Market Commentary Monday, September 21, 2020

September 20, 2020

EXECUTIVE SUMMARY

Week in Review – S&P Moves Lower; Average Stock Moves Higher
FOMC Meeting – Improved Economic Outlook Yet Rates to Remain Near Zero Through 2023
U.S. Econ Update – Solid Near-Term Numbers…Aside from Jobs Data
World Econ Projections – OECD Raises its Global GDP Forecasts
Interest Rates – Stocks Remain Very Attractive
Sentiment – Still Little Love for Equities and Lots of Affection for Bonds
Snowflake vs. 20 Big Undervalued Companies – Metric Comparisons
IPOs – History Favors Established Companies
Stock News – Updates on FDX, MDC, GILD, MET, C, FITB, ORCL & WMT

Market Review

We had another reminder last week that it is a market of stocks and not simply a stock market. *The Wall Street Journal*, in its Saturday edition, proclaimed, "Stocks Fall for Third Straight Week," which arguably made sense given that the downturn over the second half of the week pushed the S&P 500 to a loss of 0.60% for the full five days of trading. Of course, the drop in the capitalization-weighted S&P was due entirely to skids in the 5% range in mega-cap members **Apple** (AAPL – $106.84), Amazon.com and Facebook, as the average stock in the index gained 0.80% for the week. And for our portfolios, though we do still own a big position in Apple, the Russell 3000 Value index climbed 0.61% versus a drop of 0.62% for the Russell 3000 Growth index.

VALUE SHOWING SIGNS OF LIFE

While two+ months does not a trend make, it is nice to see a handsome absolute and relative rebound in undervalued stocks, especially as there is plenty of runway remaining for a return to historical norms.

Total Returns Matrix

Last Week	Last Month	Since 7.9.20	Last 6 Months	YTD	Last 12 Months	Last 24 Months	Last 36 Months	Last 60 Months	Name
0.54	0.19	2.57	9.88	6.43	7.05	14.60	12.70	21.13	Bloomberg Barclays Global-Aggregate Bond
-0.09	-0.06	0.08	7.30	6.93	7.85	18.36	16.54	23.00	Bloomberg Barclays US Aggregate Bond
-0.01	-0.17	8.11	40.65	-1.35	4.34	10.54	32.87	90.66	Dow Jones Industrial Average
0.53	-0.40	8.04	38.61	-5.99	0.45	3.46	14.80	46.38	New York Stock Exchange Composite
3.33	-1.81	7.48	66.50	4.27	11.68	4.27	30.91	58.88	Russell 2000 Growth
1.99	**-2.16**	**13.06**	**43.96**	**-18.76**	**-13.36**	**-19.86**	**-7.99**	**23.27**	**Russell 2000 Value**
2.68	-1.98	10.12	56.12	-6.98	-0.58	-7.54	11.17	41.76	Russell 2000
-0.62	-2.83	4.16	53.15	18.87	29.61	36.36	71.13	127.09	Russell 3000 Growth
0.61	**-0.50**	**8.41**	**32.42**	**-11.13**	**-5.25**	**-2.07**	**9.10**	**42.95**	**Russell 3000 Value**
-0.03	-1.71	6.18	43.65	4.17	12.35	17.19	38.79	82.97	Russell 3000
0.80	-0.53	9.44	42.20	-3.72	2.59	6.56	23.42	60.40	S&P 500 Equal Weighted
-0.60	-1.92	5.66	39.73	4.17	12.53	18.89	40.58	87.60	S&P 500
-1.35	-2.73	4.50	48.88	17.16	25.54	32.57	64.51	120.03	S&P 500 Growth
0.53	**-0.67**	**7.45**	**28.02**	**-10.53**	**-2.44**	**3.22**	**15.58**	**52.58**	**S&P 500 Value**
0.23	-2.54	4.54	55.85	10.06	16.81	18.44	43.55	81.26	S&P 500 Pure Growth
1.71	**-0.37**	**13.19**	**41.50**	**-24.89**	**-19.90**	**-22.13**	**-8.30**	**19.19**	**S&P 500 Pure Value**
0.13	4.74	22.04	26.54	-3.66	3.47	-0.04	20.25	69.02	Berkshire Hathaway B

As of 9.18.20. Source Kovitz using data from Bloomberg

We really can't complain about the latest week, and we are pleased with the resurgence of Value since July 9, 2020. Still, it was somewhat surprising to see stocks head south mid-week, with the downturn coinciding with Jerome H. Powell's press conference shortly after the Fed Chair and his colleagues at the Federal Open Market Committee confirmed that interest rates will likely stay near zero for the foreseeable future,…

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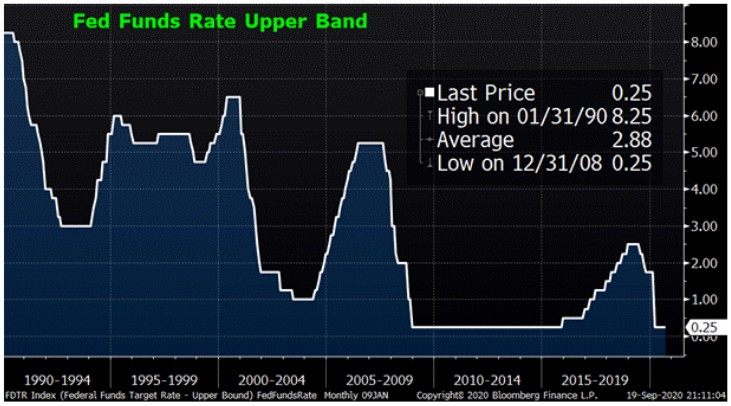
ACCOMMODATIVE FEDERAL RESERVE FOR AS FAR AS THE EYE CAN SEE

FOMC Participants' Fed Funds Rate Target Level Number with each projection					
Midpoint of Target Range	2020	2021	2022	2023	Longer Run
3.000					2
2.875					
2.750					1
2.625					
2.500					8
2.375					1
2.250					3
2.125					
2.000					1
1.875					
1.750					
1.625					
1.500					
1.375				1	
1.250					
1.125					
1.000					
0.875					
0.750					
0.625			1	1	
0.500					
0.375				2	
0.250					
0.125	17	17	16	13	
0.000					

Source: Federal Reserve, September 16, 2020

Projections updated last week from Jerome H. Powell & Co. confirmed what the Federal Reserve made quite clear on August 27, 2020: The Fed is likely to keep interest rates lower for longer to support the economy, even if it means that inflation overshoots its 2.0% target for a period of time.



Source: Bloomberg

…with the Fed indicating that it will remain highly accommodative,

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FOMC STATEMENT: 9.16.20

The Federal Reserve is committed to using its full range of tools to support the U.S. economy in this challenging time, thereby promoting its maximum employment and price stability goals.

The COVID-19 pandemic is causing tremendous human and economic hardship across the United States and around the world. Economic activity and employment have picked up in recent months but remain well below their levels at the beginning of the year. Weaker demand and significantly lower oil prices are holding down consumer price inflation. Overall financial conditions have improved in recent months, in part reflecting policy measures to support the economy and the flow of credit to U.S. households and businesses.

The path of the economy will depend significantly on the course of the virus. The ongoing public health crisis will continue to weigh on economic activity, employment, and inflation in the near term, and poses considerable risks to the economic outlook over the medium term.

