Market Commentary Monday, August 19, 2019

August 19, 2019

EXECUTIVE SUMMARY

Rates – Treasury Yields Plummet
800-Points Down – Perspective on Wednesday's Big Dow Decline
Yield Curve Inversion Part 1 – Stocks Have Done Well on Average After 2-Year Yield Exceeds 10-Year
Yield Curve Inversion Part 2 – Stocks Have Done Well on Average After 3-Month Yield Exceeds 10-Year
Recession Probability – 35% Chance Today; Highest Since 2011, but Atlanta Fed and Janet Yellen Say No Near-Term Contraction
Recessions and Stocks – Economic Downturns No Reason to Sell
Reason for Optimism – Incredibly Low Interest Rates; Increasing Dividends, Healthy Earnings
Target Prices – New Listing Coming to the Website
Stock Updates – SYMC, WMT, CSCO, DE, NTAP & TPR

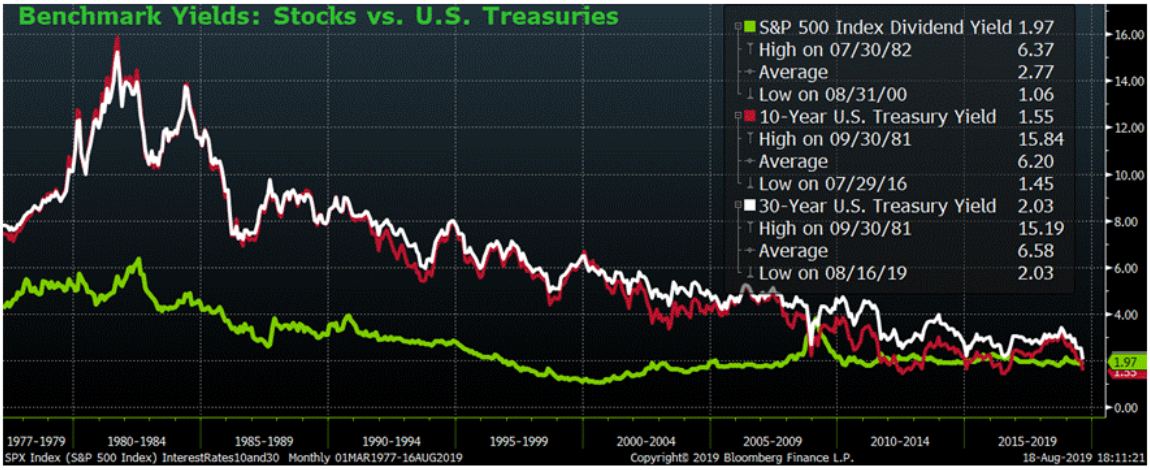
Market Review

While the trading week just completed ended on a very high note with many of the recently hardest hit stocks bouncing back sharply on Friday, it was a dismal five-day period, especially for deep value names. No doubt hurt by a heavy weighting in financial stocks, the S&P 500 Pure Value index skidded 2.60%, compared to a 0.94% dip in the S&P 500, as interest rates plunged anew.

AFAM
a KOVITZ division

THE PRUDENT SPECULATOR
Equity vs. Treasury Yields

Though stocks are not necessarily a substitute for government bonds, the current payout on the S&P 500 (1.97%) is very generous versus that available from U.S. Treasuries, with the yield on Uncle Sam's 30-year bond plumbing historic lows last week. Incredibly, over the past four decades, the only other time dividend yields have compared so favorably to the income from the 30-year was during the Financial Crisis.



Indeed, the investor love affair with fixed income in general and U.S. Treasuries in particular continued, with the 30-year government bond yield hitting an all-time closing low of 2.03% on Friday, after piercing the 2% level on Thursday, the day following another big whack in the equity markets, with the Dow Jones Industrial Average tumbling 800 points on Wednesday.

AFAM
a KOVITZ division

THE PRUDENT SPECULATOR
Giant Single Day Dow Price Moves

Days like 8.14.19, are rare, but since 1927 there have been 90+ times when the Dow has lost at least 3.046% in one trading session.

	1920's	1930's	1940's	1950's	1960's	1970's	1980's	1990's	2000's	2010's	Totals
Years Ending in 0		19	6	2	0	1	0	2	4	3	37
Years Ending in 1		31	0	0	1	0	0	1	4	6	43
Years Ending in 2		49	0	0	1	0	1	0	5	0	56
Years Ending in 3		23	1	0	0	2	0	0	1	0	27
Years Ending in 4		3	0	0	0	2	0	0	0	0	5
Years Ending in 5		0	0	1	0	0	0	0	0	2	3
Years Ending in 6		2	4	0	0	0	2	0	0	1	9
Years Ending in 7		16	1	0	0	0	8	2	1	0	28
Years Ending in 8	2	8	2	0	0	0	2	4	19	4	41
Years Ending in 9	20	5	0	0	0	0	1	0	8	1	35
Totals	22	156	14	3	2	5	14	9	42	17	284

From 12.31.27 through 8.16.19. Days of index price return drops of more than 3.046%. SOURCE: Kovitz Investment Group using data from Bloomberg

	1920's	1930's	1940's	1950's	1960's	1970's	1980's	1990's	2000's	2010's	Totals
Years Ending in 0		10	3	0	0	2	1	1	3	1	21
Years Ending in 1		24	1	0	0	1	0	1	4	3	34
Years Ending in 2		42	0	0	3	0	5	0	9	0	59
Years Ending in 3		33	0	0	1	2	0	0	3	0	39
Years Ending in 4		3	0	0	0	8	1	0	0	0	12
Years Ending in 5		0	0	0	0	1	0	0	0	1	2
Years Ending in 6		0	2	0	0	0	0	0	0	0	2
Years Ending in 7		6	0	1	0	0	6	3	0	0	16
Years Ending in 8	2	13	0	0	0	1	3	4	18	1	42
Years Ending in 9	10	3	0	0	0	0	1	0	7	1	22
Totals	12	134	6	1	4	15	17	9	44	7	249

