



Monday Morning Research Notes

March 6, 2017

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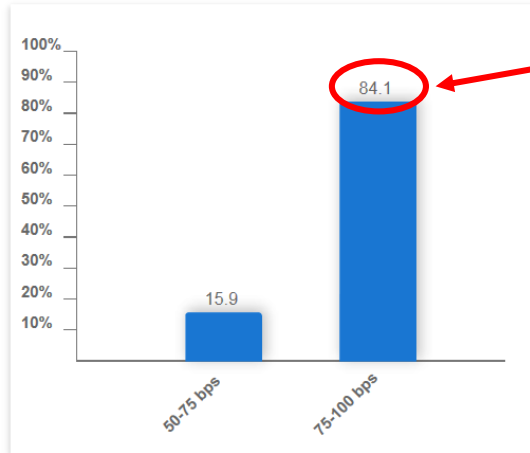
Major economic & market developments for the week ended 3/3/17

- Fed poised to hike interest rates at their meeting next week; news conference Wed. 3/15/17
- ISM and inflation stats show economy strengthening
- Chinese currency reserves dropping, new fiscal policies coming
- We foresee an increase in the Labor Force Participation Rate
- Data storage: hard drives survive and grow – an opportunity for capital appreciation
- Market breadth hits momentum low for 2017, without significant price damage in Indexes
- S&P 500 uptrend in-tact with possible short-term exhaustion gap on Trump's speech
- Even with cut, Merrill continues to charge premium pricing
- **Featured Company**: Investment management firm paying a 6.2% dividend with 47% upside potential to our 24 month price target

High probability of interest rate hike next week

CME Group
FedWatch Tool

Meeting date: Wednesday, 15 Mar 2017



Graph courtesy CME Group

Investors now see an 84% chance of the Fed hiking rates next week...

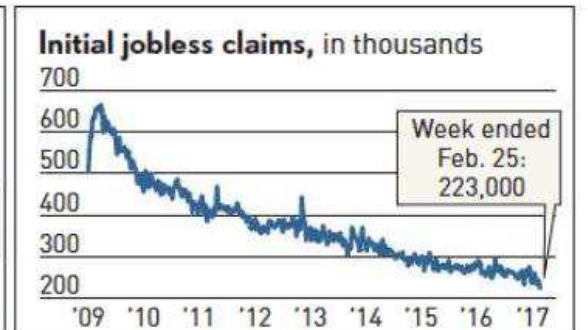
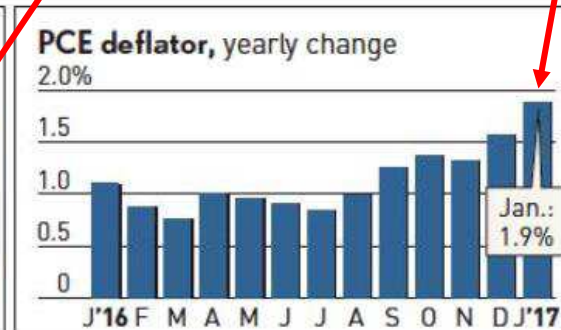
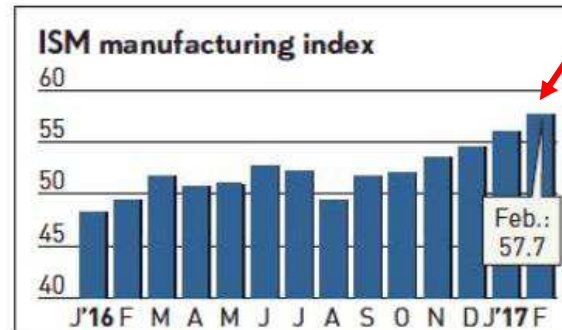
Likely due to strong ISM and inflation statistics

