

MARKET COMMENTARY MONDAY, MARCH 19, 2018

EXECUTIVE SUMMARY

Investor Sentiment – Another Big Reversal, this Time Upward, in AAll Optimism
Week #11 – Not so Good Five Days Ends on a Positive Note...For Value
The Case for Value – Fund Flows Into Tech Like March 2000, Recent Underperformance, Valuation Gap & Improving Economic Data
Fed Watch – Likely Rate Hike at Next Week's FOMC Meeting: Another Reason to Favor Value
Target Prices – New Listing Posted to theprudent-speculator.com
Stock News – Updates on QCOM, MRVL, WSM, JBL, DSW & TNP

Market Review

Funny how stocks rallied handsomely the week prior to last, despite (because of?) a big 10.9 percentage point drop to 26.4% in the number of Bulls in the weekly American Association of Individual Investors Sentiment Survey, and they struggled last week despite (because of?) a reversal in the AAll numbers. Indeed, with the number of optimists rising 10.4 percentage points to 36.8% and the number of pessimists falling 7.1 points to 21.3%, the second lowest number of Bears this year, the equity markets struggled to advance with early-morning gains often giving way to end-of-day losses.

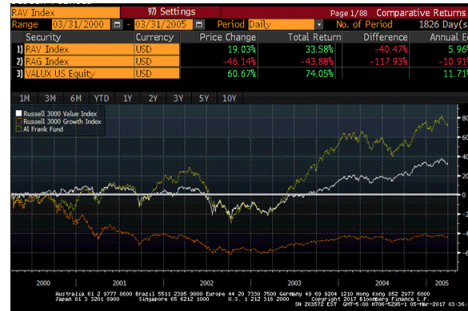
When the score was tallied for the latest trading week, the S&P 500 and Russell 3000 indexes dropped 1.20% and 1.10%, respectively, while the Dow Jones Industrial Average fell 1.51%. Interestingly, though the Value vs. Growth race was again decided in the favor of the latter (the Russell 3000 Value index dipped 1.17% compared to a 1.03% loss for the Russell 3000 Growth index), Friday's trading saw many long-suffering undervalued stocks enjoy a little time in the sun, while high-flyers like Amazon, Alphabet (Google), Netflix and Tesla saw their prices retreat. Obviously, one day hardly a trend makes, but we did find it interesting that the pullback in many technology names and the rally in Value stocks came the very day that the widely read *Markets* section of *The Wall Street Journal* reminded investors that billions of dollars have flowed into tech-stock mutual and exchange traded funds this year at the expense of far less expensive areas of the equity markets.

THE PRUDENT SPECULATOR Time for Value – Tech Getting the Flows

After several years of lagging returns, Value strategies had a great five years following the bursting of the Tech Bubble in March 2000, despite the then rich multiples on the major indexes.

Billions Flow Into Tech-Focused Funds

Investors are increasing their bets on shares of technology companies, renewing concerns that the market is becoming too dependent on a few big stocks to power its gains. Nearly \$5 billion has poured into tech-focused stock funds so far this year, the most of any major sector, according to Thomson Reuters Lipper data. That figure represents nearly half of what the group pulled in for all of 2017. In January alone, tech funds received \$3.9 billion in inflows, the most in a single month for such funds since March 2000—the peak of the dot-com bubble.



The Wall Street Journal 3.16.18

No doubt, we realize that Value has been bringing up the rear in the performance derby,...

