

SECTOR SPOTLIGHT

FINANCIALS



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RECOMMENDED POSITIONING IN FIN_{mgmt}

INVESTMENT IDEAS - LONGS

				Mkt Cap (\$M)	Trade	Trend	Tail
CME	CME-US	40,353	CME Group	40,353	✓	✓	
BEN	BEN-US	24,008	Franklin Resources	24,008	✓	✓	✓
CFG	CFG-US	18,837	Citizens Bank	18,837	✓	✓	✓
IVZ	IVZ-US	13,174	Invesco	13,174	✓	✓	
RLGY	RLGY-US	4,299	Realty Holdings Corp.	4,299	✓	✓	✓

INVESTMENT IDEAS - SHORTS

				Mkt Cap (\$M)	Trade	Trend	Tail
CBA	Commonwealth Bank of Aus	146,001			x	x	x
RY	Royal Bank of Canada	138,278			x	x	x
TD	Toronto-Dominion Bank	119,200			x	x	x
WBC	Westpac Banking Corporation	113,655			x	x	x
GS	Goldman Sachs Group, Inc.	89,303			x	x	
BNS	Bank of Nova Scotia	92,699			x	x	x
ANZ	Australia and NZ Bank	89,990			x	x	x
NAB	National Australia Bank	87,005			x	x	x
AXP	American Express Company	70,001			x	x	x
CM	CIBC	43,420			x	x	x
COF	Capital One Financial	39,734			x	x	x
DFS	Discover Financial Services	22,926			x	x	x
NA	National Bank of Canada	18,133			x	x	x
TROW	T Rowe Price	17,347				x	x
BX	BlackStone Group	20,019			x	x	x
LAZ	Lazard Ltd.	5,562			x	x	x
CWB	Canadian Western Bank	2,281			x	x	x
PRAA	PRA Group	1,525			x	x	x
ITB	Home Construction ETF	1,426			x	x	
ECPG	Encore Capital Group	844			x	x	x

LONG BENCH

				Mkt Cap (\$M)
SCHW	SCHW-US	53,645	Charles Schwab	53,645
ICE	ICE-US	35,796	Intercontinental Exchan	35,796
NDAQ	NDAQ-US	11,324	NASDAQ OMX Group	11,324
CBOE	CBOE-US	9,433	CBOE Holdings	9,433
LM	LM-US	3,580	Legg Mason	3,580
FNGN	FNGN-US	2,515	Financial Engines	2,515
FII	FII-US	2,628	Federated Investors	2,628
VIRT	VIRT-US	610	Virtu Financial	610
OZM	OZM-US	457	Och Ziff Capital Mgmt	457

SHORT BENCH

			Mkt Cap (\$M)
BLK	BlackRock		62,503
BMO	Bank of Montreal		45,871
KMX	CarMax		11,088
MIC	Genworth MI Canada		6,733
SC	Santander Consumer		4,457
CACC	Credit Acceptance		4,181
JNS	Janus Capital Group		2,536
NSM	Nationstar Mortgage		1,616
WETF	WisdomTree Investments		1,160

