Market Commentary Monday, April 29, 2019

April 29, 2019

EXECUTIVE SUMMARY

TPS 631 – Coming on Friday, May 3
Week in Review – Record Highs on the S&P; But Dow and Other Stocks Struggle
Econ News – Solid Numbers Out Last Week
Earnings – Continued Profit Growth Expected
The Case for Dividends – Competitive (and Rising) Income, Higher Returns and Lower Volatility
Market of Stocks – 25 Undervalued Bargains Yielding More than 3%
Stock Updates – AVX, T, MSFT, LRCX, INTC, DLR, BHE, TRN, NSC, XOM, GT, IP, KMB, CE, COF & CAT

Market Review

Work is underway on the May edition of *The Prudent Speculator*. If all goes according to plan, we will strive to have *TPS 631* emailed to readers no later than Friday morning May 3. This month, our Graphic Detail will review market seasonality and will also examine the composition of several of the index ETFs that have drawn so many investor dollars.

The S&P 500 closed at an all-time high on Friday, no doubt thanks to a flurry of generally favorable first quarter earnings reports from Corporate America. Per data from FactSet, with 46% of the companies in the S&P 500 having reported actual results for Q1 2019, 77% have posted EPS above estimates, which is above the five-year average.

True profit expectations had been watered down and there have been more than a few disappointments, including last week, when the Dow Jones Industrial Average and several other individual stocks actually lost ground, but Q1 reporting season overall has been very good thus far. No doubt, bottom lines were bolstered by the fact that the initial estimate of first quarter U.S. GDP growth came in at a better-than-expected 3.2%,…

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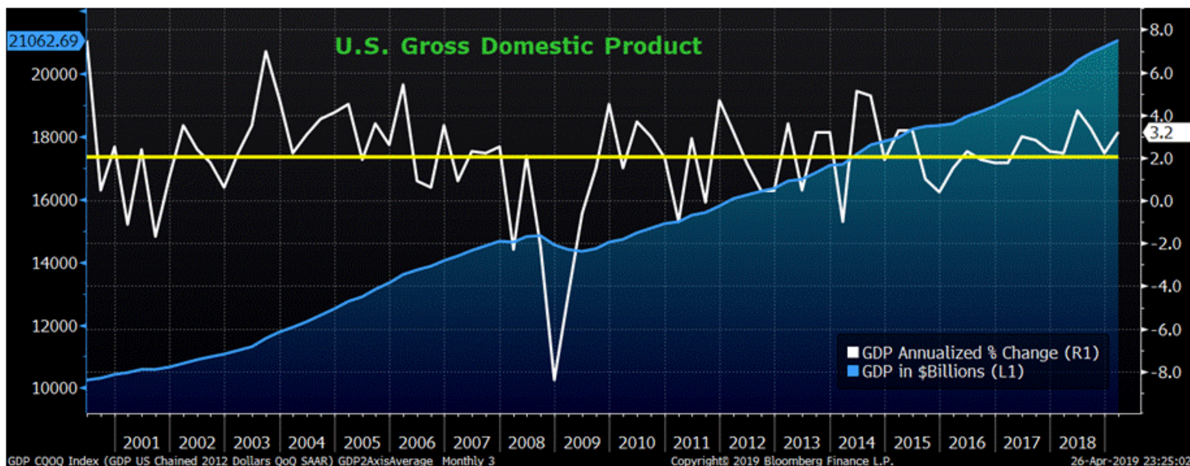
THE PRUDENT SPECULATOR
U.S. Economic Growth Picked Up in Q1

Uncle Sam calculated Q1 '19 GDP growth at a surprisingly healthy 3.2% annualized rate, improving nicely on the 2.2% rate turned in for Q4 ' 18. True, growth is likely to slow as we move forward, with some thinking a recession is imminent as ongoing trade skirmishes are not helping, but even a modest downturn would still see the economy expand on a nominal basis, with corporate profits likely remaining healthy.



…a number that was supported by other upbeat economic stats out last week.

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THE PRUDENT SPECULATOR
Improving Economic Numbers

Surprising many, given the concerns about the health of the housing market, new home sales jumped 4.5% on a month-over-month basis in March to a 692,000 annual rate, the best showing since November 2017. Meanwhile, durable goods orders last month rose a robust 2.7%, thanks to strong commercial aircraft orders, but even the durable goods orders ex-transportation number was up an impressive 0.4%.

And, the economic outlook for Q2 seems to be decent, given the latest data on the health of the consumer and the jobs picture,…

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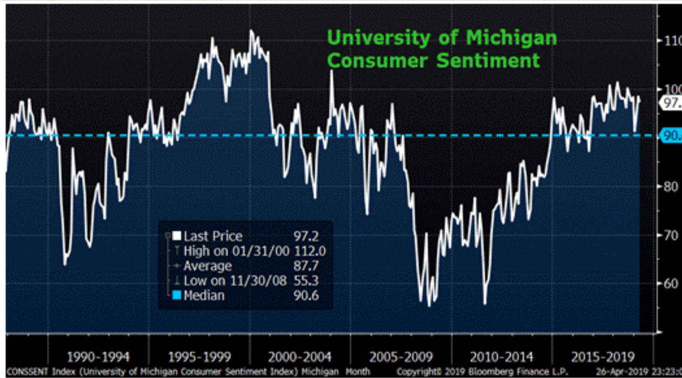
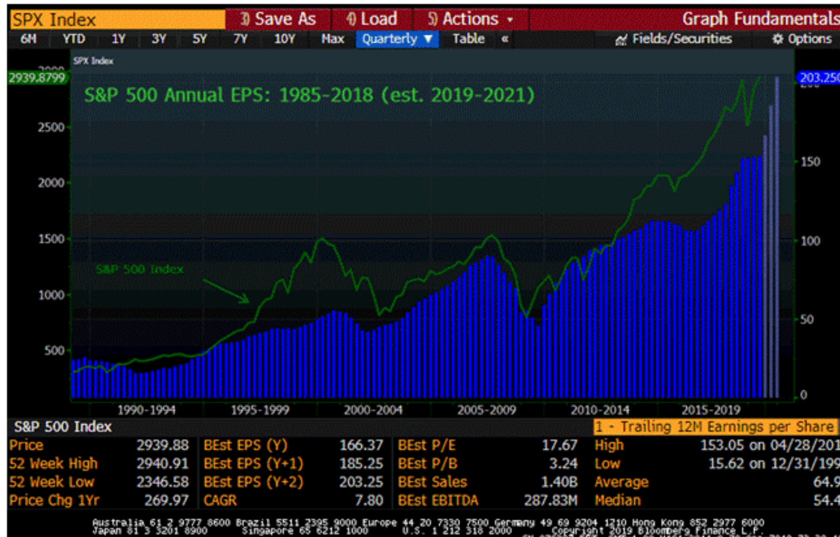
THE PRUDENT SPECULATOR
Healthy Econ Data



The latest read on consumer sentiment for April from the University of Michigan came in as expected at 97.2, versus 98.4 in March, and the figure was well above the historical average. Bouncing higher from five-decade lows, the number of first-time filings for jobless benefits climbed to 230,000 in the latest week, though the data were most likely affected by the timing of the Easter holiday. Of course, that tally is still extraordinarily low.

…all of which we think provides a solid backdrop for a continuation of generally good earnings news.

Certainly, we understand that analysts are often overly optimistic in their projections, but sizable year-over-year earnings expansion is expected in '19, with further growth likely in '20 and '21.



