Market Commentary Monday, June 24, 2019

June 24, 2019

EXECUTIVE SUMMARY

Week in Review – June Rebound Continues
BofA Fund Manager Survey – Pros Became Super Bearish During May
Perspective – 2011 the Last Time Wall Street was as Pessimistic as Today
Main Street – Sentiment Still Not Optimistic
Bond Market Love Affair – Fund Investors Continue to Move Money from Equities to Fixed Income
Smart Money? – $13 Trillion in Negative Yielding Debt
Fed Projections – 2% GDP Growth Likely This Year and in 2020
FOMC Meeting – No Rate Cut Yet; Several Appear Likely Soon
Falling Interest Rates – A Reason to be Enthusiastic About Stocks
Valuations – We Like the Metrics on our Portfolios
Stock Updates – CCL, KR, ORCL & JBL

Market Review

Even with the drama on the foreign stage temporarily shifting to the Persian Gulf and concern about a conflict between the U.S. and Iran, the June bounce in the domestic equity markets carried further last week, with *The Wall Street Journal* stating on Saturday, "The S&P 500 has advanced 7.2% despite lingering trade tensions and uncertainty over the future of Federal Reserve policy."

The *Journal* went on to say that the S&P is heading toward its best June since 1955, with the big rebound seemingly coming as a major surprise to folks on both Wall Street and Main Street. Indeed, Bank of America Merrill Lynch released its June Global Fund Manager Survey early last week, with the tally showing that investment professionals generally bailed on stocks and piled into cash AFTER and not BEFORE the big selloff in May.

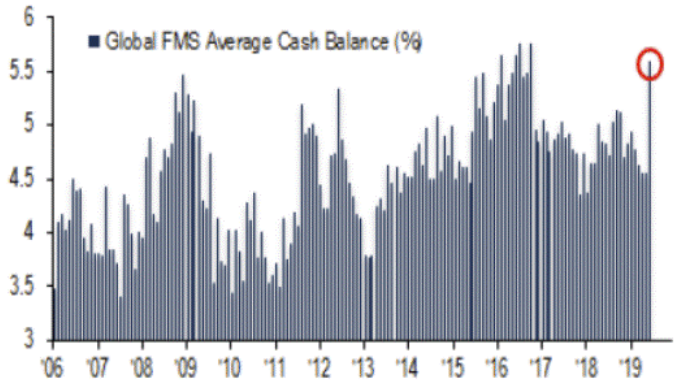
Investment Pros Have Been Uber-Bearish

The BofAML June Global Fund Manager Survey – June 7 through June 13, 2019

June FMS most bearish survey of investor confidence since the Global Financial Crisis. FMS cash level soars to 5.6% from 4.6% (Exhibit 1), biggest jump in cash since 2011 US debt ceiling crisis.
Equity bears: 2nd largest drop in equity allocation ever (largest occurred Aug '11); and FMS relative allocation of equities over bonds drops to lowest since May '09.
Bearish rotation: FMS shows huge June rotation to bonds, cash, staples, utilities, and huge rotation away from equities, banks, Eurozone, tech.

Crowded trades: long US Treasuries becomes #1 "crowded trade"; US dollar "overvaluation" highest since 2002.
Trades for the contrarian bull: "long gold, short US$", "long stocks, short Treasuries", "long Eurozone, short EM", "long banks, short utils", "long energy, short discretionary".

Exhibit 1: Biggest MoM jump in FMS cash level since Aug'11



Source: BofA Merrill Lynch Global Fund Manager Survey

Incredibly, fund managers had the largest reduction in equity exposure since August 2011 and the biggest increase in their allocation to cash since that same year, another period that illustrated our oft-stated point that the only problem with market timing is getting the timing right.

Despite Adversity, Trend Has Been Higher

Some may find it amazing that U.S. stock prices have more than doubled (with even bigger gains if dividends are included) since 2011, a highly volatile year in which the European debt crisis was front and center and Standard & Poor's downgraded its rating on U.S. government debt.

What's more, the fund manager allocation to stocks versus the allocation to bonds is now at the lowest relative level since May 2009. No doubt, readers know how well stocks have done since that turbulent period, but we think it timely to reprise a slide that we utilized couple of years back, as there has hardly been an all-clear signal given for the equity markets since the end of the Financial Crisis ten years ago.

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THE PRUDENT SPECULATOR
Bad News Usually Tops the Headlines

Interesting to consider all of the disconcerting events that have occurred on the road to all time highs since the March 2009 major market low.

Source: The Irrelevant Investor, Michael Batnick, CFA

Stocks are higher than they were in 2017, and the S&P 500 has soared from a Financial Crisis closing low of 676.53 on 3.9.09 to 2950.46 as of 6.21.19, but the average Joe generally remains unenthused about equities,…

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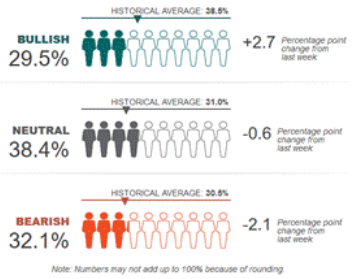
THE PRUDENT SPECULATOR
Still Not Much Main Street Optimism

AAII Investor Sentiment Survey

Since 1987, AAII members have been answering the same simple question each week. The results are compiled into the AAII Investor Sentiment Survey, which offers insight into the mood of individual investors.