LEGEND

Trade: Short-term thesis with a duration of approximately 1 month

Trend: Intermediate-term thesis with a duration of approximately 3 months

Tail: Long-term thesis with a duration of approximately 3 years

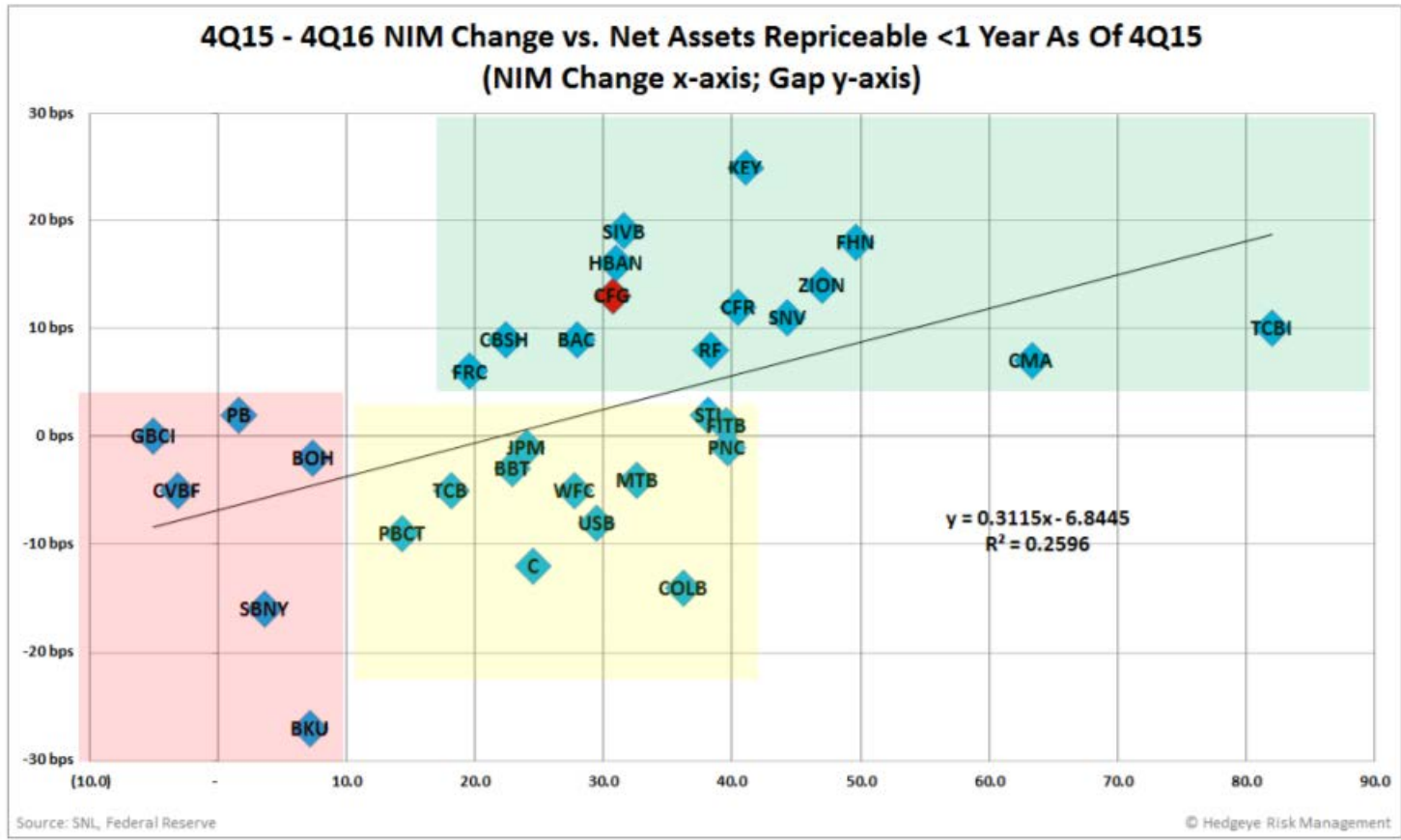
RATE SENSITIVITY IN THE GROUP

LTM Correlation to the 10-Year Treasury Yield

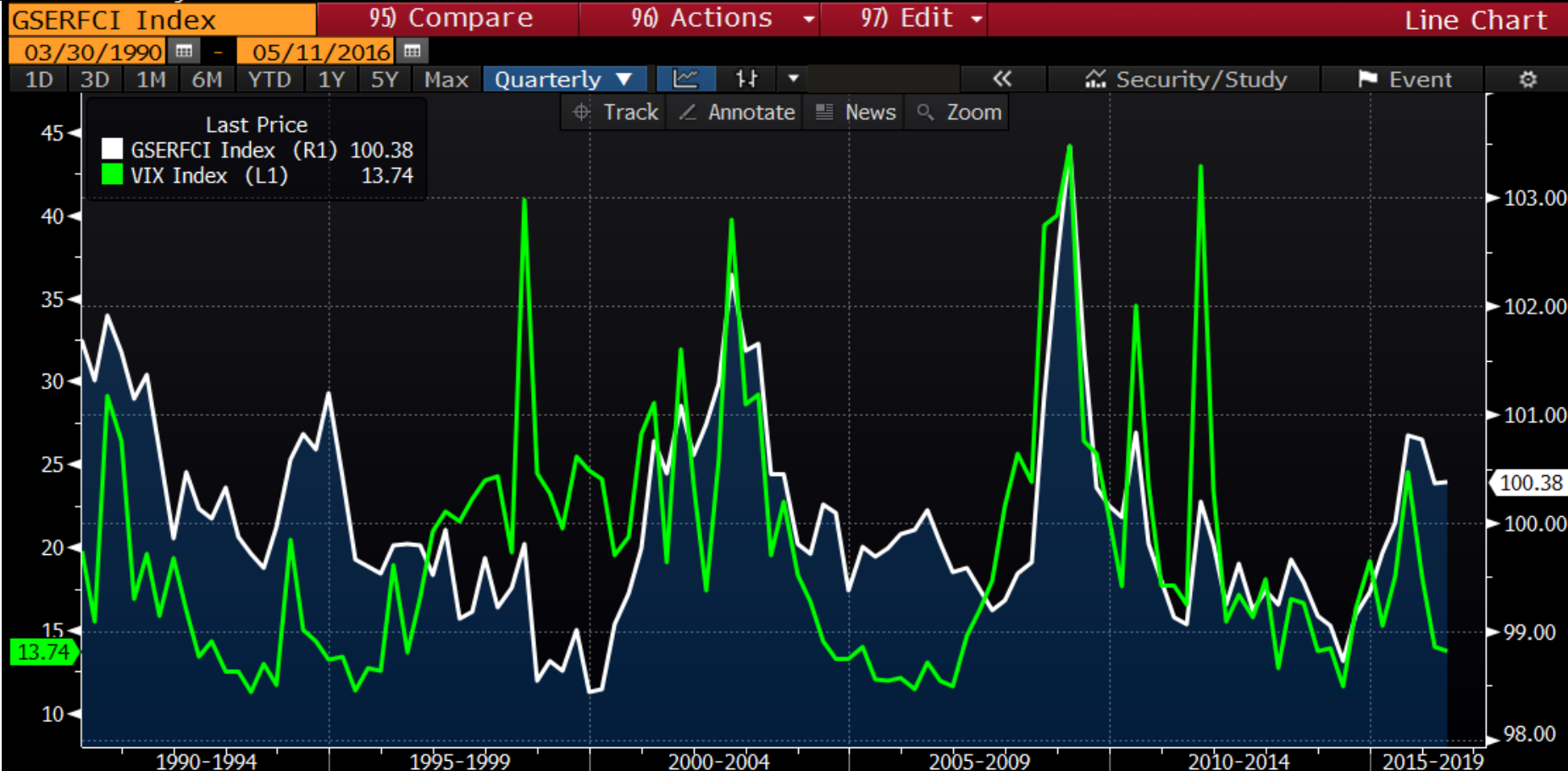
	Avg R Value	Std Dev		Median R Value	Std Dev												
Large Cap Banks	0.92	0.04	Large Cap Banks	0.94	0.04	Large Cap Banks	Ticker	R Value	Midcap Banks	Ticker	R Value	Small Cap Banks	Ticker	R Value	Small Cap Banks Cont		
Midcap Banks	0.90	0.14	Midcap Banks	0.94	0.14	Midcap Banks	COF	0.96	Midcap Banks	HBAN	0.97	Small Cap Banks	EWBC	0.96	Small Cap Banks Cont	WAFD	0.92
Small Cap Banks	0.89	0.11	Small Cap Banks	0.92	0.11	Small Cap Banks	PNC	0.96	Small Cap Banks	KEY	0.96	Small Cap Banks	WBS	0.96	Small Cap Banks Cont	NBHC	0.92
I-Banks/Boutiques	0.88	0.10	I-Banks/Boutiques	0.91	0.10	I-Banks/Boutiques	BAC	0.95	Small Cap Banks	CFG	0.96	Small Cap Banks	PBCT	0.96	Small Cap Banks Cont	BBCN	0.92
Mortgage Insurers	0.87	0.03	Life Insurers	0.88	0.30	Life Insurers	C	0.94	Small Cap Banks	RF	0.95	Small Cap Banks	FNB	0.95	Small Cap Banks Cont	UMPQ	0.92
Reinsurers	0.78	0.28	Mortgage Insurers	0.87	0.03	Mortgage Insurers	USB	0.94	Small Cap Banks	MTB	0.94	Small Cap Banks	SIVB	0.95	Small Cap Banks Cont	COLB	0.91
Life Insurers	0.76	0.30	Reinsurers	0.85	0.28	Reinsurers	JPM	0.94	Small Cap Banks	CMA	0.94	Small Cap Banks	FULT	0.95	Small Cap Banks Cont	TCBI	0.91
Financial Guaranty	0.71	0.31	Financial Guaranty	0.85	0.31	Financial Guaranty	BBT	0.91	Small Cap Banks	ZION	0.93	Small Cap Banks	ISBC	0.95	Small Cap Banks Cont	WTFC	0.91
Auto Insurers	0.69	0.31	E-Brokers	0.80	0.56	E-Brokers	BK	0.91	Small Cap Banks	FITB	0.93	Small Cap Banks	VLY	0.95	Small Cap Banks Cont	GBCI	0.90
P&C Insurers	0.62	0.41	Auto Insurers	0.78	0.31	Auto Insurers	WFC	0.89	Small Cap Banks	STI	0.92	Small Cap Banks	WAL	0.95	Small Cap Banks Cont	TCB	0.90
Insurance Brokers	0.62	0.26	P&C Insurers	0.76	0.41	P&C Insurers	STT	0.83	Small Cap Banks	SBNY	0.91	Small Cap Banks	CVBF	0.95	Small Cap Banks Cont	BOFI	0.89
Exchanges	0.61	0.24	Exchanges	0.66	0.24	Exchanges	Average	0.92	Small Cap Banks	FRC	0.90	Small Cap Banks	SNV	0.95	Small Cap Banks Cont	HBHC	0.89
