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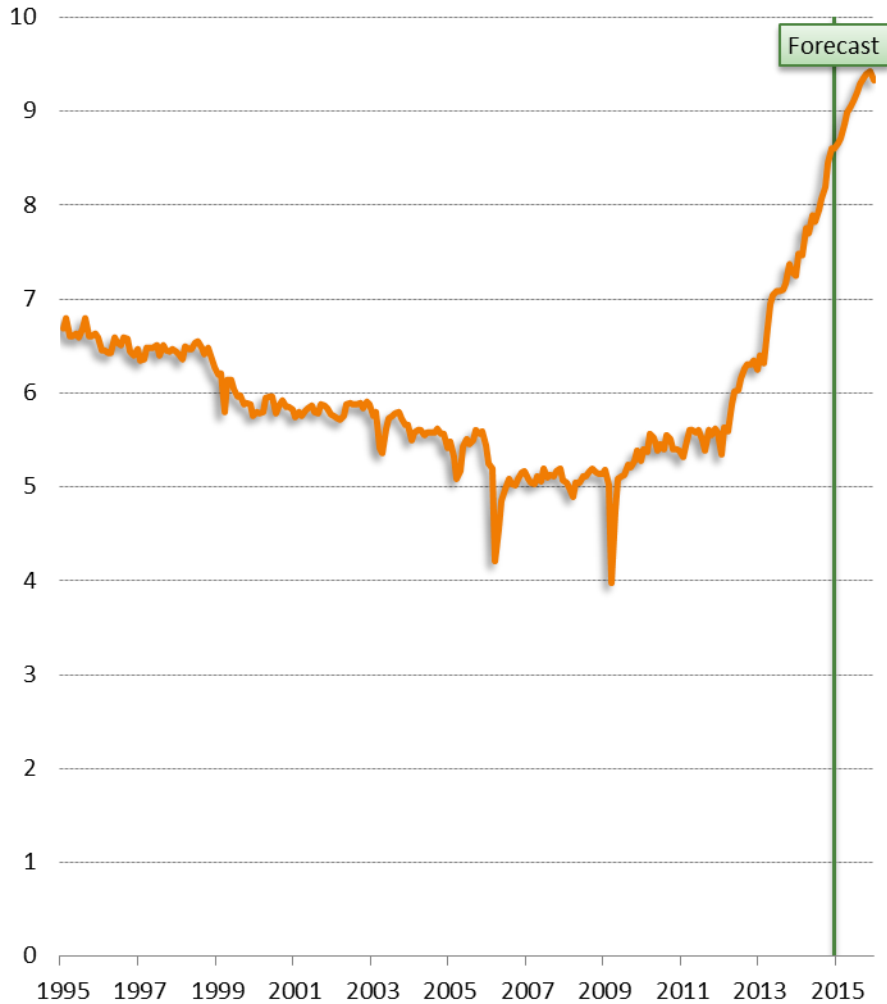
Rob Ginsberg | [Rginsberg@renmac.com](mailto:Rginsberg@renmac.com) | 212.537.8819

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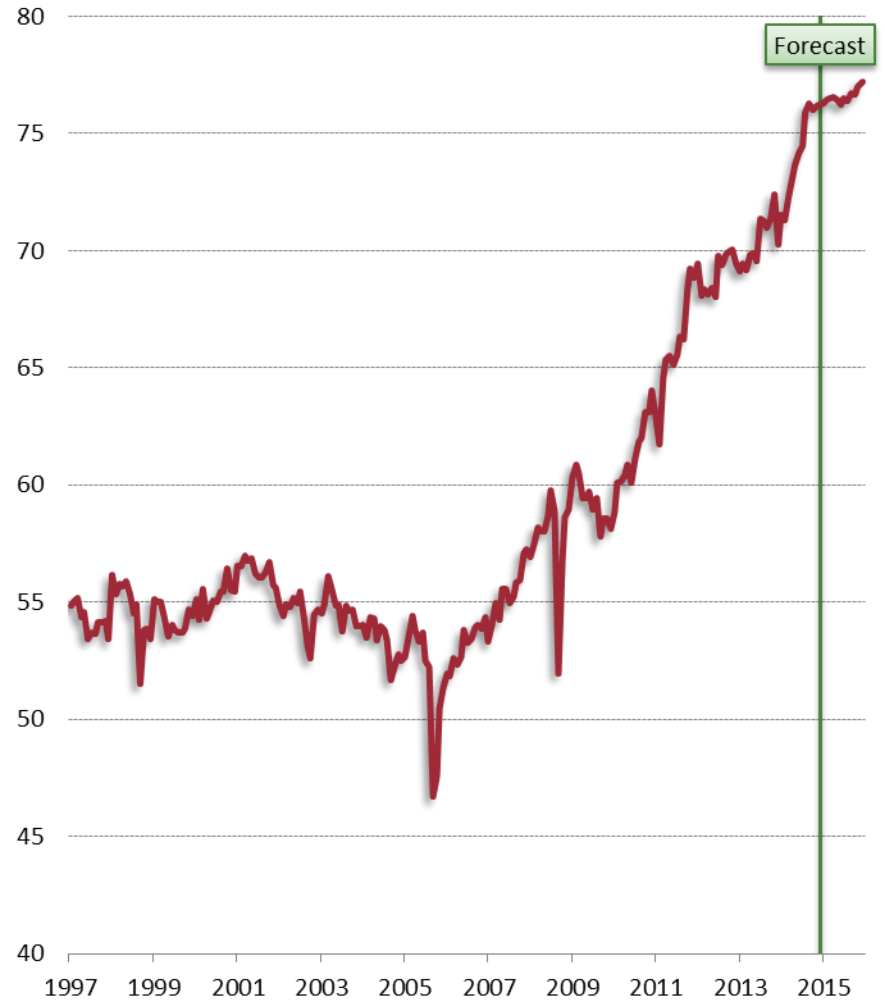
Kim Wallace

- ❖ U.S. growth allows DC to continue retreat from extraordinary policy and increase sector focus
- ❖ Late December agenda and vote outcomes set a low DC risk profile managed from the top down
- ❖ President Obama focused on international and environmental priorities
- ❖ Congressional parties will seek to differentiate from Obama without inviting crisis
- ❖ Ex-U.S. macroeconomic and geopolitical challenges present largest policy risks

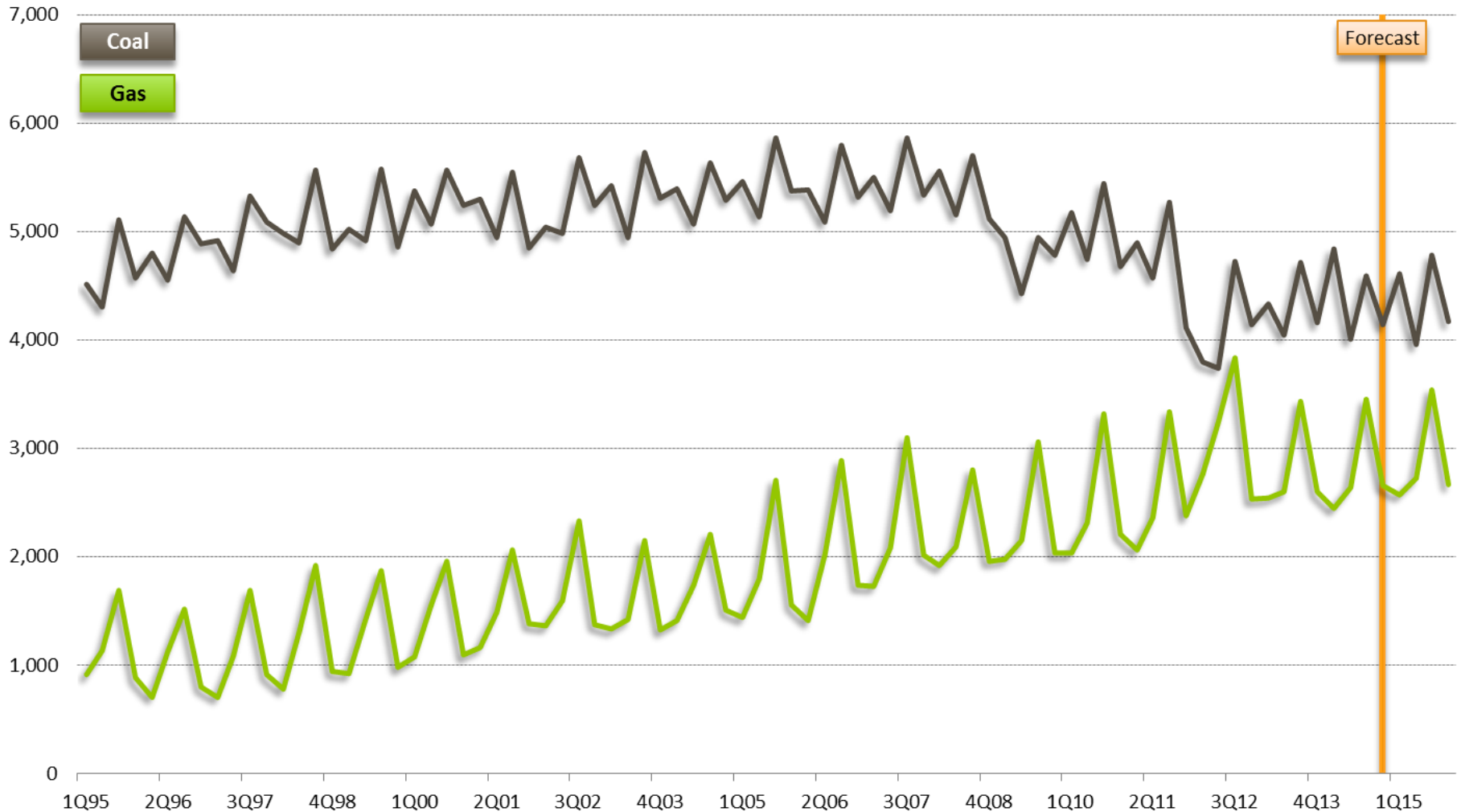
### U.S. Crude Oil Production (mmb/d)



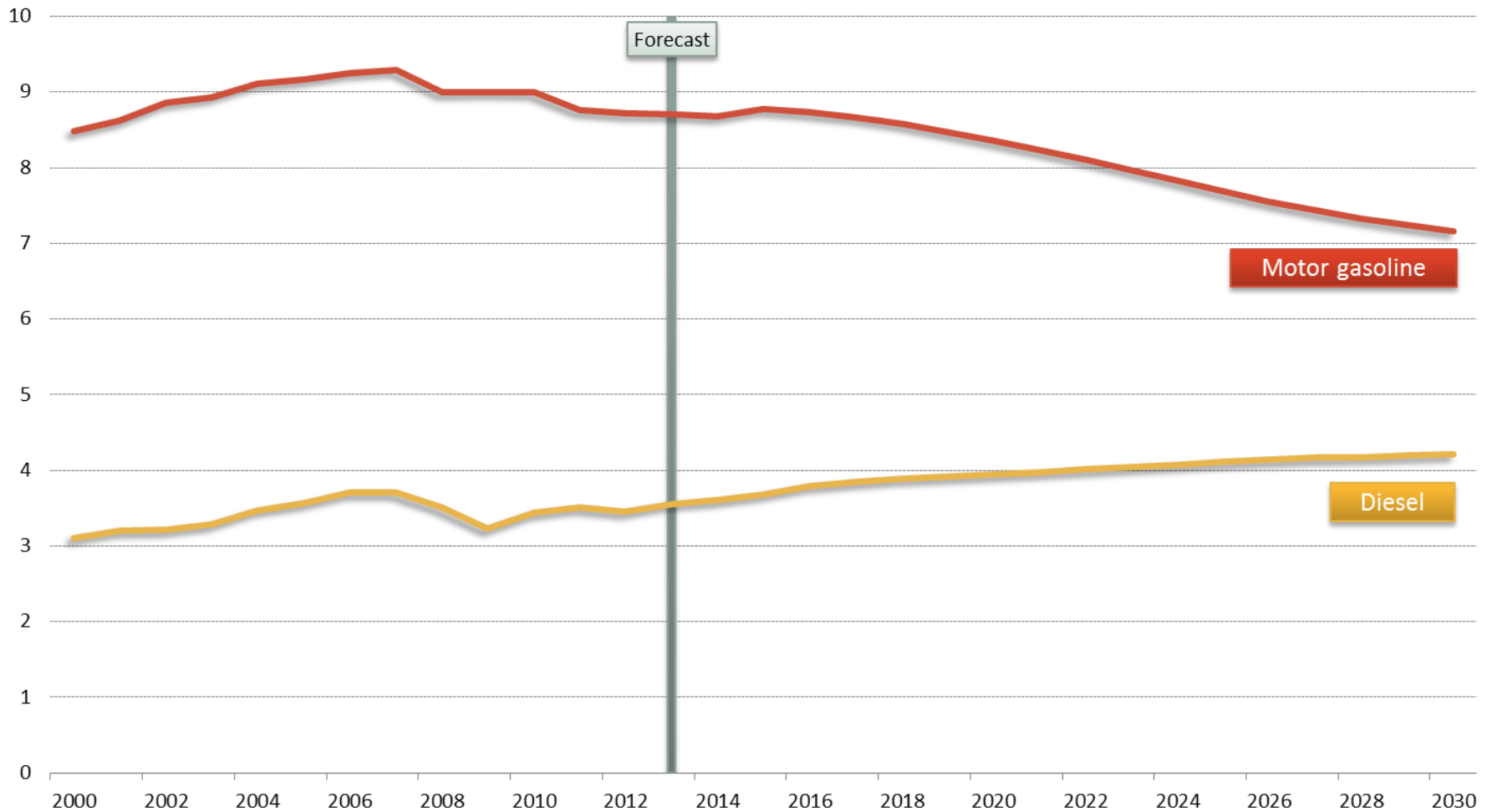
### U.S. Natural Gas Production (bcf/d)



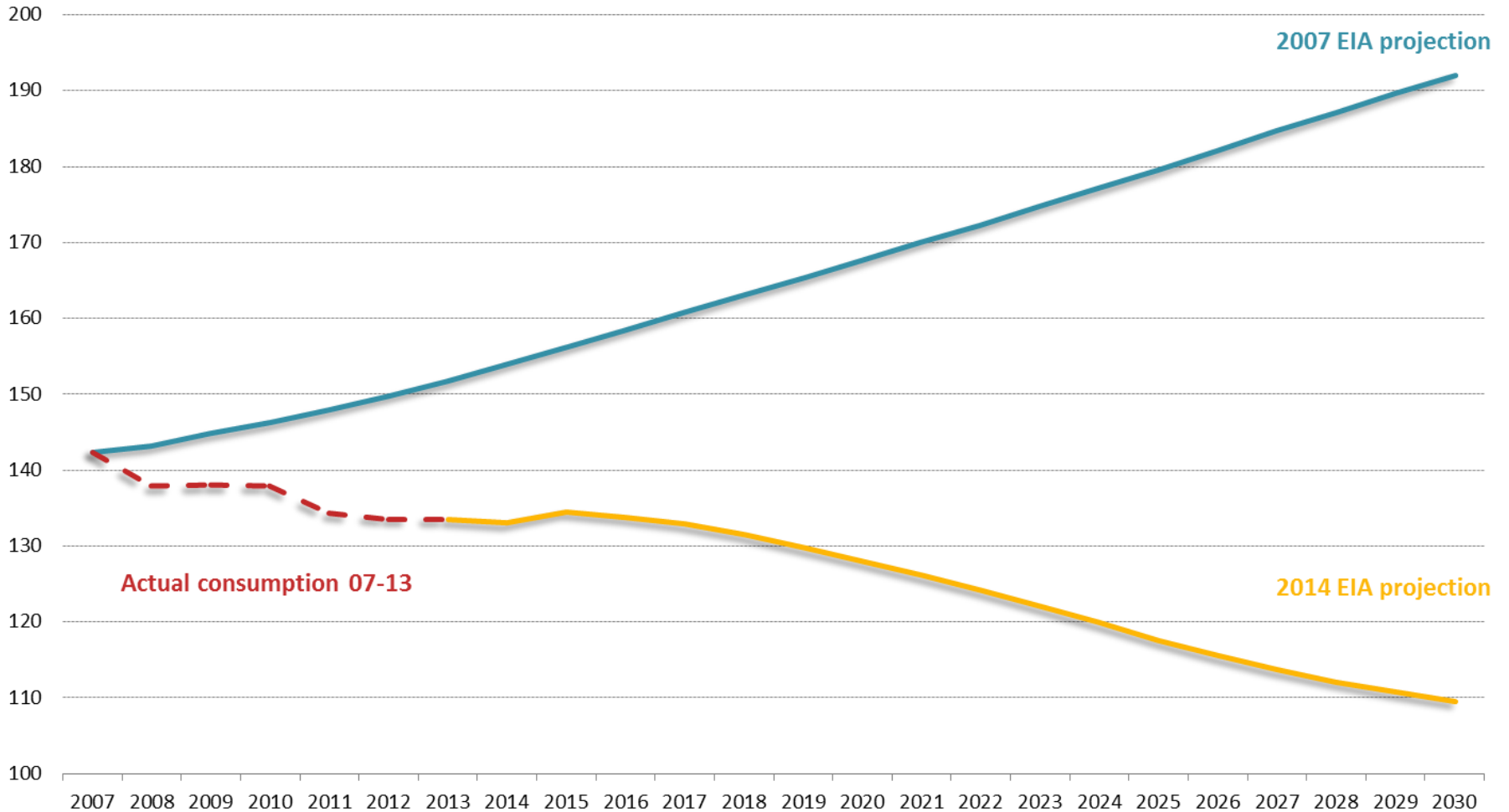
**U.S. Electric Power Generation by Source (000 mw/h)**



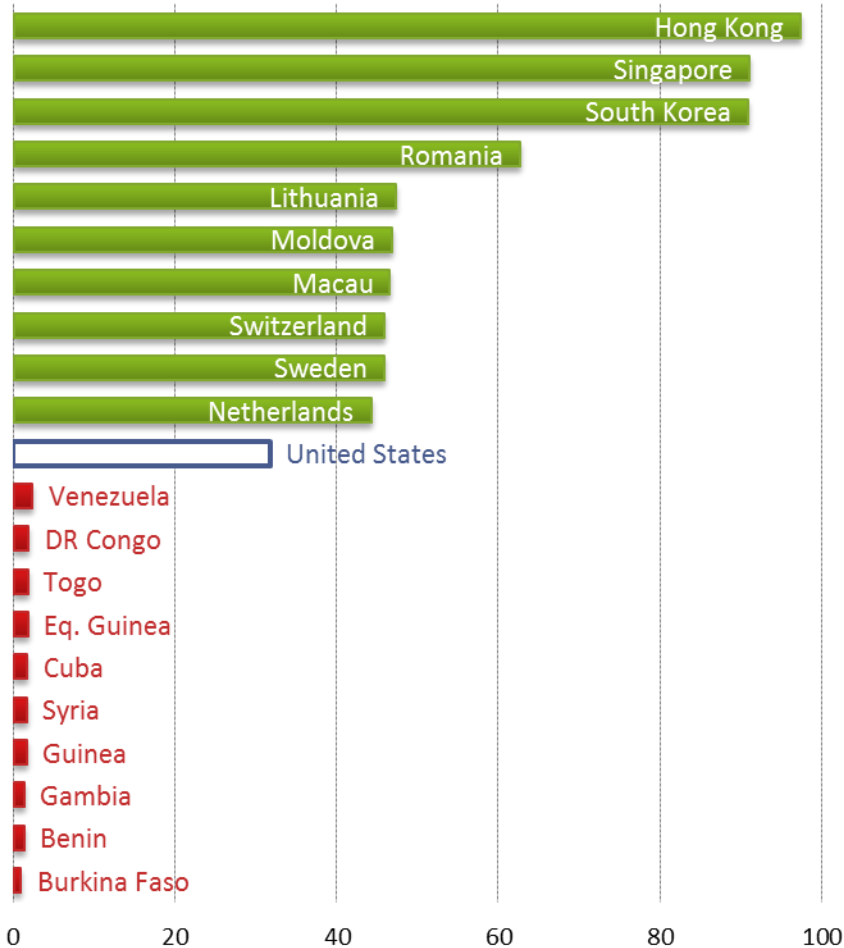
**Gasoline & Diesel Use (million barrels)**



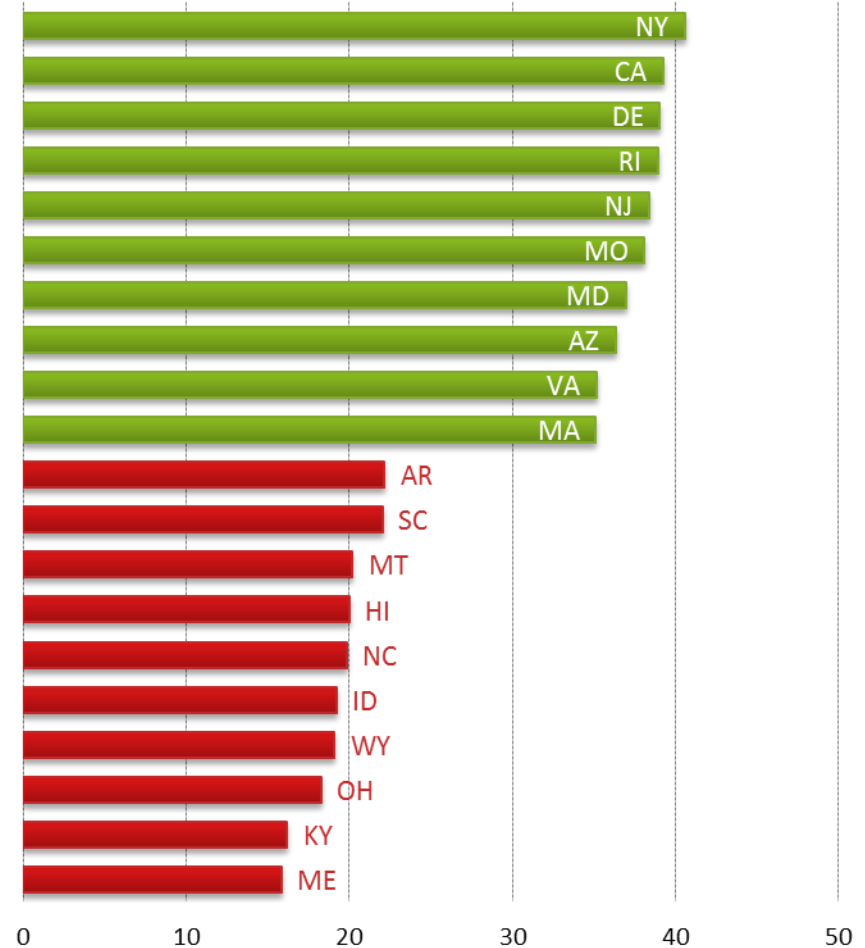
Consumption of Blended Gasoline (billion gallons)



