Market Commentary Monday, October 28, 2019

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EXECUTIVE SUMMARY

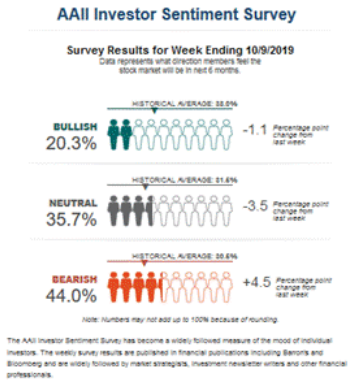
Sentiment – AAII October 9 Buy Signal Still in Play
Value – Winning the Short-Term…and Long-Term Performance Races
Value Buy Signals – Yield Curve Inversion and Weak ISM Manufacturing Number
Econ News – Still no Recession on the Horizon
Valuations – The Market is Reasonably Priced and Value Stocks are Undervalued
Stock Updates – LRCX, INTC, MSFT, CMCSA, BHE, GILD, HAL, WHR, BASFY, ONB, JNPR, CAT, ALB, BIIB, ALK & GT

Market Review

With your Editor having just returned from the American Association of Individual Investors National Conference in Orlando, we might begin this missive with the thought that the handsome market advance last week was due in part to the equity buy signal issued by the AAII Bull-Bear Sentiment Survey two-plus weeks ago when the level of optimism was the weakest in more than three years.

THE PRUDENT SPECULATOR
AAII Sentiment – Contrarian Gauge

Bullish sentiment, expectations that stock prices will rise over the next six months, dipped to 20.3% on October 9, 2019, the lowest level in three-and-one-half years (May 25, 2016). Not surprisingly, given that such pessimistic readings on the often contrarian indictor have been followed by higher-than-average equity returns, the Russell 3000 gained 8.2% and 18.4% over the ensuing 6- and 12-month periods post the 2016 tally, while stocks have rallied over the last two-plus weeks.



AAII Bull-Bear Spread

Decile	Low Reading of the Range	High Reading of the Range	Count	R3K Next 1-Week Arithmetic Average TR	R3K Next 1-Week Geometric Average TR	R3K Next 1-Month Arithmetic Average TR	R3K Next 1-Month Geometric Average TR	R3K Next 3-Month Arithmetic Average TR	R3K Next 3-Month Geometric Average TR	R3K Next 6-Month Arithmetic Average TR	R3K Next 6-Month Geometric Average TR
Below & Above Median Bull Bear Spread = 8.5											
BELOW	-54.0	8.0	831	0.24%	0.20%	1.16%	1.04%	3.29%	2.91%	6.65%	5.92%
ABOVE	8.1	62.9	822	0.17%	0.15%	0.50%	0.42%	1.99%	1.75%	4.56%	4.07%
Ten Groupings of 1653 Data Points											
1	-54.0	-14.6	161	0.34%	0.28%	1.36%	1.12%	4.38%	3.77%	8.64%	7.33%
2	-14.6	-7.0	170	0.41%	0.38%	1.26%	1.13%	3.89%	3.56%	6.98%	6.30%
3	-6.8	-1.0	166	0.28%	0.25%	1.61%	1.52%	3.27%	2.88%	6.84%	6.15%
4	-0.9	3.1	157	0.15%	0.13%	1.08%	1.01%	2.50%	2.17%	5.99%	5.56%
5	3.3	8.0	177	0.03%	0.00%	0.54%	0.44%	2.45%	2.20%	4.91%	4.40%
6	8.1	12.2	155	0.17%	0.15%	0.48%	0.39%	1.74%	1.52%	4.63%	4.12%
7	12.3	16.7	166	0.17%	0.14%	0.90%	0.82%	2.77%	2.56%	5.64%	5.21%
8	16.7	22.0	165	0.18%	0.16%	0.65%	0.58%	2.08%	1.81%	5.82%	5.38%
9	22.2	29.6	168	0.08%	0.06%	0.22%	0.14%	2.03%	1.77%	4.24%	3.65%
10	30.0	62.9	168	0.24%	0.22%	0.25%	0.18%	1.33%	1.10%	2.50%	2.05%

From 07.31.87 through 10.10.19. Unannualized. SOURCE: Kovitz Investment Group using data from American Association of Individual Investors and Bloomberg

To be sure, the good folks at AAII have become much more Bullish and much less Bearish in the days since, but the latest figures of 35.6% for the former and 28.3% for the latter remain near their respective historical averages, so we are still a long way from having to worry about stock market euphoria on Main Street. We also suspect that the big boys on Wall Street are also not that excited about recent activity in the equity markets, given that unloved Value Stocks have been the biggest winners during September and October, with a sizable performance advantage for the Value indexes over their Growth counterparts since August 31.

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THE PRUDENT SPECULATOR
Favorable Returns Growth AND Value

While many think the extraordinarily low interest rate environment and the trend toward passive investing have been the main catalysts for Growth stocks to perform very well over the last decade, we note that the returns on the more inexpensive areas of the equity market have not exactly been chopped liver…and Value has come to life of late!

Total Returns Matrix

Since 8.31.19	Year to Date	1-Year	3-Year	5-Year	7-Year	10-Year	15-Year	20-Year	Symbol	Name
-0.97	6.38	8.57	7.54	9.41	9.38	25.57	65.27	136.71	LEGATRUU Index	Global Aggregate Bond Index
-0.85	8.17	10.59	9.14	16.30	20.63	44.04	83.24	167.51	LBUSTRUU Index	U.S. Aggregate Bond Index
1.34	17.82	6.50	40.51	56.00	125.31	225.50	273.18	263.18	RUO Index	Russell 2000 Growth Index
7.83	15.70	4.07	26.18	41.82	94.65	168.71	192.11	499.99	**RUJ Index**	**Russell 2000 Value Index**
4.50	16.86	5.39	33.42	49.21	110.06	197.01	232.86	385.20	RUT Index	Russell 2000 Index
1.97	25.22	15.16	62.73	88.63	175.77	294.23	351.93	214.36	RAG Index	Russell 3000 Growth Index
5.06	19.04	11.55	33.93	47.45	113.46	192.46	214.71	300.43	**RAV Index**	**Russell 3000 Value Index**
3.47	22.11	13.37	47.97	67.24	143.46	240.85	280.52	271.06	RAY Index	Russell 3000 Index
1.11	22.05	12.87	57.63	84.26	169.57	284.49	339.58	224.70	SGX Index	S&P 500 Growth Index
6.42	23.12	15.43	40.51	54.96	122.84	203.25	215.48	247.82	**SVX Index**	**S&P 500 Value Index**
3.55	22.54	14.01	49.74	70.45	147.27	244.50	276.99	243.83	SPX Index	S&P 500 Index
0.67	20.50	12.78	47.23	62.85	167.63	301.22	385.59	371.66	SPXPG Index	S&P 500 Pure Growth Index
8.12	18.96	7.10	36.51	41.88	139.69	254.63	313.46	480.74	SPXPV Index	S&P 500 Pure Value Index
4.12	3.73	4.86	47.68	51.94	143.03	219.17	291.79	477.43	BRK/B Equity	Berkshire Hathaway Inc

As of 10.25.19. Source Kovitz Investment Group using data from Bloomberg

No doubt, the returns race has favored Growth Stocks in recent years, but like the turtle in *The Tortoise and the Hare*, the long-term performance derby has been won by Value,…

PERFORMANCE: VALUE VERSUS GROWTH

	Fama-French Value	Fama-French Growth	Difference (Value-Growth)	Periods Value Beat Growth	Number of Periods
1-Month	13.24%	9.53%	3.71%	52%	1119
3-Month	13.32%	9.55%	3.77%	58%	1117
6-Month	13.33%	9.55%	3.79%	59%	1114
1-Year	13.35%	9.53%	3.83%	62%	1108
3-Year	13.31%	9.25%	4.06%	72%	1084
5-Year	13.46%	9.30%	4.16%	78%	1060
10-Year	14.34%	9.73%	4.61%	86%	1000
20-Year	15.34%	10.07%	5.27%	100%	880
30-Year	15.63%	10.25%	5.38%	100%	760

From 06.30.26 through 08.31.19. Geometric average of rolling returns for each given time window. Returns are annualized for periods greater than one year. SOURCE: Kovitz Investment Group using data from Professors Eugene F. Fama and Kenneth R. French

…which makes us very excited about the prospects going forward for the inexpensively priced stocks that we have long fancied.

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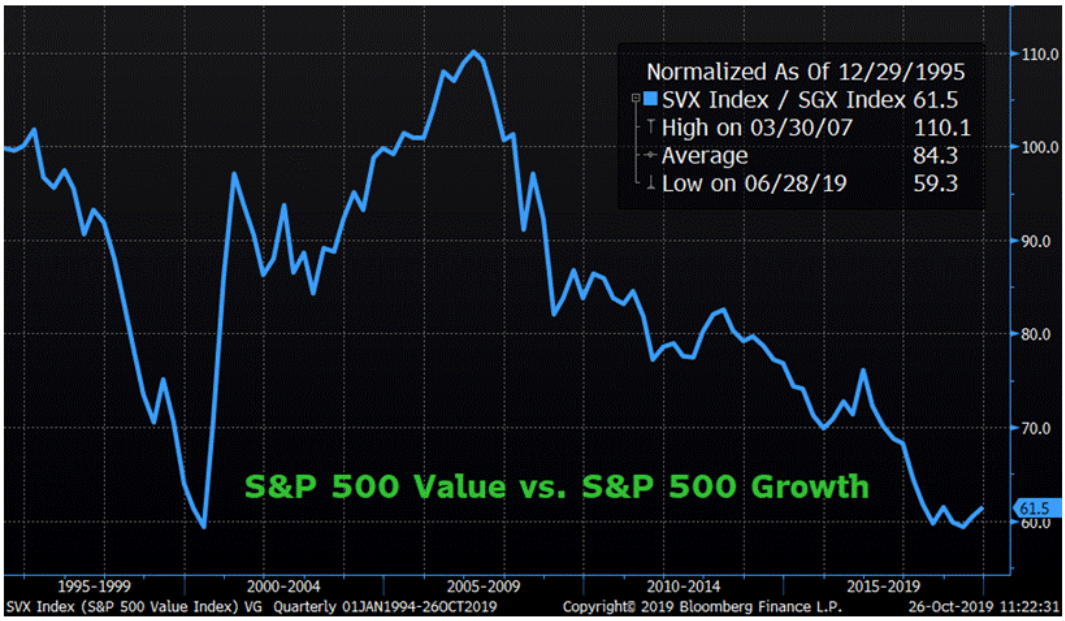
THE PRUDENT SPECULATOR
Value "Buy" Signal Same as March 2000

Value Stocks came to life in September, but there is an extraordinarily long way to go before they would make their way back to equilibrium, much less reassert their historical dominance over Growth.