E-Brokers	0.54	0.56	Consumer Finance	0.66	0.55	Consumer Finance	Median	0.94	Small Cap Banks	NYCB	0.46	Small Cap Banks	OZRK	0.94	Small Cap Banks Cont	WABC	0.89
Cards/Payments	0.44	0.40	Insurance Brokers	0.64	0.26	Insurance Brokers	Std Dev	0.04	Small Cap Banks	Average	0.90	Small Cap Banks	FMBI	0.94	Small Cap Banks Cont	BKU	0.88
Consumer Finance	0.40	0.55	Mortgage Finance	0.59	0.53	Mortgage Finance			Small Cap Banks	Median	0.94	Small Cap Banks	CATY	0.93	Small Cap Banks Cont	CFR	0.86
Homebuilders	0.39	0.41	Alternative AMs	0.57	0.60	Alternative AMs			Small Cap Banks	Std Dev	0.14	Small Cap Banks	HOMB	0.93	Small Cap Banks Cont	IBKC	0.85
Mortgage Finance	0.37	0.53	Homebuilders	0.56	0.41	Homebuilders			Small Cap Banks			Small Cap Banks	CBSH	0.93	Small Cap Banks Cont	BOKF	0.85
Building Products	0.36	0.35	Cards/Payments	0.47	0.40	Cards/Payments			Small Cap Banks			Small Cap Banks	BOH	0.93	Small Cap Banks Cont	PVTB	0.84
CRE Brokers	0.33	0.43	Building Products	0.46	0.35	Building Products			Small Cap Banks			Small Cap Banks	PB	0.93	Small Cap Banks Cont	FBP	0.80
Alternative AMs	0.30	0.60	Debt Collectors	0.44	0.70	Debt Collectors			Small Cap Banks			Small Cap Banks	ONB	0.93	Small Cap Banks Cont	OFG	0.78
SF REITs	0.29	0.05	SF REITs	0.31	0.05	SF REITs			Small Cap Banks			Small Cap Banks	UMBF	0.93	Small Cap Banks Cont	BPOP	0.75
RE Services	0.28	0.83	Fin Services	0.29	0.46	Fin Services			Small Cap Banks			Small Cap Banks	ASBC	0.93	Small Cap Banks Cont	EVER	0.52
Debt Collectors	0.25	0.70	RE Services	0.28	0.83	RE Services			Small Cap Banks			Small Cap Banks	FHN	0.93	Small Cap Banks Cont	FBC	0.36
Fin Services	0.16	0.46	Fin Tech	0.27	0.52	Fin Tech			Small Cap Banks			Small Cap Banks	PACW	0.93	Small Cap Banks Cont	Average	0.89
Fin Tech	0.16	0.52	CRE Brokers	0.25	0.43	CRE Brokers			Small Cap Banks			Small Cap Banks	BXS	0.92	Small Cap Banks Cont	Median	0.92
Home Centers	0.15	0.50	Traditional AMs	0.23	0.55	Traditional AMs			Small Cap Banks			Small Cap Banks			Small Cap Banks Cont	Std Dev	0.11
Traditional AMs	0.13	0.55	Home Centers	0.15	0.50	Home Centers			Small Cap Banks			Small Cap Banks			Small Cap Banks Cont		
Title Insurers	(0.15)	0.37	Title Insurers	(0.16)	0.37	Title Insurers			Small Cap Banks			Small Cap Banks			Small Cap Banks Cont		
Apartment REITs	(0.24)	0.26	Apartment REITs	(0.25)	0.26	Apartment REITs			Small Cap Banks			Small Cap Banks			Small Cap Banks Cont		

