Market Commentary Monday, September 14, 2020

September 14, 2020

EXECUTIVE SUMMARY

Week in Review – Equities Head South
Volatility – Selloffs Part of the Game
Market of Stocks – Value Outperforming in September
History Lesson – Value Has Performed Well Coming Out of Recession
Econ News – Q3 GDP Growth Estimates Continue to Rise
Interest Rates – Low Rates Support Equities
Inflation – Value & Dividend Payers Have Performed Well When Consumer Prices are Rising
Sentiment – Big Plunge in Bulls and Big Jump in Bears
Earnings – EPS Expected to Rebound in 2021 and Beyond
Stock News – Updates on LRCX, NLOK, C, GM, KR & ORCL

Market Review

While Friday saw a decent bounce, for many stocks, the September swoon continued last week, with tech companies generally leading the way lower. The Nasdaq Composite fell 4.06%, while the S&P 500 and Russell 3000 dropped 2.49% and 2.53%, respectively. Happily, the Russell 3000 Value index dipped "only" 1.60%, compared to a 3.38% pullback for the Russell 3000 Growth index.

To be sure, nobody is ever going to be thrilled about red ink, but trips south are an inevitable and healthy part of the process for an asset class that has produced stellar long-term returns. In fact, the current 6.95% decline in the S&P 500 since the all-time high on September 2 is now setback number 304 of 5% without a subsequent gain of 5% over the last nine decades and is the fifth such occurrence this year alone.

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%	111.3%	977	27	3.4	3/23/2020	9/2/2020
17.5%	66.8%	570	39	2.3	3/23/2020	9/2/2020
15.0%	66.5%	555	45	2.0	3/23/2020	9/2/2020
12.5%	44.3%	333	72	1.3	3/23/2020	9/2/2020
10.0%	34.9%	244	98	0.9	3/23/2020	9/2/2020
7.5%	23.7%	148	156	0.6	3/23/2020	9/2/2020
5.0%	14.8%	72	304	0.3	6/11/2020	9/2/2020

Declining Markets

Minimum Decline %	Average Loss	Average # Days	Count	Frequency (in Years)	Last Start	Last End
-20.0%	-35.4%	286	26	3.5	2/19/2020	3/23/2020
-17.5%	-30.4%	217	38	2.4	2/19/2020	3/23/2020
-15.0%	-28.4%	189	44	2.1	2/19/2020	3/23/2020
-12.5%	-22.8%	138	71	1.3	2/19/2020	3/23/2020
-10.0%	-19.6%	102	97	0.9	2/19/2020	3/23/2020
-7.5%	-15.5%	65	155	0.6	3/13/2020	3/23/2020
-5.0%	-10.9%	36	304	0.3	9/2/2020	9/8/2020

From 02.20.28 through 09.08.20. 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 using data from Bloomberg, Morningstar and Ibbotson Associates

LONG-TERM RETURNS

	Annualized Return	Standard Deviation
Value Stocks	12.7%	26.0%
Growth Stocks	9.6%	21.5%
Dividend Paying Stocks	10.4%	18.1%
Non-Dividend Paying Stocks	8.9%	29.4%
Long-Term Corporate Bonds	6.2%	7.6%
Long-Term Gov't Bonds	5.7%	8.6%
Intermediate Gov't Bonds	5.1%	4.3%
Treasury Bills	3.3%	0.9%
Inflation	2.9%	1.8%

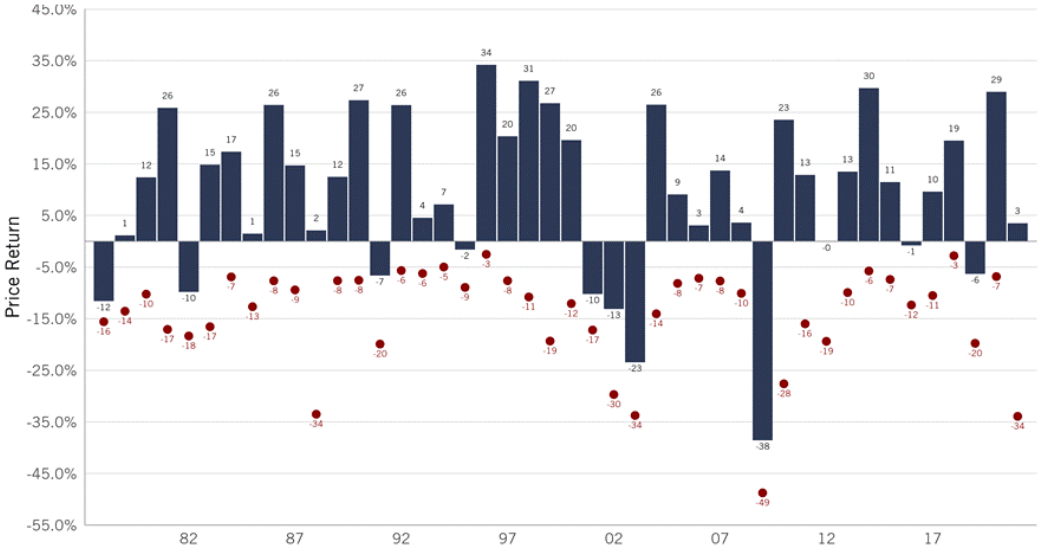
From 06.30.27 through 06.30.20. Growth stocks = 50% Fama-French small growth and 50% Fama-French large growth returns rebalanced monthly. Value stocks = 50% Fama-French small value and 50% Fama-French large value returns rebalanced monthly. The portfolios are formed on Book Equity/Market Equity at the 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 using data from Professors Eugene F. Fama and Kenneth R. French and Ibbotson Associates

Obviously, most years, including 2020, have witnessed far bigger pullbacks than the present one,…

THE PRUDENT SPECULATOR

A BIG SELLOFF HAPPENS ALMOST EVERY YEAR

While the S&P 500 has enjoyed excellent long-term returns and endured a relatively small number of negative full years since the founding of *The Prudent Speculator* in 1977, there have been corrections of 10% or more in 27 of the 44 years, including a 34% one (on a closing basis) this year.



From 12.31.76 through 09.11.20. Price returns do not include dividends. Intra-year drops refer to the largest drops between high and low close prices during a calendar year. 2019 return is year to date. SOURCE: Kovitz using data from Bloomberg Finance L.P.

…so we would not be surprised to see the latest selloff carry further, but we are pleased to see inexpensively priced stocks generally hold up much better this time around.

