

Our Goal: Exploiting The Gap Between Fundamental Reality And Market Perception

A Short-Horned Bull, With Limited Additional Upside In 2017



**Tobias Levkovich** <sup>AC</sup>  
Chief US Equity Strategist  
[tobias.levkovich@citi.com](mailto:tobias.levkovich@citi.com)  
212 816-1623

**Lorraine Schmitt**  
[lorraine.m.schmitt@citi.com](mailto:lorraine.m.schmitt@citi.com)  
212 816-1657

**Jennifer Stahmer**  
[jennifer.stahmer@citi.com](mailto:jennifer.stahmer@citi.com)  
212 816-8515

**See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures**

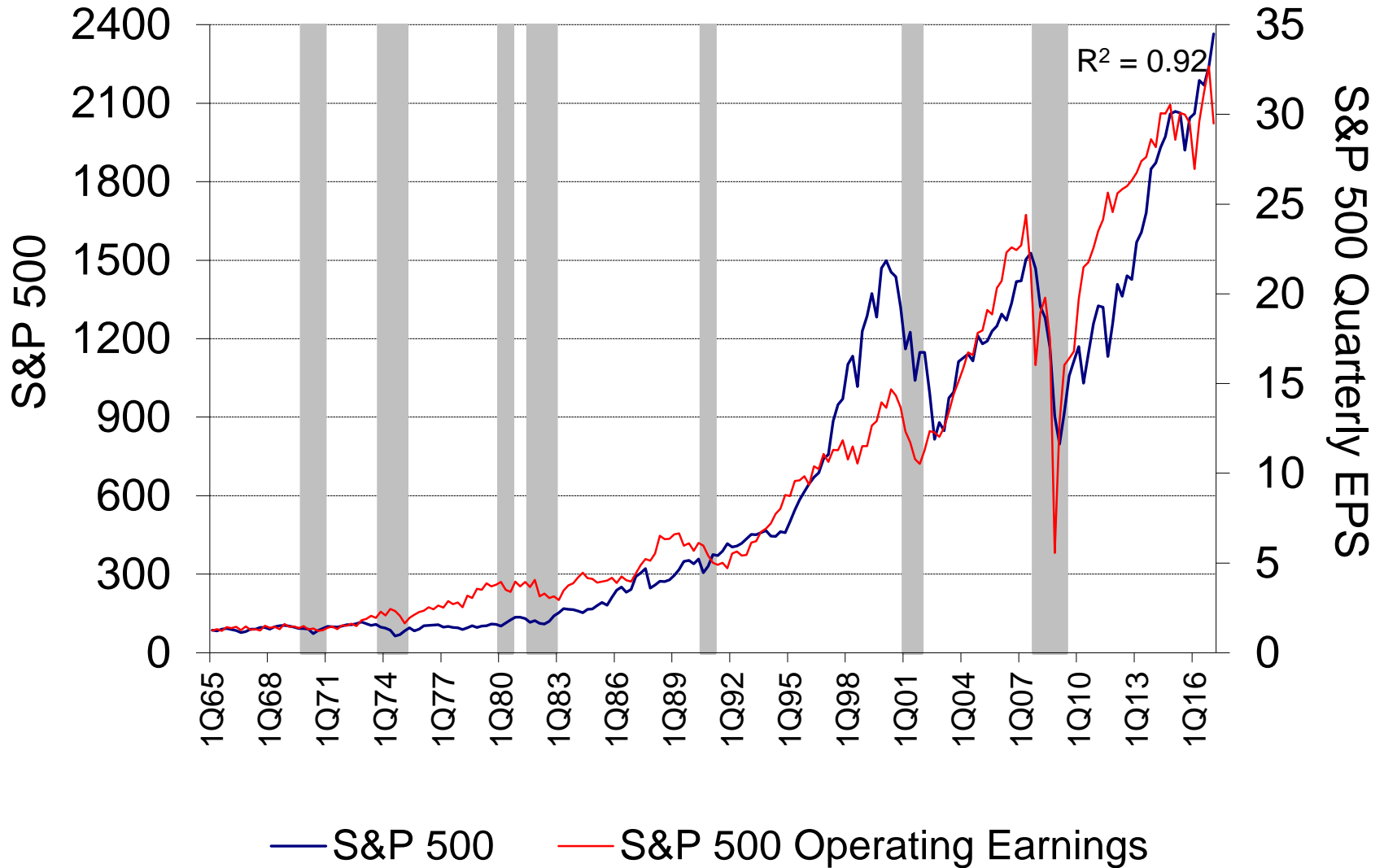
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This presentation was approved for distribution on 14 March 2017; the disclosures in Appendix A1 are current as of the same date.

- I. The rally is not about Trump hope
- II. Earnings have been and will be the driver
- III. Valuation is not as stretched as perceived
- IV. Sentiment is not all “bulled up”

# S&P 500 Performance vs Earnings

## S&P 500 vs S&P 500 EPS



Source: Thomson Reuters, Haver Analytics and Citi Research - US Equity Strategy

# S&P 500 Price Targets and Earnings

## S&P 500 Price Targets

	2013	2014	2015	2016	2017E <sup>1</sup>
S&P 500	1,848	2,059	2,044	2,239	2,425
DJIA	16,577	17,823	17,425	19,763	21,000

Source: Citi Research – U.S. Equity Strategy

<sup>1</sup>2017 target introduced on 9/2/2016 and raised on 12/22/16.