Adding to the case for Value were green lights generated by the recent yield-curve inversion…

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THE PRUDENT SPECULATOR
Value Buy Signal: Yield Curve Inversions

Inverted Month-End 2/10 Yield Curve and Subsequent Equity Returns

Statistic	Fama French Value	Fama French Growth	Russell 3000 Value	Russell 3000 Growth	S&P 500	DJIA
One-Year						
Average	16.2%	10.3%	10.6%	7.4%	9.2%	10.2%
Median	15.9%	10.1%	9.9%	10.9%	12.0%	9.7%
Max	72.7%	83.8%	61.6%	71.7%	61.2%	58.3%
Min	-24.5%	-35.9%	-16.1%	-45.4%	-26.6%	-15.9%
# Positive	59	42	49	38	44	49
# Negative	10	27	15	26	25	20
Three-Year Annualized						
Average	13.4%	6.2%	7.6%	3.9%	7.6%	8.2%
Median	15.2%	8.8%	10.3%	7.8%	10.3%	8.9%
Max	35.6%	26.7%	29.8%	22.0%	26.3%	24.0%
Min	-21.1%	-22.0%	-17.4%	-25.5%	-16.1%	-11.4%
# Positive	55	47	46	42	47	47
# Negative	14	22	18	22	22	22
Five-Year Annualized						
Average	17.5%	9.5%	12.3%	8.1%	12.2%	12.9%
Median	23.0%	11.9%	15.2%	11.6%	14.0%	13.2%
Max	31.0%	21.9%	28.2%	24.7%	27.9%	30.0%
Min	-4.8%	-5.5%	-3.5%	-10.9%	-5.2%	1.2%
# Positive	61	59	56	53	55	69
# Negative	8	10	8	11	14	0

Source: Kovitz Investment Group using data from Bloomberg, Professors Eugene F. Fama & Kenneth R. French and the St. Louis Federal Reserve. Five periods (generally very good performing) in 1978 are not included in the Russell 3000 Value and Growth Total Return Series as data did not exist.

While the financial press continues to shout about the supposed dangers of a yield-curve inversion, even as central bank buying of government debt has no doubt pushed longer-term interest rates lower, we think market history can help mitigate investor fears. After all, looking at what actually has occurred with stocks following the 69 (or 64 for the Russell indexes) month-ends when the yield on the 2-Year U.S. Treasury has topped that of the 10-Year shows that, on average, one-, three- and five-year Value returns have blown away Growth, and the S&P 500 and Dow have also performed well.

…and the weak reading on the Institute for Supply Management's (ISM) Manufacturing Index.

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THE PRUDENT SPECULATOR
Major Value Buy Signal: ISM PMI

Returns Following ISM PMI Readings of <= 47.8

Statistic	Fama French Value	Fama French Growth	S&P 500
One-Year			
Average	26.6%	22.7%	19.9%
Median	26.8%	23.6%	21.1%
Max	84.6%	83.8%	61.0%
Min	-24.5%	-28.0%	-23.6%
# Positive	151	153	153
# Negative	26	24	24
Three-Year Annualized			
Average	20.5%	14.0%	15.4%
Median	22.1%	15.4%	15.4%
Max	38.9%	28.4%	32.7%
Min	-6.6%	-7.2%	-4.6%
# Positive	176	166	166
# Negative	1	11	11
Five-Year Annualized			
Average	18.7%	13.1%	14.6%
Median	18.8%	13.3%	15.1%
Max	32.5%	25.7%	29.7%
Min	3.2%	-6.3%	-0.6%
# Positive	177	172	176
# Negative	0	5	1

From March 1948 - July 2019. Source: Kovitz Investment Group using data from Bloomberg, Professors Eugene F. Fama & Kenneth R. French and the Institute for Supply Management.

There was plenty of hand-wringing as October 2019 began when a sizable equity market selloff (so far short-lived) occurred following a sub-par Manufacturing Index (aka PMI) tally from the Institute for Supply Management. With a reading of 47.8, the PMI signified contraction in the factory sector, which would seemingly be a negative for the U.S. economy and, in turn, stocks…yet the historical evidence convincingly argues otherwise. In fact, looking at what actually has occurred with equities following the 177 times that the PMI has tallied 47.8 or lower shows that, on average, one-, three- and five-year returns have been more than fantastic, with Value leading the way by a wide margin.

On that last statistic, we respect that many are concerned that an economic contraction is possible, even as the ISM itself specifically stated that the 47.8 reading for September equates to 1.5% GDP growth in the overall economy,…

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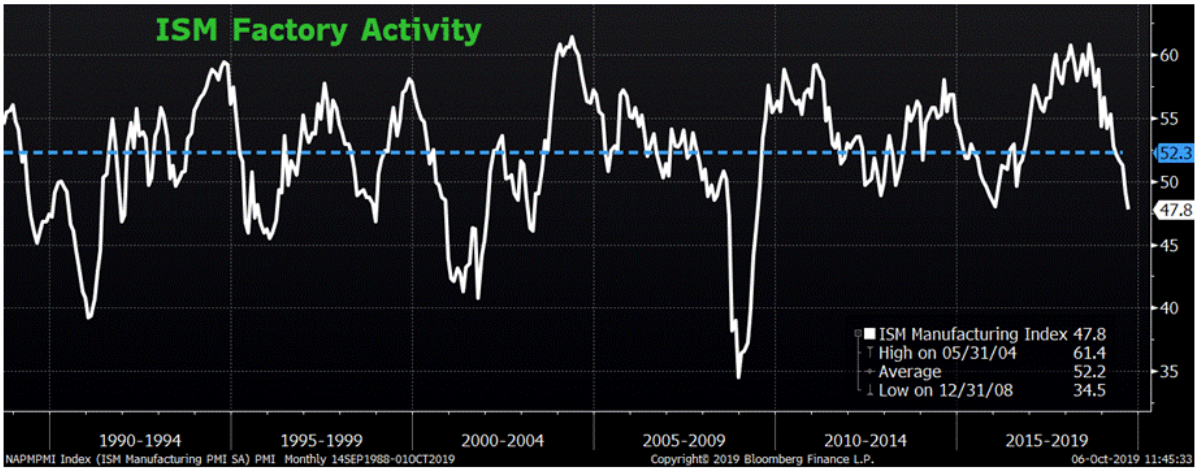
THE PRUDENT SPECULATOR
ISM Manufacturing = 1.5% GDP Growth

The latest read on the health of the manufacturing sector dipped to 47.8 in September. While the measure indicated contraction in the factory sector, manufacturing accounts for around 11% of the U.S. economy, and the Institute for Supply Management stated, "The past relationship between the PMI and the overall economy…corresponds to a 1.5% increase in real gross domestic product (GDP) on an annualized basis."



…and last week's data on housing was hardly recessionary.

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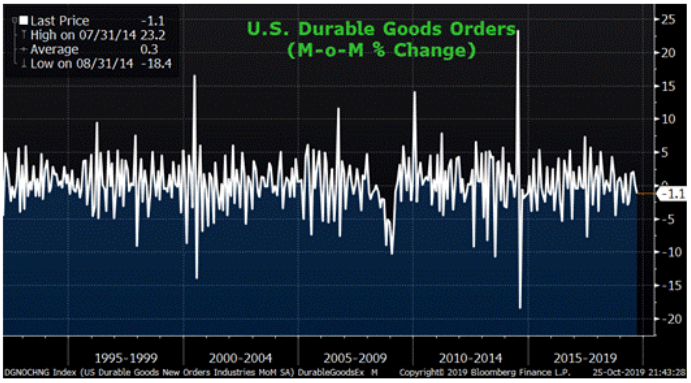
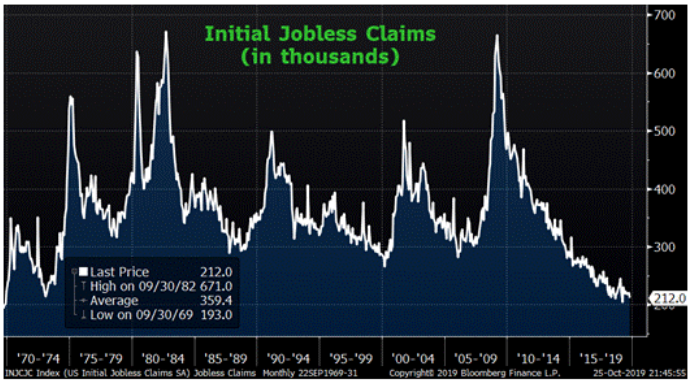
THE PRUDENT SPECULATOR
Solid Housing Numbers

New home sales in September came in at a 701,000 annual rate, beating forecasts and residing near the highest levels since the Financial Crisis. Low mortgage rates and a strong U.S. labor market have bolstered the housing market, though sales of existing homes pulled back a bit last month to an annual rate of 5.38 million, even as the tally in September was up 3.9% on a year-over-year basis, which is the best showing since March 2017.