VITAL SIGNS

Here's Why The Fed Is Ready To Hike

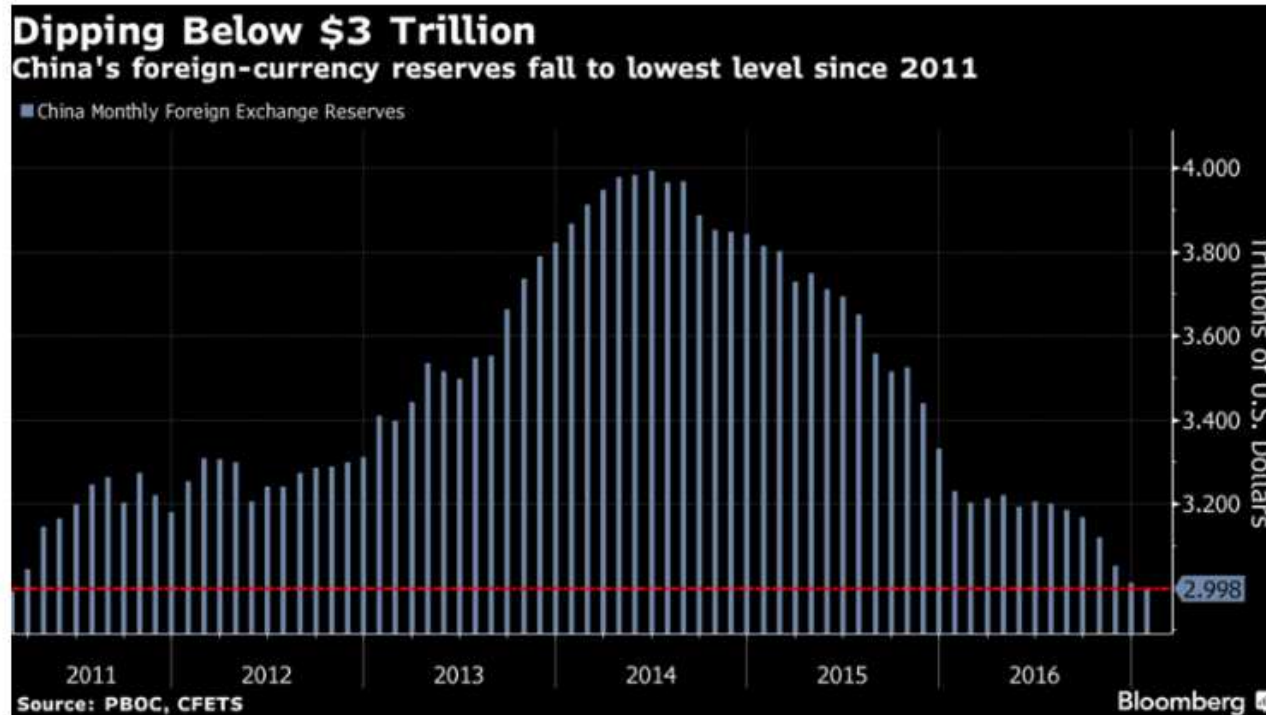
Several Federal Reserve policymakers appeared to back a March rate hike, and here's why. An ISM manufacturing index hit a 2-1/2-year high, the Fed's favorite inflation gauge rose to a 4-year high and jobless claims tumbled to their lowest in nearly 44 years.

Sources: Institute for Supply Management, Commerce Dept., Labor Dept.



Graph courtesy Investor's Business Daily

Chinese reserves dropping, new fiscal policies coming...



In China, we see:

- PMI & mfg data higher
- Corporate bankruptcies increasing
- Gov't forcing a new rationality
- Continuing transition to consumer economy
- Capital controls tightening
- Property market cooling

Further erosion of the world's largest stockpile may prompt policy makers again to tighten measures for controlling outflows and on companies transferring money to other countries. Authorities recently rolled out stricter requirements for citizens converting yuan into foreign currencies as the annual \$50,000 foreign exchange quota for individuals reset Jan. 1.

