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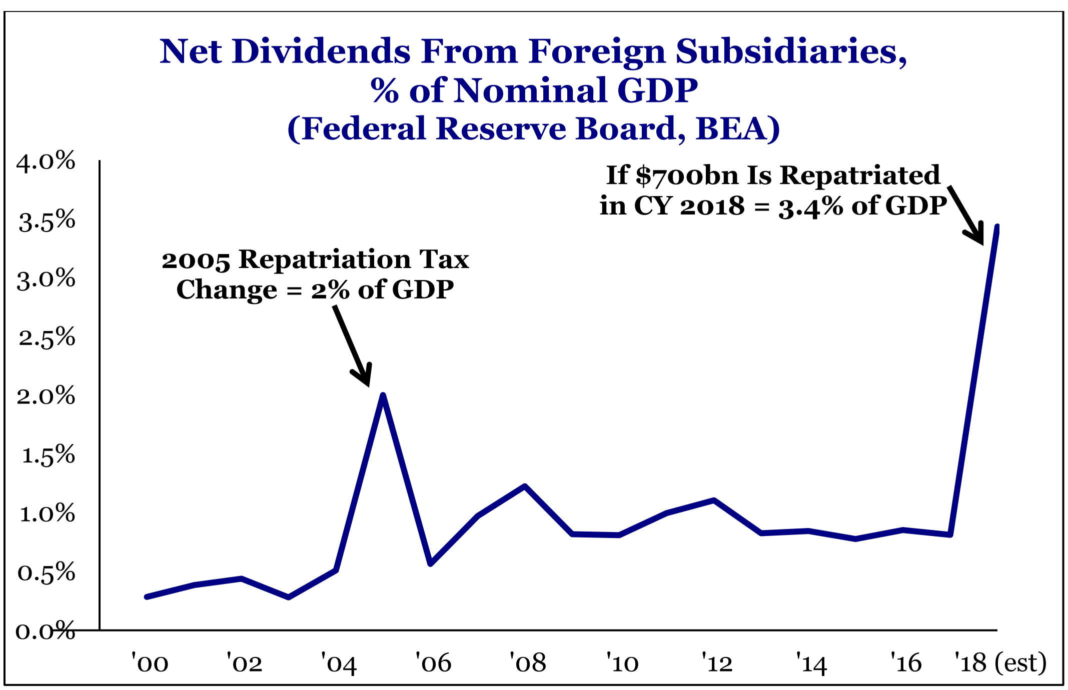
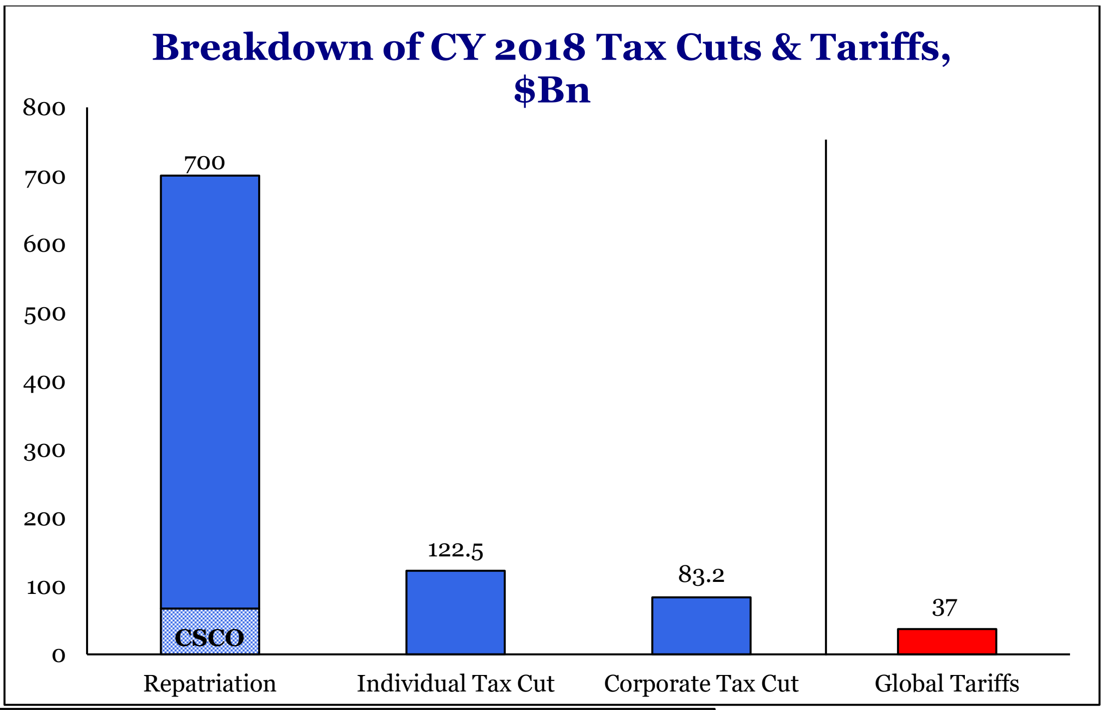
IT'S RAINING MONEY IN THE UNITED STATES

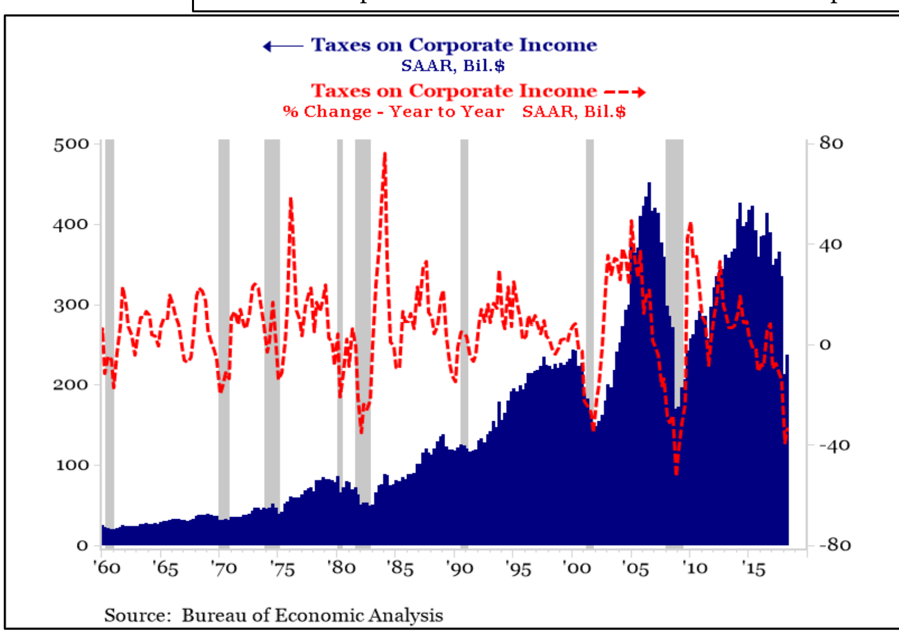
We try to stay away from hyperbole the best we can so please forgive the title of today's report. But after looking at the corporate profit data yesterday, it became clear that our 2018 theme, "shock and awe" fiscal policy, is even greater than we expected. In light of the data coming in, it's no surprise that estimates for Q3 GDP are being ramped up and stocks are making all-time highs while impeachment is all of the rage on cable news. My colleague Courtney Rosenberger, Strategas' policy quant ace, backed out gross foreign transfer data from yesterday's GDP report to estimate 2Q net repatriations. Courtney estimates US companies repatriated another $200bn in 2Q (we get confirming data in mid-September), which brings total repatriations to $500bn in the first half of the year. In the first six months of the year we hit the low range of our CY estimate and it is likely that we will hit the top end of our estimate of $700bn this year. These repatriations come on top of $120bn of tax cuts for consumers, $80bn of tax cuts for companies, and $100bn of new federal spending set to hit in CY 2018. **We are trending at around $1 trillion of fiscal policy in CY 2018 coupled with growing after-tax corporate profits**. In our view there is no way all of that money can be allocated this year. Taken together, there is a chance that growth continues to surprise to the upside into 2019 as this cash is deployed.