True, the latest numbers on manufacturing were not exactly robust, but the jobs picture remains extraordinarily healthy.

Mixed Econ Data





The headline number for durable goods orders in September came in weaker than expected, falling 1.1%, with a big drop in commercial aircraft reflecting the Boeing 737 MAX grounding and a smaller dip in motor vehicles due to the General Motors strike the main culprits. On the other hand, first-time filings for unemployment benefits continue near five-decade lows, with the latest week's tally inching down to 212,000.

Anything can happen, economically speaking, while equities will always remain a volatile asset class, but we continue to believe that stocks generally are undervalued, which seems to be a minority viewpoint, if we consider the latest poll of *Barron's Magazine* readers out this past weekend. Believe it or not, with more than 1,000 responses, 53% of those surveyed said that the U.S. stock market is fairly valued, while 42% said it is overvalued and only 5% said it is undervalued.

Certainly, we respect that P/E ratios are elevated, but Value Stocks are presently priced below the level at which, on average, they have traded over the past 24+ years,…

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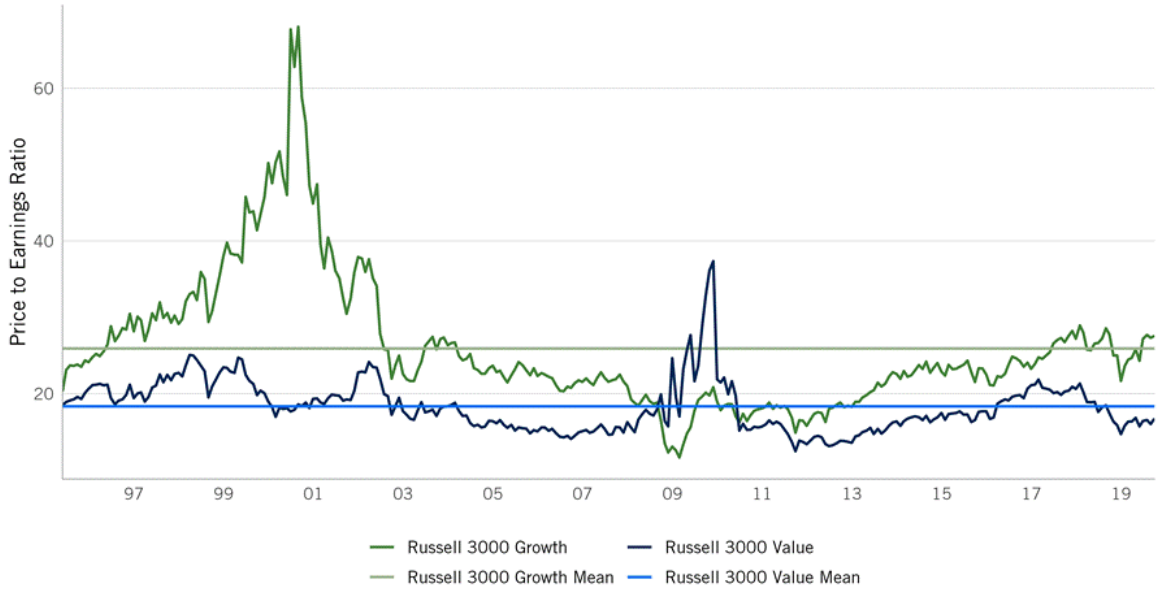
THE PRUDENT SPECULATOR
Valuation Disparity – Price to Earnings

Value stocks are trading below their historical mean on a P/E ratio basis whereas Growth stocks are priced above their much-higher mean.



From 05.31.95 through 09.30.19. SOURCE: Kovitz Investment Group using data from Bloomberg Finance L.P.

…with our portfolios boasting even lower price multiples and sporting higher dividend yields than the broad-based market indexes, not to mention nearly all of the Value gauges.

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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	13.6	12.3	1.1	2.1	3.0
Select Value	14.3	12.7	1.2	2.1	2.6
Select Dividend	14.3	12.8	1.0	2.0	3.2
Select Focused Dividend	13.2	12.3	1.0	2.3	3.3
Select Focused Value	14.3	13.1	1.4	2.4	2.7
Select SMID Dividend	12.9	11.9	0.6	1.6	3.0
Russell 3000	21.3	19.2	2.0	3.2	1.8
Russell 3000 Growth	27.9	24.4	3.0	7.8	1.2
Russell 3000 Value	17.1	15.7	1.5	2.0	2.5
Russell 1000	20.6	18.8	2.2	3.3	1.9
Russell 1000 Growth	26.8	23.5	3.4	8.3	1.2
Russell 1000 Value	16.5	15.5	1.6	2.0	2.6
S&P 500 Index	19.9	18.4	2.2	3.4	1.9
S&P 500 Growth Index	25.1	22.4	3.7	5.6	1.5
S&P 500 Value Index	16.1	15.3	1.5	2.4	2.4
S&P 500 Pure Value Index	12.0	11.1	0.6	1.3	2.8

As of 10.26.19. 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.

Further, we think that investors should not consider equity market valuations in a vacuum as the extraordinarily low interest rate environment boosts the appeal of stocks. After all, back at prior market highs in 2000 and 2007, the yields on money market funds were 6% and 5%, respectively, compared to a “risk-free” rate of 1.73% today.

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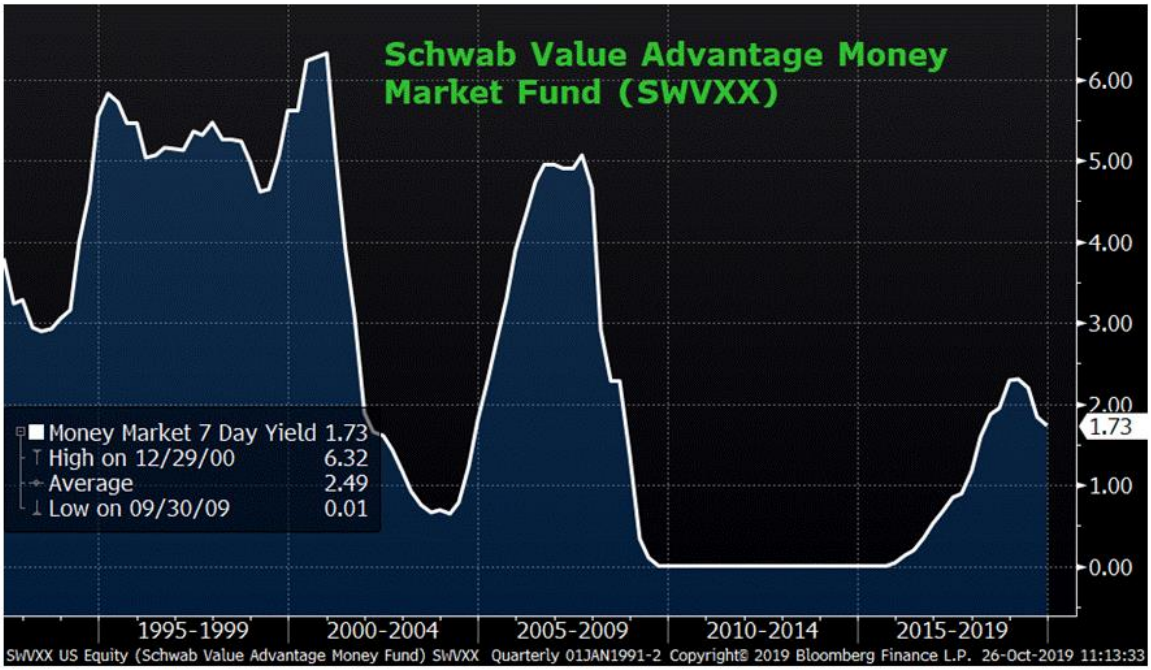
THE PRUDENT SPECULATOR
Money Market Fund Yields Over Time

The yield on the Schwab Value Advantage Fund has moved up sharply of late, but there is a long way to go to approach the 2000 or 2007 levels.



And, if one considers where we stand today versus the prior 42 years dating back to the launch of *The Prudent Speculator* in 1977, a strong case can be made that stocks are about as inexpensive as they have ever been RELATIVE to the yield on the 10-Year U.S. Treasury on both an earnings yield and dividend yield basis!

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THE PRUDENT SPECULATOR
Interest Rates Very Supportive of Stocks

The so-called Fed Model suggests that the yield on 10-Year Treasuries should be similar to the S&P 500 Earnings Yield, which is the inverse of the P/E ratio. If the 10-Year is greater than the S&P Earnings Yield, a market is overvalued and if the reverse is true, as it is today, a market is undervalued. Though some argue that the Fed Model is no longer an effective tool, we like today's relatively rich earnings yield of 5.03%.

Despite our optimism for the long-term, we never forget that ups and downs in the equity markets are very much normal, so we are always braced for inevitable pullbacks, but we know that those that have stuck with stocks through thick and thin very much have been rewarded in the fullness of time!

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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%	108.4%	928	26	3.5	3/9/2009	7/24/2019
17.5%	66.6%	575	38	2.4	12/24/2018	7/26/2019
15.0%	66.3%	559	44	2.1	12/24/2018	7/26/2019
12.5%	43.9%	333	71	1.3	12/24/2018	7/26/2019
10.0%	34.5%	242	97	0.9	12/24/2018	7/26/2019
7.5%	23.4%	148	154	0.6	12/24/2018	7/26/2019
5.0%	14.7%	72	300	0.3	8/14/2019	10/25/2019

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%	-19.5%	103	96	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	299	0.4	7/26/2019	8/14/2019

From 02.20.28 through 10.25.19. 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	13.1%	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	6.1%	7.6%
Long-Term Gov't Bonds	5.6%	8.5%
Intermediate Gov't Bonds	5.1%	4.4%
Treasury Bills	3.3%	0.9%
Inflation	2.9%	1.8%

From 06.30.27 through 08.31.19. 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

Stock Updates

Jason Clark and Chris Quigley offer updates on 16 of our companies that were out with Q3 numbers this past week, the news of sufficient importance to trigger a review of their Target Price. Keep 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/.