The Committee seeks to achieve maximum employment and inflation at the rate of 2% over the longer run. With inflation running persistently below this longer-run goal, the Committee will aim to achieve inflation moderately above 2% for some time so that inflation averages 2 percent over time and longer-term inflation expectations remain well anchored at 2%. The Committee expects to maintain an accommodative stance of monetary policy until these outcomes are achieved. The Committee decided to keep the target range for the federal funds rate at 0 to 1/4 percent and expects it will be appropriate to maintain this target range until labor market conditions have reached levels consistent with the Committee's assessments of maximum employment and inflation has risen to 2% and is on track to moderately exceed 2 percent for some time. In addition, over coming months the Federal Reserve will increase its holdings of Treasury securities and agency mortgage-backed securities at least at the current pace to sustain smooth market functioning and help foster accommodative financial conditions, thereby supporting the flow of credit to households and businesses.

In assessing the appropriate stance of monetary policy, the Committee will continue to monitor the implications of incoming information for the economic outlook. The Committee would be prepared to adjust the stance of monetary policy as appropriate if risks emerge that could impede the attainment of the Committee's goals. The Committee's assessments will take into account a wide range of information, including readings on public health, labor market conditions, inflation pressures and inflation expectations, and financial and international developments.

…even with a significantly increased outlook for GDP growth this year to -3.7%, up from a prior projection made back in June of a 6.5% decline, and a sharp reduction in estimates for the unemployment rate for this year, 2021 and 2022.

The Fed's latest projections call for a much less severe recession (3.7% plunge in real GDP) this year, and a significant recovery of 4.0% GDP growth in 2021 and a decent 3.0% expansion in 2022, while the Fed Funds rate will likely remain near zero through 2023.

Table 1. Economic projections of Federal Reserve Board members and Federal Reserve Bank presidents, under their individual assumptions of projected appropriate monetary policy, September 2020

Percent

Variable	Median[1]					Central Tendency[2]					Range[3]				
	2020	2021	2022	2023	Longer run	2020	2021	2022	2023	Longer run	2020	2021	2022	2023	Longer run
Change in real GDP	-3.7	4.0	3.0	2.5	1.9	-4.0–-3.0	3.6–4.7	2.5–3.3	2.4–3.0	1.7–2.0	-5.5–1.0	0.0–5.5	2.0–4.5	2.0–4.0	1.6–2.2
June projection	-6.5	5.0	3.5		1.8	-7.6–-5.5	4.5–6.0	3.0–4.5		1.7–2.0	-10.0–-4.2	-1.0–7.0	2.0–6.0		1.6–2.2
Unemployment rate	7.6	5.5	4.6	4.0	4.1	7.0–8.0	5.0–6.2	4.0–5.0	3.5–4.4	3.9–4.3	6.5–8.0	4.0–8.0	3.5–7.5	3.5–6.0	3.5–4.7
June projection	9.3	6.5	5.5		4.1	9.0–10.0	5.9–7.5	4.8–6.1		4.0–4.3	7.0–14.0	4.5–12.0	4.0–8.0		3.5–4.7
PCE inflation	1.2	1.7	1.8	2.0	2.0	1.1–1.3	1.6–1.9	1.7–1.9	1.9–2.0	2.0	1.0–1.5	1.3–2.4	1.5–2.2	1.7–2.1	2.0
June projection	0.8	1.6	1.7		2.0	0.6–1.0	1.4–1.7	1.6–1.8		2.0	0.5–1.2	1.1–2.0	1.4–2.2		2.0
Core PCE inflation[4]	1.5	1.7	1.8	2.0		1.3–1.5	1.6–1.8	1.7–1.9	1.9–2.0		1.2–1.6	1.5–2.4	1.6–2.2	1.7–2.1	
June projection	1.0	1.5	1.7			0.9–1.1	1.4–1.7	1.6–1.8			0.7–1.3	1.2–2.0	1.2–2.2		
Memo: Projected appropriate policy path															
Federal funds rate	0.1	0.1	0.1	0.1	2.5	0.1	0.1	0.1	0.1–0.4	2.3–2.5	0.1	0.1	0.1–0.6	0.1–1.4	2.0–3.0
June projection	0.1	0.1	0.1		2.5	0.1	0.1	0.1		2.3–2.5	0.1	0.1	0.1–1.1		2.0–3.0

Source: Federal Reserve, September 16, 2020

Looking at the current state of the economy, Mr. Powell even sounded less pessimistic than in recent pronouncements: "Economic activity has picked up from its depressed second-quarter level, when much of the economy was shut down to stem the spread of the virus. With the reopening of many businesses and factories and fewer people withdrawing from social interactions, household spending looks to have recovered about three-quarters of its earlier decline. Nonetheless, spending on services that typically require people to gather closely, including travel and hospitality, is still quite weak. The recovery in household spending also likely owes to federal stimulus payments and expanded unemployment benefits, which provided substantial and timely support to household incomes. Activity in the housing sector has returned to its level at the beginning of the year, and we are starting to see signs of an improvement in business investment. The recovery has progressed more quickly than generally expected, and forecasts from FOMC participants for economic growth this year have been revised up since our June Summary of Economic Projections. Even so, overall activity remains well below its level before the pandemic and the path ahead remains highly uncertain."

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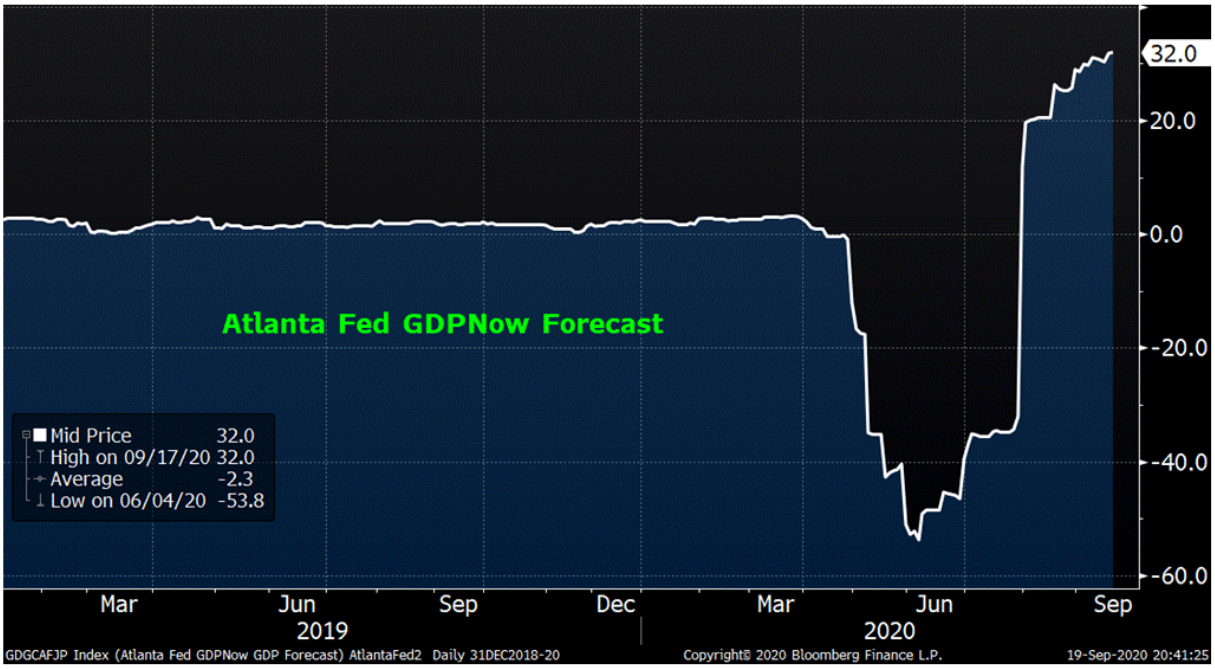
SIGNIFICANT BOUNCE IN U.S. GDP EXPECTED IN Q3

While a rebound is almost a mathematical certainty, given the magnitude of the massive Q2 economic contraction, the Atlanta Fed is now projecting a 32.0% increase in GDP in Q3 on an annualized basis.