Source: Factset, Hedgeye Calculations

POSITIVE NIM BETA AT CFG

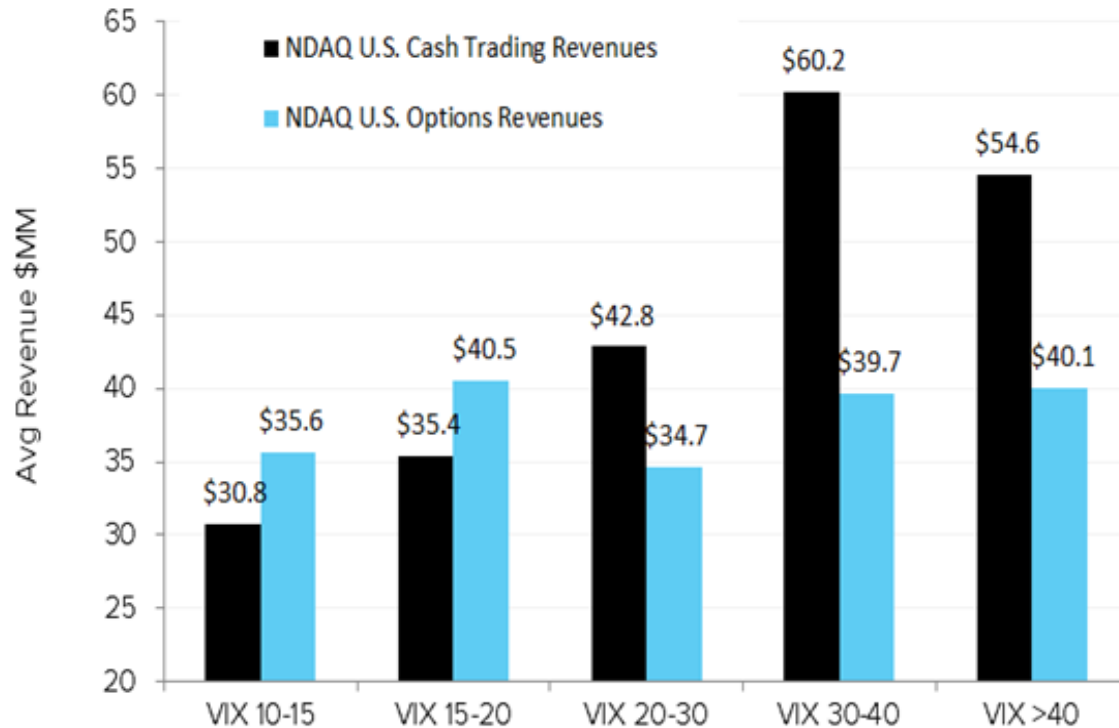


VOL IS LOW & SHOULD MOVE HIGHER

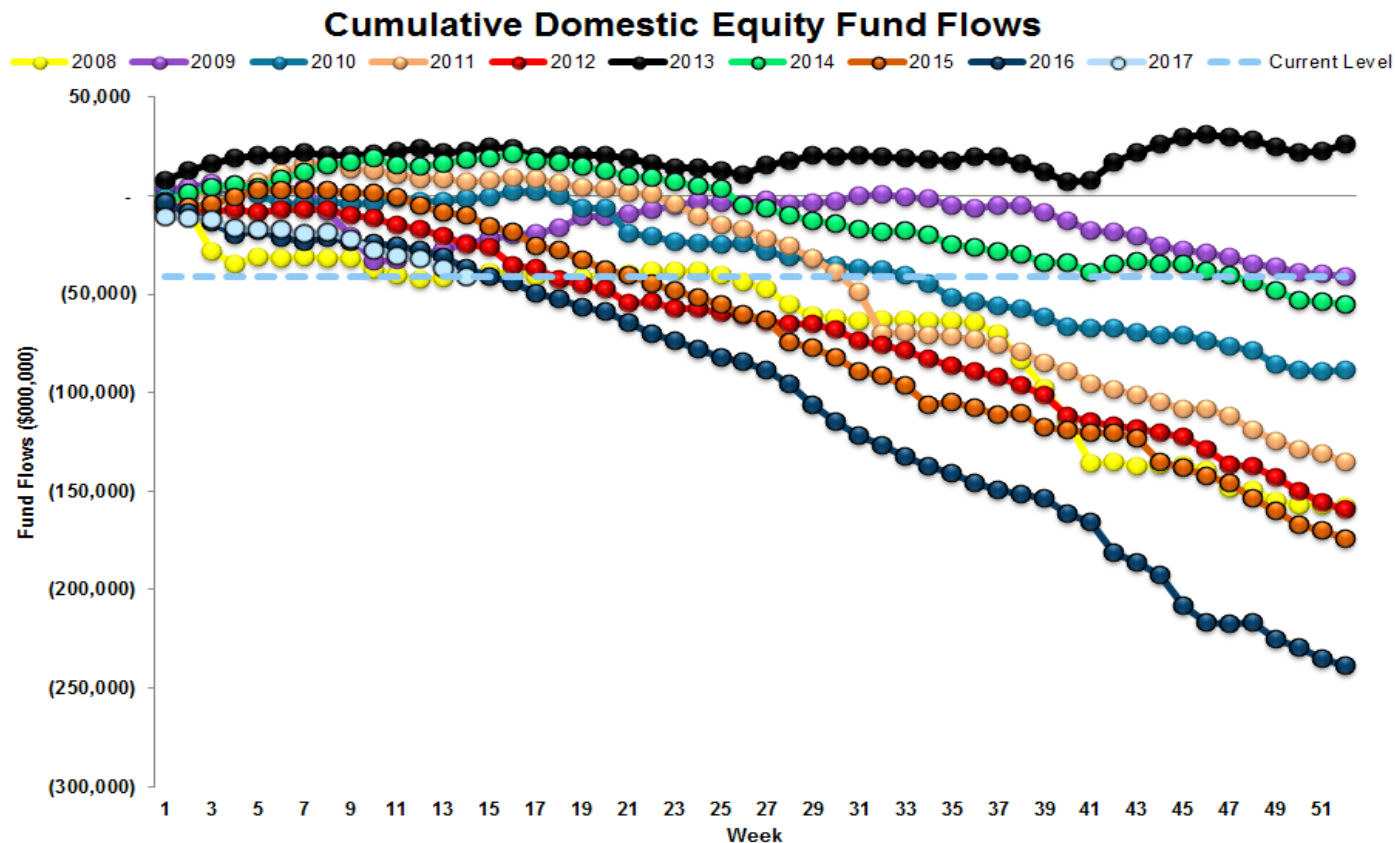


AND THE EXCHANGES WILL BENEFIT

AVG QUARTERLY REVENUE BY VIX LEVEL 2007-2013