PLACING THE SHEER MAGNITUDE OF REPATRIATIONS IN CONTEXT

Yesterday's GDP report showed that corporate taxes are down 33 percent year-over-year and running consistent with our estimate of a net $83.5bn corporate tax rate cut in CY 2018. This has helped lift after-tax, total corporate profits 16 percent year-over-year. Placing this in context, an $83bn tax cut has boosted corporate profits 1,200 basis points. By comparison, Cisco alone repatriated $67bn this year, nearly the size of the entire corporate tax rate cut for every company. And while both the financial and corporate press declare trade is destroying the global economy, the total amount of global tariffs that will be implemented in CY 2018 is just $37bn.

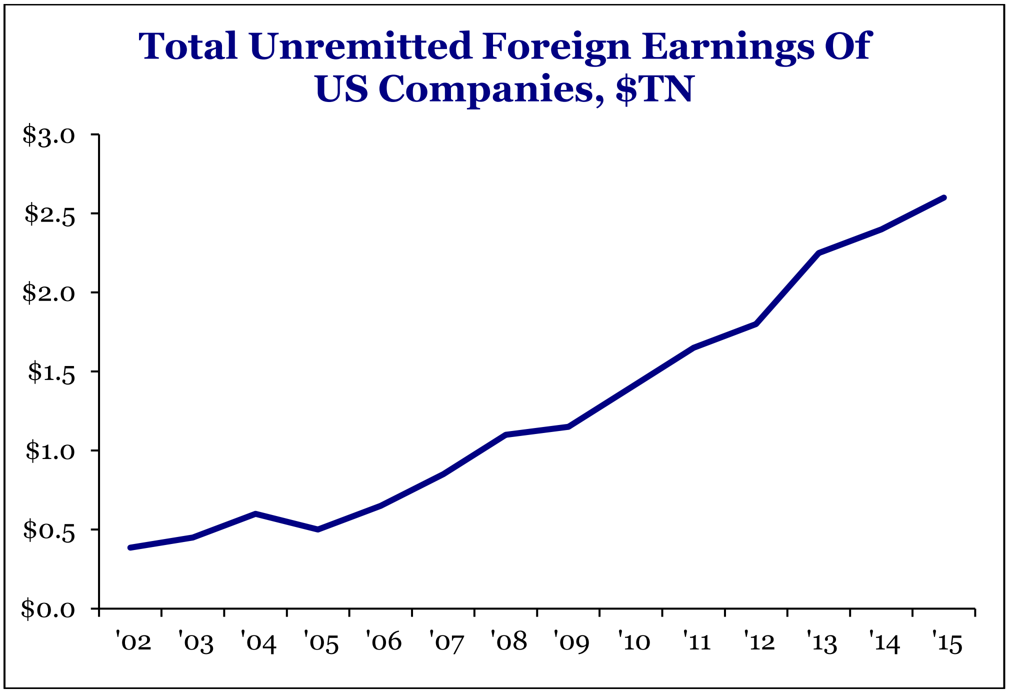


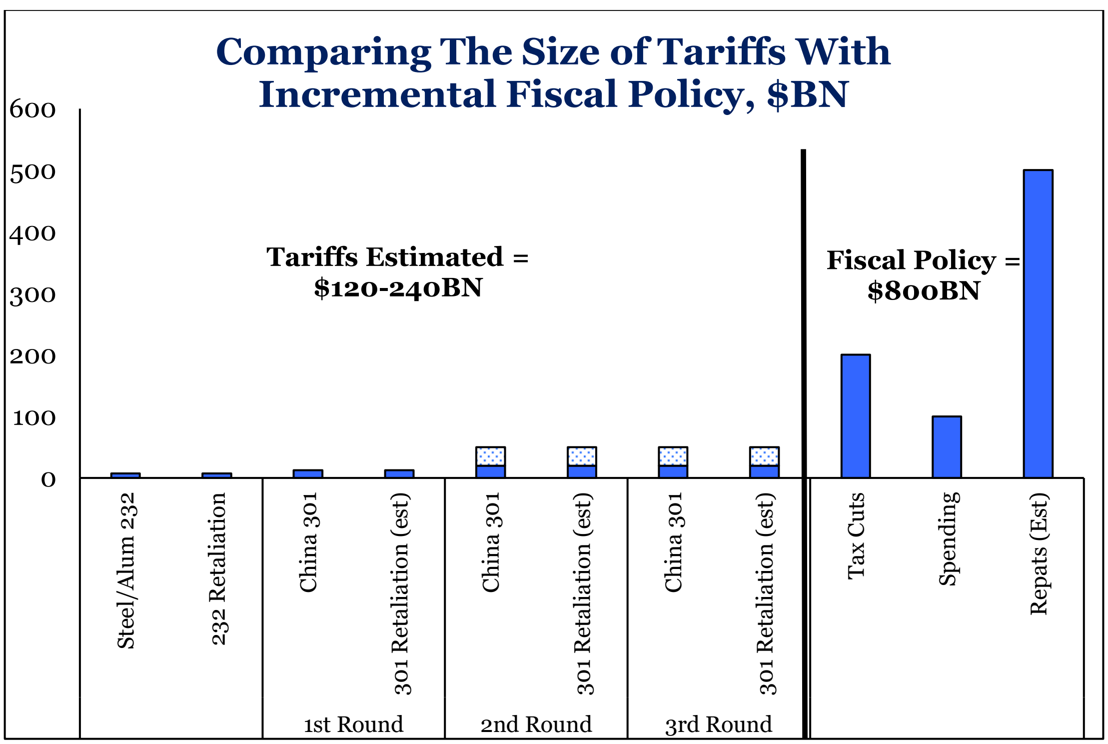


Corporate tax collections are falling as the tax rate cut kicks in. Repatriation is seven times the size of the corporate tax rate cut.