THE PRUDENT SPECULATOR Time for Value – Lagging ST Performance

Returns Race					
2018 YTD	2017	2016	Since Trump Election (11.8.16) %	Bloomberg Symbol	Index
Stock Indexes					
1.47	28.11	16.50	40.66	INDU Index	Dow Jones Industrial Average
8.64	29.73	8.97	46.40	CCMP Index	NASDAQ Composite Index
3.36	21.68	12.04	32.26	RIT Index	Russell 1000 Index
3.54	14.63	21.28	35.11	RTY Index	Russell 2000 Index
3.37	21.12	12.72	32.48	RAY Index	Russell 3000 Index
3.37	21.82	11.95	32.20	SPX Index	S&P 500 Index
6.42	30.21	7.07	42.44	RUG Index	Russell 1000 Growth Index
0.24	13.64	17.33	22.51	RLV Index	Russell 1000 Value Index
6.26	22.14	11.28	42.95	RUO Index	Russell 2000 Growth Index
0.62	7.82	31.72	27.36	RUJ Index	Russell 2000 Value Index
6.41	29.58	7.38	42.47	RAG Index	Russell 3000 Growth Index
0.26	13.17	18.38	22.98	RAN Index	Russell 3000 Value Index
7.22	27.43	6.89	39.55	SGX Index	S&P 500 Growth Index
-0.66	15.35	17.39	23.69	SVX Index	S&P 500 Value Index
Largest Bond Funds					
-1.96	3.57	0.79	-0.67	VBTIX Equity	Vanguard Tot Bnd Mkt Idx-Inst
-1.99	3.53	0.75	-0.79	VTBIX Equity	Vanguard Tot Bnd Mkt II-Inv
-0.88	8.17	0.82	8.02	PONAX Equity	Pimco Income Fund-A
0.35	2.39	0.81	2.01	VTBIX Equity	Vanguard Ttl Int Bnd-Adm
-1.92	3.10	0.76	-0.78	MWTRX Equity	Mtprtn Wst Ttl Rtrn Bnd-M
-1.66	5.13	0.73	1.52	PTTRX Equity	Pimco Total Return Fund-Inst
-0.70	7.36	0.63	7.34	PIMINIA Equity	Pimco Gls-Income Fund-Ins Ac
-0.72	2.02	-0.01	0.52	VFSTX Equity	Vanguard S/T Invest Grd-Inv
-1.27	4.53	0.21	0.52	VMTX Equity	Vanguard Mtn Trn T/F-Inv
-1.16	4.36	0.63	2.08	DODIX Equity	Dodge & Cox Income
-0.92	3.79	0.51	1.40	DBLTX Equity	Doubleline Ttl Rtrn Bnd-I
-0.53	1.89	0.07	1.14	LDLAX Equity	Lord Abbett Shrt Durt Inc-C

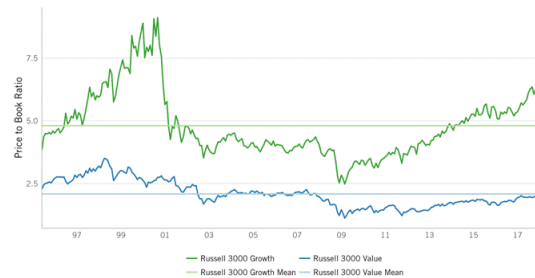
Source: Bloomberg. As of 3.16.18

Though Growth stocks have been the big winners since the Trump Election, Value did win the returns race for all of 2016 and has been the victor by a wide margin (13.4% vs. 9.4% per annum) over the past nine decades. And, with a stronger global economic outlook and reasonable valuation metrics, we think Value will again prove its mettle as we move through 2018, especially given all of the drama in Washington.

...but we find our kinds of stocks to be about as undervalued relative to Growth as we have witnessed since the peak of the Tech Bubble eighteen years ago...

THE PRUDENT SPECULATOR Time for Value – Valuation Gap

Believe it or not, despite the major market averages residing not far from record highs, Value stocks (as represented by the Russell 3000 Value index) trade at a normal (over the past 23 years) price-to-book value ratio AND the valuation gap with Growth stocks (Russell 3000 Growth index) is as wide today as it has been since 2000.



From 05.31.95 through 02.28.18. SOURCE: AI Frank using data from Bloomberg

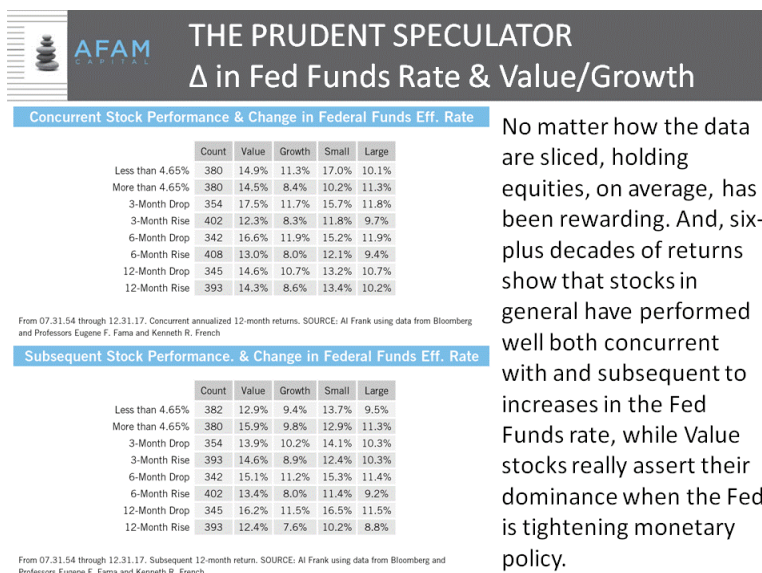
...and we think a likely catalyst for Value's resurgence will be a healthier U.S. economy,...