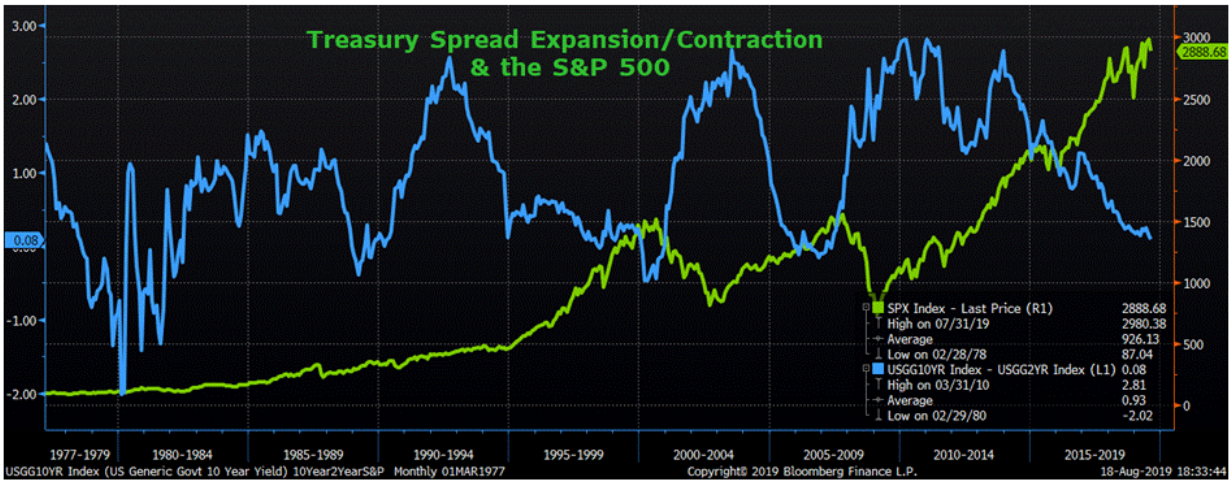
From 12.31.27 through 8.16.19. Days of index price return gains of more than 3.046%. SOURCE: Kovitz Investment Group using data from Bloomberg

To be sure, a host of factors contributed to the big mid-week drop in stocks, ranging from weak economic data in Germany to disconcerting geopolitical developments to fears about an escalation in the trade skirmish with China, but the main catalyst had to do with the inversion of the 10-year/2-year U.S. Treasury yield curve. Though it only briefly fell into negative territory on Wednesday, and the yield on the 10-Year U.S. Treasury is now 8 basis points higher than that of the 2-Year (i.e. no longer inverted), many market watchers sounded warning bells that a U.S. recession must now be on the horizon,…

AFAM
a KOVITZ division

THE PRUDENT SPECULATOR
10-Year/2-Year Spread & Equities

While the media was abuzz with recession warnings after the 10-Year less 2-Year U.S. Treasury spread briefly fell into negative territory on 8.14.19, history shows that long-term-oriented equity market investors have done just fine over the past four-plus decades despite several yield-curve inversions…and the inversion as of this moment is no longer.



…which many folks seemed to take as a signal to dump stocks, even as the historical evidence (albeit there have only been eight prior 10-year/2-year yield-curve inversions and some may quibble with our start dates) hardly supports such a course of action.

S&P 500 Total Return Post 10-Year/2-Year Yield-Curve Inversion

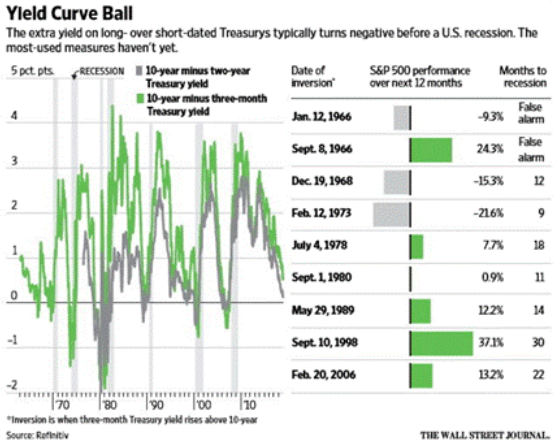
Inversion Date	1 Year S&P 500 TR	3 Year S&P 500 TR	5 Year S&P 500 TR	10 Year S&P 500 TR	To Present S&P 500 TR
8/18/1978	9.2%	45.5%	103.4%	295.0%	8470%
9/12/1980	1.8%	53.9%	86.8%	290.6%	6284%
1/14/1982	34.4%	71.2%	184.6%	440.1%	6382%
12/13/1988	32.1%	54.0%	97.7%	451.8%	1926%
3/8/1990	14.2%	47.1%	65.3%	411.1%	1477%
6/9/1998	19.6%	17.5%	-6.4%	43.3%	286%
2/2/2000	-3.1%	-36.7%	-8.6%	-6.2%	200%
1/31/2006	14.5%	-31.3%	11.7%	87.4%	200%
S&P Total Return	**15.3%**	**27.6%**	**66.8%**	**251.6%**	**3153%**

As of 8.16.19. Source: Kovitz Investment Group using data from Bloomberg and the St. Louis Federal Reserve

And, we find it fascinating that the 10-year/2-year inversion would command so much attention, when the 10-year/3-month yield curve, which inverted five months ago and is still inverted, has better predictive power as far as recessions go.

