

Strategy Flashcard

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S&P 500 to reach 2200 by 2016 end on a long expansionary cycle of moderate growth

2016 end target: 2200

2017 end target: 2400

Div Yld: 2%

	2014A	2015E	2016E
EPS	\$118	\$118	\$118
PE on yearend S&P targets	17.4	17.3	18.6
DPS	\$38	\$41	\$43
EPS/DPS growth	6%/6%	0%/7%	0%/5%

Quarterly EPS			
1Q14A	\$28.00	1Q15A	\$28.60
2Q14A	\$29.75	2Q15A	\$30.10
3Q14A	\$30.00	3Q15A	\$30.00
4Q14A	\$30.25	4Q15E	\$29.25

Reasons to still buy stocks:

- 1) ~2% US GDP likely in 2016
- 2) S&P EPS steady/higher despite \$/oil
- 3) PEs justifiable and been higher
- 4) Bond yields are nil after inflation

Dare to ask:

Why not 2500+ S&P cycle-high?
2500+ = 18x 2018E EPS \$140-145

S&P 500 avg. trailing 4qtr PE:

1960-2014	16.0
1985-2014	17.6
1995-2014	18.6
2005-2014	15.9

Sectors/Industries:

Health Care, Tech
Health Care, Tech, Consumer Disc.
Tech, Health Care, some Consumer
Big Banks, Mega-cap Tech
Tech, Health Care, some Consumer

Staples

Be selective and valuation mindful
Energy, Industrial Capital Goods

Market strategy and tactics:

Lower S&P returns than history likely, but still decent and few alternatives - stay involved, buy on dips

Consider lesson of 2014-2015: Interest rates stayed very low despite tighter labor market and initial Fed hike

Next 5%+ move is likely: **Up**

Risk of near-term correction: **Diminished**

"S&P PE stands on the shoulders of bonds."

Thematic and sector strategy:

Tilt toward:

- 1) Secular Growth Sectors - industries with strong sales growth in the middle of economic cycles
- 2) Sales Growth near 5% - industries not dependent on margin expansion to drive 5%+ EPS growth
- 3) High ROE or long competitive advantage - ability to defend ROE/margins amidst low interest rates
- 4) Dividend Growth - stocks with ability to significantly raise dividend payout ratios
- 5) Debt Capacity - companies that can issue cheap debt for acquisitions and share buybacks

Tilt away from:

- 1) Consumer companies w/tired brands or facing tough competition (seek unique products/experiences)
- 2) Smaller cap cyclical plays which are still expensive, prefer big-cap banks and select retailers
- 3) Commodity and industrial capital goods producers, prefer Transports

Risks:

- US tax on foreign profits, whether repatriated or not, threatens large multinationals and would cause margin contraction
- EM economy weakness that causes a steep decline in commodity prices, especially oil, and threatens US exports and investment spending
- A surge in long-term interest rates or any global economic shock would threaten our constructive view on the S&P for 2016

