August 2, 2018

the Prudent Speculator

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> "Your attitude, not your aptitude, will determine your altitude"
>
> — Zig Ziglar

In yet another example of why the only problem with market timing is getting the timing right, *The Wall Street Journal* on July 26 reported that some $20 billion fled long-term mutual and exchange traded funds focused on large-cap stocks during June. Those outflows were the largest in more than a decade, according to data provider Morningstar LLC, and they came just in time for the S&P 500 to climb 3.72% and for the Dow Jones Industrial Average to soar 4.83% in July. The more diverse Russell 3000 index gained 3.32% for the month, while the Russell 3000 Value index jumped 3.79% versus a 2.84% advance for the Russell 3000 Growth index.

"Investors are fleeing U.S. stocks at a rapid clip as ongoing market volatility and trade tensions push them to seek safety among less risky assets such as U.S. Treasurys," the publication proclaimed, citing one prominent investment strategist who has been "urging clients with heavy exposure to stocks to pare those positions and buy more government bonds." While one month is far too short a period to measure the value of that advice, it is fascinating to note that not only did equity-light investors miss out on some handsome returns during July, supposedly less risky government bonds had negative returns, led by a 1.50% one-month loss on the benchmark 30-Year U.S. Treasury. And it wasn't as if market volatility and trade tensions vanished during the period!

Certainly, we respect that anything can happen in the equity markets, but we have long believed that the secret to success in stocks is not to get scared out of them. Sadly, this is easier said than done these days, especially as investors are bombarded with perpetual stimuli to do something with their portfolios and are provided the ability to very inexpensively transact with a few key strokes.

Of course, it is not just folks on Main Street that find it difficult to resist the siren songs to trade. Indeed, the Chief Investment Officer of CalSTRS said last month, "Over 10 years, we struggled," considering that the largest education-only pension fund in the world had an average annualized return on investment for the decade of 6.3% as of June 30. That figure doesn't sound too bad, but it would have been better had CalSTRS not slashed its global equity long-term target from 54% to 47% in 2009 AFTER the carnage of the Financial Crisis. Unfortunately, data published last year in *The Wall Street Journal* showed that public pension plans had basically maintained an allocation to public equities of slightly more than 50% from 2010 to 2017. As such, and given that the S&P 500 skyrocketed more than 180% over those eight years, pension managers had to sell a lot of stock to keep the equity allocation from growing.

To be sure, we realize that pension plans and many other investors cannot stomach the ups and downs associated with an all-equity portfolio, despite the long-term average annualized returns of 13.4% for Value Stocks and 10.5% for Dividend Payers, but we continue to believe that those who share our long-term time horizon should have the lion's share of their investable dollars in stocks. This is especially true, given the strength of corporate profits (81.7% of S&P 500 members that have reported Q2 results have beat estimates) and the generally positive economic backdrop (the Federal Reserve said this week, "Economic activity has been rising at a strong rate"). We also like the historically low interest rate environment (the current yield of 2.99% on the 10-Year U.S. Treasury is well below the 56-year average of 6.18%) and the reasonable valuations for our stocks (TPS Portfolio presently sports an average forward P/E ratio of 12.9, vs. 17.5 for the S&P 500, and a dividend yield of 2.7%, compared to 1.8% for the Russell 3000). Throw in the most recent AAII Sentiment Survey, whereby only 29.1% were Bullish (versus a 38.3% three-decade average), and we see no reason to alter our optimistic long-term view, even as we always must be braced for downside volatility.

Chief Investment Officer
Al Frank Asset Management (AFAM)

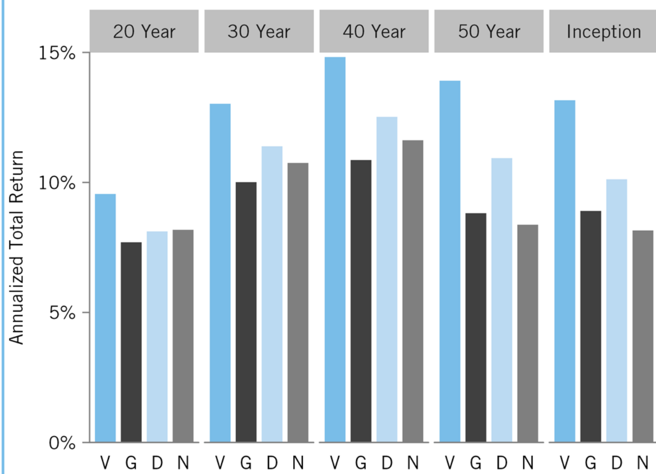
Graphic Detail

Valuation Factors Revisited: Historical Evidence

While it was nice to see two of the so-called FANG stocks spend a little time out at the woodshed during July, with Facebook skidding 11.2% and Netflix tumbling 13.8% during the month, 2018 has gone much the same as 2017 in terms of the Value vs. Growth competition. We would think that folks would naturally gravitate toward inexpensive stocks, given that most seek bargains in their everyday lives, even if it is at the local Ferrari dealer, but it is surprising that few investors seem interested in Value strategies with the weight of the historical