THE PRUDENT SPECULATOR
10-Year/3-Month Inversion and Stocks

Pundits were again shouting dire warnings that a recession is imminent back in March when the U.S. Treasury 10-year/3-month yield curve inverted. With the San Francisco Fed concluding that the spread between the ten-year and three-month yields has the best predictive power of economic contraction, stocks have performed just fine, on average, after previous 10Y/3M inversions.



S&P 500 Total Return Post 10-Year/3-Month Yield-Curve Inversion

Inversion Date	1 Year S&P 500 TR	3 Year S&P 500 TR	5 Year S&P 500 TR	10 Year S&P 500 TR	To Present S&P 500 TR
1/12/1966	-6.8%	19.3%	17.6%	46.2%	15225%
9/8/1966	28.4%	34.2%	58.3%	97.0%	18382%
12/19/1968	-11.8%	4.3%	4.8%	30.6%	12117%
2/12/1973	-19.1%	-2.6%	-4.4%	105.0%	9683%
7/4/1978	13.3%	58.4%	131.5%	352.6%	9379%
9/1/1980	5.6%	56.7%	96.8%	300.3%	6449%
5/29/1989	16.0%	42.6%	66.2%	423.5%	1612%
9/10/1998	39.8%	15.7%	10.7%	48.2%	339%
1/20/2006	15.5%	-36.2%	16.0%	84.3%	198%
S&P Total Return	**9.0%**	**21.4%**	**44.2%**	**165.3%**	**8154%**

As of 8.16.19. Source: Kovitz Investment Group using data from Bloomberg and Refinitiv via The Wall Street Journal

While we do not wish to appear cavalier and we concede that the odds of recession have increased to the highest level since 2011,…

AFAM
a KOVITZ division

THE PRUDENT SPECULATOR
Recession Forecasts: Contra Indicator?

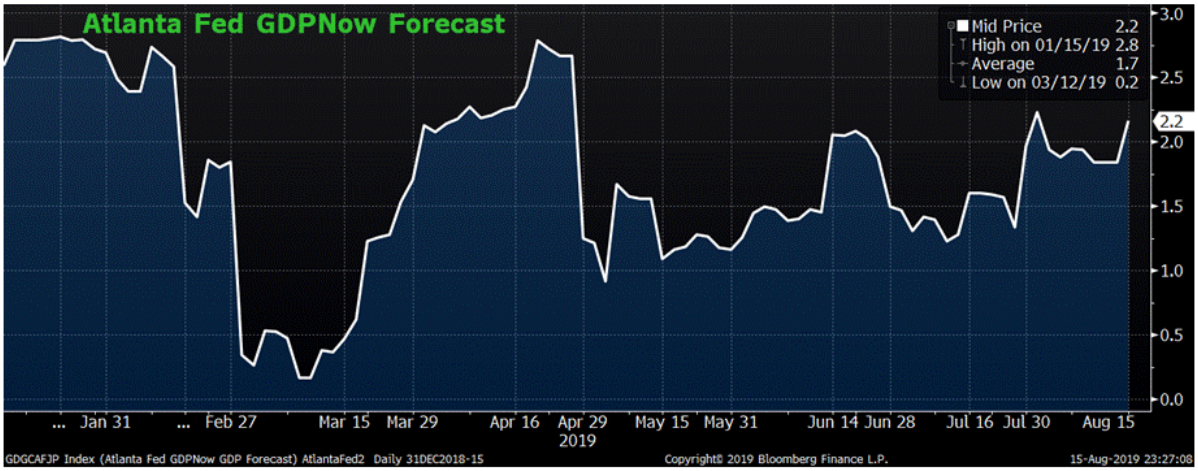
While microscopic interest rates around the world and massive central bank buying of longer-term bonds are the likely cause of the yield-curve inversions, suggesting that the events are not harbingers of recession, we are happy to see that the supposed experts now see the chance of economic contraction at 35%, back to a probability last witnessed in the fall of 2011…which proved to be a fantastic time to buy equities, as the S&P 500 returned 30.2% over the ensuing 12 months.

…we saw healthy data out last week on retail sales and the latest forward projection from the Atlanta Fed is still calling for solid economic growth.

AFAM
a KOVITZ division

THE PRUDENT SPECULATOR
Slowing Growth Argues for Fed Rate Cuts

The John Kenneth Galbraith quotation, "The only function of economic forecasting is to make astrology look respectable," appears quite apt this year, as four months ago, projections for U.S. GDP growth were near zero, only to rebound and tumble in the months since, before rising to the current guess of 2.2% today. Of course, expectations for less-than-stellar growth suggest the Fed has reason to lower interest rates.



Of course, we know very well that recessions are part of the business cycle and there certainly could be an economic contraction in the near- to intermediate-term. But, we note that Janet Yellen said on Wednesday that folks might not want to trust the yield curve inversion as a recession indicator. The former Federal Reserve Chair stated, "Historically, it has been a pretty good signal of recession, and I think that's when markets pay attention to it, but I would really urge that on this occasion it may be a less good signal. The reason for that is there are a number of factors other than market expectations about the future path of interest rates that are pushing down long-term yields."

And, even if we could somehow predict when the economic downturn might arrive, history also shows that we should sit tight in stocks, especially those of the Value variety!

As the saying goes, the stock market (and economists) has predicted nine of the last five recessions, but the 14 prior instances of actual negative economic growth illustrate that long-term-oriented investors (on average) should stay invested (in Value, preferably) no matter what.