THE PRUDENT SPECULATOR Small Business & Consumer Optimism



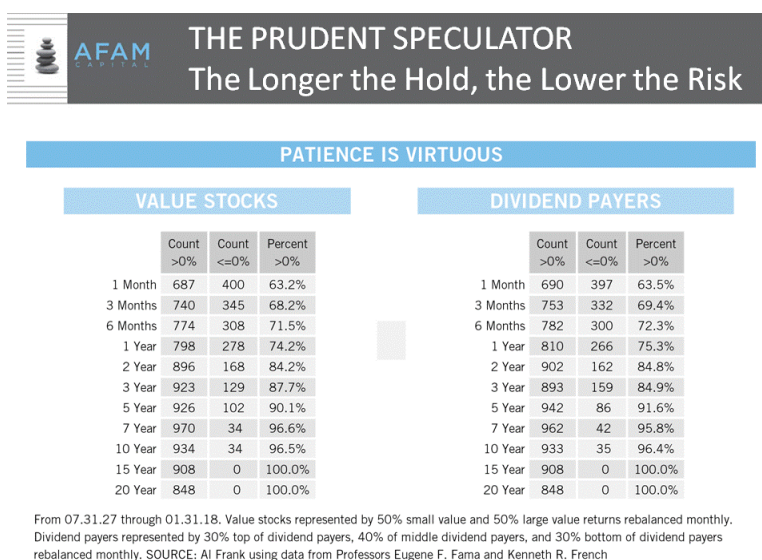
The Small Business Optimism Index rose in February to 107.6, the National Federation of Independent Business said. It was the second-highest level in the measure's 45 years, second only to a reading of 108 in 1983. Meanwhile, the University of Michigan Consumer Sentiment gauge climbed to 102.0 in March from 99.7 in February, topping the consensus economist forecast of 99.5 and hitting the best level in 14 years.

...even if stronger domestic GDP growth leads the Federal Reserve to hike interest rates three or four times this year, starting with next week's FOMC Meeting.



No matter how the data are sliced, holding equities, on average, has been rewarding. And, six-plus decades of returns show that stocks in general have performed well both concurrent with and subsequent to increases in the Fed Funds rate, while Value stocks really assert their dominance when the Fed is tightening monetary policy.

Of course, our enthusiasm for the intermediate- and long-term prospects of our broadly diversified portfolios of undervalued stocks does not preclude more turbulence in the near term, especially with the headlines coming out of Washington over the weekend. The equity futures at the time we went to press were pointing to a lower opening when trading resumes today, but as our time horizon is measured in years, if not decades, we will remain patient with short-term gyrations, secure in the belief that we will be rewarded in the fullness of time.



Stock Updates

We published to our Web site this weekend updated Target Prices for all 120 of our formerly recommended but not yet closed out stocks and Chris Quigley and Jason Clark take a look at a half-dozen of those companies in the news last week...

Advances from Broadcom to buy **Qualcomm** (QCOM – \$60.62) were stopped dead in their tracks after President Trump issued an order stating, “There is credible evidence that leads me to believe that Broadcom Ltd. might take action that threatens to impair the national security of the United States.” On Wednesday, Broadcom formally dropped its bid. With Broadcom now apparently out of the picture, former QCOM chairman Paul Jacobs was reported to have approached several large investors to raise funds to buy the San Diego-based chipmaker. While Mr. Jacobs has not formally submitted a bid or demonstrated that he has the necessary financing to take QCOM private as of this publishing, the purchase of QCOM by a U.S.-based investor (though there has been talk of backing by SoftBank, a Japanese firm) might actually have a good chance to pass the regulatory scrutiny that Broadcom’s bid did not.