Survey Results for Week Ending 6/19/2019
Data represents what direction members feel the stock market will be in next 6 months.



Note: Numbers may not add up to 100% because of rounding.

The AAII Investor Sentiment Survey has become a widely followed measure of the mood of individual investors. The weekly survey results are published in financial publications including Barron's and Bloomberg and are widely followed by market strategists, investment newsletter writers and other financial professionals.

June 19, 2019 - Optimism among individual investors about the short-term direction of stock prices continued to rebound but remains below 30% for the sixth consecutive week. The latest AAII Sentiment Survey also shows lower levels of neutral and bearish sentiment.

Bullish sentiment, expectations that stock prices will rise over the next six months, rose 2.7 percentage points to 29.5%. This is 18th time this year that optimism is below its historical average of 38.5%.

Bearish sentiment, expectations that stock prices will fall over the next six months, fell 2.1 percentage points to 32.1%. Pessimism is above its historical average of 30.5% for the sixth consecutive week.

With stocks on pace to post their best June since 1955, pessimism has lessened, but there are still more Bears than Bulls in the latest AAII Sentiment Survey, though flows into stocks in the most recent week were positive for a change via data compiled on mutual and exchange traded funds by ICI.

Combined Estimated Long-Term Fund Flows and ETF Net Issuance
Millions of dollars

Week Ended	6/12/2019	6/5/2019	5/29/2019	5/22/2019	5/15/2019
Total Equity	5,063	-9,680	-4,714	3,827	-11,397
Domestic	6,210	-8,191	-4,412	3,722	-9,569
World	-1,147	-1,489	-302	105	-1,828
Hybrid	-1,282	-1,017	-1,191	-736	-985
Total Bond	11,874	4,654	3,026	4,565	1,680
Taxable	10,603	3,224	1,402	2,486	-138
Municipal	1,271	1,430	1,624	2,078	1,819
Commodity	317	681	157	178	-708
Total	15,972	-5,362	-2,721	7,834	-11,409

Source: Investment Company Institute

…while the long-time love affair for all investors with fixed income shows no sign of abating.

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THE PRUDENT SPECULATOR
Bonds Remain Stunningly Popular

With the S&P 500 near an all-time high, many think folks are infatuated with U.S. equities, but data from the ICI show that a massive net sum of money has flowed out of domestic stock mutual funds/ETFs over the last 4+ years. Bonds have been the major beneficiary of the exodus.

Investment Company Institute

Long-Term Mutual Fund and Exchange-Traded Fund (ETF) Flows

Millions, U.S. dollars

Month	Stocks Domestic	Bonds Total	Month	Stocks Domestic	Bonds Total	Month	Stocks Domestic	Bonds Total	Month	Stocks Domestic	Bonds Total
Jan-15	-14,465	17,535	Mar-16	7,711	29,296	May-17	-10,816	33,128	Jul-18	984	25,956
Feb-15	5,547	30,321	Apr-16	-12,610	22,114	Jun-17	-8,022	29,420	Aug-18	-6,658	19,585
Mar-15	-1,494	4,905	May-16	-14,252	16,925	Jul-17	-12,386	29,164	Sep-18	880	18,102
Apr-15	-34,681	11,027	Jun-16	-15,530	16,623	Aug-17	-18,937	26,418	Oct-18	-12,009	-32,405
May-15	-17,287	5,010	Jul-16	292	33,575	Sep-17	-9,636	36,476	Nov-18	2,780	-11,250
Jun-15	-7,023	6,324	Aug-16	-9,956	30,859	Oct-17	3,211	38,818	Dec-18	-28,957	-49,413
Jul-15	-14,864	-1,255	Sep-16	-5,713	24,669	Nov-17	-4,429	21,628	Jan-19	-21,191	29,298
Aug-15	-18,569	-18,122	Oct-16	-23,109	13,855	Dec-17	-9,066	19,158	Feb-19	3,604	45,094
Sep-15	-4,725	-10,849	Nov-16	22,993	-13,289	Jan-18	10,777	56,779	Mar-19	-3,658	38,363
Oct-15	-807	15,397	Dec-16	18,859	-4,142	Feb-18	-41,447	1,772	Apr-19	-5,347	40,411
Nov-15	654	-5,573	Jan-17	4,966	31,061	Mar-18	-22,173	15,920	May-19	-20,421	16,863
Dec-15	476	-25,043	Feb-17	17,530	34,026	Apr-18	-7,422	22,435	**Totals:**	**-375,343**	**842,896**
Jan-16	-27,222	7,686	Mar-17	8,906	36,632	May-18	9,970	13,108			
Feb-16	-9,108	11,915	Apr-17	-8,370	22,116	Jun-18	-13,123	14,470			

In fact, the enthusiasm for bonds actually has gathered steam of late, with the yield on the bellwether German Bund again dipping well below zero,…

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THE PRUDENT SPECULATOR
Low Bond Yields Are Not Bad for Stocks

We remain perplexed why so many think that the "smart money" is in the bond market, especially when 10-Year Bund investors in Germany are actually willing to accept a negative return on their investment. Yes, some view super-low European bond yields as a global recession harbinger, but the S&P 500 is up some 40%, not counting dividends, since the last time the Bund yield went below zero in June 2016.

