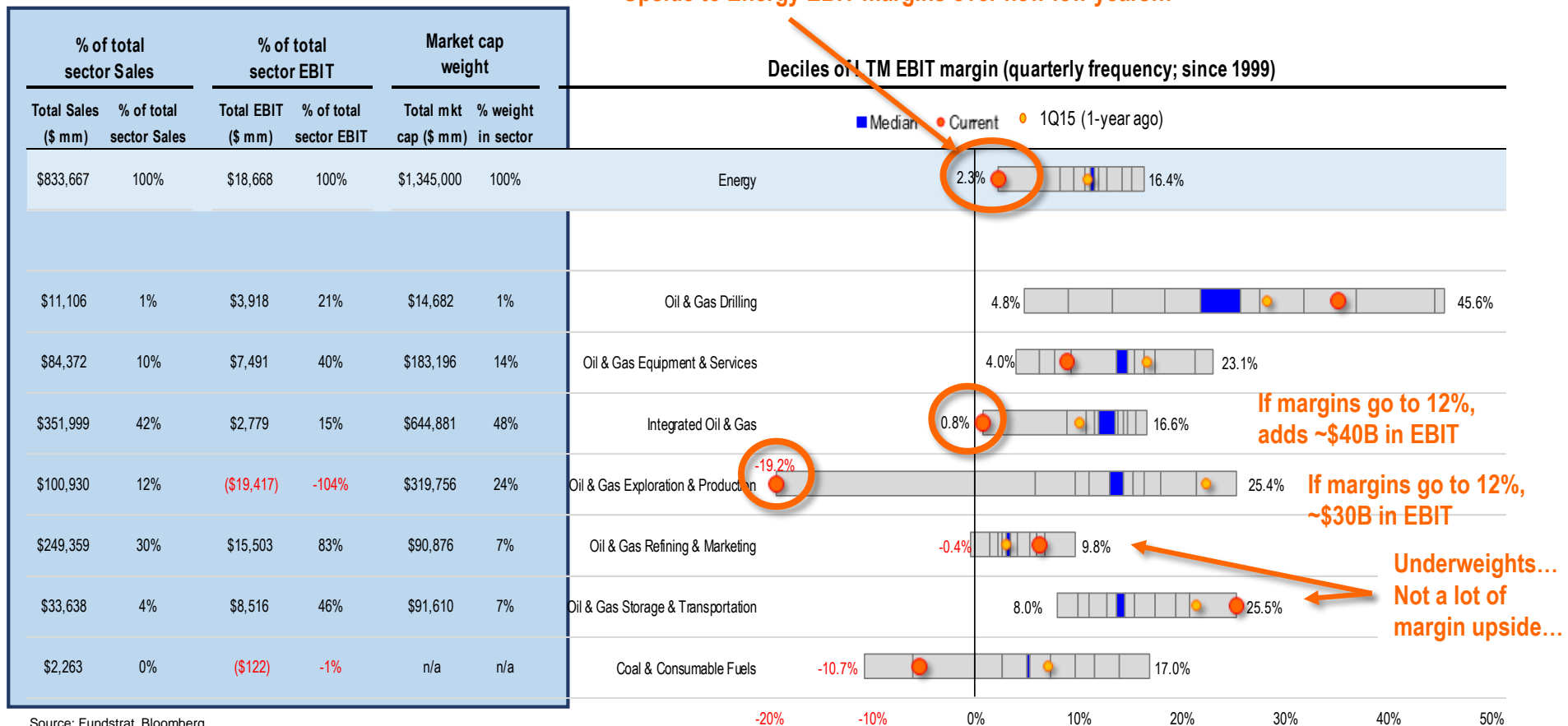
Note: incremental margin is forecast at 25% for oil price increases. Incremental net income and EPS is calendarized to adjust for fiscal year-end differences.

#4c: Energy margin recovery adds another \$5-\$8 in 2017

Another big lever to pull is the normalization of profit margins for Energy companies. As shown below, the profit margins of Integrations and E&Ps are depressed due to the rapid decline in oil prices—look how swiftly margins fell in past 12 months.

- A normalization of margins in 2017 for Integrations and E&Ps could add \$70B in EBIT in next 12 months and \$5-\$8 per S&P 500 share, depending on the magnitude of NOLs.

Figure: Deciles of Energy Sector EBIT margins
Since 1999



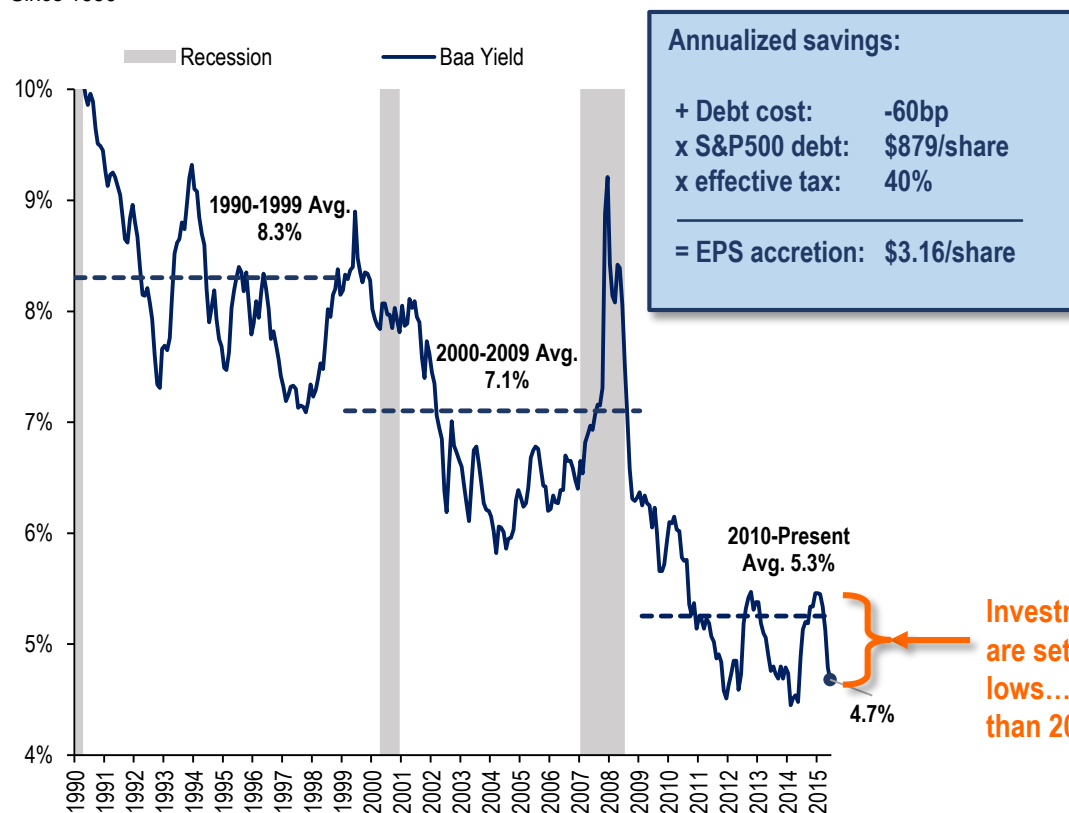
#5: Falling yields adds \$3.00 to S&P 500 EPS next 12 months

Another tailwind to S&P 500 EPS over the next few quarters is the drop in interest rates. The 10-year US Treasury bond has fallen from 2.19% a year ago to 1.36% now. And as shown on the bottom left chart, has pushed yields on investment grade bonds lower:

- We estimate that debt costs will fall about 60bp in the next 12 months. This should lead to about a \$3 EPS lift to S&P 500 EPS as shown on the table below. The simple math is 60bp of debt cost savings x \$879 debt/ share (S&P 500) x tax rate.