Of course, Treasury Department’s Committee on Foreign Investment in the United States (CFIUS) intervention was all a bit strange, from the unilateral request from Qualcomm to review the hypothetical deal (as nothing had been agreed upon) to the private equity-style concerns that the Committee cited as justification for blocking it. The Committee’s concern was not to be that Broadcom/Qualcomm would export critical national security information to Broadcom’s home base in Singapore (though it’s moving back to the United States in May), but that the merged company would chop development efforts in underperforming business segments (like 5G), causing a loss in U.S. competitiveness to China. We think it’s odd that a domestic buyer could come in and take the same private equity-style approach, totally outside of the CFIUS’ jurisdiction, and that sort of deal presumably wouldn’t be blocked. For us anyway, it’s hard to imagine what sort of halfway-decent buyer of QCOM wouldn’t make changes to underperforming business segments that include cuts or asset sales. In any event, we are left wondering if Broadcom will circle back for another pass at QCOM in June when it’s fully moved to U.S. soil and CFIUS wouldn’t be able to stop it? Or does the President’s stated “permanent” order block anything related to Broadcom from now until the end of time? We are unsure if Mr. Trump or a subsequent president could issue an order undoing the order that he issued last week.

What is clear now is that QCOM has to try to function as best it can on a standalone basis. We think it’s crucial for the company to finish up its acquisition of NXP Semiconductors, the deal that has been pending since October 2016. The automotive products and expertise that NXP brings to the table will be highly important in QCOM’s next chapter as a continuing standalone entity (for now). QCOM CEO Steve Mollenkopf offered a bit of an update on March 8, stating, “We are pleased to announce an increase in our quarterly dividend, a reflection of our commitment to returning capital to stockholders. We look forward to closing the pending acquisition of NXP and expect the strong combined cash profile of Qualcomm and NXP to further strengthen our foundation for future capital returns for our stockholders.” The yield on QCOM is now 4.1%.

We think that QCOM will be better off not having sold out to Broadcom in the long run, although our current Target Price stands at \$74. We held that Broadcom’s \$79/\$82 offer was not sufficient because it undervalues QCOM’s NXP purchase (we do not have those additions included in our Target Price because the deal is not complete, though management has gone on record with a pro-forma \$6.75 to \$7.50 adjusted fiscal 2019 EPS estimate) and counts court-

based royalty battles as worth little to nothing (management expects 1/3 of fiscal 2019 adjusted EPS to come from royalty litigation). But we all have a price, and we would be very pleased if Mr. Jacobs could come up with the \$90 or so Qualcomm's current board thinks it deserves. Indeed, that would be less tortuous than another international suitor.

Unfortunately, the Broadcom/Qualcomm CFIUS ruling was not without a little bit of collateral damage last week, this time unsettling investors over Bermuda-based **Marvell Technology Group's** (MRVL – \$23.18) bid to buy Cavium. While shares sold off a little more than 4% for the week, we think that the risk of the CFIUS turning its attention to block Marvell's bid is slim. Our view that MRVL will close on the transaction is unchanged, as is our current Target Price of \$28.

Home goods retailer **Williams-Sonoma** (WSM – \$55.32) earned \$1.68 per share in fiscal Q4 2018 (vs. \$1.61 est.). WSM had sales of \$1.7 billion, versus the \$1.6 billion estimate. On account of solid Q4 earnings, due to investments in advertising, shipping and pricing, shares rose about 2.5% following the announcement, no doubt also bolstered by fiscal 2019 revenue guidance of \$5.48 billion to \$5.64 billion (estimate was \$5.48 billion) and an EPS projection of \$4.12 to 4.22, compared to the prior \$4.07 consensus figure.

CEO Laura Alber said, "In [calendar] 2017, we made significant progress against our strategic priorities to strengthen our competitive advantages and drive accelerated growth. As a result, we saw new customer growth, improved traffic and conversion, and accelerated revenue growth in both retail and e-commerce. We ended the year as one of the few retailers of our scale to consistently deliver sustainable top line growth, bottom line profitability, and robust cash flow. In [calendar] 2018, we will aggressively pursue significant growth opportunities across all areas of the business, and particularly in our global operations and new business initiatives, which have demonstrated significant potential. We'll also continue to strategically invest in digital advertising, technology, and our customer experience, while driving efficiencies and cost savings throughout our business. We are confident in our strategies and our proven track record to further extend our leadership in home furnishings and housewares industry in [calendar] 2018 and beyond."