LT FF RETURNS: BV/PRICE & DIVIDENDS

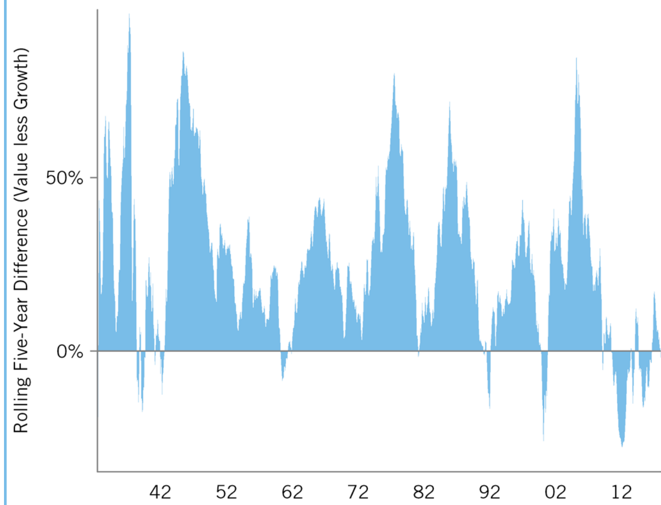
Historical data published by Fama & French (FF) show the merits of Value stocks (high Book Equity to Price) and Dividend Payers...



As of 12.31.17. Value stocks (V) are the highest 30% of Book Equity to Market Equity (BE/ME). Growth stocks (G) are the lowest 30% of Book Equity to Market Equity (BE/ME). Dividend payers (D). Non-Dividend payers (N). SOURCE: Al Frank using data from Professors Eugene F. Fama and Kenneth R. French

ROLLING 5-YEAR FF VALUE LESS FF GROWTH

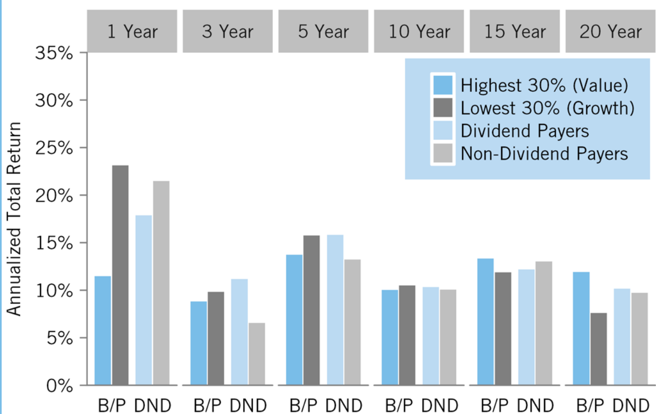
...though it has been tough sledding for Value-oriented strategies of late, which is by our view a contrarian buy signal.



From 06.30.27 through 12.31.17. SOURCE: Al Frank using data from Professors Eugene F. Fama and Kenneth R. French

ST AFAM RETURNS: BOOK VALUE & DIVIDENDS

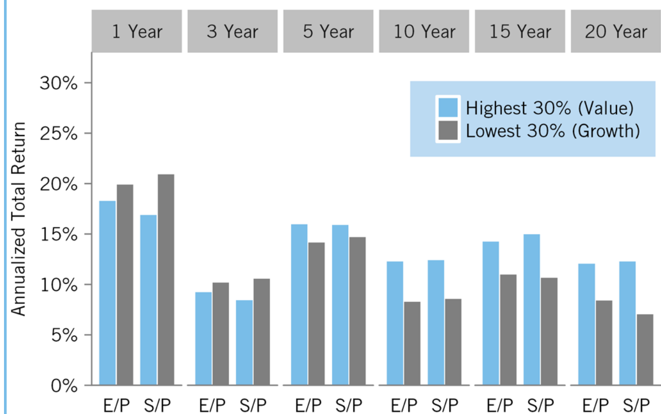
Our own number crunching validates the long-term Fama/French findings, though 2017 was not kind to Value investors,...



As of 12.31.17. Portfolios are formed using the Russell 1000 ranked by decile on (B/P) Tangible Book Value to Price and (DND) Dividend Yield (Dividend Payers vs. Non-Payers) at the end of each year. Stocks that cease trading mid-year are given the risk-free return for the balance of the year. Rebalanced annually. SOURCE: Al Frank using data from Bloomberg

ST AFAM RETURNS: EARNINGS & SALES

...with the three calendar years dating back to the end of 2014 also showing lagging relative returns for Value.



As of 12.31.17. Portfolios are formed using the Russell 1000 ranked by decile on (E/P) Earnings per share divided by Price and (S/P) Sales per share divided by Price at the end of each year. Stocks that cease trading mid-year are given the risk-free return for the balance of the year. Rebalanced annually. SOURCE: Al Frank using data from Bloomberg

evidence suggesting that inexpensive stocks have produced the best long-term returns. No doubt, we live in a world where attention spans are short, financial journalism is sensational and time horizons are focused on instant gratification, but we remain loyal to our four-decade-old strategy of buying and harvesting undervalued stocks, most often of dividend-paying companies.