DOMESTIC MUTUAL FUNDS IN TROUBLE

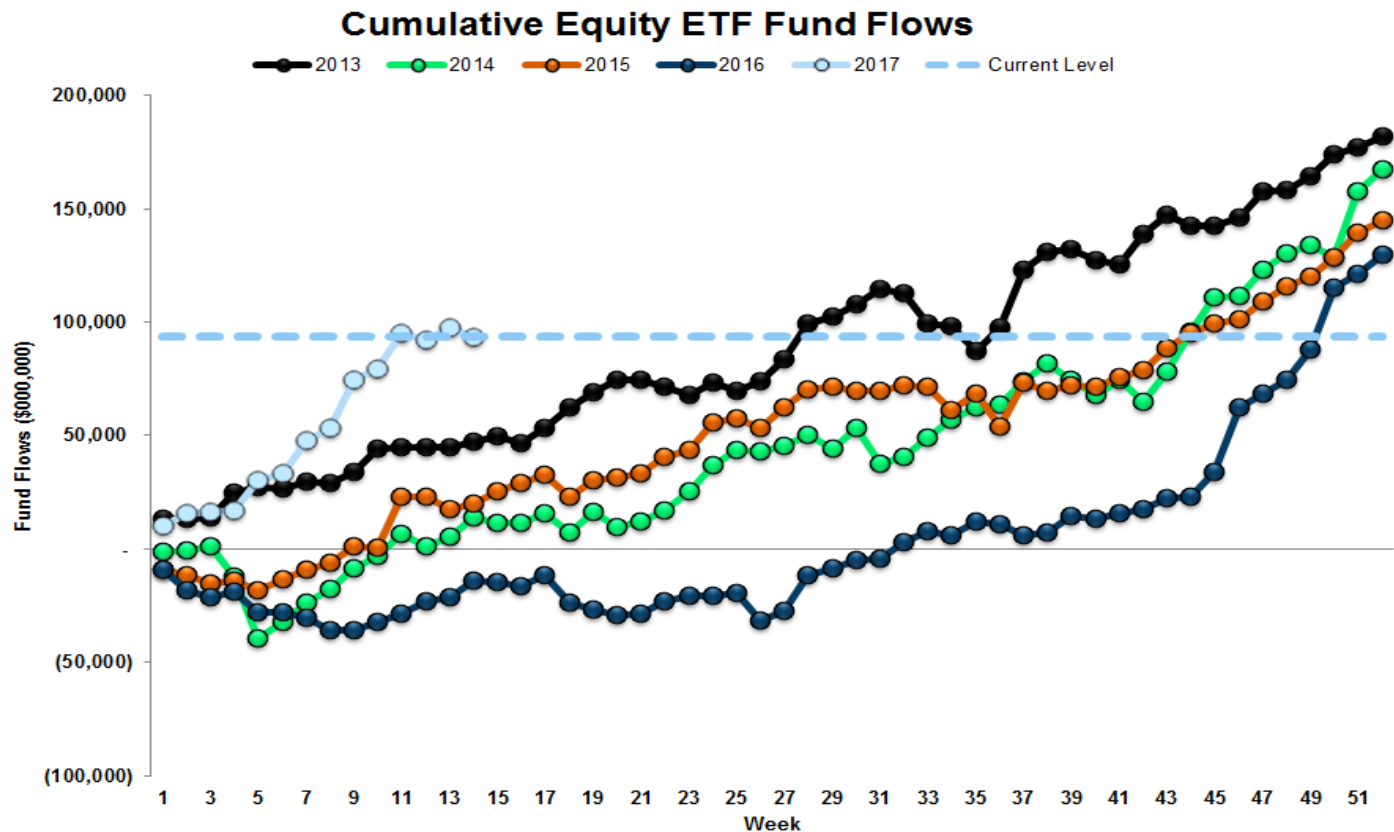


Data Source: ICI

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Domestic equity fund flows are **under duress** bordering on another record **outflow** year.