U.S. Recession Commencement (per NBER) & Equity Returns
S&P 500 and Fama/French Value Performance

Year Prior S&P 500 TR	Year Prior FF Value TR	Recession Start Date	1 Year S&P 500 TR	1 Year FF Value TR	3 Year S&P 500 TR	3 Year FF Value TR	5 Year S&P 500 TR	5 Year FF Value TR	10 Year S&P 500 TR	10 Year FF Value TR	To Present S&P 500 TR
51.9%	30.8%	August 1929	-32.6%	-32.0%	-73.5%	-64.9%	-71.1%	-61.4%	-58.0%	-47.7%	199727%
18.2%	42.6%	May 1937	-39.3%	-55.8%	-33.2%	-55.1%	-32.5%	-44.3%	53.7%	142.7%	371191%
26.3%	54.4%	February 1945	26.0%	42.2%	12.0%	28.5%	64.3%	75.7%	379.2%	468.6%	267517%
4.0%	4.6%	November 1948	19.2%	12.4%	101.8%	108.9%	145.2%	130.7%	542.0%	584.7%	217284%
3.1%	4.7%	July 1953	31.9%	25.6%	128.9%	118.0%	136.5%	138.2%	308.5%	381.9%	89757%
-1.2%	-0.4%	August 1957	10.0%	16.4%	40.2%	55.0%	55.1%	77.9%	188.9%	418.4%	41198%
-2.4%	-6.4%	April 1960	24.2%	29.0%	41.7%	51.5%	92.4%	131.0%	107.7%	268.9%	31017%
-8.4%	-20.9%	December 1969	3.9%	8.7%	41.4%	40.3%	-11.3%	-7.3%	77.0%	267.9%	13331%
-15.2%	-19.4%	November 1973	-23.8%	-14.8%	20.8%	77.1%	23.7%	142.4%	182.3%	719.9%	11257%
20.6%	31.3%	January 1980	19.5%	12.3%	49.5%	80.4%	102.4%	183.5%	342.4%	480.7%	7045%
13.0%	22.9%	July 1981	-13.3%	-0.8%	34.0%	78.6%	127.9%	217.1%	343.4%	408.6%	5670%
6.5%	-6.9%	July 1990	12.7%	9.9%	38.2%	76.0%	83.2%	129.3%	407.0%	424.9%	1367%
-21.7%	17.0%	March 2001	0.2%	14.6%	1.9%	33.8%	21.4%	83.4%	38.3%	96.0%	254%
9.0%	-5.7%	December 2007	-40.4%	-36.2%	-13.0%	-6.6%	5.3%	5.7%	117.4%	119.5%	143%
7.4%	**10.6%**	**Averages**	**-0.1%**	**2.3%**	**27.9%**	**44.4%**	**53.0%**	**85.8%**	**216.4%**	**338.2%**	**89768%**

As of 8.15.19. Source: Kovitz Investment Group using data from Bloomberg, Professors Eugene F. Fama & Kenneth R. French and the National Bureau of Economic Research

So, while we accept that the equity markets are likely to remain volatile and we recognize that we are still in the historically less-favorable summer months, we see no reason to alter our long-term enthusiasm for our broadly diversified portfolios of what we believe to be undervalued stocks, generally of dividend-paying companies. This is especially true, given the incredibly favorable interest rate dynamic,…

AFAM
a KOVITZ division

THE PRUDENT SPECULATOR
Odds of Equities Beating the 10-Year Yield

PATIENCE IS VIRTUOUS

VALUE STOCKS

	Count >1.55%	Count <=1.55%	Percent Positive
1 Month	688	416	62.3%
3 Months	733	369	66.5%
6 Months	766	333	69.7%
1 Year	785	308	71.8%
2 Year	884	197	81.8%
3 Year	922	147	86.2%
5 Year	918	127	87.8%
7 Year	974	47	95.4%
10 Year	948	37	96.2%
15 Year	919	6	99.4%
20 Year	865	0	100.0%

GROWTH STOCKS

	Count >1.55%	Count <=1.55%	Percent Positive
1 Month	657	447	59.5%
3 Months	700	402	63.5%
6 Months	732	367	66.6%
1 Year	774	319	70.8%
2 Year	826	255	76.4%
3 Year	855	214	80.0%
5 Year	876	169	83.8%
7 Year	917	104	89.8%
10 Year	917	68	93.1%
15 Year	920	5	99.5%
20 Year	865	0	100.0%

From 07.31.27 through 06.30.19. Value stocks are represented by 50% small value and 50% large value returns rebalanced monthly. Growth stocks are represented by 50% small growth and 50% large growth returns rebalanced monthly. SOURCE: Kovitz Investment Group using data from Professors Eugene F. Fama and Kenneth R. French

…and the fact that we continue to see income payouts for our companies rising…

AFAM
a KOVITZ division

THE PRUDENT SPECULATOR
Dividends Provide Handsome Income

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 8.8.19)	244	5	6	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