S&P 500 Earnings Per Share		
Quarter Ended	Bottom Up Operating EPS 3 Month	Bottom Up Operating EPS 12 Month
ESTIMATES		
12/31/2020	$49.85	$186.26
9/30/2020	$48.06	$180.87
6/30/2020	$45.86	$175.83
3/31/2020	$42.49	$170.62
12/31/2019	$44.46	$165.36
9/30/2019	$43.02	$155.93
6/30/2019	$40.65	$154.29
3/31/2019	$37.23	$152.29
ACTUAL		
12/31/2018	$35.03	$151.60
9/30/2018	$41.38	$150.42
6/30/2018	$38.65	$140.37
3/31/2018	$36.54	$132.23
12/31/2017	$33.85	$124.51
9/30/2017	$31.33	$118.56
6/30/2017	$30.51	$115.92
3/31/2017	$28.82	$111.11
12/31/2016	$27.90	$106.26
9/30/2016	$28.69	$101.42
6/30/2016	$25.70	$98.17
3/31/2016	$23.97	$98.61
12/31/2015	$23.06	$100.45

Source: Standard & Poor's. As of 4.25.19

Obviously, anything can happen in the short run, and we respect that stocks will eventually have some sort of a pullback, but we see no reason to alter our enthusiasm for the long-term prospects of our broadly diversified portfolios of what we believe to be undervalued stocks, generally of dividend-paying companies.

And speaking of dividends, your editor was interviewed by one of his favorite print journalists on Friday regarding income-oriented investments for retirees. We thought it might be "valuable" to share the notes shipped off to the reporter in support of the points discussed…

A major challenge these days for retirees and all income-oriented investors is that yields on most investable assets are very low by historical standards. Consider that the yield on the aggregate bond index is just 3.0%, compared to an average over the past four+ decades (since the launch of *The Prudent Speculator* in March 1977) of 6.6%. It is the same story with government bonds, where the 2.5% yield on the 10-Year Treasury is well below the 6.2% average. True, money market funds (like the Schwab Value Advantage fund), which had been offering income of near zero for eight years or so, now are yielding close to 2.3%, but dividends on stocks in general are very competitive vis-à-vis the yields on fixed income.

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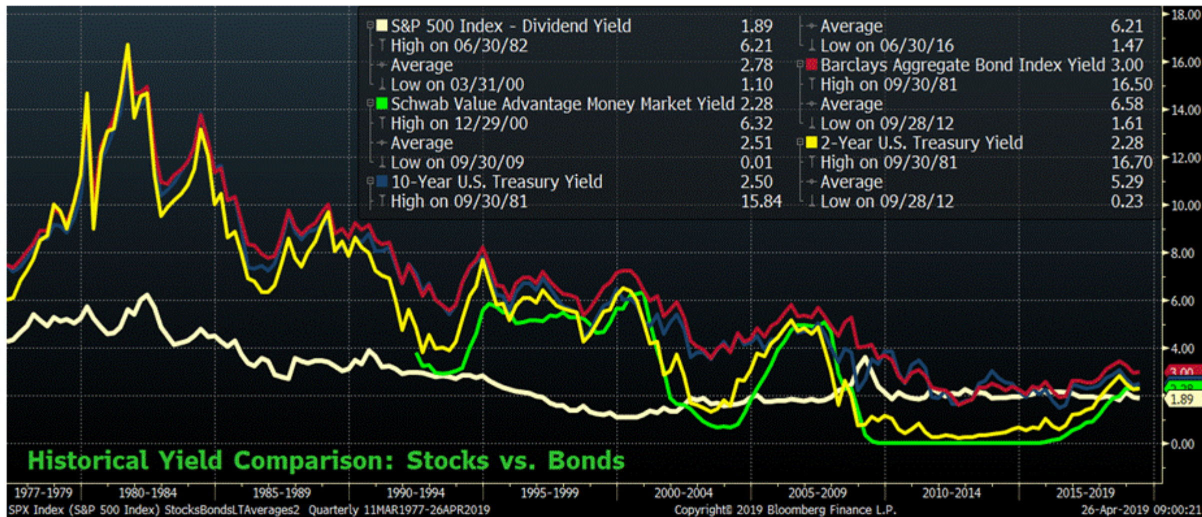
THE PRUDENT SPECULATOR
Equity vs. Fixed Income Yields

Though stocks are not necessarily a substitute for bonds, U.S. Treasuries and money market funds, the current payout on the S&P 500 (1.89%) is still very generous versus the income provided by fixed income. And, the comparison to the average yields for all of the securities below over the past four-plus decades very much favors equities.



And, it is important to note that the income streams on fixed income instruments generally are fixed, meaning no chance of a higher coupon, whereas dividend on stocks generally have risen over time. No guarantees, of course, that equity distributions will climb going forward, but the payments on the S&P 500 have nearly doubled over the last 10 years, despite that period including the Financial Crisis and lackluster economic growth once the Great Recession ended.

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THE PRUDENT SPECULATOR
Dividends Have Grown Over Time

While dividends are never guaranteed, the historical evidence suggests that Corporate America has a long history of raising quarterly payouts, whereas the coupons on most debt instruments are fixed.

COUNT OF S&P 500 DIVIDEND ACTIONS	INCREASES	INITIATIONS	DECREASES	CESSATIONS
2019 (as of 4.25.19)	142	3	4	0
2018	374	6	3	0
2017	351	5	9	2
2016	344	7	19	2
2015	344	7	16	3
2014	375	8	8	0
2013	366	15	12	0
2012	333	15	11	1
2011	320	22	5	0
2010	243	13	4	1
2009	151	6	68	10
2008	236	5	40	22
2007	287	11	8	4
2006	299	6	7	3
Source: Standard & Poor's.				

S&P 500 DIVIDENDS PER SHARE	
2020 (Est.)	$62.10
2019 (Est.)	$58.17
2018	$53.86
2017	$50.47
2016	$46.73
2015	$43.49
2014	$39.44
2013	$34.99
2012	$31.25
2011	$26.43
2010	$22.73
2009	$22.41
2008	$28.39
2007	$27.73
2006	$24.88

Source: Bloomberg. As of 4.26.19

True, holders of stocks must endure significant ups and downs that have long been associated with equity investing, but they have been well compensated over the long-term for accepting volatility. Interestingly, the statistics dating back nine decades, via portfolio return data compiled by Professors Eugene. F. Fama and Kenneth R. French, show that not only do dividend-paying stocks produce higher total returns, they have done so with lower standard deviation (a popular measure of risk).

THE PRUDENT SPECULATOR
Volatility is Normal: Value/Divs Win Race

Selloffs, downturns, pullbacks, corrections and even Bear Markets are events that equity investors always have had to endure on their way to the best long-term performance of any of the financial asset classes.

Advancing Markets

Minimum Rise %	Average Gain	Average # Days	Count	Frequency (in Years)	Last Start	Last End
20.0%	108.0%	924	26	3.5	3/9/2009	4/26/2019
17.5%	66.5%	573	38	2.4	12/24/2018	4/26/2019
15.0%	66.2%	557	44	2.1	12/24/2018	4/26/2019
12.5%	43.8%	331	71	1.3	12/24/2018	4/26/2019
10.0%	34.9%	247	105	0.9	12/24/2018	4/26/2019
7.5%	23.4%	147	154	0.6	12/24/2018	4/26/2019
5.0%	14.7%	73	298	0.3	12/24/2018	4/26/2019

Declining Markets

Minimum Decline %	Average Loss	Average # Days	Count	Frequency (in Years)	Last Start	Last End
-20.0%	-34.3%	371	25	3.6	1/6/2009	3/9/2009
-17.5%	-30.3%	222	37	2.4	9/20/2018	12/24/2018
-15.0%	-28.3%	192	43	2.1	9/20/2018	12/24/2018
-12.5%	-22.6%	140	70	1.3	9/20/2018	12/24/2018
-10.0%	-19.3%	102	104	0.9	9/20/2018	12/24/2018
-7.5%	-15.4%	65	153	0.6	9/20/2018	12/24/2018
-5.0%	-10.9%	37	297	0.4	12/3/2018	12/24/2018