BUT ETFs ARE SKYROCKETING



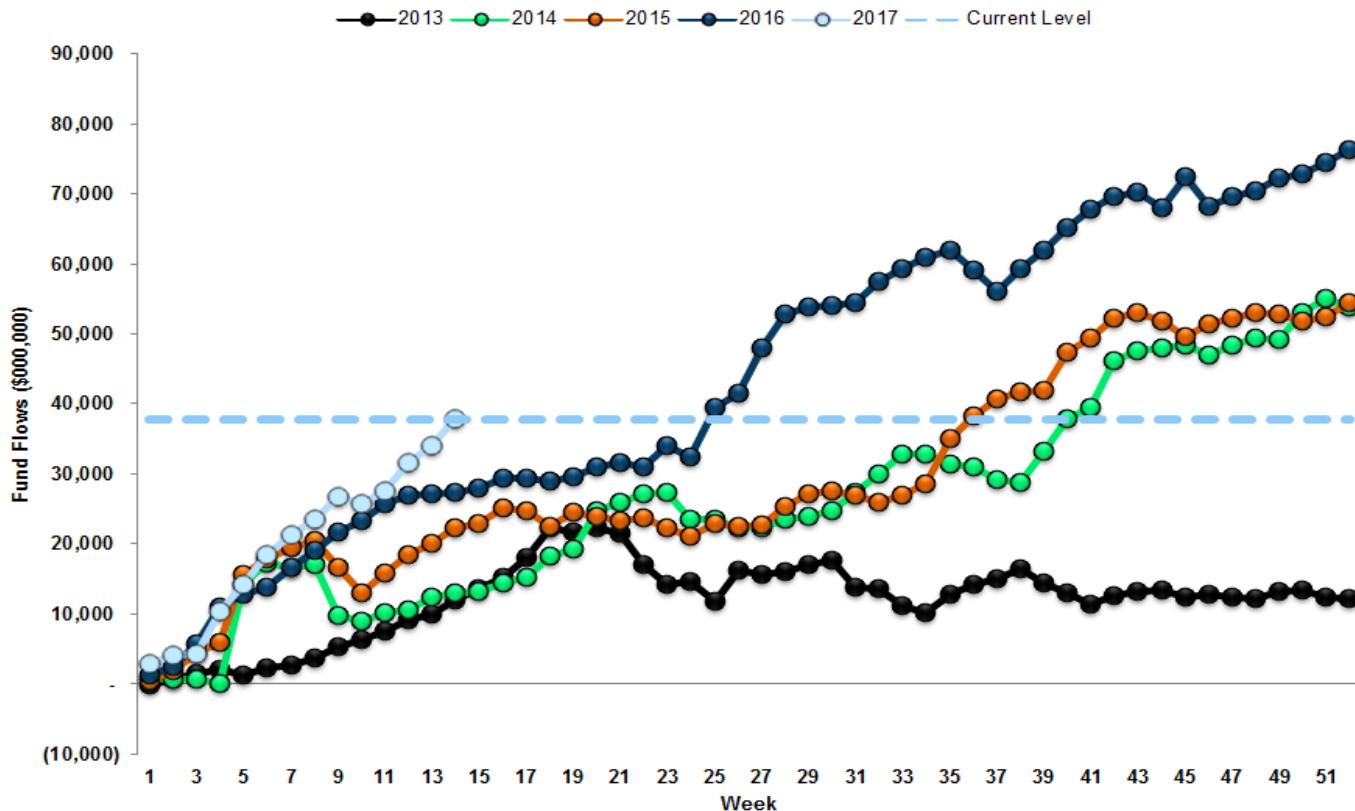
Data Source: ICI

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Meanwhile, the industry is seeing a **nonlinear response in the growth of ETFs** this year with a **new record pace** to start an annual period.

THE LAY OF THE LAND

Cumulative Fixed Income ETF Fund Flows



Data Source: ICI

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Moreover, fixed income ETFs have also **started strongly**, with **2017 out of the gate in stronger fashion than 2013-2016.**

PASSIVE HOCKEY STICK

ETFs Have Record Breaking Inflows Of \$135B In Q1

April 03, 2017

In describing the amount of money that came into ETFs during the first quarter of 2017, "enormous" would be an understatement.

"Record-breaking" is technically correct, but it also doesn't put the figure into proper context.

Instead, consider that after the first three months of last year, inflows into ETFs totaled \$20.6 billion. Over the same period this year, \$134.7 billion entered the space—more than four times the amount of 2016's first quarter. If inflows continue at this torrid pace, total 2017 inflows will reach almost \$540 billion, blowing past last year's record \$287.5 billion.

While annualizing 1Q17's Passive inflow is not a good idea, there has been a **nonlinear move** into ETFs with a **4x move in 1Q17 flows versus 1Q16**.

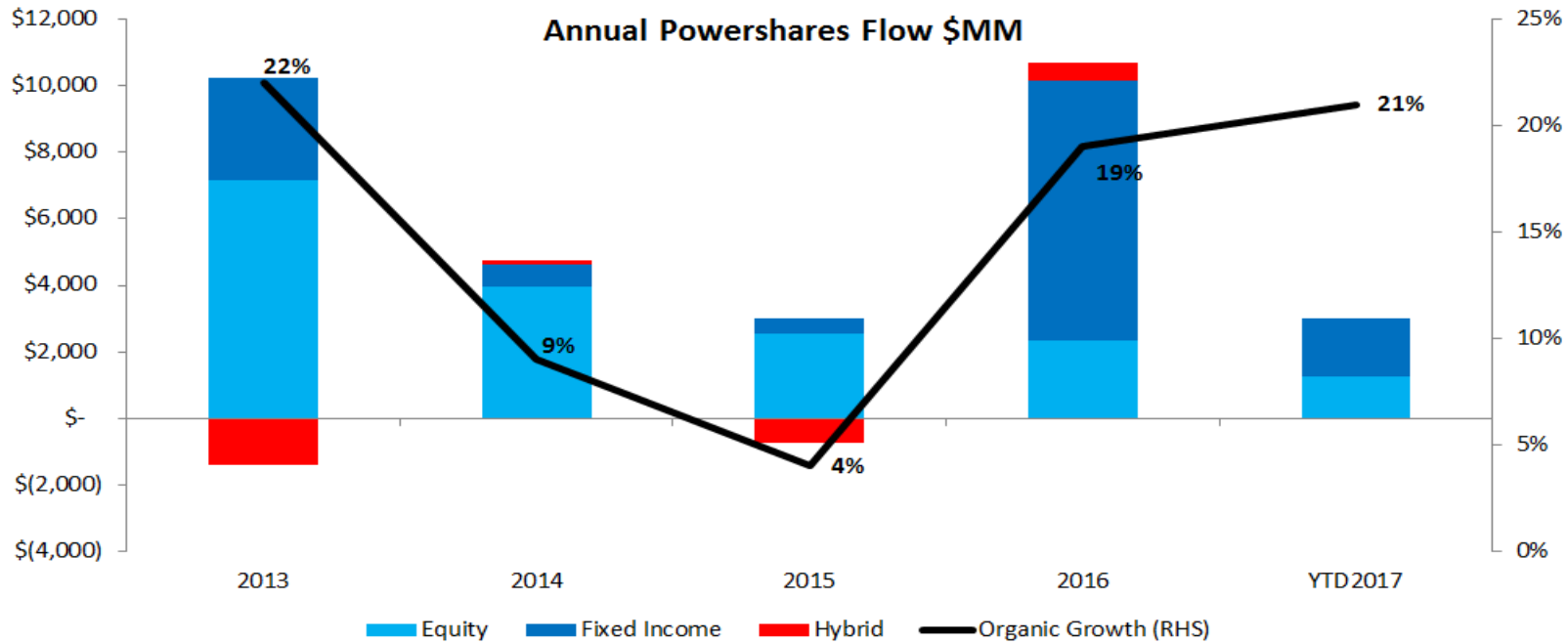
PASSIVE HOCKEY STICK

March 2017 League Table

Issuer	Net Flows (\$,M)	AUM (\$,M)	% of AUM	YTD 2017 Net Flows(\$,M)
BlackRock	22,617.19	1,085,132.02	2.08%	52,973.79
Vanguard	12,880.60	681,892.52	1.89%	40,318.59
State Street Global Advisors	4,236.99	538,009.65	0.79%	12,546.31
Invesco PowerShares	-441.57	120,865.27	-0.37%	4,058.21
Charles Schwab	2,349.54	69,452.29	3.38%	6,755.07
First Trust	634.64	45,163.70	1.41%	2,148.18
WisdomTree	-444.03	42,075.99	-1.06%	-39.50
VanEck	661.09	35,369.24	1.87%	3,840.09
Guggenheim	452.57	34,648.98	1.31%	1,917.09
ProShares	632.95	27,276.77	2.32%	1,292.70
ALPS	320.45	14,480.66	2.21%	1,364.57
Deutsche Bank	-492.21	14,021.51	-3.51%	-187.55
Northern Trust	390.79	13,478.43	2.90%	1,299.80
PIMCO	228.42	12,956.55	1.76%	384.12
Direxion	668.54	11,467.67	5.83%	579.33

Furthermore, IVZ Powershares brought in another **\$4 BB in 1Q17, good for 5th place** in the league table for ETF managers.