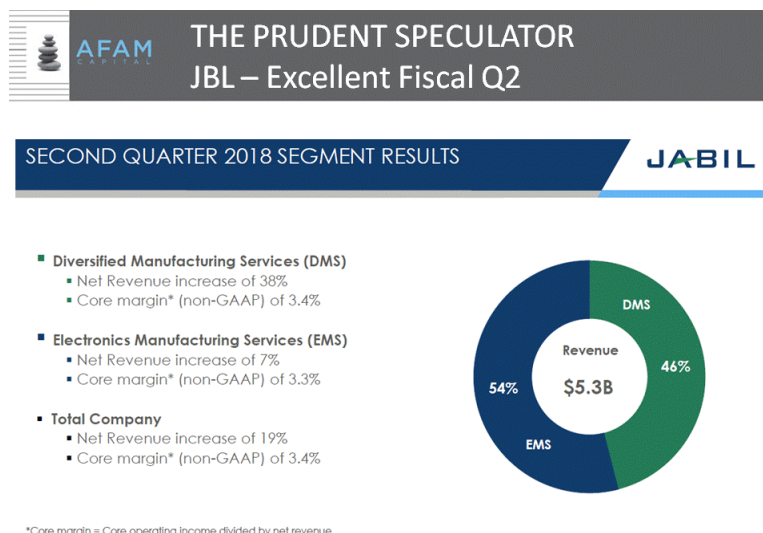
Ms. Alber continued, "We'll also accelerate our digital and supply chain investments to improve the customer experience, which we believe will result in increased sales and reduced costs" and "we are expediting the closure of a number of underperforming domestic stores. We believe this decision is aligned with shifting consumer behaviors and allows us to better leverage our resources for e-commerce growth. We estimate that we could incur one-time charges of up to approximately \$50 million, but we expect to see associated cost savings once these closures are executed."

"Looking forward to [calendar] 2018, I am optimistic about the growth opportunities that lie ahead. We will continue to execute against our four strategic priorities to strengthen our platform and drive profitable growth across our brands. A couple of key initiatives for [calendar] 2018 include the launch of buy online, pickup in store in Pottery Barn and West Elm following the successful pilot in the Williams-Sonoma brand last November and the recent rollout in Pottery Barn Kids," concluded Ms. Alber.

WSM expects to gain from a drop in domestic tax rate, which will lower taxes from 36.5% last year to between 24% and 26%. Of the \$50 million annual gain, WSM will use \$25 million for share repurchases. Certainly, increasing competition from Amazon and margin pressure aren't new risk factors for the company, and they explain a large part of the reason that the stock is trading at a bargain price by our view, but we continue to smile upon the investments in technology and in WSM's online presence, and believe those features when paired with exceptional customer service differentiate WSM's brands from the rest of the retail world. The company raised its share repurchase program authorization to \$500 million and boosted its quarterly dividend payout to \$0.43, pushing up the yield to 3.1%. Trading for just 13.1 times estimated earnings, our Target Price for WSM has been lifted to \$74.

Electronic manufacturing services firm **Jabil** (JBL – \$31.37) earned \$0.66 per share in fiscal Q2 2018 (vs. \$0.62 est.). JBL had sales of \$5.3 billion (vs. \$4.9 billion est.). Jabil benefitted from a favorable tax rate and strong performance in the DMS (Diversified Manufacturing Services) segment. Shares jumped 10% following the announcement.

CEO Mark Mondello said, "Revenue overshot the midpoint of our guidance by \$400 million, while at the same time, core earnings per share came in \$0.04 above the midpoint of our guidance range, largely driven by a favorable tax rate. So, why didn't we see additional margin dollars tied to the higher levels of revenue? The additional \$400 million of revenue was driven by the abrupt acceleration of three near-term market share wins inside of our EMS segment, combined with stronger-than-expected volumes in our Green Point sector. As for the missing margin dollars, this was based on intra-quarter investments we made in our EMS business based on the strength of the business itself combined with cost overruns in our packaging business as the team navigated tough challenges within the quarter, challenges that are common when faced with healthy growth."