THE PRUDENT SPECULATOR

MARKET OF STOCKS – UPSIDE DOWN IN SEPTEMBER

Russell 3000 Index September

8.31.20 to 9.11.20 Performance Data

Company	Weight (%)	Contribution to Return (%)	Total Return (%)	2021 Forward P/E Ratio
Winners				
788 Advancers	**18.99**	**0.51**		
Zoom Video	0.19	0.03	17.8	153.2
Nike	0.41	0.02	5.5	39.6
Caterpillar	0.24	0.02	8.1	21.1
Coca-Cola	0.57	0.02	3.1	24.7
Broadcom	0.41	0.01	3.6	15.8
Uber Technologies	0.14	0.01	10.0	-28.4
Dow Inc	0.11	0.01	10.5	21.7
McDonald's	0.47	0.01	2.1	26.8
Fedex	0.16	0.01	6.2	19.4
Sherwin-Williams	0.17	0.01	5.6	28.3
Union Pacific	0.39	0.01	1.8	21.4
JPMorgan Chase	0.91	0.01	0.9	11.5
Top 12 Total	**4.15**	**0.16**		
Losers				
2208 Decliners	**81.01**	**-5.26**		
Netflix	0.65	-0.06	-9.0	50.7
PayPal Holdings	0.69	-0.07	-9.9	40.7
Mastercard	0.90	-0.07	-7.8	37.9
Salesforce.com	0.67	-0.07	-10.8	66.4
Nvidia	0.90	-0.08	-9.0	44.7
Alphabet Inc-Cl C	1.41	-0.10	-6.9	23.3
Alphabet Inc-Cl A	1.42	-0.10	-7.0	23.2
Facebook	2.02	-0.19	-9.1	23.9
Tesla	0.90	-0.26	-25.2	111.9
Amazon.com	4.18	-0.41	-9.7	51.9
Microsoft	4.79	-0.47	-9.5	29.8
Apple	5.91	-0.80	-13.2	33.5
Bottom 12 Total	**24.43**	**-2.69**		
Russell 3000 Index TR			**-4.75**	
Russell 3000 Index Average Stock TR			**-3.32**	

Source: Kovitz using data from Bloomberg

Russell 3000 Index Year-to-Date

12.31.19 to 9.11.20 Performance Data

Company	Weight (%)	Contribution to Return (%)	Total Return (%)	2021 Forward P/E Ratio
Winners				
1053 Advancers	**59.84**	**15.71**		
Apple	4.69	2.05	53.6	33.5
Amazon.com	3.41	1.92	68.6	51.9
Microsoft	4.60	1.33	30.4	29.8
Tesla	0.47	0.69	345.5	111.9
Facebook	1.72	0.52	29.9	23.9
Nvidia	0.65	0.51	107.1	44.7
PayPal Holdings	0.55	0.32	70.1	40.7
Netflix	0.59	0.24	49.0	50.7
Adobe	0.62	0.23	42.9	42.0
Home Depot	0.85	0.23	28.9	23.3
Salesforce.com	0.51	0.22	49.5	66.4
Alphabet Inc-Cl C	1.39	0.18	13.7	23.3
Top 12 Total	**20.05**	**8.44**		
Losers				
2170 Decliners	**40.16**	**-11.50**		
ConocoPhillips	0.16	-0.11	-47.7	50.2
US Bancorp	0.19	-0.11	-36.7	12.8
Raytheon Technologies	0.32	-0.12	-29.9	16.2
General Electric	0.23	-0.16	-46.5	18.0
Citigroup	0.39	-0.22	-34.3	8.4
Chevron	0.58	-0.23	-32.9	27.6
AT&T Inc	0.78	-0.25	-22.1	9.0
Bank of America	0.70	-0.26	-26.1	11.9
Boeing	0.35	-0.31	-50.5	38.5
Wells Fargo	0.40	-0.38	-53.3	11.5
JPMorgan Chase	1.09	-0.39	-25.5	11.5
Exxon Mobil	0.67	-0.41	-44.2	24.1
Bottom 12 Total	**5.87**	**-2.95**		
Russell 3000 Index TR			**4.20**	
Russell 3000 Index Average Stock TR			**-7.61**	

Source: Kovitz using data from Bloomberg

Indeed, though the returns race remains still decidedly lopsided in favor of more richly valued names for the full year, the Russell 3000 Value index has outperformed the Russell 3000 Growth index by 526 basis points (5.26%) thus far in September. Obviously, there is a long way to go before Value reasserts its historical performance advantage, but we sleep much better at night knowing that our portfolios are reasonably priced in term of their price metrics, with generous dividend yields providing healthy income streams.

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	17.1	14.4	0.9	1.9	2.7
ValuePlus	18.6	15.3	1.1	1.9	2.4
Dividend Income	16.8	14.6	0.8	2.0	3.1
Focused Dividend Income	17.1	14.9	1.0	2.2	2.9
Focused ValuePlus	18.5	16.1	1.4	2.2	2.5
Small-Mid Dividend Value	14.3	13.8	0.5	1.3	2.9
Russell 3000	29.0	27.8	2.3	3.5	1.7
Russell 3000 Growth	42.1	35.1	4.3	10.6	0.9
Russell 3000 Value	21.8	22.6	1.5	2.0	2.6
Russell 1000	27.5	26.7	2.5	3.7	1.7
Russell 1000 Growth	38.6	33.4	4.5	11.4	0.9
Russell 1000 Value	20.9	21.9	1.6	2.1	2.6
S&P 500 Index	26.0	25.5	2.5	3.8	1.8
S&P 500 Growth Index	33.5	30.8	4.7	7.9	1.1
S&P 500 Value Index	19.4	20.2	1.4	2.1	2.9
S&P 500 Pure Value Index	16.6	23.2	0.5	0.9	3.3

As of 09.13.20. 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 using data from Bloomberg Finance L.P.