Certainly, the current quarter will mark a sensational recovery from the worst economic setback since the Great Depression, though we understand that the outlook for Q4 and beyond remains in question. That said, we find it fascinating that the latest *Report on the Economic Well-Being of U.S. households* from the Federal Reserve shows that more adults are suggesting they are OK financially today than said the same last October, prior to COVID-19 and the Great Lockdown.

77% OF ADULTS DOING OK JULY 2020 VS. 75% IN OCTOBER 2019

September 18, 2020
Federal Reserve Board issues Report on the Economic Well-Being of U.S. Households

Table 2. Share of adults at least doing okay financially (by demographic characteristics and year)
Percent

Characteristic	October 2019	July 2020	Change
Family income			
Less than $40,000	55	56	2
$40,000–$100,000	81	84	4
Greater than $100,000	95	95	0
Education			
High school degree or less	63	64	1
Some college/technical or associate degree	75	77	2
Bachelor's degree or more	88	91	3
Race/ethnicity			
White	79	81	2
Black	65	64	-1
Hispanic	66	69	2
Place of residence			
Metro area	76	77	1
Non-metro area	72	76	4
Overall	**75**	**77**	**2**

Note: Income and education categories are from the October 2019 survey responses.

Data collected to supplement the Federal Reserve Board's seventh annual Survey of Household Economics and Decisionmaking showed that U.S. families were faring better financially in July than in April, but many still faced uncertainty regarding layoffs and prospects for returning to work.

Recognizing the unprecedented financial disruptions caused by the COVID-19 pandemic, the Federal Reserve conducted a pair of supplemental surveys to monitor changes in the financial well-being of Americans. The first of these surveys was conducted in April, at the onset of the pandemic and before most financial relief efforts were in place. The April results were described in the Report on the Economic Well-Being of U.S. Households in 2019, Featuring Supplemental Data from April 2020. The second survey was conducted in July.

In July, 77 percent of adults said they were doing at least okay financially, up from 72 percent in early April, and 75 percent in October 2019. This increase is likely due to some people returning to work as well as the availability of assistance programs either from the government or from charitable organizations. A substantial number of families received one or more forms of financial assistance, and the effects of these programs were apparent in people's overall financial well-being and ability to cover expenses.

The July survey demonstrated that people appeared better able to handle small financial emergencies than they were nine months prior in October 2019. Seventy percent of adults said in July that they would be able to pay an unexpected $400 emergency expense entirely by using cash, savings, or a credit card paid off at the next statement—an increase from 63 percent last October.

The economic numbers out last week were generally pretty good, especially in regard to manufacturing,…

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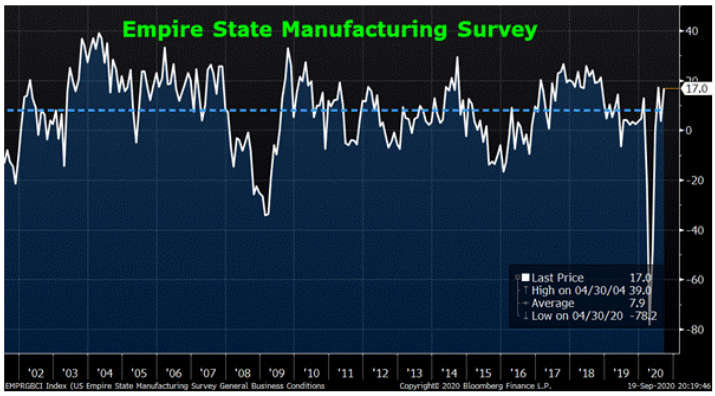
FACTORY OUTLOOK REMAINS UPBEAT IN SEPTEMBER



The Empire State gauge of manufacturing activity in the New York area jumped in September, reversing a big decline the month prior and climbing to a reading of 17.0, well-above-average for this business conditions index. The Philadelphia Fed's September measure of manufacturing activity in the mid-Atlantic region came in at 15.0, better than projected and well above the average for the index. Both numbers indicate solidly improving factory conditions.

…and housing.

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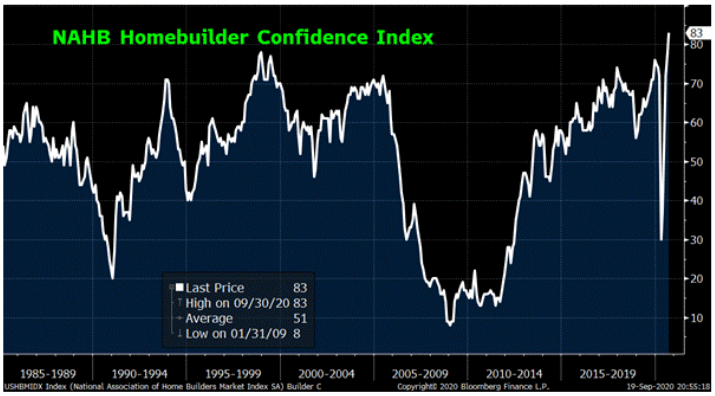
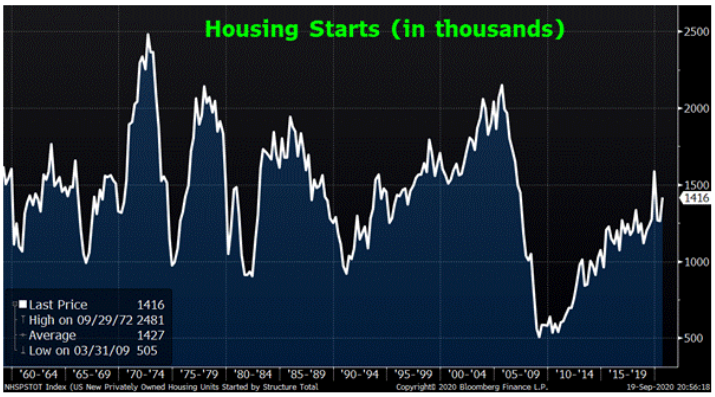
OPTIMISTIC HOUSING NUMBERS





The National Association of Home Builders' monthly confidence index for September rose sharply to a better-than-expected tally of 83, the best reading on record for the 35-year-old gauge. No doubt, record low mortgage rates are supporting the housing market, but builders do not seem to be engaging in irrational exuberance as housing starts for August edged down to a seasonally adjusted annual rate of 1.42 million units, while permits also ticked 1% lower.

That is not to say that everything is rosy economically speaking, especially considering the number of folks still out of work,…

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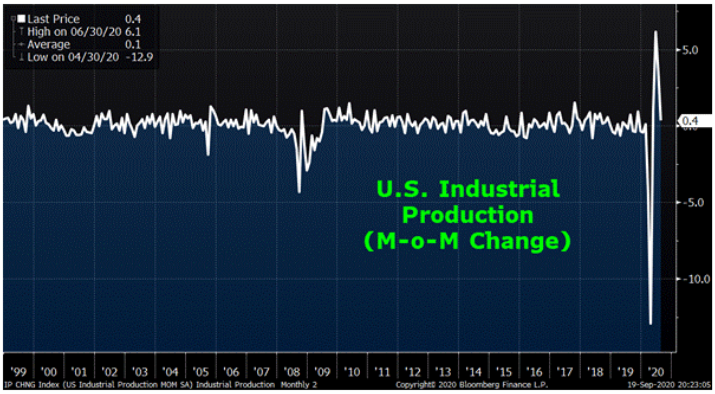
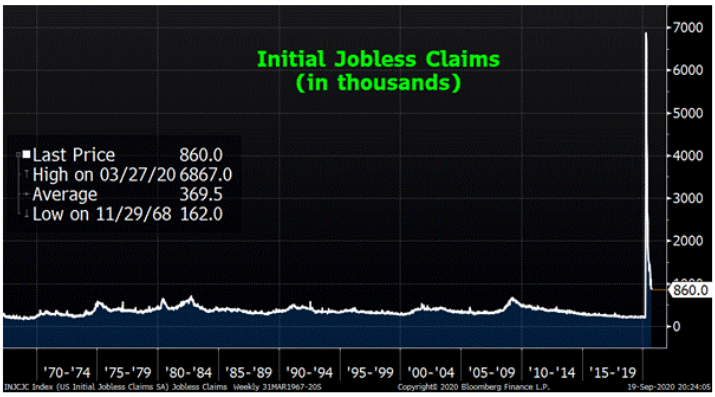
NOT-SO-GRAND ECON STATS





Factory output rose for the fourth straight month in August, with industrial production inching up 0.4%, trailing estimates of a 0.5% advance, while capacity utilization climbed to 71.4%, up from 70.6% in July. Of course, though showing considerable improvement, the labor market remains abysmal, as the number of first-time filings for unemployment benefits came in at 860,000 for the latest week, bringing the 26-week total to a massive 61 million.