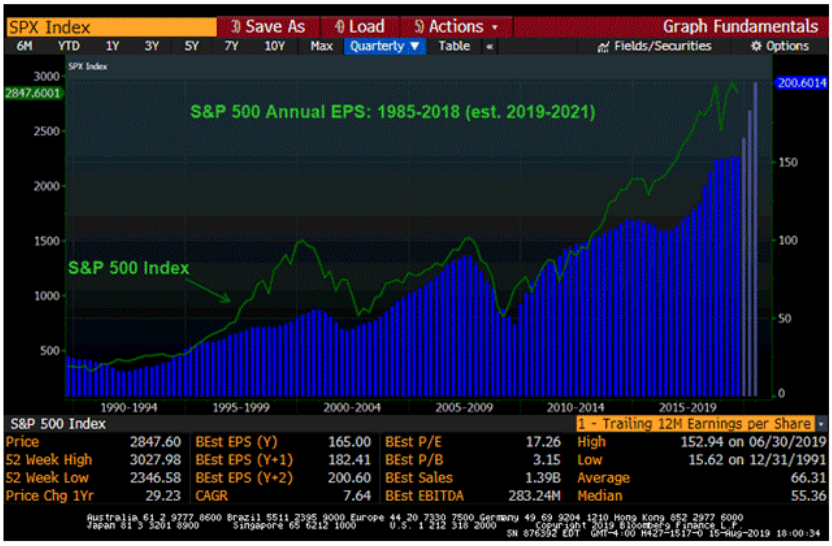
Source: Standard & Poor's.

S&P 500 DIVIDENDS PER SHARE	
2020 (Est.)	$62.33
2019 (Est.)	$58.40
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 8.15.19

…as we believe corporate profits will remain healthy, even with trade and economic concerns.

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		
Quanter Ended	Bottom Up Operating EPS 3 Month	Bottom Up Operating EPS 12 Month
ESTIMATES		
12/31/2020	$48.46	$181.85
9/30/2020	$46.70	$176.12
6/30/2020	$44.86	$170.69
3/31/2020	$41.83	$166.02
12/31/2019	$42.73	$162.18
9/30/2019	$41.27	$154.48
6/30/2019	$40.19	$154.59
ACTUAL		
3/31/2019	$37.99	$153.05
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 8.8.19

Stock Updates

We are in the process of posting updated Target Prices to our website and Chris Quigley and Jason Clark offer updates on half a dozen companies that had news last week that was of sufficient importance to trigger a review of their Target Price. 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/.

Rumors of Broadcom's interest in **Symantec** (SYMC – $23.51) turned out to be true, at least in part, sending shares up over the past couple weeks. On August 8, Symantec announced that it would sell its Enterprise Security business to Broadcom for $10.7 billion. The unit represents about half of SYMC's total revenue (as of 3/29), but only a small portion of net income. Shareholders of SYMC will get a $12 special dividend, which is expected to be tax-exempt, but we have not yet seen a definitive ruling on that yet and tax situations can vary.

"This is a transformative transaction that should maximize immediate value to our shareholders while maintaining ownership in a pure play consumer cyber safety business with predictability, growth and strong consistent profitability. In addition, it allows the Enterprise Security business to grow and compete on an enterprise platform with a worldwide sales and distribution reach which can service our existing customers," said Rick Hill, SYMC Interim CEO. "It also allows

our Norton LifeLock business, a world recognized leader in consumer and small business cyber safety to operate independently and give investors a clear understanding of the growth opportunity and strong financial performance."

While the deal sounds great, we think we would have been happier with Broadcom buying the whole thing, and we can only posit what might have prevented that. At this point, we have a few choices on the table, including to keep our SYMC shares and take the dividend. However, our ongoing evaluation of the deal terms and evaluation of the long-term remaining business remain critical to our choice of direction. Indeed, it concerns us that the remaining Consumer Digital Safety business has dropped in revenue each year since 2013, while the saving grace has been the company's 2017 acquisition of LifeLock. The Identity and Information Protection business (primarily LifeLock) grew from $776 million of revenue in fiscal 2018 to $937 million of revenue in fiscal 2019.

SYMC also reported fiscal Q1 2020 earnings on August 8, which included a strong EPS beat ($0.43 vs $0.33 est.), but most of the subsequent share move was related to the Broadcom news, we suspect. For now, we are holding on to our SYMC shares and we will evaluate SYMC's position in our portfolios as more information comes available and as other potential purchase candidates percolate. Our Target Price for SYMC is $29.

Despite plenty of worry about a looming economic slowdown and the potential impact of the U.S./China trade dispute on domestic retailers, discount mega-retailer **Walmart** (WMT – $112.99) posted strong fiscal Q2 2020 results, which led to a more than 5% increase in share price last week. For the period, adjusted earnings per share came in at $1.27, versus consensus analyst estimates of $1.22. WMT had sales of $130.4 billion (vs. $130.1 billion est.). Walmart had comp-store sales growth of 2.8%, and on a two-year stacked basis it increased by 7.3% (which is the strongest growth in 10 years). U.S. eCommerce sales grew 37%, propelled by online grocery. Net sales at Walmart International were $29.1 billion, a decrease of 1.1%, but excluding currency, they tallied $30.4 billion, an increase of 3.3%. Strength in Walmex and China was offset by softness in the U.K. and Canada.

"From a performance point of view, we're pleased with the strength we see in the business. Customers are responding to the improvements we're making, the productivity loop is working, and we're gaining market share. We're on track to exceed our original earnings expectations for the year, and that's possible because of the work our associates do every day. For the quarter, disruptive weather in parts of the U.S. negatively affected comp sales early on, yet we saw significant improvement in comps as the quarter progressed and weather turned more favorable. On a consolidated basis, we had good top-line growth in constant currency, and along with productivity gains and cost controls, we were able to leverage operating expenses by 23 basis points," commented CEO Doug McMillon.

Walmart continues to fight a good fight against Amazon, with its NextDay delivery service from Walmart.com now covering about 75% of the U.S. population. Additionally, eCommerce momentum should be supported going forward by the expansion of same-day grocery delivery to 1,600 stores (from ~1,100 today) and pick-up locations to 3,100 (vs. the current ~2,700 stores) by year-end.