Further, we like that Value stocks have performed best coming out of recession,…

VALUE STOCKS HAVE OUTPERFORMED COMING OUT OF RECESSION

U.S. Recession Trough (per NBER) & Equity Returns

S&P 500 and Fama/French Value Performance

Recession Trough Date	1 Year Post S&P 500 TR	1 Year Post FF Value TR	1 Year Post FF Growth TR	3 Year Post S&P 500 TR	3 Year Post FF Value TR	3 Year Post FF Growth TR	5 Year Post S&P 500 TR	5 Year Post FF Value TR	5 Year Post FF Growth TR
Mar-33	81.5%	88.7%	82.9%	155.7%	135.3%	169.1%	62.4%	69.5%	96.2%
Jun-38	-1.7%	-14.5%	2.7%	0.8%	4.6%	14.5%	43.9%	129.3%	65.5%
Oct-45	-7.2%	-2.2%	-6.8%	14.7%	26.6%	-1.3%	64.8%	76.2%	38.5%
Oct-49	35.1%	43.8%	29.9%	92.8%	96.5%	66.3%	177.8%	174.6%	131.2%
May-54	36.1%	60.2%	34.4%	83.7%	95.5%	69.4%	145.2%	200.3%	143.0%
Apr-58	37.2%	61.0%	51.4%	66.4%	94.4%	86.4%	89.9%	128.4%	84.1%
Feb-61	13.6%	16.9%	8.6%	35.2%	49.1%	12.1%	68.4%	137.0%	55.6%
Nov-70	11.2%	11.0%	20.5%	20.6%	13.5%	-0.7%	25.1%	44.4%	1.5%
Mar-75	28.3%	51.5%	31.3%	22.1%	98.6%	44.4%	55.6%	157.8%	96.9%
Jul-80	13.0%	22.9%	22.8%	56.1%	113.6%	69.7%	100.5%	207.7%	75.2%
Nov-82	25.6%	39.8%	21.1%	66.8%	99.7%	36.4%	103.0%	123.9%	38.2%
Mar-91	11.0%	25.5%	16.7%	29.8%	73.2%	25.8%	98.0%	154.7%	82.9%
Nov-01	-16.5%	-11.9%	-18.5%	8.4%	39.8%	13.7%	34.3%	93.7%	33.5%
Jun-09	14.4%	25.5%	14.7%	57.7%	53.2%	62.3%	136.9%	158.2%	140.8%
Averages	**20.1%**	**29.9%**	**22.3%**	**50.8%**	**71.0%**	**47.7%**	**86.1%**	**132.6%**	**77.4%**

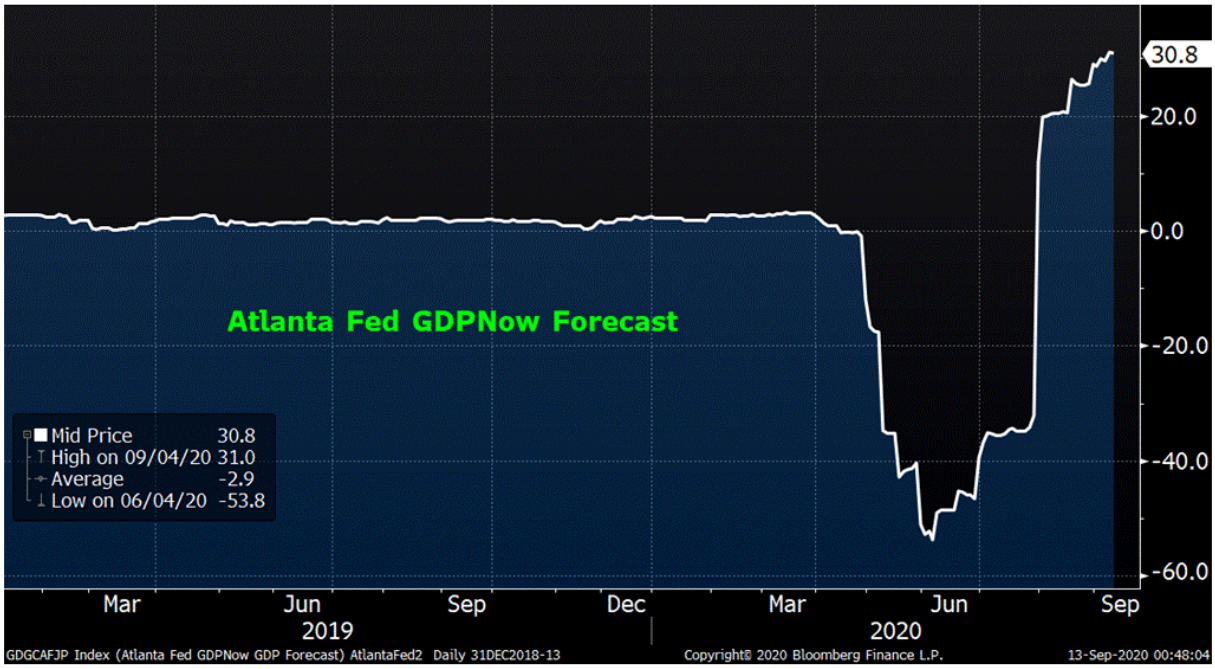
Source: Kovitz Investment Group using data from Bloomberg, Professors Eugene F. Fama & Kenneth R. French and the National Bureau of Economic Research

…with the guestimates for U.S. GDP growth in Q3 continuing to ratchet higher,…

THE PRUDENT SPECULATOR

SIGNIFICANT BOUNCE IN U.S. GDP EXPECTED IN Q3

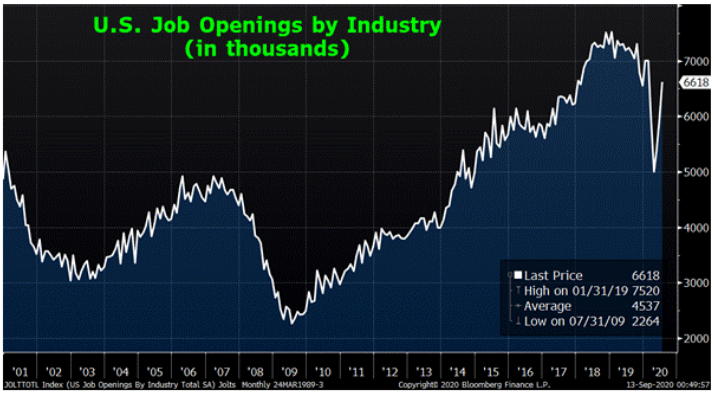
While a rebound is almost a mathematical certainty, given the magnitude of the massive Q2 economic contraction, the Atlanta Fed is now projecting a 30.8% increase in GDP in Q3 on an annualized basis.

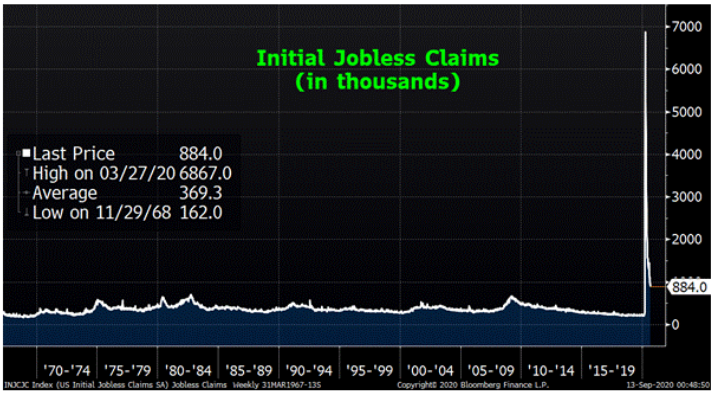


…even as we respect that the labor picture is not exactly grand.