…but pocketbooks are still open and consumer sentiment is better than most might think.

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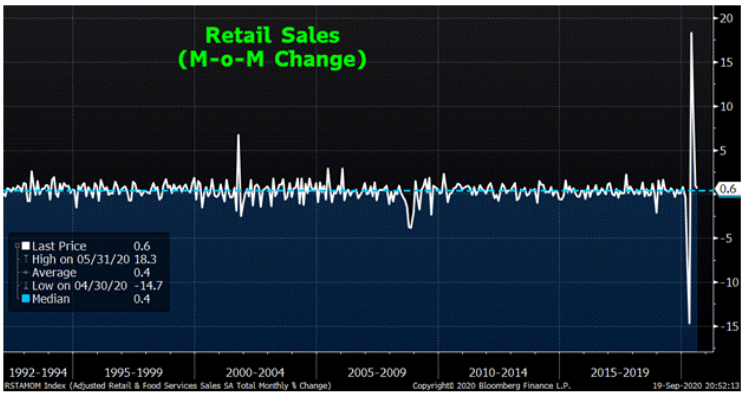
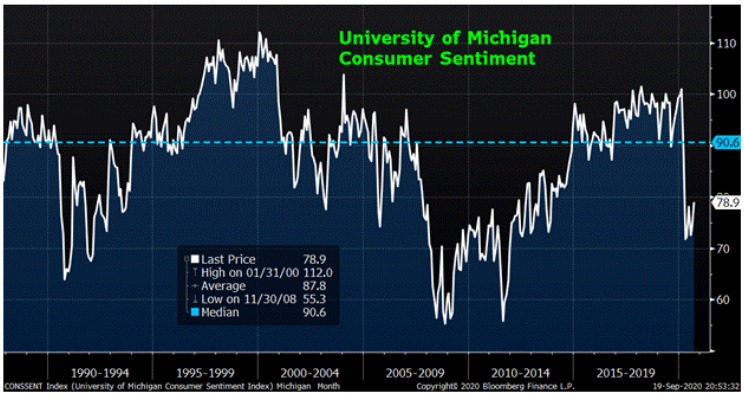
CONSUMERS STILL SHOPPING AND FEELING LESS PESSIMISTIC





Retail sales rose 0.6% in August, a figure that would be considered robust in normal times, but one that was a little disappointing as it trailed expectations and marked a pullback from the 0.9% growth seen in July. Meanwhile, the preliminary Univ. of Michigan gauge of consumer sentiment this month rebounded to 78.9, up from a final reading of 74.1 in August, though the latest number is still below average.

Clearly, the economic future is far from certain, even as forward looking measures are still on the correct side of the ledger,…

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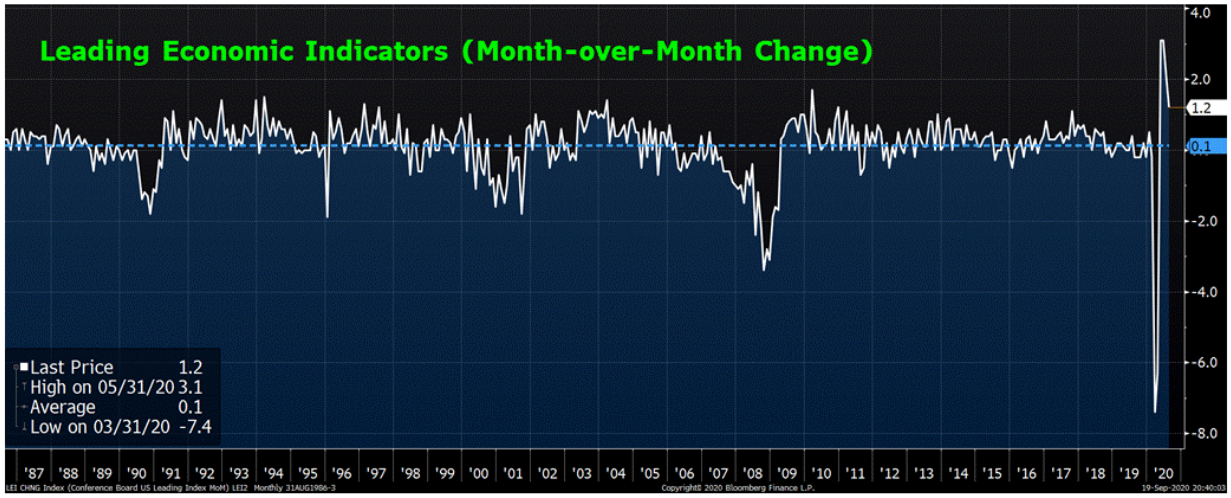
LEI STILL WELL INTO POSITIVE TERRITORY…FOR THE TIME BEING

The forward-looking Leading Economic Index rose by 1.2% on a month-over-month basis in August, down from a 2.0% advance in July. The average gain in the LEI back to 1986 has been just 0.1%, but the keeper of the metric, the Conference Board, stated, "While the U.S. LEI increased again in August, the slowing pace of improvement suggests that this summer's economic rebound may be losing steam heading into the final stretch of 2020."



…but the economic outlook around the world has also been upgraded of late.

OECD: GRADUAL RECOVERY UNDERWAY AFTER AN UNPRECEDENTED SHOCK

The outlook is subject to considerable uncertainty and projections are dependent on assumptions about the spread of the COVID-19 virus and policy developments.

OECD Interim Economic Outlook Forecasts September 2020

Real GDP growth
Year-on-year % change

	2019	2020		2021	
		Interim EO projections	Difference from June EO single-hit scenario	Interim EO projections	Difference from June EO single-hit scenario
World[1]	2.6	-4.5	1.5	5.0	-0.2
G20[1,2]	2.9	-4.1	1.6	5.7	0.2
Australia	1.8	-4.1	0.9	2.5	-1.6
Canada	1.7	-5.8	2.2	4.0	0.1
Euro area	1.3	-7.9	1.2	5.1	-1.4
Germany	0.6	-5.4	1.2	4.6	-1.2
France	1.5	-9.5	1.9	5.8	-1.9
Italy	0.3	-10.5	0.8	5.4	-2.3
Japan	0.7	-5.8	0.2	1.5	-0.6
Korea	2.0	-1.0	0.2	3.1	0.0
Mexico	-0.3	-10.2	-2.7	3.0	0.0
Turkey	0.9	-2.9	1.9	3.9	-0.4
United Kingdom	1.5	-10.1	1.4	7.6	-1.4
United States	2.2	-3.8	3.5	4.0	-0.1
Argentina	-2.1	-11.2	-2.9	3.2	-0.9
Brazil	1.1	-6.5	0.9	3.6	-0.6
China	6.1	1.8	4.4	8.0	1.2
India[3]	4.2	-10.2	-6.5	10.7	2.8
Indonesia	5.0	-3.3	-0.5	5.3	0.1
Russia	1.4	-7.3	0.7	5.0	-1.0
Saudi Arabia	0.4	-6.8	-0.2	3.2	-0.6
South Africa	0.1	-11.5	-4.0	1.4	-1.1

Note: Difference from June 2020 Economic Outlook in percentage points, based on rounded figures.
1. Aggregate using moving nominal GDP weights at purchasing power parities.
2. The European Union is a full member of the G20, but the G20 aggregate only includes countries that are also members in their own right.
3. Fiscal years, starting in April.