Mr. Mondello added, "At Jabil, we have the scale, the infrastructure and the talent, which offer us the opportunity to move closer and closer to our aspirational goal, a goal to become the most

technologically advanced manufacturing solutions company in the world. As I sit back and I really think about this ambitious goal, I'm humbled and highly encouraged by the progress that we're making...Looking ahead to the second half of fiscal 2018, we expect the broad-based growth across both of our segments to continue as we approach \$21 billion in revenue for the year. At the same time, we remain committed to delivering \$1 billion in operating cash flows and core earnings per share of approximately \$2.60 for the year."

Although **Apple** (AAPL – \$178.02) continues to be a major customer, we like that management argues that JBL is "becoming more diversified and less dependent on any single product or product family." Apple's iPhones continue to sell strongly despite many prognosticating some sort of demand implosion, leading us to believe that Jabil's Apple-related orders will continue to hold up. We think that the EMS business is also attractive, especially as the company's products reach a wide array of markets including automotive, energy, industrial, retail, networking, telecom, cloud computing and capital equipment. Of course, we also note that the stock presently trades for just 11.7 times the current EPS estimate for the next 12 months. We have boosted our Target Price for JBL to \$44.

After reporting fiscal Q4 2018 performance that was well received by investors, **DSW Inc.** (DSW – \$21.95) saw its shares sprint up more than 15% last week. The specialty branded footwear retailer posted revenue of \$720 million, which slightly trailed consensus forecasts, while adjusted EPS for the period was \$0.38, blowing away expectations of \$0.27.

CEO Roger Rawlins explained, "Our fourth quarter performance capped our first year of adjusted earnings growth since 2013. Our initiatives drove comparable sales growth and strong margin improvement at the DSW Segment this quarter. The sales inflection at our Power 35 locations, including our Lab store where we have introduced an elevated warehouse experience, prove our initiatives are gaining traction and provide us a blueprint to drive sales. We are drawing on our strong cash flow and the benefit from U.S. Tax Reform to enhance shareholder returns by boosting our quarterly dividend and reinvesting in strategic initiatives that will advance DSW's dominant position in the marketplace in the years to come."

DSW also announced that it was shutting down its ecommerce start-up business Ebuys, after failing to find a buyer for the parent of retail sites ShoeMetro and ApparelSave, which the company acquired for more than \$60 million in March 2016 in an effort to expand its online presence via a fulfillment business that sold discounted shoes on third-party marketplaces such as Amazon and eBay. Alas, as CFO Jared Poff stated, "The challenge of sourcing the right merchandising in a sustainable way and the requirements to scale the business entails unacceptable economics in the near term."

The closure of eBuys caused management to project full year revenue growth for the current fiscal year to decrease by 1% to 3%, though excluding the exit of non-core businesses and a 53rd week, total revenue is expected to increase in the 2% to 4% range. This assumes a comparable sales increase in the low single digit range and the opening of 3 to 6 net new locations for the DSW Segment, and does not include the consolidation of the recently acquired Town Shoes. Most importantly, full year adjusted EPS is expected to range between \$1.52 and \$1.67, representing earnings growth of 4% to 14%, excluding the income from the 53rd week.

The effective tax rate is projected to drop to 29% from the historical 39% rate, thanks to the U.S. Tax Cuts and Jobs Act.

We are pleased to see operations stabilizing and modestly trending up, but we continue to understand that brick-and-mortar retail faces stiff operating headwinds from numerous directions, including titans Amazon and Walmart. That said, we believe that DSW is undervalued as it trades for less than 14 times NTM adjusted earnings, while the balance sheet contains \$300 million of cash and short-term investments, with no outstanding long-term debt, though there are rent and lease obligations. And, with the 25% increase in the dividend, shares are currently yielding a generous 4.6%. We believe that DSW has an opportunity to take market share in the fragmented footwear market and we like that management has expressed a willingness to buy back stock (with \$524.1 million remaining on its current share repurchase program...which is almost 30% of the company's outstanding market capitalization). Our Target Price has been increased to \$31.