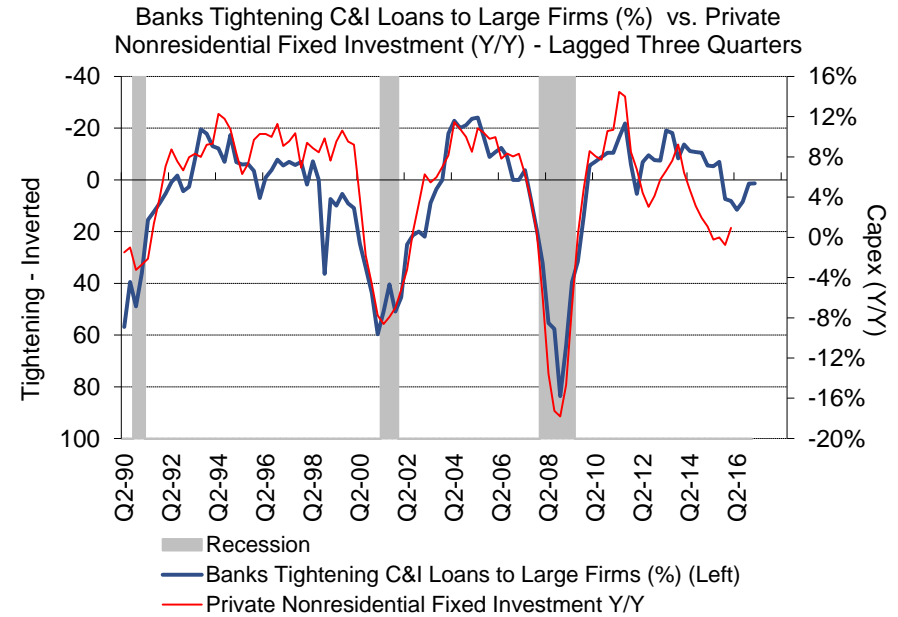
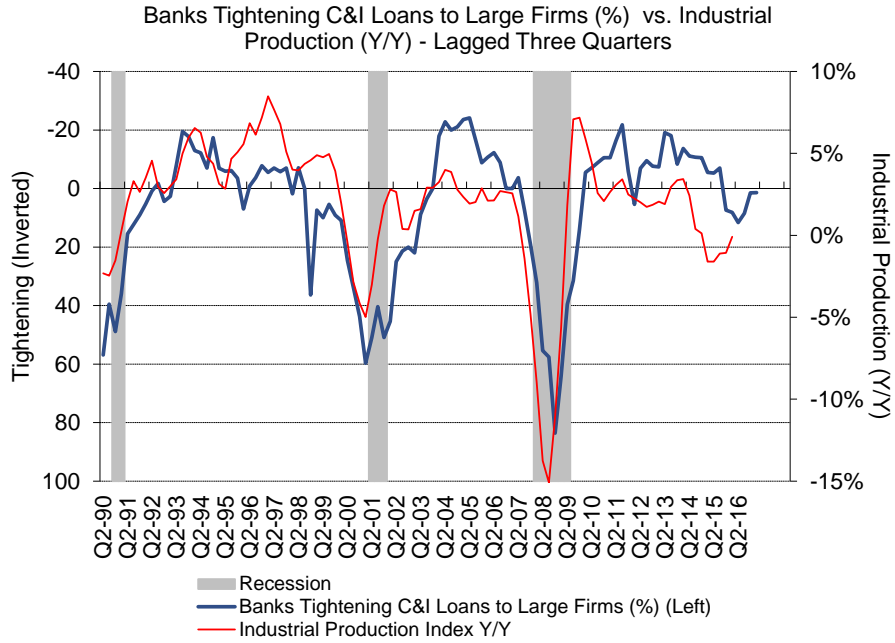
## S&P 500 EPS Estimates

	2013	2014	2015	2016E	2017E	2018E
S&P 500 Operating EPS Estimate	\$110.39	\$118.83	\$118.20	\$120.50	\$131.00	\$146.00
Y/Y Change	6.39%	7.6%	-0.5%	1.9%	8.7%	11.5%

Source: Citi Research – U.S. Strategy

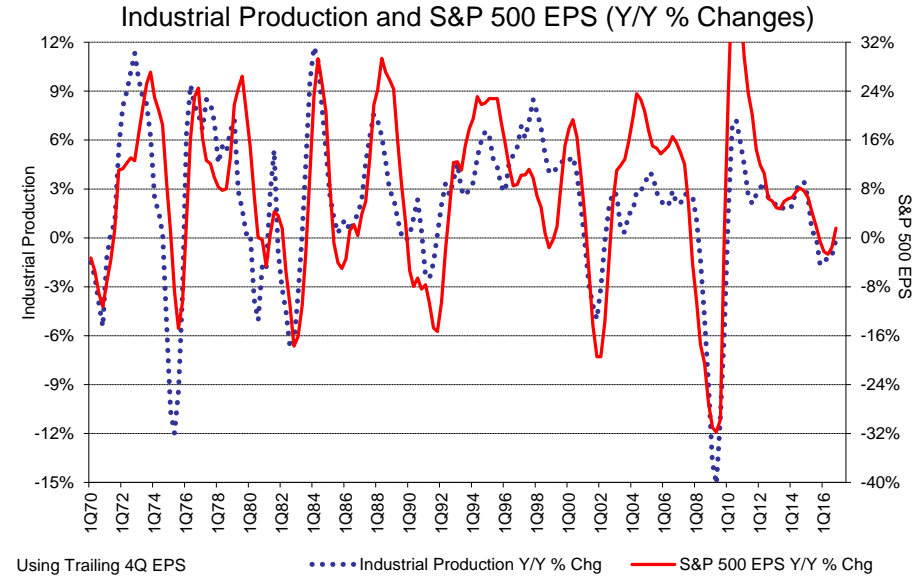
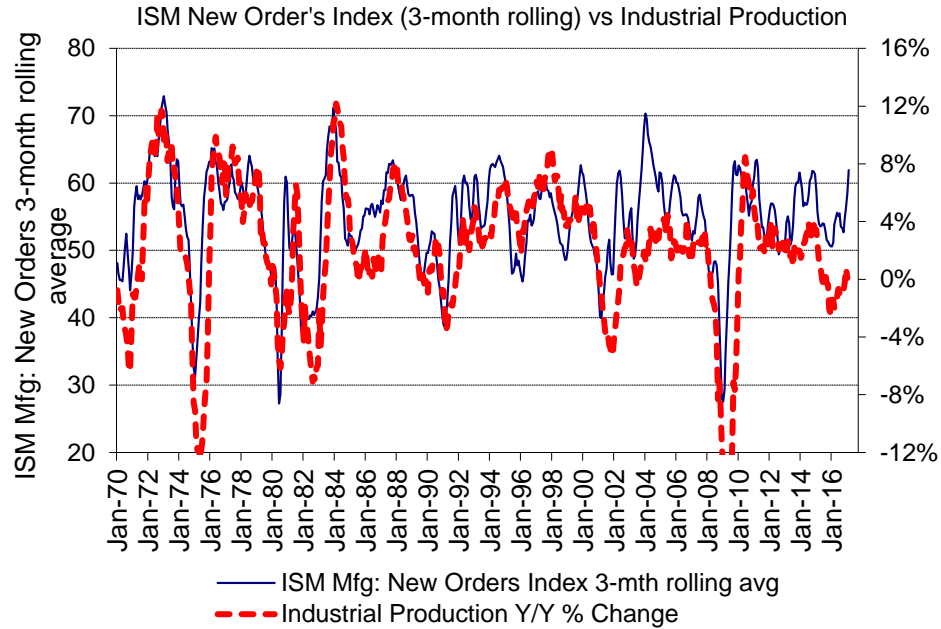
2016 forecast introduced on 3/6/15 and reduced on 6/19/15, 9/4/15, 12/18/15, 1/14/16, 3/11/16, 6/17/16, 9/2/16 and again on 12/22/16. 2017 forecast introduced on 3/11/16, lowered on 9/2/16 and raised on 12/22/16. 2018 forecast introduced on 12/22/16.