The projections assume that sporadic local outbreaks will continue, with these being addressed by targeted local interventions rather than national lockdowns; a vaccination is assumed not to become widely available until late in 2021.

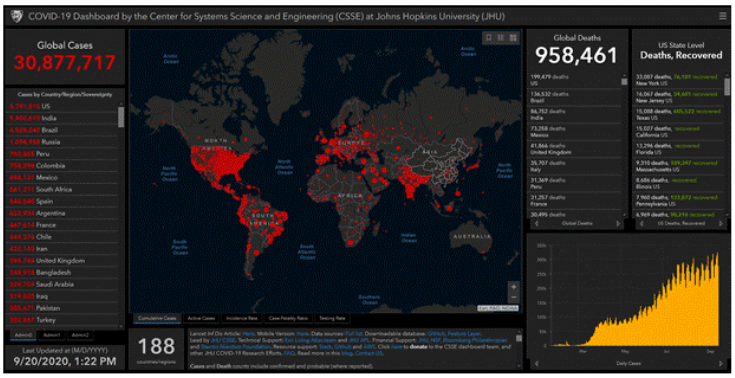
Global GDP is projected to decline by 4.5% this year, before picking up by 5% in 2021. The drop in global output in 2020 is smaller than expected, though still unprecedented in recent history, but this masks considerable differences across countries, with upward revisions in China, the United States and Europe, but weaker-than-expected outcomes in India, Mexico and South Africa.

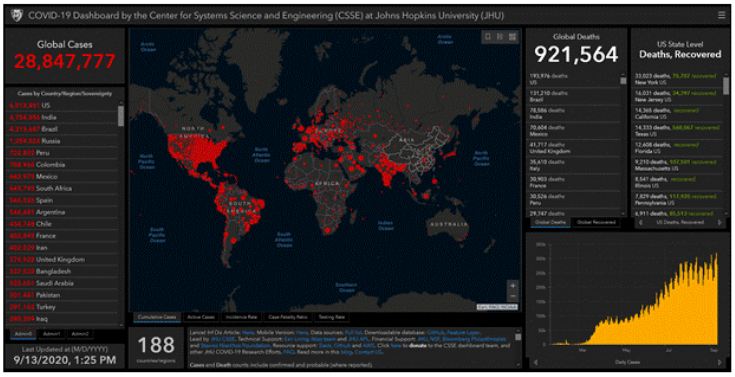
In most economies, the level of output at the end of 2021 is projected to remain below that at the end of 2019, and considerably weaker than projected prior to the pandemic, highlighting the risk of long-lasting costs from the pandemic.

If the threat from the coronavirus fades more quickly than expected, improved confidence could boost global activity significantly in 2021. However, a stronger resurgence of the virus, or more stringent containment measures, could cut 2-3 percentage points from global growth in 2021, with higher unemployment and a prolonged period of weak investment.

No doubt, developments on the COVID-19 front will be critical for the health of the economy,…

COVID-19 GLOBAL SPREAD





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

With access to testing remaining high, there was another jump of more than 2.0 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 200,000 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 dropped a bit from the 40,000 level of the last four weeks. No doubt, the approaching flu season will represent another health risk.

…while the Election and geopolitical events remain major wildcards, but we continue to find equities to be very attractive, especially from an income perspective,…

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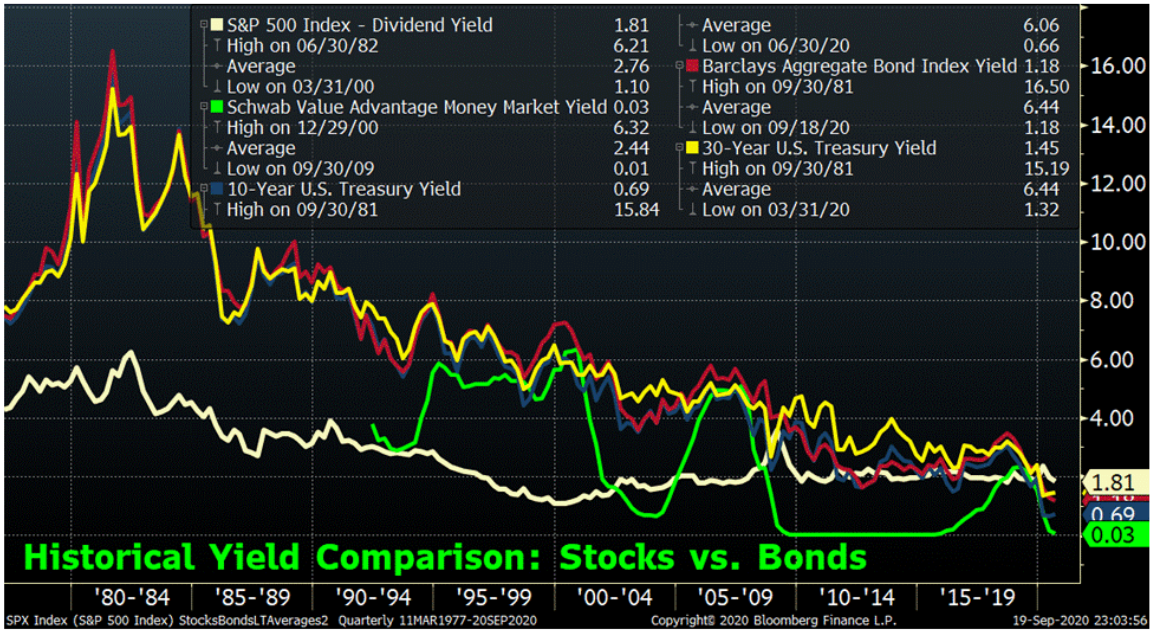
EQUITY VS. FIXED INCOME YIELDS

Though stocks are not necessarily a substitute for cash, government or corporate bonds, the payout on the S&P 500 (1.81%) 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**!

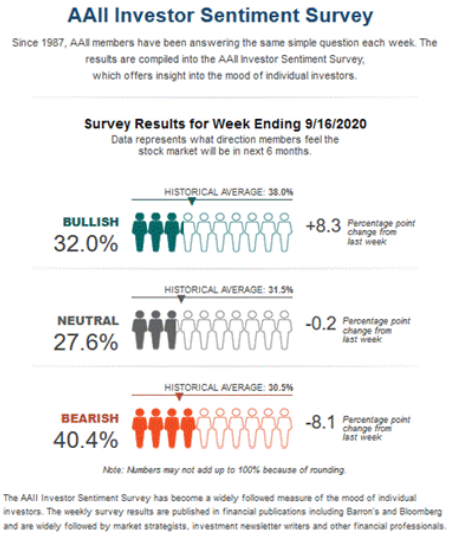


…and we remain perplexed by the lack of much investor interest in U.S. stocks.

SENTIMENT: LITTLE ENTHUSIASM FOR U.S. STOCKS

While folks on Main Street became much less pessimistic last week, they are hardly upbeat on stocks as the latest AAII Sentiment Survey saw the number of Bulls at 6.0 percentage points below normal and Bears at 9.9 points above average.