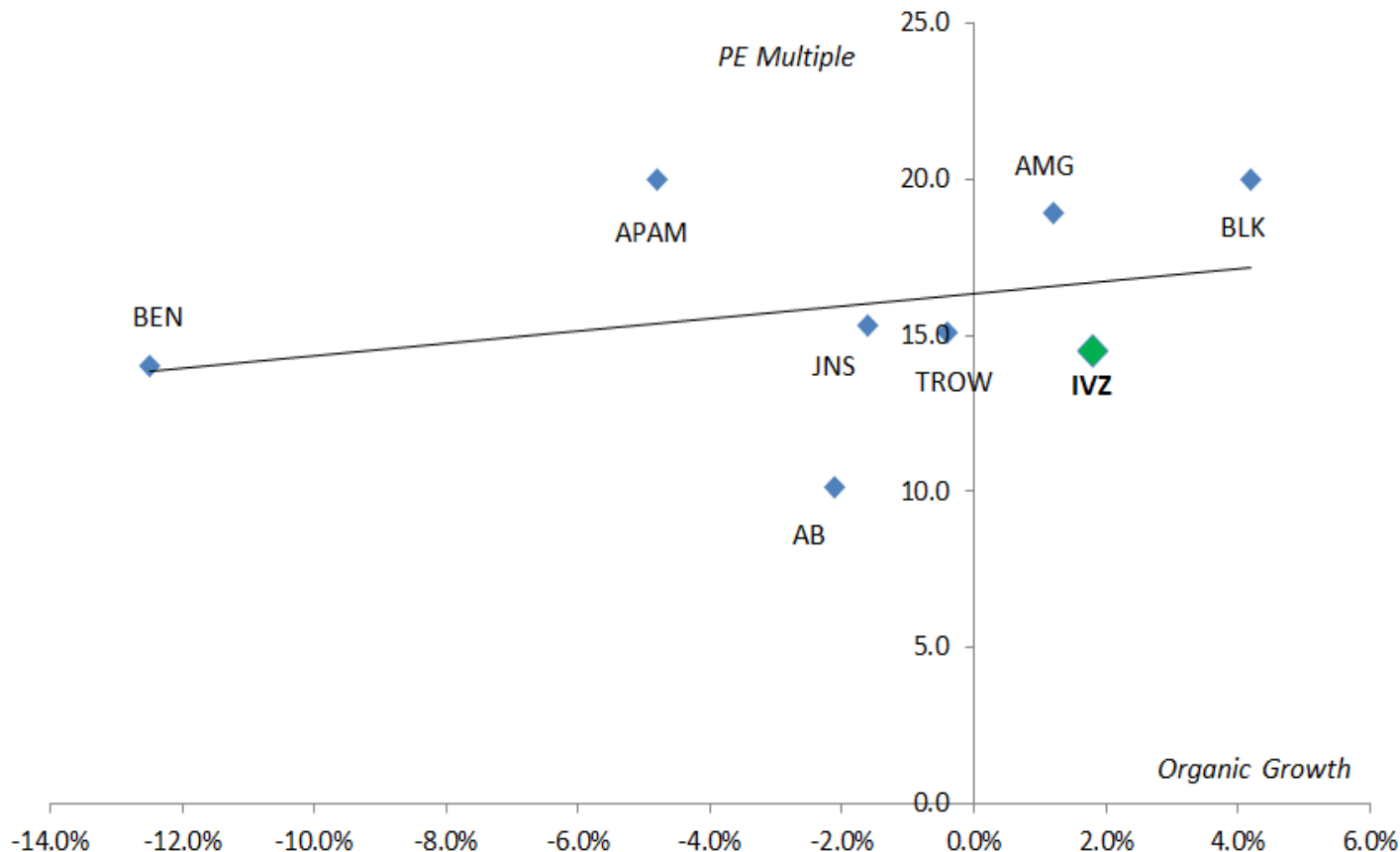
PASSIVE HOCKEY STICK



POWERSHARES GROWTH HAS TAKEN OFF AGAIN

Year-to-date annualized organic growth in Powershares has again breached the +20% level, a multiple of the 2015 level and faster expansion than the solid 2016 result.

GROWTH AT A REASONABLE PRICE



The **majority** of the major asset managers have **negative organic growth**, but of the **3** that have positive fund raising, **IVZ is the cheapest by a wide margin.**

BEST DEFENSE IS A GOOD OFFENSE?

Anxious Mutual-Fund Industry Holds ‘Seismic Shift Senior Leadership Forum’

Rivals gathered to halt trend of clients leaving for index-tracking funds that match the market



Representatives from T. Rowe Price were among the attendees at a gathering of mutual fund executives that met to discuss the problem

By **SARAH KROUSE**

Updated Dec. 13, 2016 4:29 p.m. ET

 56 COMMENTS

About 60 rival mutual fund executives gathered inside OppenheimerFunds’ Manhattan office tower in early November to discuss a problem many of them can’t shake: persistent client withdrawals.

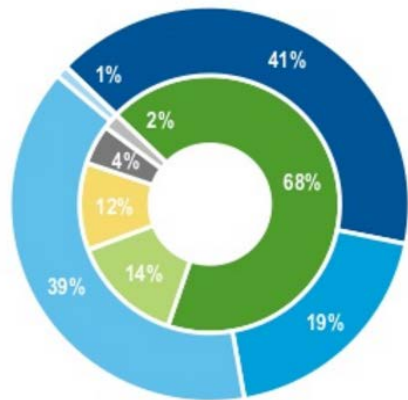
At the **end of last year**, 60 mutual fund executives met in New York to discuss the **ongoing battle against ETFs**. We think this is signaling that **more merger activity is to occur in 2017** and beyond.