…and folks deciding that trillions of dollars are best parked in debt instruments that will produce a negative return, if held to maturity.

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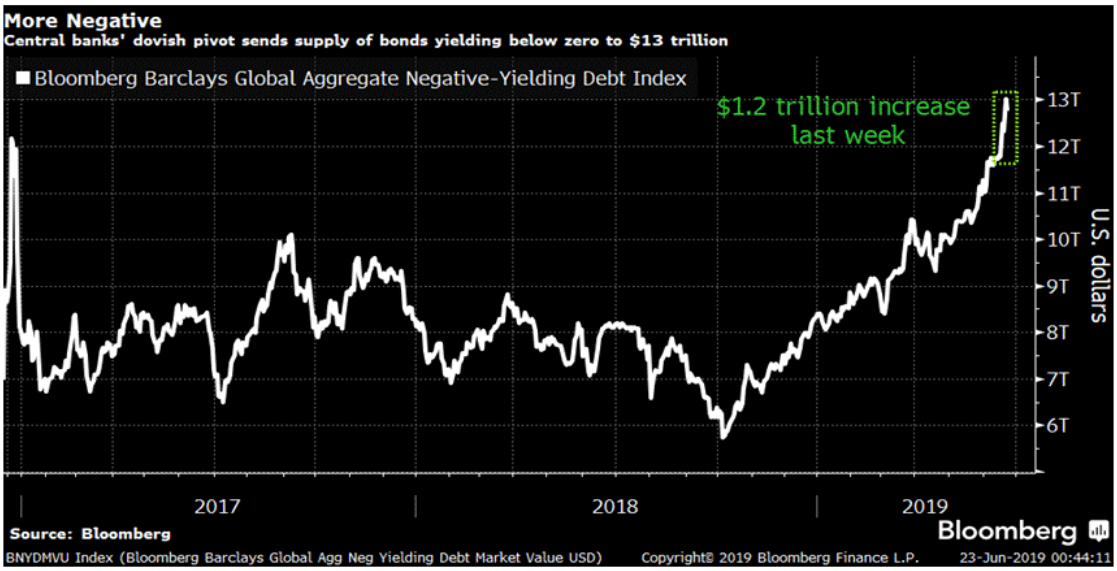
THE PRUDENT SPECULATOR
$13 Trillion in Negative Yielding Debt

Incredibly, money continues to pour into government bonds, with the latest surge pushing yields on another $1.2 trillion below zero. Stocks may be a risky asset class, but we struggle to see the value in accepting a return of less than zero if held to maturity on government debt.



Obviously, highly accommodative central bankers around the world have a lot to do with the renewed euphoria in the bond market, with the Federal Reserve last week adding to the view that interest rates will stay lower for longer. Jerome Powell & Co. did choose to leave the Fed Funds rate unchanged at 2.25% to 2.50% at the June FOMC Meeting, but the FOMC Statement read, "The Committee continues to view sustained expansion of economic activity, strong labor market conditions, and inflation near the Committee's symmetric 2 percent objective as the most likely outcomes, but uncertainties about this outlook have increased. In light of these uncertainties and muted inflation pressures, the Committee will closely monitor the implications of incoming information for the economic outlook and will act as appropriate to sustain the expansion, with a strong labor market and inflation near its symmetric 2 percent objective."

Of course, the FOMC Statement also sounded modestly upbeat regarding the economic outlook: "Information received since the Federal Open Market Committee met in May indicates that the labor market remains strong and that economic activity is rising at a moderate rate. Job gains have been solid, on average, in recent months, and the unemployment rate has remained low." And, the GDP growth projections remained the same for 2019, 2021 and the longer run, while the forecast for 2020 was bumped up by a tenth of a point,…

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No Recession & Lower Rates the Outlook

The Fed left its longer-run GDP growth projection at 1.9%, and did not change its forecast for 2019 growth (yes, growth!) of 2.1%. The long-run estimate for the Federal Funds rate was cut from 2.8% to 2.5%.