# Economy Tied to Credit



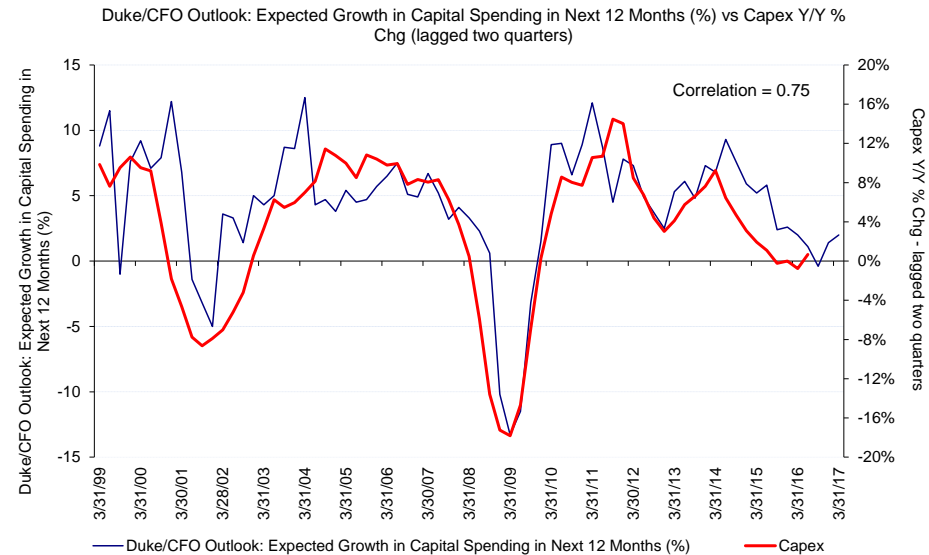
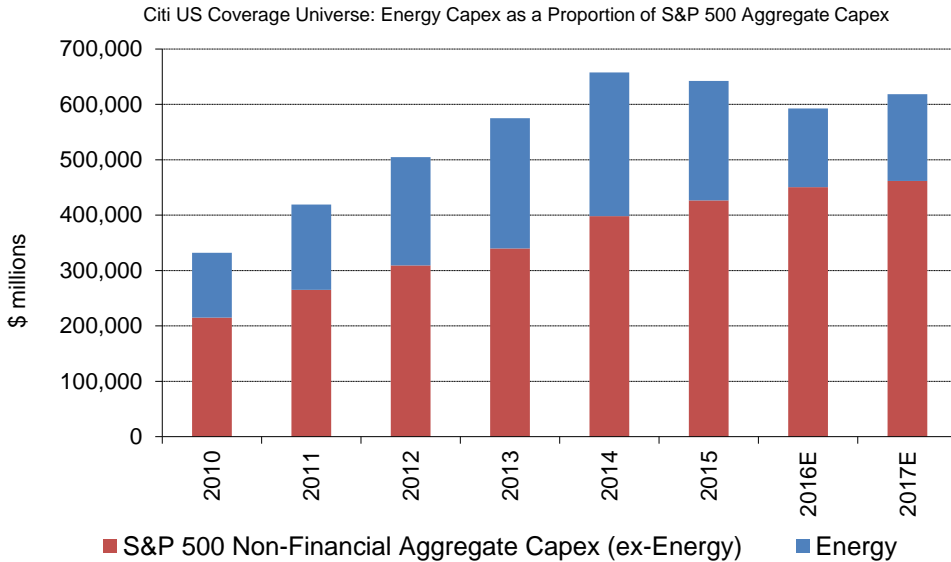
Source: Haver Analytics and Citi Research – U.S. Equity Strategy