Obviously, the long-term returns of *The Prudent Speculator* make it easier to keep the faith when investors are periodically tilting toward Growth stocks, but we can't forget that it was as recently as 2016 that Value had some time in the sun as the Russell 3000 Value index returned 17.4% that year, compared to a 7.4% advance for the Russell 3000 Growth index. And, while we might lament that we missed out on an Amazon or a Tesla, our analytics have allowed us to buy and hold stocks like **Apple**, **Alphabet** (aka Google) and **Microsoft**. Of course, each of those now "hot" tech names passed our valuation screens, so there is not one simple mathematical formula that determines whether a stock is worthy of our ownership.

Indeed, we hardly think that the traditional price-to-book-value distinction between Value and Growth tells a complete story, so we are constantly evaluating additional metrics, many of which are displayed in the accompanying charts. As we cast our lines for new investment ideas, our objective is to always be fishing in a pond stocked with companies that exhibit characteristics of those that have proven to be better long-term performers.

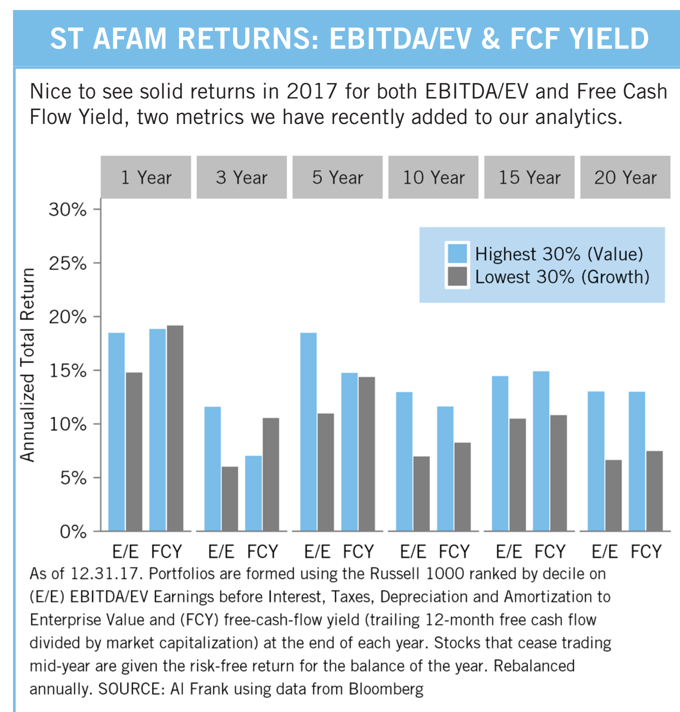
As such, we crunch plenty of our own numbers, so that we can validate the historical evidence and determine if other valuation factors are worthy of inclusion in our work. Keeping in mind that our initial screens are only one step in our investment process, we are presently thinking that Return on Common Equity and Return on Invested Capital are two measures worthy of consideration, given very good long-term AND more recent performance.

FIRST HALF OF 2018 FACTOR PERFORMANCE

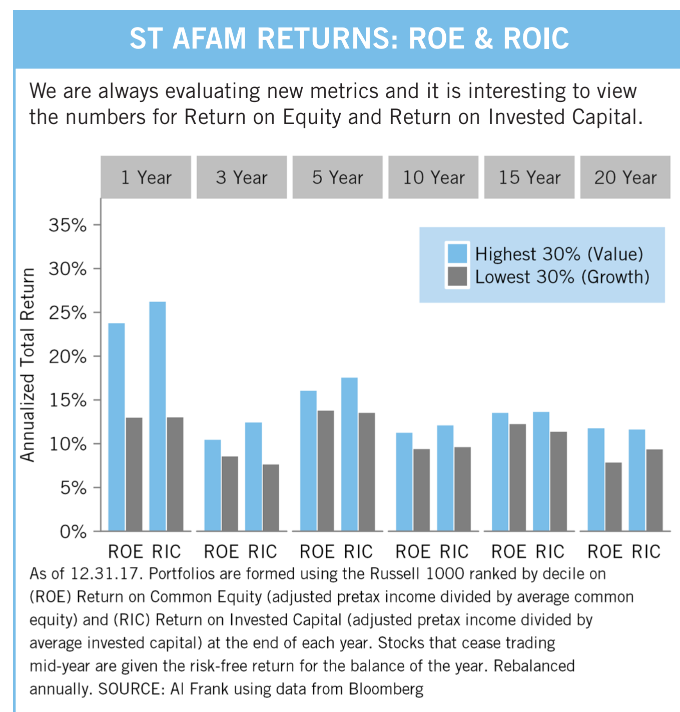
Value (High 30%) metrics performed poorly on a relative basis in the first half of 2018, more or less across the board.