From 02.20.28 through 4.26.19. Price return series. We defined a Declining Market as an instance when stocks dropped the specified percentage or more without a recovery of equal magnitude, and an Advancing Market as in instance when stocks appreciated the specified percentage or more without a decline of equal magnitude. SOURCE: Kovitz Investment Group using data from Bloomberg, Morningstar and Ibbotson Associates

LONG-TERM RETURNS

	Annualized Return	Standard Deviation
Value Stocks	13.2%	25.9%
Growth Stocks	9.5%	21.4%
Dividend Paying Stocks	10.5%	18.0%
Non-Dividend Paying Stocks	8.8%	29.5%
Long-Term Corporate Bonds	6.0%	7.5%
Long-Term Gov't Bonds	5.5%	8.5%
Intermediate Gov't Bonds	5.1%	4.3%
Treasury Bills	3.3%	0.9%
Inflation	2.9%	1.8%

From 06.30.27 through 03.31.19. Growth stocks = 50% Fama-French small growth and 50% Fama-French large growth returns rebalanced monthly. Value stocks = 50% Fama-French small value and 50% Fama-French large value returns rebalanced monthly. The portfolios are formed on Book Equity/Market Equity at the end of each June using NYSE breakpoints via Eugene F. Fama and Kenneth R. French. Dividend payers = 30% top of Fama-French dividend payers, 40% of middle Fama-French dividend payers, and 30% bottom of Fama-French dividend payers rebalanced monthly. Non-dividend payers = Fama-French stocks that do not pay a dividend. Long term corporate bonds represented by the Ibbotson Associates SBBI US LT Corp Total Return index. Long term government bonds represented by the Ibbotson Associates SBBI US LT Govt Total Return index. Intermediate term government bonds represented by the Ibbotson Associates SBBI US IT Govt Total Return index. Treasury bills represented by the Ibbotson Associates SBBI US 30 Day TBill Total Return index. Inflation represented by the Ibbotson Associates SBBI US Inflation index. SOURCE: Kovitz Investment Group using data from Professors Eugene F. Fama and Kenneth R. French and Ibbotson Associates

Not quite the Holy Grail, we know, but higher returns and lower risk is what most investors have long been seeking. And, when one also considers the longer-term time horizon that most folks should be working with, the odds of doing worse in the kind of undervalued, dividend-paying stocks that *The Prudent Speculator* has long championed than in a fixed income instrument like the 10-Year U.S. Treasury are very low. Indeed, history shows that in 93.8% of the decade-long periods dating back to 1927, dividend-payers have exceeded a 2.5% annualized rate of return!

THE PRUDENT SPECULATOR
The Longer the Hold, the Lower the Risk

While many view bonds as much less risky than equities, given that fixed income investments generally boast lower volatility, it is hard to fathom why anyone with a truly long-term time horizon would favor a 10-year U.S. Treasury today, with its 2.50% current yield, given the improving odds as holding periods lengthen that stocks will beat that return.

PATIENCE IS VIRTUOUS

VALUE STOCKS

	Count >2.5%	Count <=2.5%	Percent >2.5%
1 Month	679	422	61.7%
3 Months	725	374	66.0%
6 Months	749	347	68.3%
1 Year	778	312	71.4%
2 Year	865	213	80.2%
3 Year	906	160	85.0%
5 Year	903	139	86.7%
7 Year	951	67	93.4%
10 Year	941	41	95.8%
15 Year	913	9	99.0%
20 Year	862	0	100.0%

DIVIDEND PAYERS

	Count >2.5%	Count <=2.5%	Percent >2.5%
1 Month	674	427	61.2%
3 Months	718	381	65.3%
6 Months	757	339	69.1%
1 Year	784	306	71.9%
2 Year	876	202	81.3%
3 Year	870	196	81.6%
5 Year	898	144	86.2%
7 Year	929	89	91.3%
10 Year	921	61	93.8%
15 Year	894	28	97.0%
20 Year	862	0	100.0%

From 07.31.27 through 03.31.19. Value stocks represented by 50% small value and 50% large value returns rebalanced monthly. Dividend payers represented by 30% top of dividend payers, 40% of middle dividend payers, and 30% bottom of dividend payers rebalanced monthly. SOURCE: Kovitz Investment Group using data from Professors Eugene F. Fama and Kenneth R. French

To be sure, past performance is never a guarantee of future returns, but we have put together a diversified listing of 25 undervalued dividend payers, all of which, we think, offer capital appreciation potential in addition to a current yield of more than 3%.

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THE PRUDENT SPECULATOR
25 TPS Bargains Yielding at least 3%

Undervalued Higher-Yielding Prudent Speculator Newsletter Stocks

Symbol	Common Stock	Latest Price	Target Price	Sector	P/E	P/S	P/TBV	ROCE	EV/ EBITDA	FCF Yld	Debt/ TE (%)	Div Yld	Mkt Cap
ADM	Archer-Daniels-Midland	$40.91	$56.03	Food, Beverage & Tobacco	12.5	0.4	1.7	8.8	11.8	-17.7	57%	3.4%	22,916
AMGN	Amgen	$181.47	$226.56	Pharmaceuticals, Biotech	12.6	4.7	nmf	44.5	9.5	8.8	nmf	3.2%	111,776
AZSEY	Allianz SE	$23.82	$29.43	Insurance	11.9	nmf	1.9	11.8	nmf	nmf	nmf	2.9%	101,106
BASFY	BASF SE	$20.25	$28.88	Materials	12.4	1.1	3.6	13.7	9.3	6.1	83%	3.2%	74,397
CAH	Cardinal Health	$47.51	$79.94	Health Care Equip/Srvcs	9.5	0.1	nmf	-0.6	11.7	11.7	nmf	4.0%	14,159
CCL	Carnival Corp	$54.42	$80.47	Consumer Services	12.9	1.9	1.9	12.7	9.0	0.7	45%	3.7%	37,329
CMA	Comerica	$77.75	$107.00	Banks	10.0	nmf	1.8	16.7	nmf	nmf	nmf	3.4%	12,051
DLR	Digital Realty Trust	$116.79	$132.20	Real Estate	17.0	nmf	5.0	2.9	nmf	nmf	nmf	3.7%	25,548
DOC	Physicians Realty Trust	$18.32	$22.90	Real Estate	17.0	nmf	1.4	2.3	nmf	nmf	nmf	5.0%	3,342
ETN	Eaton Corp	$83.77	$95.12	Capital Goods	15.6	1.6	nmf	12.9	11.0	5.8	nmf	3.4%	35,537
GM	General Motors	$39.68	$56.21	Autos & Components	6.1	0.4	1.7	21.4	3.0	11.6	220%	3.8%	56,379
HSBC	HSBC Holdings	$43.07	$53.06	Banks	11.9	nmf	1.0	7.9	nmf	nmf	nmf	5.9%	174,309
IBM	IBM	$139.44	$185.22	Software & Services	10.2	1.6	nmf	49.9	8.9	9.7	nmf	4.5%	124,083
IP	International Paper	$45.99	$69.75	Materials	8.3	0.8	4.6	23.2	6.9	10.3	253%	4.3%	18,465
KMB	Kimberly-Clark	$125.74	$132.61	Home/Personal Products	19.2	2.4	nmf	nmf	14.4	4.0	nmf	3.3%	43,229
MDC	MDC Holdings	$30.34	$42.77	Consumer Durables	8.9	0.6	1.2	14.1	8.2	-1.9	70%	3.7%	1,861
PFE	Pfizer	$39.97	$48.25	Pharmaceuticals, Biotech	13.3	4.1	nmf	16.6	12.0	5.9	nmf	3.6%	221,906
PRU	Prudential Financial	$103.89	$135.94	Insurance	8.9	nmf	0.9	7.9	nmf	nmf	nmf	3.9%	42,422
SLB	Schlumberger Ltd	$43.30	$89.19	Energy	27.9	1.8	nmf	5.6	11.4	5.6	646%	4.6%	59,976
STX	Seagate Tech	$44.99	$56.99	Technology Hardware	7.3	1.1	nmf	nmf	6.4	11.1	789%	5.6%	12,563
TGT	Target	$77.12	$94.90	Retailing	14.3	0.5	3.8	25.6	7.6	6.1	115%	3.3%	39,820
TOT	Total SA	$55.17	$90.09	Energy	11.1	0.8	1.4	10.6	5.7	5.2	44%	4.3%	145,752
TPR	Tapestry Inc	$31.65	$56.11	Consumer Durables	11.8	1.5	nmf	22.7	8.1	9.9	609%	4.3%	9,178
VZ	Verizon Comm	$56.58	$67.00	Telecom Services	11.9	1.8	nmf	30.0	9.2	7.9	nmf	4.3%	234,015
WSM	Williams-Sonoma	$56.18	$84.22	Retailing	12.5	0.8	4.1	28.3	7.0	8.8	28%	3.4%	4,411