Semiconductor equipment firm **Lam Research** (LRCX – $270.05) posted earnings per share of $3.18, versus the $3.05 estimate, in fiscal Q1 2020. LRCX had sales of $2.2 billion (vs. $2.2 billion est.). Since the release, shares have gained nearly 16% on upbeat management commentary.

CEO Tim Archer said, "Our continued execution to commitments, combined with our guidance for the December quarter increases our conviction that Lam is in a strong position to outperform as wafer fabrication equipment spending inflects higher. Doug will cover the financial results in more detail shortly, but I'm especially pleased with the demonstrated earnings power of the company. At the midpoint of our December guide, calendar year 2019 diluted earnings per share will be the second highest in our history, despite the current industry cycle. I would like to take

this opportunity to thank our customers and partners for their continued support of Lam and our employees throughout the world for their contributions to these results."

Mr. Archer added, "We expect to exit 2019 with a bit supply growth rate for NAND of approximately 30%, which is well below our view on long-term demand. And as a result, NAND inventories are expected to decline to normalize levels in the first half of calendar 2020. On the DRAM front, inventories have remained elevated and we do not expect them to reach normalize levels until the second half of 2020." LRCX expects revenue between $2.35 billion and $2.65 billion in Q2, with adjusted EPS between $3.65 and $3.95.

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 nearly $12 billion in calendar 2021. Management said that the buildout of 5G would help LRCX in the near term, as 5G smartphones are expected to "drive content growth." In addition, the Chinese market continues to strengthen, despite the trade tensions with the U.S.

We like the strong balance sheet, while consensus analyst adjusted EPS forecasts for fiscal 2020, 2021 and 2022 now stand at $15.01, $18.28 and $20.46, respectively. Management repurchased $75 million worth of shares in the quarter, leaving $3 billion of the $5 billion share repurchase program that was announced in January. With the stock up 98% YTD, LRCX now trades for 17 times projected earnings, though the dividend yield is still 1.7%. Our Target Price has been hiked to $283, but we are keeping a close eye on this suddenly very popular name.

Semiconductor giant **Intel** (INTC – $56.46) reported earnings per share of $1.42, versus the $1.24 estimate, in fiscal Q3 2019. INTC had sales of $19.2 billion (vs. $18.0 billion est.). Since the release, shares have gained 8.1%, pushing the YTD return above 20%.

CEO Bob Swan commented, "Q3 2019 was the best quarter in our company's history. We generated $19.2 billion in revenue and $1.42 in non-GAAP EPS, exceeding our guidance by $1.2 billion and $0.18, respectively. We achieved record revenue both overall and in our data-centric businesses, while making continued progress on our strategic priorities. Simply put, our ambitions have never been greater. We are growing share in a large and expanding $300 billion market opportunity fueled by the exponential growth of data, which is reshaping computing. As we told you in May, we expect to generate $85 billion in revenue and $6 EPS in 3 to 4 years. But that doesn't happen just by saying it. Achieving this goal means delivering on our operational and financial priorities every 90 days."

Mr. Swan also gave a 10-nanometer update, "The Intel 10-nanometer product era has begun, and our new 10th Gen Core Ice Lake processors are leading the way. As we discussed at the May investor meeting, we are accelerating the pace of process node introductions and moving back to a 2 to 2.5-year cadence. Our process technology and design engineering teams are working closely to ease process design complexity and balance schedule, performance, power and cost. We are on track to launch our first 7-nanometer-based product, a data center-focused discrete GPU, in 2021, 2 years after the launch of 10-nanometer. We are also well down the engineering path on 5-nanometer."

Intel still has significant ground to make up after facing numerous challenges getting 10-nanometer chip to production, but we are keeping our faith. Happily, the shares have rallied most of the way back after dropping by more than 25% between April and May. We also like the company's strong balance sheet and deep bench of talent. We continue to favor the company's diversified revenue stream, low levels of debt, forward P/E ratio below 13 and 2.2% dividend yield. Our Target Price has been increased to $65.

Computing giant **Microsoft** (MSFT – $140.73) earned $1.38 per share in fiscal Q1 2020 (vs. $1.24 est.). MSFT had sales of $33.1 billion, versus the $32.2 billion estimate. Shares gained 3.5% following the announcement, and tacked on a few more dollars in after hours trading on Friday on news that the Pentagon had picked Microsoft over Amazon for a $10 billion cloud-computing contract.

Commenting on the quarter just ended, Microsoft CEO Satya Nadella said, "We're off to a strong start in fiscal 2020, delivering $33 billion in revenue this quarter. Our commercial cloud business continues to grow at scale as we work alongside the world's leading companies to help them build their own digital capability. Microsoft provides a differentiated technology stack spanning application infrastructure, data and AI, developer tools and services, security and compliance, business process, productivity and collaboration."

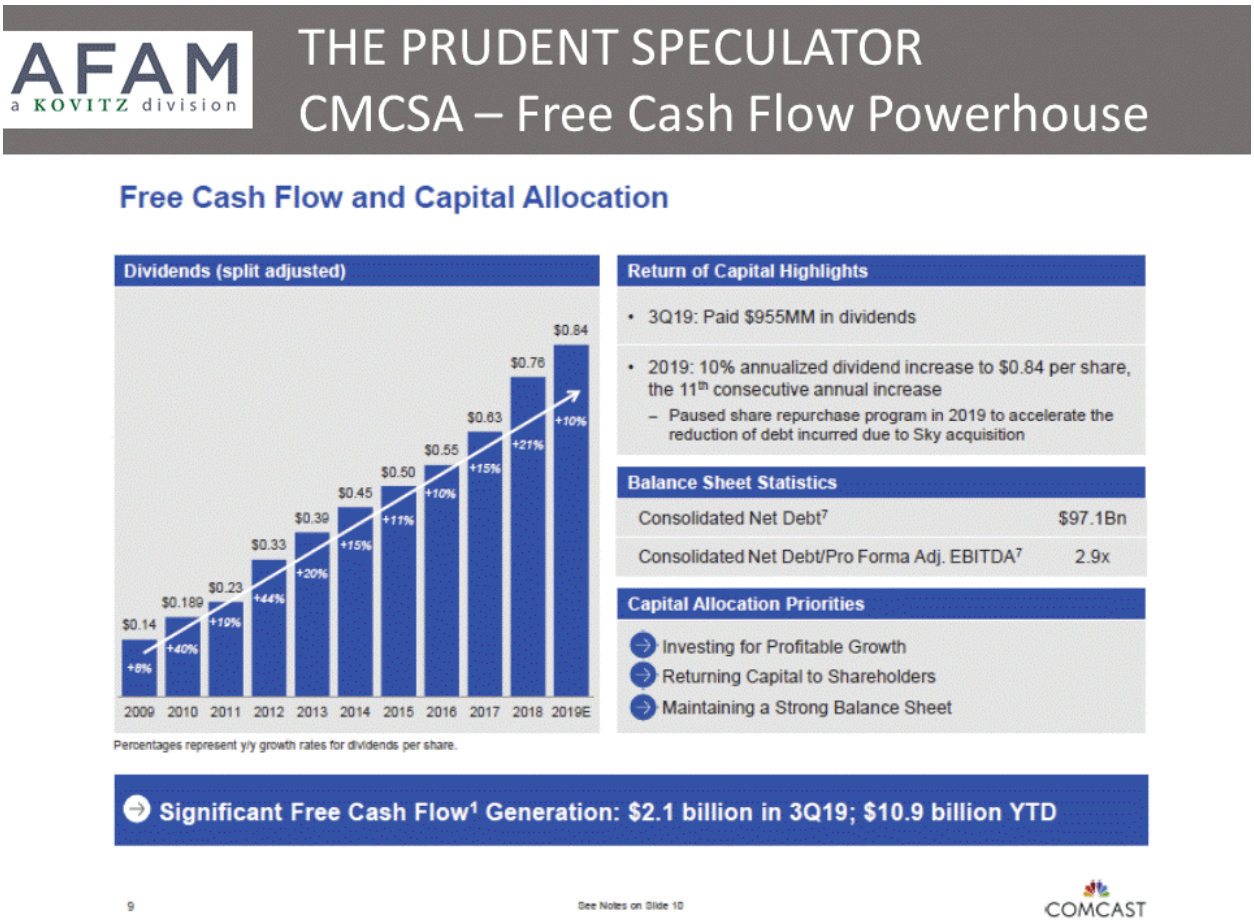
CFO Amy Hood added, “We continue to expect double-digit revenue and operating income growth driven by continued momentum in our commercial business. Given our strong first quarter results and the expected sales mix for the remainder of the year, we now expect operating margins to be up slightly year-over-year even as we continue to invest with significant ambition in high-growth areas.”

MSFT returned $7.9 billion to shareholders via dividends and share repurchases in fiscal Q1. Including dividends, shares have gained more than 40% this year. While performance has been terrific, we continue to believe there are still a host of reasons that Microsoft will continue to fire on all cylinders. In addition, we think MSFT’s valuation is still not excessive, as the stock sports a 3.6% free cash flow yield and a just-increased 1.5% dividend yield. Analysts expect the company’s EPS growth rate to be at least 12% for each of the next three fiscal years, with earnings growing from $3.88 in 2018 to an estimated $6.97 in fiscal 2022, and MSFT still scores well in our quantitative framework. Our Target Price for MSFT has been boosted again, this time to $162.

Media giant **Comcast** (CMCSA – $45.65) earned $0.79 per share in fiscal Q3 2019 (vs. $0.74 est.). CMCSA had revenue of $26.8 billion, versus the $26.8 billion estimate. Shares gyrated up and down and eventually ended unchanged following the announcement.