Metric	High 30%	Middle 40%	Low 30%
BOOK/P *Book Value per share divided by Price*	0.2%	1.3%	7.3%
TBV/P *Tangible Book Value per share divided by Price*	1.8%	2.1%	5.9%
DVD Yield *Dividends paid per share divided by Price (must be a dividend-paying company)*	0.6%	0.4%	0.4%
E/P *Earnings per share divided by Price*	-1.9%	0.7%	7.2%
SALES/P *Sales per share divided by Price*	0.2%	1.1%	7.9%
EBITDA/EV *Earnings before Interest, Taxes, Depreciation and Amortization to Enterprise Value*	0.5%	1.0%	7.5%
FCFY *Free Cash Flow per share divided by Price*	1.3%	3.2%	4.2%
ROCE *Adjusted Pretax Income divided by Average Common Equity*	1.5%	1.5%	5.6%
ROIC *Adjusted Pretax Income divided by Average Invested Capital*	3.1%	1.5%	4.3%
Average	0.8%	1.4%	5.6%

From 12.31.17 through 06.30.18. Portfolios are formed using the Russell 1000 ranked by decile. Deciles are grouped into three buckets (High 30%, Middle 40% and Low 30%), then averaged. Stocks that cease trading mid-year are given the risk-free return for the balance of the year. SOURCE: Al Frank using data from Bloomberg



As of 12.31.17. Portfolios are formed using the Russell 1000 ranked by decile on (E/E) EBITDA/EV Earnings before Interest, Taxes, Depreciation and Amortization to Enterprise Value and (FCY) free-cash-flow yield (trailing 12-month free cash flow divided by market capitalization) at the end of each year. Stocks that cease trading mid-year are given the risk-free return for the balance of the year. Rebalanced annually. SOURCE: Al Frank using data from Bloomberg



As of 12.31.17. Portfolios are formed using the Russell 1000 ranked by decile on (ROE) Return on Common Equity (adjusted pretax income divided by average common equity) and (RIC) Return on Invested Capital (adjusted pretax income divided by average invested capital) at the end of each year. Stocks that cease trading mid-year are given the risk-free return for the balance of the year. Rebalanced annually. SOURCE: Al Frank using data from Bloomberg

Recommended Stocks

In this space, we list each month 40 of our most attractively priced recommended stocks. All trade for significant discounts to our determination of long-term fair value and/or offer favorable risk/reward profiles. Note that, while we always seek substantial capital gains, we require lower appreciation potential for stocks that we deem to have more stable earnings streams, more diversified businesses and stronger balance sheets. The natural corollary is that riskier companies must offer far greater upside to warrant a recommendation. Further, as total return is how performance is ultimately judged, we explicitly factor dividend payments into our analytical work. ■