# Economic & Earnings Backdrop



Source: Haver Analytics and Citi Research – U.S. Equity Strategy

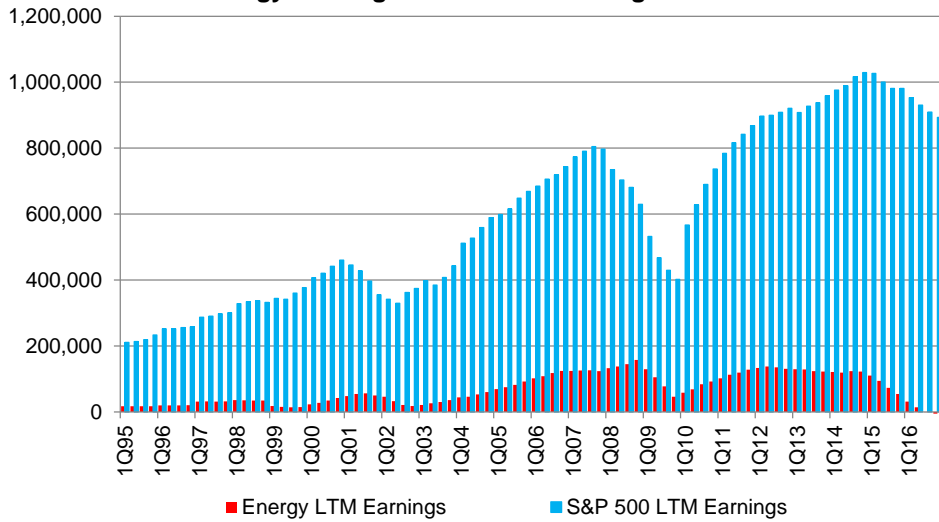
# Economic & Earnings Backdrop



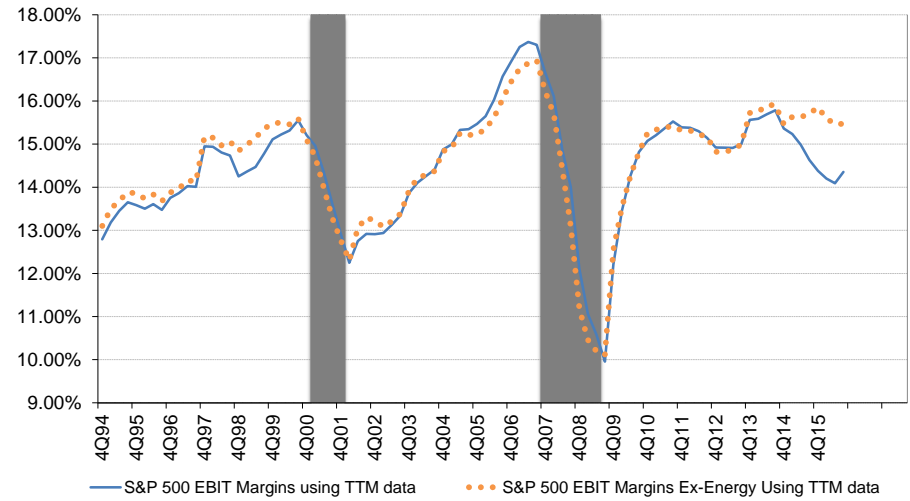
Source: dataCentral, Haver Analytics and Citi Research – U.S. Equity Strategy