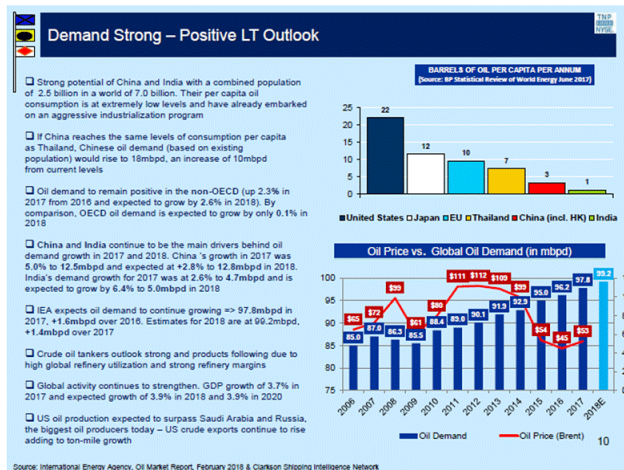
Though the stock still has a negative total return of 10% this year, shares of **Tsakos Energy Navigation** (TNP – \$3.52) bounced back a bit last week after the marine shipper reported Q4 EPS that was well ahead of consensus analyst estimates. TNP posted adjusted earnings of \$0.03 per share, far better than analyst forecasts calling for a \$0.05 loss. Revenue of \$106.6 million came in 2% below investor expectations, but TNP's fleet operated at 98% utilization in Q4. Said fleet, on a pro-forma basis, consists of 65 double-hull vessels, including 47 crude tankers, 13 product tankers and two LNG carriers. 50 vessels are in secured revenue contracts, with an average charter time of 2.6 years and minimum secured revenue of \$1.3 billion.

Despite a difficult tanker market due to a temporary surplus vessel capacity and production cuts by leading suppliers, which resulted in market spot rates in several sectors falling to exceptionally low levels, TNP's vessels achieved an average daily net revenue per vessel of \$18,343, a comparatively high rate compared to the spot market. TNP's balance sheet also remained solid with some \$203 million in cash and net debt to capital of 51%.

CEO Nikolas P. Tsakos commented, "As we enter our 25th year, we are proud to report profits in such a challenging environment. TNP's tried and tested strategy of providing downside protection while allowing for the flexibility to capture rate hikes, has proved effective once again. The markets are gradually positioning for an upturn and TNP is well placed to reap those rewards as they will occur."

The company elaborated on the outlook, "2018 started with TNP operating the largest fleet in its 25 year history, 77% of which in secured contracts averaging 2.6 years with minimum secured revenues of \$1.3 billion. Of the vessels under those fixed contracts, 40% have the ability to capture market upswings through pre-agreed profit sharing provisions which together with the vessels operating in pure spot contracts, empower the company with significant cash generating muscle when rates firm, expected in mid to late 2018...TNP continues to position its fleet to safeguard cashflows to meet all 65 vessels' costs and expenses, while having a large enough complement of spot and profit-share chartered vessels have the flexibility to take advantage of rate changes and evolving trading patterns."

AFAM CAPITAL THE PRUDENT SPECULATOR
TNP – Misunderstood Big Yield MicroCap



Though the stock has been a disappointment over the years, despite relatively sizable dividend payouts made every quarter, we remain fans of TNP as the shares change hands at 0.6 times estimated sales and 1.7 times estimated cash flow, both ratios well below the historical norms. We also like how management has navigated the turbulent industry waters: “In terms of fleet management, growth opportunities will continue to be explored and assessed provided they do not add undue burden on TNP’s balance sheet. Conversely, vessel divestments, particularly relating to our first-generation tankers, will become more important as asset prices recover, as expected, when the current schedule of newbuilding deliveries, mostly ordered on speculation, begins to decline.”

It is also worth noting that Wall Street sees TNP generating adjusted EPS in 2019 of \$0.61, after a slightly profitable 2018, though estimates are all over the map, despite 12 different analysts providing projections. And for 2020, the mean of the three EPS estimates presently offered is \$1.06, but the low estimate is a loss of \$0.39 and the high is a profit of \$1.94. Needless to say, there is hardly consensus in the forecasts, which we think creates plenty of upside potential for the stock when shipping rates improve. And, with a young fleet, a more subdued industry-wide order book going forward and relatively consistent growth in global oil demand likely for the foreseeable future, we continue to think this micro-cap name fits in well with the much more well-known integrated oil companies and oil-service names that account for the lion’s share of our Energy Sector exposure. Our Target Price for TNP remains \$7.

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