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	9/9/2020	9/2/2020	8/26/2020	8/19/2020	8/12/2020
Total Equity	-8,495	-28,307	-19,714	-15,105	-3,256
Domestic	-8,764	-18,047	-18,290	-15,776	-5,495
World	268	-10,260	-1,424	672	2,239
Hybrid	-926	-1,163	-624	-300	-577
Total Bond	13,419	24,543	20,037	17,834	20,153
Taxable	11,630	23,201	17,848	14,910	16,607
Municipal	1,788	1,342	2,190	2,924	3,545
Commodities	142	718	669	370	-97
Total	4,139	-4,209	368	2,799	16,222

Source: Investment Company Institute

That is not to say that there are no pockets of equity passion, as evidenced by the incredible demand for the latest technology stock initial public offering. Indeed, shares of cloud services provider Snowflake (SNOW) skyrocketed on Wednesday, opening for trading at $245, more than double the $120 IPO price, which itself was repeatedly ratcheted higher. True, Snowflake is a hot stock in a hot industry, with the offering documents stating, "We have achieved significant growth in recent periods. For the fiscal years ended January 31, 2019 and 2020, our revenue was $96.7 million and $264.7 million, respectively, representing year-over-year growth of 174%. For the six months ended July 31, 2019 and 2020, our revenue was $104.0 million and $242.0 million, respectively, representing year-over-year growth of 133%."

This sounds terrific, until one realizes that the stock now boasts market capitalization of $67 billion (with a "B"), and there are other restricted shares and options on the books that when issued might push the valuation up towards $90 billion. The IPO document continued, "Our net loss was $178.0 million and $348.5 million for the fiscal years ended January 31, 2019 and 2020, respectively, and $177.2 million and $171.3 million for the six months ended July 31, 2019 and 2020, respectively."

To be sure, the company might grow into its valuation one day as the cloud has tremendous potential, but Snowflake has a bevy of competitors and has not yet proved that it can make

money. That doesn't mean that SNOW will melt as many other hot IPOs have over the years, but the table below shows how Snowflake, sandwiched between railroad giant **Norfolk Southern** (NSC – $221.03) and trash hauler **Waste Management** (WM – $115.27), compares to other highly profitable and well-established companies that have already proven that their respective businesses are viable for the long term.

THE PRUDENT SPECULATOR

SNOWFLAKE VS. MORE WELL-KNOWN COMPANY VALUATION COMPARISONS

The year's hottest initial public offering arrived last week when shares of Snowflake priced well above initial expectations at $120 before opening for trading at $245, giving the Data Cloud software solutions provider a market capitalization and enterprise value on par with some of the largest (and far less expensive) companies in the U.S.

to Snowflake's Enterprise Value

Symbol	Common Stock	9.18.20 Price	Target Price	52-Week High	% Below High	52-Week Low	% Above Low	Sector	P/E	P/S	Enterprise Value	Div Yld	Mkt Cap
GILD	Gilead Sciences	$65.05	$91.93	$85.97	-24%	$60.89	7%	Pharmaceuticals, Biotechnol	11.1	3.7	84,582	4.2%	81,555
TGT	Target	$148.82	$161.67	$156.10	-5%	$90.17	65%	Retailing	21.2	0.9	83,756	1.8%	74,502
DE	Deere & Co	$221.97	$225.74	$225.38	-2%	$106.14	109%	Capital Goods	26.3	1.9	73,222	1.4%	69,560
WBA	Walgreens Boots Alliance	$36.93	$78.88	$64.50	-43%	$33.88	9%	Food & Staples Retailing	7.2	0.2	73,595	5.1%	32,001
NSC	Norfolk Southern	$221.03	$229.65	$224.99	-2%	$112.62	96%	Transportation	24.2	5.5	67,941	1.7%	56,387
SNOW	Snowflake	$240.00	nmf	$319.00	-25%	$215.24	12%	Software	nmf	164.8	67,432	0.0%	66,407
WM	Waste Management	$115.27	$127.85	$126.79	-9%	$85.34	35%	Commercial & Pro Srvcs	27.5	3.2	58,824	1.9%	48,697
GM	General Motors	$31.50	$45.35	$38.96	-19%	$14.33	120%	Autos & Components	16.7	0.4	55,418	0.0%	45,080
GD	General Dynamics	$142.99	$231.75	$190.08	-25%	$100.55	42%	Capital Goods	12.7	1.1	54,698	3.1%	41,028
MU	Micron Technology	$50.74	$66.00	$61.19	-17%	$31.13	63%	Semiconductors	22.0	2.8	54,515	0.0%	56,372
ETN	Eaton Corp PLC	$103.40	$108.12	$106.07	-3%	$56.42	83%	Capital Goods	21.7	2.2	49,509	2.8%	41,370
KR	Kroger Co	$33.21	$40.03	$37.22	-11%	$23.71	40%	Food & Staples Retailing	11.1	0.2	46,089	2.2%	25,835
BIIB	Biogen	$274.48	$428.37	$374.99	-27%	$219.70	25%	Pharmaceuticals, Biotech	7.4	3.0	46,023	0.0%	43,454
LRCX	Lam Research	$307.21	$402.31	$387.70	-21%	$181.38	69%	Semiconductors	19.3	4.5	44,022	1.7%	44,738
VIAC	ViacomCBS	$30.16	$59.29	$43.04	-30%	$10.10	199%	Media & Entertainment	7.0	0.8	39,001	3.2%	18,729
ZBH	Zimmer Biomet Holdings	$138.87	$168.12	$161.11	-14%	$74.37	87%	Health Care Equip/Srvcs	23.9	4.1	36,251	0.7%	28,753
ADM	Archer-Daniels-Midland	$47.64	$56.62	$48.56	-2%	$28.92	65%	Food, Beverage & Tobacco	12.9	0.4	35,629	3.0%	26,471
CMI	Cummins	$211.90	$219.81	$215.43	-2%	$101.03	110%	Capital Goods	18.2	1.5	34,442	2.5%	31,292
TSN	Tyson Foods	$62.03	$88.09	$94.24	-34%	$42.57	46%	Food, Beverage & Tobacco	12.3	0.5	33,946	2.7%	22,595
GLW	Corning	$32.44	$41.22	$33.86	-4%	$17.44	86%	Technology Hardware	24.0	2.3	33,437	2.7%	24,712
MCK	McKesson	$152.13	$197.59	$172.18	-12%	$112.60	35%	Health Care Equip/Srvcs	10.5	0.1	33,115	1.1%	24,674

We will pass on SNOW and other extraordinarily expensive names as we sleep much better at night with a broadly diversified portfolio of stocks that are reasonably priced and that nearly all pay dividends. Yes, we realize that chasing the latest hot trend can be exciting, but the historical evidence argues that owning established companies is the better way to go. After all, very few companies ever want to go public at a discount!