**Top 10 / Bottom 10 Countries, Average Download Speed (Mbps)**

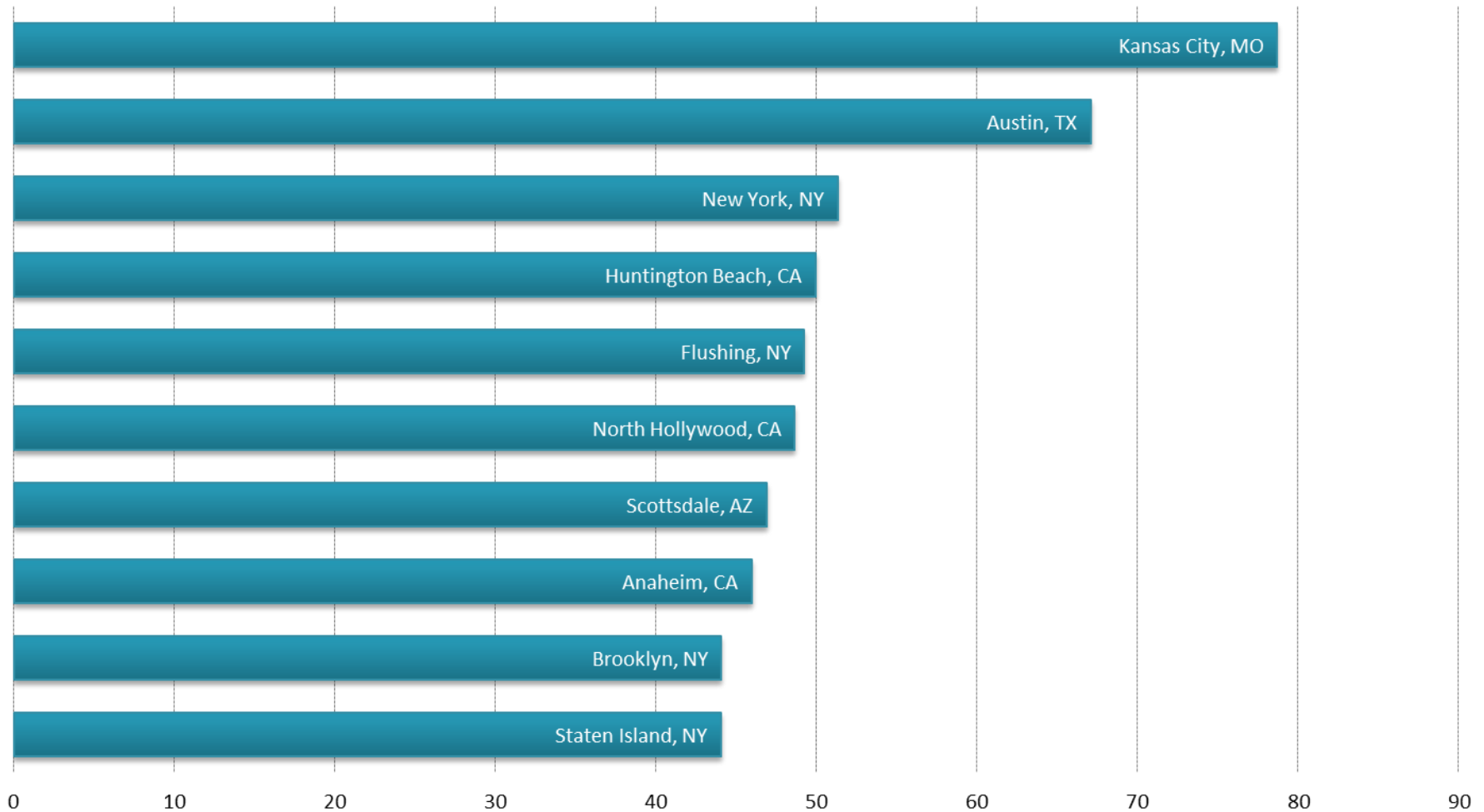


**Top 10 / Bottom 10 U.S. States, Average Download Speed (Mbps)**

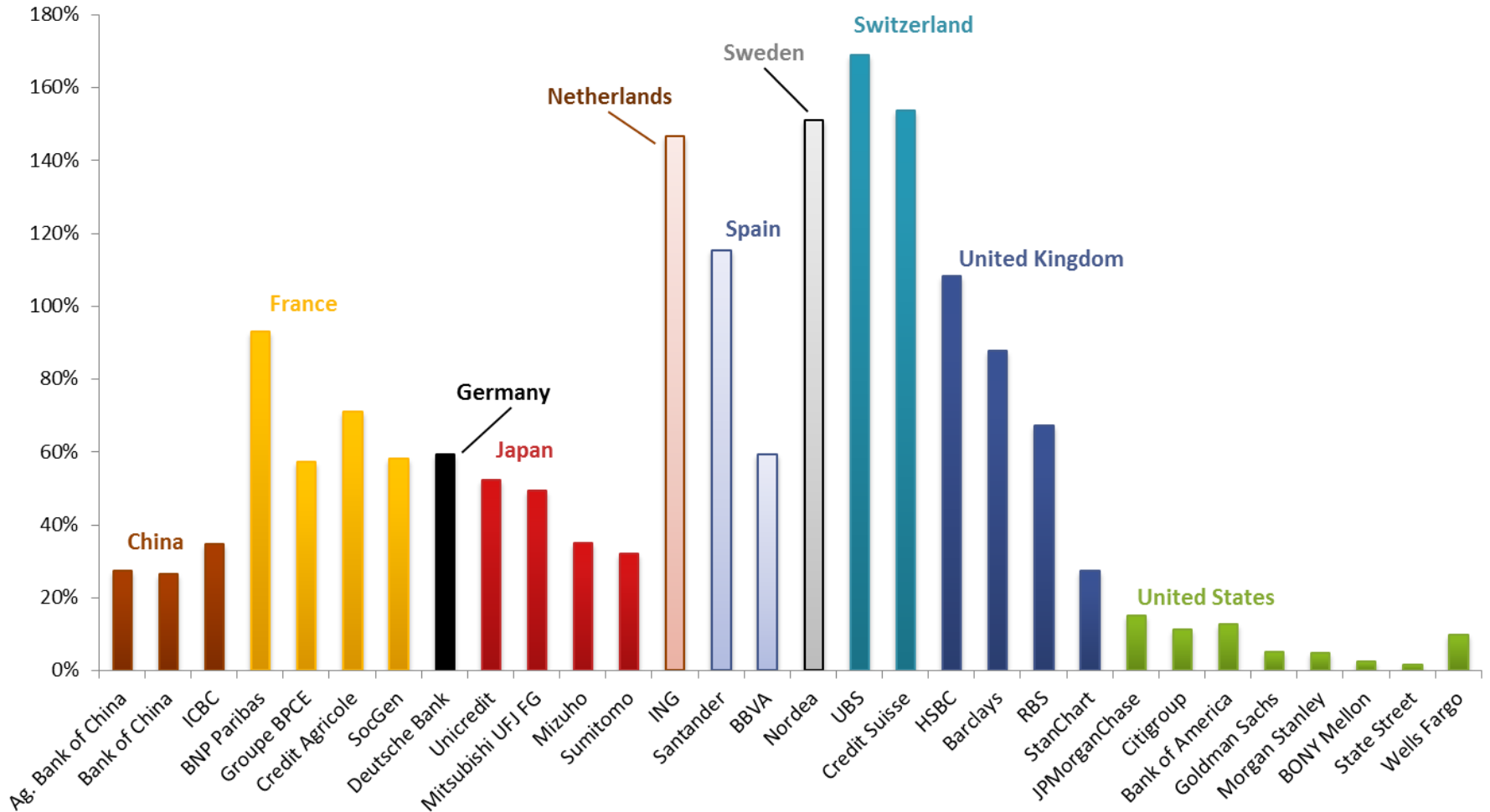




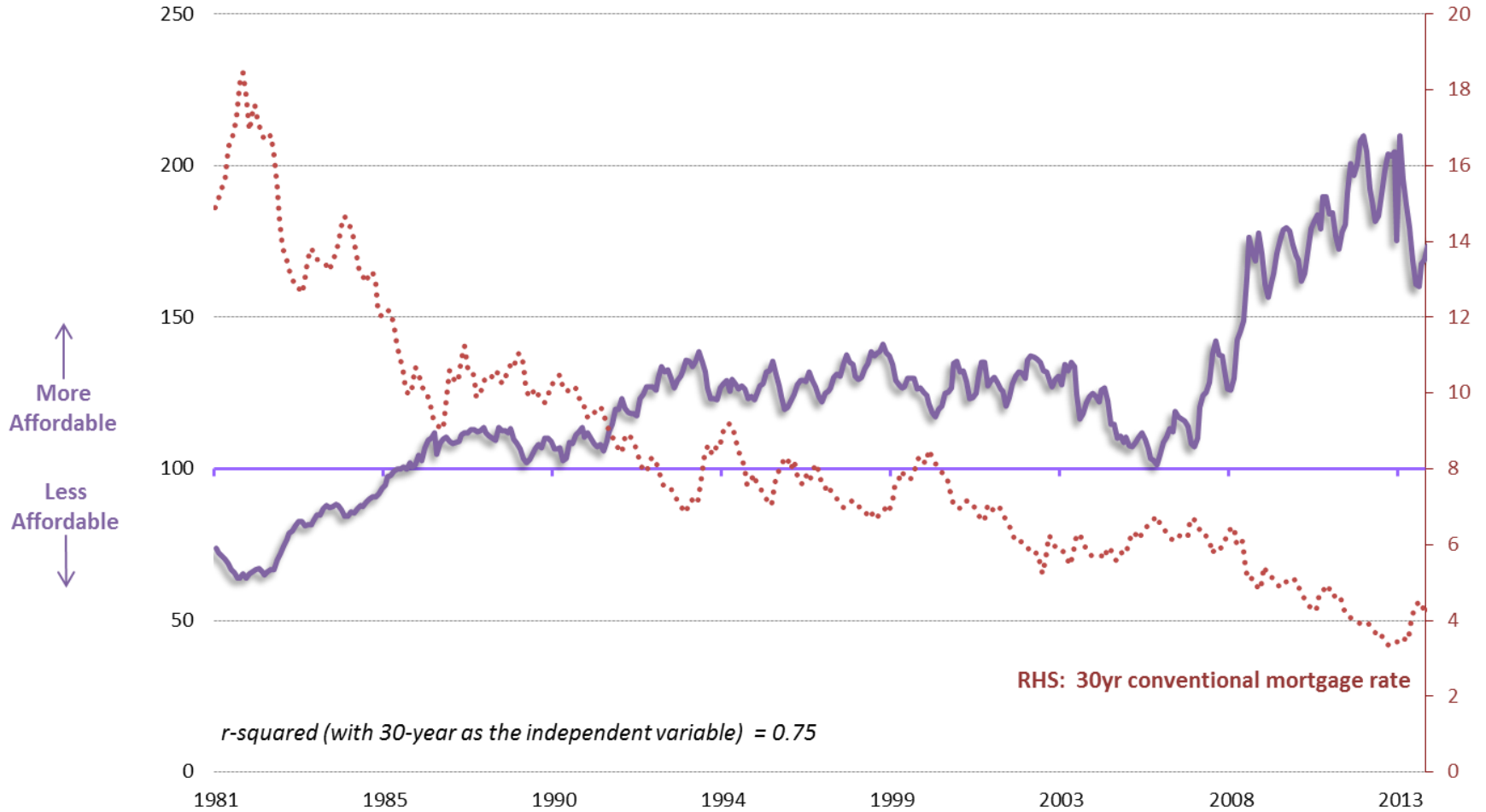
**Top 10 U.S. Cities, Average Download Speed (Mbps)**



**G-SIBs Total Assets (% home country GDP)**

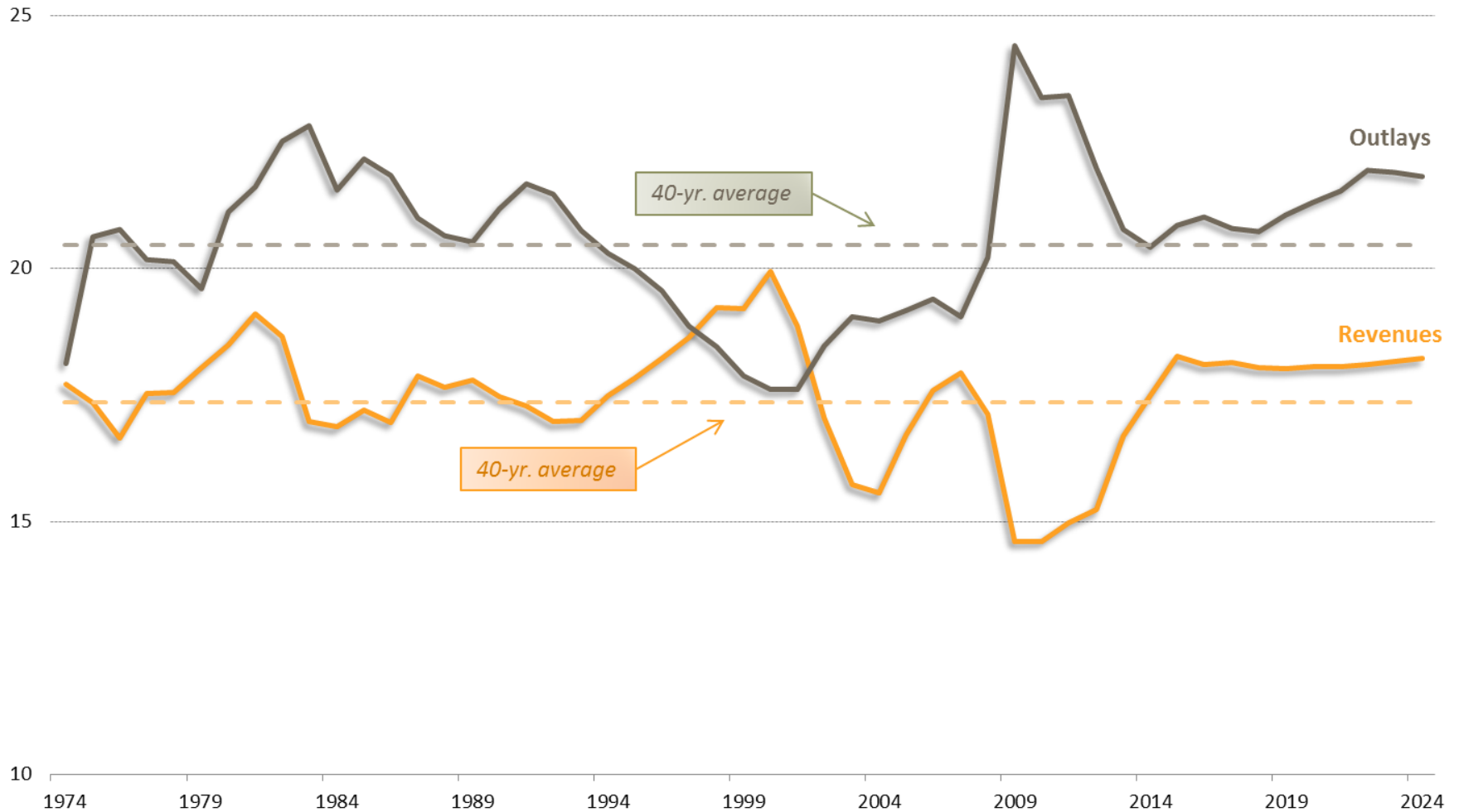


**Housing Affordability Index (Composite)**  
*Jan. 1981 - Oct. 2014*

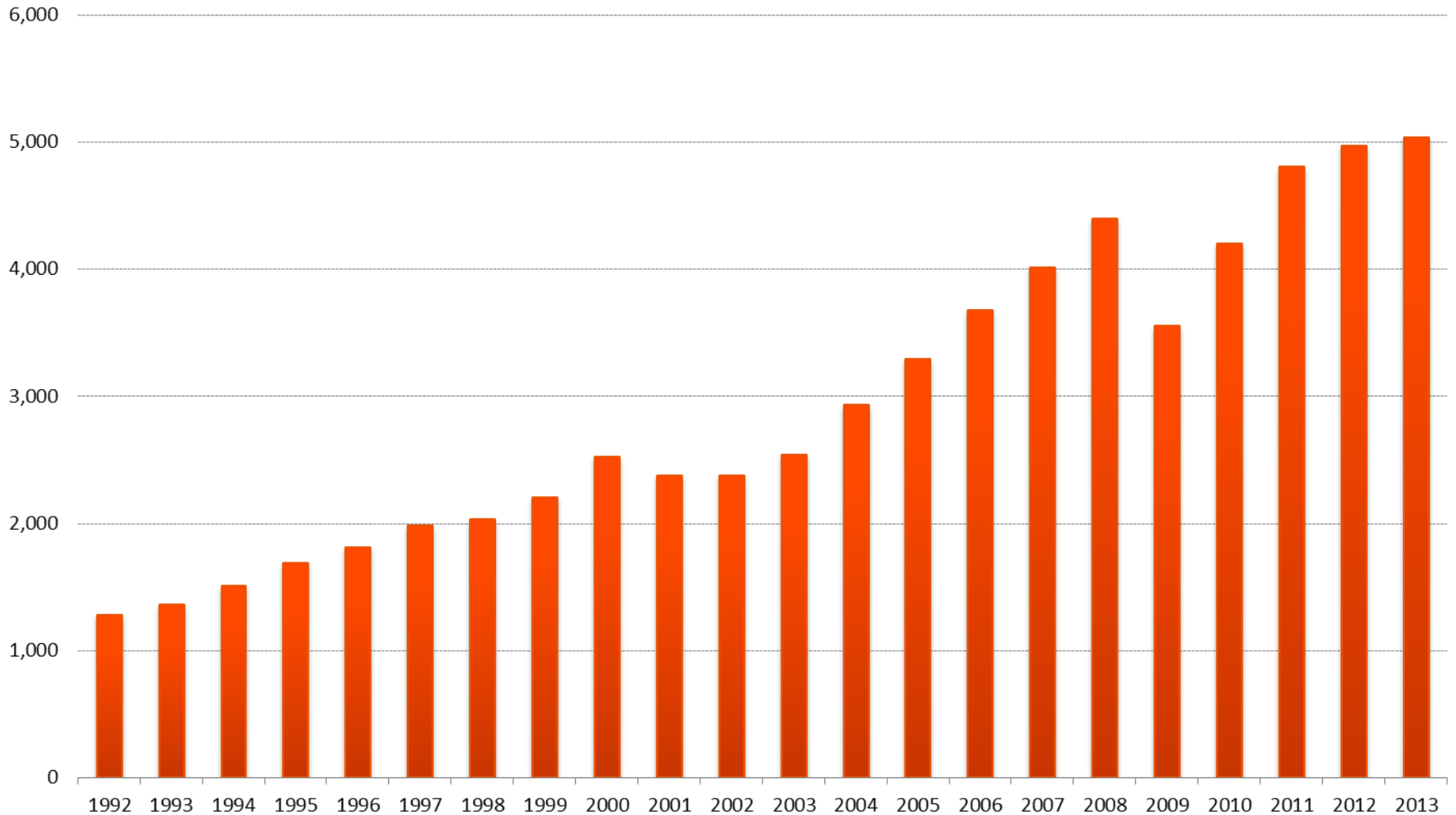


# Fiscal: Autopilot has been switched off

Federal Revenues & Outlays (% GDP)



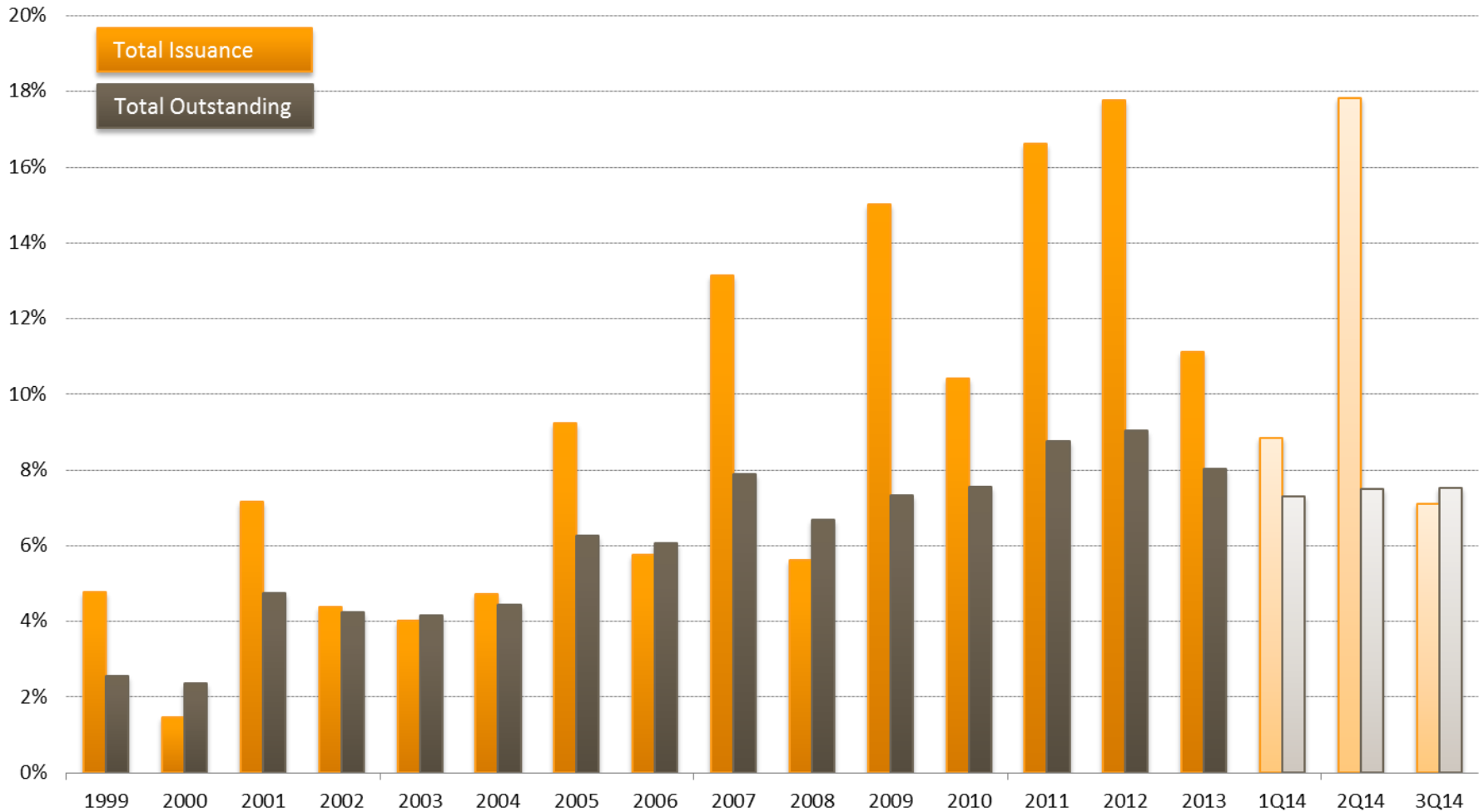
U.S. Total Trade in Goods & Services (\$B)