As of 4.26.19. nmf=Not meaningful. ROCE = Return on Common Equity. TBV = Tangible book value. EV/EBITDA = Enterprise value to earnings before interest, taxes, depreciation and amortization. FCF Yield = Free Cash Flow Yield

Stock Updates

Keeping in mind that all stocks are rated as “Buy” until such time as they are a “Sell,” while a listing of all current recommendations is available for download via the following link: https://theprudentspeculator.com/dashboard/, Chris Quigley and Jason Clark offer updates on 16 of our companies that had news last week that was of sufficient importance to trigger a review of their respective Target Prices.

Electronic components designer and manufacturer **AVX Corp.** (AVX – $16.53) posted earnings per share of $0.41, versus the $0.39 estimate, in fiscal Q4 2019. AVX had sales of $439.0 million (vs. $449.0 million est.). Shares plunged more than 10% following the announcement, a result of a soft management projection for Q1 2020 (June quarter), even as the second half of calendar 2019 is expected to be much stronger than the first.

Unfortunately, the second half’s expectation is heavily dependent on factors that are difficult for AVX to control. CEO John Sarvis said, “We do see slight slow and gradual improvement, starting at the latter part of the summer. And, also, I guess a lot of it also will depend upon what happens in the tariffs that, as you know, we’re still in discussion in relative to the United States and China about how we’re going to resolve that current issue. So, I think we’ll see something

— hopefully see some improvement there, which will also contribute improvements. So, that kind of leads us to believe that the second half will be quite a bit stronger."

Mr. Sarvis's told analysts, "Overall, orders were soft in comparison to previous quarters in FY '19, reflecting a continuous inventory build in the supply chain for commodity products, combined with the weak consumer market in China. Our core product delivery lead times remain extended on certain high-capacitance ceramics. However, we are experiencing continued lead time improvements on our standard ceramic and tantalum products. Sales in the June quarter will continue to reflect the increased inventory levels, resulting in a sales decline in a 2% range as compared to previous quarter. Our backlog has declined in light of market conditions, but remained strong and continues to support growth. The worldwide economy continues to be in turmoil after the peaking in early 2018. The global purchasing index consistently dropped through the year as we approach the crucial 50 point crossover margin. Major manufacturing regions like China did fall below 50 and into contraction."

Prices of high-end smartphone handsets and discontinuation of carrier subsidies have led to longer replacement cycles, but we expect smartphone sales to continue to grow over the longer term. Carriers have started rolling out 5G mobile networks in select cities, with growing availability expected to come online over the next few years. We like AVX's balance sheet (net cash of around $5 per share, though the company continues to make acquisitions) and 2.8% yield. Our Target Price has been reduced to $22.

Integrated telecom services firm **AT&T** (T – $30.68) posted earnings per share of $0.86, versus the $0.86 estimate, in fiscal Q1 2019. T had sales of $44.8 billion (vs. $45.1 billion est.). Shares slipped 4% following the announcement. The company has been losing DirectTV subscribers and has sold stakes in Hulu and Hudson Yards (real estate) to generate cash and pay down some debt.

CEO Randall Stephenson updated investors on the 5G buildout, "Over the last few months, AT&T has been recognized as both the best, as well as the fastest wireless network, and FirstNet has enabled us to accelerate our 5G and fiber build out. Our 5G service is now in parts of 19 cities, and we will have 5G coverage nationwide next year. We're the only carrier to offer 5G service to businesses and consumers, and we're well ahead of our competition here. And our AT&T fiber network now surpasses 20 million locations, that's both consumers and businesses. And in short, our network investments are paying off and we're not done yet."

CFO John Stephens said, "WarnerMedia continues to be accretive. Mobility is adding customers, and we saw EBITDA growth in our Entertainment Group. Offsetting these positive signs was about $400 million of non-cash impact from the reversal of revenue recognition and fulfillment deferrals. We expect those headwinds to continue throughout the year, and we've included all those in our guidance." AT&T still expects EPS growth to be in the "low-single digits" for fiscal 2019.

T – Making Progress: We Remain Patient

1Q Update:

2019 Initiatives

De-lever through strong free cash flow, non-core asset sales
$5.9B 1Q FCF, Hulu, Hudson Yards, working other opportunities

Grow wireless service revenues
Up 2.9% in 1Q, with continued postpaid and prepaid phone growth

Stabilize Entertainment Group EBITDA
Up 6.9% in 1Q, driven by broadband revenue

Deliver on merger plan, advance video strategy
1Q performance strong, WM organizing for future, SVOD beta in 4Q

Lead in network through FirstNet, 5G and fiber investments
Nation's fastest[1] and also the best[2] wireless network; 5G ramping

Expand targeted advertising, data analytics
Beginning to optimize Turner inventory

[1] Based on analysis by Ookla® of Speedtest Intelligence® data average download speeds for Q1 2019.
[2] Based on Global Wireless Solutions (GWS)® "Best Network OneScore" awarded to AT&T for overall national wireless network performance in 2018.

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We think that competition in streaming TV is unlikely to go away, with Hulu, Netflix and Amazon Prime excellent alternatives to expensive TV packages. Fortunately for AT&T, its wireless and internet service businesses have remained strong cash generators and we believe will keep that up for the foreseeable future. After all, cord-cutters need the internet to run their monthly paid streaming services. We are watching AT&T carefully to ensure the company isn't stuck holding a massive liability bag for content licenses it isn't able to monetize anymore, thereby putting its dividend payment ability in jeopardy. To us, AT&T is a better-than-utility-like exposure with a massive 6.6% yield and a single-digit (8.7) P/E ratio. Our Target Price is now $40.

Computing giant **Microsoft** (MSFT – $129.89) earned $1.14 per share in fiscal Q3 2019 (vs. $1.00 est.). MSFT had sales of $30.6 billion (vs. $29.9 billion est.). Shares traded higher by 3.3% following the announcement, briefly pushing the company above the $1 trillion in market capitalization mark, joining **Apple** (AAPL – $204.30) and Amazon in the club (though all three have fallen back below the mark).

Microsoft CEO Satya Nadella said, "It was another strong quarter with double-digit top-line and bottom-line growth, the result of picking the right secular trends, accelerating innovation and most importantly, relentlessly focusing on our customers' success. Our trusted extensible cloud platforms, spanning application infrastructure, data and AI, productivity and collaboration, as

well as business applications enables every organization to create their own intelligence systems and experiences to compete and grow."

Mr. Nadella continued, "I'm energized by our progress and incredibly optimistic about our opportunity ahead. Across all of our businesses, we are delivering differentiated value for customers and creating new categories of growth that position us well for the future."