We foresee an increase in the Labor Force Participation Rate



After an accelerated decline since 2008, we see a reversal of the trend here, due to:

- **Potential changes in entitlement plan eligibility**
- **Overall increase in economic growth rate**
- **Increasing demand for labor**

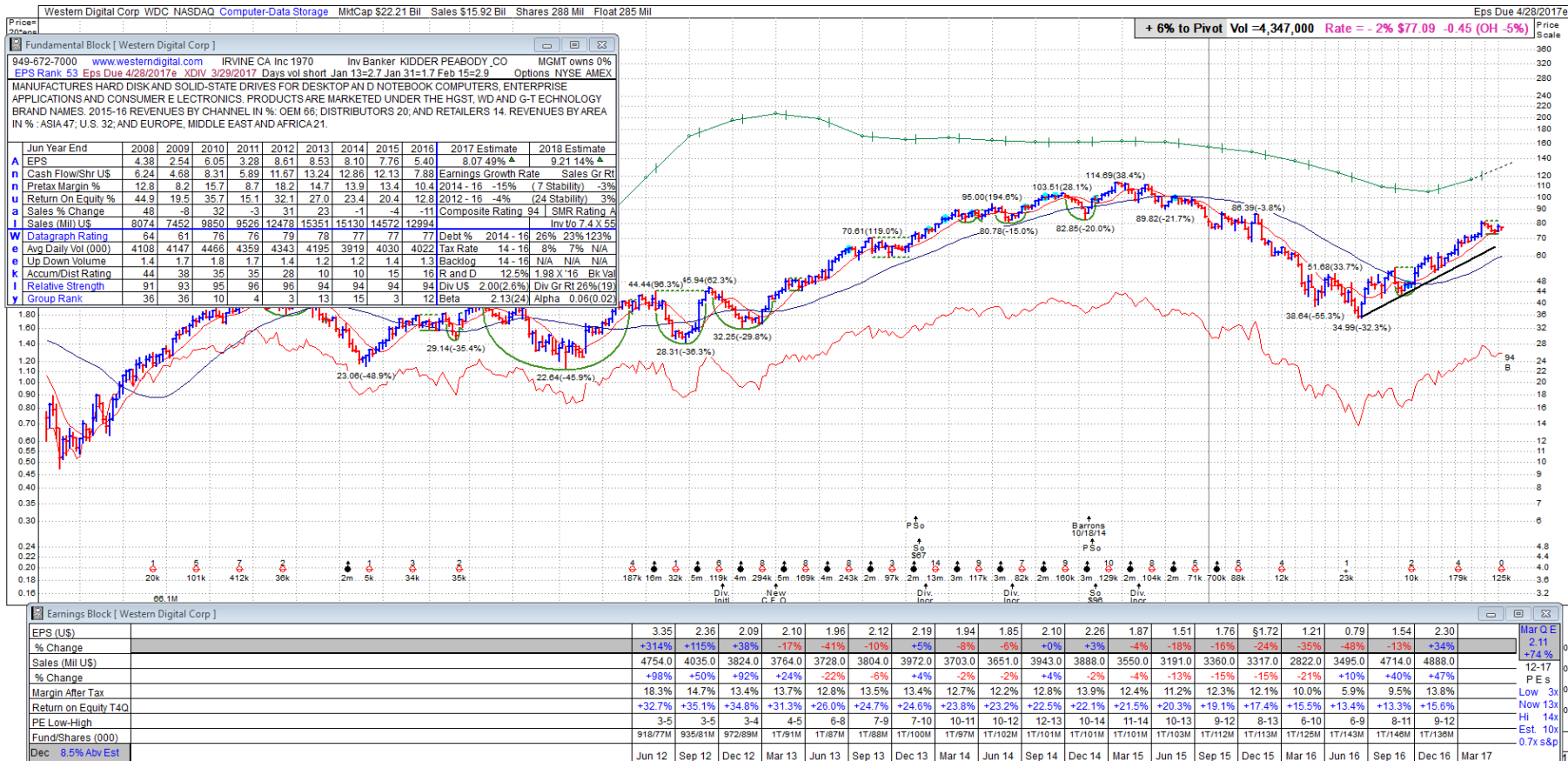
If the participation rate increases, it will mute labor cost pressures.