Economic projections of Federal Reserve Board members and Federal Reserve Bank presidents under their individual assessments of projected appropriate monetary policy, June 2019

Advance release of table 1 of the Summary of Economic Projections to be released with the FOMC minutes

Percent

Variable	Median[1]				Central tendency[2]				Range[3]			
	2019	2020	2021	Longer run	2019	2020	2021	Longer run	2019	2020	2021	Longer run
Change in real GDP	2.1	2.0	1.8	1.9	2.0 – 2.2	1.8 – 2.2	1.8 – 2.0	1.8 – 2.0	2.0 – 2.4	1.5 – 2.3	1.5 – 2.1	1.7 – 2.1
March projection	2.1	1.9	1.8	1.9	1.9 – 2.2	1.8 – 2.0	1.7 – 2.0	1.8 – 2.0	1.6 – 2.4	1.7 – 2.2	1.5 – 2.2	1.7 – 2.2
Unemployment rate	3.6	3.7	3.8	4.2	3.6 – 3.7	3.5 – 3.9	3.6 – 4.0	4.0 – 4.4	3.5 – 3.8	3.3 – 4.0	3.3 – 4.2	3.6 – 4.5
March projection	3.7	3.8	3.9	4.3	3.6 – 3.8	3.6 – 3.9	3.7 – 4.1	4.1 – 4.5	3.5 – 4.0	3.4 – 4.1	3.4 – 4.2	4.0 – 4.6
PCE inflation	1.5	1.9	2.0	2.0	1.5 – 1.6	1.9 – 2.0	2.0 – 2.1	2.0	1.4 – 1.7	1.8 – 2.1	1.9 – 2.2	2.0
March projection	1.8	2.0	2.0	2.0	1.8 – 1.9	2.0 – 2.1	2.0 – 2.1	2.0	1.6 – 2.1	1.9 – 2.2	2.0 – 2.2	2.0
Core PCE inflation[4]	1.8	1.9	2.0		1.7 – 1.8	1.9 – 2.0	2.0 – 2.1		1.4 – 1.8	1.8 – 2.1	1.8 – 2.2	
March projection	2.0	2.0	2.0		1.9 – 2.0	2.0 – 2.1	2.0 – 2.1		1.8 – 2.2	1.8 – 2.2	1.9 – 2.2	
Memo: Projected appropriate policy path												
Federal funds rate	2.4	2.1	2.4	2.5	1.9 – 2.4	1.9 – 2.4	1.9 – 2.6	2.5 – 3.0	1.9 – 2.6	1.9 – 3.1	1.9 – 3.1	2.4 – 3.3
March projection	2.4	2.6	2.6	2.8	2.4 – 2.6	2.4 – 2.9	2.4 – 2.9	2.5 – 3.0	2.4 – 2.9	2.4 – 3.4	2.4 – 3.6	2.5 – 3.5

Source: Federal Reserve, June 20, 2019

…though the FOMC Participants' estimates for the near- and long-term Fed Funds Rate came down again, with the futures market now predicting at least three and maybe four quarter-point cuts over the next 12 months.

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FOMC Fed Funds Rate Targets: June 2019

It is amazing that back in December futures market players were betting that there was a 34.5% chance of at least one hike in the Fed Funds rate by Jan 2020 and a 12.6% chance of a cut. Today, the odds of cut are 100%, with the majority expecting at least a 75 basis point reduction.

FOMC Participants' Fed Funds Rate Target Level
Number with each projection

Midpoint of Target Range	2019	2020	2021	Longer Run
3.375				
3.250				2
3.125		1	1	
3.000				2
2.875			1	
2.750				3
2.625	1	2	3	
2.500				8
2.375	8	5	5	1
2.250				
2.125	1	2	2	
2.000				
1.875	7	7	5	
1.750				

Source: Federal Reserve, June 19, 2019

99) Export — World Interest Rate Probability
United States — Instrument Futures: Fed Funds - Effective — Fed Effective Rate 2.37
1) Overview — 2) Future Implied Probability
Current Implied Probabilities — 3) Add/Remove Rates
Dates: Meeting / Calculation — Calculated 06/21/2019 — Based on rate 2.25-2.50

Meeting	Hike Prob	Cut Prob	1-1.25	1.25-1.5	1.5-1.75	1.75-2	2-2.25	Fwd Rate
07/31/2019	0.0%	100.0%	0.0%	0.0%	0.0%	28.0%	72.0%	2.04
09/18/2019	0.0%	100.0%	0.0%	0.0%	22.8%	63.8%	13.4%	1.84
10/30/2019	0.0%	100.0%	0.0%	9.0%	39.0%	43.8%	8.1%	1.74
12/11/2019	0.0%	100.0%	4.0%	22.5%	41.2%	27.8%	4.5%	1.63
01/29/2020	0.0%	100.0%	9.8%	28.3%	37.0%	20.5%	3.1%	1.55
03/18/2020	0.0%	100.0%	13.7%	30.1%	33.6%	16.9%	2.4%	1.50
04/29/2020	0.0%	100.0%	16.0%	30.6%	31.2%	14.9%	2.1%	1.46
06/10/2020	0.0%	100.0%	18.7%	30.7%	28.2%	12.5%	1.7%	1.42
07/29/2020	0.0%	100.0%	20.1%	30.4%	26.4%	11.2%	1.5%	1.39

99) Export — World Interest Rate Probability
United States — Instrument Futures: Fed Funds - Effective — Fed Effective Rate 2.40
1) Overview — 2) Future Implied Probability
Current Implied Probabilities — 3) Add/Remove Rates
Dates: Meeting / Calculation — Calculated 12/21/2018 — Based on rate 2.25-2.50