Figure: Moody's Baa Yield

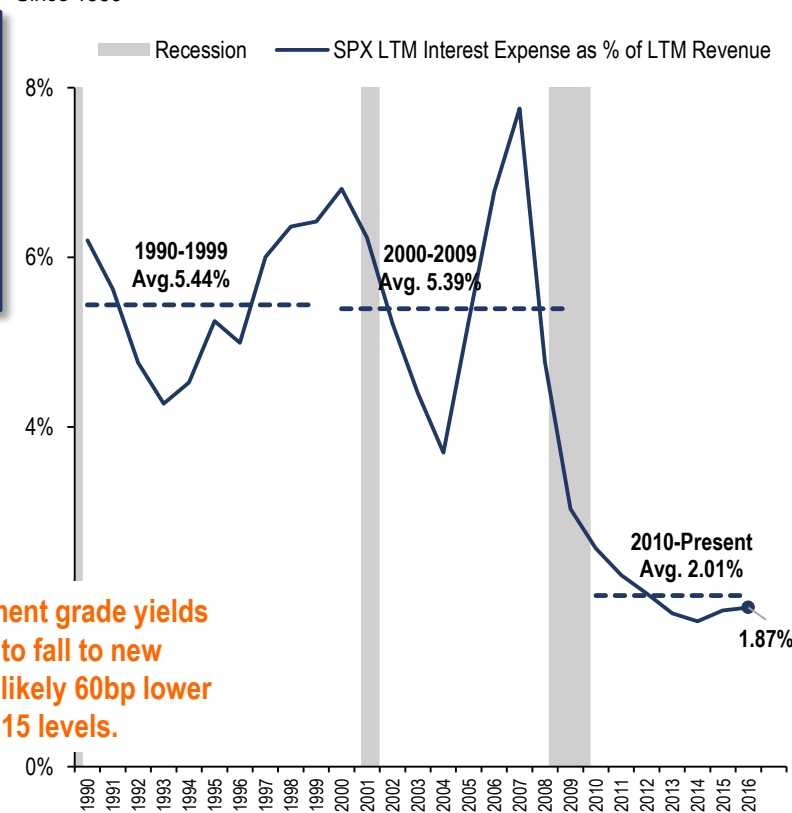
Since 1990



Source: Fundstrat, Bloomberg, St Louis Federal Reserve.

Figure: Interest burden set to fall even further...

Since 1990



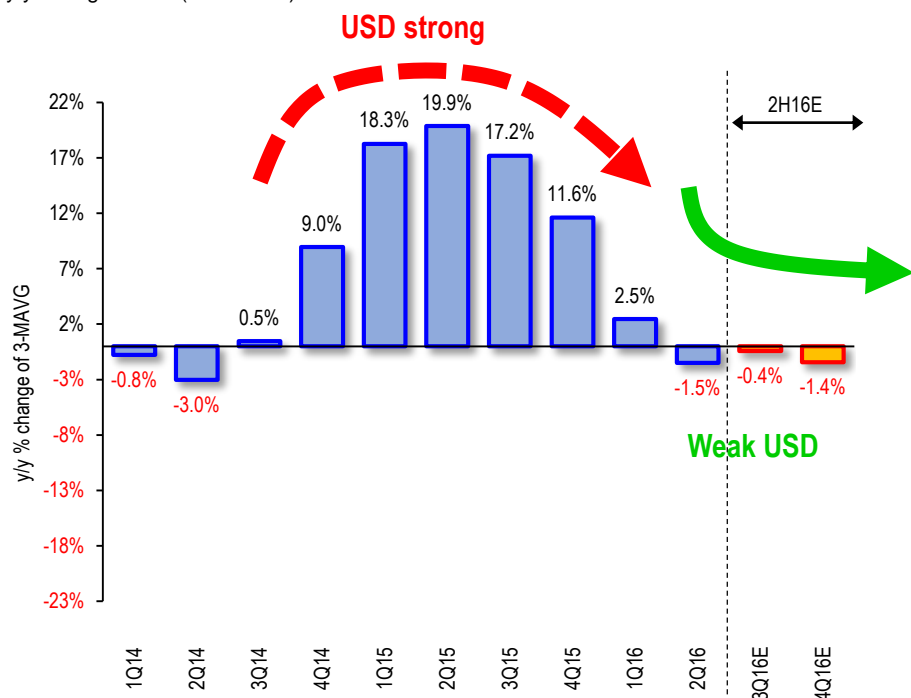
Source: Fundstrat, Bloomberg

#6: USD is a tailwind in 2016... boosting multi-national EPS...

Another simple variable to examine is the impact from USD on profits—again, we realize investors have been talking about this endlessly, but it does not alter the impact of USD and multi-national EPS growth.

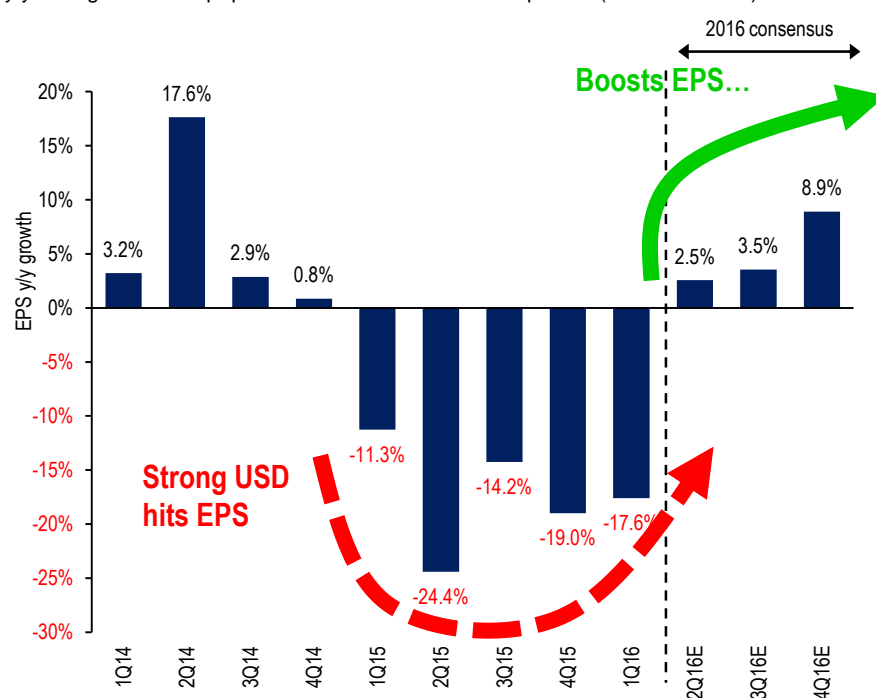
- As shown below, the strong USD gains yoy in 2015 (based on DXY) corresponded to a major decline in multi-national profits in 2015. In fact, on a casual basis, each 1% USD headwind turned into 1% EPS decline. The reasons for this are obvious—there is the translation effect (USD vs others) and the substitution effect (US cos had to sacrifice margins or volumes).
- But 2016 is proving to be very different dynamic—note that the USD is now weakening—hence, we see a recovery in multinational profits.

Figure: Dollar y/y chg turning from double-digits to negative
y/y % chg of USD (DXY Index) 3-MAVG since 1Q14



Source: Fundstrat, Bloomberg.
Note: projections for 3Q16 – 4Q16 are calculated by flat-lining the DXY Index from its current level.