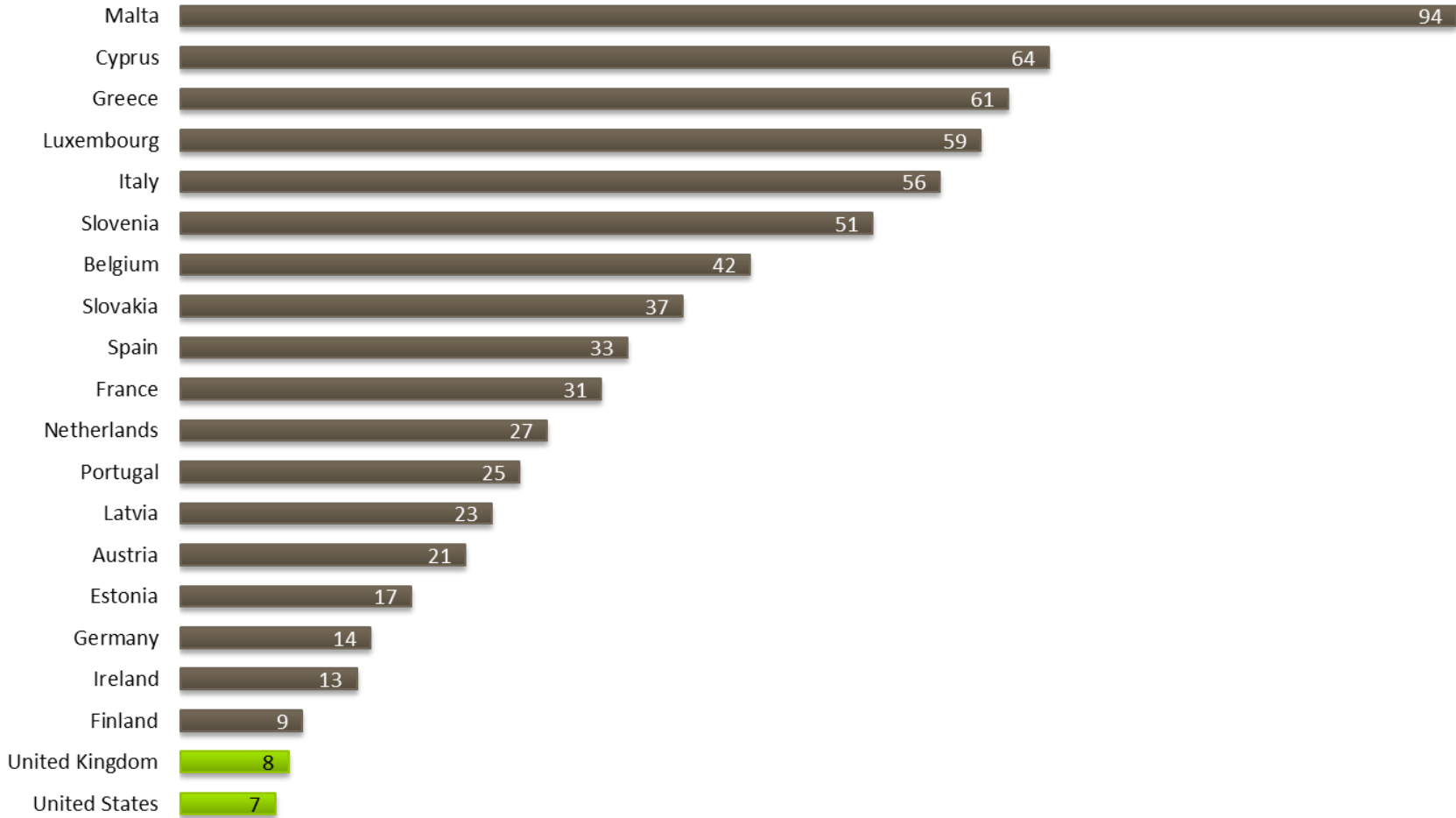
## Levels of Private Sector Engagement in PPP Contracts

	Identify Infrastructure Need	Propose Solution	Project Design	Project Financing	Construction	Operation/Maintenance	Ownership
Bid/Build	Public Sector				Private Sector	Public Sector	
Design/Build	Public Sector		Private Sector	Public Sector	Private Sector	Public Sector	
Design/Build/Finance	Public Sector		Private Sector			Public Sector	
Design/Build/Finance/Operate/Maintain	Public Sector		Private Sector				Public Sector

Europe SME Securitization as a % of...



**Eurozone Ease of Doing Business (1 = easiest)**

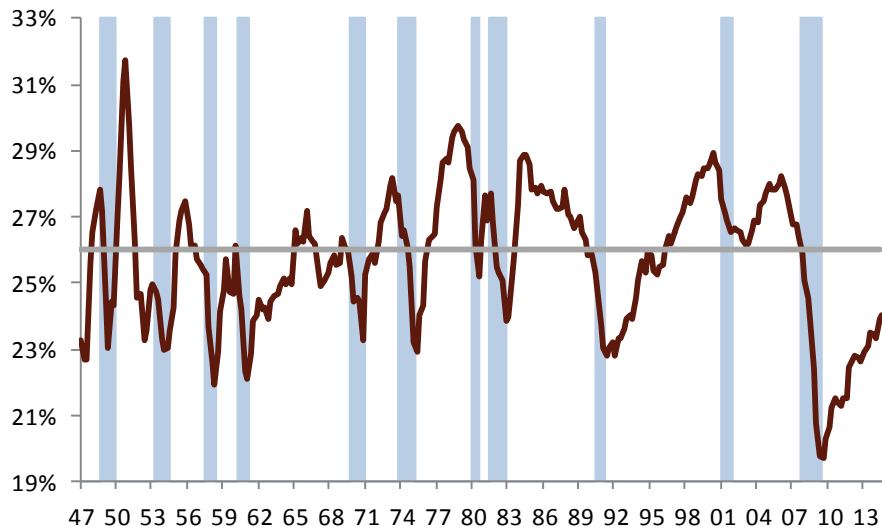




Neil Dutta

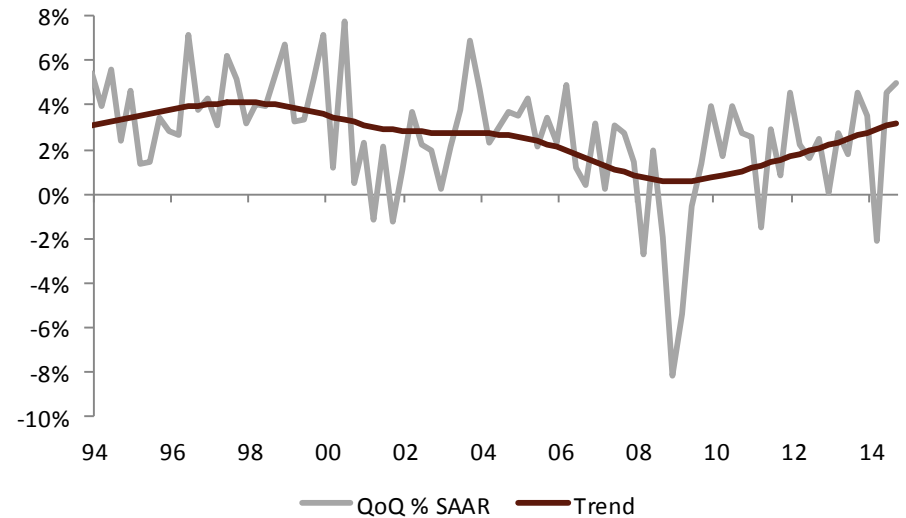
**Plenty of cyclical upside**

Durable goods + private investment (% of GDP)

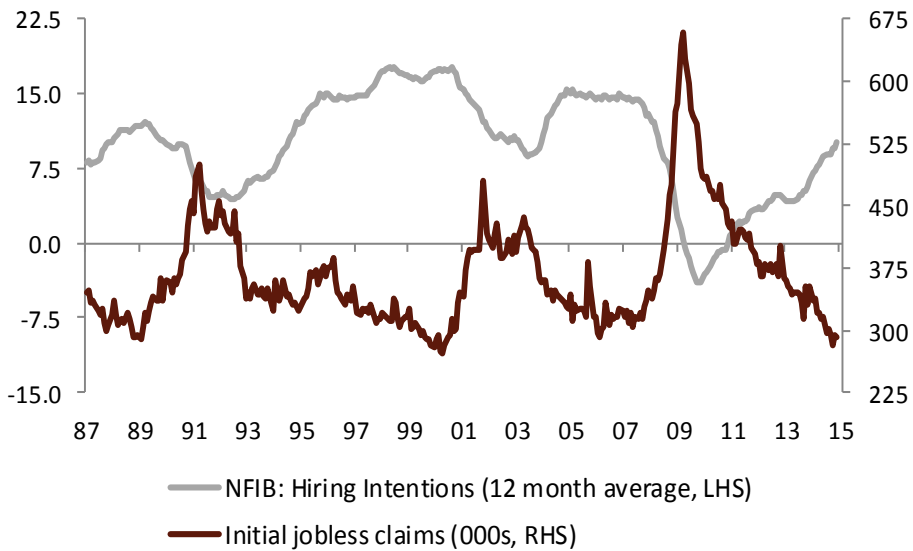


**Solid momentum under the economy**

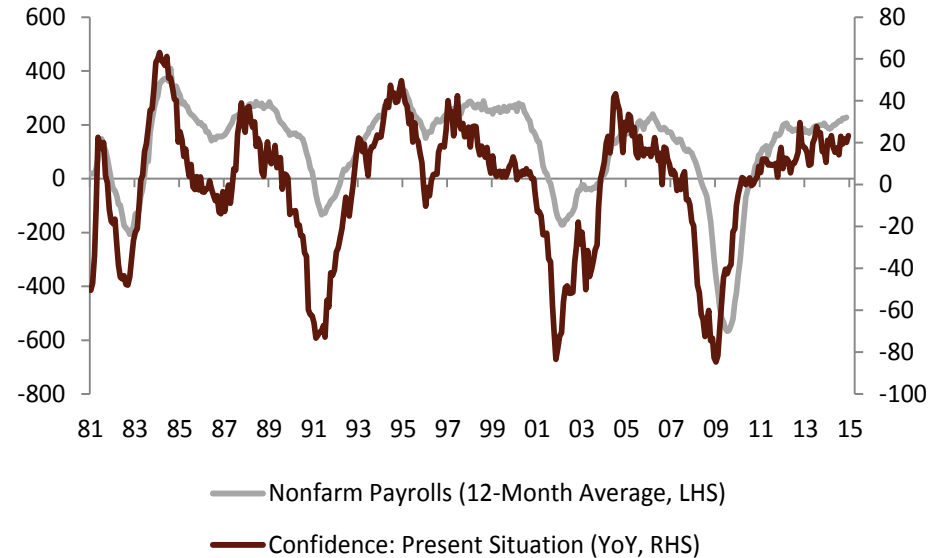
Real GDP (QoQ % SAAR)



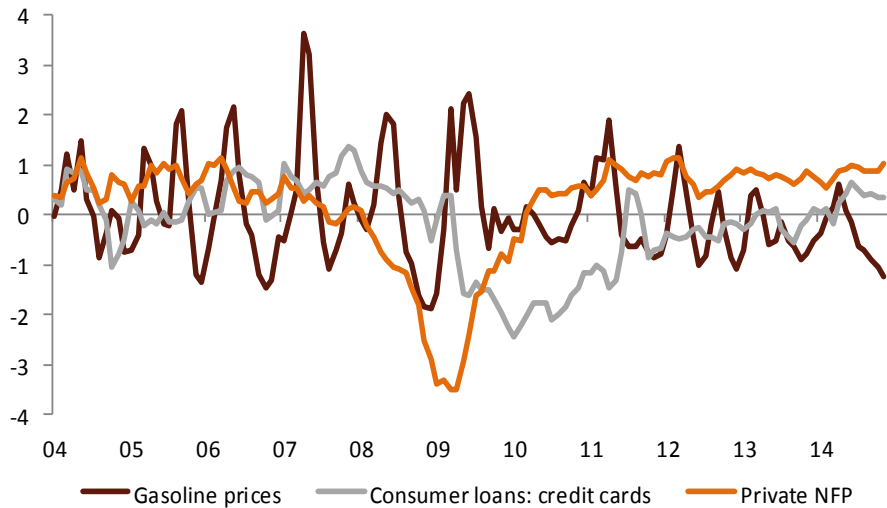
### Hiring intentions climbing as firings fall



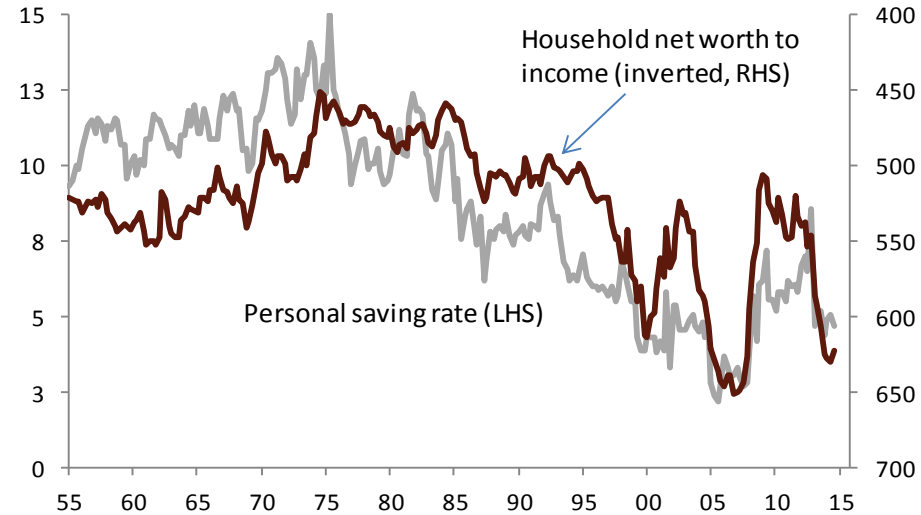
### Confidence leads employment



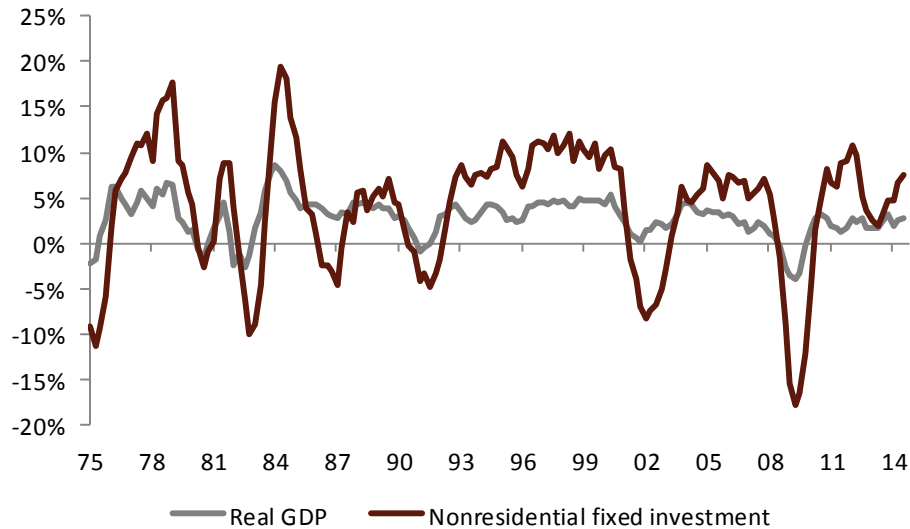
**Jobs, energy, and credit above normal**  
 (three month % SAAR, z-score)



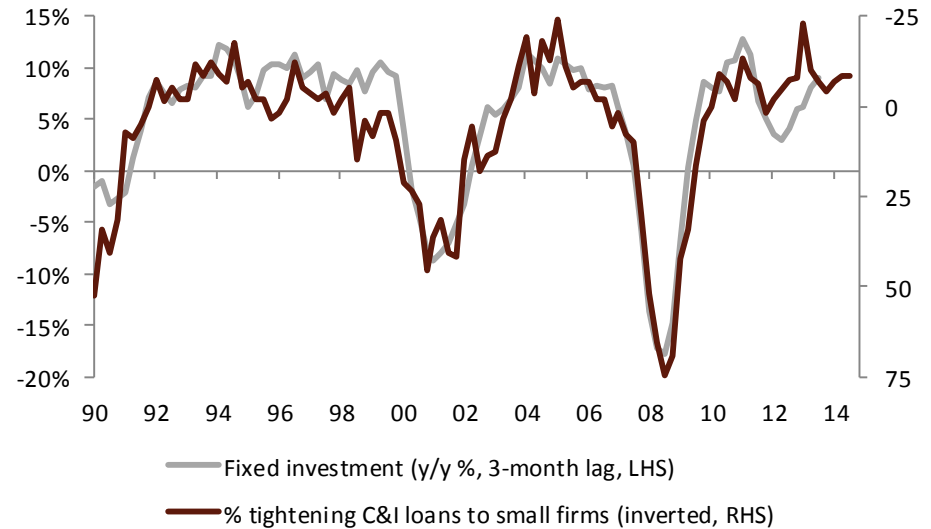
**Savings rate unlikely to shift upward**  
 (percent)



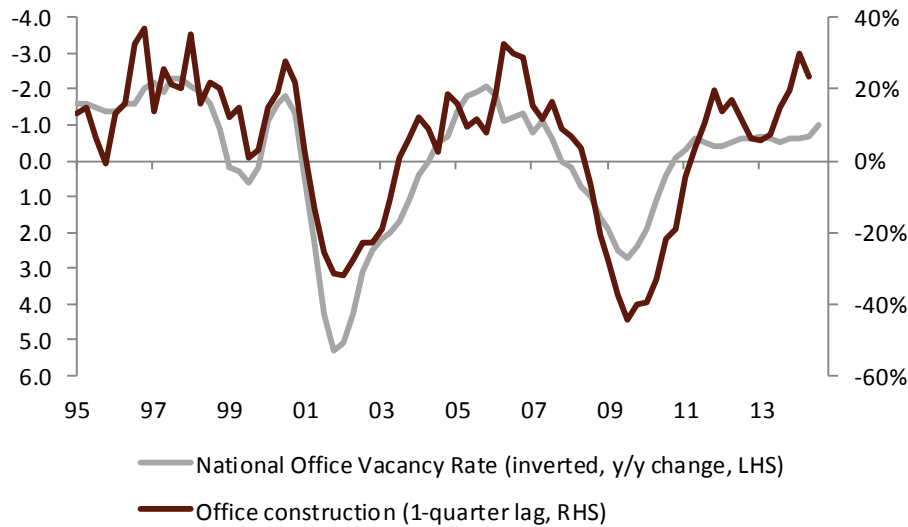
**The accelerator model**  
 (year-over-year % change)



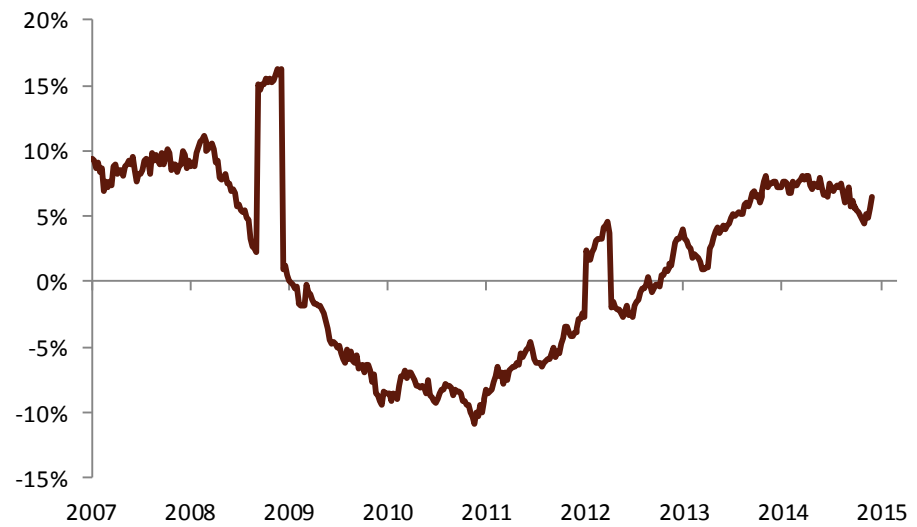
**Lending standards on C&I loans lead investment**



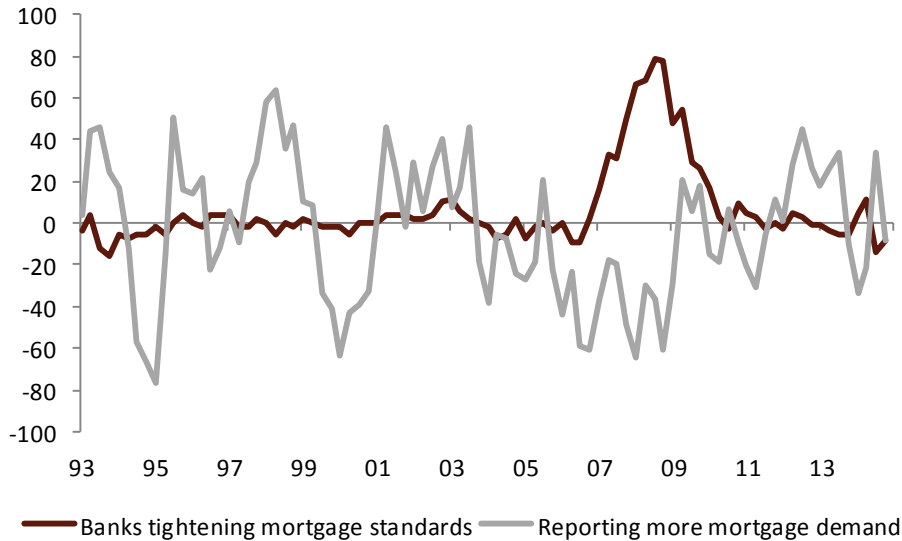
**Steady drop in office vacancies**  
 (year-over-year change)



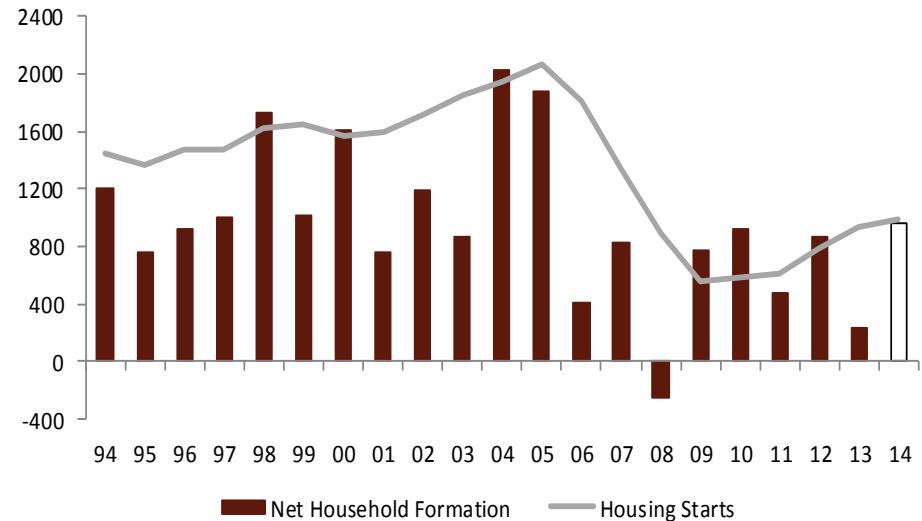
**Lending recovery in CRE**  
 (13-week % change, annualized)