Meeting	Hike Prob	Cut Prob	1.75-2	2-2.25	2.25-2.5	2.5-2.75	2.75-3	3-3.25	3.25-3.5	Fwd Rate
01/30/2019	0.0%	2.1%	0.0%	2.1%	97.9%	0.0%	0.0%	0.0%	0.0%	2.40
03/20/2019	16.1%	1.7%	0.0%	1.7%	82.2%	16.1%	0.0%	0.0%	0.0%	2.44
05/01/2019	22.1%	1.6%	0.0%	1.6%	76.3%	20.9%	1.2%	0.0%	0.0%	2.46
06/19/2019	28.0%	1.5%	0.0%	1.5%	70.5%	25.2%	2.7%	0.1%	0.0%	2.48
07/31/2019	37.2%	1.3%	0.0%	1.3%	61.6%	31.1%	5.6%	0.4%	0.0%	2.51
09/18/2019	39.1%	1.2%	0.0%	1.2%	59.7%	32.0%	6.4%	0.6%	0.0%	2.52
10/30/2019	40.8%	1.2%	0.0%	1.2%	58.0%	32.8%	7.2%	0.8%	0.0%	2.52
12/11/2019	38.6%	5.1%	0.1%	5.0%	56.3%	31.1%	6.7%	0.7%	0.0%	2.51
01/29/2020	34.5%	12.6%	0.7%	11.8%	53.0%	27.9%	5.9%	0.6%	0.0%	2.47

Source: Bloomberg

Certainly, we realize that many are worried that the recent plunge in interest rates is a harbinger of recession, despite the Fed's prediction that GDP growth will be 2.1% this year and 2.0% in 2020, but we continue to believe that long-term-oriented equity investors should put aside credit market fears such as the current yield-curve inversion,…

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THE PRUDENT SPECULATOR
10-Year – 3 Month Spread & Equities

While the important 10-Year less 3-Month U.S. Treasury spread remains in negative territory as of 6.21.19, history shows that long-term-oriented equity market investors have done just fine over the past four-plus decades despite several yield-curve inversions along the way.

…and should be excited about how appealing stocks have become on a relative basis from an income perspective.

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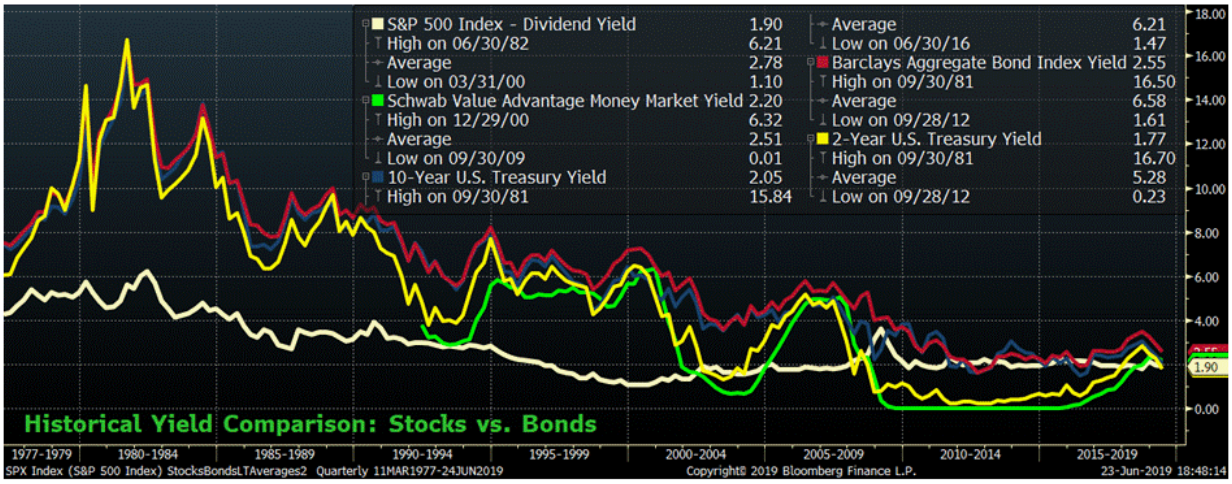
THE PRUDENT SPECULATOR
Equity vs. Fixed Income Yields

Though stocks are not necessarily a substitute for bonds, U.S. Treasuries and money market funds, the current payout on the S&P 500 (1.90%) 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.



To be sure, given the continued drama on the geopolitical stage, we have to expect market volatility to remain elevated, so we are always braced for a near-term equity pullback, even as we continue to be enthusiastic about the prospects for stocks over the next three-to-five years. In addition to a supportive Federal Reserve, we think the U.S. economy will continue to hold up and that corporate profits will remain healthy, while we sleep very well at night given what we believe to be the inexpensive valuation metrics associated with our client portfolios.