Figure: Multinationals EPS will benefit from weakening USD
y/y EPS growth for top quartile of International sales exposure (within S&P 500) since 1Q14



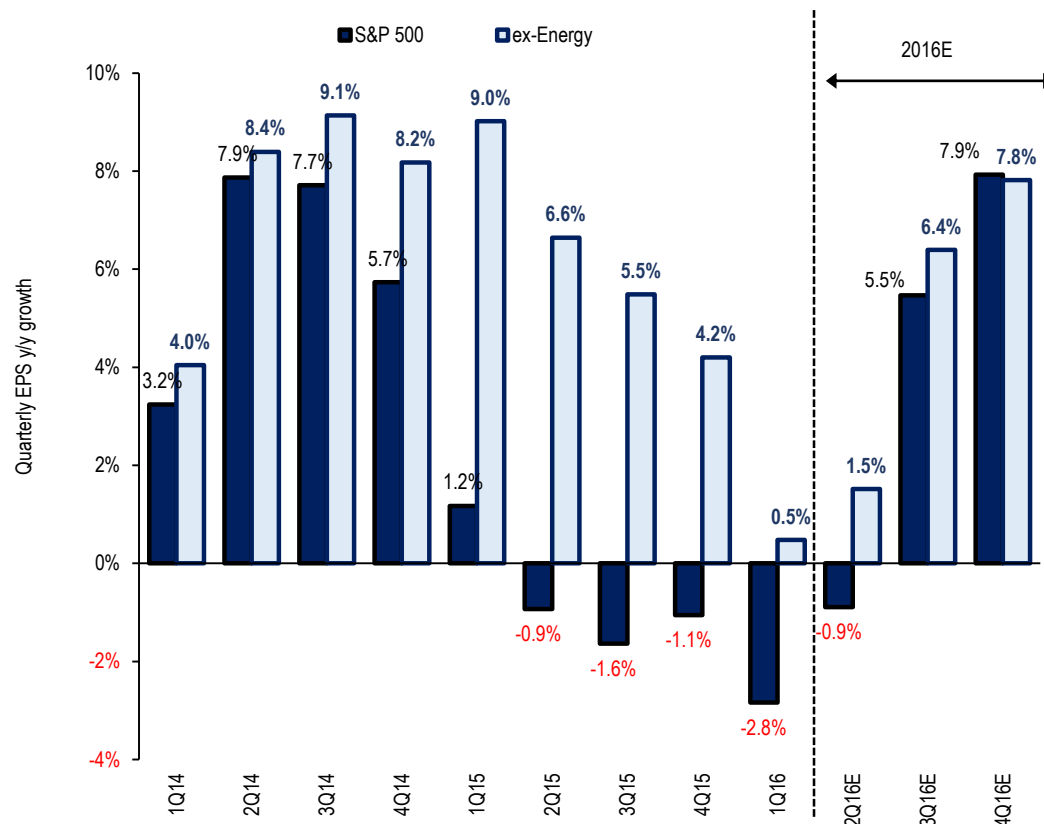
Source: Fundstrat, Bloomberg.
Note: based on a summation of the estimate-comparable net income for S&P 500 companies within the top quartile of International sales exposure (based on latest FY reported results). Estimates for 2Q16 – 4Q16 are based on consensus analyst estimates.

#7: Yes... we continue to believe profits inflect in 2H16....

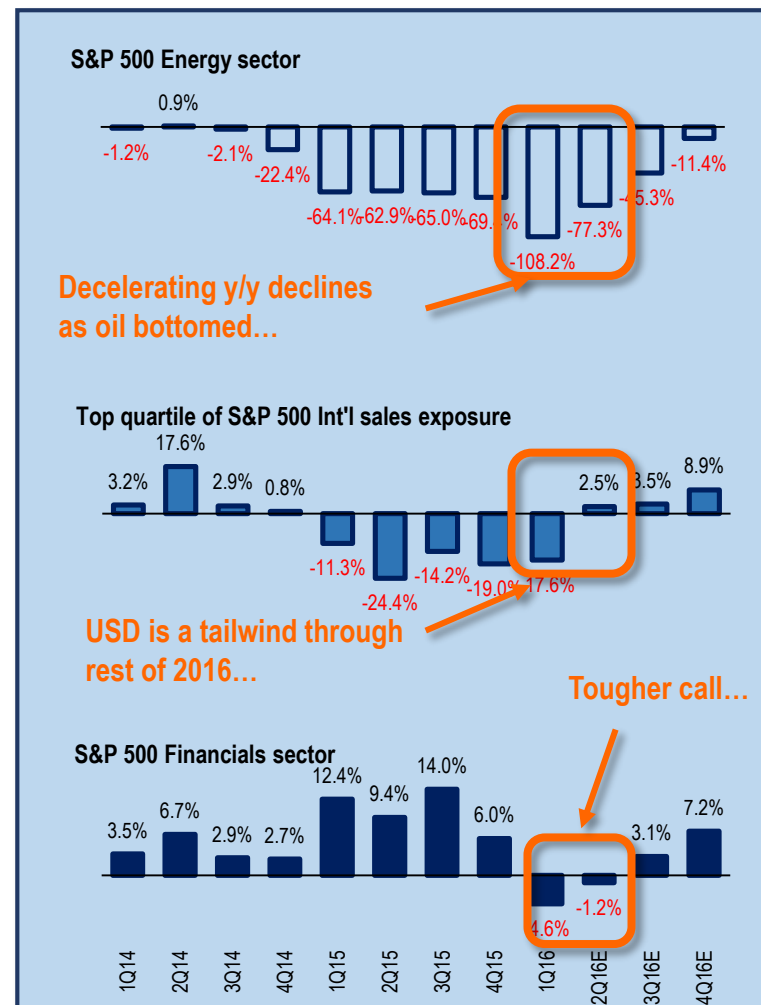
As shown below, we believe S&P 500 companies will begin to deliver an improvement in EPS growth rates in 2016. It hinges on an inflection in 3 groups:

- The most obvious are **Energy** (massive declines in 2015); **Multi-nationals** (15% declines) and **Financials** (part Energy/ part volumes).

Figure: 3 key sub-sets within S&P 500... they are collectively 60% of profits...
y/y EPS growth (quarterly) since 1Q14



Source: Fundstrat, FactSet.



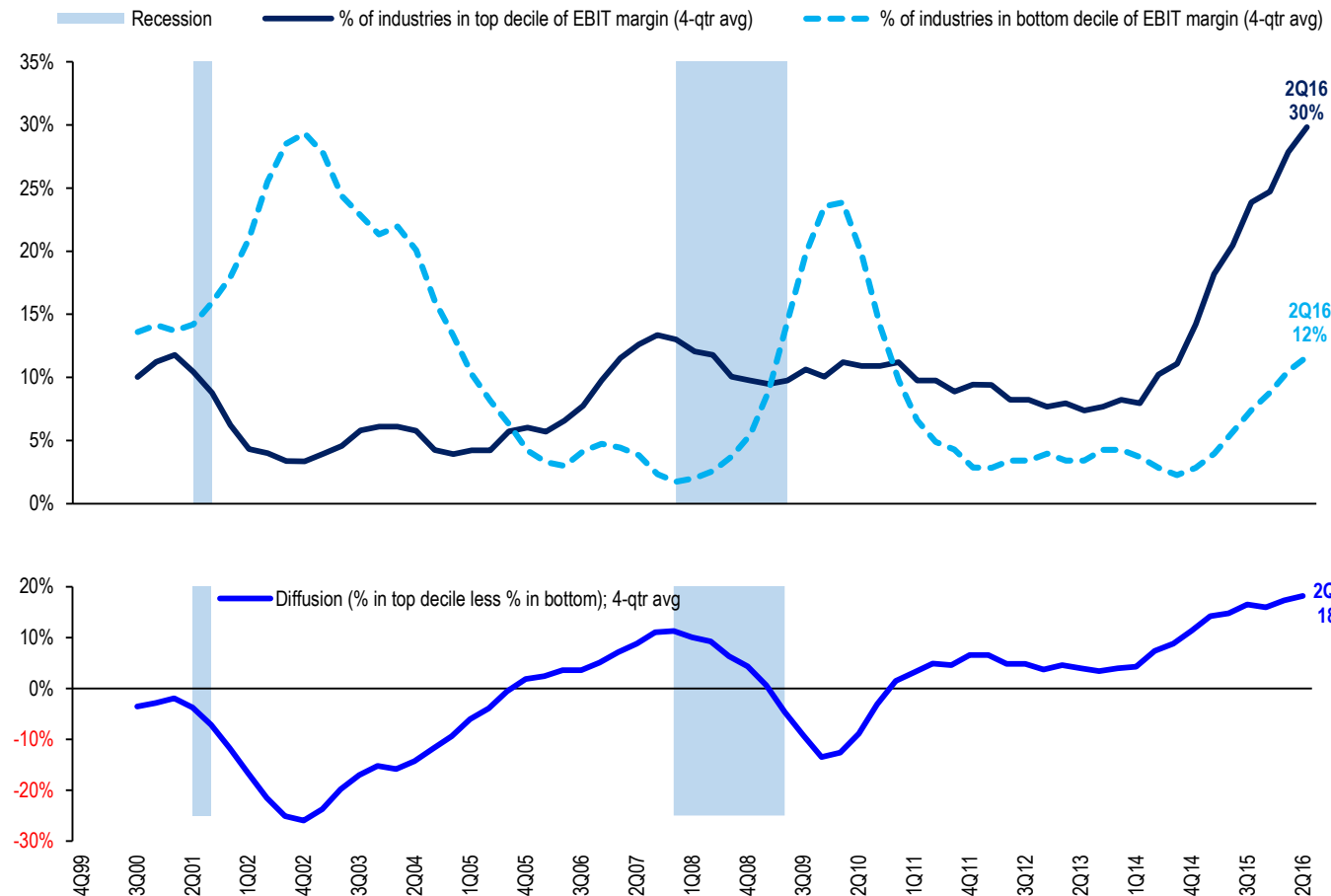
#7a: And overall profit margins should keep improving...