FRANKLIN / INVESCO WOULD ADD SCALE



FRANKLIN TEMPLETON INVESTMENTS

As of December 31, 2016

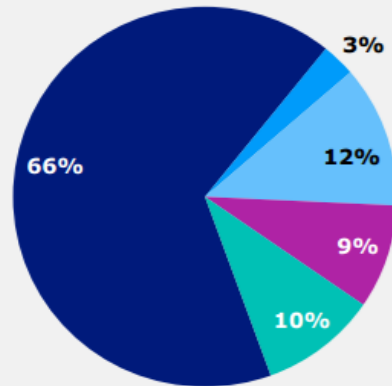


Investment Objective	Dec-16
Equity	\$ 298.3
Hybrid	138.3
Fixed Income	277.2
Cash Management	6.2
Total	\$ 720.0

Sales Region	Dec-16
United States	\$ 491.0
Europe, the Middle East and Africa	100.5
Asia-Pacific	81.6
Canada	30.3
Latin America	16.6
Total	\$ 720.0

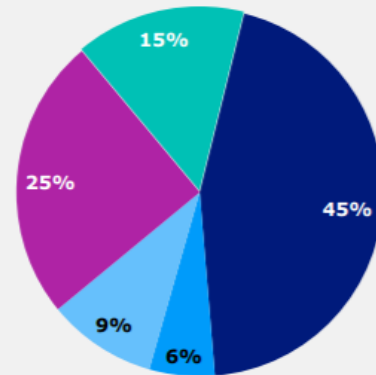


By client domicile



	(\$ billions)	1-Yr Change
U.S.	\$539.5	5.6%
Canada	\$23.1	6.5%
U.K.	\$98.2	(5.8)%
Europe	\$72.1	(4.4)%
Asia	\$80.0	25.8%
Total	\$812.9	4.8%

By asset class



	(\$ billions)	1-Yr Change
Equity	\$364.1	(1.8)%
Balanced	\$46.8	(2.7)%
Money Market	\$78.3	21.2%
Fixed Income	\$201.7	7.3%
Alternatives	\$122.0	17.2%
Total	\$812.9	4.8%

FRANKLIN / INVESCO – CHECK ALL BOXES

Active US Equity

- ✓ Franklin Income (BEN)
- ✓ Invesco Van Kampen (IVZ)

Active Foreign Equity

- ✓ Templeton Equity (BEN)
- ✓ Perpetual (IVZ)

Active Global Bond

- ✓ Templeton Bond
- ✓ Invesco (IVZ)

Private Equity/Alts

- ✓ Wilbur Ross (IVZ)
- ✓ Darby/K2/Pelagos (BEN)

Passives

- ✓ Powershares (IVZ)
- ✓ Liberty (BEN)

Balanced

- ✓ Franklin Hybrid (BEN)
- ✓ Invesco Balanced (IVZ)

Cash Management

- ✓ Invesco (IVZ)
- ✓ Franklin (BEN)

A **BEN/IVZ** would add **needed scale** to the **active management** business under arrest by ETFs. The product overlap would **allow for cost synergies and real estate consolidation.**

FRANKLIN / INVESCO – WE SPECULATE



	TTM BEN \$MM	TTM IVZ \$MM
Revenues	\$ 6,420	\$ 3,393
Comp Exp.	\$ 1,329	\$ 1,365
Non Comp Exp.	\$ 2,791	\$ 716
Total Expenses	\$ 4,120	\$ 2,081
Cost Synergies		
Operating Income	\$ 2,300	\$ 1,312
Interest Income	\$ 199	\$ 43
Interest Expense	\$ 51	\$ 93
Taxes	\$ 733	\$ 338
Net Income	\$ 1,715	\$ 924

Shares Outstanding (MM)	565	415
EPS	\$ 3.04	\$ 2.23

Cash (\$MM)	\$ 8,223	\$ 1,581
Debt (\$MM)	\$ 1,395	\$ 2,073

Stock Price Per Share	\$ 42.00	\$ 32.00
Purchase Price \$MM		

Cash %
Debt%
Stock %

Proforma BEN/IVZ	Assumptions	
\$ 9,813	Interest Income	2%
\$ 2,694	Cost of Debt	5%
\$ 3,507	Cost Synergies \$MM	500
\$ 6,201		
\$ (500)	EPS Accretion BEN	9%
\$ 4,112	Share Price Gain IVZ	25%
\$ 146		
\$ 283		
\$ 1,193		
\$ 2,783		

842
\$ 3.31

\$ 7,314
\$ 5,658

\$ 40.00
\$ 16,600

15%
15%
70%

At **\$40** per share for IVZ and \$500 MM in cost synergies, **BEN** could have **+9% EPS synergies** while **IVZ** shareholders enjoy a **+25% gain**.

GREAT DEAL OPERATOR – KNOWS BEN



Martin L. Flanagan CFA,
CPA
President and Chief Executive
Officer of Invesco Ltd.
USA

Martin Flanagan has been a Director and President and Chief Executive Officer of Invesco since August 2005. He is also a Trustee and Vice-Chairman of the Invesco Funds (the company's U.S. open and closed-end fund companies). Mr. Flanagan joined Invesco from Franklin Resources, Inc., where he was president and co-chief executive officer from January 2004 to July 2005. Previously he had been Franklin's co-president from May 2003 to January 2004, chief operating officer and chief financial officer from November 1999 to May 2003, and senior vice president and chief financial officer from 1993 until November 1999. Mr. Flanagan served as director, executive vice president and chief operating officer of Templeton, Galbraith & Hansberger, Ltd. before its acquisition by Franklin in 1992. Before joining Templeton in 1983, he worked with Arthur Andersen & Co. Mr. Flanagan earned a B.A. and B.B.A from Southern Methodist University (SMU). He is a CFA charterholder and a certified public accountant. He serves on the board of governors and as a member of the executive committee for the Investment Company Institute, and is a former chairperson. He also serves as a member of the executive board at the SMU Cox School of Business and is involved in a number of civic activities in Atlanta.

Marty Flanagan has done a **number of deals at IVZ** and is a **great** integrator. He came from **Franklin** where he was **COO, CFO, and President.**

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