Fiscal Year 2020 Guidance

The following guidance reflects the company's expectations for fiscal year 2020. Assumptions in the guidance include that economic conditions, currency rates and the tax and regulatory landscape in our largest markets remain generally consistent. Additionally, the guidance assumes no further change in fair value of the Company's equity investment in JD.com.

Metric	Updated FY20 Guidance	Original FY20 Guidance
Consolidated net sales growth	Around 3% in constant currency	At least 3% in constant currency
Comp sales growth	• Walmart U.S.: towards the upper-end of +2.5% to +3%, excluding fuel • Sam's Club: no change	• Walmart U.S.: +2.5 % to +3%, excluding fuel • Sam's Club: around +1%, excluding fuel; around +3%, excluding fuel and tobacco
Walmart U.S. eCommerce net sales growth	No change	Around 35%
Walmart International net sales growth	Between 3% and 4% in constant currency	Around 5% in constant currency
Consolidated Operating Income	• Slight decrease to slight increase, including Flipkart • Increase by a low to mid single-digit percentage range, excluding Flipkart	• Decline by a low single-digit percentage range, including Flipkart • Increase by a low single-digit percentage range, excluding Flipkart
Adjusted EPS[1]	• Slight decrease to slight increase compared with FY19 adjusted EPS, including Flipkart • Increase by a mid to high single-digit percentage range compared with FY19 adjusted EPS, excluding Flipkart • Expectations for the dilution from Flipkart remain unchanged	• Decline by a low single-digit percentage range compared with FY19 adjusted EPS, including Flipkart • Increase by a low to mid single-digit percentage range compared with FY19 adjusted EPS, excluding Flipkart
Effective tax rate	Approximately 26% to 27%	Approximately 26.5% to 27.5%
Expense leverage	At least 20 bps	Approximately 20 bps
Capital expenditures	No change	Approximately $11 billion

Walmart

[1] FY20 GAAP EPS to increase significantly compared to FY19. For FY20, adjusted EPS guidance excludes an unrealized gain of $0.19, net of tax, related to the company's investment in JD.com recorded through the six months ended July 31, 2019.

3

We know that WMT's competitive landscape will only get more intense versus rivals Amazon, **Target** (TGT – $84.21) and numerous other players that will crop up. Still, we continue to think that the steps the company has taken over the last few years to transform itself have it on the right track for long-term success. We continue to like that WMT generates strong free cash flow and remains committed to returning capital to shareholders via buybacks and dividends. True, the yield is down to 1.9%, but it still outpaces the yield of the 10-year U.S. Treasury. Our Target Price has been increased to $120.

Communications equipment firm **Cisco Systems** (CSCO – $46.96) earned $0.83 per share in fiscal Q4 2019 (vs. $0.82 est.). CSCO had revenue of $13.43 billion, versus the $13.39 billion estimate. CSCO shares fell 9% on the news, however, the company's first drop on earnings since May 2018. Macro pressures continue to take their toll on Cisco, resulting in weaker-than-expected EPS guidance for fiscal 2020 and pedestrian revenue growth.

CEO Chuck Robbins said, "We delivered strong revenue and double-digit non-GAAP earnings per share growth for the full year and in the fourth quarter. We also continued to generate healthy margins, cash flow and returns for our shareholders. Our technology is fundamentally redefining IT architectures to help our customers manage the complexities of a multi-cloud world and transform for the future. I'm proud of what our teams have accomplished. We are executing well in a time of uncertainty, delivering differentiated innovation across our portfolio and extending

our market leadership in enterprise networking applications and security. Our performance reflects our relevance as well as the ongoing value we're providing our customers as they transform for the future. We are as committed as ever to providing them with the right innovation to drive greater impact and success. As I look ahead, I could not be more confident about our unique position in the market and the tremendous opportunity in front of us."

CFO Kelly Kramer offered the outlook for fiscal Q1, "We expect revenue growth in the range of 0% to 2% year-over-year. We anticipate the non-GAAP gross margin rate to be in the range of 64% to 65%. The non-GAAP operating margin rate is expected to be in the range of 32% to 33%, and non-GAAP tax provision rate is expected to be 20%. The 1% increase in tax rate over fiscal '19 is primarily due to a forecasted decrease in tax benefits from foreign income. Non-GAAP earnings per share is expected to range from $0.80 to $0.82."

Mr. Kramer discussed the impact of tariffs, in response to an analyst's question, "We're going to run the same play that we have for all the other tariffs, and we'll continue to mitigate, we continue to do everything we can do. I think we're able to offset the headwinds from tariffs with, again, continued benefit from the software, which leads to [good] deferred revenue."

Cisco shares have had been on a tremendous run, and we are glad to have trimmed the position in many of our portfolios earlier this year when the stock was approaching what we then believed to be fair value. Obviously, given the big pullback since, some may wonder why we didn't sell the whole thing, but we think that our equally weighted portfolios have a distinct advantage over capitalization-weighted portfolios and trimming large positions is part of that, as the evidence from the good Professors Fama and French confirms. We only pared the Cisco holdings back to a full position size and we are still happy to hold the balance of our CSCO shares. Our belief is that shares are still inexpensive, with forward earnings projections of at least $3.33 each of the next three years, a forward P/E ratio of 14.1 and a solid 3.1% yield. We remain long-term fans of CSCO. Our Target Price is now $61.