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THE PRUDENT SPECULATOR
Managed Account Ports & Benchmarks

CURRENT PORTFOLIO AND INDEX VALUATIONS

Name	Price to Earnings Ratio	Price to Fwd. Earnings Ratio	Price to Sales Ratio	Price to Book Ratio	Dividend Yield
TPS Portfolio	13.1	11.9	1.1	1.9	3.0
Select Value	13.6	12.2	1.2	2.0	2.7
Select Dividend	13.6	12.2	0.9	1.9	3.3
Select Focused Dividend	12.6	11.7	0.9	2.2	3.4
Select Focused Value	14.2	12.8	1.4	2.4	2.7
Select SMID Dividend	12.7	11.5	0.6	1.5	3.2
Russell 3000	20.5	18.4	2.0	3.2	1.9
Russell 3000 Growth	26.0	23.0	2.9	7.0	1.3
Russell 3000 Value	16.7	15.1	1.5	2.0	2.5
Russell 1000	19.8	18.0	2.1	3.3	1.9
Russell 1000 Growth	24.7	22.3	3.1	7.5	1.3
Russell 1000 Value	16.4	15.0	1.6	2.1	2.5
S&P 500 Index	19.3	17.8	2.2	3.4	1.9
S&P 500 Growth Index	25.5	22.3	3.8	5.8	1.4
S&P 500 Value Index	15.1	14.3	1.5	2.3	2.5
S&P 500 Pure Value Index	11.5	10.6	0.6	1.3	2.8

As of 06.21.19. Weights based on model portfolios. Harmonic mean used to calculate the portfolio price metrics. Companies with negative earnings are excluded from the P/E and Estimated P/E calculations. SOURCE: Kovitz Investment Group using data from Bloomberg Finance L.P.

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/, Jason Clark and Chris Quigley offer updates on four of our companies that had news last week that was of sufficient importance to trigger a review of its Target Price.

The last week was not smooth sailing for cruise line **Carnival Corp** (CCL – $46.63), even as the company posted earnings of $0.66 per share in Q2 2019 (vs. $0.62 est.). CCL had revenue of $4.8 billion, versus the $4.5 billion estimate. Shares slid nearly 12% following the announcement, which came ahead of schedule, as the company's gloomy full-year forecast troubled analysts.

Carnival CEO Arnold Donald commented, "We have the foundation and we remain steadfast in our commitment to consistently deliver double-digit earnings growth and growth in return on invested capital over time. We delivered second quarter adjusted earnings per share of $0.66, that's higher than the midpoint of March guidance by $0.08 per share and only $0.02 per share lower than last year despite a $0.09 drag from fuel and currency. For the full year, voyage disruptions related to Carnival Vista are expected to have a financial impact of approximately

$0.08 to $0.10 per share, and that's from a combination of modified itineraries, canceled sailings and the unusual nature of the repair, given the unavailable damage dry dock in Grand Bahama Shipyard, where repairs otherwise would have occurred."

Looking ahead, Mr. Donald added, "We're updating our adjusted earnings guidance range, previously $4.35 to $4.55, now $4.25 to $4.35 due to the voyage disruptions; the U.S. Government's policy change on travel to Cuba, which impacted earnings by $0.04 to $0.06 per share; lower revenue yields in the second half of the year resulting primarily from ongoing headwinds for our Continental European source brands estimated at $0.10 to $0.12 per share and that represents 0.5 of our prior full year yield guidance. That's partially offset by $0.02 per share reduction in cost due to lower fuel consumption and a favorable $0.08 per share from changes in fuel and currency since the time of our March guidance."

He continued, "The U.S. Government's policy's change for travel to Cuba has the financial impact of approximately $0.04 to $0.06, as I just mentioned per share, as we have to make deployment changes very close in. While the regulatory change was disappointing as these sailings had experienced strong demand and were well booked and significant yield premiums, we were able to adjust our itineraries to provide our guests with attractive alternative vacation experiences utilizing the 6 destination ports that we own and operate in the Caribbean, which are among our highest rated destinations based on guest feedback."

Mr. Donald concluded, "In 2020 and beyond, we remain focused on cost containment and aside from the impact of voyage disruptions, we are maintaining the cost guidance we gave for the year. Included in our guidance is a planned increase in our investment and demand creation in the back half of the year to further position us for 2020. However, that increase in advertising is offset by cost savings in other areas. Now we continue to rollout applications across multiple brands, designed to enhance the guest experience and to promote onboard sales, including Ocean Medallion for Princess, and we expect to have 11 Princess ships rolled out by the end of 2020. Of course, our ongoing new-build program is integral to the growth in earnings and return on invested capital over time. And as we mentioned before, not only are our new-builds on average roughly 15% to 25% more cost efficient and approximately 25% to 35% more fuel efficient, they also help to create further demand for cruising. There are headwinds every year. And over the past 5 years, we've demonstrated our ability to overcome multiple headwinds and deliver strong operational improvement. Now this year, our growth has been hampered by a complements of events, which our people have worked hard to mitigate."

The cruise operator has been on the receiving end of a lot of flack lately, earlier in the month having agreed to pay $20 million for environmental-related violations. The judge in the case chided Mr. Donald and chairman Micky Arison for the company's third conviction of this type of crime, reminding them that without the environment, CCL would have nothing to sell. In addition, MSC Opera crashed heavily into its dock in Venice, prompting much blow back from locals, some of whom would like to see cruise ships docked elsewhere. Although CCL does not own the MSC Opera, it does sail to Venice and changes to docking there or elsewhere could have significant impact on the business.