We have listed those industries seeing all-time high in margins and those seeing all-time lows (really deciles) and as shown below, an interesting pattern emerges.

- The number reaching highest ever deciles continues to soar.

Figure: The % of industries in top decile of EBIT margin is now at an all-time high...

Since 1999



Source: Fundstrat, Bloomberg, FactSet.

There are more companies with margins hitting and sustaining new highs, than companies with margins falling to new lows.

In fact as shown on the left, this is the best relative ratio ever...

The diffusion (spread between top and bottom decile) continues to widen.

Again, we see this as an argument to remain constructive on margins (see discussion in report)

#7b: We see several industries with low margins recovering in 2017...

Of the 11 industries with lowest decile of margins (right table), we see 4 of these likely to stage a profit recovery in next 12 months. Why? Because many of these companies are commodity-sensitive or affected by strong USD.

Figure: 27 groups in top decile of EBIT margin

Consecutive # of qtrs in top decile	Industries	
7	Biotechnology	Industrials Gases
	Media	REITs
	Aerospace & Defense	Trading Cos & Distributors
	Data Processing	
6	Specialty Retail	
5	Distillers & Vintners	Airlines
	Multi-Utilities	
4	Life Sciences Tools/Services	Oil & Gas Storage & Transportation
	Oil & Gas Storage/Transport	Auto Components
	Hotels, Restaurants, Leisure	Electronic Manufacturing Services
3	Household Products	Banks
2	Specialty Chemicals	Building Products
	Packaged Foods & Meats	Communications Equipment
	Capital Markets	Diversified Chemicals
	Tech Hardware & Storage	
1	Electric Utilities	

Source: Fundstrat, Bloomberg, FactSet.

Figure: 11 groups in bottom decile of EBIT margin

Consecutive # of qtrs in bottom decile	Industries	
7	Independent Power Producers & Energy Traders	
6	Pharmaceuticals	
5	Health Care Equipment	
4	Oil Integrated Oil & Gas Systems Software	Oil Diversified Metals & Mining
3	Oil Oil & Gas Exploration	Food Distributors
2	Hypermarkets & Super Centers	
1	Oil and USD Industrial Conglomerates	Health Care Supplies

Source: Fundstrat, Bloomberg, FactSet.

PORTFOLIO STRATEGY: Favor positive revisions

12 industries have seen both positive revisions in sales and EPS for 2Q16 and they are listed below.

- **This group reflects several positive trends—weaker USD, rising commodities for some. For others, it is the strengthening US consumer (homebuilding products and autos). Overall, we think this group of industries will likely perform best during 2Q16 reporting, which starts next week.**
- **We have identified 27 individual stock ideas within this list of 12 groups (see [slide 21](#) for the list of stocks).**

Figure: Groups with both positive Sales and EPS revisions

Consensus estimate revisions for 2Q16 over the past 3 months

Group name	# of cos	Mkt cap (\$B)	2Q16 revision		3M relative return
			Sales	EPS	
1 Distributors	2	\$25	2.3%	0.8%	0.5%
2 Electrical Equipment	5	\$98	1.8%	0.4%	-2.6%
3 Life Sciences Tools & Services	5	\$111	1.5%	0.2%	-1.3%
4 Internet Software & Services	7	\$796	1.4%	0.8%	-5.7%
5 Diversified Consumer Services	1	\$5	1.3%	6.8%	-7.8%
6 Oil, Gas & Consumable Fuels	29	\$1,134	1.3%	0.8%	7.2%
7 Metals & Mining	4	\$64	0.8%	46.2%	17.1%
8 Hotels, Restaurants & Leisure	11	\$329	0.7%	0.3%	-8.5%
9 Pharmaceuticals	11	\$1,092	0.7%	0.1%	4.3%
10 Construction Materials	2	\$29	0.5%	0.6%	14.7%
11 Automobiles	3	\$103	0.3%	2.3%	-2.2%
12 Building Products	3	\$26	0.1%	0.6%	1.1%

Source: Fundstrat, Bloomberg, FactSet.

Best and worst sales revisions into 2Q16...

Figure: Groups with POSITIVE Sales revisions for 2Q16

Consensus estimate revisions for 2Q16 over the past 3 months

2Q16 revision					
Group name	# of cos	Mkt cap (\$B)	Sales	EPS	3M relative return
1 Electric Utilities	14	\$407	3.9%	-0.8%	4.0%
2 Distributors	2	\$25	2.3%	0.8%	0.5%
3 Internet & Catalog Retail	5	\$476	2.1%	-10.3%	12.4%
4 Household Durables	9	\$98	2.0%	-0.3%	0.1%
5 Electrical Equipment	5	\$98	1.8%	0.4%	-2.6%
6 Construction & Engineering	3	\$16	1.8%	-5.2%	5.3%
7 Media	15	\$526	1.5%	-5.0%	0.9%
8 Life Sciences Tools & Services	5	\$111	1.5%	0.2%	-1.3%
9 Internet Software & Services	7	\$796	1.4%	0.8%	-5.7%
10 Diversified Consumer Services	1	\$5	1.3%	6.8%	-7.8%
11 Oil, Gas & Consumable Fuels	29	\$1,134	1.3%	0.8%	7.2%
12 Household Products	5	\$370	0.9%	-1.8%	-0.6%
13 Consumer Finance	5	\$136	0.9%	-2.2%	-4.2%
14 Metals & Mining	4	\$64	0.8%	46.2%	17.1%
15 Personal Products	1	\$20	0.8%	-22.0%	-5.9%
16 Health Care Providers & Services	17	\$514	0.8%	-1.5%	2.1%
17 IT Services	17	\$703	0.8%	-6.2%	-3.4%
18 Health Care Equipment & Supplies	15	\$523	0.8%	-1.3%	8.1%
19 Electronic Equipment, Instruments & Components	4	\$64	0.8%	-5.8%	-6.4%
20 Hotels, Restaurants & Leisure	11	\$329	0.7%	0.3%	-8.5%
21 Pharmaceuticals	11	\$1,092	0.7%	0.1%	4.3%
22 Tobacco	3	\$369	0.6%	-0.7%	2.0%
23 Construction Materials	2	\$29	0.5%	0.6%	14.7%
24 Beverages	7	\$460	0.5%	-1.4%	-0.5%
25 Specialty Retail	20	\$487	0.4%	-2.8%	-3.8%

Source: Fundstrat, Bloomberg, FactSet.