CEO Brian Roberts said, “We delivered strong operational and financial results in the third quarter with each of our businesses contributing to our company’s growth. Together, we surpassed 55 million customer relationships, grew pro forma EBITDA by 7%, delivered 16% growth in adjusted EPS, generated significant free cash flow and paid nearly $1 billion in dividends while further strengthening our balance sheet. Our results in the quarter and over many years are evidence that our strategy is working. From my perspective, 4 things stood out as we wrapped up the quarter: our incredible strength in broadband; the enduring popularity of our premium content; our strong global footing just 1 year after the Sky acquisition; and how the combination of these things puts us in a unique position to compete, including in the streaming market.”

CFO Michael Cavanagh added, “For the remainder of the year, we have a positive outlook on the ad market with the start of the NFL season and the return of original entertainment programming as well as the benefit from higher upfront pricing. Despite experiencing a crowded box office so far in the second half of this year, we currently expect healthy growth in full year Film EBITDA over 2018 results. Year-to-date, Sky added 317,000 customer relationships, and we expect to return to customer growth in the fourth quarter. For the full year, at today’s currency rates, we expect Sky’s reported EBITDA will be close to $3.1 billion. In addition, in the third quarter, we monetized a substantial portion of the minimum floor value we negotiated for Hulu, which brought in $5.2 billion in proceeds. In addition, starting in 2024, to the extent that total equity value in Hulu is worth more than the total value of $27.5 billion, we will realize our share of that upside.”



We chose to boost our Target Price to $59 as we continue to like the company's overall trajectory, which in our view is propelled by its diverse media portfolio (including NBC, Telemundo, E!, NBC Sports Network, Sky), geographically diverse theme parks (Universal Parks & Resorts, including Universal Studios Hollywood) and investments in alternative methods of content delivery (Hulu). We also like the significant free-cash flow generation, forward P/E ratio below 14 and decent dividend yield of 1.8%.

Benchmark Electronics (BHE – $31.50) turned in solid Q3 results, causing us to bump up our Target Price. The electronic manufacturing services firm announced that its adjusted EPS for the quarter was $0.36 (vs. $0.34 est.). BHE had total revenue of $555.2 million, compared to the $542.0 million estimate.

CEO Jeff Benck stated, "We are pleased with the solid execution of our team in the third quarter. Revenues were up year-over-year in our Medical and Aerospace & Defense (A&D) markets with non-GAAP gross margins improving 60 bps sequentially to 9.5% and operating margins up 10 bps sequentially to 3.2% respectively. We are laying the groundwork for an even stronger Benchmark with the progress our engaged team has made on our strategic priorities which are focused on: improving our go-to-market approach, driving continued operational efficiencies, centralizing our G&A organization, and accelerating our solutions in the market."

Looking ahead, the company said that it expects to generate revenue of $520 million to $570 million in Q4, with adjusted EPS for the three-month period projected to come in between $0.34 to $0.42.

While we only moved our Target Price up to $34, we continue to like that Benchmark is expanding its product offerings and appreciate that it has been pushing for growth outside of its original markets. Along with other EMS (electronics manufacturing services) companies, we expect improving free cash flow generation from slimming inventories and the potential for a U.S.-China trade conflict easing or truce. BHE has a solid balance sheet with plenty of net cash and its shares yield 1.9%.

Shares of **Gilead Sciences** (GILD – $63.32) fell more than 4% Friday following a Q3 earnings release that did not produce a lot of excitement for investors, even as the numbers were actually in line with expectations. The biotech giant posted adjusted EPS of $1.75, versus the consensus analyst estimate of $1.73. Revenue of $5.6 billion matched projections.

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GILD – Hardly an Awful Quarter

Financial Highlights: Q3 2019

in millions, except percentages and per share amounts	Q3 2018	Q2 2019	Q3 2019	YoY Change	QoQ Change
Product Sales	**$5,455**	**$5,607**	**$5,516**	**1%**	**(2%)**
HIV[1]	3,727	4,041	4,202	13%	4%
HCV	902	842	674	(25%)	(20%)
Yescarta	75	120	118	57%	(2%)
Other Products[2]	751	604	522	(30%)	(14%)
Non-GAAP Costs and Expenses[3]	**$2,467**	**$2,645**	**$2,680**	**9%**	**1%**
COGS	771	714	759	(2%)	6%
Product Gross Margin	86%	87%	86%		
R&D	844	916	954	13%	4%
SG&A	852	1,015	967	14%	(5%)
Operating Margin	56%	54%	52%		
Effective Tax Rate	20%	22%	22%		
Non-GAAP Net Income[3]	**$2,403**	**$2,331**	**$2,224**	**(7%)**	**(5%)**
Non-GAAP Diluted EPS[3]	$1.84	$1.82	$1.75	(5%)	(4%)
Shares used in per share calculation-diluted	**1,307**	**1,277**	**1,274**	**(3%)**	**0%**

[1] HIV includes Atripla, Biktarvy, Complera/Eviplera, Descovy, Emtriva, Genvoya, Odefsey, Stribild, revenue share Symtuza, Truvada, and Tybost. Revenue share Symtuza represents Gilead's revenue from cobicistat (C), FTC and TAF in Symtuza (darunavir/C/FTC/TAF), a fixed dose combination product commercialized by Janssen. [2] Other Products include AmBisome, Cayston, Hepsera, Letairis, Ranexa, Vemlidy, Viread, and Zydelig. [3] Non-GAAP financial information excludes acquisition-related, up-front collaboration and licensing, stock-based compensation and other expenses, fair value adjustments of equity securities and discrete tax charges or benefits associated with changes in tax related laws and guidelines.

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CEO Daniel O'Day commented, "I'm very pleased with the progress that we're making on all fronts here at Gilead. Once again, we saw a significant growth in our HIV business, reaching an all-time high in quarterly HIV revenue…We received FDA approval for Descovy earlier this month. This is a really important indication for us as it allows us to extend the benefits of

Descovy to people who are at risk of HIV. To remind you, the approval was based on the DISCOVER trial, which demonstrated that Descovy is just as effective as Truvada and offers advantages in bone and renal safety parameters. We are excited to build on Descovy's status as the most prescribed dual NRTI backbone in the world by advancing its use in PrEP."

Mr. O'Day continued, "Turning to filgotinib, we've now filed for approval of filgotinib in rheumatoid arthritis in the EU and Japan and are on track to complete our filing in the U. S. by the end of the year. Our teams around the world are preparing for launch and I'm encouraged about the potential of filgotinib to be best-in-class among the JAK inhibitors. In addition to rheumatoid arthritis, we're continuing to advance filgotinib together with our partner Galapagos. We have a comprehensive program across a number of other inflammatory diseases, including ulcerative colitis, which we expect to have data on next year."

He concluded, "I'm increasingly optimistic about the future and believe we are well positioned as we enter the last part of the year and look ahead to 2020 and beyond. We will continue to build on our success as we replenish the pipeline and bring the next wave of transformational advances to patients."

No doubt, Gilead will continue to focus on its HIV franchise, where revenue has been growing nicely. The company is also allowing its recent acquisition Kite Pharma to innovate and operate as its own oncology cell therapy unit. With filgotinib coming in 2020, we think that there is still a lot of promise at Gilead. We also might expect the continued strong cash generation to facilitate more acquisitions, additional share buybacks and elevated dividend payouts. GILD shares trade at nine times NTM adjusted EPS consensus projections and carry a divided yield of 4.0%. Our Target Price for GILD has been fine tuned to $97.

Halliburton's (HAL – $20.48) third quarter earnings per share of $0.35 just beat analyst estimates of $0.34. The badly-battered shares rebounded 11% in price last week, thanks in part to the fact that the bottom line was not worse and due to news that the world's second largest oil services company intends to expand international operations while cutting costs domestically. We think the latter is the right move given the current dynamics within the shale space, where exploration and production operators are slashing their capital expenditure budgets to satisfy cash flow objectives. CEO Jeff Miller said that Halliburton had stacked more equipment in this quarter than it did in the previous six months combined. Similar to 2016, where management was able to save $1 billion in costs, the company thinks it can do the same this time around on the back of new technologies across wireline and fracturing services.

Mr. Miller spoke very positively about Halliburton's prospects abroad. The company is finding growth within unconventional, later-cycle well productivity projects, while it continues to execute its traditional drilling and completion contracts. The CEO explained, "In the last couple of years, we've had a significant uptick in unconventional activity in several Middle Eastern countries as well as in Argentina and Australia. Our production enhancement business demonstrated strong international growth year-to-date, benefiting from these developments. Halliburton leveraged our experience in U.S. shales to provide a customized application of technology, logistics management and operational excellence to maximize asset value for our international customers. In Argentina, Halliburton delivered the highest number of frac stages to

date in the third quarter as a result of consistent execution in applying service efficiency best practices in the Vaca Muerta shale play."

Undoubtedly, these remain trying times for those invested in the energy sector. On a positive note, it appears a rebound may finally be gaining traction internationally. Moreover, we believe long-term energy demand growth should offer a tailwind with the global population expected to expand to 9 billion and economic output more than doubling by 2040. While the domestic outlook remains largely uncertain, the company's margins appear to be holding up. At nearly a ten-year low, shares trade at a meaningful discount to our revised Target Price of $49.

Whirlpool (WHR – $159.36) reported earnings last week of $3.97 per share, just ahead of estimates of $3.90. Revenue for the appliance maker came in below expectations at $5.09 billion, versus the $5.13 billion estimate, with the top-line miss causing some investor consternation…for a couple of minutes anyway when trading reopened the day after the results were posted.

After a sizable rebound, the stock did pull back later in the week, but highlights for Q3 included a 5-year contract with D.R. Horton, the largest homebuilder in the United States, solid North American performance, despite weak demand in Canada, and improvement across the Europe, Middle Eastern and Asian operations (EMEA) regions. Within EMEA, Whirlpool operated at

nearly break-even for the quarter, compared to negative-single-digit margins a year ago. As planned, management has fully exited Turkish operations and has completed the sale of South African operations.