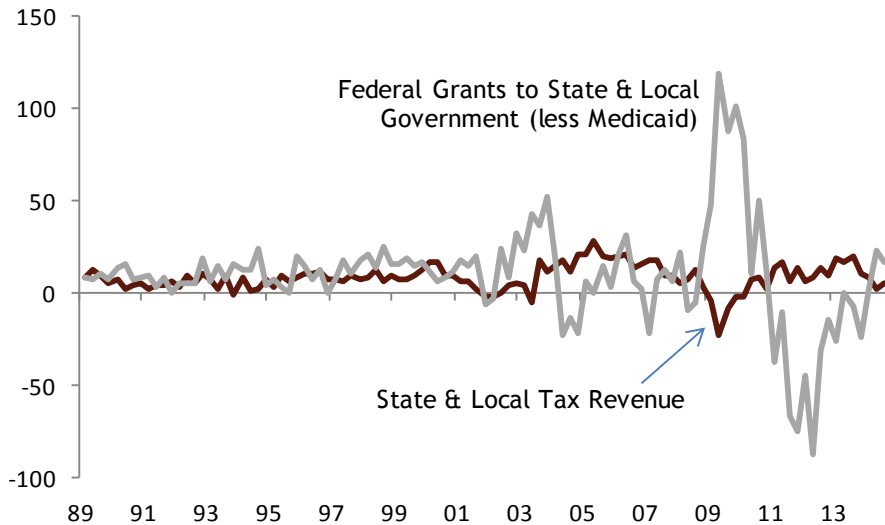
**Mortgage lending standards still tight**  
 (Senior Loan Officer Survey)



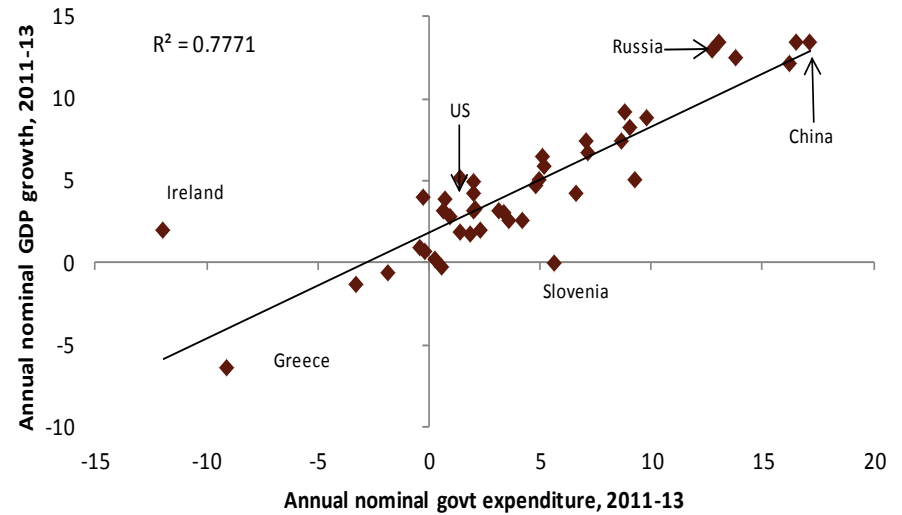
**Formations to drive construction**  
 (000s, annual)



**Easing state and local budget pressures**  
 (billions \$, year-over-year change)

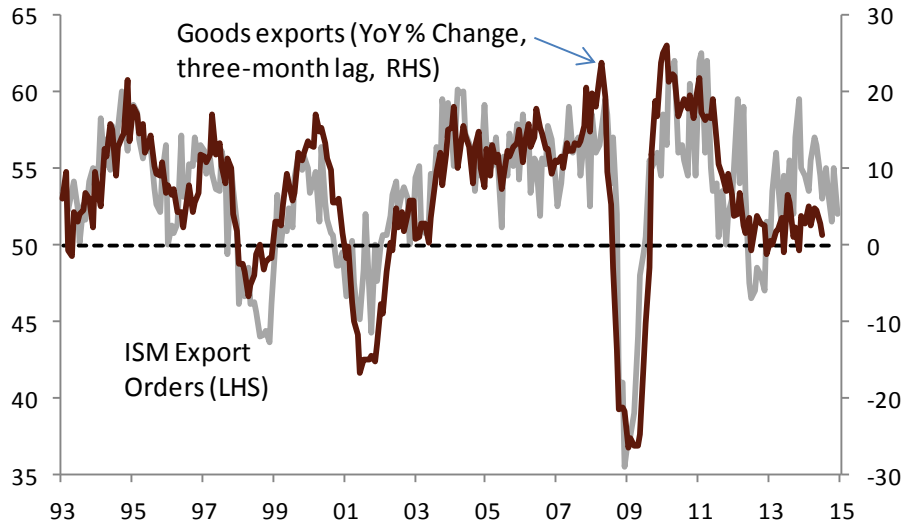


**Federal government no longer a drag in US**

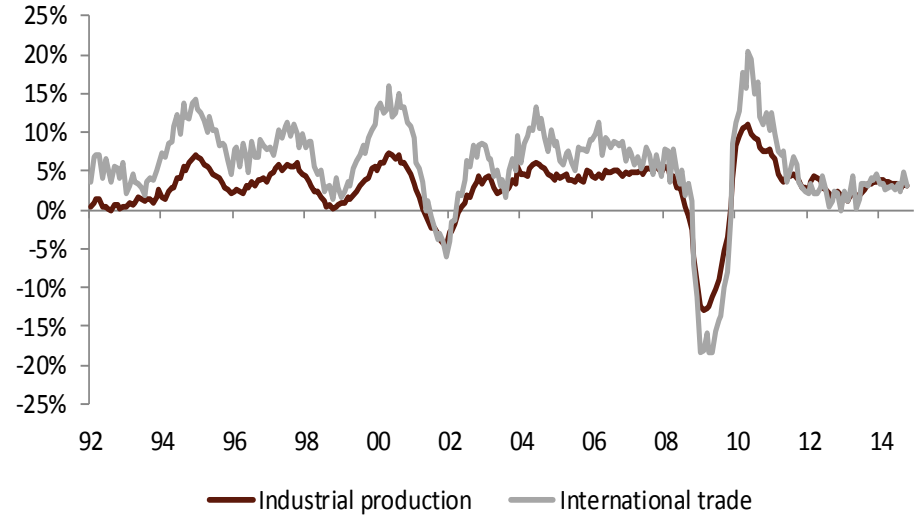




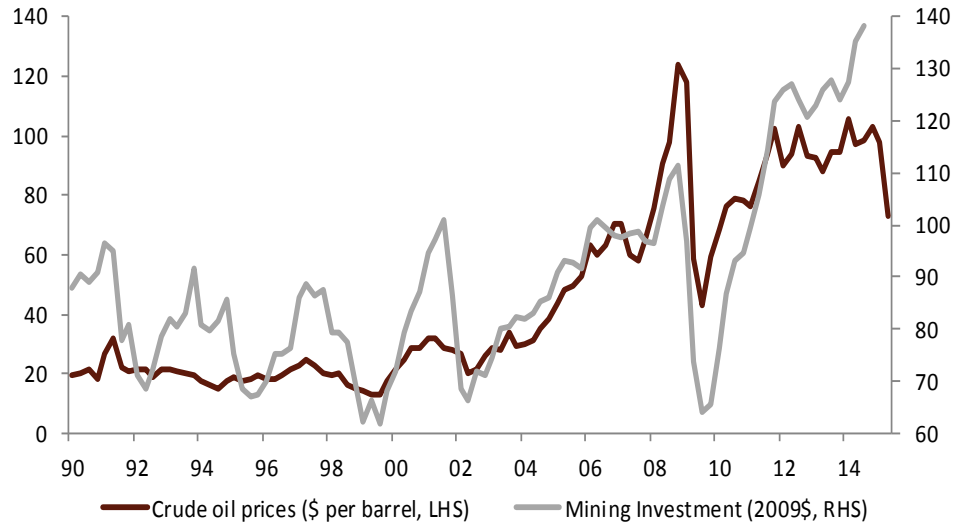
### Moderate export growth ahead



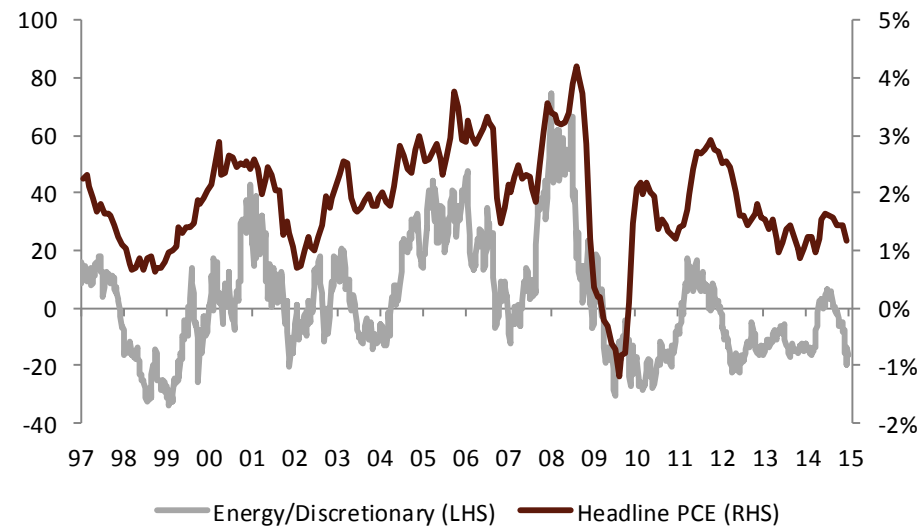
### Structural problems to global trade (year-over-year % change)



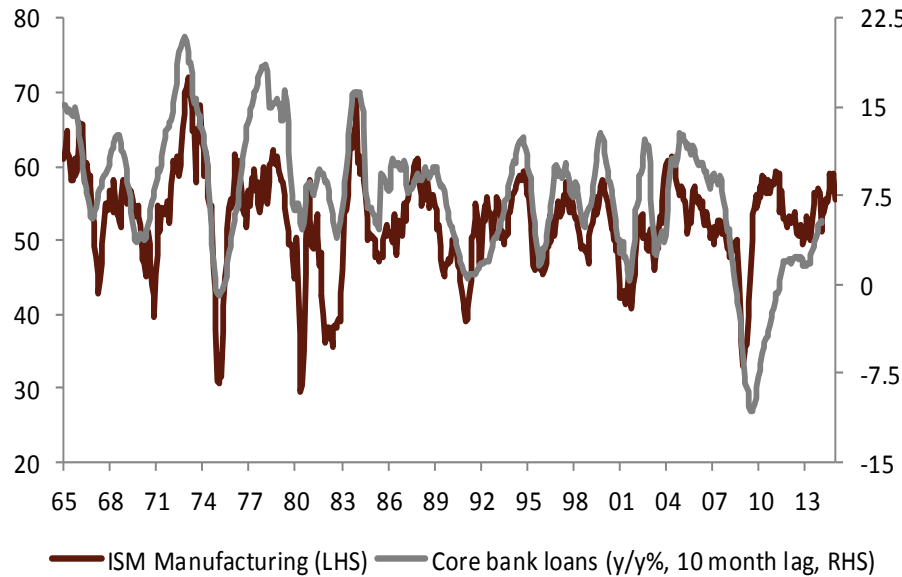
### Mining investment poised to slow



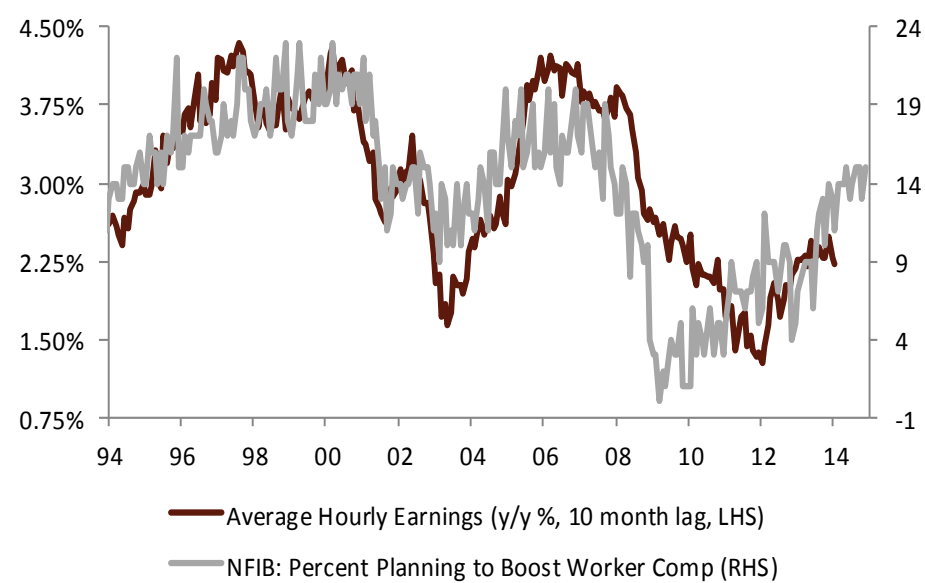
### Rising disposable income helps discretionary (year-over-year % change)



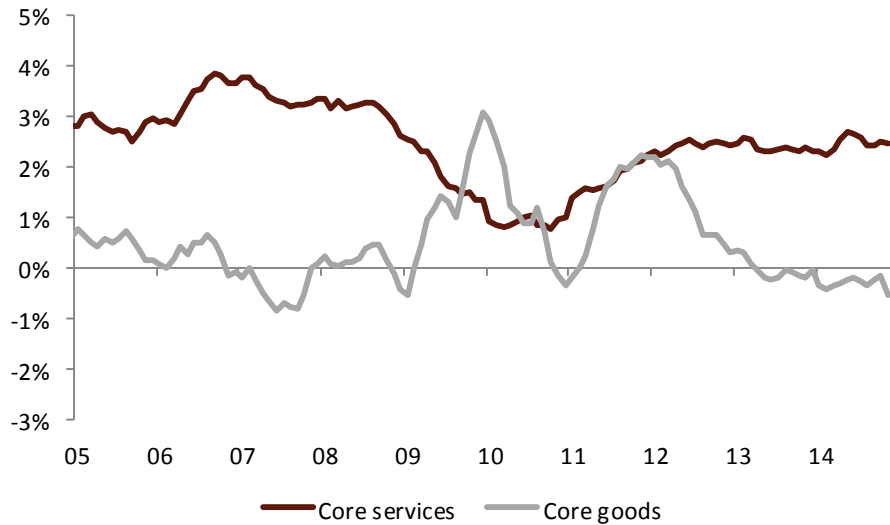
**Core bank lending to continue climbing**



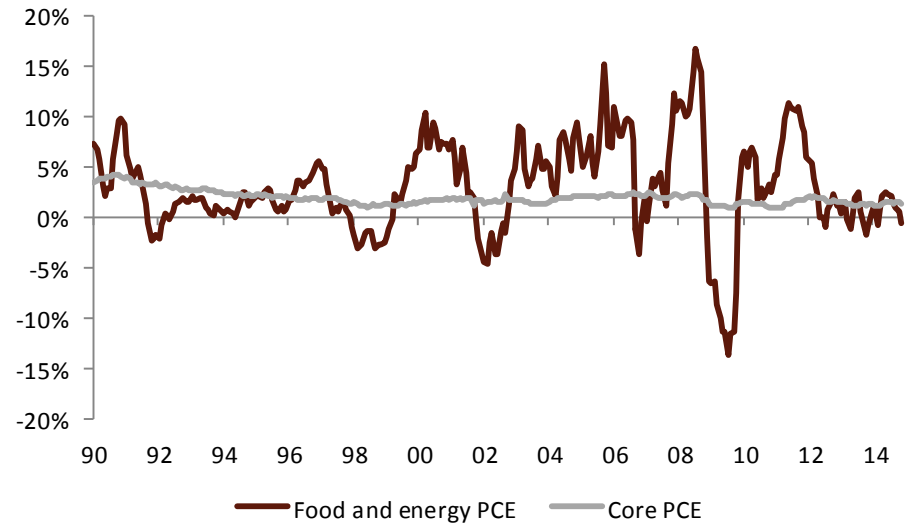
**Small businesses signal wage growth ahead**



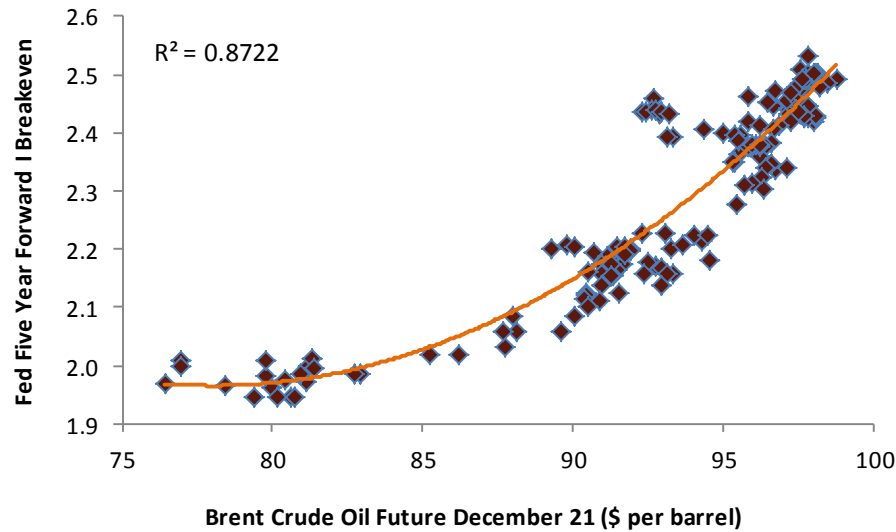
**Services sector inflation picks up**  
(year-over-year % change)



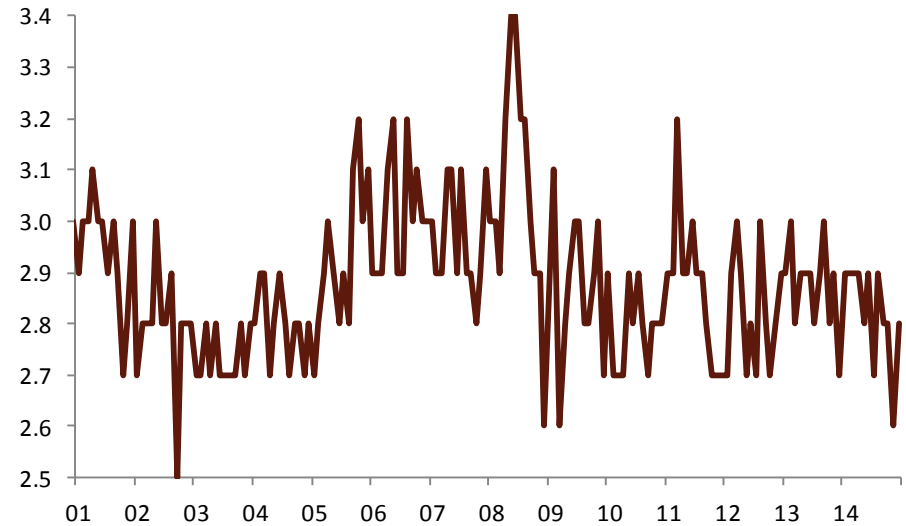
**Limited commodity pass through**  
(year-over-year % change)



**Breakeven rates can be explained by oil futures**  
(daily data since June 2014)

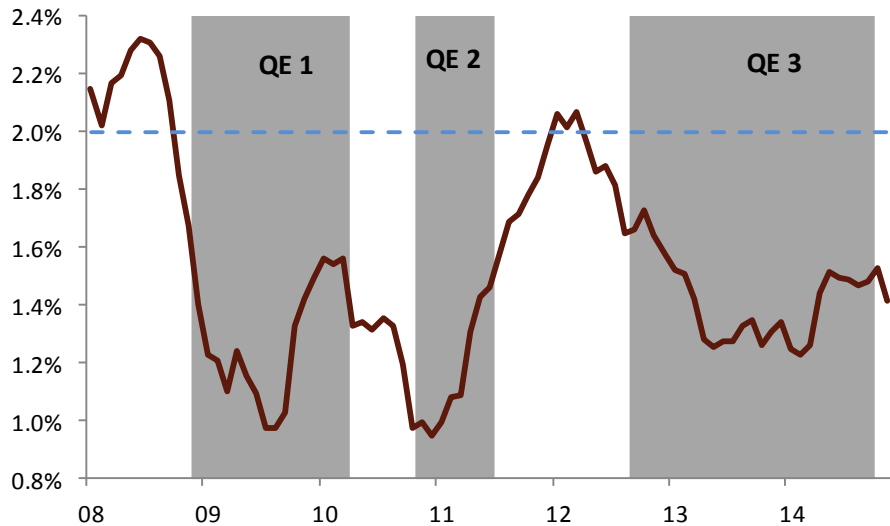


**Households expectations are stable**  
U of M Long-run median inflation expectations (%)



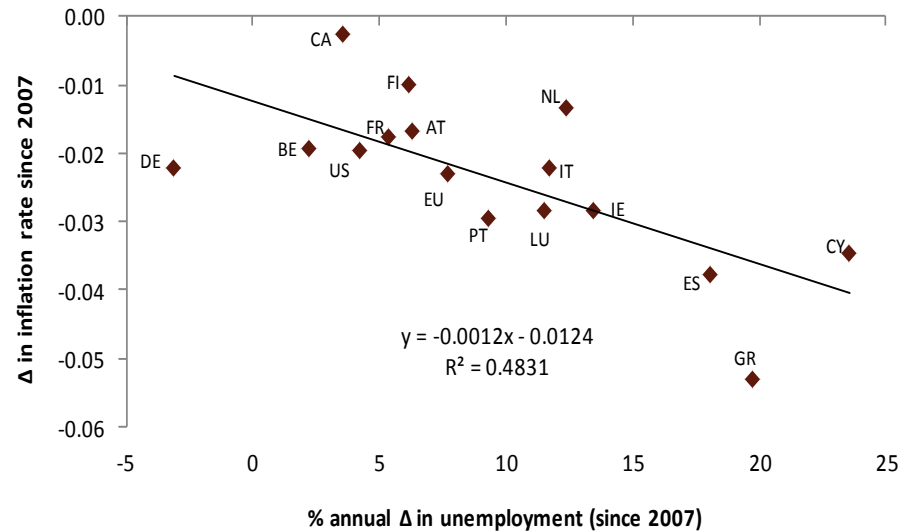
**Asymmetric inflation goals**

(Core PCE price index, year-over-year % change)