Figure: Groups with NEGATIVE Sales revisions for 2Q16

Consensus estimate revisions for 2Q16 over the past 3 months

2Q16 revision					
Group name	# of cos	Mkt cap (\$B)	Sales	EPS	3M relative return
1 Textiles, Apparel & Luxury Goods	9	\$159	-9.7%	-13.1%	-8.7%
2 Technology Hardware, Storage & P	7	\$659	-7.5%	-20.1%	-11.5%
3 Machinery	14	\$253	-4.9%	-2.2%	1.2%
4 Road & Rail	6	\$146	-4.3%	-9.2%	5.7%
5 Insurance	21	\$481	-3.0%	-6.4%	0.2%
6 Real Estate Investment Trusts (REITs)	27	\$600	-3.0%	0.5%	2.5%
7 Real Estate Management & Development	1	\$8	-2.8%	-1.9%	-14.9%
8 Capital Markets	14	\$354	-2.5%	-2.9%	-3.9%
9 Energy Equipment & Services	8	\$197	-1.9%	-148.6%	7.6%
10 Chemicals	15	\$386	-1.9%	-4.9%	-2.7%
11 Software	12	\$818	-1.8%	-7.7%	-3.7%
12 Health Care Technology	1	\$20	-1.7%	-1.7%	3.7%
13 Multi-Utilities	11	\$216	-1.5%	-3.8%	4.1%
14 Industrial Conglomerates	3	\$416	-1.4%	37.3%	2.1%
15 Professional Services	5	\$58	-1.2%	-1.7%	1.7%
16 Containers & Packaging	6	\$57	-1.0%	-2.5%	0.3%
17 Independent Power and Renewable	2	\$13	-1.0%	-14.1%	11.3%
18 Biotechnology	8	\$557	-0.8%	-1.3%	-6.3%
19 Multiline Retail	6	\$114	-0.8%	-13.3%	-7.5%
20 Diversified Financial Services	7	\$305	-0.7%	-3.3%	-0.1%
21 Air Freight & Logistics	4	\$135	-0.6%	-0.6%	-1.9%
22 Banks	17	\$955	-0.5%	-2.7%	-0.3%
23 Semiconductors & Semiconductor Equipment	16	\$520	-0.5%	1.4%	2.2%
24 Food Products	13	\$420	-0.4%	0.8%	7.0%
25 Commercial Services & Supplies	6	\$88	-0.3%	-4.7%	6.0%

Source: Fundstrat, Bloomberg, FactSet.

Revisions and relative stock price performance.

Figure: **SALES** revisions (for 2Q16) vs. relative stock price performance

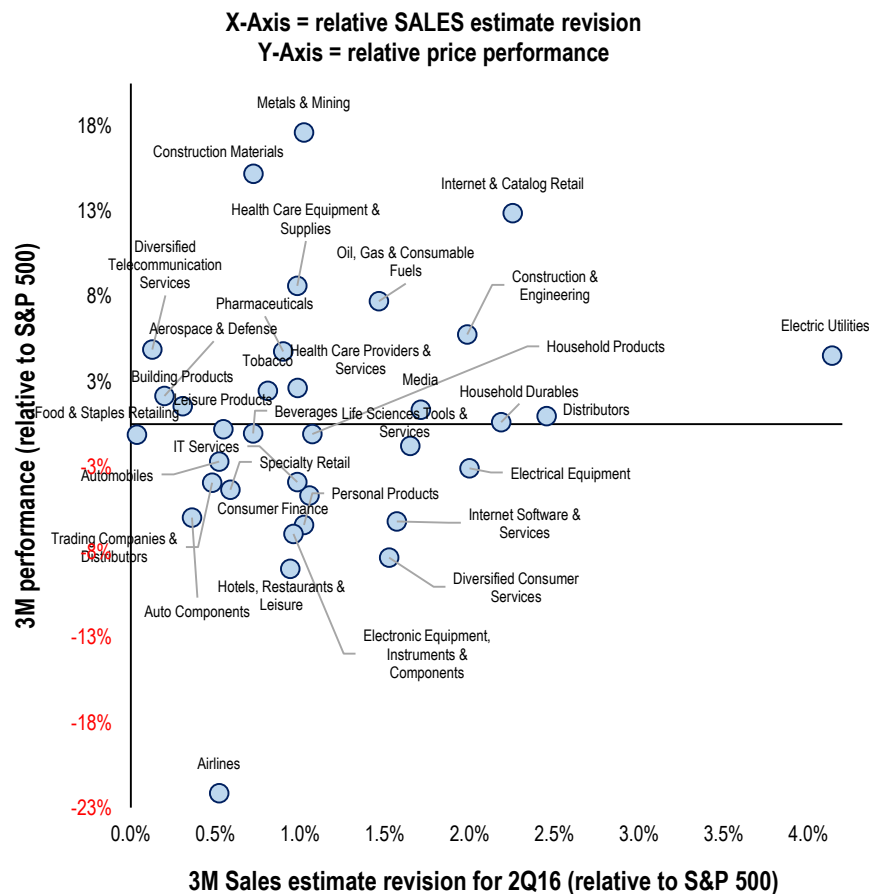
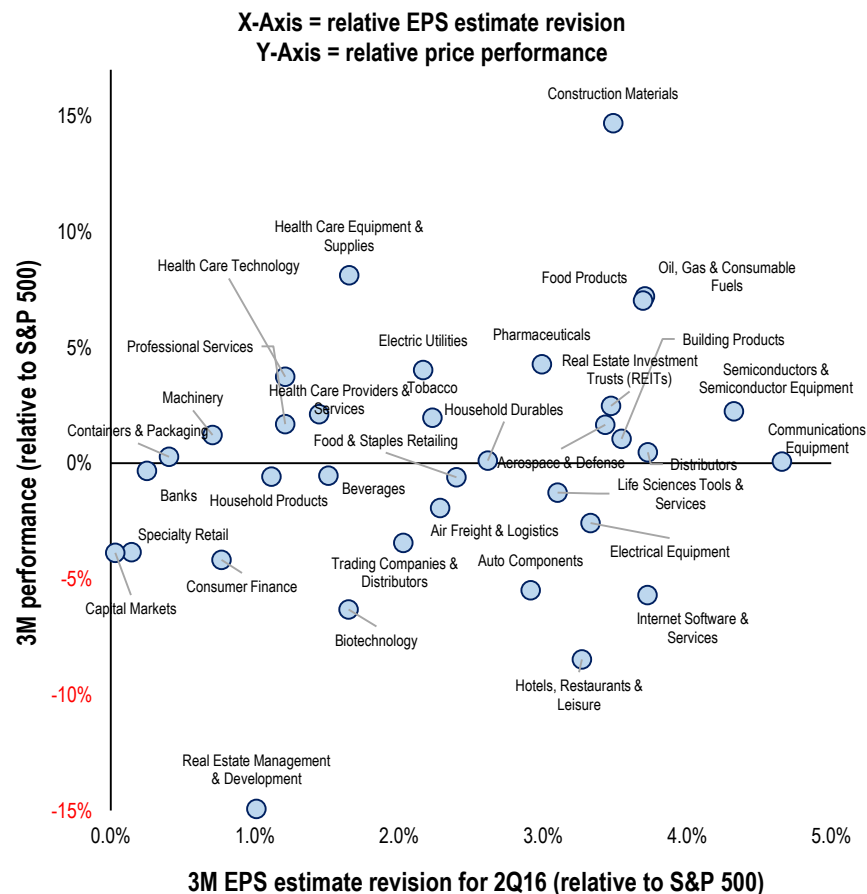


Figure: **EPS** revisions (for 2Q16) vs. relative stock price performance



Stock Strategy: 27 cos with positive EPS estimate revisions...

We screened for stocks that meet the following criteria: (i) member of one of the 12 industries with positive Sales AND EPS revisions (highlighted on [slide 18](#)), (ii) the company's 2Q16 consensus EPS estimate has been revised higher over the last 3 months, and (iii) if the stock is a member of the Energy sector, its short interest (as % of float) is above its own long-term average.