# Earnings Conviction

**Energy Earnings vs S&P 500 Earnings \$ millions**



**S&P 500: EBIT Margins vs EBIT Margins Ex-Energy using TTM data**

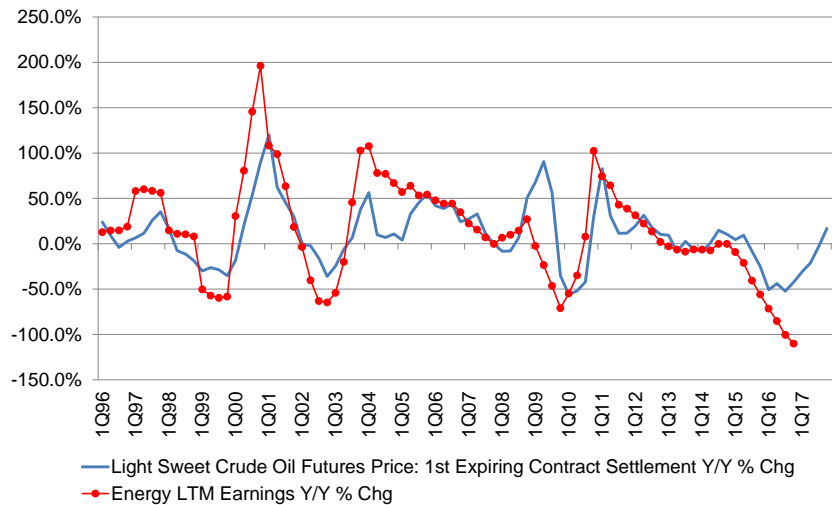


Source: FactSet, Haver Analytics and Citi Research – U.S. Equity Strategy

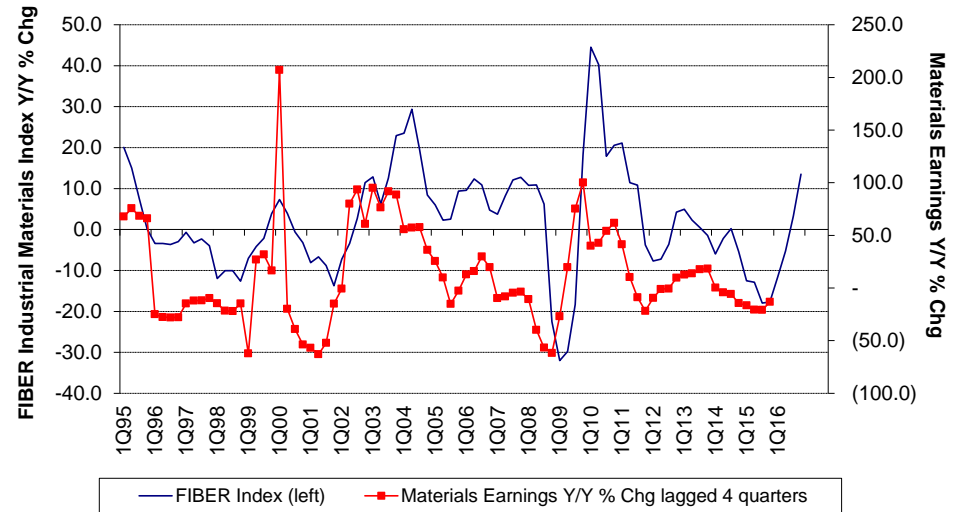


# Earnings Conviction

**Crude Oil Futures vs Energy LTM Earnings (lagged four quarters)**

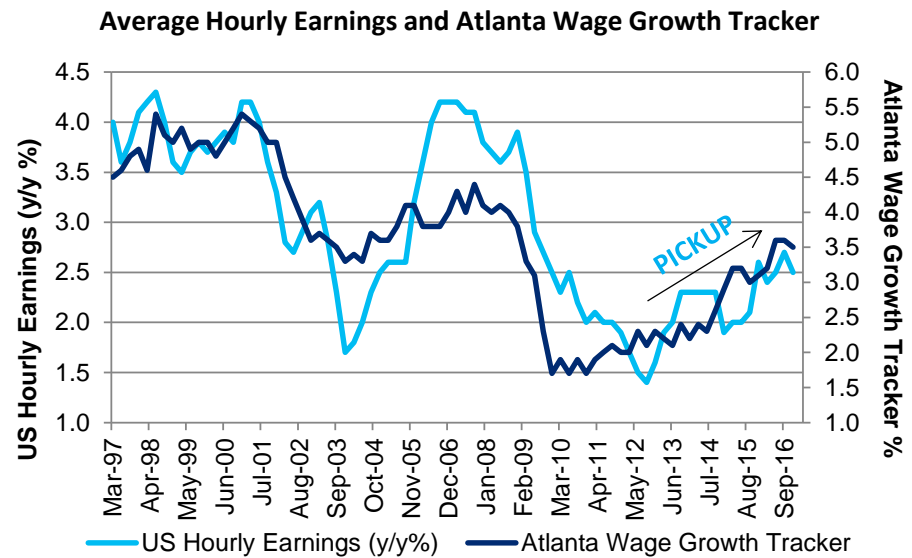
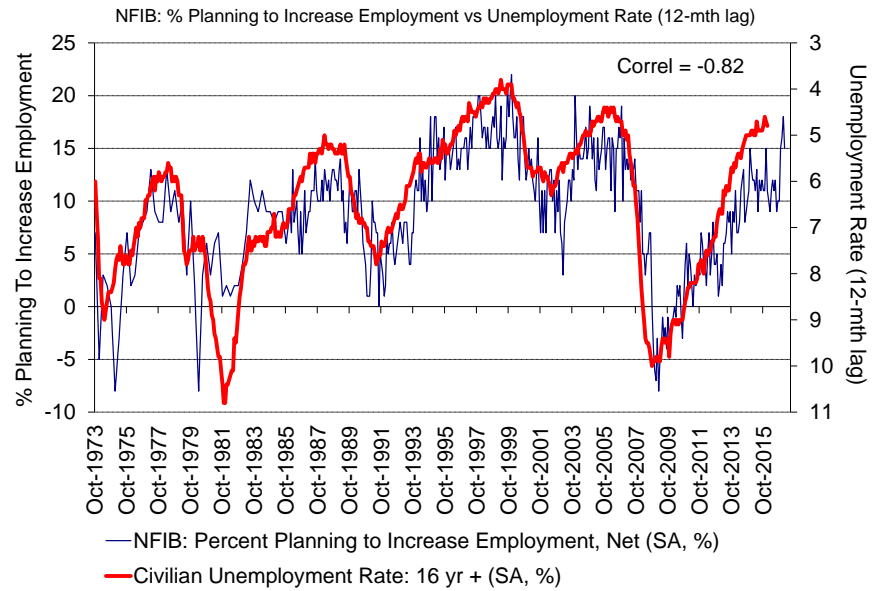