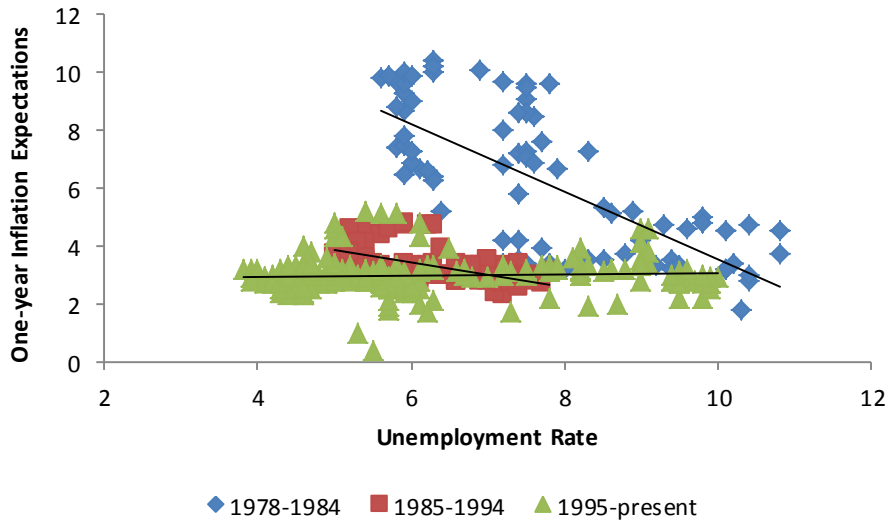


**Falling slack will help a bit**

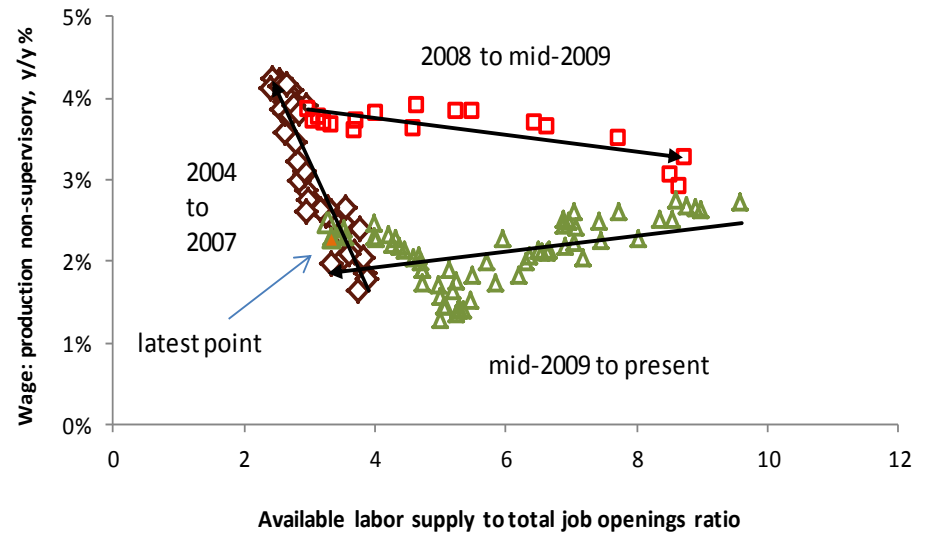
(percent change since Q4 2007)



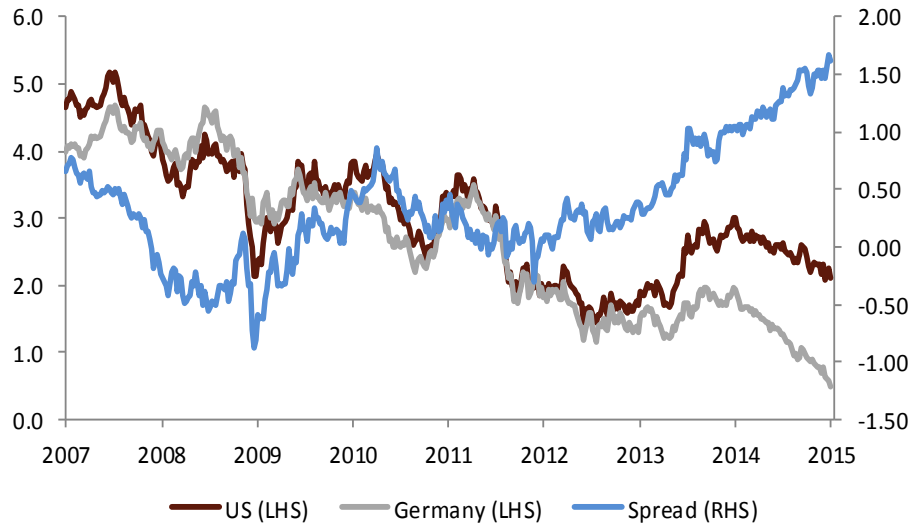
**The flat Phillips Curve**  
(Unemployment vs. Inflation expectations)



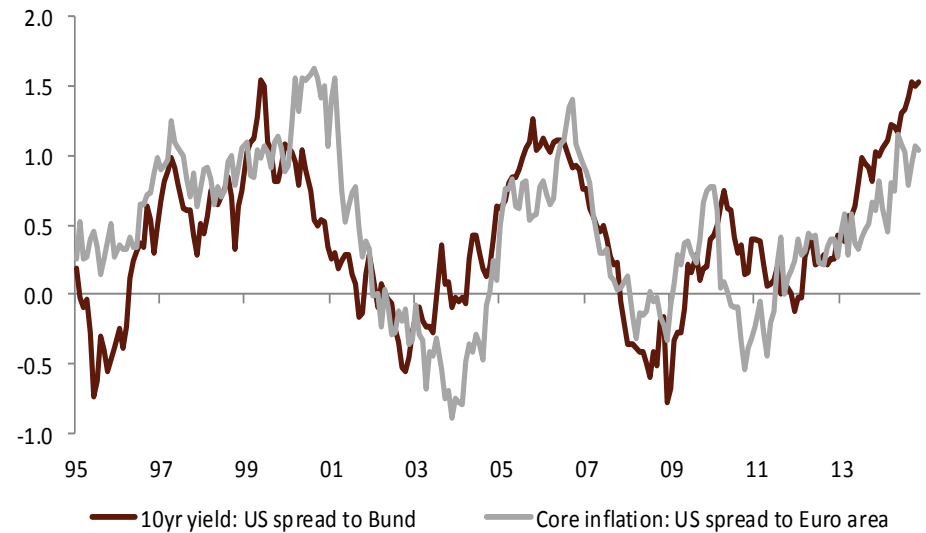
**As labor supply falls, wages will rise**



**Why haven't rates converged already?**  
(ten year government bond yields, %)

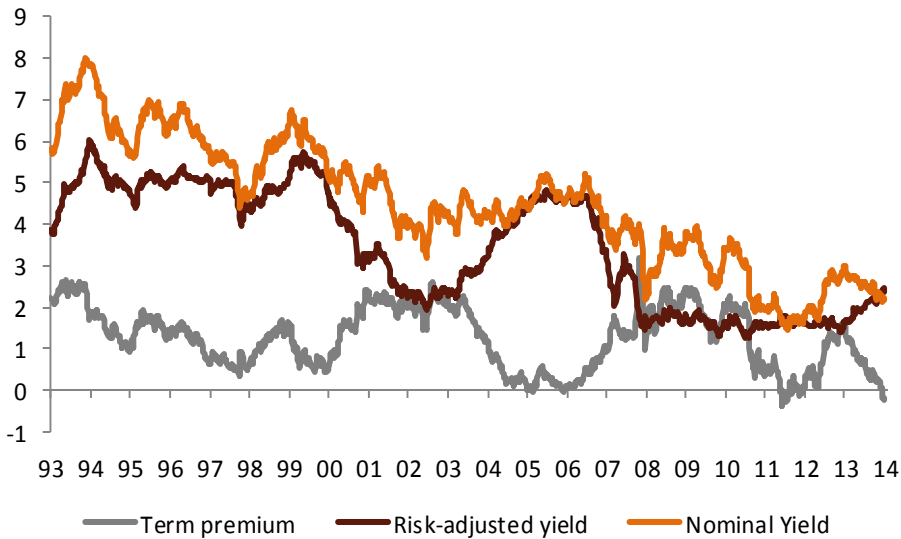


**Widening spread reflects inflation dynamics**  
(percentage points)

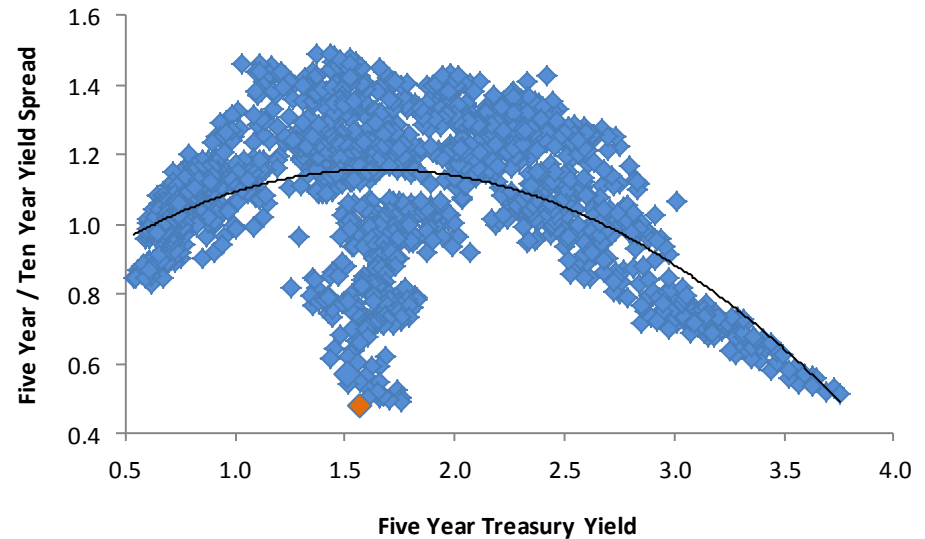




**How low can the term premium go?**  
 10 year duration (percent)

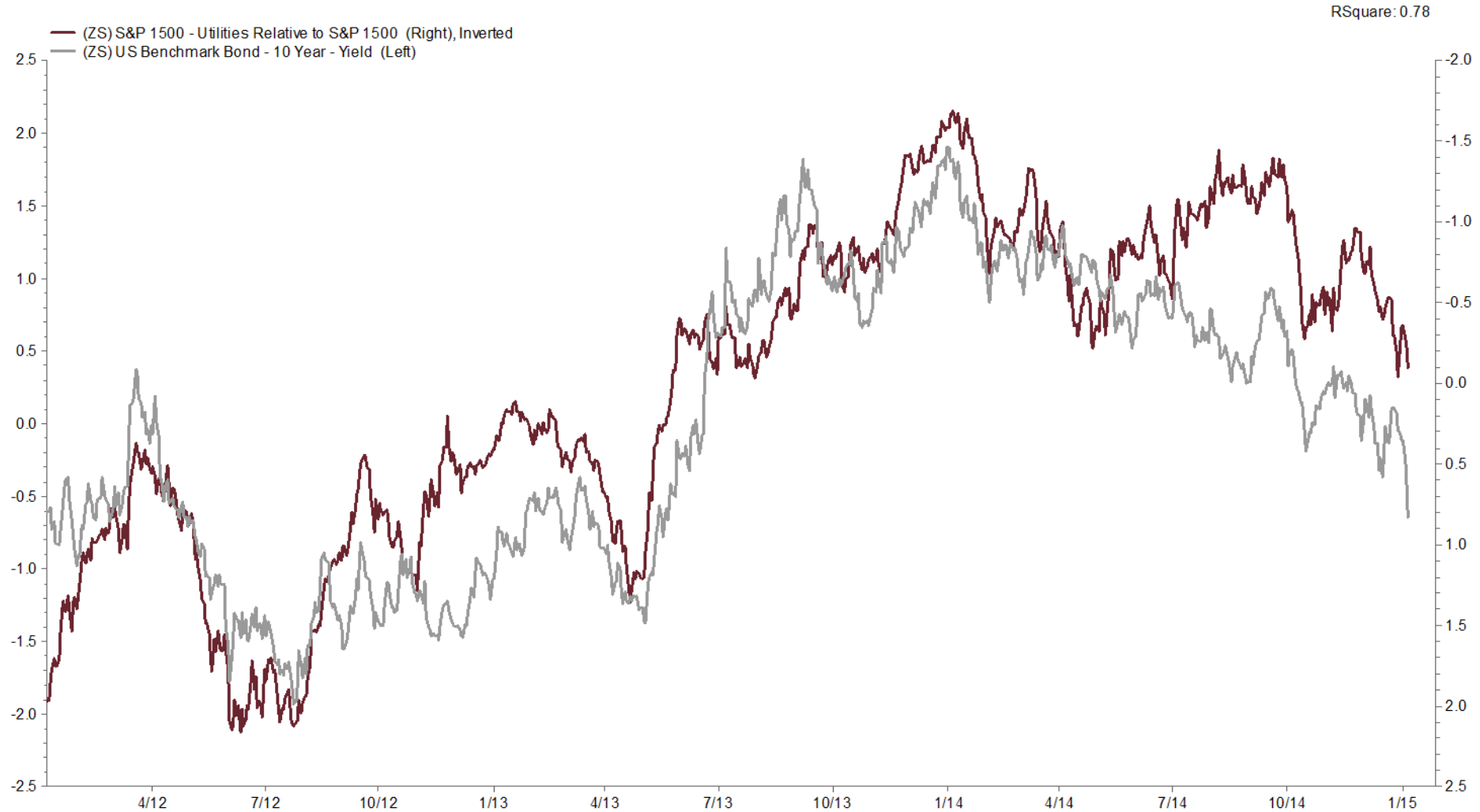


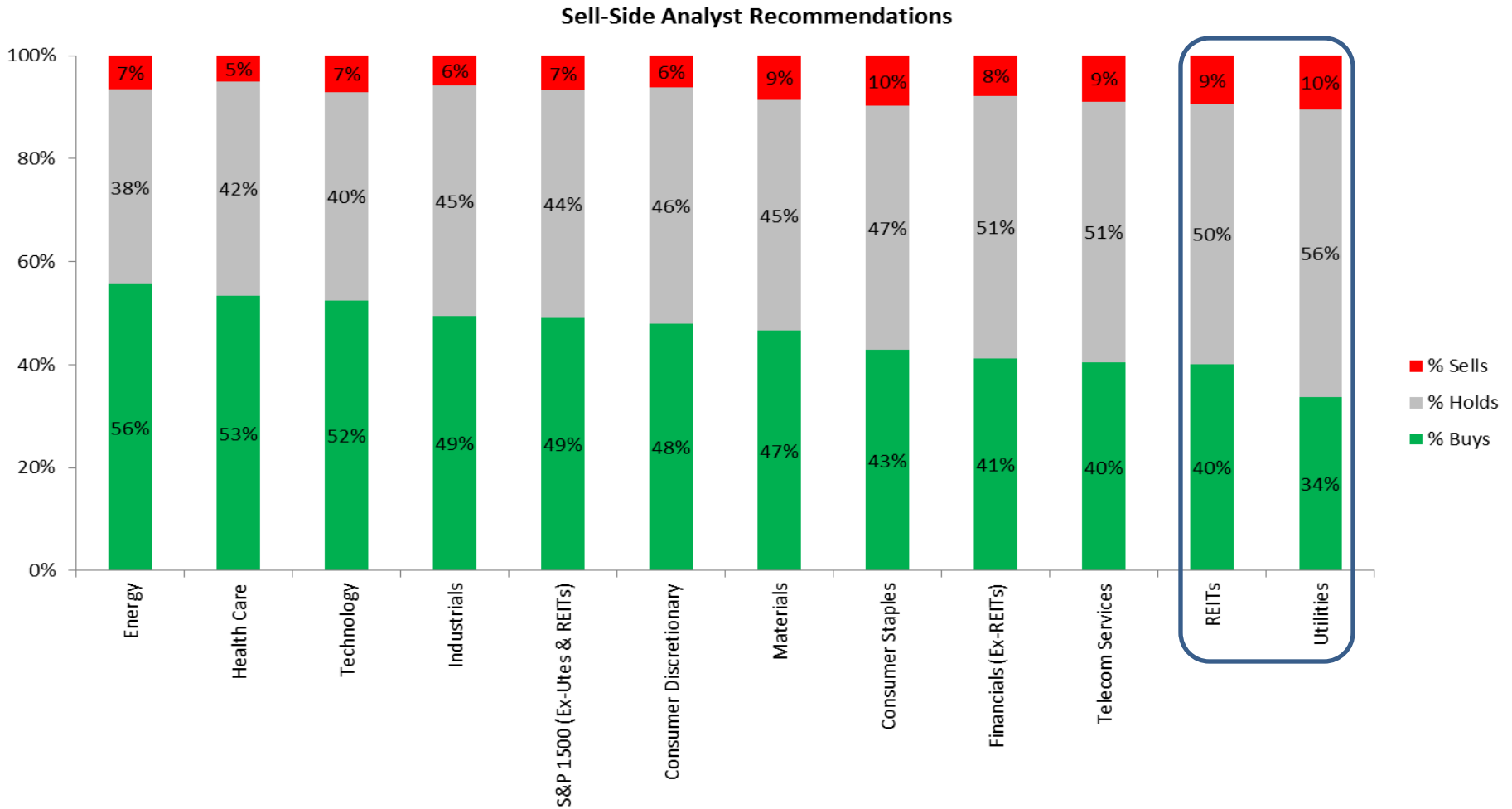
**Curve typically much steeper**  
 Data since 2008 (percentage points)



Jeff deGraaf  
and  
Rob Ginsberg

## Bond Surrogates: Biggest beneficiary of low rate environment

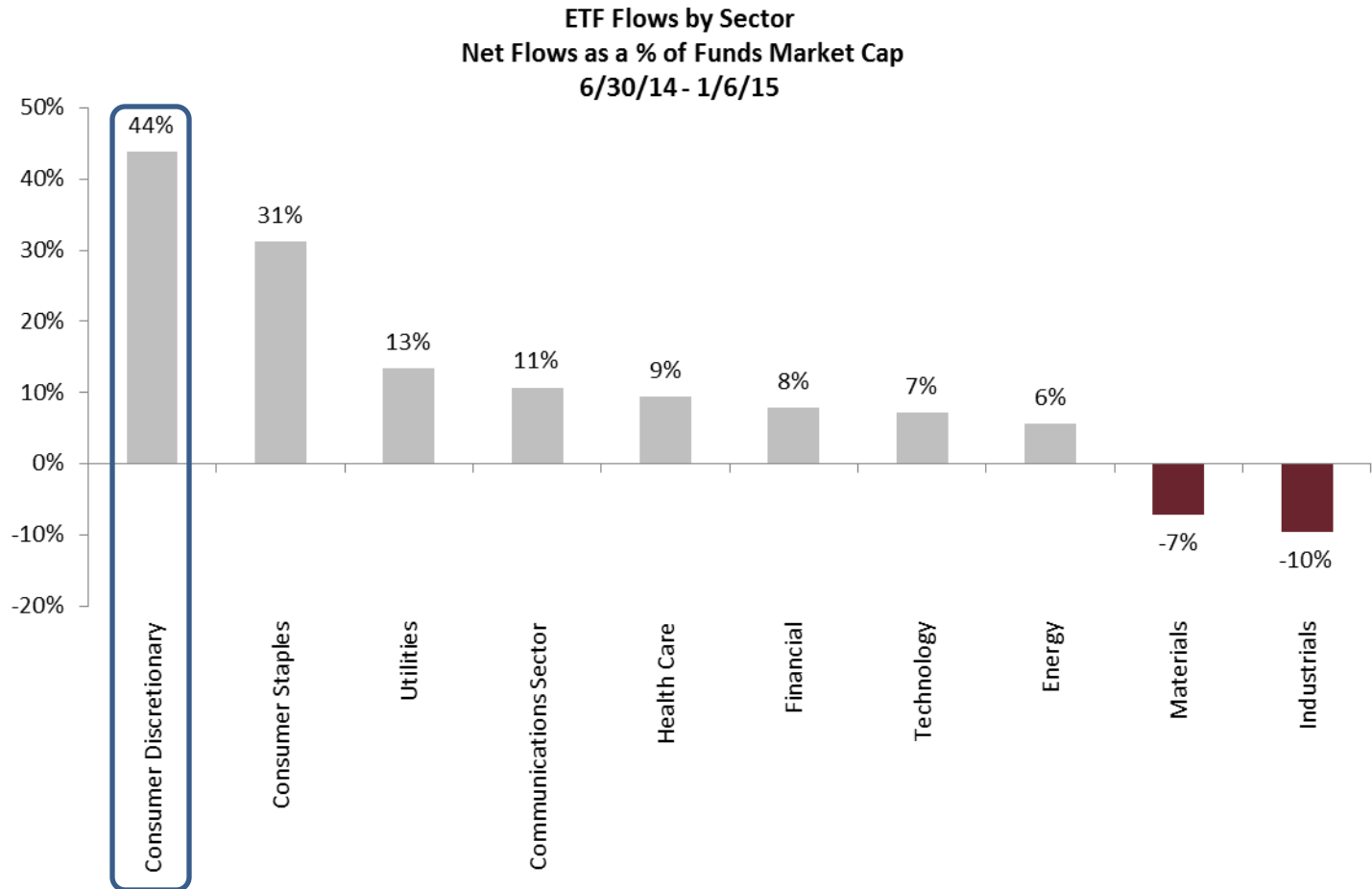




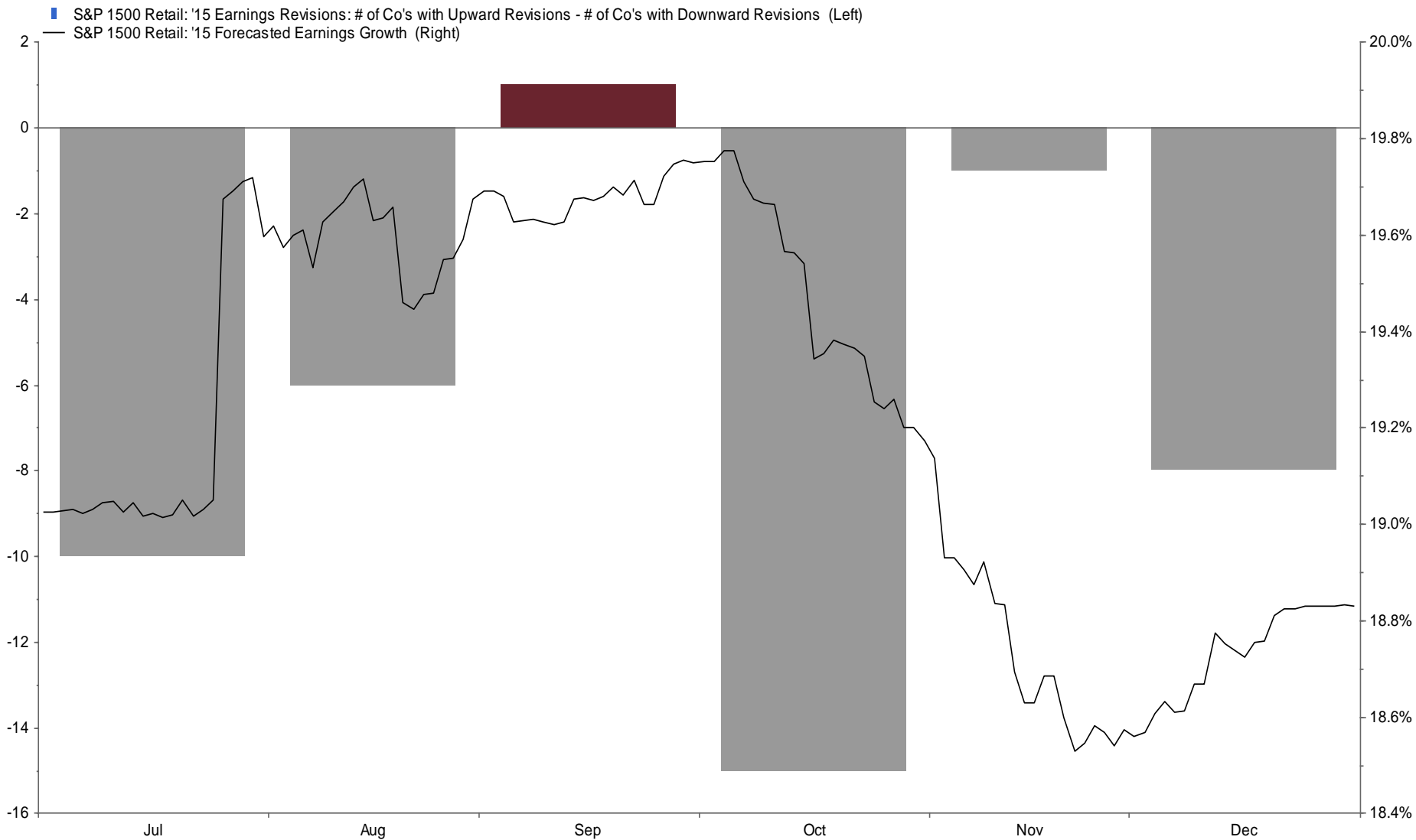
## Retail: Decline in oil has been a dramatic tailwind