				Target	Price Multiples			EV/	FCF	Debt/	Div	Mkt
Industry Group	Ticker[1]	Company	Price	Price	EPS	Sales	TBV[2]	EBITDA[3]	Yield[4]	TE[5]	Yield	Cap
Autos & Components	GM	General Motors	37.91	54.94	6.1	0.4	1.8	2.6	12.7	230%	4.0%	53,487
	GT	Goodyear Tire & Rubber	24.21	41.92	8.6	0.4	1.5	5.8	7.3	146%	2.3%	5,738
Banks	C	Citigroup	71.89	102.87	12.1	nmf	1.2	nmf	nmf	nmf	2.5%	180,919
	FITB	Fifth Third Bancorp	29.59	40.00	13.5	nmf	1.6	nmf	nmf	nmf	2.4%	20,067
	NYCB	NY Community Bancorp	10.77	14.13	15.5	nmf	1.4	nmf	nmf	nmf	6.3%	5,281
Capital Goods	CAT	Caterpillar	143.80	188.84	14.5	1.7	13.0	8.5	2.6	360%	2.4%	85,985
	CMI	Cummins	142.81	202.10	11.6	1.0	4.4	8.0	6.1	29%	3.2%	23,322
	SIEGY	Siemens AG	70.68	94.05	14.8	2.5	21.2	11.8	4.0	537%	2.4%	120,156
Commercial Services	MAN	ManpowerGroup	93.26	142.40	11.3	0.3	5.2	7.1	6.1	89%	2.2%	6,139
Consumer Dur & App	MDC	MDC Holdings	29.04	51.99	8.8	0.6	1.1	10.0	-7.4	72%	4.1%	1,633
	WHR	Whirlpool	131.10	209.74	9.4	0.4	nmf	16.1	2.1	nmf	3.5%	8,464
Diversified Financials	GS	Goldman Sachs Group	237.43	304.17	10.0	nmf	1.4	nmf	nmf	nmf	1.3%	93,148
	SYF	Synchrony Financial	28.94	50.30	9.2	nmf	1.7	nmf	nmf	nmf	2.9%	21,435
Energy	RDS/A	Royal Dutch Shell PLC	68.37	91.02	13.2	0.4	1.4	7.3	3.6	41%	4.7%	290,723
	SLB	Schlumberger Ltd	67.52	105.30	39.5	2.9	41.2	29.4	3.8	611%	3.0%	93,456
Food & Staples Retailing	KR	Kroger	29.00	39.36	13.2	0.2	7.8	7.4	3.2	409%	1.9%	23,104
Food, Bev & Tobacco	TSN	Tyson Foods	57.65	86.65	10.0	0.6	nmf	9.0	7.6	nmf	2.1%	23,032
Health Care Equp/Srvcs	MCK	McKesson	125.60	200.71	9.6	0.1	nmf	29.2	7.4	nmf	1.2%	25,091
	MDT	Medtronic PLC	90.23	103.31	18.9	4.1	nmf	14.7	3.0	nmf	2.2%	121,965
Household Products	KMB	Kimberly-Clark	113.86	134.91	17.6	2.1	nmf	13.7	5.7	nmf	3.5%	39,585
Insurance	AZSEY	Allianz SE	22.06	28.99	11.5	nmf	1.6	nmf	nmf	nmf	3.2%	94,809
Materials	IP	Int'l Paper	53.73	77.75	12.0	1.0	6.4	9.1	1.3	312%	3.5%	22,249
Media	DIS	Walt Disney	113.56	146.81	17.8	3.0	24.7	11.4	6.2	274%	1.5%	168,835
Pharma/Biotech/Life Sci	GILD	Gilead Sciences	77.83	119.32	10.5	4.3	90.5	7.1	10.4	2384%	2.9%	100,868
	PFE	Pfizer	39.93	45.93	13.9	4.4	nmf	13.3	6.2	nmf	3.4%	233,573
	SNY	Sanofi	43.36	58.12	14.0	5.3	32.6	17.2	nmf	799%	3.4%	108,413
Real Estate	DOC	Physicians Realty Trust	15.76	21.67	15.5	nmf	1.2	nmf	nmf	nmf	5.8%	2,868
	KIM	Kimco Realty	16.69	22.73	11.0	nmf	1.6	nmf	nmf	nmf	6.7%	7,033
Retailing	FL	Foot Locker	48.81	77.77	11.6	0.7	2.4	6.7	13.9	5%	2.8%	5,706
	WSM	Williams-Sonoma	58.49	77.33	15.4	0.9	4.1	7.3	7.6	25%	2.9%	4,861
Semis & Cap Equipment	INTC	Intel	48.10	60.30	12.0	3.3	6.5	8.1	5.6	72%	2.5%	221,789
	LRCX	Lam Research	190.64	253.20	10.4	2.7	6.4	7.5	7.9	40%	2.3%	29,910
Software & Services	GOOG	Alphabet	1217.26	1581.25	25.0	6.9	6.0	22.8	2.5	3%	0.0%	850,031
	IBM	Int'l Business Machines	144.93	195.67	10.3	1.6	nmf	9.9	9.5	nmf	4.3%	132,287
	ORCL	Oracle	47.68	58.04	15.2	4.8	nmf	11.1	7.0	nmf	1.6%	189,821
Technology Hardware	BHE	Benchmark Electronics	24.20	34.15	15.2	0.5	1.2	6.1	-2.4	19%	2.5%	1,149
Telecom Services	T	AT&T	31.97	43.85	9.7	1.5	nmf	9.3	9.4	nmf	6.3%	232,134
Transportation	ALK	Alaska Air Group	62.83	101.95	12.9	1.0	5.1	5.9	4.5	131%	2.0%	7,744
	DPSGY	Deutsche Post AG	35.35	56.40	14.2	0.6	34.4	8.8	3.2	1163%	3.9%	43,625
	FDX	FedEx	245.87	328.45	16.0	1.0	5.5	9.7	-1.5	127%	1.1%	65,383

As of 07.31.18. N/A=Not applicable. nmf=Not meaningful. [1] ●=First-time recommendation. [2]Tangible book value. [3]Enterprise value-to-earnings before interest taxes depreciation and amortization. [4]Free cash flow yield. [5]Tangible equity.
SOURCE: AFAM Capital using data from Bloomberg Finance L.P.

AFAM also offers private asset management services. To learn more, contact 512.600.1818 or visit afamcapital.com

Portfolio Builder

Research Team Highlights

The Prudent Speculator follows an approach to investing that focuses on ***broadly diversified*** investments in ***undervalued*** stocks for their ***long-term*** appreciation potential. Does that mean we build portfolios of 20 stocks…30…? More like 50 and up. We like stocks. And we like a lot of 'em. We don't rely nearly as much on "how many" as we do "in which," but we tend to invest in far more names than most. This expansive diversification, we find, potentially serves us well in two ways: we can further minimize the risk of individual stock ownership, while maximizing the likelihood of finding the truly big winners among the undervalued masses.

As for the "in which" part, readers should know we discriminate among potential investments primarily by their relative valuation metrics and our assessments of stock-specific risk. We buy only those stocks we find to be undervalued along several lines relative to their own trading history, those of their peers or that of the market in general. Our Target Prices incorporate a range of fundamental risks (e.g. credit, customer and competitive dynamic) that we believe the companies may face over our normal three-to-five-year investing time horizon.

Each month in this column, we suggest to readers a group of ten stocks with which to populate portfolios. The list could serve as a portfolio foundation for new investors or as a pick-list for folks already maintaining well-diversified holdings, while we usually add the names to one of our newsletter portfolios. Note that we are in no way suggesting that these stocks replace those featured in prior months as we will always issue a *Sales Alert* should we choose to exit a position. And, until such time as we say sell, any of our 100+ recommended stocks should be viewed as a worthy purchase candidate.