**FIBER Industrial Materials Index vs Materials Earnings (lagged four quarters)**



Source: FactSet, Haver Analytics and Citi Research – U.S. Equity Strategy

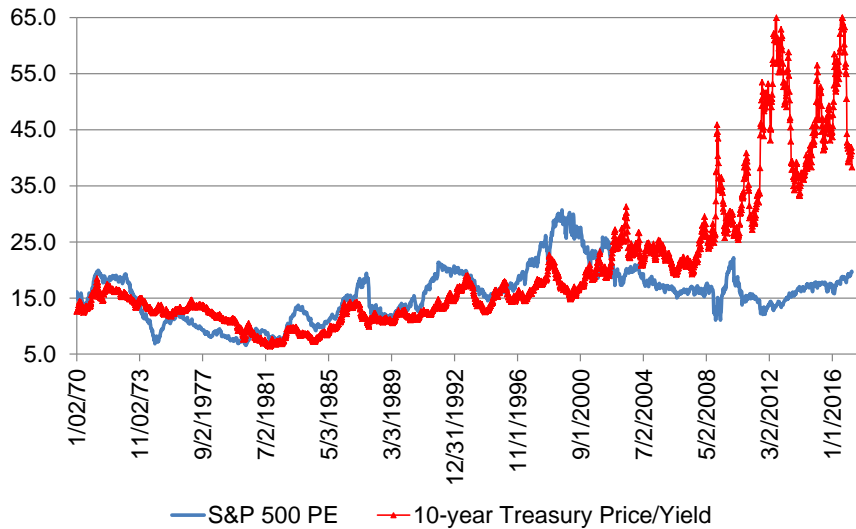
# A Consumer Kick



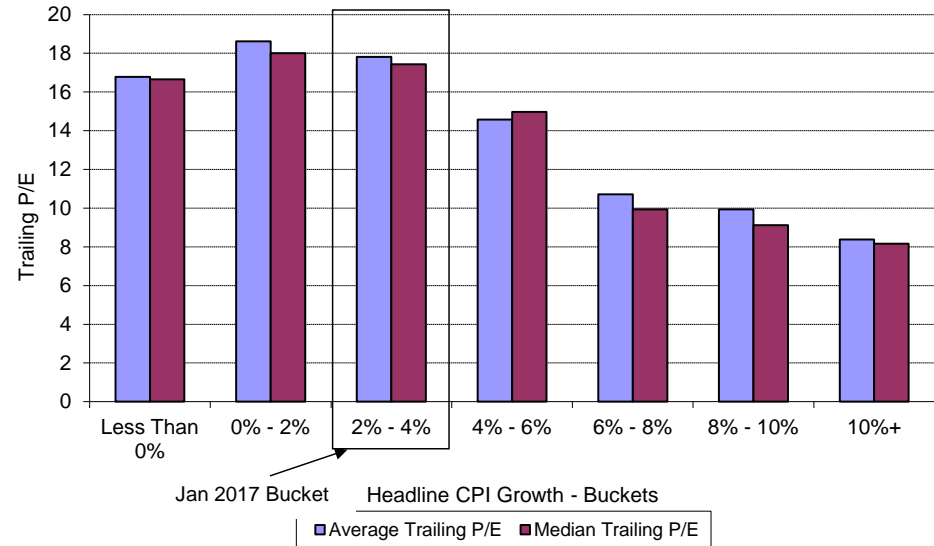
Source: Bloomberg, Haver Analytics and Citi Research – U.S. Equity Strategy

# Valuation Concerns Are Overdone

**S&P 500 Trailing PE vs 10-year Price/Yield**



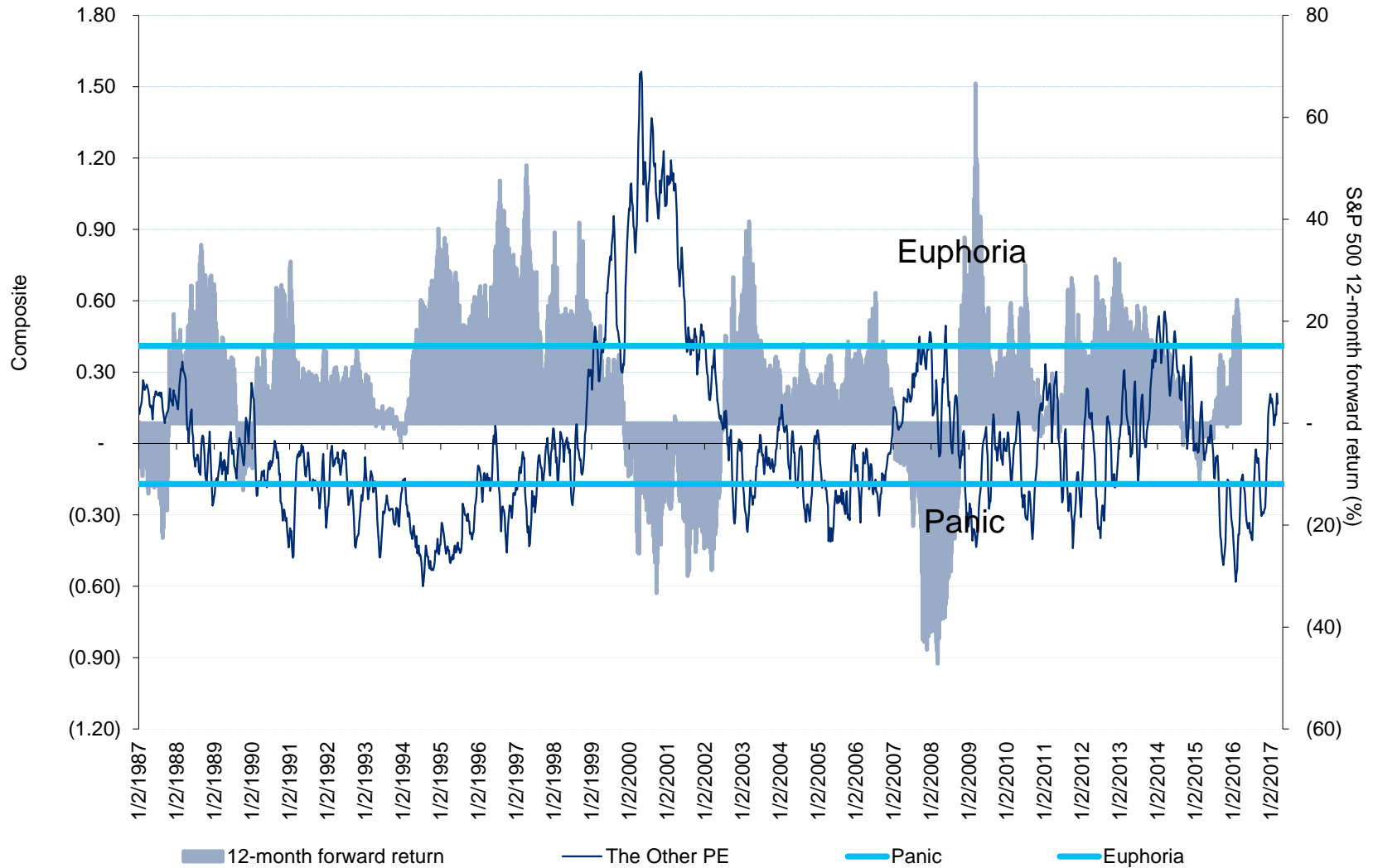
**Trailing P/E Average vs Buckets of CPI Growth**