STILL PLENTY OF CASH TO COME BACK TO THE US

US companies accumulated $2.6 trillion of unremitted foreign earnings prior to tax reform. Of that amount, we estimate companies held $1.7 trillion of cash overseas available for repatriation. In 2005, the last time Congress had a repatriation tax holiday, companies held $600bn overseas, and $300bn was returned. The major difference between 2005 and today is that today is a mandatory repatriation tax as part of tax reform. As such, we expect even more repatriations in the coming years as companies decide how to best allocate their cash.





In light of the new data we will need to upgrade the amount of repatriations in this chart. We had been using $500bn. We will upgrade this to $700bn and total fiscal policy will equal $1 trillion.

COMPANIES ARE USING REPATRIATED CASH TO PAY DOWN DEBT AND INCREASE PENSION CONTRIBUTIONS

Companies Race To Top Off Pension Plans To Capitalize On Tax Break

Companies with underfunded pensions have a rare opportunity to score a tax break in the coming months. **Pension contributions made through mid-September can be deducted from income on tax returns being filed for 2017—when the U.S. corporate tax rate was still 35%…This one-time incentive is helping corporations close a pension funding gap that topped $680 billion for S&P 1500 companies after the financial crisis**, according to consulting firm Mercer. "There will be a bit of a race to get in underneath the wire," said Michael Moran, pension strategist for Goldman Sachs Asset Management. "We're seeing a lot of contributions pulled forward." Shipping company United Parcel Service Inc., construction equipment-maker Deere & Co. and defense company Lockheed Martin Corp. , among others, have made or announced contributions worth billions of dollars to their defined-benefit pension plans ahead of the cutoff date, citing the tax law among their reasons.

Wall Street Journal **6/21/2018**

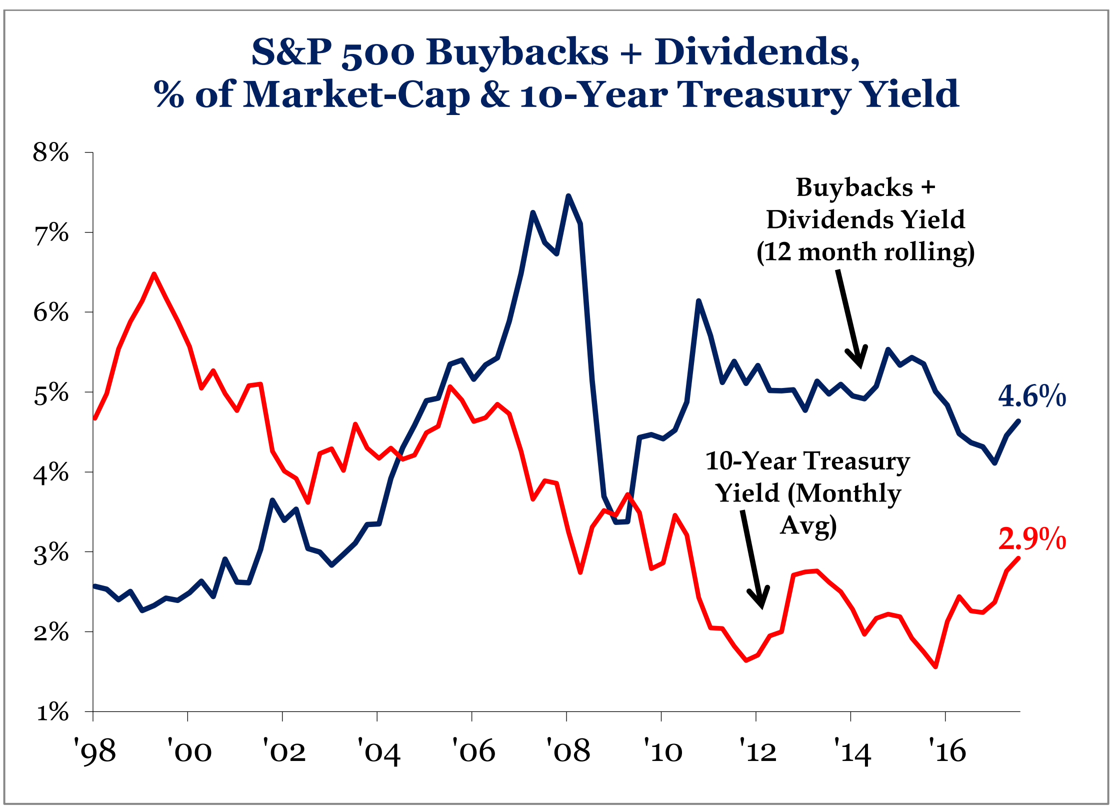
Courtney files through company statements and earning calls to see what companies are doing with their repatriated cash and she noticed more companies are citing paying down debt than any other use of cash. This would include paying down debt, not accessing debt markets when the company normally would, and/or increasing pension contributions. The tax bill specifically let companies make pension contributions through September at a 35 percent tax rate deduction to incentivize pension contributions. Our sense is that companies are using tax savings and repatriated funds for pensions. Post-September, we would anticipate other uses of cash will get attention.

S&P 500 Companies' Repatriation Plan Announcements & Comments

Use	Companies Which Discussed Use of Cash for Repatriation
Buybacks/Dividends	BEN, CSCO, ROK, ITW, CTXS, WAT, EMR, AOS, SWKS, LRCX, PFE, BIIB, PEP, JNPR, CTSH, SYMC, KLAC, ALGN, RMD, EBAY, APH, EA, A, CAT, MTD, NVDA
Paying Down/Reduce Usage of Debt	KO, SRE, UTX, ROK, CTSH, ITW, LLY, WAT, ALB, ROP, TRIP, GPN, IDXX, IT, AOS, MKC, GIS, CLX, GILD, BEN, MMC, PEP, SYMC, APH, COTY, CAT, MSFT
M&A	EMR, UTX, ROP, MAS, GIS, BEN, BIIB, MMC, JNPR, CTXS, FTV, RMD, APH, A, NVDA, WBA, MSFT
Funding US Operations/ Liquidity Requirements	JNJ, BK
Investing in Business/Capex	PFE, PEP, JNPR, KLAC, ALGN, CAT
Pension Funding	PEP