Figure: 27 companies seeing positive EPS estimate revisions for 2Q16

Priced as of 7/7/2016

	Ticker	Name	Current price	Market cap (\$M)	Daily liquidity (3-MAVG)	YTD relative return	Short interest		2Q16 estimate revisions		Upcoming earnings report date	P/E ('16E)	EV / EBITDA
							Short interest % of float	Short interest Z-Score	Sales	EPS			
Automobiles	1 F	Ford Motor Co	\$12.75	\$50,654	\$421	-10.2%	3.9%	-0.40	-1.5%	7.4%	7/28/2016	6.4x	2.6x
Building Products	2 FBHS	Fortune Brands Home & Secu	\$58.78	\$9,015	\$94	3.3%	5.6%	0.34	0.4%	1.9%	7/27/2016	22.0x	13.0x
	3 ALLE	Allegion Plc	\$68.64	\$6,571	\$42	1.5%	2.0%	0.16	1.3%	1.8%	7/28/2016	19.8x	14.8x
Construction Materials	4 MLM	Martin Marietta Materials	\$195.35	\$12,410	\$142	40.4%	5.7%	-1.00	1.7%	4.3%	8/2/2016	25.4x	13.3x
Distributors	5 LKQ	Lkq Corp	\$31.97	\$9,805	\$98	5.3%	2.7%	-0.66	13.3%	3.1%	7/28/2016	16.8x	10.9x
Diversified Consumer Services	6 HRB	H&R Block Inc	\$23.50	\$5,182	\$99	-32.1%	10.9%	0.62	1.8%	3.9%	9/1/2016	12.8x	6.7x
Electrical Equipment	7 ETN	Eaton Corp Plc	\$60.11	\$27,530	\$143	12.9%	1.4%	-0.33	0.8%	0.0%	7/27/2016	13.8x	n/m
	8 EMR	Emerson Electric Co	\$52.37	\$33,692	\$190	6.9%	2.7%	0.51	1.3%	0.6%	8/2/2016	16.7x	9.6x
Hotels Restaurants & Leisure	9 MCD	Mcdonald'S Corp	\$120.92	\$106,151	\$677	-0.3%	2.3%	0.50	1.7%	1.7%	7/26/2016	21.2x	13.4x
	10 HOT	Starwood Hotels & Resorts	\$75.54	\$12,807	\$224	15.2%	3.5%	-0.27	4.3%	1.9%	7/27/2016	25.5x	12.6x
	11 WYNN	Wynn Resorts Ltd	\$88.96	\$9,055	\$282	25.9%	13.7%	0.18	0.2%	13.0%	7/27/2016	26.3x	13.4x
Internet Software & Services	12 FB	Facebook Inc-A	\$115.85	\$331,366	\$2,880	8.1%	1.1%	-1.84	1.6%	12.1%	7/27/2016	30.6x	18.3x
	13 VRSN	Verisign Inc	\$83.40	\$9,047	\$64	-7.2%	19.6%	0.53	0.8%	0.5%	7/28/2016	23.6x	n/m
Life Sciences Tools & Services	14 WAT	Waters Corp	\$142.47	\$11,532	\$65	3.2%	3.7%	0.22	2.1%	1.2%	7/26/2016	22.0x	14.8x
	15 PKI	Perkinelmer Inc	\$52.59	\$5,734	\$35	-4.5%	2.7%	0.23	0.1%	1.8%	7/28/2016	18.3x	14.2x
	16 TMO	Thermo Fisher Scientific Inc	\$149.06	\$58,657	\$210	2.4%	1.2%	-0.83	2.4%	1.8%	7/28/2016	17.9x	16.1x
Metals & Mining	17 AA	Alcoa Inc	\$9.34	\$12,283	\$235	-8.0%	9.5%	0.46	-0.5%	13.8%	7/11/2016	22.6x	8.4x
	18 NEM	Newmont Mining Corp	\$40.96	\$21,731	\$306	125.0%	1.9%	-0.58	1.2%	36.2%	7/20/2016	27.6x	9.2x
	19 NUE	Nucor Corp	\$51.51	\$16,377	\$132	25.2%	2.7%	-0.38	11.2%	45.1%	7/21/2016	17.6x	7.2x
	20 FCX	Freeport-Mcmoran Inc	\$10.67	\$13,360	\$493	55.0%	11.5%	0.52	-4.5%	86.8%	7/26/2016	11.1x	5.9x
Oil, Gas & Consumable Fuels	21 SWN	Southwestern Energy Co	\$12.33	\$6,062	\$217	70.8%	19.6%	0.73	-4.0%	33.0%	7/21/2016	n/m	17.2x
	22 MUR	Murphy Oil Corp	\$30.00	\$5,166	\$123	31.0%	12.1%	0.71	4.9%	36.7%	7/27/2016	n/m	7.1x
	23 MRO	Marathon Oil Corp	\$14.74	\$12,494	\$291	14.4%	4.3%	0.62	-1.5%	26.7%	8/3/2016	n/m	10.6x
	24 APA	Apache Corp	\$54.90	\$20,781	\$209	20.8%	4.2%	0.52	6.2%	43.5%	8/4/2016	n/m	10.4x
Pharmaceuticals	25 BMJ	Bristol-Myers Squibb Co	\$74.08	\$123,662	\$420	5.1%	1.0%	-0.45	4.1%	5.7%	7/28/2016	28.2x	n/m
	26 PFE	Pfizer Inc	\$35.77	\$216,940	\$1,013	8.2%	0.9%	-0.10	0.9%	3.9%	8/2/2016	14.8x	n/m
	27 ZTS	Zoetis Inc	\$47.69	\$23,664	\$166	-3.1%	1.1%	-0.18	0.8%	2.1%	8/3/2016	24.5x	n/m
Median				\$12,807	\$209	6.9%	3.5%	0.18	1.3%	3.9%		21.2x	11.8x
% of stocks positive									88%	100%			

Source: Fundstrat, FactSet, Bloomberg.

SECTORS: Industrials outperform despite stronger USD...

There were several shifts in sector leadership over the past month, the most notable being **Industrials** outperformance of 40bp despite USD strengthening by 2.6%. Three of four Defensive sectors reverted from laggards to leaders, and all four outperformed as investors cautiously reposition in the wake of the U.K. referendum (Brexit). **Telecom**, **Utilities**, and **Staples** were easily the best groups to own, outperforming by 400-690bp.

Figure: Trailing 1-month relative performance of sectors

Since August 2015

Group name	8/7/15	9/7/15	10/7/15	11/7/15	12/7/15	1/7/16	2/7/16	3/7/16	4/7/16	5/7/16	6/7/16	7/7/16
S&P 500 (Abs.)	-0.2%	-7.5%	3.9%	5.2%	-1.1%	-6.5%	-3.2%	6.5%	2.0%	0.7%	2.7%	-0.7%
Cyclicals	0.3%	1.0%	1.0%	1.5%	0.4%	-2.0%	-0.2%	1.1%	1.2%	-1.6%	0.0%	-0.7%
Materials	-5.5%	0.3%	0.1%	-1.1%	0.1%	-3.2%	3.8%	1.2%	-1.3%	3.5%	1.3%	-4.0%
Industrials	-1.3%	1.1%	1.3%	-0.4%	0.0%	-0.5%	2.6%	0.7%	-0.4%	0.9%	-1.1%	0.4%
Discretionary	0.9%	1.7%	0.3%	0.9%	0.2%	-1.3%	-2.5%	2.2%	0.3%	0.8%	-2.7%	0.7%
Technology	1.5%	0.5%	1.6%	3.2%	0.8%	-2.9%	-0.7%	0.5%	2.9%	-5.0%	2.1%	-1.6%
Near Cyclicals	-1.5%	-1.2%	0.6%	-0.1%	-3.0%	-1.6%	-1.8%	0.9%	-3.2%	4.9%	0.4%	-3.0%
Energy	-9.7%	2.2%	3.9%	-2.4%	-10.2%	-0.8%	2.5%	4.0%	-3.6%	6.0%	2.9%	-1.7%
Financials	2.4%	-2.6%	-0.9%	1.0%	0.2%	-1.9%	-3.5%	-0.4%	-3.1%	4.4%	-0.8%	-3.6%
Defensives	0.9%	-0.5%	-1.9%	-2.4%	1.7%	4.3%	1.7%	-2.2%	0.6%	-1.0%	-0.3%	3.4%
Staples	2.0%	0.1%	1.4%	-4.5%	3.5%	4.6%	3.6%	-2.5%	0.9%	-0.7%	-2.3%	4.0%
HealthCare	0.3%	-1.4%	-4.8%	0.5%	0.4%	3.4%	-3.6%	-1.1%	0.6%	-1.4%	1.5%	1.8%
Telecom	-3.1%	3.4%	-4.1%	-2.6%	2.9%	4.1%	13.7%	-2.6%	-1.7%	-1.3%	-1.2%	6.9%
Utilities	2.3%	-0.8%	3.0%	-8.2%	1.5%	8.4%	11.2%	-5.3%	1.1%	-0.4%	-0.9%	5.5%





Source: Fundstrat, Bloomberg.