Source: FactSet, Haver Analytics and Citi Research – U.S. Equity Strategy

# Neutral Sentiment

## The Panic/Euphoria Model (Other PE)<sup>SM</sup>

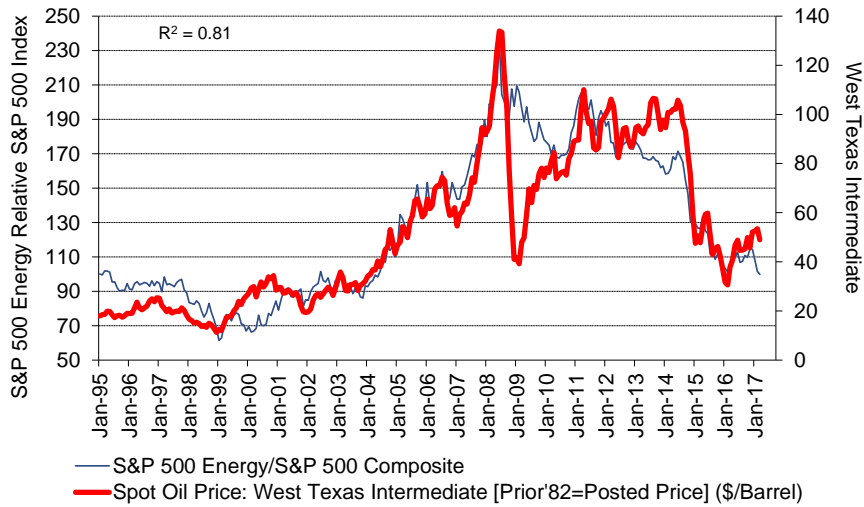


- VIX tells us very little about future stock price direction

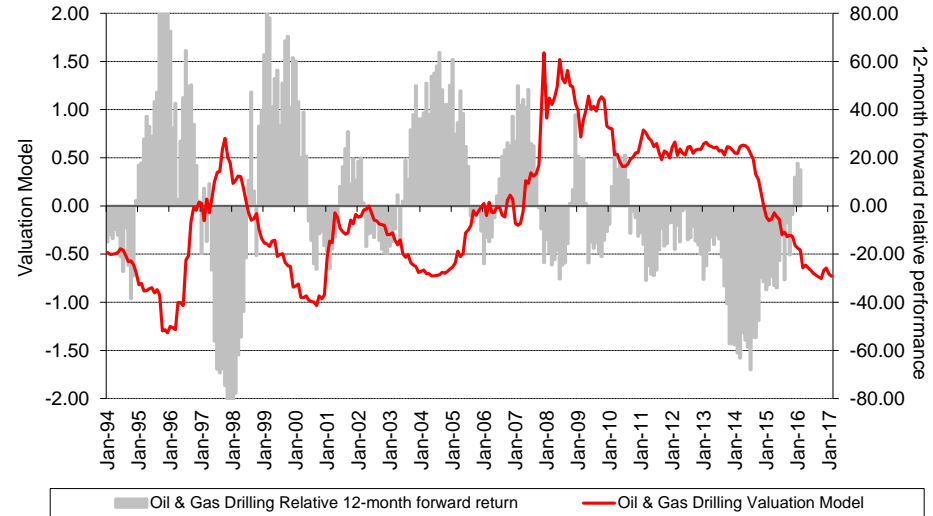
Source: Bloomberg, FactSet, Haver Analytics and Citi Research – U.S. Equity Strategy

# Theme: Energy Upside

Relative S&P 500 Energy vs West Texas Intermediate

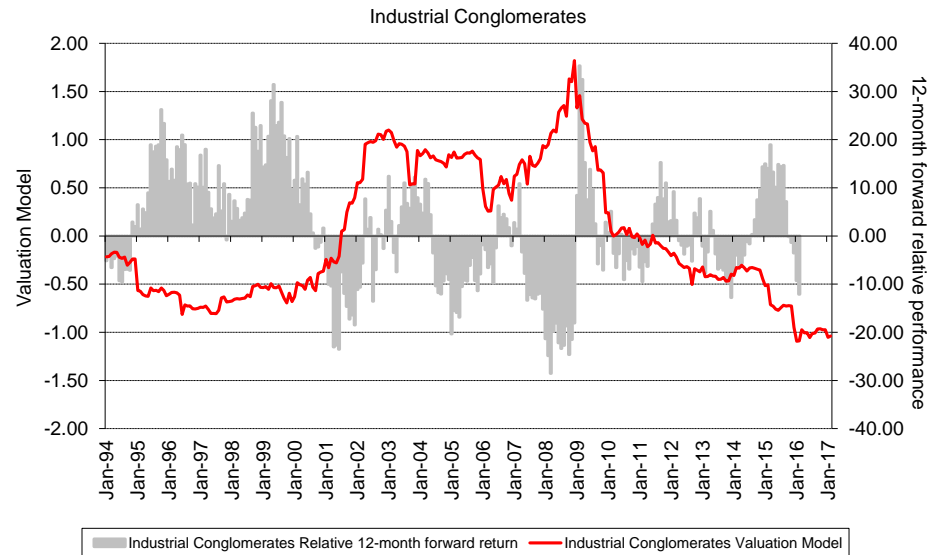
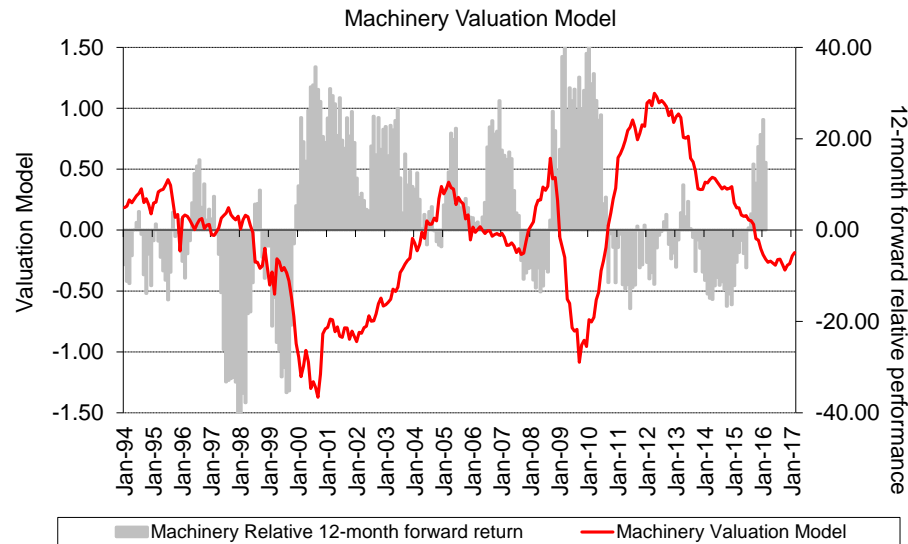