HARD TO FADE STOCKS WHILE SHAREHOLDER YIELD IS INCREASING FROM REPATRIATIONS

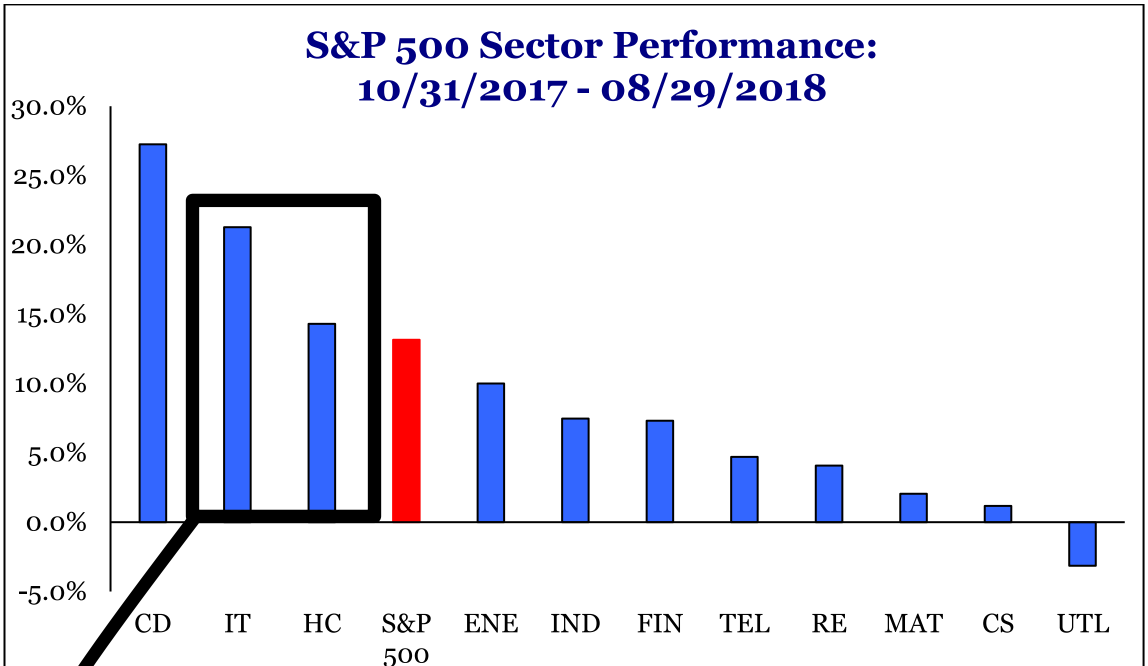
Some will argue repatriation is an accounting trick and there is no net benefit. Others will argue that the use of cash is exclusively for buybacks which limits growth. We disagree. We are talking about 3.5 percent of GDP. Even if every dollar is used inefficiently, it's going to have an impact. And from a stock market perspective, it is tough to fade stocks as companies use their repatriations to increase buybacks and dividends. A client, who has been a tremendous mentor to me, eloquently explained how stock investors should think about the impact of the policy change in the year prior to the tax change being made. Let's say companies repatriate $500bn and use all of that cash for buybacks and dividends. S&P 500 companies are currently returning $1 trillion of cash to shareholders for a shareholder yield of 4 percent. All else being equal, another $500bn of dividends and buybacks increases shareholder yield from 4 to 6 percent while the 10-year Treasury is yielding 2 percent. The punch line was that you needed to be in stocks. In practice, companies are not really going to return every dollar back to cash and stocks, and bond yields will rise. **But the client turned out to be correct. In the first half of the year, the total shareholder yield was 5.1 percent while the 10-year Treasury was 2.9 percent**. The spread between shareholder yield and the 10-year Treasury is not as wide as in the past, but still quite meaningful.



Politically, buybacks are getting a lot of attention from Democrats. And there is no doubt that buybacks have increased. But interestingly, as a % of market cap they are lower than the Obama years.

TECH & HEALTHCARE ARE THE LARGEST OVERSEAS CASH HOLDERS & ARE 2 OF 3 SECTORS OUTPERFORMING

Since the House released its tax reform plan, only three sectors have outperformed the S&P 500: 1) Consumer discretionary; 2) Tech; and 3) Healthcare. Repatriations are likely helping tech and healthcare companies which accounted for 57 percent of the total unremitted foreign earnings among S&P 500 companies.