This Month's Theme

Having a little cash to redeploy, the by-product of recent sales and dividends, we will purchase $10,000 of **McKesson** in Millennium Portfolio and $7,000 of **Synchrony Fin'l** in Buckingham Portfolio. We will also raise the ownership in the latter portfolio to $7,000 in **AT&T** and **Schlumberger**. We already have sufficient company/sector exposure in **Fifth Third Bancorp**, **Gilead Sciences, Goldman Sachs**, **IBM**, **Kroger** and **Pfizer**, so no additional purchases of any of those six this month. As usual, we will wait four trading days, until August 8, to transact.

NEWSLETTER PORTFOLIO PURCHASES

Ticker	Company	Sector	Price	Target Price
FITB	Fifth Third Bancorp	Financials	29.59	40.00
GILD	Gilead Sciences	Health Care	77.83	119.32
GS	Goldman Sachs Group	Financials	237.43	304.17
IBM	Int'l Business Machines	Information Technology	144.93	195.67
KR	Kroger	Consumer Staples	29.00	39.36
MCK	McKesson	Health Care	125.60	200.71
PFE	Pfizer	Health Care	39.93	45.93
SLB	Schlumberger Ltd	Energy	67.52	105.30
SYF	Synchrony Financial	Financials	28.94	50.30
T	AT&T	Telecom Services	31.97	43.85

As of 07.31.18. SOURCE: AFAM Capital using data from Bloomberg Finance L.P.

Fifth Third Bancorp (FITB)

Fifth Third is a diversified financial services company with $141 billion in assets, operating numerous full-service banking centers and ATMs in the Midwest and Southeastern U.S. FITB operates four main businesses: Commercial Banking, Branch Banking, Consumer Lending and Wealth & Asset Management. The firm has seemingly solid pricing power with attractive market share and a loyal client base in a number of its markets. Shares are down some 13% since mid-May and investors weren't wild about Q2 results. Although the company delivered a solid bottom-line beat, sluggish organic loan growth, a tick up in non-interest expenses and M&A risk from its MB Financial purchase were catalysts for a short-term sell-off. While there are still some headwinds to overcome, we were pleased to see net interest margins expand, with the bank continuing decent upper-single-digit net interest income growth, and we liked that expenses remained in check. We continue to believe that FITB is a good regional bank to own in a diversified equity portfolio, and while we respect that the MB Financial acquisition was a bit pricey, in the long run it should improve the company's operating leverage potential. Shares trade for an inexpensive 11.7 times NTM earnings estimates and yield 2.4%.

Gilead Sciences (GILD)

Gilead is a biotech giant whose portfolio of products and pipeline of investigational drugs includes treatments for HIV/AIDS, liver diseases, cancer, inflammatory

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and respiratory diseases, and cardiovascular conditions. GILD delivered solid numbers for Q2, beating on both the top- and bottom-lines (adjusted EPS of $1.91 vs. $1.56 est. and revenue of $5.65 billion vs. $5.19 billion est.), but the performance was a bit overshadowed by the announcement that CEO John Milligan would be stepping down. While we are not excited to see another C-Suite member depart, we were pleased to see the Q2 strength in the HIV business and stabilization in the hepatitis C franchise. We believe the better trends in the company's core products plus pipeline potential in oncology and NASH medications in the second half of 2019 could be the tailwind shares need to regain their glory. We continue to be constructive on the firm's solid balance sheet that allows management to buy back shares, and support and boost the dividend. GILD trades for less than 12 times estimated earnings and yields 2.9%.

Goldman Sachs Group (GS)

Goldman is a global investment banking, securities and investment management firm with leading positions in M&A, equity underwriting and equity trading. The company also generates significant revenue from its investing, lending and FICC businesses, while asset management is a major focus. Goldman shares are down on the year and have seemingly been stuck in neutral for some time. Nonetheless, we were pleased to see the Wall Street titan turn in a Q2 bottom-line beat that was more than 28% higher than consensus estimates and was the highest second quarter in nine years. The firm also announced the Lloyd Blankfein would step down as CEO and be replaced by David Solomon. While the legacy of Mr. Blankfein is open to debate, Mr. Solomon is taking the helm with the company in solid shape and with a lot of potential ahead. We continue to be fans of GS and like prospects for stronger revenue growth, operating leverage, potential de-regulatory policies and a possible higher price-to-forward-earnings multiple than the present 9.5.

Int'l Business Machines (IBM)

IBM is a leading provider of enterprise solutions, offering a broad portfolio of IT hardware, business and IT services, and a full suite of software solutions. IBM earned $3.08 per share in fiscal Q2 2018 (vs. $3.04 est.) and had sales of $20.0 billion (vs. $19.9 billion est.). Shares reacted well as IBM's Strategic Imperatives have started to pay off (sales up 26% y-o-y) and Technology Services & Cloud Platforms revenue grew. IBM reaffirmed its full-year guidance of at least $13.80 per share and free cash flow of about $12 billion. We remain fans of Big Blue and believe that a stand-alone Strategic Imperatives business would likely be worth more on its own than the current overall market cap. Of course, we understand that IT stocks in general have been on an almost-uninterrupted rise since 2009, and IBM's leadership and execution have left lots to be desired. Still, we are glad to see the Q2 improvement and that IBM trades for 10.4 times forward EPS, while the company has been buying back shares. IBM yields 4.3%.