The company has also acted to improve the balance sheet while returning capital to shareholders. ”Proceeds from the [Embraco] sale were used to pay off our $1 billion term loan in August, as we previously communicated. This brings our gross debt-to-EBITDA to 2.5, which puts us well on track towards our long-term target of approximately 2.0. Additionally, we completed the sale of our South Africa operations, which is another step forward in our plan to restore the EMEA region to profitability. Lastly, we repurchased $50 million of shares and expect to continue repurchasing shares at moderate levels going forward,” explained CFO James Peters.

While not as inexpensive as this time a year ago, given that the price is up more than 50% over the last 12 months, the stock still trades for less than ten times NTM earnings. We also appreciate the well-covered dividend, with the shares yielding 3.0%. We remain fans of WHR and our Target Price now stands at $201.

Shares of German chemical maker **BASF SE** (BASFY – $19.50) gained 3% after reporting Q3 2019 results, extending the recovery since the stock’s bottom in August. BASF earned $0.24 per share, versus the analyst consensus estimate of $0.22. Revenue totaled $16.9 billion, versus $16.6 billion that analysts were expecting.

CEO Martin Brudermuller said, “In Q3 2019, we basically saw a continuation of the second quarter’s business development. The trade conflicts between the U.S. and China had a continued negative impact. In addition, the uncertainties associated with Brexit reinforced the underlying trend towards an economic slowdown. Europe’s export-oriented countries like Germany are particularly affected. However, the industrial growth in the U.S. is now also beginning to soften considerably. In China, industrial production continued to grow, albeit at a slower pace. Production in the global automotive industry again declined compared with the already low level at the end of the first half of the year.”

Dr. Brudermuller continued, “We are implementing our corporate strategy with full energy, passion and speed to deliver what we promised. We are in the midst of reshaping our organization and reducing complexity. We are streamlining our administration, sharpening the roles of services and regions and simplifying procedures and processes. Increasingly, we start to see cost-reduction effects in the P&L and we notice strong interest on the customer side in the changes and the new BASF. Here are some details: we have embedded significant parts of our functional services into our operating divisions. As of October 1, the embedding of around 20,000 employees was completed. We have defined a lean corporate center to support the Board in steering the BASF Group. As of January 1, 2020, around 1,000 employees will be working in these corporate units. This is less than 1% of BASF’s workforce. The roles of the regions were sharpened to increase the customer focus and to support and enable businesses locally. At the same time, we are simplifying our process landscape and we foster an entrepreneurial performance culture across the whole organization. All these measures have one common goal: To put BASF, with its increased customer focus, back on profitable growth track.”

While we generally view geographic income diversification as a positive, it hasn't worked well recently for BASF, as the company has battled volume headwinds in the big U.S. and European markets, while South America, MENA and Asia Pacific have seen some tailwinds. Fortunately, difficult operating environments are not unusual in the chemicals biz, so we think management will be able to adapt, while the company expects the average oil price to be $65 (Brent), versus $70 in its previous outlook. We think that BASF produces a valuable range of chemicals that are critical in all macroeconomic environments. In addition, we like BASF's strong free cash flow yield, favorable valuation in our proprietary scoring framework and net current yield of 3.3%. Our Target Price has been nudged higher to $28.

Old National Bank (ONB – $18.13) released Q3 earnings that blew away analyst estimates by over 20% ($0.41 vs $0.34). The Midwestern regional bank has been operating at a high level throughout the year despite continued loan payoffs and reduced line utilization in commercial banking. The stock gained 5% on the week, though one might have expected it to be up more.

CEO James Ryan remarked, "We remain focused on improving our operating leverage despite the challenging revenue environment. Operating leverage improved 624 basis points year-over-year, and our adjusted efficiency ratio was a low 55.26%, which improved 341 basis points year-over-year. Exceptional credit quality remains a hallmark of our company with our lower in-house lending limits and diversified mix and a granular loan portfolio. Our average new commercial credit remains well under $1 million despite the record production."

Third-Quarter 2019 Key Performance Indicators

Earnings:
- Record net income increased 36% from a year ago to $69.8mm, or $0.41 per diluted share
- Adjusted net income[1] of $70.5mm, or $0.41 per diluted share, excludes $1.3mm in merger charges

Loans and Deposits[2]:
- Record high commercial production at $680mm; pipeline at $2.0bn
- Total loan outstandings impacted by continued payoffs and lower line utilization in commercial
- Credit quality remains strong with positive migration and net charge-offs of 3 basis points
- Total deposits increased $85.3mm, or 2.4% annualized
  - Low cost of total deposits at 52 bps

Operating Leverage and Expense Management:
- Positive adjusted operating leverage[1] of 624 bps year-over-year
- 17.0% year-over-year increase in adjusted revenue[1]
- 10.8% year-over-year increase in adjusted noninterest expense[1]
- Adjusted efficiency ratio[1] of 55.26% improved 341 bps from the third quarter of 2018

Return Profile:
- Adjusted return on average assets[1] was 1.40%
- Adjusted return on average tangible common equity[1] was 17.16%

Capital Actions:
- 2.2 million shares repurchased at a weighted average price of $16.80 per share, excluding commissions

[1] Non-GAAP financial measure which Management believes is useful in evaluating the financial results of the Company – see Appendix for Non-GAAP reconciliation [2] Based on end-of-period balances

OLD NATIONAL BANCORP 3

We continue to like ONB and its regional focus on Indiana, Wisconsin, Kentucky and Michigan. We view Old National as a quality bank whose management balances a conservative culture with aspirations for growth. ONB remains well capitalized and its shares currently yield 2.9%, while the forward P/E ratio is a reasonable 13.4. Our Target Price for ONB has been raised to $24.

Juniper Networks (JNPR – $25.23), a provider of internet infrastructure, earned $0.48 per share in fiscal Q3 2019 (vs. $0.46 est.). JNPR had revenue of $1.1 billion, versus the $1.1 billion estimate. Shares rose 2.9% following the announcement, as analysts generally reported seeing revenue stability in the results.

CEO Rami Rahim said, “Challenges within the Service Provider business more than offset healthy Cloud and Enterprise sales, both of which grew year-over-year. Non-GAAP earnings per share of $0.48 came in $0.02 above the midpoint of our forecast, as better-than-expected non-GAAP gross margins and strong cost control more than offset the impact from our incremental China tariffs. While we remain on track to deliver our return to year-over-year growth in the December quarter, we are now expecting a lower level of growth than we previously anticipated. The change versus our prior expectations reflects our belief that the Service Provider weakness we experienced over the last few quarters is likely to continue and that our Enterprise momentum will moderate from recent levels based on the order trends we experienced this past quarter. We

believe these dynamics will more than offset the improved momentum we're seeing within our Cloud customers."

Mr. Rahim continued, "Longer term, I believe the investments we are making in our go-to-market organization, along with the products and innovations we are bringing to market, are the right ones and should position us to deliver return to modest growth next year. I would like to extend my thanks to our customers, partners and shareholders for their continued support and confidence in Juniper. I especially want to thank our employees for their hard work and dedication, which is essential to creating value for our stakeholders."

CFO Ken Miller added, "Our revenue outlook shows a modest return to year-over-year growth at the midpoint. However, it is lower than previously expected due to continued business challenges at some of our largest Service Provider customers, the lingering impacts from our sales force transformation and macroeconomic uncertainty. We remain confident in our position in the markets we serve and in our relationships with our customers. Our fourth quarter 2019 non-GAAP gross margin guidance reflects the recent increase in China tariffs, which is offset partially by the expected increase in revenue. We continue to undertake specific efforts to improve our gross margin. These efforts include value engineering, optimizing our supply chain and service business, pricing management and increased software and solution sales. Despite the lower-than-expected revenue outlook, we continue to manage costs prudently and still expect to achieve the low end of our $1.70 to $1.80 earnings range for the full year 2019. Our Board of Directors has approved an additional $1 billion of share repurchase authorization, which brings our current authorization to $1.9 billion."

We were pleased to see revenue stability come into play, even if there's some lingering uncertainty related to JNPR's growth pipeline. Cloud customers continue to be of chief importance to JNPR, as the restructuring of the sales force is a move we view positively despite the initial cost. JNPR now trades with a forward P/E less than 14, much lower than the broader S&P 500 Information Technology sector's roughly 21 times, and yields a rich (for a tech stock) 3.0%. Our Target Price remains $36.

Despite reporting Q3 results below consensus analyst estimates, shares of construction and mining equipment maker **Caterpillar** (CAT – $139.73) rallied almost 6% on the news, evidently because investors were thinking the numbers might be worse, though potential movement in the trade talks with China likely also played a role. Of course, the stock initially cratered on the earnings news, before a terrific rebound and rally ensued.