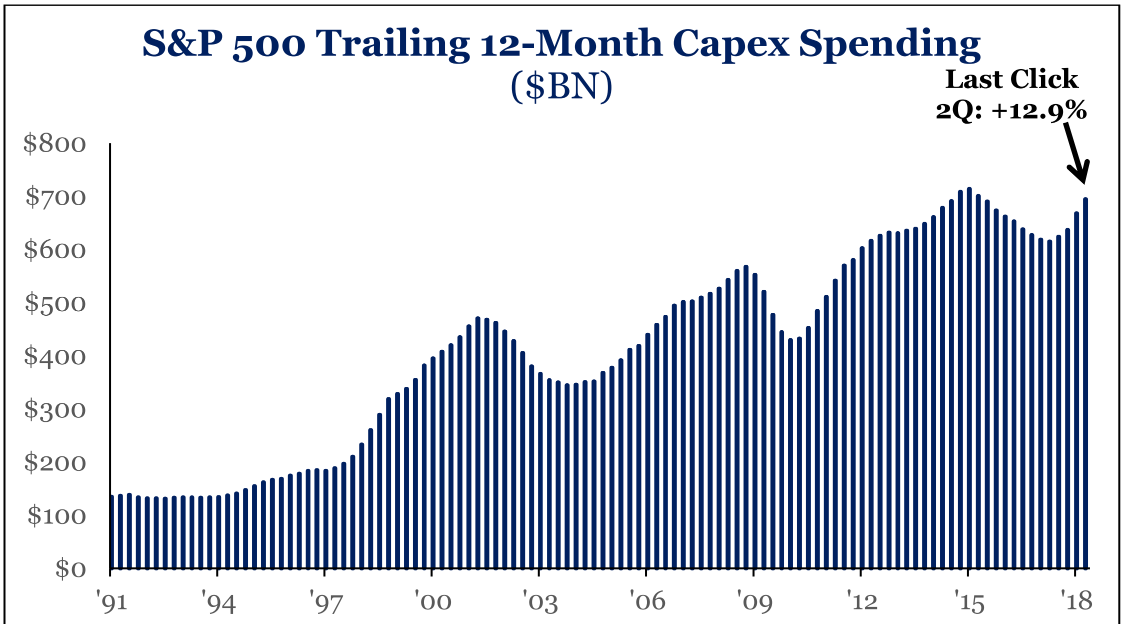


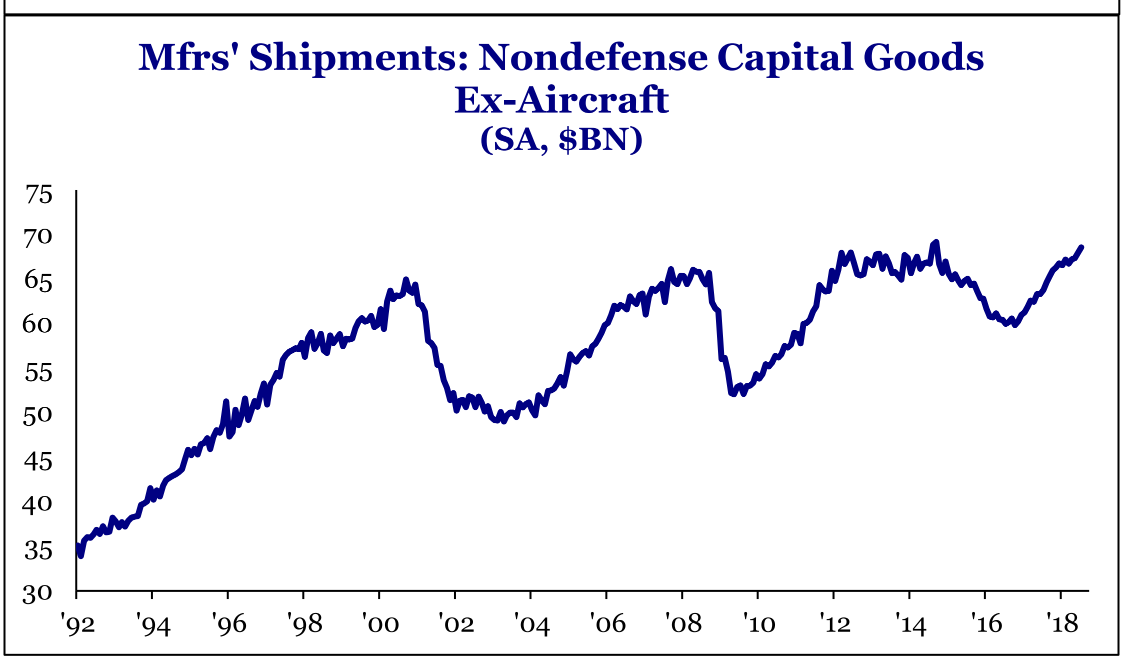
2016 Unremitted Foreign Earnings: S&P 500 Sectors

Sector	Market Value ($BN)	Unremitted Foreign Earnings ($BN)	Percentage (Sorted)
Health Care	**2733.82**	**542.88**	**19.86%**
Information Technology	**4244.76**	**782.10**	**18.43%**
Materials	505.70	76.52	15.13%
Consumer Staples	1979.83	246.10	12.43%
Energy	1430.13	145.92	10.20%
Financials	3089.30	231.34	7.49%
Industrials	2058.75	148.91	7.23%
Consumer Discretionary	2507.25	138.64	5.53%
Utilities	611.55	14.10	2.31%
Telecommunication Services	512.07	2.30	0.45%
Real Estate	612.74	2.58	0.42%
Total	**20285.90**	**2331.39**	**11.49%**