CFO Amy Hood added, "I'd like to provide some closing thoughts as we look forward to FY '20. Overall, we feel very good about the progress we've made thus far in FY '19. Our decision to invest with significant ambition in high growth areas coupled with strong execution has resulted in material revenue growth at scale and a stronger position in many key markets. As FY '20 approaches, we again see tremendous opportunity to drive sustained long-term growth. We will invest aggressively in strategic areas like cloud through AI and GitHub, business applications, Power Platform and LinkedIn, Microsoft 365 through Teams, Security and Surface, as well as Gaming. At the same time, we will continue to drive improvement and efficiency as our business scales. This consistent approach of investing in future growth while delivering strong operating performance will result in double-digit revenue and operating income growth in FY '20 with stable operating margin."

MSFT returned $7.4 billion to shareholders via dividends and share repurchases in Q3. While shares were up just 2.8% in January, they've taken off since, surging more than 25% YTD on top of a terrific 20.8% return in 2018. We believe there are still a host of reasons to think that the music at the Cloud party is unlikely to stop in the foreseeable future, and we remain complimentary of Mr. Nadella's transformation of MSFT. He has revamped the company top to bottom during his tenure, taking it from an Office- and Windows-centric firm to a software firm with significant recurring subscription revenue, a strong Cloud product and complementary products like LinkedIn. In addition, we think MSFT's valuation is still not excessive, as the stock sports a 3.4% free cash flow yield and a 1.4% dividend yield. Analysts expect the company's EPS growth rate to be at least 11% for each of the next three fiscal years, with earnings growing from $3.88 in 2018 to an estimated $5.89 in fiscal 2021. Our Target Price for MSFT has been boosted again, this time to $136.

Semiconductor equipment firm **Lam Research** (LRCX – $206.39) posted earnings per share of $3.70, versus the $3.38 estimate, in fiscal Q3 2019. LRCX had revenue of $2.4 billion, matching the consensus estimate. Since the release, shares have climbed more than 5%, continuing the spectacular 2019 bounce.

CEO Tim Archer commented, "Lam delivered a solid March quarter and continued to demonstrate strong execution in a challenging near-term industry environment. Key metrics including revenue, gross margin, and operating income margin all came in above the midpoint of guidance that we gave on our last earnings call. EPS of $3.70 exceeded the high-end of our range, helped by a favorable tax rate and the benefit of ongoing share repurchases. This performance and continued execution in the business is attributable to the support of our customers and partners and as always the exceptional efforts of Lam employees around the world."

Mr. Archer offered his take on the state of the industry, “Industry conditions are directionally unchanged from our January call. We continue to expect customer WFE spending for calendar year 2019, to be in the low $40 billions. Though since our last call we now see a marginal downtick in memory spending, offset by slightly better expectation in foundry and logic. we expect memory supply growth as we exit 2019, to be below the long-term demand trend line for both NAND and DRAM In DRAM, we continue to believe the spending correction will extend through this calendar year, as customers continue to rationalize long-term profitability with near-term focus on reducing channel inventories and bringing supply and demand dynamics into balance for our business. In NAND, recent industry data indicates that bit shipments were better than normal seasonal trend for the February month and we continue to believe this market condition setting up well for future recovery as demand and supply balance improve through the year. On the foundry and logic side 2019. WFE spending it’s slightly higher than our prior baseline as customers appear to be ramping leading-edge nodes faster than we previously forecast, which we believe is partly due to increased semiconductor content in smartphones related to 5G While predicting the exact timing of cyclical change is always difficult. Our confidence in the long-term demand drivers for Lam’s business is unchanged.”

LRCX expects revenue for fiscal Q4 2019 to come in between $2.2 billion and $2.5 billion. Adjusted EPS is expected to be $3.40 per share, plus or minus $0.20, with a gross margin around 45%.

A strong IT environment has caused demand for Lam’s gear to swell, with sales rising from $4.0 billion in 2013 to $9.6 billion in 2017, while analysts project more than $11 billion in calendar 2021. We like the strong balance sheet with north of $8 per share in net cash, while consensus analyst adjusted EPS forecasts for fiscal 2019, 2020 and 2021 now stand at $14.35, $14.82 and $17.85, respectively. Management repurchased $862 million worth of shares in the quarter, as part of the $5 billion share repurchase program that was announced in January. LRCX trades for less than 15 times projected earnings and has a dividend yield of 2.1%. Our Target Price has been hiked to $231.

Semiconductor giant **Intel** (INTC – $52.43) reported earnings per share of $0.89, versus the $0.87 estimate, in fiscal Q1 2019. INTC had sales of $16.1 billion (vs. $16.0 billion est.). Shares tumbled 9% following the announcement, weakened by Intel’s slashed forecast and the potentially troubling observation that “customers are becoming more cautious in their buying patterns.”

Interim CEO and CFO Bob Swan commented, “Our conversations with customers and partners across our PC and data-centric businesses over the past couple of months have made several trends clear. The decline in memory pricing has intensified. The data center inventory and capacity digestion that we described in January is more pronounced than we expected, and China headwinds have increased, leading to a more cautious IT spending environment. And yet those same customer conversations reinforce our confidence that demand will improve in the second half. So, we’ve reassessed our ’19 expectations based on the challenges we’re seeing.”

Mr. Swan concluded, “Our full year outlook is now $69 billion in revenue, down 3% year-over-year and down approximately $2.5 billion from our previous estimate. Given the magnitude of

change, we'll be somewhat more granular in explaining the drivers. We now see data-centric revenue down low single digits year-over-year, with DCG down mid-single digits. year-over-year off a tough compare, continued China weakness and inventory and capacity absorption. We are also anticipating an incrementally more challenging NAND pricing environment. We now forecast full year EPS at $4.35 per share, down approximately 5% year-over-year and $0.25 from our previous guide."

While the stock price is still up more than 11% this year, it has been a bumpy ride for shareholders. Shares have dropped at least 5% on both Q4 results (January 24) and Q1 results (April 25), while the news the week prior that Intel would exit the 5G chip business sent the shares up 5%. Intel has grown significantly in recent years and has encountered two major challenges that are likely to determine the course for the foreseeable future. The first is the quantity of Intel chips used around the world–it's difficult to grow at a decent clip when the company's market share is large in many areas and the need for Intel's chips isn't growing fast. The second is the miniaturization of new products. That is, how can Intel keep making chips smaller while maintaining the reliability and speed its products are known for? The 10-nanometer node is about 20 silicon atoms wide, or 1 millionth of a millimeter. The limits of physics kick in at some point and govern what can and can't be created.

As has been the case in the past, we think that Intel will successfully navigate the challenges. It might not be a quick-and-easy path to success, but the company's strong balance sheet and deep bench of talent should help move things along. We continue to like the company's diversified revenue stream, low levels of debt, forward P/E ratio below 12 and 2.4% dividend yield. Our Target Price is now $64.

Data center REIT **Digital Realty Trust** (DLR – $116.79) had FFO (funds from operations) of $1.92 per share in fiscal Q1 2019 (vs. $1.63 est.). DLR had revenue of $815.0 million (vs. $799.0 million est.). Shares fell 3% following the announcement, as guidance was unchanged despite the favorable Q1. DLR expects FFO per share between $6.60 and $6.70 for 2019 and revenue of $3.2 billion to $3.3 billion. Capex is expected to be between $1.2 billion and $1.4 billion.

"Global economic expansion remains intact. The U.S. unemployment claims recently dipped below 200,000. Central banks the world over have adopted a dovish stance and the risk of a full-blown trade war appears to be receding. As you've heard me say many times before, we are fortunate to be operating in a business levered to secular demand drivers, both growing faster than global GDP growth and somewhat insulated from economic volatility. The hyperscale data center customers who drove outsized demand in 2018 marched to the beat of their own drum. Although they have largely remained in digestion mode in the early days of 2019, we remain highly confident in the longer-term trajectory of this demand. In addition, the resiliency of our business model enables us to capture robust and diverse demand from a broad swath of customer verticals across geographic regions around the world," commented Chief Executive Officer A. William Stein.