Analysts had been expecting CCL's EPS midpoint for 2019 to be around $4.55, but the actual guidance had a midpoint of $4.30. A confluence of mostly unrelated events have put a damper on CCL's ability to execute over the near term and it's unclear when geopolitical headwinds will abate (particularly in relation to the inability to dock in Cuba), but we maintain our long-term optimism on CCL and the overall cruise industry space, given favorable demographic trends and the fact that there are still meaningful growth opportunities in emerging economies, which are encouraging for global revenue diversification and the ability to rapidly reach a new customer base.

While near-term headwinds will continue to blow, CCL shares now sport a 4.3% dividend yield and a forward P/E ratio of 10.2. Our Target Price has been trimmed to $75.

Kroger Co. (KR – $22.37) saw its shares drop over 8% last week after the grocery and convenience store operator posted its fiscal Q1 2020 financial results and issued its full-year fiscal outlook. Adjusted Q1 EPS came in at $0.72, versus the consensus analyst estimate of $0.71. Revenue for the period was $37.3 billion, versus the $37.2 billion estimate. Kroger, the nation's biggest supermarket operator, said same-store sales excluding fuel rose 1.5% in the latest quarter, a weaker performance compared with last year and below what analysts predicted for the period. Pet products, natural foods and several beverage categories were strong performers during Q1. Kroger also added 219 new private-label products during the quarter and sales in this area grew faster than total sales. The profit margin for private-label products exceeds what Kroger gets from selling national brands, however, overall gross profit margin fell in the quarter, primarily due to the performance of its pharmacy business.

CEO Rodney McMullen said, "Because the retail industry is constantly transforming, we proactively launched Restock Kroger to deliver for our customers and shareholders. It all starts with our customer obsession, which is why Kroger is assembling a platform to deliver anything, anytime, anywhere…We are building momentum in the second year of Restock Kroger, which is off to a solid start. The entire company is focused on redefining the grocery customer experience, improved upon by exciting partnerships that will create value. We are on track to generate the free cash flow and incremental adjusted FIFO operating profit that we committed to in 2019 as part of Restock Kroger. We are confident in our ability to deliver on our plans for the year and our long-term vision to serve America through food inspiration and uplift."

The company said it is seeing positive sales momentum thus far in Q2, and reiterated its forecast for EPS in the range of $2.15 to $2.25 for full-year fiscal 2020, compared with the $2.18 consensus estimate. Management wants investors to be patient, as we are, while the company continues to be transformed even in the midst of heightened competition. Mr. McMullen commented on the capital efforts to improve customer experience, "What we find is there's a lag between when you make those improvements and when the customer starts rewarding you with their checkbook." Kroger has been investing in its e-commerce operation and stated that home-delivery services or online-order-and-pickup at stores is now available at 93% of its locations and digital sales grew 42% in the first quarter. Additionally, Kroger has been developing new businesses, such as selling consumer data and targeted advertising. The company said those efforts would yield $100 million in incremental operating profit in its current fiscal year compared with the prior one.

There is no doubt that competitive threats remain from the likes of Amazon, **Walmart** (WMT – $111.13), **Target** (TGT- $87.60), Aldi and numerous others, but Kroger has been battling competition for years. We remain constructive on the company's makeover and focus on investing in online abilities as well as improving the customer experience in physical stores. KR shares trade at a very reasonable 10.1 times NTM adjusted EPS projections, while the stock yields 2.5%. Our Target Price on KR remains $34, and we think the continued pessimism and 19% drop in share price so far in 2019 is very much overdone.

System software firm **Oracle** (ORCL – $56.12) earned $1.16 per share in fiscal Q4 2019 (vs. $1.07 est.). ORCL had total revenue of $11.1 billion, versus the $10.9 billion estimate. Shares traded higher by 8.2% the day after the announcement, as investors were pleased with the company's sales growth amid the transition to a subscription license model

Co-CEO Safra Catz commented, "Our customers are maintaining and expanding this Oracle environment. And in our BYOL route, Bring Your Own License model, they have the portability to use their licenses on-premise, in the cloud or via hybrid environment. This popularity is largely because our products are capable of doing things others just can't do, whether it's security, performance or scalability, and in our cloud, autonomous capabilities. As our customers adopt our technologies, whether via licenses or cloud services, our overall customer base is growing and that growth is starting to accelerate."

He continued. "Assuming the current exchange rates remain the same as they are now, currency should have about 1% negative effect on total revenues and about $0.01 negative effect on EPS. So for Q1, total revenues are expected to grow between 1% to 3% in constant currency. Non-GAAP EPS in constant currency is expected to grow between 14% to 16% and be between $0.81 and $0.83 in constant currency. This past year, we grew 3%. And for fiscal year 2020, I expect total revenue will grow faster than last year constant currency, of course, and that we will once again report double-digit EPS growth. Total CapEx for fiscal year '20 is expected to be about $2.2 billion, but it could move a little depending on our bookings. My EPS guidance for Q1 and fiscal year '20 assumes our base rate of 20%. However, onetime tax events could cause actual tax rates for any given quarter to vary from our base, both higher or lower. But I expect that in normalizing for these one-time tax events, our tax rate will average around 20% for fiscal year 2020."