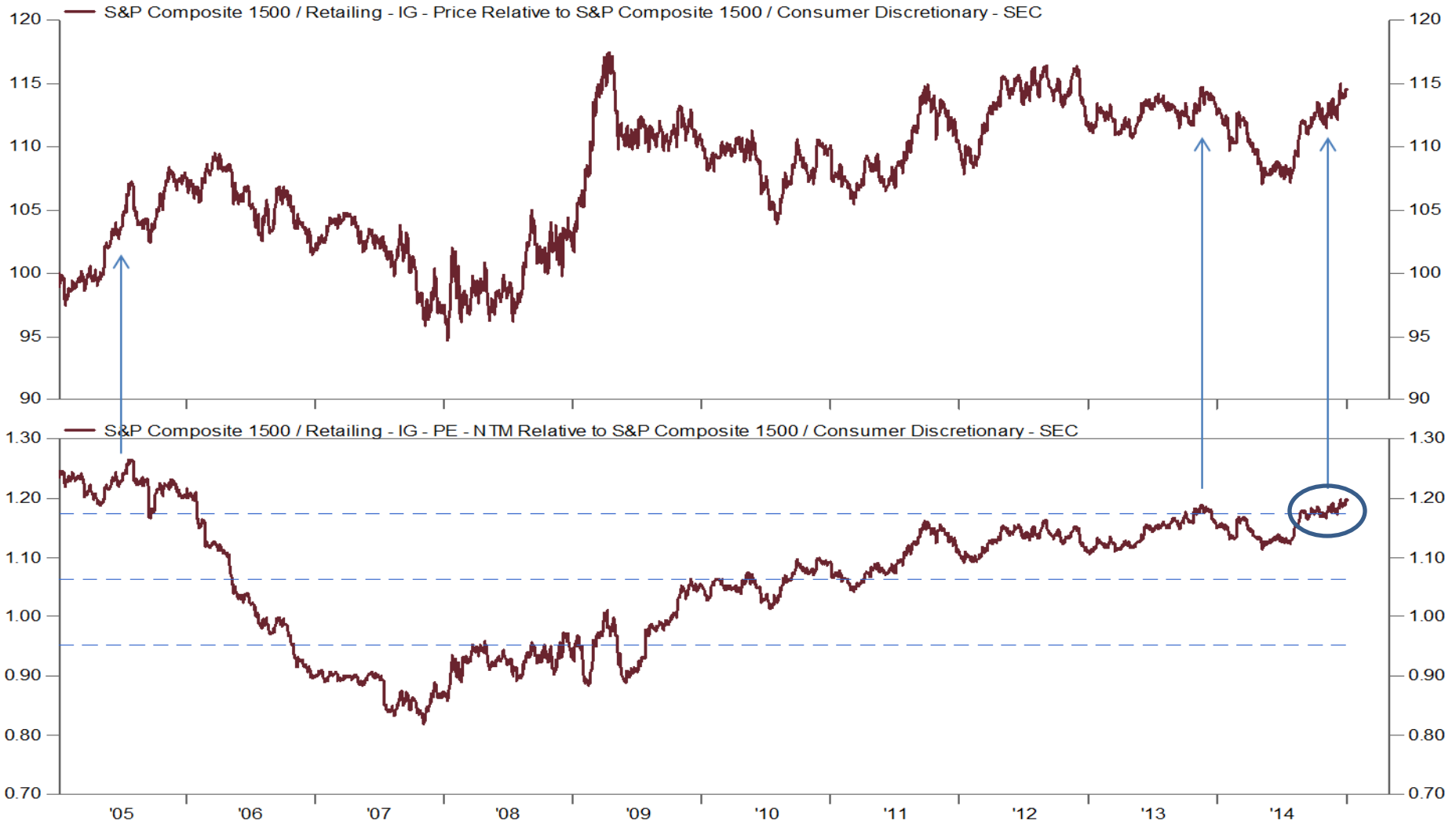
**Retail:** Since the peak in oil, investors Have piled into discretionary



Source: Bloomberg, RenMac

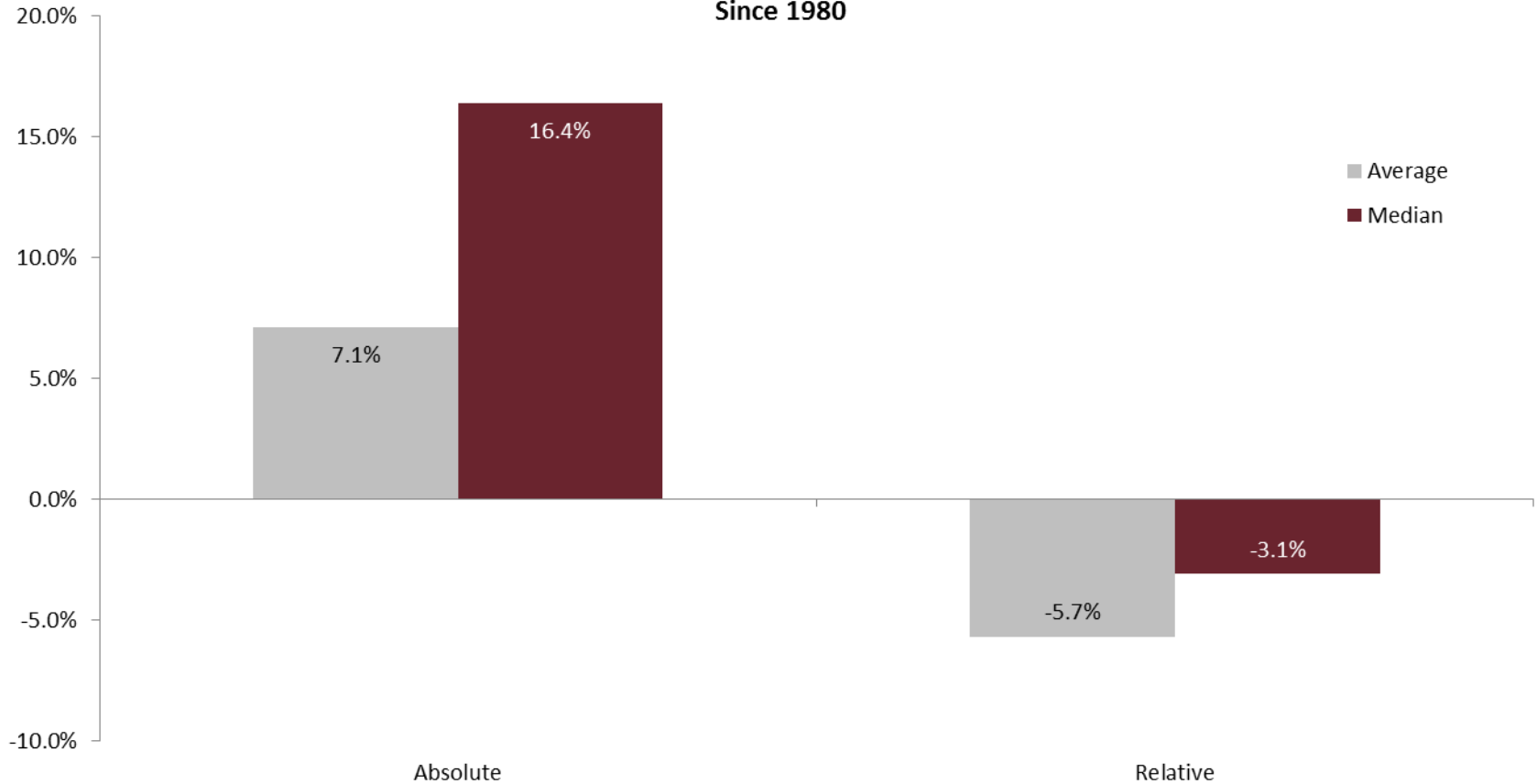


# Retail: Valuation stretched

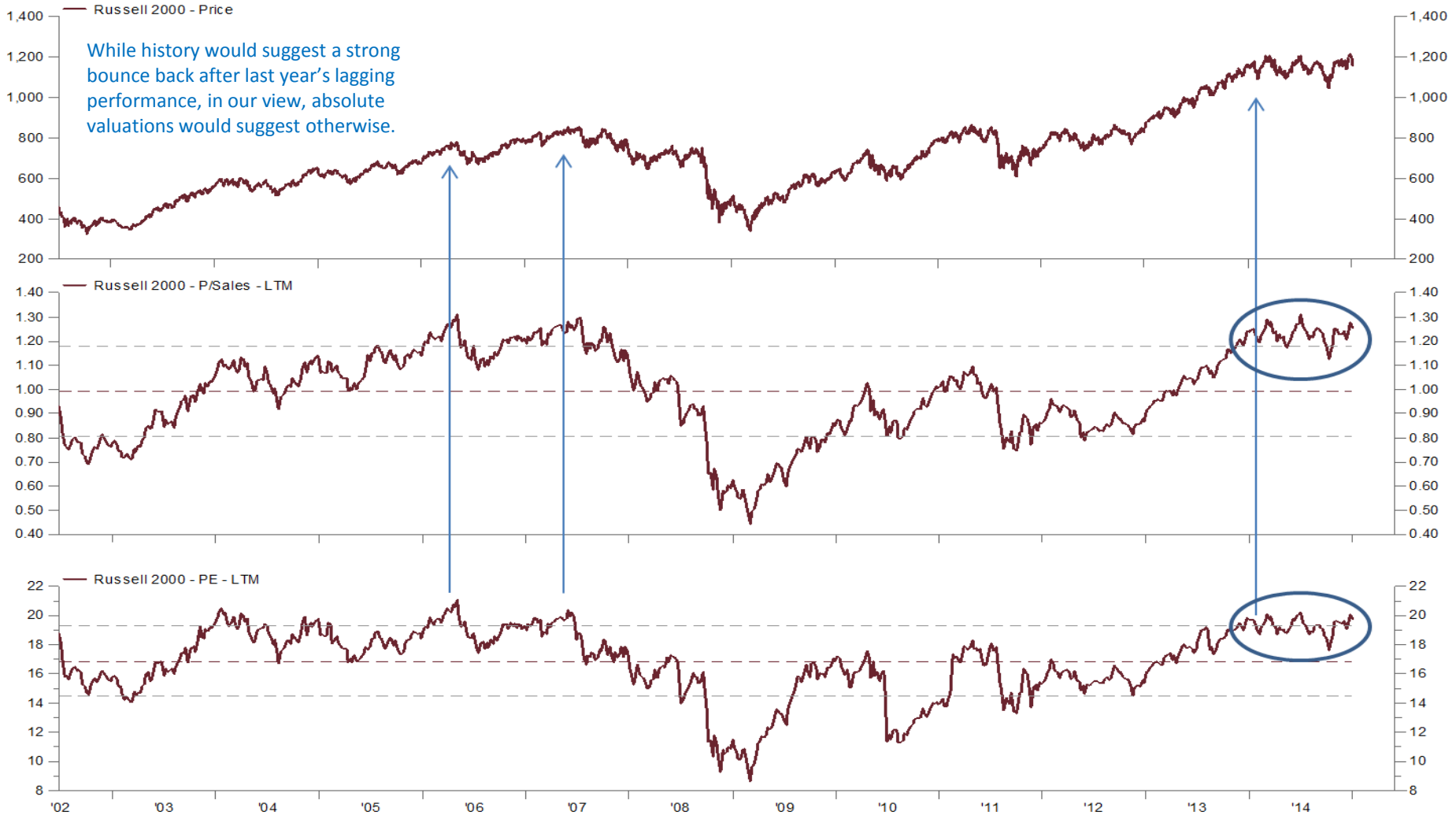




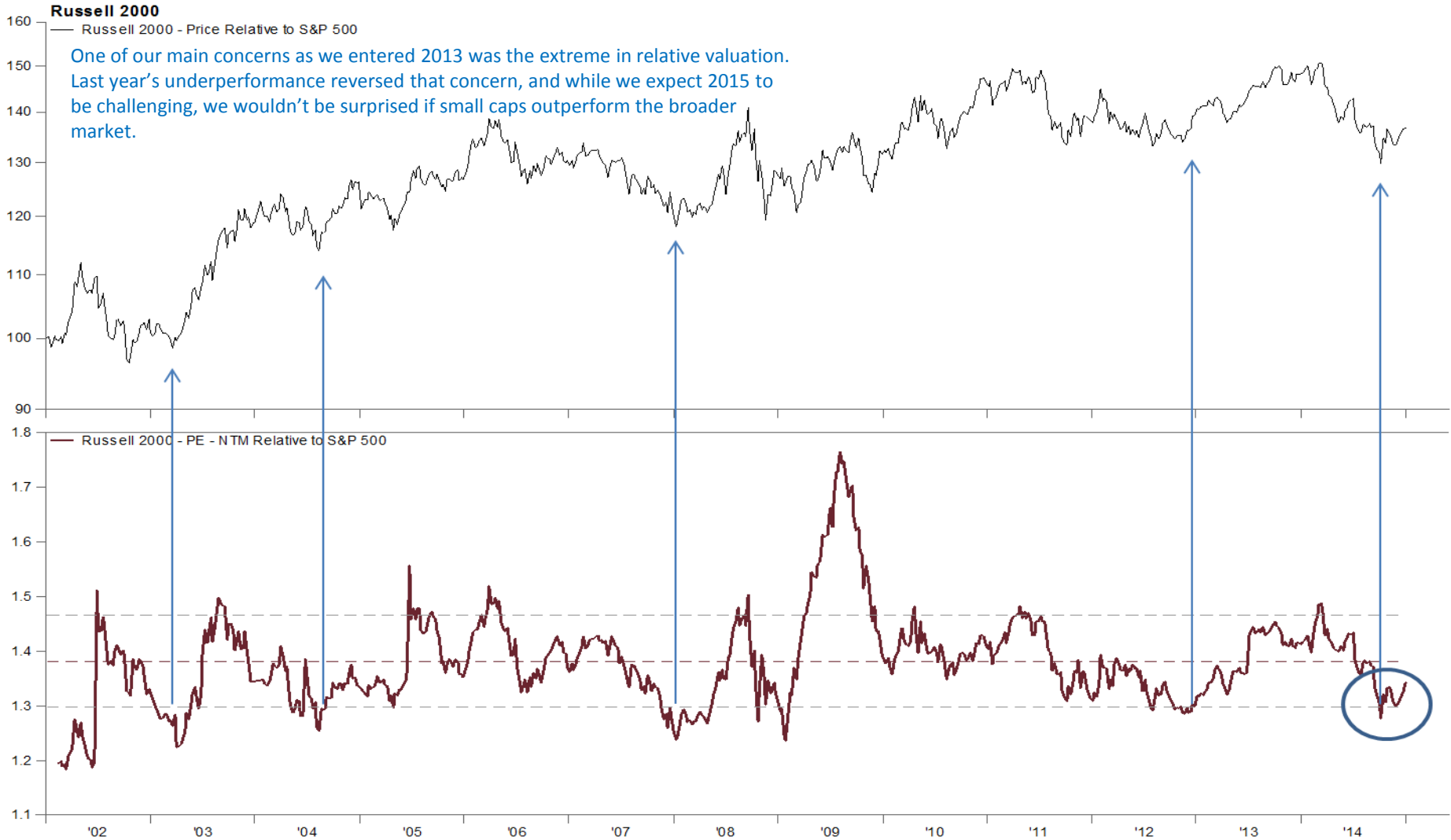
**Russell 2000 Performance Year Following Bottom Quartile Return vs. S&P 500 Since 1980**



## Small Cap: We believe the opposite will occur in 2015



## Small Cap: Relative valuation suggests outperformance



# Small Cap: End of an era?

Russell 2000

Price

We remain in the camp that the 15-year run of outperformance has come to an end



**Investors Pile Into ETFs at Record Pace – WSJ**

A Challenging Environment for Active Management – Montag.com

**Fewer active managers beat market than at any time in decade – FT**

[The Death of a "Stock Picker's Market?"](#) – Runnymede.com

**Is Stock Picking Dead? – Seeking Alpha**

**BlackRock ETF funds draw record \$102.8 billion in new money – Reuters**

**Investors Bet A Whopping \$216 Billion On Cheap, Boring Strategies In 2014 – Business Insider**

***Investors say 'bye,' but not 'ciao,' to stock pickers – Dallas News***

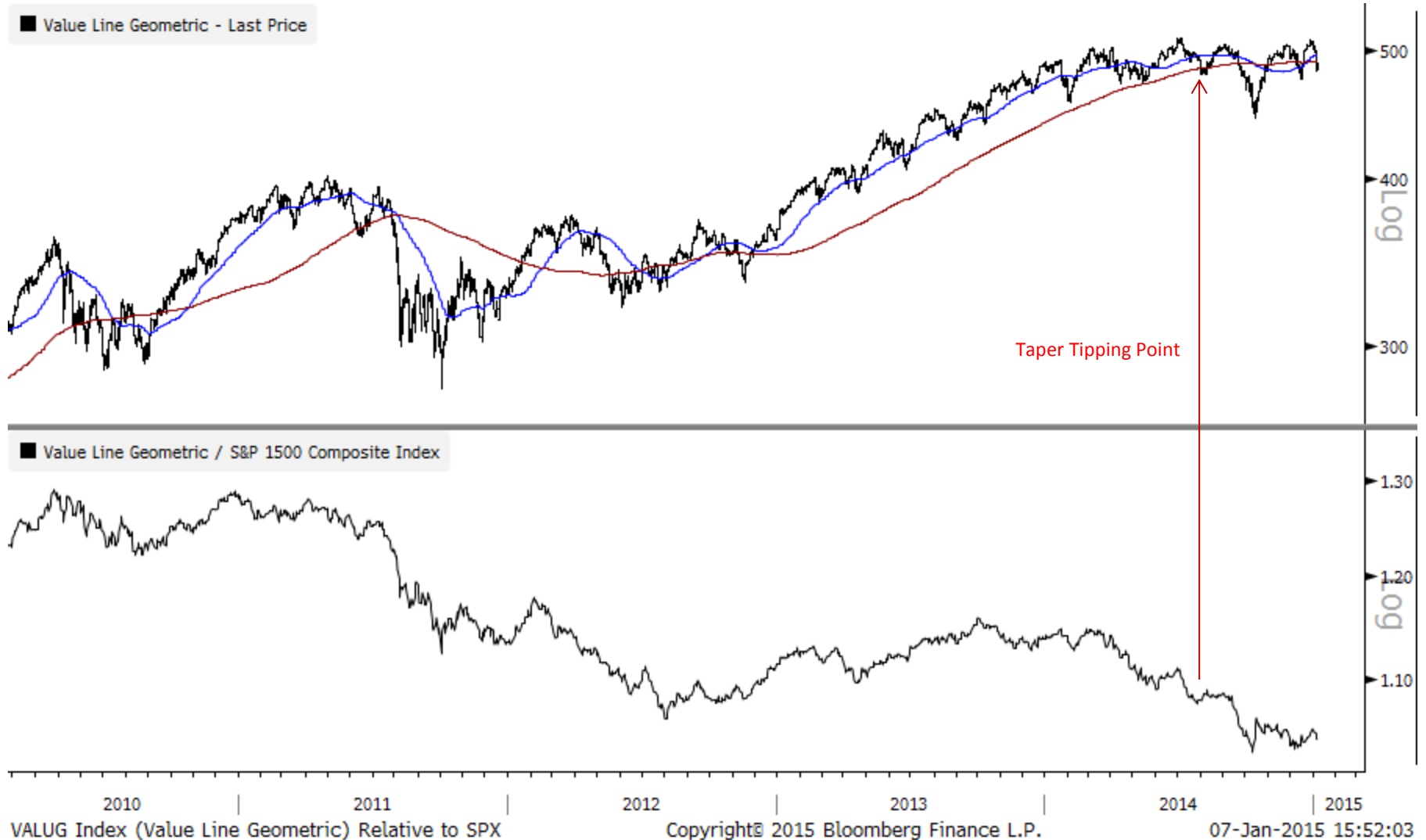
As Indexes Soar, Active Stock Pickers Can't Get Off the Ground – WSJ