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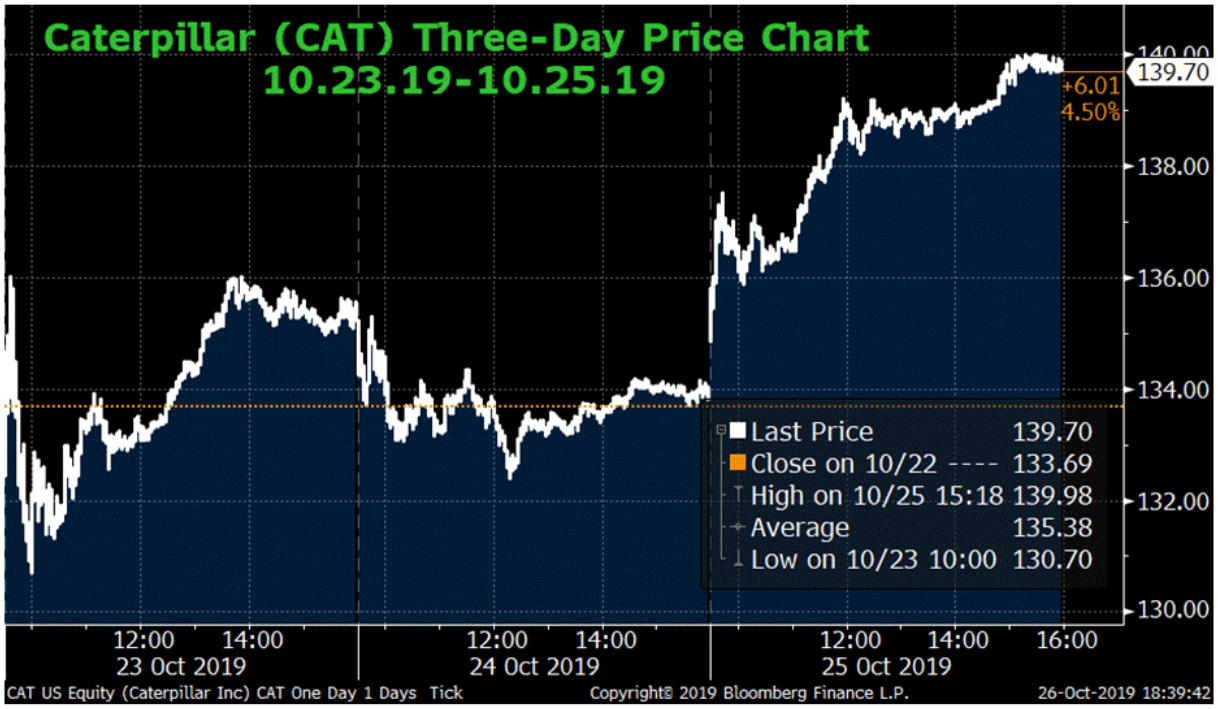
THE PRUDENT SPECULATOR
CAT – Upon Further Review Q3 Not so Bad



For the quarter, CAT reported adjusted EPS of $2.66, versus forecasts of $2.87. Revenue came in at $12.76 billion, 5% below expectations. During Q3, uncertainty due to trade tensions led Caterpillar's independent dealers to reduce inventories by $400 million, despite a 6% increase in quarterly retail sales. "Our volumes declined as dealers reduced their inventories, and end-user demand, while positive, was lower than our expectations," said CEO Jim Umpleby. "We remain focused on executing our strategy and continuing to achieve our Investor Day targets for margin improvement and free cash flow."

The company is lowering its full-year profit per share outlook range to $10.90 to $11.40, compared to the previous outlook which was at the low end of the $12.06 to $13.06 range. The revised guidance now assumes modestly lower sales in 2019. Management said it remains focused on maintaining a competitive and flexible cost structure, including managing production levels.

"In the fourth quarter, we now expect end-user demand to be flat and dealers to make further inventory reductions due to global economic uncertainty," explained Mr. Umpleby. "Caterpillar's improved lead times, along with these dealer inventory reductions, will enable us to respond quickly to positive or negative developments in the global economy in 2020. We are expanding our offerings and investing in services, including digital capabilities, to drive long-

term profitable growth, while continuing to achieve our Investor Day targets for improved financial performance."

CAT continues to have a dominant share in the U.S. market and is making headway in emerging economies such as China, India, Africa and the Middle East. While operational hurdles remain and aren't likely to disappear tomorrow, we like that management is focused on doubling its aftermarket part and service business by 2025. We also think there is potential for increased global infrastructure spending and that it could be an election year topic. With leaner operations, almost $7.9 billion in cash and billions more in free cash flow expected over the next few years, we see CAT being able to withstand changing business environments, becoming more aggressive in buying back shares and boosting the dividend (yield is 2.9%). Our Target Price for CAT is now $178.

Shares of **Albemarle** (ALB – $63.59) plunged last week after reporting weaker-than-expected preliminary Q3 results and cutting its full-year financial forecasts. The specialty chemical company said that it will post quarterly adjusted EPS of $1.53, versus expectations of $1.64. For the full-year, management said it now expects adjusted EPS of $6.00 to $6.20, versus the $6.25 to $6.65 that had been previously announced. Additionally, revenue for the full-year is now expected to come in between $3.6 billion and $3.7 billion, versus prior projections of $3.65 billion and $3.85 billion. The guidance cut comes as a result of higher lithium costs and lower lithium prices. The higher costs are primarily due to a delay in ramping up new production capacity in Chile. The bigger near-term concern is the continued move down in lithium prices.

"Despite one-time items impacting our third quarter results and challenging market conditions heading into 2020, we remain confident in the long-term growth prospects of lithium. We believe we have built a competitively advantaged position that will enable us to grow well into the future," said CEO Luke Kissam. "While disappointed by third quarter performance in an otherwise strong year, we continue to put more robust processes in place to ensure greater operational rigor. To that end, we are initiating a program aimed at capturing significant and sustainable cost savings over the next two years."

Our experience during our brief ownership history of Albemarle has not been good, to say the least, but we are long-term-oriented investors and patience has always been key to our success. While there is no guarantee, of course, that ALB will turn around, we think that over the long-term the stock has a major positive catalyst in lithium batteries as electric vehicle adoption continues to increase and the world's leading car companies race to get desirable EVs to market. In addition, lithium is used in backup and storage batteries for the power grid.

Albemarle also generates healthy profits from bromine, which is primarily used in flame retardants. While demand for bromine has slipped in TVs and computers, it has risen for servers and automobile electronics. Further, ALB generates steady cash flows from its refining catalyst business. Despite the promising growth potential, ALB shares are trading for just 10 times the revised full-year EPS guidance and yielding 2.3%. Our Target Price has been cut to $112.

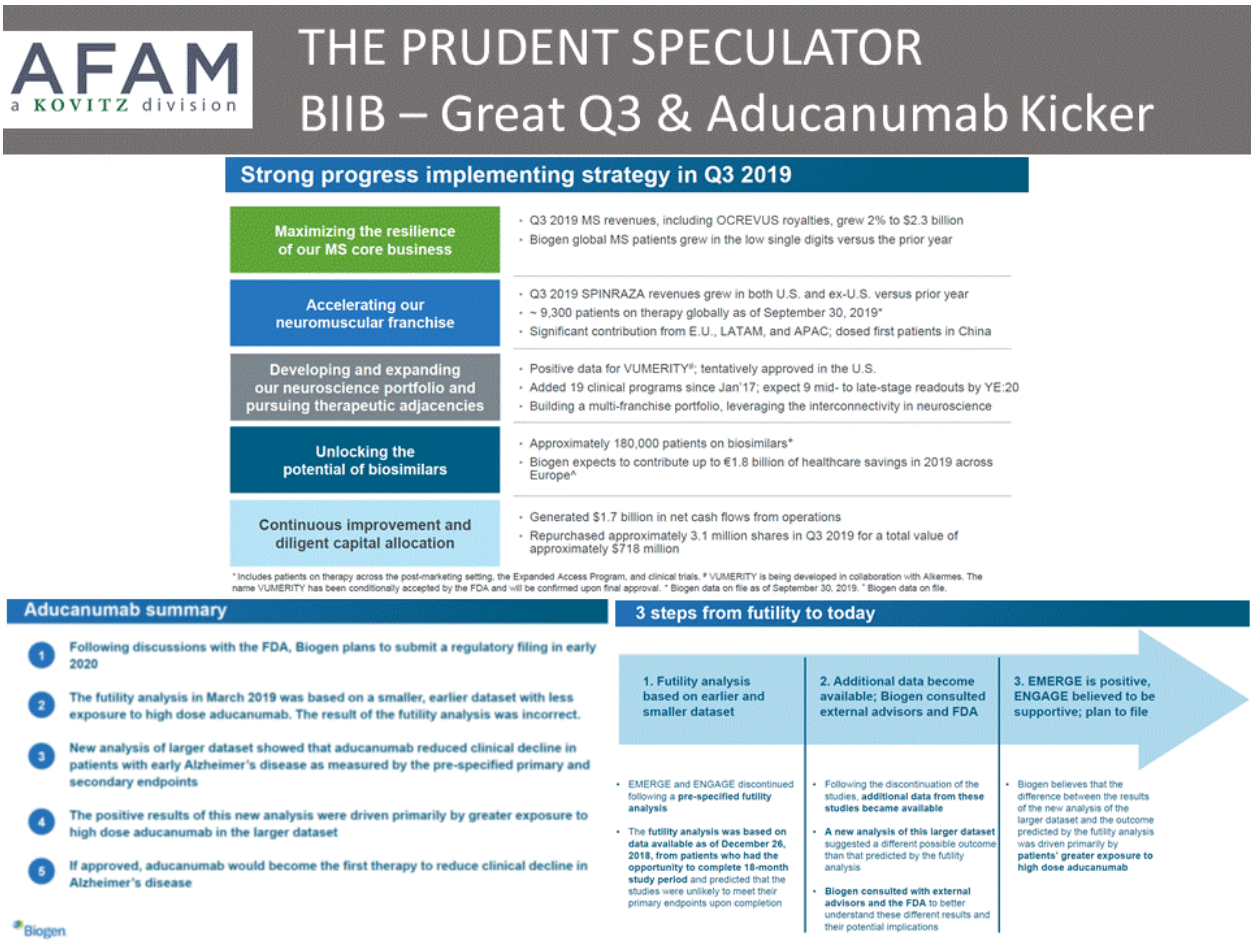
Shares of **Biogen** (BIIB – $288.04) jumped more than 30% last week after the biotech giant reported a surprising turn of events in regard to its Alzheimer's drug. Management said that after

consulting with the U.S. Food and Drug Administration (FDA), Biogen plans to pursue regulatory approval for aducanumab, an investigational treatment for early Alzheimer's disease. The company said, "Our Phase 3 EMERGE Study met its primary endpoint showing a significant reduction in clinical decline, and Biogen believes that results from a subset of patients in the Phase 3 ENGAGE Study who received sufficient exposure to high dose aducanumab support the findings from EMERGE. Patients who received aducanumab experienced significant benefits on measures of cognition and function such as memory, orientation, and language. Patients also experienced benefits on activities of daily living including conducting personal finances, performing household chores such as cleaning, shopping, and doing laundry, and independently traveling out of the home. If approved, aducanumab would become the first therapy to reduce the clinical decline of Alzheimer's disease and would also be the first therapy to demonstrate that removing amyloid beta resulted in better clinical outcomes."