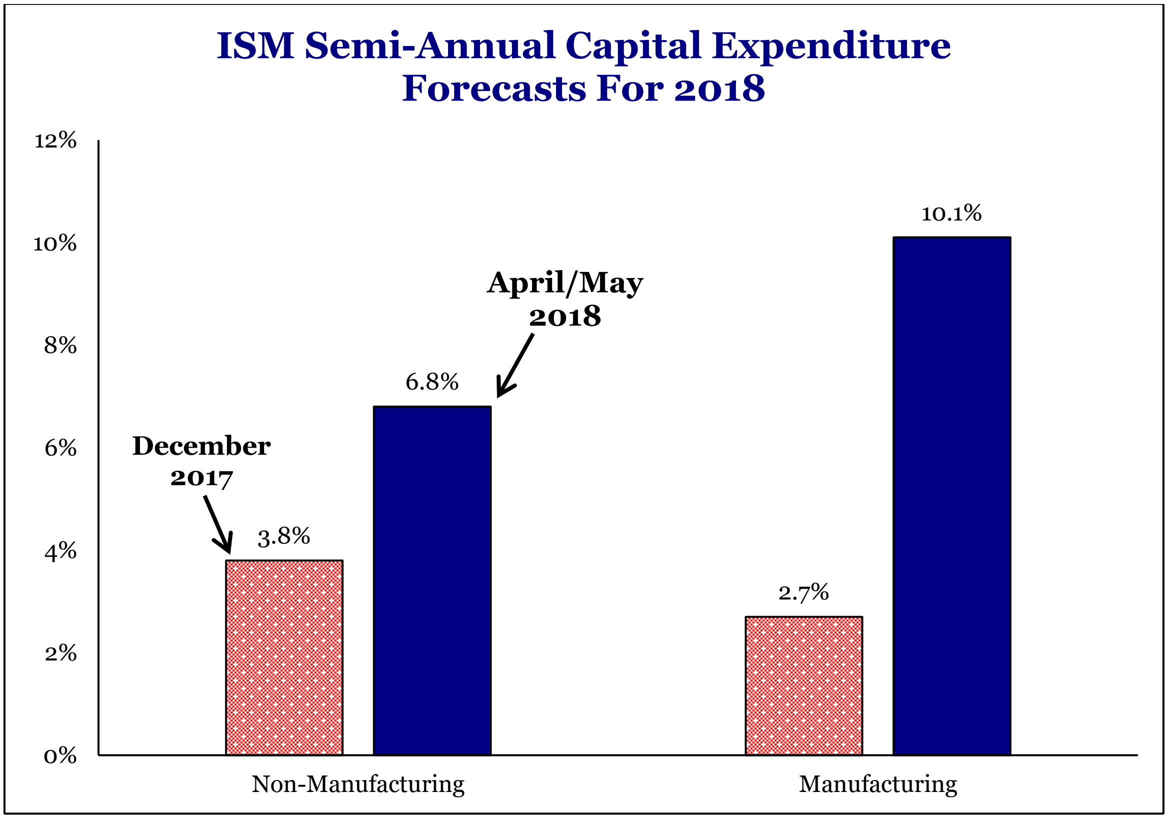
CAP EX IS BACK! IGNORE SUPPLY-SIDE EFFECTS OF THE TAX CUT AT YOUR OWN PERIL

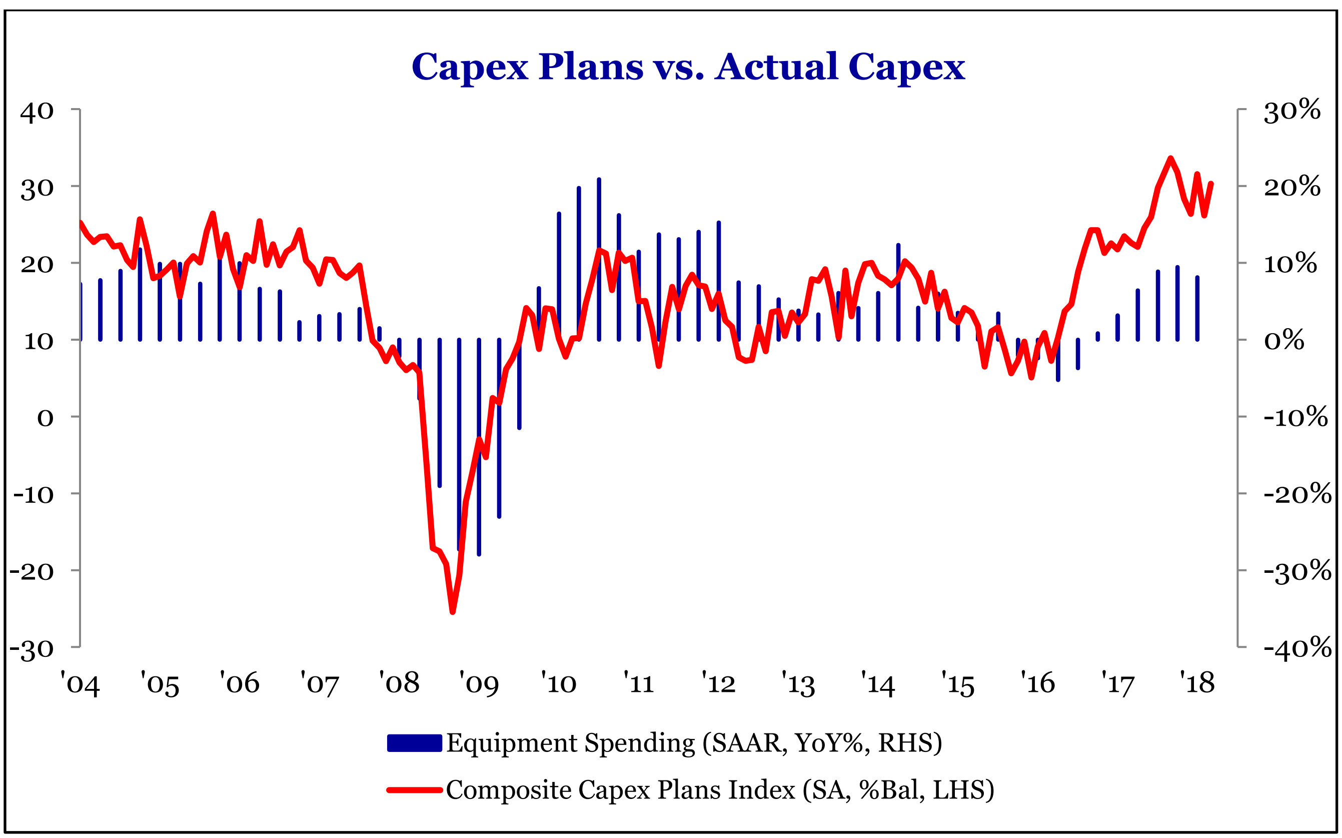
There is a belief in Washington that companies are solely using their cash for share buybacks but the data does not bear this out. More companies are reporting they are paying down debt than any other use of their repatriated cash. And we believe companies are set to use cash for investment. In addition to lower corporate tax rates and repatriation, companies can write off 100 percent of their capital equipment purchases. S&P 500 cap ex is up 13 percent year-over-year through 2Q. On Friday, the Atlanta Fed's GDP tracker upgraded projected 3Q GDP from 4.3 to 4.6 percent. One reason for Friday's upgrade was the increase in shipments for non-defense capital goods (ex-aircraft). This metric is a key input for GDP and was up 0.9 percent in July.





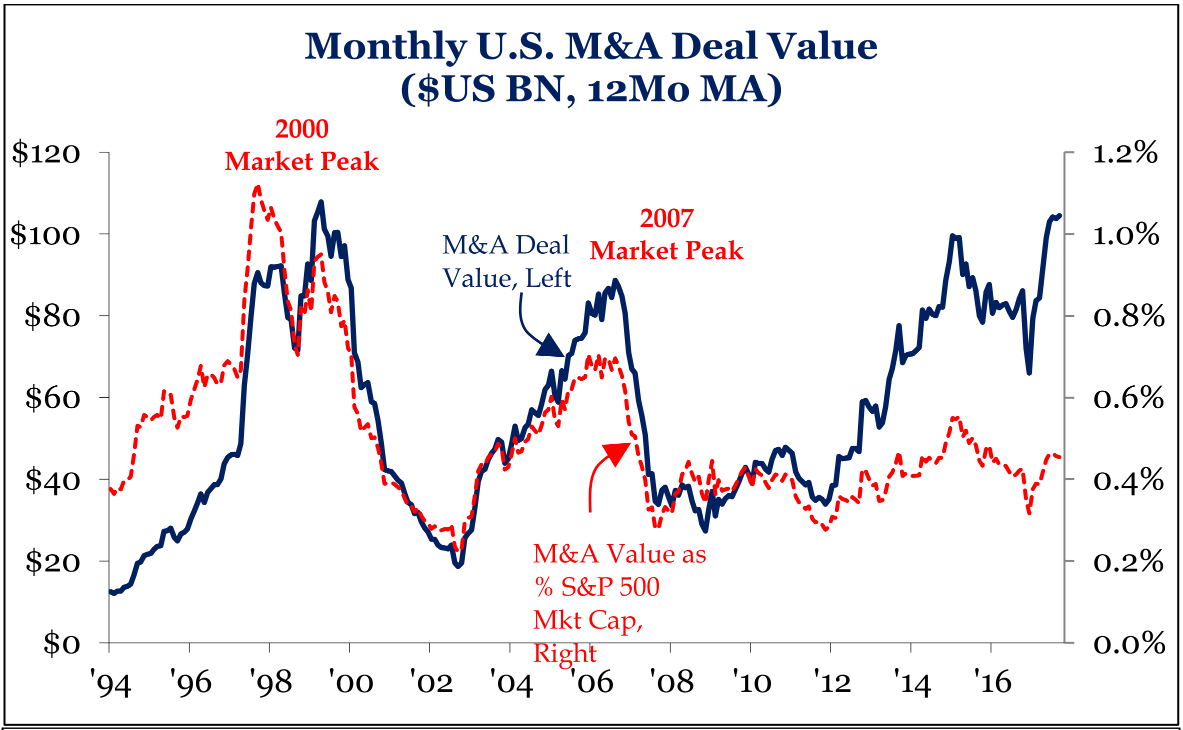
CAPEX PLANS SURGED POST-TAX CUT & REMAIN ELEVATED DESPITE INCREASED TRADE TENSIONS