Agricultural and farm machinery firm **Deere & Co.** (DE – $149.23) reported fiscal Q3 2019 financial results that came in below consensus analyst estimates. For the quarter, Deere announced adjusted EPS of $2.71, versus expectations of $2.84. DE had sales of $8.97 billion (vs. $9.38 billion est.). The stock actually rallied almost 4% on the news on Friday, a surprising move on the surface, but the shares had been down more than 15% in August on mounting concerns about China not buying U.S. agriculture products. Fears seemed to be eased a bit on management's pledge to lower costs and its offer of an outlook cut that was less than some evidently were expecting.

"John Deere's third-quarter results reflected the high degree of uncertainty that continues to overshadow the agricultural sector," said CEO Samuel R. Allen. "Concerns about export-market access, near-term demand for commodities such as soybeans, and overall crop conditions, have caused many farmers to postpone major equipment purchases. At the same time, general economic conditions remain positive and are contributing to strong results for Deere's construction and forestry business."

Deere equipment sales are projected to increase by about 4% for fiscal 2019 compared with 2018. Included in the forecast are Wirtgen results for the full fiscal year of 2019 compared with 10 months of the prior year. This adds about 1% to the company's net sales forecast for the current year. Also included is a negative foreign-currency translation effect of about 2% for the year. Net sales and revenue are projected to increase about 5% for fiscal 2019. Net income is forecast to be about $3.2 billion.

"In spite of present challenges, the long-term outlook for our businesses remains healthy and points to a promising future," Mr. Allen said. "We continue to expand our global customer base and are encouraged by response to our lineup of advanced products and services. Furthermore, we are fully committed to the successful execution of our strategic plan focused on achieving sustainable profitable growth. In support of the strategy, we are conducting a thorough assessment of our cost structure and initiating a series of actions to make the organization more structurally efficient and profitable."

AFAM a KOVITZ division

THE PRUDENT SPECULATOR

DE – Favorably Priced Buyback Program

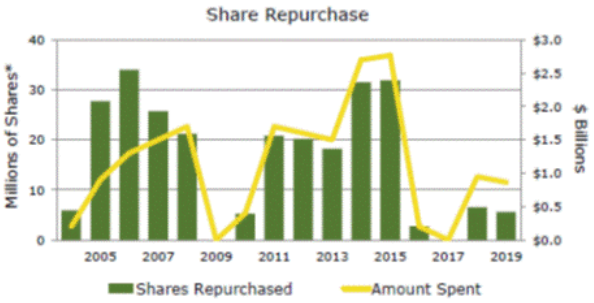
Share Repurchase

As Part of Publicly Announced Plans

37% net share reduction since 2004

3Q 2019:	
Cost of repurchases	$400.0 million
Shares repurchased	2.6 million
YTD 2019:	
Cost of repurchases	$864.0 million
Shares repurchased	5.6 million
2004–3Q 2019:	
Cumulative cost of repurchases	$18.2 billion
Shares repurchased	257.0 million
December 2013 authorization of $8 billion:	
Amount remaining	$1.4 billion
28 July 2019 period ended basic shares	314.9 million
3Q 2019 average diluted shares	319.8 million

** All shares adjusted for two-for-one stock split effective 26 November 2007*



While we weren't excited about fiscal Q3 results, we can't say that we were shocked considering weather in the U.S. earlier in the year and the U.S.-China trade issues. We agree with management that farmers will continue to hold off where possible until better visibility into the situation is available, but we think the company erred on the side of caution into the year-end. That said, we would assume in the near-term that the shares will continue to be a bit more

volatile reacting to trade headlines and any commentary around order activity. Looking past those headwinds, we remain optimistic about the long-term potential of global agriculture in general as the decline of worldwide arable land and population growth should force farmers to be more productive and should continue to drive demand for more efficient farming. Of course, while we think that Deere will benefit from continued global demand, we will be paying very close attention to input costs, trade conflict impact and regional demand changes. Shares yield 2.0% and management has made significant share repurchases. Our Target Price for DE now stands at $176.

Shares of **NetApp** (NTAP – $46.76) saw some relief after plunging two weeks ago when the data storage solutions provider reported preliminary fiscal Q1 2020 results. The final Q1 EPS results were not quite as bad as had been warned, with actual EPS of $0.61, compared to the guidance range of $0.55 to $0.60. Revenue was $1.236 billion, versus the guidance range of $1.22 billion to $1.23 billion. For Q2, NTAP now expects adjusted EPS to climb to $0.91 to $0.99 per share, with revenue in the $1.325 billion to $1.475 billion range.

CEO George Kurian said, "While I'm clearly disappointed in our weaker-than-expected top line results, the fundamentals of our business are robust, and I am confident that we have the right strategy and technologies to address the market transitions to all-flash arrays, private cloud and cloud data services. We have a strong business model as a result of the hard work we conducted to improve gross margin and cost structure over the last several years. This enables us to navigate the ongoing macroeconomic headwinds and make the strategic moves that position us well to return to growth."

"We have further analyzed the dynamics of what happened in the first quarter, and they confirmed that we are seeing a combination of slowdown related to overall macro conditions and company-specific go-to-market execution issues. We continue to see pressure on deal sizes, longer sales cycles and deferral of transactions. Our underperformance is not across the board," continued Mr. Kurian. "I am confident in our strategy and the fundamentals of our business model. Our continued strong cash generation is a great example of the underlying health of our business. We remain committed to our capital allocation policy of returning cash to shareholders through share buybacks and the recently increased quarterly dividend. We will remain fiscally disciplined with our expenditures while still investing for the long-term health of our business. We consistently receive positive feedback from our customers and partners on the value of our Data Fabric strategy, and the strong performance of our best teams demonstrates our ability to capitalize on this strength. We are confident that we can return to growth by replicating their success in reaching more customers and buying centers with our full portfolio. We will keep you updated on the progress of these initiatives on future calls."