***Accept that stock pickers do not beat the market – IFA***

**Warren Buffett to heirs: Put my estate in index funds – Market Watch**

**Most investment managers are lousy – Hartford Business**

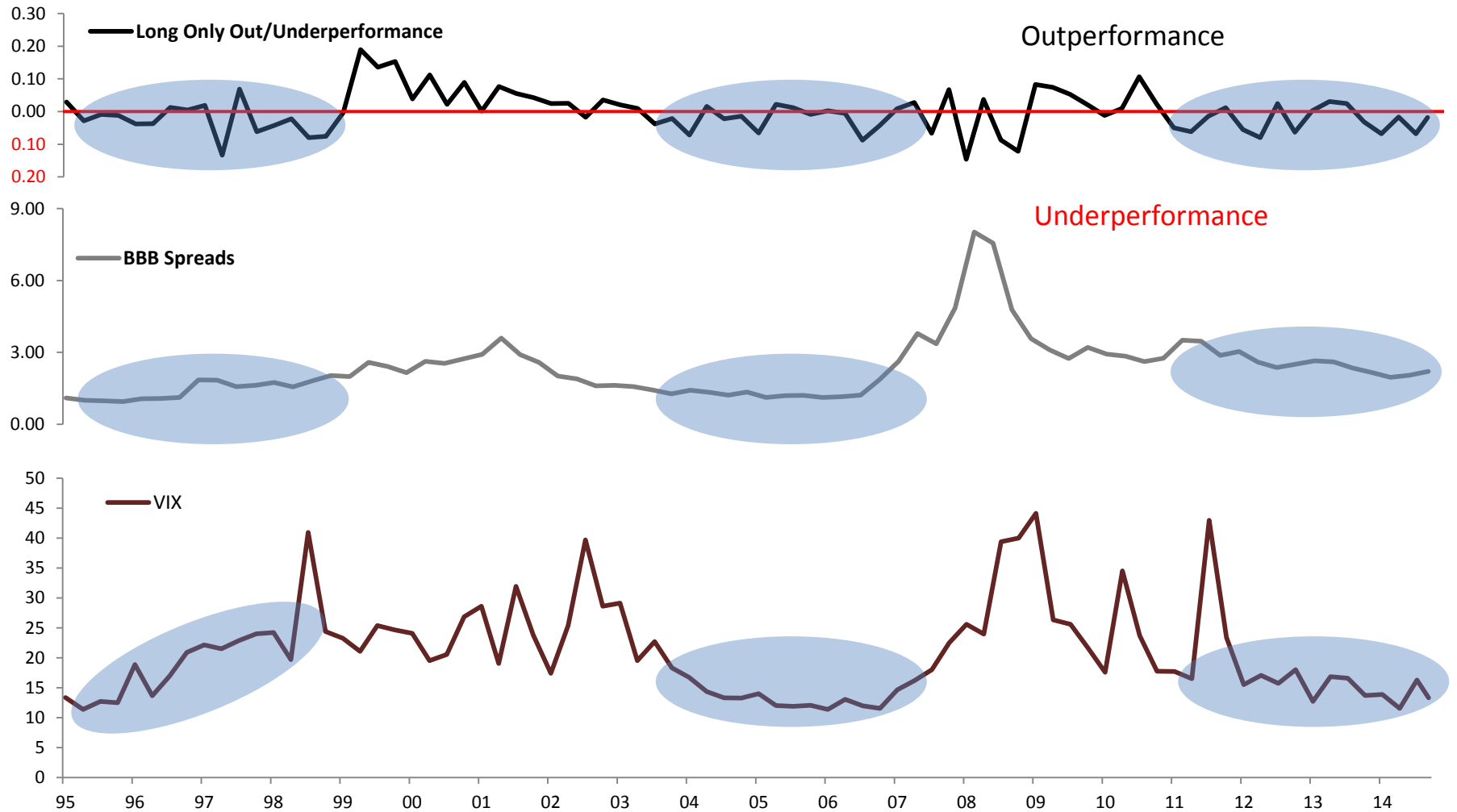
# Value Line Returns Were Flat



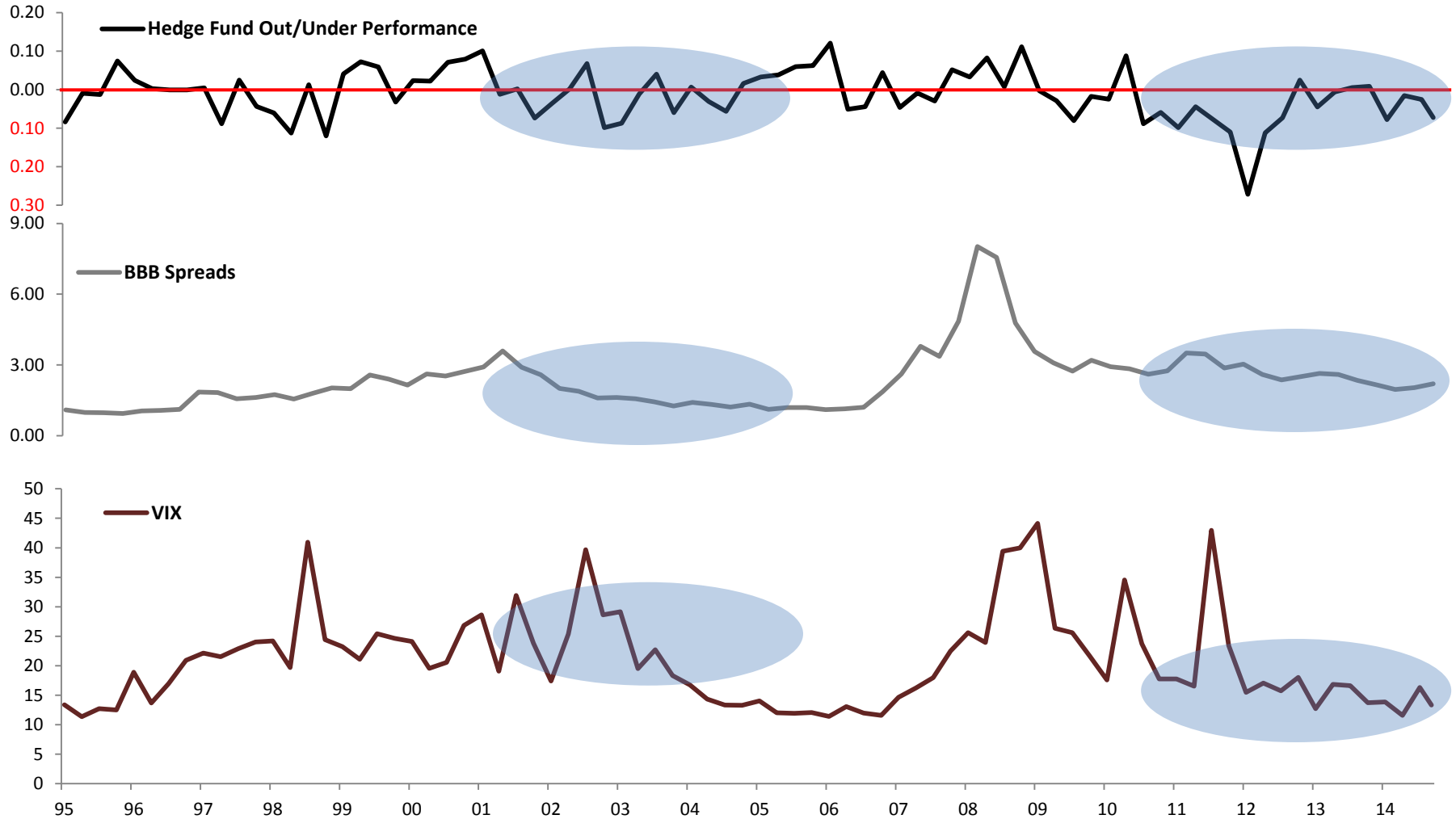
VALUG Index (Value Line Geometric) Relative to SPX

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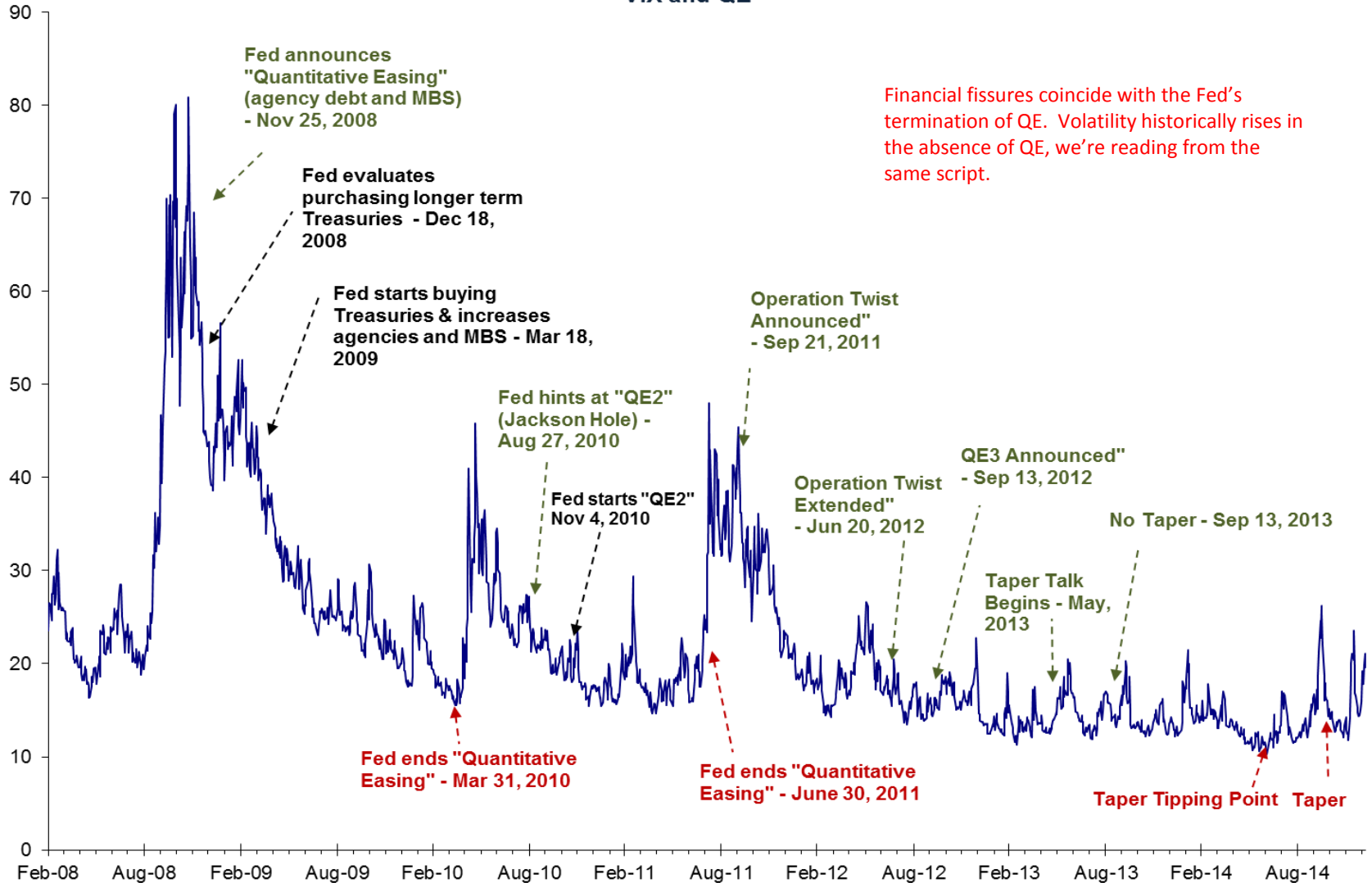
# Hedge Funds not as Consistent





# Is Today Really Different?

VIX and QE



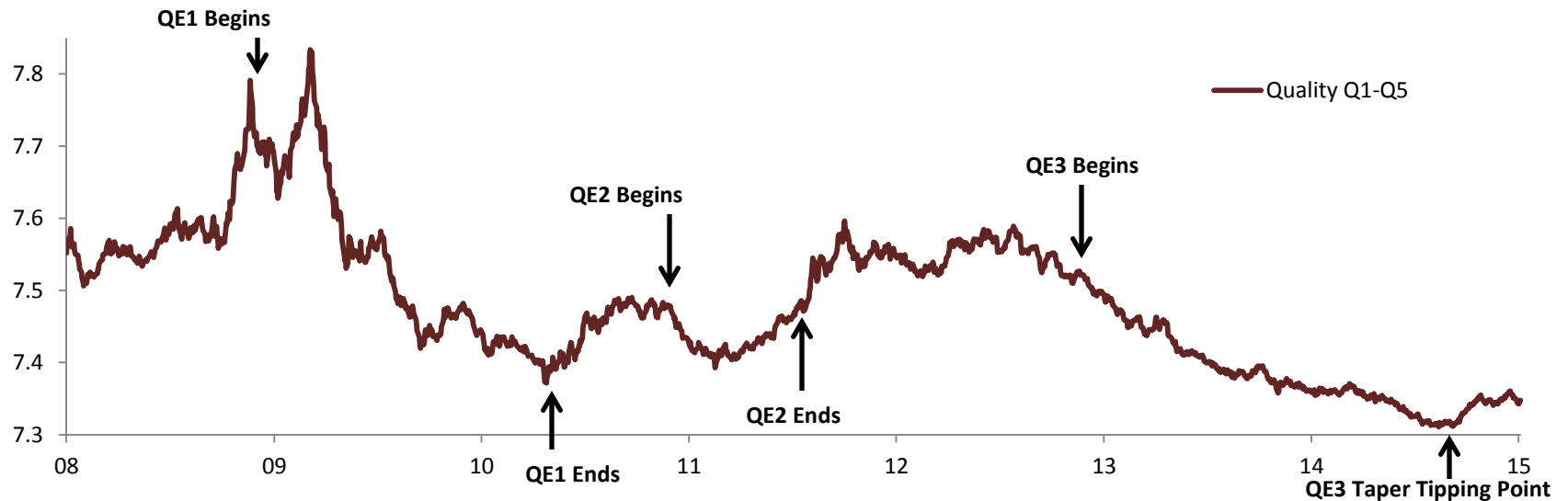
Financial fissures coincide with the Fed's termination of QE. Volatility historically rises in the absence of QE, we're reading from the same script.

# Spreads and Volatility are Linked

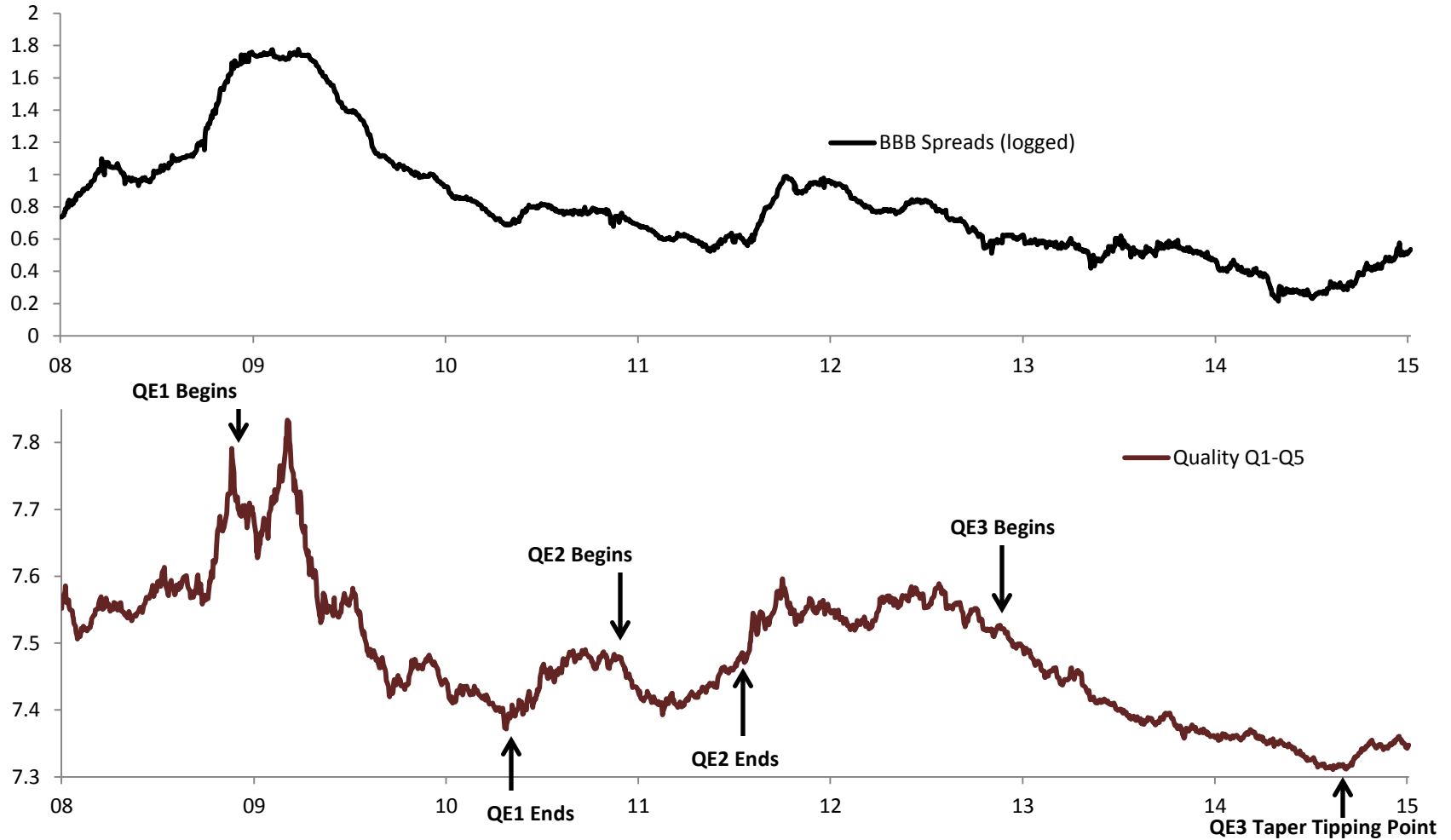


# Quality Outperforms Post QE

Why have active managers struggled? For starters, QE benefited all financial assets, but specifically low quality assets which tend to be over-owned by indexes and under-owned by active managers.

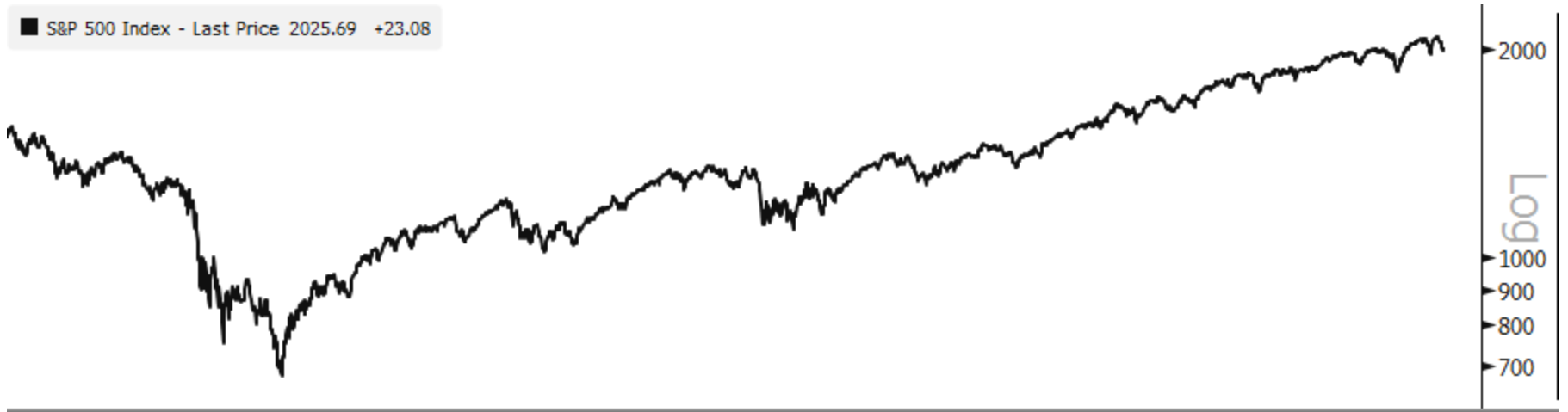


# Quality Linked to Credit



# BBB – BB Spreads Deteriorating

■ S&P 500 Index - Last Price 2025.69 +23.08



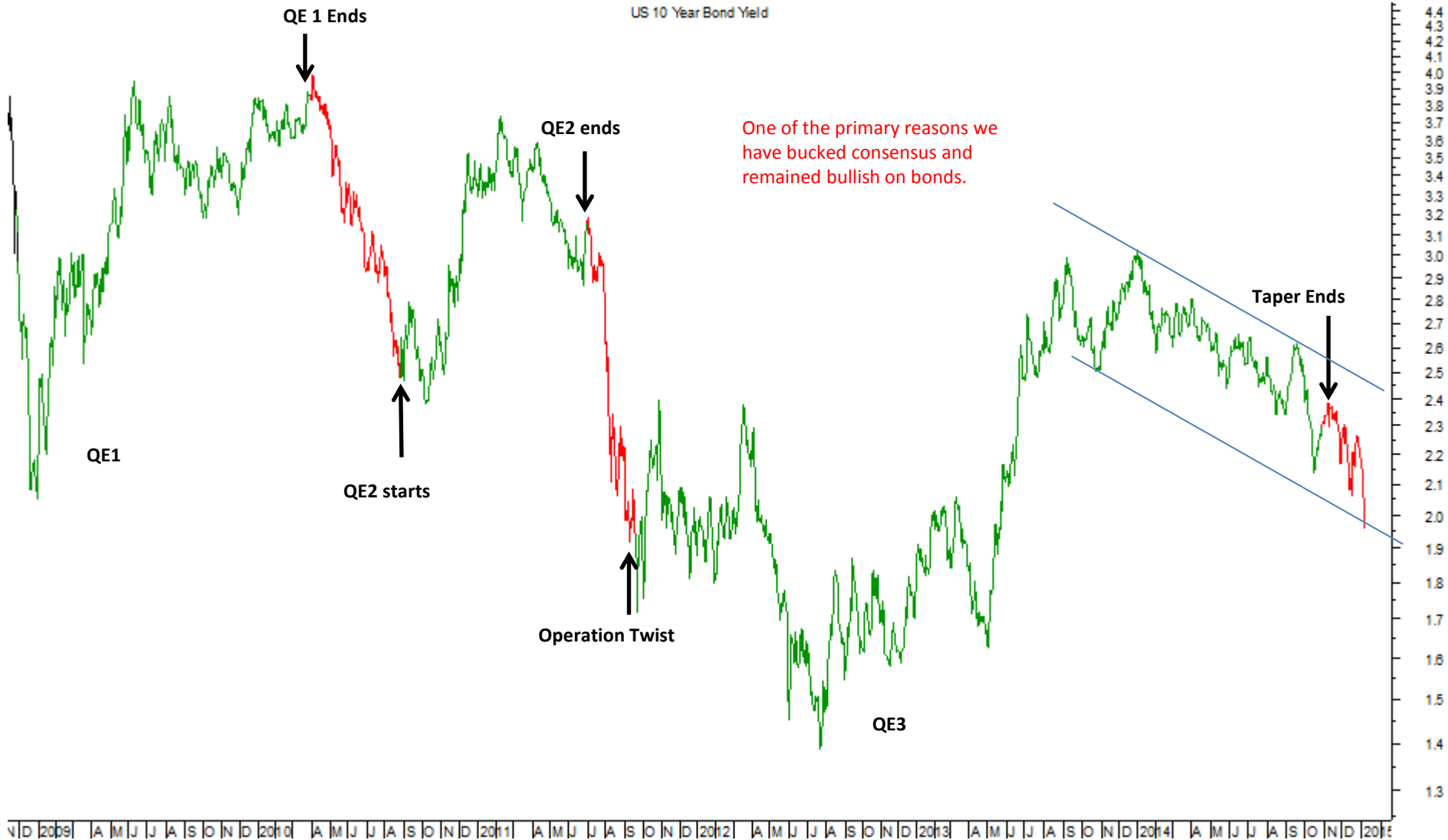
■ BFV USD Composite (BBB) 10 Year - BFV USD Composite (BB) 10 Year ... -2.0378 -.0795



# Low Volatility is Outperforming



# Yields Contract in Absence of QE

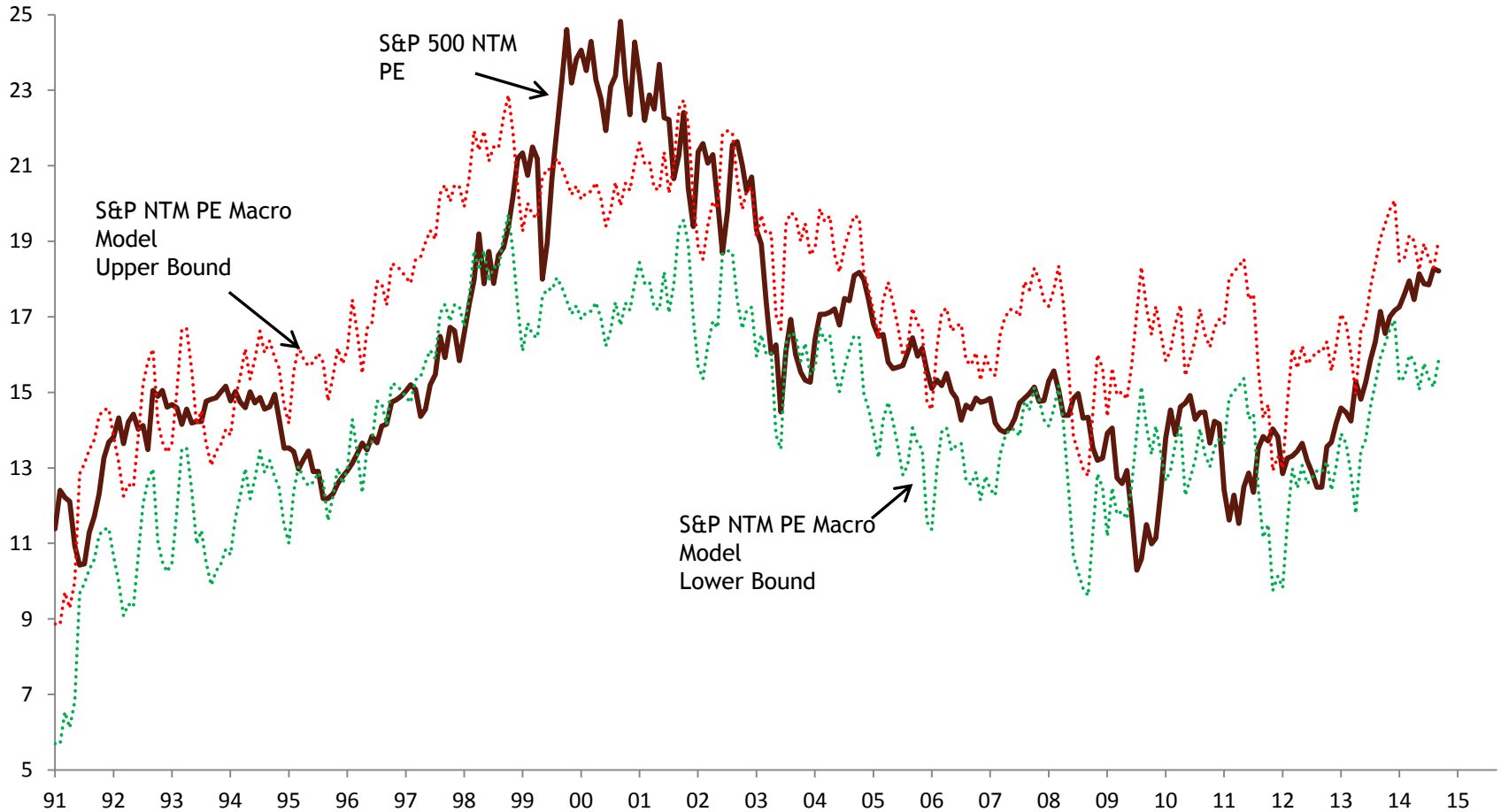


One of the primary reasons we have bucked consensus and remained bullish on bonds.