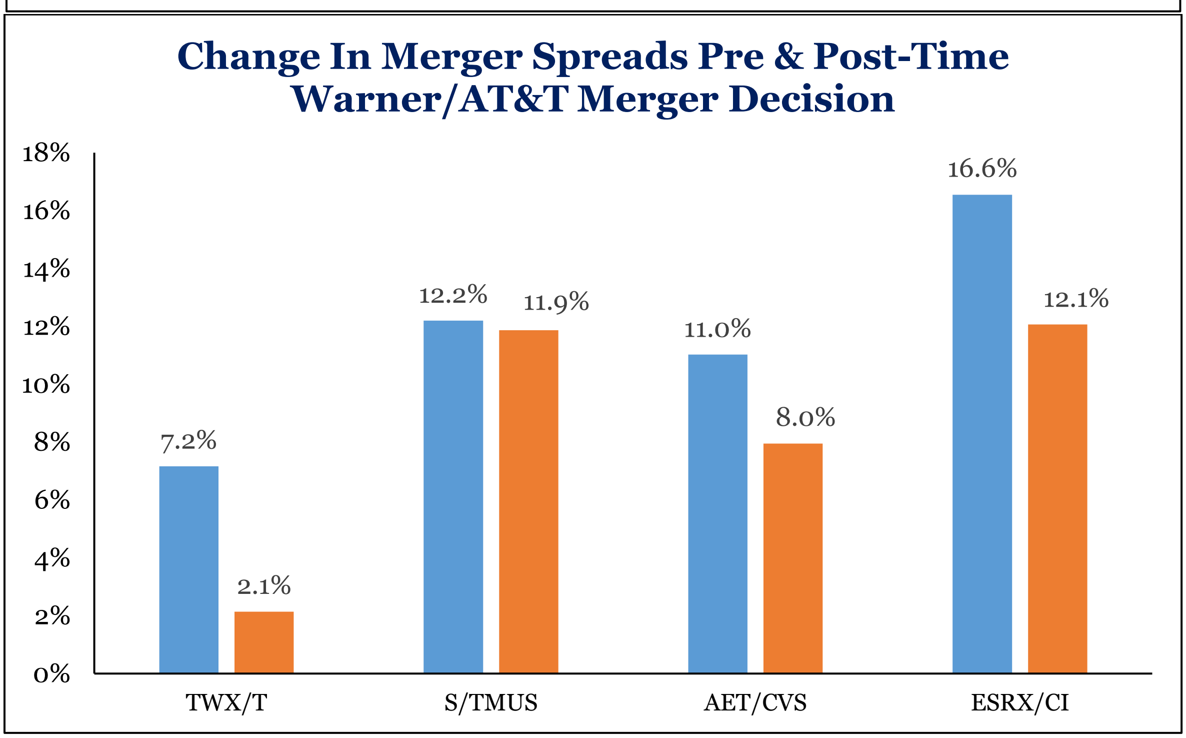




MORE ROOM FOR MERGERS & ACQUISITIONS

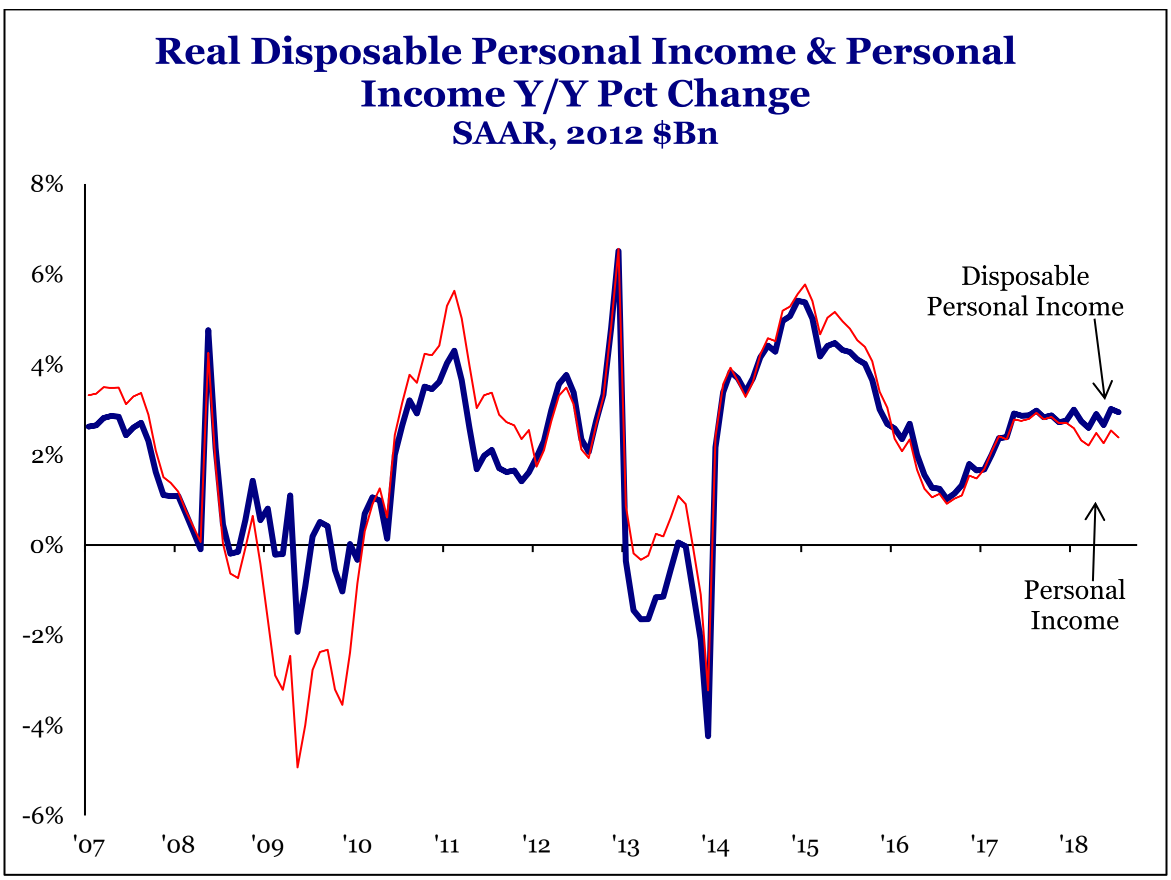
A number of high profile M&A deals have lifted the value of mergers to 2000 and 2007 levels. But as a percentage of market cap, M&A activity is still significantly below previous market peak levels. Our sense is that companies are awaiting the regulatory certainty from the Time Warner merger challenge by the federal government. After the previous court ruling approving the merger, deal spreads fell instantly. But the new government challenge has paused some of the animal spirits that were building.