THE PRUDENT SPECULATOR

DISMAL (BUT IMPROVING) EMPLOYMENT NUMBERS





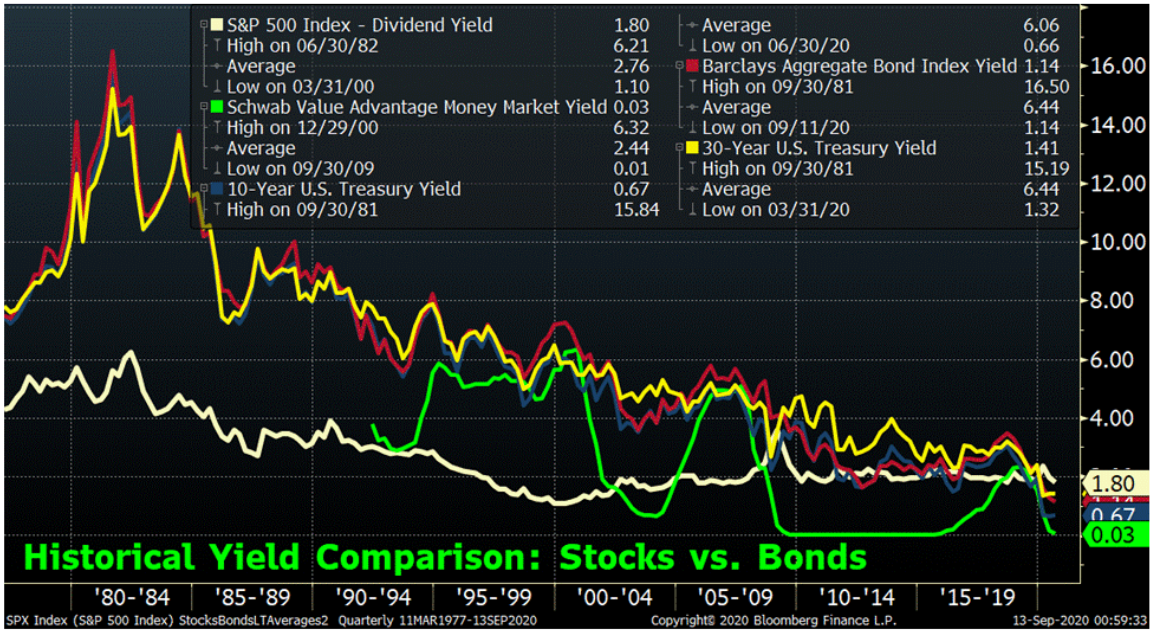
While a hefty 5.8 million people were rehired or found new jobs during July, and there were 6.6 million job openings during the month, up from 6.0 million in June, the labor picture hardly can be called good, even as the numbers today are significantly better than many had projected a few months back. Looking at more current data, first-time filings for unemployment benefits continue to be massive, with a whopping 884,000 claims in the latest week.

Of course, the current economic outlook has caused Jerome H. Powell & Co. to pledge to keep interest rates lower for longer, which we think provides significant support for stock prices,…

THE PRUDENT SPECULATOR

EQUITY VS. FIXED INCOME YIELDS

Though stocks are not necessarily a substitute for cash, government or corporate bonds, the payout on the S&P 500 (1.80%) is extraordinarily generous versus the income provided by fixed income, especially given the recent plunge in rates. Incredibly, **equities yield more than the Barclays Aggregate Bond Index and some 60 times the yield of a "generous" Money Market Fund!**



…and to let inflation run hotter than previous levels that might have caused the Federal Reserve to move to a less accommodative monetary policy stance.

THE PRUDENT SPECULATOR

FOMC STATEMENT ON LONGER-RUN GOALS AND MONETARY POLICY STRATEGY

"The economy is always evolving, and the FOMC's strategy for achieving its goals must adapt to meet the new challenges that arise," said Federal Reserve Chair Jerome H. Powell. "Our revised statement reflects our appreciation for the benefits of a strong labor market, particularly for many in low- and moderate-income communities, and that a robust job market can be sustained without causing an unwelcome increase in inflation."

Among the more significant changes to the framework document are:

• On maximum employment, the FOMC emphasized that maximum employment is a broad-based and inclusive goal and reports that its policy decision will be informed by its "assessments of the *shortfalls* of employment from its maximum level." The original document referred to "*deviations* from its maximum level."

• On price stability, the FOMC adjusted its strategy for achieving its longer-run inflation goal of 2 percent by noting that it "seeks to achieve inflation that averages 2 percent over time." To this end, the revised statement states that "following periods when inflation has been running persistently below 2 percent, appropriate monetary policy will likely aim to achieve inflation moderately above 2 percent for some time."

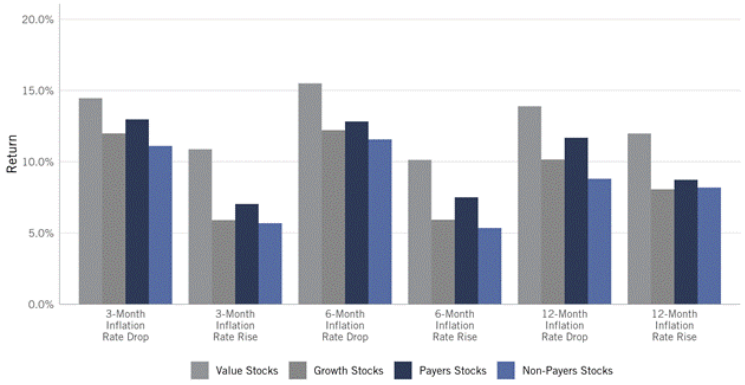
• The updates to the strategy statement explicitly acknowledge the challenges for monetary policy posed by a persistently low interest rate environment. Here in the United States and around the world, monetary policy interest rates are more likely to be constrained by their effective lower-bound than in the past.

August 27, 2020

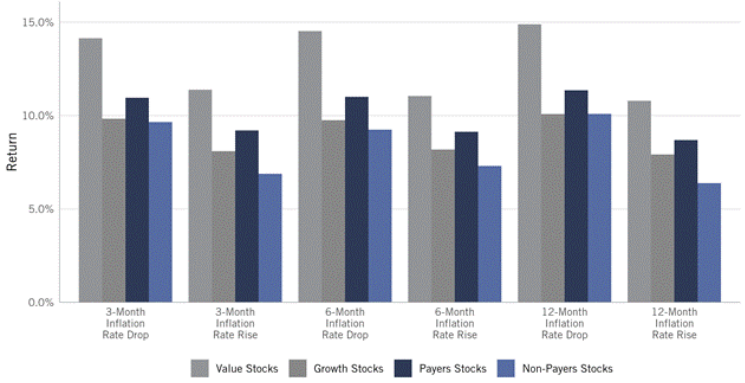
Not surprisingly, we suppose, investors have added worries about rising inflation to the list of stock-market bogeymen, but history suggests that equities, specifically Value Stocks and Dividend Payers, have performed just fine, on average, no matter if consumer prices are rising or falling, both as such a change is occurring or after it has taken place.