"With such a devastating disease that affects tens of millions worldwide, today's announcement is truly heartening in the fight against Alzheimer's. This is the result of groundbreaking research and is a testament to Biogen's steadfast determination to follow the science and do the right thing for patients," said CEO Michel Vounatsos. "We are hopeful about the prospect of offering patients the first therapy to reduce the clinical decline of Alzheimer's disease and the potential implication of these results for similar approaches targeting amyloid beta."

Almost ignored, given the aducanumab news, BIIB also reported excellent Q3 financial results. The company turned in adjusted EPS of $9.17, versus the consensus analyst estimate of $8.27. Revenue for the period came in at $3.6 billion, versus forecasts looking for $3.54 billion.

"Biogen delivered solid performance in the third quarter driven by continued resilience from our MS core business and growth from SPINRAZA and biosimilars," Mr. Vounatsos commented. "SPINRAZA continued on a strong trajectory, particularly outside the U.S., and we are preparing for the expected launch of VUMERITY, which we believe will be an important addition to our market-leading multiple sclerosis portfolio. In addition to the recent news on aducanumab, we made strong progress in our pipeline as we initiated new clinical programs targeting Parkinson's disease and brain contusion, and we look forward to nine important data readouts by the end of next year. We continue to believe that our core focus on neuroscience will lead to new innovative treatments for patients and will maximize long-term returns for our shareholders."



Versus the news in March that Biogen was going to discontinue work on aducanumab, the new update was stunning. If approved, this drug could end up being one of the biggest pharmaceuticals ever, though we realize that there is a long way to go before the FDA allows aducanumab to come to market. No doubt, there will be plenty of stock price volatility as news flows out, but independent of the Alzheimer's potential, we like that Biogen is still generating strong free cash flow which can aid in strengthening a pipeline that we already think has solid long-term potential keying on cancer and neurology disorders. All are important because BIIB still faces looming pressure from generics in the coming years for its MS drug Tecfidera and potential competition from Novartis for its spinal muscular atrophy treatment Spinraza. Even after the big jump, Biogen shares trade for less than 9 times NTM adjusted earnings expectations. Our Target Price has soared to $460.

Alaska Air Group (ALK – $71.57), a Seattle-based airline that operates primarily on the West Coast, reported earnings per share of $2.63, versus the $2.50 estimate, in fiscal Q3 2019. ALK had total revenue of $2.4 billion, matching the consensus estimate. Shares climbed 4.5% following the announcement.

CEO Brad Tilden commented, "We carried a record number of guests this past summer. Our team's full focus has returned to running a great airline and it is showing. I'd like to share 2 recent achievements: first, our people were once again recognized as the best U.S. Airline by

Condé Nast Traveler in its annual Reader's Choice Awards. This is the second year in a row that we won this award, and we're continuing an 11-year run that Virgin America had before us. We can't thank our employees enough for their skill and dedication in serving our guests; and second, 3 important labor deals, which represent over 6,000 of our people were ratified this quarter. We're proud to get these deals done for our folks."

Mr. Tilden added, "If you've done the math on our recent guidance, you've likely estimated that our 2019 margins will be somewhere around 11% to 12%, up from just below 9% last year. We're encouraged by our progress, but we do not believe we're at the destination. On the subject of ROIC, we expect to end 2019 in the range of 12% to 13%, which is up significantly from 9.4% last year. As we look beyond 2019, we're developing plans that will put us into our stated pretax margin range of 13% to 15% over the business cycle."

Alaska expects RASM (revenue per available seat mile) to increase 1% to 4% in Q4, compared with what the airline characterized as "harder comps" from Q4 last year. CFO Brandon Pedersen said, "During the quarter, we bought back $28 million of our shares, including $10 million over a 2-day period at a volume weighted average price of around $58 per share. With the dividend, which we have increased 6x since we initiated it in 2013, we expect to return $248 million to our shareholders this year or more than 25% of our free cash flow. Coming back to our 5-year plan, our fortress balance sheet positions us to substantially increase returns to our owners and/or place an aircraft order that would fund growth and allow us to retire smaller less efficient aircraft, which should improve — which would improve both our ability to generate additional revenue and lower unit costs. As we finish up our long-term fleet study, we're also developing an order strategy that allows us to best leverage our market position and structure delivery timing that preserves our ability to generate free cash flow."

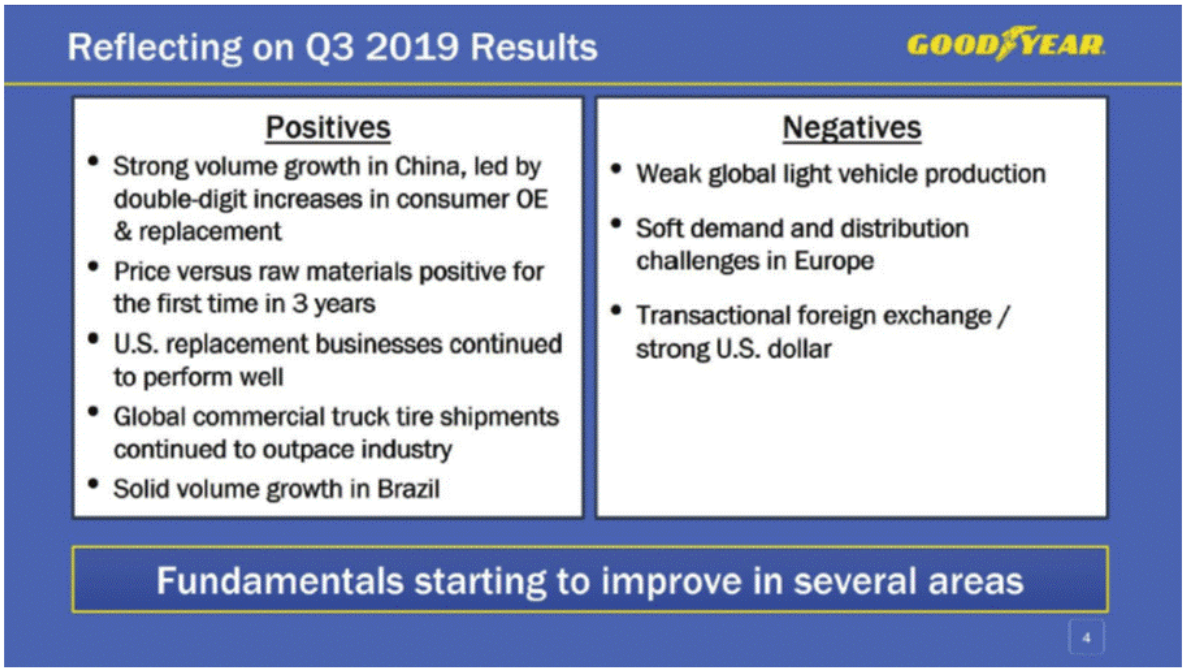
We think that ALK continues to put itself in a strong position, from both competitive and passenger experience standpoints. Indeed, the company has a strong balance sheet (especially for an airline) and has made partnership moves that best support its schedule and services. While there are occasional consolidation rumors (last week, a Stifel analyst suggested Southwest should buy JetBlue or Alaska), we think those are far-fetched, on operational and regulatory grounds. ALK trades for less than 11 times NTM earnings and yields 2.0%. Our Target Price has been elevated to $95.

Shares of **Goodyear Tire** (GT – $16.56) continued their strong rebound off of the early September lows, jumping more than 9% on Friday despite the tire maker reporting Q3 financial results that came in below consensus expectations. For the period, GT delivered adjusted EPS of $0.45 (est. $0.52) on revenue of $3.8 billion, which lagged forecasts by more than 3%. Despite the miss, it seemed investors were expecting much worse given recent disappointing results, though it was fascinating to see this news story out Friday morning, "Shares fall 9% in pre-market trading to $13.77 on 25,198 shares traded." It would seem that sometimes trading outside of normal market hours can be hazardous to one's wealth!

In regard to the Q3 results, CEO Richard J. Kramer commented, "In the Americas, we saw continued strength in our U.S. consumer replacement business and solid growth in Brazil, giving us positive momentum in these important markets as we head into the final months of the year.

Our Asia Pacific business improved in the quarter as we benefitted from the launch of several new OE fitments in China, which helped mitigate the impact of lower auto production. This is a testament to the strength of our technology and our success winning fitments on the right platforms."

He added, "Industry conditions were softer than we anticipated in Europe and we continued to see an adverse impact from lack of alignment in our distribution channels. In response, we expect to accelerate our plans to rationalize distribution in the region. These actions, which will begin early next year, should improve the focus on our brands and ensure that we capture the full benefits of the investments we are making to increase the supply of premium, high margin tires over the next few years."



After weak Q2 numbers, we wrote that we weren't ready to give up on GT yet, and we still aren't. We feel we are fairly close to the bottom of the cycle, coming comparisons are going to be easier and input costs are seemingly retreating with lower oil prices (as more than 60% of the company's raw materials costs are petroleum-based). Even with the snap back, GT's shares are still down almost 20% this year. Additionally, consensus analyst adjusted EPS estimates for 2020 and 2021 now stand at $2.21 and $2.31. While we remain patient, our patience isn't permanent, even as we appreciate management's ongoing efforts to restructure factories in Europe, modernize infrastructure, reduce headcount and adjust production volume to higher-

margin tires. True, trade tensions with China and Europe can keep headwinds elevated, but GT now trades for less than 8 times arguably trough earnings and yields 3.9%. Our Target Price now stands at $23.