"We signed total bookings of $50 million, including $9 million from Ascenty, a $7 million contribution from interconnection. We signed new leases for space and power totaling $42

million with a weighted average lease term of 10 years, including a $7 million colocation contribution. 5 of our top 10 deals in the first quarter were outside the U.S., including several top customers who were able to leverage our global platform to enable their growth across regions," added Chief Financial Officer Andrew P. Power. "Within our global account segment, we landed 2 sizable deployments north and south of the border with a leading global cloud service provider. Separately, we also landed a network edge node from another leading global cloud service provider, which we expect will enhance the interconnection profile of our campus in Dallas, Texas. We continue to track healthy demand within our global account segment, but the cloud accounted for just 1/3 of our first quarter bookings."

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THE PRUDENT SPECULATOR
DLR – Strong Cloud Potential

We think that the buildout of cloud infrastructure around the world creates growing demand for DLR's offerings as major technology companies like Microsoft work to deploy their cloud-based applications and services. With its 210+ data centers in 35+ global metro markets, DLR has enhanced metro area exposure, additional hyper-scale product offerings, cost synergies and external growth potential via a strong development pipeline. We like that the company has a broad customer base (more than 2,300 clients), solid FFO growth potential and a just-improved 3.7% dividend yield. Our Target Price has been nudged up to $132.

Electronic manufacturing services firm **Benchmark Electronics** (BHE – $27.38) earned $0.33 per share in Q1 (vs. $0.33 est.). BHE had revenue of $602 million, versus the $640 million

estimate. Shares fell more than 10% on the news, as the company's revenue dropped both quarter-over-quarter and year-over-year, while guidance for the current quarter was disappointing.

CEO Jeff Benck, who is new to the post, said, "We are dealing with the near-term challenges head-on. We have aligned capacity to current demand and are evaluating further cost actions given the delayed recovery of this segment. For the long-term, we remain positive on semi-cap and we continue to win new programs. We have differentiated capabilities to serve the customers in this market. Beyond semi-cap, we are pursuing global operational efficiency savings across the network to expand our gross margins. We have kicked off a number of projects to further improve productivity and transformation margins, which we will look to accelerate in the coming months. We are evaluating our technology investments across Benchmark to prioritize those that provide the greatest benefit to our customers balance with those that offer the greatest potential for return."

CFO Roop Lakkaraju said for Q2 2019, "We expect revenue to range from $555 million to $585 million as a result of growth in A&D and Medical sectors offset by continued semi-cap softness. Our adjusted diluted earnings per share is expected to be in the range of $0.28 to $0.36. Overall, we expect Industrials revenue to be flat due to a delayed program ramp at one customer and is expected to be up high-single digits in Q2 based on continued program ramps from Q1. We expect Medical revenues to be up mid-single digits driven from growth an existing customers. In Test & Instrumentation, we expect to further decline a mid-double digits from further softening in semi-cap. Turning now to the traditional markets. We expect computing revenues to be down low-double digits. We expect Telco to be down greater than 20% due to softer demand from one customer and ramp delays because of design stability with another customer."

We like that Benchmark continues to use the stock price weakness to buy back chunks of shares ($61 million spent in Q1). Despite the headwinds, we are optimistic that the new CEO will make positive changes, like that Benchmark continues to expand its product offerings and appreciate that it has been pushing for growth outside of its original markets. Shares trade with a forward P/E ratio of 17 (still more than reasonable for an IT name) and we remain very enthused about the balance sheet, which boasts about $7 per share of net cash. The yield is 2.2%. Our Target Price now stands at $31.

Manufacturer of transportation, construction and industrial products **Trinity Industries** (TRN – $21.50) reported earnings per share of $0.24, versus the $0.21 estimate, in fiscal Q1 2019. TRN had total revenue of $605.0 million, versus the $673.0 million estimate. Shares slid 12% following the announcement.

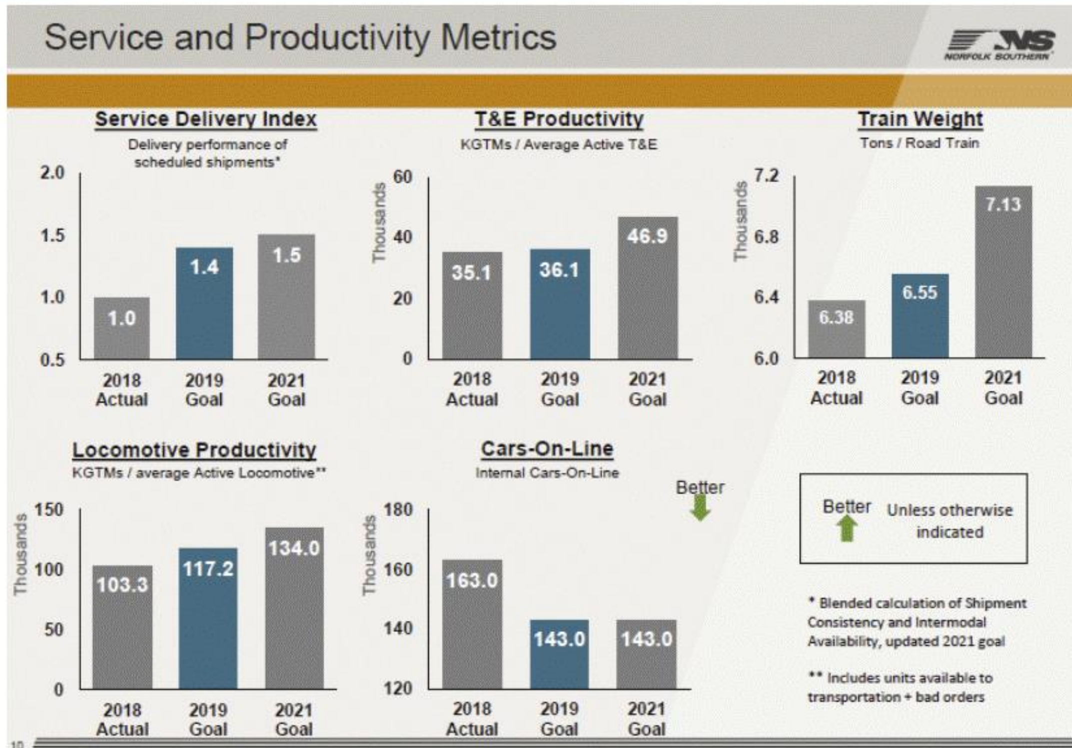
TRN CEO Tim Wallace commented, "We expect 2019 to be a strong year for us in respect to earnings growth. We remain on track to increase our earnings in excess of 60% year-over-year for 2019. Our vision for Trinityrail is to be a premier provider of railcar products and services in North America, while generating high-quality earnings and returns for shareholders. Today, we have an impressive platform that provides a host of offerings to our customers across the railcar equipment ecosphere. we've remain highly focused on deploying our capital, with the expectations of providing value to our shareholders through high returns on our investments. In

particular, we're looking for opportunities to develop additional sources of recurring revenues within the railcar ecosphere that provide predictable levels of earnings, cash flow and stable returns. Six months ago, we completed our spin-off of **Arcosa** (ACA – $30.86), so we could focus on our integrated platform of railcar products and services. We have established a strong, good leadership team and a highly motivated organization that is dedicated to driving value to our customers and our shareholders. At the beginning of my remarks, I mentioned how well our organization is performing and the high degree of confidence I have in our company. In my experience when we set our minds on accomplishing something, we deliver. I look forward to sharing progress with you as we continue on our journey."

TRN repurchased $89 million worth of shares in the quarter, $70 million of which marks the completion of the company's first $350 million share repurchase authorization and $19 million comes out of the newer $350 million authorization that expires in December 2020. TRN reiterated EPS guidance from November, which was for $1.15 to $1.35 per share in EPS for fiscal 2019. Though our grip on our shares has loosened somewhat, we are still willing to hold TRN and we also are still evaluating the small position in ACA, which is scheduled to release Q1 results on May 2. Our Target Price for TRN now resides at $29.