STYLES: Higher-risk styles underperform

Each of the high-risk styles we track (High-Beta, Contrarian, and Small-Cap) underperformed over the past two weeks in the wake of Brexit. Growth stocks posted their best outperformance since the first week of May, beating the S&P 500 by 50bp.

Figure: Trailing 1-week absolute performance of styles

Since May 2016

5/5/2016	5/12/2016	5/19/2016	5/26/2016	6/2/2016	6/9/2016	6/16/2016	6/23/2016	6/30/2016	7/7/2016	
Low Volatility 0.8%	Low Volatility 1.5%	FS: Credit easing 1.0%	High Beta 4.3%	Russell 2000 2.7%	FS: USD weakens 2.7%	FS: Value over FANG -0.1%	High Beta 5.1%	Low Volatility 2.6%	Growth 0.5%	 = Fundstrat theme strategy
Momentum (D.J.) -0.5%	Momentum (D.J.) 1.4%	High Beta 0.2%	Russell 2000 4.1%	Contrarian 2.2%	Dividend Yield 1.8%	Low Volatility -0.3%	FS: Credit easing 5.0%	FS: Value over FANG 1.0%	Low Volatility 0.5%	 = styles with higher risk
Growth -0.6%	Dividend Yield 1.2%	Value -1.1%	Contrarian 4.1%	FS: Credit easing 1.8%	Low Volatility 1.7%	FS: Stocks "new bonds" -1.2%	FS: USD weakens 3.6%	Dividend Yield 0.8%	Mega-Cap 0.4%	 = S&P 500
Dividend Yield -0.7%	Growth 0.9%	Equal Weight -1.1%	FS: USD weakens 3.7%	High Beta 1.7%	FS: Stocks "new bonds" 1.2%	Dividend Yield -1.3%	Contrarian 2.9%	Momentum (D.J.) 0.5%	Momentum (D.J.) 0.4%	 = all other styles
FS: Value over FANG -0.8%	Mega-Cap 0.8%	S&P 500 -1.2%	FS: Credit easing 3.5%	Momentum (D.J.) 1.2%	FS: Value over FANG 1.2%	Mega-Cap -1.4%	Equal Weight 2.5%	FS: Stocks "new bonds" -0.1%	S&P 500 0.0%	Fundstrat theme definitions: USD weakens: Buy stocks inverse correlation to USD (Value style, Energy / Materials / Telecom sectors) Credit easing: Buy inverse correlation to HY spreads (Value and Low-Quality) FANG ends with DANG: Leaders rarely lead the following year. Buy Value over Momentum. Stocks are the "new bonds": Buy stocks where dividend yield > co's own bond yield.
Mega-Cap -0.8%	FS: Value over FANG 0.8%	Mega-Cap -1.2%	Growth 2.7%	Equal Weight 1.2%	Momentum (D.J.) 1.0%	Momentum (D.J.) -1.6%	Value 2.3%	Mega-Cap -0.2%	Dividend Yield 0.0%	
FS: Stocks "new bonds" -1.0%	S&P 500 0.7%	Growth -1.2%	Equal Weight 2.7%	Dividend Yield 1.1%	Contrarian 1.0%	Growth -1.7%	FS: Stocks "new bonds" 2.2%	Growth -0.6%	FS: Value over FANG -0.2%	
S&P 500 -1.2%	FS: Stocks "new bonds" 0.6%	Russell 2000 -1.2%	Momentum (D.J.) 2.6%	Low Volatility 0.8%	Russell 2000 0.9%	S&P 500 -1.8%	Russell 2000 2.1%	S&P 500 -0.7%	Equal Weight -0.3%	
Equal Weight -1.8%	Value 0.4%	Contrarian -1.4%	Mega-Cap 2.5%	Value 0.8%	Equal Weight 0.7%	Value -1.9%	Dividend Yield 2.0%	Value -0.8%	Russell 2000 -0.4%	
Value -1.8%	Equal Weight 0.3%	Momentum (D.J.) -1.5%	FS: Stocks "new bonds" 2.5%	S&P 500 0.7%	Value 0.7%	Equal Weight -2.5%	S&P 500 1.7%	Equal Weight -1.5%	Value -0.5%	
Russell 2000 -2.8%	Russell 2000 0.1%	FS: Stocks "new bonds" -1.9%	S&P 500 2.5%	Growth 0.7%	S&P 500 0.5%	Russell 2000 -2.8%	Momentum (D.J.) 1.7%	Russell 2000 -1.7%	Contrarian -0.6%	
FS: USD weakens -3.1%	FS: Credit easing -0.1%	Low Volatility -2.1%	Dividend Yield 2.2%	FS: USD weakens 0.7%	High Beta 0.4%	FS: USD weakens -3.3%	FS: Value over FANG 1.5%	Contrarian -3.5%	FS: Stocks "new bonds" -0.7%	
Contrarian -4.4%	FS: USD weakens -0.5%	Dividend Yield -2.1%	Value 2.2%	FS: Value over FANG 0.5%	Mega-Cap 0.3%	Contrarian -3.6%	Mega-Cap 1.2%	FS: Credit easing -4.5%	FS: USD weakens -1.1%	
High Beta -5.3%	Contrarian -0.8%	FS: USD weakens -2.3%	FS: Value over FANG 1.9%	FS: Stocks "new bonds" 0.4%	Growth 0.3%	FS: Credit easing -4.6%	Growth 1.1%	FS: USD weakens -4.8%	FS: Credit easing -1.5%	
FS: Credit easing -5.3%	High Beta -1.0%	FS: Value over FANG -2.7%	Low Volatility 1.2%	Mega-Cap 0.4%	FS: Credit easing -0.2%	High Beta -5.1%	Low Volatility 1.1%	High Beta -4.8%	High Beta -1.8%	

Source: Fundstrat, Bloomberg.

GLOBAL CDS SPREADS: Financials driving wider spreads in Europe...

CDS spreads in Europe widened by 9bp over the past month, dwarfing both the US (+3bp) and Japan (+1bp). The deterioration was fairly widespread, as the CDS spread for each category of European Financials we track showed significant widening.

- Despite the deterioration of Financials, Energy spreads continue to stage an extremely impressive rally with both IG and HY spreads narrowing m/m – in North America, IG and HY tightened 10bp and 13bp respectively.