THE PRUDENT SPECULATOR

INFLATION Δ AND VALUE/GROWTH & DIV/NO DIVS RETURNS



From 12.31.27 through 03.31.20. Concurrent annualized 12-month returns. SOURCE: Kovitz using data from Bloomberg Finance L.P. and Professors Eugene F. Fama and Kenneth R. French



From 12.31.27 through 03.31.20. Subsequent annualized 12-month returns. SOURCE: Kovitz using data from Bloomberg Finance L.P. and Professors Eugene F. Fama and Kenneth R. French

Many have incorrectly warned that rising inflation rates will prove fatal for equities, as nine decades of returns data show that stocks in general have performed admirably on average, both concurrent with and subsequent to increases (as well as decreases) in the inflation rate over 3-, 6-, and 12-month time spans, with Value Stocks and Dividend Payers leading the charge.

Of course, pretty much no matter how historical data is sliced and diced, equities have proved rewarding in the fullness of time, provided investors remember that the secret to success in stocks is not to get scared out of them.

THE PRUDENT SPECULATOR

LOTS OF FRIGTENING EVENTS

Event	Reaction Dates		S&P Start Value	S&P End Value	Event Gain/Loss	12 Months Later	36 Months Later	60 Months Later	Event End thru Present
Pearl Harbor	12/6/1941	12/10/1941	9.32	8.68	-7%	8%	51%	76%	38390%
Truman Upset Victory	11/2/1948	11/10/1948	16.70	15.00	-10%	8%	52%	62%	22173%
Korean War	6/23/1950	7/13/1950	19.14	16.69	-13%	32%	45%	153%	19918%
Eisenhower Heart Attack	9/23/1955	9/26/1955	45.63	42.61	-7%	8%	17%	25%	7741%
Suez Canal Crisis	10/30/1956	10/31/1956	46.37	45.58	-2%	-10%	26%	51%	7230%
Sputnik	10/3/1957	10/22/1957	43.14	38.98	-10%	31%	37%	41%	8471%
Cuban Missile Crisis	8/23/1962	10/23/1962	59.70	53.49	-10%	36%	72%	78%	6146%
JFK Assassination	11/21/1963	11/22/1963	71.62	69.61	-3%	24%	14%	53%	4700%
MLK Assassination	4/3/1968	4/5/1968	93.47	93.29	0%	8%	8%	16%	3481%
Kent State Shootings	5/4/1970	5/14/1970	79.00	75.44	-5%	35%	40%	22%	4329%
Arab Oil Embargo	10/18/1973	12/5/1973	110.01	92.16	-16%	-28%	12%	6%	3525%
Nixon Resigns	8/9/1974	8/29/1974	80.86	69.99	-13%	24%	38%	56%	4673%
U.S.S.R. in Afghanistan	12/24/1979	1/3/1980	107.66	105.22	-2%	30%	31%	56%	3075%
Hunt Silver Crisis	2/13/1980	3/27/1980	118.44	98.22	-17%	37%	55%	83%	3302%
Falkland Islands War	4/1/1982	5/7/1982	113.79	119.47	5%	39%	51%	147%	2696%
U.S. Invades Grenada	10/24/1983	11/7/1983	165.99	161.91	-2%	4%	52%	69%	1963%
U.S. Bombs Libya	4/15/1986	4/21/1986	237.73	244.74	3%	20%	27%	57%	1265%
Crash of '87	10/2/1987	10/19/1987	328.07	224.84	-31%	23%	39%	85%	1386%
Gulf War Ultimatum	12/24/1990	1/16/1991	329.90	316.17	-4%	32%	50%	92%	957%
Gorbachev Coup	8/16/1991	8/19/1991	385.58	376.47	-2%	11%	23%	77%	787%
ERM U.K. Currency Crisis	9/14/1992	10/16/1992	425.27	411.73	-3%	14%	42%	132%	711%
World Trade Center Bombing	2/26/1993	2/27/1993	443.38	443.38	0%	5%	46%	137%	654%
Russia Mexico Orange County	10/11/1994	12/20/1994	465.79	457.10	-2%	33%	107%	210%	631%
Oklahoma City Bombing	4/19/1995	4/20/1995	504.92	505.29	0%	28%	122%	184%	561%
Asian Stock Market Crisis	10/7/1997	10/27/1997	983.12	876.99	-11%	21%	57%	2%	281%
Russian LTCM Crisis	8/18/1998	10/8/1998	1,101.20	959.44	-13%	39%	11%	8%	248%
Clinton Impeachment	12/19/1998	2/12/1999	1,188.03	1,230.13	4%	13%	-10%	-6%	172%
USS Cole Yemen Bombings	10/11/2000	10/18/2000	1,364.59	1,342.13	-2%	-20%	-23%	-12%	149%
September 11 Attacks	9/10/2001	9/21/2001	1,092.54	965.80	-12%	-12%	17%	36%	246%
Iraq War	3/19/2003	5/1/2003	874.02	916.30	5%	21%	42%	54%	265%
Madrid Terrorist Attacks	3/10/2004	3/24/2004	1,123.89	1,091.33	-3%	7%	32%	-26%	206%
London Train Bombing	7/6/2005	7/7/2005	1,194.94	1,197.87	0%	6%	5%	-11%	179%
2008 Market Crash	9/15/2008	3/9/2009	1,192.70	676.53	-43%	69%	103%	178%	394%
Price Changes Only - Does Not Include Dividends				**Averages:**	**-7%**	**18%**	**39%**	**66%**	**4573%**

As of 9.11.20. Source: Kovitz Investment Group using Bloomberg and Ned Davis Research Events & Reaction Dates

Time will tell how the COVID-19 Pandemic and Great Lockdown are remembered in terms of equity market disruption and ultimate recovery, but history is filled with plenty of disconcerting events. Happily, those who have stayed the course, sticking with their long-term investment plans, have nearly always been rewarded in the fullness of time.

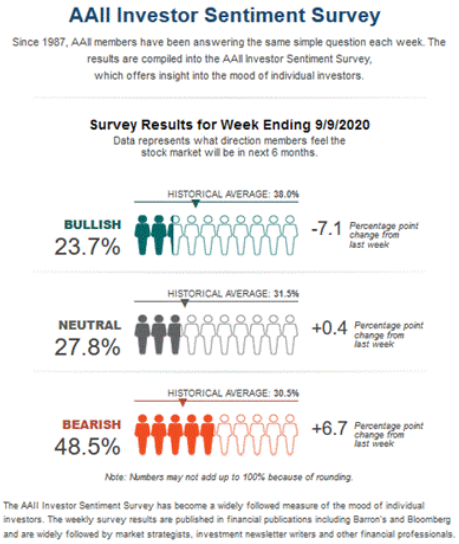
Keeping one's eyes on the long-term prize isn't easy, as investing can be an emotional roller coaster, with folks often becoming more pessimistic AFTER and not BEFORE a sizable selloff,…

THE PRUDENT SPECULATOR

SENTIMENT: NO ENTHUSIASM FOR STOCKS

Pessimism among individual investors continues to be very high, jumping last week to 18 points above normal in the latest AAII Sentiment Survey. Bullish sentiment plunged 7.1 points and is now a hefty 14.3 percentage points below normal.