THE PRUDENT SPECULATOR

IPOS HAVE UNDERPERFORMED ESTABLISHED COMPANIES

Table 20-1
Percentage returns on IPOs from 1980-2018 during the first five years after issuing

	First six months	Second six months	First Year	Second year	Third year	Fourth year	Fifth Year	Geometric Mean years 1-5
IPO firms	6.5%	0.8%	7.6%	6.6%	12.1%	19.1%	10.3%	11.1%
Size-matched	5.4%	5.9%	11.7%	14.2%	15.0%	16.1%	12.6%	13.9%
Difference	1.1%	-5.1%	-4.1%	-7.6%	-2.9%	3.0%	-2.3%	-2.8%
IPO firms	6.5%	0.8%	7.6%	6.6%	12.1%	19.1%	10.3%	11.1%
Size & BM-Matched	3.9%	4.6%	8.8%	13.1%	12.0%	17.3%	12.4%	12.7%
Difference	2.6%	-3.8%	-1.2%	-6.5%	0.1%	2.0%	-2.1%	-1.6%
No. of IPOs	8,497	8,475	8,497	8,349	7,547	6,621	5,819	

All returns are equally weighted average returns for all IPOs that are traded on Nasdaq, the Amex (now NYSE MKT), or the NYSE at the start of a period. For the first and third columns, the returns are measured from the closing market price on the first day of CRSP-reported trading until the sixth-month or one-year anniversary. For years 2-5, each year the portfolios are rebalanced to equal weights. If an issuing firm is delisted within a year, its return for that year is calculated by compounding the CRSP value-weighted market index for the rest of the year. For the size-matched returns, each IPO is matched with the nonissuing firm having the same or next higher market capitalization (using the closing market price on the first day of trading for the IPO, and the market capitalization at the end of the previous month for the matching firms). For the size & BM-matched returns, each IPO with a book-to-market ratio higher than zero is matched with a nonissuing firm in the same size decile (using NYSE firms only for determining the decile breakpoints) having the closest book-to-market ratio. Each IPO with a zero or smaller book-to-market ratio is matched with a nonissuing firm of a book-to-market ratio of zero or smaller having the closest market capitalization. For the IPOs, book-to-market ratios are calculated using the first recorded post-issue book value and the post-issue market cap calculated using the closing market price on the first CRSP-listed day of trading. For nonissuing firms, the Compustat-listed book value of equity for the most recent fiscal year ending at least four months prior to the IPO date is used, along with the market cap at the close of trading at month-end prior to the month of the IPO with which it is matched. Nonissuing firms are those that have been listed on the Amex-Nasdaq-NYSE for at least five years, without issuing equity for cash during that time.

Per calculations from Jay R. Ritter, Joseph B. Cordell Eminent Scholar Chair, University of Florida, Warrington College of Business, IPOs have underperformed other firms of the same size (market cap) by an average of 2.8% per year during the five years after issuing, not including the first-day return. The underperformance relative to other firms of the same size and book-to-market ratio has averaged 1.6% per year. Returns are through Dec. 31, 2019. (updated March 10, 2020). https://site.warrington.ufl.edu/ritter/files/IPOs2019Statistics.pdf

Stock Updates

It was again a relatively quiet week for individual company news, but Jason Clark, Chris Quigley and Zach Tart look at eight 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/, while updated Target Prices, as of 9.15.20, were posted to the site last week. We also offer the reminder that any sales we make for our newsletter strategies are announced via our Sales Alerts.

Shares of **FedEx** (FDX – $242.78) gained 4% last week thanks to fiscal Q1 2021 results that again crushed analyst estimates on the top and bottom lines. The stock should have been up much more, in our view, as the package and freight delivery giant earned $4.87 per share (vs. $2.69 est.) and had revenue of $19.3 billion (vs. $17.6 billion est.). While the company didn't offer guidance (which it pulled on March 17), management said it expects global GDP growth and trade growth on a year-over-year basis to remain negative for this year. Despite having fallen from its peak percentage of overall package volume in April, e-commerce is expected to drive 96% of U.S. growth over the near term amid what CMO Brie Carere called a "ship-a-thon." FDX

shares have gained 60% this year, which is remarkable compared to the red ink spilled for the average stock.

“There are 2 trends that have had substantial impact on our industry and showcase FedEx’ incredible value proposition. The first key trend is the dramatic reduction of air cargo capacity as a result of the significant loss of commercial airline capacity. Current estimates indicate that freighter capacity now accounts for 66% of total air capacity on the trans-Atlantic lane, 83% on the trans-Pacific and 80% on the Europe to Asia lane. This compares to pre-COVID freighter capacity of 33% for trans-Atlantic, 59% for trans-Pacific and 50% for Europe to Asia. The second and perhaps more profound trend is the acceleration of e-commerce. Pre-COVID, we projected that the U.S. domestic market would hit 100 million packages per day by calendar year 2026. We now project that the U.S. domestic parcel market will hit this mark by calendar year 2023, pulling volume projections forward by 3 years from the previous expectation.” said COO Raj Subramaniam.

CFO Alan Graf added, “If our current trends continue, we expect certain expenses, including higher variable incentive compensation accruals and increased supplies and other costs related to the COVID-19 pandemic to remain headwinds in fiscal 2021. I’ll conclude by reemphasizing that we expect to continue to benefit from our strong position in the U.S. and international package and freight markets, yield improvement opportunities and cost management initiatives.”

FedEx has $7.0 billion of cash and $3.5 billion of available credit facilities, giving the company plenty of flexibility as the pandemic evolves. FDX issued $970 million of pass-through securities with a fixed interest rate below 2%, which are secured by 19 Boeing 767 and 777 aircraft. The transaction boosts liquidity and offers additional operational flexibility at a very low interest rate. FedEx also expects to incur $175 million of TNT integration expenses in fiscal 2021 with integration completion in 2022. Shipping continues to be a lifeline for many folks, especially as shippers prepare to move vast quantities of COVID-19 vaccines that almost certainly will require special handling to maintain temperature and thereby efficacy. We continue to like the strong balance sheet, modest dividend yield and position as an industry leader. FDX trades near 16 times forward earnings and the quarterly dividend payment of $0.65 puts the yield around 1.7%. Our Target Price has been increased to $286.

Shares of **MDC Holdings** (MDC – $46.17) rose more than 3% last week after the company released preliminary net new order activity for Q3 ahead of its upcoming appearance at the Zelman Virtual Housing Summit. Management said that for the first two months of Q3, net new home orders increased 75% year-over-year to 2,477, compared with 1,418 for the same period in 2019. The increase was driven by a 73% improvement in the monthly sales absorption rate to 6.48 and a 1% increase in the average number of active subdivisions to 191.

CEO Larry A. Mizel commented, “The sharp increase in demand for new homes has extended into the third quarter, and we are increasingly optimistic that the elevated level of activity is part of a larger trend for our industry. With historically low interest rates and COVID-19 concerns as a backdrop, consumers are showing a strong preference for suburban living, part of a demographic shift that we believe was taking place before the pandemic began. As we approach the close of the third quarter, we are well positioned to reach 8,000 home deliveries for the 2020

full year. Furthermore, we believe we have the lot supply and the right product type to drive significant growth in 2021, provided that market fundamentals remain favorable."

While COVID-19's full impact on the economy in general is still unknown, we believe that MDC is poised for long-term success. Interest rates are extraordinarily low and will most likely remain that way for at least the next few years, which should help MDC as the cost of borrowing for both it and its potential customers remains extremely attractive. MDC sports a broad geographic footprint, boasts successful cost control initiatives and maintains a solid balance sheet ($1.52 billion of liquidity at the end of Q2) that the company can draw from if it must remain in a defensive posture through the crisis or can use to smartly acquire land in attractive markets. Additionally, we like MDC's focus on first time buyers (many millennials) with its Seasons collection of homes. Despite the strong performance of the stock thus far in 2020, MDC's dividend yield is still 2.9%, well above that of the 10-year U.S. Treasury Note (0.69%), and shares are trading slightly above 8 times expected NTM adjusted EPS. Our Target Price for MDC has been boosted to $59.

Pharmaceutical concern **Gilead Sciences** (GILD – $65.05) formally entered an agreement last week to purchase the oncological biotech firm Immunomemdics for $21 billion, a whopping 108% premium to the prevailing market price prior to the announcement. With the purchase, Gilead gains Trodelvy, a drug indicated and approved to treat breast cancer but with potential for expansion into other forms of cancer.