Figure: Level of Global CDS Spreads (bp)

Since June 2014

 = spreads narrowing m/m

5-yr CDS spread (bp)		6/14	7/14	8/14	9/14	10/14	11/14	12/14	1/15	2/15	3/15	4/15	5/15	6/15	7/15	8/15	9/15	10/15	11/15	12/15	1/16	2/16	3/16	4/16	5/16	6/16	7/16
Global		57	56	68	56	70	65	63	70	66	62	60	66	67	71	75	84	84	79	83	96	115	94	82	85	74	77
North America	Markit iTraxx North America IG CDS	57	56	68	56	70	65	63	70	66	62	60	66	67	71	75	84	84	79	83	96	115	94	82	85	74	77
	Bloomberg America Energy IG 5Y CDS	60	57	69	64	85	101	136	175	171	139	132	116	118	138	160	178	199	196	242	358	447	380	303	247	222	212
	Bloomberg America Sr. Financials IG 5Y CDS	64	67	77	67	80	77	73	81	80	78	74	76	75	87	81	83	79	75	75	75	94	98	103	101	97	98
	Bloomberg America Subordinated Financials IG 5Y CDS	77	88	103	87	89	82	84	91	89	85	86	88	86	97	95	107	118	98	100	102	124	108	117	106	98	105
	Markit iTraxx North America HY CDS	306	351	315	329	338	309	302	346	316	361	339	330	358	368	325	336	335	336	355	354	395	504	425	450	473	507
	Bloomberg America Energy HY 5Y CDS	258	257	299	276	347	441	536	717	732	690	1096	1068	1162	1266	1840	1810	1033	1125	1423	1597	2032	1550	1453	972	795	782
Europe	Markit iTraxx Europe 5Y CDS	58	59	71	55	67	65	55	65	56	49	56	62	68	81	66	73	83	71	72	83	110	90	82	80	73	82
	Blomberg Europe Energy IG 5Y CDS	47	49	60	50	56	65	67	93	77	65	72	67	69	76	78	94	97	88	97	137	199	148	133	108	95	89
	Bloomberg Europe Sr. Financials IG 5Y CDS	67	70	81	66	71	70	63	75	70	61	70	78	80	99	83	89	83	74	71	77	108	103	104	98	92	113
	Bloomberg Europe Subordinated Financials IG 5Y CDS	113	118	135	110	185	182	168	191	178	151	171	189	191	222	197	207	192	168	164	174	260	243	248	233	214	262
	Markit iTraxx Europe HY 5Y CDS	224	233	298	227	348	353	310	353	304	253	255	283	305	349	307	338	342	295	294	343	422	369	334	331	316	366
	Bloomberg Europe Sr. Financials HY 5Y CDS	172	205	252	199	220	203	190	205	200	162	176	186	189	217	203	266	253	265	262	354	445	408	394	392	375	416
Asia	Bloomberg Europe Subordinated Financials HY 5Y CDS	225	242	347	226	410	410	396	427	414	334	333	311	314	385	348	428	430	439	425	567	785	723	684	670	659	777
	Markit iTraxx Japan 5Y CDS	72	63	67	57	71	63	62	73	64	59	57	54	56	60	58	65	75	68	73	79	92	88	85	75	66	67
	Markit iTraxx Asia ex-Japan 5Y CDS	100	101	113	90	115	107	100	116	109	102	107	109	110	116	113	144	147	123	131	147	159	151	147	146	139	140
	Markit iTraxx Australia 5Y CDS	81	83	89	79	98	93	91	101	93	81	88	89	91	102	100	114	126	115	124	134	151	143	139	136	126	125
Markit iTraxx Emerging Markets 5Y CDS		112	112	109	112	92	92	91	88	88	88	91	91	91	91	90	89	89	90	88	88	90	90	91	92	92	92

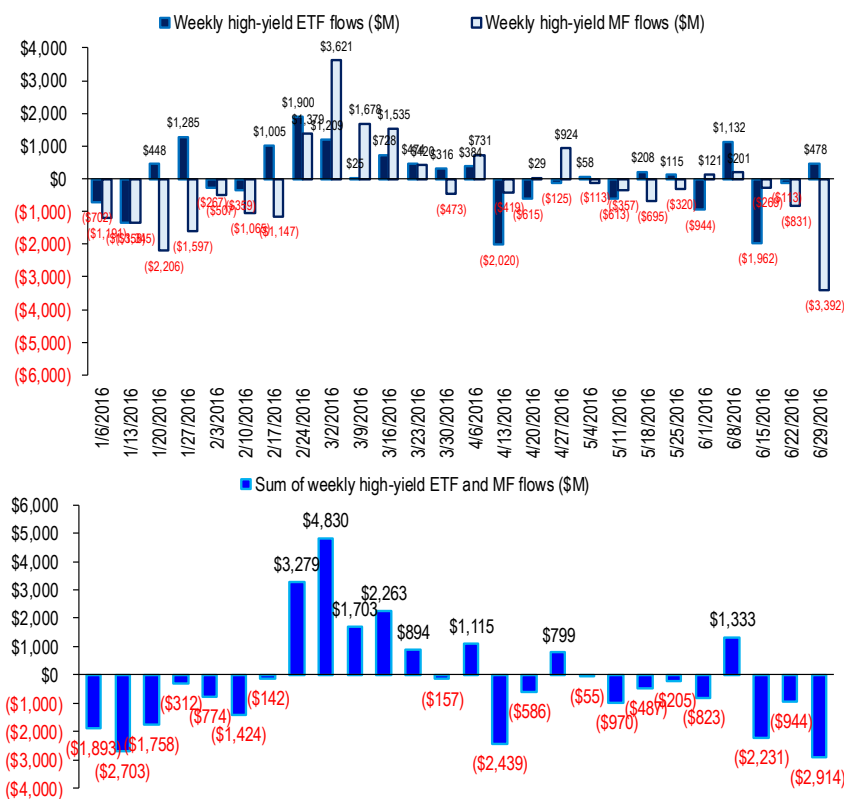
Source: Fundstrat, Bloomberg.

FUND FLOWS: High Yield sees biggest weekly outflow YTD (\$3B)...

High Yield outflows totaled nearly \$3B last week, which is the largest weekly outflow since thus far in 2016. Equities also saw another week of outflows, and the 4-week moving average sank further to \$6.7B.

Figure: High Yield had biggest weekly outflow 2016 (\$3B)

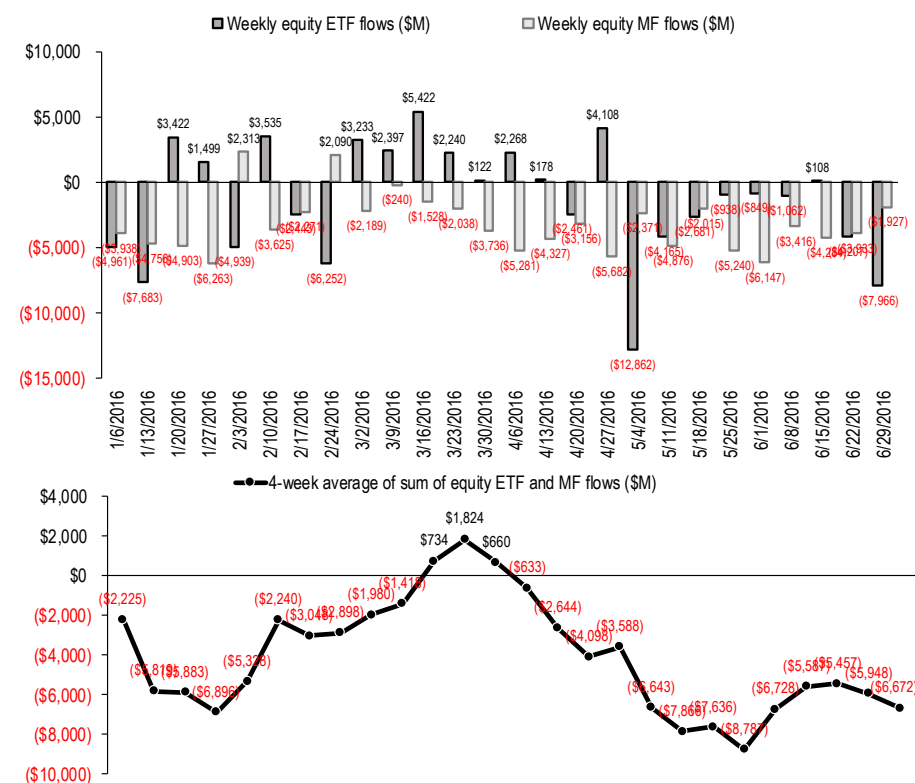
Weekly high yield ETF and MF fund flows since January 2016



Source: Fundstrat, ICI, Bloomberg. Note: ETF flows are HYG and JNK ETF fund flows.

Figure: Equity flows are persistently negative this year...

Weekly equity ETF and MF fund flows since January 2016



Source: Fundstrat, ICI, Bloomberg. Note: ETF flows are for the 25 largest equity ETFs.

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