We remain perplexed that many supposed market experts continue to argue that investors are piling into stocks, given that the latest data on mutual and exchange traded fund flows from ICI shows a massive exodus from U.S. stocks and a continued infatuation with bonds.



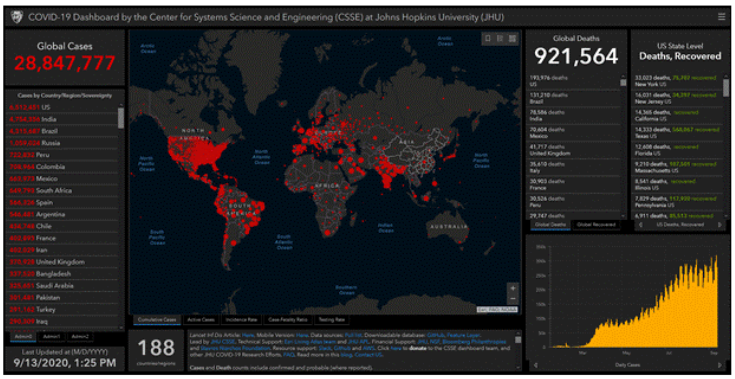
Combined Estimated Long-Term Fund Flows and ETF Net Issuance

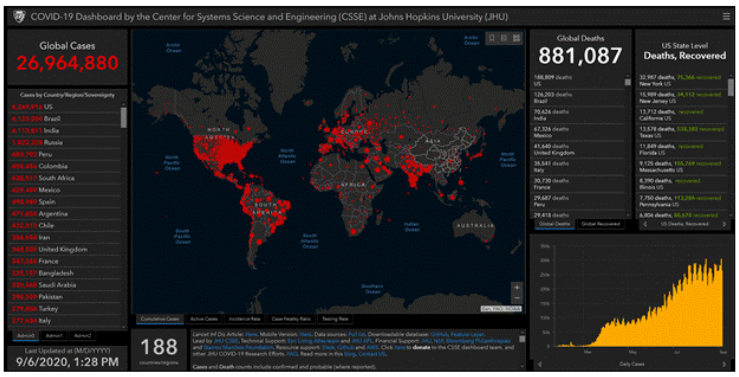
Millions of dollars

Week Ended	9/2/2020	8/26/2020	8/19/2020	8/12/2020	8/5/2020
Total Equity	-28,309	-19,714	-15,105	-3,256	-20,318
Domestic	-18,050	-18,290	-15,776	-5,495	-18,757
World	-10,260	-1,424	672	2,239	-1,562
Hybrid	-1,163	-624	-300	-577	-275
Total Bond	24,543	20,037	17,810	20,153	27,334
Taxable	23,201	17,848	14,886	16,607	23,924
Municipal	1,342	2,190	2,924	3,545	3,410
Commodities	718	669	370	-97	2,600
Total	-4,211	368	2,775	16,222	9,340

Source: Investment Company Institute

…so in these commentaries we always endeavor to provide plenty of data to back up our optimism for the long-term prospects for our broadly diversified portfolios of what we believe to be undervalued stocks. That does not mean that the near-term is not filled with concern, with developments on the COVID-19 front having a big impact on daily fluctuations,…





https://www.arcgis.com/apps/opsdashboard/index.html#/bda759474ofd4029942367b48e9ecf6

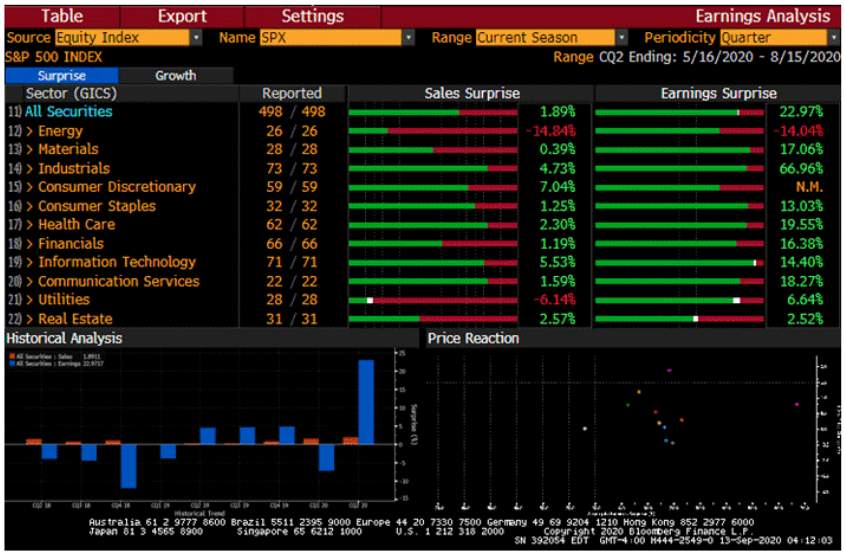
With access to testing remaining high, there was another jump of nearly 1.9 million in global COVID-19 confirmed cases in the latest week. Case counts have surged as economies have reopened, social distancing has waned and mask wearing has been inconsistent, and the U.S. is now up to nearly 194,000 fatalities. While deaths obviously lag cases, and Europe and the United Kingdom have seen new spikes in those diagnosed with the virus, the increase in the weekly fatality count has held steady at around 40,000 the last four weeks. No doubt, the approaching flu season will represent another health risk.

…while the health of the economy, the upcoming Presidential Election, social unrest, geopolitical events and natural disasters remain additional wildcards. Through it all, however, we should never forget that the business of America is business and corporate profits, after taking a big COVID-19/Great Lockdown hit this year, are likely to see significant growth in 2021 and beyond.

THE PRUDENT SPECULATOR

EPS LIKELY TO PLUNGE IN 2020 BUT REBOUND SHARPLY IN 2021

Q2 reporting season was very good, relative to analyst projections that had been a little too pessimistic in their top- and bottom-line estimates. Of course, full-year 2020 COVID-19-impacted EPS likely will be miserable, but a significant rebound is projected next year.