"This acquisition represents significant progress in Gilead's work to build a strong and diverse oncology portfolio. Trodelvy is an approved, transformational medicine for a form of cancer that is particularly challenging to treat. We will now continue to explore its potential to treat many other types of cancer, both as a monotherapy and in combination with other treatments," said Gilead CEO Daniel O'Day. "We look forward to welcoming the talented Immunomedics team to Gilead so we can continue to advance this important new medicine for the benefit of patients with cancer worldwide."

While the acquisition will likely fit nicely in the firm's oncology portfolio, it was a very high price to pay, while we note that the 2017 purchase of Kite Pharma has yet to diminish Gilead's reliance on antiviral products. Still, given that GILD's HIV franchise continues to produce strong cash flow and high returns on capital, we are happy that the company has the wherewithal to make substantial investments to ensure that long-term growth resumes, all while buying back stock and paying out a hefty dividend. GILD shares trade under 10 times 2021 adjusted consensus EPS projections and the yield is 4.2%. Our Target Price for GILD has been trimmed to $92.

Shares of insurer **MetLife** (MET – $39.67) rose 3.8% last week after the insurance giant announced both an acquisition and the resumption of its stock buyback program.

MET said that it had entered into a definitive agreement to acquire Versant Health for approximately $1.675 billion in an all-cash transaction. Versant owns the well-established managed vision care and eye health plans via Davis Vision and Superior Vision. Following the acquisition, MetLife will gain access to Versant's roughly 35 million members, and MetLife's

existing customers will gain access to Versant's extensive provider network, which is one of the largest in the industry.

"This transaction furthers our goal of deploying capital to the highest-value opportunities," said CEO Michel Khalaf. "We are pleased to welcome Versant Health, a well-run and well-respected leader in vision care, to the MetLife family. In Versant, we have found the right strategic fit with our group benefits business. We expect this combination to accelerate revenue growth while delivering greater value for our customers and shareholders."

"We are confident this acquisition will make our market-leading group benefits business even more attractive," said Ramy Tadros, President of U.S. Business for MetLife. "The addition of the strong Davis Vision and Superior Vision brands will immediately establish MetLife as a leader in managed vision care. We look forward to offering our customers the exceptional member experiences that Versant provides."

Additionally, management announced that it planned to complete the remaining $485 million on the company's current stock buyback authorization. The $485 million represents about 1.3% of MetLife's current market capitalization, and the move was pleasantly surprising, given the financial sector's general COVID-19 caution.

It's no secret that fixed-income investors around the globe have suffered for some time due to paltry interest rates. This has pressured reinvestment yields for insurers, particularly for those bearing long-dated risks like life insurance. Still, we believe that MET has a solid financial foundation, and we like the exposure to a diverse product mix. The firm is well-positioned as the largest life insurer in North America as measured by "in-force" coverage, offering financial products and services to over 90 of the Fortune 100 companies. Substantial international operations should continue to be a core driver of growth going forward. Equally important, shares change hands at less than 7 times expected NTM adjusted EPS and for less than 51% of book value, while the dividend yield is 4.6%. Our Target Price for MET has been boosted to $73.

Global banking concern **Citigroup** (C – $44.86) continued to make headlines last week, this time related to its internal controls and risk systems. These come on the back of its recent debacle with lenders to Revlon, where the firm mistakenly doled out $900 million worth of funds. Shares were been punished over 13% by the week's close as CFO Mark Mason discussed at a recent Barclays Global Financial Services conference plans to invest an incremental $1 billion into strengthening existing risk management and governance controls. Said spend is accelerated amid reports that regulators will reprimand the bank for failing to move quickly enough to make the necessary investments.

Mr. Mason also mentioned that reserve builds would likely continue in Q3 financial results, but at a much lower rate than earlier quarters this year. Citi has built quite the reserve cookie jar that now stands at $28 billion (3.9% of funded loans), which we expect to unwind to the benefit of earnings in future years as global economies gradually improve.

While there is obviously much more work to be done, the transformation journey Citi has endured ever since the Great Financial Crisis has made it a much more sound financial

enterprise. As we mentioned last week, new CEO Jane Fraser offers a fresh look for the firm, as it has come up short in meeting its own financial targets over the past decade and has the lowest return on equity of major U.S. banks. We continue to think there is a lot to like overall as ongoing restructuring, amplified capital return programs and technological investment all appear to work in our favor in the coming years. After the tough week, shares are even cheaper today, trading at about half of book value. The dividend yield is 4.5% and our Target Price is now $89.

Shares of **Fifth Third Bancorp** (FITB – $21.74) finished the week where they started as the regional bank also presented at the Barclays Conference last week. The company highlighted a new expense management program, where it continues to rationalize its branch footprint and quicken its digital transformation. CEO Greg Carmichael commented, "The recent acceleration in customer digital adoption trends raises the returns on our technology investments made over the past several years." Management was also upbeat in its reserve expectations for the remainder of the year, discounting the possibility for further builds.

We continue to like the competitive market position Fifth Third holds in its midwestern and southeastern markets. And, we emphasize that the bank is in a much better place in the current income recession, imposed by COVID-19, than it was in the balance sheet recession that was the Great Financial Crisis. While the future is still very uncertain, particularly as we enter the winter months, shares trade at an attractive 11.4 times expected 2021 earnings and for 0.75 times book value. The dividend yield is 5.0% and we've bumped our Target Price to $35.

The political theater surrounding TikTok, an app that has been wildly popular with young people and sparked national security concerns due to Chinese ownership, came to a head this weekend. On Saturday, President Trump gave his "blessing" to **Oracle** (ORCL – $59.75) and **Walmart** (WMT – $135.29) in regard to a deal for TikTok's U.S. operations. The move averts a looming shutdown of TikTok in the U.S., even as Oracle is said to be taking just a 12.5% stake and Walmart a 7.5% stake in the new company to be known as TikTok Global. Given that U.S. venture capital and private equity firms own a big stake in TikTok's Chinese parent ByteDance Ltd, the transaction evidently will satisfy Washington's demand for majority U.S. ownership in TikTok Global.

For its part, Oracle is excited to be chosen to become TikTok's secure cloud technology provider. "TikTok picked Oracle's new Generation 2 Cloud infrastructure because it's much faster, more reliable, and more secure than the first generation technology currently offered by all the other major cloud providers," said Oracle CTO Larry Ellison. "In the 2020 Industry CloudPath survey that IDC recently released where it surveyed 935 Infrastructure as a Service (IaaS) customers on their satisfaction with the top IaaS vendors including Oracle, Amazon Web Services, Microsoft, IBM and Google Cloud …. Oracle IaaS received the highest satisfaction score."

Oracle CEO Safra Catz explained, "As a part of this agreement, TikTok will run on the Oracle Cloud and Oracle will become a minority investor in TikTok Global. Oracle will quickly deploy, rapidly scale, and operate TikTok systems in the Oracle Cloud. We are a hundred percent confident in our ability to deliver a highly secure environment to TikTok and ensure data privacy to TikTok's American users, and users throughout the world. This greatly improved security and

guaranteed privacy will enable the continued rapid growth of the TikTok user community to benefit all stakeholders."

Walmart commented, "We are excited about our potential investment in and commercial agreements with TikTok Global. While there is still work to do on final agreements, we have tentatively agreed to purchase 7.5% of TikTok Global as well as enter into commercial agreements to provide our ecommerce, fulfillment, payments and other omnichannel services to TikTok Global. Our CEO, Doug McMillon, would also serve as one of five board members of the newly created company."

While there are many details still left to be worked out, and the whole thing could still fall apart, we generally look favorably on both Oracle's and Walmart's involvement. As we learn more, we may have further Target Price adjustments, but for now, we are working with $69 for ORCL and $154 for WMT.