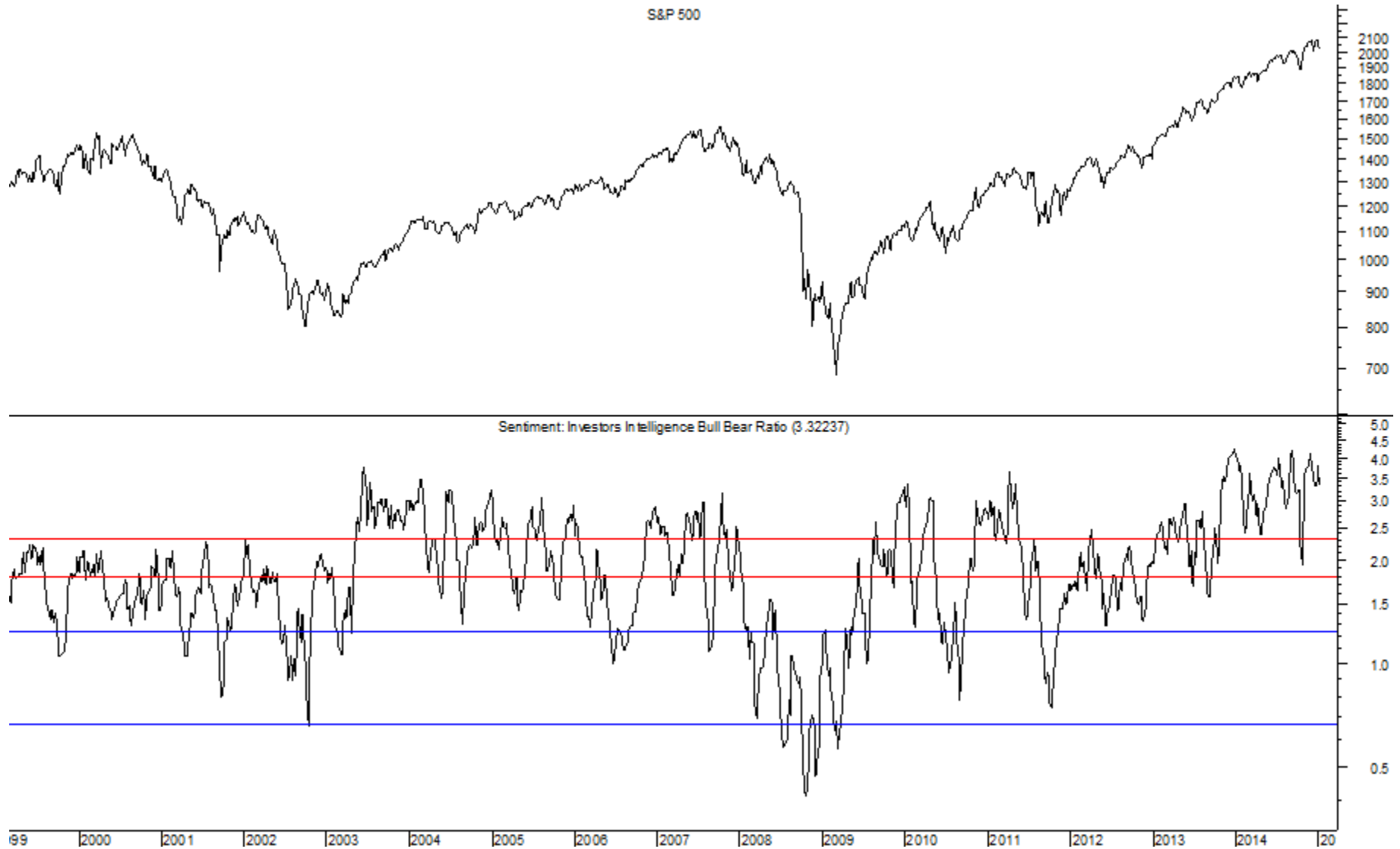




# Valuation at Top of Range



# Sentiment is Overly Optimistic



# US Bank CDS Premiums Trending

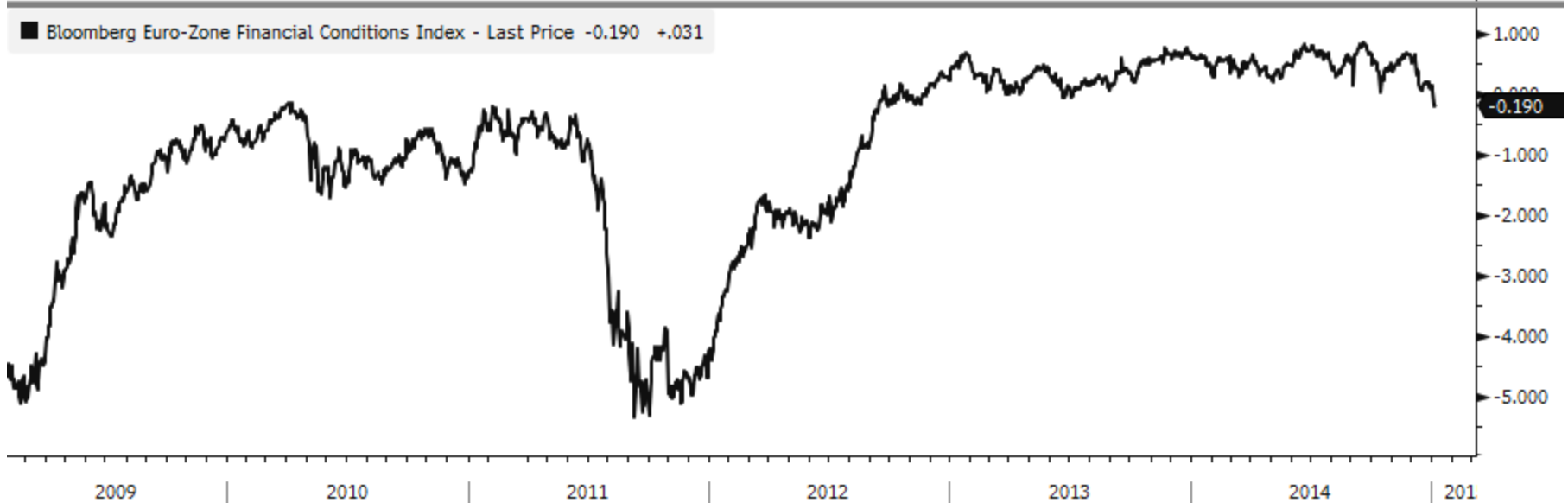


# Weak European Financial Conditions

■ STOXX Europe 600 Price Index EUR - Last Price 333.20 +1.59



■ Bloomberg Euro-Zone Financial Conditions Index - Last Price -0.190 +.031



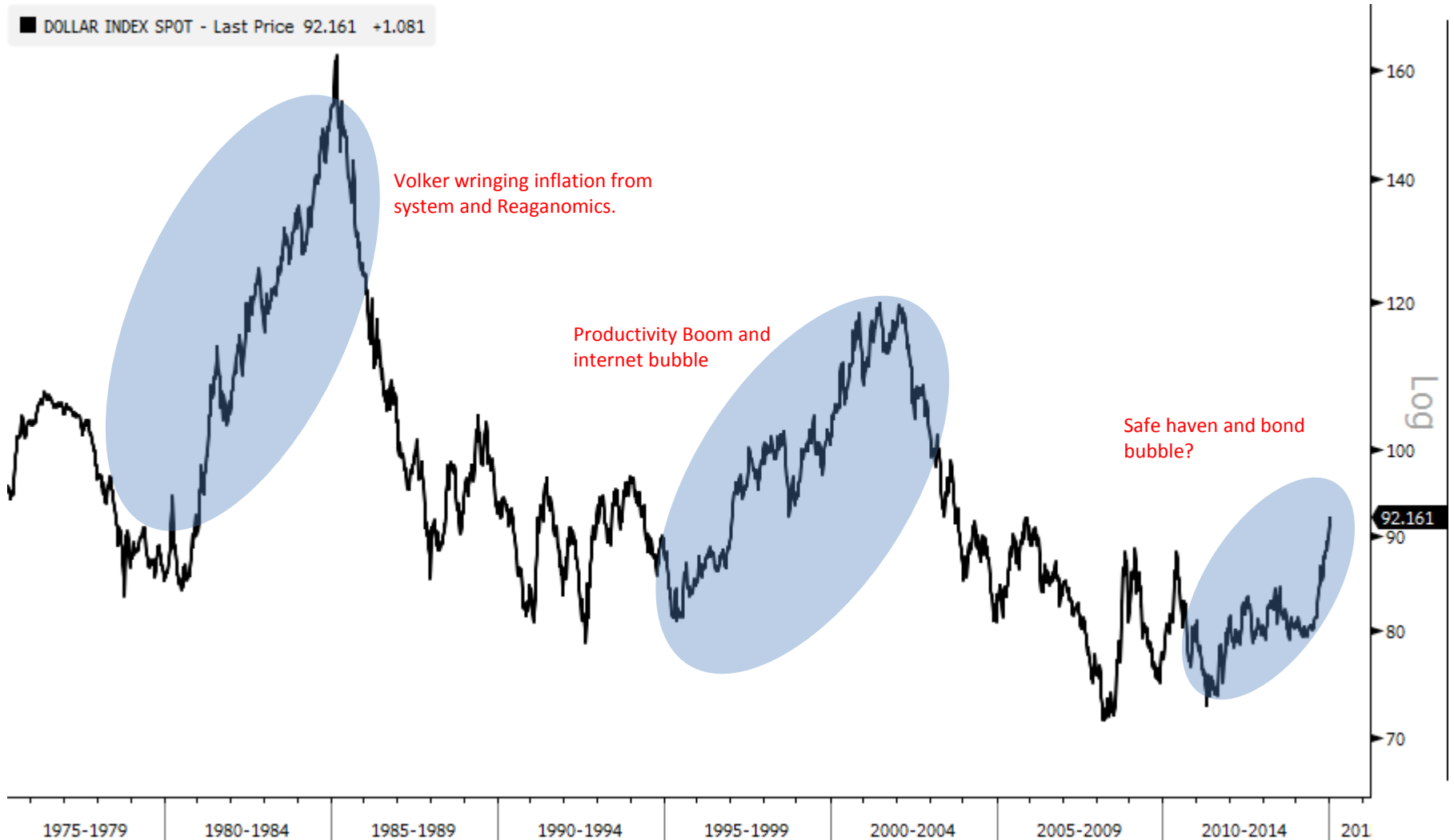
SXXP Index (STOXX Europe 600 Price Index EUR) Eur Bloomberg Fin Condtn Daily 09 Copyright© 2015 Bloomberg Finance L.P. 07-Jan-2015 12:14:49

# Buy Europe Only if Banks Improve



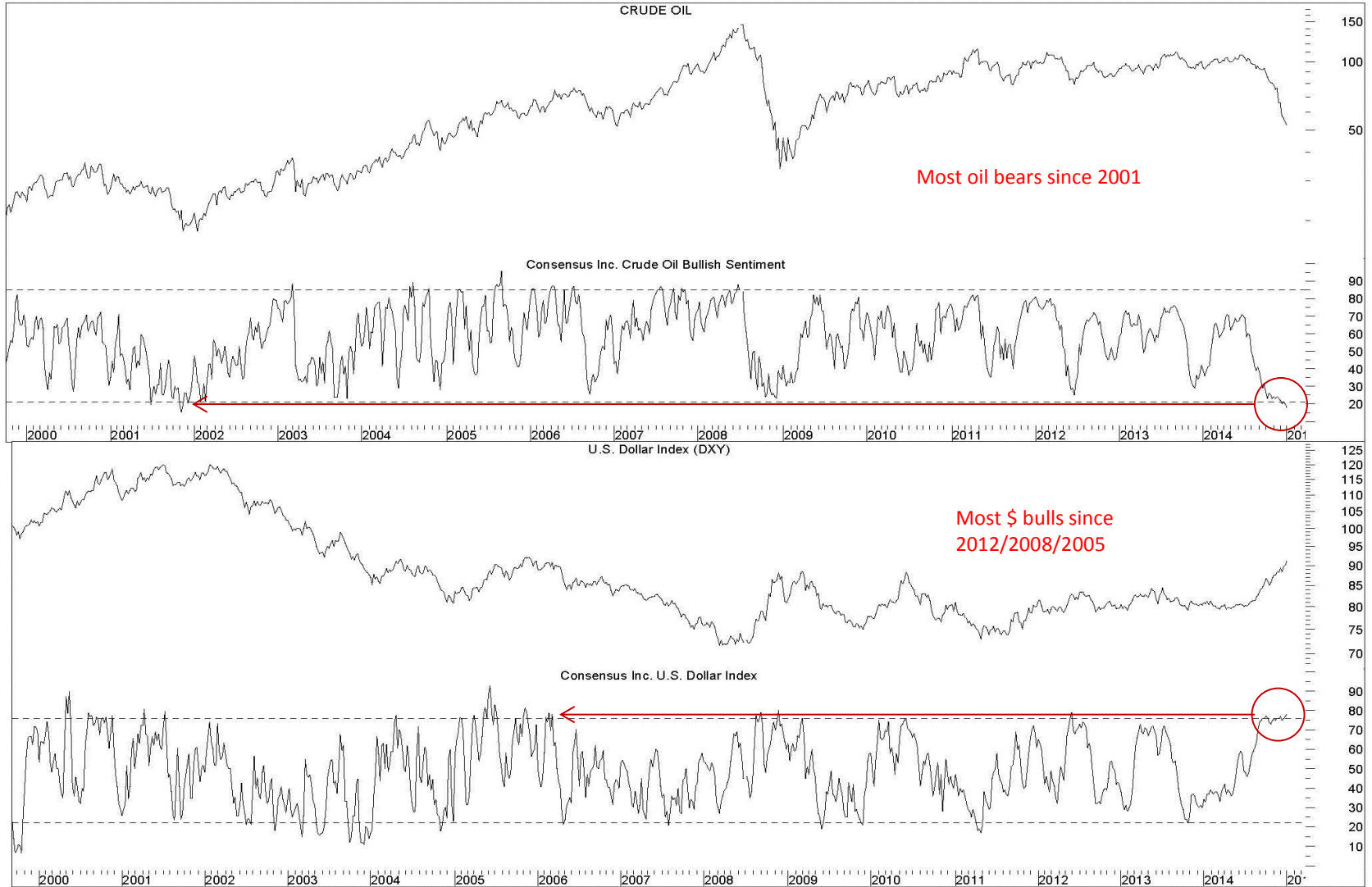
# Secular Dollar Move

■ DOLLAR INDEX SPOT - Last Price 92.161 +1.081



DXY Curncy (DOLLAR INDEX SPOT) Plain Long Term Weekly 09JAN2005-07JAN2015 Copyright© 2015 Bloomberg Finance L.P. 07-Jan-2015 12:02:38

# Pain Trades of 2015





- ❖ We believe the shift in attribution that began in July of 2014 signifies a tone change in the underlying dynamic of equity markets.
- ❖ We believe this tone change is driven by the removal of Q.E. by the central bank, and would specify the \$45B-35B level of monthly stimulus as the tipping point.
- ❖ We believe the termination of QE will have an impact on stocks and bonds that may or may not be seen in the economy at large.
- ❖ Specifically high quality, low volatility, dividend paying stocks with high net-interest margins should work.
- ❖ Bond yields are likely to remain low for the year (1.5- 2.5%)
- ❖ Active management is likely to have it's first advantage in years as volatility and credit suggest a less benign environment for equity indexing
- ❖ Our Credit/QE model (which takes into account Fed balance sheet changes) suggests a fair value of 1900 on SPX
- ❖ We like the idea of being contrarily bullish on Europe and EM, but believe such calls are premature without improvement in European bank equities and improvement in EM currencies.



# Thank you for joining us!

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Committed exclusively to providing Wall Street with specialized macro research, the founders of Renaissance Macro Research (RenMac) are dedicated to deciphering and understanding the macro factors that impact the investment world. Whether it is policy out of Washington, investment preferences within the equity markets, or the odd, but influential data point out of economics, RenMac is devoted to providing its clients with differentiated macro analysis through a dedicated sales & trading team focused exclusively on the research product.



**Jeff deGraaf, CFA, CMT - Chairman & Head Technician**

Jeff deGraaf is RenMac’s Chairman and Head Technical Analyst. Jeff has turned his style and philosophy of sell side research into a core value at RenMac. Ranked by Institutional Investor magazine for the last 14 years, with 10 of those as the #1 Technical Analyst, Jeff’s passion for markets and understanding of the world’s idiosyncrasies help to separate him from the herd. Jeff spent the early part of his career at Merrill Lynch and then Lehman Brothers, where he served on the firm’s investment policy committee as a Managing Director. In 2007 he moved to ISI as an Executive Managing Director, serving on the firm’s management committee and heading the firm’s investment policy committee. Jeff is a CFA and CMT charter holder and a member of the NYSSA and MTA.



**Rob Ginsberg - Small Cap Strategy & Sector Deep-Dives**

Rob Ginsberg is a member of the Technical Analysis team and heads-up Small-Cap Strategy and Sector Deep-Dives. He brings extensive technical and fundamental experience to the team. Prior to joining RenMac, Rob was a managing director at ISI Group, where he was also a member of Jeff’s Technical team. Before joining ISI in 2009, Rob spent 13 years at Alliance Bernstein, where he was a Senior Vice President and Portfolio Manager of growth equities. He received his MBA in Finance from Fordham University in 2003 and his B.A. in Economics from the University at Buffalo in 1995



**Alex Meintel - Resources Deep-Dives (Commodities, Energy & Materials)**

Alex Meintel is a member of the Technical Analysis team and heads-up RenMac’s Commodity Research. Prior to joining Renaissance Macro, Alex was an associate at ISI Group where he was a member of Jeff’s Technical Analysis team. Before joining ISI in early 2009, Alex played professional hockey in Germany. He graduated from Harvard University with a B.A. in Government.



**Neil Dutta - Head U.S. Economics**

Neil Dutta is RenMac’s Head of Economics. In this role, he analyzes global economic and cross market themes. Prior to his current role Neil spent 7 years at Bank of America-Merrill Lynch, where he was a Senior Economist with responsibilities for both the United States and Canada. Before that, he was an analyst at Barron’s. Neil graduated cum laude from New York University in 2005 with a B.A. in Economics and Political Science. Neil appears frequently in financial media, including Bloomberg TV and CNBC as well as being quoted by Barron’s, the Wall Street Journal, and Bloomberg News



**Kim Wallace - Head of Washington Policy Research**

Kim Wallace is the head of RenMac’s Washington Research Group. Before joining RenMac, Kim served as Treasury Assistant Secretary for Legislative Affairs, where he worked alongside Treasury Secretary Timothy Geithner. Prior to The Treasury Department, Kim spent over a decade at Lehman Brothers and Barclays Capital heading up Washington Policy Research. During his time at Lehman, Kim was ranked by Institutional Investor magazine 9 times. Kim received a Bachelor’s Degree from the University of Texas at Austin, and a Master’s Degree from The Johns Hopkins University.



**Stephen Velgot – Head of Events Driven Research**

Steve Velgot comes to RenMac with over 20 years’ experience to lead our Event Driven research product. His focus is mainly in the corporate action arena, with an expertise in situations such as spin-offs, split-offs, Dutch Auctions, strategic alternatives exploration, risk arbitrage, relative value and shareholder activism, among others. While we try to be mindful of all market relevant events, Steve has tended to spend less effort on mainstream events that are over covered by the street, and has been more well-known for finding events off the beaten path that can add value.

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- |   |  |
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RenMac executes agency-only, equity trading transactions through its wholly-owned institutional broker-dealer subsidiary, Renaissance Macro Securities, LLC. RenMac is not a market-maker and does not trade for its own account and clears customer transactions through Broadcort, a division on Merrill Lynch.