East coast railroad transportation company **Norfolk Southern** (NSC – $204.14) continued its torrid appreciation since the Christmas Eve Bear Market lows, the latest leg higher following a strong Q1 earnings report. For the first three months of 2019, NSC posted adjusted earnings per share of $2.51, versus consensus analyst estimates of $2.18. NSC also turned in total revenue of $2.84 billion, versus investor expectations of $2.82 billion. Norfolk said that it achieved record first-quarter railway operating revenue, operating income, operating ratio, net income and earnings per share.

"Our first-quarter results reflect the initial steps in the implementation of our new strategic plan that are transforming our company," proclaimed CEO James A. Squires. "We set company records for many financial measures in the first quarter, while improving our service product for our customers. We are intensely focused on the execution of the initiatives in our strategic plan that will drive shareholder value."



Despite potential headwinds to volume growth, mainly because of domestic coal, as well as weaker export pricing, we think that Norfolk is still solidly positioned to expand margins and improve its operating ratio given strides in labor productivity, asset utilization, strong intermodal volumes, pricing power and overall improved operational fluidity. While we have an ongoing internal debate about whether we should trim our current position, the operational improvements and overall business strength compel us to continue to hold all our shares for the time being for an increased Target Price of $213.

Despite strong energy prices thus far in 2019, **Exxon Mobil** (XOM – $80.49) saw its shares drop last week after the world's largest integrated oil and gas company turned in a weaker Q1 than investors were expecting. Exxon reported adjusted EPS of $0.55, which was more than 20% below consensus estimates. Revenue for the period of $63.6 billion also came in below forecasts by more than 2%. Weakness versus other peers reflected larger downstream and chemicals exposure, with the former hurt by an approximate $25 rally in oil prices and a still elevated level of maintenance.

"Solid operating performance in the first quarter helped mitigate the impact of challenging Downstream and Chemical margin environments. In addition, we continued to benefit from our integrated business model," explained CEO Darren W. Woods. "We are making strong progress on our growth plans and expect to deliver sustained value for our shareholders. The change in

Canadian crude differentials, as well as heavy scheduled maintenance, similar to the fourth quarter of 2018, affected our quarterly results."

Obviously, we do not like to see disappointing quarterly results, but we do not think anything is broken at Exxon and we believe the Q1 setbacks are short-term in nature. We continue to like that XOM is the only energy player with a Aaa credit rating (issued by Moody's) and its fortress balance sheet and capital discipline give it the financial and operational flexibility we desire. XOM yields a rich 4.3%, as the dividend was just boosted again, while our Target Price has been adjusted to $102.

Despite year-over-year Q1 volume weakness, **Goodyear Tire** (GT – $19.24) turned in bottom-line results that came in ahead of analyst expectations. For the quarter, GT posted adjusted EPS of $0.19, compared to estimates of $0.06, on revenue of $3.6 billion, which fell a bit short of the $3.7 billion forecast.

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THE PRUDENT SPECULATOR
GT – Mixed Bag in Q1

Reflecting on Q1 2019 Results

GOODYEAR

Positives

- Global revenue per tire increased 4%
- U.S. consumer replacement volume growth of 6%, led by outperformance in ≥17"
- Improving U.S. supply
- U.S. and EMEA commercial truck businesses
- Announced plans to restructure/modernize two manufacturing facilities in Germany
- Expanding portfolio of mobility and technology partners

Negatives

- Higher raw material costs (including costs driven by stricter enforcement of environmental regulations in China)
- Volatility in emerging markets, including China and Brazil
- Currency weakness in key markets
- Soft consumer demand in Europe

Making progress in a challenging environment

"We gained momentum in the U.S. during the quarter, as our consumer and commercial replacement businesses both grew share, while increasing the value we capture in the marketplace," said CEO Richard J. Kramer. "In addition, we took steps to increase our long-term competitiveness. The plans we announced to modernize our Hanau and Fulda manufacturing

facilities in Germany will improve our supply of cost-effective premium tires in Europe, helping us achieve our goal of having the right tire, at the right place, at the right time, at the right cost."

Despite the challenges and our growing impatience with the lack of consistent execution by GT, we still believe that the company can deliver long-term returns for investors. We think that continued strong employment, rising wages and solid consumer sentiment are conducive to keeping demand solid, as well as folks traveling more and thereby creating more wear and tear on tires (spurring replacements). We think that Goodyear also should gain from higher long-term demand in emerging markets. We are also optimistic that GT can keep expenses in check, improve cash flow and strengthen the balance sheet. Our Target Price for GT, which trades for 8.7 times NTM adjusted EPS expectations and yields 3.3%, remains $32.

Shares of **International Paper** (IP – $45.99) gained ground last week after the paper product company reported Q1 financial results. Despite weaker-than-expected revenue, IP surpassed bottom-line consensus expectations by 18%. For the quarter, IP reported adjusted EPS of $1.11, versus investor forecasts of $0.91, while revenue came in at $5.64 billion (versus est. of $5.73 billion). Containerboard exports were weaker than expected during the quarter (both volume and price) as customers destocked. Adjusted EBIT margin expanded by almost 80 basis points, largely due to strong earnings growth in printing papers and global cellulose fibers. While many expect customer destocking to continue to be a headwind in Q2, we believe that volumes will improve during the second half of this year.

CEO Mark Sutton commented, "International Paper delivered solid earnings and generated strong cash from operations in the first quarter. Operational performance was strong; we managed costs well and leveraged the strength and flexibility of our manufacturing system. In the first quarter, we also returned nearly $400 million to shareholders through dividends and share repurchases. Looking ahead to the second quarter, we anticipate improved seasonal demand and we are well positioned to continue generating strong cash flows in 2019."

We like that the company continues to pursue growth abroad, most recently with its acquisition of Envases Grau, a Spanish wood and corrugated board packaging manufacturer. In addition to solid free cash flow and EPS estimates in the $5.00 range for the next couple of years, IP should benefit from a lower tax rate, its emerging market exposure and the continued rapid growth rates of e-commerce (which requires an increasing amount of shipping boxes and packages). While competition will remain stiff, the packaging markets are seemingly changing quite rapidly, with dominant players like IP able to push the envelope within key success factors, making it tougher for new players to challenge. Also, IP currently trades for just 9 times NTM earnings projections and sports a dividend yield of 4.3%. Our Target Price for IP has been bumped up to $70.

Shares of **Kimberly-Clark** (KMB – $125.74) rose last week after the consumer products giant delivered solid Q1 results. KMB said its adjusted Q1 EPS came in at $1.66, outpacing the consensus analyst estimate of $1.54. Revenue of $4.63 billion exceeded forecasts by 2%.

CEO Mike Hsu said, "I'm encouraged with our first quarter results. We made excellent progress driving higher selling prices to help offset commodity and currency headwinds. We also continued to launch innovations, pursue our growth priorities and invest in our brands. In

addition, we generated $115 million of cost savings and returned $510 million to shareholders through dividends and share repurchases. We are confirming our previous full-year outlook while we maintain a strong focus on executing K-C Strategy 2022 for long-term success." KMB targets full-year 2019 organic sales growth of 2% and adjusted earnings per share of $6.50 to $6.70.

It's worth reminding readers that in January 2018, KMB initiated the 2018 Global Restructuring Program in order to reduce the company's structural cost base and enhance flexibility to invest in its brands, growth initiatives and capabilities critical to delivering future growth. Management expects the program to generate annual pre-tax cost savings of $500 million to $550 million by the end of 2021, driven by workforce reductions along with manufacturing supply chain efficiencies. As part of the program, KMB expects to exit or divest some low-margin businesses that generate approximately 1% of company net sales. The sales are concentrated in the consumer tissue business segment. Q1 restructuring charges were $152 million pre-tax ($122 million after tax), bringing cumulative charges to $1,188 million pre-tax ($905 million after tax). First quarter 2019 restructuring savings were $60 million, bringing cumulative savings to $195 million.