Data Storage – hard drives survive & grow

DATA-STORAGE DEVICES

Hard Drives: At Home In The Cloud

Flash memory is overtaking consumer markets, but cloud and data centers stick with disks



2018 earnings estimate for WDC: \$9.21

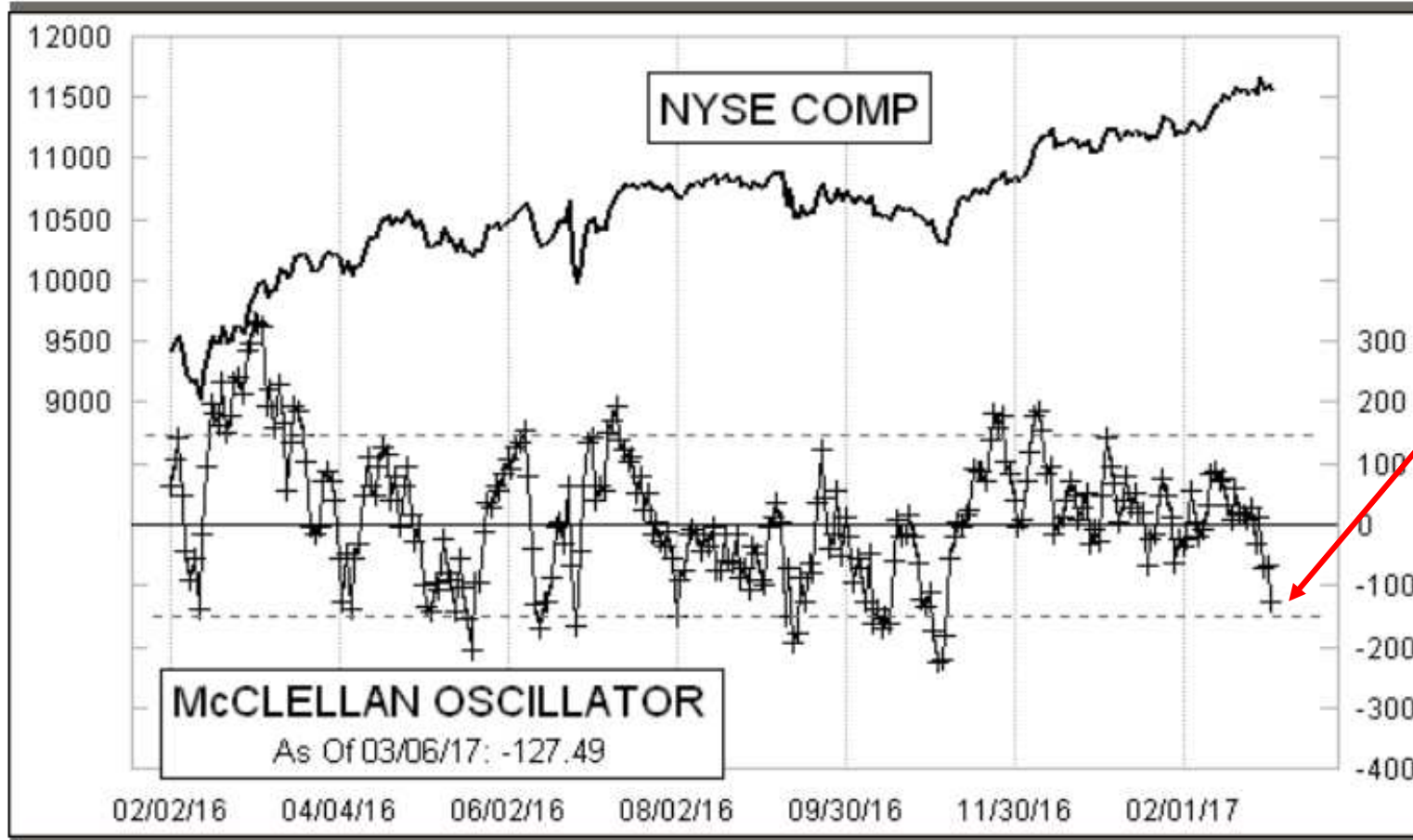
at 10x estimate= \$92.10

Or approximately 20% upside to current price

(vs. no upside for STX and NTAP at 10x 2018 earnings estimates)

Graph courtesy of William O'Neil + Co, Inc.