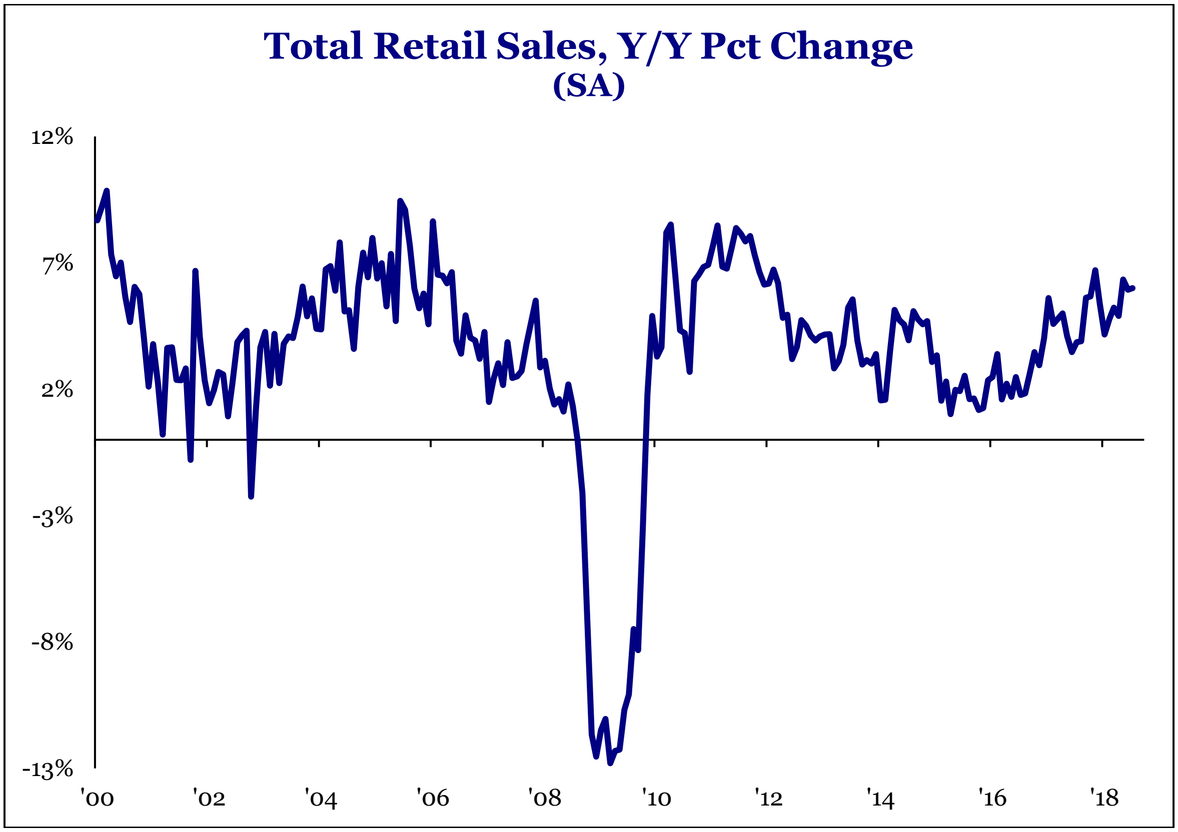


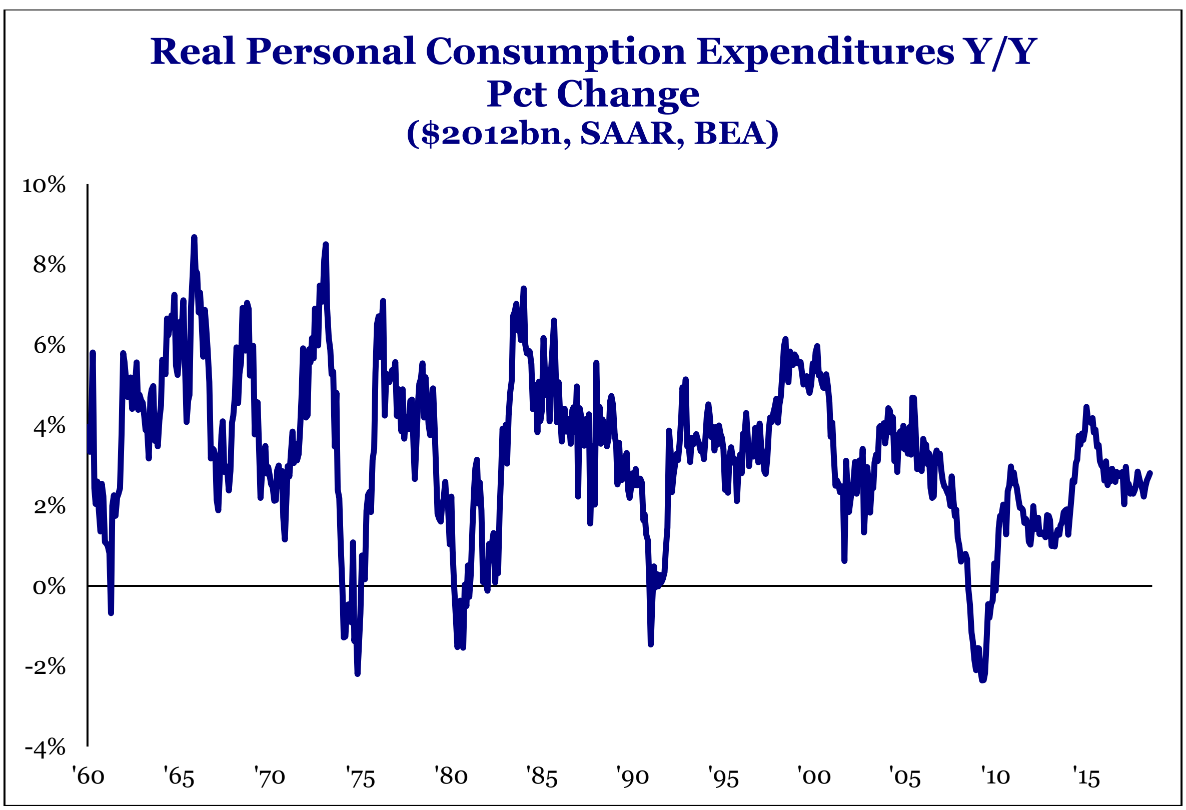
CONSUMER REMAINS STRONG: IT IS UTTER NON-SENSE TO ARGUE TAX CHANGES HAD LITTLE CONSUMER BENEFIT

One of our most out-of-consensus views going into tax reform was that the consumer benefit from tax reform was underappreciated. Nearly every press report on the consumer portion of the tax change was about the State and Local Tax Deduction (SALT) or the mortgage deduction. Our frustration in December was significant as we pounded the table that income tax rates were being cut for 90-95 percent of the population in the amount of $120bn (0.6% of GDP). This tax cut was coming in early 2018 and delivered through worker paychecks, which is akin to giving nearly every worker in America a raise of 3 percent. Consumers making $300k were looking at a 10 percent increase in their after-tax income and yet being told they were facing a massive tax increase. SALT changes were limited to really people making over $1mm a year and slightly lower in high tax states like NY, NJ, and CA. Like tariffs, the reporting was not proportional to the impact. Now that the noise has sorted out and consumer savings are growing, we are seeing a very strong consumer that is benefitting from higher disposable income and a booming jobs market. We like to look at real disposable personal income because this measures the impact of wages, bonuses, tax cuts, and higher gasoline prices for a net number.



CONSUMER IS DRIVING STRONGER GDP





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