Founder Larry Ellison added, "In Q4, we saw a surge in database license sales. We also saw a very rapid growth in sales of those database options required to run our Autonomous Database. We continue to gain overall database market share as we migrate our database users to the cloud. In the quarter, we added over 5,000 new Autonomous Database trials in our Gen 2 public cloud. Our new Gen 2 Cloud infrastructure offers customers a compelling array of advanced technology features, including our self-driving database that automatically encrypts all your data, backs itself up, tunes itself, upgrades itself and automatically patches itself when a security threat is detected. It does all of this autonomously, while running without the need for any human intervention and without the need for any downtime. No other cloud infrastructure provides anything close to these autonomous features."

We continue to be encouraged by the possibilities in the cloud business and we believe that ORCL has an experienced leadership team that will drive top-line growth to the bottom line. We have been pleased with ORCL's execution, after a difficult initial transition to the subscription model, and think that despite the fierce cloud competition, there is plenty of room for more than one firm to be successful. In addition to ORCL, we like our other cloud-centric holdings **NetApp** (NTAP – $61.46) and **Microsoft** (MSFT – $136.97). We think that ORCL shares remain undervalued, trading at less than 15 times forward earnings. That's in comparison to ORCL's competitors VMWare, SAP and Red Hat that trade for 27x, 25x and 47x, respectively. Our Target Price has been hiked to $64. ORCL currently yields 1.7%.

Electronic manufacturing services firm **Jabil Inc.** (JBL – $30.40) earned $0.57 per share in fiscal Q3 2019 (vs. $0.57 est.). JBL had sales of $6.1 billion (vs. $6.0 billion est.). Since the announcement, shares have moved up 11%. JBL was propelled by 26% year-over-year revenue growth in the EMS (Electronics Manufacturing Services) segment and strong demand in the cloud, point-of-sale, 5G/wireless and industrial sectors. The company's DMS (Diversified Manufacturing Services) segment saw a 1.3% improvement in operating margin to 2.6%.

CEO Mark Mondello commented on the top-of-mind trade situation, "Today, very few customers are moving existing production out of China. I believe this decision made by those customers is based on 3 factors: one, the deep-rooted, mature supply chain that's foundational to China; two, many of our customers don't see a reasonable payback associated with such a move; and three, a decent percentage of our China revenue is for final consumption in geographies other than the United States. With that said, if the landscape shifts and customers change their mind, Jabil's well positioned to author and implement safe and practical solutions, which best serve the needs of our customers. In fact, I believe Jabil is positioned better than most, especially when considering the commonality of our IT systems embedded throughout our seamless network of factories around the globe."

Mr. Mondello continued, "We plan to increase free cash flow roughly 25% year-on-year, fiscal '19 to '20, expand core operating margins and provide another year of double-digit core EPS growth. We will also break down the shape of the year by quarter in terms of expected core EPS contribution. Finally, we maintain a well-balanced capital return framework for which we remain fully committed."

CFO Mike Dastoor added, "In Q4, DMS segment revenue is expected to increase 4% on a year-over-year basis to $2.5 billion, while the EMS segment revenue is expected to increase 22% on a year-over-year basis to $4.1 billion. We expect total company revenue in the fourth quarter of fiscal 2019 to be in the range of $6.3 billion to $6.9 billion for an increase of approximately 14% at the midpoint of the range. Core operating income is estimated to be in the range of $215 million to $275 million with core operating margin in the range of 3.4% to 4%. GAAP operating income is expected to be in the range of $169 million to $235 million. Core delivered earnings per share is estimated to be in the range of $0.76 to $0.96. GAAP diluted earnings per share is expected to be in the range of 47% to $0.71. The tax rate on core earnings in the fourth quarter is estimated to be in the range of 27% to 29%."

JBL – Customer Risk Mitigaton

Market Diversification

JABIL

DIVERSIFIED MANUFACTURING

$ in billions	FY19E
Mechanics	$1.9
Healthcare & Packaging	$3.2
Edge Devices & Accessories	$4.1
AR/VR/Lifestyle	$0.7
Total Revenue	**$9.9**
Core Operating Margin	3.9%
Core EBITDA	$890M

ELECTRONICS MANUFACTURING

$ in billions	FY19E
Automotive	$1.5
Digital Print & Retail	$2.4
Industrial & Energy	$2.5
5G / Wireless & Cloud	$4.2
Enterprise	$4.8
Total Revenue	**$15.4**
Core Operating Margin	3.2%
Core EBITDA	$760M

See U.S. GAAP to non-GAAP definitions located at https://investors.jabil.com/

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We were pleased that JBL reported a strong quarter despite what in our view is a challenging market, considering the U.S.-China trade uncertainty and related customer concerns. Jabil has historically been sensitive to fluctuations in **Apple** (AAPL – $198.78) orders via its DMS segment, but the company has been working diligently to grow the EMS segment, reducing much of its risk to a single customer. Of course, we also note that the stock presently trades for just 9.4 times the current EPS estimate for the next 12 months. Our Target Price for JBL has been raised to $47. Shares yield 1.1%.