While NTAP took Q1 on the chin, we think that the business remains highly attractive for our long-term oriented portfolios. As an example of a headwind we think should eventually abate, the company has two large customers that are exposed to the China tariff situation and both have cut their capital spending by a significant percentage as a result. Management believes that in addition to such geopolitical battles getting resolved, the company's strong relationships with its customers should continue to grow. We think the business model remains attractive, as does the reasonable valuation (with a forward P/E near 11) and EPS north of $4 expected for each of the

next three fiscal years. The company has a strong balance sheet and the just-hiked dividend yield is a generous 4.1%. Our Target Price for NTAP now resides at $77.

Though the stock had already cratered on trade-related worries, shares of upscale retailer **Tapestry** (TPR – $19.96) plunged more than 27% last week when it turned in its fiscal 2019 fourth-quarter report complete with soft sales in its Kate Spade unit and a disappointing outlook for fiscal 2020. Overall Q4 results were relatively in line with expectations as adjusted EPS equaled $0.61 on revenue of $1.51 billion. The Coach brand reported a strong adjusted operating margin of 27.5% on strong sales of innovative product and reduced discounting. However, Kate Spade's 6% sales growth in the quarter missed investor expectations, as did margins, with the blame placed on fashion missteps and slow sales at North America outlet stores. The Stuart Weitzman brand had sales of $85 million (better than expected) and an adjusted operating loss of $10 million (worse than expected). Management now expects flat EPS in fiscal 2020 as compared with fiscal 2019, due in part to lower sales and store growth expectations for Kate Spade.

CEO Victor Luis had plenty to say about the recent results and business going forward: "Fiscal 2019 was a year of meaningful evolution for Tapestry. We experienced ongoing strength in our business internationally, while navigating a volatile backdrop in North America. Importantly, we made significant progress on our strategic initiatives, most notably building the foundation of our distinctive multi-brand platform. We generated the anticipated synergies from the successful integration of Kate Spade into our portfolio, which funded, in part, material investments in systems as well as our international development through distributor acquisitions and new store openings in key regions. We also made key additions to Tapestry's leadership team. Taken together, we believe these actions will underpin our near- and long-term growth objectives."

He continued, "Coach – our largest and most globally diversified brand – had a strong year, driven by growth in our international and digital channels, while outperforming the direct competition in North America. We understand that driving sustainable growth at Coach is essential to the success of Tapestry overall and are proud of the brand's performance, highlighted by seven consecutive quarters of positive comparable store sales…In addition, we made important advancements at Stuart Weitzman, across people, processes and product to address the challenges in the business, driving a return to topline growth in Fiscal 2019. We've also successfully expanded the brand internationally through regional distributor acquisitions and new store openings, with a focus on China, where we are just beginning to tap into this tremendous growth opportunity for the brand…At Kate Spade, the most significant milestone of the year was the debut of Nicola Glass's creative vision, reimagining the brand while staying true to its unique positioning, heritage and DNA. We are incredibly confident in this vision, supported by the emerging positive signs we are seeing, notably in the new brand codes and evolved product in the full price business. That said, the brand's financial results did not meet our expectations and more time is required to drive a positive inflection in the business, particularly in light of the traffic-challenged and competitive retail environment in North America. We acknowledge that there are opportunities to improve performance and we are addressing those areas with a sense of urgency."

Mr. Luis concluded, "Most broadly, we remain steadfast in our strategic vision and focused on maximizing the benefits of our global, multi-brand platform, while continuing to drive strength in our core Coach brand. Our conviction is reflected, in part, by the $1 billion share repurchase program we established and began to implement in the fourth fiscal quarter. Together with our annual dividend, this underscores our confidence in driving long-term, sustainable growth and commitment to returning capital to shareholders."

FISCAL 2020 FINANCIAL OUTLOOK

REVENUE	*low-single-digit growth*
	low-single-digit sales growth at Coach driven by positive comparable store sales growth low to mid-single-digit sales growth at Kate Spade solid sales growth at Stuart Weitzman
GROSS MARGIN	*modest year over year decline*
	reflects pressure from bringing Kate Spade footwear in-house and currency headwinds
SG&A EXPENSES	*approximately in-line with top-line growth*
	growth includes ongoing impact from strategic investments in new stores, regional buy-backs & systems
EARNINGS PER DILUTED SHARE	*roughly even with prior year*
	net interest expense in the area of $45 to $50M tax rate in the area of 17.5%

tapestry *Non-GAAP Financials.*

No doubt, we are frustrated by what has happened to our Tapestry investment, but we believe the massive drop on Wednesday (down 22%) was way overdone, especially considering that TPR is now off some 60% over the last 12 months, and that the stock had lost nearly 20% just in August prior to the earnings report. Despite some of the headwinds and continued hurdles in the transformation of operations, Tapestry's board remains optimistic, confirming the dividend (which now gives TPR a 6.8% yield) and maintaining a share repurchase program that has $900 million to go, which represents almost 16% of market cap as of Friday's close.

While we think Tapestry has done a good job of fixing Coach's past difficulties, including materially reducing exposure to struggling department stores, it seems to have underestimated the problems with Kate Spade. As for Stuart Weitzman, Tapestry is making progress with its production struggles and we believe that its new sneakers fit the athleisure trend. As Tapestry continues to evolve, we can't help but be excited by the fact that the stock trades for just 7.3

NTM earnings expectations, and current EPS forecasts for fiscal ‘21, ’22 and ’23 stand at $2.77, $2.86 and $3.33. We have cut our Target Price to $43, but we think that there is significant upside potential from current levels.