Market breadth hits momentum low for 2017



Market breadth hits momentum low for 2017, with very little price weakness...

In our view, this is a positive indicator for the uptrend continuing.

Graph courtesy McClellan Financial Publications

Even with cut, Merrill continues to charge premium pricing

Merrill Lynch cuts its top rate on fee accounts

Reduction from 2.7% to 2.2% could save smaller clients \$5,000 a year

Feb 24, 2017 @ 12:26 pm
By InvestmentNews



(Bloomberg News)

Merrill Lynch has lowered its top charge on fee-based accounts to 2.2% from 2.7%, a move that could save smaller investors as much as \$5,000 a year, **The Wall Street Journal** reports.

The reduction affects clients with under \$1 million in assets at the firm. Those clients with \$1 million to \$4.9 million in assets will continue to pay a maximum of 2.2%, while investors with \$5 million or more in assets will continue to pay a top rate of 2%.

Last year, Merrill began a process of changing its brokerage accounts, making its fee structure more transparent and, in some cases, less expensive, the Journal story said.

As a result of its decision last October to stop accepting commissions in retirement accounts, Merrill customers with such accounts soon will be required to choose between moving their IRA to a fee-based account or to a commission account at the firm's online Merrill Edge unit.

**Versus our fees:
\$1 mil to \$5 mil
we charge 1%
(approx. ½ of
Merrill Lynch)**

Recent position added for potential income and capital gains



MktCap \$4.20 Bil Sales \$1.97 Bil Shares 187 Mil

Price = 20.00

INVESTS IN AND MANAGES FUNDS RELATED TO VALUE-ORIENTED PRIVATE EQUITY, CREDIT-ORIENTED CAPITAL MARKETS AND REAL ESTATE ON A CONTRARIAN BASIS WITH OFFICES LOCATED IN NORTH AMERICA, EUROPE AND ASIA. SERVES PENSION AND ENDOWMENT FUNDS, AND INSTITUTIONAL AND INDIVIDUAL INVESTORS. 2016 REVENUES IN %: MANAGEMENT FEES FROM AFFILIATES 53; CARRIED INTEREST FROM AFFILIATES 40; AND OTHER FEES 7. 2016 ASSETS UNDER MANAGEMENT: \$ 192 BIL, UP 13% FROM 2015.

Dec Year End	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017 Estimate	2018 Estimate
EPS	-7.27	-1.24	0.75	-3.74	2.06	4.03	0.62	0.61	2.11	2.28 8%	2.75 21%
Cash Flow/Shr US\$	N/A	N/A	N/A	-3.40	2.67	4.88	1.31	0.99	2.27	Earnings Growth Rate	Sales Gr Rt
Pretax Margin %	1097.5	N/A	30.1	N/A	108.9	66.5	56.2	36.2	53.8	2014 - 16	-30% (99 Stability)
Return On Equity %	N/A	N/A	N/A	N/A	18.3	24.9	7.6	11.0	54.3	2012 - 16	-28% (99 Stability)
Sales % Change	-142	-462	118	-92	1566	31	-58	-33	89	Composite Rating	93 SMR Rating A
Sales (Mil) US\$	967	2110	172	2860	3734	1560	1042	1970			
Datagraph Rating	81	81	78	78	90	83	82	88	88	Debt %	2014 - 16 84% 281% 256%
Avg Daily Vol (000)	884	964	973	982	1107	1170	1228	1381	1436	Tax Rate	14 - 16 17% 7% 9%
Up/Down Volume	1.4	1.2	1.1	1.2	1.8	1.3	1.3	1.8	1.8	Backlog	14 - 16 N/A N/A
Accum/Dist Rating	62	42	29	45	62	26	33	54	58	Div D	14 - 16 5.09 X '16 Bk Val
Relative Strength	84	81	81	82	88	81	80	84	87	Div US\$	1.42 (6.2%) Div Gr Rt -2% (58)
Group Rank	79	67	89	105	95	95	92	95	87	Alpha	0.04 (0.03)

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