We were pleased to see KMB turn in a solid quarter and continue to like that the company has leading market share positions in some of the larger household product categories and that its focus on increasing its emerging market businesses should continue to be an important long-term growth driver. We also think that KMB should be able to realize future pricing and margin improvements via product innovation and marketing. Long-term sales growth should be aided by expansion in non-traditional categories and deeper penetration into emerging economies to capitalize on rising incomes and birth rates. KMB generates solid free cash flow, which supports share repurchases and a 3.3% dividend yield. Our Target Price has been raised to $133.

Specialty chemicals manufacturer **Celanese** (CE – $108.56) saw its shares rise more than 3% last week after reporting Q1 financial results. CE announced adjusted EPS of $2.62, versus consensus estimates of $2.40. Revenue for the period was $1.69 billion, which fell short of expectations ($1.75 billion).

CEO Mark Rohr explained, "Challenging global business conditions persisted into the new year, and our strong first quarter performance solidly underscores the capability of our businesses to deliver in any environment. Engineered Materials executed the project pipeline model to deliver earnings growth, both sequential and year over year, that was distinctly elevated beyond underlying market conditions. In the Acetyl Chain, another quarter of fundamentally strong earnings displayed the power to create incremental value by flexing our global network. Looking forward, we are not forecasting a significant improvement in demand in the current quarter, and therefore expect second quarter performance similar to the first quarter. Based on an expectation that underlying fundamentals will begin to improve later this year, we have confidence in reaffirming our expectation for 2019 adjusted earnings of approximately $10.50 per share. We continue to strategically invest in our businesses and further expand our capability to drive consistent growth and value creation for our shareholders."

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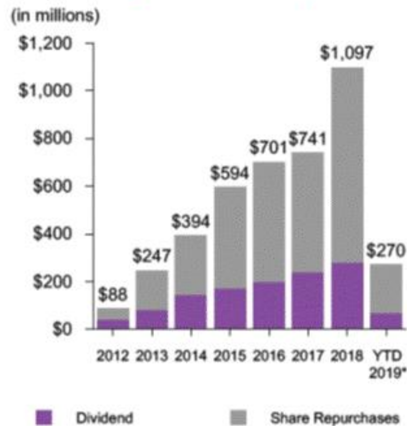
THE PRUDENT SPECULATOR
CE – Remaining Shareholder Friendly

Returning Cash to Shareholders

Dividend Payout and Share Repurchases

(in millions)



Dividend   Share Repurchases

Share Repurchases

- Deployed $200 million in Q1 2019 to repurchase ~2 million shares
- ~$500 million remaining share repurchase authorization as of March 31, 2019

Dividend

- Returned $70 million to shareholders in dividends in Q1 2019

$4.1 billion returned to shareholders since 2012 via dividends and share repurchases

*YTD Year-to-date as of March 31, 2019

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Despite some near-term operational headwinds, we continue to like Celanese and believe it can move higher still via geographic expansion and new application development. CE enjoys a cost advantage in many of its markets and we see the Advanced Engineered Materials business having attractive long-term growth potential. We also like CE's free cash flow generation which allows it to continue to strengthen its financial base, while returning capital to shareholders. CE trades for 10 times forward earnings per share and yields 2.3%. Our Target Price for CE has jumped to $153.

Shares of **Capital One Financial** (COF – $93.73) leapt more than 6% last week as the credit card behemoth posted its Q1 financials. COF reported top- and bottom-line results that were both better than consensus analyst estimates. Adjusted EPS for the period came in at $2.90, versus an expected $2.71, with the result representing sequential growth of 15% and year-over-year growth of 9%. The growth in EPS came despite a 25% boost in marketing spend. Revenue for the quarter was $7.08 billion, while forecasts were looking for $7.03 billion.

CEO Richard D. Fairbank commented, "In the first quarter, revenue, pre-provision earnings, and earnings per share all increased compared to the first quarter of 2018. As our digital transformation accelerates, we are well positioned to succeed in a rapidly changing marketplace and create long-term shareholder value."

We were pleased to see a bounce-back quarter following a disappointing Q4. We will keep an eye on the continued boost in marketing spend as we obviously want to see that result in loan growth. While COF shares have had a nice run thus far in 2019, we continue to remain long-term focused and we think there is still plenty of upside as the company focuses on managing risks, while improving efficiency, even as it invests to grow and transform itself as banking goes digital. COF trades for 8.3 times estimated earnings and offers a 1.7% dividend yield. Our Target Price has been raised to $124.

Construction equipment giant **Caterpillar** (CAT – $139.03) reported Q1 results last week that outpaced consensus analyst estimates on both the top and bottom lines. That said, shares fell more than 3% over the five trading days. CAT reported adjusted EPS of $2.94 on revenue of $13.47 billion. While it would seem by the share decline that some investors were disappointed, we thought the quarter demonstrated the company's ability to continue to bring forward innovative products and streamline operations. Most notable during the quarter was the performance of its resource industries segment, which increased revenue 18.1% year over year and expanded its operating margin to 21.1% from 16.4%.

Demand from miners was solid in the quarter, with the segment's deliveries in the Asia-Pacific region strong. This contrasted with CAT's construction industries performance in China, which had flat sales despite a strong market for construction equipment. Data from the China Construction Machinery Association (CCMA) indicated that excavator sales in China were up 24% year over year in Q1. On the company's Q1 earnings call, management said that it lost market share in this segment as competitors aggressively priced their products.

THE PRUDENT SPECULATOR
CAT – Record Q1

2019 Financial Results

First Quarter 2019 vs. First Quarter 2018

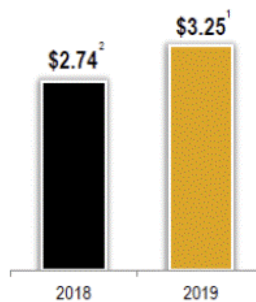
Sales and Revenues
(in billions of dollars)
$13.5

$12.9 | $13.5

2018 | 2019

Profit Per Share
(in dollars)
$3.25[1]

$2.74[2] | $3.25[1]



2018 | 2019

1st Quarter Highlights

Sales and Revenues up 5%
- Increase primarily in Resource Industries and Construction Industries
- Energy & Transportation about flat

Profit

- Record 1Q profit per share

Financial Position
- $1.2B in buybacks and dividends
- $7.1B enterprise cash on hand

[1] Profit Per Share for 2019 includes a discrete tax benefit of $0.31 per share related to U.S. tax reform.
[2] Profit Per Share for 2018 includes restructuring costs of $0.08 per share.

OUR SOLUTIONS HELP OUR CUSTOMERS BUILD A BETTER WORLD.

“The global Caterpillar team delivered record first-quarter profit per share,” said CAT CEO Jim Umpleby. “We are executing our strategy for profitable growth by investing in services, expanding our offerings and improving operational excellence.” The company continues to have confidence in the fundamentals of its diverse end markets, and expectations for 2019 performance are unchanged. However, due to a $0.31 per share discrete tax benefit, Caterpillar is revising its profit per share outlook to a range of $12.06 to $13.06, compared with the previous outlook range of $11.75 to $12.75.

While there are things to be concerned about, such as volatile input costs, the trade battle with China and a slowdown in Europe, we think the potential for increased global infrastructure spend (including rumors out of Washington) and the company’s continuing emphasis on growing leaner bode well for its already-solid free cash flow (FCF) generation. With almost $7.1 billion in cash and billions more in FCF expected over the next few years, we see CAT being able to better withstand changing business environments and becoming more aggressive in buying back shares and boosting the dividend (current yield is 2.5%). CAT trades at just 11.2 times NTM adjusted EPS, and our Target Price has been adjusted upward to $183.