Kroger (KR)

Kroger is one of the world's largest grocers, operating 2,779 supermarkets in 35 states and serving more than 9 million customers daily. After a tough 2017, shares have performed admirably in 2018, and Kroger continues to evolve its business to fend off the long-standing pressures of its numerous competitors (including giants Amazon/Whole Foods, Walmart and Aldi). While there is little doubt that competitive headwinds will continue, we believe that the challenging backdrop is understood and we like the strides and operational momentum the company has been making, not to mention its focus on online services and investments designed to engage its customers on inventory and store offerings. Fiscal Q1 2019 saw KR deliver better than expected top-line results and adjusted EPS that was 13% better than forecast. KR shares now yield 1.9% after a 12% dividend increase in late June. Shares currently trade at a very reasonable 13.7 times NTM adjusted EPS projections and KR is an example of the opportunity created for long-term-oriented investors when a stock is "Amazon-ed" by short-sighted traders.

McKesson (MCK)

McKesson is the largest pharmaceutical distributor in the U.S., providing drugs, medical products and supplies, as well developing, implementing and supporting information technology software that facilitates the integration of data through the health enterprise. Although MCK reported adjusted EPS of $2.90 in fiscal Q1 2019 that was four cents better than the consensus estimate, shares tumbled because the beat was primarily driven by a reduced tax rate. MCK has weathered contract shifts, lower price inflation of generic drugs, attention from Capitol Hill and in the media, and most recently the acquisition of online pharmacy PillPack by Amazon. CEO John Hammergren defended the company's position when rumors were circling late last year, and did so again in the Q1 earn-

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ings call, stating, “We believe we are well-positioned to drive future growth with our scaled and efficient foundation, our clear focus on several priority growth areas and improving the efficiency of our operating structure...We are extremely well-positioned to execute our portfolio approach to capital deployment and to deliver value for our shareholders through a mixture of internal capital investments, acquisitions, share repurchases and dividends.” Operational headwinds are unlikely to subside soon, but the important role the company plays in getting medical supplies and medicines from manufacturers to pharmacies, clinics and hospitals remains vital. Continued integration of acquisitions and pending improvements in its health care IT business should help drive growth. MCK trades for 9.2 times NTM earnings expectations.

Pfizer (PFE)

Pfizer is a well-known global pharma giant. While it is difficult to forecast whether potential actions from Washington will lead to lower or pressured product pricing, PFE already agreed to defer some announced price increases after being criticized by President Trump. That considered, the company reported a solid Q2 with both its top- and bottom-line results outpacing analyst estimates. While many remain concerned about generic competition for some of Pfizer’s older drugs, as well as the pending Lyrica patent expiration in 2019, we believe that the market underappreciates the company’s emerging pipeline of products and management’s increasing confidence in its organic growth potential. We like the strong balance sheet and that management said it will continue to focus on dividend growth and share repurchases. Pfizer also continues to strategically review its consumer business. That said, it seems to have shifted away from M&A and is instead targeting growing its product pipeline. PFE yields 3.4% and trades for less than 13 times NTM earnings.

Schlumberger Ltd (SLB)

Schlumberger is the world’s largest provider of services and equipment used in drilling, evaluation, completion, production and maintenance of oil and natural gas wells. The company reported Q2 earnings of $0.43 per share (vs. $0.43 est.) on revenue of $8.3 billion (vs. $8.4 billion est.). SLB saw operational delays that resulted in less margin expansion than expected, but growing E&P spending amid a climbing oil price environment should result in double-digit growth in its international business next year. Having the largest global oil services platform, a dominant international franchise, the potential benefits from recent acquisitions and the most balanced exposures of the diversified service providers, we continue to believe that SLB is one of the best-positioned energy names. We concur with management that the international space is ready for an upturn. We also like the solid free cash flow and that the high-quality stock currently yields 3.0%.

Synchrony Financial (SYF)

Synchrony provides a range of credit products through programs established with local, regional and national retailers, manufacturers, industry associations and healthcare providers. The company’s success has been driven by its private-label credit business. SYF performs the underwriting for the partners and retains the receivables while paying out rewards to retailers. Synchrony posted earnings per share of $0.92, versus the $0.82 estimate in fiscal Q2 2018, but shares have fallen more than 15% on news that the company will lose its Walmart store-branded credit card business to Capital One. SYF management is leaning towards keeping the Walmart portfolio and converting the accounts to general purchase cards, rather than selling the portfolio. The termination frees up more than $1 billion of capital (by management estimates) which could be used to go after new business or buy back more than 4% of the outstanding Synchrony shares. SYF yields 2.9% and trades for 8 times estimated earnings.

AT&T (T)

Telecom behemoth AT&T provides telephone, television, Internet and wireless service across the country. The company maintains a high-speed mobile internet network that covers 400 million people in North America and a broadband service with 60 million customer locations. In Q2, AT&T earned $0.91 per share on revenue of $39.0 billion, versus estimates of $0.85 and $39.6 billion, respectively. CEO Randall Stephenson said, “After 600 days of reviews and litigation, we did finally complete the acquisition of Time Warner. And we announced our agreement to acquire AppNexus [an ad technology company]. We’ve now assembled the key elements of a modern media company, and it all begins with owning a wide array of premium content.” In addition to ongoing strategic spending for parts of the wireless spectrum and digital content, we like that T continues to return cash to holders. The yield is a whopping 6.3%. With the Time Warner (now called WarnerMedia by T) deal complete, we think it an especially favorable time to buy AT&T.