S&P 500 Earnings Per Share		
Quarter Ended	Bottom Up Operating EPS 3 Month	Bottom Up Operating EPS 12 Month
ESTIMATES		
12/31/2021	$45.01	$164.20
9/30/2021	$42.31	$154.65
6/30/2021	$39.99	$144.31
3/31/2021	$36.89	$131.06
12/31/2020	$35.46	$113.67
9/30/2020	$31.97	$117.39
6/30/2020	$26.74	$125.23
ACTUAL		
3/31/2020	$19.50	$138.63
12/31/2019	$39.18	$157.12
9/30/2019	$39.81	$152.97
6/30/2019	$40.14	$154.54
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

Source: Standard & Poor's. As of 9.10.20

And, while we remain braced for more volatility, especially during the seasonally less favorable September and October period, we always remember, as *Stocks for the Long Run* author and Wharton professor Jeremy Siegel states, "More than 90% of the value of stocks is from earnings more than 12 months in the future."

Stock Updates

It was a relatively quiet week for individual company news, but Jason Clark, Chris Quigley and Zach Tart look at six of our companies that had developments of sufficient importance to merit a Target Price review. Keep in mind that all stocks are rated as a "Buy" until such time as they are a "Sell." A listing of all current recommendations is available for download via the following link: https://theprudentspeculator.com/dashboard/, and we offer the reminder that any sales we make for our newsletter strategies are announced via our *Sales Alerts*.

Illustrating the difficulties companies face when navigating evolving developments on the geopolitical front, semiconductor capital equipment makers took it on the chin last week after news broke that the U.S. was discussing the "blacklisting" of Chinese chipmaker Semiconductor Manufacturing International Corporation (SMIC). The largest contract semiconductor maker in the Middle Kingdom and the latest target of Washington's ire said via press release, "SMIC

solemnly declares that the company, a public company listed on the Hong Kong Stock Exchange and the Sci-Tech Innovation Board (STAR Market), is an international semiconductor foundry strictly complying with the laws and regulations of all jurisdictions where it performs its businesses. Since its inception, the company has been fully compliant with all rules and laws. SMIC has maintained long-term strategic partnerships with multiple U.S.-based semiconductor equipment suppliers. Over the years, the Bureau of Industry and Security (BIS) has granted numerous export licenses for the company. With a large and diverse customer base, serving companies in the U.S., Europe, and other Asian regions, SMIC plays an important role in the global semiconductor supply chain…The company is in complete shock and perplexity to the news."

While it's not entirely clear why SMIC ended up on the list, the Trump Administration has used the export control list to punish companies involved in the human rights violations in Xinjiang. Of course, SMIC joins Huawei on the list of Chinese companies facing Washington sanctions. Not surprisingly, given the geopolitical uncertainty, shares of **Lam Research** (LRCX – $293.99) were hit hard last week. True, the pullback in the tech sector did not help the big chip-making-equipment producer, but Lam's latest 10-K shows that 30% of revenue in the latest fiscal year (ended June 2020) was derived from China, even as SMIC is supposedly a relatively small customer.

Obviously, there is the possibility of additional punitive sanctions, but trade skirmishes have been standard operating procedure for the last few years. So, while we have trimmed our Target Price for LRCX to $402, we continue to hold tight to our remaining Lam shares, especially as we took money off the table on our position back in February.

Despite little in the way of news on Friday, **NortonLifeLock** (NLOK – $21.13) sold off nearly 6%. According to Bloomberg, trading of NLOK options was five times higher than the 20-day average, which corresponded to a trading volume spike more than 14 times the 20-day average.

On Wednesday, NLOK had a Q&A session at the Citi 2020 Virtual Tech Conference, where CEO Vincent Pilette said that behind the scenes, "everybody" was advising **Broadcom** (AVGO – $359.70) to purchase the Consumer Security business instead of the Enterprise business due to its cash-flow-rich and stable characteristics. In Mr. Pilette's view, NLOK is much more attractive than the Enterprise business that was sold off and management expects demand for consumer security software to continue to grow. He said, "so far, we've delivered three quarters of growth at around 4% to a declining customer count to, what I would call a positive stabilization of customer count, which is slightly growing. And we're now all marching towards the long-term vision which is building that cyber safety to protect and enable consumer to live their digital life free from cyber criminals."

Mr. Pilette concluded, "At all current characteristics mid-single digit grows with on the current portfolio. I do not see us lowering the operating margin…and we don't want to be driven by that because if it's good to build Cyber Safety and it's accretive to the bottom line, we will look at that business. Therefore in the long term, while we commit to rigorous execution and short-term metrics that we share sustain or offsetting the revenue growth and growing EPS faster than the revenue is kind of the balance we'll operate within."

We believe that Norton's prospects in data security remain relatively bright, and we continued to be impressed with management's ability to drive down operating costs. There's room to grow, especially as some of the one-time charges related to Broadcom are rolling off. As we suspected, NLOK has been a beneficiary as individuals are seeking online protection as the world rapidly has become more digitized and cybercrime is showing no signs of abating. Our Target Price for NLOK remains $27.

Global banking giant **Citigroup** (C – $51.00) announced last Friday that current CEO Michael Corbat would be stepping down in February of 2021. The board has appointed current president and Chief of Global Consumer banking Jane Fraser to take the seat as the first female chosen to lead a major U.S. bank. Ms. Fraser is a long-time veteran of Citi, having worked at the bank since 2004, and was Global Head of Strategy and Mergers and Acquisitions throughout the Great Financial Crisis.

On the one hand, the announcement may come as a surprise to some given the current state of the economy. One might expect the bank to wait out the storm before making such a change. On the other hand, Ms. Fraser offers a fresh look for the firm, as it has came up short in meeting its own financial targets over the past decade and has had the lowest return on equity of major U.S. banks. All considered, we'll reserve our judgement for the time being, but we think there is a lot to like overall as ongoing restructuring, amplified capital return programs and technological investment all appear to work in Citi's favor in the coming years. At just 61% of book value, shares trade at the lowest percentage of book value of any of its peers, and the dividend yield is 4.0%. Our Target Price for C is $94.

General Motors (GM – $30.46) announced a new partnership last week with the controversial electric truck company Nikola Corp. GM has agreed to provide manufacturing and engineering services to Nikola in exchange for an 11% ownership stake in the firm for a stated $2 billion, and expects to realize at least $4 billion in total benefits from the deal. Nikola disclosed that it will use GM's Ultium battery system and Hydrotec fuel cell technology in its multiple planned truck programs. The deal is expected to close by the end of September, and if it so chooses, GM is allowed to dispose of 1/3 of its stake after each of 1- and 2-year lockups, with the remaining third disposable after June 2025. Shares spiked the day of the announcement but had retraced the jump by end of week.