Oil & Gas Drilling Valuation Model



Source: Bloomberg, FactSet, Haver Analytics and Citi Research – U.S. Equity Strategy

# Capex Beneficiaries

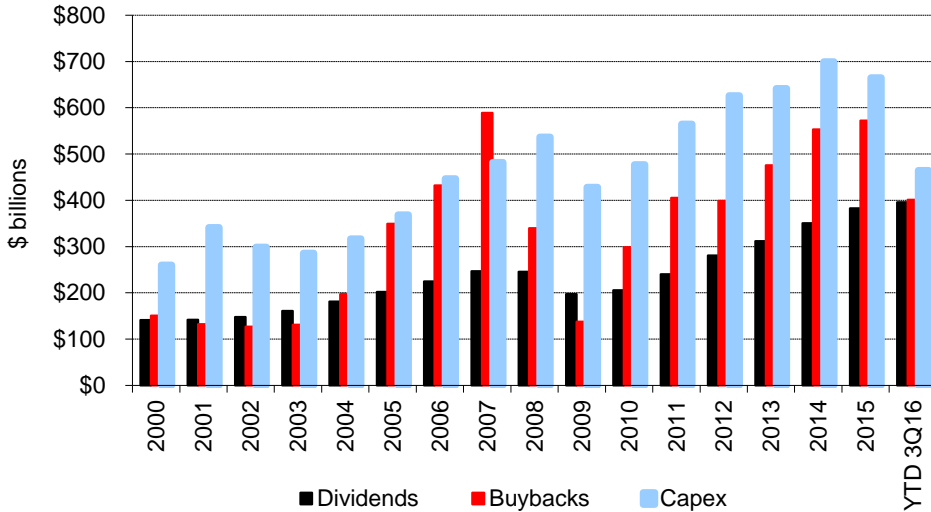


- IT stocks appear overvalued in many instances.

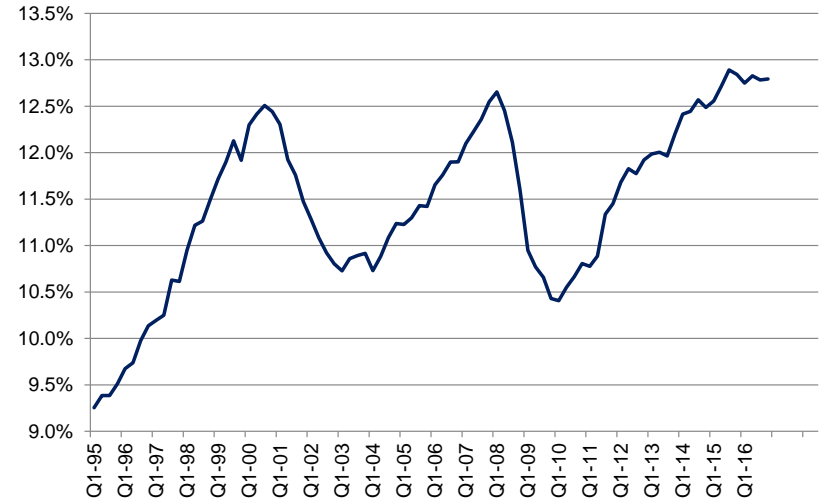
Source: Bloomberg and Citi Research – U.S. Equity Strategy

# Capex Myths Debunked

S&P 500 Uses of Cash



Real Private Nonresidential Fixed Investment ex Real Energy Spending % GDP



- Energy capex did fall from 1.05% of GDP in 2014 to 0.30% recently but is now poised to rebound.

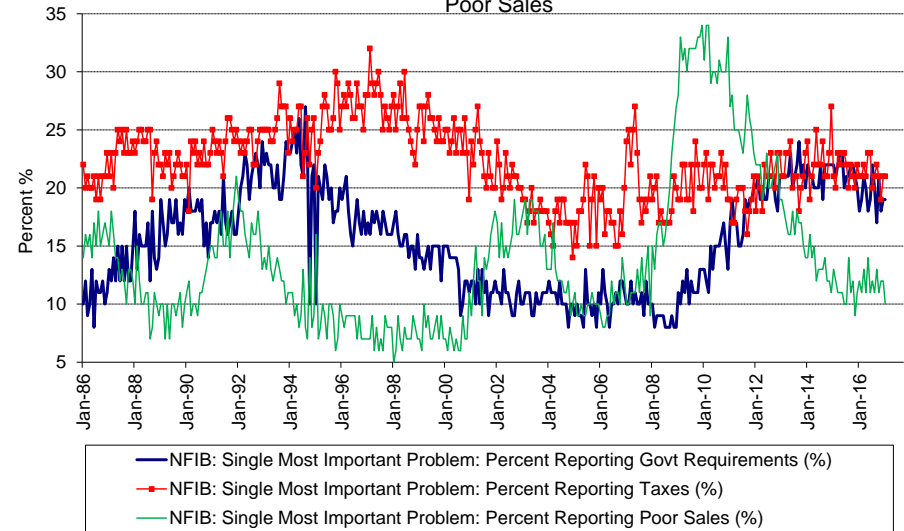
Source: FactSet, Haver Analytics and Citi Research – U.S. Equity Strategy

# The Trump "Hope" Aspect That Is Real (not Fake News)

### NFIB Small Business Optimism Index



### NFIB: Single Most Important Problem: Govt Requirements, Taxes, and Poor Sales



Source: Haver Analytics and Citi Research – U.S. Equity Strategy



# Risks to the Outlook

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- I. Geopolitics
- II. Central Bank Policy Errors
- III. Trade Protectionism
- IV. Small Business Does Not Embrace “Animal Spirits”
- V. Risk Premiums Stay Elevated
- VI. Higher Interest Rates Restrain Certain Parts of the Economy (housing, autos, etc.)

# Appendix A-1

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65%	61%	60%	72%	63%	50%

### Catalyst Watch

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