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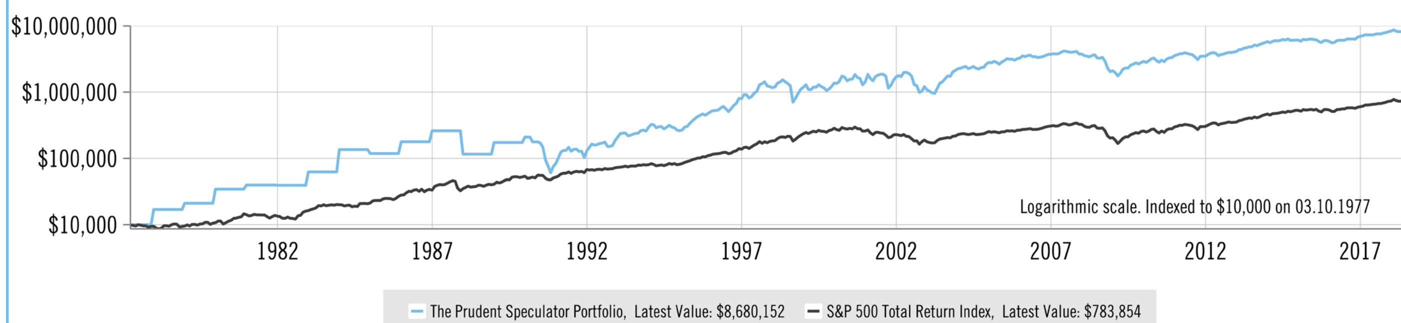
NEWSLETTER PORTFOLIO PERFORMANCE



	Jul	YTD	1-Year	3-Year	5-Year	10-Year	15-Year
Newsletter Portfolios							
Buckingham	4.35	4.42	15.19	11.19	10.14	8.14	10.24
Millennium	4.72	3.68	13.25	11.67	10.45	10.56	10.00
PruFolio	4.33	1.64	8.93	10.05	9.68	9.81	10.33
TPS	4.53	3.81	13.86	12.13	11.00	10.33	12.02
Major Indexes							
Russell 3000	3.32	6.64	16.39	12.18	12.83	10.68	9.68
Russell 3000 Value	3.79	2.59	9.91	9.77	10.05	9.00	8.87
S&P 500	3.72	6.47	16.23	12.51	13.12	10.66	9.44
Dow Jones Indu. Avg.	4.83	4.07	18.75	15.68	13.11	11.26	9.70

	Inception Date	Since Inception	Index Return	Index
Newsletter Portfolios				
Buckingham	01.21.03	12.58	10.30	Russell 3000
Millennium	12.31.99	9.78	6.02	Russell 3000
PruFolio	12.29.00	12.94	6.84	Russell 3000
TPS	03.10.77	17.79	11.13	S&P 500

Since *The Prudent Speculator's* launch in March 1977, its 1,887 stock recommendations have returned, on average, an annualized 17.32%, not including dividends.

IMPORTANT INFORMATION

As of 07.31.18. All data are total returns, except for that of all recommended stocks, which exclude dividends. Data for periods greater than one year are annualized. The Dow Jones Industrial Average Index is a price-weighted average of 30 actively traded blue-chip stocks, primarily industrial, including stocks that trade on the New York Stock Exchange and NASDAQ. The Russell 3000 Index measures the performance of the largest 3,000 US companies and represents approximately 98% of the investable US equity market. The Russell 3000 Value Index measures the performance of those Russell 3000 Index companies with lower price-to-book ratios and lower forecasted growth values. The Standard & Poor's 500 Stock Index (S&P 500) is an unmanaged index of 500 stocks that is generally representative of the performance of larger companies in the U.S. 1 The Russell 3000 Index lacks sufficient history to match that of Al Frank's TPS Portfolio. We therefore have shown the S&P 500 Index for comparison purposes. It is not possible to invest directly in an index. SOURCE: AFAM Capital using data from Bloomberg Finance L.P.

TPS Portfolio is Al Frank's actual investment portfolio. Though not presently leveraged, it has been so in the past. Buckingham Portfolio is John Buckingham's actual investment portfolio. Though not presently leveraged, it has been so in the past. Millennium Portfolio is unleveraged and hypothetical. PruFolio is unleveraged and hypothetical.

All portfolio returns are calculated on a total return basis and reflect the reinvestment of dividends, if any, margin leverage and margin interest charges, trading costs and subscription costs. There are inherent limitations with in hypothetical or model portfolio results as the securities are not actually purchased or sold. They may not reflect the impact, if any, of material market conditions which could have has an impact on AFAM's decision making if the hypothetical portfolios were real. Hypothetical performance is shown for illustrative purposes only and should not be interpreted as an indication of performance of any AFAM portfolio. The use of leverage magnifies gains and losses and increases risk to a portfolio.

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