"This strategic partnership with Nikola, an industry leading disrupter, continues the broader deployment of General Motors' all-new Ultium battery and Hydrotec fuel cell systems," said General Motors Chairman and CEO Mary Barra. "We are growing our presence in multiple high-volume EV segments while building scale to lower battery and fuel cell costs and increase profitability. In addition, applying General Motors' electrified technology solutions to the heavy-duty class of commercial vehicles is another important step in fulfilling our vision of a zero-emissions future."

GM is essentially taking a flyer on Nikola shares, which have gyrated all over the map, rising on the partnership news and then plunging later in the week on a report from a prominent short seller that Nikola's management overstated its internally developed battery and fuel-cell capabilities. However, we see the arrangement as mostly positive given the lack of an upfront

cash commitment, and Nikola's decision to use GM battery and fuel cell systems is validation of the firm's intellectual property. While COVID-19 has taken its toll on the vehicle manufacturer, GM remains in decent financial shape. We anticipate the delivery of its own Cadillac Lyriq in late 2022, with 20 others expected by 2023. With the dividend suspended for now, shares trade at just 7 times expected 2021 EPS. Our Target Price for GM has been nudged up to $45.

Despite reporting what we saw as another strong quarter, shares of **Kroger Co.** (KR – $34.47) fell almost 5% last week. Although management indicated that full-year performance will be above expectations, investors seemed bothered that exact forecasts weren't provided. The grocery store operator said that it earned $0.73 per share in the latest period, more than 30% greater than the expected $0.56, and recorded revenue of $30.49 billion, compared to the consensus analyst estimate of $29.99 billion. Same store sales, excluding fuel, jumped 14.6%. The grocer's digital sales continued to benefit from social distancing mandates and usage comfort by consumers, jumping 127%.

CEO Rodney McMullen commented, "Our top priority is to provide a safe environment for associates and customers and as the pandemic continues, we will continue to rise to meet the challenge. Customers are at the center of everything we do and, as a result, we are growing market share. Kroger's strong digital business is a key contributor to this growth, as the investments made to expand our digital ecosystem are resonating with customers. Our results continue to show that Kroger is a trusted brand and our customers choose to shop with us because they value the product quality and freshness, convenience, and digital offerings that we provide…We delivered extremely strong results in the second quarter and expect to deliver consistently attractive total shareholder returns. We are more certain than ever that the strategic choices and investments made through Restock Kroger to execute against our competitive moats – Fresh, Our Brands, Personalization and Seamless – have positioned Kroger to meet the moment, especially as customers are rediscovering their passion for food at home."

Management said that Kroger's net total debt to adjusted EBITDA continues to be reduced and that ratio now stands at 1.70, compared to 2.46 a year ago, below a target range of 2.30 to 2.50. The company held temporary cash investments of approximately $2.4 billion as of the end of the quarter, reflecting better operating performance and significant improvement in working capital. Kroger continued to buy back shares and said its board has authorized another $1 billion for stock buybacks.

CFO Gary Millerchip added, "As a result of our strong performance in the first half, the expectation of sustained trends in food at home consumption and confidence in our ability to execute against the Restock Kroger strategy, we are updating our full year 2020 guidance…There are still many uncertainties and, as a result, we are providing a wider guidance range. For the full year 2020, we expect total identical sales without fuel to exceed 13% and we expect to achieve adjusted EPS growth of approximately 45% to 50%…Relative to delivering on our total shareholder return growth targets as outlined at our November 2019 Investor Day, these factors also lead us to believe that our 2021 business results will be higher than we would have expected prior to the COVID-19 pandemic."

While competition remains stiff in the grocery space, we like that Kroger continues to remake itself and has moved more in the direction of being offensive versus defensive/reactive. Competitive headwinds won't die down anytime soon, but we are pleased to see the continued progress being made, and we believe there is more upside to be offered in KR shares. The stock trades at 13.3 times NTM adjusted EPS projections and its dividend yield of 2.1% is still attractive, especially relative to the 10-year U.S. Treasury yielding 0.67%. Our Target Price for KR has been boosted to $40.

System software firm **Oracle** (ORCL – $57.00) posted earnings per share of $0.93, versus the $0.86 estimate, in fiscal Q1 2021. ORCL had sales of $9.4 billion (vs. $9.2 billion est.). Oracle reported solid sales execution and operational success despite the COVID-related challenges, which resulted in operating income growing 8%, the company's best growth in three years. Oracle continued to benefit from a business mix that resonates with customers, led by Fusion SaaS and Autonomous Database Warehouse. Shares jumped in after-hours trading on Thursday night, but all of the gains were given up by the end of Friday's trading session amid broader market volatility.

Chairman and Founder Larry Ellison commented, "Oracle occupies a unique position in the cloud market. Oracle is the only cloud vendor that competes in both the enterprise applications market, SaaS; and the infrastructure-as-a-service market, IaaS. Our competitors in SaaS are people like Salesforce and Workday. Our competitors in IaaS are people like Microsoft and Amazon. They're different markets. We're the only one that spans these 2 markets. It's a very interesting dynamic. I believe we have the best technology in the market today at both the applications layer and the infrastructure layer of the cloud. While analysts have ranked Oracle Cloud applications #1 in both market share and customer satisfaction for some time: we're #1 in customer satisfaction in HCM, we're #1 in customer satisfaction in ERP, I can go on, but what's interesting is that those same analysts are beginning to take notice of the technical quality and customer satisfaction associated with Oracle's cloud Infrastructure-as-a-Service business."

CEO Safra Catz added guidance, "Total revenues are expected to grow between 1% to 3% in U.S. dollars. And because we will have slightly under a 1% tailwind, so in constant currency, that kind of rounds into 0 to 2% but probably at the higher side. Non-GAAP EPS in constant currency is expected to grow 8% to 12% between $0.96 and $1 in constant currency, but again, that's assuming a $0.02 tailwind; non-GAAP EPS in USD is expected to grow 10% to 14% and to be between $0.98 and $1.02 in U.S. dollars."

ORCL repurchased 90 million shares for a total of $5 billion throughout the quarter, bringing purchases over the last 12 months to 361 million shares for a total of $19.2 billion and reducing the total share count by 40% over the past 10 years. Oracle will keep its $0.24 quarterly dividend payment, consistent with the amount paid since early 2019.

We remain encouraged by recent successes and we believe that ORCL still has the right leadership team in place as the business adapts to a dynamic cloud business. The Oracle Public Cloud continues to grow, led by its unique features like Autonomous Database (which fails over with no intervention at the first sign of server trouble). We think there are significant opportunities for revenue growth worldwide and Oracle is scaling up for the opportunity. The

company reported 26 cloud infrastructure regions (compared to 24 for competitor AWS) with plans to add ten more by the middle of next year. We have always liked ORCL's relentless pursuit of the #1 spot in any competition. We think that ORCL shares remain attractive, trading for 13 times forward earnings and currently yielding 1.7%. Our Target Price has been hiked to $68.